Managing giant economic groups in the globalization context

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During recent years, the issue of managing activities of giant economic groups has received great interest from the public. There are currently 8 state-run economic groups operating in key fields of the national economy functioning as an important tool for the state to regulate the economy and exercise industrial policies. However, organization model, management and governance structure of groups are big issues that need to be examined for further improvement.

I. Brief on the history of establishing giant economic groups

Some points on establishment history of giant economic groups

There are a number of giant economic groups in many countries in the world, differing in their names, organization forms and business fields. Many giant economic groups are multi-national companies, which have the operation in many countries, fostering the process of internationalizing production, deepening the assignment of international labors and forming the so-called “Global production network and value chain”. With their giant financial and technology potentials, strong brand names and great capability on market organization; such groups are increasing their activities, penetrating into other countries’ markets as an “invasion” in economy.

Without considering positive and negative effects of these giant economic groups, they were all established and develop under three modes.

The first is from the processes of capital accumulation and gathering under the market’s movement rules and production and business performance (for almost all giant economic groups in Western American countries and some other countries...).

The second is starting from a potential company; the majority is family companies selected and granted with special treatment by the Government to implement Government’s industrial policies. In other word, the purpose is to exercise structure policy in its both broad and deep meanings conveyed by this phrase. (Cheabols of Korea are typical ones)

The third is from some state-run giant economic groups established by the Government during the centralized-planning period, or through merging some state-owned companies of similar or closely linked fields of business to form state economic groups. (As the cases of Vietnam and China).
Below will provide a more detailed analysis on economic groups of Japan, Korea, and China whose models possibly affected the formation of Vietnamese economic groups.

1. The formation of economic groups in Japan (Keiretsu)

The prototype of Keiretsu appeared in Japan in the miraculous development period of Japanese economy after the 2nd world war.

Before Japan surrendered to the Allies, Japanese industry had been controlled by big groups (called Zaibatsus). Later, in the 40s of the previous century, those Zaibatsus were broken down, but the companies under those Zaibatsu associated with each other through buying shares in order to form horizontal association among different fields of business.

Each Keiretsu usually chooses one core bank for their operation. This bank provides credit to member companies of Keiretsu and seizes capital position in companies. Each core bank has a very big controlling role to companies in Keiretsu and it operates as a supervising and capital supporting organization to members in Keiretsu.

In fact, there two types of Keiretsu association: vertical and horizontal association. Whereas horizontal associated Keiretsu represents the relationships among entities which is normally around a bank and a commercial company (including many enterprises operating in different fields of business); vertical Keiretsu is a typical case of the organization and relationship like in one company (from the phases of production, material supply to product consumption in a specific field of business)

After the 2nd world war, Japan had 6 giant horizontal associated Keiretsus including: Mitsubishi, Mitsui, Sumitomo, Dai-Ichi kangyo, Fuyo and Sanwa operating in various industries from shipbuilding, mechanics, metallurgy, construction, chemical substances to commerce. Companies within one Keiretsu normally have similar business strategies, which helps make full use of possibilities for cooperation, mutual support, and experience sharing on management and business know-how, as well as methods of marketing and penetrating into markets.

In Keiretsus of vertical association, enterprises that provide materials and spare parts operate as peripheral entities to a big factory based on sharing technology, brand name and production and business processes.

2. Korea’s Cheabols model

In the 80s of the 20th century, Korean economy had made remarkable development step. One of the underlying factors lies in enterprises in general and Cheabols in particular with bold and ambitious business strategies.

Cheabols were formed from many companies having association in finance, business strategy and joint coordination in their operation.

Besides some state enterprises, almost all Cheabols in Korea were formed from member companies which were often controlled by one or a few numbers of founding families who took governing shares. Cheabols supported Government’s industrial policies and were favorably
preferred by the Government who provide resources for their development. President Park’s
government had nationalized banks and used them to provide abundant credit resource for
Cheabols to expand their business investment. Cheabols took full advantage of these
opportunities to expand their operation and exert influence. In 1996, the 30 biggest Cheabols
seized up to 40% of Korean output.

