



DEVELOPMENT OF ENTERPRISES AND THE NEED FOR FURTHER REFORMS
OF THE BUSINESS SECTOR IN VIETNAM

10

Highlights

Le Duy Binh - Truong Duc Trong
Economica Vietnam

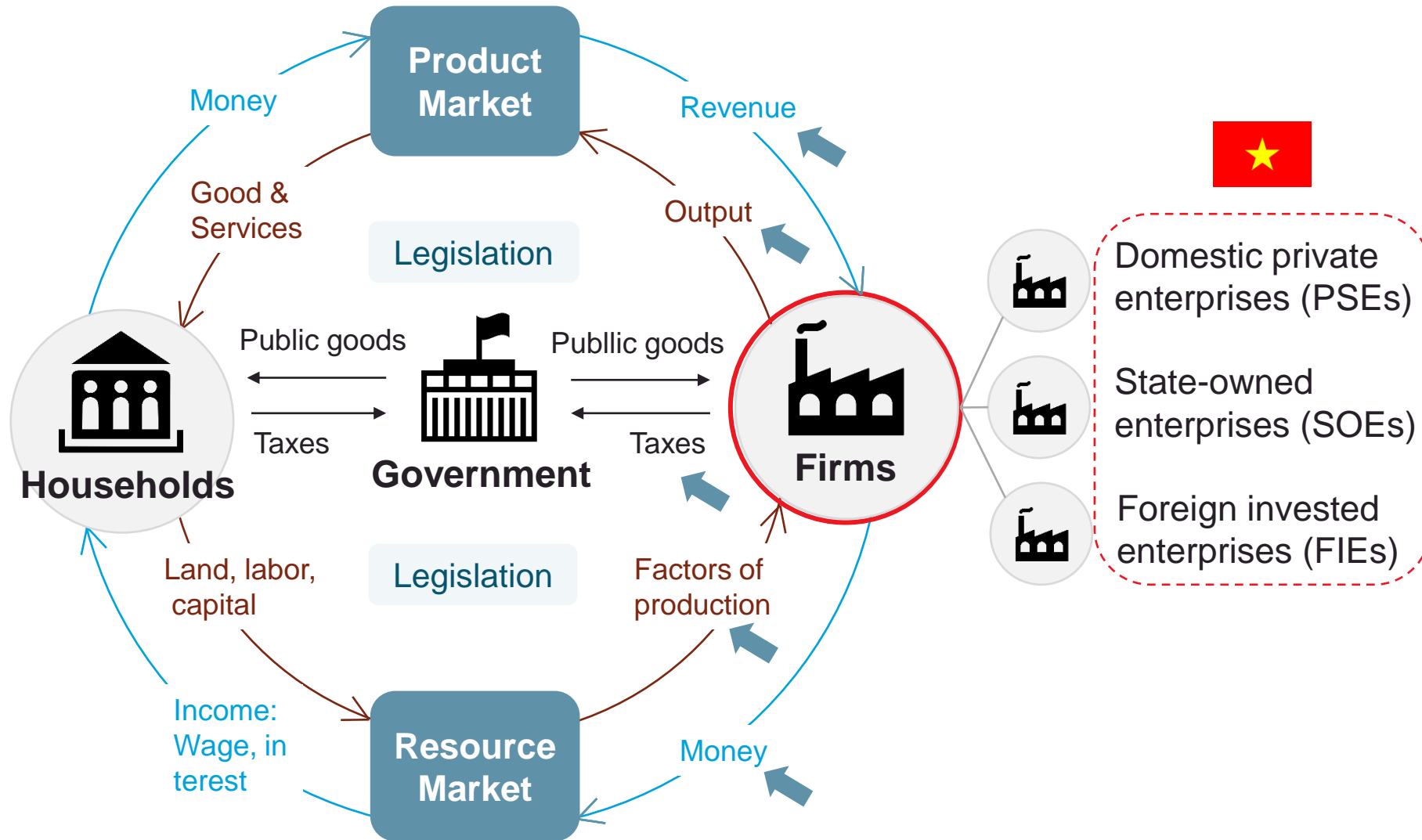


Vientianne, 19 November 2015

VIETNAM



Enterprises – a key player in an economy



To **compare** the three pillars of the enterprise sector in Vietnam:

- growth
- economic efficiency
- contribution to the economy.
- opportunities and challenges.



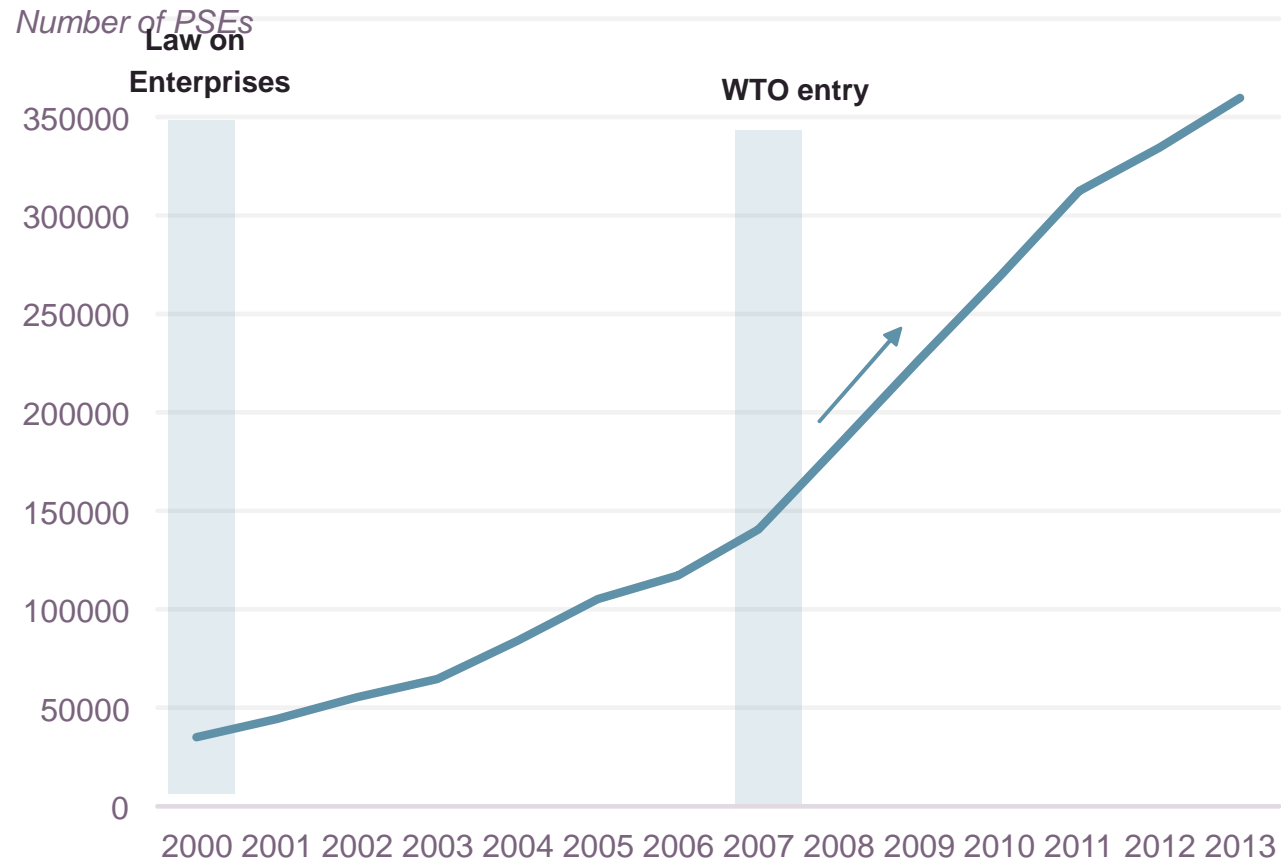


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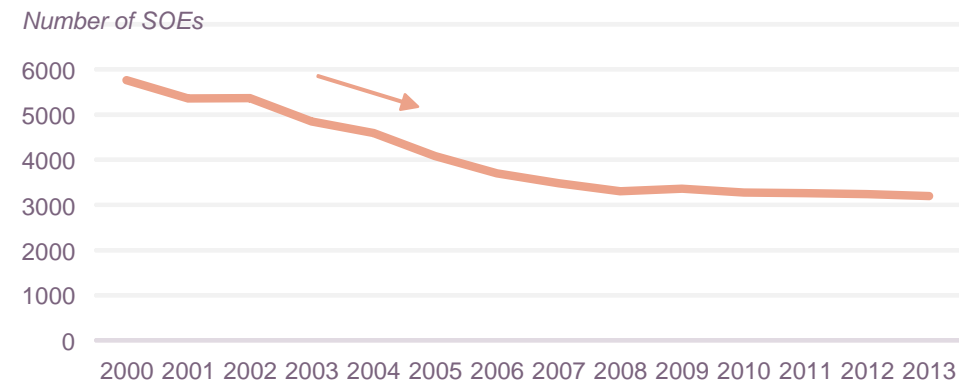
Highlights of the enterprise
sector and business
environment in Vietnam

#1. The number of PSEs is increasing dramatically

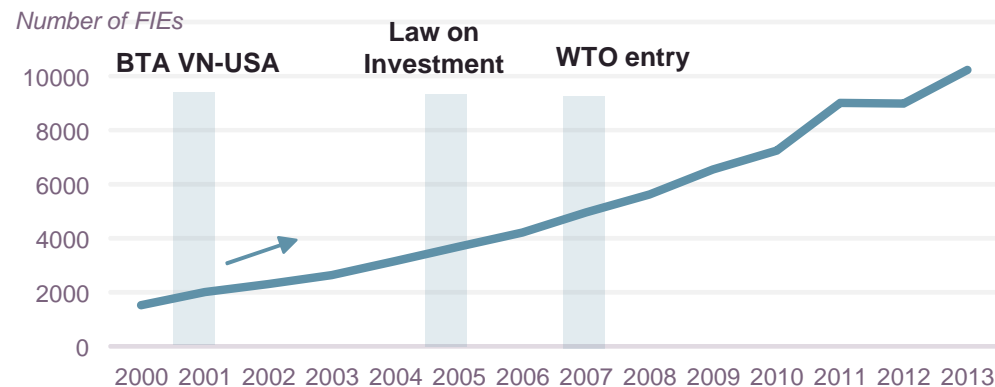
The number of PSEs has soared over the last 15-year period



