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PROJECT PERFORMANCE ASSESSMENT REPORT

VIETNAM RURAL FINANCE PROJECT (C 2855)

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*Sector Evaluation Division
Independent Evaluation Group*

Currency Equivalents (annual averages)
March 1996. US\$1 = VND11,018; September 2002. US\$1 = VND15,250

Abbreviations and Acronyms

ACB	Asia Joint Stock Commercial Bank
ADB	Asian Element Bank
BIDV	Bank for Investment and Development of Vietnam
CAR	Capital Adequacy Ratio
CAS	Country Assistance Strategy
DFID	Department for International Development (UK)
EAB	East Asia Joint Stock Commercial Bank
ERR	Economic Rate of Return
FRP	Fund for the Rural Poor
FRR	Financial Rate of Return
GOV	Government of Vietnam
GTZ	German Technical Assistance Agency
IAS	International Accounting System
ICR	Implementation Completion Report
IDA	International Development Association
IEG	Independent Evaluation Group (earlier OED)
IEGWB	Independent Evaluation Group (World Bank)
JICA	Japanese International Cooperation Agency
M&E	Monitoring and Evaluation
MTR	Midterm Review
NAB	North Asia Joint Stock Commercial Bank
NPL	Non Performing Loan
PAD	Project Appraisal Document
PCF	People's Credit Fund
PFI	Participating Financial Institution
PhNB	Southern Joint Stock Commercial Bank
PPAR	Project Performance Assessment Report
RDF	Rural Development Fund
RFI	First Rural Finance Project
RFII	Second Rural Finance Project
RFIII	Third Rural Finance Project
RKB	Rach Kien Auroral Joint Stock Commercial Bank
SAR	Staff Appraisal Report
SBV	State Bank of Vietnam
SME	Small and Medium Enterprise
SOE	State Owned Enterprise
VBARD	Vietnam Bank for Agriculture and Rural Development
VBP/VBSP	Vietnam Bank for the Poor
VND	Vietnamese Dong

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IEGWB Mission: Enhancing development effectiveness through excellence and independence in evaluation.

About this Report

The Independent Evaluation Group assesses the programs and activities of the World Bank for two purposes: first, to ensure the integrity of the Bank's self-evaluation process and to verify that the Bank's work is producing the expected results, and second, to help develop improved directions, policies, and procedures through the dissemination of lessons drawn from experience. As part of this work, IEGWB annually assesses about 25 percent of the Bank's lending operations through field work. In selecting operations for assessment, preference is given to those that are innovative, large, or complex; those that are relevant to upcoming studies or country evaluations; those for which Executive Directors or Bank management have requested assessments; and those that are likely to generate important lessons.

To prepare a Project Performance Assessment Report (PPAR), IEGWB staff examine project files and other documents, interview operational staff, visit the borrowing country to discuss the operation with the government, and other in-country stakeholders, and interview Bank staff and other donor agency staff both at headquarters and in local offices as appropriate.

Each PPAR is subject to internal IEGWB peer review, Panel review, and management approval. Once cleared internally, the PPAR is commented on by the responsible Bank department. IEGWB incorporates the comments as relevant. The completed PPAR is then sent to the borrower for review; the borrowers' comments are attached to the document that is sent to the Bank's Board of Executive Directors. After an assessment report has been sent to the Board, it is disclosed to the public.

About the IEGWB Rating System

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Outcome: The extent to which the operation's major relevant objectives were achieved, or are expected to be achieved, efficiently. The rating has three dimensions: relevance, efficacy, and efficiency. Relevance includes relevance of objectives and relevance of design. Relevance of objectives is the extent to which the project's objectives are consistent with the country's current development priorities and with current Bank country and sectoral assistance strategies and corporate goals (expressed in Poverty Reduction Strategy Papers, Country Assistance Strategies, Sector Strategy Papers, Operational Policies). Relevance of design is the extent to which the project's design is consistent with the stated objectives. Efficacy is the extent to which the project's objectives were achieved, or are expected to be achieved, taking into account their relative importance. Efficiency is the extent to which the project achieved, or is expected to achieve, a return higher than the opportunity cost of capital and benefits at least cost compared to alternatives. The efficiency dimension generally is not applied to adjustment operations. Possible ratings for Outcome: Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Risk to Development Outcome: The risk, at the time of evaluation, that development outcomes (or expected outcomes) will not be maintained (or realized). Possible ratings for Risk to Development Outcome: High Significant, Moderate, Negligible to Low, Not Evaluable.

Bank Performance: The extent to which services provided by the Bank ensured quality at entry of the operation and supported effective implementation through appropriate supervision (including ensuring adequate transition arrangements for regular operation of supported activities after loan/credit closing, toward the achievement of development outcomes. The rating has two dimensions: quality at entry and quality of supervision. Possible ratings for Bank Performance: Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Borrower Performance: The extent to which the borrower (including the government and implementing agency or agencies) ensured quality of preparation and implementation, and complied with covenants and agreements, toward the achievement of development outcomes. The rating has two dimensions: government performance and implementing agency(ies) performance. Possible ratings for Borrower Performance: Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Contents

PRINCIPAL RATINGS.....	V
KEY STAFF RESPONSIBLE.....	VI
PREFACE	VII
SUMMARY	IX
1. BACKGROUND	1
2. THE PROJECT	2
Objectives	2
Project Design	2
Quality at Entry	3
Implementation.....	4
3. PERFORMANCE RATINGS	4
Outcome.....	4
Relevance	4
Efficacy.....	7
Efficiency	12
Risk To Development Outcome.....	13
Bank Performance.....	16
Borrower Performance	16
Monitoring and Evaluation	17
4. FINDINGS AND LESSONS	18
REFERENCES.....	21
ANNEX A. BASIC DATA SHEET.....	23
ANNEX B. BACKGROUND AND ENABLING ENVIRONMENT	25

ANNEX C. PEOPLE MET**31**

ANNEX D. BORROWER COMMENTS**33**

This report was prepared by Ridley Nelson (Consultant), John Heath and Nalini Kumar (Task Team Leaders). Ridley Nelson assessed the project in February-March 2009. Marie Charles provided administrative support.

Principal Ratings

VIETNAM RURAL FINANCE PROJECT (VRFP)

	<i>ICR*</i>	<i>ICR Review*</i>	<i>PPAR</i>
Outcome	Satisfactory	Satisfactory	Satisfactory
Institutional Development Impact **	Substantial	Substantial	
Risk to Development Outcome			Moderate
Sustainability ***	Highly Likely	Likely	
Bank Performance	Satisfactory	Satisfactory	Satisfactory
Borrower Performance	Satisfactory	Satisfactory	Satisfactory

*The Implementation Completion Report (ICR) is a self-evaluation by the responsible operational division of the Bank. The Evaluation Summary (ES) is an intermediate IEGWB product that seeks to independently verify the findings of the ICR.

** As of July 1, 2006, Institutional Development impact is assessed as part of the Outcome rating.

*** As of July 1, 2006, Sustainability has been replaced by Risk to Development Outcome. As the scales are different, the ratings are not directly comparable.

Key Staff Responsible

VIETNAM RURAL FINANCE PROJECT (VRFP)

<i>Project</i>	<i>Task Manager/Leader</i>	<i>Division Chief/ Sector Director</i>	<i>Country Director</i>
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Preface

This report is the Project Performance Assessment Reports (PPAR) for the Vietnam Rural Finance Project (VRFP) (Credit 2855) approved on May 7, 1996 and closed on December 31, 2001.

The report was prepared by the Independent Evaluation Group (IEG). The assessment is based on the project completion and appraisal reports, the Development Credit Agreements, a review of Bank files, and discussions with beneficiaries, Bank staff, government officials, non-governmental organizations, institutions, donors, and private sector managers. The cooperation and assistance of all stakeholders and government officials is gratefully acknowledged, particularly the staff of BIDV. Also acknowledged is the support of the World Bank Country Office in Vietnam.

Following standard IEG procedure, copies of the draft PPAR have been sent to the government for their review and comments. Borrower comments have been included in Annex D.

Summary

This report assesses the performance of the Vietnam Rural Finance Project (RFI) approved on May 7, 1996 and closed on December 31, 2001. It also looks at the evolution of that first project into the follow-on Rural Finance II and III projects, the latter recently effective.

The enabling environment at the time was only fair. Rural sector lending was dominated by a state-owned bank, the Vietnamese Bank for Agriculture and Rural Development (VBARD), with a number of weaknesses in performance indicators. Shortly before the project, the Vietnamese Bank for the Poor (now called the Vietnamese Bank for Social Policy (VBSP)), had been hived off from VBARD to cover subsidized lending to the poor. However, apart from this subsidized lending, there were a number of other subsidized programs and the intermittent imposition on banks of interest rate ceilings for borrowers. The Bank chose to accept this environment and to be engaged in rural finance, to focus on gradual reform from the inside. This assessment considers that to have been the right decision at the time, but, with the persistence of these distortions, relevance is more questionable for the later projects.

The objective of RFI was to assist the borrower in its efforts to improve living conditions in the rural areas through: (a) encouraging private sector investments; (b) strengthening the banking system's capacity to finance private sector investments; and (c) increasing access of the rural poor to financial services.

Total project costs were US\$139.70 million with an IDA financing of US\$122.80 million equivalent. There were three components. (i) A Rural Development Fund (RDF) (planned total costs US\$113.50 million; actual US\$110.9 million). This was a line of credit to provide short, medium, and long-term credit channeled from the State Bank of Vietnam (SBV) through competing Participating Financial Institutions (PFIs) to finance household enterprise investments in agriculture and other rural operations, including fixed assets and working capital. (ii) A Fund for the Rural Poor (FRP) (planned total costs US\$19.30 million; actual US\$15.00 million). This was to be a more directed line of credit restricted to the use of the rural poor. (iii) An Institution Building and Community Development component (planned total costs US\$6.90 million; actual US \$4.90 million). There were significant startup delays and the project was extended twice to close 18 months later than expected.

Outcome is rated satisfactory based on substantial relevance, efficacy, and efficiency (although with some reservations about relevance of design). This was a line of credit operation wholesaled through SBV under an enabling environment that, while liberalizing steadily, still exhibited: a dominant state-owned PFI in the form of VBARD, a policy lending state-owned bank, Vietnam Bank for the Poor (VBP) with subsidized lending rates that was to be a player in the Fund for the Rural Poor, and the intermittent application of interest rate ceilings. This assessment concludes that, notwithstanding the policy environment, engaging with a cautiously reforming borrower with evidence of substantial growth potential was better than disengagement, particularly given the impressive rural reach of the main player VBARD and the limited capacity and strength of the growing Joint Stock Banks.

