Vietnam's Industrialization Strategy in the Age of Globalization

National Economic University (NEU)/Japan International Cooperation Agency (JICA)

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1. The purpose and methodology

This joint research between Japan and Vietnam is part of intellectual ODA by the Japanese government. It aims to present concrete and realistic policy advice related to the industrialization of Vietnam as a latecomer developing country.

Under the deepening globalization, Vietnam is striving for the national goal of *industrialization and modernization*, a goal widely shared by other developing and transition countries. After seventeen years since the inception of the *doi moi* reform, and after roughly a decade of serious international integration, Vietnam is still not prepared to take full advantage of trade and investment liberalization for economic development. The fact that international integration comes with both challenges and opportunities is generally well understood, but concrete action to raise international competitiveness is slow to emerge. Various measures such as industrial promotion, enterprise reform, FDI absorption, and trade and investment policy are not integrated. The lack of transparency and certainty in policy environment remains the most serious obstacle for both domestic and foreign firms.

Providing clear industrial vision and stable policy environment requires the collection and analysis of detailed and up-to-date information on key domestic industries as well as global market trends, and a realistic policy making based on such information. What Vietnam needs today is not general debates over "free trade versus protectionism" or "merits and demerits of regional integration," but rather, policy response with concrete numbers and timetables to the imminent industrial problems that the country faces, and the ability to design such response. Our research project hopes to contribute to this process through an in-depth study of Vietnam's industrial, trade and investment policies as well as several individual industries, and discussion of the results with the policy makers.

The appropriate economic regime for developing countries is neither a complete reliance on the market mechanism nor a return to the state-led economic planning. We regard it as self-evident that *government* and *market* be properly combined for each development task in a country like Vietnam where international competitiveness is lacking and markets are underdeveloped. It is our purpose to concretely propose how government and market should be mixed for each case, in light of Vietnam's particular circumstances.

Economics provides us with theories for analyzing the industrialization of developing countries, and we refer to them whenever useful. But theory is often highly abstract and may not give us the right answers to our urgent and pragmatic problems. In combining theory with practice, we have taken care not to uncritically assume standard theoretical premises or international experiences, and spent much time in collecting Vietnamese facts. When we cite a theory, its validity in the Vietnamese context is examined carefully.

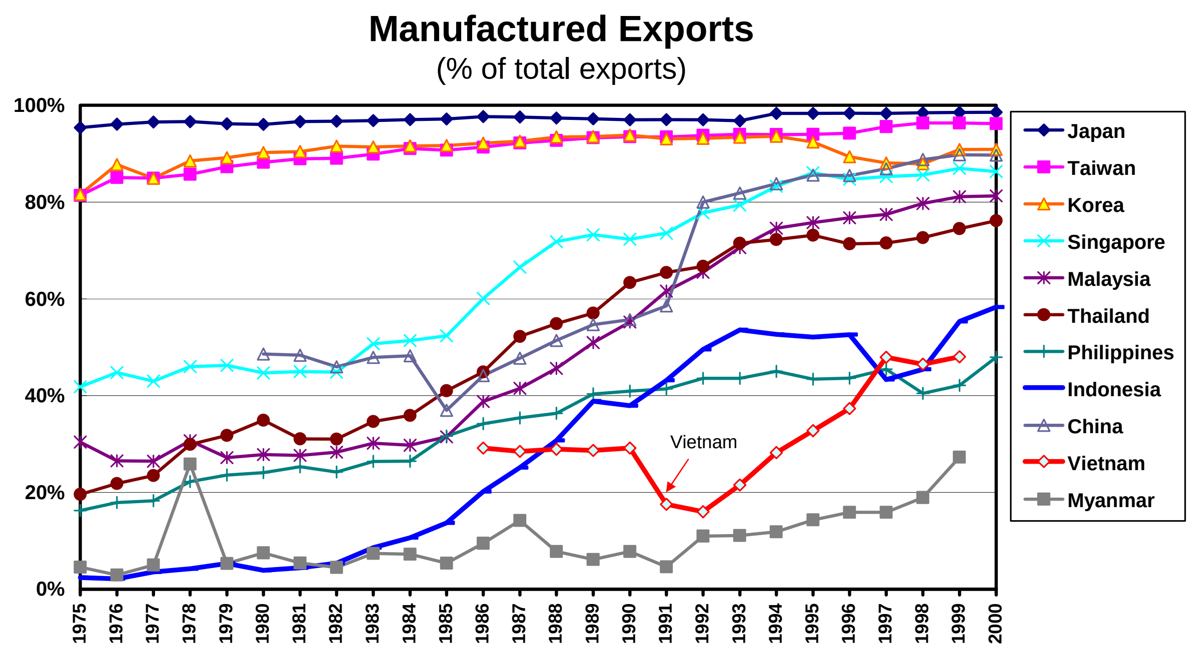
Our project team is in frequent contact with the governments of both Japan and Vietnam, and our members also include Vietnamese policy makers and business leaders. However, all of our analyses and proposals below are made from the academic standpoint, and are by no means the official views of the Japanese or Vietnamese government.

2. Asian dynamism and Vietnam's potentiality

East Asia exhibits a very unique developing pattern. One by one, countries in different development stages have achieved economic growth by participating in the production network created by private multinational corporations. Linked by trade and investment and targeting the markets of the developed countries, a system of international division of labor with clear order and structure exists in the region. Under this system, industrialization has proceeded through geographic widening on the one hand and structural deepening within each country on the other. This supply-side dynamism is sometimes called the *flying geese pattern* of development. To understand this mechanism, we must go beyond individual countries to analyze the production structure, intra-regional trade, and investment flows of East Asia as a whole.

