



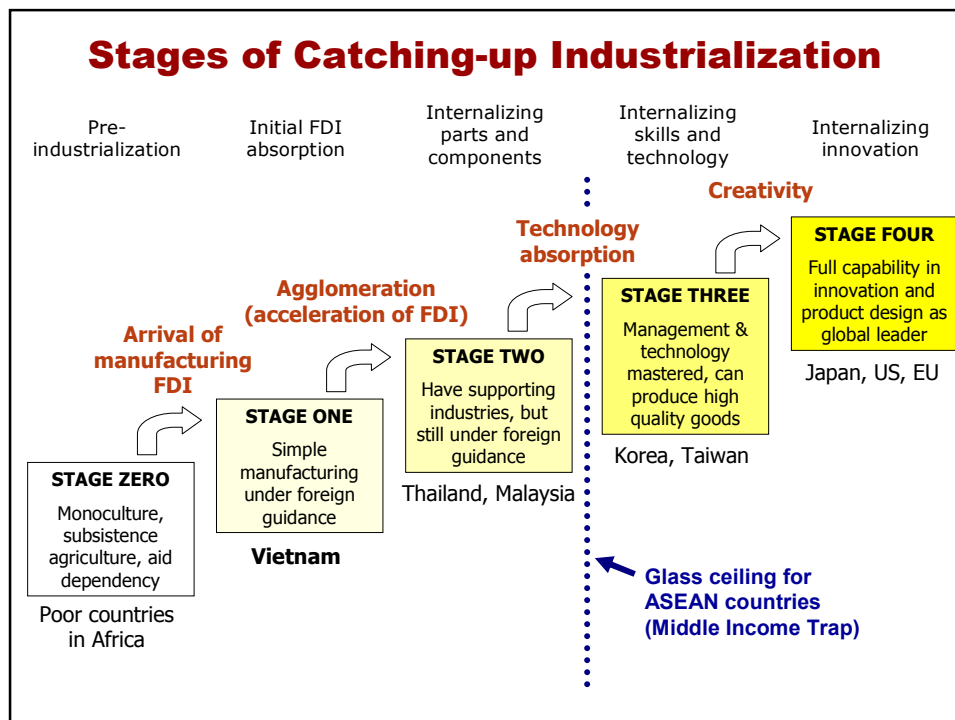
Agenda

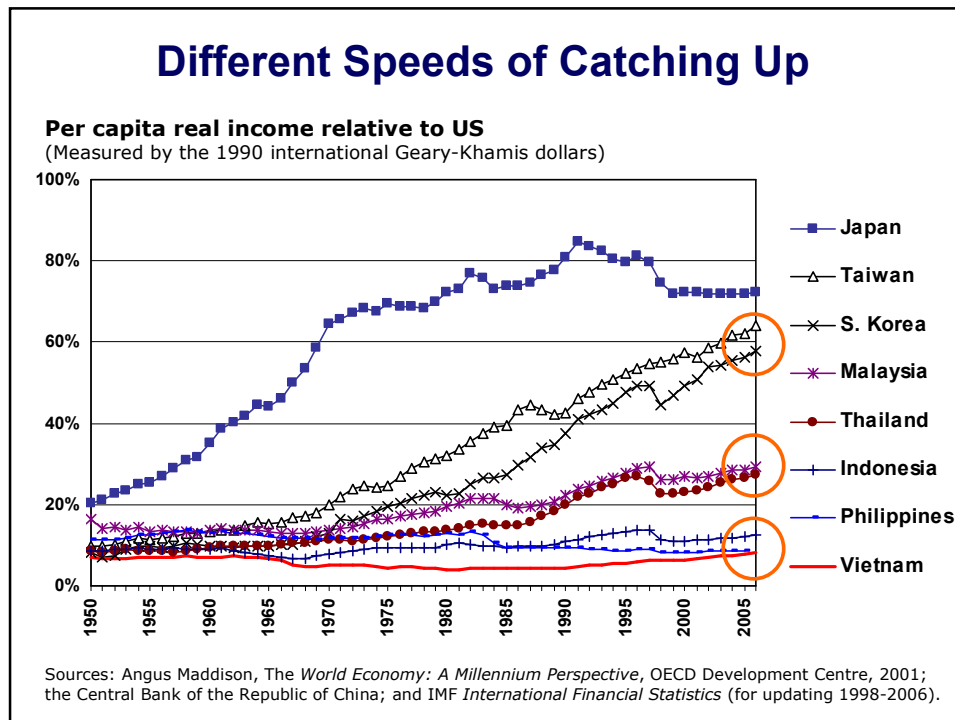
1. Middle Income Trap and Proactive Industrial Policy
2. Vietnam's challenge
3. Issues in policy content and policy organization
4. Concrete lessons from Malaysia and Thailand