The Bank has persisted with the rural finance sector in Vietnam, and the third project recently became effective. The enabling environment has gradually improved with better regulation of banks and other institutions, and most of the PFIs have grown and become somewhat stronger. Moreover, the number of PFIs increased substantially from RFI to RFII. However, a number of areas in the enabling environment remain problematic, in particular, ceilings on interest rates are still intermittently imposed, and subsidized directed credit continues under various programs. This reduces the incentives for banks to reach out into the more costly rural area, particularly against the long-standing advantage of the government owned VBARD. This impacts on savings incentives and longer-term financial services support for rural areas. While these interest rate ceilings are not always operative (currently they are in place), and while competition is certainly growing, bank CEOs will inevitably make decisions based on future expectations. The assessment finds a weakening of relevance into the follow-on projects, notwithstanding design improvements, as these persistent more fundamental issues remain unaddressed.

Although the objectives of the three projects remained largely the same, this assessment documents the main adjustments in project design over the series which has included: increasing medium and longer term lending as opposed to short; greater spread of accredited PFIs along with enhanced skills thus reducing the relative dominance of VBARD; greater lending to women; greater focus on microfinance products; and some shift in focus in capacity building from processes to institutional structures. Following the closing of RFI, for RFII and III, the Bank and borrower appropriately changed to the Bank for Investment and Development of Vietnam (BIDV) as the apex wholesale bank, removing the problem of the regulator (SBV) being also a lender. (While there remain concerns about Capital Adequacy Ratio with BIDV, there are now plans for “equitization” to raise additional capital and BIDV has generally developed well from being simply one of the PFIs under RFI.)

Both the Bank and the borrower were very slow to resolve the issue of the involvement of VBP in the project. Given the history of policy lending in Vietnam, the Bank should have foreseen that the government would be unable to meet the criteria of no subsidized lending since it was to be channeled through an institution that was intentionally set up precisely for that purpose. Towards the end of the project, when it became clear that the criteria for VBP participation could not be met, the funds were belatedly channeled through VBARD.

Subsequent to the project, two of the conditions have been somewhat overtaken by change and events. Loan size ceilings that were set at appraisal, and now apply to recycled lending, have gradually become effectively smaller due to inflation and increased incomes. Also, the boundaries of Hanoi have been enormously extended into a wholly rural area precluding many potential rural borrowers. These conditions warrant revisiting.

The following lessons emerge from this project:

- *Training programs should be designed with the objective of not only making delivery more efficient but of creating a national capacity in financial services.* This is a public good area warranting subsidy. In this project, while training at wholesale bank levels was given high priority, training at lower levels for PFIs and potential future PFIs, those that arguably most need training, could have been given more support. This was corrected to some extent in RFII and RFIII.
- *The Bank needs to revisit the impact of credit conditions in project implementation through the life of the credit, not simply the life of the project, and to design conditionality to adapt to change.* Some conditionalities that remain in effect through the life of a credit may be overtaken by events. Consideration should be given to indexing loan amount ceilings to allow for both inflation and rising per capita income through a nominal per capita, or rural per capita, income index. And in this case, the dramatic shift in the boundaries of Hanoi has reduced the potential beneficiary population.
- *The Bank should establish achievable PFI participation criteria at appraisal and ensure that at least a significant number of PFIs can meet them prior to appraisal.* In this case, the accreditation was left for later agreement, and an escape means through an institutional development plan was added. The need for this, and the fact that several PFIs still did not meet some of the criteria, suggests that they were not realistic at the outset and, indeed, that the bar set by the original criteria was misleading.

Vinod Thomas
Director-General
Evaluation

1. Background

1.1 There has been enormous progress in poverty alleviation in Vietnam since the early 1990s. Poverty incidence in rural areas fell from 66.4 in 1993 to 35.6 in 2002. But there remains a high incidence of poverty in the Central Highlands and in the Northern Mountains. At the time of the Rural Finance I (RFI) appraisal, the share of agriculture in total employment was above 70 percent. It is now, in 2009, close to 50 percent.

1.2 Since RFI, the RFII project is close to completion (expected in September 2009) and the RFIII Project has recently become effective. RFI was therefore the start of a series of Bank interventions in rural finance. In fact, even before that, the Agricultural Rehabilitation Project (Credit 2561-VN) could be considered an earlier precursor although, in this analysis, we treat RFI as the first of the rural finance series.

1.3 Annex A gives greater background on the enabling environment. Briefly, Vietnam undertook a series of major reforms beginning in the late 1980s (Llanto 1999). These included: decollectivization of agriculture; new land laws for greater security of land tenure; the removal of nearly all administered prices; a degree of interest rate liberalization; exchange-rate unification; liberalization of foreign trade and investment; some progress towards a legal framework encouraging private sector development; and initial opening up of the financial sector to domestic and foreign private banks. At the time of appraisal in 1995¹, commercial banking was dominated by the State-Owned Commercial Banks (SOCBs). They accounted for about 85% of commercial bank operations in 1994. At that time, assessing financial performance was difficult as accounting practices deviated from international standards. Apart from the Vietnamese Bank for Agriculture and Rural Development (VBARD), none of the financial institutions had been audited by external independent auditors. By then VBARD had started to shift away from financing State Owned Enterprises towards private households and businesses. By 1994, 62 percent of its lending was to rural households.

1.4 A more aggressive financial sector reform process began about 2001 around the time this project closed. The SOCBs were further restructured and policy lending to the poor was formally fenced off into a specialized entity the Vietnamese Bank for the Poor (VBP now the Vietnamese Bank for Social Policy (VBSP)). In 2006, the Prime Minister approved a plan for the development of the banking industry to 2010. However, there remains an unhealthy competitive environment, particularly for microfinance in rural areas due to interest rate caps and subsidized lending through VBSP and other programs. This is a disincentive for entry and for savings. Under RFI, there were no financial policy reforms deemed immediately essential for the implementation of the project or included as legal covenants. However, there was a covenant in the project calling for an annual exchange of views with IDA on interest rates focused particularly on whether "such rates are positive in real terms". This appears to

¹ At the time of appraisal there were 4 SOCBs, 46 private shareholding banks, 3 joint venture banks, 9 foreign banks, 69 credit cooperatives, 200 Peoples Credit Funds, 2 finance companies, and one government owned insurance company.

suggest some acquiescence in interest rates that do not fully cover costs, nonperforming loans, and profit.

1.5 At the time of RFI, microfinance regulations were rudimentary and not conducive to growth of that sector (Llanto 2004). There was a 2004 government decree on the organization and operation of micro-finance institutions. However, the regulations for the implementation of this are still evolving and being refined.

1.6 Bank support for agriculture (see Annex A for more detail) represents a mix of growth and equity interventions with a significant environmental focus. Agricultural competitiveness is seen as fundamental to sectoral growth including agricultural diversification, market development and trade integration. While agriculture is seen as important, according to staff, the current Bank strategy as of 2009 is not to divert resources from other sectors towards agriculture.

2. The Project

Objectives

2.1 The objective of the RFI project as stated in the Staff Appraisal Report (SAR) was to assist the borrower in its efforts to improve living conditions in the rural areas through: (a) encouraging private sector investments; (b) strengthening the banking system's capacity to finance private sector investments; (c) increasing access of the rural poor to financial services.

2.2 These goals were in line with the key elements of the government policy at the time and consistent with the Bank strategy. IDA was already involved in policy analysis, rural development, and institutional strengthening in the rural sector and the proposed project was intended to complement those interventions. A useful ESW report, the Financial Sector Review, provided a context for the project.

Project Design

2.3 Total Project Costs were US\$139.70 million with an IDA financing of US\$122.8 million equivalent. It had three components.

- (a) **Rural Development Fund (RDF)** (Planned Total Costs US\$113.50 million; actual US\$110.90 million). This was a line of credit to provide short, medium, and long-term credit channeled from the State Bank of Vietnam through competing Participating Financial Institutions (PFIs) to finance household enterprise investments in agriculture and other rural operations including fixed assets and working capital.
- (b) **Fund for the Rural Poor (FRP)** (Planned Total Costs US\$19.30 million; actual US\$15.00 million). In the appraisal design, this was to be a more directed line of

credit restricted to the use of the rural poor. It included short, medium, and long-term credit to be provided through the Vietnam Bank for the Poor (VBP) to individual poor households or to Joint Liability Groups (JLGs) of poor persons. The intention was to increase market access to groups previously excluded by reason of remoteness, inadequate collateral, and with limited access to resources from formal financial institutions.

- (c) **Institution Building and Community Development** (Planned Total Costs US\$6.90 million; actual US \$4.90 million) In the ICR this is referred to as Improving Financial Services to the Rural Poor due to a repackaging of components but this did not obscure funds utilization, it simply shifted labels..

2.4 While the ICR notes that none of the components were revised in terms of their objectives, there was, in fact, one significant change in an intermediary. VBP that was to channel the funding to the poorest, was not able to meet IDA conditions due to its subsidized lending and therefore, in the end, was unable to participate. The funds under the FRP component were then channeled through VBARD instead.

2.5 **Extensions.** The project closed 18 months behind the original schedule due to a slow startup including slow drafting of the two required Policy Manuals.

Quality at Entry

2.6 Project design was not given any Quality at Entry review by the Quality Assurance Group (QAG). The ICR argues that the design was largely satisfactory. However, it accepts that the FRP was not adequately formulated, leading to the abandonment of the use of the VBP. For this reason the PPAR rates Quality at Entry only Moderately Satisfactory. On this issue, the Bank appears to have been clearly unrealistic about the depth of ownership including the Assembly's views on policy lending (the general term in Vietnam for lending for social objectives). In this respect, regional management in the Bank seem to have placed more weight on country relations whereas staff were only too aware of the impending policy lending problem and the need to adhere to the well-documented lessons of experience. The project conditionality seems to indicate tacit agreement at negotiations to put aside the issue of subsidized interest rates under the Fund for the Rural Poor component for later resolution.

2.7 The analytical work on which the project was based came largely from the 1995 Financial Sector Review. This was adequately reflected in the SAR. There is further discussion of specific project design issues under the heading Relevance, but briefly, market failures at the time of project design appear to have included the lack of a level playing field, the nonperforming debt (but guaranteed by government) of the SOEs on the bank balance sheets, poor access to financial services in rural areas, under emphasis on savings mobilization, weaknesses in group formation due to lack of skills, limited lending to women for social and knowledge asymmetry reasons, and lack of market information and communication. Some of these issues were partly addressed through the training components proposed under the project. However, while considerable progress was made in access to services, non-performing loans and information, some of the other market failures remained to be addressed by other means.

2.8 The project would have benefited from at least a small pilot program testing alternative approaches with non-bank institutions and enabling some early comparative performance data to be assembled.

