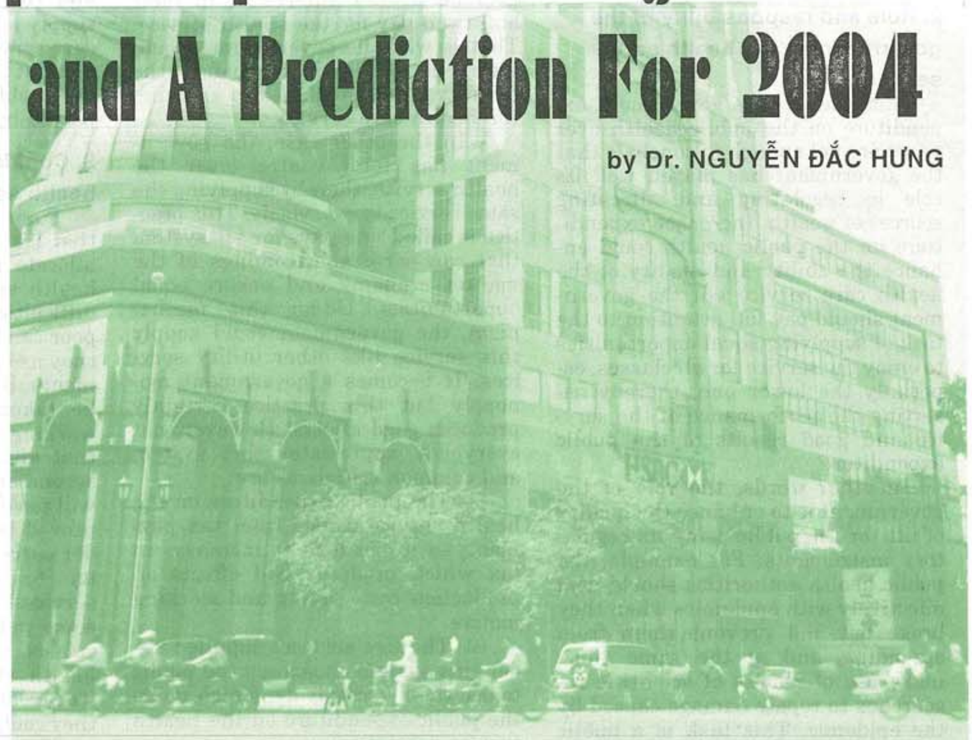
Monetary Policy and Banking Service in 2003 and A Prediction For 2004



by Dr. NGUYỄN ĐẮC HƯNG

In recent years, the FED has many times reduced the interest rate to 1%, the lowest level ever seen for 45 years, in order to deal with the recession and unemployment. A weak dollar could help the U.S. to reduce the trade gap. Its budget deficit has risen to an anormous US$455 billion in 2003 and it is expected to reach US$530 billion in 2004. The trade war in terms of clothing and electronics between China and the U.S., disputes over tariffs on steel between the U.S. and EU, the American demand for a depreciation of the Chinese yuan, Iraq problems, and political crisis and terrorism in the Middle East, have made the dollar fall drastically against other hard currencies and the gold price rise to a record height ever seen for the past eight years. All of these factors have produced profound effects on the world economy, including Vietnam.

In 2003, the implementation of the monetary policy and operation of banking sector experienced major changes in the foreign exchange market, interest rate and exchange rate.

But our rough estimate is that the implementation of the monetary policy and opeation of the banking sector gained important achievements in 2003 contributing a lot to the economic growth and inflation control. The banking system operated well and made reasonable profits. The total deposit increased by some 20% compared with the end of 2002 (the bank deposit in HCMC rose by 30.8% and in Hà Nội, 18%). Total bank loan and investment rose by 25% (HCMC 29.57% and Hà Nội 27%). Increase in the money supply was within the limit set by the National Assembly.

1. Use of indirect instruments for implementing the monetary policy

In 2003, the SBV pushed ahead with the use of indirect instruments for implementing the monetary policy: agreed interest applied to loans in the VND, liberation of interest on loans in foreign exchange, advertisement of base rate; refinancing rate; and discount rate, flexible required reserve ratio, etc. This policy affected positively changes in the interest and exchange rates, cash flow through banks and the gross investment in the economy.

From January to July 2003, the high demand for capital and keen competition between commercial banks made the interest rate rise quickly. The highest deposit rate offered by some commercial banks was 0.78% a month, or 9.36% a year in July. Most joint stock commercil banks offered a monthly rate of 0.74% compared with 0.72%-0.73% by state-owned banks. Rural joint stock banks and people's credit funds also offered a rate of 0.8% a month or higher ones. This is the highest level for the past four years. The lending rate also rose to 0.90% or 0.95% a month.

