

PART 1 PAPERS : 1 Economic Reform in Vietnam: Achievement, Present Situation, Prospect for International Economic Cooperation

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PART I: PAPERS

Economic Reform in Vietnam: Achievement, Present Situation, Prospect for International Economic Cooperation

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I. *Doi Moi*: Its significance and Objectives

Since 1986 Vietnam has carried out drastic reforms in the political, economic and social fields under the banner of *Doi Moi*, (renovation in Vietnamese). Needless to say, the priority of *Doi Moi* lies in economic reform.

In the aftermath of the North-South reunification in 1976, Vietnam started to establish a form of socialism of the Soviet type throughout the country under the Northern leadership, but was soon faced with severe economic difficulties. These difficulties were attributed, first, to the failure in developing the potential of the South, which once had a Free Economy, and second, to the economic embargo enforced by the U.S. and other Western countries, together with the withdrawal of aid by China, a former friend, during and after the Cambodian crisis. The objective of the major economic reform initiated in 1979 was, therefore, to improve the rigid and inefficient economic management (or planned economic mechanism) and thus to overcome the difficulties amidst the continuous economic embargo.

Although the need for alleviating the shortcomings of the existing economic management had been repeatedly pointed out, the reform was continuously delayed due to the lack of consensus over what course should be taken. *Doi Moi*, initiated in 1986, had two major objectives in the economic field, i.e. to promote an economic liberalization policy at home and an open door policy internationally. It must be pointed out that *Doi Moi* was promoted not only because Soviet Perestroika had started in the previous year but also because the Soviet Union, which had long been helping Vietnam, began to demand greater efficiency in the use of its assistance. The economic reform under *Doi Moi* was promoted in line with three specific objectives:

(1) The priority of investment should be transferred from heavy industries to such industries that are directly connected to daily life, or to those sectors in which

Vietnam enjoys a comparative advantage, that is agriculture, consumer goods and export goods. The transfer is expected to improve the efficiency of the investment for economic development.

(2) The rigid and inefficient economic management (or planned economic mechanism) should be substituted by one with a market-oriented economy. Particularly, private enterprises, which were once the target for socialization, should now be encouraged to pursue economic development. In addition, state-run enterprises, which had long been heavily dependent on financial subsidy, should be relatively independent of state planning and should thus establish for themselves an economic-accounting system, aiming at the reduction in the fiscal deficit as well as the improvement of economic management.

(3) The international economic relations, which were once so heavily dependent on the Soviet Union, should now become diversified under the open door policy. The purpose of the open door policy is to multiply and diversify the sources of the capital allocated for economic development by extending the economic relations to the West and Third World countries, without restricting them to the Soviet Union, which requested more effective use of its assistance.

II. Achievements of *Doi Moi*

These three basic policies of *Doi Moi*, namely the transfer of priority from heavy industries to agriculture, consumer goods and exports, the introduction of the market mechanism, as well as the implementation of an open door policy, might have been carried out more effectively in the South, which once enjoyed a free-economy, with obviously a larger economic potential, than in the North, where the socialistic style of economic management had been dominant. That is to say, the outstanding features of *Doi Moi* lay in an effort to apply the economic policy that once prevailed in the South to the whole country within the political framework of socialism.

In this regard, the revitalization of private enterprises in the South is the major achievement of *Doi Moi*. One of the main objectives for encouraging private enterprises was to create a few jobs, if any, among the continuously stagnating economy, with a constant level of 7 millions unemployed workers. It had also been anticipated that the private sector would develop quickly, if only the Government were to abolish some of the restrictions on private enterprises. The encouragement of private enterprises first took the form of licensing privately owned transportation companies or restaurants, followed by additional licensing of part-time work at home. The policy was accelerated from 1989 onwards. Although there still remain some restrictions in several sectors such as finance, numerous encouraging policies have now been promoted. Therefore there are virtually no restrictions on the number of employees in manufacturing, export and other privileged fields. One of the major roles that private enterprises have been playing is to improve the quality in the service sector which was once considered to be one of the drawbacks of the Vietnamese economy.

The second achievement of *Doi Moi* is the creation of a framework, though still in an initial stage, within which Vietnam will adopt the market mechanism and

improve the economic efficiency. The most remarkable achievement is the success, up to a certain point, in curbing inflation which was once as high as 600% annually at the onset of *Doi Moi*. The soaring inflation rate that had recorded two digits every month since 1986, began to decline from the end of 1988 and became stabilized to one digit figure of 2.5% monthly as early as in 1989 and of 4.4% in 1990.

