

# INFORMAL CREDIT AND SAVINGS ORGANISATIONS IN RURAL SRI LANKA: THE CHEETU SYSTEM

Edgar Fernando

*In this paper which discusses informal savings and credit arrangements at the grassroots level in Sri Lanka, Edgar Fernando, Director, Department of Credit Councils focusses on the Cheetu System.*

The rural credit system in Sri Lanka encompasses, within a broad spectrum both the institutionalised banking sector like the People's Bank and the Bank of Ceylon as well as informal loan transactions from friends and relatives and professional and non-professional money lenders like landlords, boutique keepers and produce buyers. By far the most important of these informal credit transactions among villagers is the Cheetu system. It is an indigenous savings and credit scheme that contributes greatly to social cohesion among members of the rural community. Increasingly in the recent past, the attention of banking officials, social scientists, research scholars and international aid agencies operating in Sri Lanka have focussed attention on the existence of these informal savings and credit societies operating at the grassroots level.

Essentially, the Cheetu system is a rotating credit association in which a group of participants make regular contributions to a fund which is given as a lump sum to each member in turn. It is a system of group credit where borrowing and loan repayment are made the responsibility first and foremost of the organiser, and next, of the entire group to ensure conformity on the part of the borrower.<sup>(1)</sup>

## Nature and Characteristics of the Cheetu System

Cheetu organizations or clubs that function in the village of Sri Lanka are of two kinds: Cheetu by drawing lots, and the system of auction Cheetus.

In Cheetus organised by drawing lots, each participant is entitled to receive the same amount of money as contributed by the participants over a given period of time. Contributions are made once a month; it means therefore that at the end of each month, one participant gets a lump sum of money. Normally, the number of participants in this type of Cheetu is eight or ten persons.

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(1) Indigenous savings and credit societies are a worldwide phenomenon. They are found in many parts of Africa, South America, the Caribbean, the Middle East and in most of east and south Asia. The Cheetu system in Sri Lanka is of Indian origin, and the pervasive influence of the practices and customs of the sub-continent had their bearings on the Cheetu as practised in Sri Lanka. Especially in Travancore, India, it had found popular acceptance, and it was one of the principal means whereby people borrowed and tried to save money. The Cheetu system in Sri Lanka, based on the Indian model, is practised extensively by the Indian community resident in England eg. Southall and West Croydon. For a comprehensive study of these societies in the countries of the Third World, see the Paper presented by Professor F.J.A. Bouman of the Agricultural University of Wageningen, Netherlands, at the Conference on Rural Finance Research, sponsored by the Agricultural Development Council, San Diego, California, USA, August 1977. See also the Report of the Ceylon Banking Commission (1935). The history of the Cheetu system, and its prevalence in different forms was one of the subjects that the Commission thoroughly investigated. It was the considered view of the Commission that if the Cheetu business was allowed to run without any public control, it was liable to degenerate into a risky instrument of depriving people of their savings!

Under this scheme the cheetu prize would vary, depending on the needs of the participants. Thus for instance, the Cheetu prize could be a dozen plates, set of cups and saucers an umbrella or even the measures of rice. It depends on the preferences of participants and their financial resources. Under the auction Cheetu system, discounts are distributed among the unsuccessful bidders only, at each auction. Here again the participants meet once a month as a general rule, and the number of participants range from ten to fifteen.

Competitive bidding is the governing factor which determines the participant who will be entitled to the Cheetu. The participants who wish to avail of the Cheetu money sooner, rather than later (eg. to overcome a temporary financial difficulty, or illness in the family) pay a premium that is distributed as interest to reward late collections. Under both systems, the organiser is entitled to the first Cheetu - it is the reward he earns for his managerial and organizational skill. It means therefore that under the auction Cheetu system, the auctioning really commences with the second Cheetu: during the first month an agreed sum of money, the Cheetu contribution, is collected and handed over to the organiser. It is the responsibility of the organiser to ensure that the Cheetu cycle ends on a happy note, with all the participants receiving their due share of the contribution or collection as their turn comes. Where a member fails to honour his obligations - a rare occurrence in village society - it is the responsibility of the organiser to make good the loss that the other participants would incur. In both types of Cheetu, the twelve month cycle is the preferred period.

