From Plan to Market:

Evaluating the Economic Transformations of China and Vietnam

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In the past few decades, two communist states in East Asia have undergone momentous transitions to free market systems without experiencing collapse or revolution. The story of China's miraculous growth over the past thirty years has attracted the attention of the world. Slightly less attention has been paid to the equally impressive transition in Vietnam. The two countries are particularly interesting to compare because both states have moved from a strictly controlled, communist plan towards a free market economy.

In evaluating the respective transformations that have taken place in China and Vietnam, it is important to answer a few key questions. First of all, one must ask why isolated communist states would decide to abandon Marxist-Leninist ideology and pursue capitalism. Once the reason why is established, it is equally important to analyze how China and Vietnam instituted the necessary reforms to establish free market systems. Lastly, as a subset of the "how" question, an evaluation of the respective transitions must ask who was responsible for instituting reforms.

The answers to these questions provide a framework to address how the process of reform was similar in China and Vietnam and how it differed. In regard to why the two communist states pursued reform, a review of China's and Vietnam's historical background show that the respective communist parties chose economic reform as a matter of political survival. In China, this decision was made largely by one man in an attempt to provide economic development while simultaneously securing his own political future. The communists in Hanoi, on the other hand, were not united under one man; rather, they were merely trying to keep up with the changes that were taking place illegally in Vietnam.

This pattern of top-down leadership in China and informally driven policy in Vietnam also characterizes how the communist states pursued reform. In China, reform was artfully crafted and gradually implemented under the strong leadership of a central figure. The Vietnamese experience, conversely, was defined by equivocation among the party leadership while lower echelons of the economy illicitly instituted change. When the communists in Hanoi were able to achieve official approval of reform, they were rarely able to enforce it. Thus, uneven growth and reform characterized Vietnam's economy in the 1980s and 1990s while China experienced strong growth and a steady, yet gradual pace of liberalization.

Recently, however, dynamic changes have taken place in Vietnam including their accession to the World Trade Organization (WTO). History has not yet provided adequate context to properly evaluate these developments; thus, the main body analysis of Vietnam's experience with reform excludes the developments of the past few years. However, because Vietnam has made extraordinary progress in this time, an attempt at updating the assessment of their transformation is necessary and is provided towards the end of this work. Although it is still too early to accurately judge, it appears that Vietnam's recent progress has been driven by both improved leadership and the efforts of private citizens.

Historical Circumstances

The two Asian neighbors have had unique and exciting histories throughout the twentieth century. The word "turbulence" aptly describes the situation in China and Vietnam for most of the past one hundred years. Fittingly then, political and economic stability were the factors that provoked reform in both countries. Despite winning out power over foreign and domestic competitors, the communist parties in China and Vietnam were facing political death because of their own failed socialist policies.

China

In China, the hybrid Sino-Soviet socialist model was strangling the country. Barry Naughton describes the implementation and effects of Maoist industrialization in his text The Chinese Economy: Transitions and Growth. The Chinese development strategy prior to 1978 suffered for two important reasons. First, policy initiatives were often the whim of one man. Mao's great degree of control over decision making led to a legacy of policy instability from 1949 to 1978. Secondly, the strategy of rapid industrialization adopted by China did not take advantage of its inherent strength—human capital. Pursuing capital-intensive industrialization policies, the Chinese Communist Party (CCP) ignored the agricultural and service economies, leaving many of their citizens jobless and starving.[1]

Mao's sporadic leadership style led to a pattern of frequent direction changes during China's socialist era. One policy would be instituted, then after a few years the great chairman would launch a new campaign in response to political criticisms.[2] The most devastating campaign was Mao's Great Leap Forward. Naughton describes it as "the most dramatic, peculiar, and ultimately tragic period in the history of the PRC."[3] The Great Leap Forward was Mao's reaction to a preceding period of increased openness and economic flexibility; it exemplifies the two main problems with the pre-reform Chinese economy. The campaign was blindly driven by Mao Zedong's political beliefs

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[1] Naughton, Barry. The Chinese Economy: Transitions and Growth. Cambridge, Massachusetts: The MIT Press, 2007. 62, 79-82
[2] Naughton 62-63
[3] Naughton 69

and stressed rapid industrialization while ignoring agricultural needs.[4] The resulting famine led to the deaths of 25-30 million Chinese citizens and a misplacement of employment away from the agricultural and service sector.

The instability and economic mismanagement of the Great Leap Forward typified the Chinese socialist experience from 1949-1978. Although the CCP did perform fairly well in industrializing China, they also exposed their citizens to years of starvation and instability. In Naughton's opinion, the disastrous effects of unwise economic policies outweighed any achievements. Because of the adverse effects of rapid industrialization, the CCP was ready to experiment with other strategies by the late 1970s. Concurrently, the party was experiencing a leadership crisis that had paralyzed economic decision making in the mid 1970s.[5] With Mao's death in 1976 the time was ripe for a fresh direction under a new leader in China.

Vietnam

The Vietnamese Communist Party (VCP) also created their own problems by trying to institute socialist reforms throughout the country. Unlike the People's Republic of China (on the eve of reforms), Vietnam had to deal with a country that was still divided by years of war. The struggles with France and the United States throughout the middle of the twentieth century created a dichotomy of Vietnams. According to the Vietnamese scholar Ton That Thien, this divide was along economic lines, in addition to political and social. "There was communism and rigid central planning in the North versus anticommunism and a capitalist free market in the South."[6] The official separation

[4] Naughton 69-70
[5] Naughton 77, 80, 82
[6] Thien, Ton That. "Cultural Issues in Vietnam's Transition." The Vietnamese Economy and Its Transformation to an Open Market System. 2005. 25

of North and South Vietnam ended in 1975, but the divided social and economic environment persisted.

In efforts to unify the country, the Vietnamese Communist Party launched anti-capitalist and agricultural collectivization campaigns in 1978.[7] During this time, the economy of the South was disassembled in order to pursue full commitment to Marxist-Leninist policies. According to Thien, the economic devastation drove "south professionals to either joining the ranks of the 'boat people' [emigrants from Vietnam] or to becoming irrelevant in their own country.[8] While the Communist Party strangled the previously economically hopeful South, the Vietnamese army invaded Cambodia provoking a subsequent Chinese attack on Vietnamese border towns. The combination of the destabilizing attempt to unify the country and the breakout of conflict with both Cambodia and China created shortages and hardship throughout Vietnam.[9] By the close of the 1970s, the leadership was forced to consider a new course.

Instituting Reform

China

In China, the decision to embark on reform was economic and political. In the late 1970s, Deng Xiaoping saw an opportunity to secure political power by improving China's economic situation.[10] An ailing Mao during the mid 1970s had led to deadlock in economic policy making.[11] The country was in desperate need of economic healing, and Deng Xiaoping saw reform as a way to begin restructuring while also securing his

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[7] Quinn-Judge, Sophie. "Rethinking the history of the Vietnamese Communist Party." Rethinking Vietnam. 2004. 285
[8] Thien 26
[9] Quinn-Judge 286
[10] Shirk, Susan L. How China Opened Its Door: The Political Succes of the PRC's Foreign Trade and Investment Reforms. 1994. 11
[11] Naughton 77

own position of power. Deng's strong leadership would push forward developmental economic reforms from the late 1970s to the mid 1980s, while repeatedly overcoming conservative opposition.

