



## For More ODA Disbursement when Public Investment is Cut

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### 1. Introduction

According to Harrod Domar and Hollis Chenery models of investment-based economic growth, the investment deficit (gap between investment and saving) is the main obstacle to the economic growth and the trade gap, as the second one, hinders development, especially in poor and developing economies. The ODA, or foreign aid, is one of external sources of capital that helps bridge the two gaps. Unlike other sources, such as FDI, commercial loans, immigrant remittance or export earnings, the ODA is an additional source to the public resource for governments to increase the public investment (as part of the gross investment), reform policies in the long run, and generate dynamic for the economic growth. And at this stage, the economic growth is supported by various sectors that help reduce poverty and inequality between classes and groups of residents.

External resources can't replace the internal

one in implementing development targets in many countries in the past decades but shortage of investment, skills, knowledge and right policies in the first stages of development in poor countries proves the importance of foreign aid. This source of foreign aid includes not only soft loans and additional source of foreign exchange, but also technical and training assistance, transfer of technologies and experience that provides a basis for plans to implement millennium targets (set by donors). Vietnam is one of poor countries in their struggle against obstacles to their socioeconomic development. Making the best use of the ODA could be considered as coordination of efforts from the public, the government and external support to establish and implement the development policy more effectively based on the world's advanced technologies and skills.

### 2. Size and rate of ODA disbursement in Vietnam

Up to the end of 2007, Vietnam has established development cooperation with 28 bilateral donors,

23 multilateral donors and 350 foreign NGOs. Vietnam has cooperated with the community of donors to organize 15 CG meetings. In the years 1993-2007, the total pledged ODA amounted to US\$42.449 billion (see Figure 1) from such leading donors as Japan, WB, ADB, France, UN organizations, and Germany. Up to the end of July 2008, the signed ODA value was US\$33.39 billion, including US\$27.72 billion worth of ODA loan and 5.68 billion worth of grant. Total disbursed ODA fund amounted to US\$20.97 billion equaling 62.8% of the committed ODA fund, comprising US\$16.14 billion credit and 4.83 billion grant.

data also show that proportion of fund disbursed for ODA projects in Vietnam by five banks for development in 2006 was low: ADB: 8.7%; AFD 19.4%; JBIC 13.1%; KFW 15.6% and WB 12.5% while the average proportion gained by regional countries was 20%.

This rate, however, seemed to improve in 2007 (US\$2 billion) and rose quickly in the first half of 2008 (US\$1.28 billion), especially in the fund for electricity, communications, agriculture and rural development projects. This result came from efforts by the Vietnamese Government and the community of donors: ODA rules were perfected constantly in 2007; delegation of ODA project management introduced by Decree 131/2006/NĐ-CP has been implemented properly; reports on works in progress have been made regularly and timely with uniformed forms; donors tried to harmonize their procedures with ones in Vietnam; the Hà Nội Commitment was carried out; and the "One UN" initiative to unify 16 UN organizations in Vietnam was implemented, etc.

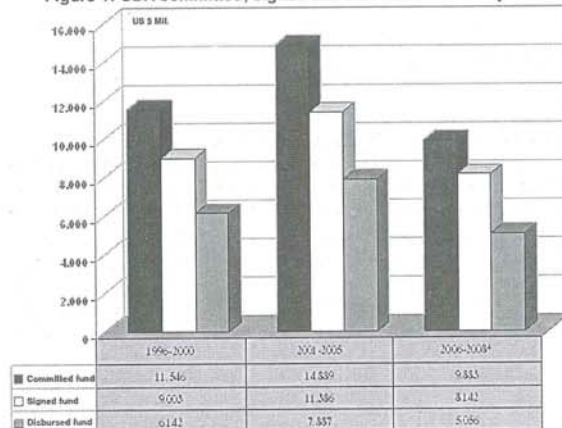
Many frame agreements were signed and carried out in 2007, such as the one between Vietnam and six UN organizations in Vietnam (US\$218 million); Vietnam-Sweden frame agreement on development cooperation (US\$100 million); the WB seven Poverty Reduction

Support Credit, or PRSC7, (US\$150 million); credit from some co-sponsors (US\$317 million) with maturity of 40 years and a grace period of 10 years and an interest rate of 0%; ADB agreement on financial support to Mông Dương thermo-electric plant (US\$931.57 million); Project to develop communications in the Mekong Delta (US\$150 million); and WB credit of US\$50 million for the HCMC Investment Fund for Urban Development (HIFU); etc.

