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VIETNAM: RURAL SERVICE PROVISION A TRANSITIONAL ECONOMY

**Thematic Paper Prepared to Inform the
Preparation of the Vietnam Rural Development
Strategy**

Hanoi
December 2008

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DISCLAIMER

The analysis of this paper represents the views of the authors and does not necessarily represent the official position of IPSARD, MARD or SNV

EXECUTIVE SUMMARY

This paper is one of a series of thematic papers aimed at informing the preparation of the Rural Development Strategy (RDS), and is prepared by independent consultants under direction of the MARD Institute of Policy and Strategy for Agriculture and Rural Development (IPSARD), and with financial support provided by the Netherlands Development Agency (SNV). It is formulated as a policy guidance paper and aims to produce a set of strong, succinct and clear arguments for policy changes relating to rural service provision, based on analysis of international experience and the rapidly evolving socio-economic, institutional and regulatory context for rural service provision in Vietnam.

All types of knowledge, infrastructure and supply services are in principle of relevance for the preparation of the RDS. However, this paper's analysis, conclusions and recommendations are mainly focus on production-related services and infrastructure, i.e. it does not include analysis of basic social services. The paper reviews in detail the cases of agricultural extension, financial services and rural water supply and sanitation.

The paper's analysis is structured around the following key dimensions of rural service provision:

- 1) **Organizing demand – the clients of services:** This is the local level, where formal or informal organizations support representation of farmers, selection and quality control of services.
- 2) **Responding to the demand – service suppliers:** Actors at this level are responsible for service management and delivery, and should be capable of responding to the diverse needs of service clients.
- 3) **Organizing the response – governance and macro-coordination of service provision:** This dimension is responsible for adjustment and renewal of policy and strategy as required to create an enabling environment for service provision, efficient and adaptive functioning of service suppliers and effective coordination between service agencies at all levels.

There is large variation in how individual countries respond to the challenge of delivering rural services in the context of the rapidly changing national and global environments. A review of international literature reveals that many developed, developing and transitioning countries in this context of change are questioning the efficiency and impact of the classical model of publicly funded/publicly provided extension service and are moving towards a broader and more pluralistic extension system, where new service providers from civil society and the business sector are increasingly engaging in service provision, along with traditional public actors. International experience suggests that reform of rural service delivery need to simultaneously consider policy, structural and process changes at all the three dimensions of rural service provision defined above.

On the basis of its analysis of the current challenges facing rural production and development in Vietnam and current systems for rural service delivery, the paper concludes that there is a widening gap between the desired performance of rural service systems, given the current challenges facing rural production in Vietnam and the objectives set for the sector, and the actual performance of these service systems. The paper therefore suggests that the following shift in the fundamental paradigm underpinning rural service provision in Vietnam is required:

A new paradigm for rural service provision in Vietnam

In order to ensure that rural services effectively support national objectives in the context of the current diversification of rural service needs in Vietnam, application of a **new service provision paradigm** that perceives farmers and rural enterprises alike as "entrepreneurs", and promotes the emergence of a demand-oriented and decentralized service market for service provision, is required. As this shift would require a fundamental re-orientation of current service delivery systems, and a careful approach to analysis, piloting and mainstreaming of this new approach should be applied.

In this context, consideration of the following vision for rural service provision reform is recommended:

Vision for rural service provision in Vietnam

The coverage, types of services and delivery modes of rural service provision in Vietnam meets the needs of increasingly diversified rural producers and stakeholders, ranging from poor ethnic subsistence farmers to large commercial agro-enterprises, and effectively support

the following objectives for service delivery, based on national socio-economic priorities:

- **Poverty alleviation and livelihood security:** Poor and ethnic minority producers in remote areas have access to relevant services that allow them to make informed livelihood and production choices based on their specific livelihood situation and production capacities, and effectively contribute towards elimination of hunger and poverty.
- **Food security:** Rural services enable farmers to meet domestic demands for food securing through production of staple food commodities
- **Product diversification and value-adding:** Rural services enable market-exposed farmers and companies to diversify and commercialize their production, enhance efficiency in all production phases, and enhance processing and value added of produce in consideration of their market access.
- **Competitiveness:** Rural services treat farmers as entrepreneurs and facilitate adaptation by farmers and agro-businesses to a more competitive and fluctuating business environment in domestic and export markets.
- **Sustainable production:** Rural services enable producers to protect the rural environment.

In order to enhance efficiency, demand-orientation and market-focus, rural services are 1) delivered in accordance with diversified delivery strategies geared to meet the service needs of increasingly diversified service constituencies, 2) delivered by multiple public and private service providers to enable competition and efficiency in service provision, and 3) paid for by rural producers, with special targeting and subsidies limited to the extent possible and linked to the demand side rather than the supply side. National policies and institutions effectively enable required reform of existing public systems, promote entry and operation of non-state service providers, and empower rural producers through collective action and organization at local levels.

Furthermore, the following critical policy initiatives for effective rural service provision are recommended for consideration by the Rural Development Strategy:

Enhancing efficiencies - Critical policy initiatives for reform of rural service provision in Vietnam

Initiatives for an enabling policy and institutional environment

- *Systemic service policy analysis* aimed at linking rural service objectives to the wider socio-economic objectives for rural development and production in the context of the socio-economic transformation of rural Vietnam
- Development of *diversified service provision strategies* catering to the needs of the increasingly diverse rural producer constituencies in Vietnam
- *Horizontal and vertical coordination and integration* of rural service delivery planning into mainstream SEDP planning to facilitate adoption of a "systems approach" to rural service provision that ensures that service provision in an integrated fashion caters to service needs related to all phases of the rural production cycle.
- *Application of the principles of Vietnam's public administrative reform and decentralization process* to rural service provision in order to separate governance from management and funding from delivery.
- *Monitoring focus on performance management and service impact*

Initiatives for enhanced relevance and coverage of services, and competence and coordination of service providers:

- *Decentralization of service provision*, including planning, content determination and finance management
- *Demand-responsiveness, flexibility and focus on production efficiency in the context of diversified service strategies* as required to respond to the need for farmers and companies to quickly adapt to rapidly fluctuating market conditions, and to enhance the efficiency of service and infrastructure investments
- *Separating service delivery from funding of services* by enhancing the control of rural producers over service funds and by allocating public funds to semi-state and private service providers
- *Limiting the use of subsidies and targeting modalities and where subsidies are justified link these to the demand side* rather than the supply side to enhance delivery efficiency and impact
- *Promoting entry and operation of multiple and diverse service providers*

Initiatives for articulation of demand by rural producers:

- *Empowerment and organization of rural producers* to take a leading role in articulation of service needs, payment for services and selection of service providers.

In order to ensure that rural service provision reform is firmly embedded in the policy and institutional reality of Vietnam, and embraced by all key stakeholders to rural service provision, it is recommended that reform of rural service provision in the context of the Rural Development Strategy should apply the following reform principles.

Principles for reform of rural service provision in Vietnam in the context of the RDS**Content principles – reform must:**

- Be based on the policy and institutional reality of Vietnam while simultaneously taking into consideration international learning and experience. An incremental approach to reform, where consensus is sought for new policy initiatives, and reform initiatives are tested before mainstreamed, is therefore required.
- Take its starting point in systemic analysis of reform needs in light of prevailing socio-economic priorities, and on this basis establish a widely agreed joint vision and strategic directions for rural service provision. Given the dynamic and interrelated nature of the three dimensions of service provision (enabling environment, supply systems and demand articulation), it is important that they are analyzed and addressed simultaneously and in a systemic fashion to enable coherent and sustainable reform.
- Consider the wider issues of governance and public administrative reform, as these impacts the efficiency of service providing agencies, public as well as semi-state and private.
- Reflect that reform needs vary between different types of services, constituencies and commodities.
- Allocate clear roles and responsibilities of different stakeholders based on analysis of their respective comparative advantages (e.g. public providers should remain in areas where they have comparative advantages but leave the floor to others in other areas).

Process principles – reform must:

- Be clear on strategic directions but at the same time take an incrementally approach to reform, i.e. not addressing too many reform initiatives simultaneously, and initially focusing on easy-wins and win-wins.
- Ensure appropriate institutional consultation for reform that includes all relevant public and non-state stakeholders to rural service provision.
- Ensure that reform agents are in place at all three levels of service delivery, i.e. the policy, supply system and demand articulation level. Inputs from reform agents at all three levels is required as it is rarely possible for decision-makers at the top of public service provision systems to gauge the diverse needs of farmers and critically assess the flaws in traditional service delivery systems, particularly at times of significant transformation.

The paper finally recommends the following **immediate reform initiatives to promote rural service reform in the context of the RDS:**

- 1) *Preparation of the diversified service provision strategies for different rural service constituencies recommended above*, as required to provide a basis for the steps proposed in the following. These strategies must build on systemic analysis of the three core dimensions of service delivery, analysis of the underlying causes of poverty and production inefficiencies in Vietnam, analysis of international experience, and analysis of the experiences of piloting of demand-driven, participatory service approaches in the context of Vietnam.
- 2) *Implementation of facilitated multi-stakeholder consultation processes* to agree on vision, overall strategic direction and action planning for rural service provision in the context of the diversified rural service provision strategies. Such consultation should be conducted throughout the preparation of the strategies.
- 3) *Testing of the diversified rural service provision strategies in selected provinces* where the composition of local service stakeholders and production conditions are representative in the context of each of the diversified service strategies.

ABBREVIATIONS

Action Aid	Action Aid Vietnam (INGO)
ADB	Asian Development Bank
CARE	CARE International in Vietnam
CERWASS	National Center for Rural Water Supply and Sanitation
GDP	Gross Domestic Product
GoV	Government of Vietnam
GRET	Research and Technological Exchange Group (INGO)
GSO	General Statistical Office of GoV
GTZ	Deutsche Gesellschaft für Technische Zusammenarbeit (German Development Agency)
INGO	International Non-Governmental Organizations
IPM	Integrated Pest Management
IPSARD	MARD Institute of Policy and Strategy for Agriculture and Rural Development
ISG	MARD International Cooperation Group
NAEC	National Agricultural Extension Center of MARD
NIPMP	National IPM Program
NTP I & II	National Target Program for RWSS, Phase I and II
MARD	Ministry of Agriculture and Rural Development
MoET	Ministry of Education and Training
MoH	Ministry of Health
MPI	Ministry of Planning and Investment
O&M	Operation and maintenance
Oxfam	Oxfam Vietnam (INGO)
P 135 I & II	Program 135 for Poverty Reduction and Hunger Eradication in Disadvantaged Communes, Phase I and II
PPD	Plant Protection Department of MARD
PPSD	Provincial Plant Protection Sub-Department
PCF	People's Credit Funds
RDS	Rural Development Strategy of Vietnam
RWSS	Rural Water Supply and Sanitation
SEDP	Socio-economic Development Plan of Vietnam
SNV	Netherlands Development Agency
SO	MARD Standing Office of the NTP-RWSS II
SOE	State-owned Enterprise
TAG	ISG Technical Ad-hoc Group
UNDP	United Nations Development Program
USD	United States Dollar
VBSP	Vietnam Bank for Social Policy
VECO	VECO Vietnam (INGO)
VNLHSS	Vietnam Livelihood Security Survey
VUSTA	Vietnam Union of Science and Technology Associations
WTO	World Trade Organization

1. INTRODUCTION

1.1. Context: Preparation of the Vietnam Rural Development Strategy

Since the introduction of the economic liberalization of “Doi Moi” in the late ‘80s, Vietnam has experienced rapid socio-economic transformation, and expects to reach middle-income status by 2010. This transformation has radically changed the make-up of livelihoods and production in rural areas, and the conditions under which rural producers operate. Furthermore, due to the economic liberalization, ongoing decentralization efforts and the public administrative reform process, the functions performed by the state, localities, state-owned enterprises and private sector agents are also changing, with localities and private sector agents taking on increasingly important roles and the central Government increasingly focusing on macro-level management of rural production and service sectors. The changes experienced by rural producers are compounded by the recent accession of Vietnam to the World Trade Organization (WTO).

With the overall aim to establish a coherent policy framework for addressing the challenges evolving from these developments, the Ministry of Agriculture and Rural Development (MARD) is in the process of preparing the Vietnam Rural Development Strategy (RDS) up to 2020.

This paper is one of a series of thematic papers aimed at informing the preparation of the RDS. The issuing of this series is part of the effort of the Technical Ad-hoc Group (TAG) established by the MARD International Support Group (ISG) to solicit international support towards the preparation of the RDS. The papers are prepared by independent consultants under direction of the MARD Institute of Policy and Strategy for Agriculture and Rural Development (IPSARD), and with financial support provided by the Netherlands Development Agency (SNV).

