APPENDIX-B

REFORMS FOR ACCELERATED INDUSTRIAL DEVELOPMENT

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REFORMS FOR ACCELERATED INDUSTRIAL DEVELOPMENT

B.1 Lessons Provided for New Stage of Renovation

1) New Stage of Renovation in Vietnam

In 1986, Vietnam adopted the "Doi Moi" and decided to transfer from the centrally planned pricing system to the market-oriented system by opening the doors to other countries for trade and investments. The country has suppressed a hyper inflation and succeeded in keeping a stable rate of foreign exchange. By 1994, these great efforts brought economic stability and steady growth and the country intended to step into a new stage of renovation in which the reform of state-owned enterprises and accelerated growth of economy should be emphasized.

In general, transition of the regime from a centralized planning regime to a market based system could be divided into several steps as shown below:

a) Establishing definite rules
b) Establishing a new legal system and administrative system
c) Keeping macro economic balance and resolution of social conflicts
d) Promoting privatization of state owned enterprises
e) Effective usage of market function (encouraging contestability)
f) Encouraging foreign trade (export promotion and keeping balance of international payment)
g) Establishing taxation, saving, banking and financing systems (including rationalization of the government budget system)

Vietnam is at the moment stepping into stages "d", "e", "f" and "g" in 1995. Although there still remain issues to be improved even in earlier stages and social conflicts caused in the transition process have not been resolved yet, major problems to be resolved could be on and after step "d" mentioned above.

In order to get effective measures to overcome problems in the coming stage of "Doi Moi", experiences in industrialized economies, those of East Asian Economies including four dragons in particular, and also experiences in transient economies such as Hungary, Czech Republic and China would be helpful.

2) Major Factors for Economic Development of Asian Economies

(1) Economic Achievement of Selected Asian Countries

The economic achievement of the Eastern or Southeastern Asian countries has attracted worldwide attention in recent years. In Table B.01, population, GDP per capita and average growth rate of GDP of selected countries and groups are indicated. The "East Asia & Pacific" region with a population accounting for 31% of the world population, recorded a higher average growth rate of GDP and GDP per capita, 7.7 % and 6.1% respectively, than other groups of countries in the period of 1980-1992 (illustrated in Table B.02). It is noted that the growth rates of GDP and GDP per capita of such Asian countries as Republic of Korea, China, Thailand, Hong Kong, Singapore, Malaysia and Indonesia was relatively higher than other countries in both the periods of 1970-1980 and 1980-1992 (see Table B.03 and Table B.04). This superior economic performance attracts the worldwide attention to the Asian Region.

(2) Industrial Development as a Factor of the Economic Growth

Table B.05 and Figure B.1 show that the rapid growth of Asian counties has been achieved through industrialization. Capital and human resources have been invested into the industrial sector in these growing economies. Agriculture was the dominant sector of the structure of GDP in the early stage of economic growth, but the industrial sector gained a superior ratio in the growing process. The sectoral structure has gradually inclined toward the services sector in the mature stage of development. Before industrialization, and even in the stage of pre-industrialization, the economy has earned foreign exchange through exports of natural resources or primary products of agriculture, forestry or fishery. Foreign exchange could be appropriated for imports of manufactured goods. In the initial stage of industrialization, promotion of resource-based industries and promotion of domestic market-oriented industries have been emphasized in order to reduce losses of international payments. Many industrialized economies had experienced import substitution strategy. Although this strategy was effective to encourage domestic industries, it sometimes prevents them from strengthening the competitiveness in the world market. The experience implies that it is important to combine the improvement of efficiency of domestic industries by inducing advanced technologies and establishing an efficient management system. The most effective measure in this respect is to keep stimulating the competition among enterprises. Through competition, domestic industries will be strengthened and the ability to export their products will be improved.

(3) Macro Economic Stability and Confidence in the Government Policy

Stability of commodity prices, interest rates, wage and salary, foreign exchange rate and custom duties, as well as consistent and transparent government policies, is the most important condition for economic development of a country. Stability is mostly dependent on political stability which greatly affects business activities, investments in particular. Experiences in Asian Economies proved the importance of macro-economic stability, political stability and consistency of government policies. Since Vietnam has overcome hyper inflation in a relatively short time, and has kept exchange rates of currencies stable, foreign investors have been interested in business in Vietnam. The macro-economic and political stability and consistency of policies seem to be a fundamental condition for the economic and industrial development in Vietnam.

(4) Educated Human Resources

The World Bank's Report, titled "THE EAST ASIAN MIRACLE" has emphasized the importance of education as a condition for the success of industrialization in the High Performing Asian Economies. As shown in the last column of Table B.05, the adult illiteracy rate in low-income economies is higher than that in middle- and high-income economies. It should be noted that the illiteracy rate in such Asian Countries as Thailand (7%) and the Philippines (10%) is low even though they are classified in the lower-middle income economies. The illiteracy rate in Hong Kong, Singapore and Korea is less than 5 per cent. The low illiteracy rate has greatly contributed to the industrialization of these economies. Vietnam has a favorable level of illiteracy for accelerating industrial development, particularly for improving industrial productivity.

(5) Higher Saving Rate and Increasing Capital Resources

The governments of the High Performing Asian Economies encouraged savings by various measures. A cyclical relation between the increase in income and the high rate of saving has been realized by the better management of prices and interest rates. If prices are unstable and exceed the interest rate for deposit, people would not like to make deposit. In the High Performing Asian Economies, the interest rate has been kept stable and exceeded the rate of price escalation. Higher savings have greatly contributed to the industrialization in these economies by providing entrepreneurs with large capital to invest. Economic growth, high rate of savings and capital investments into the industrial sector have worked well in these countries. In Vietnam, the level of savings and capital accumulation is still low to accelerate the industrial development.

(6) Foreign Investments and Advanced Technologies

The High Performing Asian Economies have made great efforts to induce modern technologies and to catch up with the advanced economies. In the initial stage of industrialization, the governments of High Performing Asian Economies imposed strict restrictions to economize the use of foreign exchange, but they gradually relaxed the restrictions on foreign exchange for inducing modern machine & equipment and knowledge for industrial production. They have also granted favorable taxation on investments in modern technology and adopted a relatively low level of corporate tax. These measures made it possible for enterprises in High Performing Asian Economies to increase their internal reserves for new investments. The reserves have been utilized to invite foreign investments from advanced countries. Foreign investors brought markets, jobs and income opportunities, know-how on management systems and innovative production system of enterprises into the High Performing Asian Economies.

(7) Export-oriented Policy Mix

Domestic enterprises were highly motivated to absorb foreign technologies and know-how and competed each other in selling their products to the world market. Even though the strategic measures by the Government to promote exports should be supplementary, promotional privileges for export industries have been indispensable for industrializing economies. Further, the High Performing Asian Economies have organized institutional facilities to open up foreign markets for exports. In Table B.06 and B.07, growth rates of merchandise exports during 1970-1980 and 1980-1992 are shown by selected countries. There are 7 countries which attained a growth rate of exports of more than 10%. It is noted that 4 of them are Asian countries. It is obvious that exports played a significant role in the economic and industrial growth of these countries.

(8) Industrial Development Policy

The Asian system of economic management by the governments emphasizes the continuation and growth of enterprises. The governments of the High Performing Asian Economies have provided enterprises in specific fields of industry with such privileges and incentives as listed below in order to establish a favorable industrial structure.

- accelerated depreciation for specific capital investments in promoted industries
- favorable long-term and low interest financing for specific industries

- applying the foreign trade insurance to specific exports
- allowing preferential interest rates to specific subjects
- supplying government subsidies to specific areas of research and development
- construction of such basic infrastructure as ports, airports, water works, etc. by the government
- imposing protective tariff on the imports of commodities which compete with specific products
- tax exemption on specific industries which have been categorized under the industrial development promotion policy

3) Lessons from Transitional Reform Experiments in China and Middle Europe

(1) Lessons from Reforms in China

a) Reform of Agricultural Sector in the Early Stage of Renovation

China started its renovation scheme in 1978, or more practically in 1984 when 4 Special Economic Zones were designated to open doors to the world markets and to induce foreign investments, particularly export-oriented investments. In the early stage of renovation, attention has been paid to the economic reform in the agricultural sector to encourage food production and to increase income of farm households. Production units have been transformed from collective units to individual households and farmers have been allowed to sell their surplus products. At the same time, price control by the government was partly relaxed. These reforms brought three major effects on the growth of national economy. Firstly, it expanded domestic markets for industrial products. Secondly, the improved efficiency in the agricultural sector brought surplus in labor supply to the industrial sector. Industries were able to employ these workers at relatively low wages. Thirdly, increased income of farm household brought the accumulation of capital. Surplus income of farmers was saved in banks or reinvested into local businesses. These effects resulted in a relatively high growth rate of economy. The averaged annual growth rate of real GNP was 9.0 % from 1978 to 1992.

b) Reform of State-Owned Enterprises in the Later Stage of Renovation

The third reform to accumulate capital through farm households has not been successfully managed by the government, and there was a great shortage in capital for accelerated industrial development. Therefore, the shortage of capital was filled by foreign investments and foreign aids. It means that China has to manage deficits in the invisible trade. The economic growth heavily dependent on foreign investments will result in spreading differences of job opportunities and income between stagnating rural areas and growing urban areas. China is now faced with these problems.

Reform of Chinese state-owned enterprises (SOEs) was partly experimented by giving autonomy to the selected SOEs in 1978, when "A Sum of Rules on Expanding Autonomy of Management of SOEs" was enacted. Experimental reform program was executed in around 6,600 SOEs. This rule was transformed into "Temporal Provision on Expanding Autonomy of SOEs" in 1984. Under this Provision, enterprises were entitled to have the autonomous right:

- to produce an extra volume to sell in the free market after accomplishing the target volume of products imposed by the government;
- to use surplus profits for specific objects (fund for developing new products, for welfare of employees and for paying bonuses) by definite shares, after paying an agreed amount to the government;
- to lease or sell idle properties to others;
- to recruit and fire employees.

c) Equitization of Large- and Medium-Size SOEs

In 1983, renovation was made for SOEs by applying a new tax system. Enterprises had to pay a profit tax at a rate of 55 %, and a definite ratio of profits after tax was paid to the government by applying the specific option which they would select among three alternatives. Remaining profits were allowed to be reserved by themselves. At the same time, the right to manage enterprises was separated from the ownership, and it was entrusted to individuals under contracts. In 1988, the Law of Enterprises was enacted to make clear the separation the management from the ownership.

In December 1993, the Company Law was promulgated. It enacted the rules to establish limited companies and stock companies. In 1994, the unified income tax was applied. This process implies that China stepped into the privatization of SOEs in the 1990s. The most important problem in the equitization of SOEs is in the right to refuse the quota system on the social obligation imposed by the government. Such quota have been imposed even to the privatized companies. Stock companies had been established under the cooperative management of companies by farmers in 1984. Stock markets were established in Shanghai in

1990 and in Shenzhen in 1991. However, the number of stock companies was only 3,261 at the end of 1993. The State is not active in promoting equitization of SOEs and prefer to reform gradually. The reasons are supposed to be as follows:

(i) The State maintains the public ownership of property in principle;
(ii) Valuation of state-owned property is difficult; and
(iii) The enterprises have insufficient knowledge and understanding of the laws and regulations

The ratio of share holding was reported as follows:

- by the State 33.8%
- by Enterprises 45.1%
- by Individuals 19.4%
- by Foreigners 1.6%

Such experiences of China will provide Vietnam with some important suggestions on industrial renovation.

(2) Lesson from Reforms in Middle & Eastern Europe

a) Contrast of Performances between Asian Transient and European Transient

The performances in Middle & Easter Europe are in striking contrast to the performance in China. Although these countries are trying to reform their regime from the centralized planned economic system to the market oriented economic system, their performances seem to be much slower than the Asian Transient Economies (see Table B.08). The major reasons for this contrast are supposed to be as follows:

(i) the different ratio of SOEs in the economy;
(ii) the strength of political governance by the Communist Party;
(iii) the geographical and cultural distance from the western market economies;
(iv) the difference of industrial structure, the weight of the agricultural sector in the economy in particula;
(v) the degree of autonomous right of economic units;
(vi) the dependency on the Soviet Union, on Russia in particular;
(vii) the length of period under the socialist regime.

Judging from these criteria, it appears that Asian transient economies including China and Vietnam have better conditions to readjust their economic system to the market-oriented economy. For instance, the share of the agricultural sector in working population was 71 % in 1978 in China, but it was only 14 % in 1985 in the Soviet Union. If there are plenty labor supplies from the agricultural sector, the private companies are able to recruit employees without difficulty. In such a situation, the employees of SOEs cannot refuse the reform of their operations. This is a major reason why Prof. Sacks insisted the necessity of a "shock therapy" in the economic reform of the former Soviet Union countries.

B.2 Basic Principles Toward New Reforms

1) Major Problems to be Overcome in the New Stage of Renovation

Although successful achievements of Vietnam in reforms in recent years must be appreciated, a series of problems remain on the way of further renovation, particularly for the new economic development through industrialization.

First of all, effective measures should be established to increase job opportunities. It is because the reduction of staff and workers in SOEs will be one of fundamental conditions for SOEs to raise their efficiency and to move into private companies. It is noted further that job opportunities should be increased in the industrial sector to encourage the raise of agricultural productivity by absorbing surplus population in the agricultural rural regions. In this sense, too, the promotion of foreign investments will play a significant role in the industrial development.

Secondly, measures should be promoted to increase sources of income. In order to increase income sources, diversification of the industrial structure will be required, and it should be achieved step by step. In this context, it is noted that a large size domestic consumer market will require a lot of consumer goods in Vietnam. To meet this requirement, Vietnam should develop a wide variety of products ranging from basic materials to complicated assembled products.

Thirdly, an effective system should be taken to transfer the income into the capital which will be used to invest into industrial activities and social infrastructure. Encouragement of savings will be an urgent issue to promote domestic investments and to reform SOEs into private companies. Consequently, the establishment of an efficient tax system and a reliable saving system should be accorded with higher priority in the coming stage of renovation.

Fourthly, efficient policy directions and management systems for industrial development should be established, including administrative reform and improvement of legal settings. The export promotion strategy should be combined with the import substitution strategy, and the measures for foreign investment promotion should be synthesized with the measures to promote domestic investment. Technology transfer will play a role of mediator between foreign investors and domestic enterprises. Further, the industrial development policy should be positively supported by the trade policy.

Finally, the management of social conflicts has been at stake. Social conflicts are in relation to the shift toward a market-oriented economy. The phenomena of these social ills are reported in a publication, saying that:

> " Social ills, like smuggling, bribery, corruption and prostitution, are on the increase. The gap between rich and poor is widening. Greed and selfishness has reared its ugly head -- at a time when many Vietnamese families are most in need, even starving. The people are undergoing dramatic shifts not only in their economy but in long established attitudes towards the broader society."

2) "Shock Therapy" or "Gradualism" ?

In legal terms, privatization could be achieved by shifting ownership from the state to the private sector. However, the substantial reform will start thereafter in terms of economic system. Three processes of shifting from the state to the private sector could be assumed as follows:

(i) Selling the state-owned property to private enterprises ("Shock Therapy" or "Big Bang");

(ii) Shifting a part of the state-owned property to private enterprises, and recruiting private owners or partners who have interest and ability to manage that property afterwards ("Gradualism");

(iii) Shifting the state-owned enterprises into stock companies, but the State keeps whole or the majority of shares in the initial stage, and shares shall be gradually sold to private investors ("Two-Step Reform").

China adopted the second process. Russia and Poland adopted the first process. Hungary and Czech adopted the third process after the establishment of the State Property Agency (SPA) in March 1990.

"Two-Step Reform" contains four different methods of how to sell or allocate shares in the later stage of reform; (a) selling a part of shares to investors; (b) allocating the majority of shares to employees and staffs (called "Management Buy Out: MBO or Employee Buy Out: EBO); (c) allocating shares to the people (by "Voucher" or "Coupon"); and (d) listing shares in the stock markets. Czech Republic adopted the "Voucher" method.

Each economy is responsible for the selection of the most adequate method of privatization of SOEs by taking unique characteristics and conditions of each economy into consideration. The most of transient economies which adopted "Shock Therapy" still remain in disorder or chaos like Russia. They have huge difficulties to recover their economy. In the case of Vietnam, it would be better to adopt a gradual process or a two-step process, because a long term learning process will be required to shift the economic system from the centralized planning system to the market oriented system. It will be possible to make the transitional process more efficient by modeling after the experiences and successful methods in the advanced economies. However, a long period will be required for the people to learn and accustom themselves to the market economy. There must be a process of learning, trying, and experimenting. A "Shock Therapy" or "Big Bang" strategy in which these learning processes are left out, seems to produce social disorder. It would be important to prevent the emergence of social vacuum.

B.3 State Enterprise Reform

1) Background of Reform

Before the Economic Renovation Policy was adopted in 1986, the Ministries were fully responsible for the control and management of all the centrally controlled SOEs, and local governments (People's Committees) were responsible for the administration of locally controlled SOEs. Namely:

i) The Ministries and People's Committees (Ministries and Committees) kept the ownership of the land used by SOEs;

ii) The Ministries and Committees owned the buildings and machinery of the factories;

iii) The Ministries and Committees took full responsibilities for the management of SOEs;

iv) The Ministries and Committees gave orders on product mix, volume of production, prices of products, raw materials, etc. in line with the instruction of SPC;

v) Investment fund as well as operating fund were provided by the Ministries and Committees out of their budgets;

vi) Operating surplus was given to the Ministries and Committees; and

vii) Deficit, if any, it was met by subsidy from the Ministries and Committees.

Without strong incentives, production efficiency of SOEs was low in many cases, resulting in deficit to be filled up by the Government's subsidies which gave big financial burden to the Government.

As of 1990, there existed about 12,000 SOEs in Vietnam, of which about 3,000 large and medium scale enterprises were centrally controlled under the jurisdiction of the Central Government (22 Ministries), and about 9,000 medium to small scale enterprises were locally controlled under the jurisdiction of provincial and district governments. 12,000 state enterprises accounted for 24% of GDP and about half of the value-added of the industry and commerce sectors. Employing about 2.1 million workers, SOEs accounted for about 7% of the country's employed work force. Of the total number of SOEs in Vietnam, 2,762 SOEs are in the industry sector, which employed about 24.7% of the total employment in SOEs. Though the scale of economic activities of SOEs is significant, their financial performance was not satisfactory. About 20% of the centrally controlled SOEs and 60% of locally controlled SOEs were loss-makers, giving financial burden to the Government.

2) Progress of State Enterprise Reform and Equitization/Privatization

(1) Reform principles

In 1988, the Government focused its attention on restructuring SOEs, adopting the following principles: (i) elimination of operating subsidies to SOEs, (ii) expansion of enterprise autonomy, and (iii) exposure of SOEs to market forces in a competitive environment, including equal tax treatment for state and private enterprises.

