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Vietnam's infrastructure sector: the landscape, opportunities and challenges

APRIL 2022

Having sound infrastructure is vital to every country's development and its citizens' quality of life. Countries need reliable infrastructure to connect supply chains and efficiently move goods and services across borders. They also need reliable health, education, and connectivity infrastructure to help their people thrive.

In this context, it's no surprise that Vietnam's Government has focused on developing infrastructure to underpin socio-economic development strategies. Despite this, and significant progress over the past two decades, infrastructure deficiencies are one of the biggest bottlenecks for investors in Vietnam.

Against this backdrop, and as Vietnam has developed and moved out of low-income country status, the means of financing infrastructure has shifted away from official development assistance and soft loans towards a heavy emphasis on private financing. Over time, this has been illustrated by the development of Vietnam's infrastructure-related regulations.

In this report, we look at the current status of the infrastructure market, with a focus on particular sectors. We also examine key regulatory and structuring issues affecting project developers and financiers.

KEY TAKEAWAYS

- With its economy growing strongly, Vietnam's need for infrastructure is increasing across a wide range of sectors, opening up numerous opportunities for infrastructure developers, investors, lenders and service providers.
- While the need for high-quality modern infrastructure in Vietnam continues to grow, the legal environment underpinning projects is becoming increasingly complex and nuanced – presenting a number of changes and challenges to consider.
- In 1993, Vietnam first issued regulations regarding investment through build-operate-transfer (BOT) projects (applicable to foreign investors). Since then, there have been numerous iterations of the regulations – each striving to find a balance between private and public interests, with varying degrees of success.
- Vietnam's first law on public-private partnerships (***PPP***) was approved in 2020, taking effect from 1 January 2021 (the ***PPP Law***). It aims to unify disparate regulations and reset the basis on which private investors deal with the state when developing key infrastructure. (You can read our overview of the PPP Law here and more about its detailed implementing regulations here.)
- The PPP Law has enshrined the Government's policy position that it should have less responsibility to backstop project feasibility compared with earlier infrastructure projects. As a result, financing infrastructure projects, particularly with non-recourse financing, remains challenging. Despite this, the Prime Minister (the ***PM***) has authority to provide bespoke support for projects implemented outside of the PPP framework.
- The transport sector (roads, ports, airports, railways) leads the way in terms of projects implemented (or set to be implemented), while the other key sectors in Vietnam's infrastructure market include power, gas and petrochemicals.

1. THE MARKET OVERVIEW

1.1 In general

As of January 2019, 336 PPP projects were implemented in Vietnam, with total investment capital of more than VND1,600 trillion (c. USD 69 billion)[1]. Most of these projects were carried out using either the BOT form (42%) or build transfer (***BT***) form (56%). A considerable majority (220 projects; approximately 65% of the total number) were in the transport sector – primarily roads. The next most common sector was power, with 19 projects.

Below, we provide a snapshot of the current status of the following key infrastructure sectors: power, gas, roads, ports, airports and petrochemicals.

1.2 Power

In Vietnam's power sector, private sector investment has been carried out in either the PPP form (primarily using BOT structures) or as independent power projects (***IPPs***) outside of the PPP regulations. In recent years, there has been significant foreign investment in renewable energy, either through direct IPP investment or from the acquisition of existing assets from local developers.

An energy project can only be developed if it has been included in a 'power development master plan'. In line with the Law on Planning, there is a national power development master plan. Each province also has a provincial master plan, with a section on power complementing the national plan. While both plans need to be approved by Vietnam's PM, the national power development master plan is developed by the Ministry of Industry and Trade (the ***MOIT***). Provincial master plans are developed by each province and appraised by the Ministry of Planning and Investment (the ***MPI***).

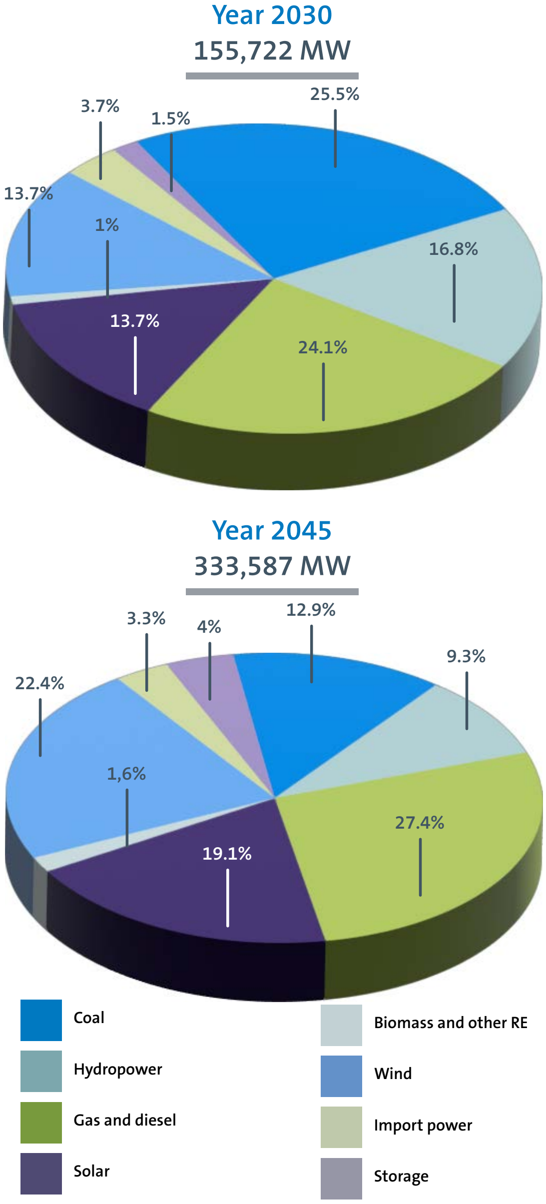
The current approved national power development master plan is the PDP7 (revised), which covers the period from 2011 to 2020 with a vision to 2030. The next national power development master plan (the ***PDP8***) is currently being drafted. The PDP8 will establish the direction of power development from 2030 up to a vision of 2045. Following Vietnam's announcement at COP26 of a 2050 net-zero emissions target, the Government has requested the MOIT to collect more opinions from experts, scientists and localities, to make PDP8 fit for purpose. While the issuance date is unknown, it is expected in Q1 of 2022.

