RESTRUCTURING OF PUBLIC INVESTMENT SEEN FROM ASPECT OF SYSTEMATIC RELATION WITH SUSTAINABLE DEVELOPMENT OF PUBLIC FINANCE

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Restructuring of public investment in the context of innovation of development model and economic structure is one of important tasks set for the five-year socioeconomic development plan 2011 – 2015. This paper presents three problems examined in the systematic relation between public investment and other policies within the public finance: (1) Budget overspend and public debt; (2) Public investment and operations of finance market; and (3) Restructuring of the public sector as an instrument for dealing with negative effects from the market. As a conclusion, the author offers suggestions about the successful and effective restructuring of public investment in future.

Keywords: public investment, budget overspend, public debt, public financial policy, finance market, state-owned companies

1. Budget overspend and public debt

A positive public financial policy must be implemented but on certain conditions.

My opinion that has been presented at the NA many times is that Vietnam has to accept budget overspend through borrowing for years to come in order to develop technical infrastructure and facilitate industrialization. It is a positive public financial policy when the capital accumulation and saving are too low to ensure a sustainable development. This policy must be based on strict conditions, such as:

- A clear policy on government and national debts must be in place.
- There must be measures to ensure efficiency of investment projects.
- Ability to repay debts in both domestic and foreign currencies must be ensured.
- Principles of opportunity cost and consistency of public investment must be observed.
- The government must practice thrift.
- Allocation of public investments must be transparent.
- A mechanism for supervising public investment must be perfected.

In the past few years, however, budget overspends have not met above-mentioned requirements, among others, with the result that the "positive public financial policy" became a negative agent that might lead to instability of public finance.

If the public investment is implemented in such a way, it not only increases risks for financial system, but also contributes to macroeconomic instability (inflation and trade gap).

In the past, especially under the National Assembly of 12th term, high budget overspend was allowed to rise and more government bonds were issued in order to ensure public investment in industries and provinces allowed by the NA. However, there is no quantitative assessment of efficiency of these public investment projects. The Ministry of Planning and Investment, of course, has its own criteria for allocating public investments but it failed to produce detailed reports on implementation of such projects. And as a result, all industries and provinces, after their development projects were approved, competed fiercely for disbursement because source of public investment was limited. This practice went against list of priorities and consistency of public investment. This source of capital was scattered while the government had to pay interest and projects could not be completed as planned because of slow disbursement.

This way of allocating public investments made me think that the central government had to cover all projects and programs after starting them otherwise all investments become a huge waste.

Vietnam is facing a lot of difficulties. All fields and provinces are badly in need of investment. It is necessary, of course, to prioritize them according to certain conditions. At a national level, investment in depressed areas should aim at political and social goals while that in regions with favorable conditions, such as the Southern Key Economic Zone, is for bigger budget income. For example, if priority is given to rural, mountainous or border areas, development program of national level must be carried out with support from the central government in all stages, from planning, implementation to evaluation of result, instead of assigning totally to local governments. In vocational training programs, full attention must be paid to development of army of teachers and employment for graduates instead of being limited to building of schools. The same thing can be applied to health care service.

Thus, allocation of public investment cannot be simply based on selection of industries or areas. Each project must be devised carefully to ensure that all projects are useful after completion and influential in local economic development. At present, Vietnam has no mechanism for determining responsibility for ineffective public investment.

What is the safe limit for public debt?

Vietnam's public debt (according to definition presented in Public Debt Management Law) of today includes mainly long-term loans, which puts no big pressure for repayment. In 2011, it is still safe for Vietnam to allocate VND85,000 billion for debt repayment out of a total budget income of VND590,000 billion (some 15%). However, if the after-debt income and regular expenditure keep decreasing, the public debt may exceed its safe limit. If budget overspend prolongs by 10 years because of increased public investment and fails to produce higher values and surplus needed for expanded production (which reflects in difference between budget income and regular expenditure plus debt repayment), danger of insecurity does exist. In other words, if Vietnam gets loans in 2001 to increase public investment when no budget surplus exists, it should gain some budget surplus in 2010 after covering regular expenditure and debt repayment. This idea forces me to suggest analyzing and assessing the public debt in the past 10 years and developing a new public financial strategy for the next 10 years to serve as a basis for assessment of financial safety. If no prediction at both macro and micro levels is in place, insecurity may become insolvable when it appears. This situation is called bankruptcy.

2. Relation between public investment and operations of finance market

In the years 2001-2005, the Vietnamese economy recovered in the wake of the regional financial crisis and gained an average growth rate of 7.5%. In this period, outstanding credit from the banking system rose by 23% or 24% on average; budget overspend was kept under 5% of the GDP; and ratio of gross investment to the GDP was 38%.

