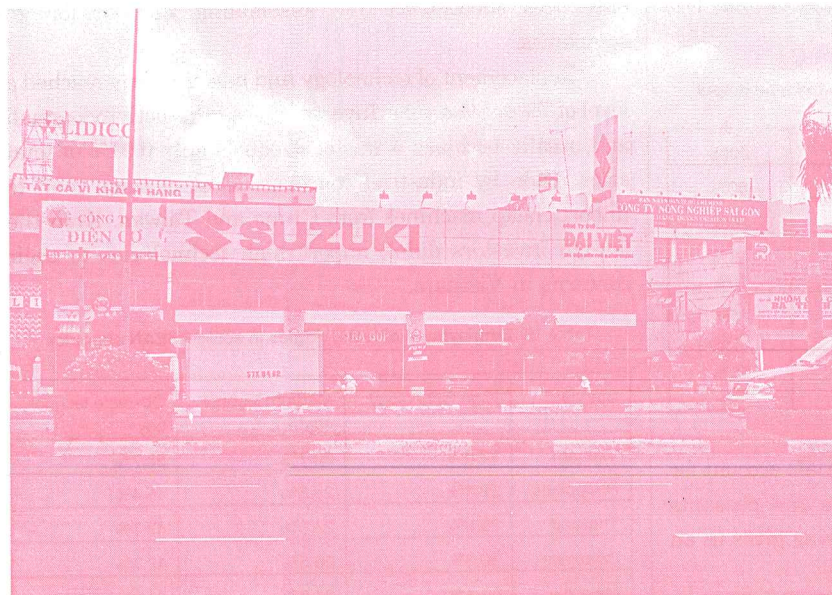


# On the Vietnam's Economic Reform During the Global Integration

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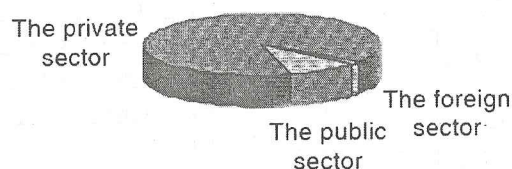
In the past two decades after the economic reform, Vietnam has become one of countries with high growth rates (some 7.1% a year), second only to China (9.2%). Vietnam is also considered as successful in poverty alleviation and limiting negative effects of the economic development. It still, however, faces many difficulties: low personal income, high proportion of poor families to the population, and low ranking in terms of Growth Competitiveness Index (81/117 countries in 2004-05). This means that Vietnam could fall farther behind if it fails to accelerate its reforms.

Table 1: Personal income in Vietnam and some other countries (US\$)

Country	Personal income
Japan	37,050
Australia	27,070
Singapore	24,760

South Korea	14,000
Malaysia	4,520
Thailand	2,490
China	1,500
Philippines	1,170
Indonesia	1,140
Vietnam	540
Laos	390
Cambodia	350

Figure 1: Distribution of labor over sectors



## 1. Role of the State and public sector in the market economy

Vietnam has committed to developing a market economy with a

“socialist orientation” – a model in which the public sector plays the leading role. In fact, this sector comprised only some 12,000 companies at the beginning of the economic reform and this figure fell to some 4,000 but they still hold 75% of the national fixed assets; 50% of public investment and 60% of credit supplied by banks. This sector, however, accounts for only 40% of the GDP and provides jobs for only 10% of the working population (see Figure 1).

Most assets in the public sector are held by major companies and many of them could only make some profits because they are government monopolies (in air transport, oil, power supply, telecommunications, etc.). Without subsidies, state-owned companies meet with a lot of difficulties in competing rivals from other sectors. According to the WB in 2003, 59% of state-owned companies gained a profit on capital rate of 5% or lower (while the bank interest rate was 7%-8% a year). Their performance is much lower if values of land and credits as favors they enjoyed are taken into consideration. These favors cause troubles for companies in other sectors and hinder strengths of the market economy, which explains why Vietnam wasn't recognized as a market economy 20 years after its economic reform, and its exports are considered as subsidized ones on which anti-dumping taxes could be imposed.

