

# **The Vietnamese Transition from Plan to Market: Transformation of the Planning Mechanism**

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## **The Vietnamese Transition from Plan to Market: Transformation of the Planning Mechanism**

For more than three decades the construction of a planned economy was the lynchpin of the program of the Democratic Republic of Vietnam (DRV) leadership for the transition to socialism. The historical reasons for the centrality of planning in this program lie, not simply in ideology, but in the disasters which beset the advanced capitalist economies during the decades prior to World War II and in the political, social and economic inequalities which colonialism inflicted on Indochina. The alternative offered by the planned economy of the Soviet Union held a powerful attraction for nationalists in Vietnam, and elsewhere, who wanted to achieve not only rapid economic development, but a more stable economic system, free of the cutthroat competition and cycles of boom and depression which caused so much suffering, and a more egalitarian and democratic society. Like other socio-economic systems, however, the planned economy turned out to be no less full of contradictions. Despite numerous reform attempts and the external appearance of rapid development, Soviet-style planning, in the last instance, lacked inner vitality. In one way or another, then, all the socialist countries have turned back to the market, though not necessarily to capitalism. This chapter examines the contradictions in the planning system of Vietnam and the way in which the planned economy itself gave rise to the seeds of its own destruction. However, while the old methods of planning have now been almost universally abandoned, the idea of planning for development is still very much alive, as the experience of numerous Asian countries testifies. And this is no less true for Vietnam. The final section of the chapter therefore examines the slow process of adjustment by the Vietnamese state apparatus to the techniques of planning within a market environment.

### **Organisation of the planning system before 1989**

In the 1970s and early 1980s, the main instrument of economic planning in Vietnam was the State Planning Committee (SPC) which was in a sense a 'super ministry' since the work of all other economic ministries was subordinate to the plan. In fact, SPC stood at the head of the whole planning apparatus which extended down to the basic production and trading units of the economy. Its function was to allocate material supplies and capital to the various components of this apparatus. The State Price Committee then worked out the accounting prices, Ministry of Finance made the budget allocations according to plan, the Ministries of Domestic Trade, Foreign Trade, Material Supply, and Food carried out the distribution of planned inputs and outputs, and the line ministries, provincial and other local economic departments as well as the industrial and agricultural enterprises were responsible for implementing the production plan. Even the 'non-state' sector, comprising agricultural and artisan cooperatives, was subject to plan directives for much of its output. Non-economic ministries, such as health and education, also received supplies and budget allocations according to plans worked out by the SPC.

The chairman of SPC was always a Deputy Prime Minister and a member of the Politbureau, while the person normally responsible for day to day management was the Permanent Vice Chairman who usually held the rank of Minister and could also be delegated to stand in for the Chairman. These two were in charge of the Committee of 15 members, or Vice Chairmen, who were usually also Ministers or Vice Ministers (thus unlike the Permanent Vice Chairman, several of the others were part-timers). Committee members were each responsible for one or more General Departments or Ministries: ministerial areas might be treated separately or in blocs, depending on their level of importance and links to other ministries. Below the Committee were a number of departments, most of which had their

equivalent in a ministry. For example, for the Ministry of Agriculture there was a Department of Agriculture within the SPC. Planning for the Ministries of Defence and Interior was also carried out by Departments within the SPC, the heads of the relevant departments, holding at least the rank of Colonel.<sup>1</sup> In addition there were a number of specialised departments, such as those for Investment Planning, Short-term Planning, Long-term Planning, Cambodia, Laos<sup>2</sup>, Personnel, Information, and technical departments responsible for the calculation of construction norms and budget estimates. There were also two research institutes (Planning; Long-term and Regional Planning<sup>3</sup>) and a journal (Planning Review).

At its peak, towards the end of the 1970s, around 800 specialists worked in the Departments responsible for line ministries and in the technical departments. The most important Departments were the Investment Planning Department, responsible for planning both the total capital investment targets and allocation of these between ministries and provinces, and the Supply Department which played a similar role in relation to inputs. Two further departments which worked closely with Investment Planning were responsible for estimates of project costs and for calculating construction norms (i.e. quantities of inputs required for particular types of construction) and allocation of supplies between projects. Capital was required to be allocated to projects according to these norms.

Comment: [TP 11/9]

Comment: [LV 12/9]

### The Planning Process

The most important planning activity of the SPC was in developing the country's annual plans. In September every year a meeting was held to discuss proposals to submit to the Prime Minister for the following year's plan. By this time of year, reasonable estimates could be obtained for the current year's outcomes which formed the basis for planning for the next. Among the main targets involved were the quantities of fuel and food to be imported and the amount of export goods which could be supplied to Vietnam's trade partners. In the lead up to the September meeting, therefore, the SPC would calculate inputs and outputs for the current year and by what percentage exports and imports could be increased in the following year.

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For the external trade plan, the SPC contacted the planning organs in other socialist countries and reached agreement with them as to the quantities and assortment of imports and exports. Vietnamese ministries were consulted beforehand to draw up a list of their requirements and key ministries were represented in the delegations which went abroad to negotiate trade deals. Since Vietnamese industry was heavily dependent on foreign inputs, the ability and willingness of the country's foreign trade partners to supply goods and capital was the key determinant of plan targets. The negotiation of trade deals was difficult for the Vietnamese because while they needed to import 'hard' goods (that is goods which their CMEA trade partners could sell in the world market for hard currency), the exports they could offer in exchange largely consisted of 'soft' goods, for which the demand was artificial. Once trade agreements had been reached, the SPC developed a set of *indicative* targets which were then submitted to the Prime Minister for approval. After receiving this approval, the targets could

<sup>1</sup> In the 1970s, this was a very high rank in the Vietnamese armed forces. Only the Chairman and Permanent Vice Chairman were involved in the planning of areas in these ministries directly related to national defence and security. However, economic activities of the two ministries which, in the case of Defence were quite substantial, went through the normal planning procedures. These areas included state farms and garment factories in the case of Defence and prison industries in the case of the Interior Ministry.

<sup>2</sup> These last two were chiefly concerned with distribution of aid to the two countries.

<sup>3</sup> In the 1990s the former appears to have been disbanded, the latter became the Institute for Strategic Planning, while the Central Institute for Economic Management was absorbed into SPC.

then be distributed to the different ministries and provinces for preparation of their more detailed plans.

Comment: [TP 11/9]

This process of developing indicative targets was the first source of conflict in the system. While the SPC knew exactly what was needed and what was the productive capacity of the economy, the Party and Government leadership were rarely satisfied. It was not normally possible for the latter to argue with the SPC's input targets, but higher output targets were frequently demanded. Excessive output targets were always justified by the productive *potential* of the country and the leadership tended to pay little attention to actual capacity.

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This was particularly a problem in relation to decisions on construction of new projects. Numerous cases can be cited in which planners argued for the abandonment of projects which they regarded as wasteful of resources. In some cases they succeeded. More often, over the two decades before 1980, political reasoning prevailed over economic reasoning.<sup>4</sup>

Comment: [LV 12/9]

One gets the sense, from talking to those involved in the planning process, that considerable courage was needed to take on the leadership over matters affecting the political objectives of the latter. The issue of who would take responsibility for bad decisions was a difficult one for the planners.

Comment: [e.g., LV 12/9; PH 23/9; DP 12/9]

One of the greatest difficulties was caused by the distribution of capital between industry and agriculture. Although about 40% of the total was invested in industry, there was always a shortage in this area relative to the desired number and size of projects. On the other hand, the roughly 20% of capital allocated to agriculture represented a very small part of its needs, largely due to the fact that a high proportion of this went to the internal migration program. Given the limited available capital and high resettlement targets, people moving to the mountain areas suffered from especially poor living conditions, due to lack of social and physical infrastructure investment, and many did not remain. In the short term then, much of the capital allocation to agriculture was wasted and, although the Investment Department frequently proposed reducing of the migration plan, the political leadership remained unmoved.

Comment: [LV 12/9]

After the Prime Minister's approval of the indicative targets had been achieved, the next step involved ministers, heads of SPC departments and the provincial People's Committees in the development of more detailed plans.

This was the second source of conflict in the system. Since the total quantity of inputs was fixed, every minister and People's Committee would argue for a bigger share of the scarce resources. In the case of fuel, for example, only about two thirds of the needed quantities could actually be imported each year, so for each ministry and province it was a matter of special pleading to maximise its share. Because of the tendency of enterprises to over order (in anticipation of shortages), the use of norms based on past experience was an important weapon in the hands of the planners during these negotiations. When agreement had been reached, the task of ministers and provincial planners was to go back and develop plans with their individual production units or, in the case of the provinces, with with district-level People's Committees to inform them how many tractors, tonnes of fuel, etc they would get and what they had to provide for the government. Enterprises learned how many resources they would receive and made their plans accordingly. They too were under stress because they nearly always received less inputs than were needed to achieve the output targets.

Comment: [TP 11/9]

At each level, therefore, there was some scope for negotiation over input and capital allocations within the constraints imposed by the technical norms.<sup>5</sup> In the final analysis,

<sup>4</sup> According to one source, the SPC only rarely challenged its political masters. However, during 1978-80, it was sometimes successful in having large scale industrial projects halted.

