

Making Difficult Choices: Vietnam in Transition



Những quyết sách khó khăn: Việt Nam trong giai đoạn chuyển đổi

Martin Rama

Based on conversations
with H. E. Võ Văn Kiệt
with Professor Đặng Phong
and Đoàn Hồng Quang

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Dựa trên các cuộc nói chuyện với Cố
Thủ tướng Võ Văn Kiệt
cùng với Giáo sư Đặng Phong và
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Bilingual/Song ngữ



WORKING PAPER NO. 40

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DFID Department for
International
Development

Dutch Ministry
of Foreign Affairs



Bilingual/Song ngữ

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1 2 3 4 5 11 10 09 08

This working paper is a product of the Commission on Growth and Development, which is sponsored by the following organizations:

Australian Agency for International Development (AusAID)
Dutch Ministry of Foreign Affairs
Swedish International Development Cooperation Agency (SIDA)
U.K. Department of International Development (DFID)
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Cover design: Naylor Design

About the Series

The Commission on Growth and Development led by Nobel Laureate Mike Spence was established in April 2006 as a response to two insights. First, poverty cannot be reduced in isolation from economic growth—an observation that has been overlooked in the thinking and strategies of many practitioners. Second, there is growing awareness that knowledge about economic growth is much less definitive than commonly thought. Consequently, the Commission’s mandate is to “take stock of the state of theoretical and empirical knowledge on economic growth with a view to drawing implications for policy for the current and next generation of policy makers.”

To help explore the state of knowledge, the Commission invited leading academics and policy makers from developing and industrialized countries to explore and discuss economic issues it thought relevant for growth and development, including controversial ideas. Thematic papers assessed knowledge and highlighted ongoing debates in areas such as monetary and fiscal policies, climate change, and equity and growth. Additionally, 25 country case studies were commissioned to explore the dynamics of growth and change in the context of specific countries.

Working papers in this series were presented and reviewed at Commission workshops, which were held in 2007–08 in Washington, D.C., New York City, and New Haven, Connecticut. Each paper benefited from comments by workshop participants, including academics, policy makers, development practitioners, representatives of bilateral and multilateral institutions, and Commission members.

The working papers, and all thematic papers and case studies written as contributions to the work of the Commission, were made possible by support from the Australian Agency for International Development (AusAID), the Dutch Ministry of Foreign Affairs, the Swedish International Development Cooperation Agency (SIDA), the U.K. Department of International Development (DFID), the William and Flora Hewlett Foundation, and the World Bank Group.

The working paper series was produced under the general guidance of Mike Spence and Danny Leipziger, Chair and Vice Chair of the Commission, and the Commission’s Secretariat, which is based in the Poverty Reduction and Economic Management Network of the World Bank. Papers in this series represent the independent view of the authors.

Acknowledgments

This paper was prepared for the high-level Commission on Growth and Development (“Spence Commission”). The views and interpretations in it are exclusively those of the author and not those of the World Bank. As an input for this paper, Professor Đặng Phong also prepared a background study on “Fence-Breaking: the Eve of Doi Moi in Vietnam.” Comments and suggestions by David Dollar, Homi Kharas, Klaus Rohland, Carolyn Turk, and Brian Van Arkadie are gratefully acknowledged. Interpretation and secretarial assistance were provided by Trần Thị Ngọc Dung, Lê Minh Phương, Nguyễn Thị Minh Hoà and Lê Bích Vân.

Abstract

After decades of war, with a dilapidated infrastructure and millions of people dead, wounded or displaced, Vietnam could have been considered a hopeless case in economic development. Yet, it is now about to enter the ranks of middle-income countries. The obvious question is: how did this happen? This paper goes one step further, asking not which policies were adopted, but rather why they were adopted. This question is all the more intriguing because the process did not involve one group of individuals displacing another within the structure of power.

To answer this question, the paper relies on the insights of those who were actually involved in the economic experiments, conceptual discussions, and political maneuvering that led to the adoption of key reforms. Especially, it builds on a series of long and regular conversations with H. E. the late Võ Văn Kiệt, one of Vietnam's leading figures. In doing so, it brings into the open the inside story of Doi Moi, a process that is not known by outsiders and remains opaque to most Vietnamese.

The relevance of this exercise is not merely historical. Understanding how reforms were engineered may yield valuable lessons for other developing countries. It is also relevant for Vietnam, as two decades of rapid economic growth have resulted in dramatic changes in its economy and society. While praising the decision-making processes that allowed Vietnam to successfully emerge from poverty, the paper also explores the adjustments that could be needed for it to become an industrial country.

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Making Difficult Choices: Vietnam in Transition

Martin Rama

*Based on conversations with H. E. Võ Văn Kiệt,
with Professor Đặng Phong and Đoàn Hồng Quang¹*

It is hard to say who the overall architect of the renovation process was because in reality there was no overall plan drawn up from the beginning to guide the process. Vietnam's transition path is such that only by traveling does the road become clear

(Professor Đặng Phong, June 2007)

Introduction: Understanding Decision-Making Processes

Vietnam is arguably one of the most successful cases in economic development in recent times. Yet, not so long ago it would have been considered a hopeless case. Decades of war had left a dilapidated infrastructure and millions of people dead, wounded or displaced. Central planning in the North and a massive foreign military presence in the South had resulted in two dysfunctional and disconnected economies. By the early 1990s, when the first somewhat reliable statistics could be compiled, income per capita was among the lowest in the world. Less than 20 years later, Vietnam is about to enter the ranks of middle-income countries, and the prospect of it becoming an industrial country within a generation is not unrealistic.

Over these two decades, Vietnam avoided the collapse in economic activity experienced by countries in the former Soviet Union, the plunge in government revenue suffered by China in the early stages of its transition, and the economic crisis that affected the East Asia region in the late 1990s. This strong performance has been accompanied by one of the fastest reductions in poverty ever documented. Recent macroeconomic turbulence may cast a shadow on Vietnam's accomplishments, but the turbulence is mainly the result of the

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H. E. Võ Văn Kiệt was Prime Minister of Vietnam from 1991 to 1997. Formerly, he was acting Prime Minister (1988–90), Deputy Prime Minister and Chairman of the State Planning Commission (1982–86), Secretary of the Party of Ho Chi Minh City (1975–1982), and Secretary of the Communist Party in Saigon-Gia Dinh during the American War. H. E. Võ Văn Kiệt died on June 11, 2008.

unprecedented volume of capital inflows Vietnam is attracting. For sure those massive inflows show that the country is entering into a new era, facing government with new challenges. But it would be wrong to see them as the end of a success story, because they are part of it.

China's growth record is usually considered to be stronger. However, since the early 1990s, exports have grown faster in Vietnam. Based on internationally comparable figures, poverty rates fell at a similar pace, if not faster too. But inequality has remained relatively stable in Vietnam, whereas it increased considerably in China.

The obvious question is: how did it all happen?

At a superficial level, the answer to this question is available. There are numerous studies documenting the policy reforms undertaken by Vietnam since the beginning of Doi Moi, its renovation process. There might be some remaining disagreements as to how those reforms related to observed development outcomes. For instance, some may consider that delaying privatization, as Vietnam did, resulted in slower economic growth and the build-up of contingent liabilities for the government, whereas others may argue that it prevented a collapse in economic activity and the emergence of a group of "oligarchs." But the sequence of decisions made, including the reluctance to privatize massively in the early stages of transition, is relatively uncontroversial.

At a deeper level the main issue is not which policies were adopted, but rather how come they were adopted? And how come the direction of reform could be sustained for two entire decades? Shortly after reunification, the 4th Party Congress reflected a strong consensus on the planned economy model, whose superiority seemed obvious after the military defeat of much stronger, "capitalist" powers. By then, the possibility of keeping the economic model of South Vietnam on a temporary basis, raised by respected Party leaders, was not seriously entertained. Thirty years later, the 10th Congress reflected a similar consensus on the need to rely on market mechanisms wherever possible. The option of going back to a planned economy deserved no consideration. By then, the debate had gradually started shifting towards the need for "democratization," and its appropriate pace and modalities.

The real question, then, is: how did Vietnam make the transition from one consensus to another? This question is all the more intriguing because the process did not involve one group of individuals displacing another within the structure of power. Unlike in other transition countries, there were no internal coups, no political purges, no open infighting.... Some of the same leaders who embraced the planned economy model in the 4th Congress were leading Doi Moi by the time of the 6th.

Equally striking, the reform process did not involve heavy outside influences. Vietnamese leaders had learned from the former Soviet Union and from China about the classical socialist model and its implementation. And they were certainly observing subsequent reform experiences in these two countries,

some times with concern. They were also eagerly learning lessons from successful East Asian countries. But the renovation process of Vietnam was not an outright imitation or import of any prepackaged economic model. The international financial institutions only became active in the early 1990s. And Vietnam was always careful to avoid aid dependency, so as to retain control over its economic policies.

Answers to this deeper question are not readily available. There are patchy accounts and abundant speculation as to the process through which key economic decisions came to be made. But it will be argued below that those interpretations tend to be quite removed from reality. A solid answer requires the insights of those who were actually involved in the economic experiments, conceptual discussions and political maneuvering that led to the adoption of key reforms.

Such is the approach adopted in this paper, which builds on a series of long and regular conversations with H. E. the late Võ Văn Kiệt. Those conversations, held in Ho Chi Minh City and Hanoi during most of 2007 and early 2008, were a unique privilege from a personal point of view. The generosity of Mr. Võ Văn Kiệt in sharing his time and insights also made those conversations an unusually rich source of information about the decision-making processes of Vietnam. More broadly, this paper can be seen as the outcome of a dialogue between an informed outsider and a leading insider, with critical historical and economic inputs from colleagues on both sides.

From a methodological perspective, the paper is in the spirit of policy history, more than economic analysis. Policy history is the investigation of the sources of unfolding policy developments, often requiring attention to processes that play out over considerable periods of time. It assumes that the shaping of public policy is more than a matter of change at a particular moment, to be captured through a snapshot. Key decisions are framed by prior events and processes. This time dimension implies that policy history may yield valuable insights on contemporary issues as well.

As with all historic accounts, it could be argued that the outcome is somewhat one-sided. Not all participants in the process stood a chance to voice their views, and a dose of subjective interpretation was involved. However, the insights offered by this approach probably outweigh its methodological limitations. The inside story of Doi Moi is not known by outsiders and, due to the political context in which reforms took place, the process through which key decisions were made remains opaque to most Vietnamese. Moreover, there are few documents to draw upon, making the personal experience of the key protagonists all the more valuable.

The relevance of this exercise is not merely historical. Understanding how consensus was built on difficult economic reforms may yield valuable lessons for other developing countries, in their often frustrated quest for prosperity. Identifying the drivers of change, as well as the obstacles along the way, could

help others navigate the turbulent waters of policy reform. Such understanding could also be useful to outsiders, especially those in the development community, as they seek to influence policy outcomes and push for further reform, in Vietnam and elsewhere.

Understanding how it all happened is also relevant for Vietnam, as it tries to cope with the macroeconomic turbulence created by its own success and strives to join the ranks of industrial nations. While many developing countries have reached middle-income status, very few have managed to go past that stage. Strong economic institutions are required to react to shocks in the short term, and to sustain productivity gains in the long term. Prudent monetary policy and effective financial sector supervision, the organization of efficient markets for infrastructure services, social insurance programs providing the right incentives, sound natural resource management and environmental protection, and a clean and transparent public administration will be needed for Vietnam to keep growing at a rapid pace, minimize the macroeconomic turbulence associated with massive capital inflows, and eventually become a high-income country.

Two decades of rapid economic growth have resulted in dramatic changes in the Vietnamese economy and society. Linkages across sectors have become much stronger, especially through finance, so that policy mistakes can entail much higher social costs. Agglomeration effects are increasingly at play, resulting in a remarkable dynamism in the main hubs of the country, but also in a growing inequality between regions and across households. And the relationship between state and society has changed as well, with the explosion in the number and diversity of stakeholders making it more difficult for the government to collect feedback on their issues and concerns.

