

## 4. DIVERSIFICATION OF BANKING COMPETITION AND COOPERATION

Banking activities is a business of Vietnamese economy which is shifting to the market economy with the State management and along the socialist line, in short a socialist-oriented market economy. One of basic features of the market economy is the fair competition and voluntary cooperation, banking activities thus cannot be beyond that requirement.

The Party Central Committee's plan of socio-economic development in the 2001-2005 period points out: "To develop the capital and monetary markets with diversified and appropriate forms including banking system, non-banking institutions, insurance firms, funds of investment and investment guarantee...with the aim to attract capital sources and expand capital and credit sources. To reform the commercial bank networks, separate policy banks from state-owned commercial banks and put state commercial banks in the competition environment. To modernize and innovate banking technologies, speed up the application of in-

untariness, equality and mutual benefit for stable and firm development. As a result, the environment and conditions for strong competition and cooperation to survive need be created so that banking activities continue to play an important role as an engine, and a breakthrough for socio-economic development in line with the national strategy.

However, Vietnam is now still in the period of transition into the market economy and even in the first decade of the 21st century, banking competition and cooperation requires suitable steps in accordance with general changes in the economy and the central bank as well as changes in instruments of monetary policies from direct to indirect ones.

To meet requirements, enhance advantages and restrict negative effects of competition and cooperation, a tight, transparent and liberal legal environment should be established. In addition, the relevant authorities must control unhealthy competition and cooperation, protect consumers, encourage the development of all credit insti-

risk settlement between different forms of banks. It should also separate policy activities from business of each state-owned commercial bank.

Vietnam has established and brought into operation the HCMC-based Securities Trading Center. The Vietnamese securities market cannot certainly be fully fledged in the next years as those in the world and regional economies. As a result, banking competition and cooperation still play an important role in optimal mobilization of investment capital for the economy's demands. At the same time, the securities market requires robust growth.

The diversification of banking competition and cooperation also depends on the economy's demands. These needs are based on the level of socio-economic development. Therefore, bankers cannot hastily provide too many high level banking services beyond customers' requirements.

Due to its history of establishment and development, the country's commercial banking system cannot attain the same level, competence, scale,

# REQUIREMENTS AND CHALLENGES OF BANKING COMPETITION AND COOPERATION IN VIETNAM IN THE TIME TO COME

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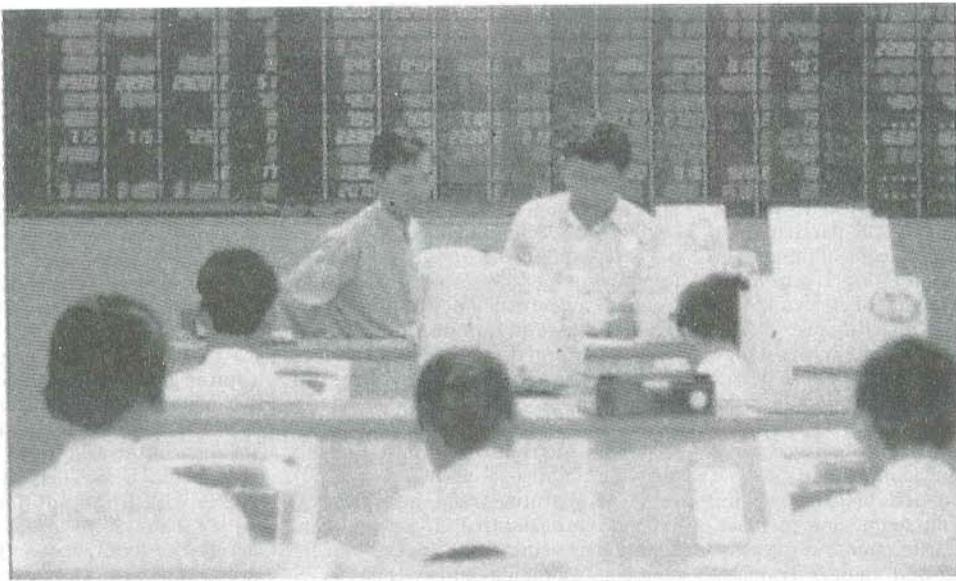
formation technology and try to improve the banking and financial systems to the regional average level".

The driving forces of competition are to tap advantages, fully use potentials, overcome shortcomings; promote positive aspects and eliminate inappropriate ones, boost development as well as cooperation on the basis of vol-

tutions and secure sustainable development of the banking system.