The reduced inflation rate is attributed to the following policies:

(1) The first step was to reduce the financial subsidy which had been formerly granted to the prices of all manufactured goods produced by state-run enterprises, and to increase the number of economic-accounting enterprises to which a larger autonomy in price-setting was given. At present, as few as 20–30% of all state-run enterprises are still dependent on subsidy, while one-third of the state-run enterprises, which have shifted to a market-oriented economy, are considered to enjoy a sound management.

(2) In the past, the employees of state-run enterprises were provided with cheaper necessities including rice under a ration system, which had been a major cause for the ever-increasing financial deficit. Therefore, the system had been abolished by July, 1988 followed by the complete liberalization in the food distribution system.

(3) In order to alleviate the discrepancy between the official rate of the Vietnamese Dong and its market rate, a kind of floating system was introduced by the middle of 1989 resulting in few differences, if any, between the two rates.

Some of the important factors contributing to the alleviation of inflation are the increase in agricultural production, the subsequently improved balance in the supply and demand, as well as the reduction in grain speculation cases. The remarkable increase in the agricultural production in Vietnam was attributed to the increase in the land area devoted to rice double cropping in the Mekong Delta, in the past 10 years as well as to the reforms in the collective sector aiming at the creation of incentives for cooperative farmers. In specific terms, the reforms implemented in April, 1988 enabled the farmers to receive the land formerly owned by cooperatives and to rent land among farmers. In other words, farmers were granted the right to use land. As a result, the Vietnamese agriculture is undergoing a drastic change from collective farming to private farming.

Due to the increase in agricultural production, in 1989 food production reached a level of 21.40 million tons calculated in paddy, followed by 21.50 million tons in 1990. In addition, Vietnam succeeded in exporting approximately 1.60 million tons of rice for two consecutive years from 1989 to 1990. Vietnam is now the third rice-exporting country after the U.S.A. and Thailand.

These liberalization policies have gradually improved the living standards of ordinary citizens. The number of goods sold in market seems to have doubled or even tripled, although a significant part consists of imported items as a result of the open door policy which will be discussed next.

III. Open Door Policy

The open door policy as an international economic policy is one of the major

achievements of *Doi Moi*. The highlight of the policy is the Foreign Investment Code enacted in April, 1988. The Code stipulates that there should be three different forms of foreign investment, that is, joint venture companies (with a minimum of 30% foreign capital), enterprises with 100% foreign invested capital and contractual business operations. Numerous preferential treatments are provided by the Code so that the amount of foreign investment can be increased.

For example, enterprises with foreign capital will not be nationalized. Foreign investors are permitted to repatriate their assets overseas within the limits of the venture term (the term in general covers 20 years, and in special cases ranges from 30 to 50 years). The corporate income tax for joint ventures is generally low and newly established ventures will be granted a tax reduction and exemption for a certain period of time. As another example of preferential treatment, enterprises with 100% foreign capital can be authorized in some specific sectors whose development is considered to be particularly important by the Government, including export-oriented sectors such as agriculture, fisheries, forestry and their processing sector, etc. The petroleum industry due to the recent discovery of petroleum resources in the South Vietnam continental shelf is another sector that enjoys special treatment increasingly attracting the attention of foreign investors.

The Foreign Investment Code was partly revised in June, 1990 in relation to the following three points: First, originally only state-run enterprises were authorized to establish a joint venture company with foreign capital. In the revised code, however, private companies are authorized or even encouraged to form joint ventures with foreign companies. Second, the old code only authorized ventures on a bilateral or bi-national basis, while the new one has paved the way for ventures on a multi-lateral or multi-national basis. Third, the code of 1988 aimed chiefly at the development of export-oriented industries, while that of 1990 at the expansion of foreign investment to encompass other fields including import substitution sectors.

Under the New Foreign Investment Code, 290 projects had been granted licenses by the second quarter of 1991. The total investment reached approximately \$2 billion in contract terms and \$5 billion in operational terms.

If we analyse the sectors which attracted the largest investment by the first half of 1991, the petroleum industry ranked first, accounting for 30% of all investment. The petroleum (crude oil) industry now occupies an important position in Vietnam, being the second largest foreign exchange earner, followed by the agricultural-fisheries industry including the processing sector which also accounts for 30%. Among other sectors which attracted the largest investment, the service industry including hotels and restaurants ranked third, and the infrastructure-related sector ranked fourth.

If we analyse which countries invested most in Vietnam, Hong Kong ranks first. In terms of total investment, however, Taiwan is closely followed by France and Canada, which invested heavily in the petroleum industry, with foreign capital accounting for 100% of investment in many companies. Furthermore, the investment by the overseas Vietnamese accounts for a relatively large part of foreign investment, although the figures are not as clear as they are in other cases. Incidentally, Japanese investors are involved in 18 joint ventures.

