



# Informal Employment, Skills Mismatch, and the High-Growth Paradox: A Comparative Study of Vietnam and India

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## Article History

Received: 06.02.2026

Accepted: 25.03.2026

Published: 18.04.2026

**Abstract:** Vietnam and India rank among Asia's most dynamic emerging economies, each sustaining headline GDP growth rates above six percent in recent years. Yet beneath these macroeconomic achievements lies a persistent structural contradiction: the majority of workers in both countries remain in informal employment, while skills mismatches between educational outputs and labour market demands continue to widen. This paper examines how labour market informality and skills mismatch jointly constrain total factor productivity (TFP) and inclusive growth in Vietnam and India over the period 2015 - 2025. Situated within the structuralist and New Institutional Economics traditions, the study employs a comparative case study methodology combining secondary data analysis with institutional mapping. The findings reveal that both countries exhibit a "high-growth paradox" in which output expansion is driven predominantly by capital accumulation rather than efficiency gains, with informality and skills mismatch functioning as mutually reinforcing productivity drags. This paper contributes to the literature by providing the first systematic comparative analysis linking these three variables across Vietnam and India, and by deriving institutional policy lessons transferable across both contexts.

**Keywords:** Informal employment, skills mismatch, total factor productivity, Vietnam, India, emerging economies, New Institutional Economics.

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## 1. Introduction

The central puzzle motivating this paper emerged from a sustained reading of Vietnam's development trajectory: how does an economy sustain growth above eight percent while the majority of its workforce remains structurally excluded from the institutions that convert growth into opportunity?

Vietnam recorded a GDP growth rate of 8.02 percent in 2025, its second-highest since 2011, while India sustained a trajectory of between 6% and 7%, reinforcing its position as one of the world's fastest-growing major economies (ISEAS, 2026; World Bank, 2025). Yet, this narrative of achievement conceals a structural tension that has received insufficient scholarly attention: the simultaneous persistence of large-scale labour informality and widening skills mismatches even as aggregate output expands at historically exceptional rates. In Vietnam, more than half of the workforce operates without formal employment contracts or social insurance coverage (ILO, 2023; GSO, 2024). In India, informal workers constitute approximately 80% to 90% of total employment - a proportion that has changed little over decades despite rapid

growth and successive reform initiatives (Chen, 2012; ILO, 2023). Compounding this in both countries is a pronounced mismatch between skills that educational systems produce and those demanded by increasingly technology-intensive industries, a gap that FDI-led growth models have tended to exacerbate rather than resolve (Blomstrom & Kokko, 1998; Hanushek & Woessmann, 2015).

This paper addresses a gap in the comparative development economics literature by examining how informality and skills mismatch interact to generate what this study terms the "high-growth paradox": strong aggregate GDP growth coexisting with stagnant labour productivity, limited wage gains, and weak technological spillovers to the broader workforce. The paper makes three distinct contributions. First, it provides the first systematic bilateral comparison of Vietnam and India linking informality rates, skills mismatch indicators, and TFP performance within a unified analytical framework across 2015–2025. Second, it applies the structuralist tradition as represented by Portes and Haller (2005), La Porta and Shleifer (2014), and Levy (2008) and New Institutional Economics (North, 1990) to the institutional

## Cite this article:

Linh, N. T., (2026). Informal Employment, Skills Mismatch, and the High-Growth Paradox: A Comparative Study of Vietnam and India. *ISAR Journal of Economics and Business Management*, 4(4), 10-15.

configurations of both economies, offering a theoretically grounded diagnosis of why growth has not translated into labour upgrading. Third, it derives mutually transferable institutional policy lessons from each country's reform experience. The paper proceeds as follows: Section 2 critically reviews the theoretical and empirical literature; Section 3 provides comparative contextual background; Section 4 outlines the methodology; Section 5 presents the findings; Section 6 discusses implications; and Section 7 concludes.

