

## ***Vietnam***

Two events dominated the economic landscape in the last six months, namely Vietnam's accession to the WTO and a dramatic boom in the stock market. Both events pose policy challenges for the government in the short- and medium-term, with the stock market already having attracted substantial short-term attention. GDP grew by 8.2 percent in 2006 with industrial value added increasing by 9.8 percent and services 8.3 percent. Within the industrial sector, the turnover of the domestic private sector expanded 23.9 percent while that of state-owned enterprises (SOEs) grew 9.1 percent.

The retail sales index grew by 20.9 percent in 2006 about the same as 2005. Implemented investment, which is different from the national accounts measure, is estimated at nearly 41 percent of GDP, growing 22.4 percent over 2005 in nominal terms. The investment share of the domestic private sector has risen from 23 percent in 2001 to 34 percent in 2006. FDI commitments, boosted by imminent WTO accession, surged to 10.2 billion dollars well above its 2005 level of 6.2 billion and surpassing the peak level of 9 billion in 1996. FDI commitments for 2007 have already reached 1.9 billion dollars.

Inflation trended down through most of 2006 reaching 6.6 percent in December, and 6.5 percent in February 2007. The moderation in prices resulted from both food and non-food components. The government has announced its intention to move towards market based pricing for petroleum products, steel, cement, coal, paper, and fertilizer. For gasoline such price adjustments have already become more market based. Electricity prices were raised by an average of 7.6 percent in January 2007, though low income households were shielded. Looking ahead, price pressures remain, as evidenced by the recent rise in steel and cement prices.

Export growth in 2006 stood at 22.8 percent about the same level as in the previous year. Exports of seafood, garments, and footwear were particularly strong, the latter despite of an antidumping suit in the EU. Import growth picked up in 2006 largely due to capital goods, in particular machinery and equipment for the Dung Quat oil refinery and industrial zone. The net result of these trends was a small trade surplus. With tourism and remittances remaining buoyant the current account is expected to have recorded a surplus of 1 to 1.5 percent of GDP. Inflows of FDI and ODA were also robust. ODA inflows reached 1.8 billion dollars while inflows of FDI, as recorded in the balance of payments, are estimated to have surpassed 2 billion dollars. Portfolio inflows also picked up in line with investment opportunities being offered by the growing domestic capital market. As a result foreign exchange reserves have seen a rapid rise: by end-December reserves had increased to over 12 billion dollars (11 weeks of next year's imports) compared with 8.6 billion dollars at end-2005.

The National Assembly ratified Vietnam's accession to the WTO in November, 2006 and the country was admitted in January 2007. In December, Vietnam was also accorded permanent normal trading relations (PNTR) or unconditional MFN by the US. Vietnam's tariff structure will witness major changes. The average tariff will decline from a current level of 17.4 percent to an average final bound of 13.4 percent. Average agricultural tariffs are to decline from 23.5 percent before accession to a final bound of 21 percent while industrial tariffs will fall from 16.6 to 12.6 percent. Tariff cuts are to be phased-in over periods ranging from 3 to 12 years, with most occurring within five years. On the services side, Vietnam will grant full trading and wide ranging distribution rights to foreign firms; it will allow 100 percent foreign owned banks; and will also significantly open up telecommunication services.

Fiscal revenues grew by 20 percent compared with 2005 and exceeded budgeted levels. Revenues from crude oil exports were buoyed by high international prices. Tax revenues from the private sector continue to rise, reaching 50 percent of non-oil revenues in 2006, up from 36 percent in 2001. On the expenditure side, minimum wage hikes have become an important contributor to the increase in recurrent outlays in the last three years. Minimum wages for state employees have been raised by a cumulative 214 percent since January 2003, the latest increase in October 2006. The minimum wage hike is also a basis for the adjustment of government pensions and other social security payments. The adjustments are designed to eliminate the minimum wage gap between domestic and foreign invested sectors by 2010 as part of international commitments. The budget deficit is estimated to have declined from 1.2 percent of GDP in 2005 to 0.7 percent in 2006. On-lending of ODA receipts to project implementing enterprises or agencies is expected to have attained 1.2 percent of GDP in 2006. Other items which contribute to public or publicly

guaranteed debt, but are not included in the definition of the budget deficit amounted to 2.8 percent of GDP in 2006. Including these items, public debt is estimated around 44 percent of GDP at end-2006, a level considered to be within manageable limits.

Stock market capitalization surged from under 0.5 billion dollars in December 2005 to 13.8 billion (22.7 percent of GDP) by December 2006, and then to a current level of 24.4 billion. The number of listed firms rose from about 40 to nearly 200 at present. December alone witnessed more than 100 new listings as firms rushed to avail of tax incentives to be withdrawn in 2007. The stock price index shot up 144 percent in 2006 and has already seen an additional increase of 50 percent in the first two months of 2007. The market is set to expand further with 20 large state owned enterprises scheduled to list in 2007. The boom has inevitably led to concerns that stocks are being overvalued by inexperienced investors. The median price-earnings ratio stood at 21 in early 2007, with about a quarter of the firms over 30. It is estimated that foreign stock holding is of the order of 4 billion dollars. The authorities have for now put to rest rumors that capital controls would be imposed in a bid to slow down foreign inflows or outflows. However measures have been announced to enhance disclosure by companies, clamp down on insider trading, and to limit bank lending against stocks.

Credit growth slowed from around 32 percent at end 2005 to 21 percent by mid-2006, but ticked-up somewhat to 25 percent by November 2006. The slower growth in 2006 was mainly attributable to more cautious lending by state owned banks as they adhered to stricter prudential standards. Lending from joint stock banks (JSBs) on the other hand grew by nearly 40 percent. Base money growth in 2006 was driven almost entirely by foreign inflows which were incompletely sterilized by the SBV. On the policy front, a new regulation stipulates that all joint stock, joint venture and foreign invested banks need to have a chartered capital of 1 trillion dong by 2008 and 3 trillion dong by 2010. For SOCBs a minimum chartered capital of 3 trillion dong is required by 2008. After nearly 15 months since the PM's decision to equitize Vietcombank and Mekong Housing Bank, the consultants to advise on the process have been hired. Under current plans the banks will conduct initial public offerings in the fourth quarter of 2007.