REFORM OF STATE OWNED ENTERPRISES
IN THE CONTEXT OF VIETNAM’S WTO ACCESSION

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PART A

REFORM – A VITAL ISSUE OF SOEs

I. Rationales for SOEs reform:

- The Resolution of the 9th Party Central Committee, Third Plenum, identified reforming and raising the efficiency of SOEs as a pivotal issue.

There are two main reasons, both subjective and objective, for SOE reform:

- Internal weaknesses of SOEs
- Acute challenges posed by international economic integration such as AFTA, APEC and the WTO in the future.

II. Assessment of current situation of SOEs’ business and production:

1. Achievements:

Over the past 10 years, we have shifted from the centrally planned and subsidised mechanism to market economy. This transition posed enormous challenges to SOEs. In addition, the 1997-1998 crisis exerted strong impacts on the Vietnamese enterprises.

In the context of complex developments and economic downturn in the world, SOEs have surmounted many challenges, survived and continued to grow. They contributed substantially to the great achievements of Doimoi and national development, which lifted Vietnam out of socio-economic crisis to move to the stage of intensified industrialisation and modernisation under the socialist orientation. This is reflected in the followings:

- SOEs were able to control key areas of the economy, which is conducive to securing the state sector’s key role so as to ensure stability and socio-economic development, thus raising our country’s position and strength.

- SOEs accounted for a large proportion of GDP, budget revenue, export volume and foreign investment projects with worthy contribution made to the fulfilment of social policies.

- SOEs became more and more adaptable to the market mechanism. Their production capacity was expanded, expertise and management capacity raised, and competitiveness enhanced. Some new industries and enterprises with modern technology and advanced management have been gradually formed.

2. Weaknesses:

However, SOEs also have been exposed to weaknesses:

a. Small scale, irrational structure and failure to focus on key areas of the economy.

There are 5,655 enterprises nationwide with the total capital of VND 126,000 billion. On average, each enterprise has VND 22 billion, out of which 58.9% have less than VND 5
billion (including 18.2% enterprises with the capital of below VND 1 billion), 15.2% have VND 5-10 billion, and 25% have over VND 10 billion.

In Ho Chi Minh city, there are 709 SOEs with the total capital of VND 19,286,821, out of which 392 are under the direct management of the city with the capital of VND 8,701,243 billion (according to the 1997 statistics).

b. Backward technology and weak management capacity with low level of autonomy and accountability in business and production. According to a survey of the Ministry of Science, Technology and Environment, our technology is 10-20 years behind that of other countries.

Ho Chi Minh city’s socio-economic development plan forecasted that in 2010 the machineries used by the city’s industries would be several generations behind the world’s general level. Most machineries and equipment of the city’s industries are backward, except some assembly lines imported recently in the areas of garments and textiles, footwear, printing, plastic, frozen fishery, high-tech porcelains and so on. The level of backwardness varies among industries and enterprises of each industry. The average life of machineries is as long as 30-40 years, especially in the mechanical industry. Most enterprises have 10-20 year-old machineries.

According to the assessment of Ho Chi Minh City’s Industrial Department, 30% of enterprises’ machineries in the city are backward, 52% bellow average and only 17% relatively modern.

c. The management capacity of most of SOEs is low. Fundamental rights in terms of state management applied to SOEs are unclear, as are the rights of the State as the owner, the rights of the directors of SOEs, and the rights to use the capital and to autonomy in business and production. Some leaders of SOEs are incompetent and irresponsible; therefore fail to meet the requirements of the market economy. On the other hand, mechanisms and incentives for attracting a highly competent pool of managers are still missing. Most SOEs encounter financial difficulties and incur prolonged and unsettled debts. Moreover, independent accounting is not strictly implemented, leading to failure in determining losses and profits.

By 31 December 2000, the total capital of SOEs under the management of Ho Chi Minh city was VND 11,113,255 billion, out of which VND 839 billion were non-performing capital in forms of redundant fixed assets, low-quality materials and goods, bad debts, accumulative losses and other losses.

