EXCHANGE RATE
A COMPLICATED PROBLEM

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In theory, exchange rate is the comparison of the value of one currency with that of another. For example, on August 12, 1994, in Tokyo foreign exchange market, the exchange rate was US$ to JPY 100, that means the price of US$ is 100 times higher than that of JPY. We can simply say that the exchange rate is the price of a currency expressed in terms of VNĐ.

Fox example, the prices of foreign currencies in HCMC market on August, 15,1994 were as follows:

US$	: VNĐ 10,985 - 10,995
GBP	: VNĐ 16,890 - 17,121
FRF	: VNĐ 2,058 - 2,093
DEM	: VNĐ 7,068 - 7,097

This was exchange rate applied to transferred foreign currency, (foreign currency deposited in a bank). There are also official rate, unofficial rate, closing rate, fixing rate, opening rate, multiple rate...

As for exporters, importers and other concerns trading in foreign currencies, the exchange rate is their main concern. The fluctuation of exchange rate will affect directly their turnover. When the exchange rate goes up (foreign currencies rise against VNĐ) the profits of exporters (or other businesses who sell goods or services for foreign currency) will rise, because when they exchange foreign currency for VNĐ, they will have a larger sum. Therefore, they always support high exchange rate, or the devaluation of VNĐ. On the contrary, this situation puts importers and those who want to buy foreign currency or repay debts by foreign currency at a disadvantage, because when the exchange rate goes up (the price of foreign currency rises) they have to exchange a lot of VNĐ for an unit of foreign currency, therefore they don't like the devaluation of VNĐ.

Thus, there emerged many opinions about the rate of exchange VNĐ to foreign currency, or exchange to US$ to be precise. There are two prominent viewpoints. The first argued that the present exchange rate is unreasonable because Vietnam exports aren't encouraged while we have a great need for foreign currency, therefore the VNĐ should be devaluated to help exporters gain as much hard currency as posible.

The second maintained that the present exchange rate is reasonable. Each viewpoint has its own logical and practical bases but I am in support of the second viewpoint. Why don't I agree with the first? The following are my arguments:

- Promoting exportation doesn't only depend on the devaluation of VNĐ, but also on many other factors such as the quality of exported products, the goodwill of the exporters, the liking of foreign markets, the pricing and marketing mix of the exporters, our output, tax system... and many others. To raise the exchange rate (to VNĐ 13,000 or even 14,000 per US$) doesn't ensure a boundless increase in exports. Many nations have stabilized their exchange rate, or even raised their currencies against foreign ones, but their exports also are on the increase (such as Thailand, Japan...).

- The devaluation of VNĐ could make the importation of machinery and equipment, raw materials and new technology more difficult.

- When the price of foreign currency rises, it could make the price of gold go high, and we could face a fever of gold and US$ prices again. Such a situation will have many bad effects on the economy: price will rise, inflation rate will not be kept under control, the people will lose their trust in VNĐ, the stability of our monetary and economic system will disappear... We have to do our best to avoid such a crisis, our achievements in recent years will be lost.

Therefore, I'm inclined to support the second viewpoint: to maintain the adjustment to the exchange rate. Due to the policy on adjustment to the exchange rate, the inflation rate was kept low, our monetary system became stable, the domestic investment increased and helped accelerate the economic growth rate (7.5% per year on average). However, in order to make this policy more effective, the Central State Bank should pay attention to the followings:

- To stabilize the monetary system doesn't mean to keep the exchange rate at a standstill, but to adjust it to the inflation rate of VNĐ and other currency as well.

For example, the price of US$ in early 1994 was 10,840 VNĐ, the inflation rate of US$ was 2.8% per year, and that of VNĐ was 9% per year, then the exchange rate between these two currencies in late 1994 (according to the theory of purchasing power parity put forward by Ricardo and Cassel) can be calculated as:

$$\text{Exchange rate (A/B) at Tc} = \text{Exchange rate (A/B) at To} \times \left(\frac{1 + \%\,IB}{1 + \%\,IA}\right)$$

Where A: US$
B: VNĐ
IA: Inflation rate of US$
IB: Inflation rate of VNĐ
Tc: Closing time
To: Opening time

$$\text{Exchange rate (US\$/VNĐ) by late 1994} = 10{,}840 \times \left(\frac{1 + 0.09}{1 + 0.028}\right) = 11{,}494$$

Thus, if we don't take other factors into consideration but inflation rate, the reasonable exchange rate between two currencies by late 1994 will be VNĐ 11,494 to US$.

- To pay attention to our balance of payments: From now on, the inflow of foreign currency will increase because we will receive a lot of foreign aid, loans from international financial institutions (IMF, WB, ADB...) and foreign governments, foreign investment, along with the source of foreign currency from Vietnam expatriates and tourists. Therefore our balance of payments will be favorable and the supply of foreign currency will increase. Thus, the exchange rate may fall below 11,494 per US$.

- Other factors, such as marco-economic index, monetary-financial policies, the difference between interest rates paid by foreign currencies and that paid by VNĐ... should be also taken into account.

Considering all above-mentioned factors, we could forecast that the exchange rate will be around VNĐ 11,200 to US$. But, the exchang rate should be continuously adjusted to the fluctuation of exchange rate in international markets, because the international exchange rate is every sensible of political, socio-economic events, of wars, acts of God, economic index, and even psychological problems♣

Recently, many economic magazines carried articles discussing the exchange rate in Vietnam economy. Although each articles mentioned an aspect of the problem or two, but in general, there were two opinions.

The first argued that the present exchange rate of VNĐ was too high in comparison with its real value, and so it's hard to promote exports and attract foreign investment. These authors petitioned the government to devaluate the VNĐ in order to encourage exports, limit imports and attract foreign investors.

The second opinion thought that the present price of the VNĐ in recent years was appropriate, stable and reasonable and if need be, it could be adjusted gradually, thereby avoiding economic, monetary and social unrest, especially psychological shock to the people and businesspersons as we have seen before the 1990s.

Thus, is the price of VNĐ low or high, reasonable or unreasonable, and if it needs adjustment, so how will we adjust it? To answer these questions isn't a simple matter, because it's difficult to quantify all of the factors affecting the exchange rate, or forecast their changes. These factors are the balance of payment in a given period, the annual inflation rate, structure of imports-exports, the difference between interest rates paid by foreign currency and by VNĐ, the policies on monetary system and trading activities, to name but a few.

We can easily agree that the exchange rate is one of the main regulator for foreign currency supply and demand, therefore it has strong effect on the production, trading, foreign trade of a nation. A low exchange rate can encourage imports (it makes imports cheaper for home buyers) and put exports at a disadvantage (it makes exports dearer for foreign buyers), therefore it discourages the capital inflow and makes foreign exchange reserve smaller. On the contrary, a high exchange rate (the price of the VNĐ is low as compared with foreign currency) will make imports dearer and exports cheaper, thus it will encourage exports.

There are usually two kinds of the exchange rate: basic exchange rate referring the relationship between home price floor and international price floor. It reflects the relationship between the price of exports and the price floor in export turnover, not in GDP of a country. The second is practical exchange rate used in foreign exchange trading in the market: this rate