Malaysia

AJDF Category B (Bank Pertanian Malaysia)

Report date: March 2001
Field survey: August 2000

1. Project Profile and Japan's ODA Loan

Site map: Malaysia

An Ipoh Plant Nursery Farmer

1.1. Background

Agricultural production has increased little since the 1970s in Malaysia. The major factor impeding the development of agriculture was the dual structure in which systematized export-oriented estate agriculture coexisted with inefficient and unsystematic smallholder agriculture. Another problem was that no small- or medium-sized enterprises had been developed in the agricultural sector. Under these circumstances, the government of Malaysia considered this project as one under which loans would be provided at a preferential interest rate as investment funds to promote capital investment in the agricultural sector and to enhance productivity. In addition, they expected that this project would offer domestic financial institutions an opportunity to shift the focus of their financing with a view to expanding the productive capacity of the country through, in particular, export promotion and the development of growth industries.

Japan, on its part, established the ASEAN-Japan Development Fund (AJDF) as part of its financial recycling scheme with the aim of helping ASEAN nations promote regional economic cooperation and private sector development, and accordingly, the decision was made to provide financial assistance[1] (Category B-the portion of a project contributing to the development of the private sector which is covered by Japan's ODA loan ("ODA loan")).

1.2. Objectives

The objective of the project was to provide long-term low-interest capital fund to

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[1] Category A covers projects contributing to the promotion of regional economic cooperation and Category B covers projects contributing to the development of the private sector.

small- and medium-sized enterprises predominantly in the agricultural sector, as well as to farmers in Malaysia through Bank Pertanian Malaysia (BPM-the Farmer's Bank), a governmental development finance institution, thus promoting the businesses of the subject enterprises and farmers.

1.3. Project Scope

The ODA loan covers the source fund of sub-loans which is necessary for the implementation of the project and the funds for consulting services.

Eligibility: Agricultural enterprises with at least 51% Malaysian shareholding, and farmers

Enterprises with paid-up capital not exceeding M$2 million and farmers with income not exceeding M$2,000/month

Eligible Industries: Agriculture including production of rice, palm oil, cocoa, coconuts, rubber, fruit and vegetables, forestry, fishery and processing of products of these industries

Items Covered by Loans: Capital investment and building (excluding land)

Terms and Conditions: (1) Loan amount: up to M$2 million (raised to M$5 million in 1991) (2) Interest rate: 6.5% per annum (upper limit) (3) Period: over 1 year up to 15 years (grace period up to 5 years) (4) Percentage of financing: less than 80% of necessary funds

Consulting services

1.4. Borrower/Executing Agency

Bank Pertanian Malaysia (guaranteed by the government of Malaysia)

1.5. Outline of Loan Agreement

Loan amount/Loan disbursed amount	¥10.442 billion/¥10.442 billion
Exchange of notes/Loan agreement	December 1988/December 1988
Terms and conditions	Interest Rate: 3.5%, Repayment period (grace period): 25 years (7 years), General untied
Final disbursement date	February 1994

2. Results and Evaluation

2.1. Relevance

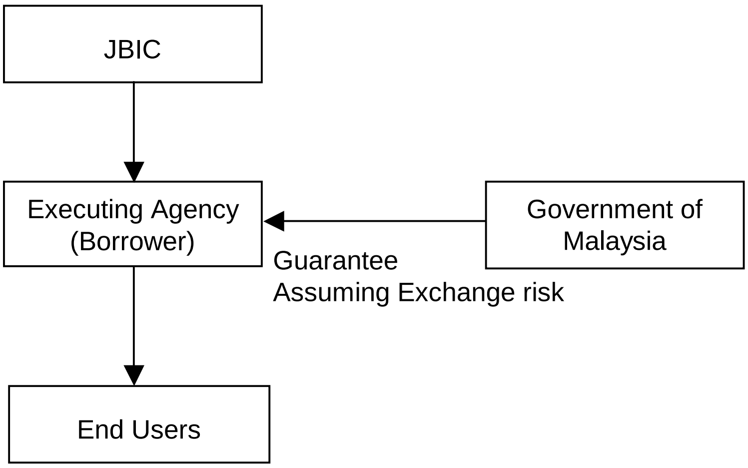
At the time of project planning, insufficient development of small- and medium sized enterprises in the agricultural sector was thought to be one of the factors impeding the development of agriculture in Malaysia. Therefore, the project plan was relevant in that it aimed to provide fixed funds at a low interest rate to small- and medium-sized enterprises that had no access to such funds in order to help them improve productivity and increase exports. As the agricultural sector's contribution to GDP had been diminishing every year, the project aimed to assist the development of the agricultural sector by extending loans to export-oriented enterprises and by covering a more diversified range of products. In this regard, the project was in line with the 3rd National Agricultural Policy (2001-2010) targeting improved productivity and competitiveness of the agricultural sector as well as the creation of sources for development of the agricultural sector. Thus, the project has maintained its relevancy to date.

