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Vietnam economic environment and financial risks

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Vietnam economic environment and financial risks
Case: Vietnam Export Import Joint Stock Bank

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Abstract

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Vietnam Economic Environment and Financial Risks; Case: Vietnam Eximbank

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This thesis analyses Vietnamese economic and financial risks. The objective of the study is to research Vietnamese business environment and the risks involved in its financial market. In order to understand the practical economic activity, the Vietnamese bank, Vietnam Export Import Joint Stock Bank, has been used a case company.

The frame of reference of thesis includes the essential factors of Vietnam's economic environment. Moreover, there are also different financial risks which have affected to both nation and local enterprises development due to the world financial crisis in 2008. The thesis is based on literature and studies concerning this subject, recent articles and business analysis from the internet to professional magazine sources.

The thesis is implemented as a qualitative research which was carried out during the period of job placement in summer of 2010. After that, the study was developed in summer of 2011 by researching theoretical literature on this subject. In addition, this thesis also analyzes important business information about Vietnam Eximbank as the case study.

In conclusion, this research would like to analyze the key information assisting Vietnamese economy become one of the most highly rated markets in Asia. However, like other emerging markets, Vietnam also has the risks involved in acquiring sustainable development. These relates to administration, research and development, technology, infrastructure and especially the financial sector which is still a weak and vulnerable market. This is important for international companies to give the decision making investment.

Key words: Financial risk, sustainable development, crisis, emerging market

Contents

1 INTRODUCTION

1.1 Scope the study

Today Vietnam is one of the fastest emerging markets in the world with the average growth rates at seven percent in the last decade. This is a remarkable economic development figure in spite of the fact that most world economies have been struggling with the recession. Therefore, this thesis aims to analyze and present the overview of Vietnam economic environment.

Vietnam is also facing the serious issues concerning to international financial risks recently. These have negative impacts on both national and domestic enterprises development. This is the reason why the thesis focuses to research on the causes and effects of financial risks to Vietnamese economic environment.

1.2 Qualitative research

According to Keyton (2001, 11), there are two types of research methods, including quantitative and qualitative. In the qualitative research method, the researcher is the primary observer and the research aims to preserve the form of human interaction (Keyton 2001, 63). Therefore, qualitative research is subjective rather than objective.

Qualitative research is understood by the description of the material form or analysis. However, qualitative method used to investigate the reason of decision making rather than the concerned factors only. Therefore, it aims to focus on the necessary and vital problems. However, it is important to define the key material in order to analyze its significance. One way to do qualitative research is to establish a research hypothesis before finding the material (Eskola, Suoranta 2001, 19)

1.3 Purpose of the study

The purpose of this study is to analyze the Vietnamese economic environment and the financial crisis which caused negative impacts to Vietnamese economy. Vietnam Export Import Joint Stock Bank (Vietnam Eximbank) is used as the case study of the thesis in order to understand the depth knowledge of both national and local enterprises development. Therefore, this study aims to analyze the financial issues which explain the reason why Vietnamese enterprises hardly receive the essential credit. Vietnam Eximbank has to face the troubles in serving its clients due to the financial crisis. The study will seek to understand the Vietnamese economic environment from the perspective of daily practical business issues since financial institution plays a vital part in national development.

1.4 Structure of the study

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2 THEORETICAL BACKGOUND

2.1 Risk definition

In general, financial crisis applies in a variety of situations that show the loss of assets or value of financial institutions in a short period. In addition, the financial crisis is also determined in other situations such as stock market crashes, financial speculation and currency crisis. Hence, the financial crisis causes the loss of monetary value which is reflected by the price of asset. Many financial crises happened due to the banking collapse and economic recessions in the world economic history like the Asean financial crisis in 1997 and the world financial crisis in 2008.

According to the definition in a business dictionary (www.businessdictionary.com), the financial crisis is a situation in which the supply of money unable meets the demand for money. This will be harmful to the liquidity of the financial market since the available money is withdrawn from banks, forcing banks either to sell other investments to replace the shortfall or to face bankruptcy.

The Economist magazine (Wall Street's bad dream, September 2008) analyzes financial crisis as a situation in which the value of financial institutions or assets drops rapidly. A financial crisis always relate to a panic or a run on the banks. The investors sell off assets or withdraw money from savings accounts when they believe that the value of those assets will decrease if they remain in the bank.

2.2 Types of financial risks

2.2.1 Banking crisis

There are different situations that lead to a banking crisis. Firstly, when a huge number of depositors suddenly withdraw the money and lead to a run on the bank. The banks used to lend out most of the cash they receive in deposits. It is hard for bank to pay back all deposits if this happens. Consequently, the bank run will lead to bankruptcy and the depositors will lose their savings unless they are covered by deposit insurance. Secondly, a financial crisis might arise from a situation in which bank runs are widespread and people do not trust the safety of the whole banking system and cause banking panic. Thirdly, the banks do not have enough available funds for lending and cause the credit crunch. In this case, the banks become an accelerator of a financial crisis.

2.2.2 Financial market crashes and bubble

Garber (2001, 10) states that the financial asset is overvalued when its price exceeds the present value of future income. The evidence for a bubble happens when there are many market participants buying the asset to selling it later at a higher price, not buying for its income. Then it leads to the risk of financial market crashes. People tend to buy as long as they expect others do the same; however, this also lead to a run when many participants decide to sell. Therefore, it is difficult to estimate the true value of an asset in order to avoid financial bubble.

2.2.3 Currency crisis and sovereign

If a country has a fixed exchange rate but is suddenly forced to devalue its currency because of a speculative attack, this is defined as a currency crisis or balance of payments crisis. In addition, if a country fails to pay back its sovereign debt, this causes a sovereign default. Both of devaluation and default issues would destroy the healthy of an economy since foreign investors do not trust the stability of national economic and withdraw the capital inflows. Moreover, the government would also not receive the essential loans from international financial organizations for solving the domestic issues when they lose the reliability.

2.2.4 Economic recession

National economic recession used to happen when the GDP growth continuously drop in two or more quarters. If serious recession occurs in the long period, this will be considered as the depression. In spite of the fact that the prolonged recession does not directly affect the financial system much, however, it still causes the financial crisis when financial market plays a centre role in the whole economic activities.

Financial crises are also caused by recessions when the Great Depression maybe used as a symbolic example. The Great Depression in America led the bank runs and stock market crashes in the period of 1929 – 1930. Therefore, there is clearly link between economic recession and financial crisis under any circumstances.

2.3 Financial risk management

2.3.1 Principle of risk management

According to the principle of management of International Organization for Standardization, risk management means identifying, assessing, and analyzing the risks in which all economic resources would be applied to control, manage and minimize the negative impacts or improve and maximize the potential opportunities. Risks are caused by different sources such as the uncertainty of financial markets, project failures, legal liabilities, credit risk, accidents and natural disasters.
With reference to the ISO 31000 standard, risk management is processed by the following steps:

- Identify the risk in the concerned interest

- Plan the post procedure.

- Concentrate on the scope of risk management, the identity and objective of stakeholder, and the causes and effects of risks.

- Set up the framework activity and risk attention.

- Analyze the risks that involving in the whole process.

- Problem solving which base on the available technology, human and organizational resources.

2.3.2 Financial risk corporation

In the fundamentals of risk management, financial risk falls into four main categories. They are counterparty, funding, interest rate and currency risks (John Holliwell, The financial risk manual, 1997, Financial Times, Pitman Publishing). These are four essential factors that risk management has to focus and take them under control in order to be sustainable development. In which,

- Counterparty is the risk that others may not implement their business obligation such as financial, delivery, goods and services or to repay a borrowing.

- Funding is the risk which occurs both in trading and capital markets. A common problem is the overtrading issue when the level of sales can not be supported by the available working capital. Meanwhile, financiers always have to consider the liquidation as the key control in order to avoid seeing any run-out of cash flow, hence the banker mantra “Cash is King”.

- Interest is the risk that the lender or depositor may be unable to recover all or some of their money. Therefore, the higher interest rate will put the fund at more risky in case of being business crisis.

- Currency is the risk that will affect directly to the value of corporation assets, amount of liabilities, sale and cost because of the change of exchange rate.

2.4 SLEPT analysis

SLEPT analysis is the new market research method which is developed by PEST analysis previously. This model includes social, legal, economic, political and technology (SLEPT) factors for analyzing macro-economic environment. In addition, it is useful for a company would like to research and invest in the oversea markets since there are differences between the countries. The key difference between domestic and international markets is the multidimensionality and complexity of the foreign markets a company may operate in (I.Doole and R.Lowe, 2008, 7). Moreover, SLEPT analysis is also the cornerstone of any business strategy for understanding the market growth/decline, business opportunities, economic potential and operation activities.

Social factors may include the cultural, population, gender and education aspects. The social factors will decide how and what the company should comply for producing the right products and services. Beside, the company culture and management have to adapt those difference social factors because of the sustainable development.

Legal factors mean the discrimination law, consumer law, trade law, employment law, and investment law. These factors will decide how a company should operates, its costs, and the product demands.

Economic means difference factors such as economic growth, interest rates, exchange rates and the inflation rate. These factors will bring the major impacts to the successful of enterprise.

Political means the factors which a government intervenes and control the economy. Those are often showed through tax policy, labor law, environmental law, trade restrictions, tariffs, and political stability. In addition, political factors also include goods and services which the government would like to provide, encourage or restrict. Moreover, the policies of health, education and infrastructure would be the key to national development.

Technological factors are research and develop activity, automation, know how technology incentives and the level of technological. They can affect to production level, outsourcing and investment directly. Furthermore, technological level will decide the costs, quality, and innovation process.

2.5 SWOT analysis

SWOT is the traditional business analysis for writing the strategic plan. It often evaluates the strength, weakness, opportunity and threat which are involved in a business or project of enterprise. SWOT analysis is essentially description of conditions whereas strategies define actions (P.Kotler, K.Keller, M.Brady, M.Goodman, T.Hansen. Marketing management. 2009). However, a SWOT analysis must apply the objective of strategic plan in order to be useful in practical. SWOT analysis includes:

Strengths are the advantages of an organization or enterprise that may use and improve for receiving the sustainable growth in each industry.

Weaknesses are the disadvantages that any firm may to face and resolve since there is no perfect power, model or operation.

Opportunities are the external chances which create the greater sales or profits in its business environment.

Threats are the external factors in its business environment that may cause troubles or obstacles for the enterprise.

3 VIETNAMESE ECONOMIC ENVIRONMENT

3.1 Vietnam in review

Socialist Republic of Vietnam locates on the Indochina Peninsula in Southeast Asia region. Vietnam shares its border with China in the north, Laos in the northwest, and Cambodia in the southwest. With reference to the population of over 90 million, Vietnam is the 13th most populous country in the world.

Figue 1: Map of Vietnam

Source: Vietnam institute of geography

Historically, Vietnam was ruled under Chinese empires in more than one thousand year and finally became independent from China in AD 938. In 19th century, Vietnam was conquered by the French and became part of French Indochina in 1887. Vietnam declared its independence in 1945 in spite of the fact that France continued to rule until 1954 when they were defeated by Communist armed forces of Ho Chi Minh president. According to Geneva Accords of 1954, Vietnam was divided into two parts, the Communist North and anti-Communist South.

After that, Vietnam War had been well known around the world since American government's funding and military aid to South Vietnam grew in the decade of 60s in order to fire with the north opponent. However American army forces were withdrawn due to the cease-fire agreement in 1973. In 1975, North Vietnamese forces won the South and finally reunited the country under Communist rule.

Despite the end of war in 1975, Vietnam faced many troubles for recovering and developing the economic because of its politic system. However, with the new renovation policy in 1986, Vietnamese government committed to increased economic liberalization and deployed the structural reforms in order to modernize the economy and to produce the better competitive, export oriented industries. This was the key to open new Vietnam era which became one of the most fast growth rate economies in Asia till present.

Vietnamese key figures

Official name: Social republic of Vietnam

Capital: Hanoi

Largest city: Ho Chi Minh City

Official language: Vietnamese

Politic: Communism

Area: 331,698 km2

Population: 90,549,390 (2011 est)

GDP: US$ 104,600 billion (2010 est)

GDP growth rate: 6.8% (2010 est)

Currency: Vietnam Dong (VND)

Exchange rate: 1 USD = 20,060 VND

Labour force: 46.21 million (2010 est)

Unemployment rate: 2, 9% (2010 est)

Religion: Buddhism (85%), Christian (10%) and others

HDI: 0.572 (113th in the world)

3.2 SLEPT analysis of Vietnamese economic environment

Vietnam is highly appreciated as a stable politic and society. The country rarely faces religious restriction and race conflict like other ASEAN countries such as Indonesia, Philippines and China. In addition, Vietnam achieves high annual GDP growth rate, maintains stable politic and macroeconomic environment due to its renovation policies. Vietnamese Communist Party succeeds in governing the country stability throughout more than thirty years. Renewal policies also gains strongly support and the market economy transition is still developed yearly. Therefore, with reference to recent terrorism and violence events, Vietnam is considered as one of the most safety investment destinations. However, the thesis will use SLEPT anaysis for showing the Vietnamese economic environment clearly.