In 1989, SOEs are given authority for: (i) adjusting product mix, (ii) procuring inputs and market outputs, (iii) introducing new technologies, (iv) hiring and firing employees, (v) setting wages and benefits in agreement with the Ministry of Labor, and (vi) allocating after-tax profits.

(2) Re-registration of SOEs

Re-registration started in 1991, including most of SOEs and Unions/Corporations. SPC was responsible for the evaluation of the applications for registration submitted by SOEs and Unions. SPC was also responsible for making recommendations to a high level council for final decision. Qualifying criteria for SOEs are: (i) existence of demand for their products, (ii) ability to preserve capital, (iii) ability to repay debts, (iv) no adverse environmental impacts, (v) clarity of ownership of assets including land use rights.

In case of unions/corporations, they must have: (i) at least, 5 SOE members with technological and commercial linkages, (ii) minimum legal capital of 500 billion dongs, (iii) an integrated accounting system or a system for consolidating the members' financial statements, (iv) a supporting feasibility study to show the viability of the corporation, (v) an organizational plan including personnel requirements, and (vi) a set of operational and organizational regulations approved by the ministries or provincial authorities.

Re-registration process was divided into two (2) phases, 1st phase from November. 1991 through March 1993 and 2nd phase from April 1993 through the end of 1994. During the 1st phase, 11,000 SOEs were examined out of total 12,000 SOEs. 2,000 inefficient and chronic loss-making ones, mostly in small-scale, were liquidated whose assets accounted for about 4% of the total assets of SOEs. 3,000 poorly performing SOEs were merged with other SOEs. The remaining 6,051 SOEs have been re-registered, of which 1,861 were centrally controlled and 4,190 locally controlled. Out of 6,051, SOEs with less than 500 employees accounted for about 90%, indicating that the average size remains small. There exist 300 medium and large-scale well-run SOEs, or about 5% of 6,051, which accounts for about 80% of the total contribution of the state enterprise sector to the budget in 1993.

The 2nd phase was for the remaining 1,000 SOEs yet to go through re-registration process and unions/corporations as well as for the loss-making strategic SOEs, initiated by the Prime Minister's Decision 90 issued in March 1994. The process should be completed by the end of 1994. According to SPC's classification, unions are classified as follows:

Classification	Process and Deadline
Viable	Registered by Sept. 30, 1994
Non-viable but important	Restructured and re-registered by Dec. 31, 1994
Primarily administrative	Liquidated or merged with other unions or SOEs by Sept. 30, 1994

In the case they fail to comply with the requirements, they must cease their operation.

Estimated Resource Flows between Government and the State Enterprise in 1991

(in billion of current dongs)

Government Revenues from SOEs		Government Expenditures on SOEs	
State enterprises:		Working capital credit subsidy	726.2
- Taxes and transfers	1,895	Investment credit subsidy	403.7
- Depreciation	1,085	Investment grants	389.0
Bank deposits /a:	85	Retained depreciation	600.0
		Amortization	100.0
		Government severance expenditure	100.0
Total	3,065	Total	2,318.9
Memo item: budgeted foreign assistance to SOE investments			(640.0)

/a : Estimated imputed bank income from deposits of enterprises in the government owned banking system, held at regulated interest rates below the estimated market deposit rate for short-term (3 month) deposits.

Source : Ministry of Finance, commercial bank balance sheets, and staff estimates.

As shown in the above table, it is clear that the recent reforms introduced to improve performance of SOEs have a considerable impact on the cost structure of

SOEs. Performance of the large, centrally owned, and export-oriented state enterprises seems to have been fairly good. However, the majority of provincial state enterprises were poorly performing and contributed little to the government revenues. As a result of government credit subsidies through the commercial banks, the net revenue flow from the state enterprise sector as a whole to the Government has been quite small.

(3) State enterprise debts

SOEs are largely dependent on the finance by state-owned commercial banks (SOCB), namely 92% of SOEs' credits were financed by SOCBs as of the end of 1993. In the case of the Bank of Investment and Development of Viet Nam (BIDV) and Vietcombank, the share of SOEs in their total credits was over 90%, and it was 67% for Incombank, 32% for Agribank and 52% for Non-SOCBs.

Non-performing assets in relation to SOEs are quite sizable. The assets of the banking system on account of SOEs are estimated at about 1.6 trillion dongs at the end of 1993. The non-performing assets of SOEs accounted for nearly 60% of the capital and reserves of the banking system and well over 75% of the capital and reserve of the SOCBs.

Recognizing the seriousness of the problem, the Government set up a National Debt Resolution Committee (DRC) in March 1991 to settle all debts of economic units and organizations to improve the financial relations and credits of SOEs with the banking system. This exercise has been proceeding in two phases. In the first phase, the DRC has established a matrix of inter-firm debt as of April 1991, which indicates that gross inter-firm debt stood at nearly 10 trillion dongs as of that date. The second phase of the exercise, which started in August 1992, deals with the debt resolution problems of enterprises which are unable to service their debt because of operational difficulties or because operations have ceased. This phase is proceeding more slowly, partly because some of the recorded debt is under dispute and is being resolved on a case-by-case basis. The DRC data also provide evidence of the potential bad debt problems facing the SOCBs, either directly or indirectly: SOCB claims on bankrupt enterprises represent 895 billion dongs that are unlikely to be recovered; claims of other economic agents on bankrupt enterprises amount to well over 2 trillion dongs, and are unlikely to be settled in their entirety. Unrecoverable inter-firm arrears could set up a chain reaction of defaults that could well feed back into the banking system. It should be noted that the above figures relate to the debt situation as of 1991; the situation today could very well be worse.

(4) Progress in the industrial sector

Due to the efforts of the Government and concerned entities, certain progress has been recorded with regard to the reform of SOEs. However, up to now small-scale SOEs, mainly locally controlled ones, were targets for reform, and the major reform for the medium and large-scale SOEs are yet to be implemented. In the industrial sector, 2,030 SOEs were in operation, of which 522 were centrally controlled and 1,508 were locally controlled as of 1993. Gross output value generated by SOEs accounted for 71.7% of the total industrial output in the country in the same year. As of July 1993, about 706,000 workers or 23.8% of the total labor force in the industrial sector were working in the state enterprises.

(5) Achievements of pilot equitization program

Under the name of "State Enterprise Reform Project", the pilot program for equitization was initiated in April 1993. As of June 1995 with the scheduled completion at the end of the year, only three (3) SOEs have succeeded in equitization out of the listed 21 as given below.

i) REE (Refrigeration Electrical Engineering Corporation)
ii) Hiep An Joint - Stock Company
iii) General Forwarding & Agency Company

All the above 3 are located in Ho Chi Minh City. REE and Hiep An fall under the manufacturing sector while General Forwarding & Agency is classified into the services sector.

The common factors lending to their success may be

i) Being medium- to small-scale enterprises with several or several tens of billions of dongs of capital and several tens to several hundreds of employees;
ii) Making profits at the time of being SOE and having business prospects.
iii) Having rather small outstanding debts;
iv) The general directors took initiative for the equitization and the idea was also agreeable to the employees;
v) Coordination between the central and local authorities was successful.

The case of LEGAMEX, which has been unsuccessful in equitization, is rather peculiar. For equitization, the enterprise was divided into 2 sections: garment and footwear and the first trial for equitization was made for the garment section. In the first stage, 1 million dollar worth shares were sold to employees, banks, financial corporations and private enterprises. Employees bought shares by means of retirement money (retirement money of one month salary equivalent per 1 year of work). However, just before the shareholders' meeting, equitization was canceled and money was returned. Presumably, the failure is attributable to: (i) large amount of debts to Comecon Bank, (ii) rumour that the evaluation of assets was not correct, and (iii) LEGAMEX is a local SOE, while the pilot equitization program has been promoted under the Central Government (MOF), resulting in inadequate coordination between the two governments.

3) Direction of Improvement

Considering the current situation and problems encountered during the process of the state enterprise reform and equitization, the following actions may be advisable to be implemented toward the acceleration of the reform activities. Overall acceleration process for enterprises reform and equitization/privatization is shown in Figure B.2.

(1) Clear demarcation between strategic and non-strategic sectors

Clear demarcation of strategic sectors and the non-strategic ones should be made and announced by the Government. In the strategic sectors, the public sector continues to play a leading role, keeping the Government's share in capital more than 50%, or 100% for certain cases.

It is understood that the following categorization is tentatively recognized by the Government at the moment:

(a) Category 1: Non-equitization (Government full control)

SOEs engaged in the basic infrastructure, including railway, public transport, port, telecommunications, airport, and electricity, shall not be equitized (Government holding 100% of their capitals).

(b) Category 2: Minor equitization (Government control)

SOEs engaged in the key industries including steel, cement, chemical fertilizer, ore mining, oil and gas exploitation, and those which make big contribution to the state revenue including tobacco and alcohol shall be partially equitized (Government's share exceeding 50% of the capital).

(c) Category 3: Equitization (Autonomous)

SOEs other than these in Category 1 and Category 2 shall be equitized. Government's capital share should be less than 50% and the enterprises should be accorded full autonomy.

The categorization should be finalized as early as possible and adopted as a firm and long-standing government policy. For some categories, a clear time table for the transference to the private sector should be formulated.

Industrial activities may be categorized into the following 6 groups:

(i) "Market failure" group, where the optimum allocation of resources cannot be attained even with the perfectly competitive market. In This group will include (i) defense and police, (ii) education, and (iii) health care.

(ii) Infrastructure group, including roads/bridges, port and airport and railway.

(iii) Public utilities group, including water and power supply.

(iv) Energy group, including the exploitation of oil, gas and coal.

(v) Basic industry group, including steel, petro-chemical, cement and chemical fertilizer industries.

(vi) Other industry group

Among the above, the first category in principle belongs to the public sector. The second and third categories are also generally handled by the public sector but under certain conditions they can be handled by the private sector or by joint efforts of the public and private sectors, including BOT (Build, operate and transfer) projects. The fourth, fifth and sixth categories are generally handled by the private sector.

In principle, direct production activities not classified as public utilities, i.e., fourth and fifth groups, are recommended to be transferred to the private sector. Considering the big contribution of the energy sector, particularly oil, to the Government revenue and hard currency earnings, however, transference may be considered in longer perspective.

Possibility and appropriateness of the transference of public utilities sector to the private, either partly or wholly, should be studied in the middle to long-term perspective. Infrastructures should basically remain in the public sector but certain private participation should be considered including BOT projects. Basic industries should be transferred to the private sector to achieve maximum economic efficiency under the market economy mechanism.

(2) Monitoring of state controlled enterprises

A State Enterprise Law to govern these strategic enterprises, which would continue to receive the Government support, should be enacted stipulating clearly the extent of autonomy as well as the degree and manner of Government control. A central agency should be nominated to assume the responsibility of monitoring these enterprises in order to secure administrative efficiency.

(3) Equitization/privatization of SOEs

The success of the equitization is a key to the smooth shift to the market economy. In the industry sector, prompt equitization of SOEs is a pre-requisite for the early take-off of an industrialized country. In order to accelerate the equitization process, the following actions may be advisable to be implemented. Possible flow for equitization of state enterprises is shown in Figure B.3.

(a) Settlement of unemployment issue

Generation of unemployment is one of the biggest problem hindering the progress of the equitization. In order to overcome the difficulty, the following measures are recommended to be taken:

i) To promote retirement of employees including early retirement by bearing a sizable portion of the retirement allowance by the Government,

ii) To provide financial incentives including preferential tax treatment to the enterprises, either public or private firms, which employ the unemployed workers dismissed from SOEs,

iii) To establish a placement system with job placement offices storing information about job offers and applications covering both SOEs and the private firms which should cover the whole country in the long run with a computer-aided network,

iv) To take necessary actions including the development of required regulations including the right of use of land and sale thereof in order to secure the mobility of labor between rural and urban areas and between the industrial sectors, particularly agriculture and industry.

If necessary actions are taken, significance of labor issues associated with the equitization would be lowered, considering the expected rapid growth of economy, large absorption capacity of the non-state sector, particularly agriculture, trade and industry sectors which together provided 1,557,000 new jobs within two years in 1989-1990 period as well as relatively small labor force in SOEs which was 3,083,000 or 10.7% of the country's total employment.

(b) Enhancement of equitization fund

Another major problem to be solved for materializing the equitization of SOEs is the lack of fund for procuring the assets or purchasing the shares of the equitized enterprises. One countermeasure is to allow more active foreign participation in the equitization by amending the Foreign Investment Law, which currently allow only exceptional cases subject to the approval by the Prime Minister. If deemed necessary, certain constraints may be imposed on the share of the foreign investors. Another option is to allow subsidiary companies in Viet Nam of foreign investors to participate in the equitization of SOEs. Another measure is to actively utilize the existing lending system for the employees to purchase the shares of their own enterprises at the time of equitization by augmenting the budget allocation for this program.

(c) Enhancement of investment fund for the equitized SOEs

At present, all the revenue generated by selling shares of equitized enterprises goes into MOF and nothing would remain as internal reserve of the enterprises.

It is recommended that privatization (equitization) fund should be set up in order to give an incentive for equitization by extending soft loans to the equitized enterprises. Its fund should come from the revenue of selling shares of the equitized SOEs. Alternatively, a part or whole of the revenue of MOF generated through selling shares of a SOE may be lent to the SOE under preferential conditions.

Table A.12 Foreign Direct Investments by Region

(As of End 1994)

Region/Province	Number of Licenced Project	Share
North Mountainous and Midland	39	3.8%
Red River Delta	241	23.4%
Hanoi	(178)	(17.3%)
Hai Phong	(34)	(3.3%)
Ha Tay	(12)	(1.2%)
Hai Hung	(9)	(0.9%)
Thai Binh	(4)	(0.4%)
Nam Ha	(2)	(0.2%)
Ninh Binh	(2)	(0.2%)
North Central Coast	20	1.9%
South Central Coast	64	6.3%
Central Highland	22	2.1%
North East South	569	55.4%
Ho Chi Minh	(384)	(37.4%)
Song Be	(42)	(4.1%)
Tay Ninh	(6)	(0.6%)
Dong Nai	(102)	(9.9%)
Ba Ria - Vung Tau	(35)	(3.4%)
Mekong River Delta	49	4.8%
Oil Block	24	2.3%
Total:	1,028	100.0%

Source: SCCI

Table A.13 Number of State Manufacturing Enterprises in Hanoi Area

		Central State Enterprises			Local State Enterprises		
		Vietnam	Hanoi Area		Vietnam	Hanoi Area	
		(1)	Surveyed (2)	%	(1)	Surveyed (2)	%
31	Food, beverage	75	18	(24.0)	327	8	(2.4)
32	Textile, apparel	52	18	(34.6)	172	17	(9.9)
33	Wood products	19	9	(47.4)	96	2	(2.1)
34	Paper, printing	35	20	(57.1)	111	4	(3.6)
35	Chemicals	58	17	(29.3)	122	5	(4.1)
36	Non - metallic	15	11	(73.3)	39	6	(15.4)
37	Basic metal	20	-	(0.0)	19	1	(5.3)
38	Fabricated metal	153	58	(37.9)	245	26	(10.6)
39	Others	18	3	(16.7)	92	1	(1.1)
	Not classified	-	-	-	-	-	
	Total	445	154	(34.6)	1,223	70	(5.7)

(1) Numbers in 1993 (Source : Statistical Yearbook, 1994)

(2) Numbers replied to Questionnaire Survey in 1994,

Figures in ( ) indicates percentage against number of enterprises in Vietnam

Table A.14 Categories and Types of Existing Industries in the Hanoi Area

		Central State Enterprises	Local State Enterprises	Private Enterprises	Total
31	Food, beverage, tobacco	18	8	1	27
311	Food manuf.	9	4	-	13
312	Other food	4	-	-	4
313	Beverage	4	4	1	9
314	Tobacco	1	-	-	1
32	Textile, apparel and leather	18	17	2	37
321	Textile	6	5	-	11
322	Apparel	8	5	2	15
323	Leather	-	1	-	1
324	Footwear	4	6	-	10
33	Wood and wood products	9	2	4	15
331	Wood and wood products	7	2	4	13
332	Furniture	2	-	-	2
34	Paper and paper products	20	4	0	24
341	Paper and paper products	3	1	-	4
342	Printing and publishing	17	3	-	20
35	Chemicals	17	5	0	22
351	Industrial chemicals	2	1	-	3
352	Other chemical products	13	1	-	14
353	Petroleum refineries	-	-	-	-
354	Misc. products of petroleum	-	-	-	-
355	Rubber products	2	-	-	2
356	Plastic products	-	3	-	3
36	Non-metallic mineral	11	6	0	17
361	Pottery china	4	1	-	5
362	Glass	-	-	-	-
369	Other non-metallic	7	5	-	12
37	Basic metal	0	1	0	1
371	Iron and steel	-	-	-	-
372	Non- ferrous metal	-	1	-	1
38	Fabricated metal products	58	26	3	87
381	Fabricated metal	10	7	-	17
382	Machinery	20	4	-	24
383	Electrical machinery	12	4	2	18
384	Transport equipment	11	8	1	20
385	Other equipment	5	3	-	8
39	Other manufacturing industry	3	1	-	4
	Total	154	70	10	234

Source: Questionnaire Survey by JICA Study Team

Table A.15 Sales Amount by Categories and Types of Industry in the Hanoi Area

(1993, Billion Dong)

		Central State Enterprises	Local State Enterprises	Private Enterprises	Total
31	Food, beverage, tobacco	738.2	154.7	0.0	892.9
311	Food manuf.	171.3	56.5	-	227.8
312	Other food	29.0	-	-	29.0
313	Beverage	225.1	98.2	0.0	323.3
314	Tobacco	312.8	-	-	312.8
32	Textile, apparel and leather	505.5	118.0	10.2	633.7
321	Textile	372.8	53.0	-	425.8
322	Apparel	97.8	18.8	10.2	126.8
323	Leather	-	7.0	-	7.0
324	Footwear	34.9	39.2	-	74.1
33	Wood and wood products	38.7	1.9	10.8	51.4
331	Wood and wood products	35.9	1.9	10.8	48.6
332	Furniture	2.8	-	-	2.8
34	Paper and paper products	101.6	20.2	0.0	121.8
341	Paper and paper products	28.9	-	-	28.9
342	Printing and publishing	72.7	20.2	-	92.9
35	Chemicals	518.5	18.3	0.0	536.8
351	Industrial chemicals	43.7	1.8	-	45.5
352	Other chemical products	372.7	-	-	372.7
353	Petroleum refineries	-	-	-	-
354	Misc. products of petroleum	-	-	-	-
355	Rubber products	102.1	-	-	102.1
356	Plastic products	-	16.5	-	16.5
36	Non-metallic mineral	128.1	50.9	0.0	179.0
361	Pottery china	9.7	-	-	9.7
362	Glass	-	-	-	-
369	Other non-metallic	118.4	50.9	-	169.3
37	Basic metal	0.0	2.4	0.0	2.4
371	Iron and steel	-	-	-	-
372	Non- ferrous metal	-	2.4	-	2.4
38	Fabricated metal products	528.4	315.8	101.0	945.2
381	Fabricated metal	52.4	21.9	-	74.3
382	Machinery	121.5	151.8	-	273.3
383	Electrical machinery	261.3	102.8	98.0	462.1
384	Transport equipment	54.2	35.7	3.0	92.9
385	Other equipment	39.0	3.6	-	42.6
39	Other manufacturing industry	13.7	0.0	0.0	13.7
	Total	2,572.7	682.2	122.0	3,376.9

Source: Questionnaire Survey by JICA Study Team

Table A.16 Central State Enterprises in the Hanoi Area

		Nos. of Enterprises
01	Min. of Light Industry (MLI)	25
02	Min. of Heavy Industry (MHI)	17
03	Min. of Transportations	16
04	Min. of Defence	16
05	Min. of Agriculture and Food Stuff	10
06	Min. Construction	9
07	Min. of Culture	8
08	Min. of Medicine	6
09	Min. of Trade	4
10	Min. of Post and Communication	3
11	Min. of Education and Training	2
12	Min. of Labor	1
13	Min. of Finance	1
14	State Bank of Vietnam	1
15	Other Central Organization	26
	(Sub - Total)	145
06	Not Classified	9
	Total	154

Source: Questionnaire Survey by JICA Study Team

Table A.17 Founded Year by Types of Industries in the Hanoi Area

	Central State Enterprises	Local State Enterprises	Private Enterprises	Total
~ 1959	30	10	-	40
1960 ~ 1969	36	21	-	57
1970 ~ 1979	33	22	1	56
1980 ~ 1989	26	8	3	37
1990 ~	22	6	6	34
(Sub total)	147	67	10	224
Not classified	7	3	-	10
Total	154	70	10	234

Source: Questionnaire Survey by JICA Study Team

(4) Recent Development

a) Strengthening of banking regulation

In 1994, the foreign exchange regulations have been tightened as shown below:

- All dealings on goods sales and services in Vietnam must be conducted in Vietnamese currency
- All revenue in foreign currency by sales of exports and services abroad should be repatriated to Vietnam,
- Vietnamese organizations and citizens are not authorized to open accounts abroad; and
- All institutions and citizens having foreign currencies have to sell or deposit to and can buy or withdraw from authorized banks or the foreign exchange market.

