Investment of rice mills in Vietnam

Le, K.N.

Chapter 2

Economic reforms in Vietnam

2.1 Introduction

This chapter is devoted to giving an overview of the reforms in the economic system in Vietnam since 1976, the year of reunification. Since the second half of the 1980s, the reforms have amounted to achieving a transition process from the centrally-planned economy, which Vietnam pursued before that date, to a market economy. This chapter concentrates on the aspects of the transition process that are important in view of the central theme of this dissertation, to wit the problem of Vietnamese private rice millers in financing their investments in an uncertain environment.

This chapter starts with a sketch of the transition process in general (Section 2.2); this section also discusses the reforms of state-owned enterprises as well as the development of private enterprises in Vietnam. Section 2.3 examines the agricultural reforms that have unleashed this sector's potential and have lead to a substantial increase in the supply of rice, especially in the MRD. Section 2.4 covers the international-trade aspect of the reform process, which is important in the context of this dissertation, because trade policy shapes the link between international markets and domestic markets. In the case of rice, this means, *e.g.*, that increasing openness to the international rice market may lead to fluctuations in domestic rice prices, which account for part of the uncertainty facing private rice millers. Section 2.5 concludes this chapter.

2.2 An overview of the economic transition in Vietnam

2.2.1 *Economic reforms in Vietnam in general*

In 1976 the Vietnamese government started imposing central planning upon the South with the launching of the 1976-1980 Five-Year Plan; the North adopted central planning in the 1950s after defeating the French. Fforde and De Vylder (1996) characterized the economic system of this period as the DRV model, where DRV stands for Democratic Republic of Vietnam, the official name of North Vietnam from 1945 to 1976. The basis of the DRV model is Soviet-style central planning focussing on heavy industry and collectivisation of agriculture, wherein state organs play a leading role in the economy through physical output targeting, allocating resources to production units, and taking care of the distribution of products to consumers and other production units. The DRV model was, however, not a complete copy of the Soviet model because the Soviet model is based on a strong state, whereas the state in Vietnam in this period appeared to be a weak one (Fforde and De Vylder, 1996). Amendments of the Soviet-type economic system became necessary already in the 1960s in the North due to increasing sectoral imbalances and growing divergences between official prices and prices in free markets (dual pricing system).[3]

The DRV model came under serious strain in the late 1970s when the political and economic isolation of Vietnam in the period of the military intervention in Cambodia and bad harvests because of bad weather added to the longer-standing problems in the functioning of the model. The state organs were no longer capable of supplying inputs to the economy and food to the people. In the 1978-1979 period, this situation led to the start of a process of “reform from below” (Fforde and De Vylder, 1996; Webster and Taussig, 1999),[4] which means that individuals, agricultural cooperatives, and SOEs were developing alternative ways of getting access to resources; this was tacitly allowed by the authorities. The failure of the authorities to effectively manage the centralised economic system showed up in considerable differences between official prices and prices in free markets that stimulated fence-breaking activities.

After the crisis of the late 1970s, the government broke off economic liberalisation and at the same time attempted to re-centralise economic management. Fforde and De Vylder (1996) used the expression “hard reform socialism” to characterize this episode. The approach of this period was well exemplified by the Three-Plan System governing the state-owned industry (Decree 25 CP), which was

[3] In those free markets, prices were basically determined by supply and demand (Gates, 2000).

[4] The reform-from-below process is also referred to as fence-breaking (*pha rao*).

launched in January 1981. Under this plan, a state-owned factory had to have a single plan with three elements. The most important element, called "Plan A", refers to the production using the inputs provided by the state, the output of which had to be supplied to the state; this type of production was supposed to have absolute priority over any other element. The other two elements, "Plan B" (free disposal of products that the factory was established to produce) and "Plan C" (production of minor products that resulted from the factory's own attempts at diversification), were also legalised (Fforde and De Vylder, 1996).

The hard-reform-socialism approach was not able to save the system of central planning. The structural tensions of the DRV model in the form of divergences between official and free-market prices resurged, taking extreme proportions in the 1986 hyperinflation (Fforde and De Vylder, 1996; Le, 1996). Another cause of the hyperinflation was the policy package of September 1985, through which the authorities increased official prices and wages and introduced a new *dong*.[5] The main adverse impact of this policy package fell upon SOEs as their cash holdings were wiped out because of higher input prices and labour costs. The indispensable subsidies to SOEs from the state budget lead to a substantial state budget deficit that could only be financed by printing money, which strongly contributes to the pre-existing inflationary tendencies.

Attempts to overcome the serious inflationary and budgetary problems and the underlying structural weaknesses caused the Sixth Party Congress of the Communist Party of Vietnam (December 1986) to abandon the hard-reform-socialism approach in favour of a policy package aimed at establishing a market economy. This policy package is often referred to as economic reform (*doi moi*). *Doi moi*, which dismantled central planning, liberalised trade, promoted private activities, *etc*., was meant to generate incentives for people to work harder and more efficiently (Che *et al*., 2002).

