April 2009
IMF Country Report No. 09/110

Vietnam: 2008 Article IV Consultation—Staff Report; Staff Supplement and Statement; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Vietnam

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2008 Article IV consultation with Vietnam, the following documents have been released and are included in this package:

- The staff report for the 2008 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on December 18, 2008, with the officials of Vietnam on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on February 27, 2009. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- A staff supplement on the joint IMF/World Bank debt sustainability analysis.

- A staff statement of March 16, 2009, updating information on recent developments.

- A Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its March 16, 2009 discussion of the staff report that concluded the Article IV consultation.

- A statement by the Executive Director for Vietnam.

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

VIETNAM

Staff Report for the 2008 Article IV Consultation

Prepared by the Staff Representatives for the 2008 Consultation with Vietnam

Approved by Kalpana Kochhar and Tessa van der Willigen

February 27, 2009

- **Discussions:** Ho Chi Minh City during December 3–4, 2008 and Hanoi during December 5–18. The mission met with State Bank of Vietnam Governor Giau, Vice Minister of Finance Ha, Vice Minister of Planning and Investment Sinh, other senior government officials, and private sector representatives.
- **Staff team:** Messrs. Ishii (Head), Chensavasdijai, and Maliszewski (all APD), Christofides (SPR), Mses. Ivanova (FAD) and Gobat (MCM), and Mr. Bingham (Senior Resident Representative). Messrs. Warjiyo and Raman (OED) attended some of the meetings.
- **Past advice:** The 2007 Article IV consultation was concluded on October 26, 2007. The IMF and authorities have generally agreed on policy priorities, including containing inflation, protecting financial stability, advancing banking sector reform, and ensuring debt sustainability.
- **Consultation focus:** Near-term policies to ensure macroeconomic and financial stability amid the global downturn. Structural reforms to sustain growth and continue poverty reduction.
- **Outreach:** The mission issued a press release at the end of the mission in Hanoi and held staff seminars at the State Bank of Vietnam and a meeting with donors.
- **Exchange arrangement:** The exchange rate regime is currently classified as an "other managed arrangement." Vietnam has accepted the obligations of Article VIII, Sections 2, 3, and 4 of the Articles of Agreement and maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions.
- **Economic statistics:** Broadly adequate for surveillance purposes, but important shortcomings remain in the areas of fiscal, state-owned enterprise, and banking operations.

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Main Websites for Vietnam Data

General Statistics Office of Vietnam (www.gso.gov.vn)

- National accounts
- Consumer price inflation
- Agricultural and industrial production
- Retail sales
- Population and employment
- Merchandise trade
- Foreign direct investment

Ministry of Finance (www.mof.gov.vn)

- Government budgetary operations
- External debt and debt service

State Bank of Vietnam (www.sbv.gov.vn)

- Exchange rates
- Interest rates set by the State Bank of Vietnam (SBV)

Customs Office and World Trade Organization (www.customs.gov.vn and www.wto.org/english/thewto_e/acc_e/a1_vietnam_e.htm)

- Tariffs
- WTO tariff reduction schedule

IMF Resident Representative Office in Vietnam (www.imf.org/external/country/VNM/rr/index.htm)

- Monetary survey
- Balance sheet of the SBV
- Consolidated balance sheet of deposit money banks
- Nominal interest rates
- Balance of payments
- Official gross international reserves

EXECUTIVE SUMMARY

Vietnam has made commendable progress in stabilizing an overheating economy, but continues to face considerable challenges. The near-term outlook remains difficult amid the deteriorating global environment. Growth is likely to slow due to weaker domestic and external demand. Risks are titled toward the downside, as exports, private remittances, and capital inflows could decline further, worsening growth prospects and adding pressure on the external position. Moreover, slower economic activity could heighten vulnerabilities in the banking system. Despite these difficulties, the medium-term outlook is still favorable, with Vietnam remaining an attractive destination for foreign investors.

Key Issues and Policy Discussions

The authorities' policy objectives have shifted toward supporting growth. They significantly eased fiscal and monetary policies in the final quarter of 2008 and recently announced a broad economic stimulus plan. Given deteriorating growth prospects, an accommodative fiscal stance in 2009 is appropriate. However, the scope for a fiscal stimulus is limited in the absence of additional concessional external financing. Staff advised the authorities to carefully balance growth and stability objectives and focus on measures that are effective, well-targeted, and temporary, such as enhancing the social safety net and accelerating existing high quality public investment projects. While inflation risks have waned, any further easing of monetary conditions may have limited impact on growth.

Staff and the authorities broadly agreed on the desirability of moving toward greater exchange rate flexibility. Despite the recent widening of the trading band and exchange rate devaluation, the dong continues to face depreciation pressures. Exchange rate flexibility should be increased further, supported by appropriate macroeconomic policies to maintain confidence in the dong.

Addressing banking sector vulnerabilities is high priority. While recognizing the need to further improve banking supervision, the authorities' assessment of the banking sector remains sanguine. Over the medium term, advancing financial sector reform will be crucial, in particular strengthening the operational autonomy of the State Bank of Vietnam (SBV).

Broader structural reforms will help sustain growth and bolster investor confidence. The main priority is to accelerate reforms that will enhance Vietnam's competitiveness. However, it will also be important to develop a long-term framework of revenue and expenditure management that will preserve fiscal sustainability. In addition to ongoing tax reforms, further efforts to broaden the tax base are needed. Spending should be reviewed to increase efficiency in public investment and to ensure adequate protection for vulnerable groups. Improving efficiency and governance of state-owned enterprises would also help reduce fiscal risks.

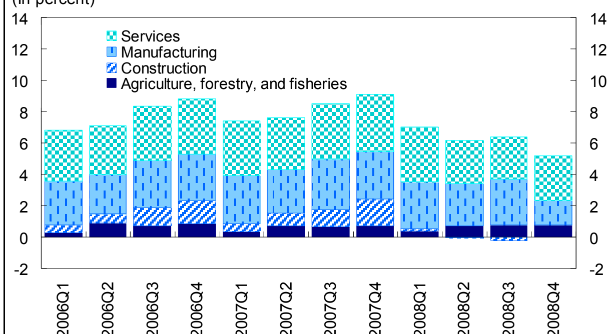
I. INTRODUCTION

1. **Following an extended period of impressive economic performance, Vietnam is facing considerable challenges.** After overheating in 2007, the economic situation deteriorated significantly in the first half of 2008. Rapid credit growth fueled by massive capital inflows, combined with higher public sector spending and a surge in energy and food prices, led to high inflation and large trade deficits. These developments weighed on investor sentiment and put strong depreciation pressures on the dong. While the authorities have made commendable progress in stabilizing the economy, Vietnam has begun to experience adverse effects from the global financial turmoil and economic slowdown. These difficulties are compounded by an already large current account deficit and low international reserves, along with weaknesses in the banking and corporate sectors. Key challenges are designing and implementing policies to ensure macroeconomic and financial stability amid the global downturn, as well as pressing ahead with structural reforms to sustain growth and poverty reduction over the medium term.

II. RECENT ECONOMIC DEVELOPMENTS

2. **Economic activity has slowed.** Real GDP growth declined from 8½ percent in 2007 to 6¼ percent in 2008—the slowest pace since 1999—driven by subdued activity in construction and services following a steep downturn in the property market, which more than offset robust agriculture production (Table 1). Since October 2008, industrial production has also contracted on a month-on-month seasonally adjusted basis, with the foreign-invested sector hardest hit.

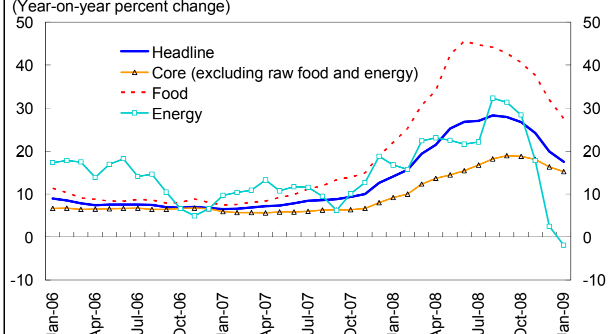
Vietnam: Contribution to GDP Growth by Sector, 2006–08
(In percent)



Source: Vietnam, General Statistics Office.

3. **Inflation increased to a 17-year high, but has eased recently.** Headline inflation rose rapidly and peaked at 28¼ percent (y/y) in August 2008. It has since moderated to 17½ percent (y/y) in January 2009, turning negative on a monthly basis in the last three months, mainly due to lower food and energy prices. Core inflation (excluding raw food and energy) followed a similar pattern, but the decline has been more gradual. High inflation led to large wage hikes, but wage pressures have eased more recently as growth slowed.

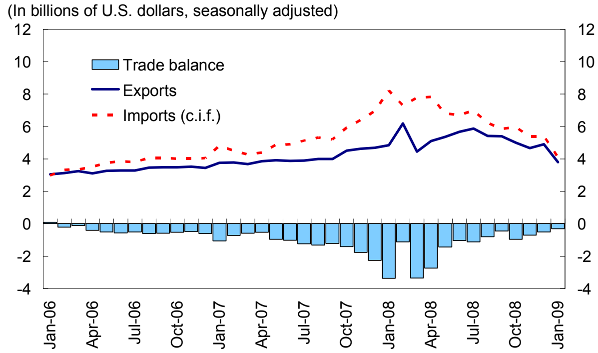
Vietnam: Inflation Developments, 2006–09
(Year-on-year percent change)



Source: Vietnam, General Statistics Office.

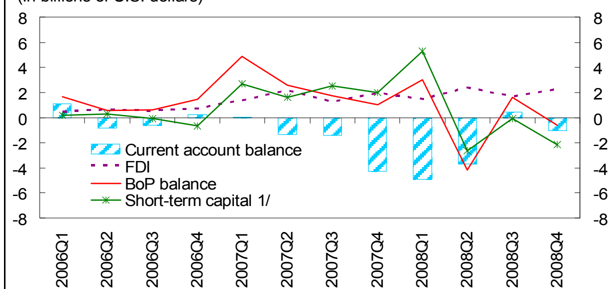
4. **The current account deficit increased sharply in 2007–08** (Table 2). While export growth was robust, strong import growth led to an increase in the current account deficit to 9¾ percent of GDP in 2007. These trends accelerated in the first half of 2008. The deficit began to narrow in the second half of 2008 as weaker import demand more than offset a slowdown in exports due to a sharp fall in global commodity prices and weakening external demand. However, it is still estimated at 10¼ percent of GDP for the year as a whole. The deficits were financed by significant capital inflows, especially foreign direct investment (FDI), keeping gross international reserves at $23 billion (about four months of imports projected for 2009) at end-2008.

Vietnam: Trade, 2006–09
(In billions of U.S. dollars, seasonally adjusted)



Source: Vietnam, General Statistics Office.

Vietnam: Current Account and Financing Sources, 2006–08
(In billions of U.S. dollars)



Sources: IMF, *International Financial Statistics*; State Bank of Vietnam; and IMF staff estimates.
1/ Short-term capital inflows include portfolio investments.

5. **The overall fiscal balance in 2008 is estimated to have improved slightly compared to 2007.**[1] A small deficit was recorded in the first three quarters of 2008, with strong revenue performance—due to increases in trade and oil taxes as well as capital revenue—mostly offsetting higher-than-budgeted expenditures. The latest estimates provided by the authorities suggest that spending in the final quarter would raise the deficit to about 4¾ percent of GDP in 2008 as a whole (Table 3). The non-oil primary balance is estimated to have improved by 1½ percentage points of GDP largely on account of lower capital spending. These estimates are subject to considerable uncertainties relating to the actual disbursement of investment projects and underlying weaknesses in the fiscal data.[2]

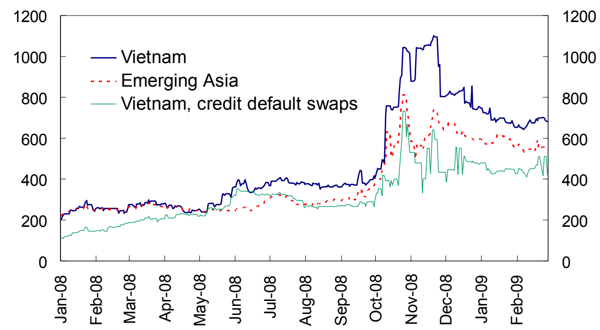
6. **The global turmoil has heightened Vietnam's vulnerabilities.** Exports of goods and services, private remittances, and FDI have all slowed. Risk perception rose more sharply than regional trends, prompting foreign investors to continue reducing their

[1] Based on IMF definition of the fiscal balance, which includes off-budget expenditures and net lending.

[2] Data for 2007 show large discrepancies between the overall fiscal deficit estimated from revenue and expenditure and that from financing.

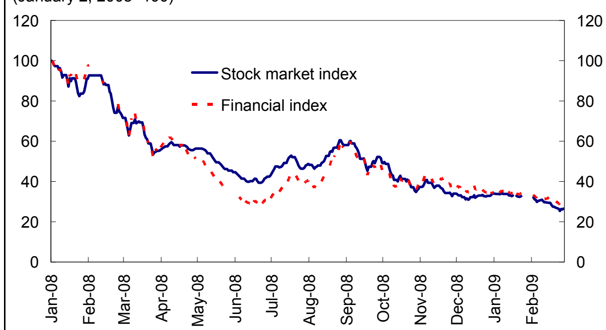
exposures to Vietnam, mainly by selling bonds.[3] The stock market has declined by 75 percent since end-2007. Depreciation pressures on the exchange rate have re-emerged, with the dong depreciating by 9 percent vis-à-vis the U.S. dollar in 2008. Due to high domestic inflation, however, the dong appreciated by 21 percent in real effective terms, much larger than other countries in the region.

Vietnam: Sovereign Bond Spreads, 2008–09
(In basis points)



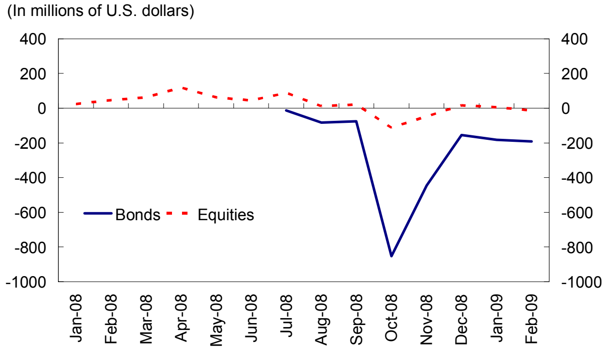
Source: Bloomberg LP.

Vietnam: Stock Market Performance, 2008–09
(January 2, 2008=100)



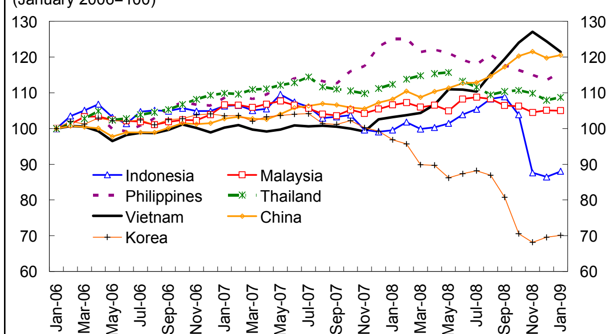
Source: Bloomberg LP.

Vietnam: Net Foreign Purchases of Securities, 2008–09
(In millions of U.S. dollars)



Source: Vietnamese Stock Exchanges.

Emerging Asia: Real Effective Exchange Rates, 2006–09
(January 2006=100)



Source: IMF, Information Notice System; and IMF staff estimates.

III. Outlook and Risks

7. **The near-term outlook remains challenging, given the rapidly deteriorating global economic conditions.** Growth is currently projected to slow to 4¾ percent in 2009—well below the authorities' target of 6½ percent and historical average of 7½ percent—on the back of weaker domestic and external demand. The global downturn is likely to reduce export earnings, private remittances, and FDI, and hence domestic demand, resulting in output falling below potential. Headline inflation is projected to drop to 6 percent (y/y) by

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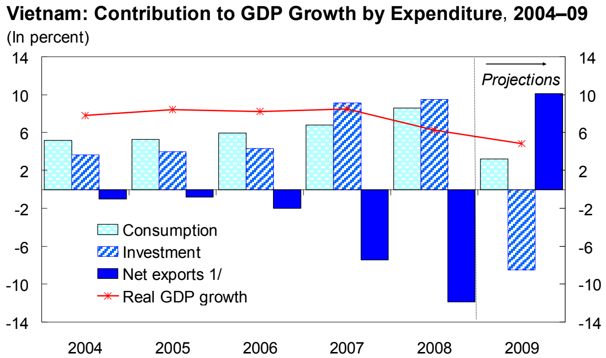
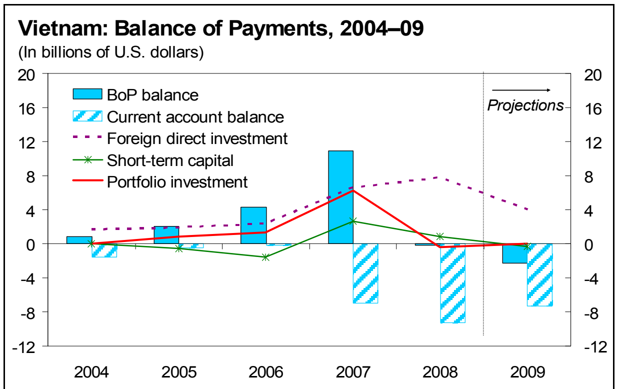
[3] At end-2008, foreign investors are estimated to hold about \$0.5 billion of government bonds, equivalent to 5 percent of total outstanding bonds, and about \$3 billion of equities, or 30 percent of total market capitalization.

end-2009 due to easing commodity prices, although core inflation could fall more gradually.[4] The current account deficit is projected to decline to 8 percent of GDP, mainly due to lower imports. However, tighter global financial conditions are expected to reduce capital inflows significantly. With low levels of gross international reserves (projected to be about three months of imports), Vietnam will remain vulnerable to external shocks.



Sources: Vietnam, General Statistics Office; and IMF staff estimates.
1/ Includes contribution from statistical discrepancy.



Sources: Authorities' data; and IMF staff estimates.

8. **The near-term outlook is subject to increasing downside risks.** A deeper, more prolonged global downturn, especially in advanced economies, could worsen Vietnam's growth prospects. Low short-term external debt (at less than 10 percent of reserves) provides some protection. However, lower exports and private remittances, especially if combined with reduced capital inflows stemming from deteriorating global financial conditions or investor sentiment, could put more pressures on reserves and the exchange rate. Moreover, slower economic activity could heighten vulnerabilities in the banking system. The authorities are aware of these risks.

9. **Nevertheless, the medium-term outlook is still favorable.** Vietnam remains an attractive destination for foreign investors. Provided that the government maintains sound macroeconomic policies and continues reforms to enhance Vietnam's competitiveness, real GDP growth is expected to rise to 7½ percent by 2013 (Table 4). The current account deficit is projected to narrow to about 5 percent of GDP by 2013, as export growth and private remittances are likely to rebound. Capital inflows are also expected to pick up as investor confidence recovers. The debt sustainability analysis (DSA) indicates that external debt levels would be manageable, provided that external borrowing remains prudent. However, the outlook for public sector debt is less favorable, underscoring the need for fiscal consolidation to preserve debt sustainability in the medium term.

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[4] The minimum wage increase of 25–30 percent in January 2009 is unlikely to significantly affect inflation since most workers in the private sector are already being paid above the minimum wage level.

IV. Policy Discussions

Discussions focused on (i) the appropriate mix of macroeconomic and financial policies to address near-term vulnerabilities and (ii) structural reforms—in particular those related to fiscal and SOE issues—essential to sustain Vietnam's progress toward becoming a full-fledged emerging market economy.

A. Macroeconomic Policies: Balancing Growth and Stability Objectives

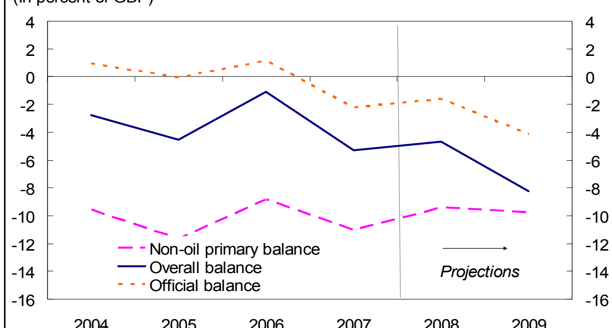
10. **With the balance of risks firmly shifting from inflation to growth, the authorities have been rapidly easing macroeconomic policies.** They have already taken a number of measures, including a significant easing of fiscal and monetary policies and increasing exchange rate flexibility and—more recently announced—a broad economic stimulus plan. However, Vietnam's external position is not as robust as other countries in the region, constraining the government's ability to pursue expansionary policies (Table 5). It is thus important for the government to carefully balance growth and stability objectives and design appropriate economic objectives and policies for 2009, while standing ready to adjust them given considerable uncertainties surrounding the outlook.

Fiscal policy

Background

11. **The fiscal stance envisaged in the original 2009 budget plan (excluding the stimulus plan) was already somewhat accommodative.** Using staff's revenue estimates, which take into account lower world oil prices than envisioned in the budget, the plan implies a slight increase in the non-oil primary fiscal deficit in relation to GDP in 2009, and an increase in the overall fiscal deficit to 8¼ percent of GDP.[5] This reflects lower revenue (by 3 percentage points of GDP) from oil and recent tax reforms,[6] and an increase in off-budget expenditure and net lending (by 1 percentage point of GDP).

