Chapter 1

INTRODUCTION

This chapter mainly focuses on Vietnam Overview, Research Objectives, Literature Review, Research Questions; Research Methods and Framework of Research.

Nations and States are historical constructs and are always in the dynamic process of being and becoming\(^1\). The 20\(^{th}\) century history is replete with decolonization, socialist revolutions and people’s democratic movements. The targets of these movements, such as, securing equality, justice and self-governance have re linked hope and aspirations of the toiling masses spread across the third world countries. Nationality struggle, therefore, essentially should have at its core the principle of anti-imperialism and anti feudalism. Vietnam has also experienced many discontinuities in the form of colonization, civil war and war with other countries. It is since 1986, we witness a period of Vietnamese stability with "\textit{Doi moi}" (Renewal). The study of the economy in transition can provide a useful insight for practitioners of diplomacy and policy makers.

With the economic renewal policy, Vietnamese banking sector has witnessed structural changes. Vietnam has built up important bases for a monetary foundation and a banking system in conformity with the market economy. More than 10 years ago, thanks to active renewal and integration, Vietnam has pushed back and controlled inflation, stabilizing macro economics, creating favorable conditions for high economic growth in the long run. And gradually shifting economic structure under the direction of modernizations and industrializations, gaining outstanding achievements in the poverty eradication cause, stabilizing and improving people’s lives.

Vietnam’s two tier banking system came into being in mid 1980s. It was a big step in the long run development of the banking sector in the market oriented economy. Its focus was to promote efficient Vietnamese banking system, making contribution to monetary policy performance, and accelerating socio-economic development of the country. The State Bank of Vietnam (SBV) has discharged its functions and its role as state monetary manager and controller and the commercial banks, performed their banking operations and diversified banking products and services. Many changes took place in the banking sector in the restructuring process, and more difficulties and challenges were confronted in course of the banking reform in the era of globalization and liberalization.

At the end of 1997, when the regional financial monetary crisis occurred, Vietnam economy also suffered many negative impacts: economic slowdown, declining of foreign direct investment (FDI), stagnating domestic demand, and serious balance-of-payments problems, fiscal or banking crises common to many countries in the region.

In the two years of East Asian recession, Vietnam has followed a cautious economic stance by introducing wise and flexible policies and suitable steps, giving priority to ensuring macroeconomic stability rather than taking risks in order to achieve higher growth. This has led to some successes; Vietnam has restricted considerably disadvantage impacts of the regional financial monetary crisis, stabilizing the economy and socio-politics, step by step regaining the growth momentum and reducing poverty.

Indeed, the regional financial monetary crisis has also revealed the weaknesses in the Vietnamese banking system, requiring strong and urgent reform measures. Restructuring Vietnam banking system is not only required urgently for regional and international integration, but also to ensure its security, sound financial health and sustainability of the banking operations as it could not be postponed. Vietnam is putting its efforts to realize the restructuring cause of its banking system under the following directions:

To implement a careful monetary policy, managing flexible interest and exchange rates, using actively indirect instruments by the market economy, gradually removing direct administrative measures so as to stabilize macro economic performance and to create favorable and open conditions for production, businesses, and services and for diversification of banking products and services. Simultaneously, bank supervision both at-site and off-site, accounting standards and financial and technical skills need to be strengthened to raise confidence among prospective users of banking services and maintain security and prevent occurrences beyond its control.

To treat non-performing loans (NPLs), upgrading financial capacity, strengthening management, and modernizing banking technology, etc, international standards and formalities have to be introduced by conducting an applicable approach. Removal of policy lending from commercial lending is also highly respected for enhancing specific functions of market-oriented banking. Further, the most concern of the government is for highly respecting and appreciating the autonomy in business operation, self-responsibility of the financial institutions. That could be done through the promulgation of prudential regulations and improving banking supervision. Further, the risk reserve funds and deposit insurance company would soon be established.

There will be proper steps and programs in order to strengthen, recover, merge or supervise weak financial institutions by treating seriously the institutions or individuals that had illegal, immoral actions, the banking system is being made more healthy and sound.

Vietnam highly appreciates the lessons and experiences gained from other countries in their endeavor to overcome the financial and monetary crisis and
restructure their banking sector. It would like to share these valuable lessons and experiences in order to build up an efficient, safe, healthy banking system, making a contribution to strengthening financial position in the region.

Across Vietnam, privately and state owned commercial banks will faced vastly changed markets in the 21st century, compared to those of the 1980s and much of the 1990s. Customers will be more demanding, competition more intense, and accounting must be more transparent. Going forward, these institutions must fundamentally reform to succeed.

New opportunities and challenges are prevailing on the global scale. This is happening in the scenery that developing countries had overcome the crisis and on the momentum to regain their economic growth. Competing in a globalized and liberalized environment is a challenge. Renovating national and international financial monetary system is required urgently; Internet and E-commerce have become daily operations of all banks.

Above features of the global economy and finance in the context of the knowledge based economy have made many new cooperation opportunities, but these have also implied many unpredictable challenges and risks for us.

These opportunities and challenges have been linking developing countries together, because harmonious combination of each nation’s, each bank’s respective benefits in a common benefit of all countries in the region will create their strength to overcome great trials.

