



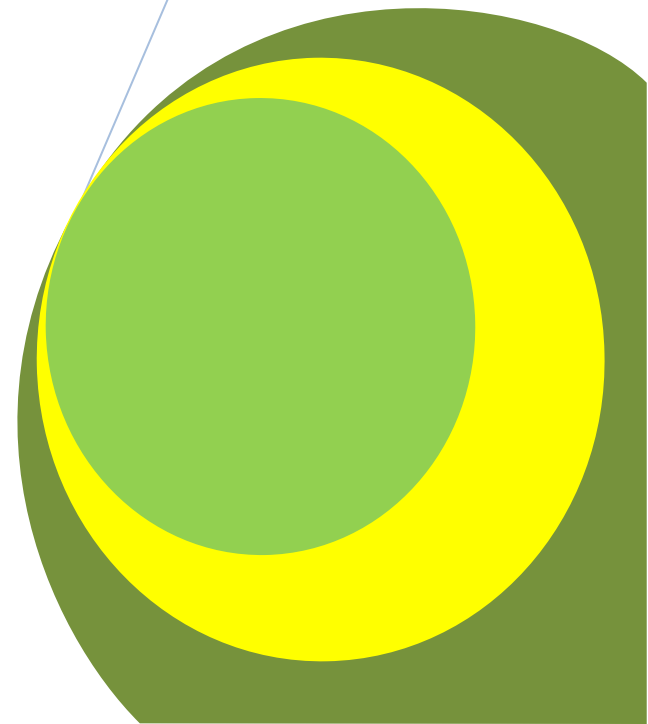
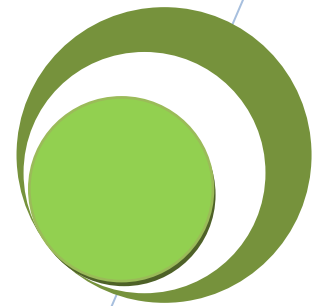
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## **Strengthening Rural Investment Climate and the Government's Effort in Northern Vietnam**

By

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*Research Article*

# Strengthening Rural Investment Climate and the Government's Effort in Northern Vietnam

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**ABSTRACT**

As many countries in the world, Vietnam is on ways to improve its investment climate from the perspective of investors. This paper aims to assess rural investment climate and analyze the Government's effort to strengthen rural investment climate in Northern Vietnam. Data used for the research was collected from a survey with 200 agro-enterprises in the North of Vietnam and statistical analysis was used to identify constraints of rural investment climate and analyze significant effects of the policy initiated by the Government to remove these constraints. As positive citing of the agro-enterprises, the Government's efforts have largely contributed to improve rural investment climate in Northern Vietnam. The analytical results showed that some constraints are believed to have positive changes such as rural infrastructure, taxation, administrative procedures, workforce and legal environment whilst other obstacles which include access to credit, access to land and macro uncertainty are emerging as the biggest obstacles for enterprises to perform their business activities. Finally, the paper expresses some policy implications that may significantly contribute to remove the obstacles of rural investment climate in Northern parts of Vietnam.

**Keywords:** Rural investment climate, Constraint, Strengthening, Northern vietnam.

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**INTRODUCTION**

In a developing country, the success of agriculture depends mainly on expanding the rural economy which in turn depends essentially on the viability, profitability and sustainability of rural enterprises (World Bank, 2008). In Vietnam, the rural area is large within living of 69.4% of population and about 48% of labor force involve in agricultural sector (GSO, 2012). In addition, rural areas of Vietnam exhibit a richly varied pattern of activities. Despite rural economy involves non-farm entrepreneurs, agro-enterprises and many households, of course, continuously derive their livelihood from farming. It hence understands well factors of rural investment climate will help firm taking advantage of business operations better.

In recent years, the Vietnam government has made significant efforts to improve the investment climate and has achieved encouraging results. Although Vietnam was only at number 99 of 155 countries in the 2005 doing business rankings, it is one of the ten most powerful reform countries (IFC and VCCI, 2005). Reforms in business registration, launch new bankruptcy law, using reasonable method of implementation of the contract and reduce costs of asset register are notable examples. Many foreign investors have appreciated the policies to improve investment climate in Vietnam which is creating a legal framework for equality and justice among all economic sectors, regardless of either foreign investment or domestic investment, includes state-owned economic sectors (Alain Cany, 2005). Vietnam's effort in improving investment climate has been recognized with stand at 98<sup>th</sup> in the ranking of 183 countries on Doing Business (World Bank and IFC, 2012).

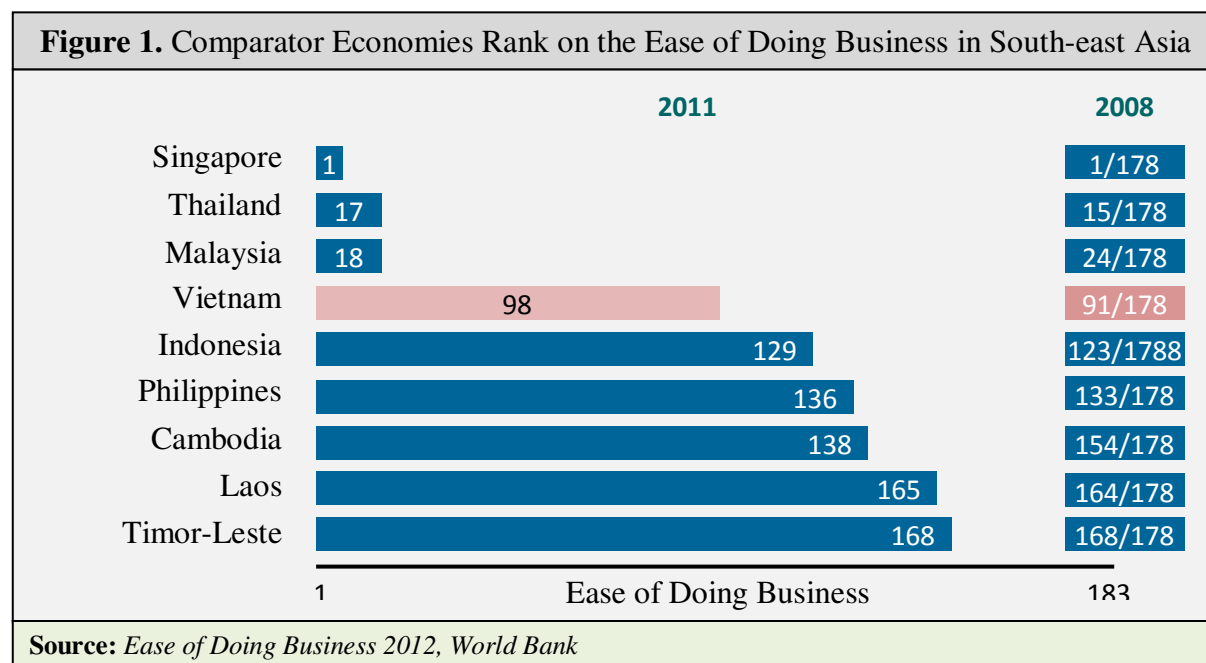
Nevertheless, investment climate in Vietnam still remains quite inflexible with poor infrastructure, complex tax framework with myriad of law, decrees, circulars and official guidance and many different tax rates, cumbersome administrative procedures and high level of uncertainty (Dzung et.al, 2005; World Bank & IFC, 2012). This is especially noticeable in rural areas. Evidence for this, investment on agriculture is not appropriate, its contribution within 20.3% of gross domestic product (GDP), only 6.5% from state budgets and around 5.6% of total foreign direct investment (FDI) during the period of 2000-2010. Furthermore, Vietnam has no control system of investment balance between urban and rural areas. The rate of registered enterprises yearly established in rural areas (9.5%) was much lower than urban (17%) during the period of 2005-2010 (GSO, 2012). In fact, there are not many companies that

showed their keenness with investing on agriculture and rural areas. Although the government has made important strides toward creating an enabling rural investment climate, but much more remains to be done, particularly in simplifying the tax regime with naturally complex procedure for issuing business licenses and operating permits, removing cumbersome administrative procedures, improving infrastructure and reducing uncertainty.

