



## CAN CHITFUND COMPANIES REALLY MEETING THE REQUIREMENTS OF LOWER INCOME GROUPS? A STUDY IN ANDHRA PRADESH.

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### **Abstract**

*Chit funds emerged as self-help credit societies even before the modern banking and credit facilities are evolved in the country. Chit funds cater the specific needs of the people in a more efficient manner in both in urban and rural areas. The comparative advantage that the institution of chit funds offers is that planning in advance. The sum total of this small chit may, at a specified time, solve the need for a larger, one-time requirement. Chit schemes are organized on a personal basis and have lesser stringencies involved. Decision making is comparatively faster. The income from chit schemes compares favorably with the incomes from bank schemes in many cases. Chit-funds are mainly popular due to the number of middle class and poor people in the country find it as an innovative way to access finance, as they require less collateral and documentation. The amount is collected from the participants at their doorstep on a flexible when the participants are able to pay. The present paper deals with the issues of how chit funds help the lower income groups without any burden on their shoulders and help them to meet their urgent requirements all the time better than any other financial organisation.*

**Key Words:** *Self Help Credit, Indigenous Sources, Contingencies, Stringencies, Collateral, and Comparative Advantage.*

### **Introduction**

An Indian concept, In the villages of Kerala , many years ago, a small group of farmers operated a unique scheme. Each farmer gave a fixed quantity of grains periodically to a selected trustee. The Trustee, after keeping aside a portion for himself and gives the rest to a member of the group to help him to meet his social commitments and other needs. The farmer who received the lot continued to give the fixed quantity till every member of the group received his lot. The additional benefits when receiving the lot earlier led to competition. Some members were even willing to forgo a certain portion (like a discount) of the lot, in order to get an earlier chance. So, an auction was held and the lowest bidder got the lot. This was the basis of what we know today as the “chit fund scheme”.

Chit fund is a typical indigenous financial institution peculiar to South India, particularly in Andhra Pradesh, Tamil Nadu and Kerala. They are called with different names in these states. Chit funds emerged as self-help credit societies even before the modern banking and credit facilities evolved. These organisations are meeting the genuine credit needs of the people of all segments of the society. .

A chit fund is based on mutual trust and confidence. It has a limited number of members preferably known to one another, for a limited period and with limited liability. The membership is voluntary. People join a chit fund either to obtain easy credit or to find an avenue for the investment of their savings. The main attraction is the availability of a lump sum either for expenditure or for saving. The expenditure may be mostly consumption expenditure, especially on consumer durables or for such purposes as marriages, religious ceremonies or to pay off an old debt and also for acquiring a house or plot of land. Thus, chit fund has become a mode of saving and a source of credit. Unlike the other



financial intermediaries, chit fund acts as an intermediary between borrowers and lenders through pooled connects the borrowing class directly with the lending class and the pooled saving is lent out to the same group of savers.

### **Organisation of chit funds**

Chit funds organized professionally by individuals or institutions, like a firm or company are in the nature of financial intermediaries. Financial intermediaries gather the savings of the people and distribute the funds to numerous borrowers, thus affecting the allocation of real resources. An effective system of intermediation helps economic development by competing for funds of savers, thus offering a rate of return to them higher than would otherwise be possible and making funds available to borrowers at costs lower than would otherwise prevail. The intermediation involved in chit fund is that the promoter of chit fund mobilizes the savings of one group of people and passes them on by turn to the same group of people, who may utilize them either for consumption or investment purposes. In so far as chit funds have no control over the end end-use of the funds, it is better to consider chit funds as a co-operative endeavor.

The two factors, namely, accessibility and relatively easy availability of credit, rather than the cost of such credit seem to explain mainly, the popularity of chit funds. Notwithstanding to the spectacular growth of banking offices since nationalization and the increase in the flow of credit to the neglected and priority sectors, chit funds have recorded substantial growth in number and volume of business.