3.2.1 Social

3.2.1.1 Education

Vietnam has the state owned network of schools, colleges and universities throughout country. Besides the private education institutions are also growing recently. Vietnamese general education is divided into five categories as kindergarten, elementary schools, middle schools, high schools, and college/university. All the courses are taught in Vietnamese. There are many public schools have been organized across the country in order to raise the national literacy rate. In addition, a large number of specialist colleges are also established to meet the demand of diversification and skilled labor forces.

Today, the largest universities and colleges used to locate Hanoi, Ho Chi Minh and Da Nang City. In Vietnam, education from age 6 to 11 is compulsory with no tuition fee. Education above these ages is not free anymore. Therefore, the poor families in rural areas have trouble in paying tuition fee for their children without the financial support from public or private assistance. Vietnamese people always consider education as the most important of life and the school enrollment is among the highest in the world. The number of colleges and universities increased dramatically in recent years, from 178 in 2000 to 409 in 2010.

3.2.1.2 Population

According to the report of General Statistical Office, the population of Vietnam is more than 90,5 million in the end of 2011. However, Vietnam is considered as the young nation which has more than 46.2 million people in the labour force. Vietnam has 54 ethnic groups and the "Kinh " group is nearly 81,6 million, account for nearly 88% of the population. The population is concentrated in the Red river delta and coastal regions. In spite of the fact that Vietnam has 54 ethnic minority groups throughout country, the “Kinh” always control national politics and economics.

3.2.1.3 Culture

Vietnam is the symbolic agricultural country which relies on wet rice cultivation. With reference to more than one thousand year under Chinese rule, Vietnamese culture is affected much by the neighbour country. In addition, Cham culture and the cultures of other minority ethnic groups are all integrated with Vietnamese culture in correlated effects. The official spoken and written language of Vietnam is Vietnamese. Vietnam is considered a part of the East Asian Cultural because of the high influences from China throughout its history.

After 1975, Vietnamese culture life is strongly influenced by the state owned media and also the politic programs. However, accompany with the economic development, international cultural influences were popularized and highly appreciated, especially with western culture. From the decade of 1990s, Vietnamese youth has been affected much by the European and American culture and media.

3.2.2 Legal

3.2.2.1 Legal system

In Vietnam, the legal system includes the constitution, codes, laws, ordinances, decrees, decisions, circulars, directives, and official letters. However, all the laws which are passed by the National Assembly only would be referred legality. Rules are issued by the Standing Committee of the National Assembly. These often apply within area where the law is not officially declared and/or regulated. Until the National Assembly give the right to Government, the Government will issue decrees or decisions or directives for implementing the issued laws or ordinances afterward.

Circulars, decisions and regulations must be issued by the ministries officially. Other state agencies and also people’s committees have the right to issue the subordinate legal documents due to their areas of responsibility. However, the codes, laws and ordinances are referred by the name, decrees, decisions, circulars and directives based on the number, signing date, and the name of issuer.

3.2.2.2 Business law innovation

Recent years, Vietnam has the positive change in legal environment for improving the business operations and becoming more transparency like the developed economies. In 2005, Vietnamese government issue the new Law on Investment and the Law on Promotion of Domestic Investment which focuses to combine all legal investment documents, reduce the illegal activities between local and foreign investors. In addition, the new law investment also simplifies the investment procedures and gives the support conditions for capital attraction. This is a great improvement when the foreign investors always complain about the complicated procedures and management of the central authorities previously. Moreover, Vietnamese government assist companies to access investment credit with different types of assets for mortgage. The Civil Law encourages corporations to use moveable estates assets, intangible and tangible assets, mortgage loans.

In 2006, the final Law on Securities was also issued to regulate how the securities market and the stock exchange market operate legality. Both foreign and local investors are protected due to new Enterprises Law which requires investors participating in the key business activities of a company and pronouncing related information honest.

3.2.3 Economic

Vietnam traditionally was an agricultural economy based on wet rice cultivating. The Vietnam War destroyed much of the country's resources. After acquiring power, the Government created a planned economy for building up the nation. In 1986, Vietnam communist party officially introduced the new economic reforms which considered the free market economy elements as the cornerstone of strategy. This was called as Renovation or a socialist oriented market economy. Private sector was encouraged in industries, trade and agriculture. Recently, Vietnam has joined international integration by enlarging markets, developing trade lead with all countries in the world. Vietnam became an official member of association of south east Asia nations (ASEAN), participated in Asean free trade area (AFTA) and Asia pacific economic cooperation (APEC) through the increasingly signed bilateral and multilateral agreements. In 2007, Vietnam finally became an official member of world trade organization (WTO). Business environment has been greatly improved as a transparent market. Trade and technology barriers are also removed in order to use both internal and external resources effective.

The Vietnamese economy in key figures

GDP (official exchange rate): $103.6 billion (2010 est)

GDP (purchasing power parity): $276.6 billion (2010 est)

GDP - real growth rate: 6.8% (2010 est)

GDP - per capita (PPP): $3,100 (2010 est)

GDP - composition by sector:	Agriculture: 20.6% Industry: 41.1% Services: 38.3%

Unemployment rate: 2.9% (2010 est)

Population below poverty line: 10.6% (2010 est)

Investment (gross fixed): 35.1% of GDP (2010 est)

Public debt: 56.7% of GDP (2010 est)

Inflation rate (consumer prices): 11.8% (2010 est)

Exports: $72.03 billion (2010 est)

Exports –commodities: clothes, shoes, marine products, crude oil, electronics, wooden products, rice, machinery

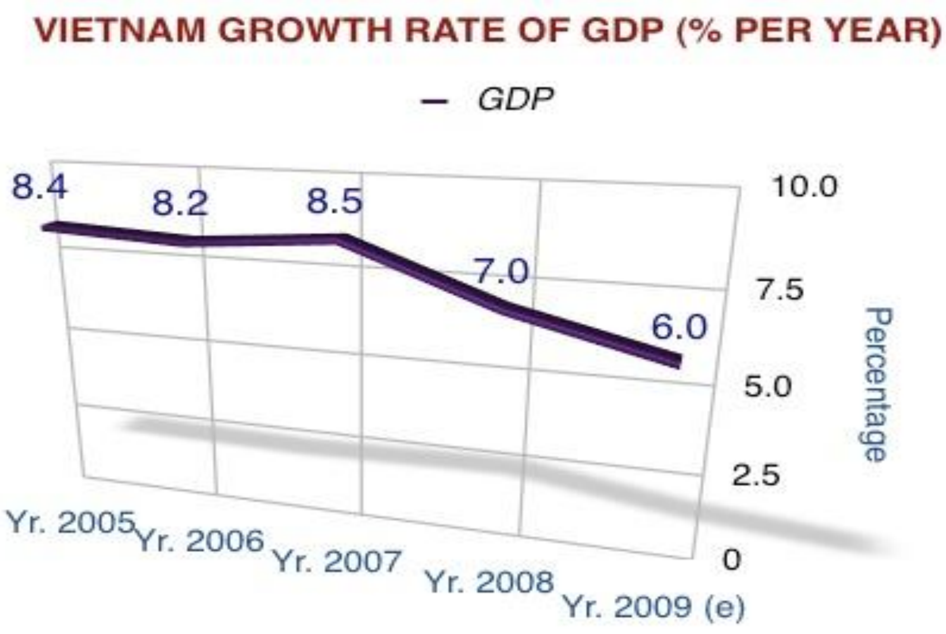
Imports: $84.3 billion (2010 est)

Imports – commodities: Machinery and equipment, petroleum products, steel products, raw materials for the clothing and shoe industries, electronics, plastics, automobiles

3.2.3.1 GDP growth rate

Vietnam achieved around 8% annual GDP growth from 1990 to 1997 and continued at around 7% from 2000 to 2005, became one of the world's fastest growing economies. During the post global economic crisis, Vietnamese economy continuously had a remarkable rapid and stable growth ratio. In spite of the fact that the global economic had been recovered slowly, Asian business region still grew strongly. Vietnam's GDP growth rate was the most impressive figure, behind China only.

Figure 2: Vietnamese GDP growth rate



(Source: Asian Development Bank's Outlook 2008, www.adb.org
Graph by www.Business-in-Asia.com)

This picture showed that Vietnam was one of the fastest growing economies in the Asia Pacific Economic Cooperation (APEC) region within the time of global economic crisis and remained its impressive growth afterward. Vietnam's economy growth achieved 5.3 percent in 2009 and 6.8 percent in 2010. It meant that Vietnam not only achieved a higher average growth rate but also a stable development. However, the speed of Vietnam's economic recovery still depended on global markets much when 60% of its GDP was exports.

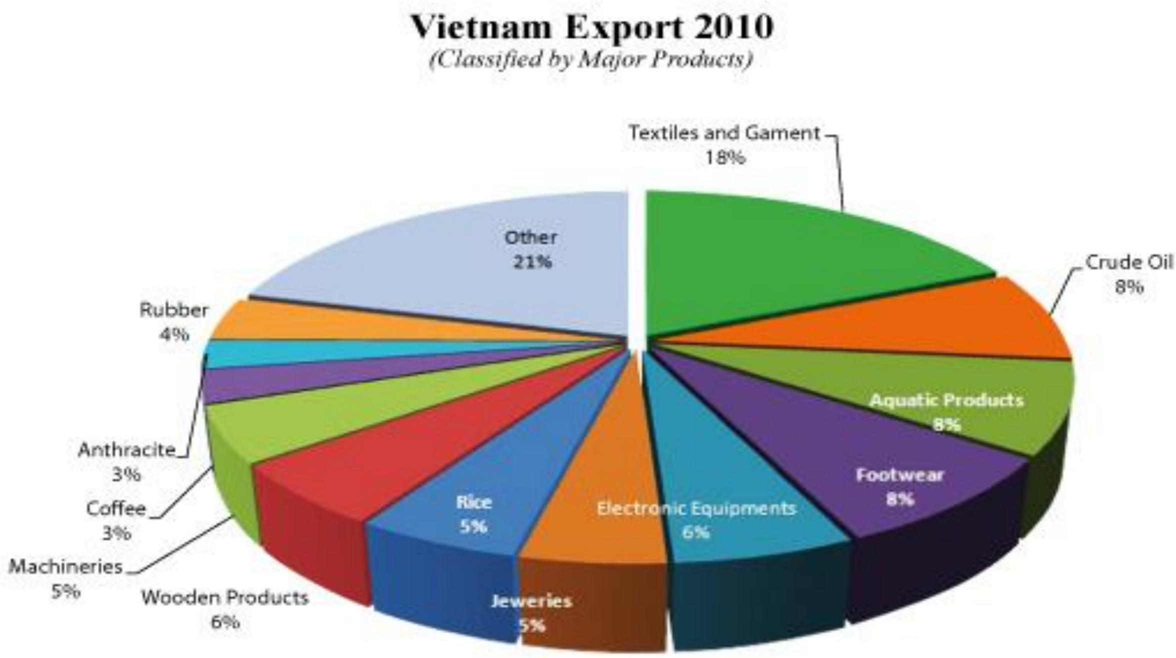
3.2.3.2 International trade

3.2.3.2.1 Export

In 2010, Vietnam' total export had the impressive growth which exceeded its previous business year nearly US$ 10 billions. This was an important encouragement despite a limited growth of global trade and decreased production of oil exports. In spite of the fact that, Vietnam's total exports met the first time of negative export growth which declined 8.9% in 2009, the exports turned back its frequent rapid growth in 2010. Total exports exceeded US$70 billion in 2010, equivalent to annual growth rate of 24%. This remarkable growth was highly appreciated because both global oil price and the production of crude oil exports were also declined and did not earn the large share of total exports as previous years.

Vietnam's exports (except oil products) accounted about US$67 billions, increased its exports volume twice after joining WTO in 2006. This remarkable export growth happened in almost business sectors and commodities. In 2010, the key export products concentrated in garments, footwear, oil, seafood, electronics and computers, wood products, handicrafts, rice, coal and other agriculture commodities. It showed a variety growth in the total export volume. The 'other' category meant all other goods, occupied a 47 % growth, higher than the rest categories. This figure indicated that Vietnam's exports varied its basket of products much and did not rely on any special strength. However, the new export commodities like pre-fabricated steel, transportation materials, plastic… were becoming more important in the future.