## 2. Literature Review

### 2.1 Informality: Contested Theories and Evolving Evidence

The ILO defines informal employment as work arrangements lacking legal or social protection coverage, encompassing own-account workers, unpaid family workers, and employees in unregistered enterprises (ILO, 2018). The dualist tradition, inaugurated by Lewis (1954) and Hart (1973), treated informality as a transitional phase through which surplus rural labour passes en route to formal urban employment, implying that industrialisation would progressively absorb the informal sector, making intervention unnecessary. This account has been substantially contested by structuralist and legalist scholars. De Soto (1989) characterised informality as a rational response to excessive regulatory burdens, while Portes and Haller (2005) demonstrated that informality reproduces itself through institutional complementarities embedded in social relations, resisting displacement by market forces alone. The most damaging empirical critique comes from La Porta and Shleifer (2014), who find across a large cross-country sample that informal firms are systematically less productive and less innovative than formal counterparts and rarely graduate to formal status, characterising them as structurally different entities rather than simply smaller or younger formal firms. Perry et al. (2007) extend this critique to the labour market dimension, showing that informal workers are disproportionately excluded from skills development, formal credit, and social mobility pathways. North's (1990) institutional economics framework further explains why informality persists despite reform: where formal institutions are weak or inconsistently enforced, informal norms and self-enforcing social codes fill the governance vacuum, creating stable but low-productivity equilibria that formal rule changes alone cannot dislodge.

### 2.2 Skills Mismatch and Its Macroeconomic Consequences

McGuinness, Pouliakas and Redmond (2018) distinguish between vertical mismatch which is over- or under-qualification relative to job requirements, and horizontal mismatch, in which qualifications are in the wrong field. Both forms impose efficiency costs: over-qualified workers are underutilised, while under-qualified workers constrain employer technological capacity and create adoption bottlenecks. Crucially, the authors identify methodological contestation across self-reported, job-analysis-based, and realised-match measurement approaches - a limitation this paper acknowledges in its cross-country comparisons. Hanushek and Woessmann (2015) provide the most influential cross-country evidence linking skills to growth, demonstrating that cognitive skill quality, not years of schooling, is the decisive predictor of long-run GDP performance. Their findings imply that quantity-focused TVET expansions, of the kind pursued by both Vietnam and India,

will fail to resolve mismatch without commensurate quality improvement. Barro and Lee (2013) complement this with evidence that rapidly industrialising economies characteristically exhibit shortages of technical and managerial competencies coexisting with surpluses of general-education graduates - precisely the configuration observable in both case study countries.

### 2.3 Total Factor Productivity and the Limits of Accumulation-Led Growth

Young's (1995) influential decomposition of East Asian growth demonstrated that TFP contributed a modest share of output gains across Singapore, Hong Kong, South Korea, and Taiwan, with capital deepening accounting for the majority that have raised questions about the sustainability and replicability of high-growth emerging-market models. Collins and Bosworth (1996) extended these findings to a broader developing-economy sample, reaching broadly similar conclusions. Hsieh and Klenow (2009) add a crucial analytical innovation: resource misallocation - the failure to direct labour and capital to their highest-productivity uses - accounts for a substantial share of the TFP gap between China, India, and the United States. Their analysis implies that closing the wedge between formal and informal sectors can generate large TFP gains without requiring new technology or additional capital, framing formalisation as a macroeconomic efficiency imperative. No prior comparative study has applied the Hsieh-Klenow framework alongside an institutional analysis of informality and skills mismatch to the Vietnam - India dyad which is the gap this paper addresses.

