Vietnam's Retail Financial Business Has Growth Potential

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I. Introduction

Vietnam has been largely isolated from the rest of the world since the war in the 1960s and 70s, and with that war followed by the third Indochina war (with China), its economy remained in a slump until the mid-1980s. It began seriously striving for a market economy with its *Doi Moi* reforms in the mid-1980s, and has generated strong economic growth for the past two decades. Vietnam is becoming strategically more important to multinationals based on their "China plus one" approach offered to the Indochina peninsula.

Investors seeking a safe haven in response to the sovereign debt crisis in the euro zone have begun repatriating the funds they had been aggressively investing in emerging markets, and this has forced emerging market governments to change course in monetary policy, from tightening aimed at suppressing inflation to loosening aimed at stimulating the economy. Vietnam is no exception to this, and stabilizing its broader economy to bring back foreign direct investment has become an urgent issue.

On the other hand, Vietnam's rich source of mostly young cheap labor and strong work ethic give it a competitive advantage, and if it can pull off balanced growth along the way to transitioning to a high-value-added economy, it should have the potential to form a huge middle class. This emergence of a new middle class should broaden the business opportunities in retail financial services.

In this paper, we look at Vietnam not only as a manufacturing center but also as a consumer market with growth potential to examine the environment for retail financial services.

II. Overview of Vietnam's economy

1. Macroeconomic structure

Vietnam is a long and narrow country stretching north to south on the Indochina Peninsula. Its population of 87 million, smaller than Indonesia's but larger than both Thailand and Malaysia's, is fairly young, with an average age of around 27 years. Its main industry remains agriculture, but in the process of opening up to the outside world it has been establishing itself as the world's factory for clothing and other light industries, and manufacturers trying to diversify the risks inherent in relying too much on China are increasingly interested in Vietnam as a way to achieve that diversification.

Vietnam spent heavily on its military in the 1960-70s, having fought not only the Vietnam War but also invading Cambodia and fighting a war with China, and these conflicts put additional stress on an already decimated domestic economy. Furthermore, under the rigidities and inefficiencies of its Soviet-style planned economy, Vietnam's productivity declined as it became more isolated from the international community, impoverishing it to the point where its economy was unable to function without subsidies from the Soviet Union.

Once it became clear in 1986 that subsidies from the Soviet Union would dry up, however, it engineered a sudden change of policy toward a set of economic reforms known as *Doi Moi*. After having championed a socialist market economy, the government not only introduced a market economy, it started to aggressively open up to the outside world after concluding that its isolation from the international community following the Vietnam War was a cause of its subsequent economic stagnation. Using its low wages as a lever to insert itself into the international division of labor, Vietnam began celebrating high growth like the rest of ASEAN.

In 1995, it established diplomatic relations with the US and then joined ASEAN, and its improving relations with the outside world led to a boom in foreign direct investment during the 1990s. Investors starting pulling their money out because of the

Figure 1: Snapshot of Vietnam

Population	About 87 million (13th in the world), 46 million working age, average age below 30
Land area	About 330,000 km^2 (90% of Japan's size)
Capital	Hanoi (population about 6.5 million)
Language/religion	Vietnamese/Buddhism (80%), Catholic, Caodaism, others
Chief industries and exports	Agriculture, forestry, & fishery, mining, light industry/crude oil, rice, coffee, apparel, marine products
Ethnic groups	Kinh (Vietnamese) and 53 minorities
Exchange rate	Roughly ¥1= 262 dong (as of 1 August 2011)
Form of government	Socialist republic (President Nguyen Minh Triet served from 2006 until July 2011)
Nominal GDP (2009)	About $103 billion (about ¥8 trillion, roughly 1.6% of Japan's economy)
Long-term sovereign debt rating	S&P: BB-(negative) / Moody's: B1(negative) / Fitch: B+/stable

Source: Nomura Institute of Capital Markets Research, based on data from the General Statistics Office, Asia Development Bank, IMF, World Bank, and the Foreign Ministry's website

Asian monetary crisis, causing growth to temporarily dip below 5%, but Vietnam returned to a growth trajectory in 2000, and has achieved economic growth of at least 7% annually since then. When it joined the WTO in 2007, it committed to phasing out restrictions on foreign capitalized firms' involvement in the financial sector and the retail business, and it attempted to stimulate its domestic market by privatizing state-owned enterprises and making domestic industries more competitive by aggressively courting overseas capital.

Meanwhile, Vietnam's biggest problem is the instability of its macroeconomy. Inflation remains a threat, and is running at nearly 20% in 2011. Because of a lack of confidence in its own currency, the dong, citizens have been buying up dollars and gold in anticipation of dong depreciation, and exporters are holding on to the dollars they have earned. This is reducing dollar liquidity and causing the dong to depreciate, thereby fanning the flames of inflation and creating a vicious circle.

In addition, it has maintained a chronic current account deficit, making its weak economic base highly dependent on foreign direct investment for a source of funds. One reason for its persistent trade deficit is its failure to broaden its industrial base, which means to expand its exports of goods in high demand it needs to increase its imports of intermediate goods even more[1]. Its current account deficit is the mirror image of its negative savings-investment gap, and according to IMF data private-sector investment as a percentage of GDP has been declining over the past three years, in contrast with other ASEAN countries[2]. This suggests the possibility that the recent shrinkage of its current account deficit is owing not to growth in exports brought by a cheaper dong, but rather to its having become less attractive as a place to invest. Another major problem for Vietnam is that the privatization of its inefficient public sector, which accounts for roughly a quarter of its GDP, is making very little progress. Its securities market, which was fully launched in 2000, remains small, with IPOs for numerous desirable state-owned enterprises yet to materialize.

In light of the conditions outlined above, the government introduced "Resolution 11" in February 2011, a program that places a priority on stabilizing the macroeconomy, and thus shifts the focus of economic policies from growth to stability[3].

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1 For example, crude oil is a major export from Vietnam, but because of its lack of refineries it must rely on the import of infrastructural goods in order to expand crude oil exports.

2 Based on IMF data using real effective exchange rates, the dong is now in an appreciating trend relative to its average in 2000.

3 Resolution 11 comprises six policies aimed at stabilizing the macroeconomy: (1) monetary tightening, (2) fiscal austerity, (3) reduction of the trade deficit, (4) improved social security, (5) raising electric power prices and setting crude oil prices based on market principles, and (6) improving the policy announcement effect. More specifically, (1) hold growth in lending to below 20%, (2) hold growth in the M2 money supply (cash plus domestic bank deposits) to 15-16%, (3) reduce the share of loans outstanding used for investing in real estate and in marketable securities to 16% by end-2011, (4) reduce gold imports and foreign currency-denominated borrowing for the import of certain designated unnecessary goods, and (5) hold the budget deficit to no more than 5% of GDP.

2. The middle class and individual financial assets

Vietnam's per capita GDP has grown by an average of about 6% in real terms over the past 10 years, finally surpassing 17 million dong (about ¥70,000) in 2008, the year after it joined the WTO (Figure 2)[4]. Vietnam's middle-class is estimated to comprise 7 million households, with the majority of these probably living in large cities[5]. That is the smallest middle-class population in ASEAN, and its growth will likely depend on macroeconomic stability over the near term and on income growth driven by infrastructure-based improvements in labor productivity over the longer term. Although the share of the labor force working in agriculture has been declining over the past 20 years, the majority of workers still make their living by farming in rural areas, earning incomes that are less than half those of urban workers (Figure 3)[6].

