

Fostering High Growth in a Low Income Country

Programme Aid to Vietnam

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Evaluation of Swedish Programme Aid

Evaluation 99/17:7 “Fostering High Growth in a Low Income Country. Programme aid to Vietnam” is one working paper in a series of 13 working papers supporting the synthesis report “Dollars, Dialogue and Development. An evaluation of Swedish programme aid”, Sida Evaluation 99/17.

In 1998 Sida, the Department for Evaluation and Internal Audit, commissioned an evaluation of Swedish programme aid.¹ The evaluation has been carried out by the Institute of Social Studies (ISS). The evaluation comprises field studies in three countries; Uganda, Nicaragua and Vietnam and desk studies of five countries; Bangladesh, Cape Verde, Mozambique, Tanzania and Zambia. There are three thematic studies on conditionality, impact of adjustment policies and modalities of programme aid respectively. Finally, there is a study of the management of Swedish programme aid and a paper commenting on the World Bank report “Assessing Aid”.

The synthesis report and the 13 working papers constituting the evaluation of Swedish programme aid are listed below.

- 99/17 Dollars, Dialogue and Development. An evaluation of Swedish programme aid .
- 99/17:1 Development by Default. Programme aid to Bangladesh.
- 99/17:2 Supporting Success. Programme aid to Cape Verde.
- 99/17:3 Reform, Rehabilitation and Recovery. Programme aid to Mozambique.
- 99/17:4 Debt, Dependence and Fragile Development. Programme aid to Nicaragua.
- 99/17:5 Counting the Donors’ Blessings. Programme aid to Tanzania.
- 99/17:6 What Does the Showcase Show? Programme aid to Uganda.
- 99/17:7 Fostering High Growth in a Low Income Country. Programme aid to Vietnam.**
- 99/17:8 A Black Sheep Among the Reformers. Programme aid to Zambia.
- 99/17:9 Trends and Turns in the 1990s. Programme aid and the Swedish experience.
- 99/17:10 Programme Aid, Policies and Politics. Programme aid and conditionality.
- 99/17:11 The Impact of Adjustment Policies. Programme aid and reforms.
- 99/17:12 From Commodity Aid to Budget Support. Programme aid and its modalities.
- 99/17:13 Assessing Aid: a Manifesto for the 21st Century?

¹ See appendix 1 Terms of reference.

Acronyms

ADB	Asian Development Bank
ASEAN	Association of South East Asian Nations
CG	Consultative Group
CIEM	Central Institute of Economic Management
CIS	Commodity Import Support
CISP	Commodity Import Support Programme
CMEA	Trading block of Communist Countries
CPI	Consumer Price Index
DAC	Development Assistance Committee
DCA	Development Credit Agreement
EDI	Economic Development Institute (World Bank)
EPZ	Export Processing Zone
ESAF	Enhanced Structural Adjustment Facility
ESW	Economic and Sector Work
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GSO	Government Statistical Office
HCMC	Ho Chi Minh City
IDA	International Development Association
IFI	International Finance Institution
IMF	International Monetary Fund
MOI	Vietnam Ministry of Industry
MOLISA	Ministry of Labour Invalid and Social Affairs
MPI	Ministry of Planning and Investment
NIC	Newly Industrialising Countries
ODA	Overseas Development Aid
OECD	Organisation for Economic Cooperation and Development
PA	Poverty Assessment
PCF	People's Credit Funds
PER	Public Expenditure Review
PFP	Policy Framework Programme
PIP	Public Investment Programme
PSF	Price Stabilisation Fund
SAC	Structural Adjustment Credit
SAP	Structural Adjustment Programme
SBV	State Bank of Vietnam
SMP	Staff Monitored Programme
SOE	State Owned Enterprise
UN	United Nations
UNDP	United Nations Development Programme
VAT	Value Added Tax
VBA	Vietnam Bank for Agriculture
VINATEX	Vietnam Textile Industry

Table of contents

Executive Summary	v
1 The Vietnam miracle	1
2 Aid to Vietnam	3
2.1 Introduction	3
2.2 Trends in aid	3
2.3 Programme aid	6
2.4 Swedish programme aid	6
3 Policy reform and policy dialogue	12
3.1 The three phases of reform	12
3.2 The political economy of reform	16
3.3 Policy dialogue	25
3.4 The role of Sweden	29
4 Socio-economic development in the period of reform	32
4.1 Macroeconomic performance	32
4.2 Supply response	34
4.3 Poverty in Vietnam	54
4.4 Gender issues	64
4.5 Environment	65
5 Macroeconomic impact of aid inflows	68
5.1 Aid in context	68
5.2 Aid and the balance of payments	69
5.3 Aid and the budget	73
6 The future of Vietnamese development and the case for programme aid	76
6.1 What is to be done?	76
6.2 The absorptive capacity constraint	77
6.3 The conditions for programme aid	78
6.4 Concluding comment	79
References	80
Appendix 1 Terms of reference	83
Appendix 2 List of persons met	92

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Executive Summary

During the last two decades Vietnam has undergone the transition from one of the poorest countries in the world, with apparent aid dependence and bleak development prospects, to one of the most rapidly growing economies with an impressive record of lifting people out of poverty. Economic performance in the early 1990s was particularly remarkable as inflation was brought down as growth was simultaneously lifted to the level of 8 to 9 per cent and this was maintained for the following years. How has this been achieved, and what has been the role of aid?

Following the invasion of Cambodia in 1978, Vietnam was shunned by most of the international community, and a US embargo prevented lending by the International Financial Institutions (IFIs), the IMF and World Bank. Most aid in the 1980s came from the Soviet Union, although SIDA and UNDP also continued support. Soviet aid collapsed from 1990, so that by 1993 aid inflows were one quarter of their level a few years earlier. The Soviet withdrawal allowed Sweden to assume particular importance as one of the sole donors, accounting for around one-quarter of total aid in the early 1990s. However, following the lifting of the US embargo in 1994 aid has surged, as many donors have started aid programmes and the IFIs have embarked on substantial lending. Sweden's aid contribution has thus fallen back to that of a middle-ranking donor, although it enjoys higher status by virtue of the historical association between the two countries. Vietnam enjoys more than \$11 of aid per person, which is a high level for a country of its size, though aid is not that high relative to some other aggregates, such as imports and investment, since the country enjoys access to other sources of forex from foreign investment, remittances and rapid export growth.

Just over one-third of Swedish aid to Vietnam in the 1980s was programme aid, this share increasing in the early 1990s, but then falling back and there being no programme aid in recent years following Vietnam's failure to conclude an agreement for the third year of the ESAF in 1997. In the 1980s Swedish import support conformed to the allocative mechanism of the Vietnamese planning system, and then was no question of countervalue since the funds were seen as part of the state's support for state-owned enterprises (SOEs). But from 1989 a number of changes were introduced to make the system more market-oriented: enterprises were to pay countervalue and the funds were to be disbursed (and hence allocated) by the commercial banks (Sweden providing technical assistance to the banks for them to be able to play this role). In the absence of formal policy dialogue around policy-based lending, discussions over import support modalities thus played an important role in the liberalisation of the foreign exchange and credit markets.

There have without doubt been major changes in economic policy in Vietnam in the last twenty years. Three phases of reform may be identified. The first, started in 1979, was primarily liberalisation in the agricultural sector (including recognition of the fact that collectivisation had never really succeeded in the South), though there was also some limited autonomy accorded to state enterprises. By 1982 the first wave of reforms had ended and there were some attempts to reverse them. But the launch of *doi moi* in 1986 saw the removal of price controls and yet further relaxation of controls on SOEs, and the start of their restructuring. Liberalisation was intensified from 1989: subsidies to SOEs were ended and over one million workers laid off as the number of enterprises was halved, and market-oriented measures introduced in the foreign exchange and credit markets. This third wave of reforms is perceived to have ended around 1993, and some (including donors) argue that there should be a fourth wave of reforms of further tariff liberalisation, privatisation, and financial sector reform.

A few facts suggest that the traditional role played by programme aid in supporting reform has been of limited relevance in Vietnam. There was no formal policy dialogue until the US lifted its veto on IFI lending in 1993 (a year before the lifting of the US' own embargo): hence policy-based lending began just as the third wave of reforms was petering out. Correspondingly aid flows themselves did not increase substantially until 1994 (there was a large inflow in 1993, but this was to pay off IMF arrears and so flowed straight out again), by which time stabilisation and increased growth had been achieved. Aside from these "surface facts", a closer examination of the political economy of Vietnamese reform further supports the idea that policy dialogue has been of limited relevance.

The reforms clearly have a strong internal dynamic, many having been driven by a bottom-up process (called "fence-breaking") by which new policies are an *ex post* recognition of changes that have already taken place. Given the strong performance of the economy there have clearly been very many more winners than losers (there have been some losers, perhaps particularly amongst marginal groups), which has created a strong social basis for reform. A reversal of market-orientation would not be politically possible today. Donor influence is thus limited on the one hand by the fact that donors would have been going along with the tide - it was not even a question of pushing on an open door, the Vietnamese had taken the door off its hinges before most donors arrived on the scene. But in addition to the strength of these domestic pressures, donor influence is limited by the nature of Vietnamese political processes.

The policy making process in Vietnam is diffuse, and does not follow the formal structures that a political scientist may map out. The system is one of consultation and consensus, with many different bodies being involved in a single decision - not just ministries but also agencies, such as the Women's Union, and the multitude of think-tanks (over-laying which is the government/party divide and the relationship between the two). In one way such a system ideally enables donors to enter the dialogue either as an actor or influ-

encing key actors (if they can be identified) - but it mitigates against the “usual way” in which donors do business by discussing with a single authority who has the power to carry out agreements reached with donors. Donor influence is necessarily restricted when it will formally engage only with government, but the Party and, in particular, the Army are important political forces with whom they will not engage (having said that, the blurring of roles between these different components is such that donors probably do engage with Army, but without it being clear that such is the case).

Finally, the nature of policy discourse in Vietnam is rather different to that which many agencies are used to. Many categories used by outside agencies are not seen as applicable by the Vietnamese: distinctions between government and party and private and public being two of the most obvious and currently important cases. Moreover, form often replaces substance, so that there is great attention to introducing legislation (often without repealing existing, contradictory, laws), but rather less explicit attention at the policy level to sorting out problems which may arise, which is done on the ground by the forces of experience.

There has been little formal policy dialogue: one World Bank adjustment credit, an IMF stand-by arrangement, an uncompleted ESAF and two ADB sectoral adjustment credits (for agriculture and finance). The World Bank credit contained only ten monitorable conditions, only two of which required actual changes in policy and one of which (maximum tariff) was reversed almost as soon as it was complied with (indeed there is doubt that it ever was). Hence there has been little scope for formal policy dialogue and there has not been much of it anyway. What donor influence there has been has come through informal channels.

The World Bank and the IMF began work in Vietnam in 1989, there being a Staff Monitored Programme from the IMF and economic and sector work from the World Bank, who also provided the expertise for UNDP projects and thus had a formal entree into macroeconomic issues. There are differences of opinion as to the importance these actors played: the economic reports, training and policy seminars clearly fed into the Vietnamese policy process, and policy-makers were grateful for guidance on implementation being unfamiliar with the specifics of a market-oriented policy. Some also say that the IMF played an essential role in the design of the 1990s stabilisation programme, though evidence from other well-informed actors in the donor community would suggest that “essential” is putting it too strongly. It must always be remembered that the Vietnamese political system is based on plurality, and that the government will seek advice from several quarters (often asking several donors for advice on the same issue); under such circumstances it is difficult to ascribe a single actor a decisive role.

As one of the few donors with an established presence, Sweden was in a position to play a role in the crucial years of reform in the eighties and early nineties, and there is a general appreciation amongst Vietnamese actors and agency staff that they did indeed do so. Five channels may be identified

through which Swedish aid impacted upon the policy process: (1) systemic effects from the evolution of import support described above; (2) publication of regular economic studies; (3) related events, such as seminars, training and study visits; (4) technical assistance (both experts and training) through projects specifically aimed at policy reform; and (5) other projects, of which the Bai Bang paper mill is a notable example.

In summary, formal policy dialogue has played little role in economic reform in Vietnam to date. However, the input of ideas has supported policy change and allowed it to be carried forward, and this is precisely the sort of input which may be expected to be most successful in Vietnam given the way the political system works. It would of course be disingenuous to claim that this is a case where “donors got it right”, since it was the US embargo that prevented them introducing formal policy-based aid at an earlier stage.

It is clear that the impact of policy changes has been largely positive. Macroeconomic performance has been good, with low inflation in the 1990s and a good growth performance. Some commentators are concerned about the large current account deficit and that savings lag behind investment - but both of these are a necessary consequence of the large aid and other capital inflows during the 1990s, not a manifestation of a weak economy. The agricultural supply response has been substantial and can be observed across most crops and all regions. The country has gone from being a rice importer to being the world's third largest exporter. There have also been huge increases in the production of coconut, rubber, tea and cashew nuts, with very large increases in yield in a short space of time. These achievements have fed through to improvements in rural welfare. Qualitative research from rural areas finds that the periods of hunger, which have been a persistent feature of the country's history, are now a thing of the past. At the national level, poverty has fallen from around three-quarters in the first part of the 1980s to around one-third today.

There have also been large increases in output in the manufacturing sector, although there has also been substantial restructuring and large lay-offs (though total employment has risen). Nonetheless, some manufacturing appears to remain inefficient and would be unable to withstand a move closer to the market through more liberalisation.

Despite strong growth in agriculture and manufacturing, the share of the former in output is falling, and that of manufacturing staying roughly constant as the tertiary sector has displayed the most rapid growth. This is the sector about which we know the least, although even a visual impression testifies to its growth and importance. There are thus some reasons for questioning for how long growth will be maintained, or more specifically, if further liberalisation will enhance growth or impede it. Liberalisation will require at least a temporary setback in the manufacturing sector. It is not clear how much longer the agricultural supply response can continue without some attention to the constraints (credit and infrastructure) on that sector, constraints which liberalisation may tighten rather than relax.

Additional concerns may be raised about gender and environmental issues. Whilst much of the former rhetoric of gender equality may have indeed been just rhetoric, it seems plausible that there was greater political attention to gender issues in the past than over the past ten years. Whilst women have benefited from the overall increase in economic prosperity there have been gender-biases skewing these benefits toward men, to the extent that some women have indeed been left worse off. Resource use is an inevitable consequence of rapid growth, but the question is whether prices encourage excessive resource use, which the evidence suggests is indeed the case. These are both areas which have been paid little attention in the formal policy dialogue.

The importance of aid's macroeconomic effects is limited by its scale - at around 5 per cent of GDP it pays for less than one tenth of imports and about 15 per cent of GDP. Closer analysis of the balance of payments suggests that export earnings have indeed been the driving force behind imports. Without any aid in the 1990s imports would have been around 5 to 15 per cent less, depending what assumptions are made about debt service, and arrears would of course accumulated rather more rapidly. The data also suggest a limited role for aid in the government budget, where the most remarkable changes are (1) a large increase in revenue, (2) a switch from non-tax to tax revenue, (3) increased expenditures, (4) substantially reduced net transfers to SOEs, and (5) a large increase in the expenditure share of the social sectors. The order of magnitude of all these changes is such as to accord a relatively small role to aid.

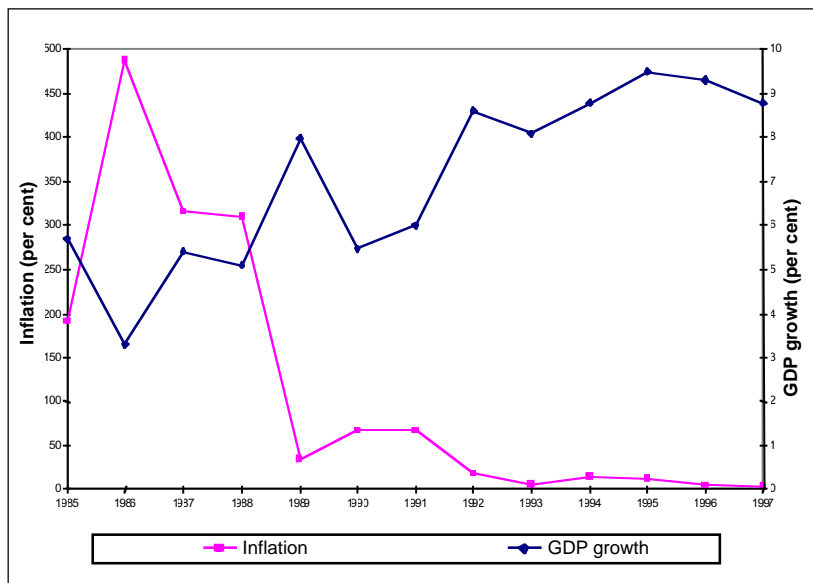
Aid has played a useful role in Vietnam's development in the 1990s, but it is not credible to argue that substantial progress would not have been made in the absence of aid. The Vietnamese themselves seem to attach particular importance to the expertise that comes with aid (and indeed with FDI), and we would agree that this has been where aid's contribution has largely lain. Whilst high aid seems set to continue, the nature of that aid is in some doubt. Donors wish to give budget aid, but believe the conditions (in particular budget transparency) are not met for them to do so. The alternatives are to scale back aid or to allow projects to expand. Current donor thinking, quite rightly, is not in favour of over-reliance on projects, and there seems little call for them in a country with a well-established government programme and a commitment to poverty reduction. Flexibility of approach, which allows continued support to the country's development, is called for.

Chapter 1

The Vietnam miracle

In the early 1980s few would have held out much hope for the Vietnamese economy, which had a modest to poor growth record and regular food shortages. The country seemed dependent on the Soviet aid it received, with little hope for development fuelled from domestic resources. Looking back from the late nineties, the picture has changed almost beyond recognition. Growth reached respectable levels in the late 1980s and has been 8 to 9 per cent for most of the nineties (Figure 1.1). Hyperinflation in the mid-eighties was brought under control, and the threatened resurgence of inflation in 1989-90 quickly quelled with a stabilisation programme which took effect at the same time as growth was reaching new highs.

Figure 1.1 Growth and inflation, 1985-97



There have been undoubted benefits to the vast majority of the population from these developments. Estimates (reported in Chapter 4) show that three-quarters of the population lived in poverty in the first half of the eighties, but that this figure had fallen to just over half by 1993 and may be expected to be around one-third by the end of the decade. Social indicators have continued to improve, both as incomes grow and spending on social services expands.

Prior to the Asian crisis, the economy was widely-tipped to be the next NIC, and some commentators would argue that the crisis is only a temporary hiccup on progress to this goal. The country has attracted large amounts of FDI prior to the crisis, plus very substantial remittances from Overseas Vietnamese.

This report examines the role of aid in Vietnam's remarkable performance, being specifically concerned with Swedish programme aid. Chapter 2 overviews the aid received by the country, and programme aid in particular. Programme aid can promote performance by policy change and the effect of the funds, resulting in three questions: (1) how has aid affected policy, (2) what have been the effects of policy changes, and (3) what has been the impact of the funds? Chapters 3 to 5 tackle these three questions. In the case of Vietnam (to a greater extent than we have found in most other country studies) aid has played some role, but not a pivotal one, in the reform process. Thus, whilst much of this report is concerned with the reform programme and its outcomes, these are not attributable to programme aid. Rather we focus on them since one of our concerns is the debate between government and donors as to the extent of reform to be pursued. Chapter 6 concludes with reflections on the future of programme aid.

Chapter 2

Aid to Vietnam

2.1 Introduction

Vietnam has undergone a change from being shunned by most of the international community in the 1980s and early nineties to having a rapidly growing aid programme, with high levels of aid per capita for a country of its size.¹ There has also been great change in the nature of aid, from Soviet-dominated commodity aid to a proliferation of Western donors with many projects, but also a sizeable amount of programme aid. These changes have also affected Sweden's position in Vietnam, so that it has moved from being the most important donor to being at best a mid-rank one in terms of aid volume – though, as we argue below, it retains some special position by virtue of its historic association with the country. This chapter plots these changes in a more detail, first reviewing the trends in total aid before moving to a more specific discussion of programme aid.

2.2 Trends in aid

Most western governments stopped aid to Vietnam following the invasion of Cambodia in 1978, though there were exceptions, of which Sweden was perhaps the most notable. However, most aid received in the 1980s came from the Soviet Union. Hence the usual source of data on aid – the Development Assistance Committee (DAC) – cannot be relied upon to accurately record the long-run trend in aid to Vietnam since their data excludes Soviet aid. Table 2.1 shows instead data from UNDP.

	1988	1989	1990	1991	1992
Disbursements	740	763	448	338	356
ODA per capita (US\$)	11.7	11.8	6.8	5.0	5.1
	1993	1994	1995	1996	1997
Disbursements	274	625	612	985	1,100
o/w BOP support	..	173	149	244	..
ODA per capita (US\$)	3.9	8.6	8.3	13.1	14.3
CG pledges	1,900	2,000	2,300	2,400	2,300

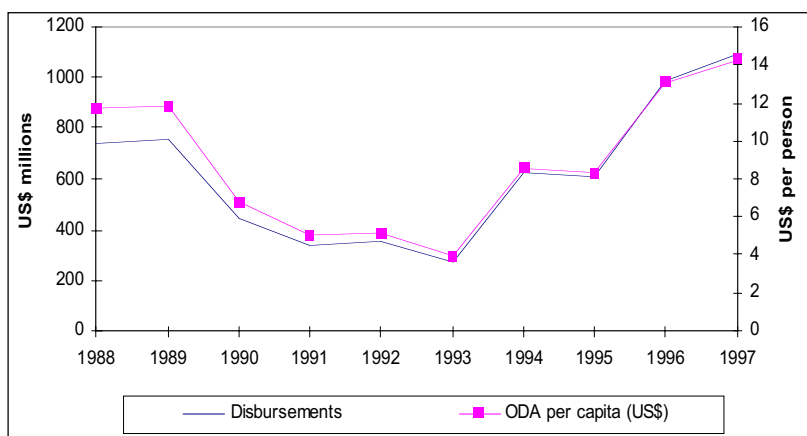
Source: UNDP

¹ There is a “small-country bias” in aid allocations so that small countries (with populations of one million or less) can receive very high aid per capita, but large countries do not: China and India each received net ODA of \$2 per person in 1996. In 1996 Vietnam had a higher aid per capita than the rather poorer (but larger) Bangladesh, and only a bit less than the much poorer (but smaller) Ethiopia.

These data are also graphed in Figure 2.1, which makes clear the U-shape as aid fell rapidly in the late eighties: aid in 1993 was barely one-third of that five years earlier. The data also show aid per capita, for which the fall is of course more accentuated.

The overall level of aid jumped rapidly from 1993 to 1994 as the aid programmes of many new donors came on stream. For example, the UK bilateral programme was begun in 1992, but large disbursements began only in 1994 (being \$2.7 million in 1993 and \$16.1 million the following year). Most significant was of course the entry of the IFIs. As shown in Table 2.2, both the IMF and World Bank actually took money out of Vietnam in 1993 as arrears were settled to clear the decks for renewed lending, whereas in 1994 between them the IFIs put over \$200 million into the country. Although there has been a levelling off in 1996–97, pledges at the consultative group (CG) have exceeded \$2 billion in recent years so that high aid inflows may be expected to continue for some time to come.

Figure 2.1 Total aid inflows



Turning to the sources of aid, Table 2.2 shows that multilateral aid has typically been around 30–50 per cent, with a dip in 1992 and 1993 (the latter being the year of the large net outflow from the IFIs). However, there has been a change in the composition of multilateral aid with, unusually, a very large share for the UN until the early 1990s. As will be discussed below, UNDP has assumed a particularly important position in Vietnam given the absence of other donors. There have also been changes in the composition of bilateral aid. In the eighties and early 1990s Sweden accounted for, on average, around half of bilateral aid (and so around one quarter of total aid, but recalling that Soviet aid is excluded from these figures). This share has shrunk during the 1990s as other donors have emerged and there has been some scaling back of the Swedish aid programme.² Several donors who gave little or no aid in the 1980s – such as Denmark, Germany and Japan, now give more than does Sweden.

² The reasons for this scaling back are not examined here, though one official in the Ministry of Foreign Affairs said there was a feeling that Sweden should not be “too important” a donor in any one country.

Table 2.2 Net ODA flows to Vietnam, 1983-96

	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
Bilateral	70.9	80.5	54.2	90.0	61.6	84.0	64.7	107.9	135.2	474.0	224.0	585.6	549.2	469.7
o/w Australia	0.0	0.0	0.4	0.1	1.2	1.0	1.0	1.4	2.6	8.4	19.6	33.4	39.8	47.7
Denmark	0.3	1.4	1.0	0.0	0.0	0.0	0.0	0.2	0.6	1.1	8.5	16.2	13.7	34.6
France	4.0	4.0	2.8	3.9	5.9	4.9	6.1	11.9	14.5	19.6	31.3	179.8	94.1	67.3
Germany	0.0	0.0	0.0	0.9	4.3	5.3	6.6	16.1	22.1	27.7	28.6	52.7	120.4	52.8
Japan	0.7	1.1	0.6	5.7	0.3	4.8	1.6	1.3	7.1	281.2	11.5	79.5	170.2	120.9
Sweden	49.8	63.0	37.5	64.0	38.4	54.4	34.1	53.7	57.2	59.7	44.1	21.1	34.0	46.2
Multilateral	105.9	109.9	114.0	146.5	111.0	147.8	48.1	81.8	103.3	109.3	34.0	311.2	279.7	458.6
o/w IMF	0.0	0.0	0.0	0.0	0.0	0.0	-9.0	-4.7	-9.6	0.0	-60.2	86.5	91.6	175.4
World Bank	3.0	6.2	7.3	5.2	0.4	0.0	-1.0	-1.0	-1.0	0.0	-0.6	125.2	46.5	188.0
UN organisations	23.4	16.8	25.8	39.2	28.3	60.2	55.8	81.3	80.0	73.6	77.4	70.4	59.4	45.8
Total	176.8	190.4	168.2	236.5	172.6	231.8	120.0	189.8	238.6	575.1	258.1	896.8	828.8	927.2
Memo item: share of total net ODA														
Sweden	28.2	33.1	22.3	27.1	22.2	23.5	28.4	28.3	24.0	10.4	17.1	2.3	4.1	5.0
World Bank and IMF	1.7	3.3	4.3	2.2	0.2	0.0	-8.3	-3.0	-4.4	0.0	-23.6	23.6	16.7	39.2
Bilateral	40.1	42.3	32.2	38.1	35.7	36.2	53.9	56.8	56.7	82.4	86.8	65.3	66.3	50.7
Multilateral	59.9	57.7	67.8	61.9	64.3	63.8	40.1	43.1	43.3	19.0	13.2	34.7	33.7	49.5

Source: OECD (various years)

2.3 Programme aid

It is difficult to get accurate data on the composition of aid. DAC's Geographical Distribution of Financial Flows to Developing Countries suggests there has been no programme aid (including debt relief) to Vietnam, which we know not to be the case. UNDP estimates, shown in Table 2.1, suggest balance of payments support to have been around one quarter of aid inflows, which seems a reasonable estimate for the mid-90s. The share will have since fallen since many donors (including Sweden) have stopped disbursing balance of payments support in the absence of an agreement with the IMF (though Japan and Germany are exceptions to this statement, and an ADB sector adjustment credit is still disbursing).