This paper is formulated as a policy guidance paper. It aims to produce a set of strong, succinct and clear arguments for policy changes relating to rural service provision, based on analysis of international experience and the rapidly evolving socio-economic, institutional and regulatory context for rural service provision in Vietnam. On this basis, the paper defines at a limited number of strategic and yet implementable policy recommendations for consideration by the RDS. Specific emphasis is put on analyzing rural service provision in the context of Vietnam’s rapid transition towards a market-based economy, as this transformation affects the service needs experienced by rural producers, and consequently poses significant challenges to adjustment of the institutional mechanisms for service provision, as well as the type of services provided.

Following the definition of “rural service provision” applied by this paper (section 1.2), the paper presents emerging international experience and trends with regard to rural service provision, and on this basis defines a set of critical dimensions to be observed as part of reform of rural service delivery systems (section 2). The overall context for rural service provision in Vietnam is then presented in section 3, followed in section 4 by analysis of the characteristics of rural service provision in Vietnam. Section 5 includes a crosscutting analysis of service provision gaps and critical issues for strengthened rural service provision in Vietnam, while finally in section 6 key policy implications and recommendations for consideration by the Rural Development Strategy are presented. In-depth analysis of service provision in the context of three illustrative service cases (agricultural extension, rural financing, and rural water supply and sanitation) is provided in Annex A.

1.2. Defining “rural service provision”

Rural populations depend on a wide range of production and livelihood related services, including *basic social services* (such as education and health), *production services* related to agriculture, forestry and other rural production sectors (such as input supply, extension, land management, financing, processing, market information and trade), and *rural infrastructure* needed to support life and production in rural areas (such as water supply and irrigation, power and roads).

All types of knowledge, infrastructure and supply services are in principle of relevance for the preparation of the RDS. However, this paper’s analysis, conclusions and recommendations will mainly focus on production-related services and infrastructure, i.e. not specifically include analysis of basic social services¹. The principal **users** of rural services as defined by this paper in principle

¹ The rationale for selecting the three service area cases for more in-depth analysis are:

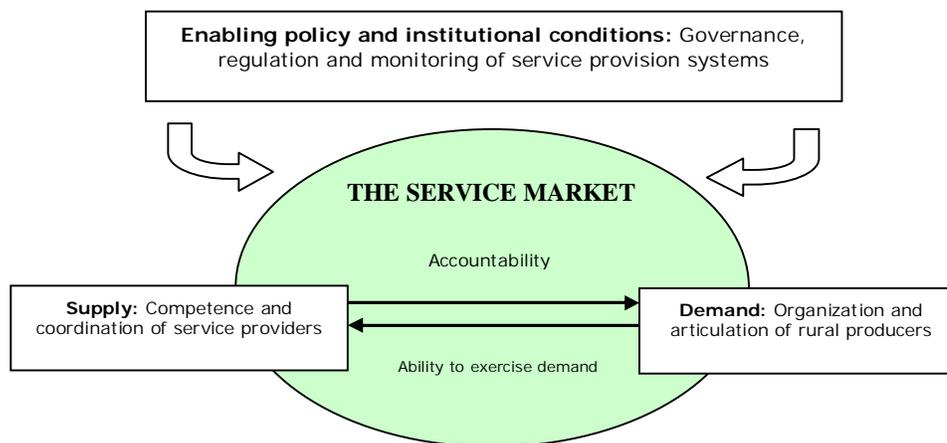
- **Agricultural extension** and related services, such as business development, and information and training. This knowledge-focused service area is selected due to its critical importance for improving productivity, income, marketing, food security, economic and social participation and investment of rural populations.

include all rural constituencies, such as individuals and families, household level producers, cooperatives, cooperative groups and commercial production enterprises, state-owned as well as privately owned. Service **providers** include public agents at the central and local levels, farmers' associations, NGOs, and public and private commercial service providers.

Rural service provision includes the following **key dimensions**²:

- 4) **Organizing demand – the clients of services:** This is the local level, where formal or informal organizations support representation of farmers, selection and quality control of services.
- 5) **Responding to the demand – service suppliers:** Actors at this level are responsible for service management and delivery, and should be capable of responding to the diverse needs of service clients.
- 6) **Organizing the response – governance and macro-coordination of service provision:** This dimension is responsible for adjustment and renewal of policy and strategy as required to create an enabling environment for service provision, efficient and adaptive functioning of service suppliers and effective coordination between service agencies at all levels.

The three dimensions of rural service provision may be illustrated as follows:



Rural service provision finally comprise the following main **types of client-provider relationships**³:

- **Open services**, such as public services where a third party pays for the services (i.e. where the Government treasury or a donor agency pay the service provider to render the service)
- **Closed services**, such as private services where the client pays the service provider directly.
- **Embedded services**, e.g. where services are provided by a commercial agro-business company as part of a business transaction (e.g. by a seed or fertilizer company).
- **Substitute services**, where services are provided directly from a project to beneficiaries⁴.

2. GLOBAL TRENDS IN RURAL SERVICE PROVISION: THE EMERGENCE OF PLURALISTIC SERVICE MARKETS

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- **Financial services**, including all main sources of financing for rural production, such as financing from formal banking institutions, micro-financing and informal financing from traders and middlemen. This service area is selected due to its vital importance for rural production.
 - **Rural water supply and sanitation.** This service area bridges provision of infrastructure and knowledge services and is critical for maintaining the social well-being of rural populations.

² Builds on the Rural Service System Framework presented by Juergen Hagmann and Mathias Braun in GTZ 2007, pp 18-21

³ GTZ 2007, pp 5-6.

⁴ In open relationships, there is an inherent risk that the service provider seeks to satisfy the priorities of the financier rather than the client, thereby making this relationship less efficient from a demand point of view. The most efficient and sustainable client-provider relationship is therefore typically the closed relationship, where client and demand orientation is ensured by the fact that clients, i.e. farmers, order and pay the services directly from the service provider. A key advantage of embedded services is their cost efficiency (the network of dealers exists already), but the commercial bias of dealers puts a limit to their value of their advisory services - they are efficient in rendering information services but can neither create innovations nor systematically train clients. Substitute services are inherently unsustainable.

There is large variation in how individual countries respond to the challenge of delivering rural services as resolving and capturing opportunities for rural poverty reduction and agricultural growth is becoming more complex in the context of rapidly changing national and global environments⁵. These global changes include market liberalization and integration of national and global markets in the context of globalization, commercialization and industrialization of rural production, climate change and migration to urban centers, scaling back the role of the state to core regulatory functions in many countries, and decentralization of government structures. In this changing and more unpredictable environment, rural producers not only have to be technically skilled, they also increasingly need to become good business managers and market operators.

A review of the literature of international rural service provision practices reveals that many developed, developing and transitioning countries, in order to address this broader range factors influencing success and failure of rural producers, are questioning the efficiency and impact of the classical model of publicly funded/publicly provided extension service. These countries therefore are moving towards a broader extension system, where new service providers from civil society and the business sector are increasingly engaging in service provision, along with traditional public actors. In this context, rural service provision is seen as a market place, where alignment between demand and supply, and hence efficiency, is achieved through the provision of services by multiple and more diverse service providers, who enter and withdraw from the service market place depending on their respective comparative advantages with regard to the quality, relevance and delivery of their services. Maintaining an effective service market requires that service demanders are capable of articulating their needs and selecting superior services. Service provision frameworks and strategies therefore cannot be prescriptive and universal, but must be demand-oriented, flexible and adaptable to fit increasingly diverse client demands, local realities, and external impact from global markets.

Implementation experience from these participative and pluralistic efforts has varied greatly in different countries, and it is apparent that successful reorientation of rural service delivery requires major policy, structural and process changes. These changes are summarized in Box 2.1 to 2.3.

Box 2.1:

International Best Practice for National Governance and Coordination of Rural Service Delivery

- **Separating governance from management and implementation - changing role of state agencies to become policy coordinators and market-overseers:** Establishment of an effective service market implies a fundamental shift in the role played by sector ministries and technical departments from a direct implementing role to a role as national “market-overseers”, i.e. assuring service coordination, client coverage, quality assurance and performance/impact monitoring of service provision systems. They also must strengthen their ability to regulate the operations of state as well as non-state service providers, and to work in partnership with client organizations and non-state service providers.
- **Vertical and horizontal integration of service delivery into macro-economic priorities and planning:** Not only sector policies for rural production but also generic policies for trade, private enterprise, infrastructure, poverty reduction, social organization and organization of general service sectors need to be reviewed and aligned to achieve demand-driven, responsive and financially sound service provision that effectively support macro-level policies for rural development. Socio-economic plans and legal frameworks therefore need to be reviewed to ensure that they effectively support integration, reflect the changed roles of service providers and allow new non-state actors to operate effectively. From a policy perspective services funded by state budgets should be targeted toward achievement of key government outcomes, i.e. focusing on social welfare, research and market management rather than provision.
- **Harmonization and alignment of donor support:** International support to the establishment of demand-driven pluralistic systems for rural service delivery should be provided in line with the Paris Declaration on Aid Effectiveness.
- **Monitoring and evaluation of the performance and impact of rural service delivery systems:** The challenges associated with establishment of effective and sustainable management information and M&E systems for complex service systems are significant and therefore needs to be established as integral parts of the design of service systems.

⁵ Unless otherwise stated, the analysis in this section builds on GTZ 2007, pp 7-13 and ADB 2004 pp. 7-11.

Box 2.2:**International Best Practice for Service Provision Responses – Organizing the Supply**

- **Qualifying new service providers:** Service clients' articulation of demand and their control over payments for services facilitates quick emergence of a more pluralistic service market, as service providers then have to compete, market their services, deliver quality and adapt to changing demands to satisfy their clients. Pluralism of agriculture extension service provision also leads to a large increase in the number of extension service providers, and to a higher proportion of service providers being located close to target beneficiaries. However, emerging service markets are often not able to meet all types of service demands efficiently, services may be of inferior standard, and there may be gaps in service coverage. Systematic efforts to enhance the qualifications of new service providers or re-training from existing public monopoly providers are therefore required. Such support in addition to technical and extension capacity building support should include business development support, such as support to certification and entry into the service market. Embedded services can be supported too along similar lines. A basic criterion for enhancing the qualifications of providers is that their skills must reflect the capacities of different client constituencies.
- **Decentralized decision-making, management and coordination:** As a matter of principle, delegation of decision-making relating to service delivery to lower administrative levels (subsidiarity) is desirable, as local agents are better informed about local service priorities and needs than agents far removed from the local context. Fund management and allocation is also more efficient if done by agents at the decentralized level.
- **Separating funding from delivery:** The common practice of budget transfer to and within rural service delivery departments leads to a centralized process whereby government agencies decide what services to deliver, where to deliver and who the beneficiaries would be. This diminishes client ownership and perceived value of extension. To ensure that service provision is independent of Government influence, open-ended funding of services from a range of sources is therefore required. Services should therefore primarily be financed by producer organizations, business sector agents or service clients themselves, except from provision of subsidies for poor and disadvantaged farming households without a sustainable market potential.
- **Private sector access to public funds for service delivery:** Separation of funding from delivery must be accompanied by policies that allow private access to public funds for extension service delivery to encourage pluralism or socialization of service delivery through mobilization of multiple public and private service providers. This must be supported by systematic efforts to enhance the qualifications of the new suppliers and the coverage of their services.
- **Private sector contributions to costs of service delivery:** Private sector access to public funds encourages private sector agents to contribute towards the cost of service delivery. The resulting socialization of service delivery and mutual leverage of public and private sector funds have in many countries led to an increase in total funding for services. Contributions to funding of services by the private sector furthermore encourages development of commercial services for commercial farmers on a user-pays basis.
- **Application of cost sharing and "user-pays" principles:** An interesting phenomenon has been the willingness of even poor farmers to contribute to the costs of service delivery when they perceive the individual benefits are real. Application "user-pays" principles ensure higher efficiency as service clients select only those services they need and from which they can expect maximum return on their investment. Direct payment by clients also ensures that clients hold providers accountable for the timeliness and quality of services, and facilitates farmer organization, as farmers with common interests are encouraged to form groups to share costs and manage service delivery inputs.
- **Recognize that poor farmers are poorly serviced and need special attention:** Service delivery often cater to resource-strong farmer constituencies, and separate mechanisms therefore need to be put in place to meet the specific needs of resource-poor and otherwise disadvantaged farmers for services that are low cost, low risk and of lower technical complexity. Increasing contributions from mainstream farmers towards the cost of rural services allows governments to redirect more of the public sector budget towards poor farmers. Public subsidies and specialized delivery mechanisms may therefore be warranted for resource-poor farmers with little potential for commercial production and barriers for cost-efficient service delivery by private service providers. Generally, the degree to which clients are required to share the costs of services should depend on the monetary benefits they gain through the service.

