

VIETNAM'S CURRENT ECONOMIC SITUATION AND FUTURE PROSPECTS

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After ten years of economic stagnation following the reunification of the country in 1975, after the fall of Saigon, the Communist Party of Vietnam adopted in 1986 a program of broad economic reforms known as the Doi Moi or “renovation.” It introduced new market rules were, opened up to a greater degree of Foreign Direct Investment (FDI) and improved the business climate. By and large, the “Doi Moi” reforms brought about profound changes in the Vietnamese “social fabric.”

Nonetheless, even after this liberalization effort, the Vietnamese government still wields a great deal of control and influence exerts over major economic

sectors through its overly involvement in large state-owned conglomerates and a range of other enterprises, including the banking system. In 2010 alone, the state sector continued to account for about 36% of the Gross Domestic Product (GDP).

The Vietnamese authorities have reaffirmed their long-term commitment to economic liberalization, to international integration and the partial privatization of state enterprises yet the structural reforms necessary to truly modernize the economy are still lagging behind. Such reforms are vital for making Vietnamese industry more productive and profitable.

Macroeconomic Indicators

Since 1986 the Vietnamese economy has been in a slow but sure transition from a purely Soviet-type centralized system, based on agriculture, to a socialist-style market economy. Vietnam is now one of the fastest growing economies in the world. It has indeed recorded annual GDP growth rates of 8% between 1990 and 1997, and 6.2% between 1998 and 2003. From 2004 to 2007 GDP leaped to more than 8% annually, a rate which was slightly reduced in 2008 and 2009, to 6.3% and 5.3% respectively. Growth returned to 6.8% in 2010, according to the World Economic Outlook (April 2011) of the International Monetary Fund.

Currently, the average GDP per capita in Vietnam is \$1,327. In 2008, having recorded GDP per capita of \$1,047, Vietnam left the group of low income countries (after exceeding the low income benchmark of \$995 per capita) and entered the group of lower-middle income countries (World Development Indicators, World Bank). According to the Ministry of Planning and Investment (MPI), the average GDP per capita will reach \$2,100 by the end of 2015, i.e., a level 1.7 times higher than that of 2010. Vietnam is now on track to also exceed the lower-middle benchmark of \$3,946 in the near future and thus enter the group of countries with medium to high income ratings.

The contribution of the agricultural sector to GDP is on the wane, accounting for 20% of GDP in 2010, down from about 25% in 2000. In contrast, the industrial sector, which accounted for 36% of GDP in 2000, gained 5% more, claiming 41% in 2010 (CIA World Factbooks, May 2011). Extreme poverty has declined significantly. The proportion of the population below the poverty line dropped from 37% in 1998 to only 10.6% in 2010 (CIA World Factbooks, May 2011). The Vietnamese government is committed to creating jobs to

meet the challenge of a workforce that grows by over one million people every year

However, growth policies have created grave problems in controlling inflation, which reached 11.8% in 2010. To curb high inflation pressure, the State Bank of Vietnam is pursuing a restrictive monetary policy. High interest rates on loans restrict access to much-needed capital for productive investments.

Foreign trade continues to be the main driver of economic growth, as evidenced by exports accounting for 58.6% of GDP in 2009 and 67.6% in 2010. Nearly seventy-five percent (74.8%) of export earnings in 2010 were derived from fossil fuels and manufactured goods. The main imports were machinery (17.5%), refined petroleum products (11.5%), steel (8.3%) and textiles.

Although exports increased in 2010 by over 25% and imports decreased slightly, the trade deficit actually fell by only 8% of GDP, spurring the government to consider taking administrative measures to limit the consequences of this imbalance. Due to the persistent trade deficit, Vietnam's currency, the dong, continues to face downward pressures, and since 2008 the State Bank of Vietnam has brought down the value of the dong by 20% through a series of corrective devaluations.

Finally, FDI have dramatically increased every year since it was first authorized in 1988.

The 2008-2009 global economic crises had a negative impact on the level of FDI, as it did in most countries of the world. Nevertheless, in 2010, \$18.5 billion of FDI were made, and this figure is expected to reach \$20 billion in 2011.

