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SEMINAR ON INFORMAL FINANCIAL MARKETS IN DEVELOPMENT

PAWNBROKING AS AN ATTRACTIVE ALTERNATIVE TO CHEAP CREDIT POLICY:

Cases from India and Sri Lanka

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ABSTRACT

Pawnbroking is a form of financial service that is widely used by poor people in many countries. It is also often depreciated or even ignored by policymakers and designers of development projects who want to give credit to the poor and who advocate cheap credit as the preferred form. Examination of pawnbroking, using evidence from India and Sri Lanka, shows that pawnbroking has many advantages that account for its continued popularity. These include convenience to users, cost structures that are appropriate for services affordable by the poor, and low transaction costs to all concerned. Confirmation of the superiority of pawnbroking as an alternative to cheap credit programs and projects, especially in rural areas, is found in the introduction of pawnbroking services by commercial and specialized banks in these countries.

Foreword

This paper is based on research of pawnbroking activities in Sri Lanka in 1980/81, The Netherlands in 1984/85 and India in 1986. Research for the Sri Lanka case study was carried out by R. Houtman; results were earlier published by F.J.A.Bouman & R.Houtman, 'Pawnbroking as an instrument of rural banking in the Third World', Economic Development and Cultural Change, Vol. 37, Oct.1988 (69-89). Data for the Indian case study were collected by R. Bastiaanssen, the second author of this paper. They have been published in extenso in his MSc Thesis 'Pawnbroking in Sangli District, India', Agricultural University of Wageningen, The Netherlands, 1986 (mimeo). In abbreviated form they appeared in:F.J.A.Bouman, 'Small, short and unsecured, informal credit in India', Oxford University Press, New Delhi, 1989. Bouman is also the first author of this paper; until his retirement in 1988 he was lecturer in 'Agricultural Credit and Cooperatives' at the Agricultural University of Wageningen in The Netherlands.

Pawnbroking as a promising alternative to the cheap credit policy in developing rural economies.

By F.J.A. Bouman and R. Bastiaanssen.

Introduction

Over the past two decades, national governments and international donor agencies have designed many programmes of assisting small rural enterprises in Third World countries through a liberal supply of credit. Most credit was priced below costprice. Administration of these so-called cheap loans was consigned to specialized farm credit institutions, cooperatives and commercial banks. Donor agencies entrusted such programmes to existing N.G.O. (Non Government Organizations) in the receiving country - or even started new ones - with the specific purpose to look after the interest of the weaker sections of the economy. Commercial banks in particular, bogged down in the conventional routine of financing large enterprises in industry and commerce and reluctant to deal with large numbers of small-time borrowers, were put under great political pressure to make loans to officially recognized priority sectors in national and regional development plans.

This cheap credit policy has not been without its critics, disclaiming the basic philosophy behind this policy while advocating interest rates that reflect the cost of lending (Von Pischke, Adams and Donald, 1983; Adams, Graham and Von Pichke, 1984). Like most other subsidies do, cheap and easy loans, of which repayment seems unimportant, create their own climate of mismanagement, dishonesty and corruption. Eager politicians have seen the distribution of these loans as a popular theme to charm the electorate and further personal ambitions and ideologies. Often, it spelled disaster for the participating finance agencies when a forced increase in the number of low-volume loan accounts resulted in overburdened bankstaff, declining control, low quality lending, alarmingly high overdues, deteriorating customer service and, finally, unviable financial institutions. Cheap credit, by itself, does not create opportunities in an hostile environment or redress unfair terms of trade between the city and the countryside. A financial policy that is not in concert with economic realities, nourishes its own culture of discontent, it stimulates evasive tactics and manipulation and erodes both lenders' and borrowers' moral behaviour.

Problems of moneylending in a penny economy

Bouman and Houtman (1983) have moved the case against the cheap credit policy one step further by arguing that raising interest rates on loans to priority sectors does not really solve the banking institutions' dilemma of moving away from orthodox banking towards grassroots development banking. Banking at grassroot level is faced with the near-impossible task of survival in an environment that has all the characteristics of a penny economy. Transactions between individuals in such economies, be they farmers (often a part-time profession), shopkeepers, traders, blacksmiths, millers, carpenters, tractor drivers, oxcart owners and other transporters, are low-volume and often of a temporary nature. The sale of produce in the market is atomized, bananas and cigarettes are sold apiece rather than in bunches or packets, melons and pineapples in slices, sugar in lumps, fertilizer in baskets or kerosine tins. Houses are built or improved in stages, while rural households temporize consumption to put savings aside for the next phase. Money transactions in such an economy are equally small, very frequent, and measured in pennies and dimes rather than pounds or dollars. Money is saved and borrowed not once but repeatedly and loans are piecemeal for very short periods. In local markets and petty trade only a few rupees may be borrowed in the morning and returned with interest in the evening.

Such money transactions offer no attraction to the formal banking sector but are taken care of by operators in the informal financial market. Formal institutions that are persuaded to handle financial services in a penny economy face two major obstacles: volume and risk. The risk factor is an obvious one and sufficiently documented in the literature on rural banking. Governments have, therefore, provided banks with easy access to preferential refinancing schemes and insurance against default on loans. This is the case for instance in India, where Annual Plans contain detailed projec for each district that are based on norms handed down by the Reserve Bank, the country's Central Bank. The Draft Action Plan for Sangli, a semi-arid and sparsely populated district in southern Maharahstra with two million people, covers 31,466 beneficiaries and includes 23 different banks (Bouman,1989:113) But these well-intended plans have also inadvertently created a banking climate of reluctant compliance and a loss of sense of direction. The phenomenal increase in numbers of loan accounts, together with the required compliance with the detailed norms of the Reserve Bank, have placed a severe strain on t banks' organizational resources by having to spend extra efforts to find suitable beneficiaries and control the use of loans.

Moreover, it made banks all the more disinclined to spend manpower and resources to make loans outside the purview of the officially recognized priority sectors that could not count on the government's generosity of preferentia interest rates and insurance against defaulting borrowers. Through lack of initiative and inspiration, or by habit, banks remained faithful to the conventional policy of staying away from making mini-loans in the penny economy. In Sangli these loans, as before, are left to the informal sector.

This reluctance of banks to bring financial services to a penny economy is understandable. Mini-loans raise the most pressing problems that looms even larger than risk. It is volume, or, rather, the lack of volume. Contrary to the risk factor, the problem of volume has drawn scarce attention in literature on development planning and banking. An example from India illustrates this point.

Essentially, a bank is little else but a money shop, buying money from the public and the Central Bank and selling it again to customers in need of capital. Like other shops, it obtains its income from the margin between buying a selling. In banking terms this is called the spread. Fierce competition in th normally lucrative banking business keeps this spread small, and the viabilit of the money shop depends on its ability to make a lot of substantial money transactions. Ideally, this is done by catering to the needs of large enterprises and rich customers, who can produce sufficient collateral to minimize the risk of defaulting loans.

