

**PUBLIC POLICY FOR THE DEVELOPMENT OF  
PRIVATE SECTOR AND SMES IN A SOCIALIST  
MARKET ECONOMY**

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**Abstract**

*The Vietnamese government has been conducting economic and administrative reforms to create a sustain market conditions for the growth of small to medium enterprises (SMEs) in Vietnam since 1986. In fact, the inconsistency in the government policy, slow pace of market reform, insufficient resource distribution, and poor initiatives to attract external support have postponed the growth of Vietnamese SMEs. From that context, this paper examines the factors contributing to the growth of SMEs by using a conceptual model of 'enabling' factors derived from an extensively review of Vietnamese literature and from an initial qualitative study of the research. Considering the Vietnamese experience with SMEs, this paper argues that in a Confucian culture and socialist market economy, where imperfect market factors, inadequate institutional support structure, and lack of proper co-ordination between policy formulation and policy implication are apparent, it is essential that the state has a key entrepreneurial responsibility to create conducive market conditions. More importantly, access to adequate resource infrastructure could create the essential shift for a pro-market venture enticing new business sectors to be part of the transitional process building the supportive infrastructure for SME grow.<sup>2</sup>*

**Keywords:** *Public policy, private sector development, small and medium enterprises (SMEs), socialist market economy, market-oriented economy.*

**1. INTRODUCTION**

The Vietnamese government has been pursuing an interventionist approach in introducing macroeconomic reform, building institutions, and enhancing managerial capability in its journey to market socialism. The interventionist measures have structured to achieve short and long-term goals through gradual improvement of the legal framework and economic policies. It is believed that this gradualist path will create a healthy legal and business environment to facilitate the development of small and medium enterprises (SMEs). The sustainability of SMEs is an important prerequisite for the successful transition of Vietnam's economy.

The study examines how the state plays an entrepreneurial role to influence the creation of sustainable market factors and healthy business conditions to support SMEs. The report investigates whether these interventions are too irregular and how well the policy measures to support and sustain the development of SMEs are perceived by SMEs. The study uses institutional approach to examine how the state can act an entrepreneurial role to manipulate the formation of adequate market factors and well-articulated policies measures and conducive business conditions to sustain SMEs. The findings suggest that in general, our findings strongly support the results from qualitative study. It also shows that the Vietnamese government

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has taken some committed initiatives in attracting external support, building infrastructure both tangible and intangible, and enabling structural flexibility for the growth of SMEs. To some extent, policies obstacles concerning different aspects such as taxation, finance, land, trade, technology and information, training, legal and administrative reform, supporting institutions have been noticeably improved and helped to benefit SMEs. However, as indication from the study, and quite consistent with what we have discussed and found in the early stage of the study, several policies' hindrances are still there which support our preliminary findings in qualitative study.

## **2. A VIETNAMESE SOCIAL AND ECONOMIC CONTEXT**

In the past few years, although there are still many inadequacies in economic development policies and public administration, the Vietnamese government has tried to improve the business environment and support the development of the private sector to facilitate economic growth. There is a pressure of economic integration into the global market and Vietnam joined in the World Trade Organization (WTO) in 2006. There is a need for Vietnamese SMEs to improve their competitiveness. Many Vietnamese SMEs are not ready to participate fully in the market-oriented economy. They are struggling to keep pace with innovation and resources.

### **Background of the Quantitative Survey Phase**

The results from our qualitative research phase indicate that although the support policies are in place, there are remain many problems. According to the findings, the problems are: poor support infrastructure, trade policy and lack of a level playing field, inadequate legal framework, business licensing and administrative reform, poor taxation system, problems in land distribution, ineffective financial and credit policy to support SMEs, lack of institutional support systems in both the public and private sectors to promote SME growth, poor technology and information to support SMEs, and inadequate training policy for managerial and professional development.

### **Administrative Reform to Support SMEs and Reducing Transaction Costs**

Richards et al. (2002) observe that government policies have gone some way to reducing the restrictions on private SMEs. First, SMEs have allowed exporting directly. This will assist small firms most of all as they were least able to bear the additional transaction costs of previous restrictions. Second, the requirement has removed to import through state enterprises to satisfy stipulated conditions of capital and qualified personnel needed for registered as an importer. Third, foreign investors have now allowed owning 30 percent of shares in existing domestic enterprises, permitting private firms to seek foreign partners.

