

# Initial Public Offering (IPO) – An Effective Tool to Increase Profit Before Tax on Asset in Vietnamese Enterprises

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## ABSTRACT

*Over the last few years, Vietnam has witnessed a very strong growth in its Initial Public Offering market. The total capital in the Vietnamese stock market at the highest point (at the end 2007) was estimated to be 35 billion USD, accounting for 50% of the GDP. However, among nearly 300,000 enterprises in Vietnam, only 443 companies listed on stock market (up to November, 2009).*

*Profitability is the primary goal of all business ventures. Without profitability, the business will not survive in the long run. Measuring current and past profitability and projecting future profitability is very important (Michael, 1995). Profit before tax on asset (PBTA) takes a very importance role in the durable development of enterprises.*

*The purpose of this study is trying to investigate how Initial Public Offering makes a great impact upon the PBTA (Profit before Tax on Assets) of the Vietnamese enterprises and provides some decisions support for entrepreneurs in planning a public offering sometime in the future. The objectives of this study are (1) to investigate the significance impact of IPOs in enterprise's PBA in the Vietnamese stock market through profit before tax on asset, (2) to give suggestions and to encourage non-listed enterprises to become an IPO. The study is performed in two steps. The first step determined whether an IPO affects firm performance or not by collecting and analyzing around 57 listed companies. The second step used a statistical method to answer the question: what are positive impacts between the pre and post IPO's PBA on Vietnamese firms. Finally, a number of suggestions and implications for further research will be presented.*

**Keywords:** *Impact, Initial Public Offering (IPO), Stock Market, Vietnam*

## BACKGROUND OF STUDY

This research was conducted based on the following motivations.

First, a number of past studies have pointed out that the stock market plays an important role in economic development in every country (Richard, 1997). An economic recession, depression or financial crisis may eventually lead to collapse of a stock market.

Second, profitability, together with sales revenue, efficiency and employee income, is one of the most important factors that presents an enterprise's operating efficiency. It is abilities of a company to earn profits. Profit before taxes on assets (PBTA) is a ratio that measures company's earnings before taxes (EBT) against its total assets. The ratio is supposed as an indicator of how effective a company is using its assets to generate earnings before contractual obligations must be paid.

Third, among the 300,000 firms in Vietnam, up to August 2009, only 443 firms are listed in the stock market. The important question has been asked, how and why does IPO impact on the profitability of

Vietnamese enterprises? If firms could have better profitability after IPO, why did so few Vietnamese companies go public?

Finally, Vietnamese stock market only opens less than eight years, therefore there are only few empirical analyses of research in Vietnamese stock market and corollary of insufficient information for investors, and those are the reasons why this research was so urgent to be conducted.

## OBJECTIVES OF THE STUDY

The primary objective of this study is to find out the impact of IPOs in profitability in the Vietnamese stock market through financial ratios and to give suggestions and to encourage non-listed enterprises to progress into an IPO. This paper will compare the pre- and post- IPOs' profitability especially profit before tax on asset by using SPSS and statistic method named non-parametric Wilcoxon signed-ranked to test significant changes in the mean (median) of profitability.

Finally, this research will give suggestions and implications for non-listed enterprises in Vietnam on the way to IPOs.

## TERMINOLOGY

### Initial Public Offering (IPO)

An Initial Public Offering (IPO) is the first sales of stock by a private company to the public. IPOs are often issued by smaller, younger companies seeking capital to expand, but can also be offered by large privately owned companies looking to become publicly traded (Black, B., & R. Gilson, 1998).

### Profit Before Taxes (PBT)

One variable is very important in calculating profitability measurements that is the profit before taxes (PBT). PBT is a profitability measurement that measures a company's profits before the company has to pay corporate income tax. This measurement is to deduct all expenses from revenue including interest expenses and operating expenses, but leaving out the payment of tax.

