

Problems with Vietnam's Growth Model in 1991-2010 in Retrospect

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ABSTRACT

Restructuring the economy and adopting a new growth model are topical issues that attract great attention currently. The paper tries to provide a panoramic view over Vietnam's growth model in the past two decades.

The growth model Vietnam has been building seemed suitable at first but becomes unsuitable when facing demands from the domestic economy and challenges posed by economic integration in the context of global competition. What are characteristics of the growth model adopted by Vietnam? What consequences has it produced? What are characteristics of an expected model and how can it be realized? These are questions that the paper wants to discuss to a certain extent.

Keywords: Growth model, restructuring, sustainable development, capital, labor, natural resources.

1. CHARACTERISTICS OF THE PRESENT GROWTH MODEL

a. An extensive development based on capital, labor and natural resources:

The gross investment as percentage of the GDP in Vietnam rose steadily over years from 15.7% in 1990 to 41.8% in 2010 (2.85 times). Compared with Southeast Asian countries and developing economies in the world, Vietnam's ratio of gross investment to the GDP is the highest (Lê & Nguyễn, 2006, p. 13).

According to a study conducted by Statistics Institute under the GSO (Thời báo kinh tế Việt Nam, 2011, p. 8), capital accounted for 57.5% of economic growth in 2001-2005, that is, increases in gross investment made the GDP rise by 4.32% a year. Another study used for drafting the Socioeconomic Development Strategy for 2011-2020 (op. cit.) found that the gross investment explained for 55% of the economic growth in 2006-2010, that is, increases in investment made the GDP rise by 3.86% a year. It is thus apparent that the gross investment has played a decisive role in the economic development in the past decade.

Regarding the labor, Vietnam enjoys a huge and increasing labor force. Its working population rose from 28.79 million in 1991 to 49.45 million in 2010 (Thời báo Kinh tế Việt Nam, 2011; GSO). Roughly one million people on average join the working population every year while unemployment rate in both rural and urban areas fell gradually.

The two aforementioned sources also report that the labor accounted for 20% of the economic growth in 2001-2005, that is, the increased labor force made the GDP rise by 1.5%. The two figures for the years 2006-2010 were 20% and 1.4% respectively, demonstrating important contribution from the labor to the GDP.

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The Vietnamese economic growth still depends greatly on exploitation of natural resources and production of raw materials. Crude oil alone accounts for over 20% of the GDP. Exports of unprocessed farm products, such as rice, vegetables, cashew nut, coffee, tea, black pepper, rubber and cassava, and minerals such as oil, coal, tin, and bauxite played an important role in the national economy. Structure of exports has experienced almost no change for years and the aforementioned exports still account for a large share in export earnings.

Such extensive development produced high growth rates in the past two decades.

Table 1: Vietnam's growth rate in 1991-2010

Year	Growth rate	Year	Growth rate	Year	Growth rate
1991	5.81	1998	5.76	2005	8.44
1992	8.70	1999	4.77	2006	8.23
1993	8.08	2000	6.80	2007	8.46
1994	8.83	2001	6.90	2008	6.31
1995	9.54	2002	7.08	2009	5.32
1996	9.34	2003	7.34	2010	6.78
1997	8.15	2004	7.79		

Source: Thời báo kinh tế Việt Nam, 2011

Except for some recession in the years 1998-1999 caused by the Southeast Asian monetary crisis and in 2008-2009 by the global financial crisis, the Vietnamese economy enjoyed pretty high and stable growth rates.

b. Low quality of economic growth:

Regarding the growth quality, however, the Vietnamese economy reveals many shortcomings and fails to ensure sustainability, which is evident in the following facts.

- Low efficiency at all levels and in all industries:

Vietnam's ICOR increases incessantly, that is, more and more capital is spent to gain the same growth rate. In other words, investment efficiency is low and decreasing steadily.

Table 2: Vietnam's ICOR

Year	ICOR	Year	ICOR	Year	ICOR
1991	3.0	1998	4.7	2005	4.9
1992	2.6	1999	5.5	2006	5.1
1993	3.7	2000	5.1	2007	5.5
1994	3.4	2001	5.2	2008	6.6
1995	3.1	2002	5.3	2009	8.0
1996	3.1	2003	5.4	2010	6.2

1997	3.8	2004	5.2		
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Source: Author's calculations based on data from GSO (2009) and Thời báo kinh tế Việt Nam (2011)

Regarding the labor force, its productivity is also very low. Calculations based on comparative prices show that the labor productivity in Vietnam rose over years, but it was very low in comparison with that in surrounding countries. Set Vietnam's productivity equals 1, then Indonesia's is 1.24; the Philippines' 2.68 and Thailand's 6.15 (Nguyễn & Trần, 2006, p. 103).