These fundamental economic and social transformations raise new challenges for Vietnam. In the absence of a strong technical capacity to regulate and monitor increasingly complex activities, there is a risk of fundamentally misallocating resources or even wasting them in a short-term crisis. Growing inequality and displays of conspicuous wealth could generate social resentment, especially if the prevalence of corruption casts doubts on the legitimacy of the new fortunes. Weak mechanisms to gather and process the demands of specific population groups, no matter how narrow, could encourage them to voice their frustration through unauthorized channels, resulting in political turmoil. These risks are hypothetical for now, but they have materialized before in the region, in countries at a development level similar to the one Vietnam is now attaining.

It is not clear that the decision-making processes that allowed Vietnam to successfully emerge from poverty and become a thriving market economy will be sufficient to develop the strong economic institutions it needs to become an industrial country. While praising such processes, the paper also explores the adjustments that could be needed to take the country to a substantially higher level of development. Knowing how it all happened may thus hold the key to

building on that success and overcoming the emerging challenges and risks along the way.

A Decade in Search of Solutions

Understanding the success of Doi Moi requires a historical approach, one that highlights the process of trying, failing, learning and adjusting, in the hope of seeing the light at the end of the tunnel.

At the time of reunification, military victory was seen as obvious proof that the economic system of the North was superior. And central planning had indeed been well suited to running the country in times of war. But the reality is that Party leaders had very limited understanding of economics, all absorbed as they were in fighting two consecutive wars. In their eyes, the model of the South was associated with French colonialism first and American aggression later, so that they could only perceive it as evil. But their education was clearly insufficient to manage a country. They possessed weak knowledge about the world and about public administration. And victory had unfortunately reduced their inclination to listen and learn.

At that time, Soviet central planning appeared to be a successful model, one that had taken a backward agrarian economy all the way to space conquest in barely four decades. The few technical cadres of Vietnam had been trained mainly in the Soviet block, whose massive economic assistance also masked the deficiencies of central planning. This combination resulted in a series of almost unconditional beliefs, of deeply rooted norms, that should not be challenged. Among them were the rigid principles of state ownership, central planning and Party leadership.

Reunification was in many ways a brutal period. An assertive state of mind prevailed among the leadership. This was when the decision was made to change the name of the Party (from Labor to Communist) and even the name of the country (from Democratic to Socialist Republic). This was also the time of massive reeducation programs, a euphemism for sending cadres and officers of the Saigon regime to prison on a massive scale.

Reunification was also a time of overconfidence and voluntarism in relation to economic development. And in all honesty, some degree of exuberance among Party leaders was understandable, after having taken a poor rural country to victory against three of the five permanent members of the Security Council of the United Nations.

It is in this upbeat atmosphere that the 4th Party Congress was held. The Congress was unanimous on the need to set a direction for the development of the country as a whole, not for the North and the South separately. In practice, this implied that the people in the South had to adopt the model of the North. Participants in the 4th Party Congress were confident that this was the right

decision, one that would allow Vietnam to escape from poverty and engage in the way to prosperity. According to the view of the leaders of the time, economic success could not be difficult compared to the hardship of fighting a war.

Yet, during the first few months after the liberation of the South, a small group of Party figures regrouped around Mr. Lê Duẩn saw merit in experimenting with the economic model of the South, at least temporarily, while keeping the socialist model in the North. Mr. Lê Duẩn, then identified as Mr. 3, was the soul of that period. Born in the central Quang Tri province in 1907, he became one of the first members of the Indochina Communist Party in 1930 and was made its General Secretary in 1960, a position he retained until his death in 1986. During the French war, he was the Party Secretary of the South and enjoyed a high reputation among local cadres and the population at large. In the 1950s, he had expressed reservations about carrying out land reform, northern style. In the same spirit, at the time of reunification he thought that the South could provide a useful pilot for the use of market mechanisms. However, he did not push for this idea and his views were not discussed at the 4th Party Congress.

The exuberant mindset of the time had resulted in an almost absolute confidence of the Party and Mr. Lê Duẩn himself that Vietnam would succeed at whatever it would attempt. Military victory against the mighty United States, while owing to support from other socialist countries, was mainly attributed to an innovative, truly Vietnamese way of fighting the war. Why would not the same hold true in the struggle for economic development? While building on the experience of other socialist countries, the 4th Party Congress was seen as an opportunity to embrace a Vietnamese version of the planned economy model. This version was an attempt to rapidly industrialize agriculture, by bringing mass production to the rural sector thanks to irrigation, fertilizers and tractors. The operation of this model, in turn, required a minimum scale, which districts alone were supposed to provide. The Vietnamese version of the planned economy model thus came to be known as “the district as a fortress.”

In an almost surprising turn of events, this version was also Mr. Lê Duẩn’s brainchild. One of his most cited statements was “to advance fast, strongly and directly to the socialist mass production, bypassing the stage of capitalist development.” The concept of the “district as a fortress” was somewhat influenced by the агро-промышленный комплекс, or agro-industrial complex, a model first introduced in the former Soviet Union that became popular in smaller socialist countries such as Bulgaria and East Germany. Mr. Lê Duẩn proposed this concept in light of the determination of the Politburo and the Central Committee to have a single economic model for the entire country. But he was genuinely enthusiastic about what he saw as an innovative approach. The Politburo accepted his views, and the “district as a fortress” approach was adopted by the 4th Party Congress.

The planned economy model soon proved to be a blatant failure. Production had been forecasted to double between 1976 and 1980, but in reality it grew more

slowly than population did. The Five-Year Plan endorsed by the 4th Party Congress, which had been touted as a great leap forward to socialism, skipping the stage of capitalism development, was actually associated with a decline in living standards compared to the already harsh war period. The tension with China only aggravated matters, leading Vietnam to join the Comecon trading block in 1978, a decision it had hesitated to make for two decades. This resulted in much higher prices for imports than before, when domestic prices from the Soviet Union applied to goods shipped to Vietnam.

The inadequacy of the planned economy model became more evident in the South, where reunification was associated with a dramatic change in the organization of the economy, than in the North, where no similar transformation was necessary. Cadres from the South were sent to the North to learn about central planning, but the administrative prices they were requested to enforce were totally inadequate. Industry and trade stagnated. Food shortages emerged, pushing Vietnam close to famine in the 1980s. Massive numbers of people fled the country, at the risk of their lives. Those fleeing were not only individuals with close ties with the previous regime, but also people who had contributed to the fight for independence. They all just wanted to leave, as material and spiritual lives had become unbearable.

The local population gradually lost trust in the leadership, while the international image of Vietnam was seriously damaged. The feeling that the country was reaching a dead end became widespread.

Even in Ho Chi Minh City, amidst a region known as the “rice basket” of Vietnam, where nature is generous and resources plentiful, people did not have enough rice to eat. Making ends meet was extremely difficult for everyone, and local leaders started to realize that the limits of tolerance were being reached. There was also a growing sense of frustration among the leadership itself, as they witnessed the failure to achieve the idealistic aspirations of the 4th Party Congress. The ensuing crisis was then not only economic, but also social and political.

The “district as a fortress” was thus an innovative concept, but clearly not a correct one from an economic point of view. Towards the end of his life, in private, Mr. Lê Duẩn recognized the failure of his brainchild. However, it was not him but rather a set of local leaders who took on changing the course of events. They initially did so through initiatives known as the “fence breaking” experiments. What all those initiatives had in common was their reliance on market mechanisms. The local leaders behind them were desperately seeking approaches that would work, and to understand why they worked. The process required experimentation beyond what was allowed by the rules. Sometimes, dangerously so.... But all these local leaders had one thing in common, and that was to be politically “bullet proof,” given their track record during the wars.

Most of the “fence breaking” experiments took place in the South. This is not surprising, given that market mechanisms were a fresh memory there, and the

entrepreneurial spirit was still alive. But in addition, the South had been granted a transitional period for the collectivization of land. The final objective was to establish the same model as in the North, but there was agreement that the transformation would have to be gradual. Distorted agricultural prices undermined the incentives to cultivate and trade, and the prospect of having to get organized in cooperatives and collectives had eroded the farmers' enthusiasm for reunification. But at least the foundations for a supply response were present.

"Fence breaking" experiments in agriculture mainly involved allocating land to farmers and directly contracting with them at prices above those set by the plan. This approach had precedents in the North, even before reunification. In 1966, Mr. Kim Ngọc, the Party Secretary of northern Vinh Phuc province, had already experimented with it. But in 1968 Mr. Trường Chinh, the chairman of the National Assembly, a member of the Politburo and the chair of the Central Committee on Theory, convened a meeting of all key Party leaders and read a long statement denouncing the Vinh Phuc experiment. Mr. Kim Ngọc was severely criticized because of his support for "illegal" contracting and the experiment was terminated.

Circumstances were more favorable after reunification, especially in the South, where supply was more responsive. And where direct contracting was used, living conditions improved visibly. What had been treated as a dangerous deviation in the late 1960s started to be seen as innovative "unbundling" one decade later.

Examples of "fence breaking" experiments are quite telling. In the late 1970s, villagers in the North were struggling to make ends meet. Many of those in Doan Xa commune had chosen to migrate to the nearby city of Haiphong and become beggars. In 1979, some of those remaining in the commune argued that it was necessary to farm out the land to individual households. The proposition was put to vote and supported by nine to one. But the inhabitants of Doan Xa also agreed not to leave any paper trail of this decision, swearing secrecy and mutual support if the authorities were to discover the "sneak contract." The result was a six-fold increase in crop volume and a dramatic improvement in living standards.

News of this development soon reached the Party leadership at the district level, and a team of investigators was sent to the commune. The initial reaction was not to renew the Party membership of the local leaders. But gradually, information about this experiment spread, and Doan Xa became a model for the entire district.

By 1980 the Party Secretary of Haiphong, Mr. Bùi Quang Tạo, had not only extended the contracting approach to the entire province: he also vowed to lobby the Party Central Committee so that the approach could be scaled up nationwide. Knowing that Mr. Trường Chinh would be reluctant to endorse farming contracts, he first exposed the "spontaneous" farming out process to Mr.

Lê Duẩn, who had the reputation of being practical. Mr. Lê Duẩn soon visited the province to assess the situation in person; he was enthused by what he saw. Shortly after, Prime Minister Mr. Phạm Văn Đồng visited in turn and expressed sympathy for the difficulties the villagers had faced. By the time the Haiphong leadership could finally expose the situation to Mr. Trường Chinh, who was by then the President of Vietnam, he did not make any comment. This time nobody was disciplined, and by 1981 the Party Secretariat had officially endorsed the contracting approach for the entire country.

Flexibility was also introduced in the industrial sector, with production plans gradually broken down into several tiers, known as Plans 1, 2 and 3, with higher-number tiers allowing enterprises a greater independence in making production decisions and selling their products on the market. Radical breakthroughs took place in specific organizations, localities and firms. Informal trading was also allowed, increasingly, in commerce.

Meanwhile, in Ho Chi Minh City bold “fence breaking” steps had included buying rice from farmers at the market price, in spite of it being five times higher than the price set by planners in Hanoi. In an eventful breakfast convened in 1979 by Mr. Võ Văn Kiệt, Party Secretary for the city at that time, the local bank agreed to provide the necessary funding, and the finance and trade departments committed to complete the administrative formalities. Mme. Ba Thi, the director of the city’s food products company, was requested to lead the unit that would purchase rice throughout the Mekong delta. This unit came to be known as “the rice smuggling committee,” a nickname that suggests how risky its activities were. Mme. Ba Thi actually expressed her concern of being arrested if she had to travel to Hanoi, to which Mr. Võ Văn Kiệt answered that he would make sure that she got food while in prison. Eventually, a sufficient supply of rice was secured for Ho Chi Minh City. Not only did Mme. Ba Thi escape prison: she ended up being awarded the Hero title instead.

