Vietnam 2001: Entering the 21st Century

Overview
Vietnam's Socio-Economic Development Strategy for the first decade of the 21st Century is currently under preparation. The Strategy envisages a Vietnam that has:

- An economy with sustainable and rapid development;
- Aspires to be a just and stable society with a high quality of life for all of its people;
- Maintains the best of Vietnamese culture and traditions;
- Aims to become a socialist market economy, fully integrated into the global economy, and competitive internationally, and;
- Intends to have the characteristics of an industrialized and knowledge-based society within 20 years.

This vision is articulated using specific targets. Among the quality of life targets for 2010 are the following:

- Eradication of hunger and hard-core poverty;
- Universalization of lower secondary education for all;
- Malnutrition rate of children to be reduced from a third to 15-20 percent;
- Life expectancy to increase from 68 to 70-71 years;
- Access to clean water in urban areas to rise from 65 percent to 90 percent, and;
- Forest coverage to rise from 28 percent to 43 percent.

These are to be attained through rapid growth and a change in the structure of the economy to a more modern, industrial and urban one that can create better-paying jobs: a doubling of GDP by 2010 to be attained through economic growth of over 7 percent per annum; investment to be increased to 30 percent of GDP; exports to grow at more than twice the rate of GDP; the share of agriculture in GDP to decline from 25 percent to 16-17 percent; industry to increase from 35 percent to 40-41 percent; services to increase from 40 percent to 42-43 percent; the share of rural employment to decline from about two-thirds to half; and the share of urban population to increase from a quarter to a third.

These are ambitious goals, but appropriate. While the progress achieved over the past decade has been impressive by almost any standards, Vietnam remains a very poor country whose huge development potential is as yet largely untapped. While the share of the population in poverty has been cut in half over the past decade, some 30 million people, or around 37 percent of the population, are estimated to live in poverty.
Currently, around 25 million people accounting for 60 percent of the labor force are unemployed or underemployed. And each year in the coming decade, over 1 million people will be added to the workforce.

This report explores the steps required to reach Vietnam's development goals over the coming decade. It begins with an analysis of the economic framework for equitable growth and poverty reduction for the coming 10-year period. It finds that the proposed growth rates, and their linkage to savings and investment rates and to the external accounts are internally coherent, and consistent with what has been achieved in other East Asian countries at similar periods of development. But drawing upon the experience of other countries, it is clear that achieving the goals will require serious policy and institutional change across a broad array of activities.

Vietnam's strategy calls for not only a high "quantity" of growth, but also a high "quality". Experience around the world shows that while growth is essential to reduce poverty, similar growth rates can have very different impacts on poverty reduction. Vietnam's goal is to share the fruits of growth broadly across all segments of the population, and also to avoid the inequities, social exclusion, and environmental degradation that has often accompanied other countries' rapid economic growth.

This is a difficult challenges, calling for a comprehensive approach to policy and institutional change. With this in mind, this report is organized around six development "pillars" that will need to be built - and have been identified by the government - if the goals are to be reached. In the coming decade strong actions will be required by government, and strong support from Vietnam's development partners, in:

- Creating a Supportive Climate for Enterprise;
- Transforming the Rural Economy;
- Enhancing Human Capacity;
- Providing Efficient Infrastructure Services;
- Improving Environmental Quality, and;
- Building Modern Governance.

In each of these areas, the report draws upon the experience of other countries to recommend the steps that will be required to reach the targets set out in the strategy. Without progress on all fronts, Vietnam will not be able to achieve the economic and social transformation that it desires.

A balanced attack across all fronts does not, however, imply that everything needs to be done at once. What is needed to prioritize actions is an identification of the
bottlenecks - the hard-to-solve problems that are impediments to success - and to attack these first. Vietnam's development partners have an important role to play in helping to make all of Vietnam's resources - including ODA - more effective.

Cutting across these development pillars are a number of large - and difficult - decisions that Vietnam is struggling with, and which will fundamentally affect its development path in the coming decade.

I. THE ECONOMIC FRAMEWORK FOR GROWTH AND POVERTY REDUCTION
On the face of it Vietnam's growth targets for the 2001-2010 period appear well within reach. Over the past decade, Vietnam has scored better on most of the aggregate indicators than are targeted in the coming decade. In reality, however, it is likely that continuing the growth rates of the 1990s will be more difficult, for two reasons:
* First, the dramatic supply response following the sequential liberalization of agriculture, small scale services, and foreign investment is no longer available. It needs to be supplemented by an equal liberalization in the manufacturing sector, where the supply response cannot be taken for granted, but will need to be earned through a consistent incentive framework;
* Second, the kinds of policy changes required to promote a new round of growth - discussed in the next section - are technically, politically and socially more difficult than those of the first round of doimoi.

The doubling of the size of Vietnam's economy envisaged over the coming decade, will need to be accompanied by a shift in the structure of the economy. The shift envisaged in the strategy - whereby agriculture continues to decline in importance, while industry becomes the key driver - is consistent with the pattern in other successful East Asian countries at similar stages of development.