<sup>5</sup> Fuel allocations for agriculture for example, were based on the number of tractors. In negotiations with a province, SPC could decide to ignore the fact that a number of the province's tractors were not working, so that

ministries or provinces with particular requirements needed to argue for these with the SPC. Committee members and heads of SPC departments, because of their close working relationship with the ministries under their control (indeed some Committee members were actually ministers or vice-ministers of those ministries), usually lobbied for these ministries, so that in practice the Permanent Vice Chairman had to be the final arbiter. The latter then had to balance all targets received from the lower levels and submit the concrete plan to the Prime Minister. However, in its negotiations with lower levels, the SPC was in a much more powerful position than in its negotiations with the Party leadership. Given the resource constraints, lower level organisations came to the SPC in the position of supplicants in competition with each other and, as we shall see below, their ability to achieve their goals depended more or less on personal relationships with those at higher levels. However, there were changes over time. In the early 1960s, when the DRV had only a few hundred factories, these negotiations could be very complicated and there was more scope for flexibility, but as the number of SOEs grew into the thousands, this scope diminished and the process became much more bureaucratic.

Comment: [TP 11/9]

At all stages of this planning activity by the government apparatus there was involvement of the Communist Party. The Politbureau, especially the General Secretary, was directly involved in the plan making procedure, particularly in the decisions on project construction and output targets, and the final plan was also approved by the Politbureau prior to being submitted by the Prime Minister to the Central Committee Plenum at the end of the year. Responsibility for arguing the case for the plan to the Central Committee lay with either the Chairman or Permanent Vice Chairman of the SPC, both of whom, of course, were members of the Central Committee.

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In December, after the Central Committee meeting, the National Assembly also considered the plan, usually discussing it for about a week and sometimes making revisions, before approving it. Once this was achieved and the Prime Minister had signed the plan, it became law and *directive* targets could be issued to construction and production units.

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The system was known by the Vietnamese as 'two downs and one up'. Indicative targets were sent down to the base units; after the development of detailed plans the units sent these up to the SPC; and in the final stage, the SPC sent directives down again to the enterprises. Each annual plan contained tens of thousands of targets - all calculated by the 800 specialists - which in turn depended on the major targets decided by the SPC as a result of its negotiations with the Party and Government leaders. The power of the SPC, as an institution, derived not only from its control over the available supply of resources, but from its control over these targets. Neither the Prime Minister nor the State Planning Committee itself (the 15 Committee members) had a full grasp of the details of the plan, since they decided only the broad aggregates. Details were known only by the heads of the specialised departments of the SPC and, indeed the finer details of factory by factory allocations were known only to individual specialists. Given the constraints on the autonomy of SPC departments, individual ministries, provinces and production units were nevertheless somewhat dependent on these specialists in their negotiations over resource allocations.

Comment: [TP 11/9]

### Operation of the Planning System

#### *Import dependence*

From the point of view of the planners, the single most important factor hampering implementation of the plan was Vietnam's dependence on imported inputs for its capital construction projects and industrial production. There were two basic problems here: the first

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those that were working would effectively receive more fuel. However, such a decision was a technically punishable offence and the case for making the allocation this way would need to be very carefully justified.

related to the initial negotiations between Vietnam and its trading partners which largely determined the basis of the former's plans; the second related to the actual delivery of supplies.

In the first case difficulties arose because what Vietnam's socialist trading partners could supply depended on their own plans. Vietnam, as an underdeveloped country, basically had to accept what was on offer and this meant that the available supply of imports was often insufficient both in quantitative terms and in the assortment. Vietnamese leaders, in their negotiations with foreign partners, were often offered capital and supplies for construction projects which may not have accorded with their own strategic plans, but which they accepted because 'something is better than nothing'. In the second case, input supply did not follow the stipulations of the plan. Foreign trade partners often did not stick to the agreements they had signed earlier, chiefly because the main suppliers, the USSR, East European countries and China, had the same planning system. In other words, their own outcomes did not correspond to the plans on which they had based their offers to the Vietnamese. As a result supplies either did not arrive, or arrived late or in the wrong assortment. So despite careful calculation, many plans did not correspond to reality:

"At the beginning when we drew up the plan it always looked very nice. But when we implemented it, all the figures began to look less convincing because the iron and steel were still in the USSR and the cement was still in China. Constructions not completed due to lack of material were many."

This could have serious effects on production in Vietnam since it required only one target not to be reached in order for significant downstream impacts to occur. For example, if the plan to import caustic soda was not fulfilled, then Sao Vang Rubber had to switch from producing tyres to inner tubes; paper producers had to increase the amount of poor quality paper, soap producers had to reduce detergent production and increase output of bath soap. These outcomes in turn impacted on, for example, the transport sector, publishers, and mineworkers.

Constraints on imported input and capital supplies also led to an enormous waste and inefficiency in construction projects. In the early 1980s there were some 10,000 construction projects in the plan, including thousands of irrigation schemes. Out of approximately \$500 million spent annually on construction at that time, the majority went on about 20 large scale projects, including the Hoa Binh hydroelectric dam, the three big cement plants (Hoang Thach, Bim Son and Ha Tien) and others. If any of these was allowed to stop, due to lack of capital, cement or steel, the SPC would immediately hear the complaints of the Politbureau. So there was always very little left over for the remaining 10,000 projects - those which did not attract the attention of the political leadership. Irrigation projects financed by the SPC, for example, required an annual expenditure \$50 million, but in fact received only \$20 million. The Ministry of Irrigation therefore decided to choose particular projects and leave the rest in semi-suspension with the result that many construction enterprises were actually only working a few months of the year.

A further implication of Vietnam's import dependence was that longer term planning was effectively impossible. Five year and fifteen year perspective plans were drawn up by the SPC, and indeed the five year plans received the most widespread attention outside Vietnam and played a key role in the Party's political propaganda. Five-year plans were necessarily more aggregative than the annual plans and not intended to be operational in the sense of determining day to day activities of production enterprises. However, the frequent adjustments to annual plans necessitated by inadequate import supplies meant that the longer-term plans had no practical significance. To take possibly the most extreme example of an unfulfilled FYP, the plan for 1976-80 was premised on availability of 5 million tonnes of fuel per annum, of which only 2 million tonnes actually arrived.

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### *Drowning in a Sea of Figures*

Again from the point of view of the planners, a major obstacle to successful planning in Vietnam was the lack of technical resources and skilled personnel. As the economy and society became more sophisticated, the planners found that the number of tasks they had to carry out multiplied in ways which given their limited resources, became impossible to handle.

The Ministry of Forestry, for example, was one of the organs responsible for planning bamboo production. It had a thick book of orders for so many billion bamboo trees to be exploited, how many to supply to companies and how many it could sell to individuals for house construction, etc., at prices fixed by the State Prices Committee for each different class of bamboo tree. The Ministry itself had many branch units engaged in compiling these lists. If a province or enterprise needed bamboo, but there was no order from the SPC, then no one could supply it, as producers who sold bamboo to those who were not permitted to buy it could be punished. But the mountain provinces were also responsible for bamboo exploitation and had the same procedures as the Ministry. The Ministry of Domestic Trade also had a plan for bamboo sales to individuals. It had to make a plan of where to get the bamboo and to whom to sell - which companies and which individuals - based on its total bamboo allocation.

In fact the Ministry of Domestic Trade had to operate with tens of thousands of figures. In the SPC Department for Domestic Trade was a list of all items, from bamboo to paper and meat, provided to the Ministry, including their sources, classifications and prices. For every Ministry there was such a book, of some hundreds of pages, containing the sources of products and to whom they could be distributed, all calculated by the 800 specialists. In the early stages of planning, when only a few hundred factories existed and fewer commodities were controlled, the system seemed manageable, but by the end of the 1970s planners realised they were drowning in a sea of figures.

Moreover, norms tended to multiply. In textile production, for example, the number of fibres per square centimetre was specified, in case shortage of fibre tempted enterprises to meet quantity targets by producing more flimsy cloth. The Ministry of Construction had to incorporate into its housing plan the number of square metres allowed for a balcony in order to ensure enterprises complied with supply norms set by the SPC. Another case arose from the import of a large scale Soviet assembly line for the manufacture of agricultural hoes. In many areas of Vietnam the topsoil was too shallow for the heavy duty hoes produced by the factory, so the localities would buy the hoes, melt them down and set up their own production facilities to produce smaller ones. In 1979 the SPC effectively hobbled the hoe producing enterprise by cutting its steel allocation. In this case, and again in the case of animal fodder processing, numerous new small-scale production facilities had to be set up to replace the old one. But this could not solve the problem, rather it increased the difficulties of planning. It is physically impossible within the plan to specify the exact dimensions of every good produced under the different conditions experienced in every region and, indeed, in every factory. In fact, in order to keep the system within manageable proportions, plan targets have to be given in a fairly aggregative way (tons, metres, etc) and this gives rise to the well known problem of production of goods which are too heavy, too narrow, etc, as enterprises strive to meet output targets with too few raw materials. Trying to strike a balance between the need for aggregative targets to keep the system manageable and the difficulties of controlling the detailed production processes under the highly variable conditions within each enterprise has been a perennial problem for planners in all the socialist countries.

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Another problem was the way in which norms were calculated. Tractors, for example, were allocated to provinces according to their presumed need and fuel was allocated according to norms based on the average level of use. But some provinces underutilised their tractors while others reached above average levels of use. Some provinces consequently received too much fuel and others too little. Before 1978 the use of fuel for the wrong (i.e., unplanned) purpose was prohibited and a punishable offence. However, in practice the provinces made adjustments themselves: fuel provided for agriculture was used for other activities. To calculate the norms in any other way would have meant providing detailed plans of the tasks to be completed by each tractor, an inherently impossible task.

