Bank on Wheels

A recent experiment has brought banking services to Vietnam's poorest

G. Nguyen Tien Hung

MA SEO SANG, a Hmong widow living on less than 25 cents a day in the mountainous region of Vietnam, needed help. She had sold her pig to pay for her husband's funeral, paid a fine incurred by her son by selling one of her buffalo, and redeemed a debt with the other. She had borrowed all she could from relatives. Moneylenders, if they would even lend to her, would charge exorbitant interest (up to 10 percent a month). She needed money to survive.

Sang's plight raises many issues related to extreme poverty, of which lack of access to credit is one. Part of the solution is microfinance—the provision of basic financial services to the poor. Microfinance can offer a path out of poverty. But how long is the path, and can it be shortened? Vietnam's experiment with the Mobile Banking Program under the World Bank's Rural Finance Project provides a partial answer to those questions. It suggests that creative ways can be found not only for lenders to reach out to the poor but also for the poor to "reach in" to lenders.

Getting credit to the poorest

According to a 1999 World Bank survey, the proportion of people living below the poverty line ($128 per capita a year in 1998) in Vietnam dropped markedly in the 1990s, but extreme poverty still affects pockets of the population. Under various programs, significant credit was earmarked for rural development. The Vietnam Bank for Agriculture and Rural Development (Agribank), with one of the most extensive branch networks in the world, was the main conduit for this flow. However, lack of access roads and high transaction costs prevented it from serving the poorest.

In 1998, Agribank initiated a mobile banking program modeled after similar programs in Bangladesh and Malaysia. It procured 159 vehicles equipped to travel on dirt roads and hilly pathways, enabling loan officers to reach remote areas to process loan applications, disburse money, collect repayments, and mobilize savings deposits. The visits followed a fixed calendar and were announced in advance. Scheduled to coincide with weekly village markets, they saved borrowers traveling time and transportation costs. This summer, another 172 vehicles will enter service.

Once the program was launched, it became clear that more than just difficult access prevented the poorest from taking advantage of its services. Their isolation caused them to have feelings of helplessness and fear. In the upland ethnic group, the higher up a mountain people lived and the longer their isolation, the more they seemed to believe that they could not get credit. Suspicion was another issue. What if the lender offered a loan and then, if a payment were late, took a farmer's buffalo, as had happened to Sang?

Above all, the poorest people lacked confidence and self-esteem. For example, the illiterate poor would wonder how they could fill out applications and receipts. Others felt they could do nothing to earn extra income to repay a loan. Many were afraid to venture into activities other than cultivation and animal husbandry, even though opportunities existed. In Lao Cai Province, for example, an increase in tourism had created a market for ethnic cloth.

Hmong farmers wait to conduct transactions with a mobile bank in Lao Cai Province. Author appears at right.

Sustainability of borrowers

But for mobile banking to work for borrowers, the following services had to be made available.

Offering appropriate loan products. To meet the needs of the poor to finance crop production, storage, marketing, and trading, Agribank is diversifying its loan portfolio and considering a range of low-cost products that would be easy to understand and use and could be disbursed when they are needed. The poor's access to credit has also been hindered by a lack of collateral, but Agribank waived collateral for loans of up to $645; the limit has since risen to $1,290.

Linking lending and saving. Initially, Agribank focused on rural lending because its credit officers perceived that the poor were too poor to save. But training and exposure to international microfinance schemes changed this perception, and Agribank began to mobilize small savings, targeting women. The effort was enhanced by data that showed that people kept only 17 percent of their savings in banks; the rest was in gold and U.S. dollars (44 percent) and other assets (39 percent).

For Agribank, linking the two means that when credit officers disburse loans and collect payments, they are also responsible for mobilizing savings. Savings both help smooth consumption and act as insurance in hard times. Unlike Bangladesh's Grameen Bank and its Rural Advancement Committee, however, Agribank did not require borrowers to open a savings account. It decided that, for the poor to feel good about the program, saving should be voluntary. Instead, the mobile banks offered people incentives to open savings accounts. They guaranteed safety for deposits and offered attractive interest rates for different maturities.

It was no easy task in Vietnam's cash economy to persuade people to open savings accounts, but after only a year, each mobile bank began to add more than 200 new accounts every month. The shift from idle assets to income-earning assets benefited savers because of the increase in income and safety.

Combining credit and human asset building. When credit is combined with training, borrowers become more productive and are more likely to be able to repay their loans. Lenders and nongovernmental organizations can work with local agencies to provide information about the market and profitable opportunities and to explain market risk and how to cope with it. There are signs that the poor have responded favorably to these initiatives.

Sustainability of lenders

For lenders, it was necessary that the mobile banking experiment be financially self-sustaining. It thus required the following ingredients:

Group-based lending. Agribank lends to individuals directly and through village-based groups: joint-liability groups (members are liable to each other) and solidarity groups (the sponsoring organization guarantees loan repayment). Group-based lending minimizes both asymmetrical information (when lenders know little about borrowers) and moral hazard (the danger that, because a borrower does not bear the downside risks of her actions, she will undertake riskier projects, making it less likely that the loan will be repaid). Moreover, the peer pressure inherent to groups ensures that members repay. Again, unlike other schemes, Agribank does not require individuals to join but offers incentives to those who do, such as simple lending procedures, longer-term loans (three years), installment payments, and other services. Through groups, members also gain a sense of collective protection and of empowerment.

