

Micro Finance in Vietnam: Three Case Studies

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List of abbreviations

BADC	Belgian Administration for Development Cooperation
BTC	Belgian Technical Cooperation
CAMEL	C apital adequacy, A sset Quality, M anagement, E arnings, L iquidity Management
CCMB	Commune Credit Management Board
CGAP	Consultative Group to Assist the Poorest
DCCU	Dairy Cooperative Credit Unit
DFID	Department for International Development
DTC	Dairy Training Centre
FAO	Food and Agriculture Organization
GDP	Gross Domestic Production
HCMC	Ho Chi Minh City
HDI	Human Development Index
HEPR	Hunger Elimination and Poverty Reduction Strategy
hh	Household
IAS	Institute of Agricultural Sciences
IDB	Investment Development Bank
I-PRSP	Interim - Poverty Reduction Strategy Paper
MIS	Management Information System
MOLISA	Ministry of Labor, Invalids and Social Affairs
NGO	Non-governmental Organization
ODA	Official Development Assistance
PC	People's Committee
PCF	People's Credit Fund
PEARLS	A set of ratios and measures used by the World Council of Credit Unions (standing for P rotection, E ffective financial structure, A sset quality, R ates of return and cost, L iquidity and S igns of growth)
PPA	Participatory Poverty Assessment
PPMU	Project Permanent Management Unit
PPP	Purchasing Power Parity
RJSCB	Rural Joint Stock Commercial Bank
ROSCA	Rotating Savings Credit Association
S&C	Savings and Credit
SBV	State Bank of Vietnam
SOE	State-owned Enterprise
TFF	Technical and Financial File
UNDP	United Nations Development Program
UNESCO	United Nations Education Science Culture Organization
US\$	United State dollar

VBA	Vietnam Bank of Agriculture
VBARD	Vietnam Bank of Agriculture and Rural Development
VBCP	Vietnamese - Belgian Credit Project
VBP	Vietnam Bank for the Poor
VLSS	Vietnam Living Standard Survey
VND	Vietnamese dong (15,000 VND = 1 US\$ in 2002)
VWU	Vietnam Women's Union

I. Introduction

Poverty alleviation is one of the most important objectives of developing countries. A promising strategy to reach this objective seems to be access to credit for the poor, so that new opportunities can be created to improve incomes. Micro finance programmes, which are specifically targeted on the poor, constitute a major tool for improving the standard of living without creating dependency and encourage them to take part in the economic process.

The concept of micro finance is not new. Its origin lies in the numerous traditional and informal systems of credit that have existed in developing economies since centuries. Many of the current micro finance practices derive from community-based mutual credit transactions that were based on trust, peer-based non-collateral borrowing and repayment.

Non-governmental organizations (NGO) and international donor organizations see micro finance as a mean for providing more efficient aid to poor families in rural areas. The money allocated by governments and donors to specialized intermediaries can be transformed into small credits extended to the poor, allowing them to develop economic activities. Credit is not regarded as an input but rather as an engine for growth.

In Vietnam the importance of micro finance in the fight against poverty is recognised by the government. In the philosophy that poor people should have equal access to credit, the state even created a special bank with a mandate to provide credit for the poor. In the last decade, all major multilateral and bilateral donors and numerous NGOs, active in Vietnam, have been involved in micro finance programmes.

For Belgium too, micro finance is an important tool in its strategy for poverty alleviation. Belgium finances several projects with a micro finance component in Vietnam. On June 9th and 10th 1998, the Belgian Administration for Development Cooperation (BADC) in Hanoi, organized, in collaboration with the Viet Nam Women's Union, a Workshop on "Projects with a Credit Component in South-East Asia". During this workshop, field actors of development cooperation projects in South-East Asia were brought together to share experiences and reflect on ideas. The majority of such programmes in the region, supported by Belgium, were represented. They included bilateral, multilateral, NGOs and cooperation between university programmes. Progress was evaluated and plans were defined.

In this study micro finance in Vietnam will be reviewed and the evolution of 3 of the projects presented during the workshop of 1998, will be monitored and discussed:

- The Vietnamese – Belgian Credit Project: “Strengthening of the institutional capacity of the Vietnam Women’s Union to manage Credit and Savings Programmes for rural poor women” – Phase I, hereinafter called "the VBCP project"
- “Participatory Watershed Management in Hoanh Bo District, Quang Ninh Province” – Phase I This project, hereinafter called "the FAO project"
- “Development of Dairy Support Activities in Southern Vietnam” project, hereinafter called "the Dairy project"

All three projects have been financed by the Belgian Government. The VBCP project and the dairy project are bilateral projects between Belgium and Vietnam and have been implemented by BADC and from April 2000 onwards, by the Belgian Technical Cooperation (BTC). The FAO project has been implemented by the Food and Agriculture Organization (FAO). The information of the case studies is based on field visits, project documents (activity report, final reports, evaluation reports,...) and discussions with project staff and beneficiaries.

1. Definition

Micro finance is the provision of a broad range of financial services such as deposits (savings), loans, payment services, money transfers and insurance to poor and low-income households and their micro-enterprises.

Micro finance goes beyond the access to and the distribution of money. It enters into the deeper issue of how money is used, invested and how savings are done. Micro finance is even more than the supply of financial services. It is a way to give people access to new opportunities. Together with the ability to increase their income, they receive information and training and learn how to manage their money. Micro finance therefore also encloses issues as: organizational and operational aspects, leadership development, trust building, small enterprise management, education and information transfer. Empowering the people improves their self-confidence and will make them feel more confident to enter into the economic, social and political life of the society.¹ These non-financial services define the specific character of micro finance and make micro finance programmes so valuable.

2. Principles and best practices of micro finance

- **Objectives**

The general objective of most programmes is to tackle poverty but every programmes has its specific objective(s). Some of the programmes are exclusively concerned with savings and credit. Others have a S&C component as part of a package (for example: projects of which the S&C scheme is one of the activities to reach the specific objective), which sometimes is used as an entry point for promoting other activities (for example in health and family planning, agriculture extension,...). It is important in a programmes to define the objectives very clearly.

- **Target**²

Targeting is directing the credit programmes exclusively on beneficiaries of the programmes, depending on the specific objectives of programmes. It is important to identify clearly who is part of the target population, to determine exactly who is eligible to participate in and benefit from the credit programme. Targeting is essential for creating and maintaining a good credit discipline, which is a condition for a programmes' sustainability.

¹ European Commission, Micro finance. Methodological considerations, December 2000, p.5.

² Gibbons David and Wayne Temlinson. The Grameen Trust, Draft Training Manual on Cost-effective Targeting, June 1995.

The provision of micro credit is mainly targeted on 'poor' and non-bankable people, i.e. those people who have no possibilities to qualify for traditional bank loans. Two categories of poor people can be distinguished. The so-called 'entrepreneurial poor' are those people who have the capacity to set up income generating activities that will eventually increase their income. The 'non-entrepreneurial poor' need direct assistance of by a social network to survive. They have no capacity to start economic activities because of a lack of personal skills or because they are so destitute that they are in no position to develop any meaningful economic activity in their living environment.³ Micro finance is targeted on the entrepreneurial poor.

Women are a popular target group for micro finance programmes.⁴ This is due to several reasons:

- Worldwide women have shown a greater spirit of enterprise, usually take their business very seriously and make an essential contribution to the economy of developing countries. Consequently loans to women generally result in a higher repayment rate, compared to loans attributed to men.
- Women have a much more limited access to credit because they don't have any assets to use as collateral for a loan, since assets or land are usually registered on the name of the husband.
- The income provided by mothers generally has a bigger impact on the well-being of the entire family unit (nutrition, education,...).

Micro finance doesn't only improve the women's financial situation, but there is also a socio-cultural (their position in the family and society), psychological (increased self-esteem) and political (more decision making power) impact to be noticed. In this respect, micro finance is a powerful tool for improving the status of women.

- **Small credit and savings**

Micro credit is typically the provision of very small loans that are repaid within short periods of time. In general, the loan size is decided based on the financial capacity of the borrowers to pay back the credit. A popular and successful philosophy in credit and savings schemes is to start with a small amount of credit for a first loan cycle in order to check the creditworthiness of the borrower and to provide an opportunity for the borrowers to practice a business with a small investment amount. With a second loan demand, the loan amount can be bigger because at that moment, they have learned how to manage their investments and they have given prove of being creditworthy and reliable. The loan period is mainly based on the type of investment and the capacity to pay the instalments. A savings component gives poor people the possibility to deposit very small amounts of savings and helps them to accumulate a lump sum.⁵

³ UNDP, Micro finance and anti-poverty strategies: a donor perspective.

⁴ BADC, Draft policy document and guidelines concerning the Promotion of Micro-credit in developing countries.

⁵ Rutherford Stuard, The Poor and their Money, January 1999.

- **Group system**

The compulsory collateral is one of the main obstacles of poor people to have access to the formal banking and lending system. Micro finance programmes typically provide credit to households who have few assets that can be used as collateral. Non-formal micro finance systems usually apply the "group system" as an alternative to have some kind of guarantee to ensure repayment.

The borrowers are organized in solidarity groups, which are the most decentralised level of a micro finance system. The nature of these groups varies between schemes. They are composed of people from the same hamlet, friends, or people from the same peer group.

The group members will meet regularly (in most schemes this is weekly or monthly). During those meetings the proposed loan use of new borrowers will be screened and it will be decided in the group whether the proposals are acceptable. Once the loan has been given to a borrower, the group will follow up the profit of the investment made. Repayments are not collected individually, but per group. If one borrower can't pay, the group has to take care of the repayment by dividing the debt among the group members. New loans depend on good repayment rates of the entire group, so that there is an incentive to timely reimburse instalments of all group members. This leads to social pressure between group members and functions as a social collateral. In many cases prospective members are asked to form groups by themselves. By making their own selection of trustworthy individuals, the chances of having to contribute for other group members diminishes and repayment rates increase.

The group system not only provides a guarantee for repayment, but also reduces the administrative costs of the scheme. In most cases, the function of group leader rotates yearly. In this way different members learn how to take the responsibility of leadership, a responsibility they would never have when lending at a formal bank. The position of group leader gives them the capacity to participate in the community and to increase their self-esteem by taking an active part in the social activities. Solidarity groups make the people more involved and responsible and form a channel for the exchange of information, assistance and advice. Mutual assistance between group members is an easy and cheap method for the dissemination of knowledge and information.

- **Services**

Complicated and time-consuming procedures to obtain loans from the formal sector are considered as a major obstacle for poor people. In many developing countries 'cheap loans' schemes at subsidized interest rates have been introduced by the formal sector intended to reach the poor. But in practice, these often don't reach the poor. Low-income entrepreneurs have shown willingness and ability to pay interest rates higher than commercial banks for services that fit their needs. It seems that the poor value access to credit more than the low cost of credit. If people need money, they generally need it urgently. Just because of the easy access, people often tend to find informal moneylenders more

convenient and flexible than formal commercial or state institutions, even if they charge much higher interest rates.

Therefore, micro finance programmes should be easily accessible. The credit should be 'nearby' and easy and quick to get. But not only the access to credit is important for the borrowers. What they really need is a combination between financial and non-financial services. These non-financial services should include information and training.

To reach sustainability, a micro finance institution should attract new clients and maintain the commitment and participation of existing clients. This means that the financial services being offered must be designed to meet the needs of the target group. No identical replications of existing schemes are advisable. A successful experience can be a total failure if copied into another context. To optimise a programme, a participatory input from the target group is a necessity. If the borrowers cannot identify themselves with the scheme, their commitment will be very low.

The schemes should have possibilities for personalized services. Not all clients will progress at the same speed. There should be different loan and savings products for clients of differing abilities and with different demands. A scheme must be a flexible instrument that easily can be adapted to local circumstances and demands. Loan and saving products should be checked regularly to see if they still meet the demand and if necessary new loan or saving products should be introduced.

Programmes and organizations providing credit to low-income groups have to find the balance between the quality and quantity of credit, the capacity of the poor to utilize the credit in an efficient way, the local situation and existence of other formal or informal schemes in the region. After the project, the donor agency will end its input of finances and at that moment the programme should be self-reliant.

- **Savings**

The integration of a saving component in a micro finance scheme has different functions:

- By linking a saving scheme to the credit scheme, people learn the principles of savings and money management, and acquire the habit of saving. Savings are a safe guard for households recovering from poverty to face unexpected events and dramas.

- Savings are a relatively cheap source of funds for a scheme, as the interest rates to attract savings are usually less than those that have to be paid to borrow funds commercially. With these extra funds, new borrowers can be attracted, who in their turn generate capital by depositing savings. The accumulation of capital for loans is of major importance for the sustainability of a programme. There is a danger that introducing a credit model without a saving mechanism may induce undesirable dependency on external funds.

- Since there is a higher motivation of the borrowers to pay back loans that are partly financed by the savings of the people of the community, a bigger involvement and as a consequence, a higher repayment rate can be expected.

- Savings contribute to the accumulation of capital in a community.⁶

The savings component of a scheme can be compulsory or voluntarily. It is important that saving schemes are trustworthy and easily accessible. Regulations and conditions (e.g. interest rates) should be clearly defined.

- **Interest rates and fees**

The interest rate has to be high enough to cover all costs.

The nominal interest rate is a public rate announced by any lending institution. However, the nominal interest rate is often quite different from the effective rate, which is the actual rate a borrower has to pay for his/her loan, including the operating costs, the financial cost (= cost of fund), service fees and loan loss provision. This could result in a different real interest rate, to which any lending institution would pay a careful look.

$$\text{Real interest rate} = \text{Effective rate} - \text{inflation rate}$$

To ensure the viability of the scheme, the real interest rate should be a positive figure. To achieve this, there are ways to increase the effective rate on loans by taking acts on those costs that the borrowers have to pay.

Micro finance loans are paid in periodic instalments. With each principal repayment, the interest is paid as well. When using a declining interest rate, the monthly interest is calculated on the outstanding balance. This means that the interest paid will decline during the loan cycle.

With a flat interest rate, the amount of the monthly interest to be paid is fixed, not taking into account what the outstanding balance of the loan is. This system is easier to calculate the repayment schedule and is easier to understand for the borrower. But in fact, the borrower pays more interest than quoted in the nominal interest rate.

To ensure viability, the minimal sustainable interest rate should be followed according to the following formula:

$$\text{Interest rate} = \frac{\text{Operating cost rate} + \text{financial cost rate} + \text{loan loss rate} + \text{capitalization rate}}{1 - \text{loan loss}}$$

Each of the above factors is presented as a percentage rate, calculated per average outstanding loan balance.

Operating costs include staff salary and allowance, renting, depreciation, training costs, technical support, management costs etc. In an effective micro finance institution, operating costs normally account for between 10 to 25% of average outstanding loans.

Loan loss provision is defined as part of unrecoverable loan. The loan loss rate can be much lower than a late repayment rate: the former one indicates actual loan written-off and the latter shows that loans are not repaid in time, which means that a big part of this outstanding loans can be recovered. Previous experience of an institution is an important factor in forecasting the rate of future loan loss. A micro finance scheme with a loan loss rate of more than 5% is difficult to be sustainable. For an efficient scheme, this rate should be around 1% - 2%.

Financial costs: in many donor projects and government programmes, part of the costs are subsidized. With the provision of a revolving fund, the cost of fund is zero. However, inflation and devaluation in money exchange should also have to be taken into account.

Capitalisation rate: this rate shows a real net profit a micro finance institution pursues. In fact, such an accumulation of profit is important. The capital fund a scheme can borrow safely from outside, is limited by the equity of the institution. The best way to increase the equity are retained profits. It is up to the management board to decide upon the rate of capitalization. For a long-term development, a capitalization rate should count for minimum 5% - 15% of average outstanding loans.

- **Management Information Systems**

Access to timely, accurate, and detailed information on the overall performance of a micro finance institution is required, if sustainability and self-sufficiency are to be reached. Therefore, Management Information Systems (MIS) should be introduced in every programme, which is the piloting tool of the financial institution. They can be manual, computerized through spreadsheet or computerized through advanced computer-programme software. A cost-effective MIS should generate both financial and operational information.⁷

⁶ Devereux Stephen and Henry Pares, Credit and savings for development, 1989, p. 16.

⁷ Gibbons David and Jennifer Meehan, The Microcredit Summit's Challenge: Working Towards Institutional Financial Self-Sufficiency while Maintaining a Commitment to Serving the Poorest Families, June 2000, p.13.

