Vietnam – little 'tiger' with big possibilities

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Abstract. In the first issue of journal (1/2016) we said we are convinced that Russia is not alone in the world. Thus, the theme of our inquiry will be searching for friendly-oriented countries—economically and politically as well. In the second part of our inquiry, we present the success story of Vietnam. Country's transition from low- income to middle-income countries per capita was amazing. Vietnam is placed among those countries with the best indicators of economically sustainable and politically friendly-oriented countries. Russia and Vietnam are connected with strategic partnership but it is insufficient for further development of economic relationships. It is urgent need to intensify the penetration Vietnamese market, searching for mutually beneficial partnership and long-lasting cooperation.

Keywords: Vietnam, World Bank, World Economic Outlook, Asian Development Bank.

Вьетнам — малый «тигр» с большими возможностями

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Аннотация. В № 1/2016 журнала в статье «Россия в поисках дружественно ориентированных стран» были поставлены вопросы: какие страны из числа дружелюбно относящихся к России сегодня можно рассматривать в качестве ее потенциальных партнеров; какие критерии необходимы для этого выбора? Учитывая неиспользованные пока возможности для плодотворного сотрудничества, наш выбор пал на одно из наиболее динамично развивающихся государств — Вьетнам. В статье представлен обзор социально-экономического развития Вьетнама и планы на ближайшую и дальнейшую перспективу. По нашему мнению, Вьетнам является надежным экономическим партнером, о чем свидетельствует растущий интерес к этой стране международных организаций и ряда стран. Поскольку свято место пусто не бывает — не упустить бы России этот шанс. Тем более что Вьетнам традиционно принадлежит к странам политически дружелюбным по отношению к России. Стратегическое партнерство с Вьетнамом требует и всесторонней интенсификации экономических отношений.

Ключевые слова: Вьетнам, *World Bank, World Economic Outlook, Asian Development Bank.*

Vietnam is a development success story. After 30 years of political and economic reforms since the launch of ***Đôi Mói*** (*renovation*) in 1986, have transformed the country from one of the poorest in the world, with per capita income around US $ 100, to lower middle income status within a quarter of a century with per capita income of around US$ 2,100 by the end of 2015. From a poor, war-ravaged, centrally planned economy, which was closed off from much of the outside world, Vietnam has become a ***middle-income country*** with a dynamic market economy that is deeply integrated into the global economy[1].

Vietnam's economic growth has been increasing since 2011, while inflation has remained in single digits. Well-balanced macroeconomic policies have helped restore stability and investor confidence, with growth being propelled by a surge in foreign direct investment and export-oriented manufacturing. Vietnam needs to continue to develop a more dynamic market economy — one that can compete globally and deliver sustainable, equitable growth over the long term. Despite remarkable achievements in reducing poverty, serious development challenges remain, with income and other socioeconomic gaps still evident in pockets of ethnic minorities and other vulnerable groups.

Vietnam's per capita GDP growth since 1990 has been among the fastest in the world, averaging 5.5 percent a year since 1990, and 6.4 percent per year in the 2000s. Vietnam's economy continued to strengthen in 2015, with GDP growth rate of 6.7 percent for the whole year. Social outcomes have improved dramatically across the board. Using the US$ 1.90 2011 PPP line, the fraction of people living in extreme poverty dropped from more than 50 percent in the early 1990s to 3 percent today. Concerns about poverty are now focused on the 15 percent of the population who are members of ethnic minority groups, but account for more than half the poor.

Vietnam's economic growth has not only been rapid, but also stable and inclusive, translating into strong welfare gains for the vast majority of the population. This is an impressive record of success — one that the Vietnamese people take justifiable pride in, while appreciating the support of the international community.

Regarding the twin goals of eliminating extreme poverty (living on less than US$ 1.25 per day) by 2030 and boosting shared prosperity among the poorest 40 percent in developing countries, Vietnam is a signature example of a country in recent times that has achieved rapid growth without a large increase in inequality. Thus, in Vietnam, the twin goals agenda suggests enhanced attention to four priority themes:

(i) supporting return to strong and inclusive growth;

(ii) giving more focused attention to non-income dimensions of poverty;

(iii) targeting communities that are getting left behind, notably ethnic minority communities; and

(iv) addressing sources of vulnerability.

The recent ***Vietnam Development Partnership Forum*** (VDPF) 2015 agreed on the need to strengthen reform efforts, competitiveness, citizens' participation, the broader inclusion agenda, the unfinished poverty agenda — particularly relating to ethnic minorities — and the increasing vulnerability of a growing number of people who live close to the poverty line. The 2015 VDPF also discussed the effective use and mobilization of development resources, which to some extent depend on implementing market institutions reforms. The VDFP, co-organized by the Ministry of Planning and Investment and the World Bank, is a platform for high level dialogue between the Government of Vietnam and Development Partners.

The World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries' prospects do not significantly differ at any given moment in time.

a. GDP at market prices and expenditure components are measured in constant 2010 U. S. dollars. Excludes American Samoa and Democratic People's Republic of Korea.

b. Non-oil GDP. Timor-Leste's total GDP, including the oil economy, is roughly four times the non-oil economy, and highly volatile, sensitive to changes in global oil prices and local production levels.

http://www.worldbank.org/en/publication/global-economic-prospects

But 30 years of success from reforms raises expectations for the future. The country's am-

[1] See: "Overall strategy for international integration through 2020, vision to 2030" (Part I, Part II, Part III). Approved on January 7, 2016 by VGP — PM Nguyen Tan Dung.
See also: "The Socio-Economic Development Plan 2016–20" *(forthcoming, draft available)* and "The Socio-Economic Development Strategy 2021–30", "Viet Nam Sustainable Development Strategy for 2011–2020". *Decision No. 432/QD-TTg on approving the Viet Nam Sustainable Development Strategy for the 2011–2020 signed on April 12, 2012 by Prime Minister Nguyen Tan Dung.*

Table 1. **GDP growth in Vietnam 1986–2015**
(constant LCU)

Indicator Name	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
GDP growth (annual %)	2.79	3.58	5.14	7.36	5.10	5.96	8.65	8.07	8.84	9.54
GDP per capita growth (annual %)	0.43	1.07	2.62	4.86	3.12	4.03	6.73	6.22	7.03	7.76

Indicator Name	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
GDP growth (annual %)	9.34	8.15	5.76	4.77	6.79	6.19	6.32	6.90	7.54	7.55
GDP per capita growth (annual %)	7.61	6.48	4.15	3.21	5.37	4.86	5.10	5.66	6.26	6.30

Indicator Name	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
GDP growth (annual %)	6.98	7.13	5.66	5.40	6.42	6.24	5.25	5.42	5.98	6.68
GDP per capita growth (annual %)	5.80	5.98	4.54	4.29	5.31	5.12	4.12	4.31	4.85	5.55

Source: The World Bank. World Development Indicators, 22 July, 2016.

bitions are aptly captured in the Vietnamese constitution, which sets the goal of "a prosperous people and a strong, democratic, equitable, and civilized country." There is a firm aspiration that by 2035, Vietnam will be a modern and industrialized nation moving toward becoming a prosperous, creative, equitable, and democratic society.

Not only are incomes higher, but the Vietnamese population is better educated and has a higher life expectancy than most countries with a similar per capita income. The maternal mortality ratio has dropped below the upper-middle-income country average, while under-five mortality rate has fallen by half, to a rate slightly above that average. Access to basic infrastructure has also improved substantially. Electricity is now available to almost all households, up from less than half in 1993. Access to clean water and modern sanitation has risen from less

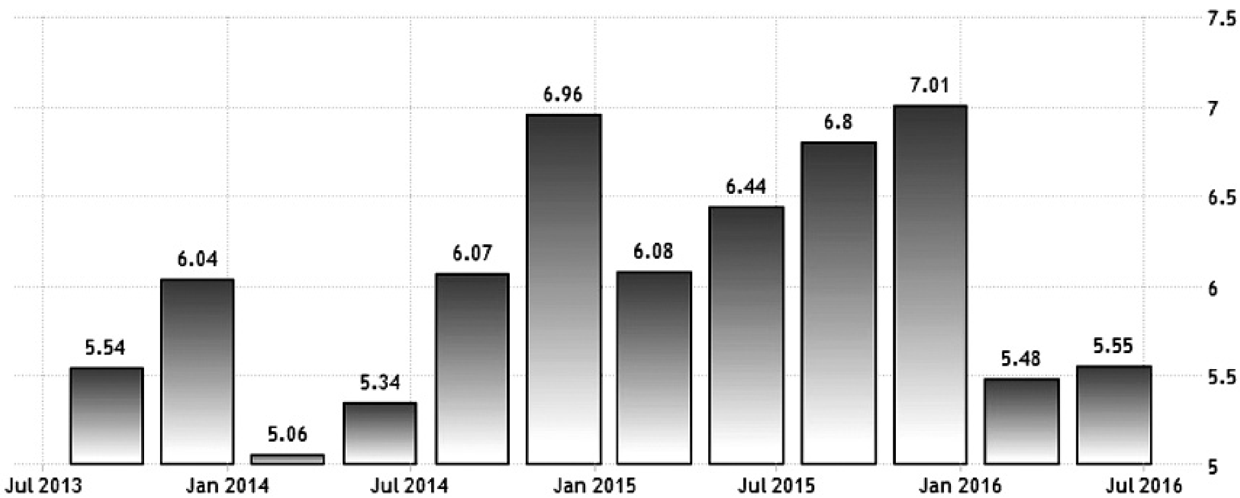


Figure 1. **Vietnam's GDP growth rate**

Source: www.tradingeconomics.com/General Statistics Office of Vietnam.

Table 2. **East Asia and the Pacific country forecasts**
(*Real GDP growth at market prices in percent, unless indicated otherwise*)

Country	2013	2014	2015	2016	2017	2018
Cambodia	7.4	7.1	7.0	6.9	6.8	6.8
China	7.7	7.3	6.9	6.7	6.5	6.3
Fiji	4.6	5.3	4.0	2.4	3.8	3.5
Indonesia	5.6	5.0	4.8	5.1	5.3	5.5
Lao PDR	8.5	7.5	7.0	7.0	7.0	6.8
Malaysia	4.7	6.0	5.0	4.4	4.5	4.7
Mongolia	11.6	7.9	2.3	0.7	2.7	6.2
Myanmar	8.5	8.5	7.0	7.8	8.4	8.3
Papua New Guinea	5.5	8.5	8.6	3.0	4.1	2.9
Philippines	7.1	6.1	5.8	6.4	6.2	6.2
Solomon Islands	3.0	1.5	3.3	3.0	3.3	3.0
Thailand	2.7	0.8	2.8	2.5	2.6	3.0
Timor-Leste[b]	2.8	6.0	4.3	5.0	5.5	5.5
Vietnam	5.4	6.0	6.7	6.2	6.3	6.3

Source: The World Bank. World Development Indicators, 22 July, 2016.

than 50 percent of all households to more than 75 percent.

In addition to the elaboration of three SEDS breakthrough areas, the five-year Socio-Economic Development Plan 2011–2015 focused on three critical restructuring areas — the banking sector, state-owned enterprises and public investment. The recent draft of the SEDP 2016–2020 acknowledges the slow progress of the reform priorities of the SEDP 2011–2015 and emphasizes the need to accelerate these reforms in 2016–2020 to achieve the targets set in the 10-year "Viet Nam Sustainable Development Strategy for 2011–2020."

Vietnam also faces an unfinished economic modernization and structural transformation agenda. Part of this relates to maximizing the gains from the ongoing structural transformations that have been a major contributor to growth since the early 2000s.

With agriculture still accounting for almost half the labor force and with significantly lower labor productivity than in the industry and services sectors, future gains from structural transformation could be substantial. The transformation from state to private ownership of the economy is even less advanced. The state also wields too much influence in allocating land and capital, giving rise to heavy economy wide inefficiencies. So, adjusting the role of the state to support a competitive private sector-led market economy remains a major opportunity. This will be important for enhancing productivity growth which has been stagnating for a long time. Vietnam needs more rapid productivity growth to underpin sustained rapid growth in order to achieve its objective of reaching upper middle income status in the next few decades.

Vietnam has boosted its international economic integration as it enters into more free trade agreements with the Eurasian Economic Union, the European Union, South Korea and the Trans-Pacific Partnership. At the same time, the ASEAN Economic Community was established on December 31, 2015, and is likely to create more opportunities for the country to integrate into regional and global economies. But while global integration has advanced well, with Vietnam embedding itself in global value chains, the benefits are constrained by the absence of linkages with domestic firms.

VIETNAM'S ECONOMY IN TRANSITION (1986–2016)

A Record of Strong and Equitable Growth, with Emerging Concerns

Vietnam is a major development success story. Its per capita GDP growth since 1990 has been among the fastest in the world, surpassed only by China. Growth has also been remarkably *stable* and *inclusive*, which, with major gains on *human development*, has contributed to impressive progress in alleviating poverty and improving non-income dimensions of welfare. But declining productivity growth, insufficient progress in including marginalized groups in the country's development (ethnic minorities in particular), and degradation of the environment call into question the durability of the current development model. Vietnam's governance structure could also be at an inflection point. The institutions that were adequate to carry the country to its lower-middle-income level are now exposing gaps that, unless addressed with boldness and urgency, are likely to impede the journey to upper-middle-income status.

In 1986 an impoverished Vietnam, on the brink of an economic crisis, embarked on a path of economic renovation (*Đôi Mói*). It was an explicit recognition that the "fence-breaking" reforms of the previous decade — opportunistically initiated to test the limits of central planning — had shown promise and that the situation was dire enough to demand a more systematic approach. *Annual inflation* was running at more than **400 percent**, the real economy on a downward slide and heavily dependent on foreign aid, food in short supply, the budget chronically short of resources, and the vast majority of the population in poverty.

