

# Vietnam's Financial System

~from the perspective of financial  
intermediary functioning~

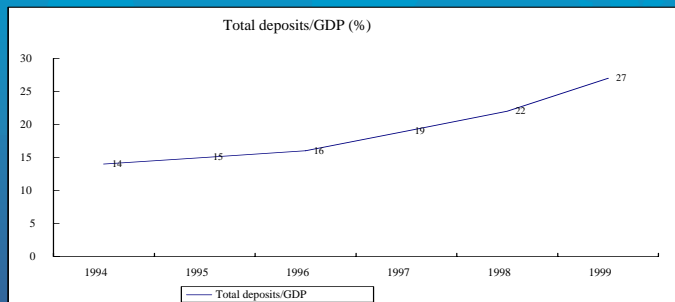
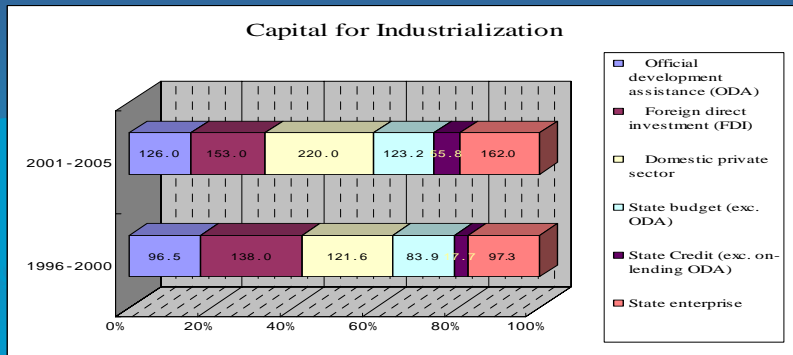
Nguyen Thi Hanh

Sasakawa Peace Foundation (SPF)

## Why financial system?

Basic observations:

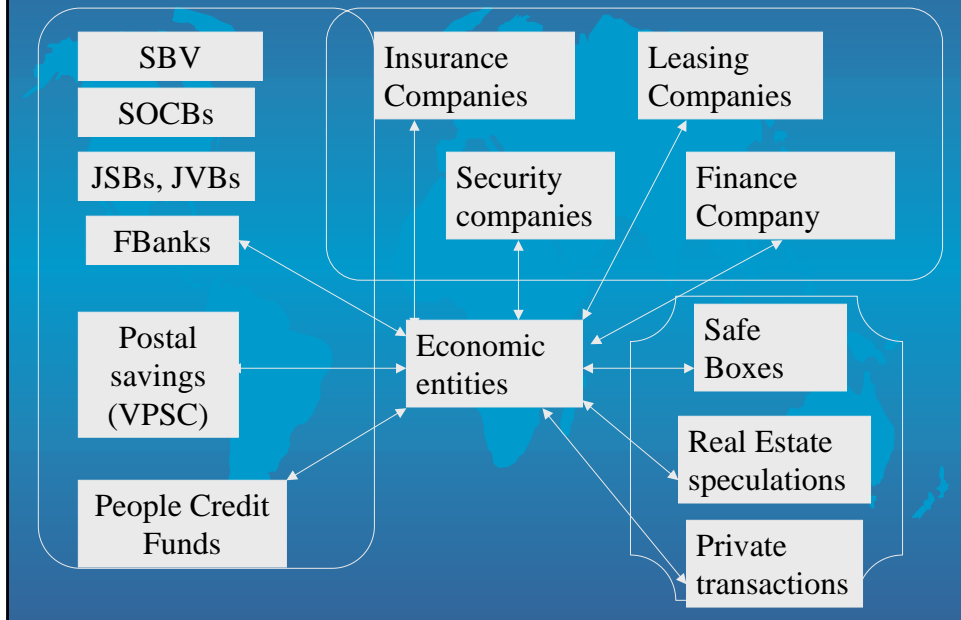
- Industrialization depends 66% on domestic capital  
=> pivotal role in capital mobilization
- Skeptical on formal financial intermediaries:
  - persistent speculations on lands
  - financial deepening: loan/GDP, deposits/GDP  
(international comparison)
  - inaccessibility for farmers
  - huge bad debts etc...