Since most Cheabols are governed by members in the same family, the management in those is
normally patriarchal and arbitrary. Their advantages are highly decisive and quickly responsive,
but the disadvantages are the feelings-driven and conservative approach in solving relationships
among members.

From legal perspective, Cheabols have no legal status, they are not a visible entity and activities
are carried out through members. However, the invisible shadow of Cheabol still covers all
activities of member companies. That is the unification in business strategies, the concentration
and allocation resources in a reasonable and flexible manner\(^1\).

3. State economic groups in China.

Since the years at the end of the 20\(^{th}\) century, China fostered the process of privatizing small
scale state enterprises; at the same time, concentrated its resources to implement many
preferential policies, developed giant economic groups to become strong enough groups in
order to compete in the context of globalization, especially in the key fields such as metallurgy,
oil and gas, shipbuilding, electronics, telecommunications, software, medicine,...(with the
policy of “seizing the big, leaving the small”).

This process started from the merging enterprises to create big corporations. Until those
corporations reach a specific size, they decentralized business rights to member enterprises,
hence improving the effectiveness of management and administration. After that was the phase
of diversifying ownership through the privatization to mobilize capital including foreign capital
linked with technology transfer to enhance the competitiveness. After accumulating financial
and technology capabilities, corporations fostered their oversea investment, made acquisition to
foreign enterprises to spread their influence and improve their global competitiveness.

It could be said that the process of forming state economic groups of China is strongly
embedded with Government’s mark and followed a closely inter-connected orders:
Concentration – Decentralization – Ownership diversification – Foreign investment attraction
(aiming at renovating technology and developing the market) – Oversea investment in order to
extend influence. All of this process aimed at targeting the requirement of improving
international competitiveness and implementing industrial policies.

II. State - owned enterprises and the formation of economic groups in Vietnam.

In the centralized - planning period, there were only 2 economic components operating in
Vietnam: state enterprises and co-operatives. Co-operatives mainly operated in agriculture,
small scale industries; and co-peratives did business in the localities of wards and communes.

\(^1\) According to Tran Khue, in Tuoi tre cuoi tuan Newspapers, 19/7/2010
The number of state enterprises reached over 12,000 with different sizes and managed by 3 levels: Ministries, People’s Committees of provinces and districts.

When the nation transited into the market economy, state enterprises did not adapt to new mechanism and they showed all weaknesses and flaws. Since 1992, Vietnamese government has implemented an intensive reform to state enterprises: A great number of enterprises (mainly under people’s committees of districts and suburban districts) were dissolved and merged. A great number of others with the majority being small and medium sized enterprises were privatized. As a result, the number of state enterprises quickly decreased from more than 12,000 in the beginning of 1990s to only 5,759 in 2000 and further reduced to 3,494 in 2007\(^2\).

Together with the process of privatization, Vietnamese government advocated the establishment of big corporations from corporations and big companies (not yet being corporations) that were already available in centralized - planning period. The first criterion (together with other criteria) to form corporations is the current amount of state-owned capital in enterprises. Accordingly, there are two types of corporations: Big corporations directly under the government with charter capital of VND1,000 billions and above, established according to Decision 91-TTg (corporations 91) and corporations with charter capital of the range from VND100 billions to under VND1,000 under the management of ministries and localities according to Decision 90-TTg (corporations 90). The purpose of the establishment was to build big state enterprises in key fields that play the main role in the national economy. Through these corporations, the government implemented state ownership in big state enterprises. Up to the year 2000, the whole nation had 18 corporations 91 and around 80 corporations 90\(^3\). Among those corporations, 21 corporations were ranked as special ones including corporations 91 and a few number of corporations 90 of big size, operating in important and essential fields (an example is Vietnam National Petroleum Corporation that was a corporation 90).

Together with the process of reforming state enterprises, the issuance of law on enterprises in 2000 has created a breakthrough step in the development of private sector economy and private enterprises. The situation of business monopoly has been reduced in many industries and fields; business environment became more competitive though much limitation still existed.