Thus *Đôi Mói* began a process of macroeconomic stabilization, unshackling the economy from state controls and gradually but steadily integrating with the global economy. More durable foundations for a market economy were built over time. And in competently managing the transition from a planned to a market-economy structure, Vietnam succeeded where many countries that had been part of the former Soviet Union have failed.

The transition economy of Vietnam enjoyed remarkable achievements in the first 20 years of economic renovation (*Đôi Mói*) from 1986 to 2006. Notably, the economy grew at an average annual rate of **7.5%** in 1991–2000 period. Vietnam's Amended Constitution 1992 recognized the role of private sector in the economy. *U. S.-Vietnam Trade Bilateral Agreement* (US-BTA) was signed in 2001. The country's stock market made debut trading in 2000. Vietnam became a member of *Association of Southeast Asian Nations* (ASEAN) in 1995, then proceeded to full membership of the *World Trade Organization* in 2007, following which registered *foreign direct investment* (FDI) reached an all-time high of US **$71.7** billion in 2008. Together with the impressive economic achievements, Vietnam also saw its diplomatic and political status constantly improved in the international arena. The country has established diplomatic relations with more than 170 countries in the world, *strategic partnerships* with 12 important economies, both developed and emerging, namely China, Japan, Russia, India, England, France, North Korea, Italy, Germany, Indonesia, Malaysia and Thailand. The country also successfully hosted important events including the *Asia Pacific Economic Cooperation* (APEC) in 2006.

Upbeat sentiment helped to send Vietnam's stock market index (**VN-Index**) to its peak of 1,170 in March 2007 before its nosedive to 250 in February 2009, auguring an imminent crisis. Since 2008 Vietnam's GDP pace of expansion has slowed down markedly, with 2012 rate declining to 5%, the lowest level in 13 years, while the macro economy faced paramount turbulence, large trade deficit, high inflation, overwhelming business closures, rampant corruption and transparency problems, demonstrations of enraged citizens, downgrading environment, and sovereignty confrontation with China.

Since the world's geo-economics and geopolitics are entering an uncharted territory of evolving complication and rising uncertainty, not only Vietnamese entrepreneurs and households but also economists and policy makers are puzzled about what have happened, although the government has made a ten-year plan for 2011–20 socio-economic development. The ruling elites appear to have written this plan based more on 'the desirable' than 'the achievable' while a clear vision for farther future based on careful projections and profound solutions is needed. Vietnamese and outsiders have been increasingly aware of noticeable gaps between the country's promising potential and actual realization. As Vietnam has been considered somehow an entrance geopolitical game of East Asia and a 600-million population ASEAN market, the keen eye of international players sticks to the Vietnamese political economic scene of the country, which will most likely define the economic and diplomatic paths in the coming years.

The four characteristic sub-periods of post- Đôi Mói transition

From the adoption of *Đôi Mói* in 1986 by the CPV's Sixth National Congress to present day, Vietnam's economy has transformed from a centrally-planned model to market oriented with four characterized sub-periods. We divide the sub-periods based on the economy's entrepreneurial perspectives, emerging cultural values, the building of market economy, and attitude toward global geopolitics and economics.

The period of "entrepreneurial policy-makers" (1986–1994)

In its history, Vietnam barely had economic prosperity that lasted for decades. Until early twentieth century, the feudalist nation was a small and outdated agrarian country with continuous wars and invasions from the North (China and Mongolia) and conflicts with the Southwest neighbor (Cambodia). In the 20th century, the French and American wars drew most national efforts to serve the combats. From the national unification in 1975 to 1985, the nation struggled with its five-year plans on collectivization of agricultural and industrial production. However, the real results were often far behind expectation because the guiding principles 'violated the most important motivation for production development, that it is worked against the working people's vital vested interests'.

Upon the failure of the 1985 price-wage-currency adjustment scheme, a severe economic crisis followed, resulting in **hyperinflation of 775%** in 1986, scarcity of staples and consumer goods, impoverished living conditions, industrial stagnation, and mounting foreign debts. The situation worsened as Vietnam could barely trade with the West due to the U. S.'s trade embargo. The chaos had put the CPV under immense pressure to get the country out of the crisis, and *Đôi Mói* policies were an answer introduced in 1986, with which it is believed that there was no "political revolution or ideological conversion on the part of the leadership". The socialist ideology remained and was reiterated by the political leader of *Đôi Mói*, the Communist Party of Vietnam (CPV) General Secretary Nguyen Van Linh that "It is not objectively necessary to establish a political mechanism of pluralism and multiparty government. Socialism is the only right decision".

However, *Đôi Mói* leaders demonstrated some remarkable entrepreneurial characteristics in their economic thinking and implementation as economic crisis and harsh realities were neither necessary nor sufficient conditions for the reform to take place which enabled an undertaking process that had brought about the long-awaited extensive reforms, learning lessons of economic policies from Ho Chi Minh's times, 1945–1969, about the adoption of a multi-sectoral economy based on different types of ownership, encouraging for foreign investments, foreign trade.

Before *Đôi Mói*, Le Duan, CPV General Secretary from 1960 to 1986, was already critical of economic models taught by the Soviet Union and China for chronic economic malaise and blunders, although despite some innovative thinking Le Duan himself was a strong opponent of market economy and much of his policy turned out counter-productive. But in his time, Kim Ngoc, Party Secretary of Vinh Phuc province from 1966 to 1967, was an accomplished entrepreneurial politician who soon recognized problems of the mass collectivization, which resulted in poor agricultural production, and the need to have property right in farm household. He 'invented' a pilot plan called ***Khoán***, which had granted a certain degree of economic freedom to farmers, leading to remarkably higher rice yield and pig herds during the American war. Ngoc's innovative ideas were basically not accepted by the North's collectivism, and for a moment was regarded as an offensive to the prevailing socialist ideology.

After the death of Le Duan, Truong Chinh, a high-ranked politburo member and who would then briefly serve as CPV General Secretary (July-December 1986), was another highly influential leader and the one who laid down the first brick for the House of Reform of Vietnam, by launching the program of extensive reforms during the 6th CPV Congress in December 1986. As Truong Chinh stepped down, Nguyen Van Linh, CPV General Secretary 1987–91, continued to bring concepts of reforms to the nation's economic life through a nationwide reform program with sweeping changes. The old-fashioned centrally-planned economy was replaced with socialist market mechanism, which promoted the concept of a multi-sectorial economy, open-door policies towards international trade and investment, and recognized private property rights.

The new Law on Foreign Investment initiated in 1987 enabled a surge of the first wave of foreign direct investments (FDI) flowing into Vietnam, which then reached 10% of GDP in 1994. Vietnam was the largest FDI recipient among developing countries and economies in transition in proportion to the size of its economy thanks to its macroeconomic stabilization resulting from *Đôi Mói* and investor expectations of continuing reforms and improvements in the general investment climate. Corporate Law and Private Enterprise Law in 1990 'broke ground' the national private growth engine. From the old Confucian view imposed by the feudalist elites, which favors "educated scholars serving the government", by 1994 over 17,400 entrepreneurial firms started up. The 1992 Constitution extended human rights and recognized the multi-sectoral economy. Land Law in 1987 (revised in 1993) granted farmers land use rights. The milestones of *Đôi Mói* from 1987 to 1994 can be summarized in the following table.

Vietnam quickly grew to become the world's third largest rice exporter in 1989 (approx. 1.2 million tons exported), after China and the United States. The entrepreneurial policy-makers had been the core element to bring about change in macroeconomic management in 1990s although the CPV reserved status quo as the unique ruler.

Economic integration and adaption of market economy (1995–1999)

An eminent reformer, Prime Minister Vo Van Kiet came in office from 1992 to 1997, and continued to advocate extensive reforms. Vietnam sought further economic integration and diplomatic relations within the region and the world. From 1995 to 1999, the normalizing of diplomatic and trade relations with the United States was among the most remarkable for Vietnam, opening up opportunities to work with the world's developed economies and international organizations around, including multi-lateral donors such as the World Bank and ADB.

While the conservative in the CPV may have been afraid of losing their control over economic development and the national politics, generally speaking the CPV adopted open policies as they saw benefits for the country while no direct threats to their power were seen. Despite existence of conflicting views within the CPV, *Đôi Mói* momentum was retained for almost two decades with political consensus over three major principles: a) Political stability is a prerequisite of economic development, and the CPV remains to be the unique power; b) To achieve economic goals, Vietnam must keep its door open to foreign trade and investment; and, c) Gradualism is preferred to avoid deviation from the socialist path. These principles have been preserved and implemented explicitly through the CPV and government's socio-economic and foreign policies.

The U.S. also had some commercial interest in Vietnam's growing economy and strategic political interest to work with allies and friends "to promote stability and development by integrating Vietnam more fully into the existing East Asian order." Over US$ 10 billion of FDI entered the country in 1996 together with billions of dollars of ODA coming from the World Bank and Asian Development Bank. FDI enterprises played an important role in creating jobs, paying corporate taxes, encouraging consumption and competition, and contributing to export growth. Vietnam's GDP grew at 9.5% and 9.3% annually in 1995 and 1996 respectively, the highest rates recorded in the post-*Đôi Mói* period.

The country also expanded its diplomatic relations within the region becoming member of ASEAN (1995), APEC (1998). The U.S. and Vietnam then expanded the relation into a US-Vietnam bilateral trading agreement (the BTA was later signed in 2001). The US-Vietnam BTA had an important political economy impact by spurring political will to speed up negotiations on Vietnam's accession to WTO in later years.

Integrating in international markets has brought about new market opportunities and helped the country to deepen its reform, but at the same time exposed the country to contagious risks. Although less hurt by the Asian financial crisis in 1998 than other major Asian economies due to its young markets, Vietnam experienced GDP growth decline to 4.77% in 1998 and committed FDI fell by half in 1997–1998 to approximately US$ 5 billion, compared to US$ 10 billion in 1996. When the Asian financial turmoil broke out, Vietnam was still a nascent market model, without stock market; and the fledgling banking system was controlled by the state-run powerhouses who occupied 75% of assets and credit portfolio. Inefficient SOEs still accounted for 50% of the country's output.

Economic boom and emerging cultural values (2000–2006)

Succeeding Vo Van Kiet, Prime Minister Phan Van Khai (1997-2006) continued to pursue further integration into the world economy, especially from 2000 to 2006. In 2005, Mr. Khai was the first Vietnamese leader visiting the U. S., strengthening diplomatic relations between the two countries. The U.S. then supported Vietnam's accession to WTO in early 2007. Under Khai's leadership, Vietnam's economy experienced economic prosperity, quickly expanding financial markets and GDP, low inflation, surging FDI inflows and faster pace of privatization of SOEs. The capitalist symbolic finance machine — the stock market — was born in July 2000.

By the end of 2000, Vietnam stock market's capitalization was negligible in economic terms, less than 1% of GDP. But by the end of 2006, the figure rose to 22.7%. In 2006 VN-Index rose 150%. From 2006 to early 2007, investors considered stock markets a 'money machine,' and herd mentality triggered huge market bubble risks. Despite immense risks, the market continued to go high as capital gains were still made easily, and macro prospects looked bright with Vietnam joining WTO soon.

An average GDP growth of 7.5% in 2000–2005 period and the economy ranked at 58th largest in the world in 2006 made Vietnam like a little tiger economy in Southeast Asia. However, the rapid rate succumbed to 'resource curse' problem as there appeared more evidence that economic growth heavily relied on overconsumption of physical assets or/and capital endowments while innovation and productivity were not the main emphasis, leading to a decline of competitiveness. Vietnam's high *incremental capital to output ratio* (ICOR) of 7–8 times, compared to other Southeast Asian economies of 3–4, and rising investment to GDP over years, i.e., 4.9% (from 1996 to 2000) to 39.1% (2001–05) to the staggering 43.5% (2006–10) show its propensity to consume more resources while seeking growth. The absence of innovation and creativity together with resource curse will be destructive in the long run. Worse, the curse is more severe in the state-owned sector whose ICOR is two or three times higher than that in non-state sector.

Under P.M. Phan Van Khai's leadership, although the state-led model was still advocated, he did not vow to establish the state-run conglomerates. (There were only two state-run conglomerates established under Khai's tenure that are Vinacomin and Vinashin) In a stark contrast, his successor P.M. Nguyen Tan Dung established other eleven conglomerates within a few years after he took office. The breakdown of investment capital of the state-owned behemoths showed remarkably greater state budget investment in SOEs in 2008–09.

Still, combining the rapid growth and booming markets, Vietnam was successful in reducing *poverty rate* from 28.9% in 2002 to 18.1% in 2004 and 15.5% in 2006. Inflation was kept under check with average CPI in the period at 4.5%, a remarkable achievement as inflation has always been a chronic disease of the post-*Đôi Mói* period.

The US-Vietnam BTA and investors' projections that Vietnam would enter WTO in 2006 and China plus one strategy contributed to make Vietnam an attractive destination for FDI. Political and social stability played a significant role in facilitating economic development and attracting FDI. FDI started to recover from 2003 (US$ 3.2 billion registered capital) to 2006 (US$ 12 billion), generating growth and employment.

Privatization (politically correct: '*equitization*') of SOEs also saw improvement in the 2002–06 period with 2,813 enterprises being privatized, compared to a handful in 1990s, 60 in 2011, and 16 from 2012 to 2013Q1.

Globalization and attitudes toward global geopolitics and geoeconomics (2007-present)

After two decades of growth, the engine started to lose its steam in late 2000s. The contemporary state-run conglomerate model has shown serious problems ranging from poor efficiency and corruption to crony capitalism. The macro economy again experienced a period of high inflation, budget deficit, declining foreign exchange reserve, mismanaged fiscal and monetary policies, high unemployment and sluggish commercial activities.

Vietnam's unstable macroeconomics with two-digit inflation in 2008 together with spillover effect of the global crisis had made the stock bubble burst in 2009. The VN-Index went down to less than 250 in February 2009 from the peak of 1170 in March 2007; and it has never regained the expected 600-point level that experts, policy makers and investors had desperately looked for while the downtrend became unavoidable in mid-2008.