### 3. Reduction in the public investment and absorption of ODA fund

In 2008, the Vietnamese Government

Figure 1: ODA committed, signed and disbursed over the years



(\*) Signed and committed ODA fund up to July 25, 2008. Source: MPI

Although Vietnam isn't totally dependent on foreign aid, it is among the world's biggest recipients of aid. The disbursed ODA rose steadily in the years 1995-2000 and reached its peak in 2000 when the ODA fund equaled some 5.5% of its GDP. The disbursement rate, however, slowed down in 2001-06 and the ODA fund was equal to 3% of the GDP (2.8% in 2006 and 3.05% in 2007) (see Figure 2)

The disbursed ODA fund in 1998-2000 was US\$4.2 billion. This figure rose to US\$4.5 billion in 2001-03 (increasing by 6% over the previous period) and 5.2 billion in 2004-06 (increasing by 16%), which shows that the disbursement rate hasn't been improved remarkably although the Vietnam's growth rate stayed around 7-8%. Other

persuaded local authorities to cut public investment to curb the inflation. For the time being, disbursement of some VND10,000 billion from the sale of T-bonds (equaling 25% of the proceeds of T-bonds) is delayed until the end of this year. The central government asked all ministries and provincial governments to review and cut fund for various projects and programs. According to An MPI report, up to July 23, 2008; 1,968 projects with a total investment of VND6,000 billion have been suspended or cut (of this figure, 1,884 projects with a total investment of VND5,662 billion are run by local governments). This effort aims mostly at projects that have just been started (72% of projects delayed), such as projects to build office buildings for local authorities, revamp historical relics, or build museums. In short, these projects are "not really necessary," or "no longer suitable and effective." The reduction in public investment as required by the central government, however, can't be limited to the act of delaying projects to be started this year and making reports on the total investment to be put in these projects. Ministries and provincial governments should accelerate the implementation of projects that produce long- and medium-term effects on the socioeconomic life (such as ones in electricity, water supply, communications, job creation, improvements in competitiveness, and development of new services, etc.)

In such a situation, fast disbursement of the

ODA fund didn't go against the said trend but, moreover, it is meaningful. Firstly, the fast disbursement accelerates completion of the projects (most projects in Vietnam are carried out very slowly in comparison with surrounding countries); increases benefits from the projects because it comes into operation sooner (lower overheads, supervision cost and commitment cost); and restructures the investment portfolio with a view to concentrating in projects with far-reaching effects that can enhance the infrastructure, improve the environment, and provide more benefits for agriculture and rural development, thereby improving the efficiency of the investment portfolio by the Government.

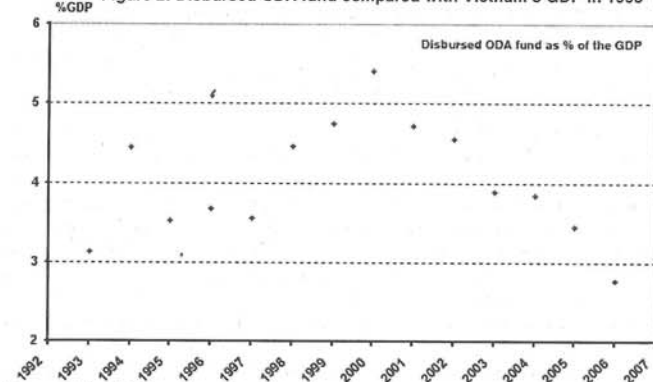
Secondly, besides ODA provided for projects, there are ODA credits supplied to small and medium enterprises in an effort to encourage clean production, energy thrift and rural development. These constitute a precious source of finance because of their low interest rates and long maturity. This source, however, can meet the demand of some 5% of small and medium enterprises.

