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Enterprise Development in the Mekong Sub-region: Its Transformation and Impact

The transition to a market economy necessarily involves a transformation of the ownership structures of a country's firms. Most directly, this process will give rise to different types of enterprises – notably private firms – and to reforms being made to state-owned enterprises (SOEs). Beyond that, however, it will have effects on the country's economic and social life, including employment, gross domestic product (GDP) growth and poverty reduction.

The experiences of the three Mekong sub-region countries: Vietnam, Lao PDR and Cambodia in their transition from centrally planned to market economies provide useful insights into changes in ownership structures and their wider impact on the economy and society. It is shown in this paper that all three countries have benefited from the enterprise development, e.g. through their contributions to job creation and poverty reduction.

Besides, the transition taking place in the countries themselves, South-South cooperation (SSC) in the region has also boosted enterprise development – in particular the growth of the private sector.

Enterprise development in the Mekong sub-region has yielded many positive effects in Vietnam, Laos and Cambodia, as well as in the region as a whole. However, the firms' contribution will still be greater if the skills, resources and efficiency of the enterprises are enhanced. Towards that end, the governments should pursue more liberal policies and push market economy reforms.

Background

Since the mid-1980s, the three Mekong sub-region countries: Vietnam, Laos and Cambodia have undertaken a shift from centrally planned economies to market economies. This shift has profoundly influenced the transformation of the ownership structures in these countries. Multi-sector economies comprising various forms of enterprises, such as state-owned, collective and private enterprises, have been formulated and developed, with private companies tending to develop at the fastest pace.

This paper looks at how firm structures have changed since the market-oriented reforms were first initiated, what impact enterprises have had on job creation and poverty reduction, and how SSC has influenced the development of enterprises. It is shown that the changes in ownership structures offer a good opportunity for enterprises in the Mekong sub-region nations to expand their domestic businesses as well as boost their external cooperation, including SSC. This will, in turn, increase the contributions companies make to the social and economic development in each of the three countries as well as in the region as a whole.

Enterprise Development

Vietnam: The concept of economic sectors has changed significantly in Vietnam since 1986. In the beginning it covered mainly the state-owned and the collective sectors, but the concept has since widened and it currently encompasses six sectors: state-owned, collective, individual and petty economies, private-capitalist economy, state-capitalist economy, and foreign direct investment (FDI).

Along with this change, following laws and policies have been added and amended in order to facilitate the development of different forms of enterprise in various economic sectors:

- Amended Cooperative Law;
- State-owned Enterprise Law;
- Private Enterprise Law (1990), Company Law;
- Firm Law (1990);
- Amended Domestic Investment Promotion Law (1998); and
- Enterprise Law (2000).

One notable outcome has been the establishment of many private enterprises, especially following the approval of the Enterprise Law in 2000. Companies have not only acquired the right to domestic operation, but also the right to cooperate, to enter into joint ventures (JVs) with foreign partners in Vietnam – including overseas Vietnamese – and to purchase shares of Vietnamese enterprises of up to 30 percent of the charter capital. Furthermore, many business registration procedures

Private Enterprises in Vietnam

As a result of the changes, 73,000 new private enterprises were registered in the years from 2000 to 2004, an increase of 3.57 percent compared with the longer 1991-1999 period. By 2004, there were 150,000 private enterprises operating under the Enterprise Law with a total capital of US$11.5mn. From 1991 to 2003, the share of the private sector in GDP increased from 3.1 percent to 4.1 percent, other non state-owned sectors from 4.4 percent to 4.5 percent, the individual sector's share declined from 35.9 percent to 31.2 percent, and the share of the foreign invested sector increased from 6.4 percent to 14 percent.

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have been streamlined, such as the reduction of registration time for new enterprises from 45 days to 15 days, the removal of 175 types of business licenses (accounting for 44 percent of existing business licenses), the fading-out of required charter capital for a number of businesses, and the application of agreed interest rates for loans by commercial banks without discrimination on different economic sectors.

The state sector has seen its share decline marginally since the early 1990s, but in contributing more than one-third to GDP, it continues to play the leading role in the Vietnamese economy. The share of the collective sector has also eased somewhat during the same period and today accounts for less than 8 percent.

In order to raise the efficiency of the SOEs, the government has adopted several reforms such as acquisition, restructuring, selling, leasing, strengthening the financial and capital management of enterprises, and encouraging SOEs to enter into JVs with foreign partners. In 2002-2003, 1,655 SOEs were listed in the reform programmes, in 2004 the number was 882, and in 2005 it is planned to be 413 enterprises.