To avoid shocks to society and strong political opposition, the CCP leadership pursued economic opening gradually by creating four special economic zones (SEZs). Initially restricting liberalization to four select cities served two purposes. First, Deng was able to assuage the fears of party members who believed that opening China to foreign firms would lead to the type of embarrassment that China experienced during the 19th century. Limiting liberalization to four cities guaranteed the curtailment of foreign influence in China.[12] Secondly, the geographic selectivity of liberalization led party officials throughout the country to desire the economic benefits of SEZs, such as currency exchange allowances and tax incentives. According to Susan Shirk "[e]nvy has a powerful effect on policy preferences."[13] The CCP's gradual approach comforted party skeptics and created a demand for further liberalization among officials. The careful, yet courageous pursuit of reform allowed Deng Xiaoping to secure China's economic future and his own political power.

This first stage of opening, mostly during the 1980s, was called "reform without losers" because the government implemented a dual-track economic system that established markets while still nurturing the old planned economy.[14] The second stage began deeper liberalization and gradually decreased government support for the state sector. Throughout the 1990s, under the economic leadership of Zhu Rongji, China privatized old state companies and attracted enormous amounts of foreign direct

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[12] Shirk 36
[13] Shirk 38
[14] Naughton 91-92

investment. Because the second stage involved serious job losses and heightened competition due to foreign firms in the domestic market, this wave of liberalization was considered “reform with losers”.[15] Although the second stage of reform brought on some economic hardships domestically, the adoption of “reform with losers” showed China’s commitment to reform and Zhu Rongji’s strength of leadership in pursuing liberalization.

Vietnam

In contrast to China, Vietnam’s move towards reform was more of a forced hand than a bold decision. Due to their inabilities to successfully lead a unified Vietnam, public opinion turned against the VCP in the late 1970s. Chris Dixon describes “increasing signs of discontent and non-compliance with central directives” since the “party-state was not fulfilling its promise of improved conditions.”[16] Often the leaders were trying to keep up with changes already being instituted illegally by private citizens or self-serving officials. Martin Gainsborough explains that an “authentic account of reform would emphasize the way reform as policy very often emerged as a response to changes which had already taken place but had not been officially sanctioned.”[17] Weak leadership forced the VCP into a game of “catch-up” with their own officials and citizens.

The lagging leadership can be seen in the first official steps towards reform. Policy change began in 1979 at the sixth party plenum. The VCP approved reforms in the manufacturing and agricultural sectors that were reminiscent of illegal household experiments during the 1960s and 1970s.[18] The changes included “production incentives and increased freedom for local managers” and a “family contract system within

[15] Naughton 100
[16] Dixon, Chris. “State, party and political change” Rethinking Vietnam. 2004. 17
[17] Gainsborough, Martin. Changing Political Economy of Vietnam. 2003. 109
[18] Beresford, Melanie. “Vietnam: the Transition from Central Planning” The Political Economy of South-East Asia. 2006. 204

agricultural cooperatives."[19] In reality, the party only gave consent and some encouragement for activities that were already taking place illegally.

Gainsborough cites Adam Fforde and Stefan de Vylder as developing the theory of "fence breaking" in Vietnam.[20] These authors put forth the idea that "the illegal involvement of state enterprises and bureaucratic institutions in markets during the era of planning laid the foundation for the market economy ahead of any substantive moves towards reform by the state."[21] Fforde and de Vylder's theory emphasizes a persistent theme in Vietnam's development. Throughout the past 30 years, Vietnam's economic development has been dependent on the informal efforts of private citizens and disobedient cadres to push forward crucial changes.

Despite the surging support of many citizens and bureaucrats, reform still suffered at the hands of VCP conservatives. According to Beresford:

> "By early 1982, a recovery was underway and party fears of the re-emergence of capitalism were renewed, causing the party to take measures against further private-sector development, including a renewed attempt to collectivize southern agriculture."[22]

The conservative backlash in the early 1980s even caused a closure of Ho Chi Minh City's state-owned export-import companies.[23] Beresford explains, however, that the

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[19] Quinn-Judge 286

[20] Fforde, Adam and Stefan de Vylder. From Plan to Market: The Economic Transition in Vietnam. Boulder, CO: Westview Press; 1996.

[21] Gainsborough, Martin. "Key issues in the political economy of post-*doi moi* Vietnam." Rethinking Vietnam. 2004. 48

[22] Beresford 205

[23] Quinn-Judge 286

planned economy continued to fail while reforms experienced success, and thus, the movement for change regained momentum by 1985.[24]

In 1986, VCP leader Truong Chinh gave a speech that endorsed the economic reforms and apologized for the VCP's initial rushed attempt at abolishing capitalism.[25] The remarks came seven years after Vietnam's official beginnings of reform and illustrates the lagging leadership of the VCP. The speech did, however, indicate the beginning of *doi moi* (renovation), Vietnam's renewed stage of reform and the first stage with some signs of commitment from the party. As explained by Beresford, "[w]hereas reform before 1986 was largely spontaneous in character, with the state attempting to manage (sometimes even reverse) the process of change, it is only after 1986 that we can speak of the state playing a role in pushing the pace of change."[26] *Doi moi* had gained the support of the majority of the VCP but conservative opposition would continue to create backlashes.

In William Alpert and Sol Sanders' evaluation of Vietnam's reforms, the VCP is sharply criticized for their inability to overcome opposition to reform. The authors stated that "Vietnamese authorities continued to avoid taking action that would diminish the privileges of Communist Party members. Whenever a conflict between politics and economics arose, it was always the economic arguments that were sacrificed."[27] As a result of the Party leadership's lack of backbone, Alpert and Sanders express that only price and exchange rate reform were implemented seriously, while banking, enterprise, and institutional reforms fell victim to conservative opposition. The two scholars'

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[24] Beresford 205
[25] Quinn-Judge 287
[26] Beresford 207
[27] Alpert, William T. and Sol Sanders. "Recent Economic History." The Vietnamese Economy and Its Transformation to an Open Market System. 2005. 39

assessment illustrates how the VCP's weak leadership has chronically injured the progression of reform and development in Vietnam.

Further Analysis

A fuller understanding of how China's reforms were pushed forward by strong leadership while Vietnam experienced equivocation from the top requires an examination of specific areas of reform. Foreign direct investment, enterprise ownership, and the banking sector are worthy of analysis because they represent crucial aspects of a country's transition to a free market system.

Note: Again, the following examination does not include the very recent developments in Vietnam. An assessment of these changes will be offered towards the end of the paper.

Foreign Direct Investment Reform

Foreign direct investment (FDI) is commonly viewed as a key to economic growth for developing countries. The involvement of foreign firms in a transitioning economy can lead to technology diffusion, "know-how" transfer, and increased amounts of capital.[28] Therefore, attracting foreign investment has been an important part of reform strategies in both China and Vietnam. China, however, has proved superior at consistently attracting a growing amount of FDI, where Vietnam has wavered throughout the past two decades. Strong leadership from the top has been the factor separating the success in China and the inconsistency in Vietnam.

China

Prior to 1992, foreign investment in China was moderate and largely limited to export manufacturing. [29] The CCP had gradually opened the domestic economy to

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[28] Huang, Yasheng. Selling China: Foreign Direct Investment During the Reform Era. 2003. 3
[29] Naughton 402-403

foreign investment by creating special economic zones (SEZs). With every wave of liberalization throughout the 1980s, a new batch of SEZs were created with "lower tax rates, fewer and simplified administrative and customs procedures, and, most crucially, duty-free import of components and supplies."[30] The success of the SEZs and Deng Xiaoping's endorsement created confidence among foreign investors.

