

2 Economic development in Vietnam during the second half of the 20th century: How to avoid the danger of lagging behind

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1. Introduction

Looking back at the 20th century and comparing Vietnam with other countries in the Asia-Pacific region, one can see a remarkably widening economic gap between the former and the latter during the second half of the century. Over the last 40 years, the Asia and the Pacific region has grown rapidly, and can be characterized by an extensive industrialization across the region. Due to its historical condition, Vietnam has lost several decades of development and lagged behind its neighbors. The *Doi Moi* has integrated Vietnam to the regional industrial surge in Asia. How is Vietnam positioned now and what is the prerequisite for it to shorten the distance between it and neighbouring countries?

2. Vietnam's Economy in the Second Half of the 20th Century

The war in Vietnam ended and the country was reunified in 1975, but the complicated political situation in the region made it difficult for the economy of Vietnam to move to a peaceful development stage right after the reunification (not until 1989 did Vietnam withdraw all its troops from Cambodia). The *Doi Moi* officially started in 1986, but bold and thorough steps only began in 1989 and showed effects in 1992 when the economy grew rapidly and the hyperinflation was curbed.

For these reasons, the second half of the 20th century can be divided into two periods: 1955-1991¹ and 1992-2000. The analysis of the first period will focus on the comparison of Vietnam's economic development with that of a number of neighboring Asian countries, the discussion on the second period will mainly assess the *Doi Moi* achievement and the positioning of Vietnam in the Asian economic picture. Prior to 1975, Vietnam had a dual economy, therefore the first period was subdivided into 1955-1975 and 1975-1991.

2.1 Characteristics of Vietnam's Economy from 1955 to 1991: A Comparison with Asian Countries

To compare the growth rate and the structure of Vietnam's economy with other countries in the region, a recalculation and conversion of Vietnam's economic

¹ The first period started from 1955 (not from 1951) since 1954 was a big historical significant point, and also for the statistical and data reasons.

indicators were needed (prior to 1993, the material product system was at work and should be converted to the system of national account of the United Nations). Thanks to the cooperation from the General Statistical Office, we have successfully completed this task in a joint research program on long-term economic statistics of Asian countries.² Although there is room for further improving the estimates of the data, this is so far the only source available for examining the long-term economic trends in Vietnam. The analysis on Vietnam below is therefore based on the findings of our study.

As shown in Table 2.1, during 1950-1973 (or 1955-1975 for Vietnam), Japan experienced an exceptional growth, with per capita GDP growth averaging 8% annually. As a result the real income of the Japanese doubled every 8-9 years.³ The next successful group was South Korea and Taiwan (5-6%), and the per capita income doubled every 12-13 years. Vietnam, China and the Philippines belonged to the slowest grower group, with the per capita GDP growth averaging only 2%, thus it took these countries up to 35 years to double their people's income. These three countries had different political experiences, but the common thing for them was that politics suppressed the development of the production forces. In Vietnam throughout most of this period the economy was characterized by the war and divided into two regions with different economic and political regimes.

Table 2.1: Average annual growth rate of GDP (%) of Vietnam and selected Asian countries in the second half of the 20th century

	1950-1973	1973-1996
Vietnam*	1.9	2.8
China	2.1	5.4
Thailand	3.2	5.6
Malaysia	2.8	4.0
Indonesia	2.5	3.6
Philippines	1.8	0.8
Taiwan	6.2	6.1
South Korea	5.2	6.8
Japan	8.0	2.5

Sources: for Vietnam see Tran (1998, 1999a); for other countries refer to Crafts (1999).

*: Statistics for Vietnam was based on the two periods: 1955-75 and 1976-95.

During this period, the North Vietnamese economy growth averaged 6% (per

² For statistics of Vietnam's economy during 1955-1975, see Tran (1999a) and for 1975-1995, see Tran (1998). The detailed calculations of this research were published in Hanoi in Vietnamese (Tran 2000). The project on long-term economic statistics for Asian countries was conducted by Hitotsubashi University (Tokyo) from 1995 to 2000.