The salient feature of the Cheetu system is that on the one hand the credit system rotates, while on the other, the savings position rotates also. While there is general uniformity underlying the principles of the system, practices vary according to each local area. Key determinants in current practice range from the customs and traditions in each locality, the socio-economic standing of the participants, to the degree of urban influence, and the impact of the

many changes in the countryside as a result of the development programmes of the Government. In the traditional (Purana) villages, the Cheetu system by the drawing of lots is the more popular, while in village areas that are in close proximity and more receptive to urban influences, the auction Cheetu takes pride of place.

Eligibility is a matter for the participants to decide. Anyone invited to join participates as a member of a Cheetu cycle as an equal. There are no formalities to be observed. The participants would join together, and agree among themselves on the rules of the game. They would decide to contribute a stated sum of money in instalments, or pay the amount decided upon at the auction at regular intervals. When the last participant receives payment, the Cheetu cycle is automatically dissolved. Invariably, another Cheetu would be organised, and so the practice goes on in the village, almost from one generation to another.

On a superficial view, membership appears to be open, and to cut across barriers of age, kinship groups, status and occupation. A hard second look, however, would suggest the inference that a careful process of selection is very much in evidence. Each grouping enlists for its membership villagers with like interests, of similar financial resources, and common forms of employment and social standing. Thus, teachers in the village school have their own Cheetu club, while farmers run another of their own. The traders and the more affluent in the community organise a separate Cheetu, while the poorest of the poor, who are often shunned by the rest of the community have their own modest arrangements. Much as a farmer would like to join a farmers' Cheetu group, he would prefer to stay away from the Cheetu club of the teachers, and the teachers in turn would like to confine their activities to an exclusive circle of teachers.

The outstanding feature of the Cheetu system, and consequently the

reason for its popularity and success, is the fact of local control and responsibility in the allocation of Cheetu money. Cheetu clubs are self selected peer groups that shape their own organization and make their own rules; there is a great deal of flexibility in the Cheetu mechanism. Its adaptability to a variety of purposes makes it a popular pastime among all strata of rural society.

An important factor that accounts for the success of the Cheetu system in rural society is that it is confined to a small group of people known to each other at a very intimate level. The participants trust each other's financial dealings. Savings capacity, creditworthiness, and a good moral standing in the rural community are decisive criteria for the selection of members. Likewise, the length of stay in the village, the kith and kin groups to which one belongs, and the company one keeps are also given due weightage in the selection process. Very often Cheetu guilds coincide with various forms of kinship and extended family ties. This is particularly so in the case of Purana (traditional) villages. In the absence of such characteristics, common and shared interests, neighbourhood relations and family ties are factors that contribute towards bringing together like minded villagers for the purpose of participating in the Cheetu.

Share contribution obligations are taken very seriously by the villagers. Cheetu practice in rural communities has, over a long period of time, evolved its own mechanisms for dealing with the problems of risk and default. Default occurs when one of the participants after having drawn his Cheetu money, avoids the payment of money to the fund. There are occasions, however, when a participant in a Cheetu cycle is forced to withdraw from the Cheetu for reasons beyond his control eg. when he is no longer able to pay the share money due to some unforeseen calamity. If he withdraws before he gets his Cheetu prize money, he has merely lost his savings, and he should take steps to retire his earlier contributions. This is generally

done by substitution of membership. The members would try to find a substitute to take the place of the one that left; if this fails, either the Cheetu organiser or a participant would take over, and would thus be entitled to two shares in the Cheetu. When several partners withdraw at more or less the same time, and no substitutes are found, the Cheetu cycle is liquidated. In such an eventuality the organiser would try his best to ensure that everyone gets his money back. Sometimes he would fail to recover all the monies contributed by the members and the organiser loses face. To maintain his honour and self respect in the village he would pay back the members out of his pocket; sometimes he is forced to do so under pressure from the participants who had parted with their money by joining a Cheetu cycle of doubtful value!

