Chapter 6:  Emerging Issues and Recommendations

In chapter 5, we analyzed the state of Vietnam’s competitiveness and growth through six determinants and point out its progresses as well as existing weaknesses compared to some selected neighboring countries. This chapter is basic for exploring in the following chapter.

In chapter 6, we first present some emerging key issues of Vietnam’s competitiveness growth based on the analyzing of the previous chapter, including production resource shortage and low quality, outdated technology, bureaucratic and corrupt administration, and slow SOEs reform. In the second section of the chapter we propose some recommendations to enhance Vietnam’s competitiveness and sustain its growth in coming years such as: address production resources shortage and quality; develop an independent and vibrant domestic private sector; strengthen public institution and government effectiveness. Each above mentioned solution includes some detail recommendations.

6.1  Emerging Issues of Vietnam’s Competitiveness

The “Doi moi” policy has brought expressive economic fruits and radical changes within the economy. Physical infrastructure and human resource have been improved compared to the previous phase, and the financial market has been initially set up. International trade and foreign investment activities have become more liberal and open, and as a result they have performed remarkable achievements. The business environment has become more attractive due to simplification of administrative procedures. As a result, investment (both foreign and domestic) has risen over time, by which productivity and competitiveness have been improved. However, the competitiveness of the Vietnamese economy appears to have many weaknesses and causes some concerns, especially compared to some neighboring countries. The emerging key issues are namely: the shortage and low quality of production resources such as inefficient and poor infrastructure, lack of skilled labor and the under-developed financial market; out-dated technology; bureaucracy, red-tape and corruption; and inefficient SOE operation and slow privatization process.

6.1.1  Production Resources Shortage and Low Quality

Over decades Vietnam has gained progress in providing production resources such as infrastructure, human resource, capital resource and natural resource. However, there have been some challenges that Vietnam has had to face: ineffi-
cient and poor infrastructure, shortage of skilled labor force and undeveloped financial market.

**Inefficient and poor infrastructure system** In a comparison with Thailand and China, Vietnam has performed infrastructure services less well than its regional competitors. Among the access indicators presented, Vietnam lags in terms of transportation and teledensity (Table 5.1).

Telecommunication is considered as the most efficient industry in the infrastructure service sector, but its labor productivity is poor compared to productivity in neighboring countries. Telephone mainlines per employee are 50, compared to 160 and 225 in China and Thailand respectively (World Bank 2006a).

An alternative perspective on what is important for competitiveness can be provided by business perceptions surveys. The World Bank’s investment climate surveys asked small, medium and large manufacturing businesses about 18 potential constraints to their businesses. Transport and electricity were ranked the 3rd and 4th most severe constraints. Transport is seen as a major or severe constraint for 24% of manufacturing firms, and electricity is a severe constraint for 19%. Transportation is considered as a greater constraint in Vietnam than in neighboring countries for which these surveys were conducted (World Bank 2006a). For electricity, the main problems are perceived to be the price and the quality. Sixty percent of firms consider the price of electricity to be excessive. In fact, EVN is reasonably efficient in terms of cost, and a requirement for EVN’s sustainability is that tariffs cover costs, so that there is little to be done about these concerns in the short term. More significantly, forty-one percent of firms are concerned about the poor quality of electricity services. Power outages and surges are estimated to cost manufacturing firms the equivalent of 3.2% of their sales. Around a third of firms have bought generators to cope with EVN’s unreliability. The unreliability imposes substantial costs even for those with generators (about 10 cents per kWh or twice EVN’s average tariff). These concerns suggest that investments in increased generating, transmission and distribution capacity, as well as reductions of system losses, are the main priorities for electricity.

Losses of electricity in transmission and distribution still perform poorly in comparison with China and Thailand. To some extent this comparison is unfair. For example, China has a higher proportion of businesses receiving high voltage supply, and therefore has lower distribution losses.

At 7.1% of total road expenditure in 2003, Vietnam has the lowest maintenance expenditure in the region and trends downward. Neglect of maintenance is inefficient since it is likely to increase long-term maintenance costs.
Vietnam’s trains have low operating speeds of 40 km/h for passenger trains and 22 km/h for freight trains. Due to the lack of maintenance and new investment, the rail network has deteriorated. Labor productivity is low at 124,000 traffic units/employee, compared with 548,000 in Thailand and 610,000 in Indonesian. Accident statistics for Vietnam’s railways suggest a neglected network. In 1998 there were 41 deaths per 1000km of track. This figure increased to 271 in 2003. Corresponding figures for Indonesia were 11 in 1998 and 16 in 2003, and for Thailand: 5 and 2 respectively (World Bank 2006a).

Causes of inefficient and poor infrastructure services are provided solely by SOEs and there is little room for competition In Vietnam most infrastructure services are provided by state-owned enterprises. Corporate governance is under the Law on State-Owned Enterprises. SOEs are not subject to the general principles of private sector corporate governance, and are not able to make their own autonomous commercial decisions. To the extent that business strategies exist they are embodied in sector Master Plans prepared by line ministries, personnel policies are controlled by the Ministry of Labor, Invalids and Social Affair, the Ministry of Planning and Investment approves their investment projects and the Ministry of Finance grants fund.

Corporate governance in Vietnam is generally said to be weak. A new Unified Enterprise Law (UEL) was enacted in 2005 for implementation beginning April 1, 2006. It is intended to provide common and improved rules of corporate governance for domestic and foreign private firms. But SOEs will only be subjected to the new UEL if they are specifically converted into either single member limited liability or joint stock companies. Subjecting infrastructure SOEs to the UEL would be a logical element of any corporatization program, but there currently seem to be little impetus in this direction.

Competition is the most powerful mechanism for improving efficiency. Competition provides firms with the incentives to keep costs to a minimum, to offer products that are better adapted to the needs of consumers, and to adapt new technologies as they become available. However, there is no competition in infrastructure (except telecommunication). In other words, state monopoly dominates in supplying infrastructure services. The continuing philosophy is generally one of trust in government planning processes and bureaucratic performance targets rather than market competition. For example, in telecommunications international experience strongly suggests that the speed of network rollout is accelerated by greater competition. Unfortunately, Vietnam is lagging behind in international best practice. Several new entrants have been authorized to compete with VNPT in fixed line and mobile services, but VNPT remains dominant, with a 90-94% share of the entire telecommunications market (including segments such as equipment con-
struction and installation). Vinaphone and Mobilefone, despite a common parent, do seem to compete, perhaps in part because they have business cooperation contracts with foreign partners. Four SOEs have been licensed to enter fixed and cell line markets, because they have traditionally had their own private networks. SPT is present in Ho Chi Minh city; Hanoi Telecom is present only in Hanoi, Viettel is an SOE owned by the military; and Viet Power Telecom is owned by EVN, the electricity utility. Effective regulation, in particular spectrum management and resolution of interconnection disputes, will be important in facilitating the progress that could be made by allowing the entry of foreign firms. In this respect, the United States has obtained an early advantage, obtaining preferential access for its firms under the Bilateral Trade Agreement (BTA). But even these advantages limit foreign ownership to 49% and 45% in the mobile and land line services markets. These limits restrict the potential for competition to drive greater investment and improved services.

At the moment Vietnam’s efforts to involve the private sector in infrastructure sectors is largely focused on meeting financing needs through the equitization program and BOTs, rather than improving infrastructure efficiency. But private participation can be introduced as a means of improving efficiency, especially when introduced through competitive bidding for the right to serve a market. Greater use of private participation as a means of improving enterprise efficiency would be encouraged with various institutional reforms.

In telecommunications, the main problems are perceived to be price and quality. The best solution to these problems may be greater competition. Greater competition would help to drive down prices, and would provide consumers with a choice in the event that they had problems with the quality of services from particular providers.

Shortage of Skilled Labor Force Despite rising educational level, 80% of the labor force is considered to be unskilled. Skilled workers are disproportionately concentrated in and around the main cities such as Hanoi or Ho Chi Minh city. There is a shortage of trainers; trainer-student ratio in Vietnam is one to 28, while the world average ratio is one to 1592.

Adapting content to the needs of a market economy is especially important in the case of vocational training. According to a recent ICA93 report, the third most important constraint faced by enterprises in manufacturing, after access to finance and access to land and infrastructure, is the shortage of appropriately skilled workers.  