- **Recognize that the business aspect of rural production is poorly covered and need special attention:** Service systems should not only focus on primary producers but also include agribusiness and some mechanisms to focus on industry development as such, e.g. supply and value chains etc.

Box 2.3:

International Best Practice for Organizing the Articulation of Demand by Rural Service Clients

- **Control over funds by rural producers:** Rural producers are empowered as clients if they gain control over service funds as this enhances the accountability of service providers to their clients rather than to external funding providers.
- **Qualified service demands by rural producers:** To be efficient, rural service systems must treat rural producers as clients, and their demands must be the starting point for service delivery. Formal and informal producer organizations are effective means to ensure that clients analyze and prioritize their demands in a qualified manner, realistically consider service costs, and collectively organize service delivery and share costs. Reliance on such organizations also constitutes a cost-effective means to reaching large numbers of individual producers and businesses. Neutral facilitation of group formation is critical for success in this context.

3. SOCIO-ECONOMIC TRANSFORMATION OF RURAL VIETNAM: CONTEXT AND TRENDS

3.1. Macro-economic transformation of Vietnam's rural production and livelihood setting

Rural production sectors, including crops, livestock, forestry, aquaculture and fisheries are of critical importance for Vietnam's national economy and poverty alleviation efforts, accounting for 22% of GDP, 30% of exports and 60% of employment. In spite of low global commodity prices, the sector over the past 5 years has maintained a growth rate of more than 4% annually, and the export revenue of agriculture products has increased from USD 2,563 million in 2000 to USD 7,200 million in 2007. Agricultural diversification is pursued both by farmers and the GoV in response to market forces, and continued improvements in rural infrastructure contribute to competitiveness and welfare. Rural poverty levels have therefore fallen with impressive speed, from 66% in 1993 to 21% in 2004. These achievements are largely attributable to initial policy reforms in the 1990s, including de-collectivization and introduction of market-based incentives through commodity trade liberalization.

The Government's general objective for rural production sectors is to focus on commodity production which is diverse, efficient, competitive, sustainable and meets domestic and export demands for food and industrial inputs, provides jobs and eliminates hunger and poverty. However, to meet these objectives, sustain past achievements, and further accelerate rural development and poverty reduction, a number of challenges need to be addressed in the coming years⁶:

- At 6% of total public expenditure, public spending on agriculture remains low compared to other Asian transition countries, but higher than low-income countries in general. However, the proportion of budgets going towards subsidized inputs and services compared to technology innovation is high, which limits efficiencies. Rural productivity is therefore stagnating.
- Obstacles remain for market-responsive diversification of rural production due to stagnating agricultural investments (1999-2002) and structural barriers to the entry of private national and foreign enterprises in production, processing and marketing, caused in part by the predominant position of state agents and subsidized state-owned enterprises. This hampers technological innovation and efforts to enhance levels of product processing and product quality.
- Environmental challenges are increasing due to unsustainable patterns of resource use, access and control, and rural areas and production therefore experience increasing threats from land degradation, food and health hazards and water scarcity. Livelihood insecurity and production disruption is further compounded by increasing frequency and velocity of natural hazards. Global warming is also posing challenges in the form of a need to adapt to new production systems.

⁶ Builds on World Bank 2005 pp. 1-4.

- Public administrative reform has progressed slowly compared to the increasing market orientation of rural producers and the decentralization process (the share of non-central government spending in agriculture increased from 43% to 79% between 1998 and 2002). Central agencies are yet to fully adapt to this significant change and their new roles of mainly focusing on sector coordination, fiscal management and performance monitoring of provinces.

3.2. Trends in the make-up of rural producer constituencies – and their service demands

Vietnam is largely an agricultural country. In 2007, rural population accounted for about 79% of the total population, equivalent to 61 million people or about 15 millions households. As illustrated in Box 3.1, clients for rural and agricultural services are very diverse with regard to ethnicity, farm size, farming practices, market exposure, resource base and access to capital, infrastructure and other production inputs, and this diversity is increasing due to the current macro-level socio-economic trends discussed in section 3.1.

Box 3.1: Profile of rural producers in Vietnam

Rural Sectors	# of Units	Main livelihoods
Small farm holders	9,780,000	Paddy rice, vegetable, animal husbandry, cash crops, etc.
Large farm holders	116,222	Animal husbandry, industrial crops, aquaculture and forests.
Ethnic minority households	2,600,000	Upland farming, forests and animal husbandry
Rural Poor households	3,900,000	Paddy rice, vegetable, animal husbandry
Cooperatives	7,677	Agriculture, aquaculture, rural services
Rural enterprises	2,399	Agriculture and aquaculture processing, rural services and input supplies

Source: estimated from GSO statistics in 2006 and 2007

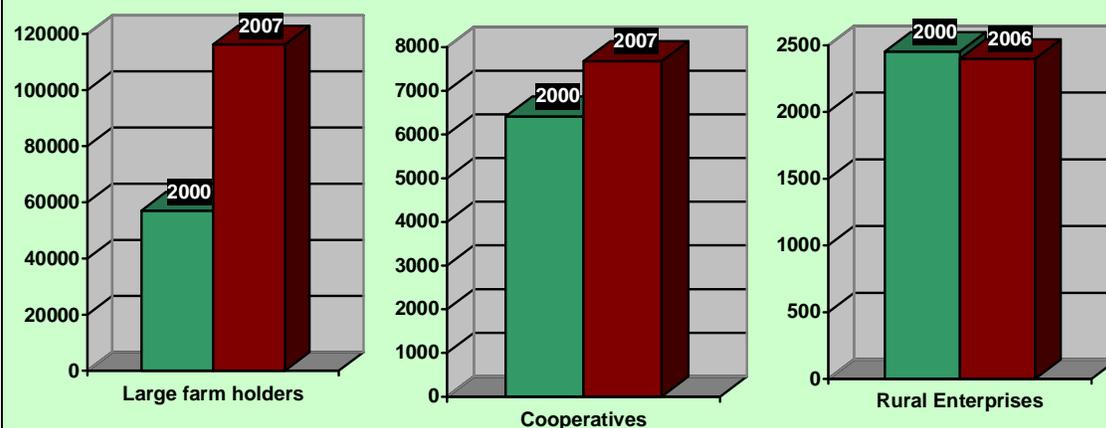
Over the last decade, some noticeable trends in the make-up and service needs of rural producer constituencies have emerged. Rural service provision needs to take these trends into account:

- The total number of agricultural households decreased by almost 7% from 2001 to 2006 while **the number of large farms has nearly doubled** from 57,000 in 2000 to 116,000 in 2007. Almost 75% of the large farms are concentrated in the Red River Delta, the Southwest and the Mekong River Delta, with the Mekong River Delta alone accounting for 47% of these farms. This trend towards increasing farm size will accelerate and suggests that more professional and responsive services are needed to serve this emerging group of producers.
- The number of poor households has reduced sharply due to the economic growth. However, in spite of the strong links between rural growth and poverty reduction, rural population groups have not benefited equally from the achievements over the past years, and disparities are likely to increase with increasing exposure to global market forces. **The poverty incidence among ethnic minorities is twice as high as in the rural population as a whole** (69% against 36% in 2002), and poverty reduction among ethnic minorities is slowing. The vulnerability of upland farming is increasing, and the exposure of ethnic minorities to markets is marginal, but increasing. This suggests a continued need for provision of services geared to rural households engaged in subsistence farming.
- The total **number of enterprises in agriculture, forestry and aquaculture has declined** due to a reduction in the number of aquaculture enterprises as shown in Box 3.2. This suggests that either rural enterprises are consolidating into fewer but larger entities, or that barriers exist to the establishment and operation of private enterprises, such as barriers caused by monopoly positions by SOEs, insufficient training of rural entrepreneurs, etc. The increasing number of cooperatives however suggests an increasing number of farmers use this option to meet their need for a collective, organized framework for production and market entry. According to the GSO, the rural service sector accounts for only 1.7% of the total revenue of agriculture. The **capacity of the agricultural service industry** is therefore not sufficient to meet the new and increasing demands of commercial rural producers and enterprises.
- The agricultural sector has increasingly integrated into global market. Both large farm and small farm holders are now to a great extent influenced by the global competition. In reality, **farmers are now more vulnerable to world prices and market forces**, and this has major implications for production related decision-making. There is therefore an increasing need for flexible and demand-responsive services that enable farmers to cope under ever-

changing market conditions, changing production patterns, competition from imported produce, price fluctuations for export commodities and production inputs such as fertilizers and pesticides, etc.

- World food prices have increased sharply in the past years, which cause **concern about food security**, especially in the context of paddy field conversion to non-agricultural purposes. Services that enable efficient production of stable food commodities therefore remain important.
- Due to increasing production fluctuations and insecurities caused by increasingly **severe and frequent natural calamities**, new types of economic risk management services, such as production insurance and similar services will increasingly be required.

Box 3.2: Number of Large Farms, Cooperatives and Rural Enterprises



4. PROVISION OF RURAL SERVICES IN VIETNAM: CURRENT MECHANISMS AND APPROACHES

The main characteristics of service provision systems in Vietnam are summarized in Box 4.1 to 4.3.

Box 4.1:

National Context for Governance and Coordination of Rural Service Delivery in Vietnam

- Delivery of rural services and infrastructure largely remain a public domain in Vietnam. Overall state management, regulation, planning and finance allocation for rural service provision remains the responsibility of central functional departments and related centers, typically organized under the Ministry of Agriculture and Rural Development, and with departments in other ministries providing complementary inputs towards state management and planning.
- This includes overall management and regulation pertaining to services and infrastructure in most rural sub-sectors (including crop production, plant protection, animal husbandry, fishery, and forestry), and covering all key types of production related services and infrastructure, including provision of physical production inputs, extension, veterinary services, processing, marketing, irrigation and water supply infrastructure, etc. State management and regulatory responsibilities related to other types of services, such as land management and provision of financial services are located in other Ministries and central financial institutions.
- Despite frequent calls for a more predominant role for non-state actors, legal frameworks and incentives for their engagement are yet to be developed for most extension service and infrastructure areas.

- Funding of rural service provision is mainly public, and channeled either through the provincial and local level line agencies of relevant central functional departments and centers, or through specialized National Programs, such as the National Target Program for Rural Water Supply and Sanitation and Program 135 for Socio-economic Development in Disadvantaged Communes and Villages. The level of funding of services from provincial governments is increasing, resulting significant variation between the proportions of funding allocated from the central Government, provinces and national programs in different localities.

Box 4.2:

Main Characteristics of Rural Service Provision Systems in Vietnam

- In spite of the ongoing decentralization efforts, central agencies maintain responsibilities for the **definition of the technical content and range of services** offered by their line agencies at the provincial and district levels (e.g. demonstration models and training), as well as technology options offered for rural infrastructure.
- **Extension services** are almost exclusively delivered by the district offices of central level agencies, such as the National Agricultural Extension Center (NAEC), and plant protection and veterinary authorities. The main service delivery modalities applied are centrally defined demonstration models and formal farmer training, which are implemented according to national cost norms, though in some cases more participatory extension approaches are applied (such as the Farmer Field School approach applied in the context of plant protection services). Participating farmers receive incentives in the form of input supply and attendance monies. Coverage in remote ethnic minority areas is limited due to tight operational budgets. Semi-state agents such as commodity-focused research institutes, unions and associations and centers also provide extension services, which are often funded in part by NAEC or provincial budgets, and applying similar implementation modalities. Aside from information provided as part of sale of production inputs, private traders and companies play a limited role in extension, but their exposure to clients in this context is probably significant. Generally, as mainstream extension services are largely provided by public providers and semi-public providers dependent on public financing, farmers' choice with regard to extension is in real terms fairly restricted.
- In most provinces, state-owned **input supply** companies maintain a dominant position in the supply of physical production inputs such as seeds, fertilizers and pesticides. However, the role played by such companies varies between different provinces, commodities and production sub-sectors, with private companies providing inputs and services on a more competitive basis in some provinces and sub-sectors. Collectors buying produce from farmers are often connected to input distributors, and collectively offer farmers credit to buy inputs that subsequently is deducted in the income generated from the sale of produce. **Processing and trading** is often managed by state-owned commodity or processing companies, who in some cases promote contract-farming arrangements to secure their supply of raw materials. Efficient operation of small-scale private input, processing and trading companies is hampered by limited access to vocational and business management training by rural entrepreneurs, and by other resource constraints.
- Several public policy banks and mainstream state-owned or private banks and other financing institutions supply **credit and loans** to rural producers, and sometimes other financial services such as product insurance. Informal providers, local credit associations and Unions also provide credit on highly varying conditions. The coverage of financial services is therefore generally high, though the access of resource-poor farmers to formal services that matches their resource level is sometimes restricted. This leaves them to secure loans from informal sources, particularly in cases where financing is needed to absorb livelihood shocks. Loans with more than a 3-year repayment period are uncommon, which restricts longer-term investments. Subsidized lending from policy banks challenge the long term viability of lending operations and restricts opportunities of private banks to increase their market share. Restrictions on licensing finally limit the number of non-state micro-financing agencies.
- There is a limited supply of **enterprise development services** such as business management, technology innovation and market information services specifically targeting small rural enterprises or larger scale state-owned and private enterprises. Some Unions are piloting provision of **legal services** to rural producers, but such services are yet to be mainstreamed in spite of a significant need for legal advice, for instance in relation to contract farming.

