Lifting the last bamboo curtain

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Hanoi now seems keen to restart its privatisation plans, following the Vietcombank offering in late December

Vietnam is a country of contrasts, a place that does not easily lend itself to easy assumptions or causal categorisations. In the West there is a tendency to treat South East Asia as homologous – what goes for Thailand will apply to Vietnam and Cambodia. And China leads with commodious coat tails.

But scratch beneath the surface and it is apparent that such casual thinking is at best misguided. The liberalisation of the Vietnamese economy, announced with fanfares at various points since 1986 is obvious to any Westerner wandering the streets of Ho Chi Minh City. Shops are well-stocked with contemporary goods, street vendors offer an array of foods, drinks, jewellery, haircuts and other services you would expect in a city of 8 million inhabitants.

But the Vietnamese government retains strict controls over the levels of foreign ownership of Vietnamese businesses, and in certain sectors state-owned virtual monopolies dominate domestic markets, access to which is restricted to foreign competition.

And Vietnam is of course one of the last communist one-party states. While it has not experienced the rapid liberalisation and retrenchment that China experienced as it opened itself to the outside world, more cynical observers may suggest that this is simply because while the government has proved adept at announcing the opening-up of particular sectors to foreign competition and investment, it has proved equally adept at ensuring progress is measured on a gastropodian calendar.

There is caution too at senior level. It is important not to forget that the fighting associated with WWII effectively ended for the country in 1975, after wars of independence with both France and the USA. Nor is it always easy having China as your next-door neighbour. When Admiral Zheng He set out on the first of his seven historic voyages from China in 1405 in an armada of 318 ships to establish Chinese trade with India and Africa, his first port of call was in Champa, the ancient name for southern Vietnam. Despite describing the area as "notorious for pirates and slavers", it is recorded that his ships were loaded with "ebony, black bamboo and aloe wood [from which incense was made]". His return visit was to sack the port. Border disputes continued thereafter. Vietnam and China in the 1980s and 1990s maintained large standing armies on their common border, and to this day there are disputes over mineral rights in the seas offshore.

With 88 million citizens, 58 per cent of who lived in poverty in 1990 down to only 8 per cent now according to WHO figures, Vietnam has experienced tiger economy growth writ large – averaging over 8 per cent over the last ten years. According to Peter Ryder, managing director of Indochina Capital, a foreign investment specialist with extensive experience in South-East Asia, much of the explosive growth Vietnam is experiencing is consumer-fuelled. "GDP is US$60 bn, and consumer spending accounts for nearly US$34 bn of that." Coralline Clarke, COO of SGMR, a travel agency specialising in trekking and adventure holidays in the region, also reports increased spending from non-Western customers. "Part of our business is motorcycle rental, but we increasingly encounter Vietnamese customers using the equipment as part of their business, or even just for mucking around. There is more disposable income than even five years ago." But with average GDP per capita at US$723 in 2006, spare cash is a relative term.

GDP growth in 2006 was 8.2 per cent, driven largely by construction, processing industry, retail trade and the tourism, hospitality and transport sectors. Economic development has been patchy geographically. Ho Chi Minh City and the surrounding provinces constitute the power-house of economic development, with GDP per capita reaching nearly US$2,000. Since 2000,

Vietnam's economy is moving from local to national to global

Vietnam's Enterprise Law has fostered the creation of over 200,000 registered private domestic enterprises, accounting for around 10 per cent of the economy and a smaller proportion of the labour force. Over time, the new Enterprise Law (2005) and Investment Law (2005), which came into effect in July 2006, should gradually contribute to an improved business environment and a more "level playing field" in all economic sectors.

As part of its effort to maintain the momentum in foreign direct investment, Vietnam has undertaken an equitisation (semi-privatisation) programme for its state-owned enterprises (SOEs), aiming to complete the programme by 2010, leaving around 550 enterprises fully in state hands. However, while the government planned to reduce the number of SOEs to around 2000 by 2005, there remained 2176 enterprises unequitised by August 2006 (Source: State Committee for Enterprise Reconstruction and Development).

The state also continues to maintain controlling shares in large number of enterprises following equitisation. This, combined with the technical challenges associated with valuing an SOE's assets to prepare for sale, has to date limited the positive impact of equitisation on FDI inflows.

In late December 2006, the Vietnamese government released a new and ambitious plan to extend the equitisation process to larger SOEs in sectors such as banking, insurance, aviation, cement, steel and textiles. Implementation will be challenging, but the intention behind the plan is encouraging from both a domestic and international perspective.

The Economist Intelligence Unit forecasts that real GDP growth for the period from 2007-11 will be in the range of 7.1 to 7.8 per cent, although the Government has set an ambitious target of 8.5 per cent. The World Bank and IMF also expect growth over the period to average close to 8 per cent.

Goods and services exports now constitute over 70 per cent of GDP, well more than double the 30 per cent share recorded in the mid 1990s. Crude oil alone accounted for 21 per cent of total merchandise export revenues in 2006. Other major export items include textiles, garments and footwear, seafood, timber products, rice, rubber, coffee, cashews, pepper and coal.

Ryder describes the Vietnamese market as "uncorrelated" to the global market, meaning that the trials and tribulations of the world's capital markets have left it relatively unaffected. Personal debt levels are low, and cash remains the predominant method of completing a transaction, whether in the market or buying a property.

