

INSTITUTE OF SOCIAL STUDIES

Working Paper Series No. 253

IS THE VIETNAMESE MIRACLE IN TROUBLE?

Raymond Mallon and George Irvin

August 1997

Comments are welcome and should be addressed to the author:
c/o Publications Office - Institute of Social Studies - P.O. Box 29776
2502LT The Hague - The Netherlands

The Institute of Social Studies is Europe's longest-established centre of higher education and research in development studies. Post-graduate teaching programmes range from six-week diploma courses to the PhD programme. Research at the ISS is fundamental in the sense of laying a scientific basis for the formulation of appropriate development policies. The academic work of the Institute is disseminated in the form of books, journal articles, teaching texts, monographs and working papers. The Working Paper series provides a forum for work in progress which seeks to elicit comments and generate discussion. The series includes the research of staff and visiting fellows, and outstanding research papers by graduate students.

For a list of available Working Papers and how to order them see the back of this Working Paper.

For further information contact:

Publications Office - **Institute of Social Studies** - P.O. Box 29776
2502LT The Hague - The Netherlands - FAX: +31 70 4260799
e-mail #publication_dept@iss.nl (Attn: Publications Assistant)

IS THE VIETNAMESE MIRACLE IN TROUBLE?*

Abstract: Recently, growing scepticism has been expressed by the major donor agencies and some Viet Nam experts about how far the Government is committed to market reform and whether the country's rapid rate of economic growth is sustainable. Below it is argued that the transition process to a market economy, far from having moved too slowly has moved at a reasonable pace. One indicator of the steady progress of reform is to be seen in contrasting the climate of economic stability at the time of the Eighth Party Congress in 1986 with the sense of uncertainty which marked the Seventh Congress in 1991. While it is true that rapid growth has given rise to a large current account imbalance, that relative poverty is growing, that inefficiency and that rent-seeking behaviour can be observed in the State Owned Enterprise (SOE) sector, evidence of these and other shortcomings can easily obscure the fact that Viet Nam's import boom is investment orientated, that overseas indebtedness is low and the outlook for sustaining the flow of domestic and foreign saving is encouraging, that the proportion of the population in absolute poverty is falling and that SOEs' labour productivity has risen substantially. While much remains to be done in consolidating the institutional structure of a market economy and promoting equity, Viet Nam appears to be facing up to the main problems of promoting sustainable, market-led growth and is performing well by regional standards.

Introduction

Following a self-imposed stabilisation programme in 1988-89 which stopped inflation and opened the economy, Viet Nam has experienced an average annual GNP growth rate of 8 percent year. Moreover, since 1995, growth has accelerated to over 9 percent and inflation has fallen below 5 percent---an impressive performance by regional standards and even more so for a country in transition to a market economy. Yet Viet Nam has received a mixed press lately.¹ Politically, the Eighth Party Congress failed to take a decision about renewing the country's political leadership² while the Party seems increasingly anxious about the erosion of orthodox values (FEER, 1996) and corruption (VET, 1997). Economically, the World Bank (1995a, 1995b, 1996) feels that the financial and legal playing field still slopes in favour of State-owned Enterprise (SOE), that too little attention has been paid to the rural sector and, most ominously, that the current account deficit is unsustainable in the long term. Various researchers and agencies have expressed concern about poverty and environmental degradation (World Bank 1995b, UNDP/UNICEF 1996). More generally, it is argued by some economists that the decline in performance of the Japan and South Korea will slow intra-regional trade and capital flows in turn leading to a slower growth rate for the four tigers, the Newly Industrialising Economies (NIEs) and transitional economies such as Viet Nam. In short, last years' optimism has turned to this year's pessimism.

* Raymond Mallon is an Economic Advisor to the World Bank based in Hanoi; George Irvin is Associate Professor of Economics at ISS, The Hague; this paper is based on Mallon (1996b).

¹ For example, see Schwartz (1995), Hiebert (1996).

This piece examines whether such scepticism is justified. Section I summarises the country's main economic indicators showing how these have evolved between the VIth (or *doi moi*) Congress and the VIIIth Congress last year. In Section II, we examine some of the main questions currently being asked by the sceptics: eg, "is the party really as committed to reform as its claims?"; "what about growing poverty?" and "is FDI-driven growth sustainable in the long term?". Section III compares Viet Nam's performance with that of other countries of the region; ie, the NIEs while Section IV concludes that despite some important lacunae in the reform process, the impetus to increasing living standards and national income via a market-based allocation of resources continued unabated.

I. An Overview of Changes in the Economic Environment

The magnitude of change that has taken place in Viet Nam since the introduction of *doi moi* can be judged by comparing key indicators at the at the time of the Sixth, Seventh and Eighth Party Congress as set out in Table 1 below.

