



Difficulties Facing the Rural Microfinance in Chongqing City and Suggested Countermeasures

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Abstract

Rural microfinance plays a significant role in promoting the development of rural economy and in accelerating the building of a new socialist countryside; in particular, it could boost the growth of rural collective organizations, agricultural cooperatives, family farms and rural micro-enterprises, as well as meet their need for capital funds. Chongqing, as the sole municipality in west China, is to build the western financial center. Besides, faced with the circumstances of being a large city with large rural areas and mountainous areas, and with the arduous task of realizing urban and rural development, developing rural microfinance in Chongqing, therefore, is of immense necessity and importance. This paper conducts a specialized study on the development of rural microfinance in Chongqing city, in the process of which the author locates many difficulties still facing its development, then countermeasures are suggested to cope with them.

Key words: Rural microfinance; Development; Difficulties; Countermeasures; Chongqing

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INTRODUCTION

Rural microfinance, as an effective model of poverty alleviation and development, witnesses its early

development in foreign countries in the seventies of the last century. In particular, the most typical microfinance model could be seen in the People's Bank of Indonesia, in the Grameen Bank in Bangladesh and in the Bancosol of Bolivia. Such rural financial innovation model has exerted immense influence to the whole world. Later on, this model finds its way into China, and has promoted the development of China's finance in rural areas. Up until now, scholars have done a lot on this issue.

Scholars in foreign countries have conducted fruitful researches from many aspects including the concept, clients, effects, operation mechanism of the microfinance as well as its realization of a sustainable development. In relation to the concept of microfinance, the international community has yet to reach a unified opinion, but some general consensus has been achieved. For example, Morduch (1997) holds that microfinance is a way of providing loans which does not need someone to provide mortgage guarantee and which has a high interest rate but involves a limited amount of loans. The clients of microfinance are poor farmers. World CGAP (2000) points out that microfinance includes capital loans, consumer loans, savings, insurance, pensions and other comprehensive range of financial services. Joanna Craig Wood (2001) also supports this view. With regard to the clients of microfinance, Elisabeth (1997, 2000) discloses that welfarism emphasizes microfinance services being provided to the poorest people, while institutionalism believes the object of microfinance should be the clients who find it hard to obtain financial services; but later on institutionalism argues that microfinance should be given to the poorest people. As for the effects of microfinance, scholars abroad believe that microfinance plays a significant role in reducing poverty and in providing money to the poor. Both Morduch (2001) and Pischke (2002) deem that microfinance's function in reducing poverty is remarkable. When it comes to the operation mechanism of microfinance, its commercial model has

been generally recognized. Morduch (2000) regards that giving subsidies is a viable way; Stiglitz (1990), Ghatak (1999), Morduch (2000) all reveal that the model of group lending has been proven feasible; Kasia (1999) and Pawlak (2000) argue that microfinance should take into account and satisfy the real needs of clients. In terms of the sustainable development of microfinance, Yaron (1994) points out that it should consider its extensibility and sustainability; Stallings (1999) believes that the key to ensuring a sustainable development of microfinance is to maintain a high repayment rate; Fernando (2003) points out that the change of NGO into a financial institution could ensure its sustainability; Besides, Jeffrey Poyo and Robin Young (2004) also reveal that NGOs in many Latin American countries have turned into formal financial institutions. In addition, foreign scholars also conduct discussions about microfinance in terms of its model, interest rate and other issues.

However, in the meantime time, scholars in China have also explored related issues regarding microfinance including its concept, effects, model, problems, and solutions. As for the concept, Sun (2004) deems that microfinance is aimed at poor families or groups who have limited capital or who are operating small-scale business; Jiao and Yang (2006) believe that microfinance is a new way of assisting the poor; Bai (2008) points out that the clients of microfinance include micro-enterprises. As for the effects of microfinance, He (2002) indicates that microfinance is of immense significance for the rural economic development and for the augmentation of farmers' income, and that such significance is more prominent when farmers' demand for finance expands. With regard to the model of microfinance, Lv (2003) puts forward a model combining government, bank and cooperative together to reduce poverty. Jiang (2008) suggests a mutual guarantee model. In relation to the problems of microfinance, Sun and Du (2000) argue that non-financial microfinance is a matter of legitimacy, whereas financial microfinance is a matter of sustainability; Chen and Xie (2002) hold that the incomplete development of rural market economy obstructs the advancement of microfinance; moreover, Wang (2007) finds that the interest rate of microfinance (below market levels) will affect its sustainable development; Zhang and He (2009) reveal the constraints of China's microfinance. As to the measures taken to promote the development of microfinance, Du and Sun (2000) believe that government should deal with different microfinance projects in different ways; Yin (2004) suggests that an agricultural insurance system should be implemented to reduce the risks. Besides, Du (2010) advises that we should build a benefit-sharing financial system. Tang (2010) considers that we should carry out innovation in terms of the system, institution and product, etc. In addition, Wu (2010) proposes the implementation of preferential policies in tax,