Figure 3a: Vietnamese major exports in 2010



Source: General statistics office, 2010

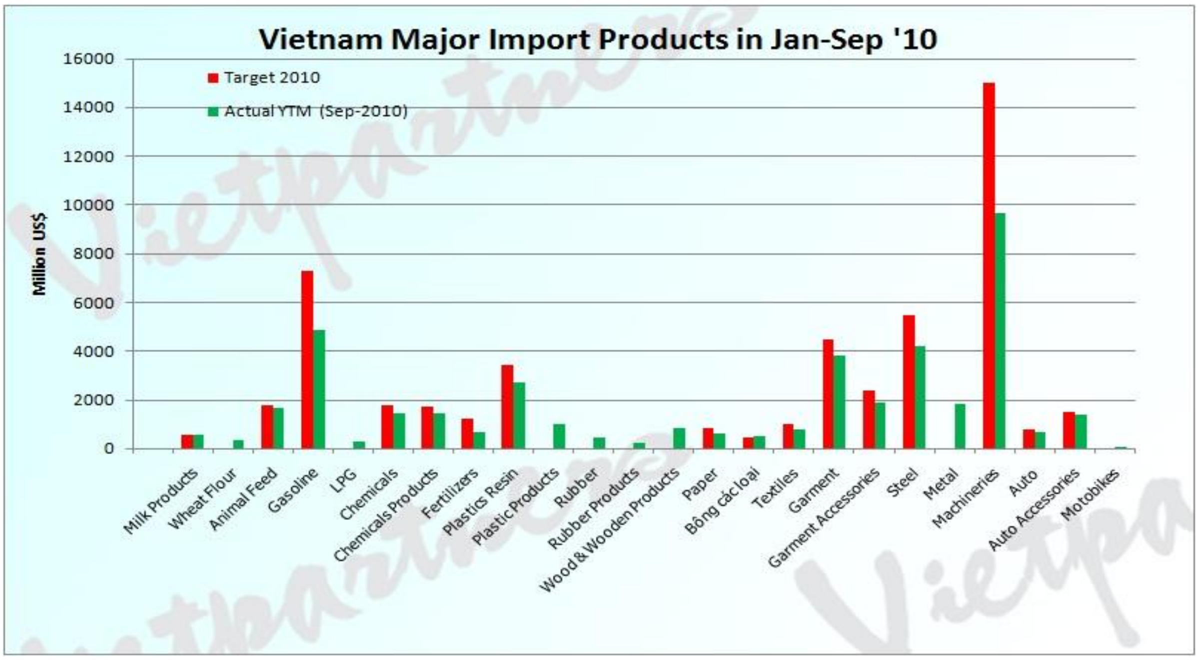
However, unlike Asian countries that used to consider China as the largest export market, Vietnam continuously relied on developed markets to increase its total volume of exports. America was still the biggest market of Vietnam's export, accounted more than 20% of Vietnam's total exports. Then it was followed by EU, ASEAN, Japan and China. In conclusion, industrialized countries accounted nearly two-thirds of Vietnamese exports. Despite some diversification of its export markets, Vietnam still faced many difficulties in term of global economic recession. Therefore, it had great efforts to penetrate in the developing markets like Brazil, India, Mexico, South Africa, Nigeria, Turkey and Middle East. These were becoming more important with Vietnamese exports in the future.

3.2.3.2.2 Import

Vietnam's imports used to grow rapidly but still lower than exports. The import growth was led by both the increase of demand and the needed inputs. In order to produce the exports, Vietnam had to import raw materials and intermediate inputs which gained a large share like chemical, rubber, paper, cotton, garments and footwear accessories, etc. According to General statistic office, Vietnam imports reached 71.63 billion US$ in 2010, increased 25.5% with 2009. However, current account deficit reduced to 12.85 billion US$ with 2009.

Despite Vietnam's exports concentrated on the industrialized countries, its main import sources came from China and other Asian markets. This trend created the trade surplus between Vietnam and the developed countries but there was also a huge deficit with Asian trade partners. Therefore, we could see two problems. Firstly, Vietnam was completely connected with the global production networks that ended in East Asia Pacific and ASEAN region. Secondly, like other developing countries which had the strength to export low cost and labour intensive products such as textile and footwear, Vietnam was also the final producer in this kind of global production network. Hence, it was a great chance for Vietnam to improve its position inside the world supply chains. Moreover, Vietnam could use regional trade agreements of ASEAN, APEC, WTO to join the global production network efficiency.

Figure 3b: Vietnamese major imports in 2010



Source: General statistics office, 2010

3.2.3.3 Investment

3.2.3.3.1 Government consumption and investment

In Vietnam, government consumption and investment were considered as the key factors of aggregate demand, especially after the 2008 world financial crisis. Real government consumption grew rapidly in

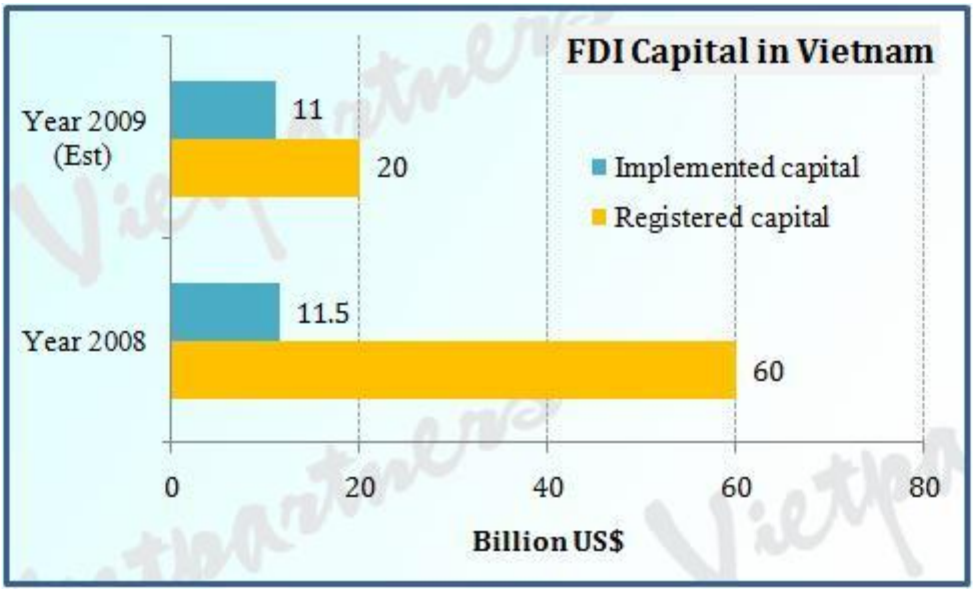
2009 (7.6 percent) and 2010 (6.9 percent). Even though government pronounced to reduce the investment for solving the budget deficit issue, its contribution to economic growth stayed the same from 2009 to 2010. The investment rate was so high that created some worries about its quality and sustainability. Government's consumption in 2010 was nearly 22% of total investment.

It was estimated that total government's implemented investment was over 40 percent of GDP in 2010. The private sector investment increased about 19%, equivalent to 38 percent of total investment. However, in order to gain annual 7 % economic growth, Vietnam had to invest 42% of its GDP. It equalled to the incremental capital output ratio of 7, this figure was 4 for China and 5 for India. In this case, government had to review its investment capacity. Therefore, how to raise the productivity of capital absolutely became one of the key targets in the Socio-Economic Development Strategy of Vietnamese government.

3.2.3.3.2 Foreign direct investment (FDI)

In spite of the fact that foreign direct investment (FDI) played an important factor of growth, there were some worries about the future prospect. In 2010, total committed foreign investment to Vietnam accounted to nearly US$13 billion. This was unexpected result in comparison with the amount of US$23 billion in 2009 and US$72 billion in 2008. However, the implemented capital increased by 7 percent, from US$ 8.4 billion to US$ 9 billion with previous year. In addition, negative factors like power shortage, lack of skilled professionals and unstable macroeconomic environment became the obstacles for investors to have the decision making. Hence, Vietnam continued to improve the investment environment and remained its attraction as one of the best destinations in Asia.

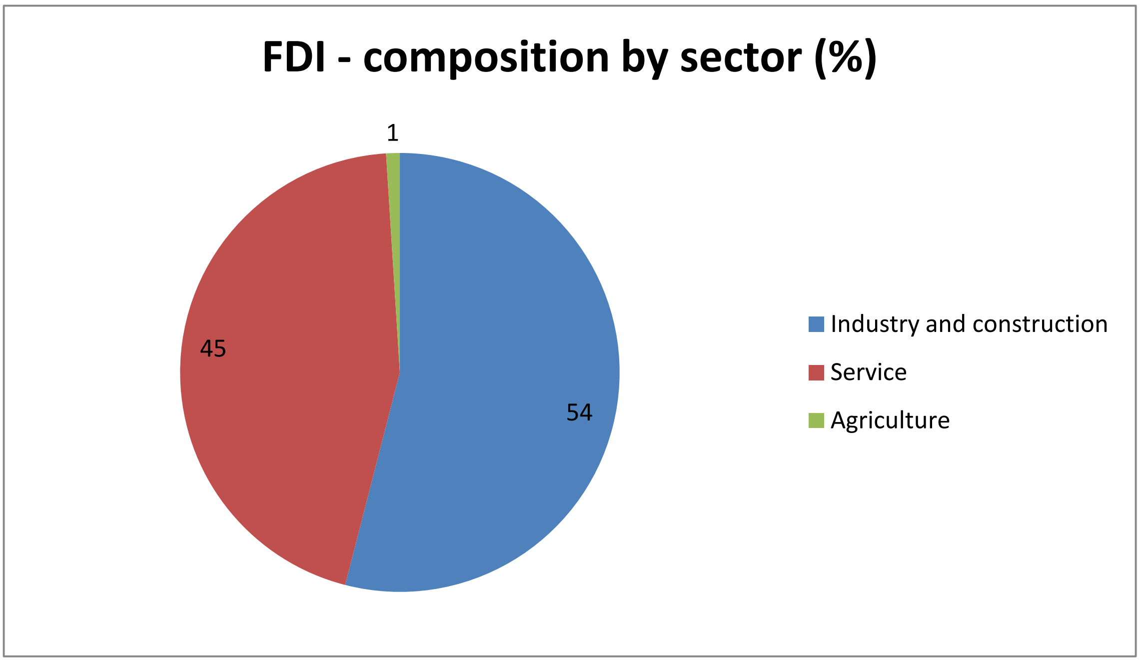
Figure 4a: FDI flows into Vietnamese market



Source: Ministry of Planning and Investment, 2010

Unfortunately, even though Vietnam desired to attract the FDI flows to industrial and high technology sectors, however, the capital tended to be shot-term investment and “raw” exploitation. With reference to the research and survey of Ministry of planning and investment in 2010, real estate (35.4%) and tourism service (40.9%) were two attractive markets of FDI. These were the popular transition trends in Vietnam after joining world trade organization (WTO) and showed the characteristic of short-term investment and speculation, not developed technology level and created the value added know-how in the whole economy.

Figure 4b: FDI – composition by sectors

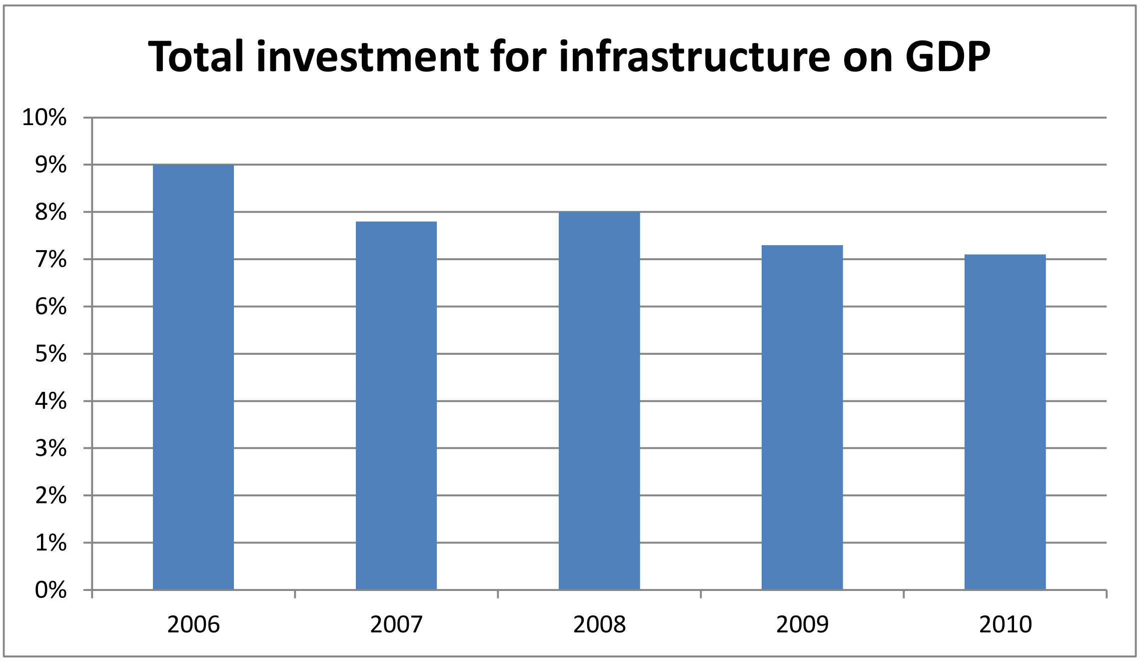


Source: Ministry of planning and investment, 2010

3.2.3.4 Infrastructure

In order to serve the economic development target, Vietnamese government concentrated on investing the infrastructure much. It is estimated that total annual investment for infrastructure was nearly 8% of GDP from 2000 to 2010, higher than international standard. The length of road system had been increased twice in comparison with the year of 2000. All urban and rural areas could use electricity system. There was 78% of rural people use pure water in comparison with the number of 40% in 2000 only. However, 40% of total infrastructure investment came from international loans and aids. Recently, total international committed loans were decreasing when Vietnam dropped out of the list of poor countries. Vietnam used to depend on the loans since the infrastructure investment required the huge capital and long term return. It was the challenge that government needs to find the solution for continuously improving its infrastructure system.