The total payable debts are VND 12,844,168 million, out of which VND 508,989 million are overdue debts.

The total debts to be recovered are VND 6,143,182 million, accounting for 52.12% of the total state allocated capital, out of which VND 301,233 million are bad debts. This indicates the state of capital appropriation happening to SOEs in Ho Chi Minh city, which leads to bad debts.
d. Low efficiency and competitiveness, rising overdue debts and a large number of unemployed and redundant employees. According to the 1998 evaluation of enterprises’ profitability, 40% were profitable, 40% fluctuated around the break-even point and 20% incurred chronic losses. In 2000, the numbers of profitable enterprises accounted for just over 40%, break-even ones reduced to 31%, and chronically loss-making ones accounted for 29%, of which most of them are enterprises with less than one billion VND capital operating mainly in provinces. In Ho Chi Minh City, in 2002, of the total of 267 enterprises, 236 were profitable accounting for 88.4%, 21 were loss-making accounting for 7.8%. The rate of return over capital was 8.4%, and over revenue was 4.1% on average. The rate of return over capital of 8.4% was lower than 12-15% of equitized enterprises. With regard to growth rate, despite the efforts made by state-owned enterprises in maintaining the average annual growth rate of 11% in the period of 1991-2000, compared to that of 14% in the private sector, and 20% in the foreign invested sector, this rate is still modest. The competitiveness of goods and products is especially low. The production cost of some products such as fertilizer, cement, iron, steel, and construction glass is 40% higher than imported price, especially 70% in the case of raw sugar.

Part B
Major Challenges facing State-owned Enterprises in the context of WTO Accession

I. Requirements of international economic integration:

In the Doi Moi process, the 3 Vietnam’s consistent economic policy pilars have been:

- Market economy moving along the Socialist line,
- Multi-sector economy,
- And, international economic integration.

- Vietnam is member of ASEAN and APEC. Vietnam has also concluded Bilateral Trade Agreement with the US.

Vietnam’s commitments in the ASEAN Free Trade Area-AFTA begin with the agreement on Common Effective Preferential Tariff-CEPT, under which Vietnam has to reduce tariff of almost all product lines from 20-40% to 10-15% by 2003 and to 0-5% by 2006.

When AFTA is implemented, Southeast Asia will become a trading area of high economic potentials. This arrangement will pay the way for the establishment of a regional link in the future with one or some currencies of high convertibility.

- Since 1998, Vietnam become member of the Asia-Pacific free trade area- APEC, an organization consists of 21 members of independent economies with the total population of 2 billions, accounting for 25% of the world area and 40% of the world population.

- On the 13th of July 2000, Vietnam concluded the US-Vietnam Bilateral Trade Agreement. This is a comprehensive Agreement on Trade in Goods, Intellectual Property Rights, Trade in Service,
Development of Investment Relations and Business Facilitation. Under this Agreement, Vietnam committed within 5 to 10 years to open almost all its markets to the US investors and importers.

- Vietnam has also actively engaged negotiations for membership status of the WTO, whose precursor is the GATT, an international organization, with close relations with the UN, established in January 1948 to reduce tariff and non-tariff barriers to international trade.

The WTO is a multilateral trade agreement, functioning under the fundamental principles of:

1. Non-discrimination in international trade. Most Favored Nation status is granted to imported goods regardless their origin.
2. Prohibition of domestic protection in the agricultural sector by putting in place discrimination policy and trade barriers including quota.
3. Emphasis of contacts and consultations to avoid violations of trade and tax interests, and trade barriers.

Non-discrimination principle is excised in reality by the provision of Most Favored Nation, in which member countries are entitled to the same treatment no less than the most preferential treatment granted to a country.

Prohibition of export subsidies means that domestic manufacturers shall not be granted unfair advantages and/or preferential treatment that allow them to predominate foreign markets.

On the grounds that one’s long-term benefits can only be augmented when one pays due attention to the creation of benefits for one’s partner. The WTO provides 40% reduction in tariff rate applicable to around 125 member countries. This tariff cut policy, on the one hand, reduces the average world tariff rate of around 5.2% to 3% and, on the other hand, facilitates international trade.