Basic clients' profile data and financial reporting on the saving and credit activities are important instruments to monitor the scheme's performances. These data are transformed in ratios which indicate the performances. They identify problems, help find solutions and serve as an 'early warning' to allow the management team to react to problems in quick and effective way. Several measurement systems are used. Most schemes follow the PEARLS system, CAMEL system or the prudential ratio of CGAP system. These 3 systems basically contain the same main categories of indicators: financial sustainability ratio, operating efficiency ratio and portfolio quality ratio.⁸

The most commonly quoted indicators are:

Financial Sustainability Ratios:

- Return on Performing Assets
- Financial Cost Ratio
- Loan Loss Provision Ratio
- Operating Cost Ratio
- Imputed Cost of Capital Ratio
- Donations and Grants Ratio
- Operating Self-Sufficiency
- Financial Self-Sufficiency

Operating Efficiency Ratios:

- Cost per Unit of Money Lent
- Cost per Loan Made
- Number of Active Borrowers per Credit Officer
- Portfolio per Credit Officer

Portfolio Quality Ratios:

- Portfolio in Arrears
- Portfolio at Risk
- Loan Loss Ratio
- Reserve Ratio

⁸ European Commission, Microfinance. Methodological considerations, December 2000, p. 93.

- **Administrative efficiency**⁹

Well-managed micro finance institutions have administration cost rates ranging from 15% to 25%, regardless the lending methodology. These include aspects such as travel costs, reporting system, equipment maintenance and salaries.

Salary and salary-related expenses usually represent a significant bulk of total administrative costs. Staff must perform as productively and efficiently as possible, while maintaining the quality of their work. Managers should carefully monitor and measure field staff performance and productivity. Two basic measures are consistently employed to monitor the efficiency of the micro finance institutions field staff:

- average number of active loan clients per field staff
- average loan portfolio per field staff

Worldwide the best practice indicator for micro finance institutions ranges from 300 to 500 clients per field staff member, irrespective of the lending methodology (individual, solidarity group, village banking). The average loan portfolio per field staff is more difficult to generalize as it depends more upon the lending methodology used, the level of poverty of the borrowers and the local operating environment.

- **Progressive lending**¹⁰

To reach sustainability and effective results on poverty reduction, a programme should increase the outstanding loan size and client growth. It is necessary to ensure that an as great proportion of available funding as possible reaches the hands of the poorest.

But they have to be able to maintain a strong loan portfolio quality (measured by portfolio-at-risk). Progressive lending, which provides for increasing maximum loan sizes as borrowers progress from one loan cycle to another, is critical for both poverty-reduction and the attainment of self-reliance. But the maximum loan size of subsequent lending cycles should be linked to the repayment performance in the existing cycle. The subsequent loan size declines by a pre-determined amount for each dropped repayment and after a number of dropped repayments, the borrower is no longer eligible for a subsequent loan.

⁹ Gibbons David and Jennifer Meehan, *The Microcredit Summit's Challenge: Working Towards Institutional Financial Self-Sufficiency while Maintaining a Commitment to Serving the Poorest Families*, p. 10-11.

1. Analysis of Poverty in Vietnam ^{11 12}

Vietnam is considered as a poor country. Based on international standards, 37% of the population in Vietnam lived below the poverty line in 1998 (defined as less than 128 US\$ per capita per year in 1998). The national poverty line determined by the Ministry of labour, Invalids and Social Affairs (MOLISA) of Vietnam is lower and defined as the income equivalent of buying 15 kg, 20 kg and 25 kg of rice per month in mountainous and remote, rural and urban areas respectively. However remarkable progress was obtained in the 90's, reflected in rising per capita expenditure and in widespread reports of improvements in broad well being. The proportion of people with per capita expenditures under the total poverty line has dropped drastically from 58 % in 1992/93 to 37 % in 1997/98 (VLSS 1993 and 1998). The number of people below a 'food poverty line' has also declined from 25 % to 15 %. This indicates that even the very poorest segments of the population have experienced improvements in their living standards between 1993 and 1998.

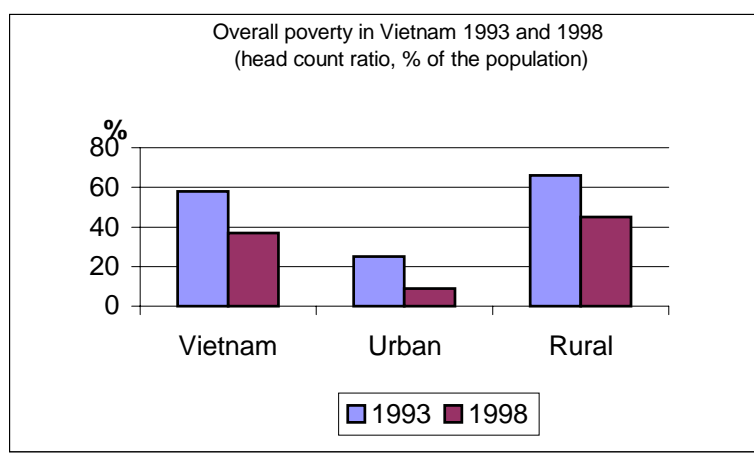


Figure 1: Poverty reduction during the 1990s

An improvement in social indicators (such as education, child nutrition, adult nutrition, access to infrastructure and ownership rates of consumer goods) during the period 1993 - 1998 can also be seen. Several Participatory Poverty Assessments (PPA), clearly show that the poor themselves feel that their living standards have improved in recent years.

Despite these major improvements, Vietnam remains a poor country with per capita income of around US\$ 380 and a Human Development Index (HDI) value of 0.682 (in 1995 the HDI value was 0.611).¹³ Figure 2 indicates the HDI ranking of the Asian countries.¹⁴

¹⁰ Gibbons David and Jennifer Meehan, *The Microcredit Summit's Challenge: Working Towards Institutional Financial Self-Sufficiency while Maintaining a Commitment to Serving the Poorest Families*, p. 8-17.

¹¹ *Attacking Poverty, Vietnam Development Report 2000*, p. 4-17.

¹² *National Human Development Report 2001, Doi Moi and Human Development in Viet Nam*, p. 27-42.

¹³ UNDP, *Human Development Report 2001*, p. 140-143.

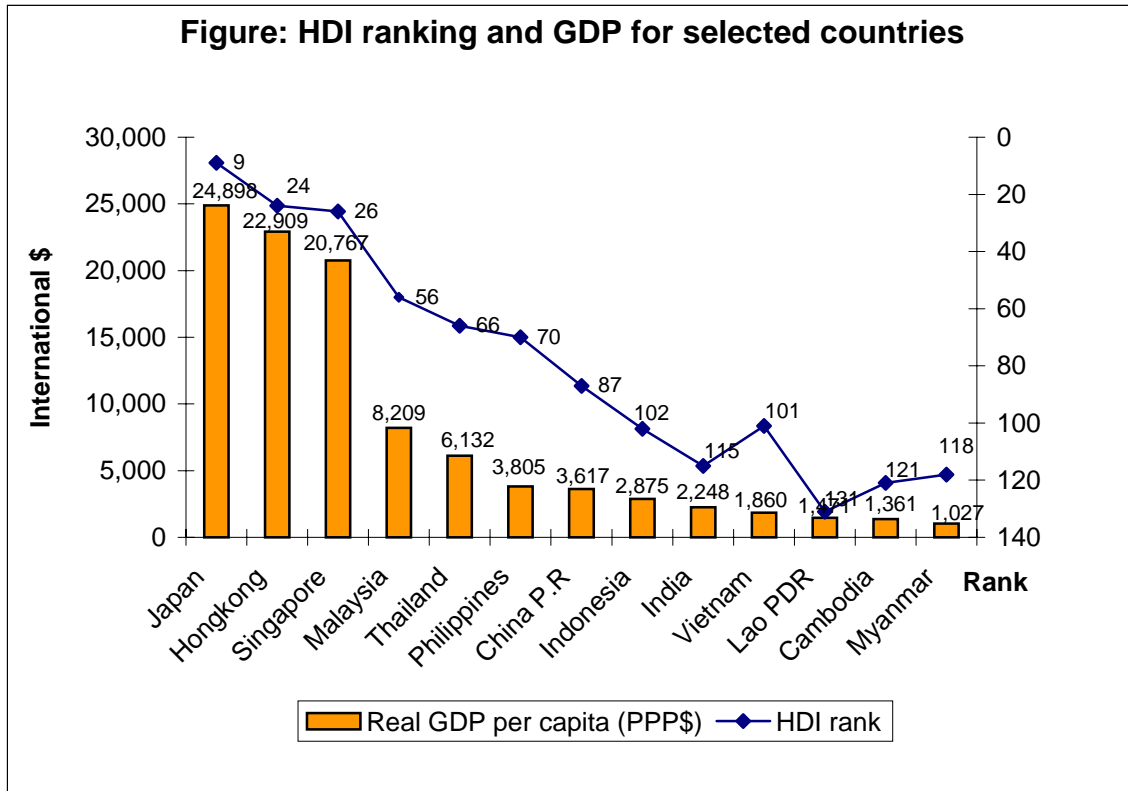


Figure 2: HDI ranking for selected countries

Poverty remains a largely rural phenomenon, with 90 % of the poor living in rural areas, and with 45% of the rural population living below the poverty line. The drastic gains in poverty reduction in Vietnam between 1993 and 1998 remain very fragile. A large proportion of individuals are clustered around the poverty line. This means that it would only take a small reduction in per capita consumption to force those now living just above the poverty line back below it. If the ‘vulnerable’ are defined as the currently poor plus those who are near-poor within a line 10 % above the poverty line, then fully 45 % of the population should be considered vulnerable. Several factors come forward as critical in explaining people’s vulnerability, most remarkably dependence on little variety of activities and sources of income. The rural poor are especially vulnerable to risks because they usually lack the assets or access to credit that provide protection against shocks.

To succeed and to ensure that poverty reduction gains are sustainable and not reversed later, Vietnam needs to deal with the vulnerability of poverty: both by assisting currently-poor households to escape from poverty and by protecting households from trends and risks which could force them below the poverty line again.

As reflected in the Socio-Economic Development Strategy 2001-2010, the Interim Poverty Reduction Strategy Paper (I-PRSP) and the Hunger Eradication and Poverty Reduction Strategy (HEPR-strategy), the Government of Vietnam aims to reduce absolute poverty drastically (from 17 per cent in early

¹⁴ National Human Development Report 2001, Doi Moi and Human Development in Viet Nam, p. 30.

2001 to below 10 per cent in 2005). Given the role of finance for poverty reduction and hunger alleviation, the Government of Vietnam is, in the framework of the HEPR-strategy, trying to improve household access to financial services by the provision of subsidized credit, especially for poor and low-income households.

2. Doi Moi^{15 16 17}

Before the year 1986, the state controlled all land, natural resources and productive activities in Vietnam. It allocated equipment and raw materials for production and organized agriculture under a collective system. It managed the distribution of agricultural products and consumer goods for personal consumption. In the planned economy, market and prices were not important since prices were set by the state planning agency at subsidized levels.

This centralized system of management led to severe economic and social problems during the '70 and '80s. In response the 6th Party Congress of the Vietnam Communist Party adopted in 1986 a reform policy in order to move towards a market economy. This reform process, called doi moi, led to the liberalization of an economic system that had been entirely centrally planned since the mid 1950s. The de-collectivisation process in agriculture resulted in the re-establishment of private land use rights and the re-emergence of private farming and private traders in rural areas.

With the adoption of the Land Law in 1988 (Resolution 10), farming in Vietnam is based on a family farm basis again, and no longer on agricultural production cooperatives. However, private ownership of agricultural land has not been introduced and all land remains State property. Since 1988, land can be rented for long-term periods (30 to 50 years) in exchange for paying a tax. In 1993, the Land Law was revised and now land use rights can be exchanged, transferred, rented, inherited and mortgaged. However, in many cases land is traded without the official documents, commonly called "Red Book" or "Red Certificate". As a result, it turns out that people who do have assets, in fact cannot use them as collateral.

The country has known a rapid transformation since the adoption of the doi moi policy. Between 1992 and 1998 the average annual GDP growth rate in Vietnam was 8.4 percent. The economic liberalization in agricultural production resulted in a sharp increase in production output. While up to the 1980's Vietnam used to be a food importing country, in 1999 it was the second largest rice-exporting nation in the world. Also the non-farm and wage employment has grown rapidly during 1993-98. A growing economy like Vietnam's provides new employment opportunities for its workers. They gradually move out of agriculture into industry and services. Although generally over the whole of Vietnam, the share of agriculture in output and employment is declining, for those living in rural areas, agriculture

¹⁵ Wolz A., The Transformation of Rural Finance Systems in Vietnam.

¹⁶ Kirsch and Ottfried, Vietnam: Agricultural Cooperatives in Transitional Economies.

¹⁷ Attacking Poverty, Vietnam Development Report 2000, p. 42.

continues to be their main form of employment. Many rural households combine several different forms of activities and derive incomes from several different sources.¹⁸

The question is whether this spectacular growth in agricultural incomes can be expected to continue in the future.¹⁹ And to what extent were the gains that agricultural producers have benefited from over the last five years, a result of a “one-shot” adjustment associated with the move to a market economy?

Some of the problems are:

- Despite the birth control programme (max. 2 children per family and 5 years between the first and the second child), the population of Vietnam will keep on growing. A lot of the good agricultural land has already been allocated and only the lower quality land is left over for the new farm households. This results in over-exploitation of the land and even puts its sustainability at risk.
- The lack of access to credit that provides protection from risks and shocks.

3. Rural finance^{20 21}

Before 1988, Vietnam was characterized by a mono-tier banking system (comprising the State Bank of Vietnam and two specialized institutions, namely the Bank for Investment and Development and the Bank for Foreign Trade). There was a state monopoly over finance with a widespread subsidy system with negative real interest rates. This led to a bank crash. Consequently a two-level system has been developed, consisting of the State Bank of Vietnam (SBV) and four state-owned commercial banks including the Vietnam Bank for Agriculture and Rural Development (VBARD). In 1995 the Vietnam Bank of the Poor (VBP) was established, a non-profit bank with focus on poverty alleviation. In the addition joint-venture banks, joint stock banks and People's Credit Funds (PCF) have been created. For rural households three main institutions are the VBARD, the VBP and the PCFs.

However, the present situation of the rural finance system can only be fully understood if one takes note of the development of the rural credit cooperatives up to their collapse in the early 1990s. From 1956 on, several Traditional Credit Cooperatives were set up (in the South these were established in 1983). Their main purpose was to gather small deposits and provide credit to individuals, farm households, small businesses and production cooperatives.²² Although they were set up as local financial intermediaries on behalf of the SBV, in reality they were established within small communities and managed by local People's Committees. Actually the term cooperative did not describe a form of mutual self-help, but rather reflected an operation, which was organized by the administration. Most Cooperatives have fallen prey of the financial reforms. As rural collectives went out of business, their loans from credit cooperatives became non-performing. There was no system of reserve assets or deposit insurance and the SBV did no longer automatically refinance the credit

¹⁸ Attacking Poverty, Vietnam Development Report 2000, p. 41- 57.

¹⁹ Attacking Poverty, Vietnam Development Report 2000, p. 53-57.

²⁰ Wolz A., The Transformation of Rural Finance Systems in Vietnam.

²¹ Kirsch and Ottfried, Vietnam: Agricultural Cooperatives in Transitional Economies.

²² Already in the early 1930s about 5,500 rural credit cooperatives had become operational, another 2,000 were set-up during the early 1980's. In the late 1980s there were 7,180 credit cooperatives.

cooperatives as it used to do before the banking reform of 1988. Most of the rural credit cooperatives collapsed. Small private enterprises – in many cases newly established – were particularly affected by the collapse of the credit. At that time these cooperatives were their only source of formal credit.

The collapse of the credit cooperatives had a major effect on the people's faith in the financial system, including the formal banking system. Many people withdrew their deposits to buy gold and dollars. Until now people have a profound mistrust in the banking system.

4. Main actors in Credit for the poor in Vietnam

Chart 1 gives an overview of the micro finance actors in the Vietnamese Finance System.