In 2006, everything looked normal (growth rate was 8.3%; outstanding loan rose by 24% and the budget overspend equaled 5% of the GDP). From 2007 onwards, however, anomalies took place: Outstanding loans rose suddenly and in the opposite direction to the growth rate (in 2007 the growth rate was 8.6% while the credit growth was 53.4%; these figures were 6.4% and 27.6% in 2008;

and 5.3% and 37.3% in 2008 respectively), budget overspend equaled some 7% of the GDP while the gross investment equaled 42% of the GDP.

According to my observations, causes of the situation are as follows:

Firstly, bubbles of stock and realty markets in 2006-2007 made the supply of credit skyrocket creating a huge volume of virtual assets (gap between financial and real assets) and inflation in those two years bridged this gap with new average market prices. The credit growth in those years did not lead to increases in real assets and only produced some changes in nominal GDP. Moreover, increased trade gap in the past three years also caused the money supply to rise while the local economy, because of a low added value in manufactured goods, could not gain a higher growth rate (it is estimated that from 70% to 80% of the trade gap was transformed into export value without making the GDP rise).

Secondly, in the years 2008-2010, the stock market was still a secondary one and all companies had to depend on banks for their working capital, which led to imbalance between supply of and demand for bank credits and favorable conditions for establishment of small-scale joint stock commercial banks and higher credit growth. This situation made the monetary policy deviate from its orientation and forced financial authorities to adopt regularly ad hoc solutions, which led to serious danger of instability. Along with effects of the global recession and financial crisis, the situation made investors lose their confidence with the result that both loan and capital stocks could not solve the problem while commercial banks enjoyed chances to gain super-profit. Although profits for banks increased, risks in the whole banking system and macroeconomic instability were not reduced and tended to change their forms instead.

Thirdly, increased and prolonged budget overspend became insolvable. Poorly planned public investment that did not observe principles of opportunity cost made the ICOR higher. To facilitate the growth rate, the public investment in 2009-2010, including investments from national budget and state-owned companies, rose quickly employing a huge volume of credit while budget overspend only relied on credit and increases in the money supply. Even government bonds also depended on supports from commercial banks instead of the public. Generally speaking, both the national budget and economic sectors were dependent on the banking system. A huge volume of money flowed to this sector but poor investment plans failed to produce a corresponding volume of assets, which lowered capital turnover.

These causes could explain the credit growth in the past three years and serious imbalance in the finance market. The major cause, of course, lies in the economic structure but financial and monetary policies, and especially the fiscal policy, have profound effects on the economic structure and they have not been estimated exactly. Thus, the urgent task is to employ monetary and fiscal policies to direct restructuring of the finance market; force companies in all sectors to execute financial restructuring; prevent commercial banks from borrowing and lending too much; and make the stock exchange a real channel of direct investment.

3. Restructuring of the public sector as an instrument for dealing with negative effects from the market

The restructuring of the public sector should aim at helping it play well its regulatory role and supply better “public goods and services” needed for a sustainable development.

From this point of view, we can see three problems with the public sector: (1) poor distinction between companies run for profit and non-profit public institutions (it does not mean that these institutions are unproductive but their owners refrain themselves from collecting profit; (2) poor management that reflects in failure of state-owned companies to ‘direct’ the market without a monopolist mechanism in spite of the fact that they are enjoying a non-profit status (having full rights to their after-tax profit); and (3) failure to supply public goods and services, and develop key industries that produce low profit and require big and long-term investment, such as engineering, supporting industries, high technologies, etc. In my opinion, public investment must reflect political determination of the government instead of depending on financial consideration taken by state-owned companies.

Thus, the restructuring of the public sector must aim at turning it into a material force that regulates effectively the market besides other regulatory instruments. This is an important feature of the restructuring because it not only improves the state control over economic activities but also links economic development with social progress and equality. A law governing the public sector is now an urgent matter to Vietnamese law makers.

In Vietnam today, it is necessary to develop a set of concepts of public finance based on ideas of a positive public finance, and use budget overspend to built infrastructure and stimulate the economic growth. This policy, however, is a two-edged sword that can produce bad effects when the public management mechanism is poor.

Restructuring the public investment requires reforms in the public financial management that has a lot to do with the administrative machinery, allocation of public investment, mechanism for supervising and assessing business performance, and conceptions of role and functions of state-owned companies. That is why the restructuring of public investment should be considered against the whole system to work out an appropriate track. One of priorities at present is a reform in the National Budget Law that aims at distinguishing two classes of budget: national and provincial ones. The central government establishes public financial regulations and local governments have autonomy in working out their own budget incomes and expenditures based on approval by provincial people's committees. The national budget (including grants-in-aid for local governments) is determined by the National Assemble. The overall goal is to make the annual Budget Act according to international practice, thereby ensuring the supervision of the national budget by the NA and local budgets by local people's committees■

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