However, the tightened foreign exchange regulation has not been strictly executed at this moment. As no foreign exchange control has been virtually existing in Vietnam, a significant amount of foreign exchanges has been circulating in the informal economy. Therefore, foreign exchange control should undoubtedly be strengthened in the medium or long term. However, imprudent execution of strict foreign exchange regulations would result in an out-flow of money from the official market to the informal market, as confidence in the banking system and in the government policy has not been established among the people in Vietnam.

b) Mortgage over land use right

As transfer of land use rights and creation of mortgages over land use rights were legalized by the Law on Land, enacted in 1993, banks are actually taking mortgages for land use rights.

In Vietnam, borrowings from banks are sometimes not possible for enterprises because of insufficient collateral available to them. This is the one of causes of financial difficulties for business activities in Vietnam. Therefore, enactment of the Law on Land will contribute to the solution of these financial difficulties in Vietnam. It should be noted, however, that creation of mortgages over land use rights by SOEs still needs specific permissions from relevant government authorities, and such cases are still not common.

2) Banks in Vietnam

(1) Types and numbers of banks

Since 1990, a series of legislation for establishment of share holding joint stock banks, joint venture banks, branches and representative offices of foreign banks have been enacted. Restrictions on the entry to the banking sector have been greatly liberalized, and the number of banks operating in Vietnam has increased significantly.

The types and numbers of banks operating in Vietnam are summarized in Table B.10. SOCBs accounted for almost 90% of commercial and investment banks operations in Vietnam in 1993. As shown in Table B.11, the assets of SOCBs are 91% of the total assets of the banks in Vietnam. The SOCBs' share in the banking revenue and net profit are 93% and 87%, respectively. In contrast to the size of the operation, the profitability and the capital/assets ratio of non-SOCBs are higher than those of SOCBs.

The roles of the four state-owned specialized banks in the banking activities are specified as follows:

Incombank	-	Banking operations in industrial, trade, service sectors
Agribank	-	Banking operations in agriculture, forestry and fishery sectors
Vietcombank	-	Banking operations in foreign exchange and foreign trade
IDBV	-	Financing medium- and long-term credits and investments for development of infrastructure and technological projects

(2) Financial performance of SOCBs

Certain financial analysis ratios of SOCBs are shown in Table B.12. However, it should be noted that financial figures may not correctly show the real financial position, because overdue accounts are not properly classified and bad debt provisions are not adequately provided because of lack of international accounting standards. The Government has given a consent to the World Bank for the auditing of SOCBs by an international audit firm. The audit will start in 1995. The real financial position would be revealed when this audit are completed.

a) Total assets

The size of banking operations is quite different among SOCBs. Vietcombank has the largest assets in the amount of 13,790 billion dongs in 1993, which is more than two time as large as those of IDBV.

b) Capital / assets ratio

IDBV showed the highest capital/assets ratio of about 10% in 1993. Vietcombank's ratio is only 3.8%, which is the lowest in SOCBs. Other SOCBs capital/assets ratios are around 5%. The capital/assets ratios of SOCBs are, though meeting the requirement stipulated by the Prudential Regulations as explained in the subsequent section, too low considering the magnitude of overdue accounts for which bad debt provisions are not provided.

c) Profitability

The most profitable bank is IDBV, whose net profit ratio was 39% in 1993. Agribank's net profit ratio is 0% or negative, and its profitability is the worst among SOCBs.

The Government's capital investment in IDBV contributed to their high profitability, as this capital contribution bears no financial costs. It is considered that Agribank's low profitability was caused by the delays of repayments from the farming sector because of crop failures.

3) Two Step Loans (On-lending Loans)

The banking systems and the Government claim that the fund for lending is insufficient and external assistance is required to acquire the fund for such on-lending. In this context, application of two-step loans (on-lending loans) has been studied, though on preliminary basis.

(1) Issues to be considered in designing the Two Step Loan

The following issues are to be considered in designing the Two-Step Loan ("the Loan") in Vietnam. The Loan is to be designed to contribute to the solution to the following key issues which the Vietnam economy is confronted with:

- Modernization of the management of enterprises and, especially, establishment of accounting standards and adoption thereof by the enterprises, is crucial for development of the industrial sectors in Vietnam.
- Further development of the State Enterprise Reform is very important for the development of the Vietnam economy, as SOEs are still producing more than 70% of the gross output of the industrial sector.
- Further promotion of foreign investments is needed for the industrial development of Vietnam.

- Shortage of funds, especially long-term funds, is one of the most serious constraints for the development of the industrial sectors in Vietnam. This issue is more serious for the private sectors and medium and small scale SOEs, because large-scale SOEs have more opportunities to obtain long-term loans.

(2) Outline of the Loan

The Loan should be considered as the first Step Loan out of serial loans sharing the same objectives. Therefore, the size of the Loan should be rather modest. Because of the pilot nature of the Loan, the target area for the refinancing of the Loan should be limited, say, to the Hanoi area. Then a post evaluation should be conducted in depth. After completion of the post-evaluation of the Loan, the second Two Step Loan will be provided in full scale.

The Loan should be provided for multiple purposes: (i) modernization of the management of enterprises, (ii) assistance in development of medium and small scale enterprises including private companies and SOEs, (iii) acceleration of the Reform of State Enterprises, (iv) relocation of plants to industrial estates, and (v) prevention of pollution and protection of the environment.

The economic useful life of machinery and equipment is usually 5 to 7 years. Therefore, the lending term of long-term loans should be 5 to 7 years. Interest rates of the Loan should be lower than the market interest rates to financially assist projects.

As the supply of long-term funds is insufficient in Vietnam, the Loan should provide long-term loans as well as working capital loans.

Foreign currency loans will be limited to import of equipment and materials and procurement of services from overseas. It should be noted that enterprises in Vietnam tend to prefer foreign currency borrowings simply because of the low interest, while exchange risks are left on the borrowers.

(3) Eligibility for borrowing loans

Enterprises meeting the following conditions are eligible for the Loan.

- Companies incorporated in accordance with the Company Law or SOEs assessed to be viable.
- Companies or SOEs which maintain accounting records in accordance with the modern accounting standards, at least, for one year the before start of appraisal of application.

- Privatized ex-SOEs should obtain priority for the Loan.
- Companies relocating from non-industrial areas to industrial areas and industrial estates should be given priority for the Loan.
- Financial position and profitability of an applicant company should be analyzed based on financial statements prepared in accordance with the accounting standards.
- Considering the importance of the foreign investments promotion in Vietnam, joint venture projects with foreign investors should not be excluded from the scope of the Loan.

(4) Three components of the Loan

The Loan should consist of three components. The first component should cover the costs associated with establishment of the base for modernization of management. These may include costs for: (i) establishment of accounting standards, and (ii) formation and utilization of specialist teams consisting of specialists in finance, management , accounting, etc. The second component should cover costs incurred in the hands of an individual company for adoption of the accounting standards, improvement of the book-keeping system, recruitment of proper staff, training of staff, computerization of the system, etc. The third component should be for the financing of to the project itself.

(5) Selection of executing bank

Incombank would be the most appropriate bank for the Loan for the reasons stated below. Financial statements of Incombank and IDBV are shown in Table B.13 and Table B.14, respectively.

- Incombank was established to provide credits to industrial, trade and service sectors and experienced in these areas, whereas IDBV was established as a development bank for financing and investment mainly in infrastructure and social sectors as seen in its financial statements,
- Incombank is already conducting two step loans funded by Taiwan and Germany, and has experience already in two step loans.
- Incombank has the head office and 6 branches in the Hanoi area, where the initial Loan is contemplated.
- "Deposits from customer", comprising 52% of the total liabilities, are the most significant funding source of Incombank. Therefore, the dependence on the Government may be relatively stronger than the other SOCBs.

4) Direction of Financial Reforms

Recommendations for the financial reforms are explained in this section. It is advised that reference is made to the diagram in Figure B.4, where inter-relationship of the recommended points is shown together with the effect of each recommendation.

(1) Increase of funds in the official financial market

One of the reasons for the shortage of funds in the financial market in Vietnam is that the bank savings mobilization is still inadequate and below its potential. It is said that the banking system serves only 7% of the population. A significant amount of private savings is not circulated in the official financial market. The size of the informal financial market is considered to be very large in Vietnam.

According to the research conducted jointly by SPC and UNIDO in 1994, the most significant financial asset held by the Vietnamese people is "Gold and U.S. dollar currency", whose share in the total financial assets held by the people is 47.5%, whereas the shares of "dong currency" and "bank deposits, shares and bonds (dong)" are only 10.1% and 12.2%, respectively. To increase funds circulating in the official market, by increasing bank savings mobilization, is definitely needed to solve the financial problems in Vietnam. The most fundamental approach to attain this goal is to enhance the confidence in the banking system among the people in Vietnam. Confidence in the banking system would be gradually enhanced by the following policy measures:

a) Government policies

The Vietnam economy experienced severe inflation many times in the past. The last hyper inflation just ceased in 1989 when the annual inflation rate became nearly 100%. Therefore, people are concerning about recurrence of inflation. This is one of the reasons for low bank savings mobilization in Vietnam. However, the Vietnam economy is recording very good performance in recent years, which is indicated by such economic indicators as relatively high growth rate, low inflation, stable dong, improvement of trade balance and reduction of deficit in the public finance. This economic success was brought by the sound economic policy adopted in the process of the economic reform, which was started in 1986 and accelerated in 1989. These recent economic success is gradually relieving the people's firmly-rooted distrust in the economy. However, it would still take some time to recover the full confidence in the economy.

Consistency and continuity of the current Government policies, including the sound economic policy, should be maintained to enhance the confidence in the economy and the financial market in Vietnam. This is the most essential condition to get in-flow of fund from the unofficial market to the official market. An example of the discontinuity of the government policy is the blocking of bank accounts and the change of bank notes, which took place twice after 1975. By these policy changes, the people's trust in the banking system was tremendously impaired. Continuity of the government policy should always be maintained.

b) Supervision of banking activities by SBVN

The current Prudential Regulations for banks stipulated by SBVN specify the following criteria:

- Lending limit- loans to a single customer shall not exceed 10% of capital and reserves of the bank
- Insider and connected parties-loans to insiders and connected parties shall not exceed 5 % of capital of the bank
- Equity participation- equity participation shall not exceed 10% of capital of the customer.
- Capital adequacy- capital / assets ratio shall be more than 5%

The Prudential Regulations are to be reinforced, and the following provisions should be included in the regulations:

Adoption of international banking accounting standards;

- Specific guideline concerning the loan classification and methods for provisioning for possible losses from overdue accounts.

In Vietnam, assessment and comparison of the financial performance of the banks cannot really be made until the international banking accounting standards are adopted. Considering the significance of overdue accounts held by banks, the minimum capital/assets ratio should also be significantly increased.

The supervisory function of SBVN should be reinforced to enhance the credibility of the banking system by strengthening the legal and regulatory framework including reinforcement of the Prudential Regulations, increasing independence in the monetary policy, and increasing well-trained staff of SBVN.

A "Bank Deposit Insurance System" should be established to protect small and medium size bank depositors from risks associated with failures of operation of banks.

c) Flexible banking instruments

The real issue in the financial market of Vietnam is that "Gold and U.S. dollar currency" are, as mentioned in the earlier paragraph, the most significant financial assets outside the official financial market. To increase funds in the official market is virtually to take these financial assets into the official market. Every effort to attain this goal should be made by the Government, including issuance of unregistered bond, as explained below:

The Vietnamese Government is now studying the issuance of bonds. In this context, the studies should be made on the points that (i) existence of the huge unofficial financial market is the reality in Vietnam, (ii) issuance of "unregistered bond", for which the name of holder is not registered, will be another practical approach to accelerate in-flow of money to the official market, (iii) people often hesitates to put their money in the official market, because their identity may be known and the source of fund may be detected, and (iv) considering the lack of confidence in the financial market among the Vietnamese people, the term of unregistered bonds should be rather short ranging from 3 month to 3 years.

d) Rectification of distorted interest rate structure

As mentioned in the earlier section, the current interest rate structure is still distorted. To resolve this distortion, the differentiation of deposit interest rates between households and economic units should be removed. Furthermore, interest rates for fixed capital loans should be set higher than those for working capital loans. Risks of fixed capital loans are considered to be greater than those of working capital loans, as the lending term of the former is longer than that of the latter. Therefore, interest rates on long-term loans should be higher than those on short-term loans. However, it should be noted that this inverted gap has become very small recently. For example, the average interest rate of long- and medium-term loans which was used to be 1.2% to 1.5%, was 1.7% per month in August 1994, and the average interest rate of short-term loans was 1.8% to 1.9% per month.

e) Abolishment of turnover tax

A Turnover Tax is currently imposed on banking activities in Vietnam. As shown below, the rates of the Turnover Tax on banks varies from 15% to 30% depending on the type of operation and bank. Agricultural banks are paying only 2%.

Agricultural banks and credit cooperatives	2%
Investment banks	15%
Foreign trade banks	30%
Industrial and commercial banks, financial companies and others	15%

The Turnover Tax is a cost factor for banking activity, and banks make their spread wider, by setting deposit interest rates lower and lending interest rates higher, to recoup the Turnover Tax cost. This "cost and pricing structure", made by imposition of the Turnover Tax, has bad impacts in two respects. Namely, lower deposit interest rates result in less mobilization of fund and, on the other hand, higher lending rates increase financial burden of the industrial sectors. Therefore, it is strongly recommended that the Turnover Tax be abolished immediately, or at least the tax rate be lowered and unified until it is abolished.

f) Unification of profit tax rate

The Profit Tax rate of SOCBs is 50% , while it is 25% for foreign branches and joint-venture banks. There are no reasonable grounds for differentiating Profit Tax rates between banks. The Profit Tax rate should be unified among banks.

g) Other measures

The Domestic Investment Law was recently enacted. One of the purposes of this law is to promote investment in business and inflow of funds from the informal market to the official market. Various regulations concerning business activities should be flexibly applied to promote domestic investment.

Foreign direct investment will certainly contribute, by equity and loan to projects, to increase domestic funds available in Vietnam. The existing policies and measures for promotion of foreign investment should be reviewed and, even, strengthened to accelerate implementation of foreign investment projects. Financial co-operation by foreign countries would be another very important source of funds for Vietnam, especially in the construction of infrastructure.

(2) "Institutional finance scheme" for development of the private sector

Approximately two thirds of bank credits were provided to SOEs in 1993, though this percentage reduced from about 90% in both 1991 and 1992 under the Government policy to direct more funds to the private sector. However, credits to the private sector still consist of primarily short-term loans for agriculture and commerce. Long-term lending is mainly provided by SOCBs, and long-term lending is still mostly directed to SOEs .

Under these financial conditions in Vietnam, private industrial sectors are suffering from serious shortage of funds, both short-term loans and especially medium- / long-term loans. Therefore, an "policy-based finance scheme" should be founded and organized by the Government initiative. The "policy-based finance scheme" would comprise the following two sub-schemes, namely "policy-based finance scheme" and "guarantee scheme".

a) "Policy-based finance scheme"

Creation of a lending scheme to provide loans to the private sector would significantly contribute to solution of the financial difficulties of the private sector in Vietnam. SOEs, which are being under the process of equitization, should also be eligible for this loan scheme to accelerate the development of equitization of SOEs. To satisfy quantitative necessity for fund of the private sector should be the first priority of this scheme. However, a qualitative necessity, such as a relatively low interest rate, longer lending term, is also to be satisfied. This lending scheme may be conducted by a governmental financial institution specially established for this scheme or a special lending scheme is designed and implemented through banks with fund provided by the Government.

As most of private sector companies have not sufficient mortgages to borrow funds from banks, a "guarantee scheme" organized by the Government for private sectors, will be an indispensable financial assistance for the private sector. It would be most appropriate that a governmental guarantee organization provide guarantee .

The real issue, associated with the aforementioned two financial schemes, will be how to obtain funds for these schemes. Though there would be no quick solution to this issue, reinforcement of the tax collection system would be surely a part of the solution to this issue. More fundamentally, the base of the Government revenue should be extended and fortified by centralization of revenues from activities of various central and local governmental entities, which are currently not collected in the budget of the Central Government. Political and government organization reform are prerequisites for the centralization of revenue.

b) Establishment of purposes and criteria for the institutional finance scheme

As the policy-based finance scheme involves artificial control and direction of fund, which is being the most scarce resource in Vietnam, toward particular business activities by the Government policy, the purposes of the policy-based finance schemes should be clearly identified in line with the overall industrial policy of Vietnam. Criteria, derived from the purposes, for obtaining fund or guarantee from the scheme should be clarified and publicly announced to secure fairness and transparency of the schemes.

