

Ohno Kenichi, Nguyen Duc Thanh, Pham Thi Huong

VIET NAM PRODUCTIVITY REPORT

IDENTIFYING GROWTH CHALLENGES AND EXPLORING A WAY FORWARD



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INTRODUCTION AND KEY FINDINGS

Productivity is a key concept in economic growth and welfare. It measures how much is expended in terms of effort and materials and how much is produced in terms of goods and services as a result. If large output is obtained with small input, productivity is high and the nation can enjoy a high living standard. If only little value is produced despite large effort and material input, productivity is low and the nation is likely to be trapped in either low or middle income. There are some nations richly endowed with natural resources such as oil, gas, diamond, copper, and the like relative to population size, which permits high income without making much human effort. But most other nations devoid of such given advantage, including Viet Nam, must accumulate knowledge, skills, and technology to climb the industrial ladder, step by step, to high income. For such nations, attaining high income and improving productivity are essentially the same thing. That is why productivity enhancement is critical for Viet Nam's socio-economic development. Viet Nam can attain high income only if it improves productivity significantly from the current level.

The Vietnamese economy is under constant pressure from deepening global and regional integration and the future risk of a middle income trap. Despite the reasonably high growth attained in the last two-and-half decades, Viet Nam's productivity and innovation remain low, and Vietnamese enterprises generally have not secured sufficient competitive advantage to cope with the global market. This Report studies Viet Nam's productivity focusing on labor productivity and total factor productivity (TFP). It analyzes the process of productivity growth of the entire economy, across sectors and over time, as well as by making comparisons with neighboring countries.

Two remarks are in order. First, we need to differentiate the level and the growth rate of productivity. Both are important but point to different aspects of economic performance, and we will study both. Viet Nam is a country that has an average growth rate of productivity within ASEAN, but the absolute level of productivity is still low. If this situation continues, it may take a very long time for Viet Nam to rise to high income. Growth must be accelerated from the current low base.

Second, productivity is a quantity-based measure which asks how many goods and services are produced per unit of input. In addition to quantity, nations must also pursue quality and innovation. Productivity, quality, and innovation are different concepts even though there are overlaps. Original and high-quality products are the hallmark of an advanced economy, and professionally trained and innovative human resources are required to generate them. Productivity, quality, and innovation are all important, but their relative importance should shift as the economy moves from an early to late stages of industrialization. A nation in an early industrialization stage producing garment, shoes, and electronic devices for export under foreign instruction and management, such as Viet Nam, must attain high efficiency to be integrated into the global value chain. Then, gradually, the nation's product mix must be upgraded from "cheap, common, and standard" to "upmarket, original, and high quality." Finally, the nation should aim to become a creator of new goods and services keenly demanded globally, which bring high income and profit to those who invent and commercialize them.

This Report will concentrate on productivity. This does not mean quality and innovation are unimportant for Viet Nam, but the current status of Viet Nam as a lower-middle income country with mostly borrowed technology calls for deep analyses and effective policies focusing on productivity instead of a broader and more ambitious research. When most workers remain unskilled and factories are operating inefficiently, it is difficult for Viet Nam to conquer the global market with high quality and innovation. Industrial challenges must be taken up in proper sequence without jumping necessary steps. We will focus on

the basics of productivity improvement such as business management, factory efficiency, workers' skill and attitude, administrative and logistic efficiency and the like, which directly impact productivity but are not yet effectively and widely practiced in Viet Nam, rather than frontline technologies such as bio-tech, AI, IoT and Industry 4.0. These things will become critical when Vietnamese factories operate at world-class efficiency and Vietnamese workers are well-trained and disciplined, and when Viet Nam is ready to move up from upper-middle income to high income.

Part I of the Report defines productivity and discusses issues related to the measurement of productivity (Chapter 1), then examines the past and current state of labor productivity in Viet Nam from various angles at both the economy level and sector level (Chapter 2). Growth accounting and shift-share analysis methods are used on the data from the General Statistics Office (GSO), the Asian Productivity Organization (APO), and others to estimate the factors contributing to Viet Nam's labor productivity growth (Chapter 3). We also compare the status of Viet Nam's productivity with those of selected economies in Northeast Asia and ASEAN (Chapter 4). Viet Nam's past and current policy efforts in improving labor productivity and TFP are reviewed (Chapter 5). Assessment of the current state of productivity in Viet Nam and the results of policy efforts in the post-Doi Moi period are valuable inputs to reform productivity policy in the future.

Part II explores the possibility of availing of additional Japanese cooperation to introduce globally acknowledged Japanese productivity methods to Viet Nam, with proper selectivity and adjustment. We believe this will become an important pillar of productivity enhancement in Viet Nam if implemented effectively and sustainably. We examine general principles that need to be followed in adopting any foreign productivity models, and study the case of how Singapore learned from Japan in the 1980s (Chapter 6). We then explain ten concrete productivity tools and methods originating in Japan and introduced to many other countries for initiating productivity movements with the help of the Japan International

Cooperation Agency (JICA), the Japan Productivity Center (JPC), and other Japanese public and private organizations (Chapter 7).