Middle Income Trap

- Development must be based on skills and technology, not a lucky endowment of natural resources or geographical advantage. Growth will slow down if the country fails to build a mindset and institutions to encourage constant upgrading of human capital (K. Ohno).
- “The [Malaysian] economy seems to be caught in a middle-income trap—unable to remain competitive as a high-volume, low-cost producer, yet unable to move up the value chain and achieve high growth...” (World Bank, 2009).

Stages of Catching-up Industrialization





Breaking the Trap Requires Human Skill and Effort

If growth is caused by external forces (geography, natural resources, FDI, ODA, overseas Chinese), a developmental trap will eventually occur.

- **Low income trap** – Laos, Ethiopia (no resource, no sea, no manufacturing FDI)
- **Middle income trap** – Thailand, Malaysia (have FDI, seaports, Chinese capitalists)
- **High income trap** – Brunei, Kuwait, Saudi Arabia (a lot of oil; no big problem)
- ➔ **Breaking the trap requires value creation by domestic human capital (hard work based on skill and technology)**



Improving Business Climate Is Not Enough

- Some argue that removing bureaucratic impediments and providing free business environment is crucial (Good Governance Approach, Doing Business Approach).
- But in low-income countries, this may not stimulate private investment unless concrete growth sources are found or created (Kyrgyzstan, Bolivia, El Salvador).
- Wise state guidance is crucial for early industrialization when private investors are weak and markets are undeveloped.



Proactive Industrial Policy

- Under globalization of the 21st century, industrial policy is still possible. But it is different from and more sophisticated than past models.
- Proactive industrial policy must satisfy the following:
 - Commitment to global and regional integration
 - Proper and ever-changing balance between state and market
 - Constant policy learning and information collection



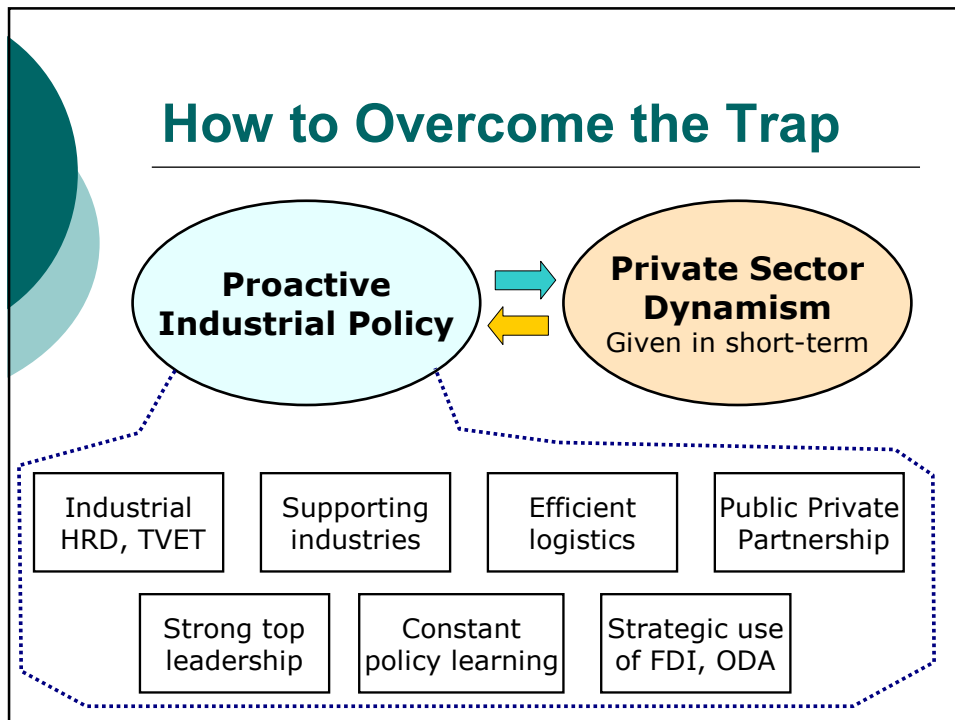
Requirements for Proactive Industrial Policy

