CHAPTER 6:

THE SECOND PHASE OF THE RENOVATION POLICY:

INTERNATIONAL ECONOMIC INTEGRATION POLICIES

OF VIETNAM SINCE 1995

To overcome the problems and difficulties of the first half of 1990s mentioned in chapter 5 and to obtain better economic performance in the face of international economic integration, at the VIII Congress held at the end of 1996, the CPV has endorsed the goal of transforming the country into an industrialized economy by the year 2020: “The strategy of Vietnam towards 2020 is striving to make Vietnam an industrialized country with advanced technical material infrastructure, rational economic structure, progressive production relations in conformity with the development of productive forces, high quality material and cultural life, strong national defense and security, and an equitable and civilized society by the year 2020” (CPV, 1996). Based on assessment of progress towards this goal in the period since introduction of the renovation policy (see section 5.3), the five-year plan for the period 1996-2000 laid out a number of broad objectives to meet the government’s long-term development goals of industrialization and modernization as follows: (i) achieving a high and sustainable rate of economic growth by increasing economic efficiency; (ii) continuing development of a multi-sectoral market economy under socialist-oriented state management; (iii) tackling serious social

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1 The plan has envisaged a doubling of per capita GDP over the decade 1990 to 2000, as a step towards the target for 2020 of eight to ten fold increase in GDP over the 1990 level.
problems, substantially reducing poverty and generally improving living standards; (iv) promoting harmonious economic development of all regions; (v) increasing internal accumulation (national savings) and creating the conditions for more sustainable and rapid development; and (vi) sustaining a high level of military security (CPV, 1996).

These were ambitious, but not unattainable targets. However, they involved meeting a series of conditions about the relative contributions of different sectors to the growth process. Industry and construction were expected to be at the forefront of the development process, even as agricultural productivity was expected to grow rapidly and the sector release labor for employment in the secondary and tertiary sectors. The targets also involved exceptional performance in mobilizing domestic and foreign savings, and in sustaining the efficiency of investments made with these savings. The targets were also conditioned on major achievements in human capital enhancement, to provide the work force with skills and health standards to meet the demands of a rapidly industrializing economy.

To implement these targets, Vietnam’s government has carried out the second phase of renovation, which emphasized economic policies for integration of Vietnam’s economy into regional and global economies. The policies for international economic integration are meant to play an important role in Vietnam’s industrialization since Vietnam is located in the most rapidly growing region of the world\(^2\). A key principle

\(^2\) According to the UNIDO projections, by 2025, Korea, Taiwan and Singapore will enjoy per capita incomes in excess of those of Australia and New Zealand. Malaysia, Thailand and Indonesia will all be above the 1996 OECD average income, and China will not be far behind. By 2025, the Chinese economy will be nearly twice as large as the economy of the United States (UNIDO, 1996: 55). Much of this growth was made possible by the expansion of world trade and international investment flows. For Vietnam, proximity to newly industrializing economies, such as Taiwan, Malaysia, Korea and Singapore, provides
embraced with the second phase of renovation is for Vietnam to pursue the benefits of engaging with the international market economy. With foreign trade and investment acting as key sources of goods and services and providing larger markets for Vietnamese producers, developments in regional and global economic blocs, as well as trends in key markets, become important factors in shaping the economic development of Vietnam. Vietnam has made great efforts to promote open trade and investment on a regional and global basis. Its accession to AFTA and APEC, and pursuit of WTO membership reflects an appreciation of the importance of these institutions for Vietnam\(^3\). However, Vietnam is not alone in undergoing economic transition - many countries in Eastern Europe and the former Soviet Union are competing for capital and markets. Therefore, Vietnam’s government has carried out a series of economic policies for integration of its economy into regional and global economic blocs - AFTA, APEC and WTO - to seize opportunities and overcome difficulties arising from international economic integration to industrialize the economy. These policies focus on both carrying out internal economic reforms in terms of adjustment of macroeconomic parameters, private sector investments promotion, resolution of SOEs issues, and implementing external liberalization in the sense of policies for FDI and foreign trade promotion.

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both market opportunities and inward flows of investment. Increasing integration within the Asia Pacific region should facilitate these flows.

\(^3\) According to Shigemitsu Sugisaki, deputy IMF managing director: “Vietnam’s adherence to sound macroeconomic policies and firm implementation of the reform agenda will sustain further progress in industrializing the country, in raising economic growth, and reducing poverty” (*The Sun*, 23 November 2001).
6.1 Internal Liberalization For International Economic Integration

6.1.1 Adjustments of Macroeconomic Parameters to Sustain Development

6.1.1.1 Argument for Adjustment of Macroeconomic Parameters

Vietnam’s recovery in the middle of the 1990s has been based on an increase in the investment rate (Table 5.6) as well as on adjustment of the investment structure toward a large-scale basis by reviewing the construction projects, canceling those not considered urgent. This is necessary to concentrate resources on completion of key projects and selecting transitional projects. Priority would also be given to comprehensive and intensive investments in existing projects. Vietnam’s continuing struggle to engender increased growth while keeping inflation, current account and fiscal deficits under control is difficult.

In order to analyze the macroeconomic constraints relating to Vietnam’s growth, it is supposed to use a 3-gap model based on 1996 economic performance (described in Appendix 5)⁴. Vietnam’s dependence on foreign savings for investment was equivalent to 9.1% of GDP (see Tables 5.6 and 6.8). In 1996, the merchandise trade deficit represented 16% of GDP, while import and export volumes were 46% and 30% of GDP respectively. Imports increased by 37% in 1996 alone (see Table 8.24). Hence, two comments need to be made: (1) reductions in foreign savings utilization can be expected to have large impacts on capacity utilization and the growth rate; and (2) Vietnam has become quite a

⁴ This exercise is useful to characterize an economy’s macroeconomic status, abstracting from year-to-year trends in setting elasticities and identifying a consistent set of ingredients required for future macroeconomic stability.
Table 6.1: Vietnam: Equilibrium Data Set for the Year 1996
(percentage of potential economic activity)

<table>
<thead>
<tr>
<th>Variable</th>
<th>Variable Definition</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>U</td>
<td>Capacity utilization</td>
<td>94.0</td>
</tr>
<tr>
<td>g</td>
<td>Growth of potential economic activity (in percent)</td>
<td>9.5</td>
</tr>
<tr>
<td>i</td>
<td>Total investment</td>
<td>28.2</td>
</tr>
<tr>
<td>(i_g)</td>
<td>Government investment</td>
<td>8.9</td>
</tr>
<tr>
<td>(i_p)</td>
<td>Private investment</td>
<td>19.3</td>
</tr>
<tr>
<td>(s_g)</td>
<td>Government savings (government revenue less consumption)</td>
<td>3.4</td>
</tr>
<tr>
<td>(s_p)</td>
<td>Private savings</td>
<td>15.7</td>
</tr>
<tr>
<td>(\phi)</td>
<td>Foreign savings</td>
<td>9.1</td>
</tr>
<tr>
<td>PSBR</td>
<td>Public sector borrowing requirement</td>
<td>5.5</td>
</tr>
<tr>
<td>(j^*)</td>
<td>Net foreign interest payments</td>
<td>3.2</td>
</tr>
<tr>
<td>x</td>
<td>Merchandise exports</td>
<td>30.0</td>
</tr>
<tr>
<td>m</td>
<td>Merchandise imports</td>
<td>46.0</td>
</tr>
<tr>
<td>(m_r)</td>
<td>Imports of raw materials and intermediates</td>
<td>28.2</td>
</tr>
<tr>
<td>(m_k)</td>
<td>Imports of capital goods</td>
<td>13.4</td>
</tr>
<tr>
<td>(m_o)</td>
<td>Other imports</td>
<td>4.4</td>
</tr>
<tr>
<td>(\eta)</td>
<td>Net foreign capital inflow</td>
<td>5.2</td>
</tr>
<tr>
<td>R</td>
<td>Change in reserves (in percent)</td>
<td>0.0</td>
</tr>
</tbody>
</table>

Source: GSO, 1999

A trade dependent economy. The public sector borrowing requirement (PSBR) was also high at 5.5% of GDP. In 1996, Vietnam’s total investment rate of 28.2% of GDP greatly exceeded the total domestic savings rate of 19.1%, consisting of a private savings rate of 15.7% and a government savings rate of 3.4% of GDP\(^5\) (see Table 5.6). Vietnam’s foreign

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\(^5\) The split between public and private investment is even more difficult to identify in the case of Vietnam. Capacity utilization in 1996 was calibrated at 94% to reflect the high rate of employment accompanying the rapid growth rate.
interest payments were a significant 3.2% of GDP. Vietnam received US$1.7 billion in actual inflows of FDI in 1996 (see the values of indicators in Table 6.1).

The calibration analysis suggests the following important challenges for Vietnam: (i) Total investment has to be brought up in line with domestic savings in order to reduce dependence on foreign savings; in an alternative scenario, the investment rate may decline to 25.4% down from the calibration value of 28.2%; (ii) There should be a consistent reduction in foreign savings utilization from 9.1% to 5.6% of GDP; (iii) A reduction in the PSBR from 5.5% to 3.5% of GDP would be consistent with this scenario, taking into account a reasonable movement of the fiscal gap with its own parameters; (iv) The import-GDP ratio could be kept at about 42%, instead of 46% in the year 1996 (though in the medium term, this indicator may decline, given the large increase in 1996), and the export-GDP ratio should increase by 3% (Table 6.3).

**Table 6.2: Adjustments of Elasticities and Parameters**

<table>
<thead>
<tr>
<th>Elasticity and parameter</th>
<th>For equilibrium data set</th>
<th>Adjustment scenario</th>
</tr>
</thead>
<tbody>
<tr>
<td>Elasticity of fiscal effort</td>
<td>0.40</td>
<td>0.50</td>
</tr>
<tr>
<td>Elasticity of private savings</td>
<td>0.50</td>
<td>0.70</td>
</tr>
<tr>
<td>Elasticity of intermediate import demand:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>With respect to overall activity</td>
<td>0.45</td>
<td>0.60</td>
</tr>
<tr>
<td>With respect to export activity</td>
<td>0.30</td>
<td>0.45</td>
</tr>
<tr>
<td>Accelerator coefficient</td>
<td>1.00</td>
<td>1.00</td>
</tr>
<tr>
<td>Private response to government investment</td>
<td>1.10</td>
<td>1.25</td>
</tr>
<tr>
<td>Proportion of investment sourced domestically</td>
<td>0.59</td>
<td>0.40</td>
</tr>
</tbody>
</table>

These changes cannot induce a large reduction in growth rates if other elasticities will be adjusted in the following direction (Table 6.2): (i) The elasticity of the fiscal effort
was increased by 25% from 0.4 to 0.5; (ii) The elasticity of private savings was permitted to increase by 40% to 0.7 from 0.5; (iii) The responsiveness of private investment to state investment was increased by 0.15; (iv) The proportion of investment sourced domestically would fall by 32% from 0.59 to 0.4, with the planned moves for entry into AFTA, APEC and WTO; (v) The elasticity of intermediate import demand with respect to overall economic activity would increase by 33% from 0.45 to 0.60; (vi) The elasticity of intermediate import demand with respect to exports would be raised by 50% from 0.30 to 0.45.

Table 6.3: Vietnam’s Economy after Adjustments of Elasticities and Parameters (as percentage of potential economic activity)

<table>
<thead>
<tr>
<th>Variable</th>
<th>Variable Definition</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>u</td>
<td>Capacity utilization</td>
<td>84.7</td>
</tr>
<tr>
<td>g</td>
<td>Growth of potential economic activity (in percent)</td>
<td>8.4</td>
</tr>
<tr>
<td>i</td>
<td>Total investment</td>
<td>25.4</td>
</tr>
<tr>
<td>i_s</td>
<td>Government investment</td>
<td>7.7</td>
</tr>
<tr>
<td>i_p</td>
<td>Private investment</td>
<td>17.7</td>
</tr>
<tr>
<td>s_s</td>
<td>Government savings (government revenue less consumption)</td>
<td>4.4</td>
</tr>
<tr>
<td>s_p</td>
<td>Private savings</td>
<td>15.4</td>
</tr>
<tr>
<td>ø</td>
<td>Foreign savings</td>
<td>5.6</td>
</tr>
<tr>
<td>PSBR</td>
<td>Public sector borrowing requirement</td>
<td>3.5</td>
</tr>
<tr>
<td>x</td>
<td>Merchandise exports</td>
<td>33.0</td>
</tr>
<tr>
<td>m</td>
<td>Merchandise imports</td>
<td>42.0</td>
</tr>
</tbody>
</table>

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6 Vietnam had increased its fiscal effort by 50% since 1989, but it is doubtful that comparable increases in effort can be achieved in the future.

7 This elasticity anticipates non-destabilizing efforts to improve the financial system.

8 This assumption might actually be conservative.
The overall results of these adjustments (see Table 6.3) suggest that growth in the range of 7-8% can be achieved. The attainable capacity utilization fell to a less inflationary level of 84.7%. Pursuant to the consistent level of the trade, ICOR, and continued access to foreign savings, the investment rate of 25.4% of GDP might permit a growth rate of about 8%. Success in improving the elasticity of the fiscal response will reduce dependence on foreign savings and foreign investments.

Hence, in 1997, the Third Plenum of the Central Committee of the CPV (the 8th Tenure) issued a resolution on strengthening the efficiency of international economic cooperation as well as mobilizing internal resources to industrialize and modernize the country. One measure to mobilize internal financial resources is to encourage private sector development.

6.1.1.2 Encouragement of Private Sector Development

In order to integrate its economy into the world and regional economies, besides SOE reforms (discussed in section 6.1.2), Vietnam’s government has paid attention to promotion of private sector (see Chapter 5). Vietnam’s private sector has developed as a result not only of productive forces unleashed, but also desire to get rich legitimately. Profits generated by business proprietors consist not only of gains from assets and capital pooled in business, but also for their management and the risks taken. Lack of compensation for such risks will discourage entrepreneurship. Therefore, the government has made legislation for the private sector, which has been introduced since the early
1990s to allow development of various forms in this sector⁹. By 1995, there were only about 1,800 joint stock (shareholding) and limited liability companies, representing only 8% of total registered capital, while sole proprietary owners accounted for most form of business in the manufacturing sector with 5,030 companies, but accounting for only 3% of total registered capital in the economy (UNDP and MPI, 1997: 68)¹⁰.

From 1995 to 1999, the number of private industrial firms rapidly rose to more than 600,000 units (Packard, 2001: 23), but their role in the economy was still small since the economic environment remained significantly biased against the private sector vis-à-vis SOEs, manifested in discriminatory financial and institutional incentive structures. Then, due to 1997-98 Asian financial crisis, the economy faced a regional slowdown. The government decided to promote the private sector by substantially reducing regulations and promulgating the Enterprise Law in January 2000¹¹, which replaces the outdated Law of Companies and Private Enterprise Law. The government realized that while the state budget’s limited revenue should be concentrated in the pivotal manufacturing and service fields, the private sector - in terms of small and medium enterprises - could invest in other

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⁹ These were the Law on Companies and Law on Private Enterprise promulgated in 1990. Recognition of the private sector was institutionalized in the 1992 Constitution, according to which a citizen has the right to do business freely in line with the law (Article 57); household and private capitalist economic activity are entitled to choose business/manufacturing forms and established enterprises without scale limits in fields favorable to the people’s livelihoods (Article 21).

¹⁰ According to Vietnamese law, there are three private ownership forms, namely (i) a limited liability company with more than two owners or more than one organization; (ii) a sole proprietor company as a small-scale one owner unlimited liability company; (iii) a shareholding (joint stock) company having more than 7 shareholders with satisfaction of the minimum capital legal requirement.

¹¹ The 2000 enterprise law exemplifies another vital step in the legal framework by further reaffirming the private sector’s long-term status and guaranteeing citizens’ entrepreneured rights.
areas to create more jobs, contributing to GDP growth and state revenue. As a result, the government has urged ministries, branches and local authorities to strictly abide by the Law on Enterprises and speed up implementation of the Law.

However, there are skeptical views on the effectiveness of the new law because a number of state agencies are still unwilling to implement it. According to a report of the Ministry of Planning and Investment (MPI), some ministries insist on implementing and enforcing old legal documents that have been nullified since the Law became effective. They have refused to issue business registration certificates or certificates for changing business scope. Previously, several ministries as well as city and provincial authorities issued “temporary bans” on the establishment of businesses in a number of fields such as travel, shipping, taxis and overseas study consultancies. The World Bank estimates that it may take another two or three years before the new Law can operate effectively, since some key supporting legislation needs to be passed, and there are numerous laws and regulations inconsistent with the new Law which needs to be abolished (East Asian Quarterly Brief, 31 January, 2000).

Anticipating such situations, the government established a task force to oversee implementation of the Law. The government scrapped more unnecessary business sublicensing in the future. Simultaneously, the MPI was asked to prepare guidelines for the establishment of business registries to help the private sector to develop, while the task force and relevant agencies were required to draft suitable conditions for new business operations, such as private detective services and public opinion surveys. By the end of the year 2000, there had been about 30 documents to be issued guiding implementation of the Law in detail. As a result of the detailed implementation of the new Law, and

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12 For instance, Decree No 02/2000/ND-CP, Decree No 03/2000/ND-CP, Decree No 30/2000/ND-CP,
renewal of administrative reform, there was little disruption in the transition from the old law to the new Law on Enterprises.

It is widely hoped that the Enterprise Law would improve the business climate because this law allows businesses to simply register their operations instead of having to navigate through the licensing labyrinth\textsuperscript{13}. Under the new Law, the virtual "temporary bans" on the establishment of businesses was over except for meeting several requirements in the new Law. In the early of 2000, Prime Minister decided to eliminate 84 sub-licenses - in the forms of business licenses and certificates for practice - found to be inconsistent with the Law and considered no longer necessary for the economy. To further stimulate business operations, the government abolished 27 sub-licenses and changed 34 others into trade conditions in August 2000 (see Decree No 30/2000/ND-CP). Hence, it could be said that with the Law on Enterprises, the government created a sounder trading environment, improved management efficiency, and made a breakthrough in administrative reform.

After more than one year of implementation of the Law on Enterprises, some remarkable results had been achieved: (i) promoting the establishment of new household enterprises. Over 14,400 enterprises were set up in 2000, a 2.5-fold increase over the previous year\textsuperscript{14}. In the first sixth months of 2001, another 9,100 enterprises were

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\textsuperscript{13} The Law helped reduce the time required for establishment of an enterprise from three months to 7 days. In HCM City, the one hour business registration system was put on trial, helping reduce establishment costs from VND10 million to VND500,000. About 150 business licenses have been revoked (\textit{Government Press Release}, 3 April 2001)

\textsuperscript{14} Among them were 50 one-member limited liability companies, 726 joint stock companies (more than in the previous 9 years) and two partnerships. Besides, over 5,000 branches and representative offices were set
registered. Deregulation of export activities since July 1998 resulted in a jump in the number of non-state export enterprises; (ii) further mobilizing internal financial sources for economic development and industrialization. The total registered capital of the enterprises and household business set up in 2000 amounted to VND24,000 billion (US$1,714 million), of which VND17,000 billion (US$1,214 million) was registered as new capital, and VND7,000 billion (USD500 million) as supplementary capital, i.e. 5 times more than in 1999. In the first sixth months of 2001, there was newly registered capital of VND11,167 billion (US$744.5 million), representing a 1.5-fold increase in the number of enterprises and a 2-fold increase in registered capital against the same period in 2000; (iii) partly reducing the critical issue of unemployment. In 2000, the new enterprises created more than 500,000 jobs and the incomes of employees were raised. Currently, there are more than 1 million, working in the formal private corporate sector, representing approximately 3% of the total Vietnamese labor force; (vi) regaining the confidence of the international community, particularly international donors and foreign investors, thereby attracting more ODA and FDI, serving the aims of economic development and industrialization, and facilitating the private sector’s integration into the world economy.

