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Economic development in a rent-seeking society: socialism, state capitalism and crony capitalism in Vietnam

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ABSTRACT

This article explains Vietnam's economic growth and industrial development despite the strong rent-seeking features of its economy. We employed three analytical rent-seeking models to assess three industries: textile-garment and telecommunications, both under a state capitalist system with varying degrees of state control, and the motorcycle industry developed in a crony capitalist manner. Our cross-industry analyses demonstrate how a developing country such as Vietnam overcomes pervasive rent seeking to achieve growth outcomes. Under conditions of controlled economic reform, the Vietnamese government managed rent seeking using various measures of state intervention coupled with gradual market openness in the industrial sectors.

RÉSUMÉ

Cet article explique la croissance et le développement industriel du Vietnam en dépit de l'intensité des activités de recherche de rente qui caractérise son économie. Nous avons défini trois modèles analytiques de recherche de rente pour évaluer trois secteurs industriels : le textile et les télécommunications, deux industries fonctionnant dans un système capitaliste d'État avec divers degrés de contrôle étatique, et la production de motocyclettes, industrie développée sous le mode du capitalisme de connivence. Nos analyses transversales montrent comment un pays en développement comme le Vietnam arrive à surmonter une recherche de rente généralisée pour obtenir des résultats de croissance. Dans un contexte de réforme économique contrôlée, le gouvernement vietnamien a géré la recherche de rente en utilisant diverses formes d'interventions étatiques couplées à une ouverture progressive du marché dans les secteurs industriels.

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Introduction

This article provides an in-depth perspective on the political economy behind Vietnam's economic and industrial development since its economic reform in 1986. Vietnam is a politically centralised country with a population of over 90 million people governed by only one party – the Communist Party of Vietnam. This makes Vietnam significantly different

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from other development cases in the region, such as South Korea, Taiwan and Singapore, in which state controls are intimately linked with a dynamic private sector (Amsden 1989; Wade 1990). Moreover, economic reform in Vietnam was not driven by factors such as benevolent authoritarianism, as it is sometimes assumed to have happened in South Korea, Taiwan or Singapore (Amsden 1989; Wade 1990; Przeworski and Limongi 1993; Means 1996). As such, Vietnam illustrates a development model in which a politically authoritarian and centralised regime operates under the political constraints created by efforts to reform the economy.

This "model" was not the result of a well-elaborated plan. Vietnam's political leaders scrambled to find solutions and maintain power in the face of post-war reconstruction in the late 1970s and economic crisis in the mid-1980s, which was further exacerbated by the early 1990s demand shock (Appendix A, Supplemental online materials). But the results of their improvisations have been relatively successful, both politically (they have not lost power) and economically. Vietnam has recently experienced high growth, with its GDP per capita tripling over the past three decades (Figure B1, online Appendix B). Even if one may suspect that part of this growth is government-distorted malinvestment, the success still cannot be denied.

Because of political centralisation, Vietnam looks like a hard case – it is a country where one would not normally expect liberalising reforms to go through.[1] For example, as argued by Nye (1997), authoritarian leaders voluntarily implement genuine institutional reforms only when they can be convinced to give up long-term power in favour of short-term benefits. This has not been the case for Vietnam, as political leaders have tried their best, and so far succeeded, to maintain their power despite the challenges. Vietnam remains a one-party system and a nominally socialist state. Similarly, as argued by Moberg (2015), one should be sceptical of "reforms" introduced by centralised authoritarian regimes, as they tend to be a cover for rent-creation and redistribution. Our narrative about Vietnam economic development does not challenge this idea per se. By various important measures, the country is still very far from a liberal capitalist model and it is undoubtedly still best described as a rent-seeking society. For example, the Heritage Foundation (2015) gave Vietnam a low rating (30) for investment freedom in Vietnam in the 1990s and 2000s, and an even lower rating (15) in recent years. Similarly, the protection of property rights is almost non-existent (in the range 10–15). That being said, its growth is not entirely mysterious. Institutional changes underlying growth have been substantial: trade freedom gradually grew from 44.6 ("repressed") in 1995 to 78.6 ("mostly free") in 2015, and business freedom increased from 40 ("repressed") to 60 ("moderately free") in those years (Heritage Foundation 2015).

Vietnam thus presents an interesting development case study of how growth can happen in a rent-seeking society, a subject of substantive interest among economists and one that is still far from being well-understood (Khan and Jomo 2000; North, Wallis, and Weingast 2009; Gray 2013; Ngo 2016). Furthermore, Vietnam showcases how different areas of the economy can operate under different economic systems. A common assumption in the comparative systems literature is that institutional changes only occur from one type of system to another type.[2] However, this need not be the case. Different types of economic systems should be understood as theoretical models, and economic reality can be, and often is, a superposition of these models, i.e. different sectors of the economy are best described by different theoretical models (Aligica and Tarko 2015, 19). In this context, our research question is twofold. First, how do countries achieve growth and development in the condition of pervasive rent seeking among various political and economic interests? Second, what are the mechanisms or economic systems that characterise Vietnam economic development since the country's economic reform in 1986?

We describe three sectors of the Vietnam economy – textile-garment (T&G), telecommunications and motorcycle – and explain why they operate under different rent-seeking systems (see Table 1, in the Conclusion). Three case studies illustrate the various mechanisms that enabled Vietnam's successful economic transformation and reform. It is this kind of superposition of different types of economic systems that explains the specific details of the dynamic of economic transition and of the attempts by the political elites to spur development without losing power. The industries are selected based on their distinct patterns of development, which we detail in the case studies. In addition, these are the industries that play a crucial role in different aspects of Vietnam's development since the 1990s. They laid the bedrock for Vietnam's participation in the global market (T&G), the revitalisation of the industrial sector in the contemporary period (motorcycle) and the construction of crucial infrastructure for the economy (telecommunications). The empirical research is based on historical, political and economic evidence from each industry's development. We collected qualitative data in five provinces of Vietnam during three periods of fieldwork, which totals eight months between December 2010 and June 2012. A total of 68 semi-structured interviews were conducted with government officials, firm managers, component suppliers, workers and industry experts during these field trips. The interviews were 1–3 hours long. We returned to Vietnam to update and crosscheck our data in June–July 2016. All qualitative data presented in this article was triangulated and crosschecked either with other interviewees or with existing literature on the issue. We also make use of recent literature that adds insights to the latest and relevant changes in the industries.

Theoretical models of rent-seeking societies

Rent-seeking societies are highly regulated economies in which entry in various markets is politically restricted across a wide-range of occupations and businesses (Buchanan, Tollison, and Tullock 1980; Congleton and Hillman 2015). The effect of these restrictions is to create rents for the incumbents, by protecting them from competition. As a result of the possibility to earn such rents, for example, artificially high profit margins or earnings, individuals and firms spend resources bidding for access to those rents. The system looks like an "all-pay auction" (Hillman 1988).[3] This bidding process is known as rent seeking. Several different economic systems have been modelled as rent-seeking societies: classical mercantilism, real-life socialism, state capitalism and crony capitalism (Aligica and Tarko 2015). All of these systems rely on rent seeking to distribute the rights to earn profits, but they differ in terms of their institutional details and their legitimising ideologies. The classic mercantilist and the real-world socialist models are the most strictly controlled, in which all production is constrained by monopoly rights. The state capitalist model is more liberalised, allowing genuine markets to exist everywhere except in the realm of the "commanding heights" of the economy, which are used to satisfy political goals. The crony capitalist model accounts for weak states, which do not or cannot offer credible and universal protections to contracts and property, but offer credible protections to some via crony relations. Real-life socialism, state capitalism and crony capitalism are particularly relevant for our case studies.

