

Commercial Banks Restructuring: Experiences of East Asian countries

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*presented at the international workshop on
Commercial Banks Restructuring*

Hanoi, 21 December 2011

Outline

- 1. Commercial Bank Restructuring: Some basic issues**
- 2. Commercial Bank Restructuring: Experiences of East Asian countries**
- 3. The current situation of Vietnam's banking system**
- 4. Structure of Vietnam's banking system**
- 5. Restructuring Vietnam's banking system: Some recommendations**

1. Commercial Banks Restructuring: Some basic issues

- **What is “Commercial Bank Restructuring”?**

Measure packages for institution, finance and legal framework for saving failed banks and restoring the banking system (*Waxman et al. 1998, WB*).

- **Commercial Bank Restructuring - When?**

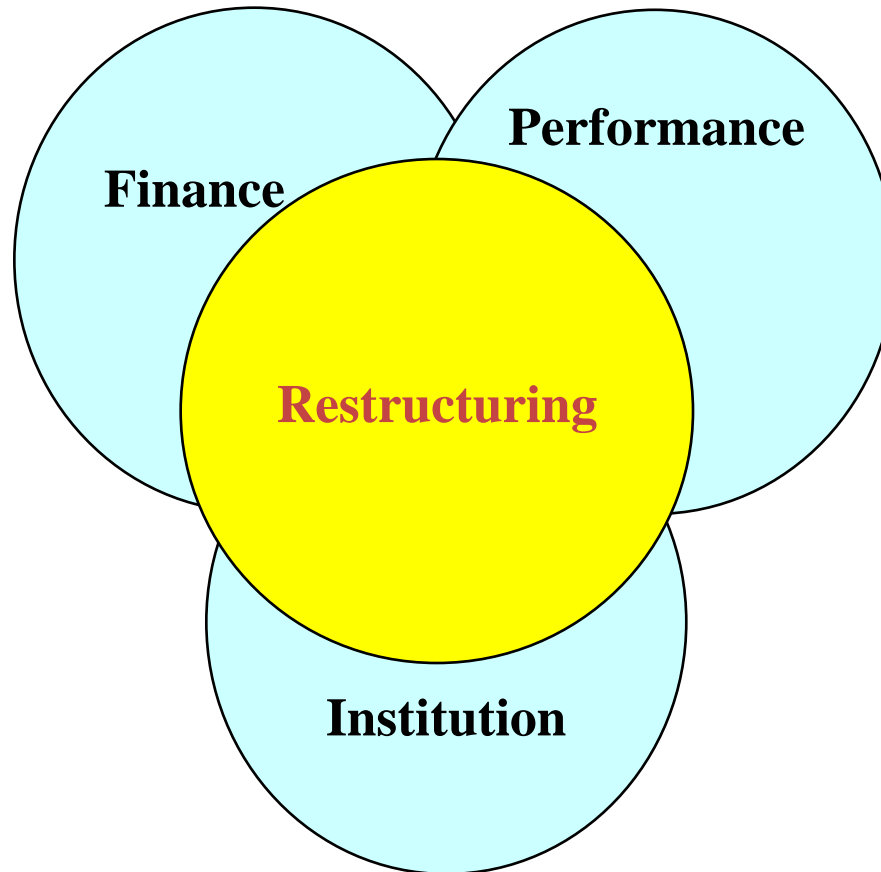
- In normal conditions, special difficulties arise (liquidity squeeze, NPLs, customer complaints,...) or

- Banks’ problems which affect 20 per cent of total deposit balance (*Lingren et al. 1999*).

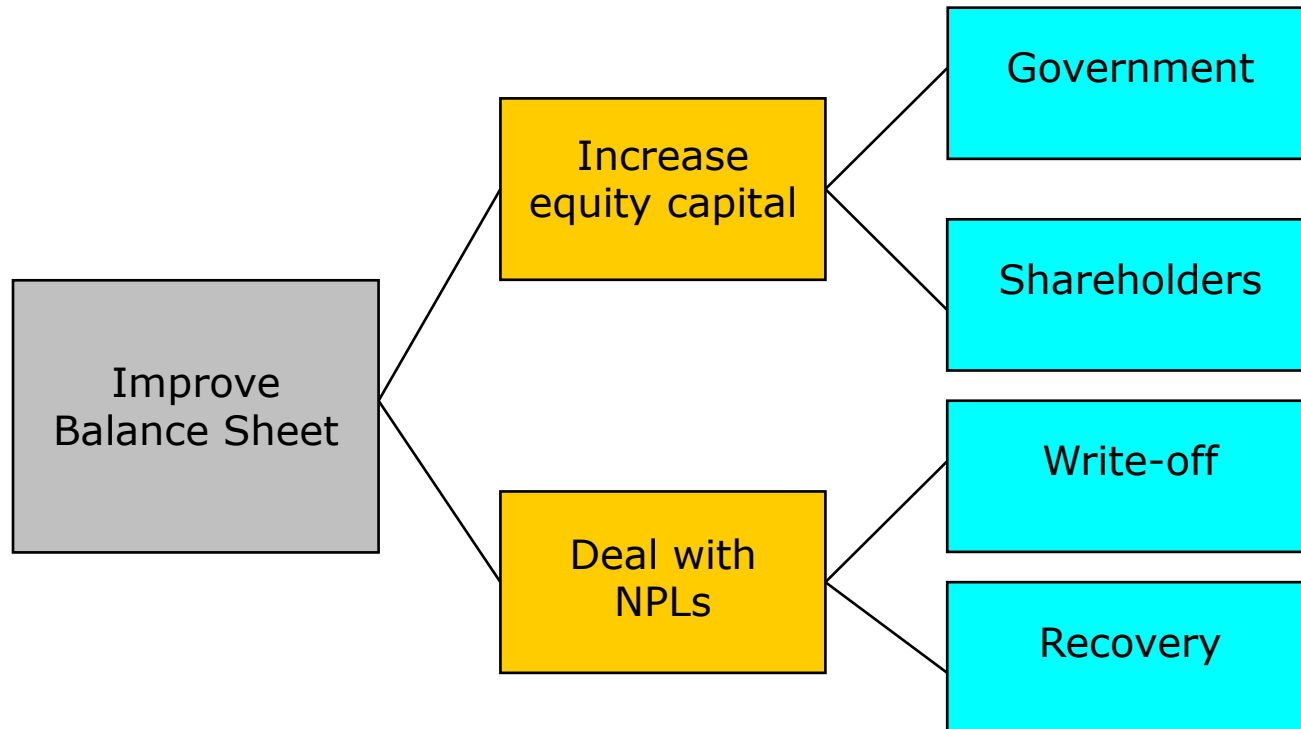
1. Commercial Bank Restructuring: some basic issues (Cont.)

- **Targets of restructuring commercial banks** (*Dziobek & Pazarbastoglu 1998, IMF*):
 - Restoring banks' liquidity and profitability
 - Strengthening banks' capacity of financial intermediaries
 - Enhancing public confidence

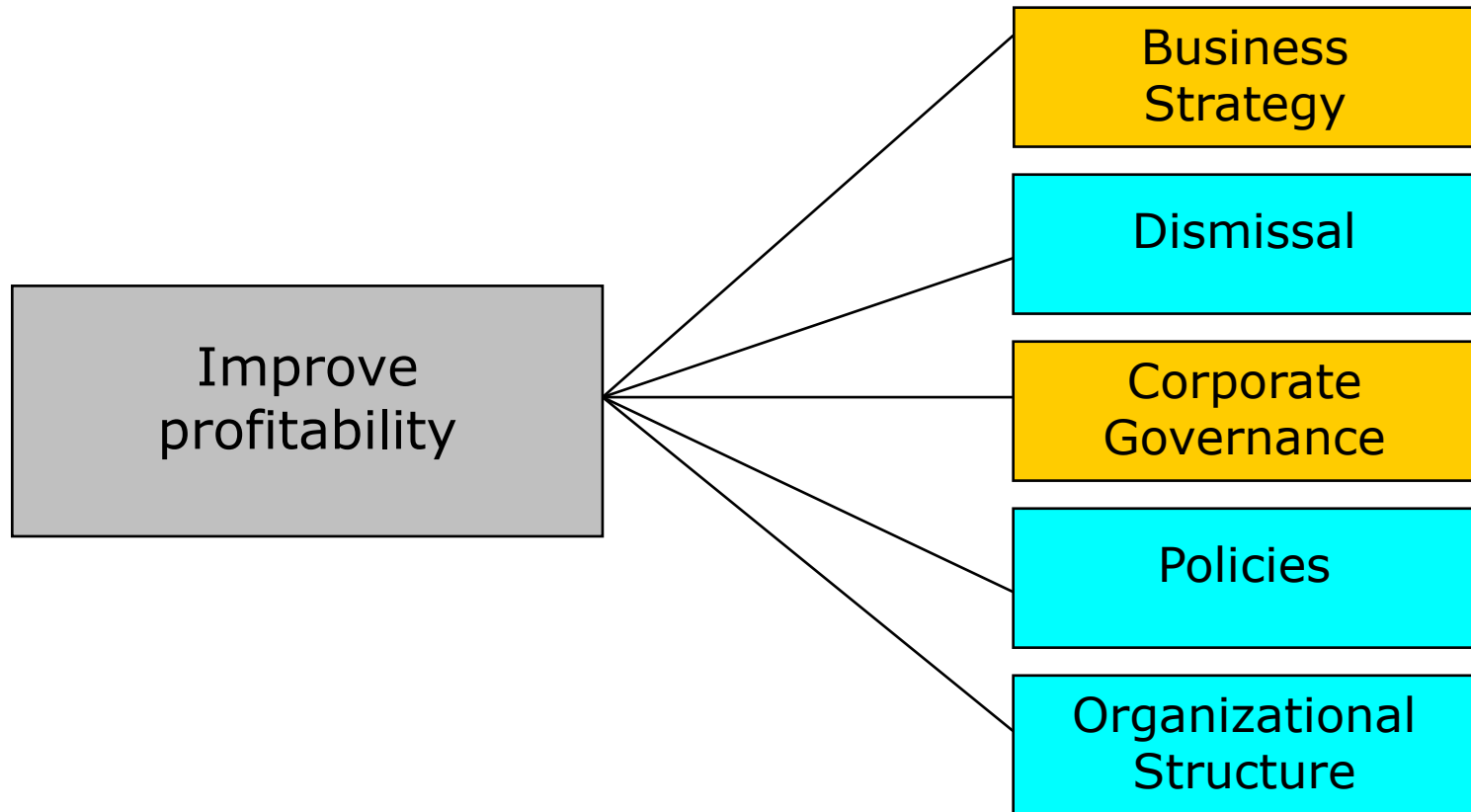
What is Restructuring?



