

# Reasons and Solutions for Insufficient Financial Supply in Shandong Rural Area of China

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## Abstract

According to the survey in Shandong rural area from China inclusive finance center, a prominent problem in Shandong is that the credit from rural financial institutions is insufficient because of the high interest rate, the baffle from mortgage and guarantee, and the reluctance or disability for financial institutions to supply more and proper products to peasants. In order to supply more and proper financial service to peasants, suitable financial institutions are needed. In Shandong rural area, small or regional commercial financial institutions are suitable and mutual folk finance is indispensable at present.

**Keywords:** Shandong rural area, finance supply

## 1. Introduction

Many economists and organizations believe that proper financial support can relieve poverty (Stiglitz, 1994; World Bank, 2001). In order to develop rural economy, China also pays much attention to the financial support to rural areas especially after 2006. In 2013, "Decision of the Central Committee of the Communist Party of China of Some Major Issues Concerning Comprehensively Deepening the Reform" points out that "to develop inclusive finance is an important part to improve and perfect the financial market". One major content to develop inclusive finance is to develop rural finance which therefore will be put on higher importance. The ways to develop rural finance are diverse. How to find the proper and the best way depends on the knowledge of the reality in rural area. Therefore surveys are indispensable. In 2004, Research Center of Rural Economy of Department of Agriculture carried out a financial survey to more than 20000 peasants in 31 provinces. In 2006, the People's Bank of China invested more than 20000 peasants in 10 provinces. The scale of these two surveys is large, but investigation about Shandong province is not detailed. And the survey of People's Bank of China had not involved Shandong Province. Pin Xinqiao investigated the rural financial situation in Jiangsu, Jilin, Shanxi, Yunnan, Hunan, Heilongjiang in 2007 and 2008, there is still no Shandong Province. Pan (2013) investigated the supply and the demand of deposit, remittance, saving and proxy among 173 peasants in Changqing district of Shandong Province. The investigation area is only restricted in a district and the number of investigated peasants are too few to reflect the overall situation of the whole Shandong Province. Therefore in order to have the overall view about the rural financial status in Shandong Province, the above investigations are not sufficient. So in January and February, 2014, China's Inclusive Finance Center (CIFIC) carried out a survey to more than 8800 peasants in 152 counties, 17 prefecture-level cities all over Shandong Province. According to this survey, the financial supply is not sufficient. The following part will describe this reality, the reasons and the solutions to resolve this problem.

## 2. The Current Situation of Insufficient Financial Supply in Shandong

According to our investigation, we find a kind of interesting phenomena in rural area of Shandong province, China, which is shown in Figure 1. The fund flow from the peasants to financial institution is more than that from the financial institution to peasants. The fund that financial institutions supply to peasants is not enough and peasants' financing demand is not satisfied well. This conclusion is deduced from the following four facts.

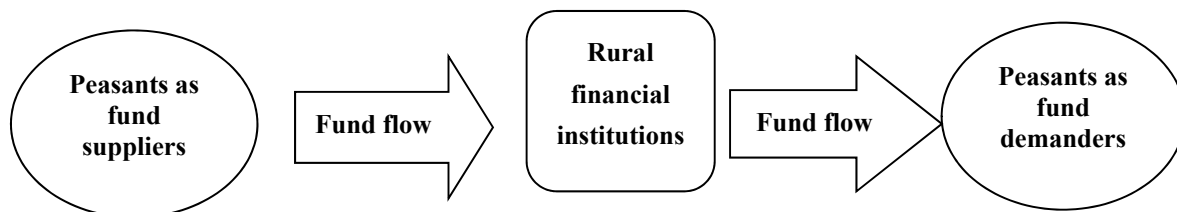


Figure 1. Features of rural financial fund flow in Shandong province

The first is that the proportion of peasants who can obtain financing from financial institutions is very small. Among all the peasants, only 12.99% peasants obtain financing. Only 48% peasants can obtain the fund among peasants who want to be financed and still more than half of these peasants can not fulfill their willing (Table 1).

Table 1. Proportion of peasants who obtain financing in 2013 in Shandong(%)

Areas	Among all the peasants	Among peasants with financing desire
Shandong Province	11.99	48.26
Jinan	12.5	42.78
Qingdao	9.82	48.87
Zibo	9.51	36.84
Zaozhuang	24.29	78.82
Dongying	5.71	16.84
Yantai	8.82	43.85
Weifang	12.26	55.43
Jining	12.96	55.15
Tai'an	17.86	75.76
Weihai	7.94	65.79
Rizhao	13.02	59.7
Laiwu	8.87	30.36
Linyi	11.43	54.25
Dezhou	10.03	33.14
Liaocheng	19.71	57.86
Binzhou	11.62	50.68
Heze	10.08	37.91

*Note.* Shandong Province includes 17 prefecture-level cities which are Jinan, Qindao, Zibo, Zaozhuang, Dongying, Yantai, Weifang, Jining, Tai'an, Weihai, Rizhao, Laiwu, Linyi, Dezhou, Liaocheng, Binzhou, Heze.

