

# **Cambodia-Laos-Vietnam: Economic Reforms and Sub-regional Integration**

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## **Abstract**

This paper reviews the gradual transitions and progress of economic reforms and transformations in Cambodia, Laos, and Vietnam (CLV) since the late 1980s and the sub-regional cooperation and economic integration among the three countries in promoting economic development and poverty reduction especially along the border areas under the development triangle initiative. Liberal market economy in Cambodia, socialist-oriented market economy in Laos and Vietnam, and global and regional economic integration stay the mainstream of the political economy of development of CLV countries. State is the main actor in facilitating economic growth while the market is the driving force. With relatively high economic growth rate driven by trade openness and the inward flow of foreign direct investments, CLV countries are emerging to be an integral part of the regional economic dynamism of ASEAN and the Asia-Pacific region. However, the remaining challenges need to be tackled are institutional capacity, good governance, and labor productivity.

Key words: Cambodia, Laos, Vietnam, economic reforms, sub-regionalism

## **1.Introduction**

Cambodia, Laos, and Vietnam (CLV), gained independence from France in 1950s, had gone through prolonged war, regime changes, instability and political upheavals. Cambodia was the last war zone in the sub-region. It gained complete peace in 1999 after the death of the Khmer Rouge leader Pol Pot and the disintegration of the Khmer Rouge remaining forces. Such historical events and structural constraints backtracked these countries from the development path. Their socio-economic progress and industrialization are left far behind other Southeast Asian countries. Only in the last two decades did these countries reemerge and be

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integrated to be part of the center of economic gravity of the Asia Pacific region. With continued economic reforms and trade openness, CLV has achieved remarkable growth since 2000 with an average annual GDP growth rate of 7 percent. Due to such high economic performance, CLV is regarded as the new Asian frontier for growth within the context of ASEAN and East Asian regional generic integration. Such growth contributes significantly to reducing poverty rate and incidents. According to the World Bank's poverty rate database, in 2008 the poverty headcount ratio at natural poverty line (less than US\$ 1.25 per day) as a percentage of total population are 22.8%, 27.8%, and 16.8% in Cambodia, Laos and Vietnam respectively.

The poverty rate and incidence in Cambodia and Laos remain relatively high. It reflects the structural and institutional constraints, particularly the ineffectiveness of the governments in implementing the development policy and poverty reduction. Governance and leadership are regarded as the core element in enabling environment in favor of inclusive growth and poverty reduction. This paper aims to review the processes and related issues concerning the economic reforms and development in CLV countries and the cooperation and integration among these three countries in the context of regional integration. It sets three hypotheses. First, political will and structure are the pull factor in implementing economic reforms and opening-up. Second, economic reforms deliver results based on institutional reforms and market forces. Third, regional and global market forces are the push factor in the economic reforms of CLV countries.

## **2. Economic Reforms and Development in CLV**

Economic reforms in the CLV started in late 1980s in tandem with the abrupt collapse of the Soviet Union, the key donor country to CLV, and the end of the Cold War. Market economy was implemented within the socialist political system. However, these three countries followed slightly different paths of reform although they were inspired by the socialist market economic system. The industrialization process in these countries took place at different levels and paces with different outcomes. For Cambodia and Laos, the rate of industrialization is much slower than Vietnam's, which is mainly led by foreign investment and private sector (Amakawa, 2007). It was observed that:

All three states seek to build a new future while also accommodating the past. As their economies modernize along different lines, they often demonstrate related characteristics...at the same time they make different modifications and adjustments to exploit the unique strengths of their individual cultures and to mask their weaknesses in separate ways. In the process, all three states display a certain respect for hierarchy and an appreciation for order, moral responsibility and achievement (John 2006:200).

Cambodia, unlike Laos and Vietnam, adopted a free market economy with higher level of openness and liberalization since the early 1990s after the UN supervised general elections and the adoption of the new constitution in 1993. Since then, international development assistance and foreign direct investment played significant role in its socio-economic development. Unlike Laos and Vietnam, Cambodian political system is constructed based on liberal democracy and pluralism. Cambodia became the member of the World Trade Organization (WTO) in 2004 before Vietnam, which joined the WTO in 2006, and Laos in 2013.

The development experiences from Northeast Asia were a source of inspiration for the regional countries and it is reflected in the development agendas of the CLV. The manifestations of which are interconnected four patterns of economic development model. First, in relation to development plans, It requires stable macro-economic management; market prices, including interest rates, centered on economic and industrial policies; and the establishment of physical and institutional infrastructures and human resources. Second, in relation to development models, it is necessary to select a combination of models appropriate for the economic and social systems and history of each country with differing levels and phases of development. Third, in relation to development assistance strategies, it is essential to ensure the effectiveness of policy dialogue and the conditionalities by continuously assessing economic rationality and the political and social costs in the hope of continuously reforming policies. Fourth, in relation to the aid approach to development management, it is important that development management be considered not only from the viewpoint of administrative improvements through institutional and organizational development within the public sector

but also from practical use of the market mechanism and managerial improvements in the private sector (Kazumi 1997).

Export oriented development model and economic openness have been the two pillars of the economic reform program of CLV. Vietnam is one of the most advanced economies in the sub-region with relatively high level of industrialization. Cambodia and Laos are in the process of moving from exporting primary products to labor intensive manufacturing, and in later stages to higher value-added economy. Service industry related to travel and hospitality is one the options for development if it is managed in a sustainable way. Tourism industry is one of the key employment and income generating industries in CLV. In 2012, tourism directly contributes about 12 percent of GDP for Cambodia and Lao, and about 6 percent for Vietnam.