Implementation

2.9 As described in the ICR, the project was implemented by three sets of players. SBV was the apex institution wholesale bank. Receiving the proceeds of the credit from SBV were the PFIs contributing at least 10% of their own financing to the total sub project cost. Below the PFIs, were sub-borrower clients who were expected to contribute at least 15% of the cost either in cash or kind, the latter generally as labor. The IDA share was limited to 75% of the cost. SBV carried the credit risk at the level of the PFIs. The PFIs carried the credit risk associated with the sub-loans. The government assumed the foreign exchange risk. Maturity of PFI loans matched the composite maturity of the related sub loans. The lending rate from SBC to the PFIs was variable, adjusted quarterly on the basis of the quarterly weighted average cost of loanable funds in the banking system, equivalent to the price that PFIs would pay if funds were mobilized in the market². PFIs were free to select sub borrowers but their lending rates followed government/SBV rules and regulations³. As indicated, these regulations have, intermittently included ceilings on interest rates.

3. Performance Ratings

OUTCOME

3.1 Outcome is rated **satisfactory**, based on sub-ratings of substantial for relevance, efficacy and efficiency. There were shortcomings in some areas such as the delay in implementing the FRP component but these were balanced by household lending under the RDF component well beyond the target. There are some questions about overall sector sustainability related to the enabling environment for new bank entrants but nearly a decade has passed since the project closed and there have been slow but steady improvements in the performance of PFIs and increasing competition developing mainly in urban areas but gradually moving outwards to rural areas.

RELEVANCE

3.2 Relevance is rated **substantial** but there are some caveats. Assessment of relevance in this case takes account of the fact that this was a project of the 1990s in a country that had

² The reference rate used was the weighted average interest rate of time deposits adjusted to take into account the costs associated with the SBV's reserve requirements.

³ Accreditation criteria for the PFIs had five elements: compliance with banking law and audit requirements; solvency; liquidity; profitability; and quality of management and staff. The project component Policy Manuals provided to PFIs gave the detail. Financial indicators were expected to achieve the following: Net Past Dues of less than 10%, Capital Adequacy Ratio greater than or equal to 8%, Liquidity greater than or equal to 30%, Profitability greater than or equal to 1%. However, it was agreed that a PFI could be accredited even if it did not meet all the accreditation criteria if there was an Institutional Development Plan (IDP) together with a training program and timetable for achieving the plan acceptable to IDA (and SBV).

only very recently embarked on the path to financial liberalization emerging from a heavily controlled economy. Engagement was very important at that time. While persistence is often important in reform support, it has become more difficult to argue that Relevance has been sustained into the third project, or even the second, as interest rate ceilings and subsidized lending in rural areas through VBSP and, via cross-subsidy, through VBARD, persists. Although counterfactuals are difficult to delineate, it could be argued that the continued engagement into the later projects may now be partially to blame for the limited development of most forms of private financial intermediation including the rate of development of People's Credit Funds and the emergence of private, initially NGO based, micro-finance institutions given the de facto barrier that subsidized credit imposes.

3.3 Relevance of Objectives. As noted above, the project objectives were to assist in efforts to improve living conditions in the rural areas through encouraging private sector investments, strengthening the banking system's capacity to finance private sector investments and increasing access of the rural poor to financial services. These were consistent with the country and Bank strategy at the time. The 1995 CAS stated, as one area of priority support, Assisting the Transition to the Market. The RFI project was listed as an element of that priority aimed at: "supporting the development of the rural financial system on a market basis." In the following CAS, in 1998, shortly after project effectiveness, there was an evolution of Bank priorities towards rural development redirecting priorities somewhat from the earlier predominant focus on infrastructure. The Rural Finance Project, by then on-going, was mentioned as important for the "development of rural small and medium firms, which in turn are essential if rural incomes are to rise."

3.4 There was no Bank Rural Finance Strategy at the time of appraisal. The March 2003 elaboration of the rural finance elements of the Bank's "Reaching the Rural Poor" strategy calls for diversity of products and institutions that fill the financial needs of low-income clients, the development of efficient, viable financial institutions and products, and an emphasis on building the capacity of micro-finance institutions. The project was broadly consistent with this but was constrained by the measured nature of the evolution of government and political thinking to slow but steady progress in reforming the sector.

3.5 Relevance of Design. We conclude that, on balance, design was relevant at that time. However, it is a rating that warrants exploration. This was a line of credit operation with institutional strengthening for the key players. It was wholesaled through a state owned bank under an enabling environment that, while liberalizing somewhat, still exhibited: (i) a dominant state-owned PFI in the form of VBARD; (ii) a policy lending⁴ state-owned bank VBP (now VBSP) that initially was to be a player in the microfinance element; and, (iii) the intermittent application of either interest rate ceilings or subsidies on interest rates for priority programs funded either from Central or Provincial level. Moreover, since it was established, VBARD had not operated on a level playing field and so had a huge head-start. With the benefit of scale and cross-subsidy from the more profitable lending, and earlier direct subsidies, VBARD was able to lend to lower income households in quite remote areas. This was not a small achievement. The challenge in assessing the relevance of design

⁴ As noted earlier the term "policy lending" is used for lending for social objectives.

therefore lies in questions of the counterfactual in relation to the stage of rural finance sector development.

3.6 At the time of appraisal, the government was uninterested in removing subsidies or in any fundamental financial sector reforms, as has become apparent in subsequent years. However, the Bank was anxious to lend to Vietnam, and to develop a strong presence in agriculture as a main pillar of that lending. So it provided a series of agricultural credit operations but with very little policy content. The Bank chose to turn a blind eye to the policy issues in order to be a major player in the sector. This PPAR assesses that to be a realistic and correct decision. While it agreed to lend to the VBP, the "policy" bank of the government whose setup the Bank was not comfortable with, it was only prepared to do so only under certain conditions. These were not, in the event, met.

3.7 In the longer term, the objective of strengthening rural finance will be best served by leveling the playing field, removing all interest rate ceilings, including the threat of them, and enabling sufficient profitability for private players to enter the market for rural financial services to compete with VBARD. That evolving scenario is broadly accepted today by most government and state-owned bank officials. It was unrealistic at the time of RFI appraisal in 1995. One factor in making this assessment, that pursuing incremental progress was better at that time than a protracted stand-off, is the fact that Vietnam's Agricultural GDP growth rate has been exceptional since 1990 although this is attributable to many factors, in particular, infrastructure.

3.8 While several alternative formulations of design were considered, at that time in 1995/96, there was no alternative to using the State Bank of Vietnam (SBV). No other state-controlled bank was suitable and private banking was in a very early stage of development. For RFII, SBV handed over to the Bank for Investment and Development in Vietnam. This was an appropriate move since it separated the regulatory body from the wholesaling bank.

3.9 The Bank Guideline on Lines of Credit dated March 3, 2008, of course, did not apply to RFI at the time of either appraisal or closing, but even at that time there was an earlier OD8.30 of 1992. It is arguable that the procedures for setting PFI eligibility standards were violated by leaving this largely unresolved at appraisal for resolution during supervision. The light coverage of PFI capacity building was also not in line with the intent of OD8.30. There was building of capacity but very little for non-state-owned PFIs. With respect to other OD8.30 elements, there was operational autonomy, albeit with the influence of government ownership in the case of SOCBs. There was an increasing degree of commercial orientation still tempered with strong social policy objectives and the use of nontraditional collateral under the FRP, but interest rates at certain periods were almost certainly insufficient for the smaller loans in more remote areas. However, the Bank did draw a line that, in the end, excluded low interest policy lending through VBP (now VBSP). The RFIII project, effective recently, goes considerably further in these directions, particularly in developing capacity but the interest rate ceiling remains, at least intermittently.

3.10 There are three other areas where design might have been enhanced. First, the project indicators show some weaknesses, in particular, the use of only cumulative figures for lending, the lack of indicators for institutional capacity development, and the lack of some of

the more basic indicators such as loan repayment rates. Second, PFI eligibility was treated lightly in design, pushing criteria and selection back onto project supervision and the design of the manuals. Third, the project would have benefited from at least a small pilot program testing alternative approaches with non-bank institutions and enabling some early comparative performance data to be assembled.

EFFICACY

3.11 Efficacy is rated **substantial**. Ratings for individual elements of the objectives are explored below.

3.12 **Project Indicators.** The main project indicators at appraisal, with the actuals achieved in parenthesis, were as follows: 50,000 beneficiaries (actual 260,000 but note that this is cumulative including recycled funds for short term loans in a project with an 18 month extension); PFIs 9 (actual 7); Savings mobilization 60 percent of total lending by PFIs (actual over 60 percent); in the RDF component medium and large sub-loan numbers 25 percent (actual 5 percent, remainder small) and medium and large sub-loans by amount lent 50 percent (actual 8 percent, remainder small); medium and long term sub-loans by amount 50 percent (actual 34 percent, remainder short-term)⁵.

3.13 The following four questions relate to the stated project objectives.

3.14 **Did Living Conditions in Rural Areas Improve?** Achievement of this objective is rated Substantial. The 600,000 loans made and the 260,000 sub- borrowers were well in excess of the target. Repayment rates were excellent at over 98 percent. While repayment is indicative of successful investment, it does not prove that living conditions were enhanced. However, the Impact Study of 2002, that the mission assessed to be of generally adequate quality⁶, found in its surveys that 93 percent of borrowing families stated that the borrowing had increased household economic benefit. More importantly, the percentage of households in the “fairly wealthy” category in surveyed households increased from 39 percent to 61 percent however there were no non-borrowers surveyed and some of this must be attributed to broad economic growth. The study found that enterprise diversification only increased to a limited extent. It also found that, for many borrowers, loan size was considered insufficient for the intended investment so additional borrower contribution and additional borrowing was often sought from other sources.

3.15 **Was Private Investment Encouraged?** Achievement of this objective is rated Substantial. The output evidence of the number of loans and the fact that the sub-borrower contribution was 35 percent, well above the percent planned, and that many borrowers sought additional lending suggests that private investment was indeed encouraged. However, see the

⁵ Note that these lending figures are impacted by the numbers and volume of short term loans recycled over the project life, giving a predominance of short-term loans in cumulative figures. For this reason, the use of an indicator of cumulative loans without additional qualification and indicators is of limited value since, over time, the percentage of short-term in the whole inevitably grows. In this case *outstanding loans* at the date of closing for medium and long term lending was reported by BIDV as 74 percent.

⁶ Enumerators used seem to have been well supervised, and did not work for PFIs or the apex bank, so did not have any vested interest in the findings.

earlier qualification that the numbers of borrowers was impacted by the greater initial short-term lending and the extended project period⁷.

3.16 Lending was to households and SME enterprises and not to State-Owned Enterprises. While the SAR had provided for some limited lending to SOEs, this was not implemented due to the focus on household and SME lending. The Impact Study reported zero lending to SOEs.