Comment: [TP 11/9]

A basic problem with the system of material balances in all planned economies of the socialist world was the problem of coordination and coherence in the face of the sheer magnitude of the calculation required<sup>6</sup> and the inevitably imperfect information. [Nove 1980: 36, 40] While these problems may have been fewer in a small economy like Vietnam's, compared with the Soviet Union or China, the resources available to the planners to carry them out were similarly smaller. Organisational strategies to ensure coordination and coherence usually involved setting up specialised bodies with responsibility for particular parts of the overall process. However, these could never overcome completely the limitations imposed by information flows and the remoteness of the decision makers from different parts of the economic system.

### Overcoming plan distortions

#### *Plan Adjustment*

The mismatch between the ambitious plans laid down by the leadership and the realities of severely constrained imported resources led to further distortions in both the procedures and implementation of planning. SPC departments responsible for the calculation of construction costs and input supply norms were forced to reduce these norms for individual projects in order to make the plan consistent with production capacity. Then, based on the reduced norms, the Investment Planning Department calculated the capital required and the Construction Department calculated the inputs. Recipients of these distorted plan norms understood that the plan was inconsistent, but had no choice in the matter. In implementing the plan, they had to build according to the real construction norms and the Investment Department had to disburse money according to these norms, not according to the plan. Projects rarely received either enough capital or enough inputs to be completed within the planned time.

At mid-year, therefore, a meeting between the Investment Department, the Construction Department and the Ministry of Finance was held to revise projects and disburse additional capital. There were three basic ways of achieving this:

1. The first was to cut capital and supplies from projects which had no chance of fulfilling the plan and transfer it to those which did. In the end, some projects therefore got the needed amount and some did not.

“Regularly at mid-year we had to re-examine implementation. For these meetings we first had to go to every province to learn the situation. One could not work because it lacked cement, but had iron. Another had cement but no iron. In some cases, managers were very good at getting everything so they not only fulfilled, but overfulfilled the plan and lacked money. So what we did in those meetings was to relieve supply bottlenecks and move cement etc. from place to place. Mid-year was very busy.

<sup>6</sup> Soviet economists were well aware of the absurd proportions of the task. Nove [1980: 53] cites a 1965 article on this: “Kiev mathematicians have calculated that, in order to draft an accurate and fully integrated plan of material-technical supply just for the Ukrainian republic for one year requires the labour of the entire world's population for ten million years.” He adds the comment that “Allowing for colourful exaggeration, the point is rather strikingly made”.

Implementers of all projects also had to go back and forth to the SPC because the SPC had the right to move supplies without consent.<sup>4</sup>

Comment: [LV 19/9]

2. The second method involved the use of the Investment Department's reserve fund. This reserve was actually very large, amounting to 10% of the total annual capital fund and could be used for two main purposes: firstly, to allocate extra capital to viable projects which were short of capital; secondly, to finance new projects which the government decided upon in mid-year. In addition, the head of the Investment department had a tiny discretionary allowance (amounting to some 0.1 percent of the total) to provide provinces with extra capital allocations or supplies. Larger allocations from the reserve fund required a lengthy consultation process with the Ministry of Finance and other ministries which might have a claim, while the Permanent Vice Chairman would have to put a very tightly argued case to the whole SPC before he could make a decision. Since an allocation to one ministry meant a loss to another, such negotiations were full of tension.

Comment: [LV 12/9]

3. The third method was to ask the State Bank to print money to provide projects with the necessary capital. Investments therefore contributed to inflationary pressure.

While the first two methods of plan adjustment described above were part of the very essence of the system of 'material balancing' on which Soviet-style planning methodology was based [Nove 1980], it could not remove the distortions. Material balancing is a system of establishing partial equilibria which makes it possible to adjust some balances without the necessity to re-work the whole set of balanced-relations. The advantage is that it gives flexibility and simplicity when shortages occur, however, the focus on a few key linkages (which, as we have seen above, are likely to be politically determined) in making adjustments means that there may be repercussions on other more 'remote' inputs and outputs which could possibly reach a large magnitude and lead to serious waste of productive resources [Dobb 1968].

### ***Fence-breaking***

Ultimately the more significant method of overcoming plan distortions was the widespread movement to go 'outside' the plan. In periods of crises, especially such as occurred during 1978-81,<sup>7</sup> shortages experienced by production units within the planned sector, and ultimately by consumers, could not be alleviated by the normal plan adjustment method. In this period and increasingly throughout the 1980s fence-breaking proved a far more effective method of overcoming disequilibrium. Fence-breaking can be conceived of as unplanned adjustment by micro-level units to the changes occurring in the plan in the interests of achieving equilibrium in the macro aggregates.

Fence-breaking was thus primarily 'bottom up', but it could also, on occasion, be a 'top down' process. In other words, it occurred at all levels of the hierarchy, often as a result of unilateral actions by production units, but sometimes through a process of negotiation and collusion between groups and individuals at intermediate levels and those at the base and, more rarely, as a result of initiatives taken by persons strategically placed within the Party and Government leadership. What all these activities had in common was firstly, that they broke the basic rule of planning that all economic activity should be controlled from the centre; secondly, they were technically illegal, although as interests changed and recognition of the failures of planning increased they were given formal approbation.

<sup>7</sup> This period coincided with the emergence of a procurement crisis in agriculture followed by increased shortages resulting from the mobilisation of resources in the second half of 1978 for the attack on Pol Pot's regime in Cambodia, the decision in mid-1979 to shift from borrowing from the dollar market (at the rate of about \$600 million a year) to repayment of the debt at something over \$100 million a year, and shortages of industrial inputs when CMEA compelled Vietnam to pay much higher prices for imported goods in 1981 (see below). The result showed up in dramatic falls in industrial output [Beresford 1989].

Among the multitude of examples of fence-breaking activities two basic types can be identified. The first involved direct horizontal contacts between enterprises. These were probably more common in the south, where the market economy was already firmly entrenched, than in the north where the hierarchical relationships of the planned economy were stronger and many enterprise managers would have been unaware of potential customers or suppliers. In the absence of evidence, however, this remains only a hypothesis. The second type involved cooperation and collusion of higher levels, most commonly the local authorities, but in some cases those at the very top of the hierarchy as well. In practice, some degree of passive collusion was probably necessary in all cases due to the illegality of the activities, but in many cases the higher authorities played an active role in assisting enterprises to find trading partners and in encouraging fence-breaking experiments.<sup>8</sup> We have argued elsewhere that fence-breaking activities enabled relatively autonomous capital accumulation [Fforde 1993, Beresford 1995] to increase beyond the limited funds retained by enterprises within the planning system.<sup>9</sup> One aspect of the collusion in fence-breaking mentioned above was that individuals and organisations (e.g. cooperatives) were often able to benefit financially. An example from the 1970s was the way in which local authorities in the southern region colluded with cooperative farmers to take advantage of the difference between fixed prices paid for quota sales and ‘negotiated’ or ‘incentive’ prices for above quota sales. Since this difference was large, for example in 1976 the plan price for paddy was 0.21 dong/kg and the ‘negotiated’ price was 0.7 dong/kg, local authorities often agreed to buy more rice from farmers at the higher price in return for a share of the extra income.

Comment: [TLT 20/9]

One of the key factors in an enterprise’s ability to fulfil its plan, in both the plan adjustment process and in fence-breaking, was the network of contacts and the negotiating skills of both the enterprise manager and the cadre responsible for material supply.<sup>10</sup> Each enterprise had a fund for applications to the SPC or for contacting other suppliers to buy materials. These lobbying functions therefore created the embryo of the ‘black’ funds within the enterprises, not merely for the purpose of corruption, but because they played a positive role in improving the function and efficiency of the factory.<sup>11</sup> Within Vietnam, advisors usually pointed to the frequent lack of technical qualifications, old age or reliance on political connections of enterprise managers as a reason for poor productivity.

†However, a young, highly qualified engineer may work with tied hands if unable to receive funds or materials. A pensioner, on the other hand, who was a provincial Party member or an army officer could be more effective. He could knock on the door of a minister, complain to the provincial People’s Committee, phone his friend who was a high ranking officer in order to borrow a few tractors, or

<sup>8</sup> Such cases had to be carefully disguised, for example, through misreporting of transaction prices or, in the case of some fence-breaking activities which received encouragement from on high, by describing them as ‘experiments’ - implying a temporary and contingent nature - rather than as something which had in fact arisen from economic necessity.

<sup>9</sup> In the planned economy enterprises maintained a production development fund, a bonus fund and a welfare fund which were designated ‘own capital’ of the enterprise. However, expenditure from these funds had to be approved by the superior management level.

<sup>10</sup> Nove [1980: 103] refers to the existence of the ‘tolkach’ in the Soviet Union whose job is to ‘agitate, nag, beg, borrow, sometimes bribe, so that the necessary materials, components and equipment arrive’.

<sup>11</sup> There was a verse for expressing this in different qualities of cigarettes: Sa Pa were the lowest quality and 3 Fives (555) the best. The result of the lobbying effort depended on the quality of the cigarettes offered:

With Sa Pa keep your distance,  
 With Song Cau you can start to deal,  
 With Dien Bien you can become close,  
 With 3 Fives you sign with your eyes shut.