The WTO is the overture of foreign trade integration at the global level in the future. Inheriting the GATT experiences and operation principles, the WTO has become:

- The largest trade organization, functioning on its charter.
- The organization’s operation has been expanded to cover the aspect of trade related intellectual property rights.
- The organization’s mechanism for dispute settlement is more effective.

To some extent, the GATT, in substance, is the document that outlines fair competition and opposes unhealthy competition in international trade. These major standards on international competition provided by this Agreement include anti dumping practices, subsidies and countervailing measures, trade related to the state sector and restrictions, opposition of unhealthy competition relating to the protection of intellectual property rights.

The WTO, within its jurisdiction, has been active in the settlement of old and new issues of the international trade and competition among countries. These include investment, competition policy, trade and environmental standards, e-commerce, government procurement, trade facilitation measures, trade and development. These issues, in nature, closely relate to international competition. Environment and labor are social standards. These standards have some things to do with trade since these standards have a concern with international competitiveness in a way that social standards if linked with competition policy would be a weapon of developed countries to protect domestic market and force developing countries to make more concession.
The Agreements on Trade Related Investment Measures, Trade Related Intellectual Property Rights and the General Agreement on Trade in Service are related to competition policy. Given the ongoing formulation of the Law on Competition in Vietnam and to be effective, education and training in this regard should be conducted. Therefore, acceding to these Agreements, during the transition period, poses great challenges to Vietnamese enterprises.

II. Great challenges facing the State-owned enterprises:

A. Opportunities:

1. WTO membership will allow access to a vast market conducive to investment in technological renovation to increase productivity and reduce cost.

2. Helps attract foreign investment, import advanced technologies, restructure production, take advantage of scientific and technological advances and information resources to narrow the gap with developed countries.

3. Given the indispensable trend of international economic integration, early accession to the WTO requires urgent restructuring of the State-owned enterprises if they are to improve and establish their strong foothold in the global competitive environment.

B. Challenges:

1. Economic globalization is a irreversible trend of the human society. In this process, market economy plays a decisive role.

Domestic competition down the way surpasses national border and becomes international competition. In this connection, Vietnamese enterprises in general and State-owned enterprises in particular, have shifted from operating under the centrally-planed economy with government endowment to operating under the market mechanism, and from enjoying favorable domestic market conditions to export products to foreign markets to competing with foreign products in foreign markets and even in the domestic market.

2. Given China’ full-fledged WTO membership, Vietnamese competitive products such as consumer’s goods, textile and garment, footwear and agricultural produces are also the highly competitive products of China and other countries in the region including Thailand, Indonesia and the Philippines. These countries have been in advance of Vietnam in penetrating into the markets of developed countries. Thereby, Vietnam is under huge competition pressure.

3. The roadmap for preparation period has been set, however its implementation is too close to the deadline. As a result, many SOEs still find themselves unprepared for integration. Restructuring production, rearranging SOEs and promoting brand manes remain slow and passive. SOEs are still infected by the legacy of the centrally-planned economy. Some still maintain a blind conviction that the issue of competitiveness can be addressed through international relations and division, or government endowment.

4. Globalization has promoted the interdependence among countries in terms of economics, technology, culture and management, however it can also lead to production and market division. Despite positive
impacts such as increased productivity, lower costs, optimal capitalization of information resources, narrowed geographical distance, cross-cutting development and higher human qualification, globalization also brings about adverse impacts, namely increased inequality, economic crises, degraded environment and the uncertainty of commodity values to domestic and regional markets.

In the process of economic globalization, developing countries speed up economic development by attracting foreign investment, adopting advanced technology and restructuring economic sectors. Meanwhile, developed countries expand markets, take advantage of cheap labour and abundant natural resources to lower costs and ease the current contradiction between relatively excessive production and saturated domestic demand. As a result, in addition to enjoying mutual assistance and mutual benefits, developed countries and developing ones are in sharp conflicts over economic interests in which inequality is clearly seen from the financial flows to technological transfer, trade and environmental protection. In this regard, SOEs are facing many difficulties in competing with MNCs which are much stronger in terms of capital and technology.

