

Credit Solutions for Rural-Agricultural Development in Vietnam

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ABSTRACT

Rural agriculture has been playing an essential role in the Vietnamese economy. The Vietnamese Communist Party (VCP) and Government regard agricultural development and farmer life enhancement as top priorities. In reality, however, there are so many targets to accomplish in order to motivate the overall development of agriculture. Among these is credit supply that is indispensable for agricultural development. Therefore, this paper presents facts of credit supply for the agricultural sector, and its outstanding problems and limitations. Based on these findings, some suggestions will be made to increase credit supply for agricultural development in Vietnam.

Keywords: credit, agriculture, rural areas.

1. INTRODUCTION

Rural agriculture has always been a major part of Vietnam's socio-economic development. Along with economic reforms, it has achieved tremendous achievements that contribute to the overall development of the country. Not only does the agriculture guarantee national food security with a large supply of produce that meets the growing demand, but it also helps make Vietnam a leading exporter of various agricultural and aquatic products, thereby improving farmers' lives and changing the face of rural Vietnam.

Understanding the importance of rural agricultural development at the early stages of founding and developing the country, the VCP and Government have directed their great attention and made numerous changes to policies on many aspects ranging from production, distribution, planning, funding, etc. with a view to facilitating and promoting agricultural development. Moreover, the VCP states that "continuing to preserve preferential credit capital and encourage banks and other financial institutions to offer agricultural loans" is a very important solution.

Despite proper care and investment given to rural credit, there exist many restrictions deterring it from becoming a "catalyst" for agricultural development. For example, there are few credit and financial services and few participants in the rural market. Additionally, accessibility to bank services of rural enterprises and residents is very limited. As a result, credit supply for agricultural development is a very important issue that should be considered as a top priority at the present time.

2. ROLES OF CREDIT IN RURAL AGRICULTURAL DEVELOPMENT

The rural financial market assumes the basic roles of the general financial market in the economic

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development and the special role in mobilizing and reallocating capital for the sake of agricultural development. The birth of the rural financial market has created favorable conditions for rural enterprises and residents to gain access to capital flows. Loans for agricultural development are escalating and the market for rural credit is expanding over years. This helps create more employment, restore traditional handicraft villages and change the economic structure in rural areas by increasing the manufacturing and service sectors. The banking system plays a significant part in implementing the policies introduced by the VCP and Government.

Credit has partly accelerated the process of accumulating and concentrating capital, means of production, and technology for agricultural development. In all cases, bank credit has helped farmers overcome difficulties in production and improve their income. Credit also contributes to building infrastructure and facilitating the application of new technology to production. At present, rural life is still difficult and facilities are outdated. To improve this situation, more investments should be provided for rural development. Consequently, bank loans serve not only as a supplementary source of working capital, but also as medium- and long-term investments to provide modern facilities and technology. Investment projects directly serving the process of production, distribution, exchange and consumption aim at developing processing industry, agricultural mechanics, supply of various services, creation of new occupations, irrigation systems, road networks, and electricity grids. They are all zero in on rural and agricultural development.

Credit has promoted the development of traditional handicraft villages, created new occupations, and provided employment for rural workers. Bank loans to infrastructure building projects have supported the establishment and development of handicraft and light industries in rural areas. The birth of plants processing farm products and traditional handicraft villages has attracted laborers from agriculture to production of raw materials, processing, and distribution network. There are now over 4,000 plants for processing agricultural products in rural areas, with over 1,000 of them being medium and large-sized plants. Many of them have applied modern technology and production lines. Additionally, there are over one million households working in over 2,500 handicraft villages, making a labor force of 11 million workers. In conclusion, credit has directly and indirectly affected the development of traditional handicraft villages and new occupations.

Rural credit has provided access to bank loans for tens of millions of rural residents, reducing rural usury. In the past, credit policies in rural areas used to be neglected, so loans for farmers were provided mainly through informal financial markets. Before 1990 when there was no policy on farmer loans, farmers had to borrow money from rural usury agents at high interest rates of up to 20% per month. It is the expansion of farmer loans that reduce usury and labor exploitation. As a result, farmers can fully enjoy the fruits of their labor.

To sum up, credit has a significant role in socioeconomic development in rural areas. To promote its role, it should be used as a capable tool for promoting agricultural development.

