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Viet Nam Economy: State-Owned Enterprise (SOE) Reform and Market Structure

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VIETNAM ECONOMY: SOE Reform and Market Structure

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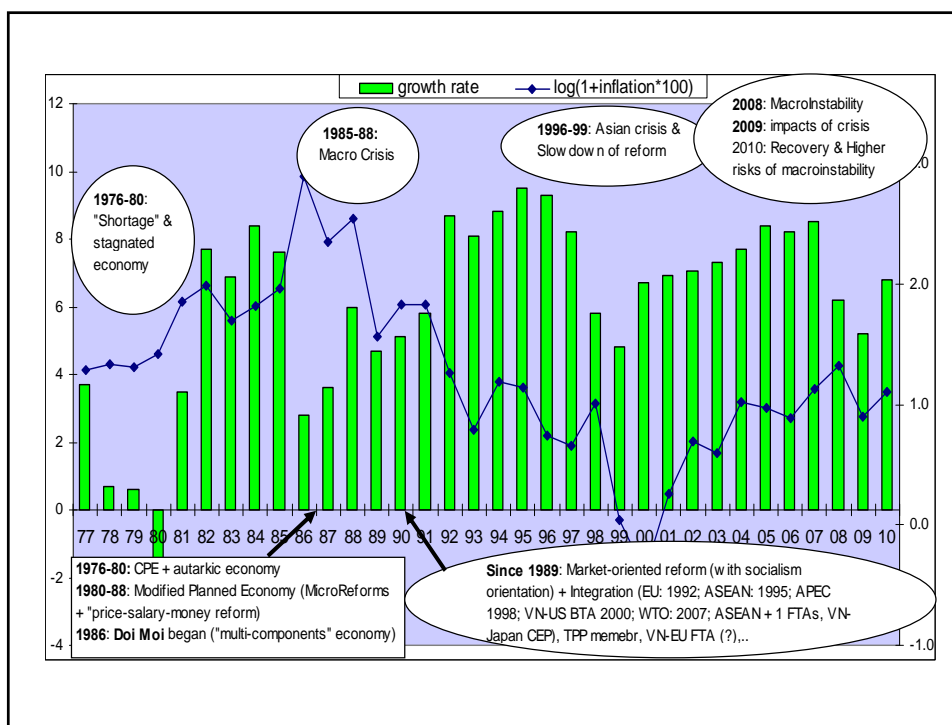
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Outline of presentation

- 30 YEARS OF REFORM AND PERFORMANCE**
- PROCESS OF SOE REFORM**
- MARKET STRUCTURE AND ROLE OF SOE SECTOR**
- KEY ISSUES**

30 YEARS OF REFORM & PERFORMANCE

- ❑ **Up to 1980:** a CPE + relatively autarkic economy
- ❑ **1980 - 85:** Some bottom-up (“fence breaking”) reforms and micro=reforms, but the failure of “price-salary-money reform” in 1985 → crisis
- ❑ **1986:** Doi Moi (Renovation) began (recognition of “multi-components” economy + SOE’s autonomy)
- ❑ **Since 1989:** Market – oriented reforms + Trade liberalization and integration (EU: 1992; ASEAN: 1995; APEC: 1998,..)
- ❑ **1996 - 99:** Slowdown of the reform process
- ❑ **2000 - 10:**
 - Stronger commitments to further reforms, but with uneven implementation
 - VN-US BTA; AFTA fulfillment; WTO accession, ASEAN+1-FTA
 - Party Congress IX (2001), X (2006) and XI (2011) → New wave of reforms?



Nature and major dimensions of VN's economic reforms

- ❑ Reform is to enlarge both sets of (economic) choices by people and their capability to exploit benefits from the newer choices
- ❑ The major reform dimensions
 - Market-oriented reforms (price liberalization; private internship and rights of doing business; SOE reform)
 - Implementation of open door policy and international economic integration (mostly in terms of trade and FDI)
 - Reforms for ensuring macroeconomic and social stability

There is consensus about the 'nuts and bolts' of (economic) transition, which encompasses three sets of reforms: liberalization and stabilization; institutional changes that support market exchange and shape ownership; and the establishment of social programs to ease the pain of transition.

