

#ClosingTheGap Mekong

# Executive Summary

## Vietnam

Entrepreneurial Ecosystem Assessment



Commissioned on behalf of:  
Dutch Good Growth Fund (DGGF): Investment funds local SMEs  
April 2019

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### Entrepreneurial Ecosystem Assessment

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The Dutch Good Growth Fund, part Investment funds for local Small and Medium Enterprises (SMEs), is a “fund of funds” investment initiative from the Dutch Ministry of Foreign Affairs. The initiative aims to improve financing for the “missing middle” – i.e. entrepreneurs who have outgrown micro-finance but do not yet have access to regular financial services. The Seed Capital and Business Development (SCBD) program was established to increase the impact of the DGGF by providing technical assistance, seed capital and business support services to intermediary investment funds and local SMEs. The program incorporates a knowledge development and sharing component that supports research, tests assumptions and shares insights into financing SMEs in developing countries and emerging markets – fostering industrywide knowledge exchange.

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#### **Disclaimer:**

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Ministry of Foreign Affairs



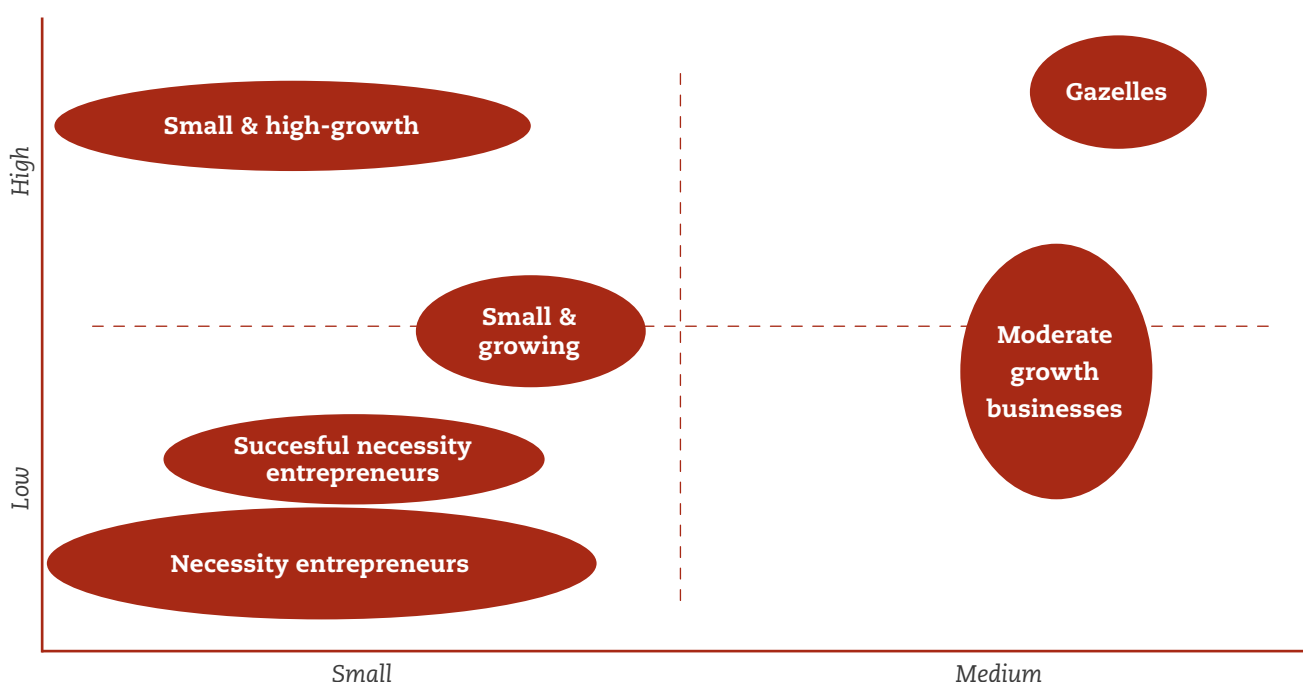


Vietnam has experienced a prolonged period of economic growth since its transition to a market-based economy through the Doi Moi reforms in the 1980s. It is now a middle-income country and one of the most dynamic emerging economies in Southeast Asia. The proportion of people in extreme poverty fell from greater than 70% in the early 1990s to about 10% in 2016, according to the World Bank.

Vietnam's strong export sector has often been credited with this success, and indeed Vietnam is one of the most globalised countries in the region, with its exports as share of GDP at the highest of any populous country. More recently, Vietnam's large and emerging middle-class market has attracted significant investment, and the country leapfrogged into a highly tech-enabled age. Groups of young startup entrepreneurs are aspiring to disrupt nearly all sectors of the economy with new technologies, spurred on both by televised pitching competitions like "Shark Tank" and significant government support for startups and small and medium enterprises (SMEs).