Despite gains from the implementation of this Law, there remain quite a few obstacles to the development and operation of enterprises as well as deficiencies in implementation of the Law, namely (i) there are some vague or unsuitable stipulations, especially those concerning household businesses and punishments for breaches of
business registration regulations. Also, some important regulations guiding implementation of the Law have not been issued\textsuperscript{15}; (ii) there still exist common negative phenomena such as requests for presentation of unnecessary legal papers; refusal to grant licenses to trades businesses not on the prohibition list; granting of licenses already abolished or invalid (e.g. certificates for slaughter hygiene, organizing trade fairs or exhibitions and so on); (iii) there are several lists of trade and business activities subject to conditions in certain areas, but the regulations for these conditions lack clarity. As a result, in some cases, government agencies have failed to grant licenses or certificates on schedule; (iv) post-registration management of enterprises remains perplexing and inefficient, particularly for management methods and inspection, checking out the identity of persons establishing enterprises\textsuperscript{16}, handling violations by enterprises\textsuperscript{17}, and launching information network systems of enterprises; (v) there are still some investors and managers of enterprises who are not fully aware of their rights and responsibilities, or who are not law-abiding.

Why are there so many obstacles and deficiencies in implementing this Law?

\textsuperscript{15} For example, so far there are no decrees on the procedures for transforming SOEs or the enterprises of political and socio-political organizations into limited liability companies; no list of trades and businesses, where foreigners have the right to contribute up to 30\% of the legal capital of these enterprises; no regulation on granting licenses for law consultancies, and veterinary services; no circulars on determining agencies authorized to approve registration of gold production and processing.

\textsuperscript{16} In fact, some authorities, especially those at district level, lack information about the personal identity of persons who would like to establish enterprises; they often ask for certification of identity issued by residential squatters or ward people's committees to be enclosed with the application for registration.

\textsuperscript{17} Practically, there are no regulations on the competent agencies, appropriate forms or procedures to deal with violations, such as not hanging signboards or wrong lettering of signboards and names and so on.
There are several reasons, namely (i) the Law has some new, complicated articles and this makes implementation difficult; (ii) civil servants, especially the leaders of ministries and provincial people’s committees, are not fully aware of fundamental changes in the Law, thereby failing to visualize the effects of such changes on fulfillment of their functions and tasks in the fields concerned; (iii) some ministries and local authorities have failed to issue proper instructions. They are not in favor of detecting and eliminating difficulties or obstacles to enterprises; (iv) a large number of civil servants deliberately attempt to prolong the old mechanisms or maintain them in a different form since they do not want to change; (v) in many cases, administrative punishment has not been strict enough; even the Prime Minister has failed to take bold steps to deal with violations in the stipulation of the Law and government decrees; (vi) enterprises are not fully aware of the significance of the expansion of their rights, responsibilities and duties in organizing their business activities and in defending their legitimate interests.

In order to overcome these obstacles and deficiencies so that further implementation of the Law on Enterprises will integrate Vietnam’s private sector into regional and global economies, some suggestions follow.

First, there must be complete preparation for implementation of the Law on Enterprises. Those ministries and agencies that have collected and publicized the lists of licenses and lists of business conditions consistent with Decree No 30/2000/ND-CP should review implementation, procedures, conditions and the system of licensing. At the same time, within their areas of competence, they should also revise or supplement the Law or suggest revisions and amendments of the Law to create more favorable conditions for enterprises. In special cases, the Ministry of Justice should introduce regulations granting certificates for law services; the Ministry of Agriculture and Rural Development
should issue regulations granting certificates of practice for veterinary services; the State Bank of Vietnam should identify competent agencies to certify statutory capital for gold producing and processing establishments, and suggest ways to do so. Besides, in collaboration with the Ministry of Justice and the Government’s Office, the MPI should identify the vague and inappropriate stipulations in the decrees guiding implementation of the Law, and suggest revisions and amendments. They should also coordinate with relevant agencies to design a list of all registered trade and business activities in the economy.

Second, discipline and order in implementation of the Law have to be strengthened. In cooperation with concerned government agencies, the MPI should prepare a decree on administrative fines for violations in business registration. In the immediate future, there are some necessary measures to be considered for use: (i) Provincial People’s Committees have to instruct and help the Department of Planning and Investment (DPI)\(^{18}\) to require enterprises to hand in annual financial statements according to regulations; (ii) Enterprises, which deliberately refuse to do so will be punished\(^ {19}\). The DPI will publicize in the mass media the names of enterprises that refuse to correct wrong information in their applications for business registration\(^ {20}\); (iii) Enterprises that apply, add to, or change the contents of their business registration are obliged to present copies

\(^{18}\) In Vietnam the Department of Planning and Investment of each province belongs to province with respect to administration, but is under the management of the MPI.

\(^{19}\) Their business registration certificates will be revoked in accordance with Point c, Clause 3, Article 121 of the Law on Enterprises.

\(^{20}\) In these cases, the DPI will request the police to check on the veracity of business registration details in line with Clause 4, Article 116 of the Law on Enterprises; and can revoke certificates of business consistent with Article 16 of the government Decree No 02/2000/ND-CP issued on 3 February 2000.
of the meeting minutes and decisions made by the Council of Shareholders, Council of Members, or Management Council; (iv) The business registry offices, under instructions and with assistance from the DPI, will supervise enterprise observance of the Law. When detecting violation, the office will, in a timely way, ask the enterprise to correct itself in compliance with the Law; if not, punishment will be imposed on offending enterprises.

Third, all overlap in the inspection of enterprises must be eliminated, and the efficiency of state management should be gradually improved. In the short term, the State Inspectorate will instruct implementation of Decree No 61/1998/ND-CP on enterprise inspection, and enhance coordination among the competent state agencies so as to minimize overlaps in the inspection of enterprises. In addition, the State Inspectorate will collaborate with concerned state agencies to put forth recommendations to amend and supplement regulations on inspection of enterprises, with special attention to making clear distinctions among “inspection”, “examination”, and “investigation”; to identifying “competent agencies” in charge of inspection and examination of enterprises so as to focus only on areas where the interests of state and society need to be defended; defining the content and scope of each kind of inspection and examination; setting criteria for appraising the findings of inspections and examinations, and making conclusion from such findings.

6.1.2 Reforms of SOEs

Apart from encouraging the private sector (see section 6.1.1.2), another way to mobilize internal financial sources is to reform the SOEs. Due to trade liberalization, SOEs have faced severe competition, not only in world market, but also in domestic markets. It has
been increasingly recognized that SOEs in Vietnam are too weak to be competitive in the world environment of economic integration\(^{21}\), since the scale of most SOEs is small or medium-sized by international standards\(^{22}\), and most of them are financially, managerially and organizationally fragile. In order to increase the effectiveness and strength of SOEs in order to integrate into the regional and global economies, the government of Vietnam has taken many measures such as carrying out new registration of SOEs, disbanding those incurring losses for a long period without hope of recovery, equitizing (privatizing) SOEs, restructuring SOEs\(^{23}\). Vietnam's policy on reform of SOEs is aimed at renovating and effectively developing the SOEs to ensure their leading role in a socialist oriented market economy as manifested in the following functions: (1) to boost economic growth and

\(^{21}\) SOEs gives rise to many problems of concern: only 40% of all SOEs are making profits, breaking even and loss-making SOEs account for of 40% and 20% respectively, i.e 60% of SOEs are not operating profitably; for many years, the financial situation of SOEs has remained unhealthy. Outstanding debt has been from 1.13 to 1.7 times larger than the state-invested capital, debt payment have accounted for 80% of SOE contributions to state revenue. The profit yield has always been smaller than interest on bank loans. 60% of SOEs have not had enough legal capital. Many products of SOEs - such as fertilizers, steel, and cement - are sold at price of 10 to 30% (or even 70 to 80% for raw sugar) higher than imported items. The products of SOEs that can be exported make up only 15% of the total. Only 1.3% of SOEs are recognized as meeting ISO 9000 standards (\textit{Nhan Dan}, 19 April 2000).

\(^{22}\) Small and medium sized enterprises account for 80% of total SOEs, over 50% of which do not have enough circulating capital in proportion to their production and business scales. Their technological bases are 20-30 years behind those in the region and the world. 34% of facilities for industrial production have been used for 10-20 years (\textit{Nhan Dan}, 19 April 2000).

\(^{23}\) IMF directors released US$52 million for Vietnam on 21 November 2001 and urged the government to quickly pursue reform of the SOEs. The disbursement brought total support for Vietnam under the current IMF program to about US$105 million (\textit{The Sun (Malaysia)}, 23 November 2001).
development; (2) to pave the way for development of other components; (3) to help government carry out its functions of macro-economic adjustment and management.

6.1.2.1 Restructuring of SOEs

a. Situation

Restructuring of SOEs has been carried out in accordance with Ordinance 388/HDBT, going through three stages:

The first lasted from 1991 to 1994, in which temporary measures were taken to deal with the organizations, mechanisms, policies and finance to rearrange the SOE units. This also involved the first comprehensive check up of the SOEs to review their performance, according to which eligible SOEs were allowed to re-register for operation\textsuperscript{24}. SOE equitization was started to carry out in this period.

The second stage lasted from 1995 to 1997, during which the government continued SOE reorganization and dissolved cartels of enterprises and state general departments that were merely administrative intermediaries. SOEs were concentrated to

\textsuperscript{24} Between 1991 and 1994, all SOEs were required to re-register, while those not meeting the prescribed capital requirements, which varied according to each industry, were to be merged into larger entities or liquidated. Producers who would like to establish new SOEs were also disciplined, by requiring larger initial capital contributions five times bigger than the minimum level for the industry, in an attempt to ensure such enterprises would be able to stand alone in the market place. The average registered capital for SOEs was about US$1.1 million, of which centrally managed enterprises averaged US$2.8 million while locally run enterprises averaged US$425,000 (GSO, 1996: 41). Although there was the process of merger and liquidation, half the current SOEs made losses during 1996 (Vietnam News, 31/12/96), and only a few hundred were large and profitable enough to supply the bulk of state revenue.
develop state general corporations 90 and 91 (see later in this section). The law on SOEs in April 1995 marked a significant milestone in instituting a legal framework for SOEs, which clearly defined their responsibility and obligations. The law abolished administrative obstacles, distinguished between state macro-management and state management of SOEs business activities, and enlarged the initiative and autonomy of basic units.

The third stage was launched in middle 1998 with Ordinance No 20/1998/CT-TTg on 21 April 1998. In this stage, the government has shifted from funding SOEs to transferring capital to SOEs, from capital allocations to fixing legal capital. SOEs may use capital and funds, and may change their capital and asset structures to develop production and business efficiently, with capital guarantees for development. They can mobilize and use capital and assets to invest in other operations. At the same time, the government promulgated Ordinance No 15/1999/CT-TTg dated 26 May 1999 on structures, operations and organizations of the general corporations.

By 1995, after completion of the first stage (1991-94), there were only 5,962 SOEs (Table 6.4), including 1,953 centrally-run SOEs and 4,009 locally-run SOEs divided into four groups:

Group 1 includes SOEs operating in the field of security and national defense, and those connected with national secrets (e.g. prospecting mineral resources). The government maintains 100% ownership over their assets. After restructuring drive, those failing to fulfill tasks allotted to them were to be disbanded. New SOEs were eventually to be established to carry on the tasks of the disbanded SOEs.

In 1988, the whole country had 12,269 SOEs (Dang Duc Dam, 1997: 126), of which 47% had less than 100 employees; only 4% of SOEs had more than 1000 employees (Tran Van Tho, 2001)
Table 6.4: Vietnam: Number of SOEs, 1988-2000

<table>
<thead>
<tr>
<th>Year</th>
<th>Total SOEs</th>
<th>Equitized SOEs</th>
<th>Sold SOEs</th>
<th>Transferred SOEs</th>
</tr>
</thead>
<tbody>
<tr>
<td>1988</td>
<td>12,269</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1989</td>
<td>12,000</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1992</td>
<td>6,545</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1993</td>
<td>6,264</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1994</td>
<td>6,019</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1995</td>
<td>5,962</td>
<td>5</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1996</td>
<td>6,025</td>
<td>5</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1997</td>
<td>5,873</td>
<td>18</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1998</td>
<td>5,847</td>
<td>57</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1999</td>
<td>5,700</td>
<td>370</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>2000</td>
<td>5,200</td>
<td>502</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>


Note: Equitized, sold and transferred SOEs on a cumulative basis

Group 2 consists of SOEs, which ensure the supply of public goods and services and serve the government’s macro-management requirements. SOEs in this group normally need big capital and get low profits, but serve the interests of the national economy. All capital of these SOEs is funded by the government.

The SOEs of Group 3 are enterprises getting big profits and becoming major contributors to budget revenue. In following years, the government may continue to hold 100% ownership, or a dominant part of the assets of these SOEs. Government can gradually reduce ownership in these SOEs by equitizing and privatizing them (see section 6.1.2.2). Group 4 comprises all SOEs, which do not fall into the above three categories.
(usually small and medium size enterprises, with backward technologies). These not need remain as SOEs. In the future, they should be equitized and privatized.

Market principles must be applied to all SOEs except those in Group 1. With regard to second group SOEs, the government may subsidize them for a number of years, but the number of subsidized SOEs and subsidy values will gradually decrease with the general development of the economy. At the same time, SOEs of this group will be disbanded whenever they are unable to develop, and new enterprises will be set up. According to market competitive principles, SOEs of Group 3 and 4 carrying out effective business will continue to develop; otherwise, they will go bankrupt. All SOEs have to comply with the Law on SOEs approved by the National Assembly on April 20th, 1995.

Moreover, in order to implement the policy on formation of large state-owned corporations consistent with the experiences of Japanese corporate groups and Korean chaebol, in March 1994, the government enacted Decision No 91/TTg on the formation of 17 enormous corporations (called General Corporation 91, or GC 91)\(^\text{26}\), aimed at significant agglomeration of capital to carry out the investment necessary for modernization of the economy, creating a diversified industrial structure, and strengthening the international competitiveness of Vietnam’s economy by separating management from ownership. Each GC91 has a minimum authorized capital of VND500 billion (about US$50 million) and at least 7 voluntary SOE members, among which there should be a separate financial enterprise responsible for raising and distributing capital. At the same time, the Prime Minister approved Decision No 90/TTg to allow various ministries and equivalent bodies to set up 76 other corporations (called General

\(\text{26 Existing GC91s are in electric power generation, coal, cement, steel, oil, airlines, rubber, textiles, leather and shoes, posts and telecommunications, railways and so on.} \)
Corporation 90, GC90) with a minimum authorized capital of VND100 billion (US$10 million) and at least 5 SOE members, but without a financial company. GCs are based on branch organization that is all the SOEs in the GCs should be producing similar or complementary products or services. In terms of size, capital and employees, GC 90s are smaller than GC 91s.

By 1995, General Corporations 91 and 90 had about 2000 member enterprises, representing 30% of all operating SOEs, i.e. 70% of all centrally-run SOEs, and accounting for 66% and 55% respectively in terms of capital and employees, (Dang Duc Dam, 1997: 167-68, Review of Economics and Prognosis, March 1999, Hanoi). In late 2000, the GCs 91 and GCs 90 had 1,392 independent subsidiaries accounting for 24% of the total number of SOEs, 66% of state capital, and 61% of the state corporate sector's workforce (Saigon Times Weekly, 25 August 2001). They play key roles in balancing major commodities, materials, and foreign exchange for the economy as well as in price stabilization and economic development.

Hence, it seems that Vietnam has been reforming its public sector in compliance with the advice of the World Bank, according to which only a handful of strategic enterprises as well as some non-strategic ones unattractive to private investors are to be retained, while all the rest should begin the process of privatization (equitization) immediately (World Bank, 1995). Such a strategy, if implemented, would leave the public sector looking very much like those of Vietnam's Asian neighbours. Nevertheless, the Vietnamese definition of what constitutes a "strategic" industry appears to differ markedly from that of the World Bank. The latter provides what it claims to be an "uncontroversial" definition of a strategic enterprise as one producing important public goods and services, which may not be available in sufficient quantities if left to the private
sector such as defense, education, flood control, water supply, and waste management (World Bank, 1995: 111). For the World Bank, natural monopolies may also be included in the public sector. The Vietnamese definition of the appropriate field for public enterprises stresses socio-economic development objectives, rather than the shorter-term efficiency-oriented criteria suggested by the World Bank\textsuperscript{27}. Thus, while accepting the need for market relations to dominate in resource allocation in order to increase the efficiency of the economy, to achieve higher growth rates, the Vietnamese government has attempted to nurture and protect state ownership of the means of production, particularly in those industries, likely to be at the leading edge of the drive towards modernization, like electronics, metallurgy, fuel, power, machinery and petrochemicals.

\textit{b. Results and Issues}

In 1999, there were more than 5,700 SOEs (Table 6.4), of which 732 SOEs belonged to group 1 and 2; the rest belonged to group 3 and 4. SOEs created 40.2\% GDP, more than

\textsuperscript{27} According to Phan Van Tiem and Nguyen Van Thanh, strategic enterprises include those producing essential public goods, that play an important role in the development of mountain and remote areas as well as those that act as the locomotive pulling the whole economy towards sustainable higher growth, in which private enterprises cannot play a major part (Phan Van Tiem and Nguyen Van Thanh, 1996: 4-5). In the opinion of Hoang Cong Thi, strategic enterprises include: (i) key SOEs in the national economy closely associated with the state's macroeconomic regulatory role, without which private companies may manipulate the government and move the economy in directions beyond its control; (ii) enterprises that invest where non-state companies are still not able to invest such as medium and small sized hydroelectric power stations, factories producing goods for exports, fertilizers and insecticides for agriculture (Hoang Cong Thi, 1992: 3).
50% of total exports and contributed more than 39% of budget revenue. It is expected that there will be 3,000 SOEs left in 2003 and only 2,000 SOEs left in 2005. Therefore, labor working in the SOEs will be reduced by 25%, from 1.6 million to 1.2 million. Among the 2,000 SOEs, there will be 1,489 SOEs in the form of joint-stock companies\(^\text{28}\), representing 65% of total SOEs, while 380 SOEs will be merged, accounting for 16.7% and the rest will be dismissed and bankrupted (Phan The Hai, 2000). SOEs, in which the government will hold a controlling stake, will not exceed 600, and will fall into three groups: (i) those operating in monopolistic sectors (power transmission, money printing, and so on); (ii) large ones which make significant contributions to state revenue, promote the development of other sectors, use high technology as well as stabilize the macro-economy (food, petrol, mining, machine manufacture, telecommunication, information, and so on); (iii) those producing necessities to develop production and improve the people’s living standards in mountainous and remote areas.

At the present, SOEs as well as restructured SOEs in Vietnam still encounter a number of problems: (i) It is not clear who the real owner of SOEs are since there are too many organizations involved. The lack of clear ownership identification undermines corporate governance as it leads to the issue of who should be monitoring the managers\(^\text{29}\),

\(^{28}\text{In June 1999, the government promulgated Decree No 44/1999/ND-CP on “transformation of the SOEs into Joint-Stock Companies” to enhance and promote the equitization of SOEs, because the government recognized that equitization is an important measure to restructure the public sector, raise capital and enhance economic efficiency.}\)

\(^{29}\text{Since 1995, the capital and assets of SOEs have been under the management of the Ministry of Finance, but the operations of SOEs have been supervised by their respective line ministries or local governments. However, the reduction in power of the line ministries has not always led to reduced interference in the day-to-day activities of SOEs. That is why the directors of SOEs are still constrained by various regulations}\)
(ii) With increasing autonomy, but without a control system, directors tend to privatize national assets in their own enterprises at the expense of the state budget and national financial system\textsuperscript{30}; (iii) The budget constraints of SOEs have converted from “soft” to “hard”, but due to increasing financial difficulties recently, have tended to become “soft” again, particularly in large SOEs\textsuperscript{31} (Tran Van Tho, 2001).