The economic inefficiency is also evident in high production cost. Particularly, business performance is very low in state-owned companies in comparison with their counterparts in non-public sectors. Extremely low pre-tax rate of return can be found in such state-owned enterprises as Building Materials Corporation (0.18); Shipbuilding Industry Corporation (0.42), Civil Engineering Construction Corporation (0.45), and Vietnam Textile & Garment Corporation (0.8) (Thời báo Kinh tế Việt Nam, 2007, p. 19).

- Poor competitiveness at all levels:

At the national level, the WEF reports that Vietnam's competitiveness is rather low in spite of its economic achievements. In 2010, its rank in terms of competitiveness was up 16 steps but it is still much lower than neighboring countries.

Table 3: Rankings in terms of competitiveness of Vietnam and some Asian countries

Country	2008	2009	2010	Country	2008	2009	2010
1. Singapore	5	3	3	7. China	30	29	27
2. Japan	9	8	6	8. Brunei	39	32	28
3. Hong Kong	11	11	11	9. Thailand	34	36	38
4. Taiwan	17	12	13	10. Indonesia	55	54	44
5. South Korea	13	19	22	11. Vietnam	70	75	59
6. Malaysia	21	24	26	12. Philippines	71	87	85
				13. Cambodia	109	110	109

Source: World Economic Forum (2010)

In the past three years, Vietnam's competitiveness ranks 11th among 13 South Asian countries (Myanmar and Laos are not ranked). It is only higher than the Philippines and Cambodia.

According to WEF estimates, five factors that affect badly Vietnam's competitiveness and business climate are: inefficient administrative machinery, corruption, poor technical infrastructure, shortage of skilled labor and poor financial access.

At the corporate level, the competitiveness is also low because most Vietnamese enterprises have small size, small capital, old technologies, and poor managerial skill. When ratios of return rate to capital and to revenue are used for assessing their competitiveness, these ratios are very low, especially among state-owned and local private enterprises.

Competitiveness of Vietnamese products, for sale either in domestic or foreign markets, is low too. Concerning products for domestic markets, their quality and price are high, and they can hardly compete against imports. According to the National Committee for International Economic Integration (Nguyễn & Trần, 2006, p. 115), prices of Vietnamese manufactured goods are 30% to 40% higher than those of similar goods produced by neighboring countries. Competitiveness of Vietnamese exports is also low because of poor designs, lack of brand names, and dependence on imported materials and foreign partners.

- Slow and unsteady changes in structure of industry:

In the past two decades, shares of service and manufacturing sectors increased against that of agricultural sector. This tendency is appropriate to industrialization and modernization program but the changes were very slow. The service sector fails to play its important role in the economic development as expected and its share in the GDP even fell over years, from 44.06% in 1995 to 38.33% in 2010 (Thời báo Kinh tế Việt Nam, 2011). Additionally, changes in the labor structure are even slower than those in the GDP structure.

Table 4: Changes in labor structure by sector (%)

Year	Agriculture	Manufacturing	Service	Year	Agriculture	Manufacturing	Service
1990	73.0	11.2	15.8	2007	53.9	20.0	26.1
1995	71.3	11.4	17.4	2008	52.6	20.8	26.6
2000	65.1	13.1	21.8	2009	51.9	21.6	26.5
2005	57.1	18.2	24.6	2010	48.2	22.4	29.4
2006	55.4	19.3	25.3				

Source: Thời báo Kinh tế Việt Nam (2011)

Structure of investment also changed in the same direction as the GDP structure, that is, more investment in manufacturing and service sectors and less investment in agriculture. In 1991, the agriculture accounted for 12.42% of the gross investment; manufacturing sector 30.86% and service 56.72%. These figures in 2009 were 6.3%; 40.6% and 53.1% respectively (Thời báo Kinh tế Việt Nam, 2011, p. 85). One of problems with this investment structure is the remarkable fall in investment in agriculture, which did not match its contribution to the GDP and failed to make the best use of advantages of agricultural production in Vietnam.