Privatization made the quantity of SOEs decrease

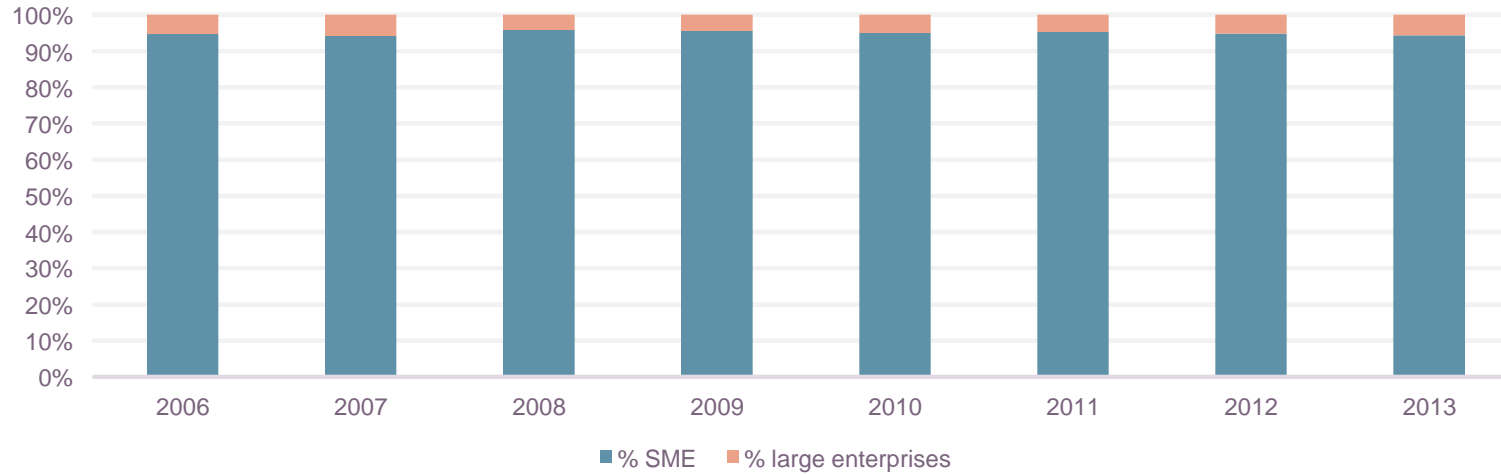


FDI promotion policies have positive impact



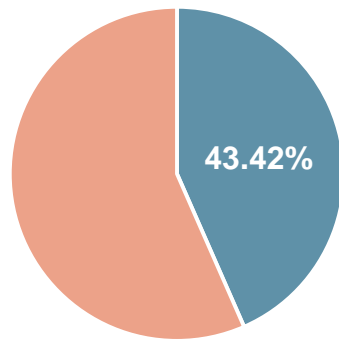
#2. Small and medium enterprises are in majority

Approximately 95% the total number of enterprises are SMEs



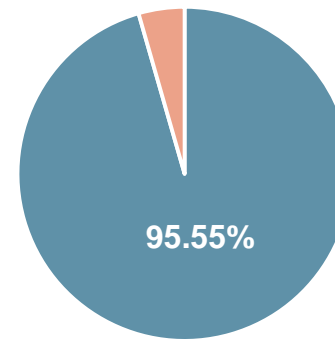
Small-scale and scattered business?

SMEs constituted nearly a half of total SOEs in 2013



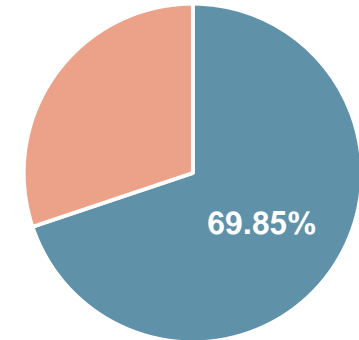
■ SME ■ large enterprises

SMEs dominated the proportion of total number of PSEs in 2013



■ SME ■ large enterprises

two thirds the total number of FIEs in 2013 are SMEs

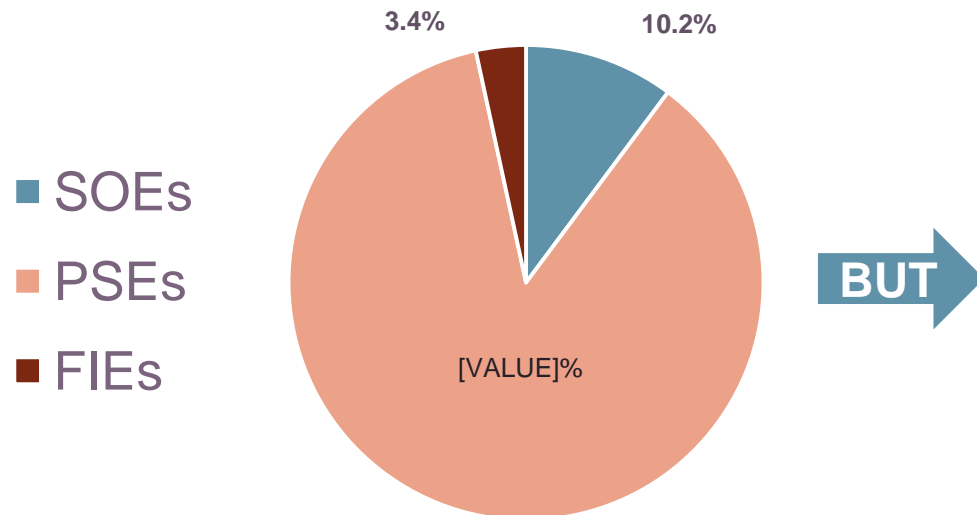


■ SME ■ large enterprises

#2. PSEs – numerous workers but low productivity

PSEs are driving force for employment generation

Proportion of labor working in each type of enterprise (%)



A fall in labour productivity in the SME sector

	Labour Productivity 1			Labour Productivity 2		
	2011	2013	Growth	2011	2013	Growth
All	77.3	61.5	0.95 [0.87]	20.7	16.5	0.96 [0.89]
Micro	65.8	54.3	0.96	18.0	14.1	0.96
Small	92.2	75.8	0.95	25.4	21.7	0.94
Medium	151.3	99.6	0.96	33.4	27.0	0.98
Urban	93.4	70.4	0.92	26.2	20.1	0.93
Rural	66.2	55.4	0.98	16.9	14.0	0.97
South	82.9	65.5	0.96	23.1	18.6	0.97
North	73.2	58.6	0.95	19.0	15.0	0.95

Note: Million real VND. Mean labour productivity (LP) growth is defined as LP_{2013}/LP_{2011} . Median LP growth in brackets.

- LP1 = Real income per worker
- LP2 = Real value-added per worker

Source: John Rand and Finn Tarp. 2013. Characteristics of the Vietnamese Business Environment: Evidence from a SME Survey in 2013

#3. PSEs tend to have low and informal innovation

Low level of technology acquisition

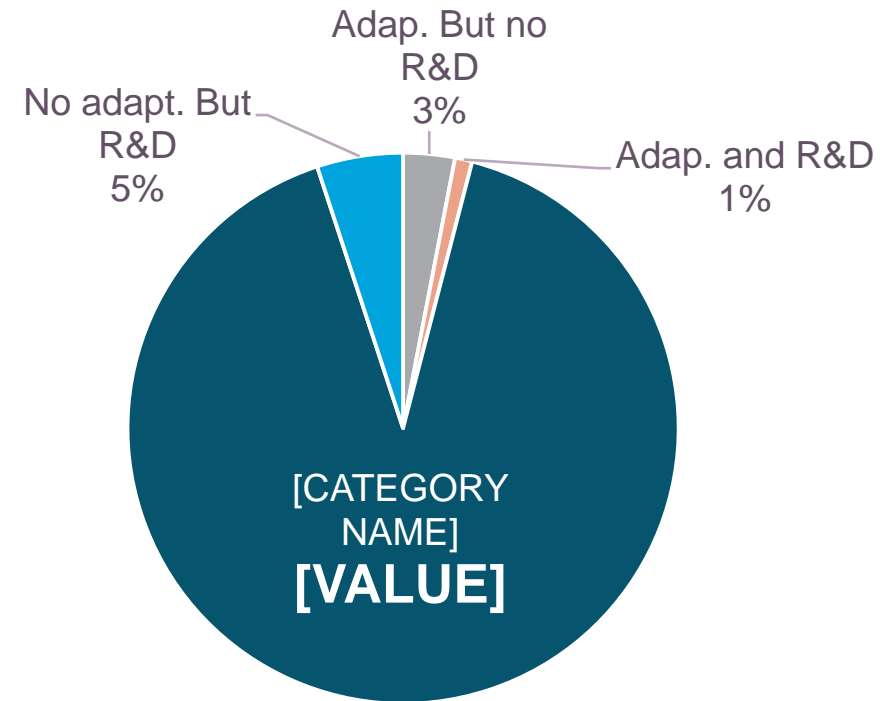
Innovation in Vietnamese firms is generally low and tends to be informal.

a report by CIEM, DoE and GSO (2014) on firm-level competitiveness and technology in Vietnam has shown that in 2011, only 800 out of nearly 8000 surveyed enterprises (**10%**) were conducting original **R&D**.



hinder PSEs to become **active players** in the **value chain** of many FIEs.