VIETNAM – AN OVERVIEW

Vietnam is a country presenting many attractive opportunities for a prospective growth. Situated in one of the most dynamic economic zones in the world and endowed with abundant natural and human resources, Vietnam is a country potentially being perspective for a rapid future development.

The country has experienced many changes over the last one decade. Transformation towards a market economy began in 1986 with the implementation of the *Doi moi* (renewal) policy. Many new legal and regulatory reforms are occurring continuously, and authorities are conscious of global competition and the importance of maintaining a favorable environment for socio economic development.

Due to inadequate investment prior to *Doi moi*, Vietnam lacks a modern infrastructure and many logistical difficulties exist. Though literacy is high, technical and managerial expertise is weak. The physical infrastructure needs investment in communication, transport and distribution. Vietnam’s legal system has already
undergone major reforms, but these remains largely untested. The financial infrastructure is embryonic, and statistical information is not independently verifiable.

Nevertheless, Vietnam is now poised to enter a period of sustained high growth.

Geography

The Socialist Republic of Vietnam forms part of the Indo-China peninsula in the heart of South-East Asia and covers approximately 331,000 square kilometers, the country shares a northern border with China, and to the northwest and southwest a border with Laos and Cambodia respectively. The Eastern Sea flanks the entire eastern portion of the country. The S-shaped country of Vietnam is strategically located for both trade and tourism. Over 1,700 kilometers of coastline and a prime position on major shipping routes makes the country a vital link in the region’s trading network.

Long and narrow, Vietnam stretches 1,650 kilometers from north to south and is divided into three regions: north, central and south, with the capital at Hanoi in the north, and the country’s largest city and main commercial center, Ho chi Minh city (formerly Saigon) in the South. Other major cities include Hai Phong- City port in the north; Hue, the old imperial city, and Da Nang in the center; Vung Tau, which is expanding rapidly as the center of the oil and gas industry, on the coast south-east of Ho Chi Minh city; and Can Tho, one of Vietnam’s most prosperous cities, in the Mekong Delta. The topography varies from rugged mountains in the north and undulating plateaus and plains in the center to tropical lowlands in the south. The highest peak is Fan Si Pan in the north, which rises 3,143 meters above sea level; the Quang Ngai – Kon Tum highlands in the center have a number of peaks that are over 2,000 meters. Approximately three-quarters of the country are highlands. The deltas of the Red River in the north and Mekong River in the south are two of Asia’s most fertile rice growing areas. Almost half of the Red river’s 1,148 kilometers flow through the country. The Mekong river, which cuts through neighboring countries: Cambodia and Laos, empties itself near the southern tip of Vietnam. Dao Phu Quoc, Con Son and Cu Lao Hon are among the more prominent islands in the south.

Natural Resources

Natural resources are plentiful, but by no means fully exploited. There is significant potential in energy sources including offshore oil and gas, coal and hydroelectric power. Substantial mineral deposits exist, among them precious stones, copper, iron, lead and building minerals such as clay and graphite. Abundant fresh and salt-water sources teem with life and prospects for a healthy as yet undeveloped aquaculture

2 Vu Tu Lap, Hanoi Education Publishing House, 1999 edition, abstract geographical Data in this section from “Vietnam geography”. 
industry exists. Fertile agricultural land, a predominantly agrarian population and temperate climate dictate a comparative advantage in agriculture, which will grow as production becomes more diversified.

Climate

The distance between north and south gives rise to a wide variation in climate. A temperate climate prevails in the north, where there are four distinct seasons. The winter season between December and early March has an average temperature of 15 degree C and the summer season between May and October has average temperature of 30 degree C.

In the South, the climate is tropical with average temperatures ranging between 25 degree C and 30 degree C throughout the year. The dry season runs from November to April, and the wet season from May to October. April and May are particularly hot with temperatures climbing to an average 35 degree C. Typhoons are quite common along the coast between July and November.

In Central Vietnam the climate is a mix of temperate and tropical. There is no dry and wet season, as rain falls throughout the year. It is relatively dry between January and May and wetter from August to October.

Annual rainfall for the country as a whole averages 1,960 millimeters. The highest rainfall occurs in the mountains of the northwest and central highlands, and the lowest in the southeastern coastal areas.

Demographics and Population

Vietnam’s population, of approx 79 million, is projected to grow to more than an average of 80 million by the year 2010. Of the 54 ethnic groups, the Viet (Kinh) is by far the largest and accounts for most lowland Vietnamese as an estimated 88% of the country’s population. The Tay, Thai, Hoa and Khmer each have a population of some one million, with ethnic groups totaling the remainder and with an annual population growth rate of 2.1% between 1980 and 1989. The population stood at 78.1 million in 1998, 51% of whom were women. The population is relatively young: 75% is under 35 years of age. Overall life expectancy is 68 years. The literacy rate is over 90%. The government hopes to reduce the current growth rate of 2.0% per annum to 1.6% by the year 2005.

