**Viewpoints**

The Ministry of Planning and Investment in Vietnam is preparing the national SME development policy 2006-2010, as part of the country’s five-year economic development plan. Based on these policies, the Agency for SME Development will design an action plan for SME promotion.

This bulletin looks at some key aspects of private sector growth, and makes some recommendations on how to develop larger and more robust private firms.

**PRIVATE SECTOR FIRMS:**

**Size matters**

The private sector has increasingly been recognized as a critical engine of economic growth in Vietnam. The Ministry of Planning and Investment (MPI) is now preparing the national SME development policy 2006-2010, as part of the country’s five-year economic development plan. Based on these policies, the Agency for SME Development will design an action plan for SME promotion.

This bulletin looks at some key aspects of private sector growth, and makes some recommendations on how to develop larger and more robust private firms.

- Simplified procedures have contributed to an increased number of registered firms
- The Enterprise Law of 1999 established the principle that firms may do business in all sectors and areas that are not prohibited, and replaced the former licensing process with business registration. The expense and time needed to establish a business have been reduced significantly. As a result, thousands of new enterprises have been registered since the Enterprise Law took effect. According to data from the National Business Information Center (NBIC), which manages the national database on company registration, for the past four years the number of enterprises registered has doubled the number registered in the years prior to the Enterprise Law. By bringing the total number of registered enterprises in Vietnam to around 125,000.

But the number of firms in actual operation is lower.

Data from the General Statistics Office (GSO) shows that there were 62,908 enterprises in operation by end of 2002, and roughly 72,012 by the end of 2003. This is understandable since firms are not measured directly by the number of enterprises. There are millions of firms, and the corporate sector as a whole reacts to changes in the external environment (such as new market opportunities and business conditions). Therefore, the number of firms is not a good indicator of firm activity. The dynamic process that occurs when firms are formed and they grow is not measured directly by the number of enterprises. The corporate sector as a whole reacts to changes in the external environment (such as new market opportunities and business conditions).

- Improvements in the corporate tax system. The current tax calculation and administration system, including VAT invoice controls, are a major constraint on companies that want to do business in a more transparent manner. As a result, companies and their suppliers need support to grow firm size.

---

(1) Business Information Center Vietnamese Chamber of Commerce and Industry
(2) Vietnam Economic Review, October 2003
(3) Federal Reserve Bank of Chicago, Economic Perspectives, January 2004
(4) World Bank, Vietnam, Business Information Center, Vietnamese Chamber of Commerce and Industry
(5) World Bank, Vietnam, Business Information Center, Vietnamese Chamber of Commerce and Industry
(6) World Bank, Vietnam, Business Information Center, Vietnamese Chamber of Commerce and Industry
(7) World Bank, Vietnam, Business Information Center, Vietnamese Chamber of Commerce and Industry
Simplified procedures have contributed to an increased number of registered firms, but the actual number of firms in operation is not as high.

- Since the Enterprise Law became effective in 2000, in Ho Chi Minh City, the number of businesses established has remarkably increased. To date, more than 50,000 enterprises have been registered, accounting for one third of all formally-registered enterprises in the whole country. While growing at a significant rate, it is widely understood that in a pond of thousands of fish, it is natural that some may die right away and others may grow up very fast. The Enterprise Law has eased the business registration process - an entrepreneur can easily register a new business without any evidence of activity, having it capitalized and operational. However, a post-registration monitoring scheme needs to be set up to maintain a database of enterprise information, and effectively support firms in their operations. Most newly established firms need to struggle by themselves in running their businesses, without much support or assistance from the government (except for regular interaction with tax agencies). The "disappearance rate" (firms closing without completing the formal exit procedures) in Vietnam is quite high, due to the absence of a post-registration monitoring system.

