

VIETNAM - COUNTRY OVERVIEW

Vietnam's poverty reduction and economic growth achievements in the last 15 years are one of the most spectacular success stories in economic development. During this period, the World Bank Group's relationship with Vietnam has also matured and grown considerably. The Country Partnership Strategy for FY07 - FY11 supports the Government's Socio-Economic Development Plan 2006-2010, which lays out a path of transition towards a market economy with socialist orientation, with the goal of attaining middle income country status by 2010.

Economic And Institutional Development

Vietnam is one of the best performing economies in the world over the last decade. Real GDP has on average grown by 7.3 percent per year during 1995-2005 and per capita income by 6.2 percent per year. The economy has proven resilient to shocks and negative impacts from SARS, avian influenza, poor weather, high commodity prices, inflation, and anti-dumping suits. In US dollar terms, income per capita rose from US\$260 in 1995 to a 2007 level of US\$835. At this pace Vietnam would enter the ranks of middle income countries by surpassing US\$1,000 per capita in 2010.

Vietnam has become increasingly integrated with the world economy and has become a member of the WTO. Exports have been the main drivers for growth, and foreign investments have been buoyant in recent years. Main manufacturing exports are garments, footwear, and wood products, reflecting Vietnam's comparative advantage of a low-cost but high-quality labor force. While external demand conditions have

been generally favorable, the supply response has been made possible by domestic reforms that have dismantled controls on economic activity and strengthened the investment climate. Between 1995 and 2005, the share of agriculture in GDP has declined from 27 percent to 21 percent, while that of industry has risen from 29 percent to 41 percent. In January 2007, Vietnam became the 150th member of the WTO after several years of intensive negotiations.

Recent growth is driven by the rising importance of the private sector. The role of the state sector in manufacturing activity has declined appreciably: from 52 percent in 1995 to under 35 percent in 2006. But this has resulted more from the emergence of a vibrant private sector than from the dismantling of the state sector, which is being restructured and focused on more "strategic" activities. Macroeconomic policies in Vietnam have been generally prudent and key economic balances have been

maintained at manageable levels. The Government's fiscal and monetary stance reflects a determination to not repeat past mistakes that resulted in a short period of hyperinflation in 1992-1996.

Economic transition accompanied by an institutional overhaul. There has been significant progress in public financial management with the implementation of a new State Budget Law in 2004. The entire 2005 budget was disclosed to the public for the first time. The National Assembly is responsible now for the approval of budget, including allocations to lower levels of government. Decentralization is another important trait of the ongoing institutional transition. The planning process, as evidenced by the

drafting process of the latest Socio Economic Development Plan, has also become considerably participatory.

A New Socio-Economic Development Plan for 2006-2010 was approved by the National Assembly in June 2006. The SEDP aims at rapid development, carefully balanced between its four pillars of economic, social, environmental development, and improved governance and institutions. The main challenges for the SEDP implementation are to address entrenched poverty among ethnic minorities, improve the quality and efficiency of public investments and development strong systems and institutions for transparent and efficient public sector management.

Medium Term Economic Outlook and Debt Sustainability

Growth performance was solid in 2007. Economic growth accelerated slightly, to 8.5 percent, making 2007 the third consecutive year above the 8-percent benchmark. Some of the potentially adverse shocks that were feared from WTO accession, especially in relation to agriculture and retail trade, did not materialize. The business climate continued to improve: business sentiment surveys consistently show an upbeat mood among enterprises, with a large majority of them foreseeing an expansion in 2008. The investment rate attained 40.4 percent of GDP in 2007. Growth was increasingly driven by the private sector, with 59,000 new enterprises registering during the year,

an increase of 26 percent with respect to the previous year. Foreign Direct Investment (FDI) commitments almost doubled, to \$20.3 billion, whereas stock market capitalization reached 43 percent of GDP by end 2007, compared to 1.5 percent two years earlier.

Some deceleration of economic growth can be expected in the short term, but medium-term prospects remain strong. High inflation and a large current account deficit have affected the investment sentiment, resulting in a slowdown of short-term capital inflows. The stabilization package adopted by the government in March 2008 has also

resulted in a decline in stock prices and a much cooled down real estate market. As part of the package the government decided to reduce its growth target for 2008 to 7 percent. However, due to statistical inertia the growth rate for the entire year can be expected to be higher than the target (Table 2). Over the medium-term, the magnitude of the investments being implemented suggests that economic growth will continue at a sustained pace.

