



Munich Personal RePEc Archive

What is in it for the poor? Evidence from fiscal decentralization in Vietnam

Nguyen, Hoang-Phuong

Maxwell School of Citizenship and Public Affairs, Syracuse
University

January 2008

Online at <https://mpra.ub.uni-muenchen.de/9344/>
MPRA Paper No. 9344, posted 28 Jun 2008 04:10 UTC

4

WHAT IS IN IT FOR THE POOR? EVIDENCE FROM FISCAL DECENTRALIZATION IN VIETNAM

Hoang-Phuong Nguyen

Like other developing countries, Vietnam has attempted to push for greater fiscal decentralization in the hope of a more efficient delivery of social services to targeted citizens. The fiscal decentralization initiative is encouraging and merits pursuit, but the present study however, shows that a misstep in the decentralization process can discriminate disproportionately against the poor. Specifically, an increase in the sub-provincial share of the total provincial expenditures is predicted to bring about an appreciable decrease in the lowest-quintile average monthly income. We suggest that the Vietnamese government require provinces to adopt pro-poor allocation norms rather than reclaiming its control over the provincial expenditure assignment. This paper's empirical findings sound a note of considerable caution that other developing countries should exercise in their fiscal decentralization efforts to avoid creating unintended consequences for the poor.

INTRODUCTION

This paper investigates the effects of decentralized public expenditures created by Vietnam's State Budget Law (SBL) in 2002 on poverty alleviation. Fiscal decentralization is the process of endowing sub-national governments with more taxing powers and autonomy in decisions on expenditures. Results of research are still inconclusive regarding the effects

Hoang-Phuong Nguyen is a Ph.D. Candidate at the Center for Policy Research, Syracuse University.

of fiscal decentralization on a country's social and economic development, but almost all developing countries have embarked upon some type of fiscal decentralization initiative (Martinez-Vazquez and McNab 2003). More attention has recently been focused on researching the effects of fiscal decentralization on social outcomes, particularly on poverty alleviation. However, no studies have explored the impact of greater autonomy in expenditure decision-making accorded to Vietnamese provinces on the amelioration of poverty. This paper attempts to fill the current gap in this increasingly growing field.

Since the adoption of the *doi moi*, or renovation, policy in 1986, Vietnam has experienced developments in several socio-economic aspects, including poverty alleviation. The developmental path has included attempts towards greater administrative, economical, and fiscal decentralization. The government of Vietnam passed the SBL in 2002 with great fanfare. Becoming effective in 2004, the law was considered a remarkable development in the process of fiscal decentralization, and, thus, was expected to lead to a better delivery of social services. The 2002 SBL features a new mechanism for expenditure assignments whereby the central government grants provinces autonomy to allocate spending responsibilities to lower-level governments. Given the relative importance of poverty alleviation on Vietnam's national agenda and of expenditure assignment, the intent of this paper is to specifically explore how much the new expenditure assignments under the 2002 SBL have actually helped, or impeded, the country's efforts to reduce poverty (Government of Vietnam (henceforth GVN) 2005, 5; Martinez-Vazquez 2001, 1).¹

Vietnam has enjoyed an encouraging downward trend in general poverty rates by region across Vietnam (See Table 1 and Figure 1). The already-high income inequity in 2002, however, increased by a substantial margin in a majority of provinces in 2004. Such inequity is reason to suspect that fiscal decentralization has indeed exerted a negative impact on the poor. In fact, much literature has noted the possible adverse effect of fiscal decentralization on resource-strapped provinces and districts. For instance, Fritzen (2006, 3) argues that fiscal decentralization will strengthen the resources and discretion of fiscally better-off and densely populated provinces and districts more than those of poorer ones. Therefore, this paper conducts an econometric test of the hypothesis that a higher degree of fiscal decentralization leads to a decrease in the poorest people's monthly income, which is a proxy for poverty.

To that end, this study proceeds as follows. The conceptual background provides working definitions of the key concepts of fiscal decentralization

and poverty. The background section also discusses factors influencing a developing country's adoption of fiscal decentralization initiatives, and briefly reviews the literature on the relationship between fiscal decentralization and poverty reduction in general and specifically in Vietnam. The next section describes the hierarchy of governmental structures and the budget-making process in Vietnam, elaborating why the new SBL-regulated expenditure assignment might benefit the rich more than the poor. In the empirical estimation section, I will develop an econometric model to test the above-mentioned hypothesis and report estimation results. I then discuss the results, analyze possible policy options to address the identified problem, and recommend which policy options the government should undertake. The final section concludes the paper with suggestions for future research.

CONCEPTUAL BACKGROUND

Definitions

Two key notions of fiscal decentralization and poverty need elaboration. First, decentralization as an umbrella term refers to the process of transferring authority and responsibility from the central government to sub-national governmental bodies. As "a core component of decentralization" (Randinelli 1999, 3), fiscal decentralization has been defined in several ways. The paper employs the following definition of fiscal decentralization developed by the United Nations Development Program (UNDP) for analytical purposes: "*Fiscal decentralization . . . constitutes the public finance dimension to decentralization in general, defining how and in what way expenditures and revenues are organized between and across different levels of government in the national polity*" [italics original] (UNDP 2005, 2).