This paper aims to assess rural investment climate and analyze the Government's effort to strengthen rural investment climate in Northern Vietnam. Methodologically, statistical analysis is used to identify the factors of rural investment climate which are considered as obstacles for firm doing business and investment; and analyze the Government's efforts to strengthen investment climate in rural areas. Data using for the research is collected from a survey with 200 agro-enterprises in Northern Vietnam. The sample was explicitly stratified by region, type of firm and business line. In every region, enterprises were selected by systematic equal probability sampling from annually updated list of firms. Although the survey results obtained from agro-enterprises do not reflect all aspects of rural investment climate, but these firms' performance are cemented to rural areas. Secondary information was also collected from various sources during the research process.

## OVERVIEW OF STRENGTHENING INVESTMENT CLIMATE IN VIETNAM

Yearly, ranking on the ease of doing business among 183 economies in the world is done by World Bank and International Financial Corporation (IFC). The rankings for comparator economies provide other useful information for assessing how easy it is for entrepreneurs in Vietnam doing business. Although this tells only part of the story but it is worth considering when assessing the Government efforts to strengthening investment climate. Globally, Vietnam stands at 98 in the ranking of 183 economies on the ease of doing business in 2011 (World Bank & IFC, 2012). In Southeast Asia, Vietnam is ranked 4<sup>th</sup> after Singapore, Thailand and Malaysia. However, the gap between Vietnam and these countries are quite large, less than 80 grades. Although Vietnam was recognized as an emerging economy and the Government has made extensive efforts to diminish obstacles of investment climate faced by entrepreneurs, but this position does not seem to be improved in comparison with 2008 (see Figure 1). This implies that creating an enabling investment climate seems to be not really satisfy investors.



On the national level, yearly ranking of the ease of doing business among 64 provinces in whole country is done by Vietnam Chamber of Commerce and Industry (VCCI). Provincial Competitiveness Index (PCI) partially reflects the provincial investment climate. In fact, the provinces with high PCI usually have a high growth rate of foreign investment capital and industrialization rate is also higher (Tuan, 2011). Some provinces in the North of Vietnam have achieved great results in improving competitiveness to attract investment as Lao Cai, Bac Ninh, Ha Tinh, etc. (VCCI, 2012).

According to Dzung et.al (2005) had a preliminary assessment of the investment climate in rural Vietnam. The survey results indicated some major obstacles of rural investment climate notes as difficulty in access to land, considerable distinction between State-owned enterprises and private enterprises in the rural investment climate. The authors also recommended that the Government should focus primarily on improving the connectivity of the firms in rural areas with public services, improving the rural investment climate should be monitored at the provincial level.

Institute of Policy and Strategy for Agriculture and Rural Development – IPSARD (2005) argues that firms are subject to the impact and benefit from preferential policies, the improvement of the investment climate. Therefore, the development of the enterprise is considered as a result of the improved investment environment. Using data survey from General Statistics Office on the establishment of enterprises in rural areas during the period 2000-2005, IPSARD showed rural investment climate in Vietnam has improved dramatically in this period and this is explained by the progress made in the amendment of laws or such as the Enterprise Law, Investment Law, etc. Many foreign investors have appreciated the policies to improve investment climate in Vietnam, especially improvement of legal framework for equality and justice among all economic sectors (Alain Cany, 2005).

There are many different studies with very similar approach, mainly from the firm side to (i) collect, find out information about the effect of policies, laws, regulations issued, (ii) explore the difficulties of enterprises in the process of establishing, operating, and (iii) propose policies to support enterprise development.

Dzung et.al (2005) suggests that difficulties for firms in the city and outside the city are the issues of access to finance (with 25% of enterprise outside the city and 28% of overall enterprise said), transport (25% of enterprise said) and access to land (nearly 30% of enterprise said). Besides that, factors of policy uncertainty, tax, trade regulations, customs, etc. are also obstacles for firm to perform both cities and rural areas. However, the obstacles differ for each type of enterprise. For domestic companies, access to land and access to finance (with corresponding 28% and 31% of enterprises) are the main obstacles while transportation, power, macro instability, land access and corruption are the main obstacles for the foreign companies. The State-company said that access to finance, labor regulations, transportation, skilled worker are the major obstacles.

According to World Bank (2011), economic restructuring from agriculture into industry and services in recent years has led to dramatic changes in conversion of land use in Vietnam. Real estate became one of the hottest growth market and the most difficult to manage. Land laws and policies have evolved over time, serving as pragmatic solutions to merge socialist ideology on land ownership with the demands and pressures of an emerging modern market economy; and to redefine and refine the relationship between land users, investors and the State. Nevertheless, inadequacy in the legal framework of land is shown in that due to the lack of specific guidance on the process of determining the applicable land prices, each province offers different solutions. In the vast majority of cases, they have imposed an administrative decision, which is not in line with the market prices (World Bank, 2011a). Moreover, according to World Bank (2011), major shortcomings in the compensation rate have led to the delay of projects, pushing the infrastructure investment rate too high and slowing down the profitability of the projects. To solve this problem, the government has adopted a series of policies such as tax increases for non-agricultural land use, allowing accumulation of agricultural land through transfer of land use rights and doing some works towards overall planning of land. These efforts were initially effective to reduce the bubble nature of land market. Hopefully, the new Land Law will be quickly passed by Parliament and the government's efforts to control the land market will create positive change which is somewhat satisfied investors.

Regarding rural infrastructure, electricity in Vietnam presently much relies on hydropower while this source heavily depends on natural conditions. Although the government has made significant progress in expanding electricity networks across the country, improving power transmission system slowly causes un-foreknowable no electricity is one of the major reasons that lead to investors discourage. However, situation of sudden power interruption due to overload or failure of grids and rotating outages occur frequently (Thanh, 2010). In parallel with the situation of electricity system, transport infrastructure in Vietnam is also considered old and incomprehensive. This is worse in remote and mountainous areas. However, in recent years the government has made great efforts to develop transport infrastructure through investment by the state budget, official development assistance (ODA) capital and residential communities. By mid 2011, there were 8,944 communes in the whole country which automobile could connect to the headquarters of Commune People Committee (over 98.6% of total). This rate reached 94.2% in 2011 and 96.9% in 2006. In 2011, there were 8,813 of these communes (nearly 97.2%) which automobile could connect to the headquarters of Commune People Committee any time in a year while this rate was only 93.6% in 2006 (GSO, 2012a).

Similarly, the importance of taxation is usual in creating an enabling investment climate. In general, tax framework in Vietnam is very complex which causes enterprises' spending much more time in practice. As AmCHAM (2009) and Gangadha et.al (2011) have described, Vietnam's tax regime is contained in a myriad of law, decrees, circulars and official guidance and there is often no simple way of identifying those that are applied in practice.

As in many other developing countries, administrative procedures in Vietnam are cumbersome and inefficient (World Bank, 2011a). In few past recent years, both central and local governments have made extensive efforts to

improve administrative procedures from perspective of investors. Under the Government's Project 30 on simplifying public administrative procedures in various state management areas, the Prime Minister signed Resolution No.25/NQ-CP on simplifying 258 public administrative procedures of priority to create better conditions for business operation and growth in 2010 that related to tax and customs, notary issues, investment, construction and environment. Continuously, the Prime Minister had approved 24 other resolutions in the plan to simplify more than 5,000 procedures in all sectors by early 2011. These resolutions urge the simplification of certain regulations by making the administrative process transparent, reducing the number of application dossiers and clarifying the procedural sequences. For the ease of starting a business, in 2010, Vietnam eased company start-up by creating a one-stop shop that combines the processes for obtaining a business license and tax license and by eliminating the need for a seal for company licensing. Consequently, many foreign investors have voted for Vietnam instead of Thailand or Malaysia which created the most attractive investment climate in the region of Southeast Asia (World Bank & IFC, 2012).

