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Investing in consumer lending in Vietnam

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In brief: In recent years there's been a sharp increase in foreign investors' interest in breaking into the fast-growing consumer lending sector in Vietnam, through the acquisition of existing local players. Our team looks at the relevant legal framework for consumer lending activities in Vietnam, and the conditions and processes applicable to foreign investment in this sector.

Background

M&A activities in the consumer lending sector has been particularly active in the recent years. Completed deals include the acquisitions by Shinsei Bank and Credit Saison of a 49 per cent interest in MCredit and HD Finance, respectively, and there are currently a number of major ongoing deals in the market.

A young and aspirational population, coupled with stable and continuous increases to incomes, has resulted in rises in spending and a subsequent increased demand for consumer lending in Vietnam. From a legal perspective, recent regulatory changes have created a clearer legal framework for the establishment and operation of finance companies in Vietnam.

Additionally, as the State Bank of Vietnam (***SBV***) has sought to impose more restrictive credit growth limits on banks in Vietnam, investment by the banks in consumer lending subsidiaries has become more attractive, due to the higher interest rates that can be charged. However, operating a consumer lending business brings unique challenges and, therefore, many of these banks have been actively looking for a foreign partner with international experience in the sector to assist with growing their new business.

These factors have resulted in consumer lending being one of the 'hot sectors' for foreign investment in Vietnam.

Overview of Vietnamese consumer lending regulations

- **Consumer lending**: In Vietnam, consumer lending is a subset of 'lending for living requirements', which can be provided by different forms of credit institutions, including commercial banks and consumer finance companies (***FinCos***).

  Consumer lending by a FinCo is defined as it lending Vietnamese Dong to an individual borrower, to provide capital for the purchase and use of consumer goods and services (see below) required by the borrower and their family.

- **Forms of consumer lending**: The law contemplates two forms of consumer lending – one-off lending or credit facility lending (ie an overdraft concept).

- **Permitted purposes of consumer lending:** Consumer loans can be provided for the following purposes:
  - purchase of vehicles, furniture and household goods;
  - payments for study, medical treatment, tourism, culture and sport activities; or
  - payment of housing repair costs.

- **Borrowing limits:** Generally, the total balance of consumer loans provided by a FinCo to any one borrower at any time is limited to VND100 million (approximately US$4400). However, this limit does not apply to consumer loans for the purchase of cars, where the car is to be used as collateral for the loan.

- **Disbursement methods:** A loan can only be disbursed directly to the individual borrower if the loan amount is less than VND100 million. Loans can also be disbursed directly to the supplier of the relevant goods or services, and this must be done if the loan is in excess of VND100 million.

  If the supplier is a corporate entity, loans in excess of VND100 million must be disbursed by direct transfer to the supplier. Otherwise, loans may be disbursed to suppliers in cash.

- **Term:** There is no restriction on the term of consumer loans provided by a FinCo and this can be negotiated with customers.

- **Interest rate caps**: Currently, there is no interest rate cap applicable to consumer lending by a FinCo. Although the Civil Code generally provides for a 20 per cent. interest rate cap for loans, the specialised banking and consumer lending regulations allow FinCos and their customers to agree on interest rates and fees without reference to this 20 per cent. cap. FinCos must issue their framework for interest rates for consumer lending, including the highest and lowest interest rates applicable to each consumer loan product.

- **Default interest rate:** The default interest rate on an overdue consumer loan is subject to the following caps:
  - for overdue principal amounts, 150 per cent of the interest rate applicable to the underlying loan that is in default; and
  - for overdue interest amounts, 10 per cent per annum.

- **Interest rate calculation**: By law, interest must be calculated based on the actual loan balance at the relevant time and not the original principal amount of the loan.

- **Required standard terms for a consumer credit contract**: A consumer credit contract between a FinCo and its borrower must have certain minimum contractual terms prescribed by law, including the purpose of the loan, lending method, credit limit, interest rate, disbursement and repayment mechanism, and prepayment and termination terms.