4.1. The Formal Finance System

In 1999, as much as 5.9 million households had access to formal financial institutions, of which 2.7 million households were poor and low-income households.²³

4.1.1. The Bank for Agriculture and Rural Development (VBARD)²⁴

The Vietnam Bank for Agriculture and Rural Development (VBARD), before called The Vietnam Bank for Agriculture (VBA), was created in 1988 out of a department of the State Bank of Vietnam (SBV). Its focus lies on financing all types of enterprises in rural areas. The VBARD has become the largest supplier of institutional micro finance to rural households: the share of rural households having access to credits, managed by VBARD, increased rapidly from 9% in 1992 to about 30% in 1994.²⁵

Although the VBARD is by far the most important financial institution in the rural area, it is still underdeveloped. Some major disadvantages are the following:

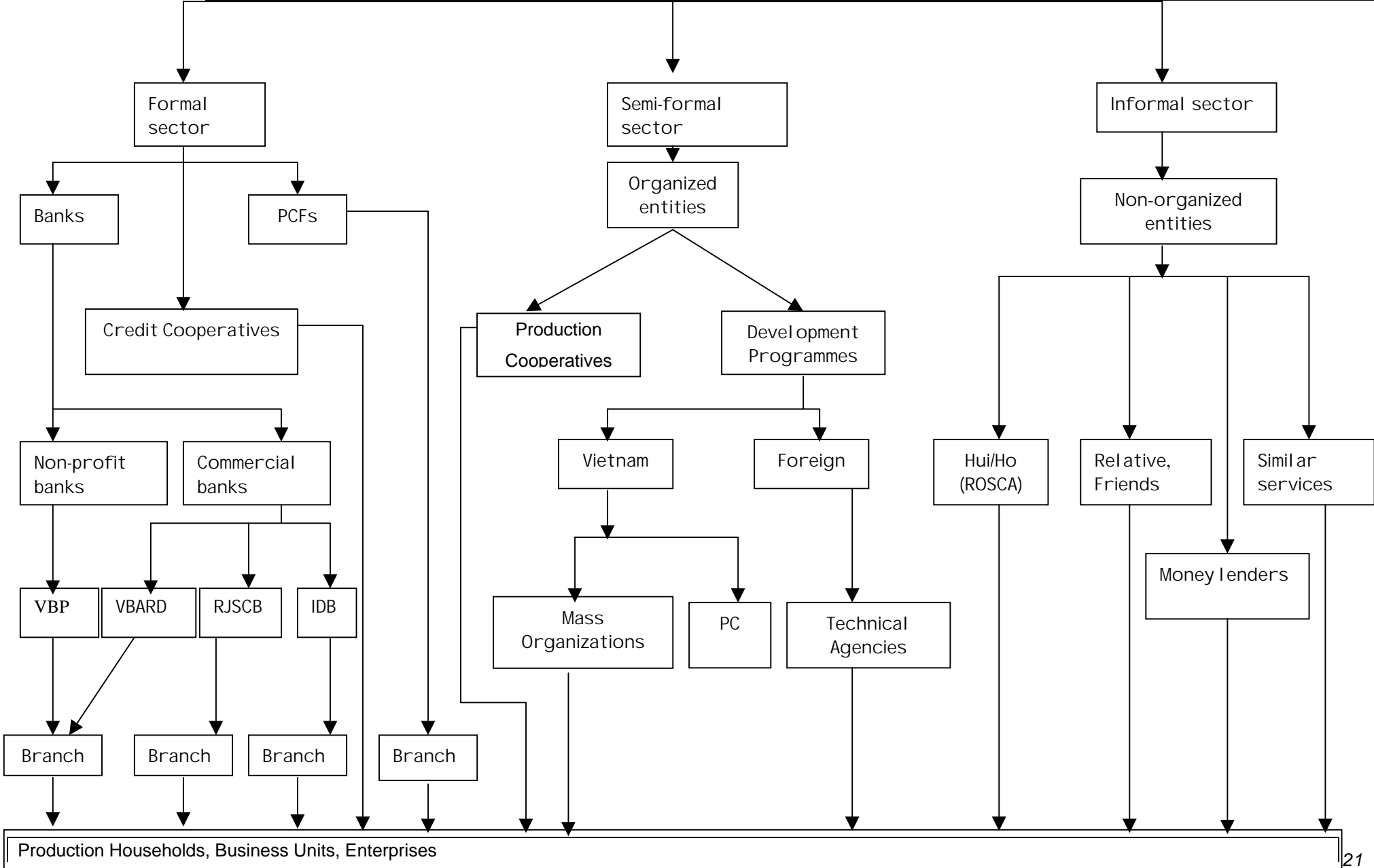
- Loan size: According to the bank's definition, loans below 5 million VND are considered "small" and represent about 50%. In table 1 it is shown that loans of 1 million VND, which represents already a large sum for the poor, represent only around 16 % of the total amount of loans allocated by VBARD.

²³ DFID and SBV, Micro finance in Vietnam: micro finance policy issues and "lessons learned" in Vietnam, p. 5.

²⁴ DFID and SBV, Micro finance in Vietnam, p.36.

²⁵ Wolz A., The transformation of Rural Finance Systems in Vietnam, p. 5.

Chart 1: Overview of Micro Finance actors in the Vietnamese Finance System



	Loan Size ('000,000 VND)					Total
	<0.5	0.5-1	1-3	3-5	>5	
share of customers %	5	11	29	33	22	100
share of total loans %	0.6	2.3	15.6	34	47.5	100

Table 1 : VBARD customer structures by loan size, 1998.

- Collateral: VBARD claims collateral when deciding about a credit application: residential property, movable assets, goods and land right use are accepted as collateral. However only about 30 % of households have "Red Certificates" of land use rights, so that the majority of rural households are unable to respond to the demands of the VBARD linked to allocating a loan.²⁶
- Banks prefer to provide credit to state-owned enterprises (SOEs). The credit amounts are much larger, and therefore, handling costs relatively small. Risks are low because in case of default the government is expected to come to their rescue.
- From the clients' point of view the procedures in getting a loan from VBARD are quite complicated. It is costly (as well in time as in money) to get the necessary paper work done when submitting the credit application. Often credit can only be asked for specific agricultural investments but not for those activities, which are of priority to the borrower.

4.1.2. Vietnam Bank for the Poor (VBP)

The state-owned VBP was established in 1995. In the framework of the HEPR, it was the intention that the approaches of VBARD and VBP complemented each other in their contribution to hunger eradication and poverty alleviation in Vietnam.

The VBP is institutionally merged with the VBARD and staffed by personnel from VBARD. It officially started operating in 1996 to provide subsidized credit to poor households. Its aim is to reduce poverty by providing loans with low interest rates to the rural poor, who do not qualify for individual loans because of limited ownership of potential collateral. The VBARD and VBP branch network is present at district level and to a limited extent at commune level, through visits of loan officers to communes on a weekly basis. This limits their outreach to the poorer, remote, rural communes. Up to 1999, over 2.3 million poor households obtained loans for a total amount of about 276 million US\$.²⁷

The VBP closely cooperates with local organizations. Local People's Committees usually help VBP identify who are the poor. Social mass organizations at villages like the Women Union and the Farmer Association help the bank monitor the loans. The borrowers don't need a collateral, but in reality it is the social mass organization, which provides a Guarantee Fund to the bank. If the borrowers do not repay the loan, the bank will take a part of the Guarantee Fund. To ensure repayment, the mass organizations organise the borrowers in joint-liability groups.

²⁶ DFID and SBV, Micro finance in Vietnam: institutional and legal structure of micro finance in Vietnam, p.12.

²⁷ DFID and SBV, Micro finance in Vietnam, p. 8.

4.1.3. People's Credit Funds (PCFs)

After the collapse of the rural credit cooperatives, SBV has been entrusted to reorganize the system of rural credit cooperatives. The result was the development of a network of People's Credit Funds (PCF). PCFs have been created in nearly all provinces of Vietnam (limited coverage in the Northern Mountainous areas). One of the most important objectives was to restore public confidence in the formal rural finance system. For psychological reasons, the term 'cooperative' has been deliberately excluded from the name of this newly established finance institution. The PCF-system has been set up as a member-owned organization, which aims at mobilizing savings from its members. It has to be managed according to the economic principle of cost covering; no 'easy money' will be available (although they did had the back-up of SVB for several years).

PCFs are shareholding banks and do not focus on the poor. 15 potential founding members are required to set up a PCF. These persons have to be better off since for setting up a PCF a base capital amounting to 50 million VND is required and each founding member has to buy minimum shares amounting to 3.3 million VND. Once the PCF is registered it aims at recruiting more members. Those who want to become member have to buy a share of 50,000 VND, an amount too big for the poor.²⁸

The PCF-network has been established predominantly in those areas which are economically better off and better developed in infrastructure. Therefore the PCF-system only has a limited role to play with respect to reducing rural poverty. Its major accomplishment will be to provide a viable rural finance system to farm and small entrepreneurial households to stimulate economic development, which indirectly contributes to poverty eradication.

PCFs are situated close to their clients, have relatively fast loan-approval processes and have the potential to provide competition in the rural financial sector.

4.1.4. Main problems affecting the Formal Finance System

The two Government-owned banks (VBARD and VBP) are the major sources of formal credit for rural households. Rather than functioning as self-sustainable independent banks, they are mainly used as a channel to provide formal credit to farm and poor households in the rural areas. Although the number of households obtaining credit has increased sharply since the establishment of VBARD, VBP and PCFs, there are still a large number of poor households unable to get access to formal institutional micro finance.

Despite general improvements, the policy environment for micro finance in Vietnam remains unfavourable for sustainable growth in micro finance operations.

4.1.4.1. Interest rate structure

Aiming at providing the poor with a preferential treatment, the Government has tried to make cheap credit available in order to assist the poor to develop their own production and business operations.

The SBV determines the interest rate for credit. This means that banks are not able to set interest rates that will cover the costs of funds, operating costs and risks. Since August 2000, the mechanism of base interest rates has been applied for all formal financial institutions, in stead of a ceiling interest rate. This liberalization of the interest rate gives financial institutions a little more freedom in determining the rates on lending and saving. However, the base interest rates are not flexibly adjusted to market prices, so the effects of base interest rate are almost the same as that of the ceiling interest rates mechanism.

With an interest rate so low and generally high operating costs, it is impossible for a bank to become self-sustainable. Because operating costs of bigger loans are rather low compared to loans of small amounts, *the provision of financial services to small rural borrowers is no longer a commercially viable option for VBARD.*²⁹ It can be argued that the policy of determining interest rates, which is supposed to stimulate economic and agricultural growth, is actually limiting the access to credit and increasing credit costs for farmers and rural entrepreneurs. For the rural financial institutions like VBARD, VBP and PCF the determined interest rates is a constraint for a sustainable expansion of their services.

Interest rate of loans has been held at 1% per month for VBARD and at 0.7% per month for VBP, which is lower than the interest rate charged by non-state owned commercial banks. Due to this low interest rate, it is difficult to raise funds. Therefore, they have to rely on borrowed fund from the Government. Although the VBP has become the major source of formal loans to the poor households, at current rates of lending and institutional structure, the bank cannot afford financial nor institutional sustainability. Basically the VBP has been a channel to provide subsidized credit to the poor.

It is generally recognised that the mechanism of subsidised credit undermines the sustainable development of micro finance. Low interest rate leads to demand exceeding the loan supply. Consequently not everybody who wants a loan can get one. Obviously banks prefer to select the least risky borrowers (such as those with good collateral) and prefer to give larger loans, which implies lower administration costs. However there is also neither guarantee nor a protection against corruption.

In the long-term the Government intends to gradually improve the ability of the poor, especially poor women, to access the formal credit system by simplifying the procedures rather than applying preferential credit policies.³⁰

²⁸ PCFs plan to include poorer areas after they have established a strong and sustainable credit union network.

²⁹ BADC and VWU, Proceedings of the Workshop, June 1998, p. 45-47.

³⁰ Comprehensive Poverty Reduction and Growth Strategy, January 2002.

4.1.4.2. Saving Mobilization

Formal micro finance institutions have no serious attitude and effort to mobilize small savings. In the government banks, savings mobilization instruments have been poorly designed. It is impossible to offer attractive interest rates to savers if interest rates on lending are limited. Taking the psychological effects of the collapse of the cooperatives in mind, the low interest rates on lending, also make the rates on savings rather low, and in the viewpoint of many people, not worth the risk of depositing their money.

From the point of view of the financial institution, interest rate margins do not create incentives to expand savings services to the poor and low-income households. For some financial institutions, small saving deposits are not accepted. For example, the minimum deposit accepted by VBARD branches is 50,000 VND, and sometimes even 100,000 VND. As a result, rural micro finance institutions must rely on savings from urban areas rather than small savings in rural areas. VBARD deposits are overwhelmingly urban with only a very small proportion coming from rural households. VBP deposits make up only 8 %of its total funds.³¹

4.2. The Informal Finance System

Although the knowledge about informal finance systems in Vietnam is weak and primarily based on anecdotal evidence, informal sector lending seems to remain of great importance in rural Vietnam. Data collected by the VLSS of 1997-98 revealed that 51 percent of credit to farm households were being provided through the informal channel (table 2).³² Compared to the results of the 1992-93 VLSS (where 73% of loan funds in rural areas were provided by private moneylenders and individuals), a significant decrease of the share of credit provided by moneylenders can be noticed: 33% in 1992-93 and 10% in 1997-98.

	number of loans(%)	average loan size ('000 VND)
Informal financial sector	51	1,752.10
money lenders	9.8	2,141.30
Relatives	24.2	1,860.90
ROSCA and other individuals	16.8	1,365.70
formal & semi-formal financial sector	49	3,208.50

Table 2: Number of loans and average loan size by sources

Despite this decline, the results of the VLSS 1997-98 reflect that private individuals remain the most important source of credit for rural poor, in most cases family members, relatives, friends and neighbours. Reasons why there is such a big informal market of credit :

³¹ DFID and SBV, Micro finance in Vietnam: institutional and legal structure of micro finance in Vietnam,. 12.

³² DFID and SBV, Micro finance in Vietnam: institutional and legal structure of micro finance in Vietnam, p. 6.

- As a result of the collapse of the credit cooperatives there is a significant lack of trust of the people in the formal banking system;
- The procedures for access to formal credit are too complicated (too long administrative procedures, collateral,...)

Three major informal financial sources of credit in Vietnam can be distinguished.³³

4.2.1. Relatives / friends / neighbours

Relatives, friends and neighbours are the first sources when seeking for credit. They lend to others at negotiated rates depending on social relationships and reputation. Taking advantage of personal information, relatives and friends in general provide loans without collateral or any other written loan contract. Interest rates are recorded low (neighbours) and in many cases (relatives and close friends) are free. The purpose of the loans is generally for emergency consumption such as illness, funeral and weddings and for the building or repairing of houses. Rarely those loans are used for buying input for production.

4.2.2. Ho/Hui³⁴

Rotating savings and credit associations (ROSCAs) have a very long tradition in Vietnam. Although they exist for many generations already, they have never been recognized officially. Usually these groups are referred to as *Ho* in the North and *Hui* in the South. They are promoting periodic saving contributions, which in turn are rotated as a fund among a limited group of persons who trust each other. Members of these associations come mainly from the same hamlet, and are even organized 'on the spot' between colleagues and friends. The savings and credit can be made either in cash or in kind. In general, membership averages 10-15 persons. Decision on interest rates, membership and loan amounts are made either jointly by all members, by a bidding process or made solely by the organiser. The life cycle of a savings and credit association ends when every participant has obtained once the total fund collected at each turn. Most of the Ho/Hui are set up to bridge short-term needs (sometimes for special purposes such as weddings, funerals or the lunar new year), but they can also be set-up to finance long-term investments.

4.2.3. Moneylenders

Private moneylenders are widespread and seem to be important sources of loan for households. It is usually the rich households with surplus of money and goods in rural areas, who lend money for long-term periods against sometimes very high interest rates. Moneylenders are reported to charge up to an average of 10% per month, which is extremely higher than the rate charged by formal financial institutions. In HCMC the reported rates of interest are even much higher 20% to 30%, even sometimes

³³ Tran Tho Dat, Analysis of the Informal Credit Sector in Vietnam, p. 1-4.

³⁴ Wolz A., The Transformation of Rural Finance Systems in Vietnam, p.16-17.

as high as 70% per month.³⁵ Sometimes the moneylenders are traders who give advances in cash or kind on the basis of the promise to receive or buy the products at harvest time. This last type of lending has been developed during the last years and it can be assumed that they will become a more important source of rural credit in the years to come.