In theory, *socialism* implemented the Marxist economic doctrine, which was used to legitimise the regime. In practice, it operated as a neo-mercantilist regime (Levy 1992; Anderson and Boettke 1997). As noted by Anderson and Boettke (1997), central planning created production ceilings. Because these ceilings cause various shortages throughout the economy, they also create positions of power to distribute the right to access various resources. In turn, this system leads people to bid for privileges and positions of power. In other words, managing an economy by central planning creates a rent-seeking society. As a socialist economy, Vietnam used to fit this model. The transition we are describing should be understood as moving from a full-scale rent-seeking society created by real-world socialism, toward a more developmental version of a rent-seeking society.

When socialist economies failed to stimulate growth and development, some of them, China and Russia most prominently, transformed into *state capitalist economies*, rather than into Western-style open market economies (Bremmer 2009). While liberalising to some extent, state capitalism relies on institutions such as "national champions" and state-owned enterprises (SOEs), usually legitimised by appealing to security concerns and nationalism. In the case of Vietnam, the SOEs were also tasked with job creation and retention for the purpose of maintaining the basic social fabric of the economy and legitimising the role of the Communist Party.

By allowing market prices to exist (albeit often heavily modified by various regulatory policies), state capitalism can be more efficient than real-life socialism. This is true even for state enterprises. For example, Ngo (2017b) points out that in the face of credible competition even state enterprises are forced to operate more efficiently. Moreover, state capitalist enterprises are often used to return additional revenues to the states (Bremmer 2009), which make efficiency concerns even more prominent. Traditionally, states obtained revenues from taxes, monetary expansion or borrowing. One of the important state capitalist innovations is that the state would also obtain some revenues from profitable state enterprises. These are either sovereign wealth funds, which operate in international markets, or state enterprises, which are profitable thanks to being granted monopoly status (for example, telecommunications services).

Crony capitalism is sometimes understood as a negative tendency within advanced capitalist systems. We are referring here to a different usage of the term. Crony capitalism is also understood as a type of economic system, characterising countries such as the Philippines, Indonesia and many South American countries. As described by Haber, Razo, and Maurer (2003) and Aligica and Tarko (2015), this is a rent-seeking system offering a second-best solution to the problem of weak contract and property rights protections. When property rights are not protected, investment and capital accumulation (either foreign or domestic) are weak; hence, development is slow or non-existent. Crony capitalist countries, while lacking universal property rights protection, do protect the property of well-connected individuals. This often happens because there is an overlap in family ties between the property or business owners and the political elites – hence the "crony" qualifier (Haber, Razo, and Maurer 2003; Aligica and Tarko 2014). The result of this selective property protection is that investment and development can occur, via these selective paths, but inequality and corruption are prevalent.

Such rent seeking is also often associated to foreign investment, as foreign investors need to establish political connections and secure political privileges in order for their intellectual property to be protected. As we shall see, this is indeed what has happened in Vietnam in the motorcycle industry, as Japanese firms managed to form the necessary political connections while Chinese firms did not. However, this situation is still better than the alternative "natural state" in which no one's property is secure and no development occurs (North, Wallis, and Weingast 2009).

As noted by Aligica and Tarko (2015), while a theoretical model of an economy system is defined by a given set of features, "real-life cases are *superpositions* of those clusters of features" (emphasis in the original) and "one has to decide which feature is the strongest and most salient one, considering that it is often the case that all features are present" (16). They conclude that one can identify a real-world case with just one of these theoretical models "only in the sense that it is that combination [of features] which predominates and is the most salient". However, as our case study illustrates, different areas of the economy manifest clear features of different models. Hence, we need to revert to the idea that a real-world example is a superposition of the theoretical models. Otherwise, we would end up with a situation in which "saliency remains a matter of interpretation and the entire discussion remains a matter of methodological dispute" (Aligica and Tarko 2015, 16).

In the remaining part of this article, we employ the analytical rent-seeking models discussed in this section to assess three industries: textile-garment and telecommunications industries, operated under a state capitalist system with varying degrees of state control and intervention, and the motorcycle industry, developed in a crony capitalist manner.[4]

The textile-garment industry: state capitalism as a controlled transition method

The development of Vietnam's modern textile-garment industry started in the late 1970s when Vietnam largely traded with other Communist countries. During this period, guaranteed market shares removed any incentive for innovation, industrial upgrade or development for producers. Although production was steady, the industry overall lacked knowledge in high-end production, marketing skills and knowledge in international distribution. In 1986, the government initiated a series of economic reforms. By the early 1990s, the Communist-style production model was replaced by low value-added operations set up by foreign investors to take advantage of the country's cheap labour cost. Some of the earliest investors came from within the region, such as South Korea and Taiwan. These investors played numerous roles in the international market as producers, exporters and global trading houses for garments produced in poor countries. In Vietnam, they manufactured garments in their own facilities – there was no foreign–local cooperation – and exported ready-made garments back to their home countries or directly to international buyers. Vietnam's abundant numbers of low-skilled labourers were initially offered low wages, thus foreign investors did not need to bid up wages. Hill (2000) argues that the economic reform led to a major "shake out" of the industry, especially the SOEs that had been exporting to the Communist bloc. The government's gradual withdrawal of subsidies caused state-owned textile factories to scramble to compete with both foreign and private entrants. Hill's observation was confirmed by our interviewees during fieldwork in 2011, with a number of them detailing similar experiences.

In the beginning, Vietnamese private and public T&G enterprises had limited success with direct export to foreign buyers, and the large export shares were organised and controlled through foreign trading houses (Hill 2000). As a result, the highest value and profit from exports were captured in Taiwan and South Korea, rather than within Vietnam. The sector's weak competitiveness is due to the heavy reliance on Vietnam's factor endowments (low-skilled labour, cheap land, preferential tariffs) and foreign inputs (fabrics, design, expertise) (Nadvi et al. 2004). Compared to the major apparel producers in Bangladesh, China and India, the T&G industry in Vietnam is a late developer, having only achieved critical mass to compete internationally starting in 2000. Between 2001 and 2013, T&G exports increased over nine times, from USD 1.9 billion to USD 17.9 billion (Figure B2, online Appendix B). Vietnam's largest export markets are the US (post-embargo), the European Union, Japan, South Korea and the Association of Southeast Asian Nations (ASEAN) (Figure B3, online Appendix B). In 2016, Vietnam was the second largest T&G exporter to the US, after China. It is the second biggest T&G exporter to Japan, and the eighth largest T&G exporter to the European Union (World Integrated Trade Solution 2017).

Although private and foreign investment has been permitted since the economic reform, the government controls a large market share via the SOEs. This allows the state to create and capture rents through regulations and export activities. Therefore, rent-seeking among well-connected investors, SOEs and government officials was frequent, especially during the 2003–2006 period when the US imposed quotas on Vietnamese exports (Ngo 2017a).[5] However, this did not lead to all-out rent capture because the central government was acutely aware that the T&G industry plays an important social role in the Vietnamese economy. The industry is one of the largest formal employers in Vietnam, providing jobs to more than two million workers. In addition, approximately 1.3 million jobs, or 10 per cent of employment, is in or related to the industrial sectors (Dam and Barbour-Lacey 2015). As the T&G industry employs a large section of the Vietnamese population, job creation is traditionally seen as helping to maintain social stability, particularly in the rural and mountainous areas of the country.[6] Through SOEs, the government has also created jobs in cotton production, of which Vietnam was an exporter until recently.

Due to the industry's important contribution to employment, which ensures stability of the political regime, the Vietnamese government has often sacrificed efficiency to ensure employment.[7] As the Vietnamese economy grew and inequality widened, the government pressured the SOEs to maintain jobs in the sub-sectors, despite the fact that some state-owned producers were suffering losses and were less productive than the private sector (Ngo 2017a). For instance, while some SOE managers wanted to opt out of cotton production, thereby reducing employment, the government decided that the goal of preventing short-term unemployment and maintaining some basic income for the poor in the remote and mountainous regions of Vietnam, where cotton is cultivated, was more important.[8] This is a typical example of state capitalist policy at work, in which efficiency considerations take second place behind social and political considerations.

