The Vietnam Economic Success Story – A Model for North Korea?

The meeting of North Korea’s Kim Jong-un and US President Donald Trump in Hanoi has focused global attention on how Vietnam has transformed its economy from one that was highly controlled to nowadays, a “socialist-oriented market economy” that genuinely fosters entrepreneurialism. Numerous reports suggest that Vietnam’s single-party communist state is being studied as a model for North Korea as it considers ways to modernize and integrate its economy, presumably once it denuclearizes and international sanctions are lifted.

When that will happen is anybody’s guess. What is undeniable, however, is Vietnam’s successful transformation over the past 30 years has been remarkable. Begun in earnest with the implementation of “Doi Moi” in 1986, the reform of Vietnam’s economy has seen the country go from one of Asia’s least developed countries (1990 GDP per capita: USD95) to one with the second-highest GDP per capita growth in the world (after China), according to The Economist. For a country with a population of 96 million, GDP per capita in 2018 stood at nearly USD2,600 on average, higher in the major urbanised cities like Hanoi and Ho Chi Minh City where it reaches USD6,700 per capita. The poverty rate plummeted from 50% in the early 1990s to below 3% today. GDP has grown from USD6.5 billion in 1990 to USD238 billion in 2018.

At the foundation of this extraordinary development was the 1987 Law on Foreign Investment, which opened the country to international participation in its economy. The impact was immediate:

- Foreign direct investment (FDI) inflows soared to 10% of GDP by 1994, which caused GDP growth to surge from around 4% in 1986-1990 to over 9% annually by the mid-1990s.
- The country went from suffering widespread food shortages in the early 1980s to becoming the world’s #3 rice exporter in the 1990s (Vietnam has since fallen to the world’s #5 rice exporter, as other higher-value added crops have displaced rice, such as the world’s #1 exporter of black pepper and #2 exporter of coffee).
- Tertiary education enrollment soared five-fold between 1991 and 2001, laying the foundation for the country’s sustained, stellar growth in the many years after the Doi Moi era. In fact, Vietnam now regularly ranks in the top 10 of the OECD’s PISA test ranking of high school students in more than 70 countries.

The government also embarked on a campaign to reduce the number of state-owned enterprises (SOEs). In the 1980s, there were an estimated more than 14,000 SOEs, a number that dropped to around 3,000 in 2015 and, today continues to decline. Some have been merged into others, while many have been privatized (or equitized as the process is called in Vietnam), selling some or a majority of shares to the private sector and outsiders, including foreigners. In addition to raising needed capital for infrastructure, health care and education, the move away from state ownership

---

1 “Doi Moi”, which translates to “renovation” in English, refers to the series of economic reforms implemented by the 6th National Communist Party Conference in 1986, and formed the foundation of the shift toward a socialist-oriented market economy.

2 The Programme for International Student Assessment (PISA) is administered by the Organization for Economic Cooperation and Development, and measures the effectiveness of educational systems in 79 countries. The test covers reading, science and math, and is administered every three years.
has been driven by a recognition that motivation to succeed, innovate and make profits rises when there is an alignment of interests between senior executives, who typically become shareholders, and the state. While the SOE equitization process has been far from smooth sailing, the government continues to make progress on reducing its stakes in non-strategic companies while at the same time generating significant funds for the treasury.

The Proven East Asian Development Model

The Vietnamese government has been following the “East Asian Development Model,” which Japan, South Korea, Taiwan and China have all used to transform their own economies and increase the wealth and welfare of their citizens. This involves land reform, which increases agricultural productivity, the wealth generated from which is then channeled into the development of an export-oriented manufacturing sector. China and Vietnam have accelerated this process by encouraging FDI (something Japan, South Korea, and Taiwan did not), and today, FDI accounts for nearly 8% of GDP in Vietnam. At the peak of FDI inflows into China in the 2000s, that figure never got much above 3% of GDP.

Growth from Manufacturing

In less than three decades, Vietnam has become the most globalized country in modern history. Consider that in the 1980s, Vietnam’s state-owned industrial base was weak, and manufactured products accounted for less than 20% of the country’s exports at the time with more than two-thirds (70%) of the workforce employed in agriculture. Today, just 40% of the workforce is in agriculture, which accounts for about 20% of exports and 10% of GDP. In contrast, manufacturing accounts for 20% of Vietnam’s exports, and high-tech products such as mobile phones contribute about one-third of exports. Since 2009, when Samsung shifted most of its production to Vietnam, the country has become the world’s second-largest producer of smart phones after China.

Exports plus imports are over 200% of GDP, much higher than any other country at present (excluding city-states like Hong Kong or Singapore) or even in modern history, according to the World Economic Forum. The second highest is Thailand at 122% of GDP.

This staggering growth has come about in large part due to formerly insular Vietnam’s pivot to greater engagement in the global economy. Vietnam has attracted approximately USD350 billion of FDI in 26,000 foreign-owned projects, according to government statistics. The foreign-invested sector currently contributes one-fifth of Vietnam’s GDP. The country is signatory to more trade agreements than any other in South East Asia, with 16 bilateral and multilateral trade agreements, including the CPTPP. Tariffs on imports have plunged from nearly 20% in 2000 to around 2% at present. According to a recent survey from the Pew Research Center, 95% of Vietnamese polled believe that “trade is good” for the country.