92 Ministry of Labor, War Invalids and Social Affairs (MOLISA)  
93 Investment Climate Assessment
workers. Only 40 per cent of workers in foreign companies operating in Vietnam have received professional training, according to the Ministry of Planning and Investment. To some extent, the severity of this constraint reflects the fast labor turnover characterizing the Vietnamese economy. Workers use the assignment with the best companies (especially, those with foreign technology and management) to learn on the job and then rapidly move on, either to create their own businesses, or to get jobs with bigger responsibilities in domestic private companies. With rapid economic growth, and the change in economic structure toward activities with higher value added and knowledge content, labor skills will have to be upgraded. However, current training programs are often outdated because teaching tools lag far behind the development of technology, particularly technology of FDI enterprises (Mac Van Tien 94). Additionally Initial training is still input-oriented and follows curricular requirements instead of workplace requirements.

Undeveloped Finance Market This development of financial market is the result of a series of reforms aimed at adapting the banking sector reform accelerated in 2001. It is not quite surprising when the survey result of WEF shows that the soundness of banks is relatively high, compared to neighboring countries, especially China, and equal to Thailand (Figure 5.4). The access to the local equity market of Vietnam scores higher than China, Philippines and Indonesia and just slightly lower than Thailand and Malaysia. However, the capital markets, which aim at supplying the economy with medium-and long-term risk capital, remain underdeveloped. The government debt market and especially the corporate bond markets are still in an early development stage. In addition, the banking sector remains financially weak and may benefit from more competition to accelerate its current reform agenda. The obstacles of access to loans, particularly SMEs, reflect an inefficient and monopolistic bank system. Our survey conducted in early 2007 shows a consistent outcome. Most respondents complain of restrictions of access to loans from SOCBs, especially private enterprises (Appendix 6).

The banking system faces several major difficulties due to its financial support of SOEs and its failure to operate solely on market-based principles. Vietnam’s banking system is regulated and controlled by the central government, which set interest rates and attempts to allocate credit to certain Vietnamese firms. The central government has used the banking system to keep money-losing SOEs afloat by pressing state banks to provide low interest rate loans, without which a large number of the SOEs would likely go bankrupt. As a result, Non-Performing Loans (NPLs) of SOCBs were estimated at approximately 15 percent of the total credit as of May 2005, which was around 8% of the GDP (World Bank 2006b, p. 19).

94 Director of the Vocational Training Science Research Center
The high volume of bad loans now held by Vietnamese banks poses a serious threat to Vietnam’s banking system. Assessment based on International Accounting Standard (IAS) audits suggest that the overall quality of the SOCBs portfolio is not improving (Ibid., pp. 30). On the contrary, according to the judgement of external auditors analyzing the limited information the SOCBs have already suffered from capital shortfall. In addition, the supervisory capacity of the SBV over the banking system is limited, as its methods are still based on compliance with mechanical rules, with little focus on risks. The institutional organization does not, as four simultaneous inspection-related systems co-exist, whereas an extensive provincial branch structure results in overlapping functions and responsibilities. More importantly, the SBV faces an inherent conflict of interest, as the regulator of a banking system that is still dominated by the SOCBs it owns. The SBV must act as the sole shareholder in the SOBCs, which have no independent board members, face serious corporate governance problems, and are subject to interference from various government authorities. Not surprisingly, the incentive structure within the SOCBs is not tied to performance targets and credit risk management practices remain weak.

The capital markets are still in the early stage of development. The securities market has benefited from the increasingly positive assessment of Vietnam’s economic potential by the international community, but it still suffers from important shortcomings, including under-developed regulations and supervisory mechanisms, an insufficient trading infrastructure and weak information system. The bond market is hampered by fragmentation. This is due to the multiplicity of channels and methods used for the issuances, and to a pattern of “buy and hold” used by investors, which results in little secondary trading. The corporate bond market remains very small, tapped only by a few large SOEs. The insurance market has been especially dynamic in relation to life, but less so in relation to property. This market suffers from an inadequate regulatory framework in relation to taxes, entrance, investments and exit. Tools such as factoring and leasing could serve to meet the needs of SMEs but are constrained due to the inadequate regulatory framework, limited funding resources, low public awareness and lengthy foreclosure procedures. As a result, the precarious state of the financial markets in general and the banking system in particular has made Vietnamese reformers reluctant to open the banking sector to foreign competition.

6.1.2 Backward Technology

Technology in Vietnam has been improved over time, allowing productivity and competitiveness to progress. However, in fact, technology development in Vietnam still lags behind its neighboring countries. Capacities of creating new technologies are still limited and could not meet requirements of the country’s indus-
trialization and modernization process. The growth of production capabilities has not led to a similar deepening of capabilities into design, research and new technology development. Such deepening is an increasingly important part of the development process as the industrial sector diversifies and uses more complex and fast-changing technologies. It is particularly important for export-oriented industries that have to continuously upgrade their processes and products. The technology development has been faced with being far behind in strong technology development tendencies and knowledge-based economy in the world.

The survey we conducted in Vietnam in early 2007 indicates that technology development in Vietnam still lags behind other ASEAN countries (Appendix 6). The other finding conducted by WEF in 2005 was consistent with ours. The figure 6.1 also shows that the relatively weak R&D linkages between university and industry research collaboration stem, in part, from problems of low quality of research institutions and universities. The survey indicates that Vietnam public research institutions and universities are not sufficiently responsive to the needs of industry and company, emphasizing academics over commercial applications in their research orientation. Vietnam receives a low score and tails countries in the region such as Thailand, China, Indonesia and Malaysia. This result roots from main causes as follows:

**Low Investment** As compared with other countries in the region, the country is still faced with very big gaps in investment in technology development. An average investment of one research program is 5,000 US dollar and that of one researcher per year is 3000 US dollar.

This rate lowers 4th, 7th, 8th, 26th-fold, compared to Thailand, China, Malaysia and Singapore respectively. The share of technology development investment from non-state sector only accounted for 9% of the total investment. This share is far behind, compared to 60% in Malaysia, and 45% in China. The R&D investment from Vietnamese companies accounted 0.01% of their total revenue. It is also very low, compared with 5-6% in NICs and 10% in developed countries. This results, in part, from the financial management mechanism of S&T activities. The mechanism hasn’t created favorable conditions for scientists and mobilized many non-State capital sources; the finance autonomy mechanism of S&T organizations hasn’t been linked together with the autonomy in the human resource management so the efficiency is limited.

95 Vietnam science and technology development strategy by 2010, p10
96 Centre Institute of Economic Management (CIEM)
Figure 6.1: Survey Technology Development

Source: WEF, survey 2004-05

Shortage of scientists There is a lack of planning on training high-level professional workforce in prioritized S&T fields, especially scientists. In fact, Vietnam lacks of the world and regional class researchers. The competence of Vietnamese scientists is still limited, in part, due to low foreign language and computer skills. Therefore it is impossible to update state of the art research in the region and world and joint international conferences.

Poor technology development environment including S&T information, consultancy for technology transfer, intellectual properties, and standard-measures-quality are still poor in terms of both facilities and capacities for providing services which can meet requirements of regional and international integration. For example, in 2004 Vietnam had zero (0) internet hosts per 10,000 inhabitants, compared with 1.3 in China, compared with 16.6 in Thailand and 1,155.3 in Singapore 97. In the same year Vietnam had 12.7 personal computers per 1000 inhabitants, whereas there were 40.88 for China, 58.34 for Thailand, and 196.83 for Malaysia (Figure 6.2)

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97 International Telecommunication Union, June 2004
In addition, the intellectual property rights regime remains weak. The legal framework should ideally provide enterprise with a strong incentive to undertake R&D and commercialize innovations. Few private investors would invest on R&D activities in a situation where everybody benefits and few carry the cost. Strong intellectual property rights regimes are therefore a key component of promoting R&D activities in any society since they allow innovators to receive a return on their investment. Vietnam officially adheres to most treaties and international agreements on intellectual property rights. However, some elements of the enforcement regime are still at variance with Vietnam’s international obligations. Particularly copyrights protection remains a problem. The Vietnamese government has made few efforts to impose criminal penalties in commercial piracy cases and stop counterfeit importation. Bottlenecks in the judicial system have caused substantial delays in the completion of the criminal and civil infringement cases. Figure 6.1 reveals a low perceived protection of intellectual property rights in Vietnam compared to ASEAN-4 countries and China.

**Limited cooperation** There is a lack of organic links among S&T research, education-training, production-business, and a lack of close cooperation among research and development organizations, universities and enterprises. The model of R&D organizations and their mechanism have not encouraged research institution, university and company together to collaborate (Figure 6.1).
In general, Vietnam’s S&T capacities are still weak. Issues that have arisen in the renovation process can’t timely be solved and can’t closely link with and meet requirements of the socio-economic development.