To better understand this managed transition, we need to look more carefully at the differences between the textile and the garment sectors, and the shift between them.

They have quite different structural features (Table C1, online Appendix C). By its nature, the textile sector is capital-intensive and dependent on both economies of scale and experience in technology management. Vietnamese producers are weak on both criteria. For instance, an interviewee at Vietnam Textile and Apparel Association (VITAS) explained that it requires, on average, USD 15 million in investment capital to establish a dyeing factory that could produce 10 million metres of fabric (interview, Ha Noi, June 2011). This is a large sum of investment capital that is not accessible for most private producers given Vietnam's under-developed credit market. The textile sector also suffers from limited skilled workers (Nghi 2011). The garment sector, by contrast, is a consumer-oriented industry where advanced technology and significant capital investment are not required. Knowledge of international marketing channels, attention to quality control, management of stocks and capacity to reliably deliver outputs are far more important in this sector. When interviewed, an expert representing the Association for Garment Textile Embroidery Knitting (AGTEK) explained that because learning to make garments requires less time and effort, it is easier to hire and train new workers. Thus, producers could stay flexible with fluctuation in consumer demand.[9]

In essence, the textile sector's history (serving rigid Communist markets), its structure (being both capital and technology intensive) and the government policies (removal of subsidies and allowing for foreign imports) had undermined the development of the local textile sector after the relative liberalisation of the industry. Nonetheless, social unrest was avoided as the workers from the diminishing textiles industry could slowly move toward the garment industry and other sectors. Consequently, during the 1990s the textiles industry in Vietnam started to shrink. By 2011, it was down to approximately 27 per cent of the overall T&G industry (Le 2011). Nadvi et al. (2004) show that, between 1989 and 1999, employment created in the garment sector was more than triple the job loss in the textile sector. Given the government's concerns over social and political stability, the expansion of the garment sector more than compensated for the job losses due to the decline of the textile sector.

The Vietnamese government managed successfully not only a gradual transformation of the T&G industry, but also a moderate decline in the overall importance of the SOEs. Until recently, centrally controlled SOEs accounted for the bulk of product output and were much better capitalised than the smaller, locally controlled SOEs.[10] However, the number of the former SOEs is decreasing due to the gradual privatisation (locally called "equitisation") as part of the government's commitment to the World Trade Organization (WTO). By 2009, SOEs declined to 1–2 per cent of the total number of T&G enterprises, but still employed a large number of workers (26,381 employees in 2014). The most common types of firms in the industry (76%) are now joint stock, private companies and limited companies, some of which also have state capital.[11] In addition, foreign-owned firms made up 18 per cent of total enterprises in 2009 (Le 2011).

As Vietnam industrialises, the economy attracts workers away from the T&G industry and creates pressure to increase wages (Goto, Natsuda, and Thoburn 2011). But such wage increases are not possible unless the industry becomes more efficient. This partly explains the high performance of the garment sector in recent years. For example, there has been productivity improvement together with high export volume and gradual upgrade along the global value chain. Some Vietnamese garment producers improved their production modality from Cut-Make-Trim (now 70% of total production) to Free-on-Board and above (30%) (Nguyen 2017).[12] Furthermore, a notable group of domestic garment producers have since been upgrading by switching part or all of their sales to the local market (Goto 2014). This is important for advancement because the local market requires the producers to perform more functions, such as developing their own brands and marketing their in-house designed products rather than engaging in simple Cut-Make-Trim assembly for foreign buyers (Goto 2014). From a market-based perspective, this seems like a straightforward structural adjustment process, similar to what happened in Western Europe in the nineteenth and early twentieth century. However, from the Vietnamese government's state capitalist perspective, restructuring and liberalisation bring about many political unknowns, which is why they have acted to prolong and slow down the transition using SOEs as stabilisers for jobs and basic income. Gradually, market competition and important upgrading emerge but in a state-controlled fashion. We do not dismiss the substantial rent-seeking activities that occurred during the reform period. However, our model and empirical analyses substantiate an important insight: the state capitalist model was employed, which was advantageous for the Communist leaders by allowing the government to create, control and manage rents such that the T&G industry transitioned towards greater economic efficiency, while providing jobs to the population and retaining the structure of the one-party regime.

The telecom industry: state capitalism in a state-controlled duopoly market

Similar to the T&G industry, the telecommunications industry developed and industrialised in the state capitalist manner, though with important variations. In a little more than a decade and half, this industry transformed from a state-run monopolistic market to a duopoly market with two major state-owned industry leaders and nine small telecom operators in 2013 (Ministry of Information and Communications 2014, 59).[13] During the early development of the industry, the state maintained tight control of entry through licensing and allowed few SOEs to lead the industrial transformation. Vietnamese leaders asserted the need to retain firm control over the telecommunications industry in order to protect the nation's security and stability, which was primary to their concerns.[14] Between 1975 and 1995, the industry was organised based on the real-life socialist model that incorporates central planning, price fixings and strict state regulations. The General Department of Post, Telephone and Telegraph (PTT), a government unit, was responsible for all aspects of postal service and telecommunications, including implementation of policies and provision of services to government offices and private consumers. In 1990, Decree 115/HDBT transformed PTT into Vietnam Posts and Telecommunication (VNPT) – a general business corporation owned by the government (Ministry of Information and Communication 2010).[15] This decree effectively created a state-owned monopoly in the telecom industry.

VNPT inherited substantial monopoly rent, exercised monopolistic power and reaped profits from a lucrative market with no competition. In addition, there was no credible political pressure or institutional mechanisms to compel VNPT to upgrade its infrastructure and management abilities.[16] As a consequence, the Vietnamese economy experienced low telecommunications penetration rate, mainly due to high tariffs, slow service and a weak infrastructure. Ngo (2017b) describes VNPT's failure to industrialise:

> [I]n 1995, only 4 in 1,000 consumers had a telephone line, and there were only 23,500 mobile connections throughout Vietnam … The telecom network was described as "outdated" and the Internet was not available for residential use … A consumer and a business owner in Ho Chi Minh City explained that it took VNPT up to one month to install a fixed phone line for a business or household in Ho Chi Minh City in the early 1990s … In addition, VNPT's tariff rates were high, making phone service too expensive for the majority of the population. In 2001, tariffs for international service in Vietnam were USD 2.00–2.30 per minute, more than twice the price of the same tariff in 2003 when Viettel offered international service at roughly 75 cents per minute.

In 1995, Vietnam joined ASEAN and normalised its trade relations with the US. This initial integration eventually led Vietnam to sign a bilateral trade agreement (BTA) with the US in 2001. The BTA contained an important provision that set the schedule to gradually liberalise the Vietnamese telecommunications industry. Subsequently, the government officially abolished VNPT's monopoly in 1995 and slowly opened the sector to competition, especially among state-owned conglomerates, for all telecom services. In the same year, Comvik Group, a Swedish telecom operator, signed the first business cooperation contract[17] with VNPT, forming MobiFone, the first mobile phone network in Vietnam. This cooperation marked a milestone in the industry's development (Ngo 2017b). Nonetheless, VNPT's monopoly officially ended only when the military-owned SOE, Viettel, received a commercial license to enter the telecom market in 1995.