After warnings given by the SBV and efforts by the Banking Association, four state-owned commercial banks that control a total market share of 70% decided to lower the interest rate. The SBV, in August, also reduce the discount rate from 4.2% to 3.0% a year, refinancing rate from 6.0% to 5.0% a year, the required reserve ratio for deposits in foreign exchange from 5% to 4%, and cut the reserve ratio for deposit in the VND by 1%. The base rate stayed at 0.625% for the whole year. The SBV also adopted a flexible approach to the open market operations, swap service and daily information about the official rate by supplying VND9,000 billion in the first half of the year. These efforts helped reduce the interest rate. In October 2003, the interest rate on loans in the VND was considerably lower: the interest rate offered by state-owned commercial banks was .06% a month for 12-month deposits and the rate offered by private banks was somewhere between 0.70% and 0.72% a month for 24-month deposits. The lending rate also reduced slightly: Vietcombank offered the rate of

0.70-0.75% a month and Bank for Agriculture and Rural Development 1.0-1.05% a month.

The rate on VND loans, however, rose slightly by the end of the year when the demand for capital was on the increase, but it wasn't as high as the July rate that was considered as the highest for the past three years.

The interest rate on loans in foreign exchange stayed low for a long time. The rate for deposits with maturity from 12 to 24 months was 2% a year while the lending rate varied between 3.5% and 4.0% a year. The interest rate on deposits in foreign exchange by banking institutions with the central bank was also lowered according to changes on the market.

2. Intervention in the market for foreign exchange and happenings in the banking sector

The most noticeable happening in the market for foreign exchange in 2003 was the rise in the gold price and the dollar in the last quarter of the year.

On the free market, the price of SJC gold rose from VND6,420,000 a tael in January to some VND8,000,000 in early December – the highest rise ever seen since 1991. The prices of the dollar and other hard currencies also skyrocketed: the exchange rate of the VND to the dollar rose to 16,350 in December.

After interventions by the SBV, the gold price reduced to VND7,700,000 and the dollar VND15,850. They still rose slightly in late December but it was expected. Thus, the price of gold on the free market increased by 23% in 2003, compared with the rise of 19.4% in 2002 and 5% in 2001. The price of the dollar rose by 6.1%, compared with 2.1% in 2002. The euro rose by 17% (from VND16,238 to the euro in January to VND19,107 in early December). The Japanese yen rose by 11.36%, to VND146.4. These rises in prices of hard currencies and gold made the market price of real estate rise by 25%, payment for imports rise by 6.6% in the dollar, 16.4% in the euro and 11.0% in the yen.

To deal with these sudden changes, the SBV quickly granted quotas to companies that imported gold. From January to November 2003, Vietnam imported 54 tons of gold and this figure is expected to amount to 60 or 62 tons for the whole year. Sudden increases in the gold price in December made the gold price on the domestic market nearly equal the price on the world market. In Dec. 3, 2003, the SBV promised to sell enough foreign exchange at the official rate to commercial banks and gold importing companies to help them import eight tons of gold.

Facing the fall of the dollar against the euro and yen, the SBV, for the first time, allowed commercial banks to sell options with a view to helping companies to prevent exchange risk.

The central bank also reduced the required sale of foreign exchange by companies to the central bank to 0%. This means that companies were allowed to sell the foreign exchange to commercial banks or send to their bank accounts at will. The SBV also allowed commercial banks to enjoy more autonomy in trading in the foreign exchange. These decisions made operation of the banking service more suitable to current conditions, produced positive effects on the exchange rate and met the demand for foreifgn exchange by exporters and importers.

On Oct. 9, 2003, the SBV Governor made the Decision 1216/2003/QĐ-NHNN proving regulations about operation of exchange offices. This Decision allows these offices to buy foreign exchange from, not sell it to, private persons, unless they are passport holders who are allowed to buy foreign exchange as permitted. Exchange offices must sell all foreign exchange they bought to banking institutions as required by regulations. The Decision also stipulates location of exchange offices, conditions and terms of getting license to open exchange offices, rights and duties of exchange offices, etc.

On Nov. 19, 2003, the SBV Governor issued the Decision 1437/2003/QĐ-NHNN providing regulations about purchasing, transferring and taking foreign exchange abroad by Vietnamese nationals. According to this decision, Vietnamese nationals can take foreign exchange abroad to various extents. For example, an immigrant could take away from Vietnam US$10,000 at most for a year; or 20% if the sum he/she takes exceeds US$50,000. The Decision also stipulates procedures, delegation of authority relating to this issue.

With measures to make necessary interventions and beef up the state control, the rise in the official exchange rate fell only by 1.8% in 2003, rather in comparison with falls in the past six years: the VND fell by 14.2% against the dollar in 1997; 9.6% in 1998: 1.1% in 1999; 3.4% in 2000; 3.8% in 2001; and 2.1% in 2002.

Table 1: Immigrant remittance and changes in the gold price

Year	Immigrant remittance (US$ mn.)	Changes in gold price (%)
1991	35.00	+88.7
1992	136.64	−31.3
1993	140.98	+7.4
1994	249.47	+8.0
1995	284.96	−3.0
1996	468.99	+2.5
1997	400.00	−6.6
1998	950.00	+0.7
1999	1,200.00	−0.2
2000	1,757.00	−1.7
2001	1,820.00	+5.0
2002	2,200.00	+19.4
2003 (est.)	2,600.00	+21.0
Total	12,243.00	

Source: SBV

The economic reform has encouraged the flow of immigrant remittance that rose steadily over years. This result originated from the effective exchange control conducted by the SBV, increases in the number of laborers working abroad as guest workers and simplified procedures for receiving money from overseas relatives.