### Profit Before Taxes on Assets (PBTA)

Profit before taxes on assets (PBTA) is a ratio that measures company's earnings before taxes (EBT) against its total assets. The ratio is supposed to be an indicator of how effective a company using its assets to generate earnings before paying the tax. It is calculated by dividing company's profit before taxes (PBT) or earnings before taxes (EBT) by its total assets; PBTA is displayed as a percentage.

PBTA tells us how efficient profits are being generated from invested capital (assets) employed. For example, the assets in a book company are valued on the basis of their original cost (less any depreciation). A high profit before taxes on assets does not always mean that we could buy the same assets today and get a high return. Nor does a low return imply that the assets may be employed better elsewhere (Richard *et al.*, 2001).

In a competitive industry, firms can expect to earn only their cost of capital. Therefore, a high profit before taxes on assets is sometimes cited as a signal that the firm is taking advantage of a monopoly position to charge excessive prices.

## RESEARCH HYPOTHESIS , RESEARCH METHODOLOGY AND DATA COLLECTION

### Research Hypothesis

In 2006, Lubos and Taylor had studied firm profitability after an IPO, this study focused on the average profitability of private firms. It predicted that firm profitability should decline after the IPO and compared the sample of 7183 IPOs in the US between 1975 and 2004. Many IPO models assumed that the entrepreneur has private information about her own firm (Chemmanur and Fulghieri, 1999). Asymmetric information may properly explain some of the observed post-IPO declines in profitability, but it is not clear in the statement of how it would generate higher declines for firms with more volatile profits and firms with less uncertain average profits.

Another possible explanation for the profitability pattern is earnings management. Teoh, Welch and Wong (1998) argued that firms opportunistically inflate their earnings through discretionary accruals shortly before going public. However, firms that willing to manipulate their earnings around the IPO are likely to manipulate them after the IPO as well. Such firms are likely to smooth their post-IPO earnings, given the apparent market preference for less volatile earnings.

In 2006, there was a boom in the Vietnamese stock market and many companies became famous after their IPO; but what about their profit before taxes on assets? Can they earn more PTBA after their IPO and is there a positive impact on companies and their PTBA in Vietnam?

Based on the objectives and the questions of this study, the following hypothesis is offered as follows,  
*Ho: There is no significant difference between the pre- and post- IPO' firm profit before taxes on assets (PTBA) in Vietnam*

*H1: There is a significant difference between the pre- and post- IPO' firm profit before taxes on assets (PTBA) in Vietnam*

### Research Methodology

To test the hypothesis mentioned above, this research performs the comparisons of pre- and post- IPO profitability performance measure. The data are obtained from a three-year period (from one year before, the year of the IPO, and one year after) in the Vietnam stock market. The study computes the mean of profit before taxes on total assets, profit before taxes on total assets in each firm covering the one-year period prior to IPO (year-1), the year of IPO (year 0), and one year following IPO (year +1). The following step is to conduct nonparametric test and Wilcoxon method to make the comparison to answer the research questions. This method was also carried out by many previous studies such as Nellis and Kikeri, (2004), Truong et al. (2004), and Toan N (2007).

### Sampling Design

At present, there are two Securities Trading Centers in Vietnam; Hanoi and HoChiMinh with a total number of companies of 443 (up to November, 2009), in which 65 companies initially listed in 2008 (Thieu, 2007) and only 41 companies had listed before 2006. To support this study, samples from 52 companies of HoChiMinh Securities Trading Center and 5 companies of Hanoi Securities Trading Center will be used. These companies will be selected for the samples according to their scale and their field so that it can represent for the whole population.

## Data Collection

To gather the data for this empirical study, first, it is necessary to determine which kind of data or information would be useful and helpful. Data are collected by choosing Vietnamese enterprises that have offered IPOs, listed on the Vietnamese stock exchanges by the end of December 2008 so that these firms should have at least one year pre-and post-IPO financial and accounting data.

Information on pre-IPO is collected from the local state-owned enterprise reform board (each province has its own SOE Reform Board), the General Department of Taxation, the General Statistic Office and the Corporate Finance Division as well as some large banks in Vietnam because these enterprises have to submit their audited financial information and their accounting statements to these organizations. Data collected includes data on profits before taxes, total assets for at least 1 year prior to IPO that are almost presented in a company's offering prospectus and other primary documents.

