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ESO# 1120

RURAL DEPOSIT MOBILIZATION EXPERIENCES
AND ISSUES IN SELECTED ASIAN COUNTRIES

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Paper prepared for the APRACA
Workshop on Rural Savings Mobilization
October 3-5, 1984
Manila, Philippines

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INTRODUCTION

Resource mobilization issues are becoming increasingly important in many developing nations. Several countries are facing problems in continuing to obtain large amounts of foreign resources with the desired term and interest conditions. Commercial lending sources have become frightened by huge amounts of foreign indebtedness. International donor agencies are less inclined to provide large amounts in grants and loans to some countries, partly because their total real resources are no longer growing at a rapid rate, they are also concerned about international indebtedness, concern is mounting over past inefficiencies in the use of such resources, and many analysts argue that such funds permit decision-makers to postpone needed economic reforms. Further, many financial institutions that have been heavy recipients of these resources have failed to attain the levels of institutional efficiency and viability expected when the grants and loans were provided.

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Although the need for domestic resource mobilization is recognized, there is less consensus about the ability to mobilize financial resources in the rural sector. This sector must be the primary source of savings in most low income countries because of its importance to GNP, exports and employment. Many policymakers believe, however, that voluntary deposit mobilization will not succeed in rural areas because of the low income of rural people, their preference for non-financial savings, and their skeptical attitudes toward formal banking and savings institutions.

The purpose of this paper is to present some information about rural deposit mobilization experiences and issues in selected Asian countries. It reports on a limited analysis we were able to conduct quickly with data easily available. Your assistance will be appreciated in evaluating our interpretation of this analysis and in identifying data and experiences that will improve a subsequent, more comprehensive version of this paper. The central argument of the paper is that most financial institutions have not vigorously attempted to mobilize rural deposits because they have become dependent on "cheaper" sources of resources. Large amounts of rural deposits have been mobilized when serious attempts have been made, but systematic disincentives must be removed in many countries before the full potential for rural deposit mobilization is realized. The countries highlighted in this analysis are Bangladesh, Indonesia, the Philippines and Thailand with selected information provided for other countries.

DEPOSIT MOBILIZATION OF MAJOR FINANCIAL INSTITUTIONS

What are the sources of funds of major financial institutions in these countries, what have been the trends in these sources over time, and how important are rural deposits? These issues are addressed in this section.

Bangladesh, Indonesia, the Philippines and Thailand have a mixed pattern of private deposit mobilization in their banking systems. Banks obtain funds in a variety of ways from governments, households and domestic and foreign firms. Table 1 reports the share of private deposits in each country relative to total bank liabilities. Although there have been rather significant year-to-year variations, the banking system in these countries report private deposits representing 50-75 percent of total liabilities. There appears to be a downward trend in Bangladesh and the Philippines since 1978, and since 1980 in Indonesia. In Thailand the share of deposits fell from 1970 to 1978, then rose to their highest level of 78 percent in 1982.

The magnitude of rural deposits is of special interest in this paper, but data were located only for Bangladesh and Thailand. Table 2 shows trends in these two countries in rural deposits as a percentage of total deposits. Bangladesh data report rural and urban deposits without defining how this classification is achieved. Rural deposits in Thailand are defined as those mobilized outside the Bangkok metropolitan area. The Bangladesh data show a fairly consistent upward trend in rural deposits from 9.2 percent of total deposits in 1976 to 15.4

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Table 1Private Deposit Mobilization as a
Percent of Total Bank Liabilities
1970-1982

| Year | Country | | | |
|------|--------------------------|-------------------------|---------------------------|------------------------|
| | Bangladesh ^{a/} | Indonesia ^{b/} | Philippines ^{c/} | Thailand ^{d/} |
| | | | | |
| | | (Percent) | | |
| 1970 | NA | 40.7 | 60.1 | 75.3 |
| 1975 | 74.3 | 56.3 | 56.1 | 72.1 |
| 1978 | 77.9 | 56.1 | 58.5 | 69.6 |
| 1980 | 72.2 | 61.1 | 51.3 | 74.5 |
| 1981 | 71.2 | 59.0 | 51.9 | 74.3 |
| 1982 | 67.3 | 56.1 | 51.7 | 78.5 |

a/ Includes demand and time deposits in commercial banks, nationalized banks, foreign banks, and agricultural and industrial development banks.

