Corporate Governance in Vietnam

SUCCESS STORIES

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Prepared by

Centre for
Asia Private Equity
Research Ltd

IFC International Finance Corporation
WORLD BANK GROUP

Contents

Foreword

Corporate Governance Success Stories in Vietnam was prepared by Centre for Asia Private Equity Research Ltd. under the auspices of the International Finance Corporation (IFC), in partnership with the Swiss government's State Secretariat for Economic Affairs (SECO).

The active participation and support of the IFC, Dragon Capital and Mekong Capital were central to the preparation and completion of this report. This report is a testament of their commitment to champion for best corporate governance practices in Vietnam.

About IFC

IFC, a member of the World Bank Group, is the largest global development institution focused exclusively on the private sector. Working with private enterprises in about 100 countries, we use our capital, expertise, and influence to help eliminate extreme poverty and boost shared prosperity. In FY14, we provided more than $22 billion in financing to improve lives in developing countries and tackle the most urgent challenges of development. For more information, visit www.ifc.org.

About Asia PE Research

The Centre for Asia Private Equity Research Ltd. ('Asia PE Research'), established in 1991, is an independent Hong Kong-based organisation that focuses on providing information of the Asian private equity investment industry. Asia PE Research provides data, incisive insights and performance benchmarks to leading global investors to help them evaluate investment decisions into Asia's private equity markets.

Objective

Corporate Governance Success Stories in Vietnam is part of the International Finance Corp.'s ongoing efforts to raise greater awareness of the merits of corporate governance. These success stories in Vietnam can serve as a guiding light for the immediate benefit and long-term value of corporate governance to corporate development.

Ho Chi Minh City Securities Corp. and Mobile World Investment Corp. stand out as exemplary models of corporate governance, among portfolio companies managed by private equity investment firms in Vietnam. The managements of both have demonstrated their commitment to pursuing best corporate governance practices. In ensuring absolute alignment of their interest with shareholders, the boards of these two companies instituted a series of measures such as management control, board effectiveness and high level of transparency that can serve as model templates for other companies to follow.

The extensive and positive impact felt by both Ho Chi Minh City Securities Corp. and Mobile World Investment Corp. after implementing best corporate governance practices can serve as a valuable reference for all those who seek sustainable business development.

Introduction

Corporate Governance in Vietnam

The Law on Enterprise 2005, implemented in July 2006, marked the first introduction of a formal legal framework on corporate governance ('CG') in Vietnam. Currently, listed companies in Vietnam are under the framework of the following principal laws and regulations –

- Law on Enterprise 2005, with the revised Law on Enterprise 2014 effective from 1st July 2015
- Law of Securities of 2006
- Corporate governance code 2007 and Amendments 2012
- Disclosure Rule 2012
- Listing rules of the Ho Chi Minh and Hanoi stock exchanges

CG practice in Vietnam is expected to undergo sweeping changes when the revised Law on Enterprise 2014 ('LOE 2014') comes into effect on 1st July 2015. The revised LOE 2014 ensures independence of the Board of Directors, seeks to eliminate conflict of interest and to improve accountability as part of Vietnamese government's drive to ensure better CG.

The following are the key changes of the revised LOE 2014, largely applicable to joint stock companies ('JSCs'), compared with the Law of Enterprise 2005.

Law on Enterprise 2014 *(effective from 1st July 2015)*	Law of Enterprise 2005
Terms of Management A maximum 10-year tenure in total for someone who can serve as Chairman, members of Board of Directors, Supervisory Board members and other key management roles.	No such a restriction.
Management & Operation Models JSCs may select either one of the following models – a) A General Shareholders Meeting, a Board of Directors, a Supervisory Board and a CEO. b) A General Shareholders Meeting, a Board of Directors, and a CEO with the following caveats applicable to Board of Directors – i. At least 20% of the members must be independent to oversee and organise implementation of control over management and operation of the company. ii. An Audit Committee under it.	Only model a) was applicable for JSCs.
Reduced Quorum and Voting Requirements • Required quorum for a General Shareholders Meeting ('GSM') of a JSC for the first and second attempts are reduced to 51% and 33% respectively. • GSM requires a 51% vote for ordinary matters and 65% for certain key matters. • The reduction of both quorum and voting requirements bring Vietnam's Law on Enterprise more in line with many established jurisdictions.	• **Required Quorum:** 65% and 51% for first and second attempt, respectively • **Voting Requirement:** 65% and 75% approval required for ordinary and key matters, respectively.
Public Disclosure on Related Persons' Holdings Chairman, CEO, legal representative, Supervisory Board members and other management personnel must notify the company if he/she owns interest in other companies and if their related persons hold 10% or more in other companies.	The required percentage for disclosure was a 35% ownership for related persons.
Reduced Large Transaction Threshold For JSCs, investment decisions or asset disposals that value at 35% or more of the company's total value of assets, approval by GSM is needed.	Large transactions that command 50% of the company's assets needed GSM's approval.
M&A Activities Enterprises of different legal entities may enter into a merger, that encourages more flexibility in acquisition activities.	Only among corporate entities of the same type of companies may be merged.
Simplified Administrative Procedures • Business lines are no longer required to be stated on the Business Registration Certificate ('BRC'), thus no amendment is required when a company needs to change its business activities. • Multiple legal representatives are allowed which brings more flexibility to companies.	• Amendment of BRC is needed for business change. • Only one legal representative.