3.17 Table 1 below gives the breakdown of enterprises supported by the main 5 PFIs. Over 80% of loans were for cultivation or animal husbandry. The Impact Study was able to estimate approximately that 15 percent of the RDF funds had gone to SMEs. It should be noted that the larger share of funds, about two thirds, was allocated to VBARD and VBARD target households not SMEs. Table 2. In Annex B gives the breakdown of lending by PFI.

Table 1. Percentage Loan Portfolio by Five of the Seven RDF PFIs and Enterprise as of June 30, 2001 (Impact Study Survey)

Enterprise Type	VBARD	BIDV	ACB	EAB	NAB
Cultivation	43%	77%	100%	95%	32%
Animal Husbandry	42%	5%			4%
Processing	1%				
Aquaculture	6%				2%
Services and Trading	4%	8%		5%	14%
Other	6%	10%			49%

3.18 **Was Banking System Capacity Strengthened?** For this objective, performance is rated, on balance, Substantial, but there were some areas of weakness. There are three main elements in this rating. First, the broader question, raised from a different angle under the heading Relevance, about whether Bank support to a system that is still not a wholly level playing field strengthened the banking system. This assessment's conclusion is influenced partly by the counterfactual, that, if the Bank had set as a condition the abandonment of interest ceilings and VBP's subsidized lending, almost certainly there would have been no series of RF projects. Second, the number of participating banks, at 7, was modest and therefore the scale of impact on institutions in RFI was inevitably modest. However, for a first project with many PFIs borderline for some of the accreditation criteria, less may well have been better than more and, in any case, it sent signals to non-participants which, in the light of the increase in PFIs under the following project, seem not to have passed unnoticed. Third, the quite tough accreditation criteria, albeit softened in practice by allowing attainment

⁷ The large size of borrower contribution is attributed by observers to several facts. First, for many borrowers, the loan size cap was too small so own contributions were added to increase this (VBARD are concerned that the cap is too small on the new third project.) or additional borrowing was undertaken. Second, deposit income was less than loan interest so many found it worthwhile to apply at least some of their savings. Third, many households were risk averse and did not want to be excessively in debt.

through approved IDPs⁸ and the training and capacity support, did result in some gains in performance ratios and a substantial increase in PFI's equity and therefore the scale of financial service capacity (see Annex A, Table 1).

3.19 While data on private sector lending to the rural sector over the project period or more recently is not available, lending to the private sector as a whole has been rising significantly⁹.

3.20 However, the performance of PFIs has been mixed (Annex B, Table 1) although generally trending towards improvement, particularly more recently post project closing. The weakest ratio evident was profitability and CAR of SOCBs and in some cases the level of non-performing loans. The Impact Study concluded that the project had helped PFIs expand capital sources mainly medium and long term and had improved profitability especially at branch level for VBARD. The appreciation of the longer term funds was confirmed during the mission. Capacity had been enhanced by training but there were still limited skills in loan appraisal of medium to long term investments. Annex B shows a steady but variable improvement in PFI ratios. However, BIDV and VBARD remain below the Basel I standards for capital adequacy¹⁰. A review of PFI performance was covered at a later date under the RFII Impact Assessment (Arthur D Little consultants 2005). While this assessment is capturing a different and larger set of 17 PFIs and 8 MFIs (most of the RFI PFIs were participating), and a later time period, it does show continued improvement. It seems probable that some of this can be attributed to a continuation of the gains of RFI. That Impact Assessment finds that, "Generally speaking, PFIs have been improving their financial performance year-on-year. In 2002, the majority of banks comply with all performance targets but Return on Assets." (However, the assessment argues that that indicator would improve if it was based on income-earning assets rather than total assets that would be more appropriate for the assessment of the profitability of core banking business.) The assessment also points to the continued decline in VBARD's market share as an indication of increased banking competition in rural areas.

3.21 With respect to the training, this included local training through the SBV-based PMU covering such topics as the project workshop, financial analysis, accreditation and sub-project appraisal; local training through VBARD and VBP on a range of subjects including training of about 140,000 members of lending groups; overseas training visits arranged by the SBV PMU; and, overseas training arranged by VBARD and VBP for their own staff. There was limited funding provision for training for PFIs and it was only for participating

⁸ The IDPs reviewed were generally of an adequate standard although VBARD's 1997 to 2000 overall plan (excluding backup material) was somewhat shallow in depth.

⁹ Data on borrowing for the economy as a whole (World Bank 2009) in more recent years shows that non-State-Owned Enterprise credit rose over the period 2002 to 2007 as a share of total credit from about 60 percent to about 70 percent in 2007 with the share of SOE credit falling from about 40 percent to about 30 percent. In 2002, Joint stock banks outstanding loans were only about VND30 trillion compared to SOCBs of VND157 trillion. By 2007, SOCBs had risen to VND574 trillion but Joint stock banks were up to about VND400 trillion. Private investment in Vietnam rose from about 14 percent of GDP in 2001 to about 18 percent in 2006.

¹⁰ Some SBV and BIDV officials argue that the CAR is less relevant to government owned banks due to the implicit government guarantee. However, the intent is to reach the standard as soon as possible. This has been made more difficult by the delay in doing this which has pushed this raising of capital ("equitization") into the current global financial crisis.

PFIs not potential future FIs. The Impact Study found that most PFIs wanted more training funds from the project particularly for skills that would enhance capacity to make decisions on longer-term lending. Given the need to build capacity in new entrants to rural lending, the focus seems to have been somewhat excessively towards the SOCBs. The project PFIs had their own internal programs set out in the IDPs sometimes using outside TA but this was through their own funds. Some training was also being undertaken in the same provinces by other donors and MFIs and by VBARD officers in the field as part of their normal responsibility¹¹.

3.22 Was Access to Rural Services Improved? On this objective, the project is rated High, although the extent of overall market coverage for Vietnam under RFI is not clear due to limited data on the size of the rural market as a whole, particularly back in the 1990s¹². The number of the direct beneficiaries reached was five times the original project target. The reach of the project was significantly above expectation partly because of the much greater share of contribution by borrowers. Sub-borrowers contributed about 39 percent of total costs. Savings were one source of this contribution partly due to caution and borrowers having savings that had a lower opportunity cost than additional borrowing.

3.23 One of the more successful aspects of increasing access was the mobile banking units under VBARD which allowed banking services to reach remote areas where branch establishment was uneconomic¹³. Under RFI, VBARD was the PFI with the smaller average loan size of approximately VND5 million (about \$450 at the time of appraisal) compared with about VND11 to 90 million (\$1,000 to \$8,000) for other PFIs. VBARD's clients are mainly rural households whereas others were mainly in the smaller urban or peri-urban areas, although often even these were for loans with rural forward or backward linkages. It is significant that, for household level lending, the PFIs other than BIDV and VBARD lent almost entirely short-term.

3.24 The selection process for borrowers seems to have varied by PFI. In some cases, VBARD borrowers were simply those in a poor commune that had not been found eligible for subsidized VBP funds and who had, during that selection process, expressed interest in a loan, in other words the above poverty line names. In other cases, it was based simply on individual loan officer contacts. For the SMEs, based on mission discussion with some borrowers, the process from application to funds flow took between a week and ten days, most being very satisfied with that. Loans through groups generally took longer owing to the number of households involved and the need to schedule meetings.

3.25 The evidence is limited on the extent to which borrowers were the poorer or poorest. It is unfortunate that the Impact Study did not do an analysis of the wealth levels of borrowers compared to non-borrowers since it appears that at least some of the raw data for

11 The mission met a VBARD officer doing good practical training work with a handicraft village group.

12 Llanto (1999) estimated the total microfinance market at about 12 million rural households and that about 50% were being reached. However, the project lending was not all for microfinance, which, in any case, was not clearly defined at that time.

13 The mission was able to see a mobile unit that had been funded under RFI and was still operating in a mountainous area.

such an analysis comparing borrowers and non-borrowers was available¹⁴. However, the small loan size cap (VBARD complains too small) is likely to have resulted in self-selection towards the poorer borrower. One would not expect the poorest to be borrowers since they were handled by VBP under their separate subsidized lending program. The predominance of household lending through VBARD is also likely to have selected towards the poorer since VBARD has a wide network in underserved and generally poor areas. The mission observed in the field that lending seemed to reach those who while obviously somewhat above the poverty of those eligible for VBP loans, were not far above, what the Impact Study classified as the “fairly poor”. The provision of 159 mobile banking vehicles is likely also to have directed services towards the poor areas since it is in the more remote areas without bank branches that these vehicles do their circuits¹⁵.

3.26 While, as noted in the literature for many years, there is no reliable way to assess whether a loan has been used for its intended purpose due to the fungibility problem, based on the Impact Study survey and on mission observation and discussion, the majority of loans appear to have been applied to productive uses rather than consumption¹⁶.

3.27 As noted in the Impact Study, the project did not do anything of significance to develop new savings products and to encourage saving although a major constraint in rural finance in Vietnam is the maturity mismatch with a lack of longer term deposits to support longer-term lending. Deposit rates are not controlled but the impact of ceilings on lending rates inevitably carries through. However, the mobile banking services did contribute to accessibility outreach for deposit taking. As noted in the ICR, these units mobilized saving on average from nearly 2,000 clients each per month at a total of about US\$1,300 per unit per month and disbursed about the same number and volume of loans per month.

3.28 **Impact on Agriculture and Other Impacts¹⁷** The project was not designed to increase agricultural productivity so this was not monitored. This was a rural finance project not an agricultural finance project. However, there is some evidence that agriculture benefited at least as measurable by inputs rather than outcomes. First, as noted, the Impact Study found that lending was predominantly for cultivation and animal husbandry. Second, mission observation in the field found evidence of both crop and animal husbandry lending, some in poor mountain areas. Third, the Impact Study found evidence at the farm level of shifts to higher return enterprises. Garden production and aquaculture increased while rice production decreased. However, due to the predominance of short-term small-scale lending, many farmers did not receive enough to fully restructure their enterprises. Productive areas of

¹⁴ Also unfortunately, the planned multi-year sample surveys (p77 SAR) were not implemented. It appears that the Bank did not push for this. Every year might have been overkill but at least a baseline and a mid-term would have been useful.

¹⁵ The mission inspected one such vehicle funded under the project that was still in quite good condition. They carry a safe in the back and an armed guard and carry out basic banking services at commune level, often in mountainous areas. It was claimed in that Province that there had never been a robbery.

¹⁶ Consumption loans can be obtained but are at higher interest rates.

¹⁷ While it is entirely outside the arena of this assessment, the mission would be remiss if it did not record that, in the mountain areas visited, where, at some time in the past, there has obviously been government support for housing of the poor of tribal groups, a majority of the roofs on houses were made of asbestos, now known to be a highly carcinogenic material. The costs of replacing it all would, of course, be enormous.

land and water were found by the study to have increased. The survey suggests that increased land area came mainly from the renting of abandoned land.