Vietnam: Fiscal Balance, 2004–09
(In percent of GDP)



Sources: Authorities' data; and IMF staff estimates.

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[5] According to the authorities' definition of the overall fiscal balance (which includes debt amortization and other items not consistent with GFS and excludes off-budget spending) and their revenue, expenditure, and GDP estimates, the fiscal deficit-to-GDP ratio will improve from 5 percent in 2008 to 4.8 percent in 2009.

[6] The tax changes include introduction of the new personal income tax (PIT) with more generous personal allowances, and a reduction of the corporate income tax (CIT) rate from 28 to 25 percent.

12. **The recently announced stimulus plan aims to support growth, ensure social security, and accelerate poverty reduction.** The authorities are aiming to: (i) support enterprises, especially small- and medium-sized enterprises (SMEs), through temporary interest rate subsidies, credit guarantees, delays in corporate income tax (CIT) payments, and a 30 percent temporary reduction in the tax liabilities; (ii) boost public investment including through state-owned enterprises (SOEs), by frontloading existing projects and simplifying budget execution procedures; (iii) stimulate private consumption through a reduction in value-added tax (VAT) rate on certain products; (iv) support exports through a reduction in some tariffs while increasing protection for certain domestic industries; and (v) enhance the social safety net to protect vulnerable groups.[7] The authorities have introduced various initiatives on a piecemeal basis, but have not announced a revised budget plan for 2009. The stimulus plan will clearly raise the fiscal deficit, but the extent of the increase is uncertain as details of the plan have yet to be clearly determined.

Discussions

13. **Given deteriorating growth prospects, an accommodative fiscal stance in 2009 is appropriate.** However, room for a fiscal stimulus is limited, especially given the already large domestic financing envisaged in the original budget plan. Staff cautioned that in the absence of additional concessional external financing, a stimulus package could further weaken the external position, crowd out private sector activity, and undermine fiscal sustainability prospects as indicated in the DSA. The authorities acknowledged these concerns, but emphasized that supporting growth and employment was the top priority for 2009. Staff urged the authorities to prepare a revised budget plan for 2009 that elaborates on how the fiscal stimulus would be financed.

14. **Staff stressed that the stimulus plan should focus on effective, well-targeted and temporary measures and be financed through reprioritizing existing spending and/or mobilizing additional concessional external financing.** In this context, staff welcomed the authorities' plan to enhance the social safety net and accelerate existing high quality public investment projects and those financed by official development assistance. However, the proposed tax measures are likely to be ineffective in stimulating aggregate demand, are not well targeted, and would complicate tax administration, while several trade tariff increases would create additional distortions. Staff is also concerned that measures to support SMEs may not be effective unless fundamental weaknesses of SMEs are addressed.

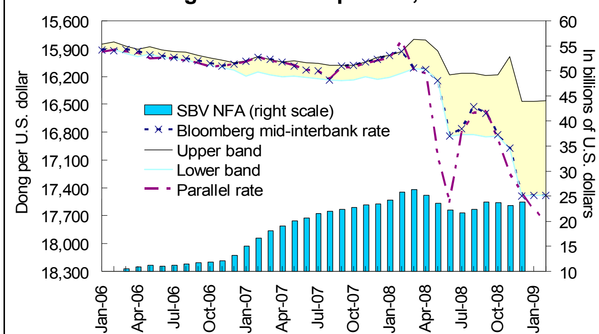
[7] Other measures include: delaying PIT payments; accelerating VAT refund procedures for exporters and lengthening the grace period on import duties for materials used in the production of exports, and speeding up customs clearance process; and reducing import tariffs on goods used as inputs in domestic production, while increasing export tariffs on natural resources and import tariffs on some domestically-produced goods.

Monetary and exchange rate policies

Background

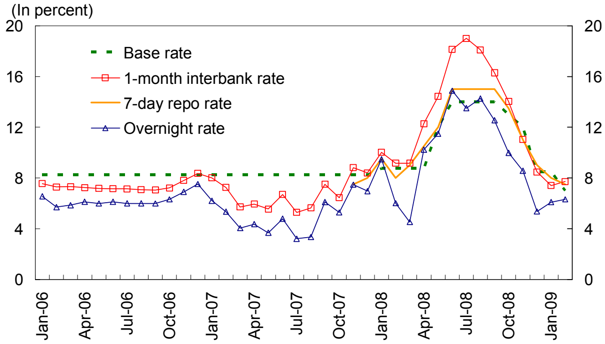
15. **The monetary policy stance has been adjusted swiftly in response to rapidly changing economic conditions during 2008.** The SBV took a number of commendable steps to stabilize the overheating economy earlier in the year, notably through a significant tightening during May–June 2008. It increased policy rates aggressively, tightened market liquidity conditions, and restricted bank lending activities through moral suasion. This led to a sharp decline in credit growth (Table 6). As the authorities became increasingly concerned about growth and inflation pressures began abating in the second half of the year, the SBV rapidly eased monetary policy. Policy rates are now below the level where the tightening cycle began,[8] and interbank interest rates as well as bank lending and deposit rates have fallen sharply (Table 7). Nevertheless, credit activity has remained subdued as banks have become more reluctant to lend due to increased risk perception, while credit demand has waned in light of weaker business prospects.

Vietnam: Exchange Rate Developments, 2006–09 1/



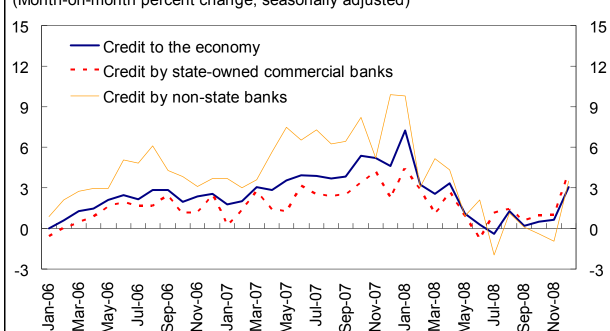
Sources: State Bank of Vietnam; and Bloomberg LP.
1/ An upward movement indicates an appreciation.

Vietnam: Interest Rates, 2006–09
(In percent)



Sources: State Bank of Vietnam; and Reuters.

Vietnam: Credit Growth, 2006–08
(Month-on-month percent change, seasonally adjusted)



Source: State Bank of Vietnam.

16. **The authorities responded to depreciation pressures by increasing exchange rate flexibility.** In June 2008, the SBV devalued the dong against the U.S. dollar by 2.4 percent, widened the dong-U.S. dollar trading band from ±1 to ±2 percent, and stepped up foreign

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[8] Since October 2008, the SBV has reduced the base (prime) rate by 700 basis points to 7 percent. In addition, the interest rates on open market operations and the reserve requirement ratio on dong deposits have been lowered sharply.

exchange market intervention. These measures, together with tighter monetary conditions, helped stabilize the foreign exchange market. With monetary conditions having since eased sharply and the economic outlook worsening, depreciation pressures on the dong re-emerged in the final quarter of the year. The authorities have intervened in small amounts to support the exchange rate, widened the band further to ±3 percent, and subsequently devalued the dong-U.S. dollar rate by another 3 percent. Despite these efforts, the dong has continued to trade at the weaker end of the band.

Discussions

17. **The authorities should assess how the recent significant monetary easing and increased fiscal spending will feed through the economy before relaxing monetary conditions any further.** Staff emphasized that further monetary loosening may have only limited impact in supporting growth, but could add to depreciation pressures on the dong. The SBV was mindful that placing too much emphasis on growth could have negative consequences on macroeconomic stability, but maintained that policies would need to be accommodative to mitigate an economic downturn. In addition, aggressive monetary easing by other central banks in the region and advanced countries has added peer pressures for the SBV to move in tandem. On the SBV's liquidity management framework, staff noted that there remains ample room to strengthen open market operations and liquidity forecasting and management, along the lines recommended by the Fund technical assistance (TA), which would help reduce interest rate volatility and provide a clearer signal of the monetary policy stance.

18. **Staff welcomed recent moves toward greater exchange rate flexibility, but noted that the dong continues to face depreciation pressures.** Staff's exchange rate assessment suggests that the dong is somewhat overvalued from a medium-term perspective (Box 1). Staff recommended that if depreciation pressures persist, exchange rate flexibility be further increased through a combination of widening the band and adjusting the official exchange rate, supported by appropriate macroeconomic policies to boost credibility in the exchange rate system. The scope for sustained foreign exchange market intervention is limited by the relatively low level of reserves. Greater exchange rate flexibility would also help improve the effectiveness of monetary policy, deepen the foreign exchange market, and pave the way for a smooth transition to inflation targeting—a framework the authorities plan to adopt in the future. The authorities agreed that increasing exchange rate flexibility was an appropriate strategy, but stressed that they would allow the exchange rate to adjust only gradually to avoid disruptions in confidence and economic activity.

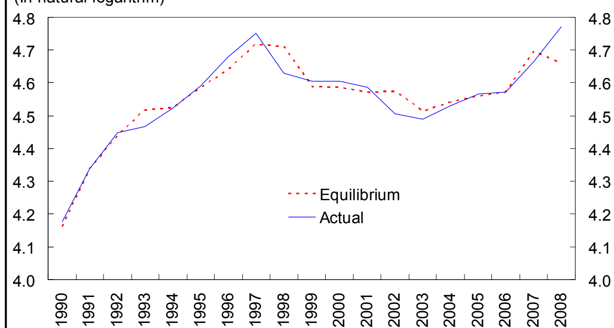
Box 1. Equilibrium Exchange Rate Assessment

Three standard, model-based approaches indicate that the exchange rate is somewhat overvalued compared with its medium-term equilibrium level.

The macroeconomic balance approach suggests some overvaluation. The current account norm is estimated at a deficit of 2.6 percent of GDP. This can be explained by the fact that Vietnam has a higher fiscal deficit, higher output growth, and a lower level of economic development than its trading partners. The underlying current account deficit in 2008 is estimated at about 4 percent of GDP, taking into account a number of temporary factors, including rapid credit growth and an investment boom by SOEs. In addition, the current account deficit is projected to decline to 5 percent of GDP in 2013.

The equilibrium real exchange rate approach produces a somewhat higher estimate of overvaluation than the macroeconomic balance approach. The equilibrium real effective exchange rate was estimated by four fundamental variables—changes in the net foreign assets of the banking system as a ratio to GDP, external terms of trade, government consumption (measured as purchase of goods and services plus government wages), and trade openness (the sum of exports and imports as a ratio to GDP).[1]

Vietnam: Real Effective Exchange Rate, 1990–2008
(In natural logarithm)



Sources: IMF, INS database; and IMF staff estimates.

The external sustainability approach produces a somewhat lower result than the other two approaches. The current account deficit stabilizing net foreign assets is estimated at 3½ percent of GDP, somewhat higher than the current account norm.

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[1] Due to structural breaks in the series and other data issues, the sample period was constrained to 1990–2008.

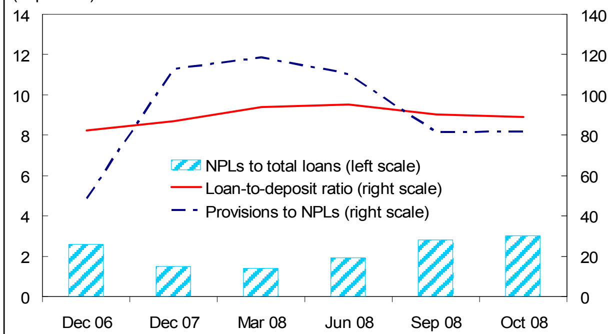
B. Addressing Financial Sector Vulnerabilities

Background

19. **Strains in the banking system emerged in 2008.** Banking conditions were mainly affected by tighter domestic liquidity conditions, higher interest rates, and a sharp decline in asset prices in the first half of 2008 as well as slowing growth in the second half of the year. Given high loan-to-deposit ratios and reliance on short-term interbank funding, a number of banks experienced liquidity problems when the SBV tightened monetary policy. Smaller private joint-stock banks (JSBs) were reportedly most affected, with some receiving emergency liquidity support from the SBV. Banks' net interest margins were squeezed by the higher funding costs and caps on lending rates.[9] Asset quality also deteriorated, with nonperforming loans (NPLs) increasing to 3 percent of total loans in October 2008 (double the end-2007 level), but provisioning coverage against NPLs at 82 percent appears sufficient, with JSBs having a higher coverage (Table 8). The banking system on the whole is still expected to report positive profits for 2008 due to higher noninterest income mainly through gains on bond trading. While full year data are not yet available, a number of banks appear to have strengthened further their capital base.[10]

Vietnam: Banking Indicators, 2006–08

(In percent)



Source: State Bank of Vietnam.

20. **The year 2009 will be challenging for Vietnamese banks, with credit risk expected to be the main concern.** The rapid credit growth in the past two years, together with the projected slowing in economic activity, could lead to asset quality problems. Banks are heavily dependent on corporate lending (about two-thirds of total loans), default rates of which, in particular among SMEs, are projected to rise. Banks are also exposed to the property market through their reliance on collateral and mortgage loans (about 10 percent of total loans), although conservative practices on loan-to-value ratios by banks (35–50 percent)

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[9] Vietnam's Civil Code stipulates that financial institutions cannot charge lending rates exceeding 1.5 times the base rate. The SBV has recently raised the lending rate cap of the People's Credit Funds (savings and credit cooperatives for rural households) to 1.65 times the base rate and allowed negotiable interest rates for consumer and credit card loans.

[10] The SBV doubled the minimum paid-in capital to 1 trillion dong by end-2008, and will increase it to 3 trillion dong by end-2010. This primarily affected smaller JSBs. Some large JSBs have strengthened capital through retained earnings and rights issuance to existing shareholders.

may help somewhat protect against a property market downturn. Foreign currency lending (about 20 percent of total loans) could also potentially turn into NPLs if the dong weakens, but banks indicated that most of the foreign currency loans were extended to companies such as exporters which were naturally hedged against exchange rate risks. Banks also face liquidity risks, especially smaller banks.

21. **Vulnerability varies across the types of banks.** Smaller and some mid-sized JSBs with weak liquidity position and rapid loan growth in the recent past are considered most vulnerable to a cyclical downturn, but are not systemically important as they account for less than 5 percent of total banking assets. Asset quality, coupled with relatively thin capital base and lower provisioning, also remains a problem for state-owned commercial banks (SOCBs), which account for about 50 percent of total banking system assets, although they may be able to receive government support.[11] Larger JSBs appear more stable and sound, as they have solid profit margins and a more diversified revenue base and are well capitalized. Some also have benefited from investment and knowledge transfer by major foreign banks in recent years.

Vietnam: Key Financial Soundness Indicators, 2007
(In percent)

	4 SOCBs 1/	Top 10 JSBs	JSBs 11–20	JSBs 21–31
Return on asset	1.0	1.3	1.2	2.0
Capital adequacy ratio (CAR)	9.4	19.0	16.4	...
Capital-to-assets ratio	4.6	11.1	11.7	24.6
Loans-to-assets ratio	63.5	53.2	48.5	53.8
NPLs to total loans	1.9	0.6	1.4	1.5
Loan loss provisions to total loans	2.1	0.5	0.5	0.5
(NPLs-provisions) to capital	-3.3	0.4	4.4	3.3

Sources: State Bank of Vietnam; Bankscope; and banks' financial statements.
1/ Excludes Mekong Housing Bank.

22. **Overall, banks' strengthened capital position may help Vietnamese banks mitigate the impact from the economic slowdown.**[12] Nevertheless, significant shortcomings in financial transparency and banking supervision complicate the analysis of banking vulnerabilities in Vietnam. The SBV has yet to release financial soundness indicators (FSIs), such as capital adequacy or profitability. Moreover, only a few of the 41 commercial banks publish detailed financial statements and disclose FSIs in their annual reports. There are also gaps in the Vietnamese accounting standards with regard to valuation of financial instruments and fixed assets.

[11] Two SOCBs have large exposure to loans classified as special mention (1–90 days overdue or first time restructured) which require a 5 percent provisioning. These loans could become NPLs, especially in an economic downturn.

[12] Staff's simple credit stress test—based on available market information for 35 banks (out of 41 banks) covering about 95 percent of the domestic banking system (excluding foreign bank branches)—suggests that most banks would remain solvent even if NPLs tripled from current levels and assuming zero profitability.

Discussions

23. **The authorities broadly agreed with staff's assessment of the banking sector and associated risks, but were more sanguine on the outlook.** While recognizing the potential vulnerabilities stemming from an economic downturn, the authorities reiterated that the liquidity-related stresses in the banking system that emerged in mid-2008 had been addressed, and that risks are under control. They noted that JSBs have been closely monitored, in particular the smaller ones considered at risk, and that banks have increased capital and set aside adequate provisions, while strengthening their risk management systems. They added that there have so far been no major bank runs or failures despite the global financial crisis and heightened market volatility.

24. **Staff emphasized the importance of closely monitoring developments and addressing any rising vulnerabilities in the banking system in a timely and effective manner.** Vulnerable banks should be placed under close supervisory watch, and banks should formulate a restructuring plan in the event their capital falls below certain critical levels. Staff also recommended that SOCBs address provisioning shortfalls in a timely manner and cautioned against channeling directed policy lending programs through them. The authorities pointed out that while the SBV is not given a well-defined mandate to intervene in troubled banks, such banks could be handled by measures—such as mergers, withdrawal of licenses, and recapitalization—which have been used in the past.

25. **The authorities acknowledged the importance of developing an effective contingency plan to deal with the impact of the global turmoil.** They indicated that, if needed, necessary measures would be taken to secure financial system stability. In this context, staff noted that a number of countries had prepared such plans, key elements of which include a temporary blanket guarantee covering all bank liabilities to minimize the risk of any runs on deposits,[13] temporary emergency liquidity support to illiquid but solvent banks subject to strict conditions, a broadening of the existing lender of last resort support system, and a restructuring or liquidation of insolvent banks, including through mergers and bank recapitalization with public funds, subject to appropriate and transparent restructuring conditions and safeguards against moral hazard.

26. **It was agreed that banking supervision needs to be further strengthened.** Recent initiatives to undertake large-scale onsite supervision, enforce strict limits on securities-related lending, raise minimum capital requirements for banks, strengthen loan classification and provisioning rules, and apply strict conditions on the provision of liquidity support, have all enhanced the SBV's oversight of the banking system. The decision to tighten criteria and conditions for granting licenses to new banks and to integrate regulatory and supervisory

[13] The existing deposit insurance scheme covers deposits up to 50 million dong (about $3,000) per person per bank, but excludes foreign currency deposits. The current limit covers about 90 percent of depositors.

functions in a single department within the SBV is also welcome. Main priorities going forward include upgrading banks' reporting requirements, introducing stress testing as an offsite supervisory tool, establishing an early warning system, and strengthening the SBV's onsite supervision program. The SBV should also strictly enforce compliance with prudential rules and address gaps in the accounting regulations. The authorities broadly agreed with these priorities and indicated that the new banking supervision department would be able to undertake more effective supervision. In addition, they were hopeful that the Fund's long-term resident advisor would help enhance the SBV's supervisory practices.

27. **Staff urged the authorities to sustain the momentum for financial sector reforms.** The authorities' plan to amend laws on the SBV and credit institutions in 2010 is welcome. Staff underscored the importance of strengthening the SBV's operational autonomy and clearly defining the objectives of monetary policy and banking supervision. In particular, the new SBV law should spell out the SBV's legal authority and operational autonomy, including the power to supervise banks and to intervene in banks, if necessary. The authorities noted that these reforms are currently under discussion and requested IMF support in advancing them.

C. Structural Reform Priorities

Fiscal reform

Background

28. **The authorities have been taking a number of steps to preserve debt sustainability.** Tax reforms include the introduction of a new PIT, and revision of the CIT, VAT, excise taxes, and tariffs on petroleum products. However, these reforms are unlikely to provide adequate revenue support, especially in the short run. On the expenditure side, the authorities are planning to move a significant portion of public investment into public-private partnership projects (PPPs). To ensure fiscal sustainability, the authorities are considering introducing a limit on government debt and balancing the budget in the long run. The authorities are also planning to introduce a new budget law in 2010, which is expected to cover a broad range of issues, including plans to develop a medium-term fiscal framework, reform fiscal decentralization, and introduce performance-based budgeting. The new law may also help address serious fiscal data shortcomings.

Discussions

29. **Staff stressed the importance of a longer-term framework of revenue and expenditure management.** While the recent tax reforms are welcome, staff underscored the need for further efforts to identify alternative revenue sources, particularly in light of anticipated revenue declines associated with WTO commitments and in the longer run a decline in oil production. The authorities agreed with staff's view and requested IMF TA to help develop the next phase of their revenue reform strategy, which will focus on property,

environmental, and natural resource tax laws currently under preparation. They also noted that a large taxpayer office was under consideration, which could increase the tax yield. Staff also recommended that expenditure structure be reviewed to improve the efficiency of public investment while ensuring sufficient protection to vulnerable groups, and cautioned against the fiscal risks arising from contingent liabilities associated with PPPs. Such projects would require a solid investment planning framework, a strong legal and institutional framework, and a clear, comprehensive, and transparent accounting framework. A careful assessment of fiscal and macroeconomic risks associated with PPPs would also be crucial.