Why do people borrow from moneylenders when they charge such a big interest? In many cases, the timely availability and quality of service are more important to farmers and rural entrepreneurs than the level of interest rate. Generally moneylenders don't ask for a collateral and have no complicated administrative regulations to follow before getting the loan.

4.3. The Semi-formal Finance System

The semi formal finance system consists of various structures of decentralised financing which offer micro finance services and try to reach those populations excluded from the official banking circuits. A survey in the year 2000, organised by DFID, identified 76 schemes outside the formal sector representing about 35% of total amount of the loans.³⁶ However, in this survey important schemes conducted by the Women's Union are missing, such as for example the TYM scheme and the VBCP project.

Mass organizations play a crucial role in the implementation of donor supported micro finance schemes. Mass organizations have their origins in the Communist Party of Vietnam and the struggle for national liberation. They form the link between the Communist Party and major socio-economic groups such as women, farmers, peasants, youth, war veterans etc. These organizations are usually represented at four administrative levels: national, provincial, district and commune. This structure enables the mass organizations to have a direct contact with the grassroots and to establish a connection with the national level.

The Vietnam Women's Union (VWU) was created on 20 October 1930. As a social organization, it represents women of all strata but predominantly rural women aged between 30 and 50. The VWU is the most important mass organization in Vietnam and works in tandem with the Government, the administration and the Communist Party structures at all levels (national, provincial, district, commune). Chart 1 shows the organization and activities of the Vietnam Women's Union.

Since the early 1990s several mass organizations encouraged micro finance schemes and the formation of groups. A number of them are active in micro finance, but the Vietnam Women's Union is the most active nation-wide. A lot of development programmes, financed by national or international funds, cooperate in its implementation with the VWU.

³⁵ Save the Children (UK), WB and DFID(UK), Poverty in Ho Chi Minh City. A Participatory Assessment, p. 54.

³⁶ DFID and SBV, Micro finance in Vietnam: a survey of schemes and issues, April 2001.

Under the Credit Law of Vietnam (Law N° 02/1997/QH10, 01/10/1998), only recognized institutions can deliver services of credit or savings. This law is not strictly applied and small credit or savings projects are tolerated because they bring important amounts of capital to the grass-root levels. Credit and savings organizations are however controlled and sometimes restricted at local or national levels. But savers and borrowers need legal protection because they cannot control the accounts and management systems of the funds. If something goes wrong the savers can lose their deposits. As a non-profit Vietnamese organization with social goals, correctly controlled and managed, the VWU obtained official support to continue its micro finance activities.³⁷

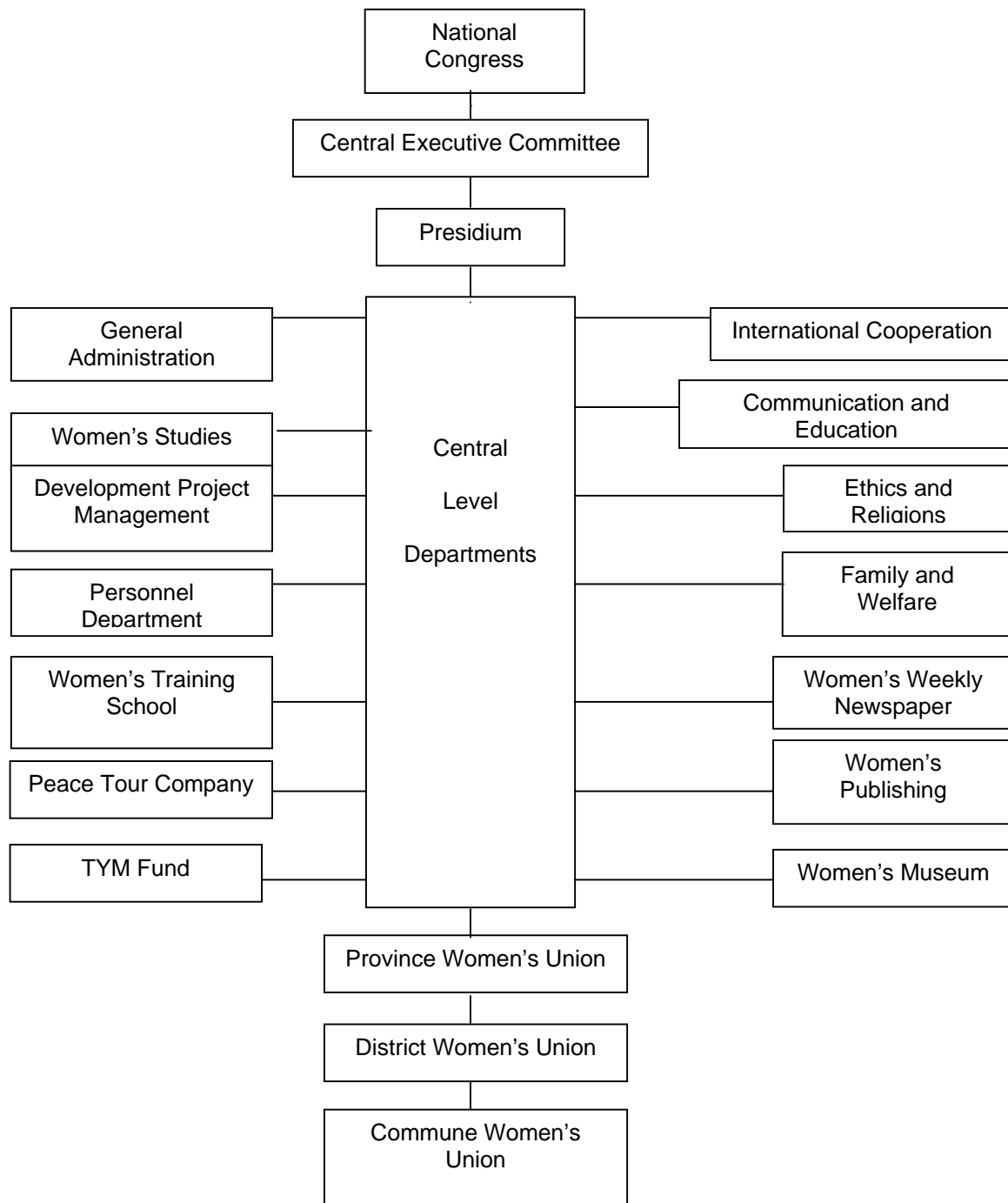
The sector is highly subsidised by donors who see this as a means for providing more efficient aid to poor families in rural areas and thus combat poverty. Poverty reduction through credit schemes has become the central concern in the partnership of many international donors.³⁸ They are operating in various areas throughout the country with different credit and saving schemes. The international organizations provide credit for poor in various models.

The general feeling is that these credit schemes work well, in particular because repayment rates are generally high. However the expansion of the schemes is less rapid than could have been expected. This can be partly explained by the rapid growth of the formal sector, but also by the lack of legal framework and the internal policy.

³⁷ Official letter from the Government Office to the VWU and the SBV, dated January 17th 2000, in: TFF VBCP.

³⁸ BADC and VWU, Proceedings of the Workshop, June 1998, p. 18.

Chart 2: Organization chart of the Vietnam Women's Union³⁹



³⁹ VBCP, Technical and Financial File.

Case study I: VBCP project

Strengthening of the institutional capacity of the Vietnamese Women's Union to manage savings and credit programmes for rural poor women

1.1. Background

The Vietnamese – Belgian Credit Project “Strengthening of the institutional capacity of the Vietnamese Women's Union to manage savings and credit programs for rural poor women” is a bilateral project following an agreement by the Government of Vietnam and the Government of Belgium, signed in 1996. The budget for the entire project amounted to 54 million Belgian francs (1,338,625 €) of which 16 million Belgian francs to be used for a revolving fund. The first phase started in December 1997 for a period of 3 years and was immediately followed by a second phase of 4 years.⁴⁰ The project is executed by the Vietnam Women's Union (VWU) and the Belgian Technical Cooperation (BTC).

1.1.1. Project area

During the first phase, the project has been implemented in 57 districts of 7 provinces throughout over Vietnam (see map 2): 4 in northern Vietnam, 2 in central Vietnam and 1 in southern Vietnam. In each district, 1 commune has been selected. Out of the 7 provinces, 1 province (Nam Dinh) is classified in the High HDI rank, 5 provinces are classified in the Medium HDI rank and 1 (Kon Tum) in the Low HDI rank. During the second phase of the project, new communes in the initial 7 provinces will be involved as well as communes selected in 10 other provinces.

1.1.2. Objectives of the project

The general objective is to improve the living standard of poor rural women and their families.

The specific objective of the project is to consolidate and strengthen the institutional capacity of the VWU in managing micro finance programs.

2. Micro finance scheme

2.1. Methodology

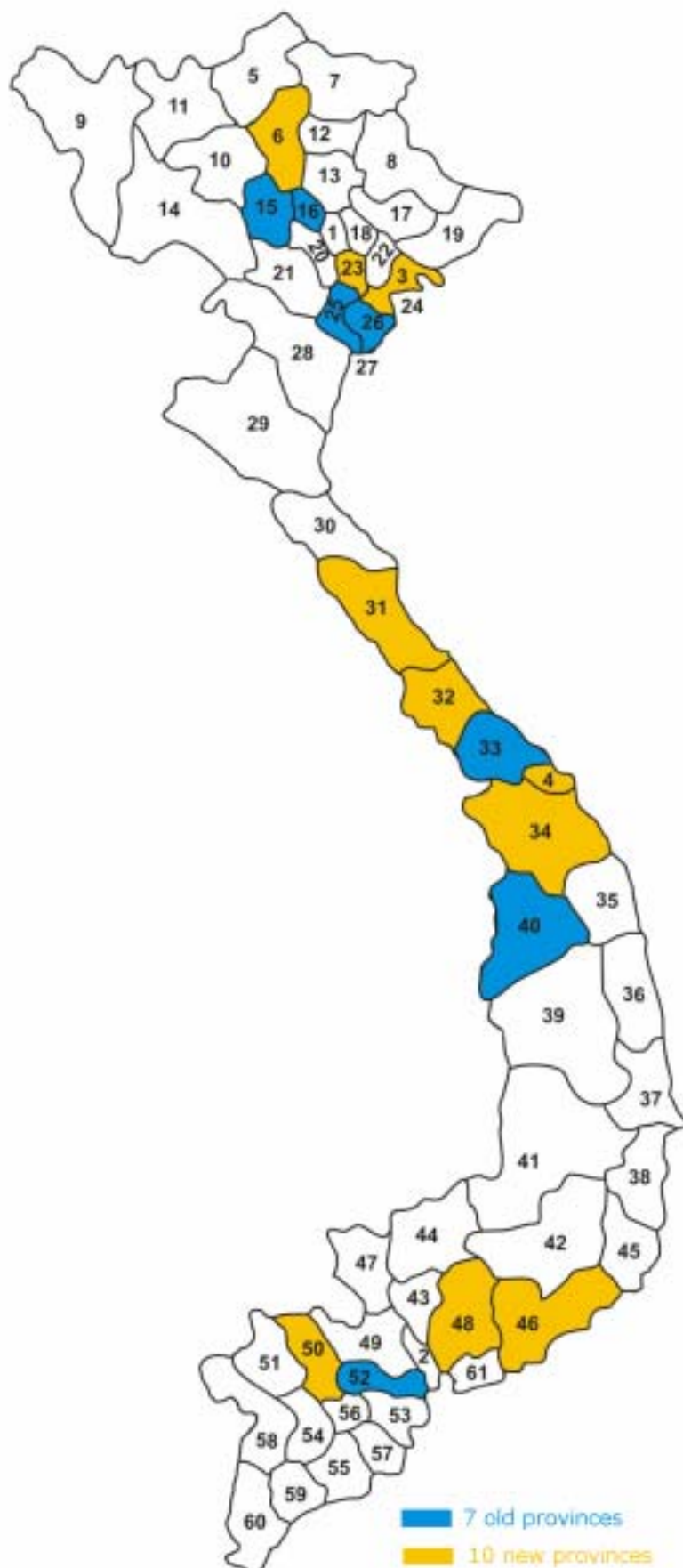
The credit model is based on the solidarity group methodology.

Groups are composed of 10 women in a similar socio-economic position, who know each other and who are willing to support each other in borrowing loans and following the project regulations. Each group selects a group leader who gets a training to manage the group. The position of group leaders rotates on a yearly basis.

⁴⁰ The current report will only tackle the results of the first period.

MAP OF VIETNAM

I. Red River Delta Region (2 City & 7 Provinces)	
1	Hanoi
3	Hai Phong
20	Ha Tay
22	Hai Duong
23	Hung Yen
24	Thai Binh
25	Ha Nam
26	Nam Dinh
27	Ninh Binh
II. North East Region (13 Provinces)	
5	Ha Giang
6	Tuyen Quang
7	Cao Bang
8	Lang Son
10	Yen Bai
11	Lao Cai
12	Bac Can
13	Thai Nguyen
15	Phu Tho
16	Vinh Phuc
18	Bac Ninh
19	Quang Ninh
III. North West Region (3 Provinces)	
9	Lai Chau
14	Son La
21	Hoa Binh
IV. North Central Coast Region (6 Provinces)	
28	Thanh Hoa
29	Nghê An
30	Ha Tinh
31	Quang Binh
32	Quang Tri
33	Thua Thien - Hue
V. South Central Coast Region (1 City & 5 Provinces)	
4	Da Nang
34	Quang Nam
35	Quang Ngai
36	Binh Dinh
37	Phu Yen
38	Khánh Hòa
VI. Central Highlands Region (3 Provinces)	
39	Gia Lai
40	Kon Tum
41	Đắk Lắk
VII. North East South Region (1 City & 8 Provinces)	
2	Ho Chi Minh
42	Lam Dong
43	Binh Duong
44	Binh Phuoc
45	Ninh Thuan
46	Binh Thuan
47	Tay Ninh
48	Dong Nai
61	Ba Ria - Vung Tau
VIII. Mekong River Delta Region (12 Provinces)	
49	Long An
50	Dong Thap
51	An Giang
52	Tien Giang
53	Ben Tre
54	Can Tho
55	Soc Trang
56	Vinh Long
57	Tra Vinh
58	Kien Giang
59	Bac Lieu
60	Ca mau



A centre is composed of three groups with 10 members each. Each centre has a monthly centre meeting chaired by an elected centre chief. The meeting schedule is fixed and includes disbursement of loans, collection of loan repayments, interest and savings. During these meetings information is shared, on topics that are not linked to micro finance (e.g. health, woman emancipation, family planning, etc.).

The procedures to obtain a non-collateral loan are simple. The project provided extensive training to the staff of the VWU at all levels as well as to group leaders and potential borrowers. Two thirds of the total funds were used for capacity building of staff of the VWU at all levels and of the clients, and for the purchase of equipment. Borrowers, who have proven to be reliable during a first loan, can apply for supplementary short-term loans to scale up their production.

