CAPITAL MARKET ISSUES

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Introduction:

Capital Market History:
The highly attractive macro story of Vietnam (Population, median age, literacy etc) have been a magnet for Emerging Markets funds seeking the new "Asian Dragon".

<u>1990s</u> Several funds were raised despite there being no stock market!!! The investments ended up in property or private equity and with the advent of the Asian crisis were liquidated mostly at barely break even if not losses.

<u>2000s</u> The second phase began with the opening of the HCM Stock Exchange in July of 2000 with just 2 listings. Subsequently more listings were added and the first equitisations occurred. This led to the boom in 2007 with the Index reaching a peak of 1170. Thereafter due to poor macro economic policies, the market plunged to a low of 234 in February 2009 and since then after a strong rally in late 2009 it has traded in a range of 420 to 520 into mid 2011.

<u>2011+</u> Late in the year into early 2012 it plunged to 330 and then rallied recently to 490 to correct to 434. Not only does this volatility reflect a lack of investor confidence and institutional support but the current level remains the lowest from the previous in Asian market except for Japan. Besides Taiwan and Thailand (which were driven by excessive speculative bubbles) all Asian markets have surpassed their previous highs.

STOCK MARKET

Opening Accounts

The current system is cumbersome and does not attract foreigners as it takes almost 6 months to open an account whereas in most other jurisdictions it only takes a week. The requirement to obtain judicial status and a non criminal record from the country of origin of the account holder proves to be time consuming and costly. This should be replaced by the simple requirement of a notarized valid passport. This would attract many more foreign investors and most importantly capital into the stock market.

Liquidity

Despite extending the trading hours liquidity still continues to be an issue due to the % trading bans which restrict the natural movement of prices. Admittedly these % are there to protect investors from sharp falls but they encumber the natural workings of the market. A suggestion would be to impose a 30 minutes halt in the trading of a security when a move up or down of more than 10% occurs. Such a pause should bring stability.

Foreign Ownership

A genuine open market should have no restrictions. However it is appreciated that certain entities of such national importance need to remain in control by local interests most notably government owned companies. A way around this would be to create a class of share with no voting rights exclusively for foreigners. This would enable companies to attract foreign capital. The bank foreign ownership limit should be raised to 49%, this would be a more realistic number.

Offshore Listing
As mentioned previously offshore listings detract from the development of the local stock market. To build a viable market both for institutional and retail investors with breadth, depth and liquidity it is essential that the capital is raised locally. (Argentina example). Furthermore with overseas listings the company becomes a foreign entity in the offshore market of its listing and generates little liquidity. HAGL example in London, hardly any trading.

BOND MARKET

Government Issues
A proper functioning bond market with defined maturities (3, 6 and 12 months, 3, 5 and 10 years). There should be a clear calendar for the auctions. There should be a few designated government authorized dealers dealing amongst themselves and not on an Exchange; this would encourage a more orderly and liquid market. To attract foreign investors the 10bps transaction tax MUST be abolished. It is senseless and generates no revenues, on the contrary foreign investors would bring much needed funds to the government.

Corporate Issues
There should be a focus to develop a corporate bond market, with fixed coupon issues, zero coupon issues and convertible issues. Such vehicles would suit local insurance companies and foreign fixed income funds.

EQUITISATION

SOE Reform
This is the most critical area for the successful development of the Capital Markets. Privatisations of State Owned Enterprises is not only key to capital markets but also to enhancing the efficiency of the economy. There has been a great deal of noise and talk but little achieved since a good start in 2007. At the VBF meeting a year ago Dominic Scriven the usual Head of the Capital Market Working Group, and for whom I am standing in today, stated that to speed up the process "a new roadmap with clear criteria and a detailed timetable" needs to be established. Why has nothing specific been published since then ?

Equitisation is the backbone of sound economic policy and one only has to see what has been achieved in other Emerging Markets. The 2 principle industries that get privatized initially are Telecom and Banking. (2 banks have already been privatized and unsuccessfully due to mispricing). The key to a successful offering is VALUATION and the only way to achieve this is to hire independent advisers (reputed investment bankers) who can price and place out the issue in line with global industry standards. There is always the fear of selling State assets too cheaply and getting blamed but these are the risks involved in the process and ironically the most successful privatisations have been those where the stake holder has left a bit of money on the table to attract investors. Overpricing issues usually leads to failure and furthermore a substantial % should be sold to create a liquid after market, not single digit %s.

Equitisation should become the lynchpin of the Capital Market Group with the Government identifying 2 to 3 candidates to be privatised within the next 9 to 12 months. The process can no longer be a discussion point it must become an action point.

Furthermore SOEs should focus on their core lines of business and expertise and not diversify into unrelated sectors, which will only distract them from operating effectively and runs the risk of causing egregious losses. Proper discipline and consistency in planning are prerequisites to run, develop and privatize the SOEs successfully.

SAVINGS CULTURE

Pension Funds

Pension schemes are another integral part of capital markets and form an essential part of social welfare by attempting to provide some form of income stream on retirement. The current system in Vietnam is a "Defined Benefit Scheme" guaranteed by the Vietnam Social Insurance Fund (SIF). This will become a bigger burden on the Government finances over the long term. It is an opportune time for the Government to consider establishing a "Defined Contribution Scheme". Such a scheme is funded by the employer and the employee and managed by investment professionals. There is no burden to the Government.

Vietnam is at a critical level in its demographic profile as its age dependency ratio is declining due to a lower birth rate, thus family support for elderly people is being reduced. Thus it is not only timely but essential for the Government to implement a "Defined Contribution Scheme" as it is highly likely that with current trends of savings (20%) the SIF could be bankrupt around 2037.

Mutual Funds

These would be the instruments used by private investment schemes. Therefore it is essential to develop a mutual fund industry of both closed and open ended funds.

Criteria for the ideal Pension System (Courtesy Stirling Finance HK)

- Integrated long term approach to ensure adequate retirement income
- Recognises changing employment structure, family patterns and personal interest
- Maximises coverage and participation
- Leads to savings culture by individuals
- Increase national savings and economic growth
- Has widespread support from community and policy makers
- Has effective regulatory structure
- Is simple to understand

CONCLUSION

As I have mentioned previously Vietnam has all the ingredients to be one of the most exciting and successful Emerging Markets. Indeed investors are looking for the new Eldorado. However there are some serious fundamental decisions that have to me made on the following fronts.

- SOE reform and Equitisation
- Consolidation of the brokers, 106 is just too many
- Improved corporate governance as to the release of news and trading
- Facilitation of account opening

It is now time to go beyond discussion and act. Unless concrete steps are taken Vietnam runs the risk of being left behind.