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A Dream Deferred? The 'Equitization' of Vietnam's State-Owned Enterprises

Vietnam's progress toward a more liberal, market-friendly economy has proceeded in fits and starts.

By James Guild

Vietnam has weathered the COVID-19 crisis better than most nations. The spread of the virus has been managed well, and despite turmoil in global markets the economy grew by around 3 percent in 2020, while running a $19 billion trade surplus. Investment inflows have likewise remained strong, leaving the country well-positioned for a post-pandemic recovery. How is it that Vietnam has fared so well?

The short answer is that the economy has undergone big structural changes in recent decades, harnessing private investment and trade as engines of growth. After Vietnam joined the World Trade Organization in 2007, foreign direct investment increased dramatically with net inflows hitting $15.6 billion in 2019. Compared to portfolio investments like bonds, which can be sold off quickly during times of uncertainty, FDI is a more stable, productive, and long-term form of capital inflow.

But Vietnam's success with foreign investment and trade is only one part of a bigger story, at the heart of which lie dramatic changes in the relationship between the state and the economy. For years, the state has been trying to unwind its direct ownership in key sectors, privatization efforts that have been critical to Vietnam's market-friendly development model. Yet the state's track record of divesting from key industries has been a case of two steps forward and one step back, with missed deadlines and revised timetables being the norm even before COVID-19.

Compared to Indonesia, where many state-owned assets were sold off in a fire sale to raise capital during the Asian Financial Crisis, Vietnam has proceeded more methodically and gradually. The government prefers the term "equitization" to privatization, because it first converts state-owned companies into joint stock companies where the state remains the sole or majority shareholder.

After that, there begins a lengthy process of gradually selling some of the shares either on the Ho Chi Minh City or Hanoi stock exchange, or on the Unlisted Public Company Market, an exchange for companies that have not been listed or whose IPOs flopped. The state often reserves a minority stake for a few hand-selected strategic investors, which begs the question of whether these truly constitute market reforms at all. Prior to any public offering or listing, various officials are responsible for estimating a market valuation and submitting formal equitization plans for approval. It is not a process designed for speed.

As Erin Cook wrote for The Diplomat, 2017 was meant to be a turning point for the state's divestment efforts as a list of 375 firms was finalized for privatization by 2020. This was punctuated at the time by Thai drink giant ThaiBev acquiring a 54 percent stake in Sabeco, a major beer company. Previously owned by Vietnam's Ministry of Trade and Industry, the investment was valued at $4.8 billion and it was hoped it would kick off a wave of state-owned companies hitting big pay days on the stock market.

That has yet to materialize at the scale envisioned. According to a report in the Hanoi Times, from “2016 to November 2020, 178 SOEs had their privatization schemes approved with a total asset value of VND 443.5 trillion (US$19.1 billion).” Yet as 2020 came to a close, only 37 of them had actually executed their plans. This is due partly to cumbersome procedural requirements, and partly to good old fashioned politics, in that vested interests within the state may not be entirely willing to cede key strategic sectors to private actors. In other cases, state-owned companies have simply been badly run and hold little market appeal.

Energy is one area where state divestment has under-delivered. Vietnam’s economy has been growing so rapidly that in order to ensure electricity supply can keep up with surging demand, the sector has been thrown open to foreign investment. Last year a liquefied natural gas power plant in Bac Lieu drew in $4 billion from Singaporean investors, just one of many multi-billion dollar foreign financed power projects in recent years. But market interest in Vietnam’s state-owned power companies has been much more muted.

In addition to owning and operating its own power plants, Vietnam’s state-owned electric utility EVN controls three power generating companies, including one called GENCO 3, which in 2018 accounted for 12.75 percent of Vietnam’s total installed capacity. GENCO 3 was the first of EVN’s generating companies to be converted to a joint stock company and listed on the Ho Chi Minh City stock exchange. But the company’s 2018 IPO was a flop, raising only around $8 million of an expected $290 million offering.

The state-owned mining company, Vinacomin, has not fared much better. Vinacomin is frequently mentioned as a candidate for divestment, although nothing concrete ever seems to eventuate. But it has tried its hand at spinning out some of its subsidiaries to private investors. One subsidiary, Vinacomin Power, placed 236.4 million shares up for sale during its 2016 IPO. Only 1.2 million ended up being sold. It may be that the government-approved valuation was too high relative to the company’s profitability, or the complexity of Vietnam’s energy markets may have turned off investors.