³ There has been a vast literature on the economic development of East Asia. The references are therefore skipped here. Among famous works on this issue published in English in the past decade are World Bank (1993) and Asian Development Bank (1997). The earlier work by Oshima (1987) and a more recent work by Crafts (1999) are also useful for understanding the pattern of economic growth in this region.

capita GDP growth averaged 3%), and the South Vietnamese economy grew at 3.9% (per capita GDP growth averaged 0.8%). In particular, the South's growth was negative in the first half of this period (1965-1975), mostly due to the widespread and bitter war. In terms of economic structure, a large share in the North's GDP was represented by industry (including mining and manufacturing sectors), while a large share in the South's GDP was taken up by services, which reflected the fact that the population was concentrated in urban areas, where the economy was sustained by American aid and military expenses.

In terms of saving and consumption, the South spent more than what it produced during 1955-1975, except for two years 1960 and 1971, therefore the investment to GDP ratio was extremely low (only 7-8% during 1955-1965 and 10-11% during the subsequent period) and totally relied on foreign aid. The North had a higher investment ratio, but during the post 1965 period, consumption also exceeded production, therefore the balance of payment deficit was always high. In general, prior to 1975 both the North and the South had little saving, and the economies grew slowly and heavily relied on foreign aid.

During that time Asian countries, with an exception of China and the Philippines, achieved significant outcomes, especially in the newly industrialized economies (NIEs) like South Korea, Taiwan and Singapore. Since the early 1960s, many Asian countries followed the import-substitution industrialization strategy, and during the 1970s the NIEs started shifting to the export-oriented strategy and competed with Japan in labor-intensive industries. The share of the manufacturing sector in GDP (an important indicator that measures the degree of industrialization) of Japan reached the peak at 35% around 1960 and maintained that level until the mid-1970s, while South Korea caught up with Japan at a high speed. By the mid-1980s, South Korea's share of manufacturing sector in GDP reached the same level with Japan at around 30%. ASEAN countries, especially Thailand and Malaysia, developed at a slower pace, but also actively participated in the industrialization process in the region. Since the late 1970s, the Asian industrial wave in Asia started spreading to China.

Since the mid-1980s, the Asian industrial wave shifted to a new stage with substantive change characterized by high speed of industrialization in China and ASEAN countries, and the shift in the industrial structure took place rapidly in various countries. Japan gradually moved to the post-industrial era, but remained competitive in this sector thanks to the shift to such technology and knowledge intensive industries as automobile, high quality electronics and machinery. Many facilities that produced household electrical appliances such as television, refrigerator, washing machine, car parts, and electronics moved to other Asian countries. Such NIEs as South Korea, Taiwan, and Singapore also shifted their industrial structures from labor intensive to more capital and technology intensive industries.

What was the context for the substantive change in the Asian industrial wave since the mid-1980s? Three factors deserve mention here. Firstly, there was a change in the attitude of ASEAN countries and China toward the operation of the multinational corporations. Previously, especially prior to 1975, these countries feared that the multinationals would dominate their economies, and tried to erect barriers to and curtail the activities of these corporations. This view changed since the 1980s; and facilitated the transfer of capital, technology and managerial skills from the more

advanced countries, such as Japan. Secondly, the Japanese yen appreciated sharply within a short period of time (only after 3 years from 1985 to 1988, the US dollar depreciated by half from 254 yens to 127 yens), which made the production costs in Japan skyrocket, and Japanese companies had to cope with it by expanding their investment abroad. Thirdly, NIEs started shifting from capital and technology importers to exporters of these resources, and have undertaken substantial direct investment in ASEAN countries.⁴ These three factors created a strong capital, technology and business skill flows in Asia and the Pacific, and accelerated the industrialization in this region.

This industrialization was also observed in the shift in the export structure of these countries. The ratio of manufactured products to total export of China and ASEAN countries increased rapidly since the mid 1980s. For example, such ratios of Thailand rose from 42% in 1980 to 77% in 1999, Malaysia from 30% to 82% and China from 48% to 90% during the same period.⁵ South Korea (and Taiwan) was a few decades ahead of these countries, and this share reached 90% in 1990, and kept unchanged since then. Of course Japan was even more advanced due to its higher stage of development and its poor natural resource endowments. Industrial development spread from Japan to NIEs, China, and more advanced ASEAN countries like Malaysia, Thailand and then Indonesia (Vietnam will be considered later). Asian economists described this phenomenon as a flying geese development pattern.⁶

The industrial wave not only extensively spread, but also intensively in Asian countries. Within the manufacturing sector, there was also a shift in the structure. Until 1980s, exporting industries of many Asian countries were mainly labor-intensive such as textile, footwear, toys and simply household tools. However, at present technology and capital-intensive products such as machinery, electronic parts, became more important as a share in exports of these countries. The intra-industry trade became more popular in these countries and moreover, many countries moved from net importers (meaning they imported more than they exported) to net exporter in many technology and capital-intensive industries. Some examples are given below.