Finance Restructuring



Performance Restructuring



Institutional capacity enhancement

Supervision	Management
<input type="checkbox"/>	<input type="checkbox"/>
<input type="checkbox"/> Model <input type="checkbox"/> Method <input type="checkbox"/> Resource	<input type="checkbox"/> Law on banking restructuring <input type="checkbox"/> Relevant regulations <input type="checkbox"/> Accounting and Auditing

- **Deposit insurance**
- **Lender-of-last-resort**

2. Commercial banks restructuring: Experiences of East Asian Countries

- **02 Research Projects:**

- Luc Can and Mohamed Ariff (2009), “**Performance of East Asian banking sectors under IMF-supported programs**”, Journal of Asia Pacific Economy, 14(1), 5-26
- Luc Can and Mohamed Ariff (2009), “**IMF Bank- Restructuring Efficiency Outcomes: Evidence from East Asia**”, Journal of Financial Services Research, 35(2), 167-187.

Context

- Financial crisis in 4 countries (Indonesia, S.Korea, Philippines and Thailand) 1997-1998
- IMF's support through 4 years (1997-2000)
- **Conditions: to implement measures as proposed and required by IMF.**
- **3 comprehensive measure packages for the financial sector.**

Policy Measures Package for Financial Sector

1. Group of measures, which stabilizes the finance-banking system:

- Liquidity Support (with conditions)
- Blanket Guarantee
- Monetary Policy tightening (interim)
- Ceiling Borrowing Rates
- Identification and closure of insolvency banks
- Loss Sharing of closed banks with creditors, Maturity Extension.

Policy Measures Package for Financial Sector (Cont.)

2. Group of measures, which **restructures** Finance-Banking Sector:

- Making review on Financial Institutions
- Making closer regulation on loan classification and risk provision
- Establishment of clear itinerary for banks to meet capital adequacy requirements (CAR)
- Intervention in insolvent banks
- Provision of guidance on methods of capital injection and NPLs purchase of banks
- Giving closer regulations on bank licensing
- Itinerary for State divestment in supported banks.

Policy Measures Package for Financial Sector (Cont.)

3. Measures group, which **renovate institution:**

- Establishment of **Financial Sector Restructuring Organization**
- Establishment of National AMC
- Improvement of independence of Central bank and Banking Supervisor
- Enhancement of supervision on banks
- Consolidation of disclosure, accounting and auditing standards
 - Issuance of regulation on risk management
 - Issuance of New Law on Bankruptcy
 - **Simultaneous Corporate Restructuring.**

Policy Measures Package for Banking Restructuring

1. Liquidity Supports to prevent failures
2. Closure of insolvent banks
3. Merging (into bank of good performance) and/ or Assumption (M&A)
4. Nationalization of private banks, eventually divestment
5. Attraction of outside capital, including foreign investors
6. Close supervision on weak banks.

Table 1: Measures and Information of Restructuring of 4 SEA Countries

Measures	Indonesia	Korea	Philippines	Thailand
Liquidity Supports (US\$ bil; % GDP)	21,7 (18%)	23,3 (5%)	0,5 (0,8%)	24 (20%)
Number of Failed banks	70/198	0	1/49	1/15
Number of other Failed FIs	0	200	25	59/91
M & A	4/7 SoCB	11/26	12/44	3 Banks & 12 FC
Nationalization of FIs	12	4	1	4
Permission of foreign investors' ownership of Controlling stocks	Yes	Yes	Yes	Yes
Closer supervision on weak FIs	Yes	Yes	Yes	Yes
Change in Bank Leadership Team	No	6/11	No	3/11
Number of Banks after Restructuring	102 (out of 198)	14 (out of 26)	41 (out of 49)	14 (out 15)

Source: Claessens et al. (1999) and Central Banks; Luc Can and M. Ariff (2009).

Research Model and Method

- 4 countries financially supported by IMF (Indonesia, South Korea, Philippines, Thailand)
- **Sampling:** 138 CBs
- **Period of 1991-2005;** divided into 3 stages: Prior to (1991-97), During (1998-2000) and Post to (2001-2005) the Period of IMF- Financially Supported.
- Comparison prior to and post to IMF-financially supported period
- **Ghosh Model (2006)** used to measure structure and efficiency of banking system and **DEA Model** used to measure efficiency of either of CBs

Table 2: Research Sample Description

	Indonesia	South Korea	Philippines	Thailand	Total
SoCBs	5	2	2	5	13
Private Banks	61	24	30	10	125
Listed Banks	24	21	21	8	74
Non-listed Banks	42	5	11	6	64
Non-restructuring Banks	21	3	17	0	41
Restructuring Banks	45	23	15	14	97
<i>Of which:</i>					
<i>Failed:</i>	29	14	8	3	54
<i>M&A</i>	4	5	6	7	22
<i>Capital Supports</i>	12	4	1	4	21
<i>divestment (Eventually)</i>	6	0	0	3	9
<i>Foreign Banks' Participation</i>	12	8	14	10	44
Total number of banks	66	26	32	14	138
Market share (%)	82	68	77	75	

Efficiency of Restructuring

Table 3: Comparison of structure between the period prior to 1996 and Post to CBs system restructuring (2005)

	Indonesia	South Korea	Philippines	Thailand
Total Assets/ GDP (%)	53 → 64	105 → 140	97 → 82	120 → 112
Number of Branchs/ 1000 people	6 → 5,2	13,8 → 13,4	7,7 → 7,2	9,6 → 9,9
Market share of total assets of 5 biggest banks (%)	71,4 → 77	49 → 65	51 → 67	71 → 78
Market share of total assets of SoCBs (%)	62 → 52	5 → 10	13 → 18	21 → 35
Market share of total assets of Banks with Foreign Participation (%)	5,2 → 22	2 → 12	4,5 → 1,2	1,3 → 5,5

Efficiency of Restructuring (Cont.)

Table 4: Comparison of activities of CBs system between the period prior to 1998-2000 and Post to Restructuring 2001-05

	Indonesia	South Korea	Philippines	Thailand
M2/GDP (%)	59 → 54	127 → 125	62 → 56	105 → 96
Bank credit/ GDP (%)	31 → 20,5	72 → 90	48 → 35	103 → 77
Cash/ Deposit (%)	9,5 → 11	5,2 → 3,5	11,2 → 10,7	8,4 → 10,5
Overdue Loans/ Total loans (%)	37 → 8,5	13 → 2,4	12,6 → 13,5	33 →
ROA (%)	-2,4 → 1,7	-2,3 → 0,75	0,6 → 1	-4 → 0,3

Efficiency of Restructuring (Cont.)

The results of research on “efficiency” of policy measures package for restructuring carried out in 138 CBs of 4 countries show that:

- Restructuring is necessary
- Closure of weak banks is a right policy in term of economic efficiency
- Banks upon M&A shall be suffering loss (less efficient) in short term
- Nationalization, eventually divestment for private investors brings better efficiency before being restructured
- Attraction of outside private capital, including foreign investors, brings better efficiency before being restructured.

Lessons learned

1. Restructuring is necessary upon financial crisis or bank in difficulties
2. Stabilizing financial system and restoring public confidence as a first strong measure
3. Emergency measures to prevent bank run from banking system while ensuring protection of depositors' interests
4. Central bank's liquidity supports needed but accounting for unwinding (divestment)
5. Establishment of legal framework and itinerary for restructuring.

Lessons learned (Cont.)

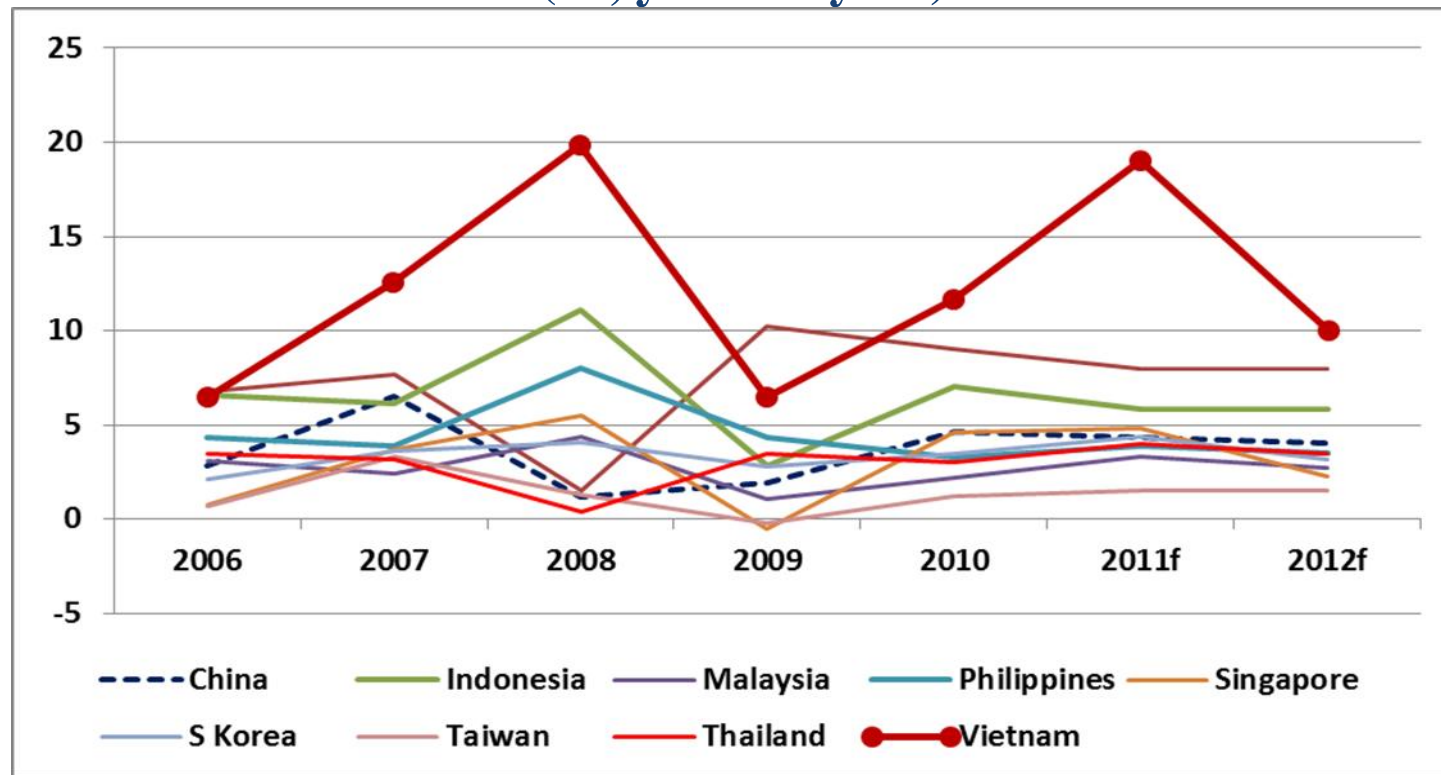
6. Specific regulation on methods and criteria of asset pricing and bank classification
7. Conditions and itinerary to meet CAR are vital
8. Development of financial solutions for restructuring costs
9. State leadership role and political decision as an indispensable factor
10. Simultaneous corporate restructuring needed.

