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Vietnam's economic transformation: Embracing change

Vu KHOAN

Philip Charles ZERRILLO

Singapore Management University, pzerrillo@smu.edu.sg

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VIETNAM'S ECONOMIC TRANSFORMATION: EMBRACING CHANGE



The former Deputy Prime Minister of Vietnam from 2002 to 2006, Mr Vu Khoan, talks about the transformation of the country from economic isolationism to its current economic strength, in this interview with Philip Zerrillo.

It has been 30 years since Vietnam introduced the 'Doi Moi' or economic renovation policy—a commitment to increased liberalisation and structural reforms necessary to modernise the economy. Would you say this has been successful? What are the continuing challenges?

Let me recall for you what it was like in 1986. We were suffering from a massive social and economic crisis at that time. Inflation was then 587.2 percent. There was a trade embargo and we were economically isolated from the rest of the world. Our key sponsor at that time was the former Soviet Union, which was itself in a deep crisis. We were a low-income country—the average annual per capita income was about US\$86. Today, in 2016, the average income is about US\$2,300 (US\$2,111 in 2015) per person per year, and Vietnam is recognised as a middle-income group country.

And we are no longer isolated. In 1986, our exports were barely US\$800 million—but by 2015, this had grown to US\$162 billion. Back then, we had almost zero foreign investment and official development assistance (ODA). Since then, we have accumulated US\$230 billion in foreign investment and US\$30 billion in ODA. What is perhaps the most rewarding part is that the poverty rate has decreased substantially. If we calculate poverty as a daily income of less than US\$1.5 to US\$2 per family, then back in 1986 almost 50 percent of Vietnam's population fell in this category, and today it is about 3 percent. To me, these numbers are the real reflection of the success of the reforms.

Let me explain more about the challenges today by providing some context. Thirty years back, we were focused on improving quantity and did not look as much at the quality. But the situation these days is that we are now more focused on quality rather than quantity, and are hence switching from extensive horizontal growth to vertical growth. To clarify, back then we relied mostly on cheap labour and a lot of capital investment, as well as the exploitation of natural resources, primarily oil and coal, for our growth. But productivity was really low. It was about one-fifteenth that of Singapore. Today, we are focusing on economic growth based on technology and skills rather than exploiting natural resources or relying on foreign investment. To give an example, if we look at our rice exports, we are second in the world—but the quality of our rice is not that good—and so our key focus today is to restructure our agriculture.

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Finally, we have been wanting to privatise and reform our state-owned enterprises (SOEs), but that has not been as successful as the government has hoped. There are several reasons for the delay. The real situation is much more complicated than we expected. First, there are several leaders and executives in those SOEs who do not want to give up their power. The second, and more difficult, is how do we value those SOEs? For example, the value of the land or equipment is very different from one SOE to another. Third, several SOEs are reporting losses—so how do we 'IPO' them? After all, it is common sense that people will only buy companies that make profits. At this moment, the companies that are much wanted by foreign investors include companies like Vinamilk, Saigon Beverage Company and Hanoi Beer, which are performing well.

As Deputy Prime Minister in charge of Foreign Economic Relations from 2002 to 2006, you have greatly contributed to the negotiation process of various free trade agreements (FTA), and also to Vietnam joining the World Trade Organization in 2007. How has Vietnam benefited from this global integration? And what are the challenges ahead?

The most important characteristic of the economic reforms of 1986 was that we opened our doors to the world and began to integrate with the global economy. Even today this policy is not only maintained, but also strongly pushed. We are currently the country with the sixth highest number of FTAs; we have agreements in place with all the strong economies of the world, including the EU, the U.S. and the ASEAN nations. Why are we doing this? It's because we recognise that FTAs give us access to a larger market and increase our exports considerably. Back in 2000, when I was the Minister of Commerce and wanted to sign a FTA with the U.S., our exports to the U.S. were about US\$760 million. Today they are worth approximately US\$45 billion in bilateral trade. Another benefit from signing FTAs is that we receive a lot more foreign investment. It also

provides Vietnamese companies the opportunity to learn to do business on a global scale. Additionally, the price of imported goods into Vietnam is much cheaper—which is very important to the country, because prior to this, it was primarily a manufacturing and outsourcing nation. Finally, because we have integrated with the world, our thinking on economic policy in Vietnam has developed a lot, which has also improved our position in the world. The key focus of our foreign affairs policy is to diversify our relationships, and integration helps us with that.

But of course there are a lot of challenges. The first is that the competitiveness of our economy is still low, and so we are concerned about how we can compete with our partners. We are also facing fierce competition for foreign investment from neighbouring ASEAN countries. Second, both the government and our companies do not have much experience in competing globally, and we have a lot to learn. Many of the restructuring processes in Vietnam have not been able to catch up with the pace of change in the world. Third, it is very difficult to manage 55 different partners. How do we maintain the balance between the domestic economy and global integration? So while Vietnam's exports are really large at US\$173.32 billion, about 70 percent comes from foreign direct investment companies.

