Development of Financial Companies in Vietnam

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In Vietnam's economic renovation, financial and monetary activities have faced a lot of improvements in the trend of market mechanism, door opening, global integration and satisfaction of increasing capital demand. In that process, besides the banking system, non-banking financial institutions (including financial companies, insurance companies, leasing companies, stock companies, investment fund management companies, etc.) have been established and developed abundantly and significantly.

There are many reasons for the appearance of financial companies. However, it is mainly due to the requirement for various financial and monetary services in economic development that cannot be satisfied by the banking system or restricted by regulations of the Banking Law. Financial companies are regarded as non-banking financial institutions which are affected by separate regulations or law.

Financial companies are differently interpreted in accordance with each country's policy. Their performance extension depends on growth of the financial market. Then, their professional operations and organizational structures are more enhanced. Nevertheless, in the world financial companies have common features: professional business in the financial market; independent accounting; permission for registration; specifically defined operations; prohibition against current or short-term deposit accounts and payment services. They are allowed to mobilize capital by opening long-term deposit accounts, issuing bonds and taking bank loans. Their mobilized capital is used for providing short, mid and long-term loans and services of factoring or leasing. Financial companies are organized into independent entities, affiliates of commercial banks or conglomerates. As compared to commercial banks, financial companies are not strictly regulated by the central bank, so they can offer more attractive credit facilities to customers. Over the past years, financial companies have made remarkable changes into larger institutions with diversified credit facilities from small loans to huge loans and leasing funds for sizable corporations.

In its renovation process, Vietnam's banking system has built a system of non-banking financial intermediaries with various forms. Financial companies are one of those forms and already brought into play. Their robust development in terms of scale and scope of activities is one of conspicuous signals showing the evolution of Vietnam's financial market in the global trend.

I. Facts of Vietnam's current financial companies

Vietnam currently has nine financial companies including seven affiliated to Vietnam's key corporations of petroleum, rubber, clothing, post and telecommunications, one of the Vietnam Prudential financial group and one of Vietnam Socít Generale. Nevertheless, the two first comers are Saigon Financial Company and Seaprodex Financial Company which were licensed by the State Bank on September 12, 1991. After 12 years of operation, Saigon Financial Company was merged with Đà Nẵng Rural Areas Joint Stock Bank to establish Việt Bank. The Seaprodex were disbanded before expiry.

So far Vietnamese financial companies can be counted on the fingers of two hands while this figure is tens or hundreds of times in developed countries and they are very profitable. It is a hot debate that banks are dominating in the financial market, which hinder development opportunities for non-banking institutions. Nevertheless, the evidence shows there are still segments inaccessible to banks or causing a lot of risks in many countries even though however strong their banking system is. It is just the destination where financial companies come. As a result, if financial companies want to extend their business, they must make the best use of their advantages and strategic plans and finally an effective legal framework is required.

In fact from 2002 until now, financial companies have been given favorable conditions for growth since Decree 79/2002/NĐ-CP was promulgated. It is obviously that more financial companies will be brought into operation because Vietnam's financial market has great potentiality for development. Until the end of 2007, there were 30 potential institutions in the list of waiting for license from the Vietnam State Bank besides nine operational companies.

1. Source of capital

As regulated, financial companies are allowed to mobilize capital from following sources: individuals and organizations, debts and soft loans, and trust funds. Most of Vietnam's financial companies are affiliated to corporations, so their mother company's funds always take a lion share, more than 50% of total working capital. Therefore they can invest these funds in major projects of their mother company. In addition, financial companies also receive capital from foreign partners.

Financial companies' loan capital remains meager, accounting for 10% to 15% of total capital. Loans are mainly in Vietnamese currency from local commercial banks. Several financial companies are licensed to make transactions in foreign currency, so they can borrow foreign debts. Financial companies' lending interest rates may be higher because their money comes from other credit institutions.

Financial companies' capability of capital mobilization has been significantly improved in recent years. However, in terms of market shares, their business performance remains modest, representing 0.12% of total credit institutions' mobilized capital in 2006, and up to 0.16% in 2007. This is a common sense because commercial banks have more advantages in capital attraction, for example, their nationwide network of branches. Besides, people get used to depositing their money in banks rather than non-banking financial institutions.

Table 1: Capital structure of financial companies (until the end of 2007) Unit: VNDbil.

Indicator	Absolute number	Share
Charter capital	5,883	15.87%
Mobilized capital	6,639	17.91%
Loan capital	4,723	12.74%
Trust funds	19,825	53.48%
Total	37,070	100%

Source: Vietnam State Bank

2. Major activities of financial companies

* Lending activities

In Vietnam financial companies' lending activities remain much restricted while foreign counterparts commonly finance projects in the forms of investment or mid and long-term loans as well as finance leasing, operation leasing, stock trading, guarantee...

