Chapter 8

Fiscal Issues in Vietnam Economy: Assessment on the Impact of Stimulus, Fiscal Tranparecy and Fiscal Risk

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CHAPTER 8

Fiscal Issue in Vietnam Economy: Assessment on the Impact of Stimulus, Fiscal Transparency and Fiscal Risk

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1. Introduction

As the global crisis unfolded in 2008 causing the world economy to slide into worst recession since the Great Depression, the contagious impacts of the crisis have been felt in all continents as well as in most nations. A decline in aggregate demand because of financial hardship and high unemployment rate was observed in nearly all countries. In response, governments of developed-countries have adopted economic stimulus packages to rescue their economies.[1] The 2010 witnessed the financial crisis taking its toll on Europe, with Greece and Ireland being the latest victims. The International Monetary Fund (IMF) and the European Union (EU) had to take measure to rescue both countries on the brink of financial collapse and to prevent a spillover to other European countries already mired in debt.

Like many other developing countries, Vietnam saw a fall in demand for its export and capital inflows. In particular, during the last months of 2008 and early 2009,

[1] These packages include such measures as writing off bad assets in the banking system, cutting taxes, investing in infrastructure, and paying out more social security benefits. Central banks around the globe have adopted a lax monetary policy, drastically cutting interest rates to levels not seen in many years and even using unconventional monetary tools to expand liquidity in the banking system.

monthly export dropped successively. Industrial production in the fourth quarter of 2008 slowed down to 15.6% compared with 17.4% in 2007. Foreign direct investments declined significantly. Consumer sentiment was adversely affected and the stock market index kept falling. Finally, GDP growth rate fell from over 8% attained in 2007 to 6.28% in 2008, and deteriorated further in early 2009 when the GDP growth rate in the first quarter was only 3. 1% and for the first half 2009 it was only 3.9%.

The government of Vietnam responded by reversing its tight monetary policy stance and the fiscal austerity implemented in the early 2008 to control its own home-made mini crisis (running inflation and twin deficits). To weather the economy from the adverse impacts of the global crisis the government announced a large fiscal stimulus package (amounting to almost 10% of GDP). GDP growth rate bounced back to 7.7% in the fourth quarter of 2009, from the previous 3.1% level registered in the first quarter and the annual GDP growth rate was 5.3% for 2009 and being estimated at 6.8% for 2010. In overall assessment, Vietnam has weather the global financial crisis relatively well.

Comparing with other Asian countries that managed to accumulate large foreign reserves and maintained healthy government budget, Vietnam is not in a good position to manage an easy exit. By pursuing an expansionary policy to assist the country through the global crisis, extraordinary pressure was put on the already problem-ridden and fragile economy and until recently it is still unclear how the government would manage its exit strategy. Although to some extent the economy recovered from the global financial crisis and grew at 6.8 percent in 2010 (almost returning to the pre-crisis level), it is not restructured to achieve a high level of growth in the future and there are disturbing structural issues facing the economy even before the 2008 global financial crisis occurred. In the post-global economic crisis environment, whether Vietnam's economy continues its economic recovery and growth at a reasonably rapid and stable rate is an important question for the policy makers as. Macroeconomic uncertainty remains as trade deficit keeps rising, government budget deficits is widening, external debt rising and there are some signs of inflation coming back. To complicate the question further, the economy is highly dollarized as evidenced by the commercial bank's offering US dollar interest bearing deposits and the state is captured by its own large SOEs and the soft budget constraint by the local (prpvincial) governments.

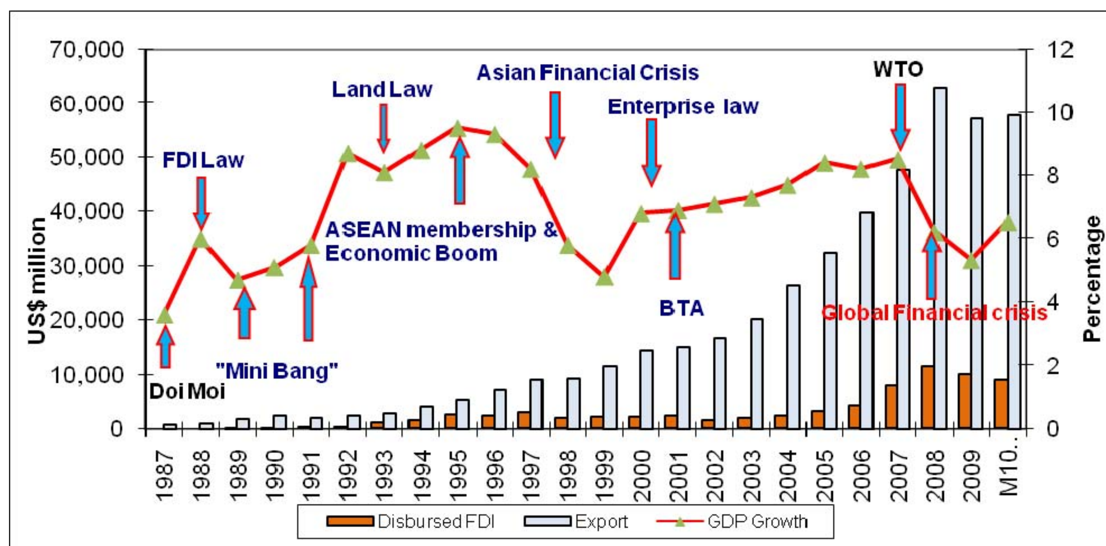
In this paper, we set out to examine the fiscal policy that the Vietnam government used to rescue the economy out of global financial crisis and their implications on the fiscal sustainability of the government. We first give an overview of the Vietnam economy and fiscal position in section two, which also discuss the fiscal stimulus package, its impact on the economy and fiscal implication. Section four pictures some potential fiscal and macroeconomic risks in the future. Finally, we plan to show the limitation in fiscal transparency of Vietnam and policy implications for future crisis.

2. Country Assessment: Performance and Fiscal Position

2.1. Overview of Economic Performance and Fiscal Position before the Global Financial Crisis

The historical evolution of three key macroeconomic indicators for Vietnam together with important economic events/reforms taken place since 1987 is presented together in Figure 1. Since its the 1989-reforms, Vietnam has recorded remarkable achievements in GDP growth and poverty reduction. Over the period 1990-2010, Vietnam's GDP growth rate averaged at around 7% per year. High and continuous GDP growth rates and successful economic development over the period has resulted in overall improvement of people's welfare and significant poverty reduction. According to the Vietnam Household Living Standard Survey the total poverty incidence declined from 58% in 1993, to 37% in 1998, 29% in 2002, 19.5 in 2004 and 16% in 2006. Besides, there are improvements in other dimension of people's welfare such as the high percentage of literate adults (over 90%), higher life expectancy (over 70 years), lower under-five mortality rate (40 per 1000 live births in 2003). Figure 1 shows that since 2000, the economy has regained its momentum after the Asia financial crisis and grew at 7% per annum, reaching 8.5% in 2007, before dropping back to 6.2% in 2008 and 5.3% in 2009 due to the impact of the global economic recession.

Figure 1. Macroeconomic Indicators: GDP growth, Export and FDI



Source: Government Statistical Office.

The economy is depending heavily on investment for growth. Vietnam has relatively high contributions of investment growth to GDP growth (Nguyen *et al*. 2010). The total investment as ratio of GDP has increased considerably during the period after 2000 reaching its peak at 43% in 2007 and 41% in 2008 and it is the large and increasing share of investment in GDP that explains in part the high growth rate accelerated since 2000 (Nguyen *et al*. 2010, World Bank 2007).[2] A direct consequence of adopting an investment-based growth strategy is the rising investment-saving gap. In comparison to other Asian countries, Vietnam domestic saving rate is moderate, staying around 30% of GDP (Figure 2). Combining with a high investment rate, the gap widened and became very large in 2007 and 2008 reaching 9.8% of GDP. With domestic investment in excess of savings, current account deficit has been getting worse in the last few years. In addition to the large trade deficit, the government runs also a large fiscal deficit (i.e. twin deficits) (See Figure 3). Vietnam government budget has been in deficit for years. After the Asian financial crisis, with the implicit expansionary policy to stimulate the economy, the government budget deficit worsens. Even after the

[2] However, the efficiency of the high level of investment has been questioned as State investment, which still occupied the massive proportion of the total investment in the country, is made either directly into public infrastructure or through loans to inefficient state-owned enterprises (SOEs), or in the form of grants to municipalities and private enterprises.

economy recovered, the government has been running on a persistent fiscal deficit. Though the fiscal deficit eased slightly from 2004 to 2006 it widened again in the following period from 2007 onwards.