As described in more detail in the next chapter, the lifting of the US embargo in 1994 enabled the resumption of IFI-lending. This lending begun with an one-year IMF stand-by arrangement for \$190 million approved in October 1993. The following November a three-year ESAF was agreed, although this was not completed, going off-track in 1997.

The World Bank quickly put in place two projects, and by October 1994 a Structural Adjustment Credit (SAC) was approved. The first tranche of this two tranche operation was released on effectiveness two weeks after Board approval. The second tranche was released in September 1996, after the Board had given a waiver one of the nine conditions. This release was rather later than had been planned (it had been expected by the end of 1995) and meant that completion was not until problems with the IMF had emerged so that no SAC II has been negotiated.

The Asian Development Bank (ADB) has financed a sectoral adjustment credit in each of the financial and agricultural sectors. ADB's rules require that an IMF programme be in place for an adjustment credit to be approved. The financial sector programme, approved in November 1996, thus narrowly avoided the formal suspension of the ESAF and so has been disbursing programme aid whilst most other donors have stopped.

2.4 Swedish programme aid³

Programme aid (PA) has been an important part of Swedish aid to Vietnam since the 1980s: of the SEK 2.9 billion disbursed from 1982/83–89/90, 37 per cent (SEK 1.1 billion) was import support. This importance has of PA declined in the 1990s as there has been no programme in recent years. Three agreements have been concluded in the 1990s. The first was a three year programme of import support for SEK 350 million, although (as can be seen in Table 2.3) previous agreements were still being disbursed in the earlier years. Second was SEK 85 million of debt relief in 1993/94, and finally an agreement for SEK 60 million of import support in 1995 which was cofinancing with the World Bank.

Here we review the objective and rationale for programme aid, followed by an analysis of conditions and procedures (including countervalue).

³ This section is based on a background report by Maria Nilsson.

Table 2.3 Swedish programme aid to Vietnam (SEK 000)

	1986/87	1987/88	1988/89	1989/90	1990/91	1991/92	1992/93	1993/94	1994/95	1995/96	1997	Total 90s
Country Frame	65 300	25 900	77 600	10 794	253 490	96 073	125 267	2 836	0	0	0	0 477 666
Import Support	65 300	25 900	77 600	10 794	253 490	96 073	125 267	2 836	0	0	0	0 477 666
tied	11 600	6 600	25 200	n.a.	20 796	126	0	0	0	0	0	0 20 922
untied	53 700	19 300	52 400	n.a.	232 694	95 947	126 267	2 836	0	0	0	0 456 744
Budget Support	0	0	0	0	0	0	0	0	0	0	0	0
Debt Relief	0	0	0	0	0	0	0	0	0	0	0	0
Ec. Ref. and Debt Relief	2 000	0	0	0	0	0	0	85 000	0	60 000	0	125 000
Sida part	0	0	0	0	0	0	0	0	0	60 000	0	60 000
Import Support	0	0	0	0	0	0	0	0	0	60 000	0	60 000
Budget Support	0	0	0	0	0	0	0	0	0	0	0	0
Debt Relief	0	0	0	0	0	0	0	0	0	0	0	0
MFA part:	2 000	0	0	0	0	0	0	85 000	0	0	0	85 000
Bilateral	2 000	0	0	0	0	0	0	0	0	0	0	0
5 th dimension	0	0	0	0	0	0	0	85 000	0	0	0	85 000
Total PA	67 300	26 900	77 600	10 794	253 490	96 073	125 267	87 836	0	60 000	0	602 666
% of total aid to the country	20.4	8.9	24.8	3.8	67.4	32.3	38.5	23.8	0	15.2	0	n.a.
Sida	65 300	26 900	77 600	10 794	253 490	96 073	125 267	2 836	0	60 000	0	517 666
% of Sida to the country	19.9	8.9	24.8	3.8	67.4	32.3	38.5	0.1	0	15.2	0	n.a.

Objectives and rationale

The general objective for Swedish aid to Vietnam, stated in several sources in the 1990s, is to support the economic reform process, as well as democracy and human rights. (Sveriges utvecklingssamarbete med Vietnam). The specific objective for programme aid has always been related to the economic side of this objective – although programme aid has been suspended on “governance grounds” these concerns relate to budget transparency rather than political reform.

A SIDA memo to government in 1990 stated that “commodity support for Vietnam corresponds directly to the overall Swedish objective for commodity support, namely to support economic growth. The supply of foreign exchange is of decisive importance for the country’s possibilities to carry out the economic adjustment programme and a large commodity support is an important component in this process... To support the reform process it is suggested that the commodity support to Vietnam continue” (Memo from SIDA to the Government (5/4/90) Utvecklingssamarbetet med Vietnam 1990/91 – 1991/92 (Development co-operation with Vietnam 1990/91 – 1991/92).⁴ This statement captures what has appeared in the agreements in the 1990s, namely that programme aid is intended to support economic development (although the most recent agreement mentions only the intermediate activity of support for adjustment).

The rationale for programme aid has mostly been put in terms of the need for forex (or external imbalance). In the early 1990s this rationale was explained in part by the end of Soviet assistance. As seen in the last paragraph, a direct link has been made between the availability of goods and economic performance (see also the objective for the 1990 agreement in Table 2.4). A further rationale was that the US embargo prevented lending from the IFIs (e.g. Supplement to the Budget Bill, 1991/92). However, later the argument became that programme aid would assist normalisation of relations with the IFIs (with the suggestion that once relations were normalised then Swedish import support could reduce in order to switch resources to priority sectors)⁵ (Memo from SIDA to the Government (31/3 1992) Utvecklingssamarbetet med Vietnam 1992/93 – 1993/94). Sweden gave the SEK 85 million of debt relief (as part of a donor support group) once the US embargo was lifted in 1993 precisely to allow clearance of arrears with the IMF.

The rationale for the form of aid may be expected to lay the basis for determining the volume of that aid (e.g. through gap calculations). However, such an argument is not usually evident in Swedish programme aid documentation, so that the amounts may appear to have been plucked out of the air. Unusually, in the case of Vietnam a rationale for the volume of programme aid has mentioned: (1) “Based on the dynamic will to reform in Vietnam and the satisfying results reached so far, it is suggested that the Swedish

⁴ From the analysis of documentation carried out for the Evaluation of Swedish Programme Aid, this appears as one of the earliest explicit linkages of programme aid to the growth objective.

⁵ This statement echoes the 1992 import support evaluation (Faber, 1992).

contribution remain at the same level as the last fiscal year” (Memo from SIDA to the Government 19/4/95); (2) “The size of the Swedish contribution has also been compared to the needs of other regions or countries where Sweden supports economic reform.” (ibid.); and (3) “The earlier level should be kept, to be in line with amounts from Denmark and Holland...” (Memo from Sida to the Government 5/12/96).

There is a suggestion in some documents that programme aid should be phased out in Vietnam. As earlier noted, one argument was that Sweden need not provide these funds once the IFIs do so. Another document argues that good export performance will limit the need for balance of payments support (Memo from SIDA to the Government, 14/9/2, St'd till Ekonomiska Reformer och Skuldl%ottnadsÅtg%order 1992/93). However more recent discussions have, as indicated, focused on the conditions under which programme aid may be resumed, and there is now no suggestion that it may be an inappropriate aid modality.

Conditions and modalities

The conditions attached to programme aid may be of two types: restrictions on use and policy conditions. The conditions on use may be further subdivided into the tying of import support (which is in the interests of the donor rather than the recipient) and other restrictions designed to ensure the efficient use of the funds. During the 1980s over half of Swedish import support was procurement tied (Faber, 1992: 32), but such tying ended in 1990/91.

The commodity import support given throughout the 1980s and in the three year 1990 grant was disbursed through an evolving mechanism which became more market-based over time. Prior to 1989 the funds were allocated to ministries who decided what should be imported (enterprises made requests to their parent ministry in accordance with the state plan). SIDA was quite closely involved in the procedure, both since some of the aid was tied, and as technical assistance was often provided for larger orders. From 1989 a number of changes were introduced. First, it was proposed that countervalue should be paid (half up-front and half six months later): it is stressed in several Swedish documents that the aid is grant to government but not to the enterprise.⁶ However, the following year it was suggested instead that countervalue should be paid in full up-front, thus requiring enterprises to obtain credit to access the funds. More importantly, with this change it was intended that it should be the banks who decide to whom they gave credit – and hence who can access the forex – rather than the ministries. There was a suggestion from the Vietnamese side that the Vietcombank should be solely responsible for this process, but Sweden refused to accept such a monopolistic situation and provided technical assistance to enable other banks to learn the necessary procedures. The conditions included on to the use of funds shown in the 1990 agreement – such that they should go to viable companies and an agreed

⁶ Many companies could not pay and by early 1992 arrears of 75 per cent were reported, although this figure was reduced to 50 per cent by changing the exchange rate used for the calculation (a procedure which entitled some enterprises to a rebate!) (Faber, 1992:36).

share to non-state companies – are thus a snapshot of conditions which were developing over time.

As discussed below, these restrictions may be seen as a part of the policy dialogue process of changing the nature of the forex market and treatment of state-owned enterprises (SOEs), which could not be done through the usual formal channels in the absence of IFI involvement. Once an IFI programme was in place, then Swedish programme aid has become conditional on that programme (see the 1995 agreement). Since the 1995 agreement was co-financing for the World Bank it was disbursed by the Bank using the procedures they had established by that time, which involve disbursement of the forex through the banking sector and no restriction on the use of countervalue. However, the Vietnamese authorities do account for the countervalue even though they are not required to! This practice came to light when the ADB Resident Representative read in the papers of the support his agency had given to the sugar mills, something of which he was totally unaware. It turned out that the countervalue from the ADB agriculture sector credit had been used for this purpose. He then asked what the funds from the financial sector credit had been used for; the reply was that they had gone to the recapitalisation of the commercial banks!

Table 2.4 Swedish programme aid agreements in the 1990s

Type	Date of agreement	Amount (millions)	Conditions	Objectives
Import support	15/6/90	SEK 350	“Goods, which need advanced maintenance or training of personnel may not be included in the programme... a certain percentage shall be allocated to non-state companies. Before the beginning of the financial year Vietnam shall forward to Sweden a proposal for a Commodity Support Plan to be agreed upon by the Parties... The funds shall be allocated to viable companies, which shall pay counterpart funds calculated at the current official exchange rate to the authority appointed by the Vietnamese government. Credit, if any, shall be on short term nature and the rate of interest charged shall not contain any undue element of subsidy.”	“In order to facilitate importation of goods of high priority for the economic development of Vietnam, Sweden shall make available to Vietnam funds for the importation of goods and services for development purposes.”
Debt relief	n.a.	SEK 85	n.a.	n.a.
Balance of payments support	8/6/95	SEK 60	“Sweden may suspend the rights of Vietnam to withdraw the Swedish contribution in the event of the suspension by IDA of the rights of the Socialist Republic of Vietnam under the DCA.”	“The objective of this Agreement is to support the ongoing structural adjustment recovery programme (the Programme) in Vietnam, as described in the document ‘Policy Framework Paper, 1994–1997’, dated September 21, 1994, referred to in the Development Credit Agreement (DCA) entered into between the Socialist Republic of Vietnam and the International Development Association for the purpose of the Structural Adjustment Credit, SAC, Credit No 2657/VN dated October 28, 1994.”

Chapter 3

Policy reform and policy dialogue

“The government’s way of framing its relationship with donors seems to attach little importance to the kind of confidence-based donor-borrower relationship that donors like to describe as ‘policy dialogue’.” (Fabricis, 1998: 17).

3.1 The three phases of reform

Economic reform in Vietnam may be characterised as having past through three stages (Table 3.1).⁷ The initial period of reform, which affected mainly agriculture – allowing farmers to produce for the market – but also saw some greater autonomy for state owned enterprises (SOEs), began in 1979 though was partly reversed from 1982 to 1985. Further impetus to reform was given by the continued low growth performance and, despite currency reform in 1985, the emergence of hyper-inflation (Figure 1.1 above). The start of the Vietnamese reforms is often dated to the launch of *doi moi* at the Sixth Party Congress in December 1986, following which price controls were largely removed and further autonomy granted to SOEs. Subsequent years saw the beginnings of financial sector and trade reform. Growth picked up by 1988; inflation was brought sharply down by 1988 (though remaining at a quite high 35 per cent) but started to climb again in 1990. The re-emergence of inflation, combined with the collapse of the Soviet Union, and so the imminent drying up of Soviet aid, provoked the third wave of reforms from 1989, including a drastic restructuring of SOEs in the early 1990s, a tight monetary policy which brought inflation down to 5 per cent in 1993, further encouragement to foreign investment, and increases in the real cost of credit and foreign exchange. These reforms ushered in a period of higher growth which has run at eight to nine per cent for most of the nineties, but dropping in 1998 as a consequence of the impact of the East Asian crisis.

Despite the introduction of new legislation during the 1990s, including a pilot equitisation programme in 1992 and acceleration of that programme in the last year, there is a feeling, especially among the donor community, that reforms ran out of steam around 1992–93. Three main areas of reform are now seen as required: further trade liberalisation, financial sector reform, and state enterprise reform.

⁷ The reforms programme is described in many places; see, for example, the sources for Table 3.1.

Table 3.1 Policy change in Vietnam, 1979-1997

	1979-85: Partial and stalled reform	1986-88: First phase of Doi Moi	1989-present: More intensive reform
General policy stance	Measures introduced to allow more autonomy for economic actors, mainly in agriculture, but also SOEs. Attempts to reverse liberalisation in 1982-85.	Sixth Party Congress in December 1986 launches <i>Doi Moi</i> ("New Way"), redefining role of central planning. Creation of central treasury to execute budget.	Stabilisation and more intensive reform efforts; replacement of planning with market mechanisms.
Fiscal policy and public sector reform			1989: Restructuring of public sector pay, so all implicit subsidies abolished. 1990: Streamlining of government ministries. Turnover tax and profit tax introduced. 1996: law on state budget defines revenue and expenditure responsibilities.
State owned enterprises (SOEs)	1981: Decree 25 allowed to buy and sell in market (though many prices remain fixed) under "three plan system". Placed on self-accounting and self-financing basis. Piece-rate payment introduced. 1982-85: measures to tighten planning of activities.	1986: Increased autonomy encouraged. 1987: Decree 217 to reduce planning targets for SOEs to one (budget contribution).	1989: Decree 176 to restructure SOEs and implementation of elimination of government subsidies; 1991: below cost imported inputs ended; 1992: end of subsidised credit. Over period, no. of SOEs reduced from 12,000 to 7,000 (over 1 million workers laid off). 1995: Law on SOEs to consolidate previous legislation.
Monetary and financial policy	1985: Currency reform (new dong replaces old at ratio of 1:10).	1988: Separation of central and commercial banking functions by creation 4 state-owned commercial banks.	1989: positive real interest rates (but SOEs receive subsidised credit). 1990: Commercial Bank ordinance, lays foundation for private financial institutions; SBV prohibited from commercial banking activities. 1997: new law on SBV specifying functions.
Price policy	1985: Decision to end subsidies in all consumer and producer prices and price controls removed on all but small number of essential commodities.	1987: Price controls removed on all commodities except rice and kerosene (remains on some public sector output, mainly utilities). Abolition of control posts for internal trade.	1989: Formal abolition of two price system. 1991: All price controls removed except for electricity.

Exchange rate policy

1988: liberalisation of forex retentions, right to open foreign currency accounts, and use transfers for imports and loan repayments. Devaluation of rate for trade and invisibles.

1989: Rate unified and devalued. Retention scheme abolished: firms can use all forex earnings, sell or keep in dollar account. State Bank kept official rate close to parallel rate until introduction limited market operations in Hanoi and HCMC in 1991. 1994: Introduction of intra-bank market. 1996: Tax on inward remittances abolished. 1997: Companies required to surrender forex earnings to banks (over and above own import requirements).

Trade policy

1981: SOEs allowed to import and export directly (with licence) and start of local government trading companies.

1988: Tariffs introduced (law on import and export duties). End of government monopoly of foreign trade.

1989: Most quotas removed (remain on luxury items). Number of trading permits increased from 30 in 1988 to 800 in 1992 and in 1993 private companies allowed to apply for permits. 1991: Regulation on setting up EPZs. 1994: Import permits eliminated for all but 15 commodities. 1995: Export quotas abolished on all commodities except rice, and reduction in import quotas to 7 commodities. Vietnam joins ASEAN. 1997: Increased number of goods subject to quotas (and sugar imports prohibited). Consumer imports subject to tariffs rather than annual import plans.

Agricultural policy

From 1979 producers can choose who to produce and sell on open market, so long as they also meet contract with collective; this system generalised in 1981 (Directive 100).

April 1988: Decree 10, part of series of reforms culminating in replacement of compulsory grain-purchase quotas with market, and Land Law for devolution land rights to peasantry with 15 year leases. Also 1988 crop and input prices liberalised.

1994: Land leases extended to 99 years.

Private sector development	1988: Resolution 16, legal basis for small-scale enterprise.	1989: Ordinance on economic contracts: establish right of legal entities to enter contracts. 1990: Company Law and Private Business Law. 1992: new Constitution recognizes private ownership. 1993: Land Law extends private use rights (to mortgaging and inheritance). 1995: new Land act limits provision from 1993 act. Civil Code lays basis for market economy with protection of industrial property rights.
Social sectors		1989: Health sector reforms: user charges, legalisation private practice, liberalisation production and distribution of pharmaceuticals. 1989: user fees in education above Grade 3. 1993: Poverty Alleviation Programme launched.
Foreign investment	No foreign investment	1990: foreign investment law revised. 1992: investment law revised to reduce discrimination in favour of joint ventures over 100% foreign-owned enterprises. 1996: new law limits import duty exemptions.
Labour markets	Labour movement restricted	1994: Labour code establishes employer and employee rights; including arbitration procedures and right to strike.
Governance	1980: Constitution	1989: Visit of Vatican envoy; 1991: constitutional amendment making Assembly highest state body. 1992: New Constitution. 1994: normalisation of relations with US, visiting officials talk of democratisation. 1997: new anti-corruption law.
Aid	(Aid from most donors, except USSR, suspended in 1978 following invasion of Kampuchea).	1989: Collapse of Soviet Aid. 1993: Major debt restructuring and settlement of arrears. 1994: Resumption of relations with US and multilaterals. 1997: decree on Aid Management and Co-ordination

Sources: Irvin (1995), Florde and de Vylder (1996) and Centre for International Economics (1998a) and various issues of *Vietnam Economic Review* and *Far Eastern Economic Review*.

These three areas are closely linked: loss-making SOEs are supported by the state-owned commercial banks, which are thus building up a large potential bad debt.⁸ A frequently cited Sida-financed report by Kokko (1997) demonstrated that, despite various liberalisation measures, a very substantial degree of protection remains. This protection has been a source of SOE profits, though their performance is said to have worsened considerably in recent years. Clearly liberalisation will weaken them still further – hence the need to restructure through closure or equitisation – and it is argued that in the interests of the overall health of the economy the government should not require the banks to effectively underwrite SOE losses (this point being seen as a main lesson of the East Asian crisis – see, for example, UNDP 1998).

3.2 The political economy of reform⁹

There is an important difference between a possible fourth wave of reform¹⁰ and measures taken thus far. There has been a strong domestic constituency behind reforms to date and it has clearly been a wholly-locally owned process. Indeed, many policy changes have in fact been *ex post* recognition of changes which have already taken place (termed “fence-breaking”). Fence-breaking has been a particular characteristic of agricultural reforms since the early 1980s, and remains so (it was expected in 1998 the law restricting land holdings to three hectares per household will be rescinded since a recent survey shows that in practice many exceed that amount). But it has also been a feature of the industrial sector, as SOE management exerted autonomy by trading on its own account. The possibility of fence-breaking brings home the fact that the Communist Party did not have authoritarian control of all parts of society, but has rather maintained its rule through a system of checks and balances operating around the principle of consensus (Porter calls it “balanced tension between opposing views” 1993: 116). As we elaborate below, whilst there has been no political reform toward Western-style democracy, it would be mistaken to characterise the Vietnamese political systems as wholly without mass representation. Moreover, the extent of support for the reforms – both as they took place and as that has built up subsequently, means that they would not be reversible. Indeed, by joining the regional groupings ASEAN and APEC the government has committed itself to further reform, rather than reversing what has already taken place.

⁸ The most recently available data (to 1996) show that the increase in bad debt is largely to private companies rather than SOEs, but personal communication from the IMF indicates that this situation has changed in the last two years. It was further stated that most SOEs are now making losses so that any loan to an SOE is likely to turn into bad debt.

⁹ Although drawing on various authorities, this account of domestic political economy is largely built upon impressions formed during the field visit. Indeed, it would be fair to say that the visit led to a radical rethinking of our outlook, which previously accepted the “received wisdom” of much writing on Vietnamese politics.

¹⁰ Three recent reports by Sida have had as their main message the need for a fourth wave of reform (Kokko and Zejan, 1996; Kokko, 1997; Kokko and Sjöholm, 1997).

The reason for such widespread support for reform is of course that the policy changes have had relatively few costs and so few losers. Agricultural liberalisation led to a massive supply response and consequently increased incomes (see Chapter 4). Macroeconomic stabilisation carried more costs, but for example the number of people who lost their jobs in SOEs was relatively small (just over one per cent of the population) and many new opportunities opened up in the private sector (total employment continued to rise). The open door policy led to an inflow of foreign investment which was especially beneficial to the urban areas in Vietnam. By contrast, the next set of reforms would undermine strong centres of rent seeking behaviour. This will happen not only because of the end of inefficient production for protected markets, but it would end the possibility of imposing transaction costs on other sectors in the economy. For example, it would end profits to be made from quota allocations for import and export. State enterprises can also function in a situation of privileged access and strong regulation as “a front company that collects rent without engaging in any productive activity itself” (Bring et al., 1998: 37). Reforms which directly affect access to such sources of enrichment will clearly arouse strong resistance.

The policy process

In order to understand how donors may affect policy it is necessary to have an understanding of the policy-making process, in particular as it appears that some of the concepts routinely employed by the donors are of questionable validity in the Vietnamese setting. We explore these issues under five headings.

1. A policy dialogue assumes that there is a current policy position which will be defended by government. But that may be the case less often than seems in Vietnam: policy making appears to be more reactive than proactive.

There is virtual consensus that Vietnamese reforms are crisis driven, the worse the situation of the economy, the better it is considered to be for reform (summed up as “bad times, good policy; good times, bad policy”). Often reforms are already rooted in experiments which had been underway and then suddenly got scope to continue. This is especially so with the major rural reforms which were responding to spontaneous processes started from below. The present regional economic crisis is thus seen by donors and members of the Vietnamese pro-market reform camp as a possibility for a breakthrough. As a consequence of the crisis foreign direct investment will become scarcer, especially as the region was an important source, and Vietnam will lose its markets in the region and exports to other areas have to compete with neighbouring countries which have become more competitive due to very substantial devaluations.¹¹ The resulting pressure on foreign exchange and credit markets could trigger off more intensive reforms. In the short run it

¹¹ Distorted market conditions in Vietnam make it difficult to directly compare costs of production with neighbouring countries, but the existence of wide-spread smuggling suggest that many local companies can only compete in domestic markets by virtue of protection. One foreign manufacturer of wash basins and lavatories in HCMC complained of competition from his own brand which was manufactured in Thailand and carried across the border by hand.

seems however the adopted solutions have been stricter exchange control and imposition of import quotas with the hope that “the typhoon will pass us by”.

So far as the possibility for aid to affect reform is concerned, this drifting attitude toward policy making is reinforced by the fact that aid is relatively new to Vietnam. The distinction between programme aid and project aid is not widely understood: instead, Vietnamese officials make distinctions between aid in capital formation and technical assistance (which they label hardware and software); programme aid is often confused with an aid programme, which is seen as a list of projects. Indeed, there is a strong emphasis on technology transfer: aid (most usually called “ODA” by Vietnamese officials) and FDI are not sharply distinguished from one another. There is often a striking unawareness of the nature of the donor demands that accompany ODA. This was particularly the case when donors stepped up their aid with the lifting of the US embargo in 1994, but examples may still be found such as micro-finance and industrial policy:

- Micro credit is a major part of Vietnam’s poverty alleviation strategy, largely comprising subsidised credit targeted at people who are declared poor by the local authorities. The donor community looks at these schemes with great reservation, arguing they distort the market and suffer from poor targeting. The schemes are top-down in nature whereas, as observed by a technical adviser from the Rabo bank (a Dutch bank which has its roots in co-operative banking) to the Vietnamese Bank for the Poor, elsewhere such schemes originate from below. This fact was reported by the management of the bank as a good thing, while donor discourse would stress roots in a movement from below as most desirable.
- An official interviewed at the Ministry of Industry had no illusions about the difficult situation of Vietnamese industry faced by liberalisation. Nevertheless, he made no recourse to arguments of improving competitiveness in such a situation, but rather reaffirmed structuralist arguments for government support to local producers to replace imports, including a desire that donors would consider investments in steel production and fertiliser as infrastructure projects.

These examples illustrate not only that Vietnamese officials often hold opinions at odds with donor attitudes, but that they willingly express these to visiting donor missions, which in many other countries are greeted with the latest buzz words of the international development community.

2. Form often replaces substance in Vietnamese policy making.

The more policy discussion is broad and general, the less substantive policy content is and there is a tendency to reason in broad and general terms. Policy dialogue centres around the goal of a full-fledged market economy. Vietnamese officials and intellectuals often say that there is agreement on this goal, but that there are differences about how to achieve it. Vietnamese attitudes toward the market often have almost Marxist overtones: a dialectical struggle between private and state sectors will come to a head triggered by the crises in the East

Asian economies which will lead to the contradiction-free situation of a free market. The market is seen as solving all problems. However this attitude is far removed from the uncertain and drifting fields of interests that actually form policy making in Vietnam. For example, market failure tends not to be clearly identified: an official the Ministry of Agriculture stated that there is not enough capital flowing into internal agricultural trade and as a result there is not enough competition among traders which depresses farm gate prices. The ultimate response to this question was however that there was not a good report about this problem. The result is that policy is often clear, but issues of practice and implementation remain unaddressed.