The December 1986 measures were followed by other measures aimed at establishing a market economy. Among other things, in 1987 the inter-provincial trade barriers were abolished. In the same year, Law on Foreign Direct Investment (FDI), intending to attract FDI, was passed. All in all, during 1987-1988 the central controls over FDI, land, foreign trade, banking, SOEs, private and household enterprises, and the agricultural sector started to ease. Notwithstanding the measures taken, the dual pricing system remained.

In March 1989, the government intensified *doi moi* with the launching of comprehensive reforms that marked the most decisive step towards addressing the structural economic problems. The reforms dismantled the agricultural cooperatives

[5] *Dong* is the currency of Vietnam. The new *dong* replaced the previous *dong* on a one-to-ten basis (McCarty, 2001).

and returned land to farming households. Commodity prices were liberalised by abolishing the state prices for most consumer goods, thus terminating the dual pricing system. Private enterprises were given more room to operate. Investment and trade regimes were liberalised, contributing to a rapid increase in rice exports (see Table 2.5). Real interest rates were brought to positive levels. Credit ceilings were imposed on SOEs. The multiple exchange rate system was unified in combination with a devaluation of the *dong*.[6] The reforms also aimed to reduce budget deficits by restraining expenditures, reducing subsidies to SOEs, and restructuring the tax system (IMF, 1998; McCarty, 2001). The reforms revived the economy: inflation dropped considerably, and GDP grew by around 8 per cent in 1989 (see Table 2.1).

Table 2.1 Vietnam: some economic indicators, 1985-2000

Year	*Annual GDP growth rate (per cent)*	*Annual consumer price inflation rate*
1985	3.8	*na*
1986	2.8	487.0
1987	3.6	317.0
1988	5.1	311.0
1989	8.0	35.0
1990	4.5	67.0
1991	6.1	68.0
1992	8.6	18.0
1993	8.1	5.0
1994	8.8	14.4
1995	9.5	17.1
1996	9.3	5.7
1997	8.8	3.2
1998	5.8	7.3
1999	4.8	4.1
2000	6.8	-1.7

Source: Fforde and De Vylder (1996); Gates (2000); Statistical Year Book 2000; Vietnam Economic Review No. 9, 2000; IMF (1998); IMF (2000); IFPRI (1996); Che *et al*. (2002); IMF (2002b).
Note: *na*: not available.

In a longer-term perspective, the reform measures of the 1986-1989 period, together with the country's strategic location in the midst of the fastest growing re-

[6] At that time, the *dong* was devalued by 97 per cent, to USD1 = VND3,971. Since 1989 the official exchange rate has followed closely the movements of the parallel market with a small premium on the official rate. Since 1994 the official and parallel market rates have been almost equal (Gates, 2000).

gion of the world, led Vietnam to rapid economic growth, especially between 1992 and 1997 (Table 2.1). Vietnam's growth performance in this period was remarkable in that, different from may other transition economies, there was no recessionary "J-curve effect" accompanying the transition (Fforde and De Vylder, 1996).

It is not easy to situate Vietnam's transition policies in terms of the usual distinction between a Big Bang and a gradualist approach. Gates (2000) argues that the approach was different in different stages: the 1987-1988 period can be characterized as gradualism, followed by the 1989-1991 period of bold Big-Bang-like reforms; afterwards, the 1992-1994 period is considered to contain "tinkering" reforms.

Since 1998 Vietnam's economic growth has slowed-down (Table 2.1). This might be due to the Asian economic crisis of 1997/1998, through the channels of FDI and exports. In 1997 FDI in Vietnam diminished dramatically: total new FDI of USD 4.5 billion in 1997 was about half of the record of USD 8.6 billion in 1996 (Riedel, 1999).[7] Exports faltered; the fall in exports was attributable to the collapse of regional markets, which accounted for some two-thirds of Vietnam's total exports, and to large devaluations of the currencies of the countries hit by the crisis. The slowing-down of the economy was also a consequence of structural weaknesses: the economy still largely relies on inefficient state-owned commercial banks and SOEs while competitive private enterprises are nearly absent (IMF Survey, January 28th, 2002). Table 2.2 gives an overview of the shares of the state-owned and non-state sectors in Vietnam's GDP. This table reveals that the share of the state-owned sector in Vietnam's GDP did not decline;[8] this is in contrast to the experiences of most other transition economies (IMF, 1998). According to Table 2.2, the non-state sector has accounted for a relatively substantial share of Vietnam's GDP. If the shares of farming households and foreign firms in Vietnam were subtracted from the share of the non-state sector in Vietnam's GDP, it would be revealed that domestic private enterprises alone have made up a much smaller share of Vietnam's GDP. This means that domestic private enterprises have played an unimportant role in Vietnam's economy. The reform of state-owned enterprises and the development of private enterprises in Vietnam are to be analysed in the subsequent subsections, which will help to explain the above-mentioned observations.

