HOW TO CARRY OUT THE EQUITIZATION PROGRAM EFFECTIVELY?

by TRẦN TÔ TỬ

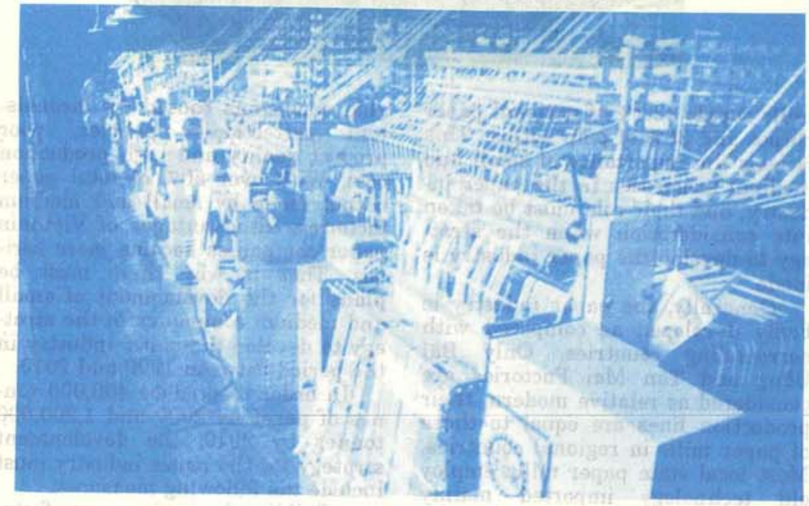
On April 4, 1997, the Politburo issued the Official Statement 63-TB/TW about the task of keeping on equitizing some state companies (SCs) effectively. This program has been affirmed by both the Party and the National Assembly. From 1992 till now, the Government and related ministries have tried to carry out this program but only 10 SCs were changed into joint stock companies (JSCs), therefore many people are of the opinion that this program was carried out too slowly. So the problem is how to carry it out more effectively.

I. THE PAST EQUITIZATION PROCESS: SLOW OR FAST?

Many experts said that the equitization of SCs had taken place at the highest speed in HCMC than in any other provinces, but in fact, this speed was very slow if we set it against what required in implementing a policy set forth by the Party and the Government since 1987.

In reality, it's difficult to assess the equitization as slow or fast because we had no master plan for this program which enables us to make correct assessments.

In present conditions when both policy-makers, managers and the public have just begun to get accustomed to the form of JSC and stock exchange, when the Companies Act hasn't been completed and we had no experience of selling a company then we can consider the equitization of several SCs within some years as fast enough. On the other hand, if we take the demand for rapid equitization with a view to restructuring the system of SCs and making the public sector financially strong enough to play the leading role in the economy into consideration, then the speed of equitization in the past few years was too slow.



Thus, the speed of equitization isn't the problem when the Government hasn't set forth a master plan with clear-stated targets for it. What we should pay attention to are how this program was carried out and what lessons could be drawn from this process.

Unfortunately, the pilot scheme to equitize some SCs in the past hasn't been summed up while the Decree 28/CP has intented to introduce this program at a larger scale. Up to now, the pilot scheme to equitize SCs in the past provided no experience needed for the equitization of SCs in banking and finance, tourist, foreign trade, communications, and agricultural businesses. So there is no surprise when this program in HCMC met with a lot of difficulties which require the Government to find out appropriate solutions.

II. HAS PROPER ATTENTION BEEN PAID TO THE EQUITIZATIONS?

JSCs could easily attract dead money from the public in general, so to encourage the development of this form of company becomes a indispensable measure to accumu late capital and improve company' production capacity and competitive ness. In Vietnam, JSCs could be se up by: allowing private persons t form new ones, and changing SC into JSCs through equitization.

At present, speaking of equitiza tion, many people thought only o SCs, but in fact, all kinds of com pany, including joint ventures, for eign-owned companies, limited an private companies, could be als equitized.

