Discussion Paper
Vietnam Development Forum

VIETNAM'S FINANCIAL SECTOR ASSESSMENT

NECESSITIES AND REQUISITES

Working Group:

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Contact address:

Vietnam Development Forum *(VDF)*

10th Floor, Phuong Nam Bank Tower

27 Hang Bai, Hoan Kiem, Hanoi

Tel: 84-4-39362633 / Fax: 84-4-39362634

Email: *hellovdf@vdf.org.vn*

Website: *http: //www.vdf.org.vn*

TABLE OF CONTENTS

PREFACE

The Vietnam Development Forum (VDF) was established in 2004 under the cooperation project between the National Graduate Institute for Policy Studies (GRIPS), Tokyo and the National Economics University (NEU), Ha Noi. The purposes of the cooperation are to renovate research methodologies, to have policy impact, to build a bridge between academic research and policy making, and to implement action-oriented development research in Vietnam.

For these purposes, VDF cooperates with Vietnamese organizations and ministries such as the Ministry of Industry and Trade, the Ministry of Planning and Investment, the Ministry of Labour, Invalids and Social Affairs, the National Financial Supervisory Commission (NFSC), and so on, in many areas including industrial strategy, social security, environment, and banking and finance. Many research projects on development policy making of Vietnam have been conducted.

Within this activity framework, in October 2009, VDF signed a Memorandum of Understanding with NFSC to jointly study financial supervision and financial sector assessment. VDF and NFSC agreed to publish discussion papers and books that would serve as reference documents of the NFSC's key activities in financial supervision and financial sector assessment. The document entitled "ENHANCING FINANCIAL SUPERVISIONS – INTERNATIONAL EXPERIENCES AND RECOMMENDATIONS FOR VIETNAM" was published in 2011 as stipulated in the MOU.

In the agreed plan of the MOU, another document entitled " VIETNAM'S FINANCIAL SECTOR ASSESSMENT – NECESSITIES AND REQUISITES" will be issued as a discussion paper. This document will not only support NFSC's consolidated supervision functions over the financial sector but also contribute partly to the preparation of Vietnam's financial sector assessment. The document provides basic information on assessing properly the status of the financial sector, identifying weaknesses and problems in the financial sector, and addressing areas for improvement for long-term development of the financial market.

The document was prepared by the joint working group of VDF and NFSC with the following key members:

1. Prof. **Kenichi Ohno:** team leader, is a professor at the National Graduate Institute for Policy Studies (GRIPS), Tokyo and the Research Director of the Vietnam Development Forum (VDF). He graduated from Hitotsubashi Unversity and received a Ph.D. in Economics from Stanford University.

   He used to work at the International Monetary Fund and is the author and editor of a number of books on international and development economics, including *International Monetary Systems and Economic Stability (1991); Development Economics of East Asia (1997); Globalization of Developing Countries (2000)*.

2. Ph.D. **Nguyen Thi Minh Hue** is a researcher at the VDF and a lecturer of the School of Banking and Finance, National Economics University, Ha Noi.

   She received a Ph.D in Banking Supervision in 2010 from the National Economics University and graduated from the master course in the University of New South Wales, Australia, in 2005. She has nearly 10 years of experiences in research and conducting projects in banking and finance under the cooperation between Vietnamese organizations, including the State Bank of Vietnam, the Ministry of Finance, and the State Securities Commission, and international organizations such as the World Bank, the Asian Development Bank, and the Canada International Development Agency. As a researcher of the Vietnam Development Forum, Ms. Hue is the author of the book "Enhancing Financial Supervision – International Experiences and Recommendations for Vietnam."

3. MA. **Tong Quang Huy** is the head of the Financial Sector Supervision Policies Division and a senior expert of NFSC.

   Mr. Huy worked at the Banks and Non-bank Institutions Department of the State Bank of Vietnam for more than 10 years with the main duties of formulating the regulatory framework on regulation and supervision of financial insittutions; regulating and supervising directly financial institutions; and producing proposals for developing activities of financial institutions.

Mr. Huy was previously a civil engineer who graduated from Technology University of Budapest, Hungary (1986). He continued to study and research in the area of banking and finance and received a Bachelor in Economics in 1993 and a Master's degree in 2002. While working in the State Bank of Vietnam, Mr. Huy was trained professionally in management and supervision of financial institutions with short courses in foreign countries including United States, France, Austria, Singapore, and the Philippines funded by IMF, ADB and foreign central banks. In 2005, Mr. Huy took a 6-month internship of banking and finance at the headquarters of the Citigroup, one of the world's largest financial banking conglomerates, in the United States of America.

4. Ph.D. **Tran Thi Thanh Tu** is a lecturer of the Falculty of Finance and Banking, University of Economics and Business, Vietnam National University. Ms. Tu received her Ph.D. in Banking, Finance and Economics in 2006. With more than 10 years of experiences in research, teaching and advising, Ms. Tu interest topics are capital structure, restructuring enterprises and banking system; her papers published in professtional journals and international conferences.

This research also enjoyed the contribution, through comments and advice, of Ms. Pham Bao Khanh, head of the Banking Supervision Division and a senior expert at the Depository Insurance of Vietnam.

In our future plan, the working group will study concrete issues related to financial sector assessment in Vietnam, and conduct detailed research on the framework, content and objectives of Vietnam's Financial Sector Assessment based on the needs of the Vietnamese Government and the support of IMF and the World Bank in financial sector assessment. The other issue to be studied will be difficulties, obstacles, and problem-solving capacity of Vietnamese stakeholders in the implementation of Financial Sector Assessment.

Authors

CHAPTER 1:

OVERVIEW OF VIETNAM FINANCIAL SECTOR AND ITS' ASSESSMENT

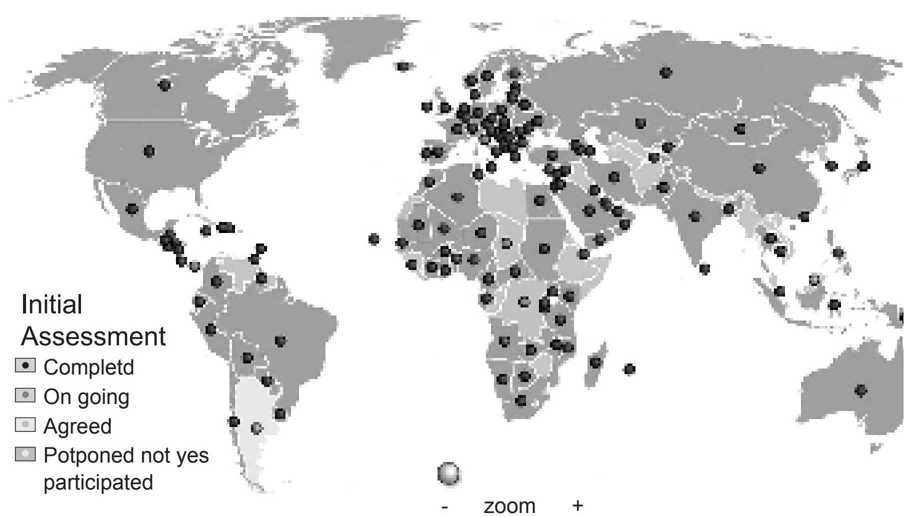
It can be seen that the financial sector in Vietnam has developed from a rather low starting point which can be counted as 0. Up to now, after over 20 years of financial sector reforms, fundamental components of the financial sector have been formed quite sufficiently in spite of unalike development degree of submarkets. Financial institutions have been developed in both quantity and quality; the legal framework for the financial sector development has been more improved on the basis of approaching to international practices. The State management in the financial sector has been gradually institutionalized. The cooperation of State management authorities in the financial sector has been better improved.

After four years of being a full member of the WTO, not only the quantity of financial institutions has increased but also types of financial services have developed dramatically in both quantity and quality. Banking activities have been open to non-banking financial institutions, credit funds, societies, unions, some ministries and several project performance organizations donored by foreign countries or non-governmental organizations, etc. The capital market has achieved certain development with a remarkable increase in the quantity of investment accounts as well as intermediates and market support organizations *(namely securities companies, fund management companies, etc.)*, particularly the bond market has more positive signs. The operation scale and scope of the insurance sector has developed. Types of insurance have developed variously with nearly 70 products of life insurance and non-life insurance. The insurance structure has gradually shifted from short-term to long-term. Also, more multi-purpose financial corporations have been founded with increasing interleaved activities. Generally, the financial sector in Vietnam has expanded its scale of operation and diversified types of financial products and services in every sub-sector, contributing considerably to the economic growth and development.

However, apart from obtained achievements, the financial sector reveals a number of weaknesses, shortcomings as well and potential risks, which are likely to result in major uncertainties or problems in operation of financial markets (such as credit markets, securities markets) in particular and the economy in general. This appeared obviously in the regional financial crisis in 1997-1998 and the global financial crisis in 2008, thereby operations of financial markets and enterprises generally ran slowly with low economic growth. The weaknesses and shortcomings partly originate from disproportioned and unharmonious development of the financial sector (banks and their operations play a dominant role); insufficient and asynchronous financial infrastructure (institutional and legal frame, information system, administration system, payment system, etc.); inadequate and incomprehensive observation and performance of international standards); etc. Moreover, a number of potential risks imply in important problems in the financial sector such as financial soundness of financial institutions on taking people's deposits; liquidity of the financial market (monetary market and capital market); and participants' transaction in the market. Interleaved risks currently imply among sub-sectors of the financial sector as well as financial corporations. Due to the fact that financial institutions are now in the process of establishment, the foundation of subsidiary companies and investment has not been adjusted in conformity to the law. The supervision and inspection systems have not been based on risks and therefore they will cope with challenges such as the development of financial corporations; the development of the capital market, especially the bond market will be related to all management organizations and authorities. This requires coordination and cooperation in the financial market.

The insufficient, incomprehensive and infrequent analysis of and assessment on the above mentioned matters will lead to improper decision on guidelines, policies and solutions. This makes the financial sector more chaotic, vulnerable and difficult to develop and especially makes potential risks arise easily. Particularly, the financial sector in Vietnam is integrating into the international financial sector more deeply at higher circulation level, and severe disruption in the financial sector is likely to occur. Therefore, Vietnam should deeply and comprehensively analyze and assess its financial sector as soon as possible annually. Thus, Vietnam should consider this a leading prioritized task in the coming time.

The assessment of the whole financial sector need to follow international standard instruction. Then, concrete works of financial sector assessment should be studied to match with the specific conditions and circumstance of Vietnam. Up to now, Financial Sector Assessment Program *(FSAP)* launched by the World Bank and IMF is considered as international manuals to every country. Under this program, FSAP is introduced in 1999 and now there are more than 130 countries parti cipated in this program and about more than 35 countries are implementing application actions. The results of the latest survey have shown that ¾ of the countries feedbacked positively and they reported that FSAP application in their country had worked efficiently. Especially, after some current crises, the countries of G 20 group have committed to assess their financial sectors following this program every 5 years.



Picture 1: Distribution map of FSAP members

Based on statistic data, the country applied totally all components of FSAP includes 23 American countries, 42 European countries, 31 Asian countries, 32 African countries and 4 Oceanic countries. Besides, the on-going countries are Angola, Benin (Africa), Sip Island (Europe); the agreed countries are Chad, Congo (Africa), SanMarino (Europe), Panama (America); the postponed countries are Brunei (Asia), Argentina (America). The not-yet-participated countries are Venezuela, Cuba (America), Vietnam, Lao, Myanmar…(Asia), Etiopia, Guinea,… (Africa)

It is clear that Vietnam is belonging to the small number of countries that have not participated in the FSAP program, while most of the participated countries have confirmed the efficiency and feasibility of the program. Therefore, studying FSAP and having actions in cooperating with international organizations to apply FSAP in Vietnam is an obvious trend in the development of Vietnam's financial sectors as well as the Vietnam's intergration into the regional and global market.

However, in order to carry out deep and comprehensive financial analysis and assessment, feasibility studies are required for performance without confusion and hindrances. Analysis and assessment results must be really useful for the improvement of the financial sector aimed at the stabilization and development of the financial sector – a sophisticated and diversified process, including the well-proportioned stabilization and development of three fundamental factors namely institutions, instruments and markets. Moreover, it is noted that the improvement of the financial sector must not be promoted beyond the overall development of the economy, meaning that the development should be synchronous, and of course, some prerequisites and infrastructure should be prioritized. We cannot be hasty as well as unruffled to wait enough sufficient prerequisites. As mentioned above, fundamental factors in the financial sector have a close relation.

