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Trade Openness and Economics Growth in Vietnam

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ABSTRACT

The advent of technology and rapid globalisation, trade policies are observed time to time due to the continuous uncertainty in world economy. In this manner, this study has focused on the trade openness and economic growth in Vietnam. The aim of this study was to examine how trade openness can impact economic growth in case of Vietnam. Therefore, quantitative analysis is carried out and secondary data was collected for the purpose of investigating the impact of trade openness on the economic growth in Vietnam. The researcher applied the autoregressive distributed lag (ARDL) bound testing model with the help of E-views to determine the impact of trade openness on the economic growth of Vietnam. From the analysis, it can be identified that there is no long term impact of the trade openness on the economic growth of Vietnam. However, the short term impact of the trade openness on the economic growth of Vietnam has been found in this study. The model will be reestimated by changing the data series.

INTRODUCTION

With the advancement of technology and rapid globalisation, trade policies are examined time to time due to the continuous uncertainty in world economy. Developing countries used to follow import substitution policy but later, may countries have shifted to export led growth policies. There have been significant changes in the trade policy that involves export-based promotion strategies. According to the study conducted by Jawaid (2014) export-based promotion strategies help to allocate resources more efficiently which results in overall economic growth. However, it was argued further that trade policies are also the result of change in exchange rates, taxes and export schemes. The following study focuses on examining the relationship between trade openness and economic growth particularly in case of Vietnam.

Trade openness also shifts the movement of foreign direct investment inflow because increase in foreign investments significantly influences the overall exports. Nguyen (2018) highlighted in his study that after 1986's reforms, Vietnam has worked tirelessly to lift trade and liberalization policies. It shifted from a typical agriculture-based economy to an industrial economy. The country encouraged foreign investors to make invests in different sectors such as health and education (Zhang, 2017). Since then, Vietnam has constantly focused on improving their economic position through foreign investments and trade activities.

The aim of the following study is to examine how trade openness can impact economic growth in case of Vietnam therefore, quantitative analysis is carried out and secondary data was collected. The researcher has used the following study to portray the current economic conditions of Vietnam in the light of trade policies, reforms and the strategies used to boost export activities. From the empirical point of view, trade openness and economic growth are both considered as important determinants for the overall prosperity of developing nations (Keho, 2017). The independent variables selected for this study are inflation, trade openness, money supply and GDP per capita whereas, the dependent variable was economic growth measured through GDP.

LITERATURE REVIEW

Trade openness

There has been significant debate and discussion over trade openness and economic growth. Most of the studies that are conducted in similar domain shed light on the concept of trade openness and its significance for the growth of economy. However, many arguments are also presented because policies and economic goals differ from developed to developing nations due to which it is not possible for the researchers to generalize the findings (Pal, Chakraborty, & Ghose, 2019; Tanaka, 2018; Zhang, 2017) . The studies that are conducted in this subject area are divided into three groups mainly aggregate country data, panel analysis and industry level effect. Each subject identifies the impact on economic growth and limitations of its implementation. The studies that were mainly conducted through panel data analysis highlighted that imports and exports both need to be taken into consideration in order to assess the impact of trade openness on economic growth.

In the light of the study conducted by Jawaid (2014) it was found that export-based plans are developed that leads towards economic growth. However, there are some economic factors that have a significant influence on the economic growth such as return to scale or competition. Furthermore, trade openness has played a significant part in economic growth. In light of the theories of Ricardo and Adam Smith, trade openness not only helps in term of improving the overall GDP rate of country but it also promotes specialization (Khobai, Kolisi, & Moyo, 2018). Countries work in accordance with their specialization which refers to the production of those products and services which can be

exported. On the other hand, those countries which do not have advantage over these products and services will import from other countries.

Also, some of the studies have indicated that trade openness helps to increase technological advancement and production rate. In this case, the developing countries also play a vital role in the development and they also absorb knowledge and expertise from rich countries (Obeid & Awad, 2018). Most of the studies that are conducted in similar domain have shed light on the fact that economic expansion can be achieved through trade activities because the openness of trade is dependent on investments therefore, comparative advantage is achieved by these countries through increased exports to countries.