PART C
STATE-OWNED ENTERPRISE REFORM

I. Guidelines

a) The State sector plays decisive role in firmly maintaining socialist orientation for economic and political development and promoting economic, political and social stability and development of the country. SOEs (including SOEs of 100% state capital and SOEs that the State holds controlling stake) must continuously reform, develop and enhance efficiency, maintain the key position in the economy, serve as an important physical tool of the State in macro-economic regulation, the major critical force facilitating the leading role of the State in the socialist-oriented market economy and the driving force of international economic integration.

b) SOEs must be rearranged to achieve appropriate structures with focus on key sectors and critical areas. SOEs should hold sufficiently major shares in major production and service sectors, and not necessarily hold large shares in all sectors, areas and products of the economy. The majority of SOEs must be medium and large sized with advanced level of technology. SOEs must be transformed to operate as companies. The process of SOE equitization must be accelerated, in which there is no need for the State to hold 100% capital. This should be regarded as a crucial part in making fundamental changes to enhance the efficiency of SOEs.

c) The management mechanism must continuously be renovated to enable SOEs to be self-sufficient and self-responsible to cooperate and compete equally with enterprises of other economic sectors in accordance to the law. State monopoly should be applied in necessary areas but must not be transformed into SOE monopoly.

While subsidies must be eliminated, sound investment policies and proper assistance are crucial for prioritized sectors and product areas. The function of state ownership agency and that of SOEs in business and production must be clearly distinguished. Direct ownership representatives of SOEs should be given more autonomy and higher responsibilities.
II. Goals and tasks

The ultimate goal of SOEs reform is to enhance efficiency of SOEs. The overall goals are to make SOEs strong and ensure their leading role in the economy.

SOE efficiency is evaluated comprehensively in all economic, political and social aspects.

The ten-year goals are to complete SOEs reform, enhance efficiency and competitiveness of SOEs to enable them to make important contributions to ensuring critical public services and social products as well as meeting the crucial needs of national security and defense. At the same time, SOEs must become the driving force of economic growth and serve as the foundation for industrialization and modernization along the Socialist line.

Set targets for the five-year period of 2001-2005

- Basically complete the rearrangement and restructuring of existing SOEs; equitize SOEs which do not need 100% State capital, merge, dissolve or liquidate SOEs which are not efficient; transfer, sell, contract or lease small scale SOEs which cannot be equitized and do not need State ownership.

- Transform SOEs which are 100% State capital to limited liability companies; revise policies on SOEs, develop a consistent legal framework to ensure self-sufficiency and self-responsibility of SOEs in business and production.

- Reform and make healthy SOEs’ finance, settle insolvent debt, labour redundancy and take measures to avoid recurrence of these problems.

- Reform and enhance efficiency of State General Corporations, and develop a number of strong economic Groups.

- Invest in the development and establishment of new SOEs which are crucial for key sectors and important areas.

- Renovate and modernize technology and management of the majority of SOEs.

III. Solutions and initial results

Since 1993, with three rounds of SOEs reforms, the numbers of SOEs have been reduced by 55% from 12,300 SOEs in 1991 to 5,655 in 2000 (mostly including small and local SOEs). Average capital of SOEs has increased from VND3.3 billion to VND22 billion.

From 1997 to 31 December 2002, 157 out of 434 SOEs were rearranged in HoChi Minh City, in which 94 SOEs were equitized, 55 SOEs were merged, one SOE was transferred, 11 SOEs were dissolved, three SOEs were put under Central management and one SOE became public entity.

- Average State capital of SOEs has increased from VND20 billion to VND37 billion.

- Regarding 92 equitized SOEs with total State capital of VND654.9 billion on book value, after financial problems and VND182 billion of capital loss (including bad debt, low-quality commodities in
stock, liquidated assets, redundant assets, etc) had been addressed, the total recounted State capital increased by VND840 billion out of VND1,112.8 billion of chartered capital. State capital on average accounts for 25% of chartered capital of joint stock companies. The State yielded VND451 billion and raised an additional capital of VND834.6 billion.