b/ Includes demand, time and saving deposits in commercial banks, foreign exchange banks, local development banks, savings banks and branches of foreign banks. Data also cover import deposits as well as foreign currency.

c/ Includes demand, savings and time deposits, import deposits, deposit substitutes, prepayments of letters of credit and foreign currency deposits in commercial, development, savings and rural banks.

c/ Includes demand, savings and time deposits, import deposits, deposit substitutes, prepayments of letters of credit and foreign currency deposits in commercial, development, savings and rural banks.

d/ Includes demand, savings and time deposits as well as deposit substitutes in commercial, development and savings banks.

Source: IMF, International Financial Statistics Yearbook, 1979.

IMF, International Financial Statistics, September 1983.

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Table 2

Rural Deposits as a Percent of Total Deposits
1976-1982

| Year | Country | | | |
|------|--------------------------|-----------|-------------|------------------------|
| | Bangladesh ^{a/} | Indonesia | Philippines | Thailand ^{b/} |
| | (Percent) | | | |
| 1976 | 9.2 | NA | NA | 36.6 |
| 1977 | 10.7 | NA | NA | 36.4 |
| 1978 | 13.3 | NA | NA | 36.5 |
| 1979 | 15.4 | NA | NA | 36.6 |
| 1980 | 14.4 | NA | NA | 38.2 |
| 1981 | 16.0 | NA | NA | 39.0 |
| 1982 | 15.4 | NA | NA | 39.5 |

a/ Data as of June 30 for each year for all banks.

b/ Data as of end of December for each year. Rural deposits are defined as deposits in commercial banks located outside the Bangkok metropolitan area.

Source : Bangladesh Bank Bulletin, March 1983.

Bank of Thailand, Quarterly Bulletin, December 1983

percent in 1979. The share fluctuated between 14.4 and 16.0 percent after that date. The share of rural deposits to total deposits in Thailand was about 36.5 percent from 1976 to 1979, then slowly rose to a peak of 39.5 percent in 1982. The data in Tables 1 and 2 can be interpreted in two ways. One interpretation is that deposits, and especially rural deposits, have not become significantly more important in recent years as a source of bank liabilities. The second interpretation is that, since total deposits have been growing, private deposits and rural deposits have also grown significantly in nominal terms in order for their deposit share to remain roughly unchanged. In Bangladesh, for example, rural deposits grew from 10,600 lakh Taka in June 1976 to almost 60,000 lakh Taka by June 1982. While total deposits grew about 3-1/2 times in this period, rural deposits experienced a six-fold increase. In Thailand, both rural and urban deposits roughly tripled from 1976 to 1982. While private deposits and rural deposits have not been an exceptionally dynamic source of bank liabilities, their growth clearly has not been a drag on overall resource mobilization for the financial systems of these countries.

Another way to analyze rural deposit trends is to review the performance of financial institutions that are oriented towards the rural sector. These institutions may have advantages in rural deposit mobilization because of their objectives, their location in rural areas and their operational policies. For this analysis, data were obtained for the Bangladesh Krishi Bank

(BKB), the rural banking system in the Philippines, and the Bank for Agriculture and Agricultural Cooperatives (BAAC) in Thailand. They represent large sources of formal agricultural credit in their respective countries. The BKB provides about 60 percent of total rural credit in Bangladesh. The rural banks in the Philippines provide about 14 percent of the rural credit in that country, and BAAC provides about 35 percent of Thailand's rural credit. Tables 3, 4 and 5 report trends in their sources of funds for 1978 to 1982 with the exception of missing data for the Philippines in 1981 and 1982.