For developing countries in East Asia, economic development is tantamount to becoming one crucial link in this production network under competitive pressure from and cooperative relations with neighboring countries and, through it, upgrading their industrial ability from low-tech to high-tech. To initiate development, they had no choice but to undertake international integration via trade and investment. Every country is under strong market pressure from above and below to constantly improve capability and climb the ladders of development. No other developing region has formed such an organic and dynamic interdependence for growth as East Asia.

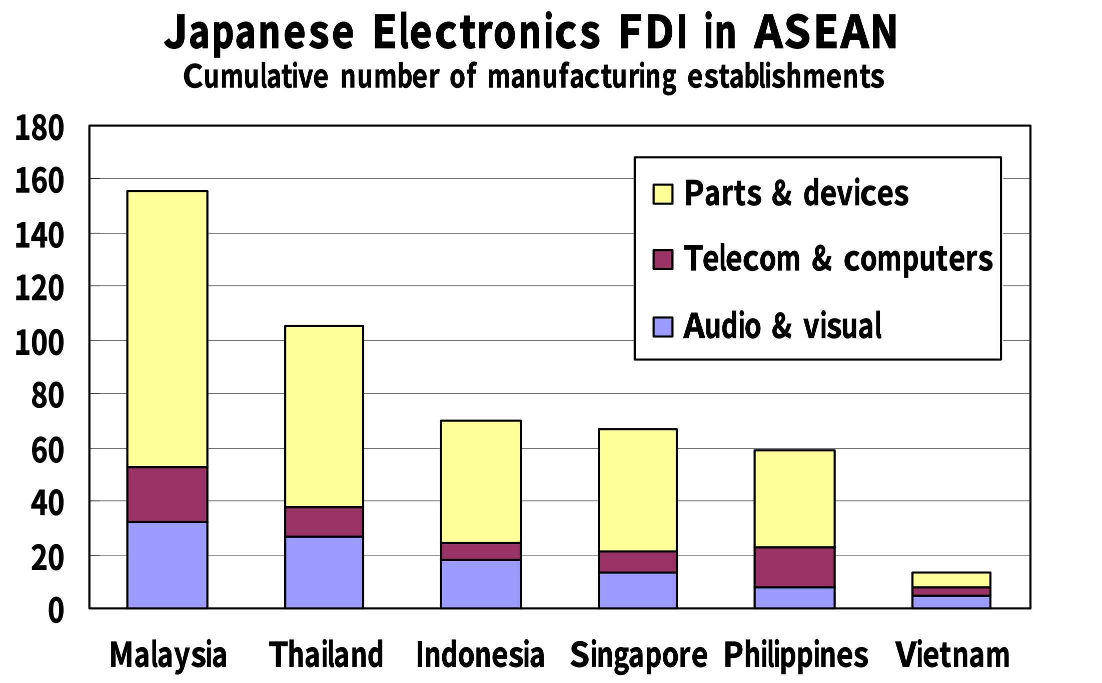
Located in the center of East Asia and endowed with skillful and diligent workers, Vietnam has a good potential to join Asian dynamism and soar as a latecomer goose. Indeed, the national goal of *industrialization and modernization* cannot be achieved except through a successful linking with this regional production network. And the signs of such linkage were already visible in the last decade. However, Vietnam at present still remains at a low stage of development in East Asia's structural transformation chain, measured by either income level or production and export structure. Moreover, there is no guarantee that Vietnam will be able to sustain high growth into the future. That will crucially depend on the quality of policies Vietnam is going to introduce from now on.



Source: ADB, *Key Indicators of Developing Asian and Pacific Countries*, 2001/1993; IMF, *International Financial Statistics Yearbook 1990*. For Japan, *Japan Statistical Yearbook 2002/1999*, Statistics Bureau/Statistical Research and Training Institute, Ministry of Public Management, Home Affairs, Posts and Telecommunications, Japan.

To participate in Asian dynamism, an effective use of FDI is absolutely essential. Competition in the global market is severe while Vietnam's competitiveness is very weak. Domestic firms alone cannot compete squarely with rivals from Japan, US, EU, China, Korea or the neighboring ASEAN countries. The only practical way to Vietnam's industrialization is to attract a large number of FDI by bold policy action, and encourage local firms to link up with their activities and improve competitiveness, step by step. Japanese firms are particularly interested in the potentiality of Vietnam as a manufacturing base.

However, Vietnam's reality at present falls far short of its potentiality. Many foreign firms cite Vietnam as a favored destination, but only a few actually come to invest. The absorption of FDI by Vietnam so far remains miniscule by the East Asian standard. The Vietnam investment boom in the first half of the 1990s lasted only a few years followed by a sharp decline of FDI, even before the Asian financial crisis started. In the recent years, there is a sign of recovery but the investment upsurge is not yet as robust as hoped. At the present level, FDI into Vietnam is well below the critical level required to join Asian dynamism. While the Vietnamese economy continues to grow relatively strongly, it is supported by a large amount of various foreign exchange inflows to the tune of USD 10 billion per year (amounting to over 30 percent of GDP). It is a *prosperity without competitiveness* which cannot be sustained forever.



