

***THE ROLE OF DONORS  
IN VIETNAMESE DEVELOPMENT PLANNING***

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## **The role of donors in Vietnamese development planning**

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### **Abstract**

Although it remains a one-party state, Vietnam has become one of the most popular host countries for multilateral and bilateral aid donors during the past decade. Vietnam's popularity is largely explained by the fact that it is perceived as a good aid recipient, and it has often been identified as a "best practice" example of how a government can manage external aid and own its development agenda. The purpose of this paper is to discuss the roots of Vietnam's strong ownership and to examine how the relations between the state and the donor community have influenced Vietnamese development planning. The first part of the paper highlights the uneven relation with the Soviet Union during the 1970s and 1980s as an explanation for the present ambitions to avoid dependence on foreign partners. The second part outlines the institutional setup for development planning that was created to match the existing institutions for central planning during the 1990s. The third part discusses the ongoing changes in the role of the state and in the institutional setup for development planning. The process of change is illustrated using the Comprehensive Poverty Reduction and Growth Strategy as an example. The paper concludes that donors have contributed both directly and indirectly to the changes in the Vietnamese model of economic planning, and that the donor community has to some extent taken on the roles played by civil society and a political opposition in parliamentary democracies.

Key Words: Vietnam, development planning, ODA

JEL Codes: P21, O21, O19

## 1. Introduction and context

Vietnam has become one of the most popular host countries for multilateral and bilateral aid donors during the past decade – for instance, it is the World Bank’s second largest aid recipient today. This is remarkable considering that Vietnam is still a communist one-party state and that most donors have a relatively short history of development cooperation in the country. Aside from its good performance in poverty reduction and economic growth, Vietnam is popular because it is perceived as a “good” aid recipient: in fact, Vietnam is often identified as the “best practice” example when it comes to aid management and government ownership of the development agenda (Conway 2004; GRIPS 2002; UNDP 1996).

Vietnam’s good reputation is often explained with the government’s decision to introduce an economic reform program in 1986, long before the international donor community had launched any official aid programs to support the country’s transition to a market economy. As a result, the government was able to maintain the lead in its relations with the many foreign development partners that entered the country some years later. It was also to maintain a centralized system of development planning.<sup>1</sup> The outcome in terms of development and poverty reduction has been highly successful. Vietnam emerged as an interesting market and investment location already a few years after the introduction of Doi Moi, despite the continuing dominance of the state sector. Economic development accelerated, reaching a peak in the mid-1990s when the annual GDP growth rate exceeded 9 percent. The share of the population living in poverty fell from 70 percent in 1987 to 29 percent in 2002. The donor community has played an important role in this process, with annual aid flows increasing from a few hundred million in 1990 to over 1.5 billion since the late 1990s.

Today, the Vietnamese state desires faster international integration. Further comprehensive reforms are needed to fulfill this objective, and the donor community has pledged to commit substantial resource to facilitate the country’s development and internationalization. However, the state still wants to play a dominant role in this process. One central question is how the relation between the state and the donor community has influenced Vietnamese development and development planning. The purpose of this paper is to examine if and how the role of the state in development planning and aid management has changed due to external influences from foreign aid and interactions with donors. We therefore explore the institutional factors that determine how the state organizes development planning and integrates donors in the process of development and change. Historical experiences and the government’s internal politics constitute the core of our analysis in explaining both the present institutional setting for development planning as well as the causes for change. Some scenarios for the future are also discussed.

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<sup>1</sup> The term “foreign development partners” refers here to multilateral donors, bilateral donors, and international non-governmental organizations.

## **2. From Soviet aid to development cooperation**

### ***Dependence on Soviet aid***

The development process in Vietnam before Doi Moi was influenced by both internal and external factors. The experiences from this period were fundamental determinants of the government's cautious attitudes towards foreigners in the years immediately after the introduction of Doi Moi. The priority in the relations with foreign actors was to defend the autonomy of the nation.

After reunification in 1975, Vietnam faced severe economic challenges. Attempting to introduce a socialist regime throughout the country, especially focusing on the South, the government introduced public collectivization of labor and other factors of production. Anti-capitalist campaigns ordered by the government in March 1978 led to a clampdown on "bourgeois trade" to drive out the private business sector that remained in the southern parts of the country (Asia 1979 Yearbook). However, the command economy was largely made up of an inefficient agricultural sector, with only a very industrial production: at the time, this led foreign experts to refer to the country as a "vegetable civilization" (quoted in Bui 1974, p.7). The economy relied heavily on economic aid from China (roughly USD 300 million per year) and a small number of Western countries. However, these aid flows were interrupted when the government's decision to send troops to Cambodia at the end of 1978 led to economic and diplomatic sanctions by both Western and Asian countries – these sanctions came to remain in place for the following decade (the US sanctions were not lifted until 1995).

As a result of the sanctions, Vietnam was forced to move closer to the Soviet Union and the Eastern European communist bloc for trade and economic aid. Throughout the 1980s, the economy was heavily dependent on Soviet aid, which made up about 10 percent of GDP and covered more than 40 percent of the government budget and 75 percent of total public investment at its peak in the mid-1980s. At the same time, the share of trade with the Soviet Union reached about 70 percent of Vietnam's total foreign trade. The only official aid that Vietnam received from others than the Soviet bloc during the 1980s came from a few remaining donors such as Sweden, Finland and the United Nations, amounting to about USD 100 million yearly. With total annual aid inflows estimated at about USD 1 billion, Soviet aid clearly overshadowed the aid from the West. McCarty (2000) shows that Soviet grant aid and soft loans supplied 90 percent of Vietnam's petroleum, iron and steel, machinery, fertilizer and cotton imports. It financed hundreds of state enterprises and accounted for 95 percent of coal production, 51 percent of cement output, and 35 percent of electricity generation. Table 1 shows how the dependence on the Soviet Union increased consistently during the 1976-1986 period (in tandem with the growing inefficiency of the domestic command economy) at the same time as the deficit in the trade with the Soviet Union increased sharply over the same period. One result was a very high level of external debt. On the domestic arena, the reliance on Soviet aid resulted in pessimistic views regarding Vietnam's own economic potential. Whenever things started go wrong, a common reaction was "Don't worry! The Soviet brother will take care of it". Like other areas, development planning also depended on Soviet aid.

Externally, the reliance on the Soviet Union forced Vietnam to implement modest and dependent politics – on conditions outlined by the Soviet Union – in return for economic and military support.

**Table 1: Soviet aid and Vietnam’s trade with the Soviet Union 1976 – 1986**

Year	Soviet Economic Assistance	Soviet Military Assistance	Total Assistance	Total trade	Trade balance	Trade with the Soviet Union / total trade
1976	n.a.	n.a.	n.a.	393	-224	38%
1977	n.a.	n.a.	n.a.	548	-196	41%
1978	700-1000	600-800	1300-1800	669	-224	36%
1979	800-1100	900-1400	1700-2500	905	-455	45%
1980	2900-3200	800-900	3700-4100	943	-458	48%
1981	900	900-1000	1800-1900	1239	-774	60%
1982	1200	1000	2200	1392	-823	67%
1983	1300	1200	2500	1529	-899	69%
1984	1400	1300	2700	1546	-914	65%
1985	1600	1700	3300	1750	-1072	65%
1986	1800	1500	3300	2297	-1459	71%

Sources: Based on information from Pike (1987), p.139 and IMF (1987), pp.412-13.

### ***From economic dependence to autonomy***

When Soviet aid diminished and eventually ended after the mid-1980s, it forced the Vietnamese leadership to revise its policies and adopt an economic reform program. At the same time, the perception of the economy changed: economics became an area with important connections to national security, which required a strong state that could control economic development and external relations.