Poverty can be defined in relation to others or according to biological necessities (Sen 1981, 11-17). For econometric estimation, the definition of poverty in the paper is oriented towards the biological approach, using average monthly income. Although income may not be a perfect measure of poverty, income data is more accessible and widely used by researchers.

What Causes Developing Countries to Embrace Fiscal Decentralization?

Developing countries adopt fiscal decentralization for various reasons. First, in a complex world fraught with national territorial disintegration, fiscal decentralization can be seen as an appropriate venue to defuse potential political and social tensions and unrest. This is particularly true of Indonesia, where the high probability of provincial separatism in the

fragile post-Suharto era made sub-provincial governments more favored (White and Smoke 2005, 4).

Second, democratization can also be an important trigger for the general process of decentralization and specifically for fiscal decentralization. The collapse of authoritarian regimes in the Philippines in 1986 and Indonesia in 1997 fueled demand for more local autonomy. Democratization characterized by greater political pluralism and the demise of the dominant-party system was the central force leading to decentralization in Mexico (Díaz-Cayeros 2004, 2).

Third, structural and economic changes could be a catalyst for fiscal decentralization. As noted by White and Smoke (2005), continuous periods of significant economic growth and urbanization create growing pressure on the central government to provide public services in a faster and more efficient fashion via fiscal decentralization. This scenario is helpful to account for Vietnam's adoption of fiscal decentralization initiative culminating in the current SBL. The factors of economic growth and urbanization are present in the case of Vietnam. Growth in Vietnam has been significantly high for more than a decade (See Figure 2). Although Vietnam's annual growth rate has lagged behind that of China, it has been considerably higher than the average for low-income countries and well above the world average. Figure 3 indicates that the percentage of people living in urban areas has steadily increased since 1990, which is another sign of economic development.

Literature Review on Fiscal Decentralization and Poverty

Earlier research focused heavily on the impact of fiscal decentralization on development in general (Bahl 1999; Schroeder 2003), and on aspects of development other than poverty, such as corruption (Arikan 2004; Fisman and Gatti 2002), public service delivery (Bardhan and Mookherjee 2006), and health (Lieberman, Capuno, and Hoang 2005). More research attention has recently been paid to the link between decentralization and poverty. Most studies, however, look into the impact of decentralization on poverty in all three of its forms: political, administrative and fiscal (Braun and Grote 2000; Jütting et al. 2004).²

Scholars in related fields of development and public finance agree that fiscal decentralization and poverty are indeed correlated. They have attempted to come up with a general framework to exactly account for how fiscal decentralization affects poverty. The frameworks presented by Jütting et al. (2004) and Braun and Grote (2000) identify the economic influence of fiscal decentralization on poverty reduction via higher efficiency and bet-

ter targeting. Despite the fact that centrally-provided investment in certain public areas enjoys economies of scale and size, it would be more efficient for lower levels of government to expend the majority of public services. Local governments are expected to be in a better position to identify their local needs (including those of the poor) and to deliver public services accordingly (UNDP 2005, 7). In other words, the efficiency advantage in combating poverty that lower-level governments enjoy relative to higher-level governments comes from the former's local knowledge and relative proximity to the target population – the impoverished.

Efficiency in public expenditures comes not only from better localized knowledge but also from greater accountability and inter-jurisdictional competition. More fiscal decentralization tends to entail a higher degree of accountability. Local governments now become more accountable to higher levels of government and to their local citizens. Greater accountability is more likely to be an incentive for local governments to improve efficiency in delivery of public services. Inter-regional competition might be able to improve efficiency by loosening the grip of local rent-seekers and the corrupt and by promoting government innovations (Shah 2007, 4).

Several reports and papers have examined various aspects of fiscal decentralization in Vietnam (Fritzen 2006; Gao 2000; Malesky 2004; Martinez-Vazquez 2004; Martinez-Vazquez and Gomez 2005; Pham 2006). Still, the study by Rao, Bird and, Litvack (1998) is the only one that examines the effect of fiscal decentralization on poverty. They argue that both general and specific transfers are needed to improve local capacity and to provide safety nets, thus, ameliorating poverty. Further research needs to be done on fiscal decentralization in Vietnam. The paper by Rao, Bird, and Litvack (1998) only looked closely into one aspect of fiscal decentralization, namely, inter-governmental transfers. None of the studies has explored the expenditure assignment implications of the 2002 SBL on poverty reduction, which is the purpose of the current paper.

FISCAL DECENTRALIZATION IN VIETNAM

The government of Vietnam has four levels: the central government and three lower government levels composed of fifty-nine provinces³ and five provincial-level cities⁴ under the direct jurisdiction of the central government, 643 units at the district level, and 10,602 units at the communal level (See Figure 4 for a complete structure). Each level of government has a popularly elected legislative body, the People's Council, and an executive authority, the People's Committee, which is appointed by the People's Council.