Consider now the plight of an average Indian rural bank that is directed to give priority to serving the weaker rather than the strongest sectors of the economy. Put the annual overhead costs of this bank at Rs 60,000.+ This includes salaries and allowances of its two loan officers, one teller and one clerk, a minimum staff to handle business; office rent, furniture an equipment such as typewriters, filing cabinets and a small computer; maintenance, forms and other stationary, postage, telephone charges and sundries. The staff might even have a small car or motorcycle at its disposal to visit out-of-the-way customers.

With a spread of four percent as profit margin, which is not unusual in I dia's cheap credit policy, this bank needs at least a loan volume of Rs 1,5 million to cover costs (four per cent of Rs 1,5 million equals Rs 60,000). That is, not counting loan default or agriculture's seasonality, when farmer may redeem their loans within six to ten months. In that case, the bank's resources are not fully utilized, but remain idle for part of the year, whil payment of interest to savers must continue.

Loans to participants in a penny economy are usually only small. Loans of the Regional Rural Banks of India, set up specifically to serve the weaker sections of society, averaged Rs 835 per account in the mid-seventies (Shett 1443). Even when put at Rs 1500 per account at present to account for inflation, our rural bank's two loan officers together need to process 1000 loans. - that is 500 each - to achieve the necessary lending volume of Rs 1,5 milli

It is true that typical low-cost institutions such as the village Primary Agricultural Credit Societies (PACS) in India, that also enjoy a four per ce spread, have much lower overhead costs. These PACS operate from humble, rent free premises, have little office equipment and a smaller, but underpaid and hence less motivated staff. In the Sangli District, annual overheads of a typical PACS vary between Rs 15,000 and 20,000. Yet, its lonely secretary would still need to make between 375 and 500 loans to guarantee a workable

+ Rs 60,000 is approx. US $ 4100 in September 1989 credit section.

In contrast, the average staff officer in the Indian banking system handl 120 deposit accounts and only 14 loan accounts per officer; the highest productivity is recorded by the very innovative Syndicate ank with 207 deposit and 40 loan accounts (Bouman, 1989: 125, citing an A.I. . report of 1985).

Other data about the managerial capacity of lenders, expressed in number of loan accounts, are hard to come by. Indonesia's official credit programme "Small Investment Credit/Credit for Permanent Working Capital (KIK/KMKP)" was set up in 1974 for the specific benefit of small enterprises in all sectors of the economy, both rural and urban. At the end of 1983, when it was surveyed by the first author, outstanding loans totaled almost US 2 billion, or more than ten per cent of outstanding bank credit in the country (Bouman, 1984:5). The programme offered borrowers a subsidized interest rate of 12 pe cent per year, which was about ten per cent below the going market rate of commercial banks at the time. Participating banks were put under great press re to make the programme a success and some of their staff were specifically trained to find suitable enterprises and beneficiaries. During the field survey, however, it became evident that most of this staff had clearly lost control of loan quality. Some enterprises had gone bankrupt, others could not even be traced because the owners apparently had stopped operations without notifying the supervising loan officer. In one case the owner had recently undergone heart surgery and could no longer work; he had not seen a representative of his bank in the past 18 months. The embarrassed bank official explained this was due to his heavy workload of supervising close to one hundred loan cases. One bank manager ventured the opinion that the maximum numbe that could be handled properly by one officer was somewhere near 50 loan accounts.

It is equally hard to find parallel data on the managerial capacity of lenders in the informal financial market. Hospes in his Conference paper reports that non-Chinese shopkeepers in Ambon, Indonesia, have between 4 and 4C borrowing customers (Hospes:6)[1], while Ladman and Torrico found that informa moneylenders in three Bolivian provinces had between 1 and 25 debtors each (Ladman and Torrico:3).[2)]

Even more telling may be that organizers of informal saving and credit sc cieties in many countries put the ideal size of these clubs between 20 and 2 members and the maximum at 50. They argued that a membership beyond 50 was "too much to handle". These statements come from organizers of Cheetu in Sri Lanka, Bishi in India, Kelompoks in Indonesia. Organizers of societies run b the Bangladesh Rural Advance Committee expressed a like opinion (Bouman,1983 5).

If this is the case in the informal financial market, with its almost daily face-to-face contact between lenders and borrowers living in close proximity, what is one to expect of lenders in the formal market where such close relationship is quite unusual? Often bankstaff have to find the neces-sary information on a prospective borrower's financial position and the via-bility of his enterprise through a series of interviews at the bank's pre-mises; or, worse, through a set of forms with a number of questions dictated by bureaucratic and institutional routine. Such routine is bound to raise both lenders' and borrowers' transaction costs and keep the latter away from the bank's windows.

Viable financial intermediation in a penny economy requires an instrumen that can overcome the twin obstacle of low volume and risk. If interest rate should reflect the cost of lending, a first concern is to minimize cost and yet make a sufficiently large number of loans. Ironically, the instrument that satisfies all the requirements of quick and safe procurement of loans has been available to lenders for ages. It is called pawnbroking.

Of private and public pawnhouses

Pawnbroking is probably the oldest method of lending in the economy. Pawn brokers are mentioned in the Old Testament (Schwed:21) and existed in ancien Babylon, Athens and Rome (Kelles:2). One could pledge almost anything, including slaves, women and children, even one's own labour, in exchange for goods or money. Nowadays the most popular form of pawnbroking is by pledging gold, jewels and precious stones. But all over the globe there are pawnhouse both public and private, whose brokers accept clothes, books,paintings, uten sils and any other article of marketable value.

In Europe, pawnbroking has had a lively, at times turbulent existence between the 13th and 18th century after Italians of Lombard started to perfect the moneylending and moneychanging business. The name Lombard Street in Lon and other European cities is still a reminder of their fame as innovative bankers in the world of finance and trade.

During that time, lucrative pawnbroking and moneylending monopolies could be bought from city and county officials. Kings,princes and generals have pawned the country's crownjewels to finance a royal marriage or a war campaign. The aristocracy, clergy, merchants and the affluent pawned their valuables, expensive clothing,stocks of merchandise and objects of art and worship to finance the purchase of privileges, ostentatious pomp and trade. The less affluent usually pawned their earthly possessions to tide over periods of scarcity and keep starvation at bay.

Interest rates on particular pawnhouse loans could be high, partly becaus of the expenses of storage and insurance[3)], partly because of the high taxes the broker had to pay to officials for the privilege of carrying out his bus ness. In the Netherlands rates varied from 40 to 80 per cent between the 13t and 16th century (Melles:20). The smaller loans carried the highest rates because of their comparably higher transaction costs; they were usually taken by the poorrer strata of society pledging their clothes and furniture.[4)]

High interest rates have always brought discredit to the professional lending business. The pawnbroker in particular was pictured as an evil Scroo enriching himself from the misery of the poor. Public-spirited citizens and the clergy started to champion the cause of official and cheaper public pawnshops run by the state or municipality. The first municipal shop in Europe appeared in Germany in 1198, in France and Italy in the 14th century (Schwed 24). In the Netherlands, the city council of Amsterdam opened the first

'Municipal Loan Bank' in 1614 (it is still in operation), followed by Rotter dam in 1635. In 1642 and again in 1650 some of the English crownjewels have been pledged at the Rotterdam pawnhouse as surety for a loan. The jewels wer never redeemed and eventually the pawnhouse had to sell them at a loss (Melles:71). In the U.S.A., the Provident Loan Society, a non-profit pawnshop in New York, opened its doors much later still, in 1894. It made history in 19? when it was offered the famous Hope diamond to pay for the ransom to the pur ported kidnapper of Lindbergh's son (Schwed:50).