1. Private sector-driven development under active globalization (SOEs are not the main engine of growth)
2. A strong state guiding private sector
3. Retaining sufficient policy instruments for latecomer industrialization
4. Constant learning for executing concrete projects
5. Internalizing skills and technology as top national priority



Requirements (cont.)

6. Substantive Public Private Partnership (PPP), not just formal dialogue
 7. Deep knowledge of industries shared by businesses and policy makers
- PIP is different from past models such as socialist planning, infant industry promotion, FDI-led industrialization or laissez-faire.
 - PIP is already practiced in many East Asian countries.



Vietnam's New Era

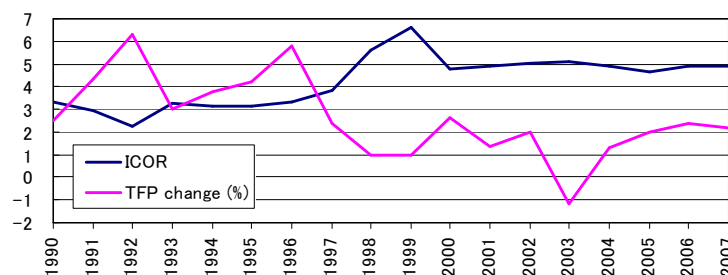
- Vietnam is entering a new era where productivity breakthrough and value creation are needed.
- Opening up and receiving FDI can attain middle income (\$1,000+), but higher income (\$10,000+) requires **proactive industrial policy** and **private dynamism**.
- The question is how to level up skill and technology embodied in human capital. Money and machines are not the problem.

Vietnam's Challenge

- AFTA, WTO, FTAs - large inflows of ASEAN products (esp. Japanese brands) may destroy Vietnam's industrial base.
- The risk of losing manufacturing base and keeping only sales agents ("hollowing-out").
- Vietnam's wage becoming too high for labor-intensive industries, but technology too low for knowledge-intensive industries.
- Vietnam needs a strategic partner to compete in global markets and greatly increase internal value in manufacturing.

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!



Problems with Vietnam's Industrial Policy Formulation

- **Policy content and structure** are outdated and unresponsive to market or private needs. They are not proactive.
- **Policy making procedure and organization** are primitive and cause these weaknesses.
- **Government trap**--inertia and difficulty in reforming policy formulation are noted by Vietnamese officials and experts.

Policy Content and Structure

Successful industrial policy making in East Asia has been characterized by

- Goal orientation:
 - Vision → Strategies → Action plans
- Mechanism to ensure implementation

- Vietnam has a vision (*Industrialization and Modernization 2020*) but it is not backed by concrete strategies or action plans.
- Only small part of approved policies and master plans are implemented in Vietnam.

<Malaysia>

Vision 2020 → IMP → OPP/Malaysia Plan → Budget
 "Become fully developed" 1991 (15 yrs) (5-10 yrs) (annual)

<Thailand under Thaksin> (2001-06)

PM's vision → Auto Master Plan → Action Plan Matrix
 Become "Detroit of Asia" Business-MOI-experts agree on targets for car/motorcycle production & export