Access to financial services is a considerable factor to strengthen investment climate. There is consensus in the empirical literature that there is a strong positive link between the functioning of the financial system and long-run economic growth (Oanh, 2012). Moreover, the literature also establishes that increased access to finance contributes to growth at the individual firm level (Trung and Itagaki, 2012; Trung and Cuong, 2010). Cuong et al. (2009) use agricultural firm survey data in Hanoi to find that firms that complain about their lack of access to finance actually have lower growth rates. In recent years, due to the impact of the global financial crisis and high inflation rate in the country continuously since 2009, has made access to credit services become more difficult.

In summary, infrastructure issues such as electricity, transportation and regulatory issues such as administrative procedure, business licenses and operating permits were likely cited as significant obstacles not because they are not efficient but because they are so poorly enforced that they do not have an impact on most enterprises. Likewise, customs formalities, commercial services, skills and educational workforce and especially legal environment are rarely considered. Enterprises have always used informal mechanism to resolve disputes. Thus, it is unlikely that many managers even understand the benefits of a strong and efficient legal system, in particularly those coming from small enterprises.

## METHODOLOGY AND DATA

Methodologically, statistical analysis is used to identify the obstacles of rural investment climate for firms doing business and investment in Northern Vietnam. In addition, statistical descriptive method is used in combination with a comparative analysis to clarify government's effort to remove these obstacles and the Chi-squared test was then used to make a reliable basis for discussing the government's efforts to improve rural investment climate in Northern Vietnam.

Data for the empirical analysis has been obtained from the agro-enterprise survey under the PhD program at Tokyo University of Agriculture (TUA) conducted by the authors. The agro-enterprise survey was carried out in 2011 with a sample of 200 agro-enterprises located in different business lines and regions across the North of Vietnam (see Table 1). The sample was explicitly stratified by region, type of firm, and business line. In every region, enterprises were selected by systematic equal probability sampling from annually updated list of firms.

**Table 1.** Sample Statistics for Agro-enterprise surveyed

Region	Agro-enterprise surveyed by sub-sector				Total
	Crops	Animal husbandry	Aquaculture	Forestry	
Red river delta	55	13	10	6	84
North-west	13	9	3	9	34
North-east	7	17	14	4	42
North central	15	8	12	5	40
Total	90	47	39	24	200

**Source:** Summarize from survey data 2011

The survey questionnaire has around 136 questions (with many questions further divided into parts) and contains information include (1) characteristics of agro-enterprise; (2) past economic activities of agro-enterprise involve productivity, sales, supplies, costs and profit; (3) agro-enterprise's investment; and (4) factors of rural investment climate where agro-enterprise operate embrace infrastructure, public services, regulations and permits, taxation, land

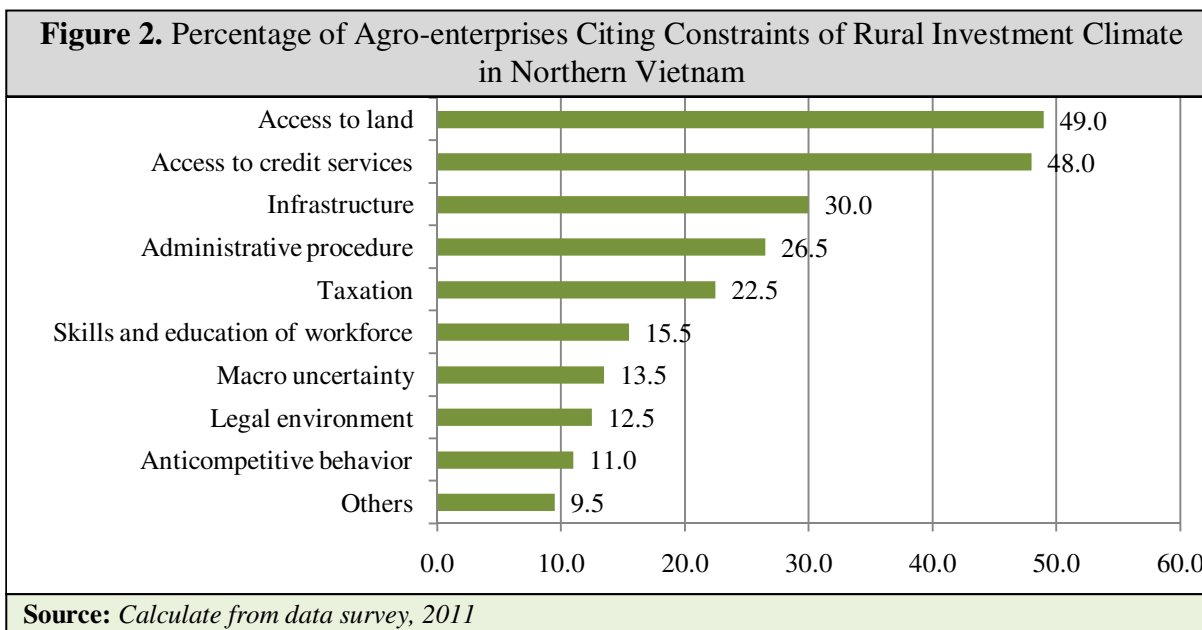
tenure security, competition as well as the respondent's perceptions about the rural investment climate constraints. Additional information related to the research problem was also collected from various agricultural institutions and local municipalities.

## STRENGTHENING RURAL INVESTMENT CLIMATE IN NORTHERN VIETNAM

### *Identification of Rural Investment Climate Constraints*

For assessment of rural investment climate as well as identifying its obstacles in Northern Vietnam, we carried out a two-hundred agro-enterprise survey based on selectively using sets of criterion<sup>3</sup> which strongly effect on firm doing business and investment. Summary results of the survey are presented in Figure 2.

Up to 49% of the agro-enterprises surveyed cited access to land as either a severe or major obstacle to doing business in Northern Vietnam. The results of surveys show that most of the respondents have problems in access to land, especially those wanting to significantly expand. The fact that access to land is perceived as such a significant problem in Vietnam even by existing firms indicates just how severe a constraint it is. Access to land was closely followed by access to credit service, which was cited by nearly 48% of the agro-enterprises surveyed. Infrastructure, administrative procedures and taxation were also mentioned as major constraints. The proportion of agro-enterprises surveyed cited infrastructure, administrative procedures and taxation as major obstacles and are 30.0%, 26.5% and 22.5%, respectively. At less severe level, some constraints such as skills and education of workforce, macro uncertainty, legal environment and anticompetitive behavior were cited by few agro-enterprises. There was 9.5% of respondents who said that remaining others such as technology, crime theft and disorder, etc. are considered as significant constraints.



The perceived obstacles are similar across all regions in Northern Vietnam, with only slight differences. Access to land and credit services are the issues most often cited as either severe or major constraints. However, their order is not the same among regions in Northern Vietnam. In the Red river delta, access to land was cited as often as access to credit service, possibly because of the large number of enterprises found in the Red river delta region. In North central and North-east regions, access to credit and infrastructure were the most often cited as severe constraints and access to land much less often cited, which may reflect the fact that most geographic area of these two regions are mountainous. In North-west region, business licenses and operating permits is cited more often than it is elsewhere, which could reflect deeply the situation of poor infrastructure. Moreover, it also indicates the bureaucracy of local authorities.

When agro-enterprises were asked to name the single biggest constraint, the rankings of access to land and credit service were reversed; nearly 26% of managers cited access to land as the biggest constraint and 19% of

them reported access to credit service. Whereas, there was 11% of the respondents said that infrastructure is one of the biggest constraint and few agro-enterprises reported taxation, skills and education of workforce, macro uncertainty, legal environment and anticompetitive behavior.