2.2. Efficiency

Figure 1 Implementation Scheme

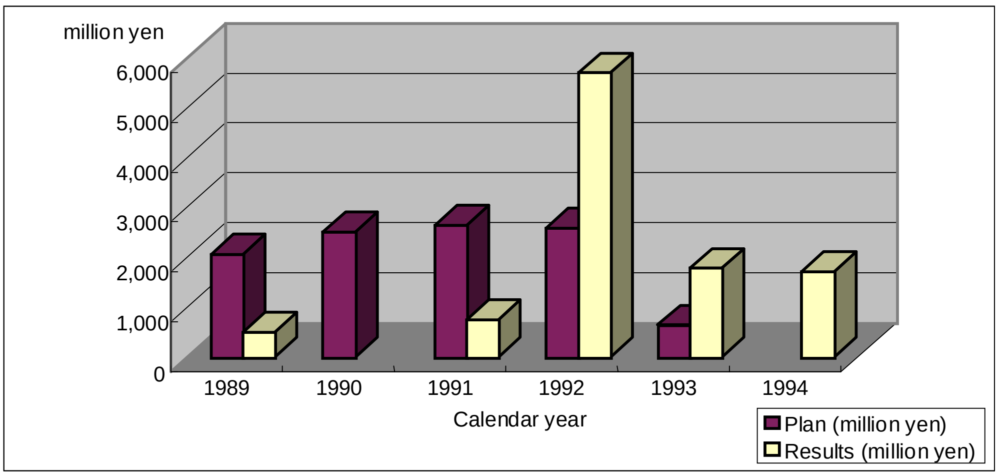
Interest rate 3.5%
Disbursement period 25 years (grace period 7 years)

Interest rate 6.5%
Disbursement period 15 years (grace period up to 5 years)



The portion of the loans covered by the ODA loan was scheduled to be disbursed over a 5-year period from 1989 to 1993. The disbursement was completed almost as scheduled with a delay of one year as shown in Figure 2.

Figure 2 Comparison of Original and Actual Disbursement



Sources: JBIC's data
Note: Amounts are based on the disbursed amounts of the ODA loan

Table 1 shows changes in the Base Lending Rate (BLR) and the Average Lending Rate (ALR) of commercial banks and the growth rates of GDP, the agricultural sector and the manufacturing industry from 1988 to 1995. Since 1988, the BLR and ALR of commercial banks have been maintained at around 7-9% and 8-10% respectively. Offering loans with the interest rate fixed at 6.5% per annum during this period meant providing small- and medium-sized enterprises and farmers who have less access to funds than large enterprises with a favorable opportunity to procure funds for investment.

Table 1 Changes in Interest Rates and Growth Rates of GDP, etc.

(%)

Year		1988	1989	1990	1991	1992	1993	1994	1995
Commercial banks	BLR	7.0	7.0	7.5	8.7	9.3	8.2	6.8	8.0
	ALR	9.0	8.7	9.0	9.7	10.3	9.7	8.2	9.3
Growth rate of GDP (%)		9.9	9.1	9.0	9.5	8.9	9.9	9.2	9.8
Growth rate of the agricultural sector (%)		2.7	4.8	-0.6	-0.1	6.9	-3.1	-1.9	-2.5
Growth rate of the manufacturing industry (%)		17.0	20.3	15.3	14.0	7.0	14.6	11.4	11.4

