

# VI INTRODUCTION TO THE CASE STUDIES

## OBJECTIVE OF THE STUDY

The general objective of this study was to analyze developments in the provision and use of financial services in rural Asia since the 1970s. In view of the large number of Asian economies, we used the country-case-study method and focused on three main features in each case: analysis of the general financial-sector strategy of the country, and specific policies implemented regarding rural financial markets to determine how they affect the framework within which the country's rural financial system operates; the evolution and trends in the structure, conduct, and performance of the rural financial markets; and analysis of information, where available, at the levels of both the financial institutions and rural firms and households, on the impact of rural financial development. Following the analyses, recommendations are made about the changes in policies, financial infrastructure, and institutional development needed to promote the establishment of rural financial markets that are consistent with sustainable development.

Chapters II and III presented a summary of the conceptual evolution that has occurred since the 1970s regarding rural financial markets. These chapters reviewed the basic functions of financial markets, identified the major participants in those markets, described the paradigm shift that is occurring in approaches to financial market development, summarized some of the recent developments in microfinance, and presented a

three-pronged framework to use in evaluating the needs and constraints of the rural financial system. The same general outline is followed for each of the six case studies presented here. However, each case is based almost exclusively on available literature, the extent of which varies considerably from country to country; the content and level of detail provided for each case varies correspondingly.

## SELECTION OF CASE-STUDY COUNTRIES

The rural economy of Asia is huge, heterogeneous, and defies easy categorization and analysis. On the one hand, Asia is home for some of the most dynamic and successful agribusinesses in the world, that satisfy domestic food demands and penetrate competitive foreign markets. On the other hand, it is home for millions of poor people who are only slightly better off than their ancestors. Prior to the financial and economic crisis that began in 1997, the region had some of the fastest-growing economies in the world but also some with poor economic performance. Moreover, some of the transition and conflict-affected countries in the region have even experienced negative growth rates. The rural financial markets in a few countries are served by strong financial institutions that provide sophisticated services on market terms, while others are dominated by weak and subsidized institutions and NGOs that are dependent on donors and whose sole function is to dispense credit.

An analysis of rural financial markets in Asia must attempt to account for this heterogeneity. Since it was impossible in this study to cover all economies in the region, the decision was made to select cases that reflect the broad range of circumstances and approaches to financial market development found in the region. Each of the six countries selected represents a particular kind of scenario.

Bangladesh and India were chosen to represent South Asia. Typical of this region, they are poor, densely populated, and the State has intervened heavily in their financial sectors.

Bangladesh has received massive amounts of donor support to develop the world's most comprehensive NGO-based system of lending to the poor. India, however, has aggressively imposed quotas and mandates on commercial banks in attempts to force them to expand the financial frontier into rural areas, and has established a vast network of regional rural banks and cooperatives.

The Kyrgyz Republic and the PRC represent Central Asia. Both are in transition from centrally planned to market economies. The PRC began to liberalize its rural economy as early as the late 1970s while the Kyrgyz Republic did not begin until a decade later. The PRC is an old country that is modernizing old institutions while the Kyrgyz Republic is new and has to build many institutions from scratch. The former is a huge, heavily populated country while the latter is comparatively small in size and population. The PRC has been among the world's leaders in agricultural growth in recent years while the Kyrgyz Republic has experienced negative growth. Both countries have made little progress in developing strong market-oriented financial institutions for rural areas.

Indonesia and Thailand in Southeast Asia represent rapid-growth economies that were severely impacted by the financial and economic crisis in the region that began in 1997. Both are experiencing a decline in average farm sizes but have dynamic agribusinesses, especially Thailand. Both countries are known worldwide for having developed rural financial institutions that today serve millions of clients with a minimum of subsidies.

## COMPARATIVE ANALYSIS

### Economic Growth

The six countries have widely different income levels (Table VI.1). In 1996, Thailand, the richest country, had a per capita GDP (\$1,956 in 1987 dollars) almost ten times that of the poorest country, Bangladesh (\$212). India's level (\$464) was roughly

double that of Bangladesh. Estimates for the Kyrgyz Republic have been quite volatile and were reported to be \$555 in 1995 dollars, while the PRC was about the same level but in 1987 dollars (\$515). Indonesia's GDP per capita (\$748) was about 50 percent higher than the PRC but less than half that of Thailand.

Real GDP per capita growth rates for Bangladesh and India have been under 4 percent per year since 1967, while the rates for Indonesia and Thailand have been in the 4 to 7 percent range. The PRC's growth rate has been higher than 8 percent since 1980. The Kyrgyz Republic is the exceptional case, reporting an annual negative growth rate of 12 percent in the 1990s.

**Table VI.1: GDP and GDP Per Capita Growth Rates**

Item	Bangladesh	India	Kyrgyz Republic	PRC	Indonesia	Thailand
Per Capita 1996 GDP (constant 1987 \$)	212	464	555 <sup>a</sup>	515	748	1,956
Annual Growth Rates (%) of Per Capita GDP (constant 1987 \$)						
1967–1980	-0.50	1.34		5.18	4.98	4.32
1980–1989	2.02	3.61		8.25	4.05	5.58
1989–1995	2.74	3.39		9.59	6.28	7.76
1980–1995	2.31	3.52	-12.0 <sup>b</sup>	8.79	4.93	6.45

<sup>a</sup> In 1996 dollars.

