



To make the best use of local sources of finance is a topic relating to important policies of the Government (to develop the economy based on internal economic strength) and many solutions have been introduced and even carried out for years. Past experience can help us now lay off ineffective ones and carry on with practical ones.

#### 1. INEFFECTIVE SOLUTIONS

##### 1. High deposit rate

To attract dead money, high deposit rates have been offered and maintained for a long time. In fact, high deposit rates have made bank deposits to increase immediately, however, this practice (adopted by not only banks, but also many companies) didn't always produce good results. High deposit rates certainly lead to high lending rate with the result that many companies suffered financial difficulties because their sales and profit were reduced. Even companies with good business performance were brought to the brink of bankruptcy. Many companies (including many state-run ones) and individuals had to secure high-interest loans to pay due debts,

as a result, the interest rate rose drastically and everybody sent their savings to them. After a while, everything went from bad to worse, a lot of borrowers became insolvent and declared bankrupt, some others decided to get away with all money they had borrowed after converting it to gold or foreign exchange. In 1997, some 30% of state companies suffered losses and this figure rose to 40% in 1998. The amount of state companies reduced from some 12,000 in the early 1990s to 5,000 at present and 40% of them are loss-makers. In our opinion, the main cause of this situation is the

high interest rate (after many adjustments, the interest rate has decreased from 14% to 1.1% a month at present, it's still high as compared with the interest rate of 2% a year in Japan). Other causes, such as high proportion of loan capital to working capital, bad management, embezzlement, etc. are of no great importance because most managers of state companies are VCP members and in all state companies, trade union and other public organizations are allowed to take part in management. Let's study an example. The Mulberry and Silkworm Corporation secured short-term bank loans and in-

vested in mulberry plantations and new factories. These plantations and factories developed well in the early 1990s but the Corporation suffered losses because of high bank interest rate while no shortcomings in management and production process were found.

Businesspersons always compare bank interest with prospective profit and they only decide to borrow if the former is lower than the latter. Marx also considered interest as part of the surplus value because it helps bankers to exploit labor. In socialist countries, by lowering the interest rate, the banking system kills two birds with one stone: encouraging

# TO MAKE THE BEST USE OF LOCAL SOURCES OF FINANCE

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businesspersons to borrow money from banks to develop the production and ensuring social equality.

Some others question how the banks can get enough money to loan to companies without raising interest rate while increases in the money supply will lead to inflation. One way or the other, the banking system in such a country as Vietnam where capital is accumulated slowly has to offer a rather high interest rate in order to increase bank deposits, encourage saving and prevent inflation. That is why the bank interest rate in Vietnam is still higher than in foreign countries.



In Japan for example, low interest rate still ensures high bank deposits for banks because of many reasons: (1) wage and salaries are paid directly to laborers' bank accounts, (2) paying by cheque is a common practice, (3) paying in gold or foreign exchange is illegal, all payments must be made in domestic currency, (4) discount is offered to payments in cheque, (5) drawers making cheques that could be dishonored will be sentenced to imprisonment, etc. If these measures are applied in Vietnam, they will produce the same results, the banks

tem, is much more dangerous than gradual devaluation. In periods when the price index is negative or increases slowly, the banking system had better issue more bank notes to finance major investment projects in order to improve the production. However, Vietnam's banking authorities haven't been totally persuaded by this opinion and gradual devaluation was reluctantly agreed on. High lending rate has made the average production cost in Vietnam increase with the result that the international competitiveness of Vietnam is poorer and poorer. So we

interest rate, speculating on real estate, spending on imported luxury goods, or paying due debts, etc., and they only made inquiries about assets mortgaged or financial strength of borrowers. If answers to these inquiries are favorable, loan will be provided at once. In Vietnam, these officers are considered as respectable. In many cases, borrowers have to give bribes (as a percentage of the loan) to these officers in order to get bank loans. That is why a lot of companies, both private and state-run ones, could mortgage an asset (a house for example)

### 3. Personnel training

Wrongdoers can invent all kinds of tricks to get money from the banks, from using false documents, giving bribes to forming "ghost companies", and there are many reports on these tricks. This fact means that bank personnel need to be trained in banking regulations and methods of estimating investment projects, assets mortgaged and creditworthiness of customers. In addition, necessary measures must be taken to beef up the work ethic of banking officers.

## II. TO MAKE THE BEST USE OF LOCAL SOURCES OF FINANCE

In our opinion, the best measures to mobilize dead money are to lower bank interest rates (in order to enhance competitiveness of locally-made goods on foreign markets) and to force (and encourage) individuals and organizations to use banking services (requiring companies to make payments through banks, punishing drawers of dishonored cheques severely, preventing payments in gold and foreign exchange, etc.). Moreover, in recessions, banking authorities had better use inflation to finance major investment projects. The heart of the problem is how to put money in feasible investment projects: good projects that could promote production will be financed by banks. In 1998, the banking system carried out this task rather well. Banks provided food trading companies with capital to help them purchase rice and other agricultural products (cashew, sugar cane, etc.) from farmers after harvests, therefore, prices of agricultural products were kept high in 1998 and farmers' income was improved. The banking system also invested in plans to build deep-sea fishing ships and new sugar refineries. These achievements are very en-



need not to raise interest rates and bank deposits will be big enough for them to supply loans to companies and individuals. If there is a shortage of capital, the Government can increase the bank circulation, because according to Keynes, gradual devaluation of the domestic currency can lead to an economic boom because everybody will spend more or turn their savings into investment. In Vietnam, the price index in certain months has become negative making businesspersons cry for help. This means that disinflation, or stabilized monetary sys-

tem, the banking authorities to consider this problem and find out measures to lower step by step the bank interest rates while keeping bank deposits large enough to ensure capital for companies.

