

**A. REALITY**

The stock and monetary markets can be defined clearly but the financial cannot. The stock market is where to purchase and buy stocks, bills of enterprises. To sell them as ruled by French law-firms must announce financial statements of three successive years so that buyers understand their losses and profits, notified accounts must be certified by competent accounting experts and so on. The monetary market is

rently and less in the future after re-organizations. Until January 1, 1996, their capital totalled VNĐ109,000 billion, or averaged VNĐ18 billion each. Their equipment lags behind from 4 to 5 generations. As much as 5% of them was newly equipped, but more than 60% of imported machines were manufactured before 1960, 15% in late 1990s, remaining 25% in 1960s and 1970s. It is striking that 80% of "new" machines were appreciated threefold to fourfold. Fixed capital

đồng accumulated and 0.32 đồng paid to the Treasury, this return ratio was not satisfactory. Around 20% of capital was lost in doing business.

According to statistics on Dec 31, 1995, state-owned firms attracted external funds 2.3 times more their State grants-in-aid. Regardless of their bank loans for working and investment, their payments amounted to VNĐ33,000 billion by late 1994, or 20% of their total turnover, 54% of total capital. If including the difference between debits and credits, their mobilized capital was 2.7 times more than State one.

2. Private firms: there are now 25,000 licensed private firms with total capital of VNĐ10,000 billion, mainly located in big cities such as Hà Nội, HCMC, Đà Nẵng City. Most of them are engaged in trade, services, food processing, construction, but only 1% of them in industry. Some 100 private firms were permitted to enter into joint ventures with foreign partners. Their quantity is though fourfold more than that State-run firms, but their capital is only 13%-14% of State one.

Through inspection, most private firms did not have bookkeeping, if any, they use double accounting. For instance, the tax inspection team of District 1, HCMC discovered 169 tax evaders out of 217 firms inspected with VNĐ700 million worth of tax evaded. Some firms set up ghost documents to take out huge loans from banks.

Both Vietnamese state-owned and private firms are being pressurized by foreign rivals. Foreign firms

# VIETNAMESE FINANCIAL MARKET REALITY AND SOME SOLUTIONS

by Dr. Lê Khoa

established by banks: the bank buys fixed and call deposits and pays monthly interest to depositors, it also makes short- and long-term loans for enterprises with certain interest rates. The financial market can be roughly defined as follows:

(a) It includes both the stock and money markets.

(b) It is where firms can find funds to meet their demand for fixed and working capital.

In fact, some Vietnamese economic terms is yet defined clearly, the term of financial market has numerous meanings according to users. In this article, we would like to mention the definition (b) and describe state-owned and private firms, their capital need and their borrowing and their selling shares to meet their demand. Then we assess the current financial market in comparison with the country's industrialization and modernization, and involve the lift of barriers for fast growth of industry and agriculture.

## I. FINANCIAL POSITION OF VIETNAM'S ENTERPRISES

1. State-run enterprises: the number of state-owned firms has reduced from 12,300 to 6,000 cur-

was concentrated mainly on enterprises under the central government, their capital is 7 times bigger than local ones whose average capital reaches only VNĐ4.2 billion.

The general survey in 1994 showed they earned a profit of VNĐ7,000 billion, central firms VNĐ3.6 billion/year, local ones VNĐ318 million/year. In 1995, one đồng for business brought in 0.19





have invested US\$8 billion in their business from 1988 until now, these funds were mainly focussed on few firms so they have a capital of hundreds of millions of US dollars each, modern equipment and high leverage

#### I. USING MOBILIZED CAPITAL ON THE FINANCIAL MARKET

It is crucial to consider whether Vietnamese firms borrow money to invest; buy new equipment; produce goods for export and import or to buy houses, land; pay debts; deceive others; embezzle public funds and lead a life of luxury.

##### 1. Borrowing for investment:

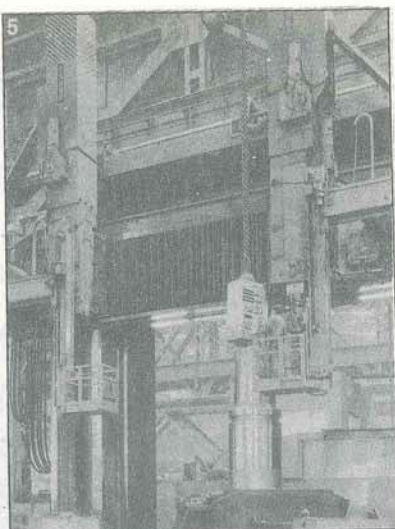
Borrowing for investment, purchase of new equipment is the most important to the country's industrialization and modernization. As mentioned above, new equipment imported in recent years usually lags behind many generations and is appreciated many times. Thus, from 1991 till now, firms have innovated 5% of their existing machinery only by importing old equipment including threefold to fourfold appreciation. This obviously cannot meet the requirement of industrialization and modernization. HCMC Service of Industry found that investment in technology innovation reached only US\$10 million from 1990 till now against the city's annually import turnover of hundreds of millions of US dollars.