Figure 2: Per capita GDP

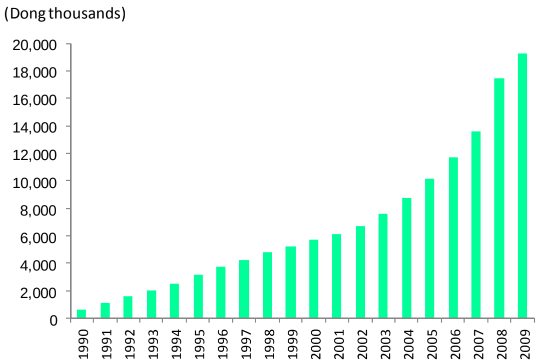
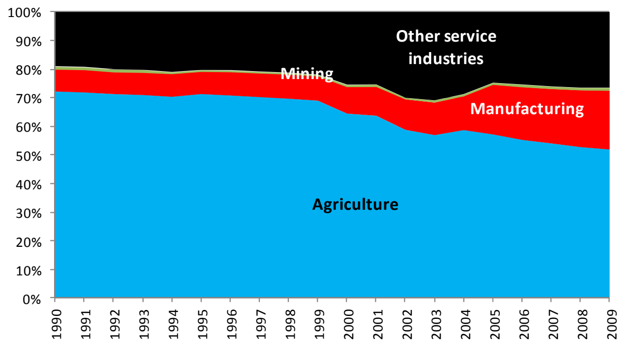


Figure 3: Distribution of labor across industries



Source: Nomura Institute of Capital Markets Research, based on World Bank and Asia Development Bank materials

Because Vietnam's main exports are crude oil, textiles, marine products, and rice, rural workers employed in primary industries in Vietnam have not seen a doubling of their incomes like those workers in such emerging markets as Indonesia and Brazil, which have benefited from the recent boom in natural resources.

Although there are no official statistics regarding the breakdown of individual financial assets, in light of the country's current per capita GDP of about $1000, it is likely that most of its citizens still lack the resources to invest in securities, and that with the dong depreciating, they will continue to hoard their assets in dollars and gold. Given its young population, however, it is easy to envision a scenario whereby future growth in incomes and macroeconomic stability will boost demand for financial services and accelerate the flow of funds into risk assets.

[4] The IMF estimates a per capita GDP in 2012 of $1,422. This probably puts Vietnam roughly on par with the stage of development that Japan was in immediately after the war until around 1950.

[5] McKinsey & Company, "Growing up fast: Vietnam discovers the consumer society", McKinsey Quarterly, August 2010

[6] For details, see http://www.bwtp.org/files/MF_Industry_Report_Vietnam_ELECTRONIC.pdf

III. Vietnam's retail financial business

1. Banking sector

1) Market structure

The banking sector, at the core of Vietnam's financial system, is young, having only existed for about 20 years. In 1990, after the launch of the *Doi Moi* reforms, the State Bank of Vietnam (SVB), Vietnam's central bank, was stripped of its monopoly on commercial banking services and four large state-owned banks were established: the Vietnam Bank for Agriculture and Rural Development (Agribank), the Bank for Investment and Development of Vietnam (BIDV), the Foreign Trade Bank of Vietnam (Vietcombank), and the Industrial and Commercial Bank of Vietnam (Vietinbank)[7]. Management at the state-owned banks remained inefficient, however, and the government decided to privatize them, using IPOs beginning in 2000 to diversify their ownership and improve their governance. After Vietnam's accession to the WTO in 2007, the competition among foreign-capitalized banks to enter its banking sector got serious.

Relative to the country's population and size of its economy, its banking sector has become overly dense with over 100 banks competing. As of end-December 2010, there were five state-owned banks, 37 banks owned by the private sector, five banks wholly owned by foreign-capitalized banks (HSBC, Standard Chartered, Australia and New Zealand Banking Group, Hong Leong Bank[8], and Shinhan Bank[9],) five joint venture banks[10], and 48 branches of foreign banks. In addition, there are credit institutions comprising 17 nonbanks and 13 financial leasing companies (Figure 4).

In 2006, the top four state-owned banks accounted for approximately 70% of Vietnam's loans outstanding, but that share has been steadily declining as a result of the recent emergence of private-sector commercial banks (Figure 5). The three biggest private-sector commercial banks are Asia Commercial Bank, Sacombank, and Techcombank, all primarily taking care of the rapidly growing private-sector small and medium business banking and retail banking for individuals.

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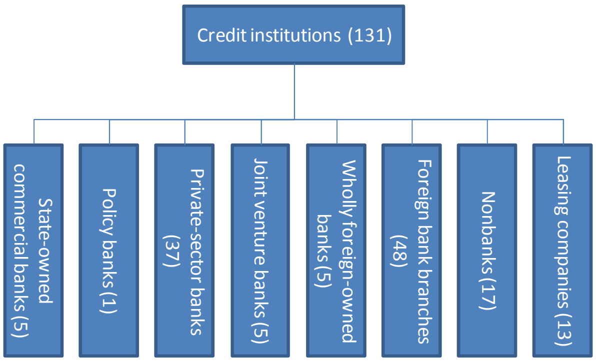
7 Vietnam has two other government-affiliated policy banks, the Mekong Housing Bank and the Vietnam Bank for Social Policies.

8 This is the banking subsidiary of Malaysia's Hong Leong Group, a conglomerate primarily involved in financial and insurance services, manufacturing and sales (including the ceramics industry and automobile sales), and real estate.

9 One of Korea's four leading banks. The other three are Kookmin Bank, Woori Bank, and Hana Bank.

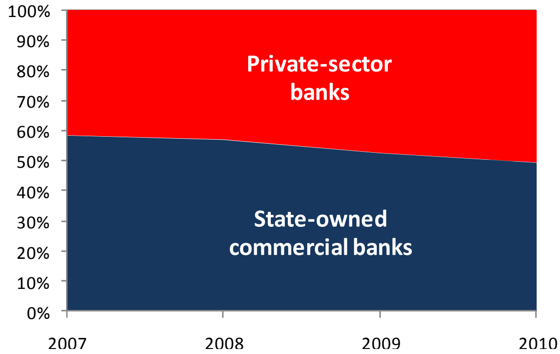
10 These are the Indovina Bank (a JV between Vietinbank and Taiwan's Cathay United Bank), VinaSiam Bank (between Agribank and Thailand's Siam Commercial Bank), Shinhanvina Bank (initially between Vietinbank and Korea First Bank, and Daewoo Securities TN, with all stakes eventually sold to Shinhan bank later TNacquiring a 50% stake TN), VID Public Bank (between BIDV and Hong Kong's Public Bank), and Vietnam-Russia Joint Venture Bank (between BIDV and Russia's Bank VTB).

Figure 4: Vietnam's banks



Note: As of end-2010. Figures in parentheses are the number of banks.
Source: Nomura Institute of Capital Markets Research, based on data from the State Bank of Vietnam

Figure 5: Loan market shares



Source: Nomura Institute of Capital Markets Research, based on IMF data

Loans outstanding grew at the fast annual rate of 39% from 2006 until 2009, and by end-2009 totaled 1,869 trillion dong, more than 100% of GDP (Figure 6). Although there is no official data published for 2010 and later, the IMF estimates that figure had grown to 3,000 trillion dong (¥12 trillion) by end-2011, which would give Vietnam the fastest expansion of credit of any ASEAN country over the past five years. This rapid growth of credit is one of the main sources of inflation, and given the financial sector's inadequate credit management systems and legislative framework, there is a rising chorus warning of growth in nonperforming loans, including those extended to inefficient state-owned enterprises and other large corporations as well as real estate-backed loans[11].

Meanwhile, in step with this expansion of credit total deposits outstanding rose to 1,800 trillion dong, although the loan-deposit ratio was over 100%, resulting in fairly tight liquidity in the banking sector overall (Figure 7). Most of the smaller players have raised their deposit rates in order to attract more deposits and improve liquidity, and if the government were to put a ceiling on lending rates in an attempt to prevent an increase in corporate bankruptcies, it appears likely that the loan spread (between lending rates and deposit rates) would narrow even further[12].

The term structure of these deposits has been getting shorter because an either flat or inverted yield curve and individuals' lack of confidence in the value of the dong have combined to encourage depositors to keep most of their funds in short-term

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11 According to the rating agency Moody's, writing off nonperforming loans takes time because of the complex legal procedures involved in disposing of the assets used as collateral, and large differences in the way NPL ratios are calculated between the Vietnam Accounting Standard (VAS) and IFRS mean that in some cases, the NPL ratio under IFRS could be as much as three times that under VAS.

12 If the authorities start tightening lending criteria in order to suppress inflation, default rates may increase as a result of higher loan rates. At the end of September 2011 when the central bank capped the rate that could be paid on dong-denominated deposits with a term of at least one month at 14% in order to constrain the rise in interest rates, it accelerated the outflow of deposits into gold and dollar assets, causing the dong to depreciate further.