3.29 Looking at the larger picture, it is not possible to link the project to overall national agricultural growth since it only provided a small percentage of total investment in the sector, however, Table 2 below shows that over the period from 1999 (the earliest point at which any impact could reasonably be attributed to the project) onwards, agricultural growth slowed somewhat from about 4.5 percent over the period 1993 to 1998 to about 4 percent over the period 1998 to 2002 and down to about 3.8 percent 2003 to 2007. However, these are high rates of growth by international standards and are particularly commendable against the substantial price declines in markets over that period. The decline in the later years can be partly explained by: (a) the approach of the sector to a binding land frontier; (b) the diminishing returns as the initial recovery productivity gains were completed, and, (c) the by now high use of farm inputs.

Table 2. Vietnam Agricultural Sector Growth Rate

Yr.:	'90	'91	'92	'93	'94	'95	'96	'97	'98	'99	'00	'01	'02	'03	'04	'05	'06	'07
Ag. Grth. %	1.0	2.2	6.9	3.3	3.4	4.8	4.4	4.3	3.5	5.2	4.6	3.0	4.2	3.6	4.4	4.0	3.7	3.4 est.

Source: GSO, Vietnam

EFFICIENCY

3.30 Based on the (limited) quantitative data available, efficiency is rated **substantial**. As in nearly all cases with rural finance projects, the Impact Study and ICR did not estimate an ERR. No FRRs were calculated for individual loans (as they were in the Philippines RFIII) because no loans reached the threshold size. However, the following evidence suggests that benefits probably significantly outweighed the costs:

- The Impact Study found high levels of satisfaction, household perceptions of income gains, and evidence of surveyed households shifting to the next higher income levels. This has been largely confirmed by a later post-RFI survey under RFII by different consultants (A. D. Little 2005).
- The very high repayment rates suggest that benefits were generally sufficient to more than cover costs.
- Mission observations suggested that generally the projected benefits for the loans had been realized. These included livestock production, small and medium rural industry, and handicraft households.

- The profitability and other performance indicators of the 7 PFIs while mixed showed that most improved somewhat over the project period and have improved further since.
- Mission rough estimates of costs per job created in the small number of borrowers visited suggested costs per job that ranged from about US\$700 to about US\$10,000, in some cases reducing under-employment for an individual. But even if this was a larger sample, there is insufficient comparator data for Vietnam to rate the comparative efficiency. The fact that many loans were small may have encouraged some degree of efficiency in job creation since small loans tend to create employment at costs below the cost of job creation by larger loans. However, there are investment efficiency aspects also since larger investments may gain in economic efficiency by actually reducing employment.

RISK TO DEVELOPMENT OUTCOME

3.31 Risk to Development is rated **moderate** on balance. There have been a number of important changes over the three projects that are enumerated below, however there remain concerns about the persistence of issues such as interest rate ceilings and subsidized lending that raise increasing questions about relevance of subsequent operations as time passes and action has not been forthcoming.

- There was a gradual increase in the share of medium to long term lending. In RFI only 34 percent by number was medium/long but even during RFI there was a shift away from short-term with more outstanding loans being medium to long. By RFII medium to long cumulatively has averaged 78 percent under the RDF component. This is expected to increase further in RFIII. This reduces the risk of failure to achieve development objectives but somewhat raises risk to repayment.
- VBARD became a smaller proportion of total lending, at about 80 percent in RFI, falling below 50 percent in RFII and expected to drop probably below 40 percent in RFIII (assuming VBARD meets the accreditation criteria). This spreads risk.
- There was a significant increase in attention to environment over the series of projects.
- Over the series the focus shifted towards SMEs and poverty reduction through employment and to the development of improved products. This is consistent with the recent literature (e.g. Beck and Demirguc-Kunt, 2008, Gine and Townsend 2004 and Beck, Levine, and Levkov, 2007) that find that it was not by broadening access to credit or by advancing entrepreneurship that financial liberalization reduced income inequality but by boosting output and demand for labor, especially unskilled, resulting in wage increases. This places the current Bank and borrower SME strategy well up at the knowledge frontier¹⁸.

¹⁸ Later in this assessment the limited use of cost per job created evidence available from both Impact Studies and loan application and follow-up documents is commented on as a missed opportunity.

- The objectives remained largely the same across the three projects but with more attention in the last project to lending product development, a factor for sustainability.
- RFIII required a larger PFI minimum contribution although actuals have been higher than the minima, again reducing risk to the wholesale bank.
- RFI only had 7 PFIs, RFII 24, spreading risk and outreach further. Under RFIII it remains to be seen how many will qualify.
- Mobile banking increased from RFI to RFII increasing outreach.
- The MIS system developed over the three projects giving stronger feedback.
- Employment data was collected under RFII and will be under RFIII but in less detail under RFI. (Under RFII planned employment creation was about 50,000 jobs, actual to date is 255,000¹⁹.
- Lending to women increased from about 30 percent in the first project to about 45 percent under RFII. Generally, globally, lending to women has been less risky.
- On capacity building, early focus was on process later focus was more on institutional structure an important element in sustainability.
- At the time of RFI SBV was not requiring audits, now all banks must be audited.
- PFI performance indicators improved over the period although some ratios, such as profitability improvement were mixed.
- RFIII includes a component to support the People's Credit Fund. Given the rapid emergence of these funds, this should have been picked up earlier. Also, RFIII includes support for non-bank supervision under SBV to back the new microfinance law, important for sustainability.

3.32 Interest Rate Ceiling and Risk to Development. While these many changes are positive for the broad objectives, some elements have not changed significantly. As noted, the most important of these for the health of the sector is the ceiling on interest rates. (Llanto 1999). Interest rate ceilings imposed on regulated financial entities result in relatively higher interest rates in the non-regulated sector. Ceilings contribute to misallocation of resources and weakened financial institutions. In a developing economy such as Vietnam the strategy should be aimed at closing the savings/investment gap which calls for the appropriate pricing of savings as well as credit. Imposing an interest rate ceiling creates an unlevel playing field for commercial banks trying to establish viable footholds in rural areas. (It should be noted, however, that ceilings are imposed by the Assembly. SBV is well aware of the potential impact and have presented a case to the Assembly on more than one occasion.²⁰) Some observers and banks argue that the ceiling is not really a significant problem and that banks

19 Although it should be noted that estimating truly incremental employment in an SME is very difficult.

20 Visits for Assembly representatives to other countries with alternative policies may be useful to demonstrate that access and institutional sustainability is usually far more important in microfinance than interest rate.

can make sufficient margin. But this is not the full story for several reasons. First, many of these banks, unable to compete with the still dominant place that VBARD holds in the rural areas are not attempting to compete at present, they are taking the still “easier pickings” in urban areas. This will change. Second, even when ceilings are removed once again, the *expectations* of possible re-imposition remain for some years, action will have a lag. Third, for the more remote rural lending, banks are competing with the VBARD history of public support and the consequent VBARD entrenched dominant position. Competitors will need even countervailing incentives to get a toe-hold against such entrenched competition. Fourth, the very fact that nearly all banks are lending both short and long term at the same ceiling rate is evidence that banks are forced by the low ceiling to push both rates, lower risk and higher, up against the ceiling to try to make sufficient profit. Fifth, VBARD itself, notwithstanding the huge advantage of its existing network, acknowledges that it has to cross-subsidize the more remote rural lending and mobile units with the profits of their easier lending. While other banks, with new products such as e-banking can be expected to slowly make inroads, with interest rate ceilings the cards remain stacked against them.²¹ The fact that the People’s Cooperative Fund (PCF) has been substantially increasing its lending to farmers, currently at 3.5% above the interest rate ceiling set for banks, is evidence that higher interest rates are not a constraint in lending to poorer borrowers. As has been found globally in microfinance, access is more important than price.

3.33 Beyond the interest rate issue, it will be particularly important that competing joint stock banks and non-bank microfinance entities are enabled by the political linkages at commune, District and Province level, to gain the same level of access and cooperation in the formation and servicing of joint liability groups as VBARD and VBSP. It was not entirely clear to the mission that this is yet the case.

3.34 Responding to the current global financial crisis, subsidized interest rates appear to be seen once more as one tool in the government response.²² The recent Decision 131 by the Prime Minister on subsidizing interest rates for institutions and individuals to help them carry out production and business plans states that banking institutions may now seek subsidies. The eligibility list so far includes state-owned banks, joint stock banks, joint venture banks, foreign bank branches, and wholly foreign owned banks. (The People’s Credit Fund program has recently been asking to be included in the list). There is to be a 4% discount funded by government. While the current global crisis is arguably unprecedented, the global experience has been that such subsidies become difficult to reverse. Increased spending on rural infrastructure is an alternative since a main reason for lack of financial services is access.

3.35 With respect to the sustainability of PFIs, Annex B, Table 1 gives the financial indicators over time up to 2007. The Impact Assessment for RFII (A.D. Little 2005)

21 The Borrower has commented that in recent years joint stock commercial banks have been expanding in rural areas and that the predominance of VBARD has declined (see Annex D).

22 Both long and short-term lending ceilings were set at a spread over SBV’s base rate that gives a borrower interest rate of 9% for short-term loans, 10.5% for medium-term loans, and 12% for consumption loans.

Deposit rates are not controlled but currently VBARD deposits are 7% for 24 months, 6% for 6 to 12 months and 5.5% for 3 to 6 months. In 2002 the ceiling was removed [by Decision No. 546/2002/QD-NHNN, dated May 30] but VBARD’s dominant role, government ownership and social objectives seem to have played a role in holding rates down. The ceiling reappeared again in 2008.

concludes that PFI's, while still facing difficulties achieving CAR and profitability targets, have been improving financial performance and the expectation in 2005 was that, with their strategic and restructuring plans, this was likely to continue. However, this PFI performance and sustainability issue is also connected to the relevance question raised earlier about the impact of continued Bank support on the levelness of the playing field and the continuation in Vietnam rural finance of interest rate ceilings and subsidies.

3.36 Finally, the shift for RFII to BIDV as the apex bank from SBV made sense for future development. It moved the apex responsibility from the central bank with regulatory and lending conflicts of interest to a commercial bank, albeit state owned. There were, and still are, some performance ratio concerns with BIDV, particularly CAR, but BIDV have been developing strong skills and remain under RFIII.

