Restructuring Vietnam's Public Investment: Problems and Recommendations

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ABSTRACT

The government's public investment plays a decisive role in the national infrastructural development and investment attraction. Yet it will be achievable on the condition that the structure of public investment is logical in terms of attraction and allocation of investment sources. As we can see, albeit public investment has greatly contributed to the national economic growth in past years, there are many flaws in its structure which have affected its efficiency. Therefore, the present paper aims to pinpoint drawbacks in the structure of public investment, the mechanism of management and utilization of public debts; and extend some suggestions for perfecting the structure of public investment in Vietnam.

Keywords: Public investment, restructuring of public investment.

1. PROBLEM

Investment is the act of acquiring necessary commodities for a specific project. Viewed from the aggregate supply side, this activity is to renew, modify, improve, and modernize the capital of the economy, as well as to raise aggregate demand and promote economic growth. It can be undertaken by economic agents such as the government, enterprises, or individuals. In the economy, even though the public investment represents a humble percentage in comparison with that from enterprises or private persons, its influence on the private investment and the entire economy is extremely profound. It is often implemented in accordance with a certain schedule and depends on the governmental decisions as well as the way of managing such investments for economic transition and sustainable development.

Since *Đổi Mới*, despite negative impacts from the global economic shocks, Vietnam's economy has maintained a stable economic growth pace. This is also thanks to increases in capital accumulation and investment. However, Vietnam's economic development have not clearly reflected its ample potential due to the fact that it has employed an inefficient growth model and depended heavily on exploitation of natural resources and capital (as admitted by VCP Central Committee report at the National Congress IX). Relying too much on capital may lead to inefficiency of investment, especially public investment. Therefore, it is advised that Vietnam should restructure its economy, especially public investment. This requires a comprehensive evaluation of the public investment for pinpointing drawbacks in its structure and having punctual adjustments.

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2. RESTRUCTURING PUBLIC INVESTMENT VERSUS ECONOMIC GROWTH

Public investment is part of governmental spending on investing commodities and the most important of which is socioeconomic infrastructure. Investment structure is part of the economic structure and plays a very important role. As Vũ (1982) put it, the public investment structure can be deemed as all quantitative and qualitative relationships among components of the public investment in a period of time and in a certain socioeconomic circumstance.

The quantitative relationship includes ratios of public investment in terms of inputs (sources of finance turned into public investments) and output (fraction of public investment in each industry and zone). Meanwhile, the qualitative relationship reflects the outcome and efficiency of public investment in every sector of the economy in their correlation and overall impacts. Any appropriate and reasonable quantitative change is able to result in qualitative changes, and all qualitative changes are always based on quantitative changes. Such changes take place over time and correspond to the socioeconomic development as well as available conditions, yet will never be identical to or reiterate any of the previous status (Bùi, 2010).

Structure and restructuring of public investment can be viewed from many facets such as (1) input including mobilized sources and their shares in the economy, (2) mechanism for allocating, managing and employing public investments, (3) output including shares of public investment allocated to each industry and zone, and its efficiency.

Public investment is very crucial to the economic growth because it represents a substantial percentage in the gross investment. Viewed from the aggregate supply side, investment decides the increase in capital, expansion of production, and improvement in technology as well as sustainable development (Mankiw, 2000). That is, investment distributed among different sectors of the economy helps establish the economic structure and then determines the economic growth.

Viewed from the aggregate demand side, the ratio and volume of investment will decide the demand for commodities and the structure of investing commodities (i.e. machines, equipment, means of transport, infrastructure, etc.); and reflect its impacts on the aggregate demand of the economy (Samuelson and Nordhaus, 1989). This greatly affects the structure and development of production of capital goods. Based on the aforementioned analysis, public investment and its structure have profound impacts on the economic structure and determine economic growth.

Examining structure of public investment means answering the question of what are sources of finance for public investment and what are their shares. Public investment comes from four sources: national budget, state-owned enterprises, state credits, and others. Yet, in basic terms, it is mainly from savings of the government, enterprises, or laypersons. Once savings soar, so does the public investment. The governmental saving is part of income retained after deducing the public expenditure. Thus, high public expenditure leads public debt, including borrowings from other entities in the economy.

In the economy, national savings depend heavily on the ratio of private and public savings and spending to the nation's income. This is the relationship between present spending and future one, and must be satisfactorily tackled. Turning savings into investment in order to achieve long-term targets as confirmed by Mankiw (2000) requires effort to guarantee the possibly highest ratio of spending. If savings are over-mobilized, it will result in the so-called "paradox of savings" which adversely impacts on the long-term development. Changes in the structure of public investment sources will ensure sustainability for these sources.

