

PROMOTING private SECTOR development in Vietnam FROM the Effectiveness of Supporting policies

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1. Background

Over the last 20 years of Doimoi (renovation) reform policy in Vietnam, private sector has significantly contributed to the outstanding success of the economy. The rapid development of this sector has been resulted from the opening -up economic policy pursued by Vietnamese government and particularly, from the issuance of the Enterprise Law. This law and other policies have been creating a favorable business environment for the private sector development.

After 20 years of Doimoi, this is a right time to review and assess our policies in order to find the way for further development. The question here is how effective the private sector development policies over the last 20 years are? How do these policies contribute to the private sector development? What are the policy weaknesses and bottlenecks? And, how these policies should be improved to reinforce industrialization and modernization in Vietnam?

To answer the above questions, this paper will focus on: (i) Overview of the development of the private sector and it's role in Vietnam for 20 years of Doimoi; (ii) An assessment of the effectiveness of the private development policies incentives; and (iii) Some policy recommendations.

In this paper, "private sector" is understood as the enterprise registered under Enterprise Law (1999). These can be limited companies, joint-stock companies, partnership companies and private enterprises. This definition excludes: (i) unregistered enterprises ; (ii) households; (iii) foreign invested firms; and (iv) state owned enterprises (SOEs). In other words, private sector in this paper is only a part of so called "non-state sector" in Vietnam.

Private sector development policies are understood as a set of related policies, which has a certain impact on its development. Many of these policies may simultaneously influence all kind of firms, meanwhile some others have impacts on only private firms. This paper will look at the following policies: (i) administrative reform for market entry, (ii) tax policies; (iii) credit policies; (iv) land policies; and (v) services to support business development. .

2- Overview of the private sector development and it's role in Vietnam over 20 years of Doimoi

2.1. From 1986 to 1999

During this period, Communist Party of Vietnam and State acknowledged the private sector as an objective and necessary economic entity in the multi-sectoral economy and it should be given favorable conditions for further development. Constitution of Vietnam 1992 stipulates "Vietnamese are free to do business by law". This idea is also indicated at various Resolutions of Vietnamese Communist Party Congresses. Based on the above awareness and guidance, there was a significant change in private sector development policy. Policies were specified in many important economic laws, such as: Private Enterprise law (1990), Company Law (1990), Law on Domestic Investment Promotion (1994) and its revised version in 1998. Therefore, the private sector has been recovered and started developing.

Company and Private Enterprise Laws have laid down a first and important legal framework for private sector development. As a result, private sector has revealed its rapid development in terms of considerable increase in number of private enterprise. In 1991, there were 414 firms. This figure increased to 5,189 firms in 1992, 15,276 in 1995, 39,180 in 1998 and 45,601 firms in 1999.

Average of fixed asset per one private enterprise (one owner) in 1991 was VND 0.1 billion, the lowest level. This increased to and stabilized at VND 0.2 billion during 1992-1996. Meanwhile, that of limited companies also increased but unstable. It was VND 0.6 billion in 1991, increased to VND 0.7 billion in 1992 and failed to VND 0.5 billion in 1996.

Number of labor in a private enterprise was 8 persons on average in 1991. This figure recorded an increase to 9 persons in 1996, 17 persons in 1997, and 19 persons in 1998. Growth rate of private firms in 1994 increased by 60% compared to those in 1993, and decreased gradually in the subsequent years: in 1995 was 41%, in 1996 was 24%, and in 1997 was 32%, about 37% on average during 1994-1997.

2.2. From 2000 to 2005

Together with some reform policies, Enterprise Law (1999) (effective from January 1st 2000, replacing Private Enterprise Law and Company Law) is a breakthrough in economic and administrative reforms, establishing a favorable business environment for private sector development, pushing up economic growth as well as creating employment. A number of the private enterprise has drastically increased (Table 1).

Table 1: Number of Newly Registered Enterprises

	1991-1999	2000	2001	2002	2003	2004	2005
Private enterprise	29,135	6,412	2,229	6,532	7,085	10,246	11,366
Limited company	15,310	7,304	7,179	12,627	15,120	20,145	20,674
Joint-stock company	524	726	1,243	2,305	3,715	6,470	6,675
Partnership company		2	0	0	1	7	8
1 member limited company		0	0	59	88	125	130
Total	44,962	14,444	21,040	21,523	26,009	36,993	38,114

Source: Information Center on Enterprise – Ministry of Planning and Investment

After 6 years of implementing the Enterprise Law, from 1/1/2000 to 31/12/2005, 158,153 new enterprises have been registered, made the total of registered enterprises to 203,115. Average number of newly registered enterprise daily during this period was 3.75 time higher than that during 1991-1999. Number of newly registered enterprise for 5 years (200-2005) was three times higher than those over 9 previous years (1991-1999). Not only number of newly registered firms has been increased, their size as well as scale has been enlarged. Growth rate of their production output exceeded those of the state enterprise and foreign invested enterprise since 2000. Yet, private firms are of small scale. Currently, they account for 96% of total number of small enterprises according to the criteria specified in Decree 90/2001/ND-CP.

