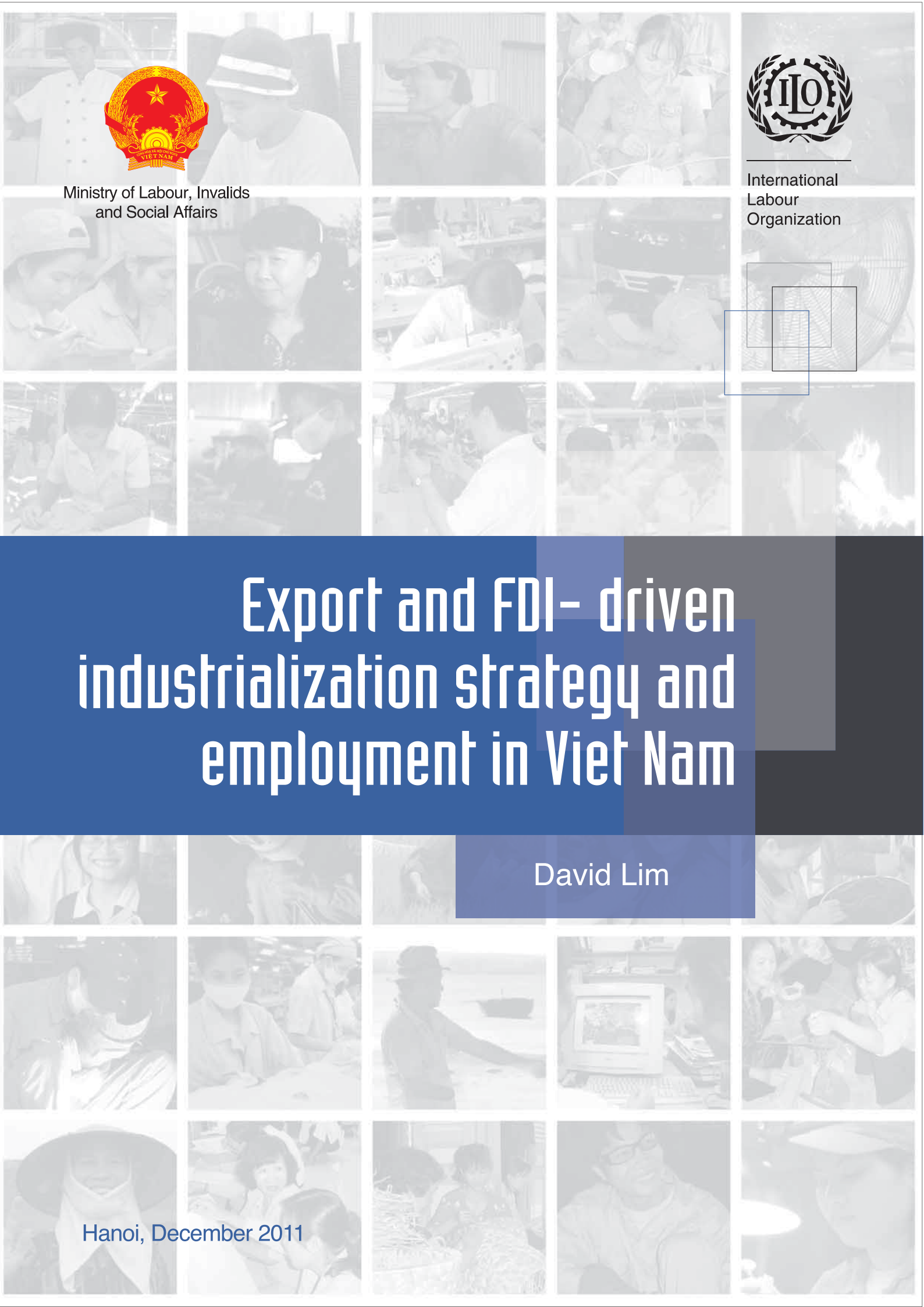

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Export and FDI- driven industrialization strategy and employment in Viet Nam

David Lim

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STRATEGY AND EMPLOYMENT IN VIET NAM

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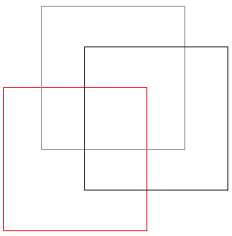

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Foreword

In December 2007, the Ministry of Labour, Invalids and Social Affairs of Vietnam (MOLISA) signed a Memorandum of Understanding (MOU) with the ILO. The primary aim was to provide MOLISA with policy advice and capacity building to support the integration of decent work and employment policies and strategies into Vietnam's national development framework. More specifically, this meant the ILO's technical advisory services to MOLISA would be anchored in Vietnam's five-year Socio-economic Development Plan (SEDP) for 2006-2010, ten-year Socio-Economic Develoment Strategy (SEDS) for 2011-2020, and the new phase of SEDP (2011-2015). This MOU was followed by an ILO mission to Hanoi in September 2008 that laid the groundwork for intensive collaboration between the ILO and MOLISA on the content and formulation of the Vietnam Employment Strategy 2011-2020 and in mainstreaming employment issues in the SEDS and SEDP. A number of tripartite consultations were held since September 2008 to identify priorities, following which several thematic studies were prepared by international and national consultants. These studies were peer reviewed in workshops and seminars before being finalized.

The results achieved over the past two decades in poverty reduction pair with less impressive achievements, especially in the creation of decent work for those who want to work. Agriculture provides full-time or shared work that has low productivity with pay and conditions that do not meet the requirements of decent work. The same can be said of that part of the services sector that provides employment of last resort. The manufacturing sector, from which much has been expected, does not have the desired labour-absorptive capacity and does not compare well with other ASEAN manufacturing sectors. A significant percentage of the labour force remains vulnerable, with incomes so close to the poverty line that only a small rise in expenditure or fall in income will push them below it. The much-lauded success in reducing poverty may not be what it seems. Youth unemployment is high and probably understated. Gender disparities are not a critical issue but disparities based on location and the statuses of workers are.

The study, Export and FDI-driven industrialization strategy and employment in Vietnam, prepared by Dr. David Lim, presents an analysis of trade and investment aspects after Viet Nam's WTO accession in January 2007, a review of its impacts on the world of work, as well as some policy implications to orient the current plan of economic reforms towards the creation of decent jobs for Vietnamese workers.

This study offers a number of recommendations for policies and institutions for employment promotion. The recommendations reflect ILO inputs to the Vietnam Employment Strategy 2011-2020. They also reflect the main outcomes of the several rounds of consultations that were undertaken in formulating the strategy which were led by MOLISA and included other ministries, in particular MPI, the National Assembly, Workers and Employers' organizations and key academics and researchers. Financial support from the Employment Policy Department of the ILO is also gratefully acknowledged.

This policy paper synthesizes the main elements of ILO technical support to the MOLISA on how investment and trade policies affect the characteristics of the model of growth, and conse-

quently its employment outcomes. It provides the foundation, based on a process of intensive collaboration with the government and social partners in Vietnam, for a coherent socio-economic framework for productive employment generation.

Acronyms and abbreviations

ADB	Asian Development Bank
ASEAN	Association of South East Asian Nations
CIE	Centre for International Economics
CIEM	Central Institute of Economic Management
CPRGS	Comprehensive Poverty Reduction and Growth Strategy
DBR	Doing Business Report
FDI	Foreign direct investment
GDP	Gross domestic product
GSO	General Statistical Office
ICA	Investment Climate Assessment
ICS	Investment Climate Survey
ILO	International labour Organisation
ILSSA	Institute for Labour Studies and Social Affairs
MDG	Millennium Development Goal
MOLISA	Ministry of Labour, Invalids and Social Affairs
PCI	Provincial Competitiveness Index
SBV	State Bank of Vietnam
SCIC	State Capital Investment Corporation
SEDP	Socio-Economic Development Plan
SME	Small and medium-sized enterprise
SOCB	State-owned commercial bank
SOE	State-owned enterprise
STAR	Support for Trade Acceleration
UNESCO	United Nations Education, Children and Science Organisation
UNICEF	United Nations Children's Fund
UNCTAD	United Nations Conference for Trade and Development
USAID	United States Agency for International Development
WTO	World Trade Organisation

Executive Summary

1. Since the 'doi moi' reforms, Vietnam has pursued an export-oriented industrialization strategy that seeks also to attract foreign direct investment (FDI), integration into the global economy and eventual accession to the World Trade Organization (WTO), which it achieved in January 2007. This has produced rapid growth in the real GDP, exports, FDI and domestic private investment, and a significant fall in the share of the state-owned sector in the economy. The percentage of the labour force in paid employment, the hours worked and real wages have grown significantly. And most of the targets set for the United Nations' Millennium Development Goals have been met, including the reduction in the incidence of poverty, which has been spectacular. Thus, the achievements of Vietnam since 1986 on the economic and social fronts have placed it in the forefront of development successes. It became the envy of less successful developed countries and earned it much praise from international development agencies and independent observers.

2. However, the record in some areas has been less impressive, especially in the creation of decent work for those who want to work. Agricultural provides full-time or shared work that has low productivity, with pay and conditions that do not meet the requirements of decent work. The same can be said of that part of the services sector that provides employment of last resort. Manufacturing sector, on which much has been expected, does not have the desired labour-absorptive capacity or that compares well with that in other ASEAN manufacturing sectors. A significant percentage of the labour force remains vulnerable, with incomes so close to the poverty line that only a small rise in expenditure or fall in income will push them below it, so that the much lauded success in reducing poverty may not be what it seems. Youth unemployment is high and probably understated. Gender disparities are not a critical issue but those based on location and the status of workers are.

3. The Vietnamese employment-output elasticity of manufacturing is low by ASEAN standards. This means that even if the Government's targeted annual real GDP growth rate of 8% for 2006-2010 is achieved, the number of jobs created, using the highest value obtained for the employment-output elasticity of 0.36, is only between 0.86 million and 1.25 million jobs, well short of the target of 1.6 million jobs. This reflects the fact that the growth generated by industries has not produced large numbers of well-paid and durable jobs. No where has this been brought out more clearly than in the state-owned enterprise sector, which contributes 34% of the GDP and over 20% of industrial production but only 9% of the total labour force. The same trend is shown in the FDI sector, which contributes 19% of GDP and 45% of industrial production but less than 4% of total labour force. The only sector that bucks the trend is the non-state domestic sector, which contributes 47% of the GDP and 35% of industrial production but employs more than 87% of the labour force.

4. The accession to the WTO so far has not helped much because exports have increased little as most of Vietnam's trading partners have already given it most-favoured nation status, and there has not been enough time for the full effect of membership to take place. The global financial crisis which began soon after the accession has also put paid to any expected increase in exports. The severe impact of the crisis on developing countries has produced calls for those with persistently large current account surpluses to spend more of this on domestic consumption and investment, and supply less cheap funds to spendthrift developed countries to indulge in current consumption and risky subprime mortgages. According to the 'global savings glut' theory, not only has the existence of the global imbalances brought about the crisis, it has also resulted in the sub-optimal allocation of

world resources and the morally indefensible transfer of resources from poor to rich countries. The theory per se des not apply to Vietnam because it has been a deficit country since 1980 but the severe impact of the crisis in the region has resulted in calls for it to de-link its growth from that of developed countries through trading more with other developing countries and producing more for domestic consumption. The scope for growth through greater trade with other developing Asian countries is limited because most it is in intermediate goods for use in exports to developed countries, while growth through producing more for domestic consumption and less for exports will take place as the economy grows. For the foreseeable future, Vietnam has to continue with its export-oriented strategy but has to pay more attention to increasing the competitiveness of its tradable sector, restructuring its industry, especially the state-owned enterprise sector, and strengthening its economic infrastructure.

5. An important reason for the export and FDI-driven industrialization not producing more employment is that the economic reforms to bring this strategy about have not gone far enough, and has continued the inappropriate use of the country's relatively abundant labour resources. Among the more important of the stunted reforms are those on trade and the state-owned enterprise (SOE) sector. While reform in trade policies has reduced the level of protection, the traditional bias in favour of import substitution and heavy industries and against labour-intensive manufactured goods for export remains, as production for the former enjoys higher rates of protection. If the tariff system had encouraged Vietnam to exploit its comparative advantage in cheap labour, manufacturing exports would make up significantly more of its exports, and created significantly more jobs. Other features of the tariff system also work against employment creation. The effective rate of protection is higher in industries dominated by state-owned and/or the foreign-invested enterprises, and lower in those with greater private sector participation, which are more labour-intensive. Profitability is larger in the more protected large and capital-intensive industries, which will direct more investment to them. The trade-policy regime resulted in encouraging output growth in industries that used very little labour.

6. The number of SOEs has been reduced significantly, the list of sectors quarantined for state ownership shortened substantially, the average size of the SOEs transformed increased, the equitisation process improved, and the efficiency of SOEs raised. However, the reform has been concerned mainly with the smaller SOEs, with the process completed only for a small percentage of the larger ones. The consolidation of many SOEs into larger firms to obtain greater economies of scale and develop their own brand names has not worked, as they continued to be protected from foreign competition. The subsequent move to convert them into 19 large conglomerates in strategic sectors will not work either because the virtual monopoly enjoyed will discourage them from taking advantage of WTO membership to break into foreign markets. Some of them have moved into real estate, where they have little expertise, in the search for quick returns, while others have founded or acquired controlling stakes in banks, which will allow them to finance risky intra-group expansion plans but with the risks borne by the country. Thus, in spite of all the reforms, the SOE sector remains inefficient, and its operation has a significant adverse impact on employment creation because of their size, capital-intensity and political influence enable them to crowd out more labour-intensive and efficient private enterprises.

7. A totally different reason for the export and FDI-driven industrialization strategy not producing more employment is that the very developments that succeeded in making it work have reduced the capacity of the economy to absorb labour. Among the more important of these are the significant increases in productivity and the much greater FDI inflows. At the start of its globalization, Vietnam's productivity was well below that of its competitors in Southeast Asia and elsewhere and this was increased substantially for it to succeed in the export market. As this was brought about by the use of more capital-intensive technology and not increases in product quality and/or greater capacity utilization, it led to significant job losses, except in industries where output increased more than proportionately. Greater FDI inflows have also affected employment creation adversely. The greater productivity of foreign firms from their size and use of more modern and capital-intensive technology, and the special treatment they receive from financial institutions on credit and from government on investment incentives and property rights have enabled them to crowd out more labour-intensive private domestic firms. The loss of employment by the displacement of domestic firms is not replaced because of the greater capital-intensity of foreign firms.