Figure 6: Lending

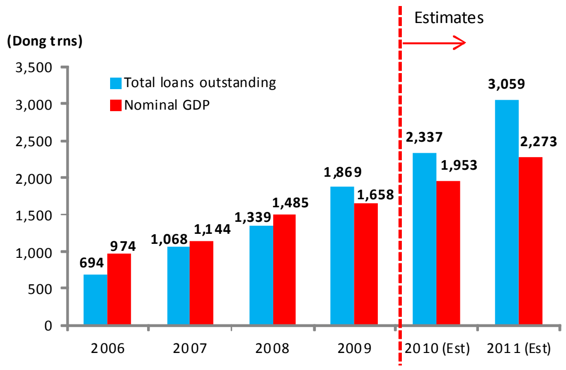
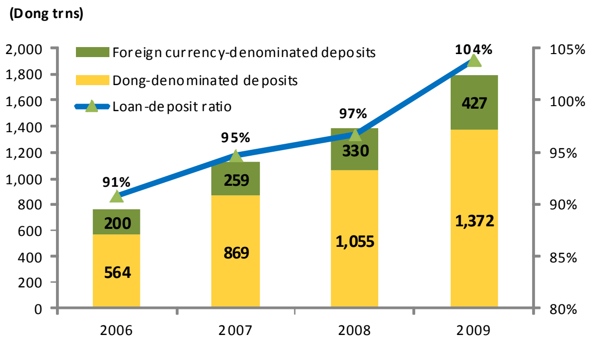


Figure 7: Deposits



Source: Nomura Institute of Capital Markets Research, based on IMF materials

deposits. Because deposit rates have been capped, banks must use various promotions in order to attract a stable source of deposits, but not enough of the longer-term risk capital needed for capital investments is flowing to businesses, particularly smaller firms.

There is also concern that the loan books of private-sector commercial banks have become overly exposed to specific sectors. Smaller private-sector banks are also at risk of an increase in their nonperforming loan ratios, because they lack the capacity to adequately assess the risk of loans to very small businesses and individuals, while their amount of real estate-backed loans has risen sharply. In response to this, in February 2011 banking regulators released Resolution 11, wherein they set a target for real estate loans to not exceed 16% of the entire loan portfolio.

2) Competitive environment

In Vietnam's banking sector, the big four state-owned commercial banks and the three largest private-sector commercial banks by assets have a combined 56% share of the loan market (Figure 8). Given that there are a total of 100 lenders, excluding nonbanks, financial lease companies, and the one policy bank, this is a highly concentrated market comprising a small number of large banks and a large number of small banks. For policy reasons, in the past the state-owned commercial banks focused on the wholesale business with state-owned enterprises, while the private-sector banks such as Asia Commercial Bank and Sacombank took care of the retail business for smaller firms and individuals. Now, however, the state-owned banks are striving to diversify the risk of their loan books and maximize profit margins by expanding their presence in high-margin retail services, and with foreign-capitalized companies also entering the market, that sector is becoming very competitive[13].

[13] From Japan, this includes the Mizuho Financial Group investing 11.8 trillion dong (about ¥43.4 billion) for roughly a 15% stake in Vietcombank on 30 September 2011, Vietnam's largest acquisition that year. In addition, Sumitomo Mitsui Banking Corp. acquired a 15% stake in Vietnam's Eximbank for $225 million in 2008.

Restrictions on the participation of foreign capitalized firms have been loosened in order to make domestic banks, which are lacking in human and other resources, more globally competitive, a move that will undoubtedly result in an increase in overseas investors taking ownership stakes in domestic banks and in overseas banks forming alliances with domestic banks. This should raise the presence of overseas banks in Vietnam substantially. Furthermore, we expect the introduction of stricter capital requirements to force many of the smaller domestic players to seek mergers, and this will likely mean an industry consolidation that results in several larger domestic banks, which could then compete and coexist with overseas banks. Regulators are targeting a

Figure 8: List of leading commercial banks

(¥ trns)

Bank	Listing status	Total assets	Loans out-standing	Loan market share	Market cap	Non-perform-ing loan ratio	ROE	capital ratio	No. of branches	No. of employees	No. of clients	Major stockholders	Notes
Agribank (Vietnam Bank for Agriculture and Rural Development)	**Unlisted**	1.76	1.33	16%	N/A	2.6%	9.6%	N/A	2,300	35,135	10mn house-holds, 30,000 firms	Gov't (100%)	Spun off from the SBV in 1988, Vietnam's largest bank in terms of assets, number of employees, and number of clients. Loans to farmers in farming villages and the countryside account for 70% of the loan portfolio.
Vietin Bank (Industrial Commercial Bank of Vietnam)	**Listed**	1.38	0.88	11%	0.17	0.7%	22.1%	8.0%	1,093	17,243	N/A	Gov't (80.3%), IFC (10%)	One of the four large commercial banks spun off from the SBV in 1988. Established to support the modernization of Vietnam's industry. Primarily lends to manufacturers; retail loans account for about 20% of loans. Listed at end-2008, invested in by the International Finance Corporation (IFC) and other overseas strategic investors in 2010.
BIDV (Bank for Investment and Development of Vietnam)	**Unlisted**	1.37	0.95	12%	N/A	N/A	18.0%	9.3%	597	16,475	N/A	Gov't (100%)	The oldest commercial bank, established in 1957. Now trying to shift its loan business from loans to exporters and small businesses to retail loans. Plans an IPO in 2011.
Vietcombank (Foreign Trade Bank of Vietnam)	**Listed**	1.15	0.66	8%	0.21	2.8%	22.6%	9.0%	400	11,415	5.2mn persons	Gov't (75.72%), Mizuho (15%), individuals (3.62%)	The oldest overseas correspondent bank, established in 1963 and listed at end-2007. It is strengthening its retail business (individual deposits have grown to account for 36% of all deposits), but only 11% of its loan portfolio is retail, 35% are loans to state-owned enterprises, and 54% are loans to manufacturers and small and medium enterprises.
Asia Commercial Bank	**Listed**	0.63	0.23	3%	0.08	0.4%	24.6%	9.0%	270	6,669	N/A	Individuals (54%), institutional investors (17%), Standard Chartered (15%)	A new bank established in 1993. Voted Vietnam's best bank by Asiamoney in 2009. Primarily writes retail loans, and the vast majority of its deposits are held by individuals. Non-interest income accounts for 28% of its income.
Techcombank (Technological and Commercial Bank)	**Unlisted**	0.56	0.20	2%	N/A	2.3%	24.9%	13.1%	282	6,960	1.3 mn persons and 45,252 companies	HSBC (20%)	(1) Established in 1993. Rapidly growing retail loans are 35%, loans to small and medium businesses 59%, and loans to large corporations 6% of its loan portfolio. By type business, the biggest share of its loans (at 37%) go to manufacturers. (2) It has made HSBC, which has a 20% stake, a strategic partner to help strengthen risk management. It is working with McKinsey and Company to roll out TechcomOne, a strategic project aimed at making it the top bank. (3) Its vision is to become the No. 1 retail bank.
Sacombank	**Listed**	0.53	0.29	4%	0.06	0.5%	15.0%	10.0%	366	8,507	N/A	Dragon Financial (6.7%), ANZ (9.8%)	Established in 1999 with capital of 3 billion dong. It has three regional banks and a development bank as parent companies. Businesses include deposit taking (including foreign-currency denominated), loans to corporations to fund capital investment, domestic and foreign funds settlement and remittances, and investment in gold, foreign currencies, and securities.

Source:Nomura Institute of Capital Markets Research banking system comprising two globally competitive banks and another 10-15 other banks within the next five years[14].

In October 2011, the central bank raised the overnight rate in the interbank market from 14.5% to 15% as a part of its monetary tightening, putting the smaller banks that primarily get their funding from the interbank market at risk of a decline in liquidity. Because the rate on deposits with a maturity of one month or longer is capped at 14%, depositors are likely to shift their funds into larger banks because they seem to be safer. On 6 December, the SVB announced that three smaller banks facing liquidity problems would be merged and receive an injection of capital from the government[15].