Our key findings are summarized in the following eight points.

First, Viet Nam’s economy-wide labor productivity has increased over time but its speed was moderate and unstable. Unlike countries that have achieved high economic development in the rest of Asia, Viet Nam has not experienced a period of very rapid productivity increase that allows an economic take-off to high income. In absolute value (constant 2010 price), labor productivity of the whole economy grew from VND 18.29 million per worker in 1990 to VND 68.40 million per worker in 2019, or by 3.74 times. On annual average, the growth was 4.65% from 1991 to 2019. Any rapidly industrializing economy is expected to attain higher labor productivity growth than this within a quarter century. China, which had labor productivity similar to Viet Nam in 1990, raised it by 8.98% annually or 9.4 times by 2017. Thus, Vietnam’s past productivity performance was good but not spectacular. Because of this, Vietnam’s speed of catching up with high-income economies has been slow (Chapter 2).

Second, Vietnam’s labor productivity evolved in three distinct stages: high growth (1991-95), stagnation (1996-2012) and recovery (2013-). In the first stage, Viet Nam steadily eliminated barriers to market and decisively integrated into the international community. These efforts were behind the initially remarkable growth in Vietnam’s labor productivity, which peaked at 7.13% in 1995. This was a reviving of economic growth from past suppression and returning to the path which the nation was supposed to tread. There was efficiency catchup within each industry (“within effect”) and rising capital intensity as constraints on private business activities were removed. Meanwhile, labor force remained relatively stable in both quality and quantity. In the second stage starting from the mid-1990s, labor productivity growth slowed down. The Asian financial crisis in 1997-98 and the global financial

crisis in 2008-09 disturbed the Vietnamese economy. More importantly, growth increasingly relied on heavy capital investment with declining capital efficiency. Lackluster productivity performance continued into the new millennium. From 2000 to 2012, labor productivity growth was only 3-4% per year. In the third stage, the situation began to improve and labor productivity growth approached the speed in the first stage (until the COVID-19 pandemic hit the national as well as global economy in 2020). TFP's contribution to labor productivity rose to as high as 73% in the period 2011-19, while the contribution of capital intensity declined. The main engine of growth shifted from heavy investment to true efficiency improvement. However, the reason for this desirable change remains largely unknown (Chapter 2).

Third, looking at the broad three-way sectoral classification, labor productivity growth was highest in the industry and construction sector (secondary industry), followed by the service sector (tertiary industry). Meanwhile, the agriculture, forestry and fishery sector (primary industry) had the lowest labor productivity growth as well as level. Even so, labor productivity growth of industry and construction, which together accounted for nearly 42% of GDP, was not spectacular by global standards, and it even began to decelerate around 2001 when Viet Nam was still a low income country. After growing rapidly in the 1990s, manufacturing labor productivity remained stagnant in the 2000s and 2010s. This slowdown was premature because dynamism of the manufacturing sector should continue for at least a few more decades to take the country to high income (Chapter 2).

Fourth, by ownership type, labor productivity of the FDI sector declined significantly beginning in the early 2000s while those of the state and non-state sectors increased steadily. The low and even declining labor productivity of the FDI sector is surprising because FDI was supposed to bring high technology and global competitiveness to Viet Nam and especially to Vietnamese enterprises, which is clearly not happening. A large part of FDI inflow has been into the manufacturing sector. In the early 2000s, the composition of FDI manufacturing

projects shifted dramatically from capital-intensive to labor-intensive ones having relatively low productivity per worker. The disappointing performance of labor productivity of the FDI sector may largely explain why labor productivity of Viet Nam's manufacturing has hardly risen since 2001, and why Vietnamese enterprises are still unable to participate meaningfully in global value chains. Suspicion is that the majority of foreign manufacturers regard Viet Nam as a location to engage in unskilled labor-intensive production—sewing, food processing, parts assembly and other simple processes—and the Vietnamese government has not introduced policies to counter this notion by greatly advancing domestic value. The situation of low manufacturing productivity perpetuates even after a quarter century of global integration. Viet Nam seems stuck at the bottom of the Smiling Curve, which illustrates high value creation in upstream (R&D) and downstream (global marketing) and low value creation in midstream (processing and assembly). Meanwhile, the increase in labor productivity of the state sector partly came from a series of reforms such as the streamlining and equitization of state-owned enterprises. This process eliminated low-productivity state activities and left highly capital-intensive industries in the public sector, thus pushing up the average labor productivity. Labor productivity of the non-state sector remains very low despite improvements over the years (Chapter 2).