### 2. Lack of Inquiries about customers

To mobilize and employ effectively local sources of finance, full attention must be paid to the use of bank loans. Surveying many banks and credit cooperatives, we saw that most loan officers weren't interested in this problem: bank loans could be used for relending at a higher

to various state-run banks and take away large sums of money, and some of them (such as Minh Phung, Epco, Tamexco, Saigon Garment Company 3, etc.) have caused great damage to the banking system when they went bankrupt. After this series of corruption scandals, many businesspersons and government officers were brought to court and new regulations were set up. In fact, banking regulations are really strict enough to prevent all frauds. If they are observed, bad debt will certainly be kept at a low percentage.



couraging and no serious banking scandals happened in 1998.

In all investment projects, there are always expenditures on fixed assets. The bank must insist on buying modern machines and production lines in order to ensure high quality products and low production cost. In addition, full attention must be paid to the question of whether these production lines are paid in the domestic currency or in the foreign one. Regrettably, this question didn't raise much interest from banks, local governments and planning and investment authorities. If these fixed assets, or the better part of them, are locally made, some bank loans in domestic currency are enough to have the project realized. If these assets should be imported, the bank should pay in foreign exchange, thereby, missing chances to make use of local sources of finance.

Thus, we see that banks' performance and lending policies are related to the policy to develop heavy industry. This policy is one of the cornerstones of the Marxist-Leninist political economics and of the fast development strategy as well, and generally, it should be considered as the backbone of the banking and monetary policy.

As we know, to develop fast, we must increase the gross investment. W.W. Rostow based his development theory on the Gross investment/GDP ratio. If this ratio reaches 30%, the economy is starting its self-sustained growth (where the economy can develop by itself without intervention from the government or banks), or in other words, the industrialization and modernization are completed. Vietnam's GDP in 1998 is estimated at US\$26.5 billion while FDI was worth US\$1 billion and

ODA was US\$1.4 billion. PM Phan Văn Khải informed us that investment from foreign sources represented some 40% of the gross investment, that is the Vietnam's gross investment in 1998 was US\$6 billion. Thus, this gross investment isn't high enough to enable the economy to come to the self-sustained growth as calculated by Rostow ( $30\% \times \text{US\$26.5 billion} = \text{US\$7.95 billion}$ ).

Due to the Asian economic crisis, it's hard to attract more foreign capital. To limit effects of the crisis and create more jobs, the only measure we can take is to mobilize local sources of finance to the best of our ability and invest in the heavy industry. With a well-developed heavy industry, the banks need only to supply loans in domestic currency. According to Keynes, if the money supply is increased when the economy is in recession with a view to inducing inflation and encouraging spending, then the inflation is of great benefit to the economy, because the spending power at present is low, companies find it difficult to sell their products and many workers are laid off, increases in the money supply will help to build new factories using locally-made materials and create new jobs. This practice can lead to a high inflation rate but it produces many good results: providing laborers with jobs, reducing hidden unemployment, raising the spending power, helping companies sell their dead stock, increase the tax take, helping banks collect doubtful debt, and ensuring a high growth rate.

In short, new factories should be built of locally-made materials and machines so all payments can be made in domestic currency, by doing so, we can make the best use of local sources of finance.

Otherwise, the economy will depend on foreign investment and imported technology and will suffer bad effects of the world economic crisis.

The plan to mobilize local sources of finance also needs certain preconditions. The first one is a program to save domestic market for local industries. Many factories have faced difficulties or have been running down because of foreign competition (foreign consumer goods were allowed by the Ministry of Trade to flood the market, or the customs failed to prevent smuggling). Public opinion appreciated the government's efforts to bring Tân Trường Sanh Company, the biggest smuggler ever found, to court and stop importing consumer goods that could be made locally.

The second precondition is to accept locally-made goods in spite of their poor quality and high production cost because it will take some time before Vietnam can produce goods of the same quality as foreign ones. To create this precondition, help from the government is much needed. Looking at the sugar industry, we can easily see that price of local sugar is dearer than imported one. Its production cost is high because of obsolete production lines, long distance between sugar plantations and sugar refineries, and the use of low-yield sugar cane strains. However, farmers can sell sugar cane to refineries at high prices and consumers are content with local sugar because import of sugar is banned. This situation is beneficial to producers, not to consumers but it's good for the economy because it increases the velocity of circulation while increases in import can accelerate the outflow of foreign exchange. Thinking through, main stress must be put on production, not on consumption. Moreover, com-

panies under the market mechanism should find ways to reduce production cost and enhance product quality in order to survive and develop. That is why Frederic List advises developing countries to protect their industries against foreign competition.

In conclusion, we think that the following programs should be carried out to make the best use of local sources of finance:

- + The Government takes measures mentioned above to encourage the use of banking services.

- + Carrying out regular inspections of banking operation, providing banking officers (especially loan officers) with training courses in banking services and regulations and ensuring reliable supply of loans to feasible investment projects.

- + The customs machinery must be strengthened in order to make it efficient enough to stop flows of contraband goods. The act of selling illegally-imported goods should be punished properly.

- + The Ministry of Trade should ban the import of goods that could be made locally as required by the National Assembly. Many other barriers could be used to protect local production.

- + The Government had better advocate using inflation to finance major investment projects during recessions.

- + To make use of domestic capital, it's necessary to develop the heavy industry and encourage the use of local raw materials and capital goods. This is also a good way to save the domestic market for local industries.

All of these programs must be carried out simultaneously and consistently if we want them to produce intended results.