(3) Improvement through State Enterprise Reform

The soundness of the real sector directly affects the financial performance of the banking sector. As SOEs are still dominant users of bank loans, further development of State Enterprise Reform is essential for improvement of the financial performance of the banks in Vietnam.

a) Development of equitization of SOEs

Inefficiency of management of SOEs is a consequence of the lack of competition in the centrally planned economy in the last few decades. Most of SOEs could not develop competitiveness and are not viable in the market economy. Equitization of SOEs is the most appropriate and fundamental approach to improve inefficient management of SOEs. Dissolution of certain SOEs should be admitted to be inevitable in process of State Enterprise Reform.

b) Renovation of management of SOEs

The share of SOEs in the production of industrial sectors is very significant. For example, in 1993, more than 70% of the gross output of the industrial sectors was produced by SOEs. On the other hand, certain SOEs are planned to continue their operation as SOE according to the Government policy. Therefore, improvement of management of SOEs is also vital for activation of the Vietnamese economy. To improve the management of SOEs, competition between SOEs and non-SOEs, on an equal footing, should be created and maintained. SOEs should not be favored neither unfavored. The following recommendation is needed to create an equal footing for SOEs and non-SOEs. The former recommendation is to deprive advantage and the latter recommendation is to remove disadvantage from SOE . Reference is to be made to the recommendation concerning "Capital tax and depreciation charges", in the chapter of "Tax Reform" (B.5), which will also contribute to the establishment of an "equal footing between SOEs and non-SOEs".

Privileged interest loan rates, which are significantly lower than the market interest rate (half, or even one third), are still provided to SOEs. In the case the following conditions are met, SOEs may obtain loans at privileged interest rates

- Having a reorganization license,
- Project meeting the borrowing conditions of the privileged interest loan; and
- Feasibility study having been conducted.

To provide an equal footing to SOEs and non-SOEs, privileged interest loans should be provided to only SOEs which are meeting the criteria for the policy-based finance scheme being applied to both SOEs and non-SOEs. Undisciplined privileged interest loans just to make SOEs survive should be abolished.

SOEs need permission from relevant government authorities if they wish to create mortgages over land use rights. Therefore, creation of mortgages over "land use rights" by SOEs is still not common in Vietnam. SOEs should be allowed to create mortgages over their land use rights by their own decision, and autonomy of SOEs and the equal footing between SOEs and non-SOEs, from financing point of view, should be strengthened.

5) Effects of Financial Reform on Economy

(1) In-flow of fund to the official market and increase of available loan funds

The most important result of the Financial Reform proposed in this chapter is "increase of confidence in the official financial market". This will accelerate, together with introduction of "flexible banking instruments" and rectification of the current distorted interest rate structure, in-flow of fund from the unofficial market to the official market. Solution of bad debts issues of the banking sector is also crucially important to increase confidence in the financial market. Therefore, it should be noted that success of State Enterprise Reform, which consists of "development of equitization of SOEs" and "renovation of management of SOEs", directly affects on confidence in the financial market.

(2) Reduction of lending interest rates

The success of State Enterprise Reform will reduce the risk of banking business in Vietnam, then consequently the current high spread of banking business will be reduced. Reduction of spread of banks will result in reduction of bank lending rates.

(3) Accomplishment of industrial policy through "institutional finance scheme"

Increase of fund in the financial market will create a better condition for expanding "policy-based finance scheme" to facilitate the industrial policy of Vietnam. The goals of the industrial policy will definitely include "development of State Enterprise Reform" and "development of the private sector". Thus, the institutional finance will assist in attainment of these policy goals.

(4) Development of the private sector

Available funds, especially medium- and long-term funds, for the private sector are very much limited in Vietnam, since most funds are still directed to SOEs notwithstanding the change of the government policy. Moreover, the financial burden due to the high lending interest rates is another headache for the private sector. These are the most serious issues for enterprises in the private sector. Increase of available loan funds and reduction of lending interest rate will significantly ease the financial problems of the private sector. The institutional finance will further assist the development of the private sector.

(5) Activation of the Vietnamese economy

All of the abovementioned effects, including accomplishment of the industrial policy, development of State Enterprise Reform and development of the private sector, will lead to activation of the Vietnamese economy. The activated Vietnamese economy will bring increase of competitiveness of Vietnamese products both in the domestic market and in the international market.

B.5 Tax Reform

The tax system of Vietnam has become very much streamlined and crystallized in the recent tax reform. There are no differentiation between SOEs and the private sectors in respect of nine taxes being collected by the Central Government. Therefore, SOEs and the private sectors are now standing on an "equal footing" in respect of the taxes collected by the Central Government, though some of the fees and charges collected by local governments still need reform. This is a remarkable progress attained in the recent tax reform.

1) Taxes in Vietnam

(1) Outline of the taxes

In Vietnam, nine taxes have been gradually introduced from 1990 to 1994. The titles of the taxes and their introduction years are listed below. A further explanation of these nine taxes is given in Table B.15.

Types of Tax	Year
Profit Tax	1990
Special Consumption Tax	1990
Resource Tax	1990
Income Tax	1990
Turnover Tax	1990
Property Tax	1991
Custom Duties	1992
Land Use Right Transfer Tax	1994
Tax on Agricultural Land Use ("Agricultural Tax")	1994

Source: General Department of Taxes, MOF

(2) Fees in Vietnam

According to MOF, there are 75 fees in Vietnam. Some examples of these fees are "Capital Tax on SOEs", "Depreciation Charge to SOEs", "Slaughter Tax", "Hospital Fee", " School Fee", "Registration of Motor Vehicle Fee". "Business License Fee", "Lottery Receipt Fee" and so on.

a) Capital Tax

The Capital Tax is charged on the capital of SOEs invested by the State. Provinces and districts are treated as parts of the State in this respect. This Tax is contributed to the Government budget through payments from SOEs to SOCBs and other banks.

The charge rate of the Capital Tax ranges from 4.8% to 6% per year. The Capital Tax is, in nature, same as interest on the State investment to SOEs. Therefore, it should be noted that the current charge rates are much lower than the market interest rates.

b) Depreciation Charges

The Depreciation Charge is another contribution from SOEs to the Government budget. A depreciation amount of fixed assets of SOEs, computed in line with the guideline by the Government, is to be paid to the Government. Therefore, funds created from depreciation cannot be accumulated in SOEs. The payment is made through SOCBs and other banks, which is similar to the Capital Tax.

For computation of depreciation amounts, the maximum length of useful lives of "machinery and equipment" and "buildings" are stipulated by the Government to be less than 10 years and 25 years, respectively.

However, it should be noted that payments of the Capital Tax and Depreciation Charges are often waived or deferred, if SOEs are in a financially difficult position.

(3) Collection system

All of the abovementioned nine taxes are collected by the Central Government (actually by MOF), either for the Central Government itself, for the provinces, or for sharing between the Central Government and the provinces. This is summarized in Table B.16.

It should be noted that the Profit Tax of non-central SOEs and private companies is collected for the provinces. The Resource Tax on crude oil is collected for the Central Government and the Resource Tax on other resources is collected for the provinces.

Tax collectors located in the provinces are directly belonging to the General Department of Taxes of MOF. Tax revenues collected by the Central Government for the province are subsequently distributed to the provincial governments, and the provincial government then allocates to districts in the province. Communal and villages, the fourth level in the government administration, are not involved in the tax revenue allocation flow.

The fees collection system is rather complicated. Fees to be collected for the provinces and districts are mostly collected directly by the respective local governments.

2) Trend of Government Revenue

The structure of the Government revenue from 1989 to 1993 is shown in the Table B.17. When reviewing the Government revenue structure, it should be noted that the unified application of the taxes to SOEs and the private sectors is the result of the introduction of the nine taxes from 1990 to 1994. Therefore, the result of the tax reform has not been reflected, to the full extent, in the Government revenue in 1993.

It should also be noted that all of the tax revenues collected by the Central Government, including those subsequently allocated to the province, are included in the Central Government budget .

(1) Dependence on revenue from SOEs

The Government revenue is still heavily dependent on the revenue from SOEs. In 1993, the share of the revenue from SOEs was 50.1%, comprising 41.6% of "Taxes and Transfer" and 8.5% of "Depreciation Charge".

The Government revenue structure will significantly change in several years, when the result of tax reform, together with the result of State Enterprise Reform and the result of development of the private sector, is reflected in the Central Government budget.

(2) Revenue from "Import and Export Duties" (Import and Export Tax)

The revenue from Import and Export Duties accounted for 19.3% of the total revenue in 1993, which is the second largest revenue source excluding "Other Taxes", whose components are not analyzed. Import and Export Duties are significant revenue source for the Government.

(3) Small share of indirect taxes in the Government revenue

Demarcation of the taxes into "direct tax" and "indirect tax" is not necessarily clear. Assuming that the taxes from "Agricultural Tax" to "Import and Export Duties" except "Profit Tax" and "Income Tax" are indirect tax, the share of the indirect taxes in the Government revenue was still only 34.9% in 1993.

Especially, the share of the Turnover Tax is only 2.8% of the revenue. It is observed that there would be much room for increasing the revenue from the indirect taxes, particularly from the Turnover Tax. However, it should be noted that, as commented in "Recommendation", a Value Added Tax should eventually be introduced in place of the Turnover Tax.

3) Direction of Tax Reform

According to the explanation given by SPC, the following is the direction of tax reform in Vietnam.

- Simplification of the tax system
- Removal of contradiction in the tax system
- Reduction of tax rate steps and reducing higher tax rates
- Expansion of types of products to be subject to special Consumption Tax and lowering tax rates
- Reduction of the Profit Tax rate and Income Tax rate
- Improvement of the "Land Use Right License" system to enforce good management and utilization of land
- Change of the tax collection system to self-assessment system
- Reform of Turnover Tax
- Lowering tax rates
- General reduction of Custom Duties rates.

In line with this direction of tax reform, it was explained by MOF that the "Personal Income Tax" and "Corporate Income Tax" are going to be introduced in place of existing the "Income Tax" and "Profit Tax".

The Profit Tax is currently imposed on business profits regardless whether they are being earned by an individual or a company. On the other hand, application of the current Income Tax is limited to only high income earners. In this proposed tax changes, companies are subject to the Corporate Income tax, and more individuals would be subject to the Personal Income Tax.

4) Recommended Tax Reform

Inter-relationship of recommended points concerning taxation is shown in "Inter-relationship of recommended points (Tax Reform)", chart in Figure B.5.

(1) Unification of Profit Tax rates and introduction of tax incentive measures

The background of differentiation of profit tax rates among sectors, i.e. higher tax rate on the light industry sector (35%) and particularly on the service sector (45%) than the heavy industry sector (25%), is to make some "adjustment" to different production cost ratios, profit ratios, turnover ratios, income level of workers, etc. in each industrial sector. However, it is considered that differentiation of the profit tax rates is not functioning as it is expected, because these various factors vary among enterprises even in the same sector while the profit tax rate is fixed for each of these three major industrial categories.

As the concept of "adjustment" is considered to be rather negative, it is recommended to convert the basic concept from "adjustment" to "promotion". Under this "promotion" concept, enterprises, whose business activities are in line with the direction of the industrial policy of Vietnam, should be given various tax incentives such as investment tax credit, allowance of tax deduction for non-cash provision expenses for specified purposes, allowance of accelerated depreciation for qualifying capital investment and allowance of double tax deduction for cash expenditures for certain purposes such as overseas market development.

Conditions for obtaining these tax incentives should be more detailedly established, rather than just by industry category, to ensure that the tax incentives work to drive the business activities in line with the industrial policy of Vietnam.

Tax rate should be equally applied to every tax payer. The Profit Tax rate itself should not be varied for the purpose of provision of tax incentives. Moreover, loss-making enterprises could not obtain benefit by the reduction of tax rate. In this respect, tax incentive by means of reduction of the Profit Tax rate is not proper.

(2) Reinforcement of tax collection system

In the Government revenue, the shares of Profit Tax, Income Tax and Turnover Tax, which are generally considered to be major government revenue sources, are only 1.9%, 0.6% and 2.8% respectively. The shares of these major taxes are much lower than expected. Revenue from the taxes, including direct taxes and indirect taxes, should be significantly increased by reinforcing the tax collection capability of MOF through the increase of the number of tax collectors, improvement of the administration of the Tax Office, and strict execution of the tax laws and regulations.

Various institutional schemes are proposed, such as "Deposits insurance system", "Trade insurance scheme", etc. These schemes could not be founded without fund. Therefore, strengthening the financial base of the Government by reinforcement of the tax collection system is vitally needed.

(3) Introduction of "Value Added Tax" ("VAT ") in place of Turnover Tax

VAT was introduced in 1993 on an experimental basis, on which wholesalers and retailers meeting certain book-keeping requirements were allowed to choose to be taxed on the value-added with rates ranging from 4 % to 16 %. According to the explanation by MOF, the Vietnam Government is now reviewing the result of the VAT trial program and this review will be completed by October 1995. Preparation of a proposal for VAT system will be finished in 1996, and VAT would be introduced in 1997.

VAT should be introduced, to full extent, to replace the Turnover Tax in a medium-term when certain prerequisite conditions, such as establishment of modern accounting standards, maintenance of proper recording of books and creation of qualification of accounting professionals such as "certified public accountant (CPA)", are met. Introduction of VAT tax in Japan, in 1989, could not be successfully done without the participation of over 40,000 accounting professionals including CPA and Authorized Tax Specialists.

The time schedule for introduction of VAT appears to be less realistic as these prerequisites may not be satisfied by 1997. In this context, the reform of Turnover Tax commented by MOF is considered to be realistic and practical. In this reform, the Turnover Tax rates will be simplified from the existing18 different tax rates ranging from 0% to 40%, to 10 different tax rates. At the same time, the Turnover Tax rates will be reduced. This Turnover Tax reform will mitigate and lessen various bad impacts of Turnover Tax on such aspects as "finance", "division work system" and "export promotion", which are explained in each relevant section in this report.

Further, it is recommended to apply a relatively low single tax rate, say 5%, to the Turnover Tax in order to minimize the negative impacts of this tax. On the other hand, tax collection should be strictly executed to secure the revenue from the Turnover Tax and to realize fairness in the sharing of the Turnover Tax burden among the people and enterprises.

When introducing VAT, it should be noted that the VAT system should be rather simplified in the initial stage. In the Japanese VAT system, substantiation of VAT value by invoices is not required, and it is considered to be simpler than that in Europe. It is worthwhile to study VAT systems in various countries before finalizing the VAT system in Vietnam.

(4) Capital Tax and Depreciation Charge

Providing an "equal footing between SOE and non-SOEs" is important to develop state enterprise reform. The recommendations are made with respect to (i) increase of Capital Tax rates, and (ii) abolishment of the Depreciation Charge.

The Capital Tax rates applied to SOEs, ranging from 4.8% to 6% per year, are far below the market interest rates. These rates should be increased significantly to strengthen the "equal footing" of the business activities between SOEs and the private sectors.

The Depreciation Charge should be abolished so that depreciation may be accumulated in SOEs to enable them to use depreciation as one of funding sources of their own. This change will contribute to strengthening the autonomy of the management of SOEs, which is one of major goals of State Enterprise Reform. It was reported that an announcement , giving more flexibility in choosing useful lives of fixed assets for depreciation, was released by the Government in early June 1995. In this announcement the depreciation charge is abolished and SOEs can retain fund from depreciation in the enterprises.

(5) Establishment of modern accounting standards and creation of qualification of accounting professionals

Modern accounting standards, including cost accounting standards, should be established by a body nominated by the Government. The modern accounting standards are indispensable tools for modernizing the management of enterprises including SOEs and private companies. Taxable income for the purpose of Profit Tax should be derived by adjusting the accounting profit, which is calculated in accordance with the accounting standards. Qualification of the accounting professional, such as Certified Public Accountant (CPA), should be established to implement the accounting standards.

B.6 Administrative Reform

1) Basic Policy and Progress

Administrative system reform should be one of major areas of renovation for the accelerated industrial development. It is because the administrative reform is to be harmoniously adjusted to the economic reforms and work effectively for the formulation of a favorable structure for economic development, particularly for industrial development. The economic managerial apparatus and administrative procedure in Vietnam have been renovated gradually along with the process of shifting from a centralized command system to a market economy. A number of measures have been taken with the aim of raising the efficiency and government managerial ability in the direction of making it more consistent with the economic renovation.

A document titled "National Administrative Reform -- An Important Step in Renovation" states that the Law of Administrative Reform has yet to be promulgated and that there will be a central resolution on this matter in the future. The Government intends to reform it into a more efficient one. In order to improve the administrative system, the Government has undertaken to streamline the management system to minimize its intervention to the economic activities so far, and has defined the functions of the government as (i) an organizer, (ii) a producer, (iii) a consumer, (iv) a financier, and (v) an economic investor.

In addition to the above functions, the new system should overcome existing complicated overlapping administrative services between central and local governments. Likewise, the recruitment system should also be improved to recruit new well educated staffs.

In 1992, the Government organized a task force to arrange streamlined governmental apparatuses for administrative reform, and a new system of salary, classification of ranks and grades, and rearrangement of staff have been implemented as follows:

i) Retrainment of aged staff.

ii) Recruitiment of young staff in accordance with new regulation.

iii) Promulgation of a decision on organization of each ministry aiming at classifying functions & responsibilities of branches. It has been applied to all ministries except for the Ministry of Finance.

iv) A decision determining function, power, organization of the State Planning Committee (SPC) was adopted on 12 August 1994.

v) The government instructions on spending a budget for retraining state staff in the whole nation and on establishing retraining institutions were issued.

vi) The instructions of 15 August 1994 ordered that every government staff must master at least one foreign language.

Despite these efforts, the administrative system of the Government still follows the former system, and there still exist many restrictions and confusion in the exercise of laws and regulations. Further, investors and enterprises have been suffering from bureaucratic attitudes of governmental offices.

2) Direction of Improvement

After the adoption of the Doi Moi policy, continuous efforts have been made by the Government to adapt itself to the market-oriented economy. There remains, however, much to do toward administrative reform, so that the Government could play a more effective role in leading the country's economy, including the industrial development.

Some suggestions and recommendations on the possible administrative reform are presented below, with a view to upgrading the administrative efficiency and adapting to the renovation toward a market economy. They are also illustrated in Figure B.6. It should be noted that the following suggestions and recommendations are made primarily from the viewpoint of the accelerated industrial development of the country. These recommendations should, therefore, be considered as a spring board for the detailed study by the Government of Vietnam.