## 3. Contextual Background

### 3.1 Vietnam: FDI-Led Manufacturing and the Limits of Enclave Formalisation

Vietnam's transformation since the Doi Moi reforms of 1986 has been remarkable. Total trade value exceeded US\$930 billion in 2025, GDP per capita reached US\$5,026, and the country achieved upper-middle-income status for the first time (Vietnam Briefing, 2026). Manufacturing and processing dominate FDI inflows, with electronics, textiles, and machinery underpinning export earnings. The government targets double-digit growth for 2026 - 2030 and high-income status by 2045 (ISEAS, 2026). Despite this, formalisation has occurred primarily within FDI-dominated manufacturing enclaves in a small number of provinces; agricultural workers, domestic service workers, and the self-employed, which comprises the workforce majority, remain largely outside formal arrangements (GSO, 2024; ILO, 2023). The TVET system has expanded in enrolment but suffers from outdated curricula and weak industry linkages, prompting foreign firms to develop proprietary training programmes whose benefits remain internal to the investing firm. In 2025, the government introduced a significant administrative reform, abolishing the district tier of government in favour of a two-tier province-commune structure designed to reduce regulatory friction and lower the cost of formalisation for small enterprises (Cimigo, 2025).

### 3.2 India: Services-Led Growth and the Durability of Structural Informality

India's growth is driven primarily by services which include information technology, financial intermediation, and business process outsourcing, while manufacturing's share of GDP has

remained below twenty percent despite Make in India and related industrial promotion programmes. GDP growth averaged 6% to 7% over the study period, supported by domestic consumption, infrastructure investment, and a recovering real estate sector (World Bank, 2025; OECD, 2025). India's aspiration of becoming the world's third-largest economy by 2030 depends on translating demographic dividends into productive employment which is a translation current labour market structures impede. Approximately eighty to ninety percent of employed Indians work informally, including an expanding cohort of gig platform workers - a "new informality" combining technological sophistication with the absence of social protection (Chen, 2012; ILO, 2023). India's ITIs enrol large numbers but face persistent criticism for poor instructional quality and weak employer linkage. The consolidation of 44 central labour laws into four Labour Codes between 2019 and 2020 is the most ambitious legislative reform in decades, but the majority of states had not completed implementation as of 2026, illustrating the implementation gap characteristic of federal reform in India (ILO, 2023).

### **3.3 Justification for the Comparative Framework**

The Vietnam - India pairing is analytically productive beyond surface - level similarity. Both economies compete to attract supply chain investment departing China amid geopolitical realignment, making labour quality a strategic differentiator. Both face an inflection point as wages rise and low-cost labour advantages erode, making the transition to productivity-driven growth urgent. Both have pursued significant reforms in the study period, creating natural variation in reform approaches. Crucially, their divergent configurations, referring to manufacturing versus services dominance, unitary versus federal governance, rapid versus incremental administrative reform, make the comparison richer than a simple most-similar-systems design. This also allows examination of how different institutional arrangements mediate common structural challenges.

## **4. Methodology**

### **4.1 Research Design and Analytical Framework**

This study employs a structured comparative case study design integrating secondary quantitative data analysis with institutional mapping grounded in New Institutional Economics (North, 1990; Yin, 2018). Vietnam and India are selected as a "most-similar systems with institutional variation" dyad: both exhibit rapid growth, high informality, and pronounced skills mismatch, but differ in economic structure, governance architecture, and reform trajectory - a variation providing analytical leverage for identifying

how institutional context mediates the relationship between the three focal variables. The analytical framework integrates three theoretical layers. At the macro level, the TFP decomposition tradition (Young, 1995; Hsieh & Klenow, 2009) establishes the productivity consequences of the structural features under examination. At the institutional level, North's (1990) framework explains informality's persistence despite growth and reform. At the micro level, the skills mismatch literature (McGuinness et al., 2018; Hanushek & Woessmann, 2015) informs the analysis of how vocational training failures interact with informality to produce mutually reinforcing productivity drags. This three-layer framework constitutes the paper's principal methodological contribution.