7 Since two-thirds of the FDI in the 1991-1998 period was directed to joint ventures between foreign investors and SOEs, the fall of FDI has deteriorated the financial condition of the latter, thereby adversely affecting their capability to repay their debts to banks, mainly state-owned commercial banks (O'Connor, 2000).

8 The reasons for this fact will be discussed in Subsection 2.2.2 below.

Table 2.2 Vietnam: shares of the state-owned and non-state sectors in GDP, 1989-2000

Year	*State-owned sector* (*per cent*)	*Non-state sector* (*per cent*)
1989	33.2	66.8
1990	32.3	67.7
1991	33.2	66.8
1992	34.3	65.7
1993	35.4	64.6
1994	36.7	63.3
1995	40.2	59.8
1996	39.9	60.1
1997	40.5	59.5
1998	40.0	60.0
1999	38.7	63.1
2000	39.0	61.0

Source: Computed from Dodsworth *et al*. (1996) for 1989-1994 (at 1989 constant prices) and from IMF (2002b) for 1995-2000 (at current prices).

2.2.2 *State-owned enterprises* (*SOEs*) *in Vietnam*

Since 1986 Vietnam has taken several measures to reform SOEs. The most decisive reforms of SOEs took place during the 1988-1992 period.[9] An important outcome of these reforms is that the number of SOEs was reduced from 12,000 in 1988 to 6,000 in 1992 after being merged and/or consolidated. Another outcome is the improvements in their financial performance. For instance, net transfers from SOEs to the budget increased from zero in 1988 to 12 per cent of GDP in 1994; net credit flows from commercial banks to SOEs fell from 9 per cent of GDP in 1998 to about 2 per cent in 1993-1994 (IMF, 1995; IMF, 1998). Since 1994 the reform progress has been delayed because the government has remained in favour of a leading role for SOEs (IMF, 1998; IMF, 2002a), as it ideologically sustains a socialist-oriented mixed economy operated on market principles. This contributes to explaining why the share of the state-owned sector in Vietnam's GDP has increased (Table 2.2). A substantial part of the increase in the share of the state-owned sector in GDP reflects the government policy of encouraging foreign investors to form joint ventures with SOEs (IMF, 1998; IMF, 2002b). According to O'Connor (2000), two-thirds of the FDI in the 1991-1998 period was directed (by the government) into joint ventures with SOEs.

[9] These reforms are discussed in several studies on Vietnam, see, *e.g.*, IMF (1998), Dodsworth *et al*. (1996).

In Vietnam SOEs are still at an advantage as compared to private enterprises in terms of access to credit, land use rights, trade protection, *etc*. Despite these advantages, since the end-1997 their performance has deteriorated: inventories have built up due to the plunge in domestic as well as in foreign demand; their contributions to the state budget have decreased; overdue loans to the banking system have risen to a very high level because the banking system has continued to finance their production (IMF, 1998; IMF, 1999), but around one-half of the number of SOEs were only loss-making or marginally profitable (IMF, 2001).

Aiming to tackle the poor financial conditions and the inefficiency of SOEs, the government took on a five-year SOE reform plan in March 2001 (IMF, 2002a). According to this plan, 1,800 out of more than 5,500 SOEs will be subject to enterprise-specific reform measures, mostly through equitisation (1,440), divestiture (140), or liquidation/closure (220). An additional 200 SOEs will be merged or consolidated. This reform plan still continues but at a slow pace.

2.2.3 *Private enterprises in Vietnam*

After the reunification of the country in 1976, the government started nationalisation or collectivisation of all relatively big private companies in the South. A limited number of smaller companies were not brought under full influence of the government but instead re-categorised as state-private joint ventures,[10] in which state organs played a dominant role (Webster and Taussig, 1999). Prior to *doi moi*, the informal private sector was disallowed and unrecorded (IMF, 2002b). Yet, Freeman (1996) maintains that the informal private sector operating outside the government's control sustained Vietnam during the difficult years between 1976 and 1986. The start of *doi moi* signalled the government's fiat of private economic activities, thus stimulating the expansion of the private sector.

In 1988 the government officially recognised the long-term importance of the private sector and guaranteed its existence as part of a multi-component economy. In 1990 the Enterprise Law was promulgated, providing a legal infrastructure for the private sector. In 1992 the new Constitution reaffirmed the legality of the private sector's standing in the multi-component economy (Webster and Taussig, 1999). Subsequently, the number of private enterprises increased substantially. For instance, the number of private enterprises grew by 60 per cent in 1994 and 41 per cent in 1995 (Webster and Taussig, 1999). Despite this, private enterprises in Vietnam are still obstructed by constraints in terms of access to market, access to bank credit, among other things (IMF, 2002b), which may have held back its growth. In

[10] These joint ventures were called "*xi nghiep cong tu hop doanh*."

