

PUBLIC INVESTMENT EFFICIENCY in Vietnam

**(Research Paper with Answers to
Diagnostic Questions)**

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PART 1- PUBLIC INVESTMENT: GRADUALLY RENOVATED, YET INEFFICIENT

1- Innovation and Development

- Vietnam is undergoing a transition and global economic integration
- In the context of renovation and integration, the economy has been growing rapidly, with the improved domestic saving currently exceeding more 30% of GDP

Chart 1

Improving living standards

Vietnam's poverty rate has fallen dramatically because of strong growth.



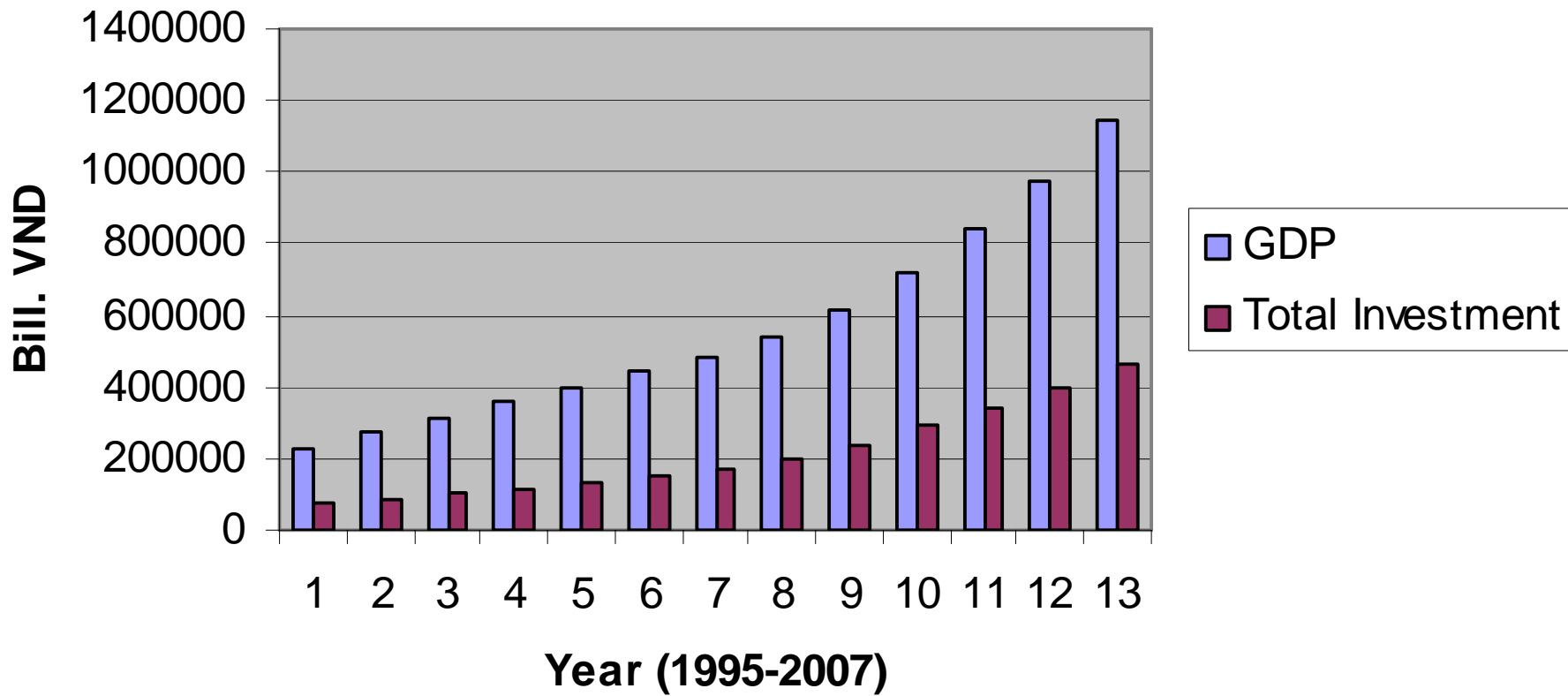
Sources: Vietnam, General Statistics Office; CEIC Data Company.

