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VIETNAM INBOUND M&A ACTIVITY: THE ROLE OF GOVERNMENT POLICY AND REGULATORY ENVIRONMENT

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Abstract

With a robust recent history of reform and opening, joining of the World Trade Organization, and negotiating a myriad of regional and global trade agreements, Vietnam has emerged as a promising destination for foreign direct investment (FDI) and cross-border mergers and acquisitions (M&A). In this paper, we provide an overview of Vietnam's inbound mergers and acquisitions and review the two main driving forces of inbound M&A, which are the legal framework reform process and the equitization of State-owned enterprises. We close by providing directions for future research in the area of cross-border M&As.

Keywords: Vietnam, merger, acquisition, cross-border, legal issues, state-owned enterprise.

Abstrak

Dengan sejarah reformasi dan era keterbukaan yang terjadi di Vietnam yang baru, bergabung dengan Organisasi Perdagangan Dunia (WTO), dan telah menegosiasikan berbagai perjanjian perdagangan regional dan global, Vietnam telah muncul sebagai destinasi bisnis yang menjanjikan untuk investasi asing langsung (FDI) dan merger dan akuisisi lintas batas (M & A). Berdasarkan studi ini, peneliti memberikan ikhtisar tentang merger dan akuisisi yang masuk ke Vietnam dan meninjau dua kekuatan pendorong utama merger dan akuisisi lintas batas yang merupakan proses reformasi kerangka hukum dan pemerataan perusahaan milik negara. Studi ini juga memberikan arahan untuk penelitian masa depan di bidang merger dan akuisisi lintas batas.

Kata kunci: Vietnam, merger, akuisisi, lintas batas, legal, badan usaha milik negara.

The 1986 Đổi Mới began an era of economic policy liberalization in Vietnam focusing on food production; private, domestic and foreign investments; and alleviating state interference in business activities.

In the following year, the Law on Foreign Investment was approved, which in principle, opened up Vietnam for foreign investment. Along the way, Vietnam made many strides on economic and financial dimensions,

but the pace accelerated after the 2006 National Congress meetings. The Congress reaffirmed commitment by the Vietnamese government in liberalization and accelerated the move toward a market economy. The 2007 accession to WTO helped kick-start the first wave of M&As, which is considered to be from 2008 to 2013, with a reported total value of US\$15bn. The year 2014 marked the second phase (2014-2018), which began with continuation of strong growth in M&As; however, there was a slowdown in the early stages, which was expected to reverse in 2016.

In this concept paper, we provide an overview of cross-border M&A history in Vietnam during the first and second wave, and a review of the legal framework governing M&As, in general, and cross border M&As, in particular. This effort is a preliminary step toward a comprehensive research project intended to assess the impact of cross-border M&As in Vietnam on the acquirer and acquired companies' valuation and financial performance.

LITERATURE REVIEW

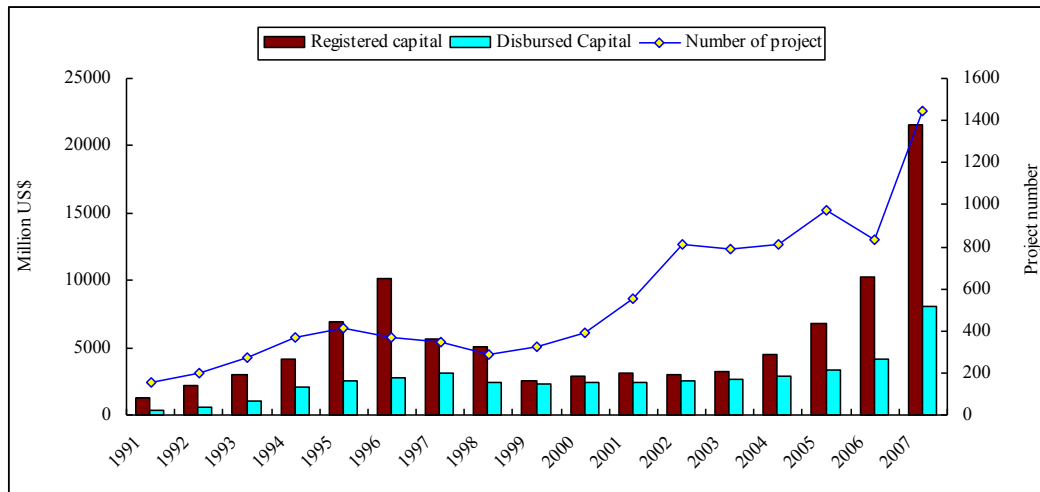
To our knowledge, the literature on M&A (including inbound M&A) in Vietnam is scant. The only extensive research on M&A in Vietnam can be found in a study by Vuong et al. (2009). Using qualitative methodology, Vuong et al. analyzed 252 cases of M&As in 1990-2009, which accounted for 40 percent of total M&A deals and included both inbound and domestic M&A cases. The study focused on analyzing the success rate of M&A deals, the frequencies and transaction values, and M&A deals in various industries.