The budget-making authority in Vietnam is highly hierarchical and follows a nested or Matruska doll model. On the one hand, budgets at lower levels of government need to be approved by both the People's Council at their level and that at a higher level of government. On the other hand, departments at the communal, district, and provincial levels report their budget vertically to the respective line ministry. All budgets are eventually consolidated in the State Budget. Under the 2002 SBL, the National Assembly of Vietnam (NAV)⁵ approves the estimated and realized state budget. In addition, NAV has legislative power over the state budget's composition and, in particular, the allocations to line ministries, central agencies, cities, and provinces (Article 15). Whereas financing norms used to be established by the Ministry of Finance, they now have to be submitted to the NAV Standing Committee for review.⁶

The process of fiscal decentralization in Vietnam began with the 1990 enactment of the Council of Ministers' Resolution 186/HDBT on Fiscal Decentralization to Local Governments. The resolution was enacted as part of the attempt at renovation. Despite lack of sophistication, it served as a sound foundation for later developments in budget laws and regulations. The resolution specified only central and provincial budget levels. A note-worthy point in expenditure assignment under the resolution is that provincial governments can keep one-hundred percent of the savings from assigned expenditures (Section II, Article 6, Clause a).

The 1996 State Budget Law and its amendments in 1998 demonstrated the considerable strides made by the government in fiscal decentralization. The law explicitly created a four-level budget-making hierarchy encompassing the central, provincial, district, and communal authorities. The law expanded the fiscal responsibilities of provincial government, and set up a stable framework for inter-governmental transfers, whereby provincial revenue shares would be relatively fixed for several years at a time before being renegotiated (Fritzen 2006, 3).

Building onto the 1996 law, the most recent budget document of the 2002 SBL was enacted in 2002 and went in effect in January 2004, which was the beginning of that fiscal year. The nature of expenditure assignment responsibilities that is regulated by the 2002 SBL is quite unique relative to common practice in other developing countries. Previously, like other countries, expenditure responsibilities were clearly defined in law for three sub-national levels of government. As the 2002 SBL regulates, provinces in Vietnam are given a budget envelope and it remains under their purview to assign expenditure responsibilities to sub-provincial governments. The rationale for the change is to allow provinces to adapt to diverse conditions prevalent in their jurisdictions.

Nevertheless, the new well-meaning pattern of expenditure assignment might bring about differential effects on dissimilar groups of population. According to Martinez-Vazquez and Gomez (2005, 356), the expenditure assignment provisions in the 2002 SBL are “vague enough to allow for important geographical variation in sub-provincial assignments of expenditure responsibilities.” In other words, the new SBL-mandated expenditure assignment might make the poor worse off as provincial governments spend more on urban districts where richer citizens overwhelmingly outnumber the poorer, and, consequently, much less on rural districts where a predominant number of poor people live.

This could happen for the two reasons. First, the lack of centrally-determined mandatory spending norms for intra-provincial allocation of funds enables provincial governments to develop their own budget norms.⁷ Martinez-Vazquez and Gomez (2005) note that unlike the per capita-based central budgeting norms,⁸ the provincially-developed norms have retained physical criteria that the central government long abandoned. More importantly, the criteria discriminate in favor of richer districts and locations with larger built-in capacities. The lack of pro-poor intra-provincial budgeting norms might reflect the fact that provincial budget officers need more time to be able to adapt their budgeting norms relevant to the specific poverty circumstances of their territories.

Second, better-educated citizens who live in physically advantaged districts tend to have more immediate access to provincial government officials whose offices are also located in urban districts. They are thus able to exert greater influence or pressure on the officials to tip the expenditure balance in favor of public services that will increase their income. A large majority of poor people who tend to live at a greater distance from provincial government officials find it harder to have their voices heard. As a result, resources spent by provincial governments have much less positive impact on the poorer people’s livelihoods or income. Budgeting norms that do not take into account true local needs render the biggest advancement in the 2002 SBL’s expenditure assignment counter-productive.

EMPIRICAL ESTIMATION

Econometric Model

The following model is an attempt to test the hypothesis that the assignment of provincial expenditures, or the degree of fiscal decentralization in expenditures, adopted by the 2002 SBL has had a differentially unfavorable impact on the poor. To test the hypothesis, the following econometric model is used.

$$Y_{i\tau} = \alpha_0 + \alpha_1 D_{i\tau} + \alpha_2 X_{i\tau} + \alpha_3 \tau + \mu_i + \varepsilon_{i\tau} \quad (1)$$

$Y_{i\tau}$ is the logged average monthly income of the lowest income quintile in province i at time τ ; $D_{i\tau}$ is the degree of fiscal decentralization in public expenditures in province i at time τ . $X_{i\tau}$ is a vector of control variables representing the provincial expenditures and capacity; τ is a dummy variable equal to unity for 2004 and 0 otherwise; α_3 indicates the time trend effect on the change in the dependent variable; μ_i represents provincial unobserved time-invariant characteristics, and $\varepsilon_{i\tau}$ is the error term over time and province.

As indicated earlier, the 2002 SBL accords provinces with greater autonomy to delegate spending obligations to districts and communes. To describe the degree of fiscal decentralization, most cross-country analyses use the sub-national share of the total government expenditure/revenue or of the Gross Domestic Product (GDP), which is taken from the Government Finance Statistics (GFS) of the International Monetary Fund. Although this measurement approach presents three problems,⁹ there is currently no better measure of fiscal decentralization (Ebel and Yilmaz 2003, 103). Following the traditional studies, the degree of fiscal decentralization, D , in expenditures in equation (1) is measured by the ratio of expenditures by the districts and communes in a province to the total provincial spending.