In addition, the establishment of GCs was considered an important part of the process of renovating, reorganizing and restructuring SOEs to form of stronger economic organizations for the government to integrate Vietnam’s economy into the regional and global economies. The GCs\textsuperscript{91} have created clear effect in the achieving large-scale state-owned industrial group to develop business activities, unite all forces for resolution of market problems, reduce unhealthy competition among SOEs, and help some members to overcome difficulties. Although GCs 91 and 90 have just been operating for a couple of years, it may be asserted that the establishment of GCs has been a success\textsuperscript{32}, meeting market requirements, while achieving needed industrial coordination in the national from many organizations (Tran Tien Cuong, 1996: 14; Tran Van Tho, 2001).

\textsuperscript{30} Generally, the financial situation of the SOEs is unknown. Nobody - including the government, the owner of SOEs - is well informed about the financial condition of the SOEs.

\textsuperscript{31} The reason is that since the second half of 1997, along with the adverse effects of the Asian crisis, many SOEs have encountered financial difficulties and the government has had to extend assistance to protect large SOEs, which are considered to be playing a leading role in the socialist-oriented market economy. In a survey carried out in 1997, Wada (1998) showed that in terms of finance, since the SOEs faced a lot of difficulties, they tended to depend on government assistance, and intervention from government has become strong again.

\textsuperscript{32} Thanks to the establishment of GCs, several of the old enterprise unions, which were deemed to be operating ineffectively, have been or will be dissolved into their component parts, thereby removing an unnecessary layer of administration.
economy for international economic integration, as well as meeting the Law on SOEs with implementation details in Ordinance No 39/CP of June 27th, 1997.

It was also recognized by the government that the success of the GCs would depend both on long-term policies adopted for their future development and on the effective use of government capital given to these GCs. According to some other East Asian experiences, the GCs should receive government support for about decade to become internationally competitive. This would be followed by partial privatization to expand their capital base\(^{33}\). Partial privatization of some operations could also occur earlier through formation of joint-ventures with foreign companies, as has already occurred in the case of the steel and cement corporations (Beresford, 2000).

Apart from the advantages mentioned, the GCs have faced some formidable obstacles in becoming international competitive, namely: (i) almost all SOE subsidiaries were small in size and had much obsolescent and incompatible equipment\(^{34}\). As a result, GCs have to subsidize loss-making enterprise members; (ii) although management boards of GCs are established by line ministries and People's Committees, the distinction between the collective responsibilities of board members and the individual responsibilities of the board chairperson and general director are not clearly specified in the Law on SOEs (Law on SOEs, 1995: Articles 29, 30, 37), particularly in relation to the

\(^{33}\) For example, POSCO, the South Korean steel company, which began as a 100% SOE, has now privatized 65% of its equity; Singapore Airlines' state equity has been reduced from 100% to 54% since 1985.

\(^{34}\) In 1996, some 92% had self-financed capital of less than US$1 million, 46% had less than 100 workers and 89% less than 500 workers. Most equipment remained obsolete in the 1990s (only 18% of SOEs have been able to invest in new technology, and 25% have integrated plant and equipment, while other SOEs suffered from incompatible machinery purchased from various suppliers in the former Soviet Union and Eastern European countries (Nguyen Ngoc Tuan, 1996: 23-5)
conservation and development of capital and to SOE losses. There are also some cases of
general directors' disregard for the board chairperson, or vice versa; (iii) GCs consist of
voluntary SOE-members (Law on SOEs, 1995: Article 6d) and the management boards of
GCs have the power to transfer capital among members and to assign or transfer the right
to implement development investment projects (Law on SOEs, 1995: Article 45)\textsuperscript{15}. These
will cause increasing tension among members and between members and superior levels.
While the advantage of the GC model is concentration of resources in a large entity, some
of the dynamism of the more efficient members may be lost in the process.

Practically, among 17 GCs\textsuperscript{91}, only five (petroleum, post and telecom, electricity,
rubber, and shipbuilding) have fared well in their businesses. Corporations with many
loss-making subsidiaries include Vietnam Coffee GC (44 out of 61 subsidiaries are in
red), Southern Food GC (8 in the red, 15 break even), Northern Food GC (5 in the red, 7
break even), Vietnam Coal GC (7 in the red, 3 break even), Vietnam Garment and Textile
GC (5 in the red, 7 break even), Vietnam Steel GC (5 in the red, one break even), Vietnam
Paper GC (3 in the red, 5 break even), and Vietnam Cement GC (3 in the red) (Saigon
Times Weekly, 4 August 2001; 25 August 2001).

Therefore, recently, the government has allowed a pilot scheme to form a new
corporate model in the state corporate sector - the parent-subsidiary corporation. The
parent corporations will be wholly state owned entities, while subsidiary companies
operate in line with the law on SOEs and are governed by parent corporations, which will
be responsible for state capital invested in their subsidiary companies. It is hoped that this

\textsuperscript{15} However, many GCs are established mainly by the addition of SOE subsidiaries to meet the required
membership and are not based on voluntary will, business cooperation and alliance in production and
marketing.
new model will produce greater benefits for corporations and their affiliates, and relations between parent and subsidiaries shift from a merely administrative to a financial basis. If, indeed, this model proves to be superior, the pilot scheme will pave the way for all 17 GCs 91 to adopt it in the next five years.

6.1.2.2 Equitization of SOEs

For SOEs as well as other types of enterprises, the need to raise funds from the capital market will inevitably arise. Yet, since the early 1990s, SOEs have met many difficulties, both in mobilizing domestic savings and in getting loans from the state banking system. At the same time, in order to realize the development strategy of a multi-sectoral economy mentioned in the VII Congress of the CPV, the government has launched a program of at least, partial equitization of SOEs (i) to get capital to expand economic and business activities, (ii) to improve efficiency by renovating the management and working atmosphere, and changing production relation between employees and managers.

With Decision No 143/HDBT in May 1990, the government decided to undertake a pilot plan of equitization for several SOEs. In June 1992, the government promulgated Decision No 202/CT-HDBT on experimentally equitizing and privatizing seven SOEs for this plan. In the following years, the government issued various directives and decrees to

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36 After 3 years of implementation of Decision No 202/CT-HDBT, only 3 SOEs, had, in fact been equitized by early 1995. These were a shipping company, a firm assembling and servicing refrigerators and air-conditioners, and a firm producing cloth bags and shoes. Equitization of the first two firms took 18 months and the third firm completed equitization after 3 years. In the first two cases, the government retained 30% and 18% shares respectively, 40-50% was sold to workers and managers, and the rest to private citizens. The results of these two pilot equitizations were reckoned to be positive. After 18 months’ of operations, the
boost this work\textsuperscript{37}. However, up to early 1998, de facto equitization has not proceeded smoothly. From June 1992 to April 1996, 5 SOEs were equitized, with 25 more from May 1996 to May 1998 (\textit{Saigon Economic Times}, 30 November 2000; \textit{Vietnamese Economic Times: Economic Situation 1998-1999}).

The reasons for the slow pace of equitization can be summarized as follows: (i) So far, some government leaders as well as policy makers in the ‘government bureau for the equitization program’ have thought of equitization as mainly a way to recuperate unsuccessful businesses and not to be applied to profitable SOEs for fear of diluting the government role in the economy (\textit{Vietnam Investment Review}, 13-19 January 1997; Nguyen Ngoc Tuan, 1996: 28); (ii) The government’s unclear instructions have led to hesitation among ministries, branches, local authorities and SOEs for fear of bad effects to their interests. Meanwhile, a specialized government authority strong enough to help the government coordinate equitization effectively has not yet been established; hence, policies towards equitization are unsynchronized and incomplete, and their implementation is complex and time-consuming; (iii) Directors and managerial staff at SOEs tend to protect their vested interests in the SOEs, and given the lack of a social safety net or other security measures, employees in SOEs also protest against drastic

\textsuperscript{37}In 1993, the government formally encouraged other SOEs to prepare for equitization. Until 1996, equitization was realized on a voluntary basis. Only the SOEs to be equitized are registered with the government and prepared the necessary procedures. In May 1996, the government issued Decree No 28/CP on transformation of some SOEs into joint-stock companies, finalizing the experimental time for equitization. Yet, implementation of equitization under Decree No 28/CP remained tardy and uneven among ministries, industries and localities.
changes in ownership since they are afraid of unemployment, which is a serious social problem in Vietnam\(^{38}\), since they consider security of employment in SOEs more important than anywhere else; (iv) The process has faced difficulties estimating the value of SOEs for the purpose of selling them off. Factor such as product quality and acceptance, or other advantages/disadvantages of business have not been included in the valuations, which have relied on book values of assets. This means information on each SOE is hardly disclosed. Nobody, including the government, is well informed about the financial situation of the SOEs (Beresford, 2000); (v) Most equitization candidates are laden with heavy debts. Many have proposed the government write off their debts before going public; (vi) Preparation of the stock exchange has taken more time than expected. In fact, the process started in 1994, but the market only opened since July 2000; so far, the impact of stock exchange on SOE reform is almost negligible. It is commonly acknowledged that the birth of the stock exchange is an indispensable element of equitization, since it allows the market to assess the value of SOEs to encourage interest

\(^{38}\) Although the economy has had high growth in the 1990s decade, industrial and service sectors have not created enough employment to absorb redundant labor in both rural and urban areas. The labor force grew by one million each year in the 1996-2000 period and will increase by 1.2 million in the next decade, while the agricultural sector has only absorbed 600,000 laborers each year, and the service sector another 200,000, but the figure is on the decline. The industrial sector labor force, which accounts for 4 million, represents 10% of Vietnam’s total labor force, and creates less than 100,000 new jobs per year (Duong Van Sinh, 2001). Thus, the unemployment rate in urban areas reached around 12-15%. SOEs currently have about 1.6 million employees, accounting for about 4% of the total labor force, or about 34% of the secondary sector, where most SOEs are (Tran Van Tho, 2001). As a result of SOE reforms, a sharp decline of SOE labor has exacerbated unemployment issue. In 1998, the government set up the National Target Program on Employment (1998-2000), National Fund for Employment Promotion and Special Fund for Reorganization and Equitization to provide financial support to retrain retrenched workers.
from potential buyers\textsuperscript{39} (see more below); (vii) Not all equitized SOEs have been successful in business. A report from Ministry of Finance announced that critical issues in equitization is how money earned from the sale of shares is spent. As it stands, companies tend to deploy the money ineffectively, leaving much capital idle (\textit{Vietnam Investment Review}, 13-19 January 1997).

In order to stimulate rapid equitization for Vietnamese economy's integration into the world economy in the late 1990s\textsuperscript{40}, the government enacted Decree No 44/CP in 1998 to replace the outdated Decree No 28/CP, which was too rigid and not suitable for the current state of the SOEs. The new decree offered more open and proper regulation on equitization and settled many problems. According to this decree, SOEs were allowed to sell shares to foreign organizations and individuals for the first time. This served to start foreign portfolio investment in Vietnam. Restrictions on shares ownership were loosened. A person can now buy as much as 20\% of SOEs total shares if the government does not hold the majority of shares. At the same time, the decree clearly lists 13 important industries in which government will continue to be the controlling shareholder. In the rest, the government will hold at least 20\% of shares in all newborn joint-stock companies after equitization. But for SOEs outside these 13 industries, the government can sell 100\% of their shares, which is somewhat similar to privatization.

In 1998, the government set up the National Target Program on Employment

\textsuperscript{39} By the end of 2000, only 4 SOEs are equitized listed on the stock exchange.

\textsuperscript{40} Vietnam joined AFTA in 1 January 1996 as a result of ASEAN membership in 1995, and became APEC member in 1998. Therefore, Vietnam will fulfill its trade obligation with other ASEAN countries by 2006 as well as with APEC countries by 2020. Moreover, together with the bilateral US-Vietnam trade agreement signed in July 2000, prospective WTO membership in foreseeable future brought many challenges for SOEs in a new era of competition in their own domestic market.
(1998-2000), the National Fund for Employment Promotion and the Special Fund for Reorganization and Equitization to provide financial support to retrenched workers to retrain and to find new jobs. Practice shows that these institutions have been necessary and have provided the preconditions for pushing SOE reforms. Until recently, equitization has not progressed, partly due to the lack of such institutional infrastructure.

As a result, since 1998, although the speed of equitization has not been as fast as expected, equitized SOEs have risen substantially in number: from July 1998 to December 1998, 100 SOEs were equitized, with 250 more equitized from January 1999 to December 1999⁴¹. Up to the end of November 2000, the government equitized and privatized 502 SOEs (Phan The Hai, 2000; Vietnam Review, No 497, May 2000: 16-18) (also see Table 6.4).

With 502 equitized SOEs in 9 years, one positive result of equitization program is that the positive economic indicators of equitized SOEs have improved: on average, registered capital increased by 19.06% per annum, turnover by 46% per year, profit by 44% and budget contribution by 82% annually for 9 years. The incomes of employees were also raised by 14.3% each year. Besides, laborers holding shares got dividends from after-tax-profits, around 22-24% per annum⁴². Therefore, in general, both managers and

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⁴¹ By the end of December 1999, there were 370 SOEs that underwent equitization. Among them, there are 165 enterprises operating in industry and construction, 151 in commerce and services, 38 in transportation, 10 in agriculture, and 6 in aquaculture. It is worth noting that most equitized SOEs are small and medium sized, of which only 10% have registered capital over VND10 billion (US$1 million). The biggest company in terms of capital is Lam Son Sugar, with registered capital of VND150 billion (US$13 million). The government remains a shareholder in most new joint-stock companies. Only 25% of the transformed SOEs are free from state capital.

⁴² If the same amount of money was deposited in the bank, it would yield 12% per year at most.
employees in equitized SOEs felt happy and believed in the government’s direction to change the form of SOE ownership (Phan The Hai, 2000). Besides, the process helped equitized SOEs attract US$103 million from individuals and entities in all economic sectors, and the government received US$70 million to use for other purposes (Saigon Times Weekly, 25 August 2001).

There are still many problems and difficulties to be overcome and settled in order to accelerate the equitization, namely: (i) equitization means “selling” the business. How to determine its price? Both Decrees No 28/CP and No 44/CP estimate the value of a business on from financial records, which is not accurate. There are only a few auditing companies, and too much SOEs. Therefore, the stipulation that pricing procedures must be undertaken by an auditing company has caused too much trouble for SOEs. It is better for SOEs price their assets themselves and then for the government authorities to check and inspect. This will speed up the process and avoid negative feelings between SOEs and the auditing companies. Besides, specialized groups, which consist of many experts with good professional skills, enthusiasm, experience and a sense of responsibility, should be set up to speed up the process and to solve problems that may occur; (ii) it is not easy to deal with retrenched workers after equitizing their companies. Thus, each SOE should prepare its own plan to solve this problem. Besides, awareness of Vietnamese citizens in general, and the officials of SOEs to be equitized in particular, on the strategies and policies of equitization need to be raised. Since equitization is not only at the micro level concerning bussiness, but also at the macro level, relating to supply for the stock exchange, the government should enact a law to provide the legal framework for equitization.

In sum, the equitization of SOEs in Vietnam is still recent, since its economy is in transition from being a centrally planned economy to becoming a socialist-oriented open
market economy integrating into the world economy. To achieve the objectives of equitization, bringing about trust and confidence, execution at the moment and in future requires unanimous, decisive and flexible government policies.

6.2 External Liberalization Policies For International Economic Integration

6.2.1 New Policy for Attracting FDI

6.2.1.1 1996 Amendments to The 1992 FDI Law

Although the Law on FDI has amended twice since enactment in 1987, it still clearly has shortcomings. Many provisions are not suitable for the new circumstances. Such conditions require replacement of the Law on FDI with another Law, which should satisfy three key tasks, namely: (i) the amended Law will be more specific and simplified; (ii) the new Law should be seen as a transitional step towards a uniform law for both domestic

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43 In Gates view, equitization is not much of an answer for SOE reform. From what she read about the formally equitized SOEs, she confirmed that (i) equitized SOEs have not responded particularly well in terms of management, efficiency, technology and so on; (ii) the informally equitized SOEs, especially at the local level, have probably done a bit better, but this is only a guess (since it is not legal, it would be difficult to do any sort of real analysis); (iii) but even if this is so, such a equitization process will transfer rents from the SOEs (SOE management and workers) to PEs (manily old SOE managers and associates) (iv) probably, the hybrid processes (alliance between state managers and private entrepreneurs) have worked better; (v) the only way that Vietnam is going to take off is through unleashing and then supporting its domestic private sector – similar to what Taiwan did. This can be done through orthodox methods of infrastructure, education, training development + encouraging sectoral development (Michael Porter type method) (Gates, 2002).
and foreign investment in the near future; (iii) with economic integration into the WTO, APEC and AFTA, the Law should take into account the possibility of a common international investment code; at the same time, the Law should make full use of Vietnam's advantages, e.g. its low level of economic development.

In November 1996, amendments and additions to the Law on FDI were made by the Vietnamese National Assembly. Compared with the law previously amended in 1992, the 1996 law brought in 26 new articles, besides amendments and additions in 29 articles, totaling 68 articles, instead of the 42 articles of the 1992 Law\textsuperscript{44}. With regard to both form and content, the 1996 Law is new, with many more open and more liberal provisions, besides containing more stringent articles aimed at preventing possible loopholes in state management in this area, expressed as follows:

\textit{a. Investment promotion and tax incentives}

The 1996 Law lists projects in which foreign investments are not permitted (Article 3), as well as projects in which investment is encouraged or especially encouraged. The government gives more privileges to projects in which investment is especially encouraged. The period of exemption from profit taxes may be extended to eight years for projects from the day they begin to earn profits\textsuperscript{45}. Of course, these projects

\textsuperscript{44} In February 1997, the government promulgated Decree No 12/CP, which comprises 104 articles providing for detailed implementation of the 1996 Law on FDI in Vietnam. Compared with Decree No 18/CP dated 16 April 1993, regarding implementation of the 1992 Law on FDI, Decree No 12/CP has a new, more liberal content. It codifies the provisions of Decree No 18/CP and introduces new provisions already raised in various laws such as Decree No 191/CP, dated 28 December 1994, regarding regulations on the formation, examination and implementation of foreign investment projects in Vietnam and Circular No 215 UB/LXT dated 8 February 1995 of SCCI guiding FDI activities in Vietnam.

\textsuperscript{45} Previously, the period of profit tax exemption was only four years, and for the following four years, profit
should meet all the conditions and norms stipulated by the government. In these cases, the profit tax rate is only 10% of profit compared with the normal profit tax of 25% (Article 38).

In order to overcome existing troubles and big inequities for the privileges given to local and foreign investors to create a more solid legal basis for state management aimed at attracting FDI in desired areas and at raising their effectiveness, the 1996 Law contains a number of more stringent provisions. First of all, provisions for the exemption of taxes on automobiles and materials imported by FDI enterprises and joint ventures have been removed, except for imports of truck, used in production and buses for the transport of workers, and materials imported for especially encouraged projects (Article 47).

The government makes sure that foreign exchange for infrastructure construction and essential import-substitution goods production projects are provided enough. This is a significant new point removing foreign investor worries when they invest in economic projects important for Vietnam, but unable to generate enough foreign exchanges for their activities (Article 33).

As for capital contribution, the 1996 Law allows the foreign party/parties to contribute in Vietnamese dong (VND) from their other investments in Vietnam (such as profit, material liquidation, capital cession), not confining them to make only to foreign exchanges contributions brought from outside Vietnam as required by the previous Law (Article 7).

b. Reinvestment and establishment of new joint ventures

taxes were reduced by 50%.
To promote desired reinvestment, the 1996 Law stipulated that for reinvestment in promoted investment projects, all or part of the profit tax paid on reinvested profits shall be refunded, but the percentage (of profit tax) to be refunded depends on sector, region, form and duration of reinvestment (Article 42).

The forms of investment in the 1996 Law have been expanded. Foreign investors investing in the construction of infrastructure facilities may enter into BOT, BT and BTO contracts with an authorized state body (Article 19). The Law also explicitly allows the joint venture to cooperate with Vietnamese economic organizations to set up new joint ventures (Article 6).