Trade openness and economic growth in vietnam

After the reform of Doi Moi in 1986, Vietnam has constantly been making efforts to revive the policies and strategies in order to stabilise their economic activities and growth. The economy shifted from agriculture based to industry-based economy though there were certain discrepancies. Moving further, foreign investment law was established in 1987 after which FDI inflow increased. However, the laws were changed during the Asian financial crisis after which the foreigners were allowed to make investments in different sectors of Vietnam (Nguyen, 2018; Nguyen, 2017). On the basis of the studies, it was found that most of the foreign based enterprises were permitted to make investments either through mergers or acquisitions. This became the turning point for Vietnam because after this, the country experienced FDI inflow (Nguyen, 2018). After this, Vietnam became a member of World trade organization in 2007 which further gave boosts to trade and FDI inflow. Vietnam had designed their complete FDI growth plan in order to attract the investors and encourage foreign investments for the purpose of local development and growth (Adegbite, 2017).

THEORETICAL FRAMEWORK

Theory of comparative advantage

In the light of the theory of comparative advantage, it was found that trade helps in use of available and local resources by importing the capital-intensive goods that have high manufacturing costs if they are produced locally. However, countries cannot forego these products from importing because these products help to gain advantage over manufacturing export quality products. According to the study conducted by Keho (2017) it was determined that comparative advantage theory is part of the neo-classical view which is driven through technology or through other external factors.

Costinot (2009) highlighted in his study that comparative advantage theory is important to understand the use of useful resources and exchange of goods and service between two countries. This theory is highly essential for understanding why the costs of production is different among all countries. Despite of the fact that similar products are being produced, the difference is observed. This is mainly due to the inflation, cost of raw materials and other manufacturing costs. However, the economic conditions of a country cannot be ignored in this regard. Also, comparative advantage theory is also dependent on many factors out of which, there are three most important elements such as labour, capital and land. This theory is also interlinked with the fact that comparative advantage needs to undertake the factor of production.

In addition to this, the existing studies have further explained this theory in the light of the economic conditions and the demand of specific sectors. The comparative advantage theory is also based on frameworks and policies that are designed by the economic policymakers along with the needs of every sector (Tabuchi, 2017). Furthermore, this

theory has also shed light on the fact that sources of comparative advantage include those products and services which can be exported at lesser price as compared to its own manufacturing costs in local market.

In light of the concept proposed by Adam Smith, it was found that international trade is important for the nation's development as well as economic welfare. Adam Smith discussed the causes and characteristics of wealth of nations and highlighted in his study that the purpose of an economy is to export goods and services in order to generate revenue. Specialization is one of the key element in this theory because it is associated with the theory of absolute advantage and comparative advantage (Davis & Dingel, 2020). The ability of a country to produce products at a cheaper rate as compared to other countries can be beneficial for carrying out trade activities. This theory was further supported by David Ricardo where he highlighted that even if a country does not have specialization of producing any product still, it will be able to achieve desired economic objectives.

Resource allocation is highly important and needs to be taken into consideration by the nations so that they are able to utilize their existing resources more efficiently and gain competitive advantage. Also, it was found from the existing studies that trade activities that are performed by countries are on the basis of the comparative advantage theory (Ren & Ma, 2018). Import and export activities are conducted so that countries that can produce products at cheaper rates can manufacture them and use them for local use whereas, heavy machinery can be imported by saving costs of ordinary products.

Endogenous growth theory

Based on the existing studies regarding trade openness and economic growth, endogenous growth theory was found to be highly relevant. The theory states that constant growth within a country will help the entrepreneurs to grow and make more investments which will ultimately lead towards economic growth and sustainability. The basic idea behind this theory is to improve the economic condition of the country through increased technological advancement and investments (Akcigit & Ates, 2019). Despite of the fact that the existing corporations are involved in making investments and move towards bringing innovation but at the same time, it cannot be ignored that the entrepreneurs are well aware of the market dynamics and they are ready to take any sort of risks. This has also been found from the past studies that international trade activities help to increase the competition so, it directs towards the trade activities that will help in long term sustainability and growth of economy. In addition to this, trade not only helps to expand the locally developed markets but it also encourages the use of technology and brings innovation in products or services.