(World Bank 1996)

Reform has also been a very complex process reflecting the changes in the way of thoughts of VN policy-makers

- ❑ Some key terms used by VN for characterizing the economy during reform
 - “Subsidized and bureaucratic centrally-planned economy” (before Doi Moi in 1986)
 - “Multi-component commodity production economy” (1986 -1989)
 - “Market-oriented economy under state management” (during 1990s)
 - “Market economy by socialism orientation” (After 2000)

“The rejection of central planning by so many countries in 1989 represents one of the truly extraordinary events in the history of economics. But the transition to the market also presents economists with formidable challenges because the path has never been trod before” (Jeffries 1993)

Achievements impressive: *VN became a low-middle income, more industrialized and open economy*

- ❑ Economic growth: 1990s: 7.2% pa; 2001-05: 7.5% pa; 2006-10: 7.0% pa.
- ❑ GDP per capita: 100 USD in the early 1990s; 1160 USD in 2010
- ❑ Poverty incidence: 70% in mid-1980s; 10.6% in 2010
- ❑ Economic structure in terms of GDP: In 1991 Agriculture: 40.5%; Industry + Construction: 23.8% (manufacturing 13.1%). In 2010: 20.3%; 41.1% (21.0%); 38.6%.
- ❑ Export growth: 1990s: 24% pa; 2001-05: 17.5% pa ;2006-10: 15.8% pa (Openness in 2010: X+M)/GDP \approx 160%)
- ❑ FDI sector: It became an integral part of the economy (2010: 19.9% GDP; 54.0% export value (incl. crude oil export); 25.8% total investment)

... but not outstanding

- ❑ Low quality of growth: High but inefficient (public & SOE) investment; high business costs; distorted production factor markets (capital, land, and labour markets); limited spill-over from FDI)
- ❑ Being engaging in global/regional production network but with weak positions in the global/regional value chains
- ❑ Substantial poverty in isolated regions + “new poor” + widening income/asset gap
- ❑ Polluted and deteriorated environment
- ❑ (Recent) macroeconomic instability (inflation; budget deficit and public debt; trade and CA deficit; expansion of financial and real estate activities but weak supervision)
 - ➔ *Growth and development sustainability?*
 - ➔ *Possibility of falling into “low cost labour trap” /”trade liberalization trap” in long run?*

PROCESS OF SOE REFORM

Why SOE reform is essential?

- ❑ Inefficiency due to principle-agent & “moral hazard” problems
- ❑ High cost of budget & risks of macroeconomic instability
- ❑ Possibility of crowding-out private sector development
- ❑ Pressure for being recognized as “market economy” (International commitment under WTO membership)

VN has recognized the inefficiency of SOE sector, but attempted to ‘restructure and equitize SOEs rather than “privatizing” them.

- ❑ In the early 1990s, Gov’t reduced substantially subsidies to SOEs and gave them greater autonomy and several inefficient enterprises were liquidated.
1990 – 94: number of SOEs fell from 12000 to less than 7000
- ❑ 1993-94: several State General Corporations (17 GCs 91 & about 70 GCs 90) were established
- ❑ In the second half of 1990s, SOE reforms stagnated
- ❑ In 2001 there were 5355 SOEs, of which 1997 enterprises are under control of Central Government. During 2001-05, Vietnam restructured 3572 SOEs, of which 2378 SOEs were equitized. However, these equitized SOEs accounted for only about 10% of total state capital in SOEs.
- In general, the performance of equitized enterprises in terms of profitability and financial state was better or much better than before equitization.