- **Infrastructure projects** are typically managed and owned by provincial or district line agencies, which contract local state-owned or private companies for system design and construction. However, one of the objectives of the P 135 is to decentralize ownership to the commune level. Systems are typically 100% subsidized by the state, except for local provision of labor inputs towards construction, which along with centralized planning of infrastructure works and central prescription of design models result in less than optimal local worthiness of investments, and consequently less than optimal production impact. System operation and management (O&M) is supported by semi-formal user groups, water cooperatives or public or private infrastructure management companies but is largely unsustainable as user fees for O&M typically do not cover costs.

Box 4.3:

Main Characteristics of Systems for Organizing Farmers' Articulation of Demand in Vietnam

- Due to the dominant role played by provincial input and trading companies in many provinces, farmers generally have limited choice with respect to selection of **input providers and production outlets**. However, these elaborate systems of state-owned input supply and trading on the other hand do provide for an element of production security for farmers, as they have secure channels for input and sale of produce, even though efficiency may be limited due to the restricted choice. **Cooperatives** are mainly engaged in provision of production inputs.
- **Extension clubs and groups** set-up in the context of public extension efforts in some provinces (but not all) are primarily seen as a means to organize delivery of demonstrations and training. Current regulations enable formal recognition of **cooperative groups** and similar semi-formal types of farmer groups, and numerous pilots aimed at using such mechanisms as a means to enhance demand articulation and generation of local funds for service provision are supported by Vietnamese centers and INGOs. However, such approaches, as well as generic village planning approaches, are rarely mainstreamed into provincial or national planning and delivery frameworks.
- **Infrastructure user groups** are, as mentioned above, established to organize payment of fees and O&M of systems, and to organize provision of village labor inputs towards construction. However, the engagement of these groups in prioritization of infrastructure inputs, selection of providers, technology choice, and design of systems is limited.

There are significant variation between provinces, service types and commodity types with regard to the role played by non-state actors, and consequently the level of choice that farmers can assert when seeking to cover their service needs. The level of choice is generally less in remote areas, where issues such as geographical distance, social and cultural differences, poverty and small farm sizes create barriers for profitable operations by non-state service providers.

More detailed analysis of service provision in agricultural extension, financial services and rural water supply and sanitation is provided in the three illustrative case studies included in Annex A.

5. ALIGNING SUPPLY AND DEMAND: MOVING TOWARDS DIVERSIFIED SERVICE PROVISION IN A CHANGING PRODUCTION ENVIRONMENT

5.1. Diversity of service needs and corresponding service provision requirements

It follows from the analysis in section 3.2 that the increasing diversification of clients is an important defining feature of rural service provision in Vietnam. This calls for a review of whether the current objectives set out for rural service provision matches these increasingly diversified needs, and for broadening of the definition of what constitutes "rural services". The increasing diversity of service needs and the implications for the objectives and overall orientation for rural service delivery systems objectives are explored in more detail in Box 5.1.

Box 5.1: Diversity of Service Needs and Corresponding Features of Service Delivery Systems

Diversity of Service Needs		Corresponding Features of Service Delivery Systems	
Key Client Categories	Service Needs	Service Objectives	Strategic Orientation of Service Systems
Poor subsistence farmers with limited market	▪ High proportion of basic education,	Services contribute effectively towards elimination of	▪ Broad mix of basic, social welfare, financial security and traditional / subsistence

<p>potential</p> <ul style="list-style-type: none"> ▪ <i>Limited resources, high vulnerability; limited shock absorption capacity; social, economic and geographical barriers for access to and effective use of services (often but not only ethnic minorities in remote areas)</i> 	<p>vocational and health inputs</p> <ul style="list-style-type: none"> ▪ Low-risk, low-cost production services matching weak resources ▪ Multi-faceted production services that enable traditional / integrated farming approach ▪ Affordable short and medium finance services suitable to support household investments and alleviate livelihood shocks ▪ Services that enable orderly out migration to areas with high employment potential 	<p>hunger and poverty by enabling livelihood strategies that enhance the viability of subsistence farming and out migration for employment.</p>	<p>production services.</p> <ul style="list-style-type: none"> ▪ Mainly public service provision due to high social welfare element and absence of non-state providers in remote areas ▪ Farmer-to-farmer services where relevant to counter need for intensive provider-client interaction and high delivery costs in remote areas ▪ Significant subsidy element justified due to public good aspect of social welfare, but subsidies should be linked to the demand rather than the supply of services. ▪ Element of client payment for infrastructure investments and services to enhance mutual accountability by provider and client ▪ Specifically targeted service content that match the complex and weak livelihood security situation faced by remotely located ethnic and poor farmer households. ▪ Participatory and demand-oriented delivery modalities that match cultural context for production and enable informed livelihood security decisions by clients. ▪ Systematic support to broad-based community organization and planning
<p>Poor farming households with market potential</p> <ul style="list-style-type: none"> ▪ <i>Limited resources, high vulnerability, and limited capacity to absorb market failures and other shocks; social and economic barriers for effective use of services (typically poor households in delta and coastal areas)</i> 	<ul style="list-style-type: none"> ▪ Relatively high proportion of basic education, vocational and health inputs ▪ Low-risk, low-cost production services matching weak resources ▪ Production services that enable farmers to chose preferred line(s) of production ▪ Market information and production management services to reduce losses from failed investments and price fluctuations ▪ Affordable 	<ul style="list-style-type: none"> ▪ Services contribute effectively to enhanced livelihood security by enabling livelihood strategies that primarily focus on enhanced production efficiency and market access but also support move to off-farm employment. 	<ul style="list-style-type: none"> ▪ Mix of basic, financial security, production services, marketing and production management services ▪ Demand-orientation and availability of wide mix of production and market services that enable farmers to pursue preferred line(s) of production ▪ Use of public-private partnership arrangements to co-fund services given mix of public and private good interest in maintaining high on-farm employment ▪ High element of user payment to enhance relevance and efficiency of infrastructure investments and services, enhance provider/client accountability, and due to private good element of farmers' market-oriented production. Any subsidy should be linked to the

	<p>financial services suitable to support household investments and alleviate livelihood and market shocks</p> <ul style="list-style-type: none"> ▪ Services that enable move to off-farm employment 		<p>demand rather than the supply of services.</p> <ul style="list-style-type: none"> ▪ Systematic support to production-focused client organization, demand articulation and planning
<p>Large commercial farms</p> <ul style="list-style-type: none"> ▪ <i>Significant economic resources and robustness; high market exposure; high capacity to pay for and absorb services (typically located in delta and coastal areas)</i> 	<ul style="list-style-type: none"> ▪ Specialized production services that support chosen product specialization ▪ High need for services supporting business and production management ▪ Specialized marketing services, e.g. market information, product certification Environmental health & quality control services ▪ Availability of range of financial services, including short to long term financing for production investment and operation, and production insurance 	<ul style="list-style-type: none"> ▪ Services contribute effectively to enhanced production efficiency, viability and marketability, by enabling technological production innovation, financing, product certification and efficient market access 	<ul style="list-style-type: none"> ▪ Focus on demand-driven technology innovation, financial, production/business management, certification and marketing services ▪ Full client payment for services as commercial production is a private good, and due to the ability of clients to pay. ▪ Significant service input from research institutes and producer associations and private providers given specialized and sophisticated nature of services and ability of clients to pay for services (i.e. demand-orientation).
<p>Small agro-businesses and traders</p> <ul style="list-style-type: none"> ▪ <i>May be formal or informal, typically household-based with limited resources and market outreach. May be service or processing oriented (e.g. trading or saw-mills), with the</i> 	<ul style="list-style-type: none"> ▪ High need for small scale business development and technology services that support chosen line of business ▪ Flexible finance services to support small scale business investments and alleviate 	<ul style="list-style-type: none"> ▪ Services contribute to wide coverage and efficient operations of multiple types of small agro-businesses and traders that are able to produce the services and processing needs of their clients 	<ul style="list-style-type: none"> ▪ Focus on small-scale enterprise development services, including business management training, technology innovation, market information and financing. ▪ Full client payment for services as private business is a private good. ▪ Significant input from private providers desirable given that clients are private enterprises

<p><i>latter more exposed to market fluctuations. Often social and economic barriers for effective use of services (located nation-wide)</i></p>	<p>livelihood shocks</p> <ul style="list-style-type: none"> ▪ Service availability in all parts of the country 		
<p>Large, commercial agro-businesses</p> <ul style="list-style-type: none"> ▪ <i>May be private or state-owned enterprises; significant economic resources and robustness; high market exposure; high capacity to pay for and absorb services (typically located in delta and costal areas)</i> 	<ul style="list-style-type: none"> ▪ Need for business management capacity building, technology innovation, market information and financing services that matches scale and sophistication of business 	<ul style="list-style-type: none"> ▪ Services contribute to effective, profitable and sustainable production and market operations of large commercial agro-businesses in a competitive environment 	<ul style="list-style-type: none"> ▪ Focus on technology innovation, financial, production/business management, certification and marketing services ▪ Full client payment for services as commercial production is a private good, and due to the ability of clients to pay. ▪ Significant service input from research institutes and business associations and private providers given specialized and commercial nature of services and ability of clients to pay for services (i.e. demand-orientation).

5.2. Gap analysis: Overall considerations for reform of service provision systems

As illustrated in Box 5.1, the clientele of rural producers is becoming more heterogenic, and service needs are becoming more complex and diverse. *Rural service systems need to address this increasing diversity*, ranging from the needs of increasingly marginalized ethnic minority farmers to increasingly sophisticated and big-scale farmer and rural enterprises. *The criteria for defining what constitutes effective and relevant service provision, and consequently the objectives, content and modalities of rural service provision need to reflect this increasing diversity, and must therefore be revisited.* The corresponding challenges for the delivery of services in Vietnam are explored in the following.

In absolute numbers, poor smallholders, including those with market potential and those without, constitute the absolute majority of rural service clients. In order to meet national poverty reduction objectives, it is therefore *critical that rural service provision systems effectively support the efforts of these constituencies to escape poverty.* However, with the increasing commercialization and market-orientation of rural production, it is also *critical that services simultaneously enable the increasing number of rural industries, commercial service agents and large-scale, market-oriented farmers in mainstream areas to take advantage of technology innovations needed to optimize competitiveness.*

Vietnam's success in intensifying existing production practices through adoption of research into improved rice varieties, and plant protection and animal health practices is well known. However, efforts to diversify rural production have had varying degrees of success, both from the point of view of individual producers and from the point of view of maximizing the effects of national investments in rural service provision and infrastructure. Large increases in production of crops such as coffee, pepper, lychee, cashew, and citrus resulting from both intensification of production practices and expansion of the land area allocated to the production of these crops point to success in the transfer of technology. However, rapid increases in production, without a good understanding of markets and profitability, have in many cases led to oversupply, price reductions and corresponding negative net returns for many farmers who diversified. It is therefore a reasonable assumption that a target driven approaches to service delivery has and will not be able effectively predict, or prevent, the down stream problems they create. Effective return on public and private investments in intensification and diversification of rural production therefore will require *application of more decentralized and demand-driven approaches to rural service provision planning.*

Finally, in the context of Vietnam's increasing exposure to global market forces, future production increase and diversification will depend less on bringing additional production factors into production (such as additional land allocated towards production of specific commodities) and more on efficiency gains in the way that public and private inputs are used and managed. Overall, *rural service provision therefore needs to focus on production efficiency*. This focus on efficiency poses a range of inter-related challenges for rural service provision with regard to the planning and funding of services, the range of service available, the modalities of delivery, the coverage and targeting of services, and the range and capacity of providers involved in service delivery.

Based on international experience and the analysis of current systems for service provision in Vietnam, it is doubtful whether the current public service provision systems will be able to effectively respond to the challenges associated with meeting the more diversified service needs of rural service clients, and therefore more effectively contribute to national objectives related to poverty alleviation and increasing the contribution of rural production to national economic growth. Likewise, as for infrastructure, while generally infrastructure coverage is impressive by international comparison, the contribution of infrastructure to poverty alleviation and productivity enhancement is less than optimal due to systemic inefficiencies, such as less than optimal investment decisions caused by centralized planning, disparities in regional coverage, lack of quality control incentives, and underinvestment in operation and maintenance.

