High input costs impede business competitiveness

In terms of input costs, there is not much difference between Vietnamese and Chinese garment companies. But production costs of Vietnamese companies are higher, due mainly to the high cost of transportation in Vietnam. There are several reasons for this. First, port-handling charges are high, as ports are monopolies operated by the State. Second, Vietnamese ports are small enough that large ships cannot access them directly, forcing Vietnamese exporters to pay for smaller ships to transport goods from the port to the large ships. A third and unnecessary cost is that Customs officers can add significantly to costs, especially for exporters who ship in small orders.

Another factor that adds to the production costs of Vietnamese companies is the requirement that the employer pays labor union fees. According to Government regulations, employers must pay a labor union fee equivalent to 2% of an employee’s income. The garment sector is labor-intensive, and workers’ wages and other payments already account for 50% to 60% of total production costs; any additional costs are a burden to businesses. Recently a regulation was issued concerning foreign-owned garment companies, which no longer requires the employer to pay this fee. But in domestic garment companies, this fee is still charged to the employer.

We would like to recommend that the Government makes further investments in infrastructure, especially in ports, to help Vietnamese exporters reduce costs. In addition, the Government needs to change the regulation that requires domestic businesses to pay labor union fees for their employees in order to level the playing field.

Mr. Dien Thanh Kiet, Vice Chairman, Ho Chi Minh City Garment and Textile Association

High input costs impede business competitiveness

The quality of roads and tracks is a real problem. If these were better, the transport costs of my company would be reduced by at least 30%.

It is true that labor costs in Vietnam are relatively cheap. However, qualified workers are lacking, resulting in us having to import more than 50% of our exports and machines from abroad. It is very expensive given the appreciation of the Euro, salary requirements of foreign workers, and transport costs.

Like other countries such as France, Vietnam requires a reasonable level of employee’s contribution to employee’s social security which is 23% of worker’s salary; the employer pays 17% and the employee pays 6%. However, many of my employees feel that the benefits they get are not worth the money we pay. So I think in terms of value-for-money, social security costs are too expensive.

Mr. Tinley Miermet, General Director, The Bamboo Factory JETRO Hanoi works to promote import and exports between Vietnam and Japan.

Every year, we carry out studies on market risks and the investment situation in these countries to help investors make informed decisions. We focus on the costs of doing business, which is one of the biggest concerns of investors. In 2004, we saw some positive changes with reduced labor costs due to reductions in Vietnamese workers’ personal income tax rates. But the most striking cost reduction was in the telecommunications sector. These are good signs for foreign investors.

Despite this progress, I think Vietnam can further reduce the costs of doing business. One solution is to develop local supporting industries that are currently nonexistent or weak, requiring enterprises to import expensive inputs from other countries. The Government, especially the Ministry of Industry, is aware of the problem and is working with Donors to address it. I think the Government needs to develop a comprehensive policy to support small and medium enterprises that can act as supporting industries.

Another area investors wish to be improved is the infrastructure. There are many Japanese manufacturers in the Hanoi-based Thang Long Industrial Zone that are expanding their investment, such as Canon. I am worried that within the very near future, Highway 5 to Hanoi will reach full capacity. There is an urgent need for expansion of the existing road, building a new road, or usage of railway as an alternative.

Finally, the cost of electricity in Vietnam is relatively high compared to other regional countries. But we are more concerned about the dual price of electricity, which discriminates against foreign investors. This is not good for Vietnam’s image. We wish the dual pricing in the electricity sector could be phased out, as has been the case with airfare, TV advertising, and water.

Mr. Karioj Ishiwata, Chief Representative Hanoi Office, Japan External Trade Organization (JETRO)
Weak legal systems are still a hindrance to economic growth

To improve the business environment, while developed countries need to focus on decentralization and deregulation, Vietnam needs to do much more than that. The most important tasks are to build a sound legal infrastructure for a market economy and a system of economic policies that enables international integration and increases the business sector’s competitiveness.

In order to expedite the reform process, Vietnam needs to accept business standards and rules that have been commonly accepted worldwide. This would show investors that Vietnamese laws and regulations, even if they are changed periodically, are consistent and continue to be simplified over time. Also important are leveling the playing field in terms of laws and regulations for all economic sectors and speeding up the reform processes for specific sectors.

Disputes are an inevitable part of business. When businesses bring disputes to the court, they look for fair and quick judgment. But in reality, there are many disputes that remain unresolved or are decided in an unfair manner. Our company is currently pursuing several contractual disputes that have been ongoing for the last six years, worth a total of USD$2.6 million. The longer the cases remain unresolved, the lower the chance we have of recovering our money in fact we risk losing it all as the parties concerned appear more time to disperse the assets elsewhere.