In Vietnam at the time, the quality of cigarettes offered was seen as an indication of the degree of respect.

connect with a friend who was director of a cement factory to ‘borrow’ ten tonnes of cement straight away.”

Comment: [DP 19/9]

In the most successful factories, therefore, the key managerial personnel often had the experience, skills and personal relationships which are easily transferable to a market environment. Efforts to replace these people with engineers, on the other hand, might have had more negative long-term consequences.

A second important feature of enterprise operation in the planned economy was the need for cash transactions. According to the plan, enterprises should be issued with cheques from the State Bank of Vietnam to buy materials from the designated supplier, but because there was not always enough available at the address appointed by the SPC, people had to buy from other suppliers, at different prices and in cash. The supplier itself may have difficulties and need to use cash to buy from others.<sup>12</sup> The problem was the balance between cheque and cash. The need for cash conferred a great deal of power on the SBV which usually took a ‘commission’, usually around 5%, but in some cases as high as 30% of the value of capital allocated to the enterprise. An enterprise allocated 100 million dong by the Ministry of Finance under the plan, might thus only receive 70-95 million in cash, depending perhaps on the degree of dubiousness of the cash requirement. It would use the cash to buy materials and equipment. After that it would sell, say, half of it on the black market to cover the deficit. This was perhaps the most important source of capital for the development of the black market at the time. While the black market was insignificant in the private sector, it was able to expand mainly on the basis of SOEs’ illegal cash requirements. Since both SOEs and the SBV colluded in issuing cash to enterprises, the authorities could rarely track down the responsible bank personnel. Thus one of the key conditions for the transition to a market economy, increased monetisation of transactions within the state sector, was already widespread in Vietnam before 1985.

Comment: [DP 19/9]

A third aspect of fence-breaking activity is its geographical distribution. It would appear to have been far more widespread in the southern region, from 1976 onwards, than in the north. One of the reasons for this may be that local authorities were generally more involved in collusion with farmers and local enterprises than in the north. Fence-breaking, in collusion with local authorities, was certainly not unknown in the north and one source mentioned, for example, that besides the well-known cases of Kim Ngoc, Party Secretary in Vinh Phu province, in the late 1960s and of Doan Duy Thanh in Hai Phong in 1979-80, the province of Nghe An had implemented contracts with households in agriculture by the beginning of the 1970s.<sup>13</sup> Others mentioned fence-breaking by northern SOEs and by individuals at a high level within the SPC. However, such collusion by higher authorities seems to have been more common in the south, with the result that fence-breaking could occur on a grander scale. The most notable case is the Long An experiment, in which the whole province switched to trading at market prices as early as 1980.<sup>14</sup> During the first half of the 1980s, this system spread to most other southern provinces and some in the north as well.

Comment: [LQH 21/9]

Comment: [E.g. PH 23/9]

All of these aspects of fence-breaking activity not only allowed enterprises and cooperatives to overcome to some extent the distortions in the plan, they contributed to the gradual undermining of the planning system. In the longer term, they made the transition to a market economy during the 1980s easier.

Comment: [TP, June 1995]

### ***Policy Responses to Fence-Breaking Initiatives***

<sup>12</sup> See Kornai [1980].

<sup>13</sup> Kerkvliet cites cases in at least eight provinces later in the decade [Kerkvliet 1995: 70].

<sup>14</sup> There was also Nguyen Thi Thi of the Ho Chi Minh City Food Company whose buying at market prices in the early 1980s was eventually hailed as a national model in 1985.

As mentioned above (pp. 6, 8), provinces and ministries frequently made adjustments to their plans on their own, without waiting for a central directive. One of the earliest policy responses to this situation was a minor change in the planning system initiated by the State Planning Committee in 1978. Instead of allocating all capital directly to enterprises, the SPC decided to provide a lump sum to the provinces for small projects. This enabled them legally to choose which projects to give immediate priority and which to leave for the future. In fact this minor decentralisation did not help resolve the problems of administrative planning because some enterprises got the capital, but not the bricks and cement or pumps. Nevertheless, it helped to establish the principle that not everything need be decided by the centre. That this was a difficult enough task was explained by one of the key decision makers:

"I had to explain to everybody that it would not affect the central power, but would be more effective at the lower level. You have to realise that there were thousands of people clinging to the system in order to make a living. In the SPC, for example, there were only ten people in charge of irrigation, but they controlled thousands of projects. Cutting central power meant cutting the power of those ten and they were bound to react."

Comment: [TP 5/9/94]

At the time of this initial reform, small projects still needed to be approved by the SPC, even if discretion in allocation of spending was given to the localities. Later, however, the reform was extended so that projects below a certain expenditure limit no longer required approval. This had an interesting side-effect. In some cases local authorities were able to build large projects by drawing up a budget below the limit requiring SPC approval, even though the real cost was well above the limit. As the ability of some localities to find their own resources increased, this practice became more common, enabling them to decide on construction projects which fell outside the national plan. For the construction of the Hanoi sports stadium by the city authorities, for example, the original cost estimate was for 7 billion dong, a figure below the limit of 10 billion dong requiring SPC approval. However its real cost was later estimated at over 5 times the original budget. As the SPC was unable to prove that the cost over-run was intentional, no penalties could be applied. Such cases indicate that the process of application to SPC to have the project included in the plan was seen as involving high transaction costs (especially in terms of delays and spending on hospitality). Other policy reforms, were also responses by the government to initiatives which were apparently already widespread in practice. Decree 25-CP in January 1981 which formalised the Three Plan system in state-owned industry was one such response. Even before 25-CP many factories had learned how to break fences. For example, a machinery factory might have a plan to produce machines, but lack the right sort of steel, so it would produce bolts for the market. Before 25-CP such practices remained illegal, but since they met a demand, the authorities had to accept the situation. While 25-CP was issued in response to the immediate crisis in input supplies brought about by application of the new CMEA prices, there was already sufficient knowledge and understanding of the role of these fence-breaking activities in helping overcome shortages to make legalisation of some production for the market an obvious solution.

Comment: [TNT 29/9]

Until 1980, Vietnam had obtained special trade conditions from its CMEA partners. The price system of CMEA involved taking the average world market prices for a given commodity over the previous five years and using these for trade within CMEA during the next five years. When Vietnam introduced its First FYP for 1961-65, it therefore received CMEA prices calculated on the basis of world market prices for the period 1956-60. The commencement of US bombing in 1965 led to an agreement with CMEA that these prices, which became known as 'stop prices', would continue for the duration of the war and Vietnam had then managed to negotiate an extension of these 'stop prices' during its post-

war rehabilitation phase in 1976-80. For 1981-85, however, CMEA insisted on adherence to its current prices, based on world market averages for 1976-80. This meant that, for example, a tonne of fuel at Hai Phong port which had cost 39 rubles in 1980 (equal to the cost of transport from the Russian port), rose to 200 rubles in 1981-85 (cf the contemporary world market price of around USD 300). The average price of all Vietnamese imports doubled, while its export prices rose only by 18%. Moreover, exports to CMEA had been only a quarter of imports, even at the stop prices, so the shift to full CMEA prices was a serious blow to Vietnam's economy. Despite an increase in Soviet loans to help cover the increased trade deficit, the amount of imports fell by 30% in 1981. Industries which totally depended on imports were forced to cut production due to the acute input shortage. This was one of the key factors in the introduction of Decree 25-CP, the three-plan system in state-owned industry. By legitimising some of the outside activities of SOEs, and encouraging others to branch out into new areas of production, the measure could help to solve some immediate problems. [Dang Phong 1995] Like other reform measures of this period, 25-CP did not therefore represent a change in ideology of the top leadership, nor was it intended to change the planning system in any fundamental way. It was brought about as a result of the historical conjuncture, the coincidence of interests among enterprises, planners and political leaders in saving industrial production in a period of crisis.

Comment: [TP 11/9];

For many SOE directors, 25-CP made no real difference to their activities. They simply carried on doing what they had already been doing for years.<sup>15</sup> However, from a wider perspective it was a very important development since it legalised what had previously been illegal. This not only enabled earlier fence-breakers to expand their non-directive plan activities, but encouraged hitherto passive enterprise managers to look for new ways of producing. 25-CP thus opened a much bigger hole in the fence than had previously been possible.

Comment: [PH 23/9].

Introduction of output contracts in cooperative agriculture in 1981 (Order no. CT-100) at first only partially resolved the problems caused by the planning system in that sector, largely because the system of official procurement prices remained intact. Many changes had been made to agricultural prices over time in order to improve procurement prospects. During wartime, these were very small adjustments: the initial procurement price of 0.21 dong/kg set in 1956 had risen to only 0.27 dong by 1976. But after unification of the country, price adjustments began to be more frequent and larger. In 1978 the price paid in the north rose to 0.4 dong. It was increased again in 1979 to 0.52 dong and again in 1981 to 2.5 dong. In the Mekong delta the procurement price was 0.21 dong in 1976, rising to 0.32 in 1978, 0.52 in 1979 and 2.5 dong in 1980. But in the 1980s the government was able to procure so little at these fixed prices that it resorted to a system of barter. In the north during 1985-87 1 kg urea exchanged for 2.5 kg paddy, while in the Mekong delta the ratio was 1 kg urea for 3 kg paddy. Nevertheless, the government seldom had enough goods to barter and procurement campaigns became major events combining moral persuasion (with most senior economic ministers and Party leaders touring the countryside to try to convince farmers to contribute) and pressure. Procurement cadres were the meat in the sandwich, under pressure from above to buy paddy at low official prices, they in turn applied pressure to the farmers.<sup>16</sup>

Comment: [TLT 20/9]

Comment: [TP June; DP 20/9]

<sup>15</sup> For example, a former director of the Tran Hung Dao machinery factory in Hanoi described his involvement in barter arrangements with other factories as early as the 1960s, often with assistance from Ministry officials in contacting potential partners.