In a more complex financial system with interconnected stock markets, real estate markets and money market, the problems do not just stay with stocks. It can be argued that there was an inter-connectedness between Vietnamese stock market, properties market and money market, showing rising complexities. After the boom of stock market and skyrocketing stock prices, many realized capital gains and speculated on real properties. This had led to a boom on real estate market from 2007 to 2010 where home prices went exponential. A free fall in prices by almost 30% in 2012Q2, coupled with no liquidity, made speculators panic. The continuous fall of property prices by another 30% in 2013Q2 killed most speculators and developers. The government admitted that VND 108 trillion ($ 5.1 billion) worth of real property become non-tradable in the second quarter of 2013.

The banking sector immediately suffered, as about 50% of credits had been extended to real estate speculations and developments. Bad debts mounted, stifling credit flows to the economy and dragged production, businesses and consumption. Tightened banking credits then triggered informal credits and hyperactivity of 'loan sharks' to the extent that the government was worried about social unrest caused by rampant financial failures in information economy and households. Government's stimulus package of US$ 8 billion in 2008 and 2009 had temporarily backed GDP growth at 6.78% in 2010 before inflation threat became real in 2011. The growth rate fell to 5.03% in 2012, the lowest within 13 years. From 2011 to 2012, the economic crisis has pushed approx. 100,000 firms out of business, ~20% of the enterprise population. Consumer price index (CPI) only slowed down in the recent years as a result of falling domestic demand.

From 2007 to present, the government's policies to use state-run conglomerates as the chief force to propel Vietnam's economy have degraded into problems of crony capitalism, interest groups and corruption, which induce rent-seeking and exacerbate the 'resource curse' problem in Vietnam. The state sector only creates 10% employment but consumes 70% total social investment, 50% total state investment, 60% commercial credit, and 70% of ODA.

The problems prevailed in banking industry and other essential industries of the country. A typical example is tycoon Nguyen Duc Kien, a senior commercial banker, who had manipulated the banking industry and gold market before being arrested in August 2012. His arrest sent a chill through the Vietnamese stock markets for three consecutive days, during which most stocks lost 20% of their value, and almost created a bank run at ACB that forced the State Bank to directly inject liquidity into the bank. Many state-run conglomerates, the government's expected to be their 'iron fists,' now turned out to be debt-stricken patients generating overwhelming losses, debt burdens or scandalous corruption worth billions of U. S. dollars, i.e. Vinashin, and Vinalines, Vietnam Electricity Group (EVN), Vietnam National Coal and Mineral Industries Group (Vinacomin). In Vietnam, when the rule of law does not catch up with the expansion of the financial sector, political connections are used to channel loans toward unprofitable sector, hindering impact of finance on investment growth.

Although Vietnam's GDP per capita reached US $ 1,555/year in 2012 and $ 1,700 in 2013, the new millennium's setting is far different from that of the 1990s. Vietnam is now part of the world's bigger game, in which it has passed the point of no return. The economy has been becoming more open and engaged in international affairs. Vietnam has started to acquire important positions in United Nations and shown its interest in world geopolitical issues by joining the ***UN Peace Keeping Operation*** in early 2014. Vietnam's participation is prepared with the help of the United States, who supports the UN operation by its ***Global Peace Operation Initiative***. The country's joining into UN peace keeping force may potentially open new possibilities for U. S.-Vietnam relation, a meaningful event in global geopolitics. The CPV and the government have tried to preserve political stability through domestic policies (despite the successes and failures) and seeking foreign supports via foreign relations. For these hard, expensive and painful lessons about market mechanism and ideology, the 'little tiger' has not roared yet.

2016–2020 SOCIO-ECONOMIC DEVELOPMENT PLAN

Vietnam aims to become an industrialized country by 2020 with GDP per capita of at least $ 3,200 in its latest plan. In the ***Socio-Economic Development Plan*** (SEDP) for 2016–2020 the government set **21** macroeconomic, social and environmental targets. The plan is based on the socio-economic development strategy for 2011–2020 which lays out the path towards industrialization by the end of the decade through a socialist-oriented market economy model.

They include average GDP growth of 6.5 to seven percent per year, with 85 percent of output coming from the industrial and service sectors by 2020. Given the target for GDP growth, total GDP at current prices over the five year period is estimated to be over VND30,600 trillion ($ 1.37 trillion).

The SEDP draws on Vietnam's stable economic growth in recent years, its commitment to ***United Nations Sustainable Development Goals*** and increased international integration as reflected in free trade agreements signed with ASEAN, the TPP, and others. However, it also takes into account Vietnam's low competitiveness, poor infrastructure[2], climate change implications (especially in the Mekong delta), weak institutions, transition towards an aging population phase and increasingly complex situation in the East Sea. Vietnam expects major advances in strengthening its institutions and legal system, increasing human capital and improving the transport network.

Recent developments

Vigorous expansion of manufacturing and construction in 2015 spurred the fastest economic growth in 7 years. Foreign direct investment is seen supporting strong growth through the forecast period. Inflation will revive but remain relatively modest. The current account is forecast to slide into a small deficit. Reforms to banks and state enterprises continue to make gradual progress, but an emerging need is better management of rapid urbanization.

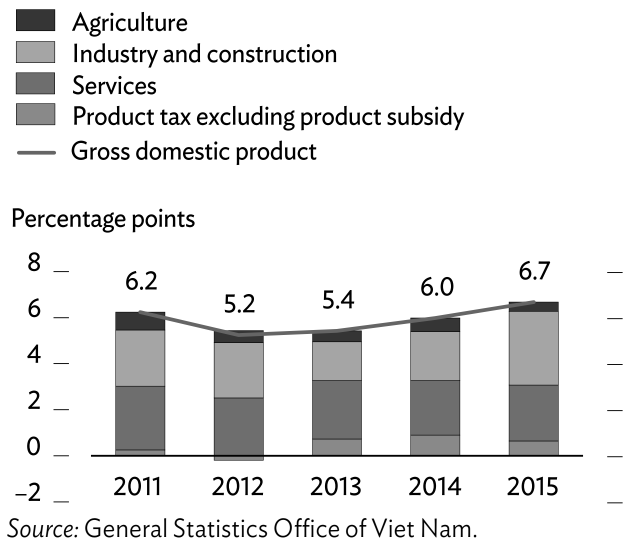
Economic growth accelerated to 6.7% in 2015, the fastest clip since 2008. *Industry* expanded by 9.6% and contributed nearly half of total growth (Figure 2). Powered by high foreign direct investment (FDI), the *manufacturing subsector* rose by a rapid 10.6%, and construction grew by 10.8% on foreign investment in factories, a recovery in the property market, and higher spending on infrastructure. FDI disbursements, which have increased substantially over the past decade, swelled by 17% to $ 14.5 billion in 2015 (Figure 3).

Growth in *services* was maintained at 6.3% last year. Wholesale and retail trade grew by 9.1% on strong private consumption, and banking and finance expanded by 7.4% as growth in credit quickened. However, a 0.2% decline in tourist arrivals dampened growth in tourism-related services. Agriculture recorded lower growth at 2.4% as global food prices fell and El Niño brought drought.

By expenditure, private consumption accelerated to 9.3%, spurred by rising employment and incomes and lower inflation. Investment also strengthened as buoyant FDI inflows and expansion in credit supported a 9.0% rise in gross capital formation. Net external demand weighed on GDP growth, though, as imports of goods and services in real terms rose faster than exports.

Notwithstanding stronger domestic demand, inflation slowed to average just 0.6% last year, the lowest since 2001, mainly on lower food and fuel prices (Figure 4 **3.31.3**). The State Bank of Vietnam, the central bank, kept policy interest rates steady in 2015 after reducing them over recent years, but commercial banks trimmed lending rates by 0.2–0.5 percentage points on aver-

[2] See, for example, "Efficient Logistics. *A Key to Vietnam's Competitiveness*" Eds. Luis C. Blancas, John Isbell, Monica Isbell, Hua Joo Tan, Wendy Tao, 2014, International Bank for Reconstruction and Development/The World Bank.



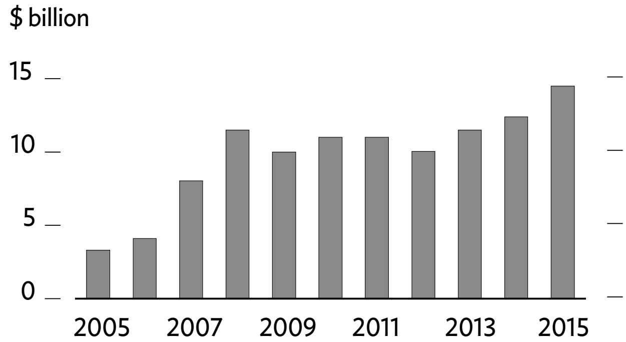


Figure 2. **Supply-side contributions to growth** *Figure 3.* **Disbursed foreign direct investment**

Source: General Statistics Office of Vietnam. *Source:* General Statistics Office of Vietnam.

Table 3. **Supply-side contributions to GDP growth (percentage points)**

Year	Gross domestic product	Services	Industry and construction	Agriculture	Product tax excluding product subsidy
2011	6.2	2.8	2.4	0.8	0.3
2012	5.2	2.5	2.4	0.5	–0.2
2013	5.4	2.5	1.7	0.5	0.7
2014	6.0	2.4	2.1	0.6	0.9
2015	6.7	2.4	3.2	0.4	0.6

Source: General Statistics Office of Vietnam.

age. Lending rates have dropped by half since 2011. Lower rates for borrowers complemented recovering consumer and investor confidence to spur credit growth to an estimated 18%, exceeding the government's initial target of 13–15%. Broad money supply increased by an estimated 14%.

To support exports, and in response to depreciation affecting other Asian currencies, the central bank devalued the Vietnam *dong* against the US dollar three times in 2015, adjusting the reference rate by 1% each time. The central bank also moved to enhance exchange rate flexibility by expanding the trading band from 1% to 3% on either side of the reference rate and changing to a daily reference rate announcement system. The monetary authority tightened regulations on foreign currency and discouraged foreign currency hoarding by mandating zero interest rates for US dollar deposits. Over 2015, the dong depreciated by 5% against the US dollar.

After several years of large external surpluses, the current account came under pressure in 2015 as imports rose faster than exports.

Merchandise imports rose on a balance-of-payments basis by an estimated 12% to $ 155 billion. Imports of machinery, equipment, and electronic components surged by more than 25%, reflecting strong demand for capital goods and inputs into export-orientated manufacturing. Imports of consumption goods rose by 10%, lifted by buoyant consumer spending.

Merchandise exports increased by an estimated 7.9% to $ 162 billion. Customs data show that the biggest gains were in exports of mobile phones and their components, which jumped by 30% and comprised 19% of total exports. Vietnam's imports and exports together now exceed

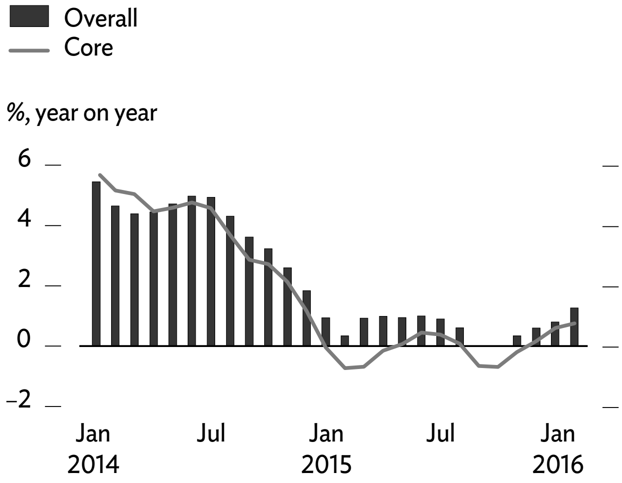


Figure 4. **Inflation, %, year on year**

Note: Core excludes food inflation.

Source: General Statistics Office of Vietnam.

165% of GDP, compared with less than 70% when the government started economic reforms in the mid-1990s.

The result was a 39% fall in the trade surplus, which, along with an estimated 17% decline in remittances, cut the current account surplus to an estimated 0.3% of GDP from 4.9% in 2014. After taking into account a smaller surplus in the capital account and sizable negative net errors and omissions, the overall *balance of payments* recorded a deficit equal to 3.1% of GDP (Figure 5). Foreign exchange reserves fell to an estimated 2 months of import cover (Figure 6).

Efforts to rein in the fiscal deficit had limited impact last year. The government reported that the budget deficit equaled 5.4% of GDP, narrowing slightly from 5.7% in 2014. Revenue rose by 10.0% and would have increased faster if not for lower oil prices and a cut in the corporate income tax rate. Government expenditure grew by 7.3%. Public debt, including debt guaranteed by the government, was projected to equal a record 62% of GDP, approaching a 65% limit set by the National Assembly (Figure 7).

Progress on economic reform remains slow. The government sold minority equity stakes in some 160 state-owned enterprises in 2015, well below its target of 289. Many individual equitizations fell short of targets. As for banking reforms, the central bank supported the mergers of several banks, following through on its plan for banking sector consolidation. Reported nonperforming loans (NPLs) declined to 2.7% of outstanding loans by the end of 2015, largely through their transfer from banks to the Vietnam Asset Man-

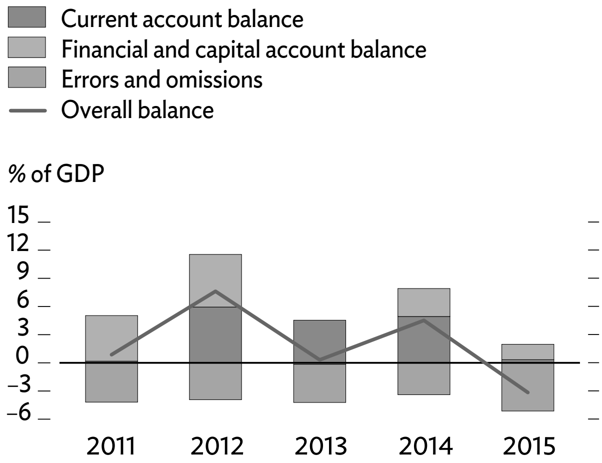


Figure 5. **Balance of payments indicators**

Sources: State Bank of Viet Nam; International Monetary Fund; ADB estimates.

