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 Schmitz, H, *et al*, (2013) Challenging the Investment Climate Paradigm: Governance, Investment and Poverty Reduction in Vietnam
 ESRC End of Award Report, RES-167-25-0443. Swindon: ESRC.



ESRC End of Award Report

This End of Award Report should be completed and submitted using the **grant reference** as the email subject, to reportsofficer@esrc.ac.uk on or before the due date.

Grant Reference	RES-167-25-0443		
Grant Title	Challenging the Investment Climate Paradigm: Governance, Investment and Poverty Reduction in Vietnam		
Grant Start Date	1 October 2010	Total Amount	£ 252,714
Grant End Date	15 February 2013	Expended:	
Grant holding Institution	Institute of Development Studies (IDS)		
Grant Holder	Professor Hubert Schmitz		
Grant Holder's Contact Details	Address	Email	
	Institute of Development Studies, University of Sussex, Brighton BN1 9RE	h.schmitz@ids.ac.uk	
		Telephone 01273-915699	
Co-Investigators (as per project application):	Institution		
Dr Neil McCulloch	IDS; now at Australian Agency for International Development		
Dr Pham Thi Thu Hang and Dau Anh Tuan	Vietnam Chamber of Commerce and Industry (VCCI), Hanoi		
Nguyen Duc Nhat	Development and Policy Research Centre (DEPOCEN), Hanoi; now at VIETSURVEY, Hanoi		
Dr Edmund Malesky	University of California; now at Duke University		

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I. Non-technical summary

Please provide below a project summary written in non-technical language. The summary may be used by us to publicise your work and should explain the aims and findings of the project. *[Max 250 words]*

This project investigates who drives economic reform and which reform components have an impact on private investment. It does this for the case of Vietnam where central government has delegated major economic reform powers to the provinces.

The research shows that in those provinces which are making most progress in economic reform, the private sector played an important role; not against government, but with government. There was no formal public–private coalition but the dynamic was one of proactive government seeking the input from the private sector, and the latter lobbying for and contributing to responsive and effective government. Both national and foreign enterprises played a role but small enterprises tended to be marginalised from the process. Some of the best insights come from comparing provinces and observing how different alignments of interest influenced the reform process.

Quantitative research on the actual impact of economic reform on private investment showed varied results. Reform aimed at improving transparency is strongly associated with higher investment. However, no statistically significant relationship was found between other reform components and private investment. The results have significant implications for policy, given the prevailing assumption that changes in the quality of local economic governance will boost private investment.

2. Project overview

a) Objectives

Please state the aims and objectives of your project as outlined in your proposal to us. *[Max 200 words]*

This project examines two research questions.

1. Does better economic governance lead to more investment or does investment lead to better economic governance?

The project explores whether there is an association between the quality of governance and the level of investment, as well as an association between improvements in governance and increases in investment. Which components of governance are most closely associated with investment and which are irrelevant?

2. Who drives improvements in the quality of economic governance?

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The project examines whether governance reform is driven more by private investors or by public actors. What lessons can be drawn from the political processes in fast improving provinces?

The project suggests a new way of examining these issues by drawing on comparative intra-country evidence and by combining quantitative and qualitative methods. Vietnam has data on investment and the quality of governance, disaggregated by province and component of governance reform, for five consecutive years. The availability of such panel data makes it possible to examine time lags and to disaggregate. Complementary qualitative research methods are used to check the quantitative results and explore political dynamics at work.

b) Project Changes

Please describe any changes made to the original aims and objectives, and confirm that these were agreed with us. Please also detail any changes to the grant holder's institutional affiliation, project staffing or funding. [Max 200 words]

There were no changes to the objectives. Project staffing was also as planned but three collaborators changed employers in the course of the project. Neil McCulloch left IDS-Sussex to work in Indonesia as lead economist for the Australian Agency for International Development; Nguyen Duc Nhat changed from DEPOCEN to VIETSURVEY in Hanoi; and Edmund Malesky changed from the University of California to Duke University. This did not diminish their commitment to this project but it did increase the coordination challenge and affected the speed of completion. We therefore submitted a request for extension to 15 February 2013 – which was granted.

c) Methodology

Please describe the methodology that you employed in the project. Please also note any ethical issues that arose during the course of the work, the effects of this and any action taken. [Max 500 words]

The project used mainly quantitative methods for the first research question, which was concerned with the relevance of reform for investment, and mainly qualitative methods for the second question, which was concerned with the drivers of reform.

