CHAPTER 2
THE STOCK MARKET AND THE FINANCIAL SECTOR IN VIETNAM

2.1 An overview "Equitization program" and financial sector

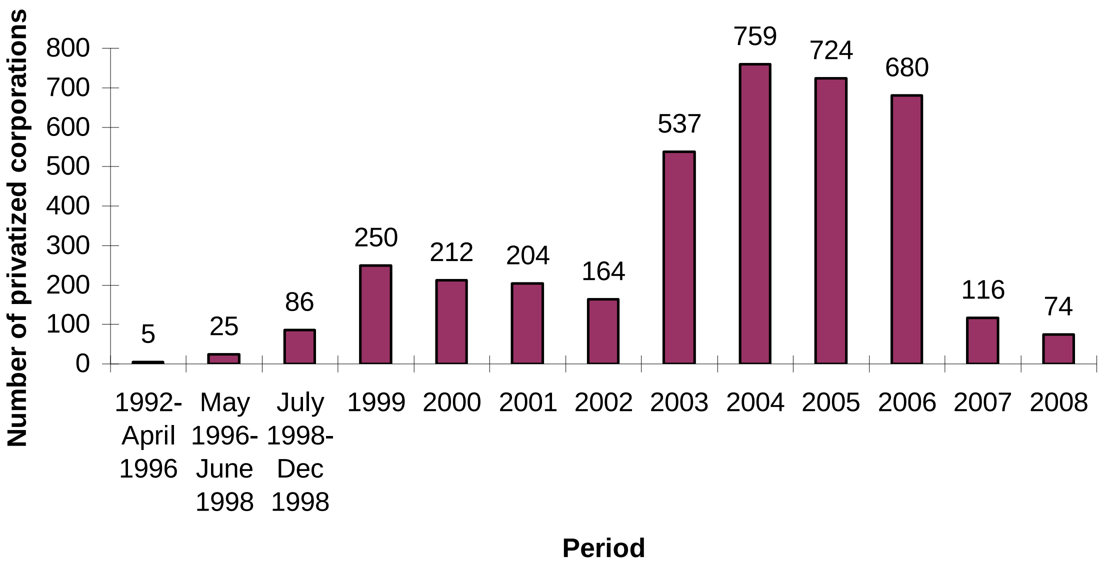
2.1.1 Equitization of state owner enterprises program

Since Vietnam reformed its economy from central planning (based on the pattern of Soviet Union) to open market in 1986, the whole economy faced many difficulties after the Collapse of Soviet and the government's budget had more burdens to support finance for tens of thousands of state owner enterprise (SOEs), included ineffective enterprises. Before the reformation, almost of them were government corporations, small and medium corporations. Their operation was based on the plan of local or central government that led to ineffective since they did not have any right to make their own decisions or to make more profitable for their business and their capital lost year by year; that lost had been covered by the government. Although the reformation started in 1986, but there were thousands of corporations should be bankruptcy, but the government still poured more finance to keep surviving; during 1997-1999, the government provided approximately 8,000 billions VND for SOEs (about 570 millions USD) in which there were 1,464.4 billions (116 billions USD) for covering the loss of SOEs. Additionally, during 1996-2000, the government had to exempt them 2,288 billions VND from taxes, clear 1,088.4 billions VND for outstanding debts, extend due date for nearly 4,000 billions VND of debts and support 8,685 billions VND with low interest rate. Those amounts were a heavy burden for the government's budget.

To reduce that burden, the government had implemented a program which namely is "Equitization of state owner enterprises program" started from 1992. The main purpose was not only to avoid of a heavily burdened budget for the economy, but also it had more objectives such as given more relaxed the independence for those enterprises – which were complicated and not transparent, and pushed the development of economy. Although the program started at beginning of 1990s, but the equities process was slowly at the beginning period, the period before the booming of stock prices (only 5 enterprises were equities during February 1992 to April 1996, and increase slightly to 25 enterprises from May 1996 to June 1998 (it was a surprise that there were 86 equities enterprises in second half of 1998), after that the number of equized enterprises was around 200 enterprises yearly to 2002. The government had forced the process with tighter policies to explore the program in 2003 with 537 joined enterprises and the program had more 759 and 724 new participants in 2004 and 2005, respectively. But in the period of 2006-2008, although there was a boom in stock prices, the participants in program reduced deeply; especially in 2008, there were only 74 new equitized companies, since many IPOs cancelled because of failure to get minimum requirement of investors in IPOs.