Figure 2. Vietnam Investment – Saving Gap

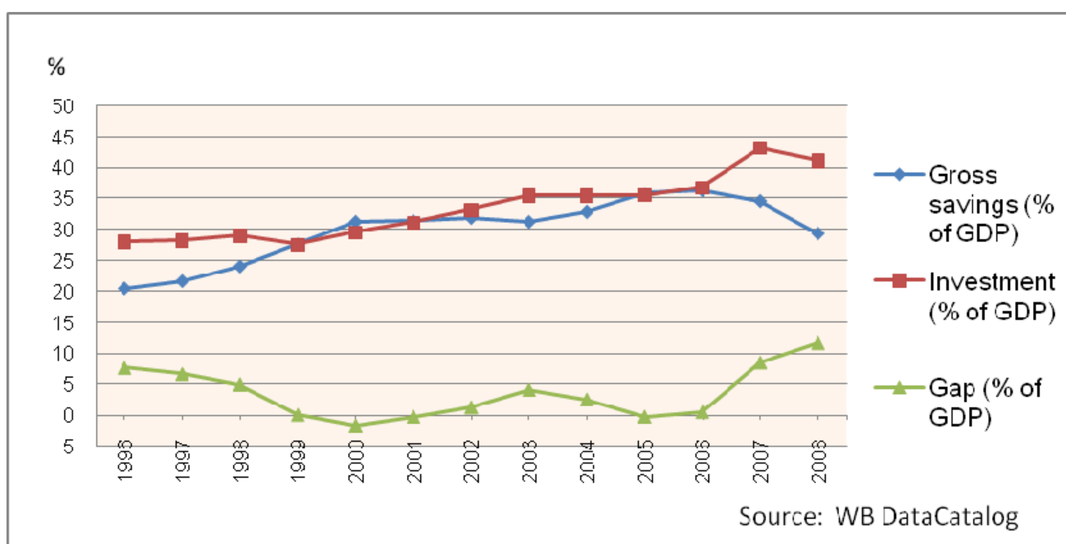
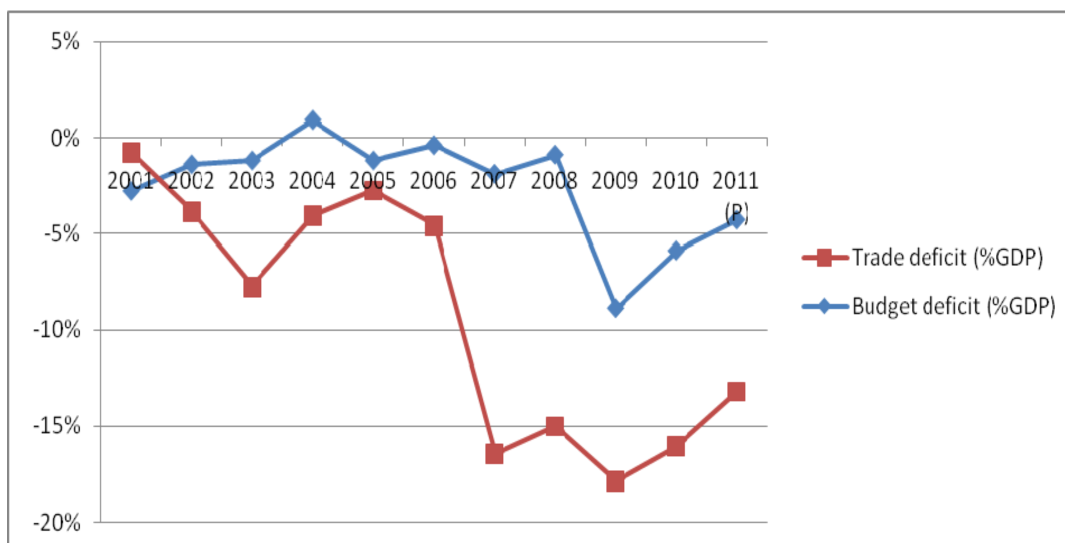


Figure 3. Vietnam Trade and Budget Deficit



Source: IMF & GSO

Table 1 shows the public debt to GDP ratio for Vietnam and some of its neighboring countries. As the table indicates, there are diverse trends in the level of

public debt of different countries, declining in the Philippines, Indonesia, and China, standing still in Thailand and rising in the remaining countries (including Vietnam). Comparing with other neighboring countries in the table, the level of public debt of Vietnam is rising fast, reaching 49% and 48.9% of GDP in 2007 and 2008, respectively.

Table 1. Public Debt to GDP Ratio for Selected Countries, 2005-2010

Countries	2005	2006	2007	2008	2009	2010
Vietnam	43.70	45.50	49.00	48.90	51.10	51.60
Thailand	48.00	42.50	38.40	37.90	45.30	48.60
Singapore	96.30	91.00	88.30	92.20	106.30	101.80
The Philippines	72.90	65.60	57.60	56.70	57.20	55.80
Malaysia	44.20	42.60	41.70	41.40	50.70	52.10
Indonesia	34.90	33.30	31.70	29.00	27.60	26.50
China	23.50	21.30	18.10	16.00	16.60	17.40

Source: Economist Intelligent Unit, The Economist Global Debt Clock: http://www.economist.com/content/global_debt_clock, accessed 13th October 2010

Serious questions about the sustainability of the public debt are raised after stimulate package introduced by the government to response to the negative impact from the crisis. According to some sources, the level of public debt is expected to be higher than 52% of GDP in 2010 and the level for 2011 is projected by the Government at 57.1% of GDP.[3] Along with state budget deficit, which is -6.9% of GDP in 2009 and is higher than the accepted threshold of -5% of GDP, this raises concerns about the fiscal risk faced by Vietnamese government. The issue will be discussed further in the next section.

Before the crisis hit in 2008, Vietnam has already been struggling with a number of problems. In late 2007 and early 2008, Vietnam was confronted with the economic overheating resulting from huge credit expansion and massive capital inflows. After a long period of striving for high rate of economic growth in 2008, for the first time, the government publicly admitted the trade-off between economic growth and macroeconomic stability, shifting their priorities from economic growth to stabilization

[3] See http://vnexpress.net/GL/Kinh-doanh/2010/10/3BA211C5/, accessed at 13th October 2010.

in 2008: a tight monetary policy and cutting back public spending on large projects. Together with a huge domestic credit expansion in 2007, and rising world energy and food prices, inappropriate attempt by the government to absorb large capital inflows (both FDI and portfolio investment) while maintaining a fixed exchange rate led to amounting inflationary pressures. As the macroeconomic situation somewhat improved by the end of 2008, the country suffered very negative impacts of global financial crisis and recession. Entering the year 2009, Vietnam is facing new difficulty and challenges additionally hit by the global financial crisis.

2.2. The Effects of the Global Crisis

Up to the first half of 2008, Vietnam was relatively unaffected by the financial turmoil; but the financial and economic environment worsened in the final quarter of 2008 and first quarter of 2009 (Table 2). In the fourth quarter of 2008, Vietnam's exports fell substantially because of the direct and immediate effects of the global crisis. According to official statistics from the General Statistics Office (GSO), the year 2009 witnesses a decline of exports by minus 8.9% due to decreased aggregate demand for its exports, and substantial fall in the prices of its export commodities, especially crude oil and other primary commodities.[4] For a country with annual growth in export values of about 20 percent, this is a serious setback. As the year 2009 closed, exports showed some signs of recovery, due to a global demand revival, but export values amounted to just $56.6 billion—10 percent lower than in 2008.

In 2008, the flow of registered FDI capital into Vietnam totaled $64 billion (tripled the registered FDI capital in 2007), while flows of implementation capital reached $11.6 billion—versus $8 billion in 2007.[5] In 2009, however, FDI inflows slowed because of capital constraints and the tightening of the world credit market. For 2009, Vietnam managed to attract US $21.48 billion, accounting for only a third of the record level in 2008 (US $64 billion), but is higher than in 2007 (US $20.3 billion). Actual disbursements for investment projects were about US $10 billion, equivalent to 87%

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[4] Despite significant increases in export volume for some of Vietnam's major export products—such as coffee, rice, pepper, rubber, crude oil, and coal—in 2009, their lower prices led to negative growth rate.

[5] When investing in Vietnam, foreign investors are required to register their planned total investment capital (often referred to as registered investment capital), which in practice may differ substantially from the actual amount invested (implementation capital).

against 2008. The slowdown of FDI inflows in 2009, with the expectation of continued lower levels in the years to come, had serious consequences for Vietnam, especially in terms of its exports and investment-dependent growth stategy. According to official statistics, FDI has accounted for more than 50 percent of the country's exports over the last six years.