When the Sixth Party Congress was held at the end of 1986, the country was facing a major economic crisis. Despite price controls on most goods and services, the annual rate of inflation was over 700 percent. The value of exports amounted to some USD 500 million, considerably less the half the total value of imports (USD 1,221 million). Although Government had recorded some notable achievements in the areas of health and education, the Central Government paid for a large standing army and civil service and supported loss-making state enterprises. Inflation was fuelled by the monetisation of the resulting deficit, people had to queue for food and sections of the population faced regular periods of famine. There was virtually no foreign investment, the technology gap between Viet Nam and its neighbours was growing, visits by Vietnamese nationals to market economies were very rare and, apart from a limited number of diplomats and aid workers, there very few foreigners from market economies working in Viet Nam.

When the Seventh Party Congress met in 1991, reforms already implemented provided greatly improved incentives to make investments to increase the level and quality of production. Farmers had been given medium-term rights to the use of land; prices and the exchange rate were largely market determined; laws on foreign investment, private enterprises, and companies had been enacted. Economic growth had accelerated to 6 percent, but part of this growth (oil and electricity) was the result of previous large investments financed by the USSR. The value of exports, at just over USD 2 billion, was about four time that recorded in 1986, but exports were

² It should be noted that a number of younger members were elected to the Central Committee; the President, Prime Minister and General Secretary are expected to be replaced at the General Assembly meeting by November, 1997.

dominated by three main commodities (oil, rice and sea products) and there were doubts about whether this growth was sustainable.

Table 1: Key Indicators of Economic Transformation

Indicator	6 th Party Congress 1986	7 th Party Congress 1991	8 th Party Congress 1996/ ¹
Economic Growth (%)	3.4	6.0	9.5
Income/capita (USD) 2/	n.a.	228	290
CPI (% , year to Dec.)	775	67	< 6
Food grain production (kg of paddy/person)	301	323	385
Budget Surplus 3/	-6.2	-3.7	-0.5
Budget Revenue 3/	14.0	13.5	23.0
Capital Investment 3/	6.3	2.8	5.3
Government Social Service Expenditure 3/	3.2	4.4	8.2
Domestic Savings 3/	n.a.	13.2	17.7
-government	n.a.	1.3	5.0
-non-government	n.a.	11.9	12.0
Foreign Savings 3/	n.a.	1.9	11.8
National Investment 3/	n.a.	15.1	29.5
FDI - USD million	-	220	2300
ODA - USD million	-	110	764
Exports -USD million	494	2042	6800
Imports -USD million	1121	2105	10200

1/ projected based on preliminary MPI data as of November 1996.

2/ sharp increase partly due to inflation differential being only partly offset by a depreciation in the Dong.

3/ per cent of GDP.

Sources: GSO, MPI and World Bank.

In 1991, Government still intervened in micro aspects of economic and personal decisions. Travel by Vietnamese citizens continued to be restricted. The number of Vietnamese permitted to travel and study in market economies was beginning to increase, but the number of policy and decision makers with such exposure was still limited. The number of foreigners working in Viet Nam had increased, but official permission was needed for internal travel, and any travel was limited to those provinces specified in the travel permit. Foreign business people, embassies and international agencies had limited flexibility in the recruitment of local staff. The (1980) Constitution provided little protection for the private sector and foreign investors.

Major macroeconomic imbalances persisted, and prospects for sustained economic development were still uncertain. 1991 inflation measured on a December-to-December basis was 67 percent, after having been brought down to single digit levels in 1989.³ External assistance from the Eastern Bloc had effectively stopped; access to financing from the IMF, World Bank and the Asian Development Bank continued to be blocked by the US Government. As SOEs were restructured and Government finances reorganised during the period 1989-93, the SOEs laid off roughly a million employees and Central Government another 160,000; most were absorbed by the low-productivity service sector. Redundancies in State enterprises and Government agencies (including the military) was politically sensitive. A large number of smaller state enterprises were thought to be inefficient; some specialists argued that SOEs should be regrouped and capital targeted at a smaller number of potentially competitive enterprises (Le Duahn Doan, 1990); others felt that many SOEs would need to be privatised or else be allowed to go bankrupt. (Truong and Gates, 1992).

The fiscal current deficit remained was 3.8 percent of GDP with the share of government revenue a meagre 13.5 percent.⁴ Public investment was constrained both financially and by implementation capacity; total investment, at 15 percent of GDP, was less than half that of most East Asian economies (ADB, 1996). Foreign investment approvals were increasing, but disbursements remained low. There remained considerable domestic and international scepticism about whether initial economic improvements could be sustained. In short, at the time of the Seventh Party Congress it seemed far from certain that Viet Nam could meet its goal of sustaining an 8 percent annual growth rate, still less meet it without raising inflation and rekindling inflationary serious expectations which would have curtailed domestic savings still further.