Over the last two decades (1990s and 2000s), CLV have experienced relatively good economic performance with an average annual GDP growth from 7 to 8 percent. Economic growth rates of CLV remain promising. In 2012, it is expected that Laos will have the highest growth with 8.4 percent, Cambodia ranked second with 6.2 percent, and Vietnam with 5.8 percent. In terms of per capita income, CLV's remain low, as compared with other countries in the region. Per capita income in Cambodia is the lowest (US\$ 760) and Vietnam is the highest (US\$ 1100) in 2012.

*Table 1: Economic Structure of CLV in 2011 (% of GDP)*

<b>Sectors</b>	<b>Cambodia</b>	<b>Laos</b>	<b>Vietnam</b>
<b>Agriculture</b>	30%	27.8%	22%
<b>Industry</b>	30%	34.8%	40.3%
<b>Services</b>	40%	37.4%	37.7%

*Source: CIA Factbook*

CLV share some similarities in terms of economic structure. Agriculture remains the key industry contributing to 27 percent of the GDP and employing about 60 percent of the total labor forces. Vietnam, a more advanced economy than Cambodia and Laos, is struggling

towards realizing its ambition to become an industrialized and modernized economy by 2020 (See Table 1).

The flow of foreign direct investment (FDI) to CLV has been stable with some certain increasing trend over the years due to political stability, stable macroeconomic performance, relatively low labor cost, financial market development, investment promotion policy, institutional environment, global and regional economic integration and openness, and some improvements in local infrastructure. Vietnam receives more than five times the amount of FDI that flows into Cambodia and Laos. It reflects the attractiveness and economic centrality of Vietnam in CLV (See Table 2). CLV needs to have a regionally integrated approach in attracting FDI especially in the CLV Growth Triangle region.

*Table 2: FDI inflows to CLV (US\$ million)*

<b>Countries</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>
<b>Cambodia</b>	483	867	815	539	783	892
<b>Laos</b>	187	324	228	319	333	450
<b>Vietnam</b>	2400	6700	9579	7600	8000	7430

*Source: UNCTAD Foreign Direct Investment Database*

The growth of production networks in East Asia since the 1980s has depended on foreign direct investment by multinational companies in countries with low wages and large pools of unskilled labor to produce manufacturing products for export (Leung *et al.*, 2010:51). Cheap labor remains competitive in CLV economies. Intensive labor industries have been the driving force of economic reforms and industrialization. There are similar wage rates between Cambodia and Vietnam (See Table 3). The key challenge for CLV economies is how to increase the wage for the workers in order to meet the high inflation rate while maintaining their competitiveness. In other words, finding ways to increase labor productivity is essential.

*Table 3: Average wages in CLV (US\$/month)*

	<b>Phnom Penh</b>	<b>Ho Chi Minh</b>	<b>Hanoi</b>
Workers (General)	101	114	96
Engineers (Mid-level)	363	265	265
Managers (Department Chief Level)	416	641	621
General staffs Non-manufacturing	225	379	372
Managers Non-manufacturing	1035	940	1013
Legal minimum wage	55	79.49	79.49

*Source: JETRO investments related cost investment survey 2012*

Although there is relatively high economic growth in CLV and the FDI flow is rather promising due to different sources of comparative and competitive advantages, CLV in the context of global competitiveness ranking remains slow. Cambodia is ranked 138<sup>th</sup>, Laos at 165<sup>th</sup> place, and Vietnam, the most competitive in the sub-region, is only ranked 98<sup>th</sup> (See Table 4).

*Table 4: Ranking in Doing Business in CLV in 2012*

<b>Topic Rankings</b>	<b>Cambodia- 138</b>	<b>Laos-165</b>	<b>Vietnam-98</b>
Starting a Business	171	89	103
Dealing with Construction Permits	149	80	67
Getting Electricity	130	138	135
Registering Property	110	72	47
Getting Credit	98	166	24
Protecting Investors	79	182	166
Paying Taxes	54	123	151
Trading Across Borders	120	168	68
Enforcing Contracts	142	110	30
Resolving Insolvency	149	183	142

*Source: World Bank Doing Business Report 2012*

CLV can be regarded as a mixed region. It is a region with high growth rates with hope and potential but at the same time it remains a poor region with relatively high poverty and inequality and also geopolitical uncertainties. The annual per capita income for Cambodia and Laos is about US\$1000 and Vietnam is about US\$1200. The poverty rate in both Cambodia and Laos is about 30 percent, and a slightly lower 15 percent for Vietnam. The income Gini Index in Cambodia, Laos and Vietnam is 41, 35 and 37 respectively (World Bank's Poverty Data). In addition, the issue of good governance (accountability and transparency) at both public and private sectors is the fundamental issues constraining inclusive and sustainable development in the CLV. According to the corruption perceptions index produced by the Transparency International in 2013, out of 177 surveyed countries, Cambodia was ranked 160, Laos was ranked 140, and Vietnam was ranked 116.

The governments of CLV have largely succeeded in implementing economic reforms and introducing major modifications to the structure of economic relations in their respective countries. The extent to which these governments have improved the livelihoods of their citizens is another issue. Their ability to build upon the economic reforms in place is also uncertain. Political reform is a separate but related issue which has proved to be even more challenging. In the political arena, too often it seems that the more things change, the more they remain the same. All three states have clearly gone beyond the end of the beginning, but each must continue to build on the reforms in place if it is to progress down the road to sustained economic and political development (John, 2006:203).

The bottlenecks of economic transition and reform are poor infrastructure, lack of human resources-especially skilled labor, and institutional weaknesses. The reform of public institutions lagged behind the needs of a rapid development of entrepreneurship and market-oriented private sector. To maintain and improve long-term competitiveness of CLV especially during the global economic downturn remains a big challenge, which requires fiscal capacity and socio-economic system resilient enough to cope with global multiple crises such the interlinked financial, economic, political, social, and ecological crises. To enhance competitiveness in the long term, the governments should modernize central banks, ministries of finances, ministries of planning and investment; upgrading of professional staffs; strengthening of judiciary and public administration reforms especially in land titling and land use rights; developing sustainable financial sector; and also improving social safety net (Leung *et al.*, 2010:4-5). In addition, both public and private sector investment in physical infrastructure needs to be increased to lower operating costs of investors; and improving governance and reducing corruption are necessary steps towards a more friendly business environment and inclusive development (Leung *et al.*, 2010:38-39).

