

POST-CRISIS MONETARY POLICIES: PROBLEMS FOR CONCERN

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1. Present situation of the world economy

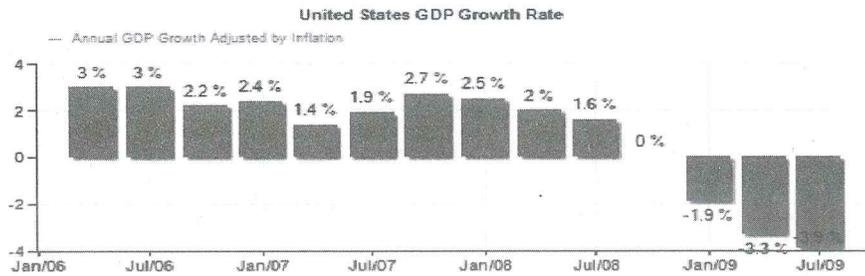
Everything started in late 2006 when the American realty market was frozen and its value fell drastically, which led to the crisis of housing credits; increased bad and dubious debts and insolvency. In June 2007, two hedge funds of Bear Stearns (the US fifth biggest investment bank) went bankrupt after staking their money on securities guaranteed by sub-prime loans for investors in real estates and in August 2007 the American Home mortgage filed for bankruptcy.

From then on, the US economy fell into a difficult situation when bankruptcies and mergers of a series of financial institutions took place: Merrill Lynch bought by the Bank of America; and Bear Stearns suffering a loss of US\$3.2 billion and sold to JP Morgan Chase at US\$2 per share (it was worth US\$170 per share one year before). Lehman Brothers declared bankrupt after unsuccessful attempts to find strategic partners; Fannie Mae, Freddie Mac, Goldman Sachs, Morgan Stanley and AIG all depended on emergent credit from the FED. The only one to blame was "Godfather" Alan Greenspan – former director of the FED for successive 18 years, from 1987 to 2006 – who had adopted a cheap money policy without a strict con-

trol, which allowed increases in sub-prime, housing and personal loans, high regard for unruly free market; stock and derivative markets, and poorer inspection of the financial system. Up to the end of August 2009, the FDIC report included 416 banks in its latest blacklist that controlled a total asset of some US\$300 billion. From early 2009 to Sep. 5, 2009, 89 banks in the U.S. had been dissolved.

The US financial crisis spread quickly and produced profound effects on the world economy, and it became the worst financial crisis in the history. When numerous economies fell into crisis, governments and central banks all over the world have quickly adopted unilateral, bilateral and multilateral measures to intervene and save their markets, such as cutting the base rates, injecting more money to the financial system, lowering the required reserve ratio, buying bad debts and shares of some banks, increasing the deposit insurance, offering stimulus packages, cutting taxes, raising the unemployment allowance, among others. Up till now, however, the world economy still faces certain difficulties and governments have to keep a close watch on changes in both domestic and international markets in preparation for emergencies.

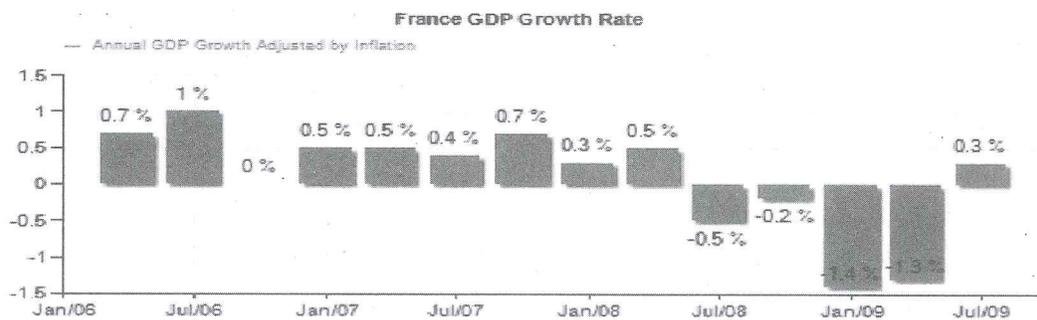
Figure 1: The US economy is still in recession in 2009