8. Much of the literature on employment creation in Vietnam has concentrated on the urban or manufacturing sector, probably because the data for analysing it is more available and of the belief that more work in the urban sector will provide work for the rural migrants. But this is unfortunate because agriculture is still the most important source of employment. Given this and the effect that an unhealthy agricultural sector will have on urban unemployment through increasing rural-urban migration, the greatest impact on the creation of decent employment in Vietnam may well lie in fostering faster agricultural growth. And for this, issues to do with bias in favour of import substitution, capital-intensive industries and the state-owned enterprises have less significance.

9. In any assessment of the policies that the Government has taken to create employment, it must be remembered that achieving the other equally important objectives of external balance, poverty reduction, and social and regional balance, in addition to the core ones of rapid economic growth and macroeconomic stability, has made the task a great deal more complicated. The type of policy instruments available has also changed, with direct intervention, so prevalent in the early 1990s, no longer possible because of globalization, and with interest rates determined, under a liberalised financial system, more by the market than government decreed. The emphasis is more on creating and overseeing the institutions that determine the behaviour of the market, with government intervening only to support the workings of the market. This combination of multiple development objectives and greater sophistication in the use of policy instruments makes macroeconomic management a great deal more challenging.

1. Introduction

1.1 Under the 'doi moi' policy of 1986 and subsequent reforms to transform the economy to a socialist one with a market orientation and integration into the global economy, Vietnam has adopted an export and foreign direct investment (FDI)-driven industrialization strategy. This study analyzes the impact of such a strategy on the creation of decent employment, as part of the 'employment, investment, trade and enterprise development' project of the MOLISA-ILO's National Employment Strategy Programme. As the accession of Vietnam to the World Trade Organisation (WTO) in January 2007 is a critical milestone in the process of global integration, and the global financial crisis came hot on its heel, the study also takes into account the impact of these two important events. And as the state-owned enterprise sector still dominates the economy, its impact will be also be examined.

1.2 Section 2 assesses the impact that the economic reforms, especially those that promoted international trade and FDI, have on economic growth and other macro economic and social variables, especially the creation of decent employment. Section 3 examines the impact of the WTO accession, and Section 4 that of the global financial crisis, assessing as well the viability of the suggested alternatives to trade in the wake of the crisis. Sections 5 to 7 identify some of the major determinants of decent employment. And Section 8 presents recommendations for increasing the capacity to create decent employment.

2. Impact of economic reforms on economic growth and employment growth

Economic growth

2.1 The reforms have resulted in rapid rates of growth in exports, FDI and domestic investment, and an increasing importance of trade and FDI in the economy (Table 2.1). From 1996 to 2008, exports grew at an average annual rate of 20%, and increased its share of the GDP from 25% to 70%, though the share of the domestic value added in the exports is considerably lower because of the heavy reliance on imported intermediate inputs (Riedel, 2009).. FDI increased dramatically, accelerating after the signing of the Bilateral Trade and Investment Agreement with the United States in December 2001, and especially after the WTO accession in January 2007. In 2007, it reached US$71 billion in 2007, which was nearly twice that of 2006, and accounted for 13% of GDP, 57% of total exports and nearly 40% of industrial output. The flow of FDI increased even further in 2008, when it was 3 times that of 2007. Private domestic investment has also risen rapidly, so that by 2008 domestic private enterprises accounted for 24% of industrial production, nearly 11% of GDP, and employed around 7% of the workforce.

Table 2.1:

Selected indicators of Vietnamese development performance, 2000-2008

Indicator	2000	2008	2000-2008
Average annual growth rate in real GDP	-	-	7.5%
Average annual growth rate in export value	-	-	17.5%
Jobs created	-	-	7.5 million
Incidence of poverty	17.5%	7%	-
Share of GDP			
Primary sector	24.5	20.9	-
Secondary sector	36.7	41.0	
Service sector	38.8	38.1	
Share of labour force			
Primary sector	71.1	56.8	-
Secondary sector	11.4	17.0	
Service sector	17.5	25.3	

Source: SEDP, 2006-2010

2.2 It has also produced rapid economic growth, with the real GDP growing at an average of 7.5% for 2000-2007, one of the fastest in the world, which pushed Vietnam's relative position in the ranking of countries by growth rate in the real per capita GDP up by 60 places worldwide and by 7 places in an already fast-growing region. Thus, it is not only growing fast but is increasingly better at it than most others (World Bank, 2006: 19). This growth has been accompanied by significant structural changes in the GDP. Industry grew most rapidly, accounting for over 50% of the increase

1. Introduction

in the real GDP and raising its share of the GDP from 30% in 1996 to 42% in 2007. Of the two sectors that make up industry, manufacturing grew at 11.5% per year, increasing its share of the GDP from 15.4% to 25%, compared to the 8.4% for mining, utilities and construction, which increased its share of the GDP only from 14.5% to 17%.

2.3 With rapid economic growth, the percentage of the labour force in paid employment increased from 17.8% in 1993 to 19% in 1998, and thereafter much more rapidly to 27.6% in 2002 (Pham and Reilly, 2007) and 33% in 2006, spreading to all population categories, especially among skilled workers in the industrial sector (Cling et al., 2009). Annual wage rates grew by 10.5% in the 1990s (Gallup, 2004; Dollar, 2004; and Nga, 2004), and 12% over 1993-2002 (Pham and Reilly, 2007), 27% in domestic firms and 34% in foreign-invested firms (World Bank, 2007: 43), which were faster than the annual growth rate in income per head. Over 1998-2006, they grew annually at 5.7%, 2.8% in agriculture, 3.4% in industry and 7.8% in services. There was also a substantial increase in the hours worked, especially in rural areas. The dominance of the state sector in employment also decreased, so that by 2005 it accounted for only 9.7% of the 42.7 million employed, with the non-state sector accounting for 88.7% and the foreign sector 1.6% (SEDP, 2006-2010: 1).

2.4 There were also dramatic improvements in many of the areas targeted by the United Nations' Millennium Development Project. For example, the wage discrimination faced by women from 1992/93 to 1997/8 in the wage-employment sector, when they earned much less than men with the same schooling and work experience (Dollar, 2004: 64), became less over time. Between 1992/93 and 2002, not only was the gender pay gap halved but the reduction was most pronounced in the high-paid jobs. Perhaps the most spectacular achievement was in the reduction in the incidence of poverty, defined as the cost of a food and non-food consumption basket that allows a person a daily intake of 2,100 calories, from 58.1% in 1993 to 16% in 2006 (World Bank, 2007: 4) and 7% in 2008. These and other achievements have pushed Vietnam from a low to a medium 'human development' country. It has led *The Economist* (2008) to call it 'the other Asian miracle' with China in the third wave of emerging Asian countries, after the original five East Asian Tigers (Hong-Kong, Korea, Singapore and Taiwan) and their followers in South-East Asia (Indonesia, Malaysia and Thailand.

Income distribution and employment growth

2.5 However, greater liberalization of the economy and involvement with the global economy has not produced equal success in other areas. One is in the distribution of income, which has become more uneven. The Gini coefficient for expenditure rose from 0.33 in 1992/93 to 0.35 in 1997-98 (Dollar, 2004: 39) and 0.36 in 2006 (World Bank, 2007: 11), and the ratio of the income of the richest quintile to that of the poorest quintile increased from 8.14 to 8.30 between 2001 and 2003 (SEDP, 2006-2010, p. 40). However, the increases are small and the degree of income inequality low by international standards (Minot, Baulch and Epprecht, 2006), and very few developing countries have managed to reduce their income inequality while increasing their economic growth and reducing their poverty level.

2.6 Perhaps the greatest failing is the inability to provide enough jobs that provide productive and secure work, adequate income, labour rights, social protection, social dialogue, union freedom, and collective bargaining and participation, known now as decent employment. Unemployment in the conventional sense has not been a problem, as the overall unemployment rate has been one of the lowest in ASEAN (ILO, 2007: 87) and has fallen consistently from a high of around 3.7% in 1993 (ILO, 2005b: 9) to 2.8% in 2001 and 2.2% in 2006 (ILO, 2008: 104). However, the unemployment rate hides the very important fact that 77% of those with jobs work in family businesses with little or no pay (MOLISA and ILO, 2009). They are mostly found among those who are poorly educated, work in the informal sector, have large families and little access to material resources and social and physical infrastructure, and ethnic minorities. These workers are clearly very vulnerable, with the situation worsened by the fact that in 2006, 4.4% of them had expenditures that were less than 10% above the poverty line and 3.7% had less than 15 million dong in assets, with the most affected being those employed by households and collective enterprises (6.8% and 7.2%) and farmers (5.8% and 4.8%) (World Bank, 2007: 31). For such workers, only a slight change in personal, family or external circumstances will force them back into poverty (World Bank, 1999). Thus, the decrease in the incidence of poverty and the claim that the growth in employment has played a significant role in reducing the percentage of the population living below the poverty line, as providing employment is an important way of reducing poverty, may be exaggerated. Moreover, the drop in the overall incidence of poverty also hides the fact that the fall is uneven, with it being the lowest for farmers and people employed by households and collectives, whose incidence of poverty in 2006 remained much higher at 25.1% and 20.4% respectively, compared to the overall rate of 16%(World Bank, 2007: 31).

2.7 Even the misleading unemployment rate shows a high 6% in 2007 for those between 15 and 24 years, which is many times that for adults, and youths make up 45% of all unemployment. In all probability, the situation is worse because some young workers might have been so discouraged after seeking unsuccessfully for work for such a long time that they dropped out of the job market and are excluded from youth unemployment statistics. A lower unemployment rate may stem from a contraction in the labour force participation rather than from an increase in employment. A more accurate measure of the youth job market is the rate of joblessness, defined as the percentage of all young people not in education or employment, because it takes account of discouraged young people, who are the most in need of support in terms of education, training, and counselling to minimise the risks of them becoming entirely detached from the labour market. No estimate of this rate has been made for Vietnam but if the finding of a recent study by the Asian Development Bank on India, Indonesia, the Philippines and Thailand that the rate of joblessness for the four countries as a group is nearly twice that of the unemployment rate (ADB, 2008), is applied to Vietnam, then its rate of joblessness will be nearly 12%.

2.8 Yet another sign of a poor employment record is the consistent decline in the employment-population ratio from 72.2% in 1997 to 68.1% in 2007 (MOLISA and ILO, 2009). Even when using a definition of employment that clearly understates the seriousness of the situation, the growth in employment has lagged behind the growth in population. While the increasing number of Vietnamese working overseas has brought long-term benefits to the country, with remittances reducing poverty directly and indirectly, and workers retuning with greater skills, the fundamental cause of workers seeking work overseas is the shortage of well-paid employment at home.

2.9 The level and growth of wages also vary significantly across the country. After controlling for worker characteristics, workers in the two primary cities of Ho Chi Minh City and Hanoi had wages that were 50% to 80% higher than in other regions, because residency permit restrictions. Despite the rapid growth of wages, inequality in wages fell only modestly in the 1990s. There are also significant differences in the average monthly wage between different categories of enterprises, with workers in private firms earning about 60% of that of their counterparts in state-owned and foreign-invested enterprises, with the gap showing no sign of narrowing.

2.10 The position of ethnic minorities deserves special mention. In 1993, their poverty rate was 86%, compared to 58% for the country. By 2004, the corresponding figures were 61% and 20% (World Bank, 2006: 106), so that not only was the percentage of the ethnic minorities who remain poor still at an unacceptably high level, they have also, when compared to the rest of the population, become relatively worse off, as the ratio of the shares of the two groups increased from 1.48 to 3.05. Estimates for 2006 show an even worse situation as the respective figures were 52 and 16%, a ratio of 3.27 (World Bank, 2007: 4). This worsening gap between the majority (Kinh and Hoa) and the ethnic minorities means that the latter, while accounting for only 14% of the population, make up 39% of all poor people. Moreover, according to the World Bank, hunger is still widespread among them (World Bank, 2006: 106). Clearly, employment creation has not helped them much and has, in fact, worsened their relative position.

2.11 There has been no substantial change in the industrial structure of employment. Of the 5.61 million jobs created over 2001-2007, 3.14 million came from the secondary sector (manufacturing, utilities and construction) and 2.9 million from the service sector, with the number of jobs in the primary sector (agriculture, forestry, fishing and mining and quarrying) falling by 0.4 million. This resulted in the share of the primary sector in the labour force falling from 64.1% in 2001 to 55.1% in 2007, the share of the secondary sector increasing from 13.7% to 19.1% and that of the service sector from 22.1% to 25.8%. On the surface, this indicates healthy structural changes in the right direction. However, as a very sizeable number of the increase in jobs, probably around 5 million, was in the informal sector, where own-account-workers make up 46.4% of the labour force, these would most probably be low-pay and low-productivity jobs (Razafindrakoto, Roubaud and Le Van Duy, 2008). In addition, the increase in the share of the services sector belies the fact that a significant percentage of it was in the sub-sectors of trade and the repair of vehicles, which have a high level of under-employment and a marked decline in the value-added per head (Jenkins, 2004b: 194). As informal employment is often chosen as a last resort when all else fails, the observed changes in the industrial origin of employment may not reflect genuine structural changes in the economy. This conclusion is supported by the figures on the share of the primary sector in the GDP. In 2001, this was 23.2%, which is much smaller than its share of 64% in the labour force, with the ratio of the two shares of 0.36 indicating a very low level of productivity arising from a high level of under-employment. The situation had changed only marginally by 2007, as the respective figures were 21% and 55%, a ratio of 0.38. It is unlikely that increased employment in the informal and/or own-account-worker sector would help to reduce the vulnerability of workers on a sustained basis.