Mr. Truong Ngoc Nghia, Vice President of Investment and Trade Promotion Centre of Ho Chi Minh City

Focus should shift towards supporting firms' expansion and growth

- Our Department of Planning and Investment can only keep track of formally registered enterprises and enterprises that formally closed down. To know the actual number of operational enterprises, it is necessary to get help from the tax authorities and other local relevant agencies. For example, in 2004, when we sent requests to 50,000 enterprises in our database to submit their annual business reports, 3,000 were returned by the post office as undeliverable.

There are some possible reasons for this phenomenon: i) some enterprises have moved to new premises without notifying our business registration agency; ii) other firms “disappear” by stopping operations but not completing the formal exit procedure; and iii) there are cases where firms never operated, because they were set up for “other purposes,” such as to get residence permits. In my opinion, the formal exit procedure is not so complicated. Many firms ignore this procedure on purpose, so as to avoid paying tax obligations.

Mr. Do Xuan Duc, Chief of Business Registration Division, Ho Chi Minh City Department of Planning and Investment

Viewpoints

- Despite an increasing number of firms entering the market, domestic firms tend to be small scale, widely dispersed and have out of date technology. Just over 45% of small firms employing less than 10 workers, just under 40% are medium sized, employing between 10 and 300 workers, and less than 5% are big firms employing more than 300 workers. The average return on capital for domestic enterprises in 2000 was 5.7% and 4.5% in 2002; among private firms it is even lower, at 2.1% in 2003.

Mr. Vu Van Tuan, Director of Industrial and Construction Statistical Department, General Statistics Office

- SMEs are often depicted like small boats that are safe and dynamic in a river or less windy bay. But when they are pushed to the open sea, their life is often threatened. SMEs tend to face more difficulties in their operations than bigger businesses, as my own company’s experience has shown. First, it is very difficult to access commercial credit. After 12 years of operation, our company has never borrowed money from a commercial bank. Despite having good business plans, banks keep requesting businesses to provide collateral for loans, and yet the loan amounts are often small compared to the value of the collateral assets. Second, newly-established firms are often advised to locate in an industrial zone. These IZs may be suitable for larger firms, in order to centralize their activities, but many SMEs cannot afford the rental rates. Third, there is often a lack of coordination between tax agencies and enterprise support organizations.

Mr. Phong Dinh Ngo, Director, Binh Hoa Dat Nam Co. Ltd Co

- At the request of HCMC People’s Committee, the public-private dialogue system was officially established in August 2003, with ITPC was assigned to be its focal point. The main purpose of this system is to provide official replies to business questions and problems. After almost three years of operating this system, we see that questions related to taxate, business procedures are the most frequently raised. Although greater efforts have been made to create a favorable business environment, there are frequent complaints about the negative attitudes of local civil servants (especially their unequal treatment between local private and foreign-invested firms). Despite strong commitment from senior officials at local authorities, some civil servants keep making trouble for firms. And firms have to pay unofficial fees and charges to overcome these obstacles.

Mr. Truong Ngoc Nghia, Vice President of Investment and Trade Promotion Center of HCMC (ITPC), Head of Management Board of HCMC Public-Private Dialogue System

- ASMED is in the process of developing an SME Development Plan for 2006-2010. This includes removing constraints faced by SMEs, and creating an enabling environment for the growth of SMEs. It is our aim that by 2010 SMEs will generate up to 2.5 million new jobs each year, and their competitiveness will be strengthened, so that more will be able to directly export their products. To achieve these objectives, we still propose a number of reforms in the legal and policy framework for SMEs, including two major issues: i) minimize the cost of business establishment and operations; and ii) improve SMEs' capabilities and competitiveness. Specific proposals to change SME-related policies include: i) further simplify the business registration procedures, by removing unnecessary business sub-licenses; ii) revitalize the current tax lump-sum scheme for household businesses, which tends to discourage them from formalizing their business activities; iii) improve land planning by decentralizing the approval of SME-scaled industrial zones projects, and establishing a network of land management agencies under the amended Land Law; and iv) remove ineffective regulations related to business bankruptcy, so that the Law on Bankruptcy can genuinely come into effect.