In continuance of building legal framework for finalizing the management and raising the performance effectiveness of state enterprises, in 2003, Vietnamese National Assembly issued law on state enterprises replacing the former one. The government issued Decree 153/2004/ND-CP dated 9\(^{th}\) August 2004 regarding management of state corporations and conversion of state corporations and independent state companies to the model of parent company – subsidiary companies.

In order to strengthen the role of state economy in general and state enterprises in particular, Vietnamese National Assembly and Government indented to establish giant economic groups. This intention was represented in the Resolution at 3\(^{rd}\) Central conference course Ninth: “to form some strong economic groups based on state corporations, with the participation of


\(^{3}\) Provided by Department of state-owned enterprises renovation.
economic components and with multi-industry business, including main business industry with high professionalism and controlling role in the national economy”.

In implementing this Decree, up to late of 2009, before the issuance of Decree 101/2009/N-CP on pilot implementing state economic groups which creates initial legal basis for the establishment and management of state economic groups, the Prime Minister decided to establish 8 economic groups on the basis of earlier established corporations 914.

Up to present, although private sector has developed rather rapidly and a great amount of state enterprises have been privatized; State enterprises in general, state groups and corporations in particular still play an important role in the Vietnamese economy.

In 2008, state enterprises sector with the core being groups and corporations, contributed nearly 40% GDP (?), created 39.5% industrial production value, more than 50% export quota and 28.8% total domestic income (excluded crude oil).5 Most of state groups and corporations operate in key fields of the economy, some of which operate in monopoly fields or with high monopoly level (Coal - mineral, Oil and gas, Electricity, gasoline and oil distribution...). State groups and corporations seize a very high amount of equity, up to VND458,645.8 billion; total allotted land are 3,658,118 ha; total asset are VND1,241,490.6 billion; total turnover are VND866,622.4 billion; incurred amount turning into the budget are VND229,873 billion; debt amount of corporations in credit organizations are VND713,612 billion; attracting 1,179,212 laborers6. Hence, state groups and corporations have a very important position in the economy of Vietnam. And, the management of state groups and corporations in order to improve the effectiveness of these economic units has special meanings to the general effectiveness of the development.

Although some groups have achieved specific certain results in developing production and business, increasing equity, developing technology, extending market..., in fact, the organization, management and operation of these groups still follow the model of corporations - companies, and are somehow similar to put a new shirt on an old mechanism (corporations – parent and subsidiary companies). There are many problems on the organization, management, and operation of corporations and the effectiveness of this model should be seriously examined, especially after Vinashin lost their debt payment ability, forcing the government to the restructure. The issue of managing state economic groups becomes more urgent and is a topic of current interest.

Before the issuance of Decree 101/2009/N-CP, these groups were established and operated according to decisions of the Prime Minister, and there was no any complete and systematic legal document on managing these groups. Therefore, the issue on managing groups mentioned in Decree 101/2009/N-CP will be examined below.


5, 6 Supervision report of National Assembly economic Committee. Regarding data on contribution of state enterprises used in this report, this report extracted from report No.285-BC/ BCSDCP of party civil affairs committee of the government on pilot implementation of economic groups
III. Decree 101/2009/ND/CP and its implications on managing groups

A. Advantage:

- The Decree provides quite complete legal regulations on organizing the management of State economic groups (although it is still in the period of pilot implementation)
- The Decree has separated activities for the benefit of the public from normal business activities, stipulated compensation mechanism when these groups implement activities for the benefit of the public in which enterprises incur loss.
- The Decree provides provisions limiting enterprises’ borrowing rate to not exceed 3 times of enterprises’ charter capital, which helps overcome the situation in which debt ratio of many state enterprises which are economic groups and corporations exceeds dozens times of their charter capital as happened earlier.

(These both contents are regulated in Decree 09/2009 dated 5th February 2009 on the issuance of regulation on financial management of state companies and managing state capital invested in other enterprises).