If the constraints in the judicial system are not addressed quickly, this will be a major barrier for investors looking to do business in Vietnam. Along with improving the legal framework for business, the Government needs to push reforms in the judicial agencies, especially the courts themselves and enforcement bodies, to ensure that laws are complied with.

Laws and policies in Vietnam still contain contradictions because a single law-making body does not exist. The recent process of revising the Commercial Law is an example. It was very difficult for the Ministries involved in the process to reach consensus because of conflicting interests between them. To resolve this issue, it is necessary to strengthen the role of the National Assembly as the single law-making body, and at the same time, minimize heavy involvement of implementing agencies in the law drafting process. The law drafting process should be improved by increasing the input of the business community as well as adopting international best practice.

New laws that are drafted should be simple. They should allow businesses to do anything not prohibited by the law rather than having to request permission. The Enterprise Law is a good example of this practice. It removed over 150 sub-licenses of all kinds and thus reduced costs, including unofficial costs, for businesses.

Drafting a good law is difficult, but implementing a good law is even more challenging. Implementation of the Enterprise Law has been not easy, as enforcement takes away “bribes” from some public servants. This has led in some cases to new sub-licenses being issued to replace ones that were just removed. To resolve this issue, the Government needs to do regular reviews of all legal and regulatory documents to “clean-up” unnecessary ones on a regular basis rather than an ad-hoc manner.

Ms. Pham Thi Phuong, Deputy Director, Macro-economic Policy Department, Central Institute for Economic Management, MPI (CIEM)

The Enterprise Law has removed 150 sub-licenses, but in fact, there are still numerous cumbersome administrative procedures that businesses still have to deal with. After registration, a business still has to go through many procedures before it can actually start operations, including applying for company name at an approved place, registering for a tax code, applying for and purchasing a red-invoice book, etc. It is worth mentioning that businesses have to complete each procedure separately before the next one can take place, hence the whole process takes more than 50 days.

Mr. Tien Loc, Chairman and President, Vietnam Chamber of Commerce and Industry

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Mr. Trung Quy, Director, Vietnam Automobile Motor Company

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The business environment in Vietnam has improved significantly for foreign investors in recent years. It took me only 11 months to get the “Thai Bamboo Factory” up and running. However, I find that there are still various unofficial costs for business. Take the example of railway transport. I have to pay a number of “taxes” to take the bamboo out of forests. The problem is that I have to pay these “taxes” at numerous roadblocks at district and commune levels. These costs are unpredictable and unfair, and therefore are not tax-deductible.

Mr. Thanh Nam, General Director, The Bamboo Factory
Weak legal systems are still a hindrance to economic growth

- To improve the business environment, while developed countries need to focus on decentralization and deregulation, Vietnam needs to do much more than that. The most important tasks are to build a sound legal infrastructure for a market economy and a system of economic policies that enables international integration and increases the business sector’s competitiveness.

In order to expedite the reform process, Vietnam needs to accept business standards and rules that have been commonly accepted worldwide. This would show investors that Vietnamese laws and regulations, even if they are changed periodically, are consistent and continue to be simplified over time. Also important are leveling the playing field in terms of laws and regulations for all economic sectors and speeding up the reform processes at the central and local level.

- Currently, Ministries are heavily involved in the law drafting process. Though their involvement is necessary, in my view, the Ministries themselves should not have the responsibility or authority to draft the actual document. Ministries should undertake research, policy analysis, and give their recommendations. The drafting of the law itself should be carried out by an independent agency, which would coordinate experts from the relevant line ministries. The National Assembly should have the authority to review draft laws on the basis of balancing the interests of the whole society rather than coordinating the interests of specific sectors.

Dr. Vu Tien Loc, Chairman and President, Vietnam Chamber of Commerce and Industry

- Laws and policies in Vietnam still contain contradictions because a single law-making body does not exist. The recent process of revising the Commercial Law is an example. It was very difficult for the Ministries involved in the process to reach consensus because of the conflicting interests between them. To resolve this issue, it is necessary to strengthen the role of the National Assembly as the single law-making body, and at the same time, minimize heavy involvement of implementing agencies in the law drafting process. The law drafting process should be improved by increasing the input of the business community as well as adopting international best practices.