Source: Electronic Industries Association of Japan (2000), quoted by Yumiko Okamoto, "Electronics and Electrical Industries,"in K. Ohno & N. Kawabata, eds, *Industrialization Strategy of Vietnam*, Nihon Hyoronsha (2003).

On the one hand, Vietnam has long been implementing a multitude of reforms in the areas of state administration, budget, banking, SOEs, legal system and so on under *doi moi* and open door policy, and improvements are surely visible. On the other hand, Vietnam is asked to accelerate trade and investment liberalization through AFTA implementation, USBTA and WTO accession while China as the “factory of the world” is taking competitiveness and FDI away from ASEAN, including Vietnam. The speed of systemic improvement in Vietnam lags behind the speed at which the outside world is changing. As a consequence, Vietnam continues to stay in a relatively disadvantaged position in Asian dynamism.

What Vietnam needs today is a comprehensive and long-term industrialization strategy coupled with master plans for individual key industries based on this strategy. Their contents must be consistent with Vietnam’s current capability, global trends, external economic policy and systemic transition policy. If the government does not clarify where the country is heading with respect to economic regime and industrial structure, firms cannot invest with confidence. The compilation of these strategy and master plans will require information on domestic and foreign economies which is more detailed and up-to-date than currently available. Such information must be continuously analyzed among concerned policy makers and business leaders.

In the early twenty-first century, industrial promotion in developing countries must take a different shape from the one practiced around the 1960s when Japan, Korea and Taiwan were growing rapidly. Back then, the infant industry promotion policy—namely, strengthening of domestic firms through temporary import protection—were permissible and actually conducted. However, Vietnam at present is unable to adopt this policy for the double reason of (i) international commitment to accelerate free trade; and (ii) low capability of Vietnamese firms compared with that of Japanese, Korean or Taiwanese firms at that time. For Vietnam, the only reasonable immediate course of action is to adhere to external openness, absorb FDI as much as possible (especially in manufacturing), and let domestic firms participate in the network of production, trade and investment provided by multinational corporations located in Vietnam. Public investment and ODA must support and complement this effort.

The outdated ideas such as the maximum use of domestic raw materials, self-sufficient industrialization, desire for vertically integrated industrial structure and compulsion for upstream investment, cannot activate domestic or foreign investment in the age of globalization. In fact, they deter international competitiveness and regional division of labor. Unfortunately, in Vietnam, very few government and business leaders adequately grasp the dynamism of the global market or Vietnam's true position in it. As a result, policies and business strategies based on false hope detached from reality are often formulated.

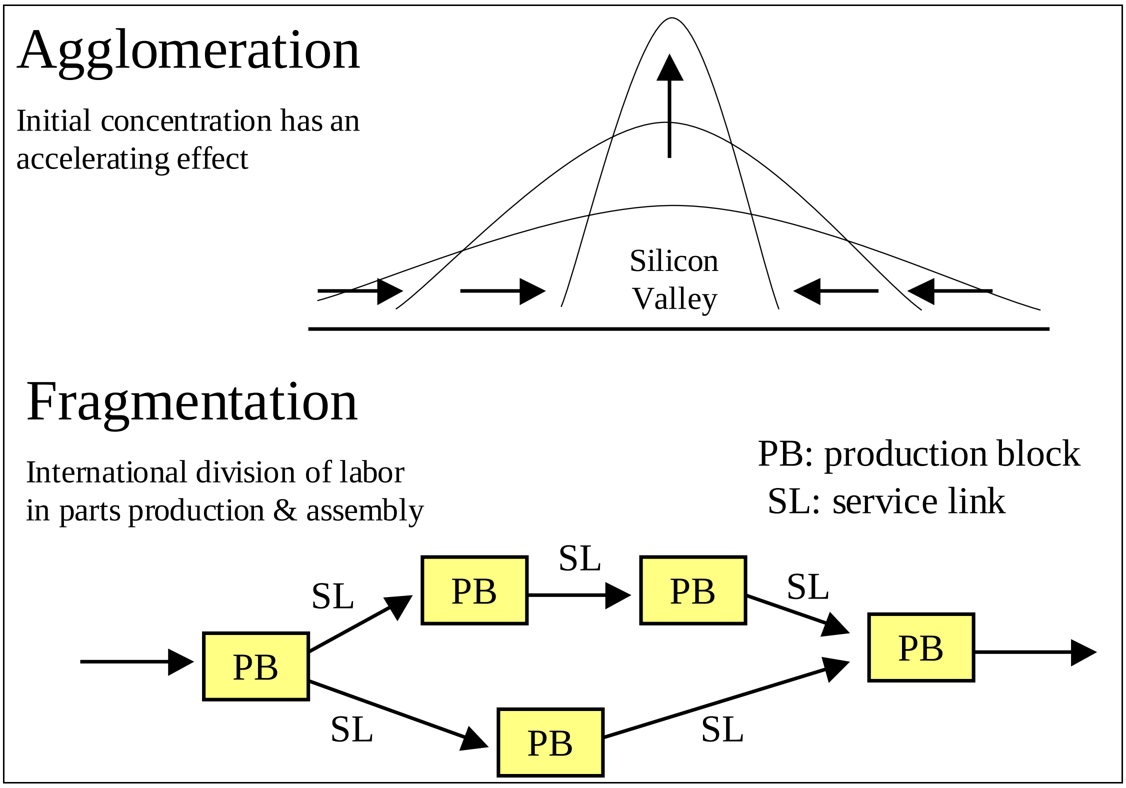
Some people say that industrialization dependent on foreign firms is not really Vietnam's own industrialization. However, no country today—including Japan—can row a boat against the global tide, and it is much less likely that Vietnam, which desperately lacks technology and capital, would succeed in this endeavor. Vietnam's autonomy in the development process is assured not by rejecting foreign influence, but by controlling the inflow of foreign influence to its own purpose. If this is done properly, the identity of the Vietnamese society will be maintained and national autonomy in the process of globalization will be secured. This type of international integration is called *translative adaptation*. Vietnam should abandon unrealistic inward orientation and embark on translative adaptation in the full knowledge of the global situation.

