

CHAPTER 9:

CONCLUSIONS AND POLICY RECOMMENDATIONS

The main objective of this dissertation has been to assess the performance of Vietnam's economy since implementation of its renovation policies, particularly since 1995 (see Chapters 5 and 6), and its impact on Vietnam's industrialization (see Chapter 7 and 8). Though protecting infant industries may incur efficiency losses in the short run, such protection has been justified by the beneficial learning effects in the long run. Opening the domestic market to imported goods may stimulate reciprocal export activities. Since renovation 1986, especially since 1995, the Vietnam government has implemented policies for the integration of Vietnam's economy into the global and regional economies. With such policies, Vietnam has made certain achievements since 1995 (see Chapter 6), but there are still many challenges, particularly trade policy reforms, industrialization policy, social inequality and income redistribution changes arising from integration into the world economy (see Chapters 6, 7 and 8) that Vietnam has to overcome to guarantee rapid industrialization and social equality¹.

9.1 Reform of Trade System

¹ The IX Congress of the CPV confirmed that as it enters the 21st century, Vietnam continues to face complex changes that will pervade every aspect of the economy, which should be integrated into the world economy with concrete and suitable roadmaps for maximum utilization of domestic resources, improvement of international cooperation, guarantees for freedom, self-sufficiency and socialist orientation, protection of national interests and security, conservation of national culture, and protection of the

Joining the AFTA, APEC, and WTO invariably involves trade policy changes to conform with the rules of these organizations, as well as some commitments to gain greater access for other members to Vietnam's markets for goods and services in return for the benefits of membership and the greater access that members may provide for Vietnam's exporters.

East Asian economies, including Japan and China, have been among the most open of all developing countries, but their openness and outward-orientation have not been based on dogmatic adherence to free trade. In East Asian economies, the governments actively intervened, both for the promotion of exports and selectively fostering import substitution. These interventions, along with other sound domestic policies, help to explain the superior growth performance of these economies (see Section 4.4). The experiences of East Asian economies indicate that with appropriate state intervention, Vietnam can benefit strongly from further trade liberalization.

9.1.1 Import Control Reduction

Becoming a member of AFTA, APEC and WTO, Vietnam has had to implement their requirements of reducing import controls. To become a member of WTO in 2005, at least, 80% of imports into Vietnam must be traded freely² (see Section 6.2.2.2). Yet, it is argued that if Vietnam liberalizes too quickly, it will be overrun by competition from other members. But good government interventions that ensure competitiveness can make

environment (CPV, 2001: 120-22).

² Compared with China before it became a WTO member, more than 80 percent of China's imports were conducted freely under market conditions (Shengming, 2000).

Vietnam competitive in a wide range of industries while being a net importer in other industries. Trade instruments are not a substitute for macroeconomic management. With good domestic policies, a liberalized trade regime in Vietnam will lead to the most efficient investment, particularly in labor-intensive industries like garments, footwear, certain agricultural products, tourism and so on³.

Another of Vietnam's concerns about external liberalization involves tariff revenue reduction. Like other transitional countries, Vietnam depends, to some extent, on import tariff revenue⁴. Consequently, Vietnam needs to coordinate tariff reduction with other tax reforms that ensure steady revenue collection. As argued in Section 8.2.3.4, the better way for Vietnam to raise revenue is by raising corporate and sale tax rates thanks to the insignificance of marginal costs, instead of raising rates for import tariffs, commodity input and factor taxes.

It is true that Vietnam has been steadily reforming and simplifying its import regime for a decade or more. Nonetheless, great complexity remained (Kokko, 1996; CIE, 1997). Vietnam still has a long way to go to harmonize its trade system with other members of AFTA, APEC, and WTO. For example, Vietnam introduced import tariffs as it began dismantling NTBs. The average tariff levels of about 16% in 2000 were modest (see Section 6.2.2.1), but the problem was with the tariff code that had 28 different rates from zero to over 100 percent (Anderson, 1999: 38). Furthermore, there was little rationale for this range. For example, in some cases, finished products had lower tariffs

³ This investment will inevitably be good for the rural communities, which attract some of this investment and send certain ratios of population to the cities for newly created jobs.

