

Development of Vietnam's Financial Sector:

The Key Policy Issues

Vo Tri Thanh
Central Institute for Economic Management

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Outline of Presentation

- **Major characteristics of VN financial sector**
- **Prospects for financial development in VN**
- **Key policy issues**

Major characteristics of VN financial system

- Reform + Integration during 1990 – 2005 ► Significant development of banking sector and emergence of stock and bond markets
- 2006 - 2007 witnessed a boom of the banking activities and securities markets (reflecting some strong eco. fundamentals and high expectation of future development)
- Financial depth changed significantly. Until 2004, VN still seen as an economy with rather shallow financial depth. 2007: Credit/GDP = 82%; M2/GDP = 110%
- Lack of transparency and weak financial supervision
- VN financial system is still bank-based and under-developed in comparison with many others

	Bank Deposit/GDP		Stock capitalization/GDP		Outstanding Bond/GDP	
	1990	2005	1990	2005	1990	2005
Indonesia	29.8	36.2	4.4	27.1	0.4	19.0
Malaysia	52.1	93.5	100.7	143.6	69.8	90.4
Philippines	24.1	45.8	20.6	35.3	22.1	38.8
Singapore	74.3	102.3	95.8	163.4	27.8	58.0
Thailand	56.8	78.7	29.2	68.0	9.7	41.1
Vietnam	15.0¹	64.7 (85.0)	0	1.1 (43.0)	0	4.5 (13.3)
China	75.6	177.8	2.4 ¹	32.0	8.5	25.6
Hong Kong SAR	205.6	242.3	107.2	528.1	1.5	26.9
India	31.4	52.2	10.4	60.1	19.9	33.8
Japan	100.0	123.2	121.7	93.8	85.9	192.5
Korea, Rep.of	32.6	68.8	48.2	72.9	34.1	78.1
Taiwan	56.8	79.7	107.6	134.8	17.0	55.9
Germany	53.8 ¹	98.1	21.7	463.6	51.6	75.1
United Kingdom	87.8	122.1	85.2	134.7	36.8	46.9
United States	59.6	57.9	57.5	134.6	122.0	158.0

Sources: CEIC data; World Bank, Financial Structure Dataset, February 2006

Note: 1. Data for 1992 (Figures in brackets are for 2007)

Prospects of financial dev't in VN

Significant market potential

- Bright prospect of high economic growth and development
- Rapid urbanization
- Young population and younger generations are early-adopters of banking services
- Room for development is huge:
 - Financial sector remains in the early stage of development
 - Access to the financial service/activities is still limited (50% of household savings are not deposited in banks. The number of personal account in banks is just about 8% of total population. Retail banking services account only for 6% to 12% of bank revenues)

Key policy issues

General issues

- Priority of reform: Focus on the SBV and banking system?
- Development of a *more balanced* financial system in long term (banking sector + stock market + bond, especially corporate bond, market)
- Financial supervision paradigm: From multiple authorities to single entity? (At present: SBV + MOF + SSC (MOF) + NCFS)

- Financial liberalization: Degree of capital account gradual opening + Role of foreign investors/institutions?
- Improvement of macroeconomic and financial statistics + building of earlier warning system
- Establishment of financial centers: Hanoi and HCM City? (necessity and conditions)
- Participation in the global and regional financial cooperation: Surveillance system + Regional bond market + Credit line/swap arrangement facilities + Monetary and ER policy cooperation?

Banking system

- New development dimensions (strategic partnership; equitization; entry of new banks and competition; banks have tended to be universal; competition) **vs.** weak financial, risk management + underdevelopment of regulatory framework + limited supervision and monitoring capacity
- High concentration ratios (SOCBs' shares accounted for 68.8% and 59.3% of total deposits, and 64.5% and 55.1% of total credits in 2006 and 2007 respectively)
 - ▶ More competition, but problem of market entry?

- NPLs have significantly declined but in 4th Q 2008 – 1H 2009 and in the future? (Large SOE and public investments efficiency; “moral hazard”) + Double mismatch problem (ST deposits $>$ $<$ LT lending and high degree of dollarization)
- ▶ SOE reform, including equitization + risk management and supervision improvement (benchmarks?) + Corporate bond market development?

Stock market

Major contradiction: “Speculative” interest (Local investors tend to invest in SR) but liquidity **vs.** investment for resource mobilization for development (IPO)? *It can be solved depending on*

- Quality of Information disclosure and transparency
- Improvement of incentives system
- Constraints/limitations of the real-estate- and stock-collateralized loans

- Development of institutional investors + SOE reform process
- Role of State Capital Investment Corporation SCIC (Concerns: Expertise + Stabilizer/ profit-oriented (as mandated) + supervision?)
- Reorganization of HOSE and HASTC (OTC + Bond market)
- Improvement of legal framework and SSC (incl. enforcement)

Bond market (Needs to have longer time to develop)

➤ **Increasing supply & demand?**

- Having more (large/focal) firms with high reputation
- Having more LT investment institutions (insurance companies + pension funds...)

➤ **Strengthening role of Government as issuer?**

- Establishing a benchmark yield curve \Rightarrow commitment to regular issues
- Nurturing a strong secondary market (Tracking the spreads quoted by dealers; creating the reliability of arrangement for exchanging the assets for cash; modern technology for facilitate clearing and settlement of secondary market trading)

➤ **Strengthening financial infrastructure?**

- Appropriate legal framework + Effectiveness of the judiciary system
- Quality of information: Strong accounting and disclosure standards
- Risk-rating and other information generating agencies
- Efficient and reliable clearing and settlement arrangement
- Tax incentives during the initial stage of development (Equity market may exist where bond markets fail to thrive)

THANK YOU!