The fiscal stance of the government remains prudent. The official deficit was lower than budgeted in 2007, and stood at around 1 percent of GDP. The overall fiscal balance including off-

budget investment expenditure was around 6 percent of GDP, similar to that of previous years. Off-budget investments include the issuance of government bonds for education, infrastructure and the re-capitalization of state-owned commercial banks (SOCBs). However, they are off-budget only in name. The choice of these investments reflects the priorities spelled out in the SEDP, and issuance of such bonds is subject to approval by the National Assembly. The stabilization program being implemented by the government includes a reduction of recurrent expenditures by 10 percent and a discontinuation of public investment projects which are not essential or lack appropriate funding.

TABLE 2: SELECTED ECONOMIC INDICATORS

	2006	2007 (e)	2008 (f)	2009 (f)
GDP growth (percent per year)	8.2	8.5	7.5	8.0
Exports growth (percent per year)	22.8	21.9	28.0	30.0
Fixed investment growth (percent per year)	8.6	10.1	10.0	10.8
BOP current account (percent of GDP)	-0.4	-9.8	-13.5	-9.5
BOP capital account (percent of GDP)	5.1	24.7	17.6	12.0
Foreign reserves (US\$ billion)	11.5	21.0	24.5	27.0
Central government bal. (percent of GDP)	-0.3	-2.2	-2.2	-2.0
Public debt (percent of GDP)	41.6	42.2	39.0	39.0

Source: General Statistics Office (GSO) and State Bank of Vietnam (SBV) for 2006 and 2007; World Bank forecasts (base case scenario) for 2008 and 2009.

The level of public debt, at 42 percent of GDP, is moderate and is considered to be sustainable. The indebtedness is similar to other ASEAN countries. The baseline scenario of the most recent Debt Sustainability Analysis (DSA) by the World Bank and the International

Monetary Fund (IMF) is broadly in line with the investment and growth outlook of the SEDP. It estimates public and publicly-guaranteed debt to increase from 44 percent of the GDP in 2007 to around 51 percent by 2016, and decline slightly thereafter. This increase,

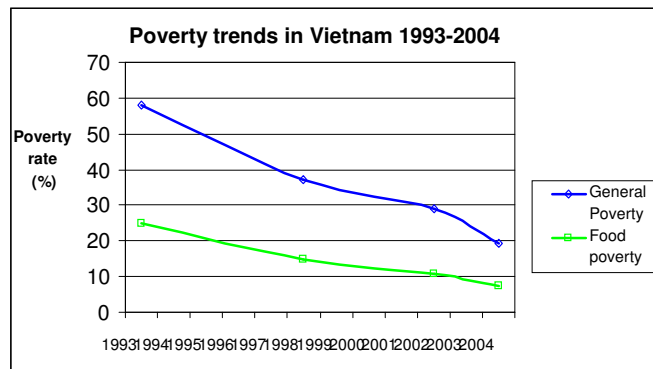
though significant, is still considered within manageable limits, especially since more than half of it will remain on highly concessional terms. The concessional component of Vietnam's debt, embodied in long repayment periods and low interest rates, is reflected in the gap between the nominal level of public debt and its net present value (about 35 percent of

GDP). External debt, both public and private, is projected to decline somewhat: from a little over 30 percent of GDP to just under 26 percent in 2017. The ratio of external debt service payments to exports is estimated to remain about 4 percent during 2007 to 2017. Vietnam should thus remain at low risk of external debt distress.

Poverty Profile

A remarkable success in reducing poverty: New household data indicate that the general poverty rate fell from 58.1 percent in 1993 to 16% in 2006. The standard metrics tracking inequality suggest that the high growth and rapid poverty reduction were accompanied by only very modest increases in inequality. The Gini coefficient, for example rose from 0.34 to 0.37 between 1993 and 2004 and declined to

0.36 in 2006. This favorable trend of shared growth is considered attributed to an egalitarian redistribution of land, the liberalization of agricultural markets, and booming low-skill labor. The data also indicate that poverty reduction accelerated in the past two years.