In March, 1991, Vietnam hosted an investment forum under the auspices of UNDP in Ho Chi Minh City, and publicized as many as 187 projects to attract foreign investment. It is said that foreign investors have already decided to take part in almost two-thirds of these projects related to sports goods, textiles as well as agricultural-fisheries processing industries, which can make the optimum use of the abundant resources of Vietnam. Little investment has yet been made either in such basic industries as engines and motors, which are considered to be indispensable for improving the productivity, or in the electronic industry such as radio and television, for which the Government has great expectations. The Government is eager to attract greater foreign investment in these fields. The Government's catchphrase for attracting foreign investors is "the abundant and skilled cheap labor," with a minimum wage of \$50 a month.

The two fundamental principles of *Doi Moi*, that is the economic liberalization policy at home and the open door policy internationally, were more or less reconfirmed during the Seventh Communist Party Congress convened in June 1991. The next Five Year Plan from 1991 to 1995 placed emphasis on the development of the market mechanism, which will lead to further economic reform. The priority was given to the agricultural-fisheries processing industry as well as to agriculture, consumer goods and export industries as it was in the 6th Congress. Although the political programme adopted in the Congress refers to long term prospect for the development of the manufacturing industry, emphasis is also placed on the development of the infrastructure and the industries with advanced technology, in addition to the processing industry which has already attracted increased foreign investment.

IV. Current Situation of the Vietnamese Economy

The economic reform under the banner of *Doi Moi* has achieved numerous results as mentioned above. However, Vietnam is still experiencing economic difficulties.

The Vietnamese economy has been confronted with a new difficulty since the second quarter of 1990, mainly due to the drastic political changes in the Soviet Union and the Eastern European countries which affected the economic cooperation between Vietnam and these countries.

In particular, the economic relations of Vietnam with the Soviet Union have undergone drastic changes since 1990, because the latter decided to review all its economic relations with the COMECON countries. First, the relations between the two countries have been substituted by those between a Vietnamese company and a Soviet company, implying that the Soviet Union as a country would no longer give a preferential treatment to Vietnam. Secondly, the barter trade based on rubles, which made provision for preferential price setting at a rate exceeding actual prices twofold or more, was substituted by a cash settlement based on international prices in dollars. As far as the Russo-Vietnamese trade is concerned, Vietnam was formerly permitted to reckon up a trade deficit every year being 1.5 times as large as its exports. (The 1989 volume of imports was three times as large as the volume of exports). The policy has changed into reciprocity since 1990, with the

ratio being reduced to 1.3 in the same year. In addition, Vietnam is requested to pay back to the Soviet Union the accumulated debt it owes. It is estimated that the Soviet assistance to Vietnam will be reduced to less than one-third of the former level in the near future.

Those drastic changes in the Russo-Vietnamese relations have exerted a considerable influence on the Vietnamese economy. The agricultural sector which used to depend on the imports from the Soviet Union for more than 60% of fertilizers was the most severely hit. It is anticipated that in 1991 the fertilizer imports from the Soviet Union will be less than 10% of the past level. When I visited Vietnam in August, 1991, Vietnamese officials were worried about the fact that the 1991 rice exports may be less than 1 million tons. If the present situation continues, not only the steadily increasing trend of rice exports for the past few years, but also the overall recovery of the Vietnamese economy may suffer a major setback. Moreover, in implementing the 1991 plan, Vietnam is likely to centralize its foreign exchange control and give priority to the imports of essential commodities to productive activities, because the availability of foreign currency is limited.

However, the major difficulty may lie in the shortage of capital for implementing the development plan. Ever since 1955 the Soviet Union started to extend aid to Vietnam, it has invested heavily in the basic sectors of the Vietnamese economy through 250 different projects, most of which involved in energy-related sectors such as hydroelectric power generation or petroleum exploitation.

The Seventh Communist Party Congress in June, 1991, adopted both the Political Report on a broad framework for the next 5 year plan and the long-term economic development strategy from 1991 to 2000. However, if we compare the official Political Report with the draft written in April, 1991, we will find many differences. In the prospects for the next 5 years, the official report places emphasis on original key areas such as agriculture, fisheries, forestry and their processing sectors, as well as on sectors which had already begun to attract foreign investment for which predictions could be made. On the other hand, there are reservations about the prospect for infrastructure-related sectors that require large investments and this aspect is discussed only in toned-down abstract terms, as in the case of the mining sector except for petroleum and bauxite, the heavy industry sector such as cement and metals, the transportation sector such as road construction and port development and also the telecommunication sector such as radio and television. Presently with the rapid decrease of the Soviet assistance (this trend will accelerate after the dissolution of the Communist Party of the Soviet Union.), and the limited assistance from the Western nations, Vietnam has not yet worked out a blue print on how to carry out future development and where to find sources of capital.

