THE VIETNAMESE BANKING SYSTEM IN THE INTEGRATION PROCESS

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1. Pre-integration period

From 1998 on, although the financial liberation and integration of the banking system to the world market wasn't publicly declared, the SBV started its preparations for the international integration when implementing the monetary policy. The preparations are as follows:

a. Step- by- step liberation of interest rate:

From August 2000 on, the SBV changed from fixing the interest rate to establishing the base interest rate for loans in the domestic currency and connecting the local interest rate with the international one on loans in foreign exchange.

On June 1, 2001, the SBV liberated the interest rate on loans in foreign exchange, allowing banking institutions to decide on the interest rates in the dollar, but it still kept strict control over the interest rate on bank deposits in foreign exchange with a view to preventing legal entities from keeping foreign exchange in their accounts and dollar from becoming a legal tender.

From June 1, 2002 on, the SBV officially allowed the liberation of interest rate on loans in the domestic currency, that is, to allow banking institutions to fix their interest rate according to market forces and creditworthiness of customers. The SBV stopped fixing the band around the base rate. However, the publicized base rate was based on the commercial lending rate offered to the best customer by banking institutions and selected by the SBV in each period. This practice helps orient the market rate and facilitates measures to control changes in the market meeting requirements and targets of the monetary policy of the period.

The strongest point of this mechanism was to create conditions for banking institutions to mobilize dead money from the public at reasonable interest rate and supply credits more quickly to customers. According to the mechanism for controlling the lending rate, a band of 0.3% per month around the interest rate on short-term loans and 0.5% on medium- and long-term ones made the interest rate fail to reflect changes in the market forces. For example, many households and businesses in rural areas found it hard to access bank credit because the supply of loans to these areas wasn't cost effective while banking institution had to observe the lending rate ceiling. As a result, many peasants ha

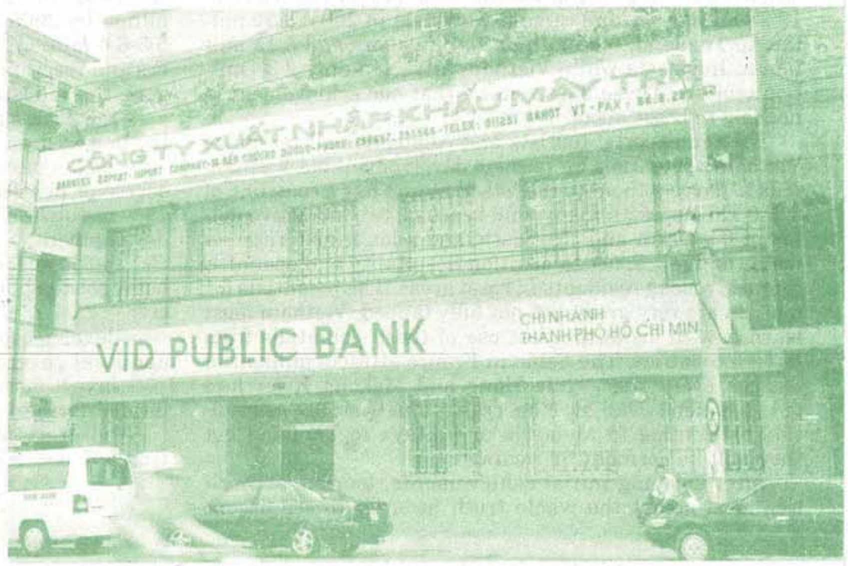


Photo by Nguyễn Ngọc Đạo

to borrow from usurers at interest rates four times higher than the official one.

The mechanism also facilitated the reform in the banking system that aimed at making it suitable to the market economy, financially stronger and safer, more competitive and able to integrate into the international money market.

b. Step- by- step adjustment to the exchange rate control:

In 2000, the exchange rate control became more flexible when possible changes in the exchange rate of the VND to the dollar were taken into account. The mechanism for exchange rate control was adjusted by various decisions by the SBV but legal entities were still forced to sell part of their earnings in foreign exchange to the SBV.

In 2001, the SBV adjusted term of trading session and increased the percentage added to the ceiling of exchange rate agreed upon signing trading contracts.