⁴ Import and export tariff revenues accounted for more than 20% of budget revenue from 1994 (see Table 8.19 and Section 8.2.3.4)

than intermediate products, creating negative protection for assembly operation (Dollar, 1999). As a result, rationalizing the tariff code must be done quickly before vested interests make dismantling protection difficult. Vietnam will also gradually deal with its outdated preferential measures for tariff reduction and exemptions. Tariffs will be lowered to the current level of 14% to 15% in developing countries. At the same time, Vietnam should safeguard the integrity of its tax laws and regulations. Taxes should be levied and calculated according to the law.

With trade reform to join the WTO, Vietnam is required to tariffy and bind all import restrictions, and offer MFN and national treatment to all WTO members (apart from the preferences given to AFTA members). Vietnam's trading partners will seek not only complete and bound tariffication, but also the lowering of tariff binding (albeit over several years), particularly in cases where protection levels are high. Where NTBs are currently in place, it is difficult to know how high those levels are. The higher these tariff bindings, the more likely other members will demand market access at low or zero tariffs. Some imported products are subject to duties based not only on the CIF import unit value, but also on reference prices. While the ostensible purpose of such customs practice is to overcome the problem of tax evasion by under-invoicing imports, the high value of some of those reference prices suggests this instrument is also serving a protection purpose. As a result, other members of these organizations will require Vietnam to reduce the use of reference prices⁵. Yet, the introduction of harmonized trade facilitation measures required by AFTA could reduce Vietnam's use of reference prices.

⁵ Because some imported food products - like dairy products, flour, sugar, and edible oils - are subject to duties not only on CIF import unit values, but also on reference prices, which, in fact, serve a protectionist purpose.

9.1.2. Export Promotion Measures

In parallel with reduction of import controls like tariffs and NTBs, following the China's experience (Shengming, 2000), Vietnam's export strategy should gradually change from extensive management of the export trade to a more intensive approach that seeks to enhance the quality of products. With the abolition of mandatory export plans and remittance of foreign exchange to the authorities and the subsequent lowering of disincentives, the obstacles that foreign enterprises encounter in gaining export approvals will be greatly reduced. Enterprises will, therefore, enhance the quality of export commodities, improve their structure and increase their economic effectiveness. The pattern of irregular growth in exports will disappear and a reasonable level of export growth will be achieved.

To date, Vietnam places quantitative restrictions on exports of items like rice, forest products and so on every year. Export taxes, levied on 58 tariff lines of farm and forestry products with rates ranging up to 45%, yielding a weighted average export tariff of 14 percent of government tax revenue to finance the country's Agricultural Price Stabilization Fund⁶. NTBs affecting exports include temporary prohibitions. A ban on exports of forest products - such as logs, sawn timber, laminated timber, cane, rattan, firewood and charcoal - is also in place⁷. This ban is to restrict deforestation, in part for

⁶ Payments from this Fund are used to support producer prices on these and other farm products when those prices are unusually low.

⁷ However, since exports of finished products - such as chip boards and wood chips - are still allowed with quotas, it is not clear how much this ban on wood product exports prevents tree felling (Anderson, 1999: 35).

environmental reasons. It should be noted that export quotas and prohibitions are not allowed under Article XI of the WTO, even though export taxes are allowed⁸. Hence, the other members are likely to demand that quantitative restrictions on exports be converted to export taxes. Converting quotas to export taxes would add to policy transparency as well as to government tax revenue. Lowering that tax over time would, of course, stimulate export growth and raise incomes of rice producers. At the same time, government revenue reduction - due to export tax decrease - would be compensated by boosting import tariff revenues because greater export earnings provide the foreign currency to import more.