V. Vietnam and International Economic Cooperation

We do hope that at the beginning of the 21st century when most of the Asian and Pacific nations will be enjoying spectacular economic growth, Vietnam, as a member of these regions, will also be able to overcome the economic difficulties and succeed in its development.

The Long-Term Economic Development Strategy adopted during the last Communist Party Congress advocates an Income Doubling Plan, by which the present level of national income would be doubled by the 21st century (the present level of per capita national income is 200–210 dollars according to the United Nations' estimate). In order to achieve this target in the next ten years, it is necessary for the Vietnamese economy to expand at a spectacular rate of more than 7% annually. It is also essential for Vietnam to seek international assistance or private foreign investment for one-third to one-half of its development fund. So long as Vietnam wants its economy to develop as well as to recover, it urgently needs to ask the Western countries for larger assistance and investment as was clearly indicated in section IV.

What is essential for Vietnam is to improve its environment at home and abroad, so that Western countries may be willing to expand their economic assistance and their private investment to Vietnam.

One of the major factors discouraging Western investment is Vietnam's immature infrastructure. Development of the infrastructure is essential particularly in the energy sector such as electricity, in transportation systems such as roads, railroads and harbors, in telecommunication such as telegraph and telephone and also in the water supply and sewerage systems. However, this development requires a large amount of capital. This is why Vietnam is looking forward to the resumption of the ODA programs by Western countries including Japan, more than it expects private investment. However, for the Western countries to resume their assistance to Vietnam, a permanent solution of the Cambodian Problem should be attained. As one of the major parties of the Cambodian Problem, Vietnam should do its utmost to restore stability in Cambodia in cooperation with other members.

On the other hand, Vietnam should pursue its economic reform in order to improve its economic efficiency, aiming at increasing the economic assistance.

The ongoing structural adjustment in the financial and monetary systems needs to be further intensified. In 1990, Vietnam tried to separate the National Bank from the Ministry of Finance for the purpose of drawing a distinct line between financial and monetary systems, which had long been combined. At the same time, the Ministry of Finance, which had been nothing more than a tax-collecting organization, was given the authority to control the national fund. As a Business Tax Law, an Income Tax Law and a Consumer Tax Law are being enacted, tax reform is making rapid progress. The banking system of the National Bank, is being reorganized and the note-issuing function is being separated from the commercial banking (agricultural, commercial, foreign trade, and investment banks) system.

Another urgent problem to be solved early in relation to the financial reforms and monetary reforms is that of the negative spread, given to state-run enterprises. Although some reforms have already been implemented for reducing the financial subsidy to state-run enterprises, national banks are still maintaining their peculiar interest system, consisting of a lower-than-inflation deposit rate and lower loan rate. Monetary subsidy that was substituted for the financial subsidy is incapable of reducing the fiscal deficit. It also prevents the sound management of state-run enterprises and only prolongs their unprofitable activities.

For the sound management of enterprises, the first step to be taken is the enact-

ment of a bankruptcy law simultaneously with the abolishment of the negative spread. In addition, a system which would be conducive to the improvement of the function of the principle competition, needs to be devised. It is obvious that under the banner of *Doi Moi*, state-run enterprises have gradually been adjusting themselves to a market-oriented economy. However, the market-oriented economy here is far different from the so-called free economy in the Western countries, as shown in the following example. In Vietnam, prices are monopoly prices, determined by an agreement between a seller and a buyer, which implies that the market structure is nothing more than a "seller-dominated" market. The incorporating experiment that has already started, as well as the privatization of state-run enterprises forecasted in the near future, will contribute significantly to the creation of the competition principle. This attempt will inevitably increase the competitiveness and the export capabilities of the Vietnamese industry, and will in the long run contribute to the improvement of the investment environment in the country.

In this regard, we would like to indicate the need for organizing a labor market, besides, that for capital, which is essential for the incorporating effort. It is true that at present, the foreign investors are permitted to recruit Vietnamese workers by themselves, in addition to depending on the list of prospective workers provided by the Government. However, since the Vietnamese workers must put laborers' contracts with the Vietnamese Government before those with investors, it appears that there is no labor market in the real sense of the word. The Seventh Communist Party Congress made it clear that the Government would give priority to the organization of the labor market in the future. However the Government should indicate what kind of labor market it has in mind.

It has been frequently pointed out that Vietnam has not been accustomed to determining how it could improve the efficiency of aid and investment, namely how to develop a market-oriented economy and how to increase its competitiveness. In this sense, the first step for Vietnam to take, in line with the present economic reform, is to nurture senior officials and economists, well-versed in the Western economy and its conditions. If Japan or any other Asian and Pacific nation wishes to extend assistance to Vietnam, everything should start from there, even in the form of technical assistance.