Based on the latest corporate governance assessment conducted by Asian Development Bank in 2013, which surveyed 529 companies in Southeast Asia, it noted that Vietnam has made marked improvement with corporate governance. It is encouraging that the CG mean score for Vietnam in 2013 has risen by 19.2%, compared to that scored in 2012.

Executive Summary

Ho Chi Minh City Securities Corp. ('HSC')

Business	Brokerage & Corporate Finance Services
Private Equity Investor	Dragon Capital
Major CG Changes	• Expanded board with an increase in both the number of independent directors and non-executive directors to ensure objectivity and independence of the board. • A formal risk management department has been established with the appointment of chief risk officer; and a professional firm has been invited to undertake an Enterprise Risk Management project. • Active communication with all stratum of management being encouraged. • Standalone internal audit which is headed by a director who is closely involved in the management's investment decision has been formed. • Decision making is guided by Limit of Authority guideline to ensure approval process is in alignment with the company's policy.
Impact of Improved CG	• Market share from the lowest quartile in 2007 to being the second largest securities firm in Vietnam. • Increased awareness of risk management. • Improved ability to retain talents and reports one of the lowest turnover rate among its peers. • Among the best performing stocks in Vietnam's securities industry.

"As the securities sector is a relatively new industry in Vietnam... and with a "trial and error" legal framework, it remains challenging to instill the concept of best corporate governance practice in the face of unfair competition."

Mr Johan Nyvene,
CEO of Ho Chi Minh City Securities Corp.,
11th Feb 2015

"Primary objective of many companies is to focus on profit rather than best CG practice ... CG practice may not be getting sufficient attention from companies in Vietnam."

"... remedies and enforcements (of CG) have not been strong enough to discourage lack of compliances."

Mr Le Anh Minh,
Director of Dragon Capital,
11th Feb 2015

Mobile World Investment Corp. ('MWG')

Business	Mobile Phone Retailing
Private Equity Investor	Mekong Capital
Major CG Changes	• Enhanced and diversified board with regular monthly meetings and clear agenda; introduction of an independent director with retail industry expertise. • Conflict of interest eliminated with founders divested from most side businesses. • Monthly revenue and gross profit report and store information has been developed that provides operational transparency. • New human resources director was recruited to develop corporate culture.
Impact of Improved CG	• Market position improved from 3% market share in 2007 to 30% by 2014. • Easier access to bank loans at lower interest rate. • Improved operational efficiency and achieve milestones earlier than target date. • Substantial revenue and net profit growth.

"MWG continually refined its execution during its 10-year life. The knowledge the company accumulated, and its orientation to continuously improve are its primary advantages over the other chains."

Mr Anh Nguyen,
Analyst of CIMB Securities,
11th Jan 2015

"There ought to be quarterly corporate governance checklist undertaken by private equity investors. If warning signs reach a certain point, investors must follow up and escalate the issue to first board and then shareholder meetings."

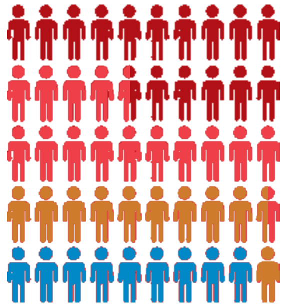
Mr Chris Freund,
Partner of Mekong Capital,
12th Feb 2015

Business : Provides brokerage, margin lending and corporate finance services in Vietnam
Location : Ho Chi Minh City
Sector : Brokerage and securities
2014 Revenue (Yr Growth) : VND831.1 billion (US$39.3 million)(+30.9%)
Type : Publicly-traded (Vietnam)
 # Employees – 2014 : 382
 # Branches & Transaction Offices – 2014 : 8

Ho Chi Minh City Securities Corp.

