Fully Developed Finance Market as a Basis for the Development of Small and Medium Enterprises

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1. The finance market in Vietnam today

a. Money market as a source of short-term capital:

In this market, small and medium enterprises (SME) could issue or trade in bills for short-term loans, deposit their idle money with banks for some interest or secure short-term loans from banks. They can also trade in T-bills and other negotiable instruments for some profit.

The open market run by the central, in the past five years after its establishment, have increased the number of trading sessions and volume traded. From Dec. 27, 2004 on, the trading session has been carried out on a daily basis and many operations were carried out online between the SBV and member banks.

In June 2001, the SBV applied liberation of interest and exchange rates and allowed banking institutions to decide their own interest rates. This measure helped it control and adjust the interest rate to changes on the market. In 2004, the rates offered by the SBV were rather stable: the base rate varies between 7.5% and 7.8%; discount rate stayed at 3%; rediscount rate 5%; deposit rate rose slightly – 0.24% to 0.48%; and lending rate rose by 0.6%. This effort affected positively the deposit and lending rates offered by banks, allowing SMEs to enjoy more autonomy in employing sources of short-term capital when their assets, performance and managerial skills are still poor.

In Vietnam today, there are three markets for foreign exchange: the inter-bank foreign exchange market; the OTC market and the free market. The inter-bank market came into operation in Sep. 20, 1999 in which the SBV acted as the final buyer and seller and played a decisive role. In recent years, the exchange rate of the dollar to the VND fluctuated in opposite directions. The dollar fell drastically on the world market, which allowed the VND to stop appreciating on the one hand. On the other hand, the increasing CPI in Vietnam made the VND fall against foreign currencies, which forced the SBV to regulate the market more carefully based on changes in market force. Up to Dec.31, 2004, the exchange rate on the inter-bank market rose by 0.84% compared with the first month of the year while the rate on the free market rose by 0.83%.

In realities, changes in many factors on the world market made the exchange rate on the inter-bank market less flexible and influential in regulating the rate on the free market. The market also supplies loans in foreign exchange to companies, especially exporters and importers.

b. Capital market as a source of medium- and long-term capital:

Commodities on this market include government bonds, corporate bonds, stocks and shares, and project bills; which constitute an important source of medium- and long- term capital for SMEs. Government bonds become a channel of investment capital for the Government and it could be used for development of SMEs. The government bonds have maturities up to 5 and 10 years; bonds issued by the Fund for Development: 15 years and special bonds issued by state-owned commercial banks: 20 years. These bonds are gradually standardized with a view to facilitating trade on the secondary market. Many companies also start issuing bonds and bills and various derivatives.

Stock market made its appearance in Vietnam in 2000 and started turning various sources of capital with different maturities into long-term capital needed for economic development. Many companies have known how to mobilize long-term capital through this market and avoid using short-term loans for long-term objectives in order to reduce risks. The privatization also leads to a source of commodities. At present, some 30 companies have had their shares listed on the market. The value of the listed shares, up to VND29,000 billion, equaled to 3.94% of the GDP in 2005. On March 16, 2004, the State Securities Commission was put under the Ministry of Finance to be responsible for working out policies to privatize state-owned companies, develop the market for bonds and securities, and set standards for accounting and auditing businesses... in order to facilitate the development of the stock exchange in the coming years, and for the time being, accelerate the privatization program and attract investors by applying various technical measures.

On March 8, 2005, the HàNội Stock Trading Center was inaugurated and there has been plan to turn it into an OTC market run by the State. This means that this center will trade in both listed and unlisted shares issued by companies that have legal capital of at least VND5 billion and 50 shareholders, and have made profit for at least one year. The Hà Nội Center thus has ability to attract customers from the free stock market. Moreover, it also trades in bonds issued by companies, and central and provincial governments.

According to the SSC, the plan to develop the Hà Nội STC comprises two phases: In the first phase, from 2006 to 2010, effort will be made to develop the centralized trading center and put up for auction shares from privatized companies; and in the second phase, from 2010 on the OTC will be developed. Foreign experience shows that this market is very useful for SMEs, hi-tech and emerging companies. According to a survey, 88.24% of respondent companies wanted to take part in the OTC.

As for the volume of commodities for the two centers in Hao Nội and HCMC, statistics show that only 29 out of some 2,400 privatized companies could have their shares listed and traded in the HCMC STC. The privatization program is still carried out and many joint stock companies have engaged in the Hà Nội Center.

The real estate market has been organized in Vietnam and it is still new to both central and local governments. When there is no source of long-term capital for housing programs, the most suitable model is financial institutions that supply long-term loans to customers in need of houses, and in the future they could develop into specialized institutions for this purpose. This market can contribute to the development of the finance market in Vietnam.

2. Measures to develop the finance market

The Government should allow financial institutions to issue more long-term commodities, such as bonds and deposit certificates, at time of their choosing without asking for permission from the SBV. Economic concerns with prestige and financial strength, including joint stock banks and foreign -invested companies, could be encouraged to list their shares in the stock market. Facilities for carrying out transactions and supervising them must be modernized and upgraded. Custody and inter-bank payments system must be automated. The organization of the SSC must be perfected by recruiting real experts so they can suggest new policies and forms of sanctions it need be.

Universities and mass media can help disseminate knowledge of investment and stock market because the public and companies get more and more options when they think of earning more money and benefits, such as buying life insurance, shares and stocks, government and corporate bonds, or investing in real estate and business instead of depositing their money with banks.

As for the market for foreign exchange, all commercial banks with enough capital, experience, personnel and public image could be allowed to trade in foreign currencies. The banking system could accept bonds and bills as common security in order to limit pressure on the stock market.

The internal value of the domestic currency must be preserved and the VND must be made the only legal tender in Vietnam. The SBV should take various measures and employ different instruments to control the exchange rate and the inflation rate.

Full attention must be paid to difference in interest rates between loans in foreign exchange and the domestic currency in order to regulate movements of capital, thereby avoiding unnecessary fluctuations and crises.

The issuance of government bonds should be planned beforehand. It must be linked with the market demand or need to repay external debts, and conditions for operations on the secondary market. The legal infrastructure must be beefed up and transparent enough to help lenders ensure validity of lending contracts in cases of default borrowers.

The banking system should improve their loan quality and reduce overdue debts, supply more loans to SMEs, private companies and family businesses by estimating their business plans instead of applying discriminatory measures, especially when most of overdue debts are in the public sector.

Policies and regulations on the insurance business must be perfected in order to facilitate operation of insurance companies, ensure legitimate interests of the insured, and encourage the public to buy insurance for their life and business. Moreover, the government can take measures to encourage insurance policies for the agriculture and peasants. This business should be open to all classes, including foreign insurers, without limits on their scope of operations. The Insurance Business Law must be perfected and observed by both the business circle and the government itself.

In short, the Government should work out an overall strategy to develop the finance market and establish close relation between the money and stock markets. Regular examinations of results, shortcomings and objectives could help the financial authorities to find suitable solutions to arising problems in the coming years, thereby supporting the development of local SMEs.■