<sup>16</sup> A report from the Thanh Hoa province, for example, criticised 'fence-breaking' by the lower levels who were seizing household goods when peasants refused to sell at government prices. Occasionally there was retaliation. In one case, villagers confiscated a procurement cadre's own bicycle for failing to provide goods in exchange for paddy, although it was scarcely his fault that he had no goods to supply. In another case a female

As early as 1980 in the south (following a ‘fence-breaking’ experiment by An Giang province in 1979) and 1981 in the north a new system of ‘negotiated’ or ‘agreed’ prices was adopted to purchase above quota amounts. These new prices were in fact determined by the government and not negotiated at all, but they were usually only about ten per cent below the market price and based on a calculation by planners that, since farmers usually sold inferior products to the government, the ‘agreed’ price in fact reflected the real market value of these goods.<sup>17</sup> In 1984 the ‘agreed’ price in the north was 18 dong/kg (compared with the official price of 2.5 dong), whereas the market price was approximately 22 dong. During the same year in the Mekong delta, agreed prices rose from 4.5 dong/kg to 9.5, while market prices rose from 7.5 to 17 dong. Despite frequent adjustments, the gap between official and market prices tended to increase over time. Due to the existence of input shortages, farmers’ inability to cover production costs at fixed prices gave them the incentive to produce for the market, while local authorities diverted scarce state inputs supplied at low official prices onto the market to boost their revenues. Moreover, rising costs of official procurement contributed substantially to the budget deficit as, throughout this period, rice continued to be sold on ration to state employees at 0.4 dong/kg. As noted above, local authorities in the south often colluded with farmers to purchase more rice at the ‘agreed’ prices, pushing up the cost of wage subsidies further. And increasingly, procurement was done at market prices until the procurement system itself was finally abolished in 1988. CT-100 therefore also played a major role in undermining the system of planning.

Comment: [TLT 20/9]

Thus during the decade after 1978, the central planning system gradually lost its power, partly as a result of government initiatives, partly due to increasing market activity by production units. Directive targets began to lose their significance. In 1981 a large number of consumer goods were removed from the ration system and only 9 major items continued to be subject to directive targets. After 1985 the majority of targets were progressively abolished. Since 1988 all agricultural and aquatic products have been traded at market prices and the SPC no longer issued plans to enterprises in these fields. Meanwhile, increasing numbers of inputs also had to be purchased in the market. The final step was in 1989 with the liberalisation of all but a handful of input prices. After that only targets for budget contributions of enterprises were issued by the SPC, but these no longer had legal force. In the market environment, actual budget contributions depended on the profitability or otherwise of the enterprises.

Comment: [TP 11/9]

Comment: [TLT 20/9].

### Why planning failed

#### *The politics of economics*

A distinction between an ‘equilibrium faction’ and a ‘reform faction’ (Shimakura 1982)<sup>18</sup> may be a useful way to look at the attitudes of Vietnamese planners concerning the difficulties they faced. The former group - the ‘equilibriumists’ - essentially accept the ability of planners to achieve an equilibrium growth path and in general they are opposed to high rates of capital construction which pay insufficient attention to the real financial and

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cadre of the State Price Committee doing her washing in a river, was prevented from leaving the water for several hours by village louts gathered on the river bank.

<sup>17</sup> As the government paid for pigs by their liveweight, farmers would feed them several kilos just before the sale. Private buyers, on the other hand, insisted on having the pig killed and the stomach removed before weighing.

<sup>18</sup> Shimakura’s argument was based on the Chinese case where the equilibrium faction was associated particularly with the ideas of Chen Yun. Kalecki, the leading East European advocate of this approach, used the concept of a ‘government decision function’ to describe the way in which planners would reach a compromise between the desire for high growth (meaning a high rate of investment) and the population’s desire to sacrifice investment and growth for the sake of present consumption (Kalecki 1969).

resource capacity of the economy. This tradition in socialist economic theory was actually initiated by the Soviet Industrialisation Debate in the 1920s in which the main protagonists were Bukharin and Shanin (advocating close attention to ‘proportionality’ between sectors or what Kornai termed the ‘harmonic’ approach) and Preobrazhensky and Feldman arguing for forcing the pace of growth through creating deliberate imbalances in favour of capital goods construction.<sup>19</sup>

One cannot say that such an ‘equilibrium faction’ existed in Vietnam. Nevertheless, an ‘equilibriumist’ *approach*, against high rates of capital construction, was implied very strongly in our discussions with Vietnamese planners. The two factors which they most consistently identified as leading to problems in the system were firstly, the over ambitious targets set by the political leadership and, secondly, the inability to fulfil these targets caused by lack of supplies from abroad. They were highly critical of the political leadership of those days for its failure to take sufficiently into account the limitations on growth imposed by existing capacity and their lack of concern with effectiveness of investment projects. Instead, the leaders were said to base their demands on the productive potential of the economy - a tendency which in turn led to the self-criticism at the Vth and VIth Party Congresses of ‘voluntarism’. In some periods, it must be said, the planners do not appear to have made much effort to dissuade the leaders from their more ambitious plans (see note 1 above) and this may be due to the fact that the Chairman of the SPC was normally himself a politician (a member of the Politbureau) and might not have given short-run efficiency criteria the same priority as his more technocratic subordinates.

At other times, however, the leadership of the SPC did challenge many projects and sometimes succeeded in halting new constructions. Moreover, at the Central Committee meeting prior to the Vth Party Congress a fierce debate developed, lasting several weeks, over the question of ‘voluntarism’. Although this lengthy and heated discussion produced only one sentence in the political report to the Congress, the subsequent Third Five Year Plan (1981-85) did reflect a turning point in favour of ‘equilibriumism’. The hugely over-optimistic targets of the Second FYP which had not even been half realised, were replaced by much more realistic targets which did, in fact, come reasonably close to realisation by the end of the period [Beresford 1989]. However, by this time the legacy of earlier ‘voluntarism’ was already strong. Resources continued to be poured into existing large scale projects, and the intended shift in priorities to agriculture, consumer goods and exports could only be very partially realised. In any case, demand for these sorts of goods was increasingly being met by the market.<sup>20</sup>

Clearly then, there was a feeling among the planners and some others that had the plans more realistically reflected the actual capacity of the economy, then the plans would have worked better. Pressure from the top was repeatedly blamed for the distortions in the plan:

Efficiency was not a concern of our leaders. Although we established all kinds of councils to ensure efficiency and they drew up all kinds of coefficients, due to the demands of the leaders the construction program was always under stress and it resulted in distortion of the plan...If the leaders consistently followed the construction norms, they could have stopped the excess of projects, but they would have

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<sup>19</sup> The debate was based on Marx’s reproduction schemes in *Capital* and concerned with the problem of how to achieve the highest possible rate of growth under a system of planned economy. This is the debate about heavy industry versus light industry priority and teleological versus genetic planning. In the 1920s this debate remained very much in the classical Marxist tradition since political economic factors were much in evidence. However, with the rise of Stalin and the Gosplan ‘engineers’, planning became much more a question of manipulating variables and the role of the State was seen as politically neutral.

<sup>20</sup> Throughout the early 1980s, state-run trade controlled only around 40 per cent of retail trade and, as we have seen, much of this was no longer subject to planned quantities and prices [see *Nien Giam Thong Ke*, various issues].

had to be very strong minded people. During my time as head of department there was only one boss strong enough who dared to argue against projects which the leaders greatly admired.

Comment: [LV 12/9]

The question is, then, what drove the leaders to ignore the advice of economic technocrats and persistently push for targets that were too ambitious? If this tendency could have been overcome, would planning have had a chance to succeed? Actually, the answer must be that this tendency could not be overcome and that therefore the persistent shortages and distortions in the plan were a necessary feature of the type of planning system that existed in Vietnam and other socialist countries. This is because the way in which the politicians' perceptions of the national interest were necessarily different from that of the planners. Two factors should be mentioned here.

First is the perception of national interest which, in the post-colonial context of all Southeast Asian countries, contained an overriding emphasis on the idea of 'modernisation' through industrialisation. Large scale modern factories were an important symbol to Southeast Asian nationalists of progress out of backwardness and poverty. Until the end of the 1960s in Southeast Asia, the development of a modern industrial sector based on construction of heavy industries and attempting to replicate the mature industrial structures of the former colonial powers, was universally pursued. Indeed, given the high levels of protection in the West against even semi-processed raw materials and light manufactures from Southeast Asia, this was a sensible strategy for countries pursuing rapid industrialisation. Vietnam, was not influenced by the changes in world market conditions in the 1970s which led to export-oriented industrialisation elsewhere in the region, but remained tied to the CMEA conception that international specialisation should only be based on the prior existence of an advanced industrial economy. Thus there are important historical reasons why the Vietnamese leaders' perceptions of the national interest did not rely on notions of comparative advantage as the basis for development policy.