The experience in mobilizing deposits is fairly similar in all three cases. Deposits are overshadowed by other sources of funds and governments, through central banks, provide the largest single source of funds to these institutions. The Bangladesh Krishi Bank appears to be increasing deposits faster than other sources of funds as the deposit share rose from approximately 23 percent in 1978 to over 29 percent in 1982. The rural banks in the Philippines, however, actually reduced their deposit share from 34.5 to 32.5 percent from 1978 to 1980, while the share of Central Bank credits rose by 2.4 percent. Deposits in BAAC represented about 16 percent of total funds in 1978. This percentage fell to 12 percent by 1980, and recovered to 15 percent in 1982. Government assistance to BAAC is important in two ways: credit from the Bank of Thailand and rules which require commercial banks to deposit funds with BAAC if they do not meet their agricultural lending targets. These two sources represent 50 to 60 percent of total funds for BAAC.

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Table 3

Sources of Funds of the Bangladesh Krishi Bank
1978-1982

| Year | Source | | | | |
|-----------|----------|-----------------------------------|---|--------------------|----------------------|
| | Deposits | Credit from Bangladesh Bank | Foreign Liabilities and Grants | Capital Account | Others ^{a/} |
| (Percent) | | | | | |
| 1978 | 23.4 | 39.6 | 5.8 | 19.8 | 11.3 |
| 1979 | 24.7 | 44.4 | 5.3 | 15.4 | 10.2 |
| 1980 | 25.4 | 51.0 | 5.1 | 10.7 | 7.7 |
| 1981 | 27.9 | 51.3 | 4.0 | 8.3 | 8.4 |
| 1982 | 29.3 | 49.8 | 4.1 | 6.3 | 10.6 |

a/ Includes current liabilities and a loan from the government

Source: Asian Development Bank, "Appraisal of the Bangladesh Bank", November 1983.

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Table 4
Sources of Funds of Rural Banks, Philippines
1978-1980

| Year | Source | | | |
|------|------------------------|-----------------------------|--------------------|----------------------|
| | Deposits ^{a/} | Credit from Central Bank | Capital Account | Others ^{b/} |
| | | (Percent) | | |
| 1978 | 34.5 | 47.9 | 13.4 | 4.3 |
| 1979 | 34.2 | 49.1 | 12.4 | 4.3 |
| 1980 | 32.5 | 50.3 | 12.2 | 4.9 |
| 1981 | NA | NA | NA | NA |
| 1982 | NA | NA | NA | NA |

a/ May include "seed funds" provided by government.

b/ Consists of liabilities to domestic sources.

Source: M. Agabin, "Philippines" Symposium on Farm Credit,
December 1982

Table 5

Sources of Funds of the Bank of Agriculture
and Agricultural Cooperatives, Thailand
1978-1982

| Year | Deposits ^{a/} | Source | | | | |
|-----------|------------------------|---------------------------------------|---------------------------------------|-----------------------------|---------------------|----------------------|
| | | Credit from Bank of Thailand | Credit from Commercial Banks | Foreign Lia- bilities | Capital Accounts | Others ^{b/} |
| (Percent) | | | | | | |
| 1978 | 15.9 | 15.9 | 43.9 | 3.7 | 14.4 | 6.2 |
| 1979 | 14.1 | 17.4 | 44.0 | 6.4 | 14.1 | 4.1 |
| 1980 | 12.0 | 26.0 | 40.4 | 6.3 | 11.6 | 3.8 |
| 1981 | 14.7 | 18.1 | 40.4 | 9.1 | 11.9 | 5.8 |
| 1982 | 15.0 | 16.8 | 40.2 | 11.1 | 11.6 | 5.2 |

^{a/} Deposits from business and the household sector

^{b/} Borrowings from the government and other liabilities

Source: Bank of Thailand, Quarterly Bulletin, December 1983.

It is clear from this analysis that rural credit sources in these three countries are clearly not self-financed by borrower deposits. The governments of these countries played an important role in creating these institutions and continue to provide them with the bulk of their funds. Any expansion in deposits experienced in these cases has been largely or wholly offset by the growth in funds from other sources so that the deposit share has been fairly constant from 1978 to 1982. The sources of deposits are not known for these institutions, but it is likely that they come from a combination of rural and urban sources.