This shift, whereby workers gradually move out of agriculture into better paying jobs in manufacturing, and thus enabling those staying in agriculture to enjoy higher returns, is essential to further success in rapid poverty reduction. But it also raises important challenges, and introduces potential social and environmental stresses. Other countries that have paid inadequate attention to balanced growth have found that such phases have been accompanied by growing inequalities, and widening urban-rural gaps.

Poverty reduction is envisaged under two scenarios. In both scenarios overall economic growth is assumed to be 7 percent per year, but in the first the growth is assumed to be shared equitably across all areas and people. In the second scenario it is assumed that rural GDP rises at the same rate as the growth of agriculture (assumed to be 4 percent per year), while urban GDP grows at roughly the rate of the industrial sector (about 10 percent per year).
Under the first scenario the number of people in poverty falls by almost 20 million over the decade, and median expenditures rise by 70 percent, while under the second, the number in poverty falls by only 12 million, (and most of those remain highly vulnerable to shocks that would push them back into poverty), and median expenditures rise only half as much - by only 34 percent. Should Vietnam be successful in achieving 7 percent growth, the actual outcome in terms of poverty reduction is likely to be between these two scenarios. Just where within this range will depend on policies chosen, and will fundamentally affect Vietnam's development trajectory, its social structure and its rural-urban drift for decades to come.

For all these reasons the comprehensive approach to development suggested in the government's strategy document and explored in chapters 2 -7 of this report is so important. In this regard, also, the approach of this report picks up from last year's Vietnam Development Report, "Attacking Poverty", which laid out a three-fold imperative for poverty reduction. First, opportunity - access to jobs, credit, land, education etc - must be provided. Second, measures to ensure equity - in access to services, jobs, and investments - must be implemented. Third, special actions to address vulnerability - to disease, job loss, and natural disaster - should be given priority. Last year's report ended with a recommendation that these imperatives should be factored into all of the areas now addressed in this year's report.

2. CREATING A SUPPORTIVE CLIMATE FOR ENTERPRISE
Vietnam's strategy recognizes that in order to achieve the goals for the coming decade, the rate of investment will need to be raised (from the present 23 percent to 30 percent), and the productivity of investment will need to be raised. This raises three difficult challenges:

- How to generate a climate in which investors are willing to take risks and invest;
- How to raise domestic and foreign savings so that the investment can be financed, and;
- How to tap into knowledge and technology, so that productivity of investment can be increased.

Fortunately, there is a set of measures - integration into the world economy, empowering the private sector, and reforming banking and state-enterprise systems - that will help address these challenges simultaneously. The government has decided in principle to move resolutely to adopt these measures in the coming years. What will be necessary to create a strong response from investors and savers will be early indications of credible and effective implementation.

**Integration Into the World Economy.** Over the past decade, Vietnam has significantly opened up to international trade and investment. Exports are equivalent
to 44 percent of GDP (compared to an average of 27 percent for developing countries) and the share of the non-state sector in exporting has risen from near zero at the beginning of the decade to 65 percent today. Nonetheless, Vietnam's trade regime today remains distorted, with effective rates of protection of over 100 percent in many industries.

While this has encouraged investment in these highly protected industries, it has enabled these industries to stay uncompetitive, and has led to high prices for Vietnamese consumers and businesses. Businesses have to pay higher prices for steel, cement and telecommunications, thus placing them at a serious competitive disadvantage; farmers have to pay 40 percent more for fertilizers than farmers in other countries (while also being penalized by rice export quotas); and consumers have to pay twice as much for goods such as electric fans and motorcycles than citizens in surrounding countries.

Like a growing number of countries, Vietnam recognizes that the process of globalization presents both an opportunity and a challenge. Vietnam's decision to honor its commitments under Afta and to sign the Bilateral Trade Agreement with the US, will have great gains for Vietnam in terms of exports, investment opportunities, acquisition of technology, and poverty reduction. Indeed, it would be wise to accelerate the implementation of commitments made under Afta.

By agreeing on a specific time-bound program of integration over the coming years, Vietnam is acting smartly. It gives potential investors a clear timeline, and thus facilitating investment preparation; and it gives those industries which may be adversely affected clear notice that they must adapt or downsize. It is vital that actions follow the announced timeline, as slippages will threaten the credibility of the entire transition. The time must be used wisely in the interim to put in place a clear and supportive social safety net for any workers who may need to shift industries, and also to build flexibility in the SOE sector. There is a serious risk, however, of investing heavily in SOEs in the near term in an effort to make them competitive when protection is reduced.

In our view, Vietnam's target export growth of 15 percent per year on average in the 2001-2010 period is attainable if it follows through on its trade policy decisions.