Policy-makers and managers also have to establish a mechanism for allocating public investment. In the market economy with governmental control, allocation of public investment must ensure both socioeconomic efficiency and short- and long-term targets.

Public investment must aim at developing socioeconomic infrastructure and attracting investment flows from non-public sectors to restructure the gross investment. Moreover, it must stimulate the intensive economic growth and enhance the technological level so as to generate the crowding-in effect on the economy in the long run (Mankiw, 2000).

In order for public investment to have positive effect on the economic growth, the policy on choosing qualified contractors for public investment projects must be constructed on the motto "Vietnamese support Vietnamese commodities"

Examining output of public investment involves identifying how public investment is divided among industries and zones and what are its effects and efficiency. Public investment in different sectors of the economy will decide a structure of industries and economic zones (i.e. economic structure). Economic structure in turn decides the economic growth because the growth rate is the product of the total growth pace of each sector or industry and its share in the GDP. Therefore, restructuring public investment is a crucial part in the restructuring of the economy.

In sum, the restructuring of the public investment must be comprehensively undertaken in all stages, from mobilization of investment sources to allocation, management and employment of public investment. This process, if done well, will bolster the restructuring of economy and beef up the transition as well as sustainable development.

3. THE CURRENT STRUCTURE OF PUBLIC INVESTMENT IN VIETNAM

Firstly, let us take a look at sources for public investment. In past years, consecutive high economic growth rates supported capital accumulation, which helped increase the gross investment and the public one as well. Table 1 shows the continuous increase in public investment in the period 1996-2010 although it rose more slowly than investment from private and foreign sectors in the years 2001-2010.

Table 1: Growth of Investment in Vietnam

Period	Gross investment	Public investment	.Private investment	Foreign investment
1996-2000	12.2	20.2	8.1	1.0
2001-2005	13.0	10.2	20.9	9.9
2006-2010	13.3	9.3	11.4	25.7
1995-2010	12.9	13.4	12.7	12.4

Source: www.gso.gov.vn

Although the share of public investment in the gross investment went down from 42% in 1995 to 38% in 2010 (apart from the peak of 59.8% in 2001), public investment still takes a crucial share in

Vietnam's investment structure. Compared with the GDP, the ratio of economic investment to GDP increased from 27% in 1995 to 31% in 2001 and 43% in 2010.

Investments by the national budget and state-owned enterprises constitute three quarters of the total investment in the public sector. Investment in the public sector, despite making up a large percentage in the gross investment, has plunged since 1996 due to the equitization of state-owned enterprises.

The ratio of public investment to the gross budget income is 1.4 in 2002, 1.22 in 2002 and 1.41 in 2009. This implies that the government had to take out a tremendous loan or the governmental savings were not sufficient for investment. It also explains why Vietnam's investment is constantly larger than the national savings as confirmed by Bùi Quang Bình (2010d). If this situation is not improved, Vietnam needs more than VND500,000 billion to complete approved public investment projects in the period 2011-2015 as scheduled; but in fact, it has just mobilized VND225,000 billion as yet (See "Tái cấu trúc đầu tư công: Phải bắt đầu từ tầm nhìn của người lãnh đạo" available at http://www.baodienbienphu.info.vn/)

The structure of input sources for public investment contains some irrationality such as: (i) public investment represents a large share in the gross investment; (ii) public investment is larger than the national savings and thus hampering the domestic spending as well as sharply affecting the aggregate demand; and (iii) excessive public investment causes the governmental debt to rise, increases trade deficit, and leads to high inflation.

The mechanism for allocating, managing and employing public investment also reveals various drawbacks that cause huge waste and inefficiency. The application-approval mechanism in allocating public investment over zones is the biggest problem. Allocation of public investment to economic zones is not reasonable and still follows a traditional fashion, that is, public investment is divided evenly among provinces partly based on population and certain conditions, such as local mineral resources, infrastructure and market conditions, etc. The zonal authority does not actively coordinate resources for local development, causing public investment to be scattered and reducing efficiency (e.g. every province wants to build its own seaport, air port, university, and industrial park or special economic zone, etc.).

Closer examination of projects (such as those related to communication, irrigation, hospitals, schools, etc.) approved by the NA for the period 2011-2015 and sources for public investment shows that two thirds of projects financed by the national budget and governmental bonds have been started and delayed for lack of fund. Furthermore, this mechanism makes local government more dependent on the governmental support without actively attracting other sources of investment.