- Since 2006, there have been new (but maybe contradictory) dimensions of SOE reform
 - To cement the equitization of SOEs and to list them in stock market
 - To equitize the large SOEs and some General Corporations (GCs), including those in important services sector
 - To transform large SOEs and State General Corporations into the holding-subsiary, and to establish *experimentally* the State Business Groups. The expectation is that they can take advantage of internal linkages, large scale and diversity of ownership to be more efficient and more competitive (?).
 - By the end of 2010, 12 State Business Groups and about 100 state holding-subsiary corporations have been formed

- To establish the SCIC: Motivations are to remove a conflict of interest concerning line ministries/provinces and to achieve a more efficient use of state capital

Role of the SCIC

The SCIC began operations in August 2006 to concentrate state shareholding in the equitized SOEs under one single entity.

The SCIC has classified equitized SOEs into three groups, A, B, and C.

- It will concentrate on strengthening or restructuring enterprises in Group A, which operates in sectors considered strategic.
- Group B enterprises with good potential will be supported for listing on the stock market.
- Group C comprises enterprises where the state does not need to invest in them over the long term. SCIC will gradually sell state shares in companies of this group.

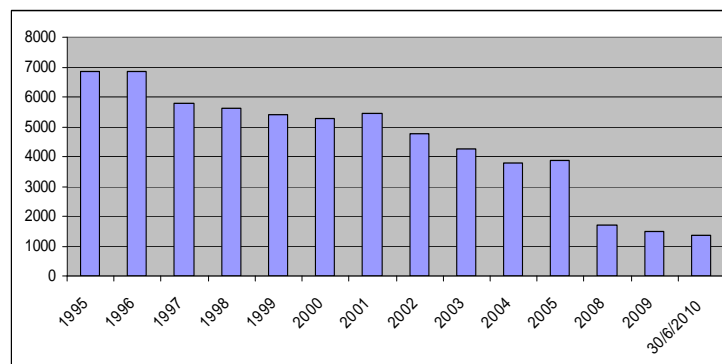
SCIC Investment Portfolio

(30/062011: 461 enterprises; VND 12,895 bill)

	No of Enterprises	% of portfolio
Group A	16	62
Group B	87	22
Group C	358	16

- To transform all SOEs in complying with Enterprise Law (no later than 1 July 2010)
(Together with liquidationg, all SOEs are to be Liability Limited firms with a state owner or share-holding companies)

Number of 100% state-owned enterprises



MARKET STRUCTURE & ROLE OF SOE SECTOR

Structure of GDP by economic sector (% at current price)

	1991	1996	2000	2006	2007	2008	2009
Agriculture-Forestry-Fishing	40.5	27.8	24.5	20.4	20.3	22.1	20.7
Industry-Construction	23.8	29.7	36.7	41.5	41.5	39.7	40.2
- Manufacturing	12.8	15.2	18.6	21.3	21.3	21.1	20.9
Services	35.7	42.5	38.8	38.1	38.2	38.2	39.1
GDP	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: GSO and CIEM's estimates

Structure of GDP by ownership (% at current price)

	1991	1996	2000	2006	2007	2008	2009
State Sector	29.3	39.9	39.0	37.4	35.9	34.3	33.2
Non-state sector	70.7	52.7	47.7	45.6	46.1	47.0	47.5
FIE sector	0.0	7.4	13.3	17.0	18.0	18.7	19.3
GDP	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: GSO

