

Study on Rural Economy and Rural Financial System Reform

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Abstract. Financial support for agricultural development and the growth of rural economy issue is a global issue. Rural finance is an important part of the financial system, the development of rural, and finance plays a positive role in rural economic development. We firstly explored the mechanism of financial system promoting rural economic growth, and then proposed new ideas on the reform of rural financial system, in terms of rural policy finance, rural commercial finance, rural cooperative finance and rural informal finance.

Current Situation of Rural Financial System in China

Rural Financial Service Structure. Through 30 years of development and reform, it has formed a relatively mature rural financial service system in China, constituting policy financial institution, commercial financial institution, cooperative financial institution and informal rural financial institution. Among them, only Agricultural Development Bank of China (ADBC) belongs to policy financial institution; there are two commercial rural financial institutions - Agricultural Bank of China (ABC) and Post Savings Bank of China (PSBC); rural credit cooperatives, rural cooperative banks, rural commercial banks all belong to cooperative financial institutions. These three types of institutions are regarded as formal rural financial organizations, while informal rural finance institutions refer to private finance organizations that are not wholly regulated by People's Bank of China and China Banking Regulatory Commission, including small loan companies, village bank, rural cooperative foundation and private banks, etc. They are playing the key role in rural economic development, as shown in Fig. 1:

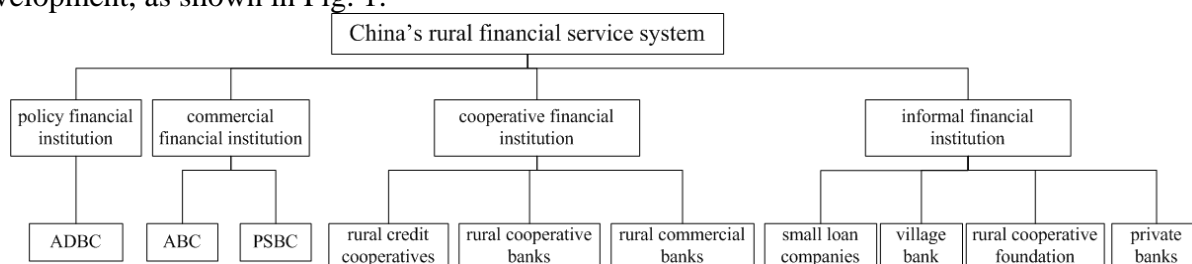


Fig. 1. China's rural financial service system

Major Dilemma. By analysis of the current situation of rural finance in China, there are some major dilemmas:

(1) Rural financial ecological environment

Current rural financial ecological environment is not conducive to the development of financial institutions. Firstly, communications, transportation and other infrastructures are poor in rural areas, and risks in agricultural production are very high, thus benefits of financial institutions cannot be guaranteed; secondly, rural credit system is not perfect, and farmers' integrity awareness is not high, so loans are often not properly recovered; thirdly, intervention from local government has affected the normal self-management of rural financial institutions.

(2) Rural financial network

With the deepening of the reform of the banking market, the main commercial banks gradually revoked or merged a lot of business outlets in rural areas. The current financial network coverage in rural areas is less than 20%.

(3) Rural financial products and services

The rural financial products and services cannot meet the needs of farmers and enterprises. The

services provided by rural financial institutions are very simple, even without the financial services beyond deposit and loan. Due to lack of agricultural insurance, the credit risk cannot be reduced, which hinders the development of rural finance.

(4) Asset structure of rural financial institutions

Due to the high risk of agricultural production, agricultural insurance blank and imperfect management mechanism, the non-performing loans rate of rural financial institutions is very high.

(5) Impact from new rural financial form

Private lending is very common in rural areas, becoming the main form of rural lending. It is hard for most of the farmers to loan from formal financial institutions, so they tend to get money through private lending when they have financial needs. In formal financial institutions, the loan procedures are very complicated, and it often takes long time to get the fund, or even they cannot get it. In this sense, the existence of informal financial organization is necessary, but it would contain a lot of risk if lack of supervision.

Mechanism of Financial System Promoting Rural Economic Growth

In Terms of Financial Intermediation Function. Financial intermediation function plays important role in rural areas that weak capital accumulation effect. In the rural financial system, to meet the fund demand in rural industrial structure adjustment and deepening industrial development, financial intermediation concentrates the decentralized rural savings, and provides cautious and speculative finance demand. Meanwhile, financial intermediation provides a good investment environment for rural savings, which is tantamount to inspire the rising savings rate in rural society. For multi-level financial functions requirements, a variety of financial instruments have derived in rural financial market, attracting farmers to abandon money saving with physical savings, thus increasing capital accumulation for rural economic development.