3. Current situation of banking market in Vietnam

- Pressures (concerns) on high inflation and interest rates,
- “Volatilized” credit
- Black credit crash sends disorder, instability
- Small capital size of banks
- Less efficiency to meet international standards
- Overdue loans liquidity risks getting worse
- Inappropriate and unsustainable income structure,
- Accounting scheme of big difference in comparison with international practices
- Unsound competitiveness.

Figure 1: Inflation (CPI) of Vietnam compared to the Region

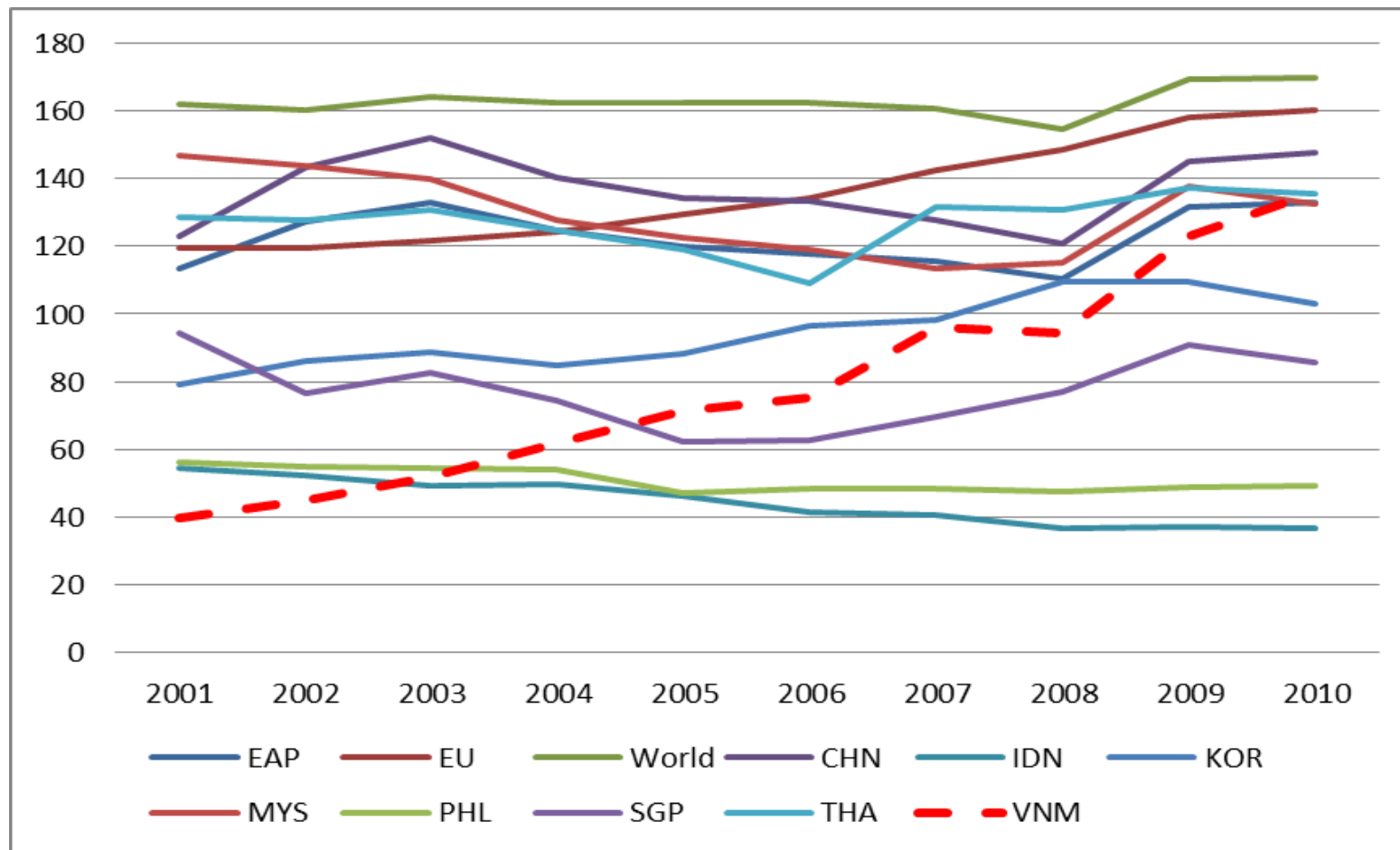
(%, year-on-year)



Source: Investment research by Citi, EIU (2011).

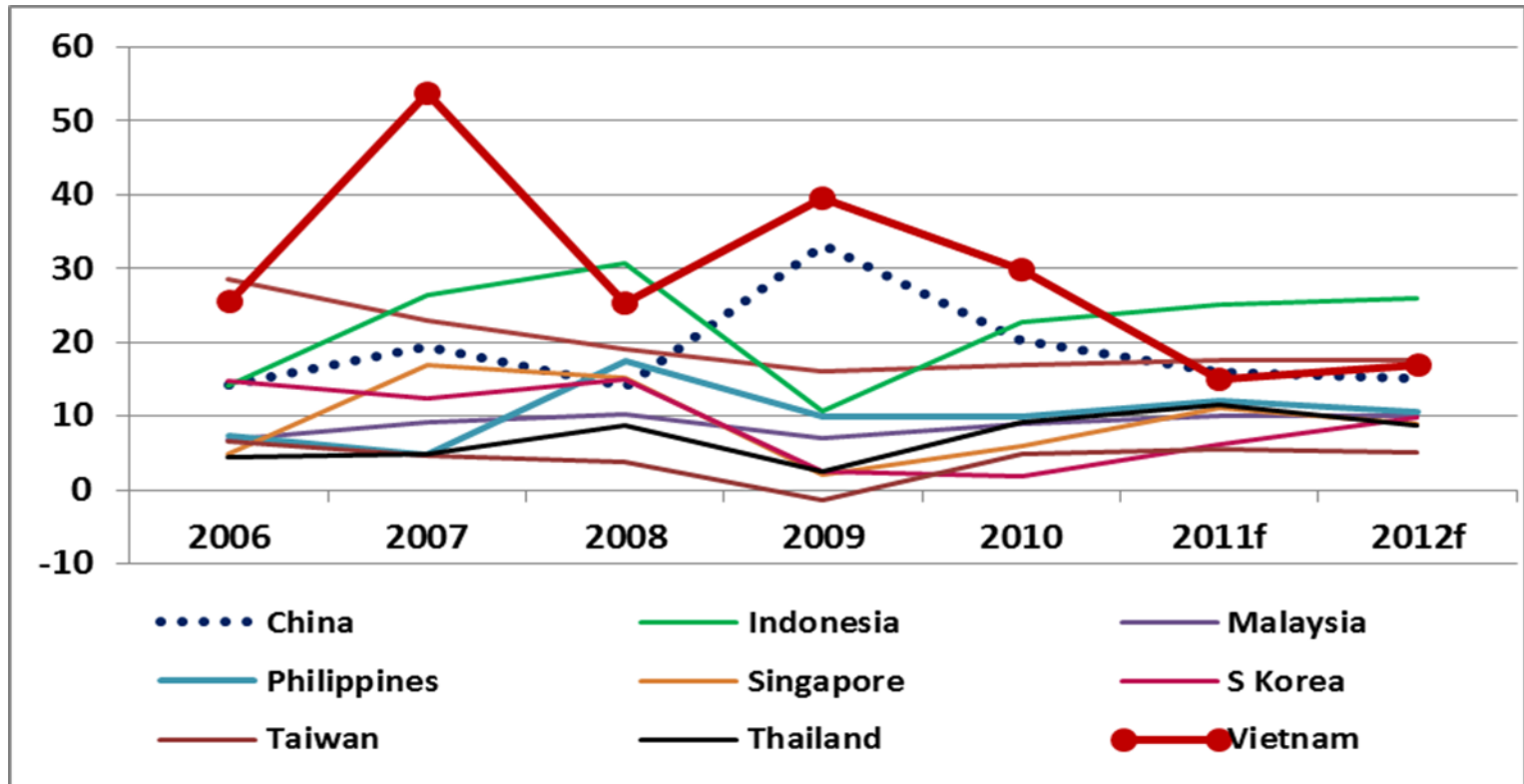
Inflation is always a great concern for Vietnam.

Figure 2: Size of credit of Vietnam and other countries (% GDP)



Source: WB Financial Sector Indicators 2011.

