

### 1. Regional and global situation

In the Asian financial crisis, many Southeast Asian countries have fallen prey of speculation of financial investors. Flows of foreign investment have gone rushing to emerging markets regardless of risk,

caused many currencies and stock indexes in different countries to fall by 30-60%. It's worth noting that the Asian financial crisis was far beyond our knowledge of traditional market crises. This is the crisis in the structure of the economy. It spread around the world and

isn't a convertible one so it doesn't induce financial speculation; (2) the dynamic of economic growth is strong because of low personal income; (3) import-substituting industrialization is at its first stage, so the economy is less vulnerable to changes in external demand as

will be in a danger of separating itself from the world market.

The Vietnamese leadership have become aware of these effects on the economy, especially on foreign trade, foreign investment and internal value of the domestic currency, and these effects made

# THE ROLE OF SMALL AND MEDIUM BUSINESSES IN THE VIETNAMESE ECONOMIC REFORM



and then rushed away suddenly causing great damage to economies that have once been considered as Asian economic miracles.

The financial crisis made many economists understand fully the vulnerability of the financial and banking systems which, after a boom period, have accumulated too many doubtful debts and unsecured loans. The crisis

caused different countries to suffer damage at the extent of their involvement in the global economy.

Vietnam, fortunately, was affected less badly by the financial crisis than its surrounding countries were. According to David O. Dapice from the Harvard International Development Institute, reasons for this situation are: (1) the Vietnamese currency

long as the low saving rate is made up for by foreign investment. However, he warned that Vietnam isn't free from bad effects of the crisis, they are only slow to come. If no important changes are made to financial, investment and monetary policies, there will be no hope of regaining the high growth rate of the past few years and Vietnam

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such existing shortcomings as poor labor productivity and international competitiveness more obvious.

In such a situation, we want to discuss here the role of small and medium businesses (SMBs) in the economic reform in Vietnam.

### 2. Looking back at the starting point

The economic reform in Vietnam is considered as an effort to save the country from the socio-economic crisis in the late 1970s and early 1980s. Many reasons have combined to bring the country to the brink of ruin but the most important are the collapse of the centrally-planned and subsidized economic model that accepts only the state and collectivist ownership, and the isolation from the active and changeable world economy.

The introduction of the market mechanism of mixed economy, or the recognition of different forms of ownership, has created a new dynamic

for the economic reform and saved the country from the danger of collapse. The recognition of different forms of ownership in the market economy is the breakthrough that saved the situation and created the new dynamic for the Vietnamese economic growth in the past 15 years. From that breakthrough started the struggle for the new and against the old. The role of SMBs is also established during this struggle.

### 3. Businesspersons and the burden of history

In Vietnam, up to 1954, trading and handicraft were still considered as subsidiary occupations and were held in low regard by everybody because of Confucian teachings which were adopted by the ruling class as the orthodox policy. In the socialist North Vietnam, businesspersons were classified as the capitalists, one of enemies of the regime, that should be overthrown forever. This repeated in the South after 1975 with the policy to reform private trading and industrial businesses. This policy, in fact, put businesspersons in an opposite position.

In the centrally-planned and subsidized mechanism, there was no place for businesspersons who were considered as "the capitalist class struggling for survival". The prolonged and serious socio-economic crisis signaling the collapse of this mechanism, a mechanism that is totally alien to the socialism as Phạm Văn Đồng put it, led to the birth of the socialism-oriented mixed economy in Vietnam.

Changes in economic thinking gave rise to new concept of business circle and its important role in the market economy. However, everything didn't change overnight especially when the legal infrastructure isn't perfect

and the free market is still captured by powerful vested interests.

### 4. SMBs and the struggle for full employment

In the mixed economy operating according to the market mechanism, all assets could be changed into cash and into productive investment. The decision to make investment depends on many factors: one's frame of mind, habit of using money, trust in legal infrastructure, investment climate, etc. Regarding the national interests, more investment means better economic growth and social progress.

A regulation made on June 20, 1998 by the Government classified all concerns whose capital is under VND5 billion and labor force is under 200 workers as SMBs. According to this regulation, 80% of existing companies of all sectors in Vietnam are SMBs. They employ some 25% of the working population and account for some 24% of the GDP. However, SMBs have made poor progress in recent years, the amount of dead money turned into investment is still small and fails to meet the market demand, and most people still feel reluctant to make investment. It's worth noting that many private persons don't want to form private businesses and companies. Certain family businesses (classified by Decree 66 issued on March 2, 1992) refused to change into private businesses or companies when their size became big enough, and many private businesses applied for permission to dissolve and turn into family businesses. In other words, many businesspersons don't want to make the size of their businesses known, or in fact, they think they couldn't do their business well if they form private businesses or companies.

Measures taken by the Government to deal with

difficulties ahead are: "making use of internal resources, expanding foreign cooperation, maintaining political stability and accelerating the industrialization and modernization program" and "agriculture and rural areas are a basis for and dynamic of the industrialization and modernization". In our opinion, the SMB is the most suitable form to make the best use of internal resources, or more exactly, the main reason for developing SMBs is their ability to create new jobs and reduce the unemployment rate, one of the most urgent problems in Vietnam today.

In the Vietnamese population structure, the under-fifteens represent 45%, the unemployment rate is around 6% (this rate in big cities rises to over 10%). Some 80% of the population is living in rural areas, but only some 10 million work days a year are needed. Subsidiary occupations, even in areas with traditional handicraft business haven't been able to meet the demand for employment.

When the labor force employed by the public sector tends to reduce because of the rearrangement of state-run companies, the labor force in non-state sectors is on the increase, from 1.5 million persons in 1990 to 2.1 million in 1993 and 2.4 million in mid-1995, not including some one million laborers who take part-time jobs in family businesses, however, this amount is still small in comparison with the increasing number of unemployed laborers.