Figure 2.1

Number of equitized SOEs



Source: Ha, P., V. N. Anh, et al. (2006) and Vietnam economic portal[1]

[1] http://www.vnep.org.vn/Web/Content.aspx?distid=8291&lang=vi-VN

The government has a plan to privatize 950 government corporations from 2007-2010, but the result in the first two years of planning was not a good signal for that plan. It could be seen that the plan could not finish in 2010 as expectation, since the stock market has been affected from the soaring and falling during 2007-2008 and the newcomers could not pay a good attention from public as the current listed shares: the capacity of the stock market depends on the source of finance, but with a somber of the stock market from 2008, many investors who have loosen almost their money cannot come back to the stock market, it could not have more demand for new listed shares, that reason leads to failure of recent IPOs.

2.1.2 Main features of the financial sector

Before 1988, the banking system was only State Bank of Vietnam (SBV) as the central bank and commercial banks. After that, the banking system appeared four state owner commercial banks[2] (SOCBs) and SBV has implemented as the central bank. However, SOCBs officially were commercial banks, but they mainly focused on lending of SOEs until recent economic reforms. Since the ban of United States released in 1994, Vietnam had more opportunities to develop the economy, especially the financial sector. During 1990s, many joint stock commercial banks established based on credit co-operatives, which gave more opportunities for private sector to reach more finance resources to expand their business. By the commitment of Vietnamese government when Vietnam became a member of WTO in 2006, Vietnam has opened the financial sector to foreign investors and allows them to have a full operation in later years such as making lending, saving or buying stocks etc.

We could see that there were unfair for private sector for a long time, instead of supporting this sector to promote development of the economy, the financial sector served as a tool to keep survival for ineffective SOEs and consumed almost resources of the economy. Consequently, a large part of SOEs avoided of privatizing to continue receiving that support from the government in last years, although they were

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[2] Bank for investment and development of Vietnam (BIDV), Vietnam Bank for Agriculture and rural development (Agribank), The bank for foreign trade of Vietnam (Vietcombank) and Vietnam bank for industry and trade (Vietinbank). There are some local/ specific SOCBs served in some sectors based on the local development such as Vietnam social policy bank, Military bank, Mekong Housing bank…

not make profitable from their business. The private sector could only reach financial support from individual partners or from their relatives.

Before the establishment of financial market, domestic investors had not much channels to invest their money. For example, in the past, the most favorite investment was gold, most of Vietnamese kept their saving money in gold or “in cash” instead of opening a saving account in the bank. That situation lasted for a long time until 1993, when the first booming prices in real estate happened in Vietnam, domestic investors had one more channel to invest their money, but it was not a good channel until 2000; the explosive prices were occurred again in two main cities in Vietnam, Hanoi and Hochiminh received more FDI. Then investors could invest into other channels, currency exchange and the stock market. One main characteristic of domestic investors are “crowded trend”, because of lacking experience, most of investors follow the trend in the market (that reason explains some fevers in gold market, real estate, currency exchange[3] and the stock market, although they have no supportive/motivate information).

2.2 The development of the stock market

Although the equitization program began in 1992, but there was no official authority for the stock market until 1996 (the State Securities Commission was established in 1996); for the initial step, IPOs of SOEs were served for current employees and the government was a key shareholder. Then the first stock exchange founded in 2000 (the second stock exchange was Hanoi Stock Exchange (HASTC) , established in 2005 for small size corporations[4]). HOSE is a main stock exchange in Vietnam; it is served for IPOs and stock/treasury bonds trading, the individual

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[3] The exchange rate is decided by SBV officially, but in the market, investors sometimes push the exchange rate over the allowance of SBV for speculation illegally.

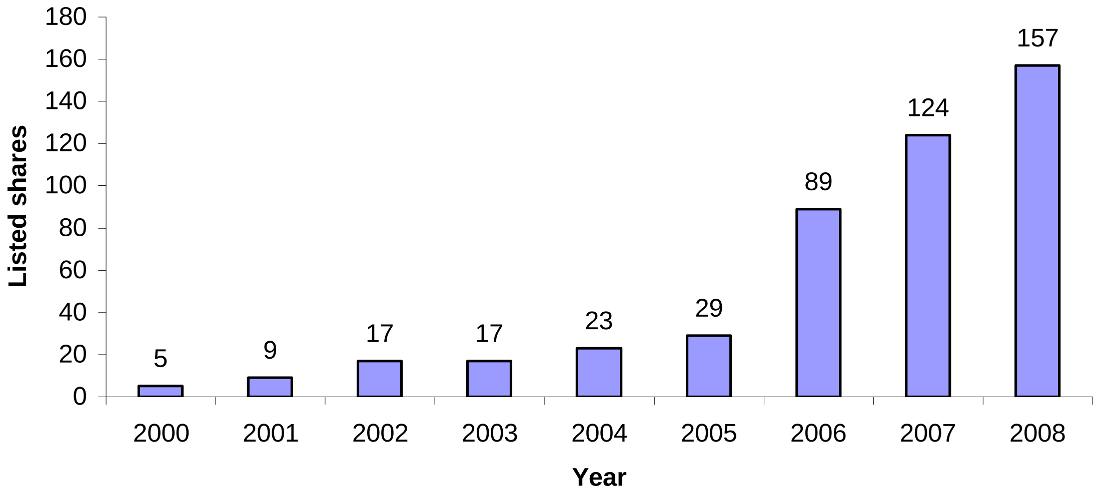
[4] Based on the Decision 14/2007/NĐ-CP dated January 19th 2007 required that HOSE is stock exchange for those corporations have more than 50 billions (about 2.9 million USD) of registered capital, and HASTC is for those are more than 10 billions VND (around 600 thousand USD) from 08 February 2009.