Ascher and Rondinelli (1999) report on the decentralization conducted by the Vietnamese government and raise five major objectives of service provision

that are important to the delivery of social services and infrastructure in Vietnam: (1) an optimal quality of services; (2) an optimal quantity of services; (3) efficiency in service delivery; (4) equity in service distribution; and (5) responsible local participation. They argue that improving the government's capacity to distribute public services and infrastructure requires a more decentralized administrative structure, and this administrative reform is vital to building institutional capacity in a market-oriented economy.

Certainly, as Ascher and Rondinelli (1999) argued, Vietnam's success in sustaining its economic transition in general and private sector development in particular will depend crucially on increasing institutional capacity to delivery public services and infrastructure effectively. However, there are still many limitations in public administration reform and bureaucracy after the 'Doi moi' program undertaken by the government in 1986. Nguyen and Alam (2008) report the three major issues in relation to public administrative reform and bureaucracy: corruption and red tape, business inspection problems and management overlap problems. This has generated significant unofficial expenses for SMEs – an undefined hidden tax on their activities. In addition, management administration is bureaucratic and not computerised.

Therefore, eliminating the restrictions on SMEs by proper administrative reform measures has the potential to result in the reduction of transaction costs for SMEs and foster their development.

### **3. RESEARCH QUESTIONS**

The article has based on the result of the second stage of the research. The adequacy of the support policy regime and the effectiveness of the support infrastructure have discussed to identify the problems of the market development process and SME development route under the socialist market economy model of Vietnam. This paper aims to answer one specific research questions:

To what extent do SMEs perceive the level of importance of critical support policies (mentioned in the conceptual model) for business growth?

### **4. RESEARCH METHODOLOGY**

The quantitative research is the further step in a triangulation approach to investigate the research questions. The research seeks to investigate the extent of difficulties and problems that have emerged from the support policies and the degree of SME perceptions of critical support factors. In addition, it also attempts to examine the association of SME characteristics and their perception of support policies and critical support factors.

SMEs were asked to rank their company size into three categories: less than or equal 30 employees, considered a small entrepreneur; from 31 to 300 employees, considered a medium firm; and more than 300 employees, considered large firms and therefore discarded from the study. These ranking criteria were based on the current SME definitions (Decree 90/2001/ND-CP, dated 2001, issued by the Vietnamese government).

The purpose of using these three categories instead of two categories was to discard any firm that has more than 300 employees and which might be considered as a large firm, and to see whether the surveyed firms represented SMEs in Ho Chi Minh City and the regional areas. The results from the survey reveal that 58.5% of firms were small firms and 41.5% were medium firms.

These figures are considered reasonable because this sector is export-oriented and a labour-intensive industry with potential for growth. This is generally consistent with the figure provided by the General Statistic Office in 2004. For that reason, this sample has assumed free from any significant size-bias that may distort the results of our quantitative analysis. As a result, the respondent SMEs have believed to be representative SMEs who are actively involved in manufacturing of foods, beverages, forestry products and seafood, or SMEs who are growing and processing aquatic products and other agricultural products in the South East.

Since our research study had conducted in a particular manufacturing industry in South East Vietnam, the largest and fastest-growing economic area, and representative of SMEs, we believe that generalization of the research findings is possible. Hence, the degree of proximal similarity in the findings will not be much different among other provincial business contexts in Vietnam. Before conducting the survey, we sent a summary of our empirical findings from the interview to a sample of respondents to make certain that the findings were convincing and of high quality. In addition, during the data collection process, researchers tested SME and economic expert opinions in Ho Chi Minh City to identifying possible problems related to the questionnaires.

Pilot testing of the questionnaires was undertaken and the researchers received valuable feedback to finalize the questionnaires before conducting the survey in the South East area. The aim of this test was to examine the clarity of the SMEs' understanding of the questions. As a result, some minor adjustments have made to improve the clarity of the research questions and the construct validity. Furthermore, the research used triangulation with primary and secondary sources and combined this with the findings of our qualitative research to construct the questionnaires.