3. FDI dynamics and the critical role of policy

The most urgent task for Vietnam's industrialization is the attraction of a large amount of labor-intensive, export-oriented FDI. To attract FDI when rival countries like China and

ASEAN neighbors are vying for it, external opening or free trade is not enough. Receiving FDI in large numbers requires a bold move and a clear signal, backed by a thorough understanding of the global market and the requirements of foreign investors. What Vietnam should create is not just a better investment climate, but the best business opportunities in East Asia. Stated generally, this requires (i) open and stable policy environment; and (ii) reduction of business costs on all fronts (details later).

The traditional trade theories derived from static comparative advantages have not lost all validity, but are unable to explain Asian dynamism. Key words for understanding FDI flows in East Asia are *agglomeration* (or *clustering*) and *fragmentation*. Agglomeration refers to a geographical concentration of certain production activity where its density stimulates further concentration. The examples include Silicon Valley in California, Hsinchu Industrial Park in Taiwan, software concentration in Bangalore, India, and electronics and garment in Guangdong, China. By contrast, fragmentation is a situation where a product is manufactured not in one location but internationally with each country responsible for a particular *production block* in the manufacturing process. For fragmentation to be profitable, the benefit of international division of labor must outweigh the *service link cost* of transporting information and intermediate goods across countries.



These forces may seem contradictory since the one is centripetal and the other is centrifugal, but they really are not. For example, it is quite possible that a certain production process concentrates in one country, creating a network with similar concentrations in other countries engaged in different production processes. Moreover, since the service link cost is subject to economies of scale, agglomeration tends to form in the areas where the service link cost is low. Normally, the two forces operate simultaneously but the pattern of their interaction is highly complex. Its dynamics depends on the physical character of the product, business strategy of each firm, and policies adopted by various countries. Within the same industry, the pattern shifts over time. While even the producers themselves cannot predict its future course easily, we can recognize what kind of forces are at play and what kind of moves multinational corporations are making at the moment. Vietnam should learn such global trends and initiate FDI attraction drives in the products and industries that may come to Vietnam. By contrast, if Vietnam tries to invite FDI which has no chance of coming, time and money will be wasted. This means going with the market, not against, and taking full advantage of its flows. At present, Vietnam is not yet equipped with the information and skills necessary to win the tough global race for attracting FDI.

Attracting FDI does not necessarily require good *initial conditions*—raw materials, low wage, capital accumulation, technology, the size of domestic demand, etc.—which are difficult to change in the short run. In these days, *policy environment* is increasingly more important than initial conditions. It is also reported that foreign investors value good policy environment more than generous investment incentives. In East Asia, countries with very different economic size and factor endowment have exhibited a similar pattern of industrialization featuring trade and investment linkage, transition from textile to electronics production, and dependence on the markets of Japan, US and EU. What is crucial is not that Taiwan used to produce rice and sugar and Malaysia once exported tin and rubber, but the governments of these countries successfully introduced policies to absorb foreign capital and technology, even though with trial and error.

Not every country in East Asia has enjoyed robust growth. Some countries remain outside Asian dynamism. North Korea and Myanmar are economically and politically closed and have not reached the point where a development strategy can be meaningfully discussed. Landlocked Laos and Mongolia face difficulties in establishing trade and investment linkages. The Philippines has not sustained high growth due to political and social instability. Moreover, the case of Indonesia is especially suggestive. This country has absorbed significant amounts of FDI and ODA, made progress in industrialization, and even participated in Asian dynamism. At present, however, Indonesia seems to have (temporarily?) dropped out of the flying geese race with respect to FDI attraction. Policy inconsistency, as well as political instability, has much to do with this situation.

Turning our eyes to Vietnam, it is true that Vietnam has achieved high growth in the last decade, but it is not yet certain whether high growth will continue in the next decade and beyond. Vietnam's weaknesses in attracting investment are already widely known and, among them, the worst problems in comparison with other countries in the region are undoubtedly *unfavorable policy environment* and *lack of infrastructure*. As to infrastructure, its establishment will have to be gradual since it will take time and money. But as to the problem of policy environment, its improvement will not require a huge sum of money or a long period as it is a matter of ideas and discipline. On the other hand, good policies must come from the revamping of the existing policy mechanism, which may be difficult. At any rate, it is our view that unless Vietnam goes through this narrow gate, sound industrialization and modernization will not be attained.

At the minimum, Vietnam should quickly abolish the existing irrational regulations concerning permits, local contents, tariff structure and so on that are hindering the growth of domestic and foreign businesses. In addition, more pro-active policies should be introduced to attract the critical mass of FDI.