In the early 1980s, South Korea moved from a net importer to a net exporter in automobile, machine tools, steel, and others. Thailand strongly developed capital equipment industry over the last 10 years: from net importer to net exporter of machine tools in 1990, as export of electrical and electronic appliances increased rapidly, trade deficit of this industry shrank very fast and the industry tended to move closely to trade balance. In China, export of machine tools increased rapidly since 1985 and more recently China moved from a net importer to net exporter in this industry; its steel and electrical appliances were also very competitive in the world market since the early 1990s. For Malaysia in 1975, machines and equipment accounted for only 6% of its exports, but by mid 1990s this share was more than 50%.⁷

Thanks to these strong developments, East Asian countries have occupied a growing share in the world market for manufactured products. Shares of these

⁴ The second and third factors were analysed in details in Tran (1993) and Tran (1999b).

⁵ Calculated from the UN Trade Statistics.

⁶ See Tran (1997), Ch. 1, and Tran (1999b).

⁷ A more detailed account on this point can be seen in Tran (1999b).

countries grew from 18% in 1980 to almost 29% in 1996. In particular, the share of ASEAN countries and China increased fourfold during the same period.

FDI flows from Japan, Taiwan and South Korea has further promoted the shift in the industrial structure in Asia. The comparative advantage of an industry has shifted from one country to another, and the industrial structure of the more advanced countries also moved in such a way that more share was taken by high value-added industries and technology intensive industries.

The strong shift in economic structure from agriculture to manufacturing and shift within the manufacturing sector from labor-intensive to capital- and technology-intensive helped Asian countries grow faster in this period. As shown in Table 2.1, during 1973-1996, except for Japan, the Philippines (and Vietnam), average per capita GDP of East Asian countries jumped compared to the previous period. Taiwan maintained the high growth of the previous period.

During this time, Vietnam belonged to the slowest growth group in the region (Table 2.1) with average per capita GDP growth of about 2.8%. This figure was higher than that of the previous period thanks to the achievement of *Doi Moi*. As mentioned previously, the impacts of *Doi Moi* has become apparent since 1992. Taking 1991 as the dividing point for the 1975-1995 period, one can see that during 1976-91, per capita GDP only grew at 1.9% (GDP grew at 4.1% but the population grew at 2.2%). This was equal to the growth rate of 1955-75 period. But for the 1991-95 period, average per capita GDP growth jumped to 6.6% (GDP growth was 8.8% and population growth was 2.2%). This was equivalent to that of Taiwan and South Korea during 1973-96.

From 1955 to the early 1990s, per capita GDP growth of Vietnam was less than 2%. This meant that a Vietnamese person needed 35 years to double the income and living standards, while a Taiwanese needed only 11 years, and a Thai 15 years. However, if the *Doi Moi*'s achievements, started in 1992, continue for a very long time towards the future, Vietnam would expect to catch up with its neighboring countries.

2.2 Vietnam's Economy in the Late 20th Century

The economy of Vietnam experienced high and stable growth (at 8-9%) from 1992 to 1997, which is comparable to the neighboring Asian countries. The Asian financial crisis in 1997 brought many countries to recession in 1998, but they recovered in 1999 and 2000. Vietnam was also affected by the crisis (mainly in the areas of exports and inflows of foreign direct investment), and its economy slowed down to 4-5% growth per annum. As this chapter takes a long term view, the issues of the last three years of the 20th century are temporarily put aside. We will return to this period when discussing how Vietnam can avoid the trap of lagging behind in the future.

Vietnam's remarkable development performance during 1992-97 can be attributed to two groups of factors. The first was related to the bold measures and policies of *Doi Moi* from 1989, which liberalized the market and mobilized resources for development, first of all in agriculture, and then in industry and services, in parallel with the efforts to bring hyperinflation under control. The second group was related to the international context that became more favorable to Vietnam. Japanese aid

commenced in 1992 and the donor community, comprised of developed countries and international institutions, started to provide official development aid (ODA) to Vietnam from 1993. This helped to quicken the pace of infrastructure development in accordance with the Government's plan.