One of the differences between public and private pawnhouses is that, after the contractual loan period has expired, the first have to put the unredeemed articles up for public auction. If the auction results in a higher price for the pawn than the original loan sum plus interest and auction cost the 'profit' can later be claimed by the original owner-pledger. Some owners however, fail to do so. Private houses do not normally hold public auctions which tend to be costly and cumbersome. The public has to be notified, catalogues to be printed, viewing days organized and extra personnel hired. Private pawnhouses prefer to sell the unredeemed merchandise to any interested party and pocket an eventual price difference themselves. To curb the suppos malpractice of pawnbrokers - high interest rates and private sales of pawns many countries have enacted legislation to restrain their activities. However, this has seldom resulted in putting a stop to the private pawnbroking business. Apparently if offers its own specific attractions to the very customers whose interests the state wants to protect.

In Europe and North America the pawnbroking business has much declined and almost disappeared after the nineteenfourties when consumer credit, personal bank accounts and overdraft facilities became widely available to the public. But recently there is a new revival, probably inspired by the phenomenal increase in the price of gold in the seventies. This has induced people to invest and speculate in gold and jewellery as a treasury for the future and a hedge against inflation. The two remaining Dutch municipal pawnhouses, in Amsterdam and the Hague, are floroushing again, particularly afte after it attrected the attention of TV and the popular press. The same is true for other countries. The glossy catalogues of Vienna's public pawnhouse in Austria rival those of Christie and Sotheby and offer a choice of objects of art, antique, je ellery and other valuables. The new interest of the publ in pawnhouse lendi has also sparked a revival of **private pawnshops** that have become, besides a point of lending, a place for the sale and resale of goods. During a recent stay in Brisbane, Australia, the first author noticed many private pawnshops doing a brisk business. Owners of (sometimes superfluous) commodities seemingly prefer to sell to a pawnshop, probably because they expect a fairer price by asking for a loan (that they do not intend to return), or to avoid unpleasant and embarrassing haggling over the price when selling to dealers in the secondhand market.

Comparative advantages of pawnbroking

Essentially, a pawnbroking contract is a sale-repurchase arrangement between lenders and borrowers that is attractive to both parties. "No credit relation, in fact, exists in a typical pawn contract. The pledger sells, as it were, his pawn for a certain sum below the going (appraised) market valu and retains the right to buy it back within a specified time by returning th original sum plus interest. If he does not, he will lose his property, but n further debt exists and hence no ever-increasing debt load"(Bouman and Houtman:73). Pawnbroking is attractive to the lender because lending on pledge sureties reduces risk and transaction costs, the transaction taking only a as long as the time necessary to appraise the value of the pawn.[5)] There is no need of assessing a client's creditworthiness, nor of close contact with and surveillance of borrowers. Pawnbroking therefore allows the lender a much larger circle of borrowers and greatly increases his loanvolume potential, the great stumbling block for lending in a penny economy. There are no costl legal procedures such as registration of mortgage deeds, that may be necessar as protection against default. Seizure of the pledged item is unnecessary because it is already in the lender's possession. If the borrower does not redeem his pawn, the broker may sell or keep it for himself. Pawnbrokers may employ agents in surrounding villages to meet a rising credit demand.This in creases his outreach without much additional cost. Repledging of pawns between brokers also takes place, the financially strong broker refinancing his colleague when the latter's funds are depleted.

In the informal credit market the private pawnbroker usually disguises his lending activities by combining these with goldsmithery or a jewel shop. He needs no large office space but only scales, a strongbox for safekeeping and expertise for quick appraisal. He keeps simple records to keep track of his transactions. Reduced risk and transaction costs also reduce the pawnbroker's interest rates, which are (much) smaller than the rates charged on personal loans where the only security is the reputation of the borrower as a reliable person who will honour his debts. Of course, pawnbrokers who deal in anything that is marketable and combine lending with a secondhand sales business, need much more room to store and display the goods that are not redeemed. He also needs to insure his merchandise against fire, theft and other mishaps. These higher costs, plus the possibility that he is left with unsaleable merchandise, are reflected in his interest rates that are higher than the rates of the pawnbroker specializing in gold and jewellery.

Pawnbroking is attractive to the borrower for the same reasons of speedy processing and low transaction costs and interest rates. He does not need to make costly and repeated visits to a bank to deal with its exhausting and at times embarrassing culture of bureaucracy and legal protection. Neither does he need to offer bribes to an underpaid secretary of his village cooperative or the agricultural extension agent,to force a favourable decision on his loan application. He also does not need to incur additional obligations such as buying from or selling produce to the lender. The borrower simply sells an item to the pawnbroker on the condition to buy it back within a specified time for a higher price.

Popularity of pawnbroking

In Asia the pledging of gold and other valuables has always been popular with people of all strata of society, rich and poor, who have since long become accustomed to save in valuables and gold. "Unlike the coins and banknotes of an individual country, precious metals and stones have universa worth. They have a high degree of liquidity because they can be sold or pledged almost anywhere..... Further, jewellery offers emotional satisfactio and bestows status on the wearer; valuables also function as a hedge against inflation, while bank balances are eroded by it. Gold and stones have a high value in relation to their bulk and are easy to hide, transport and negotiat This is important in times of natural disaster, war or social unrest" (Bouma 1989:72).

Pawnbroking is usually for short periods - three to six months[6] - which suits participants in a penny economy. Income flows in such economy are irre- gular, leading to a high demand for short term credit to tide over periods o scarcity or meet irregular expenses of sickness or other misfortune, taxes, education, social obligations, religious festivals or rites of passage. Peak times in pawnbroking in Sangli District, India, are during the auspicious marriage months March through May; at the end of Ramedan, the Moslim fasting period in Indonesia; or at the beginning or near the end of the crop cycle when money is needed to meet farm expenses or bridge the lean season of food scarcity, as observed in Malaysia. In his survey of the Malaysian informal credit market in 1986, van Nieuwkoop (63-74) found pawnbroking the most im- portant source of informal lending in the rice producing areas, both rainfed and irrigated. It was, however, of much less importance in the rubber produ- cing areas, where personal loans emerged as the dominant form of lending. Undoubtedly this was due to the regular income from rubber tapping, enjoyed by borrowers. It made lenders more willing to forego the greater security of a pawnbroking contract.

In Third World countries, and particularly in rural Asian economies where access to formal banking institutions is limited, there is a great variety of informal lending and borrowing arrangements to suit each particular situ- ation. Many arrangements are rather complicated and may involve obligations - and hence extra transaction costs - that borrowers prefer to avoid, given a choice. There are different price tags to each form of credit, ranging from zero to twenty per cent a month, even five to ten per cent a day, when.

बुडण्या पक्षा ...