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3 Climatic Data is supplied by Vietnam Meteorological Authority, 1999-2000

The population, 79% of which is rural, is distributed almost equally between the northern and southern regions, 70% of the population is employed in agriculture and more than half is under the age of 25 with large concentrations in the Red River and Mekong River Deltas. These statistics have not gone unnoticed by foreign investors who see a highly motivated, cost efficient and elastic work force with potential for an important consumer market. Population density averaged 1,124 per square kilometers in the Red River Delta (excluding Hanoi) and 385 per square kilometers in the Mekong Delta in 1994. The most populous city is Ho Chi Minh City, with approximately 4.1 million people, followed by Hanoi, with approximately 2.1 million, and Hai Phong, with approximately 1.5 million.

Vietnam’s gross per capita income of approx US$ 250 ranks it as one of the poorest countries in the world, but it is by no means impoverished. Due to an emphasis on education, Vietnam enjoys one of the region’s highest literacy rates.

History

For much of the world, The Vietnam war overshadows other events in Vietnam’s turbulent history, but this is only one in a series of many wars in a centuries-long struggle for independence.

Indeed, Vietnam’s history extends far beyond the twentieth century; ancient civilization is known to have lived here since the Paleolithic era 300,000 to 500,000 years ago. The people of today’s Vietnam trace their ancestry back to a collection of tribal groups known as the Lac Viet who inhabited the Red river valley in northern Vietnam dating from the beginning of the Bronze Age. The Lac Viet people were able to establish their own agricultural policy, which came to an end in the third century BC. Beginning from the first century BC, and for the next thousand years, the region came under China’s influence and cultural worldview as Vietnam was subject to two main influences: from India in the south and from China in the north. This influence began to wane toward the start of the tenth century after a series of uprisings led to the eventual defeat of the Chinese army in 939AD, giving way to Vietnamese dynastic rule. Vietnam remained free of external control for the next 600 years, though faced an ongoing threat from Chinese and Mongol forces. By the eleventh century AD the first significant independent Vietnamese dynasty (Ly dynasty 1010-1225) was established. Political and administrative control was exercised through its capital at Thang Long (Present day Hanoi). This period saw much development as a series of dykes, canals and roads were built and agriculture was promoted throughout the country. Administratively, the Ly dynasty introduced its own civil service examination system and a national university to train Confucian scholars. The two dynasties which followed (The Tran and the Le) rebuilt on the foundations of the Ly, creating in the process a Vietnamese kingdom that continued until peasant revolts led to its collapse in 1788. Independence did not signal an end to Chinese transgressions; however, the tale of Emperor Tran Hung Dao defeating Kublai Khan and the Mongol incursions by
impaling their fleet with bamboo spikes at low tide is only one in an endless anthology of Vietnam’s heroic battles with invading forces.

The first European to arrive was Portuguese adventures in 1516. They were followed by other European traders who set up trading centers in Vietnam dealing in silk, spices, ivory and precious woods. By the middle of the 19th century, France was in the ascendant and was able to extend her control first to the southern part of the country making it a French colony in 1867. Central and North Vietnam along with Laos and Cambodia were made protectorates as part of French Indochina in 1887 and were brought under the control of a governor-general based in Hanoi. During the Second World War, the country was occupied by Japanese troops, though the French administration continued. By the early 20th century nascent independence movements were emerging and French rule came under increasing challenge from indigenous nationalist groups, including the Vietnamese Revolutionary Youth League founded by Ho Chi Minh. Ho Chi Minh's organization formed the nucleus that became the Vietnam Communist Party. On September 2, 1945 in the wake of Japan’s defeat, The Viet Minh leader Ho Chi Minh declared the independence of the Democratic Republic of Vietnam. Efforts to re-establish colonial rule led to a war with the French, ending in 1954. A bitter civil war continued for two more decades, ending with reunification in 1975.

Following reunification, Vietnam closed itself to the non-communist world and international relations were limited to the Soviet Union and Comecon countries. Vietnam was involved in the conflict in Cambodia in 1978 and fought a border war with China in 1979. Relations today are much improved.

**International Relations**

Since Vietnam’s initiation of **Doi moi**, the country has enjoyed increasing rapprochement with other nations. This trend accelerated with Vietnam’s withdrawal of troops from Cambodia in 1989 and is evidenced by the growing amounts of foreign investment and trade with non-communist block countries. The US embargo on trade and aid was lifted in February 1994, and steady progress is being made towards normalization of political relations between the two countries. Vietnam has signed the Vietnam-US trade Agreement, recently. Vietnam has been an observer of the GATT (General Agreement on Tariffs and Trade) since mid 1994 and full membership status of ASEAN (Association of Southeast Asian Nations) in 1998.

**Government and Political Climate.**

Vietnam is today a socialist state under the Vietnamese Communist Party. Vietnam is governed under the revised version of the 1980 constitution adopted in April 1992 to

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5 Tran Quoc Vuong “*Vietnam Modern History*” Hanoi publishing House, 1999
create an institutional framework, which endorsed the market economy as an important vehicle of growth. Under the revised constitution, the communist party is a leading force of the state and society and the National Assembly, the people’s highest representative body whose 500 members are elected by universal and direct suffrage for a five years term, is open to non-party members. It is vested with constitutional and legislative power and authority and meets twice annually to discuss state economic plans, the budget, important bills and amendments, and foreign policy. It elects the President of Vietnam, who is the head of state, and the government, which comprises the prime minister, deputy prime ministers and other ministers. The Standing Committee acts on its behalf at other times and supervises the enforcement of laws and the activities of government.