interest rate and deposit reserves; Jiao (2010) considers that we should encourage innovation and diversification in regulation and management.

To nutshell, both domestic and foreign experts and scholars have carried out in-depth researches on the issue of microfinance. However, most of them are conducted from the perspective of the supply of microfinance; little is from the aspect of farmers' needs; besides, most of the researches are done from the perspective of financial system, while ignoring the study outside the financial sector; moreover, most of the researchers proceed from a microscopic point of view to discuss the sustainable development of microfinance, while ignoring the analysis carried out from a macro perspective. Based on this, the writer thus makes an attempt to explore the rural microfinance issue in Chongqing city.

1. CONNOTATION OF RURAL MICROFINANCE

No unified definition regarding the connotation of microfinance has been achieved among the scholars at home and abroad. Most definitions deal with microfinance from the aspects of microfinance's services, target clients, and purposes. There are two ways in Academia to define microfinance in general. The first definition holds that the main purpose of microfinance is to reduce poverty. Scholars who support this view believe that microfinance is mainly aimed at low-income groups, especially at the vulnerable women. With a small amount of loan provided, their production activities will be promoted, which then generates revenue that could help the clients repay the loan. The loan in this sense is different from the general anti-poverty funds; the second definition mainly proceeds from the financial services provided by microfinance, which deems that microfinance primarily provides financial services for low-income groups who find it difficult to obtain loans through the formal channels. For instance, as is stated in the "Handbook of Microfinance" by the World Bank, microfinance is an approach benefiting low-income groups. Du Xiaoshan believes that microfinance serves as a way to providing a small amount of loan to the poor who have certain debt capacity. Nevertheless, the general view is that microfinance is a limited amount of loan provided to the poor without any mortgage guarantee. Based on the viewpoints of all the scholars, the paper puts forwards another definition of microfinance. In details, the writer believes that rural microfinance could be any organizational structure or operation pattern that provides small-scale loans, savings and other comprehensive financial services for the low-income groups in rural areas in a continuous manner. According to the paper, rural microfinance is a financial innovation, an organizational innovation, and is a way to reducing poverty.

2. DIFFICULTIES FACING THE DEVELOPMENT OF RURAL MICROFINANCE IN CHONGQING

2.1 Low Interest Rate Makes Money Unable to Meet the Needs of the Poor

Reasonable interest rate in line with the market expectations is the key to the sustainable development of microfinance, and many scholars believe that the interest rate of microfinance need to agree with that of the ordinary commercial banks. In this way, the interest rate of microfinance could meet the needs of both borrowers and creditors. It is affordable to borrowers, and creditors can make up for the costs of capital, management costs, and the loss of inflation. Creditors can even make some profits. Scholar Zhang Gaiqing also believes that reasonable interest rate determines whether the poor could get loans and whether the microfinance could develop in a sustainable manner. According to the current researches, the majority of farmers believe that the interest rate of rural microfinance in Chongqing is not high, which reduces the burden on borrowers, and in theory, plays a role in poverty alleviation. But low interest rate has led to problems. On the one hand, the costs of microfinance could not be covered, including its funding costs, management costs, losses of inflation, and so on. On the other hand, low interest rate could lead to high default rates, that is, the phenomenon that the borrowers do not repay the loan on schedule or do not repay the loan is easy to see. At the same time, low interest rate could make poor farmers who really need funds difficult to obtain loans, for a part of the small loans is likely to be diverted to other areas. Besides, some loans need interpersonal relationship to support. Furthermore, most loans tend to flow into the hands of enterprises and the wealthy, which makes it unable to meet the needs of the poor.