Financial intermediation function can not only realize the adjustment of the capital surplus, but also increase the rate of savings into investment. The intermediation function in rural financial system can reduce transaction costs and information costs, and solve the problem of information asymmetry between funds supplier and demander. In addition, in rural areas lack of funds, it provides more access to capital for farmers and agricultural enterprises, so encourages farmers to engage in more large-scale, more variety and higher yield production and management.

In Terms of Resource Allocation Function. The resource allocation function in rural financial service system plays a vital role in the development of rural economy. Firstly, at project evaluation stage, rural financial institutions evaluate and select the relevant projects for the relevant projects, and aggregate the relevant information and submit to investors; then, according to the assessment results obtained, investors make comprehensive comparison on market interest rate, return on investment and other indicators, so guarantee that the allocation of funds to the department can be fully used.

In the flow process of rural monetary funds, the flow pattern of material resources is directly controlled by monetary fund movement. The rational allocation of monetary funds is the basic premise to achieve the effective allocation of rural production resources. For industry sectors, through elimination of backward industries and promotion of emerging industries, the funds guide and continually promote the rural industrial structure upgrading, and promote rural economic development.

New Ideas on the Reform of Rural Financial System

Rural Policy Financial Reform. (1) Broaden thinking and innovative ideas. The relevant departments are supposed to vigorously develop the business scope of rural policy financial institutions. Take rural production conditions and ecological environment improvement, agriculture poverty alleviation and development, rural industrial structure adjustment as new business development direction; provide medium and long term credit funds that are required for agricultural production and infrastructure construction, including working capital, technological transformation

and storage, etc. The pace of financial reform should be moderate, that is, in accordance with the initial specified reform schedule, to avoid extreme reform trend.

(2) Take advantage of foreign financing. Uniform handle the international financial institutions and international organizations lending business, especially the agricultural projects lending from The World Bank, International Development Association (IDA) or Asian Bank. For the issues in terms of fund source, fund quality and fund structure, can raise funds from financial markets by releasing agricultural finance securities, and give appropriate subsidies.

(3) Liquidize the remnant assets. Supervise loan entities to join insurance to resist natural disasters, to ensure the quality of new loans. Establish and improve the loan risk compensation mechanism, and meanwhile draw a certain proportion from operating profit, subsidy funds, financial funds and own funds to establish the loan risk compensation fund.

Rural Commercial Financial Reform. (1) Improve the quality and safety of assets. Improve the accounting management system, to prevent malpractices loans and ensure benefits of running incremental loans. Establish and implement accountability system, and execute necessary economic and administrative penalties for illegal loan lenders. Carry out comprehensive and effective supervision on compliance of loan operation, legality of the procedure, accuracy of risk prediction, rationality of the use of funds, security, mobility and efficiency of credit assets.

(2) Improve financial services and financial products. Agricultural Bank's development objective is to become a commercial bank with modern enterprise system. Therefore, when rural commercial banks shrinkage business network, reduce the scale of agricultural loans and transfer funds, these are the necessary instinct to pursue the maximization of profit. However, Combined with China's national conditions and the current situation of agricultural economic development, rural commercial banks are supposed to find a balance between supporting the rural economy and the pursuit of their own development.

Rural Cooperative Financial Reform. (1) Focus on financial innovation. Financial innovation includes original innovation and absorption innovation. Compared to original innovation, absorption innovation has weak effect, but it is with smaller risk. Rural cooperative financial institution should deal with the relationship between two types of innovation: on the one hand, make considerable strength for original innovation, to seize the commanding heights of rural financial innovation; on the other hand, should make great effort for absorption innovation, and take advantage of the existing achievements of urban financial institution innovation to adjust accordingly.

(2) Play the role of market mechanisms. Adjust to the rural cooperative finance through market forces. Government departments should not implement too strict regulation on rural cooperative financial institutions, but allow them to carry out the financial industry combined with the actual situation in rural areas.

Rural Informal Financial Reform. (1) Establish and improve the relevant legal system. Relevant departments shall formulate laws and regulations on informal finance, and be mandatory to ensure the implementation of the law. At the legislative level, firstly, make clear definition about the objects of rural microfinance; secondly, clear the business management authority of the various agencies. In addition, increase the supervision and management of rural credit institutions and employees. For the Illegal activities in the course of rural financial services, should fight resolutely, so that purify the rural financial environment and allow rural finance to run in an orderly legal environment.

(2) Establish and improve the rural microfinance payment system. Firstly, the government should increase investment in rural finance policy, and local fiscal policy should provide financial support for rural financial institutions; secondly, rural commercial financial institutions should focus on financial services in rural areas, and invest the funds to agricultural projects; thirdly, liberate the rural cooperative finance, and through scientific and rational methods, clean up and punish the non-performing loans of rural credit cooperative loans.

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