Generally, problems with the public sector have been dealt with by two measures: equitization (privatization of Vietnamese style) and promulgation of the 1999 Companies Act

that aim at encouraging the private sector. Better performance of equitized companies and boom in the private sector from 2000 on are encouraging



signs of positive changes in the structure of industry. In 2005, the new Companies Law applied to all sectors could be seen as an effort to remove discrimination of all kinds. There is also a decision that forces all state-owned companies established according to the 2003 State-Owned Companies Law to get equitized within four years after the law became effective from July 1, 2006.

In short, although the public sector played the leading role as a legacy of the centrally-planned economy in the first days of the economic reform, it has since contracted when the market economy increasingly integrates into the world community. This is a positive and inevitable change that brings the State to a new space with challenges it should face.

Firstly, the then-35% of the budget income from the public sector will reduce when more and more state-owned companies are equitized. The situation is more serious when customs duties, which account for some 20% of the budget income, are cut as required by multilateral trade agreements. In addition, the system of tax agencies lacks ability to operate in the market economy and it needs basic reforms to ensure effective and reasonable taxation, especially when it has to deal with private persons and organizations.

When the whole economy is not under direct control of the State, a system of laws that regulate all economic activities is much needed. This means that the professionalism of the legislative and executive branches must be beefed up and experience from developed countries absorbed.

Regarding the state control over the public sector and partly-equitized companies, the decision to develop powerful groups of companies is a double-edged weapon. The main objective of the formation of groups is

to gain the economies of scale and improve their competitiveness and performance. Based on this principle, the formation of state-owned groups can help beef up their competitiveness. However, they could become monopolies that hinder competition from other sector or cause damage for consumers.

The past experience shows that it's hard to dissolve major state-owned companies even if their performance and competitiveness are poor, which leads to long lasting and disastrous consequences including huge bad debts and redundancies. In other cases of companies that make profit by taking advantages of favors from the State, their directors could commit embezzlement without being punished provided that their companies still earn some profits. To deal with this situation, it's necessary to beef up the mechanism for controlling personnel and financial issues of state-owned companies and struggle against monopoly and abuse of power. To reduce pressure on the budget expenditure, the government had better accelerate the equitization program.

## **2. Corruption and management machinery**

The biggest obstacles to the economic growth in the first stages of development in emerging economies are corruption and poor performance of the administrative machinery. The corruption is not new to Vietnam but many people are of opinion that it has become widespread, serious and systematic. Although the monthly salary is around two or three million, many civil servants can afford expensive motorbike, car, beautiful houses and even expenditures for their children to make study abroad. Until recently, many cases of corruption in high places have been in the press and TV. According to official reports from the inspection bodies in 2002, these

cases involved VND2,739 billion and 12,512 hectares, and "such cases are only the tip of the iceberg."

The corruption, comprising both embezzlement and taking of bribes, produces negative effects on the economic development. Economically, it causes the production cost to rise, which leads to poor competitiveness. Domestically, the corruption leads to unfair competition. Companies that give bribes to avoid taxes can offer selling prices lower than ones offered by their rivals. The corruption makes investors worry about the business opportunities and makes the business climate less attractive. It also leads to social injustice and poor performance of the state control.

We should get to the root of the problem when dealing with this social evil. It is the unreasonable scale of salary for civil servants in comparison with ones offered by other sectors. In the market economy where labor is considered as a commodity, it's unreasonable to expect civil servants to try their best to do the jobs for a monthly salary of two or three million đồng. Rises in pay for civil servants, however, certainly lead to huge budget deficit and high inflation rate, or serious cuts in the payroll and then, higher unemployment rates. It seems that the administrative machinery fails to carry out its reform in this aspect. In 2004 for example, some 13,000 laborers in its workforce was cut and it recruited some 60,000 new ones. Thus, the corruption is inherent in ineffective administrative machinery, and the struggle against the corruption must be linked with the administrative reform. From some recent cases of corruption we can work out some feasible measures to deal with them.