2.2 Low Credit Line Promises Less Loan Funds

In general, different credit lines are provided for different institutions and individuals by loan credit institutions. Credit line is usually determined based on borrowers' credit rating. All of the rural microfinance institutions in Chongqing city almost have such a credit rating system, with the credit rating level descending from "AAA" to "AA" and to "A". The credit line varies anywhere from ten thousand RMB to tens of thousands RMB. The more "A" one borrower has, the higher his credit line will be, and anyone who has been awarded "credit borrower" more than once can enjoy an increased credit line. If borrowers' loan funds are to be used for household expenses, the credit line should be controlled within 60% of the amount of their families' net income in the previous year. According to the statistics, the credit line for most rural microfinance in Chongqing is lower than the standard level. Farmers could actually only get credit

loans ranging from several thousand RMB to twenty thousand RMB. And more than half of the farmers obtain the funds in less than 10 thousand RMB. Hence farmers' loan funds are not enough for them to use due to such a low credit line. Therefore, only by raising the credit line of farmers can their production and living needs be met. Relevant surveys have disclosed that the vast majority of farmers expect to have higher credit line, for more investments are required for their engagement in the diversified agricultural businesses. What's more, their non-agricultural expenditure is increasing. Since credit line is subject to borrowers' repayment ability and credit rating level, the poor will find it very hard to obtain a higher credit line. In turn, low credit line makes it difficult for them to expand production, which in turn makes them feel hard to acquire high credit line. All these have formed a vicious cycle, imposing difficulties to farmers in terms of borrowing enough loan funds.

2.3 Short Loan Period Affects the Demand for Long-Term Loans

Loan period is also an important factor affecting the sustainable development of rural microfinance, for it directly affects the deadline of the loan repayment period. If the loan period is reasonable, it will help farmers pay off the loans in a timely manner. Microfinance institutions will develop different loan period for different situations. According to the traditional farming households, special planting households, breeding specialized households, and others, loan periods ranging from one year to several years have been designed. These institutions have changed the traditional business model that features spring planting and autumn harvesting, but the model is still not detailed and is not in line with the needs of modern agriculture loans. According to the survey, more than half of the farmers advocate that loan period should be five years. There are also some farmers who hold that the loan period should not be too long; instead, it should be consistent with the agricultural production cycle. Others believe the loan period should be one or two years. Meanwhile, non-institutional private microfinance institutions set no clear loan period, which increases the risks of non-repayment. In this situation, creditors can ask the borrowers for repayment anytime. This makes it impossible to form large-scale folk credit industry, and thus farmers could only seek help from specialized microfinance institutions. But a shorter loan period will affect the demand of farmers for long-term loans.

2.4 Inadequate Management Capacity

Healthy and sustainable development of microfinance relies on good management capacity of microfinance institutions. In other words, management capacity largely determines the sustainable development of microfinance institutions. In reality, many microfinance institutions in Chongqing, confined to their own capacity, do not have

a good management ability. Clear strategic objectives and operational plans have not been designed. For example, many microfinance institutions do not have clear development goals; they fail to pay attention to the long-term circumstances; and their long-term plan is not in place. Besides, decision-making mechanism and financial management system are not standardized. To be more specific, microfinance institutions have not developed a comprehensive decision-making system on giving out loans; the process of giving out loans is not perfect; no standardized financial management system has been established. All these have increased the risks of small and micro business management operations. In addition, the lack of good managers also contributes to the operational management of microfinance institutions.

3. COUNTERMEASURES AND BREAKTHROUGH

3.1 Designing a Reasonable Interest Rate to Ensure Sustainability

As mentioned above, low interest rate will not only dissatisfy the needs of farmers for money, but will bring difficulties to the development of microfinance. Therefore, it is necessary to change the current situation of low interest rate. Many scholars have proposed to increase the interest rate of microfinance and to replace it with that of the commercial banks. Besides, it is suggested to relax controls on the interest rate of microfinance, and to let it determined by the demand and supply of the market. The main practice is to determine the interest rate in accordance with the standard commercial rates of interest. Since the supply of credit to the poor is always limited, we should not solely rely on a low interest rate. Instead, we should develop reasonable policies to change the current situation. In this sense, we need to relax controls on the interest rate, or the prices of loans would be distorted, leading to irrational allocation of resources and affecting the profitability of rural microfinance institutions. Also, it is worthy of noting that the increased costs caused by setting commercial interest rate can actually be offset by farmers. Studies have shown that the poor are fully able to repay the loans if the interest rate is set according to the demand and supply of the market.