## 2.1 Cambodia

After gaining power from the genocidal regime, Khmer Rouge, the People's Republic of Kampuchea faced serious structural and social issues. Since the beginning of socioeconomic restructuring, unlike Vietnam and Laos, Cambodia adopted relatively laissez-faire market economy with considerably free move of work forces and free trade following the creation of

mixed planned and market economy in which currency, banking and commercial transactions were restored. However, the results of the economic reforms were limited. Agricultural and industrial production was stagnant with diplomatic and economic isolation. The private sector was revitalized but with slow improvement.

In 1988, Cambodia further strengthened the role of the private sector through liberalization process. Foreign investment code and financial autonomy program for the state enterprises were introduced in the mid and late 1980s. The withdrawal of Vietnamese forces in 1989 created a huge burden in defense expenditure which later turned into serious inflation and local currency devaluation. The beginning of 1990s, especially after the Paris Peace Accord in 1991 and the general election in 1993 with the establishment of the Royal Government of Cambodia, created new opportunities for Cambodia to further reform or even transform its political and economic structure.

Economic reforms not only change the socio-economic structures but also political power structure of the state. It is argued “Cambodia’s transition in the 1990s has been based upon a transformation in the structure of economic incentives and opportunities, which has had profound implications for the organization of state power” (Hughes, 2003:13). In the National Program presented to the International Committee for the Reconstruction of Cambodia in late 1993, it focused on five pillars: promoting economic stabilization and growth by creating policies and processes for long-term economic management with the increase of foreign investment and private entrepreneurship; reforming administrative and judicial institutions through a clarification of the roles and responsibilities of the bureaucrats together with the establishment of effective and fair judicial system; ensuring structural adjustment and sectoral reform through the creation of commercial and investment codes; providing direct support for sustained development by developing infrastructure and social services and human resources development; optimizing the sustainable use of natural resources through conservation management and environmental protection.

With the introduction of liberal democratic system and free market economy, the economic reform of Cambodian was ongoing smoothly with certain progress particularly privatization and trade liberalization were the driving force of economic development. Official Development Assistance (ODA) and foreign direct investment (FDI) started flowing quickly

into the country, which contributed significantly to the success of economic reform and development although Cambodia is facing with widening gaps due to poor redistribution of economic outcomes to its people. Urban-biased development and bad governance are the remaining development issues.

Cambodia is regarded as one of the most liberal economic systems in the region due to low state intervention in the market. State capacity in effectively regulating the market is another issue. It tries to synergize export promotion and import substitution and foreign investment with regional and global economic integration. Given the nature of Cambodian economy and international economic environment, Cambodia needs to pursue economic openness and integration in the region and the world for its long-term survival. Cambodia has gradually integrated itself into the interdependent international economic system although it is more vulnerable to external shocks and uncertainties. Such foreign economic policy and philosophy positively impact on Cambodia's economic relations with her neighbors (Chheang, 2008:3).

Cambodian economic reforms are based on the five-year plan programs. The first five-year Socio-Economic Development Plan (SEDP I, 1996-2000) was formulated to focus on macro-economic growth, social development, and poverty alleviation. "Triangle Strategy" was developed based on three pillars: (1) building peace, restoring stability and maintaining security for the nation and the people; (2) integration of Cambodia into the region and normalization of relationships with the international community; and (3) promoting economic and social development. The second Socio-Economic Development Plan (SEDP II 2001-2005) was prepared with focus on economic growth and poverty reduction. For the Royal Government, the most formidable development challenge has been and continues to be the development of the private sector that is the engine of economic growth to achieve reduction of poverty and improving the livelihoods and quality of life of the rapidly growing population.

The Rectangular Strategy (another five-year program from 2004 to 2008) was initiated by focusing on Growth, Employment, Equity, and Efficiency in order to promote economic growth, generate employment for Cambodian workers, ensure equity and social justice, and enhance efficiency of the public sector through the implementation of the Governance Action Plan and in-depth reforms that are coordinated and consistent across all levels and sectors. As a

result, from 2004 to 2008, the economy grew about 10% per year, driven largely by an expansion in the garment sector, construction, agriculture, and tourism. GDP contracted slightly in 2009 as a result of the global economic slowdown but climbed more than 6% in 2010 and 6.7% in 2011. Cambodia Securities Exchange (CSX) was established as a public enterprise with government shareholding of 55% and the remaining stake held by the Korea Exchange. Currently there is one listed operating company- Phnom Penh Water Supply Authority- and the few more others are applying to be listed in the stock market.

From 2008-2013, the government carries out its second phase of the Rectangular Strategy focusing on good governance, environment for the implementation of the strategy, enhancement of the agricultural sector, further rehabilitation and construction of physical infrastructure, private sector development and employment, and capacity building and human resources development. Good governance is the core of the strategy relating to improving good governance such as fighting corruption, judicial reform, administrative reform, and the reform of the Royal Cambodian Armed Forces. Peace, political stability, social order, integration into the region and the world, favorable macroeconomic and financial environment, partnership in development are the key elements of creating an environment to implement the strategy.

After a serious setback in the 2013 parliamentary election, the ruling Cambodian People's Party (CPP) was under more pressures to concretely implement deep and comprehensive reforms otherwise it is going to lose its dominant role in the next polls and its legitimacy will be seriously challenged. At the first cabinet meeting on September 25, 2013, Prime Minister Hun Sen bluntly criticized his new cabinet and encouraged them to develop self-criticism and responsibility. He asked them to (1) reflect themselves in the mirror, (2) take a bath, (3) rub off dirt from body if there are any and (4) take treatment. He demanded both old and new cabinet members to change their leadership style and attitude by listening to the voices of the people and eliminating the so-called "family ministry". He further stated that "We must change or we will fail. We must change our attitude, way of thinking and action in delivering to the people."