PART 1- PUBLIC INVESTMENT: GRADUALLY RENOVATED, YET INEFFICIENT

2- Rapidly Expanded Investment Size

- The scale of investment in the recent years has increasingly expanded to reach 40% of GDP
- The government managed to spend about 30% of budget expenditure on development investment

MACRO ECONOMY



PART 1- PUBLIC INVESTMENT: GRADUALLY RENOVATED, YET INEFFICIENT

3- Improved Investment Structure

The capital structure has improved as compared to the “demand stimulation” period of 1999-2001 with increased private capital (from both domestic and foreign sources), while the share of public finance has reduced to 39.9% of the total in 2007, yet the investment scale accounted for 45.6% of GDP, a very high level among Southeast Asian countries

	Capital Formation to GDP (%)	Investment/GDP (%)	GDP Growth (%/year)
1995	27.14	31.7	9.54
2000	29.61	34.2	6.79
2005	35.58	40.9	8.44
2006	36.81	41.5	8.17
2007	41.65	45.6	8.48

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4- Renovation and Improvement of Regulations on Public Investment

The rapid growth of SOEs' investment scale and investment credits is worth a thorough analysis.

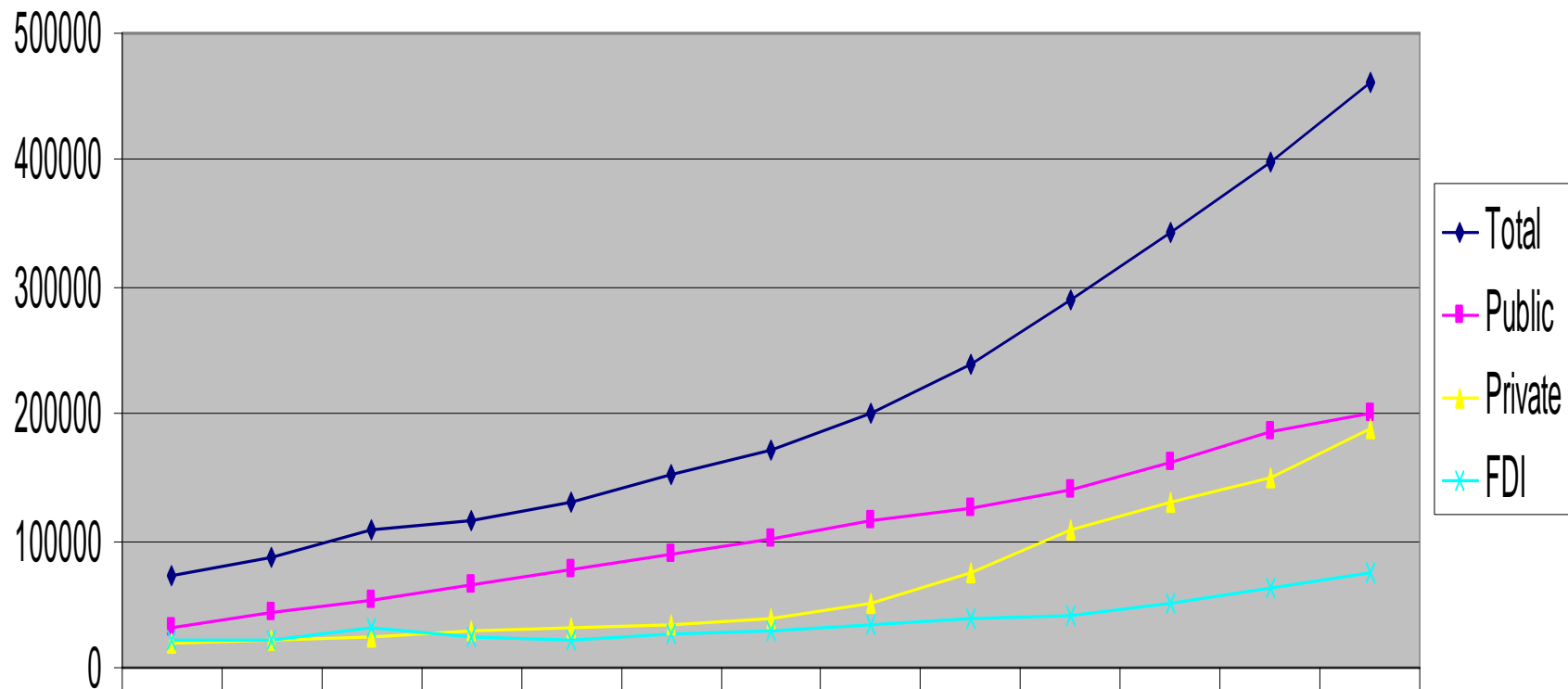
A legal document to govern the equitization of SOEs is not yet in place, hence the slow progress.