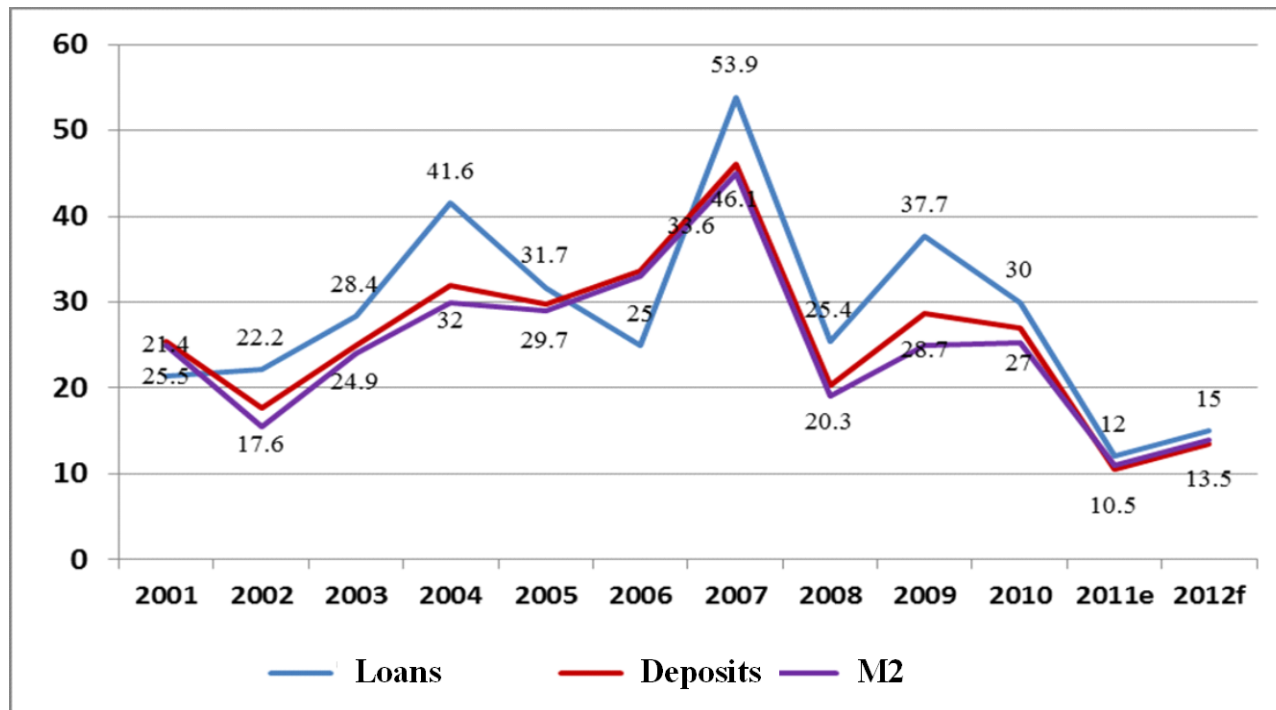
Figure 3: Credit growth of Vietnam compared to the region (% , year-on-year)



Source: Investment research by Citi, EIU (2011).

High inflation is partly due to high credit growth and “inflation import”.

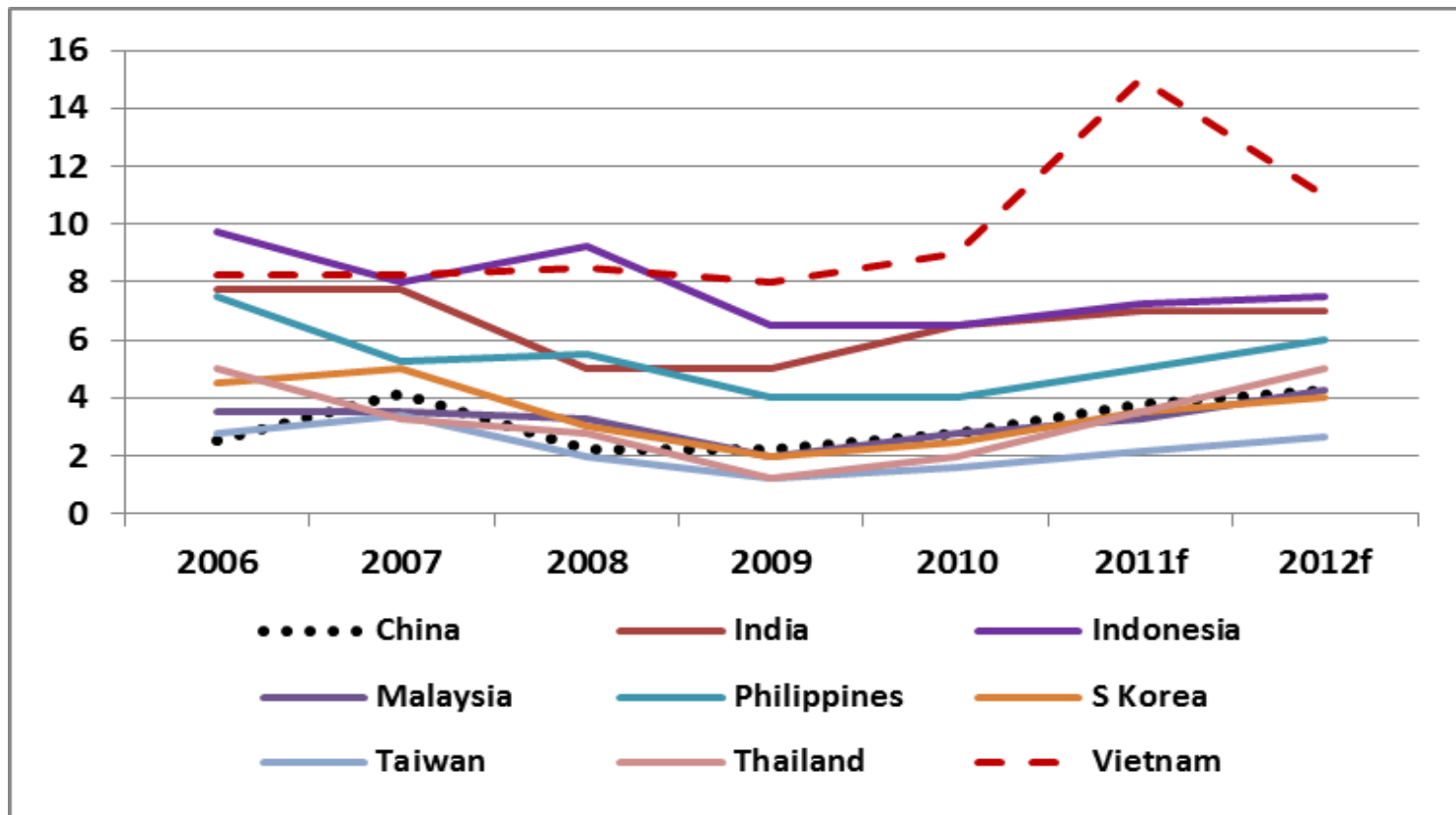
Figure 4: Credit, deposit and money supply growth of VN (% , year-on-year)



Source: State Bank of Vietnam.

For many years, credit growth is higher than deposit growth.

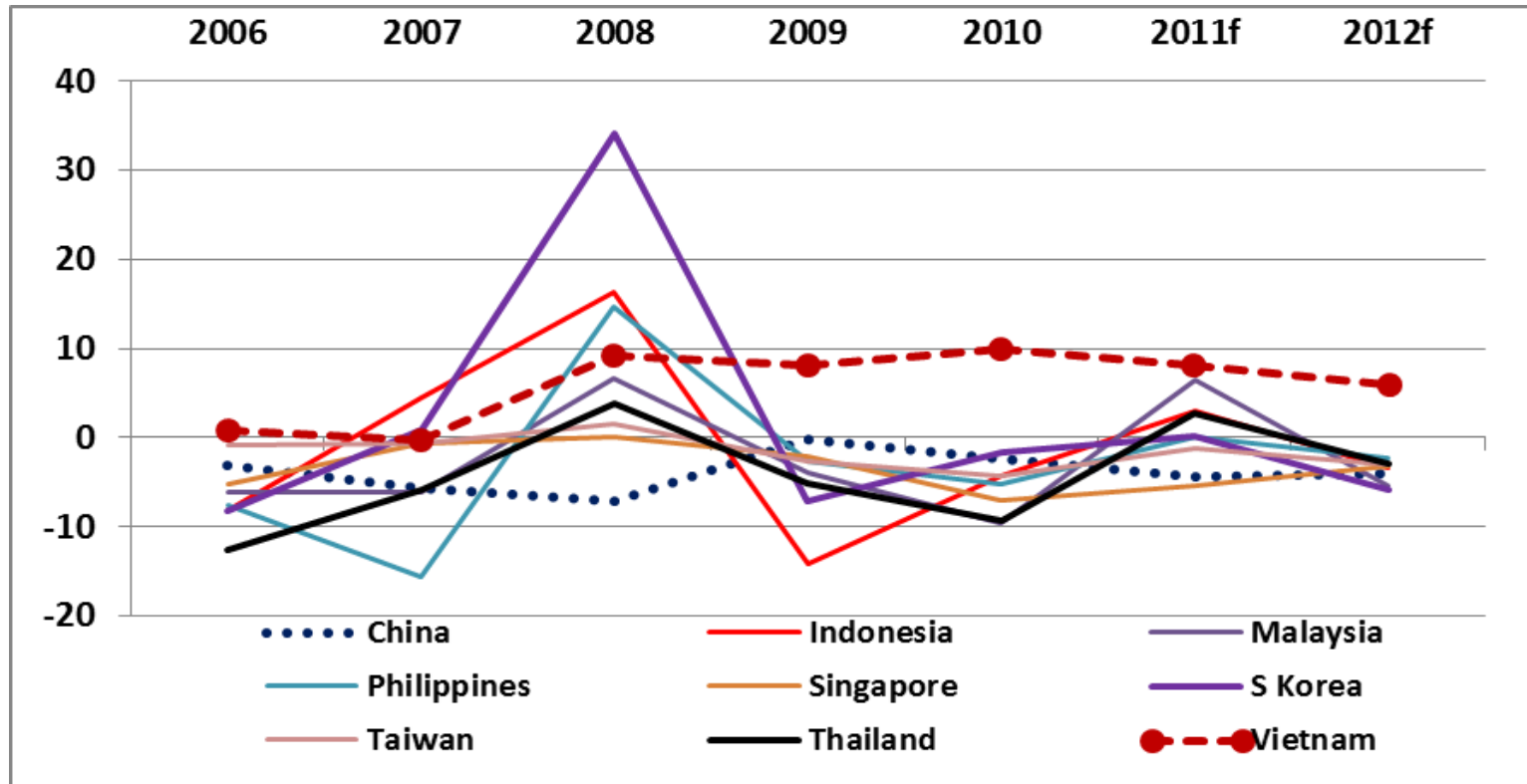
Figure 5: Base interest rate/refinancing rate of VN compared to the region



Source: Investment research by Citi, EIU (2011).

In the circumstance of high inflation, it is very difficult to keep a low level of interest rate.