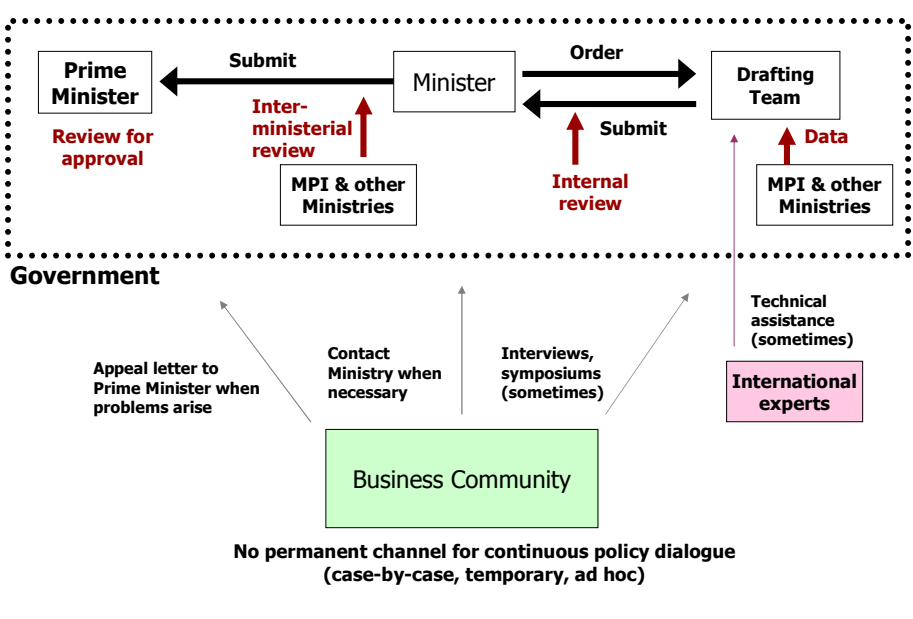
<Ethiopia>

ADLI → Ind.Dev.Strategy → M/Ps → Exp.St.Committee
 1994 2003:policy principles Leather/garment/flower/food processing

<Vietnam>

Goal 2020 → Overall industrial M/P? → Action Plan?
 SEDP/SEDS (Does not exist) (Does not exist)

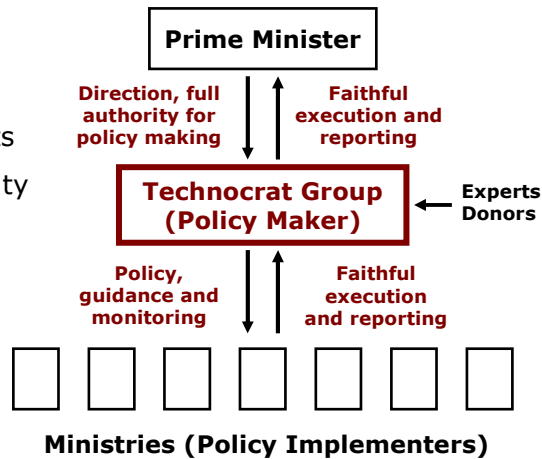
Vietnam: Traditional M/P Drafting Process



My Recommendation for Vietnam

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

Korea – Econ. Planning Board
 Malaysia – Econ. Planning Unit
 Thailand – NESDB
 Taiwan – Kuomintang Elites
 Indonesia – "Berkeley Mafia"
 Chile – "Chicago Boys"
So why not Vietnam also?



Lessons from Malaysia and Thailand

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

(Failure) Domestic private-sector capability is still weak after many decades of promotion

- Foreign dependency—inability to send foreign managers home
- Value and capability are not internalized—middle income trap
- Risk of wage pressure and FDI shifting to China/India/Vietnam

Common Policy Menu for Industrial Capability (Malaysia & Thailand)

- Legal framework and policy coordination
- Master plans and action plans
- Investment incentives
- TVET for managers, engineers, workers and students
- Management and technical consultation
- Business matching and linkage
- SME finance