##### 2. Borrowing for export-import support

The nationwide export turnover soared to US\$7 billion in 1996 from US\$2 billion in 1991, import turnover to US\$11 billion from US\$2 billion in the same period. Borrowing for export or import has good effects on economic development (if there is not large trade gap in importing consumer goods), particularly borrowing for export support. Regrettably, the figures of trade gap were 890; 900; 2,830; 4,000 in 1993, 1994, 1995 and 1996 respectively (US\$ million) not to mention illegal imports. Most of imported commodities were consumer goods or materials which can be produced in Vietnam such as fertilizers, steel, paper, glass, porcelain, diesel engines...Therefore, credit given to import outnumbers that to export, especially this credit also enjoys deferred payment.

##### 3. Borrowing for keeping goods in stock

When imports land Vietnamese ports and are ready for sales, in



principle, the bank requests the importer to settle import L/C before taking commodities. But if the importer do not have enough money to take goods, he asks the bank to use L/C for deferred payment (the bank has to guarantee to pay for L/C to foreign suppliers), or if L/C has been settled, the importer wants to borrow in accordance with the procedure of stockpiled goods in a couple of months. This procedure is also applied to domestically made goods that is unsalable at present.

By late 1996, the glut of commodities reaches around 500,000 tonnes of cement; 270,000 tonnes of steel worth VND9,700 billion; tens of thousands of paper, hundreds of thousands of color TVs, 1 million tonnes of fertilizer and so on due to excessive import. As a result, credit for stockpiling increased proportionately, to huge amounts of money. Enterprises do not have money to pay to workers, tax, due interest to banks, so they must sell their goods at cheap prices. This is a reason why the price indexes were negative over the past months.

##### 4. Borrowing for trading in houses and land

From 1990 to 1995, price of houses and land skyrocketed, this prompted many firms to trade in real estate: bought land and built houses in 4-5 months then sold and might have a return ratio ranging from 50% to 300%. Enterprises mortgaged their houses and land to banks, or used loan capital in foreign currency by deferred payment L/C-its interest rates is much lower than domestic ones-to buy houses and land. This business went

smooth when houses and land sold like a hot cake and they could easily convert real estate into money at any time. Loans for real estate business are tremendous due to houses increasingly built per year. However this figure has not been revealed, it is thus hard to point out accurately.

##### 5. Borrowing for debt clearance

Capital of state-run businesses is small, representing only from one twentieth to one tenth of loan capital, many have smaller one. Some firms have even been assigned some liabilities but not accordingly associated with assets when they were established because they have to bear losses of bankrupt businesses. As a result, many firms had to borrow money to pay debts, without it, they could not have enough capital to operate.

When the way of borrowing for debt clearance was applied on large scale, new interest would become new debt and increase fast according to double interest formula.

##### 6. Borrowing among firms

Firms only sold a small part of their products on their own, most of them were sold by others (in case of finished goods), or "supplying materials first, receiving payments later" (in case of firms producing materials, agro-products, mineral products". Therefore, firms use others' capital and as Vietnam have not used commercial bill, suppliers cannot ask for effective payments (in foreign countries, receivers must pay by commercial bill, when the bill is due, if they do not pay, they will be brought into court and forced bankrupt.)

#### III. THE FINANCIAL MARKET AND STAGES OF ECONOMIC THRIVING AND RECESSION

Since 1991, there were some signs of economic thriving due to some reasons: increase in foreign investment and aid, house and land prices, big profits from export-import activities, booming tourism...Banks easily made loans, especially opened deferred payment L/C to help firms sell imports and use the earnings to do other businesses such as buying houses and land for expected huge profits. But from 1995 to 1997, this fast and easily profitable business no longer remained. Excessive import led to fierce competition between domestic goods and foreign one. Consequently, domestic firms could not sell off their goods and pay debts to banks and taxes to the Government.