BANK PERFORMANCE

3.37 Bank Performance is rated **satisfactory** overall. However, there were some weaknesses in project design.

3.38 **Quality at Entry.** Quality at Entry is rated Moderately Satisfactory. While overall, the design was thorough and balanced, the inclusion of VBP as the conduit for the Fund for the Rural Poor (FRP) was unrealistic from the start. The Bank did not want to get involved in subsidized lending but there is evidence of differences of position on this within regional staff. There was pressure from the borrower to include lending to the poor through VBP and the Bank made the mistake of agreeing to this at negotiations in spite of the fact that VBP was expressly set up to "fence off" subsidized lending. It was never likely that common ground would be found. Also, what seems to be a not uncommon failing in such projects, the Bank could have somewhat better analyzed the place of the proposed project in the sector as a whole, including relative scale and also, for VBARD levels of implicit and explicit subsidy.

3.39 **Quality of Supervision.** Project supervision is rated Satisfactory. The mission heard praise from borrower representatives for the skills of the Bank staff in both project design and implementation. However, when the criteria for VBP participation set by the Bank could not be met, it took most of the project period to reach agreement to redirect the FRP component towards VBARD as the lending intermediary. The resolution process was very slow on both sides.

3.40 Donor coordination was given generally satisfactory marks by most of those involved, including government. The twice a year Consultative Group meetings were found useful, as were some lower level sector or thematic meetings. However, there was some suggestion of lack of coordination on pass on rates.

3.41 Finally, the ICR was generally of good quality although, as noted in the IEG ICR Review there were some gaps. This assessment finds also that it could have used more of the Impact Study evidence.

BORROWER PERFORMANCE

3.42 Borrower performance is rated, on balance, **satisfactory**.

3.43 Government. SBV was the apex institution and, in many respects, the government representative and, for the purposes of this analysis are placed in the government category. The Department of Finance was also involved on the policy and donor relationship side but more at arms length. Government performance is rated Moderately Satisfactory, as opposed to fully Satisfactory, mainly due to the interest rate ceiling issue. SBV played a very active role in the preparation of the project and negotiated their difficult role as regulator and apex bank responsibly. SBV were found by the mission to have retained extensive knowledge of this project even though it closed more than eight years ago and there was strong interest in SBV in the design and outcome of the subsequent project series. However, this assessment has raised questions about the intermittent interest-rate ceilings promulgated by the Assembly. This was not in either DOF's or SBV's hands. While policy lending is not inappropriate in the achievement of poverty goals, the government has still not clearly and consistently fenced this off from commercial lending. This strategy needs to be reassessed and coordinated by government with respect to all savings and loan or grant providing players including those at the Provincial level.

3.44 Implementing Institutions. Performance of the implementing institutions is rated Satisfactory. At the PFI level, lending decisions were generally sound as is evidenced by the very high repayment rates and predominantly adequate and improving performance ratios. However, there were weaknesses in the performance of the two SOCBs with respect to overdue debt and CAR and for three of the five other banks in some areas, including overdue debt and profitability. But at all levels repayment rates were very high.

3.45 The borrower seems to be as equally to blame as the Bank for the extremely slow resolution of the issue over the FRP component that should have been resolved at negotiations but, in the end, it was resolved.

Monitoring and Evaluation

3.46 M&E is rated **substantial**. Monitoring and evaluation in finance projects takes a somewhat different form to traditional investment projects since much of the required accounting data and performance ratios covers a substantial part of what normally would be required for M&E in a more traditional investment project. Nevertheless, M&E quality was insufficiently covered by the ICR.

3.47 Design M&E design (see Staff Appraisal Report) was left to SBV but it was to be satisfactory to IDA. The project manuals were a part of the M&E planning process. Surprisingly, the PFI accreditation criteria were not agreed by appraisal or by negotiations. The SAR simply stated that, "The PFIs would be approved on the basis of agreed accreditation criteria to be detailed in the policy manual of the RDF. SBV would inform IDA accordingly." The reason for this hands-off approach by IDA appears to have been because SBV had banking regulation criteria covering many of the criteria and it would have been difficult to have imposed different ones for an individual project. However, there is no indication in the SAR section on accreditation that the current criteria at the time represented a minimum acceptable to IDA. As noted earlier, the project indicators show some weaknesses, in particular, the use of only cumulative figures for lending, the lack of indicators for institutional capacity development, and the lack of some of the more basic

indicators such as loan repayment rates, as suggested in the OP8.30 Guideline. As also noted earlier, this assessment finds the use of cumulative lending data to be of somewhat limited value without additional information.

3.48 Implementation Implementation appears to have been carried out satisfactorily by SBV. However, the quality of reporting by PFIs was variable and, due to different accounting practices, not always uniform.

3.49 Utilization The utilization of the available data was quite strong. The data were used for a number of adjustments and to target support for PFIs. Over the period of the project the International Credit Project Management Unit (ICPMU) gained in experience and capacity and, as a result, a number of the staff shifted to BIDV²³, the new apex institution, prior to RFII. The skills in the unit are impressive.

4. Findings and Lessons

4.1 While the RFI was a traditional targeted line of credit project through a government-owned wholesale bank within a financial environment that was heavily regulated, it performed well in achieving its immediate objectives. It contributed to strengthening of the rural financial system and expanding rural outreach. Vietnam has taken a gradual approach (CAE 2001) to transitioning to a market economy within a stable political structure and a continued adherence to socialist principles. Yet it has experienced very rapid growth in contrast to former Soviet Union countries that followed more radical transitions and have not fared as well. During the early 1990s there was a strong supply response from agriculture and strong poverty impact. The burden of proof therefore lies with those who would argue that a disengagement counterfactual in rural finance would have resulted in greater progress. The assessment was not able to argue that for the first project. Nevertheless, there are a number of weaknesses in the policy environment that need to be addressed, particularly the interest rate cap and subsidies (outside the projects) and there are increasing relevance questions about the follow-on projects as these constraints to competition persist.

4.2 There was a need at the time of RFI, and there is still a need now, for a study to better understand all the implicit subsidies throughout the system not only with respect to VBARD and VBSP but programs at Provincial level also. Bank staff indicated that a study of VBARD from this perspective is under consideration. This may be too narrow.

4.3 The Bank needs to consider a more proactive approach to closed projects with loan funds that are being relent within the same fund particularly with respect to loan size caps but perhaps other criteria also. In the case of RFI, VBARD find the cap of US\$400 too low. An absolute loan size cap will inevitably shrink in real terms with inflation and with growing per capita income (substantial in the case of Vietnam). In addition, other circumstances can change, not always predictably. For example, the area of Hanoi city was recently enormously

²³ BIDV, a PFI under RFI, took over all the RFI responsibility and portfolio from SBV and are the apex bank for RFII and III.

increased by legislation as the city engulfed a whole rural province. The project agreement on excluded lending areas, as it still stands today, now legally excludes a large rural area of over 5 million predominantly rural potential beneficiaries. Some flexibility on lending parameters would seem warranted and some form of indexing of ceilings if they are likely to stand for many years as they are with credit reflows.

4.4 Both the Bank and the borrower were very slow to resolve the issue of the involvement of VBP in the project. Given the history of policy lending, the Bank should have foreseen that the government would be unable to meet the Bank's criteria of no subsidized lending through an institution that was hived off by design from VBARD precisely for that purpose.

4.5 Better analytical use could have been made, by both the Bank and the borrower, of the already available data on costs per job created. Supported by wider calculation of Financial Rates of Return on a sample basis for both smaller loans and larger, such data could have been useful for understanding growth and poverty and employment impact.

4.6 Visits in the field did not reveal much connection between the processes of making and supervising loans and the agriculture technology specialists in the extension service and the farmer field school program. The latter was found by IEG in the Agricultural Rehabilitation Project PPAR of June 11, 2002 to be quite an effective program albeit high cost. While this issue would warrant wider assessment for valid conclusions, and while there is somewhat mixed evidence on the benefits of technical linkages in the literature (Ledgerwood 1998), *a priori* it would seem efficient to attempt to pursue complementarity by connecting the smaller, less technically skilled, sub-borrower with sources of such skills either public or private. This limited linkage seems to be reflected in the Bank strategy also. The latest 2006 Bank strategic overview document with a predominantly agriculture focus, *Accelerating Vietnam's Rural Development: Growth, Equity and Diversification*, has quite limited reference to rural finance. However alternatively, this may suggest that rural finance is no longer seen as one of the major constraints.

4.7 The competitive edge of VBARD in rural areas was substantial under RFI and is still substantial although competitors are now making significant headway. Although e-banking may change costs considerably, there may be a case to counteract this competitive edge with incentives to private banks and non-bank institutions for initial branch establishment in rural areas.

4.8 The main lessons are the following:

- *Training programs should be designed with the objective of not only making delivery more efficient but of creating a national capacity in financial services.* This is a public good area warranting subsidy. In this project, while training at wholesale bank levels was given high priority, training at lower levels for PFIs and potential future PFIs, those that arguably most need training, could have been given more support. This was corrected to some extent in RFII and RFIII.
- *The Bank needs to revisit the impact of conditionality on project implementation through the life of the credit not simply the life of the project and to design*

conditionality to adapt to change. Some conditionalities that remain in effect through the life of a credit may be overtaken by events. Consideration should be given to indexing loan amount ceilings to allow for both inflation and rising per capita income through a nominal per capita, or rural per capita, income index. And in this case, the dramatic shift in the boundaries of Hanoi has reduced the potential beneficiary population.

- *The Bank should establish achievable PFI participation criteria at appraisal and ensure that at least a significant number of PFIs can meet them prior to appraisal.* In this case, the accreditation was left for later agreement and an escape means through an institutional development plan was added. The need for this and the fact that several PFIs still did not meet some of the criteria suggests that they were not realistic at the outset and, indeed, that the bar set by the original criteria was misleading.

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Note: This reference list does not include all the World Bank CASs, PADs, ICRs, and PPARs referred to for the lending programs and agriculture projects.