The *quantitative analysis* exploited the Vietnam provincial competitiveness index (PCI) which captures the perceptions of investors about economic governance at the province level. This index was available to us for five consecutive years from 2006 to 2010 in a disaggregated form – by province and by component of the investment climate. Both the collection and the processing of the data were carried out to high standards, conducted by the Vietnam Chamber of Commerce and Industry and led by Mr Dau Anh Tuan who was also a member of our research team. The overall design of the PCI and write up of the data was undertaken by our co-investigator Dr Edmund Malesky. In addition to this

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provincial level data on governance, we acquired provincial and firm level data on investment and other variables collected by the General Statistical Office in the context of its annual enterprise surveys. From these sources we built a high quality integrated data set to examine the relevance of reform and its components for private investment. This five-year panel data covering all 63 provinces enabled us to undertake econometric research that took time lags into account. Instrumental variables were identified in order to deal with the problem of endogeneity.

In order to unravel who drives improvements in reform we conducted *qualitative interview-based research* in four provinces, two in the North and two in the South. We picked provinces which made substantial and sustained improvements, since the objective was to identify the contributions of the various actors to the improvement. The bigger the improvements the greater is the chance of identifying these contributions and capturing the political dynamic behind the change. In order to identify factors critical for success and failure we compared the successful provinces with provinces which were less successful.

Comparability is an issue because there are many factors that can influence improvements in governance. Propensity Score Matching helped us to identify provinces with similar endowments. Based on these principles, the final selection of 'our' four provinces was then made using the rankings in the 2010 Provincial Competitiveness Index.

Careful selection of informants in the provinces was important. We sought to hear both the public and private sector and cross-checked information within and across public and private sectors. In each province we talked to roughly similar numbers of government officials and business leaders, conducting a total of 121 interviews. This includes interviews carried out in the capital HaNoi where we cross-checked some of the information received in the provinces.

No ethical issues arose in the course of the empirical research.

d) Project Findings

Please summarise the findings of the project, referring where appropriate to outputs recorded on the ESRC website. Any future research plans should also be identified. *[Max 500 words]*

In line with the original proposal, the quantitative research on the first question has resulted in a paper 'Does better provincial governance boost private investment in Vietnam?' This paper was produced by Neil McCulloch, Edmund Malesky and Nhat Duc Nguyen. It was published as IDS Working Paper 414 in January 2013. It has also been submitted for publication in the refereed journal *Economics of Transition*.

The findings, and their relevance, are as follows: A large literature asserts a causal relationship between the quality of economic governance and economic performance. However, attempts to establish such a link at an aggregate level have met with considerable

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methodological criticism. This paper seeks to overcome this limitation. We match a panel of Vietnamese enterprises from 2006-2010 with a unique panel dataset measuring sub-national economic governance, and then exploit rules on the terms of local leaders and the mandatory retirement age to try to estimate a causal link between local governance and domestic private investment. With one exception, we do not find a significant relationship between most aspects of local economic governance and private investment. The exception is transparency, which is strongly associated with higher investment, although the weakness of our instruments makes it difficult to determine the size of the effect. Our results have significant implications for policy, given the prevailing assumption that changes in the quality of local economic governance will boost private investment.

