RADICAL REFORM OF BANKING SYSTEM

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Banking activities depend on the macro-economic policy. The Government thus has to reform its macro-economic policy in order to strengthen the banking system.

I. SPECIFYING THE MACRO-ECONOMIC POLICY BASED ON INTERNAL FORCES

The Party and Government's macro-economic policy is fast development, industrialization and modernization based on national resources. However, the policy has not been integrated. While some ministries and agencies encourage production of plastic, glass, sugar, others allow the import of these items or cannot stop illegal imports. Therefore, there should be a consensus on the implementation of the macro-economic policy based on national resources.

1. Giving priority to the domestic manufacture of machinery and tools: The reason is the home-made machine costs only one-fifth or one-third of imported one. The investment will save foreign currency and avoid troubles in gaining foreign currency. Due to cheap prices, with the same amount of investment, the efficiency will be 3-5 times that of imported equipment. At the same time, the number of machinery will increase fast and the total investment capital accounts for 30-40% of GDP.

It is argued that local machine quality is lower than foreign one. Nevertheless, we will learn precious lessons when failing to manufacture good machinery and the work will be better. If investing in foreign machinery, we will never make our own ones.

The evidence shows we have spent US$2 billion annually but imported only machinery which were manufactured tens of years ago and refurbished.

All industrialized countries manufacture their own machinery. Developed countries have boosted their manufacturing sector. The construction of plants manufacturing essential machinery is a basic condition for political, military, economic and financial sovereignty.

2. Supervising all sources of foreign currency and prioritizing their use for buying those machinery that cannot yet been manufactured domestically: In 1998 and 1999, of the total import turnover of US$11.5-11.6 billion, 2.1-2.0 billion were used for buying machinery and equipment. This volume is too low. Vietnam is able to boost this figure to 3,4,5 and 6 billion for investment. To reach this target, the Government should supervise all sources of foreign currency and focus them on the import of machinery and equipment which cannot be manufactured locally.

By intensifying the manufacturing sector and importing machinery and equipment, we may increase the total investment capital to some 30-35% of GDP for fast economic growth.

3. Concentrating investment on state-of-the-art industries which produce highest value added: The Government is required to invest in production of electronic appliances, computers, auto and motorcycle spare parts and tires, and such high-quality items as air-conditioner, electric cooker...which are being imported in a large volume and at high prices. One dollar to import materials will generate 4 to 10 dollars of value added.

Instead of exporting raw minerals, we should process them into high- or medium-quality goods.

Moreover, we may substitute foreign high-grade goods for local ones.

4. Annually investigating plants' equipment and products, and requesting them to plan technological innovation and production of new items: The enterprises will make a plan for equipment renovation in the following years and production of new items. At the same time, they will report their equity capital, and requirements for new loans and foreign currency to import new machinery, equipment and materials for production. Based on their requirements, the Ministry of Planning and Investment will coordinate with:

- the Ministry of Industry to manufacture machinery needed for licensed investment projects, those which cannot be made domestically will be imported,
- the banks to offer loans and foreign currency to enterprises for their equipment innovation, and
- the Ministry of Trade to plan the amount of imported machinery and materials based on the local capacity of manufacturing machinery. The Customs Office will try to stop illegal imports. Provincial authorities will not allow sales of illegally-imported goods.

In brief, the macro-economic policy is import substitution by manufacturing machinery and equipment domestically, importing those which cannot be made in Vietnam, stopping the waste in using foreign currency for imports and finally banning sales of illegally-imported goods. Only by these integrated measures, local companies can boost their production and business, earn profits and repay their bank debts.

Furthermore, the investment projects should aim at full labor employment and full utilization of machinery capacity and national resources for development.

II. STRENGTHENING THE BANKING SYSTEM

This policy after proposed by scientists and then approved by the Party and the Government will become the Vietnamese industrialization and modernization line. As mentioned above, banks are responsible for implementing the Party and the Government's policies. When the industrialization policy is distinct and consistent, banks will focus all their powers and tools on fulfilling the annual economic plan, so they will be solidified.

1. Concentrating all foreign currency on banks, using as much as possible foreign currency to import foreign machinery and hiring foreign experts to build projects beyond the national ability:

The macro-economic policy increases investments at most by importing foreign machinery. To implement this policy, banks are obliged to grant foreign currency to national corporations which realize the investment projects and import essential machinery.

