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Handling Bad Debt of Credit Institutions – Experience from Vietnam Asset Management Company (VAMC)

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Abstract

Due to the impact of the global financial crisis, since 2010 Vietnam's economy began to decline, production and business activities of enterprises faced many difficulties leading to bad debt ratios at credit institutions tend to rise and having complicated movements. In order to stabilize the situation, in 2013, the State Bank established the Vietnam Asset Management Company (VAMC). VAMC's activities have brought about certain results in resolving bad debts of credit institutions. This study focuses on VAMC's bad debt handling activities from 2013 to 2018, draws on successful experiences as well as restrictions and recommends some recommendations to enhance bad debt handling efficiency of VAMC

Keywords: Bad Debts, Credit Institution, Debt Buying, Handling Bad Debts, Bad Debt in the Economy

1. Introduction

1.1. The context of bad debts at credit institutions in Vietnam in the period of 2013-2019

The bad debts at credit institutions are loans that have been due but have not been fully repaid and are overdue for more than 90 days after the due date of repayment. The system of credit institutions in Vietnam includes banks, non-bank credit institutions, microfinance institutions, and people's credit funds. By the end of 2018, the total bad debt of the whole system was VND 168.5 trillion, up 14.6% compared to the end of 2017; bad debt ratio was at 2.13%, compared to 1.99% at the end of 2017. In the whole system, there were still many credit institutions with a bad debt ratio of over 3% and the scale of bad debts were large. According to statistics of the State Bank, there were 27 credit institutions with an internal bad debt ratio of over 3%, including 8 commercial banks; 16 finance and financial leasing companies; 01 joint-venture bank and 02 foreign bank branches, of which were mainly weak credit institutions and were in the process of restructuring. The total bad debts of these 27 credit institutions stood at VND 69.6 trillion, accounting for 42% of the system's total bad debt (VAMC, 2018).

Regarding the debt group structure, among the bad debt groups from group 3 to group 5, of which group 5 debt has the highest proportion, accounting for 69% of the total bad debt. By the end of 2018, group 5 debt increased to 13% compared to 2017, with a total value of VND 115.65 trillion. Group 4 debt increased by 9.6% compared to the end of 2017, accounting for 14% of the total bad debt, with a total value of VND 23.17 trillion. Group 3 debt grew up by about 30% over the end of 2017, accounting for 17% of the total bad debt, with a total value of VND 26.68 trillion (VAMC, 2018).

In terms of collateral structure, 90% of bad debts are secured by assets with various types of collaterals such as real estate, machinery, valuable papers, etc., only 10% of the remaining bad debts have no collaterals. Through the above-mentioned statistics data, it can be seen that there are existing a relatively large number of bad debts in the whole system of credit institutions in Vietnam, the bad debts are mainly secured assets. This amount of bad debt, on the one hand, is a burden for the economy as well as the system of credit institutions but it is also a relatively abundant supply for the bad debt trading market in Vietnam and the need to buy and sell bad debts always exists. To deal with bad debts of credit institutions, macroeconomic stability, in 2013, the State Bank established the Vietnam Asset Management Company (VAMC).

1.2. Vietnam Asset Management Company (VAMC).

Vietnam Asset Management Company (VAMC) was established under the Decision No. 1459/2013/QĐ-NHNN dated June 27, 2013, of the State Bank of Vietnam, the State owns 100% of charter capital and is subject to the management, inspection, and supervision of the State Bank. Accordingly, VAMC had an initial charter capital of VND 500 billion, operating with non-profit purposes, using two main financial sources to handle non-performing loans, namely: charter capital allocated by State Bank and capital issue special bonds to buy bad debts from credit institutions.

VAMC's mission is to focus on handling bad debts of credit institutions which have a bad debt ratio of over 3% of total debt and bad debt with collaterals, especially assets secured by real estate. VAMC can buy and sell bad debts with special bonds or at the market prices.

