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THE RURAL SAVINGS MOBILIZATION PROJECT

IN THE

DOMINICAN REPUBLIC

Prepared for

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15

## THE RURAL SAVINGS MOBILIZATION PROJECT IN THE DOMINICAN REPUBLIC

The Rural Savings Mobilization Project ( hereafter RSMP ) is one of a series of efforts by USAID/Dominican Republic over a number of years to use and improve the performance of financial institutions as a vehicle for rural development. Although a relatively small project (overall costs at 1,290,000, including 500,000 AID and 790,000 host country contribution) it is an ambitious project intellectually, politically and developmentally.

RSMP was conceived as a "pilot project" to demonstrate the feasibility of mobilizing voluntary savings in the rural areas and to suggest the desirability of major changes both in the internal financial management of participating institutions and in the set of aggregate financial policies, including interest rate policies.

The project has three components:

1. Savings Mobilization in the Agricultural Bank ( hereafter BAGRICOLA )
2. Savings Mobilization in Credit Unions, and
3. Research and Dissemination.

### SAVINGS MOBILIZATION IN BAGRICOLA

BAGRICOLA was founded in 1945 as general development bank. In 1956, it began to specialize in credit for the agricultural sector. Prior to 1984, when savings mobilization was implemented under the RSMP, the bank did not mobilize domestic resources through savings or time deposits. In these years, BAGRICOLA obtained its loanable funds from three major sources: foreign donors, the Dominican government; and rediscounts under the Central Bank-administered Economic Development Fund. With the availability of these funds, there was little incentive for BAGRICOLA to mobilize domestic financial resources. The Bank had also a record of large deficits that stemmed from inefficient and costly operations, and high rates of delinquency.

One objective of the RSMP was to establish a savings capacity within BAGRICOLA that would effectively mobilize resources in domestic financial markets, thus allowing the bank to become

less dependent on foreign financing. Further, the process of savings mobilization would lead to the creation of incentives within the Bank that would encourage more cost efficiency. It was expected that BAGRICOLA would become a true financial intermediary by offering services to savers as well as borrowers.

The project played an important role in initiating thinking among bank senior-level officials about the benefits of savings mobilization. Major events in this process were two workshops. The first stimulated thinking, and the second was important in fostering implementation of the program. There were two additional factors that were instrumental in hastening the process. First, the rapidly deteriorating economic situation between 1982 and 1984 caused Dominican officials to look more to internal sources, and less to external funds, for generating loanable funds. Second, in early 1984 there was a change in the Administrator (the Chief Executive Officer) of the Bank. The new Administrator, a former Minister of Agriculture, was more receptive to savings mobilization as a policy concept and took it on as a major project of his administration. These two factors, in combination with affective promotion and support by the project, were instrumental in causing BAGRICOLA to launch a major savings mobilization program in 1984, which exceeded largely the expected targets (four branches mobilizing savings).

On June 1984, the Monetary Board authorized BAGRICOLA to receive savings deposits. On July 2, the first savings were mobilized, beginning in one branch. By October 12, 1984 RD\$ 672,000 were on deposit in fourteen of thirty-one BAGRICOLA branches. By December 15, 1984, twenty branches were mobilizing savings and RD\$ 2,827,000 were on deposit. At this point, BAGRICOLA was recommended to stop incorporating new branches in the savings mobilization program until the set of problems generated for the Bank were adequately addressed.

The savings mobilization program has created several new tasks and burdens for BAGRICOLA employees. First, the branch managers must turn around the funds mobilized into loans in

order not to lose revenue and maintain the advantage of their spread. Moreover, they must try to lend these funds to clients who demonstrate a high probability of repayment in order to cut future bad-debt losses. Given the Bank's experience with high delinquency, this means being very selective among borrowers. Second, the need to keep records and calculate interest on the savings accounts has placed a considerable burden of extra work on some personnel. There are plans to solve this through the installation of mini-computers in the branches. Third, BAGRICOLA has become very conscious of the need to reduce the costs associated with operations and delinquency as well as revenues from interest rates as it has to determine the interest rate spread between savings and loans.

In summary, it appears that BAGRICOLA has solved the "first generation" problems--getting the savings mobilization program established and in operation. In this stage, deposits were easily mobilized among existing clients and a few large depositors by offering competitive interest rates and aggressive promotion. The "second generation" problems--new tasks and burdens--suggest that future growth may be much slower. It may be that the most easily mobilized savings have already been deposited. This, in combination with the several internal management problems, will cause the bank, especially the branch managers, to move more slowly in pressing for more savings.

#### SAVINGS MOBILIZATION IN CREDIT UNIONS

The Credit Unions in the Dominican Republic, as in most Latin American countries, have mobilized forced savings through the deposits required of their members. The first Credit Union was established in 1946. In 1949, the Dominican Federation Credit Union Cooperatives and Multiple Services, Inc. (FEDOCOOP) was founded to serve as the single institution to coordinate and promote the Dominican credit union movement. In spite that by 1984 the Federation had 125 members, of which 54 were located in rural areas, its performance was judged deficient by most measures. Because of FEDOCOOP's precarious financial situation the project worked individually with each of the four selected credit unions.

The first step, after the selection process, was to work with the credit unions in educational and training programs. At this

time, additional technical assistance, mainly local, was required. By the end of October 1984, substantial progress had been made in training, but each credit union was receiving continuous technical assistance in order to address troubleshooting problems. The second step consisted in working out strategies within each credit union for promotion of the savings mobilization program among its members. A raffle was used to inaugurate the program, followed by a number of means such as: flyers delivered door to door, street banners, slides for movie theatre advertising, and radio announcements. By January 1985, three credit unions were mobilizing savings, with the fourth one incorporated in March. By the end of April 1985, close to RD\$ 200,000 were on deposits in the four credit unions. The basic philosophy for these accomplishments is to pay competitive rates.