Regarding sectors in terms of ownership, certain positive changes have taken place when shares of public and local private sectors fell and the foreign sector became larger. In 1995 shares of those three sectors in the GDP were 40.18%; 53.52% and 6.30% and they changed to 33.74%; 47.54% và 18.72% respectively in 2010 (Thời báo Kinh tế Việt Nam, 2011, p. 82).

From a weak position in the early 1990s, the foreign sector now accounts for some 20% of the Vietnam's GDP. Concerning the local non-public sectors, their shares in the GDP seemed to fall but in fact, only collectivist and personal sectors contracted while the private sector expand its market share. The private sector that could barely exist before 1990 accounted for 7.4% of the GDP in 1995 and 11.02% in 2009 (Thời báo Kinh tế Việt Nam, 2011, p. 82). The rise of private and foreign sectors and

the fall of public, personal and collectivist sectors imply that the economic structure has changed positively, and development of private and foreign sectors has been encouraged in an effort to liberate local productive forces and make the best use of advantages possessed by foreign companies.

Although certain positive changes in economic structure have taken place, they are still slow. The sectors cannot reach their full potentials. A level playing field has not been established. Performance of the public sector is poor although it enjoys preferential treatments and the largest share in the gross investment. This prevents it from playing a leading role in economic development. Moreover, cooperation for development between sectors is still low.

Regarding regional economic changes, there are achievements in moving industrial production from big and populous cities to provinces where the land stock for industrial parks is abundant and labor cost is lower. To bridge the gap between regions, many programs to support economic development in remote and depressed areas have been carried out. Master plans for regional development and cooperation between provinces in the same region are still lacking. All provincial governments want to have their own sea ports, international airports, and golf courses, etc. while huge gaps in development level between regions still exist.

- Social and environmental issues:

High and stable growth rates in many years allowed improvements in personal income. The per capita GDP rose from US\$118 in 1991 to US\$1,168 in 2010 (Thời báo Kinh tế Việt Nam, 2011, p. 94). In the past decade, Vietnam was also famous for its success in poverty alleviation. Poverty rate in Vietnam fell from 26.2% in 1997 to 10.4% in 2010 (ibid., p. 94). However, gaps in personal income between regions are still wide. Northwestern zone houses only 3% of the population but accounts for 9% of poor families while some 33% of population in Western Highlands and coastal northern zone of the Central Vietnam live below the poverty line (Nguyễn & Trần, 2006, p. 122). Additionally, income gaps between the richest and the poorest and between urban and rural areas have tended to widen in recent years.

According to the GSO Household Living Standard Surveys in 2010 and previous years show that Gini index in Vietnam is on the increase while the WB 40% standard on the decrease and the income gap between the richest and the poorest is widening, which means that the income gap between classes did exist and widen steadily.

Table 5: Gini index and 40% standard in Vietnam over years

Year	Gini	40-percent standard	The richest/the poorest
1999	0.39	18.70	7.65
2002	0.42	17.98	8.10
2004	0.42	17.40	8.34
2006	0.424	17.40	8.40
2008	0.43	16.40	8.90
2010	0.433	15.00	

Source: GSO, 2011 & Thời báo Kinh tế Việt Nam, 2011

Although Vietnam has been recently ranked by the UN among middle-income countries, most of Vietnamese families remain in poor living conditions, high infant mortality, undernutrition, dropout and illiterate rates, which imply that the quality of life and economic growth are not high enough.

The low quality of economic growth in recent years is evident in damage to eco- system and widespread pollution that has become a serious problem for Vietnam. Full attention has not been paid to environment protection at first because the national strategy only focused on economic growth and extensive development. Many programs have been launched to save the environment (afforestation, supply of fresh water in rural areas, trash collection in urban areas) but they did not produce intended results. The environment is not improved much while the pollution becomes more serious, public health is threatened, and many rare diseases emerge, which reduce life quality of the people.

2. CHARACTERISTICS OF THE NEW GROWTH MODEL

Apparently, Vietnam cannot keep pursuing the extensive development because this model does not ensure high growth quality and sustainable development. Moreover, the inputs needed for growth as capital, labor and natural resources cannot increase without bound.