The 1996 Law broadens the range of Vietnamese partners permitted to cooperate with foreign partners to set up joint ventures: besides economic organizations having juridical personality as previously provided for, hospitals, schools and research institutes on technology, science and technique are permitted to cooperate with foreign investors to establish joint venture in accordance with government decisions.

c. Unanimous decisions of Management Boards

The 1996 Law specifies and minimizes the number of questions requiring unanimous decisions of the Management Board (MB) of joint ventures to four key questions, namely: (i) appointment and dismissal of the director general, first deputy director general, and chief accountant; (ii) amendments and additions to the enterprise’s charter; (iii) approval of final annual financial statements and final financial statements of work construction; and (iv) loans for investment. With respect to other matters, the MB shall decide on the basis of simple majority voting by members present at the meeting (Article 14).

d. State management of FDI
The 1996 Law created a legal framework to heighten the quality of state management towards FDI, to reduce troublesome formalities with regard to investors, and to offer them more favorable conditions for seeking opportunities, investigating and designing projects in Vietnam. According to the new provisions, the time limit for appraising and licensing projects was brought down from 90 to 60 days. The Law also provides that the issue of permits for investment is no longer concentrated at the central level. Depending on the category of projects, the capability of the provinces and cities, local authorities are allowed to grant certain permits.

To prevent overstatement of actual investment, which has happened in certain joint ventures with foreign investors, two additional articles have been added to the 1996 Law regarding assessment of the value of equipment and machinery brought as capital contributions. According to the articles, the value of such equipment and machinery must be assessed and certified by an independent organization. The joint venture parties are responsible for the veracity and accuracy of the declared value of their respective capital contributions. At any time, the state FDI managing agency can designate an organization to reassess the value of the parties’ capital contributions. The report on the take-over of projects and financial statement on construction work must be certified by an inspection organization. The accounting system applied to FDI enterprises is thus more strict. FDI enterprises and foreign parties to business cooperation contracts use the Vietnamese accounting system. If another accounting system is to be used, approval of the Ministry of Finance must be obtained in advance. The 1996 Law also contains stipulation on tender processes. FDI enterprises and parties to business cooperation contracts must tender in compliance with the provisions of laws for tendering (Article 30, 37).
In sum, the 1996 Law on FDI marked important progress in improving the legal system for FDI in Vietnam. Amendments and additions have improved the management environment, encouraged FDI, created a basis for directing FDI to priority projects (in line with Vietnam's socio-economic development plan and strategy), prepared for international economic integration, and sought to ensure that investment cooperation with foreign countries is carried out on the principle of equality and mutual benefit.

6.2.1.2 The 2000 Amendments to the 1996 FDI Law

Although the 1996 Law on FDI is more liberal, since 1997, FDI to Vietnam has slowed down, which has been attributed to several causes, namely: (i) There are many shortcomings, which have not been dealt with timely, in a manner, giving rise to troublesome investment environment and to incapability in meeting socio-economic demands in time, especially at present, when the Vietnam's economy is integrating itself into regional and global economies and facing fiercer competition in attracting FDI; (ii) At the macro level, the master plan is being worked out too slowly and is believed to be quite poor in quality. Forecasts, especially market forecasts, are unreliable, leaving some enterprises in great difficulty since their output far exceeds demand; (iii) The system of laws and policies is changeable and disconcerted, which does not allow foreign investors to plan effectively. More seriously, the authorities at various echelons do not enforce the laws strictly. While administrative procedures are troublesome, corruption has grown and

46 Besides the causes mentioned above, another reason explaining the decline of FDI in Vietnam since 1997 was the 1997-98 Asian financial crisis, when many Asian economies that had been key investors in Vietnam fell into crisis, and could not longer invest in Vietnam as they might have before.
has not been effectively checked, with government policies unevenly implemented; (iv) Although agriculture, forestry, fisheries and rural areas are defined as priority fields for FDI, due to poor infrastructure and lack of appropriate or concerted policies, long-term relationships based on reciprocity and contracts between foreign investors and farmers have not been ensured. As a result, the foreign investment projects in these fields are few in number and hardly successful; (v) Vietnamese cadres, especially managers, whose role is decisive in implementing state policy and protecting Vietnamese interests in investment partnerships with foreign investor, are not qualified enough. A large number of cadres lack professional expertise: some fail to well understand the law and the market, others are handicapped in terms of command of foreign languages. In addition, some cells of the CPV and trade unions in foreign invested enterprises are incapable of performing their role effectively; (vi) Expenses for site clearance, the costs of electricity, transport, communications and so on are too high compared with other countries in the region. This has reduced Vietnam’s advantages in attracting FDI.

Consequently, in order to make Vietnam as attractive to foreign investors as in the 1990-1997 period, when FDI contributed considerably to Vietnam’s socio-economic development, Vietnam has to amend and supplement a number of articles of the 1996 Law on FDI in compliance with the new international economic circumstances. On 16 May 2000, the National Assembly of Vietnam approved changes to the 1996 Law on FDI favouring further liberalization, which are either supplements to existing provisions or additional provisions that have created a relatively favorable investment environment,

\footnote{In fact, amendments and supplements to a number of articles of the 1996 Law on FDI have been under consideration since 1998 when the Asian financial crisis occurred.}
giving more concessions and a more convenient regulatory framework for foreign investors in Vietnam.

The amendments in May 2000 became effective on 1 July 2000, covering the following main areas, namely: (i) making it easier for foreign investors to change their forms of investment by dividing, separating and merging during investment license period; (ii) further diversifying forms of investment and allowing ownership changes to joint-venture capital; (iii) permitting foreign investors to purchase foreign currencies necessary for their “current transactions” and other permitted transactions from Vietnamese banks, and opening bank accounts at banks outside Vietnam to service foreign loans with the State Bank of Vietnam’s approval; (iv) allowing foreign investors to mortgage land-use rights to get loans from Vietnamese banks and foreign bank branches operating in Vietnam; (v) asserting the responsibility of the Vietnamese side for site clearance, compensation for occupants and issue of land use right certificates to joint-venture companies, where the Vietnamese side contributes capital in the form of capitalized rental for land; (vi) providing certain types of relief for foreign investment projects if any changes to Vietnamese legislation have negative effects on project rights; (vii) reducing the three rates of profit remittance tax of 5%, 7% and 10% to 3%, 5% and 7% respectively; (viii) exempting import materials and spare parts for foreign investment projects in priority area or sector from duties for the first five years of production and so on (see more in http://www.mofa.gov.vn, 10 June 2000).

Although these amendments were not as comprehensive as had been hoped for by foreign investors, they are positive signs, demonstrating some initiative on the part of Vietnam’s government. It is now up to the government and the concerned ministries to quickly issue clear regulations to implement these changes.
With these two amendments to the FDI law to attract US$12 billion in fresh foreign investment and US$11 billion in realized capital of licensed FDI projects for the period 2001-2005 FDI sector (excluding oil and gas) is expected to contribute to 15% of the GDP, 25% of exports, and 10% of state revenue in 2005. The government has done many things to attract foreign investment, namely:

(i) the government allows potential foreign investors to contribute or buy shares from private firms, limited liability companies and share-holding companies. They are also allowed to acquire up to 30% of the equity capital of many equitized SOEs, but must get government approval. Foreign investors are expected to operate in a wide range of business areas, except national security as well as prohibited and conditional sectors. And may be, in the near future, foreign invested enterprises (FIEs) may be allowed to become joint stock companies, with FIEs listed on the stock exchange after going public.

(ii) the government is revising the legal framework to further improve the investment environment, cutting prices of goods and services to help foreign investors reduce costs and improve competitiveness, and developing appropriate human resources to meet the demands of foreign investors. The government has also agreed to replace the dual pricing system by a single price policy for both local and foreign investors.

(iii) the land law has been amended in a more liberal spirit and the law on personal income tax has been modified to motivate foreign investors to employ local labor and to Vietnameseize their management. According to the General Department of Land

48 The FDI sector made up 12% of GDP and 22% of exports in 2001 (Saigon Times Weekly, 8 September 2001) (see in Table 5.9).

49 The MPI has drafted the rules on FIE equitization which deals with issues such as capital transfer between shareholders, capital mobilization for expansion or new projects, FIE participation in the stock exchange and so on.
Administration, land-use rights certificates will be granted to FIEs in industrial zones and export-processing zones. Individuals are not allowed to lease land to foreign investors.

(iv) the administrative reform to simplify complicated procedures and reduce harassment by government officers has continued, thereby helping save time for investors, which is always associated with export opportunities. If a project can develop rapidly, the investor may have opportunities to win export contracts.

(v) the efforts of Vietnam’s government to ratify the Vietnam-US trade agreement seems to have produced new conditions to attract both local and foreign investors.

(v) in recent years, the concerned ministries and local agencies have paid closer attention to coping with difficulties to look for more favorable conditions for business operations. Tax and customs agencies have had talks with businesses, through which disagreements between businesses and related agencies are narrowing. Mutual understanding also paves the way for easy application of new government regulations. Apart from common incentives, local authorities have managed to have their own incentives for investors.

Apart from the law on foreign direct investment, in order to stimulate FDI inflows, in April 1997, the government promulgated the Regulation on Industrial Zones (ID), Export Processing Zones (EPZ) and High-Tech Zones (HTZ)\(^{30}\) that sees the IDZs, EPZs and HTZs as centralized zones specializing in the production for export and domestic use and hi-tech goods, and offering services for productions. This created the basis for attractive incentives made available to export oriented FDI in manufacturing and supporting services and industries. The government also tried to bring better facilities to IDZs, EPZs, and HTZs. So far, there are 66 EPZs and IDZs that have been granted

\(^{30}\) This Regulation replaced the Regulation on Export Processing Zones issued in October 1991.
operating licenses\textsuperscript{51}. Among them, Binh Duong IDZ and Tan Thuan EPZ are very successful.

The Tan Thuan EPZ of 300-hectares located in the suburb of Ho Chi Minh City has attracted 152 FIEs, with total investment commitments of more than US$650 million. Up to the end of 2001, 103 enterprises are in operation, employing more than 30,000 local workers; 68 of them have increased their investment capital by US$221 million and have leased an extra 29.12 hectares of land to expand production. Figures show that 72\% of the Tan Thuan EPZ’s lettable land is now occupied, double the average of other EPZs and IDZs in the country. Exports from this EPZ over the past decade have amounted to nearly US$1.91 billion, representing 16\% of total exports from Vietnam’s foreign invested sector, with average annual export growth of 30\%. In fact, state treatment towards EPZ enterprises has been almost the same as towards outside FIEs (\textit{Saigon Times Weekly}, 6 October 2001).

In addition, the opening of the stock exchange\textsuperscript{52} in Ho Chi Minh City in July 2000 marked another important step towards mobilizing both local and foreign capital

resources. After a year of operation, there were various kinds of securities listed in the stock exchange: (i) six companies’ shares, namely REE, SACOM, HAPACO, TRANSIMEX, LAFOOCO, SAIGON HOTEL with a total value of VND388 billion (US$26 million); (ii) three types of government bonds, which have five year payment terms and interest rates of 6.5% and 6.6% per year, worth VND1,100 billion (US$75 million); (iii) two types of five year term bonds of Development and Investment Banks worth VND158 billion (US$11 million) with an interest rate of 6.5% per year. Up to date, there are now 17 types of stocks, with combined market value of VND2,700 billion (about US$193 million) (Business Times of Malaysia, 4 July 2002). Vietnam’s fledgling stock exchange\(^{33}\) aims to double its list of traded companies at the end of 2003 as it tries to boost institutional investment by offering greater choice, which is expected to help offset speculative buying by individuals. That may reduce risks attached to stocks in Vietnam as China did a decade ago.

In the stock exchange, there are nine licensed brokerages, seven of which have permits to trade stocks on their on account as well as for clients, three foreign bank branches conducting security custodial activity, 1 designated bank doing payment and 6 audit companies\(^{34}\) which audit companies in stock exchange. Foreign auditing companies

\(^{32}\) In order to better manage and monitor all transactions in the stock exchange, Market Regulation Terminal (MR Term) and Direct Connect Terminal (DC Term) have been used. The government promulgated Decision No 139/1999/QD-TTg in June 1999 on participation ratios of foreign parties in the stock exchange.

\(^{33}\) Vietnamese institutional investors understand the stock exchange more than before, but they still don’t have enough knowledge. There are 12,000 institutional investors, more than 90% of whom are individuals. Apart from that a handful of foreign investors have also bought shares.

\(^{34}\) They are the Vietnam Auditing Company (VAC), Auditing and Informatics Service Company (AISC),
cannot engage in such services because under current regulations, they are not allowed to audit Vietnamese companies. The State Security Committee has petitioned to allow foreign auditing companies to audit securities issuers and traders.

To further improve the investment climate and foster cooperation, during the 1990s, Vietnam concluded 39 bilateral investment agreements, which provided additional guarantees for foreign investments and 26 agreements for avoidance of double taxation on income and capital.

With all the efforts of Vietnam’s government for the attraction of FDI into the country, FDI inflow into Vietnam has recovered since 1997, when the Asian financial crisis occurred. Realized capital rose from US$1,900 million in 1998 to US$2,228 million in 2000. Exports from the foreign invested sector increased from US$2,000 million in 1998 to US$3,320 million in 2000. Many other FDI indicators have gone up (see Table 5.9, 8.22, 8.23, 8.24 and sections 5.3.3.1 and 8.2.3.5). Foreign investors are interested in manufacturing industries, construction, agro-processing, fisheries, animal feed production and so on, which is good for Vietnam’s industrialization.

6.2.2 Vietnam’s Foreign Trade Policies

6.2.2.1 Schedules for Tariff Reduction and Non-Tariff Barrier Elimination

One of the most important components of the second phase of the renovation policy has been reform in the foreign trade area. In essence, the most significant reforms in Vietnam’s trade policy have been implemented since joining ASEAN (July 1995) and
hence AFTA (see Appendix 1). Since then, Vietnam has been committed to trade liberalization together with other ASEAN countries. This has also been a common stance taken by member countries of APEC, of which Vietnam has been a member since 1998, as well as of the WTO that Vietnam is seeking accession to. Moreover, this stance is a requirement of the IMF, WB and other members of the international consultative group providing Vietnam with ODA.

After joining ASEAN in August 1995, the Vietnamese Prime Minister instructed the Ministry of Finance set up a study group on Vietnam joining AFTA. Acting upon its commitments, at the conference of the AFTA Council on 10 December 1995, Vietnam announced the list of items for which tariffs would be cut during for the whole 1996-2006. Under the CEPT, Vietnam is to extend, on a reciprocal basis, most favored nation and national treatment to ASEAN member countries, and to maintain a transparent trade regime. For two years 1996-1997, according to Decree No 91/CP dated 18 December 1995 and Decree No 82/CP issued on 13 December 1996, Vietnam offered 1,496 tariff lines (products) of over six thousand tariff lines for tariff concessions. Of these tariff lines, 57% had tariffs between 0-5%, 21% had tariffs between 5-20%, while the rest had tariffs of more than 20%. In 1998, in compliance with Decree No 15/1998-ND on 12 March 1998, Vietnam offered 1,619 tariff lines for tariff concessions. In the 1999-2001 period, more 1,118 tariff lines were offered on the Inclusion List (IL) of the AFTA CEPT.

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55 In 1999, the government schedule for tariff cuts for the 1996-2006 period made in 1995 became obsolete when Harmonization System 96 was introduced, with changes in import-export duties and goods classification. At the beginning, the list of tariff lines was expressed in the six digit system. Then, this list would be translated into the eight digit system established by concerned institutions. The move has made it difficult for producers to adjust their plans to fully benefit from AFTA (Saigon Times Weekly, July 29, 2000).
Scheme for tariff concessions. Therefore, up to 2001, according to the CEPT scheme, Vietnam had offered 4,233 tariff lines on the IL for tariff concessions. Apart from that, in 2001, Vietnam had 196 tariff lines and 51 tariff lines on General Exclusion List (GEL) and Sensitive List (SL) respectively (ASEAN Secretariat, 2001; Decree No 15/1998-ND; Decree No 82/CP; Decree No 91/CP).

According to the CEPT agreement, Vietnam must include 6,130 tariff lines on the CEPT scheme by 2003, representing 95% of Vietnam's tariff lines. About 1,767 tariff lines of the Temporary Exclusion List (TEL) will be transferred onto the IL of the CEPT between 2001 and 2003. Only 5% of all tariff lines will remain on the list of sensitive unprocessed agricultural products, but like other ASEAN member countries, Vietnam will have to phase in these sensitive products by 1 January 2010; even a number of exceptional tariff lines will enjoy cuts by 2018. Vietnam will cut tariff rates on all these products to 5% no later than 2006\(^{56}\), and on nearly all commodities to 0% by 2015. Up to now, Vietnam has realized more than half its CEPT commitments. At present, 50% of the 6,130 tariff lines under the CEPT scheme enjoy tariff rates of less than 5%, while another 21% enjoy tariff rates of less than 20%; the rest still enjoy rates of up to 100% to protect domestic production\(^{57}\). As a result, tariff cuts will be carried out drastically in the future,

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\(^{56}\) According to the resolution of the ASEAN economic ministers' meeting in Hanoi in September 2001, tariff cuts between 0% and 5% will be finalized by early 2002 for five of ASEAN's six original signatories, by 2006 for Vietnam, by 2008 for Laos and Myanmar, and by 2010 for Cambodia. By 2003, the average ASEAN tariff rate is expected to be progressively reduced to 2.9% (2.4% for the original six) (MITI, *Malaysia MITI Report*, 2001: 72-75).

\(^{57}\) According to Decision 41/QD-TC dated March 17, 2000, since 1 April 2000, the import tax on 13 groups of commodities will be adjusted as follows: palm oil and element 5%, sodium hydroxide (NaOH) 20%,
creating great pressure on many local enterprises. The tariff cuts for 2001 were effective from 1 January and importers of goods on the list will get refunds for tariff differences (ASEAN Secretariat, 2001; Saigon Economic Times, 20 January 2001; 5 August 2000; 25 March 2000).

Compared with the other ASEAN countries, which have begun implementing the tariff reduction program of the CEPT, the ratio of tariff lines of Vietnam enjoy tariff rates below 5% was 50% at first stage, whereas Indonesia joined the CEPT, only 9% of tariff lines offered tariff rates below 5% for products of exporting countries, Thailand 27%, and the Philippines 32% (MOT, 1996). This could be considered as favorable for Vietnam when it participates in the implementation of tariff reduction as stipulated by the CEPT.

At the same time, there are five major issues regarding Vietnam’s implementation of the CEPT, which could have an adverse impact on the economy by 2006 if not dealt with in a timely fashion. First, Vietnam’s import tariff indices are not in conformity with international norms. Until 1 January 1996, Vietnam had applied one kind of import duty with a rather high rate, compared to other countries since import duty included the VAT fertilizers 5% (except for super-phosphate 10%), DOP 10%, plastic fiber bags 40%, plastic sheet 10% (plastic film 5%), uncoated kraft paper and cardboard 30%, garments made of vulcanized rubber 20%, knitted or crocheted garments 50% (except those for special use 5%), tiles 50%, household glassware 50% (semi-finished products 30%), pig iron pipes and conduits 20%, machinery for farm, forestry, and animal feed processing 15%, cables 5-15%, vehicles of 5-10 tons, cars and vans of under 50 seats 100%, trucks of over 10 tons 10-20%, and bicycles 80% (racing bicycles 5%). This decision aims at restricting the import of goods, which can be locally produced and encouraging the import of materials and goods which local production cannot supply (Saigon Times Weekly, March 25, 2000). In January 2001, the MOF announced a tariff cutting program under the CEPT scheme, according to which all commodities that carry import tariffs of above 20% would have enjoyed lower import duties since 2001 (Saigon Times Weekly, January 20, 2001; March 3, 2001).
tax (previously sales tax) as well as excise tax and import tariffs. As a result, when Vietnam reduced import duties before separating these two kinds of taxes, meaning partly reducing both excise tax and VAT. To satisfy CEPT requirements in terms of import tariff cuts, Vietnam has separated import tariffs from excise taxes and VAT.