The "bad moneylender" who advances
Rs 500 against a promise to repay Rs 5000

The "good moneylender" who advances Rs 5000 against a promise to repay the same amount with interest.

11B

a mini-loan is taken by petty traders on market days. Compared to many other financial arrangements, pawnshop credit represents a straightforward sale-repurchase arrangement between lender and borrower. Its quick procedures, low transaction costs, relatively low interest rate and the fact that the borrower is free from further, possibly embarrassing obligations, explain its wide popularity. Pawnbroking contracts have become increasingly important over the past decade in India, Malaysia, Sri Lanka and Indonesia (Bouman, 1989:74-80).

Curiously, the wide popularity of informal pawnbroking is not shared by lawmakers, public administrators, development planners and social workers. Nor has it attracted the attention it deserve of researchers, nor seems the banking community to have grasped its potential to improve bank-profitablity and serve a wider clientele than the usual group of more affluent customers. In this respect, the Peoples Bank of Sri Lanka is a favourable exception, as demonstrated in the case study that follows. Public opinion on pawnbrokin is infected by a strange form of moral indignation, holding that pawnshops are the poor man's bank of last resort and exploit this position to rob thei customers of their last earthly possessions. This view is probably inspired by moral and religious objections to (high) interest rates, racial prejudice (many commercial lenders being members of ethnic minorities)[7], plus an inherent belief in the superiority of formal banking institutions to serve the economy in the better interest of society at large. The stigmatization of informal moneylenders is aptly illustrated in the two pictures on the next pages. One represents the bad guy of the informal circuit, offering five banknotes of Rs 100 each to the unsuspecting borrower, signing an IOU of Rs 5000; the other shows the good and kindhearted banking official who has a cheque ready for the proper amount.

In many countries pawnhouse credit has therefore come to be regarded as a public service and legislation is enacted to curb and control the activities of the private broker. This is the case in both industrialized and developing countries. The negative view on private pawnbroking is in direct contradiction with empirical fact finding and customers' preference. Pawnhouse credit is not an expression of poverty, it is much more accurate to explain it in terms of a continuing and growing popularity to save in gold. People have a choice in putting one's savings into a bank account and subsequently withdraw them when needed; or to save in gold, jewellery and other valuables an subsequently pledge these for a loan. There is not much difference in both methods; but the fact that many, the poor included, prefer the second one, is surely indicative of certain advantages.

The why's of such behaviour should be investigated, as in the two following case studies of pawnbroking in Sri Lanka and India. These studies have been published in greater detail elsewhere (Bouman and Houtman, 1988; Bastiaanssen, 1986; Bouman, 1989). They show that despite unfavourable legislation and attempts to curb and control the activities of private moneylender the market of registered and unregistered pawnbroking is still very much alive. But there are also signs that the banking community in these countries, charged with looking after the interests of the weaker sections of society, are getting convinced that the provision of pawnbroking services is an effective instrument to reach this very target group. The experience of the Peoples Bank of Sri Lanka in particular is a hopeful sign of a turning tide.

<u>Pawnbroking in Sri Lanka</u>

As in other Asian countries, the hoarding of gold and jewellery in Sri Lanka has been a popular savings device as protection against times of adversity and social unrest. This is particularly true for the Tamil populati a minority group in the country that has regularly clashed with the Sinhalese majority in past and present. Small valuables, that are easy to hide, transport and negotiate, have become a preferential form of savings.

Pawnbroking and moneylending have been the virtual monopoly of the private market for a long time. Agricultural smallholders traditionally obtained loans from Indian Chettiars, who acted as intermediaries between the colonial commercial banks and rural customers (Bouman and Houtman:76). Their prominent role ended after the country gained independence in 1947 and the government started a programme of rural development, spearheaded by domesti banks in cooperation with the Central Bank of Ceylon. Banks were given access to easy finance and insurance facilities, to subsidize loans to agriculture and other priority sectors.

The results of this cheap loan policy were disastrous. Banks were put under immense political pressure of subsequent administrations of different political colour, each competing for the support of the masses by a virtual hand out of easy credit. Unable to handle a large number of small loans, bank lending got out of control. In 1978, 31% of agricultural loans were not repaid (Bouman and Houtman: 77) forcing the government to abandon its policy of cheap credit. The effect was immediate. Without access to cheap refinancing and insurance against bad debt losses, bank lending to risk-prone enterprises came to a virtual standstill: crop loans fell from Rs 365 million in 1977 to Rs 21 million in 1979/80+.

The People's Bank (PB) in Sri Lanka was among the first to face the challenge of rural mass-lending. Established in 1961 as the official leading agent of rural finance, it has set up a dense network of branches to facilitate access to financial services. In 1983, 340 rural banks were in operation. As early as 1964, these branches had started to offer pawnbroking facilities to compete with the private financial market. In 1970, the then existing 90 rural branches together processed 28,000 loans of which 18,000, or 64%, were based on gold pledging. How important pawnhouse loans of the PB have become over the years is shown in Table 1 (copied from Bouman and Houtman: 78).

+ Rs(SL) 100 equaled approx. US$ 6 in 1980.

TABLE 1:

Total Loans and Pawnhouse Loans by Rural Banks in Sri Lanka, 1970-83.

YEAR	RURAL BANKS (N)	TOTAL NUMBER of LOANS (rounded)	PAWNHOUSE LOANS N (rounded)	PAWNHOUSE LOANS Volume in Million Rs (rounded)	PAWNHOUSE LOANS AVERAGE SIZE IN Rs	CONSUMER PRICE INDEX (1980=100)
1970	90	28,000	18,000	2	109	43.4
1971	111	32,000	21,000	2	103	44.6
1972	242	72,000	61,000	7	115	47.4
1973	341	171,000	150,000	23	151	52.0
1974	403	262,000	235,000	38	165	58.4
1975	447	334,000	299,000	50	167	62.3
1976	503	349,000	306,000	54	177	63.1
1977	544	316,000	264,000	56	211	63.8
1978	558	305,000	249,000	61	246	71.6
1979	586	259,000	207,000	67	323	79.3
1980	641	302,000	242,000	97	400	100.0
1983	840	380,000	315,000	224	711	149.0

Source: Review of the Economy, Central Bank of Ceylon, 1980.
Note: One gold sovereign contains approximately 8 grams of gold. At the end of 1980, the PB exersized a loan limit of Rs 560 per sovereign. As the price of gold was then Rs 2,200 buying and Rs 2,400 selling, this limit represents only 25% of the intrinsic gold value of pawns. Consumer price index is taken from IMF's Yearbook of International Financial Statistics, 1986.

The average size of loans in 1970 was only small, Rs 109. To a great extent this was due to the PB policy to restrict lending to only 25% of the intrinsic gold value of pawns. In 1973, due to the rapid rise in the price of gold worldwide, loans could be raised from Rs 250 to Rs 500 per sovereign. This caused an increase in the number of PB pawn loans, to a peak of 306,000 in 1976 (or 90% of total loans). But thereafter, numbers decreased again when the extremely volatile gold market during the seventies made the PB very cautious to maintain its 25% lending limit. Disappointed customers turned back to the private pawnbrokers, lending against 50% or more of the gold value of pawns. Yet, the PB's 840 rural banks made 315,000 pawnloans in 1983, which was over 80% of total loans in that year. This represents a new development in institutional financing in Asia, which, so far, has had little success in reaching the small rural borrower.