- Delegating more power and duties to the anti-corruption and inspection bodies (the PM acting as the head of the Anti-Corruption Agency is a right decision under current conditions).



- Beefing up the role of local people's committees and courts in order to expand the army of inspectors and supervisors.

- Making and enforcing effectively the Anti-Corruption Law.

- Beefing up the role of the press and information service as a means of mobilizing the public to support this struggle.

These measures, however, could produce some immediate results but they are not long-term ones if treatment for civil servants is not improved. In addition, the struggle could meet with difficulties caused by the old mechanism in which certain persons couldn't be dealt with because they are under direct control of the central government or VCP Central Executive Board. This mechanism seems unable to cope with such shocks as the PMU18 case. The task of dealing with them depends more on determination of the leadership than on efficiency of the system.

### 3. Human resource and competition for the global integration

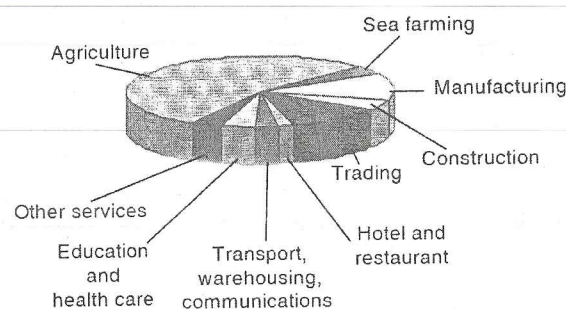
Material resource that has played an important role in the economic growth in the past two decades, thinking through, is only a necessary condition for the development. With globalization and free trade, it is not too difficult to secure capital and technologies from foreign sources. This means that the decisive factor in the competitiveness of a nation is its human resource. The boom in foreign investment in Asia in the past few decades shows that the human resource has become the most important influence on investors' decision.

Regarding the human resource, Vietnam has a big population and high human development index (ranking 108 among 177 countries according to the UNDP). According to the Ministry of War Invalids and Social Affairs, three quarters of the

working population are untrained. To reach the full potentials of the labor force, developing its quality must be considered as the strategic task.

Regarding the distribution of labor, the agriculture still employs the better part of the working population (55%) although it accounts for only 18% of the GDP. To improve this situation, it's necessary to mechanize the agricultural production and make plan to train rural residents in various occupations with a view to avoiding large redundancies. In fact, the flow of migrants to industrial estates and big cities for work is on the increase. The Government should consider it as an opportunity and launch programs to train this army of laborers in order to ensure sustainable development for the manufacturing and service sectors.

Figure 2: Distribution of labor over industries



Experience from 20 years of the economic reform shows that the market economy can bring about goods and services of better quality and lower prices in comparison with what offered by the centrally-planned economy. Why don't we improve the public services by letting them open to market forces? In fact, thousands of billion đồng have been invested in the program to develop the e-governments but only a few governmental bodies recruit employees through their websites. It's rare to see want ads offering vacancies put by official organizations or state-owned companies on the press. Many people are of the opinion that they only

recruit persons who have good relations with their leaders and meet political standards (being a VCP member for example). Along with poor salary, the nepotism in recruitment is also a big obstacle to the administrative reform. The analyses allow us to see necessary measures to improve the human resource for the administrative machinery:

- Making processes of recruiting and controlling civil servants parts of the law in order to prevent the nepotism.

- Requiring official organizations and state-owned companies to publicize their policies on recruitment through mass media.

- Limiting requirements about political background when recruiting civil servants and replacing them with

ones about knowledge, expertise or merits.

- Setting limits on the payroll and encouraging various kinds of employment (short-term contract, outsourcing, etc.) in order to save expenditures and secure experts' services.

