IMPLEMENTATION OF MONETARY POLICY IN 2000 AND SOME PREDICTIONS

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Generally, the total volume of negotiable instruments increased by 20% in 2000 as compared with 1999 (the increase rate in previous years were: 39.25% in 1999; 23.9% in 1998; 26.1% in 1997; 22.7% in 1996 and 22.6% in 1995). The money supply (M3) increased by 25% in 2000 (the increase rate in previous years were: 39.3% in 1999; 25.6% in 1998; 26.1% in 1997; 22.7% in 1996).

As for bank loans and deposits, the outstanding loan, up to Dec. 31, 2000, increased by 21% while the bank deposit increased by 25% as compared with Dec.31,1999. Increases in these indicators in previous years were: 19.2% and 34.0% in 1999; 16.4% and 34% in 1998; 22% and 25.7% in 1997 respectively. The proportion of overdue debts in 2000 was under control, staying at 11.7% as compared with the total outstanding loan (2% lower than the proportion in 1999).

In implementing the monetary policy, the central bank adopted the use of indirect instruments in an effort to integrate into the international financial community.

1. Use of base rate in preparation for liberation of interest rate

In the early 1990s, the SBV fixed the lending and deposit rates. In the mid 1990s, only the lending rate-ceiling was fixed. After many discussions, the SBV decided to regulate the monetary system through the base rate as of Aug. 5, 2000. Commercial banks are free to allow their lending rates fluctuate within a narrow band on either side of the base rate. Under this mechanism, the SVB publicizes the base rate, discount rate and refinancing rate every month.

From August to December 2000, the base rate on loans in the domestic currency stayed at 0.75% a month. The narrow band on either side of it was 0.3% for short-term loans and 0.5% for long- and medium-term ones. Bank interest on loans in foreign currencies is based on the Singapore Interbank Offered Rate for 3-month term plus a narrow band of 1.0% for short-term loans and 2.5% for long- and medium-term loan. The refinancing rate rose from 0.4% a month in August to 0.5% a month in November while the discount rate rose from 0.4% to 0.45% a month.

In the last months of the year, the demand for capital rose, most commercial banks raised the deposit rate while the lending rate was left unchanged. The rate on 12- month deposits in the VND rose to 0.6%-0.65% a month (or 7.2%- 7.8% a year), on 6-month deposits 0.4%-0.55% a month, and on 12-month deposits in the dollar 5.5%- 6.0% a year. The rate on 12-month deposits in Vietnam was nor high neither low in comparison with rates offered in other countries: Hong Kong dollar 6.4%; peso 11%; won 8.8%; baht 3.5%; ringgit 4%; Australian dollar 6.43%, euro 5.28%; yen 6.18% and the dollar 6.65%. The interest rate became a competitive instrument for banks. State commercial banks were ready to offer a rate of 0.7% per month to customers with good track record. The lending rate in rural areas was slightly higher: 1% - 1.05% a month. The common rate on loans in foreign currencies was 7.0% - 8.5% a year. Thus, the lending rate on loans in the VND fell to a level never seen in the past ten years and not different from the rate offered by many neighboring countries. Companies have stopped complaining about high or low bank rates.

The application of base rate helped form an equal relation between customers and banks: companies could choose what bank to do business with and banks had to try their best to attract customers and cut overheads.

2. Use of reserve requirements

In 2000, the required reserve was fixed at 5% of bank deposits of under-12- month terms in city banks and 1% in rural banks. Reserve requirement for deposits in foreign currencies was raised from 5% to 8% as of October 2000 and to 12% as of December 2000. Generally, the record low level of required reserve for deposits in domestic currency encouraged commercial banks to supply more loans to customers, while three adjustments to required reserve for deposits in foreign currencies aimed at dealing with rises in foreign currency deposits during the last months of the year.

3. Money market

From February 2000 on, the SBV organized 43 auctions to sell T-bills on a weekly basis. According to the plan, VND6,500 billion worth of bills are to be sold, and VND 4,800 billion worth of bills were awarded. The winning interest rate in the first quarter of the year was 6% per year, then it fell to 4.9% and rose to 5.30% - 5.35% at the year's end. Most winning bidders were state commercial banks (the Bank for Industry and Commerce of Vietnam was awarded in 50% of auctions).