Thailand: Supporting Industry Master Plan 1995

Proposed program	Outcome
1. Policy & legislation 1.1. Basic law of SME development 1.2. Law of subcontracting promotion 1.3. Restructuring of DIP for SME & SI promotion 1.4. Preparation of industrial statistics (SI database)	1. 1.1. SME Promotion Act 2000 1.2. (no action) 1.3. Establishment of DSIP & OSMEP 1.4. n.a.
2. Market development (Linkage) 2.1. Expansion of BUILD activities 2.2. Subcontracting assistance program	2. 2.1. BUILD (1993-1997) 2.2. NSDP (1994)
3. Technology upgrading 3.1. Technology extension service program (shindanshi sys.) 3.2. Expansion of occupational skill standard system 3.3. Public technical center activation program 3.4. Joint industry-university training schools	3. 3.1. (no action) 3.2. (no action) 3.3. TAI, TGI, etc. 3.4. TNI, TGI, etc.
4. Financial support 4.1. Improvement of SME financing schemes 4.2. Assistance for SME in machinery leasing	4. 4.1. SME Bank, loan agent network 4.2. Credit guarantee, machine fund
5. Upgrading of management 5.1. Entrepreneur re-education program 5.2. Continuation of technopreneur development project	5. 5.1. TNI, TGI, etc. 5.2. n.a.
6. Investment promotion 6.1. Grouped investors attraction program 6.2. Entrepreneur incubation program 6.3. Assistance for new comers penetration	6. 6.1. Amata Industrial Estate 6.2. OSMEP 6.3. OSMEP

Vietnam's Supporting Industry Action Plan Proposed by Japan (June 2009)

- Vietnam's action and Japan's support are specified in parallel.
- Short-term (mid 2010), medium-term (end 2011), long-term (end 2015).

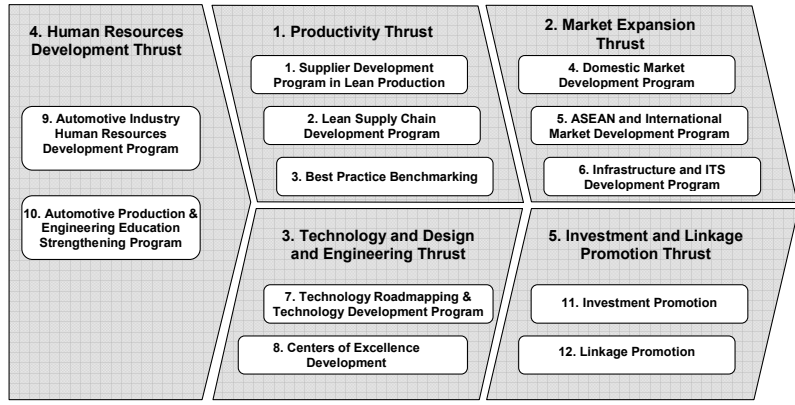
Policy framework	Definitions of SI, award system, inter-ministerial mechanism, SME laws, etc.
Human resource	Pilot TVET projects for engineers & managers, skill certification system, monozukuri university, etc.
Finance	Low-interest loans, subsidies, tax exemption, shindan system, etc.
FDI marketing	Investment seminars, SI industrial parks, linkage between FDI and locals, etc.
Business linkage	SI database, trade fairs, industry associations, etc.

Key Industrial Policy Documents

Malaysia (2009 per capita GDP \$7,750)	Thailand (2009 per capita GDP \$3,973)
Vision 2020 National Mission 2006-2020 Industrial Master Plan 2006-2020 New Economic Model (PM Najib), 2010 New Automotive Plan, revised 2009 SME Annual Report 2008	National Economic & Social Development Plan 2007-2011 Automotive Master Plan 2007-2011 Supporting Industry Master Plan 1995 SME Promotion Master Plan 2007-2011

Thai Auto Master Plan 2007-2011: (5 Thrusts and 12 Action Plans)

Vision 2011: "Thailand is the automotive production base in Asia which creates more value added to the country with strong automotive parts industry."