6.1.3 Bureaucracy, Red Tape and Corruption

Administration reform has brought considerable changes to the procedures and impacted positively social economic development, especially within the business environment. The significant simplifications in business registration introduced by the Enterprise Law of 2000 (now new Unified Enterprise Law) has led to a perceptible reduction in the number of licenses in force. The positive perception on licenses and permits can also be reflecting the success in introducing the one-door model for administrative procedures at the local level. However, administration in Vietnam is still cumbersome, with red tape and much overlapping. In addition, the law system is lax and its enforcement is weak. These salient characteristics of the administration system and institution result in emerging corruption.

Bureaucracy and red tape administration procedures are time consuming and unnecessary. The survey we conducted shows that administrative regulations are burdensome. The indicator represents an average of 2.67 (on a scale from 1 to 7 where 7 corresponds to the highest integrity standards) of which 3.28 was scored by officials, 2.29 scored by executives, and 2.58 scored by scholars. It appears that most respondents, including officials, stated a disagreement with administrative procedures. It is also not surprising that officials mark a higher point compared to executives and scholars (Appendix 6).

A previous survey of enterprises jointly conducted by CIEM and GTZ shows that in order to operate a firm, it needs to go through 13 administrative procedures, taking 260 days altogether. Nevertheless, 231 days in this estimate correspond to the time needed to acquire land, under the assumption that the enterprise wants to purchase it from the government and needs to go through land clearance and compensation of resettled populations. Getting land in an industrial zone would reduce the waiting period, on average, from 231 days to 83. And delays possibly can be much shorter if the land was purchased or rented from other enterprises. In contrast, the business registration process is narrower, only 15 days are required by Enterprise Law and the exercise requires fewer days98. This obstacle causes the land administration

98 The CIEM-GTZ study found that the deadline was respected in two thirds of the cases, with only 5 percent of firms having to wait for 30 days or more. In many provinces the registration process was actually completed in less than one week. Similarly, 70 percent of the firms surveyed received their tax code within seven days, and solely 6 percent of them had to wait for more than 15 days.
agency to rank first\textsuperscript{99} in corruption among administration bodies in Vietnam. Findings were similar in the survey of competitiveness conducted by WEF; the burden of government regulations is higher than in China, Thailand, Indonesia, Malaysia and only lower than in the Philippines (Figure 5.21).

Corruption is a consequence of weak governance and burdensome administration as well as the shortage of a law system and weak law enforcement. It represents a serious threat to development progress as well as undermines productivity and competitiveness because it raises the cost of doing business and reduces confidence of domestic and foreign investors, hence slowing economic growth and job creation. In recent years, Vietnam has made efforts to fight corruption, however, the success of these efforts are still quite limited. The commitments of Vietnam government relating to fighting corruption have translated into a series of important international agreements and legislative undertakings. Vietnam signed the UN convention against corruption in December 2003, with the intention to ratify it in 2006. In 2004 it endorsed the ADB-OECD Anti-Corruption Initiative for Asia and the Pacific. And in 2005 it passed the Law on Anti-Corruption, which by and large covers compliance with the UN convention and takes into account the principles of the ADB-OECD Initiative. In 2006, the Corruption Perceptions Index of Transparency International gave a rating of 2.6 to Vietnam (111\textsuperscript{th} out of 163 countries), compared to 2.5 in 2000\textsuperscript{100} (75\textsuperscript{th} out of 77 countries) It appears that there is some progress in fighting corruption in Vietnam although corruption is widespread. In comparison with some selected regional countries, Vietnam got a higher grade, compared to the Philippines and Indonesia, but was lower than China, Thailand and Malaysia (Figure 6.3).

The diagnostic study of corruption conducted by the Central Committee on Internal Affairs (CCIA) was released in 2005. This study used an international methodology, combining surveys and interviews of citizens, public official and enterprises. Its results show that corruption is perceived as common and existing at all levels and in all organizations, although varying to a considerable extent. The respondents thought that land administration, customs, the traffic police, tax administration and construction registers were the most corrupt agencies\textsuperscript{101}.

\textsuperscript{99} The ranking based on survey conducted by ICCA
\textsuperscript{100} On a scale of 1 to 10 where 10 corresponds to the highest integrity standards
\textsuperscript{101} The finding is similar that was investigated by the ICA
The survey we conducted shows a relatively similar finding. The average score for corruption was 2.01, on a scale from 1 to 7 where 7 corresponds to the best, indicating that most respondents, including officials, business leaders and scholars, find the corruption to be pervasive. However, attitude towards corruption is quite different between officials and business executives. While executives marked an average score of 1.55, officials appreciated a higher average grade of 2.65. (Appendix 6).

The ICA survey reveals that the forms of corruption most commonly mentioned are soliciting bribes by creating obstacles, accepting bribes for favors, and using public means for personal benefit: The “ask-give” mechanism was identified as a major cause of the corruption.

The management of the investment projects appears to be more problematic. The recent PMU 18 scandal served as a warning about the risk of resources being misappropriated. At the same time, several investigations involving contracts under the investment projects showed how challenging it is to uncover corrupt transactions. A culture of “sharing” and “taking turn” somewhat undermines the effectiveness of conventional bidding mechanism. The corruption also takes the form

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102 The ICA survey is based on a large survey of manufacturing firms in the formal sector, including the domestic private sector, foreign companies and SOEs. The survey was conducted in 2005 in 25 provinces of Vietnam, using a representative sample. A private firm was in charge of the interviews, which were carried out without the presence of government officials.
of "gift exchange" not to be reciprocated immediately, but when an opportunity arises. Based anecdotal evidence, giving out fat enveloped at wedding and funerals and losing large sums of money in card playing and other games, are among the mechanisms used to channel the "gifts". To add to the murkiness, sometimes the beneficiary is not even the public servants who are supposed to reciprocate, but rather a close relative.

6.1.4 Slow State-Owned Enterprise Reform

Vietnam has undertaken SOEs reform since 1991. Yet, it still has had an unusually large number of SOEs compared to other countries in the region (except China)-around 4,086 firms\footnote{General Statistics Office (GSO), Enterprise Survey} and these enterprises account for 54.96% of the total capital in all enterprises. The pace of SOE reform has been slow. The survey we conducted shows that one of the priorities of the Government is to speed up the privatization process (equitization)\footnote{In Vietnam, privatization is understood as equitization}.

In the early 1990s, the number of SOEs was halved from about 12,000 to around 6,000. During the time between 1998 and 2002, the transformation process in the forms of equitization, divestiture, and liquidation has reduced the number to about 5,000. In 2003, a new roadmap for SOE reform was put into operation: 55 per cent were due to take place in 2003, but the transformations fell far short of the target (945 enterprises, or 62 per cent, out of a planned 1,459 that had been completed). More importantly, most transformed SOEs have been small and medium enterprises with chartered capital less than 10 billion VND (about 0.7 US$ million); only 23 percent of companies with chartered capital over 10 billion VND have completed the process. And the shares sold for now account for only 14 percent of the total SOE capital. In 2004, despite the efforts to accelerate the transformation process, including the equitization of some General Corporations and State-Owned Commercial Banks (SOCBs), there is still no significant improvement. In the first eight months of 2004, the number of equitized SOEs accounted for 35 per cent of the target, or 350 out of 1,000. Note that the new SOE reform roadmap issued in 2003 identifies the specific names and timetable of SOEs under transformation and annual targets over the period of 2003 and 2005. The reform of the banking system has also been sluggish. Moreover, the SOE reform roadmap seems to seriously not take into account the impacts of integration by economic sector; it largely emphasizes the size of enterprises. The postponement of SOE
and banking reform is not recommendable for many reasons\textsuperscript{105}. First, there is substantial welfare cost associated with the provision of fiscal subsidies credits to inefficient SOEs. Second, subsidizing SOEs would de facto lead to a redistribution of resources to the SOEs, thereby reducing resources available to finance poverty-reduction programs. The authorities may also request SOCBs to make loans to failing SOEs. This would only transfer the burden associated with keeping afloat inefficient SOEs to the banking sector, and create difficulty for the restructuring of SOCBs.

In addition, the equitization of SOEs has brought some concerns such as the valuation of SOE assets, state capital representative of equitized SOEs, overstaff and so on. So far, divestiture mechanism, involving public auctions, is considerably more transparent. But SOEs continue to face difficulties in relation to the valuation of their assets. How to appraise landholdings and intangibles remains one of the most contentious issues. Some SOEs are also facing excessive debt levels, which makes their divestiture difficult.

While equitization increases the autonomy of enterprise management to make business decisions, it does not fully remove the distorted incentives faced by supervising line ministries and provincial governments. The latter can want to encourage local SOCB brands to lend to the firms they partly own, whereas the former could be tempted to design sector regulations in a way that favors firms with state capital. Distorted credit allocation at the provincial level and inefficient market regulation at sector level can be more damaging to the economy than the micro-management of firms. Removing the exercise of state ownership rights out of line ministries and provincial government is necessary to address this potential conflict of interest.