Table 2. Basic Quarterly Macroeconomic Data during the Crisis

	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09
GDP (year-on-year %)	6.5	5.7	3.1	4.5	5.8	7.7
Industrial production (year-on-year %)	15.8	14.1	2.9	6.8	10.7	14
CPI, end of quarter (year-on-year %)	27.9	19.9	11.3	3.9	2.4	6.9
Trade balance (% of GDP)	-5.5	-5.9	8.5	-15.2	-19.7	-18.6
International reserves (US$ billions)	24.1	24.2	23.3	19	18	16
Policy rate, end of quarter (%)	14	8.5	7	7	7	8
5-year yield, end of quarter (%)	15.9	10	9.17	9.42	10.1	11.68
Dong/U.S. dollar, end of quarter	16,600	17,483	17,797	17,798	17,841	18,479
Dong/euro, end of quarter	23,572	24,301	23,492	24,917	26,048	26,425

Source: GSO. http://www.gso.gov.vn

It is expected that Vietnam's labor force to be highly vulnerable to the global financial crisis, given its heavy dependence on exports and relatively mobile international investment. Data on the impact of the crisis on the labor market and employment, however, are limited and not reliable, complicating the assessment of the social impact of the growth slowdown.[6] According to a survey conducted by VASS,[7]

[6] See also a study by UNDP (2009). Other effects include lower demand for Vietnamese workers in other countries, such as Malaysia; Taiwan, China; and Middle East countries. As the World Bank (2009) observes, available data showed a mixed picture, and the effects are heterogeneous across enterprises and provinces.

[7] The first rapid assessment survey, in early 2009, found that job losses were widespread in industrial zones (both in the North and the South), but few took the form of open layoffs. Non-renewals of contracts and incentives for voluntary departures were more common. Job losses were frequent among seasonal workers and those on short-term contracts. Some enterprises attempted labor-hoarding measures to retain their skilled employees. Unemployed immigrants were highly vulnerable, owing to the lack of social security and **non-reversibility of** immigration (the immigrant workers largely come from areas where arable land is scarce and other opportunities are few). Another survey of the impact of the global financial crisis on labor in industrial parks was conducted by the Central Institute for Economic Management (CIEM). Evidence from this survey suggests that job losses were widespread in industrial parks in late 2008 and early 2009. Remittances to families staying in rural areas suffered as a result.

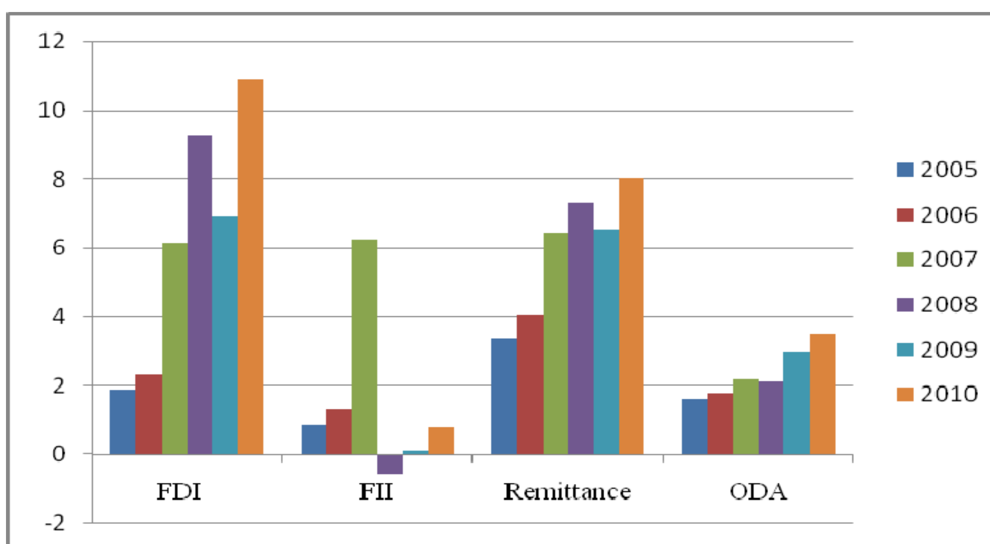
the effects have not been as bad as feared. Despite numerous job losses, frequent reductions in working hours and wages, reduced remittances, and increased reliance on informal sector jobs, major negative effects—such as rising poverty, food shortages, the need to pull children out of school or to sell land, or becoming homeless—have been relatively uncommon.

In addition to its impact on trade, FDI, industrial production, and the labor market, the global crisis has had implications for Vietnam's capital inflows, exchange rate, and stock market. Like other Asian countries, Vietnam suffered capital flight starting in the second quarter of 2008. Banks and financial institutions in the United States and the West reduced their international businesses and focused on their home markets. As a result, funds flowing into Vietnam fell sharply. In response to the booming stock and housing markets during 2006–07, short-term inflows had surged to high levels. The crisis then led to a reversal of these inflows, creating large outflows (See Figure 4). The reversal of portfolio capital flows significantly affected the stock market, with the VN-Index falling to a record low of about 300 points in 2009 from its high of over 1,000 points in early 2007.[8] Although the Vietnamese dong has long been pegged to the U.S. dollar, capital flows have had a major impact on the dong, with several small adjustments of the trading bands and devaluation. Generally, capital outflows depress the dong's value; indeed, since the beginning of 2009, the dong has lost up to a dozen percentage points in its value against the dollar.[9] Declines in exports, as well as in remittance and foreign capital inflows, have reduced the supply of foreign exchange, while expansionary monetary and fiscal policies have increased demand for it. Consequently, there has been a shortage of foreign exchange in the formal market, and the dong's exchange rate against the U.S. dollar has been transacted at the upper bound of its trading band.

[8] The Vietnamese banking system has suffered only indirectly from the crisis. This is because the financial and banking sector was not fully integrated with the global network. Furthermore, the absence of such regulation as mark-to-market has helped the banking system in the time of crisis.

[9] This decline in the dong's value is due mainly to the declining demand in exports and to portfolio outflows. The depreciation of the dong may help to improve Vietnam's export performance, limiting the negative impact from the global recession. However, a study by Jongwanich (2007) of a group of nine Asian countries finds a very weak link between the real exchange rate and export performance in these countries. On the contrary, world demand and production capacity play a more important role in determining exports of these groups of Asian economies.

Figure 4. Flows of Capitals



Source: Vietnam Military Bank

In addition to the direct effects of decreased exports and FDI inflows, the global crisis has reduced aggregate demand sharply, through the employment and income channels. The drop in domestic demand was the result of falling employment and delayed consumption and investment by domestic consumers and investors. Remittances have long been seen as important sources of capital for Vietnam, and the crisis is expected to lower the inflow of this key source of capital. Other impacts include the decline in tourism and lower income for farmers, due to lower commodity prices. [10] The effect of the global crisis on Vietnam's economy is summarized in Table 3 (adopted from Nguyen et al 2010).

[10] An indirect (but critical) effect of the global crisis on Vietnam has been the government's efforts to mitigate the impact on the domestic economy and stimulate short-term growth. These efforts may take the form of delaying or canceling some structural adjustment policies (reforms of SOEs and the banking sectors, as well as improvements in the business environment). These structural adjustments, however, are critical for sustainable growth. For example, to stimulate short-term economic growth, the Vietnamese government may resort to refinancing the inefficient banking sector, subsidizing loss-making state-owned conglomerates, and reviving real estate investment. Although these measures are useful and effective for stimulating short-term economic growth, they cannot ensure long-term sustainable growth and may in fact generate new risks. Therefore, the Vietnamese government should speed up structural adjustments to help to transform the country's growth model.

Table 3. Summary of Effects of Global Economic Crisis on Vietnam's Economy

	Period 1997-2002	Period 2003-2007	Change from 1997-2002 to 2003-2007	Highest 2-year average value before crisis	Expected potential value just prior to the crisis	2008	Forecast/ estimate 2009	Total loss during 2008-2009 compared to potential
GDP growth (%)	6.58	8.05	1.48	8.45	7.5-8	6.18	5.32	-2.18
TFP growth (%)	1.66	2.99	1.33	3.21	2.75	0.2	-0.33	-3.08
Exports growth (%)	17.77	12.91	-4.86	27.74	0.25	5.05	-0.1	-0.26
Exports/GDP (%)	50.73	68.98	18.25	75.25	0.65	78.21	0.62	-0.03
Investment (% GDP)	29.83	37.29	7.45	39.97	37.00	41.13	42.8	5.8
Capital inflows (% GDP)	0.054	0.048	-0.006	0.078	0.07	0.104	0.098	0.028
Fiscal deficit (% GDP)	-	0.051	-	0.055	0.05	0.041	0.07	0.02

Note: The potential GDP for Vietnam is expected to be in the range of 7.5-8% per year.
Adopted from Nguyen *et al.* (2010)

2.3. Government's Responses and Stimulus Packages

The government of Vietnam quickly and decisively responded to counter the negative effects of the global crisis. It reversed the course of the monetary tightening and fiscal austerity policy implemented in 2008. The government aggressively loosens its monetary policy stance by cutting the base rate from 14% per year to 7% per year within a few months. Ceiling lending interest rate (1.5 times base rate) was lowered accordingly, from 21% to 10.5% for productive activities. Lending interest rates for credit card and consumption are negotiable and fluctuating between 12% and 15%.

