

On the Analysis and Improvement of the Rural Financial System in Shenyang City of China

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Abstract: Based on information collected by interviews, fieldwork studies, questionnaires and so on, this paper is an attempt to analyze the rural financial industries in Shenyang. There are a number of studies on the rural financial system of China in recent years, but few based on municipal level. It is necessary to do such a study from the perspective of a city, as Shenyang, which can help city policy makers get a clear view of the rural financial system. After analyzing these data, some problems existent in this system can be detected. The rural financial market is actually a monopoly market, with little competition faced by the Rural Credit Cooperatives. The high deposit loan imbalance shows that money is not fully utilized in rural market and the amount of money lent to farmers is rather small. The high non-performing loan rate indicates an unfavorable rural financial environment. There are several policy recommendations made in this paper, which includes establishing a more diversified rural financial system, improving supporting service, increasing money supply and upgrading the financial environment in rural area. We have good reason to believe that these efforts would provide the market with more competitors, better service, more loans and a good environment.

Keywords: Rural; Financial system; Shenyang; Problems; Policy recommendations

1 Introduction

The rural financial system plays a very important role in developing rural economy and increasing Chinese farmers' income. Financial institutions in rural areas can lend money to farmers or township enterprises in need and help them with agricultural or other economic activities. As the development and prosperity of rural economy in Shenyang, the financial industries in the countryside also grow accordingly. Both deposits and loans in rural areas are rising in these years, and some insurance companies are extending their business in rural areas and increasing the kinds of insurance provided for farmers. However, there are still various problems existent in this market. This paper is going to analyze the rural financial system of Shenyang city, where economic development and farmers' income ranging at the middle level of the whole country. There are a number of studies on rural financial system of China in recent years, like *the Strategic Restructure of Rural Financial Scheme of China* by Zhao Yi, *the Optimal Path of Rural Financial System Reform in China* by Gu Shen, *the Weakness and Policy Recommendations of Rural Financial System of Hebei Province* by Chang Fangnan and Wang Shaochun, etc. But there are few studies based on municipal level. The real situation of financial market varies from place to place, it is necessary to analyze it from the perspective of a big city such as Shenyang, to help city policy makers get a clear view on how the local rural financial system runs and on how to improve it.

This paper is based on information collected by interviews, fieldwork studies, questionnaires and case analysis and so on, conducted by the writer and her helping hands. Each of the 8 districts (Liaozhong, Xinmin, Kangping, Faku, Shenbei, Dongling, Yuhong and Sujiatun) that have rural areas in Shenyang city is sampled and investigated. Totally 26 towns, 52 villages, 80 financial institutions, 30 township enterprises and 310 rural families were studied. Relevant government agencies also exposed certain data to this study and some government officials have narrated considerable information.

2 Basic Information Financial Institutions in Shenyang City of China

Currently, there are 7 financial institutions dealing with agricultural business at municipal level: the People's Bank of China Shenyang Branch, Shenyang Rural Credit Cooperatives, Agricultural Development Bank of China Liaoning Branch, Agricultural Bank of China Liaoning Branch, Property Insurance Company of China Liaoning Branch, Life Insurance Company Shenyang Branch and Postal Savings Bank Shenyang Branch under construction. At district and county level, the number of financial institutions that has agriculture related business is 106, among which 4 belonging to People's Bank of China system, 9 belonging to Rural Credit Cooperatives system, 13 belonging to Agricultural Bank system, 8 belonging to Agricultural Development Bank system, 22 belonging to Property Insurance

system, 26 belonging to Life Insurance system, 24 belonging to Postal Saving system.

At township level, also the main concern of this study, there are totally 375 financial institutions, among which 156 belongs to Rural Credit Cooperatives system, accounting for 41% of all the financial institutions at township level, 44 belongs to Agricultural Bank system, accounting for 12% of the total number, 90 belongs to Life Insurance Company system, around 24%, 85 belongs to Postal Savings system, about 23% (See Figure 1).