By the time of the Eighth Party Congress in 1996, the situation had changed markedly. GNP growth for 1996 was over 9 percent and the annual average during the previous five year period was 8.2 percent. Inflation had been brought down to an annual rate of under 3 percent by October 1996. At the time of writing (March 1997) inflation is below 2 percent on an annual equivalent monthly basis. Although there has been a 9 percent appreciation in the Real Effective Exchange Rate since January 1993,⁵ convertible currency exports have trebled in five years---from USD 2.1 billion in 1991 to an estimated USD 6.8 billion for 1996. Equally important, exports are more diversified, with strong growth in non-traditional export categories of garments, footwear, and processed agriculture commodities such as coffee, tea cashews, and rubber. The share of Government revenue has almost doubled and stands at 25 percent of GNP. Importantly, in terms

³ See WB (1996) Table 6.1b, p 185.

⁴ See Irvin (1996) for more details discussion of the Government's fiscal weakness.

of sustaining economic growth, the total investment share has doubled to almost 30 percent, a figure in part reflecting the very rapid growth of FDI and accelerated pace of ODA disbursements. The estimated share of Gross National Savings was 18 percent in 1996.⁶

While foreign businessmen may complain about the problems of doing business in Viet Nam, FDI inflows have increased substantially and, as a ratio of GDP, inflows are large by the standards of East Asia. The disbursement rate of ODA, limited by the country's limited administrative experience with Western aid, has now increased sharply. Private property rights, clarified under the 1992 Constitution, have been strengthened by the recently approved Civil Code, and other legislation. The number of registered private enterprises has increased rapidly, albeit from a small base. Permission is no longer required for internal travel, and the number of Vietnamese visiting and studying in market economies is growing.

Paradoxically, the reported share of State owned Enterprise has increased over this period despite the growing legal protection provided to the private sector. The reported SOE share in GDP increased from 33 percent in 1991 to almost 40 percent in 1996. Three factors explain this rise. SOEs have modernised extremely rapidly, mainly because they have absorbed new technology through FDI which they are favourably positioned to attract. Second, the figure reflects two sorts of data problems: the treatment of FDI-SOE joint venture output (see below) and the continued under-recording of private informal sector activity. With respect to the latter point, there is a continued mistrust of the State bureaucracy by the small and medium entrepreneurs, and considerable incentive still exists to avoid the unofficial rents, official taxes and reporting requirements incurred by moving to the formal sector. Given the continued low level of State salaries, 'rent seeking behaviour' is unlikely to disappear in the near future however much foreign business complain and the authorities crack down on corruption.

SOEs have benefited greatly from foreign investment in joint-ventures with state enterprises. For example, foreign investment has played an important role in upgrading technology and transferring skills that have contributed to strong growth in telecommunication services and in oil production, but national statistics record output from these sectors as being 100 percent State output. Continuing preferences given to SOEs (access to decision makers, access to quotas and land, preferential access to credit) is also a factor in the relatively strong performance of this sector,

⁵ See World Bank (1996), Figure 1.4, page 13.

⁶ See Irvin (1996),

and partly explains the strong interest shown by foreign investors in doing business with State enterprises in Viet Nam.⁷

Table 2: Changes Sector Shares of GDP, 1986-96

	6 th Party Congress -1986	7 th Party Congress -1991	8 th Party Congress -1996*
<i>Agriculture</i>	<u>43.8</u>	<u>39.2</u>	<u>32.2</u>
State	1.3	1.0	0.9
Non-state	42.5	39.6	31.3
<i>Industry</i>	<u>25.7</u>	<u>23.1</u>	<u>28.4</u>
State	16.1	15.1	20.0
Non-state	9.6	8.0	8.3
<i>Services</i>	<u>30.5</u>	<u>37.7</u>	<u>39.4</u>
State	15.7	17.0	18.2
Non-state	14.8	20.7	21.2
<i>Total</i>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>
State	33.1	33.2	39.2
Non-state	66.9	66.8	60.8

* projected based on preliminary MPI data for first ten months.

Source: World Bank and MPI.