It took Viettel five years of preparation to provide the first telecom service to Vietnamese households. Starting in 2000, Viettel offered long-distance service within the country using Voice Over Internet Protocol technology. After one year, the service was extended from in-country service to international service (Cheshier 2010). Thriving on its initial success, Viettel expanded to provide Internet service in 2002. It launched a mobile phone service – the most profitable segment of its business – in 2004. Since its inception, Viettel has consistently experienced high growth rate measured by revenue, profits and subscriber numbers in all segments of telecom service (Ngo 2017b). In 2009, the government's Decision 2097/2009/QD-TTg officially made Viettel a state-owned general corporation, a legal status that gives Viettel preferential treatment and recognition in the state sector equal to that of VNPT (Korea Research Institute and University of New South Wales 2015).[18]

There were some major factors that supported Viettel's effort to successfully penetrate the telecom market, update its industrial capability and resolve critical market failures. First, as a latecomer, Viettel had to overcome VNPT's market dominance by quickly acquiring knowledge, technology and expertise to compete with VNPT in price and quality. Second, the government supports of Viettel were implicitly conditioned on performance, which required a high degree of learning effort by Viettel. Third, the Ministry of Defence, Viettel's managing ministry, was also politically powerful and autonomous within the government, which provided Viettel a stable and dependable macro political environment to focus on technical learning and capacity building. In addition, the Ministry of Defence also supplied Viettel with important resources such as land, labour, infrastructure and access to finance, some of which were in exclusive control of the Army. This allowed Viettel to solve a number of market failures that were experienced by other operators who faced similar critical constraints.[19]

There was also skilful business management in cost savings, recruitment of highly skilled and committed engineers, vertical integration between telecom service and device manufacturing, and flexible trial-and-error business strategies. The highly successful business tactics were largely thanks to Viettel's two prominent leaders – General Hoang Anh Xuan and General Nguyen Manh Hung – both of whom previously led the telecommunication department in the Ministry of Defence. Finally, Viettel leaders were also aware of the upcoming international competition, as the industry's protection period under trade treaties were being phased out and terminated in 2015.[20] The short period of protection pressured Viettel to quickly learn new technology, update its capability and establish market dominance in the Vietnamese market before foreign competition set in.

Within a decade and a half, Viettel achieved immense industrialisation and market access. Its total revenue increased rapidly (Figure 1) and reached USD 9.38 billion in 2014, only 14 years after Viettel launched the first service (Lao Dong 2015). Meanwhile, VNPT reported its earnings at just over half of Viettel's in the same year – approximately USD 4.78 billion (Minh-Tuyet 2015). By the mid-2010s, Viettel became the fastest growing and the most powerful state-owned general corporation in the industry.

After a period of intense competition among the state-owned providers, by the early 2010s, Viettel and VNPT formed a duopoly in the telecom industry. They captured 93 per cent the mobile phone market – the largest subsector within the telecom industry (Figure B4, online Appendix B). The duopoly also led the market in all other subsectors including Internet, fixed phone lines and 3G data services. Along with the rise and success of Viettel, the telecommunications industry experienced some notable industrial development. First, the industry experienced an average growth rate of approximately 17 per cent per year from 2006 to 2013 and continued to grow in subsequent years (Figure B5, online Appendix B). By the end of 2000s, use of main telephone lines in Vietnam had increased fivefold – from 4 per 100 inhabitants in 1995 to 20 per 100 in 2009 (Nguyen, Pham, and Gullish 2005; Ministry of Information and Communications 2014). In the four years from 2009 to 2013, Vietnam also experienced a major surge in

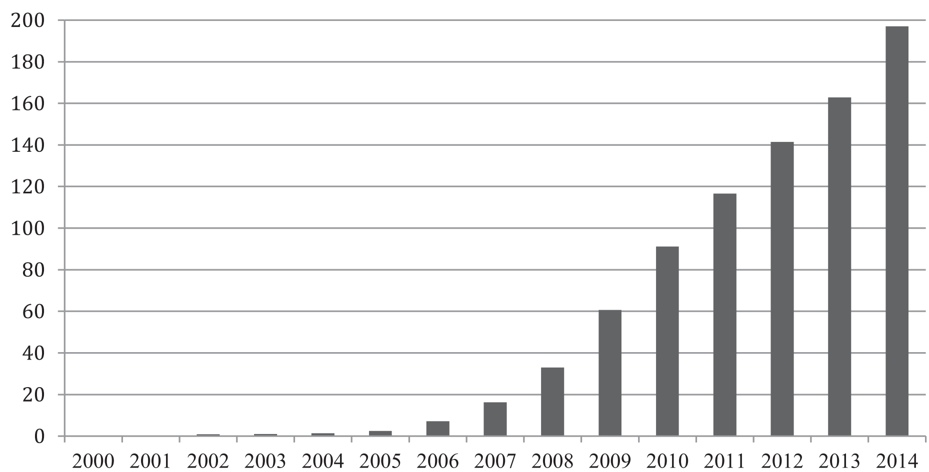

Figure 1. Viettel's revenue 2000–2014 (in VND trillion).
Source: Ngo (2017b, 465).

the use of 3G service that contributed to the country's per capita growth (Deloitte 2012). In 2014, Vietnam ranked twelfth in telecom revenues and twentieth in mobile Internet penetration in Asia Pacific (Euromonitor International 2015).[21] In the same year, mobile phone penetration was recorded at 89 per cent – a substantial improvement from 74.9 per cent in 2009 (Euromonitor International 2015).[22]

Finally, while Vietnam was a technology importer before 2000s, it started exporting telecom equipment and service in the 2010s. In the 2010–2012 period, the industry's export revenue of telecom service increased approximately 38 per cent, from USD 576 million to USD 794 million (US Commercial Service 2012). In addition, exports of telecom equipment also grew by 94 per cent from 2010 to 2015 (US Commercial Service 2014). (For Vietnam's high growth rate in exports of telecom equipment, see Table C2, online Appendix C.)

Viettel drove much of this export growth during the post-monopoly period because it was the first provider and manufacturer to export telecom service and equipment abroad. It also led the industry in the area of research and development, and pressured VNPT to upgrade its domestic infrastructures. In sum, the telecom industry transformed from a state-owned monopolistic market between 1975 and 1995, to a competitive market with 11 service providers during the 2000s, to an oligopoly market dominated by two major state-owned operators beginning in 2010s (see Figure B4, online Appendix B).

In a state capitalist manner, both Viettel and VNPT were legitimised and structured as the "national champions" to lead the industry's development on the basis of security and stability. Although private and foreign operators were allowed to invest jointly with local firms in the market after 1995,[23] the structure of the telecom industry favoured economies of scale and access to important resources such as commercial license, land, telecom frequency, infrastructure and labour. As a consequence, after a period of managed liberalisation, Viettel and VNPT emerged as market leaders holding the commanding height of the industry. In the context that competition within the state sector forced credible learning efforts and performance, national resources were used to compensate for critical market failures in land, labour and infrastructure. Thus, competition within the state sector, especially between Viettel and VNPT, reduced waste and enhanced new learning and technological upgrading. Despite rent creation and rent seeking being pervasive during this period, state operators used rents effectively to support capacity building and compete in a quasi-liberalised market. These behaviours feature the extent to which state capitalism generated growth and industrial development.

While the telecom and T&G industries both conform to the state capitalist model, there are clear differences between them. In the T&G industry, there were far more firms with diversified ownership. In addition, the role of the state was largely to retain jobs and basic income for low-skilled workers to fulfil the objectives of a socialist economy. Meanwhile, competitive markets among private, public and foreign enterprises were forcing productivity improvements among the SOEs, especially in garment manufacturing. The telecom industry, by contrast, experienced strong state control and organised into an oligopolistic market with notable competition between two state-owned conglomerates. Thus, one could argue that state capitalism in Vietnam operates in two modes: state capitalist with the goal of maintaining social orders and job retention; and state capitalist with the primary goal of controlling important industry, protecting national security and profit seeking. These two modes of state capitalism are not exclusive as there are some overlaps, but the objectives and degree to which the state maintains control over these industries led to very different industrial development and growth trajectory for each of the industries.