A possible concern about the model's internal validity is the simultaneity between the dependent variable and decentralization. The extent to which expenditures are fiscally decentralized in a province might be driven by how poor it is. However, this is unlikely since budget allocation norms from provinces to districts and communes still rely heavily on physical inputs, such as the number of schools or hospital beds.

Unobserved heterogeneity among provinces, μ_i , might systematically influence the poor's average monthly income, thus producing biased estimates. The most important unobserved, or hard-to-measure, factors that do not change within a district have much to do with efficiency in delivery of social services, especially those targeted at the poor. The following section discusses two important determinants of efficiency in public expenditures.¹⁰

First, the lack of cooperation in budget allocation between provincial governments and line ministries may lead to inefficiency in public expenditures that aim to generally improve social outcomes or to specifically reduce poverty. While line ministries are responsible for the overall financing scheme for the sector, provincial governments allocate budgets for their

entire jurisdiction. Cooperation mechanisms between line ministries and local governments are not even regulated in the 2002 SBL. Article 24 in the SBL about ministerial responsibilities in budgeting process is silent on such a necessary cooperation. That is also true of Articles 25 and 26 regarding responsibilities of provincial People's Councils and Committees in the budgeting process. Martinez-Vazquez (2005, 21) notes that the current legislation does not provide clear guidance on which government body has competence to regulate the delivery of a certain social service, which is obligated to finance the service delivery, and which is to implement it.

Second, whereas outstanding performance in revenue is highly rewarded, all forms of district or communal incentives for improved efficiency in the delivery of social services to the disadvantaged are non-existent. For instance, as a reward for revenue collections, Bo Trach Commune in Quang Binh Province funded a trip to China for forty-four communal officials (Toan 2007). Incentives for local officials to become more efficient are still lacking because no specific legal document has provided transparent efficiency indicators of local government expenditure performance. In other words, the concept of performance budgeting is not incorporated in budgeting allocations at least at the sub-national level, which is understandable given Vietnam's level of development.¹¹

Provincial heterogeneity in the two factors might bias estimation results. Nevertheless, the two aforementioned efficiency-related factors are assumed to remain unchanged, or to change negligibly, within a two-year time frame. Put differently, they are included in the term μ_t . The problem of unobserved time-invariant heterogeneity among provinces can be solved with our panel data by differencing two periods of data. μ_t is then cancelled out.

$$\Delta Y_{it} = \alpha_1 \Delta D_{it} + \alpha_2 \Delta X_{it} + \alpha_3 \Delta \tau_{\tau} + \Delta \varepsilon_{it} \quad (2)$$

Equation (2) will be used for estimation with robust standard errors to address the concern that provinces might have heteroskedastic errors because of the considerable diversity among provinces in Vietnam.

Data Description

The websites of the Vietnamese Ministry of Finance (MOF) and Vietnam General Statistics Office (GSO) supply data for the estimation (See Table 2 for descriptive statistics). The econometric model employs data for 2002 and 2004, when the new SBL first became effective. Although there were sixty-four provinces and cities in Vietnam, the number of observations in the model is only forty. Three provinces were split into six smaller ones

at the beginning of 2004.¹² The other provinces are excluded because of mismatched and missing data between 2002 and 2004.¹³ However, forty provinces are believed to be representative of the entire country of Vietnam as each of the seven regions has at least one province in the datasets.

The dependent variables are the natural log of the lowest-quintile average monthly income measured in thousands of Vietnamese dong (VND).¹⁴ Vietnam Statistical Yearbooks published by GSO report only regional poverty rates and the average monthly income earned by the five income quintiles. They do not publish provincial poverty rates or the average monthly income of those who are under the poverty line. Nevertheless, the lowest average monthly income quintile, the dependent variable in equation (2), is still a good measure of poverty. Following the guidelines advocated by the World Bank, general poverty rates¹⁵ computed by GSO are in fact also based on average monthly income levels (GSO 2006, 608). In 2002, thirty-seven out of forty provinces report the lowest-quintile average monthly income which is smaller than the poverty-line average monthly income. There are thirty such provinces in 2004.¹⁶

The control variables in X_{it} consist of the log of provincial expenditures,¹⁷ provincial capacity indicators and structural characteristics. Capacity indicators are the natural logs of per capita agricultural, industrial (both in billions of VND), and fishing (in metric tons) production. Greater capacity in agriculture, industry, and fisheries is expected to be positively correlated with the livelihood of poor people. Provincial structural variables are the proportion of females and of those who live in rural areas. The percentages of female and rural population in a province are expected to be related negatively and positively, respectively, with the average monthly income of the poor.

Estimation Results

The estimation produces expected results. A higher degree of fiscal decentralization is predicted to lead to a decrease in poor people's income (See Table 3). Specifically, a one-percent increase in the sub-provincial share of the total provincial expenditures, which is a proxy for fiscal decentralization, is expected to result in a 0.39 percent decrease in the lowest-quintile average monthly income. The result is statistically significant at the 95 percent level in both models (standard and robust). Provincial expenditures, industrial production, and agricultural production are both positively correlated with the income of the poor. Specifically, a 1.0 percent increase in provincial expenditures is predicted to lead to a 0.14 percent increase in the lowest-quintile average monthly income. Similarly, the average monthly income

of the poorest is expected to rise by 0.08 or 0.15 percent as a result of a 1.0 increase in agricultural or industrial production respectively. The larger elasticity of the agricultural production relative to that of the industrial production implies that the expansion of agriculture has a greater impact on the poor. This implication is in line with the fact that 80 percent of Vietnam's population are farmers.