Cash is also behind the burgeoning leisure and recreation industries. Aside from tourism, the government is in the process of relaxing the gambling laws, and among the international companies shortlisted to run a fixed-odds gaming licence as a joint-venture is UK giant Ladbrokes. The betting firm last year announced plans to invest US$60 million in Vietnam if moves to legalise football betting transpire. The government is considering lifting a ban on betting to raise funds for sports training and infrastructure and to regulate the current illegal betting in football, particularly English Premier League games.

Other firms have been working in Vietnam on a less conspicuous level for years. Theodore Alexander manufactures furniture and household furnishings for worldwide sale through outlets including Harrods, in a modern factory outside Ho Chi Minh City. Founder Paul Maitland Smith moved his manufacturing operations there after realising that the Government commitment to foreign investment was genuine. "As a foreign investor, you're welcome here," he says. "They do everything they can to make it easy. That is different from some other countries in Asia."

Labour costs are also about half those in the developed coastal industrial zones of China. And the workforce is educated and eager to learn. "They're very quick learners," said Antony Maitland Smith, Paul's nephew, and president of the company. "It's a highly skilled workforce and there's a tradition of fine hand-eye skills in this country. The only problem is industry

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Vietnam is well placed at the heart of Asian regional sea routes

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is growing so rapidly that the labour pool is shrinking." The company has more than 4,000 employees in Vietnam, and has received a number of accolades for the quality of its employment practices.

Exports of wood furniture rose by nearly a quarter last year, and earned Vietnam more than US$1 billion in export revenues. Footwear sales to the UK earned a further US$382 million and clothing US$141 million. While small change in comparison to the US$24 billion earned from the rapidly developing oil sector (see Oil & Gas article), the figures show an economy moving away from reliance on basic agricultural towards what has been described as a "global economic workshop competing directly with China".

In the finance sector, Vietnam's state-owned Vietinbank (formerly Incombank), one of the country's big four state lenders, plans to proceed with its partial privatisation (or equitisation) this year, when it aims to sell a 25 per cent stake to the public.

If the Government approves the plan, Vietinbank will be the second large state-owned bank to auction shares to the public, after Vietcombank raised US$652 million last December.

Pham Huy Hung, the bank chairman, told the Vietnam Economic Times newspaper that Vietinbank would apply for official approval of its share sale plan by this month at the latest. Vietinbank would have assets of about US$11.2 billion at the time of the initial public offering, and its bad loans accounted for less than 1.3 per cent of total lending, Mr Hung was quoted as saying. He said Vietinbank would select a foreign strategic partner after the IPO had taken place.

The Government approved banking reform roadmap also includes moving the State Bank of Vietnam (SBV) towards only two functions: monetary policy and supervision. This importantly complements the plans to equitise the largest state-owned commercial banks, which the SBV currently both regulates and 'owns'.

The Government last summer temporarily put the brakes on its ambitious plans to sell off stakes in large state enterprises because of concern about stock market doldrums, and fears that a potential glut of new shares would further depress the market.

Hanoi now seems keen to restart its privatisation plans, following the Vietcombank offering in late December. Since then, Saigon Beer Alcohol Beverage, one of the country's largest beer breweries, has announced plans to raise at least US$557 million by selling a 20 per cent stake. The authorities have also granted permission to Hanoi Beer Alcohol Beverage, another large brewery, to list.

Vietnam's stock market has temporarily lost its lustre. Analysts say this is partly because of policy decisions, which are constricting the flow of funds into the market. Banks, which previously had almost no restrictions on lending for the purchase of shares, were required to pare back their stock market loans by the end of 2007 to no more than 3 per cent of their total portfolios.

Some observers argue that foreign investors have had difficulties acquiring the local currency they need to buy Vietnamese shares, because of foreign exchange restrictions.

Kevin Snowball, a partner of PXP Vietnam Asset Management, said: "Foreigners aren't able to get sufficient cash into the market now to buy at levels that they have consistently felt was cheap." The stock market, which ended last year up 23 per cent, is down 4.3 per cent this year.

In the telecoms sector, Vietnam represents one of the last untapped markets for international mobile phone operators. Vodafone, the world's largest mobile group by revenue opened an office in Hanoi in June, so that it can track privatisation plans.

"Vodafone's interest in a potential stake in a Vietnamese mobile operator is at a very early stage," says a company spokeperson. "We have opened the office in Hanoi to monitor the situation."

Only a quarter of the population have mobile phones, and industry sources estimate that take-up will double in the next two years. It is also widely assumed that the Ministry of Post and Telematics will move swiftly with the privatisation of VinaFone and MobiFone, two of the countries largest mobile companies, when approval is received from the authorities.

So the potential for domestic and inward investment is considerable. Apart from protection afforded the large number of SOEs, and a 30 per cent cap on foreign ownership in unlisted equitised SOEs, the main limits on trade and investment are: high average tariffs; complex foreign investment and taxation laws; problematic levels of corruption, especially in infrastructure projects; the underdeveloped state of the financial system; and increasingly strained infrastructure, and consequent high transport, power and telecom costs.

It is clear that the Vietnamese Government is gradually loosening current foreign investment limits, for example, by raising the listed company foreign ownership limit to 49 per cent. The legal system is also undergoing major change to better align commercial statutes with international norms. The implementation of WTO commitments will also gradually contribute to a better operating environment as tariffs are cut and investment restrictions lifted. But it will be some years before this process bears fruit.

Vietnam has many economic strengths, not least the skills and entrepreneurial abilities of its young workforce. However, the risk that the bureaucratic and administrative structures will not be able to keep pace with the rapidly growing sophistication of the economy ensure that the country will have to continue to work hard to maintain current high growth rates over the long term. F