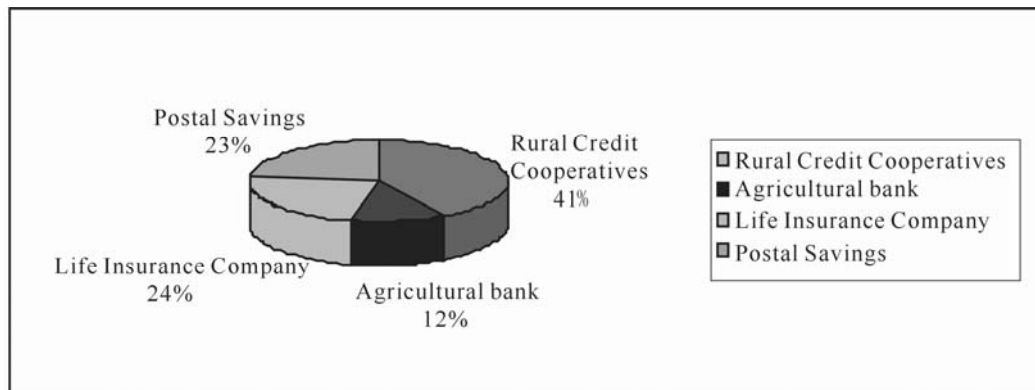


Figure 1 The Breakdown of Financial Institutions at Township Level

Now we look at the loans and deposits balance. The total number of deposits for rural financial institutions of Shenyang is 36.76 billion yuan by the end of December 2008, while the number for loans is 10.31 billion yuan, the difference is 26.45 billion yuan. Now we look at the number for some different financial institutions. The deposit is 10.2 billion yuan while the loan is 2.88 billion yuan for Shenyang Postal Savings; the deposit is 22.3 billion while the loan is 13.32 billion for Shenyang Agricultural Credit Cooperatives (See Figure 2).

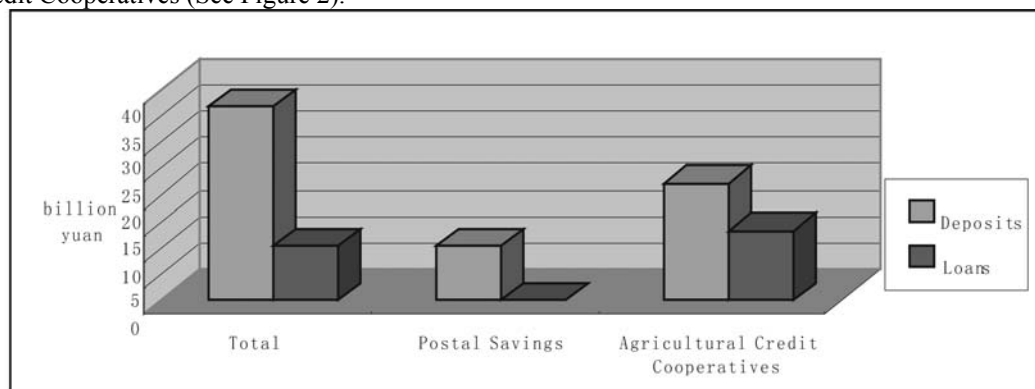


Figure 2 Deposits and Loans for Shenyang Postal Savings, Shenyang Agricultural Credit Cooperatives and Total Number of Shenyang

3 Problems in Shenyang’s Rural Financial Market

From the basic information demonstrated in the last session, we could get a rough idea about what the system like and what are the problems existent now in Shenyang’s rural financial market.

3.1 Insufficient competition

From Figure 1 we can see that the Rural Credit Cooperatives occupy a major percentage among all the financial institutions in Shenyang, around 41%, well above organizations from other systems (23% for Postal Savings, 12% for Agricultural Banks, 24% for Life Insurance Company). Actually, the rural financial market is kind of a seller’s market and the Rural Credit Cooperatives is like the monopoly in this market. The recent statistics shows that the short-term agricultural loans and private entity loans issued by Rural Credit Cooperatives occupies 87.4%, 35.8% of the total number, respectively. According to our survey, 59% of farmers and 35.29% township enterprises interviewed told that they will go to Rural Credit Cooperatives for loans as their first choice.

What attributed to this situation? In recent years, as the state owned banks undergoing reforms and commercialization, a number of banks and financial institutions in Shenyang gave up their business in

rural area and mainly focused on the city market, because they can earn more money there than in countryside. There are much fewer financial institutions left in the country area and less choices for farmers when they want to save and borrow money.

