solving unemployment. Business has gradually been used to mechanism of repayment based on interest rate and a more favorable borrowing conditions than that in the market, not depending much on the State as before, taking responsibility for utilizing capital efficiently, being able to liquidate.

We have established a necessary control mechanism for the foreign debt activities of the whole economy, maintaining the borrowing limit and duty of annual liquidation. The debt management is gradually organized, combining the borrowing with utilizing debenture capital and the efficiency of using funds of the economy.

4.2 The remaining matter of foreign debt management.

Although the legal framework for foreign debt management has been completed step by step, it has shown some matters recently, as follows:

Viet Nam has not created borrowing strategy and policy efficiently. In fact, Viet Nam has yet to create the long- run profit maximizing debt strategy. Viet Nam has not defined its suitable mechanism all-sized and systematic borrowing (ODA loans and commercial loans) and guaranteed to pay debenture capital, avoiding putting burden on state budget. At present, the policy is focussing on mobilizing and making full use of capital sources from foreign countries but it hasn't put the amount of absorbing capital together with the capability of payment in the future. The present strategy of managing foreign debt hasn't considered the firmness of foreign debt in the active relationship of occurrence of macroeconomy and balance of payment. Although the Vietnamese burden is in safe confines, foreign debt of Viet Nam since 1993 are in grace period and liability will increase in the following years.

The ODA disbursement has recently made progress but it is still estimated to be slower than that of regional countries by sponsors. The low disbursement causing delay in ODA projects, affecting the result of investment. In addition, it diminishes the favorableness of ODA and the influence on receiving prestige and movement of capital in Viet Nam. For some projects, the project considering and deciding is done without care and economic borrowing condition and tie-condition, we haven't taken the initiative in choosing list of projects according to planned target before calling investment, there is still unplanned situation of utilizing capital, we haven't defined clearly which projects have to be re-lend and which projects are supplied by the state budget.

Ability of project manager is limited. The staff is equipped with insufficient professional skill and knowledge leading to inactivates in management and preventing hazard of interest rate. Generally, debt management is still passive.

Mobilized foreign capital is used for too many targets not for an especially prior investment objective.

Inspection and supervision of implementing projects are paid little attention and they are not organized constantly. This element together with insufficient report and information has caused difficulties for evaluation debt situation and result of utilizing borrowed capital. It hasn't set up a co-ordination mechanism of information between state officers in managing foreign debt.

Part 2 Securities market development program

The establishment and development of the securities market are the majority of mobilizing capital strategy as well as accomplishment of the market economy in Viet Nam. In order to carry out the policy of Government that is: "developing the capital market, attracting the medium and long-term capital sources through banks and financial companies to meet the demand of borrowing for investment, preparing the necessary condition to set up the securities market suitably Vietnamese condition and orientation of national socio-economic development..." the Government have done a lot both theoretically and practically to put the securities market into operation in the year 2000. When researching the progress of the securities market development in Viet Nam, if is necessary to consider 2 main fields: the policy on organization apparatus, legal framework for execution of the securities market and the reality of preparing goods for securities market.

A. Organization apparatus and legal framework for securities market operation

It has been a major policy of our Party and State to create the required conditions for the step-by-step establishment of the securities markets in Viet Nam, some legal Documents on Securities and Securities markets have been issued.

Decree No.75/CP dated 28 November, 1996 of the Government on establishment of the State Securities Commission, as an agency under the Government to perform State administration and organization functions on securities and securities markets.

Decision No. 127/1998/QD-TTg dated 11 July, 1998 of the prime Minister of the Government on establishment of the Securities Trading Centers in Hanoi and Ho Chi Minh City.

With the two legal documents, the structure and working apparatus of SSC and Securities trading centers step-by-step establishment. From the beginning, SSC tried its best to train, recruit, arrange working apparatus by sending its staffs to abroad (Korea, Thailand, US, China...) and opening many training courses on securities in Viet Nam for commercial banks, insurance companies, enterprises in order to select securities traders for future operation.

Besides, SSC are responsible, in co-ordination with agencies concerned, for building initially legal framework on securities issuing and trading in trading centers. As a result, Decree No.48/1998/ND-CP dated 11 July 1998 of the Government on securities and securities markets Circular No guide 01/1998 guide Decree No.48/CP on public offering. These new legal documents stimulated fully on public offering, securities trading, financial intermediatory, secondary markets...

Securities issued to the public (Decree No.48/CP) shall be in forms of either certificates or book-entries, and either register or bearer. Par value of a share and investment unit shall be 10,000. The minimum par value of bonds shall be VND 100,000.

In order to ensure the efficient operation for securities market, the Decree stimulated securities issuing, trading in Securities trading centers.

An issuer undertaking an initial public offering of its shares shall have to meet the following criteria: Having an minimum registered capital at VND 10 billion; having been profit making in the last two consecutive years; having members of the Board of Directors and the Chief Executive Officer with experience in business management; having prepared a feasible plan to utilize the proceeds obtained from the issuance of shares; having at least 20 percent of its equity offered to more than 100 investors; having a contract with an underwriter if the total value of shares to be issued (in par value) exceeds VND 10 billion.

Decree No. 48/CP issued criteria for information, issuers must comply with the reporting regime as prescribed by SSC.

Decree No. 48/CP initially stimulated a very important financial intermediatory, underwriter. An underwriter of a public offering shall be a securities firm that meets the following criteria: possessing a license on securities underwriting activities; not being an affiliated person of the issuer. The underwriter shall be entitled to underwrite an issue where the total value of the securities thereby does not exceed 4 times of the difference between its current assets and current liabilities.

General, Decree No. 48/1998/ND-CP shall govern securities public offering, securities trading and information and securities market-related businesses in order to protect the lawful interests of investors. Although the stimulation on public offering in this decree applied only for those who trade in securities centers, it also create the required conditions for the starting establishment and development of the securities markets in Viet Nam.

B. Preparation goods for securities market

In the last stage, Viet Nam has made great effort to create goods and favorable conditions to put the securities market into operation in the initial period. This is especially shown by the progress of the bond market—an important component element of the securities market, a standard stock for others. Besides, capitalization is also focused on and pushed up. It not only has influence on improving business but also promotes and creates long-term goods for the capital market.

1. The bonds market

1.1 The legal framework of the bonds market

After the 6th National meeting of communist party, especially during 1990s, the state budget management has had a profound and wholly reforms on both policy and organization apparatus. In that situation, Treasure System was founded according to the Decision No.07/HDBT dated on January 4th 1990 in order to hand over the duty of managing the state budget fund to Ministry of Finance. As soon as the Treasure System was established, the capital mobilization for the State and for investment has shown clear changes in quality.

Stemming from the capital demand for investment, the Government has gradually institutionalized the capital mobilization by Decree No.72/ND-CP of the Government dated on July 26th 1994 on regulation of issuing bonds, marking a basis change in the quality of view, acknowledging the mean and importance of the creating capital strategy. The Decree pointed out 3 kinds of bonds: treasure bonds, treasure securities, National contruction bonds. Bonds are traded in the stock market, used in transferring relationship, inheritance, collateral and mortgage and guaranteed to liquidate on time by the Government. Bonds holders are guaranteed to enjoy the real interest plus inflation index.

Investors who are permitted to purchase bonds are: Vietnamese who are living in or out of Viet Nam; foreigners who live and work legally in Viet Nam; Vietnamese enterprises of all fields and economic sectors (including banks, insurance companies, financial firms, insurance and investment funds); foreign invested capital companies operating under Foreign investment law in Viet Nam and state bank law was approved by the Ministry of Finance to purchase bonds.

The issue of bonds is carried at under there ways: (1) Direct issue through the state treasure; (2) issue through financial intermediatory: commercial banks, fianance and insurance companies; (3) issue by auction.

The Decree No.72/CP of the Government created a primary legal framework for the issue of bonds with abundant ways of issuing. However, Decree No.72/CP still has much inadequacy, for example the definition of various kinds of bonds are poor, it can't reflect the essence and target of issuing. The regulation of issuing and transferring mechanism haven't created favorable bonds trading, the decree hasn't dealed with the way of issuing through brokerage agents in securities market, which is applied widely by many Governments. The regulation stimulated the state bank of Viet Nam has right to auction on State bonds isn't adequate with state bank law and international routine. Transferring possession of treasure bonds and National contruction bonds carried out through the state treasure cause difficulties to securities trading in the secondary market. Bonds are traded with limited volume and short time. That's why although the issuing turnover is high but the actual budget deficit is still low. Bonds haven't actually taken the role as a "standard debt" toll in capital market and currency market.

In order to complete the capital mobilization through bonds, the Government issued Decree No.01/2000/ND-CP dated on January 13th 2000 on regulation of bonds issuing replacing Decree No.72/ND-CP. This new decree stimulates relatively conceptions on bond essence, the responsibility of relevant authorities in managing bonds market. Especially, the decree creates new ways of issuing which are suitable with international routine such as: issuing guarantee and auctioning bonds though securities trading center. This is a breakthrough for the development of state bonds market in particular and for capital markets in general. Moreover, the Decree also stimulates some ways of transference, securities custody and security payment, and making favorable conditions for trading bonds in securities market. Together with the state budget law and state bank law, Decree No.01/2000/ND-CP has set up a primary legal framework for the capital mobilization, marking a new base and very important step of view, acknowledging the mean and importance of creating capital strategy.

But in addition, Decree 01/2000/ ND-CP still has inadequacy with the economic development, for example, restriction of the outstanding debt rate in response with local National contruction bonds is still low (as it has to be adjusted to the state budget law). It is also conflicts with the Decree No.63/ 1998/ND-CP of the Government on managing foreign currency...In order to stimulate actually the development of the bonds market, it is necessary to improve the legal essence, including publishing, trading and liquidating; if necessary we can adjust legal document concerned to the bonds market in order to make it suitable with the new situation.

In addition, for mobilizing the financial source from the social economy and concentrating on building constructions for human beings, the National assembly standing committee passed the ordinance on Government bonds replacing that improved by National Committee on November 25th 1993 in these basic following points:

- In order to mobilize the financial source from society for investment in national key projects and other essential projects serving for human beings, the Government issued Government bonds. The bondholders are both Vietnamese individuals and organization who are working in or outside; foreigner and foreign organizations living and working legally in Viet Nam.
- The Government guarantee the money value purchasing Government bonds with the real interest not less than 15% per year after inflation. The 5-year Government bonds is issued in unidentified certification and the state objectives (in the year 2000, Government bonds are issued to mobilize capital for agriculture and rural economic development, especially for these areas facing economic difficulties).
- Government bonds are permitted to transfer inheritance and mortgage.

The renewed ordinance on Government bonds overcame the restriction of that issued on November 25th 2000, reducing inflation hazard, organizing methodically and synchronously the professional skills of issuing; investors from mobilized capital are clearly defined. The amount received from Government bonds issuing are small but we can mobilize capital source in cash from citizens to invest in some key projects and realize the wise policy of the Government in mobilizing the long term capital for economic development.

1.2 The situation and result of capital mobilization by issuing state bonds

The state bonds market after issuing Decree No.72/CP

- *Treasure bonds*: Putting the decree No. 72 of the Government into action, national treasure has issued 1 year maturity treasure bonds including bonds pre-printed denomination without par value and bonds without pre-printed denomination with par value; since April 1995, issued

3 year-medium bonds since 1994 and 2 year bonds from September 10th 1996. This stage marked an important step in the process of reforming and completing the capital mobilization mechanism through the State treasure. The debt mechanism has gradually changed from short-term to medium term that lengthened and improves the efficiency of utilizing the state capital. Moreover, the issue of various bonds such as: registed bonds and unregisted bonds; bonds with and without par value; which are freely convertible throughout the country has drawn great attention of consumers and created a material premise to set up the capital market in Viet Nam. A fairly successful result of the issue proved the ability of mobilizing medium- term capital in the economic for the state budget and investment.

- *National contructiont bonds*: Ministry of Finance co-ordinate with Ministries and industries concerned for building projects and mobilizing capital under the cover of construction bonds such as Ho Chi Minh city bonds, Hoang Thach cement bonds, Anh Son and Phuc Son cement bonds. Thanks to this way of capital mobilizing , many projects were completed attributing to economic development for the past few years.
- *The treasure bonds auctioning market*: the Ministry of Finance has collaborated with the state bank of Viet Nam to auction treasure bonds to meet the paying demand of the state budget (with the maturity: 6 months, 9 months, 12 months). Investors participating in auctioning treasure bonds are commercial banks, financial firms, insurance companies and social insurance funds...