According to the most recent draft of the PDP8 (November 2021), the total installed capacity must be capable of meeting the maximum power demand of Vietnam as a whole. However, the currently planned development pipeline is not compatible with the consumption and supply growth within each of the Northern, Central and Southern regions.

The growth in demand in the north is the highest (around 9.3% per year for the 2016–20 period) while supply-side growth is the lowest among the regions, at 4.7% per year.[2] The demand and supply-side growth for the same period in the centre is 5.3% and 16% per year, and in the south, 6.8% and 21% respectively.[3] This incompatibility between demand and supply is driving specific policies for the development of particular power sources and the approach to transmission in each of the regions. In line with the November 2021 draft of the PDP8, the national total installed capacity is expected to reach around 155,722 MW by 2030 and 333,587 MW by 2045.

1 Report 25/BC-CP of the Government dated 30 January 2019 on status of implementation of investment projects in the form of public-private partnership (***Report 25***). To our knowledge, no further updated report has been prepared.
2 Reference materials in the MOIT workshop to collect opinions to complete the draft PDP8, November 2021, page 4.
3 Reference materials in the MOIT workshop to collect opinions to complete the draft PDP8, November 2021, page 5.

We have set out the allocation of power sources in the chart below.



(a) PPP power plants

Currently, only two BOT gas-fired power plants (Phu My 2.2 (715MW), Phu My 3 (720MW)) and four BOT coal-fired power projects (Mong Duong 2 (1,240MW), Vinh Tan 1 (1,240MW), Hai Duong (1,200MW) and Duyen Hai 2 (1,320MW)) are in operation. Nghi Son 2 (1,200MW), Van Phong 1 (1,200MW) and Vung Ang 2 (1,200MW) coal-fired power projects have achieved financial close and are currently under construction.[4]

Despite the instruction from the Politburo in Resolution 55, and Vietnam's net-zero announcement, the planned installed capacity for coal-fired power plants in the November 2021 draft of the PDP8 remains high – 39,699 MW by 2030 and 43,149 MW by 2045 for the high-load case, which accounts for 25.49% and 12.9% of the total national installed capacity respectively.[5] However, these figures have been reduced from 40,899 MW by 2030 and 50,949 MW by 2045, which accounts for 28.43% and 15.5% respectively, as set out in the draft PDP8 released in October.[6] It remains to be seen how much new coal-fired power capacity will ultimately be able to be financed and constructed.

(b) IPP power projects

Year 2030	Year 2045
155,722 MW	333,587 MW

Currently, seven IPP projects with a capacity of more than 100MW are being implemented, with a total capacity of more than 2,000MW. Two of these – the coal-fired Thang Long project (Quang Ninh province, total capacity of 2x300MW) and the An Khanh project (Bac Giang province, total capacity of 650MW) – are operational. IPP projects are developed on very different terms from PPP projects. Importantly, there is no clear regulatory pathway for investors to seek government guarantees (such as EVN credit support or currency conversion guarantees). In practice, it is also very difficult for IPP investors to obtain such guarantees.

As we analyse in more detail elsewhere in this *Report*, there are considerations to be taken into account for both PPP and IPP forms (post the PPP Law taking effect), before deciding on the investment form for a project.

(c) Renewable energy projects

Under the law, large-scale renewable energy projects can be carried out in PPP form. However, none have taken this route so far. All have been in line with legal instruments specifically issued for renewable energy investments.

The PDP7 sets out a target for increasing wind power capacity to about 2,000MW by 2025, and solar power capacity to about 4,000MW by 2025 and 12,000MW by 2030.[7] In the November 2021 draft of the PDP8, the capacity for solar power has been increased to 21,390 MW by 2030 and 63,640 MW by 2045.

However, solar power capacity will be 're-evaluated', as solar has limited operating time, and Vietnam has not yet developed a viable energy storage system. In the November 2021 draft of the PDP8, there is more focus on onshore and offshore wind power. The capacity for onshore wind power is 17,338 MW by 2030 and 38,838 MW by 2045, and for offshore wind power, 4,000 MW by 2030 and 36,000 MW by 2045.[8]

(For more information on renewable projects, you can see our renewable energy publication here. You can find the offshore wind report here.)

4 Report 32/BC-BCT, page 9
5 Reference materials in the MOIT workshop to collect opinions to complete the draft PDP8, November 2021, pages 22 and 24.
6 Reference materials in the MOIT workshop to collect opinions to complete the draft PDP8, November 2021, pages 18 and 20.
7 Article 1.3(a) of the revised PDP7.
8 Reference materials in the MOIT workshop to collect opinions to complete the draft PDP8, November 2021, page 22.