It is therefore suggested that *a shift in the basic paradigm underpinning rural service provision in Vietnam is required* to ensure that rural services effectively support national objectives. The key elements of this new rural services paradigm includes the following:

- *Farmers and rural enterprises alike should be seen as entrepreneurs*, who like business actors in urban areas should be allowed to make production decisions based on self-interest and profitability.
- Consequently, *rural service provision should be liberalized*, to ensure the emergence of a more diversified service market where multiple service providers, public as well as private, compete to deliver services that meet the demands of rural entrepreneurs, and where rural entrepreneurs select and buy services based on informed production decisions.

It is assumed that a high degree of alignment between production choices made by individual rural entrepreneurs and national socio-economic priorities for rural production will be achieved, due to efficiency gains generated from the emergence of this more pluralistic service market. Moving towards this new paradigm will require significant transformation of current service delivery systems in Vietnam, given the prevalence of public service structures and the rudimentary stage of non-state service providers and farmer organizations. *Reform of rural service delivery along these lines must however be practical and applicable in the political and institutional context of Vietnam, and careful consideration of "how to get there" will consequently be required*, including thorough preparatory analysis, piloting and a gradual approach to mainstreaming of these new approaches.

Systemic efforts in this direction are required not only in order for Vietnam to meet the challenges facing rural production, but also to better cope with the effects of the forthcoming liberalization of services allowing foreign service providers to operate in the country⁷.

5.3. Gap analysis: Specific considerations for reform of service provision systems

5.3.1. Governance and coordination of rural service provision

Focusing the role of central authorities on governance and coordination: As documented by the analysis in section 4, rural service provision in Vietnam largely remain a public activity, with central authorities not only maintaining governance functions such as state management, regulatory, planning and finance allocation functions, but also direct line management responsibilities for definition of the technical content and delivery modality of services. Central agencies furthermore, along with provincial administrations, maintain direct responsibilities for oversight of service delivery by local line agencies, and maintain ownership to numerous state owned service enterprises. At the same time, as further discussed below, provincial and local level agencies acts as funders as well as providers of services. *In order to move towards a more liberalized service provision framework, these basic linkages between governance and management on the one hand, and between funding and provision on the other, need to be severed* to enhance efficiency, relevance and quality of services delivered.

⁷ MPI/UNDP 2006.

In order to facilitate that the range of services supplied and modalities applied by public and private service providers more directly reflect local conditions and local needs, *central agencies in line with the ongoing decentralization and public administrative reform process should focus on their core state management responsibilities*. This would include:

- Overall policy development and regulation, and impact monitoring to ensure that service delivery effectively support national socio-economic priorities for rural production and development.
- Overall sector planning, coordination, fund allocation and direction to facilitate effective service delivery, including horizontal and vertical coordination and planning integration between the various central agencies performing responsibilities affecting rural service delivery⁸.
- Performance monitoring of service provision agents and evaluation of service delivery impact.

In this context, *central authorities should in particular secure an enabling environment for the engagement of a variety of service agents in service delivery*. With the capacity and coverage of non-state providers currently being rudimentary at best, this would include support to creating favorable conditions for incorporation, capacity building and operation of new service providers, as well as support to re-orientation and capacity building of existing service providers.

Addressing diversity of service needs in policy frameworks: *Different service provision strategies geared to address the diversified service need of different client constituencies need to be elaborated*, as such strategic stratification, aside from poverty targeting under specialized national programs, is largely absent in current service provision systems. *Combined, these strategies must aim to ensure that rural service provision enable: 1) poor farmers to efficiently pursue their strategies for escaping poverty, 2) efficient commercial production of poor, small and large farmers with market-potential, 3) operations of small scale rural service and processing enterprises as required for them to fulfill their critical roles in local rural economies, and 4) establishment and operation of competitive rural industries geared to increase the processing and quality levels of Vietnamese rural products.*

5.3.2. Systems for delivery of rural services

Addressing diversity of service needs in planning and management frameworks: It is unrealistic to expect that centrally prescribed solutions and planning frameworks currently applied in Vietnam will be able to cater to the increasing diversity of service needs in an efficient manner. In order to pursue diversified strategies for rural service delivery, *service provision planning therefore need to be reformed along the following lines:*

- To be efficient producers, farmers and rural enterprises require timely and affordable provision of quality services that cater to the service needs in all phases of the production cycle. Service provision strategies should therefore apply a “*systems approach*” to the analysis of service provision needs, i.e. a service needs analysis that takes its point of departure in production (and/or livelihood) systems rather than the individual parts of the production cycle.
- The point of departure for diversified service provision planning must be in-depth *analysis of the fundamental causes of poverty and/or production inefficiencies* for each client constituency, as well as a clear understanding of the strategies applied by each constituency to exit poverty and/or increasing production efficiency.
- In order to cater to diversity, local needs and production priorities, *planning decisions need to be decentralized* to the lowest possible administrative level. This in turn requires that planning frameworks genuinely incorporate local inputs rather than taking a token approach in this regard, and that *capacity building investments* are made to enhance the ability of local level authorities and stakeholders to engage in meaningful planning efforts.
- Providing service constituencies with *control over funding* for service provision will help creating strong incentives for demand-driven local service provision planning, as further discussed in the bullet on separation of funding from service delivery below.

It should be realized that it is not in the immediate institutional interests of existing public service provision agencies to institutionalize demand-driven service planning and fund management approaches piloted under specialized national programs and by international agencies in Vietnam.

⁸ An example of required horizontal coordination would be improved coordination of agricultural research, extension training and education across involved Ministries, while an example of vertical coordination would be the promulgation of provincial regulations and guidelines clarifying the functions, roles, responsibilities and degree of flexibility granted to lower administrative units with regard to management and implementation of service delivery.

High-level leadership in support of policy change and mainstreaming of alternative planning and funding mechanisms is therefore essential to make this happen.

Control over funds and payment for services: Under the current public system for service and infrastructure provision in Vietnam, service delivering agencies, such as provincial departments for agricultural extension and rural water supply, are also managing budgets for delivery and investment. In addition, services and infrastructure is mostly provided free of cost, or with provision of incentives for farmers to engage, such as in the case of agricultural demonstrations and training.

This widespread use of *subsidies and grants* is inherently ineffective, as it increases the risk of capture, inefficient investment planning, delivery and reduced cost effectiveness. The use of subsidies furthermore burdens public budgets to an extent that the coverage of services and infrastructure is often far less than what is required by local constituencies, such as for instance in the case of public resettlement schemes⁹. As a matter of principle, *subsidies and grants should therefore be limited to the extent possible, exclusively target disadvantaged producer constituencies, and always be provided in a disproportionate relationship to the private goods benefits generated by the service in question* (e.g. subsidized extension provision to poor subsistence farmers could be considered a public good and therefore justified, while this is not the case for commercial farmers and agro-businesses).

As documented in the case studies on agricultural extension and financial services, as well as other studies, *Vietnamese farmers are willing to pay for services, and even to the costs of infrastructure, provided they contribute effectively to increasing productivity and income*¹⁰. *This fact should be exploited by service delivery systems, as such client and user payment is critical for increasing the accountability, efficiency, demand-orientation and financial sustainability of service delivery.*

This does not imply that subsidies and grants should not be provided, but that *the mechanisms of subsidy and grant provision when applied should aim to prevent distortion of the quality of services and rational investment decisions*. For instance, as pointed out in the case study on financial services, the distorting effects of subsidized credit provision could be avoided if disadvantaged clients needing lower interest rates are provided with interest payment coupons from the state, rather than the state subsidizing interests and guaranteeing loans directly with financial service providers. Similarly, investment planning inefficiencies related to small scale infrastructure provision could largely be mitigated if local producers were enabled to finance such structures collectively themselves through provision of appropriately designed credit schemes, or mechanisms where the value of initial public constriction financing is subsequently "reimbursed" by the beneficiaries through phased re-payment schemes.

It is important to point out that these increased efficiencies only occur when rural producers can assert their financial influence by choosing between services offered by multiple providers. *Separation of funding from delivery and increased user financing must therefore be accompanied by policies that allow private access to public funds for extension service delivery* to encourage pluralism or socialization of service delivery through mobilization of multiple public and private sector service providers. Such systems could for instance include in-part coverage of the salary and operational costs for non-state service provision, combined with user payment¹¹.

Models for decentralized and producer-based (or community-based) service planning and finance management are already being piloted under specialized national programs and numerous internationally supported programs, and *efforts should therefore be made to mainstream positive experiences from such pilots*, including the commune investment ownership approach applied under Program 135. Following such approaches, public funds for services could be allocated to communes (or to local organizations representing local producer constituencies) based on locally organized service needs planning in the context of local SEDP planning. Communes (or local producer organizations) could then contract local public and/or non-state service providers for delivery of the services in question.

⁹ ADB 2006b

¹⁰ ADB 2006b, p. 21

¹¹ For a model applied in Germany where costs of a public extension system are shared by the state and users, see GTZ 2007, pp. 50-60

Engagement of non-state providers: Due to the dominant role of public service providers, including state-owned supply and trading companies, the role and capacity of non-state providers is limited, though there are major variations between different localities, service categories and commodities. The level of competition between providers and choice of producers therefore also varies. *There is consequently a very significant need to facilitate that multiple providers, public as well as private, can compete in local service markets, and increase their capacities and resources to do so.* Achieving this objective would require a wide range of policy initiatives, including the following:

- Provision of public funding to non-state service providers based on productivity norms and output rather than prescribed cost norms and methodologies. This could for instance include funding from public budgets of service provision staff in relevant Unions, associations, centers and local organizations representing producer constituencies.
- Focusing public sector delivery on service provision in remote areas where physical and/or social barriers make it unrealistic that non-state actors can operate on a financially viable basis.
- Equitization of state-owned service companies and break-up of their operations in smaller, more specialized units as appropriate.
- Establishment of capacity building programs and certification systems for non-state suppliers, whether public, non-profit or commercial, and promulgation of enabling legislation as required.
- Establishment of performance monitoring systems aimed at providing service users and authorities responsible for oversight of the “service provision market” with the information required to assess quality of services and improve delivery systems.

Expanding the range of services: A systemic weakness of the current target based approach to service provision planning is that the responsible public agencies have a limited understanding of profit motives, and consequently limited understanding of rural producers as market-dependent entrepreneurs. Rural producers are consequently conned by “the fashion of the day” and extension’s desire to achieve targets rather than a rational approach to business planning.

Therefore, as rural production in Vietnam becomes more diversified and market-driven, rural service provision systems need to *address not only technology of production, but also the increasing need for a broader variety of financial services and services aimed at strengthening the commercial management and marketing skills of service provision constituencies*, including farm management, market analysis, marketing, organization and negotiation, and contract and finance management. Specifically, services aimed at enabling producers to operate in the context of defined product value chains are of increasing importance. As regards technology related services, *more emphasis needs to be put on provision of a differentiated menu of technology options catering to the varying resource and absorption levels of different producer constituencies* (e.g. low-tech and low-risk solutions for poor households).

Targeting rural service provision in disadvantaged remote areas: Significant efforts have been made by the GoV to target poor regions and people through 1) decentralized categorization of the poor, 2) allocation of subsidized benefits to those identified as poor (e.g. health insurance cards), and 3) through implementation of specialized national programs aimed at providing subsidized services and infrastructure to disadvantaged localities (such as the P135 II). However, services delivery modalities are generally better geared to reach relatively well-off farmers, and the visibility of services in poor communities is low, especially in remote areas. The slow-down in poverty reduction and widening disparities between relatively well-off and the poor suggests that *service delivery targeting poor and marginalized farmer groups must be strengthened significantly*.

Due to the inherent difficulties in reaching resource poor producers, the current efforts to target services on the poor are facing a number of obstacles:

- The transaction costs associated with reaching poor producers, especially in remote areas, are prohibitively high given the current modalities applied. Alternative delivery modalities to reduce the delivery costs per farmer and identification of alternative sources of financing are therefore required if stated policies of equity, participation and socialization of services are to be achieved.
- Unless activities under national programs builds on careful analysis of underlying causes of poverty, investments under these programs will not effectively contribute to poverty alleviation. For instance, a recent study questions the justification of high investments in road construction in remote areas, as good access, given the prevalence of other underlying causes

of poverty, is not sufficient to secure private investment and hence sustainable economic development in most remote areas¹².