The mechanism for controlling current transactions, cross-border payments and exchange control at borders was less strict, allowing private persons to buy, transfer and take foreign exchange abroad. From August 2001 on, companies were allowed to decide on borrowings from foreign lenders after considering the international lending rate and exchange customs and foreign-invested companies could open capital accounts in foreign exchange.

c. Merging joint stock commercial banks with state-owned commercial banks:

In 1999-2000; any commercial banks with poor performance were to be put under SBV control and necessary measures to be taken to deal with their debt, allowing other banks to acquire them otherwise the SBV would have them dissolved. The SBV also granted legal capital to state-owned commercial banks and refund them to restructure them as required.

In 2001, the SBV consolidated joint stock banks with poor performance, such as Việt Hoa, Nam Đô and Quế Đô; required other joint stock banks to ensure the legal capital as required by law; and took special measures to supervise poorly-managed banks in order to prevent losses.

d. In 2000, the SBV introduced many mechanisms to ensure the general safety and security of the banking system: forming the Deposit Insurance Fund, forming contingency reserves, regulations on withdrawal of licenses of banking institutions, etc.

In 2001, division of territories for banking institutions was removed. Joint venture and foreign banks were allowed to take land use right mortgaged by local customers and receive deposits in the domestic currency to the order of 25% of the legal capital of local bank.

- After the BTA:

In November 2001, joint venture banks were allowed to open account in foreign exchange for Vietnamese customers to the order of 50% of the legal capital of the joint venture bank.

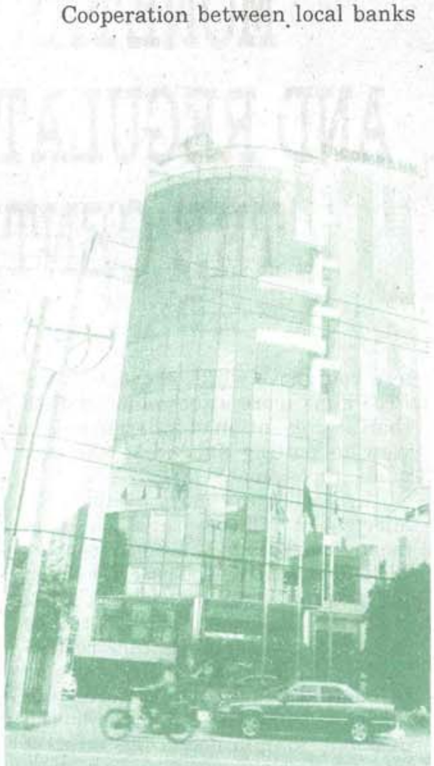
From 2002 on, banks were allowed to establish overdue debts according to international practices, which helped banks negotiate interest rate on these debts more easily.

- From 2002 on, banks were allowed to decide terms of all loans, including ones supplied to foreign-invested companies. This was the first time the overdraft facility was introduced to the public.

These could be considered as preparations for the liberation and integration process that aims at beefing up local banks and making them more competitive in supplying better and more diverse banking services.

2. Plan for integration in the years 2002-2010

Cooperation between local banks shows that they want to improve their competitiveness. In other words, local banks are making active responses to the program to liberate the interest rate and maintain the market share for local banks.



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The integration process of the banking system in the years 2002-2010 includes four parts: opening the market for wholesale banking service, enhancing the competitiveness in supplying retail banking service and applying necessary measures to ensure a safe climate for the banking service, restructuring state-owned commercial banks, and ncouraging acquisitions and merge[illegible]ong local banks.

a. Opening the mark[illegible]t for wholesale banking service: First of all, participation of foreign banks in the wholesale banking service should be expanded. Vietnam had better encourage branches of foreign banks to use Vietnam as their Asian bases and allow them to get access to companies and high-income earners in order to help them find new business opportunities.

To open the wholesale banking service to foreign banks will help local industries to get access to financial and banking services of international standards on their way to development.

b. Enhancing the competitiveness in supplying retail banking service: In this service, it's necessary to remove restrictions on establishment of branches and ATM networks, allow to issue bank cards, remove limits on bank deposit.

c. Restructuring state-owned commercial banks: This aim could be achieved by separating the task of supporting revolutionary families from the banking service; calculating exactly and sufficiently costs, expenses and income of state-owned commercial banks; and privatizing wholly or partly state-owned commercial banks.

d. Encouraging acquisitions and merger among local banks: The SBV could encourage joint stock banks to cooperate with one another in various forms to establish strong banks that could expand business beyond the domestic market. In addition, the SBV must make regulations with the aim of struggling monopoly and unfair competition from financially strong banks.

In short, the banking authorities had better perfect the legal infrastructure based on international laws and each bank improve their performance in preparation for the integration process■