Linking formal and informal credit. Local organizations provide forums to help the poor increase their self-confidence and act as a link between the formal and informal credit conduits. For example, by helping organize a solidarity group and providing loan guarantees, the Women's Organization served as a financial intermediary in an informal and imperfect market. Agribank is also studying the prospect of linking traditional mutual credit clubs (known in Vietnamese as *Hui* or *Ho*) with the joint-liability group's activities.

Reasonable interest rates. Lending to the poor involves high risk, and the risk premium must therefore be high. In the past, Agribank offered the poor in remote areas lending rates 30 percent lower than market rates. However, such subsidies affect the lender's sustainability and undermine other microfinance programs. When credit is subsidized, borrowers tend to regard it as charity and make little effort to repay. Under the Mobile Banking Program, Agribank took a dramatic step and began to charge a rate that would recover costs. The recovery rate had to include a premium to cover the cost of running vehicles and managing small accounts and the higher level of risk in rural areas. The interest rate for rural borrowers is now 12 percent a year compared with 8.4 percent for urban borrowers.

Agribank has kept this premium as low as possible to make the lending rate acceptable to borrowers. Instead of cutting interest, it cut transaction costs. It minimized operational costs by using vehicles for multiple purposes (to transfer cash between branches, and to solicit and collect savings from small businesses en route from the markets) and by holding long hours on each visit to accommodate more clients.

It has also kept the premium low by helping borrowers understand market risk, such as the volatility of coffee prices, and the need to avoid speculative activities. So far, borrowers have performed well, with loan repayment rates of 97 percent. A number of mechanisms led to this outcome: small repayment installments, access to larger repeat loans, and simplified loan documents. Repeat borrowers were not required to prepare loan applications but could sign their loan receipt or, if illiterate, mark it with their thumbprint.

So far so good

Barely five years in operation, the Mobile Banking Program has proved to be relatively cost effective, providing financial services to 315,000 poor households, about 6 percent of Agribank's clients. Preliminary data show that, on average, each mobile bank disbursed 1,921 loans, collected 1,387 payments, and transported cash on 75 occasions to 16 local points monthly. The excellent repayment rate suggests that the poor are good credit risks. The program also mobilized 1,983 small savings accounts every month, showing that the poor can be good savers.

It was also instrumental in helping the Rural Finance Project ($110 million credit component) achieve its objective of increasing the rural poor's access to financial services. Small loans (weighted average of $452) helped borrowers diversify their activities, and 99 percent of them increased their income because of the loans.

Although Agribank has not yet made a profit on its overall operations, its Mobile Banking Program has been more successful. On average, each vehicle recorded a modest profit of about $1,000 a month after allowance was made for the cost of funds, gasoline, depreciation, and staff.

In light of its progress, Agribank is studying the possibility of using groups to expand its services. In a given season, one group of farmers (say, coffee growers) may do less well than another (for example, tea or fruit tree growers). Groups in different locations would also have different results. Can IOUs be issued to channel funds from surplus groups to deficit groups? Positive answers to this question would make it possible for mobile banking to further strengthen financial intermediation in the rural economy.

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Despite the program's positive results, a number of weaknesses need to be addressed.

Security. Although there have been no robberies of Agribank vehicles in Vietnam, where security is high, carrying cash in remote areas is risky. In countries where security is a problem, mobile banks could carry the minimum amount of cash needed for transactions and would incur some costs for protection. In new programs, Internet access can link mobile banks operating in the field with district branches. Still, the presence of mobile banks in remote areas is symbolically important.

Accessibility. Mobile banks provide limited opportunities to withdraw funds, hampering saving by the poor. Agribank is studying whether groups can offer their members some access to funds in an emergency. In a mobile bank's subsequent visit, it would reimburse groups for withdrawals.

Regulations. A market economy only since 1990, Vietnam needs to develop a strong, effective legal framework for the financial system, especially in the area of prudential regulations. Two existing laws govern credit activities but do not cover the operations of microfinance institutions, whose legal status is ambiguous. Regulations are necessary for group activities and for contract enforcement.

Monitoring. Loans, payments, disbursements, and group transactions must all be monitored in places where accounting and auditing are not commonly practiced.

Group formation and training. Over the long run, lending institutions incur costs for forming and training groups—for example, in simple accounting methods, bookkeeping, cash flow, auditing, and management skills.

These last three areas—regulations, monitoring, and group formation and training—are ones that international aid donors may be able to support in microfinance operations.

Lessons learned

The Mobile Banking Program is still being developed. Much remains to be explored to address weaknesses and maximize the effectiveness of microcredit programs. But the lessons learned thus far suggest that creative ways can be found to reach out to the poor, reducing their transaction costs and thereby improving their economic prospects. The psychological dimension of poverty, which entails a propensity toward self-exclusion, needs to be considered in the design of microfinance programs.

The most controversial aspect of microfinance is its cost. Interest rates must be high enough to ensure the lender's sustainability and low enough to be acceptable to borrowers. Many experts insist that the poor are capable of paying high interest rates and are willing to do so. Others argue that, if not for microcredit, with its high interest rates, the poor would have to borrow from moneylenders at rates two or three times higher. Nevertheless, when microcredit requires a rate substantially higher than that paid by urban borrowers, the poor could perceive that they are being exploited, especially in countries where poverty eradication has traditionally implied the use of subsidies. In the long run, how the poor feel about their loans can affect how well they perform using their loans.

As for Ma Seo Sang, she received a loan of about $300 from Agribank and used the money to buy some chickens and pigs to raise. The income she made from selling her animals helped her earn a living. ■

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