

Vietnam 2035 Report

Urbanization and Spatial Transformation

Success with urbanization and economic development

Urbanization -- rising densities of people and production in cities and towns is one of the most striking features of economic development. Incomes tend to rise with urban density, especially when accompanied by increases in the contribution of industry and services to economic activity and jobs. Over the past three decades, Vietnam has undergone an extensive urban transformation that has levered economic development. In 1986, Vietnam had fewer than 13 million urban residents; Vietnam now has 30 million urban residents, and urban areas now contribute over half of national GDP. In fact, the relationship between urbanization and income in Vietnam appears to be stronger than that of China and Korea at similar urbanization levels. Alongside rising economic density, Vietnam has also had an impressive record in keeping rural-urban and regional disparities in check through central transfers aimed at poorer areas that has allowed for expansion of basic services and infrastructure across the country. Even within cities, slums and urban segregation appear to be less of a challenge than in many other developing economies.

Reshaping urban policies to support Vietnam's growth ambitions

As Vietnam embarks on an even more ambitious growth trajectory over the next 15 years, cities will need to be prepared to play a greater role in nurturing a burgeoning domestic private sector, supporting the growth of firm clusters that integrate into Global Value Chains, and providing the logistics support and managerial capabilities to enhance productivity and accelerate growth. Credibly playing this role will involve *reshaping* policies and investments such that economic density is amplified around large metropolitan areas as well as secondary cities with demonstrated potential; economic distance to large markets is reduced to enable specialization; and social division in access to services between migrants and urban residents is dissipated to encourage human capital development for greater agglomeration economies.

Emerging Constraints: Declining density, rising distance, persistent divisions

Reshaping policies is important as there are signals that the current urbanization model is constraining economic transformation. The main stress is coming from the land conversion based urban development model – with industrial zones being developed ahead of demand in recent years and proliferation of small scale fragmented urban expansion. Whilst urban industrial zones have been a critical part of Vietnam's success creating over 3 million jobs, in recent years the development of zones has been uncoordinated with investor demand. The area of land for industrial zones increased by around 77,000 hectares from 2000 to 2010 -- the equivalent of nine Manhattans (8800 hectares) with occupancy rates falling to under 50 per cent. This has major fiscal implications as zones need to be serviced with roads and infrastructure. While industrial zones have the potential to reap scale economies in the future, small scale fragmented development of urban industrial and residential land poses an even larger problem. In fact, 70 percent of land occupied by industry in HCMC is located in scattered and irregular development

outside formally approved Industrial Zones. Such land development dampens economic density. Urban development needs to be done at scale.

The second stress comes from limited connectivity between cities and markets as well as unreliability across the supply chain and high logistics costs. Consider that logistics costs account for 21 percent of GDP, compared to an estimated 15 percent in Thailand and 19 percent in China—which are primarily driven by unreliability and unpredictability in Vietnam-based supply chains. Poor road conditions slow down truck shipments to 40-50 km per hour, with nearly 30 fatal motor crashes reported daily. At the metropolitan level, gridlocks and bottlenecks pose a serious challenge to economic efficiency and make cities less attractive places to live and conduct business. For example, it takes nearly two hours to travel from the central business district of Ho Chi Minh City to the center of Binh Duong new city at off-peaked hours, a distance of only 40 kilometers. Weak regional connections are exacerbating economic distance and Vietnam’s provinces and cities are like independent oases rather than an integrated marketplace.

The third stress relates to rising social division, where migrants to urban areas have considerably lower access to urban services and have lower wages. Without “hộ khẩu” – permanent residence – migrants face numerous difficulties in access to loans, job application, motorbike registration, house purchasing and renting, business registration, medical insurance registration, etc. This reduces their ability to invest in human capital and durable assets, reducing longer term potential for agglomeration economies.