In terms of fiscal policy, the stimulus package, was initially announced at $6 billion aiming at mitigating the impact of the global financial and economic crisis on the Vietnamese economy and the population, and preventing a general slowdown of economic activities. This figure was later revised to be almost USD 8 billion.[11] To put into perspective, Table 4 presents the values of stimulus packages that neighboring countries committed to fight the global recession. Based on the simple budget deficit metric, the budget plan of late 2008 put the Vietnamese stimulus package in the top tier of the regional comparison (Table 4).

[11] Since the first announcement of the stimulus package several additional stimulus polices were adopted or announced, creating some confusion and prompting understandable concern about potentially unsustainable government spending.

Table 4. Proportion of Stimulus Package to GDP

Country	Stimulus Package(US$, Billion)	Proportion to GDP
China	586	12%
Singapore	13.8	10.7%
Malaysia	18.1	10%
Philippines	6.1	4%
Thailand	8.3	3.3%
Vietnam	8	10%
Indonesia	4.5	0.9%

Source: CIMB Research House, MPI

The package includes a number of components, such as tax breaks and public investments for infrastructure, social transfer and interest subsidy (for working capital loan). For example, the stimulus package includes one-off support of VND 200,000 per person for the poor on the last occasion of New Year Holiday; a reduction of 30 per cent of corporate income tax, an extension of nine months for the submission of 2009 tax payables and a temporarily refund of 90 per cent of VAT for exported goods with "justifiable payment documents", personal income tax exemption for the first 6 months of 2009 and 4% interest subsidy being extended to longer-term loans of up to 2 years for investment in agriculture and other productive activities.[12]

Details of the fiscal stimulus package breakdown in terms of measures are summarized in Table 5. As can bee seen in Table 5, the government's policy approach to maintaining economic growth comprised four broad components: supporting key sectors (primarily small and medium-sized enterprises, or SMEs); stimulating investment; reducing poverty and ensuring social stability; and adopting a flexible approach to monetary and fiscal policy. One of the key components of the stimulus programme was a 4-percentage-point interest-rate subsidy on new dong-denominated short-term bank loans to provide companies with working capital.

How the government's fiscal stimulus package is structured is presented in Table 6. The lack of transparency in Vietnam's fiscal accounting means that it is difficult to ascertain the exact size of the stimulus programme. It is unclear how much of the stimulus package worth VND 145.6 trillion (USD 8 billion) is new money and how

[12] See WB (2009) for further details

much has actually been spent. As usual we could expect that there is likely to have been some duplication of spending plans, and some of the announced measures involved spending that had been brought forward. At face value the VND 145.6 trillion represents a stimulus package equivalent to 8.5% of GDP, but this overstates the actual boost to the economy. Examining the Table 6 reveals that out of VND 145.6 trillion announced for fiscal stimulus package, VND 22.5 trillion is actually expenditure earmarked for 2008 carried forward, VND 37.2 trillion advanced from 2010 budget, and VND 3.4 trillion deferral of payment. It is suspected that the amount of VND 37.2 trillion advanced from 2010 budget is financed by "printing money".

Table 5. Vietnam's Fiscal Stimulus Measures

No	Policy measures	Amount
1	Interest subsidy	VND 17000 billion
2	State Development investment	VND 90800 billion
3	Tax holiday and exemption	VND 28000 billion
4	Other spending for social security and economic downturn prevention	VND 9800 billion
	Total	VND 145600 billion (equivalent to USD 8 billion)

Source: Report by the Government to the National Assembly (2009)

Table 6. Components and Size of Vietnam Stimulus Package

VND trillion unless otherwise noted	Proposed stimulus package
Revenue foregone	25.4
Corporate Income Tax (CIT)	10.4
Personal Income Tax (PIT)	6.5
Value Added Tax (VAT)	7.4
Licenses and fees	1.1
Additional expenditures	117.6
Interest rate subsidy	17
Budget advanced from 2010	37.2
Government bond carried over from 2008	7.7
Investments funded by additional bond issuance	20
Expenditures carried over from 2008	22.5
Deferral of repayment of budget allowance for 2009	3.4
Social spending	9.8
Overall fiscal stimulus	143.0
In percent of GDP	8.5%

Source: Ministry of Finance, Ministry of Planning and Investment, World Bank, IMF

2.4. The Impact of Stimulus Package

Together with the global recession bottoming-out, signs of economic recovery for Vietnam could be seen as early as August 2009[13] as indicated in Table 1, with industrial production and GDP growth picking up in the third quarter of 2009. Although the economic recovery is in large part due to the revival of external demand for Vietnam's export and FDI inflow, it is commonly believed that the policy adopted by the government worked in helping the economy through the recession. [14] According to a report by GSO (2009), together with the recovery in other Asian countries, the prospect of Vietnam's economy was improving and some attributed such recovery to government stimulus policy.[15] While there has been wide spread agreement that the prompt introduction of the stimulus package provided quick protection for the economy, there remains some debate around whether or not package was able to target the most effective businesses and sectors and evaluating the effectiveness and efficiency of the government stimulus package is a daunting task in the absence of reliable data. Here we will only present patchy evidence of the effectiveness of the stimulus package.[16]

The most obvious impact of the stimulus package implemented by the government helped keep the credit flowing into the economy and assisting enterprises to clean up their balance sheet, replacing the high interest bearing loans incurred during the turbulent year of 2008 when the interest rate each 21% with interest rate subsidized. This reduced the financial burden by easing capital costs during a period of economic pressure and enabled businesses to maintain production and jobs.

In September 2009 the Government reported that, the stimulus component worth VND 17,000 billion used for interest rate subsidy resulted in loans (for working capital) of VND 405,000 billion, of which 16% allocated to SOEs and 84% to private sector. Spurred by the introduction of government interest rate subsidies, growth of credit and money supply accelerated in the first half of 2009. The growth of total liquidity (M2)

[13] http://www.vneconomy.vn/20090828091054122P0C10/kinh-te-8-thang-buc-tranh-dang-sang.htm

[14] The effectiveness of the fiscal stimulus packages that countries, developed and developing alike, are implementing is questioned by Foster (2009), http://www.heritage.org/Research/Economy/bg2302.cfm .

[15] http://vneconomy.vn/20090901102716178P0C5/he-mo-kha-nang-tao-buoc-dem-cho-nen-kinh-te.htm

[16] An overall and full assessment of the stimulus package may be necessary but falls outside the scope of this paper.

increased to 35.8% in the second quarter 2009 from 20.3% in the fourth quarter of 2008 (Figure 4) [17]. On the other hand, there is evidence that only a limited number of enterprises could access to the subsidy program. Remaining enterprises faced difficulty in accessing capital.[18] In tandem with the fiscal stimulus package, the government also adopted an expansionary monetary stance to promote economic operations. Therefore, separating and assessing the effects of monetary policy and fiscal policy on the credit growth would be superficial since the monetary and fiscal policies in Vietnam are not independent from each other. The government of Vietnam adopted an unorthodox policy during the crisis time, using the fiscal approach to obtain monetary policy objective (lower interest rates by interest rate subsidy). The interest rate subsidy under the stimulus package, together with the accommodating monetary policy, helped injecting credit to the economy during the bad time. Another effect of the package was to restore business confidence, as reflected in part by a rally in the stock market in mid-2009. [19] Evidence of the impact of the 4% interest rate subsidized loan could be found in a recent study by Nguyen and Nguyen (2010), who use the annual survey of enterprises by the Vietnam Chamber of Commerce and Industry to investigate the impact of having access to the loan and job creation. They report positive and significant impact of such interest subsidy package on the performance and job creation by firms.

The stimulus package has also helped mitigate the impact of the financial crisis on workers. In a recent paper, Manning (2009) suggests that the impact on labor has been milder than might have been expected for a country so heavily exposed internationally. This can be partly attributed to the government's timely stimulus package and partly to other factors such as the tight labor market before the crisis, the competitive nature of

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[17] http://www.adb.org/Documents/Books/ADO/2010/Update/ado2010-update-vie.pdf

[18] According to a report by State Bank of Vietnam, only 20 percent of enterprises receive support from the interest rate program See http://www.vfr.vn/index2.php?option=com_content&do_pdf=1&id=960

[19] The government did not neglect the important role of export in economic growth performance. Although details of the export promotion allocated from the stimulus package are not available, there are some indications that the government has increased its budget for export promotion, and directly assisted companies which have to lay off workers in such sectors as textiles, shoe-making and aquaculture. As a result, the market composition of Vietnam's export shows a clear market diversification towards regions less adversely hit by the global crisis. http://www.tuoitre.com.vn/Tianyon/Index.aspx?ArticleID=302432&ChannelID=11

Vietnam's key exports, and the private sector's capacity to compete globally, despite cutbacks in demand for key export commodities (Manning 2009). In addition, the market for semiskilled and skilled workers recovered well after the Tet break (March 2009).[20] This is consistent with evidence from a rapid assessment survey conducted by VASS in May 2009, which found evidence of "green shoots," with enterprises receiving orders and recruiting more employees. The multiplier effect of the package may also help in the face of falling aggregate demand.