Second, under the CEPT scheme, tariffs must be reduced to 20% after five years and by 5% in each subsequent year to reach 0-5% by 2006. However, the number of tariff lines with rates of over 20% remains large. In the list of tariff cuts on 4,233 tariff lines announced in 2000, there were 295 lines in this tariff category, accounting for 7%. Of these, many have tariffs as high as 25%, 30%, 40% and even 100% (Saigon Times Weekly, 25 March 2000; 29 July 2000; 5 August 2000). This means that between 2000 and 2006, Vietnam must reduce tariffs drastically or apply a one time cut to 0-5% by the final year. This will present difficulties for businesses and negative impacts on the economy.

Third, Vietnam has entered the seventh year (1996-2002) of CEPT implementation, but it has yet to work out a specific road map for tariff cuts for the entire period 1996-2006 as required by the scheme. As a consequence, enterprises are at a loss in formulating and adjusting plans for production and investment, in line with tariff requirements over the last three years58. In 1997, the Government announced a schedule for tariff cuts in 2006 but it only serves as a guideline and reference. The schedule has

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58 According to the MOT, Vietnam’s exports to ASEAN with form D (a certificate of origin to be eligible for CEPT with low tariffs) make up only 0.07-0.08% of its exports to ASEAN, while the corresponding share for other ASEAN members is more than 14 times at around 1%. Given that 20% of Vietnam’s exports and 28% of imports are with ASEAN countries, Vietnamese enterprises have lost considerable advantage in intra-regional trade.
become obsolete since the new export-import tariff list was applied in January 1999, when more tariff lines were introduced and rates were adjusted substantially.

Fourth, Vietnam's tariff rates are imposed on imported commodities regardless of origins. The tariff rates completely ignore the distinction between preferential rates and common or temporary rates, although there exist provisions in Vietnam's law on export-import tariffs, which stipulate various preferential tariff rates within international agreements. In response to the requirements set up by AFTA and those of Vietnam's tax reform program, according to the Ministry of Finance (MOF), Vietnam should split the export-import tariff rates into three categories, involving common, most favored nation (MFN)\(^{59}\), and preferential rates for specific regions and countries that have agreement with Vietnam (e.g. CEPT/AFTA). This process was carried out following the National Assembly's promulgation of the VAT law\(^{60}\) and other tax law in the second tax laws reform program in 1997 (see Chapter 8).

The final issue involves the road map for eliminating non-tariff barriers. Under the CEPT scheme, after six years of implementing tariff cuts to 20\%, non-tariff barriers - such as customs surcharge and customs duty imposition - and quantitative restrictions - like import bans, quotas, import licenses and so on - must be phased out and eliminated

\(^{59}\) The Ministry of Trade (MOT) has proposed maintaining temporarily the current tariff rates as the MFN rates. Goods from other countries, yet to be offered MFN by Vietnam, will be levied with the common rates much higher than the MFN rates. The MOT views this is a urgent matter to be discussed with the MOF to reset Vietnam's export-import tariff rates.

\(^{60}\) Current VAT rates are 0\%, 5\%, 10\% and 20\%, but MOF is planning to further reduce VAT: there will be two-tiered rates in 2005 of either 5\% and 10\% or 8\% and 10\%. Higher VAT and excise taxes will mainly apply to imported goods (see sections 8.2.1.3 and 8.2.3.4).
by 2006. The Ministry of Trade has been assigned as the coordinating body responsible for working out trade policy on NTB implementation within AFTA. Since 1996, the Vietnamese government has agreed to announce NTB policies as required by ASEAN. However, so far, Vietnam has yet to complete a road map for NTB removal. In 2000, Vietnam proposed a draft schedule to lift import licenses for certain groups of commodities (see Table 6.5). Vietnam’s NTBs involve the following:

<table>
<thead>
<tr>
<th>No</th>
<th>Commodity Group</th>
<th>With AFTA</th>
<th>With Miyazawa Fund</th>
<th>With U.S.</th>
<th>With IMF</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Vegetable oil</td>
<td>2003</td>
<td>2003</td>
<td>2005</td>
<td>2003</td>
</tr>
<tr>
<td>2</td>
<td>Liquor</td>
<td>NC</td>
<td>2005</td>
<td>2006</td>
<td>After 2003</td>
</tr>
<tr>
<td>3</td>
<td>Cement</td>
<td>2002</td>
<td>2007</td>
<td>2007</td>
<td>2002</td>
</tr>
<tr>
<td>7</td>
<td>Tile</td>
<td>2003</td>
<td>2003</td>
<td>2004</td>
<td>2003</td>
</tr>
<tr>
<td>8</td>
<td>Construction glass</td>
<td>2002-03</td>
<td>2004</td>
<td>2007</td>
<td>2002-03</td>
</tr>
<tr>
<td>9</td>
<td>Steel</td>
<td>2001-02</td>
<td>2007</td>
<td>2007</td>
<td>2001-02</td>
</tr>
<tr>
<td>10</td>
<td>Cars</td>
<td>NC</td>
<td>2005</td>
<td>2006</td>
<td>After 2003</td>
</tr>
<tr>
<td>11</td>
<td>Motorcycles</td>
<td>NC</td>
<td>2005</td>
<td>2006</td>
<td>After 2003</td>
</tr>
<tr>
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<td>Petrol and oil</td>
<td>NC</td>
<td>2007</td>
<td>2008</td>
<td>After 2003</td>
</tr>
<tr>
<td>13</td>
<td>Sugar</td>
<td>2013</td>
<td>2010</td>
<td>2011</td>
<td>After 2003</td>
</tr>
<tr>
<td>14</td>
<td>Livestock egg</td>
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<td>NYC</td>
<td>IA</td>
<td>NYC</td>
</tr>
<tr>
<td>15</td>
<td>Rice</td>
<td>NYC</td>
<td>NYC</td>
<td>IA</td>
<td>NYC</td>
</tr>
</tbody>
</table>

Sources: Saigon Times Weekly, 22 December 2000; 22 September 2001
Note: - NC: No commitment; NYC: Not yet committed; IA: Immediate abolishment.
- The roadmap in the IMF column is expected for forthcoming negotiations based on the principle of “applying the AFTA roadmap to all countries”

61 With Decision 46/QD-CP dated 4 April 2001, tariff barriers - rather than licenses (NTB) - will serve as a tool to oversee import-export activities in line with AFTA, APEC and WTO requirements, further cutting the number of items whose imports require licenses to be implemented.
First, the export-import license system: (i) only enterprises, which have satisfied certain conditions stipulated by MOT\textsuperscript{62}, would obtain import-export licenses from MOT, and be entitled to import and export commodities; (ii) the licenses permitting imports and exports issued by the MOT must be obtained for a number of commodities such as those requiring export and import goods by quota, consumption goods approved by the Prime Minister, machinery and equipment imported with fund from the state budget, goods for trade fairs and exhibition, goods for foreign enterprises set up by FDI law, and so on. Decree No 89/CP does not clearly stipulate the procedure for requesting and issuing licenses for the above mentioned commodities, nor does it provide any deadline for government agencies to approve license applications; (iii) the licenses to export and import certain commodities requiring to verification by specialized management agencies such as the Ministry of Health, Ministry of Science, Technology and Environment and so on.

Second, quantitative restriction measures: (i) import quotas are proposed by different ministries and branches to the Prime Minister for approval, and then distributed by the MOT. Importers of goods subject to quotas must apply for import permits. Accordingly, the government will specify the maximum quotas enjoying low import taxes, and if these are violated, a higher tax will be imposed. Enterprises are allowed to import consumption goods valued at 20% of the enterprise’s export earnings. The quotas will be decreased 5-10% annually in line with WTO principles for gradual market

\textsuperscript{62} The conditions for getting import-export licenses include: having the legal entity, i.e. enterprise established under company law and the law on enterprises; having registered operating capital of at least US$200,000; exporting and importing in accordance with the lists of goods permitted by licenses.
opening; (ii) according to great balancing (for essential commodities), approved by the government on the basis of demand for and supply of ministries and agencies, the MOT issues import permits. The commodities controlled by great balancing include fertilizers, steel and iron, automobiles, motorcycles, and sugar.

Third, technical measures: specialized management mechanisms require that imported goods be consulted by specialized national agencies for quality and standards; quality tests require certain imported and exported goods to be tested for quality; sanitary and phyto-sanitary measures are applied for importing animals and plants.

Fourth, administrative measures: (i) the right to export and import commodities is given to certain enterprises satisfying a number of MOT requirements; (ii) authorized import contacts, often specialized GCs 90/91, are applied to goods falling into the category of great balancing; (iii) pre-shipment inspection is applied to a lot of Vietnam’s exports such as crude oil, rice, rubber, tea, ground nuts, coal, textiles and garments in terms of size, quality, quantity and price⁶¹; (iv) unit pricing tax⁶⁴ requires importers to pay surcharge and supplementary taxes according to minimum import prices of goods per unit

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⁶¹ According to Circular 37/2001/TTLB/BKHCNMT-TCHQ, the goods, which are exempted from quality inspection, include personal luggage, diplomat’s goods, sample goods, goods for exhibitions and fairs, gifts and goods exchanged in resident areas.

⁶⁴ This measure now applies in many countries, including pro-free trade economies like the US and Singapore. This tax is highly applicable to border trade, where import prices are too low to calculate tariffs on the basis of percentage. Its application can also help do away with the practice of imposing tariffs based on minimum taxable import prices (set by the government) while effectively controlling trade fraud, such as the falsification of taxable import prices. This measure will apply to agro-products and a number of industrial goods that can be imported into the country at low prices.
- such as US$2 per liter and US$1 per kg - determined by MOF. This unit pricing taxes are subject to a certain period and average CIF prices at the import border point.

Fifth, anti-dumping and countervailing duties are two kinds of taxes which have been added to trade laws. However, they have not been yet brought into force due to the lack of a clear definition of dumping and subsidy. The MOT is drafting a government decree on the two taxes; the anti-price transfer duty is now being drafted by the MOT; and the environment protection fee has been proposed for application at borders to pave the way for abolishment of the ban on imports of second hand goods. This measure will be of help as the unit pricing tax cannot be increased to very high levels (The MOT, 1997; MOT, 2000; Saigon Times Weekly, 12 May 2001).

Moreover, by joining AFTA, Vietnam is inevitably expected to participate in another important aspect of ASEAN, which is the agreement on ASEAN customs, involving the following:

(a) Harmonized ASEAN tariff nomenclature is applied to consolidate national tariff lines. Vietnam’s import-export tariff nomenclature is based on the harmonization system (HS) of the Council for Customs Cooperation, but only at the 6-digit level, and the list of import-export commodities is the 8-digit HS promulgated by GSO.

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65 The ASEAN Agreement on Customs Cooperation was signed on 1 March 1997 at the ASEAN Finance Ministers Meeting in Phuket, Thailand. The main objective of the agreement is to facilitate the simplification and harmonization of customs valuation, tariff nomenclature, and customs procedures, which aims to ensure consistency, transparency, and fair administration of customs laws and regulations.

66 Vietnam’s nomenclatures of 6-digit and 8-digit HS create favorable conditions for the Vietnam’s customs together with other ASEAN members’ customs to work out the ASEAN tariff nomenclature. On the other hand, Vietnam faces many difficulties integrating into the ASEAN tariff nomenclature since there
(b) ASEAN customs valuation system, which is consistent with GATT/WTO, applies in all ASEAN member countries, including Vietnam. Yet, since Vietnam has yet to become a member of the WTO and has only recently become an ASEAN member, the other ASEAN member countries agreed to allow Vietnam to apply WTO customs valuation from 2001. In January 2001, the General Department of Customs (GDC) announced Vietnam would shift to a new customs duty system, according to which imports would be taxed on contract prices determined by the customs valuation method of GATT/WTO67 (The Saigon Times Weekly, 6 January 2001).

(c) Publication of guidebooks on customs procedures is considered a measure to promote inter-ASEAN trade. As a result, the customs agencies of ASEAN member countries have agreed to publish the guidebook on customs procedures in each ASEAN country, which contains a great number of customs procedures, policies for import-export trade, commodities, taxes and so on. In preparation for the publication of this guidebook, Vietnamese customs has made great efforts to meet almost the requirements. Yet, due to Vietnam’s policies being in renovation, there may be published issues, but soon become outdated68.

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are big differences between Vietnam and other ASEAN member countries, which require Vietnam to adjust its tariff nomenclature. This requires coordination among various ministries, branches and enterprises, but not only among the General Department of Taxes, General Department of Customs and General Statistical Office.

67 According to the agreement on customs valuation of GATT/WTO, contract prices should be the first and most important basis for calculating import tariffs.

68 On 31 October 2000, Vietnam’s General Department of Customs (GDC) issued Circular 06/2000/TT-TCHQ, which took effect immediately, providing guidelines on customs procedures for imports and exports by foreign invested enterprises (FIEs).
(d) *The green lane* has been established in all ASEAN member countries to promote expeditious clearance of CEPT products. Further improvements are being made for the benefit of exporters, especially small and medium enterprises. Vietnam has also announced its green lane, favoring CEPT products, using a specific mark to distinguish them from other commodities, reserving special reception tables to clear CEPT products and ASEAN passengers at international airports. The GDC has also instructed Vietnamese customs to provide a green lane for CEPT products.

(e) *Common custom clearance forms* have been studied for common application in all ASEAN countries. Due to the differences in tariff nomenclatures, the application of common customs clearance forms in Vietnam can only be implemented after conversion to the 8-digit tariff HS. In addition, this is a rather difficult problem for Vietnam, since the forms to be applied are suitable for modern management methods rather than the manual methods existing in Vietnam.

(g) *Priority areas of customs procedures* include: procedures prior to submitting customs forms; procedures on imported goods for domestic consumption; procedures on customs inspection; procedures on transit; procedures on free zone. With regard to Vietnam, procedures on transit and free zones are still under study, and there are no specific regulations. In respect of other issues, there are some regulations, but they are not systematic, sufficient or uniform\(^69\).

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\(^69\) At present, Vietnam’s customs are preparing to participate in the Kyoto Convention on customs procedures, which facilitate implementation of ASEAN priority area of customs procedures. In addition, Vietnam introduced Customs Law, effective from 1 January 2002. Accordingly, customs procedures have been reduced from 17 steps to 5 steps; entrepreneurs have to contact only one customs officer to proceed with customs clearance, instead of four customs officers before; commodities listed for inspection have considerably reduced (Customs Law, 2001; *Saigon Times Weekly*, 27 October, 2001).
Apart from the agreement on customs cooperation, like other ASEAN countries, Vietnam has taken part in the ASEAN Industrial Cooperation Agreement (AICO)\textsuperscript{70}. Vietnam has drafted and promulgated documents guiding entrepreneurs to participate in the AICO program, and has set up regulations and criteria for enterprises and their products to be given concessions under the AICO program. Owing to the nature of AICO, being an earlier step of CEPT for industrial products, there should be a uniform policy for export-import trade and industrial protection. As a result, the Vietnamese government has asked for close coordination among various ministries: the Ministry of Industries is responsible for considering to the issue of licenses to take part in AICO; the MOF is in charge of determining concessional tariff rates; the MOT handles NTBs and verification of goods' origins.

In addition, Vietnam has also taken part in ASEAN agreements on services, related to numerous issues, including market access, national treatment and other sensitive issues\textsuperscript{71}. The Vietnamese government has approved and permitted the MPI to announce to ASEAN a number of legal documents on service areas. The government has also designated the ministries concerned to deal with various services as follows: MOF and the central bank for financial services; Ministry of Transport and Communication for maritime transport services; The General Department for Posts and Telecommunication is for telecommunication services; The General Department for Tourism is for tourism.

\textsuperscript{70} AICO was established in 1996 to strengthen cooperation in industrial production among ASEAN countries, attract FDI into ASEAN, and implement technological transfers. In fact, the AICO is an industrial tariff reduction program proceeding the CEPT scheme.

\textsuperscript{71} The ASEAN countries have negotiated service cooperation in line with GATT/WTO negotiations. The first service areas discussed have been tourism, aviation, shipping, finance, construction, telecommunication and business.
services; The General Department for Civil Aviation is for aviation service; The MPI is in charge of other services, namely business, professional, computer and related, research and development, real estate, rental/leasing. MPI has also been assigned to supervise and encourage the ministries concerned to actively work regional integration roadmap and to negotiate with their ASEAN counterparts.

Since joining ASEAN, in practice, Vietnam has only compiled documents by the central agencies and organized short training courses, while legal stipulations as well as investment and business activities have not been touched upon. Half of Vietnam’s 6,130 tariff lines under the CEPT scheme, which have been reduced to the tariff rate of less than 5%, are not locally made or not subject to import tariffs of more or less 5%. The products in temporary exclusion list (TEL) do not yet take into consideration to transfer them into IL. In respect of NTBs, Vietnam has succeeded in reducing some administrative procedures, which are no longer applicable to imports, exports and customs. However, an active roadmap has not been made because (i) many administrative formalities remain troublesome; (ii) trade protectionist tendencies through administrative measures still persist; (iii) a number of products, whose NTBs have been lifted, are now subject to tariff barriers (Nguyen Mai, 2000).

Though its commitment to APEC (see Appendix 2) are not as strictly tied as those to AFTA, as an APEC member, every year, Vietnam’s government has set forth and carried out an individual action plan (IAP)\(^2\), including major policies with trade

\(^2\) IPAs serve as APEC’s principal tool to promote efforts of individual economies towards achieving APEC’s goals in trade and investment liberalization and facilitation. The IPA sets out each economy’s voluntary and unilateral measures in contributing towards achieving the vision of free and open trade in Asia-Pacific region.
liberalization and progress towards investment liberalization. Vietnam’s IAP contains information on policies and measures in various areas such as tariffs, non-tariff barriers, services, customs, standards, dispute mediation, investments, and government procurement, which are similar to that of AFTA, but schedules for tariff reduction and NTB removal are lagging behind AFTA’s. Vietnam’s average tariffs for APEC products in 2000 were 16% compared with China’s 16.4%.

Vietnam submitted its application for WTO membership in early 1995 (see Appendix 3). Since then, four rounds of talks have been conducted, mainly on policy transparency and on some 1,500 questions by WTO members on Vietnam’s trade policy. The fifth round began in March 2002 (Saigon Times Weekly, 8 December 2001). Vietnam is taking part in 3-phase negotiations, with a protocol attached, on the possibility of joining the WTO: (i) tariff and other measures affecting commodity trade; (ii) market access, domestic investment, and export incentives influencing agricultural products; (iii) commitments on business services in line with GATS. Vietnam also has to sign a procurement agreement at the government level, and has to make certain commitments relating to SOEs.

According to Moore, the biggest hindrance for Vietnam becoming a WTO member is the market access issue posed by WTO members and how Vietnam will respond to the questions. In his opinion, based on the China experiences, working out a definite time frame for Vietnam, will be a tough job (Saigon Times Weekly, 8 December 2001). From the point of view of Vietnam’s MOT, the timing of WTO entry will be one

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73 Vietnam’s IPA can be accessed in the APEC secretariat website: http://www.apecsec.org.sg.

74 On 29 November 2001, Mike Moore, WTO director general visited Vietnam to speed up Vietnam’s admission to the WTO.
factor affecting the drafting of new trade and economic policies. If there is no schedule, the government agencies will not be forced to have a consistent plan for removing tariffs and non-tariff barriers as well as opening up services and investment. If Vietnam is not admitted to WTO by 2005, it will face tough challenges in trade and economic cooperation with other countries, FDI attraction, and discrimination by other countries (MOT, 2001).

According to Deputy PM Nguyen Manh Cam, Vietnam has spent four years clarifying its policies and another four years on negotiations, so more active steps should be taken if the country is to join the WTO by 2005. Since the WTO ministerial meeting has started a new round of negotiations, expected to end by 2004 when new conditions for WTO entry will be set-up. Vietnam should join the WTO by then to avoid having to meet more difficult requirements. At the same time, Vietnam should also try to boost bilateral negotiations with countries to gain their support and to form alliances to object to unfavorable requirements for developing countries’ entry into the WTO (Saigon Times Weekly, 19 May 2001).

