Industrial Strategy for Vietnam’s New Era:
Policy Content & Formulation Method

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Topics

- Vietnam’s challenge – creating internal value in manufacturing
- A proposal for the Vietnam-Japan strategic partnership for joint monozukuri
- A need for serious reform in policy formulation
Vietnam’s New Challenge

- Vietnam is entering a new era where productivity breakthrough and value creation are needed.
- Opening up and receiving FDI can attain middle income ($1,000+), but higher income ($10,000+) requires good policy and private dynamism.
- Vietnam’s future depends on:
  --Creation of internal source of growth
  --Coping with new social problems
  --New macroeconomic management

Per Capita GDP in 2004 (PPP) World Bank data

![Graph showing per capita GDP in 2004 (PPP) for various countries, with a note indicating participants in East Asian production network.](image-url)
Diversity in Governance and Economic Development

High correlation (0.90) but causality cannot be argued from this diagram
Only circled economies participate in regional dynamism

Sources: Compiled from World Bank, Worldwide Governance Indicators, Sep. 2006; and World Bank, World Development Indicators, 2006.

Different Speed of Catching Up

Per capita real income relative to US
(Measured by the 1990 international Geary-Khamis dollars)

Catching Up Process

**STAGE ONE**
- Simple manufacturing under foreign guidance
- Vietnam

**STAGE TWO**
- Have supporting industries, but still under foreign guidance
- Thailand, Malaysia

**STAGE THREE**
- Technology & management mastered, can produce high quality goods
- Korea, Taiwan

**STAGE FOUR**
- Full capability in innovation and product design as global leader
- Japan, US, EU

**Agglomeration**

**Technology absorption**

**Creativity**

Glass ceiling for ASEAN countries (Middle income trap)

Lessons from Thailand and Malaysia

**(Success)** Impressive industrialization and growth led by FDI and reasonable policy

**(Failure)** Domestic private-sector capability is still weak after many decades
- Foreign dependency—inability to send foreign managers home
- Value and capability are not internalized—middle income trap
- Risk of wage pressure and FDI shift to China/India/Vietnam
Vietnam’s Changing Sources of Growth

- Doimoi to mid 1990s—liberalization effect
- Mid 1990s to now—externally driven growth with large inflows of investment, capital and aid
- From now—creation of internal value!

Proposed Strategy for 2020

Building 3 pillars of industrial strength
- Supporting industries
- Industrial human resource
- Efficient logistics

Reform of industrial policy formulation
Concrete targets and action plans
Learning integral manufacturing

Effective use of capital inflows & ODA
Solving social issues
Proper macro management

Preconditions for industrialization
Internal Sources of Manufacturing Strength

- **Supporting industries**
  SME promotion (HRD, technology, management, finance), inviting FDI parts makers, industrial standards, quality standards and testing, factory doctors, FDI-local matching service, promoting SME networking, trade fairs & reverse trade fairs, database

- **Industrial human resource**
  Vocational schools & training centers, Meister system, curriculum reform, overseas education & training, incentive for brain return

- **Efficient logistics**
  Transport & telecom infrastructure, efficient ports & airports, trucking service, cargo handling centers, trading companies, modern distribution network, warehouse, customs and tariff systems

Malaysia’s Manufacturing++

Malaysia’s IMP3 (1996-2005) aimed at raising and broadening the value chain

**Leveling up of each industrial cluster**
- Core production
- Supporting industries
- Supporting services
- Human resources
- Logistics
- R&D
The 4th VDF-Tokyo Conference
9Aug08

<table>
<thead>
<tr>
<th>Modular manufacturing</th>
<th>Integral manufacturing</th>
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</thead>
<tbody>
<tr>
<td><strong>Parts interface</strong></td>
<td>Each product has unique parts, specifically designed</td>
</tr>
<tr>
<td><strong>Merits</strong></td>
<td>Endless pursuit of quality</td>
</tr>
<tr>
<td><strong>Demerits</strong></td>
<td>No differentiation, excess entry, low profit, lack of R&amp;D</td>
</tr>
<tr>
<td><strong>Institutional requirements</strong></td>
<td>It takes much energy and time to achieve results</td>
</tr>
<tr>
<td>Openness, quick decision making, flexible outsourcing</td>
<td>Long-term relations, building internal skills &amp; knowledge</td>
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Performance