Regarding the system of SCs most of existing 7,000 SCs in Vietnam are of small or medium size and used to depend on grants - in-aid. When this source of finance failed to meet the demand for development of these SCs in recent years, they started to rely on bank credit and open credit offered by foreign exporters.

After the Decree 59/CP was issued, commercial banks started to limit the volume of credit supplied to an SC to the amount of capital held by SC, so many SCs met with financial difficulties. In 1997, it became apparent that all SCs with small capital (only VNĐ3 or 4 billion each) would find it difficult to accumulate enough money to modernize their production lines and expand their businesses.

To solve this problem, most SCs could only think of going into a joint venture with foreign partners instead to equitizing their businesses. Some SCs, having no chance to cooperate with foreign companies, tried to remain state - run companies and avoided equitization. Their attitude towards the equitization raises a lot of questions.

In recent years, the Government as stressed the role and the importance of the domestic source of capial, however, the equitization rogram, as a measure to mobilize ead money in the public, has been ealized slowly. Many provincial uthorities paid no attention to this rogram. So it's difficult to make donestic investment equal to foreign ne as planned by the national fiancial strategy.

II. IS EQUITIZATION PRIVATIZATION?

The opinion considering equitizaion as privatization, or as deviation rom the socialist orientation has ecome an obstacle to this program. Many local authorities and departnents have been reluctant to carry ut this program. Up to now, many eople are still of the opinion that equitization is only a euphemism for rivatization. So it's necessary to larify these concepts.

It's worth noting that the Party has already adopted the policy to diversify ownership of businesses and the equitization of SCs is a measure to realize this policy, or in other words, the equitization is a process in which a state - owned company changes into a joint stock company owned by shareholders, and certainly the Government could become an important shareholder if need be.

On the other hand, the privatization is a process in which a business under the state control and ownership is transferred to private ownership (sometimes, only the control, not ownership, is transferred).

Thus, the equitization program encourages all sectors and all social classes to engage in business, that is, to put dead money in productive activities.

IV. OBJECTIVES OF THE EQUITIZATION PROGRAM

The Decree 28/CP pointed up two objectives of the equitization of an SC:

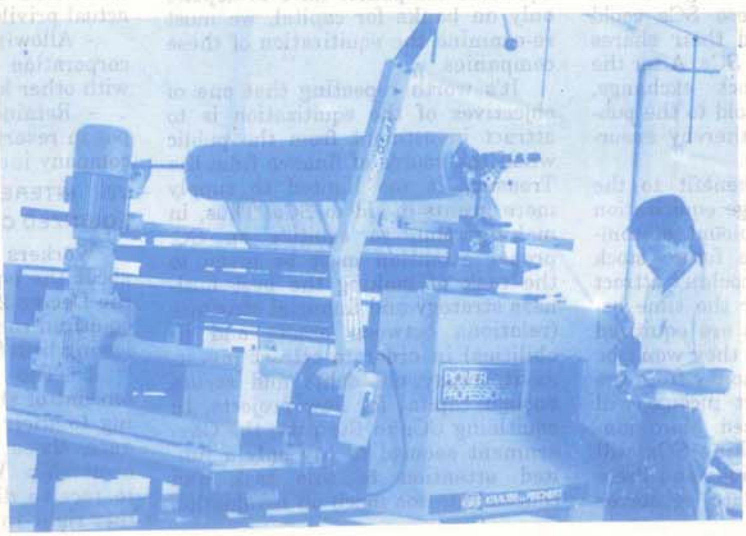
- Attracting investments from the company's personnel, private persons and organizations (both native and foreign ones) in order to modernize and develop business.
- Turning investors and company's personnel into shareholders of the company, thereby encouraging them to improve company's performance.

The Party and the Government have adopted the policy to diversify ownership of businesses with a view to making Vietnamese companies more competitive, however, this policy hasn't been realized successfully, and as a result, local companies couldn't compete against foreign giants. To solve this problem, the Government has to take measure to support local companies, and these companies have to cooperate with one another in order to survive and develop. In this effort, they can choose bewtween horizontal and vertical amalgamation.