Judging from our interviews with various groups within and outside the party and government, it seems clear that the contemporaneous reactions to Doi Moi varied between different groups in the leadership. For some groups, the reduction of Soviet aid provided a welcome reason for the leadership to rethink domestic politics and to take the initiative for reform. “Renewal or Death” was an argument heard in connection with the VI Party Congress in 1986, indicating the urgent need for radical change (Duong 1991, p.26). The choice was “Renewal”, including decollectivization of farming, reductions in subsidies, price liberalization, and marketization. The Doi Moi program was meant to move the economy from central planning to a “socialist market economy”. However, although concepts like markets, capitalism, and economic liberalization began to gain acceptance in the leadership’s ideological thinking, the reforms stopped short of political liberalization: the fundamental political control of the party and the role of the state was not subject to change. For some other groups in the party leadership, Doi Moi meant above all an effort to combat political and economic dependence on foreign powers. The view was that no amount of aid could substitute for national independence, and that “...the history of economic dependence should not be repeated .... Development must be gained and sustained by internal strength”, as noted by the interviewed government officials.

Given the lessons from the relationship with the Soviet Union, the party developed the view that the state should manage its internal and external relations in a way that could clearly separate between domestic politics and areas where external involvement could be allowed. Domestic economic policy came to be dominated by a concern for national security, under which all other policies were subsumed, in particular foreign policy. This caution with respect to external partners was retained for a long time after the introduction of Doi Moi, and was manifested e.g. as a fear that foreign assistance could be used as a tool of external influence in Vietnam's domestic affairs.

For some time after the beginning of the reform program, economic integration and engagement with the West were still officially viewed as "social evils" (quoted in Sidel 1998, p.80) and therefore had to be fully controlled by the state. The attitude to foreign donors was skeptical, in particular regarding discussions about democracy and human rights, on the one hand, and promotion of the private sector and civil society, on the other hand. The development of these domestic issues was not considered to be in the interest of the state, but they were quite often included among the donors' main objectives. The rule that guided the government's relationship with external actors was, therefore, an aim for "self-determined integration, bringing into play the nation's internal forces and taking most advantage of integration in order to strengthen effectiveness of international cooperation, ensuring independence and ownership as well as national interests..." (See Central Party Committee's Resolution 2001, p.3).

### ***External relations and foreign aid since the early 1990s***

Although the past history of war and economic dependence on foreign countries initially colored the party's and government's policies towards external actors, these policies were gradually revised as a result of the changing international environment. Economic and political dependence was still to be avoided, but excessive caution and skepticism regarding the outside world was not consistent with international integration. Hence, the policies were adjusted to balance the economic and political incentives for integration with the need for political independence: both objectives were to taken into account in the development of relationships with external actors, e.g. aid donors and regional and multilateral organizations.

After the introduction of Doi Moi and the improvement in foreign relations following the retreat from Cambodia, Vietnam aimed to increase its integration with the world economy. Cooperation with the West was emerging as a necessity for improving economic performance. A new diplomatic policy was adopted, with encouraging results. The US embargo was lifted and the diplomatic relations with the US were normalized in 1994, with a further deepening of the relations in 2000, when a Bilateral Trade Agreement was signed. Trade with the US has expanded rapidly as a result of these measures. Vietnam was admitted to ASEAN and APEC in 1995. That year, Vietnam also applied for membership in the WTO.

In the field of development assistance, several of the major international donors resumed their official cooperation with Vietnam in 1993. Vietnam's role as an aid recipient was initially colored by the concerns and worries inherited from the pre-Doi Moi period, but

the relations with the donor community have changed substantially since that time. Moreover, the relations with the donor community have contributed to important changes in Vietnamese society, not least regarding the role of the state. The Vietnamese leadership saw the reappearance of aid from major multilateral and bilateral donors in 1993 as a token of political recognition from the West for the reform initiatives and the open-door policy launched in 1986. Over the years, the party and its government have learned to engage in a dialogue with donors regarding the implementation of development policies, although the emphasis on autonomy and national control remains at the policy level. This change has been expressed by some government officials as follows: "...just the fact that we have worked with donors and the management of foreign aid has opened our views, judgments and sharpened our knowledge. We have learned to be open and it enables us to trust... The question is how to take the best advantage of foreign assistance without making Vietnam dependent on it".

Most of the donors represented in Vietnam today entered after the reforms initiated by the Vietnamese leadership had led to a strong upturn in the economy. This is important for Vietnam's relations to donors. It implies that foreign aid was not the initial driver of the economic boom. It is also important that the domestically driven reforms resulted in rapid economic growth that enabled Vietnam to avoid taking on substantial amounts of foreign debt. These factors have strengthened Vietnam's bargaining position and differentiate the country from many other aid recipients and their relations to donors: the Vietnamese government has a higher degree of control over its own national reforms and development planning. In many cases, it has meant that the government has rejected development projects where a donor's policies and aid disbursements were tied to strong political or economic conditions.

This notwithstanding, the government has come to realize that foreign aid has played an important role that could not have been substituted by other kinds of external relations (MPI 2004; GoV 1999; GoV 2004). In the new era of development cooperation with many different donors, the government has learned to maximize the support to various development programs in Vietnam while maintaining reform autonomy and the initiative in policy making. Long term cooperation with bilateral donors like Sweden and multilateral donor like UNDP has shown that a relationship of mutual trust can yield very good results. During the period 1986-1992, aid from these and a small number of other donors accounted for only about 1 percent of GDP (MPI 2004). Nevertheless, their choice to stay and support Vietnam at a time when all other donors left or imposed sanctions gave them a special status as long-term partners and trusted friends. Today, these donors no longer play any dominant role, since other international financial institutions and bilateral donors have entered with larger financial resources. However, the government still relies on these long-term partners to open doors for development cooperation in politically sensitive areas, such as anti-corruption programs, parliamentary democracy, and public administration reforms. Hence, aid has not only been used for large-scale infrastructure development, but also for policy and institutional reforms at both the central and provincial levels, often with the foreign partner chosen explicitly on the basis of its competence and capacity. The emergence of these kinds of "sensitive" development projects clearly indicates a change in the attitudes towards foreign aid and the relations with foreign donors. It is recognized that the roles and interests of each

individual donor differ, as does their potential contribution to Vietnamese development. Therefore, “adaptive” rather than “cautious” is a more appropriate characterization of the government’s new policy in its donor relations.

The more adaptive and dynamic relations with a wide variety of foreign development partners make it possible to be flexible regarding the national security concerns. This has allowed the donors to broaden their support from infrastructure to policy reform and it has also allowed Vietnam to speed up its integration with the world economy. Preserving national interests and independence remain important objectives, but they do not seem to make up serious obstacles to constructive development cooperation anymore.

The following two parts discuss the interaction between the government and the donor community and the institutional setting for foreign aid during the past two decades. The focus is on the process of change, and in particular how the institutional setting for ODA has developed through the interactions between the Vietnamese government and the donor community.

### **3. Centrally planned development policy**

As an inheritance from the pre-Doi Moi period, the government had a strong ambition to control its domestic politics and it was cautious towards the new external partners that began to arrive to Vietnam after the late 1980s. Central planning was the fundamental institutional tool of the government to manage and regulate socio-economic development. The system of central planning resulted in an institutional set-up in which the Ministry of Planning and Investment (MPI) stood – and continues to stand – at the centre of the country’s overall development planning. In this central role, MPI drafted and formulated the overall national development strategies and short-term plans, and it held the main responsibility for the management of public investment and resource allocation.<sup>2</sup> Because of this central coordination role, MPI was seen as the government’s “conductor of the whole development concert”, in which the musical players in the orchestra were inputs from different ministries. MPI’s officials considered its main task to be “Can bang cac muc tieu chinh phu va hai hoa cac loi ich”: to pursue the government’s development priorities and to balance stakeholder interests between sectoral and regional concerns, as well as between national and international actors. MPI therefore played a decisive role in overall supervision and coordination with other ministries and provinces: it was responsible for providing national development objectives, budgeting and guidelines for provinces and sectors, collecting national and external resources for local and sectoral development, mobilizing and approving ODA and FDI projects, and monitoring the implementation of development strategies and the utilization of ODA and FDI.