(1) Basic direction

From the viewpoint of industrial development, it is desirable that the public administration be renovated both at the central and local levels, in the following manner:

a) Transforming the role of the Government more toward supportive one, and restricting Government interventions to indirect ones, rather than direct ones, in principle.

b) Improving transparency of governmental decisions and administrative procedures.

c) Eliminating bureaucratic dealing with investors and business enterprises.

d) Disclosing data and information which are needed to run business, in particular financial data.

e) Keeping consistency in exercising laws and regulations.

f) Integrating services and necessary procedures imposed by ministries, departments, and agencies concerned into one channel.

g) Eliminating duplication of managerial control by central and local governments to get permissions or licenses.

h) Formulating a unified policy for industrial development and trade promotion: In view of the strong interdependence among the various sub-sectors of the manufacturing industry, unified and integrated policy should be formulated and enforced by joint efforts of the agencies concerned. The development policy in the industrial sector should also be concerted with the international trade policy.

i) Providing a competitive free market: Administrative reform should be directed toward securing a free market for all the participants on an equal footing, by avoiding unnecessary intervention and regulations by the Government.

j) Separating the roles of policy making and management: Almost all the ministries and local governments have their SOEs under their control at present. In view of the fact that policies drafted by them and the interests of SOEs under them sometimes contradict with each other, the two distinct roles should be separated.

k) Providing efficient service for economic entities: Restructuring and reorganization of the Government should aim at providing efficient services to various economic entities to support their activities. In particular, public services for the foreign direct investments should be reformed so that more efficient services can be provided through a "one-stop-service window" system, shortening the time required for going through procedures.

(2) Specific recommendations

From the view point of accelerated industrial development, more specific recommendations and suggestions for the administrative reform are given below.

a) Establishment of GDMCA and a high level committee for equitization/ privatization

Currently, ministries and local governments exert the ownership right of the land and properties of SOEs. As state enterprise reform, particularly equitization process, progresses, SOEs become more self-reliant and self-financing and ministries and local governments should become more policy-oriented, transferring the management authority to SOEs. In other words, separation of ownership and management should be executed.

Under these circumstances, it is essential to establish a state organization for the unified management of state properties and assets.

It is advisable that GDMCA be set up under MOF, assuming the following responsibilities:

(a) To exert ownership and manage all the capital, assets and debts of SOEs including land ownership and right of use thereof,

(b) To clear the outstanding debts,

(c) To implement the liquidation, merger, sale and lease as well as equitization of SOEs, either totally or partially, and

(d) To sell shares to the investors in the case of equitization.

It is appreciated that GDMCA was formed under MOF in May 1995, with responsibilities similar to those recommended above. It is also recommended that a high level committee for equitization/privatization be set up with a minister-level chairmanship to formulate a clear government policy toward equitization and to prepare the equitization/privatization implementation program.

b) Establishment of the board of investment (BOI)

Though Vietnam has succeeded in attracting a certain level of foreign investments into the country, there still remain two major constraints hindering further inflow of foreign and domestic investments. They are:

(a) Procedures for getting investment licenses are complicated and time-consuming. For example, in the case of large-scale projects, investors must go through the local government, the ministry concerned and SCCI and finally the Prime Minister for final approval.

(b) SCCI, which is responsible for handling foreign investments, does not assume responsibility for domestic investments that may not be favorable for joint project undertaking by foreign and domestic investors.

Under these circumstances, it is recommendable that a central agency be formulated as a sole agency for handling both foreign and domestic investments, providing one-stop-service to the investors. The major responsibilities of such an agency should include:

(a) To evaluate and approve the applications for foreign investment including joint ventures with domestic partners,

(b) To evaluate and approve the applications for domestic investment,

(c) To promote joint venture investments by foreign and Vietnamese enterprises as well as sub-contracts by foreign to the local enterprises,

(d) To prepare a guideline for the policy, legal framework and standards with regard to investment promotion,

(e) To determine the procedures for obtaining investment licenses as well as setting up Vietnamese (local affiliated) companies,

(f) To determine the application of the investment incentives,

(g) To prepare a list of the projects for investment promotion for foreign direct investment,

(h) To provide the investors with relevant information and data with regard to investment and marketing.

It is recommended that approval of the right of using land be also given by the BOI to the applicants after consultation with the local governments concerned. BOI's decision should supersede the ministerial orders and notices. It is desirable that BOI organization be evolved from the existing SCCI.

c) Streamlining ministries and committees for integrated policy-making for industrial development

At present, 22 ministries manage and supervise central SOEs and local governments manage local SOEs. In the industrial sector, many ministries and departments at central, provincial and district levels are responsible for the management of SOEs. In consequence, two problems have arisen as follows:

(a) In some cases, the stance of the ministry as a policy-making body contradicts with that of SOEs under its supervision.

(b) Various ministries and committees are concerned with sub-sector development of the industrial sector, without a unified development policy for the industrial sector for the regions and country as a whole.

Aiming at solving these problems, the following measures are advisable:

(a) To release the ministries/committees from the management of SOEs and convert them into policy-making bodies,

(b) To establish a central ministry which is responsible for the formulation of a unified development policy for the industrial sector.

To attain the above targets, 4 options are conceived. They are:

(a) To establish the Ministry of Industry by merging MHI and MLI,

(b) To merge the MHI, MLI and the Ministry of Energy to form the Ministry of Industry and Energy,

(c) To establish the Ministry of Industry and Trade by uniting MHI, MLI and Ministry of Trade; and

(d) To establish the Ministry of Industry, Energy and Trade by merging all the 4 Ministries.

It is said that the Government is now studying the option (b) above. This would greatly improve efficiency of the administration. In a longer term, it is considered as more advisable that the option (d) be studied, since the manufactured goods would account for the majority of trading both at home and in the export/import business.

d) Setting-up of Vietnam External Trade Organization (VETRO)

In view of the inter-dependence among the economies in the world, including the divided work system within ASEAN which Vietnam has just joined, as well as in the light of competent human resources of the country, it is likely and desirable that external trade would account for a large part of Vietnamese economy. Aiming at smooth international trading, in particular promotion of exports, it is recommendable to set up a special semi-governmental organization, "Vietnam External Trade Organization (VETRO)". Alternatively, reinforcement of the functions of VCCI (Vietnam Chamber of Commerce and Industry) toward this direction is also conceivable.

B.7 Application of Reform Measures to Foundry Industry (A Case Study)

1) Background of the Case Study

A case study on application of reform measures to the foundries in the Hanoi area has been taken up for the reasons enumerated below.

a) Inspections of the existing industries in the Hanoi area showed that foundry is one of the most promising industries to be renovated and modernized in the area. It is because the foundries have a historical background and a technical basis for development. It is also because the casting iron and steel would be exportable to the markets in the ASEAN countries and in Japan if the quality of the products is improved and when the production and marketing systems are modernized.

b) It has been revealed that there are a dozen of foundries in the existing SOEs in the Hanoi area. Most of the equipment and facilities in these foundries are under-utilized and their productivity is substantially low. These foundries are not operated for the subcontracted works.

c) It has been proposed in this Study that a divided work system should be introduced in the modernization of industries in the Hanoi area (refer to Appendix-D). The foundry industry is a candidate industry that the divided work system is typically applied.

d) In applying the divided work system to the foundries in the Hanoi area, it would be possible that the factory specialized in foundry work will be equitized or privatized.

2) Proposed Restructuring

It is proposed to set up one or two new foundries in the Hanoi area, through restructuring in the following manner:

a) The machinery and equipment for foundries available in the existing SOEs will be detached and transferred to the new foundries if they are useful and serviceable. GDMCA will intervene in the detachment and transfer of the machinery and equipment (refer to Appendix-B.3).

b) One or two new companies will be established and equipped with the machinery and equipment transferred from SOEs and with modern facilities, as well as technical staff and workers shifted from the old foundries.

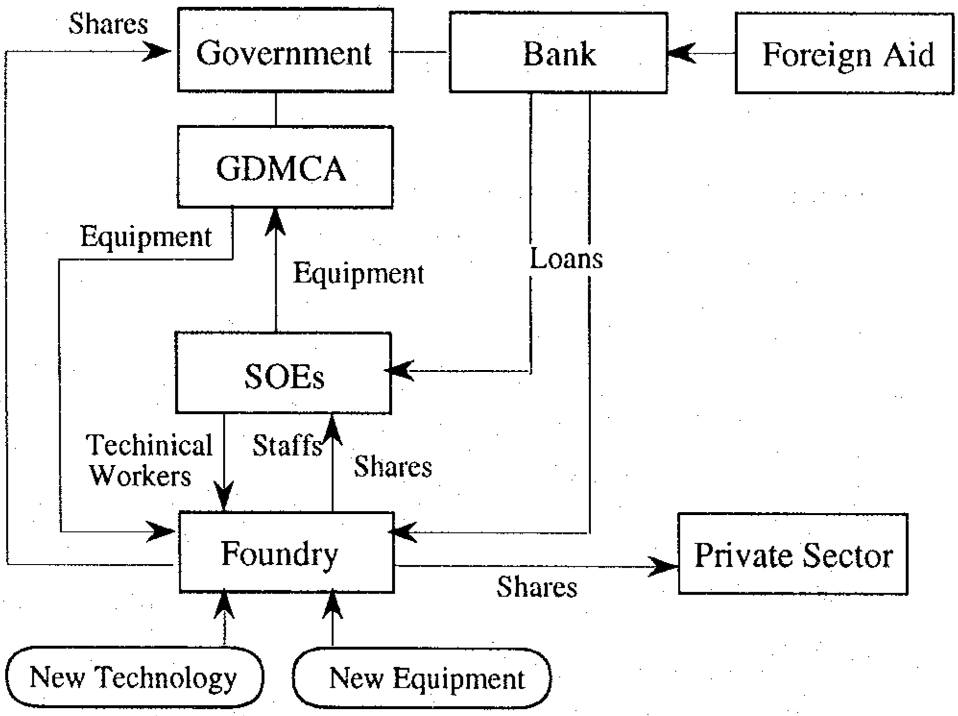
c) In acquiring the machinery and equipment, either through transfer from SOEs or new purchase, finance would be made available through SOCBs or "two-step loan" (refer to Appendix-B.4). SOEs which had transferred equipment, staff and workers would acquire shares of the new company. It would be desirable that private investors also acquire shares of such a company.

d) The new company specializing in foundry work will get the jobs as a subcontractor to SOEs and in other markets. It is prerequisite that SOEs shall stop their own foundries and get all the casting products from the newly established company.

e) The new company will improve its technology by introducing technologies from the industrialized countries through agreements on technical cooperation. The company will also develop marketing of its products in the domestic and international markets.

3) Procedure for Establishment

Provisionally, a procedure for establishment of new companies specializing in foundry is conceived as illustrated below.



It is noted that transparency of procedures is one of the key factors for success in the establishment of a new company. Particularly, valuation of the assets should be done by the responsible body, like GDMCA.

4) Effects of Restructuring

Through the establishment of a new company specializing in foundry work, it would be possible to expect the following effects that would be favorable in promoting modernization of the existing industries in the Hanoi area:

a) The specialized company will improve the productivity and skills for production.

b) The specialized company will promote the divided work system and subcontract work system, thus improving the productivity and quality of products.

c) The company will promote equitization/privatization of SOEs.

d) The company will get chances to improve its technology for production and to increase domestic sales, as well as to open markets for exports.

e) The company will serve as a model for restructuring of the existing industries and a model for equitization/privatization, as well as a model for increase in production for domestic and international markets.

It is recommended that a further in-depth study be made on this model for restructuring of the foundry industry in the Hanoi area, in line with the study on technical and managerial modernization of the foundry industry proposed in the Main Report, Chapter 4.2 of this Final Report.

Table B.01 GDP per Capita, Its Growth and Growth Rate of GDP of Selected Economies with Large Population

	Population (millions) mid-1992	GDP per capita (dopllars) in 1992	Average growth rate of GDP per capita 1980-1992	Average growth rate of GDP 1970-1980	Average growth rate of GDP 1980-1992
Ethiopia	54.8	110	-1.9	1.9	1.2
Bangladesh	114.4	220	1.8	2.3	4.2
India	883.6	310	3.1	3.4	5.2
Nigeria	101.9	320	-0.4	4.6	2.3
Pakistan	119.3	420	3.1	4.9	6.1
China	1162.2	470	7.6	-	9.1
Egypt,.Arab Rep.	54.7	640	1.8	9.5	4.4
Indonesia	184.3	670	4.0	7.2	5.7
Philippines	64.3	770	-1.0	6.0	1.2
Colombia	33.4	1,330	1.4	5.4	3.7
Thailand	58.0	1,840	6.0	7.1	8.2
Poland	38.4	1,910	0.1	-	0.6
Turkey	58.5	1,980	2.9	5.9	4.9
Iran, Islamic Rep.	59.6	2,200	-1.4	-	2.3
South Africa	39.8	2,670	0.1	3.0	1.1
Brazil	153.9	2,770	0.4	8.1	2.2
Mexico	85.0	3,470	-0.2	6.3	1.5
Argentina	33.1	6.050	-0.9	2.5	0.4
Korea, Rep.	43.7	6,790	8.5	9.6	9.4
Spain	39.1	13,970	2.9	3.5	3.2
United Kingdom	57.8	17,790	2.4	2.0	2.7
Italy	57.8	20,480	2.0	3.8	2.4
France	57.4	22,260	1.7	3.2	2.2
Germany	80.6	23,030	2.4	2.6	2.6
United States	255.4	23,240	1.7	2.8	2.7
Japan	124.5	28,190	3.6	4.3	4.1
Hong Kong	5.8	15,360	5.5	9.2	6.7
Singapore	2.8	15,730	5.3	8.3	6.7
Malaysia	18.6	2,790	3.2	7.9	5.9
Low & Middle Income	4610.1	1,040	0.9	-	3.1
Sub-Saharan Africa	543.0	530	-0.8	3.6	1.8
East Asia & Pacific	1688.8	760	6.1	-	7.7
South Asia	1177.9	310	3.0	3.5	5.2
Middle East & N. Africa	252.6	1,950	-2.3	-	2.2
Latin America & Carib.	453.2	2,690	-0.2	5.4	1.8
High Income Economies	828.1	22,160	2.3	3.2	2.9
World	5438.2	4,280	1.2	3.4	3.0

Source: World Development Report 1994, by the World Bank

Table B.02 Growth Rate of GDP and Per Capita GDP in 1980-1992 by Group of Economies

	Average growth rate of GDP per capita 1980-1992	Average growth rate of GDP 1980-1992
Low & Middle Income	0.9	3.1
Sub-Saharan Africa	-0.8	1.8
East Asia & Pacific	**6.1**	**7.7**
South Asia	3.0	5.2
Middle East & N. Africa	-2.3	2.2
Latin America & Carib.	-0.2	1.8
High Income Economies	2.3	2.9
World	1.2	3.0

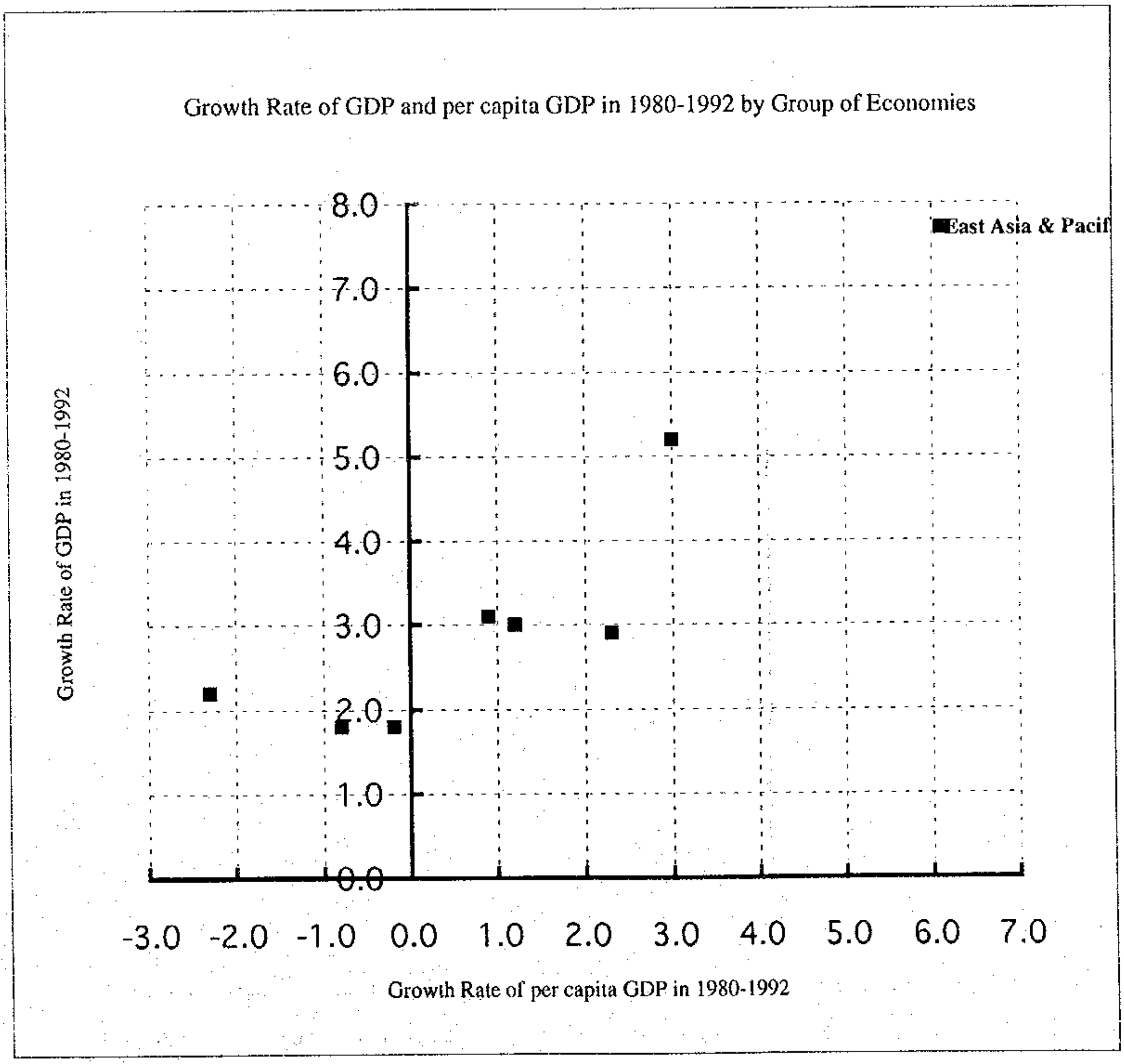


Table B.03 Growth Rate of GDP per Capita and GDP of Selected Countries or Economies