The result of auctioning treasure bonds

Year	Batches	Auctioned bonds volume (billion)	Auctioned bonds price (billion)
1995	04	243.6	222
1996	19	1,026.4	949.0
1997	37	2,917.5	2,637.3
1998	46	2,602.7	2,331.4
1999	46	3,001.6	2,772.1
Total	152		

The total issuing and liquidating turnover of all state bonds from 1991 to the end of 1999 was announced in appendix No.1

The state bonds market after issuing Decree No.01/CP of the Government

The implementation of Decree No.01/2000/ND-CP of the Government, in the year 2000, the Ministry of Finance organized the auctioning of treasure bonds through the state bank. Up to April 15th 2000, thirteen batches were auctioned, gained 2,136 billion Dong for the state budget. Since March 1st 2000, the Ministry of Finance has retained 2-year bonds through the Treasure System with the interest rate of 7% per year; the turnover was 1,369 billion VND reckoning to April 30th 2000. By now, we have held 2 auctioning batches in Ho Chi Minh securities trading center. The first one was held on

July 26th 2000 with the mobilized capital of 300 billion VND and 5 year maturity with the interest rate of 6.5% per year. The second one was held on August 15th 2000 with the same amount of mobilized capital and 5 year maturity with the interest rate of 6.6% per year. In the near future, the state treasure will collaborate with State Securities Commission to take a new way of issuing that is underwriting. This is the first success of mobilizing long term capital with the procedure suitable with international routine.

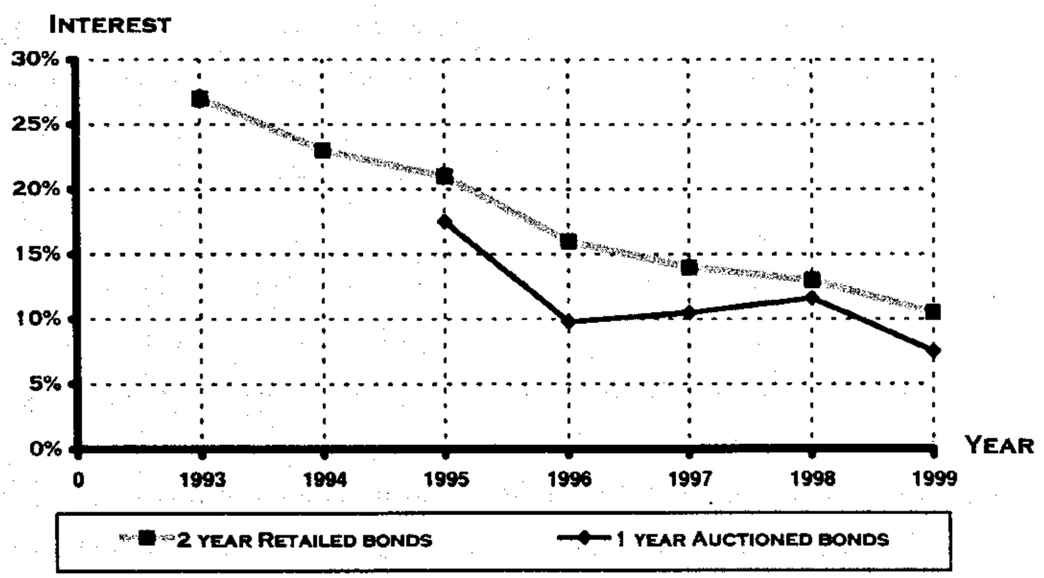
The ordinance on issuing Government bonds dated on April 4th 1999 regulated the interest rate of bonds is 10% per year. If the inflation comes over 42% after 5 years, the Government will adjust the interest rate to ensure the real interest is 1.5% per year. If the inflation after 5 years equal to or lower than 42.5%, the investors will enjoy the interest rate about 50%. After 2 months, capital mobilization reached 4,496 billion, equal to 112.4% as we planed.

1.3 Appreciation of the result

- *Achievements*

Diverse form of bonds has created standard commodity and interest in order to establish and develop capital market and help the state bank conduct currency market. After ten years, implementation of bonds issue has shown considerable progress, at first, there is only treasury credit bill retailed via the State Treasury with very short maturity (3 months, 6 months in 1991), now Government bonds with longer maturity and diversified, modern forms of issue such as auctioning through the stock trading center. Bonds issuing is step by step close to the world's issue technology. Interest rate of Treasury bond and credit bill is listed in the interest rate of currency deposits and loans and has annually decreased.

The average interest rate of treasury bonds



- *Backwards*

Government bonds have short maturity, mainly 1 or 2 years, no bonds with 5 years maturity. Thus, The usage of capital becomes passive due to balance of payment. Repurchasing and resaling bond on the secondary market is not encouraged with this present issue style. Government bonds have not yet been standardized so it can't be listed on the securities market.

There are not many kinds of bonds. Modern form of bonds such as discounted bonds and called bonds have not issued so we can't make the usage of capital potential in our society. The technology for issuing bonds has not fully done, mainly retail. The certain scheme for bonds issue has not built.

2. Capitalization of state-owned enterprises in the period of 1990-2000

First- time suggestion on capitalization of state-owned enterprises was in the Decision of the second meeting of the 4th Central Committee (11/1971): "capitalizing some state-owned enterprises into joint-stock companies and founding some new as experiment and have tight guideline, and draw experiment before expanding enterprise equitization". After 8-year implementation, the process of equitization can be divided into 2 main stages:

- *Experimental stage (1992-1995)*

The Decision No.202/CT dated on June 8th 1992 of the Chairman of Ministry Council on equitazing some state-owned enterprises into joint-stock companies and the Instruction No.84/TTg on March 4th 1993 of the Prime Minister was aimed to encourage the process of equitization. At this period, the capitalization took place very slowly. Up to May 1996, there were only 5 join-stock companies in the whole country: Transportation Agent Coporate (1993), REE company (1993); HiepAn footwear compay (1994); Export Processing Company (1995) and Animal food Processing Company (1995). Some reasons for the slow speed of capitalization: Ministries and relevant Agencies had no detail and timely guideline on capitalization, regulations of capitalization were not really attractive; equitazation policies on economic management; equitazation policy was not synchronous with other law documents on economic management. Thus, enterprises met difficulties in equitazing. In addition, managers, staffs and other classes had less confidence in equitaization policy of the state.

- *Expanding stage (after 1996)*

On May 7th 1996, the Government promulgated Decree No.28/CP of the Government in order to encourage the process of restructuring the state-owned enterprises, step by step accomplish legal framework, and speed up the process of capitalization. The Decree. No 28/ND-CP of the Government on moving state-owned enterprises to joint-stock companies. This new Decree has surmounted some shortcomings of Decision No.202/CT and created favorable conditions for enterprises capitalization. Under the regulations of Decree No.28, joint-stock companies have still maintained positive side of management, reduced negative aspects and adopted with the market mechanism. Rights of labors (shareholders) come together with rights of the company, the implementation of equitazation has changed the ownership from state into shareholders. All these things make workers themselves really own companies. So, companies can exploit and mobilize every source of capital in the society to invest in production...The recent achievements of 17 equitized enterprises have clearly shown out positive aspects of equitization. In detail, capital: 45% rise at average; turnover: 57%, profit: 70%, income of labors increases 20%.

However, after a short time of implementation, Decree No.28/ND-CP of the Government shown many unsuitable regulations which needs improvin:;, such as: rights of state-owned enterprises equitized to become joint-stock companies; rights of labors, especially low-income labors, the management of state joint-stock companies. In addition to, the jurisdiction over equitization of enterprises are not clear and specific, equitization procedure is so complex... with above difficulties, from May 1996 to the middle 1998 (3 years), there are only 25 equitized enterprises, much lower than the plan.

With new determination in the implementation of equitization, on April 21st 1998, the Prime Minister promulgated Instruction No 20/1998/CT-TTg on arranging and renovating state-owned enterprises. Accordingly, state-owned enterprises are divided into 3 groups: 100% state-owned enterprises equitized enterprises and enterprises that have prolonged losses. The instruction No.20/1998/CP-TTg of the Prime Minister required Ministries, provinces and general companies 91 to select at least 20% of business without 100% State capital to equitization. Besides, the Government promulgated Decree No.44/1998/ND-CP dated on May 7th 1998 of the Government replacing Decree No.28/ ND-CP. Decree No.44 includes many positive and expanding regulations with some drawbacks of Decree No.28 such as: the problem of evaluating business' ability, jurisdiction over business evaluation and rights of labors. Decree No.44 is appreciated to have many good points such as: process of simplifying equitazation procedures, social welfare for labors. After Decree No.44 of the Government came into force, Ministries and relevant agencies have had guideline documents to create a relatively synchronous legal framework on equitization of state-owned enterprise. With this new policy, in 1998, 86 state-owned enterprises were equitized (out of 150 enterprises had registered0, raising the total number of joint-stock companies up to 116 business from 1992 to 1998.

In order to implement actively the arrangement and equitization of state-owned enterprises, on August 3rd 1998, the Prime Minister promulgated Decision No.117/QD-TTg on the Assistant Fund. The main goal of the fund is to use financial methods to deal policies for labor and support state-owned enterprises to overcome financial problems before and after implementing equitization. In addition to, on June 25th 1999, the Prime Minister also promulgated Decision No 145/1999/QD-TTg on saling shares to foreign investors on an experimental basic. Up to the end of 1998, the total number of joint-stock companies has been 250, raising the number of enterprises, which has changed their ownership up to 370.

So, the establish of two new commodities Government bonds and state-owned enterprises'share has created favorable and important conditions for Viet Nam securities market coming into operation...

The establish of the securities market is indispensable, supports and encourages the economic development on the basic of clearing and expanding every capital source and meeting the need of capital for investment and development. With efforts and cooperation between Ministries and agencies concerned, on July 20th 2000, the HoChiMinh city securities market was officially opened and come into operation. In spite of its small size of transaction, the establishment of the HoChiMinh city securities trading center has marked imitatively successes in the implementation of our Government policy: "speed up social investment, increasing both accruement and domestic investment through the state budget, enterprises and citizens. Developing currency and capital market, establishing the securities market" (Document of the 8th National Congress).

E. Public Investment and the Issues of Its Finance

E − 1

Overview of Investment Situation and Policy in Viet Nam in the 1990s[1]

Le Viet Duc

Ministry of Planning and Investment

Investment has been one of the most important factors contributing to the high economic growth of Viet Nam through the period of economic reform, which started from 1989. Primary analyses show that there are converse trends of investment in the two periods: 1991-1995 and 1996-2000. The most concerned trend is that the growth rate of investment in the second period has decreased too much in comparison with that of the previous period. In order to rationalize causes of those trends, this report will examine investments in state sector, state-owned enterprises (SOE), private sector and households as well as foreign invested sector during the 1990s in the following aspects:

- Investment trends in the above 4 sectors;
- Reviewing investment regimes in those sectors
- Assessing problems and difficulties of current investment policies.
- Discussing some measures to amend investment regime in the next 5 years.

In the following part, we will analyze current policies on investment to see how much they help effectively allocate investment capitals, which are actually a scarce resource of the country. Particularly, the paper will discuss in detail the efficiency of public investment mechanism. Finally, in the annex 2, we will list pieces of legislation regarding the mechanism and policies on investment in the above 4 economic sectors.

Part 1 Investment situation and policy

A. Situation and policy of public investment

1. Public investment trend

Public investment is excised by the Government through 2 sources of fund: Non refund budget capital and state credit with low rate and favorable conditions. Non refund budget capital is mainly reserved to projects on infrastructure construction and human resource development sectors, which are not capable to take a very long time to return capital. State credit is a form of loan with low interest rate and favorable conditions provided to prioritize projects identified in the state development plan.

The main trends of public investment from 1991-2000:

[1] Le Viet Duc, Ha Xuan Tu and Le Quoc Ly, Ministry of Planning and Investment.

(1) With regards to the non refund state budget capital:

1) Investment from state budget capital during the last 10 year did not enjoy a stable growth. Even though its value estimated by current prices increased steadily (except a light decrease in 1994), its value by constant price increased rapidly in 1992, 1993, 1996 and 1997 but had a minus growth in 1994, 2000 or very small growth in 1998.

2) However, in overall, investment from state budget was in a going-up line in the period 1991-1993 and gradually going down from 1994 till present. On average, the growth rate of investment from state budget is 21.2% from 1991-1995 and 14.1% from 1996-2000. Thus its share in the total social investment reduced from a relatively stable ratio of 35% on average in the period 1999-1993 to a stable rate of 21% in the period 1995-2000.

3) Regarding the structure of investment from state budget capital classified by the hierarchy of administration, the share of capital managed by central authorities increased during the period 1991-1993 from 52.9% to 66% then reduced to 45.7% in 1998. Conversely, the share of public investment from local authorities' budget has increased sharply form 1994 till now after a heavy drop during the period 1991-1993.