Accession to the World Trade Organization

In January 2007, Vietnam joined the World Trade Organization (WTO) following a long and tedious negotiation process which lasted over ten years. New opportunities and challenges created by international economic integration have had significant impacts on the economy. The growth in GDP was maintained at a constant rate even during the darkest hours of the financial crisis and the global economic recession. The increase in GDP per capita also led to a rapid expansion of the middle class. Upon accession into the WTO, Vietnam was able to negotiate reasonable preferential terms based upon regional and bilateral investment agreements, which in turn further attracted foreign direct investments.

Although accession into the WTO positively influenced the country's economic growth, it also had negative consequences. The national unemployment rate followed an upward trend, reaching 6.4% in 2010. In addition, WTO membership places greater attention on the structural limitations of the Vietnamese economy and the actual quality of its products, human resources and infrastructure. It also revealed the true proportion of the difficulties and challenges that lay ahead. Acute imbalances in trade relations with some partners became worryingly damaging for the national economy as a whole and for various state owned and private firms.

Business Partners

Today Vietnam's largest trading partners include the United States, China, Singapore, Japan, Australia, Thailand, Germany, Malaysia, the UK and Hong Kong. Trade with Asian economies constitutes about 80% of Vietnam's total trade.

Economic relations with the United States are improving, but are not without problems. The governments in Washington and Hanoi reached a bilateral trade agreement in December 2001, which significantly boosted exports to the United States. Bilateral trade between the two countries increased from \$2.1 billion in 2002 to \$15.4 in 2009. Despite disagreements over textiles and catfish exports, the U.S. has become the second largest trading partner of Vietnam, after China.

Considering the rapid economic growth in China, economic relations with its northern neighbor are of utmost importance to Vietnam's economic success. Following the resolution of most of their territorial disputes, trade with China has begun to take off and, since 2004, Vietnam has imported more goods from China than from any other country.

In November 2004, the Association of Southeast Asian Nations (ASEAN) – of which Vietnam is a member – and China announced their intention to create the largest free trade area in the world before the end of 2010. This project is obviously still ongoing and it would be hazardous to foretell when it will materialize. Earlier, in 2003 and 2004, the European Union (EU) concluded bilateral agreements with Vietnam which eliminated

quotas on Vietnamese import of textiles and clothing. The same terms were guaranteed by Vietnam to the EU, the United States and Japan. Before the end of 2015 sales volume should reach \$1.26 billion, or 1.4 times more than in 2010, and imports will be kept at a level set by the Ministry of Planning and Investment (MPI).

Future Prospects

The MPI expects Vietnam's GDP to reach \$200 billion on condition that the average annual rate of growth attains 7-8% over the next five years. For 2011, the agriculture, forestry and aquaculture sectors combined could account for 18-19% of the GDP production structure; the construction industry for 40-41% and services the remaining 40-41%.

Inflation could still be a serious threat to macroeconomic stability and is expected to grow during the early months of 2012 due to recurring seasonal factors. There is also a possibility that inflationary pressures could be mitigated to varying degree when high interest rates on loans taken out in 2010 begin to mature. Keeping inflation below 7% continues to be the target set by the National Assembly. The Vietnamese government is in principle obliged to achieve this benchmark.

Vietnam's membership in the WTO is considered only as a first step towards the establishment of a larger regional trade zone. The country will need to promote its strengths and confront its challenges, accelerate reforms, improve the quality of growth towards sustainable development and the competitiveness of its industries and businesses. Also, a greater emphasis on private sector development is essential for creating more jobs

To offset the negative impacts of WTO entry, such as higher unemployment rates, the quality of infrastructure and institutional capacity must be further expanded and improved. Vietnam has to be more effective in implementing its policies of international economic integration, focusing on the quality of growth and the degree of foreign investment. It must take measures consistent with macroeconomic and financial stabilization. Vietnamese companies should prioritize joint ventures with foreign partners, while the government should more aggressively seek foreign partners and enhance business cooperation with them.

Vietnam has yet to face many economic challenges, including that of striking a balance between its fiscal policies, which are designed to keep interest rates at reasonable levels and hold inflation in check, and its overall monetary policy, so to prevent a credit crunch that would have a crippling effect on the economy. However, when all is said and done, the Vietnamese economy is still held in high esteem within the international business community, mainly because of its high growth rate and overall macroeconomic stability, two fundamental conditions required for sustainable economic development.

With the economic recovery gathering momentum in many neighboring countries, the increased flow of FDI, a more balanced and pragmatic trade policy and easier access to foreign markets will be conducive to creating appropriate conditions for the Vietnamese economy to take off. This may well result in a substantial reduction in the level of the country's public debt.

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