3.2 Unsatisfactory service quality

Due to little competition, the incentive for the Cooperatives to improve the quality of service is rather low and there are many weaknesses in the service provided by the Cooperatives. For one thing, the time limit of loans lent by the Cooperatives is somewhat shorter than necessary. The Cooperatives usually lend money from January to March each year, and withdraw from October to December at the same year. They won't let it returned next year, and the loan period is not synchronous with the agricultural production. A peanut planter told in interview, the price for peanut is 2.05 yuan per catty in September, the time peanuts starting to get ripe. If farmers can sell the peanuts after one or two months, the price can go up to around 2.7 yuan per catty. But the cooperatives require farmers to repay the loan from October; farmers have to sell the peanuts at a relatively low price. The same thing happed to scallion planters as well. For another, the yearly interest rate of the loans from the Cooperatives varies from one borrower to another, with an average 12%. The interest rates for some farmers are as high as 24% to 36%. The difference of rates makes room for the officers in Cooperatives to get their own benefits. For example, they may give a relatively low rate for borrowers who gave them "benefits" in certain forms while a high one for those who didn't.

3.3 Limited loans and unutilized deposit

Figure 2 demonstrates the considerable deposit loan imbalance in current rural financial market. The deposits in Shenyang's rural financial institutions are 36.76 billion yuan in the year 2008, while the loans are 10.31 billion yuan; the difference was as high as 26.54 billion yuan. More than 2/3 of the money has not been utilized in rural market and flowed out. By the data provided in the information part, we can calculate the loan deposit ratio is 28% for Shenyang rural financial institutions together (10.31 divided by 36.76); the ratio is much smaller for Postal Savings, 0.028%, means that in the 10.2 billion yuan of deposits for Postal Savings, only 2.88 million yuan was lent out to farmers. According to our survey, the average amount of money the Cooperatives lent is around 10,000 rmb per family each year, only covering the basic needs for simple agricultural production. Around 47.8% of farmers surveyed regarded the limited amount of loan as the most important problem in current system. While large sum of money is flowing out of rural market rather than supporting the rural development, over 57.2% of the farmers interviewed think the main way to increase farmers' income is to increase money input in the rural area. Why is that? To make it simple, many banks just do not lend loans in the countryside; it is their way. For example, Postal Savings seldom lend but only absorb deposits from citizens, and after banks reform and commercialization, numerous banks have cut down their branches, those left in rural areas mainly have saving function, no lending business at all.

3.4 Non-performing loans

According to statistics, the total amount of non-performing loan for all the financial institutions in Shenyang is 38.65 billion yuan, the non-performing loan rate is 14.3%. Among all the financial institutions, Agricultural Bank, Agricultural Development Bank and the Agricultural Credit Cooperatives were ranked top 3 in terms of their number of non-performing loans. Non-performing loans for the three banks were 13.34 billion, 9.32 billion, and 6.42 billion yuan respectively, together accounting for 75% of the total non-performing loans of Shenyang (See Figure 3). Non-performing loan ratio is 60.64% for the Agricultural Development Bank, 51.81% for the Agricultural Bank and 48.21% for the Agricultural Credit Cooperatives, which is quite high compared with other banks of this industry.

