VIETNAM ANNUAL ECONOMIC REPORT
2014

THE CONSTRAINTS TO GROWTH

Edited by Nguyen Duc Thanh

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VIETNAM ANNUAL ECONOMIC REPORT 2014

"THE CONSTRAINTS TO GROWTH"

Time: 29th May, 2014

Venue: Plaza Ballroom, Sofitel Plaza Hanoi Hotel

No.1 Thanh Nien Str, Ba Dinh, Hanoi

08:00 – 08:30	**Registration**
08:30 – 08:35	Welcome and Introduction
08:35 – 08:40	Opening Remarks by Prof. Dr. Nguyen Huu Duc – Vice President of the Vietnam National University, Hanoi Speech by Ms. Nadia Krivetz – Charge d' Affaires A.I., Australian Embassy in Hanoi
08:40 – 09:10	Introduction on the main contents of the Vietnam Annual Economic Report 2014 *Dr. Nguyen Duc Thanh – Director of Vietnam Centre for Economic and Policy Research*
09:10 – 10:00	Comments from Economic Experts 1. *Dr. Vu Viet Ngoan – Chairman of Vietnam's National Financial Supervisory Commission* 2. *Dr. Le Dang Doanh – Senior Economic Expert, Former President of Central Institute for Economic Management* 3. *Dr. Vo Tri Thanh – Vice President of Central Institute for Economic Management*
10:00 – 10:15	**Tea Break**
10:15 – 11:55	Open discussion
11:55 – 12:00	Closing Statement by *Assocc. Prof. Nguyen Hong Son*, Rector of UEB, VNU
12:00 – 13:00	Luncheon

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Vietnam Annual Economic Report 2014

THE CONSTRAINTS TO GROWTH

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PREFACE

Vietnam Annual Economic Report is a major product in one of Vietnam National University’s key research directions and has been conducted annually since 2009 by Vietnam Centre for Economic and Policy Research, University of Economics and Business. The primary purpose of the Report is to provide scientific evidences for macroeconomic policy-making of Vietnam based on reviewing and analyzing the major achievements, difficulties, opportunities and challenges for the Vietnamese economy. In addition, the Report also discusses in-depth selected macroeconomic issues of the country while maintaining an objective and independent point of view.

As usual, around May, VEPR launches the Report, bringing researchers, policy makers and Vietnamese readers the latest results after a year of meticulous research on macroeconomic situations and specific issues of Vietnam’s economy. In-depth discussion in each chapter of the report, which is resulted from modern approaches and based on empirical evidence, statistics, and analysis that has been updated and thoroughly discussed, has increased the reputation of the Reports and contributed to raise the Reports to become the flagship, not only of VEPR but also of Vietnam National University in Hanoi.

Though the Report is always launched in the first half of the year, it thoroughly discusses fundamental economic issues for the whole year, while forecasts exhibit high degree of accuracy. The Report was developed by a team of renowned domestic researchers and foreign experts. During the process of publications, the Report has been received critics and suggestions from Vietnam's leading experts in macroeconomics, international economics, and finance – banks, etc.

With significant contributions, the Report becomes reference material for managers, policy makers, researchers, and those who concern about macroeconomic issues in Vietnam. In 2013, the report series (2009-2012) was awarded Bao Son Prize Awards in the field of Sustainable Development.

In particular, this year, the copyrights for English version of this Report are under consideration to be published in Japan. Thus, the Report not only contributes to strengthen Vietnamese reader's knowledge but also the voices of Vietnamese intellectuals could be brought to the world. This is the success after five years of meticulous and hardworking as well as the initial "fruits" of the University of Economics and Business, Vietnam National University of Hanoi in the building of a "research university".

After spending 2 years on discussing the progress of economic restructuring in Vietnam, the 2014 Report revives the analysis and study of growth in mid-term and long-term.

We believe that the Vietnam Annual Economic Report 2014: The Constraints To Growth will continue to bring to readers, who are familiar with the Report series during the last five years, useful information on the fundamental issues of Vietnam's economy, through academic and methodological approach.

Hanoi, May 25th, 2014

Assoc. Prof. Dr. Phung Xuan Nha

President of Vietnam National University, Hanoi

ABOUT VEPR

VIETNAM CENTRE FOR ECONOMIC AND POLICY (VEPR) was established on July 7, 2008 as a research center under the University of Economics and Business, Vietnam National University, Hanoi (VNU). VEPR has legal status and its headquarters are located in the University of Economics and Business (UEB), Xuan Thuy, Cau Giay, Hanoi.

VEPR considers its primary mission as carrying out economic and policy research to assist in improving the decision-making quality of policy-making institutions, enterprises and interest groups by providing insights into the social, political and economic factors that drive economic affairs of Vietnam and the region. The main activities of VEPR include (i) providing quantitative and qualitative analysis of changing economic conditions in Vietnam and assessments of their impacts on various interest groups throughout the country; (ii) organizing policy dialogues among policy-makers, entrepreneurs, and other stakeholders to improve solutions to emerging issues; and (iii) conducting advanced training courses in economics, finance and policy analysis regularly and upon request.

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ACKNOWLEDGEMENTS

Vietnam Annual Economic Report 2014 by Vietnam Centre for Economic and Policy Research, University of Economics and Business, Vietnam National University, Hanoi is completed with the support from many individuals and organizations.

First and foremost, the authors would like to express gratitude to the Board of Presidents of Vietnam National University, Hanoi – especially President, Assoc. Prof. Dr. Phung Xuan Nha and Vice-President, Prof. Dr. Nguyen Huu Duc, the Board of Directors of University of Economics and Business, especially Assoc. Prof. Dr. Nguyen Hong Son, those who have encouraged and enthusiastically supported the authors during the last six years to conduct the Report series.

One of the most important contributions that must be mentioned is from ***the Board of Advisors and Commentators***, who have participated in many discussions, workshops and seminars during different stages of the Report. Thanks are due to Dr. Le Dang Doanh, Dr. Luu Bich Ho, Asoc.Prof Dr Le Bo Linh, Dr. Vu Viet Ngoan, Prof. Dr. Sc. Nguyen Quang Thai, Dr. Vo Tri Thanh, and Dr. Dinh Quang Ty for their deep analyses and constructive feedbacks to each chapter of the Report.

We are grateful to Department of Foreign Affairs and Trade, Australian Government for their generous support and cooperation for Vietnam Annual Economic Report.

We are greatly helped by VEPR staffs, especially ***the editing team*** and proofreaders. Their enthusiasm, dedication, and persistence are an indispensable part of this Report.

We would like to express our gratitude to the members of Department of Science and Technology at Vietnam National University - Hanoi and Department for Research and International Relations at the University of Economics and Business, especially Dr. Nguyen Dang Minh and Dr. Nguyen Vu Ha, for their enthusiastic support during the project.

Despite our efforts, we understand that there may be limitations and even errors in the Report. We sincerely hope to receive comments and contributions from the readers to improve our upcoming reports.

Hanoi, May 29th, 2014,

On behalf of the Contributors,

Dr. Nguyen Duc Thanh

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AANZFTA	ASEAN - Australia-New Zealand Free Trade Area
ACFTA	ASEAN - China Free Trade Area
ACIA	ASEAN Comprehensive Investment Agreement
ADB	Asian Development Bank
AEC	ASEAN Economic Community
AFAS	ASEAN Framework Agreement on Services
AFTA	ASEAN Free Trade Area
AIFTA	ASEAN-India Free Trade Agreement
AJCEP	ASEAN-Japan Comprehensive Economic Partnership
AKFTA	ASEAN-Korea Free Trade Agreement
APSC	ASEAN Political - Security Community
ASCC	The ASEAN Socio-Cultural Community
ASEAN	Association of Southeast Asian Nations
ATIGA	ASEAN Trade in Goods Agreement
BOI	The Board of Investment of Thailand
BOJ	Bank of Japan
BTA	The U.S.-Vietnam Bilateral Trade Agreement
C/O	Certificate of Origin
CAR	Capital Adequacy Ratio
CEPT	The Common Effective Preferential Tariff
CLMV	Cambodia-Lao PDR-Myanmar-Viet Nam
CPI	Consumer Price Index
dGDP	GDP deflator
ĐPT	Developing
ECB	European Central Bank
eCoSys	e-Certificate of Origin System
EU	European Union
EUR	Euro
EVN	VietNam Electricity
FAO	Food and Agriculture Organization
FDI	Foreign Direct Investment
FED	Federal Reserve System
FSAP	Financial Sector Assessment Program
FSIs	Financial Soundness Indicators

GATS	General Agreement on Trade in Services
GDP	Gross Domestic Product
GSO	General Statistics Office
GW	Gigawatt
GWe	Gigawatt - Electric
GWh	Gigawatt Hour
HKW	A Matrix of Test by Hausmann, Klinger, & Wagner
HNX	Hanoi Stock Exchange
HOSE	Ho Chi Minh City Stock Exchange
HRV	Hausmann-Rodrik-Velasco Model
HSBC	The Hongkong and Shanghai Banking Corporation
IAI	Initiative for ASEAN Integration
IEA	International Energy Agency
IEF	Index of Economic Freedom
IIP	Index of Industrial Production
ILO	International Labour Organization
IMF	International Monetary Fund
IPR	Intellectual Property Rights
ISEAS	Institute Of Southeast Asian Studies
KORUS	U.S. - Korea Free Trade Agreement
kWh	Kilowatt hour
LCOE	Levelized Cost of Energy
M&A	Mergers And Acquisitions
M2	Broad Money
MoF	Ministry Of Finance
MPI	Ministry of Planning & Investment
MRAs	Mutual Recognition Agreement
MW	Megawatt
MWe	Megawatt - Electric
NDT	Chinese Yuan
OECD	Organization for Economic Co-operation and Development
OMO	Open Market Operations
P/E	Price-Earnings Ratio
PCI	Provincial Competitiveness Index
PMI	Purchasing Managers Index
PT	Developed
QE	Quantitative Easing

R&D	Research and Development
RCA	Revealed Comparative Advantage
RIA - Fin	Financial Integration of ASEAN
ROA	Return On Assets
ROE	Return on Equity
SBV	State Bank of Vietnam
SITC	Standard International Trade Classification
SOE	State-Owned Enterprise
TC	Trade Complementarity Index
GSO	General Statistics Office Of Vietnam
TNCs	Transnational Corporation
TPP	Trans-Pacific Partnership Agreement
TPSEP	Trans-Pacific Strategic Economic Partnership
TRIPS	Trade-Related Aspects of Intellectual Property Rights
TTIP	Transatlantic Trade and Investment Partnership
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
USD	United States dollar
VAMC	Vietnam Asset Management Company
VAT	Value Added Tax
VND	Vietnam dong
VST	Vietnam State Treasury
WB	World Bank
WGC	World Gold Council
WGI	Worldwide Governance Indicators
WIPO	World Intellectual Property Organization
WTO	World Trade Organization

EXECUTIVE SUMMARY

The content of the Vietnam Annual Economic Report 2014, in addition to two chapters evaluating and commenting on the world and Vietnam's economic situation in 2013, is devoted to the analysis of the specific issues of the constraints to economic growth of Vietnam, based on growth diagnostic method. Given detected main constraints, the Report focuses on in-depth analysis of some of the main constraints for the economy, including the financial aspect that is evaluated through the assessment of commercial banking system in Vietnam by the financial soundness indicators (FSIS); challenges in the process of international economic integration; binding constraints regarding energy through the energy policy choices of Vietnam. Finally, the Report presents general observations about the economic outlook for 2014 and suggests policies to support the economic recovery and maintain macroeconomic stability.

OVERVIEW OF THE WORLD ECONOMY IN 2013

In 2013, the world economy continued to grow at a low rate, even lower than the forecasts from the international organizations, such as IMF and the World Bank, at the beginning of the year. At the growth rate of 3% in 2013, the global economic growth has remained low for 5 consecutive years. This showed that the world economy is in an orbit of low growth so that the discussions on "crisis," "recovery," or "decline" have been subdued. Although economic growth rates in the Eurozone and Japan were slightly higher than 2012, the U.S.'s growth returned to 2011's level. Besides, growth in developing economies is also lower than that of 2 years ago. In 2013, China's GDP growth reached at 7.7 %, in consistency with previous anticipation that it is shifting to a new development model at lower growth rate.