In the meantime, the business groups and general corporations are not subject to prudent management, and many of their investments have deviated from their conventional business.

PART 1- PUBLIC INVESTMENT: GRADUALLY RENOVATED, YET INEFFICIENT

5- Weak Management of Public Investment

- *Loose and overlapping regulations on investment.*
- *Weak master planning and poor project selection.*
- *Poor project preparation.*
- *Poor Investment Management*
- *Asynchronous Investment*
- *Low economic efficiency including use of fixed assets*



	1	2	3	4	5	6	7	8	9	10	11	12	13
◆ Total	72447	87394	108370	117134	131171	151183	170496	200145	239246	290927	343135	398900	461900
■ Public	30447	42894	53570	65034	76958	89417	101973	114738	126558	139831	161635	185100	200000
▲ Private	20000	21800	24500	27800	31542	34594	38512	50612	74388	109754	130398	150500	187800
✕ FDI	22000	22700	30300	24300	22671	27172	30011	34795	38300	41342	51102	63300	74100

PART 1- PUBLIC INVESTMENT: GRADUALLY RENOVATED, YET INEFFICIENT

6- Inefficient Public Investment

The government has adopted a number of policies and regulations aiming at improving the investment and public investment environment.

These adjustments are not synchronous from legal regulations, master plan documents, plan assignment to directing, monitoring implementation and use of investment funds, which lack of linkage with the market economy.

ICOR in Vietnam (2002-2006)

	2002	2003	2004	2005	2006
1- Vietnam					
a- GDP	313247	336242	362435	393031	425135
b - Delta GDP	20712	22995	26193	30596	32104
c- Gross Investment	147993	166814	189319	213931	239813
d- ICOR	7.15	7.25	7.23	6.99	7.47
2- Public Sector					
a- GDP	128343	138160	148865	159836	170001
b - Delta GDP	8519	9817	10705	10971	10165
c- Gross Investment	86677	95471	105082	115196	125413
d- ICOR	10.17	9.73	9.82	10.50	12.34
3- Private Sector					
a- GDP	150898	160498	171659	185744	201044
b - Delta GDP	9920	9600	11161	14085	15300
c- Gross Investment	35134	42844	53535	62842	72120
d- ICOR	3.54	4.46	4.80	4.46	4.71

PART 1- PUBLIC INVESTMENT: GRADUALLY RENOVATED, YET INEFFICIENT

7- Negative Developments since 2007

Since 2007, investment performance has seen negative developments in various dimensions.

Mistakes are mainly that projects are stretched and overlapping, investment incomplete and delayed, and too many small and fragmented projects.

Composition of Public Capital (1995-2007) - %

	State budget finance	Investment Loan	SOEs' capital and others
1995	44.4	19.9	35.5
2000	43.6	31.1	25.3
2005	54.4	22.3	23.3
2006	54.1	20.0	25.9
2007	50.9	19.6	29.5

PART 1- PUBLIC INVESTMENT: GRADUALLY RENOVATED, YET INEFFICIENT

8- Complex public capital structure with regard to national targeted programs and Gov. bonds

Almost all NTPs are approved by the Prime Minister, with identified total capital but without details to project level, and approved in separate decisions by the Prime Minister.

Government bonds are revenues spent via the state budget (i.e. outside budget balance. This makes the real state budget expenditures higher than the balanced figure). In 2007 Government bonds performed poorly. In the first nine months of 2007 only 26.8% of the adjusted plan was released

PART 1- PUBLIC INVESTMENT: GRADUALLY RENOVATED, YET INEFFICIENT

9- Funding by state credit

Of the public capital, the investment credit fund is accounting for 7.9%, a 12.5% increase compared with that of 2007. The state investment credits are focused on projects of difficult sectors and areas in line with the investment incentive and encouragement policy.

PART 1- PUBLIC INVESTMENT: GRADUALLY RENOVATED, YET INEFFICIENT

10 – SOE capital

In addition to capital directly funded by the state budget and state credits, about 30% of public capital comes from SOEs (with budget origin), which is a large amount, yet not being managed uniformly and effectively.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 1 – Orientation of Investment

(Is there well-publicized strategic guidance for public investment decisions at central/ministerial/provincial levels?)