9.1.3. Reform of the Foreign Exchange System

To support international economic integration, Vietnam should strategically adopt a policy of gradual reform of the foreign exchange system. First, it should relax the limitations on capital circulation related to trade, then limitations on long-term FDI and stocks, and finally, the restrictions on short-term capital floats. However, free convertibility of the capital account requires that some important conditions be met: (i) significant reduction in the financial deficit and a low inflation rate; (ii) a moderate debt level; (iii) coordination of domestic interest rates and international money market rates; (iv) enhanced competitiveness of the domestic financial system; (v) conformity of capital conditions in the domestic financial market with fixed standards; (vi) strengthened supervision and control of the domestic monetary system and establishment of

⁸ Behavior of export prohibition in general would not be tolerated, unless it can be shown to be consistent with the exceptions allowed under GATT Article XX.

government guarantees for an open monetary system

9.2 Industrialization Policy Changes

One study suggested that in 1992, China's exports were US\$36 billion (or 92%) higher than they would have been in the absence of economic reforms over the preceding decade (Drysdale and Song, 1995). In 1996, Anderson with others estimated that external liberalization associated with WTO membership would boost China's annual trade growth by 50% to 60% in 2005 (Anderson, Dimaranan, Hertel, and Martin 1996: 22). Like China, trade liberalization in Vietnam also makes changes in export and import volumes. While export volume rose by 11.8%, import volume increased by only 0.4% (Table 8.16). This suggests that with economic integration into the globe and region, Vietnam will reduce its trade deficit because commodities such as processed food, ceramics, glass, paper, wood product, cement and construction material, sewing, wearing, leather that Vietnam has strengths in producing have found consumer markets (Section 8.2.3.3, Table 8.16). However, with reference to China's experiences, the first point to underline is that normally, these gains have been accompanied by other domestic policies, particularly by substantial industrial upgrading and transformation in trade and industrial specialization⁹ (Drysdale, 2000).

⁹ The first phase of this transformation saw the emergence of the competitive strength of the textile and clothing industry as China established comparative advantage in labor-intensive production. At the same time, capital for capital-intensive production still continued in this phase as a legacy of China's heavy industrial strategies in the pre-reform years. The second phase is now under way, with the emergence of more capital-intensive exports, in areas where labor costs have risen, and are now an increasing important element in Chinese trade growth (Drysdale, 2000)

9.2.1 Changes in Industrialization Strategy

The experience of China and the simulation exercise in Section 8.2.3.3 raise a fundamental question about a industrialization strategy for Vietnam to accelerate industrial upgrading and productivity growth. Many economists and scholars in Vietnam argue that the pace of industrialization could be accelerated by giving special support and protection to leading industrial sectors. This idea was prominent in some official thinking about Vietnam's industrialization strategy and lay behind the slogan of the "two transitions", namely: the transition from a centrally planned to a market economy, and the transition from extensive to intensive growth with the development of high value-added industries. The sectors enjoying special support include electronics, automobiles, infrastructure, informatics and even the real estate sector.

Is the movement towards market prices for all sectors of the Vietnamese economy, including the new high growth sectors like electronics, machinery, and transportation equipment, likely to either encourage faster industrial upgrading or permanently lock Vietnam into so-called extensive industrial development. This is the critical problem that policy makers should be addressing. The problem is not whether the government should invest in human capital and other infrastructure to support industrial, technological and scientific development across industrial sectors, but whether the government should intervene to temporally insulate some sectors of the economy from international market competition.

Being member of AFTA, APEC and WTO will have a big impact on Vietnam's industrial upgrading. According to the simulation in Section 8.2.3.2, the further promotion of liberalization has caused many impacts on Vietnam's industrial upgrading in the forms

of changes in output, input demand, factor demand and goods prices in the whole economy and in every sector (see details in Tables 8.12 and 8.13). On the one hand, outputs of both labor and capital-intensive manufacturing industries - namely sector 4 (aquaculture), sector 5 (coal and mining), sector 6 (wine, beer, tobacco and non-food processing), sector 8 (ceramics, glass, paper and wood products), sector 9 (cement, wood product and construction material), sector 10 (chemicals, printing and other industrial product), sector 11 (sewing, wearing, leather), sector 12 (electricity, gas and water supply), sector 13 (construction), sector 15 (transport and communication) - increased. On the other hand, outputs of agriculture, banking and tourism - including sector 1 (paddy), sector 2 (rubber, coffee, sugarcane and other crop), sector 3 (animal husbandry, agricultural service and forestry), sector 7 (other food manufacturing), sector 14 (hotel, restaurant and tourism), sector 16 (finance, banking and insurance) – contracted; but sectors 14 and 16 were very negatively impacted, with output falls of 4.2% and 1.9% respectively (Table 8.13). Among output-increasing sectors, production efficiency in sectors 8, 9, 10, and 11 improved most strongly because input demand increased at rates less than output growth rates (Table 8.13).