2.2. Management of the micro finance scheme

The management of the project is conducted at 4 levels of the VWU organisation (central, provincial, district and commune), involving 334 staff members. Chart 3 shows the structure of the management of the project.⁴¹

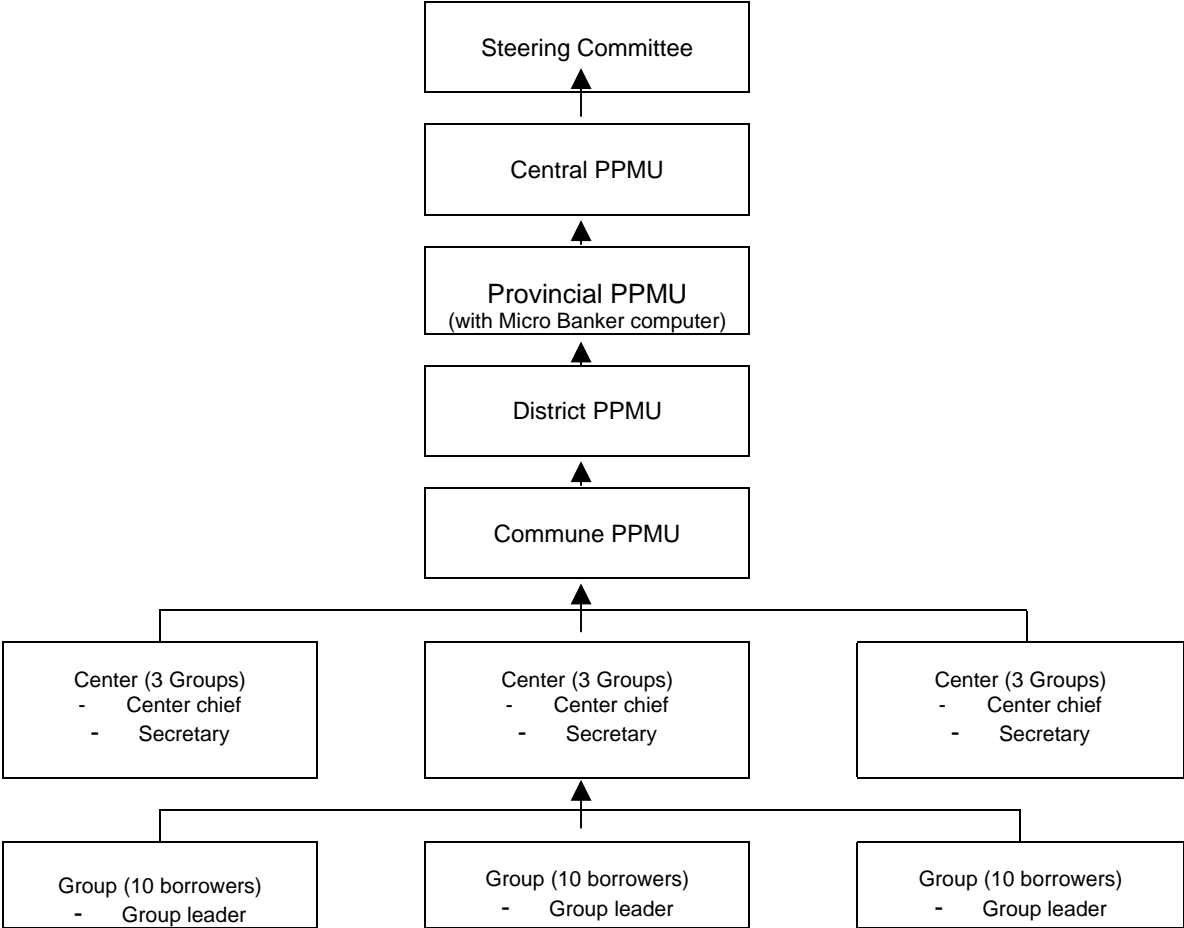


Chart 3: organizational structure of the project

⁴¹ VBCP, Technical and Financial File, annex 4.

2.3. Credit and savings scheme

2.3.1. Target group

The target group of the project are poor women in rural areas, who have the capacity to develop income-generating activities

To become a member the following conditions should be fulfilled:

- no loans from other credit projects or formal financial institutions have been obtained
- members are working poor rural women, between 18-55 years and in good physical and mental condition
- members have a resident certificate and live permanently in the area
- members are willing to follow all group regulations
- there are no opium addicts or gamblers among the members of the family

2.3.2. Loan use

The loans are used for production investment in small business projects to increase the households' economy. Prior to receiving a loan, the new borrowers have to submit a business plan together with their loan application. The vast majority of the portfolio is used for agriculture and animal husbandry (pig, ducks and chicken raising). The project helps to identify alternative income-generating opportunities other than farm business activities (for example handicraft, cook some food to sell on the market, etc).⁴²

2.3.3. Loan terms and conditions

The project has two kinds of loans (general loan and seasonal loan) and many loan cycles, which makes it possible for poor women to borrow loans from small to bigger amounts to invest in production.⁴³

General loan:

- Borrowers may choose to borrow either 500,000 VND or 1,000,000 VND⁴⁴
- The loan term is 1 year
- The principal and interest repayments are done monthly in equal instalments, from the first month onwards
- The interest rate on loans is 1% per month on the outstanding balance (= declining rate)

Seasonal loan

- The loan size can be decided by the borrower, with a minimum of 300,000 VND and a maximum of 500,000 VND
- The loan term is 3 to 6 months
- The principal and interest repayments are done monthly, from the first month onwards
- The interest rate on loans is 1,2% per month on the outstanding balance (= declining rate)

⁴² VBCP, Activity Report, Augustus 1999 - February 2000, Annex 1, p. 9-11.

⁴³ VBCP, Final Report, Hanoi 2001, annex 1, p. 2.

⁴⁴ Will be increased to 1,000,000 and 1,500,000 VND for the second phase.

The VBCP project has a special Member's Mutual fund, which is used in case a borrower dies or in case of natural disasters. Each member has to contribute 500 VND every month, out of which 300 VND is for the Natural Disaster Fund and 200 VND for the Death Fund.

2.3.4. Savings

The project works with an initial compulsory saving of 50,000 VND that is withdrawn from the loan. Besides this initial saving, monthly compulsory savings of 5,000 VND per borrower are paid together with the principal repayments. People can put as much voluntary savings as they want.

Borrowers can withdraw their savings at the end of the loan cycle, for which an interest rate of 0.5% per month is paid.

2.4. Financial management and monitoring

The financial management of the scheme has been computerized with the Micro Banker system, i.e. a banking software developed by the Food and Agriculture Organization (FAO). The system was entirely translated into Vietnamese by the project and adapted to the chosen credit model. Computers were installed at the provincial office of the VWU and connected to the central level of the project. In the head office the data of the 7 provinces are consolidated. Crystal software programme for Management Information System (MIS) has been installed, using data provided by the Micro Banker system and allowing the generation of monthly comprehensive financial reports including ratios so that appropriate measures can be taken immediately. For the follow-up of Micro Banker, two international consultants are invited on an ad hoc basis.

2.5. Results

The first loans were allocated in March 1999 in one test commune, nearly 1.5 year after the start of the project. The credit model was adapted and finalized in August 1999 and very rapidly the scheme was applied in all 57 communes, which all received a starting fund of about 7,600 US\$. Table 3 shows the results up to the 31st of November 2001.⁴⁵

	31/11/2001
Initial capital	6,177,248,282 VND
Total loans amount disbursed	39,560,100,000 VND
Outstanding balance	13,314,500,000 VND
Accumulated savings balance	3,496,400,000 VND
Accumulated number of borrowers	39,500
Active borrowers	11,921
Repayment rate	99,7%

Table 3: Overview of the results of the credit model of the VBCP up to 31/11/2001

⁴⁵ VBCP, Final Report, Hanoi 2001, p. 30.

The Micro Banker system allows the project staff to manage a big amount of customers' information and loan/savings accounts and to produce balance sheets, profit & loss statement, and trial balances at any time and this both consolidated and by branch (1 branch per province). Micro Banker provides numerous safety mechanisms such as a system of compulsory daily back-ups.

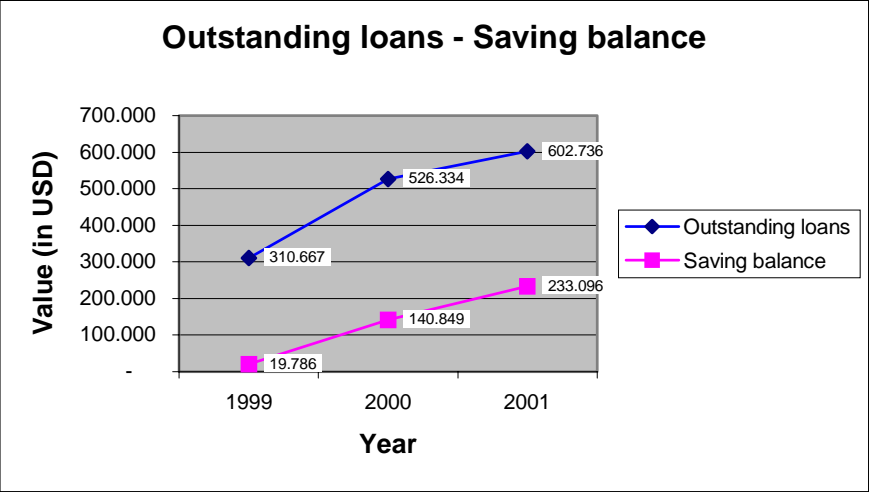


Figure 3: VBCP project: outstanding loans – Savings balance

The systematic MIS reports enable the central project staff to analyse and evaluate the status of loan portfolio, outreach of the credit/savings, financial status, operating efficiency and possibility of financial sustainability for timely decisions or adjustments. MIS also helps the head office to evaluate the accuracy of data entries done by the provincial Micro Banker users and discovers incorrect data-entry to resolve on time.⁴⁶

Training is a key factor and important task of the project to ensure good quality of the project implementation. Training of project staff is mainly focused on credit/savings management, on computer skills and the use of the Micro Banker system, on basic accounting and the management information system. Training of borrowers focused on the project's objectives, operating system, credit/savings scheme, borrowers' responsibilities, loan procedure and simple production/business planning.⁴⁷

⁴⁶ Project document: Project overview, p.3.

⁴⁷ VBCP, Final Report, Hanoi 2001, p. 28.

Case study II: FAO project

Participatory Watershed Management in the Hoanh Bo District, Quang Ninh Province

2.1. Background

The “Participatory Watershed Management Project in the Hoanh Bo District” is a multilateral project, financed by the Belgian Government through a FAO/government co-operative programme under trust fund arrangements. The first phase of the project was implemented from 1995 to 1999. A second phase of the project started in 2000, to consolidate and extend the results of phase I.⁴⁸ The Belgian contribution was 50 million Belgian francs for the first phase and 50 million Belgian francs for the second phase. The project's aim is to support the development of participatory planning and integrated watershed management by focusing on productive resources management in selected pilot areas. The project has 5 key components, one of which is a micro finance component.

2.1.1. Project area

Quang Ninh Province is located in the north-eastern part of coastal Vietnam and is one of the richer and more developed provinces of Vietnam. It is part of the northern economic growth axis, also referred to as the Hanoi, Haiphong, Quang Ninh triangle.⁴⁹ With a GDP per capita in PPP of 1,648 US\$, Quang Ninh is classified as 11th out of the 61 provinces of Vietnam in the Human Development Index, with 12 provinces in the category ‘High Human Development’.⁵⁰ With its UNESCO declared limestone islands of Ha Long (provincial capital), this province has important revenues from tourism.



Map 3: Map of Northern Vietnam

The majority of the province's 13 districts are located in midland and mountainous regions, characterized by limited access, shortage of cultivable land and a population that composed of diverse

⁴⁸ The current report will focus on the performances of the project's first phase.

⁴⁹ Report of tripartite mid-term review mission, November 2001.

⁵⁰ National Human Development Report 2001, Doi Moi and Human Development in Vietnam, p. 83-115.

ethnic minorities. Hoanh Bo District is located strategically along the coast, from north of Hai Phong to the Chinese border and is located next to the economic and industrial growing provincial capital Ha Long. The district covers a surface area of 90,229 ha and has an estimated population of around 53,000 represented by almost 11,000 households. In terms of wealth ranking and socio-economic development status within the province, this district falls in the middle category.⁵¹

The current project area includes three midland and four upland communes of the district. The seven communes constitute the home to a total of 3 different ethnic minority groups: Kinh, Dao and Tay. Among these seven communes, the three midland communes: Bang Ca, Quang La and Dan Chu constituted the project area during Phase I.⁵² Four communes that are located in more mountainous and remote areas were added during Phase II. As a consequence these communes are less developed. They are characterized by ethnic minorities with low educational level, have a subsistence agriculture and rely on forest resources for their livelihood.⁵³

2.1.2. Objectives of the project

The general objective of the project is to create a visible, measurable and sustainable impact on the watershed conditions in the midland and upland areas of Hoanh Bo through the introduction of a cost effective and user friendly participatory watershed management planning and implementation process that could ultimately represent a model for replication in other District and Provinces in Vietnam.

Specific objectives are:

- Strengthen, institutionalise and continue adaptation of participatory methodologies and techniques for Watershed Management.
- Increase productivity of the land and allied resources including income earning opportunities within the watershed area through direct assistance in the implementation of proven best practices, leading to improved environmental conditions and socio-economic settings in disadvantaged project communes and villages of the District.
- Enhance local capacity for planning, management information generation, monitoring and evaluation to facilitate continuation and replication of proven participatory watershed management concepts and practices.⁵⁴

⁵¹ Technical and Financial File, Phase II, p. 1-4.

⁵² This report will only take the 3 communes of the first phase into consideration up to the end of 2001.

⁵³ Report of tripartite mid-term review mission, November 2001, p. 8.

⁵⁴ Technical and Financial File, Phase II, p. 23.

2.2. Rural Finance component

This project has been designed and implemented according to FAO principles. During the workshop of BADC in 1998, FAO presented guidelines for the design of S&C components within projects, which should be considered prior to the introduction of such a component.⁵⁵

The guidelines are:

- strong justification for including a credit component in a development project;
- financial services component should be handled by a financial institution or another suitable local organisation. (FAO promotes the use of a variety of financial intermediaries, including formal and less formal structures. The type of intermediary involved in rural financial operations matters much less than the type of policies it follows and the environment in which it functions);
- Adoption of realistic interest rates;
- Mobilisation of local savings to be part of the development efforts;
- Full-time technical assistance during the initial start-up phase. S&C schemes demand long-term commitment which require a solid base from which to begin.

It was stated that the decision to include a financial services component in the project should be seriously reconsidered if the conditions mentioned cannot be met.

2.2.1. Methodology

In its support to the development of micro finance services, the project implements two complementary mechanisms: community based saving & credit schemes and a Guarantee Fund facility with the VBARD.

2.2.1.1. S&C scheme

The project has provided seed capital as revolving fund 222,780,000 VND (+/- 15,000 US\$) to start a saving and credit scheme. No collateral is required for those who need small amounts of capital for a short period. Borrowers are organized in solidarity groups, which meet on monthly basis. A group leader is chosen among the group members and takes the responsibility to organise the monthly group meetings and to collect monthly loan principal, interest and savings. If a new borrower wants to join a group, the group will inquire the credibility of the demand and approve the loan use.

2.2.1.2. Guarantee Fund

The project made a Guarantee Fund available, with the goal to increase VBARD lending for those who need larger amounts of money for a longer period, than can be provided by the S&C scheme. Its purpose is to substitute, on behalf of the borrower, one-half of the normal collateral requirements, which borrowers must pledge in order to take VBARD loans and for the bank to cover one-half of the costs of

⁵⁵ Coffey, Elisabeth, Rural Finance in Vietnam. The FAO experience, in: BADC and VWU, Proceedings of the Workshop, June 1998, p. 47.

default on principal repayments in case of default.⁵⁶ Guarantee funds are in principle a risk-sharing mechanism. In contrast with physical collateral, the fund serves as a means for reducing bank exposure to loss in case of default. This should induce a greater supply. At the same time the intervention should induce a greater demand by simplifying procedures for loan approval by reducing the transaction costs of taking a loan and by lowering the collateral requirements.⁵⁷

2.2.2. Management of the micro finance scheme

At the district level, a Project Management Board, with national and international staff, is responsible for monitoring and supervising the five components of the project, one of which is the credit component. The national project accountant is responsible to manage the credit scheme, assisted by a national credit consultant. Each commune has a Commune Credit Management Board (CCMB), consisted of the head of the commune Women's Union, the chairman of the commune People's Committee, an accountant and all the group leaders in the commune. This CCMB monitors the activities of the group on a monthly basis and maintains the records at commune level.

The group leaders of the local saving and credit groups have the responsibility to collect loan repayment and savings of each group member. If the group is willing to take the responsibility for a new borrower, the group leader will submit the demand to the CCMB for approval at the monthly CCMB meeting. At this meeting all group leaders of the commune are present. Besides the submission of new applicants, they transmit the repayments of their group to the accountant of the CCMB.

The guarantee fund is managed by the district branch of the VBARD and supervised by the district People's Committee and FAO project staff.

2.2.3. Savings & Credit scheme

The transfer of the revolving capital for the S&C scheme is done per commune, with yearly instalments. Once the transfer is done, the fund belongs to the project commune residents. The data on the seed fund transfers to each commune however are not clear and different figures are mentioned in the project reports.⁵⁸

Although not with full certitude, the internal audit defined the following figures in 2000 for the 3 old communes:

- Bang Ca Commune: 120,995,000 VND (= 8,066 US\$)
- Quang La Commune: 124,790,000 VND (= 8,319 US\$)
- Dan Chu Commune: 85,000,000 VND (= 5,667 US\$)

⁵⁶ Evaluation Report on Credit and Savings Activities, December 2000, p. 46.

⁵⁷ Fritzen Scott, Economic Analysis of a Guarantee Fund Intervention in Three Midland Communes, p. 6-9.