- Time

Japan=ASEAN (integral) and USA=China (modular) can form effective partnership

Source: compiled from Prof. Takahiro Fujimoto’s explanation to the Joint VDF-MOI mission, June 2005.
Vietnam-Japan Monozukuri Partnership for Supporting Industries
For Leveling Up Vietnam’s Competitiveness in the Age of Deepening Integration
A VDF Proposal

- This proposal is based on VDF’s past studies on specific industrial sectors, supporting industries, and policy formulation methodology.
- It was drafted in June 2008 at the request of Japanese Ambassador Mitsuo Sakaba (still confidential).
- It is one of the ideas guiding the new bilateral program, which is in the formation stage.

Vietnam-Japan Cooperation in the Past

- Japan has contributed to VN’s industrialization through trade, FDI, ODA and policy dialogue
- Contribution of Japanese ODA
  - Infrastructure (esp. transport & power)
  - Skills and human resources
  - Institutional reforms
  - Improving business environment
  - Urban & regional planning
  - Removing negative impacts of growth
  - Poverty reduction
- Action-oriented bilateral policy dialogue
  - Ishikawa Project (1995-2001)
  - New Miyazawa Plan (1999)
  - VN-Japan Joint Initiative Phase 1, 2, 3 (2003-09)
New Direction of Vietnam-Japan Cooperation

- Vietnam is no longer a low-income transition country. Bilateral cooperation should be more equal and strategic.
- Cooperation should gradually shift from removing negatives and providing basic conditions to proactive creation of the new source of competitiveness.
- VDF proposes Vietnam-Japan strategic partnership for internal value creation.

The Concept of Monozukuri
Japanese Style Skill-based Manufacturing

- Pursuit of high quality and customer satisfaction as the primary goal, with pride and dedication.
- Many of Japan’s excellent companies were founded by engineers full of monozukuri spirit.
Monozukuri – cont.

- Long-term relationship and skill & knowledge building within companies and among companies (assemblers-suppliers).
- Strong demand for 5S, QCD (quality-cost-delivery), kaizen, just-in-time, quality control, and other efforts for constant improvement.

The Purpose

- Establish bilateral partnership to jointly produce high skill products through division of labor:
  - **Japan** – capital- & knowledge-intensive monozukuri processes
  - **Vietnam** – labor-intensive monozukuri processes

  - Over time, as Vietnam's skill improves, transfer more knowledge from Japan to Vietnam
  - The foreign partner (Vietnam) should work closely with Japan, rather than just copying Japanese products or infringing on IPR.
Vietnam’s Challenge

- Large inflow of ASEAN products (esp. Japanese brands) may destroy VN’s industrial base including FDI producers (Daihatsu, Sony).
- The risk of becoming a low-value, simple product producer, or losing FDI to cheap labor countries.
- In the near future, VN’s wage too high for labor-intensive industries, but technology too low for knowledge-intensive industries?
- Vietnam needs a strategic alliance to level up internal capability.

Japan’s Challenge

- Japan has high technology, but faces high wages and ageing population.
- **The 2007 Problem** - Postwar baby boomers (born 1947-49) with high skills began to retire in 2007. Young workers are in shortage. Situation will only get worse as time goes by.
- Japan needs a young developing country as a reliable partner in integral manufacturing
  - The inheritors of monozukuri tradition must be found both domestically and abroad.
Proposed Features of Monozukuri Partnership

- **Resetting the mindset** – Vietnamese managers and workers must be more aggressive in learning and marketing
- **Technology transfer and capacity building**
- **Commitment to international standards** – quality, safety, environment, intellectual property
- **Positioning in the global value chain** – jointly specializing high skilled processes and outsourcing other inputs
- **Reforming policy methodology**
- **Non-exclusivity** (win-win-win) – other countries can also enjoy the benefits of this partnership