So what are characteristics of the new growth model?

- Firstly, the new model should aim at an intensive development. Regarding factor inputs, the intensive development depends on capital, labor and total factor productivity while the extensive development relies on labor and capital. TFP reflects effective use of labor and capital inputs, and effects of a wide range of other factors, from technological advances to human capital.

In recent years, TFP effects on Vietnam's economic growth has been humble, from 20% to 25%. In other words, increases in TFP made the GDP rise by 1.69% in 2001-2005 and 1.75% in 2006-2010 (Thời báo Kinh tế Việt Nam, 2011, p. 9). To achieve an intensive development, the role of TFP should be enhanced, and it should account for a larger share in the economic growth. In its Strategy for Socioeconomic Development 2011-2020, the Vietnamese government planned to increase the share of TFP to 31-32% by 2015 and 35% by 2020 (ibid., p. 10).

The new model should guarantee a higher quality of economic growth, that is, higher performance, fast, comprehensive and rational changes in the economic structure, higher competitiveness of the whole economy, and better solutions to social and environmental issues.

The new model should also ensure a sustainable development, effective solutions to macroeconomic balance and external shocks, and proactive integration into the world economy, etc.

3. ACTION PLAN

The principal objective of the new growth model is to improve the quality of growth. The following are suggestions about application of the new model.

Firstly, efficiency of employment of labor and capital should be enhanced while application of technological advances should be accelerated.

Necessary measures should be taken to attract all possible sources of capital, and more importantly, structure of capital sources should be improved by reducing the public investment, maintaining the share

of foreign capital and encouraging private investment. The ODA source should be limited because it implies a debt burden and many negative effects.

The most important task is to improve the efficiency of employment of capital regardless of its origin. To achieve this aim, an investment strategy should be introduced to orient flows of investment to major targets and actively avoid distribution of investment among too many projects, which may lead to huge wastes because shortage of fund prevents the projects, after completion, from running at their full capacity. Examining, evaluating and inviting tenders for implementation of projects also play important role in enhancing the investment efficiency.

Regarding foreign investment, licenses should be only granted to projects that employ high and eco-friendly technologies. Severe punishments against polluting projects should be imposed. Strong measures should be taken to stop transfer pricing practices among foreign-invested companies.

Labor, or human resources, should be considered as the most important factor input because it is the decisive factor in the effort to attract investment and master new technologies. Moreover, the human resources should be well equipped with necessary skills and knowledge.

Vietnam is enjoying a golden population structure. If fully tapped, the labor can contribute greatly to the economic growth. The most important indicator used for evaluating employment of labor is labor productivity. Therefore, one of the urgent problems to switch to the new growth model is to enhance the labor productivity. The higher productivity not only enhances the competitiveness but also generates a higher purchasing power because laborers gain better wages. Improving the labor productivity implies many tasks, such as enhancing skills and expertise of laborers, facilitating flows of laborers from agriculture to manufacturing and service sectors, and increasing the GDP, etc.

Modernizing the technologies in enterprises should be considered as a basic solution to a more intensive economic growth. To achieve this aim, the government should take measures to support replacement of technologies to increase added values in local products, thereby enhancing corporate competitiveness on the world market. Additionally, the government should strengthen investment in R&D activities and cooperation between universities, research centers and enterprises.

Concerning foreign-invested companies, the government can encourage them to import and transfer modern technologies by offering incentives in terms of tax, interest rate, bank loan, and other financial and monetary policies, and supporting their cooperation with local enterprises and research centers to realize technical innovations. Achieving such innovations and applying new technologies require a well-trained labor force that can employ and master new technologies. Developing high-quality human resources is therefore the most important measure to apply successfully the new growth model that is beyond the scope of this article.

Secondly, competitiveness at all levels (national, corporate and product) should be improved.

At the national level, the obstacles to Vietnam's competitiveness by both foreign and local experts, such as ineffective management machinery, corruption, poor technical infrastructure and poor financial access, should be addressed properly. Studying these problems and finding effective solutions are large projects that require investment from the government.

At corporate level, enterprises should replace their technologies, improve the management machinery, enhance the quality of work force, and invest more money and energy in marketing programs. To compete against foreign goods on international markets, more investment should be directed to design and package, support industries, development of local supplies of raw materials, and development of new products instead of producing goods according to subcontracts.