⁵⁸ Interim Audit Report, Savings and Credit Component, Hanoi 2000, p. 27.

2.2.3.1. Target group

All people of the project communes are eligible to join the S&C scheme, except for people who are not able to repay loans, people who are drug addicts, have conflicts in marriage or have debts, and people who previously accessed credit but did not repay timely and completely.⁵⁹ To receive a loan, the person has to be accepted by a S&C group. The scheme is not based on individual borrowers, but is based on the principle of households. One household can take one loan. This means that either man or women of a household are eligible to have a loan on their name and that they are both allowed to join the group meetings. Groups are formed with 5-15 members who live close to one another and know each other. Women count for 95% of the members of the scheme. In practice it is always the wife that is member.⁶⁰

2.2.3.2. Loan use

In the project documents, no directives are given for loan use. The borrowers are not obliged to submit a business plan with their loan application. Most investments are done in husbandry (Bang Ca 83%, Quang La 85% and Dan Chu 75%).⁶¹

2.2.3.3. Loan terms and conditions

The maximum outstanding loan size is 2,000,000 VND. Prior to applying for a loan, compulsory savings 2,000 VND (2 months of 1,000 VND) have to be deposited. The loan size disbursed is subject to the amount that has been saved with a savings to loan ration of 1:10. This means that each member is able to get a loan that is 10 times bigger than the savings deposited (with a max. of 2,000,000 VND). A maximum of 2 outstanding loans at the same time are allowed. A borrower, who took out a loan of less than 2 million VND, can borrow again from the scheme, up to a combined total of 2 million VND.

Loans are given for a period of 1 year. After the 4th month, monthly principal repayments have to be done in fixed instalments and have to be completed within 12 months. Reimbursement before this period is allowed. If a borrower doesn't repay the full amount of principal by the end of the 12th month period, he/she will be fined 10% of the principal still outstanding each 30 days after scheduled repayment.

Only those who have paid back loans or are making payments on time are allowed to apply for additional loans.

2.2.3.4. Interest rate

The interest rate on loans is 1.8% per month. It is calculated monthly, based on the principal still outstanding (declining rate) from the first month onwards.⁶²

The division of interest collected each month is as follows:

⁵⁹ Internal project document, S&C Rules and regulations in different project communes.

⁶⁰ Report of tripartite mid-term review mission, November 2001, annex the Rural Finance Component.

⁶¹ Report of tripartite mid-term review mission, November 2001, annex the Rural Finance Component.

⁶² Evaluation Report on Credit and Savings Activities, December 2000, p. 17.

- 0.8% management fee
- 0.8% inflation fund
- 0.2% risk fund

On numerous requests of the communes and justified by the decrease of inflation in Vietnam, the interest rate has been lowered to 1.5% monthly since July 2001.

2.2.3.5. Savings

Savings of a minimum of 2,000 VND are compulsory before getting a loan. Monthly compulsory savings of 3,000 VND have to be deposited. Voluntary savings can be done without limit during the loan repayment period. Compulsory and voluntary savings can be withdrawn prior to 12th month, but without interest. If deposited for at least 1 year, 0.7% interest/month is paid. (Together with the lowering of the interest rate on loans, the interest rate on savings has been reduced from 1% monthly to 0.7 % monthly.)

2.2.4. Guarantee Fund

A fund of 60,000 US\$ (20,000 US\$ per commune) has been provided to the VBARD. Loans provided covered by the Fund are group based and not on an individual basis as initially planned. They are higher than 3,000,000 VND with a loan term of 12 to 36 months, at VBARD bank interest rates of 1.05%. The Fund should compensate for one-half of all permanent defaults on loan disbursement of up to a total of 40,000 US\$ in each of the three communes.

2.2.5. Management information system

In the first years of the project, accounting was assured manually.⁶³ In June 1999, the Micro Banker system was introduced in the 3 communes (see also the VBCP project). The shift from a manual accounting system to a computer-based accounting system caused considerable problems and some data were lost. Once the computer system was introduced, the CCMBs neglected the use of the manual accounting system. However, the application of Micro Banker system has not been successful either (e.g. several records were deleted) and after evaluation in 2000 it was decided to return to the manual accounting system.

2.2.6. Results

2.2.6.1. S&C scheme

The rural finance scheme was first implemented in September 1996 in Bang Ca commune as the pilot site during phase I of the project, and was later expanded to Dan Chu and Quang La communes in

⁶³ Evaluation Report on Credit and Savings Activities, December 2000, p. 31.

November 1997.⁶⁴ The level of participation varies in the different communes ranging from 36 to 51% in 2001. However it should be noted that in Bang Ca, the initial level of participation amounted to 90%. Table 4 gives an overview of the coverage in the 3 project communes over the period 1998–2001.^{65 66}

	Bang Ca			Quang La			Dan Chu		
	May 98	Aug. 00	Sept. 01	May 98	Aug. 00	Sept. 01	May 98	Aug. 00	Sept. 01
# of households	223	263	258	424	490	450	156	180	156
# of participants	202	181		184	267		112	165	
Coverage	60%	62%		43%	54%		72%	92%	
# of borrowers (hh)	200	171	131	139	231	162	60	61	71
Coverage	90%	65%	51%	33%	47%	36%	38%	34%	45%

Table 4: Coverage in the 3 project commune over the period 1998 - 2001

Over the years, the fund value has increased considerably. From 1999 onwards, there has been an excess in funds. This was caused by high savings, combined with a decreasing demand of credit.

Table 5 shows the fund value of the 3 project communes from 1997 to 2001.^{67 68}

VND	1997	1998	1999	2000	2001
seed capital from FAO	229,785,000	330,785,000	330,785,000	330,785,000	330,995,000
inflation fund	11,773,308	42,054,174	59,946,729	63,122,000	94,556,700
risk fund	2,943,327	10,513,543	18,736,683	20,340,000	22,738,008
savings	31,244,200	78,500,550	116,424,472	109,052,000	71,554,617
cash&cash equivalents	660,200	11,882,346	74,415,455	97,164,000	34,162,131
outstanding loans	277,531,000	440,541,000	444,244,700	404,707,000	434,402,294

Table 5 : Fund Value of the 3 project communes over project duration

The stagnation of the amount of outstanding loans, can partly be explained by the availability of loans at lower interest rate, including loans from the project itself based on the projects guarantee fund, through the formal sector. The project cannot lend out all of the funds they collect in savings because there are competing loan sources.

⁶⁴ After the start of the second phase of the project, the scheme has scheme has been implemented in 4 new communes.

⁶⁵ Evaluation Report on Credit and Savings Activities, December 2000, p. 35.

⁶⁶ Report of tripartite mid-term review mission, November 2001, annex 5 rural finance component.

⁶⁷ Evaluation Report on Credit and Savings Activities, December 2000, p.38.

⁶⁸ Report of tripartite mid-term review mission, November 2001, annex the Rural Finance Component.

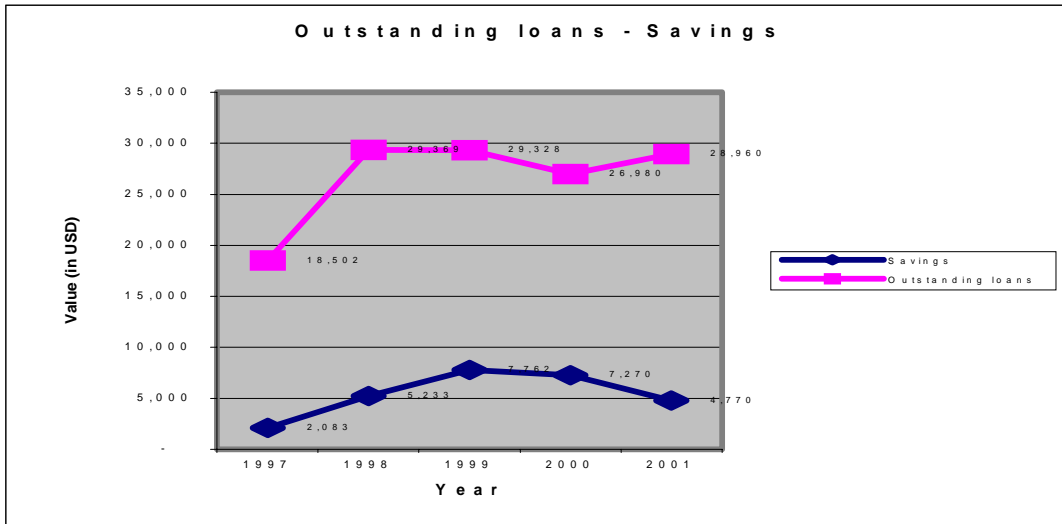


Figure 4: FAO project: Outstanding loans – savings

The amount of savings decreased drastically in 2001, due to the intervention of the Credit Boards to put a maximum on voluntary savings to reduce the growing of unutilised cash.⁶⁹

In September 2001 loans overdue of more than one month, amounted to 20% in Dan Chu, 7.6% in Quang La and 15.9% in Bang Ca.⁷⁰ All group leaders consider mandatory principal payments from the 4th month onwards are unenforceable and unreasonable and in reality only apply it from the 6th or 7th month onwards.

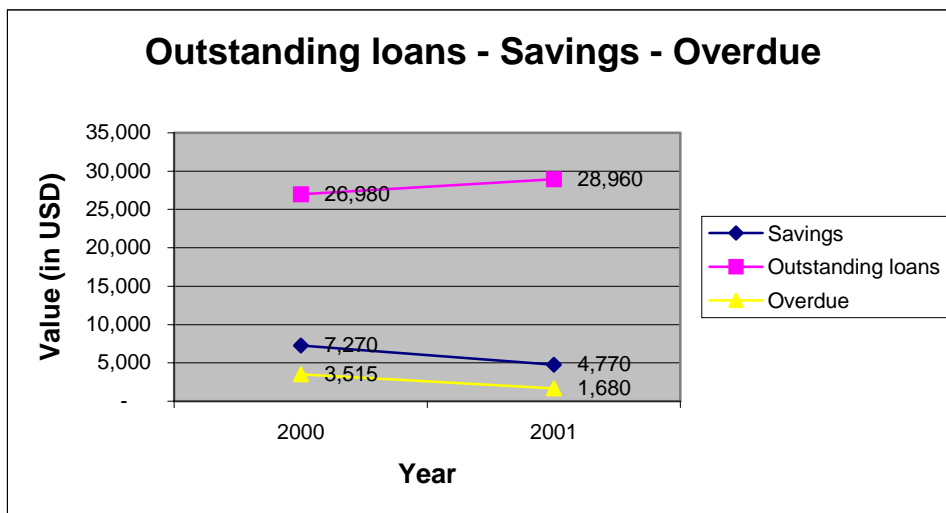


Figure 5: FAO project: Outstanding loans – Savings – Overdue.

The Credit Management Boards have allowed each borrower to have as many outstanding loans as she/he wants at one time, as long as the total outstanding loan amount doesn't exceed 2 million VND.

⁶⁹ Report of tripartite mid-term review mission, November 2001, annex the Rural Finance Component

⁷⁰ Report of tripartite mid-term review mission, November 2001, annex the Rural Finance Component.

In one of the internal project reports it was written that in the 3 communes a total of 3,580 loans for 716 borrowers were given.⁷¹ This means an average of 5 loans per borrower.

There is a serious lack of management capacity at all levels (Project Management Board, CCMBs and group leaders). Apparently people were not thoroughly trained on basic accounting principles and the project rules and regulations. A lot of group leaders think for example that 'late payment' is different than overdue and they only pay attention on overdue after loan period (after 12 months). As a result there is a too late reaction on late payments.⁷²

2.2.6.2. Guarantee Fund

The guarantee fund has significantly increased the loan availability at VBARD in the three project communes. However, instead of giving individual loans as the Fund design originally intended, Guarantee Fund loans are in practice group based with S&C group leaders, that function as guarantee fund group leaders as well.

The figures up to July 2000 are shown in the table 6.⁷³

	Bang Ca		Quang La		Dan Chu	
	Amount (VND)	# loans	Amount (VND)	# loans	Amount (VND)	# loans
before GF	20,000,000	2	130,000,000	33	16,000,000	6
Jul-00	473,900,000	49	378,700,000	63	238,100,000	20

Table 6 : Loan availability at VBARD in the 3 project communes

The distributed loans contributed to an increase of investments in horticulture and livestock production, job creation and forest protection. However, the objective of proving that a large part of previous considered non-bankable clients are actually 'safe' borrowers, is only partly achieved, as this system profited more the medium borrowers.⁷⁴

⁷¹ Internal project document, Report on Saving and Credit Schemes up to 30/04/2001 in 5 communes, p. 2.

⁷² Mr. Chung, project accountant and responsible for micro-credit component, personal communication.

⁷³ Evaluation Report on Credit and Savings Activities, December 2000, p.7

⁷⁴ Report of tripartite mid-term review mission, November 2001, annex the Rural Finance Component.

Case study III: Dairy project

Development of Dairy Support Activities in Southern Vietnam

3.1. Background

On the 28th of February 1996, a Specific Agreement was signed between the Government of the Kingdom of Belgium and the Government of the Socialist Republic of Vietnam for the project “Development of Dairy Support Activities in Southern Vietnam” for a duration of 5 years. The Belgian contribution was estimated at 50.4 million Belgian francs of which 10 million Belgian francs for a Credit Fund. The contribution of the Government of Vietnam would be 3.03 billion VND (equivalent to 0.27 million US\$). The Institute of Agricultural Sciences (IAS) in South Vietnam, BADC and later BTC have been appointed as the executing agencies of the project.

The project comprised of two components: training and credit activities. The credit component was defined as a channel to promote dairy cow raising, managed by a Dairy Cooperative & Credit Unit (DCCU). The DCCU should provide credit services to dairy cooperatives and their farmers. A Dairy Training Centre (DTC) has been developed in order to transfer technology in dairy cow raising.

The development of the dairy sector in Vietnam is relatively new. It was introduced about 20 years ago and is still limited to some highland provinces and in the region of the cities of Ho Chi Minh City and Hanoi. At the start of the project in 1996, the dairy sector faced a crisis. Producing milk in Vietnam was more expensive than buying milk on the international market and the price of a dairy cow dropped dramatically.

However, in the following years the situation improved and the number of cows in Vietnam more than tripled from 10,420 heads in 1994 to more than 35,000 in the year 2000. Also the milk consumption increased rapidly. Currently only 8.6% of all milk consumed in Vietnam has been produced locally; the remaining is imported as milk powder. Raising dairy cattle is no longer a rare adventure for farmer-speculators. Farmers see the benefit they can have from milk production and want more dairy cows. Nowadays, there are many big private dairy farms with herds of more than 40 cows.

The most important area for dairy farming is in Ho Chi Minh City and the neighbouring provinces as shown in the Table 7.⁷⁵

number of dairy cows	1994	1995	1996	1997	1998	1999	2000
Project area in HCMC	10,420	14,283	17,172	18,352	19,838	21,894	25,089
Long An province	138	410	680	743	930	1,126	1,326
Binh Duong province	256	599	675	825	1,420	1,650	1,820
Dong Nai province	1,120	1,220	1,754	1,917	2,115	2,313	2,600
Tay Ninh province		50	70	97	85	79	182
Total number of cows	11,934	16,562	20,351	21,934	24,388	27,062	31,017

Table 7: Number of dairy cows in HCMC and neighbouring provinces for the period of 1994 – 2000.

The Vietnamese Government decided to increase its support to the sector. By the year 2010 the goal is to satisfy 40% of the local milk consumption with a dairy cow with more than 3,500 litres per lactation. Several new provinces have designed programmes to develop dairy production. New milk processing plants have been installed in the provinces of Can Tho, An Giang, Binh Dinh, Nghe An. Technical skills of dairy farmers are increasing.

3.1.1. Project area

The project has been implemented in Ho Chi Minh City and the 5 neighbouring provinces of Binh Duong, Dong Nai, Binh Phuoc, Tay Ninh and Long An. The provinces HCMC, Binh Duong and Dong Nai are classified as respectively 3rd, 6th, and 7th out of 61 provinces on the HDI rank. They fall in the High HDI category of Vietnam. The two other provinces are categorised in the Medium HDI.