Figure 6: USD against VND and other currencies in the region (% changes, end of period)

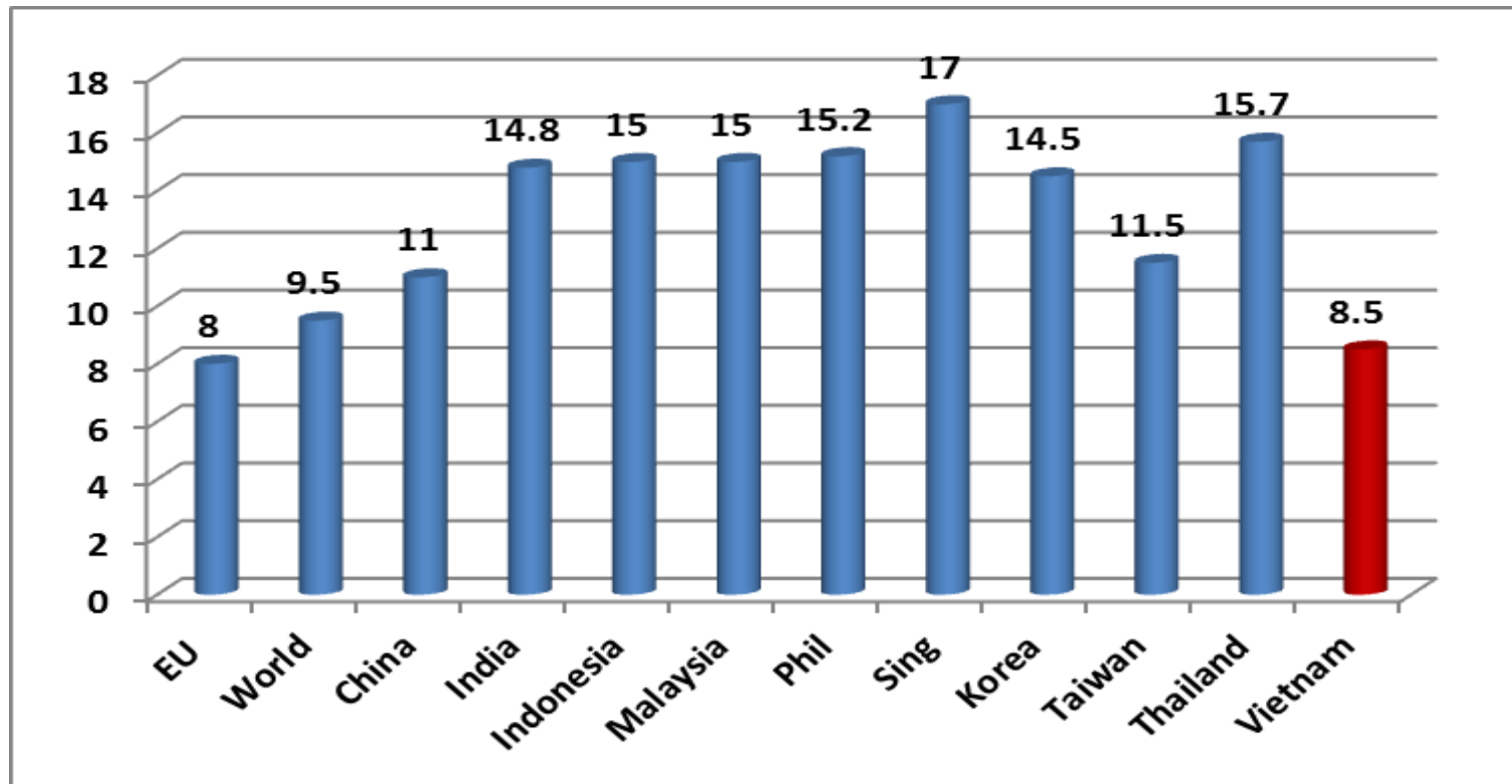


Source: Investment research by Citi, EIU (2011).

Unlike many other Asian countries, VND depreciated (against USD) since the global financial crisis in 2008.

Capital adequacy ratio is at an average level; but CAR is still low compared to the region

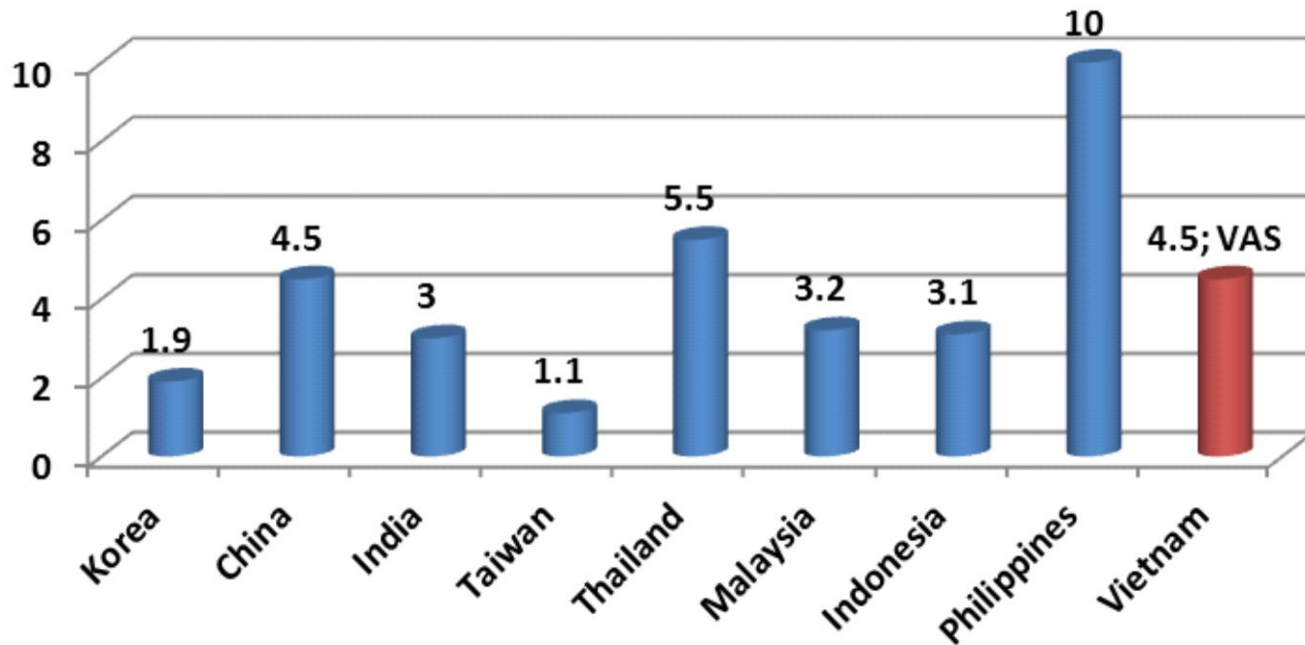
Figure 7: CAR of Vietnamese commercial banks compared to the region (2010, %)



Source: WB, FitchRatings 2011.

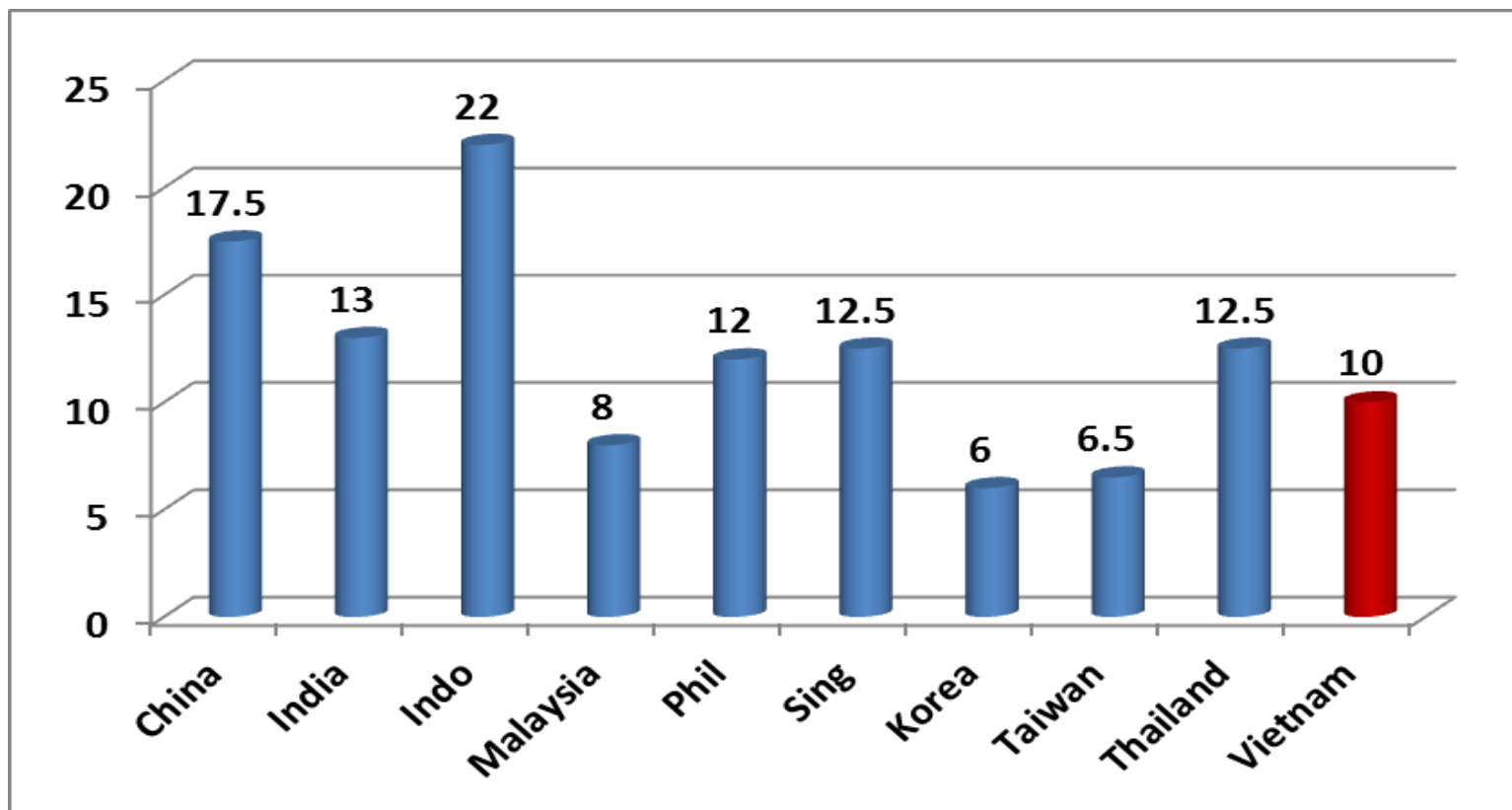
Credit risks of Vietnamese banking system at high level in the region

Figure 8: Ratio of overdue debt in 2010 of Vietnam and other countries (% total outstanding debt)



Source: FitchRatings, IMF, Central banks.