4) Regarding the structure of using state budget classified by economic sectors, the years 1994 and 1995 marked a structural change. Before 1994 and 1995, the ratio of investment in industry and construction increased very rapidly while the share of investment in other economic sectors considerably reduced. On the contrary, after 1994 and 1995, the ratio of investment in the first 2 sectors sharply decreased and the proportion of state budget capital invested in agriculture, forestry, fishery, irrigation, infrastructure, trade and services has increased very quickly.

There is a clear trend that state budget capital is concentrated to the construction of infrastructure and human resource development as expected target in order to create necessary conditions for the development of other economic sectors.

(2) Preferential state credit

1) State credit as well as other sources of capital did not experience a stable growth in the 1990s. However, it has been a source of the most rapid increase. Its growth rate was minus 50% in 1992, but went up to 200% in 1993 then reduced to 21% in 1994 and even dropped to minus 27.3% in 1995. In 1996, it again enjoyed an expected growth up to 116.9% but very quickly dropped down to 16.7%. Since 1998, its growth rate has been increasing thanks to the policy of investment promotion of the Government.

2) Because of its high growth rate, the share of state credit provided to enterprises in the total of social investment increased very quickly: this share increased from 3.2% in 1993 to 10.4% in 1996

and 19.9% in 2000. Thus in the year 2000, the share of this capital is approximately equivalent to share of public capital and higher than the self-capital of enterprises or FDI.

3) In a general trend, state credit in 1990s was more and more focussed on prioritized projects identified in plans and economic development programs of the country, especially projects aiming at developing and enhancing the effectiveness of state owned enterprises (SOEs) in the key sectors such as irrigation, multi-year crops, agricultural science and technique and infrastructure for agriculture production. In industrial sector, public investment is allocated with priority to important sectors such as electricity, cement, steel, fertilizers, petro-chemical and agriculture processing.

4) Even though the economy has been reformed towards market based economy for many years, it is recently in a tendency of returning to the old mechanism, i.e. soliciting-giving mechanism, subsidization of credit as it was in the period of central planning Such a mechanism is actually a subsidization in terms of credit for non-competitive products and prolongs the lives of ineffective enterprises.

2. Evolution of public investment policy

Public investment policy has been considerably changed since late 1980s. In 1989, the Government of Viet Nam reduced sharply the subsidization to SOEs in terms of investment; public investment is concentrated to the development of infrastructure and social welfare. In fact, many enterprises are not capable to cope with this change and the number of loss making enterprises increased dramatically. It implies so much pressure that the Government has to return to the regime of credit subsidization to help enterprises.

From 1994 and 1995, the Government reapplied policies of 1989, i.e. prioritizing public investment to sectors undesired by private enterprises. From 1994 and 1995, the Government's policy is to reduce considerably its investment to industry sector and to increase investment in infrastructure, heath care, education and other public services.

Apart from the adjustment of public investment structure, the Government issued in 1990s many legal documents to regulate and enhance the efficiency of public investment, e.g. the Decree 385/HDBT dated 7/11/1990 of the Ministerial Council issuing the Regulations on Investment and basic construction administration which has been updated by the Decree 177/CP; the Decree 92/CP in 1998 of the Government regulating in detail the process of implementing and managing basic constructions funded by state budget and other public funds; the Decree 52/1999/ND-CP date 08/07/1999 of the Government on the issuance of the Regulations on Investment and basic construction administration which replaced the Decree 42/CP is one important advance step to renovate the investment and construction regime towards removing institutional and administrative obstacles to investment and business activities of enterprises.

There are two main points in the Decree 52/CP as follows:

Renovating the regulatory regime on investment: each source of capital is managed by a distinctive mechanism, e.g. for state budget investment, the Government regulates comprehensively from the preparation of project, exercise of investment to the operation. For preferential state credit or other credit sources guaranteed by the Government, enterprises can take the lead in carrying out their investment but remained under the control of credit organizations to ensure their credibility. In this case, the Government intervenes in the phrase of making decision on investment, including the approval of the overall budget for investment, planning, architecture, standards, land and environment.

Extending the rights to enterprises, organizations and individuals in order to encourage them engage in investment and in parallel, enhancing the Government's regulation on investment on the basis of legal documents.

3. Difficulties occurred from policies applied to public investment

Corruption and waste in public investment is a phenomenon prevailed in the 1990s. Since legal and regulatory mechanisms are not sufficient and clearly shaped in the transitional period, they are open for corruption and waste by a large part of government officials who rely on their mandate to make decision on every stage of investment, from the adoption of project's proposal till the implementation of the project. From 1993, Viet Nam started to put public investment projects to auction. However, in most cases, decision is implicitly made beforehand by the Board of auction, so the efficiency of auction is in fact relatively low.

Investment policy, which is still weak in many aspects leads to inefficiency. Many projects, even large projects, have not been carried out in accordance with procedures stipulated by laws, especially in the period of implementing the Decree 385/HDBT. Criteria for clearing off public investment funds are not uniform and recording documents (receipts) are arbitrarily used. Therefore many fault-recording documents have been made to draw public investment fund.

The spread and leveling of investment capital has been an emerging problem. The implementation of project is relatively slow and the procedures of approving projects, auction and disbursement are very complicated and time consuming. The quality of some public investment projects is still very low because project-designers do not pay attention to the efficiency of projects funded by Government budget. Those projects are therefore subject to many adjustments and amendments, even in the stage of implementation, which cause a large waste and prolong the duration of projects.

In recent years, public investment plans are carried out very slowly and not in time. There is often the phenomenon that " money has to wait for projects" which is totally converse to previous fact that projects were approved but no fund available for disbursement. There are some causes of this phenomenon. Firstly, the assignment of investment plans from budget funds to Ministries and provinces is very slow so those funds can not be transferred. Secondly, while ministries, agencies and provinces are still looking for effective projects, banks themselves are also bewildered to work out credit services consistent with current complicated policy and mechanism. Thirdly, the allocation of investment funds at ministries, agencies and provinces does not match the list of projects indicated by the Ministry of Planning and Investment, therefore banks and the Ministry of Finance are not able to disburse funds.

4. Recommendation on public investment policy in Viet Nam

(1) Investment should not be scattered around but concentrated to key projects so that they can be promptly brought into practice and help enhance the economic efficiency. Once investment budget funds are allocated to ministries, agencies and provinces, a council, which compose of qualified and wise experts should be established to examine and select the most necessary projects on the basis of close scoring and voting.

(2) Prioritizing public investment funds to projects on infrastructure, agriculture, industries associated to agriculture, health care, education and human resources development.

(3) Promptly amending, completing and improving laws decrees, circulars related to the use and administration of public investment funds so that investment can be carried out in the most rapid manner. Main points for immediate actions include among others: improving the process and procedures of formulating, examining, approving, auctioning and disbursing public investment projects; Binding public investment projects to follow strictly decrees and circulars of the government and other competent ministries.

(4) Strengthening the supervision and control toward Government agencies in charge of the implementation and administration of public investment projects in order to prevent corruption, waste and impediments in the course of implementing projects.

B. Investment situation and policy in state enterprises

1. General trend of investment in SOEs

(1) Investment from self-capital of SOEs has not regularly grew: its growth rates were respectively 60%, 119.3%, 81.3% and 46.3% in 1991, 1993, 1994 and 1997 but dramatically dropped in the consecutive years, i.e. minus 46.7% in 1992, -9.7% in 1995 and 15.6% in 1998.

(2) Generally, the growth rate of investment from self-capital of SOEs has been slowly decreased. The average growth rate was 25.2% in 1991-1995 whereas it was only 21.3% in 1996-2000. There are 2 periods where the growth rate decreased: the first period was from 1994 after a peak growth in 1993 (119.3%) and the second period was from 1998 because of the Asian financial crisis.

(3) Despite of unstable growth, the share of self-capital investment of SOEs in the total social investment has a tendency of increase in the period 1996-2000 after an unstable change in 1991-19995. This

share mounted up from 13.8% in 1995 to 18% in 2000.

(4) Investment of SOEs, classified by sectors has been oriented to intensive investment and renewal of equipment with a view to enhancing products' quality so that the productive capacity increases rapidly with a large number of products satisfying export standards or import substitution.

(5) However, "instant noodle investment" and "short-term investment" are still prevailed in SOEs during 1990s: since enterprises do not have confidence in the stability of Government policy and mechanism, they invest a large amount of money but intend to draw it quickly, leading to a high proportion of deprecation cost and profit in the price of product and thus making product less competitive and can not be sold in the market.

(6) In the context of hard competition, low demand for economic growth, high valuation of Viet Nam dong, tough competition from imports, SOEs are advocated to invest in capital intensive sectors, protected sectors and industries producing goods for export within preferential quotas.

2. Evolution of investment policy vis-à-vis SOEs

Since 1991, reforms in SOEs sector have been taking place very slowly even though this sector has been chronically in difficulty. In the regulatory reform process, the reorganization of SOEs and national corporations gives a strong effect to the investment of those enterprises.

(1) Reorganization of SOEs: from 1989, in implementing the decrees 315/HDBT and 388/HDBT, the Instruction 500/TTg and Decision 90/TTg, the number of SOEs decreased from 12000 in 1990 to 5340 in 8/2000. By reducing the number of enterprises, the seize of enterprises' self-capital and budget funds allocated to them have increased. Enterprises have more capital to modernize their machinery and equipment and to produce product of good quality. As a result, enterprises' profits are in a rise and they in turn help increase the self-capital of enterprises.

(2) Establishing national corporations: In implementing the Decisions 90/TTg and 91/TTg dated 7/3/1994 of the Prime Minister, there are currently 18 national corporations functioning under the Decree 91 (so called 91 national corporations, administered by the Government) and 74 national corporations functioning under the Decree 90 (administered by relevant Ministries). Even though the mechanism and policy applied in the establishment of national corporations are still exposed to much inefficiency, they have contributed considerably to profit- making of those enterprises. The reason is that because of those mechanism and policy, national corporations became lawful monopoly enterprises, especially in terms of price setting, import-export, controlling the quantity of goods circulated in the market etc. Thanks to high profit making, SOEs in national corporations have increased considerably their investment.

(3) Changes in laws and regulations during the last 10 years have been directed to enhancing the autonomy in investment of SOEs. The Law on SOEs issued in 5/1994 allowing SOEs to diversify

their activities in many sectors. The Law on enterprises being in effective from 1/2000 removed 145 types of licenses respectively in 2/2000 and 8/2000 and facilitates business activities. The Decree 52 issued in 1999 regarding regulations on investment and construction allows SOEs the right to decide on their own investment projects funded by their self-capital and loans without Government's guarantee (except projects in Group A). Furthermore, SOEs can autonomously take the lead in all stages of investment on the basis of observing existing policies and regimes of the Government.

3. Problems and difficulties occurred by investment policy on SOEs

(1) Mechanism and policy related to financial and monetary markets are not uniform. Taxation policy is not equally imposed between sectors and businesses and oriented to protection and increased budget revenue. Tax and tariff rates are frequently changed, which put investors in a passive position. Pricing policy is also exposed to some inappropriateness, leading in one hand to price volatile and on the other hand to the monopoly of some enterprises. As a result, they set very high prices which thus affects the demands of public and in turn affect the investment of enterprises.

(2) The functioning of commercial banks is still weak. Because of low expertise and moral degeneration of some banking staff, loans are often non-refundable. Financial situation of some commercial banks became more and more difficult during the 1990s. As a result, in the last 2 years, the Government has to strengthen the banking system, which implies some difficulties for investment of SOEs.

(3) The process of streamlining SOEs has been considerably progressive in the 1990 but there are still many difficulties. The number of SOEs is still too many, the model of national corporate is facing many problems and the process of equitation is too slow. The most threading thing is the low efficiency and weak competitiveness of SOEs when they are coping with tough competitions from foreign capital investment enterprises and imported goods.

4. Policy proposals to enhance and improve the quality of investment in SOEs sector

(1) Accelerating SOEs reforms towards putting them in leveled playing field with other economic components and foreign enterprises. Equitising as soon as possible enterprises the Government does not need to hold 100 shares; giving autonomy, sale, leasing, merging, disbanding or dissolving most of loss making SOEs, except public benefit enterprises.

(2) Cresting incentives to SOEs to investment intensively and renew their equipment and technology, enhance management skills of SOEs and using up existing capacity. It is not necessary to have mass investment as it was in the last few years.

(3) Creating favorable policy to exporting enterprises which have enlarged their markets and promised great potential. Similar preferences can be provided in projects of constructing and upgrading transportation infrastructure, irrigation system, electricity networks, shrimp cultivation, multi year

crops, fruit trees, forestry and agro-forestry and aqua products processing.