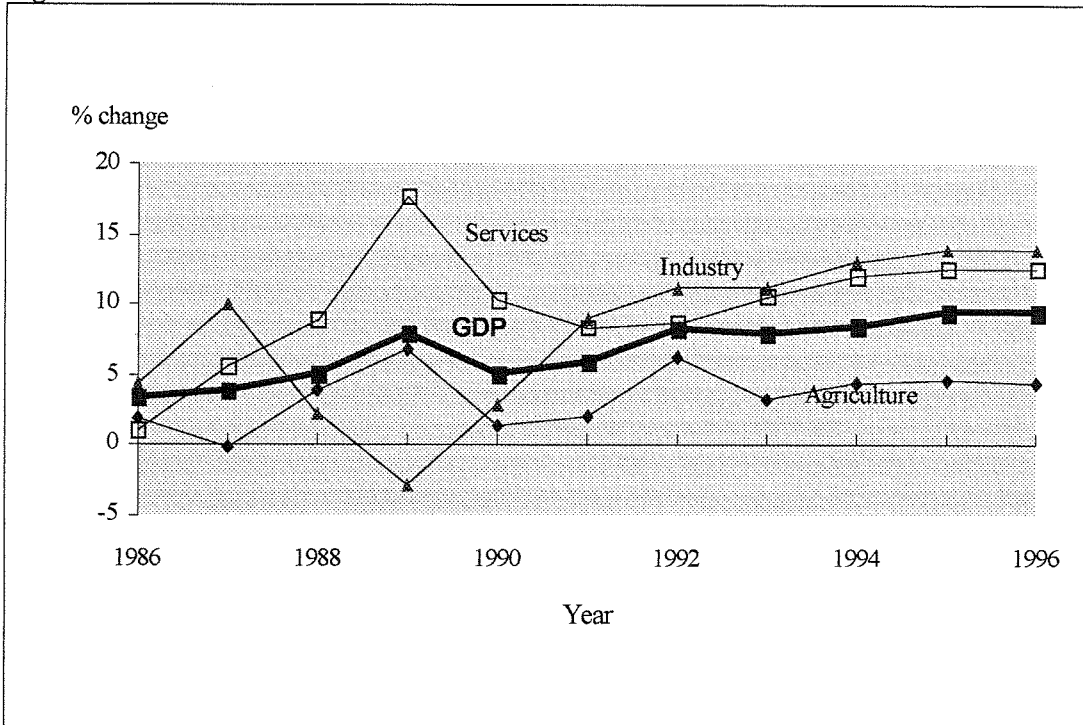
Despite the 'level playing field' objection, the number of registered private companies increased rapidly during the 1990s, from 770 in 1990 to nearly 25,000 by mid-1995 (compared with about 6,000 State enterprises). The private enterprises are mostly very small scale, but the numbers are continuing to rise, and the scale of operations of a number of these are beginning to become more substantial. Most of the former industrial and service sector co-operatives have been disbanded, but some have been reorganised as private enterprises. The number of individual or household business operations is estimated to have increased from 568,000 in 1986 to 835,800 in 1990, and 1,882,800 by 1995 (GSO, 1996). More generally, *doi moi* appears to have had an impact on the lives of the majority of the population in terms of increasing the supply of basic commodities, in particular food, clothing and shelter. Strong economic growth has contributed to marked improvements in per capita income over the last decade. Growth in *per capita* incomes have been reported throughout the country, but strongest growth has been recorded in urban areas. UNDP (1996) reports a reduction in the incidence of absolute poverty from 70 to 50 percent since

⁷ This is of course part of the 'level playing field' argument on which see Fforde (1995). The WB argues the SOEs have an unfair advantage in attracting FDI and that SOE privatisation has been minimal. As Fforde points out, had SOEs been privatised more rapidly, it is doubtful that as much FDI would have been forthcoming. Viet Nam's policy in this respect can be seen as a variant of the Korean strategy of attracting FDI to key industries privileged by Government.

the beginning of *doi moi*---a figure we think is too cautious.⁸ On the political side, rapid growth and higher incomes---particularly in the countryside---have been important in mobilising sustained support for the Party and the reform process.

These reforms have taken place despite the limited substantive changes in policy directions outlined in the Political Reports of the Party Congress over this period. These reports have all continued to stress the leading role of the State in economic development, but have been rather ambiguous about what that meant as regards the future structure of the Vietnamese economy. The 8th Party Congress documents do recognise a long term role for the private sector, whereas prior reports only recognised a role for the private sector in the transition period. However, given the range of possible interpretations of these documents, we believe that it is difficult to draw any strong conclusions about future policy directions from the Report of the 8th Party Congress.

Figure 1: Growth in GDP



⁸ The UNDP/UNICEF data is flawed in two respects. First, the figure of 70 percent refers to 1986; lack of accurate data at that time makes this little more than a guesstimate. Second, UNDP/UNICEF uses the same poverty line of 2100 calories per day as that used by World Bank (1994) based on VLSS data and adopts a 'headcount approach to measuring poverty. Moreover, Since the VLSS dataset is now five years old, it is most unlikely that the percentage of total population in poverty has not fallen since then. See Irvin (1995) for projections; the current figure is more likely to be of the order of 35-40 percent.

II. Selected Issues

How deep is the Commitment to Reform?

Some international observers have recently expressed concern about the Government's continuing commitment to reform. The political debates and delays in decision-making during the lead-up to the Eighth Party Congress contributed to such concerns. These concerns were reinforced by the high profile measures aimed at reducing "unhealthy" foreign influences (including actions against advertisers and the press), and corruption. Inconsistencies in policy making (eg, policies relating to land use, the property market, and bank operations), and frequent changes to policies directly affecting the potential viability of investments (eg, tax policies) have not helped. There were also a number of high profile disputes between foreign investors and local partners, and concerns about mechanisms for dispute resolution.