Vietnam is a one-party state with no visible opposition forces. Testament to the growing confidence in the country’s stability is the rapidly increasing level of foreign investment and funding from international financial institutions such as International Monetary Fund (IMF), the Asian Development Bank (ADB) and the World Bank (WB).

Language

Vietnamese is the official language. There are minor differences in the language spoken in the north, center and south of the country. Foreign languages in regular use include English, which in recent years has been gaining in popularity in the financial and commercial sectors. Chinese, Japanese, French and Russian are also used.

SCOPE AND SIGNIFICANCE OF THE STUDY

Like many other Asian countries, Vietnam is an agricultural country, where about 80% of the population is living in the rural areas. It is an economy based on agriculture. From a command economy, it is moving towards a market-oriented economy under socialist orientations. Vietnam has experienced many forms of colonization, civil war and war with other countries. It is since 1986 that we witness a period of stability. The study of the Economy in transition can provide a useful insight for practitioners of diplomacy and policy makers. There has been little, if any, research in this area. This is a research for an in-depth study of the management in the banking sector, encompassing related areas of economic reforms.

The current trend of research on Vietnam is largely related to economic reforms in Vietnam with little emphasis on banking reform - the core of any economic reform. The research seeks to understand and analyze the reform of management of Vietnam banking system in the transitional period from a centrally command system to a market.
oriented one and from traditional banking operations to modern banking and its impact on other sectors of the Economy and on economic growth and development. Vietnam is advancing towards joining international operations and practices in conformity with globalization process, but the process of reforms demands acceleration in the pace.

In this study, an overview of the banking system in different periods is undertaken so as to highlight its challenges and emerging trends in the reform process of management of the banking sector. The research can have some feedback on countries that have similarities in terms of political system, natural conditions and resources, human resources and lastly socio-economic conditions.

REVIEW OF LITERATURE

There is an adequate and important corpus of work in the area of economic reforms. But there is little work that links impressive performance and development of economic reforms and moreover, there is hardly any work which focuses on linking public policy, banking reforms and economic reforms. Some scholars have linked banking reform or financial restructuring with economic reforms or with economic growth and development but their focal points are not on banking reforms and financial restructuring and make only cursory references to economic reforms and to economic growth and development. Public policy has also been a relatively neglected area in the banking reforms and financial restructuring while much has been written about economic reforms.

Scholars like Alisena, Alberto 6, Vito Tanzi 7 and Ke-young Chu, Chelliah, Raja 8, Dornbush, Rudiger 9 disagree as to how economic reforms are conducted in the developing and less developed countries. They are mainly scholars from the developed countries and in the international financial governance and international trade governance, who argue that it was supporting and assisting process in the sense that these poor countries achieved the economic development and growth through foreign and international aid and loans rather than their own efforts.

6 "The Political Economy of Macro economic Stabilizations and Income Inequality": Myths and Reality, 1998
7 "Income distribution and High quality Growth", MIT Press, cam Massachusetts, 1998(eds)
8 "Economic Reforms Strategy for the next decade" Economic and Political Weekly, Vol 24, No 36, September 4-10 1999
In the Book "Money and Finance - Issues, Institutions, Policies" edited by Deena Khatkhate10, Sameekha Trust Books (1999), the scholars argue that financial crises the world over have revealed the weaknesses in the financial systems - a need for reforms. Their supervision - under the forms of completing financial assessment and independent diagnostic audits of all financial institutions and firms, issuing regulations on "special control" regime including revoking licenses of troubled banks and "special supervision" regime strengthening supervisory oversight - contribute to macro-stability. Not only is stronger supervision necessary but also the discipline of the market needs to be reinforced. Corporate governance needs to be strengthened and bankruptcy legislation made more robust. With rapid technological changes, the leader in innovation would claim the best business. Banks and financial institutions, which resist change, would, like dinosaurs, become extinct. The financial system would need to be guided by three requirements, viz, transparency, rigorous norms and appropriate incentives. The story of fiscal adjustment in developing countries is one of missed opportunities. The crisis created initiatives in right earnest, but once the immediate problems were overcome, rather than achieving fiscal consolidation, the attempt in successive budgets has been to create the illusion of achieving fiscal correction rather than really achieving it. The governments have been concealing deterioration in the fiscal balance by the way to place more emphasis on the fiscal deficit rather than more meaningful summary measures and frequently change its definition and method. Thus the claims about fiscal adjustments are illusory. Fiscal consolidation in these countries perhaps requires another crisis.

In the book "Growth and Development with reference to developing countries" A.P. Thirl Wall11 referred to the monetary policy for growth and development. He argues that monetary policy to encourage saving largely takes under the form of developing financial intermediaries which can encourage those with a productive surplus to save by taking the risk out of savers lending to investors. The development of branch banking which can tap small savings, because of the law of the large numbers, financial intermediaries are also able to borrow short and lend long, which is advantageous to lenders (by giving them liquidity) and borrow alike. Monetary policy to encourage saving may also attempt to encroach on the unorganized money market which lends mainly for consumption purposes. Paradoxically (on a classical view of the world) the development of the organized money market can both lower average interest rates in the economy at large and raise the level of saving because the unorganized market charges very high interest rates and lends mainly for consumption purposes, whereas, in the organized money market interest rates are lower and lending is more for investment purposes.


