

Vietnam's Port Potential

The Economic and Political Implications of Vietnam's Port Renovation

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Vietnam's Real Problem: Ports

Almost every analysis of Vietnam today includes at least a paragraph or two focused on Vietnam's relationship with China, especially their economic and trade relationship. How is Vietnam handling their giant neighbor to the North? How *should* Vietnam be handling them? Should Vietnam try to become a *de facto* Chinese province, positioning themselves for all the downstream economic and security benefits they can capture? Or should they quietly tout their comparative advantage – a cheap labor force, specialized commodities, less risk than investing in China – to other countries and international investors? Can they do both?

The Vietnam-China dynamic provides ample material for discussion, but when it comes to their economic relationship, all the academic theories, marketing strategies, and corporate tactics in the playbook cannot overcome one basic fact about Vietnam and China. The two countries may share a 1,350 km border on paper, but in practice, to borrow from the old adage, you can't get there from here.

Vietnam has an infrastructure problem in almost all sectors. It has an airport problem. It has a road problem. And Vietnam has a port problem. While there is some trucking activity between the two countries on the one small highway that connects them, the real potential for Vietnam to benefit from China's massive economy - or to benefit from any regional economic activity - lies on the water, and in the ports, which are currently too small and too shallow to effectively realize their economic potential.

Expanding those ports will allow Vietnam to make the economic and developmental leaps it wants to take to be a stronger and more competitive player in the Asia Pacific region. Domestically, port improvement will also change the tenuous political dynamics in Vietnam, creating not just economic opportunities, but an evolution in relations between Vietnam's central government and its provincial leaders. In effect, Vietnam's port renovations will potentially alter not just the physical infrastructure of the country, but its social, regional, and political infrastructure as well.

Geographic Reality Check: Vietnam's Limitations and Opportunities

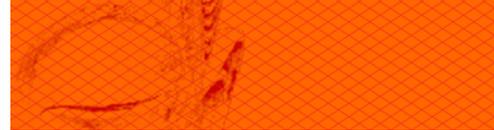
Ports. In an age where the most powerful tools behind growth and innovation are silicon chips weighing .18 microns or less, it seems counterintuitive that access to a 300 meter ship is a major economic obstacle for a country of 85 million motivated people, a third of which are in their young working prime.



Image 1. Map courtesy of <http://www.worldatlas.com/webimage/countrys/asia/lcolor/vncolor.htm>

But if geography is a form of destiny, then Vietnam's fate is tied to its ports. While technically one country, Vietnam is sharply divided by historical, linguistic and cultural differences into three regions – the North, the Center, and the South – that do not cooperate well with each other, if at all. A long mountain chain forms a prickly spine down the country's back, hampering East-West transit and trade. Even taller mountains cluster in the North at the Chinese border. This geographic reality means that with over 3200 km of coastline, Vietnam's future is still where it has always been – on the water.

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While ambitions to make Vietnam another version of Singapore - a technological and financial hub - are possible in the distant future, the leap from where they are now to a high-rise economy dealing in virtual worlds and industries has to launch with the ships coming in and out of Vietnamese waters.

Vietnam does have ports. Ships can arrive, load, and unload goods. In fact, 90 percent of all of Vietnam's goods are transported by sea. However, Vietnam does not have the size and depth of ports that it needs to effectively maximize the economic opportunities presented by its geopolitical location. A quarter of the world's sea-based trade passes through the Straits of Malacca each year.ⁱ Seven of the world's ten busiest ports are located in East Asia. Yet Vietnam has only the smallest share of this enormous pie.

The Role Envisioned – What Difference Would Better Ports Make?

The Vietnamese government has started to do something about its port problem. In the past five years, both government and private industry have focused heavily on renovating Vietnam's major ports. Vietnamese officials estimate that it will take more than 60 billion dollars to bring Vietnam's infrastructure up to an international operating standard, most of which will be spent on port renovation, access to ports, and port storage and handling facilities.

Vietnam's GDP in 2008 was 85 billion USD, and many people there still live on less than one dollar a day. Infrastructure projects worth 60 billion USD are a politically charged undertaking in any country, but especially in developing ones, where checks on graft and corruption are few and limited in scope. With such a large amount of money involved, it is worth verifying demand for improved Vietnamese ports. What, specifically, would larger ports in Vietnam do?