Segmentation of data from the 2015 World Bank Enterprise Survey (WBES) shows that 29% of SMEs in Vietnam are small, low-growth or no-growth businesses; the lowest amongst CLMV countries. Conversely, 25% of SMEs are high-growth, with growth rates over 20% per annum, with many growing to employ over 20 employees. Women-owned firms – with greater than 50% women ownership – constitute about 53% of all small and 44% of medium firms, which is higher than Cambodia, Lao PDR and Myanmar. However, the number of women-managed businesses is lower than women-owned, the opposite of the other #CTGMekong countries.

Figure 1: Sub-segments as proportion of total



Source: EMC analysis based on the 2016 Enterprise Survey (<http://www.enterprisesurveys.org>), The World Bank

The entrepreneurial ecosystem of Vietnam is by far the most developed among the #CTGMekong countries and offers lessons to the other countries in the region looking to build a thriving tech and risk capital scene that can benefit other parts of the ecosystem while alleviating some finance and administrative constraints.

### The Government Is Pushing Strongly for an Innovation-Driven Economy

One feature that sets Vietnam apart is its government's commitment to supporting startups and SMEs through public investment and further private investment incentives for technology and R&D. Notably, the ambitious "Project 844"<sup>1</sup> aims to develop a nationally-spanning innovative startup ecosystem by 2025, which would include SME investment regulations that allow the state to directly invest in startups.

<sup>1</sup> Decision No. 844/QĐ-TTg dated May 18th, 2016.

Agencies such as the National Technology Innovation Fund (NATIF) – a financial institution under the Ministry of Science and Technology (MOST) – provide grants and preferential loans for R&D, innovation and technology transfer.

The Vietnamese government has also invested significantly in industrial zones in order to concentrate manufacturing investment and export activity. As of 2017, there were more than 190 industrial parks in Vietnam, including three national-level “hi-tech parks”: the Hoa Lac Hi-Tech Park in Hanoi, Saigon Hi-Tech Park and Danang Hi-Tech Park. These parks offer modern transport, energy and wastewater infrastructure, and investment incentives including tax breaks and access to government support for research and development.

### **Despite Significant Interest from Investors, Access to Capital Remains a Challenge**

Although Vietnam has the most vibrant and diverse financial sector of all #CTGMekong countries, there remain areas of relative weakness. The state’s dominance over the banking system – particularly via state-owned banks – restricts the allocation of credit to SMEs in favor of SOEs and large corporates. This is particularly true in the non-tech sectors, where the SME Development Fund (SMEDF) has thus far failed to address the credit gap: in the past 1.5 years, it only made approximately one loan a month, with an average size of US \$300,000.

Friends and family remain the common sources for startup financing, while tech companies can access more seed financing from a growing number of accelerators. There is also a significant amount of interest from foreign VC and PE investors, but the number of domestically-managed PE funds remains limited. Because regionally-managed funds tend to look for tickets of US \$15 million or more, the supply of US \$5-\$15 million investments is limited. This is especially true in ‘traditional’ sectors that are not directly tech-oriented, where obtaining equity financing below US \$5 million is extremely difficult.

Startupcity.vn – a portal for startup and investor matching – identifies four angel networks and investment clubs and nine individual angel investors, of which three provide no information on background or track record. Interviewees describe angel networks as very fragmented, and high net worth individuals (HNWI) still prefer traditional asset classes such as securities or real estate.

From the perspective of investors, existing businesses’ corporate governance and management standards remain low in many sectors. Whilst many SMEs may be eager for investment, in practice the proportion of those that are investible is far lower. Much capital, managed by both PE and VC fund managers, is more interested in domestic market opportunities, geared to growing middle class and youthful demographics and less towards business-to-business, international economic integration and capital-intensive sectors.

### **Business Support Services Are Diverse, and Acceleration Programs Show Promise**

The supply of business support services is developing very quickly, with an increasing number of participants and diversity of services. Sources of support are equally diverse, with government, development partners, and domestic and international private sector accounting for significant investment. There are numerous co-locating services catering to startups, freelancers and small corporations. The sector has experienced rapid growth – reportedly 55% annually during the past five years – and is expected to reach 45 co-location facilities by the end of 2018. The sector caters overwhelmingly to startup entrepreneurs under 35 and tech startups, but continues to expand.

Several years ago, there were still clear gaps in the market, but within the past two years, initiatives have been launched to address these. VMI and WISE have been launched to improve mentoring and support for women entrepreneurs, although these are still in early stages and require scale to achieve sustainability. Only two ‘private sector’ accelerators – TFI and VIISA – have been operating, however new offerings are planned with significant participation from investors and international operators.

Accelerator programmes with clear goals and effective programming are increasing with the support of private sector investment. However, it is likely that capacity will remain insufficient to meet aspirations of young tech entrepreneurs. The availability of existing government support remains quite opaque to startups in the sector, who are often not aware of how to access government support or of its existence at all.

Key issues affecting the Vietnam ecosystem are summarised in this SWOT table.