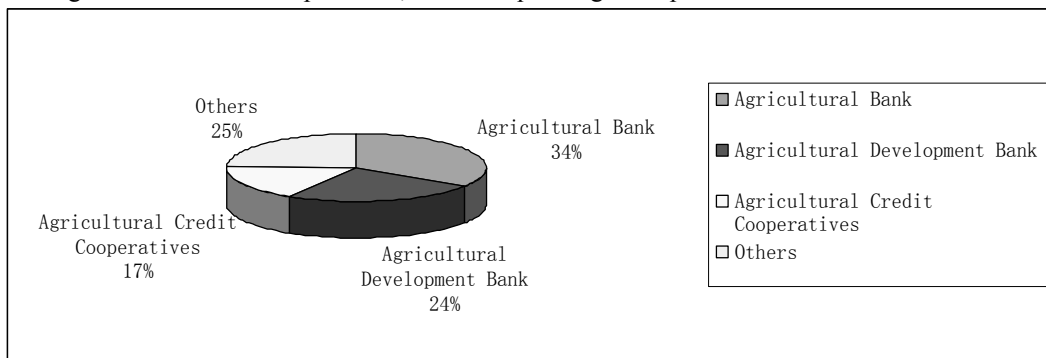


Figure 3 Breakdown of the Non-Performing Loans of Shenyang

The supervision department of banking industry told us during the survey, the amount of Shenyang's non-performing loan is quite high among the 15 vice-provincial cities; and the financial environment was ranked 44 among the 50 major cities of China. The rural financial system is even more poorly running. One of the main reasons lies in the weak legal system. The verdict of loan cases has been hard to be executed, and there are always people or organizations trying to avoid paying back to banks, especially certain government agencies and officials. Taking the Cooperatives as example, the non-performing loan in the year 2008 is 6.4 billion yuan, among which government related loan is 2.6 billion yuan, accounting almost 40%. Government related loan includes the village community loan (1.04 billion for the year 2008), government finance loan (220 million for the same year), loans borrowed by government and civil servants (700 million for the same year), and so on. It is not uncommon for government agencies or officials to do this in China.

4 Proposals Recommended

Based on the analysis above and Shenyang's reality, there are several recommendations can be highlighted:

4.1 Establish a diversified system

Firstly, government should encourage more social investment coming into rural financial market by providing favorable conditions for investors, including reduction of registration fees, business and income taxes, etc. More rural financial institutions need to be set up. Relevant government agencies need to provide help, information and guidance for those village banks, rural financial cooperative organizations and other small-amount loan institutions. Secondly, it is also very important to deepen and fasten the reform of the Rural Credit Cooperative systems. The service quality and efficiency is supposed to be improved, for example, loan procedure to be simplified, the amount of loans lent to farmers to be increased, and the period of loan to be prolonged for a little longer. Thirdly, a comprehensive agricultural insurance scheme is necessary in helping farmers and should be set up. It is better for government to choose some competitive, large-sized insurance companies as the contractor of agricultural insurance programs, so as to provide comprehensive insurance that can cover more economic plants and poultry for farmers.

4.2 Improve supporting service

The first thing about supporting service for rural financial market is to further develop the forward market of agricultural products. In order to do so, government should try to connect with leading agricultural product companies, agricultural agents, financial organizations and industry supervising departments to develop the forward market for agricultural products. Another thing is to increase the service quality of financial intermediary institutions such as services provided by law firms, accounting firms, guarantee firms and so on. Last but not least important, favorable recruiting and retaining policies should be worked out to encourage scholars and specialists to come and contribute to Shenyang. It is also very important to provide financial trainings and relevant information for agricultural agents and farmers.

4.3 Increase money supply in rural area

We can encourage financial institutions at county level and below to fully use their money as loans for farmers or to transfer their excessive deposits to rural financial organizations like the Cooperatives, so that money supply in rural area will be increased. Furthermore, government agencies in relevant can settle a basic line for rural financial institutions' loans, if banks or other institutions' loans exceed the settled amount, the part that exceeded the settled will be exempt of business taxes and income taxes. It is also important to increase the financial discount rate for farmers especially for those in poverty or remote area.

4.4 Upgrade the financial environment

The rural financial environment of Shenyang should be upgraded as soon as possible. The development of rural financial industries is supposed to be put on current government agenda and measurement need to be devised and quantified to see how well the government manages the economy. Government agencies should set the example themselves, of clearing debt with banks or other financial institutions. It is better to set the exact date for government to settle the debt, the municipal and county government can pay the loans each at a certain percentage. Furthermore, it is necessary to investigate the default cases, and punish those companies or people who purposely refuse to pay money back. More importantly, a personal credit information database should be built and the information should be shared among financial, taxes, commercial, custom departments of government.

5 Conclusion

To sum up, the problems existent in the rural financial system of Shenyang, such as insufficient competition, unsatisfactory service, limited loan and non-performing loans, have posed an obstacle for further developing rural economy and constructing “new countryside”. There are many political and historical reasons underlying this situation. Relevant government agencies should take actions to solve this problem to promote the rural economy and farmers’ life to a new level. At least 4 directions should be paid attention to: establishing a more diversified rural financial system, improving supporting service, increasing money supply and upgrading the financial environment in rural area. We have good reason to believe that these efforts would provide the market with more competitors, better service, more loans and a good environment.

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