Mr. Pham Thanh Hau, Division of General Issues and Foreign Investment Management Agency of Small and Medium Enterprises Development (ASMED)

- Vietnam’s private sector has grown significantly over the last 10 years. As an investor in private companies, we have met over 300 private Vietnamese companies over recent years. Based on our experiences, the typical private Vietnamese company has been growing at an average of around 20% per year, with some successful companies growing at significantly faster rates. We have also seen that private companies are becoming increasingly competitive against foreign-invested and state-owned enterprises. This progress is due to significant reforms implemented since the Doi Moi process began, as well as the natural entrepreneurial skills and diligent work habits of the Vietnamese people.

In spite of these positive developments, there remain some significant constraints which, if solved, could facilitate Vietnamese private companies in becoming a more significant part of the economy. For example, improvements to Vietnam’s capital markets, and the ability of private Vietnamese companies to obtain financing from those capital markets, could help to finance significant new investments, particularly in the more capital intensive sectors. At Meikong Capital, we strongly support the formation of a 5-year private sector development plan, as this
Simplified procedures have contributed to an increased number of registered firms, but the actual number of firms in operation is not as high.

- Since the Enterprise Law became effective in 2000, in Ho Chi Minh City, the number of businesses established has remarkably increased. To date, more than 50,000 enterprises have been registered, accounting for one-third of all formally-registered enterprises in the whole country. Growing at a significant rate, it is widely understood that in a pond of thousands of newborn fish, it is natural that some may die right away and others may grow up very fast. The Enterprise Law has eased the business registration process - an entrepreneur can easily register a new business without any evidence of actual operation, having it capitalized and operational. However, a post-registration monitoring scheme needs to be set up to maintain a database of enterprises and effectively support firms and their operations. Most newly-established firms need to struggle by themselves in running their businesses, without much support or assistance from the government (except for regular interaction with tax agencies). The "disappearance" rate (firms closing without completing the formal exit procedures) in Vietnam is quite high, due to the absence of a post-registration monitoring system.

Mr. Truong Tuan Nghia, Vice President of Investment and Trade Promotion Centre of HCMC (ITPC), Head of Management Board of HCMC Public-Private Dialogue System

- Currently there are three different enterprise information databases at three different agencies, and their data, in my opinion, are all accurate. The Ministry of Planning and Investment maintains a business registration database. Therefore the total figure provided by MPI is the number of formally-registered enterprises accumulated over many years - around 140,000 registered enterprises at present. The tax authority manages a database of enterprises with tax codes, since businesses have to apply for a tax code at the tax agency, after registration. This list comprises over 100,000 enterprises. The Statistics Office keeps a database of enterprises that are actually operating in the economy. This latter database excludes all "disappearing" businesses, and is updated on 31 December every year. As of 31 December 2003, there were 72,012 operational enterprises.

Mr. Vu Van Tuan, Director of Industrial and Construction Statistical Department, General Statistics Office

- There are some possible reasons for this phenomenon: i) some enterprises have moved to new premises, without notifying our business registration agency; ii) other firms "disappear" by stopping operations but not completing the formal exit procedure; and iii) there are cases where firms never began operations, because they were set up for "other" purposes, such as to get residence permits. In my opinion, the formal exit procedure is not so complicated. Many firms ignore this procedure on purpose, so as to avoid paying tax obligations.

Mr. Dao Xuan Duc, Chief of Business Registration Division, Ho Chi Minh City Department of Planning and Investment

- Despite an increasing number of firms entering the market, domestic companies tend to be small-scale, widely dispersed and have out of date technology. Just over 45% are small firms employing less than 10 workers, just under 40% are medium sized, employing between 10 and 300 workers, and less than 10% are big firms employing more than 300 workers. The average return on capital for domestic enterprises in 2000 was 5.7% and 4.5% in 2002; among private firms it is even lower, at 2.1% in 2003.