30. **The initiative to revise the state budget law is welcome.** Staff called for its careful planning and implementation, especially in the areas of fiscal decentralization and performance-based budgeting, to avoid complicating fiscal management. Bringing the definition of the budget balance closer to international standards, including elimination of off-budget transactions, would facilitate fiscal policy decision-making and help inform the public about fiscal policy stance and direction.

SOE reform

Background

31. **The pace of SOE reform has slowed significantly, and the economic slowdown appears to have weakened its momentum.** There were approximately 1,800 SOEs at the end of 2007, accounting for about 40 percent of GDP and 30 percent of credit to the economy. Assessing the financial position of the SOE sector remains difficult in the absence of information on their performance, but it is expected that the financial position of some of the larger SOEs has come under increased strain in 2008.

Discussions

32. **Staff stressed the need to advance SOE reform.** The authorities should step up the monitoring of SOEs and identify and restructure those representing significant fiscal risks. They should also press ahead with the equitization process (including SOCBs) as market conditions improve, which would help strengthen the performance and governance of SOEs, especially if the participation of foreign strategic investors is broadened. The authorities reiterated their commitment to SOE reform, recognizing that it would help sustain Vietnam's rapid economic development. The authorities explained that the slower-than-expected equitization process was due to unfavorable market conditions and intend to press ahead with their plans to equitize the remaining nonstrategic SOEs.

V. Other Issues

33. **Staff emphasized that an effective public communication strategy will help bolster investor confidence, which is needed especially in the difficult period ahead.** The SBV has taken steps to improve its communication, by providing updated monetary and

reserves data on the Fund's website, posting weekly statements on monetary and banking operations on its newly launched English-language website, and organizing regular press conferences and interviews. Another important step for the SBV is to more clearly communicate its stance on monetary and exchange rate policy to the public. More generally, government agencies should present policy initiatives in a coordinated, consistent, and comprehensive manner.

34. **The authorities should improve the quality and timeliness of data, especially in the fiscal, SOE, and banking sectors.** Higher quality fiscal and SOE data would allow for better analysis of fiscal developments and the policy stance. There is a significant perception gap on the banking sector soundness between the public and the authorities. Posting regularly key financial soundness indicators of the banking system on the SBV's website could help close the gap. The SBV indicated that efforts will be made to provide more information to the public, in line with practices of central banks and regulatory agencies in the region. They also agreed that the provision of financial information of SOEs would help foster a better understanding of their soundness.

VI. Staff Appraisal

35. **Vietnam made significant progress last year in stabilizing an overheating economy, but is now facing substantial challenges amid the volatile global environment.** Growth is expected to slow in 2009. While the current account deficit is likely to remain large, capital inflows would decline significantly. The government has rapidly eased macroeconomic policies and recently announced a broad stimulus plan to support growth. However, Vietnam's fragile external position places a constraint on its ability to pursue expansionary policies.

36. **Against the background of deteriorating growth prospects, an accommodative fiscal stance in 2009 is appropriate.** Given the already substantial domestic financing requirement and the weak external position, however, there is limited room for a fiscal stimulus in the absence of additional concessional external financing. The government should focus on measures that are effective and temporary, while ensuring that these measures are calibrated to fit within available fiscal and macroeconomic space. In this context, the authorities' intention to enhance the social safety net and expedite existing efficient public investment projects is appropriate. However, many tax measures and those to support SMEs may not be effective, and the use of import and export tariffs will cause distortions.

37. **The effects of recent significant policy adjustments should be assessed before monetary conditions are eased further.** Given a stalled credit market, further monetary action may have limited impact on growth, and instead increase depreciation pressures on the dong. To increase policy effectiveness, greater efforts should be made to improve open market operations and liquidity forecasting and management.

38. **A move toward a more flexible exchange rate regime is an appropriate strategy.** Notwithstanding moves to widen the trading band and devalue the exchange rate, the dong

continues to face depreciation pressures. Staff's exchange rate assessment also suggests that the dong is somewhat overvalued compared with its medium-term equilibrium level. If depreciation pressures persist, exchange rate flexibility should be further increased, supported by appropriate macroeconomic policies to maintain confidence in the dong.

39. **Safeguarding banking sector soundness is high priority.** While commendable efforts have been made, the SBV needs to improve supervision further and address vulnerabilities in a timely and effective manner. Having a contingent plan to deal with the global financial turmoil is also useful. Over the medium term, advancing financial sector reform will be crucial, in particular strengthening the SBV's operational autonomy.

40. **A longer-term revenue and expenditure framework will help preserve fiscal sustainability.** While the recent tax reforms are a key step in this direction, further efforts are needed to broaden the tax base. The expenditure structure should be reviewed to increase efficiency of public investment and ensure adequate protection for vulnerable groups. It is also important to minimize risks associated with PPPs. The initiative to revise the state budget law is timely, but requires careful planning and implementation.

41. **The authorities should press ahead with SOE reform.** Given their large role in the economy, efforts should be stepped up to monitor SOEs and identify and restructure those representing significant risks. Continuing the equitization process for SOEs and SOCBs would be critical in helping to improve their efficiency and governance.

42. **An effective public communication strategy and increased data availability will help bolster investor confidence.** While steps have been taken to improve communication and data provision, the quality and timeliness of data, especially in the fiscal, SOE, and banking sectors, need to be strengthened.

43. It is recommended that the next Article IV consultation take place on the standard 12-month cycle.

Table 1. Vietnam: Selected Economic Indicators, 2005–09 1/

Nominal GDP (2008): US$90 billion — GDP per capita (2008): US$1,041
Population (2008, est.): 86.3 million — Fund quota: SDR 329.1 million

	2005	2006	2007	2008	2009
				Est.	Proj.
Real GDP (annual percentage change) 2/	8.4	8.2	8.5	6.2	4.8
Saving and investment (in percent of GDP) 3/					
Gross national saving	34.5	36.5	31.8	31.2	25.1
Private	26.7	28.1	26.2	26.1	23.0
Public	7.8	8.4	5.6	5.1	2.1
Gross investment	35.6	36.8	41.6	41.5	33.2
Private	24.1	26.4	30.3	32.2	24.0
Public	11.5	10.4	11.4	9.3	9.2
Consumer price inflation (annual percentage change) 2/					
Period average	8.3	7.5	8.3	23.1	8.0
End of period	8.8	6.7	12.6	19.9	6.0
GDP deflator	8.2	7.3	8.2	21.7	4.8
General government (in percent of GDP)					
Official fiscal balance	-0.1	1.1	-2.2	-1.6	-4.1
Revenue and grants	27.2	28.7	27.6	27.2	24.0
Expenditure	27.3	27.5	29.8	28.8	28.1
Off-budget expenditure and net lending	4.4	2.2	3.1	3.1	4.1
Overall fiscal balance 4/	-4.5	-1.1	-5.3	-4.7	-8.2
Non-oil primary fiscal balance 4/	-11.7	-8.8	-11.1	-9.4	-9.7
Money and credit (annual percentage change, end of period) 2/					
Broad money (M2)	29.7	33.6	46.1	20.3	19.6
Credit to the economy	31.7	25.4	53.9	25.4	12.9
Interest rates (in percent, end of period) 2/					
Nominal three-month deposit rate (households)	7.8	7.9	7.4	8.1	...
Nominal short-term lending rate (less than one year)	12.0	11.8	11.8	11.5	...
Current account balance (including official transfers)					
(In billions of U.S. dollars)	-0.6	-0.2	-7.0	-9.2	-7.3
(In percent of GDP)	-1.1	-0.3	-9.8	-10.3	-8.1
Exports f.o.b. (annual percentage change, U.S. dollar terms)	22.5	22.7	21.9	29.5	-15.5
Imports f.o.b. (annual percentage change, U.S. dollar terms)	15.0	22.1	38.3	27.6	-19.9
Foreign exchange reserves (in billions of U.S. dollars, end of period)					
Gross official reserves, including gold 2/	8.6	11.5	21.0	23.0	20.7
(In months of next year's imports of GNFS)	2.2	2.1	3.0	4.1	3.3
External debt (in percent of GDP) 5/	32.5	31.4	33.3	29.8	31.9
External debt service (in percent of exports of GNFS)	4.5	4.2	3.8	3.4	4.5
Total public and publicly-guaranteed debt (in percent of GDP)	44.5	44.1	46.3	44.4	47.5
Dong per U.S. dollar exchange rate (end of period) 2/ 6/	15,907	16,068	16,003	17,486	...
Nominal effective exchange rate (end of period) 7/	83.6	77.3	73.3	75.4	...
Real effective exchange rate (end of period) 7/	99.8	96.8	100.5	121.9	...
Memorandum items:					
GDP (in trillions of dong at current market prices)	839	974	1,144	1,479	1,623
Per capita GDP (in U.S. dollars)	636	722	835	1,041	1,035

Sources: Data provided by the Vietnamese authorities; and IMF staff estimates and projections.

1/ Figures in 2008-09 are staff estimates and projections unless otherwise indicated. Projections for 2009 do not take into account the recently announced stimulus plan.

2/ Figures for 2008 are actual.

3/ The private sector includes state-owned enterprises.

4/ Includes off-budget expenditure and net lending.

5/ Includes private debt.

6/ Interbank exchange rate.

7/ 2000 annual average=100.

Table 2. Vietnam: Balance of Payments, 2005–09

	2005	2006	2007	2008	2009
				Est.	Proj.
	(In millions of U.S. dollars, unless otherwise indicated)				
Current account balance	-560	-164	-6,992	-9,238	-7,318
Trade balance	-2,439	-2,776	-10,360	-12,284	-7,074
Exports, f.o.b.	32,447	39,826	48,561	62,906	53,167
Of which: Oil	7,387	8,265	8,488	10,450	4,687
Imports, f.o.b.	34,886	42,602	58,921	75,189	60,241
Of which: Oil	4,716	5,665	7,248	10,181	4,152
Non-factor services (net)	-296	-8	-894	-2,315	-1,858
Receipts	4,176	5,100	6,030	6,300	5,500
Payments	4,472	5,108	6,924	8,615	7,358
Investment income (net)	-1,205	-1,429	-2,168	-1,969	-2,486
Receipts	364	668	1,093	1,068	364
Payments	1,569	2,097	3,261	3,037	2,850
Transfers (net)	3,380	4,049	6,430	7,330	4,100
Private	3,150	3,800	6,180	7,000	3,800
Official	230	249	250	330	300
Financial account balance	3,087	3,088	17,540	9,175	5,024
Net foreign direct investment (FDI)	1,889	2,315	6,550	7,800	4,000
Medium- and long-term loans (net)	921	1,025	2,045	919	1,324
Disbursements	2,031	2,260	3,397	2,461	2,987
Amortization	1,110	1,235	1,352	1,542	1,663
Portfolio investment	865	1,313	6,243	-400	0
Short-term capital (net)	-588	-1,565	2,702	856	-300
Net foreign assets of commercial banks	-634	-1,535	2,623	500	-300
Net trade credit	46	-30	79	356	0
Errors and omissions	-396	1,398	-349	-100	0
Overall balance	2,131	4,322	10,199	-162	-2,295
Memorandum items:					
Gross official reserves (excluding government deposits)	8,557	11,491	20,964	23,022	20,727
(In months of next year's imports)	2.2	2.1	3.0	4.1	3.3
Current account balance (in percent of GDP)	-1.1	-0.3	-9.8	-10.3	-8.1
(Excluding FDI)	2.5	3.5	-0.6	-1.6	-3.7
Trade balance (in percent of GDP)	-4.6	-4.6	-14.6	-13.7	-7.8
Non-oil current account balance (in percent of GDP)	-6.1	-4.5	-11.6	-10.6	-8.7
Export value (annual percentage change)	22.5	22.7	21.9	29.5	-15.5
Export volume (annual percentage change)	7.6	14.4	13.7	7.2	3.5
Import value (annual percentage change)	15.0	22.1	38.3	27.6	-19.9
Import volume (annual percentage change)	7.1	17.3	34.9	13.3	-6.8
Non-oil export value (annual percentage change)	20.4	25.9	27.0	30.9	-7.6
Non-oil import value (annual percentage change)	12.0	22.4	39.9	25.8	-13.7

Sources: Data provided by the Vietnamese authorities; and IMF staff estimates and projections.

Table 3: Vietnam: General Government Budgetary Operations, 2005–09 1/

	2005	2006	2007	2008		2009
			Est.	Budget	Est. 2/	Proj. 3/
			(In trillions of dong)			
Total revenue and grants	228.3	279.5	315.9	323.0	401.6	389.5
Revenues	224.5	271.6	311.7	319.4	396.6	384.5
Tax revenue	191.7	236.3	265.9	287.4	349.0	332.2
Oil revenues	66.6	83.3	77.0	65.6	85.8	50.6
Non-oil revenues	125.2	153.0	188.9	221.8	263.2	281.6
Non-tax and capital revenues	32.8	35.2	45.8	32.0	47.7	52.3
Grants	3.8	7.9	4.3	3.6	5.0	5.0
Total expenditure	229.1	268.4	341.4	364.0	425.3	456.6
Current expenditure 4/	149.9	180.1	229.3	264.3	307.5	343.8
Capital expenditure	79.2	88.3	112.2	99.7	117.8	112.8
Official fiscal balance	-0.8	11.1	-25.5	-41.0	-23.6	-67.0
Off-budget expenditure and net lending	37.1	21.8	35.4	70.2	45.6	71.6
Net lending	20.2	9.0	17.4	33.2	25.6	35.6
Of which: ODA financed	4.7	4.7	7.3	12.8	7.8	9.2
VDB net lending	3.7	4.3	10.0	13.4	17.8	26.4
Off-budget investment expenditure	16.9	12.8	18.0	37.0	20.0	36.0
Overall fiscal balance	-37.9	-10.8	-60.9	-111.2	-69.2	-138.7
Discrepancy	-7.3	-1.6	27.6	0.0	0.0	0.0
Financing	45.2	12.4	33.3	111.2	69.2	138.7
Domestic (net)	24.0	-1.2	18.5	90.1	52.5	114.9
Foreign (net)	21.3	13.6	14.8	21.1	16.7	23.8
			(In percent of GDP)			
Total revenue and grants	27.2	28.7	27.6	24.1	27.2	24.0
Revenues	26.8	27.9	27.2	23.9	26.8	23.7
Tax revenue	22.8	24.3	23.2	21.5	23.6	20.5
Oil revenues	7.9	8.6	6.7	4.9	5.8	3.1
Non-oil revenues	14.9	15.7	16.5	16.6	17.8	17.3
Non-tax and capital revenue	3.9	3.6	4.0	2.4	3.2	3.2
Grants	0.5	0.8	0.4	0.3	0.3	0.3
Total expenditure	27.3	27.5	29.8	27.2	28.8	28.1
Current expenditure 4/	17.9	18.5	20.0	19.8	20.8	21.2
Capital expenditure	9.4	9.1	9.8	7.5	8.0	6.9
Official fiscal balance	-0.1	1.1	-2.2	-3.1	-1.6	-4.1
Off-budget expenditure and net lending	4.4	2.2	3.1	5.2	3.1	4.1
Net lending	2.4	0.9	1.5	2.5	1.7	1.9
Of which: ODA financed	0.6	0.5	0.6	1.0	0.5	0.3
VDB net lending	0.4	0.4	0.9	1.0	1.2	1.6
Off-budget investment expenditure	2.0	1.3	1.6	2.8	1.4	2.2
Overall fiscal balance	-4.5	-1.1	-5.3	-8.3	-4.7	-8.2
Discrepancy	-0.9	-0.2	2.1	0.0	0.0	0.0
Financing	5.4	1.3	3.2	8.3	4.7	8.2
Domestic (net)	2.9	-0.1	1.6	6.7	3.5	6.8
Foreign (net)	2.5	1.4	1.6	1.6	1.1	1.5
Memorandum items:						
Overall fiscal balance excluding net lending (in percent of GDP)	-2.1	-0.2	-3.8	-5.8	-2.9	-6.3
Non-oil primary fiscal balance (in percent of GDP)	-11.7	-8.8	-11.1	-12.1	-9.4	-9.7
Nominal GDP (in trillions of dong)	839.2	974.3	1,144.0	1,338.0	1,478.7	1,623.3
Oil price (in U.S. dollars per barrel)	53.0	61.8	71.1	64.0	97.0	50.0
Domestic revenue excluding oil revenue and grants (in trillions of dong)	119.8	145.4	174.3	189.3	219.5	231.4
Customs revenue (in trillions of dong)	38.1	42.8	60.4	64.5	91.4	102.5

Sources: Data provided by the Vietnamese authorities; and IMF staff estimates and projections.

1/ Based on IMF definition.

2/ Estimates for 2008 Q4 are not available yet. The estimate for 2008 is based on budget execution through September, authorities' estimates of Q4 expenditure, and staff revenue estimates.

3/ The projection for 2009 is based on the authorities' expenditure plan (excluding net lending financed by sovereign bond issuance) and staff revenue projection. This projection does not take into account the recently announced stimulus plan.

4/ Budget data include the amount allocated as contingency.

Table 4. Vietnam: Medium-Term Scenario, 2005–13

	2005	2006	2007	2008	2009	2010	2011	2012	2013
				Est.	Projection				
	(Percentage change)								
Real GDP (annual percentage change)	8.4	8.2	8.5	6.2	4.8	5.8	7.0	7.4	7.4
Nominal GDP (in trillions of dong)	839	974	1,144	1,479	1,623	1,844	2,100	2,392	2,724
Consumer prices (annual average)	8.4	7.5	8.3	23.1	8.0	6.0	6.0	6.0	6.0
Consumer price (end of period)	8.8	6.7	12.6	19.9	6.0	6.0	6.0	6.0	6.0
GDP deflator	8.2	7.3	8.2	21.7	4.8	7.3	6.5	6.1	6.0
	(In percent of GDP)								
Saving-investment balance	-1.1	-0.3	-9.8	-10.3	-8.1	-6.8	-6.3	-5.6	-4.9
Gross national saving	34.5	36.5	31.8	31.2	25.1	26.8	27.5	28.0	28.6
Private saving	26.7	28.1	26.2	26.1	23.0	24.6	25.3	25.7	26.3
Public saving	7.8	8.4	5.6	5.1	2.1	2.2	2.2	2.3	2.3
Gross investment	35.6	36.8	41.6	41.5	33.2	33.6	33.8	33.6	33.5
Private investment	24.1	26.4	30.3	32.2	24.0	25.9	26.8	26.7	26.8
Public investment	11.5	10.4	11.4	9.3	9.2	7.7	7.1	6.9	6.7
General government fiscal balance	-4.5	-1.1	-5.3	-4.7	-8.2	-6.5	-5.8	-5.4	-5.0
(Excluding off-budget expenditure and net lending)	-0.1	1.1	-2.2	-1.6	-4.1	-3.6	-3.1	-3.1	-3.1
Non-oil primary fiscal balance	-11.7	-8.8	-11.1	-9.4	-9.7	-8.1	-7.3	-6.5	-5.8
Total revenue and grants	27.2	28.7	27.6	27.2	24.0	24.4	24.7	24.8	25.0
Revenue	26.8	27.9	27.2	26.8	23.7	24.1	24.4	24.5	24.7
Of which: Oil revenue	7.9	8.6	6.7	5.8	3.1	3.2	3.2	2.9	2.6
Grants	0.5	0.8	0.4	0.3	0.3	0.3	0.3	0.3	0.3
Total expenditure	31.7	29.8	32.9	31.8	32.2	30.9	30.5	30.2	30.0
Current expenditure	17.9	18.5	20.0	20.8	21.2	21.6	21.9	22.0	22.2
Capital expenditure	9.4	9.1	9.8	8.0	6.9	6.4	5.9	5.9	5.9
Off-budget expenditure and net lending	4.4	2.2	3.1	3.1	4.1	2.9	2.7	2.3	1.9
	(In billions of U.S. dollars; unless otherwise indicated)								
Current account balance	-0.6	-0.2	-7.0	-9.2	-7.3	-6.7	-6.8	-6.6	-6.2
(In percent of GDP)	-1.1	-0.3	-9.8	-10.3	-8.1	-6.8	-6.3	-5.6	-4.9
Trade balance	-2.4	-2.8	-10.4	-12.3	-7.1	-6.5	-6.9	-6.7	-6.3
Exports (f.o.b.)	32.4	39.8	48.6	62.9	53.2	61.7	72.8	86.3	102.6
(Percentage change)	22.5	22.7	21.9	29.5	-15.5	16.0	18.0	18.5	18.9
Imports (f.o.b.)	34.9	42.6	58.9	75.2	60.2	68.2	79.7	93.0	108.9
(Percentage change)	15.0	22.1	38.3	27.6	-19.9	13.1	16.9	16.7	17.1
Net services and transfers (including investment income)	1.9	2.6	3.4	3.0	-0.2	-0.2	0.1	0.2	0.1
Of which: Private transfers	3.2	3.8	6.2	7.0	3.8	4.1	4.5	5.1	5.8
Capital and financial account (net)	3.1	3.1	17.5	9.2	5.0	6.8	8.5	9.3	10.4
Direct investment	1.9	2.3	6.6	7.8	4.0	4.4	5.1	5.6	6.1
Portfolio investment	0.9	1.3	6.2	-0.4	0.0	0.7	1.5	1.7	1.8
Medium- and long-term loans	0.9	1.0	2.0	0.9	1.3	1.1	1.0	1.1	1.4
Of which: ODA disbursements	1.0	1.3	1.3	1.4	1.7	1.8	1.9	1.9	2.0
Short-term capital (net)	-0.6	-1.6	2.7	0.9	-0.3	0.6	0.9	1.0	1.1
Memorandum items:									
Gross official reserves (in billions of U.S. dollars)	8.6	11.5	21.0	23.0	20.7	20.8	22.5	25.2	29.5
(In months of next year's imports of GNFS)	2.2	2.1	3.0	4.1	3.3	2.8	2.6	2.5	2.5
External debt service payments (in billions of U.S. dollars)	1.6	1.9	2.1	2.4	2.7	3.4	3.9	4.2	4.6
(In percent of exports of GNFS)	4.5	4.2	3.8	3.4	4.5	5.0	4.8	4.4	4.1
Total external debt (in billions U.S. dollars)	17.2	19.1	23.7	26.8	28.9	31.1	33.4	35.9	38.9
(In percent of GDP)	32.5	31.4	33.3	29.8	31.9	31.7	31.2	30.7	30.4
Total public debt (in percent of GDP)	44.5	44.1	46.3	44.4	47.5	49.2	50.3	50.7	50.5
Domestic	17.6	18.2	19.5	19.7	21.6	23.5	25.5	27.0	28.0
External	26.9	25.8	26.8	24.7	26.0	25.7	24.8	23.7	22.6
Nominal GDP (in billions of U.S. dollars)	52.9	60.9	71.1	89.9	90.6	98.0	106.8	117.0	128.1

Sources: Data provided by the Vietnamese authorities; and IMF staff estimates and projections.

