

The policy on exchange rate is considered as one of monetary policies which aim at stabilizing the value of the domestic currency, controlling the inflation rate, and keeping the growth rate stable. The policy on exchange rate also has its own goals:

+ Stabilizing the exchange rates based on the supply-demand relationship in order to promote export, control import, improve the balance of payments and increase the foreign exchange reserves.

+ Enhancing the external value of the domestic currency and making it convertible and a real legal tender.

Those goals require the policy on exchange rate to be based on the following ideas:

- The policy on exchange rate should control the exchange rates according to the market mechanism:



PROBLEMS WITH THE CONTROL OF EXCHANGE RATE AT THE PRESENT PERIOD

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If the foreign exchange is considered as a special commodity, the exchange rate will have to change according to the price system and the control over the exchange rate should depend on the supply-demand relationship and other factors affecting it. According to the law of prices the exchange rate could be separated from the value of currencies, but when it is separated too far and too long, it will cause effects on prices on other markets (commodity, foreign exchange, capi-

tal markets, etc.) In other words, wide fluctuations in the exchange rate certainly cause damage to the economy. That is why the stability is the most important goal for the policy on exchange rate.

- The policy on exchange rate should promote export in order to improve the balance of payments:

The exchange rate is central to the functioning of the open market mechanism and affects greatly the country's international competitiveness. A trade deficit caused by the

poorly fixed exchange rate will lead to a turmoil in the monetary system and falls in the foreign exchange reserve. Such a situation could bring the economy to a financial crisis.

- The policy of exchange rate should be linked with the governmental management:

In the growing trend of globalization, the exchange rate should be kept well under control, even if it is left floating. The Government should know how to employ foreign resources to develop the economy, make timely adjustments to the exchange rate when necessary and keep it in agreement with interest rate, foreign exchange reserve, balance of payments, growth rate and budget deficit.

To reform the policy on exchange rate according to those ideas, in our opinion, the following measure should be taken:

+ The act of adopting the floating exchange rate system is suitable to the present economic reform. It allows the Government to work out an independent monetary policy which is appropriate to the market mechanism and favorable for the government management

+ Reforming the mechanism for controlling the exchange rate by liberalizing it step by step:

The gradual liberalization of the mechanism for controlling the exchange rate requires suitable steps. For the time being when the growth rate is unstable, the foreign exchange market isn't perfected, the stock market is just in the first stage of development, it's necessary to maintain the current exchange rate system. Official exchange rate and controlled small changes in exchange

rates are still effective instruments for regulating the exchange rate system.

However, the exchange rate system should be regulated more effectively. At present, the international finance market experiences many fluctuations and unofficial rate in Vietnam is on the increase. Facing such a situation, however, the State Bank of Vietnam (SBV) allowed a wider band on either side of the official rate which has been almost unchanged for a long time with the result that the difference between unofficial and official rates became wider. Although this adjustment is an effort to work out an exchange rate appropriate to the conditions of supply and demand in the market, the act of allowing a wider variation in the exchange rate makes the public feel uncertain about the policy on the exchange rate.

In my opinion, the SBV had better widen the range of variation step by step and change the official rate by degrees in order to avoid unnecessary fluctuations and regulate the unofficial rate. It's unreasonable for the SBV to allow a wide difference between the official rate and unofficial rate (or rate offered by commercial banks). This wide difference shows that the SBV failed to exert complete control over the exchange rate.

In the market economy, the Government should study and introduce a more flexible and effective exchange rate system at a right time. As for the control mechanism, the Government can allow a limited range of variation in the exchange rate in order to keep it under control, and publicize the daily official rate based on the average of buying and selling prices of foreign currencies on the interbank foreign exchange market. This practice will help to avoid the existence of too many rates in the market and make the official rate reflect the supply-demand relationship. When the difference between the official and unofficial rates becomes too wide, the Government can intervene by selling or buying the foreign exchange on the interbank market.

To control the above-mentioned exchange rate system, it's necessary to

perfect the following aspects:

+ Beefing up and developing the interbank foreign exchange market: As important part of the finance market, the interbank foreign exchange market should be allowed to operate continuously with no limit in terms of space and time. At the same time, there must be regulations that force banks and other financial intermediaries to help perfect the interbank foreign exchange market, maintain the balance between supply and demand forces and realize the policy on exchange rate as directed by the Government.

+ Beefing up and developing the interbank domestic currency market with all of its operations: This market will help the Government regulate effectively both foreign exchange and domestic currency markets.

+ Increasing the national foreign exchange reserve according to rises in import and export values and the amount of foreign exchange that exists in the economy: This task could be assigned to the SBV and even the Treasury is under the obligation to sell foreign exchange to the SBV and rebuy it when necessary.

+ Working out a reasonable structure of foreign exchange reserve based on a basket of hard currencies against which, instead of against the U.S. dollar only, the Vietnamese đồng could be measured: A diversified foreign exchange reserve will allow the Government to make the best use of international instruments of payment, balance foreign debts against flows of foreign exchange from foreign trade and direct in-

vestment, reduce exchange rate risk and dependence on the U.S. dollar.

+ Encouraging exporters and importers to diversify kinds of foreign currencies in use in order to improve the balance between supply of and demand for foreign exchange.

+ Estimating exactly major economic indicators (inflation rate, interest rate, balance of payments, foreign debt, etc.) in order to make appropriate adjustments to the exchange rate if necessary.

+ The SBV should gather information and keep a close watch on inflows and outflows, thereby estimating the supply of and demand for foreign exchange and helping with the controlling of exchange rate.

+ The SBV should control the amount of foreign debts, especially short-term ones and bank guarantee for deferred-payment loans owed by local companies.

+ A network of foreign exchange offices that covers all ports, airport, railway stations, border towns, and cities should be built.

Besides these measures, the SBV should make the domestic currency fulfil well its functions by:

Introducing other negotiable instruments with a view to reducing the demand for cash.

Encouraging the public to get accustomed to banking services.

Raising gradually the face value of the Vietnamese đồng: it's difficult to raise the value of a currency when its face value is too low. But it's unnecessary to revalorize the domestic currency as what was done in the past causing great damage to the economy. A solution to this problem is to put in circulation both old and new bank notes for some years.

Reducing the difference between lending rates charged on loans in foreign exchange and in domestic currency.

This difference could be reduced to such an extent that it still reflects the credit risk and future changes in the exchange rate. This measure will allow the central bank to prevent the exchange value of the domestic currency from falling by raising the interest rate and help adjust the exchange rate without causing damage to the foreign exchange reserve.