A propaganda poster of Deng's Southern Tour.

Source: www.iisg.nl

The moderate, but successful, experiment with foreign investment in the 1980s set the stage for further liberalization in the early 1990s. Following the People's Liberation Army's brutal suppression of the Tiananmen Square protests in 1989, anxiety spread throughout the world regarding China's commitment to further opening. Thus, when Deng Xiaoping took his famous Southern Tour in 1992, he reminded foreign investors of the success of the 1980s and assured them of China's commitment to liberalization.[31] As a result, since 1992 China's FDI has increased at amazing pace (see below chart).

A criticism of China's FDI reform, in fact, argues that the liberalization was too effective. According to Yasheng Huang, the PRC's success in attracting great amounts of FDI is actually indicative of an economic system that harms the ability of private domestic firms to compete while increasing China's reliance on foreign investment.[32]

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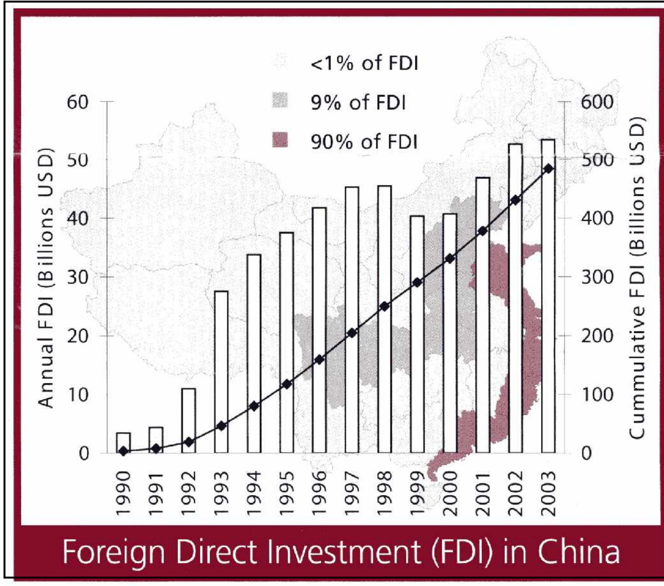
[30] Naughton 406
[31] Naughton 403
[32] Huang *xv-xvi*

Huang believes that reforming the state-owned enterprises (SOEs) should have been stressed by the leadership in order to eliminate unfair advantages that the behemoth firms have in gaining capital—both from banks and foreign investors.[33]



Following Deng's tour in 1992, China's FDI skyrocketed.

Source: www.icoste.org

Mary Elizabeth Gallagher counters this argument in Contagious Capitalism. Gallagher contends that the sequence of China's reforms (FDI liberalization before SOE reform) allowed for a less painful transition for Chinese society.[34] Instead of initially tackling ownership reform—the core of a communist state—the CCP first allowed FDI inflows to gradually increase competitiveness, and allow for a less painful restructuring of the Chinese economy.

The method and timing of China's foreign investment reforms shows strong, intelligent leadership. In order to protect domestic industry, reforms started out in limited, but successful SEZs. By restricting foreign investment to specific cities, reformers were able to assuage the concerns of conservatives in the CCP over foreign presence.

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[33] Huang 333-334
[34] Gallagher, Mary Elizabeth. Contagious Capitalism: Globalization and the Politics of Labor in China. 2005. 9

Meanwhile, provincial leaders watched jealously as cities like Shenzhen erupted overnight. Thus, the wise approach of gradual reform in the 1980s paved the way for liberalization in the early 1990s. Once China's preeminent leader Deng Xiaoping endorsed and encouraged the plan for liberalization during his 1992 Southern Tour, China's experienced exponential FDI inflows.

Vietnam

Vietnam's attempts at foreign investment reform have not been as successful. Unlike China, where FDI levels have experienced a steady rise, Vietnam has seen irregular levels of foreign investment. The blame falls primarily on the party leadership for not being able to overcome resistance within the VCP. Conservatives have opposed legislation liberalizing foreign investment, and when reform measures have passed, the leadership has failed to force local cadres into easing administrative costs for foreign firms. The VCP's success in legislating reform followed by their inability to ensure an investment friendly administration among government officials has sent foreign investors mixed signals. The result has been an inconsistent patter of FDI in Vietnam.

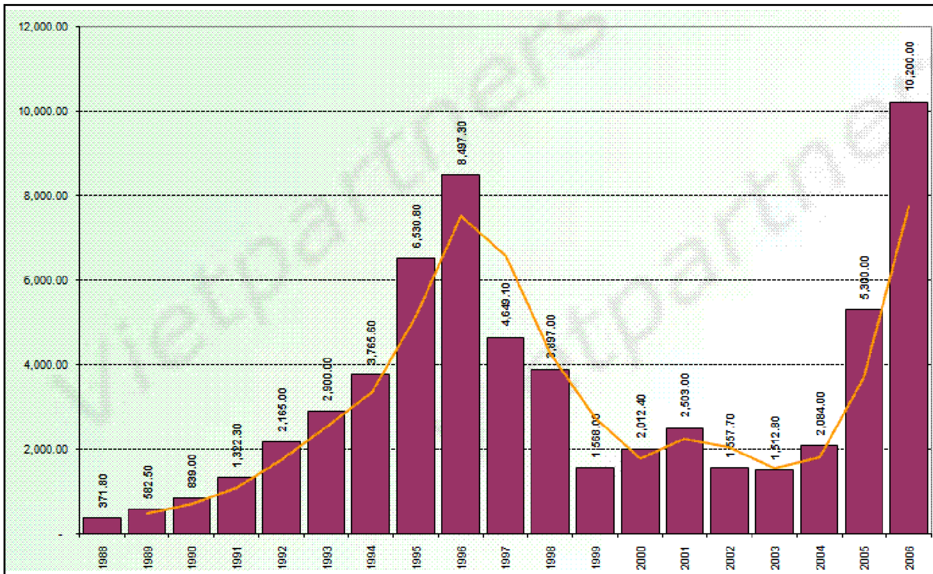
Foreign investment reform was one of the first changes carried out during *doi moi*, yet the VCP's inability to create an investment-friendly business environment has consistently shaken foreign investors' confidence. The Foreign Investment Law was the first major reform of *doi moi* and created a very liberal framework for foreign direct investment (FDI) in Vietnam.[35] The law was even amended in 1992 in an attempt to offer more incentives for investors and a more competitive market.[36] Since the adoption of FDI reform, however, VCP conservatives have dragged their feet in creating an

[35] Beresford 207

[36] Dung, Nguyen Tuan. "Foreign direct investment in Vietnam". Vietnam Assessment: Creating a Sound Investment Climate. Ed. Suiwah Leung. 1996. 69

attractive business environment for foreign investors, thus demonstrating the inability of Vietnam's leaders to enforce the party line.

Vietnam witnessed a healthy increase of FDI during the first half of the 1990s, followed by a contraction in the second half. Many scholars point to the Asian Financial Crisis as the cause of the FDI retreat, but Nick Freeman and Curt Nestor have argued that the decrease began prior to the regional collapse.[37] According to their work, the rise and fall of FDI level in Vietnam through the 1990s is "congruent with a rise and fall in foreign investor sentiment towards the country."[38] The drop-off in foreign investor sentiment was certainly influenced by the Southeast Asia investment bubble of the late twentieth century, but the decrease also points to the VCP's failure to address the true deterring factors associated with doing business in Vietnam.



