

Small and Medium Enterprises in Cần Thơ and Financial Leasing Service

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Resolute 45-NQ/TW dated Feb. 17, 2005 by the Politburo on development of Cần Thơ City in the national industrialization period set the following target up to 2020: "Developing Cần Thơ into a civilized, modern, green and beautiful city of national level as a gateway to the Mekong Delta; a center of industrial production, trading, service, tourism and foreign trade; and a financial center of the Mekong Delta."

From 2005 on, support from the central government and other provinces, and joint effort by local government and residents, Cần Thơ City has made good progress. Its gross product rose steadily over years, from VND8,546.43 billion in 2005 to 9,938.89 in 2006 and some 11,543 billion in 2007.

Its development, however, is not sustainable and failed to reach its full potential. Up to the end of November 2007, there were 4,618 companies in the city and 95.8% of them were of small and medium sizes. They are badly in need of long- and medium-term capital for replacement of their machines and production lines in an effort to improve their competitiveness and product quality. They are meeting with difficulties in securing bank loans of such terms because of banks' demand for some security and complicated procedures. Meanwhile, the financial leasing service is very suitable for them but it hasn't been common in this city.

1. Small and medium enterprises in Cần Thơ City

Up to Dec. 31, 1999, there were 1,035 SMEs in Cần Thơ and this figure has rose to 4,618 by

November 2007 due to the more open Companies Law and new position as a city of Cần Thơ, but this figure is still small in comparison with other cities in Vietnam.

Of the number of SMEs in November 2007, 57.42% of them were private businesses; 36.4% were limited companies; 5.96% were joint stock companies while state-owned companies only accounted for 0.2% after the reform in the public sector. Regarding industries, 52.44% of them were in the manufacturing and construction sector; 4.4% in the service sector and 11.63% in other fields.

Facing the shortage of capital, most SMEs in Cần Thơ have to borrow from usurers because they can't get access to formal sources of credit. According to a survey by the MPDF, 69.5% of small enterprises and 47% of medium ones in Vietnam are badly in need of capital. Of managers who answered the survey, 53% said SMEs in Vietnam lacked capital for new investment projects and 39% said they lacked working capital.

As for SMEs in Cần Thơ, my survey produced the same results. Only 30.1% of SMEs tried and succeeded in getting access to bank loans, government supporting funds or support from foreign institutions; the rest were rejected and had to secure needed capital from other sources.

The shortage of capital has become a great obstacle to replacement of machinery and production lines in Cần Thơ - based SMEs. According to a survey of the Cần Thơ Institute of Economics in 2007, over 40% of SMEs had the index of wear and tear

for their fixed assets of 50% or more. Some 55% of 1,000 surveyed SMEs employed inconsistent machinery, that is, machines from various countries and depend on various technologies.

My survey of machines employed by 251 SMEs in Cần Thơ in 2007 shows that 32 SMEs (12.75%) had machines of five years old or younger; 133 (52.99%) had employed their machines for five to 10 years; 44 (17.53%) from 10 to 15 years and 42 (16.73%) from 25 to 30 years or higher.

This situation made SMEs in Cần Thơ fail to improve their productivity and competitiveness. In recent years, many SMEs in non-public sectors have tried their best to modernize their facilities in preparation for international integration, but the shortage of capital prevented them from carrying out quickly the replacement of machinery and meeting urgent requirements. That is why development of the financial leasing service as a source of finance for SMEs becomes a matter of urgency.

From the above analyses, we can draw the following remarks of the SMEs in Cần Thơ:

- They exist in various industries and in different forms. They account for only a small percentage of the number of companies in Vietnam, and most of them are privately-run ones.

- All SMEs in Cần Thơ are badly in need of capital and their ability to access formal sources of credit is limited. And as a result, they can't modernize their technologies in order to improve their competitiveness.

- Most SMEs employ obsolete machinery. A handful of newly

established concerns have tried to improve the situation but they couldn't change the backwardness.

The following are causes of the situation:

- + After the Companies Law came into effect in Jan. 1, 2000, many SMEs have been established in Cần Thơ, especially in recent years, but a few years are not enough for them to accumulate capital needed for modernization. Moreover, the best part of their assets was machines discarded by state-owned or foreign companies, and these machines are very old.

- Policies to support SMEs haven't been carried out properly. Access to formal sources of medium- and long-term loans is limited by complicated procedures and requirements about security.

- SMEs lack sources of reliable information that can help them select kinds of machines, suppliers and prices appropriate to their resources. Moreover, laws require that all contracts of technology transfer must be approved by the Ministry of Science and Environment and many contracts haven't been approved within months. This is also an

obstacle to the modernization of SMEs.

These are also challenges to Cần Thơ City on its way to international integration. Under current conditions, the financial leasing service could be considered as an effective measure to deal with these obstacles and develop SMEs.