The above results correspond with the highly significant effects of the shares of rural and female population. As rural areas have a higher concentration of poor people, a 1.0 percent increase in rural population will have a 0.8 percent decrease in the income of the poorest. The significantly positive coefficient of the percent of female population means that women could be better at fighting against their abject poverty. Finally, the income of the poor is predicted to be 12.74 percent higher in 2004 than that in 2002.

DISCUSSIONS

The estimation result has an important policy implication. Left to their own devices, provinces are expected to allocate funds against the best interest of the poor. Seeking greater fiscal centralization by empowering provinces with expenditure flexibility is not a guarantee of pro-poor resource allocations. Although increased provincial ability to adapt to diversity has some merit, many countries as diverse as Vietnam have managed to work with defined expenditure assignments at all levels of government (Martinez-Vazquez 2005, 20). The government of Vietnam can implement two possible policy options to ensure that the poor benefit from fiscal decentralization initiatives. First, the central government might want to continue bestowing provinces with the authority to allocate budgets among their sub-provincial governments. However, the government would require that the current centrally-adopted pro-poor budgeting norms be embraced in budgetary allocation decisions at the provincial level. Budgeting norms are considered to be pro-poor if budget expenditures are more sensitive to the interests of the poor.¹⁸ To make the option more effective, the central government would need to provide detailed instructions on what criteria are incorporated in the budgeting norms for which areas of social needs. In doing so, provinces with a relatively larger number of impoverished people can benefit more from fiscal decentralization. The second option that the Vietnamese government might want to pursue is reinstating expenditure assignment regulations in the previous SBL that clearly define the expenditure norms of sub-provincial. The norms would be replicated on those currently being employed by the central government.

Under the four criteria of poverty reduction, greater fiscal decentralization, minimum implementation costs, and maximum feasibility, the first option proves to be a dominant choice for the government. Although both options will diminish poverty at a greater scale in poverty-concentrated provinces, the first one is preferable based on the other three criteria. Implementing the second option would run counter to the fiscal decentralization trend that Vietnam has been trying to push forward. Plus, the first option would cost less than the second one because the latter involves amendments to the SBL. It would take more time to amend the law than to issue a Directive, or Circular, to implement the first option. The second option also has possible feasibility problems. The government might have a hard time selling the idea of amending the SBL to the NAV and would face stronger opposition from fiscally decentralized provinces. After being used to allocating funds on their own for a couple of years, provinces would be more resolutely opposed to being deprived of the allocational right by the central government. Though they would not like following certain budgeting norms outlined by the first option, their resistance would be much less fierce relative to the second option.

CONCLUSION

Like other developing countries, Vietnam has made attempts to push for greater fiscal decentralization in the hope of a more efficient delivery of social services to targeted citizens. The fiscal decentralization initiative is encouraging and merits pursuit. However, the finding of this paper might help the Vietnamese government and policy makers to understand how a misstep in the decentralization process can discriminate disproportionately against the poor. Specifically, a 1.0 percent increase in the sub-provincial share of the total provincial expenditures is predicted to bring about a 0.39 percent decrease in the lowest-quintile average monthly income. We suggest that the government require provinces to adopt pro-poor allocation norms rather than reclaiming its control over the provincial expenditure assignment. What warrants future research is the interaction between the assignment of sub-provincial expenditures made by provinces and by line ministries. The effect of fiscal decentralization on corruption among Vietnamese government officials is also a topic worthy of significant research attention.

To conclude, this paper's empirical findings sound a note of considerable caution regarding how fiscal decentralization in developing countries can adversely impact the poor. If they are going to promote the interests of the poor, developing countries should implement fiscal decentralization with great care to avoid the erroneous steps Vietnam has made.