Directions of investment in general and public investment in particular are clearly stated in regional and sectoral socio-economic development strategies and master plans, medium-term and annual plans, and public investment programs.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 2 – Project Screening

Is there an established process for screening of project proposals for basic consistency with government policy and strategic guidance? Is this process effective? What proportion of projects so screened are rejected?

Domestic investment projects are classified into 4 groups namely:

- - Specially important projects (national importance),
- - Group A projects,
- - Group B projects,
- - Group C projects.

Only few remain to be approved by the Prime Minister. The level of decentralization varies depending on the scale and nature of projects.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 3 – On-budget project selection

Is final project selection undertaken as part of the budget process or prior to the budget process? Does the government maintain an inventory of appraised projects for budgetary consideration?

The relatively loose coordination between MPI and MOF leads to the fact that MOF's involvement in MPI's planning work is limited, but when it comes to resource allocation, the major role is played by MOF.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 4 – Project Selection by Cost-Benefit Methods

Is there a formal appraisal process for more detailed evaluation of public investment project proposals for costs and benefits? If yes, is appraisal mandatory for all projects or for projects above a certain monetary value? Is project appraisal undertaken only for specific sectors and if so which sectors? What proportion of public investment projects are formally appraised for costs and benefits?

Large (group A) projects typically approved by ministries and local governments all include NPV calculations at various levels, Smaller projects (group B or C) are usually devolved to lower levels, but cost effectiveness analysis (both economic and social) is still undertaken, including NPV calculation.

However, NPV assessments usually have low quality.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 5 - ODA and Public Investment Projects

What proportion of the public investment program is donor financed? Are donor financed projects subject to the same or different rules for appraisal and inclusion in the budget as government financed projects? If different, describe the difference. Does the government review project appraisals undertaken by donors?

Public investment projects in Budget account for up to 30% of the total budget expenditure and approximately half of total investments. In the meantime, ODA-funded projects (both loans and grants) account for nearly 15-20% of the total public investments, i.e. 7-10% of total investment.

Recently, in line with strengthening “ownership” and “partnership”, the Vietnamese party has paid more considerations to efficiency by combining various resources, by PPP.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 6 – Quality of Appraisals

Are appraisals screened by an external agency or department for quality and objectivity of appraisal?

Appraisal is led by functional departments with inter-agency participation to ensure comprehensive and systematic considerations.

For large-scale projects, the Government set up an inter-agency appraisal panel to take a rigorous assessment, with participation of associations and academia to ensure the rationale of recommendations.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 7- Capacity and Quality of appraising agency

Are project appraisals formally undertaken by the sponsoring department or by an external agency? What is the quality of such appraisals?

Appraisal is a multi-agency job, but usually led by the planning sector. The Investment Appraisal and Supervision of MPI has limited power. In fact, it only undertakes organization of appraisal, while the appraisal itself is left to individual functional bodies.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 8 – “Climbing the fence” projects

Is there an effective process to control the gates to the budgeted public investment program, i.e. the collection of projects that are formally approved for budget allocation and implementation? Are the number of oversight agencies limited, and their key roles clearly specified? Do delegation levels exist that make clear the level of materiality for bringing projects to the center? Is there an established but limited process for including projects for emergency or politically imperative reasons? What proportion of projects enter the PIP by “climbing the fence” i.e. by avoiding the gate-keeping process? What proportion of projects that “climb the fence” is donor financed?

Projects in general are subject to multiple screening and finally get to MPI and MOF. Sectors and local government have taken over the major role. Facing high inflation, the Government introduced measures of investment adjustment.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 9 – Share of new projects

What is the typical proportion of the value of new project starts relative to the ongoing public investment program? (use three year moving average).

The regulations in recent years are very clear: small projects should be completed within 2 years, medium-size – 4 years.

The proportion of new project starts to ongoing ones is around 20%, but many projects are not well-prepared, facing with lots of difficulties when it comes to implementation

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 10 – Rate of project completion

What is the completion rate of the public investment program (annual average over the past 5 years), defined as the annual public investment budget divided by the estimated cost to complete the current public investment program?

Projects often last longer than planned due to stretched investments. PIP are usually over-performed.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 11- Implementation of Procurement Plan

Do ministries undertake procurement plans in line with good practice and do they implement procurement plans effectively?

The promulgation of the Law on Procurement in 2005 and Decree guiding implementation of laws on procurement and construction have standardized this important area

To speed up implementation, some times the government tends to use “direct contracting” or limited bidding in major projects.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 12 – Review of PIP

Has the government undertaken a rationalization of its public investment program in the recent past? Did the rationalization improve the prioritization of the public investment program? Did it result in the cancellation or closure of ongoing projects? If yes, what is the percent of the PIP that was cancelled or closed? Indicate if projects were merely “deferred” rather than cancelled.