Equitized SOEs, having been able to mobilize investment capital to upgrade equipment and technology, became more efficient. Their rate of return over capital reach 12.5% per year (compared to 8.4% per year of SOEs).

- SOEs under the Trade, Construction, Land Administration Departments and District People Committees have been split and become corporations such as Saigon Trade Corp, Saigon Agriculture Corp, Saigon Housing Corp, Ben Thanh Corp, Saigon Tourism Corp with the aim of splitting the business function of SOEs from the function of State administrative management.

- SOEs adjust themselves better to the market mechanism. In 2002, the total revenue of 267 SOEs reached VND 26,384.554 billion, an increase of 10%, budget contribution grew by 8%, total profit was VND 1,092 billion, an increase of 225 billion, the rate of return over capital reached 8.4%.

However, these are only initial and modest results, which do not yet meet the demands, particularly in terms of productivity, quality and efficiency.

IV. Major goals and solutions

The period from now to 2005 is of great importance in the SOEs reform plan if we are to make fundamental changes given the challenges of international economic integration.

a. General directions:

Among the 269 enterprises:

- 105 will remain 100% State capital enterprises (57 commercial enterprises and 48 public utilities)

- 115 shall undergo ownership transfer (113 equitized and 2 sold)

- 01 will be transformed into an income-generating public agency

- 37 will be merged

- 11 will be dissolved and go bankrupt.

b. Major solutions:

1) Restructure economic sectors, make full use of the City’s status as a financial, scientific and technological center to focus investment on sectors of comparative advantages like electronics, precision mechanics, garments, leather footwear, plastics and chemicals. Step up trade promotion, register and promote trademarks of marketable and competitive products, carry out sectoral and regional development planning. In Ho Chi Minh City in particular, move polluting factories out of the city and invest in new technologies and machinery. Organize regular trade fairs to promote new products to
domestic and foreign customers. Launch the City Web and a dialogue mechanism with a view to helping solve legal and administrative difficulties that enterprises of all economic sectors may face. SOEs are required to get acquainted with e-commerce and the ISO quality control system, and develop their own websites to promote themselves.

2) With a view to encouraging the people and enterprises of all economic sectors to produce goods that the society needs and are not prohibited by the law, the Government has issued a decision on categorizing SOEs, according to which medium and large enterprises will be retained to operate in the key sectors of the economy, using advanced technologies, and accelerate the equitization of enterprises that are not 100% State-owned. This is considered a vital step towards enhancing the efficiency of SOEs. Merge, dissolve and bankrupt inefficient enterprises, transfer, sell, contract out and lease small-scale enterprises that cannot be equitized and does not need State control.

3) 100% State-owned enterprises must operate in necessary sectors, take the lead in the application of high technology, have the total capital of more than VND 20 billion and make the average budget contribution of at least VND 3 billion in the preceding 3 consecutive years.

Transform SOEs into 100% State-owned sole-proprietor limited liability companies:

The aim is to help enterprises transform their operation in accordance with the enterprise law and on the same legal platform as non-state enterprises. Measures to create a qualitative change for enterprises that are transformed and restructured include:

- Give more rights and responsibilities to the enterprises in doing business, ensure equality with other enterprises
- The State and mass organizations are holders of the enterprise.
- Create a change in the State - enterprise relationship, reduce State intervention and subsidies.
- Remove any non-economic obligation for enterprises.

According to the plan, 42 SOEs of Ho Chi Minh City will be transformed into sole-proprietor limited liability companies from now until 2005.

The State retains full ownership of public utilities operating in special sectors and dealing with urgent public issues. In the immediate, the City retains ownership of 48 such enterprises to ensure that each district with a population of 300,000 – 500,000 will have one public utility whose work will be to carry out maintenance of the basic infrastructures like the water, sewage, lightning and road systems. Organize bidding for public services contracts to encourage the participation of all economic sectors.

4) Reform and improve the efficiency of State-owned general corporations, form strong economic groups.