Resourse: Survey of China's Inclusive Finance Center.

Secondly, even among the peasants who have obtained the financing, most of them still want financing. According to table 2, in Shandong Province, only about 25% express that then need not financing any more, still about 75% say then need more financing, and 13.79% show that they need more financing urgently.

Table 2. Proportion of peasants with willing to obtain more fund who have been financed(%)

Importance level	1	2	3	4	5	6	7
Proportion	24.7	12.1	15.97	15.08	13	5.36	13.79

*Note.* 1-7 are used to represent the importance level. 1 represents the most unimportant, which also means the peasants need not financing any more, 7 represents the most important which mean the peasants need more financing urgently.

Resourse: Survey of China's Inclusive Finance Center.

Thirdly, the credit amount that peasants hope to obtain is larger than that they obtained in fact. According to Table 3, the average credit amount is RMB 67 thousand. But this amount that peasants hope to obtain is RMB 85.4 thousand according to table 4. In table 4, 80% of the peasants' desirable credit amount is below

RMB100000. We choose class mid-value RMB5000, RMB20000, RMB40000, RMB125000, RMB350000, RMB650000 respectively for each class. And according to corresponding proportion, we calculate that weighted mean is RMB 854000 which is higher than that obtained in reality.

Table 3. Descriptive statistics of credit amount that has been obtained in Shandong province

Mean (10000 RMB)	Max (10000 RMB)	Min (10000 RMB)	Standard Deviation	Kurtosis	Skewness
6.715449	150	0.1	10.0052	5.642924	60.0563

Resource: Survey of China's Inclusive Finance Center.

Table 4. Distribution and the mean of desirable credit amount for peasants

0-10000 (RMB)	10000- 30000 (RMB)	30000- 500000 (RMB)	50000- 100000 (RMB)	10000- 200000 (RMB)	200000- 500000 (RMB)	500000 and more (RMB)	Mean
11.98%	25.1%	19.11%	21.41%	14.9%	5%	2.5%	RMB854000

Resource: Survey of China's Inclusive Finance Center.

Fourthly, among the peasants who want to but did not obtain credit, there is still a significant perception that can afford a high interest rate. According to table 5, 35.63% peasants express that they can afford 5% and higher interest rate. 15.34% peasants show that they can afford 10% or more interest rate.

Table 5. The highest interest rate afforded for peasants who want to but can not obtain credit

Interest rate	Below 5%	5- 10%	10- 20%	20- 30%	30- 50%	50- 80%	80%and higher	5% and higher(sum)	10% and higher (sum)
Percentage	64.37	20.29	8.28	2.81	1.79	1.35	1.12	35.63	15.34

Resource: Survey of China's Inclusive Finance Center.

Therefore, generally speaking, the rural financial institutions can not meet the financial demand from the peasants well.

### 3. Reasons for the Sufficient Financing Supply from the Rural Financial Institution

The insufficient financial institutions' supply can be examined from the two aspects, the peasants and the rural financial institutions. From the aspect of peasants, the insufficient effective demand will affect the realized financial institutions supply. From the aspects of financial institutions, they have difficulties to supply proper financing products or the desirability to supply financial services to rural area is low. Specifically, there are four main reasons.

Table 6. Importance level of kinds of reasons for peasants with credit desire but unable to obtain credit

Reasons	Importance level
Interest rate is too high	3.35
Can't find relationships needed	2.88
Lack of mortgage or guarantee	2.62
Too far away to reach financial institutions	1.26
Don't know the types of credit	2.05
Credit amount is too small	2.22
Time limit is too short	1.99
Credit record is bad	1.33
There are unpaid credit	1.41
Others	1.38

Note. 1-7 are used to represent the importance level. 1: the most unimportant. 7: the most important.

Resource: Survey of China's Inclusive Finance Center.

The first is that the interest rate is relatively high. When asking the peasants why they can't obtain credit, the importance levels of reasons they give are shown in Table 6. "Interest rate is too high" is the most important reason. Most peasants' ability to endure high interest rate is low. This is related to two reasons. The first is that the traditional agricultural production is still the main mode in Shandong rural area, which can not bring enough cash flow. The second is that departure of main labor force from rural area is serious, and most of the left peasants are elder and children, who haven't the ability to afford high interest rate.

The second reason is the baffle from mortgage and guarantee. "Lack of mortgage or guarantee" is also an important reason according to table 6. Peasants' mortgage is very few. They don't have enough tradable assets, such as valuable machine, cars, buildings and so on. The trading of their assets, such as land contract management right, housing land use right can not be carried out freely and therefore the mortgage using these assets are facing some problems.

Peasants can not afford the high interest rate required by the financial institutions or provide proper mortgage means that the effective demand from the peasants are insufficient, which can also be understand as the products from the financial institutions are not suitable for peasants. This needs the collective efforts from the peasants, financial institutions and the society.