The government declared a national development plan for 2013-2018, which aims to achieve four goals namely (a) ensuring an average annual growth of 7%, (b) creating more jobs for people especially the youth, (c) achieving annual poverty reduction rate at more than 1

percent, and (d) further strengthening institutional reforms and good governance. In order to realize the goals, it focuses on four priority areas which are (1) human resources development, (2) continued investment in infrastructure, (3) increasing value added for the agricultural products, (4) strengthening governance and capacity of the public institutions in order to improve the efficiency of public service delivery and investment climate.

The long-term development of the economy remains a challenge since the sources of growth are narrowly based and vulnerable to external shocks (global and regional multiple crisis), natural disaster and climate change. The widening gap between rich and poor, urban and rural areas, and weak institutions in redistributing wealth and providing social justice are some of the issues that need to be timely and appropriately addressed. Diversification of sources or bases of growth is a trajectory for future development of Cambodia.

Maintaining macro-economic stability with continued economic reform is necessary for economic development, poverty reduction, and regional economic integration. It is important to consolidate fiscal policy to finance infrastructure development and human capital. Other elements of economic reforms include moving export up the value chain and joining the regional production network; improving competitiveness by addressing the low levels of education and productivity of the work force, poor infrastructure, and poor quality of governance; creating a banking system that can address the risks of greater international financial integration; and improving agricultural sector and agri-business (Davies, 2010).

## **2.2 Laos**

Laos embarked on economic reform through the first Five-Year Plan (1981-5) with the objectives to address at least two fundamental issues which were to normalize the material and culture life of the people and all nationalities, and also building the enterprises which are strategically important to the economy and national defense with the aim to gradually and firmly build material and technical bases for the national economy. In addition, the plan also prioritizes food production and sustainable natural resources management, strengthening state enterprises, gradual process of economic decentralization and privatization, human resources development, institutional restructuring and improvement, gradual trade liberalization,

attracting more foreign assistance and investment, and efficient use of foreign development assistance.

Acknowledging the poor economic performance of the first Five-Year Plan, Lao government introduced a second Five-Year Plan (1986-1990) with more emphasis on economic decentralization. Under the New Economic Mechanism, Laos accelerated decentralization of administrative controls on pricing, production targets and wages. With the implementation of market oriented price setting policy, removal of restrictions on the internal trade of agricultural products, state enterprise reform, enhanced privatization, and expansion of economic relations with the outside world, Lao economic performance was remarkably improving in the 1990s. The private sector started to play a more significant role in expanding agriculture and service sectors. Trade openness especially with Thailand, Vietnam and China significantly contributed to the export.

Becoming the ASEAN member in 1997 and with the commitment to implement the ASEAN Free Trade Area (AFTA) in 2008, the government is required to reduce tariffs to below 5%. Fiscal reform, macro-economic stability, productivity, privatization, and export strategy were further encouraged in order to meet the new challenges and grasp the opportunities from regional trade liberalization.

In the following five-year plan (2005-2010) Lao economy has grown with an average growth rate of 7.9%. The overall macroeconomic situation has remained high with relatively low inflation rate. The sources of growth are driven by natural resources and manufacturing sectors. Agriculture is expected to benefit from the recent increase in regional demand and high food prices. While the pressure from the food and fuel prices increases, the Government recognizes the importance of diversifying the sources of growth and in enhancing prudent public financial management to ensure sufficient funding for priority health and education services (Phouphet Khamphoung, Governor Statement No. 29, September 23, 2011).

Despite this high growth rate, Laos remains a country with an underdeveloped infrastructure, particularly in the rural areas. Subsistence agriculture, dominated by rice cultivation in lowland areas, accounts for about 30% of GDP and 75% of total employment. Economic growth has reduced official poverty rates from 46% in 1992 to 26% in 2010. The economy has benefited from high foreign investments in hydropower, mining, and construction.

Laos gained Normal Trade Relations status with the US in 2004, and is taking the necessary steps to join the World Trade Organization (WTO), where its related trade policy can help improve the business environment (Index Mundi, Laos Economy Profile 2012). In 2011, Laos opened its first stock market, which currently has two listed companies: Laos's largest commercial bank, BCEL (*Banque Pour Le Commerce Exterieur Lao*) and the electricity company EDL Generation Public Company.

Lao economy is projected to continue to grow over the 7th five-year National Strategic Economic Development Plan (2011-15), with real GDP growth targeted at 8%. To achieve the socio-economic development targets and Millennium Development Goals by 2015, the government continued implementing reform agendas, by focusing on improvement of business environment, enhancement of investment efficiency, strengthening public financial management, particularly centralization of revenue administration and treasury as well as redesigning the inter-government fiscal relationship, accelerating the banking sector reform. On the economic integration into the world, the government has continued to reduce the tariff under AFTA's commitments.

Based on the assessment of the economic performance, growth has been driven largely by investment while the volume of export is very low. Several challenges for economic transformation of Laos are building sound institutions and fostering a good business environment, increase international trade through, and supporting the private sector- especially manufacturing sector and small and medium enterprises to join the growing regional production network (Ishi, 2010:110-132). However, good governance remains the core issue of realizing economic reforms with concrete results in Laos. Judicial reform has not yet made significant progress and corruption remains rampant (UNDP 2007:33-40)

### **2.3 Vietnam**

In the beginning of the 1980s, Vietnam leaders recognized the shortfall of economic policies and reforms in the country and started to introduce new economic policies to address the increasing challenges stemming from low productivity, food shortage, population growth, and low personal income. General Secretary Le Duan criticized the socialist policies by the Party after the 1975:

The deep root cause of the difficulties in the economy and daily life is the following: Our economy is still primarily one of small production, and moreover suffers the extremely heavy aftermaths of prolonged war and of colonialism... On the other hand, the difficulties have also stemmed from shortcomings and mistakes of the party and state agencies, from national down to grass-roots levels, in economic leadership and management and in the running of our society (John 2006:45).