2. SUPPLY OF CREDIT IN RURAL AREAS

a. Total loan and outstanding debts:

After 20 years of economic reforms, credit policies for agriculture initiated the credit flow into rural areas. In late 1998, outstanding debts in agriculture were only VND34,000 billion. This figure for the banking system increased nine times to VND292,919 billion in 2009 (making up 15.55% of the total outstanding debt of the whole economy). This shows a continuous rise in outstanding debts in rural sector over years (Đào Minh Tú, 2010).

Table 1: Rural - agricultural loans

No.	Time	Outstanding debts (VND billion)	Year-on-year growth of outstanding debt (%)	Ratio of outstanding debts to total loan (%)	Growth rate of outstanding debt (%)
1	1999	36,103	6.19	25.93	13.21
2	2000	43,752	21.19	24.61	27.69
3	2001	57,892	32.31	26.45	23.11
4	2002	66,067	20.10	23.13	30.51
5	2003	83,742	26.75	22.91	27.96
6	2004	111,683	33.37	24.2	26.24
7	2005	142,610	20.02	24.41	20.54
8	2006	157,991	17.82	22.76	24.76
9	2007	215,023	28.65	20.52	51.00
10	2008	246,593	14.68	18.30	28.62
11	2009	292,919	18.79	15.55	39.76
12	Sep. 2010	350,315	16.54	16.81	20.06

Source: Đào Minh Tú (2010)

Vietnam Bank for Agriculture and Rural Development (Agribank) plays a major role in rural and agricultural development. It was founded in 1990 and currently has the widest network of branches in rural Vietnam. Until late 2010, it had three representative offices, eight affiliates, one main exchange floor, 158 first and second-grade branches, 2,145 third-grade branches and transaction offices, and over 1,700 ATMs. Agribank's deposit growth stands at 23.5% per annum. As a driving force in the rural financial market, it invested in 2010 over VND40,000 billion in rural-agricultural development, especially in the purchases of grains, sugarcane, sugar, *tra* catfish, *ba sa* catfish, and coffee in line with a temporary storage program by the government. Its loan supplied to rural-agricultural sector account for 70% of its total loan.

However, deposit from rural areas with Agribank equals only 85% of rural demand for loan. Despite nationwide operation, most of its loans are low-value and concentrated in rural areas with rising outstanding debts year after year. Agribank's credit growth in the 2005-2009 period is quite impressive. This indicates efforts to expand its lending policies in rural areas.

Additionally, Vietnam Bank for Social Policy (VBSP) is a pioneer in the national goal for poverty alleviation. Formerly known as a bank serving poor people, VBSP was founded in 2003 to provide credit for poor families and other preferentially-treated entities in an attempt to reduce poverty. Up to late 2010, it had 64 branches of provincial level, nearly 600 transaction offices of district level and over 8,000 mobile transaction points in communes. Additionally, it managed over 200,000 savings and credit groups and its outstanding loans for poor families amounted to VND27,463.25 billion. VBSP's rising capital mainly comes from 2% deposits from credit unions, deposits in and loans from other banking institutions, customer deposits and financial support for authorized investment. Of these, deposits in and loans from other banking institutions have the highest share and growth rate.

Besides Agribank and VBSP, the Vietnam Association of People's Credit Funds (VAPCF) is also a large credit union in the rural financial market. It has quickly become popular with farmers due to simple and farmer-friendly lending procedures, diversified credit products, and enclosed deposit insurance. Besides efforts to exploit and deploy its resources, VAPCF has well accomplished its role in bridging and implementing more than 20 projects on technical assistance and international finance. Like VBSP, however, its rural deposit can meet only 81% of the credit demand in these areas. This is a great challenge because loans from outside local Credit Fund are usually scarce and its operation is limited to certain ward or commune, making its liquidity worse.

Moreover, some others banks also set their targets at rural areas, for example TrustBank, Sacombank, Kiên Long Bank, and Liên Việt Bank, etc. However, their rural-agricultural loans account for small shares of their total loan. This is because loans for agriculture suffer higher costs and risks than for other sectors.

b. Risks of rural credit:

Despite big achievements in credit supply in rural areas, this source can barely meet the growing demand for loan. In fact, the Mekong Delta alone sees 80% of farmers get loans from the "black credit" market. According to Nguyễn Quốc Nghi (2010, 2011), Lê Khương Ninh (2011) and Trương Đông Lộc (2008), rural Vietnam is severely thirsty for capital. It is apparent that the rural- agricultural sector is a potential market, but banks are reluctant to provide it with more loans mainly because of rather high risks.