<u>Features of PB's pawnbroking policy</u>

One of the attractive points to borrowers is that a pawnloan of the PB carried an annual interest rate of 30% in 1980, reduced to 28% in 1981.[8)] This is much lower than the interest rates charged by brokers in the private market. The PB follows the common standard procedure that borrowers pay a minimum one month's interest, even for loans of shorter duration. But this interest is not deducted from the principal beforehand, as private brokers do.

A pawnloan at the PB has a duration of 1 year; it becomes renewable after interest has been paid. Borrowers who fail to redeem their pledges are entitled to a refund when the pawn is subsequently sold at a public auction and fetches a higher price than the loan sum plus interest. Unregistered private brokers tend to disregard this requirement of the Pawn Brokers Ordinance and pocket eventual profits themselves.

The PB follows the arbitrary policy that distinguishes between credit for production and consumption, and keeps its loan sizes between Rs 500 and 5000, with lower limits for consumption loans. This may be seen as a laudable effort to protect customers against conspicuous consumption, but it is contrary to the very nature of many pawnloans that are taken precisely as protection against emergencies, hardship and obligatory expenditure of religious festival. In agricultural economies the distinction between production and consumption tends to become blurred; this policy can only lead to unnecessary bureaucracy, to the annoyance of the public. The very advantages of pawnbroking, viz. low risk and transaction costs and non-monitoring of loans, are thus lost. Its sole effect is congestion at the bank's windows, compounded by the lack of experienced appraisers of valuables among bank staff. A further inconvenience is that the banks open late in the morning and close early in the afternoon and during the weekend. Customers, looking for discretion and speedy processing, turn therefore to the private pawnshops that offer an almost round-the-clock service throughout the week.

Private pawnbroking in Sri Lanka

Private pawnbroking has a long history in Sri Lanka, with occasional rumors of manipulation to the detriment of customers. This prompted legislators to curb malpractice and bring pawnbroking under control of the government. Under the Pawn Brokers Ordinance, brokers have to register and pay taxes. For some moneylenders this was a reason to go underground and continue their business illegally. The main effects of the Ordinance have been inconvenience to the public. There are now two types of private pawnshops, the registered and unregistered one. The first pays the required 2% Business Turnover Tax (BTT) to the treasury, but passes this on to customers. The second type does not pay taxes, but charges higher interest rates than before to account for the extra risk of operating illegally and being caught and fined.

However, both registered and unregistered pawnshops still draw a large clientele because of their superior service. Firstly, they are more accessible to the public than the banks. They conduct business from early morning to late at night, enabling customers to do their pawning discretely. Most lenders combine pawnbroking with a jewellery shop; this makes them experienced appraisers of valuables and shortens the time to settle a loan transaction. They do not ask for loan purposes, the pledged item being sufficient collateral to cover misfortune.

Secondly, private pawnbrokers offer loans of up to 50% of gold value of pawns and rarely put a limit on loan size. Unregistered brokers may even go as high as 80%. High loans are especially attractive to borrowers who need a lot of money on short notice. In the relationship between borrower and lender, confidence is the essential element to assure a large loan. New and occasional borrowers rarely receive more than half of the pawn's market value, but this still is twice the rate offered by the PB. Some registered pawnbrokers charge a monthly interest rate of 4% plus the additional 2% BTT. Others lend against 5% and pay the tax themselves. The minimum interest charge is for one month, irrespective of loan duration, and deducted from the loan principal in advance. Most unregistered brokers charge 7% interest per month, while escaping the 2% BTT. These rates are much higher than the ones exersized by the PB and are probably the reason why private loans are redeemed so quickly: 50% within 2 weeks, the other half within 2 months. But despite the competion of the rural banks, the private brokers conduct a brisk business. In two random case studies, their loan volume was 12 to 18 times as large as that of the average rural bank (Bouman and Houtman: 81).

Pawnshop economy in Sri Lanka

Little information is available on profitability of institutional pawnbroking. Differences in banking policy and procedures determine performance and turnover of each individual bank. According to statistics of the Central Bank, the average rural bank in 1980 had 380 outstanding pawn loans of Rs 400 each, or a turnover of Rs 152,000 (Bouman and Houtman: 84). Research carried out by the PB indicates that about half of PB branches ran at a loss in 1980 (Siriwardena: 1). This was mainly due to the high default rate on other, more conventional agricultural loans, which are costly to administer and lack suitable collateral. The other half managed to make some profit; according to the same report, these profits originated from the positive financial results of pawnbroking activities (Siriwardena: 2). There is no better proof of the viability of including pawning facilities as a service to the rural population and as a modus to reform institutional financial services.

Rumors of alleged excesses and huge profits made by private pawnbrokers will always persist. These rumors were not confirmed in a three-month study in 1981 of two such pawnshops, one registered, the other unregistered. Data have been published earlier in Bouman and Houtman (82-83; 89) and are presented as such in the Appendix, cases 1 and 2. Figures are partly based on extrapolation

The registered pawnshop in Kandy town had an annual turnover of Rs 3 million and a 32% return on working capital (assuming the broker worked with owned funds only). This return is only 10% above the 22% interest reward on a two-year savings deposit with the PB at the time. This is a small enough margin and can hardly be considered usurious.

The unregistered pawnshop-cum-jewellery store in Colombo had an annual turnover of Rs 2 million. His return on capital of 70% is considerably higher. But one should bear in mind the extra risk involved in illegal pawnbroking and the possibility of closure and extraction of bribes by officials. Another feature of illegal pawnbroking is refinancing with a registered pawnbroker, the latter requiring a commission of 1 to 2% for this service. Moreover, this particular broker, besides working with owned funds, borrowed outside capital from friend and banks at 2.5 to 4% a month. This access to outside funds increases his turnover, but also depresses return on capital.

Pawnbroking in Sangli District, Maharahstra, India

Recent developments in the financial market

Like in Sri Lanka, pawnbroking in India has been a popular form of lending for centuries; increasingly so during the past 40 years because of the steadily rising price of gold which behaves independently of the volatile world market. From Rs 87 per 10 grammes in 1946, it has climbed steadily to Rs 2200 in April 1986 (see Appendix II). This climb continued even between June 1980 and June 1981, when the price at the London market crashed from $ 662,50 to $ 421,50 per ounce. This has made saving and speculating in gold more popular in India then it was already, even with poorer strata of society.

In Sangli, pawnbroking is generally not seen as a disreputable profession. Like in many other countries, the early moneylenders in the district were outsiders, originating from Rajasthan, Gujarat or still further West. When later locals joined in, a gradual network developed of professional and large moneylenders - locally known as Savkars - refinancing smaller operators. Both categories advanced money against gold, jewellery and many other kind of pledges.

When the cooperative sector (from the 1960s onward) and the commercial banks (from the 1970s onward) started to grow in number and importance as financial agents of the rural economy, the private moneylenders lost their monopoly and the Savkars gradually left the district. Their function of refinancing small lenders/pawnbrokers has partially been taken over by the commercial banks.