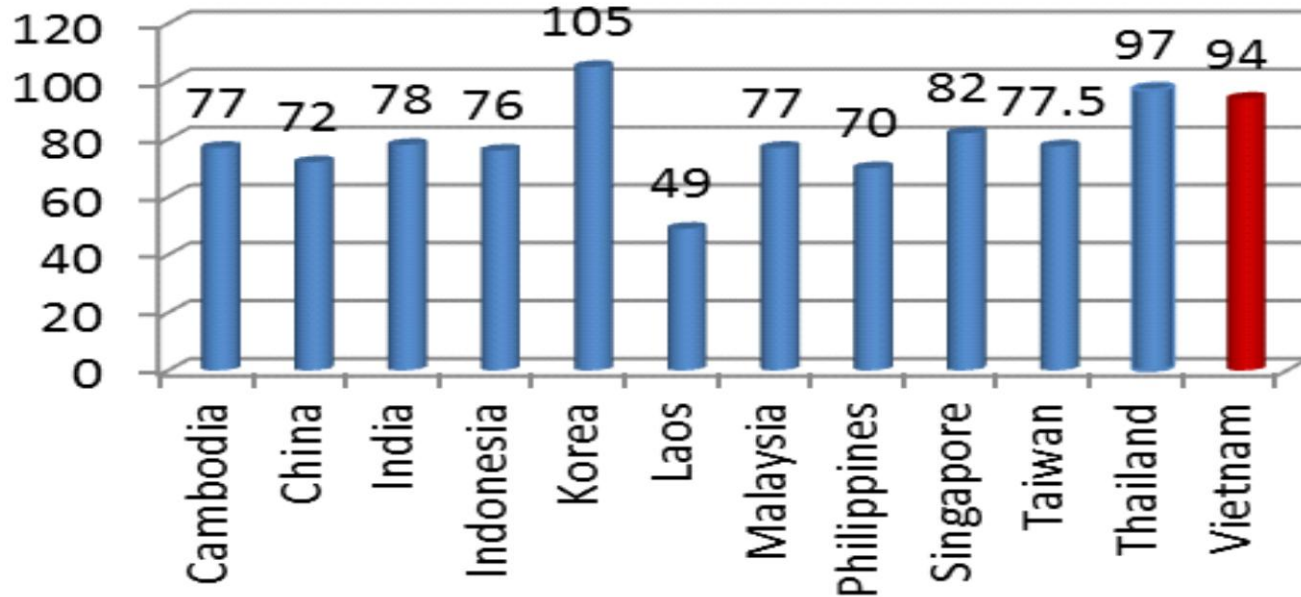
**Figure 9: Profitability (ROE, %, in 2010)
at low levels (according to **Fitch**)**



Source: Fitch, IMF, Central banks.

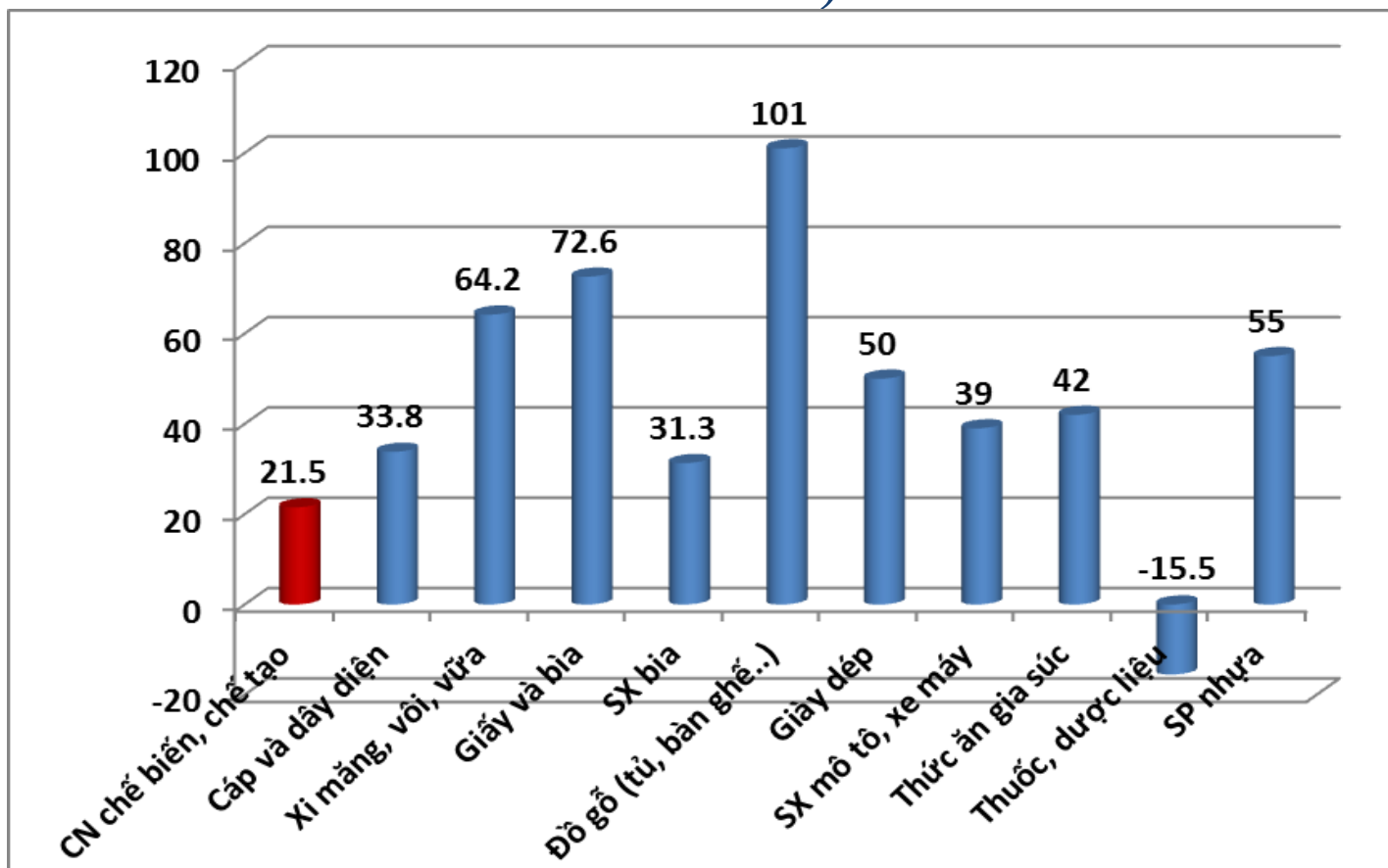
However, Vietnamese commercial banks always have a lot of liquidity risk

Figure 10: Ratio of Loans/ Deposits in 2010, (%)



Source: FitchRatings 2011, Central banks.

Figure 11: Increase in inventory index for the 10 first months of 2011 (% , against the same period in 2010)



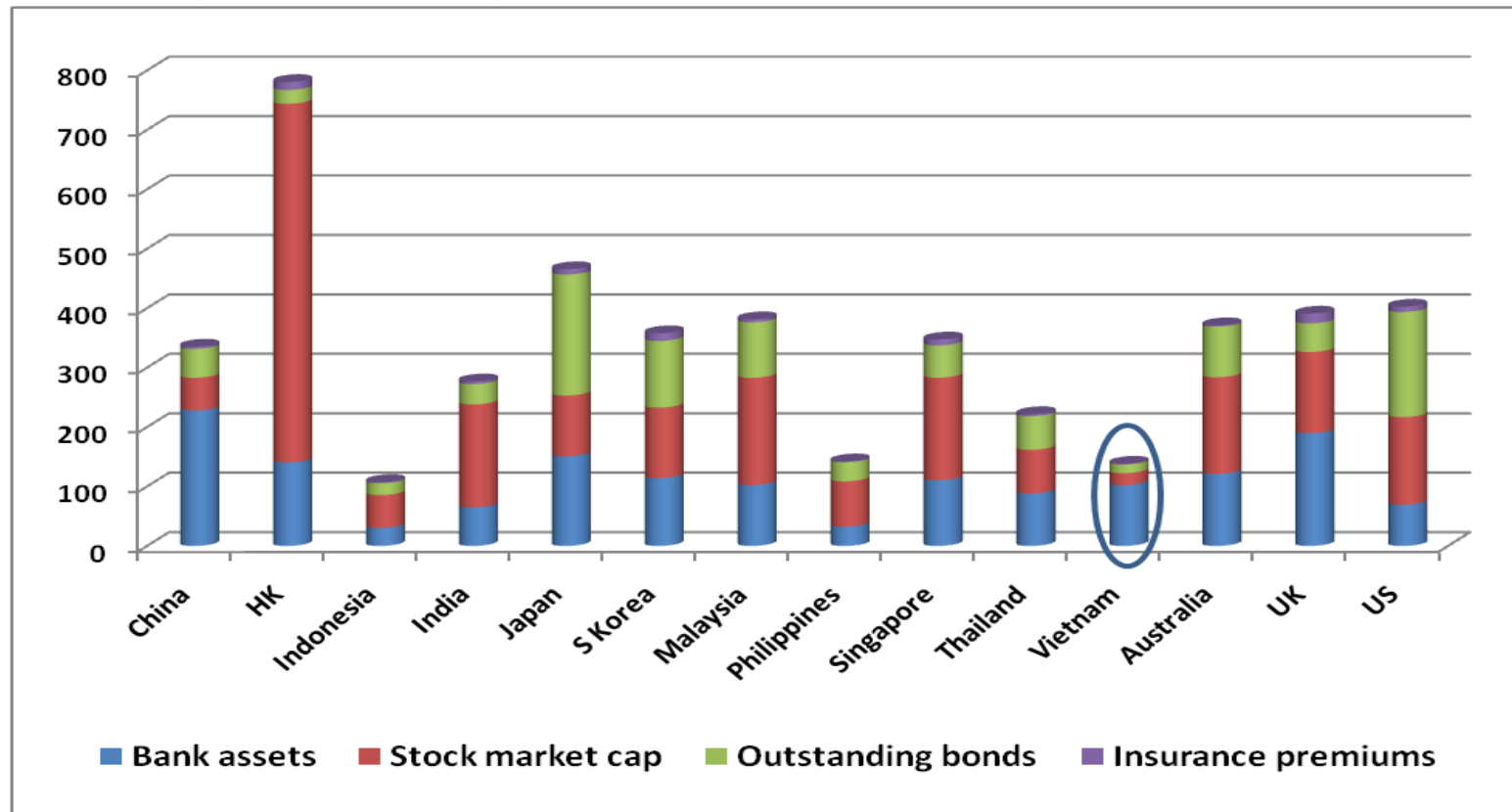
Source: General Statistics Office, MPI.