Freeman and Nestor argue that the drop in FDI predated the Asian Financial Crisis. They believe Vietnam's inconsistent level of FDI has more to do with the unfriendly business environment.

Source: www.vietpartners.com

Tuan Dung Nguyen described the foreign investment environment in Vietnam in 1996. He stated that "[t]hat the main obstacles to FDI appear to lie in the cumbersome administrative procedures and bureaucratic requirements for the issuance of project

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37 Freeman, Nick and Curt Nestor. "Rethinking foreign investment in Vietnam". Rethinking Vietnam. 2004. 179

38 Freeman 188

licenses."[39] Tuan indicates that labor regulations, administrative delays, and the requirement of multiple approvals plague the process of investing in Vietnam. The author argues that the VCP has focused on legislating incentives for FDI without securing the necessary legal framework and business environment to implement investment projects.[40]

In 2002, a new law was passed that supposedly will ease administrative red tape and level the playing field for foreign investors and domestic firms. William Sharpe argues that party conservatives will likely continue to drag their feet and scare off investors.[41] Problems with the Vietnamese business environment are also seen in the rising number of wholly foreign owned enterprises (WFOEs) in Vietnam.[42] The increase in foreign enterprises wholly independent from Vietnamese managers and firms demonstrates foreign investors' desire to escape the domestic bureaucracy.

In order to achieve the necessary business environment to attract and retain foreign investors, Vietnam needs a leadership that is strong enough to motivate party officials. The lack of a strong figure like Deng Xiaoping to perform a Southern Tour, has allowed recalcitrant VCP party conservatives to repeatedly frighten foreign investors from coming to Vietnam. In the area of FDI, Vietnam's leaders have showed their inability to effectively implement and stimulate reform.

[39] Nguyen 83
[40] Nguyen 85
[41] Sharpe, William. "Foreign Investment and Trade". The Vietnamese Economy and Its Transformation to and Open Market System. 2005. 145
[42] Freeman 183

Enterprise Reform

China

Reform of enterprise ownership has been a central problem for China's leaders.[43] As mentioned earlier, ownership reform strikes at the heart of a communist society, and thus it was initially delayed by the architects of China's transformation. The CCP initially relied on infusion of FDI to increase competitiveness in the domestic economy, while slowly instituting managerial reforms in SOEs. Once this stage had utilized its effectiveness, strong leadership was necessary to steer China through a stage of "reform with losers". Zhu Rongji became the policy driver and instituted a new era of SOE reform. By the turn of the millennium, privatization had become widespread in China, but not without costs.[44] A need for further privatization contrasted by unemployment issues create a great dilemma for the current Hu Jintao and Wen Jiabao administration; history waits to see if the CCP again rises to the challenge of providing strong leadership.

Knowing that deep reform of state enterprises would shock the core of Chinese society, the CCP initially relied on gradual managerial reforms in order to increase productivity and efficiency in the domestic economy. The policy makers developed a system of incentives that shifted the focus of SOE managers "away from plan fulfillment and toward profitability."[45] Given the disastrous effects of rapid privatization in Eastern Europe and Russia, China's initial reluctance to institute deep SOE reform appears to have been an effective strategy to increase firm profitability without devastating Chinese society.[46]

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[43] Naughton 325
[44] Naughton 324
[45] Naughton 95
[46] Gallagher 20

By the 1990s, however, this strategy had run its course, and further marketization would be necessary in order to ensure China's continued growth. Deng Xiaoping's movement to the background of Chinese politics following his Southern Tour in 1992 coincided with Zhu Rongji's emergence as the dominant figure in policy making. Zhu had been a protégé of Deng, and he came to power with a reputation for a "blunt, tough style."[47] Zhu adopted an aggressive approach to reform, strongly pushing for marketization. The change of the reins indicated a shift from "reform without losers" to "reform with losers".

Zhu Rongji

Source: http://news.bbc.co.uk

True enterprise ownership reform hallmarked the second phase of China's economic transformation. The 1994 Company Law began the process of "corporatizing" SOEs. Firms were given multiple options to reform ownership through diversification, managerial buy outs, privatization, and hybrid forms. In order to encourage ownership reform, the CCP decreased and eventually ceased budgetary subsidization of SOE losses. Hard budget constraints forced SOE managers to consider more profitable modes of operation. Enterprise ownership reform increased throughout the 1990s, pushed by increasing competitiveness and a policy of "grasping the large, and letting the small go." Following the "shakeout" of weak firms in the later 1990s, privatization had become widespread in China by the new millennium.[48]

Serious ownership reform was not without consequences. "Tens of thousands of SOEs and urban collective firms were shut down. Laid-off workers totaled 40% of the

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[47] Brahm, Laurence. "Zhu Rongji: a rare talent…" South China Morning Post. 10 March 2003. Pg. 18.
[48] Naughton 102, 301-305

SOE workforce, and the urban collective workforce shrank by more than two-thirds."[49] The decision to "smash the iron rice bowl" allowed marketization to flourish, but "significant segments of society, in both urban and rural areas, [felt] left out of the prosperity they see developing around them."[50] Additionally, when SOEs stopped receiving budget subsidization, they began relying on loans from China's banks. The effect has been an increase of non-performing loans within the financial sector (to be discussed below). Zhu Rongji's aggressive restructuring policies successfully moved China towards a modern economy, but the transition was a painful one for many Chinese.

Currently the Hu-Wen regime faces the challenge of continuing ownership reform while easing the suffering of the Chinese people. Naughton notes the new administration's less aggressive, consultative approach indicates a possible movement towards a more inclusive transition.[51] Yet, in <u>China: The Balance Sheet</u> multiple prominent authors cited SOE reform as one of three critical challenges in sustaining economic growth.[52] President Hu will have to balance his promise to achieve a "harmonious society" with the need to continue marketization. Presently, it is too early to predict if the Hu-Wen regime will be able to skillfully steer the next stage of China's transformation as their predecessors have before them. The authors of <u>The Balance Sheet</u> expressed their confidence in the CCP to do so.[53]

The Chinese leaders' pursuit of SOE restructuring despite the serious societal consequences that accompany it demonstrates their dedication to reform. Many officials

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[49] Naughton 301
[50] Naughton 109
[51] Naughton 108
[52] Bergsten, C. Fred, Bates Gill, Nicholas R. Lardy, and Derek Mitchell. <u>China: The Balance Sheet</u>. 2006. 23
[53] Bergsten et al. 39

opposed enterprise ownership reform because of the position of power they held in the state economy. Additionally the job losses associated with privatizing SOEs posed a serious political threat to the CCP leadership. Nevertheless, Zhu Rongji pushed forward SOE restructuring and in so doing paved the way for China's entry into the WTO.[54] China's leadership again provided the courage and ingenuity to advance difficult reforms.

Vietnam

Vietnam has never had a state-owned economy as dominating as China's, yet enterprise ownership reform remains a great challenge for the VCP. Resistance to reform has repeatedly and consistently came from party cadres employed as SOE managers. Thus far, the VCP leadership has not had the backbone to push for enduring and meaningful reform. Despite successfully eliminating failing SOEs in periods of liberalization, the pace of reform has been described as uneven and the message of the leadership has been called equivocal.[55] Presently, the Vietnamese economy is still dominated by the state sector because the VCP leadership has failed to implement the tough reforms necessary to push past self-interested bureaucrats.