Among the existing SOEs, 30 percent have been found to make profits, while 40 percent face weak business and 30 percent make losses. 90 percent of FDI JVs are in association with SOEs, which contributes to the improvement of labour productivity, promotes technological acquisition, and facilitates the setting-up of new industries.

Laos: The first step towards a multi-sector economy in Laos came in 1988 when the Government promulgated the Foreign Investment Law. In 1999, it passed the Constitution in which state, collective and private ownerships were protected in order to facilitate the development of all economic sectors.

During the 1990s, the Lao Government implemented a programme of institutional and law reform in order to formulate market regulations and institutions to promote the development of the private sector.

In 2001, the Lao Government launched a large structural reform programme in order to improve public spending, reform the SOEs, develop transparency of state banks' operations, encourage strong development of private enterprises, and manage efficiently the resources of development.

The reform of the SOEs that has been effectuated since the early 1990s has three aims:

- improving their management and transparency;
- restructuring inefficient enterprises; and
- and rationalising the regulations and laws concerning SOEs through tax reform.

To solve the problems faced by the SOEs, particularly the large debts and the high risk of large-sized SOEs, the Lao Government has *inter alia* implemented the decentralisation of SOEs' management; applied close control over loss-making enterprises; identified the responsibility of SOEs; reorganised large SOEs; and introduced new policies on electricity and water prices.

Although the number of SOEs has declined as a result of the reform, their role has become increasingly important due to their greater contribution to GDP growth and generation of more jobs.

Economic development in Laos

The private sector is considered as an important source of economic development in Laos. The Lao Parliament amended regulations in September 2001 that led to the private sector being given higher attention along with the greater focus on anti-monopoly regulations. Accordingly, the Lao Government has strengthened the consultation with private businessmen, simplified the investment procedures for private enterprises, encouraged small and medium-sized enterprises (SMEs), adjusted land policies, and enhanced the independence of the Industry and Commerce Bureau.

The Government has also called on international financial organisations, especially the Asian Development Bank (ADB), to help mobilise financial resources for the development of the private sector. As a result, a number of projects promoting the development of private economies have been adopted, such as the Small Private Enterprise Project in 2002, and the SME and Private Sector Development Project in 2004.

Private Enterprises in Laos

The number of private enterprises has increased sharply since 2001. Currently, nearly 97 percent of the private enterprises that operate in the processing and manufacturing industries are small-scale with less than 10 workers each. Between the medium and large enterprises (MLEs), 35 percent are owned by Laotian private businessmen, 55 percent are JVs with foreign partners, with the remainder belonging to SOEs. About 75 percent of SMEs are located in rural areas, mainly operating as rice huskers, garment establishments and retail shops. Only a small number of SMEs have the opportunity to get access to preferential credits from commercial banks.

Most of the private enterprises are small-scale, so they have very little impact on the creation of jobs, except for the members of their own families. In addition, most of them lack necessary experiences and skills to compete efficiently in the international markets.

By the late 1990s, Laos had only 65 SOEs in operation. During this period, the private sector had taken over all agricultural production and most of the industrial activities.

The International Monetary Fund (IMF) described this privatisation as 'one of the most successful programmes in the restructuring process in Laos.' About half of the existing 65 SOEs have been deemed strategic enterprises and will continue to operate as SOEs, while the other half will probably experience changes in ownership or be dissolved. Currently, industrial SOEs account for only one percent of GDP.

The average annual turnover of Lao enterprises is roughly US$250,000, with some 70 percent of the enterprises obtaining three-quarters of their turnover in their domestic markets, while 30 percent mainly depend on trade.

Cambodia: All the enterprises in Cambodia were state-owned until 1989. In the beginning of the 1990s, the national Government decided to develop the private sector as one of the measures to facilitate poverty alleviation. Since then a number of laws and regulations relating to the development of the private sector have been promulgated, including the Investment Law (1994), the Act on Organisation and Management issued by the Cambodian Development Committee and the Cambodian Investment Committee (1995), and the Tax Law (1997).

As for structural reform, several specific priorities have been identified including: unleashing business control by shifting from a control mechanism to a facilitating mechanism through the use of institutions and regulations that create favourable conditions for enterprises to develop; focusing on market development; improving the competition environment and the labour productivity; and strongly developing the private sector in the informal sector and the rural areas.

In 2004, the Cambodian Government got a loan of US$20mn from ADB for improving the business environment, to reform regulations and procedures, and to help SMEs get easier access to financial sources.

Enterprises of Cambodia

The main features of enterprises in Cambodia are that they are small in scale, that most of them operate in semi-industrial sectors like aquatic-product processing or rice husking, and that they have an average annual turnover of about US$10,000 and employ seven workers each on average. Little more than two-thirds of the firms are individually owned, with SOEs only accounting for 0.2 percent of all enterprises.