The goal of competition is to expand business for profits, but banking activities in the economy, which has a lot of risks due to subjective and objective factors in the economic shift, must fulfill the national targets. Therefore, the State should have equal policies of

and technologies as foreign banks' branches overnight. As a result, the Government cannot yet abolish relevant regulations to give equal treatment to all banks. Nevertheless, it cannot rely on this reason to delay commitments to freeing up banking activities in agreements signed by Vietnam with other countries.



## **II. THE INEVITABILITY OF THE EXECUTION OF THE TRADE LAW, FOREIGN INVESTMENT LAW, LAW ON THE STATE BANK AND LAW ON CREDIT INSTITUTIONS**

The Law on Credit Institutions, effective from October 1, 1998 has an article saying about banking competition and cooperation, Article 16, ruling: "Banking institutions are allowed to compete and cooperate legally. They are strictly banned to compete illegally, causing damage to the implementation of national monetary policies and the system of credit institutions and legitimate benefits of parties". This article also states: "Illegal competition includes illegal sale promotion; untrue information causing losses to other credit institutions and clients; speculation to manipulate the markets of money, gold, foreign currency and other illegal competition".

The Law on Credit Institutions also has regulations on the rights of banking operation, business autonomy; protection of depositors' benefits; time of transaction and responsibilities for illegally-derived money; splitting, merging, consolidation, acquisition, disbandment, connection, etc.

As a result, the Vietnam's legislation has recognized and encouraged legal banking cooperation and competition.

The branches of foreign banks and joint venture banks are affected not only by the Law on Credit Institutions but also by the Foreign Investment Law. Similarly, local commercial banks are affected by the Law on Credit Institutions and the Corporate Law. At the same time, the Trade Law has been promulgated and executed as well as relevant laws. In these laws, the State has built increasingly suffi-

cient, transparent, liberal legal framework in accordance with international common practice and the market economy. It allows to attract foreign investment, and boost the development of multisector economy in the legal competition environment. Therefore, credit institutions are also businesses trading in currency and credit and providing banking services. They are required to compete and cooperate more effectively in the competition situation of production, business and service.

## **III. REGIONAL AND INTERNATIONAL INTEGRATION**

The integration into regional and international banking activities lies in the process of general integration of an economy. That is the market access of monetary activities, bank credit and financial services to the world. Its detailed contents include the liberalization of banking activities of a country, removal of administrative prohibitions and restrictions against foreign banking activities. The legal environment for banking activities must be in accordance with international practice. In the meanwhile, the local banks' level must be raised to the region and world's standard.

In the trend of fast internationalization and globalization of economic activities, commerce, investment, service... if Vietnam wishes to avoid the danger of lagging behind, it has to integrate its economy into the regional and international community. The integration process also allows the country to attract fast foreign investment, increase capital for investment, enhance export of commodities, labor and services...and accelerate economic growth rate. The integration has good and bad effects. In addition to the aforesaid advantages, it also helps beef

up economic restructuring and eliminate shortcomings and backwardness. However, it poses great challenges which Vietnam need pay attention to, actively avoid and has appropriate roadmaps and steps.

The requirement for international integration in banking activities is originated from commitments in agreements signed by Vietnam with other countries or pledges which Vietnam has to implement when joining international organizations.

The U.S.-Vietnam trade pact has been signed on July 13, 2000 in Washington. Accordingly, in the banking field, Vietnam has to remove restrictions on local currency transactions of foreign banks by 2008. Within the next 10 years, the country has to eliminate all prohibitions against foreign banks' activities.

### **1. Main requirements of the opening and international integration in the banking area following the World Trade Organization's GATT.**

Vietnam has pledged and been on the way to joining WTO. The principal contents concerning the banking area in the negotiation process are being carried out as follows:

- In the banking sector where market-access commitments are undertaken, the measures which a member shall not maintain or adopt either on the basis of a regional subdivision or on the basis of its entire territory, unless otherwise in the specific commitments, are defined as:

+ Limitations on the number of banking service suppliers whether in the form of numerical quotas, monopolies, exclusive service suppliers or the requirements of an economic needs test;

+ Limitations on the total value of

banking service transactions or assets in the form of numerical quotas, monopolies, exclusive service suppliers or the requirements of an economic needs test;

+ Measures which restrict or require specific types of legal entity or joint venture through which a service supplier may supply a service; and

+ Limitations on the participation of foreign capital in terms of maximum percentage limit on foreign shareholding or the total value of individual or aggregate foreign investment.

- Each member shall give to banking services or service suppliers of the other member treatment not less favorable than that with conditions, terms and restrictions agreed and specified in their commitments.