This component has not developed as rapidly as desired, due to the time-consuming processes of selection of credit unions and training. There were two basic reasons. First, there was no support from FEDUCCOP as planned because of both the Federation's serious financial difficulties and its weak administrative structure. Second, the technical assistance team was heavily involved in establishing the BAGRICOLA savings mobilization program in the early months of the project. Therefore, there was insufficient time to devote to the credit union component to make it progress more rapidly.

In spite of these accomplishments, there are several potential problems that must be dealt with for this pilot effort to be successful. The critical problems will be associated with establishing a good institutional base, forming a good team of advisory personnel and funding expenses.

#### RESEARCH: DOMINICAN FINANCIAL MARKETS

Prior to the implementation of the RSMP, little research has been undertaken in the Dominican Republic on financial markets, especially by Dominicans. The universities had not emphasized research in general, much less that of financial markets. Among the public-sector institutions, the Central Bank was the only entity that undertook financial market research.

One objective of the RSM<sup>2</sup> was to develop a research capability on Dominican financial markets in the country. The purpose was two-fold: (1) to undertake research that would be useful in formulating policy for and evaluating the savings mobilization effort, and (2) to establish a capacity and capability within Dominican universities and public sector institutions to undertake research and continue to carry it out, once the RSM<sup>2</sup> is completed.

Given that the RSM<sup>2</sup> has been in effect only more than a year, the amount of research activity undertaken is quite remarkable. Furthermore, this activity has made important inroads into institutionalizing research units within the Central Bank and, to a lesser extent in the several universities and some public entities. The research has been of an applied nature. The quality is uneven, but, much of it is good and very relevant to the goals of the project. It has been important in creating a better understanding of Dominican financial markets, evaluating the performance of savings mobilization programs, and most important, assisting in policy formulation related to financial markets.

The two key elements in research activity under the project have been: (1) use of workshops to identify research projects and report the results of these projects, and (2) work with institutions and professionals to encourage them to participate in the research effort, in order to create a research capability to address policy issues for financial markets in the nation. A good number of different institutions and professionals have manifested a strong and active interest in undertaking research. Of particular importance, has been the enthusiastic support for the research effort in the Central Bank. The Bank's Financial Department has rapidly built up a research unit, which has assembled a research team that has attacked several important problems in understanding the role of non-regulated financial markets. The research unit is well established, and has the support of the Senior Bank Officials. This is important given the key role of the Bank in the nation in financial and monetary matters.

The research effort in the Agricultural Bank is much more limited. While supporting the concept of research, it has

been undertaken descriptive evaluative analysis of the savings mobilization effort, e.g., transactional costs and savings depositors behavior. The other institutions that are undertaking research studies in financial markets are: The Catholic University at Santiago and Santo Domingo, the Technological Institute (INTEC), the Superior Institute for Agriculture (ISA), and the Secretariat of Agriculture (SEA).

Although the research dimension of the RSM<sup>2</sup> got off to a good start, there are several problems. First, some of the research studies are taken longer than planned. Second, there is a need to build more solid institutional bases for research units within the universities. The work undertaken by universities has been largely an individual effort; most of it being done by persons with M.S. and Ph.D. level training. Third, there has not been any systematic manner established for publishing the research results. Fourth, some of the researchers need additional technical assistance to complete their projects.

In summary, the project has been exceptionally effective as an instrument of policy dialogue. Even if substantive results do not ultimately meet hopes and expectations, the process itself is an accomplishment in that it demonstrates how effective in-depth dialogue can be promoted on complex and controversial policy issues. The combination of public discussion, research by local investigators, and operational innovation by counterpart institutions - all supported and encouraged by flexible technical assistance and financing arrangements - is a desirable model for assistance. This model is particularly interesting in circumstances where defects in the policy environment are considered to be crucial constraints to achieving significant national development objectives

LESSONS DERIVED FROM THE RSMP

1.- The core issue in agricultural credit is not interest rates out the lack of profitability in agriculture. Until the policies and the system of access to improved technology, inputs and markets - which make agriculture profitable - are in place, donors and government "money" may not be viewed as agricultural credit ( in the sense of funds borrowed with the intention of investment in the agricultural sector and repayment). Because of the fungible nature of money, subsidized credit will be channeled to more profitable activities usually in the urban areas. In order to deal with GDR expectations and needs for AID funding for financial sector operations (beyond technical assistance and commodities for institutional improvements), USAID/DR is making an explicit distinction between: (a) money for "credit" to encourage profitable agriculture, and (b) money for contingent transfer payments to farmers for defined economic, social and political objectives. This last is justified until the policy and institutional structure of the agricultural and financial sectors are in sound condition. In this sense these operations are clearly identified as "transitional", related only to current economic difficulties of the country.

2.- Support from the S and T/RAD Cooperative Agreement Project "Rural Savings for Capital Mobilization" and its predecessor "Rural Financial Markets" was an essential factor in developing and implementing the RSMP in a timely manner.

3.- The opportunities for domestic savings mobilization are present in spite of deteriorating economic conditions. In order to minimize the "risks" of aggressive savings mobilization within institutions not previously oriented toward "banking" activity, flexible and adequate technical assistance must be assured to help local technicians deal with unfolding problems and opportunities.

4.- The implementation of savings mobilization programs within credit unions may require initially a relatively "high" investment as compared to other financial institutions, but it gives the hopes of a significant and innovative initiative in cooperative development.

5.- A project strongly oriented toward "rural" financial mar-

kets may help to open avenues of possible reform well beyond the strictly rural if it is effective as an instrument of policy dialogue. A comprehensive financial reform is desirable in order to improve the performance of rural financial markets.