Growth of Middle-Class Fuels Overall Optimism

Manufacturing jobs tend to pay better wages than agriculture, and this has been a key factor in the growth of Vietnam’s middle class, which today we estimate stands at about 20% of Vietnam’s population of 96 million. Another factor has been the implementation of policies that foster entrepreneurialism. Vietnamese people have long been inclined to start their own businesses, many growing into reasonably significant enterprises. Global market research firm Nielsen consistently ranks Vietnamese consumers in the top ten most confident. Beyond the middle class, the ranks of the “ultra-rich” have also grown. According to Vietnam Investment Review, the country currently lays claim to nine billionaires (USD terms).

Wealth creation, whether via the equitization of SOEs or the growth of SMEs and the private sector, has put Vietnam on a reasonably solid economic footing that facilitates continued growth for the foreseeable future. When the first stock exchange opened for trading in 2000, there were two listed companies with a market capitalization equal to 0.28% of GDP by the end of that year. Today, there
are more than 1,000 listed companies across three bourses, with a market capitalization in excess of 70% of GDP. Similarly, economic growth has allowed the State Bank of Vietnam to increase FX reserves to over USD60 billion, 30 times what it was in 2000, and equivalent to about 3 months’ worth of imports, a level that is considered prudent according to the World Bank and IMF.

**Vietnam’s Future Continues to be Bright**

Vietnam’s GDP growth is likely to remain robust in 2019 with consensus forecast of 6.7%, moderating slightly from the 7.1% pace the economy enjoyed last year. This is no cause for alarm, since the primary drivers for economic growth remain in place: strong manufacturing output, robust FDI inflows, long-term capital commitment from global investors, and a buoyant and optimistic middle-class consumer.

Other headline macro-economic indicators for 2019 also appear encouraging. The Vietnam Dong (VND) is forecast to devalue only 1-2% for the year, in line with average currency devaluations in recent years, and most important, at levels that are far less volatile than regional currencies. Inflation is expected to reach 3.5% and interest rates appear to be holding steady. Finally, structural tailwinds from Vietnam’s superior demographics continue to support the countries long term growth trajectory. Today, almost 36% of the population live in the major cities, and we expect that proportion to increase by 1% per year over the next few years.

Opportunities for investment in Vietnam remain abundant. The price-to-earnings ratio of companies listed on the Ho Chi Minh Stock Exchange is 15 times, a discount to regional peers, especially when listed Vietnamese companies are reporting earnings growth of 15-20%. Sectors that cater to the growing needs of the middle class, such as consumer discretionary, healthcare, education, and real estate, continue to offer great investment opportunities. An upgrade to emerging market status by MSCI will be a significant catalyst to further market growth. Beyond the stock market, what excites us are the opportunities in private equity and venture capital. There are hundreds of growing Vietnamese companies that are not ready to list but are looking for investment as well as the expertise and networks firms like VinaCapital provide. The technology scene is also seeing rapid growth, as entrepreneurs take advantage of low costs and a large talent pool, and venture capital investors are once again seeing the market’s potential.

**Will North Korea Follow Vietnam’s Lead?**

Vietnam’s evolution from an inward-looking country rebuilding after decades of conflict to one of the world’s most globally integrated, vibrant economies has been extraordinary. But the path has been winding, and at times it looked as if commitment to reform had stalled. Fortunately, today’s leaders recognize the need that continued progress requires further reforms to liberalise the economy.

North Korea’s situation is unique, and its direction unclear. But once that country is in a position to itself one day open up to the larger world, Vietnam’s experience has clearly shown the benefits of doing so in a balanced and considered way.

**Disclaimer**

© 2019 VinaCapital Group (VCG). All rights reserved. This report has been prepared and is being issued by VCG or one of its affiliates for distribution in Vietnam and overseas. The information herein is based on public sources believed to be reliable. With the exception of Information about VCG, VCG makes no representation about the accuracy of such information. Opinions, estimates and projections expressed in this report represent the current views of the author at the date of publication only. They do not necessarily reflect the opinions of VCG and are subject to change without notice. VCG has no obligation to update, amend or in any way modify this report or otherwise notify a reader thereof in the event that any of the subject matter or opinion, projection or estimate contained within it changes or becomes inaccurate.

Neither the information nor any opinion expressed in this report constitutes an offer, or an invitation to make an offer, to buy or to sell any securities or any option, futures, or other derivative instruments in any jurisdiction. Nor should it be construed as an advertisement for any financial instruments. Officers of VCG may have a financial interest in securities mentioned in this report.

Any financial instruments discussed in this report may not be suitable for all investors. Investors must make their own financial decisions based on their independent financial advisors as they believe necessary and based on their particular financial situation and investment objectives. This report may not be copied, reproduced, published, or redistributed by any person for any purpose without the express permission of VCG in writing. Please cite sources when quoting.