#### **Development of the survey instrument**

The main variables\* include eight principals, basic factors garnered from current support policies and lessons learned from other transitional economies. Many studies have also discussed those common factors of tax, credit and finance, land access, legal frameworks, technology and access to information, supporting institutions, training and trade policy (Richards et al., 2002; Rondinelli and Litvack, 1999; Havie, 2002; Harvie, 2001; McIntyre, 2001, 2002; Nadvi, 1995;

North, 1990; Dallago, 2003; Surdeji, 2000; Lee and Tan, 2002; Ngui, 2002; Abdullah, 2002; OECD, 1997). The government's current support policies for the development of SMEs and Sakai and Takada's framework (2000) provide a helpful policy framework to promote the development of SMEs in Vietnam. The eight policies are:

1. *Taxation*: Support for improving SME resources.
2. *Legal and administrative reform*: Institutional measures to improve the legal and business environment, administration reform to reduce transaction costs and business expenses.
3. *Trade Policy*: This is an institutional measure to promote a level playing field and trade promotion, building SME competitiveness and access to resources.
4. *Supporting Institutions*: Developing institutions and organizations to support the development of SMEs.
5. *Finance*: The government to support SMEs in accessing credit and capital resources and building competitive advantage using financial policy.
6. *Land*: Land is an important factor to SME development in Vietnam. The land policy has designed to ensure the fair distribution of land resources among business sectors and the land access of SMEs.
7. *Technology and information*: Supporting technological development activities are underdeveloped for supporting SME growth and their access to technology and information resources. For that reason, the government is introducing technology and information policy to support SME growth.
8. *Training*: These supports are in the form of training, provision of information, marketing support, technological advice and advisory services for business development and human resources development.

\* Other variables have obtained from the literature review on transitional economies, Vietnam's economy and the private sector development. These additional variables, together with the eight main variables have used to examine SME perceptions of the level of importance of critical support policies as enabling features for SME development, for example:

9. *Access to e-infrastructure and e-commerce*: Accessing e-infrastructure and e-commerce will enhance SME capability in approaching the market and obtaining information; it helps reduce SMEs' resources burden. Through applying such measures, Vietnamese SMEs can have the opportunity to contact potential customers and develop their business trading and production (Nguyen et al. 2007; and Le, Bach, Dinh, Nguyen, Trinh, Phan and Vu, 2006).
10. *Industrial cluster*: According to Tambunam (2005), the government, business support institutions, academic and professional training institutions, the banking system and groups of firms can gather in an

industrial cluster or industrial zone for efficient utilization of resources. Through a cluster in an industrial zone, SMEs can received better support and it will be easier for those support institutions and government to provide aid to a large group of SMEs clustered in a specific location with minimum costs of transportation and infrastructure, rather than to those who are more widely dispersed. This argument have strongly supported by many researchers, as we have discussed our review of the literature, for example, Porter (1998a, 1998b), Enright and Robert (2001), Bologna charter for SMEs issued by the OECD (2000), Dijk and Sverrisson (2003), Ionescu (2003), Nadvi (1995) and Abonyi (2003). Similarly, in the case of industrial clusters, Kuchiki (1994, 1995, and 2005), Kuchiki and Tsuji (2005) and Riedel, McCarty and Record (2005) also highlighted a number of issues regarding the prospective development of this model in Vietnam. The results from our initial qualitative study also reveal that industrial clusters and business cooperation of SMEs is strongly impacted by network relationships with other firms and by an entrepreneurial culture. This is similar to Beresford (2008, p.234) which we have discussed earlier, that in Vietnam ‘transactions are carried out on the basis of trust, reputation and social pressure’.

11. *Development of networks:* Network relationships (both formal and informal) help improve the exchange of information and sharing resources. They also facilitate SMEs in seeking cooperation to overcome small size and resource constraints and in improving their capability for innovation in terms of technology transfer and adapting new material. Moreover, network relationships promote buyer and supplier network relationships and technical support services, as well as attracting investment and enhancing efficient communication between SMEs and their network (Nadvi, 1995; Tambunam, 2005; Ritter, Wilkinson and Johnston, 2003). Findings from our qualitative research reveal that most SME network relationships in Vietnam are informal. Lacking reliable information about business partners and facing significant discrimination against them, SMEs do not have the chance to seek business cooperation opportunities.