Chit fund are the Indian equivalent of the Rotating Saving and Credit Associations (ROSCA) that are famous throughout the world. ROSCAS are informal financial institutions which are found all over the world<sup>1</sup>. They are most common in developing countries but are also used by immigrant groups in the United States. The total fund is distributed to each of the members in rotation until everyone has had a turn. Hence, only one loan is made each time the members convene. Over time, some members may take more than one loan, others may never need to borrow from the fund and use their society merely as a savings club. Both types of societies are common in developing countries, but it is the rotating savings and credit association which is more popular and is popularly known as ROSCA. The ROSCA in India is commonly known as chit fund or chitty. Its origin antedates the establishment of modern banking. Originally, contributions were in kind, paddy or rice. This made chitty very popular among the housewives who saved small quantity of rice from each daily meal to contribute to their rice bank.

### **Objectives of the study**

1. To study the influence of socio economic factors in opting chit funds.
2. To highlight the role and significance of chitfunds.
3. To analyse how chit funds are acting as an effective instrument of finance for low income households.

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<sup>1</sup> ROSCAs travel under many different names; chit funds in India, susu in Ghana, tontines in Senegal, njangis in Cameroon, cheetu in Srilanka, and pasanakus in Bolivia are just a few examples.



## Methodology

The study is based on the descriptive research by using the primary and secondary data. The sampling procedure adopted is non-probability sampling and the type of sampling followed is convenience sampling. The main research tool used is questionnaire and also interviews were conducted to record the experiences of chit managerial staff.

The study is based on primary and secondary data. The data pertaining to measure various parameters for examining the performance of Chit fund companies is collected from the published and unpublished reports. The **primary data** is collected through subscriber survey method. Personal interview method is also used to collect the data from chit subscribers. The sample size of the chit subscribers is 1220 of which 782 are from 12 registered chit fund company subscribers and 438 are from 6 unregistered chit fund company subscribers/members, selected through random sampling from different regions of the state according to the population density of the regions. Totally, a sample of 540 is collected from Telangana region, 615 from Coastal Andhra and 65 from Rayalaseema regions. The **Secondary data** is collected from various published books, journals, magazines, newspapers, websites and past records from various Governments, Private organizations involved in chit operations as well as regulations and from RBI reports, Report on Trend and Progress of Banking in India, RBI Bulletins also form part of the secondary data.

## Tools and Techniques of Analysis

For the purpose of analysis and to facilitate interpretation, simple statistical tools like percentages, averages, simple growth rate, and Pearson coefficient of correlation are used. Comparative tables with the select constructs using certain demographic variables were prepared.

Advanced Statistical tools such as Chi Square test, Standard deviation; ANOVA and Freidman's Mean Rank are used for testing the hypothesis.

## Literature Review

**Dr. C.P.S. Nayar (1973)** ,His study emphasized regulation of chit funds, their role and impoirtance in all aspects. He attempted to define chit funds with more clarity and addressed the economic implications of chit funds..

**S. Radhakrishnan (1975)** Viewed that chit funds deserve more attention and reforms. They should be credit rated and grow on sound lines.

**F.J.A.Bouman (1995)**The ancient Indian "Chit fund",, originally consisted of grain-contributions and only later changed into a monetary "Chitty". In Japan, ROSCA- had origin from 1275 . In Korea, the "kye" (Korean ROSCA) may even go back to the 9<sup>th</sup> century. In Africa, ROSCA (called as "esusu" ) appeared in the economy somewhere around the mid 19<sup>th</sup> century. ROSCA originated in Europe about 1653.

**Bala Subramanian V(2002)** opined that more amendments are required in the Central Chit Fund Act.

**Anyango, E.(2002)** described the Village Savings and Loan Associations (VSLA) accumulating savings and credit associations (ASCA) as action audit.



**Preethi Rao(2007)** described chit funds as an excellent source of finance and replacement to moneylenders. these are low cost and easily accessible credit organisations.