These two groups of factors allowed Vietnam to participate in the international division of the dynamic Asia-Pacific region. By 1994, more than 70% of Vietnam's trade was with this region (prior to 1990 more than 70% of Vietnam's trade was with the East European countries). In particular, foreign direct investment (FDI) increased rapidly during this period. These capital inflows were mainly from Japan and NIEs which attempted to promote a strategy of industrial restructuring in the whole Asia-Pacific region. In total investment of Vietnam during 1991-1995 (US\$18 billion), FDI accounted for 25% (US\$4.5 billion) and ODA 11% (US\$2 billion). Share of FDI in total capital formation increased to over 30% in the period of 1995 to 1997 and declined to 25% in 1998, and 18% in 1999 and 2000. By international comparison, however, that share in Vietnam is still high.⁸

In the mid-1990s, Japanese manufacturing corporations, especially those in household electrical appliances such as television, refrigerator, washing machine, plastic, chemical and motorcycle, had plans to move their production plants from neighboring countries to the industrial and export processing zones in Vietnam. They invested a significant amount of capital in Vietnam during 1995-97. The FDI flows from Japan for the three years totaled 93 billion yen, while the total cumulative investment of these companies in Vietnam in years prior to 1995 was only 24 billion yen. Apart from Japan, NIEs also actively invested in Vietnam, especially in labor intensive-industries such as footwear and garment.

Thanks to the initial achievements of *Doi Moi* and the favorable international conditions, Vietnam was able to join the industrial wave that was spreading in East Asia. The manufacturing share in Vietnam's export increased steadily from 1992. Garment and footwear accounted for 26% of total exports in 1997, which was higher than the combined share of crude oil and rice (25%). For comparison, the respective shares of those two groups of export products in 1990 were 1% and 38% respectively.

A deeper analysis of Vietnam's manufacturing exports suggests that these achievements in export should not be overstated, since the import contents of these products were also high (for export processing). However, one has to admit that the industrial wave from Asian countries has come to Vietnam from the mid-1990s and, if continued, as indicated by the experience of neighboring countries, Vietnam in the future would be able to build for itself a more solid industrial structure.

3. Determining the Position of Vietnam's Economy in the Late 20th Century

Where is Vietnam now in the development stage, compared to the neighboring countries? This section attempts to compare Vietnam and Thailand, the two countries which have similar population sizes (in 1990 the population of Vietnam was 66 million and Thailand was 56 million), with similar natural resource endowments, and

⁸ In 1998, FDI share in total capital formation was 12.9% in China, 13.9% in Malaysia, and 12.8% in the Philippines. See UNCTAD (2000).

especially during the 1950s, the two countries were at a comparable level of development.⁹

In addition, depending on the context, China is another comparable country for Vietnam, although no detailed exploration is made as in the case of Thailand. China is a very large country, but has similar political and economy regimes as Vietnam, and also commenced as a backward agricultural country, therefore comparison may be useful.

The comparison of level of development between countries is not easy, since one can hardly find a general indicator that covers the whole development level of a country. However, an exploration of a group of fundamental indicators in Tables 2.1, 2.2 and 2.3 may yield a fairly clear picture. A commonly used indicator is the per capita Gross National Product (GNP) or Gross Domestic Products (GDP). According to the World Bank, in 1996 per capita GNP of Vietnam was \$290, Thailand was \$2 960, and China was \$750. In 1998, the respective figures were \$330, \$2 200, and \$750.¹⁰ However, these numbers do not fully reflect the living standards, as the US dollar purchasing power varies from countries to countries. To have a more accurate comparison, one should use the GNP or GDP based on purchasing power parity (PPP). Table 2.2 shows that in 1998 the PPP per capita GNP of Vietnam was \$1 700 or half of that of China and the Philippines. Table 2.2 also shows that Thailand's living standard is 3.5 times higher than Vietnam's.

Table 2.2: PPP GNP and PPP per capita GNP of selected Asian economies in 1998

	GNP	per capita GNP	
	(USD billion)	(USD)	Compared to Vietnam (%)
Vietnam	131	1 690	100
China	3 984	3 220	191
Thailand	357	5 840	346
Malaysia	155	6 990	414
Indonesia	569	2 790	165
Philippines	266	3 540	210
South Korea	569	12 270	726
Japan	2 928	23 180	1 372

Source: World Bank (2000), *World Development Report 1999/2000*, New York: Oxford University Press.