(d) LNG-to-power

Developing gas and LNG-fired power projects is central to Vietnam's planning for baseload supply. The capacity for LNG-to-power is expected to increase in PDP8 to offset the reduction in coal-fired power.

In line with the November 2021 draft of the PDP8, the capacity for LNG-to-power is planned to be 22,400 MW by 2030 and 55,750 MW by 2045 (excluding capacity of planned coal-fired power plants proposed to be converted to LNG-to-power, which will remain unchanged at 14,783 GW by 2030). [9]

(For more information on LNG-to-power projects, see our LNG sector update here.)

1.3 Roads, ports, airports and rails

As noted above, transportation projects account for a significant majority (65%) of the total number of PPP projects implemented, or set to be implemented, in Vietnam to date. Of the 220 transport sector PPP projects, 132 (60%) are already in operation, with the rest at various stages of development.[10]

These projects have been mainly carried out in BOT and BT forms, the vast majority (96%) being road projects.

(a) Roads

The Vietnam Government is keen to accelerate the development of expressways. For the period 2021 to 2030 with a vision to 2050, it aims to have 41 expressways with a total length of 9,014 kilometres across Vietnam.[11]

To date, despite substantial interest, there has been limited involvement of foreign investors in road projects (no road projects are wholly owned and/or operated by foreign investors, and only one has any substantial foreign investment). Foreign involvement is typically limited to providing services and financing.

(b) Seaports

According to the current seaport master plan,[12] the key objectives for the period until 2030 include the development of a port system capable of handling up to 1,423 million tons of goods and 10.3 million passengers. Another priority is the development of international gateway ports and large-scale ports servicing national and inter-regional socio-economic development.

The north has been particularly hampered by a lack of deep-water ports capable of handling modern large-scale ships. However in May 2018, the Haiphong International Container Terminal (***HICT***) deep-water port in Lach Huyen, Hai Phong, opened for business.[13]

HICT is capable of accommodating large container ships, reducing the need for trans-shipments in northern Vietnam and allowing direct shipping between northern Vietnam and US and EU markets. The second phase of the port was expected to be completed by 2020, but currently remains under development.

In the centre of Vietnam, major ports are located in Quy Nhon and Da Nang, the latter being a deep-water port. There is also a proposal for the development of a seaport in Lien Chieu, Da Nang, in the PPP form.

In August 2020, Trung Nam Group held a groundbreaking ceremony for the construction of Ca Na general seaport in Ninh Thuan province (phase 1), with a designed capacity of 3.3 million tons of goods per year.

In the south, Ho Chi Minh City has a network of ports, with Saigon Port currently the 26th-largest container port in the world and the fifth-largest in ASEAN.

(c) Airports

For viable aviation infrastructure projects, the Government encourages investment in the PPP form. However, aviation sector investors face a number of challenges, including cumbersome and opaque government approval processes.

According to public information on the latest draft master plan for airports submitted to the Prime Minister, Vietnam will have 28 airports in total by 2030 – 14 international and 14 domestic (including 22 existing airports and the six new airports, Long Thanh, Na San, Lai Chau, Sa Pa, Quang Tri and Phan Thiet).

By 2050, there will be 31 airports – 14 international airports (Hanoi's Noi Bai airport will be expanded to have three runways by 2030 and four runways by 2050, accommodating 100 million passengers) and 17 domestic airports (including another airport in the southeast of Hanoi in the 2030–50 period, to ease the pressure on Noi Bai).

In the south, stage 1 of the Long Thanh airport commenced in January 2021 and is expected to be completed in 2025, and expanded by 2050 to have four runways and terminals for 120 million passengers. Da Nang airport will be expanded to have three runways and terminals for 40 million passengers by 2050. Tho Xuan airport in Thanh Hoa is expected to have two runways for 10 million passengers by 2050.

The Ministry of Transport (the ***MOT***) recently proposed using private capital in the PPP form for new airports such as Quang Tri, Sa Pa and Cao Bang.[14] The MOT has also proposed mobilising more private capital for aviation services and development of smaller airports outside the PPP form.

9 Reference materials in the MOIT workshop to collect opinions to complete the draft PDP8, November 2021, page 22.
10 Report 25.
11 Decision 1454/QD-TTg of the PM dated 1 September 2021 on approval of the master plan for the road network for the period of 2021 to 2030 with a vision to 2050.
12 Decision 1579/QD-TTg of the Prime Minister dated 22 December 2021 approving the master plan for development of Vietnam's seaport system for the period of 2021 to 2030 with a vision to 2050.
13 https://www.vietnam-briefing.com/news/port-infrastructure-vietnam-3-hubs-for-importers-exporters.html/
14 Transport Ministry proposes allowing private firms to invest in airport projects (vietnamnet.vn)

The plan for the expansion of Dong Hoi airport in the central province of Quang Binh is expected to be implemented between 2021 and 2025, with a total capital of VND2,320 billion (more than USD 100 million). The PM issued the investment policy approval on 21 October 2021 for the Sa Pa airport in the PPP form.

Meanwhile, an airport in Quang Tri with the capacity for one million passengers a year has been approved in principle by the MOT, with infrastructure conglomerate T&T Group reportedly carrying out a pre-feasibility study (***pre-FS***).

Other private enterprises, such as Vietjet, Vingroup and Imex Pan Pacific Group, have already shown interest in investing in airports.