Ownership Profile (Dec/2013)

Dragon Capital: 30.9%
Ho Chi Minh City Finance and Investment State-owned Company ('HFIC'): 29.5%
Other shareholders – domestic: 21.5%
Other shareholders – foreign: 18.1%



Ho Chi Minh City Securities Corp. ('HSC'), founded in 2003, is a leading securities brokerage firm based in Vietnam. It provides a wide range of financial services to both retail and institutional investors. Since 2009, HSC has been listed on the Ho Chi Minh City Stock Exchange ('HOSE').

HSC counted the state-owned Ho Chi Minh City Finance and Investment State-owned Company ('HFIC') as its founder. At HSC's inception, it had an initial capital base of VND50 billion (US$3.3 million). Dragon Capital, which is among the oldest and most committed investment firms in Vietnam, became HSC's investor in 2005.

In 2007, at the advent of the global financial crisis, HSC underwent extensive structural overhaul. A new chief executive officer and a number of managing directors, with specific responsibilities assigned to each of them, were appointed. By 2010, HSC's unfaltering advocacy to corporate governance was rewarded. It ranked third in Vietnam's brokerage market and by 2012, HSC ascended to be the number one securities firm in Vietnam and held that position for two years in 2012 and 2013. HSC's market share ranking fell to the number two position in 2014. It is now one of the leading brokerage firms on both HOSE and Hanoi Stock Exchange ('HNX') with a combined 10.6% market share for 2014. Its 2014 profit after tax, which reached VND376.2 billion (US$17.8 million) is the highest since its inception.

Why Change?

Despite having HFIC as a founding shareholder and a name that is representative of the country, in 2007 HSC was ranked 26th out of around 30 securities companies in Vietnam, with a market share of only 3.5%. When Mr Johan Nyvene took office as the new CEO in 2007, HSC was not only losing its market share but was also unable to retain its employees.

HSC encountered a major setback during the global finance crisis in 2008. In that year, it reported the first plunge in profit after tax since its inception, from VND132.1 billion (US$8.4 million) in 2007 to VND23.5 billion (US$1.4 million) in 2008, more than an 80% drop. The adverse macro business environment coupled with difficulties facing its own operation, have thus led HSC's management to implement comprehensive changes. The goals went beyond just to improve HSC's risk management, but also to implement leading corporate governance practices.

What did they change?

The changes in HSC were extensive. The number of board members has increased to 7, from 5 before and the number of independent directors has also increased. The most significant changes included a formal risk management committee, a standalone audit committee that reports direct to the board as well as active and constant communications with all level of management.

Summary of Key Changes: HSC

	Key Challenges	Key Changes
Board Effectiveness	**Composition & Independence:** 5 members with 1 independent member, and the board mainly comprised representatives from two largest shareholders, Ho Chi Minh City Finance and Investment State-owned Co. and Dragon Capital.	**Composition & Independence:** The board was expanded from 5 to 7 members and the number of independent directors has increased from 1 to 2; while non-executive members have increased from 4 to 5 to ensure objectivity and independence. In addition, a previous director at HSC was appointed to head the board as an independent and non-executive chairman.
Management Control	**Risk Management:** No dedicated department to focus on risk management, which was managed without formal procedures to factor in inherent risks facing the securities industry including market, liquidity, credit, operational and regulatory risks.	**Risk Management:** A series of risk management procedures have been adopted since 2009 with the chief operating officer focusing primarily on risk management and operational enhancement. By 2012 and 2013, HSC had established a formal risk management department, and appointed a chief risk officer at the managing director level. HSC also set up the Risk Management Committee at the board level, and invited a consultant to undertake a firm-initiated Enterprise Risk Management ('ERM') project. The ERM project has evolved into the Business Process Improvement project and ultimately led to the initiation of the Business Process Management project.
	Communication & Operational Transparency: The diversity of HSC's staff body created communication problems, especially with foreign nationality employees.	**Communication & Operational Transparency:** Active communication promoted with all stratum of management, with monthly meetings among the senior management, weekly meetings among middle ranking managers (conducted by the CEO and/or the COO), and quarterly briefing sessions with the rest of the employees. In particular, the CEO conducts monthly lunch with employees.
	Internal Audit: The Internal Audit Committee did not have a clear reporting procedure to the board and there was no standalone Internal Audit Department.	**Internal Audit:** Formed standalone Internal Audit and headed by a newly hired director level person. Internal Audit engages the CEO on findings and occurrences in policies and procedures, as well as progress of internal audit projects.
	Decision Making: Lack of a formal approval process in the investment process of company.	**Decision Making:** Established Limit of Authority guideline to address the issue.
	Incentives to Employees/Talent: Difficult to maintain talents as HSC followed a SOE-based salary framework.	**Incentives to Employees/Talent:** New CEO proposed a 100% increase of salary for a large number of employees at that time. In addition, a recurring Employee Share Option Program was launched that led to a relatively low turnover rate.
Disclosure & Transparency	**Information Transparency:** Lack of formal procedures with regard to investor relations activities and disclosure schedule.	**Information Transparency:** Set up formal procedures to ensure timely and accurate update in website, investor relations, and holds quarterly analyst conferences to update and discuss business results. HSC has also established various channels to provide information directly to shareholders via a regularly updated database system.