Industrial Output Structure by sub-sector and ownership								
Industrial sectors	2000				2008			
	% of gross output	% of a specific industry output			% of gross output	% of a specific industry output		
	Total	FDI	SOE	Non-State	Total	FDI	SOE	Non-State
Total	100.00	35.94	41.80	22.26	100.00	40.46	25.20	34.34
Mining industry	13.78	83.28	12.71	4.01	5.53	63.63	26.02	10.35
<i>Mining of Coal</i>	1.19	1.21	97.41	1.38	1.09	1.20	96.92	1.88
<i>Petroleum and natural gas</i>	11.47	99.85	0.15	0.00	3.49	99.90	0.10	0.00
<i>Metal ores</i>	0.11	2.39	72.25	25.36	0.11	8.10	65.09	26.81
<i>Stone and other mining</i>	1.02	1.02	48.85	50.13	0.84	1.52	36.21	62.27
Manufacturing	79.72	30.09	42.69	27.21	89.14	41.29	20.87	37.85
Food products and beverages	22.00	22.26	44.22	33.51	22.04	28.78	14.12	57.10
<i>Tobacco prods</i>	2.90	0.55	98.86	0.59	2.00	1.20	98.50	0.30
Textiles	5.07	25.98	50.57	23.45	4.16	32.10	26.64	41.26
Wearing apparel	3.05	24.82	31.88	43.30	4.05	45.39	10.33	44.28
Leather; leather prods	4.33	43.06	29.35	27.59	4.05	63.40	5.20	31.40
Wood and wood prods	1.81	12.13	20.02	67.85	1.75	22.63	9.25	68.12
Paper and paper prods	1.98	11.89	47.34	40.76	2.02	25.41	25.37	49.22
<i>Publishing, printing and media</i>	1.15	1.58	89.99	8.43	1.04	6.40	75.23	18.37
Coke, refined petroleum prods	0.12	28.92	0.00	71.08	0.06	26.52	5.51	67.98

<i>Chemical and chemical prods</i>	2.58	63.76	13.01	23.23	5.94	42.52	36.81	20.67
Rubber and plastic prods	3.26	23.67	32.20	44.13	4.93	36.55	13.22	50.23
<i>Non-metallic mineral prods</i>	9.21	21.84	58.31	19.85	7.56	29.24	40.50	30.27
Basis metal	2.98	45.40	40.20	14.40	3.09	33.51	28.05	38.44
Fabricated metal products, expt. machinery and equipments	2.91	26.83	16.63	56.54	5.21	42.25	12.34	45.41
Machinery and equipments	1.39	32.91	48.15	18.94	1.40	42.82	15.07	42.12
Office and computing machinery	0.65	98.21	0.00	1.79	1.33	99.62	0.00	0.38
Electrical machinery and apparatus	1.83	35.34	49.00	15.66	3.90	50.73	27.42	21.86
Radio, communication equipments	2.22	81.30	16.33	2.37	2.33	88.56	8.22	3.21
Medical, precision, optical instruments, watches, clocks	0.22	72.79	19.62	7.59	0.23	83.35	4.11	12.54
Motor vehicles	1.63	80.20	9.97	9.83	2.43	82.24	9.42	8.34
Other transport equipment	3.24	73.25	16.85	9.90	5.57	70.12	17.21	12.67
Furniture	1.98	27.96	8.37	63.67	3.97	46.71	6.21	47.08
Recycling	0.08	0.00	0.00	100.00	0.08	8.52	0.51	90.97
Electricity, gas and water supply	6.50	7.30	92.52	0.18	5.33	2.53	96.82	0.65
<i>Electricity, gas</i>	5.96	7.50	92.44	0.06	5.02	2.56	97.07	0.36
<i>Water</i>	0.54	5.11	93.41	1.47	0.31	2.01	92.67	5.32

Source: GSO and CIEM's estimates

Some sectors with the highest concentration indexes

	CR3	Number of firms	HHI
Crude oil and natural gas exploitation	99.97	7	6472.62
Broadcast and TV	88.52	30	5239.62
Telecommunication	85.96	354	3438.07
Post and delivery	80.45	119	2937.99
Air transportation	76.25	13	3049.06
Financial services (excl. insurance)	67.48	1519	2253.86
Insurance, reinsurance, and social insurance	63.36
Cigarette production	57.74

Source: Cuc Quan ly canh tranh (2009)