The third reason is the willing for financial institutions to take part in rural financing market is low. According to Table 6, "Can't find relationships needed" is the second important reason, which means that the supply is less than the demand of the products from the financial institutions and "credit rating" in rural financial market is serious.

The fourth reason is that some of the products from the financial institutions can not cater to the peasants' demands. According to Table 6, "Credit amount is too small", "Time limit is too short" also effect peasants credit. This means that the some products from the financial institutions are not of much help to peasants. According to table 5, among the peasants who want to be financed but are not financed, there are still 35.63% peasants can afford a high interest rate (5% and higher). This means they have the ability to afford interest rate, but they can not obtain credit, which is really a pity. If they have proper mortgage or the financial institution supply proper and more products, maybe this part of credit demand will be satisfied.

#### **4. Choosing Proper Rural Financial Supply Mode to Enlarge the Fund Supply**

Firstly, the subsidy finance should not be the main mode. The best way to decrease interest rate is subsidy. Public finance can set up special institutions to provide low or non interest-rate credit without mortgage. But the efficiency of this kind of credit is usually low and goes against resource optimal allocation. "Credit subsidy theory" believes outside fund should be pulled into rural area because local deposits are insufficient due to the low economic development level. And also due to the low economic development level, the ability to repay the interest is low. Therefore, in rural area, it is better to develop subsidy finance, not commercial finance. But according to investigation of CIFC, the average fund supply to the financial institution from the peasants is RMB 57600, the average fund obtained by peasants from financial institution is RMB67100 and only 12% of all the peasants can obtain credit, therefore, conclusion that peasants saving are enough to satisfy their own fund demand can be safely deduced. So generally speaking, the rural financing in Shandong province is not necessary to depend on outside fund. In the initial phase of economic development, these subsidy financial institutions may be the main mode to supply financial resource firstly to stimulate the economy. But when the economy develops to a higher level, subsidy financial institutions should withdraw and give way to commercial finance to enhance the efficiency of financial resources and make these resources to flow to economic units with higher productivity. And at this stage, the aim of subsidy financial institutions is to maintain the society's stability and not to give impetus to economic growth. The income per capita of Shandong's peasants is much higher than that of the whole country (Note 1) and Shandong' economy has reached to a certain level. Therefore, the commercial financing, not the subsidy financing should be the main mode in Shandong's rural area.

Secondly, national or large financial institutions are not necessary in Shandong rural market because the deposit from the peasants is sufficient. Regional (provincial, city-wide or county-wide) or small financial institution has the possibility to obtain sufficient fund resource. Besides, these kinds of financial institutions may have their own merits. When financial institutions provide products to peasants, the biggest problem is the information asymmetry. There is no good way to solve this problem and has to resort to mortgage. But the mortgages from the peasants are insufficient, which is an acute conflict in today's rural financial market. In current situation, it is difficult to make the peasants have enough mortgages in a short period. Therefore financing ways that need mortgage less are more preferred. Informal finance often needs no mortgage. One reason is that informal finance bodies are familiar with the peasant demander because they are near to each other. Inspired by informal finance,

to develop local small financial institutions is a feasible way. Because they are local, the institutions may have more information about the peasants, which can make the institutions learn more about the peasants demand and at the same time, alleviate the dependence on mortgage. But according to the investigation from CIFC, small financial institutions, such as village bank, small loan company, rural fund mutual cooperative are rare in Shandong Province. So more regional or small financial institutions should be built up. When developing these institutions, a series of preferential are needed, such as lower reserve requirement ratio, lower tax rate and so on. Besides, deposit insurance system must be built up so peasants may dare to supply their fund to these institutions and solve the fund resources problem.

Mutual folk finance should still play an important role in Shandong' rural market. According to the data from CIFC, among the fund obtained by peasants from financial market, fund from mutual folk finance occupied 32.04%, which is higher than rural credit cooperatives (30.24%) and large-and-medium-size formal financial institutions(21.33%). The biggest merit of mutual folk finance is low or with no interest. But this interest rate referred to the monetized portion. Although the monetized interest rate is a little or even none, but other kinds of interest rate still exist, for example, to help the money suppliers working or give them local specialty. In the circumstance that the monetization level is low, use other things as interest is a positive way. Besides, mutual folk finance come into being depending on kinship, friendship and geo-relation, the information asymmetry may be solved better and mortgage is not needed in many circumstances.

## 5. Conclusions

Generally speaking, the services from the financial institution or market are not sufficient because financial institution can not supply enough proper products and the effective demand from the peasant is insufficient, which are represented as high interest rate, no enough mortgages, a certain degree of impracticality of financial products and financial institutions' reluctance to act in this market. In order to solve the problem, an important way is to develop proper kind of financial institutions. In Shandong rural area, small and regional commercial finance should take the main part of the financial market because the sufficient fund resource and the advantages of these financial institutions. Besides, mutual folk finance is also needed in the current circumstance of low monetization level.

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## Note

Note 1. In Shandong province, the income per capita of Shandong's peasants is RMB 10620, and that of the whole country is RMB 8896.

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