Table 4. **Inflation, %, year on year**

<table>
<tr><th colspan="14">2014</th></tr>
<tr><th></th><th>I</th><th>II</th><th>III</th><th>IV</th><th>V</th><th>VI</th><th>VII</th><th>VII</th><th>IX</th><th>X</th><th>XI</th><th colspan="2">XII</th></tr>
<tr><td>Core</td><td>5.7</td><td>5.2</td><td>5.0</td><td>4.5</td><td>4.6</td><td>4.8</td><td>4.6</td><td>3.7</td><td>2.9</td><td>2.7</td><td>2.1</td><td colspan="2">1.2</td></tr>
<tr><td>Overall</td><td>5.5</td><td>4.7</td><td>4.4</td><td>4.5</td><td>4.7</td><td>5.0</td><td>4.9</td><td>4.3</td><td>3.6</td><td>3.2</td><td>2.6</td><td colspan="2">1.8</td></tr>
<tr><th colspan="12">2015</th><th colspan="2">2016</th></tr>
<tr><th>I</th><th>II</th><th>III</th><th>IV</th><th>V</th><th>VI</th><th>VII</th><th>VII</th><th>IX</th><th>X</th><th>XI</th><th>XII</th><th>I</th><th>II</th></tr>
<tr><td>0.0</td><td>−0.7</td><td>−0.7</td><td>−0.1</td><td>0.1</td><td>0.4</td><td>0.4</td><td>0.1</td><td>−0.7</td><td>−0.7</td><td>−0.2</td><td>0.2</td><td>0.6</td><td>0.8</td></tr>
<tr><td>0.9</td><td>0.3</td><td>0.9</td><td>1.0</td><td>1.0</td><td>1.0</td><td>0.9</td><td>0.6</td><td>0.0</td><td>0.0</td><td>0.3</td><td>0.6</td><td>0.8</td><td>1.3</td></tr>
</table>

Source: General Statistics Office of Vietnam.

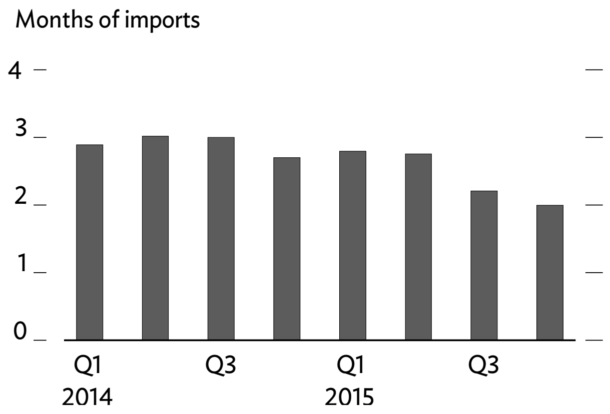


Figure 6. **Gross international reserves**

Sources: State Bank of Viet Nam; International Monetary Fund; Q = quarter.

ADB estimates. *Note:* Data exclude government foreign exchange deposits at the State Bank of Viet Nam and the foreign exchange counterpart of swap operations. Imports are on free-onboard basis.

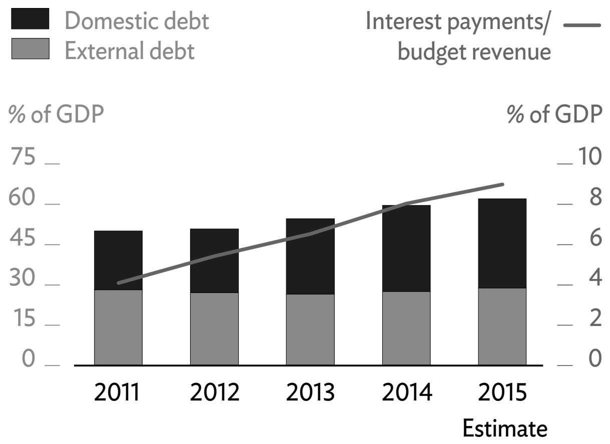


Figure 7. **Public debt and debt servicing costs**

Sources: Government of Viet Nam; World Bank; International Monetary Fund; ADB estimates.

agement Company. This company, established by the government in 2013 to acquire, restructure, and sell NPLs, had acquired $ 11.0 billion in bad loans by the end of 2015, up from $ 6.1 billion a year earlier. But with a limited capital base and lacking an adequate legal framework for resolving NPLs, it had sold or recovered by the end of December last year just 9% of the NPLs it held.

Economic prospects

The economy is projected to sustain growth at 6.7% in 2016 before the pace moderates to 6.5% in 2017 (Figure 8). Strong export-orientated manufacturing, FDI inflows, and domestic demand will be partly offset by the effect of slowing expansion in the People's Republic of China (PRC). New FDI commitments came in relatively flat at $ 22.8 billion in 2015, which suggests that disbursements of FDI could level out this year and decline in 2017. About 60% of the FDI commitments are for export-orientated manufacturing.

Rising incomes and modest (though quickening) inflation are expected to buoy private consumption. Sharply rising sales of automobiles — up by 55% in 2015 — illustrate the recovery in consumer confidence. Viet Nam has become the fastest-growing auto market in Southeast Asia. Business sentiment is similarly buoyant. A survey in December 2015 showed that 41% of businesses expected conditions to improve in 2016, and a further 40% expected stable conditions.

Prospects for growth in private investment are enhanced by a proliferation of trade and investment agreements concluded over the past 18 months. These include trade agreements with the European Union and the Republic of Korea, and commitments to participate in both the Trans-Pacific Partnership led by the US and the Eurasian Economic Union led by the Russian Federation. Viet Nam is expected to benefit as well from the ASEAN Economic Community, whose members in the Association of Southeast Asian Nations collectively form Viet Nam's third-largest export market after the US and the European Union.

These agreements will be implemented over several years but are expected to stimulate investment in the near term as businesses prepare for expanded trade opportunities. The agreements also signal to the business community the government's renewed commitment to liberalize

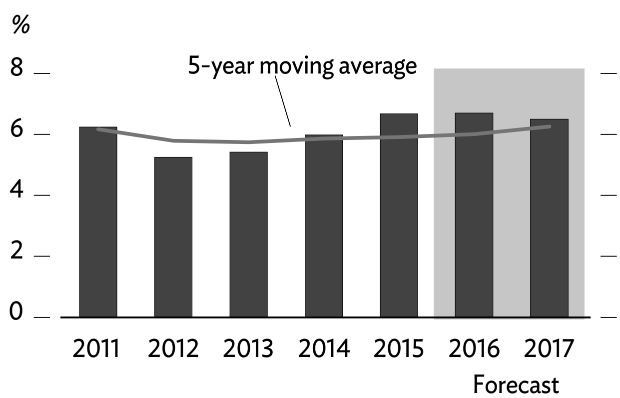


Figure 8. **GDP growth forecast**

Source: Asian Development Outlook database.

the economy. In recent years, it has eased restrictions on foreign ownership of property and corporate shares and has said it would reduce from 51 to 6 the number of industries closed to foreign ownership. The VN Index of share prices rose by 6.1% in 2015, building on 8.1% gain in 2014.

Manufacturing and construction are projected to maintain solid expansion. The purchasing managers' index showed in the first 2 months of 2016 improving business conditions for manufacturers, including a rise in new orders. Services are projected to expand at a robust pace, though prospects have dimmed for tourism from the PRC, the source of one-quarter of Viet Nam's inbound tourists. Visitor arrivals from the PRC fell by 8.5% in 2015. Subdued growth will continue for agriculture in the near term under soft global food prices and the effects of El Niño.

Inflation picked up to average 1.3% in the first 3 months of 2016 and is forecast to average 3.0% this year and 4.0% in 2017 (Figure 9). The government is expected to raise administered prices for education and health care and boost public sector minimum wages. Import prices will rise this year with dong depreciation, and higher global food and fuel prices in 2017 will add to inflation next year.

The central bank targets credit growth at 18–20% in 2016 to accommodate strong economic growth. Lending interest rates might come under upward pressure in the forecast period as inflation gradually turns up and rising demand for credit collides with tighter bank liquidity.

Fiscal policy looks set to tighten gradually but to remain supportive of growth. The government aims to narrow the budget deficit to 4.9% of GDP in 2016 and 4.0% in 2017. Continuing a shift started in 2015, the budget for 2016 puts greater emphasis on capital expenditure, which is slated to rise by 25.5%. Current expenditure is set to rise by a more modest 6.5%.

Plans for fiscal consolidation are at risk, however, from shortfalls in revenue. Over the past 5 years, reductions in corporate income tax rates, the removal of tariffs, and tax exemptions for favored firms have eroded the tax base. Low oil prices are dragging on resource tax revenue, which comprises 10% of the total. Central government revenue and grants fell from the equivalent of 27.6% of GDP in 2010 to 22.0% in 2015.

The government could use funds from the equitization of state-owned enterprises and issue more short-term securities to support the budget in the near term, but achieving a more sustainable fiscal position is likely to require tax reform to reverse falls in the ratio of tax to GDP.

Merchandise exports are seen rising by 10% in US dollar terms this year and by 14% in 2017 as new production from foreign-invested factories comes online and trade agreements take effect. Imports will also continue to grow in response to strong demand for both consumption and capital goods, and to supply inputs for manufacturing. Modest recovery is expected in remittances. The current account is forecast to slip into deficit this year and recover to balance in 2017 (Figure 10).

Sluggish progress on reforming banks and state-owned enterprises poses risks to the outlook. Undercapitalized banks with deficient financial transparency remain exposed to shocks. The upswing in credit growth could spark a new round of speculation in risky real estate. To mitigate such risks, the central bank took steps early in 2016 to tighten lending requirements for real estate and reduce the potential for maturity mismatch in bank lending. Further progress on bank consolidation and enhanced transparency, asset classification, NPL resolution, and disclosure requirements will be vital for strengthening the sector.

From desirability into reality

The Vietnamese government's development strategy is based on a series of 10-year socio-economic development strategies (SEDS). Viet-nam's Socio-Economic Development Strategy (SEDS) 2011–2020 gives attention to structural

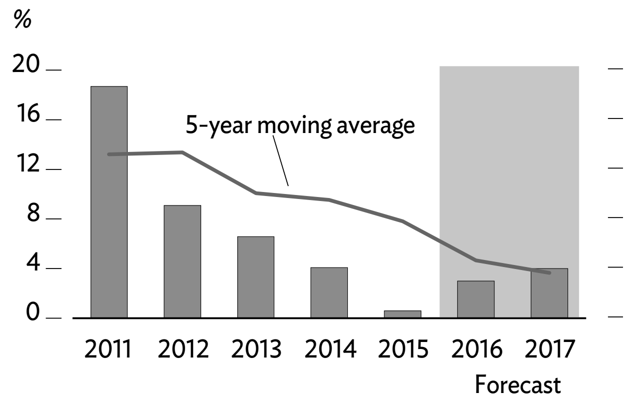


Figure 9. **Inflation forecast**

Source: Asian *Development Outlook* database.

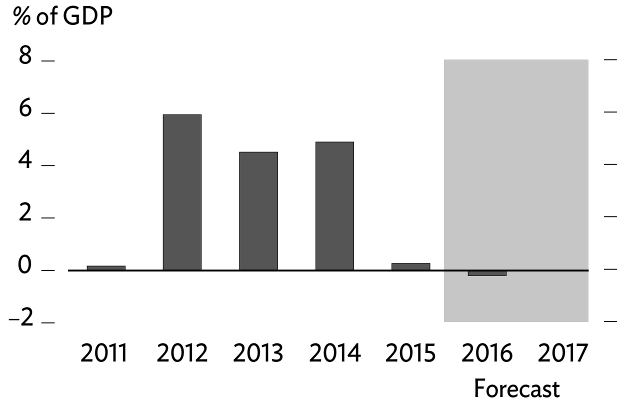


Figure 10. **Current account balance forecast**

Source: Asian Development Outlook database.

reforms, environmental sustainability, social equity, and emerging issues of macroeconomic stability. It defines three 'breakthrough areas':

(i) promoting human resources/skills development (particularly skills for modern industry and innovation);

(ii) improving market institutions, and

(iii) infrastructure development.

The five year socio-economic development plan lays out the actions needed to translate the strategies into reality. The SEDP provides a framework and direction for ministries and sectors to develop their own plans. In "Viet Nam Sustainable Development Strategy for 2011–2020". *Decision No. 432/QD-TTg on approving the Viet Nam Sustainable Development Strategy for the 2011–2020 signed on April 12, 2012 by Prime Minister Nguyen Tan Dung* the Vietnamese government set 21 macroeconomic, social and environmental targets as showed in Table 5.

Given that, the government set out 12 solutions that will guide Vietnam's socio-economic development for the next five years.

1. Development of a socialist oriented market economy, macroeconomic stability and a positive environment for socio-economic development

This includes institutional reforms towards freer markets and further privatization. Instead of direct provision, the government will support the development of a market for public services. More emphasis is also put on greater coordination among monetary, fiscal and other policies. By 2020, Vietnam hopes to have a coherent, transparent and effective legal system.

2. Economic restructuring, increase in productivity and competitiveness

Vietnam plans to promote entrepreneurship, including setting up start-up training centers and venture capital funding. Businesses are to receive support in research and development and public private partnerships (PPP) will be prioritized.

Vietnam is aiming for ***agriculture*** to develop at a rate of 2.5 percent to three percent per year with up to 50 percent of communes meeting the new rural standard by 2020.