### **Understanding of the Major Rural Investment Climate Constraints**

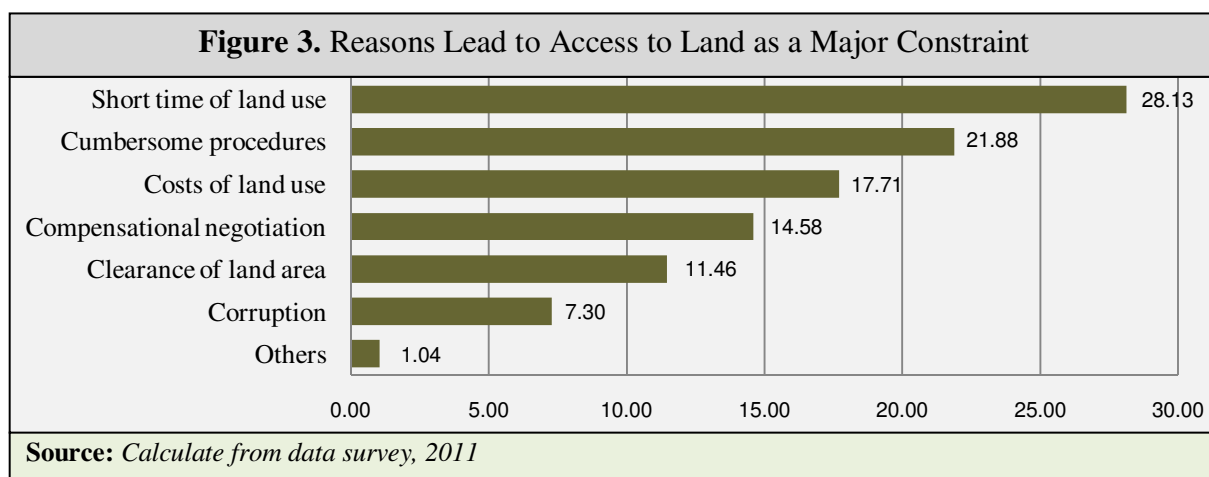
To understand the major obstacles of rural investment climate in Northern Vietnam, an analysis of reasons leading to each obstacle is necessary. This will not only clarify the causes of the obstacles but also learn lessons to overcome the obstacles of rural investment climate from the agro-enterprises surveyed. The analysis of the obstacles is also done following the ranking of the obstacles on the severe level that was cited by the agro-enterprises surveyed.

#### **Access to Land**

A nice finding of the World Bank (2011a) in Vietnam is access to land become easier in provinces with high provincial competitiveness index than other provinces. It seems that access to land is one of the most important criteria influenced on improving rural investment climate.

The analytical results mentioned above (section 3.1) show that access to land is really difficult for agro-enterprises to operate. Among the agro-enterprises surveyed cited access to land as a major, up to 28.13% reported the reason is mainly due to short time in land use and 21.88% complained about the cumbersome procedures in access to land. In term of land use costs, up to 17.71% of respondents said that this is the main reason leading to difficulty in access to land while 14.6% of them complained about the land price applied to calculate the compensation price is the main reason that caused access to land as a major constraint (Figure 3).

After finishing administrative procedures in access to land, enterprises have to negotiate with the households about land prices for calculation of compensation. In general, enterprises want to apply the price that is determined by the Government while households want to apply market price. Furthermore, an enterprise which needs to expand land area for building factory or planning material zone, has to negotiate with many households due to egalitarianism of land distribution for farmers in Vietnam.<sup>4</sup> Therefore, negotiating on price and ways of compensation between agro-enterprise and households is increasingly more complex (see Box 1). According to World Bank (2011a), in provinces with high levels of urbanization, the level of difficulty in access to land is also higher than other provinces. Uncompromising in compensation has led to many lawsuits which cause prolonged social instability and reduce the attractiveness of rural investment climate in Vietnam. Up to 11.6% of the agro-enterprises considered access to land as a major obstacle and said that the main reason is due to difficulties in land clearance while 7.3% of them reported corruption in land access is the main cause.



The small and medium-sized agro-enterprises have difficulties in access to land mainly due to cumbersome procedures, high cost of land use and short time in land rent. It should be noted that in order to quickly overcome the difficulties in access to land, a majority of these agro-enterprises have chosen to bribe officers with offers of money or gift. Up to 38.8% of the agro-enterprises which have difficulty in accessing land confirmed this. Unfortunately, all of them refused to provide evidences of the bribes. However, several large-scale agro-enterprises choose other solutions to overcome the difficulties in access to land. For example, Dong Giao Joint Stock Company has solved the

difficulty of compensation by creating jobs for members of the household who lost agricultural land for building the processing plant as employees of the company. Meanwhile, some other companies have overcome the difficulties in accessing land by signing the contract farming with farmers instead of land use right transfer when they expand their material zones such as Lam Son Sugarcane and Sugar Joint Stock Company (Thanh Hoa province), Lang Son Tobacco Company (Lang Son province).

In present, the Ministry of Natural Resources and Environment (MONRE) is on the process of developing the new Land Law to be submitted to the National Assembly for consideration and adoption in 2013. This new Land Law is expected to be basis for improving legal framework of land and more satisfy press demand from citizens and investors.

#### *Box 1. Voices of Enterprises: Waiting for Access to Land*

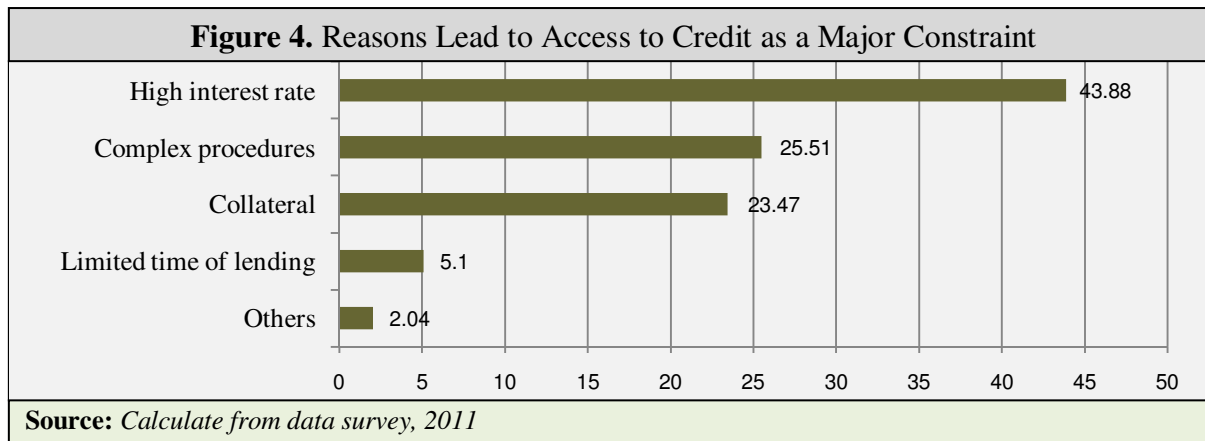
“Setting-up a project must be underlying the regional planning which is already popular. In the process of project implement, we have many difficulties in direct negotiation with households on land price applied and compensation. They pressurize us rising price through extending transfer land to us. In some cases, the clearance of land area only remain small part of the area, a part of less than households still expressed an uncooperative in compensation with land price applied presently. To ensure the progress of the project we have resigned concession to them. Of course, expenses of the project are added this extra part of compensation. This lead to arising of social injustice because the people who have previously agreed to transfer land suffer a loss and also causes socio-economic development stagnated.” – *The Director of a Fruit and vegetable processing company in Hanoi city.*

#### **Access to Credit Services**

In few recent years, Vietnam economy had to face difficult with high inflation rate maintaining between 17-23% per year. The government adopted a tight monetary policy that has been keeping it at high interest rate, over 20% per year. Therefore, enterprises have more difficulty to take a loan from credit organizations. Otherwise, higher inflation also lead to banks making more stringent requirements for lending conditions, mainly collateral value. This explains why 48% of total agro-enterprises surveyed cited they have many difficulties or can not take a loan from banks. Among the agro-enterprises which cited access to credit services as an obstacle, up to 43.9% considered high interest rate as the main reason while over 25.5% of the respondents said that the difficulty was mainly due to complex lending procedures (Figure 4). The severe lending conditions from the banks, mostly collateral value, is an important reason that caused more difficulty in access to credit services while 23.47% of agro-enterprises cited access to credit services as a major constraint. Further, the proportions of agro-enterprises report difficulty in access to credit services due to limited time in lending and other reasons are 5.1% and 2.0%, respectively.