The study of **Abhijit V. Banerjee and Esther Duflo(2007)** infer that chitfunds are lending sources to poor who save very little and find difficulty to get loans from banks and other formal sources.

**Antoinette Scholar opined** that people prefer chit funds to banks as the effective interest rates are comparatively less.

**Arjun sengupta, K.P.Kannan, G.Raveendran(2008)** mentioned that the poor and vulnerable people in India are known as common people, and the inequality is widening between the common people and the better-off sections of society.

**Prof. Mudit Kapoor(2009)**Opined strongly that chit funds being an important source of finance to common people and small businesses, should not be away from operating low value schemes. The strict rules imposed by government and increased operational costs are the main problems of chit fund companies.

In her article **Namrata Acharya(2010)**mentioned, that chit fund companies become big in size and value. The very purpose of the organisations deteriorating with the mushroom growth of unregistered chit funds.

## Data Analysis

### Age group Vs chit preference

Table 6.1 presents the Age Profile of the chit fund subscribers and the preference of the chit funds. As it can be seen from the table, the participation of subscribers below 25 years age group in chit funds (both registered and unregistered chit funds) is 7.5 per cent and it is 43.75 per cent. When it comes to the age group between 25 to 40 years,. The third segment i.e., the age group between 40 to 50 years participation is nearly 32.6 per cent which is about 16.03per cent in the age group of 50 to 60 years and the trend continues 0.02 per cent 0in the age group of above 60 years. It is pertinent to mention that, out of 1220 respondents the age group 25-40years consists of 525 participants in chit industry. It clearly shows that, 25 to 40 years age group participants are more attracted or inclined towards the chit industry rather than any other age group.

From the analysis, it is observed that the chit subscribers at the higher levels of age prefer the registered chit funds as against the unregistered. It is vice-versa in the case of the chit members at the lower age profile. This helps to surmise that the experience track of the chit members and their maturity levels associated with the age profile do bear an influence in the preference of the type of the chit fund companies-registered and unregistered.

### Hypothesis H<sub>0</sub>: Age of the subscriber will not have any influence on preferring chits.

Chi-Square value at 0.05 level of significance and degree of freedom 4 is 9.488. Since the calculated value of chi square (7.95) as evident from the table 6.1 is less than the table value of chi square (9.488), the Hypothesis H<sub>0</sub>, Age of the subscriber will not have any influence on preferring chits, is accepted. The difference between age group and the preference of chits is not significant. It is also observed from the standard deviation values in the table which are ranging from 0.368 to 0.503, as the age group of the



respondents increasing, they show higher stability in preferring chit funds. While the young age group i.e. below 25 years subscribers have less stability in preferring chit funds.

**Gender base Vs Preference of Chits**

Table 6.1 presents the gender base of the chit fund subscribers and the preference of the type of chit fund units. As it is evident from the table, Nearly 71.75 per cent of male preferring chit funds and nearly 28.25 per cent of female preferring chit funds and Men prefer chit funds more than women and it clearly shows that the male are more inclined to chit funds.

**Hypothesis H<sub>0</sub>: Gender and the preference of chit funds are independent.**

Chi-Square value at 0.05 level of significance and degree of freedom 1 is 3.841. Since the calculated value of chi square (33.376) as evident from the table 6.1 is greater than the table value of chi square (3.841) helps to conclude that the Hypothesis H<sub>0</sub>: Gender and the preference of chit funds are independent, is rejected. The difference between the gender and the preference of chit funds is significant. Hence it is concluded that the Gender has influence on preferring the chit funds. In other words, Preference of chit funds is dependent on gender. And it is also been observed from the results of standard deviation values in the table which ranges from 0.462 to 0.500 that, Male have (S.D,0.462) higher uniformity in preferring chits funds, whereas female have (S.D,0.500) less uniformity in their preference.