The long struggle for national unification is another factor influencing the way Vietnamese political leaders view the industrialisation strategy. Given the importance of electricity as a symbol of modernisation, the 500 kv north-south power line is a good example of how nationalist ideology continues to influence planning decisions. This line has been widely criticised as an inefficient use of resources, but, as one former planner put it, the decision to construct the line was partly an expression of sympathy for the south and partly to enhance the prestige of the *national* leadership in an independent-minded region. Another example is the recent decision, against all economic advice, to build an oil refinery in the central region in order to achieve a more even distribution of large-scale, modern projects throughout the country.

Comment: [LV 29/9]

Secondly, there are the shorter-term objectives of the leaders in building and maintaining their political power bases. These may be linked to the personal interest of certain leaders in promoting the welfare of their home provinces, or to the building of wider political alliances through supporting the lobbying efforts of other provincial leaders or Party organisations. This is *not* to suggest that leaders actively sought to promote particularist interests, but that the system relied heavily on personal relations developed through Party connections, provincial origins, etc. The upward flow of information from production units, provinces and ministries would be facilitated by the existence of such connections and undoubtedly led to biases in the decision-making of the leadership. This seems to be a very normal way of making political decisions. It would be rare indeed for politicians to base their decisions on the advice of technocrats alone.

The tension between the ambitious targets of the leadership and the desire of the planners for equilibrium therefore arose from the fact that the state system is not a technocratic planning organ, but a structure which is part of the system of social relations and necessarily reflects

the ideas of powerful groups in society - their understanding of what constitutes the 'national' interest. Moreover, in the existing planned economies there were no criteria of long-term effectiveness other than the decisions of the leadership, since it was not accepted that consumer demand expressed through market choices had a role to play<sup>21</sup> and it was presumed that the Party knew best what society needed. Indeed planning is, *of its essence*, a political process, since it expresses conscious choices made through the political system about the structure of the economy and direction of development. While one can sympathise with the predicament of planners, under pressure from above to allocate severely constrained resources to politically designated tasks, it is clear that the impossibility of achieving an equilibrium growth path was inherent in the planning system itself, that is, its existence as an instrument of 'socialist construction'.

### *Dynamics of shortage*

The second group to which Shimakura referred - the reformists - accepted shortage as an inevitable attribute of the planned economy. The reformist position is that the real problem of the centrally planned economy is precisely the attempt to achieve equilibrium by administrative means. In reality the system has a built in tendency to disequilibrium which cannot be overcome, due to the existence of real conflicts of interest. Kornai, for example, has explained this by the different objectives of planners and local (i.e., in his case enterprise) managers [Kornai 1982]. Once the shortage economy is established, the system of incentives it provides to both managers and planners ensures that the tendency is to exacerbate the disequilibrium rather than overcome it. The existing projects continue to consume resources without adding to the stream of output while unmet demand from wage earners employed in them rises. There is a systematic tendency for enterprises to over-order or hoard goods, to compensate for anticipated shortfalls in supply, and conversely for planners to tighten norms to compensate for the ensuing waste of resources. Ability to overfulfil plans is taken as evidence of the existence of excess capacity and tends to result in increased targets in the next round, although this may only have happened because resources were diverted from elsewhere in the economy thereby worsening the shortages in other enterprises and sectors. ('Model' cooperatives like Dai Phong or enterprises like Duyen Hai engineering, for example, were given privileged access to resources which meant that they effectively could not act as models for the rest to follow.)

In practice, the only way to alleviate shortages is to permit the use of market forces and 'loose' planning norms to allow more local initiative, as has been seen above. Market forces, on the other hand, allow for relatively autonomous capital accumulation 'at the periphery'. This may be private capital, especially in the farm and retail sectors, but is also likely to take the form of a gradual process of 'corporatisation' (i.e., the separation of legal ownership and control) in the state-owned enterprise sector. However, this may threaten the jobs and power of those in the central ministries, the SPC and the Party whose control over resources is reduced, and also leads to the fear that too much reliance on market forces may lead to the structure of the economy being determined by the international markets, as in the colonial period. Hence there is likely to be pressure to return to administrative planning methods and the persistence at the centre of the ideology of planning even in the face of the realisation that it is not working well.

As we have written elsewhere [Beresford & Fforde 1996], a common theme in the economic debates in Vietnam was the need to support the base, to free production units from controls and so enable them to develop their autonomy. This was a fundamentally reformist position, in that it reflected recognition of the inability of administrative allocation to overcome the macroeconomic

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<sup>21</sup> This is not to argue that free market economies can necessarily produce a more socially optimal solution.

disequilibrium. However, from within an environment dominated by traditional ideas of central planning and its inextricable links to the construction of socialism, this need for autonomy may not be so obvious, leading to attempts to recentralise and use measures aimed at improving organisation and production techniques at the microeconomic level to improve the effectiveness of the plan. Thus it is possible that one factor structuring the process of change at the policy level was the relative distance of individuals and institutions from the reality encountered by producers and consumers. One might speculate that the rise in fence-breaking had a profound effect upon the relative appeal to various political forces of administrative planning versus more fundamental economic reform and that, ultimately, it shifted the balance of power and influence towards the reformers.

### **The planning system in Vietnam since 1989: Continuity and Change**

In the planned economy, the SPC was probably the most powerful section of the Vietnamese bureaucracy. Its power came, not so much from its planning function - as we have seen, the plans were seldom truly operational - as from its distributional functions. It was responsible for the allocation between ministries, provinces and enterprises of capital and of imported inputs. Over nearly three decades from the inception of planning to 1987 the average annual quantity of imported technical equipment and raw materials was worth about a billion gold roubles.<sup>22</sup> The majority of this was spent on civil constructions and passed through the SPC system. Moreover, domestic raw materials were also subject to allocation by the planners, although obviously less easily controllable than imports, and even the investment of own capital of enterprises was required to be approved by the SPC. The concept of state ownership, which implied that SOEs were in fact merely workshops belonging to a larger enterprise comprising the whole state sector (Vietnam Inc.), meant that the majority of capital and materials (other than own capital, or materials obtained under the 'Third Plan' after 25-CP) could be moved arbitrarily between enterprises without their consent.

The planning apparatus was among the slowest to change during the whole process of reform. The reasons for this are clearly related, not to the inherent conservatism of the planners, but to the functions of the institution within the centrally planned economy. The SPC's *raison d'être* was as the chief instrument of resource allocation and, as such, the planners were bound to try to make the system work. Fundamental change to the system therefore necessarily came from outside the planning institutions themselves - from the fence-breaking activities of state enterprises and cooperatives and from the organisations responsible for areas most immediately affected by these activities (domestic and foreign trade, agriculture, state-run industry). In China, one of the ways in which reformist leaders could overcome the institutional obstacles posed by the existence of a powerful planning machinery was to set up *ad hoc* bodies to deal with specific areas of reform [Shirk 1993]. It seems that in Vietnam, the establishment of the State Committee for Cooperation and Investment (SCCI) to issue licences for foreign investment may have been one such body, even if the reason given is that foreign investment was not related to the planning function of SPC at the time. SPC could thus only react to changes taking place elsewhere in the economy which were gradually eroding its allocative powers. The abolition of all directive output targets and remaining fixed prices towards the end of the 1980s was but the final step in the erosion of the old planning system.

Since 1989 SPC's function of distributing materials and equipment has disappeared. All inputs are traded at market prices and anybody can, in principle, import them. In fact

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<sup>22</sup> This mostly took the form of highly concessional loans. Most of them have not yet been paid off, partly as a result of the collapse of the Soviet Union (and of the rouble) which has necessitated renegotiation of the value of these loans. Loans from Libya, Algeria and Iraq were repayable in rice and were only repaid some fifteen years after the debts were incurred.

enterprises were given autonomy over production and marketing decisions under Decree 217-HDBT in 1987. After 1990 Vietnam could no longer borrow from the USSR or Eastern Europe and the capital distribution function disappeared as well, although SPC retained extensive powers in coordination of Official Development Assistance (ODA), an area that became increasingly important in the mid-1990s. However, power in the area of capital investment has shifted somewhat towards the banks.<sup>23</sup> In the new market environment, control over macroeconomic aggregates, instead of output targets, has become the main means of economic management. A Treasury Department was established within the Ministry of Finance in 1990 to manage domestic and foreign loans and debt service, and to draw up and control the national budget including revenue collection and expenditure allocation by the government.[Concetti 1991: 8] The Ministry of Finance (MoF) has also been involved in developing new financial instruments, such new tax laws, systems for capital management, audit and accounting systems and measures to exercise control over the banking system. Moreover, in late 1994 a General Department for Investment and Development was established under the wing of MoF with responsibility for financial management of state investment, allocation of budget capital, provision of credit at preferential rates to selected projects and selecting contractors for projects using state capital [VIR 19.12.94]. Relatively speaking, then, the Ministry of Finance and the state banking system became more powerful while the SPC diminished in status. The Chairman of the SPC was no longer automatically a Deputy Prime Minister or Politbureau member and had to some extent lost his position of pre-eminence within the Ministry.<sup>24</sup> The SPC's functions also changed dramatically. By the mid-1990s, in the new environment, it saw its goals as (1) developing indicative plans for long-term socio-economic development; (2) contributing to macroeconomic stabilisation; (3) assisting renovation of the economy. The two most important functions which it performed were: firstly, the construction of perspective plans - including the issuing of a five-year Public Investment Program and plans concerning government borrowing requirements and foreign direct investment needs; secondly, the coordinaton and distribution of ODA. Then, in October 1995, SPC was merged with the SCCI to form the new Ministry for Planning and Investment (MPI) in a move which also gave it a bigger say in the development of foreign direct investment projects. The Budget Law, passed in March 1996, while reaffirming MoF's role in coordination and implementation, gave MPI a clear role in determining the parameters of medium-term fiscal strategy [UNDP 1996: 110].