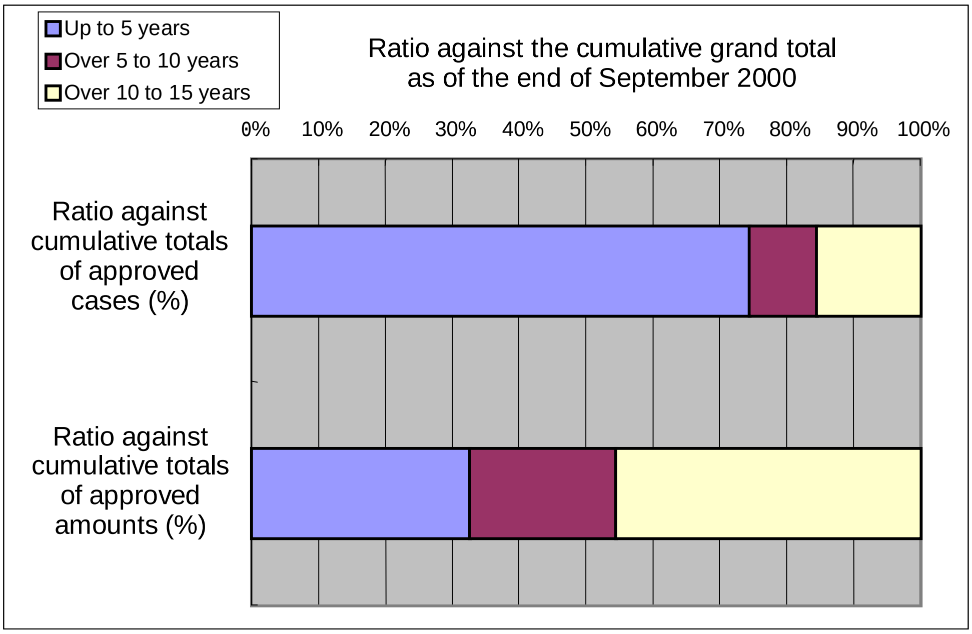
Source: Bank Nagara Malaysia (BNM) for interest rates and Department of Statistics for GDP statistics
Note: BLR and ALR are as of the end of each year.

In addition to the schemes implemented by BPM from 1988 to 1994, there were several schemes available to small- and medium-sized enterprises and farmers as part of directed finance. In comparison, the AJDF project which also covered non-Malaysian enterprises as eligible borrowers had been more attractive and convenient until 1993 when a directed financing scheme financed by the government and BNM was started along with the scheme by Ministry of International Trade and Industry (MITI) of Malaysia (neither require borrowers to be enterprises with Malaysian capital and the interest rate is 4% per annum).

Figure 3 is the classification of sub-loans by repayment period based on the cumulative total of actually approved loans as of September 2000.[2]

[2] Information on loans limited to first borrowers has not been obtained.

Figure 3 Classification of Sub-loans by Repayment Period



Source: BPM

In providing low-interest fixed funds under the AJDF project, the risk of exchange fluctuation was assumed by the government. The Malaysian government's commitment to the promotion of the agricultural sector including the development of small- and medium-sized enterprises on a long-term basis was one of the factors which contributed to the efficient implementation of the project.

2.3. Effectiveness

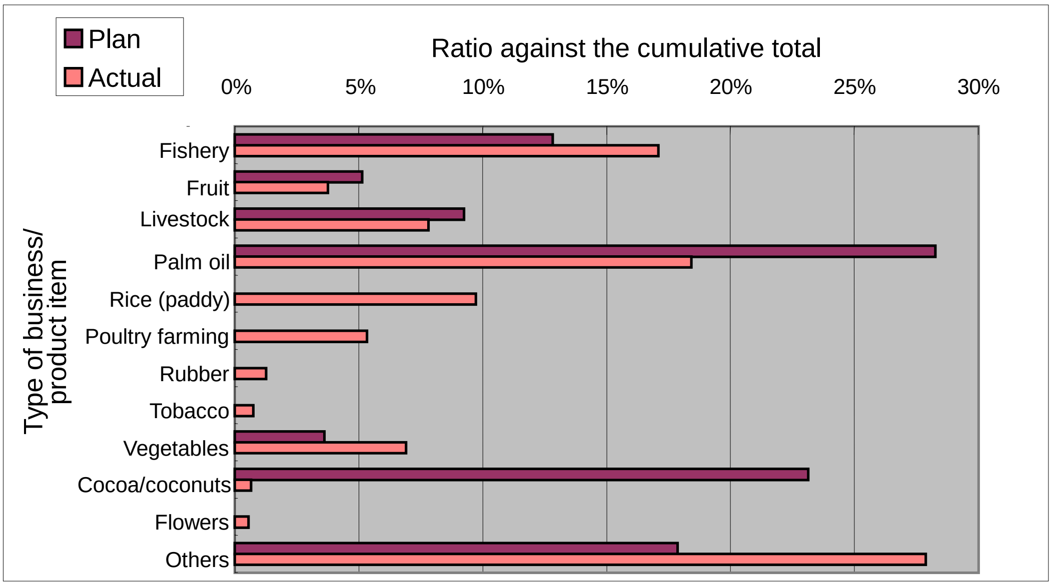
(2.3.1.) Status of Financing and End Users