4. Open market operation

In July 2000, the open market operations were officially brought into operation. Fourteen commercial banks have been given membership. Trading sessions are held every ten days. Up to Nov. 29, 2000, the SBV has conducted 13 trading sessions in which VND1,428 billion worth of T-bills and SVB bank bills were traded (of this sum, the SVB bought VND878 billion and sold 550 billion). The interest rate varied between 4.9% and 5.58% a year. However, these operations are new to SVB officials, and this market wasn't active as expected.

5. Deposit insurance

In 2000, the deposit insurance service came into operation in August, and has attracted over 1,000 customers (out of 1,026 banking institutions). The premium is fixed at 0.15% of the total deposit with maturity of under a year. The maximum deposit insurance for a depositor is VND30 million.

6. New entrants to the banking system

In 2000, no bank went out of business officially but some were under special supervision of the SVB. They are fulfilling procedures for merger or acquisition.

Some non-banking institutions came into being. They are three finance companies (ANZ-V. Tract, a foreign-owned leasing company; Shipbuilding Finance Company affiliated to the Vietnam Shipbuilding Corporation; and Oil Finance Company affiliated to the Vietnam Oil Corporation) and five brokerage firms affiliated to joint stock commercial banks (ACB, Military, Agriculture and Rural Development, Industry and Commerce, and Investment and Development). The Bank for Industry and Commerce also formed its Mortgage Company. Thus, there are, up to now, four leasing companies, nine leasing joint ventures, four finance companies affiliated to state Corporations, five brokerage firms and one mortgage company in Vietnam.

7. Improvements in the legal framework for banking service

The State Bank Law and Banking Institutions Law came into effect as from Oct. 1, 1998 as replacements for two Banking Ordinances which had been issued in 1990. Many law documents have been issued to direct implementation of these two laws. New mechanisms, however, still have shortcomings and fail to facilitate the supply of capital to the economy.

In the first half of 2000, many discouraging signs made their appearance: low growth rate, weakening spending power, stagnant price index, surplus of capital in banks, etc. Banking authorities had to take strong measures to stimulate the demand for bank loans. From August to October, the SBV made a series of important decisions:

- Decision 266/2000 dated Aug.18, 2000 on the supply of fiduciary loans by commercial banks, joint stock finance companies and joint venture banks if their overdue debts are lower than 5% of total outstanding loan.
- Decision 283/2000 issued on Aug. 25, 2000 providing regulations on bank guarantee service as replacement for six decisions issued in 1994-95.
- Decision 284/2000 dated Aug. 8, 2000 providing regulations on lending as replacement for the Decision 324 issued in 1998.
- Circulars 06/2000 dated April 4, 2000 and 10/2000 dated Aug. 31, 2000 on the deposit insurance replacing four previous circulars issued in 1996-97.
- Decision 418/2000 dated Sep. 21,2000 on customers who could get loans in foreign currencies, six classes of customers were added to the list publicized previously.
- Decision 428/2000 dated Sep.22, 2000 on the policy to supply bank loans to farm: Farms owners are allowed to get fiduciary loans up to VND20 million, or up to 50 million if they own fishery farms. The previous decisions only allowed them to get fiduciary up to VND10 million.

These Decisions and Circulars have helped facilitate the banking services and allowed banks diversify, and enhance quality of ,their services. Commercial banks started to supply credit to demand stimulating projects and offer more personal loans. In addition, the supply of loans serving policy goals is beefed up: more low-interest loans have been supplied to the poor, residents in remote and depressed areas, university students, etc. In 2000, the outstanding loans for the poor reached over VND4,000 billion, increasing by 15% as compared with 1999.

8. Control of foreign exchange and exchange rate

By publicizing the exchange rate offered by the interbank foreign exchange market, the SBV could gradually devalue the VND against the dollar without causing sudden changes in the exchange rate or difficulties for companies. In the last months of the year, the exchange rate fell by from VND5 to 7 in each trading session. According to the SBV Exchange Control Office, the exchange rate fell by 3.1% in the interbank foreign exchange market (from VND14,016 to 14,450 to the dollar), by 2.9% in the community of commercial banks (from VND14,042 to 14,460) and by 3.96% in the free market (from VND14,137 to 14,700). The depreciation of the VND was still smaller than that of currencies of other countries: baht −14.5%; yen -5.97%; peso −21.25%, rupiah -24.18%; rupee – 7%; Singapore dollar -5.31%; Taiwan dollar -2.9%; euro -20.0%; and Australian dollar -19.4%.

