

On the Strategy to Develop Bank Soundness

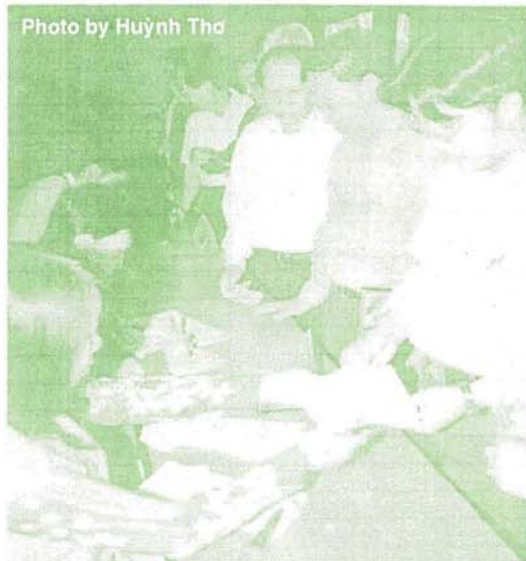
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Only a healthy banking system could compete successfully in the domestic and the world market as well. The notion of "healthy banking system" refers to its financial strength that, to a certain extent, could survive, tolerate and struggle against unfavorable effects from external environment.

In fact, we can see that the financial situation of Vietnamese banks is not firm enough. Most banks have small capital (their capital adequacy ratio is usually lower than the internationally agreed 8%) and poor management, fail to meet the market demand (because of shortage of fund, poor development of the capital market and increasing demand for capital). These factors affect badly their competitiveness, especially when the domestic is to be open to foreign players as required by the international integration. The poor performance and overload in local banks lead to a situation in which the local banks are vulnerable to external shocks. In addition, fundamental services of high priority, such as online handling, centralized customer information, etc., aren't given full attention. This means that Vietnam lacks a core banking system where basic banking services affect all services and serve as a basis for further development of this sector. This situation prevents the whole system from applying and developing modern services with the result that the system can only supply traditional ones.

The SBV, therefore, should take decisive measures to develop a firm

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banking system. At present when the Vietnamese banking system is some decades late in comparison with the world average, the SBV should carry out reengineering process to bridge the gap between Vietnam and regional countries.

Reengineering made its appearance in the 1990s and it is conceived as an effort to think through and redesign all

operations of banks with a view to improve essential objectives, such as overheads and operation processes. The reengineering is different from restructuring, reorganizing, automating, and ISO-based quality control. Their differences are shown in the following table.

The main contents of the reengineering could be considered as a revolution in banking services and it

aims at the following targets:

(1) Changing radically old processes and designing new ones:

Looking at processes in use in local banks, we saw that they were inadequate. For example, a customer usually works with two or three officials to complete a transaction, that is, there is no one-stop service in Vietnamese commercial banks. This situation may come from the fact that expertise and honesty of bank officials are not trustworthy. But is it a problem to local banks? If mistakes or corruption do take place, will they cost more money than expenditures on a large machinery and loss of time suffered by customers?

Another complex problem is the high overdue debts in most local commercial banks. According to the SBV, the overdue debt represents 11% of the bank borrowing while this percentage in foreign banks is much lower. This means that the business climate isn't the cause of the situation. Are methods of credit rating used by

	Content	Differences compared with reengineering
Restructuring	Rearranging the whole organization, replacing main positions, merging and dividing departments, allocating resources more reasonably	Restructuring doesn't aim at changing or redesigning existing processes
Reorganizing	Fundamental changes take place when the organization faces problems that affect directly its future development	Reorganizing is carried out when the organization faces problem while the reengineering aims at radical improvements when there is no threat
Automating	Replacing manual labor with automatic production lines based on IT	The automating doesn't aim at radical changes in processes
ISO-based quality control	Systematically control of processes in a company according to requirements posed by the ISO standards	The ISO-based quality control aims at systematizing existing processes without building new ones according to a new thinking way

banks or their managerial skills the real causes? To a certain extent, these factors have their own effects but the most important cause is the unreasonable lending process, because in the old process, state-owned banks had to ensure non-profit social targets and new techniques have not been applied fully. And as a result, the credit rating process failed to reflect the value of bank borrowing and part of overheads wasn't necessary because it wasn't spent on generating profit or providing customers with better services.

These analyses show that a new process is much needed. With a well-devised process, it will be hard for official to do credit rating at will, and they must pay more attention to their jobs and avoid mistakes. This will help banks to earn more profit, supply more loans and reduce the doubtful debt.

In Vietnam, when an importer wants to have a batch of imported goods guaranteed by banks, he (or she) makes contact with the bank's import department, which will discuss the customer's credit-worthiness with relevant departments before approving the borrowing plan. This process, however improved it is, is still time-consuming. This process aims at ensuring safety for the bank instead of satisfying customers' needs, and thus it doesn't encourage the bank to change its procedures with a view to reducing waste of time. Each department has its own procedures and doesn't share business and customer information with others. This practice prevents them from cooperating with one another. Moreover, many bank managers were promoted from positions of department heads, so they don't have a strategic and overall viewpoint and don't think of linking various departments in a unique pro-

cess. The reengineering method can help them overcome this problem because it aims at improving the business process, not officials or departments.

(2) Cost reduction and reasonable pricing:

One of urgent problem for the local banking system is to re-define its overheads and pricing method. Since the 1980s, the world banking system experienced sea changes. Results of continuous and unsystematic changes were multi-level management and duplication of functions. Bank products and their approaches to customers were unreasonably designed.

In addition, their processes, facilities and supporting systems developed since the 1930s - 1980s could only serve as shotgun solutions to changes in laws and competition. Structures of costs were worked out to add to the old ones instead of changing them.

Unlike manufacturing companies, processes in the banks are interdependent and overheads are usually divided among different groups of customers, products, and geographical areas. This means that the

overheads of banks couldn't be linked with a product bought by a customer at a locality. When failing to estimate exactly the overheads, banks usually make wrong pricing, and the price they set is usually lower than the value of services they supply because they don't take into account the value of convenient locations of banks and risks involved in bank borrowings.

Moreover, the ceiling interest rate in the past was set by law, which make banks didn't care how customers estimate banking services and transactions, and didn't pay full attention to their costs and profitability ratio.

When regulations about the ceiling interest rate were removed, banks started to price their services based on overheads and prices offered by rivals. Their pricing still fails to aim at meeting customers' needs and behavior. The result is that their method could ensure estimated profitability ratio but it may not be suitable to market interest rate. When expenditures on input rise, the banks should raise the interest rate in

order to ensure their profit but high rate may not be accepted by the market. The final result is that the banks become less competitive. To deal with this problem, the banks should take customers' estimate of their product quality into account when pricing their services.

(3) A new banking system:

New processes of controlling overheads and pricing their services will create a new banking system with better competitiveness and strength that allow banks to deal with unfavorable effects from outside.

Competition means supplying better services with more added values instead of waging a price war against rivals. To achieve this aim, the banks can develop their comparative advantages with a view to reorganizing their business processes. However, these advantages are not long lasting because the rivals could do the same. In my opinion, only reengineering could create a banking system with refined culture that aims at satisfying customers' needs and requirements. ■



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