**Encouraging the Private Sector.** If investment rates are to rise as needed, we estimate that domestic private investment will need to rise from the current low level of around 7 percent of GDP to 12-15 percent of GDP for the 2001-2010 period. To date in Vietnam the climate for the private sector has been grudging rather than supportive. Here Vietnam differs markedly from China, where the private sector has been recognized as a key partner in development and poverty reduction. During the 1990s the number of private firms in China increased more than ten-fold (from 100,000 to well over 1 million), while private output and employment grew at average
The Enterprise Law, which has substantially simplified business start-up has led to the registration of more than 10,000 additional domestic firms in the first nine months of this year. However, domestic firms still number less than 30,000 and produce well under 10 percent of GDP. A major recent analysis of the private sector in China finds that changing attitudes - of officials and bankers - towards private enterprise, are often even more important than improvements in the legal and regulatory framework.

The draft strategy promises a level playing field for the private sector. This will require three sets of actions:

- A shift in the social and administrative culture from one of reluctance and control towards one of active support and encouragement;
- An introduction of a transparent and predictable regulatory framework, where discretionary actions on the part of officials are minimized, and;
- Development of a financial system that allocates funds based on risk and expected return, and a clearer legal framework for land use rights and collateral arrangements.

Mobilizing Foreign Direct Investment. The government rightly envisages foreign investment playing an important role in bringing investment and technology into Vietnam. During the past decade Vietnam benefited disproportionately from direct investment inflows which were on average equivalent to 5.5 percent of GDP (compared to an average of 0.9 percent for all developing countries and 1.1 percent for China). The government projects a similar level of inflows for the current decade.

This is possible, but not under the present environment. The large inflows of the mid-1990s must not be understood as normal. Vietnam's attractiveness has sunk in recent years as other countries have become more attractive, and the high cost of doing business in Vietnam - in the form of delays in approvals, perceived capricious shifts in the regulatory environment, corruption, weak access to the Internet, very high telecommunications charges etc - have become evident. These perceptions can be reversed with strong action, but even so, Vietnam should realistically be aiming at inflows of US$1 billion per year in the near term rather than the $2 billion envisaged.

Reforming Banks and State-Owned Enterprises. Vietnam's economic goals remain seriously threatened by a large number of loss-making SOEs, whose inefficiencies are enabled by a banking system that is in turn weakened by them. SOEs still absorb around half of all bank credit, while contributing no significant employment growth. By enjoying preferential access to the state banks they have delayed the introduction of modern banking methods and contributed to a large overhang of non-performing loans (estimated at $2 billion-$4 billion).
The government's announcement to move forward with banking and SOE reform offers hope that this major impediment to development can be addressed. The government's plan to equitize, divest or close one-third of the 5,300 SOEs in the coming three years is an important step, which if implemented firmly can make a very positive contribution. But even more important will be the policies adopted for the remaining SOEs.

The parallel recent decision to reform the state banking system - by separating commercial from "policy" lending, systematically addressing the problem of non-performing loans, and creating incentives for sound banking - is a central element to the solution in that it will over time prohibit the roll-over of bad loans. But serious banking reform will take at least five years, and will require a cultural and behavioral shift within the banking profession, as well as strong leadership from the top. In the meantime, it is vital that the SOEs be subjected to greater discipline and transparency. The government's decision to expose some of the major SOEs to international-standard audits will help. Publishing audited accounts so that policymakers and citizens can know how public assets are being managed will help more.

At root there remains an internal contradiction in the draft strategy with regard to the role of the SOE sector that will need to be addressed if Vietnam's goals are to be reached. Associated with this is a risk that heavy investment will be channeled to the SOEs in the near term in an effort to prepare them for the competitive environment they will need to face in later years. Such investment needs to be undertaken with great care. Experience in numerous countries suggests that usually rather than preparing domestic enterprises for competition, such actions serve to build up opposition to such competition.

3. TRANSFORMING THE RURAL ECONOMY

The coming decade will need to see dramatic changes in rural areas if Vietnam is to achieve its development goals. Raising living standards in rural areas - the home of 75 percent of the population and 90 percent of the poor - is perhaps the most difficult challenge facing Vietnam in the coming decade. Already, farm sizes, on average only 0.8 hectare, provide only part-time work for most farm families, and the lack of growth of off-farm opportunities has been a major disappointment of the last decade.

Like all low income agricultural countries, Vietnam needs to adopt a seemingly paradoxical stance of giving a high priority to raising agricultural productivity while recognizing that success can come only as agriculture declines as an employer of labor. In transforming the rural sector so that it helps rather than hinders the attainment of the development vision, Vietnam faces four rural imperatives.

**Intensifying Agricultural Production.** The successful growth of agricultural
production (4.9 percent average annual growth) during the 1990s was largely due to increased labor and capital inputs, which combined accounted for 87 percent of the growth. Land expansion accounted for 9 percent of the gains, and technology improvement only 4 percent. Vietnam's rice yields are still well below China's, offering scope for further gains, but the coming decade will need to see different drivers of growth, with a greater role for technology change and new varieties. This will require more attention to research and dissemination. Vietnam spends only 1.7 percent of its public agricultural budget on research in comparison with 6 percent in China and 10 percent in Malaysia and Thailand.