The central role played by MPI in this specific setting is, in most other countries, partly in the domain of the Ministry of Finance (MoF). In Vietnam, the concentration of power to MPI was partly mandated by the ambition to continue planning economic development in

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<sup>2</sup> These functions were managed by the State Planning Committee (SPC) before the establishment of the Ministry of Planning and Investment. While MPI is the government’s main actor in the economic domain, there are other institutions for other strategic issues, e.g. national security and foreign policy.

spite of the increasing market orientation, and partly the result of a wish to separate two functions related to public expenditure management. MPI was in charge of the management of public investment, including planning of public investment policies and priorities, while MoF held the executive role in current public finance. This institutional structure allowed MPI to control the drafting of the national Socio-Economic Development Plans (SEDPs) and the management of public investment. For instance, MPI was responsible for the five-year Public Investment Programs (PIPs) and their budget allocations. The PIPs are lists of projects that reflect the government's investment policies and priorities. One consequence of this division of responsibilities was a "dual" budgeting system, where MPI and its departments of planning and investment at the provincial level prepared the investment budget including capital expenditures and donor-funded projects, while MoF and its departments of finance at the provincial level prepared the fiscal framework and the estimates of current expenditure. Hence, there was no unified budget until at a very late stage of the planning process, which created problems for the coordination and the management of the state budget at central and provincial levels, as well as across sectors: not surprisingly, this fragmentation was heavily criticized by the donor community (WB 2005, pp.50-52).

### ***Managing ODA in development planning***

The integration of ODA into the national overall development plans was part of this institutional set-up.<sup>3</sup> The unit within MPI that was given responsibility for ODA management was the Foreign Economic Relations Department (FERD). This organization coordinated ODA resources at the national level, including negotiating and supervising the allocation of funds to most ODA programs. In particular, FERD managed large-scale and capital-intensive loan projects. Based on the objectives outlined in the SEDP and the PIP, FERD prepared a priority list of national projects calling for ODA investment during the current five-year planning period. This priority list was used as an "investment menu" for donors to select projects for their development cooperation. In this setting, it was clear that donors were expected to conform to Vietnam's development plans and operate within the framework given by the set menu. Several donors approached by the authors report that they were typically presented with a limited set of alternative from which to select cooperation programs. However, the selection criteria and selection procedures for MPI's priority lists (the PIP and ODA project lists) were unknown to both donors and local stakeholders. In some cases, this resulted in the selection of projects that appeared to be inconsistent with the development priorities expressed in the SEDP and other official documents (WB 2005).

This centralized system arguably constrained the dynamism of provincial development and the economic autonomy and accountability of local authorities. The government and line-ministries were able to exercise a system where they planned, steered and controlled

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<sup>3</sup> Where ODA is involved, MPI has taken the leading role despite the existing ODA coordinating agencies that consist of MPI, State Bank of Vietnam (SBV), Ministry of Foreign Affairs (MoFA), Ministry of Finance (MoF), and the Office of the Government (OOG). In this structure, SBV has been the signatory of agreements with multilateral financial institutions such as WB, IMF and ADB. MoF has held responsibility for monitoring the flow of funds and controlling disbursement and payment practices. MoFA was expected to use its diplomatic tools to promote ODA mobilization, and arguably played a more symbolic role.

local governments through the provision of public services (e.g. education, health-care, culture, and sport) and infrastructure (e.g. schools and hospitals) (Thang 2004, pp.5-6). It also created a framework where MPI was at the center of a system characterized as “giving and asking for”, which refers to the decisions related to budget allocation and project approvals. David Dapice (2002) argues that with central planning, aid became a strongly politicized process, where provinces had to turn to Hanoi in order to convince MPI that their development projects were of higher priority than others, and that they should be included in the priority lists presented to donors. One consequence of this aid bargaining systems was that many provinces focused mainly on how to get a larger share of the aid budget rather than how to create sound conditions for attracting private investors.

At the same time, it was clear that the central position of MPI was instrumental in creating strong ownership of the development agenda. The institutional set-up allowed the state to regulate not only domestic development planning, but also the allocation of aid and the relations with donors. If donor and aid management had been outside the body responsible for national economic planning, it would undoubtedly have been more difficult to align aid flows with Vietnamese development priorities.

One consequence of the centralization of the ODA management was that the allocation of resources was biased towards the areas preferred by MPI. The resulting distribution of aid was unbalanced both in terms of regions and sectors. Vietnam’s Public Expenditure Review (WB 2005) notes that public investment projects included in the PIPs and ODA priority lists reflected the government’s priority to generate economic growth, and the resources for investments were consequently directed towards the richer cities/provinces where the conditions for further growth were more favorable. Only limited aid resources were allocated directly to provinces during the 1990s. Somewhat surprisingly, the Northern Central Coast and Mekong Delta regions, which exhibited the highest poverty rates, received only a small share of total aid. Much larger amounts of ODA were allocated to relatively wealthy provinces including the regions surrounding Hanoi and HCMC. The lack of concern for regional disparities arguably resulted in increased inequality between provinces (WB 2005, pp.131–132, Nguyen, B.A 2004, UNDP 2005).

Similarly, investments for poverty reduction and social development were not given the same priority as investments focusing on generating economic growth. Throughout the 1990s, aid was concentrated to prioritize growth infrastructure (Nguyen, Q.T 2002, GoV 1999; GoV 2004). For instance, examining the government’s 1993 priority list of candidate projects presented to donors, Pham (1996) demonstrated the government’s focus on large-scale infrastructure. The energy and transport sectors accounted for 70 percent of total the financial requirements for infrastructure projects, while investments for other areas such as social or rural development were very modest (Pham 1996, pp.90-91). Within the large-scale infrastructure field, there was a shift from water and sanitation in the early 1990s to energy in 1996-2000, and further to transportation infrastructure since 2001. The investments to social areas were mainly funded through separate national target programs (NTPs) established in the early 1990s (e.g. Programs 135 and Program 143). It is likely that other institutional structures for ODA administrations would have resulted in a different set of priorities for the use of external aid resources. For instance,

the share of social programs would probably have been larger if the ODA priority lists had been prepared by the Ministry of Labor, War Invalids and Social Affairs (MOLISA), or in a structure where several different ministries had been jointly responsible for setting the priorities.

## **4. A changing role for the government**

### ***Decentralization and institutional change***

The institutional structure where development planning and aid management were strongly centralized to MPI has slowly begun to change during the last few years. These changes are part of a decentralization process that is largely driven by the continuing economic reform process (not least the integration with the international economy) but it is also encouraged and influenced by the donor community. There is still some internal opposition against decentralization, as parts of the government and some line ministries are reluctant to give up central planning in favor of a more market-oriented decision making process, where other actors such as provincial authorities, public interest groups, and business groups can be strategically included in development planning. However, it has proved impossible to maintain full control at the center and to achieve the desired internationalization and diversification of the economy at the same time. These on-going changes are clearly reflected in the changes in the role of MPI and its power relationships with other national stakeholders

A first indication of these changes is the increasing prominence of the National Assembly. There are signs that some of the power of the 15-member Politburo has slowly begun to shift towards the National Assembly. Traditionally, the role of the National Assembly was largely to approve the legislative agenda of the VCP, transforming party politics into national law. Now, it is increasingly taking on the role as the nation's highest decision-making body, and is becoming more active in overseeing the state's activities.<sup>4</sup>

Secondly, the general trend of decentralization has recently been institutionalized in a number of government resolutions and decrees. The most explicit legislation is found in a resolution where the government assigns provincial authorities to participate in the decentralization of six areas of decision-making and power relationships: (i) planning, plan and development investment; (ii) budget and finance; (iii) public assets, land and natural resources; (iv) management of state owned enterprises; (v) management of public service delivery; and (vi) organization and personnel (MPI 2004).<sup>5</sup> The 2002 State Budget Law that came into force in 2004 is another legislative cornerstone. It provides guidelines for how to manage decentralization, give institutional accountability and new power to the provincial people's councils, and define the roles and responsibilities of central and sub-national authorities of government (WB 2005, pp. 47-48). The law also defines a more balanced distribution of power between MPI and MoF, in which MoF becomes the lead ministry responsible for fiscal planning, budget formulation, and debt

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<sup>4</sup> See Resolution No 51/2001/QH.

<sup>5</sup> Resolution No 08/2004/NQ-CP on "Continued Acceleration of State Management Decentralization between the Central Government and Centrally-run Provincial Governments", issued 30 June 2004.

management, while MPI remains the lead ministry for capital budget formulation.<sup>6</sup> This clearly requires better coordination between the two ministries. One interesting development is that several districts have established formal collaboration between the planning and finance functions through the creation of combined Departments of Planning and Finance (WB 2005, pp.120). So far, the same degree of coordination has not been achieved at the provincial and national levels.