The consequences of such slow growth are high unemployment and pressure on urgent improvements in the budget deficits in the developed economies. The banking system in the Eurozone remained unstable, making businesses difficult in accessing credits to implement investment projects and creat new jobs. In 2013, there were about 202 million people unemployed in the world, increased by 5 million from previous year according to the ILO (2014). Job creating did not keep pace with growth in the labor force, making worldwide unemployment rate stand at 6 % in 2013.

THE CONSTRAINTS TO GROWTH

International trade is no longer a growth engine of the global economy. The world trade flows remained subdued, rose by 3% in 2013, which is slightly higher than 2.8 % in 2012, 50% less than 2011 and 25% less than 2010. Furthermore, imbalances in the current accounts of a number of developing economies went on a downtrend, from 5 % to about 2 % of global GDP, according to the OECD (2014). This improvement was driven by narrowing the deficits in some countries having large deficits, namely the U.S., and reducing surpluses in countries with large surpluses, for examples China, Japan, the EU and oil-exporting countries. The year 2013 also witnessed several rounds of negotiation on regional trade. In particular, two important regional trade agreements that attracted the world attention are Trans-Atlantic Trade and Investment Partnership (TTIP) and Trans-Pacific Partnership (TPP). TTIP is the largest bilateral trade agreement which has ever been negotiated between the EU and the U.S. The signing of this agreement will create a new momentum for trade liberalization, open markets, contribute to boosting economic growth and job creation for countries on two sides of the Atlantic. TPP is considered the 3rd generation of free trade agreements with negotiated contents not limited to traditional issues such as the origin of goods, food safety, the customs but also important areas namely intellectual property, public procurement, and labor conditions. This agreement is expected to become the alternative version of the Doha Round of WTO, which mainly deals with protectionist measures at the border.

After a decline in 2012, the global FDI flows increased slightly in 2013, equal to the average growth rate during 2005-2007, especially the M&A outbound transactions rose 5% while green-field investment (GI) unchanged from 2012. The number of M&A transactions in developing countries reached to the pre-crisis level and the majority were outbound to TNCs in other developing countries. This is a new trend in comparison with 2007 surveyed by UNCTAD for the TNCs of emerging economies and developing countries. According to the survey, only 24% of respondents would choose M&A and 46 % of respondents choose GI, whereas before the crisis, M&A by TNCs in developing countries accounted for over 70 % FDI in these countries.

Due to low economic growth of developed economies during the early months of 2013, the viewpoint of keeping loosing monetary policy emerged in many economies. The U.S. maintained quantitative easing QE3 throughout 2013 and only began to taper since December 2013 when the labor market signaled some improvement. The ECB and BOJ continued to pursue their monetary easing solution in order to prevent low inflation. By being persistent on selected strategic policies, those major economies are expected to push the global economic growth slightly in 2014. As the results, developed countries, particularly in Europe and the U.S., would boost international investment (foreign investment out of the U.S., Japan and the EU are estimated to increase by 10 % and reach USD 950 billion in 2014). In some forecasts for 2014 – 2015, since the developed economies would recovery, the global M&A activities will gradually increase and they will be performed by TNCs in both developed and emerging markets. Due to economic recovery, countries that wish to attract FDI inflows in the form of M&A, including Vietnam, should adjust policies and implement measures to improve their investment environments to become more attractive.

Since the beginning of 2014, the Fed has continued tappering QE3 for two times and intended to shutdown this package by the end of the year. The U.S. will use interest rate as a monetary policy instrument, which can cause certain pressure on the exchange rate for many countries, including Vietnam. China has loosened the exchange rate control, the currency trading band has been doubled from 1% to 2% on either side of the Chinese central bank's daily reference rate announced in early 2014. This is a move in contrast to many previous forecasts that China's Yuan would appreciate in 2014 along with the liberalization roadmap for foreign currency transactions.

In the context of grim export situation, accessibility to neighboring markets, and exchange rate loosening policy, the Yuan is likely to depreciate in the near future to facilitate exports. This will bring remarkable pressures on Vietnam's economy. On the one hand, Vietnam’s products face strong competition from Chinese alternatives in the U.S. and EU. On the other hand, cheap consumer goods from China have wider window to penetrate into Vietnam’s market.

Sluggish global trade whould also put pressure on the export activities of Vietnam, causing risks to the balance of payments and affecting economic growth in the long run. More importantly, China is more likely to boost export to neighboring Asian and the ASEAN countries, including Vietnam, particularly if exports to major trading partners like the U.S. and the EU are not favorable.

Thus, there are high probabilities of transmission of fiscal-induced risks through international trade channels from the developed countries like the U.S. and Europe to Asian developing countries, including Vietnam. This could directly impact on demand for imports in the developed countries; therefore, Vietnamese exporters should have appropriate strategy accordingly.

OVERVIEW OF VIETNAMESE ECONOMY IN 2013

2013 is characterized by effort to keep stability in macro level and attempt to get rid of stagnation at micro level. Indicators suggest that the economy has regained balance from high inflation shock in 2011 and the economic downturn in 2012. Stable macro environment is boosting economic activity, albeit slowly, along with structural adjustments. GDP growth reached 5.42%, inched up compared to 2012, while inflation continued to fall to its lowest level in many years, reaching 6.04%. Services and manufacturing led growth, contrast to the inertia of agriculture. The fragile recovery overshadowed confidence and restricted economic activities. Retail sales rose by 5.6%, while total social investment dropped to 30.4 % of GDP – both are the lowest figure in the last many years.

The root of the recovery, and the basic productive capacity of the economy, is not very solid when domestic firms were showing weaknesses and yet to find market. Demand for exports partially recovered, yet impacts on domestic sector was marginal. Investment, production, and trade of foreign-invested enterprises became more influential on the economy, demanding greater reforms to enhance the business environment towards higher transparency and fairness between economic sectors.

Besides severe budget deficit, other micro balances did not cause much stress on the money and capital markets. Economic policy in 2013 has managed to carry on in a tight policy space, constrained by high budget deficits and low credit demand. Therefore, the effects of economic stimulus measures from fiscal and monetary sides were insignificant. The main stock indices rose sharply due to the expectation of stronger capital inflow to the market in 2014. Real estate market witnessed changes in structure and trading activity heated up, mainly for end-users.

The economy experienced a year of destruction and renewal, along with financial deleverage, withdrawal of investment in non-core and refocus on core businesses. The key bottlenecks received superficial approach; while relying on market participants to restructure and adjust, the contents of the policy lacked confidence in the ability of the market and put more trust in administrative control. Last year's report emphasizes the importance of speeding up the implementation of policies to restructure the economy in 2013, but a feasible and clear solution has yet to appear to remove the constraints are binding economic growth.

Maintaining a stable macroeconomic climate is reasonable to restore the confidence of consumers and the business community, but that is not enough when there is a lack of measures that actually tackle foundation issues. Unfriendly and unimproved business environment has and will limit investment, prolong stagnation, obstruct the restructuring process, write-off bad debts and change growth model. Economic recovery was anemic and does not mean the current economic growth model is suitable, since policies are being aimed towards maintaining stability at all costs. Economic restructuring program needs to be implemented as schedule to ensure the opportunity for reform must not be missed once again.

DETERMINING VIETNAM'S BINDING CONSTRAINTS USING GROWTH DIAGNOSTICS APPROACH

Decreasing trend of economic growth and the impediments Vietnam has to facing in short- and medium-terms are clearly pointed out in recent studies. In the period 2001-2010, Vietnam gained high growth rate relatively to neighboring countries as well as global level. However, a large part of economic growth in Vietnam resulted from the accumulation factors, especially that the quality of growth is low which is reflected in low resource-use efficiency, unsustainable structure of economic growth, and low country competitiveness.

Chapter 3 presents a study applying growth diagnostic method for Vietnam economy. Growth diagnostic framework bases on a fundamental idea that although developing countries featured by similar weakness in many aspects such as infrastructure, human resource, energy shortage, and natural resource deficiency, each of them is constrained by different factors. Regarding to the context of limited resources, policy analysis should focus on seeking these constraints rather than attempting to solve all of weaknesses of the economy at the same time. This study applies the decision tree model developed by Hausmann-Rodrik-Velasco (2005) and a matrix framework of tests suggested by Hausmann – Klinger - Wagner (2008).

It found out that the binding growth constrains of Vietnam economy includes the business environment which increase the cost of doing business; underdeveloped level of infrastructure, especially the transportation network and that energy infrastructure could be a vital constraint in near future although it is a binding constraint at the moment; market failures related to information externalities, learning externalities and the coordination failures. Besides, the inefficiency of financial intermediates, over public investment level could become a bind constraint whenever the economy returns to its high growth path. Moreover, despite that there are limitations in the quality of human resource; it is not a binding constraint for Vietnam economic growth. The politic and social stability and the flexibility of labor market is the advantages of Vietnam comparing to other regional developing countries.

A FINANCIAL ASSESSMENT OF VIETNAM'S BANKING SYSTEM USING FINANCIAL SOUNDNESS INDICATORS

Vietnam's financial system has developed dramatically for the last two decades, from a mono-bank system consisting only the State Bank of Vietnam (SBV) to a two-tier banking system. There has been a substantial and sharp increase in the number of financial intermediaries since the reforms, including commercial banks and non-bank institutions. Nevertheless, Vietnam still demonstrates specific features of a bank-based financial system where banks are dominant players. The development of the banking system is not only illustrated by the growth in numbers, but also by the increases in financial capabilities and operations.

Despite rapid development, Vietnam's banking system is exposing many weaknesses in operations and managements, which cause high risks for the entire financial sector and threatening the macroeconomic stability. Thus, the evaluation of stability and financial soundness of the banking system plays an important role for policy-making in Vietnam. Many researchers and experts have analyzed and evaluated Vietnam's banking system based on different macroeconomic parameters. However, financial soundness indicators (FSIs), developed by IMF and have been applied in many countries, still have not received much interests in Vietnam. Thus, this paper is an attempt to calculate FSIs for Vietnam's commercial banks, after the global financial crisis in 2008, and to initially analyze the stability and financial soundness of the entire system.

Because of difficulties in collecting data and differences between Vietnam's and international accounting standards, we can only perform calculations of selected indicators for 35 banks. Since most Vietnamese banks have not publicly published their 2013 financial statements, the available data is only from 2008 to 2012. However, we cannot collect all those statements for this time horizon as some banks did not publicly disclose their reports in some years (e.g. Agribank's 2012 or SCB's 2011 financial statements). The calculation of FSIs is also more limited since some banks' financial statements are not incomplete and inconsistent.

The results show that the capital adequacy ratio was always higher the 8% minimum requirement of the Basel Committee, and even well above the 9% minimum requirement of the State Bank of Vietnam. However, the asset quality has not remained secure recently because of high nonperforming loans. Though the rise in nonperforming loans has somewhat slowed the profit growth, the indicators measure earnings and profitability were still satisfactory. Finally, A decrease in both the ratio of liquid assets to total assets and the ratio of liquid assets to short-term liabilities showed that Vietnamese banks has been facing liquidity problems.

INTERNATIONAL ECONOMIC INTEGRATION: BEHIND THE EXPECTATIONS OF VIETNAM

In this chapter, we profile the process of international economic integration of Vietnam so far and particularly emphasize the constraints that make Vietnam unable to maximize internal resources and improve the efficiency of integration as expected. We also reserve a large part of this chapter to discuss about the participation of Vietnam in Trans-Pacific Partnership Agreement (TPP) and the ASEAN Economic Community (AEC) - two prevailing concerns at present. Two processes are analyzed in order to find out the potential costs and long-term benefits, and then to draw some policy implications.

Nearly 20 years of international economic integration of Vietnam has shown the positive impacts on the market expansion and foreign investment attraction, however, expectations of maximizing internal resources utilising the integration process have not been realized. The benefits Vietnam obtained are largely "static" benefits of integration; the long-term and dynamic benefits are still unexploited. The internal constraints make market forces cannot be liberalized, domestic enterprises cannot efficiently participate in a global production chain, and foreign direct investment cannot have the spillover effects to domestic businesses. Obviously, all of these lead to the risk of a "trap of trade liberalization". In addition, unrealized expectations of institutional reforms in the country have created many skeptics about the subsequent integration process, particularly TPP.