PSEs tend to adopt or adapt existing innovations rather than develop new ones



#4. SOEs remain an important player in the economy

SOEs have advantages in accessing production inputs



Own about 70% of total producing land

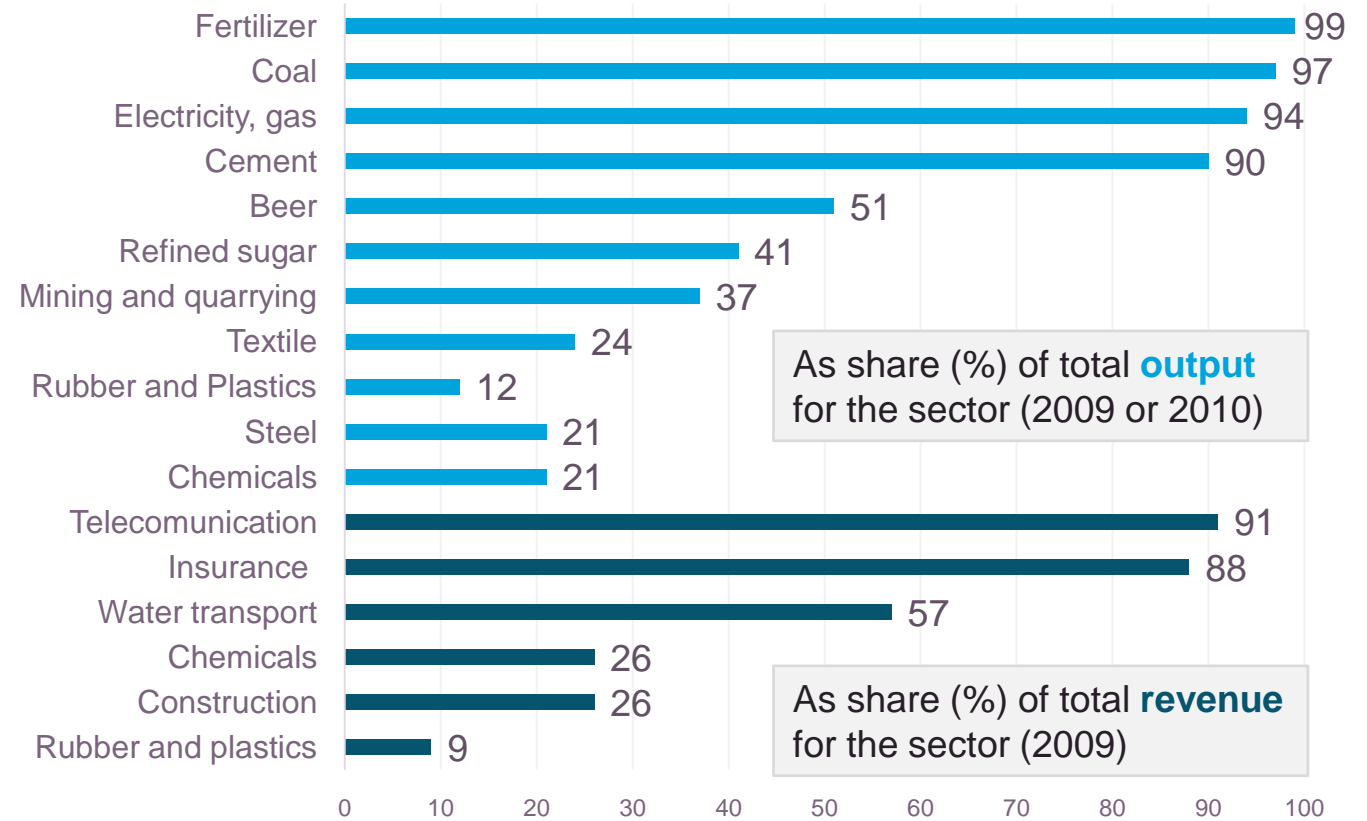


Be granted loans without collateral & often guaranteed by the Government

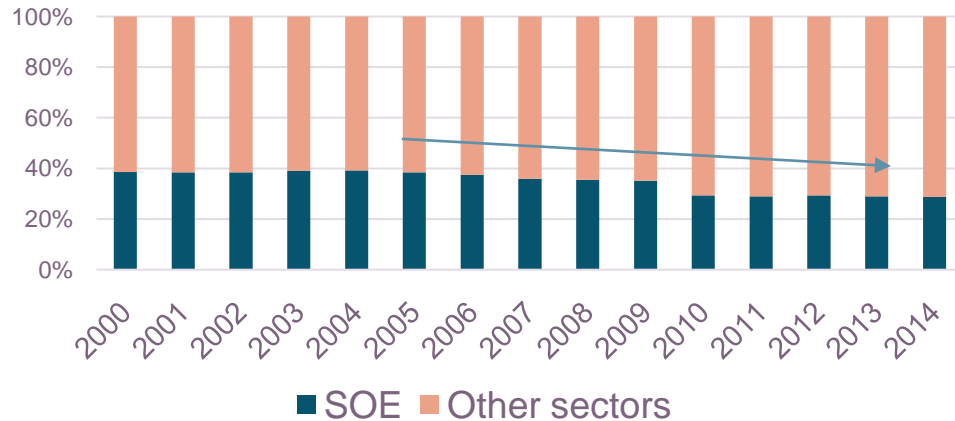


Benefit from price subsidies and special privileges

SOEs control a large share of the output and revenue in many sectors



A gradual decline in GDP contribution



#4. ...thanks to special treatments from the government

A few SOEs have the monopoly power in essential industries of the country.



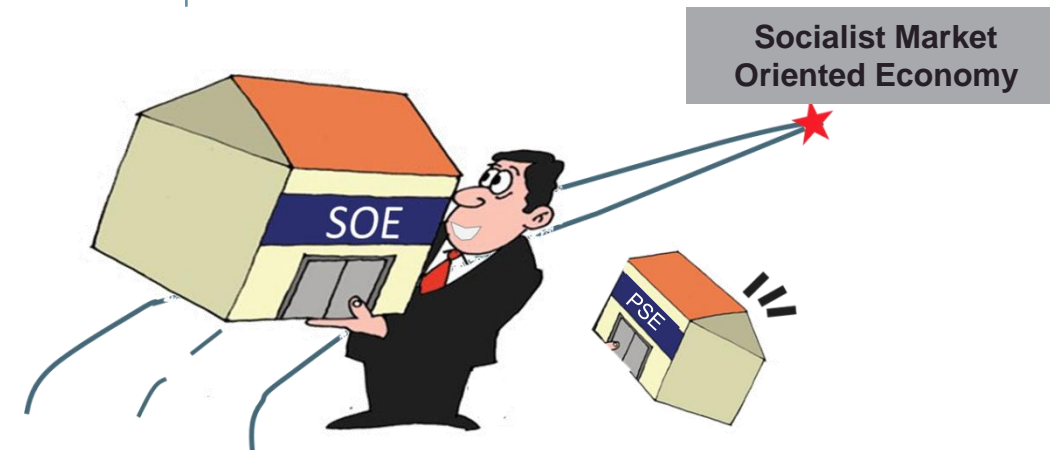
The Government assigned SOEs some functions or missions



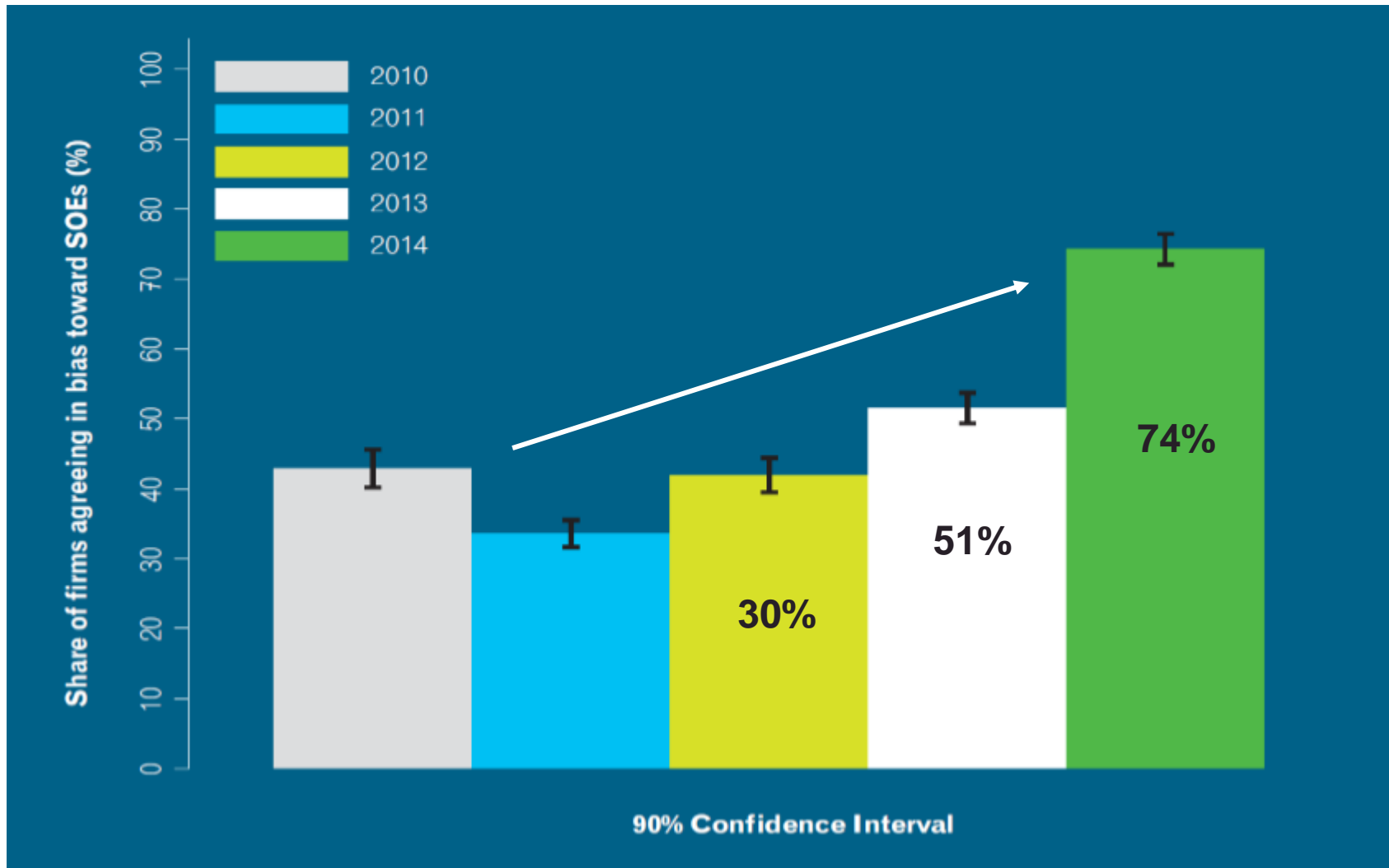
SOEs are often rescued by the State Budget when they are in troubles.



The Constitution 2013: State-Owned enterprises assumes the **leading role** in the sector socialist - oriented market economy.