	Average growth rate of GDP per capita 1980-1992	Average growth rate of GDP 1980-1992
Korea, Rep.	8.5	9.4
China	7.6	9.1
Thailand	6.0	8.2
Hong Kong	5.5	6.7
Singapore	5.3	6.7
Pakistan	3.1	6.1
Malaysia	3.2	5.9
Indonesia	4.0	5.7
India	3.1	5.2
Turkey	2.9	4.9
Egypt,.Arab Rep.	1.8	4.4
Bangladesh	1.8	4.2
Japan	3.6	4.1
Colombia	1.4	3.7
Spain	2.9	3.2
United Kingdom	2.4	2.7
United States	1.7	2.7
Germany	2.4	2.6
Italy	2.0	2.4
Nigeria	-0.4	2.3
Iran, Islamic Rep.	-1.4	2.3
Brazil	0.4	2.2
France	1.7	2.2
Mexico	-0.2	1.5
Ethiopia	-1.9	1.2
Philippines	-1.0	1.2
South Africa	0.1	1.1
Poland	0.1	0.6
Argentina	-0.9	0.4

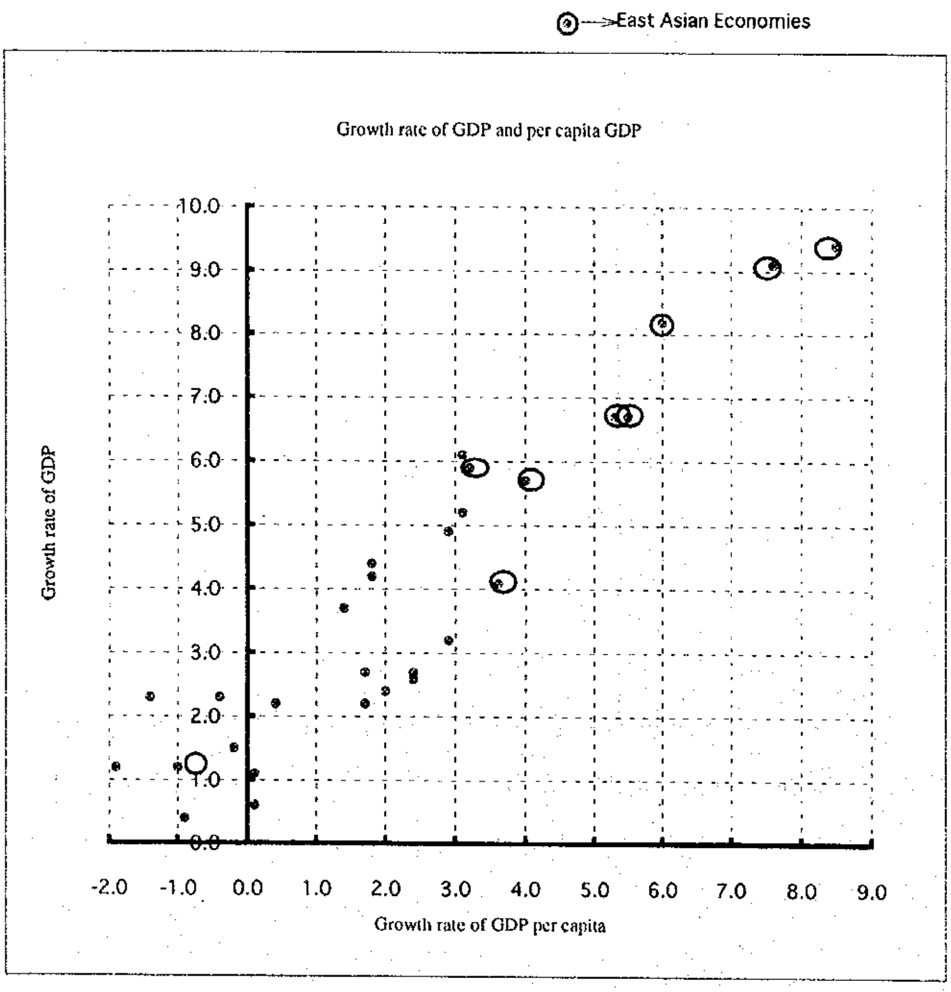


Table B.04 Growth Rate of GDP in 1970-80 and 1980-1992

	Average growth rate of GDP 1970-1980	Average growth rate of GDP 1980-1992	Index devided by World Average 1970-1980	Index devided by World Average 1980-1992
Korea, Rep.	9.6	9.4	2.82	3.13
Thailand	7.1	8.2	2.09	2.73
Singapore	8.3	6.7	2.44	2.23
Hong Kong	9.2	6.7	2.71	2.23
Pakistan	4.9	6.1	1.44	2.03
Malaysia	7.9	5.9	2.32	1.97
Indonesia	7.2	5.7	2.12	1.90
India	3.4	5.2	1.00	1.73
Turkey	5.9	4.9	1.74	1.63
Egypt,.Arab Rep.	9.5	4.4	2.79	1.47
Bangladesh	2.3	4.2	0.68	1.40
Japan	4.3	4.1	1.26	1.37
Colombia	5.4	3.7	1.59	1.23
Spain	3.5	3.2	1.03	1.07
United States	2.8	2.7	0.82	0.90
United Kingdom	2.0	2.7	0.59	0.90
Germany	2.6	2.6	0.76	0.87
Italy	3.8	2.4	1.12	0.80
Nigeria	4.6	2.3	1.35	0.77
France	3.2	2.2	0.94	0.73
Brazil	8.1	2.2	2.38	0.73
Mexico	6.3	1.5	1.85	0.50
Philippines	6.0	1.2	1.76	0.40
Ethiopia	1.9	1.2	0.56	0.40
South Africa	3.0	1.1	0.88	0.37
Argentina	2.5	0.4	0.74	0.13

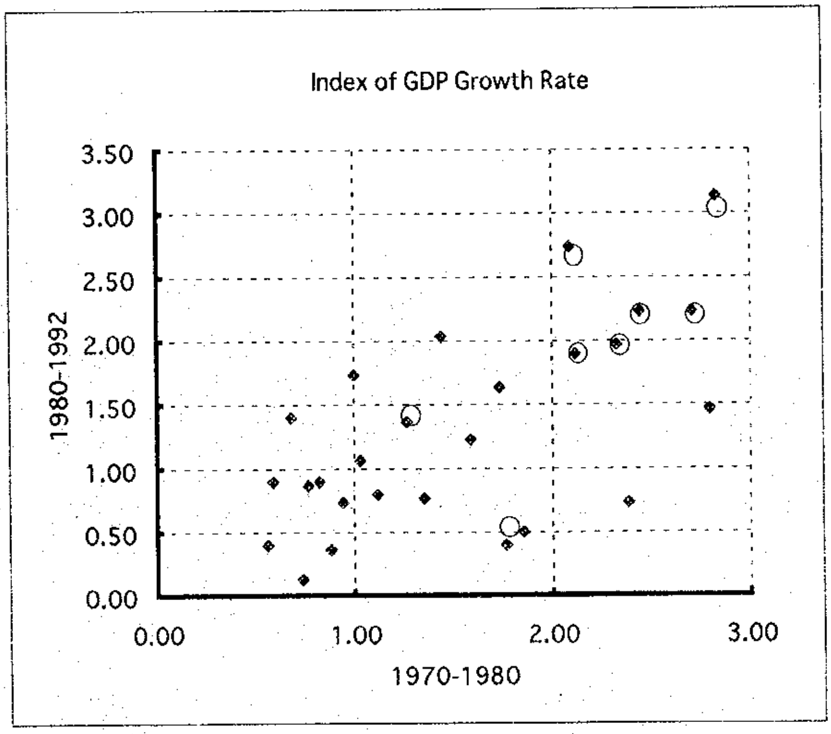


Table B.05 Distribution of Gross Domestic Product by Major Industrial Sectors in 1992 and Adult Illiteracy in 1990

		GDP per capita (dollars) in 1992	Agriculture (%)	Industry (%)	Services (%)	Adult Illiteracy (%) in 1990
A-1	Ethiopia	110	48	13	39	-
A-2	Bangladesh	220	34	17	49	65
A-3	India	310	32	27	40	52
A-4	Nigeria	320	37	38	25	49
A-5	Pakistan	420	27	27	46	65
A-6	China	470	27	34	38	27
A-7	Egypt,.Arab Rep.	640	18	30	52	52
A-8	Indonesia	670	19	40	40	23
B-1	Philippines	770	22	33	45	10
B-2	Colombia	1,330	16	35	49	13
B-3	Thailand	1,840	12	39	49	7
B-4	Poland	1,910	7	51	42	-
B-5	Turkey	1,980	15	30	55	19
B-6	Iran, Islamic Rep.	2,200	23	28	48	46
C-1	South Africa	2,670	4	42	54	-
C-2	Brazil	2,770	11	37	52	19
C-3	Mexico	3,470	8	28	63	13
C-4	Argentina	6,050	6	31	63	5
D-1	Korea, Rep.	6,790	8	45	47	4
D-2	Italy	20,480	3	32	65	e
D-3	France	22,260	3	29	68	e
D-4	Germany	23,030	2	39	60	e
D-5	Japan	28,190	2	42	56	e
D-6	*Hong Kong*	15,360	0	23	77	e
D-7	*Singapore*	15,730	0	38	62	e

Source: World Development Report 1994, by the World Bank
Note: "e" means illiteracy is less than 5 percent.

Table B.06 GDP and Merchandise Exports of Selected Economies with Large Population and Selected Asian Economies

	GDP (million $) in 1992	GDP per capita (dollars) in 1992	Merchandise Trade (million $) Exports in 1992	Average Annual Growth Rt of Exports 1970-80	Average Annual Growth Rt of Exports 1980-92
Ethiopia	6,257	110	799	-2.3	-4.3
Bangladesh	23,783	220	2,527	3.8	7.6
India	214,598	310	22,530	4.3	5.9
Nigeria	29,667	320	8,119	0.4	1.7
Pakistan	41,904	420	9,360	0.7	11.1
China	506,075	470	80,585	8.7	11.9
Egypt,.Arab Rep.	33,553	640	8,293	-2.6	3.1
Indonesia	126,364	670	27,280	7.2	5.6
Philippines	52,462	770	15,465	6.0	3.7
Colombia	48,583	1,330	6,684	1.9	12.9
Thailand	110,337	1,840	40,466	10.3	14.7
Poland	83,823	1,910	15,309	4.5	3.0
Turkey	99,696	1,980	22,871	4.3	9.0
Iran, Islamic Rep.	110,258	2,200	26,744	-6.8	14.5
South Africa	103,651	2,670	19,644	11.1	0.7
Brazil	360,405	2,770	23,115	8.5	5.0
Mexico	329,011	3,470	47,877	13.5	1.6
Argentina	228,779	6,050	14,864	7.1	2.2
Korea, Rep.	296,136	6,790	81,413	23.5	11.9
Spain	574,844	13,970	99,473	9.1	8.2
United Kingdom	903,126	17,790	221,658	4.4	3.5
Italy	1,222,962	20,480	184,510	6.0	4.1
France	1,319,883	22,260	238,299	6.6	5.2
Germany	1,789,261	23,030	407,172	5.0	4.6
United States	5,920,199	23,240	551,591	6.5	3.8
Japan	3,670,979	28,190	230,975	9.0	4.6
Hong Kong	77,828	15,360	123,427	9.7	5.0
Singapore	46,025	15,730	72,067	4.2	9.9
Malaysia	57,568	2,790	38,361	4.8	11.3
Low & Middle Income	4,695,645	1,040	829,967	3.9	4.4
Sub-Saharan Africa	269,955	530	60,219	2.8	2.4
East Asia & Pacific	1,266,819	760	289,984	9.5	10.5
South Asia	297,360	310	38,974	3.6	6.8
Middle East & N. Africa	454,541	1,950	112,185	3.9	0.8
Europe & Central Asia	1,124,423	2,080	179,275	-	-
High Income Economies	18,312,160	22,160	2,955,958	5.4	4.9
World	23,060,560	4,280	3,785,925	4.0	4.9

Source: World Development Report 1994, by the World Bank

Table B.07 Growth Rate of Exports 1970-80 and 1980-92

	Gr.Rt.70-80	Gr.Rt.80-92
Thailand	10.3	14.7
Iran, Islamic Rep	-6.8	14.5
Colombia	1.9	12.9
China	8.7	11.9
Korea, Rep.	23.5	11.9
Malaysia	4.8	11.3
Pakistan	0.7	11.1
Singapore	4.2	9.9
Turkey	4.3	9.0
Spain	9.1	8.2
Bangladesh	3.8	7.6
India	4.3	5.9
Indonesia	7.2	5.6
France	6.6	5.2
Brazil	8.5	5.0
Hong Kong	9.7	5.0
Germany	5.0	4.6
Japan	9.0	4.6
Italy	6.0	4.1
United States	6.5	3.8
Philippines	6.0	3.7
United Kingdom	4.4	3.5
Egypt, Arab Rep.	-2.6	3.1
Poland	4.5	3.0
Argentina	7.1	2.2
Nigeria	0.4	1.7
Mexico	13.5	1.6
South Africa	11.1	0.7
Ethiopia	-2.3	-4.3

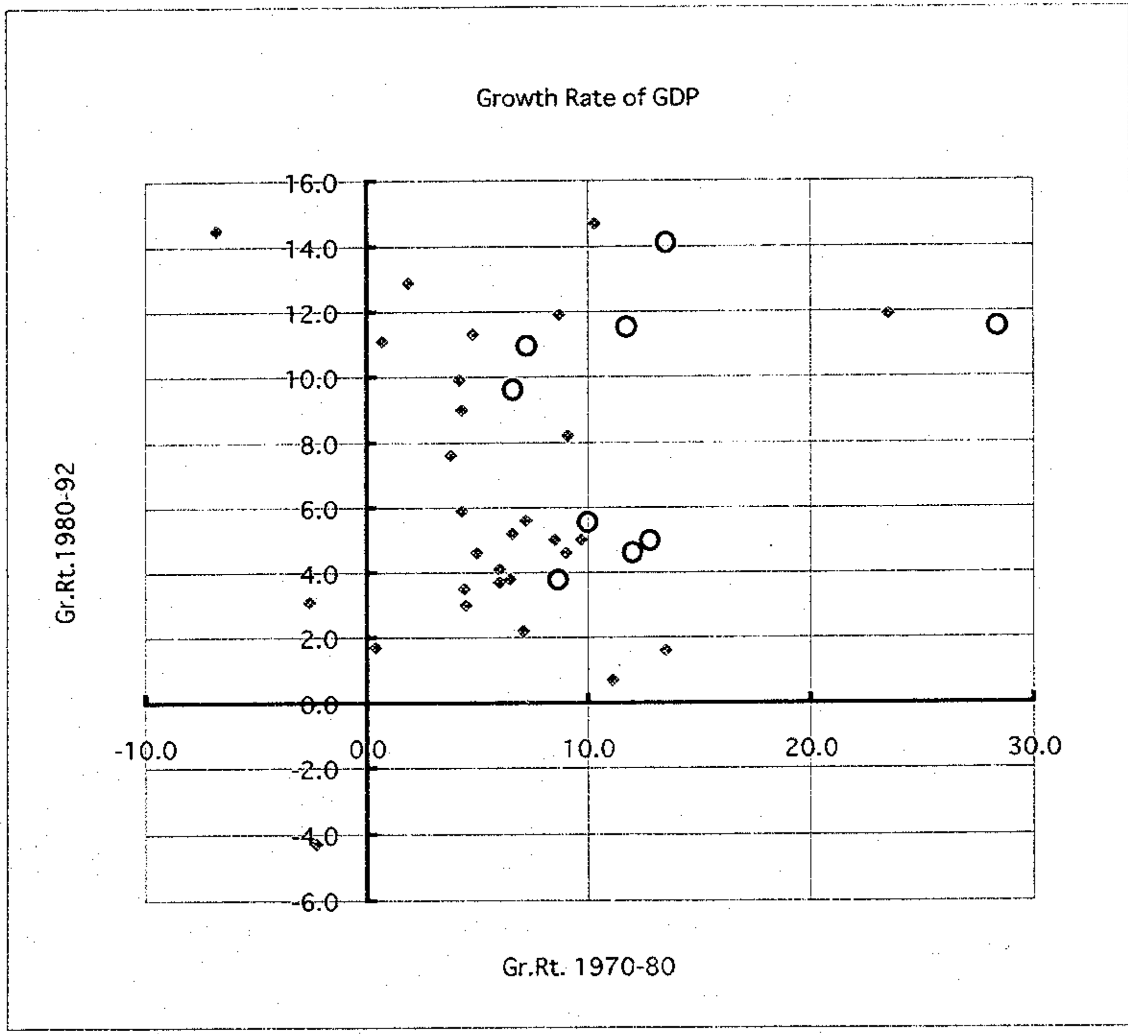


Table B.08 Major Economic Indicators of Middle European Countries, Former Soviet Union Countries

	Population (millions) 1993	Area (thousands of sq.km)	GDP per capita (dollars) 1993	GDP annual growth rate 1993	Export per capita (dollars) 1993	Import per capita (dollars) 1993	Average monthly salary (dollar,1993)
Poland	38.2	313	2,231	3.8	357	416	180
Slovak Republic	5.3	49	2,065	-4.1	1,032	1,190	174
Czech Republic	10.3	79	3,067	-0.3	1,240	1,219	200
Russian Federation	148.5	17,075	1,178	-12.0	290	182	101
Hungary	10.4	93	3,700	-2.3	857	1,205	295
Slovenia	2.0	20	6,015	1.0	3,058	3,259	414
Ukraine	51.9	604	633	-18.0	60	46	22
Belarus	10.3	208	830	-10.0	97	68	316
Estonia	1.58	45	2,633	-3.3	515	566	404
Latvia	2.68	65	1,619	-15.0	376	356	344
Lithuania	3.73	65	1,102	-16.2	598	673	422
Romania	23.2	24	1,089	1.0	210	280	81
Bulgaria	9.0	9	1,225	-4.2	398	479	114
Croatia	4.7	5	2,122	-7.0	831	949	147
Kazakhstan	16.9	2717	1,480	-	75	213	38(261)
Uzbekistan	20.7	447	1,130	-	34	47	30(207)
Turkmenistan	3.7	488	1,353	-	284	136	32(237)
Kyrgys Republic	4.5	199	1,001	-	25	25	27(208)
Tajikistan	5.4	143	645	-	49	70	19(233)

Note: Figures in parenthesis are in 1991.
Source: Tsuneo Morita, Economics on Transition of Regime, Dec.1994.