## Outline

- A bird's-eye view
  - \_ Financial institutions
  - \_ Shares in financial market
  - \_ Overall features
- Financial Intermediary Functioning
  - \_ Resource mobilization of banks
  - \_ Resource allocation
  - \_ Problems remained
- Directions for further development
  - \_ From the long-term perspective of system design

# Financial Institutions



## Overall features

- Dominance of Banking sector & SOCBs
  - Share in Deposits
  - Share in Credits
- Overall features:
  - Poor Capital and Reserve
  - Group lending & related party-lending
  - Poor risk management
  - Improper Accounting Practices and Transparency
  - Inadequate Managerial skills

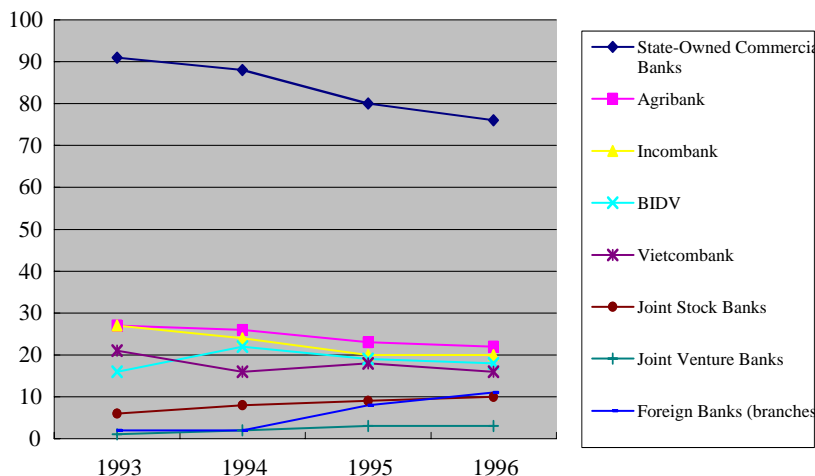
# Resource Mobilization (1)

- Dominance of SOCBs, regardless of interest rates
  - Big scale => wide networks of branches
  - Advantage in credibility <= government's bailout, traditional clients
  - JSBs, JVBs: lack of networks, traditional clients
    - => weak competitiveness => credit collapses
  - Foreign bank branches: restrictions in domestic transactions
- VPSCs & people credit funds: short of data, but seem promising



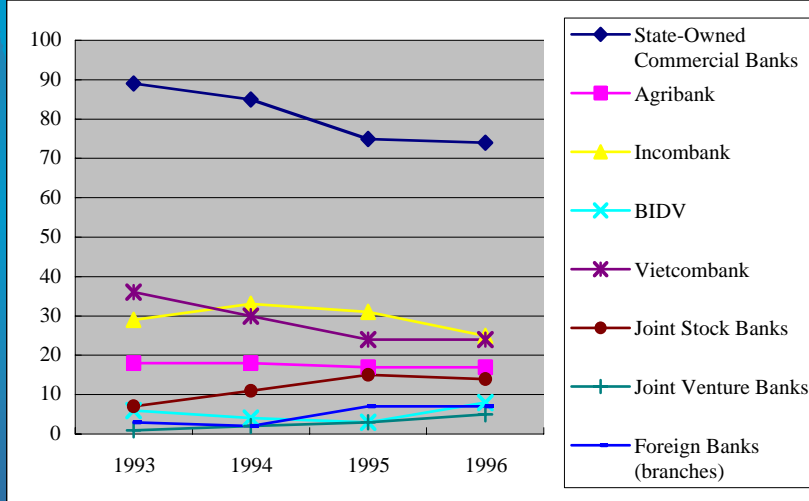
## Share in deposits

Share in deposits among financial institut:





## Share in Credit among Financial Institutions

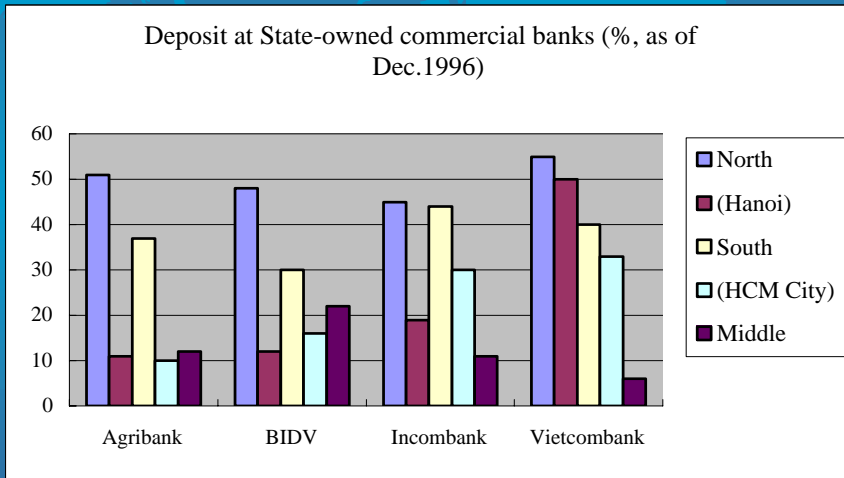


## Resource Mobilization (2)

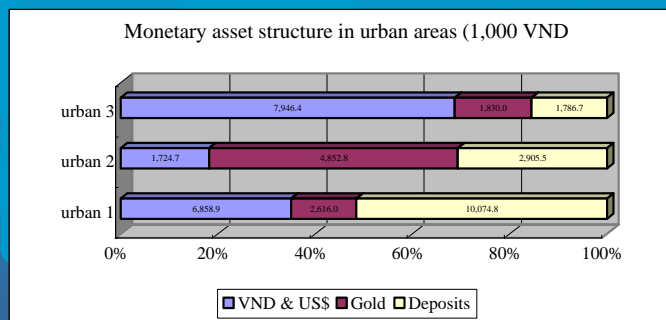
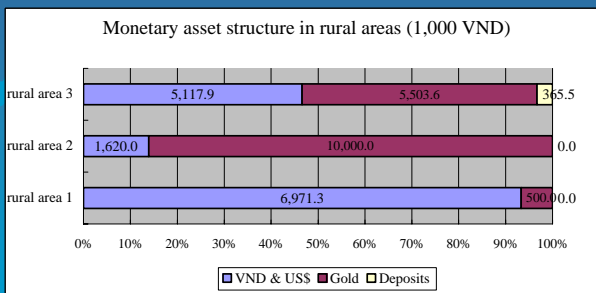
- Low fund mobilization from rural areas
  - low accessibility to banks
  - (low savings)
- Role division among SOCBs
  - Agribank - 71% from individuals <= wide networks in rural;
  - BIDV - 87% from private companies & others;



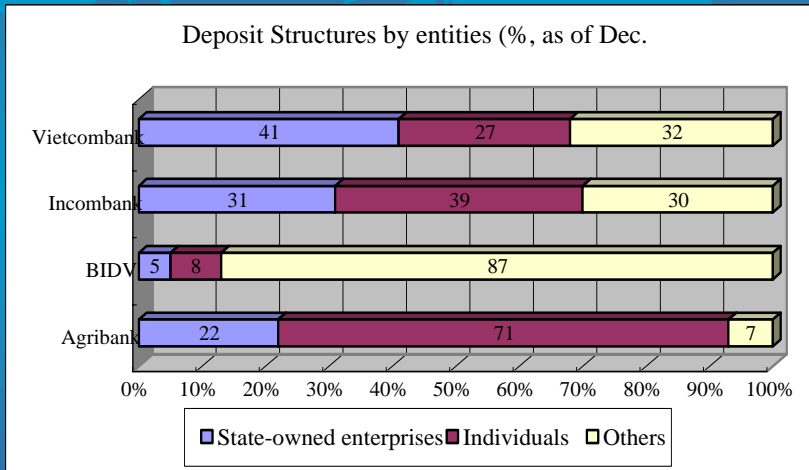
# Low mobilization at rural (1)