Annex A. Basic Data Sheet

VIETNAM: Rural Finance Project (IDA-28550)

Key Project Data (*amounts in US\$ million*)

	<i>Appraisal estimate</i>	<i>Actual or current estimate</i>	<i>Actual as % of appraisal estimate</i>
Loan/Credit amount	122.80	111.10	94
Borrower	5.80	3.50	60
Cofinancing	11.10	15.70	141
Total project costs	139.70	129.80	93

Project Dates

	<i>Original</i>	<i>Actual</i>
Concept Review	04/27/1995	04/27/1995
Begin Appraisal	11/21/1995	12/01/1995
Board approval	05/07/1996	05/07/1996
Signing	07/19/1996	07/19/1996
Effectiveness	10/19/1996	02/06/1997
Closing date	06/30/2000	12/31/2001

Staff Inputs (staff weeks)

Stage of Project Cycle	Actual/Latest Estimate	
	No. Staff Weeks	USD Thousands (including travel and consultant costs)
Identification/Preparation	29.9	73.6
Appraisal/Negotiation	49.7	139.1
Supervision	58.1	161.1
ICR	4	5
Total	168.0	515.8

Mission Data

Mission

Stage of Project Cycle	No. of Persons and Specialty (e.g. 2 Economists, 1 FMS, etc.)		Performance Rating		
	Month/Year	Count	Specialty	Implementation Progress	Development Objective
Identification/Preparation 02/1995		6	A,B,C,E,H,I	S	S
Appraisal/Negotiation 11/21/1995		6	A,B,C,H,I,G	S	S
Supervision					
02/1997	2	B,I	S	S	
10/1997	2	B,i	S	S	
02/1998	1	B	S	S	
05/1998	1	B	S	S	
11/1998	1	B	S	S	
04/1999	1	B	S	S	
11/1999	1	B	S	S	
03/2000	1	B	S	S	
05/2000	1	B	S	S	
09/2000	1	B	S	S	
01/2001	4	B,D,F	S	S	
05/2001	1	B,H,I	S	S	
ICR					
	09/2002	1	B	S	S

A: Agricultural Economist

B: Financial Analyst

C: Agricultural Credit

D: Financial Management Specialist

E: Economist

F: Environmental Specialist

G: Legal Counsel

H: Microfinance Specialist

I: Operation Officer

Annex B. Background and Enabling Environment

1. There has been enormous progress in poverty alleviation in Vietnam since the early 1990s. Poverty incidence in rural areas fell from 66.4 in 1993 to 35.6 in 2002. But there remains a high incidence of poverty in the Central Highlands and in the Northern Mountains. Share of agriculture in total employment has been declining rapidly and is now approaching 50 percent. At the time of the Rural Finance I (RFI) appraisal, the share of agriculture in total employment was above 70 percent.

2. Since RFI, the RFII project is close to completion (expected in September 2009) and the RFIII Project has recently become effective. RFI was therefore the start of a series of Bank interventions in rural finance. In fact, even before that, the Agricultural Rehabilitation Project (Credit 2561-VN) could be considered an earlier precursor although, in this analysis, we treat RFI as the first of the rural finance series. While this IEG assessment is of the RFI project, it also looks at the evolution of RFI into RFII and RFIII as a way of understanding the sustainability of the process started with RFI and as an input into the on-going IEG agriculture study. Over these three projects there has been substantial liberalization in the financial sector but starting from a very low base.

3. As discussed in the ICR, at the time of RFI appraisal, Vietnam had already taken a number of actions to shift towards a market -based economy. The mono-bank system had been replaced by a two-tier banking structure. The government had reorganized the State Bank of Vietnam (SBV) to function exclusively as the central bank and had established the Vietnam Bank for Agriculture (VBA), now VBARD, and the Industrial and Commercial Bank to take over its commercial banking activities together with two specialized banks, the Bank for Investment and Development, BID, now BIDV (the wholesale bank for RFII and III) and the Bank of Foreign Trade. These State Owned Commercial Banks (SOCBs) had been restructured as independent entities. The government had also paved the way for the establishment of private banks, branches of foreign banks, joint venture banks and rural credit unions. The interest rate structure had been brought closer to reflecting market prices although there were still controls.

4. At the time of appraisal²⁴, commercial banking was dominated by the SOCBs. They accounted for about 85% of commercial bank operations in 1994. At that time, assessing financial performance was difficult as accounting practices deviated from international standards. Apart from VBA, none of the financial institutions had been audited at that time by external independent auditors. By then VBA had started to shift away from financing State Owned Enterprises towards private households and businesses. By 1994, 62 percent of its lending was to rural households.

5. **Enabling Environment.** Vietnam undertook a series of major reforms beginning in the late 1980s (Llanto 1999). These included: decollectivization of agriculture; new land laws for greater security of land tenure; the removal of nearly all administered prices; a degree of interest rate liberalization; exchange-rate unification; liberalization of foreign trade and investment; some

²⁴ At the time of appraisal there were 4 SOCBs, 46 private shareholding banks, 3 joint venture banks, 9 foreign banks, 69 credit cooperatives, 200 Peoples Credit Funds, 2 finance companies, and one government owned insurance company.

progress towards a legal framework encouraging private sector development; and initial opening up of the financial sector to domestic and foreign private banks.

6. A more aggressive financial sector reform process began about 2001. The SOCBs were further restructured and policy lending to the poor was formally fenced off into a specialized entity the Vietnamese Bank for the Poor (VBP now the Vietnamese Bank for Social Policy (VBSP)). Bank support for adjustment and financial sector reform came through two main channels: Structural Adjustment Credit Projects that contributed to strong macroeconomic performance and helped further the transition to a market economy and, also, more focused on financial sector specifics, a series of five Poverty Reduction Support Operations (ICR 2007 on these projects). These have been followed approximately annually by further PRSCs²⁵. Outcomes of each of the first five PRSCs was rated Satisfactory by the ICR.

7. The result of these accelerating reforms has been greater financial depth. In 2007, (Thanh 2008) Credit/GDP was 82 percent, M2/GDP was 110 percent. In 2005, Vietnam bank deposit/GDP was 65 percent. However, there remains some lack of transparency and weak financial supervision and the financial system is still bank-based and relatively underdeveloped. Still about 50 percent of household savings are not deposited in banks. Less than 10% of the population has personal bank accounts. SOCBs accounted for 59 percent of total deposits in 2007. There remains a mismatch between short-term deposits and long-term lending. There is a need for further development of risk rating and other information generating agencies.

8. In 2006, the Prime Minister approved a plan for the development of the banking industry to 2010. This includes laws related to SBV, credit institutions, deposit insurance, banking oversight, plans for enhancing capability of commercial banks, improvement of the effectiveness of non-bank credit institutions, modernization of payment systems and MIS (these two with further World Bank support), a roadmap for improving the convertibility of the Vietnamese Dong, development of small-scale financial activities, and improved information for national monetary policy.

25 Briefly, the PRSCs supported the following: restructuring plans for four state-owned commercial banks (including VBARD and BIDV); the closing of nine joint stock banks and ensuring compliance with SBV regulations for the remaining ones; bringing criteria for loan classification to the standards of international practice, and revised criteria for non-performing loans and provisioning; completion of international auditing by international auditors for four SOCBs; a timetable for SOCBs to prepare credit manuals; completion of audits for VBARD and BIDV to international standards; a shift from cash-based accounting to accrual-based accounting; action plans for BIDV and VBARD to strengthen MIS; re-evaluation of unsecured non-performing loans to State-Owned Enterprises (SOEs); revised circular to strengthen creditors rights in the re-evaluation of SOE NPLs; in preparation for WTO, a plan to strengthen SBV supervision and to level the playing field for banks; adoption of a new chart of accounts to improve transparency; instructions to SOCBs on the new credit manuals to improve risk management; a 60 day time limit for SOCBs to submit audits; a directive to equitize two SOCBs (including BIDV); regulations restricting the mechanisms for policy lending of the Development Assistance Fund; further development of the securities market through easing listing requirements and a legal framework for securities investment funds; separation, in principle, of SBV's SOCB management functions from supervisory functions; regulations requiring SOCBs to classify loans on the basis of international accounting standards; and adoption of a roadmap for the reform of the banking sector. While there is a degree of slippage evident in the list of interventions from the first PRSC to the last, and some reversion towards plans and roadmaps rather than completed actions, this list represents a significant series of actions over the period 2001 to 2006.

9. Under RFI, there were no financial policy reforms deemed immediately essential for the implementation of the project or included as legal covenants but there was a broader ongoing process of financial sector policy reform outside the project supported by the Bank. However, there was a covenant in the project calling for an annual exchange of views with IDA on interest rates focused particularly on whether "such rates are positive in real terms". This appears to suggest some acquiescence in interest rates that do not fully cover operating costs, provisions for nonperforming loans, and a profit sufficient to enable expansion. There was also a condition related to the VBP Fund for the Rural Poor component which was required to meet the criteria set out in the FRP Policy Manual still to be drafted but to be agreed to by IDA. The lack of an agreed formulation at negotiations for interest rate under this Fund for the Rural Poor component seems to have been a device to avoid facing this contested issue head-on in the hope that, somehow, it could be resolved later. It never was, and VBP lending did not take place under the project.

10. **Microfinance.** At the time of RFI, microfinance regulations were rudimentary and not strongly conducive to growth of that sector (Llanto 2004). But relevant to RFII and III, in 2004, there was a government decree on the organization and operation of micro-finance institutions covering the scope of regulation, legal levels of capital, terms of operation, areas of operation, state policies, conditions and documentation for obtaining licenses, procedures, rules for mergers, splits, dissolution, and bankruptcy, required structures functions and responsibilities or boards, regulations on operation, capital mobilization, credit activities, limits on credit and mobilization of savings and financial and accounting requirements. The regulations for the implementation of this are still being finalized.

11. As outlined in the ICR, the financial reforms since the early 1990s onwards constitute significant progress. Earlier the financial sector was largely a government "window" to fund SOEs. Over the period 2002 to 2007 the equity in the 22 private commercial banks participating in RFII increased by almost ten times. Today, approximately 70 to 80% of the poor have access to some form of financial services. However, much remains to be done. Service quality is often weak, the market is fragmented, and frequently services do not meet client's needs. Access to finance, particularly medium and long term, is still limited for small and medium-sized enterprises. SOEs have greater access to financing than private firms. Even today, private firms finance about 75% of their investments through non-market means including family and friends and retained earnings. A major problem is the lack of medium and long-term funds available to banks. This is partly because only one third of deposits raised in Vietnam are longer than 12 months. There is also a substantial focus by banks on the urban areas perceived as offering less risky and less costly lending.

12. **Bank Support to Agriculture.** As noted earlier, prior to the series of RFs, the Bank had supported an Agricultural Rehabilitation Project. This had supported the rehabilitation of agricultural support services, the provision of credit to about 50,000 smallholders farmers through the Vietnamese Bank for Agriculture and Rural Development (VBARD) for on-farm development and working capital, rehabilitation of about 160,000 ha of established rubber, and training and TA for policy analysis and follow-on project preparation. Currently, the main priority areas in agriculture, both ongoing or under preparation, include: the Coastal Wetlands Project, Forestry, Rural Infrastructure (CDD), Irrigation, Natural Disaster Management, Northern Mountains Poverty, Avian Flu, IT for Rural Development and a proposed Livestock Project

under preparation. These represent a mix of growth and equity interventions with a significant environmental focus. Agricultural competitiveness is seen as fundamental to sectoral growth. The diversity of household income sources is an increasing area of attention. Bank staff report that as gains are being realized from policy shifts in land allocation, titling and the general liberalization of markets, agricultural technology for productivity increase is emerging as a priority. Also, agricultural diversification, market development and trade integration are key areas. While agriculture is seen as important, the current Bank strategy is not proposing the diversion of resources from other sectors towards agriculture.

