

OVERVIEW OF NON-STATE SMALL AND MEDIUM-SIZED ENTERPRISES IN VIETNAM

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Over the past decade, since Vietnam launched its "Renovation Policy" (doi moi) and developed a multi-sectoral economy, many small and medium-sized private enterprises (abbreviated as SMEs) have been established and grown considerably, increasing their role in the national economy.

1. What do we know about non-state small and medium enterprises in Vietnam?

Results from studies, surveys, official statistics, publications, and other articles published in recent years on SMEs, can be summarized as follows:

1.1. The development of SMEs plays an important role in the country's development

Most researchers and policy-makers agree on the important role of SMEs in the industrialization and modernization process in Vietnam. The importance of that role can be expressed in the following ways:

- promoting economic growth: SMEs account for a major part of total national production and trade, hence contributing significantly to gross domestic product, state budget and exports;
- encouraging economic structural adjustment as part of the process of industrialization and modernization. SMEs attract labor from agriculture to work in the service and industrial sectors, and from the state sector to the non-state sector. At the same time, the development of SMEs also helps to adjust and diversify the structure of the industrial sector and reduce the need for imports;
- speeding up the urbanization process; SMEs stimulate economic development in the countryside, narrowing the development gap between rural and urban areas;
- having the ability to meet fast-changing and diversified market demand appropriately, thus making the country's economic development more dynamic;
- creating many new jobs, both for skilled and unskilled workers, help to solve today's major political issue, unemployment, and improving employees' income. The average income of an SME employee is estimated to be three times that of an agricultural laborer;
- mobilizing effectively public funds, which seems to be huge but used to be saved at home;
- supporting and promoting the development of large enterprises through their links with these enterprises. At the same time, SMEs themselves often develop into large entities;
- training business managers for the market economy. SMEs are rapidly adopting new technologies, and form breeding grounds for the development of scientific and technical progress.

So how have non-state SMEs developed, in both quantity and quality?

1.2. Although some initial achievements have been recorded, until now, the development of SMEs in Vietnam is still far from the optimum level

According to the government's temporary regulations issued in June 1998, the criteria for being a SME are to have a capital value of less than VND 5 billion, and an average number of employees

across one year of less than 200. Prior to this regulation almost all documents categorized SMEs using the following criteria, based on the Vietnam Chamber of Commerce's requirements:

Table 1: *Categorization of Small and Medium-sized Enterprises*

Size of enterprise	Industrial sector		Trade and service sectors	
	Capital (VND million)	Labor (employees)	Capital (VND million)	Labor (employees)
Medium enterprise	5-10	200-500	1-5	50-100
Small enterprise	<5	<200	<1	<50

Source: According to the Vietnamese Chamber of Commerce.

Based on these criteria, most non-state enterprises (including joint-stock companies, limited liability companies, private companies and sole-proprietorship companies) are of small and medium size. Until 1996, the proportion of private and limited liability companies with capital of more than VND 5 billions was very small (comp. table 2).

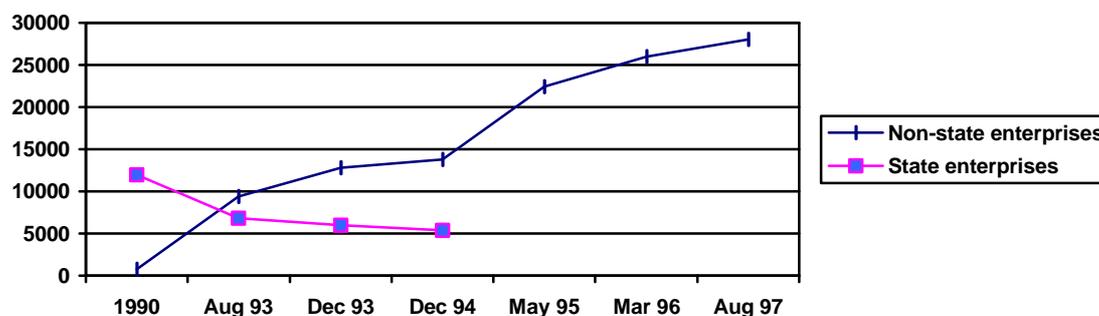
Table 2: *Capital of non-state enterprises (%)*

Capital (billion VND)	Private enterprises	Limited liability companies	Joint-stock companies
<1	95.1%	69.0%	14.5%
1-5	4.4%	25.7%	27.9%
>5	0.5%	5.3%	57.6%
Average	168.8 million VND	775.1 million VND	10,330 million VND

Source: Statistical Yearbook of Vietnam, Hanoi 1995.