**Marital status Vs Type of Chit preferred**

From the Table 6.1, it is evident that, both married and unmarried respondents preferring the registered companies to unregistered firms. But Married respondents prefer registered chit companies more than unmarried respondents. Whereas unmarried respondents preferring unregistered firms more than married category. There is much variation in preferring registered and unregistered firms in unmarried category.

**Hypothesis H<sub>0</sub>: marital status has no influence on preference of chit funds.**

Chi-Square value at 0.05 level of significance and degree of freedom 1 is 3.841. Since the calculated value of chi square (6.471) as evident from the table 6.1 is greater than the table value of chi square (3.841) Hypothesis H<sub>0</sub>: marital status has no influence on preference of chit funds, is rejected. The difference between the parameters i.e., Marital status and the preference of chit funds is significant. Hence it is concluded that the Marital status has influence on the preferring the chit funds. Married respondents are more inclined towards chit funds (91.4 per cent) whereas unmarried respondents do not show much interest in investing chit funds (8.6 per cent). The Standard deviation values ranging from 0.476 to 0.501 in the table revealed that, married respondents are more stable in investing in chit funds. Unmarried investors are not much stable in investing in chit funds.

**Table 6.1 ,Demographic Factors**

(Figures in No's)

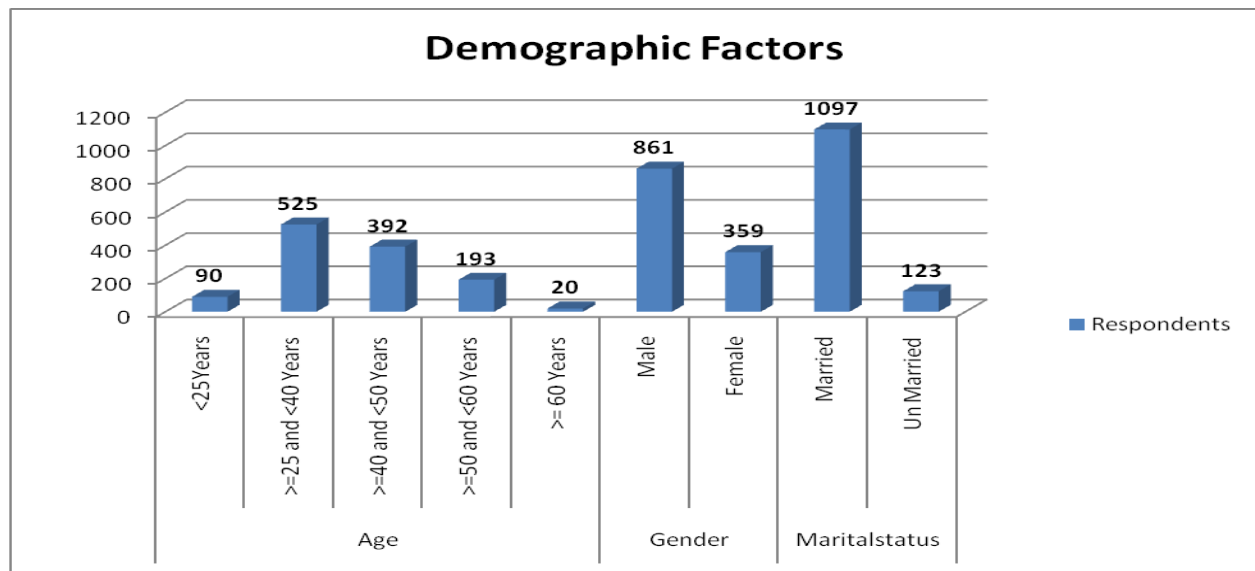
	Type of Chit		Total	Mean	Std. Dev	Test Values
	Registered	Un Registered				
<b>Age</b>						
<25Years	44(48.9)	46(51.1)	90(100.0)	1.51	0.503	Chi-Square =7.95
>=25 and <40 Years	331(63.0)	194(37.0)	525(100.0)	1.37	0.483	