Even bolder steps were undertaken subsequently. After Vietnam had joined Comecon, in 1978, Ho Chi Minh City faced many bottlenecks in imports. To address them, the local authorities allowed Chinese traders to make contacts in Singapore and Hong Kong, China and to buy products such as tobacco, fabric and gasoline, and to buy agricultural and fishery products in Vietnam to pay for the imports. To evade control by the centrally managed customs authority, goods were traded at “sea mark number zero,” with no transaction recorded.

After a few successful deals of this sort, the People’s Committee of the City authorized lower levels of government to establish companies with names beginning or ending in “imex,” to directly handle foreign trade. Soon, some of them were booming. Cholimex had eight factories, one of them assembling electronic products. Others had cold storage facilities to preserve their export items. The activities of the “imexes” gradually expanded to other regions, including Northern provinces. Before Doi Moi, exports by these “imexes”

already exceeded the centrally controlled exports of Vietnam to market economies by a factor of ten.

Having the Party leadership tolerate, then embrace and finally scale up the “fence breaking” experiments required a careful strategy by the local leaders who had initiated them. Such a strategy was inspired by the warfare theory developed by Mr. Lê Duẩn to fight the American army and its Southern ally. Its main thrust was to avoid direct confrontation with the enemy, given its overwhelming power, and instead to gradually undermine its determination. In his own words, the goal was “not to defeat the Americans but to defeat the invading spirit of America.” This was to be accomplished by choosing isolated units as targets, dealing with them one at a time, sapping the morale of the enemy, and eventually winning by attrition. During the war, this approach had gained much praise in Vietnam, proving that sophistication was more important than strength.

The group of local leaders adopting this approach to foster economic reform included Mr. Võ Văn Kiệt as one of its most respected figures, but also several Party Secretaries at the provincial level and many directors of state-owned enterprises. In trying to promote change on a broader scale, they did not want to subvert Party hierarchies. They respected the country leadership and did not aim to uproot it; instead, they wanted it to change its mind and come to a new consensus. But they knew that this would not be easy, as “fence breaking” experiments were initially seen with suspicion by senior leaders. For instance, upon arrival to Ho Chi Minh City airport the Minister of Foreign Trade at that time, Mr. Lê Khắc, commented that he could detect the smell of Yugoslavia in the air. And that sounded more as like threat than a compliment.

At the time, the Politburo had about ten members, but in reality a few of them concentrated most of the decision-making power. This narrower group included the Secretary General, the President, the Prime Minister and the head of the Personnel Department of the Central Committee. Having an open discussion of the “fence breaking” experiments with the Politburo in its entirety would have been self-defeating, as even the reform-minded would not have dared to challenge the collective on a taboo-like issue. Instead, the fence breakers identified the mechanisms at work in each of the experiments and targeted the key Politburo members who would be more interested in learning about them. Those members were approached on an individual basis, and invited to see first-hand the experiment selected for demonstration purposes.

Even then, senior leaders would not be presented with full information about the experiments, but only with their more positive aspects, highlighting the difficulty being addressed, and the way in which “fence breaking” helped overcome such difficulty. Often, local leaders had to pose as emergency fire-fighters, as opposed to determined innovators. A systematic effort was also made to avoid any discussion of the “sacred principles” endorsed by the 4th Party Congress. Key Politburo members were instead exposed, one at a time, to

functioning enterprises, to improved living standards, and to local populations supportive of the Party.

Avoiding confrontation is actually one of the main principles of the Party in Vietnam. To abide by this principle, cross referencing was chosen as part of the strategy; for instance, by mentioning to the targeted senior leader that some other key member had witnessed another, similar experiment, and had expressed support. Local leaders were repeatedly asking for permission to travel to Hanoi, to expose what they had accomplished and request the authorization to pilot new initiatives, in the spirit of those already acknowledged as successful.

By the time the support of the four key Politburo members had been secured, larger-scale economic reform was at hand, without having to resort to wasteful fights, purges or internal coups. Among insiders, the exciting years during which consensus was built in favor of the “fence breaking” experiments came to be known as “the beautiful period.” And the series of episodes leading to the new consensus was seen as captivating at every turn, like the road from Phan Rang to Dalat.

In the end, innovative local leaders who could have been whistled out were entrusted to hold the whistle, and to build upon their “fence breaking” experiments. They were invited to Hanoi, not to be thrown into jail, but to take upon bigger responsibilities. This is how Mr. Võ Văn Kiệt became the chairman of the State Planning Commission first, then Deputy Prime Minister, and finally Prime Minister. Mr. Bùi Quang Tạc, the Party Secretary of Haiphong who had scaled up direct contracting, was promoted to Head of the Central Committee on Inspection, in Hanoi. The Chairman of Haiphong, Mr. Đoàn Duy Thành, became Minister of Trade and subsequently Deputy Prime Minister. And Mr. Nguyễn Văn Chính, the Party Secretary of southern Long An province, who had adopted a high-price contracting policy, was promoted to Minister of Food, then to Deputy Prime Minister. By then, economic difficulties and the blatant failure of the planned economy model had made the norms embraced by the 4th Party Congress much less sacred. The time for change had finally come.

Two Decades of Comprehensive Reform

Large-scale economic renovation, Doi Moi, was embraced by the 6th Party Congress, which was held in 1986, only months after Mr. Lê Duẩn’s death from a prolonged illness. By then, the prevailing mindset had changed, and an agreement could be reached on the urgency of renovation. The agreement included the need for the Party to provide a critical assessment of what had been accomplished in terms of economic development, accepting responsibility for the failures, and proposing remedial action. This decision was a breakthrough of historical significance. It marked a turning point, from decline to recovery.

Above all, it represented the beginning of a change in the main economic mechanism, from plan to market.

The 6th Party Congress represented a remarkable success in terms of consensus building. Discussions were not always smooth, and participants needed to be reminded, time and again, of the value of reconciling differences. Those who wanted to move fast had to agree to slow down. Those who preferred a slower pace were asked to speed up. The end result was a middle course, restraining the fast movers and speeding up the slow ones. The compromise was to see Doi Moi as a process, whose momentum was to be built up over time in light of experience.

One clear illustration of the tensions at play concerns international relations. One group wanted to improve ties with all countries, including former enemies. Another favored a more cautious approach, still sticking to alignment with the socialist block, out of fear of weakening Vietnam's position and eventually making it fall. The compromise here was to make friends with all countries, but not to change colors. The stated goal was global integration, not ideological dissolution. Slogans were introduced by the Party to remind its members of Vietnam's decision to embrace socialism and to call for awareness of any signs of misdirection or disorientation.

The general agreement, for quick and slow movers alike, was to always work within the framework of the Party resolutions. Having to move within clearly delimited boundaries had both advantages and disadvantages. But in retrospect, when comparing resolutions over time, all the way to that of the 10th Party Congress, it is clear that this agreement allowed sustained economic reform.

The 6th Party Congress also embodied a shift in leadership mechanisms, from individual to collective. Strong personal leadership is not uncommon in East Asian countries, socialist or not. Mr. Lee Kwan Yew in Singapore and Mr. Park Chung Hi in the Republic of Korea are obvious examples of this. In Vietnam, individual leadership played a very important role during the war effort. Mr. Hồ Chí Minh, in particular, had enormous prestige among the population. Subsequently, from the late 1960s until his final illness, Mr. Lê Duẩn became the dominant figure in Vietnamese politics. His credibility derived from his contribution to the victory over the American army and the liberation of the South. But the example of the district as a fortress approach also showed that strong individual leadership could result in incorrect economic choices.

Centralized decision making was thus replaced by strong leadership but without individual leaders. There was a move towards balancing the weight of different regions (North, Center and South) in the overall distribution of senior positions. Accumulation of multiple positions by the same person was not allowed. Retirement rules were strictly enforced, even if this could result in losing highly qualified individuals. Promotions within the Party structure often involved testing an individual's ability to operate and deliver in a province he or

she was not originally from. And decisions could not be reached without previous consultation and debate, initially within the Party, increasingly reaching out beyond its boundaries.

From then on, it became very difficult to single out a decision maker. In lieu of an individual, there was a team whose members were waiting for each other. In the absence of a prestigious leader providing a sense of direction, the collective was the decision-making body. This made it more important to thoroughly discuss the issues. The collective thus became a way to mobilize intellectual resources, both from inside and outside the Party. And a consistent effort went into avoiding the division of the Party into factions, waiting for each other, and favoring solidarity over division.

An illustration of this new approach was the process followed to join the Association of Southeast Asian Nations (ASEAN). The Politburo delegated the decision on whether to become a member of ASEAN to a standing committee. But viewpoints within this committee were very different, and the debate became so heated that in the end a vote was needed to break the deadlock. Three members of the committee favored joining ASEAN, whereas one adamantly opposed. But once the votes were cast, the Party enforced discipline, and went ahead with the choice of the majority. This kind of discipline ensured the continuity of Doi Moi as a process.

The first, critical step in this process was to change the mechanism to set the price of rice. Initial moves in this direction had happened in the context of the “fence breaking” experiments, starting in 1979. But those experiments had been geographically scattered. Across most of the country, the subsidy mechanism remained in place, resulting in the supply of rice being insufficient and an inefficiently allocated.

The story of this first step is revealing of the way decisions were made by the collective. It was argued that an instruction by the Prime Minister, liberating the market, would lead to self-regulation, akin to a magic wand. Initially, this proposal was met with resistance for fear that reliance on market mechanisms would amount to abandoning socialism. It was noted, however, that the market predated capitalism, so that it could not be deemed a capitalist invention: it was rather an ingenious invention of mankind. This way of reconciling a practical goal with broader principles was far removed from anything a Western advisor could have said in favor of market mechanisms. But in Vietnam’s political context the proposal became acceptable, and the instruction was signed by the Prime Minister.

The result was so convincing that several other food markets were liberated shortly after. Even in disaster prone areas, food shortages receded. The disappearance of food rationing became the first tangible success of economic reform in Vietnam. It helped build support for doing away with the subsidy mechanism and letting goods and services flow freely.

As for socialist objectives, such as ensuring some degree of equality, they could be catered for using other policy instruments. Land reform played a fundamental role in this respect. Between 1986 and 1993 a large fraction of Vietnam's agricultural land was distributed to rural households, on a remarkably egalitarian basis.

The combination of deregulated food markets and autonomy for farmers to make cultivation decisions resulted in a dramatic increase in food supply. It also boosted the incomes of rural households. By then, barely more than one fifth of Vietnam's population lived in urban areas. While living standards were consistently meager at the time, urban dwellers tended to be better off. The sequence of reforms was such that economic growth got kick-started in the countryside, where poverty was more prevalent, and deeper. This is one of the reasons why inequality barely increased over the Doi Moi period, whereas poverty rates plummeted.

At the risk of simplifying, three main strands can be identified in the economic reform process. The focus of the first one, which includes the liberalization of the price of rice and other key products, was to introduce stronger incentives for suppliers of goods and services, be they public or private. The monopoly of state trading companies was abolished and international trade barriers were gradually reduced. Entry by the private sector was authorized in an increasingly large number of sectors and a regime supporting foreign direct investment (FDI) was approved. The management of state-owned enterprises (SOEs) was gradually freed from administrative interference and policy lending was taken out of state-owned commercial banks (SOCBs). Transaction costs for enterprise registration were substantially lowered, whereas the equitization process resulted in a gradual divestiture of state assets, increasingly affecting large SOEs and bringing in strategic investors.

A second group of measures aimed at upgrading the mechanisms through which budget allocations are made and resources channeled. Strengthening public financial management and increasing its transparency were key ingredients of this effort. There was also a transfer of responsibility for budget appropriations to the National Assembly and People's Councils, with decisions on almost half of public expenditures shifted by now to subnational levels of government. Currently, the exercise of state ownership rights in SOEs and SOCBs is being moved out of agencies with responsibility for setting or implementing policies, into a sovereign wealth fund. The management of public investments is being revamped as well. The centralized compilation of a priority list by the Ministry of Planning (MPI) is being replaced by a more transparent management of the project cycle, from budget allocations to implementation units.

