

## The End of the 'Red Road' in Vietnam

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Vietnam is recovering well from the COVID pandemic. Economic growth in the first quarter of 2022 reached 5.03%, healthy by global standards and industrial production in May was up by 10.4% compared to the same month last year.<sup>1</sup> Across the country, factories are resuming normal operations and the international tourist industry is starting to recover.

Yet there are also signs of trouble ahead. Some are obvious, such as the global economic effects from the Russian invasion of Ukraine, while others are more hidden. Chief among the latter are the extent of high-level corruption in Vietnam and the political uncertainty surrounding the future leadership of its Communist Party. These two issues are intertwined in the nexus of political, personal and business connections that characterise contemporary politics in Vietnam.

The next few years could bring political turbulence at the highest level as different elements within the party struggle for supremacy. Most of this in-fighting will probably take place behind closed doors, and it is too early to predict the outcome. However, it seems that the current party leader's attempt to 'correct' the party through anti-corruption campaigns and Leninist discipline will come to an end. The Communist Party of Vietnam (CPV) will return to its previous path of caring more about making money and less about party discipline. Economic growth will accelerate, along with the risks of boom and bust.

### Recovering from COVID

Vietnam's initial response to the COVID pandemic was strong and successful. An early decision to close its international borders drastically reduced the number of infected people entering the country. The Vietnamese authorities were able to make use of their long-established systems of neighbourhood surveillance and an effective grassroots health system to trace, identify and isolate carriers of the virus. This combination of measures saved thousands of lives in the first year of the pandemic.

Things went wrong in 2021, however. An outbreak of the faster-spreading *delta* variant of COVID in Ho Chi Minh City coincided with an anti-corruption campaign that removed the city's political leadership at a crucial moment. The disease began to spread faster than it could be controlled, and the authorities were obliged to impose a severe lockdown. For the first time in peacetime, armed soldiers were deployed at roadblocks in order to restrict people's movements. Millions of quarantined people had difficulty obtaining food and the army was unable to cope with the task of supplying them. For the first time in memory, the armed forces became the object of popular criticism. The pandemic was finally brought under control in late 2021 with a combination of vaccination and movement restrictions.

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<sup>1</sup> Government of Vietnam General Statistics Office, Press Release Socio-Economic Situation In The First Quarter Of 2022, 29 March 2022

<https://www.gso.gov.vn/en/data-and-statistics/2022/05/press-release-socio-economic-situation-in-the-first-quarter-of-2022/>

<https://www.gso.gov.vn/en/data-and-statistics/2022/05/index-of-industrial-production-in-may-of-2022/>

The economy, which had done comparatively well in 2020 with economic growth remaining positive at 2.9%<sup>2</sup>, failed to bounce back in 2021. The growth rate actually fell slightly – to 2.58% – under the impact of the new restrictions.<sup>3</sup> This year, Vietnam has experienced a ‘K-shaped’ recovery, with some sectors doing well and others not. Oil and gas production, which comprises around 10% of Vietnam’s GDP, is enjoying the rise in global energy prices but the other 90% of the economy is not. Agriculture employs more than a third of the population with services a little less than a third. While some parts of the manufacturing sector are managing to maintain exports, others are still suffering from ‘long COVID’: the lingering impact of disruptions to the labour market and supply chains that continue to cause problems for large employers and exporters.

This is having knock-on effects in the wider population. COVID has also caused falls in income and widened inequalities. In late 2021, the International Labour Organisation (ILO) noted a growing gap between a highly skilled minority of the labour force and the remaining population.

The other impact of the pandemic is on public views of the leadership. Restrictions on public expression mean that such views are not aired in national media, but the gossip is on everyone’s lips. Jaw-dropping levels of corruption have been exposed to public scrutiny. Officials in the foreign ministry are believed to have made tens of millions of dollars by overcharging Vietnamese attempting to return home on chartered flights. Another growing scandal concerns vastly overpriced COVID-test kits supplied to public hospitals. Again, officials appeared to have earned tens of millions of dollars. For a population that stoically endured the pandemic-control measures, these abuses by the political elite are hard to stomach.