However, two further problems remain. First, if income distribution is too unequal, the significance of increase in per capita income is undermined. Second, environment, living and working conditions matter. People in two countries with the same per

⁹ According to ECAFE, the predecessor of ESCAP (UN Economic and Social Commission of Asia-Pacific), in 1954, the per capita income of Vietnam was \$117, while that of Thailand in 1952 was \$108 (Indonesia was \$88). Quoted from Japan International Cooperation Agency (1995, p. 13).

¹⁰ For 1996 figures, *World Development Indicators 1999*, and for 1998 *World Development Report 1999/2000*. Per capita GNP of Thailand in US dollar declined between 1996 and 1998 due to the strong baht depreciation during the currency crisis.

capita income (based on PPP) but different in those criteria would certainly have very different quality of life. In brief, with more equitable development and better environmental condition, it is not necessarily to have US\$6 000 per capita to reach the same living standard as Thailand today.

Another group of indicators of the development level of a particular country refers to the changing economic structure. Countries with high population density and backward agriculture must follow a path of industrialization in order to develop the economy. Without industrialization, the agricultural sector itself can also not be modernized. According to the World Bank statistics, in 1994 the share of industry in GDP of Vietnam was 22%, approximately equivalent to that of Thailand in 1980. Vietnam's statistics do not allow us to accurately calculate this share, since it usually include mining, therefore the 22% might be an overestimate of the true share. According to the calculation by Dr. Viet Quang Vu, a senior statistician of the United Nations, in 1993 this share of Vietnam was only 15% (see Vu, 1997, p 90). In a book published several years ago, we based on this figure and concluded that the share of industry in GDP of Vietnam was comparable to that of Thailand in 1970 (see Tran 1997, Chapter 15). Of course, since 1993, Vietnam's industry has grown fast and its level of industrialization in 2000 might have been equivalent to that of Thailand in the latter half of the 1970s.

Regarding the share of manufactured products in export, in 1996, Vietnam's figure exceeded 40%, which was equivalent to Thailand in 1987. However, as mentioned previously, the import content of Vietnam's manufacturing export is very high. On the other hand, Thailand followed the import-substitution industrialization strategy for a long period and only started to promote export during the 1980s, especially after 1985 (therefore the level of industrialization in Thailand's export only started substantially increasing from 1986).

Another important indicator is the ratio of investment over GDP. GDP is the market value of final goods and services produced in a year. These final products, put simply, will be used either for private consumption or investment to generate new capital for production. As a result, the higher the investment rate, the faster the economy can grow in the subsequent years. As shown in Table 2.3, this rate of Thailand was 25% during the 1970s and more than 35% during the 1990s. The rate for Vietnam increased significantly in recent years; it was about 28% in 1997, which was comparable to Thailand's in the 1970s. Investment comes from both domestic (savings) and foreign sources, but domestic source is critical, hence the saving ratio relative in GDP should steadily increase. This ratio for Vietnam now is about 22%, broadly equivalent to that of Thailand during the 1970s.

Table 2.3: Investment and saving to GDP ratio for Vietnam, China and Thailand (%)

	1970	1980	1990	1995	1997	1999
Vietnam						
I/Y	-	-	12.6	27.1	28.3	19.7
S/Y	-	-	2.9	16.1	21.8	22.0
China						
I/Y	-	35.2	34.7	40.8	38.1	37.8
S/Y	-	34.1	37.8	41.1	41.5	39.0
Thailand						
I/Y	25.6	26.4	36.8	41.4	32.2	26.8
S/Y	21.2	20.1	33.6	33.4	32.4	36.4

Source: Economic Planning Agency (2000), *Ajia Keizai 2000* Tokyo: Ministry of Finance (based on the World Bank statistics)

Note: I denotes gross investment, S gross saving and Y gross domestic product (GDP).

Based on indicators of industrialization, saving and investment, together with the additional analysis above, we can conclude that at the end of the 20th century, Vietnam lagged behind Thailand by about 20 years. In 1997, based on the 1993 and 1994 statistics, the author suggested that Vietnam was about 25 years behind Thailand (Tran 1997, Chapter 15). How should the lags of 25 years (in 1997) and 20 years (in 2000) be evaluated? Between 1993 and 2000, Vietnam grew faster than Thailand, and the gap between Vietnam and Thailand should now be shorter than 25 years. This is an area where accurate estimates are difficult to obtain, so one can regard that the current gap between the two countries is between 20 and 25 years.