NOTES

- ¹ In addition to local government expenditures on poverty-related social programs, the central government established a nation-wide program called Hunger Eradication and Poverty Alleviation. In 2000, Vietnam also committed itself to the Millennium Development Goals (MDGs), the first of which is eradicating extreme poverty and hunger (GVN 2005, 5). As the first pillar of fiscal decentralization reform, assignment of fiscal responsibilities should be determined first and foremost. As Martinez-Vazquez (2001, 1) puts it, designing other fiscal decentralization pillars, namely, revenue assignment, patterns of inter-governmental transfers, or sub-national borrowing, before expenditure assignment is just like putting the cart before the horse.
- ² In their fiscal decentralization case studies of China, India, Ghana and Egypt, Braun and Grote (2000) found that the process was positively correlated with development.
- ³ The number of provinces in Vietnam has increased by 60% in five sets of provincial divisions since 1990. Malesky (2005, 1) argued that provincial separation came from the gerrymandering strategy adopted by reformists who wanted to free reform-oriented provinces from provinces dominated by the state-owned enterprise sector.
- ⁴ They are Can Tho, Da Nang, Ha Noi, Hai Phong, and Ho Chi Minh City.
- ⁵ The unicameral NAV is elected to a five-year term by popular vote. The current twelfth term has 491 deputies, and the vast majority of them are party members and recommended for election by the Vietnamese Fatherland Front, which is an organization closely affiliated with the Communist Party. NAV convenes its meetings twice a year.
- ⁶ When NAV is not in session, the Standing Committee takes charge on behalf of NAV.
- ⁷ However, the 2002 SBL requires that districts provide all levels of public education, lighting, water supply and sewerage, urban traffic, and other public infrastructure (Article 34, Clause 1d).
- ⁸ Central budgetary expenditure norms are applied for fiscal transfers from the central government to provinces. The norms classify districts and communes into four categories: urban, rural, low mountain, and high mountain regions. Currently, eleven central norms are applied to estimate provincial expenditure needs in education, training, health, administration costs, information and culture, television and radio broadcasts, sports, social protection, national defense and security, economic activities, technology, and science (Martinez-Vazquez and Gomez 2005, 361). The central government has tried to make the budgeting norms for central-provincial transfers as pro-poor as possible. See Note 27 for more discussions.

- ⁹Ebel and Yilmaz (2003, 105) identify the three problems: (a) GFS does not identify the degree of local expenditure autonomy; (b) GFS does not distinguish sources of revenue; and (c) GFS does not indicate what proportion of intergovernmental transfers is categorical (or conditional) vis-à-vis lumpsum.
- ¹⁰This is not to say that other determinants of expenditure efficiency, such as corruption or mis-targeting, are not important. They are not discussed at length because they are less closely related to the 2002 SBL, which is the focus of my analysis. However, I can reasonably assume that levels of corruption and mis-targeting are also consistent over time.
- ¹¹Let us take the United States for instance. Although performance budgeting was first initiated by members of the New York Bureau of Municipal Research in the early 20th century (Williams 2003, 643), it still faces several challenges to completely replace line-item budgeting (Kong 2005, 91). There is considerable disagreement on what should be appropriate measures of improved performance in expenditures: outcomes vs. outputs, long term vs. short term, observable vs. unobservable, and others.
- ¹²Lai Chau was split into the new Lai Chau and Dien Bien, Dak Lak into the new Dak Lak and Dac Nong, and Can Tho into the municipal Can Tho and Hau Giang.
- ¹³The MOF websites give access to only 2004 budgets of forty-nine provinces, whereas it provides access to a similar number of provinces for the fiscal year of 2002. Some provincial budgets were published in 2004 but not in 2002 and vice versa.
- ¹⁴The exchange rate of VND/USD was between 15,050VND/USD and 15,740VND/USD during the period of 2002-2004 (EIU 2005, 48).
- ¹⁵GSO computes two poverty rates (general and food). General poverty rates have a higher cut-off income level than food poverty rates. Whereas the latter further categorize income levels into rural and urban citizens, the former do not.
- ¹⁶The cut-off average monthly incomes for general poverty rates are VND 160,000 and VND 170,000 for 2002 and 2004 respectively. Depending on the exchange rates, one was considered to be poor if he or she earned approximately USD 11 per month in 2002 and 2004.
- ¹⁷Provinces' expenditures come from their local revenue and transfers from the central government.
- ¹⁸The 2003 government decision represents an example of pro-poor budgeting. It requires the use of school-aged children instead of children enrolled in school as a budgeting norm in education transfers. The norm gives a school-aged child in a rural area 1.7 times more money than an urban student (Pham 2006, 17). See DESA (2005) for further discussions on pro-poor budgeting.

REFERENCES

- Arikan, G. Gulsun. 2004. Fiscal Decentralization: A Remedy for Corruption. *International Tax and Public Finance* 11: 175-195.
- Bahl, Roy. 1999. Fiscal Decentralization as Development Policy. *Public Budgeting & Finance* 19: 59-75.
- Bardhan, Pranab, and Dilip Mookherjee. 2006. Decentralisation and Accountability in Infrastructure Delivery in Developing Countries. *Economic Journal* 116: 101-127.
- Braun, Joachim, and Ulrike Grote. 2000. Does Decentralization Serve the Poor? *IMF-Conference on Fiscal Decentralization*. Washington, DC.
- Citizen Participation and Pro-Poor Budgeting*. 2005. New York: United Nations Department of Economic and Social Affairs (DESA).
- Díaz-Cayeros, Alberto. 2004. Decentralization, Democratization, and Federalism in Mexico, in *Dilemmas of Change in Mexican Politics*, ed. Kevin Middlebrook. San Diego: Center for U.S. - Mexican Studies.
- Ebel, Robert, and Serdar Yilmaz. 2003. On the Measurement and Impact of Fiscal Decentralization, in *Public Finance in Developing and Transitional Countries*, ed. Jorge Martinez-Vazquez and James Alm. Cheltenham, UK: Edward Elgar.
- Fisman, Raymond, and Roberta Gatti. 2002. Decentralization and Corruption: Evidence across Countries. *Journal of Public Economics* 83: 325-345.
- Fritzen, Scott. 2006. Probing System Limits: Decentralisation and Local Political Accountability in Vietnam. *Asia-Pacific Journal of Public Administration* 28: 1-24.
- Gao, Govinda. 2000. Fiscal Decentralization in Vietnam: Emerging Issues. *Hitotsubashi Journal of Economics* 41: 163-177.
- Jütting, Johannes et al. 2004. *Decentralization and Poverty in Developing Countries: Exploring the Impact*. Working Paper 236. Paris, France: OECD Development Center.
- Kong, Dongsung. 2005. Performance-Based Budgeting: The U.S. Experience. *Public Organization Review: A Global Journal* 5: 91-107.
- Lieberman, Samuel, Joseph Capuno, and Vu M. Hoang. 2005. Decentralizing Health: Lessons from Indonesia, the Philippines and Vietnam, in *East Asia Decentralizes: Making Local Government Work*, by World Bank. Washington, DC: World Bank.
- Malesky, Edmund. 2004. Leveled Mountains and Broken Fences: Measuring and Analysing de facto Decentralisation in Vietnam. *European Journal of South East Asian Studies* 3: 307-337.
- Malesky, Edmund. 2005. Gerrymandering – Vietnamese Style: The Political Motivations behind the Creation of New Provinces in Vietnam. *Annual Meeting of the Midwest Political Science Association*. Chicago, IL.