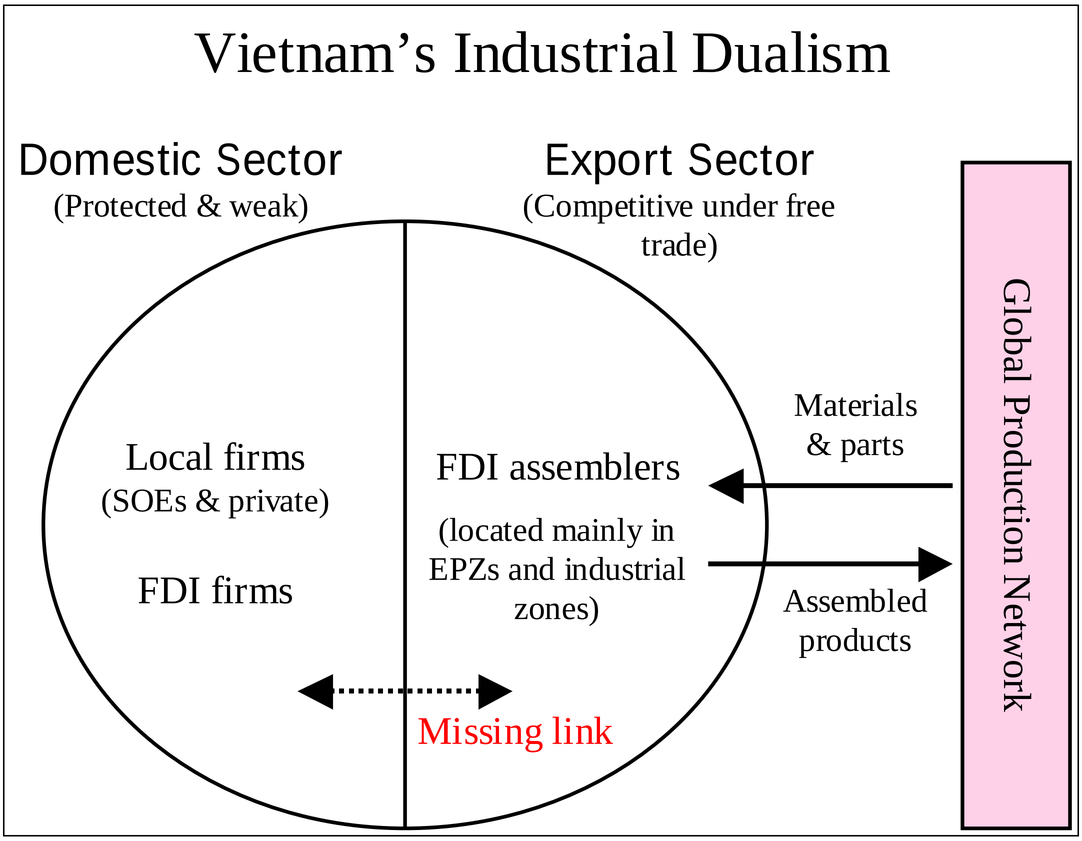
To become a part of Asian dynamism, free trade and a level playing field alone are not enough. A developing country must have information about individual key industries before it can design an industrialization strategy or identify the type of investment that can be attracted. With limited time, money and human resources, the government needs to decide which infrastructure and institution should be improved first, and how fast trade liberalization should proceed for each industry and product. Unless such information is available, the government cannot design the right policy mix, and will be forced to choose from permanent protection or big-bang liberalization. Under such circumstances, FDI cannot be invited and international integration shocks cannot be ameliorated. A country with underdeveloped markets needs to have detailed information on individual industries even if private enterprises are to take the lead in the growth process. The laissez-faire policy cannot and should not be adopted.

4. The role of domestic firms

Vietnam should aim principally at FDI-led industrialization, but domestic firms also have a very important and complementary role to play. They have the following two functions in the process of economic development.

First, domestic firms are a vehicle for spreading employment and income. Above all, the creativity of domestic firms themselves provides the source of growth. To ensure this, the government must continue to offer an open and transparent business environment, and bestow legitimacy and stability of enterprises by the formalization of the informal sector. Besides that, there is another important role. Apart from export earnings, Vietnam receives roughly USD 10 billion of foreign exchange every year (see above). Income and investment arising from these do not stay with the initial recipients. As they spend the income, additional domestic demand will be generated in the second, third, etc. rounds of derived spending. This so-called *multiplier effect* stimulates and is stimulated by the development of domestic firms. This is the mechanism by which the initial impact of foreign exchange receipt is spread to a broader segment of population.

Second, domestic firms are potentially the mother of supporting industries. A large amount of FDI will certainly industrialize Vietnam, but it is not yet industrialization by Vietnam's own ability if the key elements of production—management, technology, capital, marketing, product design, etc.—are totally dependent on foreigners. As noted above, strengthening domestic capability requires production linkage with FDI firms, especially by becoming suppliers of parts and intermediate inputs to them. The government should strongly support able and willing domestic firms to establish such inter-firm transactions (in addition to inviting parts suppliers from abroad). If successfully implemented, this policy will create a mechanism to transfer international production and management know-how to the domestic sector.



Interdependence between domestic and FDI firms should be promoted through these demand and supply channels. At present, cooperation between the domestic sector which is protected from foreign competition on the one hand (this includes foreign firms of the import-substitution type) and the export-oriented FDI sector which already participates in the international division of labor on the other is extremely weak. To overcome this difficulty, policies are needed to actively create and support the embryonic market economy, in addition to legal and institutional frameworks and a level playing field.