During a visit to the Department of Taxes officials were very clear which direction tax reform should go: a shift from direct to indirect taxes, introduction of VAT, and moving to a flat rate in corporate taxes. However, these are formal intentions and there was no strategic thinking on identification of possible problem areas in implementation. Another typical example, encountered at the Ministry of Labour, Invalids and Social Affairs (MOLISA), is the lack of any policy on wages and salaries while on the other hand there is much stress on the existence of a labour tribunal. Such a tribunal needs however a policy on, for example, the relation between pay in the public sector, the state enterprise sector and the private sector to adjudicate. It is therefore not surprising that 'According to information of the Labour Court, there have been no fewer than 252 wild cat strikes since the court was established in 1995. It is interesting that the court has not had a role to play in the resolution of such collective conflicts.' (Bring et.al, 1998;P.45) :

Legislation plays an important role in official thinking and there are regular references to decrees, ordinances and laws. A mixture of French and Eastern European thinking is evident: French in the sense that codification, rather than building upon case law, is dominant and Eastern European in terms of plan fulfilment: we have a list of a certain number of laws which we have enacted and there is a plan to enact a number more. Sometimes there is also a general awareness then of the basic issues involved, but on the whole there is little attention for responding by legislation to actual problems coming up and the implementation of laws through legal administration. The opinion in the donor community that since 1992 there have only been reforms on paper must be seen in this light (though we would suggest that this attitude is overstated).

3. Sharp distinctions between categories are often not applicable to the Vietnamese situation.

In its most extreme form one finds this lack of distinction in an equation of foreign direct investment with development aid. Contact with the outside world is virtually everywhere seen as essential to gain access to modern technology. Foreign investment is then often simply seen as a good in itself. In the Vietnamese situation, however, a substantial part of foreign investment seems to have gone in import substitution producing for a highly protected local market. This position is quite different from for example the Korean situation,

where foreign investment was regarded critically, especially with the aim to gain access to technology and marketing knowledge in order to penetrate foreign markets (Mardon, 1990). When talk turns to models of development, it tends to be stressed that the Vietnamese model is different – but there is no clear definition of a Vietnamese model. Similarly, although outside influences are eagerly sought and often referred to, they are shaped in forms which are different. For example, in the early 1990s state enterprises were reorganised through mergers into strategic groups, a move seen to be inspired by the Korean and Japanese experience (Kolko, 1997: 55), and which are indeed referred to locally as *cherboels*. However in the Vietnamese situation these were a much larger group of such entities and not only broad diversified groups were formed but also specialised strategic groups. Unlike in the other countries the formation of such entities were not tied to the penetration of particular export markets. Presently there is a shift to attention for small and medium enterprises inspired on the Taiwanese model, partly because of the fact that the big conglomerates played a major role in the East Asian crisis, but also as most private sector development in Vietnam is in that sector. Yet at the same time there is no drive to dismantle the big groups. Small and medium enterprises will be equitised first and there is a great reluctance to bring big enterprises out of the orbit of state control. That is ostensibly not led by any policy consideration as regards possible future growth of the economy, but more by considerations of practicality: small companies are much easier to process and it is easier to place their stock among employees. At the same time other considerations, which will not be spelled out, may play a role: somebody who worked for the Saigon Jewellery Company maintained for example that this company could not be equitised as gold was “too important”.

The ability of a state owned enterprise to run along market lines as such does not seem in doubt. For example, Vietnam Economic News reported that “though meeting many difficulties in the market oriented economy, the Military Commercial Bank, established in November 1994, has posted considerable gains, greatly contributing to the development of national defence economic activities. From now up till the year 2000, the branch will invest in building a military textile industrial zone and prepare for stock market ownership” (17–23/8/98). The continuing involvement of state bodies in direct production illustrates that the government/SOE divide is not a sharp one. When asked if he would like to move elsewhere one manager of an SOE replied that it was not up to him, his next posting could be in an SOE, government or the Party apparatus as the authorities saw fit.

A final and major distinction which does not seem to operate is that between the public and private domain: the private sector is sometimes called the stepchild of officialdom. The linkages between the two sectors have been commented upon incisively by outside observers: Kolko writes bluntly that “party membership is a crucial prerequisite for entrepreneurial success” (Kolko, 1997: 10). Fforde (1997: 20) describes the situation more subtly: “the way in which state activities are highly ‘private’ in their nature, penetrated by kinship

and other linkages, so that state and party resources tend to be used in ways that reflect interests driving these structures, which are not closely aligned with large business interests”. A final and apt description of the way in which state and private interests intermesh is that by Bring et al.:

One of our informants, a private entrepreneur, had previously been director of a state company. After retirement he started a private manufacturing company. Being able to take his existing stock of customers with him was a big help and he could expect to deliver goods to the public sector. He also had access to capital through his earlier bank contacts. His firm had grown under the protection of the state sector. The company's turnover had also grown very quickly ...Equally important was being able to make use of informal links to subcontracting satellite companies, which further improved flexibility. Thus the real number of workers involved in the activities of his firm was much greater than 200 (the actual number on his payroll). (Bring et al, 1998: 38).

If such situations are common then it becomes difficult to distinguish between a private sector which should be viable in market conditions and the public sector. It may also explain much wider resistance against state enterprise reform than one would assume if state enterprises were merely a sector competing with the private sector. Fforde summarised the situation succinctly as: “Vietnamese SOEs operate mainly according to local and quasi private interests, and should not be seen as fundamentally ‘public’ in nature” (1997:20).

4. The policy making process is diffuse.

Policy dialogue needs clear partners and those are often difficult to find in Vietnamese situation, which is characterised by consultation and consensus. Hence one of the donors outlined the following contradiction: on the one hand over-centralisation and on the other consensus – once a decision is made it has to be supported by all people involved. Thus, the State Bank of Vietnam (SBV, the central bank) stressed their relative independence, but at the same time mentioned many consultative procedures. Monetary policy is made by SBV in consultation with the Ministry of Finance and the Ministry of Investment Planning, but there was also mention of a fiscal and monetary council of the deputy prime minister and the constitution vested authority on monetary policy in the National Assembly. The National Assembly also selects the governor of the central bank, but it is the prime minister who draws up a list of candidates and the appointment has to be submitted to the president for approval. At first sight such procedures seem reminiscent of the rhetoric of democratic centralism which is inherent in a Communist state, where a democratic gloss is given to a highly autocratic process. However, in the case of Vietnam, it is doubtful whether it has ever been as centralised and tightly controlled from the top as other communist countries. An official in the Japanese Embassy had been in Vietnam in the early eighties when Vietnam was a much more closed society. In the past years he had gained much more insight and he wondered now whether Vietnam had ever been a centrally planned economy.

There is a multitude of agencies giving policy advice: think-tanks, the social-political agencies such as Women's Union, and Ministries themselves. The Central Institute for Economic Management (CIEM) has played a major role in giving policy advice since 1978. In the beginning it had a monopoly as all Russian aid in management training was directed through them. Now there are many donors and as a consequence many such institutions are involved in this field, such as the Strategic Development Institute and the council of economic advisors to the prime minister. When CIEM described its advisory activities it stressed the consensual nature of much decision making. It works first through its parent ministry,¹² the Ministry of Planning and Investment, then consultation with other sectoral ministries, thereafter wider consultation in society. Finally they stressed the importance of the National Assembly. Strongly characteristic of the consensual nature of this process is that there was no mention of the possibility of a direct clash between parliament and government's proposal but rather that proposals would be sent back for revision. Policy making seems to be characterised by a wide number of institutions working on proposals, but their actions are also constrained. For example, independent initiatives to identify areas of research were not known in the university. Certain institutions undoubtedly play a key role in the policy making process – notably the Ministry of Investment and Planning – but this role is embedded in much wider consultative processes.

The situation in Vietnam differs thus considerably from the one described by Wade as typical of the East Asian experience: “a ‘pilot agency’ or ‘economic general staff’ within the general bureaucracy whose policy heartland is the industrial and trade profile of the economy and its growth path... Taiwan, Korea and Japan have all used the ‘few agencies’ model in contrast to the ‘many agencies’ model of the United States and Great Britain” [Wade, 1990: 371]. In Vietnam, it is difficult even to isolate particular agencies.

5. The Communist Party, the Fatherland Front and the Armed Forces.

It is therefore not surprising that Vietnamese decision making is considered by donors to be extremely opaque. That situation is particularly so with respect to the party, Fatherland Front and the army. The Vietnamese government is firmly committed to one party rule; organisations besides the party are organised in a corporative fashion in the Fatherland Front while the armed forces are undoubtedly a great force in the political system. Yet, the following quote sums up our state of knowledge:

The Communist Party is still a crucial administrative apparatus in itself. Its administrative network, with many ramifications across the whole country, is little studied. At the central level central commissions correspond to ministries. In different social areas there are also special blocs, in which Party and Government bodies and organisations within the Fatherland Front are co-ordinated, which adds further to the confusion about the exercise of authority in society. (Bring et al., 1998: 16).

¹² All think-tanks are under a parent ministry.

Paradox is striking in Vietnam, and this fact can be seen with respect to the role of the Communist Party. On the one hand one can see recent trends as a reaffirmation of party control, a tendency which is combined with pessimism concerning the integrity of the party; Fforde writes about “the continuing effects, since around 1992–93, of the political re-centralisation and resumption of active efforts to enhance party control. The state apparatus remains fractured and ineffective, and too often driven by the desire to control and limit commercial activities” (1997: p.6). Kolko identifies the Army’s political commissar, General Le Khia Phieu as a driving force behind the attempt to maintain party control in an unsigned article in the party newspaper: the army “had the central role in maintaining not only territorial integrity but ‘political stability’ in the face of the challenge of ‘peaceful evolution’...The word ‘market’ was not used once. The market was the explicit enemy” (1997:139). Kolko stressed the creation of a standing committee from among the Politburo with overriding powers at the ensuing Party Congress in 1996, concluding that “the anti market forces are certainly preponderant on the standing board” (1997: 147). Kolko sees this however not merely as a victory for anti-market forces but also as a defeat for democratisation and opening the way for unbridled power for an elite to enrich themselves. The logical consequence of such a line of argument is that economic reform is dependent upon political reform as the centres of rent-seeking can only be challenged if there is also political change.

However, a different interpretation of these events may be offered. The party is undoubtedly pervasive in Vietnamese life and has at the very least to condone all initiatives taken. That does not mean that it is a united, centrally-directed whole. The newspapers and (English language) press tend to follow party lines, although problems are sometimes mentioned and seem to be appreciated by the public. On an individual level Vietnamese may be very critical of the government and yet be at the same time party members: no automatic distinction may be made between party members and those critical of the government. At one meeting with several strong advocates of the market, it was commented that “we are all party members here”. The party adapts to new situations: a gradual turnover in leadership and the National Assembly (which also has independent members) is developing as a centre of power in its own right.

The culture of consensus building and endless consultation indicates that there is more room for participation in the decision making process than seems at first sight. The reform process itself and the assimilation of rural unrest in recent years – centring on corruption and lack of transparency in local budgets – also indicate that these organs are not merely resisting change. Yet at the same time the rather pluralist nature of the political system can be seen as a problem. The strong regional apparatuses indicate pluralism, but at the same time these are seen as fiefdoms where uncontrolled power can lead to arbitrary and rent seeking activity. It was mentioned above that the distinction between public and private may often be blurred in Vietnam. Career structures imply often a switch between party and government posts – positions in the party

and the Fatherland Front are treated as government positions. To outsiders it is often not clear who is who, as one donor representative said when asked if they had contact with the army: “maybe, we don’t know”. The consequence of this situation may be that a possible view of the party and army suppressing civil society may hold less than it would if it were possible to clearly distinguish separate spheres of influence.

This being said, there does seem little doubt that the party retreated considerably since the onset of economic reform and so raises the question of the role of the party in contemporary Vietnamese politics. Bring et al. (1998) mentioned as the most far reaching position within the present framework that its leadership role should become symbolic, similar to the constitutional monarchy in Western Europe – the conscience of the nation rather than the leader of the nation (and thus with ultimate power to approve or reject what comes up in society). A striking example in this respect has been strong party influence in land legislation. However, the party seems also to be a repository of moral values: for example, the stress laid on social evils as a consequence of the introduction of the market. There is clearly a struggle going on in Vietnamese minds about such matters and it may be that the party may be seen as the ultimate guardian in these whereby party integrity is exemplified in the figure of Ho Chi Min.

In the Vietnamese context nationalism is of course an important force and the party may not only be the repository of such values, but also be the ultimate guardian of national unity. Vietnam is a much more diverse country than seems at first sight and relations between the ethnic majority and minorities may be a delicate issue. The differences between north and south have not disappeared after unification. These differences are sharpened by the economic liberalisation which has taken place. From this perspective the party may retain considerable legitimacy.

The big question remains that we do not know what is the moral credibility of the party in Vietnam. There is no doubt that it is questioned in certain quarters. A sceptical view on the party at the grassroots can for example be deduced from Liljestrom *et al.*

In Minh Dan brigade there are three forums where workers can discuss matters of social security and services...The Communist Party, the trade union and the Women’s Union. The workers themselves seem to view them more as formal institutions than as a platform for their own aims and influence (1998: 64).

Bring et al. write that “in general, however, people’s interest in the Party, in politics as well as in the common good, seems weak” (1998:6).

However, whichever view is taken of the role of the party, the scope of effective donor conditionality appears weak. This argument is elaborated in the next two sections.

3.3 Policy dialogue

Policy dialogue prior to 1993

The absence of the formal structure of policy dialogue has not meant that there has been no engagement on policy issues: some donors, notably Sweden and UNDP, have been engaged in policy dialogue over a long period, and both the World Bank and IMF took up discussions with the government in 1989. This is indeed the position taken by *Assessing Aid*, which states that “intensive staff time required little money and made a big contribution to the country’s reform and development” (World Bank, 1998: 108) – and the report explicitly recognises the role of SIDA (along with UNDP) several times.

The IFIs were thus involved in various ways in the period 1989–93. The IMF mainly through the “Intensified Collaborative Approach” with a staff-monitored programme (SMP) and of course negotiations for the stand-by arrangement during 1993 itself. The World Bank took a role through (1) the delivery of technical assistance for UNDP projects on macroeconomic management, including an influential seminar, “Strengthening economic management”, run by the World Bank’s Economic Development Institute (EDI), and attended by many senior government officials; (2) the outputs of economic and sector work (ESW), notably the reports in 1991 and 1993; and (3) the continuity provided by the Country Economist, in place for five years, who built up a close relationship with many officials.

It was not only the IFIs who were engaging in these types of activity (e.g. technical assistance, seminars, training courses and study tours). Donors already engaged in the country, such as France and Sweden (discussed in more detail below), also did so, as did relative new comers, such as the UK, once their bilateral programmes began.

Policy dialogue since 1993

With the end of the US veto in 1993 formal policy dialogue could begin. Central to this process is the Policy Framework Paper (PFP), which covers a three year period and is drawn up by IMF and World Bank staff in consultation with government; the policies therein provide the framework for specific loans from the IFIs. Two PFPs have been produced for Vietnam, dating from October 1994 (covering 1994–97, and so both ESAF and SAC) and February 1996 (covering 1996–98). The first of these contained 101 policy measures and the latter 124, though each credit contains only a sub-set of these: for example, SAC contained only 10 legal covenants. Disbursement of these credits is tranching, each tranche being conditional on satisfying certain conditions: SAC had to be extended twice (by nine months in total) owing to delays in completion of the PER, PIP, equitisation plans and portfolio audits of two of the state-owned commercial banks.¹³ A second SAC has been under

¹³ The second tranche was released before the second of these audits was completed, a waiver on the condition being obtained from the Board of the World Bank.

preparation since 1994, but to proceed further a new PFP and agreement with the IMF are required.

The first ESAF operation, which followed on from the one year stand-by arrangement, was not completed. Although scheduled over a three year period, annual agreements are required for disbursement to continue. No such agreement was reached in 1997 and so no funds were made available during that year. During 1998 talks have continued to try and agree a PFP, but so far (August 1998) without success.¹⁴

Other donors usually disburse their programme aid in relation to the IFI programmes. Specifically, an IMF operation must be in place and the donor may then establish a formal link with IFI conditionality by joint or parallel co-financing, or by disbursing according to an independent judgement of country performance in implementing reform.¹⁵ Some donors may establish their own sets of conditions, though this is rare for bilateral agencies. Although only balance of payments support is formally attached to conditions, most donors have stepped up their aid programmes considerably since 1994 (see Chapter 2).

The current impasse means that Vietnam has not received substantial balance of payments support since 1996. But, as mentioned in 2.3, it does receive commodity import support from Germany and non-project grants and loans from the Japanese, all of which are not subject to policy conditions. The Asian Development Bank (ADB) has two sector programme loans¹⁶, for the agricultural and financial sectors. This is possible since ADB rules require an IMF programme to be in place for programme aid to be approved, rather than disbursed, and the second programme was approved the week before the last ESAF disbursement in 1996. It is important to underline that Vietnam does continue to enjoy high levels of project aid. Given the availability of this forex (plus FDI and rapidly growing exports), the leverage given to donors by withholding PA is rather less.¹⁷

In addition to the conditionalities laid out in the credit agreements the donor communities express their concerns through regular (usually annual) Consultative Group meetings. The first of these, called an International Donor Conference, was held in 1993 and these meetings have been held under the CG label each year since then (in 1998 a “mid-term CG” was held in Vietnam also). The record of these meetings show that the donor community has shifted from whole-hearted endorsement of Vietnamese performance to disquiet over

¹⁴ The most recent Article IV consultations were concluded in May 1999, at which time a number of conditions were still outstanding for an ESAF to be considered.

¹⁵ In cases where an independent evaluation of performance is intended to be made in practice disbursement follows the IFIs.

¹⁶ Sector programme aid means that the policy conditions relate to a specific sector, though the funds themselves are general balance of payments support.

¹⁷ The argument goes both ways. Donors do not have a strong interest in restoring PA to Vietnam since it is not a heavily indebted country. Evidence from several sources (including the country studies for this evaluation) bear out the view that the IFIs are more lenient on countries with a large debt burden (to the IFIs!).

both economic matters (the extent to which controls remain) and governance issues (ranging from budget transparency to human rights). Donors also have bilateral aid talks and may exert influence on government policy through a range of formal and informal contacts, including the role played by expatriate advisors (which are discussed in the case of Sweden in 3.4 below).

How important has policy dialogue been?

All the usual structures of donor policy dialogue have thus been present in Vietnam since 1993. But the implication of our discussion of the nature of the policy making process suggest that the possibilities for effective conditionality through the usual channels are low. Consider first the formal policy dialogue. In fact Vietnam has not been subject to a great deal of policy conditionality of this nature. The SAC contained only ten conditions, only two of which required actual policy changes to be implemented. The other eight were for government to prepare plans or legislation. As discussed above, requirements to pass legislation are likely to be successful but should not be confused with implementation. The uncompleted ESAF programme focused on macro stabilisation, rather than structural reforms, though stabilisation was achieved by the time agreement was reached with the IMF. The two ADB programme loans contain rather more conditions, but very many of these are of a technical nature (such as creating a system for clearing cheques) rather than deep-seated reform (the “crisis” donors now argue to be inherent in the structure of the financial sector was not anticipated at that time).

The main features of the system, described above, which suggest a small role for conditionality are the wide-spread process of consultation and consensus, and the related strong internal dynamic given by its participatory nature and responsiveness to pressures from below. Even if “government” agrees to a PFP, or even legal covenants in an adjustment credit, the process of consultation begins only once steps are taken to meet the condition. There is then a very wide-ranging policy debate, also on other issues, involving the various institutions, and in which the donor community has no direct input. These same considerations affect informal influence also. Elsewhere donors rely on influential people within government who may be sympathetic to the donor cause and support them or pressure them if there are sticking points. But as one donor commented, in Vietnam the prime minister may say “I entirely agree with you, but it isn’t up to me”.¹⁸ Similarly expatriate advisors often play a crucial role in both giving an insider view and as a point of influence. But expatriates working in ministries in Vietnam are not insiders in the way in which they are in many other countries: they do not write minister’s speeches or key policy documents. This discussion also presupposes that donors can accurately identify where to try and target their influence, but it is not even clear that that is so.

These same considerations place a limit on the informal channels for policy dialogue. The Vietnamese have their own agenda, and may turn to donors

¹⁸ He is reported to have said this at the 1998 mid-term CG meeting in Hue.

for advice (and indeed value this advice), but it is only one input to their discussions, and may not address all issues of concern. It is quite usual that advice from several donors may be sought on a single issue – a fact that has come to the fore in the privatisation programme, where Asian governments (including Japan) have given rather different advice to that proffered by the IFIs and Western donors. Vietnamese officials do not treat foreign experts with the diffidence they may expect (and the relationship the IMF was somewhat rocked in 1993 for this reason) and one advisor is quoted as saying that “Government officials often tell me that they can always ignore what I do” (quoted in Fabricis, 1998: 16). Underlying such comments is of course a suspicion of foreign influence, which is deeply rooted in the country’s history – it is not so many years since Vietnamese conversing with foreigners were interviewed by the police and very recently that English language signs were prohibited.

In other areas Vietnamese concerns may simply be different from those that traditionally occupy donors. In several interviews (e.g. Women’s Union, MOLISA and Bank for the Poor) questions about possible adverse social effects of reform prompted responses about Social Evils rather than income-poverty effects on which donors focus (though donors have taken on board some of these issues, such as AIDS).

Available evidence confirms our general argument that there are limits to the extent of donor influence. This same view was expressed by the Bank’s country economist in the first part of the 1990s by saying that donors may have made some things easier but not really the fact that they were done.¹⁹ This position is also recognised by the statement of one IFI official that single tranche credits should be used in Vietnam as it was not a situation in which multiple tranches were likely to be successful.²⁰ The pace and direction of reform is determined by Vietnamese politics. At times there may be agreement with the IFIs: for example the introduction of VAT – however, this will be done in 1999, not 1997 as envisaged in the first PFP. Moreover, the switch to VAT is strongly “owned” by the Tax Department, being seen as a requirement for the country, rather than a being done to satisfy the IMF. In other areas the government less readily acquiesces to IFI conditions. Kokko (1997) records that after the condition in SAC to reduce the maximum tariff to 60 per cent had been satisfied several officials maintained that the maximum was still 100 per cent and that higher levels were certainly introduced during 1996 (100 per cent on clothing). In recognition of these sort of problems, the ADB refrained from including the abolition of the quota on rice exports from its conditions, even though this may be seen as the ultimate objective, and required instead an indicative minimum export price rather than a mandatory minimum (and even with this condition there have been problems).

¹⁹ Interview with David Dollar, October, 1998.

²⁰ Single tranche operations disburse once the credit agreement is signed and so effectively are payments against reforms already carried out, whereas multiple tranche operations required pre-agreed conditions to be satisfied for later disbursements. Single tranching is therefore *ex post* conditionality, currently advocated by many critics of the workings of *ex ante* conditionality.

The picture is the same if political conditionality is considered. Political reforms have occurred in recent years – but this has been in response to domestic pressures rather than external conditions. Donor pressure for human rights falls on deaf ears: the issue ranked high on the donor agenda at the 1997 Tokyo CG meeting, but a senior government official later said the meeting had been a success precisely because human rights was not mentioned.

All this is not to say that donors cannot play a useful role in the reform process, but that that role is not as they would usually, or possibly like to, conceive of it. As already explained, decision making in Vietnam draws on a wide range of opinions and then moves to consensus. Donors can input ideas to these debates, both through their own studies but probably more importantly by exposing Vietnamese policy-makers to a range of ideas and experiences through training and study-trips. On this view the donors can be seen to have played a role in reform even before the advent of formal conditionality, with Sweden being (with UNDP) the notable actor in this regard. It is to the Swedish experience that we now turn.

3.4 The role of Sweden

Sweden took a strong pro-Vietnam line during the war and continued to support the country once most donors stopped. Has this history resulted in a “special relationship” and, if so, has this relationship been exploited to allow Sweden influence on policy?²¹ Certainly Vietnamese interviewees are keen to suggest such a special role. Such a stance may be expected in speaking to evaluators working for Sweden!, but the argument is often added that Sweden is different from other donors as it is not seen as pursuing its own interests. What does experience show?

Following from the argument developed in the last section – that influence in Vietnam is most likely to be had if dialogue is of a suggestive (or reflective) rather than directive nature – there have been five main channels through which Sweden has influenced policy: (1) systemic effects from the evolution of CIS; (2) publication of regular economic studies; (3) related events, such as seminars, training and study visits; (4) technical assistance (both experts and training); and (5) projects.

As described in section 2.4, the system for the utilisation of Swedish programme aid evolved over time. This evolution was an important opportunity to engage the government on issues relating to the forex and financial markets, and to provide support to developing systems enabling institutions to behave in a more market-oriented manner (for example the technical assistance given to the commercial banks for them to handle the forex sales). This point was emphasised very strongly in the 1992 evaluation of Swedish programme aid:

²¹ We have been told that Sweden’s position enabled it to act as a go-between in the ending of the US embargo, but have not been able to document this role.

Much the most interesting feature of Sweden's CISP in Vietnam is how the programme has evolved over time. The most important reason why the CISP should be continued for the time being – albeit on a smaller scale – does not relate primarily to the shortage of foreign exchange but to the opportunities for mutual learning provided by the negotiation of the modalities of the programme and the monitoring of its subsequent performance. In the absence of a Policy Framework Programme (PFP) or Structural Adjustment Programme (SAP) negotiated with the Washington-based international financial institutions, negotiations around the design of the CISP provide an acceptable forum for arriving at conditionalities over a limited range of policies and procedures that can clearly be shown to be relevant to a legitimate Swedish concern that their foreign aid should be efficiently spent and extended in a form that would drive forward the process of economic reform rather than delaying it..... [In] the formal absence of IMF and WB adjustment programmes, [and] given also SIDA's active and long involvement in Vietnam, it is not an exaggeration to describe Sweden as being at the cutting edge of the policy dialogue mainly through the negotiations it conducts around the modalities for operating the CISP (Faber, 1992: 4 and 50).

Secondly, there has been a series of annual studies since 1990, and even other work commission before that; e.g. the first of a number of studies by de Vylder and Fforde (1988). The preface to the latter of these, written by SIDA's then Assistant Director General who was later to become an Ambassador to Vietnam, explicitly states that one purpose of the study was “to be a second opinion on the economy to the Vietnamese authorities in their search for solutions”. The country economic reports (formerly called the macroeconomic studies) have had a relatively high profile in Vietnam – partly owing to their promotion (including at on stage T-shirts with the title of the latest report) – but also as their content has at times caught the mood of the policy debate. This last statement certainly seems to apply to the three most recent reports authored or co-authored by Ari Kokko and which have argued the case for further liberalisation. These reports were well-known amongst the donors, but adopted even more fervently by the “young turks” amongst the community of Vietnamese economists who have most fervently adopted the cause of liberalisation. The Fforde and de Vylder volume, *From Plan to Market*, which was produced with Swedish support, remains one of the key texts on the Vietnamese economy, and was at one point banned by the authorities, which is a (perversely) a good indicator of importance if not influence.