- Martinez-Vazquez, Jorge. 2001. *Intergovernmental Fiscal Relations and the Assignment of Expenditure Responsibilities*. Atlanta, GA: Andrew Young School of Policy Studies, Georgia State University.
- Martinez-Vazquez, Jorge. 2005. *Making Fiscal Decentralization Work in Vietnam*. Working Paper. Atlanta, GA: Andrew Young School of Policy Studies, Georgia State University.
- Martinez-Vazquez, Jorge, and Juan Gomez. 2005. Effective Decentralization in Vietnam. *Proceedings of the Annual Conference on Taxation*, 356-361.
- Martinez-Vazquez, Jorge, and Robert McNab. 2003. Fiscal Decentralization and Economic Growth. *World Development* 31: 1597-1661.
- Pham, Huong. 2006. Fiscal Decentralization from Central to Subnational Government in Vietnam. *Seventh Annual Global Development Conference*. St. Petersburg, Russia.
- Rao, Govinda, Richard M. Bird, Jennie I. Litvack. 1998. Fiscal Decentralization and Poverty Alleviation in a Transitional Economy: The Case of Vietnam. *Asian Economic Journal* 12: 353-378.
- Rondinelli, Dennis. 1999. What is Decentralization? in *Decentralization Briefing Notes*, ed. Jennie Litvack and Jessica Seddon. Washington DC: World Bank.
- Schroeder, Larry. 2003. Fiscal Decentralization in Southeast Asia. *Journal of Public Budgeting, Accounting & Financial Management* 15: 385-413.
- Sen, Amartya. 1981. *Poverty and Famine: An Essay on Entitlement and Deprivation*. Oxford: Clarendon Press.
- Shah, Anwar. 2007. Interregional Competition and Federal Cooperation: To Compete or to Cooperate? That's Not the Question, in *Macrofederalism and Local Finances, forthcoming*, ed. Anwar Shah. Washington DC: World Bank.
- State Budget Law of 2002*. 2002. Ha Noi, Vietnam: National Assembly of Vietnam.
- Toan, Minh. 2007. *44 Commune Officials Enjoyed Foreign Trips for their Revenue Collection*. <http://www.tienphongonline.com.vn/Tianyon/Index.aspx?ArticleID=94883&ChannelID=2> (accessed October 20, 2007).
- UNDP Primer: Fiscal Decentralisation and Poverty Reduction*. 2005. http://www.undp.org/governance/docs/DLGUD_Pub_FDPR.pdf (accessed November 30, 2007)
- Viet Nam Achieving the Millenium Development Goals*. 2005. Ha Noi, Vietnam: Government of Vietnam (GVN).
- Vietnam: Country Profile 2005*. 2005. New York: Economist Intelligence Unit (EIU).
- Vietnam Statistical Yearbooks*. 2002-2004. Ha Noi, Vietnam: General Statistics of Vietnam (GSO).

White, Roland, and Paul Smoke. 2005. East Asia Decentralizes, in *East Asia Decentralizes: Making Local Government Work*, by World Bank. Washington DC: World Bank.

Williams, Daniel. 2003. Measuring Government in the Early Twentieth Century.” *Public Administration Review* 63: 643-659.

APPENDICES

Table 1. General Poverty Rates^a (%) by Region

	1995	1996	1999	2002	2004
Red River Delta	29.1	26.6	21.6	22.4	12.1
North East and North West	47.2	45.2	40.6	53.2 ^b	44.0 ^b
North Central Coast	46.9	45.1	40.3	43.9	31.9
South Central Coast	33.9	32.7	28.8	25.2	19.0
Central Highlands	48.6	45.4	40.1	51.8	33.1
North East South	27.6	26.8	20.1	10.6	5.4
Mekong River Delta	31.8	29.1	23.7	23.4	19.5

^a General poverty rates are calculated by determining a cut-off level of average monthly expenditures.

^b Data for North East and North West in 2002 and 2004 are reported by North East and North West separately. Data presented are the averages of the two.

