

Micro-loans Secured by Time Deposits

-- The Beginning of Lending Operations for China Postal Savings

By the Postal Savings and Remittance Bureau, China Post

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Background of the Pilot on Micro-loans Secured by Time Deposits

On 19 March 2006, the very first micro-loan, disbursed by the Postal Savings in the Fujian Province of China, ended a 20 year history of non-lending operations by the Postal Savings and Remittance Bureau (hereafter referred to as China Postal Savings).

Since the restoration of the deposit operations within the China Post in 1986, China Postal Savings has been in operation for the last 20 years. As a special financial institution, China Postal Savings had the permit to engage in non-lending operations, including the organization of deposits from individuals, domestic and international money transfers, acting as agent for insurance companies and state treasury bonds, and handling bill payment services. Prior to August 2003, the Postal Savings was obliged to re-deposit all its deposits with the PBC (the People's Bank of China), China's central bank, and the latter paid a higher rate of interest for the re-deposits from the Postal Savings than from other financial institutions in China. From August 1, 2003 onwards China Postal Savings was required to manage its own liabilities by providing wholesale funds to the policy and commercial banks in China and purchasing bonds and debentures from certain commercial banks. Its remaining balance of re-deposits with the PBC as of the end of July 2003 had to be transferred back to the Postal Savings within five years. Due to that regulation, the uses of Postal Savings funds were very limited.

In order to create new channels for the use of the funds, the Postal Savings has conducted in-depth research and experimentation. Following a pilot on the micro-loans secured by term deposits in the Shaanxi Province and further studies by the Postal Savings, it was decided that the micro-loan operations of the Postal Savings should start with the micro-loans secured by time deposits. Accordingly, Postal Savings lodged an application with the China Banking Regulation Commission (CBRC) for a permit to operate micro-loans secured by time deposits. In March 2006, CBRC issued a permit for the Postal Savings to pilot micro-loans secured by time deposits in certain areas of Fujian, Hubei and Shaanxi provinces. The first micro-loan secured by time deposits was disbursed in Fujian Province on March 19, 2006 quickly followed by the Postal Savings in the two others provinces on March 29, 2006.

Development of the Micro-loans Secured by Time Deposits

Micro-loans secured by time deposits are small-size term loans issued by China Postal Savings and secured by un-matured term deposits in RMB. A loan applicant can use his/her own deposits or the deposits of a third party to secure micro-loans. The loan term is within 12 months, the PBC base lending rates apply for the micro-loans, and the ceiling for the micro-loans is currently set at RMB 100,000.

The market for micro-loans secured by time deposits is huge, with large unmet demand for micro-credit from middle and low-income households in rural China. Rural households can access a micro-loan without withdrawing a time deposit in advance, which avoids the interest loss. A deposit holder can also help friends and relatives access micro-loans through pledging his/her deposit certificates.

Considering the market demand, income levels of potential clients and distribution of post outfits, China Postal Savings believes that this kind of micro-loan can target small and poor farmers. Moreover, micro-loans would enable China Postal Savings to develop its markets rapidly and to learn by doing. This would enable China Postal Savings to conduct successful lending operations and to develop other micro-loan products in the future.

To administer the micro-loans well, China Postal Savings has set up and upgraded its loan application and approval procedures and improved its management of branches and staff. The procedures of loan application, approval and disbursement, the suspension of payment for the time deposits as security, accounting and settlement, have been computerised so as to mitigate risks for micro-loans. For fund flows, micro-loans and deposits have been operated on two parallel channels. Finally, the cost centre for the operation of micro-loans secured by time deposits has been set up at the Provincial Office, instead of at the branches. The cash system is applied to the interest income and expenses.

The limited experience from the pilot indicates that the measures above have contributed positively to the development of micro-loans secured by time deposits. By July 25, 2006, 445 outlets of Postal Savings in 102 counties of 24 prefectures of Fujian, Hubei and Shaanxi provinces have disbursed micro-loans secured by time deposits. The cumulative micro-loans in the three provinces reached RMB 200 million, the loan portfolio reached RMB 76.68 million, and the average loan size was RMB 30,000. So far no non-performing loans have been recorded (see Table 1).

Table 1. Development of Micro-loans Secured by Time Deposits (RMB 10,000)

Province	Cumulative Applications		Cumulative Disbursement		Repayment	
	Amount	No.Loan	Amount	No.Loan	Amount	No.Loan
Fujian	8089.49	1368	6748.49	1161	5135.14	944
Shaanxi	9121.24	3965	6727.18	3049	3496.88	1585

Hubei	8363.41	2998	6520.79	2402	3696.78	1351
Total	25574.14	8331	19996.46	6612	12328.80	3880

Source: China Postal Savings, by 25 July 2006

Micro-loans Secured by Time Deposits Make Rural Credit More Accessible

For a long time, rural economic development in China has been plagued by the lack of a competitive rural financial market with diversified suppliers of rural credit. The shortage in the supply of rural credit has become a major obstacle for farmers in developing their production and increasing their incomes. In some areas, a shortage in credit supply has led to widespread rural usuries. Since the pilot by China Postal Savings in March 2006, the credit access of the farmers in the pilot areas has improved considerably, thanks to the low lending rate charged (in accordance with the national benchmark interest rate) and the rapid loan services with simplified procedures (an applicant with a valid deposits account and an identification card can get a micro-loan within two days after application). This tends to boost rural economic development as well as increase farmer income in these areas.