Mr. Vu Van Tuan, Director of Industrial and Construction Statistical Department, General Statistics Office

- SMEs are often depicted like small boats that are safe and dynamic enough to travel in stormy seas. But when they are pushed to the open sea, their life is threatened. SMEs tend to face more difficulties in their operations than bigger businesses, as my own company’s experience has shown. First, it is very difficult to access commercial credit. After 12 years of operation, our company has never borrowed money from a commercial bank. Despite having good business plans, banks keep requesting businesses to provide collateral for loans, and yet the loan amounts are often small compared to the value of the collateral assets. Second, newly-established firms are often advised to locate in an industrial zone. These IZs may be suitable for larger firms, in order to centralize their activities, but many SMEs cannot afford the rental rates. Third, there is often a lack of coordination between tax agencies and enterprise support organizations.

Mr. Phung Dinh Ngoc, Director, Binh Hoa Commerce Plc. Ltd Co, Head of Management Board of HCMC Public-Private Dialogue System

- ASME is in the process of developing an SME Development Plan for 2006-2010. This includes removing constraints faced by SMEs, and creating an enabling environment for the growth of SMEs. In our aim that by 2010 SMEs will generate up to 2.5 million new jobs each year, and their competitiveness will be strengthened, so that more will be able to directly export their products. To achieve these objectives, we still propose a number of reforms in the legal and policy framework for SMEs, including two major issues: i) minimize the cost of business establishment and operations; and ii) improve SMEs capabilities and competitiveness. Specific proposals to change SME-related policies include: i) further simplify the business registration procedures, by removing unnecessary business sub-licenses; ii) review the current tax lump-sum schedule for household businesses, and review surcharge from them by formalizing their business activities; iii) improve land planning by decentralizing the approval of SME-sized industrial zones projects; and establishing a network of land management agencies under the amended Land Law; and iv) remove ineffective regulations related to business bankruptcy, so that the Law on Bankruptcy can genuinely come into effect.

Ms. Pham Thi Thanh Ha, Director, General Institute for Economic and Technical Investment Management Agency of Small and Medium Enterprise Development (ASMED)

- Vietnam's private sector has grown significantly over the last 10 years. As an investor in private companies, we have seen many opportunities related to the sector, and productivity in this area is the most frequently raised. Although greater efforts have been made to create a favorable business environment, there are frequent complaints about the negative attitudes of local civil servants (especially their unequal treatment between local private and foreign-invested firms). Despite strong commitment from senior officials at local authorities, some civil servants keep making trouble for firms. And firms have to pay unofficial fees and charges to overcome these obstacles.

Mr. Truong Tuan Nghia, Vice President of Investment and Trade Promotion Center of HCMC (ITPC), Head of Management Board of HCMC Public-Private Dialogue System

Focus should shift towards supporting firms expansion and growth

- SMEs are often depicted like small boats that are safe and dynamic enough to travel in stormy seas. But when they are pushed to the open sea, their life is threatened. SMEs tend to face more difficulties in their operations than bigger businesses, as my own company’s experience has shown. First, it is very difficult to access commercial credit. After 12 years of operation, our company has never borrowed money from a commercial bank. Despite having good business plans, banks keep requesting businesses to provide collateral for loans, and yet the loan amounts are often small compared to the value of the collateral assets. Second, newly-established firms are often advised to locate in an industrial zone. These IZs may be suitable for larger firms, in order to centralize their activities, but many SMEs cannot afford the rental rates. Third, there is often a lack of coordination between tax agencies and enterprise support organizations.

Mr. Phung Dinh Ngoc, Director, Binh Hoa Commerce Plc. Ltd Co, Head of Management Board of HCMC Public-Private Dialogue System

- At the request of HCMC People’s Committee, the public-private dialogue system was officially established in August 2003, and ITPC was assigned to be its local point. The main purpose of this system is to provide official replies to business queries and problems. After almost three years of operating this system, we see that the issues related to tax are among the ones most frequently raised. Although greater efforts have been made to create a favorable business environment, there are frequent complaints about the negative attitudes of local civil servants (especially their unequal treatment between local private and foreign-invested firms). Despite strong commitment from senior officials at local authorities, some civil servants keep making trouble for firms. And firms have to pay unofficial fees and charges to overcome these obstacles.