- Like in other programs, the combination of a centralized approach to service and investment planning, centralized definition of services content and infrastructure design, and high levels of subsidy result in low incentives for local implementing authorities and beneficiaries alike to ensure effective investment planning.
- Programs relying on geographical targeting combined with high subsidies, whether directed at individual households or localities, are inherently ineffective, as they are exposed to heavy leakage, i.e. subject to diversion of investments away from the intended target group. A recent study suggests that the level of such leakage in targeted programs in Vietnam is as high as 25% (subsidized lending programs) to 45% (P135)¹³.
- It is not realistic to expect that effective service markets can be sustained in poor remote regions as the operation of private service agents in many cases will not be financially viable due the logistic and other economic barriers to business in remote areas.

A major cause of the inefficiency of targeted programs seems to be incorrect assumptions underlying the targeting approaches, including that 1) most poor people live in poor regions, 2) money and public investment flowing into poor regions will automatically lead to economic development and poverty reduction, and 3) the solution to poverty reduction lies within the poor regions themselves. Targeted service and investment approaches, by focusing narrowly on accurately identifying the poor and excluding the non-poor, ends up isolating the poor from mainstream growth, and leaving them to rely on (inefficient) subsidy schemes or external assistance.

On the basis of this analysis, *the approaches to service provision and poverty alleviation in poor regions should include the following features:*

- Service provision strategies for poor regions with limited economic development potential must reflect the fact that the solutions to the livelihood challenges of poor client constituencies may not only lie in providing services and infrastructure in the geographical areas where they live, but also in providing services enabling orderly migration to geographical areas with high employment potential, thereby enabling the remaining producers to sustain their livelihoods based on financially sustainable rural production. Such service strategies could emphasize support to household investment in basic education to ensure that more children meets the minimum education requirements for formal employment in better-off regions, and services alleviating the costs of physical out-migration and creation of employment and social contacts in better-off areas.
- To enhance the efficiency of public service provision to producers remaining in their localities, service content and modalities need to be reformed to create an environment for demand-oriented service provision. These changes must acknowledge the role of poor rural producers as entrepreneurs and ensure an element of choice in spite of the less than optimal conditions for service supply competition.
- More specifically, to reduce transaction costs and enhance coverage of service delivery in remote areas, genuine investment in farmer to farmer extension/service provision systems, that are not assuming voluntary inputs by farmer agents is required, as are investments in building service systems involving organizations representing producer constituencies in service supply. Cost effective delivery would also require introduction of result and performance based planning and incentives rather than systems rewarding activity completion.

5.3.3. **Systems for organization and articulation of demand**

Farmers' participation and influence over service supply decisions: In line with the GoV's stated objective of socialization and participation, and to facilitate efficient supply of relevant quality services, rural producers must be empowered to take a leading role in definition of service needs, pay for services and selecting service providers. *Service delivery reform must therefore include systematic efforts to facilitate and promote leadership and organization of rural producers in the context of cooperatives, cooperative groups and other types of formal and informal farmer organizations. This would require policy initiatives to:*

- Mainstream the role of organizations representing rural producer constituencies based on the positive experiences from the numerous farmer organization pilots promoted by international agencies in Vietnam.

¹² ADB 2006b, p. 25.

¹³ Viet Nam Development Report 2004, here referred to in ADB 2006a, p. 25.

- Establish effective systems for capacity building and operation of producer organizations, including systems for financing of such organizations and regulations to facilitate official recognition, independence and participatory management of these organizations. Numerous models for organization of farmers' demand articulation are available internationally from developed, transitional as well as developing countries.

6. POLICY IMPLICATIONS AND RECOMMENDATIONS FOR THE RURAL DEVELOPMENT POLICY

6.1. Recommendations on policy content: A new paradigm, vision and policy initiatives for rural service reform

On the basis of the analysis in section 5 and preceding sections, it seems fair to conclude that *there is a widening gap between the desired performance of rural service systems, given the current challenges facing rural production in Vietnam, the objectives set for the sector, and the actual performance of these service systems.* It is therefore the view of this paper that *a shift in the approach to rural service provision is required.*

Box 6.1: A New Paradigm for Rural Service Provision in Vietnam

In order to ensure that rural services effectively support national objectives in the context of the current diversification of rural service needs in Vietnam, application of a **new service provision paradigm** that perceives farmers and rural enterprises alike as "entrepreneurs", and promotes the emergence of a demand-oriented and decentralized service market for service provision, is required. As this shift would require a fundamental re-orientation of current service delivery systems, and a careful approach to analysis, piloting and mainstreaming of this new approach should be applied.

In this context, *the following vision for rural service delivery reform in Vietnam is recommended for consideration by the Rural Development Strategy:*

Box 6.2: Vision for Rural Service Provision in Vietnam

The coverage, types of services and delivery modes of rural service provision in Vietnam meets the needs of increasingly diversified rural producers and stakeholders, ranging from poor ethnic subsistence farmers to large commercial agro-enterprises, and effectively support the following objectives for service delivery, based on national socio-economic priorities:

- **Poverty alleviation and livelihood security:** Poor and ethnic minority producers in remote areas have access to relevant services that allow them to make informed livelihood and production choices based on their specific livelihood situation and production capacities, and effectively contribute towards elimination of hunger and poverty.
- **Food security:** Rural services enable farmers to meet domestic demands for food securing through production of staple food commodities
- **Product diversification and value-adding:** Rural services enable market-exposed farmers and companies to diversify and commercialize their production, enhance efficiency in all production phases, and enhance processing and value added of produce in consideration of their market access.
- **Competitiveness:** Rural services treat farmers as entrepreneurs and facilitate adaptation by farmers and agro-businesses to a more competitive and fluctuating business environment in domestic and export markets.
- **Sustainable production:** Rural services enable producers to protect the rural environment.

In order to enhance efficiency, demand-orientation and market-focus, rural services are 1) delivered in accordance with diversified delivery strategies geared to meet the service needs of increasingly diversified service constituencies, 2) delivered by multiple public and private service providers to enable competition and efficiency in service provision, and 3) paid for by rural producers, with special targeting and subsidies limited to the extent possible and linked to the demand side rather than the supply side. National policies and institutions effectively enable required reform of existing public systems, promote entry and operation of non-state service providers, and empower rural producers through collective action and organization at local levels.

Reform of current systems for service delivery to better address the requirements set out by this vision is both desirable and clearly possible in the context of the current policy, institutional and socio-economic development setting of Vietnam.

Referring to the analysis in section 5, *the overall, critical policy recommendations for policy reform of rural service provision presented in Box 6.3 are **recommended** for consideration by the Rural Development Strategy.* For detailed recommendations, please refer to the analysis in section 5 (text marked in *Italics*):

Box 6.3: Enhancing efficiencies - Critical Policy Initiatives for Reform of Rural Service Provision in Vietnam

Initiatives for an enabling policy and institutional environment

- *Systemic service policy analysis* aimed at linking rural service objectives to the wider socio-economic objectives for rural development and production in the context of the socio-economic transformation of rural Vietnam
- Development of *diversified service provision strategies* catering to the needs of the increasingly diverse rural producer constituencies in Vietnam
- *Horizontal and vertical coordination and integration* of rural service delivery planning into mainstream SEDP planning to facilitate adoption of a “systems approach” to rural service provision that ensures that service provision in an integrated fashion caters to service needs related to all phases of the rural production cycle.
- *Application of the principles of Vietnam’s public administrative reform and decentralization process* to rural service provision in order to separate governance from management and funding from delivery.
- *Monitoring focus on performance management and service impact*

Initiatives for enhanced relevance and coverage of services, and competence and coordination of service providers:

- *Decentralization of service provision*, including planning, content determination and finance management
- *Demand-responsiveness, flexibility and focus on production efficiency in the context of diversified service strategies* as required to respond to the need for farmers and companies to quickly adapt to rapidly fluctuating market conditions, and to enhance the efficiency of service and infrastructure investments
- *Separating service delivery from funding of services* by enhancing the control of rural producers over service funds and by allocating public funds to semi-state and private service providers
- *Limiting the use of subsidies and targeting modalities and where subsidies are justified link these to the demand side* rather than the supply side to enhance delivery efficiency and impact
- *Promoting entry and operation of multiple and diverse service providers*

Initiatives for articulation of demand by rural producers:

- *Empowerment and organization of rural producers* to take a leading role in articulation of service needs, payment for services and selection of service providers.

6.2. How to move forward: Some recommended reform principles and process issues for consideration by the RDS

It is important for the viability of any reform process to identify how it should be initiated and moved forward, and who should drive it. It is therefore **recommended** that reform of rural service provision in the context of the Rural Development Strategy should apply the reform principles listed in Box 6.4.

Box 6.4: Principles for reform of rural service provision in Vietnam in the context of the RDS

Content principles – reform must:

- Be based on the policy and institutional reality of Vietnam while simultaneously taking into consideration international learning and experience. An incremental approach to reform, where consensus is sought for new policy initiatives, and reform initiatives are tested before mainstreamed, is therefore required.
- Take its starting point in systemic analysis of reform needs in light of prevailing socio-economic priorities, and on this basis establish a widely agreed joint vision and strategic directions for rural service provision. Given the dynamic and interrelated nature of the three dimensions of service provision (enabling environment, supply systems and demand

articulation), it is important that they are analyzed and addressed simultaneously and in a systemic fashion to enable coherent and sustainable reform.

- Consider the wider issues of governance and public administrative reform, as these impacts the efficiency of service providing agencies, public as well as semi-state and private.
- Reflect that reform needs vary between different types of services, constituencies and commodities.
- Allocate clear roles and responsibilities of different stakeholders based on analysis of their respective comparative advantages (e.g. public providers should remain in areas where they have comparative advantages but leave the floor to others in other areas).

Process principles – reform must:

- Be clear on strategic directions but at the same time take an incrementally approach to reform, i.e. not addressing too many reform initiatives simultaneously, and initially focusing on easy-wins and win-wins.
- Ensure appropriate institutional consultation for reform that includes all relevant public and non-state stakeholders to rural service provision.
- Ensure that reform agents are in place at all three levels of service delivery, i.e. the policy, supply system and demand articulation level. Inputs from reform agents at all three levels is required as it is rarely possible for decision-makers at the top of public service provision systems to gauge the diverse needs of farmers and critically assess the flaws in traditional service delivery systems, particularly at times of significant transformation.

6.3. Specific recommendations for initiation of rural service reform in the context of the RDS

With a view to facilitate initiation of rural service reform in the context of the Rural Development Strategy, *the following immediate reform initiatives are **recommended***:

- 1) *Preparation of the diversified service provision strategies for different rural service constituencies recommended above*, as required to provide a basis for the steps proposed in the following. These strategies must build on systemic analysis of the three core dimensions of service delivery, analysis of the underlying causes of poverty and production inefficiencies in Vietnam, analysis of international experience, and analysis of the experiences of piloting of demand-driven, participatory service approaches in the context of Vietnam.
- 2) *Implementation of facilitated multi-stakeholder consultation processes* to agree on vision, overall strategic direction and action planning for rural service provision in the context of the diversified rural service provision strategies. Such consultation should be conducted throughout the preparation of the strategies.
- 3) *Testing of the diversified rural service provision strategies in selected provinces* where the composition of local service stakeholders and production conditions are representative in the context of each of the diversified service strategies.

Annex A:
Rural service provision in Vietnam: Illustrative cases

THE CASE OF AGRICULTURAL EXTENSION¹⁴

The National Agricultural Extension Center (NAEC), the main central level implementation agency for agricultural extension, oversees the national agricultural extension system comprising provincial, district and commune level agencies. While not all provinces maintain all levels of organization, the systems' coverage is nation-wide, totaling more than 13,000 staff. Demonstration models, farmer training and mass media information campaigns remain the main extension delivery mechanisms employed by NAEC, and their focus and content is prescribed centrally. Extension activities are implemented according to fixed cost-norms through contracts with a range of public or semi-public providers, including provincial extension centers, district stations, research institutions, universities and mass media. At the commune and village level, extension is often managed and delivered through networks of extension workers and voluntary extension clubs and groups.

In addition the Plant Protection Department (PPD) supports the implementation of participatory Farmers' Field Schools (FFS) in the context of the National Integrated Pest Management Program (NIPMP). This program is implemented through PPD sub-departments (PPSD) in provinces throughout the country. The program is highly dependent on funding from international resources, but increasingly funding is provided from provinces interested in the promotion of safe food production.

Extension targeting special groups in the context of specialized programs such as Program 135 is implemented through the mainstream public extension system. Aside from universities and research stations, other semi-public, business or civil society providers have limited access to participating in public extension delivery. Extension provided by such actors is probably significant, but these contributions are neither reflected in extension planning nor widely acknowledged.