The transformation of SOEs has resulted in an increase of unemployment due to the overstaffing of former SOEs. SOEs do not only have an economic function, but also a social function. They were used to generate employment. An empirical study conducted by World Bank shows that roughly 14\% of employment is overstaffed after SOEs are equitized. In order to fill in this unemployment, SMEs need to be strengthened, because SMEs create more jobs than any other enterprises.

6.2 Recommendations to Enhance the Competitiveness of Vietnam

As mentioned previously, there are some emerging issues of Vietnam’s competitiveness such as production resources shortage, out-dated technology, dominance of SOEs and their slow reform, and red-tape and corrupt administration. These issues impact negatively on productivity and competitiveness as well as sustainable economic growth in the long-term. At the same time, Vietnam cannot do everything at once to improve its competitiveness due to a limitation of resources and competence. Furthermore, national competitiveness is a large scope concept relating to many areas of an economy. In this study framework, we propose some solutions to solve some key issues, which are considered to be the most urgent\textsuperscript{106}, to enhance the competitiveness of Vietnam in coming years. They are namely: address production resources shortages; develop independent and vibrant private sector; and strengthen public institution and government effectiveness.

6.2.1 Address the Shortage and Quality of Production Resources

Although the fundamental structures in the economy have been changing, production resources have been a decisive determinant of the national competitiveness. As said previously, production resources\textsuperscript{107} in Vietnam remain short and low quality. In other words, the supply of inputs for the economy is insufficient in both quantity and quality such as lack of skilled labor, poor infrastructure (transport and electricity supply), and barrier of capital resources. Therefore, some measures are needed to fulfill production resources shortages in Vietnam in coming years.

6.2.1.1 Reform Higher Education and Develop Vocational Education

The quality and cost of human resources are the defining characteristic of competitiveness. Human resources must not only be efficient and asked but also innovative and dynamic to proactively meet the continuous changes required by an ever more competitive market place. The basic skills possessed by human resources need to be further channeled into more specialized areas so as to fulfill specific tasks which require technical skills\textsuperscript{108}. The competitive supply of certain products and services require properly trained human resources, and efforts at

\textsuperscript{106} The most urgent issues are based on our analysis and conducted survey
\textsuperscript{107} Production resources is defined as including human resources, infrastructure, capital and natural resources (see chapter 3)
\textsuperscript{108} Vietnam economy – Thoi Bao Kinh Te Vietnam (2006), “What need to be done to the integration of the higher education” VN Economy 12/05/2006 in Vietnamese
maintaining a top-class vocational and higher educational system are important components of the country’s competitiveness.

As said previously, in order to address the shortage of skilled labor force, we will propose some recommendations to raise higher and vocational education in this framework.

**Higher Education** to strengthen skilled labor force at present and to reach the long-term objective with 40 percent enrollment in higher education by 2020\(^{109}\), an appropriate balance of funding mechanisms, autonomy and accountability should be established.

At higher level of education, raising the quality and relevance of the teaching imparted involves both more private sector participation and increased autonomy of publicly-funded institutions. The new Vocational Training Law promotes offers at various levels oriented toward labor market needs and standardization of curricula. It also foresees an increased role of businesses in designing and implementing training offers. More systematic consultation should lead to an upgrade of the curriculum, teaching methods and training places, with the latter including actual workplace. One of the main constraints in this respect is overlap of responsibilities between MOET, MOLISA and other relevant bodies. The respective roles of the main stakeholders should be revised at all levels, from national government to provincial governments to local training centers.

The World Bank suggests that, on the funding side, partnership arrangements between businesses and higher education institutions should be encouraged. But they should not be seen as substitute for government resources, especially in areas related to research. Business sponsorships may lead to a neglecting of research and general knowledge, in favor of the technical skills more urgently needed by enterprises. However, support to research is one of the few tools for industrial policy available to Vietnam, as a latecomer of the WTO. The direct subsidies to industry used by other East Asia countries in their development drive are all but ruled out. Supporting laboratories, libraries and faculty working on basic knowledge would be a way to improve both quality of universities and Vietnam’s competitiveness. Grants should be provided through competitive mechanism and open to all higher education institution. A program could also be set up to encourage the return (permanent or temporary) of reputable academics and researchers from the overseas Vietnamese communities.

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\(^{109}\) This ratio is equal to that of Thailand at present
Delivering on the education agenda requires thorough rethinking of the overall financing frameworks for the sector. On the revenue side, the government strategy envisions an increased reliance on tuition fees but this has to go in parallel with the elimination of all other fees and out-of-pocket payments. For vocational training and higher education, the private sector should become an increasingly important source of funds. The government should encourage the private sector to participate in this area. However, to inhibit disadvantaged students from poor families’ subsidies to training facilities or student credit implementation\textsuperscript{110}, and/or a scholarship program should be considered.

Broader concerns are raised about the relevance of the education imparted. The credibility of the education system, hence social satisfaction with it, will depend on the match between education content and the economic development needs of Vietnam. There is a perception that the education system is functioning quite well but in the pursuit of backward goals. The survey we conducted showed that most respondents complained the education quality has not yet met the needs of the economy. Therefore, the quality debate should be related to the need for an approach to teaching and learning which is better suited to Vietnam’s transition to a market economy. Knowing how to learn problem solving, evaluation skills are necessary to deal with the uncertainties and continued changes brought by integration into the global economy.

\textit{Vocational Education} Vietnam has a huge labor force, but foreign companies still face problems finding skilled labor and competent managers\textsuperscript{111}. Vietnam must develop a master plan to expand vocational training schools to ensure a qualified labor force.

In several places, Vietnam needs to pay more attention to being devoted to vocational training with the objective of increasing the pool of skilled labor by which the national competitiveness of Vietnam will be enhanced. There is also recognition of the need for better educated and trained young people, especially in rural areas, to enable them to get jobs. Increased private participation is seen as part of the solution. The Vietnamese government should encourage the establishment of private education and training institutions; encourage more foreign companies to establish training facilities, especially those with a large number of employees; encourage training cooperation with high-quality foreign training institutions; and foster the opening of high quality, accredited and 100 percent foreign-invested

\begin{flushleft}
\textsuperscript{110} Banks should join in the education process through supplying preferable long-term loan for poor students, who their family cannot cover their study, but they have competence and want to graduate a university or college
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\textsuperscript{111} Kotaro Uchyama, General Director Staley Electricity Ltd in Vietnam
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training institutions in science, technology, techniques and economic management.

Although the government has carried the primary responsibility for vocational education, in a market economy vocational education policy design and delivery should be achieved through a new partnership between the government, employers, professional associations, industries, employees and their representatives, the local community and non-government organizations (NGOs). This partnership must create a coherent legislative framework to enable the launching of a national strategy for change. The government, apart from actually providing the vocational education, can also provide leadership and vision, facilitate, coordinate, establish quality assurance, and ensure that the vocational training is for all by identifying and addressing community service obligations.

The vocational training is best served by a diversity of public and private providers (including foreign investors). The appropriate mix can be found in many ways, with the responsibility of the government being to facilitate choice while ensuring quality. Both the government and private sector should recognize that the vocational training is an investment, not a cost, with significant returns, including the well-being of workers, enhanced national productivity, and competitiveness. Therefore, funding for vocational education should be shared to the maximum extent possible between the government, industry, and the community and learners, with government providing appropriate financial incentives. Moreover the government should seek or encourage the private sector to seek bilateral and multilateral capacity-building cooperation in vocational training.

6.2.1.2 Improve Transport Infrastructure and Strengthen Electricity Supply

As mentioned above, the infrastructure system in Vietnam, in general, is poor and inefficient. The infrastructure system needs to be improved. However, it would be difficult to improve all the infrastructure services simultaneously due to the limitation of resources and regulations. In this study framework, we propose some measures to strengthen the infrastructure services of transport and electricity which was considered to be the top priorities in our conducted survey.

Transport

Financing Transport expenditures reached 4.5% of the GDP in 2002. This expenditure should be increased substantially, which would correspond to the GDP growth. ODA currently finances 37% of the central transport expenditures. As in other sectors, the expectation that ODA financing will not grow at the same pace as GDP means that the growing sectors expenditure will need to be paid for either by consumers or the Government. To guarantee affordability of transport projects
and to supply relatively sufficiently in this area, the financing burden should be shifted to future generations through government borrowing and direct private investment. The private sector should play an expanded role in financing highways, railways, ports and airports.

Road maintenance should be strengthened. Current maintenance expenditures are at about 50% of the necessary levels. If expenditure on national road maintenance remains at their current levels over the next ten years, the condition of the network will be substantially deteriorated, with 34% of national roads being in poor condition, including 55% of the high traffic volume network (World Bank 2006a). Therefore, the Government should maintain a significant budget for maintenance and call for investments from the private and foreign sector.