Mr. Truong Tuan Nghia, Vice President of Investment and Trade Promotion Center of HCMC (ITPC), Head of Management Board of HCMC Public-Private Dialogue System
Viewpoints

- The Government is strongly signalizing the importance it attaches to SME development by tasking the Ministry of Planning and Investment to formulate the 2006-2010 SME Development Plan and Action Plan as an integral part of the SEDP 2006-2010. In addition, the Government has instructed all stakeholders to assess past achievements and shortcomings as well as the steps to be taken in the next five years with a view to improve the quality of growth.

This is a welcome change in focus. What it simply means is that stakeholders have to ask and respond to questions such as "what can we export efficiently?" instead of questions such as "what can we export?" Goals set at all levels have to be more about improving productivity, understanding its determinants and eliminating barriers to improvements. Instead of simple quantities to be achieved in various fields. In SME development in Vietnam, this new focus simply could mean setting an overall objective of achieving a significant increase in the contribution of SMEs to national employment growth in the next five years.

Focusing on improving the quality of growth, and hence, productivity, as a fundamental objective does not rule out the use of quantities in the planning and implementation of SME development policies and priorities. But to be realistic, there are good chances of getting implemented. Therefore, specific, realistic, time bound, cost effective and most importantly, measurable indicators have to be set to determine whether the overall and sub-objectives for SME development have been achieved. These indicators would have to be quantitative to be measurable, monitored regularly over time, and would involve statistics such as the number of new jobs created, number of new SMEs established, a specified increase in the number of firms that are exporting in the period from 2006 to 2010, etc. Basically, what matters is how many employees are used, and why and how are they used.

Ms. Ngoc T. D. Chief Technical Advisor, MPI-UNIDO SME Project

PRIVATE SECTOR FIRMS: Size matters

The private sector has increasingly been recognized as a critical engine of economic growth in Vietnam. The Ministry of Planning and Investment (MPI) is now preparing the national SME development policy 2006-2010, as part of the country’s five-year national economic development plan. Based on these policies, the Agency for SME Development will design an action plan for SME promotion. This bulletin looks at some key aspects of private sector growth, and makes some recommendations on how to develop larger and more robust private firms.

- Simplified procedures have contributed to an increased number of registered firms
- The Enterprise Law of 1999 established the principle that firms may do business in all sectors and areas that are not prohibited, and replaced the former licensing process with business registration. The enterprise and time needed to establish a business have been reduced significantly. As a result, thousands of tens of thousands of new enterprises have formally registered each year. According to data from the National Business Information Center (NBIC), which manages the national database on company registration, for the past four years the number of enterprises registered was double the number registered in the ten years prior to the Enterprise Law. By bringing the total number of registered firms in Vietnam to around 125,000.

But the number of firms in actual operation is lower
- Data from the General Statistics Office (GSO) suggests that there were 62,908 enterprises in operation by end of 2002, and roughly 72,012 by the end of 2003. This is a substantial number by any measure and can be seen in any country with a vibrant private sector, not only because businesses closures to be expected, they are an integral part of the dynamic process that occurs when firms leave the corporate sector as a whole - react to changes in the external environment (such as new market opportunities and business conditions).

This bulletin published with support from the Making Rules. Build development Facility (MRBF), a multi-sectoral initiative managed by the International Finance Corporation (IFC), the private sector arm of the World Bank Group. The Bulletin provides those interested in business issues with a short summary of key points of a particular topic affecting the business environment in Vietnam, and exposes the scope of work in SME development in the field. The content and opinions expressed here are only meant to provide additional reference material and do not reflect official opinion of the World Bank Group, or any other organization, or any government agencies or others involved in the field. The views and analysis presented here are only meant to provide additional reference material and do not reflect official opinion of the World Bank Group, or any other organization, or any government agencies or others involved in the field.