As for financial companies affiliated to the corporation, their main function is to give financial aids to other subsidiaries, so these companies fully utilize capital sources for lending, mainly mid-and long-term credit for major projects of the mother company. Their borrowers are mainly state-owned enterprises. This is obvious because most of the state corporation's affiliates are also state companies, except a few are equitized. For example, the Petrovietnam Joint Stock Finance Corporation has financed some 100 projects, including huge ones such as building PhúMỹ-HCMC gas pipeline, Cà Mau Electricity and Gas Complex, etc. It has offered mid- and long-term loans to projects of Cavico, new urban residence in Vinh City (Nghệ An Province), and FPSO.

Nevertheless, financial companies' lending results are very limited as compared to commercial banks. Their total outstanding loans are equal to only 0.3% of the commercial banks' figure. They have made progressive steps thanks to strategic changes in recent years as well as the Government's policy assistance, especially since the Government's Decree 79/2002/NĐ-CP on organization and operation of financial companies. They lent VND579 billion in 2006 and VND1,750 billion in 2007. This increase is very encouraging; however, it still accounts for a small percentage in total outstanding loans of credit institutions (only 0.76% in 2007).

* Financial services

While modern banks in the world have developed more than 3,000 services of various kinds, Vietnam's banks provide only 600 services. At present, financial companies have step by step extended their activities although they face limitations: no permission for local and overseas payment services, account-related services, and money transfer...Some financial and monetary services are provided by financial companies:

Financial consultancy for project and investment.

Table 2: Capital mobilization of financial institutions in Vietnam

Unit: VNDbil.

Indicator	2006	Share	2007	Share
Commercial banks	183,418	99.36%	284,026	99.8%
Finance leasing companies	960	0.52%	1,019	0.36%
Financial companies	222	0.12%	458	0.16%
Total	184,600	100%	285,503	100%

Source: Vietnam State Bank

Table 3: Lending performance of financial institutions in Vietnam

Unit: VNDbil.

Indicator	2006	Share	2007	Share
Commercial banks	165,264	97.10%	222,678	96.92%
Finance leasing companies	4,357	2.56%	5,319	2.32%
Financial companies	579	0.34%	1,750	0.76%
Total	170,200	100%	229,747	100%

Source: Vietnam State Bank

Capital settlement and financial arrangement.

Trust fund management and agent.

Consultancy for trading in foreign currencies and balance of payments, project evaluation, voucher discounting, information provision, support for stock trading ...

Table 4: Revenues from financial services of selected companies

Unit: VNDmil.

Financial company	2006	2007				
	Financial services	Total revenue	%	Financial services	Total revenue	%
Petrovietnam	4,149	16,863	24%	6,764	64,401	10.5%
Vinashin	498	4,695	10.60%	1,656	6,553	25.2%
Clothing	90	13,603	0.66%	87	14,987	0.5%
Rubber	-	4,979	0%	239	3,372	7.1%

Nevertheless, financial companies' services remain meager and insufficient; their revenues account for a small share; competitiveness is much lower than other financial institutions; and they have no exclusive services, etc.

II. Current difficulties of Vietnam's financial companies

1. Equity capital is very small

In doing business, financial companies often use much more funds as compared to enterprises in other industries and to their equity capital. Equity capital plays an important role because it decides their position and scale, and it also refers to safety indicators in their business as well as competitiveness and expansion.

Nowadays, the Petrovietnam Joint Stock Finance Corporation's equity capital is highest, but stays at VND3,000 billion (US$190 million). This figure is thus much lower than that of foreign banks and financial institutions. Other financial companies own only tens to hundreds of billion Đồng. Then how do they can win in competition against foreign institutions which will enter Vietnam's market in immediate future?

2. Financial companies' services remain inadequate and technologies poor.

The US tops the list of service providers in the world. Annually, this industry brings 70% of national income, especially American credit facilities are state-of-the-art and most facilitative in the world. Just because of this, when the Vietnam-US trade pact takes effect, Vietnam has to cope with extremely large challenges in the area of financial services. This will place a serious pressure on Vietnam's financial sector in its integration process. The world's experience shows even though the financial market is fully liberalized, foreign companies account only a modest share (from 4% to 18%) if the host country's financial system is strong.

The market share of local credit institutions and financial companies now remains some 70% of total revenue but it tends to go down. The reason is their managerial skill is restricted. They focus their loans on state-owned enterprises but these businesses operate ineffectively and suffer losses. The number of products and facilities are small and not competitive in the market. Revenues from these services are still meager, accounting for 10% to 15%, so the scale of activities and level of development is low and not compatible with their potentials.

iii. Colutions to development of Vietnam's financial companies

1. Diversifying forms of ownership

Table 5: Charter capital of selected financial companies in Vietnam

Company	Charter capital
Post Financial Company	VND500 bil.
Rubber Financial Company	VND500 bil.
Petrovietnam Joint Stock Finance Corporation	VND3,000 bil.
Clothing Financial Company	VND70 bil.
Handico Financial Company	VND50 bil.
Vietnam Prudential Financial Company	US$7.5 million
Vinashin Financial Company	VND1,023 bil.
Coal & Mineral Financial Company	VND300 bil.
Vietnam Socn Gñrale Financial Company	VND320 bil.