Economic reforms started to be the key issue for the Party Congress. In the fifth party congress in 1982, the Central Committee member Truong Chinh signaled the need to reevaluate Party policies:

This fifth congress of our party will review the implementation of the line set forth by the fourth congress, correctly assess achievements and shortcomings, recognize the actual prevailing economic and social conditions and analyze the causes of successes and difficulties. It will also set forth the main economic and social orientations, tasks and targets for 1981-85 and for the 1980s (John 2006:49).

The economic reforms initiated by the Party did not produce satisfactory outcomes and failed to meet the set objectives. So more aggressive economic reforms were required. The *Doi Moi* (renovation) policy inaugurated in 1986 was the starting point for serious economic reform with concrete results and achievements of the Communist Party of Vietnam towards industrialization and modernization. There were six policy areas under *Doi Moi*: creation of independent status for public enterprises with economic and financial independence; price liberalization; ownership diversification; opening up for foreign investment; institutional support for agricultural development and incentives; and financial system reform.

One of the most important measures of reform was to develop a sound investment law that can attract foreign direct investment. The National Assembly approved the investment law in 1987, by the regional standards it is relatively liberal, in order to attract more foreign direct investment with the hope to expand its economic relations and integration with the world

economy. Inflation was effectively managed, economic growth was evident, foreign currency reserves increased, trade deficit decreased, and there was an increase in privatization in the 1990s. International donor agencies and international lending agencies especially from Japan and US also played significant role in developing infrastructure and strengthening institutions since the early 1990s.<sup>†</sup>

Based on positive results of *Doi Moi*, the party and government of Vietnam continued reforming and opening up the economy with Vietnamese characteristics. Development strategy up to 2000 was under the framework of consolidating national independence and building socialism in Vietnam in order to make the people prosperous and the country strong, advance towards modernization in a society where the people are the masters, where compassion, cultural values and discipline prevail, where oppression and injustice are banned, and where everyone enjoy a prosperous, free and happy life. The overall objectives of the socio-economic development are:

- to immediately overcome acute difficulties, emerge from crisis and stabilize the socio-economic situation.
- to strive to eradicate famine, reduce poverty, solve the unemployment problem, guarantee basic needs, improve the people's material, cultural and intellectual life, gradually accelerate domestic accumulation and attract external resources, strengthening infrastructure and effect a radical switch in economic structure in the direction of industrialization among others.
- to create more employment, accelerate economic growth, and improve people's material and cultural life (Nguyen Ba Phuc 1996:265).

From 2001 to 2006, Vietnam experienced increasing growth rate with relatively stable macroeconomic stability. But from 2007 to 2011, it faced with lower growth rate and serious macro-instability. Different policy and institutional methods were applied to deal with

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<sup>†</sup> In November 1992, Japanese government resumed broad economic ties including the offer of a major loan package. In mid-1993, the US government ended its opposition to loans to Vietnam from international lending agencies.

fluctuated economic performances. The government issued the Law of Enterprise in 2000, growth promotion policy in 2007, inflation control policy in 2008, prevention of downturn policy in 2009, recovery policy in 2010, and macro-stabilization policy focusing on fiscal and monetary policies in 2011. Although Vietnam has reduced its poverty rate from 18.1% in 2004 to 10.7% in 2010, the income gap between the 20% poorest and the 20% richest increased from 8.4 times in 2006 to 9.2 times in 2010 (Vo Tri Thanh 2012). Moreover, there are other structural problems arising from rapid economic growth such as the quality and sustainability of growth, environmental degradation, and declining contribution of productivity to growth (World Bank 2012).

Other challenges for Vietnam in the short term would be to transform the role of the government. For the medium term, it should focus on the private sector that is innovative and capable of developing international brand name products and more responsive to global and regional changing environment (Bingham and Leung 2010:91-109). The financial market, especially the banking sector, is relatively developed in Vietnam comparing with Cambodia and Laos. Founded in 2000, the Ho Chi Minh Stock Exchange (HOSE) has more than 250 listed companies. It is one of the highest growing stock exchange markets in the region. But the banking crisis stemming from mismanagement and corruption of the Asia Commercial Bank (ACB) in August 2012 has shaken financial market in Vietnam to certain extent. In addition the chronic nonperforming loans of the fragile banking system and state-owned enterprises have dragged down economic dynamism of Vietnam.

To deal with the current economic and financial crisis arising from mismanagement of the state-owned enterprises, instable banking system, and the impacts of the global economic crisis, the government of Vietnam is carrying out its efforts to implement five sets of issues including (i) continuing to implement announced solutions to stimulate domestic demand and consumption; (ii) gradually restructuring the economy; (iii) furthering the exploitation and expansion of markets for exports; (iv) actively preventing the recurrence of inflation; and (v) continuing to make good progress in poverty reduction (Nguyen Van Giau 2009).

In the Political Platform on building up the country in the transitional period towards socialism, it proposes to examine and understand a series of relationships such as the relationship between innovation, stability and development; between economic reform and

political reform; between market economy and socialist orientations; between development of production forces and construction, and incremental improvement of the socialist production relations; between economic growth and cultural development, implementation of progress and social justice; between socialism construction and socialist national defense; between independence, sovereignty and international integration; between the party's leadership, state management, and people's ownership" (Nguyen Viet Thao 2012).