Other crucial legal and institutional changes have been introduced through several decrees on decentralization in the area of investment.<sup>7</sup> With the exception of a few National Projects that require ratification by the National Assembly (such as the 5-million hectare afforestation program, the Dung Quat Oil Refinery project, the Ho Chi Minh Highway, the Son La Hydropower plan, and other similar ventures) public investment projects are classified in three groups: A, B, and C. Group A comprises the largest projects in terms of financial investment and national priorities. Categories B and C include projects that are smaller or of primarily local significance. The Prime Minister approves the National Projects, while sectoral ministries and provincial people committee chairmen can directly approve investment for A, B, and C-graded projects.<sup>8</sup> Since investment category A has the highest economic importance, the provincial authorities and sectoral ministries need to consult with the Ministry of Construction prior to making an approval decision. At the district levels, the people committee's chairmen are allowed to approve investment projects with total investment capital of less than VND 3 billion (about USD 200,000). Commune People Committee's chairmen have the authority to approve projects with investment capital of less than VND 1 billion (about USD 70,000 USD) (Nguyen, T.N. 2004, p.11).

In line with this decentralization of public investment decisions, provincial authorities have also gained more autonomy regarding decisions involving external resources, like FDI and ODA.<sup>9</sup> Regarding ODA-funded projects, the Prime Minister approves A-graded projects including budget support projects, national projects, and inter-sectoral and inter-regional projects. The Prime Minister's approval is also required for technical assistance projects with total investment capital of USD 1 million or more. Meanwhile, approvals of B and C-graded projects and technical assistance projects with total capital of less than USD 1 million are decentralized to heads of line ministries and provincial people committees (MPI 2001). Other institutional reforms under the umbrella of a Public Administration Reform (PAR) program lend further support to the decentralization

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<sup>6</sup> MPI retains the responsibility to submit to the government the draft plan on socio-economic development of the whole country, and the major balances of the national economy, which serve as the basis for the financial and budgetary plans. Still, with the various supplementary government Decrees to guide the implementation of the Budget Law and the Government Resolution 08 on decentralization, the role of MoF is clearly becoming stronger.

<sup>7</sup> See Government Decrees No. 52/1990, No. 12/2000, and No. 07/2003.

<sup>8</sup> There are some exceptions to this generalization. 10 out of 64 provinces are managed directly under the central authority, and approval from the Prime Minister is needed for all large projects in these provinces. Similarly, a few strategically important sectors' development plans also require the Prime Minister's approval.

<sup>9</sup> In ODA management, Decree 17/2001/ND-CP serves as the main regulation. Recently, the PM has required MPI to amend this decree to make it harmonize with other decrees in decentralization in management and investment (Resolution 08/2004 and Decree 07/2003).

process. Much of the PAR process is focused on assisting participatory development planning, budgeting and investment management capacity at various local levels. Similar decentralization has taken place in the management of FDI capital (GTZ & CIEM 2004).

Although the decentralization process has grown stronger over time, it has not been seamless. One of the main problems has been the lack of capacity at the provincial level for local development planning, budgeting, and investment management. Moreover, the accountability and responsibility of local authorities as owners of public investment is unclear. There is no comprehensive system for investment monitoring and inspection. These conditions arguably create substantial risks related to corruption and mismanagement (Nguyen, T.N 2004). Hence, although local authorities have been eager to promote decentralization, there are well-founded reasons to be cautious and to focus explicitly on strengthening provincial and regional management capability. The donor community has been an important actor in promoting the necessary capacity development.

### ***MPI the intermediary***

The concentration of power to the center did not only constrain the dynamism of provincial development and the economic autonomy and accountability of local authorities, but it also created other problems. For example, considering the lack of transparency regarding the criteria and processes for the identification of priority investments in the PIP and the ODA priority lists, there were reasons to worry about how efficiently this power was exercised and whether there was a risk for corruption. The dominance of MPI also created a strong bias towards physical investment and economic growth, with much less attention to social issues and “pro-poor” expenditures than what most donors desired.

It is therefore not surprising that the role of MPI has begun to change in line with the overall trend towards decentralization (MPI 2004, GTZ & CIEM 2004) Although MPI maintains a strong position when it comes to development planning, it’s role regarding concrete ODA projects is shifting from one of control and implementation to one of intermediation. Traditionally, MPI and various sector ministries were responsible for establishing the allocative norms for the budget and provincial authorities needed to follow this. Since the introduction of the 2002 state budget law, financial norms are made public and only used to determine the total amount to be transferred to sub-national levels of government. Provincial people committees have the right to decide about the detailed allocation of resources in their jurisdiction. The increasing autonomy of provinces has undermined the traditional role of sector ministries, who can no longer control sector expenditures at the provincial level (WB 2005, pp. 57-120).

The legal and institutional reforms discussed above have paved the way for donors and provincial authorities to expand their collaboration on various ODA investment projects. MPI is still in charge of the supervision and management of investment projects in category A, which are considered to be of strategic importance for national development, but the other two categories of investment projects and most technical assistance projects are managed by provincial governments. Hence, donors do not have to spend time and

effort to convince MPI to support their favorite projects, but may instead initiate projects directly with provincial and local authorities.

The decentralization has also improved the transparency regarding investment priorities. Earlier, MPI's selection procedures were essentially unknown to outsiders, but now MPI consults with donors at Consultative Group meetings (CG) before submitting the list of priority projects to the Prime Minister for approval. This part of the decentralization process reflects both a concern for economic efficiency as well as the changing attitude towards donors, who are no longer seen as any direct threat to national sovereignty. On the contrary, the government now invites donors to establish development cooperation at the provincial level, with particular focus on building capacity for local authorities in order to facilitate further decentralization. It can already be seen that those provinces that have benefited more from decentralized ODA have also developed stronger local capacity (See GTZ & CIEM 2004). Roughly 25 percent of total ODA funds and 72 percent of projects are now managed by provincial authorities and line ministries (UNDP 2005).

One important consequence of the closer contacts between donors and provincial authorities and line ministries is that aid resources have become more closely integrated with domestic budget management. There is a clear trend away from projects that are funded almost exclusively by donors – which can be run separately from the provincial and central budgets – to projects that are co-financed with local resources. This trend has been supported by the 2002 State Budget Law and the decrees on decentralization mentioned above, as well as decrees on Grassroots Democracy. This shift is also beginning to change the sectoral distribution of ODA funds. For example, the recently launched Poverty Reduction Support Credit programs are largely based on direct contacts between foreign donors and provincial authorities, including many of the poor and remote provinces. These programs cover a wide range of pro-poor expenditures towards rural development projects from energy transmission to policy institutional support, with the exact content determined on the basis of the specific priorities of donors and provincial beneficiaries. The likely outcome is an increase in spending on social programs focusing on poverty reduction at the expense of large-scale infrastructure.

The institutional changes in development planning and management reflect some of the impact that the donor community has exercised in Vietnam: individual donors have been arguing for decentralization for a long time, and this pressure has probably had more than just a marginal impact in promoting the changes in the Vietnamese planning system. Donors have been interested in supporting decentralization and public administration reforms at both the central and provincial levels. This has occurred with the full knowledge that the institutional capacity of provinces and districts is weak. Therefore, ODA projects have systematically included components aiming to improve the management capacity of local authorities, with notable success. The improvements at the local level that have been achieved through collaboration with foreign donors have arguably made it possible to raise the objectives regarding decentralization in general. One reason why this has been accepted at the central level is probably the trust that has developed after two decades of development cooperation. Another reason is that it has proved impossible to isolate the donor community from the Vietnamese society at large.

Instead, the contacts between donors and various provincial and sectoral stakeholders have created domestic interest groups that have contributed to the changes in the Vietnamese institutional framework. This is illustrated in the discussion of the CPRGS that follows in the next sub-section.

### ***The Comprehensive Poverty Reduction and Growth Strategy***

The case of CPRGS illustrates some of the relations between the government, here acting as the controller of development policy decision-making, and international donors, exerting external pressure on the domestic decision-making process. It also illustrates how the activities of foreign donors have led to the creation of domestic interest groups that contribute to changing the Vietnamese institutional framework from within.