During the period from 1990 to 1997, private companies as well as non-state enterprises in general, grew rapidly in total number, the number of employees, and the level of invested capital and revenue. According to statistical data, in 1986 (when the reform policy was first applied) the number of private enterprises was insignificant, rising, by 1990, to 770 with approximately 100,000 employees. In August 1993, there were 9,389 non-state enterprises with nearly 500,000 employees.

Figure 1: *Number of enterprises*



By December 1993 the number had increased to 12,738 with a total capital value of VND 3,979 billions. At the end of December 1994, there were 13,772 private companies, 5,120 limited liability

companies and 133 joint-stock companies, totaling 19,025 enterprises with a total capital value of VND 6,621 billion (equal to 13.6% of the value of State-owned enterprises). In June 1995, the total number of each of the three forms of enterprises was 22,432 with a capital value of VND 8,256 billion and VND 35,547 billion revenues. In March 1996, the number of non-state enterprises reached nearly 26,000 (comp. figure 1) with a capital value of VND 10,584 billions. Thus, during the period 1990 - 1997, the development of the SME sector was remarkable, and has contributed to the high growth rate of the Gross Domestic Product (GDP) over the past few years.

SMEs are involved in almost every sector of the economy: industry, agriculture, aqua-culture, mining, processing, construction, trading and the service sector. However, most of the capital was invested in the trade and service industries, followed by processing industry and aqua-culture. These industries have a substantial domestic market, with a potential for significant profits, and a high rate of return. According to statistics from 1995, the trade and service sectors accounted for 63.3% of total enterprises and 50.3% of capital value.

SMEs are located unevenly through the country, centering on urban areas, especially large cities. 68% of joint-stock companies, 59% of limited liability companies and 12% of private companies are located in Hanoi, Haiphong and Ho Chi Minh City alone.

Between 1995 and 1997 however, the private sector contribution to GDP increased only modestly. For example, its contribution grew by 3.1%, 3.3% and 3.4% in 1995, 1996 and 1997 respectively. SMEs as well as private enterprises' effectiveness is still very low, even in comparison with SOEs (comp. table 3). This limits the potential for accumulation of capital for further development.

Table 3: Effectiveness of the enterprises in 1995

	Rate of profit/capital	Rate of profit/turnover
State enterprises	0.054	0.038
Collective enterprises	0.048	0.022
Private enterprises	0.057	0.018
Joint-stock companies	0.018	0.010

Source: Data from an economic survey in 1995, General Statistical Office.

Since the onset of the regional economic and financial crisis, the growth rate of SMEs has slowed down both in number and in effectiveness.¹ Many enterprises were unable to continue operating and went bankrupt. Some enterprises, which had been successful, are now making losses. According to a survey in Hanoi and Ho Chi Minh City, less than 50% of enterprises currently operate effectively.

In brief, although some initial achievements have been recorded, the development of SMEs in Vietnam is still far from the optimal level.

1.3. Some advantages of SMEs

In the present socioeconomic situation of Vietnam, SMEs have the following advantages:

- Legally, the operation of SMEs as well as of private enterprises in general are accepted, protected and encouraged by the government. The role of SMEs in the country's development is also recognized and respected.
- The management and production units are small, flexible and easy to adjust. Direct management and supervision, without intermediate stages, contribute to lower administrative costs.

¹ Nguyen Cuc, "Building conditions of assistant frame for small and medium enterprises in Vietnam", in: Economic Studies Review, No 238.

- SMEs are often more active and responsive to changes in the market, even in times of crisis. They can also more rapidly change their activities and products to meet market demand. In addition, they can more easily change the number of employees.
- The initial start-up investment of SMEs is relatively small. Therefore, the costs can be covered rapidly.
- SMEs can make use of Vietnam's abundant and cheap labour force, low training costs and the low cost of insurance for labourers.
- Apart from these above advantages, SMEs are also supported by domestic and foreign institutions through capital investment, professional training, technology and market development.