Figure 5: Government investment on infrastructure sector



Source: Vietnam Business Magazine, February 2011

In the 2010 Consultative Group Meeting For Vietnam, Mrs Victoria Kwakwa, Director of World Bank in Vietnam, advised that Vietnam should attract more foreign investment to infrastructure sector as the cornerstone of economic growth. It was the key factor for international investors when they would like to see the improvement of economic environment. In fact, Vietnam had great efforts to develop its infrastructure system in recent years. However, these had not met the demand of economic development, especially with transportation and electricity system. The lack of electricity occurred throughout country in the peak hours. It was the reason to decrease the productivity and also increase the cost of business. Furthermore, the weak transport system led the higher cost for logistic. This happened in rural areas and affected to agriculture business sectors seriously. Vietnam was no longer a poor country and this meant the decrease of Official Development Assistance (ODA) flows which used invest on infrastructure system. Therefore, Vietnam must increasingly improve its infrastructure system for attracting the foreign direct investment (FDI) flows.

3.2.4 Politic

Socialist Republic of Vietnam is a single party state. The cornerstone position of the Communist Party is assured inside government, politics and society. In general, the country has to be controlled under the leadership of the Communist Party. The highest representation is the Party Secretary General. The power of people is represented by the National Assembly at the central level and the People's Councils at different local levels.

The National Assembly is the supreme representative who issue the laws legality and determines both domestic and foreign policy. It is elected by universal vote. The National Assembly can elects or remove President, Vice-President, Chairman of the National Assembly, Vice-chairman of National Assembly, members of the Standing Committee of the National Assembly, the Prime Minister, the Chief Justice of the People's Supreme Court and the Head of the Supreme Office of Prosecution. In addition, the National Assembly has the responsibility to sanction the Deputy Prime Ministers and Ministers who were selected by Prime Minister.

The National Assembly is also responsible to approve the organization of the Government and its agencies. The legal duration of the National Assembly is 5 years. The official elections are held two months before the term is expired. The Standing Committee has the power to manage the daily activities of the National Assembly when there is no official meeting. During that time the Standing Committee has all its powers, even with the power of law making. The Head of State is the President who is elected by the National Assembly. He represents the Nation in both internal and external affairs.

People's Committees and People's Councils are the lower level. The People's Councils are elected by the people. After that, it elects the People's Committees. These procedures are implemented at the levels of city, province, district and commune. Each city, province, district and commune is governed by a People's Committee.

The court and prosecution systems are similar to the structure of administrative system. The Supreme People's Court is the highest justice admission in Vietnam. The Chief Justice is elected by the National Assembly within the term of the National Assembly. The Supreme Office of Prosecution has the highest power on prosecution in Vietnam. The Head is elected by the National Assembly in its term. These procedures are also applied at the levels of city, province and district.

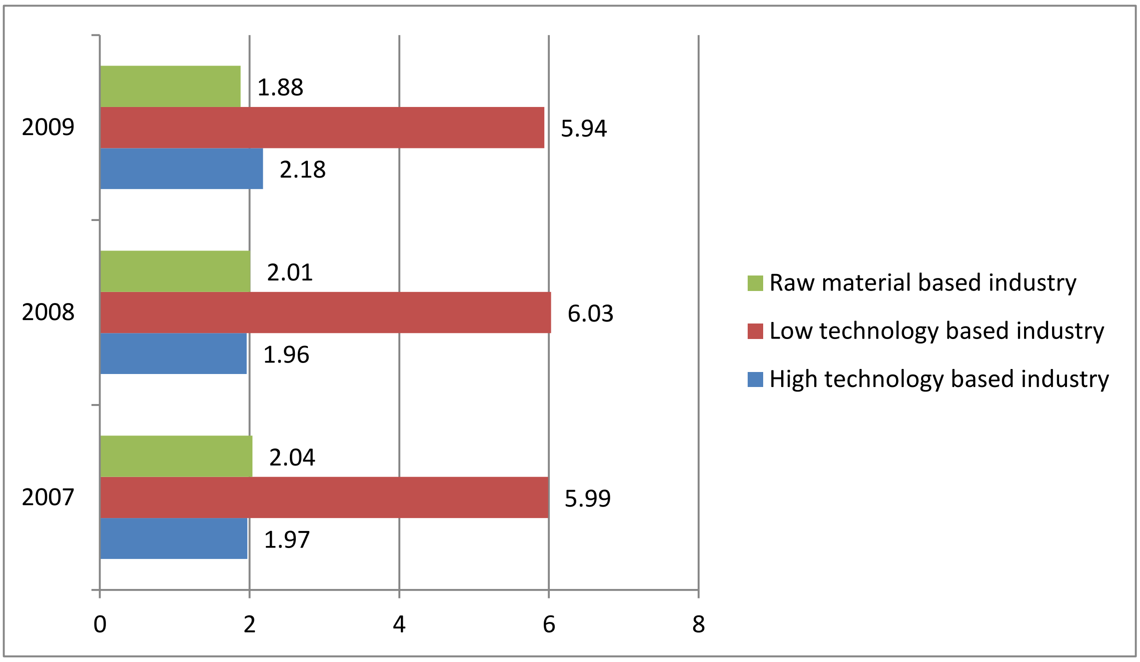
3.2.5 Technology

With reference to the politic system of communism, state owned enterprises (SOE) plays an important role of technology development of national economic based on the government investment. However, it also leads the poor and obsolete technology level because of the limited capital from the government. Otherwise, 98% of private enterprises are the small and medium enterprises (SME) only and hardly improve the technology level without the essential investment. Recently, Vietnamese government had great efforts to support private enterprises and continuously complete the equitization of state owned enterprises (SOEs).

Recently, private sector was not only treated fair but also estimated as the leading force of the economy. They gained high annual growth rate and contributed a largest share to the state budget during the period of 2005-2010. According to General statistic office, private sector achieved the highest growth rate even though it was the smallest sector. This accounted from 37% to 57.5% of the total volume of industry production in the period 2005 - 2010. There were about 200, 000 private enterprises and 89,000 farms had been established from 2005 to 2010 in agriculture - forest sector. Private sector’s products contributed to 67% of the GDP in 2010.

However, the masterpiece of Vietnam technology picture was still poor in general. According to the research of Vietnam institution of economic in 2010, industry composition based middle to high technology level was nearly unchanged in the period 2002 to 2008, increased from 24.6% to 25.4% only, lower than the average applied ratio of 60% in Thailand, Malaysia and China (2008). This had been showed in the industry exports composition clearly. In 2010, Vietnamese competitive technology level equalled to China in 1992, Thailand in 1988 and Malaysia in 1982 if it was estimated by GDP per capita. Moreover, the key exports were textile, shoes, wood products, agriculture which contained low technology or know-how goods. This absolutely was the chronic weakness of national economy.

Figure 6: Industry exports – composition by technology level



Source: Vietnam institution of economic, 2010

3.3 SWOT analysis

3.3.1 Strength

Vietnam is one of the most attractive markets in Asia Pacific region. During the 90s decade, Vietnam achieved the high GDP growth rate around 7.6% per year. This continued to increase the impressive ratio around 8% from 2001 to 2007, behind China only. In spite of the fact that the world financial crisis in 2008 affected to Vietnam much, the nation economy reached the average growth rate around 6.8% from 2008 to 2010. The statistical shows that Vietnam is the very stable economy.

Vietnam has the high quality human resource with low cost. There is over 46 million of population in the labor force and 65% of them are under the age of 30. In which, there are more than 90% of labor force achieves high school diploma and above. Thus, they are the essential skilled worker resource for enterprises. Meanwhile, the average salary of Vietnamese worker is US$ 1500 per year only. This is the reason why the foreign investor always considers as the most attractive factor of Vietnamese economy in comparison with the other Asian markets.

Recently, Vietnam has joined the globalization process strongly. Vietnam is the official member of APEC, ASEAN and WTO. Moreover, there are many bilateral economic agreements have been established with the world largest economies such as America, Japan, China and EU. Foreign investors who invest in Vietnam will also have the chance to enter ASEAN free trade agreement (AFTA) market with over five hundred million consumers.

Vietnam has the rich natural resources. This is showed clearly by the key exports when they acquired about nearly 40% of total Vietnamese exports. Accompany with the advances of textile/garment and footwear, the principal exports are crude oil, fishery and seafood products, rice (world's second largest exporter), pepper (world's largest exporter), wood products, coffee, rubber … etc.

Vietnam has the stable investment environment due to its steady politic life. Foreign direct investment during the period of 1988 to 2003 reaches US$ 40.5 billion. However, the average FDI flow raises around US$ 12 billion from 2004 to 2010. The statistic shows that foreign investors have increasingly trusted in the development of Vietnam economy.

3.3.2 Weakness

Vietnamese economy has the low level of composition. Agriculture still plays an important role in domestic economy with 20.6% but it relies heavily on the raw materials and processing. The service sectors occupies more than 38% only and do not affected much to the value added composition of economy as expected. In spite of the fact that Vietnam has the rich natural resources but those are exploiting so much that many of them will be run out in the near future such as coal, oil and forest.

Vietnam has the low technology level, especially in the industry sector. Research and development are the cornerstones of national development but they are not invested enough due to the limited capital from both state and private sectors. This issue is still the trouble that Vietnam has to face in the long time. It is also the reason why Vietnam exports are raw material based products only. The textile and footwear exports are also the semiconductors and do not earn the high profit.

Vietnam has the weak infrastructure in order to serve and follow the speed of economic development. According to General statistic office, Vietnam spends about US$ 6 billion yearly for constructing the road, highway and bridges in the last decade. However, this is still not enough for improving the national competition level as the yearly expected amount of US$ 15 billion till 2020. In addition, electricity is also the serious trouble since it is impossible to supply enough electric for all economic sectors. This issue leads many enterprises reducing the productivity much, especially with industry sector.

3.3.3 Opportunity

Vietnam has a large domestic market with the high speed market development. According to the Global Retail Development Index (GRDI) of A.T.Kearney in 2008, Vietnam replaced the first position of India and became the most attractive emerging market destination for retail investment. It was driven by a strong GDP growth rate, better investment policy and the increase of consumer demand for modern retail business. Vietnam was becoming an attractive expansion opportunity for global retailers. Vietnamese were among the youngest consumers in Asia and increased the consumption spending more than 75 percent from 2000 and 2007. In addition, urbanization was also growing strongly. This trend concentrated on Ho Chi Minh and Ha Noi rapidly. Those were two largest cities and also the fastest growth rate markets.

Vietnamese government planned to remove business restriction to foreign retailers in the domestic market and established a new program to develop wholesale and retail real estates in 2010. With reference to the rapid growth income and the open regulations, Vietnam retail market increasingly attracted international corporations, especially in service sector. However, due to the negative impacts of world business recession, Vietnam dropped to 14th position in 2010 since the inflation issue affected to consumer spending much.

Table 1: A.T. Kearney Global Retail Development Index, 2008

Country	2008 Rank	2007 Rank	Change
Vietnam	1	4	+3
India	2	1	-1
Russia	3	2	-1
China	4	3	-1
Egypt	5	14	+9
Morocco	6	15	+9
Saudi Arabia	7	10	+3
Chile	8	6	-2
Brazil	9	20	+11
Turkey	10	13	+3

3.3.4 Threat

Accompany with the economic development, urbanization has increasingly developed but lead the unfair income issues between social classes. The wealth distribution distance extends so much between rural and urban areas. According to General statistic office, the average urban income earns more nearly 4 times of rural worker in 2010. It is creating the unstable society problems and government has to close the gap for implementing the sustainable development.

Vietnam lacks the essential funding for research and development. A local enterprise becomes uncompetitive in Asian region. International corporations always consider Vietnamese enterprises as the semiconductors or outsourcing suppliers. This will not bring the bright future to domestic companies in the globalization era and also improve the competition level of country.

Recently, economic development causes the environment polluted issues seriously. This is not cared in the long time and reduces the living condition much, especially in the industry zone areas. In addition to the climate change, Vietnam faces many natural disasters in the midland and also destroys the infrastructure system. It is impossible to be compensated by the economic development since the environment polluted will destroy all achievement.

3.4 Vietnamese financial risks

3.4.1 Inflation

Recently, Vietnam has been facing the inflation issue seriously due to the world economic recession. United State and Europe Union – two largest investors cut down the foreign direct investment (FDI) flows and led the devaluation of Vietnam Dong (VND) because of the lack of foreign reserves. It was estimated that inflation rate stood at 11.75% in 2010. This happened because of the unstable economy and the related factors inside and outside country. The price of many essential goods and products rose more than 10% such as: oil, gas, metal, foods and materials. In addition, gold rose to the world record price at nearly 1,500 US Dollars per ounce and led the negative impacts to VND when people changed their assets to gold, rather than keeping VND.

According to General statistic office report in 2020, consumption price index (CPI) increased to 11.75% in comparison with 2009. The high rate sectors concentrated in food stuffs (20.6%), beverage (12.8%), construction materials (9.6%), education (9%) and textile (7.18%). Those are caused by the increase of material (input) prices since Vietnam used to import the materials for producing the consumption goods. In addition, the floods and droughts in middle land caused the decrease of agriculture production and pushed the costs of consumption goods higher as expected.