As Vietnam approaches middle-income status, a third set of more complex innovations is currently taking shape. The policy agenda is evolving from the structural reforms needed to transition from plan to market, to the institutional

reforms needed to sustain growth over time, and allow Vietnam to eventually become an industrial country.

Building on the landmark Bilateral Trade Agreement with the United States (USBTA), accession to the World Trade Organization (WTO) is leading to a substantial upgrade in legislation and standards, while fostering competition in services. An ambitious banking reform roadmap includes the creation of a modern central bank in charge of monetary policy, strengthened supervision of the financial sector, and the equitization of SOCBs. If anything, the recent macroeconomic turbulence shows how much more progress is needed on this front. In infrastructure sectors characterized by network externalities, efforts aim at creating markets and encouraging private sector entry. The health sector is starting a move from supply-side to demand-side funding, with the ambition of attaining universal coverage for health insurance. A similar transformation is taking place in relation to old-age pensions, from a transfer program for public sector workers to an insurance scheme accessible to an increasingly larger share of the population.

Some of the biggest challenges in relation to these more complex innovations concern the governance area. There has been progress in streamlining bureaucratic processes and reducing red tape. But there is concern that public administration reform has not progressed as steadily as hoped. There is also a strong determination to fight corruption, through the strengthening of government systems, an increased openness to complaints and denunciations, and the monitoring of the assets of civil servants and their immediate families. But there is also recognition that in a booming economy there are enormous opportunities for graft, and corruption will be difficult to uproot. Even the emerging concern for environmental protection has a clear governance dimension, as sound natural resource management and regional development planning will be essential for development sustainability.

When considered together, these three main sets of policy changes amount to a comprehensive economic reform, spanning all policy areas, but conducted in a pragmatic manner. The comprehensive nature of the changes undertaken is at odds with the idea, widely accepted these days, that development efforts must focus on just one or a few “binding constraints.” In Vietnam, on the contrary, it would seem that no stone was left unturned. The flip side of this diversity of reform initiatives is often their uneven progress across sectors.

Dubious Explanations of the Drive for Reform

Securing the continuation of Vietnam’s success at developing its economy and reducing poverty requires a better understanding of the forces underlying Doi Moi and the revamping of collective decision-making mechanisms that took place around the 6th Party Congress. Identifying the drivers of change can also

help pinpoint new obstacles that might have emerged over these two decades of comprehensive reform. But it may be useful to first dispel some commonly held views, which might look plausible at a first glance but do not shed so much light in practice.

One of those commonly held views sees the reform process as the outcome of a struggle between “reformers” and “conservatives.” In this view, key decision makers stood on one or the other side of some invisible line whereas circumstances, from economic hardship to natural death, gradually shifted the balance of power in favor of the reformist camp. And there is no doubt that circumstances helped. However, on a closer examination this view is problematic on more than one count. To begin with, circumstances kept changing, but the speed of reforms did not seem to be affected. If anything, the relative hardship resulting from the East Asian crisis was associated with a slowdown of reforms, not with their acceleration.

Moreover, it is very difficult for outsiders to tell who was on which side of the alleged, invisible line. For instance, Mr. Võ Văn Kiệt has been often portrayed by Western observers as a determined communist. The fact that he was from a family of poor farmers made him trusted by his comrades and paved the way for him to become a member of the Politburo at the 4th Party Congress. And with absolute confidence in communism and in the Party leaders, he implicitly endorsed the adoption of the economic model on the North across the entire country. However, he subsequently realized the problems with this model from his own experience in Ho Chi Minh City, and became one of the leading figures in the “fence breaking” experiments and in the drive up to the 6th Party Congress.

Even Mr. Lê Duẩn, on the surface a hardliner, was a more complex and subtle figure than it could seem at a first glance. While he was in charge of liberated territories in the South, during the French war, he did not favor land reform Chinese style. He did not want to prosecute landlords, and instead tried to convince them to voluntarily and temporarily surrender the use of their assets. Only landlords who were closely collaborating with the French colonial regime saw their assets confiscated on a permanent basis. Subsequently, when the country was reunified, Mr. Lê Duẩn was personally in favor of keeping the economic model of the South as a pilot to experiment with market mechanisms, at least on a temporary basis.

As for the “district as a fortress” initiative, incorrect as it might have been from an economic point of view, it was probably an attempt to bypass the slogans of proletarian dictatorship and class struggle. Following Marxist principles, each Party Congress was expected to identify the “fundamental contradiction” that needed to be solved. At reunification, many in the Party saw the tension between capitalism and socialism as such a fundamental contradiction. If so, victory required crushing the capitalists. Mr. Lê Duẩn moved into identifying a different contradiction, one between obsolete, small-scale farming and mass industrial production. Within this approach, there was no

clear enemy to defeat. From this perspective, the “district as a fortress” was not as bad a choice as its economic consequences might suggest. Mr. Lê Duẩn did not make his reasoning explicit, at least not publicly. But his close assistants knew about his political motivation. Had it not been for him, reunification would have been a much harder time.

Beyond the specific examples of Mr. Võ Văn Kiệt and Mr. Lê Duẩn, what comes out of the “beautiful period” is not a story of reformers defeating conservatives, but rather one of a reformist mindset gradually winning over. Former conservatives were not displaced, they were convinced. One telling example is that of Mr. Trường Chinh, who replaced Mr. Lê Duẩn as General Secretary of the Party in 1986. It can be argued that Mr. Trường Chinh was initially a conservative, strictly adhering to the “untouchable” principles of Marxism-Leninism. But as part of the “fence breaking” experiments, he and Mr. Phạm Văn Đồng were respectfully invited to pay visits to the field and see by themselves. This reality check, not involving any confrontation, triggered a change in their perspectives and eventually led to their support to Doi Moi.

It can even be argued that this willingness to switch to new thinking is a characteristic of politicians in Vietnam. Not only Mr. Lê Duẩn and Mr. Võ Văn Kiệt but also many others were conservative at some point in their life and reformers at some other point. In fact, some switched from being reform-minded initially to becoming more conservative over time. Ignoring this dynamic interplay of ideas and just classifying the key actors in antagonist camps is a simplification that does not help understand how economic reforms came to be embraced in Vietnam.

One variation of the “reformers versus conservatives” view associates the latter with the old generation, trained in the former Soviet block, and the former with a younger group, more exposed to Western ways of thinking. This, again, is a dubious simplification of the mechanisms at play. The key steps in the reform process were all handled by people without any formal Western training and with limited exposure to the outside world. This is clearly illustrated by their dull “packaging” of presentations and arguments, their limited fluency in English, and the resulting frustration by Western experts, often more responsive to PowerPoint presentations, catchy phrases and buzz words.

Perhaps the most obvious rebuttal of this simplified view is provided again by the example of Mr. Võ Văn Kiệt, who is widely recognized as one of the champions of reform in Vietnam. Not only did Mr. Võ Văn Kiệt lack any formal Western training: as he was actively advocating for further reform in recent years, he could not be considered young, not even by the lenient standards of East Asian societies. A similar pattern can be found at lower levels in the hierarchy.

Another interpretation of economic reforms in Vietnam sees them as the belated triumph of the South over the North. In a way, the North would have won the war, but the South would have taken the country back in times of peace.

This interpretation has some appeal, given the obvious differences between Vietnamese people from the South and the North. The former tend to be more pragmatic, more impatient, and more free-spirited too. The latter are often tougher, more cultivated, more frugal, and more disciplined. This interpretation is also supported by the history of “fence breaking” experiments, which took place massively in the South. Moreover, until recently statistics on exports per person, FDI per person, or private investment per person, in the most dynamic provinces on each side, showed the Southern ones routing those in the North.

However, from the point of view of reforms, the main difference between South and North is one of initial development levels. The North had been subject to central planning for two decades and had suffered enormously from the American war. Reunification did not make any substantial difference in living standards; if anything, peace improved the well-being of the population. On the contrary, the South was used to market mechanisms, had a better infrastructure, and a more capital-intensive agriculture. The shift to central planning, even under its “district as a fortress” version, represented a dramatic transformation, and clearly not for the better. It is not surprising that most “fence breaking” experiments happened there, relying on the more recent experience of the population with market mechanisms and a still lively entrepreneurial spirit.

As the “fence breaking” experiments clearly proved the merits of abandoning the subsidy approach and a new mindset took over, it was not only people from the South who embraced economic reform. A large fraction of cadres in government and the Party came from Nghe An and Ha Tinh, two northern provinces. On the other hand, Mr. Lê Duẩn, often portrayed as a hardliner, was born in the center of the country, and was in many ways a man of the South.

Overall, the South still does better in economic terms, which is not surprising given its higher initial development level. But the gap is narrowing by now. The fastest-growing province in Vietnam, since the early 1990s, has been northern Quang Ninh. And in terms of its dynamism, the “triangle” between Hanoi, Haiphong and Halong is already starting to resemble a coastal province in China. A closer examination of provincial performance shows success stories both in the South and in the North, mainly where the local leadership is committed to reform. Given the practice to send cadres with high potential to prove themselves in provinces they are not originally from, local leadership may not even be truly local.

Finally, another commonly held view of economic reforms in Vietnam sees them as a struggle between a grassroots movement and the central authority of the Party. Depending on the version, reforms worked because Vietnam abandoned communism, or are bound to eventually fail because it did not fully abandon communism. Beyond divergences on the outcome of this alleged struggle, in this interpretation the leadership was unable to correctly read emerging signs that were obvious to all, being as oblivious to economic realities

as it was appreciative of wartime opportunities. The reform process was therefore bottom up, and not top down. One implication of this view is that the government was not responsible for the dramatic improvement in living conditions, but rather an unnecessary irritant.

This interpretation is correct in highlighting the importance of local developments in generating change, as illustrated by the “fence breaking” experiments. But it ignores the role played by Party structures in transforming those local developments into larger-scale reforms.

The local leaders who launched this dynamic were actually high in the Party structure, and this is one of the reasons why they were “bullet proof.” Many of them were Party Secretaries at the provincial level, as was the case with Mr. Võ Văn Kiệt in Ho Chi Minh City, Mr. Nguyễn Văn Hôn in An Giang, Mr. Nguyễn Văn Chính in Long An, or Mr. Bùi Quang Tạo in Haiphong. Many, again starting with Mr. Võ Văn Kiệt, had also shown extraordinary courage during the independence wars. Mr. Đoàn Duy Thành had earned his credentials in the Con Dao prison. Mr. Nguyễn Văn Chính had been a leader in some of the fiercest battles in the Mekong Delta. Mr. Nguyễn Văn Hôn was a resolute activist in the occupied zone. Mr. Nguyễn Văn Phi, director of the Ho Chi Minh City department for foreign trade overseeing the “imexes,” had carried out secret underground activities in Saigon. And Mr. Nguyễn Nhật Hồng, director of Vietcombank in Ho Chi Minh City, was involved in secret overseas financial transactions.

These were mostly people who had fought in the war, had been tested for their political beliefs, and were trusted by the Politburo. What these local leaders did was not to subvert the existing order, but rather to convey to higher levels in the structure the solutions they had come up with, out of their own ingenuity and that of the local population. And this is why they received attention from more senior leaders.

Admittedly, the “fence breaking” experiments that paved the way for comprehensive reform later on were conducted on the fringes of the system, at the very edge of legality. However, those who led the experiments still had confidence in the Party, and this is why they respectfully raised their concerns.