investors could bid for IPOs[5] as usual as their stock purchasing in HOSE, but for trading treasury bonds and government bonds, which only served for financial institutes.

From 2000 to 2005, HOSE increased its members slowly, as showed in following figure:

Figure 2.2

Number of listed shares from 2000-2008

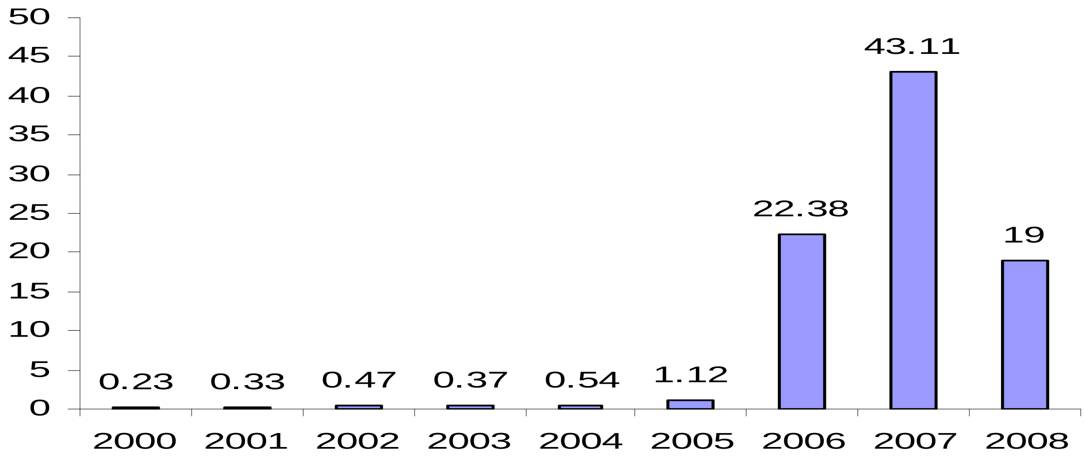


Source: Hochiminh Stock Exchange (www.hsx.vn)

[5] IPOs are as the primary market, in Vietnam, every individual investor and financial institute or foreigner (with a limited percentage) could participate to bid.

Figure 2.3

Market capitalization per GDP



Source: Hochiminh stock exchange (www.hsx.vn)

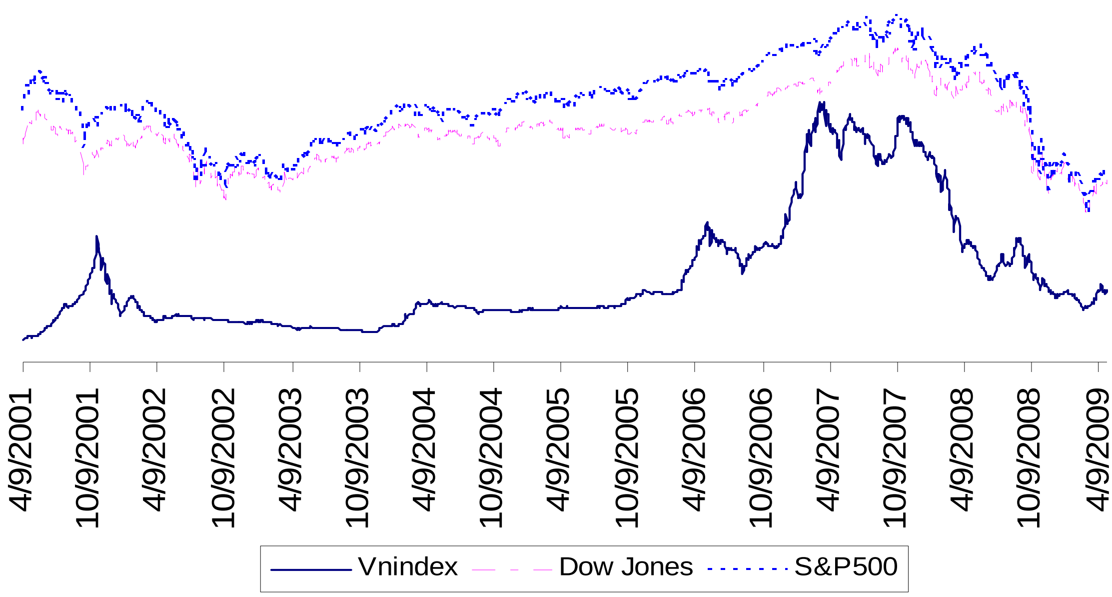
According to the number of equitized SOEs and of listed corporations, 324 listed corporations in 2008 (including 167 listed shares in HASTC), most shares of equitized SOEs are trading in OTC (over the counter), which is high risk and lower liquidity to investors.