(d) Railways

In 2018, the Standing Committee of the National Assembly passed a resolution[15] approving the investment of VND 15,000 billion (c. USD 644 million) of state budget funds for the 2016–20 period in important and urgent railway and road projects.

Despite this apparent support, there has been a general lack of enthusiasm from and involvement of foreign investors in the railway sector to date. There are various reasons, including that private investors can only invest in infrastructure that is not directly related to operating trains, such as stations/terminals and warehouses.[16]

In 2020, the PM directed the MOT to create a strategy for the development of railways in Vietnam up to 2030 with a vision to 2050. The focus will be to improve existing railway routes such as the Hanoi – HCMC and Lao Cai – Hanoi – Haiphong routes, as well as develop urban railway systems. Studies will be conducted to consider the construction of new railways connecting large seaports, industrial zones, tourism areas, highland provinces, the Mekong Delta, and international routes.

A pre-FS for a new express north-south route (1,559 km) was completed in July 2019. That project is planned in two phases:

- **Phase 1** will cover the Hanoi – Vinh and Nha Trang – HCMC segments being built before 2030.
- **Phase 2** will cover the Vinh – Nha Trang segment being built by 2040. However, the pre-FS only considered high-speed passenger transportation and, in January 2021, the MPI requested that the MOT adjust the plan to provide for lower-speed passenger and freight transportation.[17]

In terms of urban projects, master plans[18] provide for eight metro lines in each of Hanoi and HCMC, and three additional tramways or monorails in HCMC. Currently, two are under construction in HCMC, though significantly behind schedule due to EPC, fund disbursement and site clearance issues.

In Hanoi, the Cat Linh – Ha Dong line (13.1 kilometres being constructed by a Chinese contractor) was completed and put into operation in 2021, while the Nhon – Hanoi Railway Station line (12.5 kilometres being constructed by French contractors) is under construction.

The lines in HCMC are Ben Thanh – Suoi Tien (19.7 kilometres invested by the HCMC People's Committee with funding from JICA) and Cu Chi – Thu Thiem (48 kilometres invested by the HCMC People's Committee with funding from ADB, KfW and EIB). Metro line No. 5 from Bay Hien crossroad to Sai Gon bridge – phase 1 (8.9 kilometres) is also at an early stage of development.

1.4 Refinery/petrochemicals

Vietnam currently has two large operational refineries:

1. The Dung Quat Oil Refinery in Dung Quat Economic Zone, Quang Ngai. It was developed by PetroVietnam with total investment capital of about USD 3 billion, and a capacity of 8.5 million tons per year.
2. The Nghi Son Refinery in Nghi Son Economic Zone, Thanh Hoa. It was developed by four sponsors (PetroVietnam, Idemitsu Kosan Co. Ltd., Mitsui Chemicals Inc. and Kuwait Petroleum Europe B.V.) with total investment capital of more than USD 9 billion and a capacity of 10 million tons per year.

In addition, the Long Son petrochemical complex is under construction in Ba Ria – Vung Tau province. This project has total investment capital of around USD 5.4 billion, with the sole investor being the SCG group from Thailand.

The Vietnamese Government has indicated it aims to attract more investment in the refinery and petrochemical sectors to increase its value-add processing activities, and improve the quality of petroleum products. In all, Vietnam intends domestic refineries to meet at least 70% of total national demand.[19]

15 Resolution 556/NDQ-UBTVQH14 dated 31 July 2018 of the Standing Committee of the National Assembly, available at: https://thuvienphapluat.vn/van-ban/dau-tu/Nghi-quyet-556-NQ-UBTVQH14-2018-phuong-an-su-dung-von-du-phong-dau-tu-cong-trung-han-389811.aspx

16 http://baochinhphu.vn/Kinh-te/Ha-tang-duong-sat-gia-nua-Giai-phap-nao-de-thu-hut-von/376009.vgp

17 Nghiên cứu thêm phương án đường sắt cao tốc Bắc - Nam tốc độ 200 km/giờ | Tài chính - Kinh doanh | Thanh Niên (thanhnien.vn)

18 Decision 1259/QD-TTg of the PM dated 26 July 2011 issuing master plan for construction of Hanoi capital up to 2030 with the view to 2050, and Decision 568/QD-TTg of the PM dated 8 April 2013 on approval of adjustments to the master plan for transportation development of HCMC up to 2020 with the view to after 2020.

19 Section II.2(b) of Resolution 55- **NQ/TW of the Politburo of Vietnam dated 11 February 2020 on the orientation of the National Energy Development Strategy of Vietnam to 2030, with a vision to 2045** (***Resolution 55***).

2. THE DIFFERENT INVESTMENT FORMS

It is not mandatory for infrastructure projects to be carried out in the PPP form. While there are advantages and disadvantages to consider, the major benefit of investing under the PPP regime is it provides a specific regulatory pathway to seek government guarantees and support (though now on a limited basis) that will enhance project viability, mitigate risk and support financing.

While it is theoretically possible for the Government to offer such support to infrastructure projects done outside the PPP regime, there are limited precedents for this. Plus, investors face the uncertainty of direct negotiation. So far, we are aware of only two cases where the Government has provided government guarantees and undertakings (***GGU***) for megaprojects not carried out in PPP form. In another IPP, the Government issued a guarantee for the loan obtained by the project company (for repayment obligations only).