Our research stream aims to begin by a conceptual, qualitative analysis of the inbound M&A environment in Vietnam between 2008 and 2015. First, we examine the general trends of inbound M&A and the flux of inbound M&A in various industries. Second, we analyze the changes in the legal framework for inbound M&A and the equitization process of State-owned enterprises (SOEs) to provide justification for the inbound M&A trends.

Overview of the cross-border M&A activity in Vietnam

Since the Law on Foreign Investment was approved in 1987, there has been substantial FDI inflow into Vietnam. From 1988 to 2007, the Vietnamese economy attracted a total investment capital of US\$98.0 billion in terms of commitment, while the total realized capital was US\$45.5 billion. Notably, registered FDI reached a record high level of US\$20.3 billion in 2007, up by 69.1% from US\$10 billion in 2006, according to Vietnam's General Statistics Office (2006).

The M&A activity initiated at the beginning of the 1990s but did not show a clear trend until 2007, with more than 100 successful transactions (Vuong et al., 2010). From 2008 to 2013, M&A activity surged in Vietnam, creating the so-called "first wave" of M&A activity. The first wave of M&A activity in Vietnam is likely to have been driven by the integration process of the Vietnamese economy into regional and world economies that took place in the previous period, such as participation by Vietnam in the Association of South East Asian Nations (ASEAN) in 1995, the Asia Pacific Economic Cooperation (APEC) in 1998, the signing of Vietnam-United



Source: Statistical Yearbook of Vietnam, [2006]

Figure 1. FDI registered capital and implemented capital into Vietnam

States Bilateral Trade Agreement in 2000, and accession into the World Trade Organization (WTO) in 2007.

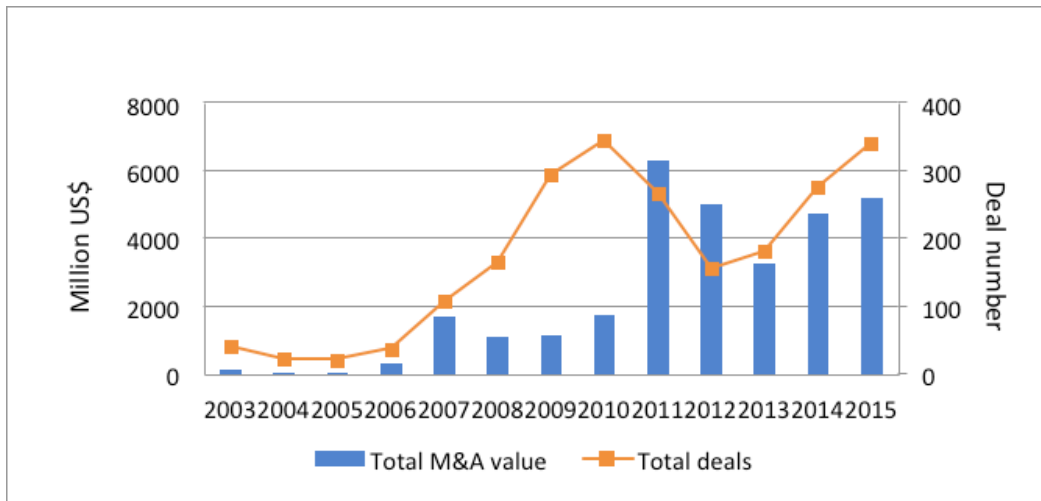
In the first wave, the total value of M&A deals rounded up to US\$15 billion. M&A value trended upward from US\$1 billion in 2008 to US\$5 billion by the end of 2012, and slightly declined to US\$4 billion in 2013¹. While the total M&A value peaked in 2012, 90% of the deal value was cross-border (inbound) M&As (Baker and McKenzie report, 2013). The second wave of M&A activity was set off in the next five years (2014-2018), with total value expected to reach US\$20 billion from 2014 to 2018.