>=40 and <50 Years	230(58.7)	162(41.3)	392(100.0)	1.41	0.493	Correlation =-0.144
>=50 and <60 Years	162(83.9)	31(16.1)	193(100.0)	1.16	0.368	
>= 60 Years	15(75.0)	5(25.0)	20(100.0)	1.25	0.444	
<b>Gender</b>						
Male	596(69.22)	265(30.78)	861(100)	1.31	0.462	Chi-Square =33.376
Female	186(51.81)	173(48.19)	359(100)	1.48	0.500	
<b>Marital status</b>						
Married	716(65.27)	381(34.73)	1097(100)	1.35	0.476	Chi-Square =6.479
Un Married	66(53.66)	57(46.34)	123(100)	1.46	0.501	

Source: Survey



### Income Vs Type of Chit preferred

Table-6.2 reveals that, the overall respondents are divided into five income groups it can otherwise read as lower, lower-middle, middle, upper-middle and upper income group segments and respondents from the middle, lower middle and lower income group segments are participating more in numbers in the chits rather than the other income groups. The participation of income groups in chit funds below ₹.10000 are 22.13 per cent and ₹.10000 to <₹.20000 are 37.79 per cent and ₹.20000 to <₹.30000 are 23.77 per cent. Maximum participants of the chit funds belong to the income group less than ₹.10000 to ₹.30000 (83.69 per cent) and only 13.36 per cent of the participants belong to the income group ₹.30000 to ₹.50000 and 2.95 per cent above ₹.50000. So it is concluded that maximum of the subscribers belong to middle and lower income groups.

### Hypothesis $H_0$ : income range and preference of chit funds are independent.

Chi-Square value at 0.05 level of significance and degree of freedom 4 is 9.488. Since the calculated value of chi square (30.118) as evident from the table 6.1 is greater than the table value of chi square (9.488). Hypothesis  $H_0$ : income range and preference of chit funds are independent, is rejected. The difference between income range and the preference of chit funds is significant. Hence it is concluded



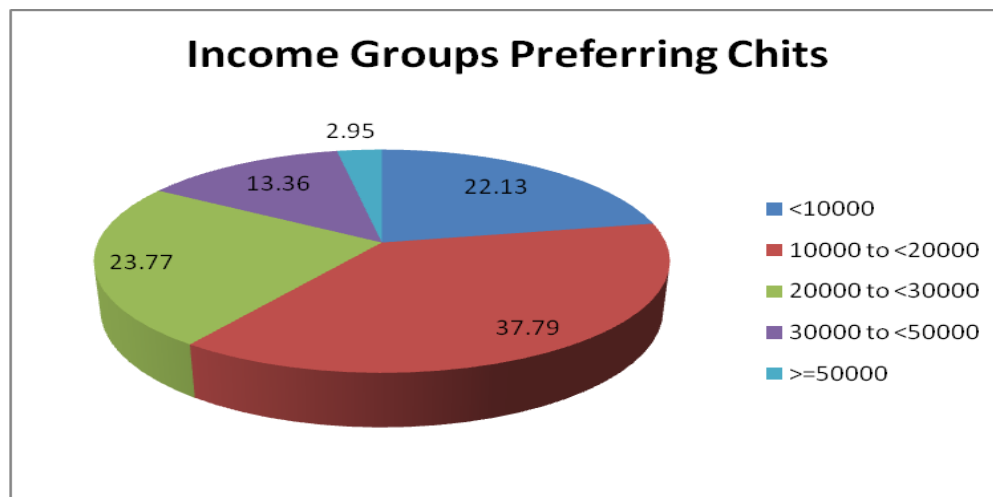
that the preference of chit funds is dependent on income level. The values of standard deviations in the table 6.2 which range from 0.232 to 0.499 shows there is high degree of uniformity in the income group above ₹50000 in preferring chit funds and choosing type of the company. While in low income group, the uniformity of preference is less.