Comment: [LTBT 29/9]

Comment: [TNT 29/9]

Comment: [TP 11/9]

### ***Administrative Reorganisation in 1995***

The new Ministry for Planning and Investment was created as part of a major government reorganisation in late 1995 (which also included the mergers of the former ministries of Agriculture and Food Industry, Forestry, and Water Resources into a Ministry of Agriculture and Rural Development, and the former ministries of Energy, Heavy and Light Industry into a Ministry of Industry). The functions of MPI were set out in Decree 75-CP of the government and, in summary, related to gathering data on development of the national economy, forecasting trends and suggesting priority areas for development, particularly for

<sup>23</sup> Since undergoing reform in 1990, banks are meant to lend according to commercial criteria, although so far this has proved very difficult, due largely to poor accounting practices of enterprises and, at least in the early 1990s, to a degree of interference from higher levels.

<sup>24</sup> SPC's staff had been reduced by early 1994 to 604 [UNDP 1994], although one source suggested that about two thirds of these should be considered 'underemployed'. The Ministry of Finance, on the other hand, appears to have increased in size, from 488 in early 1992 to 829 in 1994 [Mayo-Smith et al 1992: 35; UNDP 1994].

requirements in foreign investment and ODA, ensuring coordination between ministries and provinces and evaluation of specific project proposals.<sup>25</sup>

These functions, apart from those taken over from the SCCI, reflected the fact that SPC had faced a period of great uncertainty in the first decade of Doi Moi. Given that the new functions are vastly different from the old, it is rather surprising to the outsider that, apart from the addition of several departments related to foreign investment, the departmental structure had scarcely changed.<sup>26</sup> Rather, the reorganisation reflected mainly the government's desire to reduce the complexity and time-consuming nature of project approval which had been a source of common complaints from foreign investors, by centralising the coordination of development resources into a single agency.

The creation of MPI was one step in this direction, but it was nevertheless a step which flew in the face of advice from one of the main sources of advice on economic renovation, the World Bank, which had argued, except in cases involving national security or public safety, for abolishing the approval process altogether and 'letting the market decide' [World Bank 1995: 54-5]. In this context it is worth pointing out that one of the chief problems identified by the World Bank was that the 'rules lay out chiefly the process for applications rather than the criteria by which they will be judged' and that this gave an excessive amount of discretion to government officials [ibid.: 54]. Moreover, because of this, the system of approvals did not serve the government's policy objectives [ibid.: 43]. The argument is scarcely a justification for abolition of planning procedures and approval mechanisms. It does point, however, to a major area which the reform of administrative planning in Vietnam has not yet successfully addressed - the establishment of 'arms length' mechanisms for allocating resources, based on *economic* incentives and penalties, which are more characteristic of, not to mention effective methods of, planning in market economies.

### ***The Planning Bureaucracy's Search for a New Role***

Where previously SPC drew up annual plans which became operational, these, from 1989, became only indicative<sup>27</sup> and, in some instances, were reminiscent of the politicians' voluntarism of the past, in the sense that they consisted largely of what many Vietnamese term 'wish lists'. For example, the annual plan for a capital investment in the mid-1990s was for \$3 billion – around one billion to come from the government, one from domestic sources and one from foreign investors. However, in contrast with 'voluntarism', which enterprises and ministries were obliged to implement, the new 'wish lists' have no such power. In fact most of this capital investment plan was unfunded. The domestic investment potential was certainly there, but local investment showed little relation to plan priorities - one important reason being the relative inability of the state banking system to mobilise popular savings for

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<sup>25</sup> Summary based on an English translation by UNDP.

<sup>26</sup> The Departments of MPI were: (1) Foreign Investment Legislation; (2) Management of FDI projects; (3) Management of EPZs and Industrial Zones; (4) Foreign Direct Investment; (5) General Economic Issues; (6) Foreign Economic Relations; (7) Local and Regional Economic Planning; (8) State Enterprises; (9) Finance and Money; (10) Agriculture and Rural Development; (11) Industry; (12) Trade and Services; (13) Infrastructure; (14) Labour, Cultural and Social Affairs; (15) Scientific, Educational and Environmental Affairs; (16) Relations with Laos and Cambodia; (17) National Defence and Security; (18) Organisation and Personnel; (19) Investment Project Appraisal Office; (20) Procurement Evaluation Office; (21) Ministerial Office; (22) Representative Office in Southern Vietnam. There were also 3 research institutes (Central Institute for Economic Management, Institute for Development Strategy and Economic Research Centre for Southern Vietnam), an Information Centre (which published *Economic Forecasting Review*), a Planning School and, finally the *Vietnam Investment Review* a weekly newspaper taken over from SCCI. The Minister was Do Quoc Sam, former Chairman of SPC.

<sup>27</sup> In addition to the five-year perspective plans, the planning body issues annual Socio-Economic Development Plans in March of each year.

lending to priority projects. Foreign investors and lenders, on the other hand, showed concern for the issues of investment effectiveness and the absorptive capacity of the local economy, including the lack of a clear legal framework. Sectoral planning continued to be dominated by physical output plans which then determined requests for budget allocations. Since the availability of budget resources tended to be determined by the Ministry of Finance (MoF) on the basis of macroeconomic considerations, budget allocations were rarely sufficient to meet the needs of output plans drawn up by MPI. MoF therefore tended to adjust inter-sectoral allocations in 'an atmosphere of haste and tension' [UNDP 1996: 19] prior to submitting them to the National Assembly.

During 1995-96, MPI began to shift the focus of its planning effort to the construction of a public investment program (PIP) for the five-year period to the end of the century. While the first attempt shows a number of flaws, which will be discussed below, the public investment program is a potentially powerful instrument for 'state guidance' in the context of a market economy. Given the rapid increase in revenues achieved since 1993 and successful elimination of excessive budget deficits, the pool of government savings created gave the government a greater capacity to influence the structure of the economy through its own investment effort. Public investment tends to 'crowd in' investment from the enterprise sector as well, thereby assisting to maintain an overall high growth rate.

The restricted capacity to adapt planning methodologies to the new environment is very evident in the PIP document and is a major target of the UNDP-funded public expenditure review carried out during 1995-96 [MPI 1996; UNDP 1996]. Physical norms (output targets, capital construction projects, provision of health and education services according to population, etc) continued to provide the basis for planning of both capital and recurrent expenditure. In the case of capital investment, the PIP appeared to contain many projects for which funding was very uncertain. This leaves the plan open to the danger, firstly, that large numbers of projects would be started which could not be completed within the planned period, creating bottlenecks to growth in related sectors and, secondly, that priorities would be decided, not so much by the Vietnamese government, as by aid donors. If there is a funding shortfall, it may not be so easy to maintain the government's priorities in the face of pressure to build the larger, more prestigious projects. New projects which carry large recurrent expenditure implications, such as schools and health clinics, may be easier to cut back on than more capital-intensive projects which tend to have more flexibility in funding. Linking capital construction priorities to output targets or other highly aggregative norms also means that less attention is paid to cost effectiveness and absorptive capacity (management and other skills, local resources) which can seriously affect the quality of projects.<sup>28</sup>

Despite its coordination function set out in 75-CP, lack of coordination between MPI and other ministries was also apparent in relation to the recurrent expenditure implications of planned investment expenditure. While MPI was responsible for development planning and management of ODA, the Ministry of Finance (MoF) was in charge of the annual budget for recurrent expenditures. Moreover, there was evidently a lack of forward planning of recurrent expenditures by MoF [UNDP 1996: 54]. All public investment programs carry implications for recurrent expenditure. The positive impacts of projects can be dissipated if adequate provision is not made for maintenance and staffing in particular. In the case of new road construction, for example, lack of routine maintenance will both dissipate the initial boost to growth and increase the capital costs of subsequent rehabilitation. Much of the

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<sup>28</sup> The PIP itself suggests that concern for effectiveness of investment is stronger where foreign, rather than domestic, aid and investments are concerned (I will include the relevant quote from the PIP, but I don't have it here).

expense of Vietnam's infrastructure rehabilitation in the 1990s was in fact caused by the previous two decades of lack of maintenance. Moreover, expenditures from the recurrent budget on routine maintenance and on staffing of newly constructed facilities create long-term employment in the areas where they are located and could provide a significant boost to diversification of the rural economy. In practice, provision for operation and maintenance was insufficient to cover costs in virtually all areas except road transport, where the introduction of a transport fee in 1995 provided enough revenue for this purpose.<sup>29</sup> The lack of planning and coordination in this area was therefore a key problem in the process of shifting to a new type of planning.