CHAPTER 2:

INTERNATIONAL PRACTICES ON FINANCIAL SECTOR ASSESSMENT

Along with the integration and globalization, financial activities now not only occur in a country but also spread cooperatively among countries and regions. The guarantee of the sustainability of the financial system not only need performing individually by countries but also need cooperating internationally in order for the global stability and soundness. This appears obviously in the recent financial crisis (2008) that a country with uncertainties in the financial system faces with the financial crisis, it can easily spread the crisis to other countries or all over the world. Therefore, it is extremely essential to establish standards on management and assessment of the financial sector and financial system for all countries. Moreover, information should be shared and proclaimed to the international community by countries so that international organization *(WB, IMF, etc.)* can quickly realize or forecast development trends or fluctuations in each region or in the globe.

Arising from the demand, the World Bank has cooperated with the International Monetary Fund in conducting a research in order to give standard financial sector assessment. The research focuses on issues, as follows:

- Assessing and defining strong points, weak points and risks of the financial system

- Defining demands in financial sector development and technical assistance
- Assessing the supervision and application of international standards
- Assessing whether the supervision may finds out main causes of risks and weak points of the financial system
- Providing extremely vital infrastructure for financial sector development
- Supporting the development of necessary policies and feedbacks

The financial sector assessment program shows the international cooperation efforts in order to design standard criteria and develop common assessment method which is based on experts's experiences around the world. The program has been studied and applied widely in many countries in the world especially after financial crises in the 90s. However, after the recent crisis in 2008, the international community as well as each country realized again the necessity of the frequent assessment on the stability, soundness and development of financial sectors. Especially, the developing countries like Vietnam, the FSAP study and application should be done to follow other countries and to ensure the information transparency and soundness of the economy under the regional and global development

The main content of the program *(FSAP, 2005)* in compliance with WB/IMF instructions is summarized as follows:

1. Financial System Stability Assessment *(FSSA)* by IMF and WB

The development of international standards in financial sector assessment in order to ensure financial system stability is one of priorities of the FSAP. Specific objectives are to strengthen the legal system soundness; improve transparency of financial markets and institutions; develop financial infrastructure efficiently; provide more information for decision-making on investment and lending; enhance market integration; improve the reliability in policies and accounting system; and reduce risks leading to crises.

In order to obtain the objectives, the research team of the IMF and WB has established an international standard frame including 12 sectors to be assessed in the financial system.

The 12 issues are mentioned in Table 1 and classified into 3 main groups: (a) Transparency Standards ; (b) Standards on financial supervision and safety; and (c) Standards on financial infrastructure.

Focusing on standards on financial supervision and safety, consented supervision principles in financial sectors are as follows:

- Banking supervision: Core principles for effective banking supervision of the Basel Committee (BCP)
- Securities: Aims and principles for securities management of the IOSCO
- Insurance: Principles for insurance supervision of the IAIS
- Payment and settlement system: Committee on Payment and Settlement Systems (CPSS) with core principles for the most important and systematic payment system of the CPSS and recommendations of the IOSCO on the securities settlement system
- Anti-money laundering and financial anti-terrorism: Recommendations of the Financial Action Task Force (FATS) on Anti-money Laundering

Table 1: List of Standards and Codes and Core Principles Useful for Bank and Fund Operational Work and for Which ROSCs Are Produced

Transparency

- Data Transparency: the Fund's Specian Data Dissemination Standard/General Data Dissemination System (SDDS/GDDS)
- Fiscal Transparency: the Find's Code of Good Practices on Fiscal Transparency
- Monetary and Financial Policy Transparency: the Fund's Code of Good Practices on Transparency in Monetary and Financial Policies (usually assessed by the Fund and the Bank under the Joint Fund Bank FSAP)[a]

Financial Sector and Financial Integrity Standards[b]

- Banking Supervision: Basel Committee's Core Principles for Effecvive Banking Supervision (BCP)[a]
- Securities: International Organization of Securities Commissions' (IOSCO) Objectives and Principles for Securities Regulation[a]
- Insurance: International Association of Insurance Surpervisor's (IAIS) Insurance Supervisory Principles[a]
- Payments and Settlement Systems: Committee on Payment and Settlement Systems' (CPSS) Core Principles for Systemically Important Payments Systems and the Committee on Payments and Settlements Systems and IOSCO's Recommendations for Securities Settlements Systems [a,b]
- Anti-Money Laundering and Combating the Financing of Terrorism: Financial Action Task Force's (FATF's) 40+8 Recommendations[a]

Financial Infrastructure Standards[d]

- Corporate Governence: OECD's PrinciPles of Corporate Governance
- Accounting: International Accounting Standards Board's International Accounting Standards (IAS), currently called International Financial Reporting Standards (IFRS)
- Auditing: International Federation of Accountants' International Standards on Auditing
- Insolvecy and Creditor Rights: World Bank's Principles and Guidelines for Insolvency and Creditor Rights System and United Nations Commission on International Trade Law's (UNCITRAL) Legislative Guide on Insolvency Law.

a. These standards are assessed mainly under the FSAP.

b. Sometimes thre term financial integrity is used in a broad sense to cover both AML and CFT, as well as corporate gover-nance, transparency, accounting and insolvency regime, and the like. In this Handbook, integrity is used in a narrow sense of avoidance of financial crime, particularly money laundering, and financing of terrorism.

c. The payment and securities settlements standards covers supervisory elements, as well as design of payment settlement system, and may well be placed under financial infrastructure grouping

d. These infrastructure standards are mainly assessed by the Bank.

With widespread research and international cooperation, a handbook for the financial sector assessment has been developed with consent of international experts and agreed by all member countries. The handbook can be considered a standard document giving detailed guidance in the financial sector assessment, ensuring operation of a sound and efficient financial system.

Specific contents of the manual include:

(1) Necessities to assess the financial sector of a country

(2) Indicators on financial development, soundness and structure

(3) Assessment on financial stability

(4) Assessment on financial structure and stability

(5) Assessment on supervision on financial sectors: Banking, Insurance and Securities Market

(6) Assessment on supervision of other financial intermediates

(7) Management and supervision of micro and rural financial institutions

(8) Assessment on integration of the financial system, anti-money laundering and financial anti-terrorism

(9) Assessment on legal ground of the financial system

(10) Assessment on information and business management

(11) Assessment on the system liquidity

(12) Unification of financial system reforms

It can be seen that the mentioned contents are relatively comprehensive and sufficient, ensuring all activities and sectors of the financial system to be assessed and supervised, thereby the soundness and efficiency of the financial system are likely achieved.

2. Tools and skills required for financial sector assessment

The assessment on the financial system is aimed at developing an aggregated analysis related to financial stability and development, using a series of analysis tools and techniques such as:

- Analysis of the macro soundness supervision including: stress testing/scenario analysis, analysis on financial soundness indicators and macro financial relations
- Analysis of the financial sector structure including analysis of soundness, competitiveness, concentration, liquidity and access
- Assessment on supervision and observation of international standards, codes and guidance on the financial sector.
- Analysis of development and stability in country-specific circumstances (roles of State financial institutions, dollarization influences, causes of low development and untransparency of the securities market)

In this assessment, concepts of financial development and stability are considered in a broad sense. Thereby, financial stability includes: (a) an environment ensuring most financial institutions not to collapse and bankrupt; (b) conditions in order to avoid severe influences on main financial services in the economy such as people's deposits, investment, investors' securities, liquidity and settlement services, risk diversification, insurance services, management of funds and business management of non-financial companies. In addition financial development is aimed at intensifying and diversifying financial services to meet demand of participants in the economy efficiently, thereby fostering the economic growth.

With the concepts in a broad sense, financial stability of a country can be assessed from severe instability to sustainable stability level in the whole system. Similarly, the financial development is also assessed from the lowest level that is restricted development and only focuses on some specific financial sectors and functions to a higher level that is the comprehensive and harmonious development among financial sectors.

However, the financial development and stability should be considered in the interactive relationship. In specific circumstances, the assessment should carefully consider benefits of financial stability and costs of the maintenance of safe legal frame. Contrarily, the observation of policies on financial development can bring about macro risks and financial risks which should be taken into account and managed.

Along with goals of financial development and stability, a sound and well-functioned financial system should be considered and assessed three basic components, thereby necessary policies and actions should be developed in order for financial development and stability. The three components as basic indicators on assessment of a financial system are listed, as follows:

Component 1: Analyzing the financial stability and macro soundness supervision by competent authorities in order to control influences of institutional and macro elements (including subjective and objective elements) on financial soundness and stability.

Component 2: Making legal regulations and supervising the financial system in order to manage risks and damages, protect market development, supply dynamics for management of risks and financial institutions. Normally, guides on legal supervision and development for most of sectors in the financial system are all mentioned in standards which are internationally consented along with essential methods of assessment, only some sectors such as micro financial institutions have not been applied international standards.

Component 3: Assessing infrastructure of the financial system, including:

- Financial legal foundations, including mechanisms for insolvent financial institutions, rights of lenders, network of financial soundness.
- Foundations for liquidity of the whole system including activities in currency and monetary exchange, securities settlement and payment system, micro monetary structure, exchange rates and securities market.
- Foundations for transparency in information and management including policies on financial and monetary transparency, business management, auditing and accounting frame, mechanisms on information declaration, steps in market control for financial and non-financial institutions, credit report system.

It can be seen that the three components are all aimed at financial development and stability. Thereby, detailed performance steps should be developed in order to issue a handbook on detailed assessment which can be used by countries.

Step 1: Developing basic indicators on financial structure, financial sector soundness and development.

Accordingly, outlined guides on calculating systematic and aggregate indicators include (basic and broad) financial soundness indicators, indicators aggregated from the market on financial soundness and assessment indicators. Data resources for calculation of indicators are specifically defined. Detailed contents and scope of data are also specified according to circumstances of countries with particular structural and institutional features.

Step 2: Assessing financial stability.

This assessment includes not only qualitative assessment on risks and damages but also quantitative assessment on institutional capacities and financial foundations in order to manage risks. Quantitative assessment is mainly related to the overall control, analyzing institutional and economic elements which have impacts on financial soundness indicators (FSIs) of the banking sector, non-banking financial sector, and related non-financial sectors. The assessment and analysis on FSIs are macro safety supervision including stress testing, thereby defining major causes of risks and damages.

Step 3: Assessing financial structure and development

This is an assessment on functions of the financial sector including assessment on operation scope, concentration, efficiency, competitiveness, access and other factors related to institutional and economic factors. This focuses on analyzing factors leading to inefficiency of the market as well as hindrances in the economy resulting in the development and diversity of types of financial services. This analysis step is aimed at suggesting recommendations on changes in policies in order to make changes in financial infrastructure, supervision and legal regulations, thereby strengthening contributions of the financial sector to the economic growth and poverty reduction. Assessments in this part include quantitative analysis on financial structure and qualitative analysis on financial policies and institutions which affects the operation and financial sector structure.

Step 4: Assessing supervision on financial sectors such as banking, insurance and securities

This develops procedures on assessment of efficiency of financial supervision and regulation of banking, insurance and securities. Assessment indicators in banking are based on principles for effective banking supervision of the Basel Committee (BCP); in the insurance sector are principles for insurance supervision of the IAIS; and in the securities are core principles of the CPSS and recommendations of the IOSCO.

The standards on supervision gather core principles classified into 4 main groups:

- Legal frame on management: clearly specifying goals, functions, tasks, independence as well as decentralization of management authorities.
- Enforcement guides: including guides on observation of laws, regulations and procedures
- Frame on control and supervision: related to guides and regulations on internal control, management activities of supervised units.
- Financial safety and consolidation network: related to policies and instruments in order to improve impartiality and integration in activities of financial institutions, markets as well as authorities which protect depositors, investors and observers of policies during crises.

Step 5: Assessing other financial sectors including other financial intermediates, rural and micro financial institutions, anti-money laundering and financial anti-terrorism system

Step 6: Assessing legal infrastructure for the whole financial system related to assessment on codes such as law on central banks, law on banking, Government debt settlement and management system, capital market, insurance and financial safety network; law on enterprises, business management and regulations on protection of consumers, etc.

Step 7: Assessing infrastructure on information, management, settlement and reforms of the financial sector.

The above detailed guides are relatively sufficient to assess financial sectors and system of a country; however, it is essential to tailor properly to country-specific circumstances. For underdeveloped countries, attention should be paid to medium term development such as institutional completion and financial market development. Management, transparency and legal frame are major issues of an underdeveloped financial market. For the countries in which system linkage is considered important, particular attention should be paid to integration and linkage with other countries as well as impacts of globalization and consolidation. Countries are likely to have differences in structure as well as dollarization, operation scopes of state financial institutions, overseas banks, influences of "shocks", market discipline and internal management quality. All the differences require adjustment in priorities on aspects to be assessed as well as priorities on policy-making, policy efficiency measurement and unification of financial reforms.