EXAMPLES OF SUCCESSFUL RURAL DEPOSIT MOBILIZATION

There are examples of rural deposit mobilization activities in Asia that appear more successful than the general experience of the financial institutions summarized above. This section discusses a few examples. Since the literature search was not comprehensive, there are undoubtedly other experiences of equal merit to be included in this summary.

Credit Unions¹

The credit union movement in Asia is only 10-15 years old but has already achieved considerable success. With the exception of Korea, most credit unions are oriented towards a low-income rural clientele, and they are often located where other financial institutions are less accessible. Unlike most rural

¹ We are indebted to Paul Hebert, World Council of Credit Unions, for information on the Asian Credit Union experience.

credit institutions, their basic appeal is to provide a safe place for savings, not to push cheap credit.

Table 6 shows that Asian credit unions reported almost \$750 million in total deposits in 1983-84. This is a substantial amount of money mobilized from low-income people in the short history of the movement. Furthermore, credit unions usually do not enjoy major government incentives and subsidies received by other financial institutions. In fact, even the legal environment is uncertain for credit unions in some countries.

Korea is by far the exceptional case. Recently Korean credit unions reported over \$1 billion in total deposits. The Korean credit union movement is somewhat older than other countries, has enjoyed energetic leadership and a large part of the membership is composed of low-to middle-income urban workers who have a check-off system to automatically deduct savings contributions from their incomes.

By comparison, the credit union movement in Latin America is older and better established. However, deposits in 1983-84 totaled \$358 million compared to \$750 million for Asian credit unions. In Peru, credit unions began to falter in the mid-1970s, largely as a result of a dramatic upsurge of inflation and a failure to adjust their interest rates (Vogel). In mid-1979, USAID in Peru initiated a two-year project with the Banco Nacional para los Cooperativas (BANCOOP) to expand deposit mobilization in rural areas. BANCOOP receives deposits and makes loans. It is a second-level cooperative and deals with members

Table 6
 Finanancial Data on Credit Unions in Asia^{a/}
 1983-84^{b/}

| Country | Number | | Dollar Volume | | | |
|------------------|---------------|-----------|---------------|---------------|--------------|---------------|
| | Credit Unions | Members | Deposits | Loans | Reserves | Assets |
| Bangladesh | 11 | 13,301 | 360,221 | 337,450 | 31,904 | 406,212 |
| Hong Kong | 52 | 19,630 | 3,228,987 | 2,984,284 | 156,163 | 3,749,131 |
| Indonesia | 1,095 | 124,954 | 4,334,481 | 4,519,447 | 106,528 | 5,193,868 |
| Japan | 64 | 9,103 | 1,480,127 | 1,298,654 | 159,799 | 1,639,927 |
| Korea | 1,433 | 1,015,776 | 665,744,040 | 598,713,905 | 13,712,617 | 738,964,868 |
| Malaysia | 70 | 5,000 | 550,000 | 480,000 | 30,000 | 655,000 |
| Papua-New Guinea | 33 | 77,014 | 34,720,963 | 33,575,068 | 1,085,422 | 45,995,790 |
| Philippines | 44 | 38,000 | 4,320,000 | 4,780,000 | 291,000 | 5,965,000 |
| Taiwan | 281 | 54,490 | 32,855,785 | 32,421,553 | 2,181,687 | 38,371,530 |
| Thailand | 301 | 27,344 | 2,239,727 | 2,322,381 | 162,185 | 3,030,366 |
| Total | 3,384 | 1,384,612 | \$749,834,331 | \$681,432,742 | \$17,917,305 | \$843,971,692 |

a/ Credit unions that are members of the Asian Confederation of Credit Unions (ACCU).

b/ Reporting dates varied between end of 1983 and sometime in early 1984.

Source: The World Council of Credit Unions Statistical Report and Directory, Madison, Wisconsin, 1984, p. 5.

and non-members of cooperatives, and the general public. BANCOOP began deposit mobilization efforts in two target areas in late 1979. By mid-1980 each of the target offices had already mobilized far more than their mid-1981 goal of \$150,000. Vogel attributes this success to the payment of higher interest rates on time and savings deposits, quality of service for depositors, effective publicity and attractive prizes given to savers.