Vietnam has good opportunity to switch public agricultural allocations from production SOEs towards research and extension. Related, it will be necessary to open up supply industries, especially seeds, to full private involvement, if yields are to be increased.

**Diversifying Agriculture.** Rice, which accounts for over 60 percent of agricultural land, will need to decline in relative importance if the goal to double the average agricultural product to $2,000 per hectare is to be reached. Despite an official policy which supports diversification there remain local pressures to produce rice. Huge opportunities exist for higher value-added crops if a more supportive climate can be provided. A possible problem with the approach established in the strategy, which sets out production targets for a whole range of products, is that farmers may be encouraged to invest in growing particular crops either through incentives such as additional land or subsidized credit or through lack of alternatives and restrictions on land use.

A key question will be how to encourage diversification without introducing new distortions? An alternative to the more directive approach followed in the recent past would be one which:

- Gives farmers as much information (technical and market) as possible in a comprehensible form;
- Allows farmers access to credit at positive real interest rates;
- Creates a supportive physical infrastructure;
- Promotes the growth of agro-industry, particularly the private sector and facilitates access to international markets, and;
- Allows farmers to make up their own minds about the most appropriate investment for their farms.

**Promoting Off-farm Employment.** In every country that has successfully modernized, labor has been drawn out of agriculture into higher value-adding industry. Such a transition will be important in Vietnam not only to enable the industrial growth
required to drive growth, but also to increase productivity and to enable agricultural wages to rise. If farmers are to enjoy the same real income gains as the population as a whole, the number of workers in agriculture will need to fall significantly over the decade. In order to cater for these workers, plus the bulk of the expected increased rural workforce (thus preventing an explosive urbanization), the rural industrial picture in Vietnam will need to change dramatically.

Unlike China, Vietnam has little experience of rural industrialization. Promoting the private SMEs that must drive this process requires the same policies as to promote private investment in any areas (see above), but in addition will require increased investment in rural infrastructure, and in rural-urban transport. Provincial and district authorities will be key in ensuring that the reforms undertaken at the national level translate into an enabling environment for enterprise development in rural areas. Information and resources often take time to filter down to the local level and this could mean that reforms for enterprise development happen more quickly in some areas than in others.

**Targeting Remote and Upland Areas.** Special attention will be needed for the poorest areas. Rural poverty is widespread but is much more severe in some regions than in others. In particular, high rates of poverty persist in upland, ethnic minority areas. In 12 out of 13 of the poorest provinces (those with more than 60 percent of the population below the poverty line) ethnic minorities represent at least half of the population. This compares with an ethnic minority share in the overall population of 15 percent. Although ethnic minorities have enjoyed rising expenditures and improved socioeconomic indicators, improvements in their living standards lag well behind those for the majority population.

Ethnic minority areas have benefited from targeted programs, but their effectiveness has clearly not been sufficient to address their persistent poverty. The current focus on "sedentarizing" ethnic minority groups could usefully be replaced by much more intensive research into agricultural options for upland farming systems. This would need to be reinforced by extension services, which are responsive to traditional knowledge and farmers' needs and which can disseminate information to non-Vietnamese speakers, and land titling measures that are more in line with ethnic community traditions, practices and systems of land use.

**4. ENHANCING HUMAN CAPACITY**

Almost all indicators of human well-being have improved markedly throughout the 1990s and Vietnam has generally outperformed countries at similar income levels. For example, its net primary school enrollment rate (92 percent) and its adult literacy rate (94 percent) are amongst the highest in the developing world. Similarly its infant mortality rate (37 per 1,000) and its life expectancy (67 years) are significantly above international norms. As over the coming decade Vietnam seeks to build on this progress, it will need to address some significant challenges.
Improving the Quality of Social Services. The emphasis in the past has been on quantitative achievements: getting kids into schools, establishing an extensive health care delivery network, and target-driven reductions in population growth. The emphasis now needs to shift to improve the quality of these services and to facilitate people to make well-informed choices. In education, quality at all levels needs improvement. The basic education curriculum needs to be modernized by moving away from a system that emphasizes the recall of memorized facts, to a modern, dynamic and flexible knowledge system that encourages creative thinking and is able to make Vietnam the knowledge-based economy that it aspires to be. There is also an acute need to raise the quality of health care services, particularly at the commune and district levels.

Technical quality of services can be improved through in-service training, supervision, and quality assurance mechanisms. Public health services need to become more client-friendly and adopt a culture of service. In the field of reproductive health, the government is moving towards better preventive measures, such as counseling and information, education and communication practices, a wider choice of contraceptive methods and the improvement of staff. Improving the quality of education and healthcare will require measures to improve the training and compensation of the service providers.