The following is the analyses of the status of sub-loan disbursement by type of business and amount. All data are cumulative totals of the number of cases and amounts that have been approved since the start of the project as reported in semiannual progress reports submitted to the Japan Bank for International Cooperation (JBIC).

(a) Status of Financing by Type of Business or Product Item

Figure 4 is a comparison between the total loan amounts projected for 1989 to 1993 by type of business and product item submitted by BPM at the time of appraisal (plan) and the cumulative totals of actually approved loan amounts by type of business and product item as of the end of September 2000 (actual results). In the results, the types of business and product items eligible to receive loans were increased from the initial 7 types and items (fishery, fruit, livestock, palm oil, vegetable, cocoa, coconuts and others) to 44 types and items in a BPM list. It should be noted, however, that there were only 7 types of business and product items for which loans were given in over 100 cases of the cumulative total: fishery, fruit, livestock, palm oil, rice, rubber and tobacco. BPM explains that these results were produced in response to the demand for loans, and that oversupply of palm oil, cocoa and coconuts resulted in the smaller number of loan applications than planned. It was also mentioned that since the beginning of the 1990s BPM has been prioritizing agribusiness under the new management and promoting diversification of industries. On the whole, funds were provided to small- and medium-sized enterprises mostly in accordance with the initial plan.

Figure 4 Loan Amount by Type of Business and Product Item

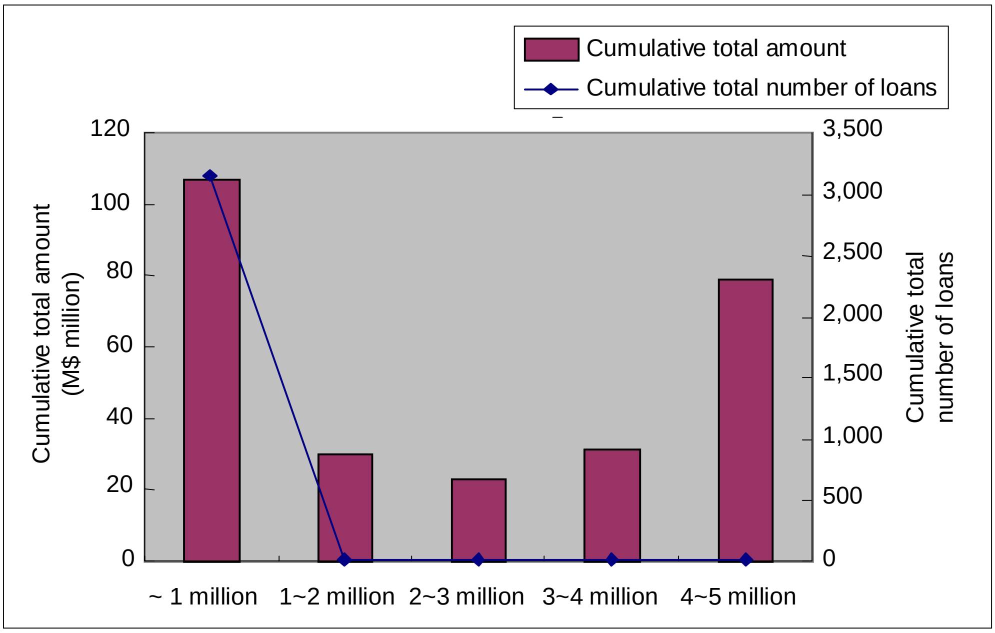


Source: BPM

(b) Results of disbursement by size of sub-loan

Figure 5 below shows cumulative totals of the amount disbursed as of the end of September 2000 by size of sub-loan.