Newly registered and expended investment increased significantly by VND 293,878 billion (about USD 18.4 billion) for 5 years, from 2001-2005, higher than the foreign investment inflow to Vietnam during the same period. Private investment has been playing an important role in development, especially it has been the main source of local development investment .

2.2.1 Achievements

Since the Enterprise Law was promulgated, the private sector has been strongly developed and becomes a driving force for socio-economic development of Vietnam. This can be shown in the following aspects:

- Private sector has created about 2 millions new jobs. It also contributed to the shift of labor structure, which was inherently imbalanced, and contributed to the economic growth and poverty reduction in Vietnam.
- Private sector contributed increasingly to the state budget, from 6% in early 2000s to more than 7.5% in 2005. This sector also increased the state revenue from registration tax, value added tax (VAT) for imported goods, and other fees. Private sector has made the business environment more active, increased competition, pushed up the reform of state enterprises, and reduced the monopoly status of many state companies.
- Private sector also contributed to export. According to Ministry of Trade, presently, domestic private sector exports account for about a half of total export value of

Vietnam. Many firms have occupied a certain international market share in some important goods. In the local areas, private sector played a key role in exporting.

- Private sector contributed to establish an equal playing field, and accelerated the international economic integration process of Vietnam. Besides, the development of the private sector also stimulates the development of other markets such as goods and service markets, labor market, real estate market, capital market, and technological market.

2.2.2. Shortcomings, weaknesses and difficulties

Besides the above achievements, the private sector in Vietnam reveals some weaknesses and constraints, specifically as follows:

- Majority of private enterprise is small, more than 85% them have a capital less than VND 1 billion. Besides several medium and large firms with fairly modern production technology, most of them are technology outdated, manually produced, semi-mechanical and mechanical, and low competitive. Therefore, their business is neither stable nor durable.
- Private sector lacks capital. They have to borrow capital from the informal market with high interest rate and for a sort time. They hardly access to loans of the commercial banks, especially to those with preferential interest rate. The main reason is that they are lacking assets to mortgage. Many of them do not know about the assistance of the Government.
- Private sector is coping with the difficulty regarding the access to land for their business. As a result, many private firms have to use their residential area for production, causing environmental pollution problems. Other firms have to hire land belonged to state owned enterprises at much higher rental fee than that regulated by the State. Therefore, they do not dare to invest in big workshops and equipment because they are afraid of having to return the rented land. Many firms face the difficulty in changing the land use purpose. Administrative procedure relating to land is very complicated, time consuming, causing high transaction costs and business opportunity losses.
- Private sector is difficult in sustaining effective for a long time and competitive in the market. The main reason is private sector is underdeveloped, they are in fact managed by family style. There exists the form of limited company but with small-size, low technological level, low capital accumulative and mobilization capability, poor management skills, lack of skilful labor; lack of business strategy, running business in "quick-fit"/short-term style, unstable; poor linkage and corporation with other firms in order to get higher profits.
- Many state regulations are not well enforced. For example, some firms abuse regulations to make profit by perjuring, evading tax, and selling receipts. Some other firms do not regularly report and declare tax as regulated. Violation of intellectual property rights such as good imitation and copying, unhealthy competition, smuggling, fraudulent trade happens regularly. Many firms do not comply the labor regulations such as labor allowance, labor safety and security, labor insurance, etc.

- Beside the above constraints and difficulties, private firms also face difficulty in terms of input materials, market access, low productivity and insecure feeling in expending their business.

In short, private sector in Vietnam has developed at a high growth rate but not in sustainable manner, and less internationally competitive. In order to develop private sector and to make it as an economic engine for Vietnam development, the State should have effective measures to push up this sector.

3- Assessment of the effectiveness of the private sector development policies

3.1. Administrative reform for market entry

Resolution No.38/CP of the Government dated May 4 1994 on reforming the administrative procedures relating to the citizen and organization identified that “administrative procedures on new firms establishment and business registration” are put in a high priority. In 1998, some reform measures to simplify the administrative procedures of firm establishment and registration were undertaken. As a result, the private sector with much potential has been primarily stimulated.

Enterprise Law (1999) was an important landmark of the state's effort to facilitate the private sector development. One of the radical change or so-called breakthrough was to abolish 150 business licenses for firm establishment and to simplify as much as possible the registration procedures. This means that citizen rights on doing business freedom, including being free in selecting business form, in establishing firms, in organizing and managing firms, and in deciding the firm size, place and industry, except those forbidden by Law, have been institutionalized and realized.

. Time for business registration approval was significantly shortened down. It is 15 days by Law, but in reality, businesses in some localities had to spend only 3-7 days for receiving business registration approval.