Annex B. Table 1. Financial Indicators for RFI PFIs

Financial Indicators	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
BIDV										
Net past dues		1.4	0.2	3.2	1.42	0.83	30.08			
Non Performing										
Loans/Loan Portfolio								31.3	9.59	3.98
Capital Adequacy Ratio		5.3	2.5	2	2.34	4.4	4.6	3.36	5.87	6.65
Liquidity		48	32.4	55.8	55.96	52.9	30.08	39.68	43.84	52.4
Profitability		0.3	0.2	0.3	0.04	0.03	0.09	0.11	0.44	0.89
Return on Equity		8.8	9.5	14.8	9	1.63	0.6	3.77	16.03	25.01
VBARD										
Net past dues		3	4.9	3.8	3.7	4.56	2.5	1.23		
Non Performing										
Loans/Loan Portfolio								NA	1.81	1.9
Capital Adequacy Ratio		9	7.3	5.1	4.2	5.46	5.56	4.79	4.56	5.86
Liquidity		31	27	59.5	34	23.52	23.59	17.81	26.65	33.18
Profitability		0.4	0.4	0.5	0.4	0.24	0.2	0.38	0.5	0.57
Return on Equity		18.9	5.4	10.5	11.2	5.55	4.34	8.32	11.86	12.1
ACB										
Net past dues		2.9	2.9	0.5	0.1	0.93	0.59	0.47		
Non Performing										
Loans/Loan Portfolio								NA	0.2	0.08
Capital Adequacy Ratio		29.3	24.3	11.2	8.71	7.01	7.46	7.63	6.81	10.81
Liquidity		56	159.8	97	94.83	70.55	46.6	46.2	71.02	57.32
Profitability		3.5	2.5	1	1.13	1.41	1.34	1.78	1.62	1.58
Return on Equity		11.1	15	16.2	20.87	30.07	28.16	36.67	33.78	31.63
EAB										
Net past dues		1	4.7	0.4	0.58	0.81	0.55	0.33		
Non Performing										
Loans/Loan Portfolio								NA	NA	0.44
Capital Adequacy Ratio		19	13.5	5.9	7.53	7.94	8.95	9.26	7.47	14.38
Liquidity		89	26	18.1	30.7	9.64	32.43	28.46	23.1	20.74
Profitability		3	3	1.5	2.61	2.56	2	1.46	1.49	1.67
Return on Equity		16.7	14.5	18.9	29.89	29.53	25.08	19.39	19.37	15.24
PNB										
Net past dues			2.1	4.8	1.24	1.43	0.53	1.3		
Non Performing										
Loans/Loan Portfolio								NA	2.89	2.9

Capital Adequacy Ratio	16.6	11.5	9.7	9.4	8.08	10.32	9.64	22.95	16.76
Liquidity	21.2	22.9	24.7	24.4	27.25	30.86	23.21	52.9	71.13
Profitability	0.7	1.3	1.53	1.22	1.38	1.7	1.41	2.1	1.74
Return on Equity	5.2	13.8	17.17	14.81	17.74	21.35	14.7	13.45	10.83
NAB/BAB									
Net past dues	2.2	3.6	0.99	-0.01	0.07	0.69			
Non Performing Loans/Loan Portfolio							NA	0.69	0.46
Capital Adequacy Ratio	13	25.1	11.37	8.9	7.18	6.29	9.62	19.66	21.11
Liquidity	24.8	90.4	28.07	30.36	15.55	63.56	58.15	52.81	63.54
Profitability	0.1	0.2	0.03	0.02	0.32	0.56	0.97	1.37	1.34
Return on Equity	0.6	1	0.17	0.22	3.83	11.42	18.92	18.5	15.26
RKB									
Net past dues	0.5	0.9	0.76	0.42	0.34	0.4			
Non Performing Loans/Loan Portfolio							0.54	0.56	0.14
Capital Adequacy Ratio	9.8	9.6	10.49	8.22	8.22	11.26	44.32	61.84	82.97
Liquidity	11.42	6.6	5.9	18.69	24.4	55.53	82.08	93.72	41.95
Profitability	0.8	0.8	1.4	0.99	0.93	1.24	1.79	1.23	3.03
Return on Equity	2.37	11.5	12.7	11.56	12.46	13.94	6.51	4.45	5.43

Table 2. Use of Credit Line by PFI and Component

PFI by Component	Credit Line at 31/12/2001 VND bill	Outstanding at 31/12/2001 VND bill	Use of Credit Line %
RDF:	1,311,929	1,285,989	98%
ACB	41,565	32,454	76%
BIDV	289,015	288,800	100%
EAB	44,336	39,200	88%
NAB	8,728	0	0%
PhNB	24,939	22,765	91%
Rach Kien	2,771	2,770	100%
VBARD	900,575	900,000	100%
FRP:			
VABARD	151,000	151,000	100%
Total	1,462,929	1,436,989	98%

Source: ICR
Note: VBARD and BIDV are state-owned

Annex C. People Met

Banks:

Vinh, Le Hong, M&E Division, VBARD
 Duong Quoc Anh, Director, banks and Nonbank Credit Institutions Dept. State Bank of Vietnam
 Le Phuong Anh, Expert, Project Management Dept. VBARD
 Nguyen Hai Long, Director Project Management Dept. VBARD
 Nguyen Manh Hung, Manager M&E Div., BIDV
 Nguyen Hai Long, Deputy Director, Techcom Bank branch
 Cao Cu Tri, Executive Vice President, BIDV
 Doan Hoai Anh, Deputy Director General, International Coop. Dept. State Bank of Vietnam
 Nguyen Van Binh, Deputy Governor, State Bank of Vietnam
 Quach Hung Hiep, Executive Vice-President, Transaction Center III, BIDV
 Dao Thu Thuy, Manager, Environment Management Division, BIDV
 Ngo Quy Cuong, Manager, Appraisal Division, BIDV
 Ms. Vien, Deputy Director, Agribank, Hoa Binh Province
 Ms Thuy, Dep. Man. Divisional Planning, Agribank, Hoa Binh Province
 Mr. Hai, Manager, Hoa Binh District, Agribank
 Mr. Duc, Director, Mai Chau District, Agribank
 Mr. Nguyen Hong Truong, Dep Dir. Mai Chau District, Agribank
 Mrs Lan Agribank Coordinator Ban Lac Handicraft Community
 Ms. Thuy, Techcom Joint Stock Bank, HQ
 Trinh Minh Duc, Accreditation Division, BIDV
 Dao Thi Hai Yen, Deputy Manager, BIDV
 Nguyen Thi Huong Mai, PFI Accreditation and Training Division

Borrowers or Potential Borrowers:

Mr. Hieu, Brick Factory Enterprise, Hoa Binh
 Mr. Quang, Piggery Enterprise, Hoa Binh
 Mr. Hoa, Tea Producer (& Fruit and Forestry Seed) Family Enterprise, Hoa Binh
 Mr. Khoi, dairy cows client, Ban Lac
 Mr. Tam, handicraft client, Ban Lac
 Ms. Thao, handicraft client, Ban Lac
 Ms. Phan, handicraft client, Ban Lac
 Hang Thang Co. Ltd, Bamboo Processor, Hoa Binh Province
 Mr Sung A Lu, cattle enterprise client (mountain area) Hoa Binh
 Mr. Ham A. Si, buffalo loan, Hoa Binh (mountain area)

Researchers:

Prof. Dao Van Hung, Vice-President, Academy of Policy and Development

NGOs:

Mr. Tam, Chairperson, Ban Lac Handicrafts Association

Mr. Tan A. Xa, Farmer Association Chairman, Hoa Binh Province (many members VBSP clients)

Action Aid

Donors:

Junichi, Imai, Senior Project Formulation Officer, JICA

Ms. Thi Hong Minh Chu, Financial Sector Officer, Asian Development Bank

World Bank:

Arie Chupak, ex TTL

Iain Shuker,

Nguyen The Dzung,

Xiaolan Wang, TTL

Trieu Quoc

Severin K

Alain Barbu

Hoonae Kim

Annex D. Borrower Comments

[from the Bank for Investment and Development of Vietnam]

Thank you very much for your letter of June 03, 2009 on Draft Project Performance Assessment of Rural Finance I (Credit No.2855). Regarding IEG concern on the imposed lending interest rate ceilings in Vietnam, BIDV, the agency responsible for the management and implementation of Rural Finance Funds, would like to have following comments:

1. The Government of Vietnam (GOV) and State Bank of Vietnam (SBV) determine the removal of interest rate ceilings would create better competition among financial institutions in providing financial services in rural areas, and are consistent in the pursuit of interest rate liberalization policy. Regarding the regulations, this policy has been prescribed in Law on Credit Institutions, in particular, namely Decision No.546/2002/QĐ-NHNN dated May 30, 2002 by SBV. Under which, the Decision stipulates that credit institutions are allowed to lend in accordance with market interest rate based on agreement between them and their clients. As such, in fact, the lending interest rate ceilings have been removed since 2002 in Vietnam. The prime rate has been used as a tool for reference and determination of market interest rate by SBV.
2. 2008 was a very tough and unusual year to the economy and the banking industry of Vietnam with the inflation peaking at 28% and global economic crisis. The deteriorated conditions forced SBV to adopt drastic monetary policy. Some credit institutions faced with liquidity problems and interest rates climbed up dramatically in the first 3 quarters. As for the stabilization package with focus on inflation fighting and interest rate reducing, the GOV must then re-use lending interest rate ceilings and consider it a temporary solution for urgent requirements. At the moment, SBV is actively working with GOV and National Assembly agencies to find out appropriate adjustments towards the liberalization of interest rate. In the short term, lending interest rate ceiling for consumption has been removed.
3. According to the data of May 2009 of VBARD, the Bank has been lending at 9% p.a for short term loans, 10.5% p.a for medium and long term loans and 12% p.a for consumption.
4. As for banking activities in rural areas: in recent years, joint stock commercial banks have been expanding to rural areas and many banks have realized big potential development of bank services in rural areas. In reality, all 24 PFIs in RF I and II have increased their number of branches and transaction points in rural areas. Some PFIs including Dai A, My Xuyen, Kien Long, Dai Tin, Western Bank have been established in rural areas regardless of long term appearance of VBARD. The competition in providing bank services to rural population, accordingly, has become more and more drastic and the main beneficiaries are the rural people. The dependence on VBARD therefore has been significantly reduced, which can be seen through the increased number of financial institutions participating in fund disbursement and the amount disbursed by VBARD in RF I and RF II. In RF I, there have been only 7 PFIs participating in the disbursement of project fund, of which VBARD's disbursement accounted for 73% of total outstanding loans; however, in RF II, there have been 25 PFIs and VBARD outstanding loans have reduced to 37% in end 2008 and expectedly even lower in RF III./.

The above are our some comments on the Draft RF I Performance Assessment Report by EIG that we would like to make.

With regards,

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