For TPP, the most obvious benefit is that the free trade commitments in the TPP will help expand export market for Vietnamese goods, firstly for labor-intensive manufactured products. This stems from the fact that TPP is a large free trade area, with the participation of industrialized countries which have high trade complementarities with Vietnam. However, the strict regulations and requirements of rules of origin, intellectual property rights, labor, environment and other issues of TPP would be great difficulties for Vietnam; even they can suppress the benefits of market expansion and investment attraction.

For integration in ASEAN, AEC will create single market and production base in ASEAN, enabling member countries to improve comparative advantages and allocate resources effectively in the region. Due to the similarity of comparative advantage in the region, ASEAN countries tend to be competitive both in expanding their export markets and in attracting foreign investment. With the ability to create connectivity and the single market in the region, AEC will limit the competitive nature of the ASEAN economies, making them more complementary. However, most of Vietnamese enterprises are yet to recognize these long term benefits.

Based upon the analysis of the integration process, we strongly confirm that integration itself cannot provide immediate benefits for businesses and countries. Integration is also a process that could not be realized overnight. Therefore, the most important thing in international economic integration is still the improvement of domestic firms' capability. To support this process, there are three important issues that we would like to mention here.

Firstly, the government should play a supportive role in the process of improving the position of Vietnamese enterprises in the regional and global production chain. Instead of supporting specific sectors, the government should consider policies to support research and development, and design activities, in an effort to facilitate the added value for exports.

Secondly, there should be a comprehensive and unified view from government to business of the opportunities and challenges of economic integration. It is necessary to develop a coordination mechanism between business community and government so that businesses can participate prior to the negotiation process until the implementation of negotiated commitments. Government - businesses consultancy need to be specific to every tariff line and regulation, while ensuring adjustment time for Vietnamese enterprises.

Thirdly, the Free Trade Agreements of the new era does not only refer to the issue of tariff reduction, but also refer to profound issues related to rules, legislation, and institutional reforms in the country. So far, Vietnam is considered a country that seriously implemented its integration commitments, including the adjustment of laws and regulations in the country.

However, it is necessary to consider the quality of law enforcement because of the fact that the institutional reforms so far are not really effective and market forces have not been liberalized. Therefore, the opportunities of external liberalization can not be utilized, even become the constraints for the development of the internal forces.

VIETNAM'S CHOICES OF ENERGY POLICIES

The World is facing a twin-pronged assault of dwindling fossil fuels, and the negative effects of burning too many carbon-based fuels. The consequences of releasing more carbon dioxide and other greenhouse gases into the atmosphere would have a major social and economic impact on the whole of Vietnam; and especially the Red River and Mekong Deltas.

In many countries (including Vietnam) this challenge is compounded by inadequate investment in electricity generation and distribution networks. This is also complicated by the need to shift generation towards renewable fuels and to invest in smart grids, or at least grids capable of handling feed-in from a greater number and wider variety of sources.

Electricity demand is growing fast, as a result of rapid economic growth and rural electrification; this is resulting in increasingly disruptive power shortages and it is tempting to look at energy demand and production forecasts and predict a crisis on the horizon. Existing oil reserves are likely to become depleted by 2029 and coal reserves critically low by 2030. However, based on existing demand forecasts and planned investment in generation and transmission, electricity looks likely to become a national challenge by 2024.

Such increases in demand are causing a major shift in the electricity generation mix, with a decline in the reliance on hydro, which is nearing marginal returns for new larger projects. This is offset by an increase in reliance on coal, followed by significant investment in nuclear.

It is improbable that renewables (including nuclear) could be accelerated to entirely plug the energy gap, and increasing imports of coal and oil are amongst the few short-term options available, creating balance of payments challenges and environmental damage. Therefore, the chapter addresses long-term investment priorities and not the inevitable response and adaptation to energy shortages. Indeed, the chapter finds that allowing shortages to occur or responding by burning more fossil fuels will both curtail economic growth. Although alarming, this is a position that Vietnam shares with many of its neighbours (such as Indonesia) and even with some European countries.

Nevertheless, increased prices stimulate exploration and innovation and many predicted crises have been avoided in the past, as new energy sources and technologies shift our paradigms. Furthermore, electricity is somewhat price elastic and rising prices would lead to reduced demand and increased investment in energy saving technologies. However, it would be unwise to become complacent and fail to plan for the shortages and necessary long-term adaptations to alternative fuels.

This chapter utilises an internal rate of return model to compare Nuclear, Geothermal, Mini Hydro, Biomass (Anaerobic Digestion, Gasification), Solar and Wind energy. The outputs suggest that Geothermal and Anaerobic Digestion should be investigated further, but that all technologies have a part to play, even the relatively expensive wind and solar may be useful for supplying off-grid communities.

It concludes that some legislative reform is necessary to stimulate renewable energy in Vietnam. It also concludes that electricity costs must continue to rise if Vietnam is to avoid rapidly increasing its greenhouse gas emissions and a balance of payments challenge. Of course, there are also some economic disadvantages of increasing the cost of electricity.

To a large extent Vietnam is at a cross roads: should Vietnam liberalise markets further and allow electricity prices to rise to reflect the true costs, or is it possible to plan for and secure the necessary investment in renewables? Whichever strategy actually constrains economic growth the least is a largely academic exercise, dependent on the limitations of the model and costs captured within in. What is important is planning for the electricity shortages and sticking to a long-term energy policy.

VIETNAM’S ECONOMIC PROSPECTS 2014 AND POLICY IMPLICATION

In addition to medium-term policies that takesing into account policy implications suggested within each chapter of the Report, chapter 7 presents two forecasts on Vietnam’s macroeconomic prospects in 2013 and a comprehensive discussion on short-term policies adopted at the moment. Similar to last year, the policy space is broader in 2014 due to low inflation; however, issues of the real economy are the most alarming. Enterprises are withering, policy measures were insufficient, policy transmission channels were ineffective and distorting desirable outcome; those are the factors that keep obstructing the recovery of the economy. The tension emerged between Vietnam and China in South China Sea is threatening the economic relation of two countries. Vietnam heavily depends on China in terms of net imports of materials and fuels, construction equipment, machines and construction services of many energy and infrastructure projects, while it is the net exporter of agriculture products such as rubber, rice, fruits, etc; therefore, a worse relation between two countries will likely have an adverse impact on Vietnam's economy.

Both scenarios express that economic growth in 2014 is likely to decline from 5.42% of 2013 due to the impact of political – economic relation with China. The less optimistic scenario gives the forecast of economic growth at 4.15% while the other puts it at 4.88% (in 2010 prices). Inflation in 2014 is predicted to fall from 2013 level, stabilized in between 4.76% and 5.51%.

A number of mid-term and long-term issues arisen for Vietnam, including selecting between policies that prioritize growth recovery, enterprise revitalization and monetary policies for macroeconomic stabilization. Once again, macroeconomic stabilization is always the solid premise for other fundamental policies.

Since expected inflation might be less than 6%, along with banks' excess liquidity, the SBV can continue to press deposit rates to decline further. However, it should be careful not to disrupt the capital market when real deposit rates become negative.

Regarding real estates market, it is necessary not to lengthen the adjustment process by supporting packages or inpractical methods, creating false expectations on this market. The best method is to help the market to self-adjust its prices (fall).

Exchange rate policies should focus on not only short-term adjustment for the second half of the year (increase by 2-3%) but also a stable future in order to promote domestic production. After a period of tension with China, exchange rates should be adjusted since the favourable macroeconomic conditions are countable.

In terms of disposal of bad debts: it is necessary to create a market for trading debt instruments and a mechanism to allow domestic and international investors to enter the market.

THE CONSTRAINTS TO GROWTH

Regarding state-owned enterprises reform, it is crucial to keep privatizating SOEs in pursuant to the Prime Minister's speech in the beginning of the year to improve government's budget position and at the same time to restructure the economy.

Besides benefits from exports, policy makers should determine the risks associated with the development trends as Vietnam further integrates into the international commitments with higher degree of free trade (ACFTA, TPP, other FTAs). Institutional reforms and an improvement in business environment are keys to successful integration.

Given the expansion of current expenditure in government spending, Vietnam needs to streamline central and local personnels to control current budget expenditure.

Facing tensions with China, Vietnam needs to committedly change the economic model, economic development path and ideology in governing the economy. The economic slowdown gives a number of lessons, given the tension with China, the call for radical reforms and reducing dependency become clearer. In the same time, it is essential to identify economic and strategic partners such as Japan, Korea, Australia, India, and ASEAN in order to build the basis for long-term cooperation, reducing reliance on China.

It is necessary to boost the productivity of the economy in mid-term and long-term by committing to institutional reform towards market-based economy to create incentives to allocate resources more efficiently; actively direct the labor market to restructure towards higher quality, encouraging labor to improve skills.

Vietnam also needs to focus on the allocation of resources, creating mechanisms to boost investment in the agriculture sector. Especially, the marine economy needs to be supported directly (in repairing and supplying materials) to fisherman. Fishing ships should be supported in logistics by national vessels.

Good Policy, Sound Economy

Vietnam Annual Economic Report 2014

THE CONSTRAINTS TO GROWTH

Ha Noi, May 29th, 2014

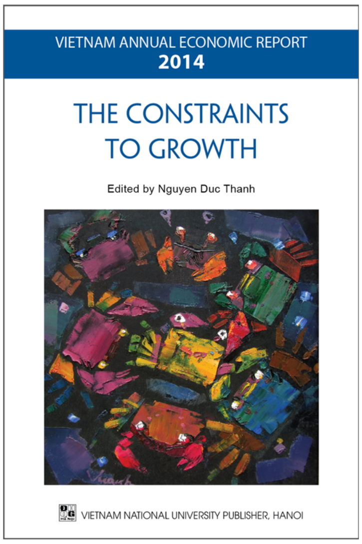
VEPR The Context of VAER 2014

❑ 2013 witnessed initial implementation of a few reform measures after years of delay due to decreasing economic growth, elevated macro instabilities, and falling productivity of the economy.

❑New Year Message of PM Nguyen Tan Dung expressed the dedication and desire of the Government to commit in strong reforms; however, the effectiveness of execution is still in doubt.

❑ China's infringement of national sovereignty in Vietnam's East Sea led Vietnam to reconsider growth model and its strategy of regional and international cooperation.

❑Troubles in international and domestic environment raise questions about the perseverance of the economy, thus, it is necessary to identify the constraints to growth so that reforms would be in the right direction.



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Chapter 1: Overview of The World Economy in 2013

Le Kim Sa, Ph.D.
Nguyen Cam Nhung, Ph.D.

Good Policy, Sound Economy

VEPR Main Contents

- Global economic growth remained low
- Global unemployment remained at high level
- Sluggish international trade continued
- Little progress on trade agreements
- Global capital flows increased slightly
- Stable input prices
- Expansionary monetary policies and discretionary fiscal policies in selected major economies.
- Prospects for 2014 and beyond
- Implications for Vietnam

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Global economic growth remained low

- Global growth remained at a low rate, even lower than those in 2011 and 2012. The forecasts from IMF and World Bank were also adjusted (IMF, 2014) and (WB, 2014).
- "Lack of motivation" from major economies. Selected countries and regions' economic growth trends show different directions.

% GDP	IMF			WB		
	2011	2012	2013	2011	2012	2013
World	3.9	3.2	3.0	3.0	2.5	2.4
Developed Economies	1.7	1.4	1.3	1.8	1.5	1.3
United States	1.8	2.8	1.9	1.8	2.8	1.8
Japan	-0.6	1.4	1.5	-0.6	2.0	1.7
EU	1.7	-0.7	-0.5	1.6	-0.6	-0.4
Germany	3.4	0.9	0.5	3.3	0.7	-
France	2.0	0.0	0.3	2.0	0.0	-
Spain	0.1	-1.6	-1.2	0.1	-1.6	-
Italy	0.4	-2.4	-1.9	0.5	-2.0	-
Developing Economies	6.2	5.0	4.7	6.1	4.8	4.8
China	9.3	7.7	7.7	9.3	7.7	7.7
India	6.3	4.7	4.4	6.2	5.0	4.8
ASEAN-5	4.5	6.2	5.2	-	-	-
Russia	4.3	3.4	1.3	4.3	3.4	-
Brazil	2.7	1.0	2.3	2.7	0.9	2.2

Source: IMF(2013, 2014), WB (2014).
Note: ASEAN-5 includes Indonesia, Malaysia, Philippines, Thailand, and Vietnam

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Global economic growth remained low

- EU: austerity has prolonged for the past three consecutive years, leading to an expected growth decline. GDP growth remained negative (-0.5%).
- US: the "fiscal cliff" program improved the U.S. budget balance. Nevertheless, GDP growth was only 1.9%.
- Japan: "Abenomics" policies have initial effects in the first year. The sharp devaluation of the yen has promoted exports dramatically. 2013 GDP growth was 1.5%, only 0.1% higher than that of 2012.