Reform the Ministry of Transport’s State Owned Enterprises\textsuperscript{112} should be a central task to improve outcomes in the sector. Frequently the Ministry’s SOEs are over-indebted and deliver low quality and delayed work. Therefore, an equitization program should be designed to close non-viable enterprises, to establish clear lines of accountability and improve commercial incentives for the remaining enterprises, and to provide clear separation between Ministry finances and enterprise finances. A further possibility would be to remove ownership of shares in the SOEs to a separate agency, to ensure no conflict of interest between the Ministry of Transport’s policy role and the profit motives of share ownership.

Competition in transport infrastructure service should be introduced gradually. Competition is the most powerful mechanism for improving efficiency. Competition provides firms with incentives to keep costs at a minimum, to offer products that are better adapted to the needs of consumers, and to adapt new technologies as they become available. Competition in the transport infrastructure is used to procure road construction, but the competition is between state-owned companies who use the same norms to prepare their bids, and typically prepare similarly priced bids. This suggests either collusion in their bids or that a greater number of competitors are required to produce vigorous competition.

Electricity

The capacity of Vietnam’s electricity system needs to double in just five years, to meet demand growth projected at 16% per year during 2006-2010. While demand-side management must be pushed as hard as possible, the main solution lies

\textsuperscript{112} In the area of infrastructure, increasing investment is indeed one of the top priorities, and evidence from OECD as well as non-OECD countries suggest that privatization has led to substantial increases in investment (OECD, 2000 Privatization, Competition and Regulations, p25-30)
in a large-scale medium-term capacity expansion program. Annual power sector investment requirements during 2005-2010 are expected to cost over US$3 billion per year. The three main financing options for the sector are self-financing by EVN using retained earnings, using different types of borrowing, and independent power producers (IPPs). EVN cannot even come close to meeting this requirement from its own resources or massive borrowings, especially without further increases in unit sales revenue. EVN has maintained profitability each year since its inception in 1995, and has retained a sound financial position. However, the size of the sector investment requirement is no match for the company’s borrowing capacity. In addition, the Government is neither willing nor able to pick up the bill (World Bank 2006a, pp. 32). Therefore, IPPs investment needs to be encouraged. One way or another, directly or indirectly, consumers need to pay the cost of the power system expansion. The task of the Government and power industry is to implement the expansion program as efficiently as possible, to keep the costs as reasonable and affordable as possible for consumers, and stimulate private investments.

The government should diversify electricity supply sources and encourage the establishment of new IPPs from foreign or domestic private firms to meet the huge and rapid increases in power demand. IPP arrangements for new power plants include: BOT ventures wholly owned by other public-owned Vietnamese entities; joint-ventures BOT arrangements, involving EVN investment with other parties (local public or foreign); and BOT arrangements wholly owned by parties, either public or private. In addition, new joint-stock company IPPs are being created from EVN’s partial divestiture of existing power plants under its equitization program. This aggressive IPP development runs in parallel with the Government’s efforts to gradually restructure the power industry, as dictated in the new Electricity Law. In general, the Government should seek to pursue all types of IPPs, as quickly as possible, in its efforts to get new plants on the system. In addition, the price of electricity should be maintained at a reasonable level, which recovers costs and earns profits, to stimulate further private investment in the period of recent power shortage.

In the electricity sector, the reform of state-owned enterprises is to focus on the transition to a future competitive market for electricity. EVN will need to be broken up into truly separate corporations. Decisions on size, structure and operational scope of newly formed shareholding companies need to ensure adequate

113 In China in the late 1980s and early 1990s, the willingness of large consumers to pay higher “second track” prices or make other types of contributions for new power plant investments, in exchange for guaranteed power in time of shortage, was the most important single factor in overcoming national power shortages. (World Bank 2006a)
competition in different market segments as well as adequate resources to ensure financial viability, but should not wield excessive control over the market. As the sector and market structure changes, distribution companies will be drivers in attracting new generation investments and hence protecting end consumers via reliable supply. Distribution companies, in particular, need to have sufficient financial strength and managerial capacity to be perceived as credible and make long-term contracts with generating companies.

The World Bank strongly recommends that competition be used wherever possible in awarding IPP power purchase agreements (Ibid., pp. 36). Through competitive bidding, supply price will be lower than negotiated one. As in Vietnam, power utilities, public officials, and especially potential power providers often argue that there is insufficient time to proceed with competitive bidding. Often, however, this is due to lack of planning and/or lack of proper incentives to minimize costs. Vietnam’s power consumers will be the ones to suffer from higher than justifiable costs, unless competitive bidding is strongly favored over negotiated contracting. In cases where negotiated contracts proceed, clear and transparent information should be provided to the public about costs and contract details. If power providers are public entities, detailed and accurate reporting of all aspects of equipment contracting, construction contracting, and power plant operation affecting costs should be openly reported to all relevant government agencies, and made public where possible.

6.2.1.3 Develop Financial Market and Reform Banking System

The government should move forward with concrete actions to open the financial sector further and increase foreign competition. A key milestone in the process was the submission of the Law on the State Bank of Vietnam and the revised Law on Credit Institution to the National Assembly in 2007 that will be passed in 2008. These two Laws should provide a new regulatory environment for the operation of commercial banks and transform SBV into a modern Central Bank for a market economy. The state owned commercial banks114 (SOCBs) should be equitized. The equitization of Bank for Foreign Trade of Vietnam (Vietcombank) and Mekong Housing Bank was scheduled to be completed in 2007, also when the equitization of the Bank for Investment and Development of Vietnam (BIDV), and Industrial and Commercial Bank of Vietnam (Incombank) is said to start. The Viet-

114 Vietnam has 5 large state own commercial banks, accounting 65% of total credit of the economy, including Bank for Foreign Trade of Vietnam (Vietcombank), Bank for Investment and Development of Vietnam (BIDV), Industrial and Commercial Bank of Vietnam (Incombank), Vietnam Bank for Agriculture and Rural Development (VBARD) and Mekong Housing Bank
The government needs to focus on cleaning up and restructuring the SOCBs' balance sheet, and enhancing the adequacy of their capital. There is a little doubt whether most of these banks will succeed in attracting private capital. However, a disperse ownership may not fundamentally change the way they are run. Allowing foreign investors to hold a larger share of capital and, especially avoiding the sale of shares in small packages, would help in attracting international banks with a sufficient scale and managerial expertise.

Other solutions could help to improve the quality of credit and facilitate the recovery of NPLs. The implementation of current plans to develop a private credit bureau and to bolster the SBV Credit Information Center could be continued. The system of registration of mortgage over land-using right certificates (LUCs), to be managed by MONRE at province and district levels, needs to be upgraded.

In fact, the transformation of SBV will require a revision of its structure, and in particular of its organization by provincial branches. Regrouping those branches by regions could help introduce an arms-length relationship with provincial People's Committees (PPCs) and the provincial branches of SOCBs, thus undermining the cozy relationship that there is at present between borrowers, lenders and supervisors. Upgrading the supervision capacity of SBV is another important priority. At presents, this capacity suffers from the duplication and overlapping of functions between departments at headquarters and provincial levels. These respective roles of SBV and other government bodies such as MOF and Deposit Insurance Agency in relation to supervision should also be clarified. Which
agency will exercise the state ownership rights in SOCBs, once this function is taken away from SBV, is also unclear.

Equally important, the transformation of SBV will require the strengthening of its capacity to run monetary policy. The increased financial depth of the Vietnamese economy and its growing openness to international capital flows, call for a better understanding of the relationship between external shocks, policy instruments and macroeconomic outcomes. For example, a major stock market correction was almost irrelevant a few years ago, but it could become a major source of instability today. Admittedly, other ongoing trends could actually strengthen financial stability. If the government were to move more fully to non-cash payments there would be greater predictability of the volume of deposits. If the economy was to become less “dollarized”, the ability of money demand trends could be enhanced as well. But even in the presence of these trends, the conduct of monetary policy in an open economy will be challenging. Upgrading the human resources of SBV and supporting the development of its in-house expertise should be priorities for technical assistance over the next five years.

The new law on securities could do much for development of capital markets. The law strengthens the authority of state stock company (SSC) over all public offerings. Securities and publicly held companies brokers and intermediaries dealing in securities will need to be licensed by the SSC, which will able to regulate issuers, intermediaries and investors in the over-the-counter market. The law also provides the legal basis for the establishment of the Vietnam Securities Depository, which is expected to become a privately owned entity. However, to make the most of this new law it will be necessary to upgrade the systems supporting trading at stock exchanges, the central securities depository, and information management by SSC. Such an upgrade would involve the introduction of registration systems for securities and individual brokers.