### The impact of Russia’s invasion of Ukraine

Vietnam’s economy is dominated by international trade: it is one of a small number of countries where trade is vastly greater than its GDP. (Total trade in 2020 was 208% of Vietnam’s GDP.<sup>4</sup>) It is, therefore, highly exposed to swings in the global economy. With the World Bank forecasting a slump in global growth – its June expectation was just 2.9 percent, compared to the January forecast of 4.1 percent, with similarly low numbers expected next year and in 2024 – the outlook for an export-oriented economy like Vietnam is unpromising.<sup>5</sup> Higher prices for oil and gas, rising food price inflation and the lingering effects of COVID-related lockdowns in China will all hit the Vietnamese economy over the next year or two. In May, Deputy Prime Minister Le Van Thanh told the National Assembly, “it’s a huge challenge to realise 2022 targets” for economic growth. The current level of just over five per cent is well below the 6-6.5% necessary to meet the government’s ambitions to become an upper middle-income country by 2045.<sup>6</sup>

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<sup>2</sup> Government of Vietnam General Statistics Office, Viet Nam Economy In 2020 The Growth Of A Year With Full Of Bravery, 14 January 2021 <https://www.gso.gov.vn/en/data-and-statistics/2021/01/viet-nam-economy-in-2020-the-growth-of-a-year-with-full-of-bravery/>

<sup>3</sup> Government of Vietnam General Statistics Office, Press Conference to Announce Socio-Economic Statistics In The Fourth Quarter And 2021, 29 December 2021 <https://www.gso.gov.vn/en/data-and-statistics/2022/01/press-conference-to-announce-socio-economic-statistics-in-the-fourth-quarter-and-2021/>

<sup>4</sup> World Bank, <https://data.worldbank.org/indicator/NE.TRD.GNFS.ZS?locations=VN>

<sup>5</sup> World Bank, Press Release: Stagflation Risk Rises Amid Sharp Slowdown in Growth, 7 June 2022 <https://www.worldbank.org/en/news/press-release/2022/06/07/stagflation-risk-rises-amid-sharp-slowdown-in-growth-energy-markets>

<sup>6</sup> Reuters, Vietnam facing 'huge challenge' to meet 2022 growth target, deputy PM says, 23 May 2022 <https://www.reuters.com/world/asia-pacific/vietnam-deputy-pm-says-realising-2022-growth-target-huge-challenge-2022-05-23/>

On the other hand, Vietnam is expected to benefit from shifts in global supply chains away from China. Stung by their experiences during the COVID crisis, many manufacturers are speeding up plans to diversify production to other countries. The relocation of even a relatively small proportion of the total investment in China would have a significant impact in Vietnam. Some companies have had great success, such as the Korean electronics manufacturer, Samsung. In 2021, Samsung's exports alone comprised one fifth of Vietnam's total exports (\$65.5 billion out of \$336.3 billion).<sup>7</sup> The question facing other investors in Vietnam is whether this success can be repeated by other companies. Can Vietnam's infrastructure, labour market and governance cope?

### How the Communist Party rules

Vietnam's governance looks stable from the outside. The country's communist leadership has remained in power for the past few decades by maintaining coalitions between different parts of the elite. These coalitions include patronage networks, regional and sectoral interest groups and also rival political viewpoints. The one thing that they all agree upon is the necessity of maintaining Communist Party rule. They often differ on the best way to do this. Some prioritise 'performance legitimacy': doing whatever is necessary to deliver a rising standard of living to as many people as possible. Others prioritise 'system loyalty': maintaining the authority of the Communist Party, even if this means constraining economic growth.

The situation in Vietnam's politics today bears strong similarities with the situation at the end of the 1990s. Back then, the security establishment's fears that economic reforms might fatally weaken the Communist Party's grip on power led the party to appoint a hard-line 'system loyalist', Le Kha Phieu as its General-Secretary. Phieu had been a political commissar in the military and knew little about economics. He was only appointed because his comrades in the 'red' position could not agree on anyone else. Phieu oversaw a turn towards China as a means of shoring up the CPV's political position and blocked the approval of a Bilateral Trade Agreement with the United States.

Phieu knew little about economics and he floundered in response to the Asian Financial Crisis. Foreign investment fell by over 60% in 1998 and again in 1999. Unemployment hit double digits and the banking sector fell into crisis.<sup>8</sup> The reds had run out of road. Matters came to a head at a momentous meeting of the CPV's Central Committee in 2000. Phieu's approach was overturned, the BTA was agreed and the CPV agreed the opening of the Ho Chi Minh City Stock Market. In April 2001, Phieu lost his job, and the party leadership was taken over by its 'performance legitimacy' wing.