3. Adjustment on financial sector assessment in conformity to country-specific circumstances

Countries with underdeveloped financial systems should focus more on medium term development such as institutional completion and financial market development. Overall issues of the financial sector in the countries should concentrate on specific aspects of financial development including banking supervision capacities; legal frame and laws on banking, non-banking institutions, payment system; credit information system; improvement of rights for lenders and debt payment mechanisms; regulation on accounting, auditing and information declaration; operation of central banks and monetary policy management; and banking restructuring. At the same time, factors which have impacts on some underdeveloped markets should also be analyzed in order to define essential issues in development of capacity and structure of a country.

Countries which have important systems should pay attention to cross-border issues. The countries are extremely vulnerable to a quick increase on overseas institutions; thus, they should focus on (a) essential steps in liberalization including prerequisites of institutions, and (b) ability of domestic institutions to struggle with increasing fierce competition during integration, especially countries participating in free commercial agreements or signing issues in financial services in the WTO.

In many countries, dollarization also causes financial risks which should be taken into consideration. Possibly, financial assessors and supervisors in a country should supply quantitative support information such as rates of foreign currency deposits and loans, circulation of currencies, foreign currency assets and liabilities of key financial institutions, net foreign exchange assets, and the state of net foreign exchange of banks *(Gulde, 2003).*

In countries which have no crises but severe financial issues that a major part of banks (or insurance companies or other credit organizations) cannot ensure sufficient capital and essential operations, financial assessors and supervisors should focus on impacts by shocks or reforms. The most negative impacts can be forecasted through stress testing or estimates on consequences of similar macroscopic events. When a macroscopic shock occurs, timely and sufficient financial restructuring can repulse crises *(Hoelscher and Quintyn 2003).*

For countries participating in the common currency union, financial assessors and supervisors should have deft actions in supervision responsibilities at national and cross-border levels (Van Beek 2000). Specifically, responsibilities in supervision on financial institutions should be taken at national level with regulations and laws such as debt classification, debt provision, licensing and other regulations on licensing market involvement. The control in cross-border transactions with the presence of 3 parties is unlike. Accordingly, monetary polices and rates in this case should be implemented at cross-border level including LLR function and solutions to crises.

For countries with the prevailing of Islam and remarkably affected by Islam, financial assessors and supervisors should consider if legal frame is sufficient to define and assess typical risks of Islamic Financial Services. Risks of Islamic Financial Services is possibly rather different from traditional financial services due to differences in designing and establishing financial tools based on Islamic Law – Sharia'a and management of overall infrastructure of Islamic finance. In the absence of a sufficient legal frame and efficient risk prevention measures, Islamic financial services are more easily affected by a series of risks (risks of liquidity, operation, markets, etc.) than conventional financial services. When possibly and properly, financial assessors and supervisors should supply quantitative analysis on sectoral size, proportion of Islamic finance, and financial indicator relevant to capital safety, bad debt, provision, and income of Islamic banks. These concepts should be tailored properly in order to reflect typical features on Islamic accounting system and financial contracts.

4. Indicators on financial soundness, development and structure

One of research results carried out jointly by IMF and WB is the development of standard indicators for countries to assess financial soundness, development and structure. Thereof, the research project also issued specific guides on main essential data resources for calculation of the indicators as well as ways and methods of data collection. This can be considered a handbook for countries to manage, supervise and assess the financial system.

4.1. Indicators on financial development and structure

The indicator system includes overall indicators on scale, level and components of the financial system; basic indicators on competition, concentration, efficiency and access; measures on scope, range and outreach scope of financial services.

The assessment on financial structure is comprehended as the consideration of overall scale of the whole financial sector, each sector and financial institutions which thereby decide efficiency of the sector in meeting demand of clients. The assessment of financial structure also consists of assessment on roles of important financial institutions such as central banks, commercial banks, wholesale banks, savings funds, financial development institutions, insurance companies, mortgage lending institutions, pension funds and financial market institutions. Functions of the financial market including money, exchange rate, capital markets (bond, stock, derivative markets and complex financial products) should also be taken into consideration.

Some indicators on financial development and structure:

For financial institutions, it should be defined:

- Quantity and types of financial institutions
- Growth trend of aggregated balance sheets of the whole system

For financial markets, it should be taken into account:

- Scale and growth trends of financial market instruments (scale and value)
- Relationships between financial market and financial institutions in many aspects including enhancement of financial instruments, participation of new institutions in the financial market (such as hedge funds), or changes in conventions among members of the financial market.

Other overall indicators that should be considered include:

- Value of main assets equals absolute and relative figures (compared to the GDP)
- Ratio of amount of money M2 as compared to GDP (M2/GDP)
- Total private credit value as compared to GDP (DCP/GDP)
- Total value of bank deposits as compared to GDP (Deposits/GDP)

It should be noted that because these indicators are vulnerable to the general financial development of each country, the analysis should make comparison between countries with similar circumstances in order to draw proper standards on “low” or “high” level

- Indicators between asset value of various financial sector groups (banks, non-banks, financial markets, etc.) as compared to total financial assets

- Value of financial tools in various financial market as compared to total financial assets

Assessment on the overall growth of the financial system and groups of financial sector plays an important role, needed information collected and analyzed is about the quantity and type of financial intermediates as well as growth of financial assets in each sector in both nominal and intrinsic value.

Though the description and finding on the trends are essential, it is required to specify factors that affect the changes and trends such as (a) changes that can be easily seen in institutions and state of their assets; (b) quantity or growth rate of instruments in the monetary and capital markets. A factor that has certain impacts on the financial system development in many countries is financial liberalization, especially simplification of conditions on market integration for banks and other financial institutions, as well as liberalization of interest rates contributing to fostering the financial market (especially monetary market). In addition, changes in regulations on safety and accounting standards are also dynamics for developing new methods of risk management or developing new risk dispersion instruments in the capital market.

4.2. Indicators on financial system expansion and diversity

Assessment on financial system expansion is the assessment on diversity of financial products and services as well as diversity of types of financial intermediate institutions and financial markets. It means that numerous financial instruments give investors more alternatives on investments with various rates of return corresponding to different risk acceptance levels, maturities, similarly numerous financial resources give producers more opportunities on capital mobilization with different interest rates and maturities. Therefore, assessment on financial system expansion should be carried out in existing financial institutions, current markets of financial instruments and list of existing products and services.

Table 4.2.1. Some indicators on financial development

Sector	Indicators
Banking	- Total banks - Total branches and agencies - Branches / 1000 people - Total bank deposits/ GDP (%) - Total bank asses/ Total financial assets (%) - Total bank assets / GDP (%)
Insurance	- Quantity of insurance companies - Total insurance premium/GDP (%) - Total life insurance premium/GDP (%) - Total non-life insurance premium/GDP (%)
Pension fund	- Quantity of pension funds - Percentage of labour sponsored by pension funds - Total assets of funds/GDP (%) - Total assets of funds / Total financial assets (%)
Monetary market	- Types and value of monetary market instruments - Value of new issuance turns and growth rate in total current value - Quantity and value of daily (or weekly) transactions of instruments
Foreign exchange market	- Quantity and value of daily foreign exchange transactions - Guarantee of foreign exchanges (rate of foreign exchange provision from import activities in a month compared to short-term foreign debts or compared to total foreign debts)
Capital market	- Quantity of listed securities (bonds and stocks) - Proportion of individual investors, companies, banks and non-banking institutions that hold securities - Quantity and value of new issuance turns (bonds and stocks) - Market capitalization value/GDP (%) - Transaction value / Market capitalization value (%) - Scale of derivative markets

The indicators are not only considered individually but also put in the correlative relation among sectors. For example, the comparison between the banking sector and non-banking sector in financial circulation is needed (comparison between total value of bank credit accounts and total value of issued stocks in the private sector). In addition, large savings accounts or financial mobilization under non-banking form are an efficiency indicator to assess financial diversity because bank deposits or loans are traditional forms applied in many countries. Therefore, it is necessary to compare the role of financial intermediates in the banking sector with that in the insurance sector, pension funds, monetary market and capital market. Moreover, the proportion of assets of various areas (individuals, financial companies, banks, non-banking institutions) for instruments of capital market or assets of common funds is essential information to assess

In addition, some indicators are used to assess common activities of the financial system mentioned in Table 4.2.2

Table 4.2.2 Indicators to assess general activities of the financial system

Content	Indicators
Competition and concentration	- Total financial institutions - Spread of input-output interest rates and prices of financial services - Index of concentration of financial intermediates (market share of 3 or 5 biggest financial institutions) - Index of concentration of the financial market (market share of biggest financial instruments compared to total financial asset value) - Herfindahl Index (HI): Total square value of all institutions in a financial sector[2]
Efficiency	- Spread between mobilization and lending interest rates - Intermediate costs (percentage of total assets)
Liquidity	- Index of transaction value compared to market capitalization value - Spread between mean bid-ask prices

[2] *The higher the index is, the higher the market concentration is*

4.3. Indicators on scope and satisfaction of financial services

The financial system provides 5 basic financial services for the economy: (1) Savings, (2) Credit allocation and lenders' surveillance, (3) Settlement, (4) Risk restriction, (5) Liquidity.

Mobilization of savings resources should be assessed the efficiency in supplying instrument of mobilizing savings from households and companies. This can be assessed by indicators such as broad money amount[3] /GDP, bank deposits/GDP, proportion of population having bank accounts, etc. In addition, other indicators are also necessary to assess the satisfaction of savings services are the quantity of bank branches, the number of population/branch, and allocation of branches and agencies. Moreover, assessment on diversity of mobilization instruments is also needed because in many countries, bank deposits are considered a traditional and popular saving service but mobilization of savings by non-banking services is also very necessary and important in diversification of financial services. Therefore, such indicator as proportion of households and companies holding non-bank assets *(such as stocks)* is also an indicator to assess the satisfaction of savings services of the financial system.

For credit allocation, bank credit in the private sector compared to the GDP is a common indicator to assess the credit satisfaction of the financial system in the economy. In addition, such indicators as total account outstanding/total bank deposits; capital amount mobilized through stock issuance and monetary instruments; credit allocation to various areas in the private sector can define the participation of bank credit with the allocation of domestic outputs; relative proportion of credit outstanding of agriculture, production and services, etc. is also information needed to assess credit satisfaction in the economy.

[3] *Broad money amount*

For settlement, in order to assess settlement system development, it is necessary to take into account the list of settlement instruments. Settlement instruments or methods include cash, cheques, payment order, telegraphic transfer, debit card and credit card. The proportion of amount and value of each settlement instruments also indicates the development of the settlement system, in an economy, if cash is dominant in the settlement system, the development of the settlement system is at low level. Days needed for cheque settlement, quantity and allocation of clearing houses, amount and value of cheque settlement accounts are basic information to assess the efficiency of the existing settlement system.

For risk restriction services supplied by the financial sectors, assessment on life, non-life insurance and derivative instrument is needed. Total insurance premium/GDP is a common indicator applied to assess the development of insurance industry, this indicator should be classified based on life and non-life insurance. In addition, for deeper assessment on contribution of insurance industry, it is necessary to supplement assessment on diversity of insurance products in life and non-life insurance such as insurance of vehicles, explosion, houses, mortgages, unemployment, healthcare, health, etc. Moreover, the development of the derivative market with instruments such as future contracts, forward contracts, option contracts, swap contracts should be assessed in terms of liquidity, satisfaction, cost and application in risk management.

For services ensuring the liquidity of the financial system, it is necessary to consider the possibility of maturity conversion and junior market structure of investments in high profit projects. High profit projects often require long-term investments; however, investors are reluctant to make long-term investments. Therefore, the role of the financial system is to ensure conversion of short-term high-liquidity investments to long-term low-liquidity investments, thereby to mobilize much capital. The maintenance of the liquidity of the financial system will help investors to easily convert their assets into money when they demand.

Besides, in addition to assessment on the aspects, overall assessment should take into account access to financial services of important groups of population such as farmers, the poor, medium and small enterprises or differences in geography. Access is assess in many aspects such as the number of types of financial institutions, number of branches and agencies, number of served clients and population per agency. Moreover, it is necessary to assess the access to financial services in terms of demand. However, it requires to conduct a survey and collect data on demand of savings and credit from households and enterprises; thereby researching the correlative relation between demand and satisfaction of the financial system. Finally, assessment on costs of financial services also plays a very important role, normally assessment on degree and trend of the spread between deposit and lending interest rates, common interest rate structure, prices of other financial services such as minimum cost and balance of bank deposits as well as time and cost of settlement services.