Therefore, the Vietnam-US bilateral trade agreement, which was signed and came into force at the end of 2001, has a positive impact on Vietnam’s WTO entry because its commitments are comprehensive and based on WTO principles. The agreement has five major sections, namely:

(i) market access for industrial and agricultural goods. Over time, Vietnam agrees to allow all Vietnamese firms and US persons and firms the right to import and export freely from within its borders for the first time. It has agreed to sharply lower tariffs on the full range of US industrial and agricultural exports, phase out all NTBs, and adhere to WTO standards in applying customs, import licensing, state trading, technical
standards, and sanitary and phyto-sanitary measures.

(iii) intellectual property rights. Vietnam agrees to adopt WTO standards for intellectual property protection within 18 months and take further measures in several other areas such as protection of satellite signals.

(iii) market access for services. Vietnam allows US persons and firms to enter its services market in all service areas, including financial services (both insurance and banking), telecommunications, distribution, audio visual, legislation, accounting, engineering, computer and related activities, market research, construction, education, health and related, and tourism. These commitments are phased-in over time, typically within three to five years.

(iv) investment provisions. Vietnam has agreed to protect US investments from expropriation, eliminate local content and export performance requirements as well as phase out its investment license regime for many sectors.

(v) transparency provision. Vietnam has agreed to adopt a fully transparent regime with respect to each of the above four substantive areas: by issuing draft laws, regulations and other rules, ensuring that advance public notice is given for all such laws and regulations, and that these documents are published and available; by allowing US citizens the right to appeal rulings made with respect to all relevant laws and regulations.

6.2.2.2. New Directions of Export-Import Policy, 2001-2010

With the reforms in foreign trade after 1995 to integrate into the world economy in line with AFTA, APEC and WTO requirements, Vietnam’s foreign trade increased rapidly with annual average growth rate of more than 18%, more than twice GDP. Since 1995,
Vietnam's exports have increased more rapidly than its imports, although not at expected rates (see Chapter 8). Thanks to a combination of import substitution and export-oriented strategies, the trade deficit narrowed considerably from US$3,888 million in 1996 to US$82 million in 1999, and a trade surplus of US$100 million in 2001 (see Table 8.24). In 1999, per capita export turnover was US$150, five times higher than in 1991 (US$30). Export increases gave rise to the establishment of more labor-intensive production establishments in textiles, garments, footwear, aqua-processing and handicrafts. This also contributed to gradual settlement of foreign debt and accumulation of foreign exchange to materials import essential for production. Recently, exports of footwear, electronics, cashew nuts, tea, coffee and rice have increased considerably. Rice exports rank second in the world behind Thailand; cashew nut exports stand third after India and Brazil; coffee exports rank third behind Brazil and Colombia (robusta coffee exports rank first in the world). Vietnamese rice, crude oil, aqua-products, textiles, garments, footwear, coffee, cashew nuts, and pepper have been recognized as meeting international standards.

Increased imports are not supposed to involve consumer goods, but rather to bring in, machinery, equipment and intermediate goods for developing new production, especially exports, and for building new infrastructure.

It is worth noting that the success of foreign trade since 1995 has profited from new regulations and policies issued recently, of which the most prominent was Decree No 57/1998/ND-CP, enacted on 31 July 1998 detailing stipulations for implementing the Law on foreign trade, goods processing and agencies for foreign partners. The key purpose of this decree is to reduce state intervention in business, and to create a convenient and equal legal framework for all enterprises’ import and export activities. The decree has ended the
regulations for import-export licensing, bringing about fundamental changes in the mechanisms for managing imports and exports. The right to do business and the autonomy of enterprises are respected. The mechanism of “requesting-giving” has been minimized. Import-export procedures for almost all goods are done directly at the customs office, where taxes are imposed on these goods. Non-tariff measures are rarely applied, to very few goods. The decree has contributed importantly to the growth of foreign trade since 1998. The number of export enterprises has risen from 2,800 in 1998 to 12,000 in 2000. These enterprises, with their dynamism and sensitivity to new sources of goods and seeking new markets, have greatly contributed to growing exports goods, which hardly used to be exported, such as vegetables, fruits, fine arts products, handicrafts and other goods. This increases demand for goods and creates more job opportunities.

Besides, many of Vietnam’s products cannot be sure of an advantage once the country fully complies with AFTA. ASEAN countries’ industrial competitive advantages are indicated by the RCA (ratio of competitive advantages) expressed in Table 6.6. Five of the nine product items relate to food processing, but none of Vietnam’s electronics and mechanical engineering industries are regarded as having a competitive advantage. Although monopolizing the domestic market, some products such as animal feed, vegetable oil and plastics are not competitive in the region (see Table 6.6). According to the International Trade Committee (TTC) under the WTO, Vietnam’s electronics industry is 15 to 20 years behind Singapore, Malaysia and Thailand in terms of technology. The plastics industry - thought to be very competitive on account of its monopoly in the domestic market - is on the same footing with that of Indonesia and the Philippines, and is inferior to its counterparts of Singapore, Malaysia and Thailand. Vietnam’s vegetable oil industry is way behind its neighbors, where Malaysia has forged ahead, leaving second
place Indonesia far behind. ITC statistics also show that Vietnam currently has the poorest integration capacity. In 2000, other countries in the region posted high export increases to ASEAN markets: while Brunei’s exports rose 70%, Myanmar’s by 66.2% and Thailand’s by 52.5%, Vietnam’s export increased by only 3.8%, since most of Vietnam’s exports are not complementary, but compete with ASEAN’s products with other ASEAN more efficient than Vietnam (Saigon Times Weekly, 29 September 2001).

Table 6.6: Ratio of Competitive Advantage of ASEAN Countries by Product, in 1998

<table>
<thead>
<tr>
<th>No</th>
<th>Product</th>
<th>Indonesia</th>
<th>Malaysia</th>
<th>Philippines</th>
<th>Singapore</th>
<th>Thailand</th>
<th>Vietnam</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Meat/meat processing</td>
<td>0.1</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>1.4</td>
<td>0.1</td>
</tr>
<tr>
<td>2</td>
<td>Dairy products</td>
<td>0.3</td>
<td>0.3</td>
<td>0.0</td>
<td>0.2</td>
<td>0.1</td>
<td>0.8</td>
</tr>
<tr>
<td>3</td>
<td>Aqua-product processing</td>
<td>3.4</td>
<td>0.7</td>
<td>3.7</td>
<td>0.5</td>
<td>8.7</td>
<td>11.3</td>
</tr>
<tr>
<td>4</td>
<td>Food polishing &amp; processing: Of which, rice</td>
<td>0.1</td>
<td>0.2</td>
<td>0.1</td>
<td>0.2</td>
<td>3.3</td>
<td>6.6</td>
</tr>
<tr>
<td>5</td>
<td>Vegetable/fruit processing</td>
<td>0.6</td>
<td>0.3</td>
<td>4.5</td>
<td>0.1</td>
<td>28.7</td>
<td>69.7</td>
</tr>
<tr>
<td>6</td>
<td>Sugar</td>
<td>0.5</td>
<td>0.5</td>
<td>3.3</td>
<td>0.1</td>
<td>7.0</td>
<td>0.8</td>
</tr>
<tr>
<td>7</td>
<td>Animal feed</td>
<td>1.0</td>
<td>0.6</td>
<td>1.3</td>
<td>0.2</td>
<td>1.6</td>
<td>0.1</td>
</tr>
<tr>
<td>8</td>
<td>Drinks</td>
<td>0.0</td>
<td>0.1</td>
<td>0.1</td>
<td>0.3</td>
<td>0.1</td>
<td>0.1</td>
</tr>
<tr>
<td>9</td>
<td>Animal/vegetable fat and oil processing</td>
<td>2.7</td>
<td>16.2</td>
<td>3.6</td>
<td>1.5</td>
<td>0.7</td>
<td>0.0</td>
</tr>
<tr>
<td>10</td>
<td>Rubber and rubber products</td>
<td>0.4</td>
<td>0.8</td>
<td>0.2</td>
<td>0.3</td>
<td>0.9</td>
<td>1.3</td>
</tr>
<tr>
<td></td>
<td>Of which, rubber</td>
<td>12.1</td>
<td>10.8</td>
<td>0.5</td>
<td>1.8</td>
<td>14.2</td>
<td>3.4</td>
</tr>
<tr>
<td>11</td>
<td>Fiber, thread, and fabrics</td>
<td>1.6</td>
<td>0.4</td>
<td>0.4</td>
<td>0.2</td>
<td>1.2</td>
<td>1.8</td>
</tr>
<tr>
<td></td>
<td>Of which, synthetic fibers</td>
<td>0.2</td>
<td>0.3</td>
<td>0.4</td>
<td>0.1</td>
<td>0.7</td>
<td>0.7</td>
</tr>
<tr>
<td></td>
<td>Silk and linen</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.2</td>
<td>0.9</td>
<td>9.2</td>
</tr>
<tr>
<td>12</td>
<td>Insecticides and chemicals for agriculture</td>
<td>0.5</td>
<td>0.3</td>
<td>1.2</td>
<td>0.5</td>
<td>1.4</td>
<td>3.1</td>
</tr>
<tr>
<td>13</td>
<td>Basic chemicals</td>
<td>0.3</td>
<td>0.2</td>
<td>0.2</td>
<td>0.8</td>
<td>0.1</td>
<td>0.0</td>
</tr>
<tr>
<td>14</td>
<td>Paint, ink, varnish, painting products</td>
<td>0.2</td>
<td>0.2</td>
<td>0.0</td>
<td>0.7</td>
<td>0.3</td>
<td>0.0</td>
</tr>
<tr>
<td>15</td>
<td>Medicine</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.3</td>
<td>0.1</td>
<td>0.0</td>
</tr>
<tr>
<td>16</td>
<td>Soap and cleansing products</td>
<td>0.4</td>
<td>0.4</td>
<td>0.2</td>
<td>0.5</td>
<td>0.3</td>
<td>0.3</td>
</tr>
<tr>
<td>17</td>
<td>Fertilizers</td>
<td>1.1</td>
<td>0.4</td>
<td>1.5</td>
<td>0.1</td>
<td>0.0</td>
<td>0.1</td>
</tr>
<tr>
<td>18</td>
<td>Plastics and semi-finished plastics</td>
<td>0.1</td>
<td>0.2</td>
<td>0.1</td>
<td>0.7</td>
<td>0.3</td>
<td>0.1</td>
</tr>
<tr>
<td>19</td>
<td>Non-electric machinery</td>
<td>0.0</td>
<td>0.7</td>
<td>0.5</td>
<td>2.2</td>
<td>1.0</td>
<td>0.1</td>
</tr>
<tr>
<td>20</td>
<td>Electric machinery</td>
<td>0.2</td>
<td>2.9</td>
<td>2.5</td>
<td>2.4</td>
<td>1.3</td>
<td>0.1</td>
</tr>
<tr>
<td>21</td>
<td>Garments</td>
<td>2.1</td>
<td>1.4</td>
<td>4.4</td>
<td>0.5</td>
<td>2.2</td>
<td>3.1</td>
</tr>
<tr>
<td>22</td>
<td>Footwear and leather products</td>
<td>4.6</td>
<td>0.3</td>
<td>1.5</td>
<td>0.1</td>
<td>2.9</td>
<td>4.0</td>
</tr>
</tbody>
</table>

The low RCAs of Vietnam’s industries and its poor integration into the regional economy, mentioned above, are partly due to policies which do not encourage enterprises to renovate technology. With Decree No 57/1998, there was a basis problem that is instability and unpredictability of the mechanism and policies. Besides, the facts show that it is necessary to issue timely stable long-term policies to manage import-export trade, which can foresee possible future difficulties to ensure suitable management measures and to create favorable conditions and dynamics for enterprises. That is why Decree No 57/1998 was replaced by Decree No 44/2001/ND-CP on 2 August 2001 on new regulations to control import-export trade in the 2001-2010 period to stimulate Vietnam’s exports. The prominent points of this new decree are (i) to continue expanding the right to do enterprises’ business; (ii) to build a roadmap to decrease NTB measures; and (iii) to apply legitimate new protective tools in line with the rules of international trade organizations and arrangements. This proves that Vietnam has committed to making drastic changes in trade policy towards liberalizing imports and exports. These commitments might be “out of the woods”, out of the current slow growth situation to move into full market economy and to be ready to compete in the world market if there will be good domestic policies to supplement them. This decree, together with other decrees and government circulars, including competition, most favored nation status, national treatment, safeguards and anti-dumping laws and so on, have met the need to flexibly settle important problems as follows:

First, export promotion: to facilitate Vietnamese goods penetration into international markets, the government allows Vietnamese enterprises, cooperatives and households to export all kinds of goods irrespective of the commodities stated in their licenses, but excluding prohibited goods. The government stipulates only four kinds of
conditional exports, including goods under quotas, MOT licenses, specialized management, and other (separate) regulations. Enterprises are allowed to sell out-sourced products, rent machines, surplus materials, discarded products and scraps under current regulations. Apart from that, foreign invested enterprises (FIEs) and foreign partners in business cooperation contracts are allowed to export other kinds of goods in addition to their own products. According to the 2000 law on FDI, export plan approval is abolished. Hence, FIEs can buy goods for export, and FIEs also enjoy the same interest as Vietnamese businessmen such as can be rewarded for success of export performance, can export goods as local do. At the same time, the government also permits foreign traders and organizations to act as sale agents for Vietnam’s businesses (decree No 44/2001/ND-CP). With this new stipulation, the number of businesses engaged in direct exports increase from 12,000 in 2000 to 16,300 in 2001 (Saigon Times Weekly, 18 August 2001).

According to Decree No 133/2001/QD-CP on the export credit support mechanism and Circular 76/2001/TT-BTC, the government has extended short-term loans on preferential terms to all eligible exporters regardless of whether state or private sectors from the Export Assistance Fund (EAF). Beneficiaries will include entrepreneurs producing goods on the priority list and those penetrating new markets or maintaining relations with traditional markets. The priority list is issued with the government, while the EAF uses the list to consider business credit applications. The loans are equal to 70% of export contract value. If exporters have opened letter of credit (L/C), the ratio is 80% of the L/C value. The maximum lending period is 12 months and annual interest rates are equal to 80% of the rates for medium and long-term loans, i.e. 5.4% (Saigon Times

25 However, FIE import activities still have to be subject to the stipulations of the Law on FDI and follow investment license requirements and other relevant legal documents.
Weekly, 6 October 2001). To help local entrepreneurs improve competitiveness, the government will provide free guarantees for bid participation and contract implementation if requested by foreign partners.

Second, import control: to regulate import activities, apart from tariffs, Vietnam is applying several major NTBs like the import license system, quotas, prohibitions, technical and administrative measures, customs surcharge levies and so on. These tools are to be gradually reduced and then eliminated by implementing AFTA, APEC and Vietnam-US bilateral trade agreement commitments as well as in preparation for joining the WTO. Vietnam has not yet applied NTB measures accepted by AFTA, APEC and WTO and has not been forced to eliminate tariff quotas, absolute tariffs, seasonal tariffs, anti-dumping and countervailing duties, environmental fees and other measures for limiting transfer pricing. They are also measures to meet the need for legitimate protection after quantitative restrictions and licenses are abrogated. Therefore, the basic future orientation of the management mechanism for imports is to gradually cut currently applied NBTs and increase new ones.

Among NTBs, reduction and elimination of import licenses are worth noting. Products imported with MOT permits have decreased. Only 15 items require MOT licenses with all import licenses due to be abolished. For imports managed by specialized agencies, the future direction of management is as follows: (i) to completely abrogate management if not necessary; (ii) to manage by stipulating standards, criteria, and conditions; (iii) in very special cases, maintain the license, but guarantee not to use

\[76\] Only stipulating technical standards, criteria and conditions for imports so that enterprises have instructions for making import procedures at the customs offices of border gates, neither issuing the license nor approving the items, quantity and value.
specialized licenses to limit the quantity of imports or not to require getting permit from the Prime Minister.

Table 6.7: Vietnam: Some Major Export Products, in 2010 (US$ million)

<table>
<thead>
<tr>
<th>No</th>
<th>Export product</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Garments</td>
<td>7,500</td>
</tr>
<tr>
<td>2</td>
<td>Footwear</td>
<td>7,500</td>
</tr>
<tr>
<td>3</td>
<td>Handicrafts</td>
<td>1,500</td>
</tr>
<tr>
<td>4</td>
<td>Electro-mechanical appliances</td>
<td>1,000</td>
</tr>
<tr>
<td>5</td>
<td>Plastics</td>
<td>600</td>
</tr>
<tr>
<td>6</td>
<td>Cosmetics</td>
<td>600</td>
</tr>
<tr>
<td>7</td>
<td>Processed food</td>
<td>700</td>
</tr>
<tr>
<td>8</td>
<td>Hi-tech products</td>
<td>7,000</td>
</tr>
<tr>
<td>9</td>
<td>Agro-products</td>
<td>8,600</td>
</tr>
<tr>
<td>10</td>
<td>Raw materials and fuels</td>
<td>1,750</td>
</tr>
<tr>
<td>11</td>
<td>Service</td>
<td>8,100</td>
</tr>
<tr>
<td>12</td>
<td>Other</td>
<td>13,100</td>
</tr>
</tbody>
</table>


Since new regulations on management of export and import trade would help companies draw up long term - instead of one year (as previously) - the business plans and to prepare for integration into the world economy, Vietnam's foreign trade is expected to grow tremendously in the 2001-2010. According to the plan for foreign trade development during 2001-2010, foreign trade in the next 10 years will help increase the country's GDP. According to economists, Vietnam's export may increase rapidly if the country becomes a member of the WTO and fully participates in the AFTA. Vietnam's animal feed, electronics, electrical appliances, vegetable oil products, pharmaceuticals, cosmetics, beer, fiber and textile, some machine tools and food-processing machinery can be competitive in the regional market by the time the country fully implements AFTA.
Vietnam's exports are expected to increase 15% annually. Exports will be restructured to reach US$58 billion in 2010 with the bulk made up by manufactured goods, hi-tech products and services, and agro-products (see Table 6.7). Commodities will generate a total export value of US$50 billion and services another US$8.1 billion. Then, the country will enjoy a good trade surplus estimated at US$5.5 billion (Saigon Times Weekly, 9 September 2000; 18 August 2001).

Market expansion is one of the main measures for boosting exports. In the Asia-Pacific region, along with Vietnam's major markets - such as the ASEAN countries, Japan, South Korea and Taiwan - the giant market of China will also be exploited. To stimulate two-way trade between Vietnam and China, Vietnam will develop official trading channels, rearrange border trade and negotiate stable barter trade in various products with large quantities. Vietnam continues to accelerate bilateral or multilateral trade with the European Union (EU), strengthen commercial relations with Russian and Eastern European countries, approach the US market (the world's biggest importer with diverse demands), and encourage foreign investors to export to the US market. The Middle East, Near East, Africa and Latin America are also considered potential markets for Vietnamese exports.

For import, Vietnam will play attention to importing modern equipment, machinery and advanced technology. Production of import substituting materials will be gradually developed. Imports of consumer goods that can be produced domestically will be restricted. The government will also carry out commitments to opening the market in line with the AFTA, APEC and WTO regulations, and give equal trading rights to foreign businesses.
6.3 Outcomes of Vietnam’s International Economic Integration Policies

Vietnam’s economic development and industrialization since 1995 have been uneven. Economic reform for Vietnam’s international integration has not always been in line with requirements. In some years, although economic growth has been high, the quality of growth has been bad, and perhaps has not contributed much to socio-economic development. In this section, Vietnam’s macro-economic situation since 1995 is analyzed, especially stabilization and economic growth; economic growth and structural change; export promotion and protection for domestic production.

6.3.1 Stabilization and Economic Growth

After the socio-economic crisis of 1986-89, with successful implementation of a number of policies to curb inflation and release productive forces, Vietnam’s economy gradually stabilized (see Chapter 5). More generally, the economy overcame the crisis in 1995, and created certain conditions for further development (CPV, 1996). GDP growth increased during 1991-95, peaking in 1995, before decreasing. The economy recovered in 2000 and 2001, with GDP growth rates of 6.5% and 6.8% respectively (see Tables 5.6 and 8.24). At the same time, inflation has been curbed (see Table 5.6). The price index was very low in 1999, and deflation occurred in 2000 and 200177 (see Figure 6.1). This mainly resulted from significant reductions in the prices of agricultural products, due to decreasing domestic demand, thereby increasing inventories. Hence, many enterprises have had to

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77 During 1988-94, high inflation, together with economic recession, led to stagnation and serious supply shortages.
reduce production capacities, leading to the retrenchment of many workers. Disposable incomes of workers went down, and aggregate demand continued to decline. Hence, the production capabilities of many industries were very low.