Moreover, researchers have laid great emphasis on this theory and found it to be relevant for studying the dynamics of trade openness and economic growth. The basic assumption behind endogenous growth theory is that those countries which have bilateral trade relationships with one another will be able to share technological resources and equipment (Pan and Ngo, 2016). However, it has been argued that nations that are not equal to each other in terms of the size of economy can compete at similar level or not. Countries like Vietnam are considered as a developing country which has potential to grow in terms of technology and innovation therefore, such economies will expect as well as pressurise the local small sized enterprises to bring innovative products in market.

Internationalisation theory

The internationalisation theory is a theory related to trade openness of countries and where the product can be produced at the lowest price (Knight & Liesch, 2016). The

cycle emerges at the parent firm where it is possible to produce the goods at lowest price possible. If not, the cycle then moves to its subsidiaries in other countries. However, the very last option is producing anywhere in the world where the company can produce goods at lowest possible cost (Narula, Asmussen, Chi, & Kundu, 2019). This directly links to trade openness since countries having policy of open trade, for example, China having open trade policy has seen exponential growth in its economy due to having trade openness. For this purpose, an example of iPhone can be quoted which is manufactured in America but assembled in China due to low cost of operations in China. The internationalisation theory helps the companies to identify the places where product can be produced at lowest possible cost in order to increase the profit margin (Amorós, Basco, & Romaní, 2016). The internationalisation theory fits the topic of study as this theory is directly related to trade openness which tends to fortify the economic growth as explained above.

Hypothesis

H_1: There is a significant impact of trade openness on the economic growth of Vietnam
H_0: There is no significant impact of trade openness on the economic growth of Vietnam

DATA AND METHOD

Unit root test: augmented dickey fuller (ADF)

The main focus of the study was to measure the influence of trade openness on the economic growth in which the secondary data is collected from the various authentic website which are the country reports and data from the world. The variables identified in the study consist of on trade openness, inflation, money supply and gross domestic product per capita and these variables are gathered from 1985 to 2019. Thus, the researcher has gathered annual time series data where the assumption of classical time series model requires testing whether the series is stationary and the errors have a zero mean and finite variance. Thus, the unit root test is performed for identifying as whether the variables are stationary or non-stationary. Arnold and Hanck (2019); del Barrio Castro, Rodrigues, and Taylor (2018); Antara and Sumarniash (2019) states that the testing of unit root is eminent as the non-stationary regressor can invalidate the standard empirical results. The unit root test that is adopted in the study is the Augmented Dickey Fuller (ADF) in which its model is provided below

$$\Delta g_t = \lambda_0 + \lambda_1 t + \lambda_2 g_{t-1} + \sum_{i=1}^{n} ni\ 1\, \Delta g_{t-1} + \mu_t$$

Where Δ is the difference operator and n represent the lag and μ_t is the random error of stationary which adjusts with the error of autocorrelation. The null hypothesis of the model is that g_t is the non-stationary series.

Autoregressive distributed lag (ARDL)

The standard log-linear function of long-run association between trade openness and economic growth of Vietnam can be expressed as:

$$Y_t = \beta + \vartheta BM_t + \vartheta CPIB_t\, \vartheta GDPU_t + \vartheta TGDP_t + \mu_t$$

In which BM_t is the broad money, $CPIB_t$ reflects on the CPI base, $GPDU_t$ represents the GDP USD and $TGDP_t$ denotes that trade of GDP. On the other hand the component Y_t represents the Log of GDP. Furthermore, μ_t denotes the usual error term and ϑ is the parameter estimate. The existence of the long-run cointegration among the relationship

between variables has been measured through the autoregressive distributed lag (ARDL) approach. There are mainly two reasons for using the ARDL approach in which the first reason is that it is applicable regardless of variables being stationary or non-stationary for avoiding regression problem. Secondly, the use of the ARDL approach avoids a low power in the identification of cointegration relationship. The error correlation model (ECM) of the ARDL model is applied which is expressed as

$$\Delta Y_t = \beta 1 + \sum_{i=1}^{m1} \vartheta_{1i} \Delta Y_{t-i} + \sum_{j=0}^{n1} \vartheta_{1j} \Delta BM_{t-j} + \sum_{j=0}^{n1} \vartheta_{1j} \Delta CPIB_{t-j} + \sum_{j=0}^{n1} \vartheta_{1j} \Delta GDPU_{t-j} + \sum_{j=0}^{n1} \vartheta_{1j} \Delta TDGP_{t-j} + \gamma_1 Y_{t-1} + \gamma_2 BM_{t-1} + \gamma_3 CPIB_{t-1} + \gamma_4 GDPU_{t-1} + \gamma_5 TDGDP_{t-1} + \mu_t$$

