SOURCES OF FINANCE FOR THE SOUTHERN VITAL ECONOMIC ZONE

REALITIES AND SOLUTIONS

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I. REALITIES

According to Decision 44/1998/QĐ-TTg by the PM, the Southern Vital Economic Zone (SVEZ), as the core of the Eastern South Vietnam, includes HCMC, Đồng Nai, Bà Rịa-Vũng Tàu and Bình Dương with close relations with the Central Highlands and Mekong Delta. It is planned to turn the SVEZ into an economic center that facilitates the development of surrounding areas.

In the years 1996-2000, it represented a 30.32% share in the GDP while it accounts for only 3.8% of the area of the country. Its average growth rate in this period was 10.1%, equaling 170% of the national average.

To achieve this growth rate, this zone attracted a lot of investments. In the said period, the total domestic investment put in this zone was VND155,260 billion equaling 35.4% of the national gross investment (it reached a peak of VND15,244 billion in 1998). This zone also attracted large sums of foreign investment: this source of capital represented 43.21% of the gross investment put in this zone. Regarding the structure of investments, we saw that 58.2% of the gross investment was put in manufacturing and construction sector.

At present, there are many problems concerning investment for development of this zone. They are as follows:

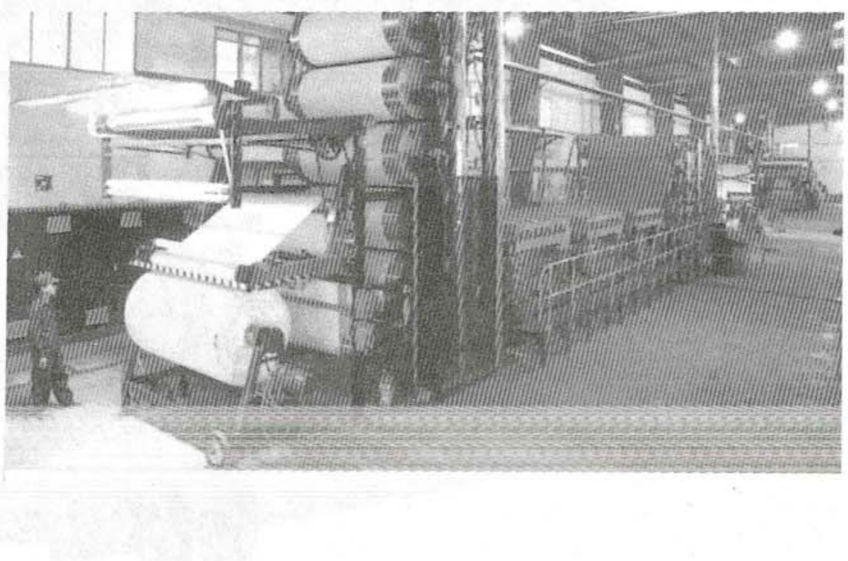
1. The gross investment of the SVEZ is still small. The gross investment in the years 1996-2000 in this zone equaled only 31.2% of its gross product. Its ICOR index was 3 which could only allow a growth rate of 10% or 10.5% while the target set for the zone is a growth rate of 14% or 15%.

2. In the second half of the period 1996-2000, there was a decrease in the realized capital as shown in the following data:

- The ratio of gross investment to GDP fell from 39.25% in 1997 to 21.87% in 2000. The ration of investment in this zone to the national gross investment fell from 37.03% in 1997 to 27.14% in 2000. Although the private investment rose year after year, this increase couldn't make up for falls in foreign and public investment.

- Forty-three percent of the decrease in the gross investment in this zone was due to falls in investment from the foreign sector, especially in 1998 when effects of the Asian financial crisis were felt (the FDI fell to VND14,291 billion in 1998 and 12,710 billion in 1999).

Falls in the gross investment



will affect the economic growth of this zone in the coming years if no effective measures are taken.

3. Distribution of investments among industries and projects isn't effective failing to ensure sustainable development.

- Investments from the government were concentrated better in infrastructure and rural development. Some projects, however, weren't completed as planned. Procedures for getting funds from the treasury were so complex that many local governments had to start other projects or have others delayed.