Figure 5 Cumulative Totals of the Amount Disbursed by Size of Sub-loan (actual)



Source: BPM

In terms of the number of loans, nearly 99% of the cumulative total were loans of up to M$1 million, while these loans occupy a little over 50% of the cumulative total amount. Among other loans categorized as over M$1 million, sub-loans of over M$2 million were extended in 31 cases, accounting for nearly 50% of the total amount.[3]

(2.3.2.) New Investment and Business Expansion

As of the end of September 2000, the cumulative total (gross) of approved sub-loans was 3,215, amounting to M$271.0 million. The uses of sub-loans are classified into new investment, business expansion, renewal and others. The number of sub-loans disbursed and their amounts are shown below. Sub-loans for new investment accounted for 83.7% of the total in terms of the number of loans and 73.6% in terms of amount.

Table 2 Use of Funds

	Number	Percentage	Amount (M$ million)	Percentage
New investment	2,690	83.7%	206.8	73.6%
Business expansion	252	7.8%	35.2	13.9%
Renewal	71	2.2%	3.0	1.1%
Others (note)	202	6.3%	26.0	11.5%
Total	3,215	100.0%	271.0	100.0%

Source: BPM
Note: Unclassifiable capital investment

2.4. Impact

(2.4.1.) Achievement of Overall Goal

Although the agricultural sector's contribution to GDP is diminishing year on year, the project is believed to have been contributing to the creation of sources for the development of the agricultural sector in Malaysia to some extent by extending loans to export-oriented enterprises and increasing the diversification of products eligible for loans.

(2.4.2.) Impact on the Environment and Society

This is under the jurisdiction of the environmental agency of the government and, therefore, BPM did no more than study the profitability of the project and the state of markets. Since end users are not allowed to apply for loans without government permission, BPM confirms that such permission has been obtained prior to extending loans.

2.5. Sustainability

(2.5.1.) Viability of Borrower Enterprises and Farmers

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3 As already mentioned, BPM modified the loan agreement in 1991 to raise the maximum limit of sub-loan amount from M$2 million to M$5 million.

No data is available concerning the number of enterprises and farmers who have borrowed funds under the AJDF scheme and are currently still in business or are engaged in agriculture. The fact that, as of the end of January 2001, among all outstanding loans to enterprises and farmers (502), 350 (about 70%) loans were in arrears indicates that many borrowers of AJDF funds are having difficulty making repayments.

(2.5.2.) Sustainability of the Project

The situation in which a large number of sub-loans have fallen into arrears, coupled with the impact of the economic crisis, has pushed up the percentage of loans in arrears in recent years. Also, the utilization of second loan disbursement from the special account is limited. It is important to improve and strengthen the ability to examine applications and the management of sub-loans for the future.

Table 3 shows the status of the cash collection of primary sub-loans. Even before 1997 when the currency crisis occurred, the cash collection ratio was around 60 %. The ratio has been declining further since the currency crisis.

Table 3 Status of Cash Collection

Unit: M$ thousand

	1994	1995	1996	1997	1998	1999	May 2000
Principal and interest due (a)	53,527	60,342	62,883	64,336	59,597	62,200	38,760
Collected amount (b)	32,339	35,568	35,730	40,132	33,162	34,148	9,796
Cash collection ratio (b)/(a)	60.4%	58.9%	56.8%	62.4%	55.6%	54.9%	25.3%

Source: BPM

Figure 4 shows the percentage of loans in arrears (Arrears Ratio by Number) and the percentage of loan amount in arrears (Arrears Ratio by Amount) which indicate the status of collection of sub-loans.