The motorcycle industry: the crony capitalist development model

The motorcycle industry in Vietnam provides a case study of industrial upgrading predominantly driven by crony capitalism and foreign direct investment (FDI). In the early 1990s, motorcycles was one of the first industries chosen as a strategic foundation for Vietnam's industrial development. In a liberal capitalist system, one does not need permission to start a new motorcycle company. This is not the case, however, in Vietnam. Under socialism, only state enterprises are allowed to produce goods. In the early 1990s, this full-blown socialist policy changed when the Vietnamese government decided to offer licenses to specific private and foreign firms. The licenses allowed them to export to and produce motorcycles in Vietnam. In addition, the government also enacted industrial programmes and provided incentives to attract foreign investors, while it also launched import substitution policies to support local firms (Ngo 2016). The intention was to increase capital investment, technology transfer from foreign investors and industrial capacity of the industry.[24] The policies, in effect, provided rents to local enterprises as well as to foreign investors in order to encourage foreign transfer of technology and know-how.

As a result, during the early 1990s, a few foreign motorcycle makers (the lead firms)[25] and suppliers quickly dominated the Vietnamese motorcycle industry, creating an oligopolistic market for Japanese and Taiwanese producers (Fujita 2007). The government also issued import licenses allowing foreign investors to import complete knockdown motorcycles from abroad. A large number of these motorcycles were second-hand vehicles that were out of fashion in Japan and Taiwan. Others were new motorcycles produced in the home country of the foreign lead firms. The lack of competition in the Vietnamese market provided foreign investors with valuable opportunities to set high prices and gain large profits. Japanese and Taiwanese lead firms also did not need to produce their motorcycles in Vietnam or use local inputs. Hence, the rents captured by Japanese investors did not spearhead industrialisation and technology transfers in this early period (Ngo 2016).

Starting in the late 1990s, in an effort to integrate into the regional and global market, coupled with lobbying of the Japanese embassy and the Japanese Business Association in Vietnam, the Vietnamese government removed a series of protection policies that had previously restricted sales of foreign motorcycles. However, to stimulate industrialisation, the government imposed a local parts requirement set at 40–60 per cent depending on the model. Because of this strict local content requirement, by the end of the 1990s, major foreign motorcycle companies had established manufacturing plants in Vietnam, including global lead firms: Taiwan's SYM and Japan's Suzuki, Honda and Yamaha (see Table C3, online Appendix C). In addition, some Taiwanese and Japanese parts manufacturers followed the lead companies and built plants in Vietnam. They supplied components to the foreign lead firms such as tyres, batteries, brakes, electric components and plastic parts in order to meet the government's local content requirements. Consequently, the majority of local Vietnamese firms did not participate in this production chain and thus there were few technology transfers and spillovers from the foreign production network.[26]

Around the same time, an industrial surplus of motorcycles in China made their way into Vietnam, mostly through the China–Vietnam border. This led to an influx of low-cost Chinese motorcycles in the Vietnamese market. This phenomenon was dubbed the "China shock" by Japanese investors (Ngo 2016). During this period, Chinese and local lead firms falsely claimed local content in Chinese motorcycles, thus allowing them to capture some of the rents that benefited Japanese investors in the earlier period.[27] In 2001, at the height of the China shock, Chinese motorcycle sales made up 80.5 per cent of total sales (Figure 2). During this period, notable industrial development occurred among the domestic firms, as they began to learn and produce components for Chinese motorcycles (Ngo 2016).

After 2002, the Japanese manufacturers successfully pressured the Vietnamese government to enforce its local parts policies and thus recaptured substantial market shares from Chinese–Vietnamese producers. They also introduced the first few low-cost models to attract consumers in the low-income group (Ngo 2016). As a consequence, a number of local assemblers and suppliers that were accumulating new capabilities through contracting with Chinese lead firms went out of business: 35 of the 51 Vietnamese firms surveyed by Fujita (2007) left the industry. This, once again, highlights the difficulty of implementing policies that largely focus on foreign investors while neglecting the development of local firms, which leads to interruptions in their learning and upgrading. The few local firms that survived the market restructuring became lower tier suppliers for Japanese and Taiwanese lead firms.

In the later part of the 2000s, the Vietnamese government made an attempt to further liberalise the economy in anticipation of Vietnam's accession to the WTO. It removed

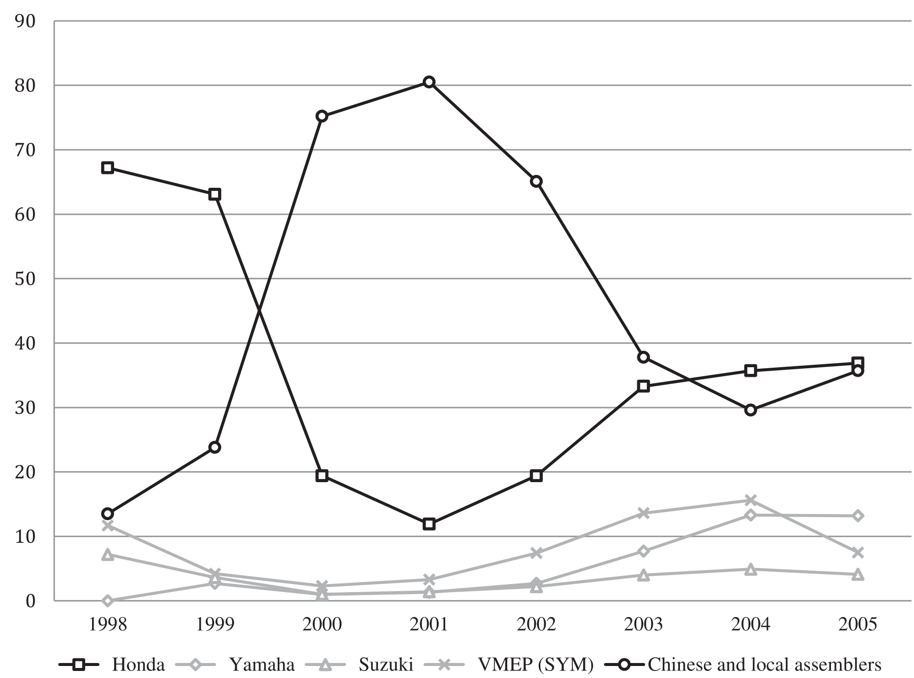

Figure 2. The "China shock": market share of major motorcycle firms, 2001–2005.
Source: Ngo (2016, 19).

prohibitions on motorcycle imports, repealed local parts requirements and reduced tariffs on imported components. Further, regulations on motorcycle registrations were relaxed so that drivers could register more than one motorcycle under a single name. These policies, coupled with Vietnam's rapid development, substantially increased demand for motorcycles. Thus, motorcycle production continued at a high growth rate. In 2011, the Vietnamese motorcycle market sold 3.7 million units and grew 22 per cent from 2010 (The Saigon Times 2012), making it the fourth-largest market for motorcycle sales worldwide, after China, India and Indonesia (Quoc-Hung 2012). It continues to be so in 2015. In 2014, there were 43 million registered motorcycles in a country of 90 million people – that is, almost one out of two people owns a motorcycle. Starting in 2010, major foreign motorcycle makers began to export their production surplus to other markets (Tran 2012). In 2012, the localisation ratio (percentage of parts in each motorcycle to be made in Vietnam) was 70–95 per cent, depending on the brand. In 2014, the industry structure was such that the five largest motorcycle manufacturers in Vietnam (Honda, Yamaha, Suzuki, SYM, Piaggio) controlled roughly 90 per cent of the market share, leaving Lifan (China), Kymco (Taiwan) and Sufat (Vietnam) to split the remaining 10 per cent of the market.