2.12 Even though gender segmentation is not an issue in wage employment, with wage disparity going down and contributing little to the wage gap between the poor and non-poor (ADB, 2005), women are still more dependent on low-paid and low-productivity agriculture and

self-employment activities, as only 20% of them are in wage employment, compared to the 33% for men (Pham and Reilly, 2007). They are also more likely to be employed in the informal sector, which consists generally of lower-paid jobs. In addition, women suffer from inequality within the household as they have to work longer hours because of the need to do housework on top of paid employment, and do not have the same power as men in making household decisions (World Bank, 1999: 74; UNICEF, 2008: 22). They are also discriminated against in the granting of land titles, which disadvantages them in the rural areas as their livelihood is tied to land, and in urban areas as land titles are often required for obtaining credit and starting small businesses (World Bank, 2006: 116).

2.13 The employment creation programme has not eliminated wage disparity between migrant and non-migrant workers (ADB, 2005). This labour market segmentation is probably due largely to regulations introduced to prevent rural-urban migration getting out of hand. Before 1990, this was strictly controlled by the government through employment policies and the household registration system, similar to that in China (Fan, 2002). Since the doi moi reforms, the household registration system no longer affects every aspect of people's lives but still restricts migration in many ways, the most important being the division of the Vietnamese population into four different categories of residential household status (K1, K2, K3 and K4), with varying degree of access to basic social services, poverty reduction programs and job services, and the right to purchase land (Waibel1, 2007). The vast majority of migrants (e.g. 87.3 % in Ho Chi Minh City) are in K4, which provides the least access and no right to purchase land, which reduces their bargaining power and lowers their wage and chances of promotion.

2.14 On top of this, all studies show that the growth of employment has lagged behind the growth of output, with estimates for the employment-output elasticity that are significantly smaller than one (Son, 2005; Huong, 2003; Ronnas et al., 2001), and becoming smaller over time. For example, for the country as a whole, the elasticity in 1985-90 was 0.66 but decreased to 0.28 in 1990-95 and 0.22 in 1995-2000, as output growth outstripped employment growth (Nguyen et al., 2002; MOLISA, 2001). For manufacturing, it was 0.20 in 1995-99 (Jenkins, 2004b), which was also much lower than those in most ASEAN countries (Ghose, 2000). Recent studies, using more recent and disaggregated data by ownership, economic sector and 1-digit economic activity, show the same pattern (Warren-Rodriguez, 2009; Nguyen, Pham and Phung, 2009). Table 2.2 presents 3-year averages of the elasticity for 1997-2001, 2002-2004, 2005-2007 and 2006-2008, and shows that the values of the elasticity for Vietnam were significantly smaller than one. It also fell consistently over 1997-2007, and though it rose for 2006-2008, this was slight and the data for 2008 was an estimate. The same results were evident in most of the sectors. For manufacturing, the value for 2005-2007 was 0.425. Values for the elasticity obtained from estimating a labour demand function using panel data for 2004-2006 were, as expected, lower because the impact of factors other than output had been incorporated, but they were also significantly smaller than one. The value for manufacturing was 0.214. These and other results suggest that growth has been driven by 'a process of capital-intensive investment in activities associated with low levels of employment generation' (Warren-Rodriguez, 2009: 3).

2.15 If an elasticity of 0.25 is used for 2006-2010 and the target annual GDP growth rate of 8% for the second SEDP period of 2006-2010 is achieved, the growth rate in employment per year will be only 2%, which is the same as that forecasted by Nguyen et al. (2008: 36). Even if the elastic

ity is assumed to higher at 0.36 (ILO, 2005b: 22), the growth in employment will still be 2.9%, which is also well below the projected annual growth rate in employment of 3.7%, so that only between 0.86 million and 1.25 million of the target of 1.6 million new jobs will be created. Even if the target GDP growth rate of 8% a year is achieved, this will not improve the employment situation because of the annual growth in the labour force of 2.1%, which requires a GDP growth rate of 8.67% just to maintain the current level of employment. The capacity of the economy to generate employment has fallen over time. In 2002-2004, it needed to grow by only 6.78% to provide jobs for all the entrants to the labour market, and in 1999-2001, 5.09%.

2.16 Amid this high level of unemployment is ironically a great shortage of skilled workers, especially in technical and management areas (SEDP 2006-2010: 40). The imbalance between supply and demand is present also across geographical areas, where in places such as industrial zones, established to spearhead industrialization, the shortage is very serious (MOLISA, 2008: 9). According to a recent Investment Climate Assessment, the third most important constraint faced by entrepreneurs in manufacturing, after access to finance and access to land and infrastructure, is the shortage of appropriately skilled workers (World Bank, 2006: 96). This shortage has led to a rapid turnover of labour, which is costly to individual firms and has hindered economic growth. It has to be tackled urgently because Vietnam cannot rely on cheap labour for its comparative advantage for long, and has to produce higher value-added products and services to remain successful in the export market.

Table 2.2: Employment-output elasticity, Vietnam, 1997-2008*

Ownership/sector/activity	Average elasticity				Elasticity from regression analysis 2004-2006 panel data
	1999-2001	2002-2004	2005-2007	2006-2008	
Total	0.368	0.320	0.227	0.315	0.193
By ownership					
State sector	0.394	0.233	0.109	-0.387	0.197
Non-state sector	0.361	0.307	0.168	0.273	0.191
Foreign-invested sector	2.775	1.981	1.209	0.382	0.190
By economic sector					
Agriculture	-0.015	-0.012	-0.225	-0.196	NA
Industry	1.221	0.801	0.554	0.949	NA
Services	0.677	0.697	0.552	0.468	NA
By economic activity					
Agriculture, forestry & fishing					
Agriculture & forestry	-0.225	-0.104	0.511	-0.304	0.127
Fishing	0.827	0.692	0.489	0.560	0.178
Industry & construction					
Mining & quarrying	1.517	1.075	-3.658	-2.215	0.220
Manufacturing	0.837	0.548	0.425	0.572	0.214
Electricity, gas & water supply	1.952	0.757	1.141	1.179	0.110
Construction	1.891	1.540	0.511	NA	0.181
Services					
Wholesale and retail trade	0.606	0.663	0.401	0.238	0.175
Hotels & restaurants	0.317	0.258	0.307	0.245	0.172
Transport, storage & communications	0.071	0.080	0.028	0.026	0.204
Financial intermediation	2.159	1.716	1.681	0.733	0.113
Scientific activities & technology	1.127	3.113	0.451	0	0.163
Real estate, renting & services	4.450	4.192	5.135	6.587	0.135
Public administration & defence	1.015	1.828	1.296	KAD	0.199
Education & training	0.742	0.438	0.499	0.410	0.199
Health & social work	2.466	1.485	0.390	0.526	0.216
Recreation, culture & sports	-2.219	-0.122	0.196	-0.159	NA
Activities of the Party	4.757	2.388	1.531	NA	NA
Community, social & personal services	1.320	1.193	1.273	NA	

Sources: Estimates for 1999-2001, 2002-2004 and 2005-2007 from Warren-Rodriguez, (2009) and for 2006-2008 from Nguyen, Pham and Phung (2009).
*Notes: *Data for 2008 are estimates; NA denotes not available*

2.17 In short, the greater liberalization of the economy and involvement with the global economy, instigated since 1986, has produced rapid growth in the real GDP, exports, FDI and domestic private investment, and a significant fall in the share of the state-owned sector in the economy. The percentage of the labour force in paid employment, the hours worked and real wages have grown significantly. And most of the targets set for the United Nations' Millennium Development Goals have been met, including the reduction in the incidence of poverty, which has been spectacular. Thus, the achievements of Vietnam since 1986 on the economic and social fronts have placed it in the forefront of development successes. However, the record in some areas has been less impressive, especially in the creation of decent employment. This is because economic growth has been generated by industries that do not produce large numbers of well-paid and durable jobs. No where has this been brought out more clearly than in the state-owned enterprise sector, which contributes 34% of the GDP and over 20% of industrial production but only 9% of the total labour force. The same trend is shown in the FDI sector, which contributes 19% of GDP and 45% of industrial production but less than 4% of total labour force. The only sector that bucks the trend is the non-state domestic sector, which contributes 47% of the GDP and 35% of industrial production but employs more than 87% of the labour force. All the available studies show that the Vietnamese employment-output elasticity of manufacturing is low by ASEAN standards. This means that even if the Government's targeted annual real GDP growth rate of 8% for 2006-2010 is achieved, the number of jobs created, using the highest value obtained for the employment-output elasticity of 0.36, is only between 0.86 million and 1.25 million jobs, well short of the target of 1.6 million jobs.

3. Impact of WTO accession

3.1 The accession of Vietnam to the WTO in January 2007 marked an important step in the country's integration into the global economy and was expected to increase Vietnam's economic growth and with this, greater decent employment growth. First, the required reduction in tariffs would reduce price distortion and produce a more efficient allocation of resources. The output of protected and inefficient industries producing for the domestic market would fall, and that of efficient industries, using more of the relatively abundant resources (e.g. labour) and producing for the export market, would rise, as they no longer have to use expensive inputs produced locally. Second, membership would enable Vietnam to take advantage of its comparative advantage in the production of labour-intensive manufactured goods to generate growth and employment. Third, greater access to the world market would increase the demand for its now more cheaply-produced goods. Fourth, FDI would increase, bolstered by the operation of a more modern legal environment and system that supports growth driven by market forces and the private sector.

3.2 There are quite a few studies on the impact of the accession on Vietnam, a survey of which has been given by Abbott et al. (2009). Some have been conducted well before the event and naturally could not incorporate all the commitments made by Vietnam and its trading partners and had to make assumptions about the tariff reductions. Others are based on very simplistic models of the Vietnamese economy, which usually make the unrealistic assumption of full employment, while some evaluate only the impact of tariff reduction following accession, despite the fact that this is only one of the commitments required. Since the accession, two studies have been conducted that take into account the precise commitments of Vietnam and its trading partners, the impact of tariff reduction, abolition of quotas and greater FDI inflows, and imperfections in the labour market. The first, Boumellassa and Valin (2009), used a dynamic computable general equilibrium (CGE) model of the world economy to estimate a real GDP growth of 2.1% by 2015. Half of the increase was accounted by the fulfilling of tariff commitments and half by the removal of quotas for textile and clothing products by the US and Europe, which enabled the more efficient Vietnamese producers to supplant their Chinese counterparts. The second, Cling, Marouani, Razafindrakoto, Robilliard and Roubaud (2009), carried out in the same project as the first, combined a CGE model of the Vietnamese economy with a micro-simulation model based on a sample of 9,000 representative households at the national level with data from the 2004 Vietnam Household Living Standards Survey to examine the impact on income distribution. They included the impact of greater FDI inflow on top of that of the removal of tariffs and quotas and produced a higher real GDP growth of 3%.

3.4 The Government of Vietnam, through the Central Institute for Economic Management (CIEM) of its Ministry of Planning and Investment (MPI), has worked with the United States Agency for International Development (USAID)-funded Support for Trade Acceleration (STAR) Project to track the impact of the accession on a regular basis, and have produced two studies so far. As the first study covers only the first nine months of membership (CIEM-STAR, 2008a), only the results of the second, which covers a longer period (CIEM-STAR, 2008b), will be presented. This found that the reduction in tariff rates, from an average of 18.4% in 2003 to 11.7% in December 2007, with corresponding import-weighted average tariff rates of 14.6% and 8.4% respectively, had only a limited impact on Vietnam's trade flows in 2007 and the first five months of 2008. This was because accession did not require Vietnam's trading partners to alter

access to their markets as they had already granted it most-favoured-nation status. Leaving aside the erratic movements of oil exports, non-oil exports in 2007 and the first five months of 2008 grew by about the same rate as in 2006 (Table 3.1). Of the key manufactured exports, only two, clothing and textiles, and plastic products, grew faster in 2007 than in 2006, but nearly 60% of the export growth of the former was to the US because of the elimination of the textile and apparel quotas. What affected overall trade more in 2007 was the large increase in domestic growth, which led to higher imports, and high commodity prices, which led to higher exports. Given the slow growth in the exports of labour-intensive manufactured goods, it is not surprising that the number of jobs created in 2007 and 2008 increased by only 2.3% and 2.0% respectively, which were lower than the 2.7% increase in 2006.

Table 3.1: Growth of total exports and key manufactured exports, 2002-May 2008 (%)

Export category	2002	2003	2004	2005	2006	2007	2008 Jan-May
Exports							
Total	11	21	31	23	23	21	32
Domestic firms	7	13	20	16	21	22	29
Foreign firms	16	29	43	28	24	21	34
Crude oil	5	17	48	30	13	2	48
Non-oil	25	38	39	27	32	32	28
All non-oil exports	13	22	28	20	26	27	28
Key manufactured exports							
Clothing & textiles	38	35	17	11	21	34	20
Footwear	20	21	15	15	18	11	18
Wood products	37	23	86	44	26	24	22
Electronics & components	2	11	60	34	23	23	31
Electric wire & cable	22	40	47	35	35	26	28
Plastic products	7	30	39	35	37	52	35

Source: CIEM-STAR, 2008b: 10 and 12.

3.5 However, FDI did increase markedly, with the level in 2007 doubling that in 2006, reaching a staggering 24% of the GDP, as the accession gave Vietnam greater credibility and exposure to investors. The euphoria created by the accession also led to significant rises in domestic private and public consumption, and in investment, which produced a domestic saving-investment gap or a current account deficit of 10% of the GDP. The resulting excess of financial inflows over financing requirements (14% of the GDP) required the State Bank of Vietnam (SBV), the central bank, to buy the surplus foreign exchange and add it to its foreign reserves, as under its policy of pursuing simultaneously a fixed exchange rate, an independent monetary policy and free capital mobility, it could not allow the currency to appreciate. The

massive accumulation of reserve assets led to a large increase in money and credit and an almost 30% rise in prices. By May 2008, domestic and foreign investors felt that the trade deficit and inflation rate were becoming unsustainable and started to move out of the domestic currency and financial assets denominated in it. The subsequent run on the currency forced the Government to clamp down on the black market in currency exchange, raise interest rate by more than 50%, redouble efforts to control credit, and promise substantial cuts in government spending. The mini crisis led the real GDP growth rate in 2008 to fall to 6.2%, a decrease of 27% from the 8.5% of 2007. However, not everything emanating from the large increase in FDI is bad as, apart from increasing the supply of funds for investment, foreign-invested firms tend to export much more than local ones, averaging over the last five years 34% a year compared to 18% a year for local firms, laying the foundation for more export-oriented growth in the future.