#### **The intended framework**

In the current international development policy debate that puts priority on poverty reduction, the multilateral development agencies (the World Bank and IMF) request countries to produce a poverty reduction strategy, summarized in a Poverty Reduction Strategy Paper (PRSP), to qualify for development aid. This initiative was led by the multilaterals and launched in 1999 as a way to restructure relationships between donors and recipient countries (Conway 2004, p.1). The political objectives embedded in the PRSP process aimed towards: (i) Shifting the focus of the government's accountability for poverty reduction from external donors to citizens; (ii) Enhancing public participation in policy formulation; and (iii) Encouraging a mode of policy-making in which accountability is related to poverty reduction outcomes, rather than the delivery of direct benefits to particular social groups.

At this time, Vietnam had achieved remarkable successes in combating poverty and was widely recognized as a development "success story" in comparison with other low-income countries (Conway 2004; IMF 2004). When the PRSP concept was introduced, the Vietnamese government was focused on the preparation of its own five and ten-year strategies and plans. These policy documents summarized the government's development policy framework, laying out the long-term development vision and action plans. Yet, there had been concern among both domestic and foreign development planners that these documents focused too much on the party's and government's political ambitions and ideologies. Appropriate development plans were expected to have more concrete objectives and budgetary targets as well as roadmaps for implementation than what could be found in these documents. In this situation, it suited the government's diverse interests to produce a Vietnamese PRSP. One motive was to sustain lucrative development assistance relationships with the international financial institutions and secure access to concessional loans. Another motivation was the insight of Vietnamese development policy planners that such a policy document could help concretize and realize the government development plans. At the same time, it was not politically convenient for the government to replace the five and ten-year plans by a policy framework made up of donor-imposed ideas. To fully adapt the domestic development policy to a whole new development concept introduced by external donors would also imply changing the existing model of development planning. Given the existing institutional setting and

domestic political conditions at the time, the Vietnamese government had both the motives and possibilities to create a fairly flexible system for exercising power and keeping donors under the principle of national ownership.

In mid-2000, the government therefore launched its own PRSP process and the final product became the Comprehensive Poverty Reduction and Growth Strategy (CPRGS) in May 2002. It reflected a “Vietnamese approach” to the PRSP concept introduced by the international financial institutions. Having the document prepared in Vietnamese, Vietnam differs from many other countries where the PRSP has been drafted in English with substantial influence from international consultants (Conway 2004; Ohno and Ohno 2005). Even though draft versions were translated into English for international comments, the process was conducted in Vietnamese for the national audience. The document was drafted by an inter-ministerial committee led by the Chairman of the Department of National Economic Issues within MPI (the department that also prepares the PIPs). The committee gathered 52 representatives from 16 ministries and national agencies.. Four regional workshops were arranged for consultation with the public to get inputs to the policy documents. Donors were invited to make comments during the different rounds of the drafting process.

The Vietnamese version of the PRSP put economic growth and poverty reduction as the two main pillars of development: this also reflects the Vietnamese government’s basic attitudes regarding strategies to promote development and tackling the country’s growing social problems. Three broad objectives were defined in the CPRGS:

1. High growth through a transition to a market economy. This lays out the government’s agenda for structural reform and concrete plans for the implementation of the transition.
2. An equitable, socially inclusive, and sustainable pattern of growth. This is embedded in the detailed plans for implementing sectoral and social policies.
3. Adopting modern public administration, legal, and governance systems. This goal aims to facilitate the design and implementation of policies and programs necessary to attain the first two goals.

The CPRGS was composed by drawing together different components from the existing sectoral plans and adding the poverty reduction elements. The leader of the drafting committee, Dr Cao Viet Sinh, identified five ways in which the CPRGS would add to existing plans and strategies: (1) CPRGS defines time-bound structural reforms and actions that will help reaching the targets in the five-year action plan, (2) all participants in the drafting process will improve their understanding of how to effectively harness economic growth to reduce poverty, (3) CPRGS includes an accountability framework, clear targets and intermediate indicators improving the capacity to measure progress, (4) CPRGS improves the poverty impacts of public expenditure and investment, and (5)

CPRGS is backed by domestic resources as well as ODA, helping to improve effectiveness and quality of ODA delivered to Vietnam.<sup>10</sup>

Inside the government, some stakeholders initially saw the CPRGS as an external document and were generally reluctant to let external actors set the agenda for Vietnam. In the initial drafting process, they therefore remained rather passive, and saw the process primarily as a way for the government to maintain access to lucrative aid. On the other hand, they also realized along the process that they could benefit from ODA by integrating their sectoral interests into the CPRGS. Gradually it became clear that it would not require very much effort to formulate a development strategy with a focus on poverty by integrating components of various existing overall and cross-sectoral strategies into the CPRGS. The adoption of the CPRGS thus became both a way to meet external demands and a way to address some ministerial economic demands, according to some ministerial representatives in the drafting committee.

The CPRGS was initially seen by donors and actors outside the government as a supplementary development document complementing existing strategies and plans. There were reasons for them to believe so. By the time the CPRGS had been produced, it mainly outlined various development objectives but without any budget allocations. This meant that there was no incentive for the government to change the old structure of using the SEDP as the main guide for budget allocation and investment. The CPRGS was instead a guide for the utilization ODA resources. Given the parallel existence of these two strands of development planning, the CPRGS was almost unknown to provincial and local authorities. For provincial and local authorities, the main budget resources were drawn from the government budget, and there, the important guidelines were the SEDPs including the PIPs. As a result, the social policies and poverty reduction programs targeted by the CPRGS ran the risk of being seen as marginal activities in comparison with alternative core priorities included in the SEDP and the PIPs. These were largely focused on construction and industry in areas that were already relatively wealthier (IMF 2004; WB 2005).

Concerning budgeting, the CPRGS indicated that donors were expected to put funds into the CPRGS while the government invested in the five-year action plan. At the same time, sectoral ministries did not classify expenditures that were to be financed from ODA resource according to the standard budget codes, making it difficult for donors to follow up how their funds were integrated in overall public expenditure. This structure was largely contrary to donor arguments asserting that aid funding had to be accompanied by recipient funding in a cooperative manner. Consequently, the donor community wanted to see the CPRGS more strongly linked to national development planning and funding, i.e. integrated with the SEDP and the PIP. However, for the Vietnamese government, the SEDP was the primary policy document: covering not only economics but also political issues and security matters, it was considered to be outside the domain where external interests and funds could be used. Therefore, CPRGS could initially only be used to

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<sup>10</sup> Dr Cao Viet Sinh, is presently Vice Minister of MPI after serving as Director of the National Economic Issues (MPI).

define development objectives, while the mainstream instruments had to be used for actual implementation.

## **Unintended outcomes**

In the few years that have passed since the introduction of the first CPRGS, its role and character have already changed.

Firstly, in an updated version of the strategy formulated in 2003, new objectives have been added to the three main goals identified in CPRGS 2002. According to the revised CPRGS document in 2003, the eight broad objectives for the country's socio-economic development for the period up to 2010 are to:

- (i) Promote rapid and sustainable economic growth coupled with attainment of social progress and equity.
- (ii) Create and equal business environment for all types of enterprises from all economic sectors.
- (iii) Continue with structural reforms to bring about a transformation of the nation's economic structure. This objective includes further integration with the international economy and strengthening the competitiveness of Vietnamese industries.
- (iv) Provide poor households with opportunities to raise their income by accelerating broad-based growth of agriculture, industry, and services.
- (v) Encourage human development and reduce inequality.
- (vi) Solve the particular problems of urban poverty with regard to employment, income, and housing.
- (vii) Develop and expand social protection and safety net for the poor.
- (viii) Undertake public administration reform.

Hence, the revision, there is clearly a stronger emphasis on equity and social issues, although economic growth remains the prime objective. As a result of this, the pattern of ODA utilization has begun to change. Firstly, there has been a reduction in the share of large-scale infrastructure, as well as an increase in the share of funds directed directly to provinces. Policy and institutional support have emerged among the biggest aid sectors, with economic management and administration development as the core sub-sectors. Pro-poor spending, including projects focusing on education, health, and area development, has also increased

Secondly, there are changes in the relations between the government and its foreign development partners. From the government side, major reforms are reshaping the institutional setting for development policy and investment planning. Regarding the donor community, both the international financial institutions and many bilateral donors have an interest in playing a greater role in the Vietnamese policy debate. The process that is underway entails an integration of the ideas embedded in the PRSP/CPRGS into the planning of the next SEDP and its subsequent implementation.