The US financial crisis led to the global one and economic recession in most economies. The world economic growth rate fell from 5.1% in 2007 to 3.1% in 2008. In 2009, based on situation in the U.S., Europe, Japan and China, the world growth rate is estimated at -1.3% and with some recovery it may rise to 2.9% in 2010. As for the US economy, analysts thought it was still in recession when its GDP growth rate was -1.9% in the first quarter of 2009 and -3.9% in the second one and its unemployment rate rose from 9.4% to 9.7% in August 2009. The European situation was a little better. Its growth rate moved from -4.9% in the first quarter to -4.6% in the second one. Unexpectedly encouraging data from some European economies evoke some hope about an early end of the global recession when France and Germany gained a growth rate of some 3% in the second quarter from -3.5% in the first one.

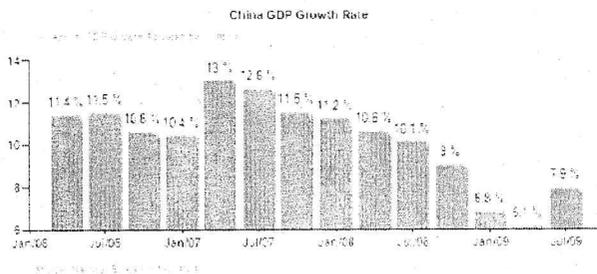
According to the latest report from the Japanese Cabinet Office issued on Aug. 17, 2009, its growth rate in the second quarter rose by 3.7% compared with the corresponding period last year after falling by 11.7% in the first quarter. Compared with the first quarter, the Japanese growth rate in the second one rose by 0.9% due to increased export and stimulus package from the government. As for China where the growth rate has varied between 12% and 13% for years, it still maintained high rates (10% in 2008; 6.1% in the Q1 of 2009; and 7.9% in the Q2) in spite of the global recession in the past two years. Reasons for this growth rate is very simple: Chinese nationalism shows itself clearly in production and trade, its cheap labor and raw materials allow it to produce goods of low prices, thereby expanding its market share in the crisis years. Thus, in spite of some difficulties because of high unemployment rates in many countries (the U.S., Japan and Europe), some light at the end of the tunnel made its

Figure 2: Signs of recovery of the French economy in the second quarter of 2009



appearance at the end of the second quarter of 2009. The world is expected to stop the economic recession and gain a growth rate of 2.9% in 2010.

Figure 3: Chinese economy is still in recession as compared with 2008



2. Vietnamese monetary policy before and after the crisis

In Vietnam in the years 2000 – 2008, the average growth rate was always over 7.5%. In 2008, the GSO reported that the growth rate was 6.23% while the CPI – inflation rate was 19.9%. Its export value in 2008 was US\$62.7billion while the import one was US\$80.7 billion, and the trade gap was US\$18 billion. These data show that the Vietnamese economy went from bad to worse along with the world economy in 2008 and the first quarter of 2009. This means that the Government should adopt flexible policies appropriate to the world and domestic monetary and economic situation.

In 2009, the growth rate target was reduced from 6.5% to 5% and a stimulus package of VND143,000 billion was offered to curb the recession tendency, stabilize the economy at macro level, and ensure social welfare. The monetary and fiscal policies have provided the economy with a good support, especially the stimulus package of VND17,000 billion that was turned into subsidies in form of low-interest loans for companies, thereby stimulating the market demand and investment. Up to August 2009, the economy gained a growth rate higher than the one in July when the industrial output rose by 10.6% as compared with the corresponding period last year. In many provinces, the industrial production gained high growth rates: Đà Nẵng 17.6%, Hà Nội 16.8%, Thanh Hóa 15.4%, and HCMC 11.4%.