4.4. Financial soundness indicators

Financial Soundness Indicators (FSIs) are used to assess the soundness and current financial state of financial institutions in the economy as well as individual clients and their institutions. FSIs play an important role in assessment on financial stability. They include specific data of each credit institutions and aggregated data. FSIs are calculated and commonly used in macroscopic safety surveillance as well as assessment and finding of advantages and weaknesses of the financial system.

FSIs are classified into 2 basic groups: basic FSIs commonly used by most countries; and encouraging FSIs which depend on countries in calculation and usage.

Table 4.4. Basic FSIs

Indicator	Area	Content
Equity/ Risk weighted assets	Capital Adequacy	Measure and assess expanded capital including unstable capitals such as unguaranteed debt capital, advantages from taxes and abnormal capital spreads
Equity level 1/ Total risk weighted assets	Capital Adequacy	Measure and assess core capital including equity and return compared to mean risky assets
Net bad debt in provision fund/ Equity	Capital Adequacy	Indicate provision fund to be supplemented compared to equity
Bad debt compared to total outstanding loans	Asset quality	Assess credit quality of bank loans
Sector loans in total outstanding loans	Asset quality	Assess credit concentration in specific sectors
Return on assets and return on equity	Income and earnings	Assess loss compensation income compared to equity of lending loans and assets
Interest Income/ Total income	Income and earnings	Indicate the importance of income from profit and loss compensation

Non-interest cost/ Total income	Income and earnings	Indicate that high non-profit costs reduce return
Liquidity assets/ Total assets and liquidity assets/ Short-term capital	Liquidity	Assess vulnerability to decrease in financial resources from the market and bank deposits
Net foreign exchange position/ Equity	Threat to exchange rate risks	Measure foreign exchange imbalance

The indicators are calculated based on aggregation of balance sheets. This calculation makes a conversion from microscopic indicators in each institution to macroscopic financial soundness indicators, so mistakes or insufficient information are unavoidable. Therefore, in addition to aggregated indicators for macroscopic safety analysis and comparison among countries, indicators calculated for each groups of institutions or analysis and supervision on allocation features of indicators are extremely essential.

FSIs are used to both assess the existing and past financial soundness in the financial system and forecast the future. Encouraging FSIs are shown in Appendix 4.4.

4.4.1. FSIs in non-banking sectors

For enterprises, attention should be paid to indicators on rates of loans, yields, liquidity, debt payment because these indicators help assess threats to insolvency of enterprises. Specifically, common indicators should be listed as debt/equity, return on equity (ROE), quick settlement index (short-term asset/short-term capital), and rate of borrow interest rate settlement (EBITDA/debt service costs-interest plus principal). FSIs for enterprises are indicator aggregated from financial statements of listed enterprises. In the scope of the whole economy, data should be aggregated from National income accounts when financial statements of enterprises lack data.

For households, indicators needed to assess reflect loans, liquidity and debt settlement. Specifically, two common indicators are household loans/GDP and debt burden/income. Household loans/GDP indicates total loans of households, mainly consuming and housing loans, percentage of GDP. If this indicator is high, vulnerability of households during changes in economics and financial markets is high. Then, policies to adjust debt settlement of households should be considered. Debt burden/income measures debt settlement from incomes of households. This indicator is also a ground to forecast the spending growth in the future: it keeps at high levels and stable during many quarters that can affect the growth rate of individual consumption.

For real estate area, indicators needed to focus on are remarkable changes in price and amount of loans and construction because this information is often signs of credit and mortgage quality in the future. A quick increase in real estate prices, normally results of observation of expanded monetary policies or large capital flowing into the market, can lead to drastic economic decline and it will affect the financial soundness. Specific indicators should be considered to assess the development state of the real estate market including supply, demand, prices and relations of the market with the economic cycle, thereby defining risks of the financial sector from the real estate area. If risks are found out from the real estate area, it is necessary to make statistics on information relevant to sizes of credit accounts and potential risks. Credit accounts related to real estate should be classified based on purposes (real estate investment for commerce or construction of companies or houses). Detailed market analyses on loans for purchasing real estate such as interest rate structure, loan diversity for purchasing real estate are also needed to manage risks and ensure financial stability.

4.4.2. FSIs in the banking system

The banking system should be focused on quantitative assessment in order for information on stability and sensitivity of the banking system. Main FSIs in the banking sector are assessed in accordance with the indicator group of CAMELS (Capital, Asset Quality, Management, Earnings, Liquidity and Sensitivity). Most indicators are aggregated from indicators for each bank, thereby calculating indicators for each bank group, for instance, domestic banks, foreign-owned branches and agencies, state banks, etc. and the whole banking system. FSIs in non-banking sectors (such as enterprises, households or insurance) can be combined to assess credit risks to the banking sector as well as threats to non-banking sectors.

4.4.3. FSIs in the insurance sector

Quantitative FSIs in the insurance sector are assessed in accordance with indicator groups of CARAMELS (Capital, Asset Quality, Reinsurance, Adequacy of claims and actuarial, Management, Earnings, Liquidity and Sensitivity). Specific indicators are shown in Table 4.4.3

Table 4.4.3 FSIs in the insurance sector: core indicators

Indicator group	Indicator	Non-life	Life
Capital	Net premium/Capital	x	
	Capital/ Total assets	x	
	Capital / Technical provision		x
Asset Quality	(Real estate value + non-transaction shareholders + debts)/ Total assets	x	x
	Equity / Total assets	x	x
	Bad debt / total outstanding		x
Reinsurance	Total net premium/ Total premium (Risk maintenance index)	x	x
	Technical provision/ actuarial average in the 3 most recent years	x	
	Technical provision/ net premium actuarial average in the 3 most recent years		x

Manage-	Total premium/ Number of staff	x	x
	Total asset value/ Number of staff	x	x
Earnings and return	Net actuarial value / Total net premium (loss index)	x	
	Total costs/ Total premium (Cost indicator)	x	
	Aggregated indicators = Cost indicator + Loss indicator	x	
	Adjusted technical provision / Technical provision		x
	Earnings from investments/ Total net premium	x	
	Earnings from investments / Total invested assets		x
	Return on equity (ROE)	x	x
Liquidity	Liquidity assets / Short-term capital	x	x
Sensitivity to market risks	Net foreign exchange state/ Capital	x	x
	Average time of capital reimbursement of assets and capital		x

4.4.4. FSIs in the securities market

The stability of the securities market should be supervised in accordance with quantitative indicators focusing on the market liquidity because liquidity securities play an important role in balance sheets of financial institutions. The market liquidity is calculated by the number of securities sold in a short time while their prices do not change much. The market liquidity can be considered in two aspects: Equilibrium and Depth. The equilibrium is the ability to equilibrate supply and demand with low costs quickly. FSI on bid and ask spread can be considered a rough indicator the measure the equilibrium of each market, thereby the bid and ask spread can hardly prove that a market with high competitiveness and a large number of sellers and buyers can increase the market liquidity. The depth is ability to carry out large transactions without many changes in prices. Low market liquidity means that investors have to make a large decrease in prices to quickly sell their securities, then the market has a decrease depth. FSI on the amount of transactions (Total average value of daily traded securities/ total value of securities) also helps assess the liquidity of balance sheets of banks when banks define the number of securities that they can convert in the market. The market depth can be assessed roughly by fluctuation index of transaction amount, size of transaction limit, spread between normal transaction prices and urgent transaction prices and fluctuations of the market.

In conclusion, the study and gradual application of FSAP instructions in financial sector assessment have been considered extremely essential and important when the world has experienced continuous crises (Global financial crisis originating from United Stated *(2008)*, European sovereign debt crisis *(2009)*, etc.). All countries including developed and developing countries have realized their responsibility in international cooperation in order to ensure stability and development for not only their own countries but also the global economy. Thereby, countries should have a consent in financial assessment and proclaim as well as supply financial data for international financial organizations *(WB, IMF)*.

CHAPTER 3:

VIETNAM FINANCIAL SECTOR ASSESSMENT

1. Overview on Vietnam financial sector assessment:

Financial sector assessment has not been paid proper attention to in the past few years and remained dispersed after the regional financial crisis in 1997 – 1998 as well as the global financial crisis in 2008. Financial sector assessment has not followed international standards and practices under requirements on deeper international integration. Therefore, financial sector assessment is not really useful in financial sector reforms.

Vietnam financial sector during over years of reform has passed 3 typical stages with tremendous difficulties and challenges:

In the first stage, the domestic financial sector seemed to be completely liberalized after the 2nd Conference of the VI Party Central Committee in 1987 allowed "implementing vigorously policies on capital mobilization from people, economic institutions under various forms on channels, ensuring benefits of depositors". In this stage, credit institutions were founded and mobilized capital liberally without any regulations on safety. The unavoidable consequence is that the whole system collapsed because it operated in the form of using money of later depositors to pay interest raes of previous depositors. One of basic causes for the collapse of credit cooperatives was imbalanced information which caused view to rely on others and unfavourable alternatives. Consequently, capital mobilization focused on high risk activities.

Next to the liberal stage, the risk restriction stage started by regulations on safety in operations of credit institutions issued in 1990. Some basic regulations were established but rather urdimentary and were not actually observed strictly along with other factors that once again led to big problems to credit institutions (in which commercial banks pay a key role) at the same time as the 1997-1998 financial crisis in the region. Due to unclear regulations on possession, some banks became unit directly under or "behind ground" of enterprises. Eventually, mobilized capital was borrowed by very banks to invest in risky business activities. Some banks were unable to make debt payment so the Government had to assign state-owned commercial banks to deal with, for instance, Nam Do bank. Fortunately, the size of troubled banks was relatively small and solutions were timely implemented so it did not cause spreading effect leading to the collapse of the whole system as occurred in many countries in the world.

And in the current stage, the financial sector has achieved certain development. The financial sector has been formed with relatively sufficient structure (banking, securities, insurance), and more and more expanded its operation and become more diversified and flexible, attracting many participants. Financial institutions in the market have increased quickly in quantity and diversity in business types and forms. Large banking corporations have been established and gradually affiliated with other major economic corporations. Financial capacity, business quality and competitiveness of domestic financial institutions have been more improved along with gradual completion of structure, management, business and adaptation to new business environment. Operating rules of market types have been established and radically met requirements on operation and development. Facilities and technologies of markets have been built towards approaching modernity. Surveillance institutions have been established in sub-markets. The State management in the financial market has been institutionalized and more closely cooperated.

However, the global financial crisis occurred when Vietnam started its integration into the international economy, so though Vietnam financial sector has not been affected much as other countries owing to new linkage with financial sectors in the world at low level, it has waved and revealed weaknesses clearly: response to external shocks of the financial sector, the Government's external capital allocation remain limited and therefore the securities market was impacted and declined in 2007-2008 when foreign capital resources increased, creating pressures and increasing inflation and commercial deficit, making investors anxious, especially foreign investors. In 2010, the Government's credit market regulation through issuance of many policies on interest rates and exchange rate created many inadequacies in credit supply for the economy, causing stagnation in business of enterprises, contributing to remarkable decrease in GDP.

In addition to the weaknesses, many challenges have been defined for the Government with a lot of questions that have not been answered such as is the current financial sector structure proper to the deep development of the economy? Are existing models of inspection and surveillance appropriate to the financial sector development? Transparency of market information and enhancement of financial infrastructure are issues to be improved more, etc. Obviously, financial sector assessment has not been paid proper attention to because until now the establishment of standard indicators to reflect financial sector state is always a leading issue that no state-owned authorities in Vietnam are responsible for proper solutions.