Inbound M&A in Vietnam is expected to accelerate as well thanks to Vietnam's further integration into the global market. Indeed, 2015 marked the year that many new Free Trade Agreements (FTAs) were signed. In 2015, Vietnam concluded negotiations for four FTAs,

including those with the Eurasian Economic Union, the European Union, South Korea and the Trans-Pacific Partnership (TPP). Granted, in light of the unexpected Trump victory in the US elections and uncertainty regarding the policies of his administration, particularly with respect to trade, it remains to be seen which path may await the recently negotiated, but not yet ratified, TPP. Regardless, as the integration process deepens, the reformed legal framework and the equitization process of SOEs are believed to be the driving forces behind inbound M&A trends (StoxPlus Report, 2016).

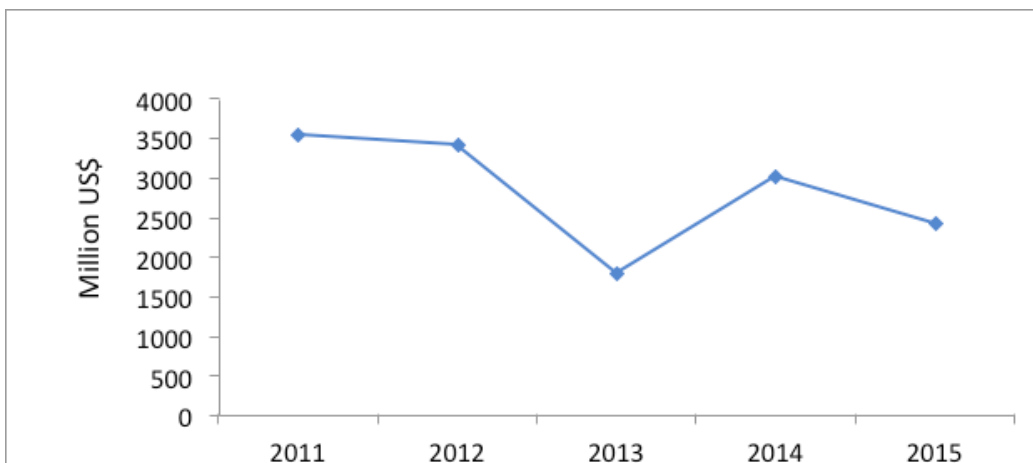
However, data indicate that inbound M&A in Vietnam fell in the 2012-2013 and 2014-2015 period. Total inbound M&A value in 2013 decreased by 47%, as compared with the previous year. While total M&A in 2015 recorded a 23% increase in deal number and 9.7% increase in deal value as compared with 2014, inbound M&A stood at US\$2.4

¹ <https://www.talkvietnam.com/2014/07/second-ma-wave-in-vietnam-to-top-first-by-5-billion/> (accessed 9 June 2016).



Source: StoxPlus Reports (2013-2016)

Figure 2. Total M&A value and deals



Source: StoxPlus Report (2012-2016)

Figure 3. Inbound M&A value

billion, which was 21% lower than the total value of inbound M&A in 2014.

Inbound M&A in various industries between 2012 and 2015

The industries that attracted the most inbound M&A (in value) are listed in Table 1.

There are several remarkable trends that can be deciphered from Table 1.