At the policy level, the Vietnamese government has begun to see the CPRGS as an action plan translating sectoral strategies into concrete cross-sectoral action plans with an

enhanced poverty reduction perspective.<sup>11</sup> This view was strengthened in 2003 when, based on a Japanese initiative (Ohno and Ohno 2005, p.3), the final revision of the CPRGS document came to include also large-scale infrastructure. As the largest donor in Vietnam, Japan arguably wields more influence than other donors (especially when Japanese views do not clash with the Vietnamese government's main priorities). The government also wants to take advantage of Japan's interests in promoting growth. The inclusion of large-scale infrastructure in the CPRGS establishes a concrete link between growth promotion strategies and poverty reduction targets. As a result, the final CPRGS document now includes all major policy areas related to comprehensive growth and it can therefore no longer be seen mainly as a social policy document.

Therefore, the government has integrated the core components of the CPRGS into the current five-year plan for 2006-2010. The Prime Minister's Directive 33, issued in September 2004, initiated the preparation of the 2006-2010 SEDP, calling for a more open and participatory planning process than for earlier long-term plans. It also encouraged planning agencies to formulate strategies that put more focus on desired outcomes – both in terms of poverty reduction and growth – rather than input targets (WB 2005, p.55). This indicated that the new SEDP would contain a partly new set of policy objectives, which, in turn, required changes in the process of planning public investment. In fact, Vietnam's annual progress report on CPRGS (IMF 2004) and Vietnam's latest public expenditure review (WB 2005) both concluded that there was already an increasing emphasis on “pro-poor” investment as a result of these incipient changes. New pro-poor targets have been added to the PIP and the criteria for public investment allocation have been adjusted to reflect the policy objectives included in the CPRGS.

One of the main institutional reforms is the establishment of an inter-ministerial working group to develop Medium-Term Expenditure Frameworks (MTEFs) at the sectoral level. This working group matches investment priorities and financial resource in a process that brings together senior officials from both MPI and MoF. Pilot MTEFs have been launched in four sectors and four provinces. The MTEFs aim primarily at (i) abolishing dual budgeting, and creating a consistent and realistic resource framework with balance between capital and recurrent expenditure; (ii) improving the allocation of resources between and within sectors by building budgets around a single, consistent, and realistic set of policy objectives; and (iii) providing sectoral ministries and provinces a hard budget constraint and increased autonomy in order to increase incentives for efficient and effective use of funds (WB 2005). The CPRGS and the MTEFs can be seen as illustrations of the new strategic priorities and integrated approaches to development planning and investment in Vietnam.

Since the CPRGS was initially meant as a guide for the external funding of public investment, donors were encouraged to align their ODA funds with the CPRGS. However, ODA funds were not included in the mainstream budget, which was based on the SEDP.

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<sup>11</sup> Conway (2004) notes that a cross-sectoral development plan with focus on poverty reduction was initiated by Ho Chi Minh City already in the mid-1990s. This subsequently resulted in the national Hunger Eradication and Poverty Reduction (HEPR) Program, which was treated as a social policy program and was separated from the general development goals prior to the existence of CPRGS.

Yet, after some time it became clear that provincial authorities and sectoral agencies had strong incentives to integrate components of the CPRGS into their regular activities in order to secure additional funding from ODA. The incentive structure, therefore, made it hard to keep the two financing systems apart, especially when more funds were committed for the national poverty reduction program outside the standard budgeting system. Interviews with ministerial representatives involved in the drafting committee suggest that some provinces were particularly successful in taking advantage of these opportunities, as well as their entitlements to extra funding from the National Targeted Program 135. This implies that strong government ownership at the policy level may well coexist with a situation where both national and international actors are intensively involved at various levels of the implementation process, influencing the ultimate outcome. It also suggests that the CPRGS and the SEDP probably need to be integrated even closer in the future. In fact, in the planning and content preparation of the 2006-2010 SEDP, the government circulated drafts for discussion to donors and non-state stakeholders, such as the research community, NGOs and representatives of the private sector. This new way of preparing the development plans may be a way to combine the growth and poverty reduction objectives. Yet, while the integration of CPRGS components into the SEDP may work in the short run, it also raises the question to what extent economic planning can be combined with the development of an internationalized and market oriented economy in the longer run.

Summarizing the effects of the CPRGS on the Vietnamese policy framework, it is possible to make a few generalizations regarding the role of foreign donors for the country's structural reforms. A first observation is that CPRGS has had an influence on the domestic politics of development planning and the process of policy making. If Vietnam had been more passive and allowed external actors to formulate a poverty reduction strategy along the standard PRSP programs, it would probably have been a marginal product. The incentives would have been directed towards keeping such a concept as isolated as possible in order to ensure national security and sovereignty. With the creation of the CPRGS, Vietnam instead took the lead and directed the formulation of the strategy, thereby avoiding a defensive position and instead creating a strategy that was largely accepted not only by donors and the international community but also domestically. The recent decision to integrate the SEDP and the CPRGS is likely to reinforce the importance of the CPRGS. Furthermore, Vietnam has come to appreciate the praise that CPRGS has been given internationally. Clearly, the fact that Vietnam is often lauded in international discussions about development and ownership has made the CPRGS better known domestically and given it a higher status. Hence, the CPRGS has become a natural part of development politics in Vietnam, even though this may not have been the intention.

A second observation is that the new framework has also opened new ways for (i) development planning, (ii) policy making and implementation and (iii) resource allocation.

(i) In comparison with the preparation and formulation of earlier SEDPs, the process leading up to the CPRGS has been substantially more transparent and participatory. Government officials have found that the approach used in preparing the CPRGS could

be a model for reforming the planning mechanism of the SEDP. It has reduced the concentration on political “hardcore” objectives and reformed development policy planning. The new cross-sectoral planning with focus on poverty reduction in the CPRGS has demonstrated that more balanced development objectives can be attained also in the country’s strategic development framework. The old SEDPs maintained an economic-focused policy to promote development, which was intended to enhance people’s living standard and reduce overall poverty. However, it did not address the social implications of economic reform. Adopting the social development perspective of the CPRGS has, in particular, strengthened the ambition to achieve sustainable growth.

(ii) The formulation process of CPRGS has established a new mechanism for policy-making in Vietnam. It provided a forum for cross-sectoral policy-making and added new voices from actors outside the government circle, which is unusual in the context of Vietnamese policy-making. The traditional model gave responsibility for national development planning and major socio-economic policies to MPI and its think-tank institutes. The CPRGS has involved new participants in the government’s policy debate. The consultative debates leading up to the CPRGS included Vietnamese NGOs and local communities through workshops and participatory poverty assessments (Conway 2004; IMF 2004). Selective draft versions were prepared to allow international donors to comment on policies and proposals, which reflects a new way of cooperating with external partners regarding development planning in Vietnam. The way donors have been involved and consulted in the CPRGS has given them a new stronger role in the policy debate: foreign donors have been accepted as legitimate partners in the debate even though the sense of national sovereignty remains strong, and even though there are still aspects of policy on which external donors are not supposed to comment remain (Conway 2004). The broader public engagement is clearly in line with the key political objectives of the PRSP process that the donor community hoped to introduce in Vietnam.

Another impact on policy-making concerns the power relationships within the central government. The establishment of the inter-ministerial drafting committee suggests that the relationship between MPI and line ministries has changed. During the drafting process of CPRGS, they worked together as a team to discuss poverty reduction in a more comprehensive and cross-sectoral manner than what had been done earlier. According to Conway (2004), the CPRGS drafting process may have empowered line ministries in their relations to MPI. However, in the short term, MPI maintains a strong position, since it has the lead role in drafting the CPRGS and guiding the reforms in the area of planning and decentralization. In the long run, however, MPI’s role is likely to be reduced by the new mode of policy-making, where it has to enter into broad roundtable debates regarding policy choices with all other ministries (rather than separate and bilateral discussion as previously): this is likely to force the MPI to accept more of the strategic objectives of other ministries. Apart from the influence on the mode of policy-making, the CPRGS has contributed to changing the nature of planning. The development policy planning under the CPRGS framework has introduced a new set of policy objectives that has been managed under explicit resource constraints. The traditional SEDPs did not provide any strategic development framework with concrete policy objectives and budget constraints to guide resource allocation. Instead, it focused more on delivering ideologies and political aims, and providing input targets.