The agricultural sector, which employs more than two-thirds of the country's population and accounts for most of Vietnam's exports, has also been hit hard by the global downturn, although the impact on rural areas has been limited. In April 2009, the government introduced a series of stimulus measures targeting the rural economy. The new policies include interest-free loans for purchasing farm equipment and subsidized loans for fertilizer and other agricultural inputs. However, in the first stimulus package, farmers, who account for 70 percent of the population, were able to access only $48 million of credit, a too small share of the total package of about $22 billion disbursed.

In addition to the stimulus package, the resilience of the business sector appears to have been a major driver of the recent recovery. The stimulus has been seen as a "rescue remedy" to help enterprises access loans to get back on track, remain in production, and create jobs. It has been important in improving the liquidity of the banking system and maintaining debt payments. After all, it is the business sector that takes the risk in responding to the stimulus, and it is its investments that keep aggregate demand from falling too far. Another key factor in facilitating the recovery is the revival of world demand for Vietnam's exports and inflows of foreign investment.

[20] Tet break is Vietnam traditional new year holiday.

3. Identification of Future Fiscal and Macroeconomic Risk

While the government's stimulus helped to support GDP growth and has enabled Vietnam to escape the worst of the global downturn, keeping GDP growth in 2009 at a relatively high estimated level of 5.3%, it has also fuelled rapid credit growth and has amplified concerns about both the country's fiscal accounts and the government's ability to keep inflation in check. Early 2010 when statistics indicated relatively strong recovery and emerging inflationary pressures, the government have been urged to normalize its macroeconomic policies. The economic outlook, however, is subject to four major risks: inflation, exchange rate, investment capital inflows and fiscal imbalances which are expected to complicate macroeconomic management and adding uncertainty to growth prospects.

3.1. Inflation

During the early 2000s, Vietnamese inflation rates were relatively low with one digit. However, sustained debt-financed investment by the government combined with accommodative monetary policy, inflation accelerated in 2007 and peaked at over 23 percent in 2008. In switching from a high-growth strategy to one of stabilization, the government tightened monetary policy in 2008 (in combination with nontraditional and administrative methods) to curb the accelerating inflation rate. As a result, inflation in 2009 fell back to less than 10 percent. The government’s ability to control inflation in 2009 was made easier by the lower commodity prices (especially oil) associated with the crisis. To counter the effects of the global crisis, however, the government reversed the course of monetary tightening. Money supply and credit expansion, together with the large stimulus package, have put renewed pressure on inflation. The interest-rate subsidy, combined with relatively low official lending rates in 2009, also resulted in a surge in domestic credit expansion and undermined the progress in taming inflation achieved in 2008. As the economic recovery began toward the end of 2009, there were

worrying signs of accelerating inflation.[21] The government openly set the inflation target at about 8 percent for 2010, but as the year 2011 drew to close, inflation was higher than the target, reaching a double digit inflation rate at 11.7 percent. On the background of recent devaluation of the Dong (almost 10% in February 2010) and the huge trade and budget deficit, the risk of inflation is looming large.

3.2. The Chronic Current Account Deficit and the Dong's Devaluation

Some researchers (Pincus 2009) has argued that the policy options available for Vietnam's government are much more limited than those of China or other neighboring countries in dealing with the global financial crisis. While China and other Asian neighboring countries have maintained a surplus current account and sound fiscal balances, for several consecutive years Vietnam is plague with a twin deficit (a large current account deficit of 12% in 2008 and large fiscal deficit as presented in details in the next section). Vietnam's chronic current account deficit in a number of occsations led to balance of payment near-crisis in the last 2-3 years. The current account deficits have reached a level that is much higher than the commonly believed sustainable level of 5% of GDP. The continuing current account deficit was mainly driven by the growing domestic credit associated with the financing of the fiscal deficit, the increase in private consumption by households and an overvalued currency and a loss of competitiveness.

Recently, with the stimulate package against the global financial crisis and a reducing foreign reserve due to increasing current account deficit and capital outflows, the domestic currency lost its favorite position and losses its value significantly.[22] By late November 2009, the SBV announced that it would devalue the local currency by over 5% against the US dollar. Again, by early February 2010, the SBV devalued the

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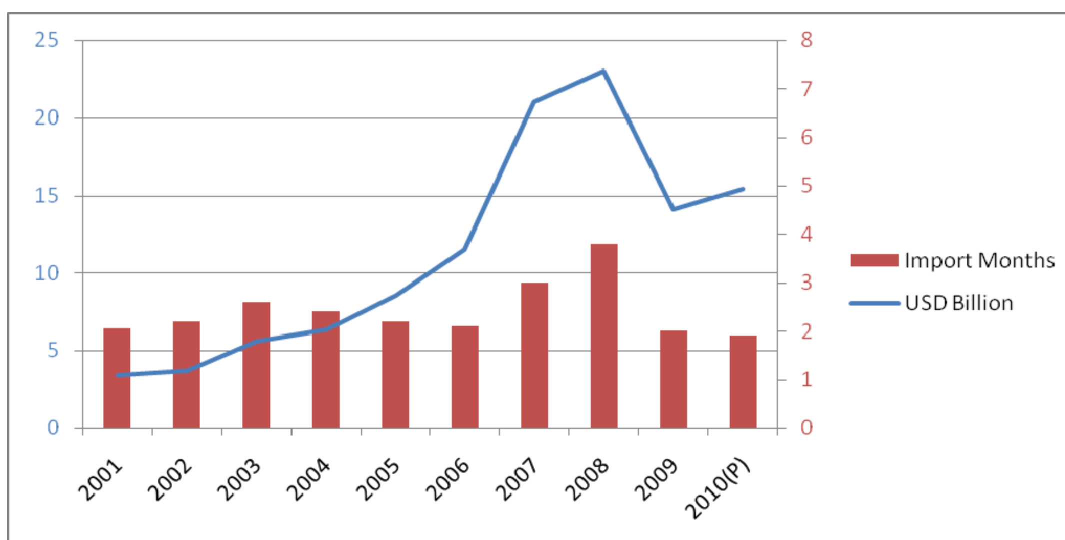
[21] Vietnam's economy depends heavily on imports (especially intermediate goods); therefore, once the world economy recovers, higher prices for Vietnam's key imports should lead to higher pass-through of import inflation. On top of that, the depreciation of the dong would lead to further pressure on inflation.

[22] The rigid exchange rate policy plays an important part in the chronic trade deficit of Vietnam. The government of Vietnam for a long time has preferred a strong national currency and has maintained a fixed exchange rate regime, pegged into USD, with irregular adjustments. The rationale for a strong currency even though it is not supportive for the export-led growth strategy is that, the country imports machinery and most of its intermediate inputs for exporting. More importantly, strong currency maintains advantage for the government in terms of debts borrowing from abroad.

Dong by another 10% against the USD. Prior to the devaluation, the dong had been under downward pressure. Demand for US dollars had risen strongly, driven by the widening merchandise trade deficit and rising domestic inflationary expectations.

Rapid credit growth, together with an expansionary fiscal policy, has led to a sustained increase in imports and a widening trade deficit. A larger demand for foreign exchange by importers, combined with market expectations that the dong would be devalued, led to a shortage of foreign exchange that was particularly severe in May–July 2009, and again in November 2009. Figure 5 suggests that the foreign reserve is running quite low, meeting only 6 import months. In 2010, the situation is getting worse and fearing that the downward pressure on the Dong would increase further in the face of the dollarization, the government had to resort to administrative measures in early 2011.