1) *Larger ports would reduce or eliminate the need for transshipment of Vietnamese exports, restoring the comparative advantage of Vietnam's cheap and relatively educated labor force.* Right now, most goods exported from Vietnam to major markets are transshipped elsewhere in Southeast Asia onto larger vessels, adding costs to goods that Vietnam is able to produce more cheaply than China, Thailand, and other regional manufacturers. Depending on fuel prices, these additional shipping and handling costs eliminate some of the comparative advantage Vietnam offers investors and manufacturers, increasing shipping costs by as much as 28 percent.ⁱⁱ



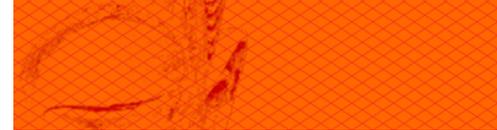
Image 2: The blue and red dots show Vietnam's major ports. Notice the clusters in the southern region and at the Chinese border in the North.

2) *In northern Vietnam, an improved port would bring Western Chinese exports to market faster and more cheaply.* A deep water port near the northern Vietnamese city of Hai Phong would cut 800 kilometers off the shipping route of goods coming out of Western Chinaⁱⁱⁱ, giving foreign businesses further incentive to use Vietnam as a second regional base to offset the cost and risk of investing in China.^{iv}

3) *Improved ports would allow Vietnam to become a transshipment and consolidation point for goods coming in and out of China.* Bigger ports would allow Vietnam to enter the transshipment market with competitive prices that could entice shippers away from more expensive transshipment points such as those in Singapore and Hong Kong.

4) *A deep-water port in Central Vietnam would eventually allow for goods coming out of northern Thailand, Laos, and Burma to be consolidated with international shipments, as well as easier export of Vietnamese oil.* The Vietnamese Government estimates that a central port would save Vietnam 1.5 billion USD a year in shipping costs for oil exports.^v

5) *Better ports would allow Vietnam to fully realize its domestic manufacturing potential in the South,* home to its large manufacturing base, by eliminating the major export bottlenecks currently experienced by domestic and international producers.



6) *Better ports would allow southern Vietnamese ports to become a major shipping hub for Cambodia, southern Thailand, and the larger Southeast Asia region.* While there is probably not enough demand for a third major hub-like Singapore and Hong Kong^{vi}, Vietnam could offer competitive rates that attract shippers serving specific routes.

This demand for and use of expanded Vietnamese ports does not suggest that Vietnam will ever rival the two major shipping hubs in Hong Kong and Singapore, or that it should. Hong Kong and Singapore are so far advanced in capacity and technology that there is no point in trying to match them.^{vii} However, Vietnam can integrate itself into regional shipping routes, shortening those routes where possible, eliminate its own transshipment costs, and make the export of goods out of the Southeast Asia landmass more economical and feasible.

Beyond Vietnam’s own domestic situation, several global trends in shipping support the argument for bigger and better ports in Vietnam. First, ships are becoming enormous, since larger ships can save an exporter millions in fuel costs.^{viii} Second, the global economic recession has driven the price of shipping down to record lows, making sea transport extremely attractive to exporters in companies of all sizes.^{ix} In fact, despite the global recession, the number of exported and imported goods coming in and out of Vietnam’s major ports in the South has increased ten percent in the last year.^x Finally, as we are seeing now, Asia is the preferred place to park idle ships and warehouse idle goods waiting for shipment.^{xi} In good times and in bad, having large, deep ports with plenty of berthing and storage space is a huge economic opportunity for an economy structured as Vietnam’s is.

The Vietnamese Economy

Despite the global recession, Vietnam’s economy is doing relatively well. Over the past decade, it has expanded an average of seven percent each year, and a recent rebound in the first half of this year suggests it may reach a growth rate of about three to five percent for 2009.

Vietnam still struggles with two looming financial problems: a slew of bad loans to state-owned and quasi state-owned enterprises, and an ongoing battle with inflation. Vietnamese leadership has relied heavily on high levels of domestic consumption, exports, and foreign investment to keep these two problems under control, or at least out of the public spotlight.

However, compared to other economies in the region, many of which have shrunk in the past two years, Vietnam’s modest growth rates and relatively stable economy are attractive to investors, especially in southern Vietnam, where special economic zones that offer low taxes and little bureaucracy can be a real bargain for manufacturers. Expatriate Vietnamese, in particular, are investing in Vietnam in large numbers.