- Regulate more tightly on rights and responsibilities of Board of Management, Chairman of Board of Management, and General Director etc. in relation with business performance of group (Articles 27 and 30) and relationship among those positions (Article 29)

B. Contents needed to be examined for further completion.

1. Objectives of establishing state economic groups.

Article 1 mentioned 5 objectives:

1/ Concentrate on investing in and mobilizing resources, form big scale companies groups in key industries and fields that need to develop, and improve the competitiveness and the integration into the world economy.

2/ Play the role to guarantee great balances in the national economy; apply high technology; create motivation for the development for other industries and fields and for the whole economy.

3/ Unite in value added chain, develop other economic components.

4/ Strengthen the effectiveness of managing and supervising state assets and capital invested in enterprises of the groups.

5/ Create the foundation for further finalizing policy mechanism and law on groups.
Comments:

- Objectives not yet guarantee target orientation which is to implement industrial policy (government’s structure policy). In a transition economy where the market is very imperfect and private sector is still small, only the market will not be able to provide a solution.

- Hence, two questions are raised:

  + Which is the key field? This is an inexplicit point and different opinions may be provided.

  + Is the activity of guaranteeing big balances of the economy a public benefit one? Will groups maintain the role of guaranteeing big balances of the national economy? On which base? When the implementation of those “guaranteeing” tasks does not follow market rule, how incurred costs will be put into account and compensated?

2. About business industries.

Specify business industries of state economic groups relating to the specification of objectives of establishing groups and decided by such objectives.

Decree 109/2009/ND-CP defines pilot industries for the establishment of state economic groups:

1/ Post and telecommunications and information technology;

2/ New shipbuilding and ship repairing;

3/ Electricity production, transmission, distribution and business;

4/ Oil and gas surveying, exploration, exploitation, processing and distribution;

5/ Coal and mineral surveying, exploration, exploitation and processing;

6/ Textile;

7/ Rubber cultivation, exploitation and processing;

8/ Producing and trading fertilizer and chemical products;

9/ Investing and trading real estates;

10/ Construction industry and manufacturing mechanics;

11/ Finance, banking, insurance;

12/ Other industries as decided by the Prime Minister.
Comments:

There is no in-principle limit on business industries for groups establishment. However, the objective of groups is to implement 5 objectives of which 2 objectives (1 and 2) relate to business industries in order to implement structure policy (developing fields that the Government considers the key one in the national economy, and overcoming market’s failures (objective 2)

In comparison to objectives, there is an emerging issue:

Concentrate on investing and mobilizing resources to form groups of big scale companies in key fields and industries that are needed to be develop and to apply high technology…. the establishment of groups in the fields of construction, textile, rubber cultivation and exploitation and processing, real estates investment is not really necessary, especially the establishment of groups being in pilot period. There are many private enterprises who are doing business quite effectively in the above mentioned business industries. Basically they have managed to create competitive market. These industries are also not industries with key role.

3. Organization structure of the groups; management and administration in these groups

1/ Organization model of economic groups according to Decree 109/CP is a multi-level pyramid one (see diagram 1) including:

- Parent company (level 1 enterprise) with 100% capital owned by the government or having governed shares.

- Corporations and subsidiary companies of level 1 enterprises (level 2 enterprises) controlled by level 1 enterprises. Level 1 enterprises are parent company of corporations. Such companies seize 100% of capital or having governed shares)

- Subsidiary companies of level 2 enterprises...

- Associated enterprises

Parent company, corporations, subsidiary companies, associated enterprises are enterprises having legal status, registering for business and operation in accordance to the law on enterprises.

2/ Management and administration in groups. There are 3 main methods:

- Manage and administrate through parent company;

- Manage and administrate through forms of investment and association;

- Manage and administrate through agreement and cooperation in using joint services within groups; exercising regulations, standards, general norms within groups that are not against the law; using each other’s products and services based on market rule.
Besides, there are other methods as regulated by the law and appropriate with regulations of member enterprises.

A question is that: Groups established according to decisions of the Prime Minister, have legal status but no legal entity, and no Board of Management. Is it right when we have been calling Chairman of Board of management of Vinatex, Chairman of Board of management of EVN, Chairman of Board of management of Vinashin for a long time? Can the groups go bankruptcy completely? From legal perspective, who will be the one that implements the function of managing and administrating the groups under the forms of investing, associating, managing, and administrating via agreement and cooperation in using services within the group? If the person who administrates these activities among member companies is parent company, then the model of economic groups does not differ from the model of corporations with parent company and subsidiary companies.