1.4. Disadvantages and Limitations of SMEs

Besides the above-mentioned advantages, SMEs in Vietnam also have shortcomings including:

- SMEs equity is often very limited (comp. table 2). They lack capital for maintaining and expanding their business and production. Meanwhile, the possibility to expand capital resources is very thin. According to the findings of a research in Hai Duong and Hung Yen in 1995, most of the enterprises' sources of capital stem from equity, followed by private borrowing, stock capital, and lastly, borrowing from state banks. State credit only plays a modest role in promoting the establishment and development of non-state SMEs.
- The material and technical base of SMEs is often very weak, characterized by backward technology. An important reason for this is shortage of capital. Many enterprises also lack the necessary information and consulting services on technology transfer, especially in rural areas. The ability of small enterprises to handle and use modern technology is limited. Many proprietors tend to focus their business strategy on industries requiring small investments and short break-even periods, often hesitating to renew technology. Moreover, the SMEs also face difficulties in terms of administrative procedures and taxes for imported technology.
- Places for productive activities are usually very small and far below the actual need of SMEs, especially in urban areas and large cities.
- The market for SMEs products is small, unstable and very competitive. Only a few items can be exported. Some researchers offer the following explanation: low quality goods and high prices due to backward technology; poor promotion and advertisement of the goods being offered; competition from illegal and tax-evading imports due to limited government control and protection.
- In general business management skills are not up to the mark. Only a few owners are equipped with business knowledge of a market economy. Most of the proprietors run businesses based on their own experience. In addition, their understanding of business law, and attitudes towards the rule of law is questionable.
- Although labor is abundant, most job-seekers are unskilled workers. While only a small number of SMEs can provide training for their employees, government support in training is negligible.
- Infrastructure is insufficient, in particular transportation, electricity and clean water. There are also significant differences between different regions, and between rural and urban areas.
- Many owners of SMEs do not fully believe in the current policy to develop a multi-sectoral economy. Laborers and the public in general still don't trust private enterprises, an attitude that finds its root in Vietnamese economic history.

- Some business associations and communities have been set up but are ineffective. Small enterprises doing business independently without linking with large enterprises will find it hard to overcome strong competition in the marketplace.

1.5. Government's policy and management over SMEs

- The freedom to do business and to set-up business is stipulated in the 1992 Constitution. Many related laws have been promulgated, and some have been revised several times. In principle, all government policies are aimed at stimulating the development of SMEs.
- However, the government has not established a concrete strategy and promulgated a specific law for SMEs. In general, law for SMEs are still in the process of completion, and some issued documents are not appropriate to the new situation.
- Although efforts to improve the situation have been made, the administrative procedures necessary to set up companies and register business activities are still too complicated, lengthy, and inconsistent, causing many difficulties for enterprises. Corruption in the government's administrative system has not been appropriately dealt with, and illegal trading, tax evasion and manufacture of counterfeit products have not been fought effectively.
- Inequality between small and large enterprises, and between private and state enterprises still exists, especially in the credit and investment policies of the banking system, and the land-use policy.

1.6 International organizations' supports

Small and medium enterprises have attracted more interest and support from international organizations than any other part of the Vietnamese economy. Many projects to support SMEs are sponsored by international organizations such as: ZDH (The SMEs-supporting Association of Germany), UNICO (The United Nations Technology Development Organization), ESCAP (Economic and Social Commission of Asia-Pacific), SMEs Development Fund of Vietnam, the EU, and the ILO (International Labor Organization).

These support projects are quite diversified, including activities such as the establishment of the fund for SME development, granting loans, providing training for business starters, business development constancy, and export promotion support.

2. Issues that need to be studied

In recent years, the term "small and medium enterprises" have appeared more and more in publications, books, journals as well as in the mass media of our country. This demonstrates the interest of the society in the development of Vietnamese small and medium enterprises. However, it also seems that we do not fully and comprehensively understand the issues involved, especially the social aspect related to SMEs. Here we put forward some aspects:

First, the concept "small and medium enterprises" itself has not been clearly defined. Statistical data, research findings, and political documents use different definitions, thus making direct comparisons difficult. Moreover, even if the concept is agreed, it is not easy to identify the actual levels of capital and profits amongst these enterprises. In Vietnam, there are many reasons for enterprises to declare a higher level of capital than the real figure, or the other way around. Some people estimate that the actual figures are "3-4 times the registered level of capital".² If that situation continues, it might be very difficult to set out the best policies for small and medium enterprises. The question is not only why enterprises present false data but also how can they be allowed to do so?

² Hoang Kim Giao, "Capital of small and medium enterprises", in: Economic Studies Review, No 219.