Application of biotechnology and information technology in production, management and agricultural extension services is encouraged. The country is also determined to ensure food safety.

Regarding ***industry***, Vietnam eyes growth of eight percent to 8.5 percent per year. By 2020, industry is set to account for 40 percent of GDP.

Particular focus is put on high tech industries. Industries that serve agriculture will be prioritized, especially agricultural product processing and manufacturing of agricultural equipment and machinery. Vietnam will also support development of renewable energy sources, especially wind and solar power. In parallel, it will invest in oil and gas extraction and processing.

Services are set to grow 6.6 percent to 7.1 percent per year and by 2020 make up **45 percent** of GDP.

Vietnam hopes to develop tourism into the leading service sector. Meanwhile, priority is also given to intellectual and technology linked services with high added value. Key service sectors include transport, ecommerce, telecommunications, wholesale and retail distribution and branding of Vietnamese products.

3. Development of economic regions and clusters

Development of business clusters based on regional master plans is high on the agenda, noting the importance of connectivity. Emphasis is put on key economic regions, economic zones and industrial parks.

4. Construction of urban and infrastructure systems

Key construction projects planned to help upgrade and improve the connectivity of Vietnam's infrastructure include:

Table 5. **Main indicators of 2016–2020 Socio-Economic Development Plan**

	Indicator	2016–2020 Target
1	Average GDP Growth	6.5–7.0%/year
2	Annual GDP per capita	3.200–3.500 USD
3	Industry, Construction & Services' share of GDP	85%
4	Total average social investment over 5 years	32–34% GDP
5	Budget deficit by 2020	4% GDP
6	Total factor productivity's contribution to economic growth	30–35% GDP
7	Average increase in productivity	5%/year
8	Decrease in power drain as share of GDP per capita	1–1.5%/year
9	Urbanization rate by 2020	38–40%
10	Share of agricultural workforce by 2020	40%
11	Trained labour	65–70%
12	*of which has* degree, certificate	25%
13	Urban unemployment	<4%
14	Number of doctors per 10,000 people	9–10
15	Number of hospital beds per 10,000 people	>26.5
16	Health insurance coverage	>80%
17	Reduction in poverty rate	1–1.5%/year
18	Hazardous waste treated 85%	85%
19	Hospital waste treated	95–100%
20	Forest coverage	42%
21	Access to clean water by 2020	90% in rural areas 95% in urban areas

North-South roads

Upgrade existing railroad gauge from one meter to 1.435m

Phased construction of a North-South high speed train

Construction of international sea ports in the North and South, and mobilization of funding for an international transit port

Phasing of investment for Long Thanh International Airport

Completion of the irrigation system in the Mekong Delta to prevent flooding, alkaline soils and salinity.

In addition, infrastructure projects to respond to climate change and sea level rise will be prioritized.

5. Mobilization and effective use of resources

Vietnam continues to re-structure investment, especially public investment in order to improve quality, effectiveness and competitiveness. Emphasis is put on saving, ensuring trade and budget balances and expanding the scope and opportunities for private investments.

The legal framework for public private partnerships will be further improved for greater transparency, stability and fairness to encourage businesses to invest in infrastructure projects.

Vietnam will promote cooperation with FDI companies (FDI — foreign direct investment) to facilitate technology and knowledge transfer. However, it will "not attract FDI at all costs". Legislation will be revised to attract foreign investment, especially high tech, environmentally friendly and value adding projects. Meanwhile, projects that widen the trade deficit are energy intensive and extract resources without processing will be curbed. In addition, projects which waste resources, use outdated technology and pollute the environment will not be permitted.

Vietnam will continue to improve relevant legislation on managing and usage of ***Overseas Development Assistance***. Procurement will be fairer and more transparent, minimizing pre-assigning contractors and using land of high commercial value. Priority will be given to projects in large scale economic and social infrastructure, agricultural development, improving modern market economy institutions, human capital (especially development of a skilled workforce), environmental protection, climate change, green growth strategy and others. Inspection and monitoring of investment projects will also be strengthened.

6. Improvement in human capital and strengthening the potential of science and technology

Vietnam plans educational reform towards a more open and comprehensive approach that has a greater emphasis on life skills, reduces workload in pre-tertiary education and encourages self-study and creativity. Emphasis is given to developing a knowledge economy with a high quality workforce in science and technology.

7. Cultural development, implementation of social progress and justice, and improving living standards in harmony with economic development

Vietnam is committed to integrating United Nations Sustainable Development goals into the country's socio-economic programs and plans.

8. Active response to climate change, disaster prevention, resource management and environmental protection

The country plans to improve regulations, policy and coordination of solutions for climate change, disaster risk reduction, natural resource management, environmental protection and land use. Matters that require immediate attention include the drought in the Central Highlands and the Southern Central region and urgent projects to prevent salinity and retain freshwater.

9. Anti-corruption, thrift and anti-wastefulness

Vietnam continues to improve relevant regulations, focusing on areas easily prone to corruption. They include asset declaration by government officials and limiting cash transactions. Inspections, auditing and prosecution are to be strengthened. The monitoring role of publicly elected bodies and the Fatherland Front in reporting corruption will be promoted.

10. Enhancing effectiveness and efficiency of state management, ensuring public freedom and democracy in socio-economic development coupled with compliance with the law

Government processes are set to be simplified and less bureaucratic. There will be clear distinctions between the functions of government agencies and the market, whereby the government only manages and provides directions for socio-economic development through legislation, planning and regulatory instruments appropriate for the market economy. Administrative intervention is to be minimized.

11. Strengthening national defense and security, fighting to preserve independence and sovereignty and ensuring political security, social order and safety

The SEDP stresses effective implementation of the strategy to protect the country under changing circumstances.

12. Improving effectiveness of external relations, active international integration, peaceful environment and favorable conditions for the country's development

Vietnam wants to improve effectiveness of multilateral relations, especially within ASEAN and the United Nations. International cooperation to ensure regional and national defense, security and sovereignty is to be strengthened. Sea disputes are to be resolved by peaceful means in line with international law and regional code of conduct. Furthermore, Vietnam intends to actively negotiate and sign new generation free trade agreements.

We will discuss nine economic indicators have been assigned targets for 2020 by the National Assembly, covering topics from GDP growth to urbanisation (see Table 6) and set out how likely they are to be achieved.

1. Average annual GDP growth between 6.5% and 7.0%

This would represent an acceleration of growth from the previous five-year period (5.9% average), but given that the global economic environment was challenging in 2012 and 2013 such stronger growth could be achievable if supported by an improved global environment, as was the case in 2015 when a 6.7% expansion was recorded. This positive outlook is of course reliant on global conditions remaining stable or improving, any global downturn over the next five years would clearly knock the target off course. Another reason for optimism is that the Trans-Pacific Partnership (TPP) trade agreement should be brought into force within the five-year period, and is expected to be a real benefit for the Vietnamese economy.

2. GDP per capita between $ 3,200 and $ 3,500 in 2020

The chances of meeting this target are a little more challenging than the first. GDP per capita in Vietnam in 2015 was $ 2,109, with an average growth rate over the past five years of 9.7%. If this growth rate were repeated over the next five years it would take GDP capita to $ 3,350 in 2020, within the target range. However, growth has slowed considerably in recent years (to 2.8% in 2015) and the fact that the target is set in US dollars makes it vulnerable to a strengthening dollar. The Vietnamese dong fell 5.1% against the dollar during 2015, thereby hitting the rate of growth in GDP per capita in dollar terms. An example of this effect is shown below:

Table 6. **Assessment of indicator achievability**

Indicator	Topic	Target	Latest Year	Recent Trend (Average)	Achievability*
1	Average annual growth of GDP	6.5–7%	6.7%	5.9% (past 5 years)	2
2	GDP per capita in 2020	$ 3.200–$ 3.500	$ 2.109	9.7% growth (past 5 years)	3
3	Proportion of GDP in Industry and Services	85%	68%	66% (past 5 years)	4
4	Total Social Investment Capital as % of GDP	32–34%	32.6%	32.4% (past 5 years)	1
5	State budget deficit as % of GDP in 2020	4%	4.4%	3.0% (past 5 years)	2
6	Fall in Energy Consumption as a % of GDP	1–1.5%	5.1%	1.3% (past 5 years)	2
7	Rate of Urbanisation by 2020	38–40%	33.0%	2.1% growth (past 5 years)	4
8	Total Factor Productivity (TFP) contribution to growth	30–35%	Unable to source data		
9	Average annual increase in labour productivity	5%	6.4%	5.4% (past 2 years)	3

*Scale of 1 to 5 where 1 is the most achievable.

	2015	2016 (with 9.7% growth, constant exchange rate)	2016 (with 9.7% growth, 5% dong depreciation)
Vietnamese dong	45.700.000	50.132.900	50.132.900
US$	2.109	2.230	2.123

Sources: General Statistics Office, with Markit calculations.

3. Industry and Services to account for 85% of GDP in 2020

Table 7. **GDP *per capita* (PPP) in selected Asian region countries**

Cambodia	$ 3.500 (2015 est.) $ 3.300 (2014 est.) $ 3.100 (2013 est.)
China	$ 14.100 (2015 est.) $ 13.300 (2014 est.) $ 12.400 (2013 est.)
Fiji	$ 9.000 (2015 est.) $ 8.700 (2014 est.) $ 8.300 (2013 est.)
Indonesia	$ 11.100 (2015 est.) $ 10.800 (2014 est.) $ 10.400 (2013 est.)
Laos	$ 5.300 (2015 est.) $ 5.100 (2014 est.) $ 4.800 (2013 est.)
Malaysia	$ 26.300 (2015 est.) $ 25.400 (2014 est.) $ 24.500 (2013 est.)
Mongolia	$ 12.100 (2015 est.) $ 12.100 (2014 est.) $ 11.300 (2013 est.)
Myanmar	**n/a**
Papua New Guinea	$ 2.700 (2015 est.) $ 2.500 (2014 est.) $ 2.400 (2013 est.)
Philippines	$ 7.300 (2015 est.) $ 7.000 (2014 est.) $ 6.700 (2013 est.)
Solomon Islands	$ 1.900 (2015 est.) $ 1.900 (2014 est.) $ 1.900 (2013 est.)
Thailand	$ 16.100 (2015 est.) $ 15.700 (2014 est.) $ 15.700 (2013 est.)
Timor-Leste	$ 5.600 (2015 est.) $ 5.500 (2014 est.) $ 5.300 (2013 est.)
Vietnam	$ 6.000 (2015 est.) $ 5.700 (2014 est.) $ 5.400 (2013 est.)
World	$ 15.800 (2015 est.) $ 16.700 (2014 est.) $ 16.400 (2013 est.)

Note: data are in 2015 US dollars
Source: CIA — The World Factbook. 2016. https://www.cia.gov/index.html.

This target looks some way off at present, with the combined sectors accounting for 68% of GDP in 2015 (28% Industry, 40% Services). Furthermore, the trend does not show a rapid increase in the share of the economy accounted for by these sectors.

Composition by sector of GDP:
agriculture: 19.3%
industry: 38.5%
services: 42.2%
(2013 estimate)
agriculture: 17.4%
industry: 38.8%
services: 43.7%
(*2015 estimate*)
(*Source*: CIA — World Fact Book)

4. Total Social Investment Capital between 32% and 34% of GDP in 2020

This target should be achievable given that it was met in 2015 (32.6%) and the average over the past five years is also within the target range. There is also the opportunity for the state to directly influence the figure given that around one-third of social investment capital emanates from sources related to the public sector (see Table 8).

5. State budget deficit of 4% of GDP in 2020

Success in achieving this target will depend to some extent on global economic conditions and the effect they have on the Vietnamese economy. Should conditions be relatively benign the target looks reachable. The target has only been breached four times in the past 15 years, but these include 2013 and 2014 (the latest available data, Figure 12) and so some improvement will be needed to reduce the deficit by the end of the decade.

Vietnam recorded a Government Budget deficit equal to 4.40 percent of the country's Gross Domestic Product in 2014. Government Budget in Vietnam averaged −3.65 percent of GDP from 1988 until 2014, reaching an all-time high of 1.30 percent of GDP in 2006 and a record low of −9.90 percent of GDP in 1988. Government Budget in Vietnam is reported by the *Asian Development Bank*.

6. Fall in energy consumption as a % of GDP of between 1% and 1.5% per year

While the data on energy usage can be volatile, the recent trend is in favor of the target being met. In the three years to 2013 (the latest year

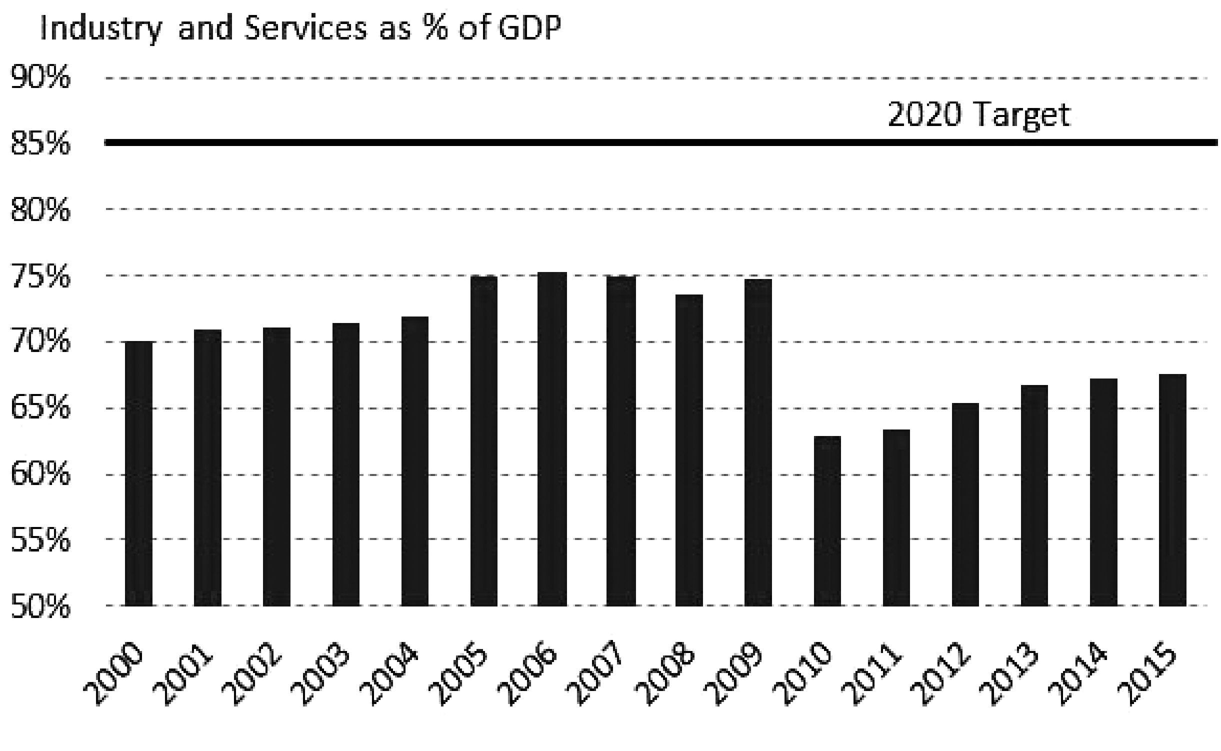


Figure 11. **Contribution of industry and services to GDP**

Source: General Statistics Office of Vietnam.