Industrial parks and export processing zones also offer a lot of new jobs. Up to December 1997, 45 IPs and 3 EPZs all over the country have employed some 65,000 laborers (some 40,000 of them come from HCMC and Đồng Nai).

However, a closer look

will reveal new facts of the matter:

+ After state-run companies were rearranged in 1990-92, the laborers employed by the public sector reduced to 1.78 million, that is, 400,000 were redundancies. By the end of 1995, more 60,000 laborers lost their jobs and the labor force in this sector fell to 1.72 million.

+ During this 5-year period, the foreign sector, with better resources and more favorable conditions, could only create some 50,000 jobs.

Thus, those two sectors that enjoy preferential treatment from the Government, didn't offer more job opportunities to laborers in the years 1991-1995.

+ In HCMC where the public sector controls some 70% of tangible assets, it's the private sector that employs 77% of the local working population.

Statistics gathered in HCMC in recent years also show that non-state sectors, in comparison with others, could create the biggest amount of new jobs and at the lowest cost and the fastest speed.

According to a report of the World Bank, the state-run company needs US\$18,000 on average to create a new job while SMBs need only some US\$800.

These facts should be taken into consideration along with the decreasing rate of job creation after 1996 whereas this rate was equal to the growth rate of working population. In 1997, the rate of job creation was under 0.6% for the first time since the economic reform was introduced. Employment also reduced by 6.2% in agriculture and 5.6% in manufacturing industry that year.

Fall in new jobs offered by the manufacturing sector was probably due to the fact that industrial production requires big investment. Half the redundancies from the

manufacturing sector found new jobs in service businesses in rural areas and one third of them in services in cities in spite of their low labor productivity. The decreasing growth rate of the service sector has also reduced job opportunities for laborers.

The low growth rate of the service sector also reflected the poor performance of the banking system and the slump in trading and real estate businesses. The low growth rate of the tourism was due to the fact that Vietnam became less attractive than surrounding countries did.

The above-mentioned facts immediately produced bad effects on employment which is always a vulnerable and sensitive problem. But the most urgent is the matter of labor and employment in rural areas where 90% of the poor live.

As we know, the economic reform was started first in rural areas and at present, to deal with challenges posed by the Asian financial crisis, we should go on with the economic reform. When the agriculture and rural areas are considered as a basis for and dynamic of the industrialization and modernization, changes in rural areas will affect greatly big cities and the manufacturing industry, and the national socio-economic life as a whole.

Hunger eradication and poverty alleviation in Vietnam in recent years was an impressive achievement. The WB report remarked that the proportion of the poor in Vietnam reduced from 70% in the mid-1980s to 50% in 1993 and somewhere between 30% and 35% at present. Only a few countries could gain high growth rates and its wealth is distributed so evenly.

However, this report also warned us that our progress was under threat because if no strong measures were taken to prevent

falls in the growth rate, the poverty would be more serious in the next two years. The increasing poverty will lead to labor surplus in rural areas, these unemployed laborers will go to big cities where some six million laborers are jobless.

How to solve the unemployment in rural areas? The Government has adopted many policy to develop the agriculture and rural areas. It's easy to see that the success of a rural development program depends mainly on the job-creating rate in non-farming businesses. Foreign experience shows that the best way to improve personal income in rural areas without causing flows of migrants to big cities is to industrialize and modernize rural areas strongly. This is what Vietnam is trying to realize although it still faces many difficulties (shortage of capital, know-how and skilled workers). At present, most of 24,000 businesses operating in rural areas are family businesses. Some 70% of them need bank loan but less than 15% could secure it.

After the Land Law was promulgated in 1993, all kinds of farm started to develop in rural areas. In Yên Bái for example, farms represent 11% of farming households and account for 60% of exports from this province. These farms have helped form a forest of 60,000 hectares. The average area of these farms is 6.13ha. Some 70% of farm area is in hills and 13.7% is from old farming fields. Some 29% of these farms have less than 6.13ha but medium-size farms (over 10ha each) represent 24%. Commercial farming started to develop: from 60% to 80% of their produce is put up for sale, this percentage even rises to 95% in certain farms producing rubber, coffee and tea.

However, these farms developed mainly in moun-

tainous areas where the population density is low and most farm area is based on land allocated by state-run farms. These farms could be seen as SMBs in rural areas.

In lowlands where the population density is high, however, the formation of farms isn't the solution to the matter of unemployment, but the best one is to develop non-farming businesses. What is badly needed now is an open policy to encourage investment in these businesses in rural areas.

In recent years, the number of SMBs in the service sector is higher than in the manufacturing one, the number of trading companies increased by three times while the number of construction companies and other service businesses increased by two times. These facts mean that SMBs prefer the service sector to the manufacturing one because they meet with less competition from state-run companies.

In the manufacturing sector, SMBs have developed rather slowly and represented only 2% of the industrial output while foreign experience shows

that only privately-run SMBs could produce consumer goods for export at competitive price and manage their production very well.

While SMBs in the manufacturing sector develop slowly, the working population keep on increasing at a rate of 1.33 million persons a year. Calculations show that in the years 1996-2010, some two million new jobs are needed.

In the past decade, the Resolution 10 to reform the management of agricultural production changed the face of rural areas and produced good effects on cities and the manufacturing sector, and now a policy of this kind is needed to free SMBs from political restrictions and public prejudice and encourage their development, especially in labor-intensive industries, agro-industries and production of exports. Their development will certainly help reduce the unemployment rate in both rural areas and cities, improve the living standard of rural residents and accelerate the anti-poverty and anti-hunger programs.