### **3. CLV and Sub-regional Cooperation and Integration**

CLV countries have followed similar foreign economic policy. Opening up to the outside world and diversification of the sources of growth are the common principles shared by these countries. Regional and sub-regional cooperation is believed to be one of the core economic strategies and foreign policy objectives. The CLV sub-regional cooperation especially through the establishment of the growth triangle is being developed quite well comparing with other growth triangles in Southeast Asia. Political will is the key to development of sub-regional cooperation scheme.

#### **3.1 Political, Security, Economic Relations**

Special relationship established during the communist movements of the three countries in the war against colonialism and imperialism is the foundation of the present triangle relations and cooperation among the three countries. During his state visit to Hanoi in February 1976, Lao's General Secretary Kaysone stated "The special relationship...is the great, constantly consolidated and enhanced comradeship between two Parties which both issue from the Indochinese Community Party" (John 2006:39). Such traditional trilateral relationship and cooperation remain relevant today. Frequent exchanges of state visits and dialogue among the three countries contribute to maintaining trust, promoting mutual understanding, and deepening comprehensive bilateral relationship. Vietnam has taken a traditional leadership role in forging and strengthening this trilateral cooperation with the objective to strengthen its regional role, particularly in countering the increasing influence of China in this sub-region.

Cambodia and Laos are believed to be under strong sphere of influence of China. Vietnam-China relations matter for both Cambodia and Laos (Mitchell 2011, Storey 2004).

Strategically, Cambodia and Laos seem to move closer to China while Vietnam is getting closer to the US. To neutralize Cambodia and Lao, Vietnam has recently doubled its efforts in creating its own networks of influence in Cambodia and Lao. In addition to traditional and political security relations, economic cooperation and integration, cultural exchanges are being accelerated. Vietnam also works hard to invite other major powers such as US, Japan, Russia to the Mekong Sub-region in order to build a balance of power and strategic equilibrium in this sub-region within the context of increasing Chinese power.

It is argued that cooperation among CLV countries is vulnerable to the changing political, strategic and economic landscape in the region especially the roles and influences of the major powers. The increasing trend of strategic competition especially between China and the United States in Southeast Asian region may put CLV cooperation and unity at risk. The territorial disputes between China and Vietnam in the South China Sea, if it leads to serious tensions or even an open conflict, will create huge wave of pressures on both Cambodia and Lao in its strategic and political responses. Both Cambodia and Lao may be forced to choose side, a scenario which is not in the best interests of both countries.

Vietnam, taking its own national interest and China factor into consideration, decided to take a proactive and dynamic strategic approach towards Cambodia and Laos. Vietnam has sent its top diplomats and leaders to visit Cambodia and Laos in order to maintain and deepen strategic trust, confidence, and comprehensive cooperation. During the visit of Deputy Prime Minister Nguyen Xuan Phuc to Cambodia in August 2012, he reiterated the time-honored relationship between the two countries. In response, the Cambodian leaders emphasized the “fine traditional friendship and comprehensive cooperation between Vietnam and Cambodia...which has developed across a broad range of interests based on a philosophy of good neighborliness, traditional friendship, comprehensive cooperation and long-term stability”. In addition, Cambodian Prime Minister Hun Sen said that the country wanted to see further cooperation with Vietnam in trade, investment, tourism and culture for mutual benefits of the two neighbors' peoples (Xinhua News 17 August 2012).

At the Vietnam-Cambodia legislative friendship conference concluded in Ho Chi Minh City on 23 August 2012, the presidents of both the national assemblies of Cambodia and Vietnam committed to build bilateral relations based on the motto, “good neighbors, traditional

friendship, comprehensive and long-term sustainable cooperation” and strengthen an ASEAN community of solidarity, strength, mutual respect and support, for the common goal of peace, security, cooperation and development (Vietnam News Agency 23 August 2012). Moreover, in his three days visit on 24-26 September 2012, the Cambodian King Norodom Sihamoni reiterated the traditional friendship between the two countries and peoples. The visit also aimed to promote and further consolidate the ties of neighborliness, time-honored friendship and comprehensive cooperation between the two countries (Voice of Vietnam 24 September 2009). The two sides agreed to strengthen the relationship for the interests of the two peoples as well as for peace, stability, cooperation and development in the region and the world at large (Vietnam Plus 26 September 2012).

During the visit of the Deputy Prime Minister Nguyen Xuan Phuc to Laos in August 2012, he noted the expanding cooperation in defence-security, education and human resource training, as well as the smooth coordination between the two countries at multi-lateral forums. In addition, President Truong Tan Sang, in early September 2012, reaffirmed the great significance of the Vietnam-Laos special relations, saying that with the aim of mutual support and assistance for prosperous development in each country, the relationship contributed to creating an environment of peace, cooperation and friendship among Southeast Asian nations – one of the factors to build the ASEAN Community by 2015.

In terms of defence and security cooperation, CLV countries have been working to cooperate on human resource development, exchange of delegations and sharing of experience in political and ideological work, including resolving border security issues, speeding up border demarcation (Nhan Dan 15 July 2012). Recently, the governments of the three countries have made significant progress in finishing border demarcation. Between Cambodia and Laos, 80% of border demarcation has been completed. Between Laos and Vietnam, the two sides have agreed to complete installation of the border markers by the end of 2012 (Laos Voices 29 June 2011). On the occasion of the gathering of more than two thousands Cambodian soldiers who were trained in Vietnam to celebrate 45<sup>th</sup> anniversary of Cambodia-Vietnam relations, General Tea Banh, Deputy Prime Minister and Minister of National Defence of Cambodia reaffirmed that Cambodia would always bear in mind the Vietnamese volunteer army and

people's great support for past struggle for national independence and the present process of national construction of Cambodia and bilateral cooperation and mutual support between the two countries are proof of the everlasting solidarity (Voice of Vietnam 17 September 2012). However, border issues and nationalism remain a key challenge of cooperation among the three countries. For instance, Cambodia-Vietnam border conflict has become the key domestic political issue in Cambodia. Anti-Vietnamism in Cambodia is on the rise since it is politically driven by the opposition Cambodia National Rescue Party (CNRP).