1.2.1. VAMC buys and sells bad debts with special bonds

Special bonds are valuable papers with a term of 5 years from the date of issuance, with no interest payment and no payment value when they are due, being issued by VAMC to buy bad debts from credit institutions. A special bond is issued corresponding to one bad debt. Special bonds are valuable documents that can be used for refinancing at the State Bank. After 5 years, if the bad debt is not handled, this bad debt will be returned to the credit institution.

The bad debts of credit institutions are purchased by VAMC when meeting the following conditions:

- 1. The debts must be bad debts* including bad debts in lending credit activities; Purchase of corporate bonds not yet listed on the stock market or not registered for trading on the market of unlisted public companies; The entrusted purchase of unlisted corporate bonds, entrusted credit for which the credit institution that sells the debt bears the risk of overdue payment of part or all of the principal and interest of 90 days or more; or overdue for less than 90 days but the bond-issuing enterprise, the trustee and the beneficiary of the trust have bad debts at that credit institution.
- 2. Bad debts with secured assets;*
- 3. Bad debts and collaterals of bad debts must be lawful and have valid documents.*

The purchase price of debts by special bonds is determined as follows:

$$\text{Face value of special bonds} = \text{principal balance sheet value} - \text{risk provision}$$

After buying debts with special bonds, VAMC does not directly handle bad debts but authorizes settlement for credit institutions. VAMC plays a leading and coordinating role with credit institutions in drastically

implementing debt settlement solutions in order to accelerate the debt recovery process, actively supporting credit institutions in initiating lawsuits and enforcing judgments, seizing collaterals and making debt auction.

For credit institutions, selling bad debts to VAMC and receiving special bonds, credit institutions only make a provision of 20% per year for the number of bonds received instead of having to set up risk provisions credit for these bad debts at 20%, 50%, and 100% - corresponding to debt groups 3, 4 and 5, and, at the same time, special bonds can be used for mortgage or refinance capital from the State Bank. By transferring bad debts to VAMC, credit institutions can reduce the bad debt burden, gain additional capital, have more time and support to handle and recover bad debts. When a bad debt is settled, the special bond of that debt will be returned to VAMC at the purchase price.

1.2.2. Trading bad debts at market value

VAMC can use its charter capital to buy back bad debts at market value. Bad debts are purchased by VAMC at market value when fully meeting the following conditions:

- Bad debts meet the same conditions as those purchased by special bonds;
- Being assessed by VAMC to be capable of fully recovering the debt purchase amount;
- The collateral of bad debts is likely to be sold;
- Borrowers have prospects of repayment or have feasible repayment plans.

When buying bad debts at market value, VAMC must do self-assessment or hire an organization with an independent valuation function to determine the value of purchased bad debts at market prices; set up a plan to buy bad debts at market prices, submit them to the State Bank and obtain approval from the State Bank. After purchasing bad debts at market value, VAMC will directly manage and handle these bad debts through such forms as seizing collateral, completing legal procedures related to collateral and debts; introduction and offer to sell the debts or collaterals; organize auctions/competitive offers/negotiate debt and collaterals to recover debts; urge and support customers to pay their debts.

2. The activities handling bad debts of VAMC

2.1. Buying bad debt by special bonds

From 2013 to 2017, VAMC focused on buying debts with special bonds. Accumulated from its inception to December 31, 2017, VAMC has purchased special bonds with 26,274 debts of 16,835 customers at 42 credit institutions, with a total of the principal balance loan of VND 309,711 billion, the debt purchase price is 279,255 billion dong.

In 2019, VAMC purchased debt paid by special bonds of 381 debts, reaching VND 20,544 billion in the principal balance with the debt purchase price of VND 19,846 billion, reaching 99% of the plan approved by the State Bank at the beginning of the year. Accumulated to the end of December 31, 2019, VAMC has purchased bad debts with special bonds to reach 359,393 billion dong of internal principal debt with the debt purchase price of 327,413 billion dong.