In this model, the null hypothesis is that there cointegration association between the Y_t and the independent variable is detected by testing the F-statistic for H_0: $\gamma_1 = \gamma_2 = \gamma_3 = \gamma_4 = \gamma_5 = 0$. If the F-statistics value is below the critical value, then the null hypothesis cannot be rejected. If the cointegration association among the variables is determined than the next step involves in estimating the long-run and short-run dynamics which are provided below in (4) and (5) model.

$$\Delta Y_t = \beta 2 + \sum_{i=1}^{m2} \vartheta_{2i} \Delta Y_{t-i} + \sum_{j=0}^{n2} \vartheta_{2j} \Delta BM_{t-j} + \sum_{j=0}^{n2} \vartheta_{2j} \Delta CPIB_{t-j} + \sum_{j=0}^{n2} \vartheta_{2j} \Delta GDPU_{t-j} + \sum_{j=0}^{n2} \vartheta_{2j} \Delta TDGP_{t-j} + \mu_{2t}$$

$$\Delta Y_t = \beta 3 + \sum_{i=1}^{m3} \vartheta_{3i} \Delta Y_{t-i} + \sum_{j=0}^{n3} \vartheta_{3j} \Delta BM_{t-j} + \sum_{j=0}^{n3} \vartheta_{3j} \Delta CPIB_{t-j} + \sum_{j=0}^{n3} \vartheta_{3j} \Delta GDPU_{t-j} + \sum_{j=0}^{n3} \vartheta_{3j} \Delta TDGP_{t-j} + \phi \varepsilon_{t-1} + \mu_{3t}$$

Where ϕ is indicated as the statistically significant coefficient error and ε is the negative sign which shows as to how fast the variables converge to the equilibrium.

RESULTS AND DISCUSSIONS

Descriptive statistics

The summary of descriptive statistics of the gathered observations can be identified from table 1. In this manner, the mean, maximum, minimum and standard deviation values are necessary to be considered from the table. The mean of Broad Money is computed as 59.194 while the mean for CPI Base 2010 has been observed as 58.170. In addition to this, the mean for GDP per capita was 782.619 and the mean for GDP USD was 68,100,000,000.00. Moreover, the mean for LOG GDP was 10.621 and the mean for Trade of GDP was 95.155. On the other hand, the maximum value for Broad Money was 158.063 while the maximum value for CPI Base 2010 was 161.31. The maximum value for GDP per capita current US$ was 2566.597 along with the maximum value of GDP USD which was 245,000,000,000.00. The maximum value of the Log GDP was 11.389 and the maximum value of the Trade of GDP was 200.384 (Agbonkhese & Oligbi, 2020). Moreover, the minimum value of Broad Money was noted to be 12.507 along with the minimum value of CPI Base which is 0.457. The minimum value of GDP per capita was noted to be 94.564 with the minimum value of the GDP USD 6,290,000,000.00. Lastly, the minimum values of LOG GDP and Trade of GDP were noted to be 9.798 and 0.825 respectively. Pertaining to the standard deviation which has also been identified in the descriptive analysis, it can be identified that the SD of Broad Money was calculated as 47.272. In addition to this, the SD of CPI Base 2010 was identified to be 50.787. On the other hand, the SD of GDP per Capita was calculated at 724.197 which shows that the GDP per capita will deviate from 724.197 and is much higher. With respect to the GDP USD, it can be identified that the SD is 69,100,000,000.00. Moreover, the SD of Log

GDP was calculated to be 0.440 along with the SD of Trade of GDP which was calculated at 59.174.