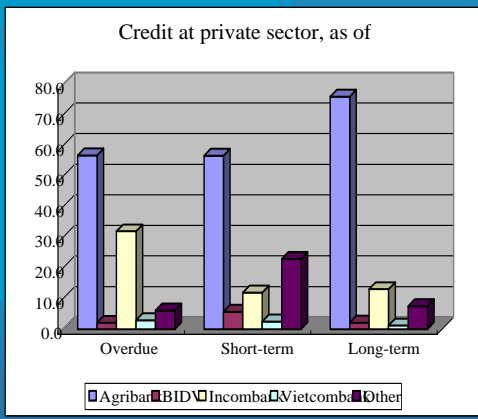
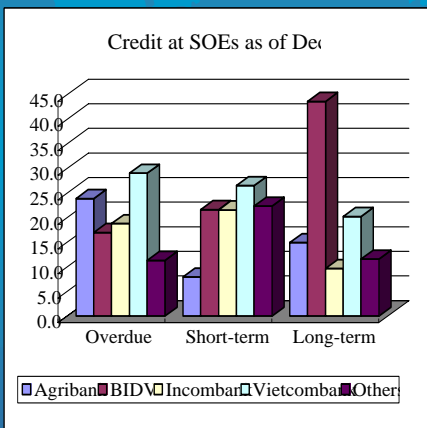
# Low mobilization at rural (2)



# SOCBs comparison (1)



# SOCBs comparison (2)



# Resource Mobilization (3)

~Household saving practices

- Savings mainly flow into Houses and Lands
- Deposits prevails traditional means
- Traditional loans bigger where deposit equal 0.

## Implications:

- ==> Accessibility does matter
- ==> minimum deposit size seems to be constraint of deposits for low income households
- Land price policy does matter



**Table 11-1 Households With/Without Deposits**

Unit: 1000VND

	With Deposits		Without Deposits	
Number of Households	71	3.97%	1,717	96.03%
Current Income	26,366		14,005	
Current Expenditure	17,431		10,055	
Current Savings	8,936		3,951	
Investment in real assets	11,363	4.59%	4,061	4.45%
assets	-1945	-0.79%	169	0.19%
Currency (VND)	2,152	0.87%	2,510	2.75%
Dollar (\$1=VND11,000)	310	0.13%	46	0.05%
Gold (1 Chi=VND 500,000)	2,595	1.05%	1,856	2.04%
<b>institutions</b>	<b>19,432</b>	<b>7.85%</b>	<b>0</b>	<b>0.00%</b>
Loans to ho/hui	8	0.00%	103	0.11%
Personal loans without interest	90	0.04%	157	0.17%
Personal loans with interest	0	0.00%	222	0.24%
Accounts receivable	110	0.04%	319	0.35%
Durable consumption good	16,649	6.73%	5,470	6.00%
Durable equipment	1,330	0.54%	2,213	2.43%
House and Land	195,349	78.95%	74,062	81.22%
<b>Total Assets</b>	<b>247,443</b>	<b>100.00%</b>	<b>91,188</b>	<b>100.00%</b>
institutions	35	5.07%	736	33.41%
Debts to ho/hui	0	0.00%	50	2.27%
Personal Debts without interest	602	87.25%	631	28.64%
Personal Debts with interest	1	0.14%	232	10.53%
Accounts payable	52	7.54%	308	13.98%
Debts to government	0	0.00%	93	4.22%
Debts to money lenders	0	0.00%	153	6.95%
<b>Total Liabilities</b>	<b>690</b>	<b>100%</b>	<b>2,203</b>	<b>100.00%</b>
Net Worth	246,753		88,985	

Note: Data are results of sample investigation

Source: *Study on Economic Development Policy in the Transition Toward a Market-oriented Economy in Viet Nam* (Phase 2), MPI/JICA, 1998, p.138



## Implications

- Policies to improve accessibility => encouraging of banking franchise
- Banking policies to encourage banks in attracting small depositors
- Models in mobilizing dispersed small savings:
  - China: strengthening PCFs
  - Japan: strengthening postal savings

## Resource Allocation (1)

- High proportion of short-term loans
  - lack of lending skills (risk managements, maturity transformation...)
  - despite of comparatively high reserve rates

## Resource Allocation (2)

- Huge NPLs
  - total bad debts/credit balance: 13.7% in 1999
  - 1/3 to 40% of total loans: foreign currency-based => huge risk in connect with exchange rate
  - SOEs hold big share => SOE reforms (securitizations)
  - PCFs- huge bad debts in 1990 (73%), but gradually reformed and improved