The motorcycle industry is significantly different from the T&G and telecommunications industries in that, while the state tried to control the industry via industrial policies and regulations, it did not use the "state champions" or the state sector to lead the industry. This is partly because Vietnam had weak industrial capacity in the beginning and needed the transfer of know-how and technology from abroad. Therefore, the state maintained weak control while using rent policies to promote industrialisation. However, this FDI-led strategy got mixed up with rent seeking via market access from Japanese and Taiwanese lead firms and fraudulent claims of local content policies by the Vietnamese and Chinese lead firms. These have prevented the industrial policy from working as intended.

The development of the motorcycle industry illustrates both the crony capitalist nature of the process and the impact of international factors such as foreign investors and trade treaties that compel competition and liberalisation. The government's failure to keep out Chinese firms, initially in violation of domestic parts requirements, a symptom of weak state capacity, resulted in market competition between Chinese and Japanese firms and induced cost competition that allowed local suppliers to join the production value chain. However, local firms' learning was cut short as Japanese firms pressured the government to enforce its local parts policies. By giving in to these rent-seeking demands, the government undermined the development of local parts producers. Despite the Vietnamese government's failure to effectively manage rent policies, the industry achieved substantial growth and industrial development after a long trial-and-error process. Our analytical use of the crony capitalist system allows us to understand some of the important factors that drive the industry's success: competing cronyism, market competition, use of foreign capital and expertise, expansion of market demand and learning efforts of local firms during the transformation.

Conclusion

All too often, a country is identified with a single political–economic model. Our analysis shows that, in some cases, such an assumption is at odds with reality. Vietnam does not correspond to a single economic system; rather, it is a superposition of socialism, state capitalism and crony capitalism. The motorcycle industry has been governed by rent seeking and government-provided licenses. The goals of technological imports and skill development have been fulfilled mostly thanks to competition for rents among the foreign lead firms and foreign investors' lobbying efforts – all of which are features of the crony capitalist system. The textile-garment and telecommunications industries have a typical state capitalist organisation, with SOEs being the most important players in the market, and they are largely designed to satisfy political, social and economic goals. Nonetheless, the government seems to have been able to engineer a gradual, if still incomplete, restructuring of the industries towards higher competitiveness. Our case studies suggest that it is important to understand the incentives of political and economic participants as they explain the ways in which a government, foreign investors and local firms chose to act within the binding constraints inherent in development processes. Table 1 summarises the rent-seeking regimes, which correspond to our three-sector analyses.

The Vietnam example is important for two main reasons. First, it provides a clear illustration of how different rent-seeking models can coexist within the same country across different sectors of the economy. This provides a serious warning against reaching conclusions about the nature of a country based solely on the analysis of one or few sectors. Second, it illustrates that a crony capitalist growth path could enable growth and development, thanks to the interplay between politics, institutions and markets, despite the lack of universal rule of law as well as contract and property protection. This observation suggests that, when state capacity is weak, a policy agenda that seeks to eliminate rent creation and rent seeking could backfire by undermining the capacity of firms and industry to overcome the weak institutions. In the context of development, growth-enhancing rule of law is not a result of simply eliminating rents and rent seeking. It is the result of a difficult and long process of building state capacity, achieving economic growth and enhancing human development.

The question for the future is whether, given the incentive structure of political elites, developing countries like Vietnam can eventually move towards an open access society (North, Wallis, and Weingast 2009) and away from the personal rules that characterise

Table 1. Summary of rent-seeking regimes in our three-sector analyses.

Industry	Economic regime	Primary goals	Effects on the industry and the economy
Textile-garment	State capitalism	Maintain social order via job creation and retention Gradually liberalise the industry Integrate with the global economy via exporting	High export volume with low value addition and technical learning Substantial private sector participation with some large-scale SOEs
Telecommunications	State capitalism	Maintain strong control of the industry Seek profits and upgrading Protect national security	High growth and development Upgraded infrastructure and technical know-how State-owned duopoly with limited private sector participation
Motorcycle	Crony capitalism	Industrialise the industry and the economy Liberalise the industry with some protection policies Rent extraction	Substantial private sector development with the dominance of FDI Some industrialisation and technological upgrading

all the different avatars of the rent-seeking society. Although we don't answer this question, we provide rich evidence about the underlining conditions that either have amplified or hindered such a move. In addition, the rent-seeking models of state capitalism and crony capitalism allow us to analyse how the political actors have managed this gradual transformation without losing power. Further, as policies adopted often appear at odds with declared aims, such as the goal of favouring technology transfers, the rent-seeking perspective offers more nuanced explanations for the forces that drive those contradictions and development outcomes. Our analyses highlight how political, institutional and market conditions, including those embedded in rent policies, liberalisation and industrial development, can favour beneficial economic reforms.

Notes

1. One important exception is China, which started its economic reform a decade before Vietnam.
2. For a review see Aligica and Tarko (2015, chapter 6).
3. In an all-pay auction, every bidder pays what they bid regardless of whether they will win. For instance, lobbying, and research and development, require payment or spending regardless of whether a desirable outcome is achieved.
4. The historical context that led Vietnam to begin its economic and industrial reforms is provided in online Appendix A.
5. Vietnam became a member of the WTO in January 2007, at which time quota restriction ended.
6. Interviews, two government officials, Ha Noi, June and July 2011.
7. Ibid.
8. Interviews with two government officials, Ha Noi, June and July 2011.
9. Interviews, Ho Chi Minh City, May and June 2011.
10. Interviews with two industry experts, Ha Noi, April and June 2011.
11. This process of SOE reform in the T&G industry is rather similar to that of China. See More (2002, Chapter 3) for details of the Chinese experience.
12. In the Cut-Make-Trim modality, foreign suppliers keep the development of styles and materials under their control and outsource labour-intensive jobs (cut, make, trim, pack) to producers in developing countries. In the Free-on-Board modality, foreign buyers order the final product, and local producers are responsible for producing the garments entirely and arranging shipment.
13. The 11 operators listed as active in 2013 were: VNPT, Viettel, FPT Telecom, HTC, CMC Telecom, GTel Mobile, Dong Duong, VTC, SPT, SCTV and Vishipel.
14. Interviews with government officials, Ha Noi, April and June 2011.
15. Two years later, the government removed the regulating body from VNPT. Thus, VNPT became a state-run monopoly without regulatory functions. This government unit is now the Ministry of Information and Communications, the managing ministry of all telecom operators (Ngo 2017b).
16. Interviews with former VNPT managers, Ha Noi, April 2011, and Ho Chi Minh City, May 2011.
17. A business cooperation contract is a written agreement between a foreign investor and a Vietnamese partner in which the parties agree to cooperate to undertake certain business activities in Vietnam and to share the revenue or profits from such activities. No separate legal entity or company is established, and there is no limitation on liability for participants (Allens Arthur Robinson 2010).
18. In general, Vietnamese SOEs are supervised by their managing industries. However, the prime minister supervises the state-owned general corporations and they report directly to him.
19. See Ngo (2017b) for detailed analysis of Viettel's industrial development during this period.

20. Interviews with a Viettel senior manager, Ha Noi, April 2011 and June 2011.
21. Mobile telecom revenues constituted 68.4 per cent of total telecom revenues.
22. Fforde (2018) observes that, similar to Vietnam, developing countries are moving more towards services in the recent decades, particularly focusing on telecommunications, financial services and tourism.
23. Foreign investors could invest by forming either a business cooperation contract or joint venture with local operators.
24. Interview with a government official, Ha Noi, July 2012.
25. Lead firms are brand-name companies that manufacture and assemble their own brand of motorcycles. They also source components from first-tier and second-tier suppliers.
26. Interviews with two local suppliers, Ha Noi, July 2016.
27. Interviews with local Chinese assemblers, Ha Noi, July 2016.

