## V. The Vietnamese Government Controls Resource Allocation and the Price and Output Decisions of Enterprises.

### A. Summary of Comment

The Government of Vietnam sets prices throughout the economy, impeding the potential operation of free market forces. It also controls capital and non-capital resource allocation, as well as the output decisions of enterprises.

### B. The Department's Standard

Section 771(18)(b)(v) of the Act directs the Department to consider "the extent of government control over the allocation of resources and over the price and output decisions of enterprises." In the Department's analysis of this factor, it focuses on the extent to which a country's economy is characterized by decentralized economic decision-making.[1] Evidence of decentralized economic decision-making includes "independent investment, input-sourcing, output and pricing actions" by individuals and companies "in pursuit of private gain."[2] Such private and independent market actions ensure efficient allocation of resources and generate prices that "tend to reflect both demand conditions and the relative scarcity of the resources used in production."[3]

Other factors relevant to the extent of government control over resource allocation and the output decisions of enterprises include: the number of goods and services subject to price controls, whether the central bank is independent of the government, whether the government is the primary allocator of capital, and the extent to which the government controls non-capital

[1] See Russia NME Memo at 17; Kazakhstan NME Memo at 12.
[2] Russia NME Memo at 17; Kazakhstan NME Memo at 12.
[3] Russia NME Memo at 17; Kazakhstan NME Memo at 12.

resource allocation.[4] In past analyses, the Department has particularly noted whether a government controls the banking sector in a country because banks "typically are the primary allocators of capital" and "where capital markets are underdeveloped, . . . it is particularly relevant to determine whether the government controls the banks."[5]

The Department has only conferred market economy status on those countries in which price controls, if any, were minimal and limited to such goods and services as public transportation, utilities, and postal and communication rates.[6] In most market economy countries whose status has been determined by the Department, the central bank operated independently of the government, generally adhered to tight monetary policies to control inflation, and did not have any interest in commercial banks.[7] Interest rates were set by non-governmental commercial banks, and banking sector reforms were instituted that, among other things, established non-governmental commercial banks as the principal allocators of capital.[8] Foremost in the Department's analysis has been evidence of state abdication of control over capital allocation in favor of market-based mechanisms.[9] A commercial banking sector that behaves as a financial intermediary,[10] or the absence of state mechanisms for capital allocation[11] indicate market-based capital flows.[12] These conditions do not exist in the Socialist Republic of Vietnam.

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[4] See, e.g., Russia NME Memo at 17; Kazakhstan NME Memo at 12.

[5] Russia NME Memo at 17.

[6] See id. at 17; Kazakhstan NME Memo at 14; Czech NME Memo at 12; Hungary NME Memo at 14; Latvia NME Memo at 15; Poland NME Memo at 23; Slovak NME Memo at 12.

[7] See Russia NME Memo at 17, 18; Kazakhstan NME Memo at 13, 14-15; Czech NME Memo at 14; Hungary NME Memo at 15; Latvia NME Memo at 17; Slovak NME Memo at 13.

[8] See Czech NME Memo at 14; Slovak NME Memo at 13.

[9] See Russia NME Memo at 18.

[10] See Kazakhstan NME Memo at 15.

[11] See Russia NME Memo at 18.

[12] Id. at 19; Kazakhstan NME Memo at 15.

### C. Analysis

As described below, the Vietnamese government still overwhelmingly controls the composition, production, and distribution of outputs in the Vietnamese economy. The government directly sets output targets and prices, allocates commodities and resources, and establishes centralized guidelines for the economy. State-control of the economy also results in prices that do not reflect market-based supply and demand conditions.

#### 1. The Government Maintains Pervasive Price Controls Throughout the Vietnamese Economy.

The Vietnamese government controls price-setting throughout the Vietnamese economy. Although the Vietnamese government's August, 2002 letter to the Department noted only that it establishes price levels in the electricity, postal service, telecommunications, and fuel industries,[13] in fact, it maintains pervasive control of pricing in Vietnam. In addition to the industries noted by the Government of Vietnam, the Vietnamese Government Pricing Committee ("GPC") also directly sets prices in many other industries such as the cement, steel, iron,[14] sugar, fertilizer,[15] and coal[16] industries. Furthermore, the Vietnamese government maintains direct control over prices set by government-run monopolies or oligopolies, described below, and industries that receive important government protection, such as the automobile and motorcycle

[13] See Letter from Ambassador Nguyen Tam Chien of the Socialist Republic of Vietnam, to U.S. Secretary of Commerce Donald L. Evans (Aug. 21, 2002), at http://www.vietnamembassy-usa.org/news/newsitemprint.php3?datestamp=20020821140647.

