

CHAPTER II

SOURCES OF CREDIT

The credit structure in this country consists of the organized and unorganized credit markets. The former comprises of formal institutions like commercial and merchant banks; borrowing companies; rural credit institutions; industrial finance institutions; housing credit institutions and various government agencies, for example the Majlis Amanah Rakyat (MARA), the Urban Development Authority (UDA), the Malaysian Industrial Development Finance Bhd. (MIDF), the Malaysian Industrial Estates Sdn. Bhd. (MIEL), Bank Pembangunan, Bank Bumiputra and so on. Another feature of the organized credit source are pawnbrokers whose credit usually takes the form of cash, goods and services, facilitating consumption, production and trade.¹ This constitutes a large market in terms of the number of participants.² The ability of these suppliers to maintain their position is largely due to the wide range of integrated services they provide to the rural economy and the limited role played by alternative sources.³ Rural dependence on their operations is substantial as a result of their being the most accessible market to

¹ Mokhzani Abdul Rahim, "Credit In A Malay Peasant Economy", Thesis submitted for the Degree of Doctor of Philosophy in the University of London, 1973, p. 5

² Ibid, p. 5

³ Ibid, p. 5

the rural economy. Hence the wide gap between the total rural need and for and the actual supply of credit at reasonable terms contributes towards the existence of these credit suppliers even though the conditions of their credit extensions are harsh.⁴ Although the government has set up rural credit institutions and co-operatives their contribution towards easing the rural credit demands is insignificant and loans "are reportedly extended only to 2 per cent of padi farmers in the Kedah and Perlis region."⁵

Moneylenders as a Source of Credit

Licensed moneylenders also play a significant role as credit mobilisers.⁶ As their lending activities are subject to the Moneylenders's Ordinance, 1951, loans obtained from them are less costly and hazardous compared to unlicensed suppliers. Their clientele is from a broad spectrum of the society; borrowers from various social strata avail themselves at the services performed by moneylenders; they are not confined to the lower income groups. This has somewhat given creditability to the institution of moneylending. They appear to be able to maintain their position in the economy despite the availability of alternative avenues of credit. This may be because of borrowers' preference to their lending methods to those of commercial banks financial institutions and government agencies. Although interest rates may be high and the inability to pay on time may involve heavy penalties, the loans are otherwise tailored

⁴ Mokhzani Abdul Rahim, op. cit., n. 1, p. 4

⁵ Ibid, p. 4

to meet the individual borrower's needs. The service provided is prompt, flexible and informal. The procedures involved are simple; applicants are not screened as they would be screened by other credit channels. What normally transpires is an introduction or recommendation of the borrower by a person known to the moneylender.⁶ Moreover loans are obtainable on an unsecured basis,⁷ giving the borrower the benefits of equity capital and exposing the lender to all the risks. For example, where the amount of loan required is small, moneylenders are usually satisfied with the production of guarantors or sureties.⁸

Accessibility to moneylenders is another factor which contributes to their popularity. In one sense they are physically accessible to everyone, as moneylenders are found everywhere; in cities as well as villages. In the other sense, they have long since been socially accepted as accessible financiers. In other words, theirs is an institution most borrowers can identify themselves with; social barriers are almost non-existent. Commercial banks and financial institutions however is a recent phenomenon. To most, they are remote and formidable.

Dependency on moneylenders has also been the result of limitations of other credit sources. Whilst the latter's lending operations

⁶ Interview with a licensed Moneylender on 10th June, 1976

⁷ Security takes the form of immovable property.

⁸ Their status in relation to the transaction is that of joint borrowers- Interview with licensed moneylender, 10th June, 1976.

stress on the purpose of loans as one of the criteria for eligibility. Moneylenders' concern is only the ability to repay. Clients of whom they have no knowledge are always investigated,⁹ in respect of their income, property and debts. As the purpose of the loan is of no consequence to moneylenders, the deversified and varied needs of borrowers are inevitable channelled to them. These needs may arise from sudden death of next of kin, loss of earning capacity through accidents or ill-health and numerous other circumstances. Moneylenders have special appeal in that urgent needs are promptly fulfilled. Hence theirs is an ideal source of credit if one disregards the advantage they take of borrowers' desperate dependency.