It can be said that due to establishment history and control of capital source, the management and administration within groups are mainly through parent company. This method has an advantage of creating tightly associations among member enterprises. If being implemented properly, it will be able to concentrate resources to exercise structure policy and develop technology within groups. However, this method can be easily controlled by benefits of parent company, which affects member companies and the objective of group establishment.

4. Groups management.

State economic groups are, in nature, owned by the whole population. The government is the representative to implement such ownership of the whole population. However, the Government itself cannot directly implement the right of ownership and therefore, the Government assigns a Board of management to represent its ownership. Members of Board of management are appointed by the Prime Minister. In fact, members of Board of management include the ones who are currently working in Ministries with state management function (The policy- planning bodies), largely from Ministry of Finance and Ministries managing economic-technical industries that were formally bodies managing enterprises with inherently upper-lower level relationship with enterprises. The remaining members are those working in the groups with tight connection to the benefit of the group. There are some issues arising here:

- Relationship between the owner and ownership representatives.
- Composition of Board of management, ownership representatives and its possible implications
- Board of management and Board of Control.
- Board of management and General Director.

Those issues will be examined one by one below.

1/ Relationship between the owner and ownership representatives.

Relationship between the owner and ownership representatives is represented in Article 21 (Board of Management), Article 22 (Responsibilities and rights of Board of Management), Article 38 (Rights and responsibilities of the owner), Article 39 (Owner and ownership
Comment: There is no regulation reflecting collective supervision of state owner to ownership representatives. In nature, capital and assets of state enterprises is under the ownership of the whole population; the State (Government, Ministries) is the representative of the whole population ownership. There is no supervision mechanism available and it is difficult to have such mechanism for the whole population to supervise during the operation process of groups. People can only supervise operation performance if this performance is publicly reported under a strict regulation (at present, such regulation is not available). Hence, the supervision of the Government- the one representing the whole population ownership- to the organization functioning as authorized representatives of that ownership is very important. This can only be implemented through collective evaluation of the Prime Minister and Ministries that are assigned the function of exercising rights of the ownership in state economic groups. Whereas, the Board of management – the representatives of state ownership – only makes period reports or reports as required by the Prime Minister but how these reports are handled and assessed is not clear. This is not to mention a high possibility that no one reads these reports. The lack of a supervision mechanism has not and continues to not strengthen responsibilities of Board of management – the representatives of state ownership in economic groups. Therefore, the implementation of representing the whole population ownership of the Government is still bureaucratic.

2/ Composition of Board of management.

The composition of Board of management is mostly officers who manage enterprises. Their benefits are very tightly connected to enterprises’ benefits which normally are short-term ones governing their decisions, affecting objectives of implementation of structure policy as well as strengthening factors that create long-term competitiveness and in many cases conflict with benefits of the owner. In Board of management in big and important groups (Coal - mineral, oil and gas groups) there are a small number of members from ministries and industries. The participation of these members also leads to two corollaries (1) Conflict between benefits of the owner and of enterprises themselves (2) Provide preferential treatment to enterprises, distorting management policies.

3/ Board of management and Board of Control.

Besides being a member (member of board of management) appointed by the Prime Minister (such person has already worked in enterprises, and has benefits tightly connecting to the enterprises), the Board of Control is elected by board of management to serve for the operation of board of management. Therefore, it depends much on viewpoints used, wills and responsibilities of Board of management, and of course, it also contains all limitations of board of management. In many cases, Board of Control does not do its function well. Vinashin is an example. The relationship between Board of Control and the mechanism of organizing the implementation of internal audit is also a problem. Internal audit aiming at evaluating business performance and financial status of enterprises is enterprises’ internal document that is the basis for providing solutions for self-correction. Meanwhile, results of the controlling are an also
basis for board of management to report to the owner (the State). These activities have the same contents but differ in their level of dissemination and they are implemented under the same entity’s administration, which is also an issue needed to be considered.