Table 5. Vietnam: Indicators of External and Financial Vulnerability, 2003–08

	2003	2004	2005	2006	2007	2008	
							Date
Financial indicators							
Broad money (M2, annual percentage change)	24.9	29.5	29.7	33.6	46.1	18.8	Dec-08
Credit to the economy (annual percentage change)	28.4	41.6	31.7	25.4	53.9	32.9	Dec-08
External indicators							
Exports value growth (in percent)	20.6	31.4	22.5	22.7	21.9	29.5	Est.
Imports value growth (in percent)	28.0	33.5	15.0	22.1	38.3	27.6	Est.
Terms of trade (percent change, 12-month basis)	5.7	2.2	5.7	3.4	3.6	6.7	Est.
Current account balance (in percent of GDP, including							Est.
official transfers)	-4.9	-3.5	-1.1	-0.3	-9.8	-10.3	
Capital and financial account balance (in billions of U.S. dollars)	3.3	2.8	3.1	3.1	17.5	9.2	Est.
Of which:							
Foreign direct investment	1.5	1.6	1.9	2.3	6.6	7.8	Est.
Portfolio investment	0.0	0.0	0.9	1.3	6.2	-0.4	Est.
Medium- and long-term loans	0.5	1.2	0.9	1.0	2.0	0.9	Est.
Short-term capital	1.4	0.0	-0.6	-1.6	2.7	0.9	Est.
Gross official reserves, including gold (in billions of U.S. dollars)	5.6	6.3	8.6	11.5	21.0	23.0	Dec-08
(In months of next year's imports of goods and nonfactor services)	2.0	1.9	2.2	2.1	3.0	4.1	Est.
Broad money (M2) to reserves	4.7	5.3	5.1	5.0	4.0	4.0	Dec-08
Reserves to total short-term external debt (residual maturity)	5.2	5.0	6.0	7.6	11.7	11.5	Est.
Total external debt (in billions of U.S. dollars)	14.2	16.9	17.2	19.1	23.7	26.8	Est.
Total external debt (in percent of GDP)	36.3	37.2	32.5	31.4	33.3	29.8	Est.
Of which: Public debt	29.0	29.7	26.9	25.8	26.8	24.7	Est.
Of which: Short-term debt	0.5	0.3	0.3	0.2	0.3	0.4	Est.
Total external debt to exports of GNFS (in percent)	60.8	55.6	47.0	42.6	43.4	38.7	Est.
Total external debt service to exports of GNFS (in percent)	6.0	3.9	4.5	4.2	3.8	3.4	Est.
External interest payments to GNFS	1.3	1.0	1.4	1.4	1.3	1.2	Est.
External amortization payments to GNFS	4.6	2.9	3.1	2.8	2.5	2.3	Est.
Exchange rate (per U.S. dollar, period average) 1/	15,638	15,774	15,907	16,068	16,003	17,486	Dec-08
REER appreciation (end of period, annual percentage change) 2/	-8.8	1.2	13.1	-2.9	3.8	21.3	Dec-08
Financial market indicators							
Stock market index (end period)	166.9	239.3	307.5	751.8	927.0	315.6	Dec-08
Stock market index (annual percentage change)	-8.9	43.3	28.5	144.5	23.3	-66.0	Dec-08

Sources: Data provided by the Vietnamese authorities; and IMF staff estimates and projections.

1/ Interbank market rate.
2/ Positive indicates appreciation.

Table 6. Vietnam: Monetary Survey, 2005–09 1/

	2005	2006	2007	2008				2009
	Dec.	Dec.	Dec.	Mar.	Jun.	Sep.	Dec.	Dec. Proj.
	(In trillions of dong)							
Net foreign assets	191.1	287.9	410.4	401.6	388.0	418.9	428.9	426.6
Foreign assets	220.5	327.0	472.3	502.1	501.1	520.3	521.6	...
Foreign liabilities	-29.4	-39.1	-61.9	-100.5	-113.1	-101.3	-92.7	...
Net domestic assets	499.6	634.7	937.8	996.7	1,016.6	1,040.9	1,193.2	1,513.0
Domestic credit	585.6	730.3	1,096.8	1,195.0	1,249.1	1,248.5	1,400.7	1,670.5
Net claims on government	32.5	36.5	29.1	-10.0	-13.5	-18.2	61.4	158.2
Of which: Government deposits	42.7	64.7	89.8	118.8	129.9	135.4	100.7	...
Credit to the economy	553.1	693.8	1,067.7	1,205.0	1,262.5	1,266.7	1,339.3	1,512.2
Of which: In foreign currency	134.3	146.4	228.5	270.5	276.1	274.6	268.7	...
Of which: By nonstate banks	144.8	219.1	444.2	534.6	570.6	554.7	575.9	...
Of which: By state-owned commercial banks	408.3	474.7	623.5	670.4	691.9	712.0	763.3	...
Claims on state-owned enterprises	181.3	218.5	334.2	374.8	391.4	392.8	413.8	...
Claims on other sectors	371.8	475.3	733.5	830.2	871.2	874.2	925.5	...
Other items, net	-86.0	-95.6	-159.0	-198.3	-232.5	-207.6	-207.5	-157.5
Total liquidity (M2)	690.7	922.7	1,348.2	1,398.3	1,404.6	1,459.8	1,622.1	1,939.6
Of which: Total deposits	559.5	763.9	1,127.7	1,175.4	1,210.9	1,279.9	1,385.3	...
Of which: Economic entities	273.3	361.8	592.2	574.4	571.8	589.1	675.6	...
Of which: Households	255.0	333.7	461.1	522.8	549.9	599.1	620.2	...
Dong liquidity	531.5	723.2	1,089.6	1,141.7	1,105.5	1,131.3	1,291.8	...
Of which: Currency outside banks	131.2	158.8	220.5	222.9	193.7	179.9	236.8	...
Of which: Deposits	400.3	564.4	869.1	918.8	911.8	951.4	1,054.9	...
Foreign currency deposits	159.2	199.5	258.6	256.6	299.1	328.6	330.4	...
	(Annual percentage change)							
Total liquidity (M2)	29.7	33.6	46.1	35.7	25.7	21.8	20.3	19.6
Of which: Total deposits	32.2	36.5	47.6	37.2	27.9	26.3	22.8	...
Of which: Economic entities	29.7	32.4	63.7	37.1	18.4	16.4	14.1	...
Of which: Households	37.1	30.9	38.2	41.1	39.5	36.4	34.5	...
Dong liquidity	32.0	36.1	50.7	37.8	24.0	17.3	18.6	...
Of which: Currency outside banks	20.2	21.1	38.9	28.1	13.8	-2.8	7.4	...
Of which: Deposits	36.3	41.0	54.0	40.4	26.4	22.0	21.4	...
Foreign currency deposits	22.8	25.3	29.7	26.9	32.5	40.7	27.7	...
Net foreign assets	31.0	50.7	42.5	17.6	1.8	4.2	4.5	-0.5
Net claims on government	123.5	12.4	-20.4	-137.8	-185.3	-218.0	111.5	157.6
Credit to the economy	31.7	25.4	53.9	63.2	54.4	39.5	25.4	12.9
Of which: In foreign currency	28.5	9.0	56.1	66.3	51.7	36.6	17.6	...
Of which: By nonstate banks	39.6	51.3	102.7	116.9	93.5	59.7	29.6	...
Of which: By state-owned commercial banks	29.1	16.3	31.3	36.3	32.3	26.9	22.4	...
Claims on state-owned enterprises	...	20.5	53.0	61.7	52.6	38.0	23.8	...
Claims on other sectors	...	27.8	54.3	63.9	55.2	40.2	26.2	...
Memorandum items:								
Money multiplier 2/	4.0	4.0	4.3	4.3	4.6	4.5	4.3	4.9
Velocity of M2	1.2	1.1	0.8	1.1	1.0	1.0	0.9	0.9
Currency to total deposits (in percent)	23.4	20.8	19.6	19.0	16.0	14.1	17.1	...
Foreign currency deposits to total deposits (in percent)	28.5	26.1	22.9	21.8	24.7	25.7	23.8	...
Foreign currency loans to total loans (in percent)	24.3	21.1	21.4	22.5	21.9	21.7	20.1	...
Gross official reserves (in billions of U.S. dollars)	8.6	11.5	21.0	23.5	21.0	23.6	23.0	20.7
NFA of the banking system (in billions of U.S. dollars)	12.0	17.9	25.5	25.2	23.5	25.4	25.2	23.2

Sources: State Bank of Vietnam; and IMF staff estimates and projections.

1/ Data include the State Bank of Vietnam and all deposit-taking credit institutions.

2/ Money multiplier is measured as the ratio of total liquidity (M2) to reserve money.

Table 7. Vietnam: Interest Rates, 2006–09

(In percent per annum, average)

	Base 1/	Refinance 1/	Repo 1/ 7-day	Interbank Overnight	Interbank 1-month	Interbank 3-month	Lending 1-year	Deposit 3-month	Bond Yield 1-year
Jan-06	8.3	6.5	…	6.4	7.5	7.9	11.8	7.8	…
Feb-06	8.3	6.5	…	5.9	7.4	7.9	11.8	7.9	…
Mar-06	8.3	6.5	6.1	5.9	7.3	8.0	11.8	7.9	…
Apr-06	8.3	6.5	…	6.0	7.2	8.0	11.8	7.9	…
May-06	8.3	6.5	…	6.0	7.2	7.9	11.8	7.8	…
Jun-06	8.3	6.5	…	6.0	7.2	7.9	11.8	7.9	…
Jul-06	8.3	6.5	…	6.1	7.2	7.9	11.8	7.9	6.0
Aug-06	8.3	6.5	…	5.8	7.1	7.8	11.8	7.9	6.1
Sep-06	8.3	6.5	…	6.0	7.1	7.7	11.8	7.9	6.3
Oct-06	8.3	6.5	…	6.1	7.1	7.9	11.8	7.9	7.7
Nov-06	8.3	6.5	…	6.6	7.5	8.2	11.8	7.9	7.8
Dec-06	8.3	6.5	8.5	7.1	8.1	8.5	11.8	7.9	7.8
Jan-07	8.3	6.5	…	7.2	8.3	8.7	11.8	8.0	7.8
Feb-07	8.3	6.5	…	5.7	7.7	8.1	11.8	8.0	7.4
Mar-07	8.3	6.5	…	4.4	6.1	7.3	11.8	7.9	6.8
Apr-07	8.3	6.5	…	4.2	5.9	7.1	11.8	7.9	6.6
May-07	8.3	6.5	…	4.0	5.8	7.1	11.8	7.9	6.8
Jun-07	8.3	6.5	…	5.8	7.1	7.9	11.8	7.7	6.7
Jul-07	8.3	6.5	…	4.0	5.9	7.0	11.8	7.7	7.0
Aug-07	8.3	6.5	…	3.6	5.5	6.7	11.8	7.7	7.1
Sep-07	8.3	6.5	…	5.6	7.0	7.8	11.8	7.7	7.4
Oct-07	8.3	6.5	…	5.7	6.9	7.9	11.8	7.7	7.4
Nov-07	8.3	6.5	7.5	6.9	7.9	8.5	11.8	7.7	7.5
Dec-07	8.3	6.5	8.0	6.5	8.3	8.9	11.8	7.4	7.8
Jan-08	8.8	7.5	9.5	7.9	9.0	9.1	11.8	7.4	7.6
Feb-08	8.8	7.5	8.0	9.1	10.2	9.9	11.8	9.3	7.5
Mar-08	8.8	7.5	9.0	6.1	9.2	9.9	15.6	11.9	7.4
Apr-08	8.8	7.5	10.5	9.1	11.0	11.1	15.2	12.1	8.1
May-08	12.0	13.0	12.0	11.2	13.7	14.1	18.0	14.0	11.3
Jun-08	14.0	15.0	15.0	14.6	17.2	17.6	21.2	18.0	19.9
Jul-08	14.0	15.0	15.0	16.2	18.9	19.3	22.2	17.2	20.0
Aug-08	14.0	15.0	15.0	15.7	18.5	19.2	22.2	18.6	17.6
Sep-08	14.0	15.0	15.0	14.3	17.3	18.2	21.8	18.3	16.8
Oct-08	13.0	14.0	13.5	12.1	15.4	16.9	19.6	16.4	16.7
Nov-08	12.0	13.0	11.0	8.7	11.9	14.1	14.1	10.5	13.3
Dec-08	8.5	9.5	9.0	7.3	9.9	11.6	11.5	8.1	10.5
Jan-09	8.5	9.5	8.0	5.2	7.3	8.5	10.6	7.2	8.9
Feb-09	7.0	8.0	7.5	6.1	7.5	8.1	…	…	8.3

Sources: State Bank of Vietnam; and Reuters.

1/ End of period.

Table 8. Vietnam: Key Financial Soundness Indicators, 2006–08 1/

(In percent, unless otherwise specified)

	State-Owned Commercial Banks 2/				Nonstate Banks				Total			
	2006	2007	2008		2006	2007	2008		2006	2007	2008	
			Sep.	Oct.			Sep.	Oct.			Sep.	Oct.
Size and balance sheet structure												
Assets (in trillions of dong)	732	904	1,007	1,010	431	904	1,017	1,031	1,162	1,808	2,023	2,041
Market share	62.9	50.0	49.8	49.5	37.1	50.0	50.2	50.5	…	…	…	…
Loans-to-assets ratio	60.2	63.5	64.4	64.4	50.9	49.1	54.6	53.6	56.8	56.3	59.4	59.0
Total loans (in trillions of dong)	441	574	648	651	219	444	555	553	660	1,018	1,203	1,203
Total deposits (in trillions of dong)	562	698	752	769	237	473	581	584	799	1,171	1,333	1,352
Balance sheet growth												
Loan growth (year-on-year)	15.5	30.3	25.0	21.5	51.3	102.7	59.7	46.8	25.9	54.4	38.9	31.9
Deposit growth (year-on year)	28.9	24.1	12.1	12.5	59.8	99.5	48.2	39.2	35.5	46.5	25.4	22.7
Capital adequacy												
Capital to total assets 3/	4.1	5.1	5.1	5.1	10.7	10.2	12.8	12.6	6.1	7.1	8.2	8.2
Asset quality and provisioning coverage												
Nonperforming loans (NPLs) to total loans	3.2	1.9	3.9	4.0	1.3	1.0	1.5	1.7	2.6	1.5	2.8	3.0
Foreign currency NPLs to total NPLs	18.9	15.2	16.0	13.7	20.6	18.8	15.7	15.2	19.2	16.2	15.9	14.1
Provisions to NPLs	40.6	113.4	74.4	74.9	87.3	111.4	102.5	100.8	48.6	112.8	81.4	81.7
NPLs net of provisions to capital	28.8	-3.3	13.1	13.5	0.9	-0.6	-0.2	-0.1	12.4	-1.5	3.8	3.9
Provisions to total loans	1.3	2.1	2.9	3.0	1.2	1.1	1.5	1.7	1.2	1.7	2.3	2.4
Liquidity risk												
Total loans to deposits	78.4	82.3	86.2	84.7	92.4	93.9	95.5	94.7	82.5	87.0	90.3	89.0
Liquid assets to total assets 4/	14.7	16.3	17.2	14.9	13.9	9.7	11.9	12.2	14.4	13.0	14.5	13.5
Liquid assets to short-term liabilities 5/	15.8	17.6	18.8	16.4	16.8	11.9	14.4	15.4	16.1	15.0	16.7	15.9
Interbank borrowing to total loans	8.8	7.6	8.3	7.1	44.3	49.9	28.7	27.9	20.6	26.1	17.8	16.7
Interbank borrowing to total deposits	7.4	6.7	7.7	6.5	41.1	46.9	27.5	26.4	17.8	23.5	16.7	15.5
Foreign liabilities to total liabilities 6/	1.6	1.6	2.5	2.1	5.6	5.2	8.1	8.1	3.0	3.4	5.2	5.1
Foreign exchange rate risk												
Foreign currency loans to total loans	17.6	18.2	17.0	16.6	31.3	27.9	29.6	29.5	22.2	22.4	22.8	22.5
Foreign currency deposits to total deposits	22.7	21.1	23.4	21.9	34.0	25.9	29.1	29.4	26.0	23.0	25.9	25.1
Foreign currency assets to total assets	22.6	19.1	21.6	18.8	32.9	22.7	29.1	27.4	26.4	20.9	25.4	23.2
Foreign currency liabilities to total liabilities	21.9	21.0	24.3	21.7	30.3	22.0	30.7	29.6	24.9	21.5	27.4	25.6
Net open foreign currency position to capital	43.7	-10.0	-19.2	-29.7	59.7	30.6	19.5	13.0	53.1	16.7	7.9	0.4

Sources: State Bank of Vietnam (SBV) data; and IMF staff estimates.

1/ The SBV does not report financial soundness indicators (FSIs). The FSIs are constructed from the balance sheet information of the consolidated banking sector.

2/ Excludes Mekong Housing Bank.

3/ Includes shareholder capital and retained earnings. Excludes provisioning. Assets are not risk-weighted.

4/ Liquid assets comprise cash, foreign currency and gold holdings, deposits at other banks, deposits at the SBV, and SBV bills. Excludes holdings of government securities. Five percent of liquid assets can be held in government securities.

5/ Short-term liabilities include all deposits, interbank borrowing, and SBV borrowing.

6/ Foreign liabilities are claims by non-residents on banks, both in domestic and foreign currency.

INTERNATIONAL MONETARY FUND AND
INTERNATIONAL DEVELOPMENT ASSOCIATION

VIETNAM

Joint IMF/World Bank Debt Sustainability Analysis 2008[1]

Prepared by the staffs of the International Monetary Fund and
the International Development Association

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This document presents the joint IMF-World Bank debt sustainability analysis (DSA) for Vietnam using the Debt Sustainability Framework for Low-Income Countries (LIC).[2] *Vietnam remains at low risk of debt distress despite the recent deterioration in its economic conditions and the global downturn.*[3] *All external debt sustainability indicators are projected to remain well below the applicable debt thresholds, reflecting Vietnam's mostly concessional and long-term structure of external debt, as well as its dynamic export sector. The outlook of public sector debt (including domestic debt) is less favorable, underscoring the need for fiscal consolidation to preserve debt sustainability in the medium term.*

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[1] This DSA was prepared jointly by the IMF and World Bank. The staffs also consulted with the Asian Development Bank. The debt data underlying this exercise were provided by the Vietnamese authorities and donor partners. Data for end-2008 and beyond are staff estimates.

[2] See "Debt Sustainability in Low-Income Countries: Proposal for an Operational Framework and Policy Implications" (www.imf.org/external/np/pdr/sustain/2004/020304.htm and IDA/SECM2004/0035, 2/3/04) and "Debt Sustainability in Low-Income Countries: Further Considerations on an Operational Framework, Policy Implications" (www.imf.org/external/np/pdr/sustain/2004/091004.htm and IDA/SECM2004/0629, 9/10/04) and "Applying the Debt Sustainability Framework for Low-Income Countries Post Debt Relief" (www.imf.org/external/np/pp/eng/2006/110606.pdf and IDA/SecM2006–0564, 8/11/06).

[3] The low-income country debt sustainability framework (LIC DSF) recognizes that better policies and institutions allow countries to manage higher levels of debt, and thus the threshold levels are policy dependent. Vietnam's policies and institutions, as measured by the World Bank's Country Policy and Institutional Assessment (CPIA), averaged 3.8 percent over the past three years, placing it as a "strong performer." The relevant indicative thresholds for this category are: 50 percent for the present value (PV) of debt-to-GDP ratio, 200 percent for the PV of debt-to-exports ratio, 300 percent for the PV of debt-to-revenue ratio, 25 percent for the debt service-to-exports ratio, and 35 percent for the debt service-to-revenue ratio. These thresholds are applicable to public- and publicly-guaranteed external debt.