Figure 2: SWOT analysis of the Vietnam ecosystem

<p><b>STRENGTHS</b></p> <ul style="list-style-type: none"> <li>• Large market for goods and services, both domestically and via export market access</li> <li>• Access to credit, financial literacy and business formalisation relatively high for the region, compared to CLM</li> <li>• Significant government support for R&amp;D, innovation and technology infrastructure</li> <li>• Relatively strong interest from foreign venture capitalists and private equity</li> </ul>	<p><b>WEAKNESSES</b></p> <ul style="list-style-type: none"> <li>• Not enough credit; banking system dominated by SOEs, and MFIs are not a viable alternative</li> <li>• Early stage risk capital (VC and PE) still difficult for non-tech startups and small growing businesses</li> <li>• Entrepreneurs find it difficult to find specific, relevant support services</li> <li>• Lack of support services outside major cities</li> </ul>
<p><b>OPPORTUNITIES</b></p> <ul style="list-style-type: none"> <li>• Expansion of credit and services to more rural areas</li> <li>• Continued openness of trade and investment, introducing foreign expertise and capital to help firms grow</li> <li>• Integration of homegrown tech solutions into Vietnam's major economic pillars</li> <li>• Expansion of business support services targeting women entrepreneurs</li> </ul>	<p><b>THREATS</b></p> <ul style="list-style-type: none"> <li>• Overly focused support for tech-centered startups not reaching many SMEs in traditional sectors or rural areas</li> <li>• Lack of reform in banking sector continues to limit credit to small firms</li> <li>• Lack of coordination amongst ecosystem stakeholders, public and private</li> </ul>

## Recommendations

The government's long-term vision for the Vietnamese economy, as outlined in "Vietnam 2035", is to become an innovation-driven economy, building on its export prowess and heavy investment in R&D. Two key strategies for this are application of technology across all sectors of the economy and integration of SMEs into global supply chains.

Vietnam is helped by a vibrant but concentrated entrepreneurial ecosystem, highly focused on tech startups and large venture capital deals. It is imperative however, that SMEs in more traditional but successful sectors are not forgotten. The ecosystem should grow to be more closely connected, providing specialised services at scale to produce SMEs that fit within the overall economy and are able to attract growth financing.

This will include specially tailored interventions to support those segments that are currently underserved by business support providers, such as women-managed SMEs and those outside of the main entrepreneurial hubs in the largest cities.

### Expand the Range of Financial Offerings Available to Entrepreneurs

Access to finance was ranked as the largest constraint for many SME segments; particularly pressing for those with high levels of growth. The state-dominated banking system does not provide enough small loans, and there are no viable alternatives for most entrepreneurs.

Credit lines to reliable private sector banks for the purpose of SME lending can help alleviate this problem for small and growing businesses. These credit lines can go together with services to help SMEs access them and build banks' capacity, bypassing traditional challenges of complex and time-consuming procedures.

Increasing the availability of risk capital in the range of US\$ 1 – 10 M will help small businesses with high growth to achieve national scale. This likely entails support for domestically managed PE funds and market oriented impact investing, both of which are in relatively short supply.

For entrepreneurs at all stages of development, non-bank financing has potential. Vietnam's digital payment platforms can use customer data to support credit decisions on short term loans. These and other solutions such as factoring, peer-to-peer lending, and supply chain finance are currently in their infancy and require regulatory, technical, and financial support.

### **Foster Sector-Specific Support Services to Integrate Vietnam's SMEs into the Wider Economy**

The large number of business support service providers in Vietnam's ecosystem mostly provide similar, generic services to entrepreneurs and tend to focus on the tech sector. The growth of technology startups has the capacity to transform the entire SME landscape by providing tech services to modernise and innovate in the wider economy.

Currently, only one-fifth Vietnamese SMEs are integrated into global supply chains, despite the export-driven nature of Vietnam's economy. Providing the services to increase this share of SMEs therefore has a very large potential impact. This will require support to implement international standards and quality systems as well as provision of export-oriented financial support, such as trade financing and factoring

Vietnam has the scale to support sector-specific niche acceleration and incubation services, providing tailored coaching and networking with knowledgeable industry insiders that lend entrepreneurs foresight, as well as suppliers and customers.

### **Expand Ecosystem Services to More Second-Tier Cities and Provincial Areas**

The existing ecosystem support services are highly concentrated in the main cities; Hanoi and HCMC, and lacking elsewhere.

A model example that could be emulated is that of Danang, which has managed to develop a dynamic entrepreneurial ecosystem focused on tech in just a few years. Key to its success have been the concerted government efforts on infrastructure and enabling policy support, catalysed private sector investment, and an active community of tech entrepreneurs and ecosystem builders.

### **Increase Tailored Support for Women Entrepreneurs**

Women still face many barriers to entrepreneurship, including insufficient managerial and business skills, as well as connections with banks and other financiers. The share of women-managed businesses in Vietnam is the lowest in the region, especially fast-growing businesses.

To tap into this potential, existing women-focused initiatives can be scaled up and used to develop best practices to provide specific mentoring, acceleration, and financing services to women entrepreneurs.