

Economics and Sociology  
Occasional Paper No. 1534

**RURAL DEPOSIT MOBILIZATION IN THE DOMINICAN REPUBLIC**

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Paper prepared for the World Bank



September, 1988

Revised  
December, 1988

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Complete financial intermediation implies loan as well as deposit services. Both loans and deposits provide income-increasing and risk-managing opportunities to holders of wealth. Both loans and deposits contribute to improved aggregate economic efficiency. Traditional approaches to the development of rural financial markets (RFMs), however, emphasized the demand for loans and neglected the demand for deposit facilities. Deposit mobilization by rural financial intermediaries, nevertheless, can be an attractive focus for the implementation of new policies and actions to promote RFM development. The USAID-sponsored Rural Savings Mobilization Project (RSMP) in the Dominican Republic (DR) has been an innovative experiment, designed to test the extent of the opportunities and problems associated with the mobilization of deposits from rural firms and households.

The DR's rapid financial development during the 1960s and 1970s was characterized by a strong urban bias. Almost 60 percent of all bank branches have been located in Santo Domingo and Santiago, the two largest cities. About 90 percent of all loans have been granted and 80 percent of all deposits have been mobilized in these two cities. At most 20 percent of the country's agricultural producers have received institutional loans; access to rural deposit facilities has been even more restricted. Banco Agricola (BA), a public agricultural development bank, has been the only institution with an important presence in rural areas, with its 31 branches scattered throughout the countryside.

Up to 1983, however, the BA had been an incomplete financial intermediary, which disbursed loans but did not mobilize deposits. Although authorized by its 1947 Charter to receive deposits from the public, in the absence of the appropriate incentives it had never attempted to tap this source of funds. Rather, it had been a "lending window" for the retailing of funds from international donors, government land-reform programs, and Central Bank rediscount lines. Loans had been granted on concessionary terms, in order to reach externally-determined clientele targets. Not surprisingly, this borrower-dominated institution lacked financial viability, did not offered farmers a permanent and reliable service, and was overwhelmed with default.

For the BA, the RSMP was a response to the loss of access to cheap donor funds and fiscal transfers in the early 1980s. This, combined with inflation, resulted in a 48 percent decline in the real value of the BA portfolio during 1982-86. While in 1980 the BA financed 254,000 hectares of crops, less than 75,000 hectares were funded in 1986. For the BA, the optimality of deposit mobilization was no longer an entirely academic question. With technical assistance from the Rural Financial Markets Program at The Ohio State University (OSU), the USAID Mission in Santo Domingo decided to sponsor a pilot rural savings mobilization project, based on the notion that funds for agricultural loans can be mobilized from the rural areas, if convenient, low-cost deposit facilities are offered. It was expected, furthermore, that deposit mobilization would trigger desirable institutional reforms.

Despite the urgent need for funds, the concept of deposit mobilization encountered considerable skepticism. It was claimed that rural households do not save, that they would not be willing to transform their wealth into financial assets, that they would not respond to incentives to deposit, and that the BA would not be capable of attracting a substantial number of accounts. The RSMP became a flexible experiment to test these hypotheses.

The RSMP included four closely linked activities: (a) pilot deposit mobilization campaigns by the BA and a few selected credit unions (CUs); (b) a general improvement of financial management by the BA and the participating CUs; (c) establishment of a Dominican research capability on financial market issues; and (d) dissemination of the results of the research efforts and institutional experiments.

The establishment of deposit facilities at selected branches of the BA was preceded by a year of complex preparation. The BA not only lacked experience in the management of deposits, but it was a troubled institution, burdened by cumbersome procedures, vulnerable to political pressure, and overwhelmed by loan delinquency. In July, 1984 passbook savings accounts were offered at the branch in La Vega. One at a time, during the following months these services were offered in four additional branches. When it became clear that rural deposits were being attracted by the BA, the decision was made to gradually expand the service to all of the bank's branches. The growth of deposits soon surpassed all expectations, as shown in Table 1.

Table 1. Banco Agricola de la Republica Dominicana.  
Deposit Mobilization Results, 1984-1987.

|                                | October<br>1984 | October<br>1985 | October<br>1986 | October<br>1987 | October<br>1988 |
|--------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Branches                       | 7               | 29              | 31              | 31              | 31              |
| Number:                        |                 |                 |                 |                 |                 |
| savings accounts               | 2,628           | 20,757          | 36,835          | 66,570          | 97,600*         |
| term deposits                  |                 | 274             | 321             |                 |                 |
| total                          |                 | 21,031          | 37,156          |                 |                 |
| Deposits<br>( '000 DR\$):      |                 |                 |                 |                 |                 |
| savings                        | 499             | 3,986           | 7,008           | 14,032          |                 |
| term                           | 537             | 2,965           | 2,454           | 7,885           |                 |
| total                          | 1,037           | 6,952           | 9,462           | 21,918          | 47,000*         |
| Consumer Price<br>Index (1976) | 210***          | 296             | 315             | 375             | 505**           |
| Total deposits<br>( '000 DR\$) |                 |                 |                 |                 |                 |
| real terms                     | 469             | 2,349           | 3,004           | 5,845           | 9,307**         |

\*: preliminary

\*\* : As of June, 1988.