The Enterprise Law (2005) is a further improvement of the Law (1999) by eliminating the differentiation and discrimination by ownership type, creating an equal legal playing field for all types of businesses and supplementing some provisions to protect investors, especially the small investors as well as some regulations on state management.

3.1.1. Achievements

It is clear that the policy reform relating to market entry, especially that regulating the new firm establishment, has made a break though for the development of private sector. . Some achievements of this reform are as follows:

First, this reform has created an “equal playing field” for all businesses regardless their ownership type. As a result more and more new firms are born. The abolishment of unnecessary business licenses and administrative procedures has “expanded” the entry opportunity for business.

Second, the reform promotes the entrepreneurship of Vietnamese, mobilizing domestic resources, especially those of private sector for the development.

Third, the acknowledgement of rights in doing business and the above reforms create favorable conditions for economic international integrations.

Fourth, the level of competition, a basic element of the market economy, has notably been increasing. Besides, goods and services markets, capital market, labor market and real estate market have been developing.

Finally, the administrative reform and capacity of the administration bodies has been improved thanks to the above change.

3.1.2. Shortcomings

Although the Enterprise Law has been implementing well in many places, yet some burdensome administrative procedures are still created by some local authorities.

Some local authorities required irrelevant procedures beyond the law's requirement. These can be requirements to prove financial capacity even for those not regulated by Law or to prove the rights to use the headquarter office. . Besides, there is difficulty for firms when registered in the field, which requires the professional certificates. As regulated, only 6 business sectors need professional certificates, but in fact, some localities asked for the professional certificates in additional business fields such as construction supervisor etc.

To complete administration procedures, including business registration, establishment announcement, application for tax code, tax invoice, custom code, seal, bank account, etc., it costs the new firm in Hanoi USD 170 totally and 63 days on average.¹

All above problems not only made the registration process more difficult with higher cost and more time consuming, more importantly, it also discourages investors and deteriorates the business environment in Vietnam.

3.2. Tax policy

Tax system has gradually been unified to apply equitably for all kinds of ownership form, including private firms. This aims at establishing a legal framework for business environment, pushing up a healthy competition, ensuring the equality on tax liability and making tax regulations suitable with the market mechanism managed by the state.

Among many Laws issued from 1986 to 2005, Value Added Tax Law and Corporate Income Law have significant impacts on firms. Besides, some tax incentives regulated in Law on Domestic Investment Promotion (1994) and the Revised Law (1998) also have

¹ According to a survey of Hanoi Industrial and Commerce Association.

positive impacts on the private sector development . That includes the policies on land use tax exemption or reduction; import tax exemption, corporate income tax incentives for investment project, which fall into the subjects which are promoted.

3.2.1. Achievements

The reform on tax declaration and payment does give firms more autonomy. This means that firms are responsible to declare, compute and pay tax according to the announcement of the state agencies and being responsible for their actions. From 1/1/2004, as regulated by VAT Law, Corporate Income Tax Law and Tax Law on Special Consumption, firms have been required to declare, compute and pay tax by themselves without the announcement of the state agencies. The administration procedures for tax exemption, reduction and refund are regulated clearer and simplifier. Unnecessary requirements are crossed out by law. Firms identify the tax preferential by themselves when declaring tax and paying tax based on that calculation.

Besides, there is an improvement in tax code registration. One tax code is applied for both domestic business and export-import. It allow to shorten time for tax code registration, simplify the administrative procedures on buying tax invoice. Firms are encouraged to print the invoice by themselves and this had reduced troublesome administration procedures. . The new tax refund process has been applied, i.e. refund first and check latter. A clear mechanism on coordination with market management state agencies has been established. This aims at improving the professional capacity of the tax officials and help them to check and supervise each other.

The tax incentive policies have stimulated the private investment and therefore, this increases the state budget revenue. Tax policy also contributes to establish the equal playing field for doing business by applying unified tax system to all types of ownership.

3.2.2. Weaknesses

However, tax policies still have shortcomings. For example, presently, 14 cost items are accepted for income tax deduction. However, these items are not specified clearly therefore they are understood and applied differently by different state agencies. In fact, the detailed regulations on the above costs limit the flexibility in doing business because it is hard to regulate all kinds of costs in the law. Some other regulations are too strict, limiting the firm autonomy, for instance, the regulations on calculating the wage in non-state owned enterprise. This cost must follow the real wage principle, not exceeding the norm of state owned enterprise in the same industry. The advertisement and marketing costs are normal costs in the market economy but limited at 10% of total cost at maximum in the Corporate Income Tax Law.

The centrally managing tax invoice and tax declaration has created loopholes for some illegitimate firms to evade tax and created negative impacts on the majority of legitimate

firms. Recently, the policy of self-tax declaration and payment has been introduced as a pilot, but not yet applied on a large scale/nation wide.