Figure 7: Vietnamese inflation rate in the first quarter of 2011

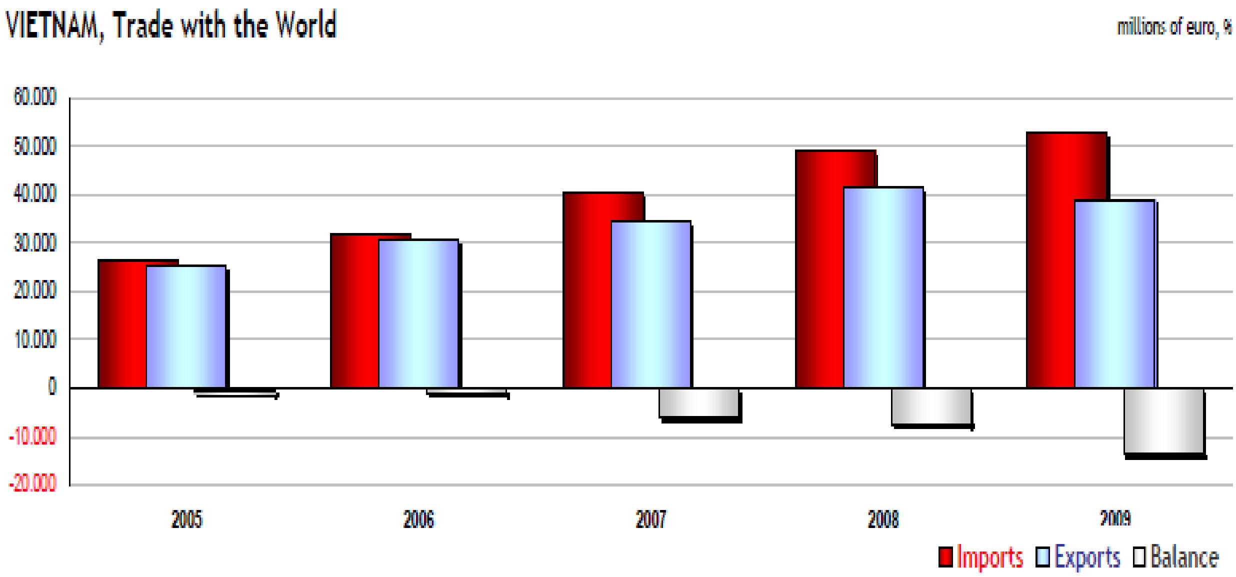
Source: General statistic office, 2011

3.4.2 Trade deficit

Since the economic renovation in 1986, Vietnam became the export oriented economy completely. However, trade deficit used to be one of the key factors to economic development. It was estimated that Vietnamese exports accounted about US$ 68 billion and imports were about US$ 81.5 billion. This meant that trade deficit valued at US$ 13.5 billion in 2010. In spite of the fact that trade deficit decreased about 500 millions US Dollars in comparison with previous year, it was still the huge amount and harmful to Vietnamese currency. Moreover, the deficit between imports and exports had not been shorten as expected.

According to national economic committee, trade deficit occupied more than US$ 13.5 billion, equal to 12% of GDP in 2010. This happened in the long time and decreased the foreign currency reserve, increased national debt and devalued VND. With reference to the huge deficit amount of trade balance, national budget and the increase of government debt, Vietnamese economy has been facing the serious financial risks. Therefore, it is difficult to lead the economy to sustainable development without any improvement of its current account balance (CAB).

Figure 8: Vietnamese trade balance picture in 2010



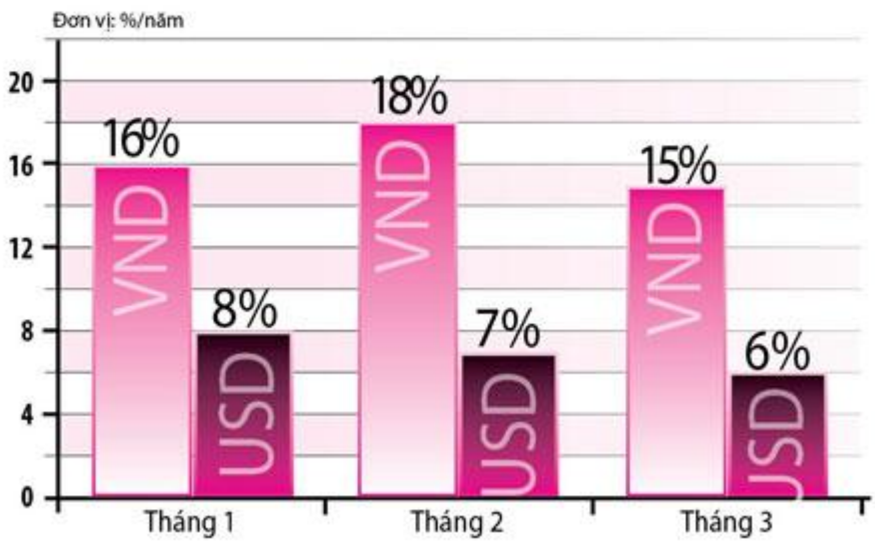
Source: Vietnam economy time, 2010

International monetary fund (IMF) warned that current account deficit (CAD) should not excess 8% of GDP in order to keep the macro-economic safety. That was why Vietnamese government had to change its trade policies for reducing the trade deficit to US$ 10.9 billion in 2011. Vietnamese economic is targeted to have the trade surplus from the year of 2015. However, this requires much efforts of government to achieve its goals when the world economic recession unable to recover in the short time.

3.4.3 Interest rate

From 2008 to present, lending interest rate of Vietnamese banks rose to the incredible ratio due to the effect of inflation issue. The lending interest rate even stood at 20 percent per year in June of 2008, the record of Vietnamese financial history. The high ratio was continuously applied in the first quarter of 2011 which accounted about 17% in average. According to Ministry of Finance, Vietnamese economy had been impacted by the world financial crisis in 2008 and led to both the downfall of banking credits and the lack of cash seriously.

Figure 9: Average saving interest rate per year in the first quarter of 2011



Source: State bank of Vietnam, 2011

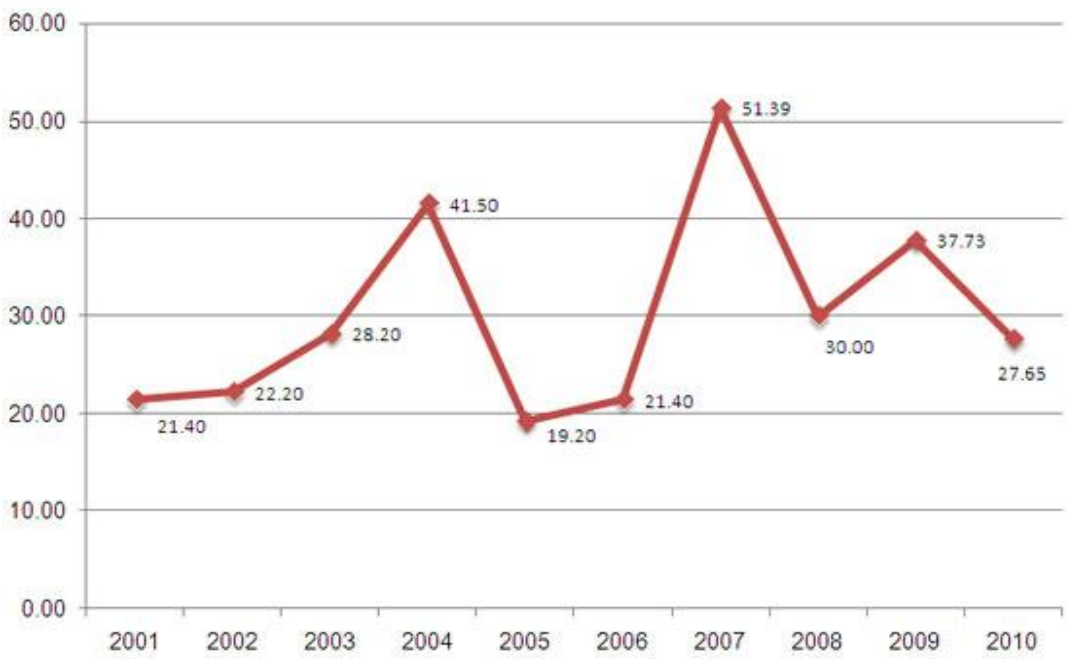
The high lending interest led the reduction of investment, productivity and credits to Vietnamese enterprises, especially with small and medium enterprises (SMEs). Hence, the inflation control policies of government needed to solve this issue. All local banks stated that the limited credits forced them had to increase the saving interest rate to 15 % or 16 % per year. Therefore, the lending interest rate also rose to 19% or 20% per year. This was the reason why Vietnamese banking interest rate stood at the highest level in the world in 2010.

According to the financial market survey of Vietnam economy time (2010, 18), many Vietnamese enterprises admitted that they needed a lot of banking loans in order to invest and enlarge the capacity. However, 80% of Vietnamese corporations could do nothing because of the record loan rate. The average lending rate was about 18% in two recent years and the enterprises could not earn profit. However, Vietnamese banks also faced the lack of cash in spite of the fact that the saving interest rate was at highest level. Those issues happened during the last two years and there was absolutely no efficient solution till present.

3.4.4 Bubble real estate and credit risks

Vietnamese real estate was the fastest growth business sector in the last two decades. Accompany with the nation development and urbanization, Vietnamese real estate market became one of most expensive places in the world, especially in Hanoi, Ho Chi Minh and Danang cities – three largest economic centres. It became the serious issue since Vietnamese income were in the low level but the urban real estate prices were as expensive as United State and European markets. There were billions US Dollars had been investing in housing, trade centres and building market. According to Ministry of Construction, more than ten billions US Dollars credits had been financed in 2010, increased by 22% in the previous year.

Figure 10: Real estate lending ratio on total financial credit



Source: Vietnamese association of banks, 2011

Vietnam economy time report in 2010 showed that there were about four hundred thousand people moved to Ho Chi Minh and Hanoi city (two largest economic centers) yearly in the last decade. They were students and people from rural areas due to the urbanization and economic transition in Vietnam. This issue created the high pressure to cities infrastructure and pushed real estate price in

Hanoi and Ho Chi Minh cities rose to 800% from 2000 to 2010. However, about 80% of real estates belonged to the speculators when the supply was always below the demand curve. The average apartment price was about US$ 1,150 per square metre and housing price was about US$ 2,900 per square metre in Hanoi and Ho Chi Minh cities. Those prices were so high that a small amount of consumers could pay since Vietnamese average income was US$ 1,165 per year and US$ 2,800 per year in urban areas.

Recently, Vietnam faced the bubble real estate issue when almost business sectors and consumers concentrated on investing so much money that led real estate market price to go far away its real value. Therefore, the financial bankruptcy problem absolutely might be happened in the near future if there was no control or restriction of government policies. Moreover, it was dangerous with Vietnamese economy since the key economic production sectors hardly received the essential loans because of the limited financial sources. It was the reason why Ho Chi Minh real estate market – the largest economic centre, had been falling down rapidly from 2009 to 2011 because the supply crossed the demand in practical.

In 2011, Vietnamese government pronounced the policies to control and reduce the credits of non-production sectors in order to stop inflation issue, especially with real estate and stock markets. It was estimated that the total credit growth of economic could below 20% and 16% for non-production sector. Moreover, State bank of Vietnam also decided to increase the obligated reserve ratio to 6% with foreign currency and 5% with VND to whole banking system.

3.4.5 Stock market

Accompany with the world financial crisis in 2008, Vietnamese stock market (VN-Index) lost 60% of value till the first quarter of 2011. It happened since the government policies aimed to control the inflation issue by supplying the capital flows to manufacture and industry sectors rather than stock market and the lack of cash flow of economy.

Figure 11: Chart flow of VN-Index and HNX-Index (primary market) in 2010

Source: National financial committee, 2010

In addition, the world economic recession increasingly led negative impacts to Vietnamese vulnerable financial market. Vietnamese stock market (HOSE) felt down rapidly in the first quarter of 2011. According to Financial Times (2010, 8), total market capital of VN-Index felt down to more than US$ 30 billion, equivalent to 33% of GDP only and the average daily value was US$ 30 million in the first quarter of 2011. Investors were worrying about the inflation issue when it increased to 19.78% in the first quarter of 2011 only. Moreover, they were also scared about the high lending interest rate which can pushed local enterprises to bankruptcy problem.

The unstable economy issues had been causing the domino drop-out of stock market. Investors were not laying the belief on government efforts and led to the bear market since all people were running away and throwing everything out of windows.