Field research reveals that high production cost of Vietnamese goods is caused by various expenses on greasing the wheels. Both enterprises and authorities should engage actively and resolutely in the fight against corruption and ensure transparency for administrative procedures or financial obligations.

Thirdly, changes in economic structure should be fast, comprehensive and rational, and linked with restructuring of the economy. Implementing the new model requires faster and more consistent changes in the economic structure. For the structure of industry, the share of service sector should be increased and more investment should be put in agriculture. Changes in the structure of industry should be associated with changes in labor structure. More attention should be paid to industries that can produce high added values, and links and cooperation between agriculture, manufacturing, and service sectors.

Changes in structure of economic sector should aim at reducing the share of public sector, maintaining the foreign sector and increasing the share of private sector. Equitization of state-owned companies has come to a halt for years because the stock market remains in the doldrums. Strong measures should be taken to revive this market.

Regarding local economy, the master plan for zonal development should be improved in order to make the best use of comparative advantages of each zone, avoid unnecessary competition between neighboring provinces, and enhance cooperation between zones.

Changes in economic structure should be linked with restructuring of the economy. This issue has recently been a center of attention for Vietnamese economists. In fact, restructuring of the economy implies revolutionary changes in various fields from industries, enterprises, institutions, markets, to human resources and sources of investment. It is a precondition for implantation of the new model.

Fourthly, social and environmental issues should be solved properly. This is the most important aspect that reflects the quality of economic growth and a basic feature of the new growth model.

The first social issue to deal with is employment. This task implies cuts in unemployment rate in urban areas and job increases in rural areas. Measures to achieve this goal are to encourage non-public enterprises, restore traditional handicraft guilds, and develop services and other non-farming occupations in rural areas. Additionally, to reduce income gaps, the government should make the best use of available instruments (taxes, social insurance, pension, allowance, minimum wage, etc.) to redistribute income among social classes.

To enhance public education level and cultural life, the government should invest in infrastructure, water and power supply, and education and health care services, especially in remote and depressed areas and communities of ethnic minorities.

Solving social problems also means a better control over population growth and social evils such as drugs, prostitutes, and criminals. This implies that the government should take stronger measures (educational, administrative, and economic ones) to achieve these goals.

Top priority should be given to protection for the environment. This task requires consistent and comprehensive efforts. The government should invest more in this project, that is, from 1% to 1.5% of the GDP as seen in many developed countries instead of 0.5% as found in Vietnam today. Enterprises should treat their wastes properly as required by laws and avoid employing obsolete or polluting technologies.

In rural areas, developing non-farming occupations should be associated with handling of environmental issues. In agricultural production, use of chemicals and pesticide should be reduced. Hill and forest land could be leased to local residents within afforestation programs. In sea farming, necessary measures should be taken to project sources of water. Besides educating in awareness of environmental issues, severe punishments should be imposed on violators of environmental regulations as criminals.

Finally, political commitment is crucial because the government play an extremely important role in implementation of the new growth model. First of all, the conception should be changed to recognize the new growth model as an urgent demand without it the sustainable development cannot be ensured and Vietnam may even face a crisis because effects of driving forces for Vietnam's economic growth in the past two decades have passed their peak while effects of the global economy forces Vietnam to get prepared for unfavorable upheavals. Without the new growth model, Vietnam may easily fall into the middle-income trap as warned by many international economists.

To achieve this goal, all possible measures should be taken to restore macroeconomic stability, including four policy instruments: monetary, fiscal, public expenditure and foreign trade policies.

One of causes that make Vietnamese economic performance poor is widespread corruption, and the government should have effective solutions to this problem. Moreover, the Vietnamese economy is deeply divided, as each province exists as a nation and has no true cooperation with others, as discussed by Hoàng (2007). The central government, therefore, has to take measures to enhance cooperation between provinces, erase interest groups, and support national interest.

In sum, adopting a new growth model is necessary for Vietnam today. A presentation on "Medium- and Long-term Issues of the Vietnamese Economy" was presented in the first session of the NA, 13th term, in which adoption of a new growth model is classified among the 10 most important issues. Apparently, besides restructuring of the economy, development of the new growth model is a preparation for a new phase in which Vietnam can enjoy a sustainable development and join the regional production network and the global chain of value■

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