[14] See Economist Intelligence Unit, Country Commerce Vietnam, Apr. 2002 {hereinafter EIU, Country Commerce Vietnam} at 38.

[15] See "Miscellaneous: Old Way of Thinking Still Depresses Economy", Vietnam News Briefs, May 13, 2002, attached as **Exhibit 5-1**.

[16] See "Coal Industry Loses on SOE Subsidies," Lao Dong, Sept. 30, 2002, in Development Vietnam Governance, Oct. 2, 2002, at 14 (stating that the Vietnamese coal industry asked the Prime Minister to raise the price of coal sold to the electricity, cement, fertilizer, and paper industries), attached as **Exhibit 5-1**.

industries.[17] State-control over price setting in these industries provides clear evidence of Vietnam's nonmarket economy status.

The government is able to achieve such pervasive control in part because of the enormous role of state-owned enterprises ("SOE") in the Vietnamese economy. In each of the electricity, aviation, and telecommunications industries, for example, the relevant SOE has at least an 80% market share.[18] Other industries that are heavily regulated by the Vietnamese government such as the cement, sugar, minerals, banking, and petroleum industries are generally dominated by a state-owned oligopoly comprised of several large firms that each has a market share of 10-40%.[19] Major Vietnamese SOEs occupy industries including agriculture and food, banking and finance, construction materials, electricity, insurance, minerals, oil and gas, seafood, shipping and transport, and textiles and garments,[20] aiding the government in directly prices in certain areas of the Vietnamese economy. This significant economic role for state-owned companies results in high prices, an inefficient and uncompetitive business environment,[21] and ensures the Vietnamese government's continuing control over the Vietnamese economy. Due to state-control of SOE price-setting, the price structures of monopolies are "hard to monitor, giving rise to hurdles to business,"[22] and further ensuring the Vietnamese government's control of the Vietnamese economy.

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[17] "Reality and Solutions," Saigon Times Magazine, Sept. 20, 2001 (authored by a senior expert at the Central Institute of Economic Management, which is aligned with the Vietnamese Ministry of Planning & Investment), attached as **Exhibit 5-1**.

[18] See EIU, Country Commerce Vietnam at 36.

[19] See id.

[20] See id. at 10-11.

[21] See id. at 36.

[22] "Reality and Solutions," Saigon Times Magazine, Sept. 20, 2001 (authored by a senior expert at the Central Institute of Economic Management, which is aligned with the Vietnamese Ministry of Planning & Investment), attached as **Exhibit 5-1**.

In an additional barrier to free market decision-making of enterprises, the Vietnamese government requires that foreign enterprises operating in Vietnam pay generally higher rates for goods and services than domestic consumers.[23] Such dual pricing effects pricing in the electricity and telecommunications sectors, and prices for television advertising, water, and transportation.[24] This type of government control also precludes price liberalization and reflects Vietnamese centralized economic decision-making.

Even new measures recently adopted by the Vietnamese government prolong centralized decision-making regarding prices. The Ordinance on Pricing, referred to by Ambassador Chien in his August, 2002 letter to Secretary Evans, that will not be implemented until 2003, allows the Vietnamese state to "even out any imbalances between demand and supply to ensure that prices are stable" and will "regulate the supply of commodities for home consumption and export, while exports, imports and reserve commodity trading will be closely monitored to curb speculation and hoarding."[25] And in another example of centralized economic decision-making, the Ministry of Trade plans in the future to "coordinate with ministries and state agencies to examine input costs for export goods {and} maintain the regime of exempting export quota fees and customs fee for exported goods."[26] Additionally, the Vietnamese government intends to continue, even under the most recent regulations, to fix prices for all "land, water surfaces and important natural resources; State assets to be sold or leased; and monopoly goods and services" and, in an important "catch-all" category that will leave significant room for the government to control pricing throughout the Vietnamese economy, "for goods and services important for the

[23] See EIU, Country Commerce Vietnam at 38.