### Continuity or change?

We appear to be at a similar moment now. The current General-Secretary of the CPV is a system loyalist, Nguyen Phu Trong, who knows little about economics. He is a fierce fighter for the supremacy of the party but is willing to outsource economic policy to a group of 'cronies' who dominate the commanding heights of business and finance. They genuflect to CPV power but carve up the economy into fiefs like mafia families in old New York. You want to invest in a

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<sup>7</sup> <https://vietnamnews.vn/economy/1118144/samsung-viet-nams-2021-revenue-exceeds-us742-billion.html>; <https://www.reuters.com/markets/asia/vietnams-2021-exports-climb-19-record-trade-surplus-with-us-2022-01-13/>

<sup>8</sup> Zachary Abuza, The Lessons of Le Kha Phieu: Changing Rules in Vietnamese Politics, *Contemporary Southeast Asia*, Vol. 24, No. 1 (April 2002), p. 128

particular sector? You had better do a deal with someone in the politburo, or their wife or their cousin.

Trong himself is generally regarded as clean: an orthodox Marxist-Leninist who seems to abhor pleasure. The same cannot be said for those around him. Even those who might be expected to keep the system honest keep questionable company. In late 2021, the Minister of Public Security To Lam was filmed eating a goldleaf-covered steak during a visit to London. The steak cost \$2000, many times more than his official monthly salary. No Vietnamese observer is surprised by the unexplained wealth of the top leadership; bribery and payoffs are seen as normal political behaviour for members of the CPV Politburo, their family, friends and allies.

Trong attempted to rein in some of the worst excesses of the political class. He fought a discreet but brutal battle against his main rival, the former prime minister Nguyen Tan Dung in the years leading up to the CPV party congress in 2016. Having despatched Mr Dung to the political wilderness he continued to pursue an 'anti-corruption' campaign to weed out Dung's main supporters and those who most endangered the reputation of the communist party. It was very successful. It was not successful enough, however, for Trong to feel he could retire and leave the country in safe hands. Unable to persuade the rest of the CPV to support his favoured successor at the following CPV congress, in 2021, he caused the party to bend its rules and allow him to stand for a third term in office.

Trong still can't get his way. He does not seem to have an heir apparent and appears not to trust any of his fellow Politburo members. Using his position as head of the CPV, he has placed allies in government departments to monitor ministers and thwart developments he dislikes. Reports from Hanoi describe a government that is almost dysfunctional. Everyone is watching their back and trying to avoid getting caught up the anti-corruption campaign while simultaneously attempting to milk the system for as much as they can get. Many ministers, bankers and officials have been prosecuted over the past five years, sometimes for actions taken long before. As a result, officials are reluctant to take any decision at all if they fear they might fall foul of a change in the political atmosphere in the future.

The next three years are likely to see more of this. The next party congress will probably take place in January 2026 but the struggles over the leadership and the direction of the communist party are already underway. There is no obvious successor to Mr Trong from either the 'system loyalist' side of the party or the 'performance legitimacy' gang. It is likely that the two sides will slug it out until they can agree on a compromise candidate. Outsiders are kept away from this bare-knuckle fight but from time to time the outside world gets to see clues. A leading figure is disciplined or expelled from the party, a court case is brought against someone rumoured to be connected to someone important, and so on. In June, the country's health minister and the mayor of Hanoi were stripped of their Communist Party membership, allowing them to be prosecuted for the COVID test kit corruption scandal. We are likely to see more such developments.

Predicting the outcome at this stage is a fool's game but predicting a period of poor government in Vietnam over the next three years is a cinch. At the moment it appears that the 'reds' have run out of road. Mr Trong appears to be in a similar position to Mr Phieu 21 years ago. Vietnam's economy is slowing down, the system he controls appears unlikely to meet popular expectations of a rising standard of living and cynicism about the motivations of the top leadership is widespread. But there is no 'clean up' candidate waiting in the wings, ready to give Vietnam a fresh start. Everyone at the top is assumed to be corrupt, the only difference with the current group is the relative priority they place on economic growth.

This 'performance legitimacy' group will pay less attention to party discipline, or rules and laws generally. Vietnam is likely to return to the boom times of the 2010s when politically-linked private enterprises were left alone to make money whichever way they could. The result then was a series of scandals, which eventually caused a backlash and the imposition of the anti-corruption campaign. Some of the victims of that campaign have been waiting for a chance to return. It looks like their moment of opportunity is approaching.