3.6 While the impact of WTO membership on economic growth and employment has been disappointing so far, it should not be surprising as there might simply not have been enough time for the full effect of membership to be felt. However, there can be little doubt that in the long run membership will benefit Vietnam. It has harmonized its tariff classifications with major trading partners and improved the country's legal and administrative system. Not only will this facilitate trade, it will also improve foreign and local perceptions of the country. The reduction in tariffs and in its escalation will increase market access for imports, including that of services, and expose it to greater competition. It will also force it to improve its poor economic, trade and financial data, which has hampered policy making, based on research, and raised the cost of doing business in Vietnam (CIEM-STAR, 2008b).

4. Impact of the global financial crisis

4.1 Perhaps a more important reason for the insignificant impact of WTO membership so far is that the expected increase in export growth had been thwarted by the global financial crisis, which started soon after the WTO accession. The crisis began as a financial crisis in the US in the middle of 2007, but quickly turned into an economic one when panic in the wholesale banking system resulted in a massive drop in liquidity and the freezing up of credit in inter-bank and repo markets. Given the size of the US economy and its trade with the rest of the world, this inevitably turned this into a global crisis. Growth in developed countries first fell and then became negative, with their imports decreasing dramatically, from a 7% growth in 2006 to zero growth in 2008 and negative growth in 2009. As the main channels of transmission from developed to developing countries are international trade and capital flows, this produced equally dramatic falls in the exports of developing countries and net private capital flows to them.

4.2 While the impact on Vietnam's export and GDP growth was not as severe as that in other countries, it was still very significant. In the first quarter of 2009, the fall in non-gold exports, while much smaller than the 60% for Japan, 20% for China and the average of 26% for the other four ASEAN countries, was still high at 11.6% (Table 4.1). Compared to the first quarter of 2008, the falls in the country's individual export items were very substantial. For example, coal exports fell from a growth of 35% to one of -21%, and electronics and computers from 25% to -8%. The only exception was handicrafts, which surprisingly grew but the increase was so great, from 3% to over 770%, that it was either a one-off affair or a case of inaccurate data.

4.3 Its impact on real GDP and employment growth has also been very severe (Table 4.2). The real GDP growth fell dramatically, from an average of 7.2% for the first quarter growth over the last few years to 3% (World Bank, 2009a: 3). The drop was worse than that in China and Indonesia but far less than that in Singapore, Thailand and Malaysia. The World Bank's latest forecast for the whole of 2009, given in November 2009, put Vietnam's real GDP growth at 5.5% (World Bank, 2009b). Other international organisations have lower forecasts for 2009. The IMF, in its April 2009 forecast, has real GDP in 2009 growing at 3.3%, rising to 4% in 2010, compared to the 6.2% in 2008 and 8.5% in 2007 (IMF, 2009a). While its October 2009 forecast put it at 4.6%, rising to 5.3% in 2010, this is still significantly below those of earlier years (IMF, 2009b). In its earlier forecast, the Asian Development Bank has growth at 4.5% in 2009 and 6.5% in 2010 (ADB, 2009a) and revised it later to 4.7% for 2009 but unchanged for 2010 (ADB, 2009b). The Economist Intelligence Unit (EIU) has been the most pessimistic, with growth forecasted at only 2.1% in 2009, rising to 4% in 2010 (EIU, 2009). All the updated forecasts have been higher because of expansionary fiscal policies, a rebound in financial markets and capital inflows, which eased financing constraints and improved consumer and business confidence, and growth from replenishing inventories depleted during the first stage of the global financial crisis.

Table 4.1: Exports by country and Vietnam's exports by commodity (%)

Country	2008 (%)	Q1-2009 (%)	Growth (%, year on year)			Q1-2009 (%)
			2008	2008 Jan-May	2009 Jan-May	
Japan	9.5	-60.0				-15.2
Indonesia	20.0	-32.0				4.4
Malaysia	13.3	-28.9				-6.2
Thailand	15.7	-23.2				-7.1
Singapore	12.9	-20.6				-10.1
China	17.3	-19.7				6.1
Vietnam	29.1	-11.6*				3.1
Vietnam						
Total exports			29.1	27.2	-6.8	
Crude oil			22.0	45.5	-44.0	
Non-oil			30.6	23.5	1.8	
Non-oil items						
Rice			94.3	94	20.2	
Other agricultural items			17.2	14.0	-19.5	
Seafood			19.8	11.6	-9.1	
Coal			38.8	34.9	-20.7	
Garment			17.7	19.0	-1.8	
Footwear			19.4	13.4	-10.1	
Electronics & computers			22.5	25.2	-8.0	
Handicraft			65.1	3.2	772.6	
Wood products			17.7	20.8	-19.8	
Other			44.3	32.9	-12.2	

Source: World Bank, 2009a: 6 and 12.

** Excludes oil.*

4.4 The severe impact of the crisis on employment creation is shown by two quantitative macro studies, using the GDP forecasts of the World Bank, the ADB, the IMF and the EIU and estimates of the employment-output elasticity. The first, by Warren-Rodriguez (2009), estimated that between 300,000 and 700,000 jobs would be lost in each of 2009 and 2010, which would increase the unemployment rate up from 4.6% to somewhere between 6.7% and 7.6% in 2009, and between 7.2% and 8.7% in 2010 (Table 4.2). The fall is due largely to the fact that the sections of the economy that produce the most jobs (e.g. the export-oriented manufacturing sector and the foreign-invested sector) will be affected most. The second, by Nguyen, Pham and Phung (2009), using more recent data, estimated that between 400,000 jobs to 600,000 jobs would be lost in 2009 and between 750,000 jobs and 1,400,000 jobs in 2010. The loss would be heaviest in the manufacturing sector, numbering 395,000 and 820,000 jobs in 2009 and 2010 respectively. The unemployment rate would be pushed up from 2.47% in 2008 to between 4.3% and 4.5% in 2009, an increase of about 60%, and to between 5.2% and 5.7% in 2010, an increase of 110%.

Table 4.2: Forecasted impact on real GDP growth and job loss, Vietnam, 2009 and 2010

Organization	Forecast for 2009		Forecast for 2010	
	Earlier	Later	Earlier	Later
Real GDP growth				
World Bank (2009a và 2009b)	3.0%	5.5%		
IMF (2009a và 2009b)	3.3%	4.6%	4.0%	5.3%
ADB (2009a và 2009b)	4.5%	4.7%	6.5%	6.5%
EIU (EIU, 2009)	2.1%		4%	
Job loss				
Warren-Rodriguez (2009)	300,000-700,000		300,000-700,000	
Nguyen, Pham and Phung (2009)	400,000-600,000		750,000-1,500,000	

4.5 These findings are supported by qualitative micro-level rapid assessments of the impact on specific sub-sectors or categories of the population, whose results have been conveniently summarised by the World Bank (2009a) and Cling et al. (2009). Thus, the World Bank reported that electronic advertisements by firms looking for workers and workers for jobs in a popular website (muaban.com.) used by semi-skilled and skilled workers show significant drops in numbers towards the end of 2008 and early 2009, before rebounding strongly in March 2009. However, the situation in industrial parks, where the labour force is generally less skilled, is worse. An ongoing survey by the CIEM with World Bank support shows that in May 2009, while the majority of enterprises in the industrial parks in Dong Nai, Hai Duong and Vinh Phuc provinces were doing relatively well, a significant minority were not. The situation is worse than depicted because the study includes only workers registered with social security, not casual and seasonal workers who bear the brunt of any fall in the demand for labour. The rapid impact assessment conducted by the Vietnamese Academy of Social Sciences, with support from the World Bank and participation of civil society organizations, show the same thing. Information gathered from structured focus group discussions with workers in Hanoi's spot labour markets, handicraft villages and one industrial park in February and March 2009, and in several other industrial parks and in rural areas in April 2009 show 'numerous job losses, frequent reductions in working hours and wages, reduced remittances, and more reliance on informal sector jobs' (World Bank, 2009a: 10).

4.6 The rapid impact assessments reported by Cling et al. (2009) show the same picture. For example, Ngoc (2009) in a study for the ILO found record job losses in the three main economic zones of Danang, Hanoi and Ho Chi Minh City, especially among foreign-invested companies, and also in many provinces (e.g. Quang Ngai and Binh Duong provinces). Fewer jobs were also being created and the hours worked and/or wages and incomes reduced. Similar results were found in a number of Oxfam case studies that concentrated on migrant workers in mobile labour markets, craft villages and industrial parks, found the same thing (Oxfam, 2009; Dinh, 2009; Nguyen Ngoc Anh, 2009; Nguyen Viet Cuong, 2009). A study on farmers in 4 provinces by the Institute of Policy and Strategy for Agriculture and Rural Development (2009) found that more than 20% of migrant workers from rural areas lost their jobs and returned home ad of these only 11% managed to find new jobs. In their own study, Cling et al. (2009) found that the

impact would also be very severe but that it would be felt most acutely in the informal sector of unregistered household businesses, traditionally the sector of last resort, when jobs in other sectors dry up. With an expected GDP growth of only 5% and historical values for the employment-output elasticity, increases in the labour force, and growth rates for the other sectors of the economy, the number of people that will end up in the informal sector in 2009 is a huge 750,000, an increase of 6.5% over its size in 2008, raising its share of the labour force from 23.6% in 2007 and 24.4% in 2008 to 25.6% in 2009.

4.7 To counter the severe fall in output and employment, authorities in Vietnam introduced classic expansionary monetary and fiscal policies. Thus, in late 2008 and early 2009, the State Bank of Vietnam (SBV), the central bank, eased monetary policy significantly and has kept it relatively loose since then. From late October 2008 to late January 2009, it cut its benchmark interest rate six times from 14% to 7%, and reduced its refinancing rate and discount rates to 8% and 6% respectively. The reserve requirement level was also lowered by 1 percentage point for the local currency and 2 percentage points for foreign currencies. In addition, in early November 2008, the exchange rate trading band of USD/VND was widened from ±2% to ±3% to better reflect the changes in the supply of and demand for foreign currencies (Le, 2009). Growth of credit and money supply in the first half of 2009 accelerated, with the growth in total liquidity (M2) especially fast, at 35.8% in the second quarter of 2009, compared to the 20.3% in the fourth quarter of 2008.

4.8 However, the expansionary monetary policies were not enough to prevent the economic situation from worsening and the Government introduced several fiscal stimulus measures in the first half of 2009. They include a temporary 30% cut in the corporate tax rate for small and medium-sized enterprises, an unemployment insurance scheme to provide financial assistance to unemployed workers, an increase in infrastructure spending, and a 4 percentage point subsidy on certain bank loans. The total cost is estimated to be 145.6 trillion dong (US$8.6 billion), or 8.9% of the projected GDP for 2009, with increases in government spending and lending accounting for the bulk (82%) of it (Table 4.3).

Table 4.3: Fiscal stimulus measures, 2009 (trillion dong)

	Amount[a]	Potential direct impact on the budgetb[b]	
		2009	2010
Measures affecting government revenue	28.0	-28.0	9.2
Measures affecting government expenditure and net lending	117.6	114.5	-24.7
Total	145.6	-141.5	33.9
Billion US dollars	8.6	-8.3	1.8
% of GDP	8.7	-8.5	1.8

Source: ADB, 2009: 163.

a Excludes quasi-fiscal stimulus measures undertaken through the Vietnam Development Bank (e.g. guaranteeing bank loans to small and medium-sized enterprises).

b Based on the assumption that the announced fiscal stimulus measures will be fully implemented, and excludes the indirect impact of the measures on the budget through their effects on public debt, growth and so on.

4.9 These fiscal measures and the fall in oil income from lower world oil prices led to a budget deficit equal to 4.8% of the GDP in 2009 from a surplus in 2008, revised later to 7% (Table 4.4). When off-budget spending and lending were added, the overall fiscal deficit came to 6.9% of the GDP. A massive increase in such spending later in the year would push this to 15.7% of the GDP. After taking into account the possible understatement of income from oil exports, the more efficient collection of taxes, and lower capital expenditure because of implementation and financing problems, the ADB (2009a) put the overall fiscal deficit at a lower but still substantial 10.1%. Since the deficit was to be financed largely by the Government drawing down on its deposits at the SBV and commercial banks, and by borrowing from multilateral and other development agencies, and assuming that monetary policy were to be tightened towards the end of 2009, this level of public debt was not expected to be unsustainable or jeopardize macroeconomic stability (ADB, 2009a).

Table 4.4: Budget as % of GDP, 2009

	Government's plan		ADB revised projections
	Original	Revised	
Budget revenue and grants	21.5	20.0	22.8
Budget expenditure	25.2	27.2	27.6
Budget fiscal balance[a]	-4.8	-7.0	-4.5
Off-budget expenditure and lending (net)	3.2	8.5	5.3
Overall fiscal balance[b]	-6.9	-15.7	-10.1

Source: ADB, 2009b: 163.
a Includes carried over 2008 revenue (as revenue) and amortization of public debt (as expenditure).
b Excludes carried over 2008 revenue and amortization of public debt but includes net off-budget expenditure and lending..

4.10 The expansionary monetary and fiscal policies had a positive impact, as indicated by the higher revised estimates of GDP growth for 2009 given in Table 4.2. The impact would have been greater if the measures had been introduced as an integrated package and not on a piece-meal basis. While the latter approach allowed some measures to be taken quickly, it created uncertainty about the ability, seriousness and determination of the Government to deal with the situation. The quick design and implementation of an integrated programme would have been better but the consensus approach to making decisions made this impossible.

