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CASE STUDY

Banks Level the Playing Field

Regulatory reforms help Vietnam develop a modern, dynamic banking sector

Photo: STAR

Bankers attended a seminar on the draft decree on the operation of foreign banks in Vietnam.

Vietnam adopted major amendments to the Law on Credit Institutions in June 2004 that will establish for the first time a level playing field for all commercial banking activities in Vietnam.

Challenge

As in other transitional economies, Vietnam's banking sector is underdeveloped and dominated by state-owned institutions with weak risk-management and supervision techniques.

Meanwhile, there is a rising demand to expand investment in infrastructure, industrial plants and human capital. More dynamic formal financial intermediation is welcome, but that requires modern improvements be made to the banking sector's legal guidelines. Foreign banks, in particular, face discriminatory restrictions on mobilizing local currency and providing certain services, even though the U.S.-Vietnam Bilateral Trade Agreement — and the entire reform process — requires that foreign banks and commercial banks work on a level playing field.

Initiative

At the request of Vietnam's State Bank and National Assembly, USAID is supporting major reforms in the banking sector. In June 2004, USAID helped Vietnam draft and adopt major amendments to the Law on Credit Institutions, which establish for the first time equal opportunities for all commercial banking activities in Vietnam. The amended law strengthens prudential and capital adequacy requirements, requires that state-owned commercial banks meet the same standards as private commercial banks, eliminates language favoring state leadership, and allows foreign banks to set up 100-percent foreign-owned subsidiaries.

Results

Vietnam's significant legal reforms are helping it develop a modern, dynamic financial system that will support private sector expansion and integration into the global economy. In 2005, USAID is supporting the development of strong regulations that will put the banking law reforms into force, especially those required to comply with the Bilateral Trade Agreement and World Trade Organization. For instance, Vietnam is expected to permit 100-percent foreign-owned bank subsidiaries to be established by the end of 2005 — five years earlier than the Bilateral Trade Agreement requires.