Similar positive deposit mobilization results were obtained in a USAID project in Honduras designed to assist five cooperatives of the Association of Savings and Credit Cooperatives (FACACH). This project provided for a restructuring of deposit interest rates and improvements in deposit services. An interest rate reform was implemented in October, 1982, and by June of the following year deposits in the five cooperatives had increased by 150 percent (Poyo).

Agricultural Cooperatives in Korea

The deposit mobilization activities of Korean agricultural cooperatives have also been very successful (Lee, Kim and Adams). In 1975, there were more than 2 million farmer members in over 1,500 primary multipurpose cooperatives and 141 special-purpose cooperatives. More than 80 percent of the farm households were members of primary cooperatives. This cooperative system performed a wide range of services. The provision of financial services through the cooperative system was one way the government implemented its rural development strategy. In the early 1960's, funds from the government and Bank of Korea represented

60-75 percent of total loanable funds. From 1961 to 1975, the real value of loanable funds in the system increased fourfold. Expanded private savings deposits provided a large part of these additional loanable funds. By 1970, private deposits had risen from 20 percent to 50 percent of total funds. The proportion of total savings deposits in the country held by agricultural cooperatives increased from 5 percent in 1963 to 16 percent in 1966. Likewise during the same period, the proportion of financial deposits in agricultural cooperatives increased from 14 percent to 17 percent of total financial deposits in the country. These percentages began to fall after 1966 because of the very rapid growth in non-agricultural economic activities.

DETERMINANTS OF SAVINGS BEHAVIOR

For rural deposit mobilization strategies to be successful, they must be built on an understanding of the determinants of savings behavior of households. The subject of savings behavior has been frequently studied and a recent paper by Lanyi and Saracoglu summarizes the key issues. Although individual studies have arrived at different conclusions in the past, a convergence of results now seems to be emerging.

Interest Rates

A fundamental question concerns the influence exerted by interest rates on saving. The alternative possibilities are summarized by Lanyi and Saracoglu (page 6): "While an increase in interest rate may stimulate savings by making future consumption less expensive relative to current consumption (substitution

effect), it may also tend to reduce saving by lowering the amount of present saving necessary to buy a given amount of future consumption (income effect)." They conclude that the available evidence, largely based on Asian and Latin America experience, suggests that the substitution effect is more important than the income effect in developing countries, although not overwhelmingly so.

The form in which savings are held is more important for our discussion of deposit mobilization than the amount of savings. In countries where interest rates have been depressed over long periods, where financial institutions and instruments are underdeveloped and fragmented, and where there is great economic and political uncertainty, the public has been encouraged to hold a large proportion of its savings in the form of real estate, consumer durables, precious metals and foreign currency. In these situations, rural savers concentrate their wealth in land, livestock, crop inventories and jewelry. When interest rate repression is an important determinant in this pattern of savings, a substantial increase in interest rates (at least large enough to insure positive real deposit rates of interest) can be expected to have a positive effect on financial savings.

Lanyi and Saracoglu conclude that the evidence from a number of countries shows that the real return on deposits has a significant effect on volume of financial savings. Malaysia and Korea were the two Asian countries included in their analysis and are

identified as examples where a steady policy of positive inflation-adjusted interest rates can lead to steady growth in financial intermediation.

In his comprehensive review of credit and interest rate policies of Asian countries, Fry concluded that most countries in the past few years have pursued policies which retard growth of the financial sector and of the economy. Nominal institutional interest rates are usually set by administrative fiat leading to inflexible and frequently negative real deposit rates. In addition, all countries included in his study (Burma, India, Indonesia, Korea, Malaysia, Nepal, Pakistan, the Philippines, Singapore, Sri Lanka, Taiwan and Thailand) pursued some form of selective credit policy or credit planning. This involves ceilings and/or floors for credit flows to priority sectors or borrowers, and differentiated interest rates set for size, group, sector or location of borrower, or for source of funds. In addition, government resources at subsidized rates are available for rediscounting loans to priority borrowers made by commercial lenders or specialized institutions. This combination of controls frequently leads to preferential interest rates for farm loans, low rediscount rates for farm lending, and low deposit rates for savings. Negative real rates often result for loans and deposits.