Majority of the agro-enterprises have difficulty in access to credit services because they often have fewer assets to ensure collateral condition for taking a loan from credit institutions. Furthermore, the less transparency in the financial statements of these companies is also accounted as a big barrier in access to credit services. In addition, a not unusual situation in Vietnam is the inequality between state enterprises and private enterprises to be clearly reflected in access to credit services.





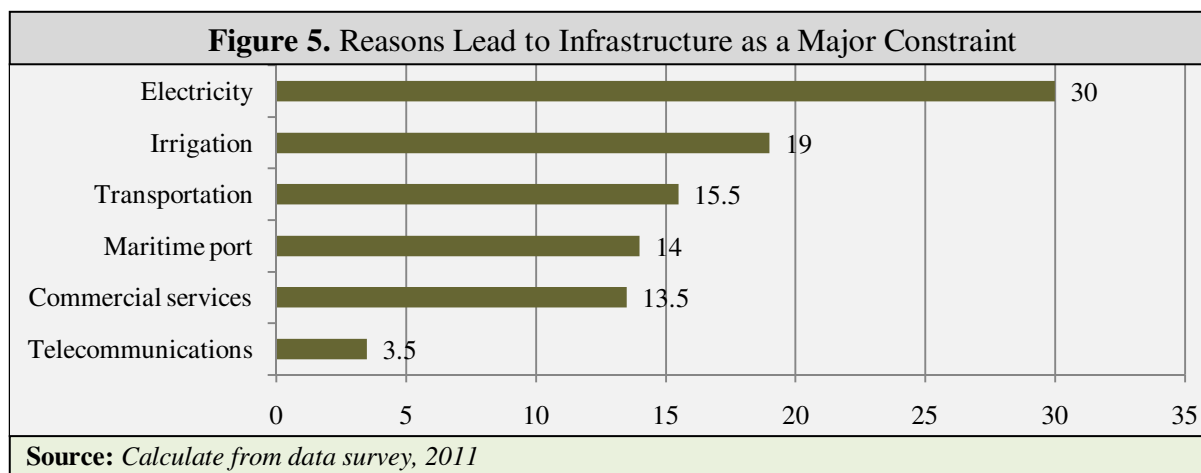
As the survey results, most of agro-enterprises faced difficulties in accessing credit under private sector. This can be explained that a majority of formal credit institutions in rural areas is under state ownership and these credit institutions seemed more priority in providing credit services to the State companies. Meanwhile, the formal credit institutions owned by private sector are only deployed in the form of branches in some rural areas with high levels of industrialization. Thus, it is considered as a big barrier for agro-enterprises access to credit services in rural areas of Northern Vietnam, especially for small and medium sized agro-enterprises in the non-state sector. Consequently, most of these agro-enterprises had to ask informal credit organizations and individuals about the loans with high interest rate. This seems to be an evidence of failure to create an enabling rural investment climate in Northern Vietnam.

### **Infrastructure**

The survey data shows that among the reasons caused, infrastructure was cited as a major obstacle by the agro-enterprises for their decision to invest, the power shortage is most severe. Up to 30% of total respondents who cited infrastructure as a major obstacle have recognized this as a main reason (Figure 5). To deal with this situation, 69% of agro-enterprises surveyed had bought at least one generator.

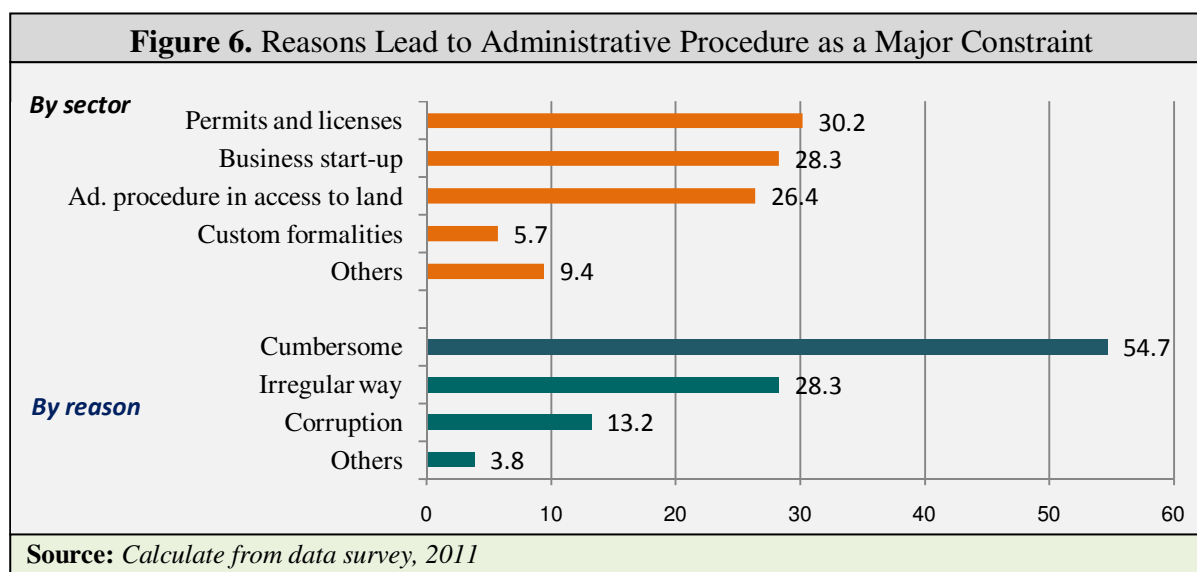
As results of the survey, a quite high proportion of the agro-enterprises cited infrastructure as an obstacle of rural investment climate, (19%) reported that degradation of irrigation system is major cause while 15% and 14% of them blamed the poor transport system in rural areas and the weakness of maritime port respectively. However, this statistic may reflect the limited horizons of agro-enterprises which are mainly small and medium sizes and their businesses operate mostly within a local economy. It means that they may find the poor transport infrastructure adequate for their needs. Noting that when asked about the factors constraining ability to trade, a larger proportion of the agro-enterprises (40%) identified lack of highways, traffic jams and transport costs as major causes.

The weakness of commercial services such as consulting, brokerage, etc. is also a noticeable cause to make agro-enterprises considered infrastructure as a challenge when they decided to invest while 13.5% of them said that this reflects true. However, most of these agro-enterprises are large-scale business or their operations related to import and export. The commercial services that they mostly complained are international legal consultancy, asset valuation and entrusted export-import services. To overcome, these agro-enterprises ask normally foreign reputable organizations for solving these problems businesses typically hire abroad.



### Administrative Procedures

As shown survey data in Figure 6, the inadequacies of administrative procedures are mainly in permits and licenses, business start - up and administrative procedures in access to land . Among agro - enterprises surveyed cited administrative procedures as a major constraint of rural investment climate, the proportions of the agro-enterprises confirmed these as 30.2%, 28.3% and 26.4% respectively. In addition, up to 7.5% of respondents said that the complications of administrative procedures were mainly due to custom formalities whereas while 9.4% of them reported cumbersomeness of the administrative procedures coming from other areas such as taxation, transportation, etc.