Gerard Clarke explains how leading into the 21st century, Vietnam had experienced two phases of uneven SOE reform. The first phase was spurred by the Sixth Party Congress in 1986 and "acquired real momentum."[56] Attempts to reduce the number of unprofitable SOEs brought the total from 12,000 state firms in 1989 to around 6,000 in 1992. As on might expect, cutting the amount of SOEs in half also meant cutting SOE jobs. About one-third of the SOE workforce (800,000 people) lost their jobs during this

[54] Brahm 2003
[55] Clarke, Gerard. "The social challenges of reform: Restructuring state-owned enterprises in Vietnam." Rethinking Vietnam. 2004. 93, 104
[56] Clarke 93

period.[57] In the following second phase, enterprise ownership proceeded with caution. Presumably because of the harsh social effects of the first phase, fewer than 500 SOEs were eliminated from 1992-1997. The VCP was able to both discontinue direct subsidization of SOEs and legislate provisions for privatization; however, the leadership's equivocation over the hotly contested ideological issue caused a slow pace of reform. When evaluating the recent history of ownership reform in Vietnam, the chronic unevenness outweighs the occasional successes.

The blame for slow progress in Vietnam's state sector reform lies flatly on the party leadership. Ari Kokko claims that "[t]he reason for the limited progress is clearly resistance from interest groups that fear losing their privileges."[58] The VCP leadership, however, is the actor responsible for ensuring economic development and societal interests over those of self-interested managers. The absence of hard budgetary constraints and full endorsement of restructuring provoked the World Bank to report that "reform mechanisms in place amount to an option, rather than a mandate."[59] Until the VCP tackles ownership reform, the country is stuck with overcapitalized SOEs, obsolete technology, and incompetent, corrupt managers.[60]

The VCP confirmed their unwillingness to reform enterprise ownership when they declared Vietnam to be "a 'socialist-oriented market economy', in which 'the state economic sector [plays] the leading role'."[61] In contrast, China's Fifteenth Party Congress in 1997 endorsed private entrepreneurship as a way to legitimize liberalization

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[57] Ibid.
[58] Kokko, Ari. "Growth and reform since the Eighth Party Congress." Rethinking Vietnam. 89-90
[59] Clarke 95 [citing World Bank]
[60] Kiem, Tran Van. "Prospects for Fiscal Reform in Vietnam." The Vietnamese Economy and Its Transformation to an Open Market System. 2005. 70-71
[61] Clarke 95 [citing the Government of Vietnam]

under Zhu Rongji.[62] Clearly, the Vietnam's private sector will have to help itself in developing a free market economy as opposed to relying on the help of the VCP.

SOE reform still poses many of the same challenges in China and Vietnam. Most importantly the fiscal system reforms will need to catch up to the restructuring of the SOEs.[63] Both countries will also need to find a way to balance marketization progress with the social safety of citizens.

Banking Reform

Banking reform is a difficult issue for both China and Vietnam's leaders, and it is one that was not really addressed until the current decade. Although China is slightly ahead in the process, an IMF policy discussion paper has noted that the patterns of reform in the two countries have been similar.[64] The banking institutions had long been burdened by the state intervention of the planned economy that led to insecure lending to SOEs. Policy-driven lending to SOEs often turned into nonperforming loans (NPLs). China did not begin to truly address banking concerns until the aftermath of the Asian Financial Crisis in the late 1990s, when Zhu Rongji implemented stricter budget constraints and attacked NPLs.[65] Vietnam took a more timid approach[66], but recently private and foreign banks are proving to be adept at catching up to international standards. At this point, it is too early to judge the success of China and Vietnam's banking reforms, but patterns indicate that again Chinese leaders have again been able to steer the path

[62] Shih, Victor. "Partial Reform Equilibrium, Chinese Style." Comparative Political Studies. 21 Aug. 2007.
[63] Kokko 89
[64] Unteroberdoerster, Olaf. "Banking Reform in the Lower Mekong Countries." IMF Policy Discussion Paper 2
[65] Naughton 461
[66] Nghia, Nguyen-Xuan. "Banking Reform in Vietnam." The Vietnamese Economy and Its Transformation to an Open Market System. 202

towards liberalization, while in Vietnam the progress of reform has been more dependent on private sector influences.

China

Naughton describes the banking sector as "one of China's most protected industries, overregulated, dominated by state ownership, and protected from international competition," and states that until recently it was "lagging behind" other aspects of development.[67] In the present decade, however, China has had to make many changes in order to meet requirements for entry into the WTO. Currently, the banking sector is in a period of transformation.

China's reform efforts began in the late 1970s, but initially changes were primarily limited to restructuring rather than liberalization. In his text China's Unfinished Economic Revolution, Nicholas Lardy explains how on the eve of reform China only had three banks: the People's Bank of China, the Bank of China, and the China Construction Bank. The Agricultural Bank of China was created soon thereafter to complete what would become known as the "Big Four" of China's banking sector.[68] In the 1980s, the People's Bank of China became the central bank while its depository and lending function was taken over by the newly formed Industrial and Commercial Bank of China (ICBC).[69] During the first era of reform, smaller joint stock commercial banks (JSCBs) were also created. Examples of JSCBs include the Bank of Communication and regional banks like the Guangdong Development Bank and the Shanghai Pudong

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[67] Naughton 450
[68] Lardy, Nicholas R. China's Unfinished Economic Revolution. Washington, DC: Brookings Institution Press, 1998. 61
[69] Lardy 64

Development Bank.[70] These banks, however, played a much smaller role than the giants that were of key concern during this period. Again, the restructuring of the 1980s should not be mistaken as liberalization.

The "Big Four" of Chinese Banking

Source: www.wikipedia.org

During the era of restructuring, the Big Four served primarily as a means to distribute budgetary money to state enterprises. The ICBC funded industrial and commercial SOEs, the Agricultural Bank lent to rural enterprises, and the Construction Bank financed new building projects. Withstanding a slight increase of competitiveness across sectors, the banks served the function of government lending institution.[71] The nature of the Big Four's role in the economy led them to take on an astonishing amount of NPLs. The fact that the banks paid little or no effort to classifying the quality of loans led to the realization in 1995 that the Big Four as a group had a negative net worth.[72] Restructuring had established a clearer organization of banks in China, but greater reform was necessary to achieve a functioning financial system.

Efforts aimed at liberalization of the banking sector did not really begin until the late 1990s. At this time, in an effort to avoid a China Financial Crisis and as WTO entry came near, Zhu Rongji implemented a two-pronged strategy to deal with the two main

[70] Lardy 66-70
[71] Lardy 65-66
[72] Lardy 119

problems facing the Chinese banking sector.[73] The first was institutional reform. Provincial-level branches that had brewed corruption were replaced by regional branches similar to the US Federal Reserve Board.[74] The restructuring allowed for greater central control and the ability to implement stricter banking and lending standards. The abundance of NPLs was the second severe problem for Zhu to tackle. He established asset management companies (AMCs) to buy the NPLs from banks and recapitalized banks that were still suffering. Theoretically, the AMCs would relieve banks of the burdens of the planned economy era, while allowing them to focus on employing wise lending practices in the future.[75] The leadership was criticized for only deferring the risk of NPLs into AMCs, but Zhu avoided a "China Financial Crisis" and by 2005 the AMCs had eliminated two-thirds of the debt they had assumed.[76] Despite the success of the late 1990s reforms, the Chinese banking sector still had a long way to go before meeting international standards.