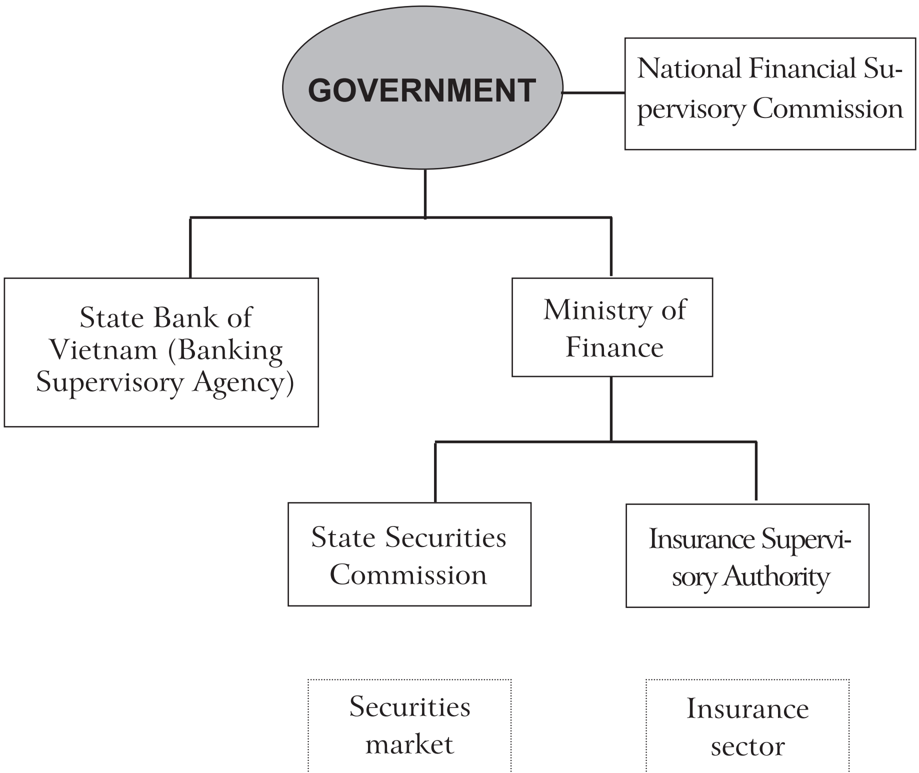
Besides, Vietnam, financial sector assessment is now carried out on the basis of specialized and dispersed analysis and assessment that are not comprehensive and systematic. With 3 financial sectors of the market as banking, insurance and securities, each sector is supervised and assessed by a separate authority. The banking sector is supervised and assessed by the Banking supervisory Agency (under the State Bank). The insurance sector is supervised and assessed by the Insurance Supervisory Authority (under the Ministry of Finance). The securities market is supervised and assessed by State Securities Commission (currently directly under the Ministry of Finance).

Upon the more and more sophisticated development with mutual impacts and influences of financial activities, components of the financial sector as well as interleaved activities that become more difficult to be controlled of financial corporations have required cooperation in close supervision and overall assessment between state-owned management authorities responsible for financial activities, different financial sector components in order to make the financial sector supervised comprehensively, avoiding interleaves risks among activities in a corporation, sectoral components and sustainable development.

Under the requirements, Vietnam National Financial Supervisory Commission was established and operated in accordance with Decision No. 34/2008/QD-TTg dated March 3rd 2008 of the Prime Ministry (in March 2008) with functions as directly giving advice and consultation to the Prime Minister in coordinating national financial market activities (banking, securities and insurance) and helping the Prime Minister generally supervise the financial market with tasks of analyzing, forecasting and warning of financial-banking system safety and risks to the national financial market.

Therefore, National Financial Supervisory Commission is considered the only authority which conducts supervision and assessment on macroscopic financial market safety. Meanwhile, specialized supervising authorities only carry out microscopic safety supervision and assessment in each sectoral component of the financial sector (Figure 1). After a period (over 3 years) of operation, National Financial Supervisory Commission has obtained some remarkable achievements in common financial sector supervision and assessment; thereby it is the first time the Committee has carried out overall financial sector supervision and assessment and suggested some early warnings along with recommendations and proposals to strengthen financial sector operation and development. However, due to objective and subjective causes, results of analysis and assessments are not really useful for the Prime Minister as well as state-owned management authorities to timely and properly tailor financial sector operation and development.

Figure 1: Authorities participating in Vietnam financial sector supervision and assessment



However, Vietnam financial sector assessment has not basically had an official mechanism on information share or cooperation among specialized supervision authorities.

The Insurance Supervisory Authority and the State Securities Commission are two components under the Ministry of Finance, information can be shared when raised issues need to be solved by the two one. However, there are hardly any mechanisms for the Insurance Supervisory Authority, State Securities Commission and the State Bank to share information or cooperate in supervision for financial sector supervision and assessment. This can be seen a gap in Vietnam financial sector supervision, analysis and assessment on risks when more insurance, securities and banking activities are alternated deeply along with an increasing number of banking-financial corporations with diversified business activities.

In addition, the role of coordination in specialized supervision of the National Financial Supervisory Commission has not been developed. Therefore, the linkage in financial sector supervision and assessment among the National Financial Supervisory Commission, State Bank and Ministry of Finance is an extremely vital issue to be timely and effectively solved by the Government.

2. Banking sector assessment

Vietnam banking sector assessment is carried out by the Banking Supervisory Agency (under Vietnam State Bank). Actually, banking sector assessment is now to analyze and assess the financial soundness, management and risks of banks; to find out and warn of risks to banking and threats to breach of law on money and banking.

Actually, in the past time, the Banking Supervisory Agency has carried out supervision and assessment on financial state, management and risks of commercial banks and non-bank credit institutions (financial companies, financial leasing company) as well as people's grass-root credit funds in the method of CAMELS but not based on risks. Banking sector assessment only carrys out simple supervision, analysis and assessment through information and data collected from periodical reports of commercial banks without frequence and continuousness it does not follow comprehensive indicators because the very indicators of CAMELS have not been observed sufficiently. Banking sector assessment on asset quality through current criteria on debt classification (in accordance with Decision No.493) of commercial banks has not followed international practices and standards (only based on quantitativeness but not qualitativeness), leading to the fact that the rate of bad debts in the banking system has not been reflected exactly asset quality in the banking system. Indicators on risk management of commercial banks are not clear. Indicators on credit risks of a new commercial bank are only revealed in the content of asset quality assessment through the statistics on overdue debts, in regulations on credit limits, capital contribution limits and purchasing of shareholders of commercial banks. This is insufficient to assess credit risks of commercial banks because it is necessary to supplement other qualitative assessment such as assessment on credit granting criteria and procedures on credit granting of banks, assessment on impartiality of credit granting, etc. However, the State Bank has gained certain achievements in commercial bank operation assessment such as assessment on observation of commercial banks in ensuring safety rates, thereby finding out commercial banks which do not meet requirements in minimum capital safety rates and outlining requirements on maximum time to increase the minimum capital safety rates to the regulated level.

It can be seen that along with stronger development and international integration in the banking system, indicators to assess the banking system now reveals many shortcomings and inefficiency in banking system state assessment. Until now, the Banking Supervisory Agency has not established new indicators to assess the banking system comprehensively in order to clearly realize advantages, weaknesses and potential risks in the sector to recommend solutions timely.

Although Vietnam commercial bank system has not recognized any collapse, dissolvement or bankruptcy of any commercial banks, it cannot confirm the safety of the banking sector in particular and the financial sector in general. The safety and no collapse or bankruptcy in the banking sector in the past time has not originated from the results of banking sector assessment of Vietnam State Bank. It is possibly believed owing to the fact that the initial development of Vietnam banking system has not coped with too many risks and the risks have not exceeded the ability to control of the State Bank, at the same time, the existing size of the banking sector in the past time has not been extremely large.

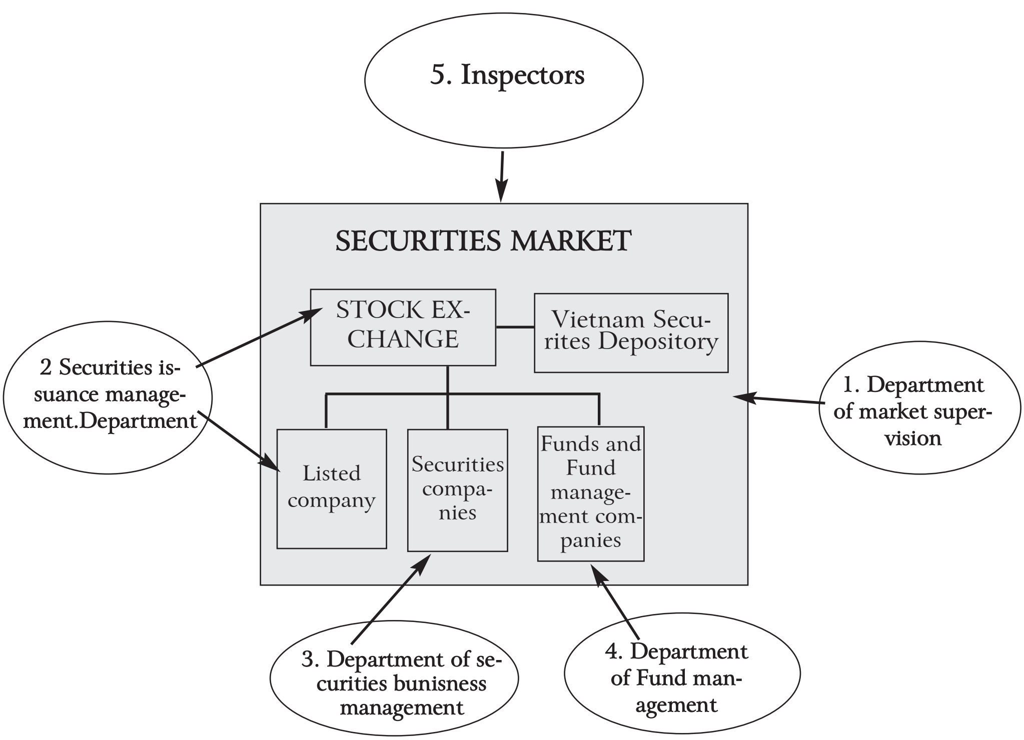
In addition, banking sector assessment of Vietnam State Bank has not paid attention to assessment on early warning for commercial banks. Risk early warning requires Vietnam State Bank to work out a list and quantity of commercial banks which have negative changes or unusual signs, leading to collapse and should be prudentially supervised. However, Vietnam State Bank currently only carries out supervision and assessment on each commercial bank individually. The overall assessment to indicate general trends of the whole banking system in each banking sector remains a shortcoming of the State Bank and it should be completed in the future.

3. Securities market assessment

Securities market assessment is currently carried out by the State Securities Commission (under Ministry of Finance with focuses on: (1) Market behavior; (2) Transactions in the market of institutions and individuals; (3) Financial soundness of institutions in the market (securities companies, Fund management companies).

The State Securities Commission carries out securities market assessment through 5 units as follows:

Figure 2: Apparatus of Vietnam securities market supervision and assessment



With the participation of 5 units, securities market assessment is dispersed. Specialized departments such as Department of securities dealing management, Department of securities issuance management, Department of Fund management, and Department of market supervision both establish legal regulation, plans, strategies, procedures and guides for their management sector and carry out analysis and assessment on aspects in the sector.

The system of indicators on supervision on securities companies and fund management companies in accordance with Decision No. 92/2004/QĐ-BTC in 2004 issued financial supervision indicators of securities companies and fund management companies, including:

- Indicators on general operations: capital changes, provision extraction and establishment, turnover changes; operation costs
- Indicators on profits: profit on turnover; return on capital; house business quality; return on equity
- Indicators on liquidity: debt on liquidity assets, debt in securities trading on capital

It can be seen that these indicators are used more in commercial bank operation assessment; however, when the operation of securities companies is not alike to that of commercial banks, the application of the indicators similar to banks seems inappropriate. Moreover, these indicators only mention formulas but not meaning and limits of criteria in assessment of operation of securities companies and fund management companies. Financial soundness assessment of securities companies and fund management companies does not actually have much significance in securities market stability and development.

Two factors which are paid attention to by investors for participation in the market and by State management authorities for securities market stability and development are market stability and transparency. However, analysis and assessment on the two factors of the State Securities Commission remain unobstructive. Generally, assessment on liquidity of the securities market has not changed remarkably.

Recently, the State Securities Commission has realized the significance of assessment on securities dealing behaviors in stead of supervision on operation of securities companies and fund management companies. Therefore, Department of market supervision was established to assess securities trading. Accordingly, on December 31st 2008, the Ministry of Finance issued Decision No.127/2008/QD-BTC on promulgating Bylaw on Securities trading supervision in the securities market. This bylaw stipulates basic rules and principles relevant to supervision and assessment on securities trading in the centralized securities market and the securities market with unlisted public companies in order to prevent legal violation, maintain the impartiality and publicity in the securities market, protect legal rights and benefits of investors. The bylaw was issued in order to prevent, find out and deal with fraud, cheat, internal transactions, market manipulation and legal violation on securities.

