# Graduate School of Humanities and Social Sciences
# Doctoral Program in International political Economy
# Executive Summary

## Formal credit and the impact on household's welfare: New empirical evidence from Vietnam

## フォーマル・ローンが世帯の厚生に与える影響：ベトナムにおける新たな実証分析

**Bui Thi Van Anh**
**200730080**

Recent years have seen an increased interest in the role of credit and microfinance on household outcome. Most of works found the positive role of credit on smoothing income and contributing to poverty alleviation. By providing the households with access to financial services and credit, the credit help-low income people improve productivity, management skills; create jobs; smooth income flows and consumption costs; enlarge and diversify their businesses; increase their income and other benefits such as health care and education (see Morduch 1995, Khandker 1998 and 2001, Coleman 2002, Remenyi 2000, Zeller at al., 2001). However, the level of impact found not consistent in all the cases and all the countries during the period.

Understanding the key role of credit on household welfare as well as on economic development, the Vietnamese Government try to make use the best this tool by renovation the financial system as well as create more opportunities to household can access credit. The financial market in Vietnam has developed rapidly after renovation and segmented into two core sectors as the formal (banks, credit institution, people's credit fund, social- political organization, job creation fund) and the informal (money - lenders, relatives, friends). This paper using data from Vietnam Household Living Standard Survey 2004 will contribute to the empirical literature on the effectiveness of formal credit on household welfare in Vietnam. The purpose and contribution of this thesis is: firstly, to propose and implement an econometric framework, that will minimize the limitations of research methodology employed in previous studies; secondly, the work will provide empirical evidence about the impact of formal credit on household welfare in Vietnam, in both urban and rural area.

To estimate the impact of credit on household welfare, we use a linear model to interpret the impact of credit on household welfare with credit (loan size of loan dummy) as the explanatory variable in the outcome function. The controlling variables include household characteristics, location characteristics, market conditions. The dependent variables as proxied for household welfare are expenditure of household, income, living consumption, food and nonfood consumption. Because the endogeneity of credit (confirmed by Hausman test), this paper used the standard solution is to employ instrument variables (IV) and two-stage least square (2SLS) method. For this paper, three IV used: competitor's characteristic (average land square owned by other household in the commune exluding that household), the market interest rate informed by formal lender, the distance to nearest bank/bank branch from a village where households are located. There IVs passed the overidentification test and can be used as valid instrumental variables for endogenous independent variable formal credit.

Results from the first stage revealed some determinants that effect to borrowing of household as well as the determinant of access to credit. We have found the determinants of loan size and credit participants to be consistently based on household characteristics, such as ethnicity of the household, dependent share, classification by authorities of being poor. Some location characteristics will be determinants of credit as geographical region or infrastructure condition.

On the impact of credit on household welfare, we found credit has positive and significant effect on household welfare in term of both loan size and loan dummy at 1 percent and 5 percent level of significant. With to access borrowing, the household have opportunities to increase their welfare by 0.75 per cent of expenditure, 0.79 per cent of income and 0.35 per cent of living consumption. The impact on food consumption and non-food consumption respectively are 0.44 per cent and 0.56 per cent when other factors are not changed. These numbers reflect the significant gains that could arise from access to credit in Vietnam. If credit increases by 10 per cent, expenditure and income will increases by 0.88 per cent and 0.90 per cent in 2004 respectively. The growth rate of food and non-food consumption following an increase of 10 per cent credit is 0.53 per cent and 0.65 per cent respectively. Living consumption will increase by 0.42 per cent when their borrowing increases by 10 per cent. This result confirms our hypothesis that access to credit or increase in the amount of loans also increases household economic welfares. This also reaffirms the findings by some recent studies (Quach et al,. in case of Vietnam, Khandker in Bangladesh or Coleman in Thailand, Remenyi in some South Asia countries…).

However, the effect we found is small, but it is significant to household welfare anyway. This permits to have optimistic expectations about the role of credit on the poverty reducing and on the living standard increasing in Vietnam. The findings here may assist policy makers on evaluation effectiveness of credit as a tool for increasing household economic welfare in comparison to using another one.