First, real estate increasingly attracted the attention of foreign investors. From the 6th position on the list of 2012, the real estate industry rose to rank first on the 2015 list. Deal value increased from US\$1.9 million in 2012 to a peak value in 2015 at US\$1.6 billion. The average M&A size per deal also showed tremendous growth, increasing from a mere US\$1.9 million per deal in 2012 to US\$86.16 million per deal in 2015 (Stoxplus Report, 2016). Second,

Table 1. Top 10 industries (in deal value) attracting inbound M&As

| Year | 2012 | 2013 | 2014 | 2015 |
|----------|---|---|--|--|
| Industry | 1. Oil and gas 2. Banks 3. Construction and materials 4. Insurance 5. Food and beverage 6. Real estate 7. Telecommunications 8. Chemicals 9. Technology 10. Personal and household goods | 1. Food and beverage 2. Real estate, 3. Utilities 4. Retail 5. Oil and gas 6. Healthcare 7. Technology 8. Travel and leisure 9. Banks 10. Construction and materials | 1. Retail 2. Real estate Food and beverage 3. Oil and gas Travel and Leisure 4. Banks 5. Chemicals 6. Industrial goods and services 7. Construction and materials 8. Personal and household goods | 1. Real estate 2. Industrial goods and services 3. Retail 4. Construction and materials 5. Insurance 6. Basic resources 7. Food and beverage 8. Financial services 9. Technology 10. Travel and leisure |

Source: StoxPlus report (2013, 2014, 2015, 2016)

industrial goods and services (mainly packaging and delivery services) quickly became the focus of inbound M&A activity in the past two years. While not present on the top 10 list of 2012 and 2013, the industrial goods and services climbed to rank second in 2015 as an attractive investment destination. The average deal value jumped from the levels of around US\$54.6 million, US\$24.4 million and US\$56.9 million in 2012, 2013 and 2014, respectively; to US\$178.2 million in 2015. The average deal size fell in the 2012-2013 period, but then increased more than four times—from US\$2.71 million per deal in 2013 to US\$11.88 million per deal in 2015. Similarly, the retail industry, as well as the construction and materials industry, increasingly drew the attention of foreign firms. The retail industry was characterized by a fewer number of

transactions, yet larger value per deal. With two deals in 2013 and one deal in 2014, the retail industry attracted around US\$203 million and US\$879 million, respectively. Target companies are big brand-names in the Vietnamese market, including Vincom Retail, sTran Anh Digital World Jsc, Nguyen Kim, and Metro Vietnam. Meanwhile, there were more deals in the construction and materials industry, with a total deal value more than doubling in the 2014-2015 period (from US\$53.42 million to US\$109.1 million) despite a tremendous fall in the 2012-2013 period (from US\$587.15 million to US\$28.53 million). Finally, the food and beverage industry drew special attention from foreign investors with total deal value surging from a mere US\$75 million in 2012 to US\$561 million in 2013, with Masan as the main target company. However, in the

2014-2015 period, there was a slight decrease in inbound M&A value in this industry, decreasing from US\$620.8 million in 2014 to approximately US\$508 million in 2015 (StoxPlus Report, 2015).

Reformed legal framework for inbound M&A activity in Vietnam

The first and second wave of inbound M&As are often attributed to the legal framework reform, which aimed at creating more favorable playground conditions for foreign investors. The Law on Enterprises (LOE), passed in 2005, unified three separate regulations related to non-state-owned enterprises (Law on Enterprises, 1999), state-owned enterprises (Law on State-Owned Enterprises, 2003), and foreign-invested enterprises (Law on Foreign Investment in Vietnam, 1996), with the aim of providing more equal and favorable treatment to non-state-owned and foreign-invested sectors. Accordingly, procedures in setting up businesses were further simplified, and the time needed for approval of business registrations was further shortened. In addition, the Law on Investment (LOI) enacted in 2005 replaced two separate laws on investment, namely the Law on Domestic Investment Promotion, which regulated domestic investors and the Law on Foreign Investment, which regulated foreign investors. Like the LOE, the LOI attempts for equal treatment between foreign and domestic investors.