Since the 19th century, national and state governments in India have enacted legislation in an effort to restrict the activities of the private finance sector. The Bombay Agricultural Debtors Relief Act of 1939 was the first in a series of Acts enforcing settlement of agricultural debts. Other Acts followed in subsequent years. Moneylenders had to register and follow prescribed lending procedures and keep proper records for inspection. The Maharahstra Debt Relief Act of 1975 arbitrarily scaled down farmers' debts with private moneylenders, who in some cases had to return pledged collateral without compensation. This latest step in the official crusade against private lenders caused a number of them to withdraw from the scene, leaving a void in pawnbroking services that was particularly inconvenient to the poorer sections of the community. The Reserve Bank of India (RBI) tried to fill the vacuum by allowing cooperative institutions to enter the pawnbroking business. In terms of loan volume, institutional pawnbroking nowadays outmeasures private pawnbroking.

Pawnbroking by formal financial institutions: advantages and disadvantages

Not all formal institutions are eager to take up pawnbroking, as this usually involve small loan amounts. The commercial banks in Sangli - almost all nationalized - often refer the small borrower to the cooperative sector as the main agent to serve the poor. Some cooperative banks specialize in pawnbroking and have a trained appraiser among their staff, in contrast to most commercial banks.

In general, gold advances are more common with rural than urban banks. Banks offer pawnloans from 50 to 70% of the market value of gold pledged. This is less than the rate prevailing in the private sector - but far exceeds the rate of the PB in Sri Lanka, where the gold price is much less stable, implying greater risk to the lender.

Loan size varies between Rs 100 and Rs 50,000; banks usually maintain a minimum loan amount of Rs 100 to 300. Extremely large pawnloans are supplied by those commercial banks that serve traders and private moneylenders, repledging their own clients' pawns with the bank. Although such refinancing is not authorized by the RBI, it is very profitable to banks; the large transactions increase loan turnover without much administration.

Prospective pledgers who turn to a bank that has no trained appraiser, are forwarded to a nearby jeweller-cum-pawnshop for proper appraisal of the pawn's value. When this same jeweller comes to the bank to repledge his own pawns, the bank can hardly refuse a reciprocal service.

The average common loan amount is estimated between Rs 500 and Rs 3000 (Bastiaanssen:25).+ Usual interest rates are between 16 and 18% annually for both cooperative and commercial banks. These rates are one of the main

+ The gold price at the Bombay gold market (per 10 grams) was Rs 2200 in April 1986.

attractions of institutional pawnbroking. Private brokers tend to charge twice higher rates; rates of illegal pawnshops may be five times higher.

Generally, pawnloans mature after six months, after which they become renewable. Around 25% of borrowers repay within 3 months, 70 to 75% within six months, 90 to 95% within one year; 5-10% of borrowers extend their loans beyond one year.

The pattern of debt and repayment in Sangli mainly follows seasonal crop cycles of planting and harvesting. Pawnbroking peaks also occur during the 'marriage season' from February through May, when people spend considerable sums on dowries and ceremonies. Pawnbroking cycles of the private finance sector follow the same pattern.

Because the gold price in India climbs continuously, borrowers are eager to repay loans. Public sales of unredeemed pawns, therefore, are rare. If one takes place, it is arranged by a reputable jeweller. As in Sri Lanka, eventual surplus proceeds of the auction are returned to the pledger after principal, interest and auction costs are deducted.

As in Sri Lanka, many pledgers turn to private pawnbrokers because of superior service and despite the lower interest rates charged by banks. Banks keep inconvenient opening hours from 10.30 a.m to 3.30 p.m. Further, banks who have no trained appraiser forward borrowers elsewhere to get a valuation report. Thereafter, clients of the bank are faced with an avalanche of forms to fill: up to ten for one transaction only. These procedures take time, patience and additional cost. If all charges of valuation fee, costs of forms, insurance, stamp duty and so on are added, total transaction costs may represent up to 5% of a loan of Rs 1400. This greatly reduces the relative advantage of lower interest rates of the institutional sector when only a small loan is needed.

Nevertheless, the act of pledging with a bank is still a less complex and harassing experience than borrowing under other institutional loan arrangements, especially when rural borrowers get involved in concessional loan.

There are exceptions, too. Cooperative banks that specialize in gold advances show a much more consumer friendly attitude.

<u>Registered and unregistered pawnbrokers in the private sector.</u>

The private registered pawnbrokers employ much less bureaucracy, although they are subject to government inspection and regulation of interest rates. Inspection, however, is only superficial and actual interest rates always exceed the prescribed ones.

Most licensed pawnbrokers are goldtraders, jewellers or goldsmiths and lend almost exclusively against gold. Very few still accept silver. They also grant personal and mortgage loans (on land, houses, vehicles). The typical urban pawnbroker is male, belongs to the middle or upper class and is normally well respected in the community. The profession is not restricted to any particular caste, nor are there indications that caste membership affects pawning transactions.

Despite the growth of the banking sector in the district, Sangli - a semi-arid region of approx. 2 million population - recorded a large increase in the number of registered moneylenders, from 183 in 1965 to 250 in 1974. But the Debt Relief Act of 1975 made many of them to close shop; in 1985 only 95 moneylenders remained to take a license. Most operate in the urban centres. It is unknown whether the overall scale of private lending has decreased as well.

The lender-borrower relationship is primarily based on trust. New customers usually need a recommendation from a third party plus proof that their pwans are not stolen. Mediation on behalf of newcomers by middlemen, known to both parties, is still common practice. Secretaries of village cooperative societies often figure in the role of mediator. Some urban moneylenders employ agents in the countryside on a commission basis. Regular customers, on the other hand, with a reputation of timely repayment, may eventually become entitled to a 'personal loan' without depositing valuables as security.

Private lenders do their own appraising and advance between 75 and 90% of the pawn's gold value, the higher advances applying to reliable and regular borrowers. Interest rates, too, depend on the strength of the relationship between the two parties. The RBI has prescribed a set of rates between 9 and 18%, but these are very unrealistic when pawnbrokers themselves have to pay 17% when repledging with banks, or more when borrowing capital elsewhere. It forces the pawnbrokers to manipualte rules and records for appearance sake. In reality, effective interest rates are 2 to 3% a month for a goldadvance, small and short term loans may carry higher rates still. These rates are consistent with those observed by others in India (cf Bouman, 1989: 91 for references).

Despite the higher interest rates compared to those prevailing in the institutional sector, the private sector attracts many customers. Like in Sri Lanka, this is largely due to superior service: convenient business hours to the public, low transaction costs and speedy and discrete service. Compared to the one hour or more, spent at a bank to negotiate a pawnloan - while other loans may take days or weeks - a private pawnloan transaction is completed in ten minutes. Unlike custom in Sri Lanka, the first month's interest is not deducted from the loan principal beforehand.

Low transaction costs are particularly attractive to borrowers of small sums. The average pawnloan in Sangli varies between Rs 500 and Rs 1500, but extremes occur at both sides of the scale. Some lenders specialize in large loans, like those who refinance fellow pawnbrokers, others may handle loans as small as Rs 50.