4. Structure of Vietnamese banking system

- Main force in the financial sector
- Do we have too many banks? (not really!)
- Joint-stock banks play more and more important roles
- Roles of non-bank institutions are still vague.

Vietnamese financial market

Figure 12: Scope of Vietnamese financial market and other Asian countries (% GDP 2008)



Source: Calculated according to Data from Beck et al. (2010) và WB Financial Development and Structure Data, updated in October/2010).

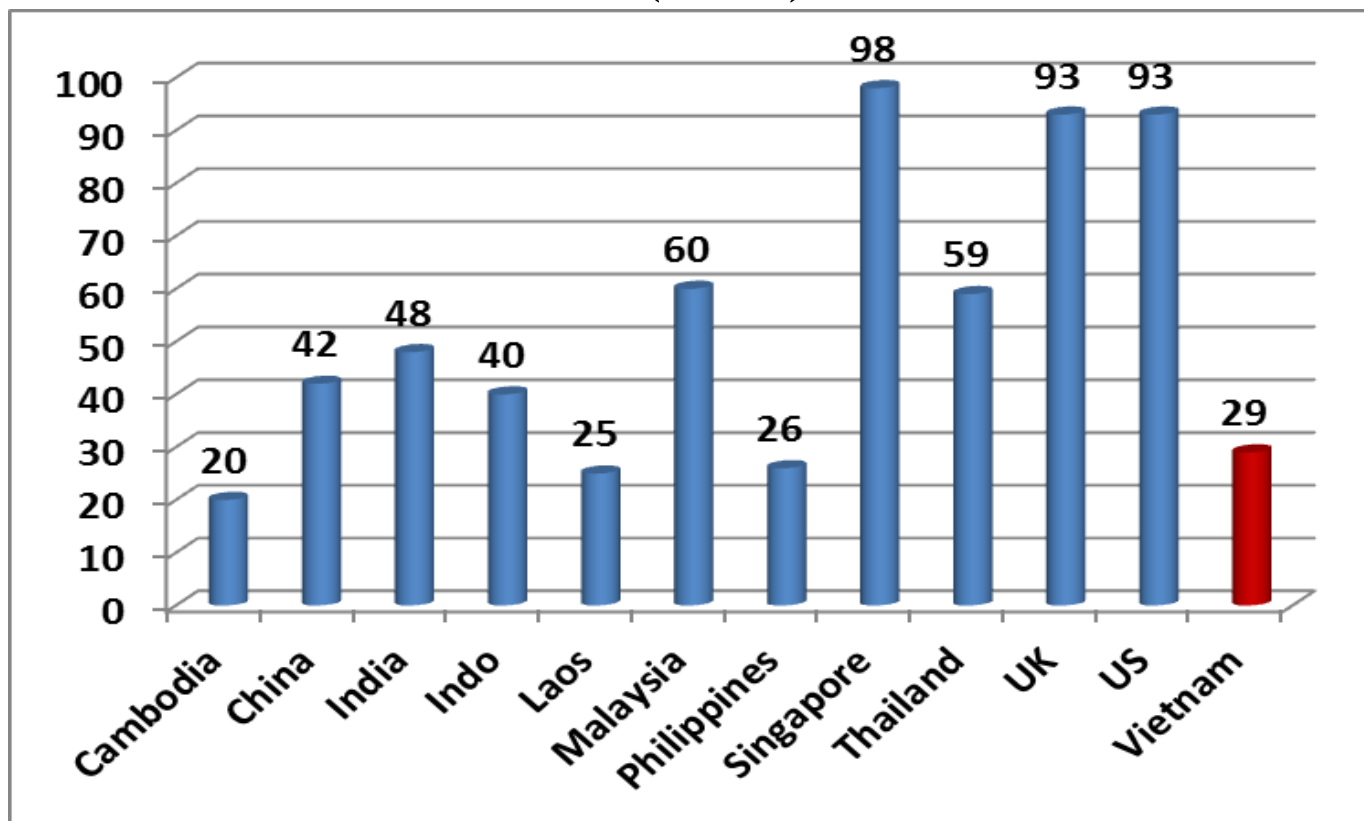
Table 5: Structure of Vietnamese financial market in 2010

Financial institutions	Asset share of financial sector	Regulator
<p>Banking and non-banking</p> <ul style="list-style-type: none"> ●5 state-owned commercial banks* (incl. Vietinbank & VCB) ●2 development/policy banks ●36 joint-stock commercial banks ●5 joint-venture banks; 5 wholly foreign-owned banks ●46 foreign bank branches and 48 representative offices ●915 credit funds and credit cooperatives. ●17 finance companies; 13 financial leasing companies. 	70%	State Bank of Vietnam (SBV)
Bonds (Gov't, corporate, bank bonds)	8.4%	
Insurance: 53 insurance companies	0.84%	Ministry of Finance
<p>Securities:</p> <ul style="list-style-type: none"> ●102 securities companies, 22 fund management firms ●6 custodian banks, 1 designated settlement bank ●770 firms and 557 bonds listed on 2 stock exchanges 	20%	State Securities Commission (MOF)
<p>Other: 1 state-managed social insurance fund</p> <ul style="list-style-type: none"> ●Deposit Insurance of Vietnam (DIV) ●Informal financial system 	1.1% n.a. n.a.	Government SBV Unregulated

Sources: SBV, World Bank, SSC, author's calculations.

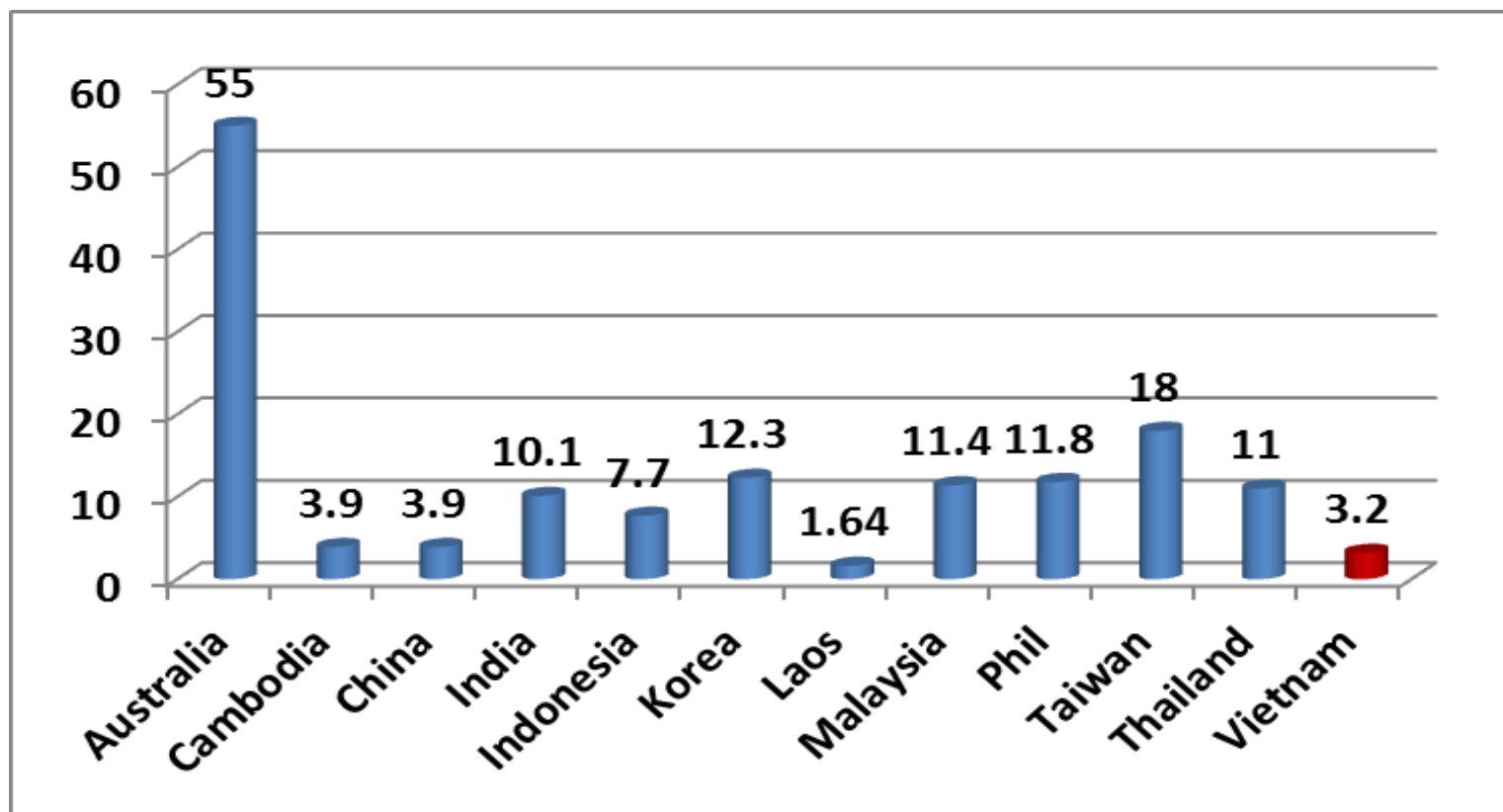
Structure of the banking sector

Figure 13: Percentage of users of banking services (2009)