A basic difficulty for the planning apparatus was the inadequacy of the data on which its plans were based. In the past, when SOEs depended on the SPC for supplies, they were willing to supply information, but in the market environment feedback on their activities became more difficult to obtain, perhaps because enterprises were more concerned to avoid government controls and tax regulations. Furthermore, much non-state sector activity was not yet reported. The volume of imports, for example, was at least approximately known (despite high levels of smuggling), but the SPC did not have data on exports except for those from the state sector; it did not know how much money was spent by tourists or how much foreign exchange was sent from abroad by overseas Vietnamese. Similarly, while the SPC calculated incremental capital-output ratios in order to make forecasts of investment requirements, it lacked the statistical basis to explain Vietnam's low ICOR.

Comment: [TNT 29/9]

Comment: [TNT 29/9]

Another major function of MPI was to advise on the compatibility of foreign investment and other major capital construction projects with its indicative plans. It provided the chairman of the Council on National Project Appraisal whose members also included the Ministry of Finance, Ministry of Science, Technology and Environment, Ministry of Construction, Bank of Investment and Development, Office of the Government and representatives of other interested ministries, departments and provinces.[Concetti 1991: 9] In this council, however, the voice of the MPI was not necessarily more powerful than that of the other ministries. The more important voice may have been the Ministry of Finance which examined the Vietnamese interest in the joint venture, or the Ministries Industry or Rural Development if the project involved those sectors. Provincial authorities also had the opportunity to comment on projects affecting their locality. However, the MPI did have a voice and foreign investors could not lose by having the it favour their project. Therefore most of them found it advisable to seek MPI approval and, in this aspect of negotiation the operations of the MPI continued in much the same way as before. Foreign delegations visiting MPI joined the procession of ministerial officials, province chiefs and Vietnamese joint-venture partners seeking MPI endorsement of their claims.

Comment: [TP 11/9]

Comment: [LDD various dates]

Nevertheless, under these arrangements, the whole process of foreign investment remains in reality as much driven by the supply of investment and the outcome of negotiations between investors and ministries or provinces as by the planning process itself.

In the area of ODA, the MPI retained some power to influence the type of projects which got funded, chiefly through its participation in donor conferences and its powers of project approval. Whereas in the past foreign aid was distributed with little regard to its economic efficiency (for reasons discussed above), the demise of the Soviet Union and emerging reliance on aid from capitalist countries meant that the effectiveness criteria changed. Negotiated aid agreements had greater force than previously, lenders usually required a tightly reasoned project proposal and aid was no longer released as a lump sum, but was disbursed according to the progress of implementation. Foreign aid donors also required a

<sup>29</sup> Compared with only 27% in 1994. About half of all the maintenance expenditure on rural roads was previously covered by 'voluntary contributions' [UNDP 1996: 88].

domestic contribution to the project, so that Vietnamese capacity to absorb aid became an important part of the calculation. At the Donor Conference held in Paris in 1993, \$2.8 billion in loans were promised to Vietnam and at the 1994 Conference \$4.1 billion were committed. However, there were considerable delays in disbursement because many of the project proposals submitted by the Vietnamese were considered inefficient or containing an insufficient domestic contribution, while many of those approved suffered from slow start-up and implementation. Concern about Vietnam's budget deficit, hence continued capacity to repay, also played an important part in the calculations of foreign lenders. Nevertheless, the World Bank reported an accelerated flow of ODA during 1995, suggesting that some of these problems may have been overcome [World Bank 1995: 15]. In other words, the Vietnamese leadership had put itself under the discipline of the international capital market - even if often on concessional terms - which meant that its development direction would inevitably be influenced by the priorities of international capital. Given that foreign aid and investment have formed a rather high proportion of the total investment effort, this influence is likely to have been large.

Comment: [LV 29/9]

However, distribution of ODA also constituted another reason for the continuing procession of lobbyists to the MPI in order to obtain approval for projects favoured by ministries or localities. Potential conflicts of interest were involved here, in that MPI provided consultancy services for ministries and provinces in drawing up development plans. It then had some influence in the decisions on which construction plans would be approved. This suggests that the system created rents for the organisation which had the potential to undermine its own planning functions. If this pattern were replicated in other parts of the administration, then the potential could become quite large. From an 'etatist' point of view, and from the point of view of the Party's stated objective of creating an economic system 'under state guidance', the strategy being pursued in the mid-'90s, of streamlining project evaluation procedures for both FDI and ODA, by reducing the number of agencies and eliminating many of the steps involved, can be seen as aimed at diminishing this potential. A question for further research suggests itself here: what happened to the rents collected - were they invested in ways which benefited the growth of the national economy, or did they follow the 'Philippine model' of being spent on luxury consumer goods or deposited in foreign bank accounts? In other words, what investment opportunities did individuals and organisations with access to capital see? The answer to this question might tell us something about the value of an 'etatist' approach under Vietnamese conditions.<sup>30</sup>

The *stabilisation* functions of the MPI largely involved assisting the maintenance of price stability through the setting of targets for, or outright banning of imports and exports in certain key commodities - fertiliser, steel, oil, cement and rice. The quotas are, however, implemented by the Ministry of Trade which therefore has more effective power in the matter than MPI.

The MPI issued, for example, export quotas for rice in the effort to maintain a low domestic price and maintain high export prices. In previous years, since the domestic cost of production has been well below the world market price, Vietnamese exporters in competition with each other, drove down the price and caused complaints from Thailand. The existence of a quota, however, means that Vietnamese rice producers have not been able to take full advantage of the large price difference between rice in Guangxi province of southern China and the domestic market.<sup>31</sup> Despite reports of large scale smuggling of rice to China,

Comment: [TNT 29/9]

<sup>30</sup> The work in progress by Adam Fforde on the process of capital accumulation and capital market formation should throw light on this.

<sup>31</sup> In 1995 the rice price in Guangxi was said to be 7000 dong/kg while in the Hanoi markets it was only around 3000 dong [Thoi Bao Kinh Te, various issues].

domestic prices had not risen substantially, suggesting that the controls may have had some impact. The main beneficiaries of this policy are undoubtedly the mainly state-owned rice exporting companies who profit from the difference between low farm-gate prices and high world market prices, although it also enables the standard of living of poor urban Vietnamese to be maintained. Since much of the profit is unlikely to be ploughed back into agriculture,<sup>32</sup> the policy may have an adverse impact on long-run productivity increases in rice production, not to mention the farmers' standards of living.

Cement is another commodity which the MPI attempts to stabilise through the use of import quotas. Since most construction occurs during the dry season, seasonal fluctuations in the price of domestic cement can be very large. Local cement producers who have an effective monopoly of the domestic market have reportedly engaged in speculative hoarding and cutting production in the dry season, when demand is high, in order to force up prices.

During one such 'cement fever', in 1995, the SPC agreed with the factories on a cement import quota which was expected to guarantee the profitability of domestic producers while discouraging speculation. Cement imported under the quota system is distributed by the Ministry of Trade. Here again, the stabilisation function of MPI seems most likely to benefit SOEs without allowing international competition to force improvements efficiency.

Comment: [TNT 29/9]

As noted above, the 1996 Budget Law also apparently increased MPI's role in setting the parameters of medium-term fiscal strategy - the size of the deficit, acceptable debt levels and the distribution of expenditure between capital and recurrent categories. Compared with Decree 75-CP, which gave MPI the role of 'monitoring' the major macro aggregates and 'coordinating' with MoF on revenue and expenditure allocations, the Budget Law appears to constitute a further recentralisation of planning powers in MPI. MoF's role was confirmed as operational rather than determining policy. At the time of writing, not enough is known about the way this will operate in practice.

This admittedly not very deep delving into the role of the State Planning Committee since 1989, nevertheless reveals something of the difficulties faced by the formerly very powerful institution in the new environment. The SPC/MPI has struggled to find a new role for itself since the abolition of directive planning, one which would allow it to hold onto its central position in the state apparatus. Above all, the necessity, in a market economy, to subordinate project planning decisions to fiscal management has caused adjustment problems to both MPI and MoF. The inevitable breaking down of the vertical hierarchy of the state apparatus which follows from the replacement of directive planning by a market-oriented economy means that horizontal relations between state institutions become far more significant than previously. In fact if planning is to work effectively in future then coordination between ministries is likely to prove far more important process, and so far the least effective, than the actual design of plans.

While MPI's functions have certainly changed dramatically, there are also clear continuities in the way it operates. The most important of these seems to be the continued use of administrative methods (quotas and approval procedures) to achieve its plan objectives which, as in the past, leads to fence-breaking by enterprises and lower levels. Moreover, the relative inability to apply administrative sanctions, due to the weakness of horizontal coordination between ministries and other economic organs, means not only that the ability to achieve planned objectives is low, but that transactions costs for enterprises are high. In the absence of clear and unambiguous rules governing behaviour, organisations and enterprises wanting project approval must still negotiate with those holding the reins of power, so that

<sup>32</sup> In one case reported to the author, a state-owned oil company was given a rice export quota.

personal networks and, reportedly, corruption play an important role in the success or failure of their applications. In the transition period, the 'arms-length' mechanisms for allocating resources, based on *economic* incentives and penalties, which characterise most market economies (albeit imperfectly), have made only a few inroads, mainly in areas influenced by foreign capital. The other major continuity in Vietnam's planning system is its continued dependence on external resources in the form of FDI and ODA. If the old planning system was unable to significantly increase the domestic contribution to capital accumulation, the new one is no more able to find a way to mobilise domestic resources in order to meet its plan objectives. As one former planning official rather succinctly put it: "The people build houses and ignore the plan".

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