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RURAL CREDIT IN CHINA

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CHINA has been an agricultural nation for over four thousand years, and somewhat more than 85 per cent of her total population belong to the rural class. It may be said that, in general, the credit needs of this large farming population are not nearly so well supplied as are the credit needs of the tradesmen and other classes of city persons, and that interest rates in the country are much higher than in the city. There are at least three important reasons for this state of affairs:

1. The small annual income of the farmers prevents them from making sufficient savings to meet such emergencies as funerals, sickness, short crops, and so forth. This statement is substantiated by the results of a study of 2,866 Chinese farms made by Professor J. Lossing Buck of the University of Nanking, which shows that the average farm area is 7.0 acres, and that the average yearly family income is only \$139.¹

2. There is a lack of mutual understanding between rural and urban classes which practically prevents investments in rural enterprises by city persons.

3. The credit supply of the country is far below the demand for credit. Furthermore, city banks do not accept farm land as security for loans.

Interest rates in country districts vary from 1.5 to over 10 per cent monthly. A monthly rate of 1.5 per cent is obtainable only from cooperative credit societies. As an extreme example of usury, it may be stated that the farmers near Nanking pay one dime as interest each month for every dollar borrowed.² This rate is available only to reliable farmers. Farmers with poor credit pay two dimes instead of one. In general, loans with high rates of interest are small loans made for short periods. This places the small farmer in a particularly unfavorable position. It is almost impossible for a farmer to regain his original economic position,

¹ Buck, J. Lossing: *Chinese Farm Economy*. p. 87. University of Chicago Press, 1930.

Family income is the actual amount of money gained by the operator from the year's business. It is obtained by subtracting the operator's cash farm expenses from his cash farm receipts. The currency in which values are given is Chinese silver currency (Mexican). The average bank exchange rate (Shanghai) of one hundred gold dollars into Chinese silver currency for the period 1921-25 was 189.30.

² One Chinese (Mexican) dollar equals approximately 12 dimes.

once he assumes debts bearing such heavy interest charges. As a result, the lands of the small farmers are gradually taken over by the money lenders. Eventually, the latter become landlords, while the farmers become tenants.

Surveys of some 500 farms, made in 1927, revealed the fact that the average amount borrowed per farm during that year was \$174.82 while the average repayment of principal per farm during the same year was \$34.35, resulting in an average net increase in indebtedness of \$140.47 per farm. The average rate of interest charged on the above loans was 3 per cent monthly, while the average rate of interest earned on the capital invested in 2,866 Chinese farms, as reported by Professor Buck, was 9.4 per cent per annum. This explains why most of the farmers would rather continue to follow poor farming practices than borrow money for productive purposes. Failure to follow improved farming practices is not entirely due to a lack of knowledge concerning such practices, but is due in large part to the fact that credit is not available at a reasonable cost. The establishment of a legal rate of interest by the National Government has tended to lower the interest rate somewhat, but it has not entirely solved the problem.³ Because of the heavy interest charges, farmers do not borrow except of necessity. In most cases the proceeds of the loans are used for consumptive purposes or to meet social obligations, rather than for productive purposes.

For the most part, farmers obtain their credit in one of the following forms: (1) short term cash or grain loans from private lenders; (2) farm mortgage credit; (3) shop credit; (4) pawn shop credit; (5) loans from mutual loaning and savings associations; and (6) loans from cooperative credit societies.

The percentage distribution of the various forms of credit, based on surveys of 500 farms, was as follows: Short term cash or grain loans, 32.6 per cent; farm mortgage credit, 27.7 per cent; shop credit 10.0 per cent; pawn shop credit, 5.7 per cent; credit from mutual loaning and savings associations, 24.0 per cent.⁴

³ The National Government established a maximum legal rate of 20 per cent per annum. However, owing to the difficulty of obtaining loans at the legal rate, some of the farmers are willing, at the suggestion of the money-lender, to add part of the interest on the contract as principal so as to keep the interest charges nominally within the legal rate.

⁴ Cooperative credit societies are a recent development in China. The amount of money borrowed by the 500 farmers included in the above survey from cooperative credit societies was a negligible percentage of their total indebtedness.

Short term cash or grain loans constitute the most common form of farm credit. The period of the loan varies from one month to one year, but is commonly from two to six months. Generally, neither security nor guarantee is required, and sometimes there is not even a written contract. The ease of obtaining such loans attracts the farmer to borrow in spite of the high interest rates charged.

In case the debtor fails to pay his debt when due, the professional money lender can go to the debtor's home and carry away the amount of grain necessary to pay the loan in full, without the consent of the owner. This can be done only by a professional money lender who has considerable power in the village and, in effect, enjoys a monopoly of the lending business. The government strictly prohibits such practices, and they have been done away with altogether in some regions.

Farm mortgage loans are commonly in rather large amounts, and the money is usually used to liquidate small debts or to defray extraordinary expenses such as those in connection with weddings or funerals. In mortgaging land, the farmer may either retain the right of farming the land by paying rent each year, or he may turn the land over to the mortgagee, in which case the income from the land would be counted as interest. The term of the mortgage is usually very long, but the farmer can redeem his land any time after the first three or five years.

The amount of shop or store credit varies in different localities. In some localities there is little or none while in others it makes up a large proportion of the total outstanding indebtedness.⁵ In the latter case, farmers are very punctual in paying their debts each year so that they can secure credit for the year following. Prices charged purchasers who buy on credit are very much higher than prices charged cash customers. This is especially true of the more important commodities such as rice, soy bean cake and so forth.