State-owned general corporations must meet the requirements in terms of business sector, have more than VND 500 billion of State capital, make average annual budget contribution of VND 500 billion in the preceding three consecutive years, have advanced technology and managerial capacity, products of good quality, high operation efficiency, and is competitive on the domestic and world markets.
State general corporations must have enough chartered capital, be capable of mobilizing capital from various sources to conduct multi-sectoral business, have a specialized sector, and linkages among member companies in terms of production, finance and market.

Complete the reform of State-owned general corporations to pool resources to manipulate core sectors of the economy, become the dominant force in ensuring macro-economic balance and stability, provide key products for the national economy and exports, make major contributions to the state budget, serve as the engine for economic growth, and proactively embark upon international economic integration.

Transform State general corporations into holding companies with the general corporation pouring capital into its subsidiaries which are either sole-proprietor limited liability or joint-stock companies of which the State holds controlling stake.

According to the City’s reform agenda, the City will maintain 6 existing corporations, establish another 3 new corporations and transform 7 companies with a strong capital position and other conditions into holding companies.

5) Accelerate the SOEs equitization:

Equitization is designed to create a form of enterprise with diverse ownerships, including the employees’ ownership, to achieve capital and state asset efficiency and better raise capital from the society for production and business activities in order to bring in a new momentum and dynamic management mechanism for SOEs and make best use of the mastership of the employees and shareholders.

SOEs that the state does not need 100% control of their capital will be subject to equitization regardless of their business and production situation.

Policies and mechanisms have been adopted and revised to prioritize the sale of shares to the employees to retain their interests. Only a share of equities will be sold to other holders. The enterprise valuation method has been improved to become more market-orientated. The value of landuse rights is considered to include in the enterprise valuation. Appropriate policies were also adopted for equitized SOEs. Equitized enterprises that are in difficulties will be given more preferences.

In 2003, the City has plan to equitize 50 enterprises.

6) Determined to take merge, dissolve and bankrupt ineffective SOEs

The state will not subsidize and finance debt owed by loss-making enterprises. The situation of handing out or “dilemma” will be stopped. For those enterprises that have less than 5 billion dong of capital and are not equitized, depending on their specific conditions, sale, contracting-out or lease will be decided. Loss-making enterprises that cannot be tranformed with above-mentioned mechanisms will be subject to merge, dissolution and bankruptcy.

The Law on Bankruptcy will be revised in a way that those who decided to establish enterprises are entitled to pronounce bankruptcy.

Between now and 2005, the City is expected to dissolve and bankrupt 11 and merge 37 enterprises.
7) Conduct auditing to have correct assessment the efficiency of enterprises. During the process of transforming enterprises into equitized and sole-proprietor limited liability companies, steps will be taken to evaluate enterprises based on market conditions and settle amounts of debt that cannot be paid to the state budget and banks. The SOEs Asset Management Company has been established to settle bad debts and assets to make healthy the corporate finance. During the past equitization process, enterprises with book value of 634 billion dong has been evaluated as 841 billion dong not to mention the settlement of 180 billion dong as unpaid receivables, poor-quality inventories, NPDs, liquidated assets...

In an effort to join the World Trade Organization, Vietnam has taken steps to integrate itself into the regional and world economy, broaden international cooperation and improve the competitiveness of the economy.

Economic globalization, an irreversible trend of humankind, will present both opportunities and challenges to countries in the world, especially developing nations.

Being a member of the WTO in the future, Vietnam will be in the position to expand market, increase export and better access new technologies – a fresh impetus for economic growth.

Having realized its position and advantages as well as opportunities and challenges as a result of globalization, Vietnam sees the need to accelerate the SOEs reform.

This is truly a comprehensive reform in all aspects from organization restructuring to policy revisions, from technology improvement to human resources training, from state management renewal to increased autonomy for enterprises so that enterprises (including enterprises that the State holds 100% control or controlling stake) will continue to reform themselves for further expanding business and improving efficiency, play a key role in the economy as an important macro-economic instrument of the State and successfully build the socialist-oriented market economy.