4. Strategy for Shortening the Gap

The analyses in the previous section broadly suggest that Vietnam is about 20 to 25 years behind Thailand. However, this does not mean that Vietnam needs that amount of time to reach the current level of development of Thailand. If proper policies are in place, the late comers can skip some stage, and this is the general trend observed in the case of Japan, South Korea and many other countries. In addition, as mentioned earlier, if Vietnam's development is more equally shared, and people live in better environmental conditions, Vietnam can reach the same level of well being as Thailand today with a lower PPP per capita income.

Compared to Thailand, Vietnam now has a number of advantages, especially in terms of human development. The United Nation Development Programme (UNDP) combines indicators of education, health and income, and comes up with a general indicator on human development (Human Development Index) for 174 countries. In 1997, Vietnam ranked 110, Thailand 67 and China 98, with detailed indices shown in Table 2.4. If ranked by PPP-based per capita GDP, Vietnam ranked 133, Thailand 60, and China 104. These numbers showed that compared to its per capita GDP, Vietnam attained fairly high level of human development. If measured by some more specific indicators, such as adult literacy rate, Vietnam is not much behind Thailand, and is

even higher than China (Table 2.4).

Table 2.4: Selected indicators on human development of Vietnam, Thailand and China in 1997

	Vietnam	Thailand	China
Human Development Index	0.664	0.753	0.701
Average life expectancy	67.4	68.8	69.8
Adult literacy rate	91.9	94.7	82.9

Source: UNDP (1999), *Human Development Report*, New York: Oxford University Press.

However, the deteriorating quality of education in Vietnam is a worrying sign (see Chapter 13 of this book for a more detailed discussion). All levels of education, from primary to tertiary and post-graduate, have problems that need to be addressed. This has attracted the attention of the whole society for the past five years. Nevertheless, to look from a more optimistic perspective, if all the current problems in education were solved, the human development of Vietnam would be further enhanced, and as this advantage is harnessed, the possibility for shortening the gap from other countries will become more promising.

Another advantage of Vietnam is its geographical location, with the long coastline which is accessible by more developed countries in the region. This natural endowment, together with the political and social stability, and the human capital mentioned above, have all attracted foreign companies to Vietnam since the early 1990s. If the investment conditions are further improved, the country would not be short of capital, technology and business skills necessary for catching up with other countries in the course of its development.

Vietnam's third advantage is that its cities and economic centers are fairly evenly distributed across the country. If an appropriate plan is made right now, population and economic activities can be spread evenly across the country, thus avoiding severe environmental pollution and income inequality between different groups of population and between regions.

The advantages mentioned above are just potential. These potentials should be harnessed to achieve high and sustainable economic growth. With a strong commitment to the country's development and a proper development strategy, Vietnam's GDP would grow at about 8-9% on average per year (per capita GDP would grow at 7% per year) during the first 20 years of the 21st century. If this target can be met, Vietnam's living standards would double every ten years. To achieve such a high and sustainable growth for a long time, it is necessary to accelerate the capital accumulation process and create conditions for effective economic development. These two points require further elaboration.

First is the issue of capital accumulation. The current problem for Vietnam is how to create a conducive environment for both domestic and foreign capital to be invested. Since the mid 1990s, the investment to GDP ratio has risen rapidly, reaching 27-28%, but then dropped substantially (see Table 2.3). This was partly due to the Asian

financial crisis, but more importantly to the inefficient bureaucracy, which increased the transactional costs for investment. The policy for the development of a multiple-sector economy was in place, but the non-state sector faced difficulties in accessing capital, information on investment opportunity and market. The orientation in the industrialization strategy was unclear and the frequently changing policies resulted in higher risks for investment projects.

In particular, FDI has steadily declined since 1997. Given that the domestic private sector is still small and the state-owned enterprises are inefficient and in transition, how could Vietnam maintain a high growth rate in the absence of a powerful reversal of the FDI trend? Looking at their neighboring Asian countries, they are fully aware of the importance of FDI in the course of globalization, and are trying to further attract FDI. After decades of development and FDI inflows, these countries were able to build a much stronger industrial base compared to that of Vietnam. The technology and knowledge in business management of these countries were improved a great deal and heavily relied on the accumulated FDI stock. As a late comer, FDI stock of Vietnam was too small compared to Thailand, the Philippines, and so on. To bridge the gap and to avoid the danger of lagging behind, more attention should be paid to the role of FDI (see Tran, 2000 about the relationship between FDI and the danger of lagging behind).