#4. The perception of SOE bias is growing

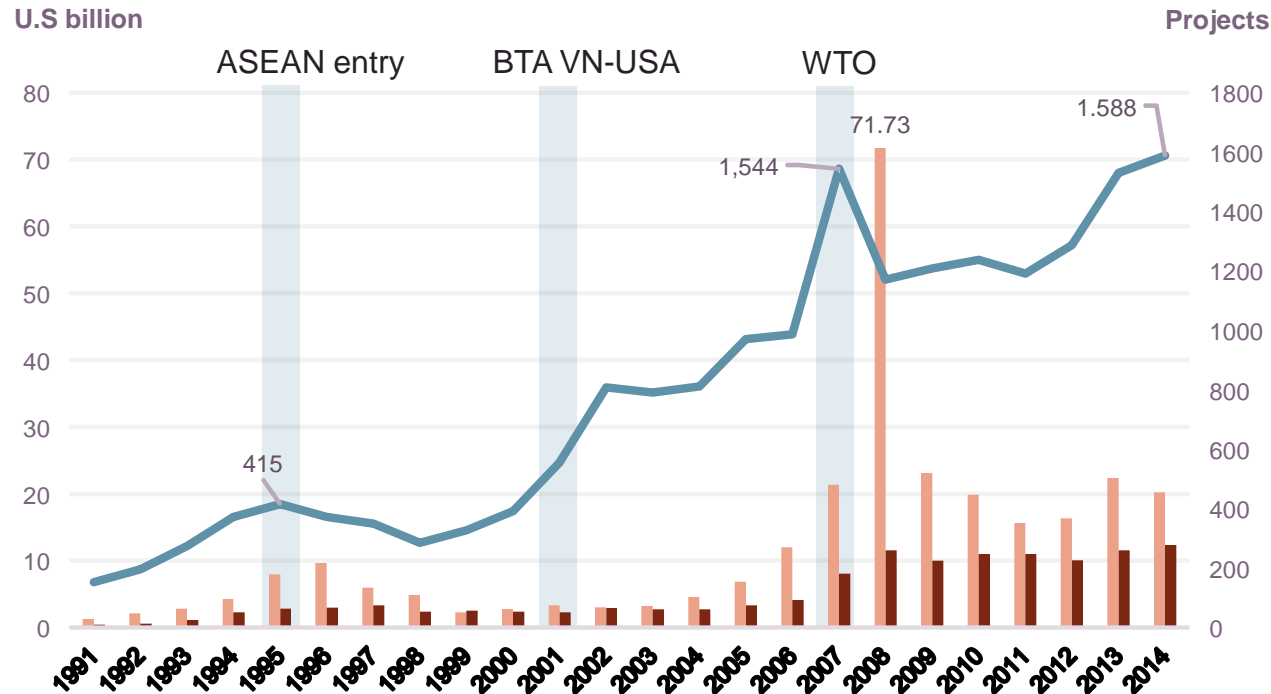


Firms assessment of bias towards the SOEs

Source: PCI-FDI Survey 2014, the figure reports the share of firms **agreeing** that there is bias towards SOEs

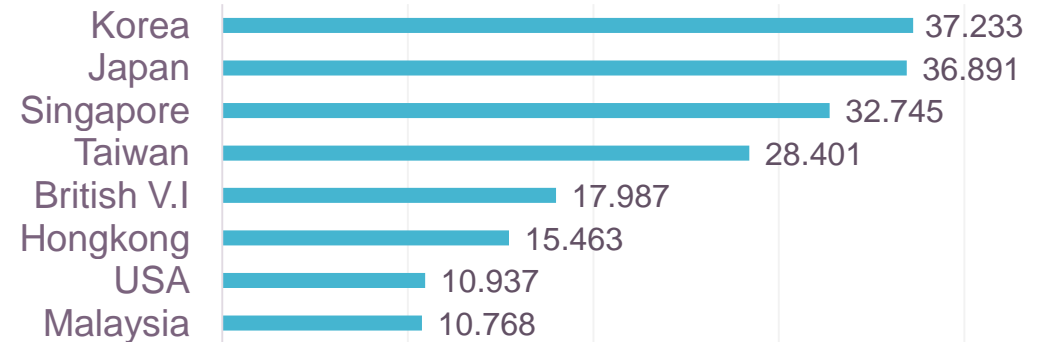
#5. FDI inflows have increased over 25-year period...

The number of new FDI projects reached record in 2014

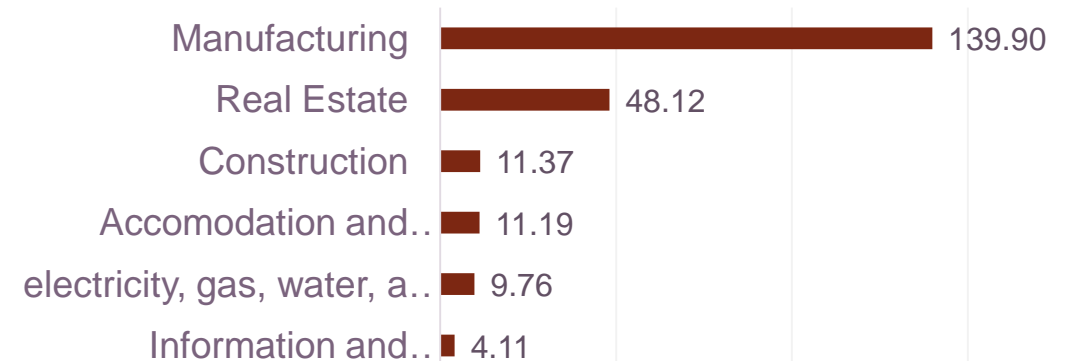


FDI flows to Vietnam are active over 2000-2013. FDI flows will certainly **benefit from actual trade agreements** and some ongoing negotiations. Most of FDI inflows to Vietnam target cheap labor and natural resources.

Top countries with largest investment capital (USD mil.)



Top industries with largest investment capital (USD bil.)



#5. FIEs are offered many preferential treatments ...

Types of preferential treatments towards FIEs

Location



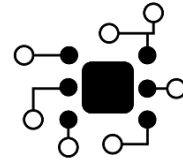
Industrial Park (IP), Export Processing Zone (EPZ), Economic Zone (EZ), Hi-tech Park.

Taxes



high incentives of taxes: corporate income tax, value added tax, import-export tax.

Other incentives



Projects *hi-tech* development will enjoy additional incentives by Prime Minister's regulation.



Strategy to attract **large multinational corporations** in technology

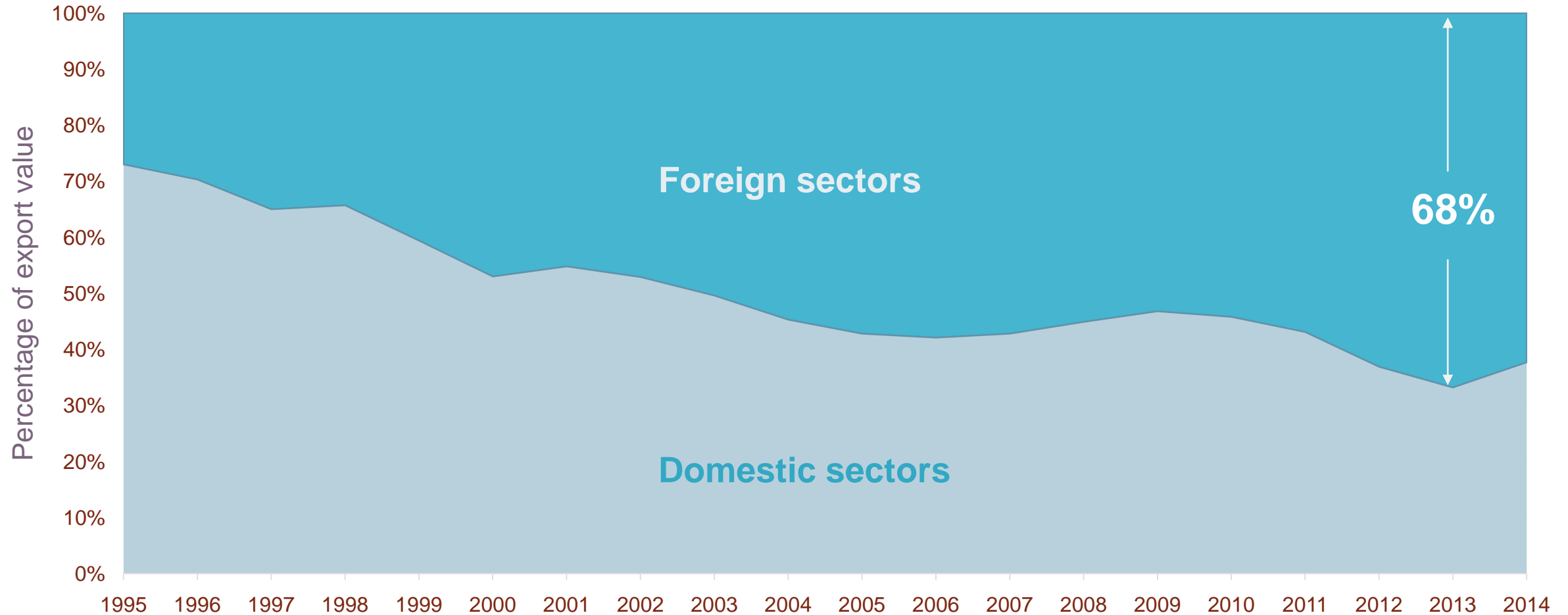


Incentives of Corporate Income Tax (CIT): 10% exemption for 15 years for hi-tech and IT investment in which: free in the first 4 years, 50% in the next 9 years.

Incentives of import tax: Free import tax for fixed asset; free import tax in 5 years from production date for materials, components (cannot produce in local market) used for investment projects; free import tax for materials (cannot produce at local) for software manufacturing.

#5. ...and they now become the driving force for exports

FIEs' export value now account for two thirds of Vietnam's total export value



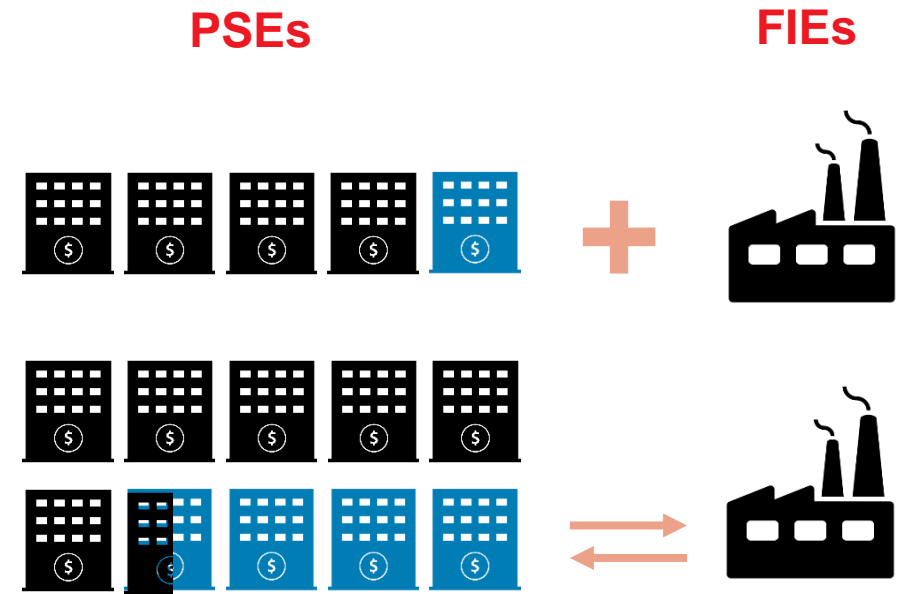
#5. but other contributions may be not commensurate

Vietnamese appears to fail to link up with FIEs

Only **one fifth** of Vietnamese businesses can “work” with FDI businesses.

There is limited technology transfer between FIEs and domestic enterprises. The majority of **domestic enterprises** are **transferring technology with each other** (accounting for **66%**).