## Resource Allocation (3)

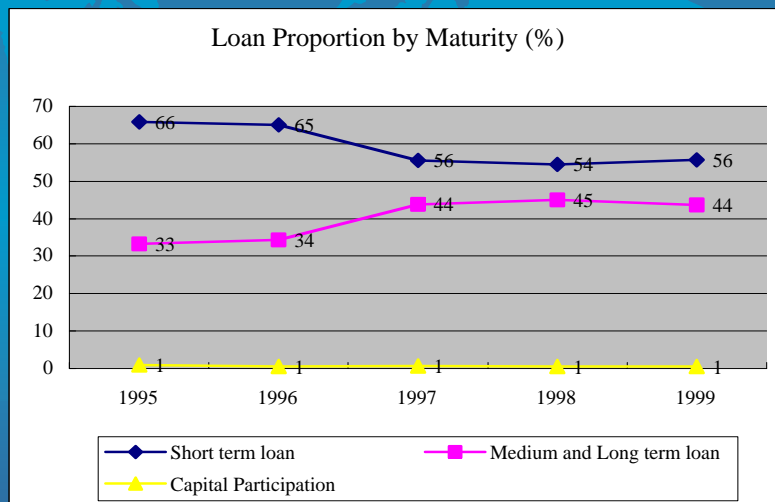
- Loans in favor of state-own sector
  - SOEs: 52% of total loans + FDI => only apx. 50% of GDP
  - loans to private sector: mainly to farm households
  - capital shortage - biggest obstacles for private companies <= lack of bailout; high risk; mortgage policies (land use right etc.); lack of legal documents; high transaction costs (for banks)
  - ==> corruptions; private borrowers to pay 6.5% kickback to “brokers”

# Implications

- Lack of lending skills, corruptions  
=> Need more transparency and competitiveness, through gradual privatization & foreign ownership
- SOE reform (securitization) to help resolve NPL issue
- Legal environment to encourage private lending; level playing field

