Vietnam

The global financial crisis and economic recession slowed economic growth in Vietnam. The international prices of commodities were on a declining trend since the third quarter of 2008, export orders for garments and other industrial products collapsed in the fourth quarter of 2008, and a slowdown in manufacturing became noticeable. The impact was apparent in the first quarter of 2009, when GDP increased only by 3.1 percent from a year earlier, or 4 percentage points below the average first-quarter growth for the last few years. However, positive signs of recovery have been emerging as a result of the government efforts to support economic activity. The government announced its stimulus package which included various measures, from an interest rate subsidy, to tax breaks, and to additional capital spending. As a result, GDP grew by 4.5 percent in the second quarter and 5.8 percent in the third, raising real GDP growth to 4.6 percent year-on-year for January-September. While manufacturing sector is still facing tough challenges because of falling demand, the construction sector is a leading factor of the recovery, with value-added in the sector projected to reach a double-digit growth rate for the whole year. Domestic consumption is also an important factor of the recovery process, with retail sales increasing 9.3 percent in real terms during January-August from a year earlier. Even though the World Bank’s forecasts a growth rate of 5.5 percent for 2009 as a whole, or more than 2 percentage points below the trend, we believe that Vietnam’s economy navigated the crisis relatively well compared to other countries in the region.

The global economic recession has had a significant impact on Vietnam’s external sector. The main concern is the performance of exports that are equivalent to 70 percent of GDP. Over the first eight months of 2009, exports declined by 14.2 percent year-on-year in dollar terms. Export turnover is down across most items and most of Vietnam’s traditional markets. This decline is less than in other developing countries, but could make 2009 the first year with declining exports since the beginning of Vietnam’s economic reforms. The decline was even more dramatic for imports which fell 28.2 percent year-on-year in the first eight months of 2009. The relative decline in exports and imports helped narrow the trade deficit and the current account deficit. The latter is projected to be about 5 percent of the GDP in 2009, down from 11.9 percent in 2008. The actual level could be higher if the economy consolidates its current recovery. Although the projected current account deficit should be manageable, foreign exchange reserves declined from $23 billion at the end of 2008 to about $16.5 billion by August 2009. Most of the decline took place between May and July, when the central bank intervened in the exchange rate market to stabilize the currency.

The fiscal deficit is expected to widen to about 9.4 percent of GDP in 2009, reflecting a decline in revenues and a significant increase in expenditures. Revenues are projected to fall in line with the slowdown in economic activity, lower oil prices and various tax breaks included in the stimulus packages. Spending is up substantially because of stimulus expenditure measures and the government commitment to social sending to ensure social welfare provision. While Vietnam is able to call for some additional external financing, a sizeable financing gap remains and the government may need to reconsider its stimulus package to maintain the fiscal balance at a manageable level. However, it is noted that the main constraint to support the active fiscal stance of the government stems from short-term financing rather than from medium-term debt sustainability.

Monetary policy has been loosened substantially to support domestic demand after a period of tightening in 2008 to tackle overheating. The central bank cut its policy rate by half to 7 percent from mid-2008 to February 2009. The policy rate cut, together with the interest rate subsidy, has led to accelerated bank credit growth. Quantitative indicators of the quality of bank portfolios (based on days in arrears and rollovers) indicate that the fraction of non-performing loans (NPLs) is on the rise. Because the lending rate cannot exceed the policy rate by more than 50 percent, the margins of commercial banks are being seriously squeezed. Low interest rates also make it difficult for the
government to issue bonds, and were associated with the reluctance of exporters to sell their foreign exchange. Recognizing emerging risks of the loosening monetary policy, the central bank recently asked largest commercial banks to cap their lending growth at 25 percent this year.

Poverty levels continued to fall in Vietnam, despite the sharp increase in food and fuel prices through the first half of 2008, followed by a period of sluggish growth in late 2008 and into 2009. While poverty fell in aggregate, the economic turbulence of the last two years highlighted a number of new vulnerabilities and continuing challenges. A Participatory Poverty Assessment (PPA) carried out in early 2008 in rural communities underscores Vietnam’s considerable recent progress in rural development – PPA respondents noted substantial improvements in rural infrastructure, better access to services, rising agriculture productivity in many regions, and more opportunities to diversify rural income sources. The PPA and related studies also suggest some slow recent progress in poorer regions with high concentrations of ethnic minorities. In addition, rapid assessments of the social impacts of the financial crisis carried out in February and April 2009 highlight growing vulnerabilities among specific populations, including Vietnam’s high numbers of migrant workers, workers in the informal sector and household-based enterprises. Greater and more effective investment in education and the training of Vietnam’s future workforce will help reduce vulnerabilities, as will the projected strong economic recovery and growing economic opportunities. However, Vietnam’s social protection system remains underdeveloped in comparison to many other countries, a gap that will need to be addressed as the country moves forward.