11 A.P. Thirl Wall "Growth and Development with special reference to developing countries" ELBS with Macmillan, Educational low-priced books scheme funded by British Government.
Similarly, a study by two World Bank economists - Cho and Kharkhate (1990)\(^{12}\) of the financial liberalization experiences of the five Asian Countries concludes that financial reform, whether comprehensive and sweeping or measured and gradual, does not seem to have made any significant difference to the saving and investment activities in the liberalized countries. It was believed until recently that removal of the repressive policies would boost saving. The survey in this paper of the consequences of reform does not reveal any systematic trend or pattern in regard to saving… it lends support to the conclusion that decisions to save are determined by several factors and the relationship between savings and real interest rates is at best ambiguous.

Other groups of scholars - mainly economists from third world countries - give importance to the tremendous internal efforts from their own countries i.e. internal efforts both from top government leaders and their own people. In their view most of economic reforms were established through the initiative of the government and it played an important role in promoting rapid and successful economic growth and development.

However, Economists \(^{13}\) of the former socialist countries views the success of the economic development as due to specific pattern of the economy and it can be understood only by analyzing the relationship and link between the government and the economy. Top leaders of the government are not only members of the government but also citizens of the country and there is a cooperative linkage between their own people with the government. This is the real reason behind an impressive economic development.

Different views have also emerged on the question of government policy towards economic growth and development. They consider that rapid and successful economic development is due to a favorable government policy, in which the focus and concern of the government is more emphasized on which sector of the economy: finance, trade, agriculture or industry ranks as first priority or at the same level of priority.

However, there is no controversy among scholars\(^ {14}\) on the question of success and impressive economic growth in Vietnam. By and large, scholars acknowledged and some placed important contributions of financial and banking sector to other sectors' development. Further, the financial and banking sector can maintain both capital base and national balance of payment and increasing the national reserve. The financial and capital contribution to other sector's development have been highlighted and got some


\(^{13}\) Prem Poddar "Translating Nations" Aarhus University press, Denmark, 1999

\(^{14}\) - Center for International Economics (CIE) "Non-tariff Barriers in Vietnam" Canberra and Sydney, September, 1999
- Central Institute for Economic Management (CIEM) "Vietnam Economy in 1998" Hanoi,
priority although not adequate space in the public policy. In 1997, the new government was elected in Vietnam completing the transition process of the top leadership of the country. The new government expressed their concern that recent pattern of growth has been unbalanced, leading to widening income differentials and a capital-intensive structure, consequently, the focus of the new government was on twin imperatives for the Vietnam economy:

1. Restoring the momentum of growth
2. Deepening the quality and sustainability of development.

To reach these goals, the new government has reaffirmed its commitment to deepening the process of economic renewal. Immediately upon assuming his office, Prime Minister Phan van Khai laid out priorities for the government. These consisted of a seven-fold program of action, among them, it was strengthening the financial sector.

Against this background the proposed research seeks to study banking reform and management from the perspective of economic development, close linkage with other sector reforms and linking public policy in a systematic manner.

Economic reform is essential in the context of developing and less developed countries on the way towards integrating International and global business and operation. Substantially, it has got advantages as a result of public policy from the government. It is the initiatives of the government aiming at the goals of improving living standards for the people and encouraging foreign investment through an "Open economic policy". The fact was also revealed that imperative economic development had to be more emphasized on the tremendous efforts from their own countries.

In the book "Banking in Asia: the End of Entitlement" published by John Willey & Sons (Asia) Pte. Ltd in 1999, the scholars: Dominic Casserley, Greg Gibb15 and the financial Institutions team make a detailed analysis of Asia’s banking systems that highlights the long term challenges, opportunities and changes that will shape Asian banking well into the first decade of the 21st century. The authors conclude that new challenges in Asia, and Asian markets are concerning entitlement. The Asian banking was focused on winning key businesses among corporate banking, and investment banking, in tune with global trends. Banks and investment banks competed in a series of loosely linked markets. They tried to earn banking profits from lending to and taking deposits from retail customers, large corporations, and middle market companies, from trading securities and investing for corporations, institutions and individuals, and providing private banking to the rich.

15 Dominic Casserley and Greg Gibb “Banking in Asia: the End of Entitlement”
In each of these market segments in Asia, the first decade of the 21st century will see more sophisticated customers enjoying greater choice in more open markets than existed before. As a result, the competitive environment will be more difficult for both local and multinational competitors, and indeed, it is no more easy money.

Restructuring of the banking systems in some countries are also highlighted by Dominic Casserley and Greg Gibb\(^\text{16}\) - the case of Hong Kong and Singapore, where they managed consolidation. The structure of the banking markets in Hong Kong and Singapore will change as the markets themselves evolve. Around the turn of the century, there will likely be more mergers than in all of the previous decade, and more forays by international competitors into the heart of local markets. What will emerge is probably fairly predictable. Consolidation will result in a few dominant local banks in each market plus a few specialist firms. Easier market entry will strengthen some multinational banks, but the strengthened position of the enlarged domestic banks will actually limit the scope for new multinational entrants to fresh approaches like direct online banking. So just as the regulatory mechanism in these two countries began declining, local banks started losing easy profits. By strengthening their banking system, Hong Kong and Singapore remained a base for regional business.