Global economic growth remained low

- China: economic growth reached 7.7%, which is consistent with previous expectations of China's new development model
- ASEAN: economic growth reached 5.1%, lower than in 2012. The lowest growth rate was that of Thailand, because of this country's political crisis, negatively affecting domestic demand and consumer confidence index.

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Global unemployment remained at high level

- Since global growth and aggregate demand remained at a low level, there were total 202 million unemployed people, increased by 5 million compared to 2012 (ILO, 2014).
- Youth unemployment continued to put pressure on medium-term human capital in developed economies.
- Global unemployment rate was predicted to increase due to the world economy's uncertainty and the Ukraine's crisis.

World labor market status (2010-2013)

	2010	2011	2012	2013	2014*
Labor force participation rate (%)	63.4	63.4	63.4	63.5	-
Job growth (%)	1.2	1.4	1.4	1.3	-
Unemployment rate (%)					
Global unemployment	6.1	6.0	6.0	6.0	6.1
Youth unemployment rate	12.9	12.7	12.9	13.1	13.2
The number of unemployed (million people)					
Total of global unemployment	195.2	193.9	196.9	201.8	206.7
Total of youth global unemployment	74.9	73.5	73.8	74.5	74.5

Source: ILO (2014)

VEPR Global unemployment remained at high level

- EU unemployment rate reached 12%, the highest level in the history.
- The unemployment rate in the U.S. in 12/2013 dropped to the lowest level of 6.7% for the last 5 years, bringing the 2013 unemployment rate to 7.5%.
- In 2013, the non-agricultural area created only 74,000 jobs - the lowest level since 1st May 2011 and much lower than the monthly amount of jobs created by the U.S. in recent years (about 200,000).

Unemployment rate in OECD and selected major economies (2010-2013) (%)

	2010	2011	2012	2013	2014*
OECD	8.3	8	8	7.8	7.5
US	9.6	8.9	8.1	7.5	6.9
EU	10	10.1	11.3	12	12.1
Japan	5	4.6	4.3	4	3.9

Source: OECD (2014)

Good Policy, Sound Economy

VEPR Sluggish international trade continued

- 2013 international growth rate was 3%, slightly higher than the 2012 rate of 2.8%, less than half of the 2011 rate and less than a quarter of the 2010 rate.
- Trade continued to stagnate because of i) weak aggregate demand in major economies, and ii) decreasing commodity prices, a result of "cheap Chinese products".

Trade growth on world goods and services, 2010-2013 (%)

	2010	2011	2012	2013	2014*
Volume of world goods and services	12.8	6.2	2.8	3	4.3
Export					
Developed countries	12.4	5.7	2.1	2.3	4.2
Developing countries	14.0	6.8	4.2	4.4	5
Import					
Developed countries	13.5	5.2	1.5	1.2	3.2
Developing countries	14.9	10	5.4	5.3	5.2

Source: IMF (2014)

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Sluggish international trade continued

- Trade deficits were narrowing in high-deficit countries like the US, while surpluses were decreasing in high-surplus countries like China, Japan and oil-exporting countries.
- Changes in consumer preferences for luxury goods in China could make import increase but trade surplus decrease.

The current account in the BOP, 2010-2013

	2010	2011	2012	2013	2014*
% GDP					
World	0.5	0.5	0.5	0.5	0.6
USA	-3	-2.9	-2.7	-2.3	-2.2
Japan	3.7	2	1	0.7	1.2
EU	0.6	0.8	2	2.9	2.9
China	4.0	1.9	2.3	2.1	2.2
Oil-exporting countries	7.1	11.5	10.4	7.4	6.7
USD Billion					
World	305	371	342	403	487
USA	-450	-458	-440	-379	-391
Japan	204	119	60	34	57
EU	73	109	246	366	392
China	130	136	193	208	152
Oil-exporting countries	319	636	608	445	414

Source: IMF (2014)

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Little progress on trade negotiations

- Although the success of the 9th WTO Ministerial Conference held in Bali, Indonesia in Dec 2013 restored confidence in the WTO, the results were still limited in agriculture and trade. There are still too many unresolved issues to finish the Doha Round.
- The boom in bilateral or sub-regional FTAs has stopped. The world is now focusing on two regional trade agreements:

  + TTIP - the largest-ever bilateral trade agreement between EU and the U.S; and

  + TPP – the 3rd generation free trade agreements, which is expected to replace the Doha Round.

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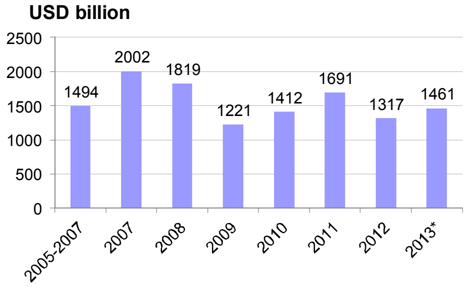
VEPR Global capital flows increased slightly

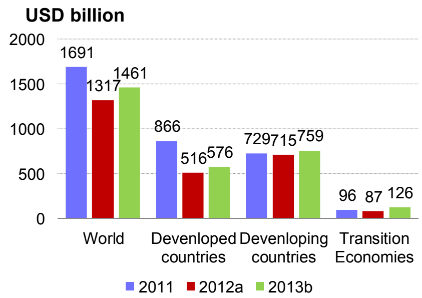
- 2013 global FDI inflows (2013) rose by 11% to USD 1.46 trillion, nearly equal the 2005-2007 average growth.
- FDI inflows to developed economies grew by 12% to USD 576 billion. FDI inflows to developing countries reached a new peak of USD 759 billion, accounting for 52% of global FDI. Transition economies experienced a significant 45% rise in FDI inflows to USD 126 billion.

Annual global capital inflows, 2007-2013



Source: UNCTAD, 2014

FDI inflows by region, 2011-2013



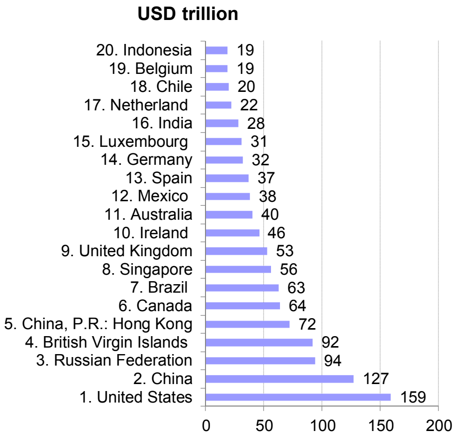
Source: UNCTAD, 2014

Good Policy, Sound Economy

VEPR Global capital flows increased slightly

- Despite a decline in 2013, FDI inflows in the U.S. was still the highest. FDI inflows in China also increased.
- Equity investment flows to India and South Korea, and non-bank credit flows to Indonesia fell significantly.
- Cross-country M&A transactions rose by 5% while green-field investment (GI) remained unchanged since 2012.
- The number of M&A transactions in developing countries returned to the pre-crisis level.

FDI inflows: top 20 host economies, 2013



Source: UNCTAD, 2014.

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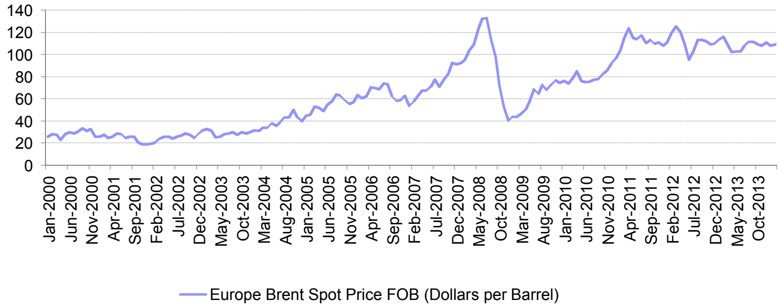
Stable Oil Price

- Oil price fell slightly in the first half of 2013 due to the low demand. However, in quarter III/2013, political unrest with concerns about tightening supplies made oil price increase slightly again.

The World Brent Crude Oil Spot Price Fluctuations, 1/2000 – 2/2014



Source: IEA

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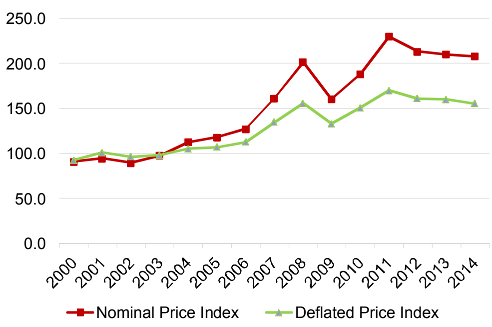
Food Prices

- Global food prices fell by 1.6% in 2013, but was still at 209.9 points on average, the third highest level in the history.
- Prices of grains (except rice), oil seeds and sugar decreased due to abundant supply, while prices of milk and meat products increased.

FAO Food Price Index



Source: FAO 2014

VEPR Pursuing QE

- The US maintained QE3 throughout 2013 and only cut down in December 2013 from USD 85 billion per month to USD 75 billion per month when the labor market signaled some improvement.
- ECB: Basic interest rate was cut down from 0.75% to 0.5% (5/2013) and to 0.25% (11/2013). ECB deposit interest rate remained at 0% to encourage lending and spending activities.
- BOJ: increased the money supply by yen 60,000-70,000 billion/year (which was equivalent to USD 683 billion/year). Expansionary monetary policy in Japan was expected to have a significant positive impact on improving employment and income (IMF, 2014).
- China: prudent monetary policy. In Feb 2013, People's Bank of China injected nearly USD 2.8 billion into the financial system to support domestic banks and other sectors. The asset securitization pilot program continued to be expanded.

VEPR Discretionary Fiscal Policy

- Global budget deficit fell from 4.4% (2012) to 3.8% (2013). Budget deficit in most countries still remained at high level.
- Japan: budget deficit has declined continuously since 2009 but remained high at 8.4% of GDP in 2013, the highest level among developed countries.
- US: budget deficit was 7.3% of GDP in 2013, the second highest level among developed countries.

Budget deficit in some main countries, 2008–2013

	2008	2009	2010	2011	2012	2013
Budget deficit (% GDP)						
World	-2.5	-7.8	-6.3	-4.8	-4.4	-3.8
EU	-2.1	-6.4	-6.2	-4.2	-3.7	-3.0
France	-3.3	-7.6	-7.1	-5.3	-4.8	-4.2
Spain	–4.5	–11.1	–9.6	–9.6	–10.6	–7.2
Germany	-0.1	-3.1	-4.2	-0.8	-0.1	0.0
Italy	–2.7	–5.4	–4.4	–3.7	–2.9	–3.0
Greece	-9.9	-15.6	-10.8	-9.6	-6.3	-2.6
UK	-5.0	-11.3	-10.0	-7.8	-8.0	-5.8
Japan	-4.1	-10.4	-9.3	-9.8	-8.7	-8.4
USA	-7.8	-14.7	-12.5	-11.0	-9.7	-7.3
China	-0.7	-3.1	-1.5	-1.3	-2.2	-1.9
India	-10.0	-9.8	-8.4	-8.0	-7.4	-7.3

Source: IMF (4/2014)

VEPR Discretionary Fiscal Policy

- Japan: for fiscal stabilization and reducing government debt, Japan cut down government expenditure by USD 83 billion, which was equivalent to over 4% of Japan's annual expenditure.
- The US: cut down USD 85 billion in 2013 fiscal revenue, and stopped tax exemptions.
- China: 2013 budget deficit was Yuan 1.35 trillion because of tax cuts and rising public expenditure. China's local public debt was not included in the Table.