Recently, some authorities are overhasty to attract more investors therefore they have issued some tax incentive policies, which are more generous than those regulated by Law. Some provinces extend the time for corporate income tax exemption regulated by Law. In opposite, some provinces do not pay attention on their tax incentive policies and even create obstacles for firms. For instance, there is a case that Tax Office did not accept the preferential investment certificate provided by Chairman of Provincial People Committee and did not reduce/exempt tax for firms as regulated by the Law on Domestic Investment Promotion².

3.3. Credit Policies

An effective financial system will contribute to economic growth by assisting firms in terms of providing credits³. Credit policies have impacts on the development of private sector by the following ways:

- They may impact on the financial intermediaries, which provide the capital for the private sector;
- Preferential credit policies of the Government would have impacts on investment in some specific fields, including the investment of private sector.

Before 1986, Vietnam had a poor and distorted credit and financial system, with one tier state bank system and without a financial market. The state bank operated as a central bank and, at the same time, as a commercial bank. With that system, the banks only lend to the state sector, especially the state owned enterprises. Consequently, capital market was not developed and commercial banks did not play their functions. This impeded the development of the economy in general and the private sector in particular.

In 1990, two Ordinances on banking, namely Ordinance on State bank and Ordinance on Bank, Credit Cooperatives and Financial Companies, were issued. Under these two Ordinances, the one tier bank system was changed into two-tier bank system. Starting from this time, private sector became a customer of the bank, although this sector seems to face difficulty in accessing an official banking credit system.

For the development investment credit of the State, Development Assistance Fund provided state credits to assist investment projects in certain industries and sectors, which need to be promoted as regulated by the Government. From 1999, Decree 43/1999/ND-CP on state development investment credits regulated that the Government would give loan for development investment projects. However, in reality, Decree 43 heavily subsidized investors in the following senses: many investment projects received preferential loans but in fact they were infeasible and inefficient; almost of preferential

² Report for the Domestic Entrepreneur Meeting 2003, CIEM

³ Harvard International Development Institute, Vietnam Economic Reform toward flying dragon, 1994

loans were given to the State Owned enterprises due to many reasons, including the thinking that if the state owned enterprises could not repay the loan, the State would absolve these enterprises from the payment of debts⁴. This creates the inequality in accessing to the state development credit and made it less effective in investment promotion as targeted.

To overcome the above limitation, Decree 106/2004/ND-CP of the Government dated 1/4/2004 on state development credit narrowed down the list of preferential credit beneficiaries. Decree identified 14 groups of beneficiaries for preferential credits representing the important fields/products which the government should support, and increased the interest rate up to 70% of interest rate applied to medium and long-term loans by state commercial banks. This aims at gradually decreasing the subsidy through credit which is relevant to the international economic integration trend and at the same time, creating the pressure to improve economic efficiency..

During 1990s, almost private firms were newly established, not long enough to formulate their image. The banks, therefore, did not want to lend money to them. Consequently, many firms could not access to the bank loan to expand their business. They mainly approached unofficial financial fund for their expansion. The survey result showed that the banking sector provided only a fourth of capital demand of private firms⁵.

One of the important reasons for the difficulty in accessing to the bank loan of the private sector is the prolonged discrimination between SOE and private firms which indicated in the banking loan regulations.

3.3.1. Achievements

Reform in the banking sector created the official financial sources for the private sector. The private sector to some extent benefited from the state development credit policy.

The discrimination among state and private sector in accessing to the banks has gradually reduced when the Law on Credit Agencies issued in 1998 and the revised law in 2003. The Law regulated the rights of commercial banks, especially the state commercial banks, in doing business. This allows commercial bank giving loan based on the market demand and financial status of the customers. The state central bank no longer controls the interest rate of deposit and loan of commercial banks. The financial institutions can set the interest rate for credit based on the capital demand and supply and their credibility⁶.

⁴ According to the report of Development Assistance Fund sent to Central Economic Committee dated 26/10/2001, the investment project of the private, joint-stock companies and limited companies were lent VND 850 million per project on average and those of small household were lent VND 55 million per project. In total, private firms and household have lent 28% of total project of Development Assistance Fund, but equivalent to only 8% of total loan of the Fund.

⁵ Report on "Survey on the practice and the future development of entrepreneurship and the private sector", Central Institute for Economic Management (CIEM), Hanoi 11/2000.

⁶ Decision of the Mayor of the State Central Bank 546/2002/QD-NHNN dated 30/5/2002 on implementing the negotiated interest rate in the Vietnam dong credit between the credit agencies and the customers.

3.3.2. Limitations

Although credit policies have been notably reformed but not radically yet, some problems still present as follows:

First, the bank still has a prejudice against private sector. They usually consider private firms as a small client, precarious operation, dishonest, having less feasible projects, difficult in supervising, and bearing a high transaction cost⁷.

Second, although the Decree 178/1999/ND-CP on loan assurance of the credit agencies regulates that banks are allowed to select the way to lend either with or without asset assurance but in reality almost no bank select to lend without asset assurance. In the coming time, if any bank apply this method, it's hard for private firm to be lent without asset assurance. Private firms consider as narrow scope, little capital, not credible enough to be lent without asset assurance. This is the main obstacle for private firms. Besides, in order to be lent without asset assurance, the borrowers have to fulfill certain condition, which is hard for young private firms.