Despite these concerns, increasing inflows of FDI suggests that most major foreign investors---mainly East Asian investors---remain convinced of Viet Nam's economic potential with actual inflows of FDI at high levels as indicated in Table 5 in section 3. Viet Nam is a substantial market; its population of 72 million makes it the third largest East Asian NIE after China and Indonesia . Moreover, an increasing proportion of approved foreign investment is being directed away from property development to manufacturing activities, which are likely to have longer pay-back periods. Domestic private investment activity is increasing suggesting that the private sector has confidence in future economic prospects. The number of limited liability companies, and limited liability share holding companies, being registered continues to increase.

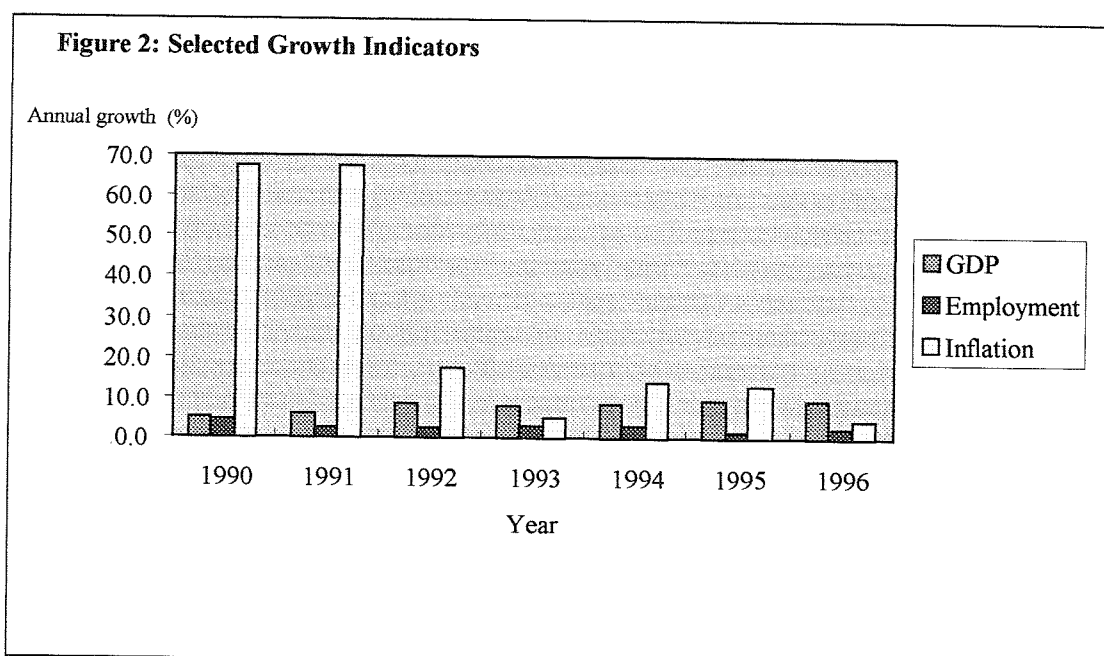
Distribution of Economic Growth and Poverty Alleviation

Since the introduction of *doi moi*, economic growth has been fairly broadly based with strong growth in coffee, tea, rubber, cashews, other industrial crops, horticulture, marine products and livestock in the agriculture sector; energy, construction materials, garments, footwear, foodstuffs, chemicals and electronic assembly in the industry sector; and in the service sector there has been strong growth in trade, tourism, finance and public services. While agriculture growth has been impressive by regional standards, the industry and service sectors have grown fastest as is apparent in Figure 1 above.

Given that 70 percent of the work-force is employed in agriculture, the more rapid growth of other sectors implies that there will be growing inequality in incomes between agriculture and non-agriculture workers unless agriculture workers can find non-agricultural employment. Employment growth in industry and services, particularly in rural areas, will be important in mitigating against

growing income inequality. The following table is not encouraging in this regard. Growth in formal employment has been much lower than economic growth and only marginally higher than population growth.

Government policy statements indicate that the reduction of poverty and the reduction of economic inequalities are important objectives. The key to achieving this will be the creation of non-agricultural employment in rural areas, implying increased investment in small and medium sized enterprises that are most likely to generate greater employment (and output) for a given level of capital. There are, however, contradictions between stated poverty alleviation objectives and a public investment plan (PIP) that includes substantial allocations to heavy industries such as cement, steel and oil refining that require large capital investments and generate minimal employment.