The first PIP was an experiment with support of international experts.

The second PIP was led by MPI in coordination with other ministries and provinces, better capturing progress in policies and mechanisms and staff capacity.

The third PIP was developed with TA offered by ADB, linked with economic reform process.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 13 – Monitoring Report

Are project implementing agencies required to prepare periodic progress reports on projects? Does this include an update on the cost benefit analysis? Are the sponsoring departments accountable for changes recorded in either costs or benefits and for the delivery of net benefits? What mechanisms exist to ensure that this occurs? Is this record of investment management used in subsequent budget discussions with the MOF or Ministry of Planning?

To improve efficiency, the government has strengthened investment monitoring, including monthly briefings at MPI (by region), briefings every six months with the Prime Minister and monthly with ministries and provinces

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 14 – Rate of Project Performance

For a representative subset of the public investment program (including Bank-supported projects), what is the average percentage cost over-run (in inflation-adjusted terms) on major projects in key sectors?

The implemented projects are classified into Group A, B, C and extremely important.

If completed projects account for 20% of the active portfolio, it also means that the average duration of projects would be 5 years or longer.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 15 – Competitive Bidding

Are projects commissioned to private contractors and if so are contracts awarded on the basis of competitive bidding? Are international firms permitted to bid on contracts? If other methods are used, describe the methods. Is there any evidence from CPARs or other reviews of procurement contributing to cost escalation or fraud?

For public investment projects funded by the state budget, procurement regulations are uniform to all types of firms and contractors.

MPI launched a procurement website at www.dauthau.mpi.gov.vn (*dauthau* is the Vietnamese word for Procurement) with increasingly improved contents.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 16 – Quality of PIP Preparation

For a representative subset of the public investment program, what is the delay in project completion relative to initial estimated time on major projects in key sectors?

PIPs are practical, though with a bit poor contents. PIP 1996-2000 was a pilot one. PIP 2001-2005 was prepared by Vietnamese agencies, constrained by the mechanisms that had not changed after promulgation of the new Budget Law. PIP 2006-2010 is quite different, emphasizing important directions and transparent decentralization mechanism and more sufficient contents.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 17 – Valuation of NPV

Is the actual NPV of completed projects measured, and is a project end evaluation undertaken to review the nature of differences relative to the estimated NPV at appraisal? What alternative methods, if any, does it use to undertake ex post evaluation of completed projects?

NPV technique is being used in comparison and selection of projects to assess project efficiency. Even the sensitivity of efficiency relative to changes of certain parameters is assessed, especially when foreign investors are involved.

PART 2 – DIAGNOSIS OF PUBLIC INVESTMENT QUALITY

Question 18 – Asset Register.

Does the government maintain an asset register or inventory of public sector property, equipment, vehicles, etc.? Is legal title to assets maintained? Are assets valued according to sound accounting principles, such that the accounting definition of an asset is met, depreciation is deducted from the asset value and where feasible, asset values are updated to reflect changed prices etc...

Budget regulation states that vehicles, equipment, buildings and workshops are all state assets, which are subject to register and monitoring.

The energy and transport sectors are holding the major part of the state's assets

PART 3 – CONCLUSIONS AND RECOMMENDATIONS

Conclusions

- a- *Reform and integration process* has been positively influencing the size, structure and efficiency of the economy as well as investment efficiency
- b- *The efficiency is low right from the beginning and during the whole implementation process.*
- c- *Weak coordination among agencies.* Weak coordination is also seen between Vietnamese agencies and donors, especially in the context of incomplete legal framework.
- d- *Lack of highly qualified staff.* The weaknesses of the management and oversight system is partly attributed to the lack of a qualified, well-trained and competent staff.
- e- *Lack of specific regulations.* It is necessary to develop specific mechanisms and concrete, quantifiable standards to control and monitor the investment process.

PART 3 – CONCLUSIONS AND RECOMMENDATIONS

Recommendations

- a- Reform and participation of civil society.
- b- Enhance coordination between the Government and the National Assembly.
- c- Improve quality of decision making, including in SOEs projects, credit and targeted programs .
- d- Open and transparent monitoring and control.
- e- Enhance coordination with the international community.

Thank you
for your attention

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