(iii) By providing a new set of policy objectives that strike a balance between socially inclusive development and growth priorities, the CPRGS will have fundamental implications for resource allocation. As discussed above, administrative and budgetary decentralization is in the interest of provincial authorities and localities. The CPRGS has facilitated the decentralization process, both by providing resources for local authorities and by providing an arena where the views and priorities of local authorities can influence the policy making process. Through the channels to policy making provided by the CPRGS, sectoral and provincial authorities have acquired much broader scope for innovative policies as well as access to resources from the national budget and external funds.

In sum, the relations with the donor community have contributed to the changes of the old conventional style of policy planning. Comprehensive consultation with donors and domestic stakeholders in drafting the 2006 – 2010 SEDP marked a giant step in this regard. It reflected both the government's new visions and the changing attitudes towards foreign donors, as well as the changes in the power relationships within the state and between the state and non-state stakeholders. As a consequence of the CPRGS, donors have increased their collective bargaining power with respect to the Vietnamese government. Above all, just by having created the CPRGS, the Vietnamese government has accepted to join the development policy debate driven by donors.

## **5. The future**

The previous section examined the changes in the institutional setting for development planning and development cooperation with foreign donors, and argued that one of the most prominent external influences from foreign aid is a change in the role of the state. This process of change is likely to continue as the integration with the world economy proceeds and creates new interest groups that are unwilling to return to the old ways. Although it is hard to predict how the next steps will look, it is possible to identify a few of the factors that will influence the direction of change. Some of these are related to the degree of decentralization, the character of the budget process, and the role of the donor community.

### ***Central planning vs. Decentralization***

Vietnam's central planning system is in a process of transition. As discussed earlier, the role of MPI and its relations with local authorities and line ministries are changing as a result of various legal and institutional reforms. Recently, there have been calls for a change that would transform MPI into a Ministry of Economics, where its role could be more clearly limited to the management of national economic policy, while the functions related to investment and capital planning should be moved to the MoF. Other suggestions call for a merger of MPI and MoF. It seems unlikely that either of these views can be realized in the short term, as the government still wants to maintain some elements of central planning to control the national economy. However, MPI is now expected to collaborate intimately with the MoF, which is gradually growing stronger, to coordinate the capital and current expenditure sides of public expenditure. Increasingly,

MPI is transforming from a master planner to an intermediary in development planning, as noted above.

Decentralization has also begun slowly. It is slow since the central government is still guiding its progress. On the one hand, decentralization in development planning and budget management has empowered sub-national governments and localities. On the other hand, the capacity and institutions at the provincial and local levels are presently not adequate for meeting the demands of further decentralization. Some cities and provinces are more developed and better prepared for the change, but the majority of provinces lack the capacity and institutional conditions. This indicates that the central government might focus less on whether changes are allowed, but more on what opportunities and demands decentralization is likely to cause. For instance, despite budget decentralization, it is not clear how responsibilities are decentralized for managing those funds that do not belong to the mainstream budget. Moreover, 80percent of provinces face more or less chronic budget deficits, making decentralization a nominal change without much real content. Hence, these provinces still rely on the “giving and asking for” system for central fund allocation. This is not likely to change with a new tax and revenue system (Le 2004, pp. 26-27).

The comprehensive support of the donor community is needed to overcome the lack of local capacity for planning and budget management. At the same time, further reforms to facilitate decentralization may be needed to define the local authorities’ accountability, responsibility, and incentives. Unless the central government can see the real need for decentralization, it will not have the right incentives to accommodate decentralization. Some examples of rational incentives for a government to decentralize are (i) to create a greater managerial efficiency, effectiveness and performance in meeting local needs; (ii) to improve public participation in government; (iii) to get public service delivery in the right place; (iv) to create a synergistic partnership in the provision of services to the people; (v) to create competitive performance spirit in provision of services to the people. (Blunt 2004, p.72). In terms of these decentralization incentives, the process has so far mainly focused on the first item, i.e. efficiency as seen from the point of view of the government and its sub-national authorities. Meanwhile, decentralization for service delivery to the local population has not been prioritized. Therefore, decentralization has sometimes been described as “de-concentration” of state tasks. It is understandable that it has sometimes been difficult to get the participation of the local communities and civil society groups in this process. It seems clear that further reform, including promotion and institutionalization of the role of civil society, will be required to proceed further with decentralization. Such measures would help ensure more openness and participation, which in turn would improve service delivery to the people at both national and local levels. Supporting the development of an open civil society that empowers people and supports the participation of social groups has been a political objective of many donors, especially the Western *Like-Minded Group*. So far, these donors have encouraged bottom-up reforms and development at the grass-root level as a way to create demand for the central government to adopt policy changes. However, an integrated approach, with continued support to the grass-root level together with pressure for institutional reforms at the central level, is likely to be a more efficient strategy for donors than a decision to focus on either of the two.

## ***National budget allocations***

Another area where further changes are likely concerns the sectoral allocation of both domestic and external funds. On the basis of the existing plans regarding the sectoral allocation of ODA for 2006-2010, it seems clear that the allocation for social and rural development will increase. However, it is unlikely that there will be any sharp increase in the state budget for education and health-care in these areas, unless there are reforms of the socialization policies in these sectors. *Socialization* in this context refers to the shift in the financing burden from the state budget to user fees and other private funding sources. However, it should be noted that these policies are increasingly criticized for their unintended negative effects on the poor in general (see Kokko and Tingvall 2007).

The recent decision to include the social development components of the CPRGS in the 2006-2010 SEDP is one of the main reasons for the shift in the budget shares of different sectors. It remains to be seen whether or not the government will aim for a fully integrated development framework where all resources – including ODA – are included (as desired by the donor community). However, as long as there is a separate ODA Strategic Framework annexed to the SEDP, there is a reason to believe that the government aims to maintain some separation between ODA and domestic resources. This notwithstanding, the CPRGS has arguably already influenced the planning process to such an extent that it may not matter exactly how the formal planning system is structured. There are strong enough incentives for provinces to include CPRGS components into their budgets to guarantee that the fundamental parts of the CPRGS will be integrated into the five-year plan as well.

Investment and resource allocations for the development of industry and infrastructure will probably continue to hold a large share of the state budget. This suggests that the role of the private sector in these areas is expected to remain limited. With the ongoing decentralization of the state budget, the government will allocate a given amount of investment funds and assign a set of investment indicators to individual ministries and for education and science to individual provinces. The detailed allocation of resources within these broad expenditure areas will be decided by the provinces. The increased autonomy and incentives to generate funds outside the state budget is likely to change the investment planning system in provinces. This could potentially help overcome the existing problem where provinces compete for the allocation of investment resources to those industries that are defined to be of strategic importance. For instance, the construction of cement, sugar, and steel industries appears as a priority in almost every provincial plan because these industries have been identified as state priorities, which makes it easier to get centrally budgeted resources for them. If provincial authorities and donors instead take the local conditions as a starting point for their joint development plans, the likely result is an improved balance in the sectoral distribution of investment, as well as between capital expenditure and recurrent expenditure, both at the provincial and central levels.

## ***The changing role of donors in Vietnam***

Donor support to the government's development and reform policies has been strong during the last decade, as indicated by the substantial annual aid pledges to Vietnam. The strong support reflects the positive relations between the government and the donor community, and contributes to reducing the worries that have historically been related to foreign interest in Vietnam. ODA has not only been economically important for different state funded development projects, but it has also focused attention on the need to strengthen the state's capacity at various levels, through legal reforms, parliamentary development, and anti-corruption programs. ODA has also generated many diverse interests within and outside the government. Both donors and national aid beneficiaries want to be involved and play a greater role in the government's development policy debates in areas where aid is used as a tool for development. This trend has affected the way the government's policy institutions work and it has altered various domestic power relationships. Thus, an institutional framework that is adaptive to the new phase of dynamic relations with external partners and domestic interest groups has begun to emerge.