In terms of economic cooperation, Vietnam is emerging to be one of the key investors and trade partners of Cambodia and Laos. Trade relations between Vietnam and Cambodia showed growth with a turnover of US\$2.8 billion in 2011 and is expected to reach US\$ 5 billion in the next five years by further facilitating trade across border (Saigon Giai Phong 10 March 2012). Bilateral trade between Laos and Vietnam is expected to increase from US\$1 billion in 2012 to US\$2 billion by 2015 (Vietnam News 15 August 2012). By June 2012, Vietnam had invested US\$5.2 billion in Laos (Vietnam News Agency 13 August 2012). Most of these investments are in mining, electricity, agriculture and services. The value of Vietnamese investment in Laos makes the country one of the top three Foreign Direct Investors. The other two are China and Thailand (Vientiane Times 10 July 2012). Laos and Vietnam committed to implement trade development scheme for 2008-2015, finishing the Laos-Vietnam border trade development master plan, and coordinating with Cambodia to sign the tripartite road transport agreement (Laos Voices 8 February 2012).

### **3.2 CLV Growth Triangle**

Growth Triangles involve economic co-operation based on encouraging specific and limited linkages of complementary economic activities across borders. It is a pragmatic response to the practical problems of formal economic integration among nations...Growth Triangles, as subregional economic co-operation, need not involve entire countries, but simply adjacent areas within countries that have complementary capabilities and resources (Abonyi 1996:5).

Growth Triangles (GTs) has become one of the key concepts of development economics and regionalism especially in Southeast Asia. The idea is to connect different regions or provinces along the border areas of three countries within a certain geographic setting. GTs in Asia are mainly driven by economic interest. Regional countries are expected to cooperate together in order to develop the economy to reduce poverty. Physical characteristics and different objectives of different GTs are common. In general, the key successes of GTs are economic complementarity, geographical proximity, political commitment and policy coordination, and infrastructure development (Thant and Tang 1996:1-14). To sustain the development of a growth triangle depends on the ability to maintain amicable relations and to reduce risk and uncertainty through transparent information sharing especially among the governments, private sector, and local people. Institutional mechanisms to operate and facilitate the operations of GT and mediate the differences in order to create win-win cooperation are necessary (Thant 1996: 260-1).

Besides economic consideration, GTs also has, to certain extent, political and security implications. In addition to the general perception and understanding of the positive contribution of GTs in economic development and peace, Acharya also alerted “The major security-diminishing implications of growth triangles are linked to concerns about the uneven spread of their benefits. Unless carefully managed, these concerns could contribute to greater domestic and inter-state tensions and undermine their potential to contribute to regime legitimacy of regional order” (Acharya 1996:36).

The Cambodia-Laos-Vietnam Growth Triangle was established at the first Summit in 1999 in Vientiane, Laos with the objectives to strengthen cooperation and solidarity among the three countries in order to develop socio-economy and reduce poverty, contributing to stability and peace of the three countries. Currently there are 13 provinces included in the Growth Triangle. For the Cambodian part, it comprises Strung Treng, Ratanakiri, Mondul Kiri and Kratie. For the Lao part, it consists of Sekong, Attapeu, Saravan and Champasak. And five border provinces from Vietnam, which are Kon Tum, Gia Lai, Dak Lak, Dak Nong and Binh Phuoc. These provinces have a total area of 143,900 square kilometers and population of about 6.8 million. However, the area seriously faces with poverty, geographic and climatic challenges, and poor infrastructure development.

The second CLV-GT Summit, held in 2002 in Ho Chi Minh City of Vietnam, provided guidelines for cooperation in the areas of transport, trade, energy, tourism, human resources development and health. At the third Summit in Siem Reap, Cambodia, in 2004, the leaders reaffirmed the role of the triangle in coordinating and developing physical infrastructure and initiated different development projects. At the fourth Summit in Da Lat, Vietnam, in 2006, the coordinating committee was established. The leaders committed to create a favorable environment for investment and attract more development resources especially from Japan. The sixth Summit was hosted by Cambodia in Phnom Penh in 2010. The leaders appreciated the achievements of socio-economic development in the 13 provinces located in the Growth Triangle. The leaders issued the action plans for the development of the Triangle especially in five areas namely transport, trade and investment, energy, agriculture, tourism, and environment. During the 7<sup>th</sup> Summit in March 2013 in Vientiane, the leaders of the three countries again determined to accelerate the implementation of the Master Plan of the Development Triangle area (2010-2020) and the MOU on special preferential policies for the triangle.

To realize the development objectives and ambitions of the triangle it requires financial, institutional and human resources. It is therefore necessary to get financial and technical support from the development partners. So far Japan has committed USD\$20 million in development assistance to this GT. Japan has so far played quite a significant role in developing the triangle through infrastructure development and connectivity projects. Japan committed US\$ 1.5 billion to implement the initiative for the Mekong Region Development to improve the infrastructure, such as transport, electricity and Information Communication Technology in the CLV, as priority issues of the regional development (Ministry of Foreign Affairs of Japan).

### **3.3 CLV and the ASEAN Regional Integration**

Development gap is one of the main hindrances in realizing an ASEAN Community. At the ASEAN Summit in 2000, the Initiative for ASEAN Integration (IAI) was initiated in order to narrow the development disparity within the region with the aim to enhance ASEAN's regional competitiveness and support each other in terms of development. In 2001, the ASEAN

Foreign Ministers adopted the Hanoi Declaration on Narrowing the Development Gap (NDG) for Closer ASEAN Integration. The goal of the NDG is to facilitate effective cooperation and mutual assistance to narrow the development gap among the ASEAN member states particularly assist the CLMV countries in realizing the ASEAN-wide targets and commitments.