But even companies with more straightforward finances have stumbled in realizing the state’s equitization mandate. MobiFone, one of the largest mobile phone operators in Vietnam, is a solid performer, booking pre-tax profits equal to 18.6 percent of revenue in 2019. Moreover, the company has little debt, and a healthy asset-to-equity ratio. If it were to file an IPO it would be an attractive investment. But its equitization plans were postponed in 2018 after allegations that MobiFone intentionally overpaid to acquire a pay TV service, a scandal that led to lengthy prison sentences for some of the people involved.

It would seem that Vietnam’s equitization efforts have so far been hampered by a string of failed IPOs, unrealistic valuations, and other internal mishaps. But an interesting pattern starts to emerge when you look beyond strategic sectors like telecommunications and energy, where various stakeholders arguably have a vested interest in maintaining state control. By comparison, the equitization of the Vietnam National Textile and Garment Group (Vinatex) has been much smoother, with the state reducing its ownership stake to about 53 percent in 2017.

As a textile and garment manufacturer and exporter, Vinatex needs to compete against other companies both globally and domestically. It doesn’t control the provision of a strategic public good, like EVN and its subsidiaries or MobiFone, and therefore is subject to a different type of political and economic calculus when it comes to state divestment. As Fujita Mai of Japan's Research Institute of Economy, Trade and Industry noted in a report on Vinatex's equitization, the "degree of external pressure for reforms and liberalization [of SOEs], as well as competition resulting from increased openness, is likely to vary substantially across sectors."

SOEs with monopoly power in strategic sectors like energy may be under some pressure to privatize, for instance if the state does not want to shoulder all of the financial burden of building out more generating capacity. But they aren't under the same pressure to reform as an SOE in a more competitive market like textile manufacturing or retail. If Vinatex can't compete with Chinese garment exporters, it will go out of business. The same can't be said for state-owned energy or telecom companies that enjoy privileged market share and little or no competition.

Looking at large strategic sectors, Vietnam's equitization process appears to have been marked by more false starts than finish lines. Major companies have had their IPOs flop or their plans scrubbed due to internal discord. But a look at the loan portfolio of Vietinbank, one of the largest commercial banks in the country, hints at the shrinking role of the state in the Vietnamese economy. In 2009, 34 percent of Vietinbank's loans were made to companies that were either completely or majority owned by the state. By 2019, that had fallen to 13 percent, with private businesses and individuals receiving 82 percent of all loans. (Foreign-invested companies made up the balance, at just 5 percent.) In fact, loans to private businesses and households more than doubled between 2015 and 2019.

Even as the pace of equitizations fails to live up to the promises, the allocation of commercial bank loans suggests the state is indeed pulling back from the economy and being displaced by private, domestic Vietnamese businesses and consumers. This is where Sabeco re-enters the picture. In 2019 ThaiBev invested an additional $3.85 billion in Vietnam Beverage, a subsidiary that controls the Thai conglomerate's 54 percent stake in Sabeco.

The interesting thing is that Sabeco hardly makes any money from exports, with 99 percent of its 2019 revenue coming from domestic sales. So while FDI is often associated with manufacturing and exports oriented toward foreign markets, it's not always the case. Sabeco underscores the important role of local companies and local consumption in all of this, as ThaiBev has channeled billions of dollars into its Vietnamese holdings in order to capitalize on a growing domestic market.

Vietnam's path toward a more liberal, market-friendly economy has not progressed along a straight line. It has lurched forward in fits and bursts, with grand plans only partially realized. But the bottom line is that the structure of the economy is gradually shifting away from state ownership, especially in truly competitive sectors like textiles and retail. And while the state may only partially, if ever, relinquish its hold on sectors such as energy and telecommunications, the overall effect has been to signal that Vietnam is open for business.

Stable, long-term foreign investment and exports are driving big current account surpluses and creating jobs, and they form an important part of Vietnam's success so far. But the strong performance of local businesses and consumers – and the state's determination to make room for them, even if haltingly – is another one that perhaps doesn't get as much attention as it should. And ultimately, it is the totality of these various things coming together that has given Vietnam some extra economic flex as it deals with the pandemic, and should help lead a quick recovery once it's over.

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