\*\*\* : As of December, 1984.

Source: Gonzalez-Vega et al, 1988.

After one year, the BA had already mobilized a multitude of small savings accounts in the rural areas. The number of accounts continued to grow rapidly, even after all branches had already offered the new service, and reached almost 100,000 by the end of 1988. This is possibly the largest number of savings deposits in any Dominican bank and it compares well with the 85,000 loans the BA had accumulated in its portfolio over the years, particularly in view of multiple loans but not deposits per household. The amounts mobilized, measured in real terms, grew rapidly as well, even after inflationary pressures accelerated recently.

Graduate students at OSU have explored the reasons for this success. The BA offered its liabilities at essentially the same terms as the other banks, although at interest rates well below those paid for funds in the dynamic unregulated markets and, recently, below the rate of inflation. No compulsory depositing mechanism was forced upon borrowers, however. Thus, while 60 percent of the depositors had borrowed from the BA at least once, only 45 percent received loans during the campaign (1984-87). Surprisingly, therefore, at least 40 percent of the depositors represented a genuinely new clientele for the BA, which demanded only a safe and convenient means to manage their liquidity, but not necessarily loans. This was particularly the case among non-farming rural households. This strong demand for deposit services was observed despite adverse economic circumstances in the rural areas during the period (low returns to agriculture, inflation, and devaluation).

The most important determinant of the BA's success seems to have been a substantial reduction in the depositors' transactions costs. With its large network of branches, the BA was the first intermediary to ever offer deposit facilities in many localities. Over half of the depositors claimed that the BA account was the first bank deposit that they had ever possessed.

The CUs which participated in the RSMP, on the other hand, were not restricted by interest-rate and other banking regulations. In addition to loan expectations and lower transactions costs, therefore, the CUs were in a position to offer to their clientele attractive interest rates. In early 1985, four CUs be-

gan to actively mobilize deposits. Within two years, their assets had grown between three and ten times, as a consequence of the voluntary deposits mobilized and of substantially improved loan collection. The participating CUs were selected on the basis of their willingness to adopt the interest rate and portfolio management policies recommended by OSU. Recognizing that these policies are an important ingredient of success, the experiment will be replicated for about 40 CUs in a new USAID-sponsored project during 1989-1993.

Deposit mobilization is generally expected to contribute to the viability of financial intermediaries by strengthening bank-customer relationships and by improving information flows. This was indeed the case in the DR. At the same time, deposit mobilization at the BA created numerous "second generation" problems. The new deposit services, for example, imposed massive data recording requirements and the BA was forced to revise its accounting and data management systems and to introduce microcomputers in order to deal with this problem. However, because of unused installed capacity (i.e., overstaffing), the BA was able to add the new service at minimal marginal cost. Indeed, less than six persons were added to the bank's total staff for this purpose.

Similarly, the BA had difficulties in rapidly lending out the funds mobilized, given concerns about the risks of default, and the lack of experience in portfolio management of the branch managers, used to disburse targeted donor and government funds only. Decentralization eventually resulted in greater responsibilities and accountability for branch managers, who for the

first time generated loanable funds locally. Thus, the RSMP became a "Trojan horse" within the BA, which forced many favorable institutional changes.

In the case of the CUs, the most interesting development has been a drastic reduction in borrower delinquency, from ratios of over 60 to less than 10 percent of the portfolio. These results have reflected a change of attitude towards control and the role of new constituency interests, as net savers have been incorporated into the cooperatives, as well as expectations of a more permanent and reliable service on the part of the borrowers.

The RSMP has been a source of important lessons. The existence of a strong demand for deposit services in the rural areas of developing countries has been confirmed. This demand has been highly elastic to the net returns received by depositors (interest payments less the depositor's transactions costs). In the DR, the CUs attracted substantial savings with higher interest rates, while the BA competed primarily with reductions in the depositors' transactions costs. In both cases, moreover, expectations of higher-quality loan services played an important role. In both cases, deposit mobilization resulted in stronger institutions. The task has not been easy and numerous "second-generation" problems have to be resolved. Moreover, expectations of new and substantial inflows of cheap donor and government funds in the near future would rapidly reduce the incentives and weaken the will to offer rural depositors this crucial intermediation service.

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