### **4.2 Data Sources, Period, and Limitations**

Secondary data are drawn from the ILO ILOSTAT database, World Bank World Development Indicators, ADB education and labour market reports, OECD Economic Survey of Viet Nam (2025), GSO (2024), MOSPI, UNESCO Institute for Statistics, and UNCTAD. The 2015 - 2025 study period captures pre-pandemic structural trends and the post-pandemic recovery trajectory, providing a temporal window sufficient to distinguish structural patterns from cyclical fluctuations. Three principal limitations apply: informality measurement methodologies differ between the GSO and MOSPI, limiting strict numerical comparability; harmonised sectoral TFP estimates are unavailable for both countries simultaneously, necessitating reliance on aggregate approximations; and the absence of primary data collection means firm-level and worker-level mechanisms are inferred from the literature rather than directly observed. These limitations are mitigated by triangulating across multiple secondary sources and maintaining transparency about inference boundaries.

## **5. Findings and Analysis**

### **5.1 Comparative Indicator Overview**

Table 1 presents key comparative indicators across the study period. Both economies have achieved measurable improvements across most indicators between 2015 and 2025, but the pace of improvement in informality reduction and TFP growth has been markedly slower than headline GDP growth would suggest which can be seen as a first-order empirical manifestation of the high-growth paradox. TFP's contribution to GDP growth remains below one third in both economies throughout the period, consistent with the capital-accumulation-dominated growth patterns identified by Young (1995) and Collins and Bosworth (1996).

**Table 1:** Comparative Labour Market and Productivity Indicators: Vietnam and India, 2015–2025

Indicator	Vietnam 2015	Vietnam 2025	India 2015	India 2025	Source
<b>GDP Growth Rate (annual %)</b>	6.7%	8.0%	8.0%	6.4%	World Bank (2025)
<b>GDP per Worker (PPP, USD)</b>	~5,800	~8,200	~9,100	~11,600	World Bank (2025)
<b>TFP Growth Contribution (% of GDP growth)</b>	~28%	~31%	~22%	~26%	ADB (2022); OECD (2025)
<b>Informal Employment (% of total employment)</b>	68%	55%	~88%	~82%	ILO (2023)
<b>Wage Growth – Informal Sector (annual %)</b>	~2.1%	~3.4%	~1.8%	~2.9%	ILO (2023); GSO (2024)
<b>Skills Mismatch Rate (% of employed)</b>	~42%	~38%	~47%	~44%	ADB (2022); OECD (2025)
<b>TVET Enrolment (% of secondary)</b>	~18%	~22%	~11%	~14%	UNESCO UIS (2024)
<b>Social Insurance Coverage (% of workforce)</b>	~24%	~38%	~19%	~27%	ILO (2023)
<b>FDI Inflows (USD billion)</b>	11.8	25.4	44.0	71.4	UNCTAD (2025)

\*Note: TFP contribution is approximated from growth decomposition estimates. Skills mismatch rate reflects the share of employed persons reporting qualification-job misalignment in employer and household surveys. All figures are approximate due to cross-national measurement variation.

### 5.2 Informality Trends: Structural Persistence with Divergent Configurations

Labour market informality has declined only marginally in both countries despite sustained economic expansion. In Vietnam, the informal employment share fell from approximately 68% in 2015 to around 55% by 2025 - a reduction concentrated almost entirely within FDI-dominated manufacturing enclaves, while agricultural, domestic service, and self-employed workers remain largely outside formal arrangements (ILO, 2023; GSO, 2024). In India, the share declined negligibly from 88% to 82%, with limited formalization, even in sectors targeted by Make in India. A critical structural distinction lies in the spatial configuration of informality: Vietnam's informal sector is relatively concentrated in rural areas, creating a discernible geographic boundary between formal manufacturing zones and informal hinterlands. On the other hand, India's informality is more diffuse when penetrating urban labour markets and increasingly present in technologically sophisticated sectors through gig employment. This suggests that it is structurally harder to address through geographically targeted industrial policy. In both cases, the La Porta and Shleifer (2014) finding is confirmed: informality has not declined as a natural consequence of growth, and the dualist prediction of automatic absorption into the formal sector has not materialised.