2.1 PPP or non-PPP?

From a bankability perspective, some of the regulations provide more favourable treatment for investment in the PPP form than the non-PPP form. Here's why:

(a) The PPP Law provides that the Government can decide on issuing guarantees on foreign currency for key PPP projects, with the investment policy decided by the National Assembly or the PM, subject to (i) foreign currency policy and the capability of the state to manage foreign currency reserves, and (ii) the 30% threshold for foreign currency support for VND project revenue (to be converted into USD) after deducting local expenses;

(b) In addition to foreign currency availability and conversion, the PPP scheme expressly provides for more guarantees and support from the Government, including priority access to public facilities and services, a mechanism for sharing revenue increases and shortfalls, and lenders' step-in rights;

(c) There is more room for the investor to negotiate bankable contracts in the PPP scheme. Specifically, the PPA for power projects does not have to follow a particular statutory form. Although the PPP contract has to follow a model form (which so far has only been issued in the form of guidance), a PPP contract by its nature allows the investor to shift certain risks to the Government side; and

(d) In practice, there is ample precedent of international financing on a non-recourse basis of power projects in the PPP form. Many international lenders are familiar with the project documents and the key risks (although it remains to be seen whether financiers will be as ready to finance projects under the requirements of the new PPP Law).

There are other considerations when comparing PPP and non-PPP regimes in the current environment:

(e) For non-PPP projects, it is less clear if a GGU will be on offer. Decree 31[20] states that subject to the socio-economic development conditions and the need to attract investment for each period, and the scale and nature of each project, the PM may decide the format and contents of a guarantee to be issued for (i) projects where the investment policy is decided by the National Assembly or the PM, or (ii) other important infrastructure projects. Decree 31 provides that such a guarantee can be in the form of (a) foreign currency support, or (b) other state guarantees as decided by the PM.

(f) Although Resolution 55 stated that energy investment projects are encouraged to be implemented in the PPP form, it appears that the PPP form is not preferable as a matter of practice in certain sectors. For example, of the various LNG-to-power projects recently proposed to be carried out, we are aware of only two projects proposed to be in the PPP form, and the Government appears to prefer that LNG-to-power projects are carried out as IPPs;

(g) History shows that negotiation of project documents in the PPP context can be very long and drawn out;

(h) The PPP Law sets out a brand-new regime that has not been tested in practice, so the investor should expect currently unknown hurdles and delays along the way;

(i) The non-PPP scheme offers some advantages that may be more attractive to the investor than those under the PPP scheme. For example, the law clearly provides that, in certain cases, the selection of an investor through bidding is not needed; and

(j) Other advantages of the non-PPP scheme include longer project life, no requirement to later hand over the project to the Government, no statutory time limit for securing finance, less stringent transfer conditions, and the possibility of some key contracts being governed by foreign law.

2.2 Investment cycle

Below are outlined the phases for investment under the PPP regime and the general investment law regime.

A PPP project must be included in the relevant master plans before the pre-FS can be formulated. Under investment law, a non-PPP project does not have to be included in a master plan,[21] except for power (including LNG-to-power) and gas projects, which must first be included in a power master plan (as has been the law and practice so far). Subject to this exception, an investment policy approval for a non-PPP project can be issued if the project complies with relevant master plans.

20 Decree 31/2021/ND-CP of the Government dated 26 March 2021 implementing the Law on Investment.

21 The Law on Investment only requires an investment project **to be consistent with** the national plan, regional plan, provincial plan, urban plan and special economic – administrative zone plan (if any) in order for the investment policy approval to be issued (Article 33.3(a)).

(a) PPP project cycle

A PPP project cycle consists of the following phases:

PPP PROJECT CYCLE

Phase 1

Pre-FS report, Investment Policy Approval (IPA), Project announcement

- Pre-FS report to be formulated by:
  - the body authorised by the authorised agency, or
  - the investor (in case the project is proposed by the investor);
- Pre-FS report to be evaluated by the PPP Evaluation Council;
- IPA to be issued by:
  - the National Assembly,
  - the PM, or
  - the Ministers of ministries or the provincial PC;
- Project announcement.

Phase 2

Feasibility study (FS) report and project approval

- FS report to be formulated by:
  - the body authorised by the authorised agency, or
  - the investor (in case the project is proposed by the investor);
- FS report to be evaluated by the same PPP Evaluation Council as mentioned in Phase 1.

Phase 3

Selection of investor

- The selection of investor can be via:
  - public tender;
  - competitive negotiation;
  - direct appointment of investor; or
  - other methods in special cases.
- Generally, public tender shall apply. The investor shall enjoy preferential treatment in the tender if it:
  - proposes the project;
  - undertakes to use domestic contractors for work accounting for at least 25% of the total investment capital of the project; and/or
  - undertakes to use domestic equipment and materials with a value accounting for at least 25% of the total investment capital of the project.
- Competitive negotiation only applies in the case:
  - i. there are no more than three investors satisfying the requirements for project implementation;
  - ii. the project is a hi-tech application project given priority for development; or
  - iii. the project applies new technology in accordance with the laws on technology transfer.
- Direct appointment of investor only applies in the case:
  - i. the requirement for national defence and security or state secret needs to be ensured, or
  - ii. replacement of an investor.

Phase 4

Project company establishment and signing of project contract

- Establishment of the project company shall comply with the Law on Enterprises;
- The PPP project contract is entered into between the project company, the investors and the contract signing agency;
- Payment of performance security deposit;
- Equity of the investors must be contributed in accordance with the schedule as agreed in the PPP project contract.