Micro and small enterprises (up to 100 workers) focus on agricultural production and rural services, whereas large enterprises (more than 100 workers) operate in the manufacturing textile and garments sectors. 84.3 percent of all the enterprises serve the domestic market. The implementation of the policies mentioned above has facilitated the development of the private sector.

Private Enterprises in Cambodia

Currently, there are around 21,300 enterprises engaged in agricultural processing in Cambodia. SMEs account for 99 percent of all enterprises and 45 percent of the workforce, mainly in the sectors of garments and textile, food processing, chemicals, rubber, plastic, and steel moulding. Since 1999, SMEs have grown at annual rate of 9 percent. SMEs are considered a fundamental force in poverty reduction and economic growth strategy.

In Cambodia, the micro and small enterprises virtually have no links or integration with domestic large-sized companies or multinationals.

According to the World Bank (WB), only about one percent of commodities and materials of domestic large-sized companies and multinationals are provided through the channels of micro and small enterprises in rural areas. In the urban areas, 86 percent of the output produced by SMEs is supplied to individual customers, five percent to intermediaries, and eight percent to other small enterprises.

Although the private sector has been developed quickly, Cambodia is still seen as a risky country for business. The WB has pointed out 10 big challenges facing private enterprises in Cambodia: corruption, crime, an uncompetitive environment, unstable policies, a weak legal system, inefficient adjustments of tariffs, high administrative costs, high tax rates, unstable macroeconomic conditions, and limitations in business license granting.

A survey of 500 enterprises in 2003 revealed the very high tax rates that these enterprises had to pay compared to their income: 61 percent for FDI enterprises, 53 percent for SMEs and 40 percent for micro enterprises. Corruption accounts for four to seven percent of companies' revenue and the inefficient and risky banking system limits the mobilisation of capital for enterprises, which instead raise a large part of their investment capital from friends, relatives and/or families.

Job Creation and Poverty Reduction

The development of the private sector in Vietnam has been regarded as an important contributing factor to the creation of jobs, higher income levels, increased revenues for the budget, and assurance of political and social stability. The policy has been proved to be practically right.

As a result of the implementation of the Enterprise Law during the past four years, the private sector in Vietnam has generated 1.6-2.0 million new jobs, raising the number of employees working in non-state enterprises to be nearly the same as that of the SOEs.

According to the Ministry of Labour, War Invalids and Social Welfare, employees working in non-state enterprises accounted for 38.6 percent of the national workforce in 2002, compared to 46.1 percent working in SOEs and 15.3 percent in FDI enterprises. Most of the employees in the private sector work in forestry, aquatic and agricultural areas, while the number working in industries and construction is modest.

The private sector has generated an increasing number of new industries and products, and has been able to efficiently exploit the advantages of Vietnam and play an important role in the country's export-oriented industrialisation strategy. In fact, many private enterprises have gained a good position and reputation in the domestic and international markets, especially in areas such as fine arts, agricultural and aquatic products, consumer goods, garments, construction materials and services.

Many areas of business, which used to be covered by the state sector, have shifted to the private sector. The dynamism of the private sector has led to the creation of more products with fine designs, good quality and high competitiveness that meet the diverse needs of social and economic life.

Private Enterprises Boosting Growth

The private enterprises in Laos and Cambodia have similarly generated a large number of jobs for the working population. The National Poverty Reduction Strategy (NPRS) in Cambodia has clearly stated that the main objective of the Royal Government is to encourage large scale sustainable economic growth along with social equity and that the private sector plays the leading role in the implementation of this policy.

In Laos, the New Economic Mechanism (NEM) launched in 1986 and the National Growth and Poverty Elimination Strategy (NGPES) promulgated in 2004 has facilitated the development of private enterprises, creating momentum for poverty reduction.

Due to the strong development of the market economic mechanism and the diversification of forms of enterprises, the percentage of poverty in Laos reduced to 29 percent in 2003 from 45 percent in 1990. Similarly, poverty in Cambodia has declined to 36 percent, and will be reduced to 28 percent by 2015 as targeted.

These are encouraging achievements. However, as poor countries with underdeveloped infrastructure and 80 percent of the population living in rural areas, the development of enterprises in rural areas in Laos and Cambodia is not capable of eliminating poverty.

The low productivity is still a serious problem for enterprises in these two countries. The small sizes as well as low and infeasible capital of the micro and small enterprises in Laos and Cambodia mean that they are unable to expand production, create more jobs and improve the income of employees.