In line with the original proposal, the qualitative research on the second question has resulted in a report 'Who drives economic reform in Vietnam's provinces?' co-authored by Hubert Schmitz, Dau Anh Tuan, Pham Thi Thu Hang and Neil McCulloch. It was published as IDS Research Report 76 in June 2012 and simultaneously in Vietnamese as Research Report of VCCI, our partner organisation. The essence of this research was written up and submitted to the refereed journal 'Development Policy Review' in December 2012.

Vietnam keeps surprising the world with the speed and depth of its economic transformation. Our research suggests that the decentralisation of certain economic powers from central to provincial government has contributed to this success. Allowing provinces to find their own way forward was central to Vietnam's progress in institutional and economic development. We sought to understand who drives the economic reform in the provinces, exploring the role of business and government and alliances between the two. Provincial government is by necessity involved in the economic reform process but who is actually driving it? The research shows that in those provinces which are making most progress in economic reform, the private sector played an important role. Not against government but with government. There was no formal public-private coalition but the dynamic was one of pro-active government seeking the input from the private sector and the latter lobbying for and contributing to responsive and effective government. Both national and foreign enterprises played a role but small enterprises tended to be marginalised from the process.

e) Contributions to wider ESRC initiatives (eg Research Programmes or Networks)

If your project was part of a wider ESRC initiative, please describe your contributions to the initiative's objectives and activities and note any effect on your project resulting from participation. *[Max. 200 words]*

This was a project within the ESRC-DFID Joint Scheme for Research on International Development. We hope to extend our engagement with that programme by producing a higher level output not foreseen in the application for this project. The findings of the Vietnam study connect in very interesting ways with findings from other research in China, Mexico and Egypt. The purpose would be to produce a paper 'Planners, seekers and the

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investment climate', submit it to a peer-reviewed journal, present it at some of the most influential development agencies and find other ways of reaching policy makers and practitioners. Such a paper could make a big policy impact, questioning the dominant approach to fostering the investment climate. This would however require additional resources. We will consider applying for a small follow-up grant through the ESRC Knowledge Exchange Opportunities Scheme.

3. Early and anticipated impacts

a) Summary of Impacts to date

Please summarise any impacts of the project to date, referring where appropriate to associated outputs recorded on the Research Outcomes System (ROS). This should include both scientific impacts (relevant to the academic community) and economic and societal impacts (relevant to broader society). The impact can be relevant to any organisation, community or individual. *[Max. 400 words]*

Dissemination and Impact in Vietnam

The research results were presented at a large event organised by VCCI in Hanoi on 5 July 2012 to launch the report 'Who drives economic reform in Vietnam's provinces'. The workshop was for policy makers and researchers, including government and provincial officials, industry associations, companies and donors. There were around 250 attendees and the event attracted extensive media coverage. This included 29 press reports/web stories (4 in English and 25 in Vietnamese) and two TV interviews with Hubert Schmitz. Follow up within and outside Vietnam was substantial. A dossier of the event and the responses is available on request. It provides evidence of substantial dissemination and discussion of our research in Vietnamese media and society.

There is also evidence that the research is being discussed in policy and advisory circles. For example, VCCI has received written reactions to our report from provincial policy makers and advisers. The research is also being cited multiple times in the latest Provincial Competitiveness Report. And the findings have been used in the diagnostic workshops offered to provinces seeking to achieve improvements in economic governance.

Dissemination and Impact beyond Vietnam

Attempts to present the results at a meeting of the Donor Committee for Enterprise Development were not successful (due to scheduling issues) but the research findings were presented to the Economics Network of AusAID in Canberra and at a DFID seminar in London on 21 January 2013.

The findings are of most direct relevance to US-AID. This agency, which has been the main funder of the annual PCI report in Vietnam, requested that this year's report cover two new areas. First, they wanted a better understanding on the longitudinal effect of governance on investment, as most PCI analysis has been cross-sectional. Second, they wanted a briefing on work using the PCI data. Our project fits both of these requests. It is

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the most rigorous panel analysis of governance improvements on investment decisions using PCI data. We suspect it is the most rigorous analysis done in any developing country as very few countries have annual data on governance and an enterprise census.