1998 the number of private enterprises increased by only 4 per cent (Nguyen, H.D., 2000).

In response to the economic downturn since 1997, the government issued a new Enterprise Law on January 1st, 2000. This new law is aimed at easing business entry for private enterprises by lifting the business licensing requirements, therefore making the establishment of private enterprises considerably easier (IMF, 2002b); business registration costs was cut significantly; the approval process was shortened from 1-2 months to 10 days. As a result, around 26,000 small- and medium-sized enterprises (SMEs) were registered in the period from January 2000 to August 2001 (IMF, 2002b).

2.3 The agricultural economic reforms

2.3.1 *The collective regime* (1976-1980)

During the 1976-1980 period, the Vietnamese government pursued a collective regime. Under this regime, agricultural production took place in compulsory cooperatives that were supposed to control 95 per cent of agricultural land. All production and distribution decisions were made by the state. After harvest the state took out a portion of the output as a lump-sum tax; the surplus over own consumption was forcefully sold to the state at a low price, around 20-30 per cent of that in free markets. The distribution of the output of agricultural cooperatives was based on work points.[11] Private trade in agricultural products was officially banned. Farming households could only use the remaining 5 per cent of land for the breeding of pigs and chickens and for vegetable production; private trade in these products was allowed but restricted to local markets.

During the collective regime, rice production was marked with stagnation, especially in 1977 and 1978 (see Table 2.3). Although the year of 1979 witnessed a recovery of rice production, rice production in this year did not reach the 1976 level. This situation forced Vietnam to import a large amount of rice so as to meet the domestic demand (Che *et al*., 2002). Since the collective regime was seen as unworkable, farmers in the South, especially those in the MRD, resisted collectivisation (Webster and Taussig, 1999). Therefore, by the end of the 1970s the MRD

[11] The work-point system works as follows. A working day that a member of a cooperative spent working for the cooperative is counted as one work point. At the end of a certain period the work points of all members are added up. Total production will be divided by the total number of work points to compute the average value of one work point. Each member will receive an amount of output equal to the number of work points he/she has received multiplied by the average value of one work point.

remained largely uncollectivised (McCarty, 2001). In 1978 only 0.2 per cent of farming households in the MRD joined cooperatives; this figure increased to 1.8 per cent in 1979 (Tran, 1998). These figures mean that the collective regime then failed, particularly in the MRD, because few real agricultural cooperatives were established during this period.

The inadequate functioning of the collective regime made reforms in the agricultural sector indispensable. According to Che *et al*. (2002), the agricultural economic reforms in Vietnam have passed through two main stages: (i) the output-contracting regime (1981-1987) and (ii) market liberalisation (1988-present), with the latter being more effective than the former in terms of boosting agricultural growth.

Table 2.3 Vietnam: rice production, 1976-2000

Year	*Amount* (1,000 *tons*)	*Annual growth rate* (*per cent*)	*Year*	*Amount* (1,000 *tons*)	*Annual growth rate* (*per cent*)
1976	11,827	*na*	1989	18,996	11.7
1977	10,597	-10.4	1990	19,225	1.2
1978	9,789	-7.6	1991	19,622	2.1
1979	11,363	16.1	1992	21,590	10.0
1980	11,647	2.5	1993	22,837	5.8
1981	12,415	6.6	1994	23,528	3.0
1982	14,390	15.9	1995	24,964	6.1
1983	14,743	2.5	1996	26,379	5.7
1984	15,506	5.2	1997	27,533	4.4
1985	15,875	2.4	1998	29,146	5.9
1986	16,003	0.8	1999	31,394	7.7
1987	15,103	-5.6	2000	32,554	4.0
1988	17,000	12.6			

Source: Nguyen (1996); Che *et al*. (2002).
Note: na: not available.

2.3.2 *The output-contracting regime* (1981-1987)

In order to improve the poor performance of the collective regime in the previous period, the government introduced the output-contracting regime with the issuing of Directive 100 CT/TW in January 1981. Under this regime, land was allocated to farming households, which were supposed to organise sowing, seedling, transplanting, maintenance, and harvesting; remaining operations (such as processing and distributing) were still carried out by cooperatives. A quota on output was set for farming households. They were allowed to retain the amount that exceeded the quota and could sell it either to the state or in free markets (Nguyen, 1996; Che *et* *al*., 2002).