**Table 6.2, Economic Factors**

(Figures in No's)

(Income in `)	Type of Chit		Total	Mean	Std. Dev	Test Values
	Registered	Un Registered				
<10000	148(54.81)	122(45.19)	270(100)	1.45	0.499	Chi-Square =30.118
10000 to <20000	288(62.47)	173(37.53)	461(100)	1.38	0.485	
20000 to <30000	196(67.59)	94(32.41)	290(100)	1.32	0.469	
30000 to <50000	116(71.17)	47(28.83)	163(100)	1.29	0.454	
>=50000	34(94.44)	2(5.56)	36(100)	1.06	0.232	

Source: Survey

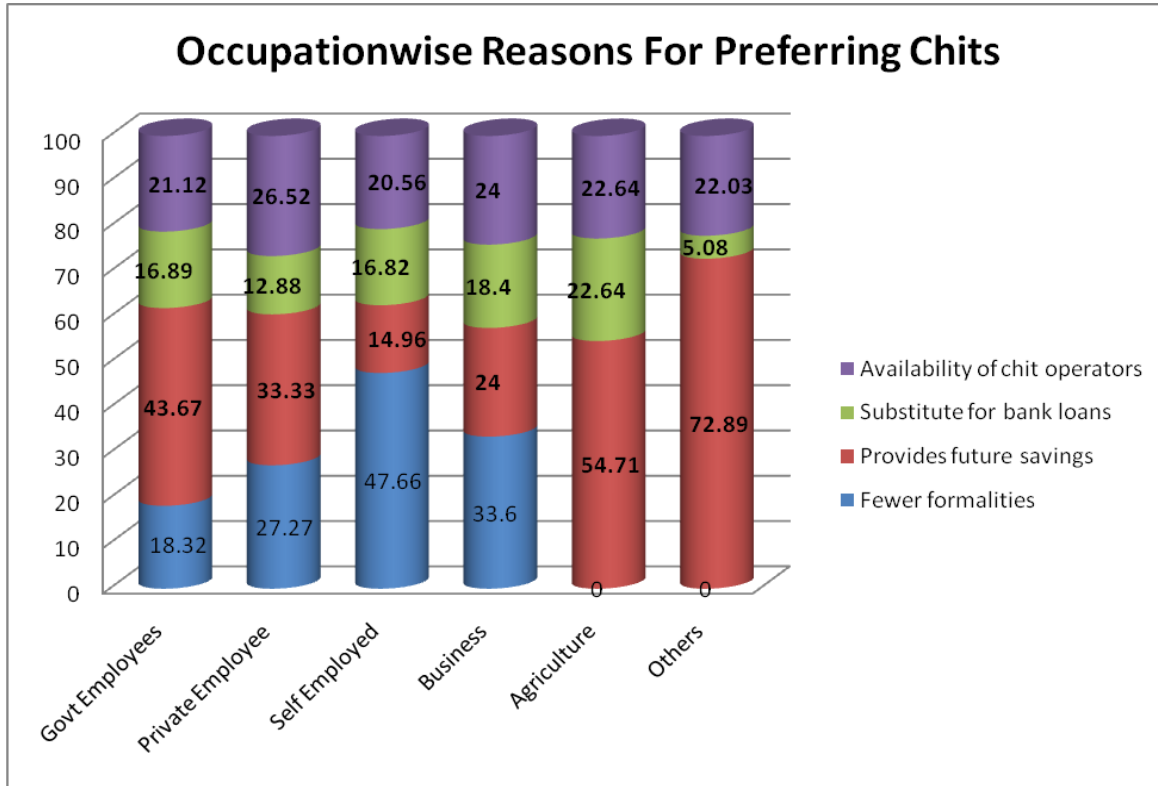


**Occupation wise Preference of chit funds - Cross Tabulation**

(Figures in percentages)

Reasons	Govt Employees	Private Employee	Self Employed	Business	Agriculture	Others
Fewer formalities	18.32	27.27	47.66	33.6	0	0
Provides future savings	43.67	33.33	14.96	24	54.71	72.89
Substitute for bank loans	16.89	12.88	16.82	18.4	22.64	5.08
Availability of chit operators	21.12	26.52	20.56	24	22.64	22.03
Total	100	100	100	100	99.99	100