- Role of SOEs declined significantly in manufacturing (Number of sub-sectors in which SOEs account for more 30% of output declined from 11 in 2000 to 4 in 2008), but not in mining sector and utility.
- Sectors with declining CR3 are those with high growth. Sectors with increasing CR3 (such as textile) could have higher efficiency (?).
- Subsectors with very high market shares of (large) SOE/State Business Groups: Electricity; Coal; Paper; Cement; Cigarettes; Fertilizers; Petroleum Product; Basic chemicals; Gasoline; Rail transportation; Air transportation.
- SOE: \approx 50% of firms having the largest share by sector (FIEs: 30-35%; private firms: <20%) (See also Table of sales by firm)

Total sales by firm and by ownership (VND billion/firm)

	2000	2006	2007
TỔNG SỐ	19.1	20.4	20.7
SOEs	77.2	259.4	255.8
<i>Central SOEs</i>	<i>153.3</i>	<i>442.5</i>	<i>407.1</i>
<i>Local SOEs</i>	<i>34.6</i>	<i>96.7</i>	<i>120.7</i>
Non-state firms	5.8	9.1	11.1
Cooperative	3.0	3.1	3.5
Private	3.5	5.9	6.4
Partnership	6.0	3.2	2.3
Liability limited	10.1	9.0	10.3
<i>Shareholding (with state equity)</i>	<i>33.7</i>	<i>101.3</i>	<i>122.8</i>
Shareholding (without state equity)	13.6	12.2	17.2
FIEs	106.2	141.4	148.3
<i>100%-foreign owned firms</i>	<i>69.6</i>	<i>98.8</i>	<i>106.4</i>
<i>Joint ventures</i>	<i>152.8</i>	<i>303.2</i>	<i>326.5</i>

KEY ISSUES

SOE reform is more political economy process rather than purely economic one. It is very much depending on the perception and awareness of the role of SOEs

- A legacy of a CPE: the ways of directing and controlling resources, esp. in public investment allocation and dealing with SOE sector
- Interpretations of the concept of “Market economy by socialism orientation”?
 - (Leading) role of the state sector and SOEs?
 - State function & ownership and income distribution?
- Problem of asymmetry in incentives for having social consensus
 - Winners and losers because of reform?
 - Overcoming vested groups?

Some more specific issues

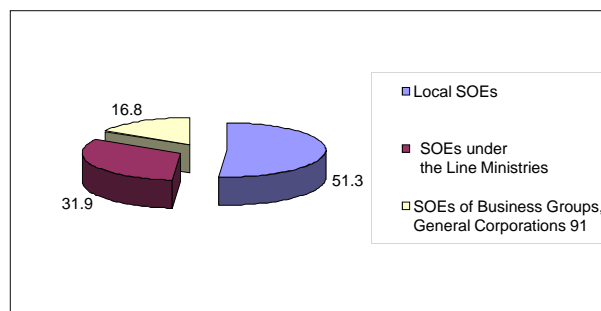
- ❑ Driving forces for VN's long term development: (SOEs + FDI)/(Private sector + FDI)/(Something else)?
- ❑ Creating "a level playing field" and an effective competition, while keeping a leading role of the State and SOE sector?
- ❑ SOEs (especially GCs and Business Groups) should be efficiency-oriented but also important instruments for macroeconomic stabilization?
- ❑ Recognizing state monopoly, but preventing it to be transformed into firm's monopoly?

- ❑ Separation between the functions of the State as the owner of SOEs and as a manager and supervisor for the whole economy (?)
 - Representative of the ownership and supervision over the State Large Corporations and Business Groups?
 - Interaction between SCIC and the line ministries?
 - Other concerns of SCIC:
 - Transparency and accountability?
 - Profit-oriented mandate but (could) being a market stabilizer?
 - Effective supervision over the SCIC?
 - Expertise in dealing with complex financial activities?

- Effective transformation of all SOEs in complying with Enterprise Law.

Requirements (and Results):

- On time (no later than 1 July 2010)? **OK!**
- Widening coverage (taking into account all forms of SOEs such as companies in a Business Groups; companies of socio-political organizations ;...)? **Acceptable**
- Guidance for managing and supervising liability limited companies with a state owner (e.g. transformed parent companies of State Business Groups)? **Limited.**



Thank you!