Malaysia: Key Organizations

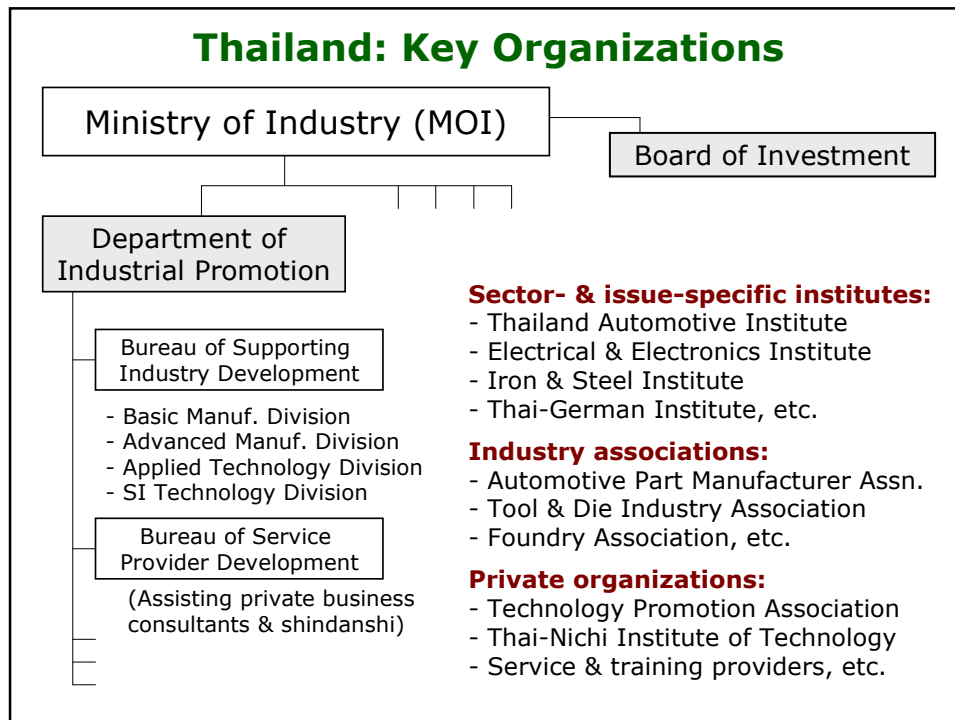
Ministry of Int'l Trade and Industry (MITI)

- Strategic Planning
- Entrepreneurship Development
- Sectoral Policy & Industrial Service
- Investment Policy & Trade Facilitation
- Services Sector Development

Implementation Agencies under MITI:

- SME Corp (SMEs)
- Malaysian Ind. Dev. Authority (investment)
- Malaysia Productivity Corp (research, training, consultation)
- SME Bank (finance)
- Malaysian Ind. Dev. Finance (finance)
- MATRADE (trade)

Service & training providers (private consultants & companies)



Investment Incentives (Malaysia)

- Malaysian Industrial Dev. Authority (MIDA) centrally approves investment licenses and incentives (no delegation of authority to local level).
- Incentives have two basic forms:
 - { Pioneer Status (corporate income tax exemption)
 - { Investment Tax Allowance
- Incentive approval:
 - Activity or product must be in the priority list
 - Review by relevant industry division followed by MIDA Weekly Action Committee
 - Criteria: value creation, innovation, linkage

MIDA: Structure of Incentives

1. Manufacturing
2. Agriculture
3. Biotechnology
4. Tourism
5. Environment
6. R&D
7. Medical device
- ...
18. Other

- 1. Main**
2. Relocation
3. High-tech companies
4. Strategic projects
5. SMEs
6. Industrial linkages
7. Machinery & equipment
8. Auto component modules & systems
9. Oil palm biomass
10. Other (7)

Eligible Items (Manufacturing Main)

I. Agricultural production (20)
 II. Processing of agricultural produce (15)
 III. Forestry & forestry products (3)
 IV. Manufacture of rubber products (7)
 V. Manufacture of oil palm products & their derivatives (10)
 VI. Manufacture of chemicals & petrochemicals (16)
 VII. Manufacture of pharmaceutical & related products (6)
 VIII. Manufacture of wood & wood products (6)
 IX. Manufacture of pulp, paper & paperboard (11)
 X. Manufacture of textiles and textile products (10)

XI. Manufacture of clay-based, sand-based & other non-metallic products (34)
 XII. Manufacture of iron & steel (12)
 XIII. Manufacture of non-ferrous metals & their products (10)
XIV. Manufacture of machinery & machinery components (10)
XV. Manufacture of transport equipment, components & accessories (29)
XVI. Supporting products/ activities (17)
XVII. Manufacture of electrical and electronic products & components and parts thereof (19)