The LOI enacted in 2014 further eased the investment procedure for foreign-

invested enterprises (FIE's). Under LOI 2014, Article 36, FIEs with less than 51% foreign ownership are not required to apply for the Investment Registration Certificate (IRC) (they had to apply for IRC under LOI 2005). This can be interpreted as the FIEs with less than 51% foreign ownership are considered to be domestic companies. The requirement for share purchase of foreign investors and FIEs is likewise simplified. Foreign investors and FIEs purchasing shares of a company are required to register their share purchase only in two cases (Article 26, 2014 Law on Investment):

- (i) if the target company belongs to conditional industries applied to foreign investors, or
- (ii) if the share purchase turns the target company into an FIE with 51% or more foreign ownership

The foreign ownership cap in a listed company, which was 49% under Decree 58/2012/ND-CP, was removed. Decree No 60/2015/ND-CP, providing guidance on a number of articles in the Law on Securities, provided no limit on foreign ownership of listed companies².

The Vietnamese government's open policy for foreign investment was particularly highlighted in the real estate industry. In the Law on Residential Housing No. 56/2005/QH11 each foreigner, including a foreign organization or an individual, was only allowed to buy one apartment. To do so, the foreign entity had to satisfy a series of hard conditions such

² Decree 60, however, lists certain cases where foreign ownership will still be restricted, such as certain sectors under Vietnam's international treaties (e.g., Vietnam's WTO commitments); and sectors restricted to foreign investors under the Law on Investment and its implementing regulations. If specific foreign ownership limitations for such conditional sectors have not yet been set, the foreign ownership in such cases will be capped at 49%.

as long-term investment, management position, making a contribution to Vietnam, having a university degree or knowledge or special skills that Vietnam needs, being married to Vietnamese citizen, and so on. Additionally, the individual had to meet conditions that they were allowed to reside in Vietnam for 12 months or more, and with the organization with investment certificates valid for one year or more. Therefore, in practice, little was achieved with that scheme, as only approximately 126 foreigners have been able to successfully purchase an apartment since 2009.

The new Law on Residential Housing No. 65/2014/QH13 provides more favorable conditions for foreigners to purchase and/or own a house in Vietnam. Foreign individuals and institutions in the following three groups are entitled to own houses in Vietnam (Article 160, 2014 Law on Residential Housing):

- (i) Foreign individuals and institutions investing in residential housing projects in Vietnam;
- (ii) FIEs' branches and representative offices of foreign companies, foreign funds and branches of foreign banks operating in Vietnam (referred to as foreign institutions); and
- (iii) Foreign individuals allowed to enter Vietnam.

Those individuals and institutions can invest in housing construction

projects, purchase or lease apartments and houses with easier conditions. For example, the condition for those in the first and second groups is that they must have the IRC. The conditions applied to foreign individuals to be entitled to real estate property ownership is that they are permitted to enter Vietnam and not entitled to diplomatic privileges (Article 160, 2014 Law on Residential Housing)³.

FIEs have also been given land use rights since 2013. In the 2003 Law on Land, there are regulations on the transfer of land-use right from the government to individuals, households and economic organizations under three forms: transfer without collecting fees, transfer with fees, and leasing land. However, FIEs are not mentioned in those regulations. The 2013 Law on Land, however, clearly defines FIEs as one party receiving land-use right transfer from the government in two forms—transfer with fees and leasing land (Article 55 and 56, 2013 Law on Land):

- (i) FIEs can be allocated land with a land-use fee for the development of a housing project for sale, or sale and lease.
- (ii) FIE's can also lease land from the government for investment projects in agricultural, forestry, fishery, and salt-making industries; for conducting business manufacturing; for constructing public utilities; and for building residential housing for lease.

³ Restraints on the number of houses and the time of ownership are still available. For example, foreign institutions and individuals are entitled to own the maximum of 30% of the number of apartments in a building, and/or 250 individual houses in a residential area with population equivalent to a ward. Foreign institutions can own the apartment/house only within the validity time of the IRC and must transfer the apartment/house to the Vietnamese government if they do not sell or offer the house to other parties when the IRC expires.