This problem is demonstrated clearly in three of the four countries analyzed by the data for key interest rates reported in

Table 7. Only the Philippines has a structure of partially floating interest rates which permits market forces to influence deposit rates. The other three countries administratively fix almost all lending, rediscount and deposit rates. Two key issues are noted in the data. First, some deposit rates are set at levels equal to or even above some agricultural lending rates. These deposit rates, of course, underestimate the effective cost of deposits because they do not include the effect of reserve requirements and administrative costs. Therefore, in many cases, the effective cost of deposits is considerably higher than agricultural loan rates. Second, rediscount rates are less than deposit rates paid on savings and time deposits. The spread between rediscount rates and agricultural lending rates are not large in all cases, but they are clearly larger than those for lending mobilized deposits.

This interest rate structure helps explain the performance of deposit mobilization in these four countries. Financial institutions, and especially those required or encouraged to make agricultural loans, cannot afford to mobilize large amounts of private deposits. They must rely heavily on subsidized sources of funds, and rediscount funds are frequently the cheapest and most reliable source. If commercial lenders mobilize deposits in rural areas, it is logical that they will flow to urban areas where lending rates are higher. Savers are discouraged from saving through financial instruments by low and negative real rates of return. Interest rate reform is a necessary condition

Table 7

Selected Loan, Rediscount and Deposit Rates

(Nominal Interest Rates Per Annum)

| Rate | Country | | | |
|--|---------------------------------------|-------------------------|--------------------------------|------------------------|
| | Bangladesh ^{a/} | Indonesia ^{b/} | Philippines ^{c/} | Thailand ^{d/} |
| Lending Rates for Major Agricultural Programs: | | | | |
| Short-term credit | 12 & 17.5 ^{e/} | 9 - 13.5 | 12, 16 & 18 ^{l/} | 7 - 14 ^{n/} |
| Medium/Long-term credit | 13 - 14 ^{e/} | 10.5 | floating | 7 - 16 ^{n/} |
| Rediscount Rates for Agriculture | 6 | 3 - 4 | 3, 8, & floating ^{m/} | 5 |
| Deposit Rates | | | | |
| Demand | 4.5 ^{f/} - 8.5 ^{g/} | 3 - 9 ^{i/} | floating | 0.5 - 9 ^{o/} |
| Savings | 10 | 15 ^{j/} | floating | 9 |
| Time (12 months and over) | 14 ^{h/} | 9 & 18 ^{k/} | floating | 13 |

- ^{a/} All rates effective from October 1980 for all scheduled Banks. Recent changes in loan and rediscount rates for agriculture not included.
- ^{b/} Data as of August 27, 1982,
- ^{c/} Information as of 1981 after reform of the interest rate structure.
- ^{d/} All information as of 1982.
- ^{e/} Higher rate refers to loans from Bangladesh Rural Development Bank--Thana Central Cooperative Associations.
- ^{f/} Call deposits and special notice accounts withdrawable at notice.
- ^{g/} Savings accounts with checking facilities.
- ^{h/} Less than 24 months
- ^{i/} Up to Rp. 1 million; 3% for balance over Rp.1 million but less than Rp. 50 million, 6% for amount over Rp. 50 million.
- ^{j/} For the first Rp. 200,000 deposited; 6% for balance over this amount.
- ^{k/} Lower rate is for state banks; higher rate for private banks with no ceilings for more than one year time deposits.

Table 7 (continued)

- l/ For supervised, non-supervised (secured) and non-supervised (unsecured) loans, respectively.
- m/ Fixed rates for short-term credit with lower rate for supervised credit and special credit programs; higher rate for non-supervised agricultural and other priority programs.
Floating rate for long-term credit and equals lending rate minus 6%.
- n/ Lending rates mainly for BAAC loans to individuals and farmer associations.
- o/ Rates paid by Government Savings Bank.