The domestic business environment in which the banking sector operates is becoming increasingly difficult. Instability of the macroeconomy has led to a steady shrinkage of the gap between loan rates and deposit rates and decline in the quality of loan assets, as evidenced by the nonperforming loan ratio rising to about 3%. The banking sector had an ROE of about 11% in 2010, considerably lower than the 17.5% average of listed nonfinancial firms and the lowest it has been over the past four years.

It has been under these conditions that Vietnam's banks have become more aggressive in developing business overseas. Vietinbank became Vietnam's first bank to establish an operation in Europe when it did so in September 2011. It opened a branch in Germany with the intention of offering overseas remittances, savings accounts, credit cards, and online banking services to local Vietnamese and German clients, and it has plans over the longer term to expand its branch network into other EU countries. Sacombank, Agribank, and BIDV have all started doing business in Cambodia and Laos, neighboring countries that are starting to experience significant economic growth, while both Sacombank and BIDV plan to start doing business in Myanmar, as well. It will be interesting to watch these banks move toward becoming regional banks on the Indochina Peninsula.

3) Retail banking is growing

Retail banking targeting the young middle class, which is steadily emerging as a result of economic growth, is starting to grow[16]. Less than 20% of Vietnam's population has a bank account, considerably less than in fellow ASEAN members Thailand and Malaysia[17], and some observers estimate that revenues from retail banking will grow at an annual rate of 25% or higher over the next 5-10 years[18]. All of

[14] Bank reform legislation announced in October 2011 will ultimately establish four internationally competitive banks by the year 2020 (http://www.saigon-gpdaily.com.vn/Business/Banking_Finance/2011/11/98549/).

[15] These were Ficom Bank, Tin Nghia Bank, and Saigon Commercial Joint Stock Bank.

[16] As of September 2011, banks had issued 33 million cards, established over 12,000 ATMs, and had over 50,000 POS systems in place, primarily in cities. In addition, at least 20 banks offer online banking, and eight banks offer mobile banking.

[17] That percentage is said to be 70-80% in Thailand and Malaysia. In Indonesia, however, penetration is low at less than 20%.

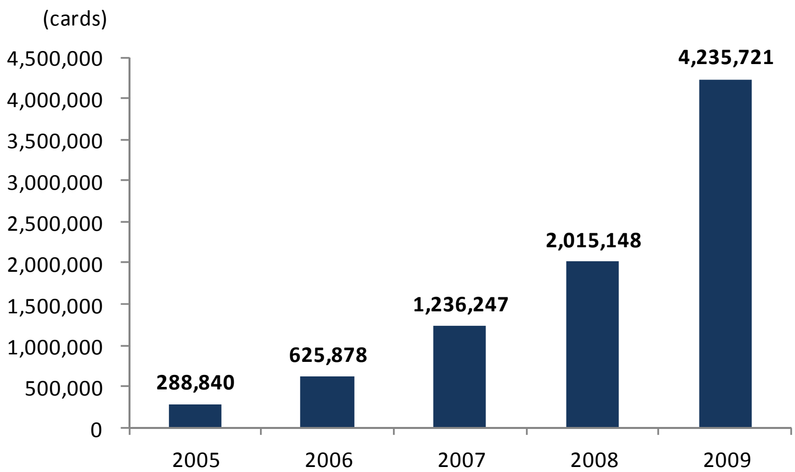
[18] McKinsey & Company, "How Young consumers could shape Vietnam's banks," The McKinsey Quarterly, March 2008

the banks are strengthening their transaction banking business, which generates fee & commission income apart from lending to individuals and very small firms, and are especially targeting the demand for online and mobile banking from wealthy, younger individuals, a demographic that has a relatively high tolerance for risk and is comfortable with information technology.

The largest domestic banks focused on retail banking are Asia Commercial Bank and Sacombank, followed by Techcombank and Maritime Bank[19]. Domestic banks currently have roughly a 90% share of the business, but foreign banks, with their superior products, are steadily making inroads. Banks from Europe raising their presence in Vietnam include Deutsche Bank and BNP Paribas, while Australia and New Zealand Banking Group, HSBC, and Singapore's OCBC Bank are also aggressively going after Vietnam's retail banking business, either by forming alliances with local players or establishing branches on their own. The regulations used to only allow foreign banks to open a single branch in a single city, but after Vietnam joined the WTO those regulations were lifted, and the cap on retail loan rates was raised in 2009.

Total issuance of debit, credit and other bank cards grew at an annual rate of between 50% and 200% over the four years beginning 2006[20]. For example, card issuance by Agribank, the country's largest bank and with 70% of its customers in the provinces, grew at an annual rate of 96% over the five years starting in 2005, reaching 4.2 million cards in 2009 (Figure 9). Even the provinces, where approximately 75% of the country's population lives and over 70% of its small businesses are based, are likely to see steady growth in demand for transaction banking in step with economic growth. In addition, Standard Chartered Bank, which in urban areas is open for

Figure 9: Number of cards issued by Agribank



Source: Nomura Institute of Capital Markets Research, based on Agribank's annual report

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[19] As of end-2010, Maritime Bank was the 10th largest bank with assets of 115 trillion dong (approximately ¥460 billion),as well as 150 branches and 217,360 customers. It has concentrated on expanding its small business and personal banking businesses over the past 10 years, and is aiming to become a top-five retail bank.

[20] Vietnam is still in the process of developing electronic commerce, and most transactions are still settled in cash. The government is promoting the use of credit cards and other non-cash settlement methods among the populace (Instruction 20/2007/CT-TTg).

business on weekends and outside of normal business hours on weekdays, was the first foreign bank to join the SmartLink Network, thereby giving its customers access to over 5000 domestic ATMs[21].

The onshore private banking business targeting successful entrepreneurs is apparently being led by HSBC and other foreign banks, but the market is still in its infancy and appears to be extremely small. Nevertheless, several individuals interviewed locally indicated that demand for wealth management among the wealthy classes was rising owing to the poor performance of capital markets. The primary service offered is not inheritance tax planning, as in Japan, but rather asset management advice[22].

Vietnam needs to further promote investment from overseas in order to raise its growth potential, but it also needs to eliminate its shortage of savings, one cause of its current account deficit; the development of retail banking will unquestionably play a major role in this regard. This will require capital investment in an IT platform and other hardware, as well as a strengthening of the software side, including by developing financial talent, diversifying product offerings, and improving credit management systems. Also prerequisite to the success of each player is that they quickly establish a core competence that they can use to differentiate their business.

4) Related legislation

After joining the WTO in 2007, Vietnam was forced to promote reform in its banking sector and strengthen the competitiveness and financial soundness of domestic banks to enable them to compete with the foreign capitalized banks entering its market. It will pursue the former primarily through the privatization of state-owned commercial banks, and the latter by strengthening capital requirements with global Basel rules as a guideline. Specifically, in May 2006 the government announced a plan to reduce its stake in state-owned commercial banks below 51% by end-2010[23], and in 2007, to accelerate that process, it raised the maximum stake that strategic nonresident investors could individually take in commercial banks to 15% from 10%[24].

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21 See http://www.vir.com.vn/news/business/corporate/standard-chartered-bank-joins-smartlink-network.html

22 Sacombank, a leading private-sector bank, established a wealth management center in 2011 to leverage its network to provide services to wealthy individuals.

23 Only two banks achieved partial privatization by end-2010, Vietinbank and Vietcombank, and the government has fallen behind in executing its privatization plan. Vietcombank, an outstanding bank, sold 6.5% of its shares, amounting to $652 million, in its IPO in 2007, and announced at end-September 2011 that Mizuho FG acquired a 15% stake. Meanwhile, Vietinbank sold a 4% stake for $64 million in its IPO in 2008, and in January 2011 IFC took another 10% stake for $182 million as a strategic investor.

24 Stand-alone overseas financial institutions not deemed strategic overseas investors are limited to no more than a 10% stake in a local bank, but that maximum can be raised to 20% upon approval of the Prime Minister (HSBC has a 20% stake in Techcombank, for example). Total overseas ownership of existing commercial banks cannot exceed 30% in aggregate, however. Maximum overseas ownership in a joint venture bank is 49%, while nonfinancial companies and other nonstrategic investors are limited to a 5% stake in commercial banks.