Today, in the enterprises of Cambodia, only 20.76 percent of the workforce has completed the sixth grade and 16.35 percent completed the 12th grade. The average percentage of employees in need of retraining in Cambodian enterprises is

60.24 percent, with the highest percentage for the micro enterprises (73.60 percent), and lowest for the large-scale ones (42.18 percent). For countries in transition to market economies, the problem of untrained workers has become a big challenge. It is also a cause of the inefficiency in business activities and the implementation of national poverty reduction strategies.

SSC Impact on Enterprise Development

In recent years, the globalisation and regionalisation processes, including the SSC, have strongly developed and influenced the increasing integration of the countries in the Greater-Mekong sub-region (GMS) – China, Vietnam, Laos, Cambodia, Myanmar and Thailand.

Since 1992, the cooperation among these countries has been considerably enhanced. At the GMS Cooperation Forum held in Phnom Penh in 1992 with the assistance of ADB, the leaders of the six GMS nations announced the Declaration on the GMS Development Programme in this, which the member countries agreed on inter-governmental cooperation in the development of electricity in order to create a more favourable environment for business and everyday life.

At the GMS Cooperation Forum in Hanoi in 1997, the six members agreed to deepen the cooperation in the field of energy, seeking investment of about US$100bn from 1998 to 2010 to build new power projects in the Mekong region.

The governments of the six nations agreed to associate the state with the private sector in order to meet this large requirement. This was the first time that the private sector was stressed in the cooperation efforts of the countries in the region.

In 2002, the Mekong Enterprise Fund (MEF) was established in Vietnam with an initial capital of US$16mn. The stated aim was to help the private SMEs in Vietnam, Laos and Cambodia in their investment efforts, especially in the field of export industries and local services. The capital for MEF has been mobilised from the ADB, the Northern Europe Development Fund (NEDF), the State Secretariat for Economic Affairs, Switzerland (SECO), the Finnish Industrial Cooperation Fund (Finnfund) and some other private investors. The financial support by MEF for SMEs ranges from US$500,000 to US$1.85mn.

In order to meet the aim of setting up a new 'growth triangle' in the Mekong sub-region, the Governments of Vietnam, Laos and Cambodia have signed various agreements such as the Agreement on the Sustainable Development and Cooperation of the Mekong Region (April 1995), the Agreement on the Cooperation Strategy for the period of 1996-2000 and 2001-2010 between Vietnam and Laos, and the Vietnam-Cambodia Trade Agreement signed in March 1998.

These agreements have provided a legal framework and a reliable base for the cooperation and development of enterprises. For example, the agreements on the free entry for ordinary visa and the reduction of import tariffs by 50 percent between Vietnam and Laos have had a great impact on the increase of exports of the two countries to US$145mn in 2004, a 30.6 percent increase against the previous year.

At present, there are 15 Vietnamese enterprises investing in Laos as JVs and building contractors. One of the typical cases is the Xekaman Hydropower Plant JV with capital of US$350mn. In addition, Vietnamese and Laotian enterprises are now trying to speed up and make more efficient their cooperation in the fields of investment promotion, management and use of aid, and training of human resources.

Vietnam and Cambodia have also advanced cooperation in their relations. As a result, two-way trade has grown from US$185mn in 2001 to US$450mn in 2004, an increase of 24 percent in 2004 compared with 2003.

Conclusion and Recommendations

Based on the facts analysed above, one may come to the conclusion that in recent years, the enterprises of the countries in the Mekong sub-region have developed rapidly both in terms of quantity and sectoral structure, particularly with regard to the reform of SOEs and the growth of the private sector. Moreover, the companies have contributed positively to the development of the market economy, the generation of jobs and the reduction of poverty.

Although the enterprises have many limitations and weaknesses due to their small sizes, low capital, backward technologies, poor skills, low efficiency, and other constraints, they will surely continue to expand, since they have quickly developed in number and diversified their business areas – from agriculture, fishery and forestry to processing and manufacturing – thereby creating more and more opportunities for future development.

In order for the enterprises in the Mekong sub-region to improve their development, operate more efficiently and, hence, contribute even more positively to the socio-economic development of each country in the region as well as to the region as a whole, the governments and enterprises in these countries need to apply more and more liberal policies. In particular, they should take the following measures:

- stronger development of the market economy;
- greater liberalisation of trade and investment;
- formulation of a common legal framework and implementation of synchronised policies;
- creation of more favourable conditions for micro and small enterprises;
- promotion of greater cooperation of businessmen through various incentives; and
- construction of improved infrastructure.

The implementation of these measures will surely facilitate the expansion and contribution of enterprises in the Mekong sub-region countries.

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