Table 2. General Corporations in Vietnam

| | |
|--|---|
| Electricity Corporation of Vietnam | Vietnam Coffee Corporation |
| Coal Corporation of Vietnam | Vietnam Tobacco Corporation |
| Vietnam Petroleum Corporation | Vietnam Paper Corporation |
| Cement Corporation of Vietnam | Vietnam Textile and Garment Corporation |
| Vietnam National Shipping Lines | Northern Food Corporation |
| Vietnam Airline Corporation | Southern Food Corporation |
| Vietnam Post and Telecommunication Corporation | Vietnam Chemical Corporation |
| Vietnam Rubber Corporation | Vietnam National Gem and Gold Corporation |
| Vietnam Steel Corporation | Vietnam Railway Union |

Source: IMF [1998]

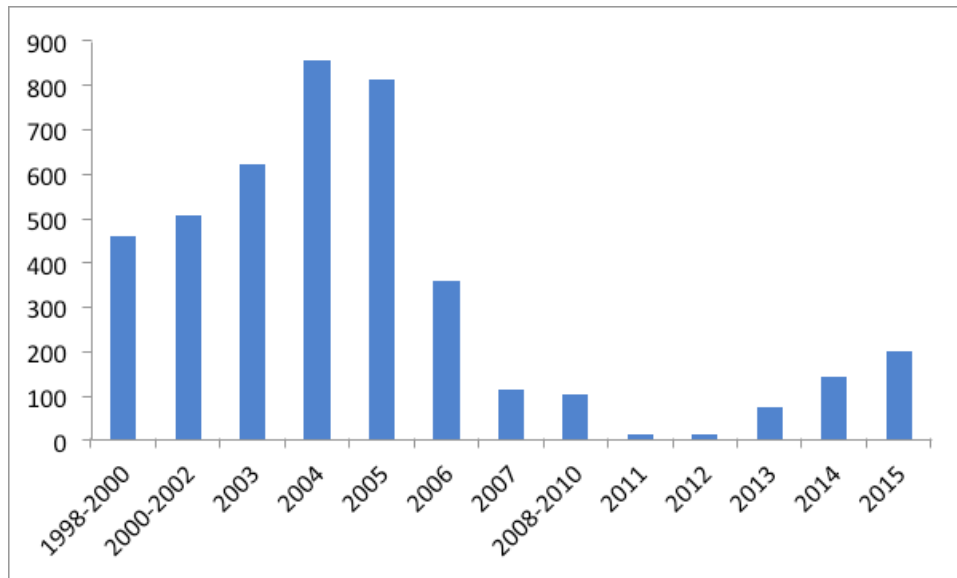
As indicated in section 4, the relaxing of regulations on residential housing and land-use rights may partly account for the increasing flows of inbound M&As in real estate, as well as the construction industry in Vietnam. The real estate industry attracted 20 deals with value up to US\$1.64 billion, which accounted for 69% of total inbound deal value for 2015; while deal value in the construction and materials industry more than doubled between 2014 and 2015 (StoxPlus Report, 2016).

Slow and sluggish SOE equitization process

Inbound M&As have been on a declining trend recently, especially, in the 2012-2013 and 2014-2015 periods. The opportunities for inbound M&A activity in Vietnam mainly stem from reductionism state ownership of former SOEs, also known as the equitization process (StoxPlus Report, 2016).

The SOE reform process started as early as 1992, six years after the landmark Đổi Mới Program was launched by the Vietnamese government. Many inefficient or loss-bearing SOEs were dissolved, reducing the number of SOEs from 12,000 in 1993 to 6,000 in 1995. From 1995 to 1996, nearly half of the remaining SOEs were grouped under 18 larger holding companies known as General Corporations (GCs), controlling essential commodities (see Table 2.1). The mission of these corporations was to reap benefits from economies of scale, to limit both monopolistic power and disorderly competition, and to conserve government administration. To the contrary, however, the GCs became highly monopolistic and conducted rent-seeking activities. This has led to reduction in the efficiency and autonomy of production decisions within individual firms (International Monetary Fund - IMF [1998]).