Rebalancing economic growth

4.11 The severe impact of the global financial crisis on developing countries has encouraged calls for them to de-link their economic fortunes from those of rich countries, as the very global sources of growth that gave them prosperity have halted or reversed this growth, with long-term negative consequences. In the case of Vietnam, even if forecasts that its GDP growth rate would return to its pre-crisis level by 2014 were accurate (IMF, 2009a; EIU, 2009), its per capita income then would be about 20% lower than it would have been if the pre-crisis growth rate had been

maintained (Riedel, 2009: 28). And if the IMF's forecast of an average annual growth rate of 5% for 2009-2014 were true, it would take 14 years to double the per capita income, compared to 10 years if the growth rate had been 7% (Riedel, 2009: 29). While the latest growth figures for Vietnam and other developing countries show that the forecasts of the IMF and other organizations were a bit pessimistic, the global financial crisis will still cause a significant permanent loss of per capita income.

4.12 Even before the advent of the global financial crisis, there is, according to the global savings glut theory, a case for countries with large and persistent current account surpluses (i.e. excess of exports over imports) or net saving (i.e. excess of saving over investment), to, as is popularly known, rebalance their economic growth (ADB, 2009a). The surpluses, mainly from developing Asia, the Middle East and the Russian Federation, have provided cheap funds to spendthrift developed countries, principally the US, which allows and encourages them to finance current consumption and risky subprime mortgages. Historical evidence suggests that large current account deficits are likely to cause financial crises (Edwards, 2002), which is borne out by the Asian financial crisis in the late 1990s (Radelet and Sachs, 2000; Corsetti et al., 1998) and the current global financial crisis. Apart from this, there are other reasons for reducing the global imbalances. First, it makes no sense for the global optimal use of capital for funds to flow from countries with high marginal returns to capital to those with low returns, especially since the latter uses the funds for consumption rather than investment. Second, a sustained high level of current account deficit can also lead to a significant depreciation of the exchange rate and reduction in GDP growth (Edwards, 2005). Third, there are economic and welfare costs to developing countries because saving too much will not improve their consumption levels and standards of living, and investing too little their capacity for future growth. Fourth, persistently large current account surpluses have produced holdings of foreign reserves that exceed what is needed for liquidity purposes (Park, 2007), which has, in turn, led to welfare losses. If, as is often the case, the excess reserves are held in traditionally safe and liquid assets, such as US Treasury bonds, the return is low. If held in liquid foreign currency assets that offer little protection against currency crisis, it can be costly. The benefit of managing better foreign exchange reserves can be higher than 1% of the GDP of many developing countries (Park, 2008). Last but not least, transferring capital from poor to rich countries cannot be justified on grounds of equity.

4.13 According to the ADB (2009a), the global financial crisis did not create the need for those Asian developing countries with large current account surpluses accumulated since the Asian financial crisis, to rebalance their economic growth. The need was already there but it does introduce greater urgency to doing something about it. It also does not preclude the continued pursuit of an export-oriented development strategy, only the need to do it with some redress of the imbalance. While the global savings glut theory does not apply to Vietnam per se because it has been in deficit for most of the period since 1980, there is no gainsaying that the global financial crisis has affected it badly.

4.14 There is a need therefore to examine the relevance to it of two popular suggested development alternatives to growth through globalization. One is to trade more with other developing countries (i.e. increase South-South trade), the other to produce less for export and more for domestic consumption. The case for greater South-South trade has been encouraged by

the very rapid rise of 197% in such trade in 1995-2005, compared to the 143% growth in trade between developing and developed countries (i.e. South-North trade). By 2005, South-South trade accounted for about 50% of the South's exports (Shirotori and Molina, 2009). Asian developing countries, particularly the 'tigers', have dominated this, accounting for 85% of South-South trade, because of their greater economic size and participation in international trade. This increased the share of intra-Asia trade in the total trade of developing Asia from 40% in 1994-1995 to 48% in 2005-2006, which was far higher than the shares of its trade with countries in the North American Free Trade Agreement (18%) and the EU-15 (16%), and with Japan (13%). The rapid growth in South-South trade took place amid the increasing importance of the South in international trade, the so-called 'new geography of international trade' (UNCTAD, 2004), which saw its share in world exports increasing from 10.5% in 1995 to 32% in 2005. The case for greater South-South trade has also been encouraged by the spectacular increase in South-South FDI flows, from $2 billon in 1985 to $60 billion in 2004. As with trade, this took place amid a rapid increase in the importance of the South in FDI flows. In 2006, it accounted for 29% of total global FDI inflows and 16% of the total global FDI outflows, the latter spearheaded by the South's transnational corporations (e.g. Tata of India), with estimated total sales of $1.9 trillion and estimated employment of 6 million in 2005 (UNCTAD, 2006; 2007). The greater economic interactions between developing countries have been facilitated by technological advances which have reduced drastically the costs of transportation and communication.

4.15 However, a more detailed analysis of the data shows that Asian developing countries cannot replace international trade with intra-regional trade as an engine of growth. An ADB study shows that the growth of intra-regional trade in Asia is due importantly to the internationalization of supply chains (Jongwanich, James, Minor and Greenbaum, 2009). As Asia becomes increasingly integrated into the global production sharing system, more and more of its exports of manufactured goods are in the form of parts and components for processing by other countries into final goods, not final goods for consumer demand. Thus, the proportion of parts and components in its manufactured exports increased continuously from 16% in 1992 to 25% in 2006, with the increase most pronounced for Southeast Asia (26% to 40%) and East Asia (16% to 26%). Their share in manufacturing imports also increased, from 22% to 36% in 2006 from 22% in 1992, with it highest in Southeast Asia (42%) and East Asia (37%), and lowest in South Asia (17%).

4.16 A significant percentage of intra-regional trade in developing Asia is also in parts and components, increasing over the period 1994-95 to 2005-06 from 44.8% to 59.3% for exports and 41.5% to 64.4% for imports (Table 4.5). The figures are similarly high for East Asia and Southeast Asia. Of the goods exported to other Asian countries, final demand of these countries absorbs only 22%, with 78% being processed into final goods for export to the US, Europe and Japan (Holland, 2009). Thus, the collapse in the demand in developed countries from the global financial crisis will not only depress their direct imports from developing Asia but also intra-Asia trade (Riedel, 2009: 43). The option then for Vietnam to rely more on intra-Asian trade rather than international trade to return to its pre-crisis growth rate is not viable. The greatest demand for the products in which it has a comparative advantage will remain developed countries for the foreseeable future.

Table 4.5: Direction of Developing Asia's trade in parts and components (%), 1994-2006

	NAFTA	EU-15	Japan	Developing Asia	East Asia	Southeast Asia
Developing Asia						
Exports						
1994-95	29.8	15.1	9.0	44.8	20.9	23.4
2005-06	17.4	12.6	8.7	59.3	40.6	17.8
Imports						
1994-95	18.1	12.6	31.4	41.5	22.6	18.7
2005-06	11.7	10.2	18.3	64.4	41.6	22.6
East Asia						
Exports						
1994-95	29.5	15.1	10.1	41.9	25.0	16.5
2005-06	18.1	11.9	9.2	57.9	44.0	13.1
Imports						
1994-95	18.	12.6	32.8	41.8	31.2	3.7
2005-06	9.7	9.1	19.0	67.9	51.8	12.4
Southeast Asia						
Exports						
1994-95	30.4	14.9	7.7	48.8	15.8	32.4
2005-06	16.1	13.3	7.8	62.8	35.6	26.2
Imports						
1994-95	18.3	11.1	30.8	42.4	15.2	27.0
2005-06	16.0	10.8	17.5	59.3	23.1	35.9

Source: Jongwanich, James, Minor and Greenbaum, 2009, Table 6: 16.

4.17 The second development alternative suggested is to produce less for export and more for domestic consumption. However, there is no need to deliberately change to such a strategy as it will happen naturally in the course of development for a growing market economy. Sustained increases in its per capita income produce changes in tastes, with consumption moving from tradable goods to non-tradable ones, which raises the relative price of non-tradable goods and shifts labour and capital resources towards their production. The rise in the relative price of non-tradable goods causes 'a secular real exchange rate appreciation (the Balassa-Samuelson effect) and leads to lower economic growth rates, higher domestic consumption rates, lower saving and investment rates, and less reliance on exports as a source of aggregate demand' (Riedel, 2009: 44). Thus, decoupling from exports takes place gradually in the course of economic development and rises in the standard of living. However, for the process to begin, the level of economic

development, the saving rate and the size of the middle class must reach a level where consumption is favoured over saving. Riedel believes that while China has reached this critical level, Vietnam is still many years behind and cannot rely on production for home consumption as a viable growth.

4.18 The evidence thus suggests that for the foreseeable future, Vietnam cannot replace its strategy to export to the rest of the world with exporting to other Asian developing countries or to produce for domestic consumption. It has to continue the export-oriented strategy that has served it so well in the past but must pay greater attention to increasing the competitiveness of its tradable sector, restructuring its industry, especially the state-owned enterprise sector, and strengthen its economic infrastructure (Riedel, 2009). However, if it were to do this, what aspects of the strategy have accounted for the unsatisfactory performance in creating decent employment and what can be changed without violating the fundamental basis of the approach? One area that is commonly mentioned is that, in spite of economic reforms to make Vietnam more open, trade-oriented and integrated into the global economy, they have not gone far enough, which has continued the misallocation of resources and prevented the economy from making the most of its relatively abundant resources (e.g. labour) and growing as fast as it could. Among the more important of the stunted reforms are those on trade and the state-owned enterprise (SOE) sector. Another but totally different one is that the developments that have been responsible for making Vietnam more competitive in the export market have reduced the capacity of the economy to absorb labour. Prominent among these are the significant increases in productivity and the much greater inflow of FDI.

5. Policies on international trade

5.1 Trade policy has traditionally emphasised import substitution and heavy industries at the expense of labour-intensive manufactured goods for export, as production for the domestic market and the more capital-intensive industries enjoy higher rates of protection. In a study on Vietnam's trade policies from the start of the 'doi moi' policy in 1986 to 1998, the Centre for International Economics (CIE) found that, although great strides had been made in changing the trade regime, it was still inward-looking, favouring 'import-substituting activities and production of non-traded goods and services over exporting activities' (CIE, 1998: xiii). This was manifested in a number of ways. First, restrictions were placed on the type of goods that Vietnamese enterprises could import and export, even though licences to take part in international trade were no longer needed. In 1998, nine major products (petroleum, fertiliser, steel, cement, construction glass, motorcycles, cars with 12 seats, paper, sugar and liquor), which accounted for 40% of total merchandise imports and 45% of total manufacturing production, had import quotas and some (e.g. certain types of writing and printing paper and construction steel) were banned. Second, all exports were disadvantaged by an extensive system of import taxes and controls, and some additionally by export taxes, though by 1998 it was reduced to only crude oil and scrap metal.

5.2 Table 5.1 gives the average nominal tariff rate and effective rate of protection (ERP) for 1998 for 31 industries producing traded goods, using production as the weight, with industry specification from the 1995 input-output table of the General Statistical Office (GSO). As the ERP measures the net impact of trade policies (e.g., tariffs and quotas) and other government policies (e.g. local content), it gives a more accurate picture of the level of protection than the nominal tariff rate. The table shows that the ERP is very significantly higher than the nominal tariff rate, indicating an escalating tariff structure where protection is much higher for the production of goods at later stages of processing, which increases effective protection above the nominal protection given to import-substitution production and increases the anti-export bias. Seven industries were very highly protected, with one enjoying an ERP of 416.1% (ferrous metal manufacturing, mainly construction steel), three rates between 150% and 200% (tobacco, alcohol and other beverages, 185%; rubber and rubber products, 179%; and soap and detergents, 162.5%), and four rates between 100% and 150% (textiles, carpets and rugs, 142%; plastic and plastic products, 139%; paper and paper products, 127%; and ceramic, glass and porcelain, 102%). In addition, five had rates between 50% and 100% (tea and coffee processing, 91.6%; vegetable and fruit canning, 75.4%; other industry, 65.1%; and other foodstuffs, 65%; and other metallic products, 50.2%), and one a rate of 40.4% (other chemical products, 44.4%). The heavily-protected industries are capital-intensive, with the clear exception of textiles, carpets and rugs, which is labour-intensive, where the country has a clear comparative advantage and has done well in the export market, producing a major anomaly in the country's tariff structure.

5.3 The bias in favour of import-substitution and heavy industries was caused by beliefs that were prevalent during the hay days of the command economy and still hold sway to a significant extent in the post-1986 period. These are that imports were a necessary evil, rather than the cheapest source of supply for consumer and producer goods, and could aid the country's export efforts; that self-sufficiency should remain an important goal of government, especially in industries deemed to be basic, for fear of being isolated in uncertain times; that industries, when threatened by imports, should be offered protection according to their needs; and that heavy industries, which form the backbone or commanding heights of the economy, should be protected (CIE, 1998: 137).

5.4 The World Bank estimated that if the tariff system had encouraged Vietnam to exploit its comparative advantage in cheap labour, manufacturing exports would make up approximately 63% of total exports, instead of 37% (World Bank, 2001: 12-13). As the number of employees per $1,000 of output for export industries (0.245) is far higher than that for import-substituting industries (0.108), this would have created a net increase of between 1.2 million to 1.5 million jobs. Thus, the bias for import-substitution resulted in a significant loss of jobs. The World Bank study was built on an earlier one by Belser (1999), which was, in turn, based on the cross-country study by Wood and Mayer (1998), which shows that in open-market economies, a large supply of well-educated workers relative to land is strongly correlated with a high share of exports in the output of the manufacturing sector. The finding confirms the prediction of the traditional Heckscher-Ohlin theory of comparative advantage that open-market economies tend to export goods whose production uses intensively its relatively abundant and thus cheap resource, which for Vietnam is labour.