Ensuring Equitable Access for all Groups. Despite widespread expansion in the provision of basic social services, gaps exist in the access to these services by groups differentiated by income levels, geographical location, gender and ethnicity. Social indicators are worse for the poor and for those living in upland areas. Ethnic minorities are particularly disadvantaged and vulnerable, and gender gaps are widening in some areas. During the transition to a market-economy, some public services that had earlier been provided at local levels - such as public creches - are no longer provided, and the burden on women has increased. The adult malnutrition rate, which was the same for females and males five years ago, is now higher for females (30 percent) than for males (25 percent), although both remain much too high.

During the coming decade, the government has announced that it will give extra effort to close the gaps between the more disadvantaged groups and the others. In education, specific programs need to be developed to respond to the needs of ethnic minorities, for example through bilingual education, and to lessen the gaps in the quality of education for different regions, income, and gender groups. School feeding programs might be necessary to create incentives for poor children living in upland and remote areas to attend school. Participation of local communities, parents and children in education management and planning is critical to sustained improvements in the sector.

Special attention to the poor is also needed in health care, where formal arrangements
fail to protect the poor. The health insurance scheme only partially covers lower income groups, the exemptions system does not work properly, and out-of-pocket payments for the poor remain very large relative to their incomes. The government's targeted program of assistance - the Hunger Eradication and Poverty Reduction (HEPR) Program - could play an important role in identifying the poor and providing targeted assistance to meet their needs, if a number of weaknesses are properly addressed. Finally, it is important to improve the effectiveness and efficiency of social safety nets and disaster management mechanisms in order to better protect vulnerable groups against the negative impact of individual and community risks.

**Improving the Level and Allocation of Public Expenditures.** Public expenditure levels in basic social services in Vietnam are currently low when compared with other developing countries. Public spending on health has grown rapidly over the past five years, reaching 7 percent of the budget in 1998 (about 1.4 percent of GDP), but this remains low by international standards. As a result, households finance 80 percent of total healthcare spending in Vietnam. There may be scope for reallocating public expenditures in health away from curative care, which currently absorbs 70 percent of the health budget, towards preventive care which receives just 15 percent of the budget, but the priority should be to increase the level and efficiency of spending overall.

In education, there is also a need to raise public spending and to improve its allocation across regions and provinces. Total education and training expenditure has grown significantly over the past five years, reaching 17 percent of total public spending (about 3.5 percent of GDP). But nearly half of total spending on primary education is financed by households, which implies an undue burden on the poor. There is little scope for the reallocation of public spending across primary, secondary and tertiary services without damaging service delivery. But there is a need to reduce existing regional variations in expenditures and quality of education by reviewing the system of budget transfer norms for allocating education funds to the provinces.

5. **PROVIDING EFFICIENT INFRASTRUCTURE SERVICES**
Dramatic improvements in infrastructure services during the 1990s have contributed to Vietnam's growth, export performance and poverty reduction. Road freight more than doubled during the 1990s, power production tripled, and access to electricity rose from 47 percent to 75 percent of the population. But even so, Vietnam remains seriously underinvested in infrastructure in comparison with other low income countries, and without continued strong investment there remains a risk that bottlenecks could choke off growth. Vietnam is also committed to bringing infrastructure to remote and disadvantaged areas, which will incur high costs while bringing high social gains. If the government is to attain its vision for the infrastructure sector in the coming decade, a four-fold strategy is required.

**Prioritize Investments Carefully.** The government's program for the coming decade
rightly envisages some closing of the "infrastructure gap" between Vietnam and its neighbors. This will involve very large investments across the full range of transport, energy, water, sanitation and telecommunications sectors. In energy alone, for example, the plan requires investments of 4-5 percent of GDP, about twice what its East Asian neighbors spend. Plans for energy and transport combined will require investment of almost 7 percent of GDP, a level equivalent to the entire public investment program in the past decade. Thus, while many investments will have good returns it is vital that care be given to establishing professional systems for careful cost-benefit analysis (in which economic, social and environmental costs are all taken into account), and that less attractive investments be weeded out early.

**Invest in Access for Disadvantaged Areas and Groups.** In addition to being fundamental in promoting national economic growth, infrastructure is a vital ingredient in reducing poverty and promoting balanced growth. Vietnam has an impressive policy for bringing services to all areas of the country, but even so, over the past five years more than half of public expenditures went to the Red River delta and the southeast, while these areas account for one third of the population and less than one fifth of the poor. The choice between investing in "growth poles" and underserved areas is one of the difficult issues being faced by the government, as in other countries.

**Diversify the Pattern of Finance.** The pattern of financing, whereby government resources and ODA financed a large share of infrastructure growth in the 1990s will not suffice in the coming decade. The needs are much too great, and ODA donors are less willing to finance investments when private investment appears available. Two additional sources - private capital and retained earnings - will need to finance more than half of new investments if targets are to be reached. Private investors have demonstrated themselves willing to finance investments in power, telecommunications, public transport, water supply, and even sanitation, but so far virtually no deal has been concluded. Immediate steps can be taken to unlock private investments waiting in the wings.