Source: CIEM, DOE, GSO. 2014. Firm-level competitiveness and technology in Vietnam – Evidence from a survey in 2013; <http://bit.ly/1S84JZN>



Transfer pricing (TP): the other side of the medal

tax arrears:
US\$23.8 million

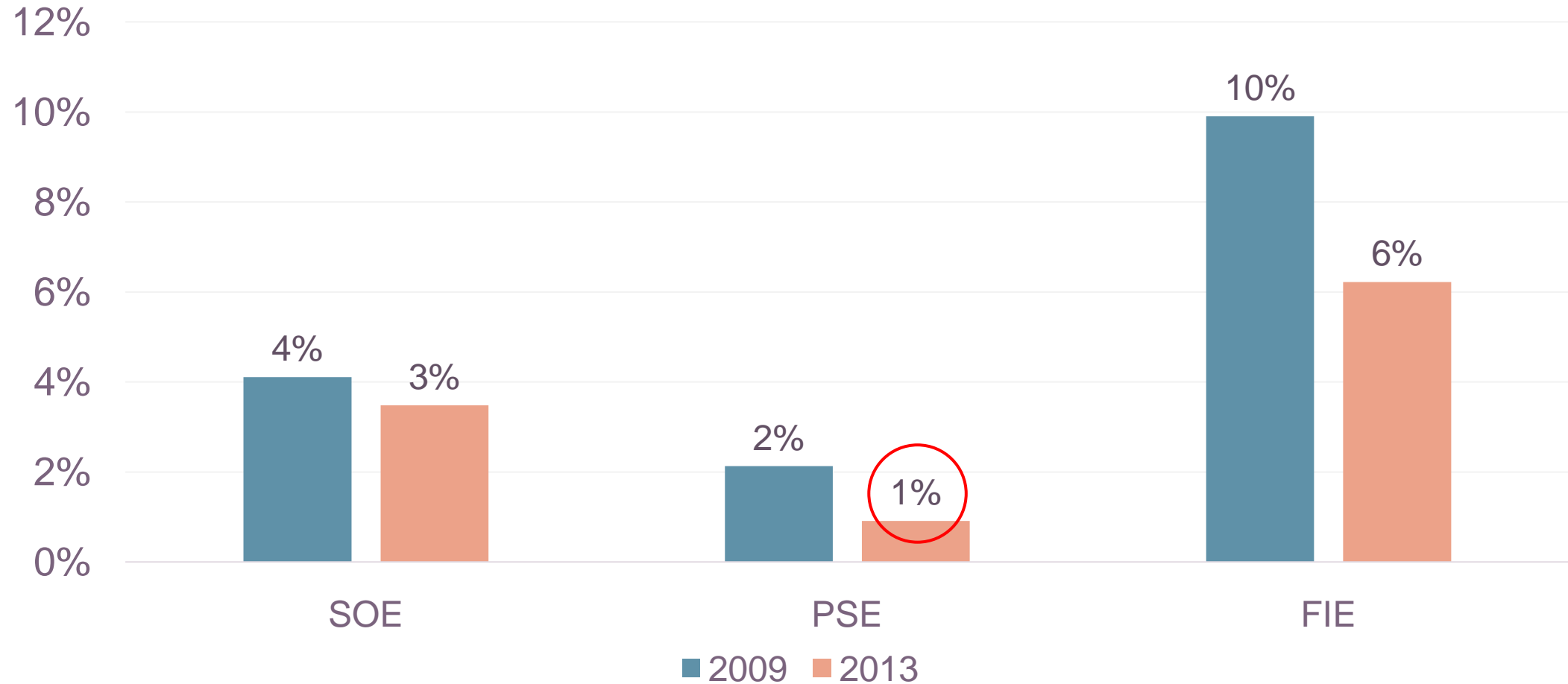
tax arrears:
US\$4.2 million

“Black-list” – suspected TP

The 'Black-list' section contains logos for four companies suspected of transfer pricing: Coca-Cola, Pepsi, Adidas, and Big C Supercenter.

#6. Widening performance gap between three sectors

Return on Capital of Enterprises in VN



#6. Widening performance gap between three sectors

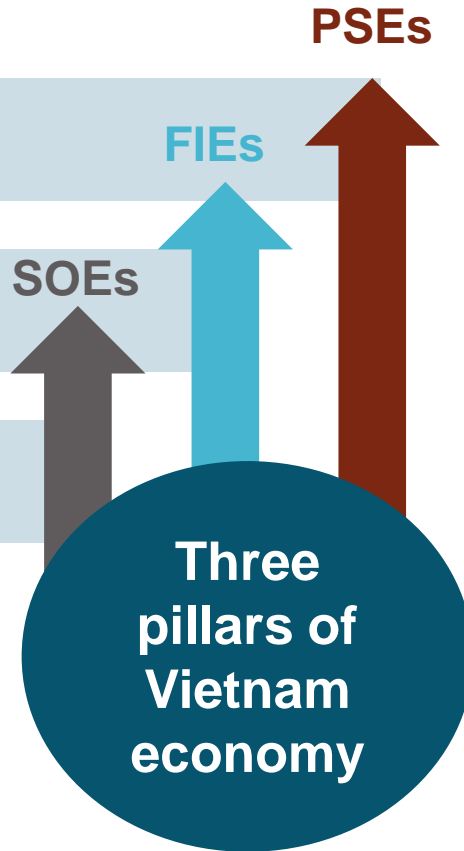
HOW TO?

- Increase labour productivity
- Capital accumulation & linkage

- Develop supporting industries
- Promote technology transfer

- Equitisation & Divestment
- Accountability enhancement

Reallocate the resources in the economy to more efficient sectors



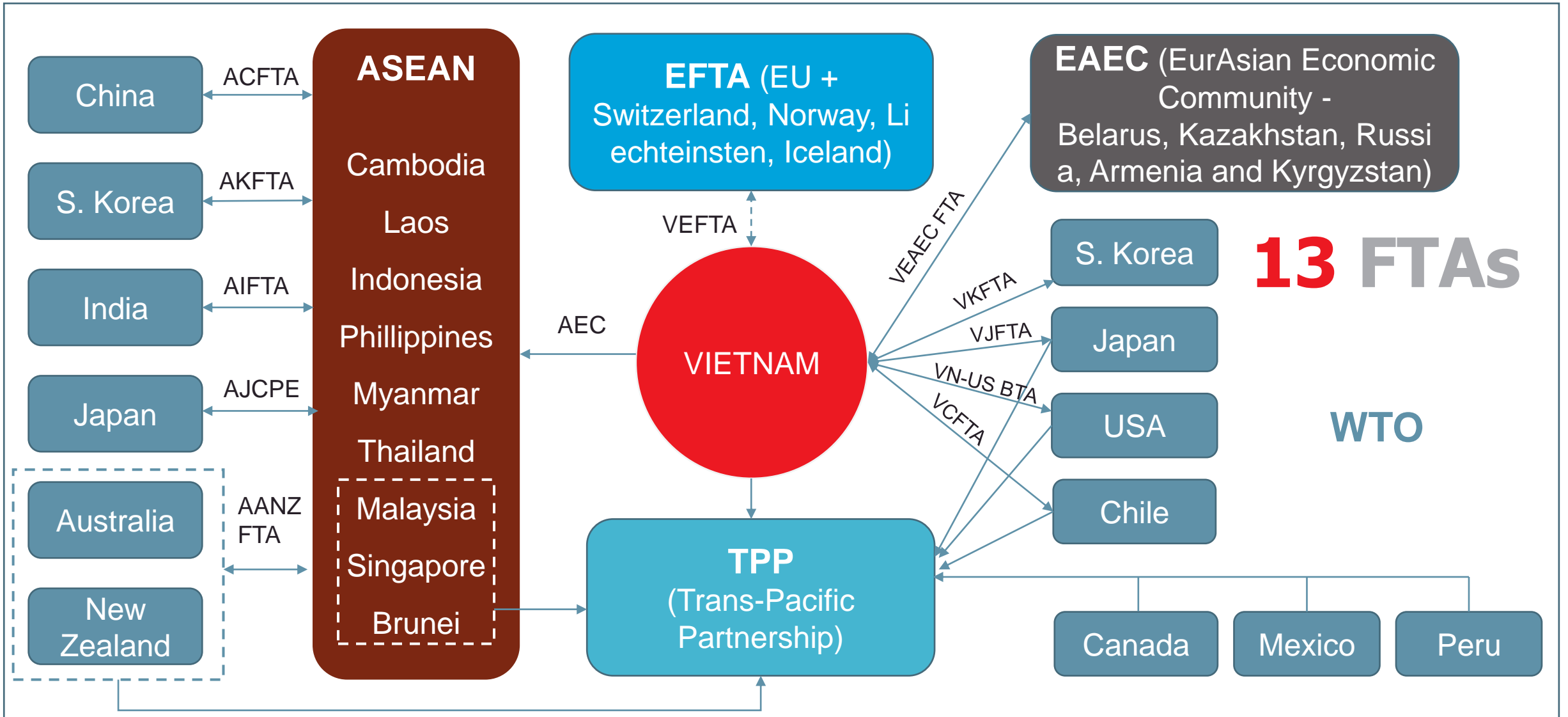
Emerging perception: **PSEs** are the **major pillar** of Vietnam economy

“ It’s important to realise that if we don’t pay proper attention to domestic firms, we may not succeed in economic development. ”

Mr. Bui Quang Vinh,
Minister - Ministry of Planning & Investment



#7. Integration: opportunities along with challenges



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62 BITs

#7. Integration: opportunities along with challenges

Expected contributions

High-standard FTAs can play a vital role in **attracting FDI**.

FTAs help Vietnam's enterprises **move up the value chain**, compete in more advanced economic sectors and supporting higher quality of jobs.

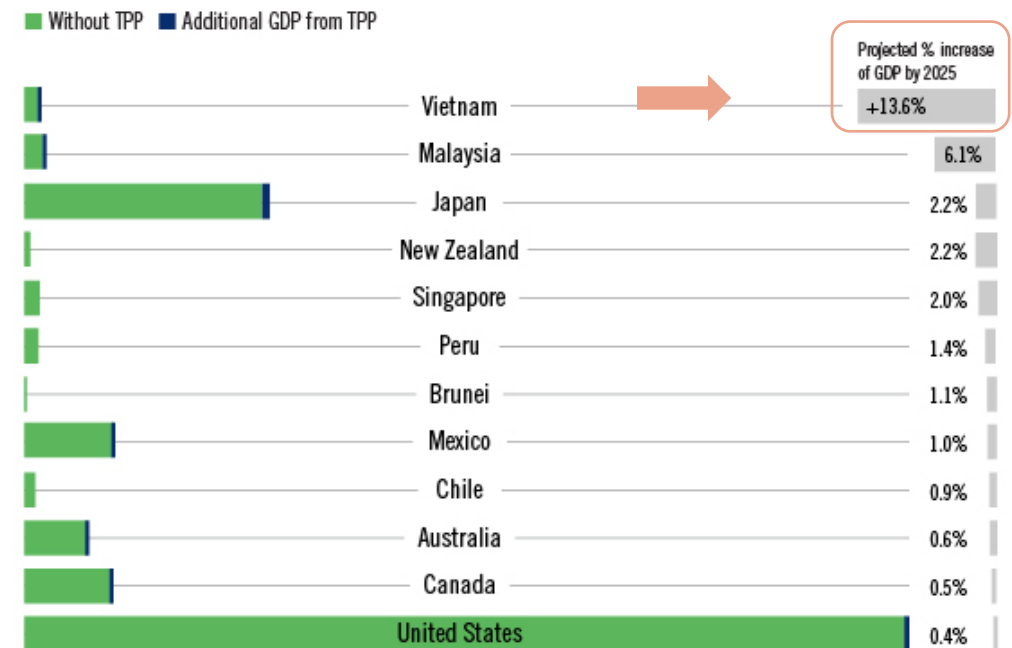
Technology transfer

(cleaner technology for a sustainable development) can be supported.