Dissemination to the academic community has started and will continue at conferences and workshops in Vietnam and internationally.

Central to the dissemination is free access and downloads of our papers and reports on the following webpages of IDS and partner organisations.

<http://www.ids.ac.uk/files/dmfile/Rr76.pdf>

<http://www.ids.ac.uk/files/dmfile/RsRr76.pdf>

<http://www.ids.ac.uk/files/dmfile/Wp414.pdf>

<http://img.vcci.com.vn/Images/Uploaded/Share/2012/07/26/ec1Dong-luc-thuc-day-cai-cach-KT-VN-out.pdf>

http://www.vbis.vn/vbis/index.php?option=com_content&view=article&id=67%3A-phong-thng-mi-va-cong-nghip-vit-nam-gii-thiu-bao-cao-nghien-cu-ng-lc-ci-cach-kinh-t-ti-cac-tnh-vit-nam&catid=1&Itemid=6&lang=vi

http://www.pcvietnam.org/articles_detail.php?article=74

<http://vietsurvey.vn/images/Wp414.pdf>

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2196392

b) Anticipated/Potential Future Impacts

Please outline any anticipated or potential impacts (scientific or economic and societal) that you believe your project might have in future. *[Max. 200 words]*

The project is likely to have a lasting impact partly because it was designed and carried out jointly with our partner organisation, the Vietnam Chamber of Commerce and Industry. VCCI is an influential organisation with strong connections to business, government and the Communist Party and the potential to affect policy processes.

Our Vietnamese collaborators also seek to influence debates among researchers. In the course of 2013 Nguyen Duc Nhat (now at Vietsurvey) will present the quantitative research on drivers of investment at a workshop hosted by FTU University in Hanoi and at the Vietnam Economist Annual Meeting in Hue. Dr Pham Thi Thu Hang will present the qualitative research on drivers of reform at a workshop 'Institutional Voids during State Re-Scaling', organised by the International Institute for Asian Studies (IIAS) in the Netherlands.

The project also sought to build capacity. While difficult to measure, we believe substantial capacity building has been achieved through collaborating intensely with Vietnamese colleagues in all stages of the research – from project design to publishing. There was mutual capacity building in that the UK researchers have learnt a great deal from the Vietnamese colleagues. The benefits are expected to show in future projects.

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You will be asked to complete an ESRC Impact Report 12 months after the end date of your award. The Impact Report will ask for details of any impacts that have arisen since the completion of the End of Award Report.

4. Declarations

Please ensure that sections A, B and C below are completed and signed by the appropriate individuals. The End of Award Report will not be accepted unless all sections are signed. Please note hard copies are **not** required; electronic signatures are accepted and should be used.

A: To be completed by Grant Holder

Please read the following statements. Tick **one** statement under ii) and iii), then sign with an electronic signature at the end of the section (this should be an image of your actual signature).

i) The Project

This Report is an accurate overview of the project, its findings and impacts. All co-investigators named in the proposal to ESRC or appointed subsequently have seen and approved the Report.	<input checked="" type="checkbox"/>
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ii) Submissions to the Research Outcomes System (ROS)

Output and impact information has been submitted to the Research Outcomes System. Details of any future outputs and impacts will be submitted as soon as they become available.	<input checked="" type="checkbox"/>
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or

This grant has not yet produced any outputs or impacts. Details of any future outputs and impacts will be submitted to the Research Outcomes System as soon as they become available.	<input type="checkbox"/>
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iii) Submission of Data

Data arising from this grant have been offered for deposit with the UK Data Service.	<input checked="" type="checkbox"/>
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or

Data that were anticipated in the grant proposal have not been produced and the UK Data Service has been notified.	<input type="checkbox"/>
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or

No datasets were proposed or produced from this grant.	<input type="checkbox"/>
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