- Unless in case of safeguarding the balance of payment, one member shall not apply restrictions on international payment and money transfer against current services concerning its specific commitments;

- Each member shall allow service suppliers of the other member to launch new banking services in its territory;

- Each member shall allow service suppliers of the other member to get access to the clearing system managed by the State and to the methods of financing and refinancing in the common process of business;

- Each member shall allow service suppliers of the other member rights to establish and expand operations in its territory including the acquisition of current enterprises and commercial organizations;

- The members pledge that in certain cases, subsidies may distort trade services, they will carry on negotiations in order to set up multilateral

principles necessary to avoid bad effects of that distortion.

- Each member shall not give late replies when any other member requests for specific information about any jointly applied measure or an international agreement.

## 2. Requirements of the ASEAN Framework Agreement on Service signed on December 15, 1995 in Bangkok

- To enhance cooperation in services among member countries in order to improve the efficiency and competitiveness, diversify production capacity and supply and distribution of services of their service suppliers within and outside ASEAN;

- To eliminate substantially restrictions to trade in services among member countries; and

- To liberalize trade in services by expanding the depth and scope of liberalization beyond those undertaken by member countries under the GATS with the aim to realizing a free trade in services.

According to the SNA regulations, the activities concerning money, payment, and relevant banking and finance services is referred to the service sector, thus, banking activities must be in compliance with the AFTA's regulations.

The negotiation mechanism: Vietnam is carrying on negotiations in accordance with requirements of the WTO's General Agreement on Tariffs and Trade and the AFTA agreement. However, the urgent problem to Vietnam is the WTO's General Agreement on Trade in Service as a basis for negotiations on the AFTA agreement with the following requirements:

- Regarding the WTO's official members, their commitments must be higher than those in the WTO's General

Agreement on Tariffs and Trade.

- Regarding those countries which are not WTO members, their commitments must be not lower than those they have made to extra-ASEAN countries. As a result, banking activities must take this condition into account.

## 3. Advantages and challenges in the process of banking competition, cooperation and integration in Vietnam in the coming time.

### a. The system of state-run commercial banks and policy banks

#### + Advantages:

- They own a huge authorized capital granted by the State, totaling VND6,000 billion, equivalent to US\$425 million; including the Bank for Agriculture and Rural Development with above US\$170 million and other banks with US\$80 million each.

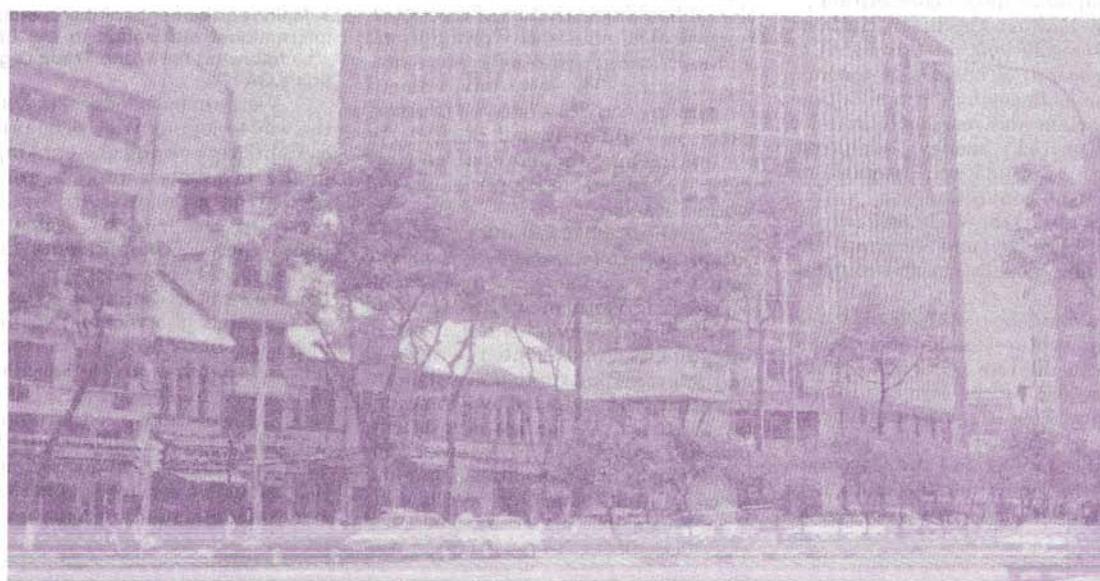
- They have a lot of branches across the country, even in residential areas and remote rural areas. Their staff is large and has good understandings about customers.

- They obtain a long business history, good experience; know the local traditional culture; and have good relations with local governments.

- They are gaining the biggest market share, from 72-78% of deposits and loans in the whole country's banking sector.