3.2 Accelerating the Establishment of Farmers' Credit System

Establishing farmers' credit system is of huge importance to the sustainable development of rural microfinance. It could guarantee timely repayment of loans, thus ensure sustainability of microfinance. First, as for the high risks in agriculture, and with the regard to the scattered loans borrowed by farmers and difficulties to recover the loans, we need to mobilize the relevant subjects, such as the local governments, village-level self-government organizations,

village collectives and farmers. So that all together could urge farmers to timely repay the loans and create a good atmosphere for giving out and recovering loans, thus increasing the recovery rate. Second, we should go deep into the farmers and do field investigations, so as to understand the circumstances of the borrowers including their property, income and production, on the basis of which we can establish farmers' credit files, and provide appropriate credit lines. Besides, we can also conduct dynamic credit rating. For example, we can increase or decrease the credit line for the farmers according to their repayment behaviors in the past. Third, local governments, village committees, village representatives could join hands together to form an Integrity Surveillance Committee, thus supervise the behaviors of farmers. They should keep abreast of the latest information about the borrowers, and ensure that the borrowers will use the borrowed funds in accordance with the designed purposes and repay the loans on time.

3.3 Perfecting the Fund Supply Mechanism for Rural Microfinance

In order to provide microfinance for the real poor people such as farmers, we need to establish a sound fund supply mechanism. The primary task is to avoid a massive outflow of funds in rural areas which has reduced the satisfaction of farmers' demands. Moreover, we could improve the ability of banks, non-bank financial institutions, and other microfinance institutions in terms of absorbing scattered funds, and increase their capacity of offering loans; secondly, the municipal government of Chongqing needs to support local microfinance institutions, and give them necessary financial investment and subsidies. Besides, Municipal-level financial resources could be allotted to policy-subsidized microfinance institutions as discount interest funds and subsidies for bad debts, encourage the opening of policy-subsidized microfinance services, and design preferential policies for the poor farmers. Finally, we could step up lending for rural farmers. As for the fund outflow in rural areas, microfinance institutions should increase lending for the poor farmers, thus supplying them with enough microfinance funds in a timely manner.

4. IMPROVING THE MANAGEMENT OF MICROFINANCE INSTITUTIONS

The management quality of microfinance institutions will directly affect their ability of sustainable development. Through improving their management level, microfinance institutions could reduce operating costs and improve management efficiency. In this sense, it is essential for microfinance institutions to do so. To the end, the primary thing is to improve the management capacity of microfinance practitioners, especially the managers, and cultivate specialized microfinance practitioners, so that

they could familiarize themselves with the microfinance business knowledge and have a good grasp of microfinance management skills; second, it is crucial to update the incentives. We can take some new incentives, such as the implementation of the incentive integrating finance quality and efficiency, encouraging lending officers to reasonably give out loans and timely recover loans. Besides, we could establish a management responsibility system suitable for the development of microfinance so that the rights and responsibilities are integrated. For the practitioners in microfinance institutions, we could implement a responsibility system in terms of giving out and recovering loans. Finally, it is recommend to change the existing loan system mode and the traditional “guaranteeing income and zero risks” system, and to carry out the “risk management” system. We can develop incentives and punishment measures based on the non-performing loan ratio for the year, stimulate the enthusiasm of loan officers, and promote the improvement of management quality of microfinance institutions.

CONCLUSION

The sound development of microfinance institutions is essential for satisfying the financial needs of farmers, especially the needs of the poor. This paper explores this point in details and takes the rural microfinance in Chongqing city as the research focus. Meticulous analysis has been carried out, followed by conclusions. Practice shows that the development of microfinance is significant for Chongqing’s urban and rural development and for the realization of new rural construction in Chongqing city. However, it should be noted that many problems are still facing the growth of Chongqing’s rural microfinance, for instance, the interest rate is not high; the credit line is too low; the loan period is short; the management level of microfinance institutions is relatively low. In order to change the unfavorable situation, the paper puts forward some specially targeted countermeasures. Specifically,

the paper holds the belief that we should determine a reasonable interest rate, apply the commercial interest rate, increase the credit line and expand the loan cycle, and enhance the management capacity of microfinance institutions. These are believed to show implications for improving the overall situation of the rural microfinance in Chongqing. However, the sustainability model on rural microfinance and its commercial operation remain to be further studied.

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