Table 8. **Social capital expenditure**

	Trillion dong	% of Total
State budget	220.40	16
Government bonds	61.70	5
Investment capital credit under state plan	62.50	5
Loan from other sources (of state sector)	86.80	6
Equity of State-owned Enterprises	66.90	5
Capital of households and private individuals	529.60	39
Foreign Direct Investment	339.30	25
Total	1,367.20	

Sources: General Statistics Office of Vietnam, with Markit calculations.

for which data are available) consumption fell at a faster pace than required by the target. However, before that usage was rising, thereby adding an element of doubt to the optimistic prediction.

7. Urbanization rate of between 38% and 40% by 2020

Based on recent trends this target looks like it will be tricky to meet. Currently, the urban population makes up 33% of the total (Figure 13), and if the proportion continues to rise at current rates it will only be at 37.3% by 2020, short of the lower band required by the target.

Urbanization has been relatively recent in Vietnam. Until the 1980s, the government's focus on agriculture encouraged workers to stay in rural areas, and as late as 1990 only 20% of the population lived in cities (Figure 13). Deeper economic reform and less-constrained rural — urban migration from the mid-1990s triggered rapid growth in cities, which developed as centers for services and manufacturing. Over the past 2 decades, the number of urban dwellers

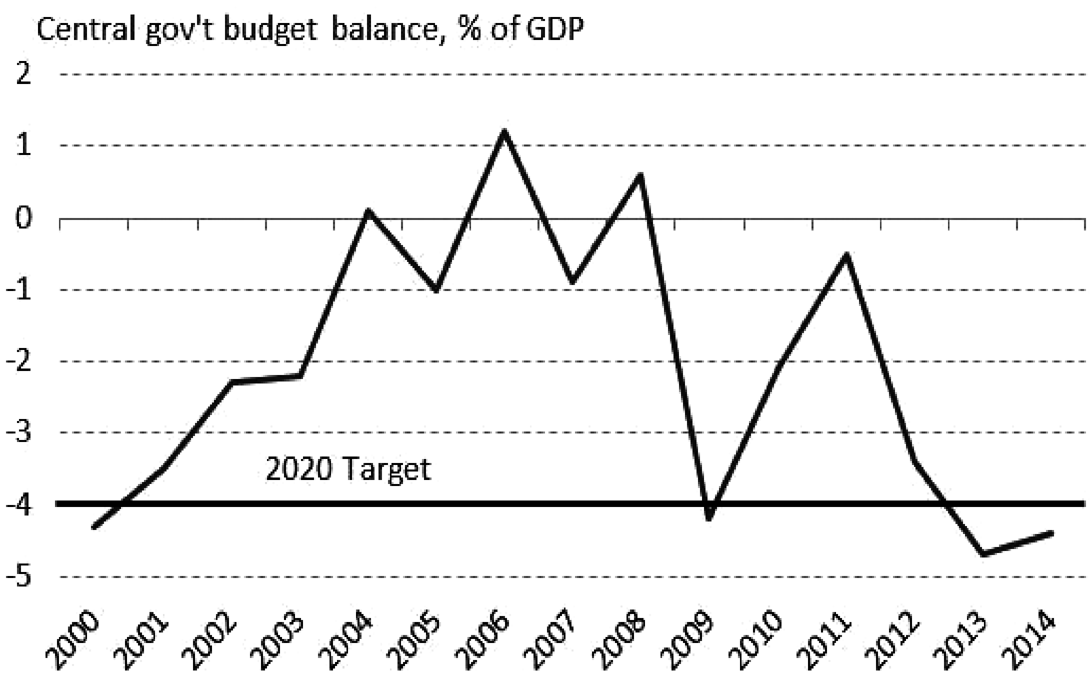


Figure 12. **Central government budget balance, % of GDP**

Sources: General Statistics Office of Vietnam.

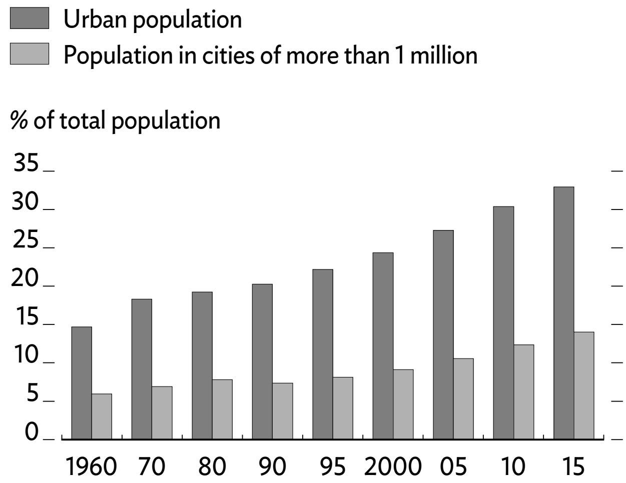


Figure 13. **Urban population in Vietnam**

Source: The World Bank, World Development Indicators online database (accessed 26 August, 2016).

has jumped to 31 million, or 34% of the population, and is projected to reach 46 million, or 44%, by 2030.

Growth in urban centers and formal employment are important drivers of the economy, as illustrated by estimates that show at least 70% of GDP is now generated in cities. However, urban transportation networks, water and sanitation systems, health and education services, and other physical and social infrastructure have struggled to keep pace. Moreover, rapidly rising urban populations strain natural resources and pollute the environment. To remain a vibrant industrializing economy, Viet Nam will need to develop more efficient urban centers that can support much larger populations. Achieving this will require progress on three fronts.

The first is urban planning. The current planning law stresses decentralized urban planning and stakeholder consultation, which requires more urban planning and management capacity in provincial and local governments. Too often, master plans are idealized visions of future cities that do not take into account the real needs of households, businesses, or local governments.

Second is the funding of urban infrastructure. Outside of Ha Noi and Ho Chi Minh City, few urban governments can raise enough revenue for infrastructure on their own, leaving many heavily dependent on the central government annual budget. This inhibits infrastructure development because local governments need multiyear funding commitments to complete projects such as upgrades to citywide drainage systems. Funding can be even more difficult for critical projects that generate little revenue, such as sewerage, which typically require significant official development assistance from abroad.

For lack of own-source funding, urban authorities sometimes rely on private developers to provide infrastructure through land-for-development deals. Such deals can undervalue public land and build low-quality infrastructure. Further, a model of urban development driven by developers can distort supply by, for example, overinvesting in higher-end housing and underinvesting in homes for the urban poor.

Table 9. **Urban population % of total population**

Year	Urban population	Population in cities of more than 1 million
1960	14.7	5.9
1970	18.3	6.9
1980	19.2	7.8
1990	20.3	7.4
1995	22.2	8.1
2000	24.4	9.1
2005	27.3	10.6
2010	30.4	12.4
2015	33.0	14.0

Source: World Bank, World Development Indicators online database (accessed 26 August, 2016).

These issues can be addressed by strengthening provincial planning, creating medium-term frameworks for funding urban services, and encouraging provincial governments to deemphasize their role as investors and focus more on planning and regulating urban services, land use, and the stewardship of natural resources.

In northern and central Vietnam, over 3,200 km of rural roads were rehabilitated between 2006 and 2014, and the share of people living within 2 km of an all-weather road increased from 76 percent to 87 percent.

Finally, urban development needs to take the environment into account. Land-for-development deals often create urban sprawl and build inappropriately in high-risk areas, including floodplains. Moreover, the present planning system does not encourage governments to effectively incorporate climate change into urban plans. As a result, cities often focus on expansion and give inadequate attention to climate and disaster risks.

Targets 8 and 9: Total Factor Productivity contributing 30% to 35% of growth, with labour productivity increasing 5% per year on average

Limited data availability regarding these targets makes them difficult to evaluate. Labour productivity grew above target (6.4%) in 2015, but below (4.3%) in 2014. Overall, most of the named targets look to be achievable, particularly if global economic conditions are stable and the TPP comes into effect as planned. The biggest challenges look to be around the proportion of GDP accounted for by industry and services and the rate of urbanisation. Meanwhile, PMI data will provide a useful monthly signal as to how the economy is faring over the five-year period.

SEPARATE LEAF FISCAL DECENTRALIZATION IN VIETNAM

Report "*Making the Whole Greater than the Sum of the Parts: A Review of Fiscal Decentralization in Vietnam*", prepared by The World Bank in Vietnam, 2015, provides a review of fiscal decentralization policies in Vietnam and their impact on the Government's development objectives. It aims to inform reform of central-local fiscal relations in Vietnam to further promote growth and poverty reduction. Study of fiscal decentralization therefore is central to understanding government spending in Vietnam and its significant impact on the country's successful record on economic growth and poverty reduction.

Local authorities have been granted increasing levels of fiscal responsibilities since the adoption of the *State Budget Law* (2002). It has enabled decentralization of important fiscal responsibilities to local authorities over the past ten years. The *SBL 2002* establishes the key principles for spending assignments, revenue arrangements, and intergovernmental fiscal transfers. It also grants provincial authorities a fair degree of autonomy to determine fiscal relationships with districts and communes within their jurisdiction. The current system allows a reasonable level of differential treatment across provinces to take account of their specific circumstances.

There is general acknowledgement that the *SBL 2002* has provided a solid framework for public finance management including intergovernmental fiscal relations. At the same time, after 10 years of implementation a number of issues arise such as: clarity of spending responsibilities and local level accountability including for national priorities and objectives; spending performance of local authorities; the effectiveness of local revenue arrangements in meeting spending needs and the potential for increased revenue autonomy for provinces; the extent to which provincial authorities are promoting or impeding central government's redistribution efforts; and the potential for increased debt financing for local authorities.

Local authorities in Vietnam are responsible for over half of total government spending, thanks to fiscal decentralization policies implemented over the past eighteen years. Total government spending in Vietnam is close to 30 percent of Gross Domestic Product; local authorities' spending is close to 17 percent of GDP. So, local fiscal policies have a significant impact on Vietnam's development. Thus it is necessary to look at the extent to which fiscal decentralization policies have achieved their development objectives.

Local fiscal policies in Vietnam determine decisions on public service delivery, and therefore the overall development trajectory of the country. Poor spending or revenue decisions at

Table 10. **Emerging Market and Developing Economies: Consumer Prices**[1]
(*Annual percent change*)

	End of Period2														
	Average									Projections				Projections	
	1998–2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2021	2015	2016	2017
Cambodia	3.8	25.0	−0.7	4.0	5.5	2.9	3.0	3.9	1.2	2.1	2.8	0.2	2.8	2.4	2.9
China	1.1	5.9	−0.7	3.3	5.4	2.6	2.6	2.0	1.4	1.8	2.0	3.0	1.6	1.8	2.0
Fiji	3.0	7.7	3.7	3.7	7.3	3.4	2.9	0.5	2.8	3.3	2.8	2.8	2.8	3.3	2.8
Indonesia	14.1	9.8	5.0	5.1	5.3	4.0	6.4	6.4	6.4	4.3	4.5	4.0	3.4	4.5	4.4
Lao P.D.R.	24.0	7.6	0.0	6.0	7.6	4.3	6.4	5.5	5.3	1.5	2.3	3.1	5.5	1.2	2.3
Malaysia	2.4	5.4	0.6	1.7	3.2	1.7	2.1	3.1	2.1	3.1	2.9	3.0	2.7	3.1	2.9
Mongolia	7.3	26.8	6.3	10.2	7.7	15.0	8.6	12.9	5.9	1.9	4.3	6.4	1.1	3.7	6.5
Myanmar	23.4	11.5	2.2	8.2	2.8	2.8	5.7	5.9	11.5	9.6	8.2	6.4	10.5	8.7	7.7
Papua New Guinea	8.6	10.8	6.9	5.1	4.4	4.5	5.0	5.3	6.0	6.0	5.0	5.0	6.0	6.0	5.0
Philippines	5.2	8.2	4.2	3.8	4.7	3.2	2.9	4.2	1.4	2.0	3.4	3.5	1.5	2.9	3.2
Solomon Islands	8.7	17.3	7.1	0.9	7.4	5.9	5.4	5.2	−0.4	2.1	2.6	3.1	2.2	2.9	2.6
Thailand	2.8	5.5	−0.9	3.3	3.8	3.0	2.2	1.9	−0.9	0.2	2.0	2.5	−0.9	1.6	1.8
Timor-Leste…		7.4	−0.2	5.2	13.2	10.9	9.5	0.7	0.6	1.5	3.8	4.0	−0.6	3.6	4.0
Vietnam	4.9	23.1	6.7	9.2	18.7	9.1	6.6	4.1	0.6	1.3	2.3	4.0	0.6	2.0	2.6

1. Movements in consumer prices are shown as annual averages.
2. Monthly year-over-year changes and, for several countries, on a quarterly basis.