#### + Shortcomings:

- Their scale is too meager. Although their authorized capital is large, but the whole system's authorized capital is only equivalent to that of the system of foreign banks' branches and joint venture banks; at the same time far lower than the authorized capital of a bank in other regional countries which amounts to US\$2-3 billion on average, or four to seven times the capital of the whole system



of state-run commercial banks in Vietnam. Moreover, a large part of the state-run commercial bank's authorized capital lies in the assets producing no profits.

- The banking technologies are backward; the bank employees' level of management and professional skill remains far behind those in regional countries and the world. The bank's apparatus is clumsy, banking activities monotonous and traditional, mainly mobilizing capital and making loans; and banking services deficient.

- Their overdue debts are high, asset quality low, facilities obsolete and business efficiency low. The scope of activities remains limited to the country.

**b. The system of joint stock commercial banks and financial companies**

- Advantages:

It is a new model in accordance

and joint venture banks

- Advantages:

Their authorized and working capital are large, especially foreign currency capital, banking technologies modern, and personnel qualifications high. Their customers include transnational companies doing global business...

- Shortcomings: Their network is narrow, they face troubles in local language and cultural traditions and habits. Nevertheless, they can overcome these shortcomings by employing local workers and overseas Vietnamese, and applying modern technologies. But some banks are still slow to surpass these obstacles.

The following table will indicate the competitiveness of Vietnamese commercial banks in comparison with the banking system in the regional economies.

#### SOME INDICATORS OF SIZE AND PERFORMANCE OF VIETNAM'S BANKING SYSTEM IN COMPARISON WITH REGIONAL COUNTRIES

Nations	Capital mobilization/GDP		Credit/GDP		Lending/borrowing	
	Year 1992	Year 1998	Year 1992	Year 1998	Year 1992	Year 1998
Indonesia	68%	91%	74%	128%	1.22	1.06
South Korea	37%	54%	58%	78%	1.58	1.44
Singapore	83%	105%	61%	85%	0.74	0.89
Thailand	68%	91%	74%	128%	1.08	1.40
China	73%	117%	95%	125%	1.30	1.07
Vietnam	23%	34.0%	27.6%	33.0%	1.14	0.98

Source: State Bank of Vietnam

with the market mechanism and the international trends. It is energetic and flexible in business doing.

- Shortcomings:

Their size is too small; the average authorized capital of the whole system is equivalent to US\$160 million, only equal to a small bank in the region. Those banks are still immature and lack experience of operations. Their organization is not united, many joint stock commercial banks show manipulation of some members in the Management Board. The shortcomings and deficiencies of the management mechanism, legal environment of the market economy, and the model of private economy and joint stock organization...are obviously indicated in the shareholding credit institutions' poor operations in the past years. Their other weak points are the same as the system of state-run commercial banks, but to higher extent, especially their percentage of arrears is very high, and their managerial competence low.

**c. The system of foreign banks**

traction of foreign investment is improved and rises in the time to come.

**3. The competition between the branches of foreign banks**

Increased advantages and market shares are going to the American, European, Japanese, Singaporean and Hong Kong's banks. The banks of other Asian countries will be inferior. This trend is attributed to the two reasons: the competence of the parent bank and the structure of Vietnamese customers, foreign investors in Vietnam and Vietnam's export markets...

**4. The competition between foreign banks' branches and joint venture banks**

The domination belongs to foreign banks' branches, only some two joint venture banks continue to maintain their market shares.

**5. The competition between Vietnam's banks and the region and the world's banks**

In the trends of opening door and integration as well as the implementation of Vietnam's agreements with and commitments to other countries, Vietnam's banking sector and financial services have to open door and integrate. As a result, the banking activities and financial services which Vietnam has prohibited and restricted before will be freed up in accordance with the roadmap. The foreign banks will expand their operations in Vietnam and the country will encounter a heavy pressure when more and more foreign banks enter Vietnam. In the meanwhile, Vietnam's banks are pressed to seek the way to head for regional and international markets.

**6. The competition between banks and other institutions**

The situation also lies in the world's common trend. That is the competition of non-banking institutions which provide banking services.

In Vietnam these institutions include the Post Savings Service Company with the service of money transfer by post, the Overseas Vietnamese Remittance Service Company and the network of international credit card services.

To enhance the competitiveness and integration of the Vietnam banking system before the above requirements, the government is required to implement a series of general solutions such as perfecting the legal environment, increasing authorized capital, reducing bad debts, improving managerial competence and bank employees' qualifications, modernizing banking technologies and implementing the role of the Association of Bankers. Each solution needs specific measures which will be deeply analyzed in another article. ■