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State-Owned Enterprises and Equitization Policy

Determinants of Technical Efficiency

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Vietnam has unique pattern of historical economic development. After getting its independence, the government of Vietnam concentrated on infrastructure reconstruction and socio-economic development. Aimed at improving the living standard for the country, the government pushed up the industrialization and modernization process. Along with the industrialization process, it also established many State-owned Enterprises (SOEs) with the expectation that these enterprises become the leading sector for the development of the economy as a whole, making Vietnam an industrial economy.

Nevertheless, the industrialization and modernization of Vietnam in the past, although received heavy supports from other countries in the socialist system, started with a very low level of production technology. In many cases, the SOEs, although large, were the combination of many small SOEs. This type of establishment still existed during the period 1990-1992 when nearly hundred of State-owned Corporations were established. In addition, the management system before the implementation of renovation program in 1986, which is known as "Doi Moi" deteriorates the incentive systems for firms to enhance their competitiveness, and for employees and manager to improve their skill. Moreover, the import replacement strategy forced the government to spread its scarce capital across field of business in the economy. Consequently, none of the SOEs had enough capital to modernize their production technology and/or to implement the R&D activities in house.

Inefficiency in the operation of SOEs - the main player in the economy of Vietnam- ; inefficiency in the investment strategy of the government; the existence of the planning system that deteriorates an incentive system for firms and employees devoted themselves for economic development; backward production technology; and closed economy were some of the main problems that have made the economic development of Vietnam fell down. At the macro level, GDP growth rate fell from 16.8% in 1976 to minus 2.87% in 1980.

In 1986, the government of Vietnam announced its renovation program to bring Vietnam out of the under developed condition. This comprehensive program tackled not only the existing issues at the micro level but also the existing issues at the macro level. Moreover, through this program, the government gradually integrates the economy of Vietnam into the region and the world economy; encouraging foreign investors to do business in Vietnam; and with domestic enterprises, the government expects that they could adapt advanced technology from abroad.

Over the past 20 years of renovation, the government of Vietnam had brought the economy out of the poor conditions. Overall, the GDP growth rate of Vietnam, though fluctuated, increased to high level, which enabled the government to reach the target of doubling GDP in every ten-year period. At the macro level, the economy of Vietnam gradually shifting from an agriculture economy toward an industrial economy. From year 2002, the industrial sector became the largest contributor to the GDP of the economy. At the

micro level, the numbers of private and foreign enterprises continuously increase. As long as the number of SOEs gradually decreases under the SOE sector reform, the private enterprises become the main source that raise the total number of enterprises to 500.000 firms by the year 2010 as targeted.

With relation to the State-owned enterprise (SOE) sector, the government also implemented a series of policies toward their development. These policies reflected the efforts of government in enhancing the efficiencies of the SOE sector because from the government's viewpoint, these enterprises still play a key role in the course of economic development of Vietnam.

Making Vietnam a "modern-oriented industrialized country" by the year 2020 is an ambitious goal that the government announced in the "Ten-Year Socio-Economic Development Strategy 2001-2010". In order to accomplish these objectives, the government planned to accelerate the industrialization and modernization progress, which concentrates the development of certain key industries such as the machinery industry, IT industry, electronic industry and energy industries. The government of Vietnam also committed to promote the development of all economic sectors: the (SOE) sector, the non-state sector and the foreign investment sector.

For the development of every economic sector, the government of Vietnam created favorable business and legal environment. Many laws and decisions were implemented to treat every economic sector with justice. For example by the year 2005, the government promulgated Investment Law to regulate and to promote the investment activities of all enterprises, which is replacing the Foreign Investment Law and the Domestic Investment Promotion Law. In addition, the government also launched policies, which allowing the non-state sector to take the shares of the State-Owned Enterprises (SOEs) after equitization or a policy that allowing foreign enterprises to change their ownership before listing on the Stock Market in Vietnam.

Among these policies, SOE sector reform is one of the most important industrial policies currently. This time, the SOE sector reform takes the form of diversifying their ownership, which allowing not only managers and employees of the equitized enterprises but also private investors and foreign investors to take (buy) the shares of these firms. This policy re-allocate the resources of the economy, here is the capital, to the development of some specific enterprises (SOEs). Different from previous reforms, the SOE sector reform this time not only affects the development of SOE sector but also affects the development of the non-state sector as a large portion of SOEs after equitization moved into this sector. Moreover, this reform allows the government withdrawing their invested capital in these enterprises for the development of public sector.

These are some of the major policies, which the government of Vietnam implemented toward sustainable development. What is sustainable development; what are the determinants of sustainable development; whether the government of Vietnam, through its development strategy and through its industrial policies to promote the industrialization and the development of enterprises, can Vietnam sustains its economic development? These are the issues must be addressed.

Whether the SOE sector reform this time could strengthen their competitiveness and make them the leading role in economic development as it was expected. This thesis attempted to find the answers for these questions. The thesis is organizing as follows: Chapter I presents the historical economic development of Vietnam, focusing on the achievement during the past 20 years of renovation and the issues that Vietnam should address for sustain its economic development in the future. Chapter I also introduces the development of SOEs along with the SOE sector reform. Chapter II presents the theoretical foundation that justified government intervention in economic activities and laid down some important criteria to

evaluate such kind of interventions. Chapter III and IV will focus on the development of the SOEs in the economy in the context of SOE sector reform. Concretely, Chapter III presents the empirical results on the development of the SOEs after equitization in the manufacturing industry with relation to the problem of inefficiency. Chapter IV then examines the technical efficiency in these manufacturing SOEs and identifies the determinants of technical efficiency enhancement.

The estimation results in chapter III are again raising the question of sustainable development for the economy of Vietnam in the future. Over the past 6 years (2000-2006), the TFP growth rate of the manufacturing sector as a whole and of the SOE sector in particular were fluctuated and were stayed at the low levels. This may raise the question on the feasibility of industrialization and sustainable development of the economy and the leading role of the SOE sector as targeted by the government.

At the industry level, the SOE sector reform this time not only affects the development of SOEs in the SOE sector but also affects the development of the non-state sector. Because the speed of SOEs equitzation is still slow, we are unable to get a clear picture on the impacts of SOEs reform to the development of the non-state sector. The pattern of influences to the development of the manufacturing industry swung between negative and positive during the examined period 2001-2006.

Nevertheless, a proportion of SOEs after equitization themselves achieved a high level of technical efficiency in the empirical analysis at the firm's level using 2006 data, which presented in chapter IV. This implies that the SOE sector reform has a positive toward the development of the SOEs after equitization and that the efficiency enhancement in the after equitization enterprises does not depends on their classification of ownership.

Also, the empirical analysis in chapter IV finds that technical inefficiency level still account for a large proportion compared with the variation of the white noise, which means that these firms still have a chance to enhance their technical efficiency.

This thesis also finds out that labor skill and management skill play important roles in the process of enhancing technical efficiency, especially, much attention should focused on the skill of the labor as they engage directly in the production process. In addition, the empirical result shows that corporate income tax exemption policy did not bring the results as the government expected. The indirect policy already ended by the year 2007. Nevertheless, the government should also review the document that govern the process of SOE sector reform, replacing the corporate tax exemption policy by other polices that promoting the R&D activities, in-house training and technical training.

Although there still have some restrictions, I hope that the results of this thesis not only help policy markers overview the effects of a specific policy implemented before but also provide them some important factors that they have to address if they want to improve the technical efficiency of enterprises in the future.