Impact Report: HSC

In the eight years since HSC's new management team took office in 2007, with the goals to implement leading corporate governance practices, HSC has been able to demonstrate the following positive results –

- **HSC's market share increased and has advanced to become the leader in its industry.** When Dragon Capital first invested in HSC in 2005, the company was ranked 26th out of 30 securities companies in Vietnam and was losing its market share. Following appointment of a new CEO in 2007 and substantially improved its corporate governance, by the beginning of 2012, HSC was the leading brokerage firm in both Ho Chi Minh City Stock Exchange and Hanoi Stock Exchange, with 12.1% market share in the country. It is now ranked as the number two firm in Vietnam's securities industry.

- **Sharply increased awareness of risk management.** The Enterprise Risk Management Project, initiated in 2012 has helped HSC to formulate standard corporate risk management structure to address various kinds of risks. As a result, awareness of risk management has improved substantially across all business lines.

- **HSC's ability to retain talents has improved substantially.** The Employee Stock Ownership Plan programme that was launched in 2007 has been an effective tool to retain talents and enhance employee engagement. HSC's stellar reputation as the number one securities house along with this programme have helped retain talents and reported one of the lowest turnover rates among its peers.

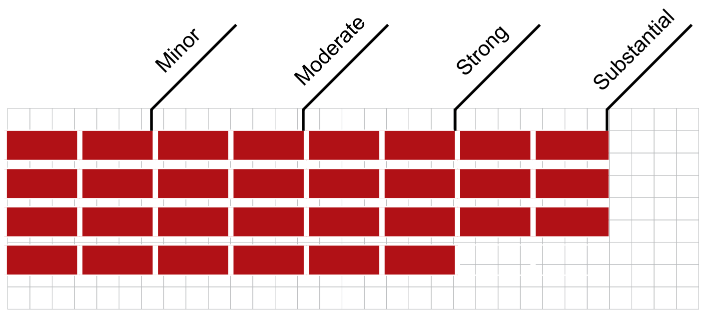
- **HSC's shares outperform VN-Index.** In the six years since HSC was listed in May 2009, HSC's share price has consistently outperformed the VN-Index by a far margin. While the VN-Index has risen by around 48%, that for HSC has surged by around 130%.

- **HSC's ROE leads its peers.** In 2014, HSC reported a 16.3% return on equity ('ROE') and 10.8% return on asset ('ROA'), both ranked top among HSC's peers in the securities industry. In fact, HSC's ROE and ROA ratios improved substantially in the five years from 2010 to 2014.

Impact Scoreboard

Qualitative Indicators

Board Effectiveness
Organizational Efficiency
Management Control
Access to Capital



Quantitative Indicators

	2006	2007	2010	2011	2012	2013	2014
Revenue	119.7	230.5	470.8	480.5	562.4	634.8	831.1
Net Profit	91	132.1	182.3	194.4	246.4	282.2	376.2
Reputation (Market Share)		3.5%				12.2%	10.6%
Share Price Performance			(48%)	(53.2%)	54.3%	13.4%	27.3%
Company Valuation (Year-end)			1,794	1,398	2,178.3	3,117.8	3,970.4

All amounts in VND billion except market share and share price performance.

Business : Mobile phone retailing
Location : Ho Chi Minh City
Sector : Consumer goods
2014 Revenue (YR Growth) : VND 15,756.7 billion (US$735.6 million)(+65.9%)
Type : Publicly-traded (Vietnam)
 # Employees – Feb/2015 : 9,822
 # Branches – Feb/2015 : 369 Thegioididong.com stores and 22 Dienmay.com stores

Mobile World Investment Corp.