12. *Improving the image of SMEs and reducing negative attitudes towards their roles.* Having identified the issue of ‘unwritten laws’ of discrimination against SMEs which exist strongly in the society, there is an emerging need for improving the image of SMEs as a main contributor to the economy (Le, 2006; Dao, Nguyen, Ngo, Nguyen, Tran, Dinh, Duong, Trinh, Nguyen and Bui, 2000; Pham, 2002a; Vu, 2001). This is consistent with the results from our interviews. The results from our study show that there should be initiatives in building positive public attitudes towards SMEs. SMEs should not be consider the least preferred place of employment and the discriminatory attitudes about the credit worthiness of private SMEs should be removed.

13. *Facilitating the entrepreneurial culture of SMEs:* North (1990, p.3) defines an institution as ‘the rule of the games in a society’. According to

North, institutions consist of formal institutions such as political and economy-related rules and organizations, but also informal institutions, which refer to codes of conduct, values and norms. Put another way, culture is an interactive aggregate of common characteristics that influence a group's response to its environment (Armstrong, 1996). Ahmed, Chung and Eichenseher (2003) argue that every culture has its own values and norms that developed over generations.

The population consisted of the following SMEs: in foods; beverages; forestry products processing; seafood; growing and processing of aquatic products; and other agricultural product manufacturers. These were in Ho Chi Minh City and regional areas such as Binh Duong, Binh Phuoc, Long An and Tien Giang. The SMEs have spread over these locations, which are the largest economic areas, with many industrial zones and manufacturing SMEs.

Responses were provided on a Likert scale ranging from 1 to 5, where number 1 was 'not important' and 5 was 'most important'. Respondents have asked to indicate to what extent they considered that these factors/statements were important to their business development.

## 5. RESEARCH FINDINGS

The overall mean for each policy factor has obtained to examine the level of importance perceived by the responding SMEs. The values of the mean score of the policy support factors range from the lowest score (2.56) to highest score (3.88). Support to create social awareness about the importance of SMEs in Vietnam and support for solving financial constraints have evaluated by SMEs as the two most critical support policies. On the other hand, support for business cluster development in industrial zones and Strategic business networkings to support SME growth are the two least critical support policies.

It is clear that from both the literature (Pham, 2002a, Le, 2006, Ho, et al., 2002) and our qualitative findings government support for solving financial constraints and taxation-related problems is very important for SMEs. It is essential to emphasize that the survey have conducted between late 2007 and early 2008, which was a very uncertain period for the financial market in Vietnam and worldwide.

As we discussed earlier, in this period Vietnamese business enterprises, SMEs and the banking system suffered significant problems due to a very high inflation rate (14-16%) and the recent decline on the Vietnamese stock exchange market. As a result, SME access to formal credit sources and informal credit was impossible (the credit interest rate in banking system was 14-18% annually). SME rate of success in accessing international credit accounted for only 1.3% of the surveyed firms in the VCCI 2001 survey (Pham, 2002a).

<b>Critical support factors and ranking (from most important factor to the least)</b>	<i>Mean*</i> (1-5)	<b>Std. Deviation</b>	<b>% SMEs rated from 4-5 score</b>
1. Policy to create social awareness about the importance of SMEs in Vietnam	3.88	.88	68.7
2. Support for solving financial constraints for SMEs	3.83	.95	65.3
3. Support for solving taxation related problems	3.66	.85	58.5
4. Support for solving land related problems	3.37	.76	40.7
5. Support to improve legal environment	3.36	.81	44.9
6. Support for trade, improving business environment and equal competition	3.35	.90	50.0
7. Support for training and skills development	3.35	.80	42.4
8. Support for accessing better technology and information	3.32	.90	39.0
9. Support for new entrepreneurs and start-up business	3.28	.77	35.6
10. Provision of business support services (from supporting institutions)	3.26	.80	33.0
11. Development of e-infrastructure ( such as e-commerce, e-government, and e-registration)	2.86	1.07	30.5
12. Strategic business networking to support SMEs growth	2.58	1.02	20.3
13. Support for business cluster development in industrial zones	2.56	.97	17.8

*5-point Likert scale: 1=Not important, 3= Moderately important, 5= Very important*

**Table 1:** Mean score and ranking (from highest score to lowest score) for critical support policies perceived by SMEs as enabling factors

On support for business cluster development in industrial zones and business networking, the research found that the support for the development of business clusters and networks was non-existent. This is due to several negative factors such as ‘mistrust’ attitudes among business sectors, lack of linkages between businesses and support institutions, poor land affordability and other resource difficulties.