Third, as the matter of fact, the main assets could be mortgaged for bank loan in Vietnam presently is the land use rights. However, regulations on land use rights and its usage for mortgage are complicated and not clear. In addition, there is no public unified registration system in Vietnam for land use right, rental and mortgage. Although one has a legal land use right certificate, the banks need to evaluate the value of that land.

Credit Assurance Fund for Small and Medium Enterprises (SMEs), a policy instrument to assist the SMEs, has been regulated but not yet established in almost provinces because the Fund regulations are not feasible and irrelevant.

3.4. Land policies.

Based on Vietnam Constitution, the Land Law was issued on 14/7/1993. The Law has been revised three times so far. The most recent revised Land Law (2003) has a significant improvement compared to the two previous versions. Besides, the regulations on state assistance relating to land are mentioned in the Law on Domestic Investment Promotion.

However, in the context of gradually formulating market institutions and the changing economic and social development process, many issues on land demand, transactions and relations have not been captured yet in Law. For example, the Law does not clearly differentiate the specific entities, which are assigned by the state for land without paying rental, or those with land use fee payment or rental. It does not clearly specify the rights of the organizations, household, individuals, using land not for agriculture farming or forestation purpose.

⁷ Report of State Bank No.1227/NHNN-CSTT (24/10/2001)

The Law on Domestic Investment Promotion regulates some policies to support the investors such as public announcement on the master planning on land use, building the small and medium industrial zone in the areas, which have difficult socio-economic conditions; building infrastructure outside industrial and exporting zones.

3.4.1. Achievements

To implement the above policy measures, many localities have taken some following actions:

- Construct small and medium industrial zones; establish local industrial clusters so that the private sector have a site to do business.
- Announce publicly the land use master plan; introduce the production location to potential investors.
- Carry out some assistance such as exempting and reducing the land use fee, land use tax for investors. For firms, which move to the planed areas, they can sell their land use rights to others in order to get additional fund for their business.
- Many localities have initiatives to assist investors in getting land for their business. They applied various measures such as simplify the administration procedures to assist firms to clear land for production. For instance:
 - In principle, firms negotiate directly with the landholders but in case firms meet some difficulties, local authorities will take the role.
 - Firms are assisted about 50-100% of total costs of land clearance and compensation for those outside industrial zones.
 - Exempt or reduce some fees such as rental fees, land use tax, etc.

A report on 10 years implementation of Law on Domestic Investment Promotion (1996-2004) done by CIEM shows that up to 2004, 4,463 projects have been assisted for land, rental fees and land use tax exemption and reduction. Of which, the private sector has 3.1 time higher than SOE in the number of project are given land for rent. But, in terms of area, total area of land given to SOE is 1.7 times larger than those given to private sector. The above evidence shows that the state policies are more and more opened/friend to private sector.

3.4.2. Weaknesses and shortcomings

Some problems on the land for business are as follows:

- Some localities do not have stable master plan of land use therefore many firms can not find the location for their business or bear high cost for land clearance and compensation;
- Some localities do not pay attention to and implement well the measures on building industrial zones and clusters, infrastructure outside the zone. The cost for renting place at the reasonable industrial and exporting zones is not relevant for the private firms (because they are small and less competitive). In addition, some policies on exempting and reducing land rental fees for investment projects as regulated by Domestic Investment Promotion Law are not yet implemented in some places.

- Many non-state firms can rent the land for their production for only a short time with high price so that affect negatively on their long-term investment strategy. For those, using their owned land usually face difficulty and disadvantaged in changing the land use objectives.
- There is an improvement in public announcement of land-use plan but it is not yet widely and regularly applied in all authorities.

3.5. Policies on business development supporting

Recently, business consultation service is booming in many industries and fields, including consultation service on real estate information, employment, education, construction design, legal issues. These services have significant impacts on the potential growth of the economy. This trend shows that Vietnam is going on a right track, under the market principles, in terms of work/labor division. However, there are some problems, existing in these services such as unprompted trend, profit-oriented, and snatching.

The issuance of Decree 90/2001/ND-CP on supporting SMEs confirms the important role of SMEs in the economy. According to this Decree, the registered firms with less than VND 10 billion of capital and less than 300 regular labors will be supported. The assistances will be taken in various programs. SMEs will partly be financed a cost for training, consultation, credit, and land, etc. This would stimulate SMEs to use many services, including business development services (BDS).