Even local importers also competed vigorously with one another, this resulted in heavy losses to some importing firms. The yield of rice, cashew, coffee though soared but their prices tumbled. Domestic prices rose while falling exchange rate led to less profit in export. Houses and land prices dropped by around 30%, hotel occupancy was low in 1996. Many firms such as Epco, Minh Phung faced heavy losses. In early 1997, the director and some executives of Tamexco were brought into court. Banks became cautious to make loans, procedures of borrowing and mortgaging were applied more prudently. As a result, state-run and private firms found hard to take out loans. They became prudent in taking out loans as they must collateralize their assets and pay debts, if not they could be put in prison while they could borrow money to pay old debts without punishment. Some firms have offloaded their goods to avoid heavy interest. If big firms such as Epco, Tamexco, Minh Phung go bankrupt, they will cause financial disaster to their creditors. Similarly, when farmers suffered losses due to falling prices of cashew nut, rice, they could not afford industrial goods or consumer ones. The economy saw many signs of stagnation in 1996-1997 while it flourished in 1991-1994.

#### B. SOME SUGGESTIONS

The financial market underwent a torrid time due to shortcomings of bankers. The banking sector therefore launched an anti-corruption campaign with its seven measures. In the Vietnam Bank for Industry and Trade alone, 208 officers have been penalized, including 3 cases of VND130-million compensation. However, in addition to corruption, some problems of macro- and micro-economic management remained unsolved: hard exchange rate, high interest rate, import of consumer goods, trade deficit, glut of commodities, losses of both importers and local producers and so on. As for micro-level, state-owned firms' leverage was too low as they were assigned debts of bankrupt firms. Because they have borrowed money to pay debts since 1991, they must pay big interest and finally they fell in insolvency. If they continue to do business, their profit still cannot offset banks' interest (not to mention payment of principal) and the nightmare of being imprisoned has puzzled them.

The situation is very complicated



and needs effective solutions. The following are suggestions:

#### I. SITUATIONAL MEASURES

To continue to give loans to firms although their leverage is too high.

1. To lend rice purchasing firms in the Mekong Delta and cashew nut processing ones:

After requiring enough guarantees for loans, in April 1997, the State Bank instructed commercial and agricultural banks to make loans for rice purchasing firms. Cashew nut buying firms were entitled to borrow money to buy up farmers' products, according to Deputy Minister Phan Văn Khải. On May 31, 1997, the State Bank issued Official Letter 417 to overcome stagnation in trading: state-run firms were allowed to borrow money from banks without mortgaging and restriction to their registered capital. The loans will be based on business efficiency. As many as VND3,000 billion worth of short-term capital were changed into medium- and long-term loans for projects specified by the Government. The program for offshore exploitation of marine products was funded VND2,000 billion. Short-term loans were granted to buy up paddy and cashew nut.

2. To liquidate some enterprises including state-run ones due to their prolonged losses:

When the firm goes bankrupt, it will cause following damages: (1) workers lose jobs (2) banks that are its creditors will suffer losses as they take back only part of their loans after the firm's remaining assets are sold (3) in case the firm is

owned by the State, the bank is the same then losses can be hard to settle. It is easier if the firm is privately or oversea owned (4) if it is a big business, its bankruptcy will lead to a domino effect on smaller ones which it owes

3. To replace Mr Tăng Minh Phung and Mr Liên Khui Thìn, directors of Minh Phung and Epco respectively with other boards of directors when both of them were put in jail and give loans to new directors so that they can maintain operations of these corporations, especially their import and export.

#### II. MEASURE TO INCREASE TURN-OVER AND PROFIT OF FIRMS

This measure aims at improving their ability to pay debts to banks and taxes to the State and to expand production. This is the most logical solution. However, the extent of application should be paid attention to: only taking correct dose of medicine can cure the illness.

*Correct medicine but inadequate dose*

1. In March, the State Bank raised the exchange rate, up by VND500/US\$1, to VND11,650/US\$1. Although some people feared that the rise in exchange rate would lead to price hike, but the price index was negative in three successive months: 1%; 0.1%; and 0.5% in March, April and May respectively. However against the peak of exchange rate: VND13,255/US\$1 in late 1991, the remedy of lifting exchange rate is not unsatisfying.