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Drafting a good law is difficult, but implementing a good law is even more challenging. Implementation of the Enterprise Law has been not easy, as enforcement takes away “benefits” from some public servants. This has led in some cases to new sub-licenses being issued to replace ones that were just removed. To resolve this issue, the Government needs to do annual reviews of all legal and regulatory documents in order to “clean-up” unnecessary ones on a regular basis rather than in an ad-hoc manner.

Ms. Phan Thanh Ha, Deputy Director, Macro-economic Policy Department, Central Institute for Economic Management, MPI (CIEM)

- Disputes are an inevitable part of business. When businesses bring these disputes to the court, they look for fair and quick judgment. But in reality, there are many disputes that remain unresolved or are decided in an unfair manner. Our company is currently pursuing several contractual disputes that have been ongoing for the last six years, worth a total of USD 2.6 million. The longer these disputes remain unresolved, the lower the chance we have of recovering our money; in fact we risk losing all the fines against the parties concerned more time to dispense the assets elsewhere.

If the constraints in the judicial system are not addressed quickly, this will be a major barrier for investors looking to do business in Vietnam. Along with improving the legal framework for businesses, the Government needs to push reforms in the judicial agencies, especially the courts themselves and enforcement bodies, to ensure that laws are complied with.

Mr. Jang in Kim, Director, Vietnam Davaco Motor Company

- Law enforcement in Vietnam remains weak. That is one reason why Vietnam’s economy is still a cash economy; cash transactions remain as long as there is little confidence in a party’s ability to enforce an agreement. If laws are to be respected, judges must be independent. That means the laws must be applied equally, regardless of the identity or status of the parties. Vietnam is trying to increase the professionalism of the courts. One possibility is to have a pilot model to encourage judicial independence and excellence, whereby, for example, in one or more judicial districts, only judges with a law degree are allowed to serve, or only judges who are not from that district can serve, or judges be rotated. If the model works, it can then be improved upon and replicated.

Mr. Secco Vecchi, Managing Partner, Russo & Vecchi Law Firm

- There is still a general lack of confidence related to contract law, mainly because most Vietnamese lawyers still have mentality of working in a centrally planned economy and they still work with model contracts from that era. Those model legal documents are outdated, incomplete and in some cases are contradictory with one another. As a result, Contract Law in Vietnam is obsolete and unable to protect businesses from contractual risks.

Mr. Pham Hung Hy, Head of Business Law Division, Law Department, the National University, Hanoi

Administrative red tape increases costs of doing business

- Vietnam needs to quickly undertake public administration reform; government agencies need to move towards transparency, simplicity and speed, in order to ensure that the economy in general and businesses in particular are able to react to constant changes in the market.

Dr. Vu Tien Loc, Chairman and President, Vietnam Chamber of Commerce and Industry

- The Enterprise Law has removed 160 sub-licenses, but in fact, there are still numerous cumbersome administrative procedures that businesses still have to deal with. After registration, a business still has to go through many procedures before it can actually start operations, including applying for a company seal at an approved place, registering for a tax code, applying for and purchasing a red-invoice book, etc. It is worth mentioning that businesses have to complete each procedure separately before the next one can take place, hence the whole process takes more than 50 days.

Mr. Vu Duy Thanh, Deputy Director, Central Institute for Economic Management, MPI (CIEM)

- Laws and administrative procedures are meant to guide and facilitate businesses activities. However, in Vietnam this is not always the case. The common perception among government bodies is that the existing laws are in place to control businesses rather than to facilitate a better business environment. As a result, Ministries often issue additional regulations and licenses to make it more convenient for them to control businesses. We need to change this perception, and procedures need to be more business-friendly.

Dr. Nguyen Si Dzung, Vice Chairman, Office of the National Assembly

Corruption is a threat to social stability and economic development

- The business environment in Vietnam has improved significantly for foreign investors in recent years. It took me only 11 months to get "The Bamboo Factory" up and running. However, I find that there are still various unofficial costs for business. Take the example of in-country transport. I have to pay a number of "taxes" to take the bamboo out of forests. The problem is that I have to pay these "taxes" at numerous checkpoints at district and commune levels. These costs are unpredictable and unfair, and therefore are not tax-deductible.

Mr. Thierry Mamers, General Director, The Bamboo Factory

- I think corruption hurts at two levels. The direct impact is that it pushes costs up, and this affects consumers’ welfare and producers’ competitiveness. But its worst effect is to foster a sense of cynicism in the Vietnamese public. If one sees that corruption is part of everyday life—that is, if it is so common that it is no longer seen to be wrong to pay or accept bribes—it becomes easier to accept corruption or even to participate. Even limited corruption makes the public believe that it is widespread, and honest and concerned officials—of whom there are many in Vietnam—are tainted by implication. The current crackdown on corruption gives me some confidence. The drive seems to be both serious and broad.