This could be followed by a clear prioritization of projects for private investment, with competitive bidding becoming the norm. Self-financing by utilities also offers great promise filling financing gaps. This will require rational pricing mechanisms, and more disciplined and transparent financial management. The government should set targets for utilities in power, water, transportation to become commercially creditworthy in the coming few years, together with the key municipalities.

**Improve the Management and Sustainability of Investments.** The government has recognized the considerable scope for efficiency gains from reducing waste and improving performance. In the water sector, decayed distribution networks allow pollutants to seep into the water supply and 30 percent of piped water is lost before it ever reaches customers. Water businesses lose almost 40 percent of their revenues
because customers are not billed for the water they use, or because companies fail to collect. Irrigation systems deliver water unreliable due to poor operation which causes users to incur pumping costs or suffer lower yields. Reforms are needed to increase competition between private and public providers of infrastructure services, and the financial and managerial autonomy of public providers needs to be increased to provide incentives for removing these inefficiencies.

6. IMPROVING ENVIRONMENTAL QUALITY
The rapid pace of change in Vietnam is placing heavy stress on Vietnam's unique natural environment. The coming decade could see a further serious worsening of the environment with irreversible consequences. Alternatively, with carefully designed policies, firmly implemented, economic growth could be used to enable an improvement rather than a destruction of the environment. The government has recently issued a strong National Environmental Protection Strategy, that recognizes the urgency of the problem and sets out programs for action.

In the last five decades, natural forest cover has shrunk from 43 percent to 29 percent of land area, and the country is facing an acute shortage of arable land. Habitat loss has led to a rise in the number of threatened species. Cities are growing at the rate of 4.5 percent per year, more than triple the rural population growth rate, placing huge pressures on municipal infrastructure and services and causing problems such as unmanaged landfills, transport-related air pollution, untreated hospital and hazardous waste, and raw sewage flowing in open channels.

Sedimentation, and point and non-point sources of pollution are threatening the health of rivers. And over-fishing and destruction of coral reefs and mangroves have reduced the fishing yield. Action is required across the range of "green" (loss of forest cover and forest biodiversity), "blue" (degradation of water resources, loss of wetland habitats and inadequate protection of marine and coastal areas), and "brown" (urban and industrial pollution) environmental areas. Four guiding principles are required.

Creating Incentives for Changing Behavior. Community empowerment, enforcement of laws and decrees, access to knowledge, and the provision of information and trade opportunities, act as incentives to induce behavioral changes necessary for environmental protection and sustainable resource use. Without such changes in behavior, the downward spiral in environmental trends in Vietnam cannot be reversed. The Government's Five Million Hectare Reforestation Program is a major management initiative to meet forest product needs in a sustainable manner, protect the environment and increase social and economic benefits.

In the blue sector, the implementation of the new Law on Water Resources will help improve the management of the country's valuable water resources. In other areas, however, controlling unregulated activities and adopting protective legislation have proven difficult, because there is no clear enforcement responsibility for coastal and
marine areas, wetlands and other freshwater bodies. Success in controlling and limiting industrial and urban pollution (the brown agenda) will depend on a credible enforcement and compliance mechanism that not only regulates pollution but also provides incentives to prevent pollution from occurring in the first place.

**Involving Communities and Citizens More Fully.** Experience around the world is clear that it is rarer that governments successfully lead on the front lines of environmental protection, but rather local communities, citizens groups and NGOs. The new government strategy gives greater emphasis to "encouraging public participation", which can build upon some important and successful ongoing pilot activities, and introduce a new and effective way of doing business. In the past, little attention has been paid to local incentives and capacity building for environmental management. The main reasons cited for this are limited environmental awareness, few environmental NGOs, and highly centralized environmental planning and management. These constraints will need to be overcome to ensure greater public participation and involvement.

**Improving Institutional Effectiveness.** The new Environmental Strategy correctly accords much higher priority to institutional development than earlier plans. The Ministry of Science, Technology and Environment (Moste), the National Environment Agency (Nea) and other government agencies with responsibility for environment are working in a weak public administration context that is neither performance-based nor outcome-oriented. Their effectiveness is currently severely limited by small budget allocations, inadequate skills, a lack of mandates at the district level, and perhaps most importantly, a lack of influence with other ministries and agencies in Vietnam.

Existing technical assistance programs have made efforts to build capacity within Moste and Nea, but these will need further support to make them more effective in the future. Capacity will also need to be strengthened at local levels to support more decentralized and local efforts at improving the environment. In addition to capacity-building, it will be necessary to streamline and reorganize environmental and natural resources functions as part of its broader efforts to reform the public sector.