Phase 5

Project implementation, accounting finalisation, transfer of facility and liquidation of project contract

- The project company shall formulate and promulgate rules to select contractors for the implementation of the project.
- The project company shall be responsible for construction quality management and supervision, under the supervision of the authorised state body.
- The accounting finalisation shall be carried out after completion of construction.
- The handover of the project facility shall comply with the agreed conditions and procedures set out in the project contract.

(b) Investment project cycle under general Investment Law regime

An investment project cycle under the general Investment Law regime consists of the following phases:

NON-PPP PROJECT CYCLE

Phase 1

Formulation of investment project proposal

- Formulation of the investment project proposal (where construction laws require the pre-FS to be formulated, the pre-FS could be used in place of the investment project proposal).

Phase 2

Investment policy approval (IPA)

- IPA to be issued by:
  - the National Assembly;
  - the PM; or
  - the provincial PC.

Phase 3

Selection of investor

- The selection of investor can be via:
  1. auction of the land use right (LUR) in accordance with regulations on land;
  2. tendering in accordance with regulations on tendering; or
  3. approval of investor.
- Generally, auction of LUR applies in the following cases:
  - land lease or land allocation to implement the project is subject to auction of LUR under law on land; and
  - the proposed area of land for project implementation has already been cleared.
- Tendering applies in the following cases:
  - the project does not satisfy the conditions for auction of LUR as stated in the preceding bullet point; and
  - the project is subject to tendering for selection of investor under the law on tendering, the law on socialisation or specialised laws.
- Approval of investor applies in the following cases:
  - the LUR auction has been conducted but only one investor registered for participation;
  - the LUR auction in accordance with land regulations fails twice;
  - tendering is conducted to select investors, but only one investor registers for participation in the tendering and satisfies preliminary requirements for capability and experience. Or, various investors register but only one satisfies preliminary requirements for capability and experience;
  - the investor has LUR, except for the case where the state expropriates land for national defence and security purposes, or for socio-economic development in the national or public interest in accordance with regulations on land;
  - the investor has LUR via LUR transfer, capital contribution, lease of agricultural land for implementation of non-agricultural investment project for production or business that is not subject to land expropriation by the state in accordance with regulations on land;
  - the investor implements the investment project in an industrial park or hi-tech zone; or
  - other cases not subject to an auction or tendering in accordance with law.

Phase 4

Investment registration certificate (IRC), Enterprise registration certificate (ERC)

- IRC shall be issued after issuance of IPA, except for projects that do not require an IPA.
- Establishment of the project company shall comply with the Law on Enterprises.

Phase 5

Project implementation

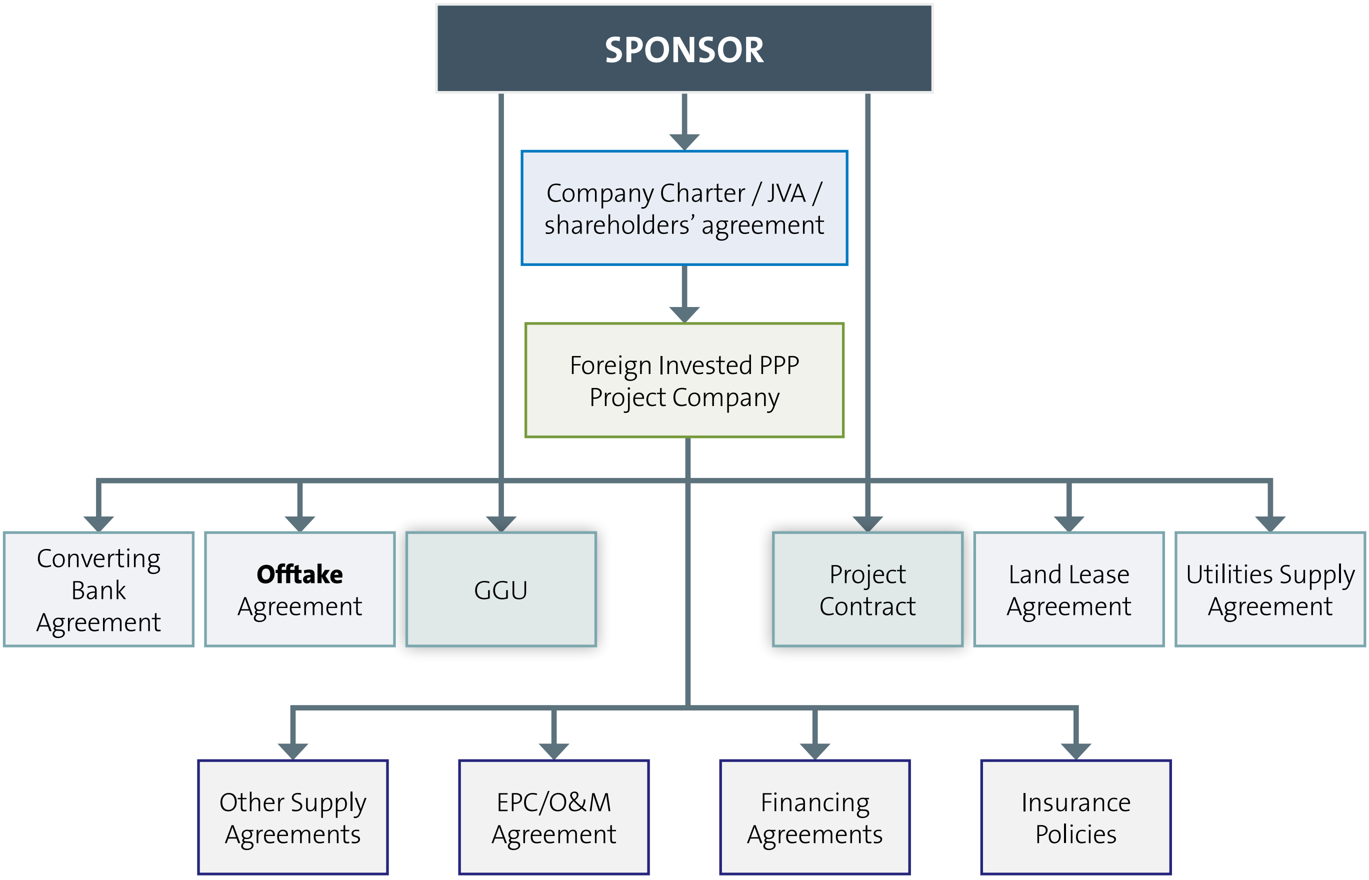
- The investor shall pay a security deposit for project implementation of 1–3% of the investment capital of the project.
- The project term shall be no more than 50-70 years, depending on the location of the project. Upon expiry of such term, the investor may apply for extension of the term.