As for the gold price, it always varies according to the price on the world market. It has change in a complicated manner for the past ten years. Rises and falls in the exchange rate also affect the market demand for gold. The following table shows increases in immigrant remittance and changes in the gold price.

There were two events that drew attention of the public in 2003: the run on the ACB (Asia Commercial Bank) in Oct. 14-16. 2003, and the issue of five notes of five deniminations on Dec. 17, 2003.

Rumor about arrest of the ACB director-general when tried to run away from Vietnam made a lot of customers go to the bank to withdraw their money before maturity dates on Oct. 14 and 15, 2003. On October 14 alone, 2,085 customers withdrew some VND700 billion, including US$16 nillion. The SBV Governor and a Vice-Chairperson of the HCMC People's Committee had to be present at the bank to assure and give advice to the public. Besides the effort made by mass media to deal with the rumor, the SBV quickly supplied funds to the ACB: VND500 billion in the first phase and 450 billion more in the second one. The Vietcombank and other commercial bank lend US$5.6 million in cash and 5.3 million more in accounts. The measures helped solve the crisis. All borrowings were repaid some days after.

On Nov. 27, 2003, the SBV informed that new notes and coins would be injectecd into circulation as from Dec.17, 2003. They were VND500,000 and 50,000 notes; and VND5,000; 1,000 and 200 coins. This decision had certain effect on the rises in the prices of gold and the dollar. After this decision, prices of gold and the dollar started to rise on Nov. 27, 2003 and skyrocketed on Dec. 3, 2003.

3. Restructuring the banking system

At its peak, the banking system included 52 joint stock commercial banks and finance companies. After some mergers and consolidations, there were 38 joint stock banks by the end of 2003. Similarly, the system of people credit funds, after being beefed up, reduced from 974 to 885 funds by the end of 2003.

In 2003, both banks and credit funds tries to beef up their financial strength; competitiveness; and banking facilities, reduce bad debts, increase their legal capital and expand their networks of branches.

After being refinanced by the SBV, the total legal capital of state-owned commercial banks increased by VND6,800 billion. As for joint stock commercial banks, their capital had been added as required by law. Some of them even increased their capital in order to improve their competitiveness and ensure the deposit ratio of 8% according to international practices. In HCMC, five joint stock commercial banks had the legal capital of over VND200 billion.

In addition, some joint stock commercial banks were undergone restructuring. On Feb. 12, 2003, the Joint Stock Commercial Bank Việt Á came into being from the merger between Saigon Joint Stock Finance Company (capitalized at VND70.6 billion) and Đà Nẵng Joint Stock Rural Bank (capitalized at VND6 billion). This bank planned to increase their capital to VND150 billion. The Quế Đô Joint Stock Commercial Bank, renamed as Saigon Joint Stock Commercial Bank, also made plan to increase its legal capital. The legal capital of the Sacombank increased from VND71 billion to 358 billion and it was expected to rise to VND500-550 billion in 2003. The Saigon Commercial Credit Joint Stock Bank planned to raise its capital to VND200 billion at the year's end.

All commercial banks were competing with one another in opening branches in new towns and industrial estates. In HCMC, commercial banks opened 14 branches of the first level, 41 branches of the second level, 29 transaction offices, six savings funds and one representative office in 2003.

4. Market for T-bills and open market operations

Up to early December 2003, the market for T-bills organized by the SBV and the Ministry of Finance achieved unexpected suscess. Up to its 48th auction held on Dec. 9, 2003, a total of VND15,151.1 billion worth of bills were awarded to bidders although the target planned at the beginning of the year was VND10,000 –12,000 billion. The auction of T-bills came up to the SBV's expectations with low interest rate and costs. If nothing unexpected happens, the SBV could sell some VND16,000 billion worth of bills in 2003.

From January to November, the SBV organized 97 trading sessions on the open market with VND14,428.15 billion awarded: 7,988.15 billion by futures buying and 11,340.0 billion by spot selling.

5. A prediction for 2004

In 2004, the money and foreign exchange market will experience complicated fluctuations affected by changes on the world market. However, main operations of the banking system will produce intended results as in 2003. The money supply, total negotiable instruments, total bank deposit and total loan will increase by 20%-24% compared with 2003. The SBV will push ahead with the use of indirect instruments for implementing the monetary policy. The exchange and interest rates will be stable as in 2003. Competitiveness of commercial banks will be improved after they are restructured. More modern techniques will be introduced to the banking system with a view to gaining high profits and supplying better services to customers. The monetary policy will be linked more effectively with other policies for higher growth rate. Banking services will be more familiar to the public and companies and the public image of the banking system will be enhanced.