



now, main commodities are still the US\$ and the VND because of trading customs of Vietnam's banks and companies.

The Vietnam foreign exchange market also has two main divisions, the spot market and the forward market where all deals are according to official rates fixed by the State Bank, however, in the past three years, most commodities were traded in the spot market. No trader makes forward dealings because there is a great difference between interest rates in foreign currencies and in VND so it's hard to fix an appropriate forward rate. At present, many commercial banks suggest developing the forward market.

At first, only 23 banks joined this market and then the member-

joint stock commercial banks, 20 branches of foreign banks, 4 joint venture banks and 2 finance companies.

A short time after its establishment, this market has operated well with its increasing membership. The amount of traded commodity has been on the increase: US\$934,150,243 in the period between October 1994 and December 1995, US\$2,325,869,938 in 1996 and US\$3,961,987,915 in the first seven months of 1997.

Looking back on the operation of the foreign exchange market in the past three years, we saw that at the beginning of 1995 when the capital inflow and export earnings increased, the source of supply in this market was abundant, many banks changed foreign exchange for do-

OPERATION OF INTER-BANK FOREIGN EXCHANGE MARKET ACHIEVEMENTS AND SHORTCOMINGS

by Dr. NGUYỄN ĐẮC HƯNG

The inter-bank foreign exchange market organized and run by the State Bank came into operation on Oct.15, 1994. It provided an organized market for foreign exchange and a basis for forming an official foreign exchange market in Vietnam. Through this market, the State Bank, acting as an end-buyer and seller will use its foreign exchange stabilization fund to intervene into the market with a view to carrying out the state policy on exchange rate. Commercial banks with license to trade in foreign exchange and database connected to the central computer at the State Bank could enter into the market. The State Bank is a member as well as the organizer and controller of the market.

Commodities exchanged in the market include six foreign currencies (the US dollar, DM, GBP, FrF, HKD, and JPY) and the VND. Up to



ship increased to 58, including 4 state-owned commercial banks, 28

mestic currency needed for their business, especially in months be-

fore the Tết Festival. The State Bank had to buy in the US dollar at that time in order to stabilize the exchange rate, keep it from falling under VNĐ11,000 to the US dollar, and prevent speculation in both the US dollar and VN đồng.

The exchange rate in 1995 was rather stable and fixed at VNĐ11,025 to the US dollar plus or minus 0.5%. Although this allowed fluctuation was small, but the long-lasting stability of the official rate and normal operation of the inter-bank market enabled banks with an abundance of foreign exchange to change it for domestic currency or buy in foreign exchange if need be.



In the first eight months of 1996, the market was lively, but from September to December 1996, there were abnormal fluctuations, foreign currencies became scarcer. The demand for foreign currency rose sharply. Many banks failed to buy in foreign exchange although they had raised the exchange rate to its ceiling (from $\pm 0.5\%$ to $\pm 1.0\%$ at the year's end). The reason was that many companies needed foreign exchange to repay debts or L/Cs. In addition, rumor had it that the VN đồng would be depreciated, therefore many banks wanted to keep as much foreign exchange in reserve as possible. Certain companies with stable and regular income in foreign exchange also refused to sell. Many commercial banks reported that their customers took deposits out of banks to buy foreign exchange and caused bad effects on banks' solvency and the VN đồng's exchange rate. In this situation, the State

Bank had to intervene to reduce the demand for foreign exchange by selling large sums of foreign exchange to banks that needed it to repay foreign sellers of raw materials, insecticide and fertilizer, thereby reducing the demand for foreign exchange and normalizing the operation of the market.

In the first eight of months 1997, the market resumed its normal activities, especially after the State Bank made regulations on deposits on L/Cs opened by importers of consumer goods and allowed commercial banks to have larger margins. In the market, from US\$1 to 6 million was traded and from 15 to

30 million changed hands between banks and their customers. However, since last September, the demand for foreign exchange has increased. Many banks couldn't buy foreign exchange although they had raised the exchange rate to its ceiling. The State Bank met with a lot of difficulty in supplying foreign exchange to commercial banks.

Establishing an organized foreign exchange market is a right policy. The operation of this market has helped the State Bank keep a weather eye on supply of and demand for foreign exchange and find out the real exchange rates between the VND and foreign currencies in recent years. Most members of the market have observed regulations and directions of the State Bank and helped to make the operation of the market more regular. In the past three years, only two violations of regulations were recorded.

Acting as a member, an organ-

izer and an end-seller and buyer, the State Bank has played well its role in preserving the foreign exchange reserves and keeping the exchange rates at a reasonable level. It has also controlled the foreign exchange market and made adjustments on time to the exchange rate policy.

Commercial banks, by taking part in this market, could improve their knowledge and skill at trading in foreign exchange, so this market could be considered as a place for them to prepare themselves to enter into foreign financial markets.

Looking back on the operation of the foreign exchange market, however, we discovered certain defects:

-Some commercial banks failed to observe properly regulations set for the market; they didn't send statement of foreign exchange receipts and payments to the State Bank as required and they only sent it when they want to buy foreign exchange.

-According to regulations, head offices of banks and non-banking institutions are only allowed to buy or sell foreign exchange in the foreign exchange market, but some branches did trading or made deal with other branches outside the market, therefore in some cases a branch wanted to make a purchase while its head office a sale and this situation made it difficult for the State Bank to control the market.

-Members of the market are allowed to make transaction through fax, telex or computer network and the State Bank has recently required members to join the VDS (Vietnam Dealing System) and only 16 out of 58 members did it. This fact has made it difficult for the State Bank to supervise the trading on the foreign exchange market.

-To control the exchange rate, the State Bank, after studying changes in supply of and demand for foreign exchange, usually publicize adjustments made to the exchange rates through mass media everyday. Some people think that this practice isn't flexible enough but some others agree with the State Bank. However, we think that in the future the State Bank had better review its way of controlling exchange rates and make it appropriate to changes in the market. Moreover, as the end-buyer and seller, the State Bank has to see to it that it will be able to satisfy what both buyers and sellers demand ■