3. STRUCTURING ISSUES

3.1 Project structure

While no two projects are the same, and each requires careful consideration in terms of structuring, the below diagram illustrates a typical contractual structure for a PPP project implemented using project finance. In Vietnam, a number of BOT/PPP power projects have been successfully financed by international lenders using this structure, though not under the current PPP Law.

In a non-PPP project, to obtain international financing a similar contractual structure is expected, except that there may be no project contract[22] and GGU.



3.2 Financing structures

(a) Project finance

Project financing is the provision of funding for a discrete single-purpose investment on a non or limited-recourse basis, with repayments principally being made from the income streams generated by such investment. So far, large-scale infrastructure projects in Vietnam have typically been financed on a non or limited-recourse project finance basis.

Typical sources of funding for large infrastructure projects have come from commercial banks (including international and local banks), development finance institutions, export credit agencies, bonds, equity, packaged up with additional credit support such as completion guarantees, performance bonds, deferred payments, and insurance.

22 We note that as at November 2021, under a draft decision on renewable energy development, the project company must also enter into a project contract with the relevant provincial PC, but other than that there would be no project contract under the general investment law regime.

(b) Bankability issues

(a) Key bankability issues

Infrastructure projects commonly face issues and risks that can't be effectively mitigated or addressed without involvement from third parties – notably, the state. While many investors have sought GGUs to backstop certain risks (eg state-owned entity obligations, currency availability and convertibility), the Government has only agreed to them in a limited number of cases for projects considered to be nationally significant (around 10 so far). In recent years, the scope of GGUs has become more limited as the Government seeks to reduce its exposure to privately funded projects, claiming that improvements in the country's legal system and general market conditions don't justify the previous levels of support.

Below, we identify the top 10 issues we see affecting the bankability of infrastructure projects in Vietnam, and comment on how they might be addressed in a GGU – via PPP project contracts or otherwise.

1. Nationalisation and compensation

Though rare, nationalisation is a major government risk for foreign investors. While protection against nationalisation is provided in domestic law and international investment treaties, this protection is often not adequate for specific projects, and needs to be further addressed in project agreements.

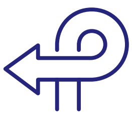
Notably, in recent draft GGUs, a guarantee against nationalisation has been absent. In PPP project contracts, nationalisation would usually be treated as a Government event for which full compensation is payable.

Political risk insurance, from private and/or multi-lateral sources such as MIGA, might also be a tool to manage nationalisation risk.

2. Legality of project documents

The risk of project contracts not being valid or permits being challenged is best mitigated by a specific Government commitment that the documents, as well as rights and assets created under them, are valid and lawful under Vietnamese law. This might take the form of a legal opinion provided by the Ministry of Justice, relied on by investors and lenders. If a key document is found to be invalid, unenforceable or terminated, it would then become a Government event for which compensation is payable.

3. Changes in law or policy



In recent years, protection against changes in law for BOT power projects has been included in BOT contracts. This regime provides contractual protection to investors from unfavourable changes in law. Investors may also be asked to share with the state the benefits that arise from a favourable change in law.

The guidance for formulating model contracts in Decree 35 states that the model contract will provide for contract amendments in the case of change in law or policies. It also states that the model contract will regulate, among other matters, changes in law or policies that affect the implementation of the project contract and the revenue loss sharing.

Protection of this nature for non-PPP projects is limited to the protections set out in the Law on Investment. There is no clear precedent to date as to how willing the authorities will be in negotiating a change in law clause in a project contract (if any) if a project is implemented on a non-PPP basis.

4. Approvals and permits

There is currently no protection available under domestic law or investment treaties for difficulties or delays obtaining relevant approvals and permits for a project. PPP project contracts and/or the GGU may provide Government commitments to assist investors with procedures. Again, this support is limited in practice and is unlikely to be expressly forthcoming for non-PPP projects.

5. Foreign currency conversion

At the start of Vietnam's PPP regime, the Government was expected to provide foreign currency availability and conversion guarantees for 100% of the project's foreign currency needs. More recently, such guarantees have been limited to 30% of Vietnamese Dong revenue after deducting local expenses. This 30% limit has now been enshrined in the new PPP Law.