(4) Encouraging banks to increase their loans to projects of SMEs, light industry and labor intensive enterprises because those projects and enterprises are more effective than projects and enterprises of large size.

(5) In the administrative work, the Government should have determining and sanctioning instructions vis-à-vis officers at Ministries, agencies and provinces who do not follow strictly legislation, especially the Law on Enterprises and Law on SOEs and try to maintain regulations for their own benefits. Enhancing the struggle against corruption and professional degeneration of baking staff.

C. Investment situation and policy in private sector

1. General trend of investment from household and private sector

(1) The growth rate of household and private sector's investment which was very low in the last 10 years did not keep up with the potential of this sector and opportunities brought about by market mechanisms and international integration process. While its growth rate were respectively 20.5% and 42% in 1991 and 1992, its average growth rate was only 9.4% for the next three years, and minus in the following 4 years (1996-1999), even dropped down to minus 10% in 1998.

(2) As the annual growth rate was low, even minus in many years consecutive, the share of household and private sector's investment in the total social investment reduced considerably and continuously during the 9 years of reforms: it fell from 43.4% on 1991 to 20.1% in 1999, then go up to 24.2% in 2000 thanks to the application of the Law on Enterprises.

(3) About 90% of investment of private sector was at first from its self-capital. However, during the 1990s, the proportion of banking loans and other unphysical loaning markets in this investment tends to increase.

(4) The structure of investment in agriculture and rural industries has been adjusted towards increasing the ratio of investment in small and medium production, exploiting competitive advantages such as natural resources and abundant labor forces to produce products that SOEs and foreign invested enterprises do not want the engage because of small market.

2. Evolution of policies regarding household's investment

(1) <u>Main policies to mobilize capital for agriculture development</u>

It can be said that the most dramatic reform of the economic renovation process of Viet Nam has taken place in agriculture sector and stemmed from this sector. Because of the implementation of many policies advocated to the liberalization of agriculture during the 1980s, Viet Nam became a crop exporting country from 1989. Resolutions of the Communist Parties, especially the Resolution 2 and 6 of the VII Section have provided more favorable conditions of agriculture productions, e.g. removing multi-prices mechanism in cooperatives, applying a market-based price system, creating an unified market for agriculture capital goods, enhancing the application of science and advanced technology n agriculture, developing agriculture service etc. The National Assembly also issued many pieces of legislation on taxation related to agriculture production such as the Law on Agriculture, the Law on import-export tariffs, Land use tax, Tax on Natural resources etc. This taxation system, which is formulated in a manner to be ready comprehensible and applicable to peasants, clarify the sums of taxes that peasants have to contribute to the Government, helping prevent the corruption and abuse of power by different levels of authorities.

Furthermore, in the 1990s, the Government adopted many types of supporting policies in favor of agriculture sector and rural areas, such as increasing pubic investment to upgrade rural infrastructure, provide investment credit to SOEs as a support to agriculture production, liberalizing domestic rice market, allowing private sector to compete in getting rice export quotas and move gradually to open up the export of rice from 2000. Discrimination between agriculture and other sector has been reduced. As a result, private investment in agriculture and rural areas tend to increase.

(2) Main policy to mobilize capital for developing non-agriculture private sector:

Since the VI Party's Congress in 12/1986, non-agriculture private sector has been recognized as an economic component and allowed to compete in a leveled field with state economic sector. In 4/1992, the National Assembly passes new Constitution, which acknowledges private ownership of property and capital goods. The confiscation of private property has been prohibited. In 1/1991, the National Assembly passed the law in private company, which allowed private sector to engage in most of economic activities. In 6/1993, the National Assembly amended the Law on foreign investment in Viet Nam, allowing Vietnamese private enterprises to create joint venture with foreign enterprises. The Law in encouraging domestic investment has also been adopted in 1994. Those policies have been obviously giving positive effects to the investment of non-agriculture private sector.

However from 1994, 1995 till end of 1999, many difficulties occurred in the private sector that regulatory policies were not adjusted in time to response to. For example, private enterprises which were already of small size and limited capital, once developing to a stagnant point had been lacking of capital, land and physical infrastructure to modernize their production and meet high product's quality requirements; the intention of strengthening the economic role of the Government and establishing national corporations; and a rapid increase of corruption, and red tape of state administration vis-a-vis private enterprises.

In 1/2000, the Law on Enterprises officially replaced the existing Law on Company and Private Enterprises formulated in 1990, that creates more favorable conditions to private sector. The most strength of the Law on Enterprises is that it eliminates inequality among investors in establishing new business, simplify formalities for new business establishment and reinforce the responsibility of investors through the mechanism of "registration and verification". The process of business registration was simplified and shortened.

3. Remaining difficulties in the application of policies and mechanism for private investment

Despite a lot of improvements in policies and mechanism for capital mobilization from the private sector, private investors have been facing difficulties regarding environment for production and trade, import and export activities, credit terms, market information and transparency. Difficulties facing the agricultural sector as well as the non-agriculture private sector are normally related to legal framework, land use rights, incentives for investment in unfavorable areas, direct access to foreign market for inputs and outputs.

Generally, the major reason that limits the mobilization of capital from rural population for economic development can be reflected in 2 ways. Firstly, the financial system is not strong enough; investment environment is not attractive or transparent; the banking system is not well developed; the organization of capital mobilization and lending is not diversified enough to meet different requirements of depositors; bank credit reserved for agriculture is limited while credit terms are not favorable for farmers. At the same time, infrastructure for agriculture and rural development is under bad conditions.

Non-agriculture private sector faces the same difficulties as in the case of agriculture and rural development. The worrying situation of investment in this sector is also attributed to the fact that business environment is unstable and government's policies are not yet supportive or encouraging to this sector. There is an idea that the Government has not realized the importance of this sector to future development of the national economy.

During 1990s, the Government issued a great number of laws. However, the promulgation of Decrees and Circulars providing guidelines on the implementation of these laws has been slow and not synchronous; the last Circular may be promulgated at the same time when the revision of law is taking place. Therefore, private investors do not believe in the stability of the legal system. Each time, they only invest a small amount of capital and withdraw their investment if it is not rewarding. On the other hand, existing policies are not equal to different economic sectors, and private investors are the victims of this unfair mechanism.

4. Recommendations on policies and mechanism governing the mobilization of capital from private sector and from the community

(1) *accelerate the development of the financial system, including direct finance from long term securities markets and indirect finance through banks and credit organizations.* At the same time, introduce more policies and mechanism that better meet people's need and aspiration in order to make the best use of this capital source for the development objective;

(2) introduce more effective policies in order to gain people's belief in the government's policy of developing a multi-sector economy, diversifying the forms of ownership, and creating a fair environment for trade; eliminate discriminative policies toward private sector and household businesses; eliminate monopoly to ensure free and fair competition among different kinds of businesses. It is necessary to minimize procedures relating to the registration of businesses, and conduct a number of reforms to make it more favorable for businesses in terms of credits, prices and taxes, while furthering combat against corruption and bureaucracy;

(3) *the government need to introduce policies to stabilize and and improve people's income.* These policies include developing rural infrastructure, imposing low taxes and removing some taxes imposed on farmers, reducing taxes imposed on industries which support agriculture and rural development, and other policies to help farmers find an outlet for their products, i.e marketing, soft loan for farmers in case they have to store their products when prices decrease...

D. Foreign direct investment, situation and policies

1. Outstanding trends in FDI

(1) *Foreign direct investment tends to increase in the period from 1987-1988, when the Law on Foreign Direct Investment was adopted, until 1995-1996, but then fell sharply since 1996 in terms of both number and value of projects.* The number of projects kept increasing from 153 in 1991 to 412 in 1995, with total registered capital increased from USD 1294 million in 1991 to USD 8640 million in 1996. However, the situation has reversed since 1996. By 2000, foreign direct investment in Viet Nam has come back to 1990 level.

(2) *The proportion of foreign direct investment in the total investment of the whole society increased rapidly in the period 1991-1995 and decreased in the period 1996-2000.* The figure, estimated at 14.7% in 1990, increased to 32.7% in 1995 and then fell steeply to only 15.9 % in 2000.

(3) *The structure of foreign direct investment has been changing in a positive way, with higher priority shifted from the production of non-tradable goods to the production of tradable goods*, thereby positively contribute to economic growth.

(4) *A common tendency in recent years is that the proportion of foreign capital invested in industrial zones, export and processing zones, business cooperation contract, and BOT projects has increased* while capital proportion and the number of projects licensed by the Ministry of Planning and Investment and Provincial Authorities has decreased very fast.

In addition to some common and positive trends as mentioned above, there have also been some irrational tendencies relating foreign investment, which limit its socio-economic effects:

(1) *Foreign investment has only been focused in areas with favorable conditions or industries which*

show quick return on investment. As a result, there is a lack of capital in areas Viet Nam needs to develop (such as agricultural processing, aqua-agriculture, manufacturing...) or in areas that face the problem of unemployment;

(2) *The tendency of diversifying sources of investment take slow effects while the proportion of investment from ASEAN countries has been increasing*. Depending heavily on investment from ASEAN and Asia, the improvement of technology and management skills takes place at slow pace, and furthermore, investment flow will go down as soon as these countries suffer from crisis;

(3) *In recent years, the proportion of small-scale projects and 100% foreign invested projects has been increasing*, while the proportion of joint venture projects and business cooperation contracts decreasing. The contributed capital of the Vietnamese side tends to be lower in proportion, just around 20% in stead of 30% as before, and mainly in the form of land use rights;

(4) *Despite some positive improvement regarding investment structure, the proportion of investment in industial production and estates trading still outweigh that in agriculture and infrastructure*. By 1998, industry accounts for 37.6 %, oil and gas 20.4%, estate 17.8%, while agriculture 6.1 % and telecommunications only 4.5 %.

2. Improvements of policies and mechanism with regard to foreign direct investment in Viet Nam

(1) Law on Foreign Investment dated 12/1987:

The National Assembly adopted the Law on Foreign Investment in December 1987 in order to create a legal environment for foreign investment in Viet Nam. However, this first version had many drawbacks, and had to be revised in 1990. This was because the law was issued in the background that Viet Nam began its renovation process, the centrally planned economy principles was still applied, and a law governing the development of market economy was not yet in place;

(2) Revised Law on Foreign Investment 1990

In June 1990, the National Assembly of Viet Nam adopted the Law on the amendment of and supplement to the Law on Foreign Investment 1987. These amendments and supplements include: (1) definition of the roles and responsibilities of the Vietnamese side, (2) more detailed definition of business cooperation contracts, (3) more detailed definition of joint ventures (4) regulations on business cooperation between Vietnamese private enterprises and their foreign partners. They also provide more concrete definitions and regulations on joint ventures.

(3) Revised Law on Foreign Investment 1992:

The National Assembly of Viet Nam revised the Law on Foreign Investment for the second time in December 1992. The amendments and supplements cover the following matters: definition of Vietnamese side consisting of 1 or more businesses of different economic sectors, establishment of export processing zones (EPZ) and business activities in EPZ, regulations on BOT contracts. In comparison with the first revision, the revised law 1992 is more concrete and focusing in some definitions. Particularly, it also provides regulations on new types of attracting and contributing investment capital.

Since 1992, along the course of revising and completing laws and other documents regarding foreign investment in Viet Nam, regulations on the repatriation of investment capital or profits tends to be increasingly strict and complicated. As a result, worries have been raised among investors since 1995-1996, and the number of projects approved went down considerably at the end of 1996.

(4) Law on Foreign Investment November 1996

On 12th November 1996, the National Assembly adopted the new Law on Foreign Investment by basically amending and supplementing the Law on Foreign Investment 1987 and its two revisions in 1990 and 1992. In addition, the National Assembly has also revised and adopted many important laws such as Commercial Law, Company Law, Law on Private Companies...

New contents of the 1996 Law include: concrete regulations on the areas and fields where foreign investment is encouraged; areas and fields where foreign investment is restricted; new regulations on the reduction and exemption of profit tax, for example, profit tax can be exempted for at most 4-8 years; exemption of import duties on machinery and transport vehicles specified for investment projects; reduction and exemption of rents on land, water and sea area used in investment projects under the form of BOT, BTO, BT; investment projects in moutainous, remote and hard-up areas; regulations on diversification of investment forms; legalization of industrial zones; regulations on the use of Vietnamese currency by the foreign parties; limitting the use of concensus voting in making decisions through the Board of Management; reducing the time for evaluating and licensing to 60 days...