The second issue is the efficiency of development. Together with capital accumulation, efficient development is the most effective way to bridge the gap with the neighbouring countries. Capital accumulation, though strong, cannot exceed certain limits, due to environment issues and the limitation in capital, technology and market. Therefore, at the same rate of capital accumulation, a country that is more efficient in development would grow faster. Table 2.5 indicates that capital accumulation played a very critical role of China, Thailand, Malaysia, Taiwan, and South Korea during 1960-94, more than in Japan during 1950-73, which was deemed miracle. However, Japan was much more efficient in development (measured in terms of total factor productivity, or TFP), therefore economic growth was higher in Japan than in other Asian countries.¹¹

¹¹ The famous argument by Krugman (1994) that Asian growth has been input-driven should be referred here. According to his view, the economic growth of most East Asian countries has been realized mainly by the expansion of inputs, particularly the capital, not by the technological progress. Therefore, he argues, Asian growth will not sustain due to the law of diminishing returns. This argument has been controversial (See for example, Chen 1997, Tran 2001) but it has been useful for drawing attention to the importance of the efficiency of development. While recognizing the importance of this issue, our scope in this chapter, however, does not extend far to such technical efficiency issue. Instead, we emphasize the allocative efficiency of capital formation.

Table 2.5: Factors contributing to economic growth of selected Asian countries during 1960-1994 (% per year)

	Output Growth	Capital	Labor	TFP
China	7.5	3.1	2.7	1.7
Thailand	7.5	3.7	2.0	1.8
Malaysia	6.8	3.4	2.5	0.9
Indonesia	5.6	1.9	2.9	0.8
Philippines	3.8	2.1	2.1	-0.4
Taiwan	8.5	4.1	2.4	2.0
South Korea	8.3	4.3	2.5	1.5
Japan*	9.2	3.1	2.5	3.6

Source: Crafts (1999), based on findings of various previous studies.

Japan's experience has many implications for Vietnam. To be efficient in development, what should Vietnam do? The author in a publication several years ago (see Tran, 1997, Chapter 2) made an analysis, which is summarized here as follows:

- First, it is imperative to create a conducive environment for sound competition (among different economic actors) and actively integrate into the world market so the capital and other production factors can be most efficiently utilized.
- Second, there should be a long-term plan for human resource development, and mechanism should be put in place to reward labor skills appropriately.
- Third, the environment should be created for science and technology to be widely applied in Vietnam, and business management skills spread throughout the country.
- Fourth, the administrative system should be reformed quickly (with clear responsibilities and authorities assigned of different levels of government so that management can be orderly organized) and qualified and capable people should be promoted to the executive positions. The existing administrative system can easily increase the transaction costs for companies and is a recipe for corruption. Given that environment, businesses would have incentives to develop under table relations with officials (coined as rent-seeking activities by development economists) instead of making efforts to find market, improve technology in order to reduce costs or improve the product's quality. A country can grow fast and efficiently when businesses make efforts in genuine profit-seeking, rather than rent-seeking, activities.

5. Concluding Remarks

During the second half of the 20th century, the industrial wave spread extensively and intensively in the Asia-Pacific region, and countries one after another joined the development process. Due to its historical conditions, Vietnam lost most of the second half of the 20th century in economic development. The reform process has integrated Vietnam to the regional industrial surge since the early 1990s. However, at

the end of the last century, there still existed a big gap between Vietnam and the neighboring countries in terms of development (eg, the gap between Vietnam and Thailand is estimated between 20 and 25 years).

Entering the new century, given the comparative advantages in human resource development and being the late comer in a dynamic region in terms of technology, capital and business skill development, Vietnam is fully capable of shortening the development gap between itself and its neighboring countries. However, that only represents Vietnam's potential and opportunity. The sufficient conditions should be a commitment to avoiding the danger of lagging behind, taking bolder steps in reform, creating a competitive environment among different economic players, and actively attracting FDI. Those are the key factors for fast capital accumulation and efficient economic development; two prerequisites for high and sustainable growth, which makes it possible for Vietnam to catch up with neighboring countries.

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