Moreover, from the list of IPO enterprises on the Vietnamese stock exchanges, it is possible to get the pre-IPO financial data by downloading information from company-owned websites and the news reporting websites as well as other sources on the internet. By governmental regulation, these companies have to reveal all their financial and accounting information to investors publicly. It is economical and timesaving by doing so through the internet.

The post-IPO financial and accounting data are rather easy to collect for the reason that they are all published on the Vietnamese stock exchange every quarter of the fiscal year. Alternatively, the data can be obtained by downloading from company-owned websites, large banks' websites on the internet, and secondary data sources. This data and relevant information are also easily available to be acquired. The companies have to, by regulatory law, disclose all their financial and accounting information in annual reports to investors and publicize their annual reports.

## RESULT AND DISCUSSION

After collecting the data from 57 listed companies, we used SPSS to run the data and the details of result as table 1. Table 1 shows that profit before taxes of some companies have been increased in the period of 2 years before IPO to 2 years after IPO. There were 55 companies' profits before taxes have been increased, that was 96% of total. In such period, 54 companies that are 95% of total companies have profit before taxes increased. In conclusion, most of companies in both periods have profitably done their businesses and increased their profits before taxes by reasonable operation, business and methods of personnel organizations.

From the Table 1, it is clear that the mean of PBT remarkably increased from 12 to 42 billion VND before and after IPO. Table 1 also shows 75% of companies had an increase in PBT after IPO. For instance, the second year after IPO compared to the second year before IPO, PBT increased from 16 to over 41 billion VND. Similarly 50% among the 57 companies increased their PBT, and especially, 25% accelerated the value of profit more than threefold from 2.88 to 8.37 billion VND (two years before and after IPO).

**Table 1. Descriptive Statistics of Profit before Taxes**

Unit: Million VND

	N	Mean	Std. Deviation	Minimum	Maximum	Percentiles		
						25%	50 % (Median)	75%
PBT of year -2	57	12,089	15,436	308	76,926	2,880	6,521	16,118

PBT of year -1	57	14,930	17,738	311	88,785	3,376	8,688	19,014
PBT of year 0	57	18,754	22,930	344	112,030	4,896	9,256	22,642
PBT of year 1	57	37,323	77,774	264	544,080	7,235	14,673	31,828
PBT of year 2	57	42,358	80,462	724	547,729	8,373	18,256	41,005
PBT of year -2 to year 2	Number of increasing						55	
	Percentage						96%	
PBT of year -1 to year 1	Number of increasing						54	
	Percentage						95%	

Note. 1USD =18,000VND

However in the larger companies, the value of PBT was dramatically increased more than seven-fold from 76.9 to over 547.2 billion VND over two years before and after IPO. The same trend was demonstrated in the smaller companies where the PBT increased from 0.3 to 7.2 billion VND through the period of two years before and after IPO. Furthermore, it is clear to understand the fact that in one year after IPO, the minimum of PBT slightly reduced but the mean of PBT dramatically increased, comparing to previous IPO (from 14,930 in one year before IPO to 37,323 in one year after IPO). In the smaller companies, PBT was a small number comparing to other companies.

Finally, there is no difference between companies' earned PBT and its mean values through the observation of all companies. For instance, 75% of the companies in the first year after IPO had value of PBT over 31 billion VND while its mean value was more than 37 billion.

