Challenges to the Reform in Vietnam's Foreign Trade

by TRƯƠNG QUANG HÙNG

The reform in the foreign trade in Vietnam started in 1986 with two main objectives: adapting to the market economy and free international trade; and promoting the export. The reform produced many encouraging results:

- The number of companies engaging in this business increased from some 30 in 1988 to 17,200 in 2003.
- Some import barriers were removed and incentive scheme for export was introduced.
- The exchange rate system was liberalized.

In spite of deregulations, companies in the public sector still enjoy preferential treatment. The import subsitution policy, protection for local goods and State control over the foreign trade still have great effects. To beef up the public sector, the Government has carried out a protectionist polict since the 1990s and increased investment in this sector. This effort made state-owned companies stronger but could also turn them into obstacles to the reform in the foreign trade according to the market economy when this sector has poor performance.

Up to now, the reform in the foreign trade has become a matter of great urgency because Vietnam promised to remove all trade barriers by 2006 as required by the AFTA agreement. The current problem is how to carry out the trade liberation to best serve the economic growth. It seems to us that there is a contradiction in Vietnamese policies. On the one hand, Vietnam is trying to liberate the foreign trade while keeps giving priority to import-substitution industries run by state-owned companies on the other hand. This contradiction could make policies hard to predict and discourage both foreign and local investors. Will investors believe the Government is determined to liberalize the foreign trade while it gives priorities to companies of poor competitiveness?

This discrimination reflects itself in the rates of import duties for example. Duty rates are low on input needed for import-substitution industries where state-owned companies account for the best part. This policy leads to great losses caused by ineffective allocation of resources. Great volumes of capital flow to these prioritized industries because they are protected well instead of being industries of high competitiveness.

The reform in the foreign trade according to the AFTA and BTA requires changes in the structure of state-owned companies and commercial banks. According to the AFTA, taxes on most categories should be reduced to the 0-5% bracket by 2006. This will affect badly the public sector and the manufacturing industry because the protectionist policy is removed. Perhaps the Government will keep financing state-owned companies in the hope that they will soon improve their competitiveness.

This approach isn't good because: (1) causing waste of money when subsidizing loss-making companies; (2) causing burdens on state-owned banks when they are forced to finance these companies while they are badly in need of reform.

Results of the reform also represent problems. The reform in the foreign trade leads to changes in market prices and allocation of resources among industries. What is inevitable is increases in the unemployment rate during the first stage of reform. The reform can also cause trade deficit when the import rises and duties are cut. That is why Vietnam has to work out an appropriate policy on the exchange rate.

The next problem relates to social and environmental issues. The liberalization of foreign trade will increase the unemployment rate and change the redistribution of wealth. And poverty will produce bad effects on the environment.

How Vietnam carries out the industrialization when policies on the foreign trade and exchange rate stop protecting local industries? It seems to me that the industrialization in such conditions is based mostly on the policy on the industrial development. Attracting foreign investment is the best way to disseminate new technologies, thereby improving the competitiveness of the whole economy. However, this task becomes more difficult because all regional countries are competing for foreign investment. Vietnam has certain advantages in attracting the FDI (low labor cost, good geographical position, and political stability). But these advantages aren't tapped properly because of unstable policies and poor infrastructure.

Challenges to the reform are numerous and Vietnam is running short of time. Bold policies are needed to deal with them and save us from falling farther behind neighboring countries.■