(5) Revised Law on Foreign Investment 2000

In the condition that investment flows have seen continued reduction in recent years, the National Assembly of Viet Nam has revised the Law on Foreign Investment version 1996. The Government also issued a Decree dated 31st July 2000, providing detailed regulations on the implementation of this Law. However, there have not been any further guiding Circulars since then. Thus, investors are still not much interested in investing in Viet Nam. Their traditional worry is that Law is fairly open and clear, while sub-laws try to limit incentives and make it difficult to implement the Law.

3. Difficulties and drawbacks in policies and mechanism governing foreign direct investment in Viet Nam

(1) *Planning for the development of FDI sector is slow and less concrete, which leads to many difficulties in evaluating projects, and poor quality of projects.* Due to the fact that a master plan for each region and area is not yet in place, and that the exploration steps do not have enough reliability, many projects including those for building restaurants and hotels, producing freshwater, audio visual products,

assembling car and motorbike, washing powder..., have been licensed improperly, which lead to excessive supply in the overall economy. Investment incentives have not yet been institutionalized to attract foreign investors to such areas as agriculture, forestry, fishery, and infrastructure development in many big cities or in concentrated industrial zones. Although joint ventures have been more facilitated, accounting for 50 % of the project number and 60% of the registered capital, this sector has the highest number of loss-making and bankrupt businesses. Part of the reason is that the existing mechanism does not stimulate the participation of non-state enterprises in joint ventures.

(2) *Policies and legal system are not synchronous, stable, and transparent.* Many changes not only disadvantage investors, but also reverse and cause damage to their business. Many legal documents are not issued in time. Some guideline documents issued by ministries, branches and local authorities tend to tighten and restrict the development of foreign investment. Most of the related documents have unclear articles...

(3) *High level of government intervention in the operation of foreign investors*: There is too much overlapping inspection and examination by different Government agencies, causing a lot of troubles for business activities. The criminalization of economic relations tends to increase. A policy to improve Vietnamese staff working in foreign investment projects is not yet in place. Corruption is becoming popular at different levels, causing delays for many foreign invested projects.

4. Recommendation on policies and mechanism in order to further attract foreign investment

(1) *Maintain the balance between maintaining government intervention in the overall economy and foreign invested sector, and creating a more favorable and attractive environment for foreign investors.* To this end, we need to identify some areas of priority in which foreign investors should be encouraged. These include some areas of higher comparative advantage in order to promote export, or areas involved high level of technology. In particular, we should give higher incentives for areas and industries that have high demand for foreign investment;

(2) *Revise the existing legal documents in order to reduce difficulties facing investors.* This can be achieved by: ensuring an attractive and transparent legal environment together with incentives of higher level than those applied to domestic investors; reducing costs and unifying prices for both domestic and foreign investors; reviewing costs of land use rights, cost and compensation for the demolition of people and the clearance of land; introducing reforms in the areas of finance, credit, and exchange with a view to equalizing foreign investors with domestic ones;

(3) Diversify forms of foreign investment, allowing foreign investors to change from one form to another; helping foreign investors when they are in difficulties by granting loans, thereby increasing the capital contribution of the Vietnamese side; encouraging private sector to take part in joint ventures with foreign partners.

Part 2 The effectiveness of investment capital

A. Impact of policy and mechanism on the effective allocation of scare resources

1. Impact of policy and mechanism on the allocation of investment capital in early 1990s

In late 1980s and early 1990s, economic liberalization and the open door policy created a milestone in the national ideology: multi-sector economy is adopted in the reality, and the motive to enrich oneself is stimulated in all social groups. Investment policies are greatly eased to allow the participation of all economic components. Capital mobilized for investment in early 1990s has grown rapidly with increasingly higher effectiveness.

The liberalized economic mechanism in all industries, together with the devaluation of the Vietnamese currency in 1988-1992, is a decisive factor to the comprehensive reallocation of all development resources, including investment capital. In fact, thanks to the new economic mechanism, which includes the removal of obstacles to investment as mentioned above, exports and other industries—both labor intensive and capital saving—have made increased profits. This encourages investors to move their capital to agriculture, light industry which are labor intensive and export-oriented, and particularly small scale industry and handicraft, instead of heavy industry as the case was in 1985-1987.

During this time, there were unprecedented incidences after the unification of our country in 1975. Laborers moved from cities to the countryside to take part in agriculture production. Capital flows were transferred from heavy to light industries, from the state to non-state industries, especially to those industries that support agriculture, service industry and consumer good production. Thus, investment was restructured, and scarce resources such as capital, land, labor, material were reallocated among different economic sectors and among secondary industries in each sector in a way that could improve the effectiveness of trade, production, and of investment capital.

The ICOR index with the deviation of 1 year has decreased from above 3 (in 1986-1089) to less than 3 in 1990, 2.4 in 1991, 1.76 in 1992, and 2.2 in 1993. Therefore, it can be assured that economic and investment policies in late 1980s and early 1990s, has brought good results for the allocation of investment capital.

Despite the fact that exact statistics on investment by different economic components in different areas are not available, the overview of the national economy shows that investment structure in early 1990s was relatively rational. In 1990-1991, the average proportion of investment capital reserved for agriculture production (particularly for export) was up to 16.4%, while only 42.4% for service and 41.2 % for industrial production.

Table 1 Investment capital structure (%)

Industries	1990	1991	1992	1993	1994	1995	1996	1997
Industrial production and construction	38.4	44.0	48.9	55.3	39.0	33.0	41.1	31.5
Agriculture, forestry and fishery	17.1	15.7	12.7	8.9	9.4	12.0	8.5	15.4
Service and social infrastructure	44.5	40.3	38.4	35.8	51.6	55.0	50.4	53.1

Source: Ministry of Planning and Investment

2. Impact of policy and mechanism on the allocation of investment capital in the period from 1993-1994

In this period, economic policies and mechanism became less responsive to the development of the production force than the case had been in 1992-1993. In some areas, such as encouragement of foreign direct investment or private investment, policies and mechanism even became more tightening. On the other hand, a great deal of foreign exchange was poured into Viet Nam: more income from oil, the lifting of US financial embargo against Viet Nam, the sharp increase in investment capital from FDI and from Vietnamese overseas, the return of international financial aid.

These sources of foreign capital made an important contribution to higher domestic saving and investment, fostering the economic growth in 1990-1995. However, excessive foreign capital led to the revaluation of Vietnamese currency, greatly reducing comparative advantage of sectors that produce internationally commercialized goods (tradable goods sector). The negative effect of this economic and investment mechanism was that both domestic and foreign investors did not dare to put their money to vital industries, high-tech industries, or capital intensive industries. Instead, they turned to invest in the production of goods that could only be domestically rather than internationally. Examples can be found in those areas as estate trading, sales, restaurant service and tourism... In 1996-1997, when those areas faced lower demand, investors again turned their money to industries or products still protected by the State. This process resulted in sharp increase in prices of land and other estates, labor, service, pushing up production cost.

Thus, investment and economic policies and mechanism after 1994 helped accelerate the process of automatic reallocation of resources in a less effective way. Ineffective use of investment capital was reflected not only at the national economy's level, but also at industry and product levels. At the national economy's level, our ICOR increased greatly in 1990s, from only 1.76 in 1992 to 5.3 in 1998, fastest growth in Asia. At industry level, the proportion of investment in agriculture fell deeply after 1991 while this industry had lowest ICOR and employed the most labors.

At product level, on the one hand, irrational regulation and policy distortion led to excessive supply and low economic efficiency. On the other hand, this inefficiency was partly due to misleading decision in choosing key industries irrelevant to the present development level of the economy. Investment was concentrated on purchasing machines and equipment assembled in other countries, and on building up factories and workshops, which led to high production cost and inward development of the economy.

Effects of investment related policies in 1993-1994 period can be rephrased as 3 dangerous tendencies: increasing exhaustion of domestic capital sources due to the imbalance and ineffectiveness of investment structure, and slow improvement of people's income (even decreased income and poorer life for people in rural areas); the recurrence of subsidized credit funds through .... whereby all industries and branches, including private and foreign invested enterprises expect preferential capital from the Government; and lastly, foreign direct investment has seen continuous decreases every year since 1996.

3. Conclusion on the impact of policy and mechanism on investment capital allocation in 1990s

The fact was that Viet Nam saw relatively high growth rates in 1990s and that huge development of investment capital was the most important factor to this achievement. However, it can be concluded that policies and mechanism in this period lessened the effectiveness of capital allocation as they turned investors to industries that met domestic demand or industries that were still under the protection of the State and reduced the competitiveness of the overall economy.

B. The role of capital mobilization through Viet Nam Postal Savings Fund

1. The objective of mobilizing capital through Postal Savings Fund

(1) The objective of postal savings service

Based on the need to thoroughly utilize all domestic sources for socio-economic development, the Government issued Decision 215/1998/QD-TTg dated 20/5/1998 allowing the General Corporation of Postal and Telecomminication to provide the postal savings service. In May 1999, the General Department of Postal and Telecomminication decided to establish a Postal Savings Fund.

The reality shows that Vietnamese people are hardworking and thrifty, but receive low income, and as a result, rarely keep their money as savings accounts in banks. Moreover, the banking network is not widespread, especially in mountainous, rural and remote areas. Forms of mobilizing capital are not diversified, and not suitable for low-income population. The mobilization of capital through the State Treasury is still limited and not on a regular basis.

However, the majority of households keep their money, from several hundred thousands to several millions VND, in their pockets. With a mobilization system convenient, flexible and suitable to the urgent need of people, these small sums of money can be utilized for the national economic development. This is the basis for the formulation of postal savings fund system. In the first 2-3 years, the post and telecommunication industry can make use of over 500 post offices to mobilize capital, more effectively than any banks. In the future, it can also extend its service to other post offices in the total of 2760 existing post offices all over the country.

The major objective of postal savings service is to attract and mobilize idle funds in all social groups to be contributed to the state budget for investing in infrastructure and some key national economic projects, in accordance with the Government's guidelines and Law on Domestic Investment Encouragement. Another objective is to motivate the saving movement in the society, in order to stabilize people's income and lives, while making better use of the post and telecommunication system.

As decided by the Prime Minister, all capital sources mobilized through the postal savings system will be kept in forms of term savings or demand savings. Presently, the postal savings service includes 2 categories for Vietnamese currency: term savings (3 months, 6 months, 12 months) and installment savings (6 months, 12 months, 18 months and 24 months).

(2) State management mechanism for postal savings funds

- The Ministry of Finance is responsible for instructing, supervising and examining the whole process: transferring, receiving, using and refunding between the General Corporation of Postal and Telecommunication and the Development Assistant Fund. The Ministry of Finance will: decide the interest rate that the Development Assistant Fund has to pay to General Corporation of Postal and Telecommunication for using funds; consider the guarantee rate for regular refunding; instruct, supervise and examine the implementation of accounting regulations provided for postal savings service; act as the State administration authority in financial issues for the postal savings service provided by the General Corporation of Postal and Telecommunication;
- The Ministry of Finance shall cooperate with the Ministry of Planning and Investment to work out and submit to the Government the yearly plan for postal savings fund mobilized by the General Corporation of Postal and Telecommunication. The State Bank of Viet Nam is responsible for supervising and controlling interest rate, the transfer of money, safeguarding the postal savings storage system.
- The General Department of Post and Telecommunication shall carry out the role of state management for postal savings service by issuing service providing licenses, setting up rules, regulations, and service standards. The General Corporation of Postal and Telecommunication is responsible for organizing the provision of postal savings service and ensuring that mobilized capital is properly transferred to the Development Assistant Fund.

2. Mechanism and policies to make effective use of capital mobilized through Postal Savings Fund

The mechanism of using mobilized capital: the General Corporation of Postal and Telecommunication retains part of the mobilized capital for regular repayment (the maximum proportion is 20% of the planned mobilized capital). The rest is transferred to Development Assistant Fund, which in turn extends loans to investment projects in accordance with the orientation of the Government and of the Law on Encouragement of Domestic Investment. The fact indicates that this mechanism has been applied flexibly in that the Postal Savings Fund usually retains only enough cash for repayment purpose.

Interest rate: Interest rate for postal savings is decided by the General Corporation of Postal and Telecommunication based on the average of the interest rate existing on the market, provided that the planned mobilized fund is ensured.

Interest rate at which the Development Assistant Fund has to pay for using mobilized capital is decided by the Ministry of Finance based on the State Treasury Bills of the same term. Ministry of Finance on the last day of every quarter (3 months) pays the General Corporation of Postal and Telecommunication the interest calculated on the net capital transferred to the Ministry of Finance.

Mechanism for transferring and refunding of mobilized capital: On the 10th or 25th of every month, based on the planned amount, the Development Assistant Fund receives the mobilized capital from the General Corporation of Postal and Telecommunication on terms of 1 year, 2 years, 3 years and 5 years. To ensure the security of the whole postal savings system, the Ministry of Finance, the State Bank of Viet Nam, and the General Corporation of Postal and Telecommunication shall cooperate in supervising its operation.