There is also concern about attempts to protect capital intensive industries through the continued use of import quotas and taxes. These restrictions are in effect a tax on unprotected sectors, including many light industries, which are likely to generate the greatest employment. Equally, there is concern about lobbying efforts of some foreign investors, together with their SOE joint-venture partners, to secure protection from competition. Unlike South Korea, Viet Nam has made no effort to link old-style ISI to export growth by making the protection to domestic enterprise conditional upon their meeting export targets.⁹ Clearly, the problem of inefficient commercial policy will need to be tackled if Viet Nam is to implement the stringent goals of

⁹ The best account of South Korean industrialisation strategy remains Amsdem (1989).

tariff reduction quota elimination envisaged in ASEAN's commitment to completing the Asian Free Trade Area (AFTA) by the middle of the next decade.¹⁰

Savings and Investment

As noted earlier, FDI has been a major factor in recent growth. National investment has almost doubled in the last five years to almost 30 percent of GDP. Most of this growth has been financed from rapid increases in foreign savings, with sharply increased inflows of FDI and, to a lesser extent, ODA. However, there is some concern about the level of commercial foreign borrowings, with implicit or explicit government guarantees.

Government savings and investment have also increased as a result of improved revenue performance. However, while private domestic savings have increased in absolute terms, the ratio of private domestic savings¹¹ to GDP has remained unchanged at around 13 percent. Reported private domestic savings (and investment) remain low compared with other East Asian economies. This partly reflects under-developed market institutions, continuing suspicions about official institutions and continuing preferential treatment to State enterprises and foreign investment. If recent high growth is to be sustained, greater emphasis will need to be given to addressing these issues and increasing private domestic savings. Domestic private investment will be much more likely to be directed to small and medium size enterprises that are likely to generate a higher incremental output (and employment) for a given level of capital investment.

Table 3: Economic Growth in Selected Countries (percent per annum)

	1991	1992	1993	1994	1995	Annual average (1991-95)	1994 per capita GDP USD
Viet Nam	6.0	8.7	8.1	8.8	9.5	8.2	215
Indonesia	8.9	7.2	7.3	7.5	7.6	7.7	880
South Korea	9.1	5.1	5.8	8.4	9.2	7.5	8220
Laos	4.0	7.0	5.9	8.1	7.1	6.4	320
Malaysia	8.6	7.8	8.3	9.2	9.3	8.6	3520
Myanmar	-0.6	9.7	5.9	6.8	7.7	5.9	235
Philippines	-0.6	0.3	2.1	4.4	4.8	2.2	960
Thailand	8.5	8.1	8.3	8.7	8.6	8.4	2210

Source: ADB, *Asian Development Outlook*, 1996.

¹⁰ The AFTA agreement was signed by ASEAN countries in 1992. For a recent study of the impact of trade liberalisation on Viet Nam, see Vu Quoc Huy *et al* (1996).

¹¹ GDS is defined as GNS minus the sum of net factor payments and transfers, government current savings and foreign savings.

III. Recent Economic Performance in a Regional Perspective

Viet Nam has recorded an average growth rate just above the average rate for all Southeast Asian countries during the last five years. During this period Viet Nam's economy, as measured by the country's Gross Domestic Product (GDP), has grown at a similar rate to that achieved by Thailand and Malaysia, and well above the Philippines and Myanmar.

Viet Nam has moved rapidly from a closed economy to an increasingly open economy. External trade and foreign investment flows as a percentage of gross domestic product (GDP) now compare favourably with that of Viet Nam's rapidly developing neighbours. Annual export growth averaged 25 percent from 1991 to 1995, compared with 20 percent in Thailand and 16 percent in the Philippines¹². However, this was initially from a low base. Exports from Viet Nam amounted to USD 3.6 billion in 1994 compared with exports of almost USD 13.4 billion from the Philippines and almost USD 45 billion from Thailand. In contrast, exports from Myanmar amounted to less than USD 0.4 billion in the same year. Viet Nam's exports growth remains strong with exports projected to reach USD 6.8 billion in 1996.

Table 4: Growth of Trade in Selected Countries (percent per year)

	1991	1992	1993	1994	1995	Average annual (1991-95)	Total Value (1994) USD billion
<i>Exports</i>							
Viet Nam	18.0	21.2	15.2	26.3	45.0	25.1	3.6
Indonesia	10.5	14.0	8.3	9.9	11.1	10.8	40.2
Malaysia	17.0	18.1	16.1	23.1	26.6	20.2	56.9
Myanmar	11.1	25.6	10.8	7.6	8.0	12.6	0.4
Philippines	8.0	11.1	15.8	18.1	28.9	16.4	13.4
Thailand	23.8	13.7	13.4	22.2	24.5	19.5	44.5
<i>Imports</i>							
Viet Nam	18.8	20.4	38.3	28.4	58.3	32.8	3.3
Indonesia	15.7	7.8	6.0	13.9	23.1	13.3	32.3
Malaysia	26.8	10.1	17.8	28.1	30.6	22.7	55.3
Myanmar	-42.5	18.5	8.8	0.5	9.0	-1.1	0.4
Philippines	-1.3	20.5	21.2	20.7	24.4	17.1	21.2
Thailand	15.8	6.0	12.1	18.5	28.4	16.2	44.4

Sources: Viet Nam General Statistical Office; ADB *Asian Development Outlook* 1996.