Source: Survey



### Occupation wise Preference

From the Table-6.4 it is observed Government salaried (43.67 per cent of them) and private salaried respondents (33.33 per cent) prefer chit funds for future saving, where as self employed (47.66per cent) and business people (33.6 per cent) prefer chit funds because fewer formalities are involved. Agriculture respondents (54.71 per cent) and all other occupational respondents (72.89 per cent) also prefer for future savings.

### **Hypothesis H<sub>0</sub>: occupations do not differ significantly for various reasons of preferring chit funds.**

Chi-Square value at 0.05 level of significance and degree of freedom 30 is 43.773. Since the calculated value of chi square (2.991) as evident from the table 6.4 is lesser than the table value of chi square (43.773). Hypothesis H<sub>0</sub>: occupations do not differ significantly for various reasons of preferring chit funds, is accepted. The difference between the occupational background of the respondent and their reasons for preferring chits is not significant. Hence it is concluded that the all the given reasons are effective in preferring chit funds by various occupations. No particular occupation prefers particularly for a purpose. They prefer for all the given purposes time to time. Some times for saving, and the other time for liquidity needs and so on. It is also observed that, dual feature (both saving and investment) of chit funds and liquidity feature are mostly attracting features by all the occupations. The purpose of saving in chit funds by government employees and business class is saving, while private salaried and agriculturists prefer chit funds as it gives better liquidity. There exists negative correlation (-0.048) among the occupations in preferring chit funds for various reasons.





**Table-6.7, Purpose of Investing in Chit funds**  
(Figures in No's)

	Total	Friedmans Mean Rank	Std. Deviation
Conduct & expand business	93(100) (7.62)	1.00	0.000
To buy consumer durables	83(100) (6.8)	1.00	0.000
To buy or build house	150(100) (12.3)	1.00	0.000
For children education	156(100) (12.79)	1.03	0.159
Saving for the old age	82(100) (6.72)	1.10	0.299
Marriage	96(100) (7.87)	1.40	0.492
Agriculture purpose	63(100) (5.16)	1.95	0.215
To pay-off old debts	96(100) (7.87)	1.26	0.441
To buy gold or ornaments	42(100) (3.44)	1.00	0.000
For medical expenses			
To lend to others/invest	54(100) (4.43)	2.00	0.000
Contingent liabilities.	206(100) (16.89)	1.86	0.344
Total	1220(100) (100)	1.36	0.480
<b>Pearson Chi-Square</b>	<b>7.868</b>		
<b>Pearson's R[correlation]</b>	<b>0.689</b>		

Note 1. Figures in side brackets indicate percentage to Row Total.

2. Figures in lower brackets indicate percentage to Column Total.

Source: Survey

### **Purpose of Investing in chit funds by classification of chit companies**

It is observed from the table 6.7 that the subscribers invest in chits due to contingent liabilities are 206(16.89%), Children Education purpose 156(12.79%), for construction of house 150(12.3%), for medical expenses 99(8.11%), for marriage of self and other family members and to pay off old debts is 96(7.87% each), conduct and expand business 93(7.62%), for consumer durables 83(6.8%), for old age requirements 82(6.72%), they are less than 5 percentage of subscribers are invested for the purposes of



investment(4.43%) and for buying gold ornaments(3.44%).Among the registered subscribers the investment made for children education 152(19.44%), for construction of house 150(19.18%), for conducting and expanding business 93(11.89%), for consumer durables 83(10.61%), for old age requirements 74(9.46%), and to pay off debts 71(73.96%) put together 623(79.66%). This gives a clear picture that most of the registered chit subscribers are finding it safe hence they are investing for fulfilling their personal responsibilities. Respondents prefer unregistered firms for entirely different purposes. They prefer unregistered for in the first place, to meet contingent liabilities secondly, to meet medical expenses and agriculture purpose and it is also the performing purposes and marriages.