Table B.09 Selected Interest Rates

Interest rate (per month)	1989	1990	1991	1992	1993
Demand Deposit- Households	5.0%	2.4%	2.1%	1.0%	0.7%
-Economic units	1.8%	0.9%	1.0%	0.3%	0.1%
Three-month Savings- Households	7.0%	4.0%	3.5%	2.0%	1.4%
-Economic units	3.0%	1.8%	2.1%	1.5%	0.8%
Lending Rates					
Agriculture	3.7%	2.4%	3.3%	2.5%	-
Industry and Transport	3.8%	2.7%	3.0%	2.0%	-
Commerce and Tourism	3.9%	2.9%	3.7%	2.7%	-
Fixed Capital	-	0.8%	0.8%	1.8%	1.2%
Working Capital	-	-	-	2.7%	2.1%
SBVN					
Transaction Balances	-	-	1.0%	0.3%	0.1%
Refinancing Agriculture	-	-	-	0.9%	*1
Refinancing Other Users	-	-	-	1.2%	*1
Inflation rate	2.7%	7.7%	4.8%	1.1%	1.2%

*1 Refincaning rates were set at 60% and 80% of lending rate for agriculture and other sectors, respectively.

(Note) Figures are Interst rates and inflation rates in December in the year

(Source) Financial Sector Review- An Agenda for Financial Sector Development, World Bank July 20, 1994

Table B.10 Banks in Vietnam

I. Four specialized banks

(1) Investment and development bank
the Bank for Investment and Development of Vietnam

(2) Commercial banks
the Industrial and Commercial Bank of Vietnam
the Agriculturl Bank of Vietnam
the Bank for Foreign Trade in Vietnam

II. Other financial institutions and their number as of December 1994

Joint stock banks	43
Finance companies	2
Credit co-operatives	62
Joint venture banks	3
Foreign Branches	9
Foreign banks having epresentative office	38

Source: JICA Study Team

Table B.11 Comparison of Finance Performance Indicators

(Amount: in billion Dong)

	SOCBs		Non-SOCBs		Total	
Total Assets	35,149	91%	3,657	9%	38,806	100%
Income	3,657	93%	258	7%	3,915	100%
Expenses	3,088	95%	175	5%	3,263	100%
Net Profit	569	87%	83	13%	652	100%
Net Profit Ratio	16%		32%			
Capital / Assets	5.5%		20.5%			
Return on Assets	1.6%		2.3%			

(Source) Processed information otained from "Financial Sector Review - An Agenda for Financial Sector Development World Bank July 20, 1994"

Table B.12 SOCBs- Finance Performance Indicators

(In billion Dong)

	Total Assets			Capital / Assets			Return on Assets		
	1991	1992	1993	1991	1992	1993	1991	1992	1993
IDBV	2,143	4,209	5,577	55.5%	13.4%	10.5%	2.8%	2.6%	2.5%
Incombank	5,399	6,246	8,284	4.4%	5.7%	4.7%	2.5%	0.7%	1.9%
Vietcombank	14,049	16,036	13,790	1.0%	2.5%	3.8%	1.4%	1.9%	1.9%
Agribank	4,971	5,140	7,498	3.8%	8.4%	5.8%	-2.3%	-0.9%	0.1%
SOCBs total	26,562	31,631	35,149	6.6%	5.5%	5.5%	1.1%	1.3%	1.6%

	Income			Expenses			Net Profit			Net Profit Ratio		
	1991	1992	1993	1991	1992	1993	1991	1992	1993	1991	1992	1993
IDBV	108	253	357	48	144	216	60	109	141	56%	43%	39%
Incombank	454	1,083	1,264	317	1,038	1,103	137	45	161	30%	4%	13%
Vietcombank	599	904	742	400	516	481	199	388	261	33%	43%	35%
Agribank	376	960	1,294	489	1,004	1,288	-113	-44	6	-30%	-5%	0%
SOCBs total	1,537	3,200	3,657	1,254	2,702	3,088	283	498	569	18%	16%	16%

(Source) Financial Sector Review - An Agenda for Financial Sector Development
World Bank July 20, 1994

Table B.13 Financial statement-Incombank

(In million Dong)

BALANCE SHEET

ASSETS	1992		1993	
1. Cash	122,287	1.9%	112,783	1.4%
2. Due from the State Bank	634,157	9.8%	520,738	6.3%
3. Due from other banks	458,769	7.1%	233,829	2.8%
4. Precious metals	9,561	0.1%	7,760	0.1%
5. Loans	4,216,788	64.9%	6,166,916	74.2%
6. Joint-venture investment	100,580	1.5%	82,028	1.0%
7. Land premises & equipments	157,513	2.4%	191,031	2.3%
8. Other assets	793,529	12.2%	994,805	12.0%
Total	6,493,184	100.0%	8,309,890	100.0%

LIABILITIES				
1. Due to customers				
AMONG-On demand	2,019,001	31.1%	2,995,847	36.1%
-On time	1,893,838	29.2%	1,360,110	16.4%
Sub-total	3,912,839	60.3%	4,355,957	52.4%
2. Due to other banks	194,726	3.0%	112,357	1.4%
3. Capital & reserve funds	397,100	6.1%	392,543	4.7%
4. Borrowings	1,269,646	19.6%	1,376,109	16.6%
5. Issuing promissory note	10,815	0.2%	1,065,675	12.8%
6. Profit before tax	123,855	1.9%	161,076	1.9%
7. Other liabilities	584,209	9.0%	846,173	10.2%
8. Difference	-6	0.0%		0.0%
Total Liabilities	6,493,184	100.0%	8,309,890	100.0%

INCOME STATEMENT

	1992		1993	
1. Interest income				
Interest collected from loans and deposits	1,019,588	100.0%	1,094,970	99.6%
Share-earning		0.0%	4,183	0.4%
Sub-total	1,019,588	100.0%	1,099,153	100.0%
2. Interest expenses				
Interest on deposits	661,697	64.9%	542,405	49.3%
Interest on borrowing funds	185,575	18.2%	113,095	10.3%
Sub-total	847,272	83.1%	655,500	59.6%
3. Net interest income	172,316	16.9%	443,653	40.4%
4. Non-interest income				
Foreign exchange and trading of gold	54,339	5.3%	12,383	1.1%
Banking commission	3,772	0.4%	11,622	1.1%
Other income	5,582	0.5%	140,875	12.8%
Sub-total	63,693	6.2%	164,880	15.0%
5. Non-interest expenses				
Foreign exchange and trading of gold	26,262	2.6%	7,060	0.6%
Salaries and pensions	33,626	3.3%	80,436	7.3%
Other expenses	52,266	5.1%	359,961	32.7%
Sub-total	112,154	11.0%	447,457	40.7%
6. Income before taxes	123,855	12.1%	161,076	14.7%
Income taxes	78,527	7.7%	80,538	7.3%
7. Net profit	45,328	4.4%	80,538	7.3%

(Source) Annual Report 1993 of Incombank

Table B.14 Financial Statements- IDBV

(In million Dong)

	1992		1993	
BALANCE SHEET				
ASSETS				
1.Claims to the economy	2,024,684	21.2%	3,725,317	31.5%
1-1.development Credits	1,525,458	16.0%	2,842,949	24.0%
1-2.Short-term Credits	449,226	4.7%	882,368	7.4%
1-3 Other	50,000	0.5%		0.0%
2.Development Financing	5,351,747	56.0%	6,267,628	52.9%
3.Treasur Bond	2,100	0.0%	2,100	0.0%
4.Reserves	738,422	7.7%	1,420,269	12.0%
5.Other assets	1,443,118	15.1%	429,596	3.6%
TOTAL ASSETS	9,560,071	100.0%	11,844,910	100.0%
LIABILITIES				
1.Capital and Funds of which:	2,105,352	22.0%	3,189,177	26.9%
(of which fund for development credit	1,540,000	16.1%	2,605,800	22.0%)
2.Foreign loans for development investment	0	0.0%	618,538	5.2%
3.Fund for development financing	6,508,152	68.1%	6,513,081	55.0%
4.Deposits from clients	533,619	5.6%	1,044,630	8.8%
5.Bonds issued	24,100	0.3%	8,505	0.1%
6.Borrowings	134,507	1.4%	115,505	1.0%
7.Other liabilities	278,441	2.9%	355,474	3.0%
Difference	-24,100	-0.3%		0.0%
TOTAL LIABILITIES	9,560,071	100.0%	11,844,910	100.0%

PROFIT AND LOSS STATEMENT	1992		1993	
Income	357,106	100.0%	258,125	100.0%
Expenses	215,919	60.5%	127,832	49.5%
Profit before tax	141,187	39.5%	130,293	50.5%
Tax	67,770	19.0%	75,993	29.4%
Profit after tax	73,417	20.6%	54,300	21.0%

(Source) Annual Report 1993 of IDBV

Table B.15 Outline of Taxes in Vietnam (1/3)

(1) Profit Tax

The profit tax imposed on taxable incomes of enterprises, including state enterprises and private enterprises. Components of the calculation of taxable income are "total income", "appropriate expenses" and "other profit". Concepts of these components are specified in the tax law. Taxable income can not be derived by adjusting an accounting profit in accordance with the general accounting standards, because such standards are not virtually existing in Vietnam.

The tax rate are differentiated among the sectors as shown below:

- Heavy industries : 25%
- Light industries : 35%
- Service industries : 45%

The tax rates for small enterprises significantly reduce to 1% to 2%. A "small enterprises" are defined to be an enterprise whose taxable income is less than specified amount. Specified amount is ranging from 0.75 million Dong to 3 million Dong depending on sector.

If "monthly average taxable income per capital contributor" is exceeding 10 million Dong, sur-tax at the rate of 25% is imposed on the exceeding part.

Tax losses, caused only from specified reasons such as natural calamities, war etc., may be carried forward to subsequent two years.

(2) Special Consumption Tax

Special Consumption Tax is imposed only specific products such as cigarettes, liquor, bear and fire-cracker. The tax rate ranges from 15% to 100%.

(3) Resource Tax

Resource Tax is imposed on exploitation of natural resources such as metallic resources, gold, precious stones, petroleum, gas, etc. The tax rate ranges from 1% to 20% depending on resources.

For the resources exploited by foreign organizations, the prices to be taxed is determined by the Council of Ministers in reference to international prices.

(4) Income Tax

Income Tax is imposed on income of individual persons. The tax rate of Income Tax is an accelerated tax rate ranging from 0% to 50% depending on the amount of the income. The minimum threshold in the accelerated income tax rate steps is 500,000Dong per month. Sur-tax at the rate of 30% is imposed on the income greater than 5 million Dong per month.

Foreign person is subject to the same income tax rate as local people. However, income less than 2.4 million Dong per month is exempted form Income Tax. Sur-tax is not applied to foreign individuals.

(5) Turnover Tax

Turnover Tax is imposed on all products sold in Vietnam except for the following products:

- Agricultural product subject to Agricultural Tax
- Products subject to Special Consumption Tax
- Products to be exported

There are three sectors for the the turnover tax:

- Low tax sectors- 0% to 10%
- High tax sectors- 30% to 40%
- Other sectors- - 1 % to 6%

The low tax sectors are mainly industrial sectors including "mining", "metal working", "cement production", etc. and the high tax sectors are service sectors including "lottery", "dancing hall", "shipping agent", etc.

(6) Property Tax

Property Tax is imposed on the current value of property. The tax rates are 0.5% for land and 0.3% for buildings. Farming land is exempted from Property Tax.

Table B.15 Outline of Taxes in Vietnam (3/3)

(7) Custom Duties

Custom Duties is often called as "Import tax" in Vietnam. But they are the same tax.

Custom Duties is imposed on various sectors at 28 different tax rates ranging from 0% to 200%. Generally higher custom duties are imposed on consumer goods.

Custom Duties will be exempted or paid back, upon application, for import of material to be exported after processing.

(8) Transfer Right of Using Land Tax

"Transfer Right of Using Land Tax" is imposed on transferring value of right of using land and to be paid by a transferor. The standard tax rate is 5%. However, if transferor has not paid rent or has been exempted from the payment of rent, the tax rate is increased to 10% for agricultural land and 20% for non-agricultural land.

It should be noted that the tax rate is significantly increased to 40%, if the purpose of land is changed from farming to non-farming including industrial activities. In this case, tax is usually recharged to the transferee by the transferor, and the tax is included in the purchase costs of the land.

(9) Tax on Agricultural Land Use ("Agricultural Tax")

Agricultural Tax is imposed on organizations and individuals using land for farming purposes. Land includes land for cultivation, surface water for culture and land for forestry.

Land is categorized into 6 categories in consideration to various factors such as quality of the land, location, topography, climatic conditions, conditions of irrigation, and the tax rate is differentiated in these 6 categories.

Table B.16 Taxes Sharing Between Central Budget and Provincial Budget

Taxes Collected for Central Budget	Taxes Shared with Province	Taxes Collected for Province
Profit Tax (Central SOEs) Customs Duties Special Consumption Tax (Excise Duties) Resource Tax (crude oil) Transfer Right of Using Land Tax	Personal Income tax Turnover Tax	Profit Tax (Non-Central SOEs) and private companies) Tax on Agricultural Land Use Resource Tax (Non-crude oil) Property Tax

(Source) Ministry of Finance

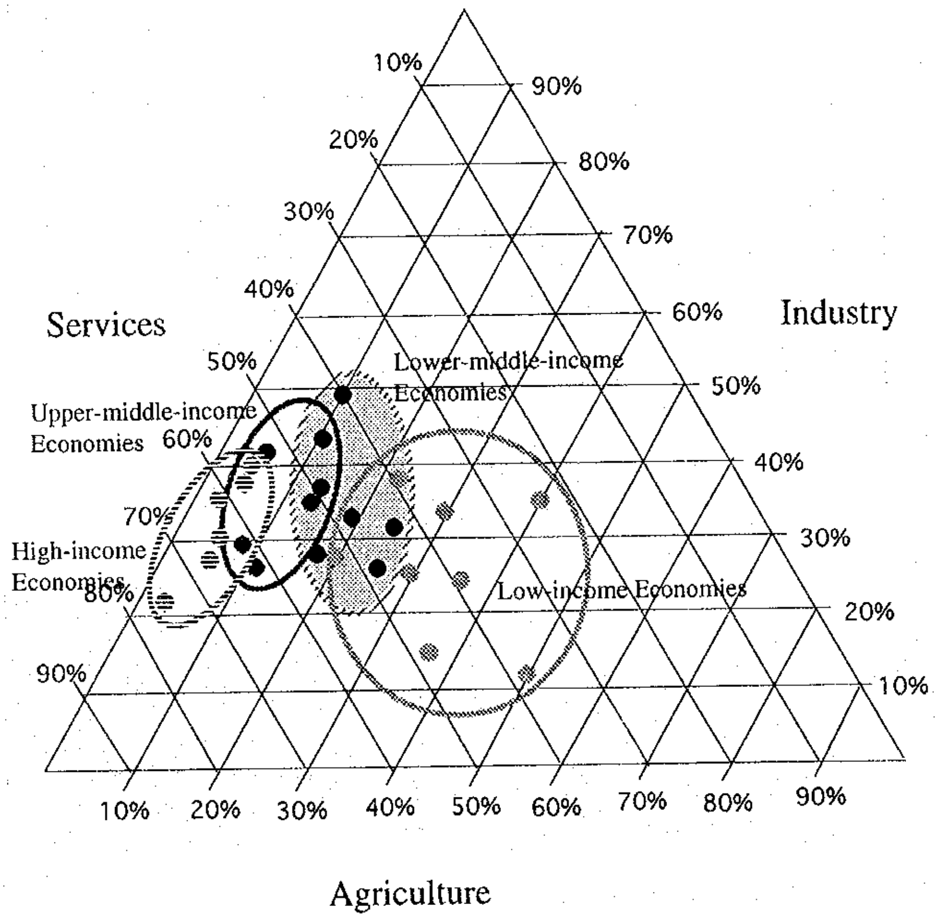
Table B.17 Government revenue

(In billion Dong)

	1,989		1,990		1,991		1,992		(Rev.) 1,993	
State Enterprise	2,244	57.6%	3,620	58.8%	5,927	57.2%	11,383	54.1%	15,279	50.1%
Taxes and Transfers	2,029	52.0%	3,112	50.6%	5,305	51.2%	9,106	43.3%	12,685	41.6%
Depreciation	215	5.5%	508	8.3%	622	6.0%	2,277	10.8%	2,594	8.5%
Non-State Sector	736	18.9%	965	15.7%	1,977	19.1%	3,816	18.2%	5,533	18.1%
Agricultural Tax	308	7.9%	298	4.8%	707	6.8%	1,294	6.2%	1,351	4.4%
Non- Agricultural Tax	428	11.0%	667	10.8%	1,008	9.7%	1,992	9.5%	3,376	11.1%
Turnover Tax	160	4.1%	262	4.3%	250	2.4%	582	2.8%	863	2.8%
Profits Tax	73	1.9%	118	1.9%	161	1.6%	420	2.0%	593	1.9%
Income Tax					62	0.6%	153	0.7%	184	0.6%
Lincense Tax	24	0.6%	31	0.5%			72	0.3%	112	0.4%
Commodities Tax	72	1.8%	75	1.2%	69	0.7%	22	0.1%	16	0.1%
Wholesale Tax	18	0.5%	32	0.5%						
Slaughter Tax	16	0.4%	26	0.4%	35	0.3%	45	0.2%	52	0.2%
Land Tax					5	0.0%	18	0.1%	180	0.6%
Other	65	1.7%	123	2.0%	426	4.1%	680	3.2%	1,376	4.5%
Other Taxes					262	2.5%	530	2.5%	806	2.6%
External Trade:	363	9.3%	733	11.9%	1,099	10.6%	2,194	10.4%	5,900	19.3%
Non-Commercial Import Ta	109	2.8%	126	2.0%						
Import and Export Duties	254	6.5%	607	9.9%	1,099	10.6%	2,194	10.4%	5,900	19.3%
Joint Ventures									389	1.3%
Other Revenue	556	14.3%	835	13.6%	1,080	10.4%	2,782	13.2%	2,401	7.9%
Grants					270	2.6%	848	4.0%	998	3.3%
Total Revenue	3,899	100.0%	6,153	100.0%	10,353	100.0%	21,023	100.0%	30,500	100.0%

(Source) Vietnam Public Sector Management and Private Sector Incentives- World Bank , September 26, 1994