Table 4 Status of Collection of Sub-loans

	1994	1995	1996	1997	1998	1999	May 2000
Number of outstanding loans	2,596	1,902	1,423	1,095	837	663	
Number of outstanding loans in arrears	1,675	1,310	1,072	895	687	567	
Arrears Ratio by Number (%)	64.5	68.9	75.3	81.7	82.1	85.5	
Outstanding loan amount (M$ million)	153.9	164.4	163.6	151.9	131.7	105.8	103.4
Loan amount in arrears (M$ million)	21.2	24.8	27.2	24.2	26.4	28.1	29.7
Arrears Ratio by Amount (%)	13.8	15.1	16.6	15.9	20.1	26.5	28.7

Source: BPM

The Arrears Ratio by Number had increased from 64.5% in 1994 to as high as 85% as of the end of 1999. One of the factors that raised the ratio was insufficient utilization of second loans from the special account, which resulted in a decrease in the number of sub-loans. The Arrears Ratio by Amount, which had remained below 20% until 1997, increased to exceed 20% in 1998. As of May 2000, the ratio was nearly 29%.[4]

As of the end of January 2001, 502 loans using AJDF funds were outstanding, amounting to M$91 million. Among these, 350 loans were in arrears[5] with an outstanding amount of M$30 million. Therefore, the Infection Ratio and Arrears Ratio by Number and Amount were 69.7% and 33.3% respectively.[6] The table below, which gives the breakdown of arrears by amount, indicates that most loans in arrears are in amounts of less than M$1 million.

Table 5 Sub-loan Arrears by Loan Amount (as of January 2001)

Amount of Sub-loan	Number of loans	Amount
Less than M$ 1 million	98.2%	59.1%
M$ 1 million or over and less than M$ 2 million	0.3%	2.0%
M$ 2 million or over and less than M$ 3 million	0.3%	6.1%
M$ 3 million or over and less than M$ 4 million	0.6%	13.4%
M$ 4 million or over and less than M$ 5 million	0.0%	0.0%
M$ 5 million or over	0.6%	19.4%
Total	100.0%	100.0%

Source: BPM

Loans in arrears as of the end of 1999, which amounted to M$28.052 million, are classified by period in arrears as below.

Table 6 Classification of Loans in Arrears by Period in Arrears

Unit: M$ thousand

Period in Arrears	3-6 months	6 months-1 year	1-2 years	Over 2 years	Total
Amount in Arrears	1,053	598	4,418	21,983	28,052
Ratio	3.8%	2.1%	15.7%	78.4%	100.0%

Source: BPM

4 The total amount of all BPM's outstanding loans was M$1,864 million as of June 2000. Among these, loans in arrears amounted to M$737 million and the Arrears Ratio by Amount was 39.5%, 10% higher than that of the AJDF project. BPM has said that non-performing loans (NPL) in arrears for 1 year or longer accounted for 22% of loans in arrears as of June 2000.

5 BPM classifies its loans in arrears, called gross NPL, into 6 categories by the period in arrears from A (less than 3 months) to F (over 24 months). Interest on loans in arrears for over 12 months is not accounted for as profit. In the case of category E loans, 50% of the amount which is considered irrecoverable is offset against reserves, and in the case of category F loans which are in arrears for over 24 months, 100% is offset against reserves.

6 BPM pointed out the following situation, including its own financing management system, as the cause of delays in repayments and defaulting by end users:

(a) Because of a shortage of bank employees who manage sub-loans, adequate technical support has not been provided to end users;

(b) End users' awareness of their repayment obligations is low; and

(c) Economic conditions have deteriorated due to external factors.

More than 78% of loans in arrears have been in arrears for over 2 years. By industry, loans in arrears in fishery-related industries are large both in number and in amount.[7] By type of business and product item, the outstanding amount is large in livestock farming (beef cattle, dairy farming), miscellaneous food products, rice, vegetables and tobacco. As for cocoa, market conditions have been extremely bad, although there have been signs of recovery recently.

(2.5.3.) Utilization of Special Account

Disbursement of the ODA loan was completed in 1994 and thereafter the special account has been used to provide loans. However, sub-loan approvals have decreased since 1996 and no loans have been approved since 1998 up to the time of evaluation.