Directive 100 CT/TW was a success although it gave farming households only a limited control over the production and the distribution of rice. During the 1981-1986 period, rice production increased remarkably by 28.9 per cent, from 12.4 million tons to 16 million tons (see Table 2.3). For the first time, food production grew faster than population, leading to an increase in average food production per capita from 273 kilogram in 1981 to 304 in 1985 (IFPRI, 1996). The achievements obtained between 1981 and 1986, however, were not sustained. Production stagnated, eventually precipitating the food crisis in 1987 when bad weather came (Fforde and De Vylder, 1996).

2.3.3 *Market liberalisation* (1988 - *present*)

Further economic reforms to overcome the stagnation of food production in 1987 were needed. This led to the market liberalisation starting with Resolution 10, which became effective in 1988. This resolution is the first tentative move towards private property rights. It defined farming households as autonomous economic units and allowed them to own machines, buffaloes, oxen, and agricultural instruments. In addition, farming households were entitled to purchase, sell, and transfer means of production. Collectivised land was returned to farming households for a long-term use, ranging from 15 to 50 years depending on the type of crops grown. Farming households were also allowed to keep 40 per cent of the contracted output, which could then be sold in free markets. The fact that Resolution 10 brought most aspects of the management of production to individual farming households and provided them with incentives to work harder is likely to be an important factor behind the substantial increase in rice production in 1988 and 1989 (Table 2.3). Pingali and Xuan (1992) argue that the incentives of farming households contributed largely to the increase in the average paddy yield.[12]

Although successes were achieved, problems remained. The rice market was still controlled by the government. The fragmentation of land into small plots, particularly in the North, caused difficulties in mechanisation, irrigation, specialisation, and product procurement. Rural unemployment was high. Rural industry remained poor, failing to absorb redundant rural labour. Agro-product processing capacity fell behind agricultural production. Poor rural infrastructure jeopardised the sustainability of the reforms. The rural economic structure was still biased towards rice and food (IFPRI, 1996).

[12] More generally, Nghiem and Coelli (2002) emphasize that the incentives of managers and workers in farms and factors have had a great impact on the economic performance of Vietnam during the *doi-moi* period.

Because of the shortcomings of the previous reforms, Resolution 5-HNTW was set forth in 1993. This resolution reaffirmed the autonomous role of farming households and entrusted them with the right of long-term land use. It also accepted the rights to exchange, transfer, lease, inherit, and mortgage land; this encouraged investment in land reclamation, replenishment, and improvement so as to multiply seasonal crops. Resolution 5-HNTW also focussed on the issue of rural development, including rural industry. The private sector was encouraged alongside renovating SOEs. As a result of Resolution 5-HNTW, rice production soared (see Table 2.3); this trend has sustained. In 2000 rice production was more than double that in 1986, the year when *doi moi* was initiated. Nowadays, farming households operate in free markets.

In sum, the economic reforms in the agricultural sector have given farming households more autonomy and proper incentives, thereby encouraging them to work harder and to invest in their land and crops. This has resulted in an enormous increase in rice production, which has secured the food need of the Vietnamese and contributed largely to rice exports of the country.

2.4 External trade liberalisation and developments in exports

In this section, attention will first be paid to the developments in the foreign-trade regime of Vietnam in general and in Vietnamese exports in particular. Afterwards, this section will concentrate on the changes in the trade regime regarding the rice sector and the developments in rice exports. Concerning the international trade aspect, developments on the export side, especially in the rice sector, are the factor of interest in the context of this dissertation. This explains why little explicit attention will be paid to the effects of the trade reforms on Vietnamese imports.

2.4.1 *External trade liberalisation in general and developments in exports*

The DRV model of central planning stressed autarchic growth and ignored the export sector (Fforde and De Vylder, 1996), meaning that opportunities for international trade on the basis of Vietnam's comparative advantage were not exploited. In 1978 Vietnam opened up the economy to its partners of the trade grouping of communist countries, the Council of Mutual Economic Assistance (CMEA), of which Vietnam was a member.[13] In the mid-1980s, CMEA-partners accounted for some 80 per cent of Vietnam's foreign trade, with the Soviet Union being by far the most

[13] For an insight into the functioning of the CMEA see, *e.g.*, Csaba (1986), Lanjouw (1995).

most important trade partner within this group.[14] The collapse of the CMEA created an extreme difficulty for Vietnam's foreign trade, which was already weak, and hence forced Vietnam to find other trading partners.