- Because the FDI was concentrated in certain industries, there were signs of excess of supply over demand (beer, cement, steel and sugar), and some factories could use some 15% of their installed capacity. This situation originated from the lack a master development plan and the presence of some unreasonable policies (for example, excessive protection for such products as steel and cement).

- In the past few years, some ODA - financed infrastructure projects have been realized in this zone but they were carried out slowly because projects weren't prepared carefully, site clearance was done slowly, counterpart funds weren't available and tender invitation wasn't made on time.

- The source of credit from state-owned banks is available but well-prepared projects were rare. Most private investment was put in service industry. The State failed to stimulate the demand for investment.

4. Financial authorities lacked policies to make the best use of public investment and in the near future there is no prospect of finding effective solutions for this problem.

Table 1: Investment in SVEZ in 1996-2000 (VND bil., 1994 price)

	1996	1997	1998	1999	2000
Investment	28,821	34,258	33,803	28,519	29,859
HCMC	18,645	22,959	23,983	18,897	19,700
Đồng Nai	4,423	4,770	3,711	2,615	2,682
Bình Dương	2,138	2,722	4,050	5,325	5,679
Bà Rịa-Vũng Tàu	3,615	3,807	2,059	1,682	1,788
As % of the national gross investment					
SVEZ	37.03	38.06	38.54	34.58	27.14
HCMC	23.96	25.51	27.34	22.91	17.91
Đồng Nai	5.68	5.30	4.23	3.17	2.45
Bình Dương	2.75	3.02	4.62	6.46	5.16
Bà Rịa-Vũng Tàu	4.64	4.23	2.35	2.04	1.62

Table 2: Structure of investment in SVEZ (%)

	1996	1997	1998	1999	2000
Public investment	11.21	13.07	12.05	13.00	16.71
Foreign investment	47.17	46.27	42.28	42.67	37.48
Private investment	41.62	40.66	45.68	44.33	45.81

Source: Reports from local governments in the SVEZ

II. OBJECTIVES

In mobilizing capital for the SVEZ, full attention should be paid to the following objectives:

- Top priority should be given to the investment for development when making socioeconomic development plans.

- Both domestic and foreign sources of finance could be mobilized for development but the domestic source will play the decisive role.

- In mobilizing funds, the Government could make use of the system of financial-monetary instruments by perfecting the finance market and developing the stock market.

- Ways of employing funds economically and effectively in accordance with the modernization and industrialization program should be worked out.

Measures to mobilize capital for investment should be based on ways of tapping potentials of the SVEZ and liberalizing labor forces.

To achieve a growth rate of 11% or 12% in the 2001-2010 period, the SVEZ needs from VND80,000 to 92,500 billion a year and keep the ICOR index at low level (from 3 to 4).

III. SOLUTIONS

1. Reforms in management of public investment

In managing the national budget, the central government had better allow local governments to retain a bigger part of their tax revenues because investment from SVEZ provincial budgets is low in comparison with its gross product (only 2%). That is why the SVEZ governments always lack funds for infrastructure development and industrial production. Besides increasing part of budget revenues retained by local governments, the central government could give more autonomy to local governments in deciding their expenditures in a manner appropriate to local socioeconomic development. More details of this reform are as follows:

- The central government only sets targets for local budgets (total revenue and expenditure, and percentage of total revenue to be sent to the central budget); local governments are allowed to decide on how to generate budget revenues and what to spend their retained revenues on provided that they observe the following principles: expenditures on administrative machinery should accord with regulations; expenditures on development projects and other social and cultural programs are determined by local governments in accordance with their resources. This reform could encourage local governments to control existing sources of revenue and generate new ones, and more importantly, to use public expenditures more effectively.

- The Government could give incentives to surpass the revenue target set for local governments. The use of this extra revenue will be determined by provincial People's Committee and People's Council provided that this revenue is used for development projects. This measure will offer equal opportunity to all provinces.

- Local governments could be allowed to use their financial reserves set aside as required by law to invest in development projects when money from the central budget is slow to be allotted, and they should repay the debt when receiving the allotted money.

- Besides issuing project bonds, local governments could borrow from the central fund for investment and other sources of idle money. The central government could guarantee foreign loans made by local governments.

- Local governments could be allowed to impose surcharges or surtaxes on certain imported goods (cigarette and alcoholic drinks for example) or fees on the use of public works.