Strategic overseas investor is defined here as an investor who not only provides capital, but also commits to helping the bank it is investing in to develop products and services, and to providing management support (risk management, liquidity management, and building an IT platform) and help improving corporate governance. In addition, to ensure their long-term commitment to Vietnam and prevent speculative, short-term financial investments, they are prohibited from transferring their stock for a period of five years[25]. Foreign banks' participation in the Vietnamese market used to be restricted to either taking a minority interest in a joint venture bank or establishing a branch or representative office, but a 2004 revision to the 1998 Law on Financial Institutions and a directive issued in 2006 made it possible to establish a wholly foreign capitalized bank that can compete on an equal footing with domestic banks.

Next was a strengthening of capital requirements aimed at making the banks more financially sound, by setting minimums for amount of capital and capital ratios. The minimum amount of capital for an overseas bank to open a branch in Vietnam is $15 million, and the requirements for establishing a bank wholly owned by a foreign bank are minimum capital of 3 trillion dong, total assets of $20 billion in the year prior to application, and the parent bank taking at least a 50% stake in the new bank[26]. The initial plan was for commercial banks that did not meet these requirements by end-December 2010 to either be made into a joint venture, have its services limited, or its license revoked, but only 20 banks actually met the requirements, while 29 could not in light of the weak stock market. This resulted in the deadline being extended to end-2011. Nevertheless, it remains difficult for most small commercial banks to attract investment, and given the stock market's weakness, we think industry consolidation is likely. Regulators have proposed raising minimum capital to 5 trillion dong by 2012 and again to 10 trillion dong by 2015[27].

With an eye on eventually adopting Basel III rules, they raised the capital requirement in October 2010 from 8% to 9%. Furthermore, to improve liquidity, they have placed limits on investing in securities and on writing loans for real estate businesses[28].

The other main restrictions on activity and type businesses are as follows. To begin with, because Vietnam has universal banking and thus no restrictions on services, domestic commercial banks can enter such businesses as insurance, securities trading, and financial leases, and there is no restriction in principle against their taking stakes in other financial institutions. Domestic commercial banks are limited in the number of branches they can open based on their capital, but those restrictions do not apply to foreign banks or joint venture banks[29]. Interest rate restrictions were liberalized in

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25 The period in which transfer of stock is restricted is shortened to three years for nonstrategic overseas investors.

26 Based on Decree 141/2006/ND-CP. An overseas firm must have total assets of at least $20 billion to take a 15% or greater stake in an existing state-owned commercial bank, and this has been cited as one factor slowing the privatization of state-owned commercial banks.

27 “Vietnam: 2010 Article IV Consultation – Staff Report and Public Information Notice”, IMF, September 2010

28 Based on Circular No.13/2010/TT-NHNN.

29 Based on State Bank of Vietnam Decision 888 of June 2005.

2001 for foreign-currency-denominated loans, in 2002 for dong-denominated loans and deposits, and in 2007 for dollar-denominated deposits. In accordance with Article 128 of the Law on Financial Institutions, foreign banks are prohibited from lending more than 15% of their capital to a single customer (although loans to other financial institutions are excluded from this restriction), unsecured loans and loans at favorable terms to related firms[30] are not allowed, and loan amounts are limited to no more than 5% of capital.

Further structural reforms of the banking sector came in 2006 with Prime Minister Decision 112, which improved corporate governance, promoted the disposition of nonperforming loans, strengthened asset liability management, enhanced the supervisory function, and pushed further use of IT. The supervisory functions are currently separated, with banks and nonbanks under the central bank, insurance companies under the Ministry of Finance, and securities brokerage firms (and fund managers) under the State Securities Commission of Vietnam, which reports directly to the Ministry of Finance, but that Decision also directed that the establishment of an integrated financial regulatory body to handle all of these functions by 2020 to be taken under consideration.

2. Capital markets

1) Market structure

As with other emerging markets, indirect finance is the predominant means of financing in Vietnam, but capital markets initially created in 2000 began growing rapidly from 2005. Over the last few years, in particular, the central bank's monetary policy has consisted of a series of interest rate hikes aimed at stemming inflation, and large companies with good credit are likely to increasingly turn to capital markets for their funding needs.

Capital markets in Vietnam have a short history of not much more than a decade. Pursuant to a directive handed down in July 1998[31], it was decided to open securities exchanges in Ho Chi Minh City and Hanoi to encourage industrial modernization, promote competition among domestic firms, and achieve greater business efficiency. The Ho Chi Minh City Securities Exchange (HOSE)[32] began operations in July 2000, and the Hanoi Stock Exchange (HNX)[33], which primarily deals in government bonds and the stock of mid-sized startups, was established in 2005. A tax incentive that exempted firms from corporate income tax for the first two years after they were listed expired at the end of 2006 and policies encouraging IPOs were introduced, resulting in more than 150 companies going public in 2006. The number of listed

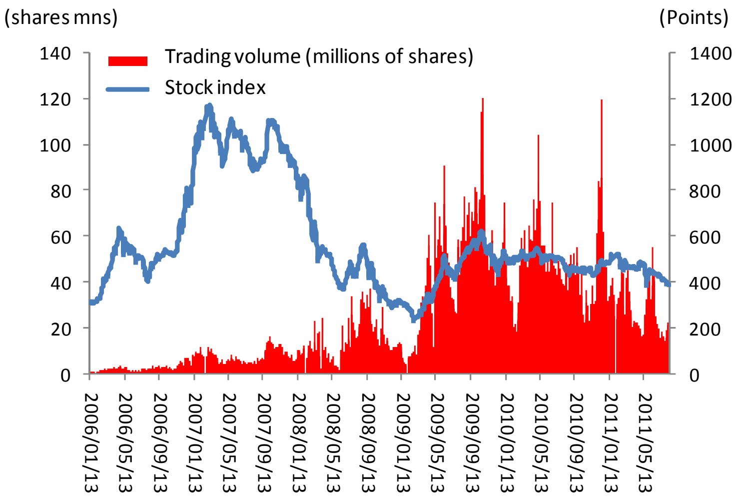
[30] Defined as companies whose major shareholder and directors' own at least a 10% stake.
[31] Based on Decision No.127/1998QD-TTg.
[32] The predecessor of HOSE was the Ho Chi Minh City Securities Trading Center (HSTC).
[33] The unlisted shares of at least 3000 firms are traded over the counter, including stock issued to the employees and customers/suppliers of state-owned enterprises converted to joint stock corporations, and in 2007 the Ministry of Finance issued Decision 3567, establishing the UPCOM market in 2009. To protect investors, the government is working to strengthen disclosures on unlisted stocks with a scarcity of information.

companies continued to increase[34], and as of end-September 2011 there were 295 stocks[35], 47 corporate bonds, and five mutual funds listed on the HOSE, and 388 companies listed on the HNX. As of 13 September 2011, market capitalization was approximately $24.9 billion on the HOSE and $5.1 billion on the HNX, for a total of approximately $30 billion, equivalent to 30% of Vietnam's GDP.

Vietnamese stocks have underperformed the stocks of other ASEAN countries since the financial crisis. The VN-Index, a market cap weighted average of the stocks listed on the HOSE, had risen to nearly 1200 points in 2007, after Vietnam joined the WTO, but following the financial crisis had dropped sharply to 235 points by February 2009, and it has yet to recover its pre-crisis level (Figure 10)[36]. Nevertheless, some of the local players we interviewed opined that because what look to be attractive valuations are likely to increase acquisitions by overseas investors, there should be growing opportunities in the investment banking business.

In addition, as is the case in other emerging markets, Vietnam's stock market is highly concentrated, and not that liquid. The top 40 companies by market capitalization account for over three-fourths of the entire market, and both market capitalization and turnover are between 30% and 40% of GDP, lower than in other countries in Southeast Asia.

Figure 10: Share price performance in Vietnam



	P/E ratio (August 2011 average)
Malaysia	17.4
Indonesia	29.2
India	17.6
Vietnam	8.1

Source: Nomura Institute of Capital Markets Research, based on Bloomberg data

34 The IPO schedule of Vietnam Airlines and other state-owned firms has been delayed considerably by the weak stock market.