The Jarque Bera and probability were also considered while predicting the nature of the data and is being considered essential for the purpose of determining the normality of data. The value of Jarque-Bera for Broad Money has been obtained as 4.881 [p=0.087]. In addition to this, the values for CPI Base 2010, GDP per capita and GDP USD were obtained as 4.305 [p=0.116], 8.729 [p=0.012] and 10.111 [p=0.006]. Moreover, the values of Log GDP and Trade GDP were 1.289 [p=0.524] and 2.406 [p=0.3]. This shows that the data is normally distributed.

Table 1: Descriptive Statistics

	Broad Money	CPI Base 2010	Gdp Per Capita Current US$	GDP USD	LOG GDP	Trade of GDP
Mean	59.194	58.170	782.619	68,100,000,000.00	10.621	95.155
Median	36.372	47.919	404.807	31,200,000,000.00	10.493	97.001
Maximum	158.063	161.31	2566.597	245,000,000,000.00	11.389	200.384
Minimum	12.507	0.457	94.564	6,290,000,000.00	9.798	0.825
Std. Dev.	47.272	50.787	724.197	69,100,000,000.00	0.440	59.174
Jarque-Bera	4.881	4.305	8.729	10.111	1.289	2.406
Probability	0.087	0.116	0.012	0.006	0.524	0.300

Unit root testing-ADF

In this section of the study, the unit root testing has been carried out for the purpose of determining that either the data is stationary or non-stationary. The findings of Harvey, Leybourne, and Taylor (2013) suggests that Augmented Dickey-Fuller (ADF) is applied for the purpose of determining the stationarity of data. In this manner, it becomes essential to discuss the supposition that there is a unit in time series in null hypothesis of unit root. With respect to table 2, the t-statistics of Broad money along with CPI, GDP per capita Log GDP and Trade can be identified which shows the value 1.878 [p=0.9997], 1.238038 [p=0.9978], 3.237842 [p=1], -0.014 [p=0.9503] and 0.198 [p=0.969]. This identifies that time series data of all the variables have a unit root as the p=value is greater than the threshold of 0.05.

Table 2: Unit Root Testing

ADF Test	**T-Statistics**	**Prob.**
Broad Money	1.878214	0.9997
CPI	1.238038	0.9978
GDP Per Capita	0.158621	0.9654
Log (GDP)	-0.014978	0.9503
Trade (%)	0.198686	0.969

Autoregressive distributed lag (ARDL)

Pertaining to the existence of unit roots in the time series data, it becomes essential to integrate the concept of auto-correlation for the purpose of estimating or predicting the future values which are based on historical analysis. In this manner, it is necessary to discuss the lag technique which assists in predicting the values. Since the time series data of this study consist the unit root, therefore, the Autoregressive Distributed Lag (ARDL)

is used to determine the causality among the variables. The findings of Tan and Févotte (2012) also suggests that ARDL model is usually used for predicting the future values on the basis of iterative values while maximising the observations of marginal log.

The table below provides the model which has been developed in relation to the Log GDP and other independent variables through the ARDL. From the table, it is evident that the Log GDP is dependent and is considered to be significant at the threshold of 1%. In the case of independent variable, the Broad Money is significant at its level however, infers that there is no relation among the variables in the long run. On the other hand, the Trade of GDP is dependent on its first lag and is significant in the short run while having a positive association with the variable. The CPI Base 2010 has the positive association among the variables in the long run however, is not significant at its level (Akgun & Tektufekci, 2017). Lastly, the Log GDP per capita is significant at its level and it has the positive association among the variables. On the other hand, the value of R-square is calculated as the 0.999 while the adjusted R-square showed the similar value of 0.999 [p=0] which shows that the impact is significant at its level. However, the association among the variables is much high which is the case of multicollinearity.