Government Debt Status in some countries, 2008–2013

	2008	2009	2010	2011	2012	2013
Government Debt (% GDP)						
World	64.9	74.9	78.6	79.0	80.6	78.6
EU	70.3	80.1	85.7	88.1	92.8	95.2
France	68.2	79.2	82.4	85.8	90.2	93.9
Spain	40.2	54.0	61.7	70.5	85.9	93.9
Germany	66.8	74.5	82.5	80.0	81.0	78.1
Italy	106.1	116.4	119.3	120.7	127.0	132.5
Greece	112.9	129.7	148.3	170.3	157.2	173.8
UK	51.9	67.1	78.5	84.3	88.6	90.1
Japan	191.8	210.2	216	229.8	237.3	243.2
USA	72.8	86.1	94.8	99.0	102.4	104.5
China	17.0	17.7	33.5	28.7	26.1	22.4
India	74.5	72.5	67.5	66.8	66.6	66.7

Source: Public Expenditure Reform, Fiscal Monitor, IMF (4/2014)

VEPR Discretionary Fiscal Policy

- EU: Instead of reducing budget expenditure or raising taxes, some countries started to focus on economic growth and job creation

  - France: gradually stopped the tightening fiscal policies to promote growth and job creation.

  - Italy: approved a stimulus package of around EUR 3 billion to support public projects (6/2013), reduced EUR 550 million in household energy costs.

  - Spain: announced a budget package of EUR 3.5 billion (approximately USD 4.6 billion) to 2016 with 100 job creation measures, and carried out a new reform program in the next 3 years focusing primarily on pensions, employment and the banking sector.

VEPR Prospects for 2014 and beyond

- The world economy in 2014 contains many uncertainties because of difficult political conditions such as the crisis in Ukraine, China's reforms and the visit of the US President Barack Obama to 4 Asian countries. Conflicts between major countries will certainly affect developing countries in Asia.
- Global monetary policies in 2014 will be more diversified. QE3 will probably end smoothly, but it can cause negative consequences for financial markets. The central banks of New Zealand and India increased basic interest rates, while the ECB and BOJ continued to pursue their monetary easing solutions in order to prevent deflation.

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VEPR Prospects for 2014 and beyond

- International trade should improve thanks to a rise in Europe's aggregate demand, East Asia's regional trade will be dynamic again. TTIP and TPP agreements are expected to end in 2014, and promote international trade. Predictions of export-import growth will be 4.6% in 2014 and 5.1% in 2015 (IMF, 2014 and World Bank, 2014).
- Commodity prices may fluctuate. Food prices may fall thanks to better harvesting. Basic metal prices will decrease because of a decrease in demand and an increase in supply. Oil prices will be affected by different geopolitical issues.
- Global FDI is expected to increase slightly to USD 1,600 billion in 2014. Net foreign portfolio capital inflows to developing countries is expected to rise sharply again, by 22% compared to 2013, reaching USD 87.8 billion (UNCTAD, 2014).

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VEPR Prospects for 2014 and beyond

- Global economy growth is expected to increase slightly in 2014 thanks to better international trade and higher global capital flows.
- Given that Ukraine crisis will not be worse, the global economy in 2014 is predicted to grow by 3.6% (IMF, 2014) and 3.2% (World Bank, 2014).

World Economic Growth Forecast 2014

% GDP	IMF	WB	UN	ADB	HSBC
World	3.6	3.2	3.0	-	2.6
Developed economies	2.2	2.2	1.9	-	1.8
USA	2.8	2.8	2.5	2.8	2.5
Japan	1.4	1.4	1.5	1.3	1.3
EU	1.2	1.1	1.4	1.0	0.8
Developing countries	4.9	5.3	5.1	-	4.9
China	7.5	7.7	7.5	7.5	7.4
India	5.4	6.2	5.3	5.5	5.0
ASEAN-5	4.9	-	-	-	-
Russia	1.3	-	2.9	-	2.0
Brazil	1.8	2.4	3.0	-	2.2

Source: IMF (4/2014), WB (1/2014), UN (2014), ADB (4/2014), HSBC (2014).

VEPR Implications for Vietnam

- The U.S. could stop QE3 and use interest rate as a monetary policy instrument. This will cause a certain pressure on many countries' exchange rates, including Vietnam.
- China loosened the exchange rate control from 1% to 2% in early 2014. The Yuan is likely to continue to depreciate in the near future to promote exports. This will create remarkable pressure on Vietnam's economy. On the one hand, Vietnam's products will have to compete with Chinese products in the U.S. and EU. On the other hand, cheap Chinese products will have better opportunities to penetrate into Vietnam market.

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Implications for Vietnam

- Demand for imported goods in developed countries like the US and EU might decrease because of their fiscal policies. Thus Vietnamese exporting enterprises should have suitable strategies for market development.
- If the developed country group grow better in 2014, the global M&A will gradually increase again and will be made between TNCs of the developed country group and the emerging economy group. Thus, Vietnam's investment environment will need to improve to compete with other ASEAN countries.

Good Policy, Sound Economy

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Chapter 2: Overview of the Vietnamese Economy in 2013

Nguyen Duc Thanh, PhD.
Ngo Quoc Thai

VEPR

Main Contents

1. Overview (growth and inflation)
2. Components of Aggregate Supply
3. Components of Aggregate Demand
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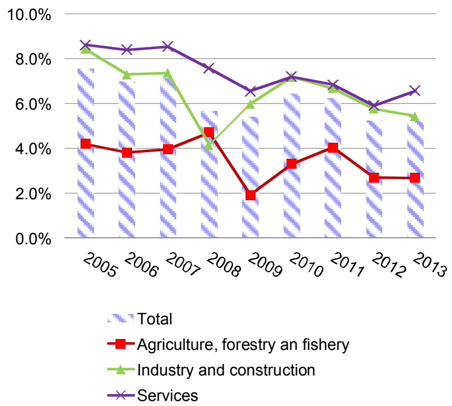
5. Capital Market and Money Market
6. Property Market
7. Macroeconomic Policies

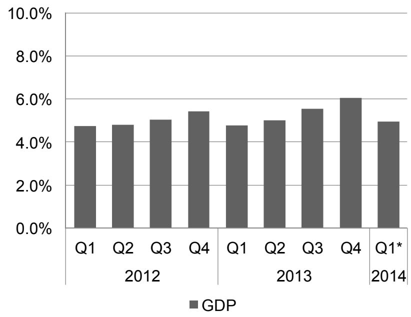
Good Policy, Sound Economy

VEPR

I. OVERVIEW

Economic Growth





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Economic Growth

- Double-dip slowdown: GDP growth rate declined in 2008 and 2009, rose in 2010, and declined again in 2011 and 2012.
- Economic growth was not easy to recover because of static expectation; after the first slowdown, the health of Vietnamese economy was worse off.
- 2013 and 2014Q1: fragile recovery, relatively weak if any.
- Divergence: services and industry: 5.5-6.5%, agriculture: 2.7%.
- Industrial production: manufacturing 7.4% vs. mining -0.2%.
- Business cycle: growth seems to be on long-term trend, potentially a mini-boom in short term.
- Favorable factors can consolidate its upward trend in 2014, but the risks still remain and have not been controlled.

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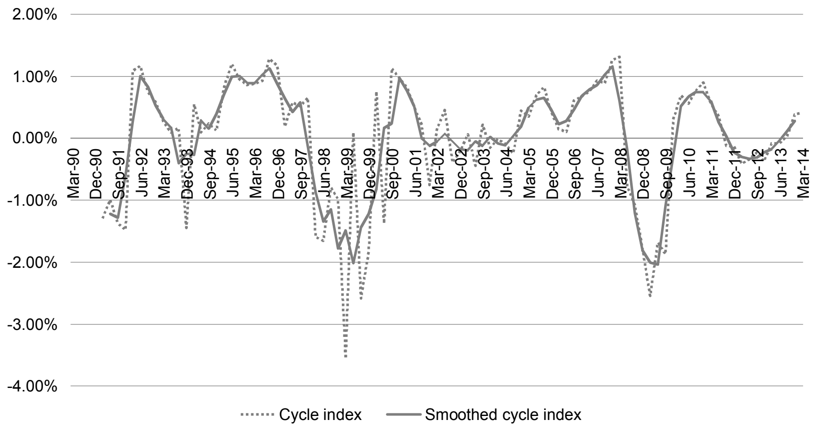
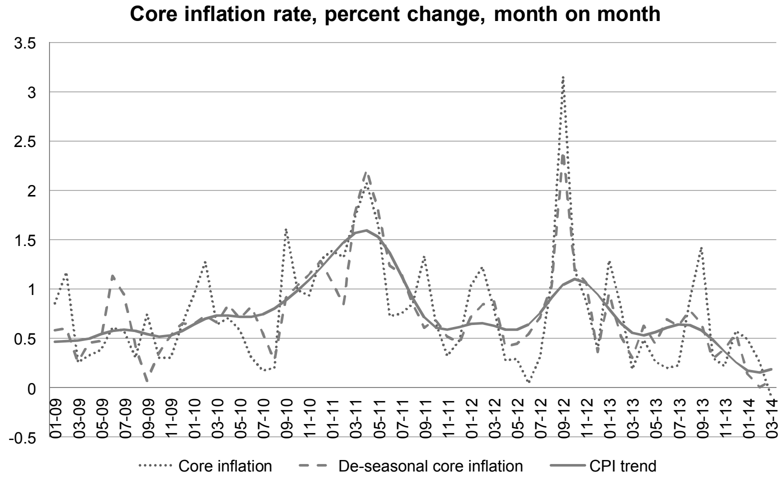
VEPR Growth trend

VEPR Economic cycles



VEPR Inflation



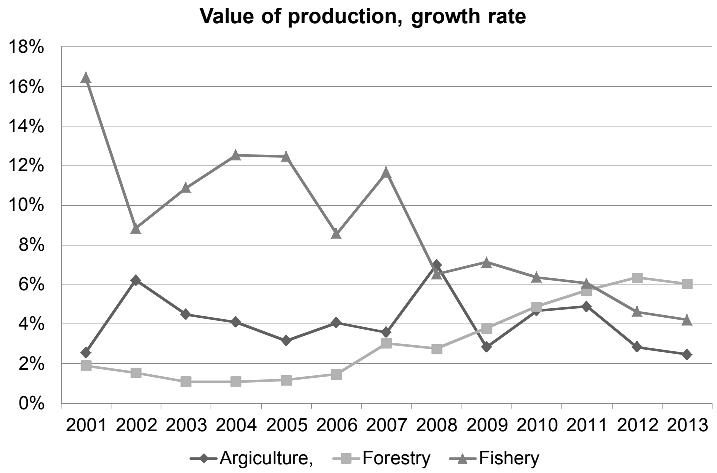
VEPR Inflation

- The lowest average annual inflation in the last 4 years.
- The downward trend was interrupted by prices adjusments in health and education, which accounted for 50% of the annual CPI increase.
- The price of necessity goods including electricity, fuels, and food rose.
- Core inflation: showed weak aggregate demand; went on a downward spiral in 2013, recorded 0% in Lunar New Year 2014.
- Inflation by GDP deflator: lower inflation (4.76%) showed a stronger indicator of economic downturn. CPI was strongly distorted by price adjustments of public services.
- Adjusments helped reduce the pressure on budget; however, mechanism distorting price signal still exists, latent risks of fixing market defects caused by price controls.