The equitization process should also be more tightly linked to the development of the capital market, with a clear requirement for SOEs to meet the standard that applies to publicly held companies. The equitization of the exchanges should be also considered, as a way to separate the ownership of the markets from their supervision. Consideration should also be given to the establishment of an investor protection fund, as an incentive for investors to trade through regulated brokers. The development of contractual savings policies to expedite the formation and growth of private sector pension funds would generate new demand for securities and the regulations for institutional investors. In terms of the bond market, the government could create a debt management policy that aims to build sizable and predictable debt issuances and an integrated primary market.
The government should provide the issuance of benchmark bonds for the development of the government bond market. The corporate bond market should capitalize on the availability of benchmarks, which should allow banks and enterprises to control the maturity and currency mismatches. This in turn could contribute to reducing NPLs, by helping reduce systemic rollover of short-term loans to infrastructure enterprises. Securitization needs to be made possible in order to provide new means to finance infrastructure projects, SMEs and housing development.

6.2.2 Develop an Independent and Vibrant Domestic Private Sector

The competitiveness of the Vietnamese economy would have a greater achievement if it were supported by a robust private sector, and reform of the inefficient SOE sector and banking system. The reforms and the restructuring of SOEs have meant that there are many entrepreneurial opportunities available to private firms, especially SMEs. The key task for Vietnam is to provide promotion and to create a fair competitive business environment for development of the private sector, which is considered a dynamic force for the competitiveness of the economy. In this section, we propose some recommendations to enhance the reforming of SOEs and to promote the development of private enterprises, especially SMEs, by which domestic private sector is bolstered, and become more independent and vibrant.

6.2.2.1 Strengthen State-Owned Enterprise Reform

As analyzed in the previous sections, SOEs equitilization process has been slow in recent years and there still exist a large number of SOEs in almost all industries of the economy. While both theoretical and empirical studies show that privatization (equitization) of SOEs has brought more efficiency of enterprise operation and its economy, the survey of 550 equitized SOEs conducted in 2005 by World Bank indicates that the diversification of ownership has also contributed to increased efficiency at the enterprise level, by which the national productivity and competitiveness have been increasing. Almost 90 percent of those firms reported an improvement. Turnover has increased by 13 percent on average and on pre-tax profits by 9 percent, which is considerably more than among non-equitized SOEs. Investments and salaries have increased as well. The study also suggests that performance improved faster when the reduction in the state share of capital was larger. This sign shows that it is time for Vietnam to speed up equitization of SOEs.

This improvement is not due to a change in the management team of equitized SOEs. In more than 80 percent of the cases, the chairman of the Managing Board, the director, the deputy directors and the chief accountant remained in their jobs. More importantly, there is a clear concentration of power. It appears that the real
change is in the motivation and autonomy of the management team. More than 96 percent of the respondents stated that their managers paid more attention to performance, and enjoyed a higher autonomy to pursue profit objectives (World Bank 2006c).

### Box 3 A number of privatization methods (OECD 2000)

<table>
<thead>
<tr>
<th>Method</th>
<th>Description</th>
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<tbody>
<tr>
<td><strong>Initial public offerings (IPO)</strong></td>
<td>An open competitive procedure that allows for share pricing and company valuations by market. Building competition in offering process itself is important. IPO are highly transparent methods of sale, but to be effective, however it requires a development of capital market, legal framework and large privatization candidates.</td>
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<tr>
<td><strong>Trade sales to strategic investors</strong></td>
<td>Especially vulnerable to competition failures. The state is often tempted to sell its controlling stakes to local interests with negative results on the competitiveness of industry, especially the case of the sensitive sector (i.e utilities). The main benefits that trade sales bring are the introduction of considerable managerial and technical know-how and a stable investment environment for economically important firms or sectors. The latter is especially crucial for countries where capital markets are shallow.</td>
</tr>
<tr>
<td><strong>Management or employee buy-out</strong></td>
<td>The acquisition of a company by the existing management. It is frequently used as a means of divestment by companies seeking to focus their core activities. The new owner-managers of the buy-out frequently improve its performance as they usually are well aware of any remedial action required and have serious incentive in the form of their stake. Additional capital is provided by financial institutions and venture capitalist and also in many cases by allowing other employees to join in so-called employee buy-outs.</td>
</tr>
<tr>
<td><strong>Liquidation</strong></td>
<td>The distribution of a company’s assets among its creditors and members prior to its dissolution. This brings the life of the company to an end. The liquidation may be voluntary or compulsory.</td>
</tr>
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</table>

The reduction in SOEs has been mainly through equitization, whereby the SOE after a sale of shares is converted to a joint stock company (JSC) that operates under the Enterprise Law rather than the SOE Law. Other forms of SOE transformation have been mergers, conversions to limited liability companies, and outright sales liquidation. Therefore, in this study framework, we focus on how to speed up the equitization process of SOEs because empirical evidence shows that the equitization of SOEs is best method than any other ways in the current context of Vietnam. Initially, the focus of equitization had been on smaller SOEs, but since 2004 the average size of SOE transformations has been rising. The equ-

115 Dictionary of Business and Management, Oxford University Press 2006, p327
116 Dictionary of Business and Management, Oxford University Press 2006, p 315
uitization process itself has undergone major improvements, with appraisals being conducted by outside evaluators and the sale of shares taking place at market price, via auctions at the Securities Trading Centers.

The restructuring of SOEs should maintain a priority over the next five years but it should involve increasingly large SOEs and lead to divestiture of a larger share of their capital. And it ultimately aims to create companies (both private and state) which can compete domestically and internationally. The Government should make efforts to steadily speed up the reorganization and renovation of state enterprises by diversifying the ownership to improve efficiency and competitiveness and to expand the scope of equitization of state enterprise. In addition, the Government needs to put pressure on SOEs to force them to be IPO under the road map. The World Bank suggests that the State should only hold controlling shares in corporations and joint stock companies (JSCs) in the most important fields or sectors which play key roles in the economy such as petroleum, telecommunication, fertilizer, and so on. The State also should hold 100 percent shares of non-equitizable businesses in the fields of national defence, securities, and pure public service provision. The suggestions are in line with economic theory, that stresses that the state should for efficiency reasons, concentrate on the provision of public goods and let private actors be responsible for other products and industries.

The auction mechanism has been implemented to equitize SOEs, accelerate equitization pursuant to market principles, and SOEs equitization must parallel the public offering and listing in the stock market. There is a focus on equitizing large-scale businesses, entire corporations and attracting more capital through their valuation in the stock exchange. The Government should also be required to completely dispose of loss-making state enterprises in a suitable way and to reclaim land and water surface of no or limited use from institutions, organizations or SOEs or provide it to other investors.

The successful equitization process of SOEs requires the development of financial market and competition conditions. The development of a financial market (stock exchange) encourages SOEs to equitize their companies. In order to develop a financial market, Vietnam should prioritize to reform its banking system and set up a regulatory framework of stock market operation (see the previous section).

117 No permission of joining of private sector
118 Which private sector does not want to do or do inefficiently
The holding company model is to be used for large-scale corporations which can not be equitized as a whole. In their case, the chosen approach is to equitize their member businesses and transform the remaining ones into the Single-member (state) or limited companies of several state members; at the same time, transforming those corporations into the form of group companies held by a holding company. The management board is reorganized to represent the ownership in the corporation.

The State needs to separate its management functions from owners’ management and from business administration functions. The key to accomplish this separation in practice is to gradually narrow and eliminate the function of representatives of line ministries, agencies and provincial city people’s committees in the governance and management board of state enterprises. In most cases, the exercise of state ownership rights is to be transferred from line ministries, agencies and provincial governments to the recently created State Capital Investment Corporation (SCIC), a holding company under MOF with a mandate to allocate state capital so as to maximize its returns. Such transfers should increase the incentives to allocate resources or reliable information on the performance of the enterprises in its portfolio. In practice, larger enterprises will need to be listed and smaller ones fully divested or disbanded, so as keep the size of the portfolio manageable.

Some of the most difficult challenges ahead are related to the exercise of enterprise ownership rights on behalf of the government. The current strategy foresees the transfer of the state share of capital from line ministries and province to SCIC. But there seems to be less clarified in relation to the state share of capital in General Corporations 90/91. If that share is to remain out of SCIC, other mechanisms will be needed to strengthen their corporation and increase transparency of their operations. Similarly, the experience of the economic groups reporting directly to the Prime Minister will have to be closely monitored and evaluated, so as to develop an appreciate regulatory framework over time.