I. Background and Baseline Assumptions

1. **Vietnam's external debt position has historically been robust.** Most of its debt is concessional, carrying a low average, fixed interest rate, and long maturity with no bunching of repayments. With support from a variety of multilateral and bilateral creditors,[4] it also has a fairly diversified currency composition. Vietnam has access to strong private remittances, which help to finance its trade deficit, and large foreign direct investment (FDI) inflows which provide significant non-debt-creating financing. The stock market has also received strong inflows until recently. Moreover, the government has been prudent in external borrowing, with total external public debt estimated at 25 percent of GDP (30 percent including the private sector) in 2008.

2. **The domestic public debt position also remains manageable.** Total domestic public debt (including Vietnam Development Bank) is estimated at only 19.7 percent of GDP at end-2008. The average implied interest rate as of end-2008 was about 6 percent, although this is expected to rise in nominal terms because of higher inflation. The bulk of amortization will fall due within one to three years.

3. **The assessment of Vietnam's debt situation has not changed significantly since the last DSA despite the recent deterioration in economic conditions.** External borrowing has been limited, as the larger current account deficit has been largely financed by higher FDI inflows and some short-term borrowing by banks. Domestic financing of the government deficit is estimated to have risen by about 2 percentage points of GDP to 3½ percent of GDP in 2008. However, government borrowing could be much less if the bulk of the deficit were financed by drawing down the government's sizeable deposits.

4. **The main baseline assumptions underlying the DSA are summarized in Box 1.** A critical assumption is that Vietnam will continue to pursue sound macroeconomic and financial policies and structural reforms to support growth and continue further poverty reduction. Based on these assumptions, the non-interest current account deficit is projected to decline from about 9½ percent of GDP in 2008 to about 4 percent in 2013 and remain broadly unchanged thereafter.

II. External Debt Sustainability Analysis[5]

5. **Public- and publicly-guaranteed (PPG) external debt is likely to remain manageable, with all external debt ratios projected to be well within the indicative thresholds.** Although the current account deficit has increased markedly since the last DSA, non-debt-creating financing has also risen considerably. Higher GDP in dollar terms also

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[4] Information on Vietnam's creditors can be found in the Ministry of Finance's External Debt Bulletin at www.mof.gov.vn.

[5] This analysis focuses on PPG external debt, which accounts for about 80 percent of total external debt.

contributes to the lower ratios. Exports were strong, aided by the global commodity price boom (although the boom has since reversed, with the new lower commodity price projections incorporated into the baseline). Finally, the ratio of short-term external debt (measured on the basis of remaining maturity) is under 10 percent of gross foreign exchange reserves, indicating resilience in the face of sudden capital withdrawals.

Policy-Based External Debt Burden Thresholds for Vietnam

	Thresholds	Vietnam's Ratios 2007	2008–28 1/
PV of debt in percent of:			
GDP	50	17	16
Exports	200	22	19
Revenues	300	63	64
Debt service in percent of:			
Exports	25	4	4
Revenues	35	8	7

Sources: Vietnamese authorities; and IMF staff estimates.
1/ Average for the period, under the baseline scenario.

Box 1: Key Macroeconomic Assumptions for Baseline Scenario (2009–28)

Real GDP growth will average 6½ percent per year during 2009–13 (below the 10-year historical average of 7.2 percent), and thereafter will decline gradually, as Vietnam's level of development and demography begins to converge to those of more advanced neighbors. Gross domestic investment is expected to decline from 41½ percent of GDP in 2008 to about 35 percent in 2028, while domestic savings remaining at the current level of about 31 percent of GDP.

Inflation will decline from 23 percent on average in 2008 to 6 percent by end-2009 mainly due to lower commodity prices, and will remain at that level through 2013. Thereafter, a further decline is assumed reflecting productivity gains.

Average interest rates on foreign borrowing will gradually rise from around 3 percent during 2008 to above 4 percent by 2028, as the share of concessional loans in total debt gradually declines.

Net capital inflows will fall from about 10 percent to GDP in 2008 to 8 percent in 2013 and stabilize thereafter. The non-debt-creating part of FDI will decline from about 7 percent of GDP in 2008 to under 4 percent in 2028. Concessional official development assistance is assumed to increase slightly from $1.7 billion in 2008 to $2.2 billion in 2018 before falling to $1.1 billion by 2028. Commercial borrowing will remain broadly constant (with some fluctuations) at around 1½ percent of GDP.

The primary fiscal deficit (including off-budget expenditures and net lending) will rise to 6½ percent of GDP in 2009 and gradually decline to 3 percentage points of GDP in 2013 and further to 2 percent of GDP on average during 2014–28. Expenditures will fall by about 2 percentage points of GDP to 30 percent of GDP between 2009–13, with a rise in current expenditure more than offset by a decline in capital and off-budget expenditure and net lending. Revenue will also increase by about 1 percentage point of GDP to 25 percent of GDP between 2009–13. Beyond 2013, expenditures will remain broadly constant in percent of GDP, while revenue will rise further to 27 percent of GDP by 2028 as the government finds alternative revenue sources, assumed to more than offset a decline in oil revenue.

Government financing (excluding the possible impact from a government stimulus plan, which is not incorporated in the baseline) will increase by about 3½ percentage points of GDP in 2009, mostly through domestic financing. During 2009–13, government financing will decline by 3 percentage points of GDP, mainly through lower domestic financing. The mix of financing will remain broadly stable thereafter.

Contingent liabilities or exceptional financing items are not assumed.

6. **Under the baseline scenario, the present value (PV) of PPG external debt is projected to initially rise in relation to GDP, exports, and government revenue, followed by a decline over the longer term.** In terms of averages over the whole projection period, these ratios are projected to remain broadly constant relative to the base period. With Vietnam being a very dynamic and open economy, the PV of external debt as a share of exports is low and projected to decline from 22½ percent in 2007 to 13½ percent in 2028. The debt service ratio (to exports and to revenue) is also expected to decline after an initial increase.

7. **Stress tests indicate that the PV of PPG external debt is most sensitive to exchange rate depreciation and to a loss of access to non-debt-creating flows.** A 30 percent one-time depreciation of the dong would increase the PV of external debt in relation to GDP by 8 percentage points relative to the baseline, and a loss of access to non-debt-creating flows by 3 percentage points by 2013. A loss of access to concessional loans would have a similar negative impact albeit over a longer time horizon (5–10 years).

III. Public Debt Sustainability Analysis

8. **Public debt management is likely to become more challenging, with its ratio to GDP now projected to be higher than in the last DSA due to a significant deterioration in the overall fiscal balance.** The PV of public debt in relation to GDP is projected to rise from 37 percent in 2008 to 46 percent in 2013, and thereafter gradually decline to 43 percent by 2028. This ratio could be higher depending upon the size of fiscal stimulus which is being worked out. The debt service-to-revenue ratio is expected to increase from 6 percent in 2008 to 11½ percent in 2013 due to lower oil revenue, before starting to gradually decline.

9. **Stress tests indicate that the PV of public debt to GDP ratio is most sensitive to an increase in debt-creating flows followed by an exchange rate depreciation.** Both a one-time 30 percent nominal depreciation of the dong and an increase in debt-creating flows by 10 percentage points of GDP would increase the PV of public debt (relative to the baseline) by 7–8 percentage points by 2013. However, even the most extreme negative shock would not destabilize (cause to rise indefinitely) the PV ratios over the longer term.[6]

10. **The stress tests underscore the need for prudent fiscal policy.** The debt service-to-revenue ratio would triple or more (relative to its initial level) under the higher debt-creating flows scenario and under the depreciation scenario. Under a permanently lower GDP growth it would double by 2013.

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[6] In addition to the favorable structure of external debt, this reflects the fact that the bulk of domestic debt is also long term.

IV. Conclusion

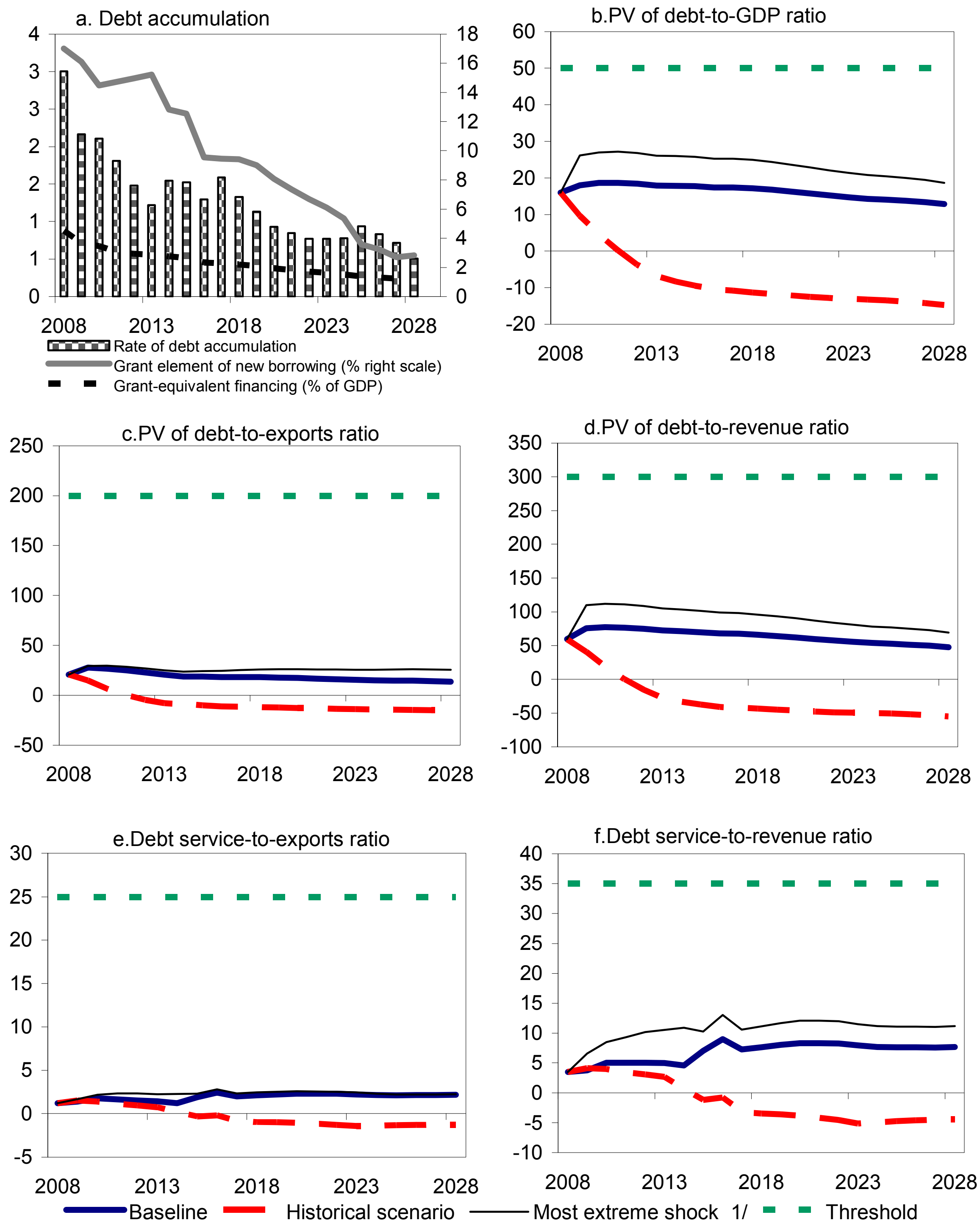
11. **Vietnam remains at low risk of external debt distress.** Compared with the last DSA, the projected PPG external debt ratios and projected paths are more favorable, and remain well below indicative thresholds even under the most extreme of the standard shocks normally considered.

12. **Total public debt, however, is expected to be adversely affected by the ongoing global downturn.** Public debt will also be affected by the government stimulus plan to mitigate the economic slowdown. Provided that the package is prudently financed, and that the government increases the revenue base to more than offset the expected loss of oil revenue in the long run, the burden of public debt could be manageable.

13. **However, the results are critically dependent on the assumptions underlying the projections.** The most important of these include: (i) sound monetary and fiscal policies and boosting non-oil revenue as oil production declines in the long run; (ii) healthy export growth and continued dynamism of the Vietnamese economy more generally; (iii) continued access to non-debt-creating external financing, especially private remittances and FDI; and (iv) continued access to concessional financing by multilateral and bilateral sources.

14. **A risk that deserves special attention is the possible impact of potential government contingent liabilities.** Such liabilities could arise from the need to recapitalize some banks or to deal with problems in state-owned enterprises. The size of the fiscal stimulus and its financing is also important.

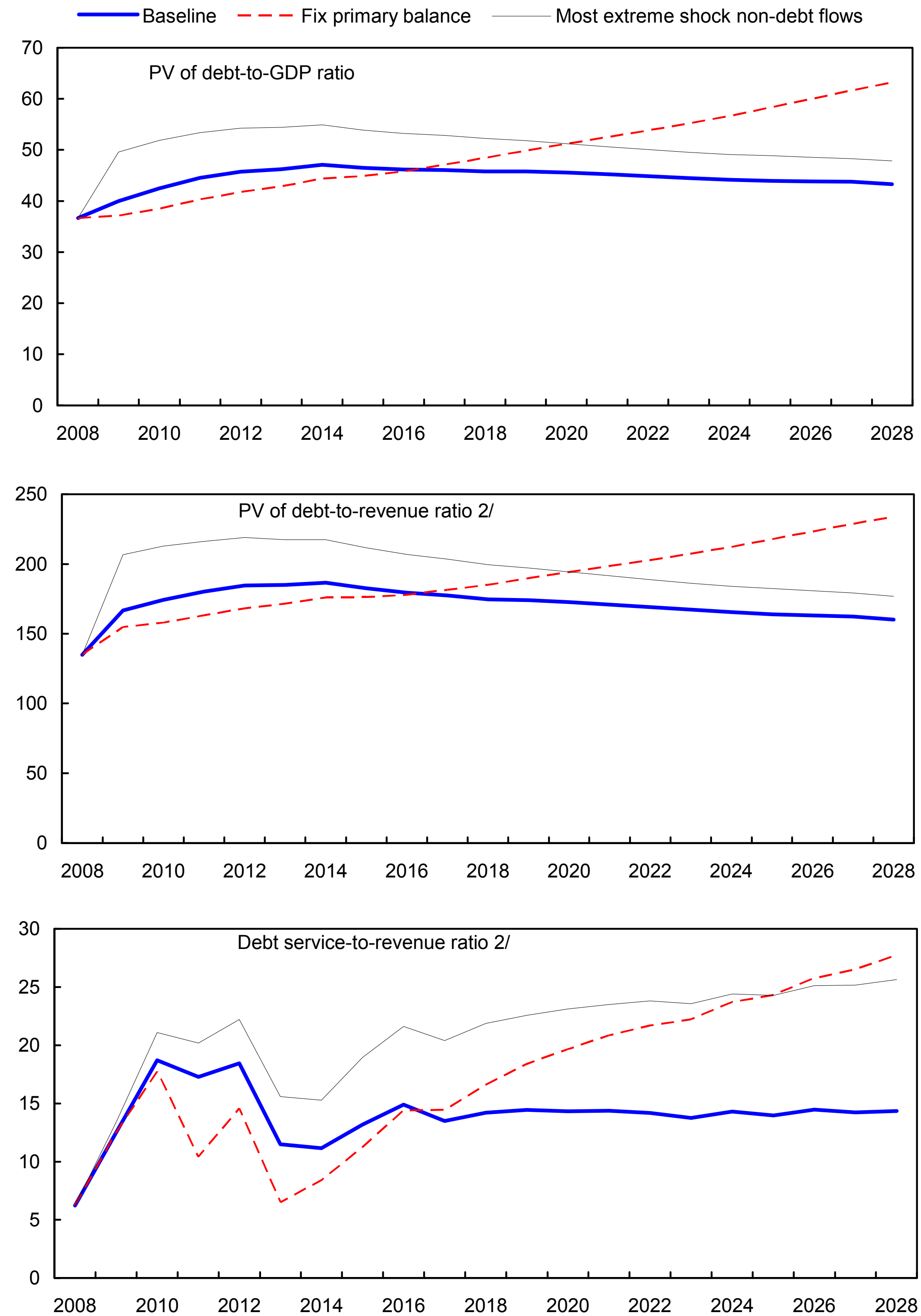
Figure 1. Vietnam: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2008–28 1/



Source: IMF staff projections and simulations.

1/ The most extreme stress test is the test that yields the highest ratio in 2018. In Figure b. it corresponds to a one-time depreciation shock; in Figure c. to a terms shock; in Figure d. to a one-time depreciation shock; in Figure e. to a non-debt flows shock; and in Figure f. to a one-time depreciation shock.

Figure 2. Vietnam: Indicators of Public Debt under Alternative Scenarios, 2008–28 1/



Sources: Vietnamese authorities; and IMF staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2018.

2/ Revenues are defined inclusive of grants.

Table 1a. Vietnam: External Debt Sustainability Framework, Baseline Scenario, 2005–28 1/

(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average 2/	Standard Deviation 2/	Projections									
	2005	2006	2007			2008	2009	2010	2011	2012	2013	2008–13 Average	2018	2028	2014–28 Average
External debt (nominal) 1/	**32.5**	**31.4**	**33.3**			**29.8**	**31.9**	**31.7**	**31.2**	**30.7**	**30.4**		**26.8**	**22.5**	
Of which: Public- and publicly-guaranteed (PPG)	26.9	25.8	26.8			24.7	26.0	25.7	24.8	23.7	22.6		21.6	14.9	
Change in external debt	-4.6	-1.1	1.9			-3.5	2.2	-0.2	-0.5	-0.5	-0.3		-0.7	-0.2	
Identified net debt-creating flows	-6.5	-6.6	-1.9			1.8	3.3	1.7	0.7	-0.2	-0.9		-1.2	-0.7	
Non-interest current account deficit	**0.1**	**-0.7**	**8.8**	**0.2**	**4.6**	**9.4**	**7.0**	**5.9**	**5.5**	**4.8**	**4.0**		**3.1**	**3.2**	3.1
Deficit in balance of goods and services	5.2	4.6	15.8			16.2	9.9	8.7	8.6	8.0	7.3		6.9	6.9	
Exports	69.2	73.7	76.7			77.0	64.8	69.2	74.7	80.6	87.2		94.5	94.5	
Imports	74.4	78.3	92.6			93.2	74.6	77.9	83.3	88.6	94.6		101.4	101.4	
Net current transfers (negative = inflow)	-6.4	-6.6	-9.0	-5.7	1.6	-8.2	-4.5	-4.5	-4.5	-4.7	-4.8		-5.0	-5.0	-5.0
Of which: Official	-0.4	-0.4	-0.4			-0.4	-0.3	-0.3	-0.3	-0.3	-0.3		-0.3	-0.3	
Other current account flows (negative = net inflow)	1.3	1.3	2.1			1.3	1.7	1.7	1.3	1.4	1.4		1.2	1.2	
Net FDI (negative = inflow)	**-2.3**	**-2.6**	**-7.3**	**-3.7**	**1.7**	**-6.9**	**-3.4**	**-3.5**	**-3.6**	**-3.7**	**-3.7**		**-3.7**	**-3.7**	-3.7
Endogenous debt dynamics 3/	**-4.3**	**-3.3**	**-3.5**			**-0.7**	**-0.3**	**-0.8**	**-1.2**	**-1.2**	**-1.2**		**-0.6**	**-0.2**	
Contribution from nominal interest rate	1.0	1.0	1.0			0.9	1.1	0.9	0.9	0.9	0.9		1.2	1.1	
Contribution from real GDP growth	-2.7	-2.3	-2.3			-1.6	-1.4	-1.7	-2.0	-2.1	-2.1		-1.8	-1.3	
Contribution from price and exchange rate changes	-2.6	-1.9	-2.2			…	…	…	…	…	…		…	…	
Residual (3-4) 4/	**1.8**	**5.5**	**3.8**			**-5.3**	**-1.1**	**-1.9**	**-1.1**	**-0.4**	**0.6**		**0.4**	**0.5**	
Of which: Exceptional financing	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 5/	...	...	23.5			22.5	24.6	25.2	25.6	25.9	26.2		22.4	20.4	
In percent of exports	...	...	30.6			29.2	37.9	36.4	34.3	32.1	30.0		23.7	21.6	
PV of PPG external debt	**...**	**...**	**17.2**			**16.0**	**18.0**	**18.6**	**18.7**	**18.4**	**17.9**		**17.1**	**12.8**	
In percent of exports	**...**	**...**	**22.4**			**20.7**	**27.8**	**26.8**	**25.0**	**22.9**	**20.6**		**18.2**	**13.6**	
In percent of government revenues	**...**	**...**	**63.0**			**59.5**	**75.7**	**77.0**	**76.3**	**74.8**	**72.3**		**65.9**	**47.8**	
Debt service-to-exports ratio (in percent)	**4.5**	**4.2**	**3.8**			**3.4**	**4.5**	**5.0**	**4.8**	**4.4**	**4.1**		**4.1**	**4.4**	
PPG debt service-to-exports ratio (in percent)	**1.7**	**1.6**	**1.3**			**1.2**	**1.4**	**1.8**	**1.7**	**1.5**	**1.4**		**2.1**	**2.2**	
PPG debt service-to-revenue ratio (in percent)	**4.4**	**4.3**	**3.7**			**3.5**	**3.7**	**5.1**	**5.0**	**5.0**	**5.0**		**7.7**	**7.7**	
Total gross financing need (in billions of U.S. dollars)	0.6	0.0	3.4			4.9	6.2	6.2	6.3	6.2	5.9		7.8	20.4	
Non-interest current account deficit that stabilizes debt ratio	4.7	0.4	7.0			12.9	4.8	6.1	5.9	5.3	4.3		3.9	3.4	
Key macroeconomic assumptions															
Real GDP growth (in percent)	8.4	8.2	8.5	7.2	1.2	6.2	4.8	5.8	7.0	7.4	7.4	6.4	7.0	6.0	6.7
GDP deflator in U.S. dollar terms (change in percent)	7.4	6.4	7.6	2.5	4.8	19.0	-3.9	2.2	1.9	2.0	1.9	3.9	2.0	2.0	2.0
Effective interest rate (in percent) 6/	3.0	3.6	3.7	3.1	0.6	3.4	3.7	3.1	3.1	3.0	3.1	3.2	4.6	5.2	4.7
Growth of exports of G&S (in U.S. dollar terms, in percent)	20.7	22.7	21.5	16.9	8.8	26.8	-15.2	15.6	17.6	18.2	18.5	13.6	9.1	8.0	9.4
Growth of imports of G&S (in U.S. dollar terms, in percent)	15.3	21.2	38.0	17.7	12.9	27.3	-19.3	12.9	16.6	16.5	16.9	11.8	9.1	8.0	9.3
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	17.0	16.1	14.5	14.7	15.0	15.2	15.4	9.4	2.8	7.2
Government revenues (excluding grants, in percent of GDP)	26.8	27.9	27.2			26.8	23.8	24.1	24.5	24.6	24.8		26.0	26.9	26.2
Aid flows (in billions of U.S. dollars) 7/	1.7	1.8	1.8			2.0	1.6	1.8	1.8	2.0	2.0		2.2	1.2	
Of which: Grants	0.2	0.5	0.3			0.3	0.2	0.2	0.2	0.2	0.2		0.4	0.8	
Of which: Concessional loans	1.7	1.6	1.7			1.7	1.7	1.8	1.9	1.9	2.0		2.2	1.1	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			0.9	0.7	0.7	0.6	0.6	0.6		0.4	0.2	0.4
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			25.0	22.6	21.0	20.0	20.5	21.0		15.1	11.3	13.7
Memorandum items:															
Nominal GDP (in billions of U.S. dollars)	52.9	60.9	71.1			89.9	90.6	98.0	106.8	117.0	128.1		199.2	450.6	
Nominal dollar GDP growth	16.5	15.1	16.7			26.4	0.8	8.2	9.0	9.5	9.5	**10.6**	9.1	8.0	8.7
PV of PPG external debt (in billions of U.S. dollars)			12.2			14.3	16.3	18.2	20.0	21.5	23.0		34.2	57.9	
(PVt-PVt-1)/GDPt-1 (in percent)						3.0	2.2	2.1	1.8	1.5	1.2	2.0	1.3	0.5	1.0

Source: IMF staff simulations.