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Online Appendices

Economic development in a rent-seeking society: socialism, state capitalism and crony capitalism in Vietnam

Canadian Journal of Development Studies / Revue canadienne d'études du développement
Christine Ngo and Vlad Tarko

APPENDIX A

Historical Context of Vietnam's Economic and Industrial Reforms

The 30-year war left Vietnam with heavy war damage and an extremely impoverished economy. As soon as the US lost the war, it imposed a trade embargo cutting off Vietnam not only from US imports and exports but also from trading with American allies. The World Bank, the IMF, and UNESCO – influenced by the American government – all denied Vietnam aid (Davies 2015). In addition, the Vietnamese government's central focus on heavy industry to revolutionize "the relations of production" largely led it to neglect agriculture and consumer goods industry (Bui 2000, 22). Farmers were forced to hand over crops in exchange for ration cards. Without incentives to produce, agriculture production crashed. Annual food production was not enough to feed the people, and the average food per capita (measured in rice) reached only 300 kg per year (Bui 2000). In consequence, the ten-year period before economic reform was marked with poor quality of life, serious shortages of food, consumer goods, transports, health and education services, as well as high inflation. This prolonged period of stagnation and looming crisis pressured the Vietnamese government to move away from the central planning model with a strong focus on heavy industries in the Sixth Party Congress in 1986 (Bui 2000). Thoburn (2013) points out that in the mid-1980s "[i]nflation was over 700 per cent per year, exports were only half the value of imports and there were severe shortages of food and consumer goods" (103).

In 1989, the revolutionary changes in Eastern Europe marked by the fall of the Berlin Wall, followed by the collapse of the USSR two years later, created an additional economic shock and adjustment in Vietnam. First, USSR's aid and trade fell sharply – 29% in the first 6 months of 1991 causing a sharp decline in demand of Vietnamese goods (Elliott 1992). The subsidized prices of goods and raw materials that benefited Vietnamese industries and consumers also disappeared together with the USSR collapse. However, by 1991, the economic reform started in 1986 was underway, and Vietnam weathered the external shocks much better than other former communist states, particularly Cuba (Weeks 2001). Nonetheless, the discontinuation of trade links among communist countries pressured Vietnam to recommence trade relations with China in 1991, European Union in 1992, Southeast Asia (by joining the Association of Southeast Asian Nations) in 1995, and the US in 2001. Elliott (1992) asserts that the collapse of the Soviet Union slowed political reform in Vietnam and thus led to increased crackdown of political dissent and gradual economic openness throughout the 1990s. The demand shock from the fall of communism in Eastern Europe affected Vietnam most strongly in the textiles and garment industry, which was mainly organized as a collection of state-owned enterprises (SOEs). It was the search for new markets in some major sectors such as textile and garment that forced the Vietnamese government to liberalize some parts of the economy.

In 1997, Vietnam's economy was hit hard by the regional financial crisis, which slowed growth by half during the 1998–1999 period, compared to the earlier period (1995–1996) (Bui 2000). Given the weak regional and global demand, Vietnam's economy deflated and market access halted, which led to stagnation in production and consumer demand. Recovering was slow initially. Bui (2000) suggests that the slow pace of economic development in the years following the financial crisis was partly due to internal problems – weak capital market, lack of skilled labor, and inadequate infrastructure. The Communist leaders were made aware then that the country needs deeper integration to upgrade its industries. While the economy recovered in early 2000s, Vietnam was well under way in its negotiation to become a member of the WTO.

As the government searched for options and ideas to reform the economy, the communist leaders looked to experiences from successful Asian countries – Taiwan, South Korea and most importantly China. The Chinese economic reform started a decade earlier provides a useful model for Vietnam: (1) cautiously and gradually open up industries while SOEs continue to be primary players in the economy and (2) attract foreign investment to promote technological change, exports and industrialization.

APPENDIX B

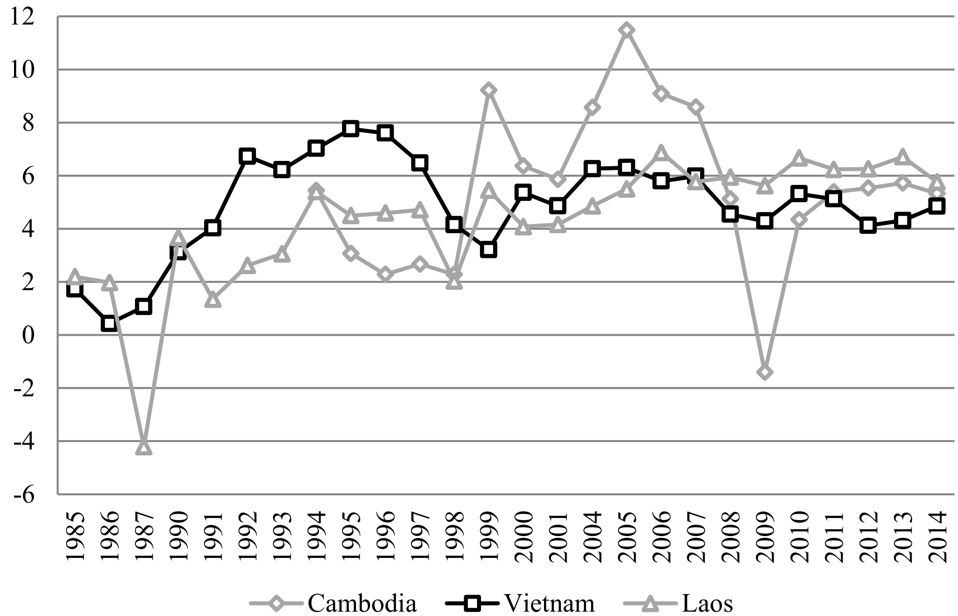

Figure B1. Annual GDP per-capita growth rates (in %), 1985-2014 of three formerly socialist Southeast Asian countries.

Source: World Development Indicators (2016).

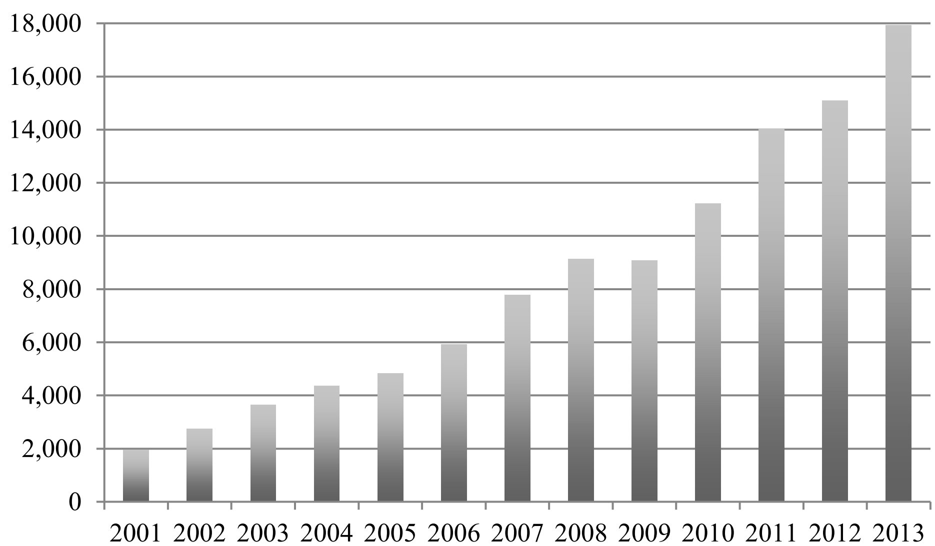

Figure B2. Total export value in the textile and garment industry, 2001–2013 (in USD millions).