Linked to these various publications have been seminars for discussion and training, which are an important means of disseminating ideas. Training has also been a component of technical assistance for economic reform. In the 1990s Sweden has had to projects that have deliberately played this role: Direct Support to the Economic Reforms and Strengthening the Rule of Law. The former has included support to tax policy and administration, courses at the National Economics University, and co-operation with the General Statistical Office and the Central Institute of Economic Management (CIEM). In addition to more formal training there have been many study visits by Vietnamese officials to Sweden, including: the Minister of Health, to study

and discuss Swedish experiences in health financing; the Vice Minister of Culture and Information to study media and cultural issues; a delegation from the Prime Minister's Research group on Economic and Administrative Reform, to discuss issues related to the reform agenda; a delegation from the government and the party, to learn about popular movements and the NGOs as input to legislation; and the Vice Minister of Construction received honorary doctorate at Lund University.

Influence may also be exerted through projects where this is not the primary intention, either through explicit conditions attached to project implementation (tariff reform in the energy sector is a common example) or from systemic effects, particularly in the case of large projects. Between 1975 and 1990 SIDA put SEK 2.8 billion into the Bai Bang project, making it Sweden's biggest aid project (and almost certainly the biggest in Vietnam). The evaluation of this project makes a strong case that there were systemic effects from the introduction of the Scandinavian management model. Most of the features of this model were that of capitalist management: i.e. autonomous decision making at the level of the firm in accordance with the profit motive, but also with a "Scandinavian human element". Spill over effects stemmed from four sources: (1) direct effects on other firms as Swedish exports provided advice to managers at other mills, who also made visits to Bai Bang; (2) indirect effects on state enterprises who looked to Bai Bang as an example to follow, especially once changes in legislation from 1989 gave them the autonomy to do so; (3) movement of trained managers from Bai Bang to other enterprises (although the evaluation only mentions this effect with respect to blue collar workers) and (4) : "it is... likely that the operation of the model at Bai Bang influenced the direction of reforms implemented under *doi moi*" (CIE, 1998: 84) since the Vietnamese institute used as the counterpart in management training at Bai Bang was at the same time involved in drafting key legislation for state enterprise reform.

A convincing case can thus be made that Sweden has been active in utilising various channels of policy dialogue, and in ways that may be expected to work well in a Vietnamese setting. We would re-emphasise that the appropriate form of policy dialogue appears not to be to lay down conditions to be followed, but to facilitate debate around issues and policies. This model has worked in the past in Vietnam and seems the most likely to work in the future.

Chapter 4

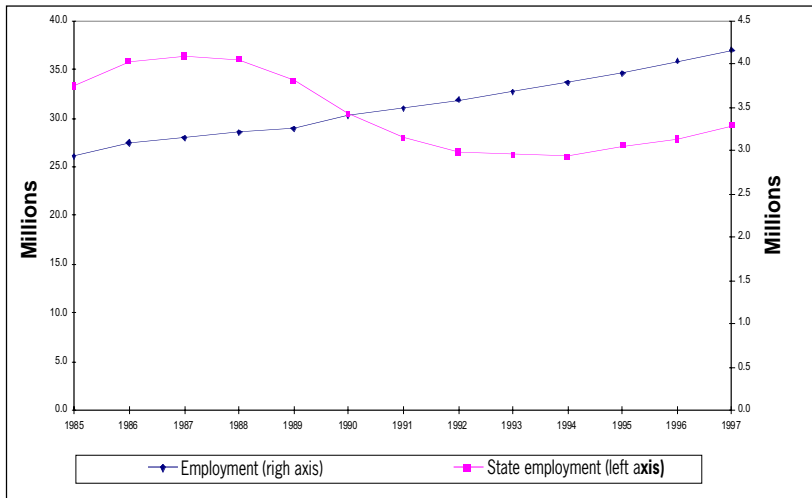
Socio-economic development in the period of reform

4.1 Macroeconomic performance

As documented in section 1.1 there is no doubt about Vietnam's success at the macroeconomic level. Growth was around 5 per cent in the 1980s and has exceeded 8 per cent each year since 1992. A measure of stabilisation was achieved in the late 1980s and, then, perhaps most remarkably, the re-emergence of hyper-inflation was combated with a successful stabilisation programme whilst accelerating growth. This strong growth performance has been accompanied by a continued expansion of employment (Figure 4.1). From 1985 to 97 the labour force grew by 42 per cent, which compares with population growth of 30 per cent over the same period. This employment growth has thus swamped the, admittedly steep, decline in state sector employment from the mid-80s (although this decline has been reversed from 1993 – Figure 4.1). Real wages have risen in the state sector: the average doubling from 1992 to 1996 (though only rising by 50 per cent for management positions).

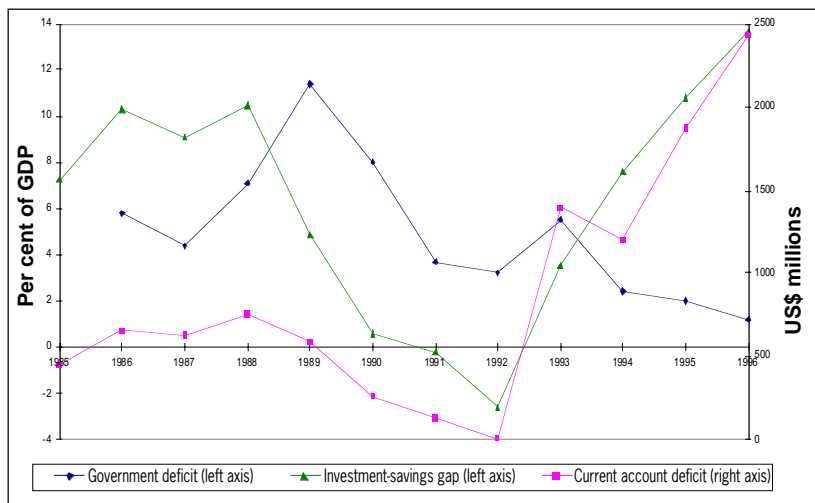
The areas of common concern about Vietnamese macroeconomic performance are the current account deficit, the budget deficit and the investment-savings gap. For example an ADB report stated that: “one weak spot that must be closed is the country's huge resource gap... while the savings ratio increased, it has not been able to keep pace with investment demands” (Asian Development Bank, 1998: 110 and 111). However this point of view ignores the fact that these deficits are driven by the high level of inflows: foreign investment, remittances and aid. A country with large inflows must have a current account deficit – hence in 1992 when there were practically no inflows then imports and exports were roughly equal. The same point may be made with respect to aggregated investment and savings. Subject to the private investment-savings balance, this same relationship should hold for the government deficit. However, this relationship is complicated by the fact that

Figure 4. 1 Employment trends, 1985–97



not all aid passes through the budget, which partly explains the rather different picture shown by the government deficit – this picture is also different given that the government has sought to stabilise the economy which may also mean that some aid has not been spent, and so is deficit-reducing rather than increasing.

Figure 4. 2 Current account and budget deficits, 1985–96



But in order to fully understand how the economy has grown, and what have been the implications of this growth for the welfare of the Vietnamese people we need to look beyond these aggregates to the sectoral level. This we do in the remainder of this chapter.

4.2 Supply response

It is obvious that economic reform and liberalisation have led to a supply response in the Vietnamese economy. The main question in this part is whether further reforms as proposed in policy dialogue will lead to a further supply response. The main conclusion to be drawn is that there may be reasons to doubt this, albeit that such reforms may have merits from the point of view of sound financial management and economic rationalisation.

The supply response is discussed under two headings: agriculture and manufacturing. This leaves out two important sectors in the Vietnamese economy: oil and the informal sector. Vietnam's emergence as an oil producer and exporter coincided with economic liberalisation. The exploration and exploitation of the oilfields is in the hands of joint ventures in which the state is dominant. Russian companies are important partners. There is, however, no precise information on the growth and management of this sector. Nevertheless, it is doubtful whether liberalisation of the economy has a major impact in these sectors. They are mainly driven by the perceived movement of world prices. The service sector will be discussed. It is obviously important and an important growth sector: between 1990 and 1995 the number of people employed in private trade, alimentation and services grew from 836,000 to 1,177,000. There is however not the information to ask sensible questions about supply responses which may result from further liberalisation.

Observation of everyday life in Vietnam shows immediately its importance: trade, restaurants, craftsmen etc. are abundant. This vibrant economic activity is obviously a result of liberalisation. However, a large part of the sector is informal and poorly documented. It is not possible to disentangle which actual economic activities this growth caused to take place and this is crucial in judging its economic importance. An important issue, for example, is whether there has been a crowding out in this sector resulting in the same output being produced by more people or genuine growth in output. There is no answer to the question whether the informal sector is mainly an urban phenomenon. For example: State owned enterprises have remained involved in the inter-regional rice trade by default; a class of inter-regional traders has failed to emerge. However, it should also be pointed out that inter-regional trade in rice has only recently been legalised and that SOEs, acting as autonomous enterprises, have the capacity and infrastructure to conduct this trade so as to make it a difficult market to enter.

Nevertheless, since 1992 services is the most important sector. Table 4.1 shows that the proportion of the industrial sector in GDP remained relatively stagnant and that agriculture is relatively in decline (though maintaining substantial real growth). Throughout the 1990s all three sectors show rates of growth, but these are the greatest in industry, followed by services and agriculture respectively. The base from which these sectors grew differed, which explains why these different growth rates did not result in more dramatic changes in the composition of GDP.

	Agriculture, forestry and fisheries	Industry and construction	Services	Total
1985	40	27	33	100
1986	38	29	33	100
1987	41	28	31	100
1988	46	24	30	100
1989	42	23	35	100
1990	39	23	39	100
1991	41	24	36	100
1992	34	27	39	100
1993	30	29	41	100
1994	29	30	42	100
1995	28	30	42	100
1996	27	31	42	100
1997	26	31	43	100

Sources: General Statistical Office Statistical Yearbook 1996 and 1997.

Much of the debate on the Vietnamese economy is framed in a distinction between a private sector, which may be subdivided in to an informal and formal sector and state owned enterprises. Further liberalisation is seen as the major mechanism to unshackle the private sector which will lead to an increased supply response. The difficulties of such a perspective are twofold. As already stated one is that little is known about the informal sector. The other problem is that in the Vietnamese context the difference between the private and the state owned sector can often be blurred as argued above. Official statistics will, for example classify joint ventures between foreign investors and state owned enterprises as wholly belonging to the category of foreign invested sector.

Agriculture

There is no doubt that decollectivisation is a major explanatory factor for a huge supply response in Vietnamese agriculture. (Table 4.2 documents agricultural reforms in more detail). The big breakthrough in this process took place in 1988 when the household was recognised as an economic unit that can lease land on a long-term basis. The land law, promulgated in June 1993, is the logical conclusion of that process. It gave farm households more rights over their land and extended the period of tenure to 20 years for annual crops and land used for aqua-culture. The lease for land under perennial crops, which require more long-term investment, was extended to 50 years. Under this law farm households can “exchange, transfer, lease, inherit, and mortgage the land use right”²². It also gave a right to renew the lease, provided that the law has not been violated. The most important restriction on land rights is, however, a limit of three hectares per household in order to ensure a

²² Chapter 1, Article 3, item 2.

fair land distribution to all peasants and to avoid undesirable speculation in land. The People's Committee is the authorised body which grants farm households certificates of the right to use land, so that households can implement their rights.

The results have been dramatic and can be best illustrated by rice production, which is the main crop in Vietnam. The crop has also a highly symbolic importance because food shortages were a major reason for the 'fence breaking' preceding the onset of reforms in 1981 and the persistence of reform in 1988. Vietnam was still a rice importer in 1988, but an export of 1.4 million tons of rice in 1989 turned the country into the world's third rice exporter. It has retained that position since then, with the exception of 1995 when it slipped to fourth place. While food production grew quickly in 1988 and 1989, by respectively 11.5 per cent and 9.9 per cent, the rates of growth were even higher for rice production alone: 12.6 per cent and 11.7 per cent. In the decade 1988–97, rice production grew by 5.6 per cent annually, which was not only due to more extensive cultivation – an annual growth of 2.4 per cent in sown area- but also a growth in productivity of 3.1 per cent annually (Men, 1997).

The rapid growth of rice production has not only raised the consumption of food per capita and established national food security, but also was essential for macroeconomic success: it helped to bring inflation down and rice exports since 1989 are a major source of foreign exchange. In 1997, Vietnam became the world's second largest rice exporter with the amount of exported rice of 3.56 million tonnes; this was superseded again in 1998: 3.7 million tons. Rice exports grew by an average of 49.7 per cent annually for the 1989–1997 period. Rice thus contributed to a considerable degree to the growth in exports of Vietnam, albeit that the share in exports is declining: for example 10 per cent in 1997; 11.2 per cent in 1998 as compared to 27 per cent in 1989 (Men, 1997 and VET, December 1998).

Table 4.2 Agricultural Reform Process 1979–1998²³

Policy Measures	Objectives	Main Features	Impacts
The sixth Plenum of Party 1979 on 'some urgent problems in improvement of economic management'.	to encourage all economic units to fully utilise available resources for an output increase to help overcome the economic difficulties and the food shortage.	(1) Recognising the importance of economic incentives for economic development; (2) Widening the autonomy for economic units; and (3) Accepting factors of a market economy like free marketing and market prices.	Some agricultural co-operatives experimented contracting out land (not only idle land) to members for family production. Food production recovered and grew again.
The Directive #100 of January 1981 on 'Output contract to labour groups and individuals'.	to provide more economic incentives to farmers and hence encourage them to use rural resources more efficiently in order to generate much more output for the nation to escape the food crisis of 1980	The co-operative contracted land to the farm households against a certain amount of output quota to be delivered back. It kept the overall control over the production process. The income distribution regime changed from per head quota to labour base.	Farmers had more freedom in allocating family labour and disposing excess output after delivering output quota. Farmers' income improved in both terms: kind and cash in the first years after the contract implementing.
The 1983 Agricultural Tax Ordinance	to uniform the tax base country-wide for equity and rationality; and to encourage farmers replot fallow left land in use and expand crop areas extensively and intensively.	Agricultural tax focused on the land quality, area and average yield per hectare rather than just area and output as previously. The tax was in paddy and the rate was fixed for five years at about 1.0% of the average output. Reclaimed land was tax free for 3 to 5 years.	Farmers reacted positively to capture the new incentives. Fallow land was again put in use and more land was reclaimed for cultivation of both annual and multi-year crops. The total sown area recovered and increased.
The 1986 "Renovation" or "Doi Moi" Programme	to surmount the economic and social crisis and stabilise the macroeconomy; and to transform a basically centrally planned economy to a market oriented economy with state regulation.	Official recognition and confirmation of a multi-sector economy with the co-existence of five economic components state, state-capitalist; capitalist, co-operative and private sector. The state regulation and leading role of the state sector were emphasised.	The economic rethinking process started but no marked change took place in the practice. The combined result of an inappropriate incentive system and natural calamities caused a slow-down and stagnation in agriculture.
The 1987 partial food trade liberalisation	to smooth the food flow country-wide, and create a national food market under the state control to meet the planned food consumption targets.	Abolition of the policy of food self-sufficiency at the district level introduced in the late 1970s. Only state companies were allowed to ship food from one province to other province and regions.	The development of food production in the surplus regions was encouraged and food imbalance was reduced country-wide. Transaction costs were greatly reduced.

²³ Table prepared by Ngo Thi Men.

<p>The Resolution #10 of 1988 on "Renewal of economic Management in Agriculture" and the Resolution #6 of 1989 on confirmation of the farm household as the basic economic unit in the rural economy.</p>	<p>to fully liberalise productive forces and reorganise production and management for a rapid agricultural growth in order to overcome the food crisis in 1987 and famine in early 1988; and transform the existing backward and a basically mono food agriculture to a diversified and commodity based agriculture.</p>	<p>Co-operatives contract out land to farm households on a long-term basis of fifteen years for annual crops, and forty years for multi-year crops. Means of production were also either rented or sold to the farm households. The farm household is the basic economic unit in the rural economy while the co-operatives act as supporting units. Agricultural tax and irrigation fee are the only farmer's obligation to the government. The output quota is so to fixed that farmers can get at least 40% of the average output and kept stable for five years.</p>	<p>The farmers gained greater control over their economic life and the coercive impact of the co-operatives were eliminated. Collective agriculture quickly lost its meaning. Land, labour and financial resources have been more efficiently allocated and utilised. A very strong supply response reemerged particularly from the food/rice farmers. Private food marketing was explicitly recognised. The food crisis ceased.</p>
<p>The 1989 radical economic reform with price and trade liberalisation</p>	<p>to unequivocally transform the national economy to a market oriented economy by making an end to the subsidy regime.</p>	<p>Most macro and micro prices were liberalised. The exchange rates were devalued to a realistic level. Real interest rates were kept positive. The internal trade was liberalised. The private sector was allowed to start business in all industries except the entry to the international trade of some national strategic goods; such as rice and fertiliser.</p>	<p>Agriculture benefited much from the reform and grew rapidly. Rice sector made the remarkably high growth, partly due to the favourable weather, making Vietnam the third world largest rice exporter after three decades of being a larger food importer. Farmer's income increased and rural living conditions have improved absolutely. However, negative social effects are also on the rise.</p>
<p>The gradual reform in the banking system towards development of rural credits by establishing the Bank for Agriculture (VBA) in 1990, the People's Credit Funds (PCFs) in the years 1993-95, and the Bank for the Poor (VBP) in 1995, and the authorisation for lending to rural households in 1993</p>	<p>VBA: to meet the growing needs for rural credits of the farm households, rural traders and agribusinesses for increasing investments; PCFs: to mobilise idle funds and provide credit services to households and businesses; and improve the local assess businesses; and improve the local assess for borrowers and savers; VBP: to contribute to hunger eradication and poverty alleviation.</p>	<p>The VBA at first took over the branch network of the SBV in the rural areas and later developed its own networks. Collateral is needed for granting credit. Land use right certificates are commonly used as collateral. Mass organisations (Joint-liability groups) are widely used at the retail level to distribute and collect loans in order to reduce transaction costs and risks for the VBA. PCFs are member-owned organisations operating under the principle of cost-covering. VBP is a non-profit bank operating based on the VBA network and getting VSB's support for covering the low interest rates.</p>	<p>Increasing number of farm households gets access to the formal credit system which helps sustain and expand agricultural production, develop processing, storage and transport capacities and speed up the commercialisation of agricultural products, and market these to the domestic and international markets. The private credit share rose rapidly from 10% in 1991 to 82% in 1995. The VBP and PCFs also help many of the poor in the rural areas escape from hunger and impoverishment.</p>

<p>The 1993 land law and the 1993 land use tax ordinance</p>	<p>to provide farm households more rights over the contracted land and guarantee them a stable and long-term land tenure in order to encourage long-term investment in land improvement, further reclamation of new land and more efficient allocation and utilisation of agricultural land.</p>	<p>The farm households can exchange, transfer, lease, inherit and mortgage land use right. The land tenure was extended to 20 years for annual crop and 50 years for multi-year crop. The per farm household land is limited to three hectares for annual crops. Agricultural land use tax was reduced from about an average of 10% to 7% of the yearly output. A further tax exemption is applied to newly reclaimed land for multi-year crops.</p>	<p>The land fertility has improved through more investment contributing to an increase in yield of most of the crops. Moreover, the total sown area has increased; especially that used for multi-year industrial and export crops. The two have contributed to a relatively high and sustainable growth in the sector since 1993.</p>
<p>The establishment of the Price Stabilisation Funds (PSFs), April 1993</p>	<p>to support agricultural producers and consumers to stabilise their income during the period of sharp price fluctuations.</p>	<p>The funds were founded by extracting the so-called excess profits obtained by exporting or importing companies and advantaged enterprises. The use of the funds is decided by the government for subsidising interest rates on credits given to the SOEs for output procurement at times when farm gate prices fell sharply and subsidising transportation costs for food and fertiliser to be shipped and sold to the remote, food deficit and disadvantaged regions.</p>	<p>The PSFs have to a certain extent helped mitigated the price fluctuation in some input and output markets. However, the result has not been as positive as expected as the procedures for releasing the funds is often complex and not timely. In addition, the SOEs are usually not those who directly buy and sell agricultural outputs and inputs from and to farmers; beneficiaries are not really matched.</p>

The importance of rice as compared to other crops as well as to other food crops is obvious from Figure 4.3 which compares the sown area as well as from Figure 4.4 which compares output of rice with that of other food crops. The time series of the latter ones are highly fluctuating. This is typical for peasant crops, because low technology makes crops more sensitive to climatic factors. One other food crop seems however to become rapidly more important: maize. The average yearly output of maize was just over one million tons in the decade 1988–97 while in the preceding decade 1978–88 it was only about half a million tons. This is important as rice cultivation mainly takes place in the two big deltas: the Red River Delta and the Mekong delta and an increase in maize would suggest growth in the output of food crops outside these areas.

Figure 4.3 Total sown area and sown are by crop, 1980–96

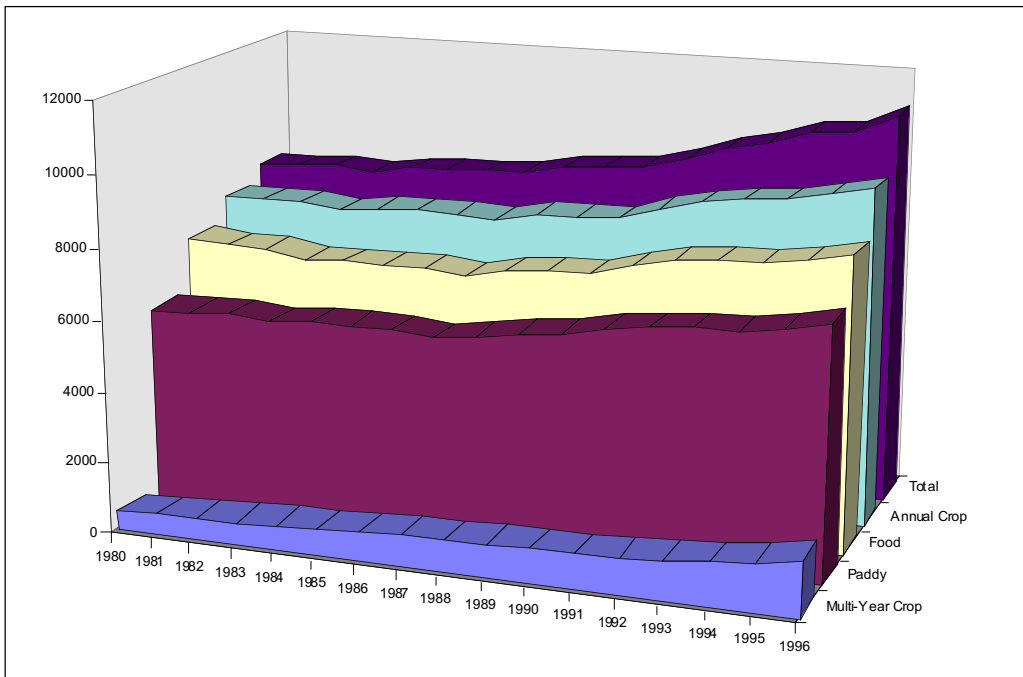
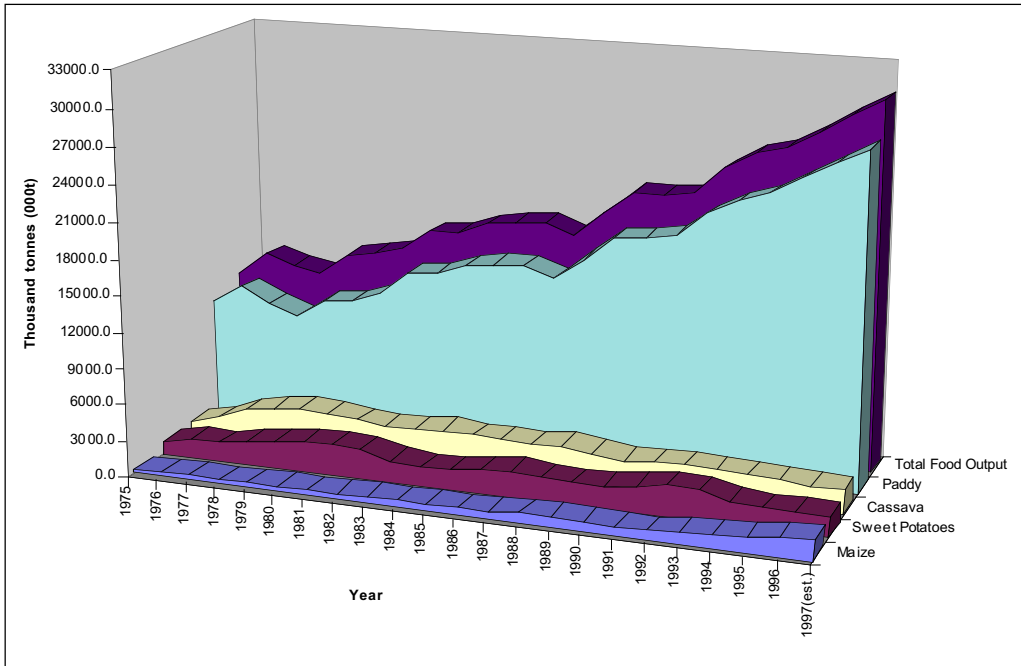


Figure 4.4 Food output (by crop)



The output figures of the crops called industrial crops in Vietnamese terminology provides more evidence of the geographical breadth of the supply response. Coffee, mainly cultivated in the highlands of central Vietnam in between the two deltas, is the major agricultural export earner after rice. In the decade 1988–97 production grew from 0.3 million tons to four million tons. The production of coconut, rubber, tea and cashew nuts also increased by huge percentages. All crops, except for coconut, are for the largest part exported. The designation of industrial for these crops is understandable as these crops tend to be grown on big plantations, but in Vietnam output rose especially after contracting parts out to peasant households. Coffee yields increased fivefold after change of ownership in the decade 1988–97 and rubber yields increased two and a half times in that period (see Table 4.3).

Livestock is of relatively minor significance in Vietnamese agriculture, albeit that it is usually allotted 25 per cent of output in statistics. That reflects the importance of the water buffalo as a working animal in many peasant households. Cattle raising is, however often difficult. Land for grazing is in short supply, especially in the densely populated deltas. Nevertheless, in the decade 1988–97, the cattle population increased (25 per cent) as well as the numbers of pigs kept (51 per cent). Chicken rearing however, increased most (67 per cent). Fisheries must also be mentioned when discussing the supply response in Vietnam, as the volume of fish and shrimp exports increased in the decade 1988–97 two and a half times.