Figure 5. Foreign Reserves



Source: IMF

3.3. Investment and Capital Inflows

The investment ratio and GDP growth in Vietnam go hand in hand for the period under study (Figure 6). Vietnam's economic growth strategy, which relied on extensive investment, was made possible by increasing government debt and heavy inflows of foreign savings (FDI, ODA and more recently FII). FDI inflows have been an

important source of funds for investment in Vietnam, accounting for over 30 percent of total investment.[23] Since the early days of economic reforms in the 1990s, Vietnam has enjoyed considerable transfers of resources in the form of ODA, most of which was in the form of non-refundable grants or loans on highly favorable terms (with a large grant component).[24] Unlike the situation in other countries, the private sector in Vietnam plays an important—but not a dominant—role in investment. Until 2006, the state sector was the most important source of investment, but its share in investment has declined from 60 percent in 2001 to 33.9 percent in 2008, before rising again to more than 40 percent because of the fiscal stimulus package.[25]

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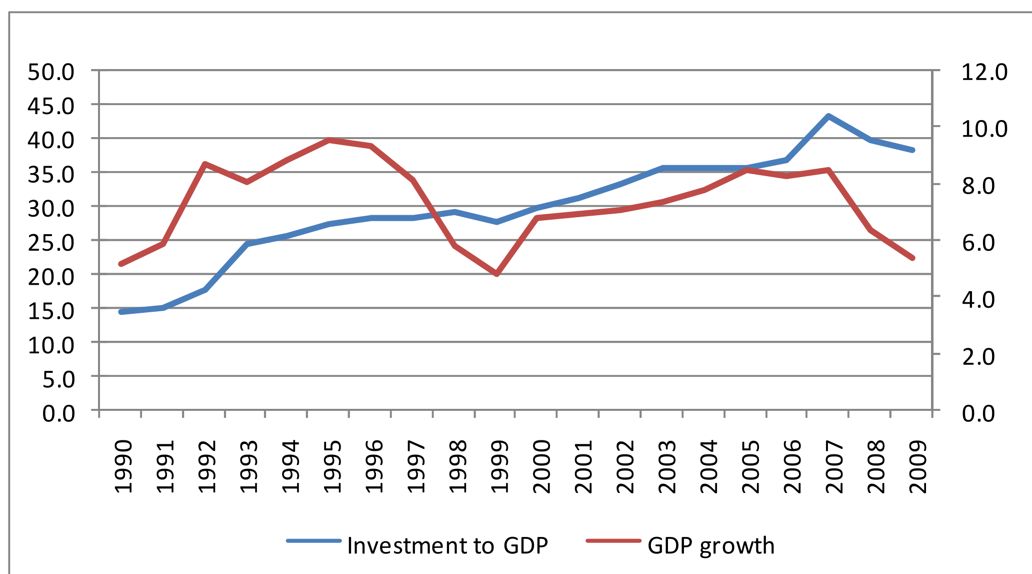
[23] The current financial crisis has put Vietnam in a delicate position. On the one hand, it now would like to be more selective in attracting FDI; but on the other hand, it still needs to compete against other countries for the smaller pool of capital. The comparative advantages offered by Vietnam's abundant, cheap, skillful, and compliant labor force has largely disappeared and will become less important. Vietnam cannot rely on an unskilled-labor advantage to compete for FDI as it could in the last 20 years. Therefore, rather than seeking greater investment for its own sake, policy makers should concentrate on building a climate conducive to efficient investment. Vietnam still lags far behind other countries in the region in this respect. The supporting domestic manufacturing sector has not emerged.

[24] ODA has facilitated the construction of important infrastructure projects, rural development, education, training, and administrative reform. In the foreseeable future, given the commitments of donors, ODA will remain available, but the terms of ODA loans are bound to become less advantageous as Vietnam grows.

[25] State investment is made either directly into public infrastructure or through loans to SOEs, or in the form of grants to municipalities and private enterprises. The general declining trend of the state sector is irreversible and contrasts with the increasing roles of the private domestic and FDI sectors. During the crisis, the investment share of the state sector recovered, but we do not expect the state's role to rise over the long term. Our projections for the three economic sectors are for the general declining trend of the state sector to continue and for the shares of FDI and domestic private sectors to increase—with the domestic private sector becoming the most prominent.

Figure 6. GDP Growth and Investment



Source: ADB Key Indicators 2010

The question Vietnam faces now is whether it can still rely on the old strategy of investment-based development. The answer depends in part on its ability to sustain the inflows of foreign savings and on how the country uses such inflows. In the face of the government's growing need to secure additional funding, ODA takes on greater importance. This is especially true when FDI inflows and export earnings are falling. On this front, the Japanese government has resumed its ODA for Vietnam; the Asia Development Bank granted Vietnam budget support of $500 million; and, most recently, the government has secured an unprecedented level of ODA—$8 billion—from international donors. While we expect that such cheap ODA funding will still be available in the medium term, ODA funds will become more expensive over the long term, and Vietnam may have more difficulty competing for them as its economy develops.

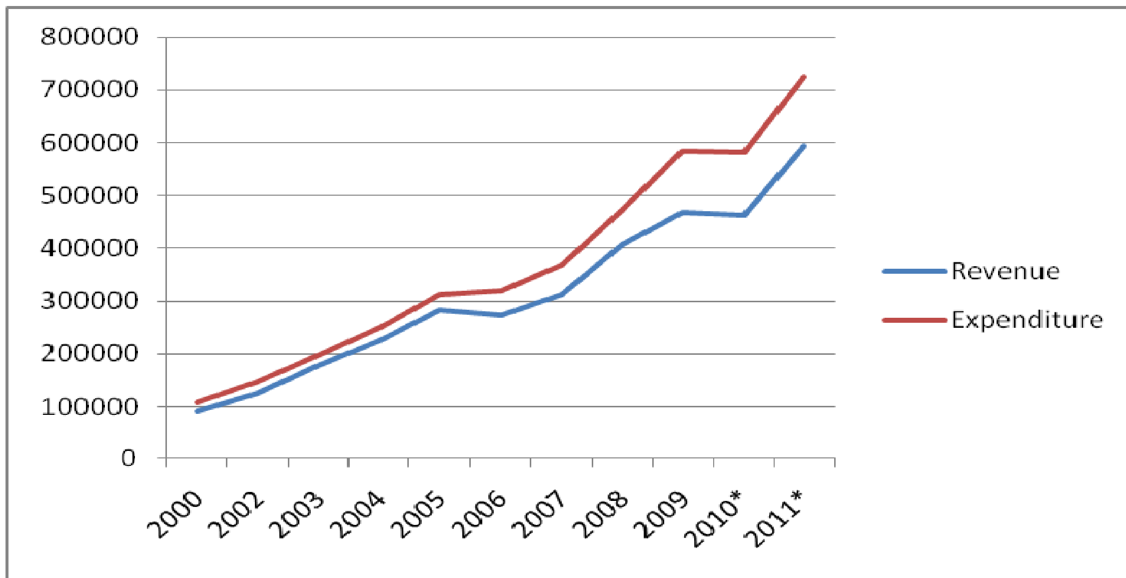
There is also the issue of destabilizing capital inflows. As previous experienced in 2007, the sudden inflows capital (both long-term FDI and hot money) had not been accommodated with appropriate policy led to high inflation, overheating and bubbles. With the possibility of resurgent capital inflows once the crisis is over it is also essential to manage inflows effectively. Responses should address currency flexibility, clear and

stable monetary and fiscal policies, an appropriate regulatory and supervisory framework, and even carefully crafted temporary capital controls.

3.4. Fiscal Risks Faced by the Government

Before the global financial crisis, Vietnam's fiscal position was held in check with fiscal rules approved by the National Assembly. State budget revenue from taxes and fees has been strong, increased from 25% of GDP in 2004 to 26.5% of GDP in 2008. Total government revenues also increased in the same period, from 27.7% of GDP in 2004 to 29.4% of GDP in 2008. General government expenditures however was also on the rise during this period, from 31% of GDP to 37% of GDP, respectively. General government budget deficit was kept under -5% of GDP; total public debt was less than 50% of GDP in 2008. The situation, however, has been changed during the course of the global financial crisis. Vietnam's fiscal position suffers from the external shock, reducing its revenues and grants, and from stimulate package used to remedy negative impacts from the global financial crisis. Figure 7 illustrates the evolution of the budget deficit of Vietnam during the last few years. The government's operating expenditure has been rising more sharply than its tax revenue since 2000, and the buget deficit is getting wider, especially after the global financial crisis in 2008. Despite a lack of clarity about how much of the stimulus will be incorporated into the annual budget and how much will be off-budget, the government's budget deficit widened dramatically in 2009.

Figure7. Budget Collections and Expenditure



Source: Ministry of Finance

Tables 7 and 8 show the structure of government budget and the breakdown of government source of revenues, respectively. Like any other country, in Vietnam, increasing government spending at a time of recession with contracting revenues posed complicated questions. The already-deficit national budget was being put under further strain by a marked reduction in revenue (lower revenue from lower economic activities due to global crisis, lower crude oil royalties due to falling price). Looking at Table 7, in the recent past, crude oil royalties have been an important source of revenue (and export earnings) for the government as over 20% of government revenue comes from oil export, but with global oil prices falling sharply from the highs that they reached in 2008, the government's revenue position is weak, leaving less scope for generous spending plans. As indicated in Table 7, in 2009 crude oil royalties contributed only 12% as contrasted with 24% in the 2008 in the government budget. As can be seen in Table 8, Vietnam has a narrow tax base and only a small segment of the Vietnamese working group pays income tax as the majority of the working population are low wage earners. Although revenue collection in 2009 was in access of the planned revenue it may be due to increased efficiency in tax administration rather than due to a broaden tax base.