FTAs can **boost small business exports** by reducing trade costs, lowering risks, and opening new markets for SMEs. FTAs are expected boost direct exports by SMEs to 25% of Vietnam's total exports.

The “heavy lifting” of concluding comprehensive trade agreements with the United States and its FTA partners also makes it **easier for Vietnam to negotiate** - and benefit from - additional higher-standard FTAs with new trade partners.

Projected GDP by 2025 in the 12 TPP Nations



Risks & Challenges

- Vietnam companies may **not be ready** for dealing with challenges
- Vietnam has **a low competitiveness level** (labor-intensive economy), while main trading partners are productivity-driven economy (Chile, Mexico), or innovation-based economy (US, Canada, Japan, Singapore, Malaysia, Australia, New Zealand).
- Tough **requirements** to meet: Rules of origin, Sanitary and Phytosanitary Standards, Technical standards, Intellectual property
- Government lacks appropriate **policies** to support vulnerable industries.

Industries are most vulnerable to FTAs entries



Livestock industry



Pharmaceutical industry



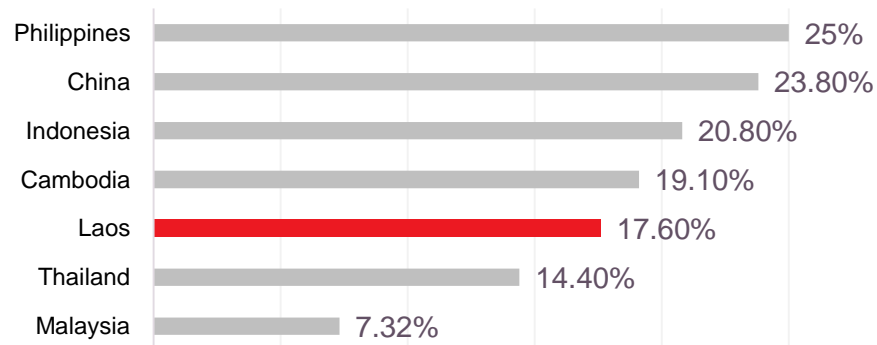
Sugar industry

#8. Challenges to reform: a mountain to climb

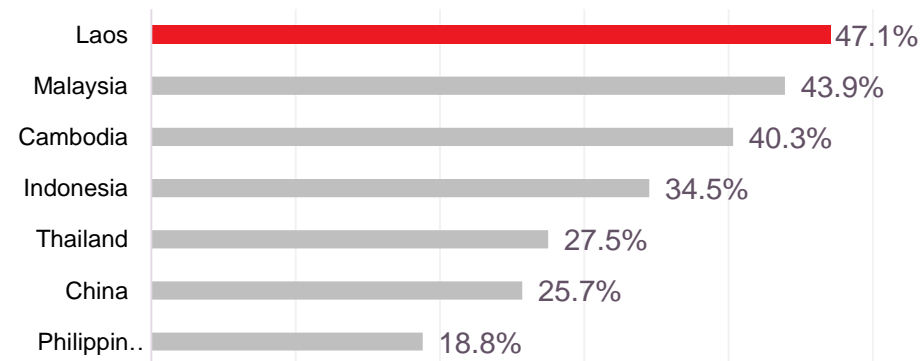
“How would you compare the business environment in Vietnam to other countries in which you considered investing?” (PCI Vietnam 2014)

% Firms **agreeing** Vietnam is **superior than** neighboring countries in aspects of:

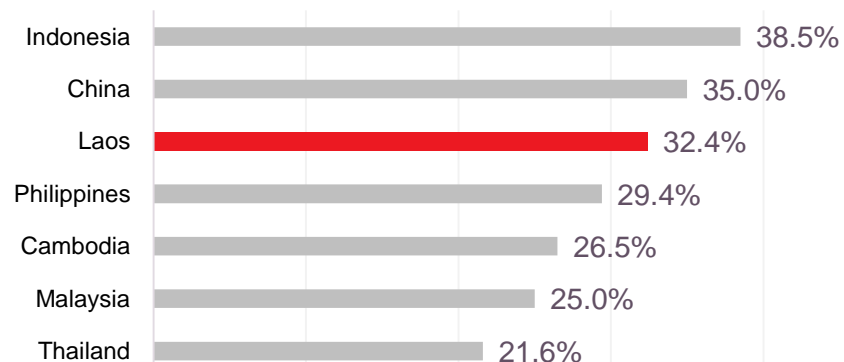
Less Corruption



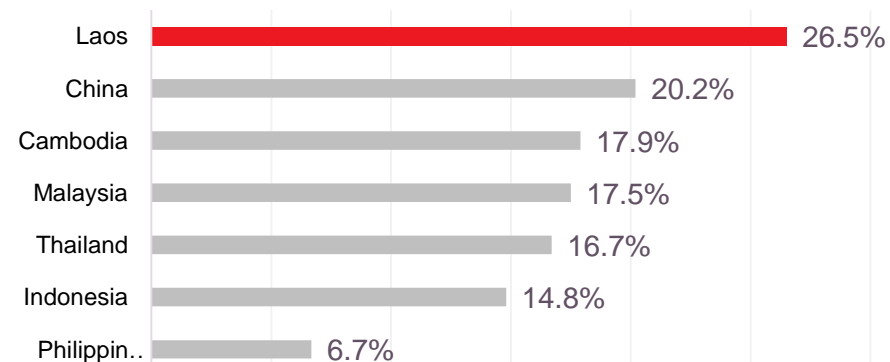
Better Infrastructure



Fewer regulations



Public Services better

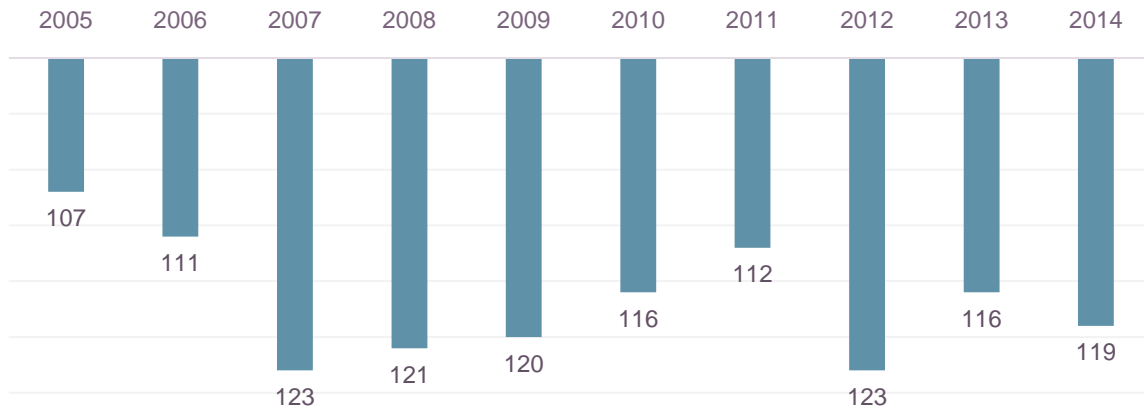


Weaknesses of Vietnam relative to neighboring countries in 2013 & 2014 are:

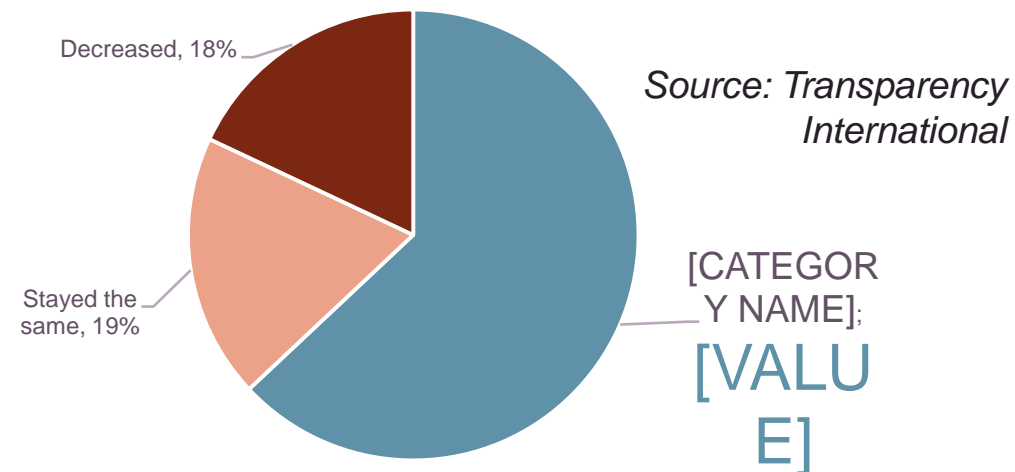
- corruption
- quality of infrastructure,
- regulatory burdens,
- quality of public services