From the beginning of its operation, May 1999, through August 2000, the Postal Savings Fund has mobilized VND 2211 million, of which VND 1315 million has been transferred to Development Assistant Fund. This Fund has been operating more and more effectively. However, it is currently difficult to evaluate how efficiently the mobilized capital has been used at the Development Assistant Fund. This is due to a number of reasons, particularly the following:

The Postal Savings Fund has only been in operation for 1 year; the mobilized capital is too small to evaluate its social and economic effects.

Furthermore, this small sum (estimated at VND 1200 million) will be transferred to the Development Assistant Fund and add to its own capital of VND 7000 million, which will be put to different purposes without separating mobilized capital and State Budget's fund. It is therefore difficult to evaluate the mobilized capital alone.

The Development Assistant Fund itself only started its operation at the beginning of 2000. Presently, it is carrying out feasibility study and some trial projects. As a result, it is difficult to evaluate the Fund's operation.

However, from what the Postal Savings Fund has achieved, it can be asserted that this Fund is necessary and that its mobilized capital has made its contribution to the Government investment and to the implementation of Government's guidelines on pushing up the demand. Hereby, we will discuss on the effectiveness of this policy and mechanism.

C. Evaluation of public investment policies and mechanism

Two major objectives of public investment are to develop infrastructure and to formulate a number of state-owned enterprises. To evaluate the effects of public investment policies and mechanism, it is impossible not to mention its important role to the national economy. The importance and constructive effects of public investment in Viet Nam can be reflected by the following two points:

(1) *Public investment is the most important for long-term development.* To achieve fast and stable development, and to carry out long-term industrialization projects, it is clearly important to invest in infrastructure including roads, ports, energy, post and telecommunication, water-resource system, land reclamation ... These projects require large initial investment, but have low profitability and late return. It is, therefore, impossible for other economic components especially private sector, to invest in these areas because they are neither interested in nor strong enough to take part in these projects. As a result, only state sector, with capital mobilized through the state budget and from foreign assistant sources, can carry out these projects.

The practice in Viet Nam shows that, infrastructure is one of the prime concerns for investors when they choose to invest in any area. Not only foreign investors but domestic investors also keep away from underdeveloped areas. Without investment to develop production and improve income, there will not be enough capital for infrastructure development as well. This vicious circle constitutes the fact that developed areas become increasingly developed while in areas with degraded infrastructure, economic development is more and more difficult and there is a danger of being lagged behind. Over the past years, public investment in our country has been reserved for the development of infrastructure, human resource, health care service and education. Therefore, public investment has played a vital role in creating pre-conditions for the development of other economic sectors.

(2) *Public investment is the prime source of investment for the development of basic industries, capital-intensive industries, or those industries vital to national economic development*

As analyzed above, industries that require large amount of capital but have low return on investment can not be developed without public sources. In fact, the government has mobilized the public investment sources to develop these industries through State-owned enterprises with a view to remove the "bottle-neck" in the economy, facilitating the development of other economic sectors.

Although the excessive intervention of the Government in economic activities may, to some extent, pose negative effects to the development of private sector, public investment has basically been positive and supportive to the development of other economic sectors in Viet Nam, even the foreign invested sector. For example, without investment in water system, electric supply, transportation, post and telecommunication (which goes beyond the ability and interest of private sector), private sector can not have survived nor carried out its business. Without primary industries and capital intensive industries, there would be a shortage of input, semi-products, machinery and equipment for the production of the private sector.

(3) *Public investment in Viet Nam also plays an important part in the development of agriculture sector.* In fact, the stable and fast growth of economic development in 1990s was partly due to State's

public investment in agriculture.

(4) *Public investment plays a pivotal role in the development of public services, health care service, culture, education, science and technology...* It is decisive to enhancing the quality of human resource for long-term development. It is also important for the reallocation of social production force, reducing the gaps between the rich and the poor, removing the difference in the level of development.

(5) *In difficult economic situation, as the case has been since 1977, public investment has accounted for an increasingly higher proportion and motivated other economic components to invest.* In fact, public investment has gradually pushed up the investment demand of other economic components.

There are some worries that the increasing proportion of public investment over the past years may have negative impacts on the growth of private sector's investment by reducing credit supply and raising the cost of capital mobilization by the private sector. However, practical and theoretical experience from many countries around the world has proved that it is not a cause-and-effect relation. The impact of public investment on private sector's investment depends on whether they are supplements to or substitutes for each other. The impact would be positive if they are supplements.

The practice in Viet Nam has proved that public investment has been reserved for developing infrastructure and some primary industries, both of which are necessary for the development of the national economy in general and for private sector in particular. Thus, public investment is supplement to private investment, reducing cost and improving capital efficiency. Generally, growth in public investment is positive to private sector's investment in Viet Nam as well as in other developing countries, especially those countries at the same level of development.

In brief, it can be concluded that the positive effects and importance of public investment, and of public investment mechanism are great to the national economy of Viet Nam. It has been proven that:

Public investment mechanism witnessed a great deal of improvement in 1990s and has become increasingly adaptive to the requirements of the national economy. Public investment mechanism was not in place until 1990 when the Government issued Decree 385/HDBT, the first government legal document regulating the management of investment and primary construction. Since then, a number of legal documents have come into effect. Up to now, Viet Nam has a relatively complete and comprehensive policy and mechanism for the mobilization and management of public investment, which is up to international standards and ensuring the effectiveness of public investment.

Many modern and scientific methods for the management of public investment have been in place to evaluate and select projects with a view to meeting the practical need, while ensuring the socio-economic effects. Public investment structure has been adjusted in a way that socio-economic effects are improved in the long-run and capital efficiency is enhanced through tendering regulations.

Recommendations

It is a visible potential that the domestic capital source will increase following the momentum of economic development. However, the problem of how to mobilize this potential for the course of economic development used to be relatively thorny. Therefore, in the next 5 years, it is necessary to conduct a comprehensive renovation of the mechanism for mobilizing investment capital from all sources. This renovation should be based on increased economic liberalization and reduction of obstacles caused by cumbersome and bureaucratic administration, and conducted in a way that participation of all economic sectors is encouraged. New policy and mechanism should attract capital from all sources, small and large, in order to carry out the industrialization and modernization policy set by the Communist Party.

In addition to full exploitation of capital sources, it is also urgent to renovate the management and personnel structure to improve the capital efficiency. We are making another step towards the knowledge-based economy and globalization. Therefore, efficiency and effectiveness should be top priorities, as well as basis for any development process. This is the biggest demand and challenge for Viet Nam at the threshold of 21st century.

Table 2 Value, structure and growth rates of investment resources

Investment resources	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Total (bill dong. current prices)	6747	11526	19755	34167	43100	68048	79367	96870	96400	103900	124600	147480
Investment from state budget	2237	2246	7045	12558	10300	13575	16544	20570	20700	26000	29700	34280
State credit	300	1060	636	2391	3200	3064	8280	12700	14800	19000	21200	25000
Investment of SOEs	420	1300	574	2418	2000	9409	11070	13300	16100	19000	22300	25000
Investment of private sector	2800	5000	7000	8000	14400	20000	20773	20000	20500	21000	29000	35000
Foreign direct investment	990	1920	4500	8800	13200	22000	22700	30300	24300	18900	22400	28200
Structure %	100	100	100	100	100	100	100	100	100	100	100	100
Investment from state budget	33.16	19.49	35.66	36.75	23.90	19.95	20.84	21.23	21.47	25.02	23.84	23.24
State credit	4.45	9.20	3.22	7.00	7.42	4.50	10.43	13.11	15.35	18.29	17.01	16.95
Investment of SOEs	6.22	11.28	2.91	7.08	4.64	13.83	13.95	13.73	16.70	18.29	17.90	16.95
Investment of private sector	41.50	43.38	35.43	23.41	33.41	29.39	26.17	20.65	21.27	20.21	23.27	23.73
Foreign direct investment	14.67	16.66	22.78	25.76	30.63	32.33	28.60	31.28	25.21	18.19	17.98	19.12
Growth rates. prices of 1995												
Total of investment		25.6	49.8	51.2	9.1	15.7	13.3	12.5	-3.4	1.9	14.8	
Investment from state budget	11.7	11.9	41.6	70.9	-13.8	11.8	31.2	24.8	5.2	18.7	9.35	
State credit		...	-50.0	200.0	21.0	-27.3	116.9	58.8	16.7	21.3	6.8	
Investment of SOEs		60.6	-46.7	119.3	81.3	-9.7	25.1	46.3	15.6	11.6	12.35	
Investment of private sector		20.5	42.0	7.1	17.7	4.6	-1.1	-4.4	-9.8	-3.2	32.2	
Foreign direct investment		-11.1	131.4	116.5	49.7	33.3	14.3	3.8	-23.0	-26.5	13.4	

Source: Ministry of Planning and Investment (MPI)

Table 3 Role of foreign direct investment in total investment

- Realized foreign direct investment (million USD)	214	394	1099	1946	2671	2646	3250	1956	1563	1600
- Exchange rate (VND / USD)	7400	10000	11000	10980	11027	11300	12300	13900	14000	14200
- Total inves. of whole society (mil usd)	1558	1976	3106	3925	6171	7024	7876	6935	7421	8775

Source: Ministry of Planning and Investment (MPI)

Table 4 Foreign direct investment incentives in selected Asian Countries, April 1997

	Viet Nam	China	Thailand	Philippines
Profit tax	10% 15%	15% 20%	20% 25%	20% 25%
Tax holidays	2-4 years	2 years	3-8 years	6-10 years
Import duty exemption	Equipment, raw materials, kits, commodities	Equipment, raw materials, kits, commodities	Equipment, raw materials for construction	All kinds of raw materials

Table 5 Evolution of FDI in Viet Nam (number of projects and millions of USD)

Indicators	88-90	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Number of projects	213	153	195	273	371	412	368	331	275	230	
Registred capital	1582	1294	2036	2652	4071	6616	8640	4654	3897	1567	1600
Legal capital	1272	859	1553	1728	2099	3311	3096	2221	1795		
Contribution of Viet Nam to legal capital	265	212	215	367	551	878	695	321	626		
Number of projects disolved	6	37	48	34	58	56	52	80	95		
Capital value of project disovled	24	293	402	79	217	477	1023	352	2428	564	
Expired projects	2	1	3	3	1	2	3	3	3	1	
Expired capital	0.25	1.00	13.94	15.50	0.13	0.50	74.60	0.82	19.09	1.00	
Number of projects supplemented capital	1	6	10	51	73	122	134	132	133		
Capital value of projects supplemented capital	0.3	7.7	49	222	504	1247	684	1146	875	641	600
Projects in implementation	72	83	142	215	314	362	334	322	275		
Effective investment capital	959	1468	2315	3671	4233	6570	7666	4397	3897		
Disbursed investment capital		214	394	1099	1946	2671	2646	3250	2189	1933	2000
Disbursed legal capital		190	366	845	1297	1606	1489	1373	545	251	
Legal capital disbursed by Viet Nam		46	66	220	271	428	393	288	143	73	
Legal capital disbursed by foreign partners		144	300	625	1026	1178	1096	1085	402	178	
Foreign capital in Viet Nam		168	328	879	1675	2243	2253	2962	2062	1758	1800
Turnover		151	224	485	1023	1852	2583	3851	3910	4600	5500
Budget contribution					128	195	263	315	317	271	260
Exports of foreign invested enterprises		52	112	257	352	440	786	1790	1983	2577	3250
Imports of foreign invested enterprises						1458	2043	3197	2668	3398	4000
Employment in foreign invested enterprises (by thousand people)									270	296	327

Source: Economy and forecast review, MPI, 10-11/2000.

E－2

Changes in Domestic Investment Activities and Appraisal of the Vietnamese Public Investment Plan

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As a consequence of the adoption of the "Doimoi" (reform) policy at the 1986 party convention, the Vietnamese economy set out upon the road to a market economy, while retaining a socialist foundation. This opened the door for foreign direct investment, attracted by such factors as the reform policy and access to a market of almost 80 million people, abundant supplies of diligent, low-wage workers, and the potential of local reserves of natural resources. It has also resulted in the economy taking off, as evidenced in the 8.2% annual growth rate in GDP (target growth rate: 5.5–6.5%) witnessed in the 5th 5-year plan (1991–1995). Based on this success, parliament approved the 6th 5-year plan (1996–2000) in November 1996. As part of the execution of the 6th 5-year plan, the Vietnamese government established the 1996–2000 "Public Investment Program" (PIP) as a tangible indicator of domestic investment. This program was designed with the technical assistance of the World Bank and United Nations Development Programme (UNDP), and was approved by the Prime Minister in June 18, 1996 in the form of Decree No. 2920/QHQT. For expansive details of PIP, the reader is referred to K. Mori, "Study on Economic Development Policy in the Transition Toward a Market-oriented Economy in Viet Nam."