“With the help of micro-loans secured by time deposits, my dream of pond production of fish comes true,” a borrower exclaimed over the counter at the Liujiachang outlet of Songzi City. Her name is Peng Youfang, from Group 7, Wuxidi Village, Chendian Township of Songzi City in Hubei Province. It has long been her desire to contract a fishpond, but she couldn’t find enough money to do so as she had to pay for her children’s schooling expenses and cover daily consumption from her limited family income. She was deeply moved when her mother-in-law offered her a Postal Savings deposit of RMB 15,000 for her to undertake fish production. But she declined the offer, as the time deposit was the lifetime savings of her mother-in-law and the only money available for her old age. After she learnt about the micro-loan secured by time deposits program advertised on TV, she and her mother-in-law went to Liujiachang Post Office Branch the next day, bringing the RMB 15,000 time deposit certificate with them. With the help from the branch staff, she was able to fill out the application form immediately and her application was quickly processed. She was told that she could receive her loan before 2 p.m. on the same day. Peng was overjoyed and said: “like me, many other farmers also need micro-loans. Compared to loans from commercial banks, the lending rate of the post saving micro-loans is lower, the loan processing time is shorter and the services are better. If I need another loan in the future, I will come back to the branch.”

In the areas where micro-loans secured by time deposits have started, there are many other farmers who, like Peng, have benefited from the micro-loans secured by time deposits pilot programs. Many farmers have become repeat clients, repaid a loan and then borrowed a loan from the Postal Savings.

A Trial Lending Program for China Postal Bank

There has been significant public concern about the establishment of a Post Bank in China after July 2005 when the State Council passed ‘the Postal Reform Plan.’ The public refocused on China Post Bank after June 2006 when CBRC approved the establishment of China Postal Savings Bank. The current micro-loans secured by time deposits can be regarded as a trial lending operation for the China Postal Savings Bank to be set up soon.

In a recent interview by the Financial Times, Mr. Tao, the Director General of China Postal Savings, stated: "despite a relatively simple and low-risk product for commercial banks, micro-loans secured by time deposits is a brand new product for us. Using the pilot, we hope to develop our credit culture, train our staff, increase our revenues and improve our image. The outcome of the pilot will be judged by the objectives. Following a successful pilot, we are going to replicate it and gradually start up new loan products, from partial deposit pledged loans, to individual micro-loans on collateral, group guarantee loans, and to individual loans, etc. Currently, we have completed the baseline surveys and system building, and are working on the computerized system."

Some commentators note that the ‘test fly’ of micro-loans secured by time deposits can benefit the Postal Savings by raising the market awareness of Postal Savings staff, as staff can learn by doing. This will undoubtedly be conducive to developing effective the Postal Savings Bank’s credit operations in the future and prepare Postal Savings for a real take-off.

By offering loan products, China Postal Savings is in a position to develop itself into a large-scale full service provider for microfinance services in China. Currently China Postal Savings has 35,000 outlets throughout China. The savings deposits organized by China Postal Savings reached more than RMB 1,255 billion (about US\$ 156 billion).

The Great Help Received from the Bank Regulator

The relationship between the bank regulators and banks is often described as the relationship between cats and rats. However, this has not been the case for the micro-loans secured by time deposits launched by China Postal Savings.

In Fujian Province, the CBRC officers responsible for supervising Postal Savings were called ‘teachers’ by the Postal Savings staff. For Chen Dan, deputy director of Fujian Postal Saving Bureau, the ‘teacher’ is Chen Qiong, deputy director of Fujian Banking Regulation Bureau.

“During the operation of micro-loans secured by time deposits in Fujian, Chen Qiong and her team gave us a lot of assistance, and we are like a family,” said Weng Hongnian, director of Fujian Postal Saving Bureau. He added: “Pan Jie, the deputy director of Fujian Post Office and my direct boss once mentioned to me that our development will be faster, if other government departments are as efficient as the

CBRC Office in the province - you should not complain, if you are punished by the CBRC in the future in light of the amount of help you have already received from them.”

According to Chen Qiong, any changes have their internal and external causes. The bank regulator can help only if a financial institution is willing to be supervised. The sound relationship between the Postal Savings and the CBRC in the province is based on the desire of the Postal Savings to receive the supervision from the CBRC. Mr. Weng also mentioned that: “Mr. Tao Liming, Director General of China Postal Savings Bureau, made it clear to me that my task is to turn Fujian Postal Saving into a real bank, which needs to be authorised by the CBRC.” Perhaps the strong desire of performing well for micro-loans from the top down in China Postal Savings has contributed to the positive interaction between the supervisors and Postal Savings. Such a positive interaction has in turn ensured a stable and healthy development of the micro-loan pilot with Postal Savings.

In addition, the CBRC has paid great attention to the flow of funds back into rural areas. According to Cai Esheng, Vice Chairman of the CBRC: “micro-loans secured by time deposits are an experiment with the reform of China Post.” China Post should take the opportunity and use micro-loans to help build China’s new socialist countryside.” Liu Andong, the Director of China Post, and Mr. Tao Liming have repeatedly called for the channeling of funds back into rural areas to support building China’s new socialist countryside. The common goal of channeling funds back into rural areas has made the CBRC and China Postal Saving work hand in hand.