The hierarchy, in turn, was responsive and gave consideration to those concerns. It is clear that not all those who tried to introduce changes were successful. But the economic difficulties associated with the old mechanism somehow reduced the opposition towards fence-breakers. As a result, fences were broken locally, but dismantled centrally. In 1979, in an effort to overcome hardship, the 6th Plenum of the Party’s Central Committee implicitly endorsed fence-breaking actions by issuing a policy on “untying production.” In 1980 local authorities were authorized by the central government to export and import directly, thus legitimizing the “imexes.” In 1981, the Secretariat authorized contractual arrangements throughout the agricultural sector of Vietnam. And in 1981, the three-tier system for enterprises was legalized, together with the

promotion of horizontal relations among enterprises and between enterprises and the market.

Doi Moi substantially amplified this trend. But it also took place within the context of Party resolutions, not outside them. In sensitive areas, moving from local experiments to nationwide policy required the endorsement of the Politburo. The drive for reform was thus processed inside the Party, not against it.

What these commonly held views on economic reforms share is their depiction of the underlying politics in confrontational terms. In all cases, the implicit hypothesis seems to be the existence of a non-cooperative equilibrium, involving a tension between two antagonistic camps. The identity of those in each camp varies slightly depending on the specific view considered, from reformers-versus-conservatives to young-versus-old to Southerners-versus-Northerners to grassroots-versus-leadership. And those who hold these views appear to sympathize with one of the two camps. Simplifying, their support goes for a more or less idealized group of young grassroots reformers from the South, even if the boundaries or membership of such group would be difficult to spell out.

This overlap between interpretation of a political process and alignment with one set of participants in it, in turn, suggests that the most commonly held views about reform in Vietnam are not that scientific. It is difficult not to sense in these views a deep antipathy for communism, the regime of the North, the influence of the former Soviet block or some combination of them. Regardless of whether such antipathy is justified or not, it may taint the interpretation of facts and thus reduce its usefulness. In a way, it feels as if those holding these views about economic reform in Vietnam, unlike those who undertook the “fence breaking” experiments or implemented the reforms under Doi Moi, were still fighting the Vietnam war.

Limited Confrontation and Few Losers

The reform process of Vietnam is better understood as a basically cooperative way of processing change, in which key participants went to great lengths to avoid “defeating” others, even if that entailed costly compromises. The willingness not to create losers was most obvious at the economic level. But it can also be found at the political and ideological levels.

Seeking consensus seems to be a long-rooted tradition in Vietnam, one that some historians trace back to the kings of the 13th century. Regardless of its origins, it can be argued that this tradition also permeated the Communist Party. Over its history, it is difficult to pinpoint a major political purge or an episode where one group of Party members physically suppressed another.

While a centralization of power took place during the American war, the 6th Party Congress reinstated consensus building as the main decision-making mechanism. Power then shifted back from individual leaders to the collective. In

a strict application of the principle of “democratic centralism,” the minority had to align with the Party line. Once a resolution was passed, there was no further questioning, and everybody was called to support its implementation. Internal debate was encouraged in the process of making a decision. But lively debates, or even fights over ideas, did not amount to factionalism. In practice, when consensus could not be reached, participants tended to adopt the “wait and see” attitude, rather than try to impose their views.

The search for consensus was not without costs. Its flip side was, at times, the adoption of watered-down policy measures, not going to the root of the problems being addressed. And the process to adopt key measures was often protracted. This has resulted in frustration among Western experts, who have complained repeatedly about the slow pace of reform in Vietnam, despite the fact that progress on development outcomes (from output to exports to poverty) was among the fastest in the world.

For instance, it is clear that Vietnam could have signed the USBTA much earlier than it did, and it possibly could have entered the WTO earlier than China. But a group of senior leaders approached these two critical steps to global integration in a cautious manner, and needed time to come to terms with them. Similarly, many thought that the resolution of the 10th Party Congress was not up to the new challenges faced by Vietnam at the time. But they agreed to live with that decision.

The determination to avoid conflict was also brought to bear on international affairs. As part of the Doi Moi process, Vietnam chose to disengage from factionalism in the global arena. One of the decisions of the 6th Party Congress was to befriend all countries in the world, including former enemies. Before, a distinction was made between three groups of countries. Those in the socialist group, embracing “proletarian internationalism,” were seen as siblings. Countries in the Third World group, which had in common their efforts to free themselves from colonialism, were considered friends. The remaining countries, capitalist and imperialist, represented the enemy; for different reasons China also fell in this last group. But this classification had isolated Vietnam, and the 6th Party Congress decided to do away with it. Seeking to treat the United States and China as partners, rather than enemies, represented a major step away from confrontation.

Economic reform was also associated with a clear attempt to avoid creating losers in the ideological arena. There were limits not to trespass in this respect, with a thin line separating the acceptable “renovation” from the unacceptable “peaceful evolution.” Moving from the subsidy system to market mechanisms was never presented as the rejection of socialist principles, but rather as a tool for their implementation. Agreement was reached that markets were not a capitalist invention. And to make it clear that economic reform did not amount to ideological renunciation, the expression “market economy with a socialism orientation” was coined.

Many would question the vagueness of this concept. It suggests a stronger emphasis on equality and a bigger role for the state, compared to a “capitalist” market economy. But beyond that general statement, it is difficult to identify specific implications on how markets should be organized. And yet, this very vagueness might have helped avoid a potentially difficult ideological discussion.

The compromise here was to move ahead on economic reforms, but not to question the Party’s “sacred principles.” This was a way to give reassurance to those who were concerned about abandoning Vietnam’s political system. For instance, when the leaders of Haiphong vowed to extend the contracting approach to the entire nation, the first thing they set up to do was to read carefully the statement by Mr. Trùng Chinh, criticizing the Vinh Phuc experiment. This was to push for reform without embarking in an ideological confrontation.

A similar ambiguity is at play when the Party continues to identify itself as the representative of “workers,” despite the fact that an increasingly large fraction of its members is made of successful entrepreneurs. In practice, from the 6th Party Congress onwards the notion of “class struggle” has been downplayed. Insisting on a struggle, any struggle, would have been at odds with the effort to rely on consensus as the main mechanism for the collective to make decisions. But openly abandoning the class struggle would have amounted to renouncing Marxist principles, which in turn would have alienated a substantial constituency within the Party.

Vietnam’s success in adopting comprehensive reforms is also associated with the determination to avoid creating losers from a material point of view. In this respect, the focus on poverty reduction and social inclusion can be seen as application of the Pareto principle, according to which a reform can be considered welfare improving only if at least some people benefit from and nobody is made worse off because of it.

Not making losers was easy in the initial stages of Doi Moi, given that the situation was extremely difficult for almost everyone. With the country at the edge of famine, no one could do much worse. So initially there was no need to think about compensating anyone for the consequences of economic reforms. However, as the economy emerged from extreme crisis conditions the move from the subsidy system to market mechanisms could have had a negative impact on specific population groups, or have favored some groups much more than others. Policy measures adopted after the initial stages of the Doi Moi process tried to prevent both declines in living standards and increases in inequality.

Consider the reform of SOEs, which aimed at enhancing the authority of directors to make decisions without administrative interference. Those directors could lose from market liberalization and the privatization of state assets. But they were spared. The introduction of stronger incentives to maximize profits was done in such a way that insiders could appropriate a significant share of those profits through bonuses and other additional payments (some of them not

official). As for privatization, the initial phases of the equitization process allowed SOE directors to become partial owners of the enterprises they managed.

Workers in the public sector, probably the only large group that would have qualified as privileged under the subsidy system, were also spared. When some basic forms of social protection such as access to old-age pension were extended to the formal private sector, the benefits of public sector workers were grandfathered, with the budget making up for unpaid social security contributions.

A cash compensation program was also set up for redundant workers from SOEs. In its initial phase, the amount of compensation was determined in a hurry, to cope with the factory closures prompted by the collapse of trade with the former Soviet block. Subsequent stages saw a deliberate effort to set compensation at a level that would make redundant SOE workers roughly indifferent to job separation. Tracer surveys of separated workers reveal a relatively high level of satisfaction with the assistance received, suggesting that the effort was successful. This program has been maintained for years, in spite of its considerable cost to the budget.

The overall growth strategy also had the effect of raising the income of agricultural households, which were certainly not part of the public sector elite. The eminently egalitarian redistribution of agricultural land, combined with the liberalization of trade in commodities, did much to boost rural living standards and reduce poverty. The measures taken to attract FDI, to a large extent in labor-intensive sectors, also provided an avenue out of poverty for unskilled rural migrants. The commercialization of agriculture and the rapid creation of wage employment were thus instrumental in preventing great increases in inequality, in spite of the fast pace of economic growth.

More recently, a sound system of intergovernmental transfers has been put in place, to redistribute resources from richer to poorer provinces. The move towards greater fiscal decentralization, in 2002, led to the establishment of transparent rules to allocate budget funding to lower levels of government, first for recurrent expenditures and subsequently for capital expenditures. Combined with targeted programs aimed at providing benefits to specific population groups, these budget allocation norms result in substantial income redistribution. With some of the poorest provinces receiving the equivalent of half of their GDP through transfers of this sort, the volume of resources channeled to lagging regions in Vietnam is much larger, in relative terms, than it ever was in the European Union. This arrangement, again, is an illustration of the deliberate effort of the Vietnamese government to preserve social inclusion, hence to minimize resentment and social tensions as the country grows richer.

Processing and Accepting New Ideas

Because of its ability to minimize confrontation and to avoid creating many losers, the reform process in Vietnam can be better understood as a basically cooperative undertaking, with policy changes driven by the acceptance of new approaches by the leadership, rather than by the victory of one group of insiders over another. This interpretation, in turn, makes it important to understand how information and views are collected, processed, and brought to the attention of those with the authority to approve them and to launch their implementation.

What makes a new idea interesting and potentially acceptable? At some point, specific innovations may seem too bold or too radical, given the historical context, to be given serious consideration. For example, the proposal by Mr. Lê Duẩn in September 1975 to keep the economic system of the South on a temporary basis, so as to experiment with market mechanisms, falls into this category. But other daring innovations ended up being accepted by the Politburo and other senior members of Party and government. Where did the impetus come from? At the risk of simplifying, there are three main sources of innovative ideas: international experience, local think tanks, and experimentation on the ground. The relative importance of these sources varies depending on the circumstances.

International experience featured prominently in the policy orientations of Vietnam, even before reunification. For instance, there was an important role of Chinese advisors until the mid-1950s, when Maoism was seen as classic theory by many Vietnamese. The Chinese version of land reform became popular, and its implementation led to extremely grave consequences. It took a public statement by Mr. Hồ Chí Minh to revert this trend. As a result, from 1956 onwards Chinese orientations such as the great leap forward, people's communes or the Cultural Revolution were watched with greater concern. For Vietnamese leaders, the Cultural Revolution represented a brutal attempt to suppress divergence of opinion in the face of economic decline. From that point onwards, the Chinese influence on Vietnam receded, with the ties between the two countries being completely severed after reunification.

Reliance on Russian experts became more common during the American war, when the direct influence of the Soviet block became stronger. There was of course recognition of the differences between, say, the Soviet Union and countries like Romania, Hungary or Poland. In fact, the Bulgarian experience was an important inspiration for the "district as a fortress" approach of Mr. Lê Duẩn. The shift towards the model of the Soviet block became unambiguous around the time of reunification.

Towards the end of the American war, Vietnam invited two delegations of economic advisors from the Soviet block. The first one, from East Germany, arrived in 1973; the second one, from Russia, in 1974. Size considerations explain the interest in East Germany. Russia was deemed as too big an economy for its experience to be directly relevant for Vietnam. However, not much of practical value came out of these missions.

Another socialist country whose size was commensurate to that of Vietnam was the Democratic People's Republic of Korea. In 1973, Mr. Lê Duẩn had sent a delegation there. It was led by Mr. Trần Phương, head of the Institute of Economics and a direct advisor to Mr. Lê Duẩn. But the delegation was unimpressed. Upon its return Mr. Trần Phương reported that there was nothing for Vietnam to learn from the economic model of the Democratic People's Republic of Korea.