Effectively running the SCIC for a profit will be technically demanding. Reallocating state capital to the most dynamic enterprises while fully divesting from the worst performers (and possibly liquidating some of them) should increase economic efficiency. But it requires knowing who the good performers really are. Share prices in stock market can help in this respect. One of the priorities of the SCIC should thus be the preparation of large companies for listing. However, for many smaller enterprises this will not be an option thus other performance assessment mechanisms will be needed.

119 General Corporations 90/91 were established by the Prime Minister under Decision No 90 and 91 in 1990 and 1991.
6.2.2.2 Promote Development of the Private Sector

In written responses to questions submitted by the Wall Street Journal, September 26th 2007 the Vietnamese PM said:

“The Vietnamese government is now trying to reduce its role in directing the country’s economy and bolster that of the private sector in driving the country forward. The private sector is an important part of the economy, and the government is paying particular attention to how to facilitate private businesses”.

Developing a multi-stakeholder economy, one that allows space for the private sector to prosper, requires a level playing field for all enterprises regardless of their ownership. In this respect, the Vietnamese government should issue several policies that encourage the development of the private sector. Vietnam should make the role clear as a driving force of the private sector and create favorable conditions for the development and investment of the private sector without limiting their scale, field and region. The government should eliminate all forms of discrimination, praise good producers and entrepreneurs, and encourage the development of large private enterprises, private economic groups and, enterprises owned by women. This recommendation is to minimize the scope of state monopoly and eliminate business privilege.

Vietnam needs to implement a series of reforms aimed at creating a more conducive business environment. They range from the introduction of new legal frameworks to the simplification of administrative procedures. Urgently the government has to issue the rules and regulations to implement the Unified Enterprise Law and the Common Investment Law (MPI). The Vietnamese government should encourage firms in developing e-commerce, using the internet to search market information advertisement and business opportunities, and continue improving supportive environment to provide favorable conditions for enterprises of different types to develop; focus on a streamlining of administrative procedures, time and cost for all domestic and foreign investors to participate in Vietnamese market; remove limitations of investment and labor scales; remove discrimination in terms of access to opportunities, resources and market information.

As previously mentioned, a major constraint facing private enterprises, especially private SMEs in Vietnam is a shortage of funds. Private SMEs lack access to long-term loans, an equity financing system and access to collateral. The strict collateral requirement by banks and the low incentives for SOCBs to lend to

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120 Some signs of discrimination and unfair treatment that discourage these economic sectors from investing their capital in business and production development
SMEs, and on the other hand the unwillingness of private SMEs to deal with SOCBs, are serious restrictions. This generates a vicious cycle that prevents many SMEs from entering the formal credit sector, and forces them to rely on informal credit. Thus, local governments should establish credit guarantee companies to support SMEs’ access to finance. Financial policies have an important impact on capital mobilization and development of enterprises. Vietnam’s banking system reform aims to address the shortages and problems of availability of credit and capital for the economy. However, the impact of these reforms on the domestic private sector will continue to remain limited if the private sector continues to experience difficulties in securing access to land use rights, their potentially most valuable source of collateral. In this respect, Vietnam should also abolish limitations on capital contributions and mobilizations of foreign-invested enterprises and institutionalize the mechanism that allows foreign investors to use as collateral their property, including land and values of land-used rights in accessing loans from credit institutions who are permitted to operate in Vietnam.

The competition law and associated policies should be implemented consistently, to avoid situations of privilege or excessive market power. Similarly, the strategy to create major corporate groups around General Corporations under the PM should not inadvertently create an anti-competitive business environment. The possible combination of multiple commercial and financial interests under the SCIC could also facilitate practices compromising the objective of sound corporate governance, such as transfer pricing and affiliate party transactions.

Through business associations121, the voice of the business sector should be strengthened. These organizations effectively represent and communicate the interests of the business community to authorities, as an input of policy making. Channels of policy dialogue between government and representatives of the business community should also be strengthened and formalized, so as to benefit from the direct knowledge and perspective of enterprises and to communicate policy orientations more clearly. However, in promoting the role of business associations must also be exercised not to allow them to become an anti-competitive industry Cartel. In addition to playing the role of a lobbying body, the business associations can be a standard setter for business practices and ethics for their industry. This useful function could turn into being a hurdle for potential new entrants if not properly watched from the perspective of competition policy.

121 In many countries business associations are playing a crucial role on identifying and advocating the needs and demands of the business community and relevant authorities (Harvie 2003, pp. 199)
The image of the private sector has to be improved in the country. The vital role of private companies for employment generation and modernization of Vietnam should be acknowledged and disseminated through the media and the educational system at all levels. Given the many years of discrimination against private enterprises and private entrepreneurs, stronger and more frequent endorsement of private business by the Vietnamese leadership is required as was the case in China. Regular public exhortations by top leaders of the Party and Government to the bureaucracy to provide support to the private sector under the laws would be extremely helpful. Stories in the media of domestic private business successes and visits by top leaders to successful private exporters would help to reinforce the value of private business in Vietnam’s development. The Government should continue to praise successful young private entrepreneurs through awards and public media, by which the image of private businesses is improved and younger Vietnamese generations are encouraged to do business.

6.2.3 Strengthen Public Institution and Government Effectiveness

The pervasive corruption at all levels of government shows the weak public institution and inefficient governance. It reflects the lack and weakness of law system frameworks and its enforcement as well as a red-tape and cumbersome administration. This results in a less attractive business environment in Vietnam and deters domestic and foreign investors. In order to create a better business climate and improve competitiveness, some measures are proposed to fight corruption and strengthen public institution and governance.

6.2.3.1 Launch a Strong and Effective Anti-Corruption Campaign

Despite much talk, often involving grand principles, corruption is an under-researched topic in Vietnam. Country-specific information and data is still limited and scattered, whereas cross-country indicator are not reliable enough. Deterring of corruption is a top priority because corruption represents a serious threat to development progress. It raises the cost of doing business and undermines the confidence of domestic and foreign investors, thus slowing economic growth and job creation. It drains the capacity of government and deprives vulnerable people of the right to basic services. Importantly, it compromises social values and norms and undermines public confidences in the institutions. But corruption cannot be eliminated overnight. International experiences suggest that there is no quick-fix recipe, and constant and concerted efforts are needed for lasting and sustainable impacts to be achieved (World Bank 2007a).

While far from being perfect, the legal framework to combat corruption is indeed being put in place. The capacity of government agencies to detect and investigate
corruption does not seem to be a major limiting factor. However, it is unlikely that the passing of laws and a more active investigative stance will suffice. A combination of powerful forces makes it difficult to achieve a “critical mass” in the fight against corruption. With rapid growth creating temporary rents and leading to dramatic changes in the prices of assets such as land, the opportunities for unlawful gains are widespread. Meanwhile, the collective nature of corruption protects those engaged in wrongdoing. In these circumstances, it is almost impossible for any government agency to cover all fronts. Stakeholders outside government, including the media, civil society organizations and the public at large, have to be engaged.

The role and responsibility of the society in anti-corruption, such as social-political organizations, mass media, enterprises and industrial associations must be strengthened. The media has recently been encouraged by government to write more proactively about corruption and to publicize corruption cases as reported by the police and government agencies. The purpose is to raise awareness about the necessity of fighting corruption, to publicize laws and regulations, to help mobilize public support and hopefully convince potential perpetrators that the risks of detection and severe sanctions are becoming dissuasive enough. In doing so, the media has increasingly assumed a supervisory role over the administration. Journalists should be encouraged further to detect corruption cases on their own and they have indeed done so in a number of highly visible cases. But there is still a tension between policy and reality, due to lack of clarity on where the lines are drawn and fines applied to investigative work. Thus, the adoption of a more determined stance in the fight against corruption and the passing law on Anti-corruption may have encouraged the media to address the issue more openly. The number of articles dealing with corruption has increased by roughly 60 percent between 2005 and 2006, for both types of media, regardless of definition used.

The mechanism to conduct asset declaration of managers, civil servants in administration agencies and organizations, and to monitor the assets of civil servants, introduced by the Law on Anti-Corruption, needs to be implemented urgently. Success in this area will depend on the design of the mechanism. For example, it is clear that monitoring the assets of civil servants in Vietnam is beyond the capacity of any agency. Thus, there is a need to be selective, focusing on positions of responsibility. Also, the diagnostic study on corruption and the CCIA survey both indicate that some agencies are more exposed to corruption than others. Priority should be given to the monitoring of assets of civil servants in such agencies as Tax, Customs, Land, Construction, and Police.

122 These agencies are considered to be the most corrupted following the diagnostic study of the CCIA
The responsibilities of heads of agencies in the fight against corruption should be clarified. Their aim is to prevent cases of bureaucracy, harassment and the abuse of power affecting citizens or enterprises. Heads of agencies should be instructed to establish all effective monitoring mechanism in relation to these problems and to introduce hotlines and other entry points to gather comments and complaints.