To rapidly integrate into AFTA, APEC and WTO, the Vietnam government should deliberate and elaborate plans for trade liberalization as well as protection of several manufacturing industries, since it is allowed to apply safeguard measures to protect infant industries in the transitional period. Yet, protecting some manufacturing industries, Vietnam should pay attention to three criteria of protection for infant industries, namely: (i) the protected industry achieves fast productivity growth over time; (ii) satisfaction of the Mill test (the infant industry must grow faster than competing world producers); and (iii) satisfaction of the Bastable test (i.e. the benefit of infant industry

promotion must eventually compensate for the costs involved in the learning period) (see more in section 3.2).

9.2.2. Private Sector Development Policy

One of the most important policies for rapid economic integration into the world economy should be considered for development of small and medium-sized private enterprises. In East Asian Economies, small enterprises have employed more people than large companies and have high rate of job creation¹⁰. Therefore, Vietnam's government should have a strategy for SME development, which in turn is needed to generate meaningful jobs, incomes, poverty reduction, domestic savings and taxes to sustainably support increasingly higher levels of human well-being in Vietnam. The government can support SME participation in global trade by providing trade and market information services, market research, and trade missions for SMEs. The government can also help SMEs by arranging international matching services, providing appropriate information and data, and conducting trade fairs and expositions. The government can develop small business incubators and industrial parks for SMEs involved in international trade and investment (Chris Hall, 1994). Vietnam's government can also offer relief for SMEs from domestic value added and other taxes, and provide financial incentives, grants, and guarantees to them for exporting and investment. The government not only encourages SMEs to take an international perspective and to develop competence in international trade through management training programs, but also provides consultancy services to SMEs interested

¹⁰ Free entry of new firms, most of which started out as small and medium sized firms, was a key element of economic success of East Asian economies.

in exploring and entering export markets. Moreover, the government can sponsor technology programs that help upgrade production and service capability of SMEs to international standards¹¹.

Like other transitional economies, Vietnam has conducted preferential treatment to SOEs at the expense of private enterprises in terms of access to trade licenses, land, credit and bureaucratic approvals, placing domestic private enterprises at a significant disadvantage. Whereas equitization of SOEs in itself may not require private sector development, a level playing field on which the private sector can compete with SOEs is essential for development of the private sector. Therefore, to establish the level playing field for both SOEs and PEs, it is necessary for Vietnam to carry out a number of reforms including changes in legal, financial and budgetary policies. Apart from that, private sector development can also be enhanced by policies that encourage decentralization of functions and services.

At the same time, the government should take effective measures to restructure SOEs and to equitize those that can be better managed by private businesses and non-government organizations. Managing equitization effectively requires careful goal setting, program development, and program implementation and follow-up (Dennies and Iacono, 1996). Vietnam's experience of equitization in the past few years suggests that if government officials do not have clearly articulated goals and objectives, it is difficult to choose appropriate methods of equitization and to design the structural reforms that will

¹¹ Notably, the Central Committee of the Party finished the fifth Plenum (tenure IX) in March 2002 which devoted considerable attention to the possibility of allowing the further development of the private sector. It is also worth noting that members of the CPV will now be able to engage in private business.

be necessary to make them work effectively¹².

Besides, the government must prevent excessive collusion through antitrust laws, reducing barriers to entry, and eliminating marketplace impediments to competition. At the same time, Vietnam should enact economic stabilization policies aimed at improving the balance-of-payment, rescheduling SOE debts, controlling money supply, reducing subsidies to SOEs, and adjusting wages appropriately, especially for civil servants.