Presently, no statistics on BDS such as number of customers, number of suppliers, market size, growth of the market, etc. is available. But based on the survey result of CIEM in collaboration with IFC and MPDF in 2002 on non-state SMEs and other studies, some basic descriptions on BDS in Vietnam can be outlined as follows:

- BDS started developing in Vietnam and accounted a small percentage in GDP, about 1% of GDP in 2002 with the low growth rate, approximately 1-2% annually⁸.
- Businessmen, even policy makers and government officials are not well aware of the role of BDS as an instrument for firm development. Markets for BDS, including services on training, accounting, consultation on finance and tax, especially management consultation are poorly developed, both in supply and demand sides.
- Percentage of private firms using BDS out of total number of private firms in the South is highest whereas it is lowest in the Central areas. The firms using BDS mainly locate in big cities, particularly in Hanoi and Hochiminh.
- Private firms do not use BDS as much as expected. Private sector considers that they can get this kind of services from their owned employees or from other individual relations. They do not need to buy this kind of services regardless of its usefulness, importance or popularity. This is the main thinking of private sector on BDS.
- Quality of BDS in Vietnam is low, the capacity of the supplier are much lower than those in the region and in the world. Services are too poor and underdeveloped to meet the demand of SMEs.

⁸ See "Legal environment for BSS in Vietnam" done by VCCI, CIEM, GTZ, 11/2003.

- Service suppliers in Vietnam are poorly developed. Almost private suppliers are small, lack of capacity to meet the demand. State suppliers are still subsidized and not dynamic. Supply from abroad is limited. Supplier lack of information on the need. They do not cooperate with each other to supply a package of services to the customers⁹.
- It is a lack of competition in providing BDS and to some extent it is in a monopoly status. Consequently, quality of the services is poor, price is high, no pressure to be improved.

3.5.1. Achievements

First, some policies assisting the BDS partly help firms in doing business such as export award, assistance for training cost, etc.

Second, some policies contribute to the establishment of the BDS market. Development of this market provides more business opportunity for firms. Firms can either provide BDS or be developed further due to using BDS.

3.5.2. Shortcomings and unsuccessfulness

First, regulations are not detailed, relevant and clear enough (for example those on business legal consultation) therefore many of assistance policies have not been implemented yet, in particular those regulated in Decree 90/2001/ND-CP.

Second, policies are not continuously and radically implemented. For instance, currently, the supporting policies on training and trade promotion are no longer implemented as before. Firms have to find financial sources to train their workers by themselves as before.

Third, it is lacking of specific assistance programs. The implementation of the assistance programs totally depends on the local budget. Therefore, some provinces carry out the policies, some do not. Besides, localities will provide the assistance based on their capacity. This creates differentiations in assistance policies across countries.

4. Overall assessment

Most policies on private sector development assistance have been issued since late 1990s. Some indicators on the private sector development (such as number of private firms, contribution to state budget, export and import value, etc.) indicate this sector's rapid growth since 2000. This means that some policies do have certain impacts on the development of private sector.

4.1. Successful policies

The analysis shows that some policies are more effective than others.

⁹ Ho Hung, "Bridging supply-demand" p.37 Saigon Economic Times, 15/1/2001

First, administrative reform on firm establishment can be considered as the most successful policy. The Enterprise Law is highly appreciated by business community because it eases administrative burden to firms. The other successful policy relating to administrative issue is to abolish administrative barriers in export-import.¹⁰ This made the number of export-import firms increase from less than 1000 before 1999 to tens of thousand of firms presently.

Second, tax policy can be considered as successful one. The VAT law has positive impact on private firm management. The Law regulates strictly on tax invoice so that firms have to register for business and tax code. This leads to the increase in the number of registered firm during 2000s. The Corporate Income Law and the tax incentive policies regulated in the Law on Domestic Investment Promotion stimulate the private firms. The reasonable tax rate and tax incentives make firms being better off if they register officially. As a result, this increases the state revenue from private sector.

Third is the credit policy. Due to the banking reform, it is easier for the private sector to access to the bank credit. The discrimination between private and state sector has been reducing. The confidence of banks in the solvency of the private firms increases.

4.2. Ineffective policies

Land policy is the most ineffective one. Presently, real estate market is frozen meanwhile many firms do not have site to do business. There are many problems on land policies such as land clearance, land planning, removing the environmental polluted firms, land tax incentives, land use fees, rental fees and many others. Although, the Land Law (2003) is more detailed and relevant than previous laws, the land market is still out of State control, the transactions in an unofficial land market still account the majority of the total land transaction, no signal of zooming out.

Business supporting policies are not successful as well. Some policies have been issued to promote business development services. However, as analyzed above, these policies are infeasible, not detailed and inappropriate. Most beneficiaries of these policies are big firms, which in fact do not need the assistance from the State. Meanwhile, young firms, which are in need of the support are not benefited from the above policies. Most business development services are poorly developed, including consultation, training, information, marketing, product design, trade promotion.