2. Financial leasing service in Cần Thơ City

Cần Thơ is the only city in the Mekong Delta under direct management of the central government, but its economy still develops slowly. SMEs in this city account for only 1.2% of the number of companies in Vietnam and most of them are badly in need of capital.

In 2002, ALCII opened a branch in Cần Thơ City and up till now it has been the only concern supplying this service in the city, and annual sales by this branch accounts for only 7% of the ALCII total sales.

Up to Oct. 30, 2007, ALCII - Cần Thơ had 580 customers and its total outstanding loan was VND270 billion. The number of customers in the past three years varied from 578 to 608 but the structure of customers has changed: it included major

state-owned companies in the manufacturing sector at first and then private concerns are in the majority. This change shows that the financial leasing service is appropriate to SMEs in non-public sectors.

Total value of leasing contracts, however, is still small and the market demand is not well satisfied. The situation shows us the following shortcomings in the financial leasing service in Cần Thơ:

- Number of leasing companies, and their capital and competitiveness are limited. For the past six years, ALCII - Cần Thơ has been the only concerns supplying this service and its capital is limited. In 2006, its capital for financial lease was VND272.365 billion (70% of this figure came from loan capital) and in 2007 this figure rose to VND273.549 billion (loan capital accounted for 69% of it).

The supply of long- and medium-term loans by commercial banks has been improved. The lending rate is lower and some privileged companies can get support from local authorities when borrowing from banks. And as a result, the financial leasing service is at a disadvantage and has to witness its customer base contracting. In short, limited source of finance and keen competition from commercial banks prevent the financial leasing service from offering products of high quality and reasonable price to SMEs in Cần Thơ.

- Total sales and market share of the leasing service is very small. The sales from this service in Cần Thơ in recent years only equaled some 7% of the total sales from this service all over the country. The total outstanding debt to this service equaled 3.14% of total credit supplied in Cần Thơ in 2005, and this figure in 2006 was 3.03% and 1.54% in 2007.

Photo by Huỳnh Thơ



The fund for leasing is limited while assets and forms of leasing are not diverse enough. As for the fund, the financial leasing service has to depend on owner's capital and loan capital (which accounted for 69% of ALCII-Cần Thơ capital in 2007 for example) while deposits from customers and proceeds from issue of bonds by financial leasing concerns are very limited.

As for assets leased, they are mostly transport vehicles, machine used for construction and office machines. And these assets are usually leased according to short-term contracts and other leasing forms are not common.

My survey of 100 SMEs in Cần Thơ in November 2007 shows that only 5% of them have done business with financial leasing companies; 16% haven't done any business with them although aware of this service; and 79% are not aware of it.

3. Obstacles to development of the leasing service

The poor development of the leasing service, in my opinion, comes from the following causes:

- The legal infrastructure for this service is not perfect: Although the Decree 16/CP on organization and operation of financial leasing companies came into effect on May 2, 2001 as a replacement for the Decree 64/CP, regulations about hire-purchase business are still inadequate causing a lot of difficulties to this service. What is much needed here is a law on the leasing service that can create a perfect legal infrastructure for its development in Cần Thơ and the whole country as well.

- Information about this service can hardly reach investors and businesspersons: Many investors and companies in Cần Thơ know nothing about the leasing service and they miss chances to get access to leasing companies when necessary or feel reluctant to employ it.

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- Financial leasing companies are not free to mobilize necessary capital or sources of finance: Because ALCII-Cần Thơ, the only leasing company in Cần Thơ, depends on its holding company based on HCMC, it can not employ various channels of capital (such as advances from customers, and sales of bonds, etc.) to increase its fund for operation. This limits ability to finance by leasing companies.

Moreover, leasing companies are not allowed to finance a customer with a sum of money that is higher than 30% of its working capital. If the leasing companies want to lend a big sum of money, they can turn this sum into equity capital, but the SBV hasn't issued regulations about this practice, so leasing companies can't do anything in this direction.

- The service fee is still high because customers have to pay the VAT when paying the rental, along with fees relating to import of assets, registration of assets, check of assets quality, honorarium for public notary when signing the leasing contract. The total fee is usually from 20% to 25% higher than leading rate on long- and medium-term loan. Compared with the price offered by

foreign supplier, the cost of a hire-purchase contract is some 10% higher.

- Procedures for completing a leasing contract are time consuming and complicated. Managerial skills of leasing companies are not high because managers usually pay too much attention to administrative procedures relating to the leasing contracts and legal entity of customers or track record of customers instead of feasibility of their business plans. That is why it takes a long time to enter into a contract. As for newly established SMEs whose assets used as security for the leasing contract are small, they can hardly get support from the leasing companies. In addition, many managers of leasing companies spend too much time investigating the business plans of customers before offering the leasing contracts.

To develop Cần Thơ City into a financial center of the Mekong Delta, local authorities should work out plan and measures to deal with the above-mentioned difficulties in order to encourage this service along with others in the banking and financial sector, and help SMEs overcome their shortage of capital and develop in a more sustainable manner. ■