Criticisms of the Moneylending System

Although moneylenders are necessary to the economy, their operations have caused grievances and evoked criticisms. The general sentiment is that they are no more than social parasites, profitting from the misery of borrowers. They are normally equated with exorbitant interest rates and fraudulent practices. Loans meant to ease a borrower's predicament become in reality his doom. In addition to interest, a borrower is usually required to sign for a principal sum which is more than what he actually receives. For example, he may only receive \$700/- of the principal sum of \$1000/- which he signs for.¹⁰ The interest charged

⁹ Interview with licensed moneylender on 10th June, 1976

¹⁰ According to one moneylender, this is in fact his mode of operation; his justification being that the extra sum is necessary to cover expenses which otherwise would be borne by him, as stipulated by Section 23 of the Ordinance.

is hence based on the \$1000/-. The writer cannot furnish details of the actual operations of moneylenders as there are no well-defined arrangements and the actual workings vary among Chettiars, Sikhs and Chinese Moneylenders. The latter however are known to employ thugs to harass and intimidate clients in order to procure payments.¹¹

Despite the grievances and criticisms of the moneylending business, proceedings in respect of malpractices committed by moneylenders are seldom instituted mainly due to the lack of evidence. In some cases, the consequences of a suit are far from desirable. For example, a borrower who is a civil servant is never likely to bring an action in respect of a harsh and unconscionable loan transaction,¹² as he is in the first place, prohibited from borrowing from moneylenders.¹³

¹¹ According to one moneylender they beset the place, employment of debtors on the 1st, 15th and 30th of each month and forcibly demand payment of loans.

¹² Section 21(2), Moneylenders' Ordinance, 1951

¹³ By virtue of General Order 9(1)(d) of the Public Officers (conduct and Discipline) (General Orders, Chapter "D") Regulations, 1969, an officer of the public service is prohibited from borrowing either as principal or surety from, or placing himself under a surety from, or placing himself under a pecuniary obligation to a person who is a registered moneylender.

As failure to pay may result in bankruptcy proceedings being filed against him, the borrower usually continues paying what the Ordinance terms as "excessive interest." This is bankruptcy proceedings tantamount to "serious pecuniary ~~embarrassment~~ t"¹⁴ which could lead to disqualification of promotion and higher appointments.¹⁵ Serious pecuniary embarrassment is also regarded as necessarily impairing the efficiency of an officer and ~~making~~ him liable to disciplinary actions,¹⁶ for example, the stoppage or deferment of increment. These consequences therefore result in condonation of abuses in loan transactions.

Problems Faced By Moneylenders

The business of moneylending has its own share of problems and difficulties. It constantly faces risks of non-payment, and the incidence of bad debts is relatively higher. Though these may be recovered through civil suits, there have been instances of abscondment of debtors.¹⁸

¹⁴ General order (10)(1), Public Officers (Conduct and Discipline) (General Orders, Chapter "D") Regulations, 1969.

¹⁵ General Order 10(6) Public Officers Regulations, 1969 op. cit. n. 14

¹⁶ Ibid, General Order 10(2)

¹⁷ Interview with licensed moneylender, 22nd May, 1976

¹⁸ Ibid

Moreover litigation is a slow process and lenders may not recover their money until a lapse of a number of years. Moneylenders in general¹⁹ feel that their interests are inadequately protected under the Ordinance. In addition, they resent certain provisions, for example that which imposes the burden of costs and expenses on them.²⁰ Other cases of dissatisfaction relate to the amount of interest chargeable from the date of judgement to the date of realisation, which at present is 6 per cent. Moneylenders are fighting for this rate to be increased to 18 per cent, since loan agreement itself stipulates an interest of 18 per cent from the date of loan to payment of the whole principal sum. However the courts appear, to them, to be unsympathetic.

The above, coupled with growing competition from other sources of finance, the incidence of income tax and so on have evoked less enthusiasm in the business. Some of the Chettians for example have ceased in the pursuit of their normal avocation, the consequence of which is the partial flight of capital to India.²¹ The Chinese moneylenders however, have flourished considerably, accounting for more than 70 per cent of moneylenders.²²

¹⁹ Series of interviews

²⁰ Section 23, Moneylenders' Ordinance 1951.

²¹ Interview, op. cit., n. 17

²² Interview with Registrar of Moneylenders, 31st May, 1976. According to him, finance companies licensed as moneylenders are mostly Chinese-owned.