Table 4.3 Yields of Industrial Crops 1975-96 (yield in tonne per hectare)

Year	Tea	Coffee	Rubber	Pepper	Coconut
1975	0.4	0.5	0.3	n.a.	n.a.
1976	0.4	n.a.	0.5	0.9	4.2
1977	0.4	0.3	0.6	1.3	3.7
1978	0.4	0.3	0.5	0.8	4.2
1979	0.5	0.2	0.5	0.5	4.6
1980	0.4	0.4	0.5	1.2	4.5
1981	0.5	0.2	0.5	0.9	4.3
1982	0.5	0.2	0.5	0.8	4.5
1983	0.5	0.2	0.4	0.7	5.2
1984	0.6	0.1	0.3	0.6	4.7
1985	0.6	0.3	0.3	0.6	4.8
1986	0.5	0.3	0.2	0.9	4.5
1987	0.5	0.2	0.3	0.8	4.0
1988	0.5	0.3	0.2	0.8	4.1
1989	0.5	0.3	0.2	0.9	4.5
1990	0.5	0.8	0.3	0.9	4.2
1991	0.6	0.9	0.3	1.0	4.9
1992	0.6	1.1	0.3	1.2	5.6
1993	0.6	1.3	0.4	1.1	5.7
1994	0.6	1.5	0.5	1.4	5.9
1995	0.6	1.2	0.4	1.3	6.7
1996	0.6	1.3	0.5	1.4	5.1
1997(est.)	0.6	1.5	0.5	1.4	n.a.

Source: GSO Statistical Yearbook.

This is an indication of a wider trend: agriculture remains important in Vietnamese exports, albeit that its overall share in the economy is diminishing. The share of agriculture in GDP declined in the decade 1988–97 by 20.6 per cent, but the share of agriculture in exports declined by only 8.5 per cent. (Table 4.4). Vietnamese statistics do not always correlate with each other and these figures are difficult to compare with the most recent export figures for 1998, published in the Vietnam Economic Times. These show the diversification agricultural exports: Rice, US\$ 1.1 billion; Marine products US\$ 800 million; Coffee US\$ 550 million (VET, April 1999).

Table 4.4 Exports by commodity (US\$ million)

	Heavy industry	Light industry	Agricultural products	Forestry products	Aquatic products	Others	Total
1990	617	636	783	127	239	2	2404
1991	697	300	628	176	285	1	2087
1992	955	350	828	141	308	0	2581
1993	1014	527	920	98	427	0	2985
1994	1168	938	1280	112	556	0	4054
1995	1378	1550	1746	154	621	0	5449
1996	2085	2101	2160	212	696	2	7256

Liberalisation has undoubtedly led to a major supply response in Vietnamese agriculture, but it is not the only explanatory factor. In the period of collective agriculture and especially in the early eighties massive investments were made in agriculture. The driving force behind this was Vietnam's integration in the CMEA, the trading block of communist countries which was striving for autarchy. Investments in plantations of tropical crops – especially coffee and rubber – fit into this policy. A major factor in the increase of rice production is the investment in irrigation after unification of the country. At that time the intensity of rice cultivation in the Red River delta was already at its peak, but that was not the case in the Mekong delta in the South, where the government has invested in irrigation and where the supply response to liberalisation occurred. There would have been no supply response in agriculture without liberalisation, but the supply response that came was possible due to centrally directed investments in the previous period.

If investment is a necessary factor in the supply response which emerged in Vietnamese agriculture, then this supply response may soon exhaust itself. The share of investment in agriculture in total government investment declined from 21.2 per cent in the 1976–1980 period to 18.3 per cent in the 1981–1985 (Fforde and de Vylder, 1988; p.141). It rose again during 1986–1988, before the second wave of decollectivisation- to over 20 per cent but declined again to between 6 per cent and 7 per cent in recent years causing the share to fall to 13 per cent for the whole decade 1988–1997. Neither did agriculture share in the boom of foreign direct investment (FDI) since 1988. Only 3.9 per cent of total FDI was invested in agriculture (Men, 1997).

So, both public investment and FDI in agriculture are small. It is, however, highly unlikely that agriculture can grow at above 4 per cent per year, as it did recently, without much more investment than mentioned above. For example Quang (1998), as quoted in Men (1997), assumed that in order to make agriculture grow by 3 per cent to 4 per cent a share as high as 25 per cent or about 30 per cent of public invested funds is required and this has not been forthcoming. Therefore private investment within the rural sector would have to be considerable to make up the “shortfall”.

Investment is not only required for irrigation, but also infrastructure, and cash required for other agricultural inputs. On the latter, Jansen suggests however that it is not investment in infrastructure that drives increased output in the 1990s, but “the shift in responsibility to household farms in the 1980s resulted in a sharp jump in the efficiency of production. But this jump reflected a catching up; once efficient production was established, further efficiency gains levelled off and the growth of output became dependent on the increased use of inputs [e.g. fertiliser and seeds]” (1999: 17).

It is therefore not surprising that credit in order to overcome the seasonal cash fluctuations is important. The main rural financial institutions that emerged following the 1988 reform and 1993 land law are the Vietnam Bank for Agriculture (VBA), established in 1990, the People's Credit Funds created in between 1993 and 1995, and the Bank for the Poor which came into being

in 1995. These institutions serve the growing demands of farm households and rural traders who need money to do business in agriculture. The VBA gives not only credit to production households but it also provides credit to agricultural traders and agricultural processing units in both state and non-state sectors. Other sources of rural credits supporting agricultural development are the People's Credit Funds (PCFs), which are meant to act as mutual funds. Their interest rates are in general higher than those imposed by the VBA but much lower than those existing in the informal credit market or usury. The Funds have helped many households, who lack access to the VBA or need more credit than the VBA credit limit to operate efficiently. Together with the VBA and the PCFs the Bank for the Poor also helps provide small credit at lower interest rates to the poor in the rural agricultural areas. The latter aims particularly to help poor households to reach self-sufficiency in food production and to start earning cash through commodity production. The VBA is the hub of this network. By the end of 1996 there were 16 rural joint stock banks and close to 900 People Credit funds, both of these remain however dependent for their main sources of funds on borrowing from the VBA and the State Bank of Vietnam. The activities for the Bank of the Poor are administered through the branches of the VBA (Jansen, 1998: 18).

The growth of rural credit has been spectacular. The outstanding credit of the VBA was, in 1990, equivalent to 9.3 per cent of agricultural GDP; by 1995 that ratio has increased to 19.9 per cent. More importantly, the share of credit to agricultural production households had increased from 14 per cent of all VBA credit in 1991 to 79 per cent in 1995; the share of loans to agricultural state enterprises had dropped sharply. Nevertheless, there is a credit famine in rural Vietnam and just under half (47 per cent) of all rural households were indebted in 1992/93 and about three quarters (73.1 per cent) to other private individuals. (Jansen, 1998a p.18 and VLSS, 1994). The lack of collateral is a major stumbling block in expanding rural credit and this is especially a problem as there is a big backlog in granting certificates of the right to use land. After the land law had been in operation for five years, only 45 per cent of all households had been granted certificates. Rural credit seems therefore an essential ingredient of the supply response which has occurred so far and is a condition for further supply responses.

It seems beyond doubt that the agricultural sector in Vietnam is in need of more investment and some see further liberalisation as a prerequisite for that. This refers then in the first place to rice marketing and especially to the international trade in rice. The latter trade is a monopoly of SOEs that are allocated quotas. Such a system prevails only in this sector – which is by far the biggest in Vietnamese agriculture – and the international trade in all other commodities is liberalised. Private middlemen therefore buy from the farmer and can sell either to the general public throughout Vietnam or to the exporting SOEs. The latter therefore manipulate the price through demand management. In addition rice exports faced an additional tax, which has gradually been phased out. The net result is that rice prices within Vietnam

are depressed and the farm gate price is not considered to give adequate incentives.

Vietnamese rice consumers thus benefited significantly from a low rice price while a comparison with the world price shows what producers could get. Men (1997) estimated the percentage difference between the domestic retail price of rice (not the wholesale price) and the average world border price (not the country's border price but the Thai border price) to be 29 per cent. Domestic rice can thus be seen as under-priced by that amount. She compares that with the figure of 10 per cent suggested by David (1994;p.74) and IFPRI (1996:p.208) which mentions 24 per cent of export value.

Vietnamese rice consumers benefited thus significantly from a low rice price while a comparison with the potential world price shows what producers could get. This is reinforced by the impression that the terms of trade are moving against rice producers. Men (1997) is cautious about this. The evidence on the terms of trade of rice growers within Vietnam is not unambiguous, but it seems to be moving against them in recent years. The rice price grew by an annual average of 23.8 per cent over the 1989–95 period in nominal terms, but it fell by 6.5 per cent in real terms. This was partly compensated by a decrease in the fertiliser price. The exchange ratio between fertiliser and paddy fell from 3.5 to about 1.7 over the period 1991–95, but it deteriorated again during 1995–96 when the ratio became 2.2. A comparison of the rice price with the Consumer Price Index shows also a relative decline of the terms of trade. For example, in 1996 the rice price declined to 97.3 per cent while the CPI increased to 104.5 (VET, 1997). Jansen (1998a) also calculates deteriorating terms of trade for the agricultural sector as a whole since 1991.

This situation has obvious advantages from the vantage point of the national economy: it maintains food security and keeps inflation down. A low rice price does not only benefit the urban sector. About 53 per cent of those labelled poor in the Vietnam Living Standards Survey are net buyers of rice. As most of the poor live in rural areas, a considerable number among them produce rice as well. (VNLSS, 1993). Despite the fact that the farm-gate price was not seen as adequate there has been not only an increase in the quantity of rice produced, but Vietnam has also produced better quality rice.

There are reasons to doubt whether further liberalisation would result in higher prices at the farm-gate. Too little is known about the intermediate trade in rice to draw firm conclusions. SOE's are not only involved in rice trading by design, but also by default of emerging private marketing structures. However, until now, long distance rice movement from the rice surplus regions – the Mekong River Delta – to the rice deficit regions in the North has been regulated and co-ordinated by the government and performed by the SOEs. That did not result from a monopoly position, but from market failure. Private traders appear to be unwilling to risk trading nation-wide and have rarely been observed to operate beyond the distance of 400km (IFPRI, 1996). There is also a big shortage of handling capacity and post-harvest losses are therefore

large. The efficiency gains of private marketing structures have thus been limited. However the margins in the rice trade are large. Men (1997) estimates the margin between farm gate price and export price at 37 per cent in 1996 and this comes close to the margin of 35 per cent which David (1994) found in 1992.

Rice is a politically charged issue in Vietnam. Although there is reluctance to trade over long distances within Vietnam, this does not prevent a lively smuggling trade across the border with China if the rice price is higher there. The upward movement in price as a consequence led the government to reintroduce restrictions on inter-regional trade from July 1995-November 1996 and the illegal trade with China declined considerably. Price stabilisation can however also be argued for on rational grounds and there has been a price stabilisation fund since 1993. The rationale for this is twofold: first, Vietnam is a price taker on the international market and therefore the export price is very susceptible to price movements; second, the production of particular crops is strongly bound to particular regions in Vietnam. There is little mobility of production factors, which would enable producers to switch from one product to another. That argument counts for the other crops as well.

From this discussion the following conclusions may be drawn:

- Decollectivisation has led to major supply responses in Vietnamese agriculture.
- An additional explanatory factor in these supply responses is investment that predated decollectivisation.
- The supply responses resulting from these have reached their limit and further supply responses are dependent upon further investment.
- This has partly been forthcoming through the growth in agricultural credit to finance inputs.
- But on the whole, agriculture is a sector that has greatly contributed to economic growth and received little further investment in return.
- The agricultural sector in Vietnam – notably the rice sector – has received prices substantially below world market level and therefore subsidised other sectors.
- It is however doubtful whether further liberalisation will lead to a bigger supply response and may endanger macro economic stability (inflation) as well as food security.
- The marketing of agricultural produce is characterised by significant market failures. Intermediate trading networks tend not to arise, and function poorly where they do exist.
- There could thus be a significant role for state intervention to enable the emergence of an effective marketing system and to provide incentives for further investment in agriculture.

Manufacturing: a fast growing sector with great structural weaknesses

The industrial sector in Vietnam has achieved high growth rates in the 1990s. Despite the fact that Fforde (1997: 64) saw in the sector “the classical signs of the beginning of a cyclical slowdown”, the growth rate in industrial output in 1997 was still 13.2 percent, which was nevertheless somewhat lower than in previous years (1996; 14.1 per cent; 1995; 14.5 per cent). The growth rate of industry remained higher in 1997 than that of GDP by more than 5 per cent, also slightly less than in the previous years. Total employment in manufacturing has however, not risen, in 1991 – 3,394 thousand as compared to 3,395 thousand in 1995 – which is in part due to the restructuring of SOEs that was still occurring in the earlier part of this period. Constant employment with rising output is of course reflected in a large rise in productivity. Industry has also attracted a major share of foreign direct investment: 39.8 per cent of approved projects and about 30 per cent of actual investments. Only oil and gas had a similar share in approved and actual foreign investments. One particular sector of manufacturing – textiles, garments and shoes has become a leading export sector. Garments and textiles exports were only worth US\$ 20 million in 1990 and in 1997 this had risen to US\$ 1.3 billion in 1997. Shoes started from US\$ 5 million in 1992 and rose to US\$ 955 million in 1997. The sector takes second place after oil.

Nevertheless there are structural weaknesses in Vietnamese industry, which are seen by observers, donors as well as the Vietnamese Ministry of Industry (MOI). It may be best to formulate the latter’s vision first: Vietnam has a heritage of industries with outdated technology dating from the period of central planning. The open door policy brought in foreign direct investment and new technology, but that was to a large extent import substituting industry producing behind tariff barriers. The main export oriented industries are in garments and textiles, but these industries have few backward linkages. It can mainly be characterised as a ‘putting out’ way of doing business where only the labour in the last production stages is value added in Vietnam. Consequently there is a resistance to the removal of trade barriers as it could wipe out the old industries as well as the import substituting industries. The main mistake is seen as a lack of government direction in industrial development. Foreign direct investment was not channelled to areas where Vietnam needs most new technology – the heavy industry dating from the period of central planning – and to what are called support and service industries and may be better termed as creating backward linkages to industry in Vietnam. The call is for more centralisation to channel energies in those directions and the attempts to create a decentralised industrial structure at commune and provincial level is then seen as a mistake as more direction is needed.

The opposite view is that Vietnam needs a period of ‘creative destruction’. Much of the industrial growth has taken place in state owned enterprises, often in conjunction with foreign partners. The tax breaks given to them, as well as the favourable access to credits of the state sector and the higher prices

paid by consumers in a protected market are a long term loss for the Vietnamese economy. Liberalisation will lead to a cheaper cost structure of imported products and the survival of the genuinely profitable enterprises. (Fforde, 1997) A levelling of the playing field because the restructuring of state owned enterprises will lead to the burgeoning of the suppressed private sector. Kokko and Sjöholm (1997) have argued specifically in this context as well to aim at further development of small and medium enterprises at the lower levels as a main ingredient for a strategy in which the market can work. "An industrial environment with competition between many smaller SOEs would promote higher allocative and productive efficiency for several reasons" (ibid.). It would break the power of resistance of the big state owned enterprises to liberalisation; it would facilitate industrial diversification and it would simplify the monitoring task of local authorities forcing industries to reduce slack and inefficiency.

The nature of these arguments may best be illustrated through looking at some industries which exemplify the nature of industrial development in Vietnam.

Textiles and garments: spectacular growth but low value added

This sector shows a mixture of great success and structural weaknesses. This is shown to begin with in the difference in performance between the textile sector producing mainly yarns, fabrics etc. and the sewing sector producing garments. The first one grew in the period between 1990 and 1997 by 45 per cent but this is incomparable to the phenomenal rise of the confection sector, which rose almost fivefold: 495 per cent. Both sectors have been predominantly state owned, but that has been more and increasingly so in the textile sector (state share of gross output: 1990: 67 per cent; 1997: 70 per cent) than in the garment sector (share of gross output: 1990: 61 per cent; 1997: 55 per cent). Within the state sector a much larger part of the textile sector is centrally owned and managed (share of gross output: 1990: 24 per cent; 1997: 20 per cent) than in the garments sector (share of gross output: 1990: 59 per cent; 1997: 57 per cent). It is therefore not surprising that the growth of gross output in textiles is not as fast in the private sector compared to state enterprises (State: 1990–97: 38 per cent; Private 1990–97: 67 per cent) while the opposite is the case in garments (State: 1990–97: 446 per cent; Private: 625 per cent). The state has brought the centrally owned textile industry together in one strategic group – VINATEX – comprised of 55 companies, but it is not clear in how far this has resulted in a tight centrally controlled structure. The figures on the number of establishments in the industry tend to be contradictory, but it seems that a fairly decentralised structure operates. For example an article on the textile industry in Ho Chi Minh city -said to be responsible for 70 per cent of total output in the sector mentioned that there are thirteen state enterprises in the sector and 4000 non state enterprises while in the garment sector there are 17 state enterprises and 4,400 privately owned units.

There seems therefore to be no reason to see this sector as repressed; liberalisation and open door policies have led to growth in output as well as in

exports. The latter is especially the case in the garment sector, where exports multiplied more than fivefold in the period 1990–97. The export of textile fabrics is much smaller and shows a much more uneven export performance. Yet, at the same time the quality of this growth is in doubt. VINATEX said to use for example only 60 per cent of its capacity in July 1998 and the main reason is the inferior quality of its products which make it impossible to compete in international as well as on domestic markets. Vietnamese textiles have only a small domestic market share (one fifth) and it cannot compete with, particularly Chinese, imports (VEN 33). Another source mentions an even a lower market share (30 per cent) and “the remaining 70 per cent is met by goods smuggled from China, Thailand and Taiwan”. Local yarn is of poor quality and has a high wastage: “the garments made of domestic raw materials can only serve the rural market or armed forces. However the rural markets have been flooded by Chinese products “and resulted in the voluntary dissolution of many local textile and garment handicraft establishments” (VER 48).

The garment industry for export tends to be limited to only the last production stages and has few backward linkages. This is evident from the fact that the boom in garment exports was accompanied by a steep rise in the imports of textile fabrics, yarn and auxiliary materials for sewing. The sluggishness of the textile sector as compared to the garment sector is explained by outdated equipment in the former. There is not sufficient information on the rate and nature of investment in the two sub-sectors. If one compares the percentages of gross output which is said to be from the ‘foreign invested sector’ then this is slightly higher in the textile sector (1997: 17 per cent) than in the garment sector (14 per cent). The following comment is enlightening: “Generally the investment structure in the textile industry has remained irrational. There have been enterprises that just focused on borrowing to invest in modern and expensive equipment, but their poor management has led to finished products with high prices that are unable to compete with imported goods. Even loss making business performance or leaking of the state capital and assets, with typical examples of the Nam Dinh Textile corporation or Minh Phung Garment Company” (VER, 48) has occurred. The situation in this sector is therefore probably very uneven, albeit that there is obviously a vibrant export garment sector.

The garment sector may however, not be particularly profitable. That is partly a result of the few backward linkages, the fewer the stages in the production process, the less is the value added. Vietnamese industry also does not manage to penetrate the top end of the market. Another major factor is under-capitalisation: the industry is highly dependent upon bank credit, which is usually of a short-term nature. This would fit an industry concentrating on the last stages of production where turnover is high and each contract can be financed separately. Interest charges are therefore an important part of the cost structure. The main comparative advantage on which Vietnam has competed in this market is cheap labour and in this respect the upheavals in the Asian economies may put it at a disadvantage. Countries whose currencies

have devalued considerably – unlike the Vietnamese Dong – will have highly competitive labour costs now, which will squeeze profits further.

The economic turbulence in the region may affect the Vietnamese textile industry in other ways. Foreign investment in the sector has virtually all come from within East and South East Asia: Malaysia, South Korea, Taiwan, Japan and Hong Kong. There is no definite information of the sources for which the Vietnamese textile industry has subcontracted but it is most likely that this will also be for firms in this region. The destination of exports is about a third to the European Union, one third to Japan and the rest to other countries in the region like South Korea, Taiwan and Singapore. A much smaller proportion goes to the former countries of the Soviet Union and very little to the USA. Only the market in the EU is secure and it is likely that foreign firms may also like to produce in Vietnam for that market as they can profit then from Vietnam's import quota. High hopes are expressed for the US market, but access there may be dependent upon progress in the stagnating talks about trade liberalisation.

Motor vehicles and motorcycles: import substitution by joint ventures in a protected market

Import substituting industries have also expanded rapidly in Vietnam after liberalisation. Often these attract a considerable share of foreign investment and can be seen as a means for foreign firms to produce for the Vietnamese market behind tariff walls. The domestic market for motor vehicles is small in Vietnam, but motorcycles are highly desired and very numerous. The big brand names have all established assembly plants in Vietnam – the Japanese firms Honda, Suzuki, Yamaha, Kawasaki, the Italian firm Piaggio as well as a Taiwanese company. The Vietnamese government put conditions with respect to the domestication rate of the inputs used. Imports should move from Complete Knockdown Kits (CKKs) to Incomplete Knockdown Kits and after two years 5–10 per cent of components should be locally made which should rise to 60 per cent after five years. Production started in 1991 and reached an output of 70,000 motorcycles in 1997 by foreign investors, while an additional 3,000 were produced by state enterprises. In May 1997 the Vietnamese government halted the importation of fully assembled motorcycles and Complete Knockdown Kits.

This industry has therefore a protected market where demand is high. Yet, the industry has problems. The 1997 ban led to big price rises to which the government reacted by giving permission to import 100,000 CKKs in early 1998. The demand for these remained high and prices skyrocketed again. In the beginning of 1998 the price of a popular model rose by \$500 to \$2600 in a few months and the complete stock of 100,000 CKKs was sold out in June 1998. The prices of motorbikes which contained at least 10 per cent locally manufactured components remained stable and demand was not high for these; “the quality and design as well as prices of these bikes have not yet been accepted by local consumers”. (Vietnam News, 17/8/89) Capacity utilisation of existing assembly plants is poor. In 1998 capacity was projected at 900,000 motorbikes, while only four out of the six licensed joint ventures

were actually producing and aiming at an effective operating capacity of 200,000. Annual demand was estimated at 500,000 motorbikes a year.

The situation is even more confusing with respect to motor vehicles. No less than fourteen assembly plants have been licensed in Vietnam and eleven of those are operational. The big names are there as well, for example Mercedes-Benz, Toyota, Isuzu, Nissan and Ford. Output of assembled motorcars is small, a mere 6000 units in 1998. All production is reported to be financed by foreign direct investment, albeit at the same time as joint ventures are mentioned without specifying the amount of capital the local partners bring in. The car market in Vietnam has been expanding, but remains relatively small: the number of registered cars rose between 1990 and 1996 from 200,000 to 400,000. Figures for planned and actual planned and installed capacity to assemble are large, but actual production is small. For example the Ford plant is meant to have a capacity of 15,000 cars per year, but hopes to sell 500 vehicles in 1998. The most likely explanation for the situation seems to be that car manufacturers are jockeying for positions in what they see as potentially a big market through planning assembly in the protected environment. Relatively little of that may be realised. Their production is also limited by strict quota for the import of kits. Hopes on a speedy localisation of inputs or production for export seem unfounded. The import of fully assembled motor cars – as well as second hand vehicles – with which they have to compete in a small market continues.

Import substitution of this kind shows all the problems that are habitually associated with it. Backward linkages in the economy fail to establish themselves. Thus, manufacturing remains highly import dependent as foreign producers use it as a means to get access to a captured market, which is however less so in the case of motor vehicles than that of motor cycles. Products manufactured behind high tariff walls are expensive and cannot compete on quality.

Cement: outdated technology producing products that cannot compete in the region

Heavy industry was the priority area during the period of central planning. It is therefore not surprising that state ownership is most common there and it is here where one would expect most problems of outdated technology. The cement industry is a borderline case in this category, because it tends to be more successful as an import substitution industry than for example steel manufacturing. Transport costs of such a bulky product leads easily to a comparative advantage and it does not require the high quality specifications needed for backward linkages to more specialised industries as in the case of, say, machine tools. Economic growth has a necessary concomitant boom in construction and that should provide a ready market. Output of cement has grown considerably in the 1990s: in 1997, 7,475 thousand tons were produced as compared to 2,534 in 1990 (a rise of 294 per cent). Virtually all of it is produced in the state sector. Foreign partners and non-state sectors became involved only recently and then in a minor role (12 per cent in 1997). It is produced throughout the country in local vertical kilns under provincial management.

Nevertheless the industry is not competitive. Fforde (1997) writes about stocks being high in the industry and Vietnam Economic News talked about high stockpiles in 1998 as well (no.34). Cement imports grew rapidly in the 1990s, from a low base of 221 thousand tons to 1650 thousand tons in 1996. The Vietnamese government banned cement imports to ward off stiff competition from China and North Korea in 1997 but nevertheless there are complaints about cement from Indonesia and Thailand still widely available in the south of the country. The other countries in the region produce much more than demand (1.6 times) and Vietnamese cement is said to be four times more expensive than the regional price, which would probably dwarf the advantage with respect to transport costs. The devaluation and further slackening of demand in the region will reinforce these tendencies. At the same time major investments have streamed in and Vietnam is expected to produce 16,800 thousand tons in 1998. Government has reacted to that by halting further investment in the industry including 'the construction progress of the Haiphong, Hoang Mai and Tam Diep cement factories which domestic entrepreneurs have invested using foreign loans'.

Concluding comments on manufacturing

The main comment is that economic reform and trade liberalisation will imply a rationalisation of Vietnamese industry and thus a negative supply response, at any rate in the short run. The situation as described in the textile industry is applicable to footwear, another fast growing export industry: the assembly of electrical appliances and computers will show the same phenomena as the motorcycle and vehicle assembly industry. What happened in the cement industry will be fairly typical in the older industries. The general picture is one of, sometimes extraordinarily, rapid growth, but a growth of low quality. It is also a growth, which was to a large extent possible because of an interventionist state building high tariff walls and investing heavily.

A second conclusion is that there is no reason to believe that growth in manufacturing is hampered by a repression of the private sector. A recent survey of private manufacturing in Vietnam (Ronnas, 1998) found that enterprises had grown in income, assets and value added per worker since 1991. "Considering the short time span between the two points of observation, a mere six years, the transformation can be considered as quite dramatic" (ibid: 39). The main problems they faced were concerned with limited capital, lack of demand and too much competition, not interference of local officials, uncertainty of government policies and difficulties to get licences etc. Enterprises did not find governmental regulations and official attitudes to be a severe constraint, for the most part. On the contrary, about 61.7 per cent of the urban enterprises received some form of assistance from the government (ibid: 75). Further internal liberalisation might lead to a bigger supply response if it would improve access to capital. The overall level of indebtedness among the surveyed enterprises was not high, but the size of the debts was much larger among the recently established enterprises than among the old ones. "This suggests two things: Firstly that bank loans have increasingly become

available to non-state manufacturing enterprises and secondly, that loans are predominantly taken at the time of establishment” (ibid:12). The capital constraint has also to be seen in conjunction with the constraints seen in lack of demand and stiff competition: the question is whether there are many new outlets for such investments as a result of more bank loans. If the capital constraint is as big as it seems, then it is also doubtful whether the economy will easily mobilise the capital to take over the state owned enterprises.