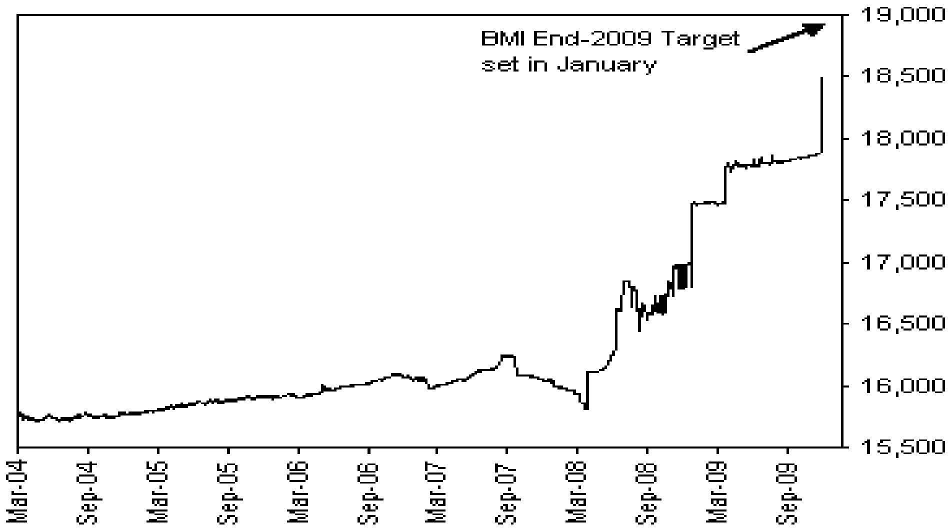
3.4.6 Exchange rate

Vietnamese currency (VND) lost 26% of its value in the last 7 years. However, it was extremely started from 2008 due to the world financial crisis. In the first quarter of 2011, VND lost 8.5% of its value when State Bank of Vietnam issued the new exchange rate. The official exchange rate was 20,600 VND in

1US$. With reference to the inflation rate of 12% in the first quarter of 2011, many financial experts are forecasting about the devaluation of VND in the near future if there is no incredible change.

In theory, devaluation of VND would increase the exports, reduce the imports and improve the trade balance. This also decreases the expensive imports which lead the inflation. However, the foreign currency reserve reduced to US$ 10 billion in comparison with US$ 16 billion in 2009 and US$ 24 billion in 2008. Accompany with the fall down of foreign currency reserve, there were many macroeconomic issues had not been resolved such as inflation, trade deficit, government consumption, etc… Those led the vicious circle of devaluation, budget deficit and inflation to Vietnamese economy within the last three years. In practical, VND continuously lost the value in spite of the fact that almost Asian currencies were increasing the value in comparison with US Dollar.

Figure 12: The change of exchange rate of VND vs USD from 2004 to 2009



Source: State bank of Vietnam, 2010

Today, VND is still the fixed exchange rate and under the control of State Bank of Vietnam (SBV) in order to avoid any negative impact with its vulnerable economy. In addition, this is also the tool of government for adjusting the policies. Previously, VND used to be undervalued for encouraging the exports in the long time. However, it is also one of the key factors to raise inflation rate and Consumption Price Index (CPI), especially in the time of world financial crisis. According to General statistic office, inflation and CPI were always above 20% from 2008 to 2010 and turn the living standard down seriously.

3.4.7 National debt

At present, Vietnamese reliable debt index had been dropped by many international financial institutions. According to publication of Moody's Investors Service (December, 2010), this organization reduced national reliable debt index from B1 to Ba3. In the report of Vietnamese public debt, Mr Tom Byrne, Vice president of Moody's pointed four issues that brought national debt index down. They were:

Firstly, according to Moody's, Vietnam was facing the risk of increasingly trade balance crisis. The risk started from the increase of trade deficit, capital withdrawal of international investors, the reduction of foreign currency reserve and devaluation pressure of VND.

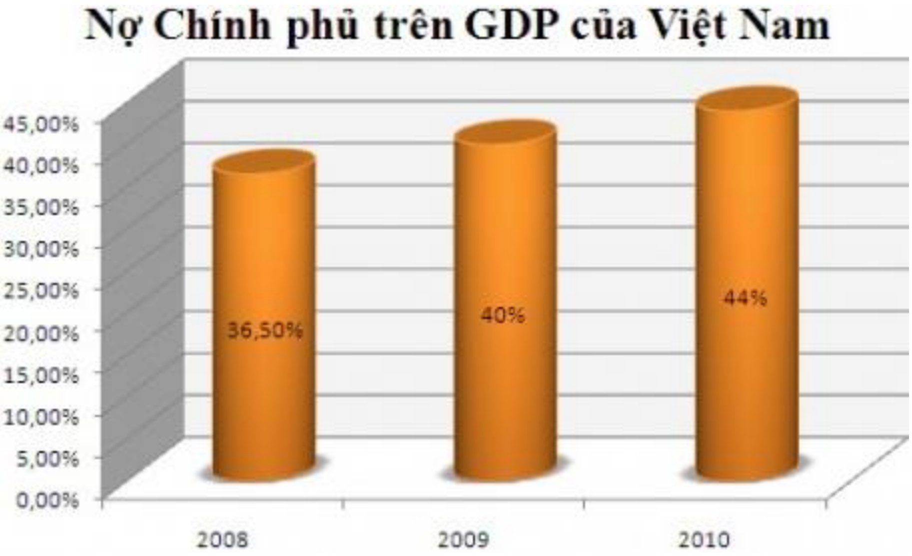
Secondly, inflation rate increased to more than 10%, the exchange rate was under pressure, led to the capital withdrawal in international balance of payment.

Thirdly, there were many dissent policies of economic development pushed the increase of national debt in charge of state owned enterprises (SOEs) and banking system.

Finally, many largest SOEs had the bad debt with a huge amount of payment, especially with Vietnamese shipping corporation (Vinashin). Moreover, Vietnamese government also lacked essential capital in order to give the financial support to the largest SOEs.

Mr Tom Byrne, Vice president of Moody's said, "Moody's believe that the inefficient economic policies make Vietnam hardly solving the pressure of balance of payment and lead to the unstable economic issues at present. Vietnamese government should continuously improve the economic policies in order to meet the demands of changing world business environment".

Figure 13: Government debt on GDP of Vietnam



Source: General statistics office, 2011

According to Ministry of finance, Vietnamese public debt was about 56.7% of GDP in the end of 2010. In which, the external debt of the whole economy was US$ 30 billion, equivalent to 28.5% of GDP. It was the reasonable level of international standard but still led the high pressure to current account balance (CAB) issue and the decrease of foreign reserve.

3.5 Vietnam financial risk management plan

Due to the negative impacts of world financial crisis, Vietnamese government pronounced the urgency regulation which concentrated on the key seven solutions in order to control the unstable economy issues in 2011. They included:

- Manage the monetary base control policy carefully
- Deploy the fiscal balance base control policy.
- Reduce the deficit financing.
- Reduce budget deficit.
- Improve the industry productivity.
- Reduce the trade deficit.
- And adjust the consumption prices.

This package solution was implemented immediately for controlling the inflation of consumption price index (CPI) and reducing the burdens of poor people.

Figure 14: Monthly CPI growth rate from 2010 to 2011 in Vietnam

Source: Vietnam economy time, 2011

Mr Nguyen Tan Dung, Prime Minister of Vietnam has presented the new monetary and fiscal policies in 2011. Those policies concentrate on stabilizing the exchange rate in order to make Vietnamese people believe in the value of local currency. Moreover, government has to increase the budget revenue to 8% and decrease the deficit financing to 10% in the fiscal year of 2011. With reference to the interview of Prime Minister Nguyen Tan Dung (Vietnam economy time, Feb 2010, 2), in order to acquire its targets, the government needs to follow:

Firstly is to implement the monetary policy carefully and flexibility for controlling the credit growth rate under 20%. In which, the primary credits will be offered to agriculture production, material industry and infrastructure sectors based on the approved plan of fiscal year. In addition, interest rate would be reduced to the acceptable level for supporting domestic enterprises. Government will use interest rate as the tool of inflation control.

Secondly is to manage the exchange rate flexibility due to the change of market. The Bank of Vietnam will call and use all regulations and resources for controlling the exchange rate, not devaluate the value of VND under any circumstances. Otherwise, all largest state owned enterprises have to sell the foreign currencies to the state bank in order to assure the safety reserve ratio. This is the key solution that Vietnamese government used successfully in the 2008 financial crisis. Moreover, the ineffective projects will be stop funding immediately and restructure the public investment base on practical demands.

Thirdly is developing the key industries, encouraging the variable exports and strongly reducing the import deficit by high tax policy on luxury goods. The prices of many agriculture products have been increasing due to the lack of world supply. It is the good chance for Vietnamese products exports and enlarges its market share. Improving the living standard of farmers, resolving the trade balance issue, and reducing the pressure of exchange rate are all key targets.

4 CASE STUDY OF VIETNAM EXIMBANK

4.1 Introduction of Vietnam Eximbank

4.1.1 Profile

Name and form of the company: Vietnam Export Import Joint Stock Bank (Vietnam Eximbank)

Line of business: Financial sector

Products / Services: Individual and corporate credits, financial investment, international settlement, foreign
currency trading, gold trading and card services

Turnover: 278 millions US Dollars (2010)

Total assets: 6.15 billion US Dollars (2010)

Net profit: 75 million US Dollars (2010)

Number of employee: 3,927

Organization structure: Joint Stock Corporation

Listing: Ho Chi Minh City Stock Exchange (HOSE)

Type of stock: Common

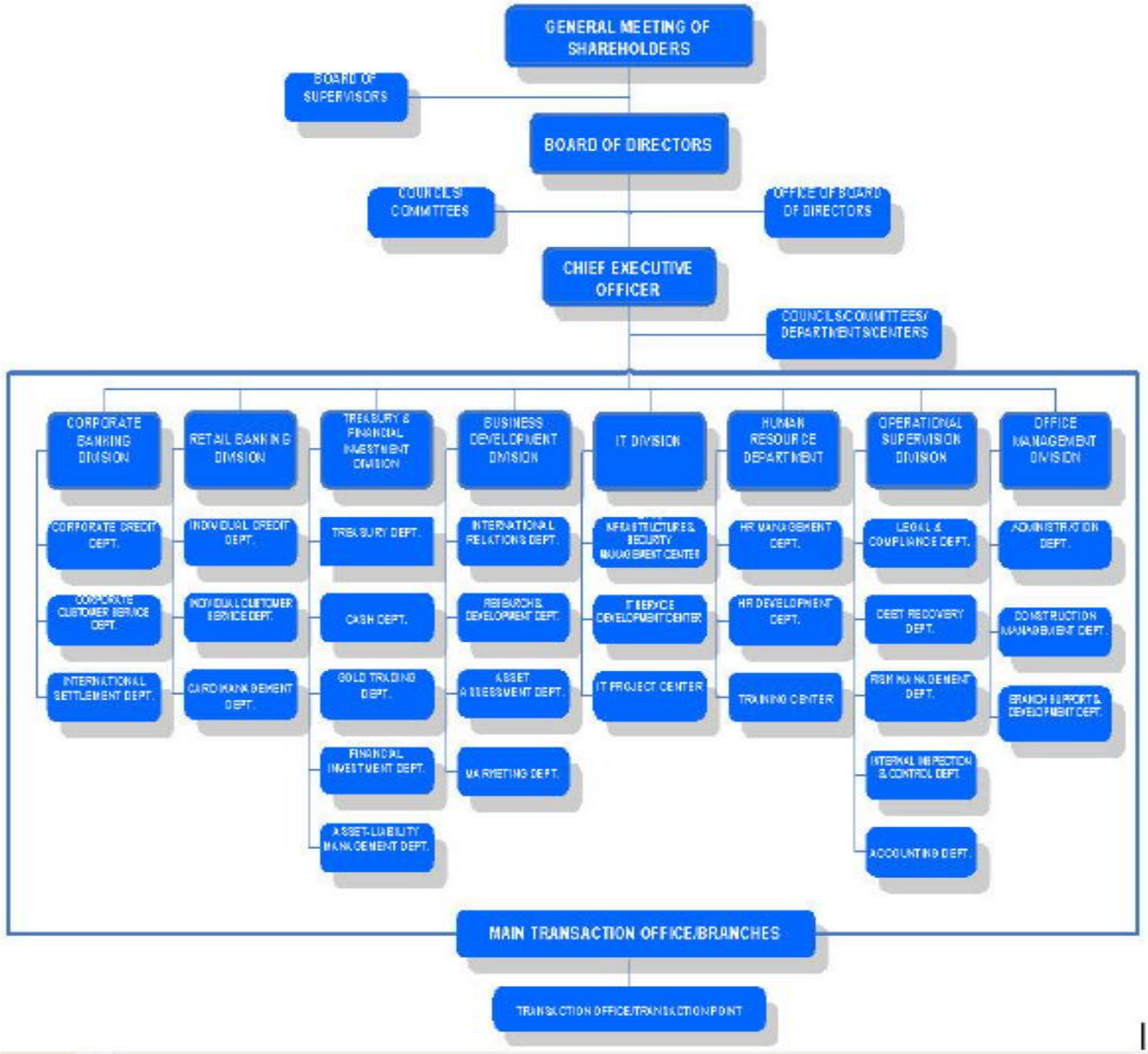
Internationalization: Joint partner of Sumitomo Mitsui Bank Corporation (SMBC), cooperation with more than 700 bank and financial organizations across 72 countries worldwide.

