

VIETNAM'S SOE IPO BONANZA: BRINGING METHOD TO THE MADNESS

Initial Public Offerings (IPOs) are the “flavor of the season” in the Vietnam stock market. We attempt a structured approach to help investors shortlist and prioritize their SOE IPO investment options.

14 November 2017

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Post-listing share prices rallies following large IPOs are being driven by their scarcity value. What seems to be driving the post-listing run-up in share prices of large SOE IPOs in Vietnam is what we call the “scarcity premium”. This “scarcity premium” is being driven by the fact that Vietnam is a market with emerging market-like mainstream allure but frontier market-like access barriers.

- 1) **Vietnam is in vogue:** as one of the few enduring, non-commodity-driven high growth stories in the world, it is a “must-have” in most Asian equity portfolios. While still a “frontier market”, it is enjoying the attention typically commanded by emerging markets.
- 2) **Access barriers persist in Vietnamese equities:** while Vietnam is enjoying emerging market-like “share-of-mind” and mainstream publicity, it is still a frontier market with a relatively shallow equity market where liquidity and size of most listed names renders them inaccessible for most foreign institutional investors; this is exacerbated by the fact that most “investible” companies are already at their foreign ownership limit.

The huge “ticket-sizes” of SOE listings is giving a whole class of FIs access to Vietnam for the first time. This, we believe, is driving the impressive share price rally following large IPOs. This is not just restricted to the SOE domain – even large IPOs of private companies is generating similar levels of interest and post-listing returns for investors as evinced in the performance of recently-listed VJC has shown. But the premium placed on size means that SOEs are naturally going to comprise the majority of successful post-IPO equity stories; as an economy still transitioning from a “command-and-control” model to a totally market-driven one, Vietnam still has a disproportionate number of SOEs dominating basic industries that will closely track the Vietnam economic growth story: F&B, Tourism, Aviation, Infrastructure, Transportation, Energy and Utilities.

With the government set to privatize and list a slew of state-owned enterprises (SOEs) over the next few years, investors need to be selective. The strong pipeline of IPOs will boost the supply of “investible” companies, leading to a possible compression of the scarcity premium that is currently driving up post-listing share prices; this might reverse upon Vietnam’s inclusion into the MSCI emerging markets club which will massively boost demand for Vietnamese equities without commensurate supply but that is unlikely to happen for the next couple of years. In the interim, investors would be well-served to pick a few names rather than betting broadly on the post-IPO price juggernaut to drive returns.

To help investors navigate this sea of choice in the SOE space and prioritize their IPO investment targets, we prepared a simple list of criteria to “score” upcoming IPO names on their relative attractiveness. **Our simple IPO-scoring model shows that PV Power, Becamex IDC and PV Oil are the 3 most attractive IPOs to consider over the next 6 months. Note that our recommendation does not factor in the IPO valuation.**

Figure 1: Attractiveness Score by IPO expected between 4Q2017 and 1Q2018 (on a scale of 1 to 5)

Company	Industry	Expected time	Attractiveness Score	Component Scores							
				Size of IPO	Free float	ROE	Degree of Market Power	Sector growth prospects	Foreign Room (remaining)	Strategic Investor Participation	
Binh Son Refinery	Oil&Gas	1Q2018	3.1	3	1	3	4	3	5	3	
GENCO 3	Utilities	4Q2017	3.1	3	3	1	3	4	5	3	
PV OIL	Oil&Gas	4Q2017	3.6	5	4	1	4	3	5	3	
PV POWER	Utilities	4Q2017	3.9	5	4	1	3	4	5	5	
Song Da Corp	Construction	4Q2017	2.6	2	5	1	2	2	5	1	
VICEM	Construction Material	4Q2017	3.3	N/A	N/A	3	4	3	N/A	N/A	
VINAFOOD 2	Agriculture	4Q2017	2.3	N/A	N/A	1	3	3	N/A	N/A	
Vietnam Rubber Group	Rubber	4Q2017	3.3	5	3	2	4	3	5	1	
BECAMEX IDC	Real Estate	4Q2017	3.9	5	4	2	4	4	5	3	

Source: VNDIRECT

OUR SCORING CRITERIA EXPLAINED

Institutional accessibility and interest

Size of IPO: We believe that size is important as large IPOs are more accessible by large global Foreign Institutional Investors (FIIs); large IPOs also tend to attract the attention of retail investors due to the greater publicity they receive which in turn drives some “front-running” and greater liquidity for institutional investors that are looking to exit after riding the post-IPO rally. The larger the IPO the higher the score.

Free float: Stocks with greater free float are more accessible by large global FIIs; in the absence of actual trading history, free float is also the best predictor of liquidity. The higher the free float, the higher the score.