Further liberalisation of external trade would undoubtedly lead to a drop in supply from the manufacturing sector. The complaints about smuggling, the importation of second hand goods and lack of competitiveness in the domestic market are virtually universal. The response of the Vietnamese government has usually been a further regulation of importation and outright banning of imports. Trade liberalisation may give access to foreign markets that are now relatively closed, notably the US market. It might also lead to large devaluations which would make Vietnam more competitive as compared to other countries in the region. Their increased competitiveness makes the future for Vietnamese industry particularly bleak.

Finally, trade liberalisation may bring by default the technological renewal that government intervention has failed to achieve. There are powerful arguments for further liberalisation of trade (Kokko, 1996; Kokko and Zejan, 1997a). The benefits for Vietnam of foreign direct investment producing for a protected local market are doubtful. Old industries producing low quality and expensive goods for which there is no demand are a questionable asset for a national economy. The Vietnamese experience with opening its doors to foreign capital and expanding in manufacturing has also not led to the technological transfers which are necessary.

The situation is in that respect bleak: A survey of the Ministry of Science Technology and the environment of 2,292 state owned enterprises showed 1,217 had imported outmoded equipment from 20 different countries. In 1,000 others, half of the equipment was battered. An investigation of 727 pieces of equipment revealed that 70 per cent of the equipment dated back from the 50s and 60s and one piece even to 1929. Half of the equipment was reconditioned and 10 per cent was past life expectancy. It is ironic that Vietnamese enterprises in textile, leather and seafood processing poured huge investment into importing outmoded technology which produced only low-quality products and polluted the environment. (Vietnam Courier, 16–22/8/98). The description of the situation at an anthracite mine is illustrative: “the Coc Sau mine uses a 30 year old conveyor belt system, and a mix of trucks from Russia, Japan and the US to move coal from the mine”. There was “no evidence of systematic planning in mine development, inadequate ventilation systems and poor safety standards”. (Financial Times 5/6/98). The Vietnamese case was not one in which the market was governed to create comparative advantage by a purposeful strategy in industrialisation. It is therefore difficult to see much benefit in the continuation of the present situation maintaining protection and banning imports. The question is whether a decimation of

Vietnamese industry could be avoided by the acquisition of technology in strategically chosen areas using regulation and state intervention.

4.3 Poverty in Vietnam

It is beyond doubt that the Vietnamese record in poverty alleviation is commendable, though concerns remain about the distribution of the benefits of growth. Everyday life in Vietnam makes the overwhelming impression of a society where life is getting better and that is borne out by other evidence. The overwhelming majority of communes in the Vietnam Living Standards Survey (VLSS) of 1992/93 (114 out of 120) said that the quality of life had improved in the past five years. A MOLISA survey of 1994 found that more than half of the respondents thought life had improved since 1990 (Jansen, 1997: 32). Such impressions are borne out by the calculations of Dollar and Litvack (1998), reproduced in Table 4.5. The poverty indices for 1993 are the actual data from VLSS – and using these data combined with information on growth they project past and future poverty measures under various assumptions about distribution. They argue – largely based on the Chinese experience – that the most likely scenario is that the Gini has risen from 0.30 in 1984 and will continue to rise to be 0.38 by 2000. Hence the poverty headcount was probably around 74 per cent in 1984 (the headcount is not very sensitive to distribution at such high poverty levels anyway), had fallen to 55 per cent by 1993 and will fall further to 34 per cent by 2000.

	1984			1993		2000			
Gini	0.24	0.30	0.34	0.38	0.34	0.24	0.30	0.34	0.38
Headcount index	77	74	76	74	55	14	22	27	34
Poverty gap	25.8	28.9	31.8	34.7	17.0	2.0	5.7	6.2	10.6
Poverty severity	11.0	14.5	16.2	19.8	7.1	0.4	2.0	1.9	4.3

Source: Dollar and Litvack (1998: 15)

However, such results are not considered a reason for complacency and the incidence of poverty in Vietnam since the onset of economic reform has been extensively analysed. The major document used in this respect has been the Vietnam Living Standards Survey of 1992/93 (VNLSS, 1994), which was the basis for a poverty assessment by the World Bank (World Bank, 1995). These results are extensively used by Jansen, (1997, 1998). Tuan Phong Don and Hussein Jalilian made a comprehensive overview also based on this survey as well as the General Agricultural and Rural survey and a study of the budgetary allocations. We also had access to a survey of vulnerable groups by Fforde (1998). Differential effects on various groups and in different areas play a major role in this literature. Finally, there is a recent regional study by Liljestrom et al. (1998) which offers more qualitative data in the context of a poor region as a contrast the general findings.

The general situation with respect to poverty.

Summary: The extent of poverty may be overestimated in Vietnam and remaining restrictions on the free market may have more effect to reduce poverty than is commonly recognised. This refers particularly to legislation restricting the land market.

Vietnam is a poor country and the incidence of poverty as measured by the VLSS survey is high: 50.9% of the population is below the poverty line. Poverty appears in this study therefore as pervasive. However, several reasons have been advanced as to why this figure may be an over-estimation: (1) the poverty line is calculated on a rice calorie intake which was converted in monetary terms and translated into dollars; Griffin (1998b) suggests that the calorie standard adopted is on the high side, furthermore the prices and exchange rate adopted in the conversion may have led to overestimation of the degree of poverty (Irvin, 1995); and (2) rural households may have under-reported marketed production and appear therefore poorer than they are. Third, the survey was carried out at a time of relatively low rice prices, which made the net rice producers relatively poor as compared to the net rice consumers (ibid.). Poverty estimates are of course sensitive to the poverty line adopted; Jansen makes this point by comparing the VLSS figure with other estimates produced by GSO: "Vo-Tong Xuan quotes results from the annual survey of the General Statistical Office that suggest that the proportion of people below the poverty line declined from over 30 per cent in 1990 to 19 per cent in 1995 (Vo-Tong Xuan 1996)" (Jansen, 1998: 27). Hence the definition of poverty remains a matter of debate, including of course the what differences may emerge from adopting non-money metric indicators (e.g. McKinley, 1998).

More reservations can be made on the interpretation of VLSS findings. The relatively even distribution of land is often mentioned as a factor alleviating poverty, but this is not linked to the policy behind it. The Land Law of 1993 limited the amount of land per household to three hectares. Although this will probably be raised to five hectares, this is more to legalise the existing situation than to change the principle of limited landholdings per household. As the majority of the poor (90 per cent) are found in the rural areas the effects on poverty of a relatively equal land distribution must be considerable. For example Fforde writes that "the rather high welfare levels of vulnerable groups seems closely linked to land distribution. This points to the role played by the local Party and state organisations in limiting land concentration and social differentiation" (1989: 53). The Vietnamese government is reluctant to unshackle the land-market but donors press for this. The primary reason is to provide adequate incentives, but it is also expected to reduce poverty. For example, UNDP advocates a further development of land markets: "If the land market were allowed to operate more freely, it is likely that more poor people would sell out and move to less crowded regions or switch to non-farm jobs with the proceeds of their land sales. Land use would also be more efficient if this happened and many of the poor would improve their lives" (1995: 44). This argument not only overlooks the effects of an egalitarian pattern of land use rights, but it is also doubtful whether larger farms would lead to more

efficiency. The present distribution limit stimulates intensification of land use and small plot sizes stimulate in the first place intensification through the use of labour – which is abundant – rather than the use of machinery. The latter tends to respond to an enlargement in size. De Vylder (1993; p.32), while pleading for some latitude in the development of land markets, warns against a “Bangladeshisation” and mentions then the Red River Delta where land is more scarce than elsewhere.

Increasing fragmentation can lead to inefficiencies and plot sizes become smaller, especially in the Red River Delta. Despite the egalitarian distribution of land, there are rural households without land. According to (Don and Jalilian, 1998) “particularly in the Mekong Delta where 12 per cent of the households do not have land’. However it is doubtful whether one needs to liberalise land-markets further to stimulate internal migration. This is – especially from North to South – already common in Vietnam and is also government sponsored (Don and Jalilian, 1998:22) Fforde (1997) reports: “Doc Lac, the large Central Highlands province that is Vietnam’s major coffee producer, has been the site of ethnic difficulties as a rush of ethnic Vietnamese have settled on land previously occupied by the indigenous population”. Such problems are however, not a necessary consequence of migration. Liljestrom et.al. (1998) describe a variety of relationships between Kinh immigrants and local people.

Regional patterns in poverty

Summary: The regional differentiation in poverty profiles is beyond doubt and is a logical consequence of differential income effects of supply responses. Such differences should however not obfuscate the effects on poverty alleviation of economic reforms throughout Vietnam. More attention may also be needed for the effects on regional disparities in poverty of the restriction on rice marketing and the discriminatory nature of the land tax. Further liberalisation may therefore imply an exacerbation of interregional inequalities and it may be that effective poverty alleviation requires government intervention in the form of interregional transfers

We have mentioned already that poverty is more a rural than an urban phenomenon in Vietnam, but the VLSS also reveals important regional disparities. On the one hand, some regions, notably the South East – which includes Ho Chi Minh City – are relatively better off. The poorest regions are Northern Upland, North Central and Central Coast. Poverty is strongly associated with distance from cities and the coast. It reflects however, not only a lack of access to markets but also essential differences in endowment (Minot, 1998) Poor areas are often mountainous. Another distinguishing characteristic of poor regions is the concentration of minority ethnic groups there. These elements form the main ingredients of debates on poverty in Vietnam.

The distance from markets is particularly important in Vietnam as so much of poverty reduction can be explained by the effects of economic reforms on income. The reduction of poverty in Vietnam is in the first place a result of such income effects and will be found there where the supply response in

agriculture is the strongest. The predominant crop in these supply responses is rice and that is concentrated in the Mekong and Red River Delta. The industrial crops are also regionally concentrated, for example coffee is mainly found in the Central Highlands.

It is also likely that the fast growing industrial sector led to increased incomes in the poorer households and this is also geographically differentiated. It has to be kept in mind that manufacturing grew throughout the country, but the rate of growth differed. The share of the regions in which the big urban centres are found – the Red River delta, which contains Hanoi and the paradoxically named North East South area of which Ho Chi Minh city is a part – grew from 51 per cent to 68 per cent between 1991 and 1997. The growth in that share came particularly from North East South: from 45 per cent in 1990 to 51 per cent in 1997. The share of Ho Chi Minh city alone remained at 27 per cent. However, these effects must not be overstated. Whilst the major industrial centres have all experienced rapid growth, their growth performance is around the median level. We analysed the growth in industrial production over the period 1991–97 (data from GSO Statistical Yearbook) and found a zero correlation (0.007) between initial output and growth – a result we find since several provinces have experienced very rapid growth from low bases.

The service sector has grown very fast, but is virtually undocumented (see above). However, given the fact that this sector tends to be linked to other sectors, it is to be expected that growth will also have been concentrated in particular areas, particularly in the big urban concentrations.

It is useful to compare the insights of the Vietnam Living Standards Survey with the more qualitative account of the changes since Doi Moi in North-Eastern Vietnam by Liljstrom et.al (1998). The authors went back in 1993 to four villages and adjacent forest enterprises they had studied in 1987. The problem which they encountered is in some senses specific to the area: whereas the forest enterprises had been set up in the first place aiming at production, the problem had changed in 1993 to one of re-afforestation. Their findings have, however, clear wider implications for what happened in Vietnam as they found considerable progress in mountainous areas inhabited primarily by ethnic minorities. A rural environment where the main income generating effects of the rice boom passed by and where poverty is supposed to be the most serious in Vietnam. In three of the four locations they found, however great improvements with respect to poverty:

- Lam Tien Village: “One of our deepest impressions of Lam Tien village is that the former perennial food shortages have definitely ended” (ibid: 29).
- Phuc Tam Village: “Thanks to improving commercial, production and service activities, the living conditions in the village are greatly improved” (ibid: 87).
- Khuoi Nieng Village: “The flood gates are opened and all contained forces burst forth. Enterprising households here make more money than anywhere

else we have been. So far we have reckoned incomes of wealth households in tens of millions of dong; in Khuoi Nieng they earn hundreds of millions “(ibid: 133).

- Summarising: “By now the reader is familiar with the typical features of Doi Moi: farmers’ households gradually taking over production links; workers leaving collective rows and building their own houses; enterprise managers reducing their workforce and signing contracts with both farmers and workers; land being redistributed; and first and foremost, fewer people being hungry and underfed” (ibid: 133).

The general conclusion that economic growth tends to be strongest in regions that are already rich is probably true, but it should not obfuscate the fact that income effects had poverty alleviating consequences throughout Vietnam.

The discussion of disadvantaged regions usually pays too little attention to the poverty alleviating effects of government policies there. Most of these areas import rice and in that respect the consequences of market liberalisation were profound there. Whereas they were formerly provisioned by the government at a fixed price, they now had to buy on the open market. In consequence Liljestrom et.al found rice to an upcoming crop in the mountainous areas. The restrictions in the rice trade which keep the consumer price of rice in Vietnam down are of course beneficial for all the poor in Vietnam as food is usually a bigger portion of their expenditure. But this argument counts especially for alleviating the regional differentiation in poverty as rice importing regions tend to be the poorest ones.

Similarly the land tax is often considered merely as a tax on the agricultural sector which primarily affects the poor. A new land tax ordinance was promulgated in the same year as the land law, 1993. It gave a reduction of the land use tax by 30 per cent compared to the 1983 land tax ordinance, from 10 per cent on average to 7 per cent of the average output calculated from the past five year period. This tax amount would be kept stable for ten years. The new tax ordinance of 1993 further provides economic incentives to disadvantaged areas and people, and ethnic minorities by giving them tax reduction and/or exemption in cases of bringing in bare hill land or idle land for cultivation of perennial crops. It is therefore not only a progressive tax which taxes fertile land more than marginal land, but it also stimulates development in the poorer areas. Although the impact of the land law and land tax ordinance of 1993 is positive everywhere, it has been most effective in the cultivation of multi-year crops, especially in industrial and perennial export crops – hence it stimulates profitable cultivation practices in poorer areas.

Government interventions combat regional inequalities through interventions in rice marketing and discriminatory taxation, but a more positive government intervention may be needed as well. That means in the upland regions initial investment in roads and elsewhere in irrigation. Government expenditure in relevant sectors – transport because of roads, forestry, as it is crucial in the development of the mountainous regions and agriculture, as it covers irrigation

which has a wider national impact- has been protected and grew in the nineties (Don and Jalilian, 1998: 15). But their share of the total budget is and remains small. It would require intergovernmental transfers from the richer regions to the poorer ones. However “despite the equalizing tendency of the transfer system, per capita local government expenditure is significantly lower in provinces with lower per capita GDP. This means that poorer provinces are less able to finance an appropriate level of government expenditure on antipoverty programs, especially in such basic social services such as primary education, health and social relief” (World Bank 1995: ix). That argument would hold as well, if not more so, for the capital expenditure needed in these fields.

Social Services and social sector spending

Summary: It is remarkable that major social indicators in Vietnam have not deteriorated despite the introduction of user fees in education and health; but the nineties have also witnessed substantial increases in real social spending. The latter sector has even been privatised to a considerable degree. School enrolment is the only indicator that has shown a decline. Participation in education is also a particularly distinguishing characteristic between poor and non-poor in Vietnam and therefore a particularly suitable field for budget support targeted at poverty alleviation.

The poor tend to be less educated, have a higher fertility rate and have bigger households. These facts raise the relevance of social sector spending as a means for poverty alleviation. Economic reform has meant the introduction of user fees in education and health and one expects that the poor are particularly hard hit by this. Nevertheless, there is an increase in the share of public expenditure on health and education in the first half of the nineties (see section 5.3 below). Even though this was much more so with respect to education than to health (Don and Jalilian, 1989:15; Jansen, 1997: 28) school enrolments stagnated or declined in the beginning but increased later on. The health sector changed in character: “Taking the public and private sectors together, it is clear that the public sector role in financial health care is small – the state paid only for 16% of all health expenditures in 1993. Even for important public services private payment dominates” (World Bank, 1995. p.100). The targeting of the subsidies is however only weakly pro poor. Only at the lowest levels – the commune health centres- do the poor benefit most from state subsidies. Segall et al. (1999) document that funding to commune health centres has risen substantially in the 1990s²⁴ and that there have been corresponding health benefits from these increases, but they are also critical of the impact of user fees on the poorest and the targeting of exemptions. A similar situation exists with respect to education. “Poorer individuals receive a larger share of the primary school subsidy than their share in the overall population” (World Bank, 1995 p.90). However, “the levels of education on which most funds are spent are not much attended by the poor”. (Jansen, 1997. p.30).

²⁴ The authors report real spending (in 1995 VND) per person for four health stations: the 1991 figures were 4.5, 6.7, 5.0 and 2.6 and those for 1995 7.5, 6.2, 9.7, 9.8 respectively; i.e. a mild fall in one case, close to doubling in two and near quadrupling for the fourth.

The effects of economic reform in the social sectors may therefore have weakened the position of the poor, but this has to be seen in conjunction with a very good performance in Vietnam with respect to social indicators. The figures available usually cover a wider period than the onset of economic reforms, especially the effects of macro economic stabilisation and the introduction of user fees, but there is no indication as yet that this has led to a worsening of the situation. Health indicators improved after economic reforms. Life expectancy went up; infant and child mortality went down; crude death rate went down; maternal mortality went down. Functional literacy has always been high in Vietnam and seems to be stable. School enrolments in post primary education decreased initially after the reforms of 1988, but they are rising again in the 1990s. Enrolment rates may however, be decreasing. On the other hand there is an increase as well in the completion rate of primary schools. (Jansen, 1997: 24; Jansen, 1998: 8–9; UNDP, May 1998 Annex B and see especially Don and Jalilian, 1998: 20 for most recent figures which are very optimistic).

Unless one doubts the validity of these outcomes and then raises very big questions on governance in Vietnam there is ample reason to support the government in these fields. Prescott (1997) critically discusses health and education spending with respect to the way they are targeted at the poor and identifies important areas for support. If one wants to target government spending – supported by aid – at the poor, then education seems to be the most relevant field as it so obviously disables poor people who want to rise out of poverty. Fforde found education to be the most crucial variable in distinguishing the vulnerable in Vietnam: “the vulnerable rural population is, numerically, dominated by the under educated” (1998: 30). The great majority of the vulnerable were in Target groups 2 and 3 (working women with low levels of education and young people with low levels of education) who make up some 85 per cent of the vulnerable. That they fared relatively less badly than expected “must be to do with their relatively good access as their capital assets are well below average” (p.26). It is also striking that 53 per cent of the young people with low levels of education said that economic difficulties were preventing them from studying. Jansen (1998) mentions as well that economic reasons are predominant among those leaving school: in 50 per cent of the cases at primary level; 35 per cent at the level of lower secondary school and 26 per cent at the upper secondary level.

Social safety nets

Significant transfers are made in the Vietnamese economy through social security spending. According to the World Bank (1993: 109) outlays for social protection were almost as much as for education and health combined in 1992. The amount was also growing and doubled by 1994. By far the largest amount (82 per cent) was spent on pensions and disability payments for government workers. Another 7 per cent went to war victims and 11 per cent of the budget was for social relief. A part of the latter amount goes to regular relief targeted at the “lonely elderly”, orphans and handicapped. This covered however only 140,000 people in 1994. The World Bank PA concluded that

the profile of who benefits from these transfers is not pro-poor and proposes that the large expenditures on social protection will require a substantial reallocation of the budget from pensions to social relief. In this connection, it is noteworthy that the World Bank report mentions a decree of 1993 to shift social security from the state budget to a Vietnam Social Security organisation to be implemented in 1994.

Fforde's survey of vulnerable groups supports this general view. He found consistently that those receiving state benefits in his survey of vulnerable groups in rural Vietnam were relatively well off. Invalids capable of work (p.44): "Those receiving regular social benefits have higher average per capita net incomes at 1.29 million dong compared with 1.17 for those who do not receive regular benefits". Invalids incapable of work: "Those receiving regular social benefits have higher per capita net incomes at 1.15 million dong as compared with 1.08 million dong for those not receiving benefits" (p.45). The situation is more complicated with respect to the aged. He found a subgroup of 39 per cent who reported regular income from benefits. These incomes are high, at 270,000 dong a year on average; however there is almost no difference between the per capita net income of this group and those who do not report regular benefits - 1.52 million dong as compared to 1.54 million dong (p.50). Among orphans, the sub-group receiving regular social benefits (38.5 per cent of households), he found that per capita net incomes averaged 0.90 million a year, compared with 1.1 million for those who have no benefits. The benefits made up only about 10 per cent of net incomes (average value of 88,000 dong) (p.52). A minority receive state benefits. The results suggest however that these benefits are going to the richer households and Fforde notes that these are not 'low' in comparison with accepted poverty levels (p.53). Fforde(1998) concludes "There is no 'crisis' with regard to Vulnerable Groups. On the whole, existing interventions and their own efforts are resulting in welfare levels that are acceptable" (p.53).

There may be some undue optimism with respect to the fate of vulnerable groups. Liljestrom et.al (1998), found several factors distinguishing the poor and non-poor which indicate that social security may be problematic in Vietnam. "In present conditions, the winning households have the following assets: they are healthy and able couples in a stable marriage; that means two pairs of productive hands; and they no longer have small children. The poor on the contrary have only one pair of hands in a situation where the number of productive hands counts; the family has a sick member; they come from poor families and cannot count on assistance for investments or in need; and they do not eat well and lack the energy to witch to other kinds of work when forestry fails to provide jobs" (ibid: 248-50).

Combating poverty through credit

Vietnam aims to lift up the poor through production rather than distribution. The aim is "not to provide subsidies to the poor, but rather to create favourable conditions for them to lift themselves out of poverty" (Don and Jalilian, 1998: 21). This may be a sentiment borne by the grass roots as well. Fforde(1989)

reports that the vulnerable groups respond to their disadvantaged states much more by relying upon their family and market opportunities than on local community or state support and concludes that “it is the potential (or not) to integrate into the changing opportunities offered by the new market economy that is crucial” (ibid:54). “A key issue facing these families is how to exploit the market opportunities that they see open to them, to do so they feel they need capital, know-how and services” (ibid:41). It is therefore striking that the government sees funds for credit -notably the Bank of the Poor- as its major commitment in the Hunger Eradication and Poverty Reduction Program funds for credit (Don and Jalilian. 1998: 26–7).

The belief in credit as a means to combat poverty is pervasive in Vietnam and returns again in the study of Liljestrom et.al (1988). For example: “the collective provides credits to members. Households lacking capital can buy materials, fertilizers and insecticides from the co-operative on credit and pay it back at the end of the harvesting season” (ibid:79). “The existence of an agricultural bank in Pu Think commune is further evidence of the relatively advanced state of commodity production and the role of money. The bank has a direct impact on the process of land use. All interviewed households in Phuc Tam had borrowed money from the bank at least once. Among the ten beneficiaries, nine had paid back their loans in time, while one had only managed to pay back the interest” (ibid: 87). “Another task devolving on the Women’s Union is assisting members to develop their family economy by lending funds to them. In 1993 the Women’s Union stood as guarantor for bank loans of 10.5 million dong with an interest rate of 2.2 per cent. This sum had been lent to twenty-one members who did not, therefore, have to mortgage their property for the loan. Nearly all the women have used the money to buy pigs. Up to November 1994, the women had repaid the loans to the bank” (ibid:90). “A number of farmers have borrowed 2–3 million dong from the bank. This is not enough to meet the farmers’ needs” (ibid:142). “The couple paid 300,000 dong for the house in 1993. They were able to borrow from the enterprise after the special assistance programme ended in 1992” (ibid:164). “However, since the 1990s more credit is available. Especially in 1994 and 1995, the employees have been able to borrow between 1 and 3 million dong on a three year term from the enterprise. The money has been used for livestock, fishponds, houses, and goods like TV sets and motorbikes” (ibid: 221).

There is however a big difference of opinion on the use of credit to combat poverty between donors and the Vietnamese government. The former insist on a strictly commercial operation in the financial sector and reject the notion that in order to combat poverty interest rates should be adjusted downwards and operating costs should be subsidised.

Conclusions on poverty

Liberalisation of the economy has probably not hurt many, but the benefits have been concentrated in some areas: urban more than rural and cash crop growing areas more than especially the mountainous regions where most of

the ethnic minorities live. Further reduction of poverty out of growth may be more problematic than it has been the case thus far. The service sector may be saturated. Further trade liberalisation and reform of state owned enterprises are likely to lead to a contraction in manufacturing. The supply response in agriculture may have been exhausted and coming up to constraints of capital, infrastructure and necessary technical innovation.

The track record in terms of outcomes has been good with respect to poverty. Therefore it may be worthwhile to pay attention to the poverty effects of contested policies as these are restrictions on the free operation of the market; land, rice, subsidised credit and discriminatory taxation on land; regulating the rice market and discriminatory taxation. As Vietnam has such a good record in social sector spending with favourable outcomes, the case for budget support in order to combat poverty is clear and then education appears to be a crucial area.

Finally, it may be that the struggle against poverty escapes to a certain extent the power of policy making. Firstly, because much poverty alleviation takes place irrespective of the state. As Fforde observed: 'the key agency (for the vulnerable) is probably not 'the family ' as surveyed here, but that net of kin relationships around individuals, that includes those close relationships that they can count upon when they meet difficulties'(1998: 53). Liljestrom et.al (1998) mention factors that distinguish those who are successful in the transition from those who are not: (1) they have a family and kin network for mutual support in crises and for investments; and (2) they are locally well-rooted insiders.

A second set of factors relates to cultural phenomena which are difficult to capture. These refer to what may be called entrepreneurship. Liljestrom et.al (1998), bring out what has been common in other studies as well. Economic success in rural Vietnam depends in the first place on a diversification in sources of income. However, when it comes to an interpretation of the reasons why some make use of such opportunities and others do not, they come to quite intangible factors. For example, lack of flexibility – some workers are imprisoned in the past, and unable to see new options. Fforde (1998) found that on the whole vulnerable group members' households are not very different from their neighbours and it is therefore difficult to single out the factors that make one stuck at the bottom and others not. He concludes then that "the key issue facing these families is how to exploit market opportunities that they see open to them" (ibid: 41). Government policies have some influence on that, but ultimately this refers to factors in society which are difficult to capture.