Ownership Profile (2006, before Mekong Capital's Investment)

Founding Shareholders: 100%

Ownership Profile (Feb/2015)

Founding Shareholders: 40.6%
CDH Investments Ltd.: 12.2%
Mekong Capital : 11.6%
Mutual Fund Elite: 6.9%
NT Asia: 5.5%
Employees & Other Shareholders: 23.2%

Mobile World Investment Corp. ('MWG') was founded by five entrepreneurs in 2004 and is a mobile phone retail chain. Within three years, in 2007, MWG had established five stores in Ho Chi Minh City and chalked up a sale record of 10,000 phones per month. In order to accelerate growth, MWG invited Mekong Capital as a financial partner which has invested US$3.5 million in MWG for approximately 32.5% stake. In July 2014, MWG was listed on the Ho Chi Minh Stock Exchange.

Since enlisting Mekong Capital as a financial partner, MWG has worked closely with Mekong Capital and implemented a series of measures to improve management reporting and bonus systems, among others. MWG's financial results are testimonials to the benefits of corporate governance. When Mekong Capital invested in MWG, the company only held less than 3% market share of Vietnam's mobile phone retail market. By 2011, MWG has firmly established itself as the leader in its home market.

In the years since Mekong Capital invested in MWG, from 2006 and 2014, the company's net revenue has increased by more than 45 times to VND15.8 trillion (US$735.6 million) while its net profit surged by more than hundred times to VND668 billion (US$31.5 million). When MWG was listed in mid-2014, its market value stood at VND4.3 trillion (US$201.1 million); and it reached the US$500 million mark in September 2014, ahead of 2015 target stipulated by Mekong Capital.

Why Change?

Despite the fact that MWG was a profitable company before Mekong Capital invested in 2007, the company has always set the high goal to position itself as a value-added retailer. The company aims at moving from a traditional retail structure, which is organized around core functions (Merchandising, Supply Chain and Stores), to an integrated model built around the customer. Founded by five entrepreneurs who were used to having constant dialogues with each other, prior to Mekong Capital's investment, these founders represented the board. There were no third party and/or independent directors to provide third party opinions. The governance of the board was therefore loose. For MWG to move forward to be a key player in the market, changes were critically important.

What Did They Change?

Since Mekong Capital invested in MWG in 2007, the corporate governance structure began to take shape. The ad hoc meetings among the founders of MWG changed into regular monthly meetings, with clear meeting agenda and active participation by other members was encouraged. To eliminate conflict of interest, founders had all divested their side businesses [1]. At the same time, family members of the founders were no longer employed without adhering to a set of guidelines and strict restrictions on relatives not reporting to each other. The most significant change was the introduction of an outside expert. In 2012, an international expert from a leading multi-national technology retail company was brought in, not only as an independent board member, but also to provide retail expertise.

[1] One of the five co-founders continued to invest in start-ups. Eventually he stepped down from the board of MWG and is the only one of the five co-founders who is not currently on the board or Inspection Committee.

Summary of Key Changes: MWG

	Key Challenges	Key Changes
Board Effectiveness	**Composition:** Comprised six board members, one from Mekong Capital and five founding shareholders. No independent board member to provide third party opinions on the management of the company.	**Composition:** Representative of Mekong Capital became a member of MWG's board. The changes were most extensive in 2013, with the number of board members increased from six to nine. making the board much more diversified. Of the nine, four were founding shareholders, two non-founding executives; and three independent directors. In the latter, it included a retail expert and representatives from both Mekong Capital and CDH Investments.
	Procedures: There were unstructured board meetings, which lacked focused, in-depth discussions of strategic issues.	**Procedures:** Five meetings per year were held since Mekong Capital invested in the company, with active participation from a range of members. The board meetings have a clear agenda.
	Conflict of Interest: Some of the founders, who sat on the board, had side businesses. Family members of the founders were employed.	**Conflict of Interest:** Founders divested from most side businesses. One of the board members, who decided to focus on its other businesses, resigned from the board of MWG.
Management Control	**Management Structure:** No third party representatives and instead the five founders represented the management.	**Management Structure:** A retail expert was brought in as a consultant and non-executive director to provide international best industry practices in all the major business activities.
	Financial Management: No structured process.	**Financial Management:** Monthly revenue and gross profit report by region/category as well as store information, subsequently to include brand and category, management reporting template was developed, with strategically-important operational KPIs and provided to the board monthly.
	Human Resources: No human resource director.	**Human Resources:** Recruited key managers to support the growth of company. Apart from managers in sales development, and marketing, a new human resource director was recruited to develop corporate culture. He is also a member of the board.
	Key Person Risk: The five founders were sole decision makers on MWG's corporate strategy and operations.	**Key Person Risk:** All independent directors, and representatives from Mekong Capital and CDH Investments also participate in strategic decisions.
Disclosure & Transparency	**Disclosure:** Meetings were held on ad hoc basis, unstructured and no real discussions.	**Disclosure:** Monthly meetings, thorough background notes with clear agenda.
Family Governance	**Family Governance:** Family members of the founders were employed in the company and there was no compliance regulation regarding this.	**Family Governance:** A clear set of compliance regulations with respect to employment of staff relatives was introduced.