VEPR II. Aggregate Supply

- **Agriculture, forestry and fishery**
- **Industry and Construction**
  - Consumption and inventory
  - Vietnam PMI
- **Services**

VEPR Agriculture, forestry and fishery

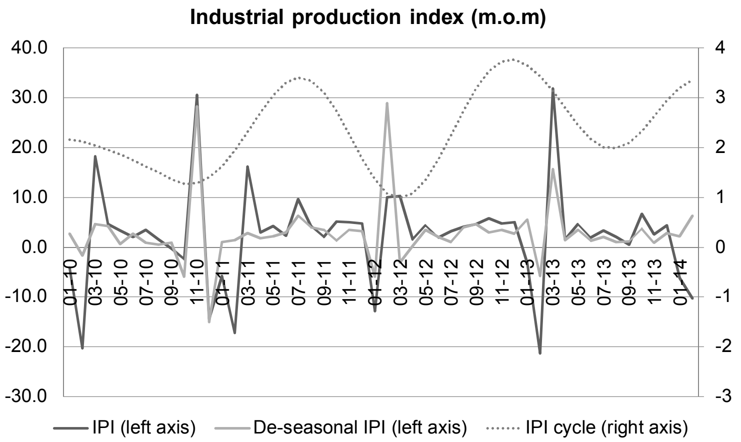


Source: GSO

VEPR Agriculture

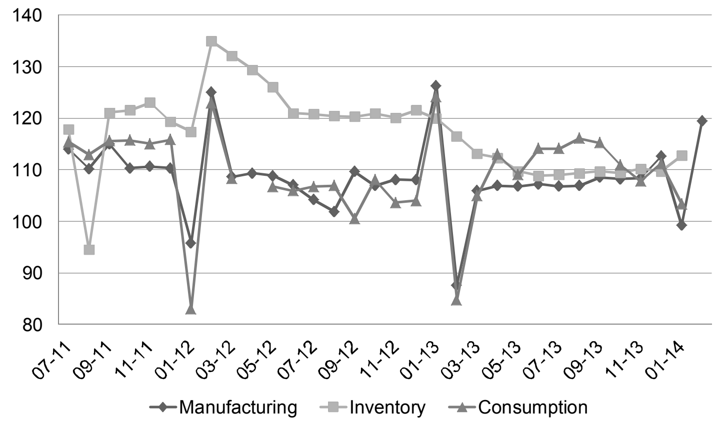
- Agricultural production momentum become exhausted, structural adjustment was witnessed, though the sustainability is in doubt.
- Heavily rely on natural conditions and chemicals, rice production is vulnerable.
- **Rising competition from Thailand, Myanmar; major rice buyers attempted to grow rice to ensure food security.**
- **State monopoly on the export and temporary rice storage revealed ineffectiveness.**
- Experience from large-scale rice farming: high potential, but too early to apply country-wide.
- Small-scale breeding was decreasing due to inefficiency, facing the growing competition from big and foreign corporations.
- Forestry showed high potential for sustainable development.

VEPR Industry



Source: GSO and author's calculation

VEPR Shipment and Inventory Index



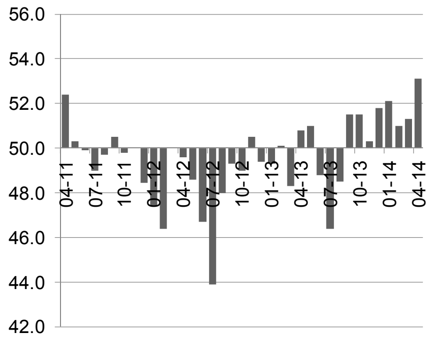
Source: GSO

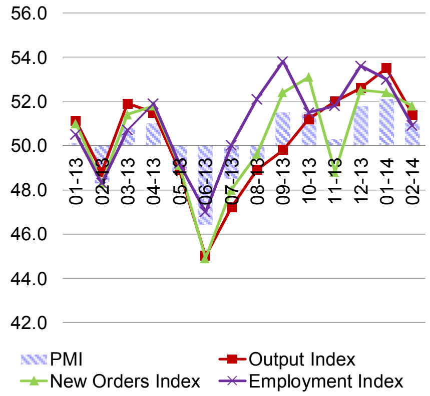
VEPR Industry

- The whole industry has not gained much momentum compared to 2010 - 2012 period, a strong rebound in manufacturing.
- De-seasonal IPI: production continued to expand, but slower than 2011 and 2012. **The upward trend since Q3 is a positive signal, strengthened the foundation of economic recovery.**
- The electricity consumption growth reduced because i) the decline of heavy industry and the increase of manufacturing industry and ii) the slowdown of urbanization.
- The number of employees in foreign-invested enterprises increased the most rapidly among enterprises, though maybe just seasonal/short-term employment.
- Reduced pressure from inventory thanks to sharp recover in shipment.
- IPI is **consistent** with changes in PMI: output index and orders index went up since Q3, but still weaker compared to 2012.
- The input prices continuously increased=> possibility of transfer pricing at FDI enterprises.

VEPR Vietnam Manufacturing PMI

As of April 2014, PMI has increased for 8 months in a row; if this trend remains unchanged till July, the recovery will have stronger ground.





Source: HSBC – Markit

VEPR Services

- Diverged in growth rate due to prolonged difficulties.
- Real estate trading rose modestly.
- Transportation and storage (+5.59%) and retail sales (+6.52%) resulted from anemic economic activities.
- Silver lining: accommodation and catering services (+9.91%) and information and communication (+8.82%).
- Retail sales was low (+5.6%) as real income barely increased.

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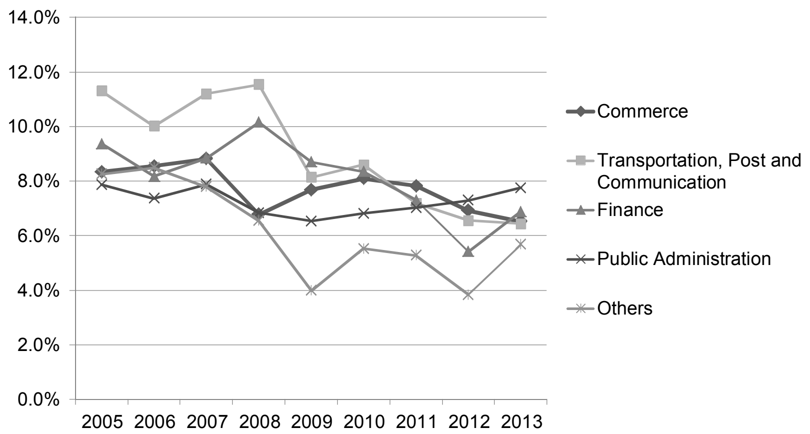
Retail sales, nominal change



Source: GSO

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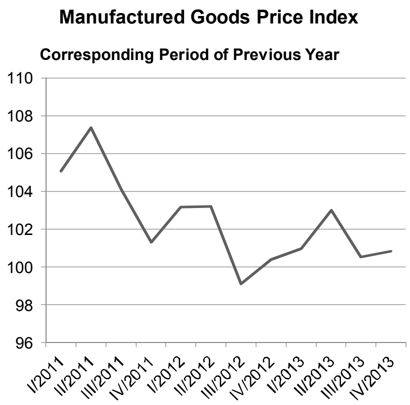
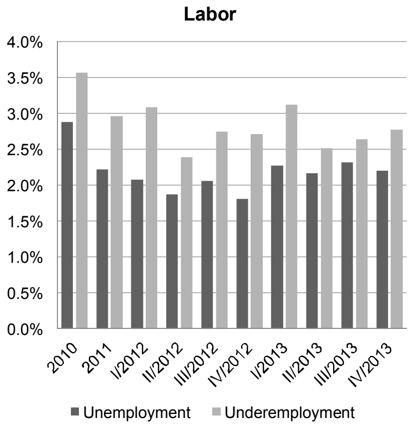
Factor markets

- Input prices rose significantly, mainly in natural resources, such as mining (+9.6%) and water (8.4%).
- Output prices of manufactured products increased slowly (3.4%) compared to mining (6.7%), electricity (9.2%), and water (7.2%).
- The unemployment rate went up (2,2%), 3.58% in urban vs. 1.58% in rural areas.
- Official labor market became more competitive, unofficial labor market expanded: from 34.6% (2010) to 35.8% (2011) and 36.6% (2012); estimated 2013: 33.4%, urban areas reached nearly 50%.

VEPR Factors Market





Source: Ministry of Industry and Trade, GSO

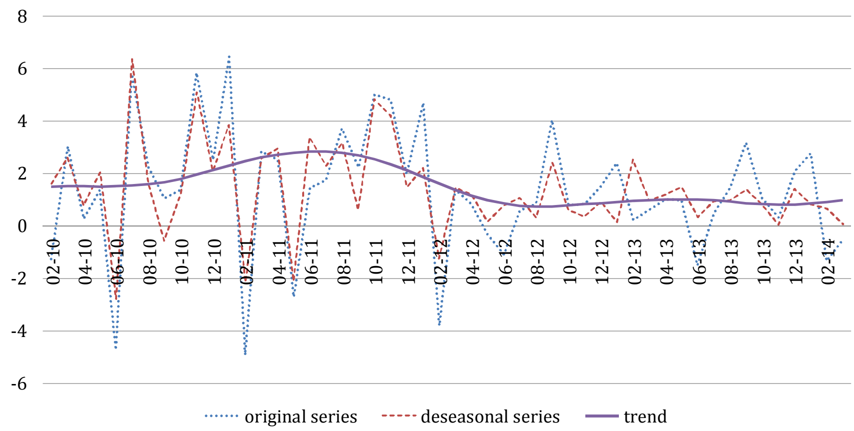
VEPR III. Aggregate Demand

- **Government expenditure**
- **Total social investment**
  - Foreign Direct investment
- **Final Consumption expenditure**
- **Net export**
  - Export volume
  - Import volume

VEPR Final Consumption

- Percentage of consumption in GDP: Final Consumption increased slowly, the proportion of GDP used for this expenditure decreased.
- A tendency to give priority to saving and cut spending.
- Nielsen: The consumer confidence index increased to 98 points at the end of 2013 from 87 points in quarter III/2012, forecast a return to upward trend in expenditure.
- The growth of expenditure was not clear despite the supporting low inflation.

VEPR Retail Sales Growth



Source: MIT and author’s calculation, deseasonal using x13

VEPR Government expenditure

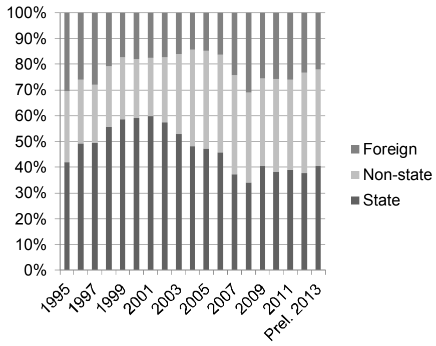
- Current expenditure accounted for 78%.
- Expenditure on defense, security witnessed the highest increase (over 13%), followed by special expenditure, education and training, economic entities.
- Because of the adjusted minimum wage and the increase in the number of employees (the number of officials increased by more than 25%, the number of civil servant increased by 15%).

Good Policy, Sound Economy

VEPR Investment

- Cooled down: total social investment accounted for 30.4% GDP.
- From 2009, State sector made up almost 40%, FDI sector decreased to 22%.
- Investment of state sector at constant price did not change, restructuring of public investment just to deal with unreasonable capital financing, no progress in the allocation and management mechanism.

Total social investment by ownership

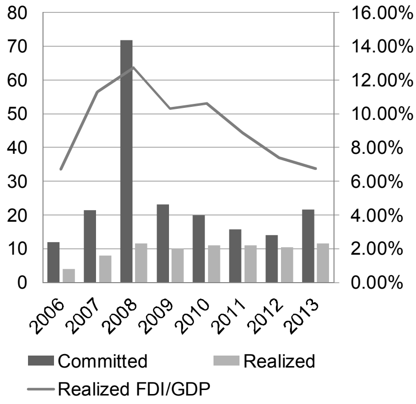


Source: MPI

VEPR Foreign Direct Investment (FDI)

- More confident: committed FDI rose to 40% compared to 2012; 70% into manufacturing.
- Realized FDI/GDP decreased to 6.7%.
- Ease of Doing Business index did not improve (ranked 99th).
- Tax incentives and investment procedures applied case-by-case, macro environment quickly stablized
- Vietnam's competitive index ranked 70, jumped by 5 places thanks to macro stability.
- M&A projects to penerate market: finance, consumer, construction, materials.

FDI, VND billion and % of GDP



Source: MPI

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VEPR Net Exports

- Trade flourished thanks to foreign-invested enterprises, which accounted for 61% of export volume and 56% of import volume and grew by 25% compared to 3.5% of domestic enterprises.
- The share of electronic goods and phone in total exports increased from 4.4% in 2008 to 24% in 2013, exceeding agricultural products since 2012.
- Export of manufacturing products led to corresponding increase in import of parts and components, mainly from China and Korea.
- Domestic supporting industries and technology transfer were limited.
- Export volume of coal, crude oil decreased significantly; agricultural products such as coffee, rice, manioc witnessed decreases in both prices and quantities.
- Import of petroleum declined by 20% showed the economy was still weak.
- Balance of trade: Domestic enterprises logged a net imports of $6.48 billion (petroleum included).