Thirdly, ODA for programs, such as poverty reduction (PRSC 1 to PRSC7) and program 135 (stages 1 and 2), is added to the budget income as interest-free loans of long maturity with a commitment fee of 0.75%, which constitutes a good external resource for the Vietnamese government in terms of finance, technology and

dynamic for economic reform, poverty reduction and improvement in public management. Finally, the ODA could be considered as a source for covering the trade deficit and stabilizing the exchange rate.

It's worth noting that most ODA-financed projects aim at

Figure 2: Disbursed ODA fund compared with Vietnam's GDP in 1993-2007



Source: MPI and ADB

upgrading and building the infrastructure while ODA credits try to reduce the poverty and ODA technical assistance helps reform procedures and develop human resource. They always produce positive effects on the socioeconomic life and are different from projects to build new office buildings or history museums that contribute nothing to the economic growth. Thus, the cut in the public investment has nothing to do with ODA-financed projects. Moreover, the Government should increase the supply of capital outlay to accelerate projects that are carried out when the inflation rate is high.

#### 4. Some suggestions

##### a. For the time being:

- To improve the ODA disbursement, the Government had better turn part of budget expenditure on projects that have been delayed into capital outlay for ODA projects, especially ones that have been postponed by hikes in prices of building materials, in order to accelerate the work, reduce arising expenses and ensure their positive effects on the economic growth when they come into operation.

- ODA credits from authorized banks and governmental institutions could be used particularly for supporting small and medium enterprises when the bank interest rate is too high (21% a year). Of courses, the small and medium enterprises as recipients of such credits should implement requirements set forth by donors (clean production, energy thrift, rural development, etc.).

- Disbursement of capital of US\$467 million from the PRSC7 program signed on July 29, 2008, and US\$274 million for the program 135 of the Stage 2 must be accelerated. This is the ODA support with no interest rate for programs to alleviate the poverty, and support low-income residents in rural and vulnerable sectors in order to limit the increasing poverty during a period of high inflation rate.

##### b. In a longer run:

The ODA is an external resource that could support medium-term development projects (2011-2015 and 2016-2020) to improve and modernize the infrastructure in key economic zones and big cities. The ODA source in the

coming period will not be as large as in the past and degree of preferential treatment is also lower (because Vietnam's personal income surpasses the medium level), so dependence on this source for development is not feasible. So full attention must be paid to the following:

- (1) The ODA should be used only for projects of top priority in such fields as energy, urban communications, and clean water, etc.

- (2) The ODA should be used for projects to develop communications in big cities and developed areas (highways, metros, monorails, etc.) because this source comprises not only financial support, but also technologies and managerial skills. The ODA source will account for 40% or 50% of the gross investment and be the most suitable source of capital (because of its long maturity and low interest rate) for Vietnam to keep the structure of long-term investment in balance and make the need for investment in development harmonize with resources available for different generations.

- (3) Private sector should be allowed to take part in ODA projects because this practice can attract capital from this sector to infrastructure projects. To realize this cooperation, the Government should make the best use of technical assistance from the WB, the ADB and Japan (they have experience and are good at attracting private investment in the infrastructure projects) to build the legal basis for the cooperation and mechanism for distributing risks.

- (4) An Investment Law should be made to establish transparency of the public investment. This law can help define the delegation of rights and duties to use the public investment, classification of projects, roles of different sectors in the infrastructure projects, criteria for assessing and valuating projects... thereby enhancing efficiency of projects financed by the public investment ■

#### Reference:

- ODA Bulletins issued by the MPI in 2007 and 2008.
- <http://mpi.gov.vn>
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