In a society in transition from a centralized subsidy-based economic mechanism, to a market economy, such as in Vietnam, there are two sides of every field of the economy: official and unofficial activities. Official business data frequently differs from the actual situation. E.g., the "administrative transaction" expenses may be for one item, but are declared for another one; in reality the conditions for borrowing money and for winning a tender are not always as simple as stipulated. These and many other phenomena are easily found out just by reading Vietnamese newspapers. All of them are close to "unwritten laws" that all enterprises must obey and sometimes obey even more strictly than other official laws if they want to continue to exist and develop.

Operating in such an environment, together with the difficulties and shortcomings summarized above, the risks for small and medium enterprises are relatively high. To compete and develop, enterprises have to take into account the "unofficial" dimension. The quicker small enterprises want to develop into large enterprises the more they have to take account of the "inofficial" side and sometimes to a dangerous extent - the extent to which the line between success and law violation is very thin. Perhaps it is not a coincidence when most of the recent important economic law violation cases are related to enterprises, which used to be regarded as successful.

On the other hand, when enterprises cannot or do not dare doing so, limiting the "official" degree in their business activities is often a simple measure to protect their interests. Some private companies want to dissolve their business in order to register their operations under Decree 66 (household business). In other words, many investors do not want to do business on a large scale, or in reality, they cannot do "business in the form of companies or private enterprises".³ Short-term interest is often put before long-term strategy, and sometimes even before an enterprises' prestige. This is very worrisome for the development prospects of small and medium enterprises in our country at the moment. Are the conditions for that development not only the amendment of some laws or degrees, but further reform of the legal framework as well as management mechanisms?

The social acceptance of SMEs would have great significance for the development of this sector in the future. For a long period prior to the reforms, private sector activities were limited and discouraged in many ways. As a result people are often biased against, disrespect, and despise this group of enterprises.

Nowadays, perhaps, many people cannot fulfil their dream of being "proprietors". However, some of them still keep in their mind the image of businessmen as the rich, opportunists, and exploiters of labor, rather than those who produce goods and create jobs for society. Employees of small and medium enterprises do not believe in and have not been content with their work, unlike those who work for state-owned or large enterprises. Therefore, it is hard for small and medium enterprises to attract qualified and highly skilled labor compared to the state sector unless they pay much higher salaries. Moreover, it is not easy for small and medium enterprises to be optimistic for their rapid and stable development in the future.

Another issue is the link between SMEs as well as their links with other large enterprises through the establishment of associations, support funds, agreements on strategies and markets, and cooperation in production and distribution of goods and services. From an economic perspective, these links are vital, especially for small and medium enterprises, in order to be able to regulate the market needs, reduce negative competition and limit risks. The expression "business must have partners, trading must have associations" shows the need for associations of businessmen in the traditional Vietnamese society. However, associations tend to be unofficial and based only on close relationships, friends, and neighbors etc. not on the economic and functional relations as in modern societies. Until now, the degree of cooperation among small and medium enterprises is not only limited but is of similar nature to those in traditional societies.

³ Vu Quoc Tuan, "Making socioeconomic environment for the establishment and development of enterprises", in: Sociological Review (Vietnamese), No 4/1998.

Perhaps, the ability to create associations in a systematic way only exists in large foreign invested enterprises. The major function of those systems is the distribution, rather than the production of goods. In addition, "*in this cooperation, small and medium enterprises often lose out economically due to unfair practices of large enterprises*".⁴ The link between small and medium enterprises on the one side and large state-owned enterprises on the other may be more complicated. It is clear that as long as the government does not have a concrete mechanism to encourage, direct and control the links between enterprises, that such associations cannot actively facilitate the development of small and medium enterprises.

3. Conclusion

The establishment and development of SMEs plays an important role in the industrialization process in Vietnam. It is also an inevitable dimension of socioeconomic development in our country at the moment. However, apart from some initial encouraging developments, the operation of SMEs in recent years has revealed many shortcomings and difficulties of both objective and subjective natures.

For a steady development of SMEs, besides the perfection and implementation of government policies, economic solutions, technological development, a reform of the legal framework, and social acceptance of SMEs are also necessary conditions for their successful future development.

Basically, economic laws can be applied in many different countries. However, the effective application of such laws depend heavily on the cultural, social and political characteristics of each country. Therefore, in order to lay the ground for policies that meet the above-mentioned requirements, other concerned social aspects relating to SMEs are also important and need to be focused on so that they can be fully understood.

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⁴ Duong Ba Phuong, "Improving medium and small enterprises in rural areas in progress of industrialization and switching to market economics", Hanoi: Agricultural Publishing House, 1996: 196.