In this economic climate, Vietnam’s port development is ultimately a gamble on a near-term global recovery that will see export rates return to the double digits Vietnam had in the earlier part of this decade. With high levels of public confidence in the Vietnamese economy, domestic consumption – along with significant government spending – is sustaining growth and stability until that recovery happens.

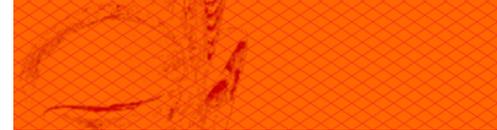
Ultimately, even with a return to higher export levels, Vietnam still desperately needs a major infrastructure



Image 3. Container terminal in Hong Kong, courtesy of Wikipedia.



Image 4: Plans for expansion of the Saigon Port, courtesy of the Vietnamese Consulate in the Netherlands.



upgrade in and around its ports to succeed in the long term. If infrastructure improvements are in place in time to capitalize on an improved global economy, the payoff for the Vietnamese and for international investors in Vietnam will be significant.

How Big Is the Port Problem?

An accurate assessment of Vietnam's current and future port capacity is complicated by the fact that almost all of the major ports are in some phase of improvement. Separating the ambitions and projections of the Vietnamese Government from the reality of how those improvements are progressing is a difficult task as well. Government documents explaining how government and investor money will be used to upgrade existing facilities primarily include only targets for improvements, not the starting point or baseline. As a final complication, upgrades to Vietnam's ports are conducted by a wide variety of agents. In the South, where the most progress to date has occurred, a joint venture of Asian investors is leading the way in port expansion.^{xii} In the northern and central regions, where state-owned enterprises (SOE) or Vietnamese government ministries are conducting the upgrades, progress is considerably slower, since it is hampered by the poor administration, corruption, and bureaucracy that is typical of projects conducted by the Vietnamese government and Vietnamese SOEs.

The Vietnamese government is also trying to formalize its authority over all of the ports, both publicly and privately funded. The Vietnamese Ministry of Transportation recently drafted the "Vietnam Seaport System Master Plan Outlook to 2030" for the Prime Minister. Submitted in June 2009, the report, which has not been made public, attempts to coordinate the construction and renovations at Vietnam's 33 major ports by bringing them all under a central port authority.^{xiii} Government oversight of major infrastructure projects does not have a great track record. In 2006, senior Ministry of Transportation officials were caught using 50 million USD in state and donor funds for a major construction project to bet on British soccer matches.^{xiv}

Such scandals notwithstanding, coordination will likely help Vietnam's ports in the long term. However, what those ports need now is depth. The following chart depicts both the current and projected sizes for Vietnam's major ports. Ports

can be measured in a variety of ways: berthing space, cargo handling capacity, cargo handled, maximum size of receivable vessels and number of ships received. Because Vietnam's primary port problem is an inability to host larger vessels in a market where vessels are rapidly expanding in size to cut cost, this chart measures and compares only the maximum receivable vessel size, or dead weight tonnage (DWT), which is the cargo carrying capacity of the ship. Handling capacity, berthing space, and storage capacity are also important metrics for shippers. Vietnam lags far behind in these areas as well.

The numbers used to create this chart were drawn from individual port profiles at the Vietnamese Seaport Association and compiled by region. Data from Thailand, Hong Kong, and Singapore's largest ports is included here for a regional perspective.

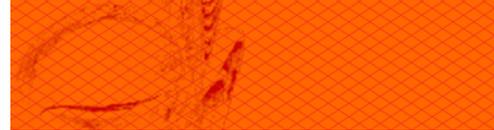
The good news for Vietnam is despite their current predicament, things are improving. The Vietnamese government and foreign investors are spending 4.5 billion dollars over the next five years to improve the seaport infrastructure. In the South, the planned expansions are expected to increase average container import-export growth by 20 percent annually over those same five years. Between that level of spending and of growth, Vietnam is poised to finally reach the economic maturity it has been striving for over the past two decades.