**Hypothesis  $H_0$ : purpose of saving in chit fund and the type of chit Fund Company are independent.** Chi-Square value at 0.05 level of significance and degree of freedom 11 is 19.675. Since the calculated value of chi square (7.868) as evident from the table 6.7 is lesser than the table value of chi square (19.675). Hypothesis  $H_0$ : purpose of saving in chit fund and the type of chit Fund Company are independent, is accepted. The difference between the two is not significant. Hence it is concluded that purpose of saving and Type of Chit are independent. There is no association between purpose of saving and type of company. The results of standard deviation values ranging from 0.000 to 0.480 also prove that, respondents preferring registered and unregistered firms for entirely different purposes. There exists positive correlation (0.689) between the registered and unregistered chit fund firms as the purpose of saving in the firm is concerned.

## Summary

- Chit fund is a typical indigenous financial institution. As a non-banking financial intermediary, it has been serving the needs of the community for many decades now. Even after the tremendous expansion of banking and credit facilities in the country, chit funds are growing in size and value. A chit fund is organized by a small group of people well-known to each other, who agrees to contribute periodically a certain amount of grain or money and to distribute the entire collection (fund), or a part of it, to one of the subscribers on some mutually agreed basis. The chit fund is regarded more than a savings bank to the saver and more than a lender to the debtor. The main aim of the paper is to enquire into the operation and intricacies and challenges of Chit funds.
- Today chit fund in India is highly institutionalised and stand in the status of a financial industry. No doubt the chit fund industry consists of both registered and unregistered chit funds. The money circulated in the registered chit fund industry ranges from 10-50 percent of the bank finance. But, the number of chit fund schemes registered has been on the trend of decline over the years ending 2010. The rate of reduction in the number of chit fund schemes, registered between 2005 and 2010 are around 12 to 15 percent.
- As the age group of the people increasing, they show higher stability in preferring chit funds. While the young age group i.e. below 25 years subscribers have less stability in preferring chit funds. Male are more inclined to participate in chit funds than female.
- Maximum participants of the chit funds belong to the income group less than ₹10000 to ₹30000. So it is concluded that maximum of the subscribers belong to middle and lower income groups. The major participants in the registered chits are Business, private and Government salaried respondents, they account for more than 60 per cent. The business class and private salaried class are participating more than 50 per cent in chits (in both forms). The most of the subscribers in chit funds are participating for saving as well as investment. Among the



occupations, the share of participation of business and self employed is Next it is salaried respondents (both government and private)

### **Suggestions**

Chit funds help the people not only to overcome their financial constraints but also acts as a profitable avenue of investment helping to earn good returns. Chit funds if properly used, serve as effective tools to meet the unplanned, unforeseen and unexpected expenses with ease. Therefore chit funds should be encouraged among the rural as well as urban as a spring boat for enterprising and also empowerment.

An attractive feature of the chit funds is that it is a unique instrument which has both saving as well as borrowing in one scheme. Moreover chit funds are the only financial institutions which are working more on mutual co-operation and self-help rather than profit making of a single individual. Chit funds act as banks in some aspect like accepting subscriptions and disbursement of credit. It is estimated that chit funds offer parallel banking services Chit funds are not incorporated under companies Act, and they should not be allowed to accept public deposits. The regulation of chit funds does not come under the purview of Reserve Bank of India. So State governments should take active part in regulating these chit funds under special legislation and implement the strict rules and regulations on public deposits and interest rates. If properly regulated by the State governments, these institutions can better serve the low and the middle income groups.

Keeping the credit needs of the low income people, government should take an effective action or pass a rule to protect the interests of the poor and safeguard their money. The government should provide the required facilities in the form of subsidy to the chit fund industry to conduct small value chits and encourage the chit fund industry which is so far working independently without government support.

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