Through amalgamation, the public sector could penetrate into the private sector and play the leading role by buying qualification shares instead of using administrative measures to take control of the company. Moreover, state - run corporations, through amalgamation, could avoid difficulties in internal control and attracting capital from businesses in other sectors in order to forming bigger groups.

Thus, a company which doesn't aim at the two above -mentioned objectives could consider the equitization as a long-range strategy to combine two or more companies into one organization in order to improve their profit making performance. This could be seen as the third objective of equitization. However, before equitization, it's necessary to decide what objective is the most important in order to select appropriate measures.

If the equitization of an SC aims at mobilizing more capital, the company can choose to issue shares to both company's personnel and the public in general and limit the amount of shares sold on credit to company's personnel to the minimum because the company is in need of capital.



If the main objective is to change company's personnel into shareholders, different measures will be taken to help its personnel buy shares (selling them on credit for example) and limit the amount of shares sold to the Government and the public.

If the company wants to form cooperative relations with other concerns, then the better part of shares will be offered to company's trading partners and the amount of shares sold to company's personnel will be limited.

V. WHAT COMPANIES AND METHODS OF EQUITIZING WILL WE CHOOSE ?

One of difficulties in equitizing SCs is the task of choosing companies to be equitized, although the Decree 28/CP stated that an SC would be chosen to be equitized on the following conditions: (1) having small or medium size, (2) not being the type of companies which must be owned totally by the Government, and (3) having feasible development plan.

SCs with financial difficulties or loss - making SCs will be certainly unattractive in the eyes of investors, so it's difficult to equitize them, but the Government will be reluctant to equitize successful companies because they provide the Treasury with stable income. Other companies making no big loss or profit all want to remain SCs or cooperate with foreign partners instead of being equitized.

To solve this problem, the Government had better consider the following measures:

1. The Government can decide on equitizing an SC without consulting with the SC leadership : because the State Companies Act allows the Government to do it if this act is suitable to the strategy to restructure the system of SCs.
2. The Government has to rearrange the system of SCs and the distribution of grants-in-aid and subsidies. After rearrangement, three lists must be made: companies to be dis-

solved; companies to be equitized and companies to be maintained within state corporations.

3. As for loss-making companies, or profit-making ones which need not to be under state ownership, the Government can equitize them by two steps:

- Changing an SC into a private limited company with at least 7 members who are other SCs: In this stage, the equitized SC is still under the public ownership.

- Changing this private limited company into a public limited company after several years of operation: In this stage, those member SCs will sell all, or a part, of their shares to the public according to the objectives set forth for the equitization of this SC.

This 2-stage equitization is of great benefit to the economy and the Treasury as well.

If the SC in question is making loss and unattractive in the eyes of investors, nobody will buy its shares, or its shares must be sold at knock-out price at the expense of budget income. So the Government had better change it into a private company owner by a group of SCs who will carry out a program to improve the company performance. When the company's financial situation is better, it could be turned into a public limited company and its shares could be sold at reasonable prices in the stock exchange that would be formed in the coming years. By doing so, the budget income is assured.

As for profitable SCs, if they are equitized before a stock exchange is formed, their shares couldn't be as high as they are sold by auction in the stock exchange. Thus at present, when the stock exchange hasn't come into being, these SCs could also be equitized and their shares are only sold to other SCs. After the establishment of stock exchange, those shares will be sold to the public at market price, thereby ensuring the budget income.

Considering the benefit to the economy, this 2 - stage equitization could increase the amount of commodity traded in the future stock exchange although it couldn't attract much dead money for the time being. Moreover, if SCs are equitized through existing way, they won't be able to attract dead money from the public and the budget income will not increase as expected. More dangerously, if loss - making SCs still exist in state corporations and there is no plan to regulate resources among member SCs of the corporation these loss-making SCs will certainly go bankrupt.

The 2-stage equitization will allow a reasonable distribution of resources among member SCs and help to remove barriers between different managing and regulating bodies, and between central and local authorities.