For many countries, inflation for the earlier years is measured on the basis of a retail price index. Consumer price index (CPI) inflation data with broader and more up-to-date coverage are typically used for more recent years.

Source: World Economic Outlook, April 2016. International Monetary Fund.

local level, coupled with lack of transparency can lead to inefficient spending, unequal development across the country and reversal of the country's successful record of growth and poverty reduction. Despite the importance of fiscal decentralization in Vietnam's development, there has been little study on the successes and failure of policies and institutions in this area. The report responds to demands for more analysis of fiscal decentralization policies in Vietnam and the extent to which these have delivered on their intended objectives of equity and efficiency to promote economic growth and poverty reduction. It aims to inform future changes to the system of intergovernmental fiscal relations through revisions to the *SBL 2002* and adoption of ***2016–20 Stability Period regulations***. The SBL 2002 establishes the key principles for spending assignments, revenue arrangements, and intergovernmental fiscal transfers. It also grants provincial authorities a fair degree of autonomy to determine fiscal relationships with districts and communes within their jurisdiction. There is general acknowledgement that the SBL 2002 has provided a solid framework for public finance management including intergovernmental fiscal relationships.

The report responds to demands for more analysis of fiscal decentralization policies in Vietnam and the extent to which these have delivered on their stability, equity and efficiency objectives. It builds on existing research and aims to provide new analysis and perspectives on the above areas through extensive study of available data, consultations with central and local authorities, and reviews of laws, regulations and policies at central and local levels. It covers the following five pillars of fiscal decentralization:

(i) expenditure decentralization and accountability;

(ii) expenditure performance of local authorities;

(iii) local revenue arrangements;

(iv) intergovernmental fiscal transfers; and

(v) local borrowing.

Study of fiscal decentralization therefore is central to understanding government spending in Vietnam and its significant impact on the country's successful record on economic growth and poverty reduction. To date however there has been little analysis of how fiscal decentralization has enabled local authorities to effectively, efficiently and accountably spend money on public services for development. Spending decentralization has grown more quickly than information and knowledge on local fiscal policies in Vietnam.

After 10 years of implementation of the *SBL 2002*, a number of issues arise in relation to the system of intergovernmental fiscal relations. These include:

- clarity of spending responsibilities and local level accountability including for national priorities and objectives; spending performance of local authorities;
- the effectiveness of local revenue arrangements in meeting spending needs and the potential for increased revenue autonomy for selected provinces;
- the extent to which provincial authorities are promoting or impeding central government's redistribution efforts; and the potential for increased debt financing for local authorities within prudent limits.

To date however there has been little analysis of how fiscal decentralization has enabled local authorities to effectively, efficiently and accountably spend money on public services for development. Spending decentralization has grown more quickly than information and knowledge on local fiscal policies in Vietnam. This has prompted a number of questions from the National Assembly, the Central Government, and other stakeholders including:

How are local spending choices aligning with national level objectives?

How much spending responsibility do local authorities actually have?

Are current policies and institutions sufficient to ensure that the money is spent well and in line with citizens' needs?

How much do provinces spend on delivering a given level of public services and what might explain the differences?

What results are being achieved?

How effectively are local authorities able to raise revenues to finance local spending?

Are fiscal transfers sufficient to effectively cover all local spending needs?

Are transfers being equitably distributed?

Are there more opportunities for provinces to borrow to meet investment needs?

These are some of the questions that report tries to answer to help inform future changes to central-local fiscal relations. The report finds that fiscal decentralization policies have helped to channel more spending to the poorest parts of the country where development needs and costs of service delivery are higher. There is fairly wide variation in spending efficiency across provinces. Some of it is due to factors outside of local authorities' control (e.g. population density, geographic location). But the report also finds that money could be better spent through improvements in budget management and accountability.

The level of local revenue has increased over time, and the evidence suggests that the current policies do not impact negatively on revenue collection efforts. Another positive feature is that revenue and fiscal transfers have on the whole been quite equitable. However, local authorities currently have little to no autonomy over revenue policy and administration. Some autonomy over revenue can increase accountability between state and citizen and promote better use of the resources. It can also enable certain provinces to better meet their investment needs. The study finds that the latter can be complemented with some increase in local borrowing levels.

A combination of these measures should help to maintain the government's successful redistributive policies to meet social objectives, and enable high economic potential provinces to invest in growth enhancing initiatives, whilst enhancing transparency to ensure accountability. Lack of transparency and coordination in intergovernmental fiscal relations can lead to fragmentation and unequal development across the country. Intergovernmental fiscal relations should ensure that development efforts of all provinces exceed the sum of their individual parts so that they can help eliminate extreme poverty and promote shared prosperity in Vietnam.

FREE TRADE AGREEMENTS

Trade contributes to economic performance by improving productivity and by giving producers and consumers access to greater varieties of goods at lower prices[3]. It also stimulates competition and encourages technology and investment flows. Countries have long pursued these benefits by gradually reducing tariffs through the General Agreement on Tariffs and Trade (GATT) and World Trade Organization (WTO) agreements, enabling world trade to grow twice as fast as output. In recent years, however, global negotiations have ebbed, NTBs have become more prevalent[4], and world trade growth has slowed.

Since the rebound from the great trade collapse of 2008–09, when world trade fell by much more than GDP, global trade growth has slowed notably, both in absolute terms and relative to world GDP growth. This slowdown has been more pronounced in emerging market and developing economies, where it intensified in 2015. In the two decades leading up to the global financial crisis, international trade expanded rapidly, at a pace roughly double that of world GDP. World trade volume growth, however, has moderated notably in recent years, both in its level and relative to GDP growth. As a result, the increase in trade as a share of global GDP has decelerated.

The slowdown in trade has been remarkably widespread. An analysis of recent trade patterns of 174 individual countries reveals that trade growth has weakened in an overwhelming majority of countries.

This holds true even after the weak growth in income and the decline in trade prices are taken into account. Most countries have been importing less, relative to their incomes during 2012–15, than in the years leading up to the global financial crisis. For 65 percent of the countries, accounting for 74 percent of global imports, the ratio of average import volume growth to GDP growth (a simple measure of the income elasticity of import demand) observed during 2012–15 was below that during 2003–06.

The observed slowdown in import income elasticity has been more pronounced in emerging market and developing economies than in advanced economies[5].

[3] The relationship between trade and economic performance has been widely studied; see, for example, WTO and World Bank (2015), OECD and WTO (2013), Stone and Shepherd (2011), Wacziarg and Welch (2008), and Sachs and Warner (1995).

[4] Evenett, Simon J., and Fritz, Johannes. 2015. The Tide Turns? Trade, Protectionism, and Slowing Global Growth: The 18th Global Trade Alert Report. Geneva: Centre for Economic Policy Research. Available at: www.voxeu.org/sites/default/files/file/GTA18_final.pdf.

[5] World Economic Outlook, April 2016. *Too Slow for Too Long*. World Economic and Financial Surveys, International Monetary Fund, 2016.

Today's lower tariffs, improved logistics, and better information systems enable firms to exploit gains from international specialization far more extensively than they did in the past. Firms in the United States and elsewhere have developed complex global value chains, often focused on the Asia Pacific, to raise productivity. These systems, along with new areas of economic integration made possible by technology, have stimulated demand for still lower trade barriers, better connectivity through ports and communications, and clearer, more coherent rules to facilitate international business operations.

Global trade negotiations have failed to keep pace with these trends. To fill the vacuum, more than 220 free trade agreements (FTAs) have been signed and in effect in the Asian region alone (see Table 11). Yet bilateral or small regional FTAs are 'second-best' strategies for deeper integration. To take advantage of an FTA, exporters have to prove that they meet 'rules of origin' (ROO)[6] and often cannot do so in an agreement that does not cover complete supply chains. Also, smaller FTAs tend to focus on narrow, regional goals and have little influence on global rules. They also tend to be inefficient, as they encourage the use of costly products from FTA partners instead of those efficiently produced by non-partners.

Absent effective global negotiations, large and ambitious regional agreements — frequently called megaregional agreements — offer a way forward. They can include a sufficient number and range of partners to limit the costs of trade diversion and to have an impact on global rules. Yet their membership can be small enough to reach compromises on difficult issues. The TPP is the first megaregional agreement concluded in over two decades (the European Single Market and the North American Free Trade Agreement were similar in ambition) and could have large, systemic effects.

Global Economic Prospects, June 2016. *Divergences and Risks*. A World Bank Group Flagship Report, International Bank for Reconstruction and Development/The World Bank, 2016.

[6] Rules of origin ensure that only goods primarily produced in an FTA zone are eligible for tariff preferences. A producer might have to prove, for example, that inputs in the production process that originate outside the zone fall below a percentage limit or consist of different products in terms of the customs classification.

After years of negotiations, agreement on the TPP trade deal was reached on October 5th, 2015. Vietnam is one of 12 countries (Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, United States of America, Vietnam) currently part of the agreement which now passes on to the signing and ratification stage. This is potentially a lengthy process with the possibility of political difficulties in a number of countries. For example, the new Canadian government has expressed some scepticism about the deal in the past, while doubts are also present in the US and Japan. However, if and when it is finally implemented, the deal has the potential to provide a major boost to export trade at Vietnamese manufacturing firms.

The Trans-Pacific Partnership (TPP), concluded on October 5, 2015, reflects inevitable compromises but appears to have met its two key objectives: to establish new, market-oriented rules in a host of rapidly changing areas of international commerce and to reduce trade and investment barriers among TPP countries to yield considerable gains for the United States and its 11 partners.

The TPP is a landmark accord. In 2014 its member countries had combined GDP of $ 28 trillion, or 36 percent of world GDP, and accounted for $ 5.3 trillion in exports, or 23 percent of the world total[7]. They are unusually diverse, comprising low-, middle-, and high-income countries with varied economic systems. The agreement itself is deep and comprehensive, targeting economic integration with provisions that range from goods, services, and investment to critical new issues such as the digital economy, intellectual property rights, regulatory coherence, labor, and the environment. The role of the TPP in launching international cooperation on so-called *next-generation trade rules* cannot be assessed at this time, but it may prove to be its most valuable contribution in the long run.

Economic modeling can show, however, the effects of the scheduled liberalization elements of the TPP, provided it is ratified by its members. The estimates reported here suggest that the TPP will increase annual real incomes in the

[7] Data from the World Bank's World Development Indicators database.

Table 11. **FTA Status by Country/Economy, 2015 (as of February 2016)**

COUNTRY/ ECONOMY	Under Negotiation		Signed but not yet In Effect	Signed and In Effect	TOTAL
	Framework Agreement signed	Negotiations launched			
Afghanistan	0	0	1	1	2
Australia	0	5	0	12	17
Bangladesh	0	2	1	3	6
Bhutan	0	1	0	2	3
Brunei Darussalam	0	2	0	8	10
Cambodia	0	2	0	6	8
China, People's Republic of	0	7	0	16	23
Fiji	0	2	0	3	5
Hong Kong, China	0	1	0	4	5
India	1	14	0	13	28
Indonesia	0	7	1	9	17
Japan	0	8	1	14	23
Korea, Republic of	0	8	1	15	24
Lao PDR	0	2	0	8	10
Malaysia	1	5	1	14	21
Mongolia	0	0	1	0	1
Myanmar	1	3	0	6	10
Nepal	0	1	0	2	3
New Zealand	0	5	0	11	16
Pakistan	0	6	2	10	18
Papua New Guinea	0	2	0	4	6
Philippines	0	4	0	7	11
Singapore	0	8	1	20	29
Sri Lanka	0	2	0	5	7
Taipei,China	1	1	0	7	9
Thailand	1	8	0	13	22
Viet Nam	0	5	1	9	15
TOTAL	5	111	11	222	349

Notes:
1. *Framework* Agreement signed: The parties initially negotiate the contents of a framework agreement (FA), which serves as a framework for future negotiations.
2. *Negotiations* launched: The parties, through the relevant ministries, declare the official launch of negotiations or set the date for such, or start the first round of negotiations.
3. *Signed* but not yet in effect: Parties sign the agreement after negotiations have been completed. However, the agreement has yet to be implemented.
4. *Signed* and in effect: Provisions of FTA come into force, after legislative or executive ratification.

Source: Asian Development Bank. Asia Regional Integration Center: https://aric.adb.org/fta (accessed on August 26, 2016).

United States by $ 131 billion[8], or 0.5 percent of GDP, and annual exports by $ 357 billion, or 9.1 percent of exports, over baseline projections by 2030, when the agreement is nearly fully implemented. Incomes after 2030 will remain above baseline results by a similar margin. Both labor and capital will benefit, but labor will get a somewhat more than proportionate share of the gains in total.

Given these benefits, delaying the launch of the TPP by even one year would represent a $ 94 billion permanent loss, or opportunity cost, to the US economy as well as create other risks. Postponing implementation will give up gains that compound over time and defer or foreclose new opportunities for the United States in international negotiations. Unexpected political challenges or competing trade projects may also erode decisions in partner countries, further increasing the costs from delaying TPP ratification. While the United States will be the largest beneficiary of the TPP in absolute terms, the agreement will generate substantial gains for Japan, Malaysia, and Vietnam as well, and solid benefits for other members.

Given these wider objectives, TPP negotiators sought to eliminate traditional barriers as well as update rules to meet business and social goals. In the event, the tariff reductions in the TPP are deeper and wider than anticipated, including in 2012 study[9]. The TPP will eliminate three-quarters of nonzero tariffs immediately on entry into force (EIF), and 99 percent when fully implemented[10].However, it will include some divergences even among intraregional tariffs: Although most of its tariff schedules treat partners equally, some schedules, including those of the United States, retain differences among them.