"Focusing for victory" is the case of Taiwan. Banking in Taiwan is challenging, but market share is by no means locked up. Faced with an unprecedented degree of choice, corporations and retail customers are becoming increasingly sophisticated and demanding. Banks, regardless of their size, are under significant pressure themselves through pricing, products and services. They must do so in a market that is becoming deregulated and made increasingly complex by the convergence of competition across product line. Traditional boundaries between deposit taking, lending, stock brokerage; investment banking and foreign and local players are whittled away by market liberalization. Generalist bank that lacks a particular product, industry or customer expertise stand to suffer most. Customer loyalty is gone, and market share is up for grabs in Taiwan. In the first decade of 21st century, Taiwan's domestic markets – which are considerably larger than the more internationalized markets of Singapore and Hong Kong – will become an important testing ground for the evolution of banking in Asia. After emerging from years of protected regulation, Taiwan's efforts to fully liberalize will provide important lessons in banking for China and Southeast Asia. Taiwan's experience will shed light on how domestic banks must focus and innovate to survive in a globally competitive market place, as well as offer insight to global competitors looking for a niche in one of Asia's dynamic domestic markets.

In the case of four Southeast Asia Countries: Thailand, Malaysia, Indonesia and the Philippines - lessons of fiscal adjustment\textsuperscript{17} and monetary policy\textsuperscript{18}, in order to capture the opportunities in the first decade of 21st century, financial institutions will have to reinvent themselves. Doing so will require many to secure new lifelines. Long-held notions of ownership and control will have to be sacrificed in exchange for capital. Moreover, the need for rapid aggressive strategic restructuring will require institutions to alter assumptions about who should lead, what product to pursue, which customers to keep or discard and, for many, which long-standing employees to retain. Restructuring done well will result in lean, highly motivated, and focused organizations. A well-managed transformation will enable Southeast Asia’s most dynamic competitors to reinvent themselves for the 21\textsuperscript{st} century. Development trends and the nature of future challenges and opportunities in these four Southeast Asia countries are similar, but banking priorities within the big four will differ. Thailand is typical of early failing and quick recovery, Malaysia is muddling through on its own terms, the Philippines is somehow rebounding and Indonesia worries about the Chinese investors’ stay. Winners in Malaysia, Thailand and the Philippines will intend to emerge through the carefully managed consolidation of several players. In Indonesia, winners will have to integrate operations from as many as 20-30 banks left in ruins by the crisis. While reinventing for the 21\textsuperscript{st} century will be difficult, many winners in Southeast Asia- domestic and foreign – may look back on the crisis as the period that launched some of their greatest opportunities.

Japan is argued by Yoshiaki Shikano\textsuperscript{19} as an example of modernizing the banking system and mobilizing the wealth. Mobilizing wealth is key to growth and modernization. The problem at the core of Japanese economy was a mountain of bad debt. The 1980s bubble economy had created a one-time US$ 1.5 trillion surge in bank debt, linked mainly to the overheated real estate market. By 1997, total debt in Japan still equaled 175 percent of GDP, compared with less than 90 percent in the U.S. and the U.K. Approximately US$ 1 trillion or 13 percent in total debt was bad. Relative to the size of the economy, Japan’s bad debt burden was at least five times larger than the U.S. savings and loan crisis of the 1980s. Still, the question in the closing years of the 20\textsuperscript{th} century remained: Would Japan make the tough decisions needed to mobilize its immense wealth, get its economy back on track, and develop a modern financial system worthy of the world’s second largest economy?

Looking ahead to next decade, the opportunities in Japan are attractive. In terms of revenue or volume, almost every financial services market will be among the two or three largest in the world. Many of these markets are likely to reap healthy profits once

\textsuperscript{17}Lessons of Fiscal Adjustment" - Selected Proceedings from World Bank Seminar, World Bank Operations Evaluation Department, 1999

\textsuperscript{18}Nor Mohamed Yakcop " Monetary Policy in Malaysia"
Binhadi " Monetary Policy in Indonesia"

\textsuperscript{19}Yoshiaki Shikano " Financial Liberalization, monetary policy and the role of Central bank in Japan" - Central Banking Course lectures -
the financial system restructures and returns on invested capital are forced to reflect the inherent risks of the businesses. The challenge is bringing through the difficult restructuring period. If banks and other participants spend enough time understanding the changing competitive requirements for success, their return over the long run will be high enough to justify their investment.

Dominic Casserley and Greg Gibb\textsuperscript{20} consider Korea as a new order in the making. It has shown itself to survive in the new world of Korean banking. Between the 1960s and the 1990s, South Korea went from being a poor agricultural country to an industrial powerhouse. Critical to this transformation was the government-controlled banking system, which channeled consumer savings into a capital base for a relatively small number of chaebol or industrial groups. Korean Exchange Bank (KEB) was among those at the forefront of the nation’s remarkable rise. KEB was an extremely strong institution with strong links to “Korea Inc”. A new order is created in the new world banking, the Korean financial institutions will need to develop a management focus on shareholder value creation (rather than volume or revenue growth), sharpen their business strategies, and demonstrate excellence in banking fundamentals such as risk management and asset-liability management. In short, Korean banks will have to cram 10-15 years of the U.S, or U.K banking evolution into just 2 or 3 years - at most - and do so in a change resistant environment with historically strong Unions.