#8. Challenges: a high mountain to climb

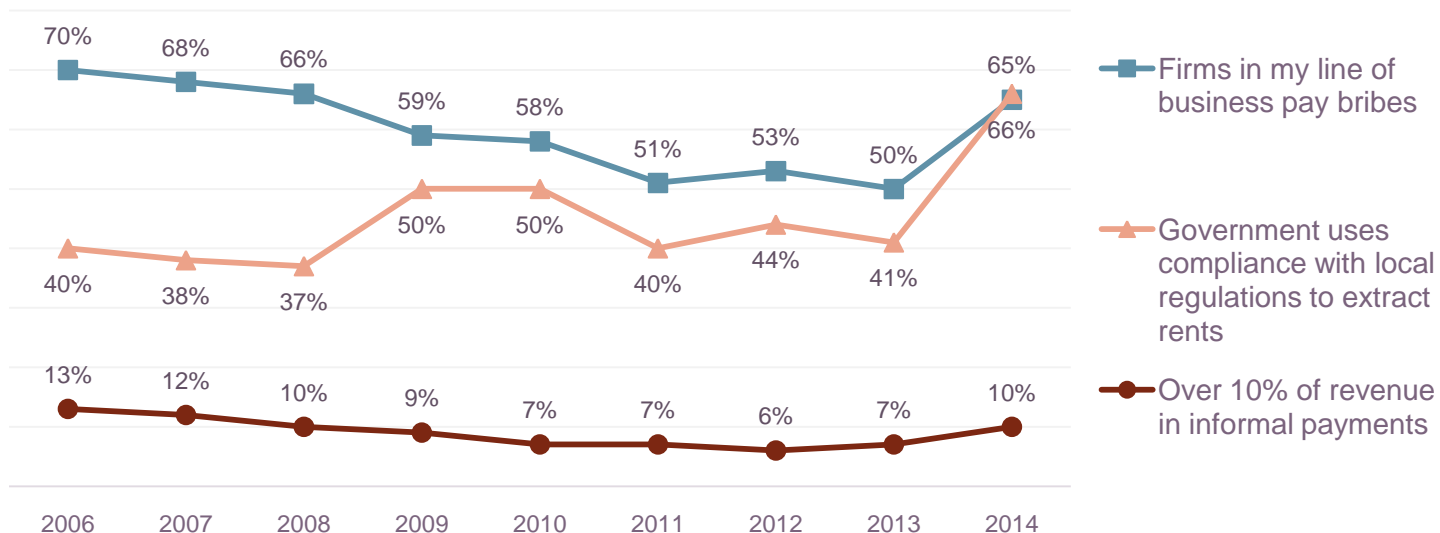
Vietnam's rankings in Corruption Perception Index



Percentage of people who feel that from 2007-2010 the level of corruption in Vietnam has:



Key indicators of informal charges (2006-2014)



Source: PCI Survey Questions: To what extent do you agree with these statement, "Firms in my line of business pay bribes", "Government uses compliance with local regulations to extract rents", and Percentage of revenue firm has to spend for informal payments. Figures reports the scores in the median province.

#8. Challenges: a high mountain to climb

Regulatory Burden: thousands of official letters (administrative orders/ công văn) each year



Reflect an inconsistent, non-transparent and unpredictable legal system



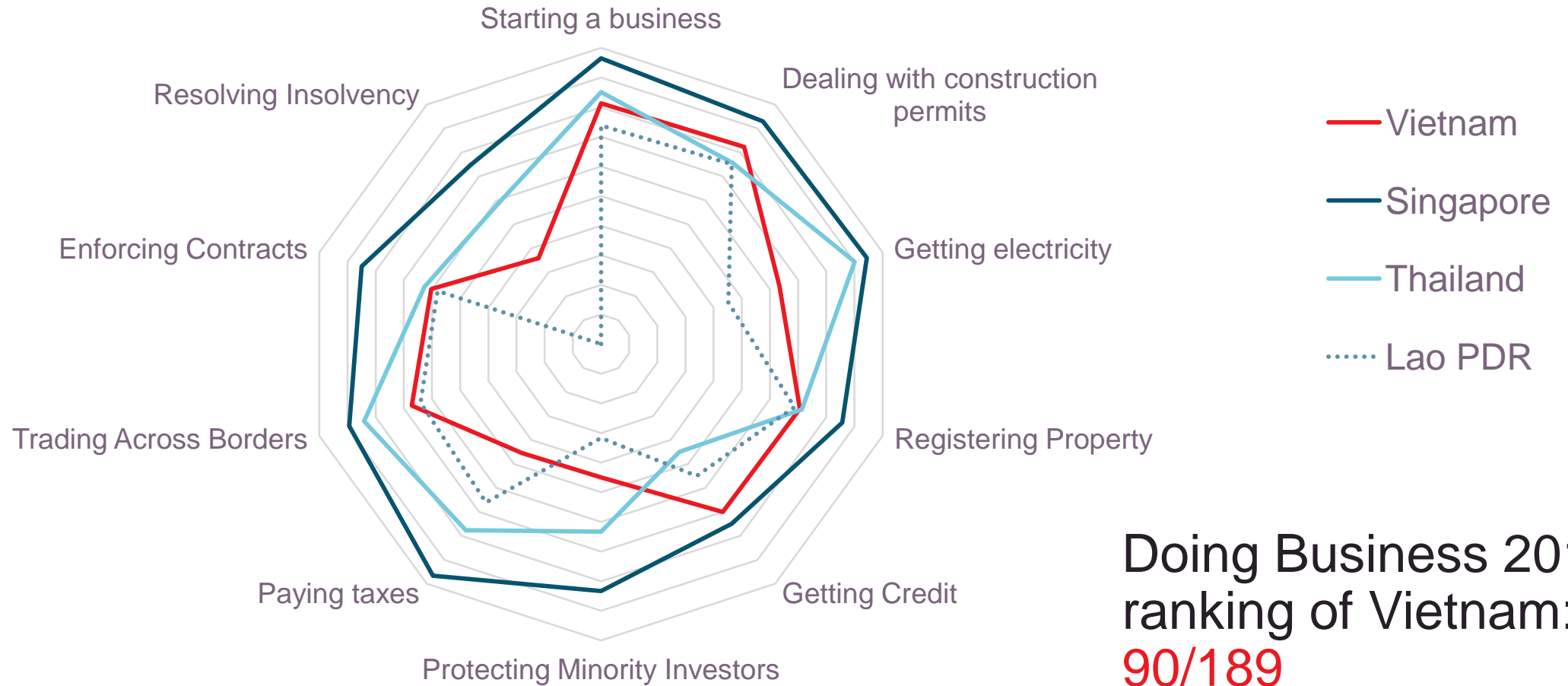
Increase the cost of compliance and create legal risks for enterprises



Negatively affect the competitiveness of enterprises in Vietnam

#8. Challenges: a high mountain to climb

Key indicators in Doing Business 2016



Doing Business 2016
ranking of Vietnam:
90/189

#8. Challenges to reform: a mountain to climb

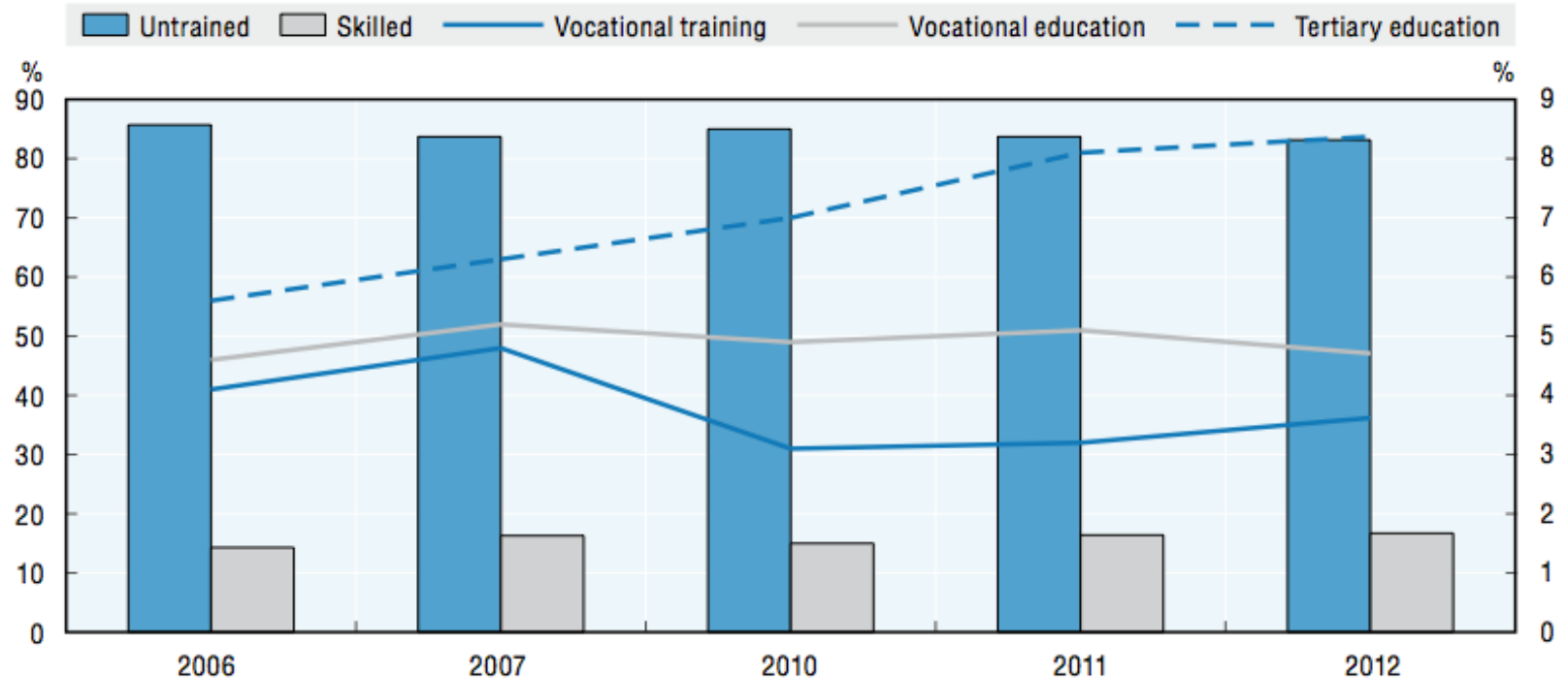
Low percentage of skilled workers in the labor force, the figure struggled to increase

- Percentage of untrained workers **hardly improved**
- University and training institutions failed to offer **skilled workers** for companies.

→ Rapid demand for skilled labor is not met by the market supply

→ obstacle to raise competitiveness and achieve growth goals

Structure of labor market in Viet Nam, by skills (%), 2007-12



Source: Economic Outlook for Southeast Asia, China and India 2014: Beyond the Middle-Income Trap © OECD 2013

#9. Reforms continue to progress but at gradual pace

The first structural reform – “Doi Moi”

Since 1986, Vietnam has embarked a vast program of structural reforms with objectives of turning a centralized economy into a **market-based economy** with **socialist orientation**

- Abolishing agricultural collectives
- Removing price controls on almost all traded goods&services
- Encouraging the establishment of private businesses
- Opening up the domestic market to foreign investment, including foreign-owned enterprises
- Liberalizing gradually the banking sector so that interest rates are determined according to market conditions
- Developing and improving the efficiency of the domestic markets for goods/services & for capital (stock/bond markets)
- reformed legal system through revising Laws and Codes.
- Actively joining in international integrations.