Figure B.1 Structure of GDP by Major Sectors



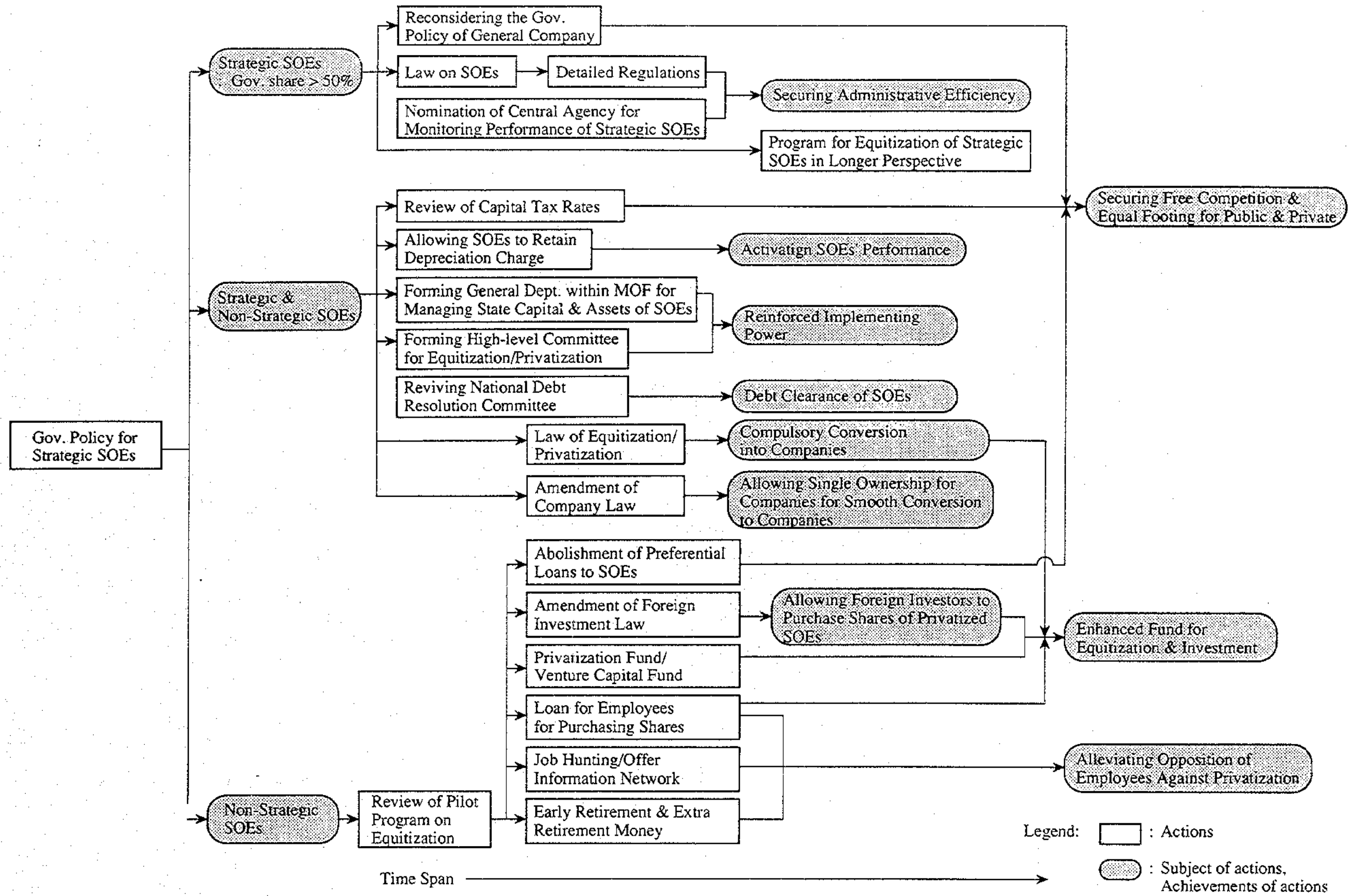


Figure B.2 Acceleration Process for State Enterprise Reform / Equitization / Privatization

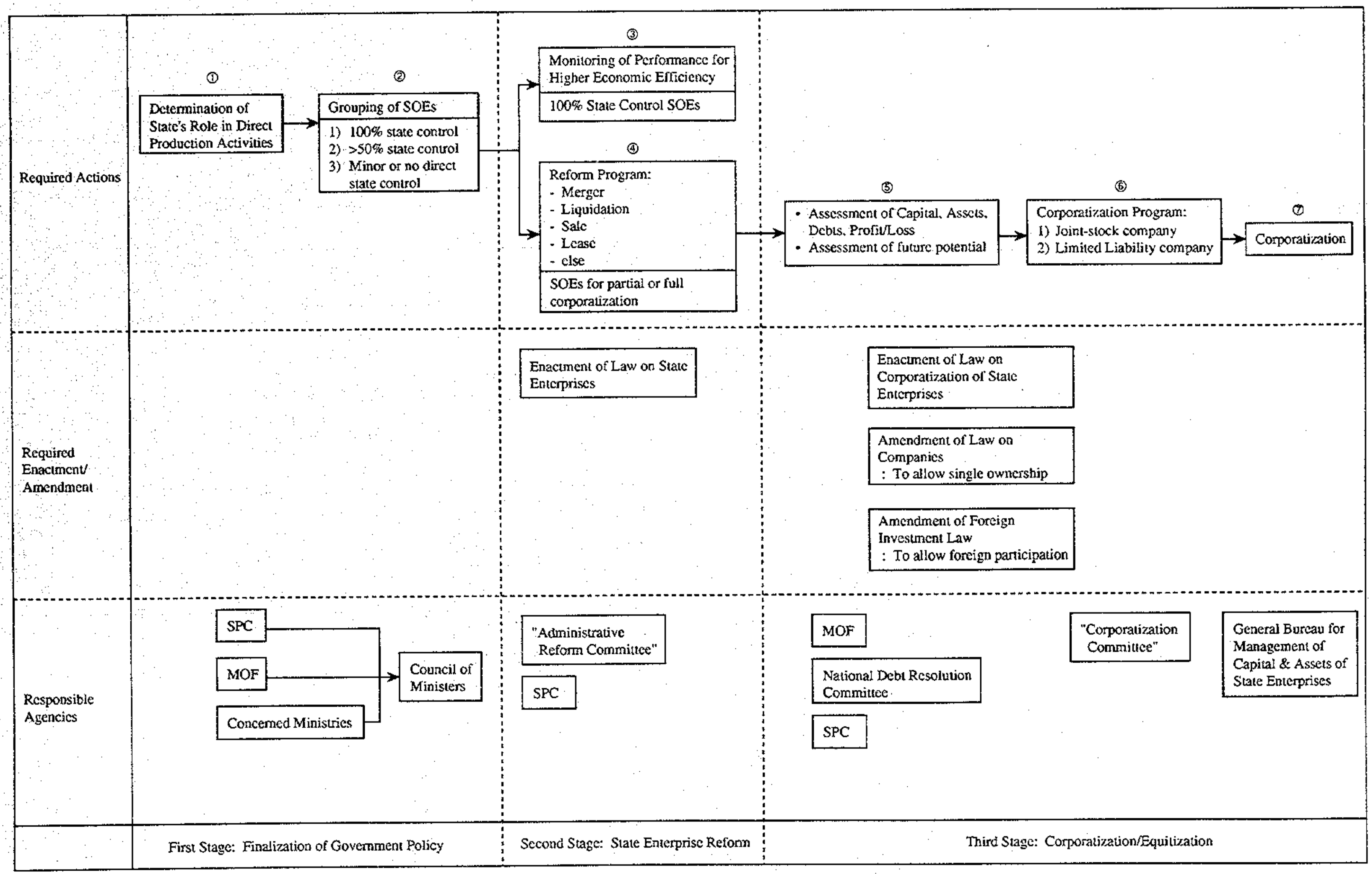


Figure B.3 Possible Flow for Corporatization/Equitization of State Enterprises

Figure B.4 Inter-relationship of Recommendation Points (Financial Reform)

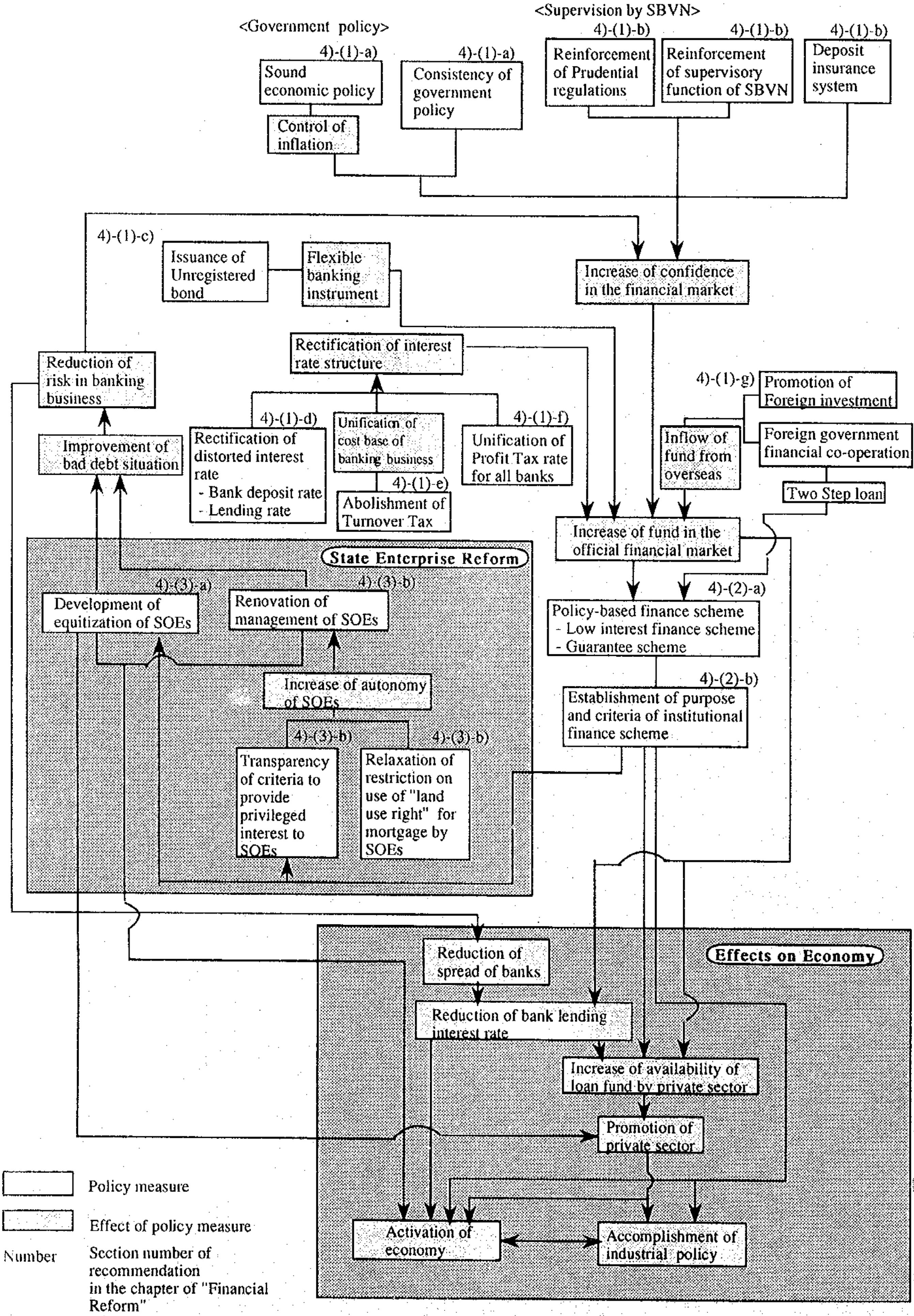
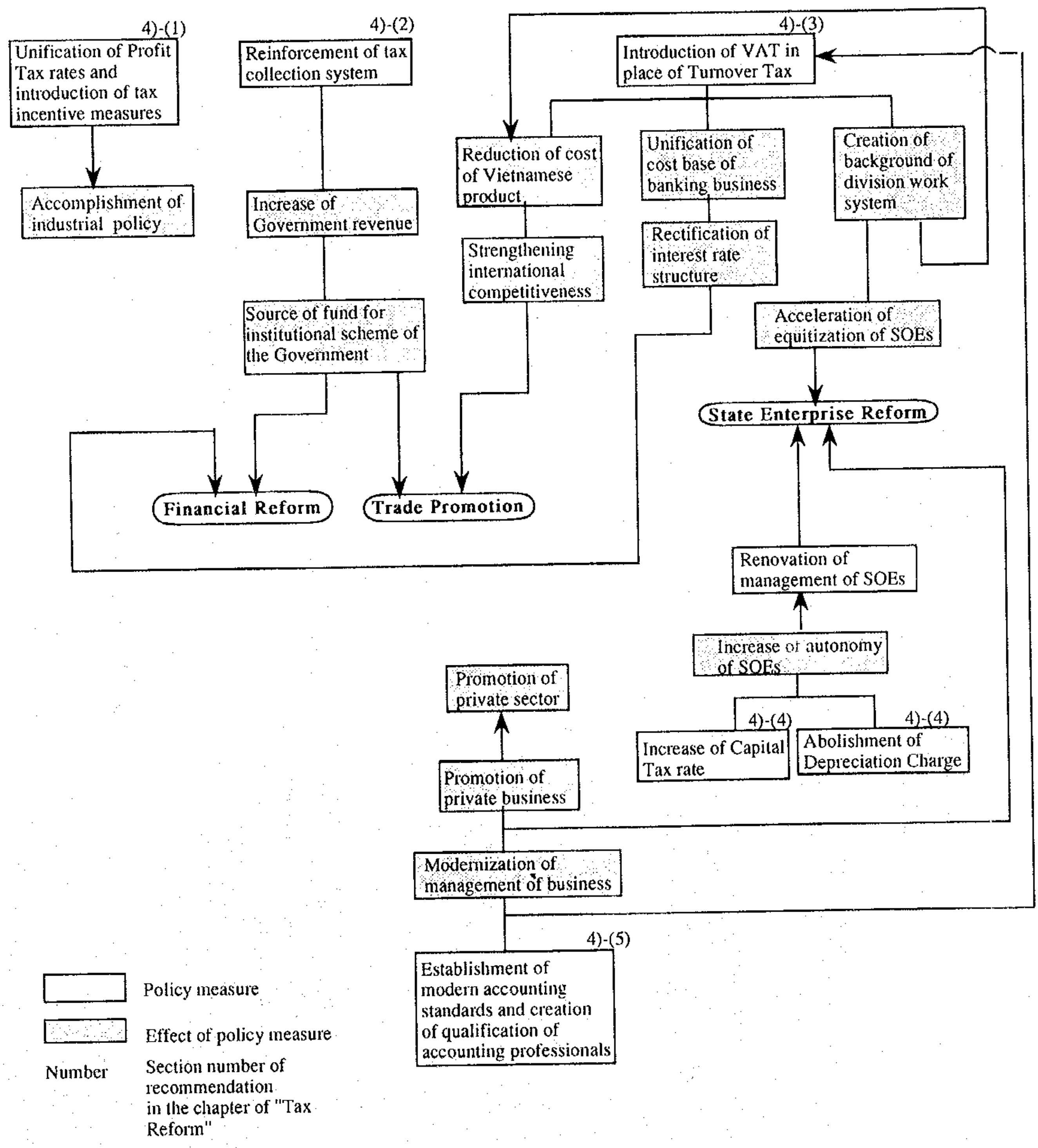


Figure B.5 Inter-relationship of Recommendation Points (Tax Reform)



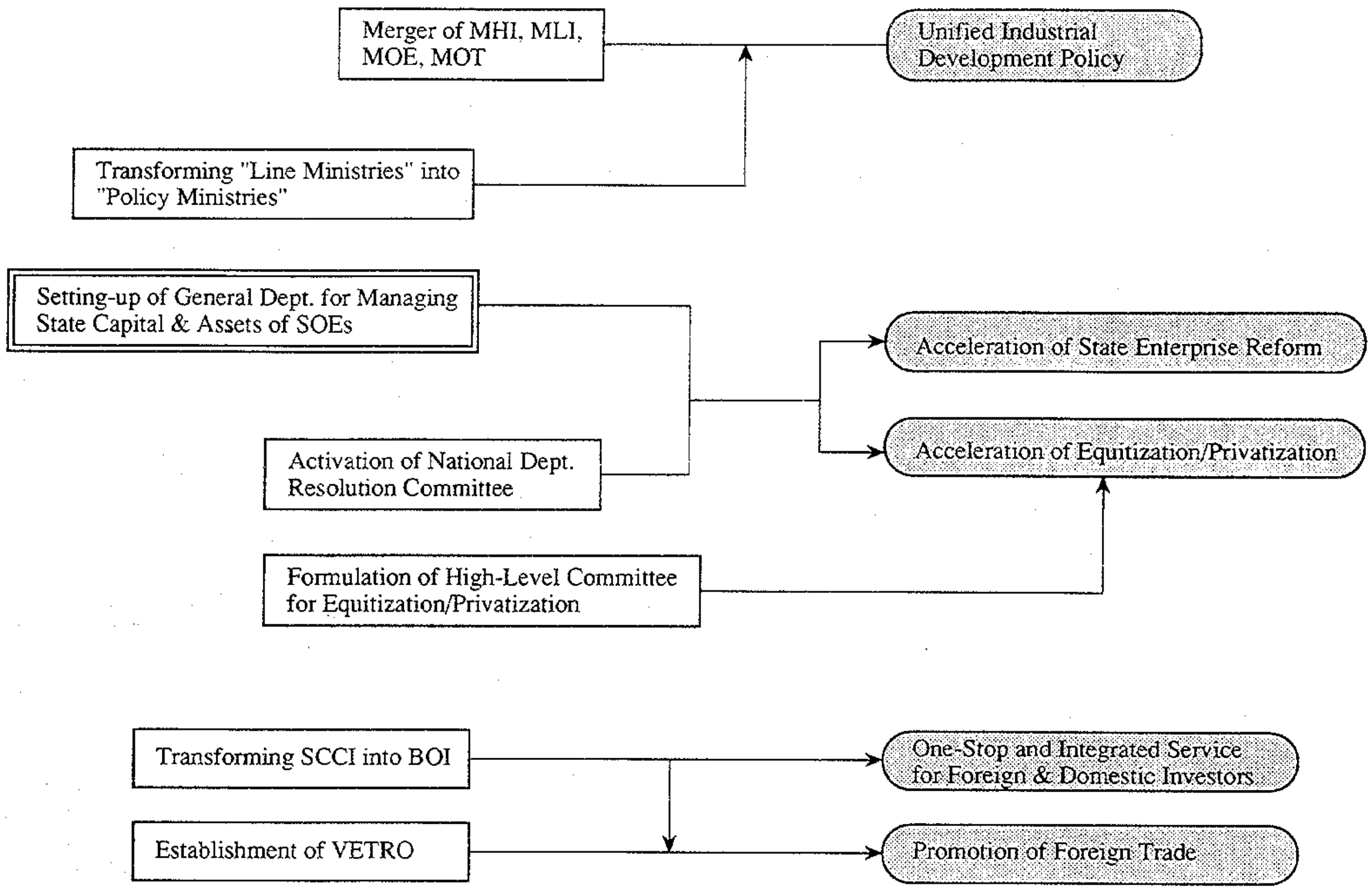


Figure B.6 Direction of Administrative Reform