Sources: Bangladesh Bank Bulletin, March 1983.
Bangladesh Bank, Annual Report 1982-83.
Bank Indonesia, Report for the Financial Year 1982-1983.
Bank of Thailand, Quarterly Bulletin, December 1983.
F. Villegas and M. Cristostomo, "Agricultural Credit Policies in the Asian Countries," Singapore, November 1981.
C. Gonzalez-Vega, "Indonesia: Financial Services for the Rural Poor," Resources Management International, February 1982.
APRACA, Agricultural Credit Policies and Programmes in Asia: Country Profiles, 1982 and Strategy for Recovery of Loans, APRACA No. 9, 1983.

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for increasing incentives for savers to demand financial instruments and for increasing incentives for financial institutions to supply attractive financial instruments to savers.

Access to Banking Facilities

Although the rural population in low-income countries is responsive to deposit rate changes, there may be little scope for deposit mobilization if there is limited access to financial institutions. It appears that the four countries emphasized in this paper recognize this problem and have pursued policies to expand the network of rural banks and/or bank branches. The data in Table 8 report the growth in numbers of banks/branches from the early 1970s to the early 1980s. The definition of banks used in the data sources consulted varied over time in these countries, but it is clear that a substantial increase has occurred. This increase represents at least a doubling of branches in Thailand during this period and almost a tenfold increase in Indonesia.

Governments carefully regulate the creation of new banks/branches. The Governments in these four countries used a variety of measures to stimulate the expansion of banks into rural areas. Bangladesh placed considerable importance on extending banking services into rural areas in the second half of the 1970s. Beginning in 1976 the nationalized commercial banks were required to provide agricultural loans, and until 1981 the Bangladesh Bank required them to establish two rural branches in order to obtain

Table 8

Number of Rural Banks/Rural Branches of Banks in
Bangladesh, Indonesia, Philippines and Thailand
1970-1983

| Year | Country | | | |
|------|--------------------------|-------------------------|---------------------------|------------------------|
| | Bangladesh ^{a/} | Indonesia ^{b/} | Philippines ^{c/} | Thailand ^{d/} |
| 1970 | 416 ^{e/} | 593 ^{g/} | 486 | NA |
| 1975 | 729 | 2777 ^{g/} | 768 | 542 ^{i/} |
| 1978 | 1634 | 3251 ^{g/} | NA | NA |
| 1980 | 2437 | 3365 ^{g/} | 1155 | 1084 ^{j/} |
| 1982 | 2932 | 5801 ^{h/} | NA | NA |
| 1983 | 3016 ^{f/} | 5810 ^{h/} | NA | NA |

- a/ Includes rural branches of all banks and all data as of June 30.
- b/ Excludes rural branches of commercial, development and savings banks except where otherwise indicated.
- c/ Refers only to rural banks and their branches, including cooperative rural banks. Excludes rural branches/offices of other agricultural lending institutions.
- d/ Data for commercial banks and Bank for Agriculture and Agricultural Cooperatives except where indicated.
- e/ 1972 figure
- f/ End of March
- g/ Pertains only to village units of Bank Rakyat Indonesia.
- h/ Rural banks are here defined to include village banks, paddy banks, petty trader banks and employee banks. These are basically unit banks. Data as of March 30.
- i/ 1974 data and only commercial banks included
- j/ Includes 58 BAAC branch offices.

Sources: Rana, Pradumna B., "Domestic Resource Mobilization Through Financial Development: Bangladesh," Asian Development Bank, Manila, February 1984.

Sugianto, "Problems of Lending Institutions: Bank Rakyat Indonesia Experience," Symposium on Farm Credit, Manila, Philippines, 1982.

Bank Indonesia, Report for the Financial Year, 1982-1983.

M. Agabin, "Philippines", Symposium on Farm Credit, Manila, Philippines, 1982.

L. Bhisalbutra, "Thailand", Symposium on Farm Credit, Manila, Philippines, 1982.

a license to open an urban branch. By 1982, 66 percent of the branches of scheduled banks were located in rural areas compared to 47 percent in 1976 (Rana). This expansion is associated with the large increase in rural deposits mentioned above. This policy has been suspended, however, because the expansion was not coordinated, resulting in a surplus of branches in some areas while other areas still have none. Furthermore, Rana reports that a large proportion of rural branches are not viable because of the low rate set on agricultural loans and because commercial banks can obtain subsidized rediscount funds for only 50 percent of their agricultural loans. The banks, therefore, are still basically urban-oriented and channel a considerable volume of rural deposits to urban areas.