The uncontrolled sources of foreign currency such as overseas remittances, tourist spending, illegal border trade, and illegal investment which are estimated at US$3-5 billion/year must be attracted to the banks to import foreign machinery for economic development.

In the market economy, the best way to attract floating foreign currency is to buy them for prices higher than illegal importers. The banks will have no losses when doing so because they will sell high-quality consumer goods to importers at the exchange rate as high as the buying price of floating foreign currency. At the same time, the banks should ask policemen to arrest illegal foreign exchange traders. The central bank should determine two exchange rates, an official one for importing machinery and materials as well as common export activities, another for purchasing floating foreign money.

Most of developed countries has to control foreign exchange because it is blood of the national economy. The major deficiency of banks is not to mobilize foreign currency and not to focus it on importing machinery.

The foreign currency registers some US$15-17 billion annually (US$11-12 billion from exports, 2-3 billion from tourist spending, and 2-4 billion from foreign investment). If using 5-7 billion for building major plants, we will achieve much larger investments.

2. Earmarking credit for investments in high-grade manufacturing projects with highest value added:

The central bank has right to print and supply more money. When the economy grows, the volume of goods increases, therefore the volume of bank notes rises accordingly. In recent years, the private enterprises have no adequate capital to build plants worth US$1 billion up to produce petroleum, vehicle components, motorcycles and computers. It is obvious that only the Government is able to carry out these projects. The demand stimulus programs are not effective because private companies do not take loans from banks for investments in the recession stage. As a result, Keynes suggested that the Government implemented mammoth investment projects. The establishment of state enterprises is very easy with the Prime Minister's decision and afterwards the banks or the Ministry of Finance grant capital to the company. The PM assigns high qualified officials to the management board. If this plan is approved, an interbank agency will be set up to focus redundant capital on state corporations to build oil refineries, computer plants, etc. As such, the banks' capital gluts will be settled and a series of large plants will be built every year.

The banking system reform program as mentioned above is very simple but effective. The banks are only required to offer US$5-7 billion to major projects which will be realized at a fast speed. The Vietnam economy with investments accounting for 30-35% of GDP will see a rapid growth because it reaches the necessary investment scale.

III. INCENTIVES FOR MAMMOTH INVESTMENTS

1. Forex preference for producers and exporters instead of preference for importers

When the money supply increases to fund mammoth investments, the Government should apply soft exchange rate to encourage export and local goods protection. Meanwhile, the exchange rate should be higher so that foreign tourists and nationals are willing to sell foreign currency to banks. As such, the Government should apply the multi-rate system including higher exchange rate for buying foreign currency from tourists and Vietnamese, this rate will be used for importing luxuries and lower rate for importing machinery and materials and buying foreign currency earned from export.

2. Reduction of interest rate for mammoth investments:

The saving deposits should be reduced to stimulate demand, banks should accept current deposit accounts with low interest rate. To implement this, banks has to supply diverse services as foreign banks instead of receiving deposits with high interest rates and thus giving loans with higher rates.

Vietnam's bank interest rates are much higher than those of foreign counterparts, for example, Japanese banks apply an interest rate of 2% per year as compared with nearly 1% per month in Vietnam. This forces enterprises to pay interests higher than their payroll and their profits are mainly used for bank interest payment. One of reasons for low purchasing power is that the people put their idle money into banks for more income. In addition, the prices of local goods are usually more expensive than those of imported ones because Vietnam's enterprises are subject to too high interest rates. When cutting deposit and loan interest rates, the banks will stimulate demand effectively because the people will use their money for investment or consumption. The enterprises' interest burden will be removed. The banks will have enough capital for lending because if necessary they will re-collateralize the enterprises' assets at the central bank. Obviously, the central bank should have a liberal policy for re-collateralizing so that the commercial banks are able to reduce deposit and loan interest rates.

3. Preferential loans for investments: This is a proof of a good monetary policy. In Minh Phụng and Epco cases, loans were offered to import consumer goods, invest in real estate, and repay due debts for taking new loans and there were almost no lending programs for plant construction.

To encourage investors to build plants, the banks should apply soft interest rates for new plant construction. Loans for importing consumer goods and buying land will be subject to high interest rates.

In brief, the banking system reform may be rather easily conducted. The Party and the Government determines mammoth investment policies and banks implement these policies by integrated measures with a view to fully utilizing the national resources for development ■