As I observe the world, I believe that nations tend to follow two paths. First, there appears to be an increase in protectionism in some form in many countries. Those countries now want to protect their local markets. The second tendency is that they want to carry out free trade through FTAs. While these seemingly opposing trends exist in

parallel, they also complement each other. I personally believe that it is imperative for us to open up to the world. If you want to only focus on your local consumption, it is a closed circle which is also getting smaller. Moreover, you cannot develop it as fast, especially if you are a developing country.

In your opinion, what role have the politicians and administrators played in the economic development of Vietnam?

There is a common misunderstanding among foreigners that Vietnam does not reform its political policies. That is totally wrong. From Doi Moi days, we have not only focused on restructuring economically, but also on political reform. The Vietnamese have a saying that before you decide to follow any ideology, you need to first fill your stomach. So we had to first focus on economic reforms. However, at the same time, we were observing conflicts in other nations like the former Soviet Union, and we realised that these conflicts or civil unrest do not bring any benefit to the people. So to restructure our economy, we needed to maintain a certain amount of political stability. But the truth is that the ideology Vietnam wanted to follow was without precedent—we have never seen it in any other country. So we have to observe how it goes.

The second characteristic is that when we wanted to restructure the government, we wanted to revamp the party. We wanted to switch the Vietnam government to one that is ruled by law. Prior to 1986, when we, the bureaucrats and party members, used to go to a parliament session, there was almost no discussion. Everything was decided by the government, that is, by the ministers. Now it is completely different. The

parliament has great influence and power. It has to sign off on key initiatives such as the budget and proposed FTAs. All parliamentary sessions are shown live on television. Members of parliament are now able to challenge members of the government, and that too is broadcasted live. Similarly, before our reformation, we had only four to five newspapers. Today we have over 5,000 newspapers. There are also approximately 175 television channels, including several that are privately-owned. Around 50 percent of the population has access to the Internet, and for every 100 Vietnamese people, there are 145 mobile phones. Society is much more open now.

And finally, while the government observes and learns from the general human rights situation in different parts of the world, we believe we have to adjust those observations and learnings to fit our situation. So for instance, we realise that the literacy level of our people is still low, but we do note that over 70 percent of Vietnamese are farmers, and that we have had 30-40 years of war.

How can Vietnam avoid falling into the middle income trap?

We have actually recognised that we are at risk of falling into that trap, and that is why we are focusing on restructuring the economy and changing the model to focus on quality instead of quantity.

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That's going to be our focus for the next several years. This is a key topic being discussed today at the Central Committee meetings as well as in the parliament.

We are also facing a new challenge that we have not faced before—climate change. Vietnam is a country that will suffer a lot from this phenomenon. Already, our economic growth in 2016 is forecast to be below expectations because of this. Climate change in the Mekong Delta, which is located in our southern provinces and is the region that provides rice for the whole nation, has changed everything. This region can no longer focus on rice production, as the ocean has taken over, salinisation has increased, and it is now short of fresh water. The other key challenge associated with climate change is that the vast majority of farmers are soon going to start moving to urban areas in search of a livelihood. Hence, we have to push for the development of industries so that we have jobs for those farmers, or else larger social issues will arise.

Education too will play a big role here, and is currently a great challenge. Up to now, our education system has had a lot of issues. We teach a lot of theory but provide hardly any practical experience. We are also focused on training a lot of university students to get a degree, but there are not enough skilled workers. It should actually be the other way round, because now we are concerned about unemployed university students, and at the same time, a lot of international companies can't find enough skilled workers. And with the ASEAN Economic Community, the market will soon open up and we will be flooded with skilled workers from these countries. So we are concerned about this. In fact, the situation is very similar

across many ASEAN countries that follow Confucianism, where the ideology is to focus on becoming government officers and highly educated professionals, instead of being skilled workers.

What do you see to be the most pressing challenges and greatest opportunities for Vietnam's economy in the coming five years?

There are three key challenges that Vietnam's economy is facing today. The first one is that we are still battling the consequences of the last few years that had their origins in the 2008-09 financial crisis, manifested in the high budget deficit and soaring public debt. There is also the slower economic growth rate taking place the world over at a time when Vietnam is trying to integrate with the world. To my mind, the second challenge is climate change, which is really affecting us, particularly when we are restructuring our economy. It's similar to how one has to lower the speed of a car when making a U-turn. And the third challenge is Vietnam's relationship with other countries, which is taking place at a time when the fourth—digital—industrial revolution is happening.

But I am very positive, and if I had to write a letter to the next generation, I would tell them not to be as foolish as we were. Because 40 years from now, the world will be totally different. At 80 years of age today, I have experienced writing with pen and ink to typing on laptops, to smartphones—and maybe one day, who knows, there will no longer be any phones? But while everything *will* change, *how it* changes is more important.

Climate change is really affecting us, particularly when we are restructuring our economy. It's similar to how one has to lower the speed of a car when making a U-turn.

Vu Khoan
was the Deputy Prime Minister of Vietnam from 2002 to 2006

Philip Zerrillo
is the editor-in-chief of Asian Management Insights and the Executive Director of the Centre for Management Practice, Singapore Management University