IMPACTS OF GLOBAL FINANCIAL CRISIS ON VIETNAM'S ECONOMY AND RECOMMENDED POLICY RESPONSES

Vo Tri Thanh

Amid the context of deepening global financial turmoil and economic slowdown, Vietnam's economy, including its financial system, has been unable to avoid certain 'seismic' impacts, notably through three key channels of (i) trade, (ii) investment; and (iii) capital mobility and financial market.

Firstly, financial crisis and economic recession in the U.S. and other major trade partners of Vietnam (e.g., EU, Japan) will possibly continue to restrain its export growth rate to a considerable extent. In fact, Vietnam's export growth rate has decreased since September and October compared to previous months.

Secondly, Vietnam is likely to find more difficult in mobilising external fund; capital inflows such as remittances, FDI, Foreign Indirect Investment, and commercial loans, may continue to decrease. There is a high possibility of postponement, even cancellation, in the implementation and disbursement of FDI.

Thirdly, foreign investors may possibly change their behaviours in Vietnam’s capital market, where they hold a significant proportion of value of shares and bonds. They may realign their investment strategy and restructure investment portfolio, not excluding a withdrawal of capital out of Vietnam. Their movements, plus with psychological effects of the world financial turbulence, may trigger considerable fluctuations in the capital market of Vietnam. These troubles, combined with difficult mobilisation of external capital and high trade deficit, will put considerable pressures on the exchange rate regime and the financial and banking system as well.

Although Vietnam's macroeconomic situation showed some positive signs following implementation of eight policy packages issued by the Government in April 2008 (month-on-month inflation and trade deficit seemed to decline, particularly since September 2008; plus with improved BOP and the liquidity of the banking system), nevertheless, the level of overall macroeconomic instability is still quite severe. YoY inflation remains high, even ex-food and foodstuffs inflation; BOP is still of questionable stability. Meanwhile, difficulties facing enterprises, particularly small and medium enterprises, social pressures and bad debts of the banking system have become more problematic – because many enterprises fell in troubles and real estate loans accounted for a relatively high share in total outstanding loans and many loans were actually of 'subprime' lending nature. Public confidence is low. Risks and challenges of macroeconomic stability have not yet to come

In addition to possible impacts of the world economic developments, Vietnam’s economic outlook is also subject to its policy responses. Taken these factors together and with the use of statistics data accessible to September 2008, a macro-econometric modelling team of the Central Institute for Economic Management (CIEM) has estimated some basic economic indicators of Vietnam for 2008 and forecasted for 2009. Accordingly, Vietnam will find it hard to achieve the growth rate of 7 per cent in 2008. Forecast for 2009 is mainly based on the assumptions that Vietnam’s major trade partners would experience lower growth rate, world prices of major commodities would reduce compared to 2008; meanwhile, Vietnam would pursue a cautious tightening of macroeconomic policy. Given the current context, Vietnam’s economy is most likely to follows the ‘pessimistic scenarios’ in 2009, i.e., economic growth rate is around 6 per cent and YoY inflation is in a range of 13-14 per cent.

It is also noted that import reduced both in terms of quantity and value but trade deficit remained very substantial. In addition, together with unpredictable volatilities of the world economy and national economic slowdown, state budget revenue as a share of GDP may reduce significantly, while budget expenditure demand is hard to restrain, even faces rising pressures. Many nations such as China and ASEAN countries also face mounting difficulties, and thus they will step up for export expansion to markets other than developed countries, including Vietnam. As a result, Vietnam's enterprises will be exposed to more fierce competition.
Broadly speaking, international organizations and financial institutions such as Economist Intelligence Unit and CitiGroup also agreed that Vietnam’s economy in 2009 would be equal to or even lower than its economic growth rate in 2008, i.e., in a range of 6-6.5%.

The choice of policy at present is multi-faceted (economic, financial, social and political aspects), complex and sensitive. Vietnam, thus, faces both internal and external mounting pressures. Externally, Vietnam’s economy experiences a very high level of openness (total two-way trade turnover accounting for 160 per cent of GDP, FDI accounting for over one-fifth of total investment, foreign investors holding shares worth of 25 per cent of market capitalization and bonds worth of 35 per cent of total bond value) and exposes to considerable macroeconomic stability. Domestically, Vietnam faces huge pressures to continue strengthening the macroeconomic environment and to ensure social and political stability as well. At the same time, macro-policies would find difficult to have impacts on different objectives and social groups in the same direction.

Recommended policies for the time being and for 2009 still needs to rely on the most basic ideas of eight policy packages that the government issued in April 2008, including the following:

- to take macroeconomic stability to be on top of priorities and attention (inflation control might be of lesser attention);
- to strengthen joint efforts of comprehensive coordination and flexible implementation of macroeconomic policies (considering a gradual and cautious loosening of monetary policy in consideration of with market responses and forecasted fluctuations of the financial and banking system and BOP – within the two recent weeks to early November 2008, State Bank of Vietnam (SBV) announced two times of cutting benchmark interest rate from 14 per cent a year to 12 per year a year to starve off economic slowdown) together with implementation of measures of reforming state-owned enterprises, supporting enterprises (particularly small and medium enterprises), and guaranteeing social security; and
- to select some essential fields for providing continued supports, thereby creating necessary fundamentals for assurance of high and sustainable growth in the long term.

Read more briefings in this series at www.ids.ac.uk/go/financial-crisis-impact

Dr Vo Tri Thanh is Director, Department for Macroeconomic & Integration Studies, Central Institute of Economic Management, Hanoi, Vietnam. He is acknowledged as one of the most influential thinkers on economic policy and development for the Association of South East Asian Nations (ASEAN) countries of his time. He won the United Nations Special Prize for a co-authored report in 2001 for impact on social policy which joins other prizes for his outstanding research. This is an eclectic mix on financial markets, institutional reform for private institution development, risk assessment, transition from planning to a market economy, industrial upgrading in Vietnam, a perspective on the ASEAN economic community from ASEAN's transitional economies. His research contains challenges to address social inequality in Vietnam and to alleviate poverty. Dr Vo Tri Thanh is a major influencer, with many publications about Vietnam, as a country, as an emerging economy. He is also fluent in the foreign languages of Russian and English.