Foreign currency guarantees can also be given under the general investment law regime if there is appetite from the Government to give support. It is expected that the 30% threshold will still apply in such cases, although the law does not limit it expressly.

Private currency hedge products may be available to mitigate this risk but, obviously, come at a cost that can adversely affect project economics.

6. Guarantee of performance by state entities

Many projects rely partially or wholly on revenue streams from state-owned offtakers. If they default on their obligations, payment or otherwise, projects can quickly grind to a halt. Previously, the Government was willing to provide full guarantees of state-owned counterparty obligations, to give comfort to investors and lenders. However, in keeping with contemporary policy, the Government now seeks to significantly limit the scope of such guarantees, arguing that the market should make its own risk assessment based on past performance and credit ratings of state entities such as EVN.

In practice, the Government may negotiate limited guarantees of financial obligations of key state entities for some major projects. But, again, it is difficult to see such guarantees being offered outside of the PPP regime, and even then, it would be in only highly nationally significant projects.

7. Governing law: Vietnamese law vs. foreign law

Foreign investors and lenders have indicated a strong preference for a well-developed foreign law, such as English or Singaporean law, to govern key project contracts, in order to provide maximum certainty. Vietnamese counterparties typically advocate strongly for Vietnamese governing law, arguing that they are more familiar with it, that the projects take place in Vietnam and that the law itself is sufficiently developed.

The practice to date has been for PPP project contracts to be governed by foreign law. However, the new PPP Law provides that Vietnamese governing law will be mandatory for the PPP project contract and any contract entered into between a Vietnam state body and investors or the project company. This means that under the PPP regime, foreign law can no longer be the governing law for the GGU and project contract.

8. International dispute resolution and enforcement of arbitral awards

As Vietnam is a party to the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards, it has agreed to allow enforcement of arbitral awards made in, or by, an arbitral tribunal of a country that is also a party to the Convention. However, the process requires recognition and enforcement by the courts of Vietnam (which have been known to refuse awards on the grounds that the process or award fails to comply with 'fundamental principles of Vietnamese law'). Since such principles are not clearly defined, Vietnamese courts have significant discretion in practice when it comes to enforcing a foreign arbitral award.

9. Early termination payments

Under the PPP Law, early termination payments are allowed only in very limited circumstances – specifically, when a PPP project contract is terminated due to national interest requirements, national defence and security and protection of state secrets, or when the contract signing agency is materially in breach of the contract. However, there is no formula for calculating the termination payments in these cases, so they would need to be negotiated on a bilateral basis.

The PPP Law appears to provide for only two scenarios where termination payments can be made – for national interest, to ensure national defence and security or to protect state secrets; and in case of breach by the contract signing agency. Decree 35 seems to allow the project contract to provide for termination payments in all cases. However, Decree 35 cannot go outside the ambit of the PPP Law, so there may not be much room for investors to negotiate this issue on the basis of Decree 35's apparent broader ambit.

It is critical that project sponsors negotiate clear and detailed agreements on termination payments in project documents. Essentially, a termination following a breach by Government parties should entitle the sponsor to a payment that sufficiently covers all equity and finance costs, plus an agreed return on equity. While termination payments by the sponsor or project company are more vexed, ideally the sponsor should be seeking to cover at least its financing costs. Termination following force majeure will usually have a separate regime, depending on which party is affected by it.

10. Security gaps

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(c) Other key Vietnamese law issues related to financing

1
Borrowing limits

Under Vietnamese law, a borrower issued with an 'investment policy approval' and/or an 'investment registration certificate' approving its investment project may only borrow long-term funds (ie borrowing with repayment terms of a year or more) to implement that project – up to the limit of the difference between the borrower's equity and the total amount of registered investment capital specified in its investment registration certificate.

2
Overall national borrowing limit

There is an overall limit on the total amount of foreign loans for the whole country approved by the PM for each year. Technically, if the national loan limit for the year (which we understand is around USD5.5 billion/year) is exceeded, registration of the loan, a prerequisite to disbursement of long-term loans, may be refused by the State Bank of Vietnam.

3
Thin capitalisation

In line with the PPP Law, an investor's equity ratio must be no less than 15% of the total investment capital of the project.

There is also a thin capitalisation requirement for non-PPP project companies using land leased from the state, being 20% for projects using a land area of less than 20 hectares and 15% for projects using 20 hectares or more.

There may also be further thin capitalisation requirements in line with regulations governing specific sectors. Project lenders will also impose their own equity controls as a condition of finance.

4. FINAL WORDS

Although the need for high-quality modern infrastructure in Vietnam continues to grow steadily, the legal environment underpinning projects is becoming increasingly complex and nuanced. In particular, the PPP Law has introduced a number of changes that will have a material impact on projects. This includes those that were already in advanced development stages before its effectiveness. The changes have not yet been tested, and it will take time to see how these play out in practice.

The policy position enshrined in the PPP Law is that private investors and lenders ought to share more risk with the state. Put another way, the Government's position is that, as Vietnam and its legal system and markets mature, the Government should have less responsibility to backstop project feasibility. While this is a reasonable position, it remains an open question whether the market will accept it; and, just as importantly, how positions will develop between lenders seeking certainty and sponsors seeking to develop and operate projects that stand or fall on their own merits, without recourse to parent company balance sheets.

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