Image 6. Manufacturing and construction project in Yen Phong Industrial Park. Image courtesy of the NYT.^{xv}

The Politics of Ports

Unfortunately, it is in the uneasy relationship between government expenditures and proof of performance that Vietnam's port problem becomes political. For instance, plans to turn Hai Phong port – one of the largest renovation projects and most expensive at 1.6 billion USD^{xvi} – into "Vietnam's international gateway" do not track with demand so much as politics. In 2008, Hai Phong handled only 14 million metric tons of cargo throughput. In contrast, Saigon Newport handled more than 25 million metric tons of cargo throughput in 2008. Regionally, the proportions are similar. The 23 tightly clustered major southern ports handled more than 78 million metric tons of cargo. The nine main ports in



the North had close to 59 million metric tons of cargo throughput, almost half of which was coal, not in actual goods.^{xvii} This data is not a secret or a surprise to anyone in the Vietnamese government: all of these numbers are drawn from the Vietnamese Seaports Association 2005-2008 throughput reports for the 32 main ports in the North and the South. While the Vietnamese Government wants the Hai Phong-Lach Huyen port to be the gateway; the Saigon area ports already *are* the gateway. Rapid progress on the southern port renovations, conducted as they are by international investors and private companies, is only going to further reinforce that sharp distinction.

Regional economic disparity is nothing new in Vietnam. The Vietnamese leadership in Hanoi has already made large concessions to provincial autonomy, which amounts to a muted form of regional autonomy – both political and economic – in the South. However, Vietnam has never faced the kind of economic disparity that this level of port expansion could bring, and the political fallout from that degree of economic empowerment will be significant.

What It Means for Us

Vietnam’s port development is a relatively good thing for U.S. investors, and it tracks with U.S. policy in Vietnam, which seeks to encourage Vietnam’s economic development in a way that supports free and fair markets. There is not much that the United States Government can specifically do to encourage port development, especially since involvement in infrastructure projects is something the U.S. government wisely avoids. However, U.S. investors and U.S. exporters, both of whom are poised to benefit from the expansion, can certainly have an impact regionally and locally on the quality and direction of individual port upgrade projects, since U.S. investors are often extremely influential at the local level.

More importantly, both U.S. officials and businesses can and should emphasize the importance of making these changes in a way that makes smart economic sense for Vietnam, both in terms of making the right choices for large expenditures and ensuring that port upgrades are done to international standards. The United States and Vietnam will both realize the greatest benefit from these massive upgrades if are done well and done wisely.

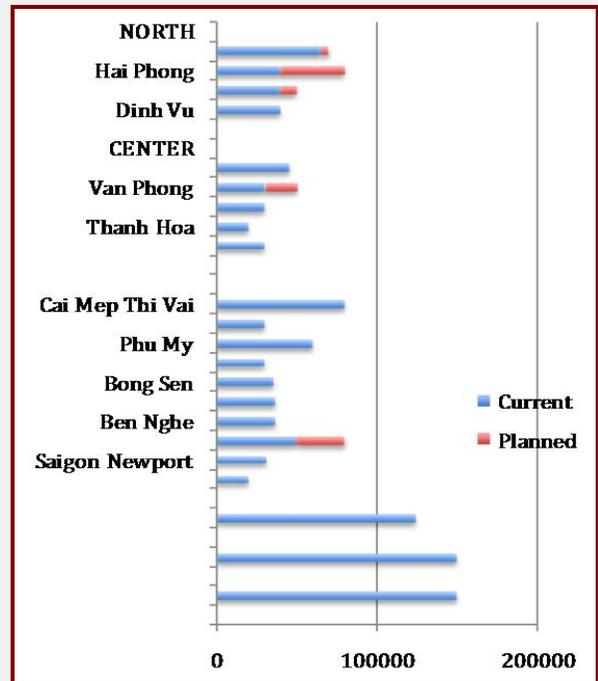


Image 5. Vietnamese and regional ports measured by DWT. The numbers used in this chart were derived from Vietnamese and English language primary sources^{xviii}, government reports, news reports, and investor reports.^{xix}