A question may be raised next is how the Government can fund the deficit. It is planned that the Government will issue VND 64 trillion worth of bonds in of 2009, and VND 6 trillion in 2010. However, the failures of recent bond issuances has shown that this is not currently an effective way for of capital mobilization in Vietnam. In an effort to raise additional funds for its stimulus package, the government has recently attempted to sell US$1bn of dollar-denominated domestic bonds of various tenors in 2009. However, these efforts were barely successful with investors demanding higher yields than the government is willing to offer (Nguyen *et al*. 2010) .

Up to 31/12/2009, the public debt accounted for 52.6% of GDP, of which government debt was 41.9% while the limit provision of the Prime Ministry is 50%, the guaranteed debt at 9.8%, the external debt level at 38.8% of GDP and the local government debt at 0.8% of GDP. This level which is projected to reach 56.7% of GDP by 2011, including government debt at 44.5% and external debt at 42.2%, shows that the national financial sustainability is running the risk of surpassing the threshold. In the medium term, this rate is anticipated to continue to increase as the government keeps pursuing the investment-based development strategy and therefore incurring more debt.[26]

Medium-term sustainability of fiscal position of the country is at high risk since the worrying issue is repayment capacity which is presented through the growth rate of debt, the internal acceleration rate over capital and the investment to GDP, given investment-based development strategy followed by the government. On average, during the period 2001-2009, public debt per capita in Vietnam increased by 18% per year, nearly triple the growth rate of GDP per capita of Vietnam contemporaneously. The growth rate of Vietnam's public debt in 2010, standing at estimated 12.3%, is lower than some countries in the region. It is, however, double the growth rate of Vietnam at the present. The external debt rose in an increasing pace, from the growth of 4.18% in 2004 to 12.66% in 2005, nearly doubled in 2006 at 21,81% and specially probably making up 34% in 2010. Meanwhile, the acceleration rate from the internal economy over the total capital account continued to fall (from 87.4% in 2006 to 68% in 2009), in contrast to the upward trend in the share of investment in GDP (43% in 2009).

[26] http://vneconomy.vn/20101002083857533P0C9920/nam-2011-no-cong-co-the-o-muc-60-gdp.htm

Contingent liabilities including publicly guaranteed debt is one of the main risks to fiscal sustainability. In September 2008, foreign currency debts guaranteed by the government stood at US$4 billion[27]. These borrowings are mostly foreign commercial bank loans of large SOEs in the transport and power sectors. However, the probabilities of these enterprises' bankruptcy or less productivity are assessed to be higher as a guarantee can create a moral hazard whereby these enterprises have little incentive to minimise risks to ensure the debt is repaid. The second reason is because in Vietnam, guarantees are usually not part of the budget process, thus there is less careful analysis of the risks involved and as the result, this enables the government to support riskier ventures than those which fall within the budget process. The shortage of stringent exposure and reporting procedures for guarantees can contribute to inappropriate issuance or overuse of guarantees. Therefore, the ineffective use of government guaranteed debt may put a debt burden to the government's budget and the current emerging problems related to the Vinashin's 80 trillion VND debt were a strong warning.

Some analysis done by the World Bank, however, suggests that there are rooms for fiscal policy implementation in Vietnam and the fiscal position of the country remains strong (World Bank 2009). The baseline scenario of the most recent Debt Sustainability Analysis (DSA) by the World Bank and the International Monetary Fund (IMF) 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. There are two important aspect of Vietnam's debt: First, Vietnam government has a long history of prudent external debt and a large component of Vietnam's external debt is highly concessional with long repayment periods and low interest rates. Therefore, although this increase is large and significant it is still considered within manageable limits. 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.

[27] Bulletin external debt No5, Ministry of Finance, Vietnam.

The DSA concludes that Vietnam should thus remain at low risk of external debt distress.[28]

The analysis above conceals a important issue in Vietnam, i.e. the soft budget constraints faced by both the large SOEs and local government. Budget constraints are soft when SOEs and local governments can expect to be bailed out by the federal government in times of financial crisis (Kornai, Maskin and Roland 2003). At the moment, the government does not have a stringent and effective monitoring and control mechanism in place to monitor the borrowing of local government and SOEs. Local governments, according to the budget law, are allowed to issue international bonds so as large SOEs. According to recent report by the Economic Committee of the National Assembly, the total outstanding borrowing by the large SOEs and business groups has amounted to 49% of GDP in 2009, increased from 23.9% of GDP in 2008. The recent collapse of a large shipbuilder (Vinashin) with the total outstanding amount of debt reaching USD 4 billion is a warning for the fragility of the situation in Vietnam.

[28] Further details of the DSA can be found here http://imf.org/external/pubs/ft/dsa/pdf/dsacr09110.pdf

Table 7. Vietnam Budget Structure in recent Year (Billion VND)

		2000	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
		%	%	%	%	%	%	%	%	%	%	%
	GDP	6.8	7.1	7.3	7.8	8.4	8.2	8.5	6.3	5.3	6.8	
A	TOTAL REVENUE	100	100	100	100	100	100	100	100	100	100	100
1	Domestic revenue	50.9	49.6	44.4	46.5	42.2	50.4	51.1	50.2	57.5	63.7	64.2
2	Oil revenue	25.9	21.4	20.7	21.6	23.4	29.3	22.0	24.0	12.9	14.3	11.6
3	Customs duty revenue	20.9	25.5	19.1	15.5	13.4	15.7	18.1	22.3	22.5	20.6	23.3
4	Nonrefundable grants	2.2	1.8	1.7	1.3	1.3	1.3	1.1	1.2	1.4	1.1	0.8
5	Others		1.7	14.2	15.1	19.6	3.2	7.7	2.2	5.6	0.2	
B	TOTAL EXPENDITURE	100	100	100	100	100	100	100	100	100	100	100
1	Exp. on investment development	27.2	30.5	30.2	26.6	25.3	26.8	27.6	24.8	30.8	21.6	20.9
2	Principal payment			12.9	13.8	12.9	12.7	13.3	10.8	11.1	12.1	11.9
3	Current expenditure	56.7	52.7	48.4	43.4	42.2	50.6	55.9	55.4	55.2	63.7	60.9
4	Contingency		0.4	0.1	0.0	0.0					2.6	2.5
5	Others	16.1	16.5	8.5	16.2	19.6	9.9	3.2	9.0	2.9		3.7
C	Deficit (classified by VN)											
	Deficit/GDP (%)	0.05	0.05	0.05	0.05	0.05	0.05	0.05	0.05	0.07	0.06	0.05
D	Total financing (classified by GFS)	100	100	100	100	100	100	100	100	100	100	100
1	Domestic financing	69.9	71.8	76.5	79.1	79.6	74.2	76.1	77.3	76.4	82.5	76.8
2	Financing abroad	30.1	28.2	23.5	20.9	20.4	25.8	23.9	22.7	23.6	17.5	23.2

Source: Ministry of Finance

Table 8. Vietnamese Revenue Breakdown

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011*
Total revenues and grants (Unit: Billion VND)	90749	103888	121716	158056	198614	238686	264260	315915	416783	442340	528100	595000
A. Current revenues	96.9%	97.1%	97.2%	92.3%	90.7%	91.9%	92.3%	89.4%	90.6%	90.0%	92.2%	94.0%
I. Taxes	87.6%	88.3%	87.2%	81.0%	78.3%	80.3%	87.2%	84.2%	86.2%	83.7%	87.0%	88.5%
1. Corporate income tax	31.9%	32.1%	30.3%	30.0%	28.7%	31.8%	38.2%	32.6%	32.5%	25.3%	26.6%	25.9%
2. Individual income tax	2.0%	2.0%	1.9%	1.9%	1.8%	1.8%	2.0%	2.3%	3.1%	3.2%	4.4%	4.9%
3. Value added tax	18.8%	18.6%	21.3%	21.0%	19.5%	19.2%	20.7%	22.1%	21.6%	24.1%	28.2%	30.6%
4. Special cons. tax for domestic	5.8%	6.0%	6.0%	5.6%	6.4%	6.6%	6.5%	5.5%	5.2%	6.6%	6.8%	6.7%
5. Natural resouces tax	8.3%	8.1%	7.0%	6.1%	8.8%	8.9%	7.7%	6.3%	6.4%	4.2%	4.9%	4.4%
6. Imp - Exp. tax, special cons. tax on imports	14.8%	16.8%	18.0%	14.2%	10.9%	9.9%	10.0%	12.2%	14.4%	17.4%	13.6%	13.5%
7. Other tax	6.0%	4.7%	2.7%	2.2%	2.3%	2.2%	2.3%	3.1%	3.0%	2.8%	2.5%	2.5%
II. Fees, charges and non-tax	9.3%	8.9%	10.0%	11.3%	12.4%	11.6%	5.1%	5.3%	4.4%	6.4%	5.1%	5.6%
B. Capital revenues	0.9%	0.9%	0.9%	5.9%	7.8%	6.5%	6.3%	9.2%	7.7%	8.5%	6.8%	0.8%
C. Grants	2.2%	1.9%	1.8%	1.9%	1.4%	1.6%	1.4%	1.3%	1.7%	1.5%	1.0%	1.7%
	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	97%