Table 7 Cash Flow of BPM's Special Account: State of Utilization (Estimate)

Unit: M$ million

	1994	1995	1996	1997	1998	1999	May 2000
Number of approvals	29	88	6	3	0	0	0
Balance brought forward	56.7	70.7	53.6	46.3	44.1	47.1	51.0
Sources	71.4	35.6	35.7	40.1	33.2	34.1	9.8
Disbursement from JBIC	39.1	-	-	-	-	-	-
Sub-loan repayment	32.3	35.6	35.7	40.1	33.2	34.1	9.8
Applications	57.4	52.7	43.0	42.3	30.2	30.2	4.5
Disbursement of sub-loans	48.1	35.7	22.2	18.9	2.9	0.5	4.5
Repayment of principal	0.0	7.1	12.8	14.8	17.6	19.6	
Payment of interest	9.3	9.9	8.0	8.6	9.7	10.1	
Balance carried forward	70.7	53.6	46.3	44.1	47.1	51.0	56.3

Source: BPM
Note:
1) Figures for 1995 and thereafter were estimated based on the difference between the balance of the ODA loan and that of sub-loans in 1994.
2) The revenue includes both the principal and interest because they were difficult to separate.

(2.5.4.) Sustainability of Executing Agency

(a) Organization and Management System

The Board of Directors of BPM comprises 7 members including representatives of the Economic Planning Unit (EPU) and the Ministry of Finance as well as politicians. In addition, there are three alternate directors respectively representing EPU, the Ministry of Finance and the Ministry of Agriculture who attend the board of directors meetings on behalf of absent directors.

BPM has a total of 238 offices including 12 state offices, 142 branch offices and 84

[7] Fishery cases are those in which funds were provided by BPM to procure fishing boats. The risk is high in such cases for the following reasons: many borrowers sell their catch to the brokers from whom they borrowed operation funds, putting less priority on the repayment to BPM; catches are insufficient; and fishing boats cannot be accepted as security on loans.

patriot centers[8] (according to 1998 annual report). The total number had decreased to 235 in 1999. It had 2,379 employees as of 1999, including 307 specialist employees and 2,072 support employees.[9] BPM has not been hiring in recent years and, therefore, the number of employees is declining as shown below.[10]

Table 8 Change in Number of Employees

	1997	1998	1999
Specialist	327	312	307
Support Staff	2,195	2,126	2,072
Total	2,522	2,438	2,379

Source: BPM
Note: Specialist employees are those who have a degree or higher academic qualification and support employees are those who have diploma or lower educational qualification.

Regarding the AJDF project, loan appraisal is performed by Pinj. Kmoersil (Commercial Loan , 8-10 staff) of JAB. Operashi Kredit (Credit Operation Dept.) at the head office and Pengawasan. Pinjaman (Loans Supervision, 6-8 staff) of the same department is responsible for managing financing. The data obtained in the field survey reveals that loan approvals were being made by branch offices. However, as mentioned below, all loan approvals are being given by the head office as of February 2001.

BPM mentioned that the financing activities of the AJDF project have been carried out smoothly in terms of organization and procedures through promotion and marketing activities utilizing the nationwide network of branch offices, and that the efficiency of in-house procedures for the approval of sub-loans has improved through the implementation of the project. Meanwhile, BPM is aware of the shortage of skilled employees and the lack of employees’ experience in screening particularly in the field of agribusiness.

(b) Financial Status

BPM’s financial status during the past 9 years is shown in the table below. BPM has been suffering from excessive liabilities since 1989[11], and had a M$318 million shortage in capital as of the end of FY 1999.[12] The authorized capital of BMP is M$ 100 million and the paid-up capital is M$42.5 million. In spite of excessively

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[8] These centers, which were established with a view to attracting deposits, are open for business 3-4 days a week operated at fixed counters instead of movable ones. They played an important role in collecting deposits at low cost after 1991.

[9] As of February 2001, there are 75 Credit Officers (professional employees) and 135 Credit Support Officers (support employees).

[10] Given that the amount of loans has been decreasing in the last 3 years, the outstanding loan amount per employee has been decreasing.

[11] BPM appropriated M$ 100 million for reserves in 1988 and M$ 259 million in 1989, and reported a deficit for both years.

[12] In 1997 and 1998, in particular, the increase in the financial cost resulted in a loss in net profit.

small capital, it has increased its assets threefold in the past 9 years (the gross assets as of 1999 amounted to M$4,307 million). Particularly rapid increases have been observed in deposits in the procurement area, and in investment and loans in the area of operations. However, deposits dropped sharply in 1999 from the previous year.[13] Achieving sound finance through capital expansion and disposal of bad loans is an important issue, which BPM will need to tackle for the future.