4/ Board of management and general director.

The relationship between board of management and general director has not been clearly defined and depends much on specific individuals. (This relationship is somehow similar to that between standing committee and people’s committee in localities that we are under the process of studies for further improvement). In many cases, board of management participates quite deeply in administration activities, restricting initiatives of general director. (Comment from economic groups supervision delegation). This is one of the causes of disunity in some state economic groups. Especially, the responsibility boundary of Board of management and General Director to the enterprises’ operation performance is a big issue. Board of management makes collective decisions with collective responsibilities, while general director is taking the top position in an administration system with very clear individual responsibilities.

5. Regulations on investment within State economic groups.

Decree 101-ND/CP prohibits controlled enterprises to make investment in controlling enterprises in the same group (Article 16), but allows member enterprises to diagonally invest in each other. Because of their functions, scope for doing business of members in groups is different; some enterprises have more important role than others in the implementation of group’s objectives. The investment of enterprises into each other leads to a possibility that enterprises may focus on immediate benefits and ignore the long-term development strategy of the group. The issue would be more serious if economic groups (parent company and subsidiary companies) invest in enterprises outside the group, including investment in much risky services business (financial services, real estates) according to Decree 09/2009/ND-CP, even though the investment level is limited but it is still very wide. This Decree is also stipulates that Board of management (ownership representatives) decides to invest in other enterprises that are not decided by state owner. These persons – as analyzed above – attach very tightly to enterprises’ benefits, and are often governed by enterprises’ benefits with less care about investing in improving long-term competitiveness. (See diagram 1)

6. Regulations on business industries besides the core ones.

Decree 101/2009/ND-CP still allows state groups and corporations to do business in industries beside their core ones of enterprises. This may distract resources in the implementation of objectives as set out in establishing groups. Data shown in Table 1 do not reflect the evidence that the expansion of business industries to other fields helps groups maximize their profits. That is because the expansion to other fields is not an inherent strength of the groups, especially in financial services, real estates with high risks. The lack of information and management experience in the context of rapid changing market will easily lead to bad results. The excuse is often provided by groups to justify their investment in business industries that do not relate to their establishment objectives is to maximize profits - “to take short-term profits for serving long-term objectives” which is rejected by the reality of doing business. From 2006 to 2008, investment of groups into high-risk fields tended to be on the rise while profit percentage per
invested capital unit was more and more decreasing and lower than rate of return from doing their core business industries\(^7\). (see table 1)

Allowing groups to invest in banks may let groups abuse capital ownership position to finance less effective projects of the groups, which go against with the standards on credit.

\textit{Diagram 1: Pyramid- organization diagram and regulation on the investment of State economic groups and members}

\begin{itemize}
\item Investment of parent company and subsidiary companies (100% capital or having governing shares)
\item Investment among member companies into each other (not being regulated and being decided by parent company's Board of Management)
\item Investment to outside of the industry (not exceeding 30% of company that is invested; not exceeding 20% in case of financial services)
\item Investment in associated companies (contributing share capital with status of a shareholder)
\end{itemize}

\(^7\) Report on supervising economic groups and corporations of National Assembly Economic Committee
Table 1: Capital invested in financial services and real estates of special groups and corporations

<table>
<thead>
<tr>
<th>No.</th>
<th>FIELD OF INVESTMENT</th>
<th>2006 INVESTED CAPITAL</th>
<th>PROFIT/INVESTED CAPITAL</th>
<th>2007 INVESTED CAPITAL</th>
<th>PROFIT/INVESTED CAPITAL</th>
<th>2008 INVESTED CAPITAL</th>
<th>PROFIT/INVESTED CAPITAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Credit</td>
<td>3,409,083</td>
<td>5.75</td>
<td>7,880,262</td>
<td>11.23</td>
<td>10,524,365</td>
<td>3.61</td>
</tr>
<tr>
<td>2</td>
<td>Insurance</td>
<td>589,747</td>
<td>10.26</td>
<td>2,350,866</td>
<td>2.56</td>
<td>2,674,860</td>
<td>4.59</td>
</tr>
<tr>
<td>3</td>
<td>Securities</td>
<td>818,700</td>
<td>8.21</td>
<td>1,900,757</td>
<td>12.64</td>
<td>2,039,823</td>
<td>5.05</td>
</tr>
<tr>
<td>4</td>
<td>Investment fund</td>
<td>449,848</td>
<td>4.51</td>
<td>1,373,339</td>
<td>2.78</td>
<td>1,762,238</td>
<td>0.34</td>
</tr>
</tbody>
</table>