Liberalisation of international trade became part of the transition process in Vietnam. Apart from opening-up export markets, trade liberalisation contributes to creating a market economy by allowing competitive forces coming from abroad. At the same time, the internal price structure in the country will become aligned with the price structure in the international market (Williamson, 1991). To achieve this, first of all it is necessary to abolish quantitative restrictions (QRs) on imports, which cut the link between international and domestic prices. Trade liberalisation therefore should start with a first phase of elimination of QRs and replacement them with import tariffs. In the second phase, tariffs should then be reduced (Williamson, 1991). Vietnam introduced import tariffs, along with export taxes, in 1987 (IMF, 2002a). The government has, however, been slow in eliminating QRs on imports. More generally, among transition economies, liberalising international trade in Vietnam has been sluggish, especially on the import side. During much of the 1990s, there still was a rather high degree of trade restrictiveness (IMF, 2002a). In fact, Vietnam has followed a policy of import substitution aimed at protecting inefficient, loss-making SOEs (Gates, 2000).

On the export side, the pre-reform institutional arrangement was the trade monopoly of the state that was applied in the DRV-model. Exports were based on annual plans. A problem of this centralised arrangement was the lack of proper incentives. Gradually, incentives to stimulate exports were brought into the trade regime. In 1980 an export bonus system was introduced. By fulfilling export targets, exporters earned bonuses of 2 to 3 per cent of the value of exports; higher bonuses were possible in case exports exceeded targets. Direct contacts between domestic producing units and foreign clients became possible in some cases (IMF, 1981). Shortly afterwards, the latter reforms were reversed, however, in the framework of the hard-reform-socialism approach (Fforde and De Vylder, 1996), which was discussed earlier in this chapter.

After a period during which phases of decentralisation and re-centralisation took turns, major reforms in the export regime came in when *doi moi* was launched in 1986. In December 1987 a new system of trade taxation was introduced, bringing market-oriented elements into trade policy. The maximum export-tax rate was 10 per cent (IMF, 1988). In June 1989 the export regime was changed in that exporters were allowed to select any export-import company for their business activities and were no longer tied to a specific company under the annual planning sys-

[14] For a better understanding of the role of the Soviet Union in this trade grouping, see, *e.g.*, Dietz (1986).

tem. Certain producers were allowed to obtain foreign trading rights and to engage in direct business contacts with foreign companies (IMF, 1990). Like in the case of QRs on imports, Vietnam has also been rather slow in abolishing QRs on exports in the form of export quotas. For instance, the export quota on rice lasted until 2001 before it was terminated (IMF, 2002a).

The international-trade reforms seem to have contributed to the rapid growth of exports in the 1993-1997 period, with the average annual growth rate being more than 30 per cent over this period (see Table 2.4).

The Asian financial crisis erupting in 1997 caused a decline of prices of Vietnam's export commodities because of the declining demand from the crisis-hit countries. At the same time, Vietnam's exports lost competitiveness as the *dong* appreciated in real effective terms. As a result, export growth plummeted: in 1998 exports grew at only 2.4 per cent (see Table 2.4).

The reform of international trade in Vietnam got a new momentum with the issuing of Decree 57 in July 1998. This decree effectively extended the right to export unrestricted goods to all domestic enterprises (IMF, 2000a), thus infringing the international trade monopoly of a small number of SOEs. In 1999-2000 exports rebounded (Table 2.4), as the Asian region began to recover from the crisis and as exports to the European Union grew fast; in 1999 non-oil exports to the European Union grew by 24.8 per cent, accounting for as much as 48.5 per cent of the total increase in non-oil exports (World Bank, 2000b).

In April 2001, with a view of providing a more stable export-import environment, the government announced the five-year (2001-2005) import-export regime. This regime was contrary to those applied in the previous years, when only annual changes of the import-export regime were announced (IMF, 2002a). The new approach provided a scheme for eliminating quantitative restrictions, tariff reductions, and other trade measures.

Table 2.4 Vietnam: export revenue and growth, 1993-2000

	1993-1997 *average*	1998	1999-2000 *average*
Annual export revenue (USD million)	5,744	9,365	12,995
Annual growth (per cent)	30.1	2.4	24.2

Source: IMF, 2002a (Table IV.2).

In October 2001, the United States passed legislation implementing the milestone bilateral trade agreement with Vietnam, which has eased the access of Vietnam's products to this huge market and marked an important step for Vietnam towards WTO accession. In the meantime, preparations have been made to reach bilateral trade agreements with other WTO members, to align existing bilateral agreements and modify Vietnam's laws so as to meet WTO standards.

Developments in Vietnam's foreign trade will also increasingly undergo the influence of its membership of AFTA, which started in 1996.[15] Under AFTA, tariffs on 97 per cent of tariff lines will be reduced to at most 20 per cent by 2003 and 0-5 per cent by 2006 (IMF, 2002a). In turn, Vietnam will benefit from the tariff reductions of its AFTA partners.

2.4.2 *The trade regime in the rice sector and developments in rice exports*

After a number of years being a net importer of food, Vietnam exported around 1.4 million tons of rice in 1989 and has since then remained one of the leading rice exporters. This remarkable turnaround is largely attributable to the reforms that took place in the agricultural sector (see Subsection 2.3) and the opening-up to international trade as well (See Subsection 2.4.1.).