This report focuses on domestic investment, and particularly the Public Investment Program, as these are keys to future economic growth in Viet Nam. In addition to reviewing Viet Nam's economic performance in the 1990s, we draw on all available data in evaluating the forthcoming 7th economic plan and the place of public investment within it. In authoring this report, extensive use was made of Le Viet Duc, Ha Xuan Tu and Le Quoc Ly at MPI, "Overview of Investment Situation and Policy in Viet Nam in the 1990s," one of a series of reports consigned to the Vietnamese government as part of the third phase study on development policy for market economy transition assistance in Viet Nam.

1. Trends in investment activities in Viet Nam

In 1999, the Vietnamese GDP was around the VND 400 trillion (more than JPY 3 trillion) mark, of which consumption made up a sizeable 75% (68% in personal consumption and 7% in government sector consumption), overall investment 27% and net exports a deficit of 2%.

Table 1 Viet Nam: GDP, by expenditure category at current prices, 1993-99

	1993	1994	1995	1996	1997	1998 est.	1999 est.
Consumption	116.7	148.0	187.2	225.2	250.6	283.4	301.7
Investment	34.0	45.4	62.1	76.4	88.7	104.8	109.0
Net exports	-12.2	-16.8	-20.8	-29.8	-25.5	-26.3	- 8.8
GDP	140.0	178.5	228.8	272.0	313.6	361.0	399.9
(% of GDP)							
Consumption	83.3	82.9	81.8	82.8	79.9	78.5	75.4
Investment	24.3	25.5	27.1	28.1	28.3	29.0	27.3
Net exports	-8.8	-9.4	-9.1	-11.0	-8.1	-7.3	-2.2
GDP	100.0	100.0	100.0	100.0	100.0	100.0	100.0

(Source: IMF "Statistical Appendix and Background Notes", and GSO data)

The ratio of total investment to the Vietnamese GDP has been on the rise since 1993, at which point it accounted for 24% of the GDP. This was a key factor in the growth of the Vietnamese economy throughout the 1990s. Table 2 details the make-up of total investment according to procurement source, based on data supplied by the Ministry of Planning and Investment (MPI).

Table 2 Trends and structure of investment in current prices

(Unit: Trillion VND, %)

	1991	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**
Total investment	11.5	19.7	34.1	43.1	68.0	79.3	96.8	96.4	103.9	124.6
By state budget	2.2	7.0	12.5	10.3	13.5	16.5	20.5	20.7	26.0	29.7
By state credit	1.0	0.6	2.3	3.2	3.0	8.2	12.7	14.8	19.0	21.2
By SOEs	1.3	0.5	2.4	2.0	9.4	11.0	13.3	16.1	19.0	22.3
By private sector	5.0	7.0	8.0	14.4	20.0	20.7	20.0	20.5	21.0	29.0
By FDI	1.9	4.5	8.8	13.2	22.0	22.7	30.3	24.3	18.9	22.4
FDI (m USD)	214	394	1,099	1,946	2,671	2,646	3,250	1,956	1,563	1,600
(% of Total)										
State budget	19.5	35.7	36.8	23.9	20.0	20.8	21.2	21.5	25.0	23.8
State credit	9.2	3.2	7.0	7.4	4.5	10.4	13.1	15.3	18.3	17.0
SOEs	11.2	2.9	7.0	4.6	13.8	14.0	13.7	16.7	18.3	17.9
Private sector	43.4	35.4	23.4	33.4	29.4	26.2	20.7	21.3	20.2	23.3
FDI	16.7	22.8	25.8	30.6	32.3	28.6	31.3	25.2	18.2	18.0
Total investment	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

(Source: MPI)

One feature of total investment in Viet Nam is that the relative share of investment attributable to the state budget and state credit rose throughout the 1990s (from 30% in 1991 to 40% in 2000). The increase in investment funded by state credit in the latter half of the 1990s is particularly clear. This statistic underlies the fact that state credit has been used as an instrument to facilitate the policy-based funding of items such as key industries and social infrastructure, within the constraints of fiscal expenditure. From the latter half of the 1980s, the Vietnamese government changed its political tack, reducing capital investment subsidies to state-owned enterprises (SOEs) as part of a move to enhance fiscal accountability. However, the recent rise in state credit gives the distinct impression of assistance to SOEs having being transferred from subsidies to credit from state-owned commercial banks. The soft budget constraint of old would appear to be very much alive, and making its presence felt in the pressing problem of burgeoning debt in the financial structure of state-owned commercial banks furnishing the loans, in the form of non-performing loans. Unlike government subsidies, state loans operate around the principle of target projects being subject to redeemability appraisal prior to project initiation, and banks must learn to abide with this doctrine. Note that "state budget" investment includes all official development assistance (ODA).

Private sector investment comprises self-financing on the part of SOEs, private sector investment (including individual businesses and agriculturalists) and foreign direct investment (FDI). In the mid-1990s, FDI was the main driving force in the private sector, but more recently, SOE self-financing has come to make up the backbone of private investment. This is partly due to FDI falling off from 1998 under the effects of the Asian currency crisis, which has resulted in the relative impact of FDI being diminished. There is a heavy weighting of small-scale regional and agricultural producers within the private sector. The risk associated with such operators due to a general lack of collateral and marketing skills, and also the relative inaccessibility of formal financial services to such concerns, are reasons for the lack of vitality in private sector investment. Additionally, the handling of private sector investment previously placed it at a disadvantage over SOE investment in terms of the loan conditions placed on it. This imbalance in the financial system is being progressively corrected by way of measures such as political decree no. 178 of December 1999 (involving a change in collateral policy).

FDI into Viet Nam is predominantly from within Asia, and centers around ASEAN countries. Since the Asian currency crisis of 1997, however, the stance of investors toward Viet Nam has become increasingly wary. According to an MPI report, investment targeted at export-bound production based around industrial estates and export production zones has increased in recent years, and there has been a drain on efforts to maximize investment efficiency and aim for short-term investment returns. FDI provides a means not simply for the private sector to benefit from funding, but to import advanced foreign hardware and expertise, and also enhance management skills. In this sense, it is in the interests of Viet Nam to improve domestic investment conditions by way of such measures as streamlining investment approval procedures and expanding investment incentives, in order to encourage further FDI.

While limited data makes analysis difficult, a breakdown of investment capital by sector is presented in Table 3, based on data sourced from MPI.

Table 3 Investment capital structure, by sector (%)

	1990	1991	1992	1993	1994	1995	1996	1997
Industry & construction	38.4	44.0	48.9	55.3	39.0	33.0	41.1	31.5
Agriculture, forestry, etc.	17.1	15.7	12.7	8.9	9.4	12.0	8.5	15.4
Service & social infrastructure	44.5	40.3	38.4	35.8	51.6	55.0	50.4	53.1

(Source: MPI)

Throughout the first half of the 1990s, at a time when Viet Nam maintained a high growth rate, investment in industry and construction was dominant. The second half of the 1990s then saw a shift in the investment focus toward the service sector and social infrastructure.

Note:

1. Legal regulation of FDI commenced with the enactment of the Foreign Investment Law in 1987. This was then revised variously in 1990, 1992 and 1996 to enhance transparency and increase investment incentives through such means as promoting particular sectors and offering tax breaks. More recently, the latest revision in June 2000 included such provisions as encouragement of export-promotional investment, although no direct effort has been made to address the issue of investment recoverability.

2. The Vietnamese public investment program and the state of program realization

2-1. The background behind the enactment of the PIP

"An outline and appraisal of Viet Nam's Public Investment Plan", published in Development Assistance Research (Vol. 3/4, 1996) under the direction of the former OECF, details the developmental process of PIP as well as the 1st PIP (1996–2000). The following is based largely on this article.

Prior to the enactment of PIP, there was no medium- or long-term all-encompassing public investment plan, and the State Planning Committee (SPC)—the forerunner of the MPI—was responsible for setting out the public investment plan on an annual basis, as part of the process of planning the budget. The methodology employed in this operated on a year-to-year basis, according to the following procedure:

- The SPC would write a report detailing the key sectors for that fiscal year and distribute it to all ministries.
- All ministries would use that report to make up a list of investment projects for that year.
- The SPC would coordinate with the various ministries in forming an impartial investment budget and distribute it to all ministries.

This system was founded on the accumulation of all the project lists from the various ministries and was fraught with various problems, including i) a lack of project prioritization and consideration for ongoing projects based on an expansive, long-term perspective, and ii) problems in coping with urgent projects. Additionally, in dealings with other countries, the Vietnamese government found itself being asked to provide an account of the domestic public investment plan and prioritized ranking of investment projects, as part of increasing capital receipts resulting from FDI and public assistance (ODA).

At the same time, the World Bank was impressing upon Viet Nam the need for a medium- to long-term PIP as part of efforts to reform its fiscal and budgetary system. Monetary assistance from UNDP and the Dutch government was used to fund technical assistance to aid in the enactment of a public investment plan. In providing the Vietnamese government with economic structure adjustment funding (ESAF) in September 1994, the World Bank enforced the condition that a public investment plan be put in place for the three years from 1996 to 1998. Based on this, at the start of 1995 the Vietnamese government started work on the enactment of its first 5-year PIP, to commence in 1996. The objective of the plan was 5-year macroeconomic growth predictions and estimation of the level of investment necessary to achieve that growth, with investment being distributed across individual sectors and regions, based on consideration of means of capital procurement. The first PIP benefited from technical assistance from the World Bank and went through a process of incorporating the various opinions of all donors and affiliated institutions. It was approved by the prime minister in June 1996 and by parliament that November, before finally being enacted. The second PIP, which is to start in 2001, underwent the same developmental process and benefited from similar assistance. It was prepared with the cooperation of relevant ministries (headed by the MPI), government organizations and regional authorities, and is on the agenda for approval by parliament and also at the 9th party congress this March.

2-2. Planning and evaluation of performance of the first PIP (1996–2000)

Levels of investment and fund procurement plans as laid out in the first PIP (1996–2000), as well as predicted performance, are presented in Tables 4 and 5.

Table 4 Investment and fund procurement in the 5-year economic development plan

	1991-1995	%	1996-2000	%
Investment	**18.0**	**100.0**	**41.0-42.0**	**100.0**
State	7.7	43.0	15.6	37.1
FDI	4.9	27.0	14.0	33.3
Private	5.4	30.0	12.4	29.5
Fund Source	**18.0**	**100.0**	**41.0-42.0**	**100.0**
ODA	2.0	11.1	8.0	19.0
FDI	4.5	24.7	14.0	33.3
Domestic	11.5	63.9	21.0	50.0
Euro bond	-	-	1.0	
Investment / GDP	19.1%		30.0%	
ICOR	2.0-2.5		3.0-3.3	

(Sources: Government Report to CG, IMF data; Unit: Billion of USD, 1995)

As compared to investment performance over the 5 years leading up to the first 5-year PIP (starting in

1996), the size of investment relative to the GDP was forecast to jump up from 19% to 30%, with foreign direct investment predicted to increase sharply. This met with criticisms of the project being overly ambitious.

Table 5 Original targets and estimations of actual performance of the first 5-year economic development plan (1996–2000)

(Unit: trillion VDN at 1995 constant price)

	Planned 5 year	1996	1997	1998	1999	2000 committed	Likely outcome
Total	**460.0**	**73.0**	**83.6**	**76.5**	**77.9**	**88.4**	**399.5**
Domestic resources	232.0	42.5	46.7	44.0	48.5	56.5	238.3
External resources	227.5	30.5	36.9	32.4	29.4	31.9	161.2
PIP	**173.2**	**22.8**	**28.7**	**28.1**	**33.7**	**36.0**	**149.4**
Domestic resources		13.2	18.0	15.0	18.6	19.3	
External resources		9.6	10.7	13.2	15.2	16.8	
State budget funding	**96.8**	**15.2**	**17.8**	**16.4**	**19.5**	**18.4**	**87.3**
Component of ODA		4.4	4.7	5.3	5.5	5.9	
State credit	**76.4**	**7.6**	**10.9**	**11.7**	**14.2**	**17.6**	**62.1**
Of which, ODA loan		3.7	4.3	6.0	7.6	9.0	
SOE self-funding	**66.0**	**10.2**	**11.4**	**12.7**	**14.2**	**15.8**	**64.5**
Private domestic investment	**76.5**	**19.1**	**17.2**	**16.2**	**15.7**	**21.4**	**89.5**
FDI	**144.3**	**20.9**	**26.1**	**19.2**	**14.1**	**15.1**	**95.5**
(Macro indices)							
GDP growth rate	**9-10%**						**6.7%**
Industry production	**14-15%**						**12.2%**
Agricultural production	**4.5-5%**						**4.9%**
Services	**12-13%**						**7.0%**

(Sources: MPI comments on PIP, Public Expenditure Review 2000)

According to the predicted performance of the 5-year investment plan up to 2000—as determined by the MPI—total investment amounted to 87% of the figure predicted in the original plan, and PIP 86% of the original figure. The principal reason for the target figure not having been achieved is that FDI fell off sharply from 1998 under the effects of the Asian currency crisis. It is worth noting that while investment in the public sector was weak, growth in private sector investment exceeded predictions.