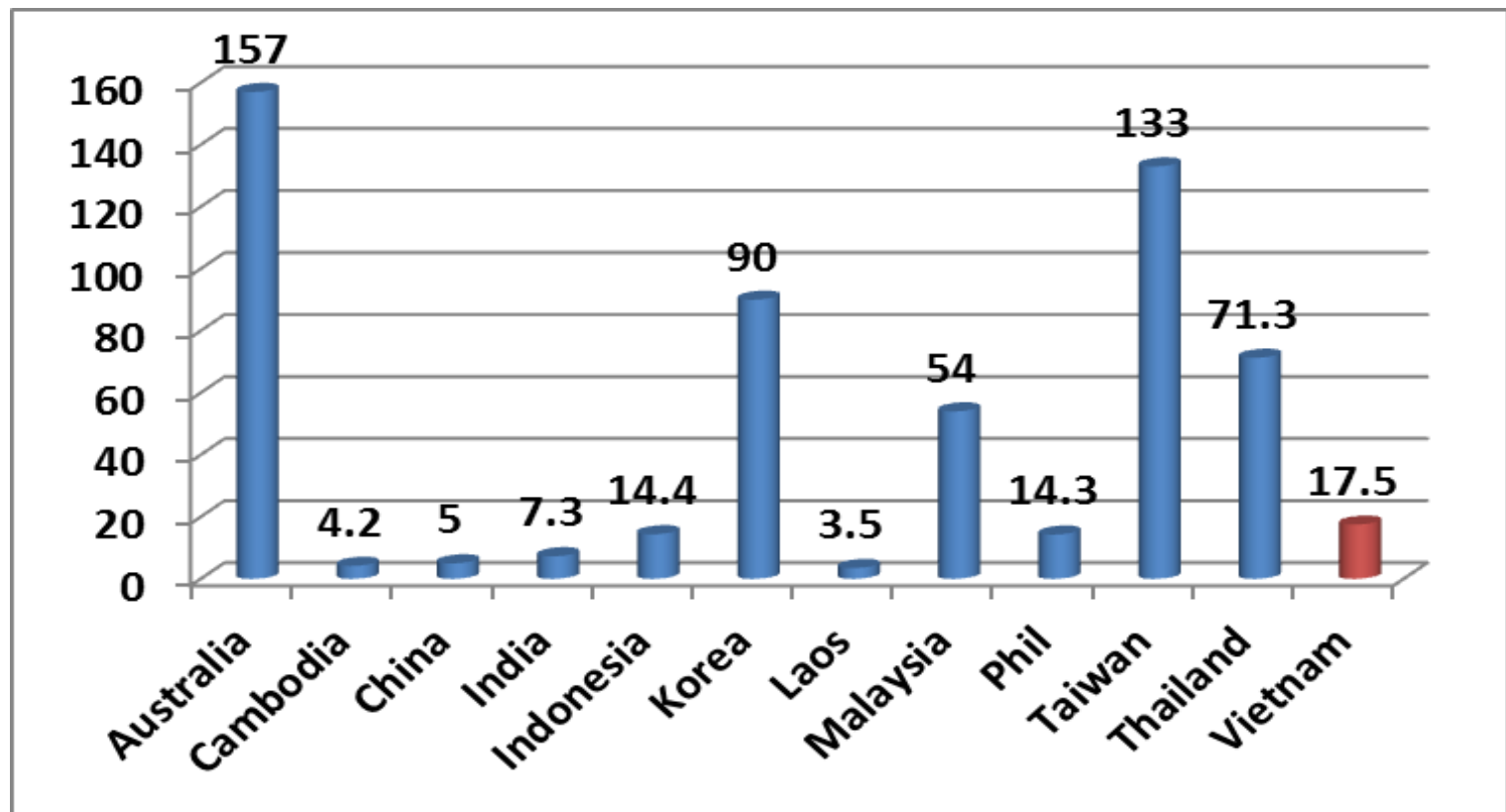
Source: WB, ADB 2010.

Figure 14: The number of branches of commercial banks/100,000 adults in 2009



Source: WB, Central banks.

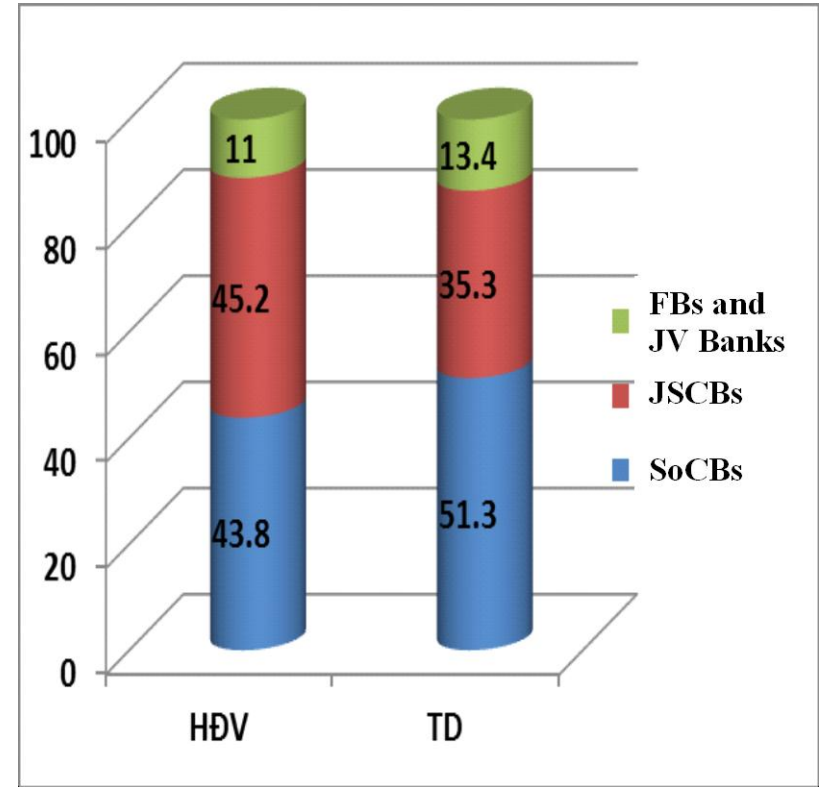
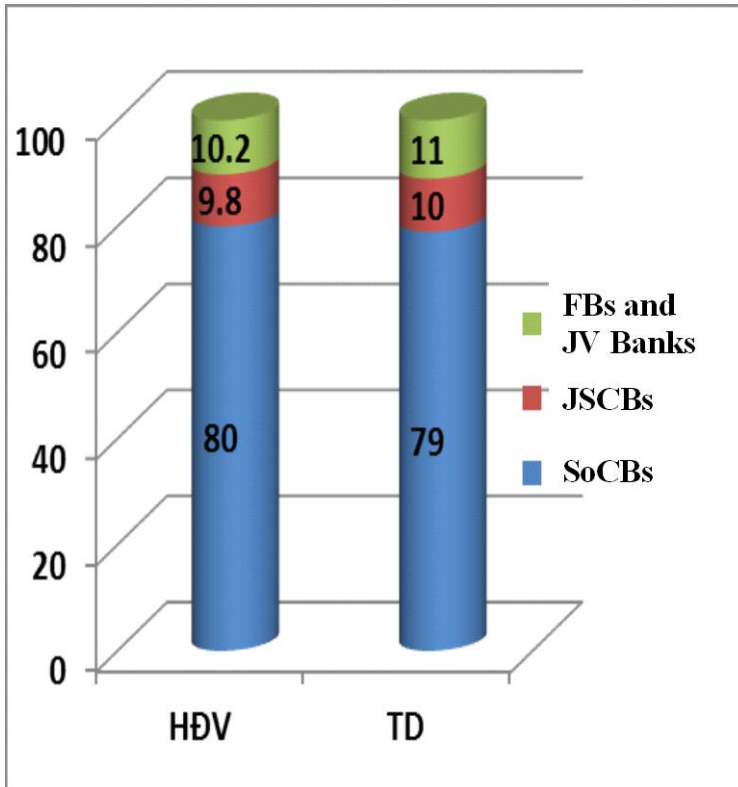
Figure 15: The number of ATMs/100.000 adults (in 2009)



Source: WB, Central banks.

Figure 16: Ratio of deposits and loans

[%, 2001 (left hand) vs. T10/2011 (right hand)]



Source: SBV 2011; A consultant project report by IBM Belgium, DMI, Ticon and TAC 2007.

5. Restructuring the banking system in Vietnam: Recommended measures

- **To combine both overall measures and individual measures**
- **The group of overall measures:**
 - Liquidity support
 - Continue to maintain ceiling rate?
 - Review, amend regulations on debt classification and risk provisioning
 - Set up an itinerary for raising chartered capital (upon application of Basel II)
 - Review regulations on licensing
 - **Increase roles of Deposit Insurance Institution**

Recommended measures (cont.)

- **The group of overall measures (cont.):**
 - To set up a banking system restructuring agency?
 - To guide regulations on selling-buying overdue debts in more open way (China securitized overdue debts since 2004)
 - To speed up investigation and supervision
 - To promulgate regulations on risk management
 - To increase independence of State Bank and banking supervisory agency
 - **To restructure the system of non-bank institutions (including VDB and Vietnam Bank for Social Policy)**
 - **To resolutely restructure SOEs and invest, restructure the stock and real estate market.**

Recommended measures (cont.)

- **The group of individual measures for commercial banks:**
 - To set up criteria and make assessment, classification of commercial banks (CAMEL??) to restructure and allocate credit
 - Ailing banks should be merged or supported by a “healthy” bank
 - Injecting State capital to save some banks is necessary, but it requires a suitable itinerary of capital divestment
 - To allow private investors, including foreign investors, to repurchase/supplement capital partly to problem banks
 - In the project of restructuring commercial banks, it is necessary to set up financial alternatives for restructuring costs (guarantee for bond issuance?).

The group of individual measures for commercial banks (cont.)

- Together with adoption of new debt classification, **to completely deal with NPLs and continue to raise minimum capital**
- To set up, implement and monitor implementation of itinerary of restructuring the banking system (often within 3-5 years)
- **To require each commercial bank to restructure** (finance, organization, activities, etc) and **renovate corporate governance** in banks.

Other measures

- To doing more researches on experiences of restructuring the banking system of countries in the Asian region (objectives, itinerary, results, etc)
- To draw lessons from the former restructuring stage (1998-2001)
- To implement both “renovate” organization and performance of State Bank (the problem of “legislation”)
- Political determination and goodwill is especially important.
- To develop bond market and debt transaction market.

Other measures???

- **Welcome your discussion**
- **Thank you**