This decision has initially established mechanisms on supervision and assessment including models and relationship between the State Securities Commission and Stock Exchange. Thereby, the Stock Exchange also carries out supervision and assessment on trading and supply of services relevant to securities trading within its competence, at the same time takes responsibility in clearly defining violations under its competence and reporting the State Securities Commission to deal with violations. The State Securities Commission takes responsibility in making regulations and procedures on effective supervision and assessment on the basis of reporting, exchanging and supplying information timely, sufficiently and exactly, active cooperation, and restriction on overlapping of supervisors. However, Decision No.127 only promulgates the most basic regulation on supervision and assessment on securities trading in the Stock Exchange including responsibility and power in securities trading supervision; supervision and assessment content; supervision and assessment criteria; supervision and assessment methods. The State Securities Commission also promulgates consistently periodical (daily/monthly/annual) trading supervision reports, abnormal trading supervision reports and required trading supervision reports. Accordingly, supervision reports will be made and submitted to the State Securities Commission by the Stock Exchange for surveillance. Information and criteria in supervision reports only help the State Securities Commission supervise daily trading simply. When the finding and accuse of violations in securities trading remain limited, requirements in information in abnormal trading supervision reports are not significant.

4. Insurance supervision

Insurance sector assessment is now under the responsibility of Insurance Supervisory Authority (under the Ministry of Finance). Insurance sector assessment is mainly analysis and assessment on financial soundness, business of insurance enterprises in order to early find out insurance enterprises at risk of insolvency in order to timely recommend solutions to deal with, protect legal right and benefits of insurance participants.

Therefore, insurance sector assessment is carried out mainly based on indicators on insurance enterprises stipulated in Decision No.153/2003/QD-BTC in order for supervision and assessment on financial soundness, business of insurance enterprises. The indicators include:

- Indicators on non-life insurance enterprises: Indicators on general operation; Indicators on return; Indicators on liquidity; Indicators on provision
- Indicators on life insurance enterprises: Indicators on general operation; Indicators on operational changes; Indicators on liquidity; Indicators on paying capacity; Indicators on return

Insurance enterprise indicators have been developed since 2003 based on the Insurance Regulatory Information System of USA with thresholds proposed by foreign advisors. However, in this stage, the insurance market in Vietnam is inexperienced, so indicators are only "copied" but not tailored to real circumstances in Vietnam. By 2009, Vietnam insurance market was at the first stage of development with 50 insurance enterprises including 11 life insurance enterprises, 28 non-life insurance enterprises, 1 reinsurance enterprise and 10 insurance brokerage enterprises. In developed economies, turnover of insurance accounts for a high rate of 8 – 15% of GDP, meanwhile in Vietnam the rate is now only 2% of GDP (sources: Nguyen Kim Anh and coworkers, 2009). With small size and new development, insurance business has not large impacts on socio-economic living as well as on the financial sector in general. Therefore, insurance enterprise indicators stipulated in Decision No.153 has not been verified if they are really proper to the market in Vietnam. Insurance companies have only dealt with requirements in calculation of indicators (12 non-life insurance indicators and 14 life insurance indicators) simply but they have not really realized significance of these requirements in insurance risk management or early warning.

The Insurance Supervisory Authority bases on value limits that have been defined to compare with indicators of each insurance enterprise, if any enterprise is found out indicators out of allowable value limits, it will be inspected and required to adjust. This is considered an early warning for insurance enterprises with indicators out of allowable value limits. However, the determination of value limits or thresholds in insurance business should be clarified scientifically and practically. Currently, these values are still “copied” from the USA insurance market but they can hardly perform their role of early warning for insurance business in Vietnam.

Thus, it is necessary to carry out a research and establishment of proper standards indicators for Vietnam insurance assessment. Thereby, indicators should ensure the feasibility in data collection and calculation based on existing database as well as accounting regimes in Vietnam. Moreover, the establishment of standard values reflecting risk thresholds in Vietnam insurance is needed. Value thresholds should be continuously adjusted and researched in order to find out impact factors and grounds to define more proper value thresholds.

Briefly Vietnam financial sector assessment and supervision has been still uncentralized and not efficiently cooperated by specialized supervisory authorities. The unification of financial sector supervision and assessment requires aconsent, comprehensiveness and consistency. There by Vietnam should define a unified assessment under the participation of relevant agencies and a coordinating agency in order for general assessment on all financial sectors.

CHAPTER 4:

IMPORTANT ITEMS OF VIETNAM FINANCIAL SECTOR ASSESSMENT

1. Assessment objectives/ missions

Vietnam comprehensive financial sector assessment program will help:

- Find out advantages, weaknesses, risks and challenges to the financial system, especially in the context of integration
- Define requirements in upgrading infrastructure of the financial system appropriate to coping with risks and challenges in the new context, responding to/coping with internal and external shocks
- Develop a comprehensive framework on Vietnam financial system stability assessment, define schedules and strategies on Vietnam financial system development.

2. Assessment contents/scope/objects

Financial sector assessment in accordance with FSAP focuses on 3 key backbones as follows:

- ***Pillar 1:*** Analyses on macroscopic financial system safety and stability supervision, analysis on internal and external factors which affect the financial system soundness and stability, analysis on factors which af+fect risks and vulnerability if each sector and the whole financial system.

- ***Pillar 2:*** Financial system management and supervision in order to manage risks and vulnerability, protect the market stability; offer dynamics of effective management, propose to apply the best international practices in financial sector management and supervision, suggest methodologies of assessment.

- ***Pillar 3:*** Financial infrastructure, including (i) financial legal foundations, including mechanisms on bankruptcy, creditors' rights and financial safety, (ii) infrastructure in system liquidity, including money, foreign exchanges, foreign exchange markets and securities, (iii) transparency, management, information infrastructure, including transparency of monetary policies, mechanisms on supervision and information declaration of credit institutions, credit report and information system

On the basis of 3 pillars of FSAP, in the coming time, Vietnam assessment program should focus on backbone 1 and 2. Because when Vietnam financial market has not developed adequately with uncompleted financial infrastructure, limited transparency and management capacity of participants and weak mechanisms on supervision and information declaration of credit institutions, financial infrastructure assessment does not contribute much to strengthening financial sector supervision and assessment. Moreover, Vietnam financial sector assessment and supervision now show outstanding shortcomings such as macroscopic market supervision; assessment on linkage of banking, securities and insurance; systematic assessment on factors which have macro influences on the whole financial sector but not individual influences on credit institutions or each financial sector. Thus, Vietnam financial sector assessment currently should focus on systematic assessment.

3. Defining approaches/methods/standards of the assessment

Observation of international standards is the only way to access technical assistance programs of developed countries of international financial institutions. However, in the context of new development of Vietnam financial market, if the financial sector assessment program is determined to observe a series of international standards in financial sector assessment and supervision, it will cope with certain difficulties. Thus, it is necessary to select priorities in applying standards, to define which standards only used to consider conditions to apply, which standards cannot be applied.

Thus, Vietnam comprehensive assessment program should focus on prioritizing banking sector supervision and assessment standards. Standards on insurance sector and securities should be only considered conditions for performance. Standards on information declaration, accounting, management, etc. should be only researched for international experience and models.

Because Vietnam commercial bank system still accounts for a large proportion in the financial sector in terms of size, market share, capital, human resources, branches, etc. Therefore, the observation of international standards in banking system assessment and supervision will reflect absolutely the overall picture of the financial sector in general and the banking system in particular. In addition, the insurance sector and securities in Vietnam account for only a small proportion and are very inexperienced so the "reluctant" and "inflexible" application of international standards will cope with many difficulties from data collection, information processing to calculation and assessment on financial safety soundness indicators.

4. Roles of relevant parties in assessment

The specification of roles and responsibilities of relevant parties during assessment process plays a decisive role in quality and efficiency of the assessment program. With the uncentralized model, no formal authority in Vietnam is sufficiently well-informed and empowered to assess the whole financial system in conformity to indicators jointly issued by the World Bank and the International Monetary Fund in the FSAP framework.

The National Financial Supervisory Commission which plays a role as a counselor of the Prime Minister in financial system supervision has been considered an overall supervisory authority. However, after over 3 years of operation, it has not efficiently acted its role due to difficulties in data collection and cooperation of relevant authorities.

Actually, the supervisory coordination as well as consultation of the National Financial Supervisory Commission has not been well-performed when its macro safety supervision depends too much on data resources supplied by specialized supervisory authorities. It has not virtually developed a mechanism in supervisory coordination between specialized supervisory authorities actively. The mechanism is only well-performed when it specifies responsibilities in sharing inter-ministerial information among authorities, promulgates sanctions on providing incorrect and untimely information, stipulates specific obligations and responsibilities before the Prime Minister in case of mistakes in supervisory cooperation among parties, etc.

In addition, the National Financial Supervisory Commission has coped with difficulties in overall supervision due to limited human resources and other resources when it lacks highly-qualified staff in macro safety supervision. According to the viewpoint mentioned in the research topic on proper financial supervisory model in Vietnam of the Banking Academy in 2010, the National Financial Supervisory Commission has still focused too much on analysis of macro economic management but not macro safety supervision. Therefore, it should imminently focus on performing effectively supervisory coordination while specialized and uncentralized supervision remain existed in Vietnam financial supervision.

This requires an independent and objective authority to assess specialized supervision in financial sectors. Accordingly, the Supervisory Commission can effectively act its role in giving consultation, performing policy review and making reports to the Prime Minister on the overall picture of the financial market and system.

In short, shortcomings in Vietnam financial system assessment are listed as a lack of full mechanisms and sanctions on cooperating and sharing inter-ministerial information among relevant authorities.

Based on the role and concentration of information, the State Bank of Vietnam currently has the most influence and largest coverage because it holds and controls information on foreign currencies, interest rates and banking sector. Therefore, along with the application of financial system assessment indicators of the FSAP, the State Bank has full competence in making reports on macro safety supervision (including fluctuations and influences of interest rates and exchange rates on the economy) and reports on financial system stability. It is essential for Vietnam to make the two reports based on analysis results on assessment indicators of the FSAP.

5. Development of assessment schedules

The FSAP of the IMF defines 5 steps of overall assessment on financial sector development and stability (see more Chapter 2), including: (i) assessment on conditions in the banking sector on financial soundness, access and infrastructure indicators, (ii) assessment on influences of the macro economy, support policies on financial stability and development, (iii) assessment on risks of the financial system, (iv) assessment on financial system structure and development demand and (v) assessment on legal framework and efficient institutions of the financial policies, the specification of priorities should take into account typical features in Vietnam:

- The financial system and market are still in the stage of new development
- The legal framework has not been completed, there is a lack of characteristics in common between national laws and specialized laws
- Conditions to observe international standards on: (i) information declaration, (ii) accounting, (iii) business management and (iv) no or insufficient risk management
- In addition to objectives of macro economic stable development, it is necessary to implement socio-economic objectives, the Government's policies on social welfare or poverty reduction

In response to urgent demand of overall financial market supervision, a series of prioritized assessment tasks in the 2011-2015 period are suggested, as follows:

Step 1: Developing mechanisms on supervisory cooperation between authorities with details on information sharing; rights and obligations in assurance of information accuracy and properness; sanctions in the process of supervisory cooperation and information sharing

Step 2: Improving banking sector assessment in conformity to FSAP guidance. At the same time, specialized supervision in the banking sector by the State Bank of Vietnam should be continuously reinforced and developed based on core principles for effective banking supervision of the Basel Committee under the support of Japan International Cooperation Agency (JICA). In addition, the State Bank should make periodical reports on macro safety supervision and reports on financial stability in which banking sector is put in the center.

Step 3: Improving securities market assessment in conformity to the FSAP indicators in parallel to securities market development strategies. Thereof, the supervision is implemented in compliance with aims and principles for securities regulations of the IOSCO under the cooperation of the State Securities Commission and National Financial Supervisory Commission

Step 4: Improving insurance assessment in compliance with the FSAP indicators. Specifically, insurance supervision is implemented in compliance with principles for insurance supervision of the IAIS under the cooperation of the Insurance Supervisory Authority under the Ministry of Finance and the National Financial Supervisory Commission

Step 5: Investing in infrastructure for insurance, payment system and financial infrastructure indicators on business management, accounting and auditing standards, anti-money laundering, rights of bankruptcy, etc.

CHAPTER 5.

SOME CONSIDERATIONS IN VIETNAM FINANCIAL SECTOR ASSESSMENT

To Vietnam, implementing FSAP is a precious opportunity which will helps Vietnam to strengthen financial structure and to gain longterm stability and development of the economic growth

Some basic data analyses show Vietnam has weathered the global crisis well. But macroeconomic risks stemming from expansionary policies adopted during the global crisis have materialized. Even as most fiscal stimulus measures expired end-2009, monetary policy has remained accommodative, contributing to continued strong credit growth and rising inflation.