In short, after 20 years of renovation, the private sector has been increasingly acknowledged and supported for development. However, the majorities of state supporting policies to this sector have been issued the ten recent years. These policies do contribute to the increasingly development of the private sector. Among five policies analyzed above, the administrative procedure reform for market entry is the most

¹⁰ Decree 57/1999/ND-CP guiding the implementation of Trade Law abolishes the requirement for export-import firms such as requirements on USD 200,000 working capital, employees graduated from International Trading University and fluent in English.

successful policy, tax and credit policies are successful to some extent. Land and business supporting policies are still problematic. However, it is certain that any policy has shortcoming. The more important is to point out the shortcoming of the policies and take additional actions to improve the policy effectiveness.

5. Policy recommendations

5.1. Market entry policy

- A firm name bank should be established so that investors can refer to when they establish a new firm. This will be helpful for investors and avoid the duplication in the firm name. Online application for business should be realized in order to save time for investors. Because investors need to come to the business registrar once when they receive the business registration certificate. This will save time on going to the registrar, especially in case their application profile need to be revised or supplemented.
- Firm registration regulations should be reformed to give more responsibilities to the investors on the information they provide. Registrar only certifies the right of doing business of new firms. Establishment of the national network will shorten down the time for business registration.
- The regulation on firm seal registration should be changed. Firms should allow make the seal by themselves. They are only requested to register the seal with the police before using it. This will save time for firms. Because the objective of seal registration is to avoid the duplication in seal with other enterprises.
- Finally, in order to push the development of the private sector, it is necessary to make a consistent change in many aspects from ideology, legal system, policies, to capacity, attitude and working method of the state management organizations. The main direction should be opening up to people, believing in people and protecting the legal and relevant benefits of the people.

5.2. Tax policy

State management organization on taxation should implement the following measures:

- Stakeholders should participate more during the process of making tax regulations and policies. People, especially firms should have their voice in drafting the tax regulation and policies. By doing that, regulations can reflect the common interest, including tax payers and state.
- Study on the abolishment of fixed rate tax scheme; allow firms to print tax invoice by themselves, in the future firms should also declare and pay tax by themselves.
- Ministry of Finance needs to implement well the tax reform agenda stipulated in the Decision 201/2004/QD-TTg dated 06/12/2004 of the Prime Minister on approval of agenda for tax system reform to 2010, including the following points:
 - o VAT: To 2008, VAT system should be improved by reducing the number of goods and services exempted from tax, applying one tax rate in order to assure

the equality in tax responsibility and ease the tax computation, improving the tax computation methodology and identifying the level of revenue to be taxed, being suitable with the international rule.

- Corporate income tax: To 2008, the tax should be improved by reducing tax rate, reducing tax exemption and reduction objects, unifying the tax rate and tax incentive among different ownership forms to push investment and create an equal playing field.
- Personal income tax: Issuing a personal income law, which widens the taxpayers, reducing the tax rate gap between the Vietnamese and foreigner.
- Tax management: Issuing the Tax Management Law, which regulates clearly the liabilities, responsibilities of the tax payers, tax state collector, and related individuals and organizations.

5.3. Credit Policy

The most urgent action is to strengthen the financial and banking system. Some following measures should be done:

- Increasing the information technology application in the banking system in Vietnam, especially computerizing and creating an internal information network of the whole banking system in order to improve performance, reduce risks. It helps to collect fast and reliable information on customers so that the banks can avoid making wrong decision and assist the banks in applying the new services.
- Training and increasing the capacity of the bank staff in project appraisal and at the same time formulating the project appraisal indicators, stimulating the consultation service of the bank on project formulation and loan so that firms could access to the bank credit.
- Popularizing the non-cash payment and auto-banking service.
- Establishing the mortgage registration system nationwide in order to be more convenient for firms and safer for the banks. The practice shows that loan assurance by valuable papers such as trade paper, bond, deposit certificate is convenient for both borrowers and lenders due to simple administrative procedure, fast, safe. By doing that, commercial banks do not need to care about the financial capacity of the borrowers instead they only need to look at the organizations, issuing that papers.
- Financial leasing service should be developed because this will help small firms to have capital for their production when they cannot access to the bank. Establishing and developing venture capital and debt company.

Program to assist capital for private firms: Presently, private firms are lacking of capital, State should establish the program to assist capital for private sector in Vietnam. This will provide capital assistances for business establishment and expansion.

For business establishment, the State will provide capital to establish a new firm through non-profit financial institutions. The financial institution will appraise the investment project based on several relevant criteria, including feasibility and efficiency. For example, State can provide a certain percentage of total investment under the form of

loan at 0% interest rate to establish a new firm. The firm will refund the loan after a certain period, e.g. 2 to 5 years or longer. To implement this policy, the State should stimulate localities to establish the investment fund. The central state budget and the local budget will provide the initial capital for the fund. Latter on, the Fund will mobilize capital from other sources. Beside, State will finance the interest and operational cost for this fund.

For assistance to expend the business, State will provide loan with low interest rate for private firms through commercial banks and compensate the interest rate for the banks. State should give the long and medium loan to firms because recently many private firms have to use short-term loan for long-term investment.