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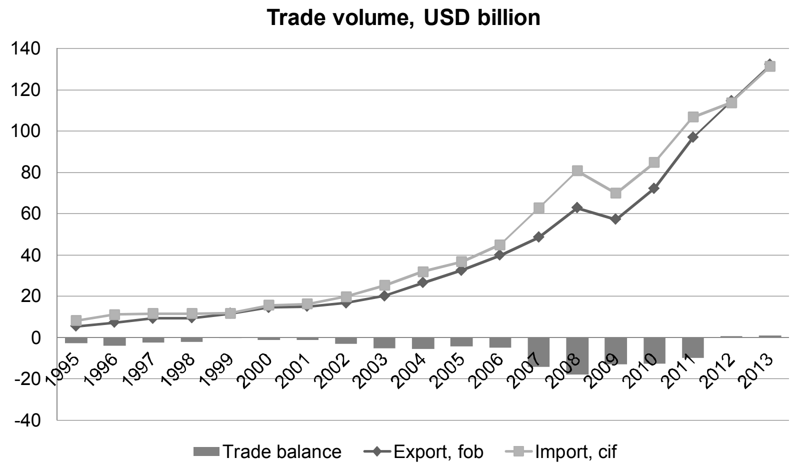
VEPR Trade



Source: GSO

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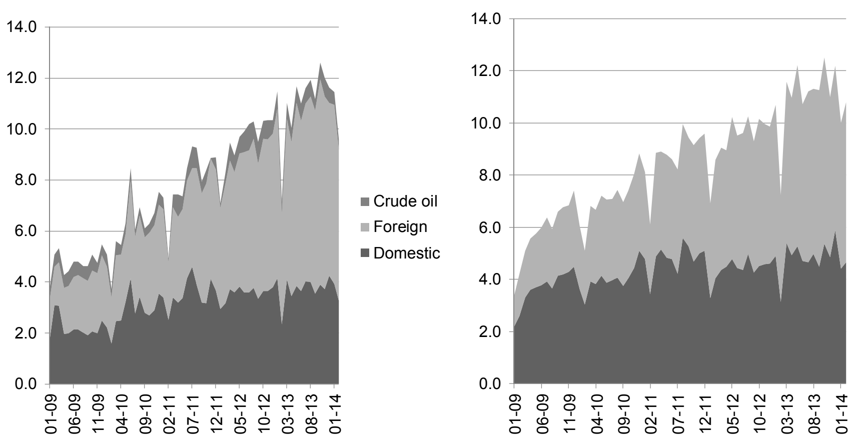
VEPR Export and Import, billion USD



Source: GSO

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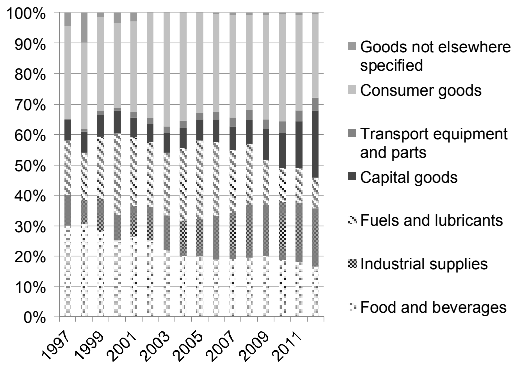
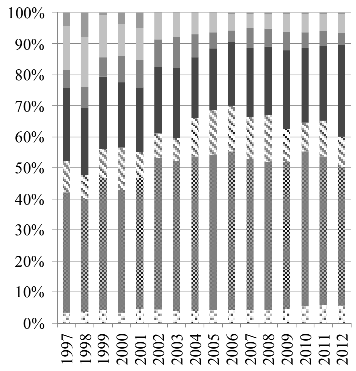
VEPR Structure of exports and imports

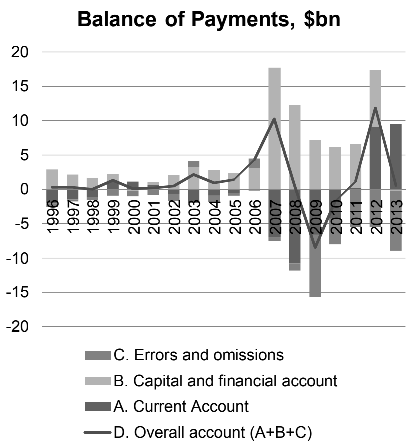




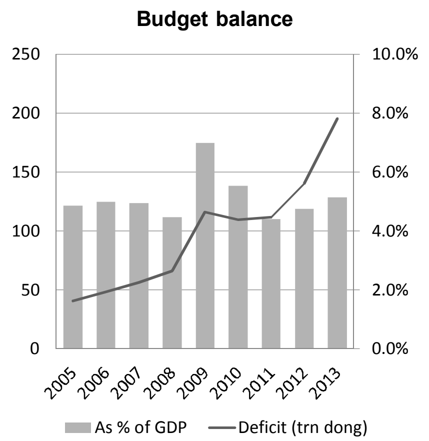
Source: UN Comtrade

Good Policy, Sound Economy

VEPR IV. Macroeconomic balances



Source: IFS (IMF), SBV



Source: Author's calculation from MOF's data

VEPR Balance of Payments

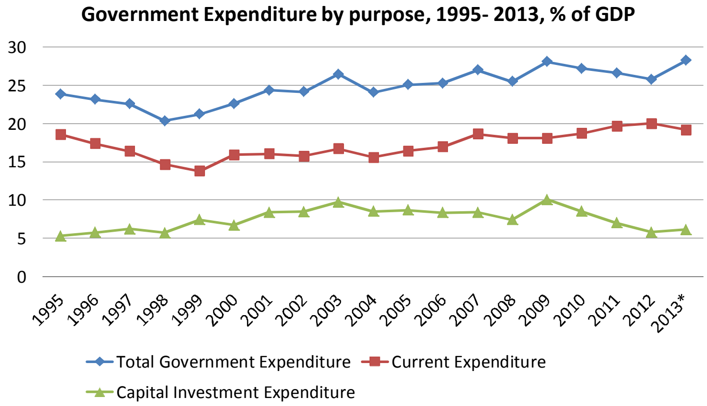
- Current account: remittances nearly 10.65 bilion USD, trade account balanced, current account surplus estimated at 5.2%-5.6% GDP.
- Capital and finance: supported by FDI, effected by the sudden surge in outflows in late 2013Q2.
- Cheap money did not flow into the domestic financial market, Vietnam did not fall into the vicious circle of financial instability.
- State Bank of Vietnam purchased USD for reserves, at the end of 2013: $ 30 billion equivalent to 12 weeks of imports.

VEPR Budget balance

- Deficit 190,200 billion Vietnam dong, equal to 5.15% of GDP.
- Tax revenues declined due to business difficulties and bankruptcy => raised tax collection at the end of the year (retained earnings from State corporations, companies, interests from oil and gas exploitation).
- Expenditure did not decrease correspondingly, raised risks to the capital markets and hamper confidence in financial institutions.
- Public debt: 56.2% of GDP (2011: 54.9%, 2012: 55.7%) excluding the foreign debts of SOEs.
- Foreign debt decreased to 39.5% of GDP.

Source: MOF

VEPR Structure of Expenditures

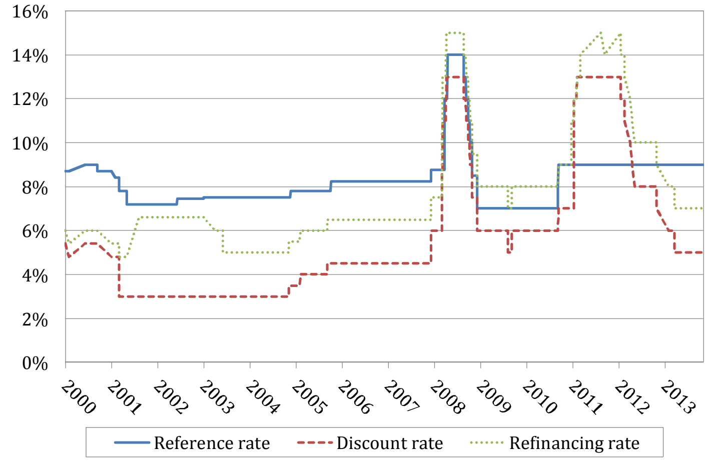


Source: ADB (2013)
**2013*: Author's calculation from MOF's data

VEPR Capital Market

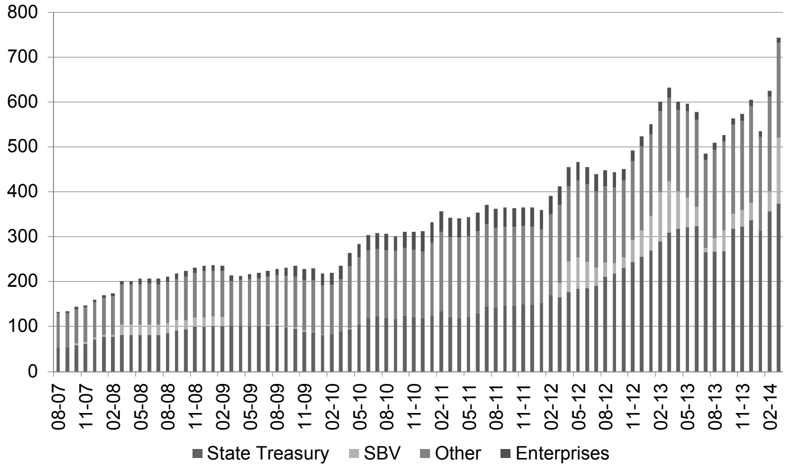
- Interest rate kept falling, abeit slower, but term deposit increased.
- Haunted by inflation => real interest rates is kept positive.
- Banks has plentiful capital but credit rose slowly because of low credit demand (many businesses dissolved , real estate market has not rebounded).
- Deleveraging: credit-deposit ratio decreased to 85%.
- Commercial banks purchased bonds and State bank bills to release the capital, offered interest rate fell.
- Large volume of bonds to compensate the budget deficits (+13.6%).
- Non-performing loan ratio was not under 7.92% (in balance sheet/official: 4.73%, outside balance sheet : 3.19%).
- State bank claimed NPL ratio at 9% vs. Moody's 15%.

VEPR Operating interest rates



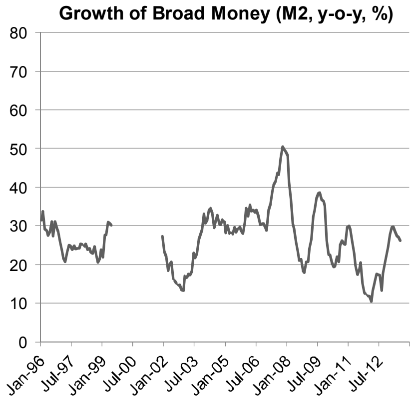
Source: SBV

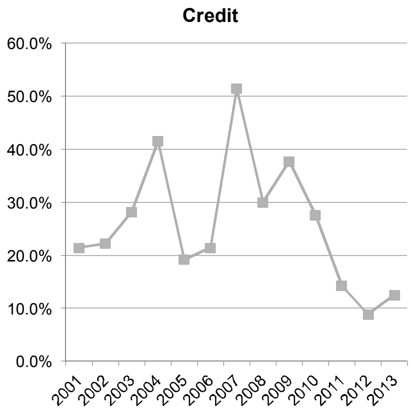
VEPR Outstanding bonds, trillion VND



Source: ADB Bonds Online

VEPR Money supply (M2) and credit





Source: ADB, SBV

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VEPR Monetary market

- Abundant liquidity.
- OMO interest rate decreased to 5.5%, trading rules were stricter, interbank market activities is in order.
- SBV issued state bank bills again since 2013H2 to control the appreciation of Vietnam dong, relieve the pressure on the exchange rate which lasted for more than 1 month.
- Along with selling USD, SBV withdrew VND through OMO, and monitored 14 commercial banks. SBV intervened strongly to maintain the confidence and market expectation in exchange rate.
- If exchange rate decreases by 2% - 3%, exchange rate is still high, affecting export and import.