  Specifically, regarding the applicable interest rate, the law requires various information to be specified in the consumer credit contract, such as the annual base interest rate; the principles, factors and time for determining the interest rate; the applicable overdue interest rate; the applicable overdue principal interest rate; and any other applicable fees.

- **Disclosure requirements:** FinCos must provide a draft consumer credit contract to customers for their review before execution of the contract. In addition, FinCos are required to provide an additional explanation of specific clauses in the contract, if requested by customers.

  FinCos must also publish their standard form contracts, or the general terms and conditions used in its contracts, at its headquarters, points of service promotion and on its website. FinCos also need to provide such standard terms to their customers and obtain confirmation from them of their receipt of such information.

- **Point of service promotion:** FinCos are allowed to open 'points of service promotion' (***POSP***) to introduce their consumer loan products to customers at the suppliers' locations (eg supermarkets or car dealerships). However, activities at the POSP are strictly limited to the introduction of consumer loan products and the collection of customer information. FinCos are not permitted to conduct other activities at the POSP (eg cash loan disbursement or collection).

Foreign investment in consumer lending

Restrictions on foreign investment in consumer lending

Foreign investors can invest in the consumer lending sector in Vietnam by either setting up a new FinCo or acquiring a stake in an existing FinCo.

The ownership restrictions and requirements for foreign investment depend on the method of investment and the corporate type of the FinCo to be set up or acquired by the foreign investor, as follows:

<table>
<tr><th>FORM OF FINCO</th><th>FOREIGN OWNERSHIP LIMIT</th><th>MAIN REQUIREMENTS FOR FOREIGN INVESTORS</th></tr>
<tr><td>Single member limited liability company (SLLC)</td><td>No restriction – a foreign investor can be the single member (ie own 100% of the SLLC)</td><td rowspan="2">› Licensed to conduct banking activities in its home country;
› profitable for at least the three preceding years before investment;
› total assets of at least US$10 billion as at the end of the preceding year;
› stable rating from international credit rating agencies;
› no breach of law by it in its home country for the five consecutive preceding years before investment; and
› not a strategic shareholder, owner or founding member of any other credit institution in Vietnam.</td></tr>
<tr><td>Multiple member limited liability company (MLLC)</td><td>No restriction on the total foreign ownership level – foreign investors can own in aggregate 100% of a MLLC.
However, the total ownership interest of a single investor and its related persons is capped at 50%. This restriction also applies to Vietnamese investors.</td></tr>
<tr><td>Shareholding company</td><td>Foreign investors are not allowed to establish a shareholding FinCo.
For acquisition of shares in an existing shareholding FinCo:
› one individual: 5%
› one foreign organisation: 15%
› one strategic foreign investor: 20%
› one foreign investor and its related persons: 20%</td><td>(a) A foreign investor holding less than 10% interest: no specific requirement.
(b) Non-strategic foreign investor holding 10% interest or more:
› stable rating, or higher, from international credit rating agencies; and
› as at the end of the preceding year, total assets of at least US$10 billion (for investors that are credit institutions); or total charter (equity) capital of at least US$1 billion (for other investors).
(c) Strategic foreign investor:
› must be a bank or a credit institution permitted to conduct the corresponding finance activities in its home country;
› 'stable' rating, or higher, from international credit rating agencies;
› at least five years' experience in conducting international banking and finance activities;
› total assets of at least US$20 billion as at the end of the preceding year; and
› must not be holding more than 10% of the charter capital in any other credit institution in Vietnam.</td></tr>
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Setting up a new FinCo

As set out above, foreign investors are allowed to set up a FinCo with up to 100 per cent foreign ownership in the form of a SLLC (if there is one single investor) or MLLC (if there are two or more investors – either foreign or Vietnamese). Foreign investors are not allowed to set up a FinCo in the form of a shareholding company.

Founding investors of a FinCo are subject to a lock-up period of five years from the date of the FinCo's establishment. However, during this period they are permitted to transfer their interest to another founding investor.