XVIII. Manufacture of professional, medical, scientific & measuring devices /parts (6)
XIX. Manufacture of photographic, cinematographic, video & optical goods (4)
XX. Manufacture of plastic products (7)
 XXI. Miscellaneous (25)
 XXII. Hotel business & tourist industry (6)
 XXIII. Film industry (2)
 XXIV. Manufacturing related services (9)
 XXV. Manufacture of kenaf based products (1)
 XXVI. Protective equipment & devices (3)

Eligible Items - Detail (XVI. Supporting Products/Activities)

XVI. Supporting products/activities

- | | |
|--|---|
| 1. Metal casting | 12. Advanced composite materials |
| 2. Metal forgings | 13. Mould designing |
| 3. Metal surface treatment/finishing | 14. Advanced surface treatment or finishing for precision engineering plastic parts |
| 4. Machining | 15. High purity gas piping system system & parts thereof |
| 5. Moulds, tools and dies | 16. Metal stamping (*) |
| 6. Powder metallurgical parts (sintering of metal parts) | 17. Galvanizing, shearing or slitting of metal sheets or other related engineering services (*) |
| 7. Heat treatment | |
| 8. Mould texturing | |
| 9. Irradiation service | |
| 10. Gas sterilization service | (*) -- Incentives provided in promoted areas only (Sabah, Sarawak, Perlis, Kelantan, Terengganu, Pahang & the district of Mersing in Johor) |
| 11. Overhaul, repair, reconditioning, modification or servicing and testing of turbine engines | |

Capacity Building and TVET (Thailand)

Organization	Period	Remark
King Mongkut's Institute of Technology	1961-	Top-level university in engineering, esp. ICT
Technology Promotion Association (TPA)	1973-	Training, consultation, publication, language
<i>Shindanshi</i> (business consultant) program	1999-2004	450 SME consultants produced
Automotive Human Resource Development Program	2006-2010	Various assistance by Denso, Honda, Nissan and Toyota
Thai-German Institute	1999-	technical training in CNC, CAD/CAM, mould & die, etc.
Thai-Nichi Institute of Technology (TNI)	2007-	Private university to teach Japanese style production in theory & practice

Business Matching and Linkage	
Malaysia	Thailand
<p>Vendor Development Program (1988-1996)</p> <p style="text-align: center;">↓</p> <p>Industrial Linkage Program (1996-)</p> <ul style="list-style-type: none"> 1. Financial incentives 2. Business matching 3. Support package (R&D, technology, marketing, etc.) 4. Allowances for anchor firms (assemblers) providing training & TA for SMEs <p>Eligibility – SMEs with 60% or more Malay capital</p>	<p>BOI Unit for Industrial Linkage Development (BUILD, 1992-)</p> <ul style="list-style-type: none"> 1. Vendor-meet-customers (BOI intermediates anchor firms & vendors) 2. Marketplace (monthly meetings of anchor firms & vendors) 3. Sourcing (MNCs present their component needs) 4. ASEAN Supporting Industry Database

SME Finance (Malaysia, end 2008)
<ul style="list-style-type: none"> ○ 54 commercial banks providing loans of RM54.4b to 117,524 SMEs. ○ 6 development finance institutions providing loans RM4.8b to 31,220 SMEs. ○ 5 Bank Negara (central bank) special funds for SMEs (RM7.6b outstanding). ○ 114 government funds and schemes for SMEs (RM9.7b outstanding). ○ Credit Guarantee Corporation since 1972. ○ SME debt resolution scheme, 56 venture capital companies, leasing and factoring

Rental Factory Scheme for SMEs

Thailand

- Ota Techno Park for inviting Japanese high-tech SMEs (private, since 2006).

Malaysia

- SME Bank Factory Scheme for Bumiputra (ethnic Malay) SMEs (public, since 1984).