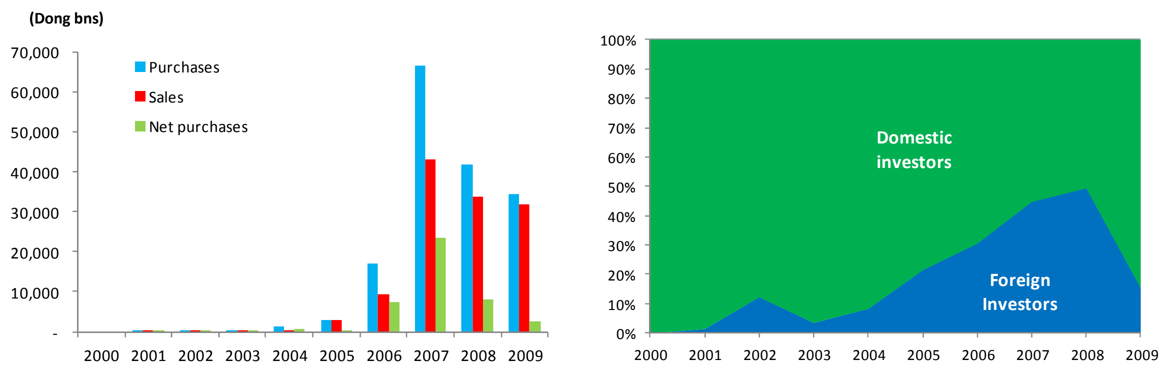
35 The five largest companies based on market cap (in order, the Masan Group (Vietnam's largest conglomerate), Baoviet Insurance, Vietnam Dairy Products, the real estate company Vincom, and Asia Commercial Bank) account for nearly 40% of total market capitalization.

36 The P/E of the VN-Index was considerably higher than that of the MSCI Emerging Markets Index from 2006 to 2007, but Vietnam's stock market probably was just experiencing a bubble, given its pullback since the financial crisis.

There were over 100,000 investor accounts at end-2006, but that grew to approximately 300,000 in 2007 as a result of a sharp increase in portfolio investment from overseas following Vietnam's entry into the WTO, and topped 1 million accounts in 2010. As noted earlier, however, because the stock market is currently weak and unlikely to generate a better return than the roughly 14% interest rate offered on bank deposits, individual investors have been shying away from the stock market. Furthermore, these individual investors have a low level of investment literacy, and are easily swayed by the herd instinct[37]. Individual investors account for the bulk of stock trading in Vietnam and make speculative, short-term trades, behavior that tends to drive market volatility higher. In contrast, market participation by domestic institutional investors like pension funds and insurance companies[38] is still low. Trading activity by overseas investors began rising sharply in 2005, growing to account for nearly 50% of all trades by around the time of the financial crisis, but by end-2010 that share had fallen to around 20% (Figure 11).

The size of the bond market as of end-September 2011 had grown 22% YoY to 353 trillion dong (approximately $17 billion), which equates to roughly one sixth of GDP (Figure 12). Government bonds account for about 90% of that total at 321 trillion dong (about $15 billion), with corporate bonds comprising the remaining 32 trillion dong (about $2 billion). The corporate bond market, although still small, is growing rapidly, with issuance outstanding up 35% relative to 2010, versus only 21% growth in government bonds. Looking at the maturity structure of government bonds, over half have a remaining maturity of less than three years, while long-term government bonds with a maturity of at least 10 years went from accounting for nearly half of all

Figure 11: Trading in stocks by overseas investors



Source: Nomura Institute of Capital Markets Research, based on Ho Chi Minh City Securities Exchange's annual report and other materials

37 Our interviews locally suggest that the core individual investors are principally active traders classified as wealthy, a group that accounts for 60% of trading volume.

38 In June 2005, Vietnam established the State Capital Investment Corporation (SCIC), a sovereign wealth fund modeled on Singapore's Temasek Holdings. SCIC's primary objective is to strategically invest in the reform of state-owned enterprises and critical industries. Its portfolio includes stock in over 700 companies, primarily in the financial, telecom, transportation, consumer goods, healthcare, and IT sectors.

bonds seven years ago to only about 5% now (Figure 13). The average government bond yield is around 12%, and the biggest bondholders are domestic commercial banks, which in principle hold to maturity. In contrast, the primary holders of corporate bonds are the insurance companies[39].

The government bond market grew suddenly in October 2005, when it successfully floated a global offering for $750 million. The corporate bond market, where most of the major issuers are state-owned enterprises, was expected to grow following the easing of issuance requirements in 2006[40], but the market remains small and illiquid, with nearly 90% of issuance privately placed. Impediments to development of the corporate bond market on the supply-side include insufficient ratings from credit rating agencies, the absence of market makers, the lack of yield curve indices, and the small number of corporate bond types being traded[41], while on the demand side impediments include the thin investor base in the absence of participation by pension funds, mutual funds, and other institutional investors. Because the effort involved in preparing a prospectus for issuing a bond is not much different than that for issuing stock, and because there is no real advantage in terms of issuance costs, there is no incentive to use corporate bonds in terms of fund raising efficiency.

As part of the initiative modeled on the EU for an ASEAN Economic Community, the region's capital markets are scheduled to be integrated by 2015, with the ASEAN Trading Link set to launch in 2012. Initially, stock traded on exchanges in Singapore or Malaysia will be tradable on either exchange starting in June 2012, and stocks in Thailand will be added in August. Stocks from the Philippines will be added later, while Indonesia and Vietnam are still waiting on approval from regulators. Vietnam probably needs to work hard to maximize its use of such infrastructure as Asean

Figure 12: Bond market issuance outstanding

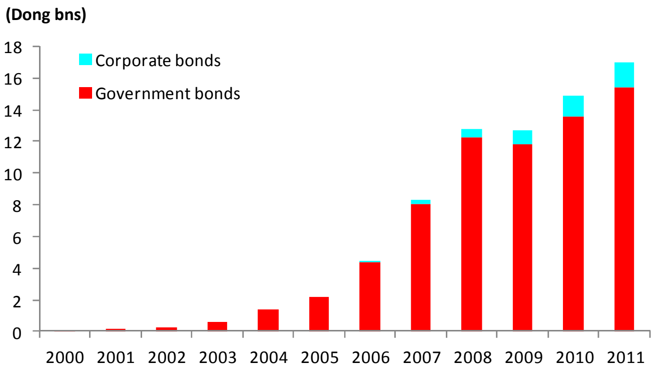
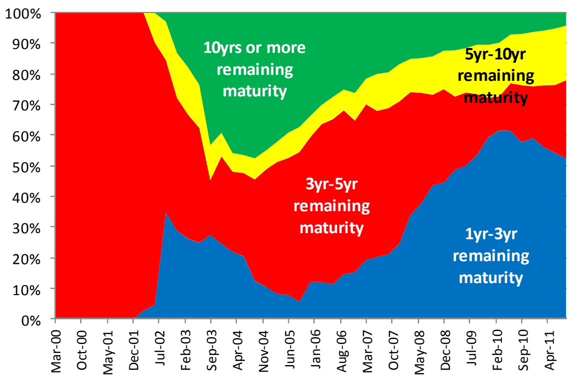


Figure 13: Government bond maturity structure



Source: Nomura Institute of Capital Markets Research, based on data from the Asia Development Bank

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39 IFC, "Vietnam Capital Market Diagnostic Review", August 2007

40 Based on Decree 52/2006As an example, because previous rules required issuers to have recorded profit for three consecutive years and be underwritten by a credit institution, only 10 companies actually issued corporate bonds.

41 The most common type of corporate bond issued is a simple straight bond, but local interviews indicate that demand has recently been rising for convertible bonds and other equity-linked bonds.

Trading Link, attract some of the investment funds flowing into the ASEAN region, and further increase the liquidity of its capital markets.

2) Competitive environment

The number of brokerage firms in Vietnam has grown rapidly, faster than the market itself. What consisted of 14 firms at end-2005 had grown to 105 firms by end-2010, an excessive number, even compared with other countries in Asia, when considering the size of its stock market[42]. Because upon joining WTO Vietnam committed to allowing the establishment of wholly foreign-owned brokerage firms starting in January 2012, industry consolidation will undoubtedly accelerate moving forward, and the State Securities Commission of Vietnam (SSC) also wants a consolidation of the overcrowded industry.