The findings indicate that SMEs placed more emphasis on the need for ‘Policy to create social awareness about the importance of SMEs in Vietnam’ (mean 3.88) and then follow-up on support for solving financial constraints (mean = 3.83). Support for solving taxation related problems has ranked the third critical factor with a mean value of 3.66. It seems from the data that SMEs have a good understanding of the need for support to solve land related problems (mean = 3.37); support to improve legal environment and equal competition (mean = 3.35);

and *support for training and skills development* (mean = 3.35). These factors have ranked by SMEs as the fourth, fifth, sixth and seventh critical factors, respectively.

The findings of this research highlight a key finding that cultural factors such as the need for improving the image of SMEs and reducing prejudice against SMEs are vital. For that reason, the *Policy to create social awareness about the importance of SMEs in Vietnam* is a necessary step to facilitate the development of SMEs through encouraging entrepreneurial culture and entrepreneurial activities.

According to the results shown in *table 1*, 39.0 % of responding SMEs indicated the *need for accessing better technology and information* was of special importance (rated between 4 and 5). *Support for new entrepreneurs and start-up business* and *provision of business support services from supporting institutions* have rated at a mean value of 3.28 and 3.26 respectively. They have ranked ninth and tenth.

On the need for *support and development of e-infrastructure* (such as e-commerce, e-government and e-registration), SMEs did not perceive it as critical as other factors. The surveyed SMEs rated this at the mean value of 2.86, indicating a ranked level of eleventh. '*Strategic business networking to support SMEs growth*' and '*Support for business cluster development in industrial zones*' were considered by SMEs as the two least important factors, with mean values of 2.58 and 2.56 respectively.

*Support for solving land related problems* and *support to improve legal environment* are ranked fourth and fifth. Perhaps the surveyed SMEs expected a clearer and specific strategy in the allocation and distribution of land resources and improving legal environment. This is similar to the situation described by Pham (2002b, p.40) that 'SMEs become powerless and disadvantaged because of their small scale and their lack of access to collateral. The last resort for SMEs is their real estate. According to the survey data, 61.5% of SMEs have to use their house for business purposes, indicating an underdeveloped property market, with negative effects on the credit market'.

Such defective market factors, unconducive business environment, discrimination against SMEs in accessing resources, together with inadequate support mechanism and the weak entrepreneurial role of the state have hindered SME growth. The ranking for *support for training and skills development* and *support for accessing better technology and information* were seventh and eight respectively, indicating that the government needs to develop customised training programs to enhance management skills, technology capabilities, and information access and e-commerce capability of SMEs.

According to VCCI (2001), only 37.8% of entrepreneurs in their 2001 survey have attended business management and training course. This figure could explain why training has considered important to SMEs.

A further examination of the quantitative data indicates the need for support for new start-up business, provision of business supporting services from institutions, and development of e-infrastructure (e-commerce, e-government, and

e-registration). Although these are critical, SMEs do not consider these factors as their top priority. In the absence of a network relationship and inter-business cooperation, the importance of e-infrastructure has not considered by SMEs as an important factor. The findings provide a picture that suggests that the Vietnamese government needs to take command as an entrepreneurial state to create a matrix engaging all-important stakeholders to work together with greater synergy, focus, commitment, and leadership.

### Discussion

The findings show that SMEs would perceive some direct support policies (finance, taxation, land) as more important than other policies. Though this section has not gone further in explaining to what extent these support policies packages should provided to different SMEs, we hope that it proposes an insight into the pathway of designing relevant policies to satisfy SME demand for support. This could also be a helpful suggestion for policy makers and academic researchers to become aware of the important role of private business and to take a more positive view of their valuable contributions to Vietnamese economic development.

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