Sequencing and coordinating policies: Institutions accompanied by Infrastructure

There are two main sets of policies that need to be addressed for Vietnamese cities to better support and enable economic growth - Upgrading institutions and expanding connective infrastructure. Consider these in turn:

Upgrading institutions:

1. **Enable land markets:** At the core urban policy reform is the need to let land markets emerge and flourish. Reforming land institutions like strengthening land registration and bringing in market land valuation are a priority to reduce excess and fragmented urban land conversion. Increasing transparency of land pricing by establishing mechanisms to regularly publicize land values obtained in auctions and individual land sales can be a good starting point. These efforts need to be tied to local government fiscal reforms that promote broader use of land and property taxation as an alternative to land conversion fees for revenues.
2. **Enhance planning coordination:** Local governments are rewarded for business expansion within their boundaries, undermining potential clustered development or scale economies in infrastructure investment. The City Classification System encourages local infrastructure development leading to fragmented urban development. There is need to strengthen institutions for integrated urban planning – within and across sectors (land use and transport) that appreciate the importance of scale economies at the corridor or metropolitan area/conurbation or regional level. In countries like Japan and South Korea,

the institutional mandates for land, infrastructure, transport and water resources is vested under one line ministry. Such an arrangement facilitates better coordination of policies at the territorial and city level. This is a critical juncture for Vietnam to manage urbanization properly and this requires a “Whole of Government” approach, which would require GoV to carefully review the mandates within the various line ministries and align them to international best practices.

3. **Strengthen Urban Planning:** There is urgent need to strengthen capabilities in urban planning department to integrate socio economic realities in development of physical plans. Further master plans and other physical plans need to be linked with the budget process; if plans cannot be supported by key investments, their credibility will erode. Finally, coordination mechanisms that can align provincial and city plans are essential; the socio-economic development plans, urban master-plans and sector infrastructure plans are prepared by different departments often run on different schedules and use inconsistent data and projections for planning. The timing of planning needs to be synchronized and the number of plans that govern within a territorial space needs to be reduce considerably (ideally to 2-3). Vietnam also needs to create a professional cadre of urban planners who can plan and manage cities. A greater emphasis to this discipline needs to be made in the university level education and also the talent that is hired within the ministries and provinces.

Expanding connective infrastructure:

1. **Mainstream integrated transport and logistics platform:** The government should push to mainstream integrated planning for transport and logistics across modes, geographies, and public sector functions. One primary reason why transport modes at present are not only misaligned with regard to supply and demand but also relative to each other is that they are planned individually and on a largely decentralized, fragmented basis.
2. **Improvements in road quality and logistics.** Congestion in major urban areas has led to bans on trucks operating within city limits. Limited capacity of bridges and roads as well as the overall condition of transport infrastructure increase costs. Road access to big ports, including Haiphong, Danang, and HCMC, need to be rebuilt to enable cargo to reach the ports. There is also a logistics related need to focus investments on key road corridors and expressways and bottlenecks to tackle issues in supply chains and reduce the burden of road transport costs on the economy.
3. Expand level and quality of urban transport services at the level of the demand and needs.

Payoffs: A vibrant portfolio of towns and cities

Policies that strengthen urban institutions will enable urban development at “scale” and connective infrastructure should expand market access to enable economic specialization. As a result, Vietnam will be able to benefit more from agglomeration economies across a vibrant portfolio of towns and cities that will support economic integration and rapid growth. Using the

framework developed in the World Bank's World Development Report "Reshaping Economic Geography", the portfolio of cities will perform mutually complementary functions:

- Metropolises like Ho Chi Minh City will be interlocutors with the global economy, and provide the urban diversity that encourages learning, innovation and new product development, connecting people and firms to the whole world.
- Cities like Danang will allow producers to benefit from being clustered near each other because they can choose workers and materials from a bigger pool, and they also lead to beneficial competition between producers because they can shop around. These cities will be aggregators for the hinterland economy as well as be part of global value chains.
- Towns like Buon Ma Thuot in the Central highlands famous for its coffee can allow firms and farms to exploit plant level scale economies by providing roads for moving inputs and outputs and schools for the families of workers.

Over the next two decades, policymakers should focus on enabling cities deliver on their potential functions, thereby enhancing economic development.