The largest brokerage firms are the independent Saigon Securities and Ho Chi Minh Securities, followed by the bank-affiliated ACB Securities (under Asia Commercial Bank) and Sacom Securities (under Sacombank)[43]. Online brokerages include FPT Securities, part of the FPT Group, Vietnam's largest IT firm, and the insurance company affiliated Baoviet Securities. The largest foreign-capitalized player is Kim Eng Vietnam Securities, a subsidiary of the Kim Eng Group, a Singapore-headquartered firm with operations throughout the ASEAN region (Figure 14)[44].

The top 10 players have more than a 50% share of the securities brokerage market, with the remaining 95 firms competing intensely to divide up the other half of the pie.

Domestic securities firms are primarily in the brokerage business, but many are expanding their investment banking businesses, including proprietary trading, the private placement of bond issues, IPO advisory, and M&A[45]. Although revenue from, for example, advisory services may be very small, the objective is to increase brand awareness among investors by offering a full line of services. Our local interviews suggest that although the performance of brokerage businesses has deteriorated as a result of the weak market, some of the firms have been expanding their online trading platforms. All of the firms are apparently trying to alter their earnings structure to become less vulnerable to external factors.

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42 Vietnam had 105 brokerage firms as of end-2010, the third most behind Indonesia's 119 and China's 107, but the capitalization of its stock market is less than 1% that China and less than 10% that of Indonesia. One of our local interviewees thought the number of brokerage firms may decline from 105 down to around 35 in the future.

43 Our local interviews suggest that the top 10 commercial banks own nearly all of the brokerage firms.

44 Foreign capitalized firms are entering the business by forming joint ventures with local brokerage houses. Daiwa Securities, SBI Securities, Dragon Capital from the UK, Morgan Stanley, and Citigroup have all done so.

45 Pursuant to Ministry of Finance Decision No. 38/2011/TT-BTC, the commission rate for trades of stock (including unlisted stock) and beneficiary certificates is between 0.15% and 0.5% of the transaction price, and for the underwriting of stock is between 0.5% and 2% of the value of the deal.

Figure 14: Leading securities brokerages

($ mns)

Company	Affiliated with	Market share	Sales	Market cap	ROE	Main products and services	Notes
Saigon Securities	Independent	12.4%	75	351	12.6%	1. Security services, asset management, investment banking, proprietary trading, research, and investment advisory 2. Retail services: brokerage, transaction support, online transactions, market research, portfolio management, and investment trusts	1. Building strategic investor relationship with Japan's Daiwa Securities 2. Voted Vietnam's best brokerage house three years straight by FinanceAsia 3. The leading domestic securities brokerage among overseas institutional investors (with over a 30% share of the brokerage business with overseas institutional investors) 4. Has 470 employees and 54,000 customer accounts
Ho Chi Minh Securities	Independent	7.7%	24	95	11.7%	Brokerage and sales, research, investment banking, and proprietary trading	1. Based on Ho Chi Minh City's master plan for developing the financial industry, established the Ho Chi Minh City Investment Fund for Urban Development in April 2003. 2. Leading shareholders: Ho Chi Minh City Finance and Investment State-owned Corporation (30.4%) and Dragon Capital (30.97%)
Thang Long Securities	Military Commercial Bank	7.5%	65	N/A	4.6%	Brokerage, investment advisory, custodian services, securities underwriting, and investment banking	1. Established in 2000 by the Military Commercial Bank, it is one of Vietnam's first five securities brokerages 2. 600 employees
ACB Securities	Wholly owned subsidiary of Asia Commercial Bank	5.0%	25	N/A	16.7%	1. Online transactions 2. Research 3. Brokerage and investment banking (overseas institutional investors and individual investors)	1. 60,000 clients 2. 250 employee
Sacom Securities	Subsidiary of Sacom Bank group	4.9%	69	51	6.1%	Brokerage, corporate advisory, investment banking, research, and investment advisory	1. Brokerage accounts for less than 10% of revenue 2. Has 44,216 individual investor clients 3. 350 employees
FPT Securities	Subsidiary of FPT Group, a leading IT firm in Vietnam	3.6%	11	N/A	2.0%	1. Securities brokerage 2. Proprietary trading 3. Investment advisory 4. Custodian services and securities underwriting	1. SBI Holdings acquired 20% of outstanding shares in November 2010 2. Sales figures based on SBI Holdings press release
Baoviet Securities	Baoviet Insurance Group	3.1%	12	62	6.5%	1. Brokerage (individual investors and institutional investors) and research 2. Custodian services 3. Investment banking and financial advisory 4. Proprietary trading	1. The first in Vietnam to acquire a securities industry license, established in 1999 2. Established BVS@Trade, an online trading platform, in 2010 3. Over 40,000 securities trading accounts
Viet Capital Securities	Independent	2.8%	19	N/A	16.0%	1. Investment banking 2. Research and brokerage services	1. 111 employees 2. Majority of revenue comes from proprietary trading 3. Brokerage accounts for about 10% of total revenue
Kim Eng Vietnam Securities	Kim Eng Group	2.8%	6	N/A	5.6%	1. Brokerage and research 2. Custodian services 3. Investment consulting 4. Securities underwriting 5. Corporate finance	1. Established in 2007 2. At least 100 employees 3. In a strategic alliance with Kim Eng Securities and Mitsubishi UFJ Securities 4. Not involved in proprietary trading
VPBank Securities	VPBank and OCBC Bank	2.8%	N/A	N/A	N/A	1. Investment banking (stock and bond capital markets division, M&A advisory, and corporate turnaround services) 2. Securities brokerage and proprietary trading	1. Established in 2006 to enhance VPBank's investment banking business 2. Financial data unavailable

Note: Market shares based on H1 2011 trading data published by Ho Chi Minh City Securities Exchange. Financial data is the most recent available.
Source: Nomura Institute of Capital Markets Research

Based on data from the World Bank, Vietnam has an estimated 25 million Internet users, roughly 30% of its population, and this represents 100-fold growth over the past 10 years. Internet usage is growing at a faster pace in Vietnam than in neighboring Thailand and the Philippines, and there are private-sector surveys indicating that half of the population in urban areas, primarily relatively wealthy young people, access the

Internet on a daily basis[46]. This suggests there is ample room for growth in the proportion of trading conducted online, currently said to be less than 20% for retail investors, and there are some securities firms for which online trading already accounts for half of their brokerage income.

Most of this trading is of simple cash equities, but demand for derivatives and other new financial products is growing[47]. Currently, however, the securities firms have not yet put sufficient systems in place on the supply side, while back up on the regulatory side is also lacking[48]. The foreign-capitalized firms entering the market are expected to increase the use of derivatives and other new financial products, and this should raise the level of financial product expertise among local firms.

Many of the local firms, facing major competition from the entrance of foreign firms, are being forced to secure medium- to long-term funding and refine their medium-term business plans in order to ensure their survival moving forward. When seeking alliances with foreign firms, they must decide between offering an equity stake or just forming a business alliance. Furthermore, to prevail under highly competitive conditions, they will probably need to strengthen corporate governance, seek thorough compliance, improve risk management, avoid reputational risk by adhering closely to standards of conduct, and establish corporate brands.

Over the longer term, if market mechanisms work to expel inefficient firms and make it easier for the survivors to attain critical mass, securities firms with a strong financial base and the ability to offer quality services should emerge, and this would probably create a desirable environment for investors. We heard the same opinions on this in our local interviews.

3) Mutual funds

The mutual fund sector is small and still developing. According to SSC data, asset management companies in the onshore business had aggregate sales of 600 billion dong (roughly ¥2.4 billion) and net profit of $200 billion (approximately ¥800 million) in 2010. There were apparently 47 asset management companies as of end-2010 (see Figure 15), with assets under management of over 100 trillion dong (about ¥400 billion)[49].

