Privatisation back on the agenda in Vietnam

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Published: January 30 2011 18:13 | Last updated: January 30 2011 18:13

Standing in front of a bust of Ho Chi Minh, Vietnam's late revolutionary leader, in November, two unlikely allies shook hands on a deal that could signal the way forward for the communist country's state-dominated economy.

Hans-Ulrich Doerig, chairman of **Credit Suisse**, and Nguyen Van Quynh, deputy head of the Communist party's commission for organisation, had just signed an agreement under which the investment bank would help train executives from Vietnam's manifold state-owned enterprises, or SOEs.

Credit Suisse's bridge-building with Vietnam's ruling Communist party probably has less to do with any ambition to move into corporate training and more to do with a desire to win advisory business as the country's long-stalled privatisation programme gets up and running again.

In recent weeks, two of Vietnam's largest SOEs – fuel distributor Petrolimex and flag-carrier Vietnam Airlines – have announced plans to complete **partial initial public offerings**, by the end of this year and the end of 2012, respectively. If these IPOs progress according to plan, other big and relatively well-run SOEs such as mobile phone operators Vinaphone and Mobifone, Vietnam Steel Corporation and the Bank for Investment and Development of Vietnam may follow suit.

The government's privatisation drive slowed to a crawl over the past four years during the global financial crisis and the corresponding collapse of Vietnam's burgeoning stock market.

The global market recovery since then, while steady rather than spectacular, has created more favourable conditions.

Despite achieving an average economic growth rate of 7 per cent a year over the past decade, Vietnam has suffered from **chronic macroeconomic instability**, with stubbornly high inflation, a weak currency and sizeable trade and budget deficits. Economists believe that government support for inefficient SOEs, which soak up significant amounts of state cash, has been a major cause of this turbulence. **The near-bankruptcy of Vinashin**, a large state-owned shipbuilder that in December defaulted on a $600m loan arranged by Credit Suisse, has increased pressure on the government to accelerate reform of SOEs, many of which are badly run and subsist on a diet of cheap government credit, preferential access to state land and monopoly market positions.

"If Vinashin had been privatised four or five years ago, we wouldn't be in the position we are today," says Andy Ho, managing director of VinaCapital, a fund manager that has invested in privatised companies.

While the government usually keeps controlling stakes when it "equitises" companies – a term the Marxist-Leninist party ideologues prefer to "privatisation" – analysts believe the process is a key element of SOE reform.

Privatisation is "very important" for Vietnam's SOEs, says Nguyen Quang A, a former government economic adviser, for all the well-known reasons; shareholders can hold the management to account and employees have a vested interest in the company's success. The added transparency of audit and financial reporting would impose discipline on management.

As well as selling shares to the public, some large, part-privatised SOEs such as insurer Bao Viet Holdings and lender Vietinbank have also benefited from bringing in strategic foreign investors. HSBC, which owns 18 per cent of Bao Viet, has supplied its Vietnamese partner with a number of mid- and senior-level executives who have helped improve efficiency through better risk management and IT systems.

However, Mr A warns that equitisation is only one part of SOE reform. "You also have to dismantle all the monopolies and let companies compete healthily in the market," he says.

It is a view shared by Jonathan Pincus, head of Harvard University's economics teaching programme in Ho Chi Minh City.

"It shouldn't just be about **selling a stake** in Vietnam Airlines but allowing other companies to compete by removing Vietnam Airlines' monopoly over fuel and other airport services," he says.

The Vietnamese government, which believes that the state must continue to play a leading role in the economy, is likely to proceed with caution.

A person close to Petrolimex says that while the independent valuation process has been completed, the government remains "very nervous" about the proposed IPO and will probably sell only a small stake initially.

In addition to retaining majority equity holdings, the government exerts control over SOEs by regulating pricing structures and forcing many companies to sell their products below cost, whether they are aircraft seats, petrol or electricity.

But if it is to attract more investors, the government will have to relax this “belt-and-braces” approach.

Mr Ho says the willingness of VinaCapital and other large investors to participate in the upcoming IPOs will ultimately depend on the government’s agreeing to realistic valuations.

The **recent experience of Indonesia’s state-owned airline**, Garuda, which had to scale back its IPO after the high valuation put off many foreign investors, suggests this will not be an easy process.