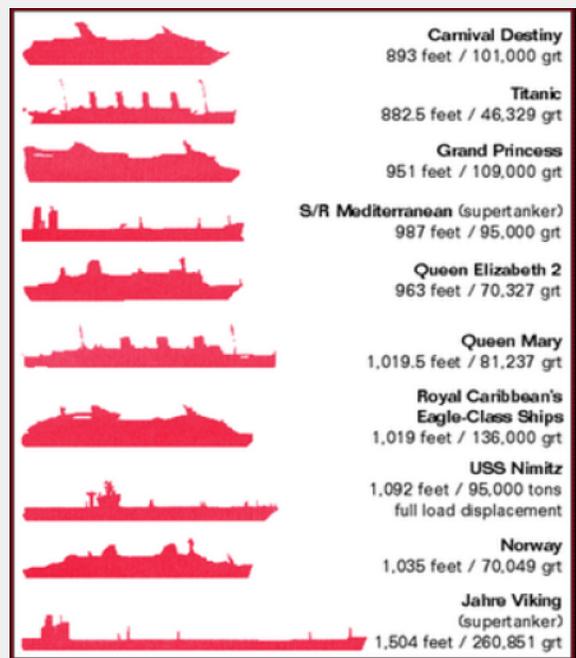
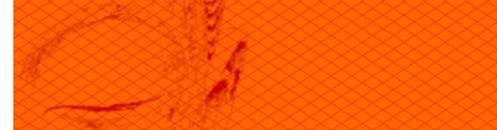


Image 6. A comparison of ships by gross registered tonnage. Gross registered tonnage is the total internal volume of the vessel, while dead weight tonnage measures carrying capacity. Nevertheless, this image does give a useful visualization of size comparison.



Looking Ahead

Port development is at the heart of the political, economic, and security problem facing Vietnam: how to integrate, how to grow, how to change. Vietnam's real challenge is managing The Vietnam That Was and Is vs. The Vietnam to Be. Rapid development of ports in southern Vietnam will be a major strain upon preexisting regional tensions and disparities. At the same time, that development will be Vietnam's entrée into an industry dramatically affected by the global recession and other security issues. Vietnam will enter that competition with its standard comparative advantages – cheap and educated labor, niche exports, and prime location – at a time when its economy is doing relatively well and investors are looking for opportunities to offset more precarious risks in the region. Should the Vietnamese Government overcome its habit of putting political preference above economic reality, Vietnam's ports could potentially be the stepping-stones to development that they are hoped to be.

ⁱ *The Economist Print Edition* (June 10, 2004). Shipping in South-East Asia. Retrieved July 4, 2009, from http://www.economist.com/displayStory.cfm?Story_ID=E1_NSVNRDN

ⁱⁱ Ruckel, Christopher. Ports in Vietnam Stunting amid Economic Development. *Business in Asia* (2006). Retrieved June 28, 2009 from http://www.business-in-asia.com/ports_in_vietnam.html

ⁱⁱⁱ *Portworld* (April 20, 2007). Feasibility study for Vietnam deep water port completed. Retrieved June 28, 2009 from http://portworld.com/news/i67577/Feasibility_study_for_Vietnam_deep_water_port_completed

^{iv} Investment and Trade Promotion Center, (January 20, 2009). Vietnam offers grand opportunities, but big challenges as well. Retrieved on June 28, 2009 from http://www.itpc.gov.vn/investors/news/2009/2009-01-02.745892/2009-01-20.025680/MISNews_view/?set_language=en

^v Vietnam Seaports Association (May 7, 2009). Deep water port promises premium profits. Retrieved on July 1, 2009 from http://www.vpa.org.vn/detail_temp.jsp?page=1&id=1167&cate_id=22

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^{viii} *Shipping and Shipbuilding News* (May 28, 2008). New designs on the world's biggest container ships. Retrieved on June 28, 2009 from http://www.shippingtimes.co.uk/item_10082.html

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^{xiv} *BBC News*, (April 4m 2006). Vietnam ministry hit by scandal. Retrieved on July 7, 2009 at <http://news.bbc.co.uk/2/hi/asia-pacific/4874600.stm>

^{xv} Photo retrieved on July 7, 2009 from <http://www.nytimes.com/2008/06/18/business/worldbusiness/18invest.html?pagewanted=all>

^{xvi} Investment and Trade Promotion Center, (January 20, 2009). Vietnam offers grand opportunities, but big challenges as well. Retrieved on June 28, 2009 from http://www.itpc.gov.vn/investors/news/2009/2009-01-02.745892/2009-01-20.025680/MISNews_view/?set_language=en

^{xvii} Vietnam Seaports Association, multiple pages. All statistics were compiled using the port profiles available, beginning with <http://www.vpa.org.vn/english/members/north/B12OIL.htm>

^{xviii} Vietnam Seaports Association, main page. Retrieved on July 1, 2009 from <http://www.vpa.org.vn/english>

^{xix} *World Port Source*. Ports of Call. Retrieved on June 28, 2009 from <http://www.worldportsource.com/ports/VN.php>