# How to Speed up Equitization of State-Owned Enterprises

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## I. Introduction

The equitization of state-owned enterprises (SOEs) is an important policy of the Vietnam's Communist Party and Government: The Government has promulgated a lot of decrees and circulars on SOE equitization since June 1992. Recently Prime Minister signed to issue Decree 109 providing guidelines for transforming SOEs into joint stock companies with the following targets:

– Transforming SOEs into joint stock companies under diversified ownership, and attracting funds from foreign and local investors for financial strength, technological innovation, management renovation and business performance and competitiveness promotion.

– Harmonizing interests between the State, enterprises, investors and workers.

– Combining SOE equitization with development of the markets of capital and securities.

After 15 years of equitization, 3,782 SOEs are changed into joint stock companies. The value of state-owned capital is not only preserved but also increased 2.5 times. These businesses have recorded a lot of significant achievements: their sales double, annual net income up 20%, and payment to the state budget up 2-2.5 times. Especially, equitized SOEs have produced profits, played a leading part in the economy. However, these results remain slow in comparison with requirements for international integration. The Government still holds a 46.5% stake, business equity reaches only 12%, and their fund raising is limited. Equitized SOEs still use the same operational methods as state businesses. The former chief executives are not changed, so their management is not really reformed. The equitization lasts for a long time, even 430 days per enterprise. The value of business property is assessed perplexingly and passively and there are a lot of divergent arguments on the equitization of hospitals, schools, public utility businesses, and so on.

As a result, the comprehensive evaluation of SOE equitization over the past years is extremely essential. It helps suggest necessary measures to boost up SOE equitization with a view to reaching the set target by 2010.

## II. Equitization performance over the past years

**1.** The number of SOEs which have gone public increased significantly: Only five enterprises (four located in HCMC) were equitized from June 1992 to December 1995, but the figure soared to 582 in 2000 and 3,782 by December 31, 2006 (See Table 1).

**Table: The number of equitized SOEs over the past years**

| Year | The number of equitized SOEs | Total |
|---|---|---|
| 6.1992 – 1995 | 5 | 5 |
| 1996 | 6 | 11 |
| 1997 | 4 | 15 |
| 1998 | 105 | 120 |
| 1999 | 250 | 370 |
| 2000 | 212 | 582 |
| 2001 | 204 | 786 |
| 2002 | 164 | 950 |
| 2003 | 532 | 1,482 |
| 2004 | 753 | 2,235 |
| 2005 | 754 | 2,989 |
| 2006 | 793 | 3,782 |

Source: Ministry of Planning and Investment

**2.** The SOE equitization has brought real benefits to workers, investors, the State and even the business. The surveys show 92.5% of equitized SOEs are now running profitably, their pre-tax profits increases 2.3 times and their payment to the Treasury rises 26.5% per business. In addition, the state-owned capital is not only preserved but also climbed 2.5 times, productivity up 64%, workers' income up 35%, and working population increasing due to production expansion. As far as investors are concerned, the value of their shares rises 2 to 3 times and their dividends are much higher than the bank interests.

**3.** Equitized SOEs can raise funds by issuing more stocks, so they are important suppliers for the securities market. In turn, the securities market is the channel providing capital for joint stock companies. Just because of this, their financial position becomes stronger than before equitization and they have favorable conditions for innovation of technology and equipment and business expansion.

**4.** Equitized SOEs will do business in compliance with current laws, so they can escape the situation that state administrative agencies like to make specific and deep intervention in the company's affairs, but they reject their responsibility for damages caused by them.

### III. Challenges and limitations in the process of soe equitization

**1.** From June 1992 until now, although the sectors have already equitized 3,782 SOEs, the implementation stays slow as compared to the planned target. The remaining 2,176 SOEs hold nearly 90% of total charter capital, or some VND270,000 billion. Nevertheless, their business efficiency is not worth their existing resources. According to the State Audit's investigation outcomes for 2006, there are still a lot of inefficient SOEs, even in the red for a long time, six out of 21 state corporations' show audited loss of VND351 billion in 2005 and progressive loss of VND985 billion by December 31, 2005. Therefore, this is a big challenge: their slower equitization, their greater losses and their leading role can not be fulfilled.

**2.** Nowadays, state-owned corporations, groups of companies, holding companies hold 100% of total charter capital. Most of them need not have a 100% or 51% stake. The state's holding 46.5% stake partly restricts involvement of strategic and foreign investors. This is also an opportunity for equitized businesses to rely on the state protectionism and dodge fair competition with other sectors in the economy.

**3.** The assessment of SOEs' value before equitization remains inadequate, mainly depending on the experience of the evaluation council for SOE value. Their assessment is not the same in different times, thus making businesses face troubles and waste of time, and even hurdling the equitization process. The underestimation of land-use right can damage state-owned capital. The same effects happened if the value of brands and trade advantages are undervalued. These are very important problems in the process of equitization. The inventory of existing assets as conducted at present cannot reflect intangible and tangible values of the business. Several SOEs have not yet obtained enough legal documents of factory buildings and land-use right, so they find it very hard to be transformed into joint stock companies.

**4.** Those state businesses which have already gone public still operate as before equitization from business planning to profit distribution. Even 80% of enterprises maintain the former management like director general, deputy director general, chief accountant. This easily reduces energy and inventiveness of the business and finally its efficiency. In general, their mind and management have been less renewed in accordance with new conditions of legal status, so their competitive edges are rusty.

**5.** All forms of business cannot enjoy fair treatment in the business climate. Equitized SOEs have not yet adapted themselves to the market mechanism. They still fear that they are not given priority in land allocation, offered unsecured loans, and granted a grace period of debt repayment after equitization.