2. One of reason causing troubles to the national economy is to import a large quantity of consumer goods



and those local firms can meet the market demand. It also pushed home importers to fierce competition (Epco, Minh Phung and Tamexco, for example, sold fertilizers at low prices to settle their debts), led to a torrid time of local producers due to fighting against foreign goods. The volume of imported fertilizers reached 4 million tonnes per year while demand was around 3 million tonnes. The import value soared to above US\$11 billion in 1996 from US\$2 billion in 1992, up by five times, not to mention illegal import. Therefore, the Government has decided not to import more fertilizer, cement, paper, motorbikes, sugar and so on in the last half of 1997. This is truly proper, though insufficient as the list does not include all items which need protection and restriction over import such as foreign milk, cotton, fruit, coffee, cosmetics and so on. Illegal import of consumer goods have not been reduced yet due to low exchange rate such as foreign spirit, cigarettes...

c. The Government should urgently use a fund of VNĐ3,000 billion to boost economic development (using short-term capital to grant medium- and long-term loans to projects specified by the Government). However, some argued the fund was not enough to make the economy thrive as it is too small against the value of trade deficit in 1996 (US\$4 billion).

### III. STRONG MEASURES TO SHIFT FROM STAGNATION TO FAST DEVELOPMENT WITH A GROWTH RATE BETWEEN 14% AND 15% ANNUALLY.

#### 1. Exchange rate

On the *Phát Triển Kinh Tế* published in November 1996, Mr Van Ngọc wrote: "According to fairly correct calculation, our real exchange rate is VNĐ13,400/US\$1. The nominal exchange rate was VNĐ11,030/US\$1 in late 1996, that is our currency has appreciated by 21%. It caused a fall of 21% in import price, so although tax rates imposed on imports rose, local producers could not compete with foreign goods due to their cheap prices. On the contrary, prices of goods made for export went up by 21% (due to increase in domestic price) and so exporting businesses suffered losses or gained less profit." In our opinion, the suitable exchange rate

ranges from VNĐ13,500 to VNĐ14,000 to US\$1, the same as Mr Ngọc's calculation. Nonetheless, if we want to reduce illegal import, we should attract floating US dollars into banks. Therefore, in addition to official exchange rate, the Government should offer preferential rate to US dollars of tourists, remittance, outside sources with a price 5%, 10% or 15% higher than official rate. These dollars will be sold to those who want to buy foreign goods at high prices.

By this way, the Government can help boost local production.

#### 2. Using quotas to reduce imports

The list of restricted imports issued for the last half of this year should include more items. For instance, if foreign powder milk floods the market, it will put obstacles to the development of home cow breeding. We propose the Ministry of Trade should consult Vietnamese producers when setting import quotas and permit only import of goods of which the market is short so that local firms can sell their products and pay debts to banks and taxes to the State.

#### 3. Lowering interest rates

Nominal interest rates (above 1%/month) have though dropped, but it is still far higher than that of Japan (0.5%/month) or other countries. In fact, real interest rates went up in 1996 and 1997, due to negative price indexes in months. So we propose the State Bank to cut nominal interest rates in order to reduce the increase in real interest rates.

#### 4. Supplying money for huge investments

ments

Because of negative price index, the Government should supply money for huge investments with the aim to cause price hike, turnover and profit to firms. The amount of supplied money could reach US\$4,000 million (equivalent to the trade gap value in 1996). With these funds, the Dung Quat, Vũng Tàu Ports and some export processing zones could be completed fast and the problem of excessive steel, cement could be solved.

#### 5. Changing credit from supporting import, lending for settling old debts, buying houses and land, keeping goods in stocks to lending for innovating equipment

The Government should give incentives to investments: classifying kinds of credit which it allocates, credit for innovating equipment should enjoy preferential interest rates (0.4%-0.5%/month) and others could pay higher ones (1%-1.1%). The State Bank should make re-funding for investment with interest rate of 0.3%-0.4%/month so that commercial and investment banks do not suffer losses.

#### 6. Overcoming debt crisis of state-owned firms

The unorganized market economy, after flourishing during from 3 to 6 years, will face stagnation which could last from 3 to 6 years. This repression will lead to bankruptcy of big and small firms, falling GDP and prices, depreciating shares and so on. But it also make firms financial position healthier: badly managed firms will be replaced with good ones. Then a new stage of development starts and it is likely to fall in another stagnation.

Stagnation will cause numerous losses to the national economy. So the Government has to take strong measures to overcome it. Most effectively, the State Bank supplies money for huge investments and debt settlement of good state-run firms. This measure could avoid losses of stagnation. On the whole, the Government should shift from hard exchange rate into soft one, accept the appropriate money supply to settle debt and invest in large projects instead of curbing inflation only.