Map 4: Map of Southern Vietnam

In the project area, the VBARD was the only formal bank available for agricultural production credit. Occasionally a loan was allocated by VBARD to purchase dairy cattle. Collateral is needed for loans of more than 10,000,000 VND with a duration of 24 to 36 months. The interest rate is 1% per month (flat rate). The repayments are done as a lump sum at the end of loan cycle.

⁷⁵ Synthetic Activity Report, p.7

3.1.2. Objective of the project

The general objectives of the project are:

- improvement of living standards for dairy smallholders
- self-sufficiency in milk production in the project area

The specific objective is to make dairy smallholders activities profitable and sustainable around Ho Chi Minh City.⁷⁶

3.2. Credit component

3.2.1. Methodology

The developed credit system is based on the revolving fund principle, but does not follow the classic key principles of micro finance. The approach combines veterinary technical follow-up of the cows and provision of credit for the purchase of dairy cows. Technical support is provided during the entire loan cycle, beginning with the purchase of a cow that is selected jointly by the farmer and the DCCU veterinary technician.

The project only provides loans to farmers belonging to dairy cow cooperatives, under the responsibility and after agreement of these farmer associations and cooperatives. There is no direct peer pressure but there is a commitment between the project and the individual borrower in the form of joint-investment of each dairy cow. By joining such cooperative, farmers can benefit from the financial and technical services provided by the project. The cow purchased with the loan, and her female offspring are considered as collateral for the farmers. Since the loans are used for the purchase of dairy cows, the amounts are considerably higher than those in a regular credit scheme. As a consequence, the repayment period is longer as well.

3.2.2. Management of the credit scheme

The project had a credit management team, composed of a Vietnamese coordinator, a credit manager, a credit assistant and a veterinary technician. The Vietnamese credit officers have extensive technical knowledge on dairy farming and participate actively in the identification of good cows to purchase. A Belgian international expert was involved from 1996 until 2000.

After the failure of agricultural cooperatives at the end of the 80's a New Cooperative Code has been developed. The project stimulates the creation of dairy cow cooperative or association groups according to the new law. Each group has to select a correspondent (group leader or collector) responsible for collecting loan repayments and for the monthly reporting of the veterinary follow-up of the cows. This person is the key person to ensure timely repayments. He/she functions as a trustee of

the loan collection. An incentive system has been set up and awarded at the end of each year during a meeting of the credit unit. The project staff is in direct contact with the correspondents. Every year a meeting of the credit unit is organized by the DCCU for the correspondents to analyse problems of the preceding year and to discuss the action plan for the year to come.

The DCCU works closely with the training centre. Before joining the credit scheme, the farmers follow a training on techniques in dairy cow raising and a precise technical follow-up of the cows is done.⁷⁷

3.2.3. Credit scheme

3.2.3.1. Target group

The target group are poor farmer residents in the project area. The priority beneficiaries should respond to the following criteria:⁷⁸

- Dairy farmers with one dairy cow;
- Dairy farmers with 1 cow and a calf of minimum 1 year;
- Farm labourers who have gained experience in dairy farming and who plan to start their own dairy farm;
- Female-headed households having up to 4 dairy cows.

Other farmers with 2 to 4 animals can also be eligible for project loans at less advantageous conditions. A feasible investment business plan in dairy cow raising is the first requirement to access the project's credit scheme. A technical condition to receive a loan is the construction of a stable and a minimum fodder production of 200m². Since the farmer has to pay at least 10% of the cost of the cow by himself, own capital is required to purchase the cow. The project aimed to reach 30% of female borrowers.

3.2.3.2. Loan use

The credit can only be used to purchase a cow that is at least 3 months pregnant.

3.2.3.3. Loan terms and conditions

A loan can account for maximum 90% of the price of the cow; the farmer himself must pay the remaining. The cost fluctuates between 8,000,000 VND and 10,000,000 VND. The loan size depends on the market price of a cow.

A loan file consists of the loan application, a loan contract and a technical veterinary report of good health and of pregnancy of the cow (>3 months) to be purchased. Each paper needs to be approved and signed by the borrower, the group and the local people's committee. The loans are disbursed at the moment of purchase of the cow and transferred directly to the cow seller by a VBARD cheque.

⁷⁶ Technical and Financial File, p. 2.

⁷⁷ Project Report for the fifth Steering Committee of 28 1999, p.9

Late repayments are penalized with a double interest for every month of delay (individual) and loss of credit line advantage (repeated loan) for the whole group. The correspondents, who are responsible for the repayments of their group, lose their bonus at the end of the year.

Loans are given for a period of 4 years. Monthly principal repayments have to be done in fixed instalments, financed by the selling of milk. At the time of loan disbursement, each borrower gets his/her repayment schedule for a loan term period of 4 years. The repayment periods can be chosen by the farmers, according to the availability of cash: the most chosen option are payments every two weeks. For the purchase of heifers, a grace period of maximum 6 months (until milk production) is allowed without payment of interest.

3.2.3.4. Interest rate

The interest rate on loans is 1.0% per month, based on the one of the VBARD.

The reimbursement of the interest is allocated as follows:

- 0.15% for solidarity fund
- 0.55% for operating costs of the credit unit
- 0.10% for bad debts
- 0.05% for capitalization
- 0.15% for bonus of the staff of the credit unit and bank costs

A solidarity fund has been established, accounting for 0.15% of the interest and is used to support farmers who encountered specific problems with their cows. Smallholders can only be beneficiary of the fund if the necessary care for their cows had been assured. The solidarity fund pays one third of the original purchase amount if the cow dies in the first year after purchase, 20% in the second year but nothing after more than 24 months. For cows older than 5 years the farmers would not receive any reimbursement.

3.2.3.5. Savings

In the project design it was decided that there would be no savings component within the credit scheme. The main arguments for this decision were:

- the project is too small and too specific to develop a banking activity
- there is no legal framework for such project to handle monetary transactions in Vietnam.

3.2.4. Financial management and monitoring

The system has been managed through an MS-Excel programme in the project office in Ho Chi Minh City. The MIS can provide the following information:

- Personal borrowers files and a personalized schedule for repayments of principal and interest
- Technical information about each purchased cow

- Separate loan ledgers per group to monitor its income and expenditures
- Monthly portfolio analysis providing i.e. the delinquency rate, the repayment rate, the outstanding loans and the portfolio at risk
- Performance indicators (the number of loans, the amount of loans and the economic impact)
- Financial transactions, available funds with their allocations
- A monitoring system with inquiries on average loan amount, total disbursed amount, percentage of women participation, evolution of loans per month, total amount of matured loans.
- Monthly financial statements per group (cash flows, income and expenditures, liquidity, assets)

These functions are interlinked and regularly checked with group bank accounts, where unused cash normally is deposited.

A monitoring system on technical performance of the dairy credit-cows has been organized, which provides information on the efficiency and sustainability of the dairy activity (milk production during lactation, calving interval, lactating period, dry period, number of inseminations per cow, services per conception and abortion rate).

3.2.5. Results

The first loans were given in November 1997 through VBARD who received 25% of the interest income for financial services. After one year the staff of the credit unit directly handled the credit scheme by themselves. At the end of September 2001, there were 17 credit associations/ cooperatives established and provided with credit. Each of them has its own account in VND at a local bank and a correspondent, who was designated for collecting loan repayments.

The following indicators can be deduced from the project reports on credit activities.⁷⁹

Indicators	TFF	Jun-99	Jun-00	Mar-01	Sep-01
Repayment rate	-			99,5%	100%
Portfolio at risk	-			<1%	0%
Number of credit groups	-	13	15	16	17
Total revolving fund (USD)	241,000	90,995	193,889	243,524	258,569
Number of loans	400	168	353	452	501
% of women participation	30%	36%	39%	42%	41%

Table 8: Indicators of performance of the Dairy project.

Initial grant budget: 3,208,802,315 VND (equivalent to 213,920 US\$)

Net increase of asset from all expenses over 5 years: 656,810,793 VND (equivalent to 43,787 US\$)

Outstanding loan balance: 2,937,876,516 VND (equivalent to 195,858 US\$)

Thanks to a very strict financial control (based on a monthly cross checking of the bank accounts) and a good management of the available capital the performances of the credit scheme are excellent. The long term sustainability strategy is well prepared. The number of loans (501 loans) has been higher than the 400 initially indicated in the project document.⁸⁰ Together with a very high repayment rate, the credit system is building up reserves, which are now partly used to cover administrative costs and cow mortality risk in the future. The internally generated income is already sufficient to cover all transaction costs and the DCCU working costs. The repayments are deposited at the groups accounts of the borrower, gradually permitting new purchases of cows. A system of transfer of the revolving fund between groups has prevented that big amounts of money are 'sleeping' at the bank. The withdrawal of the international expert in August 2000 did not influence results

Techniques to develop cow and dairy activities were introduced to the borrowers as a strong support for repayments. The benefit of a technical monitoring during the entire loan cycle has served both the farmers and the project in ensuring the capacity of loan reimbursement of the borrowers.

⁷⁹ DCCU, Report of the Credit activities, June 1999; period April - June 2000; period January - March 2001; period April - June 2001.

⁸⁰ Technical and Financial File.

VI. Discussion

Overall, the three projects presented in this study are considered as being successful. External progress review missions confirmed the positive results. For the VBCP project and the FAO project, both governments decided to extend the scope of the projects with an additional budget. The Dairy project will phase out in the following years, that is to say, the Belgian financial support will be spread over a longer period than was planned, in order to allow the DCCU to prepare to function independently without external donor support. The overall good results of the projects are remarkable because all three projects were ambitious and success was not obvious at all.

At the workshop of 1998, where the three projects were presented, only the FAO project could demonstrate results of its credit component. The VBCP project and the Dairy project were still in a preparatory phase and were just starting off their credit activities. So the FAO project is, at the moment of this study, in a more advanced stage of implementation than the two other projects. It is known that in many cases the results and impact of micro finance schemes only become visible after a few years of implementation.

It is clear that all three projects tried to integrate good practice principles of micro finance in their functioning. Overall, the Vietnamese environment was rather favourable in the past years with very low inflation rates. Nevertheless, all projects faced their specific problems.

The VBCP project planned project activities throughout the entire country and during the second phase, the project area is even more spread out. With only one commune per district in each of the seven provinces involved, it was obvious from the start that communication, logistics and follow-up would be major problems. This spread also implied that more staff had to be involved than was foreseen. However, despite these setbacks the project quickly became one of the major donor supported schemes nationwide. This was only possible thanks to the strong involvement of the VWU, at all levels, who consider this project as important for their organization. Considering the important position of the VWU, the results of the project may have a major impact on the micro finance policy in the semi-formal sector in Vietnam in the future.

The dairy project was set up according to a classic project approach. At the beginning of the project, some scepticism about this project was found, both among Vietnamese and Belgian authorities.⁸¹ But at the same time, it was recognised that such a risky investment in the dairy sector could only be supported by a donor funded programme and that the development of the sector would take time. Meanwhile the situation has changed. Foreign investment has been attracted i.e. important players such as "de Friese Vlag" and Nestlé. Milk consumption is raising quickly and the milk production per cow is quite high.⁸² The Vietnamese government is also impressed and is decided to fully support the sector in view of diversification of its agriculture policy. The project has certainly contributed a lot to this

⁸¹ Mr. Paul Verle, Representative BTC, personal communication.

⁸² Dairy project: Progress Review Mission of 1999.

evolution, since nearly 90% of the dairy cows of Vietnam are raised in the project area. Since nearly two years, the DCCU manages the credit component entirely by its national staff. The credit model is theoretically sustainable, i.e. with current interests IAS staff and other running costs can be paid.

The FAO project was set up, based on a participatory approach with an important involvement of the beneficiaries. When launched, such an approach was innovative in Vietnam and had only been experienced by a few NGOs on a small scale. Based on the overall results the value of this approach has been recognised by Vietnamese authorities at different levels and the model has been introduced in other rural development projects.⁸³

During the workshop, FAO did a comparative analysis of FAO S&C components with internationally accepted standard guidelines. This project was an example for other FAO projects with a micro finance component in Vietnam.⁸⁴ In 1999, the credit component was considered the most successful component of the project.⁸⁵ However, in comparison with the two other projects, the credit component currently turns out to be rather weak. Since the workshop, the S&C component has faced some serious problems.

Compared to the two other projects however, it should be stressed that the project is implemented at district level with project staff and partners with low competence and absorption capacity. Despite the guidelines of FAO⁸⁶, the project has run for a period of 9 months without full-time technical assistance between the first and the second phase.

During the second phase, the project area has substantially enlarged, which made the management even more complex. Nevertheless, the project staff of the second phase does a remarkable effort to solve the problems encountered and to prevent the same problems to occur in the new project communes. A considerable part of the overdue has been recovered, in the new communes new project regulations are applied with much more emphasis on the group system and the project returned to a manual book keeping system.⁸⁷

In the following, certain aspects of the micro finance models of the 3 projects are discussed in detail:

- **Objectives**

The development of a micro finance scheme is in none of the 3 projects the only specific objective. In the first phase of the VBCP project, the specific objective is the strengthening of the institutional capacity of the VWU in managing micro finance programmes. This objective was certainly reached. Because of the dispersed location of the communes involved, the number of VWU staff involved and trained is impressive. The second phase of the project is an expansion phase and has an additional objective, i.e. to establish an effective and viable micro finance programme. Currently, the seven branches are not yet self-sufficient but considering the widespread of the communes and the short time

⁸³ For example: the BTC-project "Multi-sector Rural Development Project in Quy Chau, Nghe An Province".

⁸⁴ BADC and VWU, Proceedings of the workshop, p45-64.

⁸⁵ TFF-Participatory Watershed Management in Hoanh Bo District, Quang Ninh Province, phase II.

⁸⁶ See case study FAO project of this report

⁸⁷ Mr. Koen Everaert, personal communication.

of implementation, that could hardly be expected. Now that the capacity of the VWU has improved considerably, the second phase should focus on the S&C scheme itself and even a third phase is planned to reach sustainability and financial viability.

The credit component of the FAO project is one of the tools to reach one of the specific objectives, i.e. increasing productivity of the land and allied resources. As such this objective has been reached in the three communes involved.

The specific objective of the Dairy project is to make the dairy smallholder activities profitable and sustainable around Ho Chi Minh City. This specific objective has been reached but it is recognised that improving circumstances outside the project, such as trends on the international market, increasing milk consumption and cheaper production costs, have certainly contributed to the success. The credit component was an anchor point to support the switch from dairy cattle raising in Ho Chi Minh City to the surrounding rural areas, where expertise was low.

- **Target group**

In Vietnam, women clearly take the management of the households' economy in hand. In the three projects women's participation has been encouraged. In contrast to the two other projects, the VBCP only allows women to participate in the scheme. Only when a borrower dies, she can be replaced by her husband, who then becomes responsible for the loan repayment. In the FAO project and the Dairy project, the participation is open to men and women. In practice, women are well represented, particularly in the FAO project, with 95% female borrowers.

The Dairy project is implemented in three provinces with a High HDI and 3 provinces with Medium HDI. The provinces involved in the VBCP project are generally poorer than Quang Ninh Province and the provinces around HCMC. Considering the high cost of one milking cow (10 million VND), the Dairy project doesn't directly focus on the poor. It is clear that in none of the 3 projects the poorest of the poor are involved.

In the selection of the communes that could participate in the VBCP project, one of the important criteria was the lack of other sources of credit in the commune. In one case, the increasing possibilities of lending in a selected commune has even lead to the selection of another commune in the same district. For many borrowers, the reception of their first loan of 1 million VND (around 70 US\$) is the highest sum they ever possessed.

- **Group system**

All 3 projects work with the group system but in completely different ways.

The VBCP project applies the so-called classical group system as worked out at the Grameen Bank in Bangladesh⁸⁸, with the exception that the weekly meetings have been reduced to monthly meetings. Women in Vietnam are very hard working and they can't afford to regularly 'waste' time on meetings. However, the attendance rate to the meetings appears to be high. The group leaders request a strong discipline and the reimbursement per group is close to 100%. Even the decease of a borrower or unexpected events, such as floods, were no reason to cancel loans.⁸⁹ Based on the available data it was impossible to have an idea whether group members are often asked to reimburse for another member. It would be interesting to do a survey with questionnaire on this matter.

In the Dairy project, the 'correspondents' are fully responsible for the repayments and the cow bought is used as collateral. However, indirectly there is peer pressure with the established incentive mechanism of possible reimbursements to the cooperative at the end of the year. Good reimbursement of its members enables the cooperative to develop further. The association or cooperative decides on new loan applications and these will not be allocated to bad payers.