1/ Includes both public and private sector external debt.
2/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.
3/ Derived as [r - g - r(1+g)]/(1+g+r+gr) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and r = growth rate of GDP deflator in U.S. dollar terms.
4/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.
5/ Assumes that PV of private sector debt is equivalent to its face value.
6/ Current-year interest payments divided by previous period debt stock.
7/ Defined as grants, concessional loans, and debt relief.
8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 1b. Vietnam: Sensitivity Analysis for Key Indicators of Public- and Publicly-Guaranteed External Debt, 2008–28
(In percent)

	Projections							
	2008	2009	2010	2011	2012	2013	**2018**	2028
PV of debt-to-GDP ratio								
Baseline	16	18	19	19	18	18	**17**	13
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2008–28 1/	16	10	5	0	-4	-7	**-11**	-15
A2. New public sector loans on less favorable terms in 2008–28 2/	16	19	20	21	22	22	**24**	24
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2009–10	16	18	18	18	18	18	**17**	13
B2. Export value growth at historical average minus one standard deviation in 2009–10 3/	16	0	-13	-11	-10	-10	**2**	11
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2009–10	16	18	19	19	19	18	**18**	13
B4. Net non-debt creating flows at historical average minus one standard deviation in 2009–10 4/	16	20	22	22	22	21	**19**	13
B5. Combination of B1–B4 using one-half standard deviation shocks	16	-4	-22	-21	-19	-18	**-3**	10
B6. One-time 30 percent nominal depreciation relative to the baseline in 2009 5/	16	26	27	27	27	26	**25**	19
PV of debt-to-exports ratio								
Baseline	21	28	27	25	23	21	**18**	14
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2008–28 1/	21	15	7	0	-5	-8	**-12**	-16
A2. New public sector loans on less favorable terms in 2008–28 2/	21	29	29	28	27	25	**26**	26
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2009–10	21	28	27	25	23	21	**18**	14
B2. Export value growth at historical average minus one standard deviation in 2009–10 3/	21	0	-15	-13	-11	-9	**2**	10
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2009–10	21	28	27	25	23	21	**18**	14
B4. Net non-debt creating flows at historical average minus one standard deviation in 2009–10 4/	21	31	32	30	27	24	**20**	14
B5. Combination of B1–B4 using one-half standard deviation shocks	21	-4	-26	-22	-19	-17	**-2**	8
B6. One-time 30 percent nominal depreciation relative to the baseline in 2009 5/	21	28	27	25	23	21	**18**	14
PV of debt-to-revenue ratio								
Baseline	59	76	77	76	75	72	**66**	48
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2008–28 1/	59	41	19	0	-15	-28	**-43**	-55
A2. New public sector loans on less favorable terms in 2008–28 2/	59	80	84	87	88	88	**94**	90
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2009–10	59	75	76	75	74	71	**65**	47
B2. Export value growth at historical average minus one standard deviation in 2009–10 3/	59	-1	-52	-47	-42	-39	**9**	40
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2009–10	59	75	79	79	77	74	**68**	49
B4. Net non-debt creating flows at historical average minus one standard deviation in 2009–10 4/	59	84	93	91	89	86	**73**	49
B5. Combination of B1–B4 using one-half standard deviation shocks	59	-15	-92	-84	-79	-74	**-10**	36
B6. One-time 30 percent nominal depreciation relative to the baseline in 2009 5/	59	110	112	111	109	105	**96**	69

Table 1b.Vietnam: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2008–28 (concluded)

(In percent)

	Projections							
	2008	2009	2010	2011	2012	2013	**2018**	2028
Debt service-to-exports ratio								
Baseline	1	1	2	2	2	1	**2**	2
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2008–28 1/	1	2	1	1	1	1	**-1**	-1
A2. New public sector loans on less favorable terms in 2008–28 2/	1	2	2	2	2	1	**1**	1
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2009–10	1	2	2	2	2	2	**2**	2
B2. Export value growth at historical average minus one standard deviation in 2009–10 3/	1	1	1	0	0	0	**-1**	1
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2009–10	1	2	2	2	2	2	**2**	2
B4. Net non-debt creating flows at historical average minus one standard deviation in 2009–10 4/	1	2	2	2	2	2	**2**	2
B5. Combination of B1–B4 using one-half standard deviation shocks	1	1	0	0	0	0	**-1**	1
B6. One-time 30 percent nominal depreciation relative to the baseline in 2009 5/	1	2	2	2	2	2	**2**	2
Debt service-to-revenue ratio								
Baseline	3	4	5	5	5	5	**8**	8
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2008–28 1/	3	4	4	3	3	3	**-3**	-4
A2. New public sector loans on less favorable terms in 2008–28 2/	3	5	5	5	5	5	**5**	5
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2009–10	3	4	6	6	7	7	**8**	8
B2. Export value growth at historical average minus one standard deviation in 2009–10 3/	3	5	2	0	1	2	**-2**	6
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2009–10	3	4	6	7	7	7	**8**	8
B4. Net non-debt creating flows at historical average minus one standard deviation in 2009–10 4/	3	5	6	7	8	8	**9**	8
B5. Combination of B1–B4 using one-half standard deviation shocks	3	4	2	-2	-1	0	**-5**	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2009 5/	3	7	9	9	10	11	**11**	11
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	-1	-1	-1	-1	-1	-1	**-1**	-1

Source: IMF staff projections and simulations.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 2a. Vietnam: Public Sector Debt Sustainability Framework, Baseline Scenario, 2005–28 1/

(In percent of GDP, unless otherwise indicated)

	Actual			Average 2/	Standard Deviation 2/	Estimate	Projections								
	2005	2006	2007			2008	2009	2010	2011	2012	2013	2008–13 Average	2018	2028	2014–28 Average
Public sector debt 1/	44.5	44.1	46.3			44.4	47.5	49.2	50.3	50.7	50.5		50.2	45.4	
Of which: Foreign-currency denominated	26.9	25.8	26.8			24.7	26.0	25.7	24.8	23.7	22.6		21.6	14.9	
Change in public sector debt	-1.0	-0.4	2.3			-1.9	3.1	1.6	1.1	0.4	-0.1		-0.6	-0.5	
Identified debt-creating flows	-2.0	-4.8	-1.3			-3.9	5.4	2.0	0.7	0.2	-0.3		-0.4	-0.4	
Primary deficit	3.7	0.3	4.3	3.1	1.7	3.6	6.6	4.9	4.1	3.6	3.1	4.3	1.9	1.1	1.8
Revenue and grants	27.2	28.7	27.6			27.2	24.0	24.4	24.7	24.8	25.0		26.2	27.0	
Of which: Grants	0.5	0.8	0.4			0.3	0.2	0.2	0.2	0.2	0.2		0.2	0.2	
Primary (noninterest) expenditure	30.9	29.0	32.0			30.8	30.6	29.2	28.8	28.4	28.1		28.1	28.2	
Automatic debt dynamics	-5.7	-5.1	-5.7			-7.5	-1.2	-2.9	-3.4	-3.4	-3.4		-2.3	-1.5	
Contribution from interest rate/growth differential	-4.7	-4.4	-4.4			-5.4	-1.5	-2.5	-3.0	-3.3	-3.4		-2.3	-1.6	
Of which: Contribution from average real interest rate	-1.2	-1.0	-0.9			-2.7	0.6	0.2	0.2	0.1	0.1		1.0	1.0	
Of which: Contribution from real GDP growth	-3.5	-3.4	-3.4			-2.7	-2.0	-2.6	-3.2	-3.5	-3.5		-3.3	-2.6	
Contribution from real exchange rate depreciation	-1.0	-0.7	-1.3			-2.1	0.3	-0.4	-0.3	-0.1	0.0		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g., bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	1.0	4.4	3.6			1.9	-2.3	-0.4	0.4	0.2	0.2		-0.2	0.0	
Other Sustainability Indicators															
PV of public sector debt	...	...	36.6			36.7	40.0	42.5	44.5	45.7	46.3		45.8	43.3	
Of which: Foreign-currency denominated	...	...	17.1			17.0	18.4	19.0	19.1	18.8	18.3		17.1	12.8	
Of which: External	...	...	17.1			17.0	18.4	19.0	19.1	18.8	18.3		17.1	12.8	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 3/	3.3	5.2	1.8			5.9	5.0	9.4	9.2	8.2	8.0		5.7	5.0	
PV of public sector debt-to-revenue and grants ratio (in percent)	…	…	132.5			135.0	166.7	174.3	180.4	184.5	185.0		174.7	160.1	
PV of public sector debt-to-revenue ratio (in percent)	…	…	134.3			136.7	168.5	176.1	181.7	185.8	186.3		175.9	161.2	
Of which: External 4/	…	…	62.7			63.2	77.6	78.8	77.8	76.3	73.7		65.9	47.8	
Debt service-to-revenue and grants ratio (in percent) 5/	5.4	5.3	5.4			6.2	12.5	18.7	17.3	18.5	11.5		14.2	14.3	
Debt service-to-revenue ratio (in percent) 5/	5.5	5.5	5.5			6.3	12.6	18.9	17.4	18.6	11.6		14.3	14.4	
Primary deficit that stabilizes the debt-to-GDP ratio	4.7	0.7	2.1			5.6	3.5	3.2	3.0	3.2	3.3		2.5	1.6	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	8.4	8.2	8.5	7.2	1.2	6.2	4.8	5.8	7.0	7.4	7.4	6.4	7.0	6.0	6.7
Average nominal interest rate on forex debt (in percent)	1.9	2.1	2.2	2.3	0.4	2.3	2.1	2.0	1.9	1.9	1.8	2.0	3.1	3.9	3.2
Real exchange rate depreciation (in percent, + indicates depreciation)	-3.8	-2.8	-5.5	-1.5	3.4	-8.2	...	...	...	...	...	...	...	...	...
GDP deflator (in percent)	8.2	7.3	8.2	6.2	2.4	21.7	4.8	7.3	6.5	6.1	6.0	8.7	2.9	2.9	3.1
Growth of real primary spending (deflated by GDP deflator, in percent)	0.2	0.0	0.2	0.1	0.1	0.0	0.0	0.0	0.1	0.1	0.1	0.0	0.1	0.1	0.1
Grant element of new external borrowing (in percent)	...	...	...	…	…	17.0	16.1	14.5	14.7	15.0	15.2	15.4	9.4	2.8	...

Sources: Vietnamese authorities; and IMF staff estimates and projections.

1/ Central government plus selected wider public sector entities; debt measured on a gross basis.

2/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

3/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

4/ Revenues excluding grants.

5/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

Table 2b. Vietnam: Sensitivity Analysis for Key Indicators of Public Debt, 2008–28
(In percent)

		Projections						
	2008	2009	2010	2011	2012	2013	**2018**	2028
PV of debt-to-GDP ratio								
Baseline	37	40	42	45	46	46	**46**	43
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	37	36	36	38	39	40	**43**	52
A2. Primary balance is unchanged from 2008	37	37	39	40	42	43	**48**	63
A3. Permanently lower GDP growth 1/	37	40	43	45	47	48	**50**	56
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2009–10	37	39	41	43	44	44	**43**	38
B2. Primary balance is at historical average minus one standard deviations in 2009–10	37	38	41	43	44	45	**44**	42
B3. Combination of B1-B2 using one half standard deviation shocks	37	37	38	40	41	41	**38**	33
B4. One-time 30 percent real depreciation in 2009	37	48	50	52	53	53	**51**	51
B5. 10 percent of GDP increase in other debt-creating flows in 2009	37	50	52	53	54	54	**52**	48
PV of debt-to-revenue ratio 2/								
Baseline	135	167	174	180	184	185	**175**	160
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	135	149	149	152	156	158	**165**	192
A2. Primary balance is unchanged from 2008	135	155	158	163	168	172	**185**	234
A3. Permanently lower GDP growth 1/	135	167	176	183	189	191	**190**	208
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2009–10	135	164	170	175	178	177	**163**	141
B2. Primary balance is at historical average minus one standard deviations in 2009–10	135	159	166	173	177	178	**170**	157
B3. Combination of B1-B2 using one half standard deviation shocks	135	154	157	161	164	163	**147**	121
B4. One-time 30 percent real depreciation in 2009	135	199	205	210	214	213	**196**	187
B5. 10 percent of GDP increase in other debt-creating flows in 2009	135	207	213	216	219	217	**200**	177
Debt service-to-revenue ratio 2/								
Baseline	6	12	19	17	18	11	**14**	14
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	6	12	17	9	13	4	**13**	22
A2. Primary balance is unchanged from 2008	6	12	18	10	15	6	**17**	28
A3. Permanently lower GDP growth 1/	6	13	19	18	19	12	**17**	23
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2009–10	6	12	18	16	17	10	**12**	11
B2. Primary balance is at historical average minus one standard deviations in 2009–10	6	12	18	13	17	9	**14**	14
B3. Combination of B1-B2 using one half standard deviation shocks	6	12	17	11	15	6	**10**	7
B4. One-time 30 percent real depreciation in 2009	6	13	21	20	22	16	**22**	26
B5. 10 percent of GDP increase in other debt-creating flows in 2009	6	12	22	39	22	24	**17**	18

Sources: Vietnamese authorities; and IMF staff estimates and projections.
1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the length of the projection period.
2/ Revenues are defined inclusive of grants.

INTERNATIONAL MONETARY FUND

VIETNAM

Staff Report for the 2008 Article IV Consultation—Informational Annex

Prepared by the Asia and Pacific Department

February 27, 2009

Contents Page

ANNEX I. VIETNAM: FUND RELATIONS
(As of January 31, 2009)

I. Membership Status: Joined: September 21, 1956; Article VIII

II. General Resources Account:	SDR Million	Percent Quota
Quota	329.10	100.00
Fund holdings of currency	329.10	100.00
Reserve position in Fund	0.01	0.00

III SDR Department:	SDR Million	Percent Allocation
Net cumulative allocation	47.66	100.00
Holdings	1.18	2.48

IV. Outstanding Purchases and Loans:	SDR Million	Percent Quota
PRGF arrangements	74.52	22.64

V. Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
PRGF	Apr. 13, 2001	Apr. 12, 2004	290.00	124.20
ESAF	Nov. 11, 1994	Nov. 10, 1997	362.40	241.60
Stand-by	Oct. 6, 1993	Nov. 11, 1994	145.00	108.80

VI. Projected Payments to Fund: (SDR million; based on existing use of resources and present holdings of SDRs)

	Forthcoming				
	2009	2010	2011	2012	2013
Principal	20.70	24.84	20.70	8.28	0.00
Charges/interest	0.65	0.48	0.36	0.29	0.27
Total	21.35	25.32	21.06	8.57	0.27

VII. Exchange Arrangement:

Vietnam's exchange rate system is currently classified as an "other managed arrangement." The State Bank of Vietnam (SBV) sets the central rate vis-à-vis the U.S. dollar on a daily basis and allows interbank foreign exchange market rates to fluctuate by ±3 percent. The SBV increased exchange rate flexibility substantially during 2008, by widening the dong-U.S. dollar trading band from ±0.75 to ±3 percent on three separate occasions. In 2007, the trading band was widened twice from ±0.25 to ±0.75 percent.

Vietnam maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions, except for those exchange restrictions imposed for security reasons of which Vietnam has notified the Fund pursuant to Executive Board Decision No. 144-(52/51), 8/14/52.

VIII. Article IV Consultations:

Vietnam is on a 12-month consultation cycle. The last Article IV consultation was held in Hanoi during June 18–27, 2007 and was concluded by the Executive Board on October 26, 2007 (IMF Country Report No. 07/387). In addition, staff visits took place in December 2007 as well as April and September 2008.

IX. Technical Assistance:

Technical assistance is currently focused on monetary operations, banking supervision, tax policy and administration, and AML/CFT. A resident advisor began assisting the SBV in the area of banking supervision in December 2008.

X. Resident Representative:

Mr. Benedict Bingham assumed the Senior Resident Representative post for Vietnam and Lao P.D.R., based in Hanoi, on October 17, 2007.

ANNEX II. VIETNAM: RELATIONS WITH THE WORLD BANK GROUP[1]

A. Partnership in Vietnam's Development Strategy

A new Country Partnership Strategy (CPS) was presented to the World Bank Board in February 2007. The CPS is fully aligned to Vietnam's Socio-Economic Development Plan (SEDP) 2006–10 and sets out the World Bank's planned support between FY07 and FY11. The objectives of the SEDP are mapped into four broad pillars which are the organizing principles of the CPS: (i) improving the business environment; (ii) strengthening social inclusion; (iii) strengthening environmental and natural resource management; and (iv) improving governance.

A common theme underlining the four pillars is the need to complete the remaining first-generation structural reforms, while moving forward on a set of ambitious second-generation reforms. The former group relates to the transition to a market economy and the restructuring of the state sector. The latter group focuses on the institutional underpinnings for the operation of a more complex economy, as Vietnam becomes a middle-income country. Through these reforms, the role of the Government will be transformed from direct producer of goods and services to regulator and provider of the foundations for a well-functioning, equitable, modern market economy.

Improving the Business Environment: Support for this theme focuses on banking reform and overall financial sector development; improved competitiveness with fuller integration with the world economy, including through improved quality, efficiency, and equity of the higher education system; a more level playing field for enterprises; a better foundation for knowledge-based growth and enhancing agricultural competitiveness; and investment in more efficient and reliable infrastructure.

Strengthening Social Inclusion: Priorities for World Bank Group support are better understanding of poverty and piloting new instruments to reach the poor; mainstreaming gender issues across the portfolio and including people with disabilities in the development process; increasing access to and quality of basic infrastructure services for the rural poor; increasing access to affordable and better quality education and health care services; including and empowering ethnic minorities in the development process; improving policies and services to address the needs of urban poor and migrants; and reducing vulnerability to adverse shocks, including natural disasters and climatic hazards.

Strengthening Environmental and Natural Resource Management: Rapid economic growth is putting the environment under increasing stress. The livelihoods of poor people in Vietnam

[1] Questions may be referred to Ms. Myla Taylor Williams (202-473-6997).

still depend overwhelmingly on natural resources. The World Bank's activities will focus on livelihood-supporting roles and public benefits of better management of the environment and natural resources. In practice, this will raise a range of challenges related to regional planning; land, forestry, water resources and integrated river basin management; and the introduction of modern tools for environmental protection.

Improving Governance: Progress across the first three pillars will require institutions with enhanced transparency, accountability, and stakeholder voice and participation. World Bank support under this pillar will focus on strengthening public financial management, simplifying administrative procedures, and modernizing the planning process through more participatory approaches and greater accountability of public service providers for achievement of development outcomes.