Some IMF's recommendations to Vietnam:

- Sustaining stabilization measures until getting lower inflation, strenthening reserves, and being ready to take next steps if necessary.
- Monetary tightening should be achieved mainly through market-based instruments. In the short term, administrative measures could play a supportive role, but they should be compatible with increasing confidence in Vietnamese Dong.
- Strengthening the autonomy of the State Bank of Vietnam would support achieving inflation targets.

- Maintaining stability in the foreign exchange market will require disciplined monetary policy.
- Simplify the exchange regime with steps towards a more market-determined exchange rate.
- Acceleration of fiscal consolidation by saving the bulk of anticipated revenue overperformance in 2011. Over the medium term, fiscal deficits need to be reduced further to close to pre-crisis levels.
- Timely action to help safeguard financial stability in the wake of rapid credit growth and potential vulnerabilities from connected lending. Weak banks should be restructured or merged with stronger entities, while protecting small depositors and taking care to avoid system-wide repercussions.
- encourage efforts to improve coordination among supervisory agencies, set up an effective crisis management framework, and prepare contingency plans.
- encourage addressing longstanding safeguards assessment issues and AML/CFT deficiencies.

Owing to methodical logical execution with common indicators and close association, affiliation, FSAP indicators are only appropriate to the countries with developed financial sectors and infrastructure. For highly efficient and feasible FSAP in Vietnam, indicators should be adjusted proper to conditions and circumstances of Vietnam. Specifically:

- In Vietnam, the legal frame and mechanism has been currently developing and implementing; the financial sector and structure has initially developed. Thus, it is not necessary to specifically assess the observation of these indicators but focus immediately on assessing financial market mechanism, development and supervision capacity. The assessment on observation of the indicators can be implemented in the stage of updated assessment;

- Vietnam has not widely applied international standards in management, accounting, auditing and mechanism of insolvency clearly, so it should focus on specific assessment on the issues in FSAP;

- Vietnam has currently applied an uncentralized model of financial sector management and supervision, at the same time it has not applied a mechanism of close cooperation and information sharing between specialized management and supervisory authorities of the financial sector. Therefore, the Government should ensure a mechanism of clear, close and efficient cooperation and information sharing between management and supervisory authorities of the financial sector before developing indicators on financial sector assessment;

- Human resources: Authorities participating in FSAP must commit to send staff with proper professional and foreign language qualification working as a full-time job during preparing and implementing the program. After finishing the Program, they will be nuclear staff for later sef-assessment and promoted. If the staff should be further qualified, authorities should actively propose WB/IMF to support finance as well as international consultants through TAs;

- Ensuring input information, data: The quality of imput information and data is a decisive element to ensure the success of the Program. In Vietnam, preliminary study shows that financial sector management authorities seem not really ready from supplying information and data due to various reasons including reasons related to legal regulations. Therefore, the Government should timely require and instruct authorities participating in the Program to supply input information and data, at the same time develop and unify a mechanism of accessing sensitive information and data before implementing the Program.

APPENDIX 1[5]

Calculation results of some Financial Soundness Indicators (FSIs) based on banks' public information (2010)

No.	Bank	Capital-based FSI					
		Capital to assets	Nonperforming loans net of provisions to capital*	Return on equity*	Gross asset position in financial derivatives to capital	Gross liability position in financial derivatives to capital	Net open position in equities to capital
	Sector Level	7.46%	12.27%	20.41%	0.28%	2.23%	9.02%
1	Vietcombank	6.68%	22.61%	29.14%	0.09%	0.22%	20.19%
2	ACB	5.76%	2.55%	28.88%	0.36%	0.11%	19.56%
3	Habubank	10.09%		17.74%	0.08%	0.29%	6.41%
4	Nam A Bank	13.80%		10.53%	0.00%	0.00%	9.51%
5	SHB	8.41%	10.59%	19.90%	0.06%	0.04%	9.14%
6	Techcombank	6.88%	13.52%	32.83%	0.28%	0.32%	0.81%
7	VIB	6.34%	0.00%	22.04%	0.03%	0.32%	5.58%
8	Bao Viet Bank	15.30%	0.01%	11.01%	0.00%	0.00%	0.00%
9	Đai A Bank	23.42%		5.87%	0.00%	0.00%	2.47%
10	Đai Tin Bank	17.02%		12.54%	0.00%	0.00%	8.27%
11	Eximbank	14.31%	5.65%	16.97%	0.07%	29.23%	7.35%
12	Lien Viet	15.16%	0.71%	19.13%	0.00%	0.29%	0.39%
13	MHB	4.83%		5.04%	0.00%	0.05%	12.24%
14	Tien phong	15.29%		8.83%	0.00%	1.13%	0.27%
15	VPBank	8.88%		17.10%	0.00%	0.10%	2.50%
16	An Binh	14.17%		14.47%	0.02%	0.04%	7.17%
17	BIDV	6.34%	28.55%	22.02%	0.08%	0.48%	13.63%

[5] *Calculated by a group of reseachers (Nguyen Thi Minh Hue, Pham Duc Manh, Khuc The Anh, Le Thi Ha, Le Thi Nhu Quynh,Trinh Hung Linh from National Economics University - NEU*

18	Maritimebank	5.51%		30.73%	0.00%	0.84%	7.61%
19	Phuong Đong	16.90%	8.72%	14.71%	0.00%	0.10%	5.72%
20	Sai Gon cong thuong	19.00%	6.84%	31.90%	0.00%	0.24%	16.54%
21	Agribank	4.78%		9.13%	0.41%	0.29%	3.40%
22	Kien Long	21.59%		11.91%	0.03%	0.02%	4.30%
23	MB	9.65%	6.27%	29.23%	0.00%	0.00%	14.32%
24	Nam Viet	8.24%	15.22%	13.13%	0.11%	0.00%	27.13%
25	Oceanbank	7.13%	7.23%	21.80%	0.00%	0.16%	12.68%
26	PG Bank	12.19%	7.08%	17.93%	0.05%	0.01%	3.95%
27	Phuong Tay	16.40%	2.41%	4.18%	0.00%	0.00%	0.30%
28	Gia Đinh	27.56%		4.72%	0.00%	0.00%	0.00%
29	HD Bank	7.76%		16.89%	0.02%	0.30%	5.78%
30	Sacombank	9.93%	3.25%	20.10%	2.42%	0.00%	4.92%
31	Southernbank	6.80%	15.95%	16.36%	0.04%	0.16%	4.39%
32	Tin Nghia	12.06%		13.66%	0.00%	0.00%	0.61%
33	Vietinbank	5.09%	8.15%	29.52%	0.30%	0.71%	11.42%
34	SeAbank	13.08%		14.76%	0.00%	0.40%	3.41%

	Bank	Asset-based FSIs			
		Liquid assets (core) to total assets*	Customer deposits to total (noninterbank) loans	Return on assets*	Nonperforming loans to total gross loans*
	Sector Level	22.65%	102.48%	1.52%	1.25%
1	Vietcombank	30.24%	117.40%	1.95%	1.91%
2	ACB	24.92%	129.62%	1.66%	0.25%
3	Habubank	25.45%	93.11%	1.79%	
4	Nam A Bank	27.14%	99.68%	1.45%	
5	SHB	25.17%	108.34%	1.67%	1.27%
6	Techcombank	34.94%	150.39%	2.26%	1.34%
7	VIB	31.20%	111.97%	1.40%	
8	Bao Viet Bank	40.92%	137.29%	1.68%	
9	Đai A Bank	27.65%	92.70%	1.38%	
10	Đai Tin Bank	17.23%	84.14%	2.13%	
11	Eximbank	28.49%	96.21%	2.43%	1.14%
12	Lien Viet	19.48%	128.57%	2.90%	0.23%
13	MHB	29.16%	85.01%	0.24%	
14	Tien phong	16.09%	140.04%	1.35%	
15	VPBank	24.06%	98.35%	1.52%	
16	An Binh	29.25%	117.40%	2.05%	
17	BIDV	17.79%	93.79%	1.40%	2.15%
18	Maritimebank	32.53%	141.25%	1.69%	
19	Phuong Đong	23.31%	76.78%	2.49%	1.75%
20	Sai Gon cong thuong	10.91%	87.16%	6.06%	1.66%
21	Agribank	11.85%	89.30%	0.44%	
22	Kien Long	19.30%	95.87%	2.57%	
23	MB	34.32%	134.87%	2.82%	0.79%
24	Nam Viet	29.16%	98.19%	1.08%	1.61%
25	Oceanbank	35.87%	236.22%	1.55%	0.78%
26	PG Bank	17.37%	102.61%	2.19%	1.10%
27	Phuong Tay	40.18%	154.45%	0.69%	0.60%
28	Gia Đinh	28.55%	72.65%	1.30%	
29	HD Bank	31.06%	117.47%	1.31%	
30	Sacombank	24.98%	97.69%	2.00%	0.46%
31	Southernbank	24.93%	84.82%	1.11%	1.50%
32	Tin Nghia	11.41%	89.72%	1.65%	
33	Vietinbank	14.79%	89.16%	1.50%	0.54%
34	SeAbank	36.08%	123.22%	1.93%	

	Bank	Income- and expense-based FSIs			
		Interest margin to gross income*	Trading income to total income	Noninterest expenses to gross income*	Personnel expenses to noninterest expenses
	Sector Level	77.32%	1.80%	44.37%	45.62%
1	Vietcombank	71.05%	7.36%	39.43%	56.55%
2	ACB	75.85%	4.79%	39.35%	44.94%
3	Habubank	59.21%	14.60%	30.60%	40.55%
4	Nam A Bank	65.65%	21.65%	42.73%	
5	SHB	81.83%	8.03%	45.73%	41.18%
6	Techcombank	67.48%	-0.05%	33.65%	47.52%
7	VIB	82.65%	4.35%	46.99%	
8	Bao Viet Bank	80.76%	16.21%	42.01%	41.52%
9	Đai A Bank	61.57%	28.16%	52.00%	
10	Đai Tin Bank	82.94%	-6.69%	35.91%	
11	Eximbank	78.55%	-0.39%	27.69%	53.41%
12	Lien Viet	92.23%	5.01%	38.50%	32.70%
13	MHB	92.25%	-2.27%	77.17%	
14	Tien phong	46.34%	1.71%	42.84%	
15	VPBank	82.30%	-4.86%	41.59%	44.00%
16	An Binh	89.93%	-1.34%	43.82%	42.61%
17	BIDV	80.01%	-0.02%	48.27%	55.47%
18	Maritimebank	74.41%	10.46%	35.82%	45.26%
19	Phuong Đong	89.52%	0.84%	40.06%	48.74%
20	Sai Gon cong thuong	47.28%	0.80%	22.71%	
21	Agribank	76.27%	1.03%	55.82%	54.73%
22	Kien Long	105.25%	-11.84%	38.35%	
23	MB	81.47%	-0.07%	29.03%	45.23%
24	Nam Viet	93.13%	0.26%	52.27%	44.47%
25	Oceanbank	103.53%	-7.36%	30.48%	40.61%
26	PG Bank	77.79%	3.97%	42.53%	45.84%
27	Phuong Tay	88.14%	10.88%	58.86%	44.75%
28	Gia Đinh	94.31%	0.83%	53.69%	51.23%
29	HD Bank	73.52%	-3.07%	47.55%	48.08%
30	Sacombank	76.95%	-12.57%	43.07%	
31	Southernbank	29.24%	53.60%	38.19%	
32	Tin Nghia	107.07%	-1.33%	30.24%	
33	Vietinbank	81.58%	-0.95%	48.57%	57.54%
34	SeAbank	78.11%	5.26%	31.05%	

APPENDIX 2:

Comments on some typical indicators of Vietnam Commercial Banks in 2010

Information and analyses in this paper is calculated and reviewed carefully based on the public financial statements of banks. However, the authors of this paper have no responsibilities on the accuracy of the information defined below. The comments and analyses in this part should be used as reference source

The authors classified 34 investigated banks based on banks' size into groups in which Big4 group includes Vietcombank, Vietinbank, Agribank, BIDV; G12 group includes Big4, ACB, Sacombank, Maritime Bank, Military Bank, VP Bank, VIBank, Techcombank, Eximbank. Indicators are calculated for each bank, group of banks and the whole group of 34 banks. Some banks have published the financial information inadequately, so that banks will be removed out of some indicator calculation

1/ Capital to assets

This FSI provide an indication of the financial leverage-that is the extent to which assets are funded by other than own funds – and another measure of capital adequacy of deposit-taking sector.

This indicator is calculated for 34 banks. The sector level's is7.46%. There are 11 banks of which indicator is lower than the sector level, including 9 of G12 and all of Big4. This indicates that major banks are using high debt rate, partly because of their abilities in attracting custumer's deposit.