Table 6 The estimated sectoral allocation of PIP (1996-2000)

	% of PIP	**% of Capital budget expenditure**
Agriculture, forestry and aquaculture	18	45
Industry	45	4
Transport and communications	26	40
Education and training	4	10
Cultural, health, social affairs, and sports	6	17
Science, technology, and environment	1	4

(Source: MPI)

Table 6 presents a sectoral breakdown of investment, from which it is plain that industry accounts for almost half of investment, followed by investment in transport and communications, with primary industry in third place. It is also evident that investment in primary industry and social infrastructure relies heavily on capital budget expenditure.

Table 7 details the regional breakdown of PIP, from which it is evident that the Red River delta, south east region and Mekong delta account for around 70% of all investment. Data on the regional breakdown of investment is a primary source of information to the government in stipulating regional policy, and is vital in gauging the balance of investment from year to year and prioritizing policies.

Table 7 The estimated allocation of investment, by region

Region	% of PIP
Northern mountain area	7.6
Red River delta	26.0
North central	9.0
Central coastal area	11.7
Central highland	4.7
South east region	27.6
Mekong delta	15.6

(Source: MPI)

2-3. The framework for the second 5-year PIP (2001–2005)

MPI is currently working on finalizing the second PIP, and no detailed information on the original act tabled for approval by parliament and at the party congress this March is available. None the less, it is being laid out in accord with the economic framework of the next 10-year socio-economic development strategy, details of which are as follows:

- Double the GDP by 2010, and to this end, aim for an annual economic growth rate of 7% or higher
- Scale of investment: expand out to 30% of the GDP
- Scale of exports: double the ratio of exports to the GDP
- Reduce the scale of agricultural production (from 25% to 16–17% of the GDP)
- Increase the scale of industry production (from 35% to 40–41% of the GDP)
- Expand the service sector (from 40% to 42% of the GDP)
- Reduce the proportion of regional jobs (from 2/3 to 1/2 of the overall population) and concentrate the population in the cities (from 1/4 to 1/3)

Table 8 Macroeconomic goals for 2001-2010, and a comparison with the 1990s

Indicator	Actual average annual growth rate 1990-2000	Targeted average annual growth rate 2001-2010
GDP	7.6 %	7-8 %
Agriculture	4.2	4
Industry	11.2	10
Services	7.2	7
GDP per capita	6.0	5.8
Export earning growth	20.5	14
Manufactured exports	28.2	18.5
Labor force	2.8	2.4

Note: All values real growth rates (Sources: Draft Strategy and World Bank estimates)

The following is a comparison of the second 5-year PIP to the first 5-year PIP, based on data gleamed in interviews with MPI.

Table 9 Next five-year PIP (proposed)

(Unit: billion USD 1995 / billion USD 2000)

Source of funding	1996-2000	%	2001-2005	%	Condition
Total investment	**41.4**	**100**	**56-60**	**100**	**30%/GDP**
State budget	8.7	21	11.5	20	7% growth / year
Domestic fund	5.2	13	8	14	
ODA	3.5	8	3-3.5	6	
State credit	6.9	17	9-10	17	9-10% / year
Domestic fund	2.9	7	4-4.5	8	
ODA	4.0	10	5-5.5	9	
Public investment total	**15.6**	**38**	**20.5-21.5**	**37**	
SOE self-funded	5.9	14	9-10	17	9-10%/ year
Private enterprises	6.9	17	15-16	27	15-16%/ year
FDI	13.0	31	10-11	19	8.7% / year
Non-public investment	**25.8**	**62**	**34-37**	**63**	
Domestic fund total	20.9	50	38.5	66	
Foreign fund total	20.5	50	20.0	34	

(Source: Interview with MPI)

As with the first PIP, the second PIP assumes total investment totaling 30% of the GDP. This level of investment would appear to strike a balance with the expected GDP growth rate of 7%. ODA is predicted to regress as the economy grows, while it seems reasonable to expect domestic funds to rise. The second PIP predicts rapid growth in investment from private companies as compared to public investment, the achievement of which depends on new incentives for private sector investment. A slowdown in the reform of SOEs is also expected to have a significant effect in this respect. The degree of momentum that private sector economic activities get up will be determined by the efforts of the Vietnamese government to promote the private sector and also by the level of improvement in existing constraints on management and fund availability. The key to the furtherance of domestic and foreign private companies is the provision of a level playing field with SOEs.

The breakdown of sectoral investment is as follows.

Table 10 Investment allocation, by sector (2001-2005)

	1996-2000	2001-2005
Agriculture and rural areas	18%	15%
Industry	45%	45-47%
Transport and communications	26%	14-15%
Culture, education, health, etc.	11%	23-25%

(Source: MPI)

MPI documents on the sectoral breakdown of investment suggest a marked shift from the past 5 years. Notably, investment in hard infrastructure such as transport will be curtailed, and investment in "human basic needs" (HBN) such as education and health services will be doubled. Here, the marks of the doctrines of the World Bank poverty reduction strategic paper (PRSP) are plain to see. Investment in the HBN sector will be heavily dependent on government funding and be largely incompatible with conventional loans, in which sense strict monitoring of the disposal of funds and investment effectiveness will be required. Additionally, priority should be given to investment in agriculture and industry, due to these sectors having a relatively high standing, having the potential to create jobs and being associated with high investment efficiency.

3. Outstanding issues in PIP

3-1. Mechanism of deciding and making investments

Preparation and execution of the investment plan, and construction management regulations are as stipulated in Decree No. 52/1999/ND-CP of July 8, 1999 approved by the prime minister. The planning and execution of the investment plan as stipulated in the decree are roughly as detailed below.

State budget and state credit disposal planning and follow-up:

- Line ministry and regional people's committees make up initial investment project plans
- Line ministry and regional governments confer on the general investment plan for the upcoming financial year
- Investment plans are sent to MPI (by September)
- MPI integrates the investment plans of other ministries/agencies and regional governments, and works within budget constraints to determine the necessity and priority of projects in consultation

with ministries and regional governments, based on MPI initiatives. The results of this process are then presented to the government.

- The government decides on items of project category A, and MPI on items of project categories B and C, and instructs the line ministry and relevant regional government as to the execution of the investment. (The classification of projects according to categories A, B and C is based on the sector in which the investment is to be made and the size of investment. Category A status is a reflection of national project standing.)
- MPI issues an annual budget to bodies executing investment.
- Ministries/agencies and regional governments issued with budgetary information select investment projects within the bounds of the allotted budget, stipulate an investment project list, and submit the list to MPI and MOF for investment item registration (by the end of February).
- Government ministries and regional governments must manage annual investment projects in line with their project lists
- The Prime Minister's Office, MPI and MOF all have a say in the management of budget-funded investment.
- The system of appraisal and execution of state loans is basically the same as for the budget, except that the Development Assistance Fund (DAF) acts as a credit institution in managing investment.
- MPI assumes the role of prime liaison for ODA funding and executes investment with the approval of the Prime Minister's Office. Responsibility for disposal of funds is shared by MOF (non-remunerative items) and the State Bank of Viet Nam (SBV: state credit).

MPI acts as an intermediary in coordinating the Public Investment Plan, but the mandate for project determination lies with a range of different bodies, according to the project type. Additionally, the determining body and executing body are separate entities. As a result, the process from plan determination to execution is a complex one, and it takes time for consensus to be reached. One reason for delays in investment execution is that there are physical limits to the project appraisal, management and other capabilities of staff. In the future, there will be an increasing demand for pre-evaluation of investment items and post-execution monitoring of investment effectiveness, for which purpose it is of vital urgency that specialists be nurtured and skills generally enhanced. The transferral of investment determination to the regions should be pursued in order to enhance the efficiency of public investment execution, but for this to occur, regional specialists must be nurtured and inter-compatible regional administration achieved.

Table 11 Organizations in charge of investment plan determination and execution

Source of funding	Investment plan initiator	Determining body	Executing body	Remarks
State budget (ODA)	Line Ministries People's Committee MPI (coordination, allocation) (ODA – MPI)	A—PM's Office B—MPI C—MPI (ODA—PM's Office)	- Register investment item with MOF - Line Ministries - People's Committee	(Unrecoverable) project appraisal: MPI
State credit (ODA)	Same as above (coordinating with DAF and other bodies)	Same as above	Policy-based credit institutions such as DAF Funds made available to DAF by MOF and SBV (ODA)	(Recoverable) project appraisal and credit analysis: DAF
Investment on the part of SOEs	The SOE in question	The SOE in question	The SOE in question	Principally self-funded Restrictions apply to the target of investment
Investment on the part of PEs	The PE in question	The PE in question	The PE in question	
FDI	The investor in question	The investor in question	The investor in question	

(Source: MPI)

In the past, the Bank for Investment and Development of Viet Nam (BIDV, in charge of investment in priority industries and mountainous and other disadvantaged regions) and Investment Assistance Fund of the Investment Development Bureau (under the control of the MOF) had control of state credit, but in January 2000, the Development Assistance Fund (DAF) was set up, and made the principal vehicle for state credit to industry development and redeemable social infrastructure development projects. As a result, BIDV has been restricted to operating as a simple commercial bank. The DAF managing board is made up of representatives of the Prime Minister's Office, the Ministry of Finance, the Ministry of Planning and Investment and the State Bank of Viet Nam at the deputy minister/governor level, and forms the executive decision-making body for the fund. Daily operations are left in the hands of the board of directors. In theory, loan appraisal is at the sole discretion of the fund (except for category A items), although it is unclear whether this is the case in practice. In order to firm up the management of DAF, credit analysis, risk management and other specialist skills should be enhanced at the personnel level, and autonomy guaranteed, the actualization of which will be reflected in the future performance of the fund. Moral hazard is also a concern, as policy-based loans by way of fiscal assistance are expected, through such measures as debts being covered by fiscal decree.

Other outstanding issues identified in "Viet Nam 2010 — Entering the 21st Century", authored by a Vietnamese assistance donor group (made up of organizations including the World Bank, UNDP and ADB), are as follows.

3-2. Prioritization of investment

In order to enhance investment efficiency and in turn bump up productivity, it is vital that investment be prioritized by way of pre-investment cost benefit evaluation. In addition, factors such as environmental impact statements (environmental assessment) and evaluation of the external economic effect of investment, should be taken into consideration. In order to maintain the balance between supply and demand in the service industry and avoid investment redundancy, region- and sector-wise demand and investment needs must be documented. By way of carrying out such accurate pre-investment assessment, it is possible to reduce the various transaction costs associated with investment.

3-3. Coordination of the long-term plan with annual plans

In stipulating and executing the next 5-year PIP, MPI must carry out an annual investment review and a mid-term investment review half way through the 5-year term, in order for compatibility to be maintained between the 5-year long-term plan and each annual investment plan. Changes in the economic landscape can alter the urgency of investment projects, and developing a flexible investment framework incorporating regular inspection of investment plans and adjustment of project priority can be expected to contribute to investment efficiency.

3-4. Estimation of the maintenance cost of investment

On completion of investment projects, annual maintenance costs must be provided in order to sustain the long-term viability of the project assets. For this purpose, assessment of recurrent costs commensurate with the original investment must be made. At present, MOF has sole jurisdiction over such funding, but ideally it should coordinate with MPI and MOF. Re-investment in unusable assets must be recognized as being the source of large-scale fund loss.

3-5. The promotion of private sector investment

Domestic investment is a vital element of future Vietnamese economic growth. Specifically, investment in the public sector acts directly to raise the standard of social welfare in Viet Nam, and infrastructure development both enhances private sector investment efficiency and catalyzes investment. In order for public investment to be effective, fiscal regulations must be upheld, specialists nurtured, investment planning/ execution procedures streamlined and investment efficiency enhanced. In order for public credit to be effective, on the other hand, it is essential that financial robustness be maintained by way of prudently assessing loan redeemability. Further improvement in the capabilities of the investment system and those running the system is needed.

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