Deviant behaviour in respect of Cheetu obligations is visited with sanctions of varying degrees. These sanctions could range from the member being disallowed to participate in future Cheetus to his being ostracised more or less by the rest of the community. An errant member would soon realise that he was being kept away not merely from one Cheetu club but from all such organizations in the village; he would find it difficult to negotiate a loan even from the local money lender or the trader. Sometimes these sanctions can be of a serious nature particularly among the fishing communities that dot the coastal areas like Pamunugama or Pitipana on the western shore. It would indeed be a daunting prospect for a villager to transgress the accepted standards of behaviour, and even though he may leave the village for a while, the rest of the community would await the day for the maverick to return to his village.

Mutual trust, honour and responsibility, especially in financial transactions do not mushroom overnight with the formation of a Cheetu club; effective groups are built up, rather, over a long period of testing

and tentative associations. The compulsions of village society coupled with the stigma attached to dishonourable conduct could incur collective disapproval, and these act as effective and built in barriers against fraudulent default. Indeed, such default is viewed as a personal affront by the other members of the Cheetu club.

A noteworthy feature of the Cheetu system is its diffusion of responsibility. Thus, eligibility and credit rating are matters that are the exclusive concern of the group of participants in the Cheetu Cycle. It is a group decision - a fellow villager is simply invited to join the forthcoming Cheetu, and he thereby stands elected. The terms and conditions of the loan or rebate are stipulated by the participants who make their own decisions, and are each other's customers. The entire Cheetu operation is initiated, worked out and terminated by the villagers themselves. Hence, the rules and regulations that regulate the Cheetu operation are intelligible to all, and are consistent with the socially and culturally accepted norms of rural society. In point of fact the Cheetu partakes of an almost institutionalised character in the village community: the participants themselves would decide what contributions are to be made, who is eligible for participation, and the sanctions that are to be applied in case of errant and deviant behaviour.

It bespeaks of the ingenuity of the rural people that a cheetu cycle does not last more than twelve or eighteen months. If a cheetu cycle runs beyond this period there is always the risk of default, either by death of the participant, deliberate non-payment of share contribution, or by migration to the new settlement schemes under the Mahaweli Development programme. By confining the Cheetu cycle to a short period of twelve months or so, these risks are greatly minimised.

The overhead costs of Cheetu operations are negligible. Very often the only items of expenditure are an

exercise book and a pencil, where all transactions are carefully documented. There is no need for any office space, staff, tables and chairs, typewriters and other office paraphernalia. The organiser is in charge of all monetary transactions, and it is his responsibility to ensure that the money is collected by the due date. The contributions so collected are handed over to the participant whose turn it is to receive the Cheetu. The procedure is simple and straightforward. As a matter of general practice, participants meet in the home of the organiser; in certain villages the meeting place so rotates, and it is usually the home of the recipient of the Cheetu money for the current month. The money is carefully counted, and the organiser hands it over to the participant whose turn it is to receive the Cheetu. This transaction which is concluded in a few minutes, is done in the presence of all the other participants.

### The Dynamics of the Cheetu System

One of the most compelling reasons for rural people to join Cheetu clubs is that it generates the principle of forced savings. If a villager has a few rupees with him, the normal tendency would be for him to spend it on consumption needs and other trivialities. The Cheetu practice enables him to accumulate more sizeable sums for a worthwhile cause: the saver has the relatively secure knowledge that his small periodic savings will be eventually converted into a large lump sum, and at an earlier date than when saving individually.

The repayment of share contributions is in instalments tailored to suit the debtor's cash flow pattern. In point of fact, the debtor himself opts for the repayment schedule by joining a Cheetu cycle of a particular frequency and duration and particular contributions. To illustrate the proposition: if there are three Cheetu cycles among farmers in a village that operate simultaneously, with share contribu-

tions of Rs.100/=, Rs.50/= and Rs. 10/= respectively, a farmer could opt to join the cycle which suits him best, as far as payment of the Cheetu instalment is concerned.

Rural people participate in Cheetus for anticipated consumption or social expenditure. A prudent mother might visualise the situation where she might utilise the Cheetu money for payment as dowry for settling her eldest daughter in marriage. Or again a fisherman in the coastal village of Kepungoda might expect to spend his Cheetu bonanza in an ostentatious way during the Christmas season. The new bride might like to invest money on an almirah for the home, but she may not have the initial deposit money; hence her justification for participating in the Cheetu. Sometimes Cheetu money comes in the form of an insurance for an unexpected contingency like a death in the family or a major flood that would bring the villager to the brink of ruin.