The IAI framework covers a variety of human resource development programs expected to contribute to the objective of integrating the four newer member countries (Cambodia, Laos, Myanmar and Vietnam) into ASEAN. A training centre was set up in each of the four countries, and since 2002 the four centres have been conducting training courses for government officials in a wide variety of fields, including English language, information technology, public administration, trade and tourism management.

The first IAI Work Plan for the period 2002-2008 accomplished implementation of a total of 134 projects/programs attracting a total investment of about US\$191 million from ASEAN-6, and about US\$20 million by dialogue partners, development agencies and other partners. This does not include the other IAI related substantive support given to the CLMV, nor other projects implemented in the CLMV sub-region. The IAI Work Plan has been formulated based on the key program areas in each of the three Blueprints, the 1<sup>st</sup> IAI Work Plan 2002-2008, and the project ideas contained in the Mid-Term Review of the 1<sup>st</sup> IAI Work Plan 2002-2008.

Criteria for projects in the IAI Work Plan include identification of the precise needs of CLMV in terms of external assistance, the importance of a project's role in national development plans, its effectiveness in building CLMV capacity for participation in ASEAN programs, long term continuity and sustainability, and absorptive capacity of CLMV countries. This will ensure that IAI projects have coherence, focus, ensure adequate coverage, reflect substantive gaps in priority sectors and activities essential for integration, and more importantly are responsive to the needs of CLMV.

In the second IAI Work Plan from 2009 to 2015, it provides specific action programs to support CLMV in implementing the three pillars of the ASEAN community building namely the ASEAN Economic Community, the ASEAN Socio-cultural Community, and the ASEAN Political Security Community. It has two main activities: scientific survey and policy support intervention. It tries to identify the bottlenecks and difficulties of CLMV countries in

implementing the ASEAN blueprints and then provide capacity building support to these countries. The Work Plan is subject to be reviewed periodically to monitor the process of implementing the ASEAN blueprints and the emerging needs of CLMV countries.

In terms of resources mobilization, it comes from the ASEAN member states, ASEAN Secretariat, ASEAN dialogue partners and sectoral partners, regional and international financial institutions, private sector, foundations, and non-governmental organisations (NGOs). For instance, Singapore, the richest country in the region, has shown its economic support to implement the IAI. Singapore's initial commitment to the IAI was S\$59.5 million for a five-year period. At the 10<sup>th</sup> ASEAN Summit in 2004, Singapore extended its support commitment for a further three years, from 2006 to 2008, with a contribution of S\$28.9 million. At the 13<sup>th</sup> ASEAN Summit in 2007, Singapore reaffirmed Singapore's continued commitment to the IAI by pledging another S\$30 million to cover technical assistance projects from 2009 to 2011. At the ASEAN Summit in Bali, Indonesia in November 2011, Singapore announced an extension of its contributions to the Initiative for ASEAN Integration (IAI) for another four years from 2012 to 2015, with a total fund of S\$50 million.

The CLMV countries also created its sub-group among themselves. The first Summit among the leaders of the four countries was convened in Vientiane in 2004. In the joint statement of the 5<sup>th</sup> CLMV Summit in 2010, the leaders reasserted their commitment to promote trade and investment by effectively implementing all the existing agreements between and among the CLMV countries; further strengthen close coordination in using the economic corridors across the CLMV countries especially the East-West Economic Corridor, the Southern Economic Corridor; improve information sharing, joint research, and technology exchanges in the fields of agriculture, forestry, livestock and fisheries; further implement coordinated tourism policies and activities particularly the air link connecting CLMV major cities as well as cultural and natural heritage sites and push forward cultural connectivity among the four countries; promote educational exchanges, scholarship programs, and joint training programs, and deepen closer cooperation and integration within Greater Mekong Sub-region and ASEAN frameworks. Japan is the main donor country supporting the CLMV countries. It has provided US\$ 20 million under the Mekong-Japan cooperation framework.

#### **4. Conclusion**

Economic reforms in CLV countries are the results of both domestic and external pressures. It has produced significant economic growth and poverty reduction. Political will plays a key role in initiating and implementing those reform policies. Both state and private institutions are the catalysts of economic reforms. Economic globalization and regionalization are the push factor in facilitating the reform processes. Market-based economy with certain state's intervention and outward looking development strategy are the foundation of development strategy.

Geographical linkages, traditional friendship, and sub-regional economic relations connect Cambodia, Laos, and Vietnam in many ways. CLV is becoming a new frontier of regional integration in Southeast Asia. Continued economic policy reforms together with regional integration are taking the center stage of the governments in the sub-region. Regional cooperation on development has contributed to narrowing the development in the region through mainly investment infrastructure. The new dynamic has been undergoing in CLV with the increasing flows of investment and expansion of international trade from the region and beyond. CLV Growth Triangle is emerging to be a factor in linking border areas to promote trade, tourism, agriculture, and other sectoral cooperation schemes and narrowing the development gap within the countries since the border regions are less developed.

Improving investment climate and expanding trade relations will further strengthen and sustain economic development and help in poverty reduction in the CLV countries. To realize this, the CLV countries are required to improve both hard (especially road connectivity) and soft infrastructure (especially trade and investment facilitating measures and institutional reform) with the support from ASEAN and development partners. Good governance and institutions building require more steam in order to increase the economic competitiveness of these countries.

The pertinent challenges facing CLV are how to effectively and timely transform from economic development to poverty reduction and social protection. Investing in human resources and technology are necessary for CLV to move from cheap labor intensive industries and primary products exported economies to knowledge based and services economy. CLV need to increase labor productivity and better mechanism of wealth distribution. Inclusive

growth and sustainable development need to be conceptually integrated into development and integration discourses and implemented at local, national and regional levels.

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