(Source: Vietnam State Bank)

Previously, there are two kinds of financial companies: joint stock companies and state-owned affiliates. Nevertheless, two joint stock companies applied for disbandment in 2002 and 2003 (Seaprodex) or merging (Saigon Financial Company). At present, financial companies are operating in two forms of state-ownership and foreign investment. As such, their ownership has not yet been diversified. Therefore, the first solution is to concentrate all efforts on attracting investment capital from various economic sectors. This not only raises funds for working but also build new mechanism for better management.

In addition to these above categories, attention should be paid to financial companies for projects of public utility and national benefits. For example, huge funds are needed for building Hồ Chí Minh Highway. In other countries, financial companies are commonly established to exploit and manage funds for this project and this company will be disbanded upon completion of the project.

Foreign investors should be permitted to own shares of local financial companies so that their capital and managerial skills are useful for development of Vietnam financial market. They may also enter joint venture with local partners in financial companies, banks, state-owned and private enterprises, and individuals which hold shares of financial companies.


Photo by Huỳnh Thơ

2. Extending networks of financial companies.

Financial companies are a kind of non-banking financial intermediaries whose key function is a bridge between capital supply and demand. In other words, input and output of financial companies are capital. As a result, their activities are not bound in headquarter, but extended to the places where there are large capital demand and supply.

At present, financial companies have no broad networks of branches, so they face not a few difficulties, especially for a subsidiary because member companies of a corporation scatter over the country while the financial company is not allowed to do payment jobs. In principle, financial intermediaries channel capital from suppliers to those in need. These institutions work well mostly due to their nationwide network of branches.

Branches should be opened in those localities where there are related industries. For example, the Petrovietnam Joint Stock Finance Corporation needs to open branches in localities where there are petroleum industry and major financial centers including Hải Phòng, Cần Thơ, Khánh Hòa, headquarters in Hà Nội and HCMC and soon establish branches overseas.

3. Training managers and staff

Financial companies should have plans of training the high quality human resources to meet international business criteria in the process of integration. This is a determinant to their success. They have focused their efforts and conditions on building an army of professionals as well as giving suitable incentives and promotion opportunities. The task cannot be fulfilled overnight, but it must be maintained for a long time.

The army of officials for international integration must be standardized, especially those directly involved in the process of negotiating, and signing international contracts, inspection, and legislation, operation of new technologies.

The birth and operation of financial companies is new to Vietnam. Most of their officials move from commercial banks, but many of them, especially in industry corporations have no experience in money trading. Therefore, they should be retrained to meet requirements of new tasks as follows:

- Selecting and sending some young qualified and potential workers to official coursed so that they are trained in management and operation of financial companies in the market economy.

- Organizing on-the-job courses to update knowledge and skill to do current tasks.

In addition, financial companies may hire advising experts. They help not only find suitable strategies for operations but also improve the staff's knowledge and profession.

4. Other solutions

- Vietnam's financial companies should fully utilize the advantages of "home ground" such as language, custom, legislation to make quick access to modern financial services and finally to increase their market shares in the current fierce competition.

- Vietnam's financial companies are required to learn experience and advanced administration of foreign financial companies and establish partnership with them on the basis of equality and mutual benefits.

- They have to improve their development strategy to navigate the organization and business scale. Therefore, they need to build a complete system of financial institutions to accumulate sufficient capital for the corporation's activities and targets.

- The management board's powers and obligations should be enhanced in accordance with international common practice. The company's risk management model must operate effectively with a strict process of control, report and inspection.

- The company has to promote product quality, diversify services, focus on expansion of key services and finally make a good balance in using mobilized capital.

- Financial companies are a rather new kind to Vietnamese customers, so they have to concentrate their efforts on marketing to attract them to services and strengthen their brand. That is also a measure to promote their confidence and familiarity, thus mobilize idle money from the people. Their brand should also be diffused in domestic and foreign financial markets.

- The companies should heighten their financial potentials and risk prevention ability. To do that, they must set up a road map to increase their equity capital to meet the Government's requirements and raise funds by issuing valuable papers and medium- and long-term bonds; borrowing money from domestic and foreign credit institutions and holding trust funds for individuals and organizations. At the same time, financial companies should boost up medium, long-term lending, co-financing, investment in profitable projects of energy, tourism, industry, mineral so that the share of these assets account for 40-45% of the total value.

In short, Vietnam's financial companies' potentials for development are so great. The establishment and development of financial companies will generate more capital channels for the national economy. It also fulfills businesses' demand for medium and long-term loans, especially for small and medium enterprises, and lends money to individual customers for consumption. Nevertheless, the State Bank shall consider the licensing of financial companies so that they operate safely and efficiently. Moreover, they should focus their targets on auspicious services such as lending for consumption and installment sale, issuing ATMs, etc.■

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