Comprehensive rules are the most distinctive aspect of the TPP. In some areas the agreement builds on the WTO rulebook but tightens disciplines and creates new mechanisms to improve implementation. It includes more comprehensive rules for service trade and investment than were in WTO agreements and allows exceptions only on a negative-list basis. It improves mechanisms for setting food standards and technical barriers and for assessing the conformity of products with them, and begins to cut through the 'spaghetti bowl' of overlapping trade agreements by establishing a single set of ROO that allows inputs produced in any TPP member to count toward meeting ROO standards. The TPP also strengthens intellectual property (IP) rights and prescribes greater commitments toward enforcing them[11], and it has more comprehensive and enforceable rules on labor and the environment than previous agreements.

In other areas the TPP breaks new ground with provisions that were absent from or tangentially addressed by prior agreements. It sets new standards for access to telecommunication networks, prohibits tariffs on electronic commerce, limits restrictions on cross-border data transfers, and rules out data localization requirements. It also brings state-owned enterprises (SOEs) more clearly under international rules, ensuring that their purchases and sales are on a commercial basis, including their service exports and foreign investments. It has special chapters on trade facilitation and small and medium enterprises (SMEs) in order to improve access to online platforms and to make regulations simpler and easier to meet. Many of these provisions are enforceable under a new dispute settlement mechanism.

Large gains are also projected for Japan, Malaysia, and Vietnam. Japan benefits from improved market access throughout the TPP region, including early liberalization of auto imports in markets other than the United States,

[8] Peter A. Petri and Michael G. Plummer. *The Economic Effects of the Trans-Pacific Partnership: New Estimates*. Working Paper series, WP 16–2, January, 2016. Estimates are in constant 2015 dollars. The apparent precision of the estimates should not be misinterpreted. Exact numerical results are provided to help readers compare relative magnitudes and check the internal consistency of results, but estimates could be one-third larger or smaller — as sensitivity analyses indicate— due to uncertainties in data and assumptions.

[9] Petri, Peter A., Plummer, Michael G., Zhai, Fan. (2011). *The Trans-Pacific Partnership and Asia-Pacific Integration: A Quantitative Assessment*. East-West Center Working Papers, Economics Series, No. 119, October 24, 2011.

[10] Freund, Caroline, Tyler Moran, and Sarah Oliver. 2016 (forthcoming). *Tariff Liberalization*. In *Assessing the Trans-Pacific Partnership*, volume 1. PIIE Briefing 16–1. Washington: Peterson Institute for International Economics.

[11] Additional areas covered in the IP chapter include explicit coverage of state-owned enterprises so that they cannot evade IP rules, enhanced penalties for counterfeits that threaten public health and safety, and digital copyright policies. Data exclusivity for biologic products was set at five years, with additional measures to reach eight-year effective protection (but not 12 years, as US negotiators had sought).

and from domestic reforms that reduce distortions in its protected service and investment sectors. Percentage gains are especially large for *Vietnam* and *Malaysia*, where the agreement should also stimulate domestic reforms and provide access to protected foreign markets. Other significant percentage gains are projected for the smaller economies of Brunei, Peru, Singapore, and New Zealand.

The TPP is not generally estimated to have large income effects on nonmembers. Some gain and others lose, the latter to the extent that the TPP diverts trade from nonmembers to members or erodes previous preferences in TPP markets. Losses are tangible for China, India, and Thailand, which compete with TPP members for TPP markets, and for Korea, because the TPP will erode that country's advantage in US markets under KORUS. But except for Thailand, these losses are small compared with GDPs. Some nonmembers, including the European Union and Hong Kong, experience net gains, in part because of the assumption that TPP provisions liberalize some trade with nonmembers.

As the TPP awaits ratification, the timing of its implementation is uncertain. The central results assume EIF in 2017. In an alternative simulation, we repeat the TPP experiment but delay the launch of implementation — the start of staged reductions of trade barriers — to 2018, keeping other assumptions unchanged.

In the simulation of a one-year delay, the benefits in every future year are lower than in the central scenario with EIF in 2017. Given that gains consist of a stream of future benefits, the «value» of the agreement can be calculated as a present value, the discounted sum of future benefits. This is similar to the calculation a business would apply in determining the value of an investment project. Table 5 shows the present value of the TPP with several plausible discount rates, ranging from $ 961 billion to $ 2,316 billion for the United States if the TPP is implemented in 2017, and across lower values if it is delayed. A one-year delay thus results in permanent losses from $ 77 billion to $ 123 billion for the United States and $ 308 billion to $ 525 billion for the world.

Delaying the TPP could generate still further, unquantified risks for the conduct of US commercial diplomacy. Given political uncertainties in many TPP member economies, some that are prepared to ratify the TPP now may be unwilling to do so later, and in that case the benefits to be realized will shrink. The benefits might be also reduced if, while waiting, TPP members choose to advance alternative free trade arrangements to hedge their bets. And other trade and investment initiatives that the United States is or could be involved in — including high-valued negotiations with Europe and on the enlargement of the TPP itself — would have to be delayed or possibly abandoned, with corresponding costs.

Once in place, the TPP is likely to promote additional integration in the Asia-Pacific region and beyond, with larger attendant gains. It is potentially a pathway to the Free Trade Area of the Asia-Pacific (FTAAP), which could include all APEC members and, based on our earlier studies, more than double the gains for the United States. The *Transatlantic Trade and Investment Partnership*, in negotiation since 2013, would also have large effects. And broader global negotiations may pick up steam. These and other initiatives would benefit from competitive pressure from the TPP.

Once fully implemented, the Trans-Pacific Partnership (TPP) trade agreement should greatly benefit exporting manufacturers in Vietnam as barriers to trade are removed, aiding their competitiveness overseas. Let's look at some of the reasons for optimism among Vietnamese firms.

One of the key tenets of the deal (the details of which are largely secret at this stage) will revolve around the removal of trade barriers between the participating nations. The removal of tariffs on Vietnamese goods exports to countries such as the US would boost the price competitiveness of Vietnamese producers, particularly compared with competitors who aren't part of the agreement, notably **China**. Moreover, a number of commentators, including ratings agency Fitch[12], estimate that Vietnam will be the biggest gainer of the 12 countries currently part of the agreement. One of the reasons for optimism among Vietnamese firms revolves around the types of goods they produce.

Vietnam could see a significant boost to long-term economic growth, investment and exports, should the Trans-Pacific Partnership (TPP) agreement drafted on 5 October be ratified, says

[12] https://www.fitchratings.com/site/pr/992111

Fitch Ratings. Of the 12 countries that are party to the TPP, models suggest Vietnam would see the biggest benefits in terms of economic impact.

Vietnam could see a positive economic growth effect in excess of 10% over the 10 years to 2025 under the TPP agreement, according to the estimates of one study by Petri, Plummer and Zhai[13]. Fitch believes that the agreement would have significant impact on two key areas in Vietnam — trade and domestic economic policy.

The free trade elements of the TPP will lower tariff barriers, giving Vietnam greater access to large consumer markets in the US, Japan, Canada and Australia. TPP signatories accounted for 39% of Vietnam's total exports and 23% of imports in 2014. The potential positive effect on trade could be transformative, with the aforementioned study estimating the TPP will boost Vietnam's exports by over 37% over 10 years. Notably, Vietnam in August also concluded the terms of a free trade deal with the European Union, putting it on course to complete free trade agreements with three of its four largest export destinations — the EU, Japan and the US.

The agreement does much more than just lower tariff barriers — it also aims to address wide-ranging barriers to trade by setting rules governing intellectual property rights, business competition policies including those related to state-owned enterprises, public procurement policies, supra-national dispute resolution, and labour standards. As such, the TPP has the potential to act as a key policy anchor for structural reforms and economic liberalization that could bolster productivity and foreign investment for Vietnam.

Vietnam already benefits from high GDP growth and stable FDI inflows. GDP growth accelerated to 6.5% over the first three quarters of 2015, implying a 3Q growth rate of 6.9% yoy versus 6.5% in 2Q. Strong and improving macroeconomic stability was a key driver of Vietnam's upgrade to 'BB-'in November 2014.

But further upside for Vietnam's rating will likely continue to be challenged by wide fiscal deficits and high public debt. Fitch estimates the general government deficit will rise to 6.9% of GDP in 2015 from 6.1% in 2014. Public debt levels (excluding guarantees) have grown to 45% of GDP, though this is broadly in line with the 'BB' peer median of 41%. External finances have been strength for Vietnam in recent years, but a pickup in credit growth thus far in 2015 has spurred demand for imports and squeezed the trade account. Fitch estimates this will likely drag the current account surplus to under 1% in 2015 from 5% in 2014.

Implementation risks could be significant as the TPP agreement heads to national legislatures for ratification. Opposition in the US from Congress and leading presidential candidates in the lead up to the 2016 elections there could yet scupper or delay the TPP. Within Vietnam, while ratification is more likely, there could be difficulties in implementing some areas of structural reform.

Data suggest that the Textiles and Apparel sector has been one of the main areas of negotiation, an important area for manufacturers in Vietnam with textiles and footwear combined accounting for almost one-fifth of their exports.

TPP membership will also provide a meaningful boost because Vietnamese firms will be able to leverage existing established trade relationships, which are by no means confined to its near neighbors. The other TPP members currently account for around two-fifths of Vietnam's exports, with 17% to the US alone. With trade set to become easier with these countries, their importance as export destinations will likely increase.

Aside from the potential benefits from the removal of barriers to trade, the TPP also covers some elements that might prove problematic for Vietnam to implement. Protection for labour rights, particularly with regards to industrial relations, would require a loosening of central control. Meanwhile, stricter environmental standards could add to costs for firms as they are forced to adapt. However, the overall impacts of the deal should be positive and any reforms in the aforementioned areas will help the economy in the longer term. The fact that the government has agreed to a deal which will reduce some of their own control highlights how positive they perceive the overall agreement to be.

With Vietnam currently one of the best-performing Asian emerging markets, the country

[13] Petri, Peter A., Plummer, Michael G., Zhai, Fan. (2011). *The Trans-Pacific Partnership and Asia-Pacific Integration: A Quantitative Assessment*. East-West Center Working Papers, Economics Series, No. 119, October 24, 2011.

Table 12. **Key Export Goods for Vietnam**

Sector	Share of Vietnam export, %
Textile, sewing products	13
Electronic parts (including TV parts), computer and their parts	7
Footwear	6
Fishery products	5
Wood and wooden products	4

Source: Government Statistics Office of Vietnam.

Table 13. **Exports to other TPP countries**

Country	Share of Vietnam exports (2012), %
USA	17
Japan	11
Malaysia	4
Australia	3
Singapore	2
Canada	1
Mexico	1
New Zealand	0
Chile	0
Peru	0
Brunei	0

Source: Government *Statistics Office of Vietnam.*

is well placed to build on this strength once the benefits of the TPP are realized. The government will therefore hope that the ratification process will run smoothly and without too much delay. Once more details on the agreement are released it will be easier to determine how firms will be able to gain from its eventual implementation and what pitfalls might lay ahead.

TOWARDS 2035

Vietnam is transitioning to a market-based economy. Since the launch of Đôi *Mói* in 1986, Vietnam has recorded significant and historic achievements. Success from reforms raises expectations for the future, and there is a firm aspiration that by 2035, Vietnam will be a modern and industrialized nation moving toward becoming a prosperous, creative, equitable, and democratic society. Motivated by these aspirations, the Government of Vietnam and the World Bank Group jointly prepared the "***Vietnam 2035: Toward Prosperity, Creativity, Equity and Democracy***" report that gives further shape to Vietnam's aspirations, highlights the key development challenges that remain, and outlines a series of policy recommendations to help Vietnam achieve its 2035 goals. Vietnam 2035 report recognizes six key transformations:

(1) to enable economic modernization with a competitive private sector firmly in the lead;

(2) to improve the country's technological and innovative capacity;

(3) to reshape urban policies and investments for more dynamic cities and urban centers;

(4) to chart an environmentally sustainable development path with increasing adaptation and resilience to changing climate patterns;

(5) to promote equality and inclusion among marginalized groups for the development of a harmonious middle-class society; and

(6) to establish a modern rule of law state and a democratic society.

Vietnam 2035 report structures these transformations and the reform agenda around **three key pillars**:

- balancing economic prosperity with environmental sustainability;
- promoting equity and social inclusion; and
- enhancing the capacity and accountability of the state.

Besides advisory work, as of March 2016, the World Bank has provided almost US$ 21 billion in grants, credits and concessional loans to Vietnam. Vietnam's existing portfolio consists of 45 IDA/IBRD projects and trust funds operations, with total net commitments of US$ 8,745 billion.

Vietnam received the first loan from the IBRD, the Bank's lending arm for middle-income and poorer creditworthy countries, in 2009, to support a program of public investment reforms. By now, IBRD has committed over 2.8 billion USD to Vietnam, helping the country advancing quicker in its development path.

Four aspects of the approach to reforms proved most effective. ***First***, Vietnam chose to be pragmatic and flexible, both in the sequencing and the pacing of reforms. Reforms were introduced incrementally, after extensive consensus building, and wholesale shock therapies were avoided. And if internal or global experience suggested course correction, the system proved adaptable. *Second*, Vietnam played to its strengths by focusing on labor-intensive production and agriculture. *Third*, the emphasis on building human capital was early and effective. Vietnam already had relatively high levels of literacy and life expectancy. The human-capital base was further expanded following *Đôi* ***Mói***, enhancing the returns on the market-oriented reforms that followed. *Fourth*, where a domestic consensus was harder to forge, Vietnam used its commitments under external trade agreements to good strategic effect, particularly to usher in some of the more complex enterprise reforms. Each of these four aspects of the approach remains important for the next generation of reforms.

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