In reality, farmers tend to get small loans, which raises bank overheads. At Agribank alone, despite nationwide operation, its loan values are low with 40% of its customers borrowing less than VND5 million and 35% borrowing VND5-10 million. Additionally, agricultural production is often threatened by natural disasters and epidemics, therefore it is always a risky business. Vietnam, as a tropical country, has favorable conditions for insects and epidemics and is flood-stricken every year because of its lowlands, which damages agricultural production.

Additionally, prices of principal agricultural products drop continuously due to slow investment process, delayed production, reduced expenditure from consumers, and changeable policies. Some farmers have to get loans from banks and may become default if risks occur. Aside from objective causes, there are other causes from the poor awareness and unreasonable loan use of borrowers,

entailing ineffective business performances. As a result, they default on their loans or take long time to pay them off. Even worse, many of them refused to pay their debts.

Therefore, many banks are lukewarm about credit supply in rural areas. An indication of this is the very modest share of rural-agricultural loans given by dominant rural banks. Specifically, the outstanding debts for rural-agricultural sector of TrustBank make up only 12% of the total loan. In the past few years, Sacombank expanded its network to remote areas across the country but rural-agricultural loans only equal 12% of its total loan. Even at a big bank like Vietinbank, this figure stands below 40%. The same number is also recorded at Kiên Long Bank, whose target is the rural market.

Table 2: Agribank outstanding loan and bad debt rates in 2005-2010

Year	2005	2006	2007	2008	2009	2010
Total loan (VND billion)	161,106	221,661	246,118	294,697	354,112	414,755
Bad debt rate (%)	2.3	1.9	2.5	2.7	2.6	3.7

Source: Agribank annual reports

The bad debt rates of rural banks, especially Agribank, are very high. This affects their decision to open branches in rural areas. As a result, many banks are uninterested in investing in this sector, indicated by the modest share of loans given by rural dominant banks.

4. SHORTCOMINGS IN CREDIT SUPPLY IN RURAL VIETNAM

Rural-agricultural credit has over the past contributed to full use and exploitation of land, labor force, and natural resources. It has also played a considerable role in rural-agricultural development. However, there remain some unsolved problems and restrictions.

Despite rises in total loan, mobilized capital, the number of transaction points, and transaction volumes, products and services from rural banks are unsatisfactory. They are mainly traditional credit services such as giving loans, taking deposits, transferring money, and making payment without products tailored for rural areas. Payment services, agricultural insurance, agricultural credit insurance, and remittances are limited. Banking products have no supportive service enclosed such as training, instruction and counseling. Agribank has the widest variety of products (194 items), but its rural products are centered on deposit and lending only.

Human resources are insufficient in terms of quantity and quality. The human resources of rural financial intermediaries and even Agribank lack professional skills related to rural finance. Moreover, they have poor risk management capability in the view of risk awareness, information management, and standardization of banking services (especially for micro-financial agencies). A portion of credit staff shows ignorance of agricultural production, economic and technical norms, and policies on agricultural extension. This makes their lending projects unsuitable and lending proposals (loan volume and maturity, etc.) lack objectivity and accuracy (Nguyễn & Tô, 2010).

Accessibility to banking services of rural enterprises and residents is still restricted. Some banks have no rural transaction offices and make little investment in small and medium enterprises as well as farming and household businesses. Furthermore, their administrative reforms are progressing

slowly, and they also do not facilitate farmer loans. These affect the overall efficiency of the banking sector and the expansion of rural-agricultural investment.

Ability to ensure local sources of working capital of rural banking institutions is very weak. Deposits from local residents can satisfy only 30%-40% of the total loan supplied to local customers while the rest are taken from urban branches. This makes the lending rates in rural areas higher than those in urban ones.

Financial abilities and sustainability of rural financial institutions show numerous inadequacies. Except for Agribank and VBSP, on the whole, most of the institutions operating on the rural financial market have limited financial resources. The sustainability of micro-financial institutions is uncertain and their profitability is low.

Although the capital of financial intermediaries enjoys a continual rise, its growth fails to catch up with that of credit or fully meet the capital demand in the rural-agricultural sector. Investments are dispersed and disproportionate to the economic growth. Investments per unit of plants, animal or household are small and do not create a tight connection between production, processing and consumption. Outstanding debts of cooperatives are low.