Besides, this FSI also shows a latent risk, the bank's liquidity. Because the fact that capital is bank's , if it is too small in comparision with total resources, banks will remain liquidity difficultly. Agribank's indicator is the smallest with 4.78%, followed by MHB and Vietinbank with 4.83% and 5.09%, respectively. Large banks, although, are holding low capital to assets ratio but with their prestige, large quantity of capital, they can operate more stable and resist strong fluctuations from the economy. However, to the rest banks, this low FSI will be a ominous problem.

2/ Nonperforming loans to capital

This FSI is intended to compare the potential impact on capital of NPLs, net of provision. Provided that there is appropriate recognition of NPLs, this ratio can provide an indication of the capacity of bank capital to withstand NPL-related losses. However, the impact of NPL losses on capital is uncertain in most circumstances, as, for various reasons, the lender might expect to recover some of the potential NPL losses; for example, the borrower might have provided the lender with collateral or other forms of credit risk mitigation.

This FSI is calculated over 18 banks with sector level is 12.27%. BIDV, Vietcombank and Southernbank hold the highest ratios with 28.55%, 22.61%, 15.95%, respectively. Vietinbank is also in the group having high ratios with 8.15%.

The fact that most large banks' figures are higher than sector level's shows bad quality. This may result from many reasons, such as lending into securities or real estate sector, or considering borrower's application unappropriately. Debts of group 5 accounts for nearly 50% of total bad debt, partly reflecting business efficiency of Vietnamese enterprises in the crisis period.

Another reason is that banks has possibly coped with pressure from credit growth for profits but not paid attention to project appraisal and consideration of borrowers' solvency. In accordance with data of the State Bank, up to the end of June 2011, total bad debt of the banking system stood at about 75,000 billion VND, increasing by 50% as compared to the same period. At the end of July, the rate of bad debt was 3.04% on total outstanding loans, at the end of August 2011, it was 3.21% on total outstanding loans.

Debt uncollection or trading, transfer is also an important cause.

3/ Liquid assets (core) to total assets

This FSI is intended to show the bank's capacity to meet the money withdrawal which are expected or not.

In Viet Nam, this FSI was diversified in 2010.

- **Big 4:** Banks in this group, excluding Vietcombank, had this FSI below 20%. Specifically, BIDV: 17.79%, Agribank: 11.85%, Vietinbank: 14.79%. A majority of capital was used for the assets which are expected to be highly profitable. However, this also meant that risks were unavoidable. The low proportion of liquid assets indicated vulnerabilities in these banks if they faced liquid shocks (In case of uncertainties, these banks have extremely serious impacts on the whole financial system). Nevertheless, these are state-owned banks with large business scales so that they built the firm confidence for their customers. Thus, the possibility of these banks encountering liquid crisis was slim.
- **The banks facing liquidity problems such as:** Tien Phong (16,90%), SCB (10,98%), PG Bank (17,37%), Đai Tin (17,47%), Tin Nghia (11,54%), Kien Long (19,97%). Those banks that had this FSI under 20% and significantly lower than other banks. It was also noted that the two banks with lowest figures (SCB and Tin Nghia bank) along with De Nhat bank have just undergone the first emergence in bank sector in Viet Nam, which was adopted by the central bank. Tien Phong bank has also received support from external investors to overcome the difficult period.

  In G-12, excluding Sacombank which had this FSI of 16.85% (less than 20%) – the liquidity risk level of this bank is considered low owing to its operational scale and efficiency - all remaining banks have this FSI standing at high positions, above the average number at sector level.

4/ Customer deposits to total *(noninterbank)* loans

This FSI is intended to measure the banks' ability through making comparison between customer deposits and gross credit, excluding inter-bank loans. When the amount of customer deposit was lower than gross credit, banks would face vulnerabilities because banks use unsustainable capital to finance the assets that lack of liquidity.

The average figure for all involved banks was 102% that was considered to be safe. However, for individual bank, there were some banks having this FSI significantly below the average number such as: Đại Tín (84,14%), MHB (85,01%), Phương Đông (76,78%), SCB (87,16%), Gia Định (72,63%), Southernbank (84,82%), Tín Nghĩa (89,72%) and core banks like Agribank (89.30%), Vietinbank (89.16%). Agribank and Vietinbank have an ability to bear under the pressure of liquidity, but other banks are quite small and vulnerable.

5/ Return on equity

This FSI is intended to measure the efficiency of using equity. This FSI is high because of the high return level or the low capitalization and vice versa.

There were 10 banks having this FSI above the average figure of 20.41% at sector level. Of which, there were 8 banks belonging to G-12. Tecombank held the highest position of 32.83%, which was followed by SCB and Maritimebank (30.73%). On the contrary, Western bank had the lowest figure of 4.1% and closely after was GiaDinh bank with 4.72% and MHB (5.04%). There was a clear difference in banking system when core banks had this FSI much more higher than the smaller banks.

6/ Return on assets

This FSI measures the banks' ability to make profit in accordance with total assets.

The average number at sector level was 1.52%. There were 21 banks, which had 7 banks belong to G-12, having this FSI above the average figure. Of which, there was only Vietcombank – a bank in Big 4- having this FSI exceeding the average.

Although Big4's ROEs were classified as top group, their ROA was considered to be lower than other banks. It can be explained by non-performing assets, a huge amount of fixed assets and infrastructure of this bank group. However, it cannot be denied that state-owned banks have experienced the reduction of the market share, making way for proportional increase of joint stock banks. The competitive favors stemming from historical elements and other complicated "mechanism" relationships such as inherent large network, "traditional" relationships with state-owned enterprises, enjoyment of preferential resources from the Government. However, state-owned banks' strengths were also reasons which resulted in negative impacts on the competitiveness of these banks: the weakness in non-credit operations, inactiveness, etc.

7/ Nonperforming loans to total gross loans

This FSI is intended to measure the quality of loans and was calculated for 18 banks with data available. The average figure was 1.25% and there were 8 banks having this FSI above the average figure. BIDV was the bank with highest number of 2.15%, which was followed by Vietcombank and Phuong Dong bank with 1.91% and 1.75%, respectively.

The matter that many core banks possess a large proportion of NPLs indicated that quality of loans was not good.

8/ Interest margin to gross income

This FSI is intended to measure interest margin to gross income. This FSI can be affected by equity to total assets because with a certain amount of assets, more equity means less debts and this results in less interest expenses, more profits. This FSI for banking system in Viet Nam was 77.32% with 21 banks having this FSI above the average figure.

Commercial banks in Viet Nam has made profit mainly from interest, not yet dynamic in diversifying operations with the aim of seeking other sources of profit. However, this matter was appropriate because the financial market has not developed yet in Viet Nam, many banks which have just established remained weak, lack of experiences in taking part in other operations such as: securities trading, gold trading,...

Especially, some banks with this FSI above 100% meant that losses in other activities had to be compensated by interest. For example, Tin Nghia Bank had the highest figure of 107.07%, it did business at a loss in 2010 and the loss of 110971 million VND from FOX trading, gold trading and other losses of 62244 million VND. The two remaining banks had this FSI above 100% were Kien Long bank (105.25%) and Oceanbank (103.53%).

9/ Trading income to total income

This FSI is intended to capture the share of deposit takers' income from financial market activities, including currency trading, and thus help in assessing the sustainability of profitability. This FSI is calculated by using gains or losses on financial instruments as the numerator and gross income as the denominator.

In Viet Nam, according to the research group's calculation, this FSI at sector level is 1.8% in 2010 and the biggest figure belongs to Southern bank with 53.6%, the lowest figure belongs to Sacombank with 12.57%. Four core banks, which are big4, have modest numbers, of which, BIDV and Vietinbank's figures are below zero percent, two remaining banks are Vietcombank (7.36%) and Agribank (1.03%). There is only one Vietcombank's figure exceeding the average number. Overall, this FSI is low for all banks in Viet Nam, reflecting the unsustainable profitability in banking sector while taking part in financial market activities and Viet Nam banks have made money mainly from credit activities which bring interest income for the banks. However, in Viet Nam, activities aiming to earn profits on financial instruments in financial market are rather risky, thus, many banks had to face losses in such investments. Besides, banks with this FSI standing at high percentage like Southernbank ought to take the sustainable profitability into consideration because these risky activities contributed considerably into their gross incomes.

This FSI was not uniform amongst the banks. It proved that there were many ways for banks to look for profit and it depended on each bank. In fact, many banks had to pay price for such dangerous investments.

10/ Noninterest expenses to gross income

This FSI measures the size of administrative expenses to gross income *(interest margin plus noninterest income)*. This FSI measures the administrative costs in comparison with gross income and assesses the deposit takers' effectiveness in using capital.

In Viet Nam, the research group calculated that this FSI was 44.37% – such a high percentage, so, it meant that half of the gross income was spent on administration. Such a high figure meant that the administration was weak or this was due to the bank's plan to expand its performance. In Viet Nam, perhaps, both the elements contributed to this big number.

Of 4 core banks (belongs to big4), there was only Vietcombank's figure *(39.43%)* which was below the average number of 44.37% and all three remaining banks exceeded this average figure. More specifically, there were BIDV with 48.27% nearly equal to Vietinbank's number of 48.57%, Agribank with 55.82%. Overall, these FSIs for individual bank were quite similar, nevertheless, it worth careful consideration for banks with unusually high figures like MHB which had this FSI was 77.17%. If those banks were not expanding their scales, the banks had to take a look over their administration capacities.

In Viet Nam these days, a majority of commercial banks need to be expanded or invest in equipments, thus, the costs such as improving information systems, further education for staff are significant. This results in the high number for this FSI and it is understandable.

11/ Personnel expenses to noninterest expense

This FSI measures the incidence of personnel costs in total administrative costs.

On average, in Viet Nam, the personnel costs in bank sector made up approximately a half of administrative costs (45.62%). In main banks, this cost was more than that in smaller banks, for example, the figure was 56.55% for Vietcombank, 55.47% for BIDV, 54.73% for Agribank and 57.54% for Vietinbank in 2010.

According to 2011's statistics, the average income of staff at Vietcombank was 22.4 million VND per month and this big number are number one across the banking section in terms of staff's salaries. The average income is thanks to the before-tax profit of over 5,900 billion VND in 2011.

As Vietinbank's 4th quarter financial statement noted, the average salary in this bank was 20.27 million VND each month while the average income was 20.76 million per month. In 2011, Vietinbank gained a before-tax profit of 8,105 million VND.

In comparison with the average income of 18.52 million VND and the salary of 17.9 million VND in 2010, the salary of staff at Vietinbank in 2011 was nearly 3 million VND higher.

In 2011, the income of staff at Sacombank was highly possibly higher than in 2010 when the total payroll fund doubled but the number of staff increased by only 13%.

According to the unaudited financial statement in 2011 of mother Sacombank, expenses on staff doubled those in 2010, from 907 billion VND to 1,816 billion VND. Thereof, salaries and allowances increased from 817 billion VND to 1,690 billion VND.

In the financial statement, the specific average income at Sacombank was not mentioned; however, if we temporarily make a calculation that the payroll fund of 1,690 billion VND divided by 9,600 staff makes 176 million VND per year *(about 14.7 million VND/person/month)*. In 2009 and 2010, the average income of staff at Sacombank was 9.4 million VND and 8.6 million VND/person/month respectively.

Data based on the payroll and total number of staff in some banks shows that in 2011, the income of staff averaged about 16 million VND at ACB, 7-8 million VND at Extrimbank, etc.

In 2010, the average income of staff at Vietinbank ranked the first with 18.55 million VND/month and at Vietcombank the second with 17 million VND/month. The two banks gained the highest profits in 2010. Banks having sequent high income levels are SCB, Baoviet bank, BIDV, SHB, ACB, Techcombank and Lien Viet Post Bank.

It is noted that SCB ranked the third in average salary in 2010 with an average income of 13 million VND/person/month – increasing by 30% as compared to 2009. SCB is one of three banks incorporated into new SCB along with Tin Nghia Bank and Ficombank.

Other banks having an average income of over 10 million VND/person/month are Bao Viet Bank *(12.9 million VND)*, BIDV *(11.8 million VND)*, Eximbank *(10.6 million)* and SHB *(10.3 million)*. ACB – the largest of private banks – possessed an income of 9.9 million VND, decreasing 3.3% as compared to 2009.

Banks with low incomes are all small ones such as Westernbank *(5.7 million VND)*, Easternbank *(6.3 million VND)*, HD Bank *(6.4 million)*, etc.

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