In the unorganised money market in rural Sri Lanka, the initial interest free Cheetu money that accrues to the organiser is important: he could deposit it in the People's Bank or the National Savings Bank as a fixed deposit, and receive interest at the rate of sixteen or eighteen per cent per annum, at the prevailing rates of interest; alternatively, he could invest his money in some small scale business undertaking, or expend it on the education of his children. For the recipient of the final Cheetu, it is an enforced saving insofar as he extends credit to his fellow members who received the Cheetu money earlier. The intermediaries between the first and the last recipients alternate between debtor and credit positions: every member saves until he receives his Cheetu for the instalment he pays is a de facto saving. Once a participant receives his Cheetu money, he commences to repay the loan in instalments. In simple terms, it means that the Cheetu money received by members at intermediate points in the life cycle of the Cheetu includes a share equal to the

sum of their past and current contributions, and additionally a portion which is a loan to be repaid out of their future contributions.

Cheetu organizations in rural Sri Lanka have a socialising function. The spirit of give and take, and a feeling of togetherness pervades the atmosphere: if calamity strikes one of the participants, the other members would not hesitate to help him out of his difficulties. Even though he might be the recipient of the final Cheetu, the membership would arrive at an amicable settlement whereby the unfortunate victim would be given the forthcoming Cheetu, or the one immediately after. In his hour of need all his fellow Cheetu associates are with him. It is an expression of the principle of mutual aid which is the golden thread that binds the village community together.

#### The Cheetu Ordinance No.61 of 1935

The modern refinement of the traditional Cheetu system is recognised by law and is governed by the Cheetu Ordinance No. 61 of 1935.<sup>(2)</sup> The incorporation of Cheetu practices into the statute book was debated in the State Council in the context of mounting concern due to the unchecked proliferation of Cheetu clubs, their mismanagement, abuse of power and corrupt practices that sucked the villager of his life blood and condemned him to a perpetual state of servility.

An important provision in the new legislation was that it sought to exempt Cheetu operations under fifty rupees from its purview. This was not a concession to the Villagers who were used to the traditional Cheetu system which was a normal practice in the rural community: it was, rather, an admission of the inability on the part of the authorities to effectively supervise and control every form of Cheetu operation. In introducing the Bill in the State Council on 22 October 1935

seeking to legalise Cheetu operations in the country, Hon. Peri Sunderam, Minister of Labour, Industry and Commerce said.<sup>(3)</sup>

"The reasons for exempting Cheetus under Rs.50/- is that it has become such a popular institution in many parts of the country that if we try to include every Cheetu, the object of the Ordinance will be defeated, because supervision and control will become almost impossible. Therefore one took into account that private Cheetus under Rs.50/= should be exempted where people had confidence in each other and wished to organise small Cheetus and carry on in that manner".

The Cheetu Ordinance No. 61 of 1935, as amended, provides for the registration and control of Cheetus. Under this Ordinance no scheme or arrangement purporting to be a Cheetu will be deemed to be a Cheetu, unless at the time of the formation of that scheme or arrangement, the persons joining as subscribers and the person acting as the Manager of the Cheetu agree upon and adopt the essential terms and conditions as spelt out in the law.

Under Section 4 of the Ordinance, every scheme or arrangement which, notwithstanding that it purports to be a Cheetu in the eyes of the law, for the purpose of the Ordinance is only deemed to partake of the nature of a Cheetu: No rights or claims under any scheme or arrangement which only partakes of the nature of a Cheetu is enforceable in a court of law. In *Paramasothy V Suppramaniam*<sup>(4)</sup> (1938) it was held

(2) Legislative Enactments of Ceylon, Chapter 159 Vol 6 (1956 Revision) Government Press, Sri Lanka.

(3) Hansard 1935 Vol 3 page 3938.

(4) 38 New Law Reports 529.

that a contribution for a Cheetu which does not comply with the provisions of the Ordinance is precluded from maintaining an action for the recovery of his contributions.