VI. WHY DID EQUITIZED COMPANIES MEET WITH DIFFICULTY IN SECURING BANK LOANS?

Many equitized companies met with this difficulty and made other SCs worry in spite of the fact that the Article 10 of the Decree 28/CP affirmed that: "Equitized companies are allowed to borrow money from state commercial banks enjoying the same status and interest rate as SCs". But state commercial banks are also bound by banking regulations.

This fact causes no surprise because in the past, all debts owed by SCs were guaranteed by the government without limit, that is why state commercial banks are always ready to supply loans to SCs. When these SCs become JSCs which are limited by guarantee, banks will certainly consider the borrowers solvency before supplying loans. At present, the State Companies Act and the Decree 59/CP affirmed that SCs are limited liability companies, therefore both SCs and equitized companies met with difficulty in borrowing from banks.

Then what is the cause of this situation? In the market economy, limited companies are those which have the biggest ability to attract money from the public by issuing bonds, bills and shares. Then if equitized companies have to depend only on banks for capital, we must re-examine the equitization of these companies.

It's worth repeating that one of objectives of the equitization is to attract investment from the public when the source of finance from the Treasury is too limited to supply more grants-in-aid to SCs. Thus, in making plan to equitize an SC, proper attention must be given to the task of making the best business strategy and financial structure (relations between assets and liabilities) in order to attract investment, repay old debts and secure enough capital for new projects. In equitizing SCs in the past, the Government seemed to pay only a limited attention to this task and concentrate too much on revaluation of assets of SCs which would b equitized.

We had better remember tha equitization means not only an ac of changing a business into a JSC but also an effort to modernize an improve the health of a company' finances.

VII . PREFERENTIAL TREATMENT O EQUITIZED COMPANIES

According to the Decree 28/CF an equitized company enjoys the fol lowing privileges:

- A reduction of 50% in corpora tion tax for the first two years afte coming into operation under th Companies Act.

- An exemption from registratio fees when assets of equitized SC ar transferred to the JSC.

- Before equitization, fund for bo nus and benefit could be divide among company's personnel in orde to help them buy shares.

- Equitized companies are al lowed to borrow money from stat commercial banks enjoying th same status and interest rate a SCs.

- Equitized companies can im port or export goods as allowed b law.

- Reasonable and necessar spendings during equitization ar allowed, with approval from th Ministry of Finance, to be added t the value of company.

However, only two privileges are really of some value: a reduction in corporation tax and an exemption from registration fees. Other privileges allowed by the said Decree have been offered to all kinds o company.

To encourage the equitization and formation of JSCs, the Government had better grant them such actual privileges as:

- Allowing JSCs to enjoy lower corporation tax rates as compared with other kinds of company.

- Retained profits that will be put in reserve fund are exempt from company income tax.

VIII. INTERESTS OF WORKERS OF EQUITIZED COMPANY

Workers are also worried a lot about the equitization. According to the Decree 28/CP, the workers of an equitized company enjoy the two following benefits:

1. The Government gives an amount of shares to workers according to their seniority and performance, these shares are under state ownership. Workers have the right to receive dividend and to transfer this right to their child working for

the company but they aren't allowed to sell these shares. The value of shares granted to a worker won't be higher than his/her 6-months' salary. The total amount of these shares won't top 10% of the company's value. The worker enjoys this right for life.

- In fact, this regulation allows workers to receive divident while the share is still under state ownership, or in other words, the Government possesses shares and workers a kind of coupon giving them the right to receive dividend. Thus, the Government had better make a change to this regulation and it could read as follows: Workers are provided with a kind of dividend warrant allowing them to receive dividend derived from shares owned by the Government.

- Another problem is that where this dividend warrant (or the right to receive dividend) will go if the worker stops working for the company and has no child working there. Moreover, if the Government sells these shares to the public through the future stock exchange, then the worker will lose this right to new shareholder. So the Government had better solve this problem before equitizing the company. The following are our suggestions:

+ As for the worker who stops working for the company and has no child working there, he/she is allowed to enjoy the right to receive dividend for life if he/she comes to retiring age or retires on medical grounds. If he/she changes his/her job, he/she is allowed to enjoy this right for one more year before it is transferred to another worker in the company.