- The policy to allot a specific area of land to private persons or companies who agree to undertake an infrastructure project, as realized by Bà Rịa- Vũng Tàu government, proves to be effective. The central government had better make regulations on this practice with a view to preventing abuses.

2. Mobilizing private investment

Besides preferential treatment offered by the Domestic Investment Law, companies in the SVEZ can enjoy more incentives to invest in high technologies (cuts in company income tax, new site for relocation, etc.).

a. As for state-owned companies, the Government had better encourage them to increase their capital investment from retained profits or borrowings from banks and finance market. Measures that could be taken are as follows:

- If the payment for company income tax made by the state-owned company for this year is higher than the amount it paid in the previous year, the extra amount could be returned to the company in order to help it increase its capital investment. The new capital goods will be exempt from capital tax and after-tax income generated by these capital goods will be at disposal of the company.

- The central authorities only set the minimum percentage of amortization of capital goods (or the maximum time for amortization) and let the director of the company decide on the amortization rate with a view to encouraging the company to replace its capital goods.

- Allowing state companies with increasingly high profitability ratio to enjoy the following privileges:

+ to form funds for bonuses and social welfare equaling six months' payroll.

+ to increase pay for laborers higher than the official salary scale.

+ to provide directors of companies with responsibility payments.

- Revaluing resources allocated to state companies in order to determine companies' responsibility for managing and developing these resources.

- Company directors can be allowed to decide on recruitment of laborers and their salaries according to company's business performance. As for the management, directors are selected (through examination) and appointed by central authorities; directors can appoint vice- directors and chief accountants according to standards set by law and with approval of provincial governments. If the company suffers losses for three successive years, the management (director, vice- director and chief accountant) are to be fired and bear responsibility for damage caused by their decisions.

- State-owned finance companies could be formed, in the SVEZ provinces at first, to direct and manage public investment and act as state representatives in both state and private companies with a view to helping companies increase their capital investment.

- Giving more autonomy to local governments in valuing assets of state companies to be privatized, sold or leased.

b. As for private companies, the Government had better ensure them treatment no less favorable than what is given to state companies in terms of financial services, licenses to export and import, quota allocation, tax incentives and other relating matters. To encourage their capital investment, the Government could take various measures, such as:

- Forming a credit guarantee fund for private companies in order to provide them with an access to state-run sources of credits and other financial services.

- Forming associations of private companies according to their fields of activity: These associations can undertake various tasks, such as managing the credit guarantee fund for small and medium enterprises, supplying information and advisory services and helping their members work out common business strategies, etc.

- All measures to supporting companies in the SVEZ will be determined by local governments with approval from the central government. To achieve this aim, local governments should reform their administrative procedures for examining investment projects and granting certificates of investment preferences; and then, carry out regular inspections and apply sanctions to companies that violate regulations.

3. Mobilizing foreign investment

a. Better infrastructure:

In recent years, the infrastructure in the SVEZ has been improved but it still falls short of expectations of investors. In the coming years, the SVEZ governments should pay full attention to this matter by:

- Perfecting the infrastructure inside and outside industrial parks (but priority should be given to project inside industrial parks),

- Granting land to companies that undertake infrastructure projects in forms of BOT, BT, and BTO,

- Developing and upgrading vocational training centers in order to provide skilled laborers for FDI projects.

b. Better public image for the SVEZ:

The SVEZ has potentials for foreign investment and faces competition from other industrial parks in neighboring countries, so it needs marketing campaigns and incentive schemes to attract more foreign investors.

c. Detailed list of projects for the ODA source:

In the past, there were only a few projects in the SVEZ financed by the ODA source, so local governments should prepare everything for receiving ODA-financed projects by:

- Making plans to attract and use the ODA source in accordance with the master plans for investment in province,

- From these plans, making a list of projects qualified for support from donor countries with a view to avoiding inconsistency between objectives set by donor countries and by the master plans for investment.

- Expanding relations with international financial institutions to look for support for development projects.

All above-mentioned solutions will produce intended results only on condition that they are part of a system of solutions dealing with a wide range of socioeconomic problems (reforms in education, administrative machinery and legal infrastructure, etc.). Working out the system of solutions will demand a lot of efforts from local governments of the SVEZ provinces and cities■