Relevance of services and delivery modalities: The demonstration model and training approach has resulted in some undeniable achievements. Some models are effective in terms of adoption by farmers, such as models promoting higher yielding or shorter duration rice. The main reasons for success include low cost technology, proven ability to increase net income and demonstrated high impact from technology. Models that involve complex and high cost technologies, and hence high inputs by farmers, have associated high risk and limited improvement in net income are less successful. Recent reviews have found that while there is a reasonably good awareness of the demonstrations by non-participating farmers, there is a need to develop strategies for wider dissemination of successful demonstrations. This calls for more systematic use of farmer-to-farmer extension systems, particularly in remote areas, where social and geographical barriers prevent intensive contact between extension agents and rural producers. However, the relatively high initial investment costs in establishing Farmers Field Schools and similar methodologies (caused by the need for intensive training of Trainers-of-Trainers and Farmer Trainers), among other factors, have prevented mainstreaming of these approaches, even though their efficiency in enhancing the knowledge base of farmers has been demonstrated in the context of Vietnam. A systematic approach to mainstreaming of such systems, aimed at reducing overall delivery costs by reaching a critical mass of participating farmers is therefore needed in order to fully institutionalize FFS approaches as a main element of extension in Vietnam.

Aside from targeted cost norms and subsidies being applied under national programs such as the P 135, there is no policy on research and extension models specifically targeting the poor, and no formal guidelines for establishing pro-poor training methodologies or including poor farmers' experiences and indigenous knowledge into training curricula and materials. Messages by extension workers are generally more suitable for lowland, homogenous, resource-intensive farming and less suitable for highland farming with small, scattered farms, sloping and poorly irrigated land. Extension messages often concentrate

¹⁴ The analysis contained in this section builds on ADB 2004 and ADB 2006a unless otherwise stated.

on “new” technology with relatively high levels of inputs, and often involving increased risk. This focus on income generation is appropriate for better-off farmers but often require more resources and knowledge than are available to the poor. Extension workers often do not understand the needs of poor farmers, management of risk, indigenous farming practices and opportunities to improve them¹⁵. This, along with the fact that the prevailing theoretical, classroom-based approach to training is relatively inaccessible to poor, ethnic minority farmers, means that the *current extension system and messages are of relatively higher use for mainstream farmers than marginalized ones*.

Current extension messages are mainly focused on technical aspects of crops, livestock, fishery and forestry production. However, there is a *relatively poor understanding of farming as a business*, and a consequent need for extension services to cover a wider range of commodities, issues related to farm business management, commodity chain management (post-harvest storage, processing, marketing, reduction of input costs, use of labor, credit, group action, etc) and market information management. This poses a particular challenge for larger-scale farmers, cooperatives and agro-enterprises, who are left to seek business related advice from non-state agents, or to hire the required services directly. Similarly, *limited attention is put on provision of advisory services in the field of farmer organization*, i.e. advise and support specifically focusing on establishment and operation of formal or informal farmers’ organizations.

Coverage and outreach of services: Reviews of farmer training indicate that during the first 10 years of operation of provincial extension services, *more than 50% of farmers have not attended farmer-training programs of any kind*. In remote and poor areas the proportion of farmers attending farmer-training workshops is even less, and regional poverty assessments and other studies suggest that the level of contact between poor farmers and public service extension workers is low, with wide geographical differences¹⁶. The low level of service in remote and poor areas is mainly caused by the fact that the motivation and ability of local extension workers to service such areas, poor farmers and ethnic minorities is often restricted due to shortage of budgets for transportation and accommodation, as budgets for variable operational costs, though high in comparison with most countries, to a large extent are used for provision of incentives for farmers to participate in training and demonstrations.

To address these issues, recent national programs targeting poor regions, such as the P 135 II, focuses higher levels of extension funding on remote communes, and also more systematically more extensionists from the district to the commune level, employ local persons at the commune level, and apply higher cost norms for remote communes.

Farmers’ participation and influence over extension decisions: Current regulations promote farmers’ participation, empowerment of farmers’ organizations, socialization of services and pluralism in service delivery. However, *in reality, the provincial and national agenda of models is decided, demonstration sites and farmers selected, and the models implemented with little participation from farmers*. Where Extension Clubs and Extension Groups operate successfully, the process of deciding which training to deliver is initiated at the “grass roots” level and subsequently consolidated into district and provincial training programs. However farmer groups often comment that training actually delivered rarely reflect their original planning inputs, and that services seems to be based more on the skills of extension district staff than the needs of farmers.

Experience from numerous international programs, including programs of Action Aid, Oxfam, VECO, GRET and CARE, documents the opportunities as well as institutional and policy barriers to building sustainable and independent farmer organizations that can effectively channel farmers’ demands for extension, engage in farmer-driven information collection and extension, and generate funds for purchase of extension inputs. While many

¹⁵ World Bank 2005b and MPI/UNDP 2004.

¹⁶ Estimates based on VNLHSS 2004 suggest that 36.4% of poor households on average attended meetings on agricultural extension, ranging from 14.8% in the Mekong Delta and 50.8% in the North-east. On average 7.8% of poor households were visited by agricultural extensionists in 2004, with regional variances ranging from 1.0% in the North-eastern South and 12.2% in the North-east.

pilot have been successful¹⁷, these experiences are yet to be mainstreamed into provincial or national level extension systems.

Engagement of non-state providers: Semi-public extension agents include mass organizations (particularly the Women and Farmers Unions), associations (e.g. the Vietnam Tea Association), and centers and institutes affiliated with VUSTA and other Unions. Funding for their extension activities vary and is often dependent on provincial and NAEC budgets. Extension methodologies and delivery modalities therefore often follow those of the public providers. Business agents, such as state-owned and private fertilizer and pesticide companies, provide information as well as inputs to farmers. Contract production of crops is sometimes encouraged, and some marketing/processing companies provide credit. Informal local traders and input providers also provide information to farmers. Surveys suggest that farmers do not rate these agents as major sources of information and advice, and are concerned about the integrity, quality and accuracy of the information provided. However, the level of contact with farmers of these agents is likely to exceed that of the public extension system.

The actual contribution to extension from these sources is unknown. However, it appears that the de facto monopoly situation of public providers in many areas restricts access of non-state providers and hence free choice of clients to choose their preferred providers. It also appears that where services provided by business agents and similar providers do exist, this is a reflection of the fact that the needs of specific client groups are not fully covered by public services. In the context of the increasing commercialization of agricultural production, the role of business sector agents in extension and service delivery is likely to increase significantly in the future.

Public support for enhancing the qualifications of non-state extension agents appears to be limited.

Subsidies and payment of services: The policy of subsidizing farm inputs involved in demonstration and paying farmers to attend associated training has the potential to encourage farmers to attend activities even if the topic or modality is inappropriate and the quality poor. While the use of incentives for farmer adoption has undeniably played a part in the adoption of new technologies for intensification of existing practices¹⁸, the sustainability, efficiency and demand-responsiveness of incentive-based demonstrations as an extension methodology is questionable due to the inherent inefficiencies and high costs associated with this approach. It is therefore unlikely that this model will be able to generate the significant change needed in the context of the current transformation of rural production in Vietnam.

MARD supported farmer needs studies have revealed that 80% of farmers would be willing to pay for extension and training if the content was directly useful to farming. This demonstrates the potential of a more pluralistic agricultural extension delivery system in the context of Vietnam.

¹⁷ Among many potential examples, see for instance the successful pilots documented in Dialogs 2005 and 2006.

¹⁸ MPI/UNDP 2004. In this study, 70% of farmers responded that the demonstrated crops/animals were not in accordance with the farmers' preferences, and 52% quoted that 'getting input' subsidy was the main advantage of being involved in demonstration models. Only 22% identified learning something new as the main advantage.

THE CASE OF FINANCIAL SERVICES FOR RURAL PRODUCTION

Policies enacted in 1989 as part of the “Doi Moi” liberalization process allowed individual households to borrow from formal financial institutions such as the Vietnam Bank for Agriculture and Rural Development (now AgriBank). This is cited as a major factor contributing to the 20–30% growth per annum in rural lending over the past decade¹⁹. The access to credit plays a crucial role in rural production and reduction of poverty and vulnerabilities in Vietnam. Many smallholders borrow formally to diversify, intensify or specialize their production, with small-scale investment in livestock production being a common strategy for leaving subsistence farming. Borrowing money is also a typical household coping strategy in times of emergency or to cope with the shocks resulting from flooding or other natural calamities. Many poor households borrow frequently in times of food shortage and repaid after the rice harvest or when they receive wages. Finally, when investments fail, many households cope with the crisis by borrowing and reinvesting.

A wide range of formal and informal suppliers support the provision of financial services in the rural areas of Vietnam:

- The main players in rural financial service provision are the **formal policy lending institutions**. Among these, the AgriBank serves a broad specter of rural producers, mostly on a commercial basis, while the Vietnam Bank for Social Policy (VBSP) mainly serves the poor through provision of state subsidized and guaranteed loans. VBSP and AgriBank are the two most important sources for provision of financial services to the poor. AgriBank implemented 111 projects at a value of US \$ 4 billion as of end 2007, with large and subsidized credit lines received from ADB, World Bank and ADF, among others.
- **Commercial banks**, including state-owned banks, urban and rural joint stock, joint venture and foreign banks.
- The role of cooperatives in the form of **People’s Credit Funds (PCF)** is also significant, and their number growing, reaching 982 in 2007. These Funds often operate in populous areas near towns, and are typically formed of savers comprising traders and better-off farmers. Operating as officially recognized entities, the PCFs provide an opportunity for savers to gain relatively high returns on savings while enabling borrowers a reliable source of credit at rates that are not significantly higher than commercial rates.
- **Mass organizations** such as the Farmers and Women’s Unions are also reaching out to the poor and women in rural settings. Their activities include provision (against commission) a range of facilitation services in connection with formal lending from AgriBank and VBSP (e.g. identification of households eligible for subsidized loans, loan processing, support for formation of production groups, interest collection), as well as independent micro-finance lending with funding provided by international development programs.
- **Informal lending** from friends, relatives, moneylenders and Hui and Ho (informal lending groups) constitutes an important source of financing for rural producers. These sources are used frequently and for a variety of purposes, including food in times of food shortage, shocks emerging from human or animal disease or natural disasters, and repayment of formal loans. Interests are high, with interests even from relatives reaching 2–3% per month for longer term lending. Such informal lending provides a safety net of last resort for many rural producers. Informal lending groups are not common.

The outreach of some key financial players for agriculture and rural development is summarized in Table 1:

Table 1: outreach of key financial service providers for agriculture and rural development

¹⁹ ADB 2006b, p. 21.

Financial actors	# of branches	# of borrowers	% poor	% women	Average loans (US\$)
AgriBank	2,096	10,000,000	47	-	850
Vietnam Bank of Social Policy	8,749	5,648,000	32	61	383
Peoples Credit Funds	986	1,200,000	48	38	610
Capital Fund for Employment of the Poor	24	68,500	100	75	175
Microfinance Working Group	46	184,000	100	-	90

Source: Lene Hansen and Lilian Diaz: *Vietnam Microfinance Industry Assessment*, 2008

The table demonstrates that millions of people receive loans from different sources. According to industry assessments, rural loans are more easily available in Vietnam than in many other countries.

For rural investments, most loans credit originates from the formal financial institutions, while in the case of shocks and emergencies, most lenders turn to informal sources, including in particular moneylenders, who are the only sources that provides urgently needed funds on the spot and in a fully flexible manner.

AgriBank has achieved substantial success in provision of unsubsidized loans for investment in annual and perennial crops, fisheries and livestock, handicraft and trade, and rural infrastructure. Credit is available to most rural households, including mostly average income and near-poor households, but also to poor households. This success is attributable to the use of land-use certificates as collateral and the strong tradition in Vietnam for repaying debts, resulting in repayment rates of 95% and above in most areas. Easy access is enabled by fairly simple loan application procedures and relatively quick disbursements, typically ranging between 10 days to two weeks. Local authorities and mass organizations also facilitate formal rural lending, especially in government lending programs for the poor.

When considering all sources of credit, including private moneylenders, informal saving and credit groups, friends and relatives, *very few people indeed are fully excluded from access to some form of financial services*. The wide coverage of financial services for agricultural and rural development in Vietnam can largely be attributed to the diversity of financial service providers and their ability to target different needs.

However, in spite of these achievements, a number of weaknesses in current rural financial service provision exist²⁰:

- While the credit processing time of 10-14 days on average for lending from formal policy banks is acceptable to most borrowers for investments, the processing time for group lending takes up to 2 months. Furthermore, this timeframe is not suitable in the case of lending for emergency purposes, and emergency borrowers are therefore left to seek credit from moneylenders at substantively higher rates. Most emergency borrowers could recover by themselves by working harder and reducing consumption, if they had timely access to credit at affordable cost, and if the credit was of long maturity so that they had sufficient time to recover. Formal policy lending institutions could therefore contribute significantly to poverty reduction by reducing the high costs to rural producers of loans for emergencies, for instance by opening up for provision of quick formal loans to people who are already clients.
- While the lending policies of the formal policy financing institutions are generally flexible lending policies, actual implementation varies significantly in different localities reflecting the discretionary power of local loan officers at the grassroots. Locally imposed restrictions include restrictions on maximum loan size, requiring lending to groups only in remote areas, limiting loan extension, and restricting loan use to productive investments. The latter restriction denies access to loans for other

²⁰ ADB 2006b pp. 14-17 and 22-24.