A large number of small private enterprises have emerged since the promulgation of the new enterprise law in 2000. Some say this reflects private dynamism in Vietnam and hope they will become the pillar of economic growth, overtaking SOEs and FDI. As noted above, we also welcome the sound growth of this sector with much expectation. But from the viewpoint of whether this sector can really become the principal actor in Vietnamese industrialization in the face of fierce competition from abroad, we cannot be overly optimistic. Expectation is important, but it must be a realistic one.

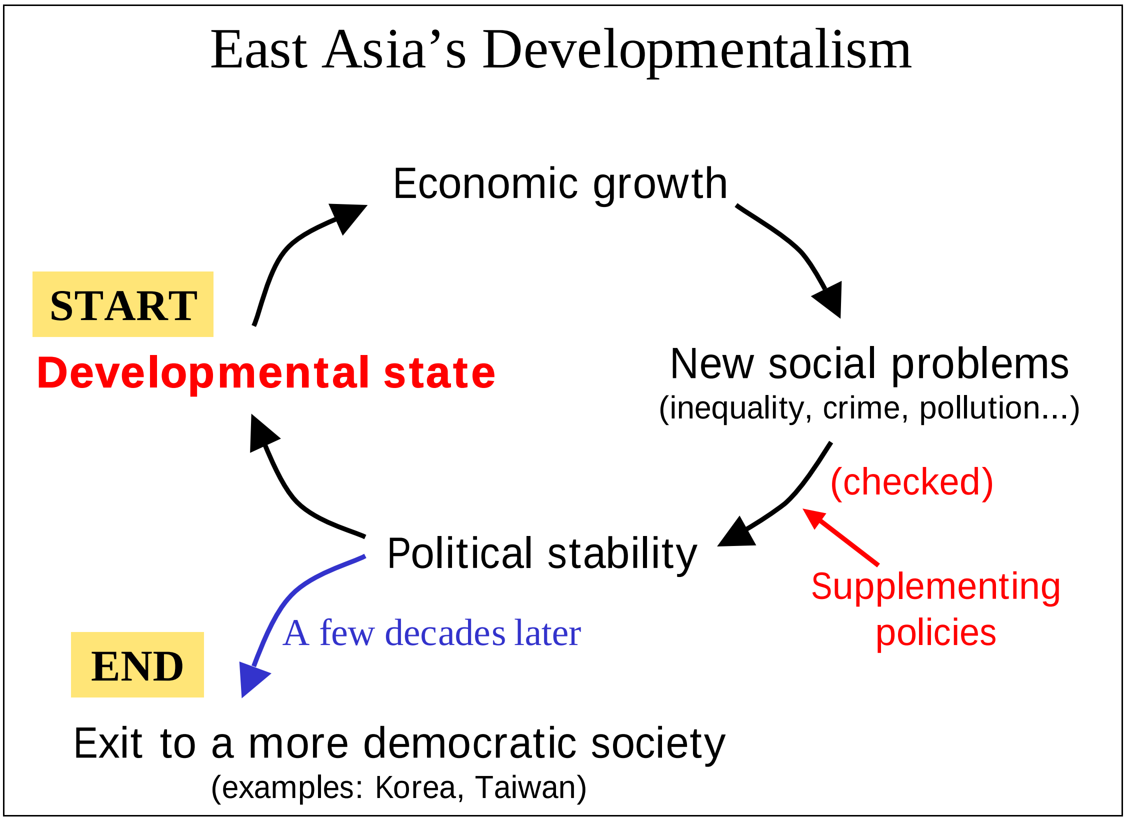
The private sector in Vietnam is dominated by small businesses such as street shops, family factories and simple services catering immediate neighborhood. Some of the "new" businesses are really the incorporation of previously informal enterprises. Some private firms have the potential to become competitive (Biti's, Trung Nguyen, etc.), but their number is too small. Private manufacturing firms with internationally competitive technology are even rarer.

As the list of the best Vietnamese companies includes not only private firms but also SOEs (Vinamilk, Hanosimex, Garco 10, etc.), it is clear that what is essential is not ownership form but whether or not the firm operates with entrepreneurial spirit in an open competitive environment. Prejudice such as "private firms are superior to SOEs" (or vice versa) should be abandoned. Domestic firms with the potential to cooperate effectively with FDI firms should be selected and strongly supported, regardless of ownership form.

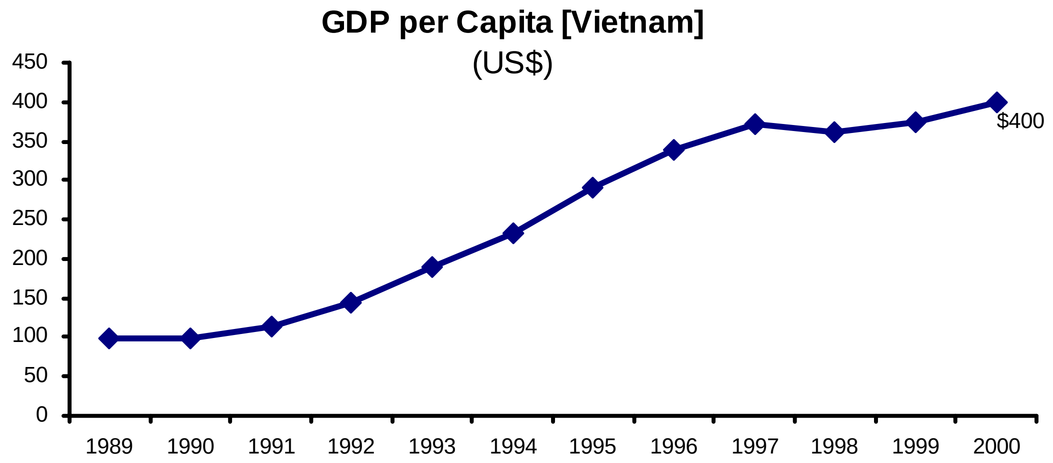
5. Economic growth and poverty reduction