The above analysis has shown that the management organization, regulations on investing, doing business and administrating economic groups, as well as on responsibilities of board of management and general director should be comprehensively examined for further improvement to increase the effectiveness, competitiveness and serving industrial policy of the Government.

It should be emphasized that there is no theoretical evidence affirming the state enterprises are ineffective, though in fact, there are a number of enterprises with very low effectiveness besides several effective ones. The problem lies in the enterprise administration and mechanism for that administration.

IV. Suggestion for improving state economic groups in Vietnam

1. From lessons of groups in Japan, Korea and China

Some characteristics in the organization and operation of economic groups (Keiretsu of Japan, Cheabols of Korea and corporations of China) may have certain influences to the organization and management of state economic groups in Vietnam. But the biggest difference is in the ownership regime; almost all Keiretsus of Japan and Cheabols of Korea evolved from family companies.

Although being big and strong groups, because of the existence of mechanism on investing into each other and multi-industries operation based on Banks, in the period of 90s of the last century, Japanese economy depressed, many large banks were strongly affected by bad debts coming from Keiretsus that forced banks to either merge or go bankruptcy. This weakened the association in Keiretsus. Many managers and business circle think that Keiretsu is not an effective business model. From that assessment, although almost all Keiretsus still exists, they do not concentrate or closely associate like before 90s.

Meanwhile, in Korea, despite of great contributions to the development of Korean industries thanks to government’s preferential treatments with tight binding (for example, after a specific
period of time, Cheabols that received preferential treatment must be able to export their products), the East Asian crisis in 1977-1979 had serious effect to the Korean economy, with one of the reasons originating from the operation of groups (Cheabol). Those groups were considered to be organizations covering too many industries with weak organization, ineffective management and no global competitiveness. The half of 30 biggest Cheabols of Korea went bankruptcy or had to restructure. Deawoo, the 4th biggest Cheabol of Korea failed completely and other Cheabols had to exert their great effort to comprehensively restructure. Korean government also promulgated strict regulations to manage the Cheabols’ operation, specifically:

- Make the management transparent by announcing financial reports and information of doing business and administration of Cheabol.
- Do not allow parent company to guarantee debts for subsidiary companies within the group.
- Set up and control financial targets aiming at guaranteeing financial safety, including the regulation on the debt ratio to not exceed 2 times of equity.
- Concentrate on core industries to improve global competitiveness.
- Regulate on individual responsibilities for Cheabol leaders in managing and administrating the groups. Provided increased rights for minority shareholders.
- Limit tortuous investment among Cheabol members and forbid some transactions among members.
- Prohibit Cheabols to own non-banking financial companies...8

Some Korean scholars indicated that the collapse of Cheabols and new regulations on activities of Cheabols increased national competitiveness of Korea. For China, although there are specific results in the process of establishing and operating corporations, this model is still not clear and needs time for improving and demonstrating its greater advantages.

2. Suggestions for improving the management of economic groups in Vietnam.

With the rapid development of technology and science, and in the context of globalization and economic integration, enterprises including state enterprises operate in below conditions:

- The continuous development of technology and innovation; and products’ life cycle is shortened;
- Protection barrier is minimized (even being rejected). *Competition is at global level* and is very sharp;
- There exist activities of multi-national companies and the formation of production network and global value chain.
- Enterprises can only compete when they have greater productivity based on applying advanced science and technology, using high-quality human resources in a reasonable production organization with modern management skills.
- For our country, the private sector is newly formed, aggregate potential is still small, hence, state enterprises, especially groups and corporations play a very important role in the implementation of these requirements. Being a late implementer of industrialization course, state economic corporations must play “main attack” role, and must be a tool for