In the FAO project, the collateral for loan repayment is also based on peer pressure. However, compared to other experiences in Vietnam, overdue loans are numerous and their is certainly less discipline and follow-up.

Group leaders change rules and regulations (e.g. reimbursement starts later than agreed upon) or do not apply them (in case of non-repayment, the group members were not enforced to pay the debt of their group member). In addition, the group principle has also been applied for the management of the Guarantee Fund and was often managed by the same group leaders. This has the potential to undermine the S&C scheme: when borrowers jointly take a loan from the Guarantee Fund, in stead of individually, the lower interest rate of the bank (1%) is applied. When the group members split the loan they can each obtain a small loan at a cheaper interest rate than with the S&C scheme of the project.

- **Preparation and design**

The design of the VBCP project and the Dairy project took a long time, but once applied they have hardly been changed. For both projects it is known that the schemes were extensively discussed with all parties involved. The major modifications implied additional loan possibilities such as seasonal loans (VBCP project) and limited possibilities for an association or cooperative to obtain loans for equipment, such as for example a milk-cooling tank instead of the purchase of a cow (Dairy project).

⁸⁸ Gibbons David and Wayne Temlinson, The Grameen Trust, Training Manual on Cost-effective Targeting June 1995

⁸⁹ Mr. Romain Baertsoen, VBCP, personal communication.

From the beginning of the project implementation of the FAO project, deficiencies in the project design and documentation regarding rules and regulations of the credit scheme have been reported.⁹⁰ Continuous adaptations seem to be necessary. As a result the project has a continuous problem in the application of its regulations. The new communes of the projects' second phase apply new improved regulations. But without a uniform regulation system for all project communes, this makes the management even more difficult.

- **Interest rate**

Compared to surrounding countries, the applied interest rates in rural finance in Vietnam are rather low. This is a result of the applied policy of the Government of Vietnam to give subsidized credit to the poor. Until recently, it was the SBV who determined the ceiling interest rate applied by all financial institutions. When designing the S&C schemes, both the VBCP and the Dairy Project have adapted their interest rates to the Governments' policy. In the year 2000, the Government changed its policy towards a base interest rate. But it takes time to implement this new regulation. In practice, the pressure on micro finance projects to follow the rates of the VBARD is still very high and in reality the schemes cannot fully determine the interest rate by themselves. The pressure upon S&C schemes is not primarily because their loans are more expensive than those of the formal system (they are still far cheaper than moneylenders), but because the local project partners often feel that they are expected to follow the Government initiative to provide cheap credit to the poor.

Even in case the projects intend to elevate their interest rate, this is, in contrast with commercial banks, not easy for an ongoing S&C scheme. For the borrowers, the interest rate is a very sensitive issue and they would not easily accept an increase. It takes a lot of time to explain carefully what the interest is used for and why this is higher than the subsidized credit of the formal banks.

In practice, the VBCP project and the Dairy project apply an interest rate close to the one of VBARD. These rates are low but with low loan loss provisions, low inflation rate, low operational costs and a strict management, these rates seem to have prospects of viability anyhow. The Dairy project is in theory financial sustainable with an interest rate of 1% per month.

The interest rate of the FAO project is higher than in the two other projects but higher rates alone cannot automatically be associated with the popularity of the schemes.⁹¹ With higher loan loss provisions the higher interest rate doesn't mean that viability of this scheme is better than the other two.

⁹⁰ Fritzen Scott, Rural Credit Design, Management and Household Decision Making, p. 11-17.

⁹¹ CG and UNDP, Microfinance in Vietnam: A collaborative study based upon the experience of NGO's, UN agencies and bilateral donors, p.15.

- **Savings**

Low local savings are considered as a burden for further economic development in Vietnam. Until today an important part of the population prefers to buy gold and hide it somewhere in a safe place rather than deposit it in a financial institution. Also in the many existing micro finance schemes, low savings are considered as an important constraint for the further development of these programmes.

In micro finance savings are often considered as an indicator of success. However, as reported at the micro credit workshop of 1998⁹², the savings component often is a weak part of S&C schemes of the semi-formal sector in Vietnam. With the low lending interest rates, the savings interest rates are low as well, so that saving becomes less attractive. With low returns, restrictions on access to savings and low confidence, it is understandable that people appear reluctant to save and don't like to deposit their savings for a long-term period.⁹³ In schemes with compulsory savings, a mentality of 'minimum balance only' seems to be no exception. Developing a savings component and increasing the revolving fund is considered as an important asset to obtain viability of the scheme.

Despite these reserves for savings, there has been a remarkable amount of voluntary savings in the FAO project. Apparently a significant fraction of participants simply wants to save, without borrowing. In theory this is to be welcomed, but then a good financial management is indispensable.⁹⁴ In the FAO project, with a decreasing demand of credit, these funds were 'sleeping' at the bank, for which interests had to be paid. In this way, these savings are a cost for the scheme. In 2000, the Credit Board decided to put a ceiling on the total amount of accepted voluntary savings to limit the growth of unutilised cash.⁹⁵ In another programme supported by Belgium in HCMC, the savings component is high but most of it is used to meet the loan demands and "sleeping" funds are limited but are revolving.⁹⁶

The amount of savings in the VBCP project is gradually increasing, but still far off from the PEARL target. No savings component is included in the Dairy project.

- **Non-financial services**

Borrowers do not only need support on how to manage the financial aspects, but also may need technical advice in order to select appropriate activities (e.g. market study) and to apply them (e.g. for raising livestock and growing new crops). The Dairy project and the FAO project have important components in the project to respond to these needs. For the Dairy project, it can nearly be considered as the most important aspect of the DCCU. In this way they contribute to the training of farmers with little experience in dairy cattle breeding. Activities such as supporting farmers to select new cows

⁹² BADC and VWU, Proceedings of the workshop, p.10.

⁹³ Mr.Houtman, Micro Banker expert, personal communication.

⁹⁴ Campion Anita, Mobilizing small, medium and large savings. Motivations and financial risks, p.18.

⁹⁵ Evaluation Report on Credit and Savings Activities, FAO project, December 2000, p.41.

certainly enhanced the trust of the farmers. For the VBCP project this aspect has been less developed. As a consequence, borrowers nearly all invested in pig raising in certain villages. In the long term such a lack of diversification could create new problems and should therefore be analysed. During the monthly centre meetings certain technical aspects have been introduced but there is certainly room for improvement. The project staff is aware of this and considers it as challenge for the second phase, were they now start to include training sessions for the borrowers on small economic enterprises and help the borrowers to identify income-generating opportunities other than farm business activities (for example handicraft, cook some food to sell on the market, etc).⁹⁷ This is an important aspect, which still needs to be further developed.

- **Relations with the formal sector**

During the workshop of 1998, it was observed that the link between the formal and the semi-formal finance system is weak in comparison with neighbouring countries such as Thailand and the Philippines.⁹⁸ There is an apparent lack of trust and few trials of big donor agencies, such as the World Bank and the Asian Development Bank, to set up major programmes with Vietnamese Banking Institutions. The described projects have weak relations with the formal sector as well. All three have regular contacts with the banks, but the working relations did not develop beyond that stage.

With bigger loans involved, one could expect some competition between the formal sector and the dairy sector, but this was not the case. Loans for dairy cows were the exception in the formal sector. This can partly be explained because in the formal sector the capital of a loan has to be reimbursed as a lump sum at the end of the loan cycle. Obviously with a population who has no habit of saving, this is risky. With a DCCU loan, the capital has to be reimbursed in regular instalments. This is not difficult for farmers because of the daily income of the selling of milk. With the new Government policy to support the dairy sector and considering the success of the DCCU, representatives of Banking institutions have contacted the DCCU to analyse the credit model and the reasons of success.⁹⁹ Thanks to the possibility to slowly phase out the project with the support of the Belgian Government, a better integration of the DCCU in the formal sector could be a way to reach sustainability of the programme.

In the FAO project, the results of the Guarantee Fund in collaboration with VBARD, does not inspire to continue the cooperation. Although during project implementation the gap between the VBARD and the population has narrowed, it was also reported that the loans did not reach the target group of poor households. After the Guarantee Fund is exhausted, banking lending in the project communes will likely decrease, thereby defeating the original purpose of the fund.¹⁰⁰ Part of the problems have their origin in the design of the scheme, but it should be noted that in another dairy project supported by Belgium¹⁰¹

⁹⁶ Evaluation of the two years activities of the social workers team in PMU415, Tan Hoa – Lo Gom Canal Sanitation and Urban Upgrading project, 2001.

⁹⁷ VBCP, Activity Report, Augustus 1999 - February 2000, Annex 1, p. 9-11.

⁹⁸ BADC and VWU, Proceedings of the Workshop, p.9.

⁹⁹ Mr. Long, DCCU, personal communication.

¹⁰⁰ Evaluation Report on Credit and Saving Activities, FAO project, December 2000, p.49.

¹⁰¹ BTC project: "Development and extension of the dairy farming activities around Hanoi"

the experience with a guarantee fund was disappointing as well.¹⁰² With the State Bank Decision 76 which theoretically eliminates collateral requirements on loans under 10 million VND, the system of Guarantee Fund now is obsolete for micro finance in Vietnam.¹⁰³

The VBCP project has no operational links with the formal sector and even tries to select communes where possibilities of loans from the formal sector are limited or inexistent. However, the VWU is represented in the management board of the VBP and has obviously strong links in this way.

- **Management Information System**

The financial management of the Dairy project and the VBCP project is fully computerized. At any moment these projects are able to present results that are up to date, backed up by written proofs such as bank statements. Both projects are capable to provide ratios such as required with the monitoring systems like PEARLS or CGAP. Late repayments are immediately noticed and generate an intervention. In contrast, the data of the FAO project are not complete and much less transparent. Record keeping has been extremely poor and the available data doesn't allow to carry out a real monitoring.

The Dairy project uses a simple MS Excel file, created by the project staff, corresponding to the needs of the project. Because of the relatively small number of loans (about 500 in 2001), this option was justified. The system is cheap and easy to handle. The major disadvantage is the lack of safety measures e.g. data can be modified at any time by anyone able to use the programme, so that regular internal control is essential.

With more than 30,000 loans in a period of 2 years, the needs of the VBCP were completely different. The FAO Micro Banker programme, selected by the VBCP, is far more complex. It has strict work flows and safety measures (e.g. compulsory daily back-ups in all branches). This programme has proven to be effective in banking institutions worldwide (for example the Grameen Bank), but had not been tested on a project level before. The results are positive, but this was certainly due to the many precautions taken before and after the installation of the programme. Initially the programme had to be adapted to the VBCP credit model and needs. The programme had to be completely translated into Vietnamese because hardly anyone of the future users mastered the English language. On demand of the international Micro Banker staff experts, extensive training at all levels was included in the preparation period. The scheme was first tested in one pilot commune and then gradually applied, so that modifications were possible. At any time, staff of the central office can be consulted to solve problems. Occasionally international Micro Banker staff experts are called for punctual visits. In return, the performance of the VBCP staff is well appreciated by the Micro Banker experts. On several occasions project staff has been invited at international workshops about Micro Banking and their remarks were taken into account for further improvement.

¹⁰² Ms. Thanh, micro finance expert, personal communication

¹⁰³ Evaluation Report on Credit and Saving Activities, FAO project, December 2000, p.49.

However, the installation of the Micro Banker software was not cheap (5,000 US\$) for the extended version, which was still a bargain because the FAO now disposes of a Vietnamese version. However, the investment is considered essential. For a scheme on large scale (and even extending drastically in the second phase), only a professional approach can lead to credibility of results, essential for further development of the sector.

The FAO project also applied the Micro Banker system, more or less at the same time as VBCP. However, the application proved no success. Several explanations are possible. The project was already ongoing with a manual accountancy system. With the introduction of the Micro Banker, the group leaders and CCMBs had to adapt to the software. The low capacity of local staff, high turnover of staff, and lack of follow-up certainly have played a role as well. A lack of training and a lack of computer competency necessary to use the software effectively, had the result that no one at the commune level knew for example how to retrieve data from the computer, rendering its function of a data management system pointless.¹⁰⁴ Another major reason for failure seems to be lack of discipline to apply the scheme as agreed upon. From time to time VBCP project staff helped the FAO project, but there has never been any real technical follow up of the implementation of the Micro Banker system.

Considering the relative low number of loans, the Micro Banking programme was probably too complex for a small project at commune level. In the second phase of the project it was decided not to use the Micro Banker software anymore.

- **Legal framework**

Under the Credit Law of Vietnam, only recognized formal banking institutions (VBP, VBARD, PCFs) can deliver services of credit and savings. The so-called informal (moneylenders, ROSCAs) and semi-formal sector (VWU, NGO projects, international donor projects) don't fall within this legal framework. The importance of non-formal micro finance schemes in the reduction of poverty is however admitted by the Vietnamese Government¹⁰⁵ and in practice the activities of these projects are tolerated.

Appropriate financial management of micro finance can easily run out of hand and the recent past experience has shown that even formal banking institutions can crash. Therefore, it is comprehensible that the Government tries to take the necessary precautions to avoid new financial crisis situations and is not willing to allow all kind of schemes to develop on the spot. In the framework of the general reform agenda, a banking reform strategy is currently being developed but it is not expected that the problem of legalization of the semi-formal micro finance will be quickly solved.

This means that the three projects presented above conduct illegal activities. International funded projects function under the legal umbrella of the projects' international agreements. It is possible that problems occur once the validity of an international agreement has expired.

¹⁰⁴ Evaluation report, FAO project, December 2001, p.32-34.

¹⁰⁵ Comprehensive Poverty Reduction and Growth Strategy, January 2002, p. 20.

The legal problem partly explains why the Vietnam Women's Union is often used as a way to channel funds to commune level. The VWU has a network that reaches out to all communes and districts of Vietnam. They are recognized and trusted at the highest level. In 2000, the VWU has been assured by the Prime Minister of Vietnam that they can continue their credit and savings activities in the future¹⁰⁶, but the practical regulations still have to be developed. However, this trend will also confront the VWU with a fundamental problem: developing a formal financing institution inside the VWU seems incompatible with its social mission.

¹⁰⁶ Official letter from the Government Office to the Vietnam Women's Union and the State Bank of Vietnam, dated January 17th 2000.

VI. Conclusion

The S&C schemes presented in this study have been developed based on accepted principles of good practices, adapted to the specific situation of Vietnam.

When presented at the BADC workshop in 1998, the VBCP project and the Dairy project had hardly any results to present. Three years later, they both developed into important reference projects for Vietnam. In the current circumstances, the credit component of the Dairy project is sustainable. With the rapid developing Vietnamese dairy sector and the interest of the formal sector for the applied scheme, the project could have a major impact on the development of the dairy sector in Vietnam and the diversification of the agriculture around HCMC. The results of the VBCP project, after 3 years of implementation, are impressive and better than was expected. The project quickly developed into one of the bigger donor supported schemes in Vietnam. The project is not yet sustainable, but considering the dispersed initial set-up this could not be expected.

The success of these two projects can partly be explained by an extensive preparation period, prior to the start of the S&C scheme, by a thorough training programme and by a close follow-up of the activities. The S&C schemes were designed very carefully, taking into account all possible circumstances and trying to avoid loopholes. The regulations are clear for both borrowers and staff and strictly applied. An appropriate Management Information System proved to be an important asset: shortcomings are quickly noticed and trigger the necessary reactions. With complex schemes such as the VBCP project, a specialized computer programme seems to be a necessity. This implies of course that the necessary funding should be made available for purchase, technical support and training. In the smaller scheme of the Dairy project, a cheaper and less sophisticated alternative proved to be appropriate.

In 1998, the S&C scheme of the FAO project was considered as one of the better projects presented at the workshop. The results were at that moment far better than those of other FAO projects in Vietnam. However the scheme did not develop as was expected. An appropriate MIS is not available and results cannot be presented as for the two other projects. Discipline is lacking, the scheme is not applied as designed and modifications are made continuously. An improvement of the financial management is urgently needed. The current project staff is well aware of the serious problems and takes the necessary measures for improvement of the situation. However, it could be considered to stop new loan disbursements while awaiting clarification of the data.

Based on these results, it seems to be possible to develop satisfying micro finance schemes in Vietnam in the current circumstances. Long term prospects of these projects will however largely depend on the evolution of the legal issue of semi-formal micro finance institutions and the further development of the formal Vietnamese financial sector in the coming years.

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