9.2.3 Promotion of Social Equity and Human Resource Development

In China and other Eastern European countries, one of the social problems that has arisen from their economies' integration into the world economy has been lay-off by SOEs. This, in turn, has resulted in higher levels of unemployment in urban areas and lower incomes for the poorest segments of both urban and rural labor forces. As a result, the establishment of a social safety network to protect economically vulnerable segments of the population in these countries is considered the most important policy priority, which involves (i) protection of the pension system, where the pension is the primary and sole source of cash incomes for aged and infirm people; (ii) creation and maintenance of reasonable unemployment benefits for those workers released from their jobs in SOEs or laid-off due to restructuring after privatization, or in the process of changing employment; (iii) establishment and maintenance of a health and social insurance system to provide subsidies for workers who face short-term loss of income because of health contingencies;

¹² Apart from that, SOE reform and privatization in Vietnam have proceeded slowly because once stabilization was achieved and foreign investment began to flow into SOEs, policy makers lost enthusiasm for SOE reform.

(iv) maintenance of social assistance programs for the disabled, the disadvantaged, or the poor who are adversely affected by economic reforms, economic opening and/or privatization (Lin, 2000; Sanjeev and Hagemann, 1994: 14-17).

In contrast to the experience of these economies, the most vulnerable people in Vietnam are not those laid off by SOEs¹³, which had only 4 percent of the total labor force in 2001 (Tran Van Tho, 2001), but very poor rural households¹⁴ (see Sections 7.3.4 and 8.2.3.1). Therefore, the government of Vietnam should alleviate widespread poverty and protect economically vulnerable segments of the population from the catastrophic impacts of economic integration, at least until they are able to participate productively in market activities¹⁵. This requires strengthening or creating new organizations and fiscal arrangements for: (i) providing social services and increasing the access of the poor to

¹³ Those people laid off by SOEs were among the better off in Vietnam - they were provided with generous severance packages (on average, one year's salary, or four times higher than in Russia) and were quickly absorbed by the growing private sector.

¹⁴ The main reason for some households in Vietnam's rural areas are more vulnerable today than prior to the reforms is due to changes in the methods for financing local services. During the centrally planned period, local agricultural cooperatives were able to serve many social functions, including the operation and maintenance of local schools, health clinics, day-care centers and hunger relief for the destitute. With transformation to the system of household contracts in 1988, these local services had to be financed by household contributions and payments. The vast majority of households attained higher incomes, which has helped finance these services, previously funded by cooperatives. Yet, for those whose incomes did not increase (orphans, disabled, aged without family support, people living in remote areas, individuals or communities facing shocks such as severe family illness or natural disasters), the cancellation of the cooperative system left a serious gap in the social safety net (see more in Section 7.3.4).

¹⁵ Since 1997, Vietnam has been appreciated by many international organizations like the World Bank, ADB and so on, for achievements in poverty alleviation.

basic education and health services; (ii) opening access to credit for the poor by changing the criteria for creditworthiness and decentralized credit institutions; (iii) expanding productive employment opportunities and sustainable livelihoods for unemployed and underemployed people; (iv) increasing the participation of the poor in the development and implementation of poverty alleviation policies and programs to assure they are needed and appropriate; (v) providing an adequate social safety net to protect those excluded temporarily or permanently from the market; (vi) pursuing policies that promote economic growth and increase productivity so that new opportunities are available for the poor to improve their living standards; (vii) increasing the people's capacity to use resources in a sustainable and environmentally beneficial manner.

In order to achieve these goals, there should be an effective labor market, which distributes labor among the various economic sectors through mechanisms of demand and supply. Like China, the labor market in Vietnam consists of workers in rural areas who are employed in agriculture or in small commercial, service, and production enterprises, and workers in urban area who are employed in the formal sector (both public and private sectors) or in the informal sector as self-employed or casual wage labor (see more in 7.3.2).

Therefore, the task of Vietnam's government is to create a freer labor market and to steadily improve its functioning and efficiency. The government plays an important role in assuring that employers of both public and private sectors are free to decide on the size of their work force based on efficiency criteria. Workers should be free to allocate themselves with little or no restriction between the public and private sectors, between large and small enterprises, between enterprises and self-employment, and among different industries and sectors of the economy. Policies should ensure that workers have

unrestricted geographic mobility. Labor policies should create an effective legal framework for employee-employer relations that protect the rights of both. Apart from that according to experience of East Asian economies, the government should enact the policies which provide a social safety net for workers temporarily unemployed or permanently disabled, and occupational safety regulations that protect the health of workers without placing on employers an undue comparative disadvantage.