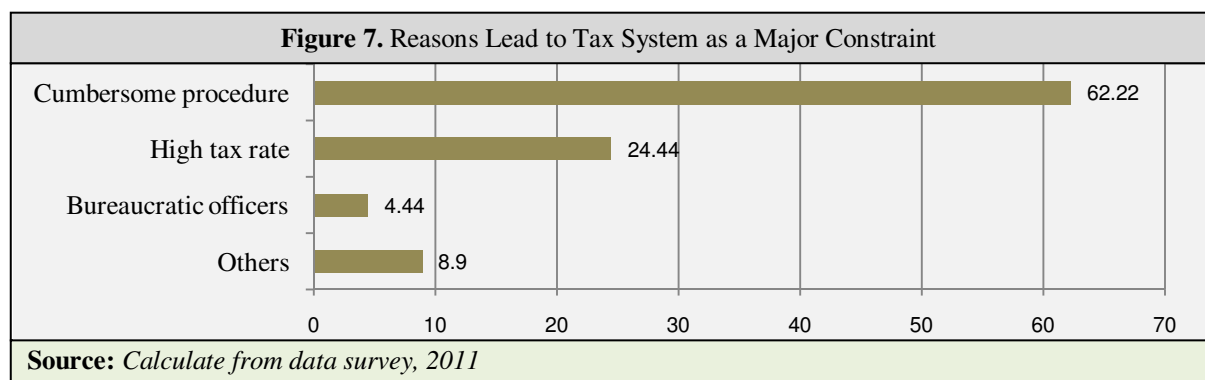


The data in figure 6 also showed that the main reason leading to the agro-enterprises' anxiousness about administrative procedure is cumbersome with 54.7% of the agro-enterprises cited administrative procedures as a major constraint voted. Whereas, up to 28.3% of them complained about complications of administrative processes and the lack of coordination and standardization among agencies in the process of issuing licenses and permits. Agencies often require different formats or content for what is essentially the same information, requiring applicants to prepare separate documents with minor variations and decreasing the comparability of application files among departments and agencies. In addition, 13.2% of the agro-enterprises which denote their despair of administrative procedures reported the major cause is due to corruption in the administrative offices while 3.8% of them said that

due to other causes such as officers' bureaucracy. As survey results, an agro-enterprise takes nearly 60 days to deal with issues related to administrative procedures each year in average. This long waiting may be an underlying major reason which caused bribery and the fact that many companies have overcome this obstacle by doing that. Some other companies had to give up and look for other investment options in other provinces or other countries.

### **Taxation**

In present, the tax system in Vietnam is said to be complex with myriad of law, decrees, circulars and official guidance and many different tax rates. The survey data shows that among agro-enterprises accounted tax as a major handicap for their businesses, up to 62.2% responded that difficulties come from the complexity of tax procedures (Figure 7). As survey results, spending nearly 1,000 hours per year to ensure compliance with the procedures and regulations related to tax is possible cause of bribes in order to reduce waiting time. A majority of agro-enterprise cited taxation as a major obstacle (24.4%) complained the current tax rates are too high for them to operate, especially the rate of corporate income tax. Only a few agro-enterprises (4.4%) reported that officers' bureaucracy is main reason leading to taxation considered as a major constraint while 8.9% of the agro-enterprises believe that inadequacy of taxation is due to other causes.



### **Other Constraints**

As shown in Figure 2, the remaining obstacles of rural investment climate including skills and education of workforce, macro uncertainty, legal environment and anticompetitive behavior also somewhat affect agro-enterprise's decisions in business, particularly investment decisions. The main reason for the agro-enterprises to complain about skills and education of workforce is shortage of workers trained in marketing and agricultural techniques. In fact, majority of graduate students are eager to look for work in big cities that is considered better than the jobs in rural areas.

The process of economic reform known as "Doi Moi" in Vietnam has resulted to a reasonable level of macro-economic stability through past twenty years. However, evidences of macro uncertainty in recent years such as weakness of monetary policy, slow economic growth, and high rate of inflation have seriously affected firm's business activities in general and business activities of agro-enterprise in particular. Consequently, the proportion of the agro-enterprises cited macro uncertainty as one of the biggest obstacles of rural investment climate is 15% (see Figure 2).

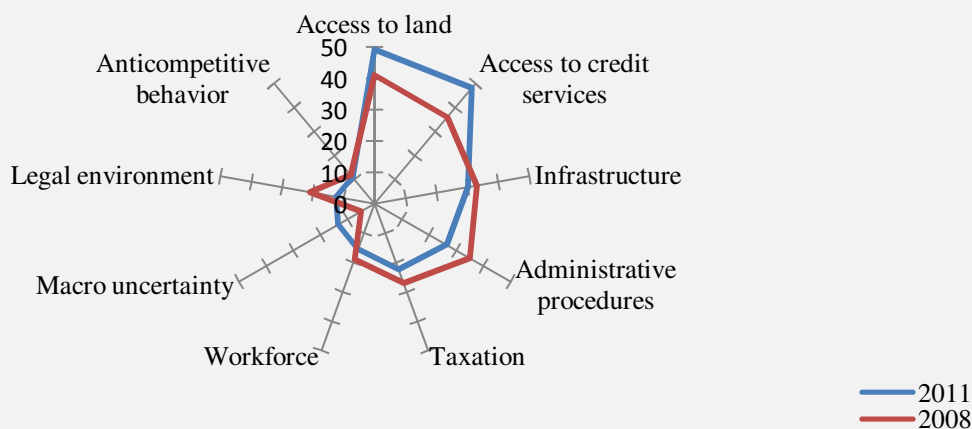
Finally, legal environment and anticompetitive behavior are also what made agro-enterprises not to feel secure about their investment, especially foreign investors. Evidence for this argument is 12.5% of the agro-enterprises surveyed reported that they have not enough confidence to invest in the context of current legal environment while 11% of them considered anticompetitive behavior as the biggest constraint for their businesses (see Figure 2). The weakness and inefficiency of legal system are considered to be the main cause of incomplete legal environment and the unfair treatment between state enterprises and private enterprises are considered as one of the biggest reasons that impede market participants.

### **The Government's Effort to Strengthen Rural Investment Climate**

In the context of the economy is difficult, the investment climate in Vietnam should be strongly and decisively improved, especially in rural areas. That is the biggest support from the government for enterprises to perform their businesses. The results generated from the survey with 200 agro-enterprises in 2011 have somewhat shown the

Government's efforts to create an enabling rural investment climate in Northern Vietnam. As shown in Figure 8, it has a positive sign of the Government's efforts to strengthening rural investment climate in Northern Vietnam under recognitions of the agro-enterprises that was tested. To understand clearly the Government's efforts to strengthening rural investment climate, it is better to analyze the government's effort to eliminate by constraints of rural investment climate. Accordingly, the government's efforts will be analyzed following the ranking on the severity of the constraints.

**Figure 8.** Constraints of Rural Investment Climate in the Period of 2008-2011



Source: Calculate from data survey, 2011

### Improvement of Rural Infrastructure

Proportion of agro-enterprises surveyed considered rural infrastructure as a major obstacle of rural investment climate in 2011 decreased compared to 2008, from 33% to 30% (see Figure 8). This result from the Government's efforts to improve rural infrastructure were recognized in recent past years. Some infrastructure items primarily for business operation and residents in rural areas such as power grids, transport roads, telecommunications, etc. have been many significant improvements that contribute to create an enabling rural investment climate in Northern Vietnam.

In average, agro-enterprise had no electricity with 31.2 days and faced to 34.7 times of sudden power interruption in 2008. In the North Central and Northwest regions, these figures are much higher, 47 days and 51 times respectively. This situation has improved somewhat in 2010 when the number of days in rotating outages was 25.0 days and the number of sudden power interruption was 30.2 times a year (see Table 2). This achievement could be attributed to the Government's efforts to transfer management of the grid from the agricultural cooperatives to the branch of electricity at district level.<sup>5</sup>

**Table 2.** Improvement of Infrastructure and Public Services in Rural Area of Northern Vietnam

Obstacle	Item	2008	2010	$\chi^2$ test
Electricity	Number of day to get a new electricity connection	4.62	4.19	NS
	Costs of electricity (000VND/kw)	1.78	1.86	---
	Number of day face with outage in a year	31.2	25.0	**
	Time of sudden power interruption	34.7	30.2	---
	Lose of revenue from outage annually (mil.VND)	128.3	117.1	NS
Transportation	Number of day merchandize delivery in domestic destinations delayed in a year	16.1	15.6	*
	Lose of revenue from merchandize delivery in domestic destinations delayed annually (mil.VND)	23.9	31.4	NS
	Ratio of transport costs to market value of products in average (in percent)	2.18	1.87	---