Table 2 shows that most of companies increase their total assets in the period of 2 years before IPO to 2 years after IPO. There are 56 companies that have their total assets increased, accounting for 98% among all companies. There is only one company hasn't increased their total assets because it's a construction company (Construction and Infrastructure Development Joint Stock Corporation company), the company used it's assets to pay for its debt. In the short term, such figure is equivalent with 53 enterprises and that is 93%, respectively. It proves that the companies have launched right solutions to attract more capital and investment in the assets after IPO. It is easy to see that the 25th company has total assets that significantly increased after IPO, from nearly 41 (asset of year -1) to more than 59 billion VND (asset of year 1). Similarly, the 50th and 75th companies have increased their total assets in the period of one year before and after IPO. 75% of the companies have total asset over 209 (asset of year -2) and dramatically increasing to 340 billion VND (asset of year 2). Total assets of smallest companies (minimum) one year after IPO, which was compared to the one before IPO were accelerated from 6 (asset of year-1) to over 12 billion VND (asset of year 1). Similarly, in the largest companies, the value of asset also considerably climbed up from 7,547 to 12,569 during the period of two years before and after IPO.

Finally, in the year before IPO, 75% of the companies had total assets over 209 billion VND, but its average reached up 327 billion VND. This result could explain why there was some high value of total assets in some companies (the maximum is 7,547 billion VND).

Table 3 shows that the profit before taxes on assets (PBTA) has reasonably increased for all sample companies in both long and short phases. Specifically, in the long period, the value of PBTA mean (median) increased from 10.09 (6.68) to 12.40 (10.09) percent after IPO. In the meantime, these values are 10.78 (7.68) and 12.63 (9.22) percent in the short period. Increases of PBTA mean (median) values in both periods are found to be statistically significant with p-values 0.003 and 0.00142 (at 0.01 levels). Thus, as indicated earlier, the values of PBTA showed good improvements in firms after IPO.

The result from table 3 reveals that there is a significant increase in the mean of profitability before IPO and after IPO with the p value. (2-tailed) = 0.000. We accept the Hypothesis H1: There is a significant impact between the pre- and post- IPO' firm profitability in Vietnam.

**Table 2. Descriptive Statistics of Total Asset**

	N	Mean	Standard Deviation	Mini-mum	Maxi-mum	Unit: Million VND Percentiles		
						25 %	50 % (Median)	75%
Asset of year -2	57	327,944	1,045,232	4,562	7,547,006	33,900	76,192	209,176
Asset of year -1	57	362,946	1,151,264	6,056	8,301,707	41,513	82,867	239,711
Asset of year 0	57	430,267	1,442,938	13,345	10,604,802	44,853	107,080	242,419
Asset of year 1	57	505,706	1,566,853	12,211	11,562,321	59,343	155,037	316,033
Asset of year 2	57	606,106	1,761,043	21,571	12,569,456	68,232	165,000	340,583
Asset of year -2 to year 2	Number of increasing					56		
	Percentage					98%		
Asset of year -1 to year 1	Number of increasing					53		
	Percentage					93%		

Note. 1 USD = 18,000 VND

**Table 3. Results on Profit before taxes on Assets in IPO Companies**

Sample	Variables	N	Mean (median) before	Mean (median) after	Mean (median) difference	Z-statistics for difference in performance (after - before)	p-value	Percentage of firms that changed as expected
Long Period Sample (-2 To +2)	PBTA	57	0.1009	0.1240	0.0231	-2.96754	0.00300**	81.63%
Short Period Sample (-1 To +1)	PBTA	57	0.1078	0.1263	0.0231	-3.19000	0.00142**	77.55%

Note. \*\* Significant at the 0.01 level  
1 USD = 18,000 VND  
(-2 To +2) means two years before and after IPO  
(-1 to +1) means one year before and after IPO

## RECOMMENDATION AND LIMITATION

Throughout the data analysis, it is obvious that IPOs have a positive impact on firms' profit before taxes on assets in Vietnam, however until now there are only a small number of listed companies in Vietnam (accounting for only 1% of the total companies). Vietnamese government should launch more policies to encourage enterprises go public. Some policies are recommended as followed:

Firstly, in the past Vietnam subsidized its economy, though state owned enterprises equalization process have been performed for many years, many of them still operated inefficiently. The government should carry strong methods to help those inefficient operated state owned enterprises and then IPO such enterprises.