¹² Major exports include crude oil, garments, marine products, rice, footwear, coffee, cashew nuts and coal. Major imports are petroleum products, machinery, vehicles, fertilizers, construction materials, and consumer goods. East Asian countries, including Japan, Singapore, South Korea and Hong Kong are Viet Nam's major trading partners.

As previously noted, inflows of Foreign Direct Investment (FDI) to Viet Nam have increased sharply in recent years¹³, with other East Asian economies the dominant source of investment. FDI inflows to Viet Nam during 1995 were high, even relative to other Southeast Asian countries, and the WB/IMF estimate a further increase to USD 2.3 billion during 1996. While foreign investors face many difficulties operating in Viet Nam -- especially during project start-up---major investors have subsequently expanded operations beyond the levels initially planned and approved. Given the continuing high levels of approvals, the ratio of FDI inflow to GDP is likely to remain high during the coming years.

Are Viet Nam's capital inflows sustainable? They would be unsustainable if, for example, they led to growing foreign indebtedness, a debt service problem with a build-up in arrears. While it is true that Viet Nam inherited substantial unpaid debt in the form of unpaid syndicated loans extended to the South in the 1970s, in May 1996 agreement was reached with the London Club covering most of this.¹⁴ The ratio of interest and amortisation payments to exports has been falling since 1990 and is now about 11 percent, a figure which gives no cause for alarm. The supply of private and public foreign savings thus seems more likely to rise than to fall.

Table 5: Foreign Direct Investment (FDI in millions of US dollars)

	1989	1990	1991	1992	1993	1994	1995
<i>Viet Nam</i>							
Total Value FDI Projects Approved 1/	539	600	1223	1937	2800	4071	6616
IMF/WB est. of FDI inflows 2/	100	120	220	260	832	1048	1781
<i>Other SE Asia FDI Inflows</i>							
Indonesia	682	1093	1482	1777	2004	2109	na
Malaysia	1668	2332	3998	5183	5006	4348	na
Philippines	563	530	544	228	763	1126	na
Thailand	1775	2444	2014	2116	1726	640	na

Sources: 1/ Ministry of Planning & Investment;

2/ WB/IMF. Other country data from ADB; *Asian Development Outlook* 1996. In addition to FDI, the other SE Asian nations have also received increasing levels of portfolio investments in recent years.

A more difficult question is that of the sustainability of a the trade deficit equal to about 10 percent of GDP. In fact, the trade deficit must be understood in part as accommodating

¹³ Major sources of FDI approvals to mid-November 1996 were Taiwan (USD 4.1 billion), Japan (USD 2.7 billion), Singapore (USD 2.5 billion), Hong Kong (USD 2.4 billion), and South Korea USD 2.3 billion).

¹⁴ The London Club agreed to a debt reduction package worth USD 900 million amounting to half the outstanding total (World Bank, 1996: 18). Much of the rest of the country's outstanding debt is to the FSU and is currently being renegotiated with the Russian Federation, the crucial issue being that of agreeing on a Rouble exchange rate.

the large inflow of ODA and FDI; ie, the trade gap merely reflects the foreign savings 'wedge' between total investment and domestic savings. It is 'unsustainable' only to the extent that its composition shifts from intermediate inputs to consumption goods imports in excess of export earnings. While there is some concern that this might be happening, government has reacted by tightening fiscal policy such that the current budget is expected to go into surplus in 1997 (World Bank, 1996). The greater challenge now seem to be increasing the micro-efficiency in the SOE sector, improving the country's ODA 'absorptive capacity' and accelerating the modernisation of financial institutions responsible for private domestic savings mobilisation.

IV. Concluding Remarks

While some aspects of reforms have moved ahead at a slower rate than some observers expected and/or may have considered desirable, a review of the past decade leaves little doubt that the reforms already implemented have been substantive. Reforms have contributed to marked improvements in macro-economic stability and growth in output, trade, and inflows of foreign direct investment. Economic growth during the last five years compares favourably with that of other ASEAN economies and the newly industrialising countries. Nevertheless, Viet Nam has still a long way to go if it is to 'catch-up' with other ASEAN economies in terms of output, trade and capital stock *per capita*.

The country has moved from a situation where reforms tended to be crisis driven, to a one where the authorities are beginning to develop a longer term vision of where the country is heading. While there continues to be a risk of an economic downturn, the risk of economic collapse that existed at the time of the Seventh Congress appears to have been averted. This has provided the scope for greater consistency and predictability in policy making. It also has provided an opportunity for various interest groups to be better organised, and in some cases this may imply the need for greater efforts to 'sell' reforms. This means improved capacity is required to undertake more sophisticated analysis of the distribution of the costs and benefits of proposed reform measures.