Photo: *The 6th National Congress of the Communist Party of Vietnam marked a turning point of the economic development*

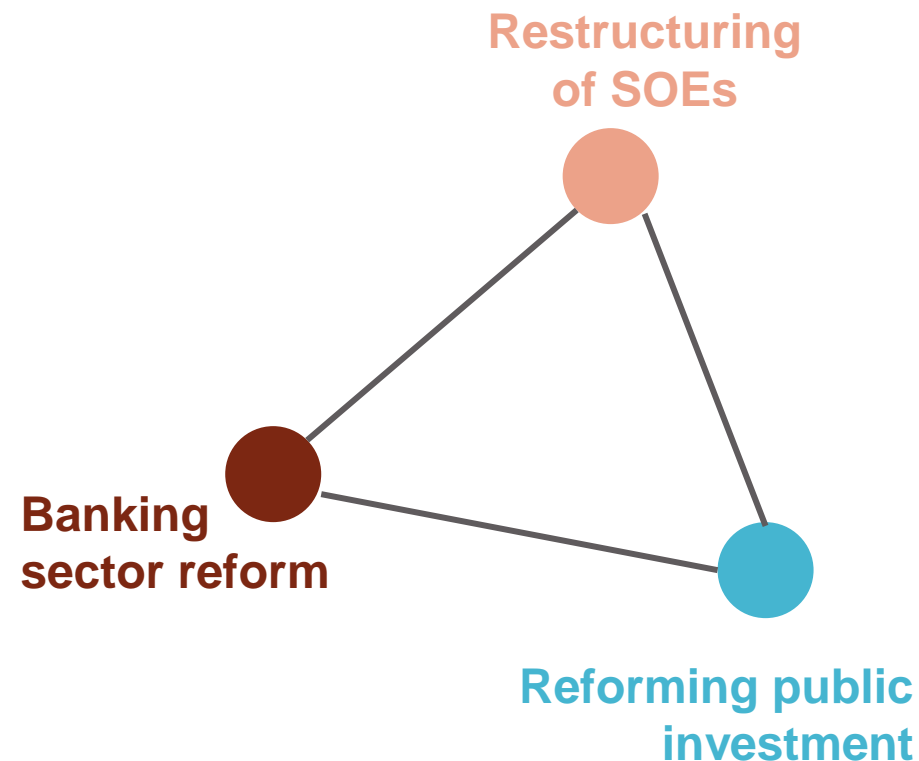
#10. Stronger reforms much needed

The Socio-Economic Development Strategy 2011-2020

Continues the 1st structural reforms, while paying more attention to environmental sustainability, social equity, and emerging issues of macroeconomic stability.

It defines three “**breakthrough areas**”:

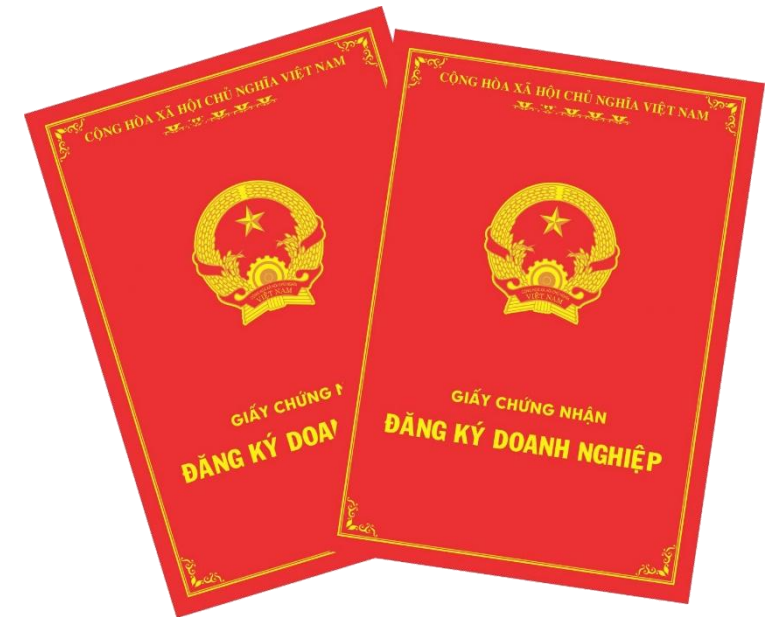
- i) promoting human resources/skills development (particularly skills for modern industry and innovation),
- ii) improving market institutions, and
- iii) infrastructure development



#9. Vietnam is in need of the second structural reform

Economic governance and institutional reform

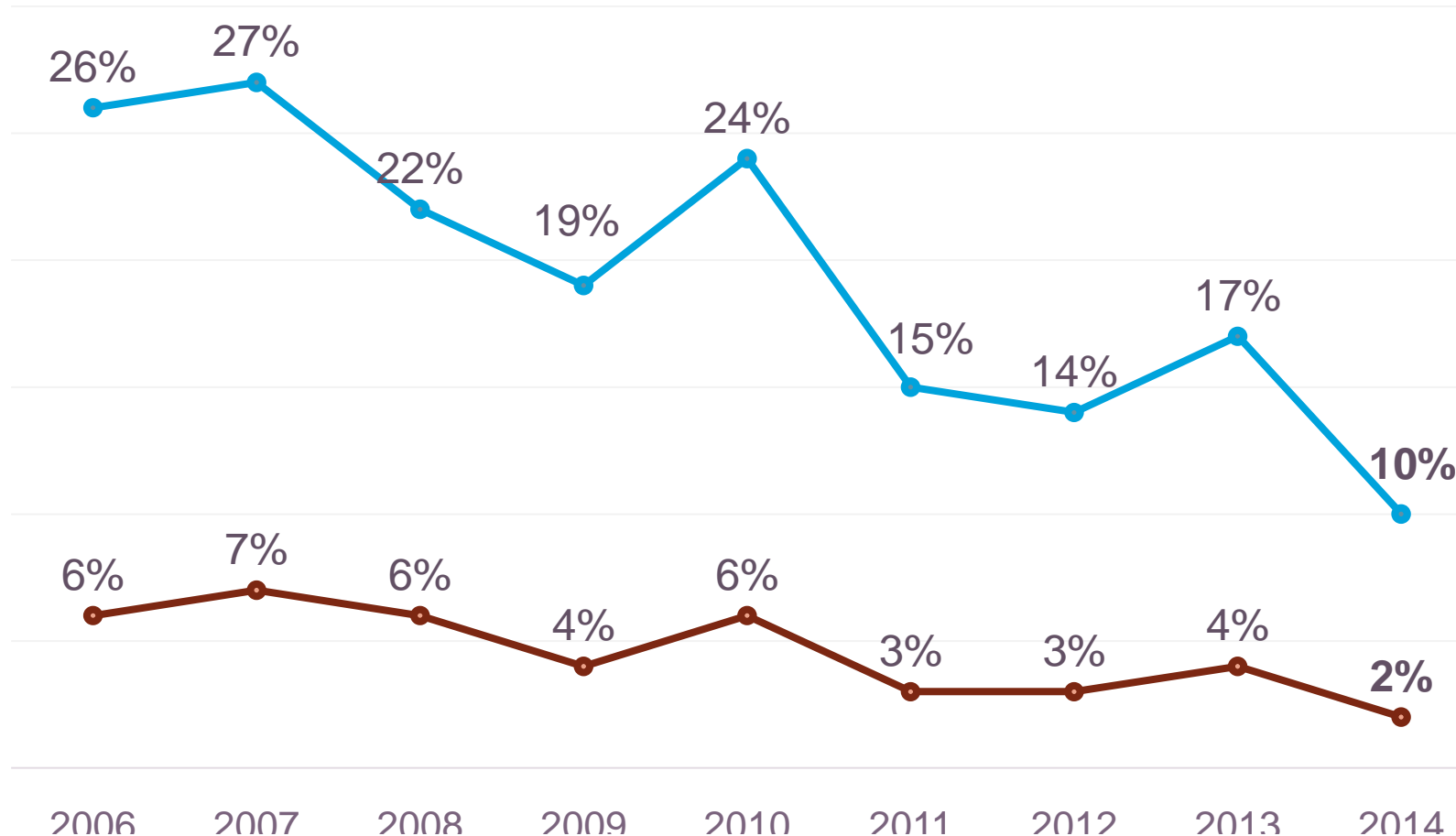
- 2014** ● Have been really done business in all non-prohibited lines, which are reduced to just 6.
→ Lower risks, costs and improve business climate
- 2000s** ● Was done business in any business lines which were not prohibited by the State, but had to register to official agencies.
→ Less complicated and reduced costs.
- 1990** ● Private business was legally accepted, but was only allowed to produce and trade in business lines stipulated by the State
→ Very complicated procedures and high costs



Enterprise Law and Investment Law were reformed in 2014 has offered more opened and free business environment.

#9. Vietnam is in need of the second structural reform

Indicators of entry costs (wait time to be fully legal)



Positive changes: the typical wait time for a firm to be fully operational reached a record low in 2014.

Source: PCI Vietnam 2014

- Wait more than 1 month
- Wait more than 3 months

#10. Stronger reforms much needed

Resolution No. 19/NQ-CP

Target of **2015**: time for admin procedure will be decreased a half compared with current time period and as same as 6 *developed countries in ASEAN and China*.

In **2016**, strive for improving the index of Vietnamese business environment for reaching at least reaching the average of the ASEAN-4 countries.

“ *All the ministries and local authorities must consider boosting administrative reforms, improving the business environment and enhancing the economic competitiveness as the key tasks in 2015 and 2016.* ”

Vietnam's Prime Minister
Nguyen Tan Dung



The **Resolution No. 19/NQ-CP** stipulates in particular tasks that **each ministries, agencies, local governments** should focus on implementing in 2015.



A short **summary**

10 highlights

1. The number of PSEs is increasing dramatically, and small and medium enterprises are in majority
2. PSEs – numerous workers but low productivity
3. PSEs tend to have low and informal innovation
4. SOEs remain an important player in the economy thanks to special treatments from the government
5. FDI inflows have increased over 25-year period. They are offered many types of preferential treatments. FIEs now become the driving force for exports, but other contributions may be not commensurate.
6. The performance gap between three enterprises sectors is widening.
7. Integration: opportunities along with challenges
8. Challenges: a high mountain to climb.
9. Reforms continue to progress but at gradual pace
10. Stronger reforms much needed

- VCCI, USAID. 2014. Provincial Competitiveness Index of Vietnam.
- CIEM, GSO, UoC. 2014. Firm-level technology and competitiveness in Vietnam. Evidence from a survey in Vietnam.
- World Bank. 2015. Are there preferential treatments of State-owned enterprises? A review of regulatory framework and evidences from practice
- OECD. 2013. Economic Outlook for Southeast Asia, China and India 2014: Beyond the Middle-Income Trap ©
- Duc Khuong Nguyen. 2015. Past experiences and new policies to cope with ongoing challenges and to sustain economic growth
- Sources: Office of the U.S. Trade Representative, “TPP Issue-by-Issue Information Center, E-Commerce and Telecommunications,” <https://ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership/tpp-chapter-chapter-negotiating-6>. Asian Development Bank.
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- <http://gso.gov.vn>
- <http://moit.gov.vn>
- <http://mpi.gov.vn>
- <http://ciem.gov.vn>