Table 1: The numeral of debt buying by special bonds until 2019

Criteria	Unit	Accumulated to 31/12/2018	2019	Accumulated to 31/12/2019
Amount of the debt	Debt	26,982	381	27,363
Principal balance loan	Billion dong	338,849	20,544	359,393
Debt purchase price	Billion dong	307,567	19,846	327,413

Source: Summary report of VAMC's 2019 activities

Most of the debts bought by special bonds, VAMC authorized the entire management, debt settlement for credit institutions to actively implement. VAMC plays a leading role and closely coordinating with credit institutions in the implementation process, especially the seizure of collaterals, completing legal procedures related to

collaterals and debts, looking for investors to sell collaterals, debts, and procedures related to lawsuits and judgment execution.

Processing and recovering debts purchased with special bonds, as of 2019, VAMC has settled 163,868 billion dong of special bonds, debt collection reached 125,796 billion dong. In the period of 2016-2019, more than 50% of bad debts that credit institutions sold to VAMC by special bonds were recovered, contributing to significantly reducing the bad debt ratio at credit institutions. In particular, in 2017, VAMC has collected 30,852 billion dong, an increase of nearly 2,000 billion dong compared to 2016, exceeding the plan by 40%.

Table 2: Results of handling debts purchased with special bonds from 2013 to 2019

No.	Criteria	Unit	2013	2014	2015	2016	2017	2018	2019	Accumulated
1	Amount of the debt	Debt	1,514	8,644	14,310	1,241	565	708	381	27,363
2	Debt purchase price	Billion dong	30,947	77,198	99,243	40,036	31,831	32,631	19,846	331,732
3	The total amount of debt handling	Billion dong	146	4,875	17,142	28,853	30,852	37,250	125,796	244,914
4	Debt handling ratio	%	0.47	6.31	17.27	72.07	96.92	114.16	633.86	73.83

Source: Summary of the authors' group from VAMC's annual report

Based on the summary data in Table 2, it can be seen that VAMC's debt handling has been promoted since 2017 after the National Assembly's Resolution No. 42/2017 / QH14, VAMC was more autonomous in its operations and receive the support of the State Bank and authorities in the process of debt settlement. Therefore, the debt settlement result in VAMC increased rapidly from 97% in 2017 to 633% in 2019. During the period of 2013-2019, VAMC's debt settlement result reached 73.83%.

2.2. Buying debt at market value

In 2017 was the first year VAMC successfully implemented debt purchasing activities at market value at 05 credit institutions, with the total debt purchase price of VND 3,141 billion and total principal outstanding of VND 2,938.6 billion, reaching 100% of market debt purchase plan in 2017 approved by the State Bank (VAMC, 2018).

In 2019, thanks to an increase of the charter capital of VND 500 billion, VAMC has signed contracts with 04 credit institutions to buy debt at market value for 16 customers of 37 debts with a total purchase price of VND 2,247 billion, reaching 112% of the market debt purchase plan approved and adjusted by the State Bank (Nhưng, 2020).

Accumulated from 2017 to the end of December 31, 2019, VAMC has purchased bad debts at the market value of VND 8,013 billion with the original principal balance of debt with the purchase price of VND 8,207 billion.

Table 3: The numeral of debt buying at market value until 2019

Criteria	Unit	Accumulated to 31/12/2018	2019	Accumulated to 31/12/2019
Amount of the debt	Debt	46	37	83
Principal balance loan	Billion dong	5,882	2,131	8,013
Debt purchase price	Billion dong	5,960	2,247	8,207

Source: Summary report of VAMC's 2019 activities

Debts purchased at market value, VAMC directly manages and handles debt, not authorizing credit institutions to sell debts. Accordingly, VAMC has actively implemented the full debt management process, urged, recovered debts from customers, carried out procedures for handing over, seizing, and valuing ... to deploy the handling plan debt recovery. After buying debt at market value, VAMC has immediately implemented appropriate debt settlement solutions such as regularly urging customers to pay debts, applying debt restructuring, seizing and selling collaterals by auction or agreements; assisting the buyers in completing legal procedures related to project transfer to recover debts. As a result, in the first year of buying debt at market value, VAMC has basically recovered the debt purchase amount with the total amount recovered from the debt purchased at the market value of VND 2,641 billion compared to VND 3,141 billion debt purchased. In 2019, VAMC has recovered bad debts bought at the market value of VND 1,630 billion. Accumulated to December 31, 2019, VAMC has recovered bad debts purchased at the market value of VND 5,178 billion out of VND 8.013 billion of debt purchase, reached 64.61%. Also in 2019, VAMC has organized many successful auctions with a total winning price of nearly VND 831 billion, the total value of assets sold exceeded the starting price of VND 3.15 billion.