Since around 1999, global development strategy led by the World Bank and the UNDP has elevated *poverty reduction* as the sole goal of development, with the contention that ODA must be used for that purpose only. The *Millennium Development Goals* (MDGs), or a number of poverty reduction targets such as halving the ratio of absolute poor between 1990 and 2015, were agreed. All low-income countries are now required to draft a *poverty reduction strategy paper* (PRSP) In Vietnam, PRSP is renamed the *comprehensive poverty reduction and growth strategy* (CPRGS) paper.

However, it is up to each developing country to decide whether or not poverty reduction should be the highest development goal. Even before MDGs and PRSP were invented, Vietnam introduced the multi-sector socialist economy as the model and prepared the five-year plan and the ten-year strategy as the ultimate guiding documents. Furthermore, Vietnam has long strived for industrialization in order to catch up with more developed countries, and simultaneously emphasized concern for social justice in that process. This concern addresses not only poverty reduction but also a much broader range of issues such as emerging gaps, ethnic minority, environment, crime, corruption, social discipline and cultural development. This growth strategy is also common to a large number of high-performing East Asian countries.



Generally speaking, Vietnam's social achievements are fairly good by the standards of developing countries with similar income, or even those of much higher income. Moreover, most social indicators improved during the 1990s, despite new problems generated by economic liberalization and international integration. In particular, Vietnam by now has already achieved the principal target of MDGs, namely, halving the ratio of absolute poor between 1990 and 2015. The population below the poverty line declined from 58 percent in 1993 to 32 percent in 2000. This remarkable social performance by international standards owes much to the combined policy of high growth and social justice mentioned above (however, this by no means implies that Vietnam's remaining social problems are insignificant). Social policies alone without growth would not have attained this result.



Sources: *Statistical Data of Vietnam Socio-Economy 1975-2000* (Statistical Publishing House,2000); ADB, *Key Indicators 2001* .
Note: Calculated from GDP, Population and Exchange Rate.

As of 2003, international organizations and European donors have come to the recognition that economic growth is essential for poverty reduction. However, the ideas that (i) growth must benefit the poor most; and (ii) growth assistance should be given to vulnerable groups, rural communities and remote areas rather than urban industries or large-scale infrastructure, are still strong. Whether limited resources should be concentrated in a few growth points (big cities in the North and the South in the case of Vietnam) or more widely distributed across poor regions is an old problem in development strategy. The important thing is to balance the two, not to choose the one or the other. The view that growth assistance must be directed exclusively to poor people and poor regions is too extreme. The two-tier policy of maximizing growth (even if its initial impact is uneven) and redistributing its fruits to general population is a viable option for poverty reduction, and it may even be more effective than directly targeting the poor.

There are three major channels for poverty reduction. The first is the pro-poor measures such as education, health, rural development and gender. Secondly, there is the market channel in which income generated by growth spreads via labor mobility, demand expansion and reinvestment. This phenomenon is sometimes called *trickle-down* with a negative connotation that it alone is not sufficient to eliminate the income gap. Nonetheless, it is a very powerful channel in many developing countries including those in East Asia, and its effect can hardly be ignored. Thirdly, there are a large number of policies for complementing the market channel and redistributing the fruits of growth, from the so-called *social safety net* to the proper design of investment and tariff policies. The current debate over pro-poor growth is often narrowly focused on only a small number of these channels. It is important to choose policies from the entire menu. And, in all cases, economic growth must first be secured as a precondition.

Three Channels of Pro-poor Growth
(1) Direct channel (impacting the poor directly)
Health, education, gender, rural jobs and development, etc.
(2) Market channel (growth helps the poor via economic links)
Inter-sectoral and inter-regional labor migration
Increasing demand (cf. proto-industrialization, multiplier effect)
Reinvestment (through formal, informal and internal finance)
(3) Policy channel (supplementing the market channel)
Price support, taxes and subsidies
Fiscal transfer, public investment, infrastructure
Micro and SME credit and other financial measures
Proper design of trade and investment policies
Pro-poor legal framework

6. Summary of policy recommendations

Our policy advice is summarized below. For details, please see the respective subpages.

(1) *Attracting a large amount of export-oriented FDI*

While export-oriented FDI has already come to Vietnam, its size has so far been very small compared with the accumulation in Southern China, Thailand or Malaysia. For Vietnam to deeply engage in the regional production network, far greater FDI than at present must be absorbed. Foreign investors are attracted to the *business environment for low cost* and the *formation of agglomeration*, but since the latter is the outcome of successful FDI absorption, the initial effort must be directed to improving the business environment. There are many factors affecting the cost of investment, including:

--quality/price of factors of production and intermediate products
--quality/price of infrastructure services including electricity and roads
--distribution, transportation and telecommunication
--taxes, subsidies and tariff structure
--Liberalization of production, trade and investment
--administrative efficiency

and so on. Vietnam should rapidly improve on all these fronts, with due attention to details and overall consistency, in order to become the best business location in the world. In building these conditions, (i) regular dialogue with enterprises to understand their requirements; (2) guarantee of policy stability and transparency; and (3) the display of strong policy commitment and active PR, are necessary as crosscutting measures. Furthermore, establishing and strengthening an organization for rapidly solving trade- and investment-related claims, such as Japan's Office of Trade and Investment Ombudsman (OTO), should be considered.