46 http://www.cimigo.vn/en-US/WhatIsNew/2010-01/cimigo-releases-report-about-internet-usage-in-vietnam-netcitizens-report-2011.aspx

47 Margin trading and short selling, prohibited by law until August 2011, are now allowed, and expected to grow.

48 Under the suitability and "Know Your Customer" rules, in principle Vietnam's securities brokerages must make one confirmation phone call after receiving signed agreement documents from the customer before opening a trading account. There is no obligation to apply in person, and trading accounts can be opened online.

49 “Stock Market: Vietnam Fund Management Firms Post Profit of VND200B in 2010”, Vietnam News Brief Service

Figure 15: Leading asset management firms

Fund management firm	Registered capital (dong bns)	Year license acquired
Viet Nam Investment Fund Management	210	2009
Viet Capital Asset Management	150	2006
FPT Fund Management	110	2007
MB Capital Management	100	2007
PVFC Capital	100	2007
Thanh Viet Investment Fund Management	88	2004
Saigon - Hanoi Fund Management	60	2008
ACB Capital Management	50	2008
IPA Securites Investment	50	2008
Minh Viet Capital	50	2008
RNG Fund Management	50	2008
Viet Nam Alliance Fund Management	50	2008
Vietinbank Fund Management	50	2010

Source: Nomura Institute of Capital Markets Research, based on SSC data

It appears that all of the funds are currently of the closed-end type[50], and there are five funds listed on the Ho Chi Minh City Securities Exchange, with a turnover in 2009 of about 7.2 trillion dong (¥30 billion). The SSC was set to announce guidelines for establishing open-end mutual funds, demand for which is rising, by end-2011, and the establishment of mutual funds, retirement funds, and ETFs may take off. On the other hand, capital markets have performed poorly, and speculation is rife that there will be an exodus of money from many mutual funds coming up on redemptions in 2012 to 2013. Many market participants fear that nonresident investors will withdraw their funds, citing problems with Vietnam's macroeconomy.

There is also a possibility in the near future that the SSC will consider offering tax incentives to encourage greater participation in mutual funds and the many retirement funds targeting younger workers.

Although there is no data available on mutual fund sales channels, sales are "open architecture," and we think the primary sales channels are insurance companies, securities companies, and banks. With sales strategies increasingly turning to banking sales channels, we think it likely that banks will play a central role in distribution in Vietnam, where independent investment advisors are nonexistent.

50 Under the Securities law, there are two types of mutual funds in Vietnam. There are public funds, of which there are both closed-end and open-end varieties, and there are member funds. Public funds must be valued at at least 50 billion dong after listing and be registered with the SSC. In contrast, member funds can have up to 30 investors, all of whom must be institutional investors, and although there is no requirement for registration regulators must be notified of their establishment.

4) Related legislation

The primary regulator of securities markets is the SSC, which was established in November 1996 and placed under control of the Ministry of Finance in February 2004. The SSC has primary responsibility for overseeing and developing capital markets, specifically by (1) proposing strategies to develop Vietnam's securities markets; (2) devising and implementing securities-related regulations; (3) overseeing stock exchanges; (4) licensing and supervising securities companies, investment advisory companies, asset management companies, and custodian institutions; (5) supervising and checking the compliance of issuers, investors, and other market participants; and (6) licensing and training certified securities industry professionals[51]. Nevertheless, the SSC appears to lack independence, supervisory capabilities, and the ability to enforce related laws, while compliance by the securities firms is not very thorough, primarily owing to inadequate employee training. The penalties placed on securities firms for legal infractions are mild, and the industry overall seems to lack the mechanisms needed to build highly transparent securities markets that overseas investors can trust.

The 2006 Securities Law, enacted on 1 January 2007 to strengthen securities regulation and ensure the orderly development of securities markets and entrance into the WTO, is the center piece of the legal framework for securities markets. The Securities Law, incorporating IOSCO principles, emphasizes market monitoring, transparency, disclosure, and investor protection. Rules related to securities firms, including suitability rules and the separate management of client assets, are covered under Decision 27, the operation of asset management firms is covered by Decision 35, the establishment and investment of mutual funds by Decision 45, and rules on corporate governance applied to listed firms by Decision 12.

The maximum equity stake allowed for foreign capitalized firms[52] is 49% for listed and unlisted large companies[53] (30% for listed banks), although that rule will be abolished from 1 January 2012 as part of Vietnam's commitment to the WTO, thereby allowing the establishment of wholly foreign-owned securities companies[54]. In addition, to prevent holding companies from simultaneously controlling multiple securities firms, Decree 14 states that individuals holding at least 10% of the stock of a securities firm cannot hold 5% or more of the stock of a different securities firm.

The minimum capital requirements are 25 billion dong for the securities brokerage business and 165 billion dong for the securities underwriting business[55], and a company must meet three conditions in order to get a license from the SSC: (1) have the facilities needed to provide service, (2) meet the minimum capital requirements,

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51 Based on Decision 63/2007/QD-TTg. Decision No. 17/112/127 also touches upon the SSC's authority. HOSE and HNX also function as regulatory agencies in lieu of the SSC for exchanges and market participants.

52 There are no restrictions on foreign ownership of bonds.

53 Public companies are firms that have at least 101 shareholders excluding professional investors and paid-in capital of over 10 billion dong.

54 Vietnam began issuing local branch licenses to foreign securities firms in 2011.

55 Other capital requirements are 100 billion dong for proprietary trading and 10 billion dong for securities investment advisory (Decree 144/2003/ND-CP).

and (3) have employees able to provide securities-related services without a problem. A license from the SSC enables a securities firm to engage in (1) the brokerage of securities trading, (2) proprietary trading, (3) securities underwriting, (4) securities investment consulting (research and investment advisory), and (5) investment banking services[56].

A roadmap for Vietnam's capital markets until 2020 was released in August 2007, with the challenges identified as the sustainable development of capital markets, the strengthening of competition, and the protection of individual investors[57]. Specific goals included raising the market capitalization of securities markets to 50% of GDP by 2010 and to 70% of GDP by 2020.

One recent development is the issuance of new guidelines on securities transactions[58] by the Ministry of Finance on 1 June 2011 aimed at raising stock market liquidity, including the formal approval for opening multiple trading accounts and trading on margin. The SSC plans to release more detailed guidelines on margin trading in the future, including on the initial margin requirement and maintenance margin requirement for listed stocks and mutual fund beneficiary certificates.

IV. Conclusion

Vietnam's financial markets are still young, not having really gotten started until about 20 years ago, and dominated by the banks, while its still small capital market is only 10 years young and still developing. With the full-on participation of foreign-capitalized firms sparked by Vietnam's joining the WTO in 2007, however, the capital market has grown rapidly, and the government is targeting growth to 70% of GDP by 2020. Progress toward the goal of economic integration of the ASEAN region by 2015 is moving forward, and with the integration of capital markets also accelerating as a result of the ASEAN Exchanges initiative, Vietnam will need a strategic framework to attract money from overseas investors and increase market liquidity. Economic growth is also getting underway in the neighboring countries of Cambodia, Laos, and Myanmar, and if their financial and capital markets become more developed it will probably further intensify the competition to attract overseas capital.

Vietnam's per capita GDP is just now surpassing the $1000 level, not a level that seems sufficient to give its people the financial wherewithal to invest in securities. With its extremely young population, however, Vietnam has a strong need for such retail financial services as Internet and mobile banking for IT-savvy younger individuals, particularly in urban areas, and if incomes and consumption grow in step with the economy, it is not difficult to imagine there being natural growth in demand for credit cards and ATMs. The government is doing its best to foster the development

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56 This includes corporate restructuring, corporate finance, M&A, IPO assistance, and valuation services.

57 No. 128-2007-QD-TTg

58 Circular 74/2011/TT-BTC

of the retail finance business, including by implementing policies to promote a cashless society.

To foster growth in its financial market, which has ample leeway for further development, over the near term Vietnam must put a priority on stabilizing the macro economy while gaining the trust of domestic and overseas investors and depositors, and over the longer term the industry will need to enhance its product offerings to match the diverse financial needs of individuals joining the ranks of the wealthy, improve customer service by thoroughly training employees, install IT platforms, and strengthen credit management systems. Overseas firms can help by providing not only capital but also management expertise during this process, and should play a very important role in the development of Vietnam's retail finance business.