In terms of the Ordinance every Cheetu should be formed by the execution of a written agreement between the Cheetu manager (organiser) on the one hand, and the intending subscribers severally, on the other. Every such agreement should contain all the essential terms and conditions, with the actual amounts, dates and other particulars necessary in each case.

These stringent requirements would suggest the inference that a Cheetu agreement in the eyes of the law is a very formal undertaking which provides adequate and effective safeguards against deceit, fraudulent misrepresentation and corrupt practices. Among the members of the rural community, these legal formalities are never observed, even though the Cheetu contribution might exceed the statutory limit of Rs.50/=. Rural people have neither the time nor the understanding to comply with all these meticulous details. Additionally, such an arrangement robs the village Cheetu of its basic characteristic - its informality.

The underlying principles of the statutory law relating to Cheetus are determined by the English law concepts of trust and equity. Cheetu practices in the village, however, are more in consonance with the Common Law of Sri Lanka and would seem to be heavily influenced by the idea of good faith, the principle of *Uberrima fides* of the Roman-Dutch law. Village Cheetu practice is also conditioned by traditional custom and usage, rather than on a rigid adherence to codified law based on English concepts.

#### SOME CONCLUDING OBSERVATIONS

Cheetu organizations form an

integral part of the informal and unorganised money market in rural Sri Lanka. It has captured the imagination of all segments of rural society and it is flexible and adoptable to rural peculiarities and local conditions. In spite of the strains of commercialism and the seductive penetration of a money economy, the traditional socio-economic pattern of the rural communities which provide for a mutual set of a relations for individuals within the system still has its influences in the rural areas. Cheetu clubs are part of the reality of community life in the villages in Sri Lanka, and they are a necessary component in the socio-economic pattern of the rural community.

In presenting the national Budget in Parliament of 14 November 1984, the Minister of Finance conceded that the banking sector was not geared to cater to the special needs of the country. He was particularly concerned about the rural sector, the small man and self employment. To fill this lacuna he had decided to establish Regional Rural Development Banks in various parts of Sri Lanka. In the words of the Minister of Finance, these new banks

"will be specifically empowered to grant loans to farmers, fishermen, cooperative societies and various societies and groups involved in production, processing and marketing. The success of these banks would depend entirely on the understanding, training, motivation and devotion to duty of the personnel who will be manning them. As far as possible these persons will be selected from the area of operation of each bank. We expect these personnel to act as 'barefoot bankers' mobilising the savings of the area, carrying out viable lending operations and helping the rural people to raise their standards of living....."

Despite the fact that the Government is now directly involved in the provision of rural credit through the Department of Cooperative Development, the People's Bank,

the Bank of Ceylon etc. these institutional arrangements have not succeeded fully in dissuading the villagers either from accepting credit from money lenders or from participating in traditional Cheetu organizations. The infirmities in the present institutional system would suggest therefore that an opportunity be afforded to test the efficacy of indigenous credit and loan operations as exemplified in the Cheetu system.

There is today a strong case for suggesting that the informal money market in the rural areas, demonstrated in part by the operation of the Cheetu system with its informality, flexibility and adoptive potential in generating both savings and credit for the rural people, be intergrated with the organised banking sector so as to provide a more meaningful banking service to the rural sector.

The establishment of the new Regional Rural Development Banks makes it indeed time opportune to initiate positive action in this direction. It is of course necessary to devise adequate safeguards to ensure that such a merger does not involve the weakening or the disruption of the traditional practices. The Cheetu system has survived for generations among the rural communities of Sri Lanka, pre-dating the introduction of State sponsored credit programmes. As Professor Bouman points out in his survey of non-formal credit organizations at the village level in developing countries, the fact that these clubs and organizations have held their own in the face of the onslaughts of commercialism and a money economy, especially Western banking methods and economic institutions in whose utility and effectiveness development planners place unlimited faith and trust, suggests the inference that there is still a need and a place for them alongside other, more modern financial intermediaries.

(5) See "The ROSCA : Financial Technology of an Informal Savings and credit Institution in Developing Economies", by Prof. F.J.A. Bouman in 'Savings and Development' published by FINARFICA, Cassa Di Risparmio Delle Provincie, Lombardy, Italy. Quarterly Review No. 4 1979.