Source: Table 5.6
*Figure 6.1: Vietnam: Economic Growth and Inflation*

The reasons for the economic situation in 1996-2001 are as follows: First, the economic achievements in 1990-95 mainly stemmed from the release of productive forces (constrained during the period of bureaucratic centralism), better mobilization of both domestic and international capital resources in the form of FDI and ODA, and export increases. However, sources of economic development, mainly relying on endogenous capabilities of the economy in previous years, were exhausted. As a result, when the Asian financial crisis occurred in 1997, with small foreign reserves, the Vietnamese
economy, which were subject too much to international savings\(^7\), could not face up to the challenges of the crisis. During 1993-98, FDI accounted for 25%-32% of total gross capital formation\(^8\) (GCF) (Table 6.8).

**Table 6.8: Vietnam: Gross Domestic Capital Formation by Source (%)**

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<tbody>
<tr>
<td>Public investment, of which</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State budget</td>
<td>40.2</td>
<td>38.0</td>
<td>35.1</td>
<td>44.0</td>
<td>38.3</td>
<td>38.3</td>
<td>45.2</td>
<td>48.1</td>
<td>54.0</td>
<td>61.5</td>
<td>59.0</td>
</tr>
<tr>
<td>State credit</td>
<td>24.8</td>
<td>14.3</td>
<td>24.1</td>
<td>27.5</td>
<td>15.3</td>
<td>19.9</td>
<td>20.8</td>
<td>21.2</td>
<td>22.8</td>
<td>25.2</td>
<td>20.3</td>
</tr>
<tr>
<td>SOEs</td>
<td>0.0</td>
<td>8.7</td>
<td>3.8</td>
<td>7.0</td>
<td>8.5</td>
<td>4.5</td>
<td>10.4</td>
<td>13.1</td>
<td>10.5</td>
<td>14.2</td>
<td>20.5</td>
</tr>
<tr>
<td>Private investment, of which</td>
<td></td>
<td></td>
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<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Households</td>
<td>46.7</td>
<td>47.7</td>
<td>43.9</td>
<td>30.8</td>
<td>31.3</td>
<td>29.4</td>
<td>26.2</td>
<td>20.6</td>
<td>21.1</td>
<td>20.2</td>
<td>22.1</td>
</tr>
<tr>
<td>Private enterprises</td>
<td>39.8</td>
<td>35.9</td>
<td>38.2</td>
<td>25.9</td>
<td>25.4</td>
<td>22.6</td>
<td>20.2</td>
<td>19.1</td>
<td>17.0</td>
<td>16.4</td>
<td>17.5</td>
</tr>
<tr>
<td>FDI</td>
<td>7.0</td>
<td>11.9</td>
<td>5.7</td>
<td>4.9</td>
<td>5.9</td>
<td>6.8</td>
<td>6.0</td>
<td>1.5</td>
<td>4.1</td>
<td>3.9</td>
<td>4.6</td>
</tr>
</tbody>
</table>


It is worth adding that of total foreign capital, loan capital accounted for the main part, and was still increasing proportionately. In other words, having flowed into Vietnam’s economy in the last few years, foreign capital was mainly unstable (loans) compared with stable capital (paid-up capital of foreign companies) (Figure 6.2, Table 6.9). New foreign capital declined dramatically in the late 1990s, but recovered in 2000-01, though it could not achieve the level of the 1990s, which would influence economic growth, not only at present, but also in the future.

\(^7\) During 1996-2001, particularly 1996-98, the economic growth of Vietnam was more dependent on international resources, including FDI and ODA. The contribution of the foreign sector to Vietnam’s GDP increased from 6.4% in 1994 to 7.4% in 1996 and 13.3% in 2000 (see Table 5.9).

\(^8\) This ratio was high compared with 22% for Malaysia in 1988 (Jomo, 1998: 76; Ariff, 1991: 75), 7% for Taiwan in 1987 and 2.5% for South Korea in 1975 (Purcell, 1987: 81; Amsden, 1989: 77)
Table 6.9: FDI Actual Capital Structure: Actual Loans and Paid-up Capital (%)

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</thead>
<tbody>
<tr>
<td>Actual paid-up capital</td>
<td>92</td>
<td>91</td>
<td>78</td>
<td>67</td>
<td>63</td>
<td>56</td>
<td>41</td>
<td>27</td>
</tr>
<tr>
<td>Actual loan capital</td>
<td>8</td>
<td>9</td>
<td>22</td>
<td>33</td>
<td>37</td>
<td>44</td>
<td>59</td>
<td>83</td>
</tr>
</tbody>
</table>


Moreover, a significance of Vietnam’s consumption has been covered by foreign savings in the form of relatives’ remittances from abroad, estimated at about US$2.3 billion in 2001 (*Vietnam Investment Review*, 6 September 2002). Thus, it could be said that Vietnam’s economic growth - depending so much on foreign capital (see Section 6.1.1) - was vulnerable and unsustainable, although FDI and relatives’ remittances from overseas can be considered more stable than portfolio investment\(^3\).


Figure 6.2: Vietnam: FDI Capital Structure: Loan and Paid-up Capital

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\(^3\) Suggested by the Mexican and Asian financial crises in 1994 and 1997 respectively.
Second, the growth of the economy has been very subject to government investment, including investment by SOEs, but has been less dependent on the private sector. Public investment - which involves state budget investment, SOE investment, state credit - accounted for 38% in 1991, 45% in 1995 and 61% in 1999, whereas domestic private investment declined dramatically from 47% in 1991 to 20% in 1999 (see Table 6.8), mainly derived from households savings, and not from private enterprises' savings (see Table 6.10). However, thanks to the Law on Enterprises enacted in 2000 (see Section 6.1.1), private investment rose again to 22%, while public investment declined to 59% (Table 6.8). This tendency, which has just started, needs more attention and incentives from the government to increase. With the experience of the last ten years, it appears that when public investment went up, private investment went down because the private sector could not compete with the SOE sector’s advantages in terms of easy access to credit, capital and imported raw materials, assistance for product marketing, simplifying bureaucratic formalities and so on.

**Table 6.10: Vietnam: Investment and Savings, 1990-2000 (% of GDP)**

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</tr>
</thead>
<tbody>
<tr>
<td>Gross domestic capital</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>formation</td>
<td>14.4</td>
<td>15.0</td>
<td>17.7</td>
<td>25.1</td>
<td>25.5</td>
<td>27.3</td>
<td>28.2</td>
<td>27.6</td>
<td>13.6</td>
<td>21.0</td>
<td>24.1</td>
</tr>
<tr>
<td>Domestic savings</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Of which:</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- SOE</td>
<td>2.9</td>
<td>10.1</td>
<td>13.6</td>
<td>14.8</td>
<td>15.0</td>
<td>17.0</td>
<td>19.1</td>
<td>20.1</td>
<td>17.0</td>
<td>18.0</td>
<td>19.5</td>
</tr>
<tr>
<td>- Government</td>
<td>10.3</td>
<td>10.0</td>
<td>9.3</td>
<td>9.5</td>
<td>9.7</td>
<td>9.4</td>
<td>9.9</td>
<td>10.4</td>
<td>11.0</td>
<td>12.9</td>
<td>11.1</td>
</tr>
<tr>
<td>- Private sector</td>
<td>-9.6</td>
<td>-7.0</td>
<td>-4.3</td>
<td>-3.5</td>
<td>-3.2</td>
<td>-3.3</td>
<td>1.1</td>
<td>2.8</td>
<td>-1.4</td>
<td>-2.0</td>
<td>-0.4</td>
</tr>
<tr>
<td>Foreign savings</td>
<td>11.5</td>
<td>4.9</td>
<td>4.1</td>
<td>10.2</td>
<td>10.5</td>
<td>10.3</td>
<td>9.1</td>
<td>7.5</td>
<td>-3.4</td>
<td>3.0</td>
<td>4.6</td>
</tr>
</tbody>
</table>

**Source:** GSO, 2001; Table 5.6

Since the key source of SOE investment has been state credit, the ratio between loan capital and own capital (enterprise savings) has gradually increased. Public finance
declined seriously: government debt increased dramatically to deal with SOE bad debt of over VND199,000.00 billion (US$14.2 billion) and overdue debt from the commercial banking system equal to 14.5% of outstanding debt in 1999. This can give rise to instability and uncertainty in the financial system, if investment has not been efficient enough to service the loans, i.e. to reimburse loan principal and pay interest. Thus, it can be said that unsound investment policy may burden the state budget and exacerbate macroeconomic imbalances.

Third, the economic growth of Vietnam has not been sustainable, as expressed by Vietnam's ICOR and TFP indicators. Its ICOR increased from 2.88 for 1991-95 to 4.45 for 1996-2000, and even rose to 5.4 in 1999 before declining to 5.0 in 2000 (see Section 8.2.3.2). The increase in the ICOR reflected the focus on infrastructure investment and unsound investment mechanisms. The average TFP value for 1996-2000 was 1.7, compared with 1.5 in 1990-91 (Tran Dinh Thien, 2001: 83; Table 5.5).

Maintaining economic growth and stabilization, as measured by the inflation rate, has been the main objective of macro-economic policy. Vietnam, which experienced economic recession with hyperinflation in the late 1980s, recognized its negative impacts on production and economic development. Therefore, up to 1997, Vietnam's macro-economic policy focused on inflation control by constraining aggregate demand. However, since 1997, particularly in 1999, when the retail price index went down to nearly 0%, stimulation of aggregate demand - by which the government hoped to achieve

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81 At this moment, infrastructure investment is necessary, but should be kept efficient and at appropriate levels.

82 In principle, if macro-economic policy pays attention to curbing inflation, it could lead to income reduction and lower economic growth.
economic recovery - has become the key goal of macro-economic policy\textsuperscript{83}. Nonetheless, demand stimuli - like increases in state budget expenditures, loosening credit supply limits, reducing both borrowing and lending interest rates, and so on - did not succeed in stimulating aggregate demand. The Japanese experience shows that demand stimulus measures were not enough to revive and sustain economic growth, but can lead to high inflation and economic instability. As a result, the government should not only use demand stimulus measures, but should also combine demand and supply stimulus measures.

In sum, since 1995, Vietnam's economic growth has achieved high levels, but has not been stable, sustainable and reliable\textsuperscript{84}. The economic situation in recent years has exposed Vietnam's economic instability and other weaknesses. The potential and comparative advantage of the economy has not been well exploited. As a consequence, Vietnam must have a sound investment policy and create a favorable investment environment to get back to high and sustainable economic growth.

\textbf{6.3.2 Economic Growth and Structural Change}

With economic growth, Vietnam's economic structure has also changed. The proportion of agriculture in GDP declined from 27.2\% in 1995 to 23.2\% in 2001, while the share of

\begin{footnotesize}\begin{itemize}
\item Demand stimulation was carried out in Vietnam through investment increases from the state budget for public projects to use up a good part of the steel and iron inventories.
\item Due to the Asian financial crisis, Vietnam's economic growth went down dramatically in 1998. However, thanks to implementation of the law on enterprises, elimination of the export-import licensing system, establishment of the stock exchange in Ho Chi Minh City and some banking and financial reforms, Vietnam's economy has recovered since 2000 (see Chapter 6; Table 8.24).
\end{itemize}\end{footnotesize}
the industrial sector in GDP went up from 28.8% in 1995 to 39.3% in 2001 (see Table 5.8; Tran Dinh Thien, 2001: 87). This change in economic structure reflected Vietnam’s industrialization. Nonetheless, unlike other East Asian economies, the share of Vietnam’s service sector in GDP has not increased (see Table 6.11). On the contrary, the service sector’s share went down from 44% in 1995 to 39% in 2001 (see Table 5.8; Tran Dinh Thien, 2001: 87).

**Table 6.11: Economic Structure of Some East Asian Economies, 1980-1999 (%)**

<table>
<thead>
<tr>
<th>Economy</th>
<th>Agriculture</th>
<th></th>
<th></th>
<th>Industry</th>
<th></th>
<th></th>
<th>Service</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>South Korea</td>
<td>14.9</td>
<td>8.5</td>
<td>5.0</td>
<td>41.3</td>
<td>43.1</td>
<td>43.5</td>
<td>43.7</td>
<td>48.4</td>
<td>51.5</td>
</tr>
<tr>
<td>Taiwan</td>
<td>7.7</td>
<td>4.2</td>
<td>2.6</td>
<td>45.7</td>
<td>41.2</td>
<td>33.1</td>
<td>46.6</td>
<td>54.6</td>
<td>64.3</td>
</tr>
<tr>
<td>China</td>
<td>30.1</td>
<td>27.0</td>
<td>17.3</td>
<td>48.5</td>
<td>41.6</td>
<td>49.7</td>
<td>21.4</td>
<td>31.3</td>
<td>32.9</td>
</tr>
<tr>
<td>Thailand</td>
<td>23.2</td>
<td>12.5</td>
<td>10.4</td>
<td>28.7</td>
<td>37.2</td>
<td>40.1</td>
<td>48.1</td>
<td>50.3</td>
<td>49.6</td>
</tr>
<tr>
<td>Vietnam</td>
<td>39.3</td>
<td>37.8</td>
<td>25.4</td>
<td>19.8</td>
<td>23.9</td>
<td>34.5</td>
<td>40.9</td>
<td>38.3</td>
<td>40.0</td>
</tr>
</tbody>
</table>

**Sources:** GSO, 2001; Table 7.5.

However, the economic structural changes mentioned above have not been significant, and caused the following number of socio-economic issues to be settled:


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</tr>
</thead>
<tbody>
<tr>
<td>Labor force</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
<tr>
<td>Agriculture, Fishery and Forestry</td>
<td>72.6</td>
<td>72.9</td>
<td>73.0</td>
<td>70.0</td>
<td>69.7</td>
<td>69.2</td>
<td>68.7</td>
<td>68.2</td>
<td>67.8</td>
<td>62.6</td>
</tr>
<tr>
<td>Industry and construction</td>
<td>13.9</td>
<td>13.4</td>
<td>13.3</td>
<td>13.2</td>
<td>13.2</td>
<td>12.5</td>
<td>12.5</td>
<td>12.7</td>
<td>12.9</td>
<td>13.2</td>
</tr>
<tr>
<td>Services</td>
<td>13.5</td>
<td>13.7</td>
<td>13.7</td>
<td>16.8</td>
<td>17.1</td>
<td>18.3</td>
<td>18.8</td>
<td>19.1</td>
<td>19.3</td>
<td>24.2</td>
</tr>
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</table>

**Source:** GSO, 2001; Ministry of Labor, Invalids and Social Affairs, 2001
First, the economic structural changes were not proportionate to employment in agriculture, industry, and services, and between urban and rural areas (see Table 6.12). The majority of the population of the country still lives in rural areas and works in agricultural activities (Table 6.13). This suggests that economic growth in Vietnam has been mainly based on capital increments, not on labor productivity gains. Therefore, the few beneficiaries from economic growth and structural change are mainly concentrated in some big cities, while the majority of the population lives in rural areas, particularly in remote and mountainous areas, largely remaining unemployed or underemployed, and hence have not benefited from economic development. As a result, the income gap between rural and urban populations has widened, giving rise to serious social problems such as heroin addiction, crime, family problems and so on. To reduce such problems, the government should pay attention to both economic growth and social equity, enabling all regions and ethnic groups within the country to benefit from economic progress\textsuperscript{85}.

\textsuperscript{85} A more complex question relates to the best strategy for investing limited public investment resources. Given that around 77% of Vietnam's population lives in rural areas, at very low levels of income, what would be the most effective rural development strategy for Vietnam to maximize the positive impacts on the well-being of the Vietnamese people? The choice facing Vietnam ranges between largely investing limited resources in the three urban growth poles (surrounding Ho Chi Minh City, Danang and Hanoi-Haiphong) or a strategy involving more evenly distributed investments across the country. The former approach risks leaving rural areas further behind, combined with the sometimes unmanageable challenges of rapid urbanization faced by a number of major Asian cities. The latter strategy risks dispersing limited investment resources and the loss of economies of scale.

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</thead>
<tbody>
<tr>
<td>Total population</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
<tr>
<td>Urban</td>
<td>19.5</td>
<td>19.7</td>
<td>19.9</td>
<td>20.2</td>
<td>20.6</td>
<td>21.0</td>
<td>21.4</td>
<td>22.7</td>
<td>23.3</td>
<td>23.6</td>
<td>24.0</td>
</tr>
<tr>
<td>Rural</td>
<td>80.5</td>
<td>80.3</td>
<td>80.1</td>
<td>79.8</td>
<td>79.4</td>
<td>79.0</td>
<td>78.6</td>
<td>77.3</td>
<td>76.7</td>
<td>76.4</td>
<td>76.0</td>
</tr>
<tr>
<td>Population growth rate</td>
<td>2.0</td>
<td>1.9</td>
<td>1.9</td>
<td>1.8</td>
<td>1.7</td>
<td>1.6</td>
<td>1.6</td>
<td>1.4</td>
<td>1.4</td>
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</table>

Source: GSO, 2001; Ministry of Labor, Invalids and Social Affairs, 2001

Second, in recent years, the industrial structure has been biased in favor of using more capital, instead of more labor, and producing import substitution commodities for the domestic market. Since 1991, the labor force in the SOE sector has not increased, while employment rises in foreign invested projects have not been consistent with invested capital (see Section 6.1.2.2). According to statistical estimates, owing to the concentration of FDI in petroleum, on average, more than US$40,000 of FDI creates only one job. Thus, it could be said that most public investment and FDI, focused on capital-intensive industries, created few jobs. These industries remain highly protected. Moreover, these industries - such as cement, steel, car assembly and so on - developed for a few years before falling into crisis due to excess supply. In other industries like sugar, capacity has continuously expanded, but raw materials have not kept pace. Apart from that, close linkages among processing industries, assembly industries and services have not developed.

Third, previous economic growth has relied on the public and FDI sectors. The ratio of FDI to GDP increased from 6.4% in 1995 to 13.3% in 2000. Meanwhile, although the non-SOE domestic private sector is now recognized and given attention, its ratio to
GDP decreased from 53% in 1995 to 48% in 2000\textsuperscript{6}. The SOE sector ratio to GDP has not changed since 1995, accounting for 39% to 40% (see Table 5.9; Tran Dinh Thien, 2001: 89-95). To date, most joint ventures have involved foreign partners and SOEs. In agriculture, forestry and fisheries, the SOE and PE situations have not changed since 1991. Vietnam’s GDP structure reflects the following serious problems: (i) since the private sector - which is believed to be dynamic, resilient, flexible, quickly adjustable to external changes, and able to create more employment - is still not given priority, it has not been able to grow as fast as other sectors\textsuperscript{7}; (ii) although SOEs have improved since 1995, they still face many problems. In recent times, due to the Asian financial crisis, a large number of SOEs have been in serious trouble (see Section 6.1.2). Table 6.14 shows some SOE financial performance indicators; (iii) SOE monopolies in domestic markets

\textbf{Table 6.14: Vietnam: Financial Indicators for SOEs, 1997 (%)}

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Debt/legal capital</th>
<th>Debt/assets</th>
<th>Short term debt/assets</th>
<th>Long term debt/assets</th>
<th>Over due debt/Short term borrowing</th>
<th>Bad debtors/ Receivables</th>
</tr>
</thead>
<tbody>
<tr>
<td>SOE Average</td>
<td>138.8</td>
<td>58.9</td>
<td>46.5</td>
<td>10.2</td>
<td>5.9</td>
<td>4.9</td>
</tr>
<tr>
<td>Profit-making SOEs</td>
<td>116.7</td>
<td>53.9</td>
<td>44.1</td>
<td>7.4</td>
<td>1.4</td>
<td>1.1</td>
</tr>
<tr>
<td>Breaking-Even SOEs</td>
<td>176.6</td>
<td>64.1</td>
<td>48.4</td>
<td>14.3</td>
<td>4.8</td>
<td>6.9</td>
</tr>
<tr>
<td>Loss-making SOEs</td>
<td>278.0</td>
<td>84.9</td>
<td>61.4</td>
<td>20.4</td>
<td>32.6</td>
<td>26.4</td>
</tr>
</tbody>
</table>

\textbf{Source: MOF, 1999}

\textsuperscript{6} In February 2002, the Central Committee of the CPV finished the Fifth Plenum (IX Tenure) which devoted considerable attention to the possibility of allowing further development of the private business sector. Notably, members of the CPV will now be able to engage in private business (Resolution of the Fifth Plenum of Central Committee of CPV (IX Tenure), \textit{Communist Review}, February 2002).