9.3. Some Preparations for Entry into the WTO

In 1995, Vietnam made its initial application to join the WTO. The first stage of the process required Vietnam to describe its trade regime and to respond to WTO members' questions for clarification (see Section 6.2.2.1). In Vietnam's case, WTO members asked over 1,500 clarifying questions, more than for any other previous applicants, and indicated that Vietnam's trade regime was extraordinary complicated and difficult to describe on paper. The evidence suggested that Vietnam's trade system was complicated and restrictive in principle but relatively open in practice. This phenomenon came from the common practice of paying bribes to move goods quickly through customs. This closed-on-paper but open-in-practice regime created two serious problems: First, as long as Vietnam has great labor cost advantages, paying bribes to move goods may not be a major impediment to growth, but as Vietnam develops, the corruption could become a more systemic impediment¹⁶; Second, industrial countries, such as the United States -

¹⁶ For example, according to Rafidah Aziz, Malaysia MITI Minister, due to various high "hidden costs" in Vietnam, many Malaysian companies which had moved to Vietnam were now thinking of returning to Malaysia (*The Star*, 3 August 2002).

which tolerated an asymmetric relationship in the past, in which developing countries could maintain restricted trade regimes while enjoying MFN status in the U.S. market - have now reassessed their positions (Dollar, 1999). Therefore, in Vietnam-US bilateral trade, the US government has required Vietnam to meet WTO standards in order to get MFN status in the US market. This will increase Vietnam's interest in consolidating trade reform by removing restrictions on paper, reducing opportunities for corruption, and meeting international standards expected by other WTO members.

The experiences of other recent and prospective acceding countries, particularly China, suggest accession to WTO members' markets might not occur if there were no significant commitments to not introducing export subsidies¹⁷, to making the services market accessible, and to removing at least some preferential assistance to State Trading Enterprises. On the contrary, accession will be successful if Vietnam abides by WTO rules, including getting intellectual property rights legislation in order, publishing details of all trade and trade-related policies, and notifying the WTO any changes to these policies.

While the WTO does not forbid licensing systems, it requires the methods to be transparent, quotas open, and formalities simple. The products subject to import licenses will need to be administered in a much more transparent and rules-based manner, as stipulated in the WTO Agreement on Import Licensing Procedures. Consequently, the direction of trade reform is to reduce the variety of commodities controlled by license and

¹⁷ Even though GATT contracting parties only had to commit to reduce their export subsidies. Up to date, Vietnam does not subsidize its agricultural exports, which is the most thing demanded by other members in the future. Yet, the government wish expressed in its Memorandum on Foreign Trade Policy is to reserve the right to use agricultural export subsidies in the future (SRV 1996: 78). While that is in principle negotiable, in practice it is likely to be disallowed.

transitional measures - including non-quota license management and open competition - will be introduced. Overlapping cross-management measures will be alleviated and formalities simplified. Vietnam's licensing system will conform more closely with the international standards set by the Tokyo Round Agreement on Import License Formalities.

There are provisions in the WTO's Sanitary and Phytosanitary (SPS) Agreement and the GATT Article XX allowing import restrictions where necessary to protect human, animal or plant life or health. However, a case would need to be made for each case so claimed. The members will scrutinize the cases carefully, and again, are likely to apply stricter standards than currently apply to present WTO members (Anderson, 1999: 34).

SPS import bans apply to meat, eggs, dairy products and honey from Vietnam (SRV, 1996: 128). These and other quarantine restrictions on Vietnam will have to be justified scientifically to conform to the SPS agreement. Although Article X of the agreement provides some scope for LDCs to delay compliance, bilateral accession negotiations will nonetheless focus on any excessive barriers which, if not reduced to what is scientifically justifiable, could be basis for complaints of not opening market by those members adversely affected.