- purposes, such as education investments and coping with emergencies, and thereby misses the opportunity to mitigate two critical causes of rural poverty.
- Given the need for rural infrastructure development and the shortage of grants from government or other funding agencies, demand exists for long-term loans for private investment in small-scale rural infrastructure. Providing long-term loans to finance such improvements, to be repaid by beneficiaries later, could accelerate rural development by alleviating the constraint of insufficient funds for rural infrastructure development. However, lending for these purposes has been limited, mainly due to restrictions faced by formal policy lenders to access long-term funds.
 - Subsidized loans to poor households, particularly in remote areas, are provided mainly by VBSP, but also in some cases by AgriBank. Lending rates are 0.45% or 0.50% per month compared with commercial rates of 1.15% per month from AgriBank and 1.35% from PCFs, and collateral is not required. The performance of these lending programs is mixed. On the one hand, in many cases careful loan appraisal ensures that such lending assists poor households to escape poverty by enabling them to sustain a viable means of production using their own savings while at the same time repay their loans. However, there is also significant leakage of subsidized loans to the non-poor, including village leaders.
 - Except for large traders or shop owners, few rural producers keep savings account in banks or PCFs. This seeming lack of demand for bank deposit services in rural areas visited is caused by insufficient public confidence in banks, a shortage of cash in many rural households, and more importantly, (iii) farmers' lack of ready access to formal credit when needed, especially in times of emergency. To the extent that savings are possible, rural households therefore prefer to invest in immediately disposable assets such as buffalos and jewelry, or to lend savings to others.

Two main implications arise from this analysis. First, on the demand side, while the coverage of financial services is quite widespread, formal institutions cover not all types of credit needs. As a consequence, poor rural farmers and small-scale service and processing enterprises in particular are exposed to high-cost lending from moneylenders, and it appears that there is a significant rise in the level of debt in resource poor households and enterprises. *There is therefore a need to increase the access to formal loans to ethnic minority, poor households and small enterprises, particularly in remote areas.* Moreover, it is difficult to obtain longer term financing for production investments requiring a financial cycle than 3 years, which restricts upward mobility for small-scale producers and enterprises.

Secondly, on the supply side, the reliance on subsidized lending to the poor results in inefficiencies with regard to the outreach and coverage of financial services, poses challenges to the longer-term viability of major policy lending institutions, and distorts the market for financial services. In the Vietnamese context, aside from the leakage of subsidized loans to the non-poor, the following two issues are of concern:

- Subsidized loans provided by VBSP are capped by the Government at highly subsidized interest rates of 0.45–0.50% per month, compared with 1.15% per month by AgriBank and 1.35% by PCFs. This regulation hurt VBSP's incentive to mobilize deposits, as interest rates for deposits are higher than the subsidized lending rates. Furthermore, while the Government funds interest subsidies, reimbursement from the GoV to lenders is reportedly slow, and this has probably reduced the incentive of policy lenders to expand lending in remote areas. This suggests that interest subsidies hurt the sustainability of financial institutions and, therefore, in the long run hurt borrowers by reducing the incentive and capacity of financial institutions to expand the supply of credit to the poor.
- As the key government vehicle to channel subsidized credit for policy purposes, VBSP is fully guaranteed by the Government, and exempt from taxes, state budget remittances, and the deposit insurance scheme²¹. Such subsidized lending provide clear disincentives for other commercial banks to devise lending programs targeting rural populations, as these may not be able to compete head-one with such subsidized operations, resulting in the poor, ethnic minorities and small-scale rural enterprises having less choice. In the long-term, creating a competitive playing field

²¹ Hansen 2008

among multiple financial service providers is desirable in order to increase service quality, efficiency and sustainability.

International experience shows that poor people are willing to pay commercial interest rates, their priority being easy and rapid access to credit rather than low interest rates. This, along with the systemic implications for the viability of financing institutions and for maintaining a competitive market for financial service provision, suggests that interest subsidies are unnecessary and maybe even harmful, at least in the long run. To encourage savings mobilization and provide incentives to expand and sustain lending to the poor, *it may therefore be better if AgriBank and VBSP were allowed to lend to poor borrowers on a commercial basis, charging interest rates high enough to cover their operational costs and lending risk.* If any need exists to subsidize poor borrowers, interest coupons could be issued by the Government and distributed directly to those for whom an interest subsidy may be justified.

Abolishing subsidized lending would ensure that lending risks are put on the lending institutions rather than the GoV. This in turn would provide incentives for better loan appraisal, limit the exposure of scarce GoV funds to losses on guaranteed loans and consequently leverage limited GoV resources into larger banking resources for the poor. On the borrowers' side, not having the choice of servicing subsidized loans before commercial ones would help to improve repayment of commercial loans. Allowing banks to lend to the poor on a commercial basis may therefore sustain poor people's access to formal credit in the long term, as it would provide incentives for both lenders and borrowers to improve performance and hence reduce the risk of lending to the poor.

In the context of the increasing commercialization and market exposure of Vietnamese rural producers, there is finally an emerging need for increasingly sophisticated and broader financial services, especially from small enterprises, large farm holders, cooperatives and households with family members having migrated for off-farm employment. Clients now not only need loans but also other financial products, such as leasing finance and remittance. *An appropriate legal framework for regulation of the financial service provision sector, fair competition for commercial banks, and entry of other types of financial institutions to enter the market and diversify their services is therefore necessary.* For small farm holders, the poor and ethnic minority, the GoV finally still needs to play a more progressive role in providing an enabling setting for banks and financial institutions to provide quality and competitive financial services on a commercial basis.

THE CASE OF RURAL WATER SUPPLY AND SANITATION

The case of rural water supply and sanitation

The National Target Program on Rural Water Supply and Sanitation Phase II (NTP II) is the main instrument for service delivery in RWSS. The program aims to ensure that 85% of the rural population has access to hygienic water, 70% have hygienic latrines, and that all rural schools, health clinics and other rural institutions have clean water and hygienic latrines by 2010. In addition, the GoV's programs P135 II and P 134 provide RWSS services in remote ethnic minority areas. The NTP II is jointly administered by the Ministry of Agriculture and Rural Development (MARD), Ministry of Health (MoH) and Ministry of Education and Training (MoET) and affiliated local level agencies. The key agencies responsible for RWSS service provision under NTP II are the MARD Standing Office (SO) and the National Center for Rural Water Supply and Sanitation (CERWASS) and its provincial and district level agencies, which are primarily focused on construction related aspects of RWSS implementation.

Coverage and relevance of services and delivery modalities: RWSS services provided under the three programs cover districts nation-wide. Under the NTP II, the previous unilateral focus on piped water supply in several, but not all, provinces has replaced by a promotion of a mix of water supply technologies. However, the preferred construction designs generally emphasize the more heavy construction designs as the payments of companies responsible for the design of facilities (often companies associated with provincial and district RWSS authorities) are based on the total value of the subsequent infrastructure works. The incentive to opt for lighter designs that can more easily be implemented directly by communities or small-scale local companies is therefore limited. The quality of water supply schemes is often less than optimal due to incentive systems that reward activity completion over quality, and barriers to effective quality control by benefiting communities.

Due to institutional barriers to cohesive intervention planning between the SO, MoH and MoET, the coordination between infrastructure construction (primarily CERWASS) and the provision of related health and hygiene awareness-raising inputs (joint responsibility of the three agencies) is insufficient. The NTP II's relative emphasis on sanitation, which is characterized by a limited construction element (latrines) and a higher element of awareness-raising and information support, has, for the same reasons, been limited.

Due to the infrastructure-driven approach to RWSS, the emphasis on establishment and mainstreaming of mechanisms for operation and maintenance (O&M), including allocation of adequate budget provisions for this purpose, is generally not sufficient to ensure sustainable O&M of RWSS schemes. The actual coverage of well-functioning schemes that fulfill norms for water quality set by the MoH is therefore substantively less than the official coverage figures, which are based on the number of schemes constructed rather than the number of functional schemes. Due to the logistical, financial and other barriers to construction and O&M in remote mountain areas, the coverage in terms of scheme construction as well as functioning schemes for ethnic minorities and other poor groups of is significantly less than the national average.

Farmers' participation and influence over infrastructure decisions: Currently, communities mainly participate in RWSS implementation through provision of labor inputs to scheme construction. To increase sustainability of investments, communities need to influence decision making in all aspects of the project cycle, including decisions about investment identification, technical choice, financial and other types of contributions to investments, supervision of construction, and management of assets after construction. This involves developing processes that are practical and sustainable, and ensures poor and non-poor groups access to RWSS.

There is therefore an urgent need to create the conditions for communities to increase participation in local decisions and make more informed choices about investments in RWSS and the services they require. In this way, households can select water supply and sanitation options that most effectively respond to factors such as their socio-economic situation and available water resources. As a result people would be more proactive in

selecting RWSS investments, and the targeting of ethnic minorities and the poor would be improved. To achieve this objective, communities need improved access to information about RWSS issues such as low cost technologies, O&M, management models before the selection of priorities for inclusion in the commune SEDP.

Local authorities supports the creation of Water User Groups or cooperatives as a means to manage the provision of community labor inputs to construction and as a framework for O&M, including collection of user fees. However, the capacity and inclination of local authorities to genuinely support community organization efforts is limited, particularly in the case of remote areas with logistical and social barriers, and the sustainability of these efforts is therefore questionable. Although there are many models of good practice on community participation available, in particular from donor-assisted and INGO projects, these models have not been mainstreamed into the system in most provinces, and levels of participation in RWSS therefore remain poor.

A key principle in RWSS implementation is commune ownership of investments. However, in most provinces, aside from very small and technologically simple investments, districts are still the project owner of RWSS investments, which limits demand-responsiveness of service delivery.

Engagement of non-state providers: While it is a stated policy goal of the GoV to increase private sector involvement in RWSS, the regulatory environment is not conducive for such involvement. According to prevailing regulations, public agencies at the provincial, district and commune levels are the primary project holders of RWSS infrastructure projects. The role of private sector agents is therefore limited to provision of construction inputs under competitive contracts with local authorities, while universities, associations, centers and similar agents are contracted for information and awareness-raising activities. It is difficult to attract qualified private companies to bid for RWSS construction and maintenance contracts due to the relatively limited size of these contracts, particularly in remote areas with logistical social barriers to effective implementation, and due to the predominant position of state-owned contractors in many localities. Some institutional models for O&M involve contracting or establishment of companies or cooperatives for this purpose.

Subsidies and payment of services: Rural water supply investments are generally provided free of costs for users, aside from provision of labor and land inputs towards construction and payment of user fees towards O&M. The NTP II budget is VND 22,600 billion, of which public budgets are projected to account for 24% of expenditures; community contributions 36%, preferential loans 25%; and donors 15%. This distribution provides an indication of the proportion of financing expected from the users of RWSS services but based on experience from the NTP I it is unclear if the projected proportion of non-state investment is realistic. Subsidies for poor households and households in especially difficult communes are provided for water supply service delivery under the P 135 II.

The subsidy-based approach to RWSS investments often prompts local authorities and beneficiaries to welcome any investment in their area. The executing and implementing agencies also have an incentive to construct as many schemes as their budgets allow, irrespective of the worthiness and relevance of individual schemes. This, combined with the centrally defined design models and the supply-driven approach to scheme design and construction, results in less than optimal investment planning, high O&M costs that in most cases can not be covered by local fee collection, and little incentive for beneficiaries to take a proactive role in scheme planning, implementation and O&M. In addition, as illustrated above, the grant based nature of RWSS programming puts a heavy burden on public budgets.

To ensure that only truly worthy investments receives public support, a better alternative may be to make long-term loans available to private entities, individuals and beneficiary representatives for investments. Recent surveys suggests that rural producers and households, individually or collectively, are willing and able to infrastructure investments that bring them more benefits than costs, if they had access to long-term loans with low

interest²². Low interest credit for RWSS is actually available from the Vietnam Bank for Social Policy (VBSP). However, the implementation of this policy is uneven, with total loans in some provinces amounting up to 30 billion VND and in others only 2 billion VND, which far from meets the requirements of local constituencies. There is also a lack of coordination between the bank and IEC service providers responsible for raising local demand for RWSS services. *There is consequently a significant need to explore the options for strengthening systems for credit-based RWSS delivery.*

²² ADB 2006b, p. 21.

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