\textsuperscript{7} According to some domestic investors, in Vietnam’s legal environment, the private sector is unable to carry out big projects due to shortage of capital.
such as telecommunications, civil air transportation and so on, are seen as the cause of Vietnam’s unfavorable business environment compared with other countries in the region (JETRO, 2000). These monopolies do not stem from SOE strengths, but rather from government protection and SOE monopolies in production, business, foreign trade and so on.

Fourth, although the FDI sector has developed rapidly and contributed significantly to economic and export development via transfers of technology, entrepreneurship, skills, marketing skills and so on (see Sections 6.2.1 and 8.2.3.5), the current FDI situation in Vietnam has raised some concerns as follows: (i) since two thirds of FDI into Vietnam originates from Asian economies, FDI inflows have not recovered to pre-Asian crisis levels, and even approved investment proposals have not materialized; (ii) most disbursed capital has concentrated on heavy industry (15%), oil and gas (28%), and estate property (17%), where Vietnam does not have comparative advantage in terms of cheap labor, and hence, cannot improve its competitiveness; (iii) unlike its ASEAN neighbours, in the past, FDI to Vietnam was for import substitution products, i.e. for the domestic market, rather than for export; (iv) of the actual FDI project capital, the ratio of

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88 These industries have been strongly protected by government. Thus, protectionist pressure - which originated not only from SOEs, but also from foreign invested enterprises - impeded economic reform and structural adjustment for Vietnam’s international economic integration.

89 According to FIAS, 25% of Vietnam’s FDI projects tended to be export-oriented, while in Indonesia, this indicator was 72%, in Malaysia 56% and in Thailand 48% for 1980s-1990s. Moreover, Gates’s work on trade and looking at effective rates of protection, found that most FDI products in Vietnam are not contributing more than 20% domestic value added while many enjoy very high ERP.
loan capital has rapidly risen\textsuperscript{80}. This practice is warning that in the near future, due debts of FDI projects increased dramatically, whereas FDI projects’ possibilities and opportunities of earning foreign exchanges for the debt payments have been limited, thereby weakening the international payment balance of the economy and restraining payment of foreign debts; (v) another big problem of Vietnam’s FDI is relatively open in principle, but complicated and restrictive in practice, i.e. there is the gap between the formal institutions and the reality of application. This phenomenon came from practice of paying bribes, hence pushing production costs up too high\textsuperscript{91}; (vi) the major partners of foreign investors in joint venture projects are SOEs, which have got many shortcomings, which need to be overcome (see Section 6.1.2). Apart from that, since there are increasing contradictions and suspicions between SOEs and foreign investors within joint ventures, the latter want to establish projects with 100% foreign ownership. Foreign investors do not transfer the latest technologies to joint ventures, do not pay attention to long term investment strategy for sustainable development of joint ventures\textsuperscript{92}.

In sum, the above shortcomings of recent economic structural changes originated

\textsuperscript{80} More than 80% of actual capital in foodstuffs, estate property, and construction originated from borrowings

\textsuperscript{91} Practically, this phenomenon is the institutional issue from bottom to top and back to bottom, which can not be remedied by laws passed by the National Assembly.

\textsuperscript{92} According to Gates, as Vietnam enters more and more trade agreements, FDI is going to become one critical ingredient for technological/economic “catch-up”. But effective strategies and policies must be developed to play vital roles in industrialization. FDI can be encouraged by creating conducive conditions and establishing an industrial promotion unit (like the Malaysian Industrial Development Authority, MIDA), for example. Thus, one can leave the domestic sector selection process to the market, but encourage “good” future industries to enter Vietnam’s market through FDI, which, with appropriate policies, should positively influence Vietnam’s domestic firms (Gates, 2002).
from mechanisms of investment allocation and management. To date, most socio-economic capital resource allocation has been decided by administrative decision, not by market forces. Vietnam has been in transition to becoming a market economy for more than 15 years, but its mechanisms of investment allocation and management have not been transformed in line with market forces and still have administrative and centrally planned characteristics. Therefore, all efforts to raise investments in line with the tendencies mentioned above might improve economic performance in the short term, but will make the economy much more inefficient in the medium and long term.

6.3.3 Exports and Protection for Domestic Production

6.3.3.1 Exports

Practically, export growth has been one of the important factors to increase economic growth and create employment in the last decade. Exports in 2000 were seven times bigger than in 1991. Export growth rate gradually decreased from 34.4% in 1995, to 33% in 1996 down to 27% in 1997 and 2% in 1998\(^3\) (see Table 8.24 and Section 6.2.2.2). Nonetheless, some things worth paying attention to are: (i) in general, the value added of exports has been low. For example, in the apparel industry, the export value added was only 20%; (ii) the export structure has changed slowly since 1991. Raw (unprocessed) agricultural and fisheries products and minerals (mainly crude oil) accounted for the

\(^3\) In 1998, because all Vietnam's Asian partners were affected by the Asian financial crisis, export growth - which was low with rate of about 2% - mainly originated from high rice exports. Recently, the rise in fisheries exports has created more opportunities for economic structural changes and export diversification in rural areas, thereby further promoting exports in the future.
major part of Vietnam’s exports. The rest are light manufacturing products like leather products, textiles and garments, produced by processing contracts (see Table 6.15); (iii) hi-tech products, a very small part of Vietnam’s total exports, have mainly been produced in foreign invested enterprises; (iv) except for crude oil and some engineering goods, the main export products were produced by private sector. In other words, investment in SOEs has not improved the economy’s competitiveness and produced many export commodities.

**Table 6.15: Vietnam: Export Structure, 1990-2000 (percentage)**

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</tr>
</thead>
<tbody>
<tr>
<td>Minerals and crude oil</td>
<td>25.7</td>
<td>33.4</td>
<td>37.0</td>
<td>34.0</td>
<td>28.8</td>
<td>25.3</td>
<td>28.7</td>
<td>28.0</td>
<td>27.9</td>
<td>31.0</td>
<td>35.6</td>
</tr>
<tr>
<td>Agricultural, forestry, fisheries</td>
<td>47.9</td>
<td>52.2</td>
<td>49.5</td>
<td>48.4</td>
<td>48.1</td>
<td>46.2</td>
<td>42.3</td>
<td>35.3</td>
<td>35.5</td>
<td>32.7</td>
<td>30.1</td>
</tr>
<tr>
<td>Light industries and handicrafts</td>
<td>26.4</td>
<td>14.4</td>
<td>13.5</td>
<td>17.6</td>
<td>23.1</td>
<td>28.5</td>
<td>29.0</td>
<td>36.7</td>
<td>36.6</td>
<td>36.3</td>
<td>34.3</td>
</tr>
<tr>
<td>Total</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

*Sources: GSO, 2001*

Although markets for export commodities have been extended and diversified\(^{94}\), Vietnam’s exports have mainly gone to Asian, particularly East Asian markets, accounting for 70% of export volume, thereby making Vietnam subject to economic fluctuations in the region (see Table 8.18).

These shortcomings in export structure and markets make Vietnam’s exports very vulnerable, particularly when external turbulence like the Asian financial crisis of 1997-98\(^{95}\) occurred. When the regional economies recovered, these shortcomings were revealed

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\(^{94}\) At present, Vietnam has economic and trade relations with 154 countries and economies in the world.

\(^{95}\) Exports of agriculture, fisheries and forestry products are highly sensitive to demand fluctuation. The exports of rice and coffee in 2001 are good examples of their sensitivity. Whenever demand declined, their prices and export volumes also went down.
more clearly. Because of the impact of the crisis, the economic structures of economies in the region changed, causing import demand for Vietnam’s goods to change. These economies do not demand Vietnam’s goods as much as before the crisis, while Vietnam has done little to improve its commodities’ competitiveness\textsuperscript{96}. Vietnam’s manufacturing products were mainly consumed in the domestic market, even if they were hardly able to compete with imported goods, particularly from China. In the near future, except for crude oil, it is difficult for Vietnam to increase both export prices and volumes. If export prices are raised, the competitiveness of commodities will decline. At the same time, if Vietnam were to increase export volumes, it is required to invest more in export manufacturing industries.

To increase exports, one thing should be done immediately is to develop the services sector - tourism\textsuperscript{97}, (both sea and road) transportation\textsuperscript{98}, and information technology and telecommunications\textsuperscript{99} - for which Vietnam has much potential. Apart from that, in the medium term, Vietnam can expand its exports to new markets, if it

\textsuperscript{96} Because of economic structural reforms in neighboring countries due to the crisis, Vietnam’s competitiveness has relatively declined from 48 of 59 in 1998 down to 53 of 59 in 2000 (World Economic Forum, 2001).

\textsuperscript{97} Vietnam has strong potential for tourism development. Foreign tourists to Vietnam increased rapidly from 1.0 million in 1996 to 2.5 million in 2001. It is estimated that in 2005, foreign tourists going to Vietnam will be around 4 to 5 million.

\textsuperscript{98} Vietnam has a convenient geographical position to develop transportation services, such as road transport for Laos and Northern Thailand, and sea transport to Japan and other neighbor economies.

\textsuperscript{99} Vietnam’s human resource development (HRD) index has been high compared with neighboring economies for many years. The Vietnamese are good at mathematics and other natural science subjects. These have potential to develop information technology and telecommunications, but require more investment capital.
intensively raises investments in export industries and diversifies its exports. In other words, changes in the export structure must combine with investment and resource allocation policies to exploit its comparative advantages to raise commodities’ comparativeness (see Section 6.2.2.2 for reference).

6.3.3.2 Imports

Imports to Vietnam rapidly rose during 1991-2001. Imports in 2001 were more than seven times higher than in 1991. During 1991-95, the annual average rate of import growth was 24%; the highest rate of 54% was achieved in 1995, while in 1996-2001, the rate was only 14.7%, for which the rate in 1996 was 37%; 4.3% in 1997; -0.8% in 1998; 1.7% in 1999; 31% in 2000 and 15% in 2001 (see Table 8.24). Thus, like exports, imports achieved high growth during 1993-96, then, suddenly fell in 1997-99, and then rose again in 2000 and 2001\(^{100}\). Obviously, fluctuations in import growth were closely related to economic performance, FDI and exports. From 1997, Vietnam’s imports went down, not only due to decreased economic growth, but also because of administrative measures to restrict imports. In order to avoid trade deficits, Vietnam reduced imports of equipment and machinery. This may stabilize the macro-economic situation in the short term, but may cause negative impacts on economic performance and stabilization in the medium term.

It is argued that, in general, in the first stage of industrialization, trade and current

\(^{100}\) One key reason for renewed import increases was that since 1999, the Vietnamese dong has appreciated in comparison with other regional currencies, which discouraged exports, encouraged imports and local consumption.
account deficits are inevitable. But these deficits - which were too high by international standards for Vietnam in 1991-98 (see Table 7.3 and 8.24) - were offset by FDI and ODA (which are less volatile and stable), thereby not making the economy unstable and uncertain in the short term.

However, with the transformation of its economic and export-import structures, one can conclude that Vietnam’s economy in the period of 1991-2001 followed the classical model of import substitution. In other words, trade and industry policies still reflected protectionist ideas, expressed in the following ways: (i) commodities, which were supplied for the domestic market by domestic producers, could not be imported; those goods, not adequately supplied by domestic producers could only be imported subject to quantitative restriction measures as well as technical and administrative measures (see 6.2.2.1). In practice, this solution originated in centrally planned economic mechanisms; (ii) many provinces and cities carried out investment policies to create self-sufficient production structures for each province and city. For example, they planned to build and develop cement, sugar, brewery, soft drink industries and so on to consume within the province/city, ignoring scale economies, efficiency and competitiveness consideration; (iii) although adjusted, tariffs imposed on imported consumer goods were still high. Moreover, the government selection and designation of import-export contacts (by administrative measures) (see Section 6.2.2.1), i.e. giving monopolistic rights to some GCs-90 or GCs-91 to do export-import activities were big impediments to import goods

However, although a developing country, in the first stage of industrialization, China has got trade and current surpluses for many years (for example, see Asia Monitor; Vol. 8, No 5, May 2001).
and expand economic relations with foreign countries\textsuperscript{102}.

These policies affected the resource allocation, and thereby, the creation of less efficient production and market structures as follows: (a) these policies increased prices of local products, and in turn, reduced domestic market size for these products. Local industrial products with high prices could not be sold in rural markets since incomes of peasants were still generally low. As a result, industrial structure was not linked to promotion of agricultural production and rural development\textsuperscript{103}; (b) the policies encouraged passive SOE behavior in doing business and raising competitiveness, which did not encourage SOEs to renovate technologies and products, or to look for foreign markets for export sales. Such behavior will survive as long as the government does not end subsidies, which is the main reason for such complaint rent seeking activities\textsuperscript{104}; (c) the policies did not encourage investments in materials production and provision, but often paid attention to finished goods production. This means that the earlier manufacturing structure did not exploit domestic materials strengths, but preferred to import materials from abroad. As a result, it could be said that industrial and trade policies in the last ten years, particularly from 1995, have created production structures not suitable for Vietnam's comparative

\textsuperscript{102} Since 1999, the government enacted some decrees and circulars for more trade liberalization, such as direct export-import permits given to the private sector, changes in quota procedures, elimination of quantitative restrictions and so on.

\textsuperscript{103} While the inventories of strongly protected products - such as cement, sugar, steel, iron and paper - rapidly went up, these products were continuously imported in large quantities in 1999-2000. These proved that domestic demand for these products exists, but the market only accepted lower prices.

\textsuperscript{104} GCs-90 and GCs-91 worried very much when the government decided to eliminate some protection measures for certain products produced by these GCs in accordance with resolution No 46/2001/QĐ issued on 4 April 2001.
advantages and consumption structure, thereby making production inefficient and less competitive even in the domestic market.

6.3.4 Economic Development and Industrialization, 1995-2001

Unlike 1986-94, 1995-2001 was characterized by big foreign financial inflows into the economy, which was favorite factor for Vietnam’s rapid industrialization\textsuperscript{105}, and required Vietnam to improve the efficiency of its economy and to combine with domestic sources to develop. However, since the government was afraid of impacts of big foreign financial sources, economic reforms were slowed down. Then, the government carried out separate and dispersed solutions. In some respects, there were signs of reforming the centrally planned economy, albeit in new forms such as production subsidies, loan write-offs for some SOEs, and so on.

Since the middle of 1997, macro-economic policies have mainly concentrated on temporary administrative measures to deal with the Asian financial crisis. These measures were necessary to cope with the crisis, but lasted too long and were applied too widely to many aspects of the economy such as exchange rate determination, management of foreign exchange and of export-import activities. At the same time, some problems - like competition, fair business, enterprise bankruptcy and so forth - have not been addressed. Direct administrative interventions have rapidly and regularly increased in many areas, particularly in foreign trade. As a result, the achievements of previous economic reforms

\textsuperscript{105} FDI, annually, accounted for 23\% of gross domestic capital formation in 1995-2001. Foreign invested enterprises accounted for 34\% of gross industrial production, 22\% of total imports, and 13\% of GDP (CPV, 2001)
have been reduced.

The IX Congress of the CPV held in April 2001 endorsed further implementation of comprehensive economic renovation in combination with administrative reform for 2001-2005 and beyond, for which economic structural adjustment to exploit all comparative advantages of the economy is key. As mentioned earlier, the present economic structure created unstable, uncertain and unsustainable economic development, with political and social implications. The economic situation in 1999-2001 proved that if there was no economic structural adjustment\textsuperscript{106}, the economy could not bring into full play the impulse to recover and grow faster. Therefore, in the future, the government has to focus on economic reform and structural adjustment, to combine economic and administrative reforms with integration of Vietnam’s economy into the world economy, to combine efficient use of internal financial resources with good use of foreign savings.

6.4. Conclusion

Since 1995, Vietnam’s government has carried out the second phase of renovation, which emphasizes economic policies for integration of Vietnam’s economy into the regional and

\textsuperscript{106} The efficiency of macro-economic policy reform depends on economic structural adjustment with transformation of resource allocation and use as well as governmental apparatus reform. In turn, structural adjustment will only be successful if it gets support from macro-economic policy reform. For example, trade liberalization will affect the interests of the staffs directly or indirectly involved in the licensing system and “requesting-giving” mechanism, who protested against trade liberalization. Consequently, trade liberalization has been subject to sound adjustment of the economic structure and governmental apparatus reform. On the contrary, appropriate structural adjustment within each SOE and among SOEs will affect the pace and scope of trade liberalization.
global economies. This means that Vietnam has made great efforts to promote open trade and investment in line with AFTA, APEC and WTO requirements. These efforts have involved both internal and external liberalization. According to Japanese Ambassador to Vietnam Yamazaki, foreign investors were much impressed by Vietnam’s recent efforts to speed up economic reforms, especially implementation of the landmark law on enterprises and the revised 2000 law on FDI (Saigon Times Weekly, 16 June 2001)\(^\text{107}\).

Vietnamese economic integration into the world has involved all sectors, economic fields, localities and enterprises. Therefore, the best action motto right now is to take initiatives to pro-actively integrate into the world’s economy, meaning that all advantages and weaknesses of each unit should be identified to work out appropriate solutions to ensure sustainable advances stemming from economic integration. Integration into AFTA is a preparatory step towards integration into APEC and the WTO in future. The AFTA roadmap is suitable for Vietnam’s stance on conditional, selective and time-limited protection aiming at pushing the transformation of its economic profile in favor of developing business capability and the economy as a whole. This needs strong political will and close cooperation between government and business, in which increased enterprise competitiveness is the pivotal issue deciding the success of integration. Enhancing competitiveness is not the only businesses responsibility, but also of the government and the entire society. In doing so, the government must first create a

\(^{107}\) That is why over nine years from 1993 to 2001, the Consultative Group for Vietnam agreed to provide official development assistance (ODA) of US$14 billion, of which more than US$9 billion was disbursed (Saigon Times Weekly, 16 June 2001). Three major donors for Vietnam, including Japan, the World Bank and Asian Development Bank, made up 80% of total ODA capital.
competitive environment, which must be stable, open-minded and cost-effective for businesses.

The economic strength of each country lies in the competitiveness and efficiency of enterprise activities. By international standards, Vietnamese enterprises are mainly small and medium, whose notable shortcomings remain low productivity, backward technology, poor quality and design of products. Therefore, Vietnam’s government has enacted the law on enterprises and carried out restructuring as well as equitization of SOEs to boost production and enhance enterprise competitiveness. In general, Vietnamese enterprises have no business strategy with the ambition of dominating the market, have not put much investment in research and development, and lack sudden progresses in doing business. Facing global integration, many enterprises are experiencing problems. They want the government to prolong protectionist measures and give priority to certain branches and fields. However, in the immediate future, Vietnam will implement AFTA and the US-Vietnam bilateral trade agreement. There will be many impacts on Vietnam’s industrialization, particularly on enterprise activities. As a result, enterprises must be either competitive or be eliminated. Each enterprise should bear full responsibility for business, market research and improvement of product design and quality; each should learn to choose suitable customers and investment partners. Enterprises should know how to cooperate with each other in joint efforts on a voluntary and mutual basis to increase their strength in competing and protecting their legitimate rights. In the Chapter 8, there will be impact calibration of international economic integration on Vietnam’s industrialization by using a computable general equilibrium model basing on counterfactual analyses.