Gan Peigen\textsuperscript{21} refers China as another example of sustaining a careful balance between boundless growth and opportunity and competition in an increasingly open and market-driven economy, and of economic and banking systems reform. The two decades of reforms started in 1978, when Deng Xiaping decided to begin reforming China, his guiding principle was simple and to the point "to get rich is glorious" Over the next 20 years, China will be buoyed by a strong and globalizing world economy that augers to support Chinese economic expansion. During this period, China’s economy grew at an average rate of 9 percent per year. The reform can be separated roughly into three phases:

- Phase 1: Opening to market forces (1978-1985)

- Phase 2: Reforms of economic structure and industrial Policies (1985-1993)

- Phase 3: Restructuring the SOEs and the financial systems (1993 Onwards)


\textsuperscript{21} John Gan Peigen "The Banking System in China" Central Banking Course lectures - Reserve Bank of India printed by Bhavan’s Associated Advertisers& Printers, Tadeo, Bombay, 1999
China’s financial markets by 2010 will be the largest in Asia. At the same time, building a profitable business will require extraordinary creativity and drive in the face of unique obstacles. For the most part, China’s banking industry will still be a regulator’s world, where, FDI inflows are greater and a large market is emerging and if China’s economic reforms during the 1980s and 1990s are a guide, future financial industry deregulation will take an incremental approach. Yet, during this period of incremental deregulation, the competitive balance will change significantly. The banks that will ultimately become major players in China will be those that understand where the long term potential of this market lies, build strong risk controls, and develop superior organizations capable of winning the most profitable businesses. By 2010, the eventual long-term winners will be clear, so the serious competitors in China will be making their moves in the first few years of the next century.

India has been shown by Dominic Casserley and Greg Gibb\(^{22}\) as a struggle for freedom or in another words, it had controlled its economy to give the way to liberalization. The four phases of banking system evolution has reflected the government’s changing priorities. The planned conscious growth and development of the banking sector commenced in 1969. Since then, the sector has evolved through three distinct phases:

The first phase, spanning all of the 1970s and 1980s, was characterized by unbridled branch expansion and asset growth. The banking sector was identified as the key instrument of economic development in 1969, the government nationalized 14 banks that year and another eight in 1980. By 1997, public sector banks accounted for 80 percent of all banking assets. In addition, policymakers imposed a strict credit-rationing approach, prescribing formula-based lending norms and high-directed credit obligations to ensure that banks channeled funds to strategic sectors.

The second phase, in the early 1990s (1992-1995), brought initial reforms aimed at building a sound banking foundation. It was an attempt to align the Indian financial system more closely with the international order; The Reserve Bank of India (RBI) launched its wave of financial reforms in 1992. These initial reforms focused on cleaning up bank balance sheets and forcing greater disclosure and transparency in accounting. Specifically, the RBI introduced unambiguous policies for asset classification, income recognition, and loan loss provisioning, coupled with mandatory compliance with Bank for International settlement (BIS) capital-adequacy standards and more stringent norms for investment valuation.

From a regional perspective, these reforms enabled to rank India near the top of the regulatory class. For some of its Southeast Asian neighbors, it took the 1997-1998 crisis to emphasize tougher introduction of loan accounting and provisioning policies

\(^{22}\) Dominic Casserley and Greg Gibb “Banking in Asia: the End of Entitlement” John Willey & Sons (Asia) Pte Ltd, 1999
that India put in place 5 years earlier. But these early reforms caused much pain for Indian banks. Indeed, 12 of the 27 public sector banks reported losses in 1993.

The third phase from 1995 onward (1995-1999), involved further reforms, mostly geared to enhancing competition. Financial reform continued, although the changes were less dramatic. The focus of reform shifted to promoting competition and market pricing mechanisms. While the first wave of reforms had a one time impact on banks' balance sheets, the latter wave will have a more fundamental effect on their business strategies. RBI allowed banks to compete freely for loan customers, doing away with the archaic consortium system that forced borrowers to parcel out business among their existing set of bankers. The central bank also freed interest rates across virtually the entire maturity spectrum, with rates now only influenced, rather than determined, by the RBI's market signals. Nine new private banks were permitted to commence operations in this period. Windows for foreign capital were opened, and Indian banks thus faced a whole new range of competitors. The result was a sharp decline in margins in most traditional product market segments by 1997.

Despite this, banks managed to post higher profits than in the past due to volume expansion and fewer incremental problem loans. Of the eight public sector banks that reported net losses in 1995, only three remained in the red by 1997. As a group, the public sector banks more than doubled their net profit ratio, from 0.25 percent of total assets in 1995 to 0.56 percent in 1997. Most of the recapitalized banks managed to turn the corner, and some even repaid the government its equity. Four more public sector banks made their first public stock offerings in this period, further lessening the sector's dependence on government capital.

As the 1990s drew to a close, Indian banks were on the verge of entering a fourth phase, one likely to be marked by consolidation (2000-2010). Indian banks face tough times in the first decade of the 21st century. Assuming the government can muster sufficient political will, the reform process will continue, forcing banks to achieve higher standards of disclosure and transparency, apply tighter loan loss-provisioning norms, and attain higher capital-to-risk-asset ratios. Indeed, the RBI announced in its 1998 credit policy that banks would have to increase their capital ratios from 8 to 9 percent and adopt tighter provisioning norms for non-performing assets in the year 2000.