In the first eight months, total sales of goods and services rose by 18.4%; export value equaled

US\$37.3 billion while the trade gap was US\$5.1 billion equaling 13.7% of the export value. Compared with July 2009, the August CPI rose by 0.24%, or 3.47% compared with the last December one. The gross investment in the first eight months equaled 42.5% of the GDP while the realized FDI in this period reached US\$6.5 billion.

The growth rate in the second quarter rose to 4.5% from a rate of 3.1% in the first one. Considering the first half of the year, the GDP rose by 3.9% compared with the corresponding period last year. The GDP growth in the third quarter was 5.76%, much higher than a rate of 4.5% in the second quarter, making the growth rate in the first three quarters rise to 4.56%. It allows us to expect that the planned growth rate of 5% for 2009 may be achieved. These data show that the Vietnamese economy is on the road to recovery and may gain a growth rate of 6.5% or 7.0% in 2010 if suitable policies are adopted.

Figure 4: Vietnamese economic recession in 2008

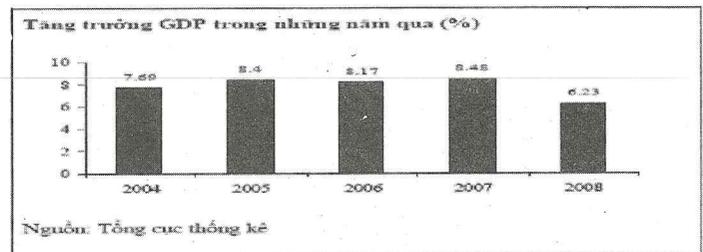


Figure 5: ADB prediction of the Vietnamese macro economy

3.10.1 Selected economic indicators (%)				
	2009		2010	
	ADO 2009	Update 2009	ADO 2009	Update 2009
GDP growth	4.5	4.7	6.5	6.5
Inflation	4.0	6.8	5.0	8.5
Current acct. bal. (share of GDP)	-11.5	-7.0	-9.7	-9.0

Source: Staff estimates.

The monetary policies before and after the crisis were not strictly a tight or cheap money one and based on signs from the market instead. In 2008, to control the inflation, the SBV raised the base rate many times along with the required reserve ratio, and exerted strict control over in-

crease in the bank credit. When the world economy was in recession in the second half of 2008, and Vietnam suffered some deflation in the last quarter of 2008, the SBV decided to reduce the required reserve ratio and base rate, and supplied short-term capital to banking institutions in difficulties through its open-market operations. Namely, the SBV adjusted the base rate seven times in 2008: three times the SBV made it higher – from 8.25% a year to 8.75%; 12%; and 14% – with a view to slowing down the increase in the bank credit; and four times the rate was cut – from 14% a year to 13%; 12%; 11%; and 8.5%) – in an effort to move to a cheaper money policy and prevent further recession. These adjustments forced banking institutions to reduce their lending rate from 21% a year to 12.75%, and the increase in the bank credit was kept at 22% (this figure in 2007 was 54%).

In 2009, the SBV kept employing flexibly instruments of the monetary policy to lower the lending rate, provide more liquidity and help banking institutions to expand their lending service. The base rate was reduced from 8.5% to 7% per year (the max lending rate is set at 10.5%), the refinancing rate from 9.5% to 7% per year, and the discount rate from 7.5% to 5% per year. In addition, the required reserve ratio was reduced from 6% to 3% for 12-month fixed and call deposits in the VND, and from 2% to 1% for fixed deposits in the VND with maturity of 12 months and longer.

The present monetary policy is a flexible and controlled one that aims at stopping the economic recession (a growth rate of 5% as a target), creating more jobs, keeping the inflation rate under 10%, ensuring safety for the banking system, and improving the balance of payments.