3. Experiences from VAMC's activities

The results of dealing with bad debts have shown that VAMC is an effective and feasible tool to handle bad debts, contributing to settling bad debts for the credit institution system, solving difficulties for businesses, and creating conditions for the enterprise to recover. Besides, VAMC strengthens financial health, especially in facilitating and promoting credit expansion to the economy safely and effectively.

VAMC uses a special bond tool to buy bad debts, in essence, to keep bad debts for credit institutions, helping these credit institutions to have opportunities, resources and time to resolve bad debts. VAMC's purchase of bad debts by special bonds has achieved certain results in recent years, contributing to the handling of bad debts quickly, bringing the bad debts ratio to below 3%, ensuring the safety of the banking system, creating conditions for credit institutions to have more capital to supply the economy and restructure for surviving and development. However, through the handling of NPLs of VAMC, there is a number of limitation issues as follows.

Firstly, VAMC buys bad debts by special bonds, in fact, VAMC is only a place to store bad debts for a time to help credit institutions reduce the pressure of provisioning without being able to direct financial supplement for credit institutions, so the process of dealing with bad debts is only technical and its effectiveness is limited.

Secondly, after acquiring bad debts with special bonds, VAMC does not directly handle bad debts but authorizes credit institutions to directly handle them, VAMC only supports the procedures for seizing and selling collaterals. Thus, the handling of purchased debts of VAMC is still quite passive and depends on the activeness of credit institutions.

Thirdly, VAMC's chartered capital is only VND 500 billion initially, and be added another VND 500 billion in 2019, making it difficult to meet bad debt acquisition activities at market prices, limiting the ability to handle bad debts of VAMC.

Fourthly, although buying debt by special bonds or buying at market value but the implementation of VAMC's right to seize, transfer, mortgage collaterals still face many difficulties. Many mortgage contracts do not specify and not all bad debts can be secured collateral; The transfer of real estate projects without land-use certificates still faces many difficulties when conducting the transfer procedures at the competent authorities. Therefore, discouraging organizations and individuals from buying back debt from VAMC.

Fifth, during the process of debt settlement by VAMC, the borrower agrees to add collaterals as land use rights under the 2013 Land Law, VAMC has no lending function and cannot directly receive the mortgaged by land-use rights. This limitation greatly affected the handling of bad debts that VAMC had bought.

4. Recommendations

To facilitate and improve the efficiency of VAMC's in purchasing and handling of bad debts, there are some recommendations:

The Government and the State Bank of Vietnam consider continuing to finance VAMC so that VAMC can afford to buy bad debts at market value, paving the way for VAMC to change its operational mechanism from debt purchase by special bonds to buy at market prices, thereby increasing the autonomy in handling debt of VAMC.

The authorities should urgently consider and permit the establishment of the Debt Trading Center. There is currently a relatively large amount of bad debts in the Vietnamese credit institution system, which can be considered as a fairly abundant supply for the bad debt trading market in Vietnam. The establishment of the Debt Trading Center is really necessary to promote the development of the debt trading market, which can be used as a place to provide information, consulting services, brokerage, purchase, and sale the bad debts and collaterals at credit institutions.

The Government and functional agencies should urgently adjust and complete the guiding regulations on the seizure, transfer, and mortgage of collaterals from bad debts of credit institutions, especially are collaterals by land use rights, assets attached to land-use rights or properties attached to land in the future. Assuring VAMC to carry out the right to seize, transfer and mortgage safely and conveniently.

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