<sup>b</sup> Real GDP annual growth rate.

Sources: ADB (1997c); World Bank (1998c).

## Land, Population, and Agriculture

The enormous differences in the size and population of these six countries can be seen in the data in Table VI.2. The PRC has about 9.6 million square kilometers (km<sup>2</sup>). India is approximately one third that size, Indonesia one fifth, Thailand one twentieth, and the Kyrgyz Republic and Bangladesh only about one fiftieth. Their respective population densities give a quite different perspective. Bangladesh is in a category all its

Table VI.2: Land, Population, and Agriculture

Item	Bangladesh	India	Kyrgyz Republic	PRC	Indonesia	Thailand
Total Area (km <sup>2</sup> '000)	144.0	3,287.6	198.5	9,561.0	1,904.6	513.1
Population (1997) (millions)	125.6	955.2	4.7	1,230.0	199.9	60.6
Annual Population Growth Rate (%) (1993–1997)	1.9	2.0	0.9	1.1	1.6	1.1
(1993–2010) <sup>a</sup>	1.7	1.5		0.8	1.3	0.7
Population Density (persons/km <sup>2</sup> , 1997)	872	291	23	128	105	118
Rural Population as Percent of Total Population						
1975	90.7	78.7	62.1	82.7	80.6	84.9
1985	86.6	75.7	61.8	77.5	73.9	82.1
1995	81.1	72.8	60.8	68.9	63.7	79.6
Share of Agricultural Labor in Total Labor Force (%)						
1966	85.16	73.73		80.25	69.70	81.37
1975	78.01	71.08		76.26	62.08	75.37
1985	68.90	66.74		73.24	56.46	67.48
1995	60.56	61.87		69.54	51.78	60.32
Cropped Area per Capita (ha, 1994)	0.08	0.18	0.32	0.08	0.16	0.36

<sup>a</sup> Source: Projections of the International Food Policy Research Institute, Washington DC.

Sources: ADB (1997c); Rosegrant and Hazell (1999).

own with nearly 900 people per km<sup>2</sup> in 1997; India is second with about one third that density. The PRC, Indonesia, and Thailand have just over 100 people per km<sup>2</sup>, while the Kyrgyz Republic has only 23. In addition, there are considerable differences in population density within the countries.

Annual population growth rates are still about 2.0 percent for Bangladesh and India, which is consistent with their low income levels. The PRC, Kyrgyz Republic, and Thailand are at about 1 percent, while Indonesia is 1.6 percent.

Countries and regions within countries with very high population densities offer the potential to create highly concentrated financial programs that can provide small loans and deposit services to a large number of poor clients in a relatively small area. The entire country of Bangladesh fits this

situation. Programs operating in sparsely populated areas, however, face a difficulty in achieving high levels of bank staff productivity. Even though the PRC has a huge population, this country is implementing lending programs for the poor in relatively sparsely populated areas.

The differences in land quality among the six countries are reflected in the amount of cropped area available per capita. These estimates place Bangladesh, the poorest of the six, and the PRC in the same category of having only 0.08 hectares (ha) per capita. India and Indonesia are somewhat better off with roughly twice as much land per capita. The Kyrgyz Republic and Thailand are the two relatively land-abundant countries with over 0.30 ha per capita. The share of agricultural labor in the total labor force is declining in all six countries. It is surprising, however, that with the relatively high per capita income in Thailand, that country still has about 60 percent of its population employed in agriculture, which is about equal to the level in Bangladesh, the poorest country.

The reported growth rates in agricultural productivity reflect general perceptions about these countries (Table VI.3). Bangladesh's agricultural growth rates are low and were lower in the 1990s than in the previous decade. Indonesia and India have had fairly strong agricultural annual growth rates of about 3 percent. Thailand is intermediate with 3.6 percent growth while the PRC has the highest rate, close to 5 percent. With the exception of Bangladesh and the Kyrgyz Republic, the rate of agricultural growth has surpassed population growth rates, thereby providing room for improvement in per capita food consumption.

The sources of agricultural productivity growth reveal fairly consistent patterns since 1961. The PRC has had consistently high growth rates in both labor and land productivity, as has Indonesia. India has had a slightly slower productivity growth than Indonesia in both indicators. Thailand's performance has been poorer than these three cases but has been somewhat better than Bangladesh in labor productivity growth. The relatively poor performance of Bangladesh implies that it has been especially difficult for that country to improve rural incomes and food availability per capita.