Shortly after reunification, those external models which Vietnam had been studying initiated their own transitions. In China, Mr. Deng Xiao Ping came to power in 1978 and initiated the reform process in 1979. However, this was also a time of military conflict between the two countries. At that time, Vietnamese leaders regarded China's economic reforms and the four-modernization drive with suspicion, as the initiative of an enemy and a betrayer of socialism. There was more receptiveness to the changes happening in Russia, with the assumption of power by Mr. Mikhail Gorbachov in 1985, and his move towards glasnost and perestroika. The government of Vietnam was definitely interested in these experiences, and open to adopt new ideas that would work. However, such openness did not lead to outright copying. For instance, Russia went through economic reform but also through political reform. From a Vietnamese perspective, the latter was a source of considerable turbulence, undermining the Party's authority and interfering with the smooth implementation of economic reforms, so that it was not seen as a model to imitate.

As for Western countries, for quite a long time Vietnamese leaders had very limited information about them. They were aware of the socialist model, which they perceived as successful, and felt a sense of solidarity with other socialist countries. They also knew that there were a number of politically independent countries with their economies built alongside the capitalist model, which they lumped together in a Third World group. But their knowledge of the specifics of a market economy was totally insufficient to serve as guidance for economic reforms. And Third World ideas did not have any significant impact either.

The first serious exposure to economies organized along different principles was in the East Asia region. Military intervention in Cambodia had resulted in a complicated external situation for Vietnam. On the diplomatic front, that was the worst time ever, with criticism coming from all quarters, including from otherwise friendly socialist countries (not to mention China's vehement opposition). In 1988, Mr. Võ Văn Kiệt met then with Singapore's Mr. Lee Kwan Yew, who stated that a precondition for the normalization of relations with

Vietnam was its withdrawal from Cambodia. Such withdrawal had already been decided by the time of the meeting, which facilitated the dialogue and transformed Mr. Le Kwan Yew into an important reference for Vietnam. His optimism about the country's potential made him an enthusiastic advisor of senior leaders. The spectacular economic success of Singapore certainly made it a model to learn from. And the combination of market principles with a considerable degree of political control made it particularly attractive to the Vietnamese government.

The Republic of Korea became another country for Vietnam to watch. As a technical assistance program was set up by the United Nations Development Programme (UNDP), one of its first uses was to fund a study tour to Seoul, in 1990. The delegation was led by Mr. Trần Xuân Giá, who was then chairman of the Office of Government and later became Minister of Planning and Investment. The delegation was impressed by the speed at which the Republic of Korea had developed after the end of its own devastating war. In a telling reflection of the difficult times Vietnam was going through, it alternated between official banquets, to honor the victors of the Vietnam war, and meals on sidewalks, to save on UNDP per diems, which amounted by then to months of salaries.

Donor assistance played an important role too. Having maintained a continuous presence in Hanoi, the Swedish were influential in sponsoring workshops, bringing experts and funding study tours. As the momentum of reform gathered pace, the government also maintained an active dialogue with Japanese experts, whose views on economic strategy often varied from those of their Western colleagues.

The normalization of the relationship with the Bretton Woods institutions formally took place in 1993. But contacts had been established earlier than that. In 1989, an important initiative was undertaken to separate budgetary functions from central bank functions; to move the commercial operations of the State Bank of Vietnam to commercial banks; and to authorize the establishment of joint stock banks, credit cooperatives, and foreign bank branches. Mr. Võ Văn Kiệt was the first Deputy Prime Minister at the time. To handle this eminently complicated issue he took an unprecedented approach in the socialist system, namely to set up two independent groups of specialists to conduct studies and provide advice. Mr. Võ Văn Kiệt listened carefully to the advice of the two groups and combined their most suitable proposals for the development of an ordinance on the banking sector. Mr. Huỳnh Bửu Sơn was then charged to contact the International Monetary Fund (IMF), which shortly after sent a mission to Vietnam to help finalize the legal documents for this important reform.

The UNDP, which together with Sweden was among the few donors with a presence in Vietnam, was instrumental in mobilizing expertise from the World Bank before the normalization of the relationship with the Bretton Woods institutions.

Still, for quite a while several senior leaders saw those institutions with suspicion, as controlled by industrial countries and in particular by the United States. At first, they were mainly treated as a source of finance. And the government of Vietnam was keen to avoid depending too much on their resources, so as to keep policy choices fully under its control. As the sense of suspicion was gradually dispelled and the relationship with the Bretton Woods institutions matured, more importance was attached to their technical inputs and economic analyses. But throughout the 1990s the government stuck to its choices when the recommendations were not deemed well-suited to the circumstances of Vietnam, as in relation to rapid privatization for instance.

Over time, the relationship with the World Bank was substantially deepened, to the point where Vietnam is by now the largest borrower from its concessional lending arm, the International Development Association, except for India. The World Bank also acquired an increasingly important role as coordinator of the donor community and purveyor of analytical work. From 2001 onwards, a regular cycle of policy lending operations was established, with an increasingly large number of donors supporting it, through both funding and technical inputs. These operations only involved strict policy conditionality at their inception, gradually evolving into a mechanism to ensure the coherence, timeliness and content of policy reforms.

On the other hand, the relationship with the IMF became increasingly loose, with disbursements stopping in 2002 and the last lending program expiring in 2004. On the surface, the fallout was over a technical issue, namely the possibility of subjecting the central bank to external auditing. But the fact that no side wanted to compromise reflected a growing disagreement on the speed of policy reforms, especially in relation to the privatization of SOEs and SOCBs. Vietnamese leaders had also been sensitive to critical views from senior policy makers in the region on the way the IMF had handled the East Asian crisis of 1997.

Universities and research centers started to be established by independent Vietnam at the end of the 1950s. Examples include the Economic Institute, created in 1960 under the Vietnamese Academy of Social Sciences (VASS) and the Central Institute for Economic Management (CIEM), founded in 1978. However, until well into the Doi Moi process, the contribution by these institutions to economic reform was quite limited. This can be explained both by their official mandate and their human resources policy. The mandate was to support the leadership, not to provide independent views. In particular, following economic developments and policy debates in market economies was not part of the mandate. As for their human resources, key advisors and researchers were selected by the Central Committee of the Party after clearance from its Personnel Department. As a result, those recruited tended to be chosen on the basis of their political loyalty, ideological alignment, or ability to interpret the views of the leadership, more than on their technical merit. Not surprisingly,

their basic knowledge was drawn from the classical works of Karl Marx and V. I. Lenin and most of their reference books were of Russian origin.

During the decade in search for solutions, “informal” think tanks actually made a more important contribution to economic reform than mainstream institutions. The case of Ho Chi Minh City is telling in this respect. In 1976, unsatisfied with the official economic advice received from the North, and aware of the limited technical knowledge of the team in charge of running the city, Mr. Võ Văn Kiệt established a unit in charge of mobilizing the intellectual resources from the former regime in the South. The goal was to ask for honest advice, confront the views from all sides, and to choose in each case the recommendations that seemed more appropriate. One of the members of this unit was Dr. Nguyễn Văn Hào, a specialist in macroeconomic policy. More striking was the participation of Mr. Nguyễn (“Jacky”) Xuân Oánh, a former Deputy Prime Minister of the regime of the South and a Harvard-trained economist whose father had a close relationship with the resistance. The work of this unit was not without frustrations. After some time, discouraged by the fact that few of his suggestions had been retained, Dr. Nguyễn Văn Hào asked for the permission to leave the country with his family, which was granted.

Developments accelerated around 1984. By then Mr. Lê Duẩn’s health had deteriorated and his personal prestige was undermined by the failure of the “district as a fortress” approach, which people saw as his idea. In parallel, the role and prestige of General Secretary Mr. Trường Chinh were on the rise. Mr. Trường Chinh convened a group of highly respected, open-minded specialists to help develop thinking innovations. This group was led by Mr. Hà Nghiệp and Mr. Trần Nhâm. Jointly with a dozen other experts from various sectors, this group was directly involved in the preparation of the contents of the 6th Party Congress.

In subsequent years a number of researchers and journalists started to report on the “fence breaking” experiments and to analyze the reasons for their success. First in a cautious way, more openly over time, workshops and seminars were held to provide information to senior leaders and even to the Politburo. This intellectual ferment greatly contributed to the reform momentum that led to the 6th Party Congress. By then, the role of think tanks and research institutions started to be seen in a more positive light.

A change in the role played by mainstream think tanks and research institutes is noticeable since Doi Moi. In 1989, the Institute for International Relations undertook to translate Mr. Paul Samuelson’s famous economics textbook into Vietnamese. Lacking the resources to pay for the copyright, it wrote to the author, who graciously waived any fees for Vietnam. Gradually, other books and documents were translated, and courses on the market economy were organized. Also in 1989, a team from the World Bank institute in charge of training was even invited to give a course on inflation and stabilization, with attendance by the Prime Minister and various ministers.

The composition of the two independent groups set up by Mr. Võ Văn Kiệt to study and give advice on banking reform is equally revealing of the spirit of the time. One of the groups consisted of scientists who had been trained in the Soviet block and held high-ranking positions in government. The other group consisted of banking specialists from the old regime in the South.

Between 1989 and 1993, a critical contribution was made by a project set up in the Office of the Council of Ministers under the leadership of Mr. Vũ Tất Bội. This project put together funding from the UNDP and various agencies, and used it to translate a large amount of material, organize ministerial level seminars, and send young economists and lawyers to study abroad. From this group emerged individuals who were later instrumental in international trade negotiations and the formulation of new regulations for business development.

By now, several of the mainstream think tanks and research institutes are playing a much more active role in informing public policies and supporting economic reform. CIEM has made important contributions to the legal framework for doing business, including enterprise registration, corporate governance and investment approvals. It has also conducted rigorous evaluations of the impact of SOE equitization. VASS has been the focal point for the sectoral studies supporting the negotiations for WTO accession, and is playing an important role in the analysis of poverty and related social issues. The Institute of Labor Studies and Social Affairs (ILSSA) is making increasingly important contributions in relation to labor policies and social insurance. Equally valuable initiatives are under way at the Ministry of Health, in relation to health insurance, and at the Ministry of Industry and Trade, in relation to power sector reform. In all cases, a drive towards increased analytical rigor is noticeable.

Underlying this upgrading of the technical input to public policy is the availability of better data. For quite some time, hard evidence was not an essential input for policy making in Vietnam. No sophisticated impact evaluations were needed to realize that the “fence breaking” experiments were associated with better economic outcomes. The channeling of resources to the poor could rely on the classification of households produced by local authorities, often involving consultations with villagers and even direct voting on the list of “poor households.”

As the economy becomes more developed, and the policy issues more complex, the tools needed to inform economic policy become more sophisticated too. The first official effort to estimate GDP took place in 1989. The first nationally representative household survey for Vietnam was conducted in 1993, with funding from UNDP and technical support from the World Bank. Since then, surveys of that sort have become part of the core business of the General Statistics Office (GSO). Samples are much bigger and the frequency of data production is higher. Since 2000, GSO has also conducted annual enterprise surveys. The quality and accessibility of budget data has also improved substantially, thanks to sustained efforts by the Ministry of Finance (MOF). And

experimentation is under way on governance indicators. On the other hand there is considerable room for improvement in critical areas such as monetary policy and the financial sector, public expenditures at subnational levels, public debt data, and the balance of payments.

In the end, major policy decisions still require the blessing of the Politburo. The viewpoints of VASS on WTO accession would not had been so relevant if it were not for the ability of its chairman, Dr. Đỗ Hoài Nam, to convey them to the Prime Minister, especially prior to the 8th round of negotiations, in 2004. At that time, several leaders were still approaching accession from a “concessions” perspective, rather than from a “development” perspective. Similarly, the support of the Politburo for an ambitious roadmap for banking reform, secured in 2006, was greatly facilitated by the personal involvement of Dr. Cao Sỹ Kiêm, former Vice-chairman of the Economic Commission of the Party. This was after almost one year of low-key technical work by a small group of domestic and foreign experts.