Around the turn of the millennium, the CCP made banking reform a priority, but unwise lending and poor management still abound. As when they were created, the Big Four still comprised the majority of the market and are weighted down by NPLs and poor management. The weaknesses of the Big Four stem from the old planned economy—policy mandated lending and poorly educated, politically-appointed managers. The smaller JSCBs demonstrated "younger, more highly trained staffs and considerably lower amounts of bad loans on their books."[77] Since the JSCBs had less of a connection with

[73] Shih, Victor 1250
[74] Naughton 103
[75] Shih 1250-1251
[76] Naughton 463
[77] Naughton 456

the planned economy, they had been able to improve lending practices and attract young, better-educated staffs.

The CCP took notice of the success JSCBs had experienced, and in 2003 the Central Committee officially agreed to slowly restructure the Big Four into JSCBs.[78] A recent report by Kumiko Okazaki of the RAND Corporattion explained how the multiple stages of the banking sector's transition. The process began with further capital injections by the government and a second round of NPL absorption into AMCs. Once the Big Four's books were in better shape, the PRC moved towards attracting foreign strategic investors to the SOCBs. In addition to capital, the foreign *strategic* investors were expected to bring greater corporate governance and management practices to China's behemoth banks. Finally, the Big Four were listed publicly to complete their transition to joint stock status (Note: the Agricultural Bank of China is yet to list). As a result of foreign strategic investment and public listings, the Bank of China, the Industrial and Commercial Bank of China, and the China Construction Bank have improved accounting methods and information disclosure.[79] The CCP has successfully transformed three of the Big Four into joint stock banks with foreign strategic investment and the Agricultural Bank should follow suit in the near future.

Additionally, the introduction of domestic operations for foreign banks in December 2006 will continue to increase competition and therefore banking practices.[80] According to Ozakazi, the PRC is betting on a "win-win" strategy where they will create

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[78] Okazaki, Kumiko. "Banking System Reform in China: The Challenges of Moving Toward a Market-Oriented Economy." Santa Monica, CA: The RAND Corporation, 2007. 25.
[79] Okazaki 27-36
[80] Okazaki 43

opportunities for foreign banks to profit and opportunities for domestic banks to strengthen. In conclusion, Ozakazi stated:

> "Chinese banks have moved decisively into the market economy. They have addressed their most serious weaknesses. They have learned from foreigners and are prepared to deal with foreign competitors. Chinese government regulations have become far more sophisticated. But important bank vulnerabilities remain, and China's financial system is still far from being able to accomplish its central task: allocating credit in an efficient way to all sectors."

Although the goal has not quite been met, the PRC has succeeded in creating the environment for liberalization. When institutional restructuring and capital injections were not achieving a healthy banking sector, the CCP made the bold—and politically dangerous—decision to increase foreign influence in the Chinese financial market. The strategy has already paid off in three highly celebrated SOCB IPOs, and the Chinese banking sector is now well positioned for full liberalization.

Vietnam

The banking scenario in Vietnam is quite similar to China's past. The sector is mainly composed of a few large SOCBs in addition to smaller JSCBs. Vietnamese banks are historically not profitable and like China's they are heavily burdened by bad loans due to state-ordered lending.[81] Also, like China, Vietnam's banking sector is in a period of great change. Reform efforts have received poor marks from scholars, but Vietnam may be at the tipping point that China approached at the conclusion of the 20th century.

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[81] Unteroberdoerster 3

Vietnam's early banking reforms look very similar to those of China. In 1988, the government split the state bank to form four SOCBs: Vietcombank, Industrial and Commercial Bank, Investment and Development Bank of Vietnam, and Vietnam Bank of Agriculture and Rural Development. Soon after, Vietnam allowed the establishment of JSCBs. Like in China, the SOCBs engaged in state-ordered lending and soon found themselves drowning in NPLs. The Vietnamese banking sector experienced the other problems of China's past, as well, including poorly trained managers and policy driven lending. [82]

Nguyen-Xuan Nghia criticized the VCP's efforts at banking reform for many of the same reasons addressed in foreign investment and enterprise ownership reform. In his work "Banking Reform in Vietnam", Nghia claims the following are impediments to progress: "(1) the consensus-based leadership that lacks an individual or group of individuals aggressively pushing for change, (2) the risk aversion of the Communist Party of Vietnam (VCP) which has avoided giving the private sector a more active role, and (3) powerful vested interests in the state apparatus."[83] Congruent with the VCP's disappointing leadership in other aspects of reform, Vietnam's top officials have thus far fallen short in addressing banking reform.

To be fair, it is possible that Vietnam is just now reaching the tipping point that the Chinese financial sector met around 2000. The VCP now finds itself attempting to clear the WTO commitments that China recently tackled. Realizing the challenging requirements of WTO accession and after experiencing a small crisis due to weak lending in 2000, Vietnamese leaders have attempted to push for a more stable banking sector.

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[82] Nghia 202-203, 209
[83] Nghia 202

Recapitalization and restructuring plans have tried to put SOCBs on a "commercial footing".[84] Additionally, VCP leaders have repeatedly stated their commitment to improving accounting practices and lending standards. Nghia argues, however, that given the ideological constraints of the VCP and the ineffectiveness of the government, delays should be expected.[85]

Evaluating Vietnam's Recent Progress

The preceding empirical studies have shown two equally distinct patterns in China and Vietnam. The reform embarked upon by the CCP in 1978 has met extreme success, continually being pushed forward by the strong leadership of Deng Xiaoping then Zhu Rongji. In contrast, Vietnam's path toward economic liberalization has been rocky, experiencing great setbacks because of the absence of strong leadership. For China, the trend has continued to date. Although history has not allowed enough time to completely judge the Hu-Wen administration, all signs indicate that they are handling China's growth prudently and effectively.[86] Fortunately for the Vietnamese people, the bumpy trend of reform may have come to a close. Since 2001, Vietnam has witnessed renewed growth and persistence in reforms.

A recent International Monetary Fund (IMF) report on the state of Vietnam's economy revealed great successes over the past five years. For one, the GDP has consistently been driven upwards, with growth at 7.1% in 2002 and a projected 8.3% growth for 2007. During the same period, Vietnam has witnessed an extraordinary boom in the stock market and increasing amounts of FDI. Most importantly, in the past year

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[84] Nghia 204-205
Oberdorersheien 4
[85] Nghia 212
[86] Bergsten et al. 39

Vietnam has successfully entered into the WTO. The hallmark event means that Vietnam will have to continue to liberalize and address the remaining problems from the planned economy. Overall, the IMF reported that Vietnam's "near-term outlook remains broadly favorable."[87]

Two possible explanations can account for the return to progress in Vietnam.

Relying on Outside Sources

The VCP's history of wavering leadership and ineffectual reform certainly leaves doubt over whether the party is responsible for Vietnam's recent success. An alternate explanation is that the Vietnamese economy has instead turned to outside sources. After years of disappointing leadership, the Vietnamese people may have grown tired waiting and instead took up the initiative to privatize the economy. This explanation rings true with Gainsborough's argument that the VCP's reforms were merely official approvals of formerly existing informal changes.[88] Developments in Vietnam's recent past also support the idea of reform relying on sources outside of the VCP.