Table 3: Coefficients

Variable	***Coefficient***	***Std. Error***	***t-Statistic***	***Prob.****
LOG_GDP_(-1)	1.204333*	0.184075	6.542634	0
LOG_GDP_(-2)	-0.636397	0.121257	-5.24831	0
LOG_GDP_(-3)	0.071581	0.019733	3.627511	0.0013
BROAD_MONEY____OF_GDP_	-0.000154**	6.20E-05	-2.48829	0.0202
TRADE____OF_GDP_	8.88E-05	6.85E-05	1.296646	0.2071
TRADE____OF_GDP_(-1)	0.000307***	8.36E-05	3.66758	0.0012
CPI__BASE_2010_	2.44E-05	3.61E-05	0.676871	0.505
LOG(GDP_PER_CAPITA__CURRENT_US$_)	0.441245***	0.004425	99.7084	0
LOG(GDP_PER_CAPITA__CURRENT_US$_(-1))	-0.536236	0.081374	-6.5898	0
LOG(GDP_PER_CAPITA__CURRENT_US$_(-2))	0.292565	0.053493	5.469186	0
LOG(GDP_PER_CAPITA__CURRENT_US$_(-3))	-0.035697	0.009224	-3.86981	0.0007
C	2.783105	0.544763	5.10884	0***
R-squared	0.999967	F-statistic	66652.45	
Adjusted R-squared	0.999952	Prob. (F-statistic)	0	
Significant at 10%; **Significant at 5%; ***Significant at 1%				

DISCUSSION

With respect to the hypothesis of this study which is that there is a significant impact of trade openness on economic growth of Vietnam, it has been identified that there is no significant impact of trade openness on economic growth of Vietnam in the long run. This has been due to the reason that the trade openness is difficult for the country to handle as the country lacks the resources in terms of the human as well as technology to manufacture the goods. In this manner, the country will not be able to export the goods which will results in the trade deficit. This has also been argued in the study of Jariya and Hassan (2018) that more number of imports for the country cause the issue of negative balance of payments which results in the trade deficit. In this manner, the country can face huge loss in term of economic instability and borrowing funds from IMF. Overall, this will increase the interest rate in the country which will eventually increase the inflation. In this regard, the country needs to identify the benefits and impact of the trade openness on the economy of the country. This is due to the reason that the identification of the impact will result in the decision making capability of the country in terms of investing the capital for ensuring the growth of the country (Donald, 2019).

However, the analysis identified that there is a positive association of the trade openness on the economic growth in the short run. This means that the trade can impact the economy of the country in the short run. This has been due to the reason that the country can support the export capacity and has enough resources to cater the demands of exports in the short run. In this manner, the exports of the country can exceed its imports which will results in the positive balance of payments. This has also been argued in the study of Murindahabi, Li, Nisingizwe, and Ekanayake (2019) that increase number of export in the country can have positive impact on the economy of the country. This makes it necessary for the country to focus on the trade openness pertaining to the short term positive impacts on the economy of the country. In addition to this, the country can also support the demands of exports by reinvesting the revenues from exports in short term or with the promotion of foreign direct investment. This will help the country to support the increased demand of exports while acquiring the resources which helps in increasing the revenue of the country. The increased revenues will also ensure the growth of the business along with the growth of the economy.

CONCLUSION

With the advent of technology and rapid globalisation, trade policies are examined on timely basis due to the uncertainty in world economy. In this manner, the developing countries used to follow import substitution policy but later, many countries have moved to export led growth policies. There have been significant changes in the trade policies that involves export-based promotion strategies. Due to these policies, the countries are able to generate revenue by increasing the number of exports while stabilising the economy. This is due to the reason that the export of materials results in the inflow of cash which revolves and rotates in the economy of the country. In this manner, the country is able to strengthen the economic conditions. However, it is also necessary to consider the capacity of the country in terms of supporting or meeting the demands of the increased exports. This becomes crucial for the country in terms of balancing the net imports and exports. This is due to the reason that the balance of payments must be maintained.

In this manner, it makes it necessary for the country to identify the long and short term impact of trade openness on the economy of the country. Soon after the reform of Doi Moi in 1986, Vietnam has constantly been making efforts for the purpose of reviving the policies and strategies in order to stabilise their economic activities and ensure the economic growth. The economy diverted from agriculture based to industry-based economy though there were certain differences. On the other hand, the foreign investment law was established in 1987 after which FDI inflow increased in the country.

However, the laws were changed during the Asian financial crisis after which the foreigners were allowed to make investments in different sectors of Vietnam. Based on the analysis, it has been identified that there is no long term impact of trade openness on the economic growth of the country. This has been due to the reason that the country do not possess enough resources for the purpose of supporting the long term exports. In contrast to this, the short term impact of the trade openness has been identified on the economic growth of the country.

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