

ON BUSINESS PERFORMANCE OF COMMERCIAL BANKS IN HCMC

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1. Overdue debt in HCMC commercial banks

a. Increased overdue debt: After the Decision 445 issued on Jan. 5, 1998 by the SBV Governor, the ratio of overdue debt showed signs of decrease but it was still higher than the acceptable level.

2. Causes

a. External causes:
- Poor business climate: Natural disasters in Vietnam and external effects after the Sep. 11 catastrophe caused a lot of difficulties for local companies, including banks and export ones. Other factors originating from the business climate, such as

- Poor banking inspection: Inspections were carried out regularly but carelessly. Many violations haven't been discovered for years. The banking authorities failed to inspect systematically and methodically and work out plans to prevent possible violations. Many inspectors didn't understand their functions and duties as suppliers of information and advisors for commercial banks.

b. Internal causes:

- Careless application of banking regulations: The report on banking activity in HCMC says that "Many commercial banks failed to inspect the use of bank loans and even control assets mortgaged to them. Many banks, eager to expand their business, went against banking regulations thereby causing serious consequences when they didn't observe regulations on exchange control, foreign loans, periodical reporting, bank guarantee service, etc. In certain banks, overheads and payroll kept increasing in spite of poor business performance." We saw here that certain banking officials lacked the sense of responsibility and the inspections were carried out nominally. If strong measures had been taken after discovery of violations, consequences wouldn't have been so serious.

- Supply of credit beyond the control: Extending more credit is a need to commercial banks but the supply of credit should be kept under control. The above table shows that the supply of credit increased over years while the managerial skills of banking officials weren't improved. That is why they fail to estimate the feasibility of borrowing plans, classify borrowers or keep a close watch on the use of bank loans. This leads to poor loan quality.

- Poorly-controlled process of extending loans: This process includes many stages, from classifying borrowers, estimating borrowing plans, controlling the use of loans to handling overdue debts, and it wasn't carried out properly. Most banks only paid attention to assets mortgaged and ignored the feasibility of

Table 1: Overdue debts by classes of borrower in 1999 - 2000

Borrower	1999		2000		2000 compared with 1999	
	Overdue debt (VND bil.)	%	Overdue debt (VND bil.)	%	Overdue debt (VND bil.)	%
State company	370	43.3	809	14.9	+439	-28.4
Collective company	215	25.1	3,982	73.4	+3,767	+48.3
Private company	152	17.8	398	7.3	+246	-10.5
Joint venture	8	0.9	41	0.7	+33	-0.2
Others	109	12.9	192	3.6	+83	-9.3
Total overdue debt	854	5.3	5,422	20.0	+4,568	+14.7

Source: SBV reports

The table shows that the overdue debts by collective companies rose very quickly (48.3%) and these debts could become bad ones. Rises in the overdue debts by other borrowers are also alarming. The main reason for this situation is the fact that commercial banks guaranteed their customers' debts or opened deferred payment L/Cs for a handful of customers. They wouldn't have been in such a situation if ordinary precautions had been taken.

b. Increased bad debts: At present, bad debts in both state-owned and joint stock banks represent a big percentage of outstanding loan although their ways of doing business have been improved remarkably. This situation forces them to classify their customers more exactly. The doubtful debt accounts for 50.6% of the overdue debt in HCMC commercial banks, 20% in joint venture banks and 12.2% in branches of foreign banks. It seems that there is nothing to prevent doubtful debts from becoming the bad ones.

corruption, unfair competition, commercial frauds, etc. also made companies face financial difficulties and even went to the brink of ruin. That is why many companies failed to pay debts in time. Of course, there were also directors who tried to get away with bank loans.

- Economic policies: Although the legal infrastructure has been improved in recent years, many policies and regulations include defects, loopholes and contradictions. In addition, the policy to privatize certain state companies and reform the public sector made business plans of companies unstable causing certain risks. Inconsistent banking regulations and precautions caused a lot of difficulties for commercial banks while many necessary regulations are still lacking, such as those about contingency fund, deposit insurance fund, risk precaution center, independent auditing, etc. creating loopholes that could be exploited harmfully.



business plans presented by customers. As a result, banks kept too many mortgaged assets but couldn't retrieve bank loans and they suffered increasing overdue debt. In fact, from 70% to 80% of the overdue debt to banks were in mortgaged assets while banks couldn't sell them to retrieve loans.

- Incompetent banking officials: This is the main cause of credit risk. A wrong estimate by the loan officer could turn a loan into doubtful debt right after the loan is extended. Besides offering loans, the loan officer should give advice on the business plan presented by the customer. This is one of ways of ensuring the loan quality. Regrettably, most loan officers lack this ability. In addition, certain officers were ready to approve the borrowing plans for some bribe.

- Poor internal audit and inspection: As we know, the internal audit is the best measure to avoid risks. However, most banks have failed to pay full attention to this instrument. That is why they took years to discover violations by loan officers and more years to handle and repair damage.

3. Measures to ensure loan quality in HCMC banks

a. Beefing up banking operation:
 - Banks should ensure the process of extending loans: All stages of the process should be carried out properly for the benefit of both banks and customers. At present, the classification of companies in HCMC isn't done regularly. Banks could meet with difficulties in doing so because company's financial statement is usually shrouded in secrecy or inexact and the number of companies increased quickly after the Companies



Law came into effect. In addition, loan officers are usually assigned a large amount of credit or shifted from branch to branch, so they couldn't keep a close watch on company customers.

Loan officers should have rights to write down their opinions on the lending dossier when their opinion is different from those of their superiors. This measure could enhance the sense of responsibility and prevent corruption among banking officials.

- Diversification of loans: Bank loans should be distributed among classes of customers and industries because of their different degrees of risks. In addition, banks could offer a wider range of loans secured by all kinds of assets, including negotiable instruments.

- Secured loan only: Although company's business performance could serve as a basis for decision to extend loans, collateral is usually demanded because companies could go

bankrupt or suffer losses caused by bad business climate. Bank managers had better have mortgaged assets evaluated by experts with a view to facilitating the process of collecting debts.

- Better internal audit: Banks could have auditing companies control their investments with a view to distributing risks. To beef up the internal audit, banks could form departments specialized analyzing and estimating business plans and use of bank loans in order to discover dangers in time.

- Other precautions: Bank could take additional precautions, such as standardizing banking officials, adopting incentive schemes, assigning right officers to right jobs and launching advertising campaigns,

etc.

b. Role of the central bank:

- Realizing regulations on deposit insurance.

- Forming the auditing company specialized in banking activities.

- Dealing with complaints about mortgage and guarantee.

- Establishing a committee on loan supply.

c. Help from the Government:

The Government can allow state commercial banks to supply fiduciary loans to districts damaged by natural disasters. The use of fund for this program should be well under control with a view to saving banks from unnecessary losses. Regulations on the handling of mortgaged assets should be made as soon as possible to help banks retrieve debts before value of these assets falls. In short, the Government should develop the statutory framework favorable for the banking system and other industries as well. ■