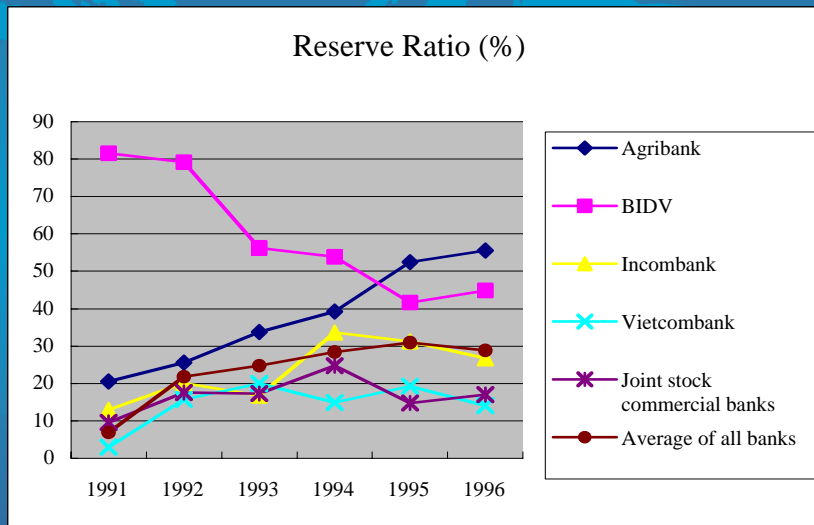


## Loans by Maturity

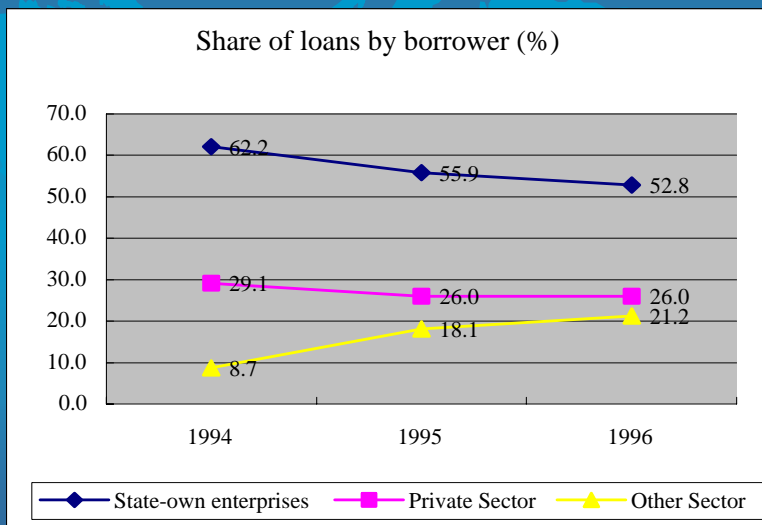




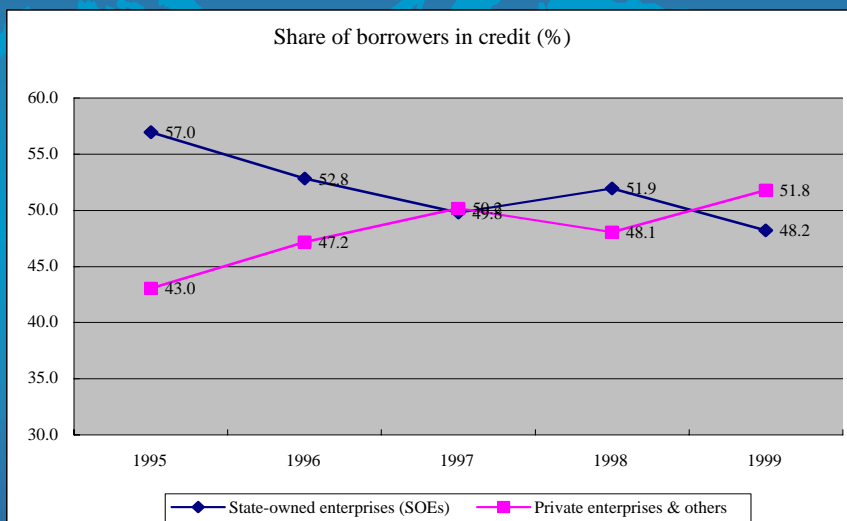
# Reserve Ratios



# Share by borrowers (1)



## Share by borrowers (2)



## Capital for Private Companies

**Table 16 Capital sources at start up establishing of private enterprises (In rural urban areas)**

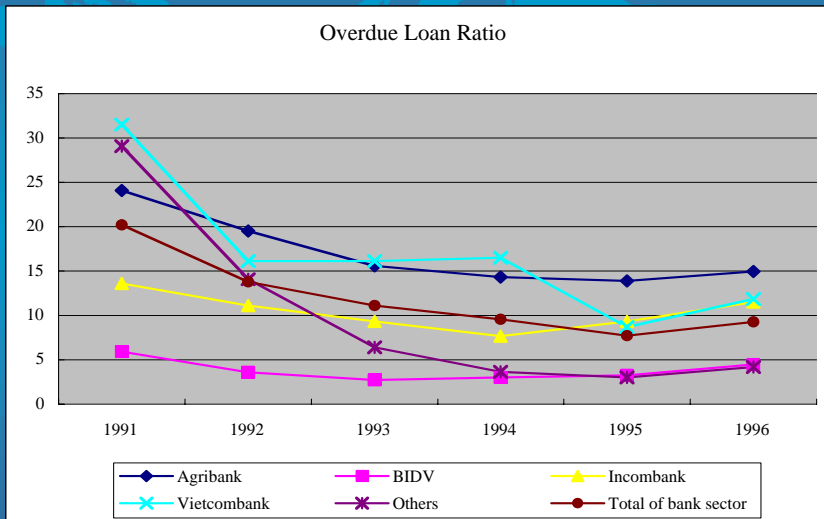
Unit: %

	Urban area	Rural area
<b>Own capital</b>	<b>91.2</b>	<b>90.3</b>
Non interest loan	3.1	3.8
<b>Banks credit</b>	<b>0.8</b>	<b>1.9</b>
Credit cooperatives	0.0	1.0
Local authorities	0.0	0.3
Worker contribution	2.2	0.1
Borrowing from individuals	1.3	2.3
Others	1.5	0.3