Challenges Remain in Tackling both Persistent Pockets of Poverty and Poverty among Ethnic Minorities. These impressive achievements in

reducing poverty and the absence of striking increases in inequality sit alongside slower progress for an important sub-group of the population:

ethnic minorities. In 2006, 10.2 percent of the Kinh and Chinese people were living in poverty, compared to 52.2 percent of ethnic minority people. Though accounting for only 13.5 percent of the total population, ethnic minorities now constitute 44.4 percent of the poor. The poverty gap¹ for ethnic minorities is 15.4 percent, compared to only 2 percent for Kinh people.

Development Outcomes

Vietnam has outperformed many other countries in terms of progress towards achieving the Millennium Development Goals (MDGs). Five of the ten main MDG targets set for 2015 have already been attained, and another three could be reached ahead of time (Table 3). However, Vietnam might only partially achieve the target on reversing the loss of environmental resources and could miss the target on halving the share of the population without drinking water and sanitation. Also, it should be noted that alongside a remarkable performance on nearly all of the MDGs, important disparities in achievement remain between the Kinh majority and ethnic minority groups. For example, fewer ethnic minority children are enrolled in school, especially girls. Maternal mortality and child mortality rates are much higher in mountainous areas where many ethnic minorities live than in the rest of Vietnam.

¹ Poverty gaps reflect the average distance between the expenditures of the poor and the poverty line, in percentage of the latter.

Challenges Ahead

For Vietnam to achieve middle income status by 2010, it is imperative that the foundations of a modern market economy are established. Key challenges include:

1. Completing the **structural reform** agenda, including the implementation of WTO commitments and the banking reform roadmap,
2. Establishing an efficient **regulatory framework for infrastructure** while expanding the capacity to fill the supply gap in energy, transport and water;
3. Setting up **social security systems** that would provide for health care financing, pensions for retirees and support for temporary unemployed; and improving the quality of education throughout the system;
4. Protecting the **environment** and better managing natural resources;
5. Establishing a **public administration** based on principles of efficiency, accountability and transparency, and
6. Implementing the **Anti-Corruption Law** and regulations effectively.

TABLE 3: PROGRESS TOWARDS THE MILLENNIUM DEVELOPMENT GOALS

	Eradicate extreme poverty and hunger	Progress	Status
Target 1	Halve between 1990 and 2015 the proportion of people living in poverty	Poverty reduced by more two thirds between 1993 and 2006.	Already achieved
Target 2	Halve between 1990 and 2015, the proportion who suffer from hunger	Proportion reduced by more than two thirds between 1993 and 2006	Already achieved
Goal 2	Achieve universal primary education	Progress	Status
Target 3	By 2015 boys and girls to complete a full course of primary schooling	Grade 5 completion rate (gross) is 104 percent for boys and 98 percent for girls.	Likely to be achieved
Goal 3	Promote gender equality	Progress	Status
Target 4	Eliminate gender gaps in primary and secondary education no later than 2015	Gender equality at all school levels, except for ethnic minorities	Already achieved
Goal 4	Reduce child mortality	Progress	Status
Target 5	Reduce by two thirds between 1990 and 2015, the under-five mortality rate	Reduced by 65 percent between 1990 and 2005 (down from 53 to 19 per 1000)	Likely to be achieved
Goal 5	Improve maternal health	Progress	Status
Target 6	Reduce maternal mortality by three quarters, between 1990 and 2015	Fell by two thirds, from 250 per 100,000 births in 1990 to 85 in 2007	Likely to be achieved
Goal 6	Combat HIV/AIDS and other diseases	Progress	Status
Target 7	By 2015 have halted and begun to reverse the spread of HIV/AIDS	Infection rate went up from 0.34 percent in 2001 to 0.44 in 2005	Likely to be achieved
Target 8	By 2015 halted and reverse the incidence of malaria and other diseases	Malaria cases severely reduced; with only 35 malaria-related deaths in 2007	Already achieved
Goal 7	Ensure environmental sustainability	Progress	Status
Target 9	Embrace sustainability and reverse the loss of environmental resources	Forest cover up but loss in closed-canopy forest and biodiversity	Uncertain to be achieved
Target 10	Halve, by 2015 the share of people without drinking water and sanitation	Rapid progress on drinking water; much slower on hygienic sanitation.	Uncertain to be achieved

Source: United Nations Development Program, GSO and World Bank.