Source: Ngo (2017a, 161).

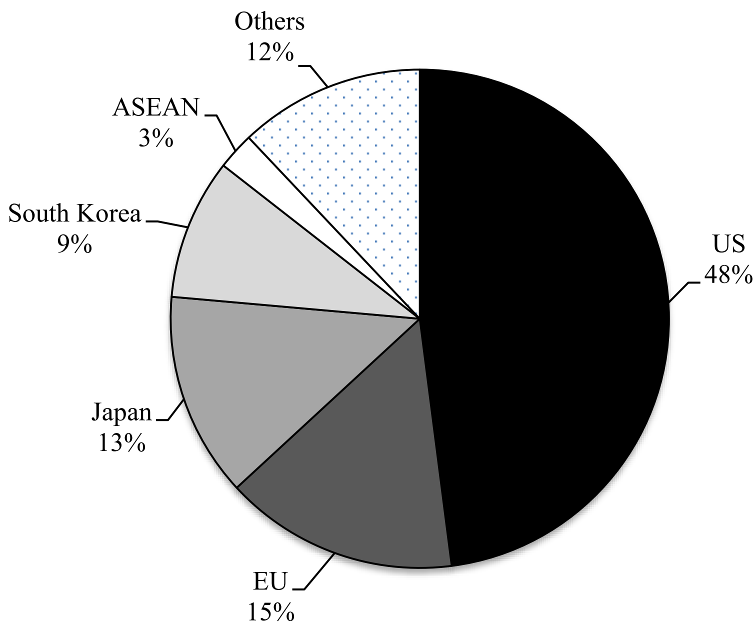

Figure B3. Market shares for textile garment exports in 2013 (in %).

Source: General Department of Vietnam Customs (2014).

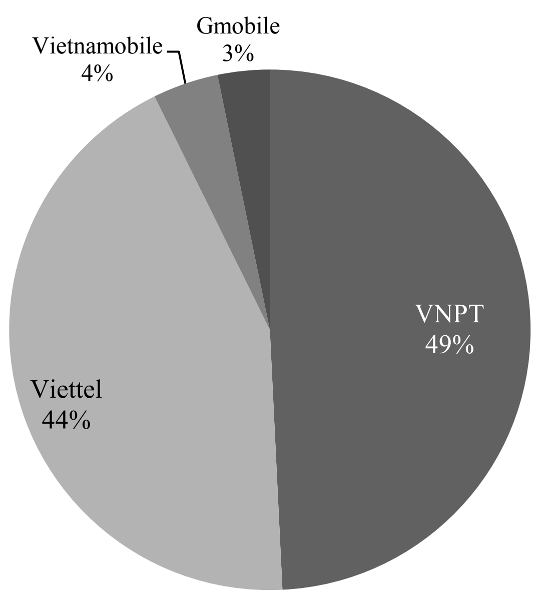

Figure B4. Market shares of mobile phone service providers by subscribers in 2013.

Source: Ministry of Information and Communications (2014).

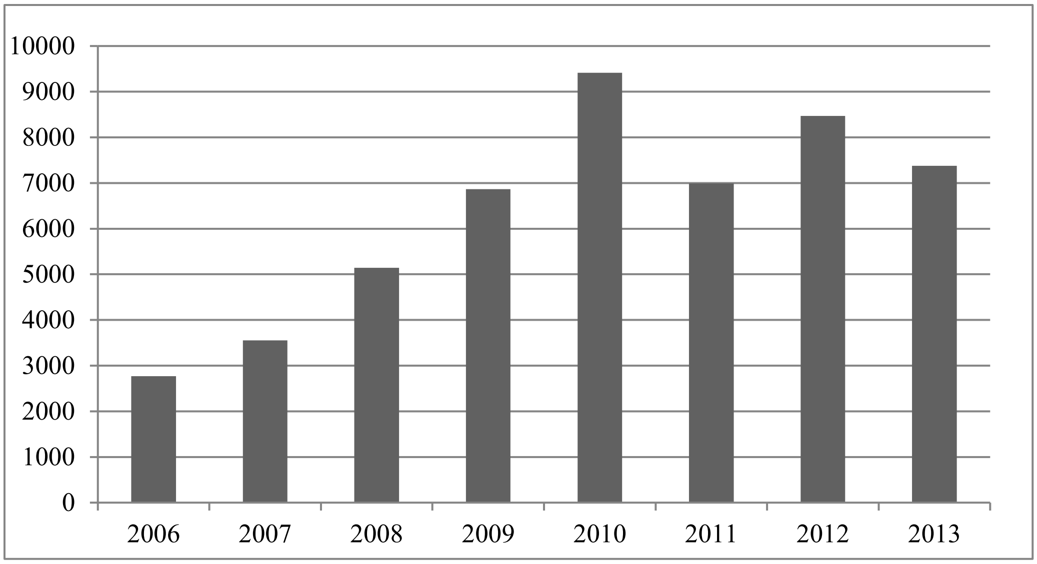

Figure B5. Total revenue of the telecom sector in Vietnam, 2006–2013 (in USD millions).

Source: Ngo (2016a, 1,058).

APPENDIX C

Table C1. Key distinctions between the textile and garment sectors in Vietnam.

Characteristics	Textile	Garment
Intensity	Capital intensive	Labor intensive
Economies of scale	More important	Less important
Ownership	SOEs* and foreign firms	SOEs*, foreign and Vietnamese private firms
Vertical integration	Common to have integration with spinning, weaving, dying, and finishing	Some integration during the central planning period but less so as garment exports increase
Size	Mostly large firms	Mostly small- and medium-sized firms
Market	Mostly domestic (except for unfinished fiber)	Mostly foreign (especially the European Union, Japan and United States)

Note: *SOE = state-owned enterprise.
Source: Adapted from Hill (1998).

Table C2. Vietnam's local production and import-export of telecommunication equipment, 2010–2015 (in USD million).

Year	2010	2011	2012	2013	2014 (estimated)	2015 (estimated)
Total local production	1,196	1,375	1,650	1,750	2,000	2,300
Total exports	49	56	65	75	85	95
Percentage export growth year-on-year	Base year	14.3	16.1	15.4	13.3	11.8

Source: Ngo (2017b, 472)

Table C3. Major foreign motorcycle firms in Vietnam, 1992–2014.

Name of company	Year of license	Ownership structure, country of origin, and per cent owned
Vietnam Manufacture & Export Processing Co., Ltd.	1992	Chinfon Group (producer of SYM motorcycles) (Taiwan, 100%)
Vietnam Suzuki Corp.	1995	Suzuki Corp. (Japan, 35%) Sojitz (Japan, 35%) Vikyno: Southern Agricultural Machinery Corp. (Vietnam, 30%)
SuFat Vietnam Corp.	1996	Sufat (Vietnam, 100%)
Honda Vietnam Co., Ltd.	1996	Honda Motor Co., Ltd. (Japan, 42%) Asian Honda Motors (Thailand, 28%) Vietnam Engine & Agricultural Machinery Corp. (Vietnam, 30%)
Yamaha Vietnam Co., Ltd	1998	Yamaha Motors (Japan, 46%) Hong Leong Industries (Malaysia, 24%) Vietnam Forestry Corporation (30%)
Lifan Motorcycle Manufacturing JV Co.	2002	Chonqing Lifan (China, 70%), Vietnam Import-Export Technology Development Co. (30%)
Kymco Vietnam	2004	Kymco (Taiwan) Hoa Lam (Vietnam)
Piaggio Vietnam	2009	The Piaggio Group (Italy, 100%)

Source: Ngo (2016b, 9)

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