Despite the liberalisation measures related to rice exports, Vietnam's trade policy *vis-à-vis* processed rice remained negative in the sense that it led to a negative Effective Rate of Protection (Fukase and Martin, 1999).[16] The ERP for processed rice, amounting to minus 22.5 per cent, can be explained by the import tariffs on pesticides and fertilisers and the large share that these inputs have in the costs of paddy production. According to Nguyen (1996), pesticides and fertilisers made up around 65 per cent of the variable costs of rice farmers. In addition, the rice export sector in Vietnam can be characterized as (i) being largely variable, in terms of both quantity and value of rice exports (Table 2.5 below) and (ii) still being dominated by state-owned food companies (SOFCs).

The variability in rice exports

Table 2.5 shows a great variability in rice exports of Vietnam, in terms of both quantity and value. According to this table, the coefficient of variation of the quantity of rice exported was 45 per cent, and that of the value of rice exports was 51 per cent. This variability is attributable to the instability of the world rice market

[15] AFTA stands for ASEAN Free Trade Area. ASEAN's membership nowadays further includes Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, and Thailand.

[16] The Effective Rate of Protection (ERP) measures the change in the value added in a certain sector that results from tariffs on the product of the sector and tariffs on intermediate inputs.

and, to a lesser extent, Vietnam's government policies on food security.

The variability in Vietnam's rice exports partly stems from a distinctive instability of the world rice market (IFPRI, 1996; Minot, 1998). There are at least two sources that cause the instability of the world rice market.

Table 2.5 Vietnam: rice exports, 1989-2000

	Quantity		*Value*	
Year	*Amount* (1,000 *tones*)	*Annual growth rate* (*per cent*)	*Amount* (*USD million*)	*Annual growth rate* (*per cent*)
1989	1,372	*na*	310.2	*na*
1990	1,478	7.7	275.4	-11.2
1991	1,016	-31.0	229.9	-16.5
1992	1,953	92.0	405.1	76.2
1993	1,649	-15.6	335.7	-17.1
1994	1,962	19.0	420.9	25.4
1995	2,025	3.2	538.8	28.0
1996	3,047	50.5	868.4	61.2
1997	3,682	20.8	891.3	2.6
1998	3,793	3.0	1,006.0	12.9
1999	4,550	20.0	1,035.0	2.9
2000	3,477	-23.6	668.0	-35.5

Source: http://www.saigonnet.vn.
Note: na: not available.

First, the instability of the world rice market stems from the disturbances in the demand of rice-importing countries. According to IFPRI (1996), these disturbances result from economic sources (*e.g.*, Japan's negotiations in the framework of GATT to open-up its domestic rice market) or nature adversity (*e.g.*, the El Niño typhoon in Indonesia). To illustrate the quantitative significance of both examples: (i) Japan increased its import volume of rice from 11 thousand tons in 1990 to around 2.5 million tons in 1994 because of the negotiations in the GATT framework, and (ii) Indonesia imported only 22 thousand tons of rice in 1993 but had to import as much as 6 million tons in 1998 due to the impact of the El Niño-related drought during 1997-1998 (World Bank, 2000b). Second, the instability in the world rice market may also originate from rice-exporting countries. Although rice is produced in a number of countries, more than 90 per cent of rice production concentrates in Asia. This regional concentration of rice production exposes the world rice market to weather shocks that usually hit many countries in the region at the same time.

The above-mentioned disturbances of demand for and supply of rice may lead to substantial volatilities of rice prices in the world rice market. This is because both demand for and supply of agricultural products in general, in which rice is an example, can be characterized as inelastic, especially in the short run (Ghosh *et al*., 1987; Lanjouw, 1995). If demand for and supply of rice are inelastic, any shift of either demand or supply or both will result in substantial volatilities of rice prices.

The variability in Vietnam's rice exports is also a result of the government's policy with respect to food security. IFPRI (1996) indicated that the amount of rice actually exported was below the amount that could have been exported even if the government maintained a reasonable domestic rice consumption of 1,425 calories per person per day. Despite this, the government has still limited rice exports by adjusting rice export quota's every year. In addition, from time to time the government has imposed bans on rice exports. For instance, in the second half of 1998 the government limited rice exports because of the concerns over domestic stocks being short (Reuters, June 2nd, 1998;[17] Dow Jones, June 16th, 1998).[18] In November 2001, the government ordered rice exporters in the main rice-growing region to stop offering new rice export contracts after seeing domestic rice reserves falling (BBC News, November 21st, 2001).[19] Such unpredictable bans have created adverse consequences. Foreign buyers have encountered an absence of a clear set of policy rules that are followed consistently; they then lose confidence. This lost confidence may be one of the reasons for the discount at which Vietnam's rice has been sold in the world rice market compared to rice of the same quality from Thailand.