### 5.3 Skills Mismatch: Quality Failures Over Quantity Shortfalls

Despite expansion in Vietnam's TVET enrolment and the large scale of India's ITI network, employer-reported mismatch rates have declined only marginally in both countries (ADB, 2022; OECD, 2025) which are consistent with Hanushek and Woessmann's (2015) finding that educational quantity without quality improvement fails to resolve mismatch. In Vietnam, the central failure is supply insufficiency at the higher technical and engineering levels: multinational manufacturers consistently report difficulties recruiting adequately trained technicians and resort to proprietary in-house training that generates human capital without broader spillover effects. In India, mismatch takes the form of quality and relevance failures rather than enrolment shortfalls: ITI graduates frequently possess credentials but lack practical competencies, reflecting curricula developed with minimal employer input. Critically, both forms of mismatch interact with informality in a compounding cycle: informal workers are systematically less likely to access training than formal employees, perpetuating low skills, which perpetuate the low-productivity informal employment that is all that is accessible without recognised qualifications — a mechanism consistent with Perry et al.'s (2007) characterisation of informality as an exclusion rather than merely an exit phenomenon.

#### **5.4 TFP Performance and the Productivity Gap**

TFP's contribution to GDP growth: approximately 28% to 31% in Vietnam and 22% to 26% in India across the study period. Such figures are substantially below contributions observed in economies that have successfully transitioned to productivity-driven models such as South Korea in the 1990s. Capital deepening, driven by FDI inflows and public infrastructure investment, accounts for the dominant share of output expansion in both countries, directly replicating the pattern Young (1995) identified for earlier East Asian developers and raising analogous sustainability concerns as diminishing returns to capital accumulate. Applying the Hsieh and Klenow (2009) misallocation lens, the coexistence of highly productive formal-sector firms, such as multinational subsidiaries in Vietnam, large-cap IT firms in India, with vast arrays of low-productivity informal enterprises represents a significant resource allocation inefficiency. Reducing this misallocation through formalisation and skills upgrading does not require new technology. In fact, it requires institutional reforms that close the wedge between formal and informal sectors - reforms that both countries have pursued, but incompletely.

#### **5.5 Reform Assessment: Divergent Approaches, Common Shortfalls**

Vietnam's most significant reform, which is the 2025 abolition of the district tier of government, directly lowers the administrative cost of formalisation by reducing the bureaucratic interfaces small enterprises must navigate (Cimigo, 2025). Complementary measures including an extended reduced VAT rate and major infrastructure investment are coherent, centrally coordinated, and implementation-focused, reflecting the advantages of Vietnam's unitary governance structure. India's reform agenda is more ambitious in legislative scope (the consolidation of 44 central labour laws into four Labour Codes) but more fragile in implementation: the majority of Indian states had not enacted the codes as of 2026, reflecting the federal coordination challenges that Papola and Pais (2007) identified as systematically limiting earlier Indian labour reform cycles. India's skills initiatives, including PM Vishwakarma and the Skill India Mission, represent meaningful efforts but independent assessments consistently identify gaps between enrolment targets and labour market placement, suggesting that programme design has prioritised scale over relevance.

### **6. Discussion**

#### **6.1 The Common Trap: Accumulation-Led Growth Without Labour Upgrading**

The comparative analysis reveals a structural trap applicable to both economies despite their different models. Headline growth has been sustained by attracting foreign capital into sectors exploiting low-cost labour rather than by catalysing a transition to higher-value production anchored in domestic skills and institutional quality. As Baumol, Litan and Schramm (2007) argue, economies dominated by replicative rather than transformative entrepreneurship face a productivity ceiling that becomes increasingly binding as factor cost advantages erode. Both Vietnam and India are approaching this ceiling. The model that has delivered impressive welfare improvements in poverty reduction, rising formal-sector wages, infrastructure expansion carries within it the structural constraint that makes its continuation increasingly

difficult: without labour upgrading, the next phase of growth cannot be powered by the same inputs that drove the last.

