AN OUTLINE OF THE VIETNAMESE FINANCIAL MARKET

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I. SITUATION

In the 1990s when the market economy started to develop in Vietnam, a financial market and its instruments came into being and developed.

1. Money market:

After two banking ordinances were issued in 1990, the 2- level banking system took shape and allowed banking institutions to flourish. At the same time, sub-markets of the money market are also operational:

- Market for short-term credit: This is the traditional market for banking services in which banks mobilize deposits and supply short-term loans in various forms.

- Inter-bank market for domestic currency: This market was established in 1993 by the Decision 136/QĐ-NH2 to smooth the flow of capital between commercial banks before they resort to the SBV.

- Inter-bank market for foreign exchange: This market came into being in November 1994 after the Decision 203/QĐ-NH13 to regulate the supply and demand of capital in foreign exchange between commercial banks, thereby establishing the market exchange rate used for determining the official rate.

- Market for SBV bills serves as a basis for open market operations by the SBV.

- Market for T-bills.

The financial market provides the SBV with instruments for implementing the monetary policy and smoothing the flow of capital, especially short-term one, between economic sectors.

2. Capital market

- Market for long-term credit: In the past few years, the number and size of commercial banks became bigger (in 1990 there were only four state-owned banks for the whole economy, and in 1999 there were five state-owned commercial banks; 48 joint stock banks, four joint venture banks and 103 branches and rep offices of foreign banks), and the policy on interest rate was adjusted to the market mechanism. These factors allowed commercial banks to mobilize more and more long-term deposits. Many banks could turn short-term deposit into long-term loans because the market for long-term credit is well connected with the market for short-term one.

- Market for financial leasing service was formed in 1995 by the Decision 64/CP dated Oct. 9, 1995. Businesspersons who find it hard to secure bank loans because of complicated procedures can get help from finance companies to buy new machinery and technologies.

- Stock market: The legal infrastructure for the stock market has been developed by degrees. Many law documents have been issued to regulate operations of this market:

+ Decree 72 dated June 8, 1992 on issues of government bonds;

+ Decree 120 dated Sep. 17, 1994 on issues of bonds and shares by state-owned companies;

+ Decree 23 CP dated March 22, 1995 on issues of bonds in foreign markets;

+ Decree 48 dated July 11, 1998 on stocks and stock market;

+ Decision 127/1998 dated July 11, 1998 to establish the Stock Exchange Center;

+ Decree 01/2000 dated Jan. 13, 2000 on issues of government bonds.

We could see that in the past few years, the capital market in Vietnam involved mainly the supply of credit through banks. In many companies, from 60% to 70% of their working capital is from bank loans. Commercial banks must try their best to meet the demand for loans that will be greater in the coming years. At present, one of their difficulties is the high proportion of overdue debts. Therefore the stock market is one of measures to help mobilize idle money from the public.

Besides the capital market, other instruments for mobilizing long- and medium-term capital also made their appearance: government bonds, company shares and bonds, bank bonds, etc. These instruments also encourage small savers to turn their savings into investments.

3. Shortcomings

The financial market, however, has revealed many shortcomings:

(1) Commodities trade in the stock market are scarce and less diverse:

The privatization of state companies is carried out too slowly. Up to June 2002, this program included some 900 state companies only and most of them are of small scale. Only 10% of joint stock companies are of medium scale (with capital of VND10 billion or more) but they are reluctant to engage in the stock market because they see no benefits in doing so. On the stock markets, there are stocks from 19 companies and two kinds of bonds (issued by the government and Bank for Investment and Development) to be traded. Total value of listed securities is some VND4,000 billion equaling 0.37% of the GDP. In the past two years of operation (up to June 30, 2002), 322 trading sessions were held and the 41.3 million stocks and 841,000 bonds with total value of VND1,673 billion were traded, or sme VND5.2 billion a session.

Besides shares and stocks, all bonds are of short term. There is no bond of long term (over five years).

Besides T-bills and SBV bonds, many other negotiable instruments need to be standardized before being traded on the market. That is why Vietnam has no secondary market for valued documents

(2) The financial market, because of its small size, fails to accumulate sources of capital:

After its establishment in 1993 the inter-bank market for domestic currency hasn't been active enough. Main activity in this market is the one-way supply of domestic currency from the SBV to joint stock commercial and joint venture banks. The market lacks an organizer. The interest rate is fixed by the SBV only and fails to reflect the supply-demand relation. In addition, there is no close relation between the SBV and commercial banks because monetary instruments aren't flexible enough with the result that policies introduced by the SBV produced no remarkable effects on the market.

The inter-bank market for foreign exchange came into operation in 1994 and its volume of trading rose steadily, from an average of US$58 million a month in 1997 to some 217 million a month in 1999 and over US$1 billion in 2001. However, imbalance between supply and demand is very common because the public tend to withdraw foreign exchange when the dollar rises against other hard currencies and the SBV foreign exchange reserve is small.

The volume of deposit mobilized by banks is still small, equaling only 34% of the GDP in 1998 (this figure is 117% in China; and 91% in Thailand and Indonesia.)

The stock market is still at its pilot stage and hasn't become a reliable source of capital for both the Government and companies. It fails to attract leading companies in each industry. Main activity there is to trade in listed stocks in small quantities: In the past two years, only two listed companies issued new stocks (Hải Phòng Paper: one million, and REE 7.5 million.) Activities in the stock market show that there is no close relation between the primary and secondary markets, and between the stock market and privatization program.

There is no interaction between the money and stock markets when mobilizing the capital. Interest rates offered differ over stocks because of the government intervention. SBV open market operations have no effect on the interest rate offered by the stock market.

Professional financial institutions needed for development of the financial market are still lacking.

II. MEASURES TO PERFECT AND DEVELOP THE FINANCIAL MARKET

The following are some principal measures we suggest to beef up the financial market. More details about these measures will be presented in another paper.

1. Diversifying listed securities

The legal infrastructure must be perfected and many laws must be made in order to ensure lawful trade in securities of all kinds.

2. Beefing up the financial market

a. Money market:

- Restructuring state-owned commercial banks and forcing them to operate under the market mechanism and allowing foreign banks to trade in the domestic currency.
- The SBV must use instruments to implement the monetary policy instead of intervening in commercial banks' operation and day-to-day business.
- The SBV must work out plans to connect inter-bank markets for foreign exchange and domestic currency to help commercial banks secure necessary funds in any currencies on time.

b. Capital market:

- Tax incentive and better and more diverse banking services are two effective ways to encourage the public to have their money handled by banks, which helps banks increase their funds at low cost.
- Banks must offer the same lending policy to all sectors. Legal framework for lending, mortgaging and land using rights must be more transparent in order to allow the private sector to get easier access to formal loans.
- The banking authorities must adopt policies to support rural banks with a view to helping them supply more credits to small and medium businesses in the agricultural sector.
- The Government had better allow all sectors to engage in the finance leasing market and give tax incentives to finance companies operating in rural areas
- The privatization program must be accelerated. The Government should persuade leading corporations enjoying monopoly to issue bonds or shares through the stock market, and establish the OTC market to attract small and medium companies.■