Foreign individuals are entitled to ownership of not more than 50 years, but this time can be extended.



Source: Data from 1998 to 2013 are taken from StoxPlus report 2014. Data for 2014 and 2015 are taken from Huong (2016)

Figure 4. Number of SOEs privatized via IPOs

The continuous integration of the Vietnamese economy into the world economy has created pressure to establish big companies that could compete with international corporations. As a result, while efforts were made to impose uniformity on the legislation governing all economic sectors, the role of SOEs was reinforced with the reforms conducted on GCs. In 2005, GCs were transformed into either parent-subsidary companies or Economic Groups (EGs)—big conglomerates that were expected to be internationally competitive⁴. While the GCs were reinforced with the new models, the equitization process continued to be conducted in small and

medium-sized SOEs. However, despite the equitization program, in many cases, the state still held the largest share of the equitized companies (Fredrik Sjöholm, 2006).

Equitization of parent-subsidary GCs and EGs has been gradually implemented in recent years, in correspondence with the requirement of the government for all GCs and EGs to complete their divestitures from non-core businesses (StoxPlus report, 2014)⁵. Non-core businesses mainly belong to banking and financial services, construction and materials, food and beverages, and electricity.

⁴ Under the parent-subsidary scenarios, the parent company was a business entity that controlled its subsidiary companies based on the level of investment of the parent company. A few GCs were transformed into EGs, which were diversified business groups that oversaw several parent-child model corporations. The EG approach was a way of integrating interrelated GCs and other companies. Member companies were allowed to diversify their businesses into areas outside their domain. (United Nations Development Program – UNDP, 2007).

⁵ Notable EGs in which the state divested from non-core businesses include Vietnam Airlines (airline industry), Song Da Corp (construction industry), Vinalines (shipping industry), Vinatex (textile and garment industry), Vinacomin (coal and mineral industry), Vinachem (chemical industry), VNPT (telecommunication industry) and EVN (electricity industry).

However, state divestiture from listed companies remained modest. Average state ownership in listed companies declined slightly from 36.06% in 2013 to 36.01% in 2014 (StoxPlus Report, 2015). In the equitized SOEs under the management of the Ministry of Industry and Commerce in 2011-2015, the state remained the controlling shareholder, with more than 90% share of ownership (Diep, 2015).

As indicated in Figure 4, the number of SOEs privatized via Initial Public Offerings (IPOs) between 2007 and 2015 dropped significantly compared to the previous period. The number of SOEs equitized from 2011 to November 2015 accounted for 75% of the equitization plan.

CONCLUSION

Research on cross-border M&A activity focused on Vietnam is scant. We provide a broad-based overview of the background and an examination on the legal framework governing M&A activities, as well as the equitization process of SOEs in Vietnam. While the changes in the regulatory environment along with Vietnam's steady and high economic growth rate are attributed to the influx of inbound M&As, especially in the real estate sector, the sluggish SOE equitization process can partly account for the recent declining trend in inbound M&As.

Plans are under way by our team to continue this stream of research rigorously by investigating several dimensions of cross-border M&A activities, including:

1. Assessing the impact of cross-border M&As on the company valuation (e.g., measured by stock

performance). This assessment would be done within a traditional event analysis framework, where we would look at:

- a. The immediate impact of M&A announcement on stock prices.
 - b. Comparing trends of performance before and after the announcement during a relatively short time horizon.
2. Investigating financial performance of the foreign entities involved in cross-border M&As in Vietnam in order to assess whether the strong interest in these activities by foreign companies is justified and is likely to continue into the future. This is particularly meaningful given the fact that the state remains the controlling shareholder in equitized companies. It is useful to know whether investing in such companies benefits the foreign acquirers.
 3. Compare both the short-term impact and long-term financial performance of cross-border M&As in Vietnam with those of the other emerging economies such as Thailand, Malaysia, Philippines, and Indonesia.
 4. Conduct a sectoral analysis of cross-border M&As to discover which industries are the highest-yielding industries for foreign companies to consider for M&A activity.

This preliminary concept paper is essentially the starting point, laying out the foundation for future research in this area.

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