The pattern of loan terms and loan use resembles the one in the institutional sector. In general, the smaller the loansum, the longer the repayment period. Large borrowers incline to speedy redemption, to avoid high interest costs. Registered pawnbrokers prefer loan extension to auctioning or selling pledged articles, even when the collateral is sufficient to cover the debt. Public auctions involve official permission, red tape and bad publicity, which is contrary to the required discretion. If need be, the broker arranges a quiet, private sale with the consent of the pledger.

The number of licensed moneylenders in Sangli may have decreased after 1975, but a new class of moneylender has emerged: the part-time, small-scale operator, who is refinanced by the former. Civil servants, traders, teachers and personnel of sugar factories have taken up pawnbroking without a license. They have a regular income and access to banks as well, which befits their role of lenders. In Sangli, this phenomenon was very marked in Ramenandnagar, a small and new industrial town, where factory foremen practised lending after factory hours as a sideline. They cater to a limited clientele and may accept other articles than jewellery and gold pledges.

Type and performance of these informal pawnbrokers vary considerably and are dictated by social factors on the one hand - as with lending to relatives and friends - while others operate on a predominantly commercial basis. Especially in the risk-prone semi-arid zones of the district, where little institutional credit is available, there is a great need for locally available informal credit sources. From the study in Sang - the impression was gained that five to ten informal moneylenders (both male and female) operate in each community of at least 2500 villagers. Their numbers seem to grow rather than decline, which may be due to the spectacular rise of the gold price in India, where the habit of paying dowries in gold has a long tradition. Elsewhere in the district, the introduction of irrigated cultivation and improved agricultural technology have stimulated farmers to invest in and profit from new crops and activities: sugarcane since 1960, followed by grapes,betel-and rosegardens and dairy development. This caused a rise in loan demand that could be met by pawning previously hoarded objects of gold. The resulting boom in the formerly dormant economy, that started in the irrigated areas, spread outwards to other regions and occupations, bringing employment, albeit often part-time, and higher incomes to many. This, in turn, caused a rising demand for consumer goods, even from the have-little rural households, that could partly only be met by borrowing from informal credit sources.

Unlicensed pawnbrokers tend to serve a clientele at the poor end of the spectrum, whose limited loan demands (up to Rs 500) are unattractive to formal financial institutions. The informal moneylender must be very sure of the reliability of the borrower, as his operations are illegal and therefore vulnerable. There is always the danger of confiscation of pawns by police whenever a discontented debtor registers a complaint. Consequently, village pawnbrokers restrict their lending to their own community.

Part-time pawnbrokers not only accept gold, but also silverware, copper and brass pots, clothes and objects of emotional value. Loan rates depend on the lender-borrower relationship rather than the market value of pledges, and range from 5 to 10 % a month. Each transaction has its own particular circumstances that dictate loan conditions. Undoubtedly, some lenders take advantage of borrowers with urgent credit needs.

Unlicensed pawnbroking is both expensive and risky. Loans are small and short term (2 - 4 months only); pawns must be stored and guarded and, other than gold, may loose market value quickly. Finally, the illegal broker face fines and punishment when caught. A high rate of interest, therefore, is by itself insufficient proof of excessive exploitation.

Pawnshop economy in Sangli

Data on the profitability of institutional pawnbroking are not available Some banks may do little, some cooperative institutions no business at all. Others have turned it into a specialization which presumably must be rewarding. Data on the profitability of a moderately frequented private and registered pawnshop are presented in Appendix I, case 3. Like in the foregoing two Sri Lankian case studies, figures are partly based on extrapolation. Our pawnshop had an annual turnover of Rs 390,000 on 300 goldadvances Annual return on capital is calculated at approx. 20%. Compared to the 12% available on a fixed deposit with a bank, this return is not exceptionally high.

Compared to the two Sri Lanka case studies, the figures are much lower, both on the debit and credit side. Pawnbroking, however, represents only a part of the moneylending, comprising also personal and mortgage loans. Moreover, for many houses it is only a sideline to its main activity, the regular gold trade.

An estimation of profitability of illegal village pawnbroking would be of little use. It is only a part-time activity with low turnovers and there is no uniformity at all in operations. But despite its risks, profits appea sufficiently high to bring ever more new brokers into the market.

SUMMARY

Lending to small rural enterprises in developing economies faces two major obstacles, risk and volume. These cannot be overcome by raising interest rates on mini-loans, nor by conventional banking procedures. There are simply too many loans required to obtain a lending volume that covers the bank's overheads. Paradoxically, the instrument that satisfies all the conditions of quick and safe procurement of loans, has been available since early history. It is called pawnbroking.

Except in the more realistic world of informal finance, pawnbroking carries an undeserved stigma of usury and exploitation of the poor. The label is wrong. Compared to ther modes of lending in a penny economy, pawnhouse loans are attractive to both lenders and borrowers because of speedy processing, low transactions costs and interest rates and the fact that they involve no further obligations but a simple sale-repurchase arrangement. Pawnhouse credit is also not an expression of poverty, but rather an indication of the popularity of gold and valuables as a savings device to protect people against future eventualities.

This is demonstrated in two brief case studies of pawnbroking in Sri Lanka and India, where its growing popularity has probably much to do with the spectacular rise in the price of gold since the early seventies. But the banking community in both countries, charged with promoting rural development, has apparently not yet fully grasped the great potential of pawnbroking to bring financial services to the poorer strata of the rural community. The People's Bank (PB) in Sri Lanka is a notable exception, and its experience with pawnbroking a hopeful sign of a turning tide. The PB's 840 rural banks made 315,000 pawnloans in 1983, which represented 80% of total loan numbers in that year. Moreover, those branches that specialized in this mode of banking, managed to make a profit, while others that concentrated on more conventional agricultural loans without suitable collateral, ran at a loss. There is no better proof of the viability of institutional pawnbroking.

The banking community is Sangli District, India, appeared too immersed in the many details of official development policies and plans to pay attention to innovative procedures that did not carry the approval of its supervisor, the Reserve Bank of India (RBI). Yet here, too, are signs of change, banks refinancing private brokers without authorization of the RBI

In both countries, the informal credit market of private moneylending pawnbrokers, registered as well as unregistered, is booming. In India, the price of gold behaves independently from the world market and has climbed continuously to higher peaks since 1946. This has made saving in gold - and hence pawnbroking - nore attractive than it already was. In villages and small rural towns there are many new entrants into the market of informal pawnbroking. But also in Sri Lanka the public frequents the priva-te shops because of their superior service compared to that of the banks. Despite this great popularity, official opinion of private pawnbrokers is still negative in both countries. Research proved this wrong. Profit margins of private pawnhouses appeared reasonably moderate and there were no signs of malpractice. Particularly antagonistic legislation towards informal lenders in India has only caused inconvenience to the public.

Research into pawnbroking activities of both institutional and non-institutional sources offered no particular problems, given a proper approach The stigma of illegal pawnbroking, however, impeded the collection of accurate data, but not an impressionistic view of the nature of its activities As seems to have become habitual with surveys of rural finance markets, both studies concentrated on sources of credit. Future research should pay more attention to needs and problems of borrowers.