B. World Bank Group Strategy and Lending

The World Bank Group is employing a broad range of instruments, elaborated in the CPS, to support the objectives laid out in the SEDP 2006–10 and other key strategies of the Government. These instruments include the World Bank's Poverty Reduction Support Credits (PRSCs), other development policy and investment operations, and analytical and advisory activities; the IFC's equity, loan and technical assistance (TA) participations and the Mekong Private Sector Development Facility (MPDF); Multilateral Investment Guarantee Agency (MIGA) activities; and donor partnerships and ODA coordination.

Scale of the World Bank Group Program: The World Bank's operational program is calibrated based on an assumption of annual IDA envelopes on the order of $900 million equivalent. Actual allocations depend on Vietnam's performance relative to other potential IDA recipients and on the overall resource envelope. At $1.2 billion equivalent, the FY08 IDA program significantly surpassed that of prior years (see Table 1). Vietnam is now the second largest IDA-only borrower after Bangladesh, and the third largest user of IDA resources after India and Bangladesh. There are currently 40 active IDA credits totaling $4.6 billion equivalent, of which $1.2 billion has been disbursed. The IFC and MIGA programs are also expected to grow in the coming years.

IBRD Eligibility: During the CPS period, Vietnam's GNI per capita is projected to move steadily towards the IDA graduation threshold. In FY08 the World Bank confirmed Vietnam's eligibility for IBRD borrowing. The first IBRD operation is planned for FY09. In the initial phase of Vietnam's IBRD/IDA blend status, IBRD borrowing is expected to be incremental to, as opposed to substituting for, IDA financing.

Lending Program: The ongoing second series of five Poverty Reduction Support Credits (PRSCs VI-X) is the centerpiece of the World Bank's lending program during the CPS period. These operations support the reforms envisaged chiefly in the SEDP 2006–10, which also serves as the Poverty Reduction Strategy (PRS) for Vietnam. PRSC VII ($150 million

Table 1. Vietnam: FY05–08 Commitments

Fiscal Year	Project Name	IDA Amount (US$ million equivalent)
2005	PRSC IV	100
	HIV/AIDS Prevention	35
	Targeted Budget Support for Education for All	50
	Road Safety	32
	Urban Water Supply Development	113
	Second Rural Energy	220
	Forest Sector Development	40
	Avian Influenza Emergency Recovery	5
	Second Payment System and Bank Modernization	105
	Total	**700**
2006	PRSC V	100
	ICT Development	94
	Mekong Health Support	70
	Customs Modernization	66
	Red River Delta Rural Water Supply and Sanitation	46
	Second Transmission and Distribution	200
	Third Rural Transport	106
	Natural Disaster Risk Management	86
	Total	**768**
2007	PRSC VI	175
	Second Higher Education	60
	Program 135 Phase 2 (DPL)	50
	Avian and Human Influenza Control	20
	Mekong Transport Infrastructure Development	207
	Mekong Transport/Flood Protection (Additional Financing)	25
	Ho Chi Minh City Infrastructure Fund (HIFU)	50
	Coastal Cities Environment and Sanitation	125
	Total	**712**
2008	PRSC VII	150
	Tax Administration Modernization	80
	Northern Upland Health Support	60
	Land Administration	75
	Third Rural Finance	200
	Hanoi Urban Transport Development	155
	Northern Delta Transport Development	170
	Da Nang Priority Infrastructure Investment	152
	Rural Distribution	150
	Total	**1,192**
	Total FY05–FY08 Commitments	**3,372**

Source: World Bank.

equivalent) was approved by the World Bank's Board in June 2008. The five PRSC operations in the first series mainly supported implementation of the Government's Comprehensive Poverty Reduction and Growth Strategy. PRSC I, a two-tranche operation for $250 million equivalent, was approved by the World Bank's Board in June 2001. It focused on structural reforms in trade liberalization, the financial sector, SOEs, and private sector development. Subsequent PRSCs have had significantly broader scope and supported policy actions in areas such as health, social protection, education, and environmental protection and natural resource management. They have also included actions to build modern governance systems in Vietnam, such as those aimed at public financial management and public administration reform, and fighting corruption. The number of PRSC co-financiers has increased from 4 for PRSC I to 12 with contributions exceeding $200 million for PRSC VII. In addition to providing resources, PRSCs serve as an effective donor coordination device as well as a single, unified platform for policy dialogue between Vietnam's partners and the Government on a broad range of issues. The World Bank's operational program also includes sector development and investment operations aligned with the four pillars of the CPS. A sector development policy operation supported poverty reduction, while well over half of sector investment commitments have financed infrastructure projects, with the balance focused on the health and education sectors, rural development, and public administration reform. Forthcoming World Bank operations will likely exceed $1 billion in each of the next two fiscal years, again with well over half to finance infrastructure investments.

Knowledge Program: The World Bank supports the Government's efforts to strengthen institutional capacity through its knowledge program of analytical and advisory services. The annual Vietnam Development Reports (VDRs), written in coordination with a large number of donors and submitted to the annual year-end Consultative Group meeting, summarize the accumulated knowledge in a specific policy area of Vietnam's reform agenda. Recent VDRs have focused on tackling the challenges to attainment of SEDP objectives (2007) as well as thematic areas such as social protection (2008), business development (2006), and governance (2005). The next VDR will focus on financing Vietnam's development. Other reports during this period included Infrastructure Finance, Higher Education and Skills for Growth, Country Financial Accountability Assessment, Policy Agenda for Health Sector Transition, and a series on Vietnam's Infrastructure Challenges. Forthcoming reports include High Quality Education for All, Health Financing, Financial Sector Strategy, Infrastructure Regulatory and Policy Reform, Regional Development and Integrated Urbanization, and Prioritizing Climate Change Investments. In addition, the World Bank continues to provide advisory services in areas such as tax policy, social security, and public financial management reform.

C. IMF-World Bank Collaboration in Specific Areas

Since the expiration of the PRGF in April 2004 the two institutions have closely collaborated in the discussions of PRSC triggers and benchmarks in the policy areas which used to be covered by the PRGF agreement. The IMF has provided Letters of Assessment in support of PRSC operations. In the area of public financial management, the World Bank has an investment credit to support the introduction of a modern Treasury and Budget Management Information System, and coordinates technical inputs on a large multi-donor trust fund for public financial management reform. The World Bank is also following up on the technical assistance provided by the IMF in relation to tax reform and revenue management. An investment credit for tax administration reform has been set up to this effect. Joint work is also under way in support of the establishment of a modern central bank, with the IMF providing technical assistance on monetary policy and operations and both the World Bank and IMF providing technical assistance on banking supervision. The World Bank has also set up an investment credit to reorganize the State Bank of Vietnam and to develop appropriate information management systems.

Since 2005, the World Bank and the IMF have jointly prepared an annual Debt Sustainability Assessment. More recently, they joined efforts in commenting on the direction and contents of the SEDP 2006–10, including a Joint Staff Advisory Note submitted to the World Bank Board in December 2006. The IMF and the World Bank also collaborate in the development and timely dissemination of reliable economic and financial statistics. The IMF focuses on improving balance of payments, and national accounts, and price statistics, while the World Bank provides assistance on issues related to the production of high-quality household and enterprise surveys.

The two institutions have coordinated closely on the recent macroeconomic turbulence faced by Vietnam. Their joint inputs to government have been instrumental in the adoption of the stabilization package of March 2008 and its subsequent implementation.

ANNEX III. VIETNAM: RELATIONS WITH THE ASIAN DEVELOPMENT BANK

The Asian Development Bank (AsDB) resumed its operations in Vietnam in October 1993. The Country Strategy and Program (CSP) 2007–10 was endorsed in October 2006 and is fully aligned with and supports implementation of the Government's Socio-Economic Development Plan (SEDP) 2006–10. The goals of the CSP are to help the Government reduce poverty incidence to 10–11 percent of households by 2010, achieve the Millennium Development Goals/ Vietnam Development Goals and exit from low-income country status. The new CSP focuses its operations on: (i) *Business-led, Pro-poor Economic Growth:* AsDB support aims to help the Government develop the foundations for increased private sector investment and employment; (ii) *Social Equity and Balanced Development:* in addition to supporting education, health, targeted poverty reduction, and rural infrastructure, the CSP addresses communicable diseases such as avian influenza and HIV/AIDS; gender and other equity issues are mainstreamed in AsDB projects; (iii) *Environment:* the CSP supports natural resources management, emphasizing the link between resources depletion and persistent poverty, through assistance on biodiversity, water, and coastal resources management and livelihood improvement. *Governance* is addressed through all AsDB operations and *regional cooperation* is strongly supported through a number of projects.

From October 1993 until end 2008, the AsDB approved 78 public sector loans totaling over $6 billion, comprising $4 billion from highly concessional Asian Development Fund (ADF) and $2 billion from less concessional Ordinary Capital Resources (OCR). The contract awards achievement in 2008 was $390.4 million as compared with $261 million in 2007. Disbursement in 2008 attained $264.6 million as compared with $229.9 million in 2007. The AsDB has also extended technical assistance grants amounting to $175 million for 225 projects. In addition to public sector operations, the AsDB has provided $220 million for eight private sector loans, as well as $60 million in guarantees under two projects. Vietnam also receives substantial support under the Greater Mekong Subregion (GMS) initiatives, involving Cambodia, China, Lao P.D.R, Myanmar, Thailand and Vietnam.

Support for policy and structural reforms to improve public sector efficiency and to encourage the development of the private sector is a vital component of AsDB operations in Vietnam. So far, the AsDB has approved 15 policy-based program loans in the agricultural sector, the financial sector, SOE reform and corporate governance and public administration reform, SME development and in support of the multi-donor supported Poverty Reduction Support Credit (PRSC). AsDB's policy dialogue included support for increased efficiency of state-owned utilities through reforming their rate structure and other measures to increase cost recovery and to strengthen financial management, policy analysis, and planning. A high-level capacity building program is also in place under the Japan Fund for Public Policy Training (JFPPT) funded by the Government of Japan.

Following a reorganization of AsDB's regional departments in May 2006, Vietnam is covered by the Southeast Asia Department, along with Cambodia, Brunei Darussalam, Lao P.D.R., Myanmar, Thailand, Malaysia, Philippines, Indonesia and Singapore. The resident mission has been gradually strengthened and is responsible for country economic monitoring, programming and donor coordination functions, in addition to administration of 36 percent of the ongoing loan portfolio. The resident mission has helped the government prepare the results-based SEDP 2006–2010, through a broad, consultative process, including preparing the results framework for monitoring SEDP outcomes. To implement the principles of the Paris Declaration on Aid Effectiveness, the resident mission actively participates in the Partnership Group on Aid Effectiveness with the Government and other development partners, taking a lead in harmonizing social and environmental safeguard policies between the Government and donors. The AsDB also actively participates in the "Six Banks Initiative," with Agence Française de Développement (AfD), KfW development bank, Korea Eximbank, JBIC/JICA and the World Bank, to harmonize project preparation, implementation, monitoring and evaluation practices and improve the quality and effectiveness of investment projects.

AsDB and Fund staff work closely together to support the process of economic reforms in Vietnam. AsDB staff interacts with Fund missions, exchange information, and regularly consult on policy matters. The resident missions of the two institutions cooperate closely. The AsDB is taking part in the 2008 Vietnam debt sustainability analysis for the first time, with the Fund and the World Bank.

Table 1. Vietnam: Public Sector Lending, by Sector, October 1993–December 2008
(In millions of U.S. dollars)

Sector	Number	Approved Amount
Lending	78	6,031.0
Agriculture and natural resources	15	912.5
Education	7	323.0
Energy	6	883.8
Finance	7	410.0
Health, nutrition, and social protection	5	231.2
Industry and Trade	4	98.5
Law, economic management, and public policy	5	176.4
Transportation and Communications	16	2,372.2
Water supply, sanitation, and waste management	6	357.2
Multi-sector	7	265.7
Technical assistance	225	175.2
Advisory and operational purposes	145	107.1
Project preparation	80	68.1

Source: Asian Development Bank.

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Table 2. Vietnam: Sovereign Loan Approvals and Disbursements, 1997–2008

(In millions of U.S. dollars)

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Loan approvals	359.60	284.00	220.00	188.50	243.10	233.50	179.00	296.40	577.70	308.19	1,438.86	764.70
Loan disbursements	149.3	127.8	191.2	218.9	176.2	231.7	233.2	182.4	223.7	184.07	229.88	264.56
Un-disbursed balance at the												
beginning of the year 2/	842.42	997.48	1,191.56	1,190.38	1,086.15	1,118.80	1,198.10	1,191.59	1,313.69	970.63	1,316.67	1,456.84
Memorandum item:												
Technical assistance approvals	9.51	5.93	10.34	9.12	8.42	9.28	8.61	7.68	12.25	16.07	13.12	25.81

Source: Asian Development Bank.

1/ Excludes approved loans that are not yet effective.

ANNEX IV. VIETNAM: STATISTICAL ISSUES

As of January 21, 2009

I. Assessment of Data Adequacy for Surveillance
General: Data provision has some shortcomings, but broadly adequate for surveillance. Most affected areas are: national accounts, government finance and external sector statistics.
National Accounts: The General Statistics Office (GSO) provides quarterly (cumulative) and annual data on GDP by type of economic activity and annual data by expenditure (both in current and constant prices), and monthly and annual data on external trade, industrial output, retail sales, and prices. The annual constant price GDP estimates have 1994 as the base year and are in need of updating. While the national accounts methodologies are broadly consistent with the *SNA93*, the compilation process suffers from poor data collection practices and a lack of coordination and communication between data collection agencies. **Prices statistics:** The CPI methodology is largely in line with international standards. However, there is only a notional inclusion of owner-occupied and rental housing. Also, there is a need to adopt a geometric mean of price relatives at the lower level of aggregation, instead of the upward biased arithmetic mean. Trade price indices are also compiled, but not used in the national accounts.
Government finance statistics: Budget classification is broadly consistent with the *1986 GFSM*. Government operations data reflect the consolidated operations of the state budget, which cover all four levels of government (central, provincial, district, and commune). However, they exclude data on off-budget investment expenditure, quasi-fiscal activities of state-owned enterprises (SOEs), and extrabudgetary 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 compiled on a regular basis. Compilation is on a cash basis for final annual data, but varies for provisional data depending on their source. As a result, government financing data, in particular domestic bank financing, cannot be reconciled as reported in the fiscal and monetary accounts. The Bank and the Fund have recommended improving the coverage of fiscal data.
Monetary statistics: A key shortcoming is insufficient sectorization of bank credit. STA has encouraged the SBV to develop a reporting scheme for a comprehensive breakdown of banks' credit to the economy by borrowing sectors, sub sectors, and ownership of enterprises. In addition, STA has recommended that: (a) a list of SOEs that have been privatized and therefore should be classified as private enterprises should be distributed to banks in order to guide their data reporting on enterprises; (b) funds for on-lending should be reclassified out of banks' "unclassified liabilities" to "other deposits." Further cooperation from the authorities is needed to resolve data discrepancies involving credit data for a state-owned bank. These discrepancies may reflect possible noncoverage and/or omission of certain loans and financial leases, offset by lower deposits and other liabilities.

External sector statistics: Monthly and annual trade data have been compiled using customs reports, but the coverage and accuracy of these data need to be improved. In particular, the commodity breakdown of a large share of reported exports and imports (approximately 17 percent and 27 percent respectively in 2006) is unknown. Data on invisibles continue to be based largely on banking records, which provide incomplete coverage and identification of the types of transactions. Improvements are particularly needed for data on tourism revenue and workers' remittances. STA has recommended that the GSO, Ministry of Planning and Investment, and State Bank of Vietnam work jointly to improve FDI questionnaires and processes, including collecting data on both stocks and flows. Overlapping responsibility for debt statistics has at times resulted in some deficiencies in coverage, including the lack of monitoring certain leasing arrangements (e.g., for aircraft).	
II. Data Standards and Quality	
Participant in the General Data Dissemination System (GDDS) since September 2003.	No data ROSC is available.
III. Reporting to STA	
Annual GFS data through 2004, excluding extrabudgetary funds and social security funds, have been reported for publication in the *GFS Yearbook*, using the 1986 GFS format. No sub-annual fiscal data have been reported for publication in *IFS* since 2001.	

Vietnam: Table of Common Indicators Required for Surveillance
As of January 21, 2009

	Date of Latest Observation	Date Received	Frequency of Data[8]	Frequency of Reporting[8]	Frequency of Publication[8]
Exchange Rates	Oct. 2008	12/19/08	D	M	W
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	5/31/07	6/27/07	M	I	NA
Reserve/Base Money	Sep. 2008	12/29/08	M	I	NA
Broad Money	Sep. 2008	12/29/08	M	I	NA
Central Bank Balance Sheet	Sep. 2008	12/29/08	M	I	NA
Consolidated Balance Sheet of the Banking System	Sep. 2008	12/29/08	M	I	NA
Interest Rates[2]	Oct. 2008	12/29/08	M	I	NA
Consumer Price Index	Dec. 2008	1/16/09	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	...	...	...	...	NA
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	6/30/07	8/1/07	Q	Q	A
Stocks of Central Government and Central Government-Guaranteed Debt[5]	2006	6/26/07	I	I	NA
External Current Account Balance	Q4 2007	5/27/08	A	A	A
Exports and Imports of Goods and Services[6]	Q4 2007	5/27/08	M	M	M
GDP/GNP	7/31/06	7/23/07	Q	Q	Q
Gross External Debt	2006	8/3/07	I	A	NA
International Investment Position [7]	...	...	NA	NA	NA

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Services data available on an annual basis.
[7] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

Statement by the IMF Staff Representative on Vietnam
March 16, 2009

1. This statement provides information on economic and policy developments that has become available since the staff report was circulated to the Executive Board on March 2, 2009. This information does not alter the thrust of the staff appraisal.

Economic and financial developments

2. **Indicators of economic activity are all pointing to a slowdown.** In the first two months of 2009, industrial production growth slowed to 2½ percent (y/y), with large contractions in many items including steel, electronics, cars, motorcycles, and footwear. Retail sales weakened significantly, growing by only 1¼ percent (y/y) in real terms. Tourist arrivals also declined by 15 percent (y/y). Vietnam's growth prospects are likely to worsen in light of these developments and the rapid deterioration in the global environment, although the fiscal stimulus plan (see below) may help mitigate the downturn.

3. **Inflation continues to decline owing to falling food and fuel prices.** Headline inflation moderated to 14.8 percent (y/y) in February, turning negative on a month-on-month basis for four months in a row. Core inflation (excluding raw food and energy) also fell to 13.7 percent, and saw the first month-on-month drop (0.2 percent) in nearly six years.

4. **A significant contraction in imports contributed to an improvement in the trade balance, which recorded a small surplus in the first two months.** Exports of goods fell by 5 percent (y/y), notably crude oil, rubber, electronics, and wooden and ceramic products, while imports contracted by 43 percent, with significant declines in nearly every category. Exports to traditional markets, such as the United States, European Union, Japan, and ASEAN have reportedly declined by 20 percent (y/y).

5. **However, this has been offset by a weakening of capital inflows.** Portfolio investment outflows continued, contributing to a further decline in the stock market (by 20 percent year-to-date), and foreign investors have been divesting their remaining bond holdings. As a result, the dong has continued to trade at the weaker end of the band. In January, gross international reserves fell by $0.7 billion to $22.3 billion.

Policy developments

6. **Monetary conditions have been relaxed further.** While the State Bank of Vietnam has kept the base rate unchanged at 7 percent since February, the reserve requirement ratio for dong deposits was reduced further to 3 percent from 5 percent effective March 1. Banks have started extending loans under the interest rate subsidy scheme which began in early February, with the bulk of the loans channeled by state-owned commercial banks.

7. **The government is expected to submit a revised budget plan for 2009 to the National Assembly in May.** The authorities have started implementing some of the stimulus measures. Preliminary staff estimates based on limited available information suggest that the aggregate cost of the stimulus package could be large (4 percent of GDP), but these estimates are still subject to a significant degree of uncertainty. Moreover, they have not yet been integrated into a revised budget, and it is not clear to what extent the package might be financed by reallocation of existing expenditures. Consequently, the total size of the fiscal stimulus in 2009 and how it will be financed are still not clear. Nevertheless, these estimates reinforce staff's concerns about the need for a revised fiscal plan that is consistent with available financing. In the absence of additional concessional external financing, a sizable fiscal stimulus could further weaken the external position, crowd out private sector activity, and undermine fiscal sustainability prospects. With regard to the measures, while measures to support the poor and the removal of some export duties are welcome, staff is concerned that other measures are inefficient and not well targeted.

Vietnam: Fiscal Stimulus Measures for 2009
(In percent of GDP)

Measures	Nature	Cost
Revenue (total)		1.7
30 percent corporate income tax (CIT) reduction for small- and medium-sized enterprises	Temporary	0.3
Deferral of CIT payments by nine months for some businesses	Temporary	1.0
Delay in personal income tax payments for five months 1/	Temporary	0.3
50 percent VAT reduction for selected goods and services and for imports	Temporary	0.1
Provisional VAT refund for exporters	Temporary	Negligible
Deferment of time for payment of import duty for some sectors	Permanent	Negligible
Elimination of export duty on exported timber goods produced from imported timber	Permanent	Negligible
Removal of export duty on selected products 2/	Permanent	Negligible
Expenditure (total)		2.3
Subsidized credit for enterprises	Temporary	1.0
Increase in off-budget capital spending	Temporary	0.5
Social safety net measures:		
Policies to reduce poverty in 61 districts	Temporary	0.4
Promoting investment in housing for the poor	Temporary	0.2
Support for low-income civil servants	Temporary	0.1
Total cost		4.0

Sources: Information provided by the Vietnamese authorities; and IMF staff estimates.