In sum, the rice export sector of Vietnam has encountered a great variability in terms of both quantity and value. It is very likely that this variability influences the demand for and the price of rice in the domestic rice market because more than 35 per cent of the total amount of milled rice produced in Vietnam is exported (Minot and Goletti, 2000), and the domestic demand for milled rice appears to be stable.

Limited access of private rice millers to foreign markets

In 1989 Vietnam had its first experience with rice exports. During the 1989-1990 period, only state-owned food companies (SOFCs) were allowed to export rice.[20] In

[17] *Source*: http://www.reuters.com.

[18] *Source*: http://icsea.or.id.

[19] *Source*: http://news.bbc.co.uk.

[20] State-owned food companies in Vietnam belong to two General Food Companies. The Northern Food Company (often referred to as Vinafood 1) is supposed to oversee all the provincial SOFCs in the North of the country down to Thuathien-Hue province, and The Southern Food Company No.2 (Vinafood 2) to oversee the SOFCs in the South of the country.

the 1991-1993 period, the government imposed restrictions on rice exports by reducing the number of SOFCs allowed to export rice in order to mitigate frictions among them. In 1992 the total number of rice exporters was 40, mostly in the South. Subsequently, the number of rice exporters was further reduced. In 1996 the number of rice exporters was 16. In 1998 there was an important change in the government's policy with regard to the rice export sector: in this year private rice millers were allowed to apply for rice export quotas (Prime Ministerial Decision 12/TTg in January 1998), provided that they (i) have had previous experiences in rice trading; (ii) possess sufficient milling and storage facilities; (iii) are able to supply at least 5,000 tons per shipment; and (iv) are financially sound. In fact, only a handful of private rice millers in the country were immediately able to meet these stringent requirements. In 1999 there were only four non-state rice exporters out of the total of 37 rice exporters.[21]

As a result of having a history of privileged access to foreign markets, to information, as well as to cheap bank loans,[22] SOFCs have largely dominated the rice export sector of Vietnam (Minot and Goletti, 2000). This would mean that private RMs have limited direct access to foreign rice markets. Indeed, there is evidence that private RMs have played a minor role in the rice export sector. For instance, in 1999 Vinhphat Company was granted rights to export 6,000 tons of rice, and Thanhhoa Company received a rice export quota of 5,000 tons in 1999 (Wall Street Journal, April 16th, 1999). Although these companies are the biggest private RMs of the country, the quotas they received were as tiny as around 0.2 per cent of total 4,550 thousand tons of rice exported in 1999. The peripheral role of private RMs in the rice export sector is also mentioned in some other studies on rice markets in Vietnam. IFPRI (1996) emphasizes the important link between private RMs and SOFCs in the rice circuit in the MRD in the sense that most of private RMs sell their output through SOFCs. Nielsen (2002) uncovers that private RMs in Vietnam have been working as subcontractors to SOFCs.

In 2001 the quota requirement on rice exports was abolished and anyone entitled to export food and agriculture-related goods can export rice freely (IMF, 2002a). However, having lived long in such an unfavourable condition private RMs may not be sufficiently prepared to trade internationally. Private RMs virtually do not have direct interactions with foreign traders but rather through SOFCs.

[21] These four non-state food companies are Thotnot Food Processing Enterprise Ltd. (Cantho province), Thanhhoa (Tiengiang province), LADF Company (Longan province), and Vinhphat (Ho Chi Minh City).

[22] SOFCs often receive cheap, or even interest-free, credit from the state-owned banks, especially to acquire the so-called buffer stocks (*Source*: htttp://www.fpt.vn).

2.5 Conclusions

The economic crisis in the central-planning era urged the Vietnamese government to reform the economy. The Vietnamese economic reform (*doi moi*), which was initiated in 1986, appears to have contributed largely to the country's economic growth, especially during the 1989-1997 period. It is remarkable that Vietnam did not experience the recessionary J-curve effect that characterized a number of other transition countries. Since 1998 economic growth in Vietnam has slowed down due to the Asian financial crisis in 1997/1998 and the structural weakness of the economy, with the latter being a more important and lingering factor. The structural weakness of Vietnam's economy is because, despite *doi moi*, SOEs retained a privileged position of SOEs *vis-à-vis* private enterprises.

The reforms in the agricultural sector have created incentives for people to increase rice production, among other products, leading an ample paddy surplus. The surplus, together with the international-trade reform, has facilitated the growth of rice exports of Vietnam. Although the rice export industry was successful in exporting a substantial amount of rice, it has been vulnerable to the instability of the world rice market. In addition, the position of SOFCs is still dominant, and few private rice millers are able to directly participate in the rice export industry.