Notes

1) The largest wholesaler of Chinese origin supervises a network of 34 shops which he supplies with consumer goods on credit. They act as his sales agents starting their business with an original loan from the wholesaler of Rp 500,000 (approx. US$ 260.-) as working capital. This is an unusually high number of clients and Hospes remarks that this undoubtedly explains why the wholesaler's own shop has only limited opening hours, because of the considerable time spent on checking his debtors (Hospes:16/17).

2) Of the 873 different lenders in the region, "81 per cent made only one loan and only 4 per cent made more than three loans. The pattern was similar in each of the three provinces. Each province had at least one person that made eleven or more loans; the largest number was twenty-three" (Ladman an Torrico:5).

3) For instance, after wintertime, people used to bring their precious fur coats to the municipal pawnhouse of Amsterdam for safe custody and protectic against moths. Bicycles, on the other hand, were pawned after the summer fo storage during the cold and muddy winter. Pawnhouse staff had to be very careful in noting all particulars of the goods before storage, because of th owners' careful examination for possible damage after redemption. Smart pledgers used to claim compensation for bald patches or scratches that had been there already before storage. Furniture, in particular, was susceptible to damage during transport to, or storage in the pwanhouse.

4) The strange appeal of the pawnhouse to some is best illustrated by the 'weekly pawns', consisting of the Sunday clothes of the poor. These were brought in on Mondays, to be redeemed on Saturdays for use at Sunday's churc service and thereafter. The owners reasoned that this way their best clothes brought at least some money in for the weekend, which was not possible when they remained locked away in the cupboard....

5) One of the important functions of the auctions of public pawnhouses is to enable its staff to keep abreast of current prices and consumers' preferences.

6) The six-month contract is the more common one all over the world; usually it is renewable after interest has been paid. A special form of pledging that resembles pawnbroking, is the pledging of trees, the borrower selling usufruct rights until the debt and interest are repaid, after which he take: repossession of his trees. Pledging of cocoa and oilpalm trees occurs in West Africa, of coconut palms in Kenya, of clove trees in Indonesia and of fruit trees in Fiji and Sri Lanka. Contrary to pawnbroking, pledging of tre usually covers one to more years and is a form of leng term lending in the informal finance market that is worthy of more attention than hitherto give by researchers.

7)"Those who frequent the Arab moneylenders are for the most part officials and towndwellers..... These Arabs are often dealers in jewellery as well as moneylenders..... They are ruthless usurers, their practices are those of usurers in all ages and in every clime" (Fruin:113, on moneylending in Indonesia in the nineteen-thirties).

8) Inflation in those yeras was also high, between 20 and 25 per cent. To make saving attractive and collect sufficient capital from the public, the PB had to offer up to 22 per cent interest on long term savings accounts.

APPENDIX I

1. Data from a registered pawnshop in Kandy town, Sri Lanka
(see I[illegible]man and Houtman, 1988:82-83;89)

- number of pawnloans: 3000 a year
- average loan sum : Rs 1000
- 50% of loans redeemed in two weeks ;
  50% of loans redeemed in two months
- interest rate 5% a month

1) annual turnover : Rs 3 million
2) average outstanding loan amount :
   (1500 x 1000 / 24) + (1500 x 1000 / 6) = Rs 312,500
3) required working capital, assuming 10% idle capital :
   110% x Rs 312,500 = Rs 343,750
4) interest received annually plus BTT :
   (1500 x Rs 50) + (1500 x Rs 100) = Rs 225,000
5) annual costs were as follows :

BTT, 2% of Rs 3 million	Rs60000
pawnshop licence	Rs 1400
salaries (manager, accountant, clerks)	Rs34800
shop rent	Rs15000
urban quarter tax (estimated)	Rs 250
rent of safekeeping facility at bank	Rs 250
sundries (electricity, furniture, stationary)	Rs 3300
total annual costs :	Rs 115,000

6) annual return on capital : (225,000 - 115,000) / 343,750 = 32 %

2. Data from an unregistered pawnshop-cum-jewelry store in Colombo, Sri Lanka

- number of pawnloans : 800 a year
- average loan sum : Rs 2500
- 50% of loans redeemed in two weeks ;
  50% of loans redeemed in two months
- interest rate 7% a month ; no BTT charged

1) annual turnover : Rs 2 million
2) average outstanding loan amount :
   (400 x 2500 / 24) + (400 x 2500 / 6) = Rs 208,330
3) required working capital, assuming 10% idle capital :
   110% x Rs 208,330 = Rs 229,130
4) interest received annually :
   (400 x Rs 175) + (400 x Rs 350) = Rs 210,000
5) annual costs were as follows (as far as known and imputed to lending activities) :

imputed salaries (4 co-managers)	Rs 36000
shop rent	Rs 10000
urban quarter tax	Rs 125
rent of safekeeping facility	Rs 125
sundries (estimated)	Rs 2750
total annual costs :	Rs 49,000

6) annual return on capital :
   (210,000 - 49,000) / 229,130 = 70 %

APPENDIX I (contined)

3. Data from a registered pawnshop in Sangli, India
(see Bastiaanssen: 42-43; Bouman, 1989: 97-98)

- number of pawnloans : 300 a year
- average loan sum : Rs 3000 (with duration of 3 months);
  Rs 1000 (for all other pawnloans)
- 15% of loans redeemed in 3 months ;
  40% of loans redeemed in 6 months ;
  35% of loans redeemed in 1 year ;
  10% of loans redeemed in 2 years
- interest rate 2% a month

The owner is the sole operator and has no hired help.

1) annual turnover :
   (45 x 3000) + (255 x 1000) = Rs 390,000
2) average outstanding loan amount :
   (45 x 3000 / 4) + (120 x 1000 / 2) + (105 x 1000 / 1) +
   (30 x 1000 / ½) = Rs 258,750
3) required working capital, assuming 10% idle capital :
   110% x Rs 258,750 = Rs 284,625
4) annual interest received : 24% x Rs 258,750 = Rs 62,100
5) annual costs were as follows (estimated) :

moneylending licence	Rs 100
inspection charges	Rs 500
insurance	Rs 2000
safe locker	Rs 250
shop rent, imputed	Rs 1000
tax / representation	Rs 1150
sundries	Rs 1000
total annual cost :	Rs 6,000

6) annual return on capital : (62,100 - 6,000) / 284,625 = ± 20 %

APPENDIX II

Gold Prices in India (Rs per 10 grams)

YEAR	AVERAGE PRICE	YEAR	AVERAGE PRICE
1946-47	86.66	1975-76	519.10
1950-51	97.28	1976-77	549.50
1955-56	82.13	1977-78	637.33
1960-61	114.91	1978-79	994.64
1965-66	133.34	1979-80	1345.00
1970-71	184.96	1980-81	1610.00
1971-72	200.16	1981-82	1655.00
1972-73	242.14	1983 (Febr.)	1740.00
1973-74	369.23	1984 (Febr.)	1895.00
1974-75	519.10	(July)	1985.00
		1986 (April)	2200.00

Source: C.P.S. Nayar (Personal Communication)

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