**6.** The legal framework for equitization is slowly established, and regulations are amended many times, causing obstacles to the equitization process. The procedure for equitization is still complicated, unspecific and cumbersome. The auction sale of stocks is not yet carried out publicly and transparently with asymmetric information. All of this has disappointed investors, hampered the equitization and given rise to negative behaviors in the IPO – initial public offering.

### IV. Measures to boost up soe equitization

#### 1. Conception and objective

SOE equitization is both an inevitable trend in international integration and a breakthrough measure to change the business's ownership.

The Government has planned to equitize 1,500 SOEs from now until 2010. In addition, all affiliated businesses of groups of companies and corporations must complete their equitization by 2008.

#### 2. Measures to spur SOE equitization

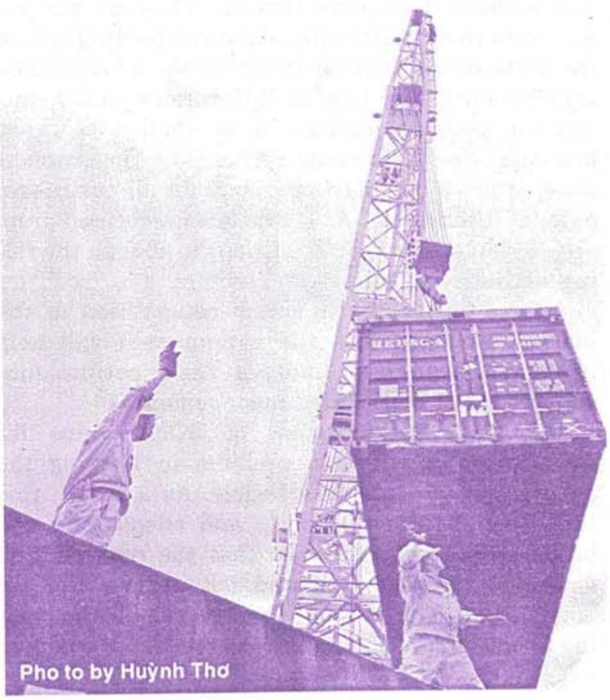
*2.1* Equitized businesses should change old views into new ones about activities in the condition without state protectionism. They are also required to think differently about the leading role of the state sector in order to secure the whole industry's benefits. The Law on Enterprises must be respected seriously because it is applied to every business, every economic sector. The Government must secure a fair playing ground for all businesses without discrimination. If this law is executed properly, it will create good conditions to abolish the ruling authority of ministries, sectors, and localities and force businesses to accept competition in the market economy. Just the environment will help equitized businesses improve their performance and get rid of SOE-styled management.

*2.2* The determination of SOEs' value for equitization is the core problem in keeping the equitization process on schedule. As a result, this task must be done properly and adequately, and based on market factors so that the real value of business's assets is figured out at the time of equitization. The value of their stocks on the trading floor will help justify the assessment of business value.

The value estimation of trade advantages and brands is a hot problem in the SOE equitization process because these factors play a decisive part in the market economy. These intangible assets must be included in the business value to prevent damages and losses to the State. In assessing the business value, the following techniques should be applied: the appropriate market value of total net assets based on independent assessment, comparison with other businesses in the same industry and size. This practice will assist SOEs in their choice of proper methods and they are able to check the reasonableness of the assessment.

*2.3* The state ownership of controlling shares at 33% of total businesses to go public in future is out-fashioned because it easily facilitates the business's desire to maintain the old-styled management, thus reducing their efficiency and limit the shareholding of outside and strategic investors for business expansion after equitization. If equitized businesses can select high-qualified and talented leadership, the Government can still control the business with its stake just from 20 to 30%.

*2.4* The businesses are hunting experienced and skilled chief executives of officers (CEOs) for their expansion and success in the harsh competition. Just because of this, the Government should allow the management board of businesses, corporations and groups of companies which already go public to decide their chief executive officers (CEOs), wages and salaries, and bonuses on the basis of turnover and profit.



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*2.5* The equitized business's IPO in 2007 requires a detailed road map in accordance with the plan of each corporation and group. Obviously, the construction of road map for stock sales in the Government's favor is a factor but not a top priority of equitization because the equitization will be slow and the economy suffers more losses if the State insists on selling for good prices. Furthermore, high IPO prices will cause difficulties to workers' holding stocks in accordance with their rights. In contrast, the stocks with reasonable prices on the securities market have real value, and more opportunities of stock ownership will come to workers.

*2.6* With respect to 71 corporations and groups of companies, the Government has given green light to equitization of the Bank for Foreign Trade (Vietcombank), Bank for Housing Development in the Mekong Delta, Housing Development Corporation (Vinaconex) and 26 large corporations by the end of 2007. Therefore, to implement the road map and organize the general meeting of shareholders by the end of 2007, the Government should instruct ministries, industries and local People's Committees to establish the equitization steering board for each corporation and group. They are also permitted to hire foreign consultants, set up the IPO road map and call for strategic investors.

*2.7* To combine equitization with ownership diversification and enhance efficiency of state management agencies, the State should implement administrative reform strictly and improve the salary system so that the public servants fulfill their responsibility and have motive for promotion.

**Conclusion**

In short, the country's SOE equitization is a proper decision to deal with shortcomings of ineffective performance of SOEs. The evidence shows equitized SOEs have recorded significant achievements; nevertheless, the equitization pace remains slow in comparison with development requirements. As a result, the SOE equitization should be boosted up with the above-mentioned measures along with every business's strong efforts with the aim to reach the planned targets of basic SOE equitization by 2010. ■

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