Source: Vietnam Statistical Yearbooks.

Table 2. Descriptive Statistics

Variables	Obs	Mean	Std. Dev.	Min	Max
Log of the Lowest-Quintile Average Monthly Income in 2002	40	4.809	0.203	4.446	5.321
Log of the Lowest-Quintile Average Monthly Income in 2004	40	5.058	0.222	4.605	5.654
Sub-provincial Share of the Total Provincial Expenditures in 2002 (%)	40	35.232	13.063	10.434	60.014
Sub-provincial Share of the Total Provincial Expenditures in 2004 (%)	40	44.493	13.818	8.289	71.289
Log of provincial expenditures in 2002	40	13.662	0.392	12.936	15.309
Log of provincial expenditures in 2004	40	14.182	0.438	13.577	15.816
Log of per capita Agricultural Production in 2002	40	0.448	0.554	-1.114	1.145
Log of per capita Agricultural Production in 2004	40	0.473	0.572	-1.190	1.195
Log of per capita Industrial Production in 2002	40	0.891	0.966	-1.355	3.561
Log of per capita Industrial Production in 2004	40	1.359	0.990	-0.851	4.264
Log of Fishery Production in 2002	40	3.167	1.393	-0.446	5.183
Log of Fishery Production in 2004	40	3.378	1.308	1.009	5.323
Percent of Population who live in Rural Areas in 2002	40	0.789	0.138	0.180	0.939
Percent of Population who live in Rural Areas in 2004	40	0.782	0.139	0.205	0.928
Percent of Female Population in 2002	40	0.509	0.005	0.499	0.522
Percent of Female Population in 2004	40	0.510	0.006	0.497	0.521

Table 3. Estimation Results
Time and District Fixed Effects for 2002-2004

Variables	Coefficients	t-statistics	t-statistics (Robust)
Degree of fiscal decentralization	-0.0039	-2.17**	-1.96**
Log of provincial expenditures	0.1425	3.34***	2.82***
Log of industrial production	0.0820	4.30***	4.26***
Log of agricultural production	0.1458	4.20***	4.19***
Log of fisheries production	-0.0080	-0.63	-0.55
% of rural population	-0.0082	-4.79***	-4.85***
% of female population	0.0836	2.82***	3.06***
Time dummy variable (2004=1)	0.1274	3.37***	3.09***
Intercept	-0.5645	-0.33	-0.35

***p<0.01, **p<0.05

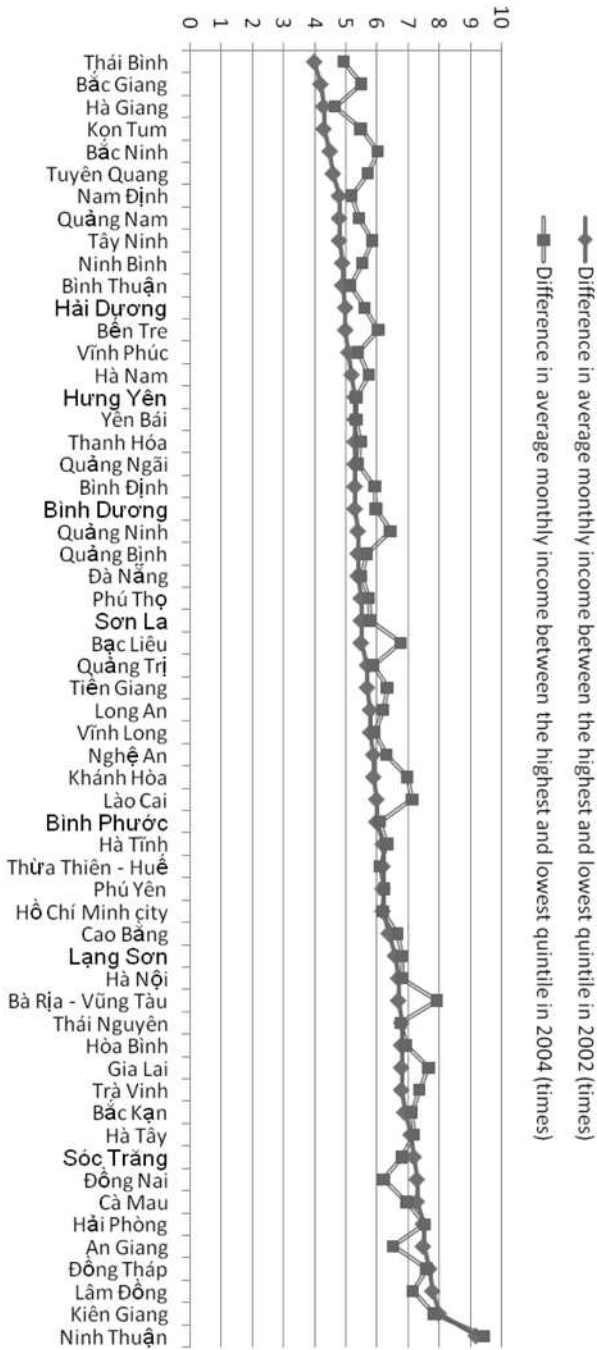


Figure 1. Income inequity in 2002 and 2004 by province