Table 5.1:
Average tariffs and effective rates of protection by input-output industry, 1998

Industry	Average tariff (%)	Effective rate of protection (%)
Agriculture	11.4	16.1
Forestry	0.5	0
Fishing	20.0	24.1
Mining	1.6	-0.8
Fuels	10.0	17.3
Vegetable and fruit canning	40.0	75.4
Tea and coffee processing	50.0	91.6
Sugar	3.0	-18.8
Tobacco, alcohol and beverages	50.0	185.4
Other foodstuffs	25.9	65.0
Textiles, carpets and rugs	39.7	142.7
Leather, footwear and bleaching	20.0	23.3
Wood processing and products	10.9*	16.1
Paper and paper products	30.0	127.4
Petroleum and natural gas	33.5*	NA
Fertilisers and pesticides	0	-5.6
Chemical products	3.0	-2.2
Pharmaceuticals	9.1*	22.7
Soaps and detergents	30.0	162.5
Rubber and rubber products	43.4	179.0
Plastic and plastic products	34.7	139.0

Other chemical products	17.5	44.4
Ceramics, glass and porcelain	40.8	102.4
Cement	14.4	28.7
Other non-metallic minerals	11.3	20.0
Manufacture of ferrous metals	40.0	416.1
Manufacture of non ferrous metals	0.7	-4.7
Equipment and machinery	8.3	9.9
Electrical and electronic products	23.6	59.8
Other metallic products	28.3	50.2
Other industry	40.0	65.1

Source: CIE (1998): 122 and 124

5.5 The finding that exports contribute significantly more to employment creation than import substitutes was confirmed by Jenkins (2004a). This decomposes the change in the demand for labour into four components: (i), change in the demand for producing for domestic demand, (ii), change in the demand for producing exports, (iii), change in the demand for producing import substitutes, and (iv), change in productivity. For the manufacturing sector for 1995-99, the growth in domestic demand created 443,000 jobs and the growth in exports, 700,000 jobs (Table 5.2). The demand from growth in producing for import replacement fell by 224,000, and increases in productivity led to a further loss of 570,000. Having a more export-oriented strategy would have increased employment creation, as the net trade effect was 476,000 (700,000 less 224,000). The same results were obtained when regression analysis was used to identify the determinants of employment. The share of imports in output was negatively related to employment, which is expected because firms are forced to become more efficient to compete with imports. The share of exports in output was positively related, which implies that the country's comparative advantage in labour-intensive activities has offset the increase in productivity needed to be competitive in the export market. The same results were obtained when changes in import and export shares were used as indicators of openness. Thus, an export-oriented strategy creates more jobs than an import-substituting one, so that government should not only continue its policy of openness but accelerate it.

Table 5.2:
Sources of employment growth in manufacturing, Vietnam, 1995-99

Source	Number of jobs
Domestic demand	434.974
Exports	698.703
Import penetration	-224.259
Productivity growth	-569.500
Total employment change	339.918
Net trade effect	474.444

Source: Jenkins, 2004a: 20.

5.6 Such a high level of protection leads to an inefficient allocation of resources and harms the economy in a number of ways. First, it penalises consumers by making the goods they buy more expensive, and producers and exporters by increasing their production costs through having to use more expensive inputs produced locally under protection. Second, it directs domestic investment and FDI towards protected and inefficient industries. For example, over 50% of FDI were in sectors with nominal tariff rates over 34%, and around 65% in sectors with effective rates of protection over 60% (CIE, 1998: 131). It reduces the creation of jobs as it produces a perverse impact on employment creation. In spite of their limited employment impact, import-substituting and heavy industries are encouraged while, in spite of their greater employment impact, their labour-intensive counterparts are discouraged as they face greater competition from imports.

5.7 In a more recent study, Athukorala (2006) found that up to 2003 the bias in favour of import-substitution and capital-intensive industries has continued. The average unweighted nominal tariff rate increased from 13.4% in 1997 to 16.65% in 2003, while the trend to simplify the tariff system, which initially reduced the number of tariff bands from 35 to 15, was reversed so that by 2003, it had grown to 60. In some industries where Vietnam has a comparative advantage in exporting, the tariffs on intermediate goods used as inputs are much higher than those on intermediate imports used in import-competing industries, thus favouring import-substitution over export promotion. While Vietnam's nominal tariff structure (number of tariff lines and bands, range of tariff rates, average tariff rate and variation in the rates) is generally in line with those in its competitors from ASEAN and China, a different picture appears when the comparison is on the ERP (Table 4.3). In 2003, the ERP of 44% for Vietnam was much higher than those for Malaysia (16%) and Thailand (22.7%). More tellingly, it was much higher than the rates registered by Indonesia (25%) and the Philippines (32%) nearly ten years ago. This prompted the observation that based on the order of magnitude, 'the level of effective protection to domestic production in Vietnam is clearly out of line with the protection levels in other countries in the region' (Athukorala, 2006: 174).

Table 5.3:
Effective rate of protection in manufacturing in selected East Asian countries, 1970-2004

Country	Year	ERP (%)
Indonesia	1975	74
	1987	70
	1990	59
	1995	25
South Korea	1970	40
	1975	55
	1980	67
	1985	80
	1988	28

Malaysia	1969	45
	1979/80	31
	1988	23
	2003	16
Philippines	1992	32
	1999	10
Thailand	1981	74
	1988	51
	2002	25.2
	2004	22.7
Vietnam	1997	121
	2002	95
	2003	44

Source: Athukorala, 2006: 175.

5.8 Many features of the protective system act against the creation of greater employment. First, in spite of direct measures (e.g. rebate of the import duties on intermediate imports) to reduce it, there is still a considerable export bias (measured by 1 – [(1 + ERPd)/(1 + ERPx)] 100, where ERPd and ERPx are the effective rates of protection for production for the domestic market and the production for the export in the same industry respectively, with a positive value showing a bias against exporting, a negative value one in favour of exporting). As industries that succeed in the export market have to use intensively factors of production that are abundant and therefore cheap in Vietnam (e.g. labour), the export bias acts against labour-intensive industries and so slows down employment creation. For the well-established large exporting firms, which enjoy the most compensation, the bias in 2003 was still 25%, having fallen from 55% in 2001. The bias is present even in those sectors where Vietnam has excellent chances of succeeding in the export market such as garments, plastic products, leather goods, ceramics and other manufacturing. For the average exporter, the respective figures were 57.7% and 137.1%. If there had been no compensation, the export bias in 2003 would have been 105.4% and that in 2001, a massive 483.2%. Some industries faced with a high export bias (especially wearing apparel, shoes and furniture and electronics) have done well in the export market only because the firms doing the exporting are foreign-invested enterprises, for whom the crucial comparison is between the relative profitability of producing in Vietnam and elsewhere, not the size of the export bias per se. During 1995-2002, foreign-invested enterprises accounted for over 90% of Vietnam's annual increase in manufacturing exports. However, the export bias has deterred local firms, in particular small and medium-sized ones, from entering the export market. And as these are labour-intensive, it acts as a hindrance to employment creation.

5.9 Other aspects of the tariff structure observed by Athukorala (2006) for 2003 (Table 5.4) but representative of the system since 1986, also slow down job creation. First, the effective rate of protection is higher in industries dominated by SOEs and/or the foreign-invested enterprises (FIEs), and lower in those with greater private sector participation (e.g. leather and leather products, rubber

and plastic products, and furniture and other manufacturing), which are more labour-intensive. Second, profitability, measured by the price-cost (P-C) margin, is larger in the more protected large and capital-intensive industries, which will direct more investment to such industries. Third, protection is higher in more capital-intensive industries, as measured by the capital per worker (F/E), which encourages investment in such industries. The impact that these features have on employment creation in manufacturing can be seen in the fact that while output in 1999-2000 grew by 9.5%, employment grew by only 1.8%. Output growth was in industries that used very little labour, the result of the trade policy regime, whether intended or not.

Industry code	Industry	ERP	SOE/Y	FIE/Y	E share (%)	P-C (%)	K/E (m. dong)	ΔY/Y (%) 1990-2000	ΔE/E (%) 1990-2000
15	Food, beverages & tobacco	72.98	48.8	39.3	12.2	21.5	16.0	8.0	-2.2
16	Tobacco products	55.30	98.5	1.5	1.0	42.2	8.0	9.8	-5.0*
17	Textiles	70.97	49.8	43.4	10.5	20.7	16.7	13.2	-3.1
18	Wearing apparel	70.56	34.2	47.1	15.5	14.4	5.0	15.4	10.2
19	Leather products	39.15	17.5	67.7	19.2	5.2	6.3	3.0	38.3
20	Wood & wood products	1.15	31.1	28.5	2.5	14.7	2.2	12.9	3.8
21	Paper & paper products	17.09	58.6	17.2	2.7	12.8	9.6	8.3	3.6
22	Printing & publishing	-4.09	97.1	1.1	1.8	21.7	6.6	-19.8	6.0
23	Coke & petroleum products	2.90	-	76.7	0.1	14.4	36.2	14.1	73.7*
24	Chemicals & chemical products	9.67	50.8	38.9	4.0	15.7	7.4	18.2	4.8*
25	Rubber & plastic products	35.67	47.7	28.5	3.5	17.4	12.6	13.3	18.1*
26	Non-metallic mineral products	50.83	62.7	29.6	7.1	27.2	11.2	10.7	-3.6*
27	Base metal products	0.75	40.8	56.5	2.9	11.3	10.1	15.9	1.5*
28	Fabricated metal products	-20.94	23.9	58.4	2.3	13.1	10.7	13.5	8.8*
29	Machinery & equipment	-8.58	43.0	36.6	2.8	19.1	4.2	14.6	3.0*
30	Office, accounting & computing machines	-14.15	-	100.0	0.3	4.2	49.6	20.4	42.7*
31	Electrical machinery	13.15	47.7	40.8	2.4	15.4	8.3	12.6	-9.0
32	TV & telecommunication equipment	13.43	15.1	82.9	1.4	16.6	32.2	12.0	-10.6
33	Medical & optical equipment, & watches	-2.95	22.9	71.5	0.4	14.5	14.0	13.1	15.5*
34	Motor vehicles	79.22	18.2	77.0	1.0	25.6	12.9	19.9	16.1*
35	Other transport equipment	28.10	24.1	70.8	2.3	11.8	4.1	13.2	7.5*
36	Furniture & other manufactures	23.61	8.5	60.7	4.0	10.2	3.5	12.2	4.4*
37	TOTAL	43.90	43.6	45.4	100.0	18.0	10.2	9.5	1.8

Source: Athukorala (2006: 178).
Notes: - Zero or negligible.
** Data for 1995-1999.*

5.10 In line with the preparation for, and the requirements of, WTO accession, tariff levels were reduced consistently. At the 8-digit level, the simple average tariff rate went down from 18.4% that year to 17% in June 2006 and 13.7% in December 2006. By December 2007, it had fallen to 11.7%, with the most spectacular falls in the apparel and textile sectors. The greater impetus to trade and economic growth that this reduction brings has been strengthened by making the biggest cuts for products with higher rates, which has led to a 'compacting of the frequency of tariff rates from a bi-modal distribution with a substantial frequency of tariff rates from 35 to 50 percent in 2003, to a more uni-modal distribution with almost 80% of all tariff rates at 20 percent or lower' (CIEM-STAR, 2008a: 2). All other things being equal, a more compacted or uniform tariff structure with the same overall average as a highly differentiated one tends to produce a more efficient allocation of resources because it reduces the gain from lobbying for protection and enhances transparency and economic efficiency. An uneven structure increases the tendency for importers to shift goods to less heavily taxed categories, and corrupt custom officials to do the opposite unless bribes are paid. Import revenue and the opportunity to improve physical and human infrastructure are lost, and the bribe increases the effective price paid by importers, which reduces the quantity imported and welfare. The time spent by importers to avoid tax and by them and custom officials to reach agreement is also time-consuming and wasteful in itself.

5.11 However, other aspects of the tariff reform have not been so positive. First is that even though the average tariff levels have fallen in most sectors, there are still large differences in the levels among product sectors. For example, even after the December 2007 cuts, while the average rates are lower than 10% for cotton, minerals and metals, chemicals and non-electrical machinery, they are around 50% for beverages and tobacco, and between 20% and 30% for fruits and vegetables, coffee and tea and transport equipment (CIEM-STAR, 2008b: 50). Second is the presence of a significant and growing number of peak tariffs, which are rates that are at least three times higher than the overall average of the group. At the 8-digit level, the number of products enjoying peak tariffs increased not only in absolute terms, from 320 in 2003 to 408 in December 2006 and 619 in December 2007, but also as a percentage of the total number of tariff lines, from 3.0% to 3.82% and 7.5%. These are concentrated in a few important industries, which also registered increases in the number of such tariffs (e.g. transport equipment, increasing from 290 in June 2006 to 295 tariff lines in December 2006) (CIEM-STAR, 2008b: 47). Thus, even though the overall average rate has fallen, the presence of peak tariffs for a sizeable number of individual products in important industries can produce a significant level of protection and inefficiency in the allocation of resources.

6. Policies on state-owned enterprises

6.1 Another area where faster reform could have created more employment is the SOE sector. The programme to reduce the number of SOEs in manufacturing, non-oil exports, and banking credit started in 1986 with the 'doi moi' reforms through equitisation, merger, conversion to limited companies, outright sale and liquidation, with the first the most important. Progress has been good, as the number of SOEs had been reduced from 5,759 in 2000 to 3,720 in 2006 and their share in manufacturing, non-oil exports, and banking credit banking reduced significantly. The list of sectors where total state ownership is to be retained has been shortened substantially, and the average size of the SOEs transformed increased. The equitisation process itself has been improved, with appraisals now conducted by outside evaluators, shares auctioned publicly at market prices, and the percentage of non-employees, including foreigners, in the shares auctioned increasing. Accession to the WTO has also limited the scope for granting subsidies. The efficiency of SOEs has also improved. A survey of equitised SOEs in 2005 reported an average increase of 13% in turnover and 9% in pre-tax profits, which are considerably higher than those in non-equitised SOEs, with the performance better the smaller is the share of state ownership. The census on enterprises reported the same thing, as the total factor productivity of equitised SOEs was higher than that of non-equitised ones, and not too different from that of private enterprises (World Bank, 2006: 63).