As 8 years of operation, HOSE has improved itself period to period to adopt for the development of the Vietnamese stock market: at the first date, it only had two trading sessions per week to daily trading as present. The capacity of HOSE is increased year to year, it can be seen from the trading volume: it was a small volume in the first days (around 10,000 shares), then increased from one to two millions units in 2006, got ten time in 2007 (10-13 millions units approximately) and reached to 12-15 million units in 2008, as mentioned previous sections, this fluctuation was led by an increase of investors and the other impacts of "Equization program", FDI and credit growth in previous years. Although the trading volume increased, but the value is fluctuated according to the stock prices in each period; the trading value was from 0.176 billions in the first session to 1,066.422 billions VND (in the peak of VNindex, March 12, 2007) and fell to about 400 billions VND per session at the end of 2008 (and nearly 200 billions VND at the first quarter of 2009).

HOSE has signed corporation program to London stock exchange, New York stock exchange, Malaysia, Singapore, Tokyo, Hong Kong and Thailand stock exchanges for technical support and training, it also is an initial step for listing Vietnamese stock in those stock exchanges. Even that the Vietnamese stock market has no linkage to other foreign stock markets (Figure 2.3 will show the trend of VNindex to the stock market in United States, the study would like to attach two indices: the main index is Dow Jones and other is S&P500, in which the same trend from third quarter of 2008 was caused by the world economy recession, but VNindex has fallen down deeper than Dow Jones or S&P500), but it affected by foreign investors, since they could hold for maximum of 30% unlisted shares and 49% listed shares (that permission has been changed in 2009, foreign investors could hold 49% for any listed or unlisted shares); as Tung (2007) found that foreign investors' trading led the domestic investors to follow and made a crowded psychology in 2007, around 20-30% trading value of total market.

Figure 2.4

The trend of VNindex, Dow Jones and S&P500



Source: www.hsx.vn and www.finance.yahoo.com

Currently, the stock market is not presented as an indication of the growth of the economy, because it does not illustrate the performance of listed corporations, the fluctuation in the stock market was caused by investors' behavior as mentioned above. The fever in stock trading is a motivate for all stock prices increasing during the boom in a maximizing range, and almost of them fell during the post-booming period, and lost at least 30% in comparison to the prices in booming period. The listed corporations rarely increased their capital or got financial support from new issuance of shares, they preferred loan from the banks which they has been as traditional customers before equitizing with lower cost. Hence, the stock market is a channel to make more liquidity for their shares; they did not provide any long term commitment to their shareholders and investors cannot receive transparent information as their requirement.

Due to the fever in 2007, SBV would like to cool down the stock market via its instrument with an argument that securities corporations and commercial banks relaxed the stock lending during 2006-2007, especially the lending for IPOs: investors could use that share as collateral and get around 30-40%, SBV had a decision for securities corporations and commercial banks to reduce the stock loan for unlisted shares (7318/NHNN-CSTT dated August 25th 2006), then SBV increased the rate of risk for stock lending to 150%[6] (cash is 0%), this term was increased to 250% at the beginning of 2008 and the outstanding debt for stock loan did not allow to excess 20% of registered capital[7], those decisions also required securities corporations and commercial banks reducing their stock loan to make cool the fever in the stock market; in parallel, they had to reduce the current debts to under 20% which caused a sudden change in lending policy and pushed investors to refund their borrowing at the due date and to stop extending any new loan for investors. That made an unavoidable falling of stock prices.

As mentioned in chapter 1, SBV did not only require reducing the stock loan, it also has indirectly affected to the stock market: SBV raised the reserve for commercial banks to 1% for each kind of account and asked SOCBs to buy

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[6] Decision 03/2007/QD-NHNN dated January 19th 2007

[7] Decision 03/2008/QD-NHNN dated February 1st 2008

government bonds in the first quarter of 2008 with expecting to lower money supply in the economy, that requirement has left a burden for SOCBs and a competition of increase saving interest rate (in other side, it also increased the lending rate) to third quarter of 2008, during that period, most of commercial banks and financial institutes were lack of cash for their activities, that phenomenon was a pressure to pull down again the stock prices.