+ If the Government wants to sell the share, the worker will be the first one who has the right to buy it and the government must give the worker proper notice of the sale.

2. Workers are allowed to pay for an amount of shares within five years with an interest rate of 4% a year. The total amount of shares sold on credit to workers won't top 15% of company's value (this percentage increases to 20% in companies that own at least 40% of company's value). The amount of shares sold on credit to a worker mustn't top the amount he/she buys and pays in cash. If the worker fails to keep up the instalments for two successive years, he/she must return shares to the Government. Before paying the last instalment, the worker isn't allowed to transfer these shares to other persons.

This regulation causes a lot of problems:

- Workers who have money enough to pay in cash for an amount of shares, are allowed to buy the same amount on credit, if the market price of share increases, the gap between rich and poor workers in the company will widen and the rich will become richer. This result is contrary to our socialist orientation.

- On the other hand, if the market price of share decreases, workers who buy shares on credit will stop paying their instalments in the hope of returning shares to the Government because the price of this share is lower than its face value so they would rather return shares than pay instalment.

This result could be considered as favorable for workers if they are allowed to buy shares on credit according to heir seniority and personal performance. This result is undesirable in respect of shares bought on credit according to personal finances.

In order to encourage company's personnel to buy shares and prevent the gap between rich and poor workers, and between managers and laborers as well, from widening, certain measure must be taken to protect workers' interests.

+ According to current regulations, workers who are provided with dividend warrants must be official employees or contract workers for at least three years. We think that the Government had better sell shares to retired workers because they have contributed something to the present company's value.

+ According to regulations, the value of shares granted to each worker doesn't top his/her six months' salary. We think that this value of shares could equal six months' salary if they are granted to a worker with one year's seniority, and for every two years the worker works for the company, he/she will be granted an amount of shares that equals his/her one month's salary. This practice will encourage workers to have a loyalty to the company.

+ The sale of shares on credit to workers should be based on their seniority and performance. In addition, other measures to help poor workers buy shares must be also taken, such as: giving them five years' credit, allowing them to make payment by monthly or quarterly instalments, etc.

IX. HOW TO SETTLE DEBTS AND PAID - UP CAPITAL AFTER EQUITIZATION?

This is one of worrisome problems to SCs before equitization although they recognize that equitization will help improve their financial situation.

All companies have financial problems to be solved before equitization. Settling debts is also a problem to the process of making financial plans. Companies have to negotiate with debtors and creditors about ways of settling debts, except for the cases in which existing assets aren't big enough to repay debts. In these cases, assets of the company are too small to be equitized.

As for paid-up capital in joint ventures, the three following problems must be dealt with in equitizing an SC:

1. To make a plan to settle paid-up capital in joint venture: up to now, there is no solution to this problem, therefore we want to suggest here some solutions:

a. To transfer the paid-up capital to another SC which will work in partnership with foreign parties.

b. Before equitization the company will keep on holding the ownership of the paid-up capital which will be considered as a part of assets being equitized. The equitized company will be the owner of this paid-up capital and the new partner in the joint venture.

c. The paid up capital is also equitized, that is, the Government will carry out a pilot scheme to equitize a joint venture. It's a new way to diversify ownership in joint ventures.

2. To open negotiation with foreign party about plans to settle this paid-up capital: According to the Foreign Investment Law, a joint venture is a limited company, the transfer of share capital must be agreed on by related parties. Taking the solution (b) for example, the paid-up capital of the SC, after equitization will be under joint ownership, so this transfer must be accepted by other parties in the joint venture, because these parties will decide whether they want to work in partnership with the new party or not.

3. To evaluate the paid-up capital: value of this capital will increase or decrease depending on business performance and prospect of the joint venture. This value will be taken into consideration when assets of the SC is revaluated before the equitization, if we take the solution (b)■