6.2 However, much more remains to be done. The transformation programme started very slowly, with the momentum picking up only in 2003. Initially it concentrated on the smaller SOEs, which created little impact, and while the average size of those transformed has increased, the programme is still mainly concerned with the smaller ones. In addition, only 23% of the SOEs being transformed that have capital of over VND 10 billion have completed the process. At the same time, the move to consolidate many SOEs into larger firms, to be called general corporations, to obtain greater economies of scale and develop their own brand names has not worked, as they, unlike the Korean chaebol on which they were based, continued to be protected from foreign competition (Harvard Vietnam Program, 2008: 30). It is also unlikely that the subsequent move to convert them into 19 large conglomerates focussing on strategic sectors will work either because this has given them a virtual monopoly of many heavy industries, which discourages them from taking advantage of WTO membership to break into foreign markets. Some of them, along with equitised state firms and private firms, have bought real estate in the search for quick returns, a move that is very far removed from the original purpose. Other conglomerates (e.g. Petro Vietnam) have founded or acquired controlling stakes in banks, which will allow them to finance risky intra-group expansion plans but with the risks borne by the country. Such developments have led some to fear that conglomerates will become 'vehicles through which politically powerful people enrich themselves at the expense of the state' (Harvard Vietnam Program, 2008: 32). Elements of this may be seen in the slow progress in transforming the SOCBs into commercially-oriented institutions. While these no longer have to lend money to SOEs owned by provincial governments, they still do so when directed by these governments. Such policy lending might be increased by supervising ministries designing sectoral regulations that favour enterprises with the financial backing of SOCBs. The combination of distorted credit misallocation at the provincial level and inefficient market regulations at the sectoral level will damage the economy. And after 20 years of reform, there is still an unusually large number of SOEs, compared to other countries. According to the Economist Intelligence Unit, all this will lead to inefficiency as 'vested political interests may impede reform, thereby preventing the necessary restructuring of some SOEs, which will hamper overall improvements in competitiveness and will constrain Vietnam's growth performance' (Economist Intelligence Unit,

2007: 36 and cited in Harvard Vietnam Program, 2008: 3), which will slow down the rate of economic growth to 5% from 2010 onward.

6.3 The impact of the slow pace of change in the SOE sector on employment creation has been significant because of its size, capital-intensity and inefficiency. It still accounts for 40% of the GDP, which has not changed noticeably since the 1990s and while its shares in manufacturing and banking credit have declined, these are still high at around 32%. Such dominance will normally draw capital and other resources away from the private sector on a significant scale, the so-called 'crowding out' effect. It has indeed been argued that the crowding out of private investment has made the SOEs the major cause of unemployment in Vietnam (Jenkins, 2004b). The problem has been exacerbated by the extreme shortage of capital, which many surveys have shown to be the most important constraint to growth in Vietnam. For example, the comprehensive Investment Climate Survey (ICS) carried out by the GSO in 2006 covering 1,150 formal enterprises in 25 provinces, shows that access to finance headed the list of constraints, with 23.3% of the enterprises saying that it is their biggest problem, a result that is consistent with that of an earlier ICS. The problem for the private sector has not been made any easier by the fact that SOEs have better access to finance than domestic private firms (World Bank, 2006: 75). While the private and non-state sectors account for 90% of the jobs created and 70% of industrial output, the financial system allocates the majority of the credit and capital to the state sector.

6.4 The 'crowding out' impact of SOEs on employment creation has been worsened by their capital-intensity and inefficiency. In 2005, the SOEs accounted for 40% of the GDP but only around 10% of total employment, a ratio that has not changed since 2000. This shows that the SOE sector, with its operation in the mineral, petrochemical, and metal sectors, is relatively capital-intensive and certainly much more so than the domestic private and foreign-invested sectors, as shown by a direct comparison of their capital-labour ratios (Table 6.1). This capital-intensity and enclave nature of production tends to minimise both employment creation and the spill-over into the rest of the economy. If anything, the data under-states the true capital-intensity of SOEs. During the period of central planning, SOEs had a social function as they were used to provide work for the families of those who fought during the wars and had suffered disproportionately. As a result, SOEs were over-staffed and a restructuring and reorganisation programme led to the shedding of many redundant workers, with the social safety net introduced in 2002 to help these and those similarly affected in state-owned farms, to find alternative jobs. However, many SOEs are still heavily over-staffed compared to similarly-sized profit-oriented enterprises. If the remaining redundant workers had been excluded from the labour force, the capital-intensity would be higher. This over-staffing has, of course, accounted for the observed slow growth of employment in SOEs, as they are able to increase output without taking on extra workers.

Table 6.1: Capital/labour ratios of enterprises by ownership, 2005

Chỉ số	State-owned enterprise		Non-state-owned enterprise		Foreign-invested enterprise	
	Level	% of total	Level	% of total	Level	% of total
Number of enterprises	3720	2.8	123392	94.0	4220	3.2
Number of employees (1000)	1907	28.4	3369.9	50.1	1445.3	21.5
Number of employees per enterprise	513		27.3		342	
Annual average capital of enterprises (trillion dongs)	1601.1	52.3	857.0	28.0	604.6	19.7
Annual average capital of enterprises/employees (trillion dongs)	0.00083		0.00025		0.00041	

Source: GSO online data.

6.5 The aim of the reorganisation and renovation of the SOEs is to increase their efficiency and competitiveness and though much has been done, their operational effectiveness, as admitted by the SEDP 2006-2010, is still low and there is a need to accelerate the process (Socialist Republic of Vietnam, 2006: 23 and 119). Another indicator of inefficiency is the over-staffing noted earlier, and the need to eliminate this remains one of the most urgent on the reform agenda. The World Bank noted that while the majority of SOEs are profitable, their returns on equity are often modest. For example, recent audits of 44 major SOEs in Ho Chi Minh City show profit margins of only 6.7%, which is surprisingly low, given the very rapid rate of economic growth and the built-in privileges that SOEs have over private firms (World Bank, 2006b: 64). A number of factors may be responsible for the poor economic performance of SOEs. First, most equitised SOEs continue to be managed by the same individuals as in the past, and old habits die hard. Second, their directors may have allocated the most lucrative contracts to companies that they or their families own, leaving the less profitable ones to the SOEs (World Bank, 2006: 64). Third, and perhaps most important, SOEs have been sheltered from foreign competition by tariffs and a trade control system that favours import-substituting activities and production of non-traded goods over exporting activities (CIE, 1998). In addition, they have been heavily protected against domestic competition from private enterprises. Bad habits from a long period of dependence on state protection have been hard to break.

6.6 When the 'crowding out' effect is combined with the high capital-intensity and inefficiency of the SOEs, the adverse impact on employment creation is amplified, as the more capital-intensive SOE sector not only deprive the more labour-intensive private sector of funds but also does not make efficient use of them. Thus, there is a need to improve the efficiency of the SOEs and to remove the obstacles placed on private enterprises, for this will not only increase the contribution of a major actor to Vietnamese economic growth but also increase growth in the more labour-intensive private sector, thus producing a two-pronged attack on unemployment. The government has

recognised this as the SEDP 2006-2010 has set a high priority for increasing the speed and scope of equitisation along market lines, concentrating on the larger SOEs. The plan is to equitise 1,500 SOEs by 2010, leaving only 28 business activities remaining totally state-owned and only 554 wholly state-owned companies, made up of 26 large-scale economic groups and corporations, 178 enterprises in national defence, security and vital production, 200 in agriculture or forestry, and 150 which are members of corporations or economic groups. Chronically non-profitable enterprises will be disposed of, and the role of government in the governance and management of SOEs gradually eliminated, with state-ownership rights to be undertaken by the recently-created State Capital Investment Corporation (SCIC), a holding company under the Ministry of Finance, whose function is to allocate state capital to maximise its return.

6.7 To accomplish this, changes in several important regulations are necessary, such as changing Decision 155 to reduce the list of totally state-owned activities and Decree 187 to make equitisation process more market-oriented, using public auctions as the main mechanism. It will not be easy implementing these changes because entrenched vested interests will make it hard for the government to 'construct a firewall between economic and political power' (Harvard Vietnam Program, 2008: 3). For example, it appears that the state share of capital in general corporations may not be transferred to the SCIC. If correct, this will introduce inconsistency in the programme and require the introduction of mechanisms to improve their operation and transparency (World Bank, 2006: 65). Setting up the SCIC is a necessary step in the equitisation programme but it will face many difficult challenges. It has to identify good from poor performing SOEs and the annual classification of SOEs in three tiers, introduced with Decision 271, has not always been reliable or easy to implement. Success in listing on the stock market by SOEs will help but this is possible only for the larger enterprises, and other methods have to be used for the smaller ones. The SCIC has to be run transparently, which requires it to report not only the aggregated returns but also the performance of the companies under its portfolio. It also requires it to divorce its commercial from its financial interests, and to base lending decisions on risk assessment rather than connections, which is difficult as it is part owner and part financier. In reality, for the SCIC to run at a profit, it will need to have a manageable investment portfolio, which means that it may be necessary to exclude a large number of small, non-strategic enterprises from its operation.

7. Policies on globalization

7.1 Important though the impact of policies on trade and the SOE sector on the creation of decent employment, paradoxically, a greater impact might have been the changes needed and implemented for Vietnam to integrate successfully into the global economy. An important requirement was to increase Vietnam's productivity, which, at the start of its globalization, was very low by the standards of its competitors in East Asia and Southeast Asia. For example, in 1990 its value added per worker in manufacturing was only 6%, 9% and 19% of those of Thailand, Malaysia and Indonesia respectively, and 57% of that of China (Table 7.1). The same was true of its value added per worker in agriculture. The productivity levels would have to rise very substantially if Vietnam was to compete successfully against these countries. Another requirement was to increase the level of FDI, which, in terms of FDI per capita or FDI per $1000 GDP, was low in 1986-1990, compared to that in ASEAN and developing countries in general (Table 7.2). The low level of FDI had to be increased significantly for the investment funds, management and technological benefits, and access to international markets that it provides.

Table 7.1:
Country comparisons of value-added per worker in manufacturing and agriculture

Country	Value added per worker in manufacturing (US$)		Value added per worker in agriculture (US$)	
	1990	2000	1990-92	2003-05
Vietnam	971	2,130	214	305
China	1,702	5,258	254	401
Indonesia	5,155	6,151	484	583
Malaysia	10,917	17,149	3803	5,126
Thailand	16,005	8,276	497	621

Sources: Manufacturing data (Jenkins, 2004b: 203); agricultural data (World Bank, 2008: 357).

7.2 Between 1990 and 2000, Vietnam increased its productivity in manufacturing by nearly 120%, and improved its position relative to the other ASEAN countries, and worsened only in relation to China because of the latter's stellar industrial performance (Table 7.1). The productivity rise in agriculture of nearly 43% was less dramatic but significant nonetheless, and produced relative inter-country movements similar to those in manufacturing. If the increased productivity is caused by such factors as increases in product quality and greater capacity utilization, there may not be any job losses as these will not reduce employment directly or indirectly. However, the situation is very different if it is caused by technological progress as this allows more output to be produced with fewer workers. Job losses in the firm or sector concerned can be avoided only if the reduced demand for labour per unit of output is offset by an increase in labour demand from the expansion in output. There may even be increases in jobs in the same or other sectors in the long run if it leads to the creation of new products or the expansion of markets (ILO, 2005a).

Table 7.2: Comparative FDI flows in Vietnam and other developing countries

Nước	Average annual FDI flow			Average annual FDI flow per $1,000 GDP (US$)		
	1986-1990	1991-2000	2001-2006	1986-1990	1991-2000	2001-2006
Vietnam	40	1436	1,649	6	70	37
Cambodia	0	147	229	-	45	43
Indonesia	599	1593	2,060	6	7	5
Malaysia	1,182	4934	3,480	31	65	29
Singapore	3,333	9565	15,587	124	121	148
Thailand	1,227	3260	6,367	17	26	40
ASEAN	6,979	23,088	31,824	24	40	40
China	2,926	32,765	59,272	8	42	36
Developing countries	26,776	140,205	255,575	8	24	30

Source: UNCTAD, 2008: Table 1.2: 9.

7.3 In the case of Vietnam, increased productivity was caused by the introduction of more efficient technologies and the available evidence is that this has led to job losses in the short and medium terms. The adverse effect of rising productivity on employment growth is seen in the micro study of SOEs in the textiles and garment industry by Thoburn et al. (2007). For firms to be part of the value chain of leading global buyers from Europe, America and Japan, they have to install newer vintages of equipment that use less labour per unit of output and per unit of investment. Thus, globalization pushes the industry to shed labour, and employment will fall unless output increases more than proportionately, which happened in the garment, but not the textile, industry. As a result, employment in the textile industry fell by 31% in the 1990s, mainly in areas dominated by female workers, such as spinning and weaving. Interviews conducted with SOE executives confirmed that the main reason for increased productivity was the need to regain losses in export earnings from the collapse of the Soviet and Eastern European markets, where Vietnam enjoyed preferential treatment (Thoburn, et al., 2007: 349).

7.4 The negative relationship between rising productivity and employment growth is also found in the macro study by Jenkins (2004b), which used decomposition analysis by ownership for manufacturing employment over two separate periods, 1990-94 and 1995-99. In the analysis by industrial sector, he found the increase in labour productivity within industries to be a far more important reason than resource mis-allocation from the bias in favour of import-substituting and capital-intensive industries and the capital-intensive SOE sector. For example, for 1995-99, if there had been no structural or productivity growth, employment growth would have been 1,665,246 but when structural change and productivity growth were incorporated, it was only 288,628 (Table 7.3). Thus, there was a very significant decrease in the employment per unit of output, with productivity growth accounting for a fall in employment of 1,123,185 and structural

change a much smaller one of 252,260. In the analysis by ownership, it was found that the special treatment given to SOEs had a far smaller impact on employment growth than increases in productivity. For example, for 1995-99 in the SOE sector, productivity change led to a drop in employment of 341,382, reflecting the massive retrenchment of workers under the restructuring program, and the change in share a smaller drop of 169,516. The respective figures for domestic firms were 804,609 and 311,578. Foreign-invested firms increased their share in employment but this impact was reduced by a drop in productivity, caused probably by a switch to more labour-intensive industries.