E-government needs to be implemented to increase efficiency, to boost transparency and to reduce corruption. IT centers have been established in almost all government organizations and much has been done in terms of equipment. Several provinces are setting up their own e-government interfaces. However, business process reengineering has not been given enough emphasis. Introducing IT systems such as e-businesses and citizens, in order to reduce clearance times, minimizes fraud and reduces the scope for abuse. Fragmentation and quality are issues of concern, partly due to the dispersed nature of IT development, which is being conducted by ministries and provinces with limited coordination.

The competence of officials at both local and government levels should be improved and trained. The clearest message from the survey is that business people are concerned about the corruption and lack of professionalism of officials. To effectively tackle corruption, the government needs to make rigorous efforts in recruiting highly motivated and talented people, especially for crucial positions to the quality of business environment. In addition, a practical step forward would be to modernize the curriculum of the government and party schools at both central and local levels (Vu 2003). China and Singapore have successfully designed curricula that effectively enhance the competence and commitment of government officials and staff, who go through mid-career training programs in these schools. The main focus of their training is on economic development strategy, policy analysis, and teamwork.

Reporting by the media is a potentially effective deterrent of corruption. A more active media is bound to lead to increased reporting on corruption. Therefore, reliable mechanisms to collect feedback from citizens and enterprises are needed. Updating the diagnostic study on corruption, and conducting further research on more detained aspects of it, would certainly help. On a more regular basis, a technical agency like GSO should be entrusted to regularly gather the view of households and firms on their experience with corruption in various government agencies.

123 Including local and government officials
6.2.3.2 Strengthen Public Administration Reform

The government should continue to strongly implement an administration reform program. There is a clear continuity in the government strategy for public administration reform, with the year 2006 simply marking the beginning of the second phase of the PAR Master Program 2001-2010. Functional reorganization, aimed at focusing the government on a stewardship role, remains the core of the strategy. The scope and content of the state’s economic management should be defined more clearly; adjust the functions of the government so that the government, ministries and central branches can concentrate on policy-making and exercise the monitoring and supervision of the implementation of state, plans, policies and legislation.

Focusing government activities on policy making has implication both on decentralization and on the direct provision of services by units with budget funding. In the former, regulations on central-local decentralization and decentralization among different levels of local authorities improve their powers and responsibilities, clearly defining the tasks for which local authorities should have full decision-making power, those that have been wholly decided by the central authorities. As for the latter, state administrative management needs to be separated clearly from management of public services.

Discussing about functional reorganization focuses on simplifying the structure of ministries (and departments at a local level). At present, there are twenty two ministries and they should be reduced further. On the other hand, there is a clear need for better policy coordination across ministries. The OOG (Office of Government) can only partially fulfill the coordination role, as its functions are to a large extent administration. The creation of an empowered technical body above current ministries, which coordinate in making policies among ministries, especially between the Ministry of Finance, State Bank of Vietnam and Ministry of Plan and Investment, could be considered.

In order to simplify administrative procedures, several proposals need to be implemented such as: the widening of the one-door model to different levels of government; decentralizing authority to the lowest level possible together with closing inspection and checking by superiors; preventing the trend of being too bureaucratic in public organizations; continuing to eliminate currently unnecessary business licenses and business conditions to facilitate for all investors.

In addition, it will also be necessary to introduce immediately common standards for IT application and e-government interfaces. The ability of IT systems across government to dialogue with each other will be essential to move in the direction of a single identification number for enterprises and a single social insurance
number for individuals. ISO standards in quality management of administrative agencies and procedures should be adopted widely at all levels of government

Strengthening employment and pay policies remain a priority. The objective of the salary and wage policy in the upcoming time is to go against subsidy and privileges, eliminating egalitarianism; implement the principle of distribution on the basis of labor and outcome of production activity of each organization and business; separate salary and wage policy for administrative cadres and civil servants and public employees working in public service delivery organizations based on financial autonomy; and make sure publicity and transparency in income, controlling and legalizing salary-nature earnings so that salary will become the major source of income. An appropriate wage policy will contribute to the improvement of effective governance and reduce the pervasive corruption in Vietnam.

6.2.3.3 Improve Framework and Enforcement of Legal System

The commitment to build a transparent society under the rule of law has been implemented since the last amendment to the constitution in 2001. Therefore, four priorities have been emphasized to reach this objective (The SEDP 2001-2010). The first one is to reform the law-making process, by facilitating greater participation by citizens, enhancing the representative role of legislative bodies, and improving the skills of legal draftsmen. Second is to ensure the constitutional and legal norms, by monitoring administrative regulations and reducing the number of forms of legal documents. The third priority is to strengthen judicial reviews, building independent administrative tribunals to help ensure the citizens’ rights to complain. And fourth is to empower district courts with increasing jurisprudence over civil and criminal cases gradually building a system of high courts for appeal and other specialized courts, on intellectual property issues, for instance.

The SEDP emphasizes the social dimensions of legal and judicial reform. Accordingly, Vietnam needs to reform the methodology and process of developing legislations and issuing regulations to ensure effective participation of the people in the development of legislations, effectively organizing the collection of people’s comments before the issuance of legal normative documents, specifying that legal normative documents are to be made in mass media. Another objective is to protect people’s assets; eliminate unsuitable and unnecessary legal regulations related to business community, citizens’ living and working, confiscation or temporary seizure of citizens’ property; competent authorities must compensate in money and kind to those people who have suffered from wrongful rules against the Law. Access to justice receives a special attention. Legal consultation service should be extended to the people, especially the poor, ethnic minority people living in re-
mote and isolated areas. And there is explicit reference to the need to encourage social organizations, mass organizations and civil societies to engage in managing and monitoring some public fields.

Improving the process for formulating laws requires ensuring that policy debate precedes the actual writing of normative documents. It also requires the expansion and strengthening of standing technical committees and professionalizing the drafting process. A revision of the Law on Laws could support a more logical sequencing of policy formulation and drafting process. But practice could also change within the existing legal frameworks, as shown by the open and participatory process adopted by the National Assembly. Regardless of whether the Law on Laws is revised, the system of law promulgation needs to be refined to ensure uniformity between legal normative documents.

The judiciary system should be reorganized and needs to be strengthened to become more independent and effective. To gain these objectives, the judiciary system needs to be separated gradually from the existing administrative structure; the jurisprudence of district courts needs to be expanded; appeal courts and specialized courts needs to be established; and judicial support services (such as lawyers, judicial police, notary and other paralegal services) need to be upgraded.

An adequate framework should be provided for civil society organizations and their involvement in service delivery, as well as grassroots democracy. On the judiciary front, improving the quality of court decisions requires the creation of entry points to resolve complex legal issues, either through specialized judges appointed to help tribunals make decisions promptly or through key legal sector specialists who would provide the relevant information. Further professionalizing judges, especially those working at province and district levels, and upgrading their skills, are necessary for the public image of justice. The scope for the creation of specialized courts should be explored as well. Modernizing the administration of the courts could be necessary to promote their efficiency and ensure the independence of judges. Budget allocations for courts should be decided directly by the National Assembly and People’s Councils, rather than by higher courts. In the long term, it would be necessary to re-examine and clarify the functions of the procuracy, which currently has both prosecutorial functions and the function of controlling the judiciary. Ultimately, the procuracy should be transformed into an institution in charge of public prosecution.

Publishing the decisions of the courts is essential to develop the capacity of the judiciary system to interpret the Law and ensure its enforcement. It would also improve the quality of the decision making process by the courts, and thus raise
the credibility of courts in society. Allowing greater access by the media to court proceeding could be another way to promote transparency.

Ensuring access to justice, especially for the poor, could be partly accomplished through strengthening the legal and administrative means of defense attorneys. The funding and capacity of the legal aid system should be enhanced. Access to legal support should be simplified for marginalized and vulnerable groups, allowing NGOs to participate in this area.

In brief, Vietnam cannot do everything in order to enhance its national competitiveness at the same time. The top priorities need to be done are following as:

The first priority is to address the shortage of production resources supply (skilled labor, transport infrastructure and electricity supply). The Vietnamese government needs to reform higher education and develop vocational training, improve transport infrastructure and electricity supply, and develop financial market and reform the banking system.

The second priority is to develop an independent and vibrant domestic private sector. The Vietnamese government needs to strengthen state owned enterprise reform and promote development of the private sector, especially small medium sized enterprises (SMEs).

The last one is to strengthen public institution and government effectiveness. The Vietnamese government needs to launch a strong and effective anti-corruption campaign, strengthen public administration reform, and improve framework and enforcement of the legal system.