Given the government’s high stake in the banking system, consolidation is unlikely to be a completely market-driven process. It will require Government consensus on the need for and benefits of consolidation, as the political will to take the process forward. Regulators are likely to move towards building such a consensus, though the pace of change will hinge on the political leadership's priorities.
In an informal economic report on Vietnam, the World Bank consultative group meeting held in Hanoi, December 14-15, 1999 reported that although Vietnam largely remains a largely agrarian society, it could benefit greatly from the East Asian economic recovery. However, it has not yet implemented the policy changes required as per its suggestions. From a command economy, Vietnam is advancing towards a market-oriented economy under socialist orientations and Vietnam has also experienced many discontinuities in the form of colonization, civil war and war with other countries. The focus and concern of the government are: the implication of slower growth, poverty reduction and social equity. The government policy is to gain advantages of support and assistance from international community and at the same time makes use of its own material and manpower to join rapidly in international business operations. That’s why “Doi moi” (or renovation) was introduced in 1986, specific structural reforms designed to promote the transformation of Vietnam from a centrally planned to a market-oriented economy. This includes: reorganizing collective agriculture into household holdings; granting greater autonomy to state enterprises; deregulating prices; reducing the budget deficit through tax and expenditure reforms; tighter monetary policy to control inflation; unifying the official and market exchange rates; deregulating foreign investment laws; and encouraging the parallel development of the private sector.

This policy is symbolized in the Vietnam’s development Agenda delivered by Prime Minister Phan Van Khai in his speech at the opening session of the national assembly in November 1997, consisted of a seven-fold program of actions:

- Improving macroeconomic stability and competitiveness
- Strengthening the financial sector
- Reforming state owned enterprises
- Raising productivity through infrastructure development
- Accelerating rural development and increasing environmental protection
- Investing in people and promoting social equity
- Improving public administration, transparency and participation.

Of these goals, strengthening the financial sector is the first priority.

QUESTIONS TO BE PROBED

The study seeks to answer the following:

1. To what extent the banking reform in Vietnam is aimed:

(a) To strengthen and develop other sectors of the economy and make contribution to the reform of other sectors of the economy?
(b) To provide financial and capital bases for development of other sectors?
(c) To maintain national balance of payments?
(d) To increase national reserves domestically and internationally?

2. To what extent is banking emerging as a public policy contributing towards Development and growth?

3. Which areas of banking operations and practices demand first priorities and what is the extent of changes in the style of management?

4. Given the significance of reform of the management of the banking sector to national economic growth to what extent is the public policy in Vietnam likely to address banking system and development issues directly and positively.

RESEARCH DESIGN AND METHODS

It never happens that always all evidence point in a single direction and therefore it is always arguable whether the result of an investigation is "complete" or final. Thus what is attempted in this study is not a complete knowledge of reality but an investigation that provides a clear approximation to it. To make the research more authentic the following research methods had been conducted:

- A survey of literature and an effort to scholarly debate in the area. The statistics can be used where required to generalize the research findings and verifiability, which assumes the central importance of evidence to substitute the hypothesis laid out.

- A field study was conducted for:

Collecting primary and secondary data from financial institutions through Annual Reports of the State Bank of Vietnam, Ministry of Finance, four state owned commercial banks, fifty one Joint Stock Commercial banks, four joint venture banks and ten branches of foreign banks, credit co-operatives and financial companies. Vietnam General statistical office, IMF, WB, ADB, IFC offices in Vietnam etc. were also consulted.

- Interviewing policy makers, Bank officials and Bank staff.

- Survey research sampling: Simple random sampling, systematic sampling and area sampling can be used to estimate the parameters of a field of interest, and

- Case studies including site visit observation.
These methods have common characteristics of helping to reduce uncertainty in research and thus these methods were applied wherever necessary and to the extent feasible.

Data sources

It is important to mention here the fact that the paucity of adequate, updated or systematic data sets on both sector economy and banking sector of Vietnam Complicating the task is the reliability of updated sets. This problem arises more particularly in regard to research with little emphasis on banking reform. Updated data inadequacy has put heavy limitations on arrival of any suggestive conclusions. Compounding the updated data inadequacy is the provision of data sets of last two years reference, which would state the current status disregarding the actual change that has taken place over the years. Therefore, any such effort, which provides current account with base year, would give us the precise magnitude of developmental change during a given period of time, particularly in the banking operations.

As mentioned above, the following are the main sources from which data are collected.

2. Summary of World Bank (WB), International Financial corporation (IFC), International Monetary Fund (IMF), Asian Development Bank (ADB), various issues from 1986 to present.
3. Annual Reports of the SBV, Vietnam Commercial banks, covering various years from 1986 to the present.

Period of Study

The study aims to capture developmental reform effort of management in the banking sector and its impacts on the other economic reforms during and post "renewal" process. Particular focus has been laid out on Vietnam reform and banking reform from 1986 to 2001 with a relative emphasis on pre" renewal" process encompassed in the study for the purpose of a comparative study of a command system with market oriented one.