Foreign Room: Stocks which meet the size and liquidity requirements of foreign institutional investors but have limited foreign room typically see a “gold rush” as investors outbid each other to get a piece of the pie before the foreign room fills-up. So, non-intuitive as it may seem, we award more brownie points to IPO stocks with lower FOL caps.

Future earnings and shareholder value creation prospects

Return-on-equity: Given that most large IPOs are that of SOEs and that SOEs typically realize low returns on capital, profitable IPO candidates are in high demand (e.g. SAB).

Market power: Investors love monopolies (e.g. ACV). Unlike private sector companies, SOEs offer investors the ability to ride the growth of government monopolies or oligopolies which effectively eliminate risks from competitive threats.

Sector growth prospects: SOEs in high growth sectors are particularly sought-after for obvious reasons. ACV’s monopolistic position in the high growth aviation sector is the key reason for the seemingly unstoppable rise in the company’s share price, following its listing earlier this year. SOEs in dying, mature industries (of which there are many) would not command such attention even if they held monopolistic market positions since pricing power alone cannot deliver sustained earnings growth.

Strategic investor participation: We reward IPO candidates with clear plans for strategic investor participation as we believe that strategic investors will improve efficiency and returns on capital over time. This creates upside particularly for poorly-run, clunky SOEs. The greater the number of strategic investors that have expressed interest, the higher the score we award the SOE. This is because, competition among the strategic investors often tends to drive up the share price.

THE TOP 3 MOST ATTRACTIVE IPO INVESTMENT CANDIDATES

PV Power – PetroVietnam Power Corporation

PVPOWER plans to sell 20% of its shares in an initial public offering in December 2017; initial price expected at VND14,400/share. PVPOWER also plans to sell an additional 28.882% stake to strategic investors and 0.118% stake to employees, thus reducing state-ownership to 51%.

- PVPOWER is the second largest electricity generator in Vietnam (after Vietnam Electricity Corporation – EVN), contributes 12% total capacity and 13% annual output.
- One of the biggest IPOs in 2017. With expected initial price of VND14,400; total size of this IPO can reached VND6,271bn (US\$276mn).
- State-ownership to be reduced to 51% and seeking participation from strategic investors which should help improve operational efficiency and returns-on-capital down the line; more than 3 parties have expressed interest already.
- PVPOWER stands to benefit from the continued strong growth in electricity demand in Vietnam.

Becamex IDC will hold a public auction of 311.2 million primary shares at a starting price of VND31,000/share and will collect proceeds of VND9,647bn. The company will IPO on the Ho Chi Minh Stock Exchange on 1st December 2017. Price offered to employees is the lowest successful bidding price at the public auction..

The issuance to strategic investors will be held after completion of the public auction. The Government targets a minimum ownership of 51% in Becamex IDC post-IPO and Binh Duong's People Committee will represent the government's stake.

Becamex IDC – Industrial Investment and Development Corporation

- Largest industrial park (IP) developer with 11.9% of total IP area in Vietnam currently being operated by Becamex IDC, its subsidiaries and associates.
- IPO to be worth nearly US\$350mn, making it one of the biggest IPOs in 2017.
- Becamex IDC is also a big player in the infrastructure segment. Becamex IDC has built an integrated infrastructure development value chain spanning design, building materials, and construction.
- Becamex IDC has numerous advantages given its huge undeveloped land bank which is located in Binh Duong, a major population center and emerging industrial hub with the second highest FDI disbursement nationwide and complete transportation links to HCMC and large ports in Southeast Vietnam.
- Becamex IDC stands to benefit from the strong continued growth in industrial park development on the back of continued manufacturing FDI into Vietnam.

PVOil plans to sell 20% of its shares in an initial public offering in 4Q2017; initial price expected at VND14,300/share. PVOil also plans to sell an additional 44.7% stake to strategic investors and 0.2% stake to employees, thus reducing state-ownership to 35.1%. Expected to list on HOSE in 1Q2018.

PV Oil – PetroVietnam Oil Corporation

- PVOIL is the second largest petroleum distributor in Vietnam, with 22% market share in domestic petroleum and the sole seller of Vietnamese crude oil
- State-ownership to be reduced to 35.1% and expected 44.7% stake to be hold by strategic partners, PVOIL is expected to draw lots of attention from international strategic partners in given its nationwide petrol station network.
- A near-monopolistic play on the continued development of Vietnam's hydrocarbon industry.

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RECOMMENDATION FRAMEWORK

Stock Ratings

Definition:

- Add The stock's total return is expected to reach 15% or higher over the next 12 months.
- Hold The stock's total return is expected to be between negative 10% and positive 15% over the next 12 months.
- Reduce The stock's total return is expected to fall below negative 10% over the next 12 months.

The total expected return of a stock is defined as the sum of the:(i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings

Definition:

- Overweight An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
- Neutral A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
- Underweight An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

Country Ratings

Definition:

- Overweight An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
- Neutral A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
- Underweight An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.

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