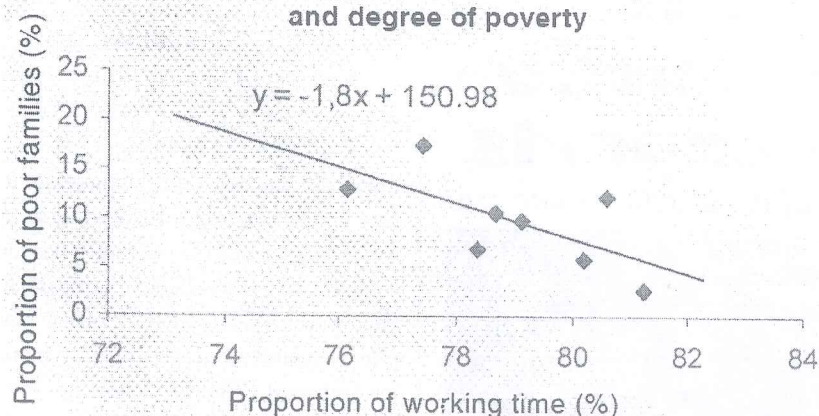
### 4. Poverty alleviation

One of the biggest achievements in the past two decades is to reduce the proportion of poor families from 57% in 1993 to some 20% in 2005. This is a striking result but the proportion of poor families is still high and requires more efforts in the coming years. It's worth noting that the economic growth doesn't mean bread for everybody because nothing can ensure all classes will enjoy the same improvements in their living standard. In fact, high growth rates usually result in wider gap between the rich and the poor. Thus, the poverty alleviation must be central to all development strategies.

Some 90% of poor families are in



**Figure 3: Relation between working time and degree of poverty**



rural areas and live on agriculture, so agricultural development is the main solution to the poverty problem. The biggest obstacles to this solution are low productivity caused by a small-scale production and shortage of capital. The mechanization in the agriculture requires accumulation of land and supply of low-interest credit. Those two conditions in their turn depend a lot on efforts by the Government.

Another factor affecting the productivity is the poor scientific research and dissemination of techniques among peasants. As a result, Vietnam ranks fourth in terms of sales of rice although it is the world's second largest exporter of rice because the productivity is closely linked with quality and production cost.

In addition, there is a relation between poverty and working time in the agricultural production. At present, the average proportion of working time in Vietnam is 79%. The Figure 3 presents the relation between the working time and degrees of poverty in eight regions in Vietnam and shows that the poverty proportion will reduce by 1.8% when the proportion of working time increases by 1%. This means that more subsidiary occupations must be introduced to rural areas to reduce time of idleness among peasants.

Another feature of the Vietnamese agricultural production is the important role of farming in comparison with processing of farm products and generating of added value. Three direct consequences of this feature are the low value of the output, high degrees of risk for export of farm products because of unre-

state-owned farm products processing factories and encourage private and foreign investment in this field. The infrastructure in rural areas in recent years has helped improve the living conditions there and reduce the production cost. To make the best use of the improved infrastructure, it's necessary to increase the investment in production and processing of farm products in rural areas.

The last issue to take into consideration is the ability of peasants to deal with natural disasters. Damage caused by natural disasters in Vietnam equals some 2% of the GDP every year (some VND120,000 billion). This figure is small as compared with the GDP but the damage usually concentrates in the poorest provinces, which limits results of the poverty alleviation programs.

Achievements in the past are



dictable changes in prices on the world market, and negative effects of unstable supply of farm products.

In recent years, the farm products processing business have developed in many provinces but it still has a long way to go to meet the market demand. In the coming years, the Government had better equitize

encouraging but they mainly come from efforts to remove obstacles built up by the old mechanism and liberate the productive forces. In the coming years, more reforms in all fields are much needed to ensure very high growth rates and bridge the widening gap between Vietnam and other developing countries ■