Awards: Certificates of excellence in international settlement quality by Wachovia Bank N.A New York, Standard Charter Bank and The Bank of New York Mellon

4.1.2 Organization structure model

According to its strategic orientation, Vietnam Eximbank is step by step implementing preparatory work for the establishment of "Eximbank' multi-functional financial group" base on the organization and governance model suitable to international practices. This group is expected to operate on the following model

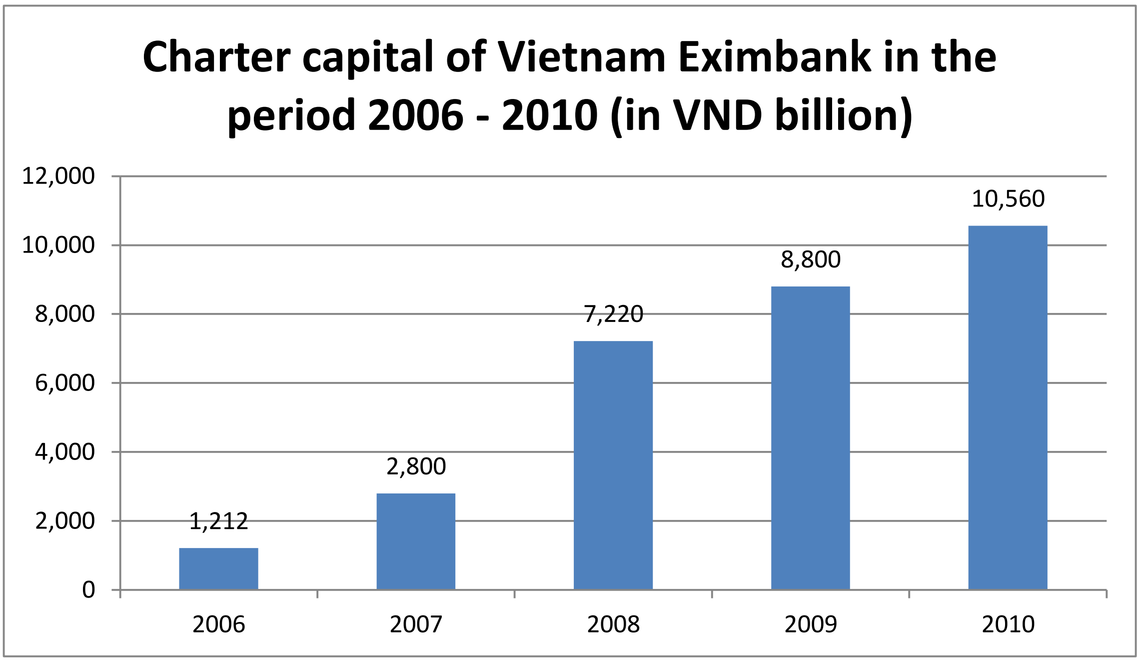
Figure 15: Organization model of Vietnam Eximbank



4.1.3 Business in review

Vietnam Export Import Commercial Joint Stock Bank (Vietnam Eximbank) is the first commercial joint stock bank in Vietnam which is established on 1989 in accordance with Decision of Chairman of the council of ministers. After twenty years of operation and development, the current charter capital of Eximbank is VND 10,560 billion, equivalent to US$ 520 million. Total asset is VND 131,111 billion, equivalent to US$ 6.5 billion. The turnover in 2010 is VND 5,582 billion, equivalent to US$ 278 million, increase 55% with previous year; and profit before tax earn VND 2,378 billion, equivalent to US$ 115 million, increase 62% with 2009. In 2010, Vietnam Eximbank has return on equity (ROE) at 13.5% and return on asset (ROA) at 1.85%

Figure 16: Charter capital of Vietnam Eximbank



Source: Vietnam Eximbank annual report, 2010

At present, Vietnam Eximbank has a nationwide network with its head quarter in Ho Chi Minh City, 1 main transaction office, 52 branches and 108 transaction offices, and has 3,927 employees. From the international aspect, Vietnam Eximbank has so far established correspondent banking relationship with more than 720 banks and branches in 65 countries around the world.

4.2 Financial risks of Vietnam Eximbank

With reference to the world financial crisis in 2008 and the slowdown of national economic in 2010, Vietnamese financial market has to face many negative impacts in 2011. The changes of interest rate, exchange rate and gold price in both local and international markets affects to the business activities of whole banking system seriously in general and Vietnam Eximbank in particular. In addition, with the change of SBV financial policies for resolving the inflation issue, Vietnam Eximbank also need to adjust the business plan in 2011. Therefore, there are four financial risks that Vietnam Eximbank has to solve as following:

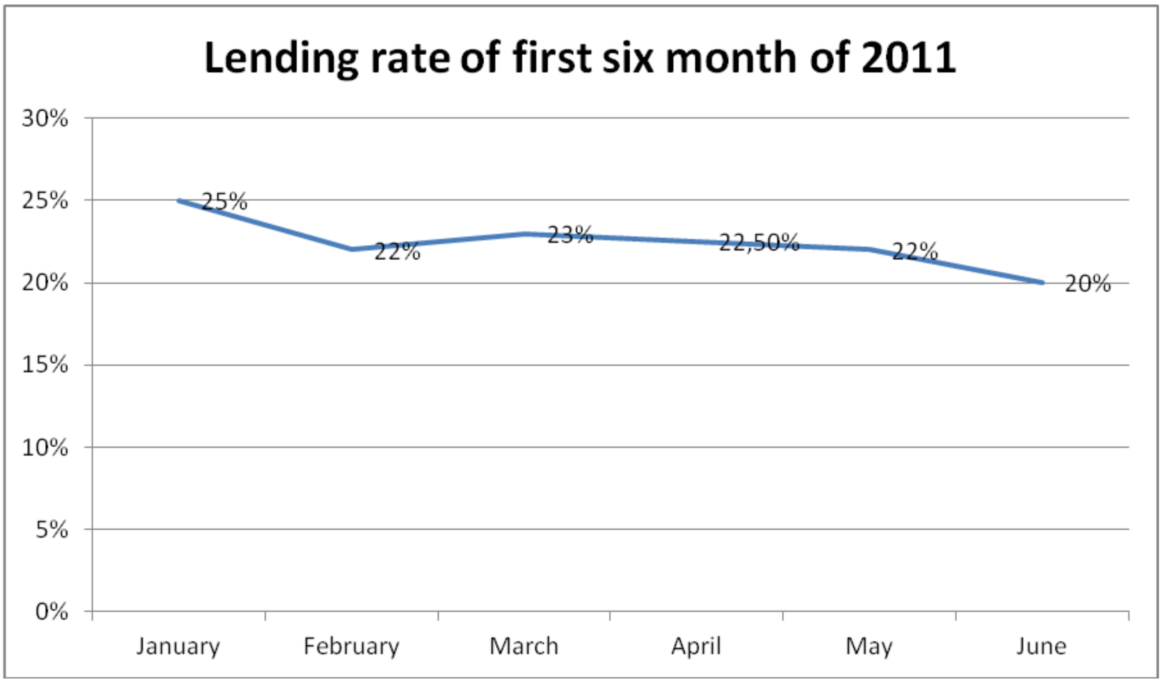
4.2.1 Interest rate risk

Interest risk arises when there is a difference in the re-pricing term of a bank's assets and liabilities due to fluctuation of interest rate in the market, causing direct effects on the bank's income. In recent years, Vietnam economy faces the inflation issue seriously due to the world financial crisis in 2008. The average inflation rate is always around 18% in the last three years. Therefore, it leads the banking interest rising very high in order to reduce the negative impacts of inflation. In 2010, Vietnam Eximbank offers the interest rate of saving account at 14% per year, and 18% per year for loan. It is one of the most attractive offers since State Bank of Vietnam (SBV) issue the maximum interest rate at 14% for whole banking system. However, there are two serious problems that is affecting to its business activities includes

Firstly, the nominal maximum saving interest rate is 14% per year due to the regulation of SBV. However, there are some small banks which lack the cash have offered the "extra interest bonus" of 3 % and/or 4% for attracting the cash flows. This leads the money withdrawal issue from one bank to another bank in order to have the higher interest rate, especially with personal accounts. It is estimated that Vietnam Eximbank has been lost VND 405 billion of saving account, equivalent to 0.7% of total mobilized fund in 2010. This not only affects to the liquidity of Vietnam Eximbank but also lack the essential fund of loan for corporate clients. In this case, if Vietnam Eximbank increases the saving interest rate will also lead the higher lending rate even though it is 18%.

Secondly, according to Mr Vu Khac Hai, Director of Vietnam Eximbank – Hanoi branch, personal customers always asks for the high saving interest for reducing inflation issue of economy. Vietnam Eximbank has to offer the maximum saving interest rate at 14% per year. Therefore, the lending rate must be 18% in order to assure the profitable business. However, it is still a very high ratio, especially with corporate clients. It is difficult for enterprises to earn the profit higher than the lending rate when the world economic is still in the recession time and exports accounts nearly 60% of GDP. In addition, both inflation and high lending rate also limit the spending power and individual consumption loan. In spite of the fact that Vietnam Eximbank business earns the 55% growth rate in 2010, it is hard to remain its result in 2011. It is estimated that total credit growth rate is 10% only in the first quarter of 2011 and may be lower in the rest of year.

Figure 17: Vietnam Eximbank's lending rate in 2011



Source: Vietnam Eximbank business report, 2011

In order to limit this kind of risk, Vietnam Eximbank should pay much attention to regulate interest rate actively and flexibility by applying different lending interest rate or mobilizing interest for each type of product and service for each period, narrowing the difference between the average term of assets and liabilities on the basis of ensuring the highest efficiency. In particular, for mid and long term loans which are often exposed to the interest rate risk, Eximbank can apply the floating interest rate policy based on market interest rate from time to time, thus minimizing the interest rate risk. Moreover, the operations of the Assets – Liabilities Management Committee (ALCO) in the interactive relation with other functional department in the risk management model aiming at approaching international practices also increase the efficiency of interest rate risk management of Vietnam Eximbank

4.2.2 Credit risk

Credit risk is the risk which leads to asset losses in case the borrower fails to execute part of or all of the commitments made in the Credit Agreement with the Bank. This risk also includes payment risk when a third party (guarantor) fails to execute its obligation to the Bank. In 2010, Vietnam Eximbank gain total credit of VND 62,346 billion, increase 62% with 2009. It is the impressive credit growth within the recession period. However, there are still the negative impacts and affect to its business activities. The overdue debt is VND 1,361 billion, equivalent to 6.09% of total debt, increase 2.2% with previous year.

According to Decision Number 18 of State Bank of Vietnam which is applied to whole domestic banking system, loan and advances to customers are classified into five groups based on the payment status and other qualitative factors as follows:

Group 1: Current

- Undue debts which, according to the Bank's assessment, could be fully recovered, both principal and interest when they fall due;
- Debts which are overdue less than 10 days and according to the Bank's assessment, could be fully recovered, both principal and interest and both overdue principal and interest in accordance with the remaining payment schedule.

Group 2: Special mentioned

- Debts which are overdue from 10 days to 90 days;
- First time rescheduled debts which, according to Bank's assessment, could be fully recovered, both principal and interest, within the rescheduled payment term.

Group 3: Sub – standard

- Debts which are overdue from 91 days to 180 days;
- First time rescheduled debts, except for debts which are classified in Group 2;
- Debts of which interest was waived or reduced because customer was not able to fully repay interest in accordance with the payment schedule.

Group 4: Doubtful

- Debts which are overdue from 182 days to 360 days;

- First time rescheduled debts which are overdue for less than 90 days within the rescheduled payment term;
- Second time rescheduled debts.

Group 5: Bad

- Debts which are overdue for more than 360 days;
- First time rescheduled debts which are overdue for less than 90 days within the rescheduled payment term;
- Second time rescheduled debts which are overdue within the second time rescheduled payment term;
- Debts which are rescheduled for three times or more;
- Frozen debts and debts are waiting for resolution.

With reference to this regulation, Vietnam Eximbank meets some financial risks in 2010. Total credit growth for corporation has been reduced from 69.1% (2009) to 65.45% because of the high lending interest rate. In addition, the negative loans also rise in comparison with the previous year, especially in group 3 when it increases nearly 580%. Both of the economic recession and high lending interest rate issues lead to the repayment risk seriously since the corporate profitable drop much, or even lower than lending interest rate. It is an urgent situation in spite of the fact that the bad loans occupy 1.9% of total credit only.

Loan classification billion)	2009	2010 (in VND
G1: Current	61, 219	37,446
G2: Special mentioned	240	231
G3: Sub standard	295	54
G4: Doubtful	162	174
G5: Bad	427	474

To manage risk in the credit activities, Vietnam Eximbank should implement the following measures:

- Dispersing risk by industry: instead of focusing funds on one or several industries, allocating funds to a variety of industries from manufacturing to trade, services and personal consumption.