In the area of foreign investment, private firms in Vietnam have created industrial parks (IPs) that fulfill the needs not being carried out by the VCP. The main cause for the unstable FDI inflows in Vietnam was the VCP's lack of commitment to creating a friendly business environment for foreign firms. Potential investors were discouraged by Vietnam's excessive red tape and corruption. Recently, private developers have built IPs that remove the startup hassles of business in Vietnam.

A 2005 Foreign Affairs article by Sandie Robb outlined the advantages of IPs. The author highlights the benefits of the Amata Industrial Park located near Ho Chi Minh

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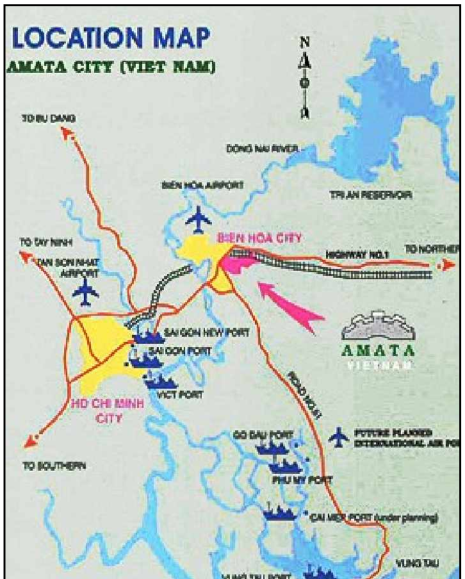
[87] IMF. "IMF Executive Board Concludes 2007 Article IV Consultation with Vietnam." 21 Nov. 2007.
[88] Gainsborough 109

City. The Amata grounds boast "a bank, a post office, a customs office, freight forwarders, sports facilities, a cafeteria and a medical centre." Robb adds that:



Source: www.business-in-asia.com

"Many IPs act as a 'one-stop shop' for the requirements associated with legal bureaucracy that can so often frustrate investors. Building permits, worker recruitment, licensing and other activities can take months rather than years because the parks often have a direct and strong relationship with local authorities."[89]

By providing foreign firms with the roads, facilities, and service of the Western world, private IPs are making Vietnam a much more attractive location for FDI. Given the prediction that IPs will attract approximately $7B of FDI between 2006-2010,[90] the argument that private sector efforts have driven Vietnam's recent turnaround is worthy of consideration.

Developments in the banking sector also support the idea of progress being pushed by forces outside the VCP leadership. Reports throughout the 2000s have shown how private banks and JSCBs in Vietnam have bettered their operations and attracted foreign investment. A WTO case study illustrated how Dong a Bank had increased its

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[89] Robb, Sandie. "Investors Eye Favorable Environment." Foreign Affairs. Sep/Oct 2005: Vol. 84, Iss. 4. 3
[90] Ibid.

capital ten times over fifteen years and accounted for 70% of total currencies in Vietnam. The authors point out that the largest SOCB had not met this achievement.[91]

Additional stories highlight the successes of privatized JSCBs. A 2003 Far East Economic Review article showcased Lam Hoang Loc, a Vietnamese banking executive who turned the privatized Vietnam Joint-Stock Bank for Private Enterprise around. The energetic businessman stressed how he would focus on improving customer service and professional ethics. According to an interviewee, Loc's strategy is working; the customer stated he had converted to the private bank to avoid "under-the-table" costs associated with SOCBs.[92] Other JSCBs have pursued better banking practices by opening up to foreign investors. Recent Wall Street Journal reports have illustrated how preeminent Western banks like HSBC, Deutsche Bank, and Citibank are seeking ownership in Vietnam's smaller, privatized banks.[93] The attempts of Vietnam's JSCBs to improve banking practices either through acquiring bold leadership or through foreign strategic investors demonstrate how the recent progress in reform may be driven by entrepreneurs, not VCP members.

A reliance on Vietnamese citizens for advancing marketization would not be a shock, given the VCP's lackluster leadership during the 1990s. Such a trend does not necessarily represent a well-conceived movement by the private sector. Instead, it is

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[91] Sam, Phan Vam and Vo Thanh Thu. "Preparation by Viet Nam's Banking Sector for WTO Accession." Managing the Challenges of WTO Participation: Case Study 45. No date provided.
[92] Cohen, Margot. "Vietnam's savvy private banks." Far Eastern Economic Review. Hong Kong: 17 July 2003. Vol. 166, Iss. 28; pg. 42.
[93] Hookway, James. "Vietnam, Ripe for Retail Banking; Citi, Others Move to Build Business When Rules Ease." The Wall Street Journal. New York: 30 April 2007. Pg. C5.
Linebaugh, Kate. "Global Banks Continue Their Push Into Vietnam." Wall Street Journal. New York: 2 Feb. 2007. Pg. C3.
Wall Street Journal. "Banks Plan Vietnam Operations To Help Expand Retail Networks." Wall Street Journal. New York: 20 July 2007. Pg. A10.

possible that efforts outside of the VCP's leadership have consistently progressed while those under the party have stagnated. Over time, a pattern appears in which Vietnamese citizens are driving change while the VCP is trying to keep up. This argument rhymes true with Fforde and de Vylder's "fence-breaking" theory of the 1990s, in which policymakers have played a passive role in reform.

A Leader Emerges

An alternate theory is that Vietnam has finally found their equivalent of Deng Xiaoping or Zhu Rongji—a tough proponent of reform. With strong advocacy from the top, Vietnam may have been able to more firmly pursue a transformation to a free market during *doi moi* and the 1990s. Vietnam's FDI levels may have grown consistently if they had a Deng Xiaoping and a Southern Tour. Although history has not yet granted enough time to fully judge, Vietnam may have found their man.

In 2001, the VCP Secretary General Le Kha Phieu entered the Ninth Party Congress standing accused of "ineffective leadership, failure to revive Vietnam's stagnant economy, inability to root out widespread corruption in the party, and 'antidemocratic' behavior."[94] The politically conservative Phieu was viewed as being "out of touch with a re-emerging reformist trend."[95] Naturally, the man who replaced him was viewed as more of a vehicle for change—someone who would actually work to rein in the bureaucracy and re-attract foreign investment.[96] Vietnam's new leader was Nong Duc Manh. Within months, Manh outlined key priorities for Vietnam: strong leadership,

[94] Thayer, Carlyle A. "Vietnam in 2001: The Ninth Party Congress and after." Asian Survey. Jan/Feb 2002: Vol. 42, No. 1. 81.
[95] StratFor. "Vietnam: Seeking Balance in Reform." 16 April 2001.
[96] CNN. "Vietnam endorses new leaders." 28 April 2001.

economic development, and SOE reform.[97] Manh's foci for improvement struck at the heart of the VCP's failures during the 1980s and 1990s.

The first step in strengthening party leadership was to attack weak leaders. Manh made clear his intentions to fight corruption amongst the VCP.[98] In 2003, the government pressed corruption charges against two high-profile former VCP Central Committee members. At the risk of weakening party legitimacy, Manh attacked corruption in the highest echelons.[99] Since high levels of corruption were cited as deterrents for foreign investment in the 1990s, the struggle to clamp down is strongly related to Vietnam's economic growth. By increasing the ethics of the VCP and the government of Vietnam, Nong Duc Manh hopes to secure FDI to fuel continued growth.

Nong Duc Manh represented a fresh change for the VCP. He immediately reinvigorated the efforts for reform and tackled hard issues like corruption.