#### **6.2 Informality as an Active Cause, Not a Passive Symptom**

A central contribution of this paper is the reframing of informality from a symptom of underdevelopment to an active cause of productivity stagnation. The conventional policy literature in both Vietnam and India positions informality as a poverty correlate that will diminish as growth proceeds. The evidence assembled here directly contradicts this view. Informal workers are excluded from employer-sponsored training, statutory apprenticeship schemes, social insurance enabling worker mobility, and formal financial markets that creates a self-reinforcing cycle in which informality perpetuates low skills, which perpetuate low productivity, which perpetuate low wages, which make formal employment's compliance costs unattractive to both workers and small firms. Levy's (2008) analysis of how institutional design inadvertently subsidises informality confirmed here for Vietnam and India implies that breaking this cycle requires simultaneously reducing the cost of formality and increasing the relative cost of informality, a dual intervention that neither country has yet implemented with sufficient coordination.

#### **6.3 Cross-Country Institutional Lessons**

The comparison yields concrete transferable lessons. India's institutional infrastructure for skills development such as the ITI network, National Skill Development Corporation, and sector skills councils offers Vietnam a model of institutional scale it has not yet achieved, though Vietnam must replicate India's breadth while avoiding its quality and relevance failures. Specifically, Vietnam could adopt employer-led sector skills councils, an approach that has improved training relevance in economies including the United Kingdom and Australia (ADB, 2022). Conversely, Vietnam's administrative reform boldness, particularly the consolidation of governance tiers to reduce firm-level regulatory burden, offers a model India could pursue through state-level regulatory simplification without requiring federal consensus. Both countries would benefit from redesigning social protection systems to decouple benefit access from formal employment status. This can eliminate the structural incentive that currently makes informality rational for workers and small firms alike (Perry et al., 2007; Levy, 2008) which is also an approach consistent with the ILO's Social Protection Floors Recommendation and implemented with measurable formalisation effects in Brazil and Thailand.

### **7. Conclusion**

This paper has examined the high-growth paradox, which refers to the coexistence of strong GDP growth with persistent labour informality, skills mismatch, and constrained TFP, through a comparative institutional analysis of Vietnam and India over 2015 - 2025. Despite their markedly different economic structures, both countries face a fundamentally similar challenge: growth models built on capital accumulation and low-cost labour that have delivered impressive headline outcomes but have failed to generate the labour market transformation required for inclusive and productivity-driven development. Three findings stand out. First, informality has declined only marginally despite sustained growth, confirming the structuralist position that it constitutes a self-reinforcing institutional trap. Second, skills mismatches reflect deep institutional failures in training system design rather than

mere under-investment - the failures that North's (1990) framework explains as the product of misaligned incentive structures and weak enforcement. Third, TFP data confirm that capital accumulation rather than efficiency gains drives the majority of output growth in both economies, consistent with the Hsieh and Klenow (2009) misallocation framework and Young's (1995) cautionary analysis.

The policy implications are actionable and specific. Both governments should condition FDI incentive frameworks on domestic workforce training and formalisation commitments by investing firms, shifting from labour-cost attraction toward labour-quality development. Investment in TVET quality, through employer-led curriculum governance, competitive accreditation, and expanded apprenticeship systems, is more urgent than further enrolment expansion. Social protection floors should be extended to informal workers without penalising formal employment, eliminating the structural subsidy to informality. Administrative simplification should be treated as a macroeconomic efficiency priority. Future research should pursue firm-level and worker-level primary data collection in both countries and incorporate econometric panel analysis as harmonised cross-national datasets become available. The high-growth paradox is not structurally inevitable but resolving it demands institutional ambition commensurate with the macroeconomic aspirations both Vietnam and India have set for the decade ahead.

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