Pawn shops charge 2 per cent interest monthly and the maximum period of such loans is eighteen months. Extra charges, in addition to interest, are made in some instances, which raises the actual interest rate to 2.5 per cent per month. In some places, farm im-

⁵ For example, in Chang Shu District alone, farmers' purchases of bean cake amount to approximately \$20,000,000 annually, of which over 60 per cent represents purchases on credit. Prices to persons buying on credit are at least 2 per cent higher than prices paid by cash customers, and in addition, interest at the rate of 2 per cent per month is charged on outstanding accounts.

plements and grain may be pawned. While the pawn shops provide a convenient source of credit for farmers, they do not help a great deal since the majority of farmers do not have much which they can pawn. The number of pawn shops is decreasing.

The mutual loaning society, which is indigenous to China, is very popular in both rural and urban communities. Such societies are always organized by someone who wishes to borrow. He invites a number of his friends and relatives to become members while he becomes head of the society. Meetings are held at regular intervals. At each meeting each member turns over to the head of the society a certain sum of money for each share which he owns and the money collected in this manner, except that collected at the first meeting which always goes to the head of the society without interest, is turned over to some one member. The number of such collections which an individual member may receive is determined by the number of shares which he owns. If he owns only one share, he may receive only one such collection, and so forth. The amounts which the individual members pay for the use of the funds differs somewhat depending upon whether or not they receive one of the earlier collections or one of the later ones. In general, the payments are so arranged that the persons receiving the last few collections have somewhat the advantage on the basis of the returns which they receive on their money. In effect, the members receiving the earlier collections are in the position of borrowers, while the members receiving the later collections are in the position of lenders. In all cases after each member has received a collection for each share which he owns, the society is dissolved. Some of the more important ways of determining the order in which collections shall be allocated to members are as follows:

1. By throwing dice, in which case the member throwing the highest figure receives the collection. After a member has received one collection for each share owned, he may not, of course, throw dice for subsequent collections.

2. By competitive bidding, the member offering to pay the highest interest rate receiving the collection. However, after a member has received one collection for each share owned, he may not bid for subsequent collections. Under this method, the interest is paid in advance by deducting the interest charge from the collection. This system of determining the order in which each member

shall receive the collection is prohibited by the government since it tends to result in usurious interest rates.

3. By determining the order in which each member is to receive the collection at the time of organization. This is preferable to either of the other methods mentioned.

The advantages of the mutual loaning society are: (1) that it mobilizes local credit resources; (2) that it enables members to obtain loans at somewhat more reasonable interest rates (about 2 per cent per month); and (3) it provides a means for saving. Its principal defects are: (1) the frequent inability of the head of the society to fulfil his obligations, namely, the collection of the amounts due from the various members, or the payment of such amounts from his own resources in case of their default; (2) the fact that the society is frequently dominated by a few powerful persons; and (3) the fact that in many cases the benefits are unequally distributed among the members.

The cooperative credit societies are a new form of organization in China, and are still in an early stage of development. The first society was organized in Nanking in the autumn of 1923. There are now over 1,000 such societies, located chiefly in the provinces of Kiangsu, Hopei, and Chekiang. Although cooperative credit societies are new in China, and are still in an experimental stage, the cooperative idea is not new to Chinese farmers. The National Government has taken steps to promote cooperative credit organizations.

Most of the cooperative credit societies have been very punctual in making repayments, but there has been little or nothing turned over to the societies in the form of savings of the members. Apparently the only way to build a sufficient reserve fund in each society is to force the members to increase their membership shares each year.

A few of the encouraging developments in the field of cooperative credit may be briefly summarized as follows:

1. The provision for unlimited liability of the members of cooperative societies has been found to work out satisfactorily. This is not surprising in view of the fact that personal credit is traditionally prevalent in the rural districts of China and that under the family system each member of the family is liable for the debts of every other member.

2. Cooperative "grain saving projects" have been successfully

carried out by some of the cooperative savings societies, thereby enabling their members to carry themselves through the difficult period which usually precedes each harvest. Each member deposits every year a certain amount of grain, the combined deposits forming a reserve supply for lending to members in time of need. Repayments, both of principal and interest, are in the form of grain.

3. Cooperative irrigation and drainage projects have been carried out by some of the cooperative societies. Such projects reduce the chances of crop failure due to flood or drought, and on the low-lying rice lands, enable the farmers to grow a winter crop on the land.

4. The granting of short term loans for cooperative marketing has enabled farmers to sell their cotton crop at a net premium of 21.3 per cent over the local price. In silk producing districts, improved credit facilities have enabled farmers to produce silk of a better and more uniform quality, thereby raising the price at which their product sells as well as greatly widening the market for it.

The Farmers' Bank of Kiangsu Province, which was established in July, 1928, by the Kiangsu Provincial Government, grants loans to the rural cooperative societies in Kiangsu Province, and the number of such societies in that province is increasing rapidly. Up to the end of June, 1929, the 495 rural cooperative credit societies in Kiangsu had a total paid up share capital of \$31,104, and unpaid share capital of \$8,964.

The lack of cheap and adequate credit in rural communities is one of the important factors limiting agricultural production and rural improvement in China. Cooperative credit societies have an important rôle to play in China in the development of credit and savings systems in rural districts, which will not only provide sufficient working capital for the farmers, but will provide it on such a basis that they can borrow with some hope of retaining their financial independence.