The impact of technical inputs like those produced by research institutes and think tanks is clearly amplified when an effective communication channel exists with senior leaders. Such communication still involves “bullet proof” mediators, who can convince the highest instances of the Party of the merit of new ideas, without running the risk of being labeled as revisionists. For important reforms, the mere technical soundness or attractive packaging of technical inputs is not enough. Senior leaders must be convinced that recommendations are based on the reality of the country, would serve its best interests, and would be compatible with political stability.

To some extent, this cautious attitude can be seen as a legacy of the decade in search of solutions. At the time, assistance from other socialist countries might actually have delayed economic reforms, by masking the deficiencies of central planning. More importantly, the blind copying of outside models, not well-suited to the realities of Vietnam, appeared as a mistake not to repeat. This was true of the models of China and the former Soviet block. After Doi Moi, the same caution applied to the “lessons of international experience” or “best practice models” advocated by Western experts without first making sure that they were relevant in Vietnam’s case. This cautious attitude was reinforced, from 1989 until the early 1990s, by the collapse of the former Soviet block. Senior leaders were then concerned about the implications of “peaceful evolution,” and this is how slogans such as “integrate but do not dissolve” and “renovate but do not change colors” came to be coined.

In an almost paradoxical manner for a country ruled by a Communist Party, this cautious attitude and the emphasis on relevance have led to a deep sense of mistrust of anything that may look ideological, regardless of whether it is inspired on the “sacred principles” of socialism or on economic “first principles.” Inductive reasoning tends to be favored over deductive approaches. Piloting new ideas and extensively discussing the outcomes is a common practice, one which

represents a defensible approximation to policy evaluation. And there is no scaling up of the pilots until consensus has been reached on their merits. Admittedly, this process takes time and often leads to frustration, especially among Western experts who are not aware of its history. But the Vietnamese approach to processing and accepting new ideas also reduces the risk of major policy blunders and costly policy reversals. This approach is clearly an important legacy of the decade in search of solutions and the “fence breaking” experiments.

Emerging Challenges and Risks

The basically cooperative way in which new ideas on economics were processed and accepted by the Vietnamese leadership over the last two decades may explain why the country was so successful at raising living standards, reducing poverty and avoiding major crises. But continuity should not be taken for granted as Vietnam moves into the ranks of middle-income countries. Its own success is confronting the country with new challenges, and the mechanisms underlying Doi Moi may be less well-suited to address them than they were to support the transition from plan to market.

Simplifying, the emerging challenges for Vietnam can be classified into three main categories. First, as the economy has become more integrated, both domestically and internationally, the effects of inadequate policy decisions can be greatly amplified. Financial crises, in particular, are among the biggest risks usually faced by middle-income countries. They are an even bigger risk in Vietnam, given the unprecedented capital inflows the country is attracting as a result of its own success. Second, as agglomeration effects favor rapid productivity growth in the urban hubs of the country, maintaining moderate levels of inequality will become increasingly difficult. In a context where corruption is still widespread, the legitimacy of wealth could be called into question, resulting in social discontent. And third, as the economy has become more diversified and the number of stakeholders has exploded, channeling their feedback to the government will become more difficult. Failure to acknowledge the change in the relationship between state and society could in turn fuel political turmoil.

These three risks have actually materialized in the region before, affecting other countries at a development level similar to that Vietnam is currently attaining. In Thailand, inadequate supervision of the financial sector and the liberalization of the capital flows combined with inappropriate exchange rate policies resulted in the Thai baht crisis, subsequently compounded by an excessively tight budgetary policy. While the country recovered from the turmoil, it has not managed to return to its previous growth performance. In Indonesia, three decades of rapid economic growth had raised incomes across the board, but a small urban group with very good connections at the highest

levels of power became conspicuously rich. Resentment about this apparently ill-acquired wealth contributed to the Suharto backlash, and since then Indonesia's economy has not done so well. In China, high inflation and urban unemployment led to social unrest and alienation in the late 1980s. One visible manifestation of the discontent was the Tiananmen Square demonstration, which the government could easily suppress, but at a considerable cost in terms of international image.

The first risk, namely failing to effectively manage and guide economic developments, is amplified by the increasing financial interdependence of the economy. The last two decades have witnessed a considerable financial deepening, so that the inability of one group of stakeholders to service their debts, or their capacity to rapidly restructure their assets, can launch shock waves throughout the economy. In the past, the nonperforming loans of SOEs made SOCBs unprofitable, if not formally insolvent, resulting in a liability for the government budget. But they did not threaten the overall economic stability of Vietnam. Capital could not flow freely in and out of the country either, so that turbulence in foreign financial markets had limited consequences for Vietnam. This is not the case anymore. Both financial deepening and international capital mobility can increase economic efficiency, but they also create vulnerabilities requiring highly capable economic management.

The quest for consensus, in turn, has resulted in reforms advancing at different paces across sectors. The resulting imbalances also reduce the capacity of policy makers to control economic developments. For instance, consensus was reached on the need to accede to the WTO earlier than on the urgency to reform the financial sector. To some extent, this sequencing was justified. WTO commitments were used as a way to "lock in" major economic reforms, including increased competition in financial services. The practical irreversibility of those commitments, in turn, made the reform of the banking sector a necessity. But the result is a mismatch between a surge in capital inflows and the absence of a modern central bank, with strong capacities to conduct monetary policy and supervise the financial sector.

Imbalances of this sort are also obvious in other areas. In relation to infrastructure services, and especially to electricity, the need to cope with a surge in demand is leading to massive investments before appropriate market organization and regulation are in place. As a result, capital could be inefficiently allocated, market power could be concentrated among a few players, and the price of electricity could be excessively high. In relation to the environment, industrialization is advancing at a fast pace before instruments for pollution control and natural resource management are effective. The consequences could be costly to reverse later on. In these two examples, the uneven pace of reforms may not result in short-term crises, but the long-term consequences cannot be ignored.

The second major risk faced by Vietnam as it enters the group of middle-income countries is to confront growing social resentment. By redistributing agricultural land in an equitable way and promoting FDI in labor-intensive sectors, the Doi Moi process dramatically raised the incomes of rural households and unskilled workers. This in turn helped contain the increase in inequality, to a remarkable extent for a rapidly growing country. But the economy has become much more sophisticated, with a rapid transformation taking place in industries with higher value added and in services. High incomes are now associated with information technology, financial services, real estate, or upscale retailing. These sectors greatly benefit from agglomeration effects, and are bound to develop in the economic hubs of the country. The earnings gap between urban and rural areas could then increase dramatically, with those less able to integrate in this modern economy (and especially ethnic minorities) being left behind.

Inequality is also bound to increase as a result of capital gains, especially in relation to land. With a booming economy, rapid urbanization and massive land conversion, properties in the “right” locations see their value surge. Knowing what the right locations are and being able to acquire the properties before the surge in prices takes place is a sure road to riches. But not everybody knows and not everybody can acquire. Insufficient transparency in zoning policies, limited issuance of land-use right certificates, inappropriate pricing of land plots and weak capacity of land administration offices all result in relatively few people making fortunes. Those who see their land reclaimed at low prices and witness how others make the capital gains can only feel aggravated.

The prevalence of corruption could add to the resentment. In the poor Vietnam of the early years of Doi Moi, petty corruption was an accepted way to make ends meet. It was the individual equivalent of “fence breaking” in the face of an overregulated and inefficient system. As the economy develops, markets function more adequately and people grow richer, corruption is increasingly associated with greed, more than need. The prevalence of corruption may thus undermine the legitimacy of wealth more generally. In a context where many people can be expected to become rich in a few years, sometimes very rich, doubts about the legitimacy of wealth may lead to bitterness among those who fall behind.

The third risk is more political in nature. When Doi Moi was launched, the diversity of stakeholders was very limited in Vietnam. Caricaturing only slightly, there were rural households engaged in small-scale agriculture and urban households linked in one way or another to SOEs or the government. Therefore, the diversity of issues and concerns faced by the Vietnamese people was limited too. And most of those issues were in one way or another related to securing a subsistence-level living under very difficult conditions. Under these circumstances, it was relatively easy for the Party to gather the views of the population. It could not go wrong by favoring the average farmer in the deltas,

or the average public sector worker in the cities, even if this approach did not work so well for ethnic minority households in the highlands.

Two decades later, the number of stakeholders in the Vietnamese economy has exploded. In addition to small-scale agricultural units and the public sector, there is a large group of FDI companies and a thriving private sector. Hundreds of thousands of domestic private enterprises have been created, and a large minority of Vietnamese households runs a small business of one sort or another. The diversity of production and exports has also increased remarkably, with new dynamic sectors emerging one after the other, from garments to sea products to furniture to software. And there are even a growing number of civil society organizations.

These multiple stakeholders have specific concerns in product markets, in labor markets, or in their relationships with a range of government agencies. But the traditionally effective mechanisms used by the Party to gather feedback from society are not necessarily well suited to handle so much diversity. Understanding the issues faced by all these groups, and addressing them properly, amounts to an enormous information processing task. Measures are being taken to increase the government's capacity to perform such a task. But there is still a risk that specific groups of stakeholders may become alienated if their concerns are not addressed, and could seek to express their grievances in destabilizing ways.

Which Role for the International Community?

Over the two decades since the beginning of Doi Moi, donors and international organizations have provided both resources and advice to support the reform drive of Vietnam and to help it emerge from poverty. This process has included both successes and failures. As the country moves higher into the ranks of middle-income countries, the volume of international assistance is bound to decline in relative and even in absolute terms, which makes the next decade a very crucial one in terms of engagement. This is the time to assist Vietnam in laying the institutional foundations for it to continue on a sustained growth path, even after many donors wrap up their development cooperation.

The Vietnamese government has a tested approach to policy reform, one that involves exploring new economic ideas and creating consensus around them. But in order to address the emerging challenges, this approach also needs adjustments, some of which could be perceived as threatening. Reassuring the senior leadership that this is not the case, and that the proposed adjustments are in Vietnam's best interest, may require emulating the process whereby innovators managed to convince the Politburo that relying on market mechanisms was not incompatible with the objectives of socialism.

Members of the international community will be unable to make the case for adjustments of this sort unless they are “bullet proof,” as were the provincial Party leaders who carried out the “fence breaking” experiments. Outsiders will not be listened to if they seem to have a poor grasp of Vietnamese realities. And their recommendations will only be credible if it is clear that they are not driven by hidden agendas, and especially by politically motivated agendas. If there is no trust, there is little chance that new ideas volunteered by donors and international organizations will get serious consideration by Vietnam’s senior leaders.

The successes and failures of the last two decades are telling in this respect. At one end of the spectrum, a donor like Sweden had the necessary credibility, because it stood by Vietnam’s side during the most difficult years of the American war. This tested solidarity allowed the Swedish cooperation agency to engage in a dialogue on corruption with the Party at a time when the issue was almost taboo. Probably no other donor would have been listened to. This engagement, while frustrating at times, paved the way for an important change in policy. The Party identified the fight against corruption as a top priority at the end of 2003, at which point it chose to move away from a mainly punitive anti-corruption strategy to one involving systemic reforms and increased transparency.

At the other end, initially there was limited trust in the Bretton Woods institutions, which were feared by some to be at the service of industrial countries in general, and the United States in particular. The World Bank had a solid engagement in relation to infrastructure development and poverty reduction programs. But skepticism remained in relation to the advice being provided on structural reforms, especially in the aftermath of the East Asian crisis, when the Vietnamese leadership became more cautious. At that time, the World Bank and the IMF insisted on the privatization of SOEs and SOCBs as the cornerstone of any serious reform program. In doing so, they faced resistance from Vietnamese authorities, who preferred a more gradual approach.