Table VI.3: Growth in Agricultural Productivity

Item	Bangladesh	India	Kyrgyz Republic	PRC	Indonesia	Thailand
Average Annual Growth Rate of Agriculture (%) <sup>a</sup>						
1980–1990	2.7	3.1		5.9	3.4	4.0
1990–1996	1.2	3.1	-4.6	4.9	2.8	3.6
Annual Growth Rates in Labor Force in Agriculture (%)						
1961–1969	1.02	1.19		4.04	0.79	2.08
1970–1979	1.11	1.41		0.77	0.60	1.97
1980–1989	1.79	1.54		0.65	0.83	1.39
1990–1993	2.06	1.14		-0.08	0.40	0.42
Annual Growth Rates in Labor Productivity per Worker in Agriculture (%) (dollars/worker)						
1961–1969	0.37	1.37		1.48	2.51	1.91
1970–1979	1.29	2.62		2.90	2.32	0.69
1980–1989	0.21	1.62		5.39	1.92	1.44
1990–1993	0.57	1.74		2.66	2.33	1.50
Annual Growth Rates in Land Productivity in Agriculture (%) (dollars/ha)						
1961–1969	1.39	2.78		3.40	3.95	1.56
1970–1979	1.50	3.60		1.61	2.06	1.14
1980–1989	2.86	3.03		5.62	3.96	2.07
1990–1993	1.73	3.04		3.43	3.48	1.56

<sup>a</sup> World Bank (1998c).

Sources: FAOSTAT. Agricultural Production Indices, 3 November 1998; Land-Use Domain, 22 May 1998; Population Domain, 24 August 1998. Available: <http://faostat.fao.org>. See also Rosegrant and Hazell (1999).

## Structural Transformation

The evolution in the GDP share of the major sectors of the economy has followed the classic pattern of structural transformation (Table VI.4). The agricultural share has declined in all countries over the 22-year period from 1975. With the exception of the Kyrgyz Republic, there is an inverse relationship between the share of agriculture in GDP and per capita GDP.

**Table VI.4: Share of Major Sectors in GDP**  
(percent)

	Agriculture			All Industry			Services		
	1975	1985	1997 <sup>b</sup>	1975	1985	1997 <sup>b</sup>	1975	1985	1997 <sup>b</sup>
Bangladesh	59.1	41.8	29.3	11.1	16.0	17.5	29.8	42.3	53.2
India	40.5	33.0	27.0	23.7	28.2	30.0	35.8	38.8	43.0
Kyrgyz Republic			46.5			21.4			32.1
China, People's Rep. of	34.0 <sup>a</sup>	28.4	20.2		43.1	49.0		28.5	30.8
Indonesia	31.7	23.2	16.1	33.8	35.8	43.9	34.6	40.9	40.1
Thailand	26.9	15.8	11.2	25.8	31.8	39.8	47.3	52.3	48.9

<sup>a</sup> World Bank (1997a) for the PRC for 1970.

<sup>b</sup> ADB (Available: <http://www.adb.org>) for 1997 data.

Source: ADB (1997c).

The 11 percent agricultural share for Thailand is especially low considering that 60 percent of the population is still employed in agriculture, suggesting a potentially large emerging gap in incomes between rural and urban areas. However, as discussed in the case study, this gap has been reduced through nonfarm income earned by farmers. The patterns are not so consistent for industry and services across the six countries. The PRC has a larger share of GDP in industry than implied by its per capita GDP, while Thailand has a relatively lower share. Likewise, the size of the service sector in India, and especially Bangladesh, is higher than expected from their per capita incomes.

## Financial Deepening

Financial deepening refers to the growth of the financial sector relative to the rest of the economy. As the economy modernizes, financial deepening occurs because the financial sector must accommodate the demands of a more productive and sophisticated production sector. A popular measure of financial deepening of the banking sector is the ratio of  $M_2$  to GDP where  $M_2$  refers to the sum of money in circulation plus

near money such as savings accounts. This ratio is reported for the six countries in Table VI.5.

Table VI.5:  $M_2$ /GDP

Year	Bangladesh	India	Kyrgyz Republic	PRC	Indonesia	Thailand
1975	0.11				0.16	0.34
1980	0.19	0.46		0.37	0.17	0.38
1985	0.26	0.51		0.54	0.24	0.56
1990	0.30	0.56		0.79	0.40	0.70
1996	0.35	0.55	0.16	1.12	0.55	0.80

Sources: ADB (1997c).

All the case-study countries showed significant increases in financial deepening of the banking sector during the past two decades. The rates of change have been quite different, however. The PRC reported a sharp increase in savings in the 1990s; its  $M_2$ /GDP ratio surpassed 1.0 in 1996. Thailand's  $M_2$ /GDP ratio more than doubled from 0.34 to 0.80 in the same period. India and Indonesia were at the same level of 0.55 in 1996, but India started from a higher base and has grown more slowly. Bangladesh recorded a low ratio, 0.35, while the Kyrgyz Republic was even lower at 0.16, indicating the limited role that the financial sector plays in that transition economy.

These data provide insights into the role of the financial systems in these countries. Evidently banking is relatively more important in the PRC and Thailand than in the other countries. In the former case, savings have grown enormously due to rapid income growth and the absence of consumption and private investment alternatives. In Bangladesh and the Kyrgyz Republic, a large amount of money circulates outside the banking system. Some savings are mobilized by NGOs in Bangladesh, but they are not reported in bank statistics. Inefficiencies in banking and restrictions on interest paid on savings are additional explanations for the low levels of financial deepening observed in some countries.