8 See explanation in footnote 1
the government to carry out industrial policy, specifically structure policy. Korea and China used economic groups to implement their industrial policy. In order to increase the operation effectiveness of state enterprises and to implement industrial policy, state economic groups should be improved towards the following suggestions:

Redefine the objectives of establishing groups as well as regulations on the investment:

For state economic groups, business operation should aim at two objectives:

(1) Implementing structure policy; accordingly groups make investment in key fields of the national economy (fields that are long-term development trend of the global economy), and in industries that can have strong spill-over to other economic industries.

(2) Maximum profits.

Those two objectives are related to each other but not always at the same pace. During the implementation of the first objective, the one of maximizing profits may not be immediately achieved (because investment has to be made in research and development, innovating technology, improving the quality of human resources, organizing the market, building brand name etc. to create long-term competitive advantage...). On the contrary, if profit maximization is too much focused, short-term benefits will be pursued and paid much attention, which can affect the first objective.

Since Vietnam is fostering economic structure shifting to basically become an industrial country towards modernization in the next 10 years, state economic groups need to concentrate on the first objective. Accordingly,

- The maximization of profit can be assigned to State Capital management and business Corporations for the implementation.
- In industries and fields where private sector has strongly developed, basically, the competitive market has already been formed, the privatization should be carried out, and therefore, the state does not need to have governing shares. Transferring capital should be made from these enterprises to invest in those that implement structure policy.
- According to many researchers, multi-level pyramid organization model in agriculture is not effective (profits gained by rubber corporations in recent years are mainly due to the difference in land rent originating from increased price of rubber). In agriculture field, establishment of industrial-agricultural complex should be made with vertical association from production – processing – distribution within one value chain.

Accordingly, it is necessary to:

- Closely regulate investment among groups’ members. Stipulate different rates of diagonal investment in member companies that have different positions in implementing structure policy. When needed, parent company can move a part of capital from subsidiary companies for implementing the task of innovating technology and developing main products.
- Restrict investment to outside of groups, reduce the allowed ratio of investment to outside. The investment to outside is only allowed if it achieves the increase in domestic
content rate, added value of products, and exporting ratio. Do not invest in financial services and real estates.

Place state economic groups in the international competitive environment; closely control natural monopoly. Resources invested by the state in groups must associate with achieved results under defined criteria to implement structure policy and improve global competitiveness through a defined roadmap; closely supervise the use of resources in implementing this roadmap over time.

Make public and transparent the operation performance of groups thanks to regulations on compulsory audit and report this result to National Assembly. This is a mechanism for National Assembly – the representative of people – to supervise activities of groups and to increase ownership responsibilities of Government bodies.

Strengthen groups’ management mechanism and organization

- In order to overcome the situation in which members of board of management are also the ones participating in policy planning, which leading to above mentioned corollaries, we should form an agency that implements state ownership in economic groups. (May take into account of General Department of state enterprises management). This agency assigns persons to participate in board of management of economic groups. This agency can also assign persons to participate in board of management of SCIC.
- Increase the number of independent members in the elements of Board of management (for groups and corporations aiming at profit maximization, these independent members are to protect interests of minority shareholders.).
- Set up mechanism for collective evaluation by the Prime Minister, Ministries and agencies on the operation of Board of management and economic groups.
- Strengthen the role of Board of Control within groups. Board of Control is established by the owner and makes reports to the owner. Meanwhile it also sends the results of controlling to Board of management without the approval of board of management. With this structure, Board of management organizes the implementation of internal audit.
- Redefine debt ratio on equity. Only accept groups that have coefficient of debt on equity over a regulated limit when they invest in innovating technology to assure the competitiveness.
- Build up a system of criteria for evaluating the effectiveness for each economic group based on their long-term objectives to serve the Government’s structure policy and improve the groups’ global competitiveness. Make more specific identification of responsibilities of Board of management and General Director, etc. related to the implementation of these long-term objectives.