Telecommunication	Number of day to get a new landline/ mobile phone/ internet connection	1.62	1.21	***
	Number of day face with back-out of telecom connection problems in a year	9.74	5.34	***
	Lose of revenue from telecom connection problem (mil.VND)	13.9	11.8	NS

**Notes:** \*, \*\*, \*\*\* significant at 10%, 5% and 1% levels, respectively; <sup>NS</sup> no significant

**Source:** Calculate from data survey, 2011

Despite the significant improvement of power supply capacity as well as to reduce sudden power interruption, electricity service is still considered as one of the biggest challenge for business operations in rural areas of Northern Vietnam. Most of the enterprises surveyed said that the main cause of delayed infrastructure improvements of the power sector comes from Vietnam Electricity Corporation (EVN), a state company, holding a dominant role in this sector. Early opening of the Son La hydroelectric power plant (2.400MW) to synchronize the national grid and setting up plan to build a series of hydro and thermal power plants are the praiseworthy Government's efforts to satisfy the need of existing power for the enterprise and residents. In parallel with the enhanced power output, the Government is promoting the projects of grid improvement by calling investment from state budget, JICA, WB, ADB in order to improve quality of electricity service. Nonetheless, there is still a long way to go in rehabilitating the grid system and completing its segments including the remaining "ring" connection in Northern Vietnam, especially North-west and North central regions.

The Government's efforts to improve rural transportation system have been widely recognized in recent years. As survey data shown in Table 2, number of day merchandize delivery in domestic destinations delayed in 2010 decreased 0.5 days compared with 2008. Consequently, the ratio of transport costs to market value of products reduced 0.31 percent (from 2.18 in 2008 to 1.87 in 2010). This can be explained that the Government to improve rural transportation by foreign loans and other partial mobilization of financial resources from the people. The results of the Government's efforts to improve rural roads are thought to reduce transportation costs for agro-enterprises is limited partly due to fuel price increase in the period 2008-2010, from 15,000 VND/liter in 2008 to 19,500 VND per liter in 2010. Nevertheless, the slow progress of implementation in several key projects has made these efforts with point reduction in assessment of enterprises. That fact makes the rural transport infrastructure already weak as shown shortcomings, does not meet the requirements of economic development. Except the Nation Highway 6 linking Hanoi to Son La where is considered as the capital of Northwest region has been completed and allows connection to many places in the region and large vehicles can operate, some major roads have started many years ago but not yet finalized. For example, the National Highway No.3 linking Hanoi to Thai Nguyen where there is an industrial center and is the largest area of tea production in the country, the National Highway No.2 connecting Hanoi and northern mountainous provinces such as Phu Tho, Yen Bai and Lao Cai is important lifeline to promote trade with China in which agri-products are the strength of Vietnam. Rural transport infrastructure is becoming big obsession for investors and this could grow if the government's efforts are not really aggressive. As survey results, majority of the agro-enterprises surveyed said that rural infrastructure, in general, had made progress but most of them reported that is nothing progressive about transportation infrastructure, even worse than before.

In addition, the survey data shows that all agro-enterprises surveyed use at least one telephone or a fax machine and the managers of these companies are using mobile phones. The proportion of agro - enterprises surveyed using the internet was 67% and this proportion is the highest in Red river delta, accounted 89.3%. In present, internet has come to be one of the most efficient ways for enterprises to communicate and to conduct business with distant clients. Moreover, quality of telecom services is increasingly improved in rural areas of Northern Vietnam. As survey data shown in Table 2, number of day to get a new landline/ mobile phone/ internet connection and number of day face with back-out of telecom connection problems in 2010 reduced 0.41 and 4.4 days compared 2008 respectively. Breaking previously the monopoly of Vietnam Posts and Telecommunication Group (VNPT) has contributed largely to the positive change of the telecommunication industry.<sup>6</sup>

### ***Simplification of Administrative Procedures related to Business***

The results from the government's efforts to simplify administrative procedures have also been recognized. The evidences for this achievement is the proportion of agro-enterprise surveyed cited administrative procedures as a major obstacle of rural investment climate has decreased from 35% in 2008 to 26.5% in 2011 (see Figure 8). In average, the number of days that agro-enterprise takes to deal with administrative procedures has also decreased from 71 days in 2008 to less than 60 days in 2011. In terms of the ease of starting a business, Vietnam eased company start-up by creating a one-stop shop that combines the processes for obtaining a business license and tax

license and by eliminating the need for a seal for company licensing in 2010. This led to reduced number of procedures from 11 in 2008 to 9 in 2011 and less than 5 days for compliance of starting a business (see Table 1). Further, the costs of starting a business also decreased nearly one third compared with these in 2008. This positive change is cited by over 53% of total agro-enterprises surveyed. However, many respondents (nearly 73%) said that the waiting time in a month and half is too long to complete procedures of a starting business. As shown in Table 3, to deal with construction permits requires averagely 8.09 procedures, 161.1 days for waiting time and costs of 27.26 million VND in 2008. Up to 68% of total agro-enterprises reported that there is a large improvement in dealing with construction permits. This large improvement is due to the government made dealing with construction permits easier by reducing the cost to register newly completed buildings by 50% and transferring the authority to register buildings from local authorities to the Department of National Resources and Environment in 2010. Results of other research from World Bank (2011) also affirm this finding. However, many enterprises (nearly 43%) said that they are not satisfied with the present regulations of issuing construction permits because of a long time waiting and more complex procedures. Thus, improvement of regulations issuing construction permits should be one of the priorities and ensures that standards are met while making compliance easy and accessible to all.

**Table 3.** Regulations and Permits for Agro-enterprise Operate in Northern Vietnam

Items	Procedure (number)			Time (days)			Costs (mil. VND)		
	2008	2010	$\chi^2$ test	2008	2010	$\chi^2$ test	2008	2010	$\chi^2$ test
Starting a business	11.12	8.86	***	51.2	46.0	***	3.54	2.52	***
Construction permit	8.09	7.94	**	161.1	156.8	**	27.26	23.40	**
Import	8.03	8.15	NS	26.1	23.0	***	10.55 <sup>a</sup>	14.37 <sup>a</sup>	NS
Export	6.07	6.24	*	28.2	25.3	***	8.41 <sup>b</sup>	11.50 <sup>b</sup>	**

**Notes:** <sup>a</sup> or <sup>b</sup> is import/export costs per container  
 \*, \*\*, \*\*\* significant at 10%, 5% and 1% levels, respectively; NS no significant

**Source:** Calculate from data survey, 2011

According to data collected by the survey in 2011, although the number of days to compliance custom formalities for export was less than 3 days than in 2008 but the costs increased dramatically, more than 3 million per container while the number of customs formalities have no change. Similarly, waiting time to compliance custom formalities for import was down 2 days but the costs increased around 3.8 million VND per container in comparison with 2008. Up to 46% of the respondents said that import and export procedures have been improved but not so much. As understanding clearly, the Government has introduced tools to facilitate trade, including one-stop shop, risk-based inspections and electronic data interchange systems. In 2009, the application of new customs administration procedures as part of the World Trade Organization (WTO) membership reform program has partly reduced trade delays. These changes help improve the trading environment and boost firms' international competitiveness. Nonetheless, these efforts are not enough to satisfy agro-enterprises when over 36.5% of them engaged in import and export are not satisfied with the current customs formalities, especially procedure for customs drawback.

In summary, the positive change in simplifying administrative procedures related to firm's business activities is mostly recognized by domestic enterprises but this is still despair of the majority of foreign investors. Regulations and permits for operating are also improved when there are 36% of total surveyed enterprises that cited this positive change. Notably, a resolution stating hundreds of administrative procedures needed to cut was issued in 2012 which expressed the government's determination and commitment to strengthening investment climate, especially in rural areas.