[24] See id.

[25] "Pricing Authorities Draft Blueprint to Promote Stability, Curb Dumping," VNS, Mar. 29, 2002, at http://vietnamnews.vnagency.com.vn/2002-03/28/Stories/16.htm, attached as **Exhibit 5-1**.

[26] "Strategy to Counter Weak Exports," Dau Tu, Sept. 11, 2002, in Development Vietnam Governance, Sept. 18, 2002, at 3, attached as **Exhibit 5-1**.

national economy and people's livelihoods."[27] The Vietnamese government also may "stabilize" prices by adjusting supply and demand of domestic, imported, and exported goods, and by controlling stocks of goods, or by setting maximum and minimum prices.[28]

As evidenced by these new policy pronouncements, the Vietnamese government has no plans to let the market broadly determine costs and prices in the Vietnamese economy. In fact, in the telecommunications and electricity sectors, for example, the Vietnamese Government Pricing Committee recently explained that "conditions for lawful competition have not been created . . . so the Government must still fix prices. When the conditions for competition are established in these sectors, when there's no abuse of monopoly status to increase prices and harm consumers' rights, the State will consider phasing out its direct intervention in price-fixing."[29]

Finally, in a further example of the degree to which state-control of the Vietnamese economy pervades daily transactions, state-run "grassroots market control agencies" have a role in Vietnam's price-setting.[30] While information on these local market control agencies is sparse,

[27] "Much-Anticipated Price Regulations Unveiled," VNS, June 1, 2002, at http://vietnamnews.vnagency.com.vn/2002-05/31/Columns/Legal%20Bulletin.htm. Ordinance 40-2002-PL-UBTVQH10, effective July 1, 2002, gives the state power "to fix prices (either specific prices, standard prices, price scales, or maximum/minimum prices)" in the industries listed herein. A synopsis of the Ordinance is attached as **Exhibit 5-2**. Although it is described as a "stop-gap" measure pending implementation of the Law on Competition, only some elements of the Ordinance appear to relate to antitrust or monopoly pricing controls.

[28] "Much-Anticipated Price Regulations Unveiled," VNS, June 1, 2002, at http://vietnamnews.vnagency.com.vn/2002-05/31/Columns/Legal%20Bulletin.htm, attached as **Exhibit 5-1**.

[29] "Pricing Laws Won't Stifle Competition," VNS, May 31, 2002, at http://vietnamnews.vnagency.com.vn/2002-05/30/Columns/Interview.htm, attached as **Exhibit 5-1**.

[30] Id.

it appears that municipal and provincial governments also exercise some degree of control over the setting of prices at the local level.[31]

### 2. The Vietnamese Government Controls Capital Allocation Through Control over the Banking Sector.

Vietnam's banking industry is "tightly controlled" by the Vietnamese government.[32] The State Bank of Vietnam ("SBV") operates under strict Vietnamese government control, has a mandate to (1) manage the Vietnamese state budget and the state reserve, and to (2) serve as a commercial bank and supply capital to the Vietnamese economy.[33] Inherent in the SBV's mandate is the recognition that the Vietnamese government controls capital allocation in Vietnam.

The SBV's tasks include operating as the central bank of Vietnam, issuing legal instruments on currency and banking operations, and generally managing the activities of Vietnamese credit institutions.[34] Additionally, the SBV controls the four state-owned commercial banks ("SOCBs"), which comprise 80% of the Vietnamese banking sector.[35] The SOCBs lend to SOEs as a matter of policy,[36] their services are essentially reserved for the Vietnamese government,[37] and they are reluctant to make private loans.[38] Through the SBV and the SOCBs, the Vietnamese government is the primary allocator of capital in Vietnam. The

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[31] See, e.g., "Pricing Department Deputy Suspended," Lao Dong, Sept. 18, 2002, in Development Governance Vietnam, Sept. 25, 2002, at 14, attached as **Exhibit 5-1**.

[32] See Maureen McLaughlin & Nigel Russell, "Banking & Finance – Vietnam," July 2002, {hereinafter Banking & Finance} at 1, available at http://www.usvtc.org/, attached as **Exhibit 5-3**.

[33] "Set for Big Overhaul," Saigon Times Magazine, Nov. 23, 2001, attached as **Exhibit 5-1**.