4.4 Gender issues

The notoriously difficult task of attributing changes to policy interventions is particularly difficult in the case of analysing the status of women. Analyses of the gender-impact of adjustment in fact often dwell on the unequal status of women, whereas the pertinent issue is how this status has changed over time

and how these changes have been influenced by policy. In Vietnam analysis is further complicated by the fact that the communist government had many policies to achieve gender equality, and, as is shown below, did increase women's economic and political participation: there is therefore a danger of looking back at a lost "golden age" without critical reflection on women's day-to-day experiences in earlier periods.

The first constitution established the equality of the sexes, and several subsequent measures were enacted to improve the status of women such as the 1960 Law on Marriage and the Family which outlawed polygamy. In the three decades following the revolution women increased their political representation (as shown for example by the percentage of women elected to the National Assembly²⁵ – Table 4.6 – and economic participation (women's share of the labour force in state enterprises rising from one-twentieth to over 40 per cent) (and this is not to mention their contribution to the war). At the same time, the Party seems to have aligned itself with conservative social conventions, so that unmarried women who had children had to write pieces of self-criticism, to publicly acknowledge their mistake in public meetings and had their pay cut if they did not lose their job altogether (Nguyen Thanh Tam, 1996).

Percent of women in National Assembly		Share of women's employment in the state sector	
I	2.5	1955	5
II	11.6	1965	27
III	18	1975	42
IV	29.7	1985	46
V	32.3	1992	44
VI	26.8		
		Number of policy documents about women	
VII	21.8	1945	0
VIII	17.7	1960	5
IX	18.5	1975	20
		1989	12
		1994	7

Source: Tran Thi Van Anh and Le Ngoc Hung (1997)

Table 4.6 shows that women's representation in the National Assembly has fallen since the mid-70s, having peaked at just under one-third in section V (1971–76). This fall may be attributed to the "heavier residue of feudal attitudes in the South" (Tetreault, 1996: 50); however, it should also be noted that the number of policy documents about women has fallen sharply. There would

²⁵ The National Assembly is of course not the only channel for women's representation; the role of the Women's Union is of particular importance, although there are differences of opinion as to how representative it is.

therefore be some grounds for thinking that the political weight given to women's issues has declined over time. But what can we say about how they have been affected by economic changes?

The first point to make is the same as that made with respect to poverty: income growth has been so rapid that most, though not necessarily all, will be better off and the focus is thus more on the distribution of benefits. In support of this perspective, Tran and Le (1997: 96) report that surveys show that over 70 per cent of rural women say their lives have improved. But there is evidence that some things are not getting better. Over the period 1985–92 employment in the state sector fell by over seven million (World Bank, 1993: 233), during which period the long-run rise in women's share of state employment was reversed (Table 4.6) – hence it is clear that women were disproportionately represented amongst those made redundant. For those women made redundant, especially in urban areas, opportunities are limited, especially as urban migration has grown rapidly with liberalisation. Precise data are not available, but it is known that the majority of migrants are male (a fact which is partly picked up by the increasing share of women in the agricultural labour force in the 1990s). This tendency reinforces the possibility of single mothers and female-headed households, to whom social stigma still attaches (as indicated by the Vietnamese term for them as “lonely women”) and who are more likely to be poor than other households. For those women who do migrate, or those made redundant in urban areas, one possibility is prostitution – estimates suggest that the number of prostitutes had been reduced from half a million during the war to 10,000 in the early 1980s, but by the 1990s the figure had increased ten-fold to 100,000 in addition to established routes exporting Vietnamese women to Cambodia (for the U.N. peace-keeping force) (Barry, 1996). Government has named fighting prostitution as one of its top ten priorities, but it seems unlikely to be able to combat the social and economic forces that drive women to resort to this means of survival.

In summary, whilst much of the former rhetoric of gender equality may have indeed been just rhetoric, it seems plausible that there was greater political attention to gender issues in the past than over the past ten years. Whilst women have benefited from the overall increase in economic prosperity there have been gender-biases skewing these benefits toward men, to the extent that some women have indeed been left worse off.

4.5 Environment

Economic growth on the scale experienced by Vietnam is certain to have environmental consequences; these are summarised in Table 4.7. As Perrings (1998) argues the question is not whether there have been such impacts but whether, owing to unpriced negative externalities, these impacts are greater than would be socially optimal, with the possibility of adverse long-run implications for sustainable development.

Perrings argues that it is indeed the case that private actors ignore the environmental consequences of their actions and that many public goods, such as the conservation of coastal and upland forests, are under-invested in. Moreover, some of the resulting environmental effects are irreversible and so will have costs well into the future. There have, however, been some positive aspects of *doi moi* for the environment, such as the establishment of clearly defined property rights in natural resources, and the development of institutional capacity, with international support, to tackle environmental issues. Hence government and donors have acted to address environmental concerns (e.g. World Bank, 1995), but further steps could be taken to internalise externalities. Such policies are, however, not usually part of the formal policy dialogue process, meaning that they not form part of the conditions to which programme aid is subject. This is not to say that environmental concerns are wholly absent: for example the 1996–98 PFP does include a policy area “environment and natural resources”, but this is area 18 out of 18 areas, with fairly general measures such as “promote environmentally responsible farming technologies”. Nor have environmental issues be a focus at CG meetings: the Danish government mentioned them in their statement to the 1995 and 1996 meetings, but, according to the official minute, other donors did not.²⁶ Whilst less formal, and project-related, policy dialogue may address environmental issues, if they are of great importance some thought may be given to incorporating them more formally.

²⁶ In comments on an earlier draft we were informed that Sweden has raised environmental issues at the CG meeting (though, as stated, this fact was not reflected in the official record prepared by the World Bank). We were also told of the emphasis placed on this issue in several ways, including visits by past and current Swedish Environment ministers. These facts bear out our argument that other channels for influence exist other than PA, but do not alter our contention that environmental matters have been marginalised in the formal policy dialogue process.

Table 4.7 Environmental consequences of economic reform	
Source	Environmental impacts
Resource depletion from agricultural growth	<p>Loss of habitat in forest areas (from logging and conversion forest land to agriculture and aqua-culture);</p> <p>Loss of ecological services from conversion wetlands to paddy;</p> <p>Increased flood damage and siltation major catchments due to de-vegetation of wetlands</p> <p>Increased storm damage in northern coastal areas and coastal erosion in southern coastal areas due to depletion of mangrove forests;</p> <p>Reduced productivity in both agriculture and aqua-culture due to acidification of drainage water from cultivated acid sulphate soils;</p> <p>Severe depletion of almost all inshore fish stocks due to excessive fishing and destruction of mangroves and coral reefs;</p> <p>Reduced coastal protection as a result of coral reef damage caused by siltation, dynamite fishing and coral mining;</p> <p>Increased soil and water pollution from fertilizer and pesticide use.</p>
Industrial growth	<p>Increased emissions to air, water and soil;</p> <p>Dispersal of hazardous waste during flooding.</p>
Other effects	<p>Air pollution from increased traffic;</p> <p>Adverse consequences of rapid urbanisation.</p>

Source: Perrings (1998)

Chapter 5

Macroeconomic impact of aid inflows

5.1 Aid in context

Chapter 1 indicated that Vietnam receives high levels of aid for a country of its size. But these high aid levels must be set in context in three respects. First, given the size of the economy aid the ratio of aid to various aggregates (such as imports) is not particularly high. Second, aid is just one of several sources of forex: both remittances and FDI have grown rapidly in the 1990s, as have own forex earnings from exports. Third, the increase in aid from 1993 occurred after both the growth turnaround and stabilisation, so the story is clearly more complex than saying that growth was responsible for either of these achievements.

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
GDP	..	12.5	5.5	4.1	3.6	2.1	4.0	3.0	4.2	4.5
Imports	52.4	45.7	25.3	16.1	14.0	6.6	11.9	8.1	9.4	..
FDI	..	763.0	373.3	153.6	136.9	32.9	59.6	34.4	54.3	..
Investment	..	71.5	30.3	18.8	20.4	8.6	15.8	11.1	15.2	15.4
Government expenditure	..	69.8	32.6	31.5	20.8	9.9	19.6	15.0	23.3	..

Source: national aid, balance of payments and government accounts data from GSO.

Figure 5.1 reports aid relative to various aggregates. It is striking that in the 1980s Vietnam had the manifestations of a typical “aid dependent” economy, with aid paying for over half of imports, nearly three-quarters of investment and over two-thirds of government expenditure. Yet by the mid 1990s these ratios had been dramatically reduced: aid accounted for less than one tenth of imports, and, being half of FDI (rather than over seven times larger as earlier), financed about one sixth of investment. Aid’s share relative to spending was still substantial but not dominant as it had been in the 1980s.

These figures place a limit on the potential impact aid may have had. In some other countries covered by the Global Evaluation of Swedish Programme

Aid, aid still covers half or more the import bill and it is easy to argue that real imports would have fallen by a third or more should aid not have been available.²⁷ But in Vietnam during the 1990s the relative contribution of aid is such that an impact of this magnitude cannot be expected. If aid finances 10 per cent of imports than the no aid scenario implies at most a 10 per cent reduction in imports. Such orders of magnitude suggest that aid can have played a useful role in supporting growth, but that it has not been essential for that growth. We can also make the point that was made in respect of policy dialogue; namely that the timing of the increase in aid compared to growth and inflation show that aid was responsible neither for ushering in the period of high growth nor for bringing about macroeconomic stabilisation

5.2 Aid and the balance of payments

The aggregate which aid may be said to have most directly affected is the current account, which having been almost in balance in 1992 has worsened thereafter. However, as already argued in section 4.1, it is not necessarily so that the negative current account is indicative of structural weakness in the Vietnamese economy. A current account deficit must be offset by a capital inflow. This is an accounting identity that must hold: the question is what is causing what? Does an inability of Vietnam to earn enough by its exports to pay for import requirements create a financing gap which must be filled by foreign inflows? Or does an exogenous capital inflow create a current account deficit by allowing imports in excess of exports? Capital inflows to Vietnam have first and foremost been Foreign Direct Investment (FDI), followed by ODA (ODA is one third to one half of FDI), both of which are manifestations of the confidence of the international community in the Vietnamese economy. These inflows, together with very rapid export growth, have financed burgeoning imports. But it is notable that there was no import compression in the years when there were no capital inflows (indeed imports continued to grow), further that the nominal exchange rate was reasonably stable in these years and that growth climbed up to over 8 per cent. The worst that can be said is that Vietnam is creating potential future balance of payments problems for itself if export earnings do not grow sufficiently to meet future service obligations from current inflows.

A more detailed analysis of these arguments can be made by examining the sources and uses of forex.

A first way to look at these data is to identify main trends or abrupt changes. Doing so shows the following main features:

- debt service has only exceeded 20 per cent of uses of forex in one year (1989) and has been much less (around 10 per cent) in the 1990s – actual

²⁷ Although this evaluation is concerned with Programme Aid the data do not allow us to readily distinguish the effects of programme aid from other aid at this level. Where such a distinction may be made then we do so.

debt service (adjusting for arrears has been rather less) (nearly \$1 billion of arrears were cleared from 1993–95, but practically twice that amount was received in debt relief over the same period).

- aid fell in the early 1990s, being particularly low in 1991 and 1993 (though debt relief was high in the latter year), but these falls were not matched by a corresponding reduction in imports, which can be explained by the fact that between 1990 and 1991 exports rose by about twice the fall in aid, and other inflows and remittances (private transfers) also rose; a similar pattern can be observed for 1992–93.

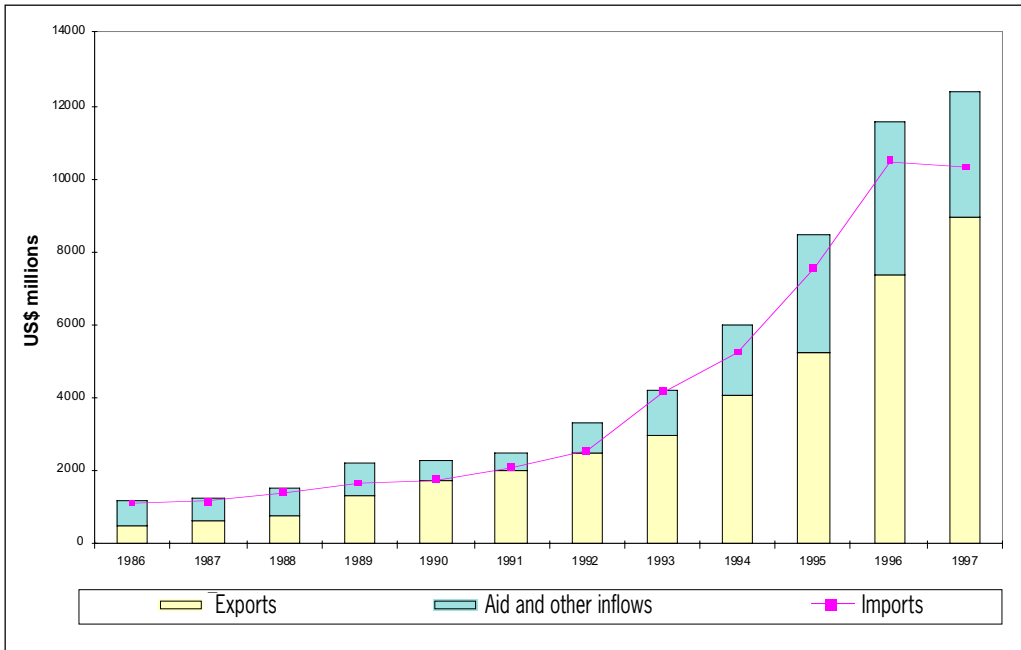
These impressions confirm the idea that imports are not largely driven by aid. Exports in fact account for 70 to 80 per cent of the sources of forex, and it is (indeed more than 80 per cent in recent years), correspondingly, the availability of export revenue that is a main factor behind the level of imports. This fact is brought home by Figure 5.1 which shows the level of imports against the main sources of forex. In the late 1980s imports were financed by all sources of forex and experienced some modest growth. From 1989–92 exports began to grow, and so did imports (at the same time some resources were devoted to debt service). From 1994 onwards the import bill has exceeded export earnings, but the strongest growth can be seen to come from this latter source: there is also some growth in other sources (which has helped finance the increase in debt service). Although grant aid is included in the aid figure it is only about half the total, so that Figure 5.1 also illustrates how a growing trade balance has been created by increased inflows allowing imports to grow in excess of exports.

Table 5.2 Sources and uses of forex, 1986-97 (US\$ millions)

	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
<i>Uses of forex</i>												
Imports	1121	1184	1412	1670	1772	2105	2535	4162	5244	7543	10480	10313
Debt service	265	233	363	563	279	345	476	651	547	769	729	1317
Decreasing arrears	0	0	0	0	0	0	0	265	292	439	0	0
Increasing reserves	0	0	0	105	162	270	261	0	0	0	471	368
Other	112	128	89	246	381	247	269	495	418	247	488	568
<i>Sources of forex</i>												
Exports	494	610	733	1320	1731	2042	2475	2985	4054	5198	7337	8955
Aid	540	591	740	763	363	169	551	209	579	688	1100	829
Debt relief	0	0	0	34	0	0	0	883	526	547	0	0
Private transfers	30	10	4	9	34	67	59	70	170	474	1050	1000
Arrears accumulation	317	297	320	291	298	332	196	0	0	0	591	181
Other inflows	111	37	41	100	168	220	260	949	1172	2091	2036	1601
Reserves	6	0	0	0	0	0	0	477	0	0	0	0
Other	0	0	26	67	0	137	0	0	0	0	54	0
Total sources (and uses)	1498	1545	1864	2584	2594	2967	3541	5573	6501	8998	12168	12566
<i>Memo item:</i>												
Actual debt service	-52	-64	43	272	-19	13	280	916	839	1208	138	1136

Note: actual debt service is debt service adjusted for accumulation or settlement of arrears. Source: IMF (1998) and World Bank (1993)

Figure 5. 1 Imports and the sources of forex



The data may be further analysed by constructing a counterfactual balance of payments in the absence of the aid inflow. These are shown in Table 5.3, and are constructed as follows. All aid, including debt relief, is set to zero. It is also assumed that no arrears are settled. Under scenario 1 it is assumed that imports are reduced by an equivalent amount to the reduction in aid - a mechanistic simulation which formally captures the maximum possible impact of aid on imports. We see that even in this case imports are between 74 and 92 per cent of their actual level, though over twice as many arrears are accumulated over the period as a whole. In scenario 2 a debt service embargo is set at 10 per cent of export earnings, which roughly halves the amount of debt paid (though not so much in recent years - and in 1991 10 per cent of export earnings were more than sufficient to meet the country's debt obligations). In this case imports are 85 to 104 per cent of their actual level.

This simple counterfactual analysis thus adds further support to our view that aid has played a modest role in the balance of payments. Over the 1990s as a whole, imports have been perhaps 10–15 per cent higher than they would have been in the absence of aid, and arrears have been settled that would not otherwise have been. We do not wish to undermine this useful contribution, but we do believe it is clear that this has not been essential to growth.

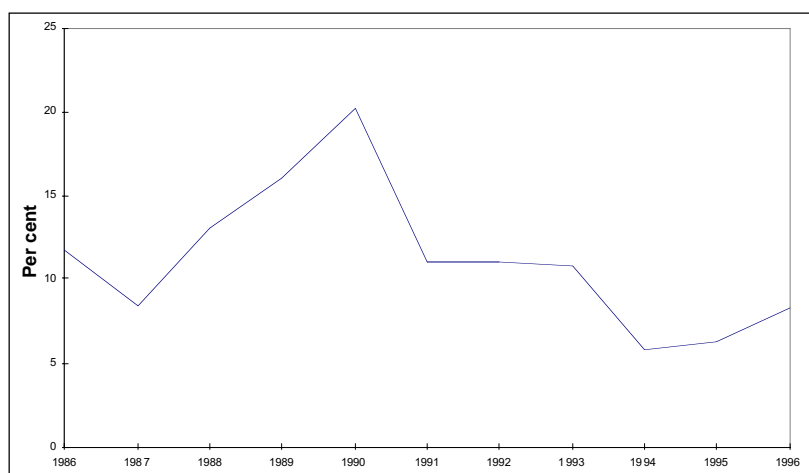
	1990	1991	1992	1993	1994	1995	1996	1997	Additional arrears (90-97)
<i>US\$ millions</i>									
Factual	1772	2105	2535	4162	5244	7543	10480	10313	602
Scenario 1	1409	1936	1984	3070	4139	6308	9380	9484	1598
Scenario 2	1515	2183	2353	3651	4633	6699	9625	9901	2812
<i>As a per cent of actual imports</i>									
Factual	100	100	100	100	100	100	100	100	100
Scenario 1	80	92	78	74	79	84	90	92	265
Scenario 2	85	104	93	88	88	89	92	96	467
<i>Memo item</i>									
Scenario 2 debt service as % of actual	62	59	52	46	74	68	101	68	

Source: calculated from sources and uses of forex.

5.3 Aid and the budget

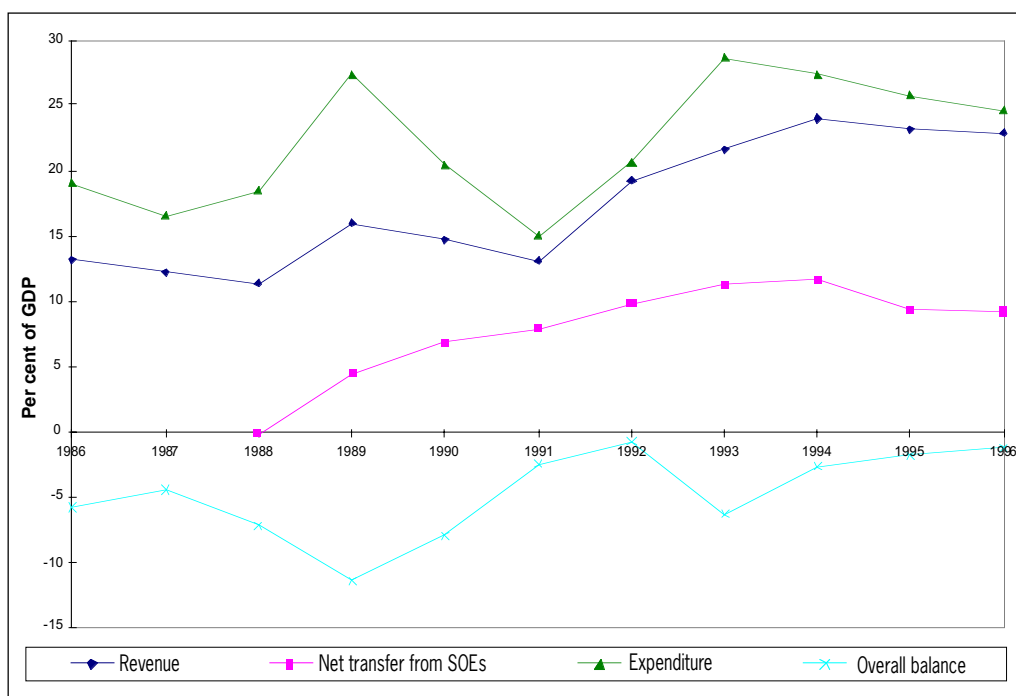
Analysis of the fiscal impact of aid is complicated by the fact that not all aid passes through the budget: this will have been particularly true of programme aid that was import support to state enterprises and for which no countervalue was paid, as was the case into the early 1990s. But we can identify that aid which does so, and hence its relative importance. Figure 5.2 shows aid (grants and foreign financing) as a percentage of government expenditure. This figure was from 10 to 20 per cent until 1990 and has been from 5 to 10 per cent thereafter; that is not very much. Hence we can conclude that aid has not been the driving force behind government expenditure.

Figure 5.2 Aid as a per cent of government expenditure



The main fiscal story for Vietnam is one of stabilisation with increased expenditure, which has been achieved by a substantial increase in revenue over the years 1991–94. This story is told in Figure 5.3. Up to 1990 the deficit was 5 to 10 per cent of GDP, with revenue laying between 10 to 15 per cent.²⁸ Expenditure was erratic, but mostly below 20 per cent of GDP. Since 1991 revenue has climbed reach over 20 per cent of GDP. This increase has come from higher tax revenue as non-tax revenue actually fell over this period. In 1988 tax and non-tax revenue were equal to 3.4 and 9.7 per cent of GDP respectively. Whereas in 1996 these figures were 19.5 and 3.4 per cent. This change has come about partly as the revenue from SOEs (typically 8 to 10 per cent of GDP) has changed from being non-tax to tax revenue (as SOEs now operate on a more arm’s-length basis from government), but there has also been a substantial increase in trade taxes (from one to six per cent of GDP) and some increase in tax payments from the non-agricultural private sector.²⁹

Figure 5. 2 Fiscal performance (as per cent of GDP)



The improved performance of SOEs is an important part of the overall fiscal picture. As Figure 5.3 shows, net transfers from SOEs rose from close to zero in 1988 (in fact negative) to 8–10 per cent by the mid-1990s. This increase was achieved by the virtual elimination of budgetary transfers to SOEs, which fell from 8.5 per cent of GDP to 0.5 per cent between 1988 and 1996, as

²⁸ The revenue figure shown excludes grants, but the deficit is after grants.

²⁹ These tax data are from IMF (1988: 22).

revenue from them remained roughly constant. Hence during the 1990s government expenditure has risen by around 10 per cent of GDP, which is itself perhaps remarkable in an economy growing as rapidly as has Vietnam's, and savings equivalent to 8 per cent of GDP have become available to spend elsewhere. What, then, has happened to the pattern of spending?

Table 5.4 shows expenditure shares from 1986–96, divided into three periods (where these periods correspond to the sharpest breaks identified in the annual data). Vietnam does not correspond at all to the, anyhow inaccurate, stereotype of the adjusting economy: overall spending has risen, capital expenditure has preserved its share, and the share of social services has increased dramatically (indeed more than doubled from the first period to the last). Within social services the largest increase has been taken by pensions and social relief, which as noted in the previous chapter, are poorly targeted, and then rises in education and health. The falling share has largely come in the category “other”, which captures the reduced transfers to SOEs.

The overall picture then is that fiscal performance has been good. The deficit has been reduced at the same time that expenditure has risen. The rise in expenditure has been strongly oriented to the social sectors. On the basis of this evidence we can tentatively argue that, to the extent that PA makes additional resources available, they would be most likely to fund higher levels of social spending.

	1986-1988	19889-92	1993-96
Current expenditure	74.1	77.4	75.3
General administrative services	4.4	8.6	8.7
Economics services	11.1	6.0	7.2
Social services	13.9	23.1	29.9
Education	5.2	5.4	8.0
Health	2.6	4.2	4.1
Pensions and social relief	4.6	8.5	11.6
Other social services	1.5	5.0	6.2
Other	44.7	39.8	29.6
Capital expenditure	25.9	22.6	24.6
Total	100.0	100.0	100.0

Note: Other includes transfers and interest payments. Source: World Bank (1993) and IMF (1998).

A final question before leaving the issue of fiscal performance is whether aid played any part in stabilisation (which has been found to be the case elsewhere). We have already argued that the timing and magnitude of aid mean that it is unlikely that it played a vital role. The closer examination of these data in this section appears to bear this view out. Aid is recorded as accounting for a small share of government expenditure, and one that fell quite sharply during the early-nineties stabilisation episode. This is not to say that countervalue is unimportant – and as mentioned in Chapter 2 the Vietnamese authorities are aware of these funds and treat them as a part of revenue. But they were not sufficient to bring about the stabilisation, which was achieved by economic policies of the Vietnamese government.

Chapter 6

The future of Vietnamese development and the case for programme aid

6.1 What is to be done?

In the mid-1990s the target to double income during the decade was revised upward to one of doubling per capita income. Now Vietnamese policy-makers are reeling from the realisation that growth will be pushed down below the target on over nine per cent from the impact of the East Asian crisis (official figures predict growth of 6–7 per cent, though some in donor circles suggest a far lower figure). Which direction should they turn in?

The reaction so far has been mixed. There was a tightening of exchange and import controls, but there are also signs of very gradual process on SOE and financial sector reform. The mixed reaction represents differing opinions amongst policy-makers as to the direction to take. There is far more uniformity of opinion on the part of the donors who see the way forward through liberalisation and privatisation. Here we do not intend to elaborate a full strategy for Vietnamese development; indeed to do so would be contrary to our intent, which is to suggest only that a wide range of options needs to be explored and thought through, and that the donor community does the Vietnamese a disservice by not facilitating such debate.