**Diversifying Sources of Financing for Environmental Programs.** Preliminary estimates indicate that to meet the targets of the Environment Strategy, the government will need to spend several-fold more than what it currently spends on the environment. Given the competing needs on the budget, however, it is highly unlikely that the full needs can be met from the budget alone. The first need, therefore, is to prioritize the expenditures. Second, the government should consider a mix of financing instruments to support the implementation of the Strategy, aside from traditional ODA. These would include increased allocation from revenue budgets in sectoral ministries, widening the use of cost recovery measures, environmental user fees and pollution charges, using environmental funds, accessing GEF resources and also tapping into emerging instruments, such as carbon trading. Finally, increased
effectiveness of development aid to the environment - in line with government investment priorities - can be achieved through more effective coordination and partnership.

7. BUILDING MODERN GOVERNANCE

The 10-year strategy recognizes that fundamental to Vietnam's transition will be the development of improved governance structures. Experience from many other countries suggests that delivering the strategic targets will involve an evolution in the role of the state, and actions to build a modern governance structure.

**Strengthening the Public Service.** Vietnam has already started to reform its public administration into a service which can meet the demands of a more modern, market-oriented economy. But progress has been slow, and further actions are needed urgently. The Public Administration Review (Par) completed by the government proposes a number of reforms, beginning with the critical area of civil service reform. It recognizes that substantive and enduring change will require major changes in human resources and in organizational practice and policy. Vietnam not only needs a strong, well-organized public administration system, but also an adequately remunerated service with a personnel policy and grading system capable of effectively implementing these changes. Equally important is that the public service be compact and coherent, with a clear mission, defined goals, and is performance-oriented and accountable. Practices, methods, systems and procedures need to be revised to foster and enhance a new working culture of excellence and of service delivery.

**Creating Transparent and Professional Financial Management Systems.** Substantial progress has been achieved recently with the publication of the state budget in June 1999, publication of Government Financial Statistics (GFS) in the IMF yearbook, improvements in accounting and auditing standards, and improvements in debt management and ODA management. Yet, these are only the first steps towards making the management of public resources transparent and accountable. The budget coverage is only partial and immediate steps could be taken to publish more detailed information on the public accounts. Reorganizing the Vietnamese Accounting Association would present an opportunity to form a professional body consistent with good international practice. Similarly, a Public Sector Accounting Standards Board should be set up to establish and implement public sector accounting standards. A framework needs to be put in place to ensure that public corporations act in a transparent, accountable manner and provide financial information for public scrutiny.

**Developing Legal Systems.** For the last decade, Vietnam has been engaged in building a state ruled by law, as mandated by the 1992 Constitution. Although much has been achieved, officials and development partners agree that in virtually every major sector of the legal system much yet remains to be done. Currently, there is no comprehensive strategy for developing Vietnam's legal system, and legal development
has tended to proceed in an ad hoc fashion. While this piecemeal approach has been the way legal development has taken place in most countries, most other countries had the luxury of developing their systems over centuries. Vietnam, in contrast, is keen to integrate quickly into the regional and world economy and to become a modern, industrialized nation by the year 2010. This will require a well-functioning legal system to underpin this transition. A comprehensive legal development strategy needs to be designed so that Vietnam can put in place a complete, coherent and well-functioning legal system in a relatively short time.

Creating a Participative and Responsive Government. Government strategy documents give high priority to improving peoples' participation, access to information, and awareness of legal rights and obligations. Recent research indicates that poor people in Vietnam are hungry for a two-way flow of information: information from government to them about the nature and timing of policies and programs that affect their lives, and from them to government with a view to influencing some of these policies and programs. Access to such information channels is often felt to be limited to a few "well-connected" participants. More widespread access would lead to a more equitable and inclusive pattern of development.

The government is taking measures to address these shortcomings by implementing the Grass-roots Democracy Decree, which offers a crucial and encouraging legal framework for increasing community participation at the local level. The new Law on Science and Technology is also an important step forward in providing a clearer legal framework for the operation of research-oriented associations and NGOs. A supportive legal framework also needs to be provided for associations and NGOs not involved in charity or research, and which are therefore not covered by the existing legal framework. A comprehensive and clear Law on Associations which would offer a supportive environment, balanced with appropriate state oversight functions and accountability mechanisms, is needed.

To ensure that women have an equal voice, Vietnam needs to take a gender-sensitive approach to participation and encourage and support more equal participation in public life by women. This is not only right from an equity point of view but, as recent research indicates, will also promote faster development and cleaner business and government (less corruption). This can be achieved through means that ensure equal access to education (especially secondary and higher), equal access to information (including legal literacy), and facilitating greater participation of women in political and other leadership positions, especially at provincial and lower levels.

Fighting Corruption. Fighting corruption is an important priority. Vietnam's leaders need to set an excellent example and must continue to show their determination to fight corruption at all levels. While there are individual steps which can help with this, such as minimizing red-tape and reforming procurement, it is important that the reasons behind corrupt behavior are understood and measures taken to address these
at the same time. There is much international experience that can assist Vietnam in this task.