The nature of Viet Nam's requirements is also changing. In order to sustain medium to long-term growth, there is need for a greater focus on institutional reforms and development. Some key medium-term challenges include: financial sector development to improve domestic resource mobilisation and allocation; further progress towards a more consistent regulatory framework or 'levelling the playing field' for all economic sectors in order to achieve increased and more efficient commercial investment; further reducing institutional constraints to small and medium

enterprise development with the aim of ensuring more equitable distribution of the benefits of growth; improving corporate governance systems for State enterprises; increasing competition faced by remaining monopolies; further trade liberalisation, especially in reducing barriers to entry to external trade; accelerating implementation of committed programs and projects to improve education, training, and other social services; and, accelerating the development of physical infrastructure. There is still much to be done to develop the institutions required to support a market economy, including capital market institutions, accounting and other professions, and to strengthen the legal framework and enforcement mechanisms for protection of property rights and commercial activity.

More generally, there remains need for further public administration reform to streamline decision making authority and to clarify and enforce established lines of authority and accountability. Regulations need to be simplified to reduce the administrative discretion presently exercised by some government agencies in order to reduce incentives and opportunity for corruption, and to generally reduce the transaction costs of undertaking business activities in Viet Nam.

Party and Government documents include commitments to reforms in many of these areas. While past experience suggests that progress in addressing the issues will be gradual, the probability of maintaining strong growth (7-10 percent per annum) over the next 2-3 years remains high, given the already approved pipeline of investment projects. Over the longer-term, prospects for sustained strong growth depends on sustaining current progress in developing market institutions. In short, the economics of the project are hardly in doubt. What continues to be underestimated by all sides to the debate is the time required to build the firms foundations of a genuine market economy, a process in which what Fforde has called the 'breakout' of 1988-89 was only one signpost along a long road.

References

- Amsden, A. (1989) *Asia's new giant: South Korea and late industrialisation* New York and Oxford: OUP.
- Asian Development Bank (1996) *Asian Development Outlook 1996 and 1997*, Hong Kong: OUP.
- Forbes, D.K. et al. eds (1991) *Doi Moi: Vietnam's renovation and performance* Political and social change Monograph 14, Research School of Pacific Studies, Canberra: ANU.
- General Statistic Office (1996) *Impetus and Present Situation of Viet Nam Society and Economy after Ten Years of Doi Moi*, Hanoi: Statistical Publishing House.
- GOVN (1996) *Development and Official Development Assistance in the Period of Strongly Promoting Industrialization and Modernization in Viet Nam*, Government of Viet Nam: Government Report to Consultative Group Meeting, Hanoi.
- Hiebert, M. (1996) *Chasing the Tiger New York*: Kodansha International
- IMF (1996a) *Viet Nam: Transition to a Market Economy* Washington, DC: IMF
- IMF (1996b) "Vietnam---Recent Economic Developments" *IMF Staff Country Report* No. 96/145, Washington DC, December.
- Irvin, G W (1995) 'Vietnam: will market transition increase poverty?' *ISS Working Paper* No 200, May.
- Irvin, G W (1996) 'Emerging issues in Viet Nam; privatisation, equity and sustainable growth' *European Journal of Development Research*, Vol 2, No 8, December.
- Le Dang Doanh (1990) 'Economic renovation in Vietnam: achievements and prospects'. Paper presented at the conference on *Doi moi, Vietnam's economic renovation* held at the Research School of Pacific Studies, Australian National University, 19-21 Sept. 1990.; reprinted in Forbes et al, 1991
- Mallon, Raymond (1996a) *Review of State Enterprises: Policy Developments, Achievements and Remaining Constraints* Draft report prepared for the Asian Development Bank, Hanoi, May.
- Mallon, Raymond (1996b) "Doi Moi and Economic Development in Viet Nam: some general comments", discussion paper presented at the *Vietnam Update Conference*, ANU (Canberra), December
- Schwartz, A. (1995) "The Honeymoon is Over" *Far Eastern Economic Review*, 13 July.
- Truong, D.H.D. and C. Gates (1992) 'Effects of Government policies on the incentive to invest, enterprise behaviour and employment: the case study of Vietnam' *World Employment Programme Research Paper* No. 57, Geneva: March.
- UNDP/UNICEF (1996) *Catching Up: Capacity Building for Poverty Alleviation in Viet Nam* Hanoi: UNDP.

VET (1996) "Corruption: Vietnam clamps down" *Vietnam Economic Times*, issue 35, March.

World Bank (1995a) *Viet Nam: Economic Report on Industrialization and Industrial Policy*; Report No 14645-VN: Washington DC: October 17.

World Bank (1995b) *Viet Nam: Environmental Program and Policy Priorities for a Socialist Economy in Transition* Report No.13200-VN, Washington DC: February 27. (Vol 1 of 2)

World Bank (1996) *Viet Nam: Fiscal Decentralization and the Delivery of Rural Services*, Report No. 157435-VN, Washington DC: October, 31.