1/ Assumes these payments will be foregone.
2/ Exported rice and fertilizer, crude and pure copper, and barium and apatite ore.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 09/36
FOR IMMEDIATE RELEASE
March 17, 2009

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2008 Article IV Consultation with Vietnam

On March 16, 2009, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Vietnam.[1]

Background

Following an extended period of strong economic performance, Vietnam is facing considerable challenges. Growth moderated to 6.2 percent in 2008, from a historical average of 7½ percent. Rapid credit growth fueled by massive capital inflows, coupled with a surge in commodity prices, led to high inflation and large trade deficits in the first half of 2008. While inflation pressures are subsiding with easing food and energy prices, growth is expected to slow further to 4¾ percent in 2009 on the back of weaker domestic and external demand. The current account deficit is projected to decline to 8 percent of GDP, mainly due to lower imports. Near-term risks are on the downside, as the deteriorating global environment could worsen Vietnam's growth prospects and reduce capital inflows, putting pressure on reserves and the exchange rate. A slower pace of economic activity could also heighten banks' vulnerabilities.

Spillover effects from the global turmoil have become more apparent since October 2008. Exports of goods and services, private remittances, and foreign direct investment have all weakened. Risk aversion remained acute, prompting foreign investors to continue reducing their portfolio exposures to Vietnam, particularly in bonds, and the stock market lost two-thirds of its value in 2008. Depreciation pressures on the dong have also resurfaced.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

Macroeconomic policies have reversed course as concerns over growth increased and inflation pressures waned. Earlier in 2008, the State Bank of Vietnam (SBV) made considerable efforts to stabilize the overheating economy. In the fourth quarter, the SBV rapidly eased monetary policy by lowering its policy rates by 7 percentage points to 7 percent, and reducing reserve requirements sharply. To alleviate depreciation pressures on the exchange rate, the SBV devalued the dong and widened the dong-U.S. dollar trading band. However, the dong has continued to trade at the weaker end of the band. More recently, the government has announced a broad economic stimulus plan aiming to support growth and protect vulnerable groups.

Fiscal policy has also become accommodative. With spending stepped up in the final quarter, the overall fiscal balance in 2008 is estimated to have recorded a deficit of 4¾ percent of GDP. The original 2009 budget plan (excluding the stimulus plan) indicates a widening of the overall deficit to about 8¼ percent of GDP with a large domestic financing, reflecting lower revenue from oil and recent tax reforms and an increase in off-budget expenditure and net lending. The non-oil primary deficit is projected to rise slightly.

Strains in the banking system emerged in 2008. Banks have high loan-to-deposit ratios and rely heavily on short-term interbank funding, and their profit margins were squeezed by the higher funding costs and caps on lending rates. Smaller joint-stock banks were reportedly most affected, with some obtaining liquidity support from the SBV. Nonperforming loans (NPLs) doubled to 3 percent in October 2008 from the end-2007 level, and some banks are likely to face a substantial increase in NPLs with a slowing economy.

Executive Board Assessment

Executive Directors commended the Vietnamese authorities for the significant progress they have made in stabilizing the economy, which was overheating in 2008. Directors welcomed the recent improvements in inflation and the trade balance. They noted, however, that Vietnam is facing substantial near-term challenges stemming from the sharp deterioration in global economic and financial conditions, and that risks are tilted firmly to the downside. Economic growth is expected to slow in 2009 with capital inflows, exports, and private remittances likely to decline significantly, while the current account deficit will remain large. Slower growth could also heighten banking system vulnerabilities. At the same time, Directors agreed that the medium-term outlook is favorable, with Vietnam remaining an attractive destination for foreign investment.

Directors considered that an accommodative fiscal stance in 2009 to help mitigate the economic downturn is appropriate. They cautioned, however, that in the absence of additional concessional external financing, a large stimulus could further weaken the external position, crowd out private sector activity, and undermine fiscal sustainability. Most Directors encouraged the authorities to revise their budget plan for 2009 in the light of these concerns, and with a view to ensuring that the stimulus measures envisaged are well targeted and effective in supporting aggregate demand.

While welcoming the recent tax reforms, Directors agreed that longer-term revenue and expenditure reforms will be needed to preserve fiscal sustainability. They called for further efforts to broaden the tax base. Also, the structure of expenditures should be reviewed to ensure the efficiency of public investment and the protection of vulnerable groups. Directors welcomed the initiative to revise the state budget law.

Directors advised the authorities to assess the effects of recent monetary adjustment before considering easing further. To strengthen the monetary framework, they recommended improvements in open market operations and liquidity management. Directors took note of the recent devaluation of the dong and the widening of its exchange rate trading band, and in that context, they welcomed the authorities' intention to allow greater exchange rate flexibility, supported by appropriate macroeconomic policies. They noted the staff's assessment that the dong appears somewhat overvalued compared with its estimated medium-term equilibrium level, although the precise degree of the deviation is difficult to ascertain.

Directors considered that the strengthened capital position and improved provisioning practices of Vietnamese banks may provide them with a buffer against the impact of the economic slowdown. Nevertheless, bank loan portfolios could come under pressure as economic growth slows. Directors encouraged the authorities to develop a more comprehensive contingency plan to help the banking sector confront the effects of the global financial turmoil. Directors welcomed the recent efforts to improve bank supervision, but called for further improvement to ensure that bank vulnerabilities are assessed in a timely and effective manner. They encouraged the authorities to advance financial sector reform, in particular, strengthening the operational autonomy of the State Bank of Vietnam.

Directors welcomed the authorities' intention to press ahead with the reform of state-owned enterprises (SOEs), while noting that the equitization process has been postponed due partly to unfavorable market conditions. The planned reforms will help strengthen the performance and governance of SOEs and sustain Vietnam's rapid pace of economic development.

Directors welcomed the steps taken to improve data provision, and emphasized that this—along with an effective public communication strategy—will help bolster investor confidence. They encouraged the authorities to continue to improve the quality and timeliness of data, especially in the areas of the fiscal accounts, SOEs, and banking.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Vietnam: Selected Economic Indicators, 2005–09 1/

	2005	2006	2007	2008 Est.	2009 Proj.
Real GDP (annual percentage change) 2/	8.4	8.2	8.5	6.2	4.8
Saving and investment (in percent of GDP) 3/					
Gross saving	34.5	36.5	31.8	31.2	25.1
Private	26.7	28.1	26.2	26.1	23.0
Public	7.8	8.4	5.6	5.1	2.1
Gross investment	35.6	36.8	41.6	41.5	33.2
Private	24.1	26.4	30.3	32.2	24.0
Public	11.5	10.4	11.4	9.3	9.2
Inflation (annual percentage change) 2/					
CPI (period average)	8.3	7.5	8.3	23.1	8.0
CPI (end of period)	8.8	6.7	12.6	19.9	6.0
GDP deflator	8.2	7.3	8.2	21.7	4.8
General government (in percent of GDP)					
Official fiscal balance	-0.1	1.1	-2.2	-1.6	-4.1
Revenue and grants	27.2	28.7	27.6	27.2	24.0
Expenditure	27.3	27.5	29.8	28.8	28.1
Off-budget expenditure and net lending	4.4	2.2	3.1	3.1	4.1
Overall fiscal balance 4/	-4.5	-1.1	-5.3	-4.7	-8.2
Non-oil primary fiscal balance 4/	-11.7	-8.8	-11.1	-9.4	-9.7
Money and credit (annual percentage change, end of period) 2/					
Broad money	29.7	33.6	46.1	20.3	…
Credit to the economy	31.7	25.4	53.9	25.4	…
Interest rates (in percent, end of period) 2/					
Nominal three-month deposit rate (households)	7.8	7.9	7.4	8.1	...
Nominal short-term lending rate (less than one year)	12.0	11.8	11.8	11.5	...
Current account balance (including official transfers)					
(In billions of U.S. dollars)	-0.6	-0.2	-7.0	-9.2	-7.3
(In percent of GDP)	-1.1	-0.3	-9.8	-10.3	-8.1
Exports f.o.b. (annual percentage change, U.S. dollar terms)	22.5	22.7	21.9	29.5	-15.5
Imports f.o.b. (annual percentage change, U.S. dollar terms)	15.0	22.1	38.3	27.6	-19.9
Foreign exchange reserves (in billions of U.S. dollars, end of period)					
Gross official reserves, including gold 2/	8.6	11.5	21.0	23.0	20.7
(In months of next year's imports of GNFS)	2.2	2.1	3.0	4.1	3.3
External debt (in percent of GDP) 5/	32.5	31.4	33.3	29.8	31.9
External debt service (in percent of exports of GNFS)	4.5	4.2	3.8	3.4	4.5
Total public and publicly-guaranteed debt (in percent of GDP)	44.5	44.1	46.3	44.4	47.5
Dong per U.S. dollar exchange rate (end of period) 2/ 6/	15,907	16,068	16,003	17,486	...
Nominal effective exchange rate (end of period) 7/	83.6	77.3	73.3	75.4	...
Real effective exchange rate (end of period) 7/	99.8	96.8	100.5	121.9	...
Memorandum item:					
GDP (in trillions of dong at current market prices)	839	974	1,144	1,479	1,623

Sources: Data provided by the Vietnamese authorities; and IMF staff estimates and projections.

1/ Figures in 2008-09 are staff estimates and projections unless otherwise indicated. Projections for 2009 do not take into account the recently announced stimulus plan.
2/ Figures for 2008 are actual.
3/ The private sector includes state-owned enterprises.
4/ Includes off-budget expenditure and net lending.
5/ Includes private debt.
6/ Interbank exchange rate.
7/ 2000 annual average=100.

Statement by Perry Warjiyo, Executive Director for Vietnam and Narayanan Raman, Senior Advisor to Executive Director March 16, 2009

1. On behalf of the Vietnamese authorities, we thank Mr. Ishii and his team for their constructive engagement and candid discussions, which have been usefully crystallized in the concise set of papers. The authorities found these discussions to be helpful in clarifying their thinking on a number of key issues. We would like to provide some background on recent developments and the authorities' view of the near-term outlook, and the policy options under consideration. We also wish to highlight the key areas where deeper engagement with the Fund could be especially helpful.

Recent Developments and Outlook

2. In the early part of 2008, the Vietnamese authorities faced difficult challenges in relation to domestic economic management, which have usefully been outlined in the staff report. While growth remained robust, with GDP increasing by 6½ percent in the first six months of the year, inflation and the trade deficit both rose significantly, partly as a result of the worldwide impact of rising food and fuel prices. It should also be noted that part of this increase is explained by one-off supply shortages arising from unfavourable weather conditions and plant and livestock disease in the early part of the year. For these reasons, inflation, which had hitherto been maintained at a relatively comfortable level, rose to over 28 percent during the year. At the same time, the trade deficit in 2008 reached US$18 billion, resulting in an expansion in the current account deficit.

3. In response to these developments, the authorities reacted with commendable swiftness, tightening monetary policy and instituting a more prudent fiscal stance. Directors will recall that at the time of the staff's informal briefing to the Board in June 2008, we outlined the authorities' 8-point solution package that included deferment or cancellation of a number of public projects, a tightening of monetary policy, and structural reforms to enhance overall economic efficiency. Even at that early stage, the measures' effects were already being felt and staff have helpfully highlighted that this improvement continues to gain momentum. Inflation clearly has peaked and will retreat to more comfortable levels by end-2009, while the trade deficit is rapidly correcting. The authorities also note that in January 2009, the trade account recorded its first surplus in three years, and expect this improvement to continue going forward.

4. The authorities concur with staff that the outlook for 2009 continues to be subject to great uncertainty. It is clear that global macroeconomic conditions will continue to deteriorate. As a result of the adverse outlook, the authorities have rightly shifted their focus from inflation to growth, a view that staff endorse. In general, the authorities concur with the staff's assessment of broad agreement on the direction of policy. On monetary policy, the

authorities have already taken proactive measures to respond to the crisis. As a result, money market conditions have remained stable, allowing credit to continue to flow. Going forward, policy will take into account the steady decline in inflation. In terms of the fiscal stance, the tighter position in 2008 will be appropriately relaxed in 2009 to help stimulate the economy.

5. Further, the authorities agree with staff's assessment that there is a downside risk to growth. In view of this, Vietnam's central bank, the State Bank of Vietnam (SBV), has been instructed to closely monitor and assess the US and global financial markets in order to identify the impact of the crisis, and to propose solutions to the Prime Minister. The key issue is one of how best to protect the Vietnamese economy while ensuring that hard won gains on macroeconomic stability are preserved. Thus, the authorities have introduced and implemented a number of measures to actively respond to the negative impact of the global financial crisis and resulting economic slowdown. In particular, the authorities have adopted a Resolution on emergency measures to counter the economic slowdown, sustain growth and ensure social safety. The main aims of the package are to:

- Promote production, business and exports;
- Stimulate consumption and investment;
- Implement flexible monetary and financial policies;
- Ensure social safety; and
- Ensure the full and well-targeted implementation of these measures.

6. Having said that, the authorities are well aware that any stimulus, particularly fiscal stimulus, will need to be financed domestically, given the sense of flux in global markets. Therefore, the authorities will ensure that any moves to source funding from domestic bond markets will be done in a sustainable manner. The authorities are also keen to point out that like many economies in the region, Vietnam has a high savings rate and in this environment, government bonds remain an attractive asset. The authorities would also like to clarify that their stimulus plans are not being crafted in response to regional "peer pressure". It is, however, true that the stance of regional peers provides additional information regarding the cyclical position of the regional and global economies. Further, the sizes of the various responses provides a useful cross-check to the authorities' own planned response.

7. The authorities agree with staff's recommendation to enhance communication. In fact, communication and the provision of data has received great attention and the authorities have made considerable progress. Important data on macroeconomics, financial, banking, business etc. have been provided in a more timely and comprehensive manner, thereby enhancing investor's confidence.

8. The authorities fully agree with staff that the medium-term outlook for Vietnam remains positive. Continuing inflows of foreign direct investment in these difficult times

indicates that global investors share this assessment as well. Since the beginning of the year, the authorities licensed 67 projects with a total investment value of US$1.5 billion.

External Stability

9. The SBV reiterated its goal to allow significantly greater flexibility to the *dong* over the medium term, and fully agree with staff's assessment that greater flexibility would be appropriate with the increasing sophistication of the Vietnamese economy. However, this transition is being pursued with appropriately prudent steps in order to avoid any negative impact on Vietnam's economy and external position. In the DSA, staff have clearly shown that the balance sheet effects of a large *dong* depreciation could be significant. Further, too significant a depreciation could reverse the process of de-dollarization, thereby rendering monetary policy less effective. Having said that, the authorities can confirm that the candid discussions with the staff on the options available were particularly helpful. They intend to look at all options, including adjusting the trading band and keeping a close eye on the central rate during this process. The authorities also point out that following the steps taken on the exchange rate in 2008, the *dong'*s value in the parallel market, which had diverged from the official rate, closed significantly to within 2 percent.

10. The authorities also note that while it has risen, the current account deficit remains fully funded by stable long-term flows including concessional financing, ODA and foreign direct investment. They also note that should some of these flows decline, there will be an automatic correction in the current account due to lower capital and intermediate imports. Further, the deep pool of domestic savings has meant that the exit of foreign portfolio investors was covered by local investors. Foreign portfolio investors have mostly exited the Vietnamese market and further outflows present a negligible risk. The reserves position remains relatively ample at over US$22 billion, allowing the SBV to ensure the foreign exchange market continues to function.

11. The authorities agree with the primary conclusions of the DSA exercise, particularly that Vietnam remains at low risk of distress. As staff have rightly pointed out, Vietnam's debt position has historically been robust, which is the product of a very prudent debt management strategy. The authorities intend to maintain this strategy, carefully calibrating the level of debt to the capacity of the economy to bear the risks. Public debt, in particular, has risen in recent years but the authorities stress that part of this has been related to meeting pressing infrastructure needs. Addressing these needs could enhance economic efficiency, thereby raising overall growth levels. The authorities believe that by strong growth, the debt position will become even sounder going forward. Further, a part of the outlays were to put state-owned enterprises on a sounder footing, and will be recouped when privatization (equitization) takes place. The bigger challenge will be the gradual loss of access to concessional resources in the transition to being a full-fledged emerging market economy.

Financial Sector Stability and Policies

12. The authorities found the staff's analysis of financial sector stability to be balanced and well researched. They agreed with many of the key findings, most notably that Vietnamese banks remain in a strong position. Capital levels have been raised, non-performing loans remain low and provisioning practices improved. As at end-2008, equity capital in the banking system increased by 30 percent compared with the level a year earlier, while the capital adequacy ratio improved from 8.9 percent to 9.7 percent over the same period. Further, the very conservative valuation practices, coupled with equally prudent levels of financing, mean that loans given out cover between 35-50 percent of the assessed value of any asset. This has kept NPLs from rising significantly and provides banks with significant protection against credit risks arising from changes in valuations. While the NPL ratio increased to 2.1 percent at the end of 2008 compared to 1.5 percent as at end- 2007, the authorities note that this is still a very low level and well within control.

13. Nevertheless, the SBV has taken proactive steps to ensure that emerging risks are minimized. These include:

- Requiring commercial banks to review all their deposits and investments in foreign banks and financial institutions in order to have contingency plans to reallocate these deposits to safer institutions and those less affected by the crisis;
- Requiring commercial banks to review and check all their investment lending, particularly their exposure to high risk sectors such as real estate and purchase of securities, and to strengthen supervisory and prudential measures on these loans.
- Exercising greater oversight over these risky loans, as well as reviewing and monitoring bank capital levels; and
- Strengthening the bank resolution framework, including completing the development of regulations on debt factoring, setting up vehicles to deal with impaired assets of commercial banks, and preparing and submitting regulations on dealing with problem banks to the Prime Minister. These actions will provide the legal basis for the restructuring of weaker banks and credit institutions, thus ensuring the safety and soundness of the banking system.

14. The authorities expect that the financial sector will continue to exhibit strong growth over the medium term. The staff report clearly highlights the still-significant portion of the population that does not yet have access to the banking system. Therefore, this strong growth should be seen as a form of convergence as the country modernizes. In a financial system at Vietnam's level of development, the authorities believe that the first and best line of defense against risks is capital, which is why they have placed such great emphasis on raising capitalization levels. Having said that, the authorities are well aware of the need to remove institutional roadblocks to greater effectiveness. In this connection, the work being

undertaken on the SBV Law and the Credit and Financial Institutions Law is the cornerstone of the efforts to overhaul and modernize Vietnam's regulatory and supervisory framework. The authorities are grateful to the work being undertaken by MCM in providing them feedback on their proposals. The authorities also appreciate the Fund's assistance in many other areas of financial sector management, including crisis management.

Structural Reforms

15. The authorities continue to implement structural reforms on a number of fronts, spurred by the historic economic transition Vietnam is making as well as in anticipation of full implementation of WTO commitments.

16. On the fiscal front, there is strong impetus to enact and implement the new State Budget Law, which will go to the National Assembly later this year. The Law will improve the relationship between the central and provincial authorities, lay out a clear basis for reporting revenues and expenditures, thereby improving execution of fiscal measures and transparency and timeliness of reporting. In addition, the authorities have embarked on a pilot multi-year rolling budgeting framework for six ministries and three local authorities. The results so far have been positive and the authorities hope to expand the program.

17. The authorities also concur with staff with the need to prepare for the loss of tariff revenues and forestall over-dependence on oil revenues. To this end, the authorities are considering a number initiatives, including setting up a large taxpayers unit and examining the role of taxes on assets. Indirect taxes will also form an important part of future reforms. On the expenditure side, the authorities feel there is a need to balance fiscal sustainability with the pressing needs of a rapidly growing economy. This balance has led to a careful examination of public-private partnerships. Having said this, any recourse to PPP arrangements will be done carefully and prudently, following a period of careful design and testing of modalities. Staff's reminder of the potential risks was very useful in this regard.

18. On monetary policy, the authorities are preparing significant legislative changes that will enshrine the responsibilities and authority of the SBV. In particular, the SBV Law will clarify many of the important roles the SBV will need to play in a fast modernizing economy. They expect to bring a revised draft of the law to the National Assembly shortly.

19. On the financial sector, the authorities will continue to press for better provisioning and risk reporting standards. Staff rightly point out that reporting requirements were tightened significantly with the introduction of the new loan categories. The SBV is also significantly strengthening its supervisory capacity by intensifying both on-site and off-site monitoring. As we noted earlier, the regulators are also working closely with the fiscal authorities to ensure that the crisis resolution framework can meet potential demands. In this

regard, the authorities were satisfied with the framework's robustness in dealing with the market disruptions experienced last May.

The Role of the Fund

20. Unsurprisingly, the key to improved policy formulation and implementation is capacity. The authorities have made key strides in upgrading their capabilities but shortcomings remain. In this regard, the important role played by the Fund, both by staff at headquarters and the Resident Representative's office in Hanoi, cannot be underplayed. It is also worth pointing out that the authorities' have requested assistance from the Fund precisely in the areas where surveillance has highlighted room for improvement. This is a testament that the staff's advice is being taken seriously. It should be noted that in areas such as financial stability, statistical improvements and the fiscal framework, the staff have taken the lead role. In particular, there have been a number of missions during this past year by MCM staff to look at crisis management and resolution frameworks. Work is also being undertaken at HQ to provide feedback on the legislative reforms proposed by SBV to enhance regulatory and supervisory capacity. The authorities hope that the Fund will continue to provide assistance going forward.