(2) Selection and enhancement of import-substitution industries

Policy for import-substitution industries (which sell domestically) is more difficult than that for export-oriented industries and calls for more information and delicate measures. This applies to both local and FDI firms of import-substitution type. These firms face the double problem of a small domestic market on the demand side and the lack of supporting industries on the supply side, both contributing to high cost and weak competitiveness. While they are currently protected from foreign competition, protection will be removed as AFTA implementation and WTO accession proceed, threatening their survival. To cope with rising competitive pressure, the combined strategy of *selection* and *enhancement* is advisable, where some firms exit and those who can improve productivity survive (instead of trying to keep all of them). The ultimate fate of each industry will be decided by the market and entrepreneurial effort, but the government has roles to play in that process, including (i) designing an appropriate tariff reduction schedule for each industry to encourage bad firms to leave and good firms to become efficient; (ii) pre-announcing this schedule and adhering to it even under political pressure; and (iii) temporarily supporting firms with realistic plans and without breaching external trade commitments. However, such conditional protection entails substantial risk if it is carried out without sound information and analysis. If that happens, selection and enhancement will not succeed and the national economy may incur a large and unnecessary cost.

(3) Intensive policy for attracting and fostering supporting industries

Vietnam constantly drafts and revises a large number of policies for localization and related incentive and penalty measures for the purpose of creating supporting industries. However, the complexity and distortion that these measures generate ironically serve as hindrance to production and investment for both domestic and foreign firms. Support for parts industries must be done in a realistic—not forced—way. Instead of penalizing firms with low localization, the government should offer a free and low-cost business environment for all firms, and additionally assist firms with high contribution. More concretely, the following are recommended:

--Selection of a small number of SOEs as candidates for parts suppliers, and concentrating financial and technical assistance on them.

--Preferential finance, tax, tariff and technology measures for domestic private firms trying to produce parts.

--Designating 3 to 4 existing industrial parks as “parts industrial parks” and drastically improving their business environment.

--A special award system for firms that export parts or sell parts to exporting firms (however, this must be a temporary measure as export subsidies are prohibited under WTO).

The Vietnamese government should take the lead in constructing a comprehensive policy package containing all these, and request interested donors (including Japan) to provide necessary assistance. Available external assistance should be able to cover industrial studies, SME promotion, design of trade liberalization, enterprise check-up by foreign experts and senior volunteers, reform of economic policy making, and PR and marketing for FDI attraction.

(4) Importance of dialogue in the policy making process

In Vietnam’s policy process, there is no effective mechanism to collect detailed and up-to-date information on domestic industries and global markets which is vital for industrial promotion and FDI attraction. Under globalization, the vicissitudes of firms and industries are determined by international competitiveness—price, quality, speed, service, product design, etc.—and not by a list of inward-oriented quantitative targets of production and investment. While international competitiveness is hard to attain immediately, as the first step we propose institutionalizing regular dialogue between policy makers and domestic and foreign firms for policy formulation. At present, policies drafted by a few officials at concerned ministries are circulated among other ministries for comment. This process lacks inputs from the business community and is without necessary information and analysis. When an inconsistent policy generates a big problem, it is handled belatedly by the decisions of the prime minister or the deputy prime minister. This process is ad hoc and without long-term vision. Vietnam needs a system to regularly survey the needs and impediments of domestic and foreign firms, share this information with all stakeholders, and use it for policy formulation. Monthly meetings for individual industries are useful, but they should be complemented by additional, informal contacts (but keep some distance between government and businesses lest cooperation might degenerate into collusion). Annual dialogue between government leaders and foreign investors is not enough, nor is a letter to the prime minister after an unfavorable event has occurred.

(5) The special team under the prime minister for directing economic policies

Vietnam's decision making takes place in a complicated web of vertical and horizontal authorities. Responsibility is diffused and the process is not transparent. Policies lack clarity and consistency, and response is slow when speed is needed. Industrial strategy (MOI), FDI and ODA (MPI), trade negotiations (MOT), tariff structure (MOF) and technical standards (MOSTE) are dealt with by different ministries without coordination in substance. Even within the same ministry, departments do not talk to each other. Under these circumstances, it is impossible to introduce policies for individual industries and products in an economically meaningful manner. At the minimum, MOI and MOT should be merged. For a more fundamental solution, we propose the establishment of a small group of highly capable professionals. With full confidence and support of the prime minister, this group should be given the authority for economic policy making and supervision of all economic ministries and organizations. Such top-down decision-making has been adopted by many East Asian countries for a few decades in order to sustain an economic catching up. It should also work well for a latecomer country like Vietnam which just started the process of high growth. Under severely limited human and nonhuman resources, agility and flexibility in policy making can be realized by concentrating authority in this small group (needless to say, concentration of economic policy authority is a different matter from the question of how to distribute political authority).