Secondly, the government should loosen compulsory policies for enterprises which plan to go to IPO like capital and so forth so that IPO process is more favorable and there will be more and more companies listed in Vietnam Securities market.

Lastly, in the Vietnamese stock market nearly 70% investors are individual investors and they are easily affected by the crowd psychology. VN Index is easily affected by the rumor. Government should take strict disciplines to prevent rumors on the Vietnamese stock market such as giving a punishment to the investors for spreading rumors.

On the side of Vietnamese companies, it is predictable that the Vietnamese economy will continue to post a high growth rate in 2009, even in the global economic crisis. Investment by foreign investment firms and privately owned domestic firms is thriving. In this context, every company wants to show good performance in order to attract more capital. The positive results from IPO process will become a good motivation for Vietnamese companies to promote their own decisions to offer IPOs in Vietnam.

#### APPENDIX 1: PROFIT BEFORE TAX ON ASSET IN IPO COMPANIES

No.	Code	Company	Year of IPO	PBTA (%)				
				-2	-1	0	1	2
1	BT6	Chau Thoi Concrete Corporation	2002	0.06	0.06	0.07	0.13	0.16
2	SAV	Savimex	2002	0.38	0.36	0.33	0.35	0.37
3	RAL	Rang Dong light Source & Vacuum Flask Joint Stock Company	2006	0.09	0.14	0.08	0.08	0.08
4	PJT	Petrolimex Joint Stock Tanker Company	2006	0.10	0.09	0.11	0.11	0.13
5	TRI	Saigon Beverages Joint Stock Company	2001	0.06	0.07	0.07	0.08	0.05
6	GIL	Binh Thanh Import-Export Production and Trade JSC	2002	0.04	0.04	0.04	0.04	0.10
7	TS4	SEAFOOD JOINT STOCK COMPANY No 4	2002	0.05	0.12	0.11	0.07	0.07
8	HAS	Hanoi P&T Construction & Installation Joint stock Company	2002	0.04	0.04	0.05	0.05	0.05
9	KHA	Khanh Hoi Import Export Joint Stock Company	2002	0.00	0.00	0.00	0.01	0.01
10	AGF	AN GIANG FISHERIES IMPORT & EXPORT JOINT STOCK COMPANY	2002	0.40	0.39	0.52	0.44	0.40
11	VNM	Vietnam Dairy Products Joint-Stock Company	2006	0.09	0.15	0.20	0.23	0.21
12	PGC	Petrolimex Gas Joint Stock Company	2006	0.16	0.15	0.14	0.18	0.07
13	VIP	Vietnam Petroleum transport Joint Stock Company	2006	0.10	0.14	0.20	0.14	0.17
14	HAP	Hai Phong Paper Joint Stock Company	2000	0.11	0.11	0.11	0.12	0.11
15	BBC	Bien hoa Confectionary Corporation	2001	0.27	0.27	0.12	0.30	0.26
16	SAM	Cables and Telecommunications Material Joint Stock Company	2000	0.02	0.03	0.03	0.02	0.05
17	BPC	Bim Son Packing Joint Stock Company	2002	0.04	0.05	0.05	0.15	0.15