8. SUPPORT FROM THE INTERNATIONAL COMMUNITY  Vietnam is embarking upon a 10-year period that will shape its development for decades to come. If it is successful in reaching the goals it has set itself it will, by the end of the decade, be well on its way to building the base for a modernizing economy. In order to reach its goals, it is choosing to turn to the global economy as a market for its products, and a source of capital, technology and ideas. It is important that the international community support it in its efforts.

International trade and investment will be the most important contribution that the international community can bring. As Vietnam opens its own markets and follows market friendly domestic policies, it can expect its own exports to grow - from the current level of $14 billion towards the goal of $50 billion by 2010. The international community can support this process by reducing their own trade distortion, especially non-tariff barriers and domestic subsidies.

Foreign investment, likewise, will play a crucial role in introducing technology, management skills and market know-how to Vietnam. Whether the government's hope of inflows of $2 billion per year (5.2 percent of projected GDP) during the next decade is reached will depend on progress in creating a clear and efficient regulatory environment. For its part the international business community needs to demonstrate strong corporate citizenship and positive "externalities" in the form of skills upgrading and technology transfer.

ODA needs to play a strong continuing role in the years ahead. During the 1990s, ODA inflows rose from near zero to around $1.3 billion per year. While relatively modest by the standards of other low income countries, these inflows (totaling some $6 billion for the 1990s as a whole), have played a very constructive financial and technical role across a broad range of activities, while supporting Vietnam's gradual policy and institutional renewal.

International NGOs - which in aggregate have invested around $80 million annually in grant funds for poverty programs - have also played a highly valuable role, introducing lessons and methods from international experience, especially in poverty reduction programs. Over the past two years the international community has recognized that with the large numbers of donors, programs and projects in Vietnam it was necessary to move towards a new way of doing business if funds were to have maximum impact on poverty reduction and economic development. This recognition has been part of increased understanding globally as to what makes development cooperation effective. Strands to this thinking are:

- The importance of a strategic vision: too often development interventions have been undertaken with inadequate understanding of the broader policy and
institutional context. It is essential that ODA supports policy and institutional reform and never substitutes for it;

- Minimizing gaps, avoiding duplication, and lowering transactions costs: too often ODA has been less effective than it could have been due to fragmentation and uncoordinated programs. Working as genuine partners can substantially improve overall cost-effectiveness, but requires changed behavior from us all, and;

- The need to focus on outcomes rather than inputs: traditional measures of ODA success have too often been in the form of disbursements, timelines or completions rather than impacts on the quality of life. Investment in improved monitoring and evaluation systems, with a focus on on-the-ground impact, is needed to help change mindsets and improve effectiveness.

In an effort to address these issues, the government, donors and NGOs in Vietnam have sought to establish partnerships in key areas and sectors to facilitate discussion, design and implementation of programs. A companion volume to this report ("Partnerships for Development") is a compilation of brief notes prepared by some of these groups. In the spirit of the new approach, these notes seek to link the programs supported by the international community to Vietnam's goals and strategy for the coming decade.

**Part I: Pillars of Development**

Part I provides a commentary on the emerging draft Ten Year Socio-Economic Development Strategy for 2001-2010. This document lays out the vision and the strategic directions for Vietnam during the first decade of this new millennium. It is currently in draft form and is undergoing an extensive process of consultation within the government (at national and local levels) and the society at large.

Part I comments on the comprehensive development agenda laid out for the next decade. It starts with a framework for rapid growth and poverty reduction and then examines the strategies required for:

(i) Enterprise development;
(ii) Rural development;
(iii) Human and social development;
(iv) Infrastructure development;
(v) Environmental quality, and;
(vi) Good governance.

Since the government is formulating a long-term development agenda, it will need to take a comprehensive approach to development and tackle all these "pillars" of development. Without progress on all fronts, Vietnam will not be able to achieve the economic and social transformation that it desires. A balanced attack across all fronts
does not, however, imply that everything needs to be done at once. What is needed to prioritize actions is an identification of the bottlenecks - the hard-to-solve problems that are impediments to success - and to begin by attacking these first.

What is also needed is that the energies of all of Vietnam's development partners are harnessed so that they are all working together in partnership to make all of Vietnam's resources - including aid resources - more effective.

For the full text of this section please refer to the Asian Development Bank's Home Page: adb.org.

**Part II: Partnerships for Development**

This section addresses the theme of stronger partnerships to help the government of Vietnam to attain its vision and implement its strategy. It brings together a series of thematic notes on Vietnam's development strategy, prepared by the development partnership groups in Vietnam.

These notes seek to describe and distill Vietnam's goals and the steps needed to get there. They also describe how the donor community can help Vietnam in attaining its vision. The work of the development partnerships, and the production of these notes, are indicative of an important new direction in international development cooperation, both in Vietnam and in many other countries.

Around the world, there is a recognition that the old ways of working have not produced the results that had been expected. The current time in Vietnam offers international partners the opportunity to actively listen to the government's articulation of its long-term development goals and to work together to identify and address the constraints and roadblocks that would prevent the goals being reached.