** Estimate Budger for 2011*
Source: Ministry of Finance. The State Budget Report

3.5 . Fiscal Transparency

Since 1996, the Government has begun the process of enhancing fiscal transparency, with the issuance of the budget law and its implementation. In 1997, the budget formulation process was clarified together with the reporting and processing of budgetary information. In addition, the promulgation of the Ordinance on practicing thrift and combating wastefulness in public agencies (March 1998) and the decree on implementation guidelines to legalize fiscal transparency (June 1998) also expanded the accessibility to budgetary information for government agencies, donors and the Vietnamese public.[29] According to the Article IV Consultations report published by the IMF in 2007, the Ministry of Finance's (MoF) State Budget Department "produces provisional monthly, quarterly, and annual data on government operations shortly after the end of the reference period; final data for the fiscal (calendar) year are published after a delay of about eighteen months" (p.15). The data represent the consolidated operations of the state budget, which covers all four levels of the government: central, provincial, district, and commune. They exclude off-budget data on nor investment expenditure or quasi-fiscal activities of SOEs and extra-budgetary funds, among which are the social Security Fund, Enterprise Restructuring Fund, Development Assistance Fund, Export Support Fund, local development funds, and the Sinking Fund (for repayment of on lent funds), for which data are not complied on a regular basis.

Starting in late 2001, the MoF began posting annual budget outturns and plans on its external website, including by major revenue and expenditure items. However, the statistics has not yet meet international standards of functional classification, and this, in turn, might hamper formulation, execution, and monitoring of fiscal policy" (p. 16). Therefore, further considerable actions must remain to be taken so as to improve the coverage of fiscal data as recommended in the 1998 Bank-Fund report on fiscal transparency, the STA multisector statistics mission of 2001, and the 2005 Public Expenditure Review.[30] Vietnam does not yet subscribe to the IMF's Special Data Dissemination Standard (SDDS), but has participated in the less rigorous General Data Dissemination System (GDDS) since 2003.

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[29] World Bank, Vietnam taking stock, 2000, http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2003/10/24/000012009_20031024162829/Rendered/PDF/269800VN0Taking0stock0200001public1.pdf

[30] IMF, "Vietnam: Article IV Consultations" Country Report No. 07/387, Annex IV

Overall, Vietnam displayed a number of deficiencies in the area of fiscal transparency and its Financial Standards Index was only ranked in the very low group, i.e. 85/93 nations, with the indicators for fiscal transparency standing at the intent declared level by The Financial Standards Foundation . Nonetheless, Vietnam is recognized to make good progress in fiscal policy reforms aimed at improving transparency.[31]

4. Conclusion and Implications for Future Crisis

In 2008, as the global financial crisis unfolds, the severe impacts have been felt on all continents including Vietnam. The economy is weathering the global economic crisis quite well thanks to the decisive, timely and determined policy responses. The experience in Vietnam points to the importance of strong fiscal policy to confront the falling aggregate demand due to the global economic downturn. Experience also shows that engineering a good stimulus package that is timely, well targeted and fiscally sustainable is not an easy task as shown by the still ongoing debates on the stimulus package. In retrospect, it appears that the government of Vietnam chose an effective mix of stimulus measures. The rapid loosening of monetary policy, together with the first phase of the interest rate subsidy scheme acted as a "mass bail-out" for the frozen banking and credit sector; meanwhile exemptions and deferrals of tax payments succeeded in preventing a more severe economic downturn. The interest rate subsidy has kept credit flowing into the economy, at a time when banks could have preferred to sit on their liquidity and avoid taking risks. It also allowed the refinancing of enterprise debts contracted at very high interest rates, which could have led to numerous defaults in the context of rapid disinflation. In addition, it boosted the profits of commercial banks, at a time when the deterioration in the quality of their portfolios and thin interest rate margins could have made them vulnerable.

Unlike other countries, Vietnam does not have modern social insurance mechanisms yet, thus lacking an important automatic stabilizer in the economic turbulent time. Instead, Vietnam had to rely on other mechanism such as cash transfers which is fraught problems.

While striking the right balance between stimulus and stability becomes more pressing, the macroeconomic debate should not relegate other key policy reform agendas to the

[31] http://www.estandardsforum.org/vietnam/standards/code-of-good-practices-on-transparency-in-fiscal-policy

backburner. There is a need to support economic activity and to preserve stability, and the government should strike the right balance between them. However, there are also key structural reforms which are required to sustain long-term growth. The crisis highlights the necessity and offers the opportunity to execute these reforms as well as tackle structural problems. From our point of view, the most important issues are boosting competitiveness and improving the environment for investment.

Despite all these short-term challenges, though, Vietnam's positive medium-term growth outlook still rests on a sound footing. This includes its young and relatively well-trained population which promises to yield a positive demographic dividend. Although there are some concerns about budget deficit and the debt sustainability, overall the fiscal sustainability of Vietnam is still within the manageable range if the government exercises restraints in its fiscal expenditure (budget advancement).

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Appendix. Investment in Vietnam

Table. Investment in Vietnam

		Investment by Sector			State Investment by central and local government		State Investment Composition		
Year	Total investment	Non-State Sector	FDI Sector	State Sector	Central Government	Local government	State Budgeted	Loans	Equity of SOE and others
1995	100	27.6	30.4	42.0	54.3	45.7	44.6	19.9	35.5
1996	100	24.9	26.0	49.1	57.8	42.2	45.6	19.3	35.1
1997	100	22.6	28.0	49.4	56.1	43.9	44.0	23.7	32.3
1998	100	23.7	20.8	55.5	56.5	43.5	40.4	28.3	31.3
1999	100	24.0	17.3	58.7	56.9	43.1	41.3	32.1	26.6
2000	100	22.9	18.0	59.1	59.8	40.2	43.6	31.1	25.3
2001	100	22.6	17.6	59.8	55.6	44.4	44.7	28.2	27.1
2002	100	25.3	17.4	57.3	49.7	50.3	43.8	30.4	25.8
2003	100	31.1	16.0	52.9	50.5	49.5	45.0	30.8	24.2
2004	100	37.7	14.2	48.1	50.5	49.5	49.5	25.5	25.0
2005	100	38.0	14.9	47.1	51.1	48.9	54.4	22.3	23.3
2006	100	38.1	16.2	45.7	50.7	49.3	54.1	14.5	31.4
2007	100	38.5	24.3	37.2	48.2	51.8	54.2	15.4	30.4
2008	100	35.2	30.9	33.9	49.4	50.6	61.8	13.5	24.7
2009	100	33.9	25.5	40.6	49.8	50.2	64.3	14.1	21.6
2010	100	38.1	36.1	25.8					

Source: Vietnam Statistical Office

Table A1: Sector of State Enterprise

	Total	Under 0.5 billion VND	From 0,5 to under 1	From 1 to under 5	From 5 to under 10	From 10 to under 50	From 50 to under 200	From 200 to under 500	From 500 and above
					In absolute number				
2000	5759	133	167	1272	924	2047	968	165	83
2001	5355	113	100	1009	818	1948	1061	204	102
2002	5363	73	86	856	748	2001	1194	284	121
2003	4845	64	50	630	602	1815	1217	328	139
2004	4597	35	31	509	516	1663	1238	402	203
2005	4086	27	27	397	423	1405	1121	429	257
2006	3706	31	25	319	365	1195	1064	407	300
2007	3494	26	21	270	324	1085	992	438	338
2008	3287	27	16	226	266	968	966	425	393
					Percentage				
2000	5759	2%	3%	22%	16%	36%	17%	3%	1%
2001	5355	2%	2%	19%	15%	36%	20%	4%	2%
2002	5363	1%	2%	16%	14%	37%	22%	5%	2%
2003	4845	1%	1%	13%	12%	37%	25%	7%	3%
2004	4597	1%	1%	11%	11%	36%	27%	9%	4%
2005	4086	1%	1%	10%	10%	34%	27%	10%	6%
2006	3706	1%	1%	9%	10%	32%	29%	11%	8%
2007	3494	1%	1%	8%	9%	31%	28%	13%	10%
2008	3287	1%	0%	7%	8%	29%	29%	13%	12%

Source: GSO