[34] See Banking & Finance at 1, 3.

[35] See Economist Intelligence Unit, Country Report Vietnam, July 2002 {hereinafter EIU, Country Report Vietnam} at 9.

[36] 2002 Index of Economic Freedom (Washington, D.C.: The Heritage Foundation and The Wall Street Journal, 2002) at 414 (quoting the EIU), attached as **Exhibit 6-4**.

[37] Id.

[38] Amy Kazmin, "Vietnam's Change of Heart," Financial Times, Aug. 28, 2002, attached as **Exhibit 5-1**.

SBV's predominant lending to the SOCBs, estimated to comprise 74% of all SBV lending,[39] severely restricts the level of capital available to the private sector, a de facto distortion of the cost of capital to that sector. The close relationship between banks and SOEs, "resulting from a combination of policy, historical and legal biases, continue to constrain development of a competitive banking system capable of making commercial decisions on lending."[40]

Unlike Kazakhstan, at the time the Department determined it had sufficiently transitioned to a market economy, it is impossible to conclude that Vietnam "has significantly increased the extent to which capital is allocated according to market forces."[41] Furthermore, although banks are now theoretically free to set the interest rates that they charge on loans and offer on deposits, the Vietnamese government continues to restrict the interest rates offered by the SOCBs, which occupy 80% of the Vietnamese lending market,[42] thereby effectively maintaining state control over capital allocation. Moreover, before June, 2002, during the period relevant to this investigation, the SBV set a "fundamental rate" for all loans, including those offered by non-governmental banks, which allowed banks to charge up to 30 basis points per month above that rate for short-term loans, and up to 50 basis points per month for long-term loans.[43] Under this system, banks were not able to base interest rates on the relative riskiness of particular loans, and high-risk borrowers had no access to capital.[44]

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[39] See Banking & Finance at 1, 3.

[40] John Gillespie, Margin Painter & Bob Warner, "Vietnam and Australia, Report of the Governance Sector Strategic Review," (Prepared for AusAID), Apr. 2002, at 10, available at http://www.ausaid.gov.au/publications/pdf/vietnam_governance_review.pdf.

[41] See Kazakhstan NME Memo at 14.

[42] See EIU, Country Report Vietnam, July 2002, at 9.

[43] See id. at 27.

[44] See id.

The Vietnamese government also controls capital allocation by limiting foreign participation in the banking sector. Although there are 34 joint-stock banks ("JSBs") in Vietnam, which account for approximately 15% of the lending market, foreign shareholders generally may not invest in JSBs.[45] Additionally, foreign banks are limited to particular types of direct investment they may make in Vietnam. Operating restrictions imposed by the Vietnamese government ensure that the four joint-venture banks, 27 foreign bank branches, and 53 foreign bank representative offices remain small.[46] The Vietnamese government's restrictions on onshore foreign currency transactions by most borrowers also limit foreign currency lending by foreign enterprises.[47] Given that most foreign enterprises lend to SOEs and foreign-invested enterprises "due to the scant (if any) credit history and lack of accountability of private Vietnamese companies,"[48] foreign-invested and foreign banks also indirectly play a role in the Vietnamese government's continuing ability to control capital allocation.

In practice, Vietnam continues to have a weak banking system. Despite recent reforms to the Vietnamese banking sector, the Vietnamese government, through the SBV and the SOCBs, remains in control of capital allocation throughout the Vietnamese economy.

### 3. In Contravention of Market Economy Principles, the Vietnamese Government Regulates Output and Sets Strict Production Targets, Thereby Controlling Non-Capital Resource Allocation.

The Government of Vietnam retains strict control over major sectors of the Vietnamese economy. This is accomplished through granting many state-run enterprises the opportunity to occupy a role in the Vietnamese economy that is not available to other enterprises:

[45] See Banking & Finance at 1.
[46] See id.
[47] See id. at 2.
[48] Id.