The gradual depreciation of the VND, low interest rates on loans and deposits in domestic currency and high interest rate on deposits in foreign currencies made customers prefer to borrow in the VND and deposit in the dollar. That is why the deposit in the dollar in commercial banks rose quickly, three times faster than deposit in the VND, representing 40% of the total bank deposit. When the bank interest on the world market rose, many Vietnamese banks deposited their dollar stock with foreign banks with a view to making some profit. On the other hand, outstanding loan in the dollar increased slowly.

As for the exchange control, the SBV made Decision 258/2000 on Aug. 14,2000 on regulations on foreign exchange offices replacing previous regulations.

According to Decision 418/2000 made on Sep. 21,2000 by the SBV Governor, six more classes of loans in foreign exchange could be supplied by banks. Eligible for these loans are persons or organizations that need foreign exchange to pay for imported goods or services needed for local production and business; invest in projects approved by the PM; invest in production of exports; pay external debt before it becomes due (if the debt is guaranteed by a domestic banking institution), or want to discount export bills, etc.

According to Decision 468/2000 by the SBV Governor, foreign-invested companies or foreign partners in joint ventures could buy foreign exchange from local banks when they want to import materials, pay principal and interest for short-term external debts, pay principal and interest for long-term debts approved by the SBV, pay principal and interest for borrowings in foreign exchange from banks that are allowed to operate in Vietnam, transfer legal capital; capital for reinvestment; and capital for realizing business cooperation contracts after stopping operation.

However, many people are worrying about the widespread use of the dollar as a legal tender in Vietnam. But we should admit that this situation is unavoidable because the VND isn't convertible, the banking system is poorly developed, smuggling activities are widespread and law enforcement is weak. According to IMF experts, this situation is common among developing and transitional economies, so the Government couldn't use administrative measures to ban the use of the dollar because it would affect badly the flow of immigrant remittance and export promotion.

The public are also interested in the fact that a large amount of foreign exchange is deposited with foreign banks while the shortage of it is so great that Vietnam had to borrow from international organizations and foreign governments. The cause of this situation is the difference between interest and exchange rates in Vietnam and the world market. When the rate on loans in the dollar in Vietnam is lower than the rate offered by foreign banks and no local company could afford borrowings in foreign exchange, it's understandable for local banks to deposit it with foreign banks. The Government should take other measures to encourage the demand for capital in foreign exchange instead of preventing local banks from doing so.

9. Some predictions of banking activities in 2001

The Vietnam's monetary policy aims at accelerating the growth rate and controlling the inflation, therefore main targets set for 2001 will be corresponding with those achieved in 2000. It's planned that the total volume of negotiable instruments will increase by 20% - 22%; the M3 by 24% - 26%; bank deposit by 25%-27%; and loan by 20% - 22%.

More companies and institutions will come into operation: the Mortgage Company in the second quarter of 2001, the Bank for the Poor and Political Objectives in the third or fourth quarter, Export Promotion Fund run by the Bank for Foreign Trade in the first or second quarter in preparation for the formation of the Eximbank.

The Bank for Agriculture and Rural Development will establish its brokerage firm. In 2001, it's planned that from five to six commercial banks will be dissolved, merged or sold; from 80 to 100 people's credit funds will go out of business; and regional credit funds will be turned into branches of the Central Credit Fund.

The legal infrastructure for banking service will be made more suitable to international practices. The SBV will beef up the mechanism for controlling the banking system by using indirect instruments. Competition between banks will be keener but state commercial banks, branches of foreign banks and some major joint stock banks will have advantage.

The control through base rate will be strengthened. It's estimated that the base rate will stay at 0.75% a month for some time. The deposit rate will be slightly lower in the first half of 2001 and rise again in the second half.

Discount and refinancing rate will be the same as in 2000. The open market operations, market for T-bills and interbank foreign exchange market will be perfected and help beef up the control mechanism through base rate.

The exchange rate will be kept close to changes in the world market. The exchange rate will keep on falling and reach the rate of VND15,000 to the dollar by the end of 2001. Commercial banks will have large stock of foreign exchange. SBV branches will be authorized to grant license to bring foreign exchange abroad, customers need not go to Hà Nội to get this license.

We hope that there will be fairer competition in the banking business and the banking system will contribute more to the economic development in 2001.■