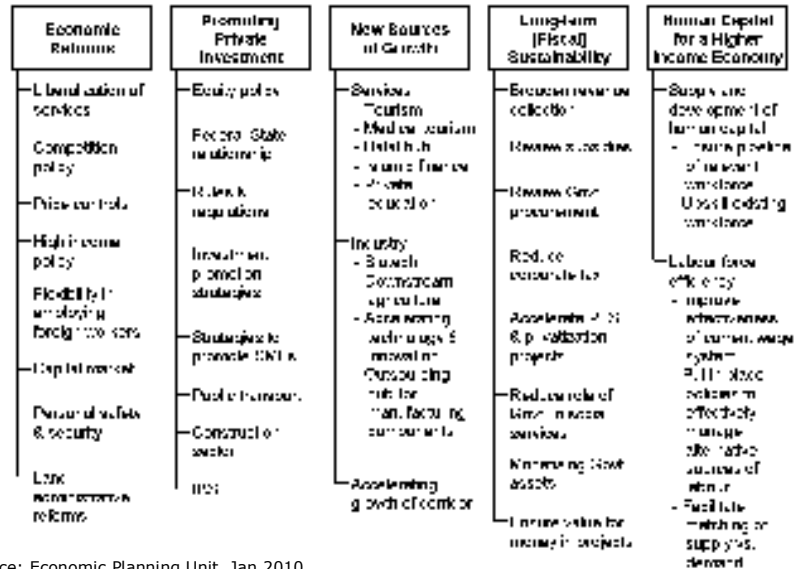
- Both offer temporary factory space until SMEs graduate to larger plots.
- Administrative and other supports are provided to renting SMEs.

Malaysia: SME Bank Factory Scheme

Location	Factory Scheme	Number of plots	Type					Plot area (sq ft)
			1 floor	1.5 floors	2 floors	Semi-detached	Bangalow	
Kota Bharu	Pengkalan Chepa 1, Kelantan	23	17	6				1,000-1,800
	Pengkalan Chepa 2, Kelantan	20		16		4		4,400-6,500
Kuantan	Bandar Pusat Jengka, Pahang	20	20					900-4,500
	Gebeng II Kuantan, Pahang	20		16		4		4,960-7,300
K. Terengganu	Chndering, Kuala Terengganu	26		26				1,800
	Kampung Raja, Besut, Terengganu	15	15					1,800-2,700
	Mergong Barrage, Alor Star, Kedah	17	17					1,800
Alor Setar	Sungai Petani, Kedah	18				16	2	3,500
Johor Bahru	Tampoi, Johor Bahru, Johor	22	22					1,800
	Sri Gading II, Batu Pahat, Johor	20		16		4		4,200-6,250
Ipoh	Menglembu, Perak	29				29		1,750
Seremban	Seremban, Negeri Sembilan	22				22		1,690
Bandar Bayan Baru	Seberang Prai, Pulau Pinang	17		17				1,800-3,200
	Simpang Ampat, Pulau Pinang	12				12		3,000
	Bayan Lepas, Pulau Penang	4		4				2,303
Kangar	Kuala Perlis, Perlis	15		11		4		1,800-3,200
Bandar Melaka	Telok Mas, Melaka	18		18				1,800-3,200
Shah Alam	Shah Alam, Selangor	38		38				2,000-5,040
	Sungai Buloh, Selangor	3			3			4,500
	Sunway Damansara, Selangor	14				14		3,700-4,800
Kuala Lumpur	Batu Caves, Selangor	23		23				3,336-4,410
Kota Kinabalu	Lak Kawi, Sabah	15		15				2,500
Kuching	Kota Padawan, Kuching, Sarawak	6				6		2,275
	Muara Tabuwan, Sarawak	5				5		3,200-3,800
TOTAL		422	91	206	3	120	2	

Malaysia: "New Economic Model"

Prime Minister Najib's Strategy to Overcome Middle Income Trap



Source: Economic Planning Unit, Jan.2010

Conclusion for Vietnam

- Policy experiences of neighboring countries must be studied selectively and in detail.
- Clear policy vision and targets must be set in SEDP 2011-15 and SEDS 2011-2020.
- An integrated and concrete policy package must be designed and implemented to realize SEDP/SEDS goals. Vietnam must learn how to draft this policy package.