

would minimize the danger that government-supported SME centers compete directly with private providers, or undercut the existing market by providing subsidized services.

B. Projects by Location

170. Donors are starting to fund more PSD activities at the provincial level, focusing particularly on assisting local authorities with the implementation of laws and regulations enacted at the national level. While the majority of projects (69%) are still concentrated in the major urban areas, there does not seem to be any glaring gap when it comes to project locations, although mountainous and more remote regions such as the North West, the Central Highlands, and the South East, comprise less than 10% of all projects.

C. Projects by Beneficiaries

171. SMEs are the focus of 50% of donor PSD activities. Half of the projects inventoried also include a capacity building component for government agencies. Rural non-farm SMEs have not received focused donor support in the same way that urban SMEs have in the past. Household enterprises and those in the semi-formal/informal sector have also been overlooked as beneficiaries. Most credit lines are being channeled to only a handful of financial institutions, most of whom are state-owned or government affiliated. This concentration of resources has the potential to reinforce the existing government dominance in the banking sector and crowd out private players.

D. Projects by Sector

172. Of the 58 PSD projects inventoried in this study (not including Judicial and SOE reform projects), only a quarter target a specific sector or economic activity. Conversely, 80% of sector-specific projects are focused on export-oriented businesses and activities. Even within the services industry, interventions in the tourism, hotels and restaurant sector are focused more towards the external market, rather than the domestic market. Three sectors were mentioned by donors as potential areas for further support:

- *Services.* The field of Information and Communications Technology (ICT) is one area that has a lot of potential and the tourism industry could also use additional support.
- *Agriculture.* Assistance in growing quality rice is another gap that was mentioned by donors during interviews.
- *Manufacturing.* The manufacturing of furniture is a growing industry and could benefit from additional donor inputs.

173. The above review shows that there is a significant – though not always systematic – presence of external assistance sources in the area of PSD. Policy dialogue on wide-ranging PSD issues has mainly been supported by multilateral agencies (World Bank, IMF, ADB), USAID (under the STAR project) and most recently by Japan under the New Miyazawa initiative. Funds for long term credit have been provided on a fairly large scale, but perhaps without enough attention to diversification of channels and mechanisms. There is a rich variety of initiatives in the areas of microcredit, business services, training in small business management and entrepreneurial development, but the results have not been systematized into an approach replicable on a large scale.

V. SUMMARY OF THE ANALYSIS AND IMPLICATIONS FOR ADB STRATEGY

174. The principal findings of this private sector assessment can be summarized as follows:

- The private enterprise sector already plays a significant role in the economy, generating over 40% of GDP and employing 30% of the workforce. If one includes private farm households to these numbers, total contribution to GDP becomes 60% and employment close to 90%. Total value-added of the private sector remains low, as most private enterprises are microenterprises selling low value-added goods into local markets. The growth of most private enterprises continues to be constrained by their difficult access to finance, land and information.
- The Government recognizes the importance of the private sector in supporting the continued growth of the economy. While the general attitude of the government appears to favour control over private sector activities rather than facilitation, important progress has been made in improving the conditions for investment. The large body of new legislation which has been introduced to govern business activities now requires some harmonization, but the most relevant challenge is moving from legislation to implementation, and ensuring predictable and transparent application of existing laws.
- The State intends to retain a significant role in the economy, not only through heavy regulation but also in the ownership and management of thousands of SOEs which compete directly with the private sector and generate an estimated 29% of GDP. SOEs enjoy preferred access to credit, land and markets which deters private enterprises from making the investments required to successfully compete against them. Improving competitive conditions is a major challenge for the government going forward.
- Viet Nam's infrastructure development needs are considerable. However, the government's attitude towards private sector participation through BOT and other similar arrangements is unclear, and the capacity of local governments to develop public-private partnership opportunities is weak. Conflicting regulations both allow and prohibit private sector participation, and low tariff levels, incomplete regulations, and "bundling" of sector utilities all contribute to reducing the potential for widespread private sector participation. During the next five years, gradual removal of these barriers should be accompanied by individual demonstration projects, at both the national and provincial level. At the same time, given the large investment requirements, there is scope for gradually increasing private contractors' participation in public procurement.
- In Viet Nam's highly regulated economy, local governments play a critical role in improving conditions for private investment. The creation of "one-stop shops" in some provinces has greatly reduced the time and costs associated with regulatory compliance, and has catalyzed more investment. The replication of these best practices throughout the country should produce a similar result.
- The market economy requires reliable mechanisms with which to resolve disputes. While key legislation is now in place to govern contracts, bankruptcy, creditor rights and arbitration, much remains to be done to strengthen the mechanisms for the enforcement of decisions. This effort should be part of a broader program to strengthen the capacity and transparency of the judicial system.
- External assistance to PSD comes from a variety of multilateral and bilateral agencies and NGOs. While their programs broadly cover all of the important components of the investment climate (legal and regulatory, access to resources and markets, SOE reform, judicial reform), support tends to be concentrated in the design rather than the implementation of reforms, particularly in the area of land reform, private participation in infrastructure and dispute resolution.

This analysis, taken together with ADB's current programs in Viet Nam and the bank's overall technical focus, forms the basis of the proposed PSD strategy outlined below.