Data about September 2009 show that the CPI rose by only 4.11% compared with the last December one, and by 2.42% compared with September 2008. The 2009 CPI is estimated at somewhere between 7% and 8%. Thus, the SBV decision to keep the base rate at 7% up to the end of 2009 is reasonable. To keep the refinancing rate at 7% per year and discount rate at 5%; and use the open-market operations to regulate disposable capital of banks is necessary in the near future. Until recently, there has been an opinion arguing that the present cheap money policy might make the infla-

tion rate rise higher and the situation in March 2008 might repeat. This argument also mentions risks involved in the program to subsidize loans for companies and says that such subsidies can be turned into investments in securities and real estate or sent to wrong destinations. However, encouraging signs from the market in recent months have shown that a tight-money policy is not appropriate and the Government had better implement the monetary policy flexibly according to changes in the market forces.

In implementing the policy on interest rate, the SBV should pay full attention to macroeconomic targets and changes in the CPI and above all, it should regulate according to the core inflation, because the inflation in Vietnam is subject to various external and internal factors (especially the external ones) and its high openness to trade (170% of the GDP). In Vietnam, prices of food and rice are important to decisive to the CPI. Changes in prices of rice and crude oil in particularly affect greatly the CPI and inflation rate.

Up to September 2009, it's estimated that the total liquidity rose by 21% or 22% compared with the figure in Dec. 31, 2008. Total deposits with banking institutions up to September 2008 rose by 22-23% compared with Dec. 31, 2008. Total credit supplied up to August 2008 rose by 28-29% compared with January. Thus, an increase of 30% or 32% of bank credit by the end of 2009 is reasonable enough (this figure in 2008 was 22%). The SBV, however, should beef up its inspection in order to ensure safety for the whole banking system and limit the credit risk.

As for commercial banks, besides expanding their market shares and credit supplied, they should ensure loan quality and beef up inspection before and after lending.

Regarding the exchange policy, the SBV, to help banking institutions set the exchange rate when facing complex changes in the foreign exchange market and reduce differences between the official and unofficial rates, increased the band around selling and buying prices for the dollar three times in 2008, from $\pm 0.75\%$ to $\pm 1\%$, $\pm 2\%$ and $\pm 3\%$, as compared with the average rate offered by the inter-bank market. When the trade gap increased in early 2008, the SBV, on June 10, 2008, increased the average rate on the inter-bank market by 2% (from VND16,139 to 16,461 to the

dollar), and by 3% more (up to VND16,989 to the dollar) on Dec. 25, 2008. This measure created a new price level for 2009 to promote the export, limit the trade gap and improve the balance of payments.

On March 23, 2009, the SBV Governor signed the Decision 622/QĐ-NHNN to increase the band around the exchange rate to the dollar from $\pm 3\%$ to $\pm 5\%$ as from March 24, 2009. This Decision made the exchange policy more flexible and suitable to changes in the market forces and allowed banks and companies to work out their business plans for 2009 in a more proactive manner. In addition, the SBV sold more foreign exchange to banks in order to facilitate import of essential goods, stabilize the exchange rate and prevent speculation on foreign exchange.

The exchange rate, especially the one to the dollar, ceases to be a worry for commercial banks and companies in the near future. In August 2009, the SBV informed that it was buying foreign exchange from foreign investors in large quantities. At the macroeconomic level, the balance of trade in the first three quarters was deficit (the trade

gap was US\$6.5 billion compared with US\$18 billion in 2008) while US\$7.2 out of 12.5 billion worth of registered FDI have been realized, and US\$1.7 billion out of US\$3.2 committed ODA could be disbursed in the near future. The SBV, therefore, has no reason for depreciating the VND, and it had better pay full attention to stabilization the exchange rate in order to secure macroeconomic stability. Falls in the export are due to decreases in the market demand and prices on the world market, not to an unreasonable exchange rate. The SBV, however, should implement the exchange rate policy more flexibly and intervene more actively in the market to reduce differences between official and unofficial rates.

At present, the Vietnamese economy has passed its crisis period as seen from a global aspect. When 94 out of 118 countries gain no growth rate or suffer a negative rate, Vietnam is included in a group of 22 countries that gain positive growth rates, which allows us to recognize positive effects of economic policies adopted by its Government.