Impact Report: MWG

The year 2015 marked Mekong Capital's 8th year of partnership with MWG. After a period of gradual adaptation of corporate governance code, MWG recognises the benefits –

- **MWG's market shares has increased and advanced to be among the leaders in its industry.** When Mekong Capital invested in MWG in 2007, the company held less than 3% market share of mobile phone retail in Vietnam. By December 2014, according to GfK's report, MWG's market share has reached 30% by December 2014. Its largest competitors in 2007 have both subsequently disappeared.

- **MWG's access to bank loans was easier and at a lower interest rate** than that incurred by other local private companies, thanks to its strong business performance over the years, resultant from an effective Board of Directors and effective management control, and regular auditing by a Big-4 auditor.

- **Enhanced management control of the company through a disciplined management reporting process.** The monthly report that tracks key strategic and operational metric developed in 2011 has helped MWG's data-driven decision-making process. With a much more efficient tracking system, MWG's inventory days have been reduced from 55 days to 43 days in the period 2012 – 2014.

- **Board discussions and decision-making is significantly improved.** The board now meets five times per year with active participations by a range of members. The meeting agenda is clear with thorough background notes, that lead to open and candid deliberations before decisions are made.

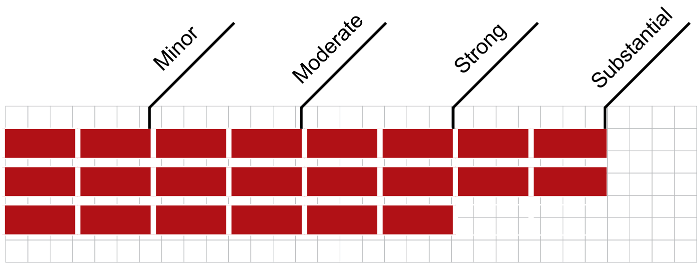
- **MWG was able to report envious growth, in both revenue and net profit.** In particular, MWG's net profit has been able to grow at a faster rate than its revenue, suggesting the company is generating profit more efficiently.

- **MWG boasts operational efficiency.** In 2008, Mekong Capital set a goal for MWG to open 50 stores and to reach a US$100 million valuation by 2013. MWG achieved the goals by 2011, two years ahead of schedule. The goal was then lifted to reach US$500 million by 2015 and MWG was able to achieve this goal post by September 2014, well before the target date.

Impact Scoreboard

Qualitative Indicators

Board Effectiveness
Organizational Efficiency
Management Control



Quantitative Indicators

	2006	2007	2010	2011	2012	2013	2014
Access to Capital							
• Total Borrowing				299.4	391.3	513.2	618.7
• Interest Expense/ Total Borrowing				9.3%	14.4%	5.2%	3.4%
Net Revenue	348.0		2,817.0	5,387.5	7,375.0	9,498.8	15,756.7
Net Profit	5.6		110.0	158.6	125.1	255.6	668.1
Reputation (Market Share)		<3.0%					30.0%[1]
Share Price Growth							127.4%[2]
Company Valuation		171.5[3]				2,103.9[3]	12,202.9[4]

All amounts in VND billion, unless otherwise specified.
[1] According to GfK's report.
[2] Share price change from IPO date, 14th July 2014, to 31th December 2014.
[3] Based on private equity transaction took place in that year.
[4] As of 31st December 2014.

International Finance Corporation
WORLD BANK GROUP

East Asia and the Pacific
J. Christopher Razook
Tel: + 852-2509-8512
Email: crazook@ifc.org
URL: www.ifc.org/corporategovernance

Vietnam
Nguyen Nguyet Anh
Tel: +844 3937 8741
Email: Nanh2@ifc.org
URL: www.ifc.org/vietnamcg

Centre for Asia Private Equity Research Ltd
URL: www.asiape.com

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