18	CAN	Ha Long Canned Food Stock Corporation	2001	0.22	0.22	0.42	0.31	0.22
19	KHP	KHANH HOA POWER JOINT – STOCK COMPANY	2006	0.13	0.17	0.14	0.11	0.11
20	BTC	Binh Trieu Construction and Engineering Joint Stock Company	2002	0.18	0.16	0.15	0.15	0.11
21	PMS	Petroleum Mechanical Stock Company	2003	0.12	0.12	0.11	0.20	0.16
22	SFC	Saigon Fuel Joint-Stock Company	2004	0.06	0.06	0.02	0.04	0.08
23	GHA	HAPACO JOINT - STOCK COMPANY	2006	0.11	0.10	0.11	0.09	0.04
24	VTC	VTC Telecommunications Joint Stock Company	2003	0.03	0.03	0.03	0.21	0.14
25	SSC	Southern Seed Joint Stock Company	2005	0.07	0.06	0.07	0.07	0.10
26	TNA	Thien Nam Trading Import Export Corporation	2005	0.05	0.05	0.06	0.06	0.15
27	DHA	HOA AN JOINT STOCK COMPANY	2004	0.15	0.14	0.14	0.20	0.18
28	BMP	BINHMINH PLASTICS JOINT STOCK COMPANY	2006	0.06	0.05	0.05	0.09	0.10
29	BTS	But Son Cement Joint Stock Company	2006	0.06	0.07	0.06	0.09	0.13
30	DTC	Vigracera Dong Trieu Company	2005	0.17	0.19	0.14	0.21	0.15
31	REE	REE - Corporation	2000	0.17	0.17	0.18	0.19	0.16
32	PPC	Pha Lai Thermal Power Joint-stock Company	2007	0.25	0.27	0.36	0.33	0.35
33	VSH	Vinh Son - Song Hinh Hydropower Joint Stock Company	2005	0.03	0.02	0.06	0.03	0.03
34	SGC	SAGIANG IMPORT EXPORT CORPORATION	2006	0.09	0.07	0.08	0.07	0.03
35	FMC	SAO TA Foods Joint Stock Company	2006	0.29	0.29	0.25	0.30	0.29
36	RHC	Ry Ninh II Electric Joint Stock Company	2006	0.12	0.12	0.14	0.14	0.25
37	TTP	Tan Tien Plastic Packaging Joint Stock Company	2006	0.07	0.12	0.17	0.11	0.16
38	CLC	Cat Loi Joint Stock Company	2006	0.06	0.06	0.07	0.08	0.08
39	DHG	HAU GIANG PHARMACEUTICAL JOINT STOCK COMPANY	2006	0.09	0.09	0.10	0.10	0.10
40	DHA	HOA AN JOINT STOCK COMPANY	2004	0.06	0.06	0.07	0.07	0.12
41	BMC	Binh Dinh Minerals Joint Stock Company	2006	0.17	0.17	0.19	0.21	0.20
42	CII	Ho Chi Minh City Infrastructure Investment joint Stock Company	2006	0.11	0.09	0.10	0.05	0.05
43	CYC	Chang Yih Ceramic Joint Stock Company	2006	0.10	0.13	0.08	0.08	0.07
44	CID	Construction and Infrastructure Development Joint Stock Corporation	2005	0.13	0.08	0.09	0.10	0.12
45	CJC	Central Area Electrical Mechanical Joint Stock Company	2006	0.04	0.07	0.09	0.08	0.08
46	NKD	North Kinhdo Food Joint Stock Company	2004	0.04	0.04	0.03	0.04	0.05
47	KDC	Kinh Do Corporation	2005	0.04	0.03	0.11	0.12	0.12
48	MHC	HANOI MARITIME HOLDING COMPANY	2005	0.11	0.16	0.08	0.07	0.08
49	PNC	Phuong Nam Culture JointStock Corporation	2005	0.04	0.04	0.04	0.09	0.09

50	BHS	Bien Hoa Sugar Joint Stock Company	2006	0.05	0.08	0.09	0.13	0.10
51	DIC	DIC INVESTMENT AND TRADING JOINT STOCK COMPANY	2006	0.04	0.04	0.04	0.06	0.03
52	DMC	Domesco Medical Import - Export Joint Stock Corporation	2006	0.02	0.02	0.03	0.04	0.04
53	DRC	Da Nang Rubber Joint Stock Company	2006	0.03	0.07	0.03	0.06	0.06
54	ALT	Alta Company	2006	0.03	0.03	0.05	0.06	0.06
55	DNP	DongNai Plastic Joint Stock Company	2006	0.07	0.06	0.07	0.07	0.06
56	COM	Materials - Petroleum Joint Stock Company	2006	0.02	0.10	0.09	0.08	0.09
57	NHC	Nhi-Hiep Brike-Tile Joint Stock Company	2005	0.08	0.05	0.16	0.13	0.10

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