Some of the ongoing reforms, like the aim to publish concrete criteria for ODA mobilization and allocation to provinces, illustrate how much the government has adapted to the changing circumstances. In the Hanoi Core Statement on Aid Effectiveness 2005 agreed between the government of Vietnam and the donor community at the Mid-term Consultative Group Meeting (CG Meeting) in Can Tho, the government promises donors to take the leadership to guide and coordinate ODA through national/sectoral program, while donors commit to use these plans as a basis for their funding decisions. This requires that the government presents a single comprehensive program and budget framework, where it identifies investment priorities which the donors can use for their own aid allocation. Hence, the government is expected to define what forms of ODA it wants and how it wants it to be delivered, instead of focusing on maximizing the total value of aid inflows.<sup>12</sup> One motive for this new policy could be that the government is increasingly aware that Vietnam will soon graduate from its status as a concessional credit recipient. ODA inflows are likely to fall, both in absolute and relative terms, and it is more important than before to ascertain that the available development assistance is used efficiently.

The line-up of donors is also changing. The UNDP and a few bilateral donors with a long history in the country played an important role in supporting the government's reform initiatives during the 1980s and the first half of the 1990s. Today, their roles as lead donors have been taken over by the international financial institutions and some larger bilateral donors, like Japan, who provide substantial credits for infrastructure investments and other reforms. Given the comprehensive reforms Vietnam needs in order to meet the challenges from socio-economic changes and international integration, it is likely that the government will need donor support in the future as well. However, it is unclear what kind of development assistance Vietnam will strive for. The World Bank and some other international donors with large amounts of resources – but also strict conditionality

regarding the use of these resources – are positioned to play important roles in future development cooperation. The relative strength of these donors suggests that it may be more difficult to preserve Vietnamese ownership and autonomy over the development agenda than during the first decades of Doi Moi. At the same time, Vietnam is probably less dependent on financial assistance and better able to create domestic investment resources than ever before. Moreover, the cost of external funding will increase when Vietnam graduates from the low-income country group and loses access to concessional credits. This suggests that credits for physical infrastructure may become less important in future development cooperation. Instead, it is possible that programs focusing on institutional development and “soft” infrastructure – public administration, parliamentary development, anticorruption programs, leadership training, and higher education in general – will be more prominent. In these areas, UNDP and traditional development partners like Sweden still play an important role and have comparative advantages in opening doors to cooperation in new sensitive reform areas.

It is unclear how the balance between these two types of development cooperation will develop. Yet, the present choices provide an indication of how substantial the changes in the Vietnamese government’s attitudes towards foreign development partners really are: the choices Vietnam confronts are not mainly related to worries about ownership or autonomy, but concern what kinds of development cooperation and what level of integration are most efficient and valuable.

## **6. Concluding remarks**

The development of the relations between Vietnam and its foreign development partners can be summarized in the form of four observations.

The first point to note is that the lessons from the economic relations with the Soviet Union have had a fundamental impact on Vietnam’s attitudes towards foreign aid and the relations with foreign donors during the decades of Doi Moi. Vietnam grew heavily dependent on Soviet aid before the mid-1980s – largely on the conditions outlined by the Soviet Union – and the termination of aid flows that preceded the decline and eventual collapse of the Soviet Union was a severe shock to the Vietnamese economy. The common Vietnamese perception is that the country gave up too much of its autonomy in return for Soviet aid. One of the strongest determinants of Vietnam’s early relationship with Western donors was to avoid repeating the same mistakes. For a long time, the key priorities for policy making were therefore national security and independence, defined in a broad sense to include economic aspects. The overriding goal was to avoid renewed dependence on external resources and relationships. One consequence for development cooperation with foreign partners was the requirement that Vietnam should maintain strong ownership of its development agenda and control any foreign resources allowed to enter the country. Over time, the deepening relationships with some donors like Sweden and the UNDP have gradually taught the government to trust external partners and to open up for policy dialogues. This has reduced the focus on national security, sovereignty, and independence, and softened the Vietnamese leadership’s hesitant attitudes to international cooperation.

The second observation is that the institutional setting for national development planning and integration has been determined by the overall attitudes towards foreign donors. The need for strong Vietnamese ownership of the development agenda required a decision-making structure where much power was centralized to a strong actor (the Ministry of Planning and Investment) that could exercise ownership on Vietnamese terms and integrate development aid into the country's economic plans. The fact that MPI had primary responsibility both for the national economic plans and for the resources provided in the form of ODA was important to facilitate this task. However, the centralization of ODA management was not only a way for the government to allocate domestic and international resources according to its own preferences, but also a way to reduce the bargaining power of external donors. For instance, donors were not encouraged to initiate their own projects - largely capital investment projects - but instead asked to select projects from priority lists prepared by the MPI. These lists took into account the specific interests and priorities of individual donors, but only to the extent that they coincided with the interests of Vietnamese authorities.

This institutional structure has slowly begun to change as a result of the changing attitudes towards foreign donors. As foreign aid organizations have been allowed more freedom in seeking collaboration with provincial and regional authorities, the government has relaxed its strict central control of aid allocations. In particular, donors are allowed to initiate smaller ODA projects directly with the relevant regional or provincial authorities. This implies a change not only in the relations between MPI and foreign donors, but also a transformation of the relations between MPI, provincial authorities, line ministries, and various stakeholders outside the state: MPI is taking on the role of an intermediary rather than acting as a master planner, as it did in the past.

The changing role of MPI can, in fact, be seen as an illustration of the changing status of central planning and resource allocation in general. Decentralization accompanied by major legal reforms is underway, giving increased autonomy and decision-making power to provinces and localities. This development can be interpreted as a cautious shift away from central planning. A third observation therefore concerns the adjustments taking place in the Vietnamese planning system as a consequence of the collaboration with foreign development partners. The adoption of the CPRGS marks a change in how development assistance and development issues are included in the plans. Before CPRGS, Vietnamese authorities tried to keep ODA separate from other resources available for public investment: the objective was to maintain the system of central planning with as little outside interference as possible. However, over time, the position of MPI and the separation between ODA and other public investment resources met pressure from two sides. On the one hand, foreign development partners insisted that the government should act to integrate ODA resource into the central budget, in order to be able to provide local resources to complement the foreign contributions. On the other hand, regional and provincial authorities gradually learned that they could interact directly with foreign development partners in order to promote ODA project ideas, instead of only lobbying MPI to include their projects in the priority lists presented to the donor community. With promises of financial backing from a donor, they could increase their bargaining power in the negotiations with MPI, raising the likelihood that MPI would support the project and provide counterpart financing to match the foreign resources.

The two processes eroded the traditional form of central planning where MPI directed development according to the preferences of the central government. The CPRGS has institutionalized a new set of policy objectives for public investment and initiated a new structure for decisions about resource allocation. It may also have contributed to the emergence of new power relationship within the central government, particularly between line ministries and MPI. Arguably, MPI is becoming weaker while line ministries and other stakeholders are gaining more influence. The changing institutional structure is increasingly adapted to a market-oriented economy, in which the interests of many different stakeholders are assumed to be taken into account in development planning.

Finally, it can be noted that the Vietnamese economy is undergoing a number of changes that are arguably in the interest of many of Vietnam's foreign development partners. Some examples are decentralization, changes in the planning and budgeting process, increased public participation in policy debates, and a stronger role for the private sector. The donor community has clearly played a role for the diffusion of the new practices, and many of the changes started in aid-funded programs but have gradually spread to other areas. The role of Vietnam's foreign development partners have been to introduce ideas, exert some pressures for change, but also to provide an arena where the government has been able to test new ideas and refine its thinking on development policy. To some extent, it can be argued that the donor community has taken on the roles played by civil society and a political opposition in parliamentary democracies. Although Vietnam still has a long way to go in its transition from central planning to a more market oriented system with a strong civil society representation in policy making, it can be argued that the trends are favorable, and that the relations with the donor community are contributing positively to Vietnam's development.

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