

Enhancing the Open Market Operations

by Dr. TRẦN HUY HOÀNG

in order to help banking institutions get access to the market when necessary.

The interest rate on the open market was not much different from the market rate. In 2001, the interest rate varied between 4.9% and 5.3%. The SBV also supplied some VND5,500 billion to banks according to the policy to stimulate the market demand introduced by the Government.

In 2002, 85 trading sessions were held with total sales of VND9,145.53 billion, which helped commercial banks engage in bidding for T-bills. The awarded interest rate on the open market for sale was 4.9% a year and 4.7% for purchase, a bit lower than 2001 rates.

After three years of operation, the SBV has gradually beefed up its control over the market economy and the open market operations (OMO)

ited at times. And as a result, the money market enjoyed some stability.

- By engaging in the OMO, bank members could employ their sources of capital more effectively and flexibly in the market economy. The increasing sales on the OMO showed that it employed well disposable capital of banking institutions.

To reach the full potential of the OMO, we need many technical factors: quantities and quality of paper assets; qualification of bank members; trading mechanisms and techniques, coordination of instruments of the monetary policy, etc. From this viewpoint, we see that the OMO in Vietnam still contain some shortcomings.

2. Shortcomings

- Bank members didn't attend all trading sessions. In fact, each ses-



1. Open market operations in the past few years

In the past few years, the Open Market Committee always observed regulations and changes in the market when making decisions on purchase and sale paper assets. From July 2000 to December 2001, the SBV held 64 trading session with total sales of VND7,755.78 billion. Of these sessions, 24 ones put interest rate on auction; 40 ones put quantities on auction. Decisions on ways of trading were based on disposable capital of bank members.

In 2000, trading session was held every ten days. From 2001 on, sessions were held every week. In 2003 when the disposable capital of banks reduced remarkably, the SBV decided to hold two sessions per week

achieved the following results.

- OMO affected the disposable capital of banks, thereby orienting them towards targets set by the SBV.

- By supplying more money, OMO encouraged both production and spending according to the demand-stimulating policy.

- Legislature for OMO is suitable for conditions in Vietnam. Computers and softwares needed for OMO have been installed and started to produce good results, which made trading sessions smoother and safer.

- Organization and control of the OMO are always in accordance with changes in the disposable capital and interest rates.

The interest rate on the OMO was kept stable, which helped make the market rate stable accordingly even if the source of finance was lim-

ited only attracted from one to four members, most of them were state-owned commercial banks because they control most commodities. Thus, the proportion of members who frequented to trading sessions was very low. Keen competition at auctions also discouraged small-size banking institutions. That is why most joint stock commercial banks were absent from trading sessions. As for branches of foreign banks, they had no ability to take part in the OMO because their funds in the domestic currency were limited, which made the OMO less busy and competitive.

- Sources of commodities traded on the OMO were limited. Main commodities were T-bills and SBV bonds. In addition, they are all of short - term class, which limited

trading on the OMO. This is the biggest problem for the OMO now.

Although the SBV bonds have high liquidity but they are only issued as required by the monetary policy. In other word, they are more a shotgun instrument than a commodity.

T-bills are also of high liquidity and suitable for the OMO but the quantity was small with the result that the main commodity was the SBV bonds. The shortage of commodities has limited effects of the OMO a lot.

The process of making decisions on the interest rate offer and quantities to be traded was not flexible enough. Increases in the supply of capital from the OMO were lower than the supply of loans guaranteed by paper assets. The software used for auction was not centralized with the result that bank members found it hard to use and handle when something wrong happened.

Under current conditions, it is understandable to see poor velocity of the capital.

Another fact to consider is that the secondary market of the OMO is at a standstill while interbank markets are not perfect enough, which affected badly the OMO. The main cause of the situation is that many commercial banks didn't take part in bidding for T-bills because they had no idle money and didn't want to invest in T-bills with maturity of 364 days at most. In addition, joint stock commercial banks usually offer deposit rates higher than state-owned banks' ones, which forces them to look for more profitable investments and refrain from offering low inter-

est rates competing against state-owned banks in trading sessions. That is why most joint stock commercial banks limit themselves in traditional banking services: taking deposits and supplying loans. When they have no ability to invest in the primary market, they certainly never think of the secondary market where the interest rate is lower and prices of paper assets higher.

These analyses allow us to conclude that, besides some achievements, the OMO as an instrument for realizing the monetary policy in the past few years produced only limited effects on the money market. To enhance the performance of the OMO, we suggest the following measures.

3. Measure to enhance the OMO performance

a. Attracting more members to the OMO:

To attract more commercial banks, the banking authority must ensure them a level playing field. In fact, state-owned commercial banks can get funds according to instruction from the central government or SBV and they use it to buy paper assets and enjoy higher interest rates while private banks have no such privilege. This situation leads to negative discrimination and fails to stimulate the demand for credit.

In addition, it's necessary to disseminate information about the OMO to banking institutions and train officials in these operations.

The interest rate auctions must be made more flexible and suitable to the market rate. In fact, most trading sessions were less attractive be-

cause the interest rate of paper assets trade on the OMO was usually lower than the market rate. This also leads to unfair competition between state-owned and privately-run commercial banks.

b. Diversifying and increasing commodities:

Besides listed paper assets, the OMO had better allow trade in long-term securities in order to supply more commodities and link the open market with others, especially the stock exchange in allocating sources of capital.

The shortage of commodities is the biggest difficulties for both the OMO and stock exchange. The SBV could consider allowing the trade in company bonds in order to help industries secure more capital. Purchase of company bonds by the central bank, in fact, always produces positive effect on investment structure.

c. More trading patterns:

Holding regular trading session seems the best suitable to the OMO in which the SBV could buy or sell with time and quantity appropriate for the implementation of the monetary policy.

d. Conditional measures:

To ensure success for the above-mentioned measures, the banking authority should develop the interbank, money and stock markets because they serve as a basis for the development of the OMO. In the long run, the quality of bank members should be revised. Banking institutions must improve their competitiveness and ability to carry out operations in the money market. ■