The output-related structure of public investment is reflected via purchase of commodities and services by public fund. A reasonable structure of such purchases not only stimulates the development of related industries but also enhances the economic growth. Public investment project is often of large scale and represent a tremendous demand for commodities and services. The output structure comprises purchase of commodities and services from foreign and local enterprises. Ordinarily, when local enterprises cannot complete a project or a part of its which requires high technology or good management, foreign providers will be hired.

Vietnam, in recent years, has also imported a large amount of commodities and services used for public investment projects. As the Vietnam's Association of Construction Contractors put it, around 90% of EPC (engineering, procurement, and construction) contracts fall to Chinese contractors. Nearly a half of VND248,000 billion worth of public investment in 2010, which was financed by the national budget and foreign loans, fell to the hand of Chinese contractors (Tấn Đức, 2011). By July 2009, around 30 Chinese enterprises have participated in 41 crucial EPC contracts in Vietnam (which related to national resources or energy security) either as the main contractors or as investors. For instance, SEC, in 2009, became the EPC contractor for two thermal power stations (Quảng Ninh 1 and Quảng Ninh 2) which costs over US$400 million for each, and another one (Vĩnh Tân 2) worth US$1.3 billion. Also in 2009, Dongfang Electric Corporation of China in collaboration with Marubeni of Japan won the project of Hải Phòng 1 thermal power station which costs US$500 million; and then in March 2010, they once again won another EPC contract worth US$1.4 billion for the project of Duyên Hải 1 thermal power station (Phạm Huyền, 2011).

Based on aforementioned analysis, public investment, viewed from aspects of allocation, management and employment, has some drawbacks such as (1) the application-approval mechanism fails to encourage local government to mobilize sources of finance; and (2) use of public investment for buying goods and services needed for publicly-invested projects is not reasonable, that is, (i) many commodities and services in Vietnam are imported while local enterprises can supply them, or (ii) policies in choosing providers of such commodities and services are not adequate and need adjustments. These drawbacks have severely affected the national economic health such as (i) the GDP growth rate and aggregate demand are impeded due to unsaleable commodities and services, (ii) the trade deficit becomes higher, and (iii) Vietnam's currency is devalued and thus pushing inflation rate up.

In order to consider the output structure of public investment, let us start from the efficiency of public investment and allocation of public investment among zones and industries. As mentioned above, division of public investment among too many zones leads to waste of resources. The investment efficiency, in general, is not high, which may partly be due to drawbacks in public investment. Moreover, since 1995, in order to push the national GDP up, it has required more investment. Yet, contribution of public investment to the rise in GDP is quite humble (see Figure 1); and once the efficiency of public investment is low, that of the gross investment will go down accordingly (see Figure 2).

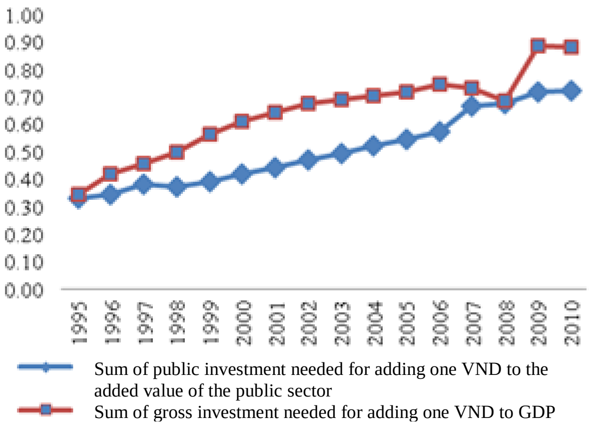

Figure 1

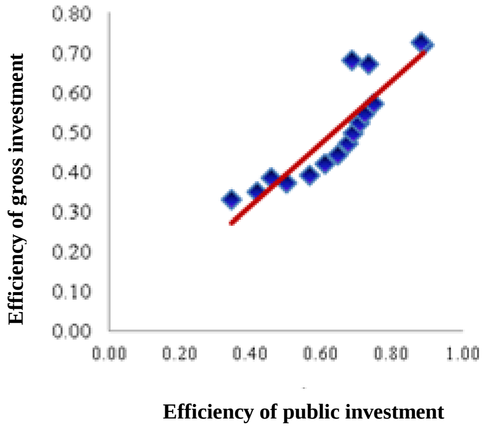

Figure 2

Source: Author's calculation based on data supplied Tài khoản quốc gia và Đầu tư của TCTK (National accounts and investment by stock market), www.gov.vn

Regard sources of investment in industries in Vietnam, Table 2 shows that investment in agriculture is rather low, just roughly 7% and has not matched the role of agriculture in Vietnam. In the construction industry, the gross investment contributes around 45 to 47 percent while public investment is just 40 to 41 percent, or even 34.6% as in 2008. For investment in the service industry, the gross investment constitutes 44 to 47 percent while the public investment makes up 51 to 57 percent. As we know, public investment is often used for socioeconomic infrastructure or industries that manufacture capital goods instead of construction and services as seen in Vietnam today. This tendency is unreasonable.