Becoming a member of AFTA, APEC, and preparing to be a member of the WTO, not only put pressure on Vietnam's policy-makers to move forward with dismantling NTBs and rationalizing the tariff code, but also force Vietnam's government to stop direct supports or subsidies to SOEs¹⁸. This kind of direct or indirect support through tariff

¹⁸ However, many forms of domestic support for agriculture are allowed by APEC and WTO. In Vietnam's case, these include such public investment programs as agricultural research and development, rural education and health, rural infrastructure (like roads, electricity, telecommunications, irrigation), mitigation

barriers will not be acceptable to Vietnam's trading partners. Even protecting certain industries in Vietnam would clash with Vietnam's commitments to AFTA, APEC and eventually to the WTO to reduce protectionist barriers. Thus, WTO accession requires Vietnam to eliminate SOE privileges including monopoly positions and provision of cheap credit to SOEs, meaning that WTO accession offers an opportunity for the Vietnam government to reduce the anti-trade bias and inefficiencies of SOEs in terms of marketing, transportation and distribution services.

Some additional components that might be considered in developing good trade policy practices and effective WTO involvement follow: (a) adopting an economy-wide, all-of-government view of trade and trade-related policies, rather than an ad hoc piecemeal or sectoral view of selected issues; (b) understanding well the long-term trading interests of the economy and using this knowledge to develop a clear strategy for seeking out highest-pay-off market access opportunities; (c) taking an active interest in new issues of pertinence to Vietnam as they emerge on the WTO agenda; (d) engaging the domestic interest groups who stand to gain from Vietnam's involvement in the WTO (particularly exporters) to help skeptics, and those who fear they might lose from more openness of its virtues; and (e) analyzing the effects of prospective and potentially negotiable policy changes at home and abroad on the Vietnamese economy, particularly

of natural disasters such as floods and typhoons, and the greening of barren land and mountains. At the same time, domestic support in the form of payments from the Agricultural Price Stabilization Fund are more questionable, since these payments directly support producer prices when they fall below certain thresholds, and thereby boost the trend level of production above what it would otherwise be. As a result, at the very least, the government may be required to make the operational rules of the Fund explicit and transparent, and to bind the levels of support via this mechanism.

in the context of rapid industrialization and structural changes¹⁹ (Hoekman, 1995; Anderson, 1996; Michalopoulos, 1998; Anderson, 1999) .

To get opportunities from WTO membership, according to Anderson (1999), Vietnam should consider the following choices:

* *Whether or not to bind tariffs at well above applied tariffs.* It might be argued that this would provide bargaining chips for future negotiations, and leave the government with flexibility to raise protection rates in the future. However, economies even bigger than Vietnam have found that they are too small to have any bargaining power with such chips, and found that the downside of retaining some flexibility to raise protection is that it leaves the government vulnerable to protectionist interests seizing the opportunity to raise protection, whether the government likes it or not.

* *Whether or not to keep MFN tariffs well above the lower preferential ones to fulfill AFTA commitments.* It is argued that Vietnam can compete within ASEAN, but cannot compete with the rest of the world. The fallacy in this argument is that every economy has comparative advantage in some products and no economy has a comparative advantage in every product. So, only currently protected industries, which do not have comparative advantage, may find it difficult to compete if AFTA commitments were multilateralized. The downside of retaining higher MFN tariffs and lower tariffs on AFTA trade²⁰ is that it may cause welfare-reducing trade diversion and lower Vietnam's overall tariff revenue collection.

* *Whether or not to keep industrial tariffs high so as not to slow down or reverse economic industrialization and modernization.* It is argued that if the domestic prices of

¹⁹ This will improve the government's understanding of Vietnam's trade interests.