To encourage the government to be more decisive, the Bretton Woods institutions argued that timid reform could result in an economic meltdown. Vietnam was included in the list of Highly Indebted Poor Countries (HIPC), as if its external situation was weak enough to warrant debt relief. By now it is clear that Vietnam is at low risk of external debt distress. Vietnam’s growth performance was also questioned, with the Bretton Woods institutions reporting figures much below those of the government. Those alternative figures were based on simple macroeconomic consistency models, known for their sensitivity to assumptions. These bleak scenarios might have worried Vietnamese authorities for some time, but exaggeration is not a solid foundation for credibility.

In 2001, an agreement was finally reached between the Bretton Woods institutions and the government on a structural reform agenda. This agreement

paved the way for a series of policy lending operations which eventually became the main platform for the policy dialogue between the government and the international community. Shortly after, Vietnam was also taken out of the HIPC list.

In 2003, the World Bank retroactively accepted official statistics on growth and dropped its own alternative figures. It also accepted the government's gradualist approach in relation to SOE and SOCB reform. Its focus shifted instead towards WTO accession as the main mechanism to "lock in" further reforms. Importantly, the World Bank moved away from a negotiation approach towards an active analytical collaboration with the institutes and individuals who advised senior policy makers. This engagement approach had been used since the late 1990s with MOF and MPI, effectively, in relation to public financial management reform and planning reform respectively. Among others, it was subsequently extended to VASS, in relation to WTO accession, and to the Economic Commission of the Party, in relation to financial sector reform. Working together with those who could in turn directly discuss with senior leaders improved mutual understanding and helped build mutual trust.

The IMF, on the other hand, remained unimpressed by the government's stance on SOE and SOCB reform. In 2004, a dead end was reached and the IMF's lending program formally expired. Since then its influence on Vietnamese economic policies has been more limited.

Another important lesson for the international community concerns the nature of the ideas put forward for consideration. Those leading the "fence breaking" experiments were particularly careful to avoid anything that could look ideological. Instead, they emphasized the practical aspects of their innovations, including the specific problem they aimed to address and the ways in which these innovations contributed to the wellbeing of the population. Opportunities were found to pilot the implementation of new ideas, and assess their consequences. Over time, especial attention was also given to the compensation of those who could stand to lose from reform.

This kind of practical, non-ideological focus has not always characterized the recommendations made by the international community. In relation to economics, supposedly universal "first principles" have at times taken prevalence over a good understanding of the actual institutional constraints faced and the way in which markets are organized on the ground. On issues related to regulation, some recommendations seem to be shaped by the donor's own legal tradition, which in spite of all the caveats is treated as preferable to the alternatives. Even regarding citizen's rights and participation, there is some difficulty to think of "democratization" as something potentially different from adopting a Western political system. Regardless of whether donors are right or not regarding those first principles, legal traditions and political systems, new ideas packaged this way could look too far removed from the needs and concerns of Vietnam. As a result, they could fail to receive serious consideration.

Those leading the “fence breaking” experiments also paid especial attention to the decision-making process underlying policy reforms. They cautiously identified who among the decision makers could be more receptive to an innovation, and who held an implicit veto power over its scaling up. For instance, for some the most significant initiatives, such as reforming the financial sector, the Politburo needs to give its approval. And there is a preparation process leading to the discussion. Conveying the right message is thus not enough; the message also needs to be delivered to the right place. This is again an area where the successes and failures of the last two decades carry important lessons for the international community. Often, massive technical assistance was provided by donors to government units that had no authority to decide on the proposed reforms, and no real inclination to support them either.

The international community may also need to learn patience. There may be no action on a specific reform initiative until consensus is reached among the key players in government and in the Party. If so, donors could be well advised to adopt the “wait and see” approach, as did so many times those leading the “fence breaking” experiments. Banging on the table may not do much to speed up matters, while it may deteriorate the relationship with government, and reduce the opportunity to contribute once the decisions are made. A natural complement of patience is comprehensiveness. Which initiatives will move fast and which will stall is seldom clear, even for insiders. Being able to provide substantive inputs across a range of policy areas increases the chance of supporting change, wherever it happens.

Conclusion: Sustaining Reform in the Next Decade

The consensual mechanisms that allowed Vietnam’s transition from plan to market, and from poverty to middle-income levels, should continue to support its transformation past that stage, into becoming an industrial country. Seeking new ideas to improve economic management, finding ways to build consensus around them, and compensating those who could stand to lose from their adoption, should go a long way in that direction. However, adjustments may also be needed, so as to address the emerging challenges brought by two decades of rapid economic growth and social transformation.

The risk of losing control over economic developments, stemming from increased financial integration and the uneven progress of reform across policy areas, requires a rapid upgrade of the government’s technical capacity.

The traditional approach to policy reform, which included piloting, assessing the results, building consensus, and scaling up, would be useless in the event of a financial crisis. The measures needed to support global integration, banking supervision, the regulation of infrastructure, environmental protection, or health sector reform, are basically technical in nature. The commitments made

in the process of WTO accession, or the accounting and auditing standards needed to support business transparency, build on an enormous body of internationally accepted standards and norms. Assessing the options to set the price of electricity, or to compensate health care providers, requires sophisticated microeconomic analysis.

All the creativity of “fence breaking” experiments would be insufficient to move into these new areas. The search for consensus, while making policy reversals more difficult, could now lead to missed opportunities and excessively slow reactions. The “wait and see” approach, which helped minimize conflict, would entail massive costs when a crisis needs to be averted, or addressed.

Competent policy units in line ministries and regulating agencies, well-staffed think tanks able to conduct solid policy reviews, and strong economic departments in universities will be increasingly needed to identify the most promising measures and conduct a rigorous evaluation of their outcomes. But the experience of think tanks in the run up towards Doi Moi should be considered in this respect. Then, the most useful knowledge did not come from official institutes, staffed with researchers chosen on the basis of their political loyalty and their ability to interpret the views of the leadership. Unofficial think tanks, involving true experts, made a more important contribution. In the same spirit, the upgrading of the government’s technical capacity should be based on principle of excellence, mobilizing talent from all quarters.

Strengthening the technical component of economic policy will be all the more important as powerful interest groups start to emerge. Until quite recently, the Party was the only real power in Vietnam. Moreover, almost everybody stood to gain from reforms, and determined efforts went into compensating the few who would not, so that there was little economically-motivated maneuvering to influence economic policies. At most, there was procrastination in their implementation. However, the very success of reforms has created several influential economic units that would benefit if further reforms were not adopted. Among them are the large “economic groups” supposed to become Vietnam’s economic champions. These groups would benefit from retaining dominant positions in their sectors, and they would also be keen to mobilize financial resources in questionable ways.

Unlike the potential losers of the earlier phases of Doi Moi, these groups have the clout to articulate and convey their preferred policies in ways that make them look as serving the public interest. Lobbying of this sort is common in most countries, industrial and developing alike. If anything, Vietnam was an exception, due to the overwhelming weight of the Party in the decision-making process. But as interest groups emerge, the government needs to have the capacity to scrutinize their claims on technical grounds, so as to make sure that public goals are not undermined.

The risk of social resentment in the face of growing inequality requires measures both to preserve social inclusion and to fight corruption, and the

government is clearly moving in these two directions. But the magnitude of the challenge is such that success cannot be taken for granted.

There are now effective mechanisms in place to massively redistribute government revenue from richer to poorer provinces, and that should help. However, financial resources alone may not be enough for the living standards of ethnic minorities to catch up with the rest. Policies taking into account the cultural specificity of these groups, from the collective cultivation of land to the use of forests as public goods to the reluctance to pursue formal education, still need to be developed. This is easier said than done, unfortunately, and nobody seems to have workable solutions to rapidly lift ethnic minorities out of poverty.

The growing diversity of stakeholders also makes it more difficult to identify losers from policy changes and external shocks, and to set up effective mitigation mechanisms. In the past, creating opportunities for the directors of SOEs to benefit from liberalization and privatization, and providing cash compensation for redundant SOE workers, was enough to ensure a reform without losers. Today, there is uncertainty as to who exactly will be affected by the commitments made to access the WTO, or by fluctuations in international prices. In the presence of such uncertainty, an insurance approach is warranted. Setting up universal mechanisms effectively providing protection to all households, regardless of the source of the shocks they face, will be essential to preserve social inclusion, and with it the support for further reform. A modern social insurance system would then be the substitute for the more targeted compensation mechanisms used over the last two decades.

The risk of facing social resentment would be aggravated if some of the emerging fortunes were seen as ill-acquired. From this perspective, containing corruption is an urgent priority and the government is taking determined steps in this direction. Eliminating red tape, increasing financial transparency, strengthening administrative systems, processing complaints and denunciations, monitoring the assets of senior civil servants and their immediate families, and regularly assessing popular satisfaction with government agencies are all steps in the right direction. However, in a booming economy the opportunities for corruption may expand more rapidly than the capacity of the government to contain it. Even determined efforts could fail to offset the perception of widespread corruption, regardless of whether it is justified or not.

In practice, an effective fight against corruption may require more room for independent reporting and criticism. Subordinates or colleagues of a corrupt civil servant may know more about the specifics (which modalities, which assets?) than officials from a watchdog government body, no matter how diligent. Those asked to pay bribes in exchange for services, or losing business opportunities because others paid bribes, may be in the best position to uncover the wrongdoing. Journalists may be able to investigate and cross-check popular gossip, helping to either defuse it or to provoke a response through appropriate administrative or judiciary channels. But for these more independent

mechanisms to work effectively, the government needs to adopt a less defensive stance. Some defamation and unjustified criticism could be the price to pay for this increased openness. But the potential benefits probably outweigh the cost.

This sort of increased openness would also help defuse the third major risk faced by Vietnam as it joins the group of middle-income countries, namely the possibility of turmoil prompted by groups (no matter how small) who feel alienated.

In practice, this would require gradually strengthening citizens' rights. The Vietnamese government has been better than most developing country governments at delivering social services and improving the wellbeing of the population. But it has also tended to be more defensive than others when, for any reason, the supposed beneficiaries do not feel satisfied, and voice their grievances. This should not come as a surprise. The fight against French colonialism first and then against American invasion had prompted a neglect of the law. In a process that was common to other, newly independent countries, the government ruled by decree. No objection to administrative orders was permitted, legality became more of a formality, and even the Ministry of Justice was eliminated until 1981.

Nowadays, there is a clear reversal of this trend, with the enforcement of the rule of law as one of the main objectives of the reform process. Specific measures are being adopted that should strengthen the ability of citizens to convey their views, and seek redress if needed. They include the shifting of increasingly larger responsibilities to the National Assembly and People's Councils, as well as the emphasis on "grassroots democracy" at the commune level. Meanwhile, a clear vision has emerged in relation to legal and judiciary reform, and it clearly goes in the right direction.

However, as for the fight against corruption, effective implementation will take time, and meanwhile some turbulence can be expected. Additional initiatives could be considered to mitigate such possible turbulence, including experiments with new feedback mechanisms from society to state. Strengthening the capacity of the National Assembly (in particular, its specialized committees) and enhancing its role in the drafting of laws would be one such initiative. In the same spirit, People's Councils should be better able to exercise their oversight functions, especially in relation to budgetary allocations. On the judicial front, upgrading legal aid services and effectively processing administrative complaints would help as well. At some point, increasing the number of candidates participating in elections for the National Assembly and allowing referendum initiatives at local levels could help channel the growing diversity of views through the system, rather than outside of it.

In sum, the decision-making processes of Vietnam might be the main reason why the country has done so well, constantly identifying obstacles, seeking solutions, and building consensus around them. Those processes should also help Vietnam move into its next phase of development and become a middle-

income country. However, their very success has resulted in fundamental changes in the Vietnamese economy and society. To address these changes, the decision-making processes may need some adjustment too. Reinforcing the capacity of an independent technocracy, allowing more openness in relation to corruption, or strengthening the rights of citizens may hold the key for Vietnam to sustain its success and become an industrial country within a generation.