Figure 6: Thailand is still in recession in 2009

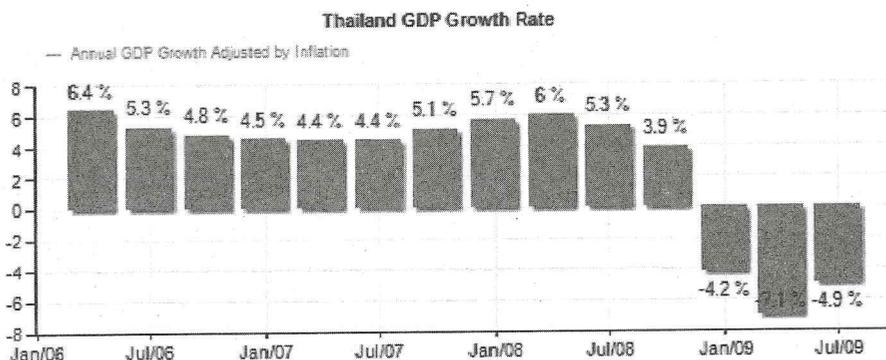
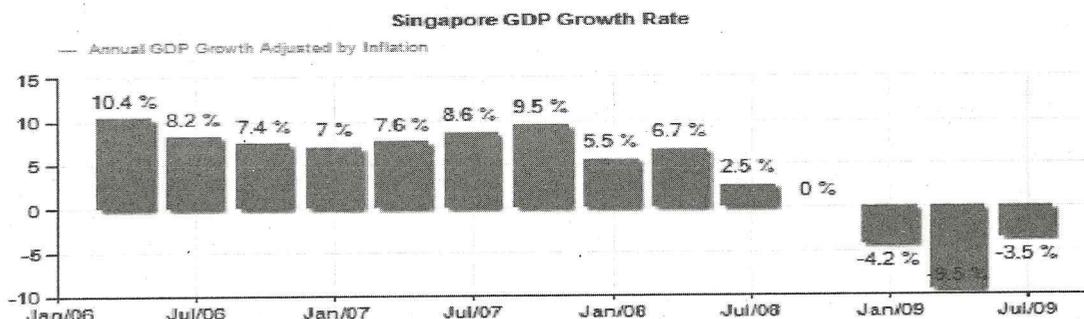


Figure 7: Singapore is still in recession in 2009



In the near future, however, besides implementing the monetary policy flexibly based on signs from the market and macroeconomic targets, the SBV should pay full attention to the following problems:

- Beefing up the supply and disseminating information about the monetary policy in order to prevent negative effects caused by misunderstanding and unreasonable worries; and reforming the banking system with a view to facilitating relations between banking institutions and customers, thereby improving performance of the SBV and the whole system.

- Program to provide subsidized loans according to PM Decisions (131/QĐ-TTg dated Jan. 23, 2009; 333/QĐ-TTg dated March 10, 2009; 443/QĐ-TTg dated April 4, 2009 and 497/QĐ-TTg dated April 17, 2009) and SBV guidelines must be carried out actively and continuously. Inspection and supervision of the supply of such loans must be carried out regularly in order to ensure that they are sent to right destinations.

According to an SBV report, up to Sep. 24, 2009, VND404,256.10 billion worth of subsidized loans has been granted: VND62,181.79 billion to state-owned companies; 273,161.70 billion to non-public sectors; and 68,912.60 billion to personal businesses.

- Inspection and supervision are also important to the task of ensuring safety for the whole system as it is expanding its scope and network. At present, the banking system in Vietnam comprises

five state-owned commercial banks with 1,203 branches of level 1 and transaction offices; 39 joint stock commercial banks with 898 branches of level 1 and transaction offices; 40 branches of foreign banks; five foreign banks; five banking joint ventures; 17 financial leasing companies, and one central people's credit fund with some 1,000 local branches. Violations of banking regulations discovered by inspections and investigations must be punished properly and timely. This is one of salutary lessons learned by all countries suffering the crisis. A document publicized by the INF on March 6, 2009 says that the main reason of the financial crisis is the failure to control strictly the banking system and observe the market disciplines ■

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