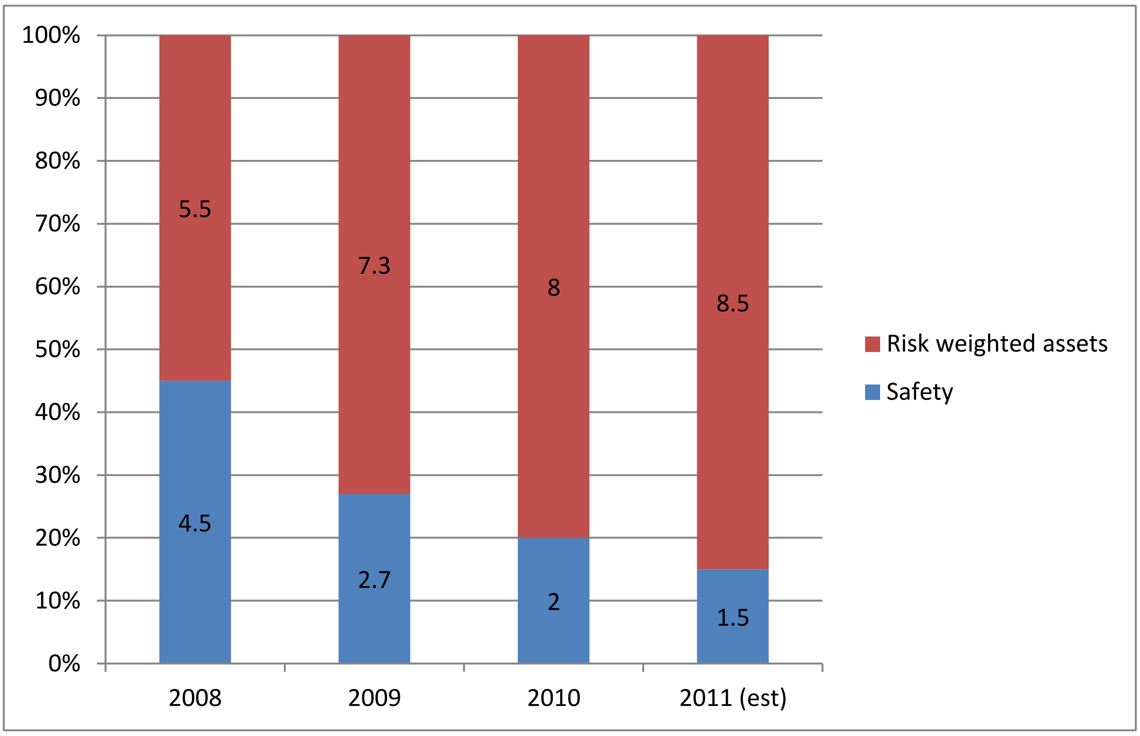
- Setting specific limits for each branch and issuing a full set of regulations guiding details of the process of credit offering and post lending management.

- Taking the initiative in establishing risk provision in accordance with law stipulations to ensure safety of the credit activities of the bank; regularly conducting inspection activities before, during and after lending.

4.2.3 Bad debt and capital adequacy ratio (CAR)

Accompany with the high growth rate of GDP, real estate market increase 240% in Hanoi and 180% in Ho Chi Minh cities from 2006 to 2008. The housing price rises so fast that are always warned as the bubble market. Like Mr Vu Khac Hai said, “people ask for the loans and then reinvest to real estate market”, the result is total credit for real estate market increase so much throughout Vietnamese banking system. Vietnam Eximbank’s capital rise from VND 1,212 billion to VND 10,560 billion from 2006 to 2010 due to the successful business but it also supply a large share loans and investment to real estate market. However, the financial risk finally occurs when housing price fall down in the last two years. In 2010, the supplemented credit for real estate of Vietnam Eximbank is VND 4,000 billion, equivalent to 18.2% of total credit, and the bad debt is VND 200 billion. This issue will be more seriously since the price of real estate market decrease nearly 30% from 2009 to present. It is believed that the housing price continuously decrease in the next two years because of the unstable economic environment. Therefore, the bad debt of real estate will not only affect much to Vietnam Eximbank business but also increase the credit risks.

Figure 18: CAR of Vietnam Eximbank



Source: Vietnam Eximbank business report, 2011

In spite of fact that Vietnam Eximbank' capital increase nearly 1000% from2006 to 2010, the ratio of capital to its risk has been reducing much in the same period. According to Vietnam Eximbanh Annual Report in 2010, capital adequacy ratio (CAR) is decreased to 20% with 32% in 2009. It is estimated that this CAR would decrease to 15% in 2011 when the macroeconomic environment has not been improved much. However, it is still the safety ratio in comparison with the compulsory CAR of State Bank of Vietnam of 10% in accordance with Basel Accords. Hence, with reference to the concern of bubble real estate market and domestic business recession, the bad debt will continuously decrease its CAR. In addition, Vietnam is the vulnerable financial market when personal customers tend to have the bank run in case of occurring the bad rumour. That is why Vietnam Eximbanks always keep CAR at 15% and higher despite it means the lower development of business.

For solving this kind of risk, Vietnam Eximbank should apply the regulation of State Bank of Vietnam which requires local banks reducing the credit for real estate and construction sector to 20% in the July and 16% in December of 2011. Those are the main factors to increase the inflation issue and create the bubble real estate market in Vietnam. Therefore, it will bring two positive impacts to national economic in general and Vietnam Eximbank in particular.

Firstly, the lower inflation leads the reduction of interest rate and the corporate clients can apply the essential loans for developing business. The high lending rate is restricting the business of enterprises and causes the possible bankruptcy issue, especially in the long term slowdown of economy.

Secondly, it able to limit the possible burst of bubble real estate market since its price rise so fast and unable to control efficiency. Credit for real estates occupies the huge amount in total credit of Vietnam Eximbank and the market collapse maybe lead to bankruptcy for both bank and companies.

4.2.4 Foreign exchange risk (FX risk)

In theory, foreign exchange (FX) rate risk incurs when there are differences in the term or the type of currency of those foreign exchange position held, which may lead to the Bank's losses in case the exchange rate fluctuates. The FX operations of Vietnam Eximbank mainly serve the needs of international settlement of corporate customers and of foreign currency trading on the international market. However, due to the inflation issue and the unstable of international currency and gold markets, there are two risks that Vietnam Eximbank must deal in 2010.

- Vietnam Eximbank is one of largest banks in serving the foreign currencies to local enterprises which operates in international trading sector. It is estimated that total export and import activities though Vietnam Eximbank services worth US$ 5.1 billion in 2010, increase 31% with 2009. However, Vietnam Eximbank meets the lack of foreign currencies seriously in 2010. Unlike Western countries, all business and personal transactions are processed through banking system. Vietnamese people still have the habit of cash culture. The high inflation brings the fear to the loss of VND value. In addition, there are more than ten small banks announce the loss in 2009. These encourage Vietnamese people buying and reserving US Dollars at home in order to keep the assets safety. Total foreign currency mobilization in Vietnam Eximbank decrease 9% in 2010. This affects to international business activities much since Vietnam Eximbank unable to supply the essential credits for its regular import clients. Therefore, Vietnam Eximbank must borrow nearly US$ 100 million with high lending rate from the other financial organizations, increase 300% with 2009. Consequently, the bank must offer the higher lending rate to the customers. It is the burden to regular clients in the time of economic recession and they have no choice but decreasing the business activities. Moreover, according to Mr Vu Khac Hai, Vietnam Eximbank must sell a part of its foreign currencies to State Bank for solving the lack of foreign reserves. This absolutely affects to FX business of the bank in 2010 much. The foreign reserves of Vietnam are reducing much because of the trade deficit. It causes the lack of foreign currencies to whole banking system. Based on Vietnam financial market environment at present, it is forecasted that the lack of foreign currencies will remain in the next two years at least and also reduce this business activities of Vietnam Eximbank about 6% in 2011 and 5% in 2012.

- Gold and foreign currency trading are the important business of the bank. In 2010, due to the world financial crisis, gold price rise from US$ 900 to US$ 1200, increase 33% with 2009. On the other hand, the value of US Dollar loses nearly 13% in 2010 when American state would like to reduce the current account deficit (CAD) and encourage the exports. These are the unexpected changes and Vietnam Eximbank hardly forecast the market trend. Total profit of foreign currency and gold trading is US$ 800,000 in 2010 only, decrease 850% with the previous year. It is the urgent figure and Vietnam Eximbank absolutely maybe faces a huge loss in 2011 if there is no right adjustment. In addition, it also reduces the foreign currencies capacity of the bank in spite of the fact that the lack of foreign currencies has occurred in 2010.

Figure 19: World gold price in 2011

Source: KITCO, Aug 2010

In order too minimize FX risk, Vietnam Eximbank should comply with safety measures as follow:

- FX risk management focus on managing the net FX position and gold trading position (not positive or negative more than 30% of the equity capital of the Bank only), and complying with prevailing regulations of the State Bank.

- Always maintaining a proportionate rate between assets and liabilities in foreign currencies and an appropriate net FX position

- Providing training to staff with high professional knowledge who are able to analyze and forecast the fluctuations of exchange rates of currencies and make decision whether to buy or sell currency contracts.

- Using more financial tools which can prevent FX risk such as forward, future, swap or option contract in FX trading.

5 CONCLUSION

Vietnam is an attractive economy which has the variety natural resources. With reference to the centre strategic location of Indochina region, it is the entry for all corporations penetrating the market of five hundred million people of ASEAN free trade area (AFTA) in particular and of the Asia Pacific Economic Cooperation (APEC) markets in general. In addition, with half of the population under the age of 30, well educated labour and low wage costs, Vietnam has rapidly become a remarkable growth economy in the last decade. This is due to the open economic policy of the state in 1990 and increasingly harmonizing in the global economy.

Despite the negative impacts of the world economic recession, Vietnam still achieves an average GDP growth rate of 6%, behind China only. The FDI flows are increasingly invested into the key industry and service sectors. It presents a reliable economy which is highly appreciated by foreign investors. However, it is too early to say whether Vietnam is becoming another Asian tiger such as China, Thailand, Singapore, etc. There are many obstacles that Vietnam has to improve in order to achieve the sustainable development. The weak infrastructure, bureaucratic legal system, low technology level and vulnerable market are all serious issues that Vietnam needs to solve in the long term future.

Running a business in Vietnam requires corporation recognizing the potential risks involved in its economic environment. Vietnam changed to a market economy more than twenty years only. The communist not only succeeds in keeping the stable business environment but also limits its development ability since the economic activities are often controlled under political targets. It is different with the market oriented economy in the West. In addition, like all emerging markets, Vietnam must deals with the hidden risks from the high growth rate target. One example of risk is the financial sector. This is the cornerstone of a national economy but it is also the main weakness of Vietnam. All key financial organizations are state owned enterprises. The private and foreign banks have not occupied an important role in the domestic market because of the limit of capital when Vietnam has not opened financial market completely. It is the reason why the financial organizations have not met the demand of business development yet. Meanwhile, they are also the factors causing serious inflation when modern financial risk management is not applied in the state owned banks effective. Therefore, Vietnamese financial market is still vulnerable and must be improve its infrastructure to cope with the demands of business in particular and sustainable development in general.

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Appendix

Interviewee: Mr Vu Khac Hai, Director of Hanoi Branch, Vietnam Eximbank

1. In your opinion, what factor would bring the negative impacts to Vietnam Eximbank business at present?

   Inflation, Vietnam has the average inflation rate around 18% in the last three years and this is causing the devaluation of VND much. Our bad debts are increased faster since there are many bankruptcy companies recently.

2. Why does Vietnam Eximbank offer the so high interest rate to both of personal customer and local enterprises?

   In Vietnam, personal customers requires the saving interest rate must equal or nearly equal to inflation rate as the insurance. If not, they will withdraw money for buying gold or US Dollars. In this case, the inflation rate would be higher seriously. This issue pushes the lending interest rate so high.

3. How can Vietnam Eximbank reduce the credit risks?

   Actually, there are many clients facing the bankruptcy issues because of the 20% lending interest rate. So that, we need to reduce the saving interest rate first. However, it requires the action of State Bank of Vietnam (SBV) as the leader of banking system. If all the banks apply the low saving interest rate, the lending rate will drop. This will benefit to both of banks and clients. That is why Eximbank and ten other banks propose SBV to give the new official credit standard which focus on reducing the average interest rate to 12% as soon as possible. In addition, I think government also needs to encourage people sharing the difficult of nation economy through public information channels. If they believe in economic policies and value of VND, they will accept the lower saving interest rate.

4. What about real estate? Is this one of the key factors to cause the higher bad debts in Vietnam Eximbank?

   Right, Vietnamese real estate market rises so fast that the bubble issue happen clearly. How can the housing price in Hanoi and Ho Chi Minh equal to New York and London? It is quite crazy with the poor country like Vietnam. All big companies like doing real estate projects because of the incredible profit. People ask for the loans and then reinvest to real estate market. This happens in the long time and pushes the housing price so high with its real value. Like other banks, Vietnam Eximbank also meets this kind of credit risk. In spite of the fact that it is not seriously yet but we must control and reduce the possible bad debts of real estate before it become dangerous.

5. What cause Vietnam Eximbank lack foreign reserves in spite of the fact that it is the key strength previously?

   Almost corporate clients of Vietnam Eximbank are doing export and import business. That is why we are rich of foreign reserves previously. However, the trade deficit of Vietnam is going on and become seriously. Vietnam Eximbank must sell the huge amount of foreign currencies to SBV. Meanwhile, the unstable economy and devaluation of VND encourage personal customers buying and keeping their foreign currencies at home, not in the bank. Truly, it affect to our international business in 2010.

6. What do you think about the credit business of Vietnam Eximbank in next year?

   In spite of the fact that SBV require all the banks reduce the interest rate to 14% as maximum but it is still the high ratio with local enterprises. In short term, Vietnam Eximbank impossible offer the low lending rate immediately. This will reduce the growth rate of credit. However, I think it do not bring the negative impact to our business much.