Although the procedures for supplying credit have been simplified, they are unsuitable for farmers, especially those related to land mortgages. Many of them are a big deterrent to ill-educated farmers and therefore lead to social problems of informal lending brokers, usury, etc. as well as tardiness in providing financial support for their business operation.

5. SUGGESTIONS ABOUT CREDIT SUPPLY FOR RURAL-AGRICULTURAL DEVELOPMENT

a. For the government:

The government should encourage research and implement policies for attraction and expansion of the scope of micro-financial institutions, offer more loans to poor families and create a link between formal and informal credits. Financial resources needed for rural-agricultural development will be very large while domestic resources are limited. Therefore, control over capital should be relaxed and restrictions on investments from outside the rural-agricultural sector should be removed. Furthermore, due to the recent WTO accession, Vietnam should open its door to foreign financial institutions as a fulfillment of the commitment to international integration.

By changing interest rate controls and supporting policies, the government can make the rural financial market more transparent and equitable. The government should cut subsidies for interest payments, adopt a rational policy on interest rates and let the rural financial institutions operate according to market mechanism. The phasing out of preferential interest rates can help increase deposits, improve business performance, and create a level playing field for all financial intermediaries participating in the rural financial market. For example, all banking institutions operating in rural markets can be allowed to write off bad debts or stop collecting interests on doubtful debts as VBSP and Agribank do (Hà Thị Thiệu Dao, 2010).

Additionally, it is of necessity to develop the market for agricultural materials, boost mechanization and apply technological advances to agricultural production. This helps banks expand their operation and increase investment for rural agricultural development.

Measures should be taken to develop and upgrade infrastructure and communication system, ensure the smooth operation of the financial market, fulfill requirements about information for an effective management and administration of the financial market.

Finally, the government ought to improve the legal system on the management and supervision of the financial market, guarantee the sound and effective operation of this market, impose strict punishments to keep its operation under law, protect interests of all participants in the market and provide them with equal access to credit.

b. For banking institutions:

Depending on total loan supplied annually, banking institutions should proactively build plans to attract deposits and other sources of capital, especially sources used for rural-agricultural development based on their characteristics and capabilities. They should also give training courses to their staff, and make more investments in facilities and technology to better serve the rural-agricultural development. In particular, priority should be given to investments in zones of commercial farming as planned by the government, aquatic production zones and centralized animal farms. Moreover, traffic networks and tourist destinations should be upgraded.

Lending modes should be flexible, such as lending investment projects, lending based on credit limits, or co-financing, etc. in order to help borrowers proactively employ their loans for agricultural production, simplify lending procedures, and save intermediate costs of taking bank loans. Moreover, forms of financial credit should be diversified for rural-agricultural sectors.

Banks should advise borrowers on closed production process (production – processing – consumption) prior to offering loans. Every stage in the process should be smoothly carried out based on business projects and investment plans,. This is a win-win situation for banks and borrowers in the processing of giving loans and collecting repayment when the products are sold (Đào Minh Tú, 2010).

Professional expertise of the staff should be enhanced through training in rural finance, agricultural production and the government policies on rural development. In addition, lending procedures should be simplified (simple procedures and quick receipt of loans) in order to provide farmers with easy access to loans at minimum costs. The use of loans should also be supervised with the help of local authorities and civic organizations.

6. CONCLUSION

In sum, rural-agricultural development is considered a top concern for the VCP and Government. It is also an important issue in the strategic targets of the banking system during the industrialization and modernization process. Development of rural credit has reaped encouraging achievements. For example, total loan and the network of bank branches in rural areas are on the rise.

These achievements are a precondition for the banking system to strengthen future investment in rural areas. However, there remain some drawbacks such as the poor diversity of rural banking services, limited accessibility to farmer loans, and few financial institutions operating in rural areas.

Thus, for development of a stable financial market, reforms should be carried out in every single segment of the sector. Each segment should play well its role and reflect social visions and benefits that it is responsible for. Completely changing ideology and action and taking timely and consistent measures on credit policies for rural-agricultural development in the future can help alleviate poverty, promote the industrialization and modernization of the agriculture, guarantee national food security, bring prosperity to the agricultural economy, improve farmers' living standard, and change the face of rural Vietnam in the future■

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