Source: vietnamembassy-usa.org

The fight against corruption is only one of several tactics the VCP has adopted to reinvigorate foreign investor interest in Vietnam. Since 2001, Vietnam has capitalized on state visits, economic conferences, and business meetings to focus the foreign investment community's attention on the Mekong Delta. In 2005, Prime Minister Phan Van Khai's visit to the US was highly celebrated as the first official visit since the end of the Vietnam

[97] Thayer 84
[98] Thayer 85
[99] StratFor. "Communist Dilemma: Expose Corruption, Maintain Legimitacy." 26 Feb. 2003.

War. The VCP leadership, however, was concerned with reminding America of the future, not the past. As the PM toured the country, he visited not only with President George W. Bush and Defense Secretary Donald Rumsfeld, but also with business executives from Microsoft and Boeing.[100] In the following year, the VCP utilized the hosting of the Asia Pacific Economic Cooperation (APEC) Council to exhibit the country's improved infrastructure and business environment.[101] The meeting of the regional economic powers provided a perfect opportunity for Vietnam to demonstrate its progress and attractiveness for FDI. Although the backdrop of these events may be state visits and economic conferences, the VCP has continually been focused on exploiting these occasions to highlight Vietnam as a FDI destination.

Signals indicate that the strategy of Manh and the VCP is working. A recent UN survey ranked Vietnam as the sixth-most attractive global destination for FDI. Ahead of Vietnam were the behemoths of China, India, the US, Russia, and Brazil.[102] Given its relative size disadvantage, Vietnam's ability to evenly compete among the other giants is remarkable. To date, FDI commitments have continued to surge as the current levels are up 36% from one year ago.[103] As Vietnam persists in promoting its benefits as a destination for FDI the inflows increase, fueling the growing economy.

General Secretary Nong Duc Manh's dedication to fighting corruption and increasing FDI certainly has played some role in Vietnam's renewed growth. The contrast between Vietnam under Manh's leadership and the era of his predecessor is stark. Prior to his election to the VCP's top post, economic reforms had stagnated due to

[100] StratFor. "Vietnam: Shopping for a Bigger Share of U.S. Investments." 20 June 2005.
[101] StratFor. "Vietnam's Big Chance." 15 Nov. 2006.
[102] EIU. "Country Report: Vietnam." Nov. 2007. Economist Intelligence Unit. 10.
[103] EIU 14

conservative foot dragging. The equivocation in implementing reform stemmed from the top down because of the concerns of vested interest groups. Manh's coming to power represented a true commitment to reform. Since 2001, Vietnam has attacked the tough phases of its transition to a free market economy and the results have been impressive. Although the country is still struggling with SOE reform and bureaucratic regulation, Vietnam has displayed significant success in attracting FDI and battling corruption and their progress is expected to extend to other aspects of reform.

Chicken or the Egg

After observing both the driving force of Vietnam's citizenry in pushing forward marketization and the pivotal role of Nong Duc Manh's leadership in reinvigorating reform, the question remains as to which element has been the greater factor in Vietnam's renewed progress. On one hand, the mobilization of the Vietnamese people towards marketization may have created the circumstances that allowed Manh's coming to power. As party members became involved with successful private sector practices—became jealous of those who were involved—the VCP as a whole may have became more reform friendly. Thus, the "re-emerging reformist trend" that elevated Manh to General Secretary may have been driven by Vietnam's private sector. On the other hand, the recent successes in the private sector can be credited to the market-friendly reforms under Manh. Private banks would not be competitive, JSCBs would not attract foreign investors, and IPs would not be built, if the government of Vietnam did not grant its permission. Therefore, it is more enlightened to see the two elements of Vietnam's renewed progress as playing off one another and making intertwined contributions to the country's growth.

The collaborative efforts of the VCP and the private sector can be seen in the past few years. For instance, in the Prime Minister's visit to the US in 2005, he was accompanied by 80 Vietnamese entrepreneurs in addition to the official government ensemble.[104] The rare inclusion of private businessmen in an official state visit demonstrates how the VCP is embracing the additions of the private sector in the reform process. Similarly, the VCP has taken hints from the successful privatization of JSCBs and will be launching an IPO for the large SOCB Vietcombank in late 2007. Following the IPO, Vietcombank will seek foreign strategic investors, similar to the strategy of the Chinese Big Four.[105]

Vietnam has linked government entities and private sector forces in progressing reforms, and the result has been mutually beneficial. Instead of one entity or group pushing forward liberalization, the VCP and the private sector have benefited from one another. The VCP has pushed forward banking reforms after seeing the successful transitions of JSCBs. Also, Vietnam is relying on its entrepreneur to recruit FDI during state visits. Meanwhile, the private citizens of Vietnam are enjoying an increasingly liberalized economy, allowing for growth and development. Both parties to Vietnam's economic progress deserve credit for the country's success as they have played off one another.

Conclusion

Both China and Vietnam have made impressive transformations towards free market systems. Vietnam, however, has just recently gained leadership strong enough to push through the necessary reforms to become a healthy, liberalized economy. Prior to

[104] StratFor. "Vietnam: Shopping for a Bigger Share of U.S. Investments." 20 June 2005.
[105] Thomas, Beth and Nguyen Dieu Tu Uyen. "Vietcombank Will 'Definitely' Sell Shares This Year, Ha Says." Bloomberg.com. 20 Nov. 2007.

Nong Duc Manh's ascendancy to General Secretary of the VCP, Vietnam's reform efforts had been characterized by equivocation and a reliance on entities outside the party to advance change. The VCP had been forced into accepting reforms in the late 1970s as the populace grew weary of socialist collectivization plans and shortages caused by decades of war. In some cases the party was simply legalizing illicit market activities that had been taking place prior to reform. [106] The VCP's approach towards liberalization throughout the rest of the 20th century reflected this "forced hand" mentality. The leadership endorsed reforms to keep up with informal market activities, but never had the backbone or political power to force vested party interests into compliance. As a result, the pace of SOE reform was slow and uneven and foreign investors were scared off by rampant corruption and bureaucratic red tape. The weak leadership of the VCP effectively stalled Vietnam's liberalization for the last quarter of the 20th century.

China's transformation starkly contrasted that of Vietnam as popular leaders consistently pushed through reforms. The process of introducing China to a market economy started slowly and purposefully. Deng Xiaoping was able to overcome conservative opposition by initially restricting liberalization to select cities. Support for reform grew as the SEZs succeeded. When greater liberalization efforts began in the early 1990s, Deng was able to capitalize on his leader status to reinvigorate reforms in his famous Southern Tour. Soon after Deng successfully kick-started the second phase of reform, Zhu Rongji took over China's the economic reigns. Yet again, the CCP installed a strong leader, dedicated to economic progress. Zhu pushed China through the tough "reform with losers" stage and prepared the country for entry into the WTO. Presently, the Hu-Wen administration is again demonstrating steady leadership as they continue

[106] Gainsborough, Martin. "Political economy of post-doi moi Vietnam". Rethinking Vietnam 48

SOE reforms and the marketization of the banking sector. Consistently, throughout the history of China's reform era, strong leadership has been able to rally the CCP around necessary reforms and continue the push for development.

Although both China and Vietnam are now performing extremely well economically and demonstrating a commitment to liberalization, Vietnam's path has not been as steady as China's. The current VCP leaders should look to past mistakes and hope to learn from them. In China, the Hu-Wen administration should persist in the steps of their predecessors. With continued dedication to liberalization, China and Vietnam will eventually complete their transformation to a free market economy.

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