7.5 Thus, the main cause of the slow employment growth in manufacturing in the 1990s was the increased output per worker, and not the shift towards more capital-intensive industries, whether these were owned by state-owned, domestic or foreign-invested enterprises. The increased productivity was caused by the need to be more competitive as the economy became more open and engaged in the global economy. At the beginning of the 1990s, the value-added per worker in manufacturing in Vietnam was very low by ASEAN standards, as the technology used was old and inefficient. It increased very rapidly over the decade, with productivity growth faster in industries with higher import to production ratios (Jenkins, 2004a), showing the need for industries producing traded goods to be more competitive than those producing non-traded ones. The slow growth in employment growth from the need to be more productive has been worsened by the high dependence on imported inputs, which has reduced the indirect or multiplier effect. In 1999, of the four most important industries, only food and beverages had an imported materials and supplies to sales ratio (21.7%) that is below the manufacturing average of 32%, with leather and footwear, clothing, and textiles registering ratios that ranged from 44% to 57% (Jenkins, 2004b: 205). Thus, Vietnam faces a dilemma in its globalization programme. As its production costs rise with wage increases, it can no longer compete at the bottom end of the value chain and has to increase its productivity to continue its rapid growth rate in exports. However, by doing this, the capital-intensity of its operation will rise and adversely affect its capacity to create jobs.

Table 7.3: Decomposition of employment growth by type of firm

Firm type	Period	Share change	Productivity change	Interaction
State-owned enterprise	1990-95	-16,566	-625,346	7,657
	1995-99	-169,516	-341,382	47,330
Domestic firm	1990-95	-367,085	-819,227	105,166
	1995-99	-311,578	-804,609	86,482
Foreign firm	1990-95	9,288	51,216	25,706
	1995-99	65,586	41,401	15,908
All enterprises	1990-95	-374,364	-1,420,357	138,529
	1995-99	-415,508	-1,104,591	149,720

Nguồn: Jenkins, 2004b: 201.

7.6 FDI inflow to Vietnam has increased very rapidly in recent years, where it went from an annual average of $40 million in 1986-90 one of $1,649 million in 2001-06. As a percentage of the GDP, its growth was especially rapid in the 1990s, where it averaged $70 per $1,000 of GDP, which was much higher than the ASEAN average of $40, and higher than that in most other countries in the region, including China (Table 7.2). As the economy grew, the ratio fell, so that by 2001-06 it was at a level ($37) more typical of that found in ASEAN. By 2006/07, FDI accounted for 13% of the GDP, 38% of industrial output, 18% of gross fixed capital formation, 57% of exports, and 22% of employment (Table 7.4). For industrial output and exports, this makes the foreign-invested sector the most important sector in Vietnam.

Table 7.4: Indicators of importance of FDI in Vietnam (%)

Enterprise type	% of GDP (2007)	% of industrial output (2007)	% of gross fixed capital formation (2006)	% of exports (2007)	% of taxes (2002)	% of employment (2006)
Foreign-invested enterprise	13	38	18	57	37	22
State-owned enterprise	40	32	52		52	28
Private domestic enterprise	47	30	30	43	11	50

Source: UNCTAD, 2008: 28; Riedel, 2009: 28.

7.7 The general expectation is that the rapid growth in FDI inflow and its significance in the economy will benefit Vietnam because, apart from the direct effects of providing the required savings and foreign exchange for investment, and improving access to international markets, it can have positive spill-over effects. Thus, it transfers management and technological skills to domestic producers, enables them to enjoy economies of scale by purchasing their products, improves the quality of their products, and increases their productivity by providing more competition. However, FDI can also have negative spill-over effects, such as environmental degradation, transfer pricing and loss of national control over strategic sectors of the economy. An adverse effect of central importance to this study is the crowding out of private investment because of the foreign firms' greater productivity, from using more modern and capital-intensive technology, and by the special treatment they receive from financial institutions on credit and from government on investment incentives and property rights. The loss of employment by the displacement of domestic firms is not replaced because of the greater capital-intensity of foreign firms. There is some, though not strong, evidence of this crowding out in Vietnam.

7.8 There is no shortage of evidence to show that foreign-invested enterprises (FIEs) are more capital-intensive than private domestic enterprises. For example, in 2005, the average capital per employee of FIEs was $25,000, compared to the $11,000 for the local private enterprises (UNCTAD, 2008: 20). If manufacturing industries were divided into high, medium and low capital-intensive groups, in 1995 nearly 50% of FIEs were in the high capital-intensity group, compared to 33% for SOEs and 38% for domestic firms, though by 1999 the differences were less stark, the respective shares being 39%, 31% and 35% (Jenkins, 2006: 131). In 1997, the capital-labour ratio of FIEs was seven times that of SOEs and eleven times that of private

Vietnamese firms. On average, for a given output level, SOEs generate nearly three times and local private firms nearly six times as many jobs as FIEs. In their study of the processing industries of textiles and garment, food processing and mechanics and electronics, Nguyen, Vu, Tran and Nguyen (2006) found that FIEs are about three times as capital-intensive as their local counterparts.

7.9 This greater capital-intensity has led to greater productivity. While FIEs accounted for 38% of industrial output, their share of industrial employment was only 22%, a ratio of 1.7, compared to the ratio of 1.1 for SOEs and 0.6 for private firms (Table 7.4). This shows that labour productivity is significantly higher in FIEs than in the rest of the economy, which is corroborated by the fact that the average earnings in FIEs in 2002 was double that in private firms and almost 50% higher than in SOEs (UNCTAD, 2008: 23). The same conclusion was drawn by Jenkins (2006) in his decomposition analysis. The difference in the number of jobs created per unit of output can be decomposed into two components. The first is differences in the employment per unit of value added, which is the inverse of labour productivity, a proxy for differences in technology. The second is differences in the ratio of value added to output, a measure of the degree of vertical integration. In turn, each component can be decomposed into intra-industry differences and differences in the industrial composition of output. The most important reason for foreign affiliates generating a smaller number of jobs is their higher productivity through the use of more advanced technology, though their lower level of vertical integration from greater dependency on imported inputs and their greater concentration in less vertically integrated industries are also important.

7.10 There is some prima facie and empirical evidence that domestic private industrial enterprises had been crowded out by FIEs and SOEs. Earlier reforms had largely by-passed them, and it was not until 1990, with the passing of the Law on Private Enterprises and the Law on Companies, that they received some assistance (Athukorala and Tran, 2009). However, even after that, biases favouring FIEs and SOEs remained, and the procedures for obtaining business licences and re-registration were complicated and opaque, giving rise to bureaucratic red tape and corruption. Thus, in 1986-1999, their development was relatively weak compared the FIE sector with the other sectors of the economy, including the FIE sector (Mallon, 2004). That the administrative discrimination had hindered their development can be seen from the fact that after it was removed by the new Enterprise Law of 2000, their numbers increased four-fold between 1991-99 and 2000-06 (Athukorala and Tran, 2009: 7). Jenkins found that for 1995-99, industries where foreign ownership had risen significantly had tended to lag behind in employment growth (Jenkins, 2006), suggesting that foreign affiliates had crowded out labour-intensive local firms and decreased their market share. It also forced the remaining ones to adopt more capital-intensive and therefore less employment-creating techniques in order to survive. The market share of SOEs was not similarly affected because of their greater involvement with foreign affiliates in joint ventures but those not in such joint operations have also to adopt more capital-intensive techniques to compete. UNCTAD pointed out that competition from FIEs was likely to produce the failure of some SOES and private enterprises (UNCTAD, 2008: 28), and Riedel that the private corporate sector could have suffered from FIEs' greater and cheaper access to bank credit and property rights, which could also have forced some private firms into joint ventures with foreign firms to benefit from the preferential treatment (Riedel, 2009: 15).

On the other hand, a study by the CIEM, from a survey in late 2004 of 33 domestic enterprises and 60 FIEs in the textiles and garment, food processing and mechanical and electronics industries, found that domestic enterprises saw competition from FIEs to be no more onerous than from other domestic enterprises (Nguyen, Vu, Tran and Nguyen, 2006: 55-56). The same study carried out a macroeconomic study on the spill-over effects of FDI but did not test specifically for the crowding-out effect. A final verdict on the issue will have to wait for the conduct of more rigorous studies.

8. Summary

8.1 The following main conclusions on the impact of the export and FDI-driven industrialization strategy on employment in Vietnam can be drawn from a survey of the existing literature.

- Much has been achieved on employment creation and equity reduction but not enough work has been provided for those who want to work and for many who do find work, it often does not meet the requirements of decent work.

- The unemployment rate of around 2.5% in recent times understates the actual level of labour under-utilization, and even the reported urban and rural unemployment rates are high by ASEAN standards.

- Agriculture provides full-time and shared work that has low pay and productivity, with income and conditions that do not meet the requirements of decent work and the same can be said of some sections of the service sector.

- Some of the changes in the industrial origin of employment are illusory because many workers in the service and own-account-worker sectors are there as a last resort, putting up with low pay and long hours until they can find something better.

- Youths account for 45% of all unemployment in Vietnam, with an unemployment rate that is many times that for adults, and the seriousness of the problem probably understated because many young people might have dropped out of the system from despair after failing consistently to find work.

- While disparity in wage employment between men and women has gone down and gender labour segmentation contributes only marginally to the wage gap between the poor and non-poor, women are more likely to find work in the low-pay and low-productivity agricultural, informal and self-employed sectors, while facing inequality in the household and discrimination in the issue of land titles.

- In spite of the marked drop in the incidence of poverty, many of those living above the poverty line are vulnerable, as their income is very close to the poverty line where only a slight increase in spending or fall in income will push them below it again.

- Migrants or workers in the informal or self-employed sector, who constitute an important section of the vulnerable, face wage discrimination, largely because of the restrictions they face in accessing support services.

- The number of workers seeking employment overseas is rising and though this can be seen positively as they reduce the pressure on the local labour market, increase employment and reduce poverty through remittances, and produce greater world output, it fundamentally reflects a shortage of well-paid jobs at home.

- The manufacturing sector, on which much has been depended to provide decent work, appears not to have the labour-absorptive capacity desired and does not compare well with that in other ASEAN manufacturing sectors.

- The capacity of the economy to absorb labour is very low compared to that of many other ASEAN economies and reflects the fact that growth of output has concentrated on industries that do not hire much labour.

- Unless the labour-absorptive capacity is increased significantly, the target of 8 million jobs over 2006-2010 would not be achieved, even if the target GDP growth rate is achieved, and the global financial crisis has made this highly unlikely.

- Ironically, many of the decent jobs created cannot be filled because of a serious shortage of skilled workers.

8.2 Two important events, accession to the WTO and the global financial crisis, have not helped the situation.

- Accession did not require Vietnam's trading partners to alter access to their markets as they had already granted it most-favoured-nation status Vietnam's trading partners had already granted it most-favoured nation status.

- There has not been enough time for the full effect of membership on trade to take place.

- The global financial crisis had come hot on the heels of the accession and would have negated the increase in export that had been expected in normal times,

- There has been much soul-searching on the wisdom of continuing an outward –looking development strategy because of the belief that the use of the large persistent current account surpluses of Asian developing countries as cheap funds to support the current consumption and risky investments of spendthrift developed countries, principally the US, has led to the crisis.

- However, the alternative strategy suggested for Vietnam of trading more with other developing nations is not viable because South-South trade is largely in intermediate products used in producing final goods for export to developed countries, so the linkage to these countries still exists.

- The other alternative of producing more for domestic consumption is unnecessary and premature as it will happen naturally in a growing market economy once development reaches a certain stage, and Vietnam is no where near that stage.

- In the foreseeable future, Vietnam has to continue with its export and FDI-driven strategy but with greater efficiency.

8.3 The labour-absorptive capacity of the economy can be increased by accelerating the rate of economic reform.

- Trade policies need to be more open, with the bias towards import substitution and heavy industries and that against exports removed.

- The tariff system has to be changed to encourage the exploitation of the country's comparative advantage in cheap labour, so that manufacturing exports make up significantly more of its exports, and create significantly more jobs.

- The effective rate of protection for industries dominated by more capital-intensive state-owned and/or foreign-invested enterprises should be lowered to reduce the bias against enterprises with greater private sector participation, which are more labour-intensive.

- Less help should be given to large and capital-intensive industries, so that the higher profitability from higher protection would not attract more investment and perpetuate the bias against employment creation.

- Reform in the SOE sector has to extend beyond the smaller enterprises, and completed more quickly for the larger ones.

- The protection that SOEs enjoy from foreign competition has to be reduced to improve the chances of success of the programme to consolidate many enterprises into larger firms to obtain greater economies of scale and develop their own brand names.

- The conversion of the consolidated SOEs into 19 large conglomerates in strategic sectors has to take place without them enjoying virtual monopoly power.

- The move by some SOEs into real estate in the search for quick returns should be monitored more carefully because they have little or no expertise in this area, as should the move to establish banks or acquire controlling stakes in banks, to prevent them from financing risky intra-group expansion plans where the risks are borne by the country.

- The size, capital-intensity and political influence of SOEs should not allow them to continue crowding out labour-intensive and efficient private enterprises.

- The need to change the policies on trade and SOEs is greater because of the urgent requirement for Vietnam to increase its productivity significantly, through using more modern and capital-intensive technology, which will reduce the labour-absorptive capacity and produce a trade-off between productivity and employment growth in the short and medium term.

- The urgency for such reforms is also greater because the greater number of foreign firms, with their bigger size, use of more modern and capital-intensive technology, and special treatment in obtaining credit, investment incentives and property rights, have enabled them to crowd out more labour-intensive private domestic firms.

- The loss of employment by displacing domestic firms is not replaced because of the greater capital-intensity of foreign firms.

8.4 In discussing the impact of export and FDI-driven industrialization on employment, sight should not be lost of the fact that agriculture still plays the dominant role in providing work, and that the greatest impact on the creation of decent employment in Vietnam will probably come from having a buoyant agricultural sector. Sight should also not be lost of the fact that achieving the multiple development objectives in a globalized market environment has become more challenging.

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Export and FDI- driven industrialization strategy and employment in Vietnam

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