Importance of Supporting Industries

- Supporting industry promotion is the first important step to realize the vision of monozukuri partnership.
- Assembly-type manufactured products – large part cost (80-90%) vs. small assembly labor cost (5-10%).
- Without quick access to domestic suppliers with QCD, assemblers cannot compete (added transport cost + long lead time).
- ASEAN4 have been promoting supporting industries for a long time, but with limited success in creating non-FDI suppliers.
The Concept and Scope of Supporting Industries

MITI 1985 – First official use of the term “supporting industries” (susono sangyo)
Ichikawa 2005 – Survey and scope of SI (included in VDF’s Industry Book)
VDF survey on VN’s supporting industries (2006)
Thuy 2007 – Concepts, scope, international experiences (included in VDF’s SI Book vol.1)

- Sectoral vs. horizontal definition (by industry or by process)?
- VDF’s working definition – “a group of industrial activities which supply intermediate inputs (i.e., parts, components, and tools to produce these parts and components) for assembly-type or processing industries” (Thuy 2007, p.38E)

Mr. Kyoshiro Ichikawa’s Memo (JICA Expert at MPI)

- Definition - “Supporting industries include (i) production of parts for final products; (ii) processing and treatment of such parts; and (iii) processing and treatment of materials for producing such parts.

<table>
<thead>
<tr>
<th>Supporting industry producers</th>
<th>Promotion measures</th>
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<tbody>
<tr>
<td>FDI Japanese</td>
<td>FDI promotion, tax incentives, industrial parks (for SI)</td>
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<td>Taiwanese &amp; others</td>
<td></td>
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<tr>
<td>Vietnamese SOEs</td>
<td>Educ. &amp; training of managers; tech. transfer (subsidies); SME finance</td>
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<td>Private SMEs</td>
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- Human resource – common issue for FDI and local firms: (i) top management; (ii) middle managers; (iii) workers
The Concept of Supporting Industries

Suggested Policy Menu

- The following policy menu is constructed from:
  - Vietnam’s Supporting Industry M/P 2007, Motorbike M/P 2007
  - Opinions of Japanese and Vietnamese experts
- This list is intended to be a reference for further discussion only.
**Policy Menu for Supporting Industry Promotion**  
*(A tentative list for discussion)*

<table>
<thead>
<tr>
<th>Policy area</th>
<th>Measures</th>
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<tr>
<td>1. Capacity building (for specific firms)</td>
<td>- Shindanshi (enterprise evaluation) system</td>
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<td>- TA for management and technology</td>
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<td>- Large-scale mobilization of retired Japanese engineers</td>
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<td></td>
<td>- Intensive support for limited sectors (e.g., die &amp; mold)</td>
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<td>- Awards, PR and intense support for excellent suppliers</td>
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<td>2. Human resource (general or institutional)</td>
<td>- Management/technical centers and programs</td>
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<tr>
<td></td>
<td>- Large-scale mobilization of retired Japanese engineers</td>
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<td></td>
<td>- Alliance between FDI firms and local universities/centers</td>
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<td></td>
<td>- Monozukuri school (to be upgraded to university)</td>
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<td></td>
<td>- Meister certification system</td>
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<td>3. Finance</td>
<td>- Credit guarantee</td>
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<td></td>
<td>- SME finance institutions</td>
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<td></td>
<td>- Two-step loans</td>
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<tr>
<td>4. Incentives</td>
<td>- Exemption or reduction of taxes and custom duties</td>
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<td></td>
<td>- Grants or loans for specified actions</td>
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**Policy Menu (cont.)**

| 5. Linkage                         | - Database and matching service                                          |
|                                   | - FDI-vendor linkage program                                             |
|                                   | - Parts Industry Association and Business Study Meetings                  |
|                                   | - Trade fairs and reverse trade fairs                                    |
|                                   | - Linkage with Taiwanese suppliers (motorcycles, electronics)            |
|                                   | - Improving logistics between Hanoi and HCMC                            |
| 6. FDI marketing                   | - Creation of strategic industrial clusters                             |
|                                   | - Industrial parks and rental factories                                 |
|                                   | - Efficient logistics and infrastructure                                 |
|                                   | - FDI marketing targeted to specific sectors or companies                |
| 7. Policy framework                | - Supporting industry master plan                                        |
|                                   | - SME law                                                                |
|                                   | - SME ministry                                                           |
|                                   | - Business associations and industry-specific institutes                  |
|                                   | - Quality standards and testing centers                                  |
Next Steps Proposed by the Japanese Side

Japan (EoJ, JICA, JETRO, experts) and Vietnam (DPM Hai, MOIT, VCCI) will set and implement concrete action plans. VDF will support both sides.