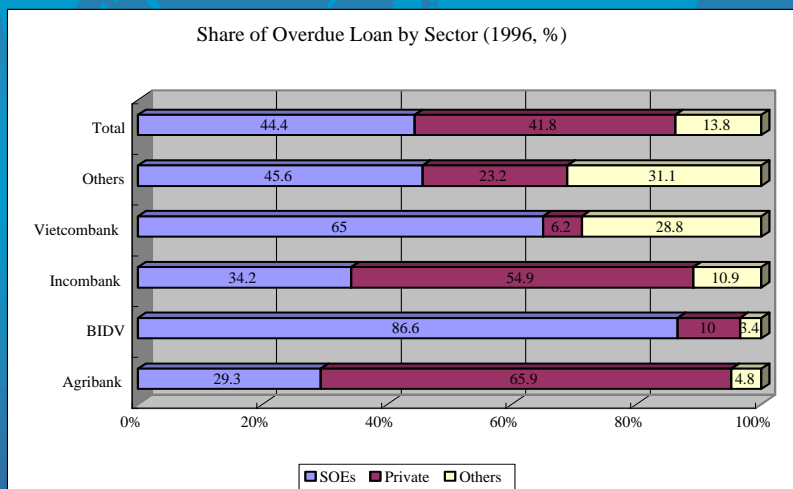
Source: *Study on Economic Development Policy in the Transition Toward a Market Economy in Viet Nam* (Phase 3), MPI/JICA, 2001, p.56



## Overdue Loans (1)



## Overdue Loans (2)





## Interest rate policies

- To be an instrument to encourage banking franchise <= “financial restraint model” (Hellman, Murdock, Stiglitz)  
Ex: deposit rate ceiling & lending rate floor
  - Current interest policies to have adverse effects:
    - Ceiling on loan interest rate
    - maximum spread between lending & deposit rates
- => hard profit earning for JSBs, JVBs (which have to compete fiercely with SOCBs)
- => unsound competition causes deeper financial troubles when law enforceability limited

## Interest rates

Implications:

- To revise the above-mentioned interest policy combination
- Ceiling on loan rate to be abolished in 2002

**Table 21** Ceiling interest rate on loans

Unit: % monthly

Areas	Jan1999	Feb99	Jun.99	Aug99	Sep1999	Oct1999
Urban area	1.25	1.15	1.15	1.05	0.95	0.85
Rural area	1.25	1.25	1.15	1.05	1.05	1.00
Rural joint-stock co	1.25	1.25	1.15	1.15	1.15	1.15
People credit fund	1.50	1.50	1.50	1.50	1.50	1.50

Source: *Study on Economic Development Policy in the Transition To Economy in Viet Nam* (Phase 3), MPD, 2000, p. 75

## Directions for further development ~ system design

- Banks (Indirect finance) to continue playing dominant role
  - two types of financial system & corporate governance issues
  - prerequisites in transitional economies
  - advantage of “path dependence” approach

## Ownership Structure

- While the sequence remains to be complicated issue, Gradual Privatization & Foreign Ownership to be inevitable
  - foreign ownership => more efficiency, competitiveness with technology transfer
  - financial market to be open to foreign ownership in few years (following the BTA with the US, WTO accession)



## Other issues

- System of commercial banks and long-term investment banks in tandem
  - capital market under-developed
  - lacks of banking skills in maturity transformation
- Security and Bond Market continuing to be developed, of course
- Government to continue to play big role in the system design

THANK YOU !!



Reference (1)

## 金融制度構築の理論的検証

### 金融システムの分類:

- 証券市場中心の金融システム（通称アングロ・アメリカンシステム）
- 銀行中心の金融システム（ドイツ・日本型金融システム）

	U.S	U.K	日本	フランス	ドイツ
証券市場	中心的	中心的		比較的重要でない	重要でない
銀行	競争度合い				
外部企業統治	敵対的買収	敵対的買収	メインバンク		Haus-bank



Reference (2)

## 移行経済に特有な金融問題

- 証券・資本市場が元々不存在
- 市場が不完全
- 経済取引インフラの不備と著しい情報非対称性問題
- 金融取引に関する人的資源欠如
- 低い組織的能力
- 結果としての著しいプリンシパル・エージェント問題

Reference (3)

## コーポレート・ガバナンスー 銀行監視への期待と疑問

### 銀行監視への期待

- 敵対的買収の場合のフリーライダー問題の解決
- モニタリング費用の重複問題の解決
- 機関投資家によるフリーライダー問題の解決

### 銀行監視への疑問

- 競争がファストベストだが、激しい競争はシステムの不安定性を孕む
- “Who monitors the monitor?”問題