The Rural Bank Act of 1952 marked the beginning of a major effort in the Philippines to expand banking into rural areas. Under the Rural Banks Program, the Government provides equity capital to match private investment in rural banks on a peso-for-peso basis. The Central Bank and other government agencies provide technical assistance in the organization and operation of rural banks, training of officers and farm advisory services. An important incentive is the rediscount privilege with the Central Bank at preferential rates of interest. Rural banks are exempt from a variety of taxes, charges and fees. Some rural banks accepted demand deposits, but now this function has been exclusively granted to commercial banks. With these incentives, the number of rural banks multiplied at a fast rate, reaching 931 banks with 1,029 offices by 1978 (Lee and Jao).

Serious loan repayment problems have created great financial problems recently for many rural banks and has slowed their expansion. Various measures are being implemented to ease the liquidity problems created by slow loan recovery (APRACA).

In Thailand, the Bank of Thailand relaxed its tight control over opening new commercial bank branches in 1975. In 1976, about three times as many branches were opened as compared to the average number opened per year during the previous four years. However, the rate of expansion slowed in 1977 because the banks experienced difficulty in meeting the credit target which required that at least 60 percent of their local deposits must be lent in the local area and at least one-third of the loans had to go to farmers (Meyer, Baker and Onchan).

Other Determinants of Deposits

Interest rates and access to financial institutions are likely to be key determinants of rural deposits in most situations, but other subtle, less well-documented factors may also be important. The effective rate of return on deposits is an important issue. The real interest rate is a key variable in determining effective rates, but there are other factors. Several countries have used prizes, raffles, lotteries, and other devices to stimulate interest in deposits. Prizes raise the effective rate of return, while raffles and lotteries introduce the possibility of earning an exceptionally high return and appeal to the gaming interests of savers. Complicated procedures for making

and withdrawing deposits work in the opposite direction by lowering the effective rate of return. Studies of the transactions costs of borrowing show that the value of non-interest costs sharply increase the effective cost of formal loans (Adams and Nehman, Ahmed). Likewise, the value of time lost to make and withdraw deposits, the costs of passbooks and photographs for identification cards, and other miscellaneous costs can significantly reduce the real return on deposits. Studies are required to determine the incidence and magnitude of these costs, and how they affect savings.

Although the potential for rural deposit mobilization is great, the unit cost per depositor or account may be large for small deposits made by poor people. Some of the costs identified above may be used by institutions to screen out small deposits. Some institutions accomplish this by setting limits on the minimum size of initial and/or existing accounts. Innovations and streamlined procedures are required to reduce costs and open up deposit possibilities for more savers. A small amount of the huge subsidies currently spent for agricultural loans should be directed towards institutions that experiment with savings innovations so solutions to these problems will be more quickly found.

Banks are highly regulated institutions and as such have relatively high costs. It will always be difficult for them to reduce costs. Credit unions may have greater potential in this area because they are less regulated and have found ways for depositors to willingly assume some of the administrative costs.

Their experience may suggest ideas that other institutions can adopt to reduce costs.

CONCLUSIONS

The major financial institutions in Bangladesh, Indonesia, the Philippines and Thailand have not been very successful in mobilizing rural deposits. Fragmentary data suggest, however, that a large untapped deposit potential exists. Institutions heavily engaged in agricultural lending have few incentives to mobilize rural deposits. The administered interest rate structure that exists in these countries is a major disincentive because rediscount or other government funds are cheaper sources of funds than deposits. Interest rate reforms are required which increase the return to savers, raise the cost of refinance funds relative to deposits, and increase the lender's return from agricultural loans. The establishment of floating deposit rates in the Philippines and the recent increase in rediscount and lending rates for agriculture in Bangladesh are steps in the right direction. The recent expansion in rural banking in all four countries is also helpful by making deposit facilities more accessible. The challenge now is to identify how institutions can efficiently mobilize large numbers of small deposits so the effective return is high for savers and bank administrative costs are reduced to manageable levels.

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