²⁰ This could well be legal under GATT Article XXIV.

protected heavy industrial goods were relatively lower than the prices of farm products due to the removal of industrial tariffs, the output of agriculture would be larger than for industry. Thus, Vietnam would revert to being a more agrarian economy, especially if investment in rural infrastructure were to expand. However, this view ignores three important points: (a) agriculture is made profitable in ways which would boost the commercialization of agricultural production and lead to a lot of upstream and downstream agribusiness activities; (b) unskilled labor-intensive manufacturing would also blossom with less competition for resources from currently protected heavy industries; (c) the greater income generated from allowing the country's comparative advantage to be better exploited would raise the demand for myriad goods and services that are not tradable internationally because of prohibitive transport costs, which would encourage growth in the output of non-tradable goods (see Berg and Taylor, 2000, for more argument).

** Whether or not to keep the prices of food staples such as rice low to assist poor consumers.* Of course, restricting non-food imports and food exports lower the domestic price of food relative to other tradable commodities. Yet, the majority of the poor in Vietnam are net sellers rather than net buyers of food. In this case, the poor become poorer because of low food prices, and the majority of net food buyers with high incomes enjoy much better incomes than farm households. In case of food price rises, the small minority of farm households, who suffer from such price rises can be assisted much more cost-effectively through more direct means, most obviously by providing an environment that facilitates the growth of unskilled labor-intensive activities;

** Whether or not infrastructure and human capital investments in rural areas are too expensive per capita to be warranted.* It is obvious that there is a greater density of

population in urban areas, so, it is relatively cheaper to provide urban people with roads, electricity, telecommunication services, basic education, health services, and the like. However, a number of studies demonstrate that social rates of return to infrastructure and human capital investments in the rural areas of developing countries are very high, even when farm prices are lower than in international markets. These rates would be even higher when farm prices are allowed to rise.

9.4 Concluding Remarks

From what has been mentioned earlier, it can be said that external liberalization to the outside world and reforms of domestic policies and institutions are two sides of the same coin – sometimes, they complement each other, and sometimes, they inhibit each other. External liberalization cannot proceed without domestic reform; at the same time, liberalization may be a precondition for domestic reform. Vietnam's economic reforms have unfolded in a gradual and progressive, rather than an abrupt manner. Liberalization and reform should match each other, not only in depth and breadth, but also in terms of timing. This has proved to be one of the most important underlying factors in the recent success of Vietnam's reforms and integration. Until the year 2001, how widely Vietnam opens itself to the outside world will depend largely upon the progress of domestic reforms introduced by the government in light of the experiences of the transitional economies and the EANIEs in the last forty years.

From China's experience, in order to face the challenges of rapid integration into AFTA, APEC and the WTO in the 21st century, Vietnam's government should create a

system of governance²¹ that promotes and supports market development, and at the same time, advances the health, safety, welfare and security for its citizens. Vietnam's government must find new and effective ways to use political power in support of socially equitable economic development. To get new and effective ways, Vietnam must redefine the state's role in the economy and society; improve government efficiency and responsiveness to citizens' needs; expand infrastructure and social overhead capital needed by individuals, businesses, and industries to integrate effectively into the global economy; decentralize and democratize the government and political system; and strengthen the administrative and financial capacities of local administrative authorities²².

²¹ The concept of governance can broadly be defined as the "exercise of political power to manage a nation's affairs, and it encompasses the state's institutional and structural arrangements, decision making processes, implementation capacity, and the relationship between government officials and the public" (Pierre Landell-Mills and Ismail Serageldin, 1992: 304). Three elements of governance are considered important for development, namely: (i) the form of the political regime; (ii) the way the authorities manage the country's economic and social resources; and (iii) the capacity of government to design, formulate and implement policies and discharge functions (World Bank, 1994: xiv)

²² It is widely thought that in order to perform its functions more effectively and to ensure the implementation of structural adjustments, Vietnam should decentralize more administrative and political system. The reason is that the ability of businesses and industrial production to compete successfully in international trade and investment and to generate profits in domestic markets depends on the quality of support services and physical infrastructure, but central government may not be able to create an effective business environment or to respond quickly to changes in local needs and conditions. Therefore, decentralization allows citizens, or their representatives, to influence the formulations and implementation of policies more effectively than if all decisions were made by a small political elite or only by national political authorities. Political decentralization implies the selection of representatives from local electoral jurisdictions. Selection of officials from small jurisdictions allows citizens to better know their political representatives and allows local representatives to better know the needs and desires of their constituents.