### **Improvement of Tax System**

As mentioned in Figure 7, the complex and inefficient tax system in Northern Vietnam is mainly due to the tax administrative procedures. In recent years, the government has made efforts to reform the tax regime toward more efficient and equitable in order to attract investment and promote economic development, especially in rural areas. In 2010, the government started to apply electronic tax. Under the new way, enterprises would report to tax authority through online software instead of taking time to apply tax documents at the tax authority as before. As the data survey, enterprises can reduce 112 hours of time per year for applying tax documents to tax authority in average, from 1,071 to 959 hours. Consequently, the proportion of agro-enterprises surveyed said that taxation as the major

obstacle has decreased from 27% in 2008 to 23% in 2011 (see Figure 8). In addition, the truth is that tax incentive policies were promulgated to support agro-enterprises which operate in difficult and remote areas.

### ***Improvement of Legal Environment***

In recent years, the legal system of Vietnam has increasingly been improved both in terms of diversity and efficiency. To facilitate enterprises by building the efficient legal environment, a series of laws relating to firm performance which are considered the biggest barriers for business activities of enterprise have been reviewed and revised. These laws include Land Law, Enterprise Law, Investment Law, Commercial Law, Civil Law, Maritime Law, Procurement Law, Construction Law, Intellectual Property Law, Customs Legislation, Environmental Protection Law, Tax Administration Law, Accounting Law, Value Added Tax Law, Corporate Income tax Law and about 200 guiding documents of the government agencies. The review and amendment of these laws is based on some basic criteria that are the most general nature, consistent with the business characteristics of enterprises such as transparency, rationality, consistency and feasibility. This is the Government's effort to create a favorable legal environment for firms to operate has been recognized in recent years. As empirical evidence, the proportion of agro-enterprises surveyed cited legal environment as a main obstacle has been significantly reduced from 21% in 2008 to 12.5% in 2011 (see Figure 8).

However, the submission of the important legislations to National Assembly for consideration was delayed has significantly affected enterprises' operation in general and business activities of agro-enterprise in Northern Vietnam in particular. This delay is significant for the legislations such as Land Law, Business Law, Intellectual Property Law and documents guiding the implementation of Investment Law. This makes a part of enterprises continue to keep their opinion that legal environment is still a major obstacle for them to operate, especially foreign enterprises.

### ***Government's Efforts to Remove Other Constraints***

Although not yet achieved positive results in the improvement of infrastructure, administrative procedures or tax system, but the Government's efforts in improving quality of workforce in rural areas have also been considered as a success. Proportion of agro-enterprises surveyed cited skills and education of workforce as major obstacle was only 15.5% in 2011, lower than 19.0% in 2008 (see Figure 8). This is a result of the implementation of policies to support job training for the members of households who acquired land to build industrial parks, demobilized military personnel and programs to support training for youth residing in rural and remote areas. More importantly, the government has applied policies which partially exempt the vocational training institutions from corporate income tax in recent years and this has attracted rural labors to apprenticeship with cheaper costs.

Similarly, the anti-competitive behavior was also lightly reduced. As shown in Figure 8, 11% of the respondents said that the barriers to enter the market were worrying in 2011 while this proportion was 12% in 2008. Similarly in the fields of administrative procedures and legal environment, majority of foreign enterprises reported that the anti-competitive behavior in Vietnam is emerging as a major challenge, particularly in distinction treatment between state-owned enterprises to other enterprises.

### ***Sluggishness in Improving Access to Land***

As shown in Figure 8, the proportion of agro-enterprises cited access to land as a major obstacle was an increase, 49% in 2011 compared with 41% in 2008. Moreover, number of day required to complete the process for access to land in 2010 is higher than 5.8 days than 2008 (see Table 4). This increase is mainly spent in the time of land clearance (see more Box 1). This implies that the government's efforts to improve access to land were considered as failures. The analytical results presented above (Section 3.2) also showed the main reasons that made agro-enterprises to express more despair in access to land are short time in land use, tortuous process and cumbersome administrative procedures in land access, negotiating land rent and land compensation. Despite the government has taken efforts to revise 1992 land law to overcome the inadequacies in access to land and the debate about land ownership but the new Land Law was delayed to submit to National Assembly for consideration is the main cause of despair of enterprises. In addition, the Government's efforts to control land market has not shown the signs of success that is most clearly reflected higher market value than the real value. This is considered a major cause leading to higher costs of land rent and difficulties in negotiations of land compensation.

**Table 4:** The Government's Efforts to Remove Problems in Access to Land

Items	2008	2010	$\chi^2$ test
Number of day required to complete the process for access to land	209.6	217.4	
Time of visits to authorities (times)	36.2	29.9	NS
Number of document required to complete the process for access to land	36.1	30.3	NS

**Notes:** , , significant at 10%, 5% and 1% levels, respectively; <sup>NS</sup> no significant

**Source:** Calculate from data survey, 2011

### Difficulties in Improving Access to Credit Service

Regarding to access to credit service, it has appeared many signs which are not much bright prospect of finance in the period of 2008-2010. Besides the difficulties of the world economy, inflation approaching 20% annually over the past three years in Vietnam has caused more difficulties for enterprises. As survey data shown in Table 5, conditions to obtain loans from credit institutions increasingly difficult. The time needed to obtain a loan from banks increased 0.57 days while interest rate increased 1.16 percent in the period of 2008-2010. Whereas, estimated value of loan needed (as a percentage of the loan) rose sharply during this period, from 132.6 percent in 2008 to 141.3 percent in 2010. This fact forced the government to implement contractionary fiscal policy and contractionary monetary policy to stabilize and towards long-term development. Of course, these policies had a great impact on enterprises to operate. Despite this, the Government has also made efforts to limit the difficulties in access to credit service. For example, in late 2008, the government has decided to launch credit support package for enterprises with preferential interest rates and credit guarantees for small and medium sized enterprises. However, the difficulties of the economy extended causing this support package is only implemented in 2009. As a long-term solution, the government has applied policies easing operating conditions for the private banks and allowed foreign banks operating but market share of these banks recognized having more flexibility in lending is still negligible and most of them only have small branches in rural areas.

**Table 5:** The Government's Efforts to Remove Problems in Access to Credit

Items	2008	2010	$\chi^2$ test
Time needed to take a loan from credit institutions (days)	7.64	8.21	
Interest rate (%)	16.78	17.94	**
Estimated value of loan needed, as a percentage of the loan (%)	132.6	141.3	***

**Notes:** , , significant at 10%, 5% and 1% levels, respectively; <sup>NS</sup> no significant

**Source:** Calculate from data survey, 2011

In term of agriculture, the Government issued Decree No. 41/2010/ND-CP on credit policy for the development of agriculture and rural areas in 2010. This decree has allowed microfinance institutions to participate formally in the field of agricultural and rural credit rather than emphasizing the major role of Bank of Agricultural and Rural Development as before. However, the troubles of lending procedures, long time waiting to approve and limited amount of loans have not been able to satisfy enterprises. Consequently, the proportion of agro-enterprises surveyed cited access to credit service as a major obstacle has increased from 36% in 2008 to 48% in 2011 (see Figure 8).

## CONCLUSIONS

The investment climate is such as a "big pond" for firms to expand their operation through investment and the firms being great and healthy in term of the "pond cleaned" (Trung and Itagaki, 2012). Therefore, the government's efforts to strengthening rural investment climate will promote rural economic development. Analytical results of the study identify the major obstacles of rural investment climate in Northern Vietnam such as access to land, access to credit service, infrastructure, administrative procedures and taxation. Some other obstacles that made agro-enterprises less depressed are skills and education of workforce, macro uncertainty, legal environment and anticompetitive behavior.

The analytical results also indicated government's efforts to strengthening investment climate in rural areas. Accordingly, the government's efforts to reduce complications of administrative procedures, improve infrastructure and legal environment, reform tax towards efficient and equitable system have achieved encouraging results.



Nevertheless, the Government did not seem to achieve the goal of improving access to land and credit service. The increase in level of macro uncertainty was also a sign that the government has not succeeded in controlling toward sustainable economic development.

To create faith in a bright future for investors, the Government's efforts to create an enabling rural investment climate through reducing obstacles should be made more active, particular in access to land and credit services. Furthermore, the Government should promote breaking the distinction between state-owned enterprises and private enterprises.

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