An example of the donor position are UNDP's presentation of the negative lessons from the Asian crisis, the first three of which are: "High economic growth, even in the presence of healthy macroeconomic policy indicators, do not necessarily imply sustainable development.... State-directed lending in commercial areas eventually has heavy inefficiency costs... Similarly, state-influenced lending. has heavy costs..." (UNDP, 1998: 15–16). This is one view of the Vietnamese crisis. Another would be to point out that in the early 1960s Korea had social and economic indicators similar to those of South Asian countries, but today is a high-income country with infant mortality and literacy levels comparable to those of developed countries. These achievements are not going to be eroded by a few years of low, or even negative, growth,

and stand in contrast to the adverse impact of market liberalisation in many transitional economies. It is then perhaps rather hasty to reject the Korean model on the basis of the current crisis. Again, without going into the arguments in detail, it is not difficult to construct a scenario under which the fourth wave of liberalisation has substantial costs and rather fewer benefits. This is not to deny that a crisis has occurred, but it can also be pointed out that many (including the Chief Economist of the World Bank) argue that the main lesson here is the need for more regulation in some markets rather than less.

To find an alternative voice to that of the donors in Hanoi at present one need look no further than the 1997 World Development Report of the World Bank (1997). This report advocated a role for the state considerably greater than that conceived in the donor's vision of the fourth wave: the need for regulation of financial markets is stressed, but also including activist functions of fostering markets and cluster initiatives. The extent to which these activities should be engaged in depends on how the capacity of the state is viewed, and that too is a matter for debate in the Vietnamese context.

6.2 The absorptive capacity constraint

A common complaint is of Vietnam's low absorptive capacity for project aid, which is seen as preventing utilisation of funds available for investment. MPI reports that absorptive capacity is only 30 per cent, with some donors recording far lower figures (e.g. only 9 per cent for Japan). Three observations may be with respect to this statement: (1) the figure is some senses misleading; (2) to the extent that there are problems of absorption this may be argued to come mainly from the bureaucratic and administrative requirements of donors rather than inherent weaknesses on the part of government; and (3) such a constraint applies only to project aid, not to non-project aid.

The 30 per cent figure is calculated as disbursements up to the current time divided by the value of aid pledged at the five CG meetings held since 1993. However, it can be argued if commitments or pledges are the appropriate denominator: pledges are relevant if the ability to prepare project proposals is a binding constraint, whereas using commitments as the denominator better captures problems in implementation. MPI state that of the US\$10.8 billion pledged in the five meetings \$8.0 billion has been committed, so that using commitments as the denominator would raise average absorption to 40 rather than 30 per cent. But even this figure is misleading since the typical project is planned for a four to five year period, with extensions of one or two years being common; disbursements usually peak around the third year. A better measure of absorptive capacity is actual versus planned disbursements, though this number is not readily available for many donors. However World Bank figures for the end of 1996 show that \$388 million of an expected \$407 million (95 per cent) had been disbursed; this percentage is 90 per cent if the one completed credit and \$150 million adjustment credit are excluded.

It therefore appears that implementation capacity is not so severely constrained as the cited figure of 30 per cent may suggest. Nonetheless, the annual pledges of around \$2 billion result in disbursements which have only just climbed above \$1 billion, so there may be some problem preparing projects for donor funding. A reason often given for this is that it is only a short time since many members of the donor community arrived and so time is required to gain familiarity with the different procedures of each. This argument has some merit, what is less clear is why the Government of Vietnam, which appears perfectly capable of carrying out its own expenditure programmes should have to comply with such a wide range of donors requirements.³⁰ Moreover the government is quite capable of determining its priorities and carrying out its own programmes accordingly: for example, there is great concern with “social evils” which precedes donor interest in this area and there are a number of own-initiatives on poverty (such as the Bank for the Poor, which donors do not support owing to the subsidised interest rate charged).

Other countries with high and continued levels of project aid finance bear witness to the adverse effects that may follow, in particular institutional destruction as the time of government officials is taken up with catering to donor needs (meeting visiting missions etc.) rather than carrying out their usual functions and as donors create project institutions that by-pass the usual government channels.³¹ Such a situation may still be avoided in Vietnam by adopting aid modalities which allow greater control by government.

6.3 The conditions for programme aid

The basic pre-conditions for programme aid are generally seen as being:

- macroeconomic stability
- liberalised and well-functioning forex and credit markets to allow the sale of programme aid funds
- a sound orientation in development policy
- capacity to implement sectoral spending programmes
- transparent budget with spending priorities in accordance with donor priorities

³⁰ Our impression is that the level of service delivery is extremely high for a country of Vietnam's income per capita, with a range of public services (libraries, parks and street cleaning) which are either non-existent or in a very sorry state in comparable countries. This capacity appears to extend to the social sector.

³¹ Virtually all domestic agencies in Vietnam have created an International Co-operation Department which has the task of dealing with external agencies, which is an appropriate institutional response to prevent other officials being deflected from their proper duties (the one exception we visited was the Bank for the Poor, which has been by-passed by the donor community).

Vietnam satisfies the first and second of these.³² The second is returned to below, as whilst Vietnam is currently less market-oriented than donors would like it can be argued that the latter perhaps ought be more modest in their policy demands. With regard to the third condition it was argued above that the government does have the capacity to carry out programmes it believes in: failings in the implementation of aid-financed projects should not be confused with a general absence of capacity. The fourth condition that of governance is more difficult. There is in Vietnam a strong genuine commitment to poverty alleviation and a wide concern about social issues, though having said that government spending can be argued to be misallocated both overall and in poverty reducing programmes. What is lacking is budget transparency, though this is an area of current negotiation, with government promising to publish 1997 budget outcomes in time for the 1998 CG meeting. A judgement therefore need be made if this one problem should delay a move to sector budget support given its advantages compared to the disadvantages of project support.

6.4 Concluding comment

Donor conditionalities and policy dialogue operate in Vietnam in a difficult environment. One position to take was voiced at the German embassy, that is to resort to a technical and supporting role in the reform process as Vietnamese policy making cannot be influenced in another way. Most donors have such projects, and we have argued that they can have a positive role, though one could wish for greater diversity of opinion than is seen at present. A second alternative is to wait until the crisis situation becomes untenable and reforms will have to take place. A third alternative is to have a 'modest' faith in the homegrown nature of Vietnamese reforms, which would warrant budget support. The big issue looming there is governance as in the absence of a clear and transparent budget such support may not be warranted, but there may also be grounds for some faith on these issues. The evidence does not really support the idea that corruption is more rife than in other countries enjoying the donors' favour, and capacity to implement expenditure programmes considerably higher. We propose a donor shift to budget support without delay.

³² Whilst there is a need for financial sector reform, it is not claimed that private sector firms are unable to access credit.

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Appendix 1

Terms of reference for an evaluation of programme aid

1. Background

Balance of payments support has constituted a considerable part of Swedish aid in the 1990s, but its share of total aid has declined in recent years. In 1990/91 balance of payments support represented over 20% of the aid channelled through Sida, or 1,607 million Swedish Kronor. It has then decreased to a total amount of 663 million Swedish Kronor in 1995/96, decreasing to 6% of total aid through Sida. Even though decreasing in volume and percentage, balance of payments support remains a substantial part of total aid.¹

The overriding objective of Swedish balance of payments support has, except for some minor changes over time, been: *economic growth and sustainable development*. Swedish balance of payments support has primarily been given to the poorest, most indebted, Swedish programme countries implementing a structural adjustment program with support from the Bretton Woods institutions². Since the majority of the least developed countries is found in Sub Saharan Africa the lion part of the assistance has been aimed to this region. While both bad economic management and external shocks have adversely affected the stability of the recipient countries, Swedish disbursements of balance of payments support have as a consequence been low and resulted in high balances.

¹ Swedish balance of payments support through Sida has been given both within the so called country frames and as special allocations in support of economic reforms. In addition to the Sida channel the Ministry for Foreign affairs directly supplies the World Bank and IMF with funds to support their credit schemes which also can be regarded as a balance of payments support. These funds are not included in the above figures.

² Programme countries are: Nicaragua, Ethiopia, Eritrea, Uganda, Kenya, Tanzania, Mozambique, Zambia, Zimbabwe, South Africa, Botswana, Namibia, Angola, Guinea Bissau, Cape Verde, India, Sri Lanka, Bangladesh, Laos and Vietnam. The concept of *programme countries* has now changed but we will stick to this term since we are looking back a few years to the time when they were still classified as programme countries.

There are different forms of balance of payments support. Some of the resources have been diverted to support the purchase of imported goods, other to pay off debts. Balance of payments support is also closely linked to the concepts of “budget support” and “sector programme assistance”. Budget support and sector programme assistance also provide the recipient country with untied resources. The collective term used for balance of payments support, budget support and sector programme assistance in this text is “programme aid”.³

This study is *mainly* concerned with balance of payments support, i. e. focuses on supplying the country with foreign exchange to sustain the balance of payments situation. However in today’s debate it has been increasingly important to discuss the use of the local currency generated by the forex. When a donor puts more emphasis on the fiscal situation and the use of local currency the term “budget support” or “sector programme assistance” is used. In this evaluation we will pay *some* attention to these forms of assistance.⁴

2. Reasons for the evaluation

In Government decision dated 1996-11-18 Sida was tasked with evaluating Swedish balance of payments support to selected countries. In accordance with these directives the Department for Evaluation and Internal Audit started an evaluation process aimed at assessing the effects of balance of payments support on economic growth to some recipient countries of Swedish assistance.

The globalisation of the economy has changed the conditions for giving balance of payments support in the 1990s, perhaps to a greater extent than for other forms of aid. It is therefore of interest to assess how the changing economic conditions have affected the possibility of this type of aid to achieve its objectives.

Balance of payments support has effects on foreign exchange availability, fiscal behaviour, monetary variables, economic growth and income distribution. In addition, balance of payments support is usually a vehicle for policy conditionality, which in turn also affects the above mentioned variables

Few assessments and evaluations have thoroughly reviewed how the *various* forms of balance of payments support help to achieve the objective of *economic growth and sustainable development*. One of the aims of balance of payments support has been to sustain reforms so that the country can adjust and reach stability. Another aim has been to create favourable effects in the economy through the resource transfer itself. How different forms of balance of payments support may contribute to economic growth is rarely elaborated on

³ In Sida terminology “budget support” is sometimes found under the heading “balance of payments support”.

⁴ The reason why focus is on balance of payments support in this evaluation and not equally focused on budget support is lack of many existing examples of budget support. Countries which have experienced this kind of assistance include Cape Verde, Mozambique and Uganda.

in the Sida memorandums preceding the choice of support, or in Swedish government decisions.⁵

3. Purpose and scope of the evaluation

The *purpose* of the study is to evaluate the impact of the resource transfers on economic growth. Furthermore, the purpose is to see how the change in economic policy in recipient countries of Swedish programme aid has changed the preconditions for achieving economic growth. Moreover the evaluation will assess whether the conditionality package attached to the support has been fulfilled in accordance with the timetables and, lastly, the evaluator are to review the literature on how reforms have affected economic growth.⁶

The study shall present *recommendations* on the use of different forms of balance of payments support, the use of budget support and the use of sector programme assistance as instruments for enhancing growth. Recommendations should be directed to Sida and to the Ministry for Foreign Affairs. Information about the evaluation findings is to be communicated to the recipient countries.

The evaluation shall consist of case studies and desk studies. The objects for the *case studies* are Uganda and Nicaragua. An additional Swedish programme country constituting a third case study is left to be suggested by the evaluators to complement the two predetermined ones. The two countries, Uganda and Nicaragua, represent major recipients of Swedish balance of payments support with untenable balance of payments situations as main obstacles to self-sustained development. The purpose of conducting case studies is to enable the evaluators to search for primary data and conduct interviews with key persons (in addition to the use of data bases and existing literature).

The selection of countries for the desk studies, and a third case study, will be a matter for the Tender Invitation. The selection will have to be confined to Swedish programme countries receiving programme aid . The desk studies are to make use of existing data bases and review the literature to complement the case studies in search for general conclusions.

The evaluation shall cover all forms of balance of payments support, budget support and sector programme assistance provided by Sida. There is no point in distinguishing Swedish support from other donors' balance of payments support because of fungibility. The evaluation shall mainly concentrate on support given in the 1990s.

⁵ In an open economy situation with perfect capital mobility this is less interesting since the forex most probably is fungible, but looking back a few years this was not the case in many countries.

⁶ In most countries the conditionality package means the Policy Framework Paper prepared by the Bretton Woods Institutions.

4. The Assignment

The study shall comprise of the following tasks;

(A) The rationale behind the Swedish support

The assessment in (A) and (B) will be based on all Swedish programme countries that received Swedish programme aid 1990-1997.

1) Distinguish between the explicit objectives of different forms of Swedish balance of payments support (import support and debt relief), budget support and sector programme assistance through Sida to the programme countries since 1990 until 1997 and analyse how these objectives have changed over time⁷

2) Assess the relevance of the stated objectives for Swedish balance of payments support, budget support and sector programme assistance in relation to the support form⁸

3) Examine the Sida memorandums sent to the Swedish government, and the Swedish government decisions on balance of payments support, budget support and sector programme assistance, to assess the *rationales* behind giving support and analyse how they have changed over time

(B) Reviewing different forms of Programme Aid

1) Review the different Swedish forms of balance of payments support, budget support and sector programme assistance, and their respective categories, to determine how much of the funding has been disbursed between 1990 and 1997.⁹

2) The evaluators are also to elaborate on how the balance of payments support and budget support/sector programme assistance relate to each other *conceptually and in practice*.

(C) Concluding fungibility

The assessment will be based on findings from both the case studies and from the desk studies concerning a total of eight selected countries. This also applies to D and E. The findings are to be based on empirical work.

1) Examine how economic policy, affecting the effectiveness of programme aid, has changed in the selected Swedish programme countries during the 1990s.

⁷ There are a limited number of cases where budget support and sector programme assistance have been the targeted form of support, and the comparisons between balance of payments support and these “newer” forms will therefore be restricted by the availability of data.

⁸ In case of lack of relevance in the stated objectives the evaluators are to suggest an additional set of objectives relevant to and adequate for this kind of support in order to carry out the evaluation in relation to appropriate objectives

⁹ Forms of balance of payments support; import support and debt relief. Categories of import support; consumer goods, intermediate goods and capital goods.

Categories of debt relief; e.g. fifth dimension, multilateral debt funds.

2) Examine the various sources and uses of foreign exchange, including balance of payments support given by donors.

3) Conclude to what extent fungibility exists in the balance of payment identity when there is an inflow of balance of payments support, and under what economic policy conditions the degree of fungibility may change.

4) Conclude to what extent fungibility exists in the categories for debt relief and import support, and under what economic policy conditions the degree of fungibility may change.

5) Analyse how budget support may affect the country's balance of payment situation and vice versa, i. e. how balance of payments support may affect the country's budget situation given at least two scenarios, viz: a) a regulated economy b) an open economy.¹⁰

(D) Assessment on how balance of payments support may have contributed to growth

1) Examine the possible *chain of effects* between the balance of payments support and economic growth:

- a) when there is high probability of fungibility (open economy- no restrictions on aid),
- b) when there is low probability of fungibility (regulated economy- restrictions on aid).

In (a) an assessment on how an increment of “untied” foreign exchange has affected growth is to be carried out. In (b) an assessment will be carried out specifying the different forms of balance of payments support (and their categories) and their respective impacts on growth via intermediary variables. The following relationships are to be considered in the evaluation for both (a) and (b):¹¹

- how balance of payments support forms may have affected growth via macro stability (prices, real interest rate and real exchange rate),
- how the balance of payments support forms may have affected growth via movements in the real exchange rate,
- how balance of payments support may have reduced the debt overhang and have affected growth via increased investments
- how balance of payments support may have affected growth by an increase in imports,

¹⁰ Above all theoretically, but also empirically if the availability of primary data allows to.

¹¹ It might be useful for the evaluators to distinguish between the short-term objectives of the support (intermediary variables) and its long-term objectives (growth in output). The evaluators are to try to

¹² For import support and debt relief the evaluators are also to distinguish between the effects from different categories i.e. in a low probability of fungibility of funds scenario (b).Appendix 2quantify the impact of the support on intermediary variables and (if possible) on growth.

- how balance of payments support may have affected growth by an increase in international reserves.¹²

It is important to clarify under which economic policy conditions the conclusions are valid (regulated economy vs. open economy).

It is also important that the evaluators make clear in the report which factors they respectively control for and not do control for.

2) The evaluation shall discuss whether the chosen form (and category) of balance of payments support, in comparison with other forms (and categories) of balance of payments support, has been an effective and relevant mean to achieve a favourable impact on intermediary variables and a contribution to economic growth.

3) Examine empirically (if possible) the possible *chain of effects* between the budget support and sector programme assistance and economic growth, also taking into account relevant intermediary variables

(E) The implementation and the effects of reforms

1) Examine how many and which of the reforms conditioned to the balance of payments support have been implemented in accordance with the timetables. The evaluation shall also make an assessment on the implementation status of the reforms that lagged behind time schedules – how far/close to fulfilling the schedules they were.

2) Examine if in general any specific groups of reforms lagged behind timetables and if in general any specific groups of reforms were implemented in accordance with the timetable.

3) Review the literature to summarise the findings about how policy changes – due to the conditionality package – have affected growth; generally in developing countries and specifically in the Swedish programme countries.

(F) Present lessons learned as well as recommendations related to the findings on above issues

1) Compare the *impact* of the various forms of balance of payments support on growth and conclude under which policy conditions one type of support is to be preferred to another.

2) Compare balance of payments support with budget support and discuss under which policy conditions the donor shall focus on the balance of payments situation rather than the fiscal situation or vice versa, and when it is of equal importance to focus on the balance of payments situation and the fiscal situation.

3) Compare the conclusions from the above – the actual results from the case studies and desk studies – and assess the relevance of the stated objectives and rationales in Sida memorandums.

4) Discuss *briefly* the impact on economic growth of programme aid in relation to the impact on growth of other forms of assistance, including project support

(G) Statistical data and methods

1) Discuss the statistical basis used and assess the extent to which lack of data, economic models and other knowledge about constraints in the data and methodology affects the results. Discuss how this uncertainty may affect the conclusions and recommendations.

5. Methods, Evaluation Team and Timetable

The evaluation shall be undertaken in close cooperation with Sida and the relevant authorities in the countries selected for the case studies. The three case studies require field studies in the respective countries. Contact persons have been identified in the Nicaraguan and Ugandan administrations. The Department for Evaluations and Internal Audit also reserves the right to take part in one of the field visits by agreement with the contracted team.

The study should take into consideration earlier evaluations of balance of payments support (see especially *Evaluating Programme Aid, Volume III, Annotated Bibliography, ISS*) and other relevant documents, specifically the ongoing evaluations of “The Special Program of Assistance for Africa (SPA)” and IMF’s evaluation of the ESAF.

National statistical sources and comparable international sources will be used along with interviews and discussions with key-informants. Under (A) and (B) a Swedish-speaking team member is necessary. For foreign firms this might mean linking a Swedish researcher or consultant to the team. For the fungibility assessment (C) both *a quantitative and a qualitative* approach will have to be applied. Much emphasis will have to be put on collecting primary data in the respective case studies. To sustain the quantitative work in assessing fungibility the qualitative work will have to be built on systematic interviews with key officials in the administrations. Both *quantitative and qualitative* work have to be employed in (D) as well, specifically the qualitative work will have to encompass systematic interviews with the private sector to determine what factors influence private investments (the World Bank is now preparing a survey on this issue in Uganda and the evaluators may possibly be able to use some of their findings).

We recognise the difficulties in concluding fungibility, especially for the desk study countries. Naturally, we only expect the evaluators to carry out qualitative work in the case study countries (in addition to quantitative work). For the desk study countries we encourage the evaluators to make use of available data for the quantitative work and findings from previous studies to conclude fungibility and assess the impact on growth.

When statistical methods are employed the evaluators should attempt a consistent use of sensitivity analysis using different assumptions.

The evaluation will be carried out by a team with profound knowledge of and experience in:

- macroeconomics analysis,
- national accounts and balance of payment statistics,
- economic policy and government systems in developing countries,
- ability to speak and write in English and Spanish.

The team-leader is to have documented experience of evaluation in a team-leading position.

The study is envisaged to require an estimated 80-100 man weeks.

The *tentative* time schedule for the evaluation is:

- Nov 1997: Tender for consulting services.
- Dec/Jan 1997: Contracting the winning tender for the evaluation.
- Feb 1997: Preparation of inception report, including work plan.
- Oct 1998: Submission of annexes or background reports.
A seminar to be held at Sida in Stockholm.
- Nov 1998: Submission of a main report and the annexes
or background reports.

6. Reporting

- a) An inception report shall be presented to Sida commenting and interpreting the terms of reference for the assignment. The inception report shall include a work plan for how and when the work will be carried out.
- b) In connection with the field visit a debriefing shall be held reporting to relevant parties in the recipient country.
- c) A main report with findings, conclusions and recommendations from the case studies and the desk studies is to be prepared. The main report shall keep an educational format and the more technical discussions are to be left in the annexes or background reports.
- d) Draft reports for the desk studies and the case studies, showing the analysis made and methods used, findings and conclusions, shall be presented together with the main report. The case studies, building on field visits to three countries, shall be presented in different reports for each country. The desk study for the five countries can either be presented in one report or several reports depending on the methods employed by the evaluators. The reports can then either be appended to the main report or separate background reports.

The main report shall be written in English and should not exceed 80 pages each, excluding annexes. The outline of the reports shall follow Sida Evaluation Report – a Standardised Format (see Annex 2). Five (5) copies of each of the draft case studies and draft desk studies shall be submitted to Sida no later than October 30, 1998. Within five weeks after receiving Sida's comments on the draft reports, a final version of each case study and a main report in two copies each and on diskette are to be submitted to Sida. Subject to decision by

Sida, the reports will be published and distributed as publications in the Sida Evaluations series. The evaluation reports shall be written in Word for Windows or a compatible format and should be presented in a way that enables publication without further editing.

The evaluation assignment includes production of one summary according to the guidelines for Sida Evaluations Newsletter (Annex 3) and the completion of Sida Evaluations Data Work Sheet (Annex 4). The separate summary and a completed Data Work Sheet shall be submitted to Sida along with the main draft report.

Appendix 2

List of persons met

Henny Andersen, Economist, Embassy of Sweden

Brian van Arkadie (consultant) [interviewed during visit to ISS, The Hague]

Ellen Berends, Counsellor, Embassy of Netherlands

Thierry Blin, Commercial Attache, Embassy of France

Bui Anh Tuan, Vice Dean of Postgraduate Faculty, National Economics University

Cao Duc Phat, Director, Department of Agricultural and Rural Development Policy, Ministry of Agriculture and Rural Development

Chu Thi Hao, Deputy Director, Department of Agricultural and Rural Development Policy, Ministry of Agriculture and Rural Development

Stefan Dahlgren, First Secretary, Development Cooperation, Embassy of Sweden.

Dang Kim Chung, Head of Section, Planning and Foreign Relation, MOLISA

Dr. Dinh Trung Tung, Head of Department of Civil and Economic Laws, Ministry of Justice

David Dollar, former World Bank country economist, World Bank [interviewed in Washington D.C.].

Dr. Duong Duc Ung, General Director, Department of Foreign Economic Relations, Ministry of Planning and Investment

Robert Glofcheski, Senior Economist, UNDP

Ha Thi Hanh, General Director, Vietnam Bank for the Poor

David Holmertz, First Secretary, Embassy of Sweden

Neal Forster, Project Economist, UNDP

Jost Peter Kadel, Second Secretary, Embassy of Germany

Professor Dr. Luong Xuan Quy, Rector, National Economics University

Kazi Matin, Lead Economist, World Bank

Nguyen Bich Vuong, Deputy Head International Cooperation Department, Vietnam Women's Union

Nguyen Cat Giao, Director, International Cooperation Department,
Ministry of Agriculture and Rural Development

Nguyen Duc An, Standing Deputy Director, Projects Coordinating
Department, Ministry of Health

Nguyen Duc Toan, Deputy Director, NEU Business School

Dr. Nguyen Huu Dzung, Director, MOLISA

Dr. Nguyen Le Minh, Vice Director General, MOLISA

Dr. Nguyen Minh Tu, Director, Economic Management Policy Research
and International Cooperation, CIEM

Nguyen Thanh Ha, Director, International Cooperation Department,
National Economics University

Nguyen Thi Thanh Ha, Committee for Foreign Aid Management and
Reception, Ministry of Finance

Nguyen Tien Thanh, External Finance Department, Ministry of Finance

Erik Offerdal, Resident Representative, IMF

Bengt Rudolf Personn, Project Team Leader (statistics), Statistics Sweden
(in MPI)

Pham Cong Minh, Committee for Foreign Aid Management and
Reception, Ministry of Finance

Pham Hoai Giang, Chair of International Relations Department, Vietnam
Women's Union

Pham Quang Trung, Deputy Director, NEU Business School

Rolf Samuelson, First Secretary, Embassy of Sweden

Paul Stott, Principal Operations Officer, World Bank

Tetsumi Murata, First Secretary, Embassy of Japan

Tran Minh Huan, General Director, Department of International
Cooperation, Ministry of Industry

Tran Phi Tuoc, Deputy Director, Department for International Relations,
MOLISA

Truong Thi Khue, Vice President, Vietnam Woman's Union

Dr. Brian van Arkadie, consultant (interviewed in the Hague)

Jean-Pierre Verbiest, Resident Representative, Asian Development Bank

Dr. Vu Van Me, Senior Expert, International Cooperation Department,
Ministry of Agriculture and Rural Development

Vu Xuan Nguyet Hong, Senior Economist, International Cooperation
Division, CIEM

Dr. Peter Wolf, Economic Advisor, GTZ/CIEM

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Evaluation of Swedish Programme Aid

Does Swedish debt relief contribute to economic growth? Does economic growth reach the poor? Does Sweden influence policies in partner countries? Have donors supported the “right” reforms? These are some of the questions discussed in this evaluation of programme aid, with an emphasis on the Swedish experience.

Programme aid – that is, import support, debt relief and budget support – has constituted a considerable part of Swedish aid in the 1990’s. However, the volumes of programme aid have fallen both in relative and absolute terms during this same period. Few evaluations have assessed how different modalities of programme aid further economic growth and sustainable development. Sida therefore commissioned an evaluation of programme aid with a twofold purpose. Firstly, to assess the impact of aid on the policy dialogue, as well as on the outcome of the policies. Secondly, to assess the impact of aid transfers on economic growth including the distributional effects. Thirteen working papers have been synthesised into the final report “Dollars, Dialogue and Development”. The working papers comprise field studies of three countries; Nicaragua, Uganda and Vietnam and desk studies of five countries; Bangladesh, Cape Verde, Mozambique, Tanzania, and Zambia. Furthermore, three thematic studies have been carried out on conditionality, impact of adjustment policies and modalities of programme aid respectively. Finally, there is a study of the management of Swedish programme aid.

The evaluation was commissioned by Sida’s Department for Evaluation and Internal Audit which is an independent department reporting directly to Sida’s Board of Directors. The evaluation has been carried out by the Institute of Social Studies (ISS), The Netherlands.



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