> The State believes {state-run enterprises} can fulfill the assigned task of regulating the market and prices, or can undertake social responsibility, such as for the stockpiling and export of rice and coffee, the trading of textbooks, the transport and trading of iodized salt in rural areas. Quite a few {state-run} corporations have even been assigned to do what are actually functions of administrative agencies, including planning for regional and sectoral development, and international cooperation.[49]

The Vietnamese Government controls the economy through the actions of SOEs, which compile their own regulations, have direct access to financing from the state, enjoy special treatment, have close state agency connections, and "find it easy to get their proposals approved or problems solved with top priority."[50] As a result, certain large economic sectors in Vietnam are characterized by a state-controlled monopoly. These sectors include civil aviation; telecommunications; internet; telecommunications equipment; international shipping; railway; electric power; stock market; port construction and operations, port services, bus stations, roads, etc.; imports and exports of print media products and textbooks; printing and production of movies; and cigarettes. Other economic sectors, such as the petroleum; insurance; commercial banking; cement; steel; sugar; coffee exports and imports; rice exports and imports; and non-hotel tourism industries, are characterized by a state-controlled oligopoly.[51] Control of enterprises in these industries and economic sectors provides the Vietnamese government with significantly ability to allocate non-capital resources in Vietnam.

Local state-controlled monopolies also exist in a variety of industries. Through these monopolies, the Vietnamese government is further able to control non-capital resource allocation. In a particular province, for example, it may only be possible to purchase products

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[49] "Reality and Solutions," Saigon Times Magazine, Sept. 20, 2001 (authored by a senior expert at the Central Institute of Economic Management, which is aligned with the Vietnamese Ministry of Planning & Investment).

[50] Id.

[51] Id.

such as beer or cement produced by the local state enterprise.[52] Throughout Vietnam, only local state-run food enterprises can buy and sell rice, which results in "serious market distortions" in that industry.[53] Through national and local state-control of enterprises, the Vietnamese government prevents a free market from developing and protects domestic SOEs from foreign competition.

In addition, the Vietnamese government controls allocation of non-capital resources through direct controls on private business activities such as quotas on output[54] and restrictions on imports.[55] Municipal People's Committees set the allocation of quotas for companies in Hanoi, Ho Chi Minh City, Hai Phong, and Da Nang, while the Ministry of Trade sets the allocation of quotas for all other enterprises.[56] The Ministry of Trade also controls the petroleum, glass, iron, vegetable oil, sugar, motorbikes, and nine-seat motorized vehicles industries by issuing trading licenses in these sectors.[57]

The Vietnamese government also controls resource allocation in Vietnam through its setting of annual production targets for <u>all</u> industries in conjunction with the Vietnamese Communist Party.[58] In the agriculture industry, for example, the Vietnamese government's targets involve plans to contract half of all output to SOEs by the year 2005.[59] Similarly, the

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[52] <u>Id.</u>

[53] <u>Id.</u>

[54] <u>See</u> "Vietnam Govt Releases 5 Year Trade Policy Plan for the 1st Time," <u>Asia Pulse</u>, May 24, 2001, attached as **Exhibit 5-1**.

[55] "Vietnam Revamps Export, Import Rules to Drive up Trade," <u>Xinhua</u>, Apr. 10, 2001, attached as **Exhibit 5-1**.

[56] <u>See</u> "Vietnam Govt Releases 5 Year Trade Policy Plan for the 1st Time," <u>Asia Pulse</u>, May 24, 2001, attached as **Exhibit 5-1**.

[57] <u>See</u> <u>id.</u>

[58] <u>See</u> EIU, <u>Country Commerce Vietnam</u>, at 10-11.

[59] <u>See</u> "Contracts Help Farmers, But Will Firms Lose Out?," <u>Vietnam Investment Review</u>, Apr. 1, 2002, attached as **Exhibit 5-1**.

government recently lowered production targets in the coffee industry to increase Vietnam's capacity to compete on an international level. To reach the government's new output target, coffee plantations will be decimated.[60] The Vietnamese government has also lowered land-lease fees and land-use taxes for farmers who followed farm development plans defined by local people's committees and farmed unused water and land areas.[61] These decisions and policies demonstrate the continuing pervasiveness of government control over Vietnamese resource allocation, which distorts free market forces and price determination in the Vietnamese economy.

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[60] See "Trade: VICOFA Proposes Fewer Coffee Exporters," Vietnam News Briefs, Apr. 19, 2002, attached as **Exhibit 5-1**.

[61] See U.S. Commercial Service, Vietnam Country Commercial Guide, at 62-63.