Based on the studies on the policies on SME in 15 EU countries (1994)¹¹, direct subsidy and subsidized loan policy plays an important role for establishing the new R&D based firms. Therefore, in Vietnam, Development Assistance Fund should not limit to provide loan and assist the investment projects in certain industries and areas as regulated in the Decree 106 of the Government on State Development Investment Credit, but rather expend also to assist the R&D based investment project.

- Credit Assurance Program: This program should be established. These aims at compensate for the loss of the banks when the borrowers (firms) cannot pay back their loan. However, based on the international experiences, some following issues should be paid enough attentions when establishing that program:
 - o The relationship between lenders and the person, who give the credit insurance, will play a decisive role for the program success.
 - o The success of the program can be assessed only after 5-7 years of operation, or even longer.
 - o Most program in the world insured 60% to 80% of total loan, some others insured 6 months of interest rate with the above ratio. Some regulated differently.
 - o Fund for the program can be from state budget, credit institutions, firms, individuals, or other domestic or international sources. The operational cost of the program should be covered partly by the state budget, interest from fund deposit at the bank, application and project appraisal fees. International experiences show that the program will be run well if it is funded from both state and non-state sources.
 - o The establishment credit insurance fund at local level as regulated by Decree 90/2001/ND-CP is an important measure and need to be implemented nation wide. This bases on the performance and financial situation of firms, not bases on the firm assets. This kind of Fund would help banks be more confident on firms and lend them more. This Fund also reduces administrative procedures to firms and shares with firms the risk.

5.4. Land policy

¹¹ Vu Quoc Tuan, Development of SMEs: International Experiences and Practices in Vietnam'

- In the short-term, the State should include the land value in the total asset of the organization, which is assigned land by state. The State should collect the land use fee, and should provide land compensation and assistance to the people, who have to return land to the State. Land price should be adjusted probably to ensure that no loss for state budget meanwhile the people would accept it.
- For long-term, land policies should focus on the following issues:
 - o Establish and complete the financial mechanism for real estate market. Direct, regulate and monitor the real estate market, enable all ownership forms to participate the market. Exploit and efficiently use the real estate, especially those owned by State. Mobilize at large the resources from land for development, industrialization and modernization.
 - o Improve the policy to mobilize fund for infrastructure development by land auction.
 - o State should take back the land assigned to organizations but not being used or misused.
 - o Doing well master planning of land use, call for investment in land publicly or organizing public land auction. Authorize provincial People Committee to rent the large size land out to firms so that firms do not have to wait for the decision from many organizations.
 - o Separate land renting from constructing the industrial, export or high-tech zones. By doing that, State can carry out the policies on giving investment preferential to firms, which do business in the zone.
 - o In order to develop the official real estate market, provinces and cities should establish the land management agencies, which are responsible for several tasks relating to the real estate market such as land registration, land rent, land auctions, etc.

5.5. Supporting policies to business development

Development of the business sector accelerated the development of the BDS. However, presently, regulations on the BDS are still lacking of. Therefore, the legal framework for this sector needs to be improved to push up the development of the BDS. Specifically:

- Revise or supplement regulations on business development service market such as Decree 87, Decree 90.
- Abolish the irrelevant barriers, which limit the demand for this kind of service. For example, deplete the irrelevant regulations on the expenditure on business development service. Provide tax incentive for suppliers of BDS.
- Increase the awareness on the benefits of using BDS: propagandize the benefits of the BDS through the conference, training courses, meeting of the associations, etc. to increase the awareness of the business community.
- Support to the suppliers of BDS: Government and donors should give more supports to BDS suppliers to strengthen their capacity, especially in the field of human resources, machines, technology, marketing skills.
- Annually, the Government should evaluate the capacity of the BDS suppliers based on the certain criteria. Based on the evaluation results, the Government will provide

assistance to some selected ones in order to improve their capacity to meet the demand, especially the demand of the SMEs.

- Issue the Decree on management and assistance of BDS in order to establish a set of mechanism to support stably and effectively the development of this service.
- Formulate the Strategy on the development of the BDS market for the SMEs in Vietnam. The Strategy should identify clearly the objective of developing the market, the growth rate of the market and the measures to promote the BDS market during 2006-2010 and the vision to 2020. Only by developing that strategy, the supports to SMEs would become more effective.
- The export award and subsidy program should be redesigned to be suitable with the international rules. Because, most export subsidy programs are against by many trading partners and they can be a reason for the lawsuits on dumping. Therefore, export award should not be a long-term measure. Vietnam should apply good policies, invest in infrastructure, and cut down transaction costs to create favorable conditions for export firms.

Development of the private sector in Vietnam is a long-term process. Many supporting policies to this sector have been issued for ten recent years. There are still shortcomings of the policies because “we are learning by doing”. In the future, the private sector in Vietnam will definitely develop fast and become an important engine for economic growth and development due to its dynamics and pressure from global economy. In this context, the supporting policies of the state should be improved to be a “midwife” for the development of the private sector in Vietnam./.