BPM was 100% funded by the Ministry of Finance of Malaysia as of September 2000. According to the audit report for FY1999, the Ministry of Finance agreed to capitalization of M$429.6 million of the government's long-term loan and M$125 million loaned under the Agriculture Special Credit Scheme in its letter dated December 30, 1998. Therefore, BPM has not accounted for interest on these debts since January 1, 1999. In the evaluation survey conducted in February 2001, BPM mentioned that capital increase requires revision of the Bank Pertanian Malaysia Act, that the amount of credit to be capitalized is M$530 million, and that the capital has yet to be converted although the government (Ministry of Finance and Ministry of Agriculture) has basically agreed to this increase. The statement concerning the negotiations with the government on capital increase appeared in the audit report as early as 1991, indicating that this is an issue of 10-years' standing. However, concern was raised in the audit report for 1999 over that fact that no increase in capital has not realized.

PBM, in its part, has taken the following measures in an effort to improve financial conditions: 1) established new departments to handle commercial business, enterprises and retail lending respectively on an exclusive basis in order to improve the quality of loans; 2) introduced a unified system to manage all loan approvals while setting policy guidelines for high-quality loan appraisal; and 3) in addition to the loan management department, established a new department to handle loans in arrears and implement measures to address the issue of bad loans in a timely manner in cooperation with state branches.

[13] As of the end of FY1999, percentage ratios of loans, investments (corporate bonds, trust funds, etc.) and cash and bank deposits against total assets were 32%, 43% and 21% respectively.

Table 9 Balance Sheet

Unit: M$ million

	1995	1996	1997	1998	1999
Cash, bank deposits, etc.	833	850	518	645	967
Loans receivable	1,126	1,466	1,563	1,471	1,358
Investments and affiliated companies	1,903	1,662	2,221	2,090	1,866
Fixed assets	113	121	123	124	117
Total Assets	3,976	4,098	4,425	4,330	4,307
Deposits	3,244	3,303	3,660	3,753	3,381
Institutional loans	238	285	244	272	618
Borrowings	614	601	601	612	600
Japan's ODA loan	219	207	195	183	171
Other liabilities	25	35	93	15	26
Capital	-146	-126	-172	-323	-318
Total Liabilities and Shareholders' Equity	3,976	4,098	4,425	4,330	4,307

Source: BPM

Table 10 Profit and Loss Statement

Unit: M$ million

	1995	1996	1997	1998	1999
Profit					
Commission and interest received	127	155	185	212	175
Return on investments	153	188	172	203	189
Other	-10	2	0	-31	-30
Sub-total	270	345	356	384	335
Government subsidy	26	35	7	4	20
Total	296	379	362	389	355
Expenses					
Interest paid	176	223	270	360	199
Personnel expenses	38	49	44	45	46
Reserves	8	27	30	43	36
Other	50	60	63	90	69
Total	271	359	408	539	350
Net profit	25	20	-46	-150	5
Loss carried forward	-201	-181	-226	-376	-372

Source: BPM

3. Lessons Learned

Nothing particular

Comparison of Original and Actual Results

Item	Plan	Actual
1. Project scope	1. Sub-loan Eligible industries: Agriculture including production of rice, tobacco, palm oil, cocoa, coconut, rubber fruit and vegetables, forestry, fishery and processing of products of these industries Eligibility: enterprises with at least 51% of Malaysian shareholding and farmers, enterprises with paid-up capital not exceeding M$2 million and farmers with income not exceeding M$2,000/month (farmers with annual income from M$1,000 to M$24,000) Items covered by loans: Capital investment and building (excluding land) Terms and Conditions: loan amount up to M$2 million; interest rate: 6.5% per annum (upper limit); period over 1 year up to 15 years (grace period up to 5 years); percentage of financing: less than 80% of necessary funds 2. Consulting services	Same as the plan (Except that the loan limit has been raised to M$5 million. The requirement of “farmers with income not exceeding M$2,000/month” has not been confirmed by submitted materials.)
2. Implementation schedule	1989 to 1993	1989 to 1994
3. Project cost Foreign currency Local currency Total ODA loan portion	 ¥10.442 billion ¥ 0 ¥10.442 billion ¥10.442 billion	Same as the plan