Mr. Secco Vecchi, Managing Partner, Russo & Vecchi Law Firm
In terms of inputs, there is not much difference between Vietnamese and Chinese garment companies. But production costs of Vietnamese companies are higher, due mainly to the high cost of transportation in Vietnam. There are several reasons for this.

First, port handling charges are high, as ports are monopolized operated by the State. Second, Vietnamese ports are small enough that large ships cannot access them directly, forcing Vietnamese exporters to pay for smaller ships to transport goods from the port to the large ships. Finally, there are unnecessary pro-forma payments to Customs officials that add significantly to costs, especially for exporters who ship in small orders.

Another factor that adds to the production costs of Vietnamese companies is the requirement that the employer pays labor union fees. According to Government regulations, employers must pay a labor union fee equivalent to 2% of an employee’s income. The garment sector is labor-intensive, and workers’ wages and other benefits, including bonuses, have accounted for more than 50% of total production costs; any additional costs are a burden to businesses.

Recently a regulation was issued concerning foreign-owned garment companies, which no longer requires the employer to pay this fee. But in domestic garment firms, this tax is still charged to the employer.

We would like to recommend that the Government makes further investments in infrastructure, especially in ports, to help Vietnamese exporters reduce costs. In addition, the Government needs to change the regulation that requires domestic businesses to pay labor union fees for their employees in order to level the playing field.

Mr. Dyep Thanh Kiet, Vice Chairman, Ho Chi Minh City garment and Textile Association

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Like other countries such as France, Vietnam requires a reasonable level of employee’s contribution to employer’s social security which is 23% of worker’s salary; the employer pays 17% and the employee pays 6%. However, many of my employees feel that the benefits they get are not worth the money they pay. So I think in terms of value for money, social security costs are too expensive.

Mr. Tien Le, General Director, JETRO Hanoi

Vietnam has made considerable progress in closing the business environment. In 2004, we saw some positive changes with reduced labor costs due to reductions in Vietnamese workers’ personal income tax rates. But the most striking cost reduction was in the telecommunications sector. These are good signs for foreign investors.

Despite this progress, I think Vietnam can further reduce the costs of doing business. One solution is to develop local supporting industries that are currently nonexistent or weak, requiring enterprises to import expensive inputs from other countries. The Government, especially the Ministry of Industry, is aware of the problem and is working with Donors to address it. I think the Government needs to develop a comprehensive policy to support small and medium enterprises that can act as supporting industries.

Another area investors wish to be improved is Vietnam’s infrastructure. There are many Japanese manufacturers in the Hanoi-based Thang Long Industrial Zone that are expanding their investment, such as Canon. I am worried that within the very near future, Highway 5 to Hai Phong will reach full capacity. There is an urgent need for expansion of the existing road, building a new road, or usage of railway as an alternative.

Finally, the cost of electricity in Vietnam is relatively high compared to other regional countries. But we are more concerned about the dual price of electricity, which discriminates against foreign investors. This is not good for Vietnam’s image. We wish the dual pricing in the electricity sector could be phased out, as has been the case with airfare, TV advertising, and water.

Mr. Kentaro Ishikawa, Chief Representative Hanoi Office, Japan External Trade Organization (JETRO)

The electricity price in Vietnam has been under review since 1994 and has already increased 17 times in 2004. The price of electricity in Japan is lower compared to Vietnam. In addition, foreign investors are burdened by the high rate of electricity. This is a concern for Japanese investors.

Mr. Tien Le, General Director, JETRO Hanoi

The cost of electricity in Vietnam has increased significantly over the past year. In October 2004, the “one-stop service” model involving administrative procedures had been implemented in 75% of provinces, 85% of districts and 12% of communes. However, public administration is still considered by many to be inefficient and negatively impact the business environment. Some of the most common problems include:

- Excessive administrative procedures for business registration, which in some cases are required for up to 160 days.
- Arbitrary interventions of governmental administrative bodies in business activities.
- Government offices harassing and creating difficulties for businesses.
- Lack of transparency and accountability of government administrative agencies.

Another specific example of weak public administration is the process of land registration. The authorities involved have not been able to improve this process, which is still taking a long time, with an average time of 60 days and a total cost of 35% of GDP per capita, which is too high.

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