Fifth, the shift-share analysis shows that the driving force of labor productivity in the period 1991-2015 was the within effect (improvement in each sector) though there was also a subperiod, from 2001 to 2010, when the shift effect (labor movement across sectors) was the dominant contributor. However, the shift effect recently subsided even though a large proportion of Vietnamese labor still remains in rural areas and engaged in low productivity agriculture, and industrialization is far from complete. This premature slowdown of inter-sectoral labor movement may point to the existence of barriers to labor mobility such as the small size of production and market of sectors with high labor productivity, or the lack of skills in Vietnamese workers who cannot meet the labor

requirement of globally competitive industries. Put more positively, there is much room for Viet Nam to improve overall productivity by removing such barriers and stimulating labor mobility across sectors. Experiences of early industrializing economies such as Northeast Asian economies and Singapore show that the within effect, which is primary, and the shift effect should both be dynamic and interactive to sustain high productivity growth. In Viet Nam's development stage, which is lower middle income, both effects need to be greatly re-activated (Chapter 3).

Sixth, when compared with selected Northeast Asian and ASEAN countries, Viet Nam's labor productivity is still very low despite reasonably high economic growth in the past two-and-half decades. In 2017, labor productivity of Viet Nam's nine sectors (following the APO's industrial classification) was at or just above the lowest level in the region. Viet Nam's labor productivity was the lowest in construction; and transportation, storage, and communications. It was the second lowest, only above Cambodia, in agriculture, forestry and fishery; manufacturing; electricity, gas and water supply; wholesale and retail trade, repair of vehicles and household goods, hotels and restaurants; and community, social and personal services. Meanwhile, Viet Nam's performance was closer to average in mining and quarrying; and financial intermediation, real estate, renting and business activities (Chapter 4).

Seventh, Viet Nam has made policy effort to improve labor productivity by establishing the Viet Nam Productivity Institute (VNPI) in 1997 and preparing conditions for national productivity enhancement, which was also called "quality growth". In the First Decade of Quality (1996-2005), a number of foreign productivity methods were introduced to Vietnamese enterprises to raise productivity while ensuring quality. The Second Quality Decade (2006-15) expanded and prototyped additional models. In 2010, National Program 712 targeted TFP's contribution to GDP of at least 35% by 2020, and this target was achieved already in 2018. After two decades of effort, a policy framework has been laid and

agencies and experts accumulated experience. Nevertheless, productivity movement in Viet Nam is still partial and fragmented, focusing only on the business sector and covering only some aspects of productivity. As explained above, Viet Nam's productivity remains near the bottom of the region and the productivity movement is top-down rather than being driven by the initiatives of individuals, firms and community groups. Productivity agencies and their mandates are scattered in different ministries which makes policy coordination difficult. Productivity policy needs to be integrated at the national level, by establishing the National Productivity Council or a similar high-level mechanism, with strong authority to direct and monitor implementation (Chapter 5).

Eighth, support for productivity enhancement has been offered through international cooperation, especially from Japan and the Asian Productivity Organization (APO). This has contributed greatly to Viet Nam's productivity movement, but more is needed because current productivity performance is far from the desired level. This Report lists ten Japanese productivity methods which produced good results in Japan and many Asian countries and the rest of the world, but not yet introduced to Viet Nam in earnest. Viet Nam should study them carefully and choose some of them for execution in proper sequence, with selectivity and adjustment to Viet Nam's reality. Viet Nam may also learn productivity from other countries, but it is advisable to start with Japan because the Japanese government is ready to cooperate further, and the Japanese business community is also willing. At the same time, the learning must not be passive but effectively owned and promoted by the Vietnamese side. Viet Nam can learn technical aspects of productivity from foreigners, but administrative and institutional mechanisms that spread good practices must be homemade because political, economic and social circumstances differ from country to country. Copying foreign tools works only to a certain point, beyond which a truly domestic system is needed to design and implement policies in a way most suitable for Viet Nam. Viet Nam's Productivity movement must be "Made in Vietnam" (Chapters 6 and 7).



The Vietnamese economy is under constant pressure from deepening global and regional integration and the future risk of a middle income trap. Despite the reasonably high growth attained in the last three decades (1990-2020), Viet Nam's productivity and innovation remain low, and Vietnamese enterprises generally have not secured sufficient competitive advantage to cope with the global market. This Report is the first comprehensive study on Viet Nam's productivity focusing on labor productivity and total factor productivity (TFP) in a continuous time span of three decades. It analyzes the

process of productivity growth of the entire economy, across sectors and over time, as well as by making comparisons with neighboring countries, using different methods.

When most workers remain unskilled and factories are operating inefficiently, it is difficult for Viet Nam to conquer the global market with high quality and innovation. Industrial challenges must be taken up in proper sequence without jumping necessary steps. Instead of discussing the frontline technologies such as bio-tech, AI, IoT, blockchain, etc. of the Industry 4.0, the author argues that the basics of productivity improvement such as business management, factory efficiency, workers' skill and attitude, administrative and logistic efficiency and the like, should be widely understood and effectively practiced in Viet Nam. The latest technologies will become more relevant when Vietnamese factories operate at world-class efficiency and Vietnamese workers are well-trained and disciplined, and when Viet Nam is ready to move up from upper-middle income to high income.