- Sep.2008 – Kick-off Meeting for Supporting Industry Action Plans (Hanoi, hosted by VCCI) - agreed
- Jan.2009 – Finalization of Action Plans and initiation of implementation - agreed
- Action Plan time scope:
  - End 2009 – Short-term actions
  - 2013 – Medium-term actions
  - 2020 – Long-term actions
- Action Plan also linked with:
  - Vietnam-Japan Joint Initiative Phase 3 (2008-09)
  - Bilateral cooperation after the conclusion of Vietnam-Japan EPA (soon?)

Serious Reform in Policy Formulation Needed

- For continued industrialization for higher income, Vietnam needs a fundamental reform in policy formulation. Minor changes of the current system are not enough.
- **Government trap** – low efficiency, low morale, low salary → brain drain from the public sector → low-quality policies
- Strong political will and risk-taking at the top level (Prime Minister) is needed to initiate such reform.
VN’s Policy Process Is One and Only
K Ohno, VietnamNet Interview (May 13&15, 2008)

- VN’s high growth owing to good location and good workers; not because of good policy.
- Industrial strategies are (i) not based on private sector voices; and (ii) not implemented because details are not given. These are unique weaknesses in VN not seen in other countries.
- The same people from planning years are still in charge. I propose a technocrat group directly under PM, as seen in many E Asian countries.
- There are too many public-sector research institutes which fail to produce useful policy analyses. There should be competition among policy-oriented research institutes to convince policy makers and general public.

Vietnam: Traditional M/P Drafting Process

Prime Minister

- Review for approval

Minister

- Submit
- Inter-ministerial review

MPI & other Ministries

- Order
- Submit
- Internal review

Drafting Team

- MPI & other Ministries

Government

- No permanent channel for continuous policy dialogue (case-by-case, temporary, ad hoc)

Business Community

- Appeal letter to Prime Minister when problems arise
- Contact Ministry when necessary
- Interviews, symposiums (sometimes)
- Technical assistance (sometimes)

International experts

Data
Policy Formulation for Vietnam: A Proposal

- Elite technocrat group under strong leadership of Prime Minister
- Choose young, well educated officials and experts
- Simplify policy authority and procedure

Diagram:

Prime Minister

- Direction, full authority for policy making
- Faithful execution and reporting

Technocrat Group (Policy Maker)

- Policy, guidance and monitoring
- Faithful execution and reporting

Experts

Donors

Ministries (Policy Implementers)

Multi-layered Model

Malaysia

Organization for drafting Industrial Master Plan

Source: MITI website.
Note: Numbers in parentheses indicate the number of members in each committee or group.
Malaysia:
Drafting of Industrial Master Plan 2006-2020 (IMP3)

IPC: Industrial Planning Committee (headed by MITI Minister)
SC: Steering Committee (headed by MITI high official)
TRGs: Technical Resource Groups (headed by various experts)

Central Coordination Model:
Thailand under Thaksin 2001-06

Strong Prime Minister

Policy direction
Order to be concretized

Master plans
Policy actions

Direct inputs

Private Sector

Relevant Ministry

Industry-specific Committees

Industry-specific Institute

Experts
Under New Policy Structure
Vietnam Should Achieve:

- Strong top-down visions from PM; sufficient authority for technocrats to execute orders
- Action-oriented policy making with speed and flexibility
- Removal of bureaucratic formalism & inaction, nepotism, corruption, secrecy
- Public sector - competitive recruitment, sufficient salary, internal promotion mechanism, pride to serve the country
Summary of Policy Advice

- Reform policy formulation greatly, by creating a technocrat group under Prime Minister.
- Draft an overall industrial master plan with concrete goals and action plans up to 2020.
- Vietnam-Japan Monozukuri Partnership should be an important part of this 2020 vision.