The general licensing process for setting up a FinCo comprises the following main steps:

- **SBV in-principle approval**: The investors apply to the SBV for an in-principle approval for the establishment and operation of the FinCo.
- **SBV establishment licence**: After the in-principle approval is issued, the investors apply to the SBV for an official licence for the establishment and operation of the FinCo.
- **Enterprise registration certificate**: The FinCo must then apply for an enterprise registration certificate, to the Department of Planning and Investment (***DPI***) where its head office is located.
- **Charter capital contribution**: The investors deposit the charter capital of the FinCo with the SBV before the FinCo's commencement of operations.
- **Post-licensing steps**: The FinCo must complete various administrative and organisational steps to prepare for its official operation, including setting up its operational systems and passing a physical SBV inspection.
- **Commencement of operations**: The FinCo must commence its operations within 12 months after the SBV licence is issued; otherwise, the SBV may revoke the licence.

Investing in an existing FinCo

Instead of setting up a new FinCo, foreign investors can invest in an existing FinCo, to leverage its existing network and resources. The relevant foreign ownership restrictions and requirements for foreign investors are discussed above.

The approval process for a foreign acquisition of an existing FinCo depends on its corporate form.

Investing in an existing SLLC and MLLC FinCo

There is no specific regulation of the approval process for an acquisition by a foreign investor of a stake in a FinCo in the form of an SLLC or MLLC. In practice, we understand that the SBV will apply similar processes to the establishment of a new FinCo.

If the capital transfer results in conversion of the FinCo's legal form (eg from an SLLC with one investor to an MLLC with two or more investors), the FinCo must apply for the SBV's approval for such conversion in parallel with the capital transfer approval process.

Please note that the law does not provide for any lock-up period for foreign investors acquiring a stake in an existing FinCo organised in the form of a limited liability company.

The main licensing steps for a foreign investor to acquire a stake in an SLLC or MLLC FinCo are as follows:

- **SBV In-principle approval**: The investors must apply to the SBV for an in-principle approval for the capital transfer and (if applicable) conversion of the FinCo's legal form.
- **SBV licence**: After the in-principle approval is issued, the investors must apply to the SBV for an amended licence for the establishment and operation of the FinCo and for approval of the capital transfer. Changes to the FinCo's management following the capital transfer will also be approved in this step.
- **M&A approval**: While it is not entirely clear under the current law, the foreign investor may need to apply to the DPI for an M&A approval for the capital acquisition after the SBV approval is issued.
- **Enterprise registration**: Finally, the FinCo must apply for amendment of its enterprise registration certificate to reflect the new investors in the company.

Investing in an existing shareholding FinCo

A foreign investor acquiring shares in a shareholding FinCo will be subject to the following lock-up restrictions:

- five years for foreign strategic investors; and
- three years for a non-strategic foreign investor holding 10 per cent or more shares.

The main licensing steps for a foreign investor to acquire shares in a private shareholding FinCo are as follows:

- **SBV approval**: Prior approval from the SBV is required for any acquisition by a foreign investor of 5 per cent or more shares in a FinCo.
- **M&A approval**: While it is not entirely clear under the current law, the foreign investor may need to apply to the DPI for an M&A approval for the shares acquisition after the SBV approval is issued.
- **Deposit and payment of the purchase price**: Within 30 days from the SBV's approval, the foreign investor must deposit the purchase price into its VND indirect investment capital account opened at a bank in Vietnam. At closing, the foreign investor must pay the purchase price to the seller through this account.
- **Notification of foreign ownership ratio**: The target FinCo must notify the SBV of the change in its foreign ownership level within 15 days from completion of the transaction.

If the target FinCo is a public or listed company (though there are not presently any such FinCos in Vietnam), additional steps, and approvals from the State Securities Commission, may be required under the securities regulations (eg tender offer or off-band trading approval).

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Allens is a leading international law firm in Corporate and M&A in Vietnam, with a particularly strong track record in banking, insurance and consumer finance M&A. For further information on consumer lending and investment in the consumer lending sector in Vietnam, please contact us.

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