Table 2: Distribution of Investment Among Industries in Vietnam (%)

	2005		2007		2008		2009		2010	
	Gross investment	Public investment	Gross investment	Public investment	Gross investment	Public investment	Gross investment	Public investment	Gross investment	Public investment
	100	100	100	100	100	100	100	100	100	100
Agriculture, forestry, and mariculture	7.5	7.1	7.1	7.2	6.9	8.2	7.5	6.7	7.1	6.7
Manufacturing & Construction	47.7	41.3	45.7	42.0	46.3	34.6	47.7	40.4	45.7	40.0
Service	44.8	51.5	47.2	50.8	46.8	57.2	44.8	52.9	47.2	53.3

Source: www.gso.gov.vn

Table 3 illuminates the above-mentioned analysis. The ratio of public investment in manufacturing sector (which are supposed to enhance the technological level of the economy) is roughly 10%. Investment in socioeconomic infrastructure just accounts for 32 to 35 percent of the total public investment. This is to state, public investment has been thinly distributed although its sources are limited.

Table 3: Distribution of Public Investment in Infrastructure and Manufacturing Industry

	2005	2007	2008	2009	2010

Manufacturing industry	9.2	10.9	5.9	9.3	9.1
Production and supply of electricity, gas, hot water, steam, air conditioners	14.6	13.4	11.5	15.1	14.9
Supplying water; managing and treating waste and sewage	3.9	3.9	3.9	3.9	3.8
Information and communication	5.6	5.6	5.6	5.6	5.6
Education and training	5.4	5.6	5.6	3.9	4.0
Medicare and social welfare	3.4	3.3	3.6	2.8	2.8
Entertainment	2.1	2.3	2.0	1.6	1.6

Source: www.gso.gov.vn

In general, viewed from the output structure, public investment bears a lot of drawbacks such as (i) it is thinly distributed, and thus hindering projects from completing as scheduled, causing waste of resources and failing to encourage specialization and cooperation; (ii) public investment is not focused on socioeconomic infrastructure, and thereby creating a bottleneck in the economic growth of Vietnam; and (iii) the low efficiency in public investment causes that of the gross investment to decline.

4. PROBLEMS WITH THE STRUCTURE OF VIETNAM'S PUBLIC INVESTMENT

The aforementioned analyses show that there are a lot of drawbacks in the structure of Vietnam's public investment, which must be well tackled to facilitate the economic development in the period 2011-2020.

- The efficiency of public investment is not high. Many of publicly-invested projects must be deferred due to lack of capital and thereby causing a great deal of unnecessary waste and curbing labor specialization as well as production cooperation.

- Public investment exceeds the national savings, generating a severe imbalance between accumulation and spending, huge trade and budget deficit, and high inflation.

- Inappropriate allocation of public investment leads to unbalances in the socioeconomic development as well as an uneven economic growth among zones and industries.

- The policy on buying commodities and services contains a lot of irrationalities, adversely affecting the aggregate demand and domestic production.

- Local authorities have not been active enough to mobilize other sources of investment but depend on the governmental support.

- Main goals of public investment are still unachievable when the public investment in infrastructure is quite modest. Investment in technical enhancement and technology is limited and that in agriculture is extremely low.

5. RECOMMENDATIONS

Vietnam's public investment, despite contributing a lot to the national economic development in past years as well assuring the role of the government in macroeconomic management, contains many drawbacks. Therefore, in order to restructure the public investment, it is suggested to attend to the followings:

- Enhancing the socioeconomic efficiency should be considered as the basis for restructuring of Vietnam's public investment in time to come. Efficiency of publicly-invested projects should be improved and should generate positive effects on the efficiency of the gross investment.

- Cut public investment gradually to balance the national savings and reduce public debts as well as guarantee the harmonious relationship between accumulation and spending.

- Allocate capital appropriately to each zone, and focus on major socioeconomic infrastructure projects and key industries to promote the technological capacity of the national economy.

- Improve the policy on buying commodities and services needed for publicly-invested projects in the direction of supporting Vietnamese commodities and stimulating the development of local production; harmonize procedures of tender with international practices, establish online bidding programs, and organize a panel of inspectors and appraisers under the National Assembly to inspect and appraise big projects.

- Use of public investment should help mobilize other sources of investment.

- Promote the active role of local authorities in attracting sources of investment■

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