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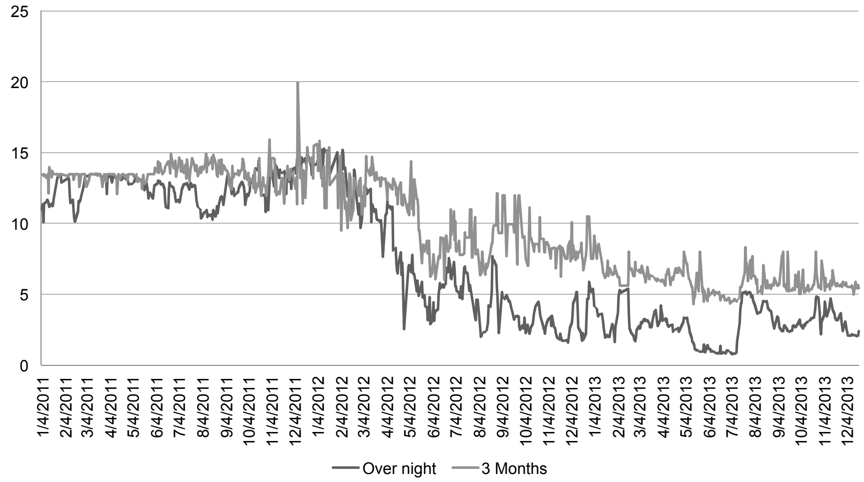
VEPR Vietnam interbank offer rates (%)



Source: SBV

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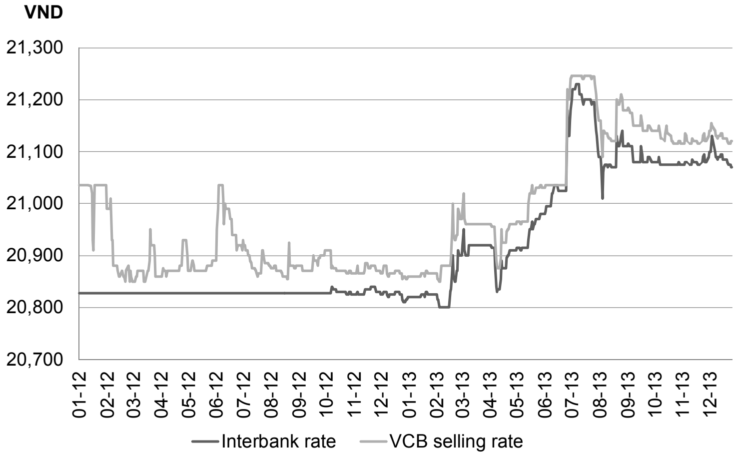
VEPR Nominal exchange rates



Source: SBV, VCB

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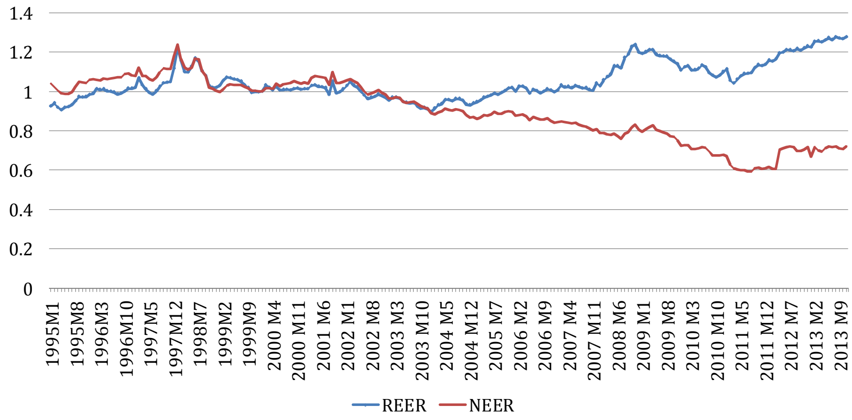
Nominal Effective Exchange Rate and Real Effective Exchange Rate,1995-2013



Source: Author's calculation

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Asset Markets: General

- Gold prices decreased significantly (-24%).
- Credit institutions were required to terminate lend and deposit in gold bullion.
- SBV auctioned 70 tons of gold.
- World Gold Council: Vietnam's gold demand increase to 80.3 tons.
- VN-index rose significantly, thanks to optimistic outlook for 2014 (allow higher percentage of ownership of foreign investors).
- Foreign investors were large net buyers, showing the positive outlook on the economy.
- Stock market capitalization to GDP ratio reached 31%.

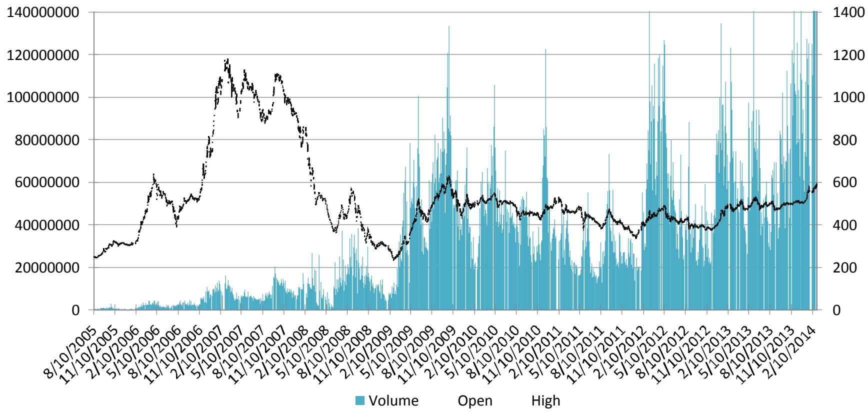
VEPR Asset Markets: Property Market

- The real estate market self-regulated through price and competition.
- 30 trillion aid package did not have a significant impact in real estate market, slow disbursement at 5% as of the end of 2013.
- Absorption rate rose significantly, higher transactions in the Southern market.
- Bright potential for real estates: 951 million USD has been committed into 21 FDI projects.

VEPR The Gold Market

Source: SJC

VEPR Securities Market (HCM)



Source: BIDV Securities Company

VEPR Macroeconomic Policies

- Policy space
  - Narrow: budget deficit did not allow policy-maker to implement expansionary fiscal policies. Because of the low credit demand, decreasing interest rate had limited effect on the economy.
- Policies
  - Target: Policies were toward stability, waiting for the sign of recovery.
  - To make a more competitive economy.
- Restructuring
  - This progress was clearer than 2012, although still slower than the expectation.

VEPR

2013 Constitution

- Lack essential changes: “socialism-oriented market economy”, leading role of State sector, land and resources owned by the people.
- Maintain current economic institution packed with malfunctions and corruption.
- Radical reforms under the risk of deferment, causing anxiety to investor; small effect in short-term but possibly clearer in long-term.
- Open window for interpretation and implementation of Constitution, risks associated with different interpretation, creating opportunities for interest groups.

VEPR

Chapter 3:
Identifying Vietnam's Binding Constrains Using Growth Diagnostics Approach

Nguyen Duc Thanh, Ph.D.
Pham Van Dai, MA

VEPR Introduction

- Identifying growth constraints is practically important but is a complicated academic work.
- Washington consensus conventional approach tends to ignore the specific features of each economy, and apply general principles without any priority (Stiglitz, 2003).
- Growth diagnostic is a new approach and soon becomes popular among academic and policy makers.

VEPR

Framework

- Decision tree Hausmann-Rodrik-Velasco (2005).
- Diagnostic principles:
  - High shadow price of constraints
  - A movement of constraint generates a significant movement of target function.
  - Agents attempt to overcome the constraints.
  - Agents less constrained tend to outperform agents more constrained .
- Matrix of tests Hausmann-Klinger-Wagner (2008).

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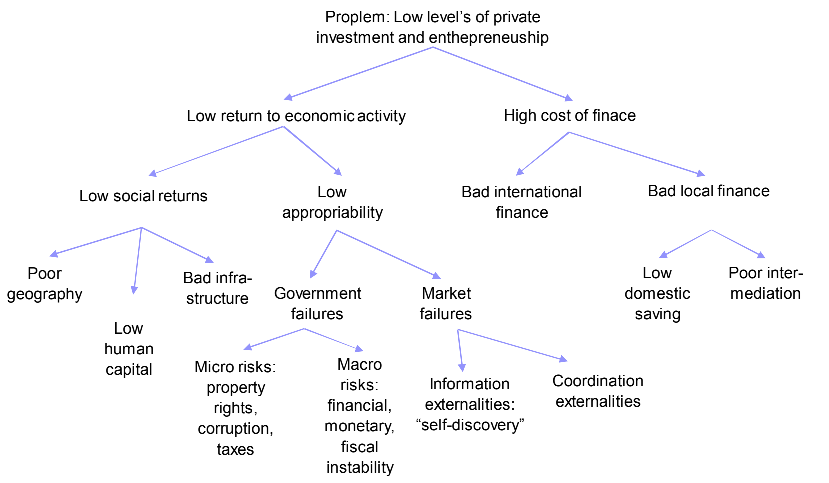
Framework

Growth Diagnostic Problem Tree



Source: Hausmann, Rodrik and Valesco, 2005

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Framework

Matrix of tests HKW

Binding Finance		Binding social returns					
		Lack of complementary factors		Low appropriability			Coordination problem
				Government failure			Market failure
				Ex ante	Ex post		
Low average savings	Bad finance	human capital	Infrastructure and public goods	Ex ante risks	Tax	Low property rights, crime, corruption	Low R&D, Low self-discovery
High lending interest rate		Low lending interest rate					
Low net cash flow from banks		High net cash flow from banks					
Investment elastic to interest rate		Lack of investment response to interest rate change					
Access to external finance			Low infrustructure wrt comparable countries	High static markups and low entry, in industries with entry costs	Monopoly power, high markups, regulated entry	Expropriation	Low sophistication (EXPY) and few new industries
Short loan duration, credit rationing		Inward migration of high skills		Political risk, social risk		Social unrest	Growth responds to new industries
High deposit interest rate	High spread	High returns to education	Shocks to infrastructure (hurricane, war)	Tax policy risk	High taxes, top marginal tax rate, corporate tax, VAT	Open conflict	
	If it's high risk, the low profits	Procyclical minceriean returns	Growth elastic to infrastructure change	Labor market risks	Restrictive labor regulations	Corruption (illegal tax rate)	Few products "nearby" to move (openforest low)
Negative relation between growth and current account	Monopoly powers: high P/E ratio of banks	Returns decrease as education grows	High losses in transport ()	High expectation of losing future profits	Cost of doing business		High returns to coordination activities

Source: Hausmann, Klinger, & Wagner, 2008

VEPR

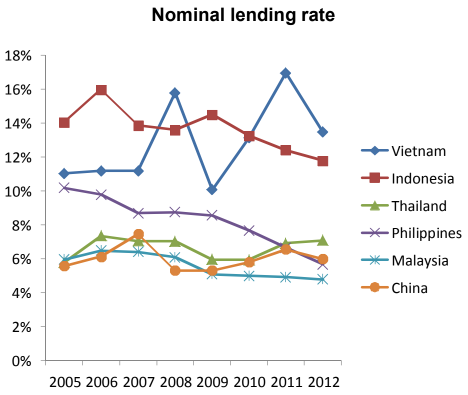
Backdrop of Vietnam economic growth

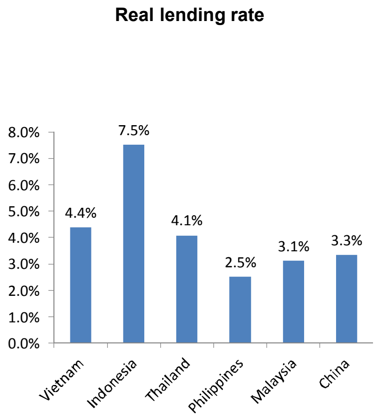
- Decreasing trend of economic growth.
- Fail to improve productivity.
- Unsustainable investment-led growth.
- Middle income trap?

=> *Which is growth constraints?*

VEPR Finance constraint

- Inflation is the cause of high lending rate in Vietnam. Real lending rate is not too high compared to neighboring economies





Source: Author's calculation from data provided by Worldbank

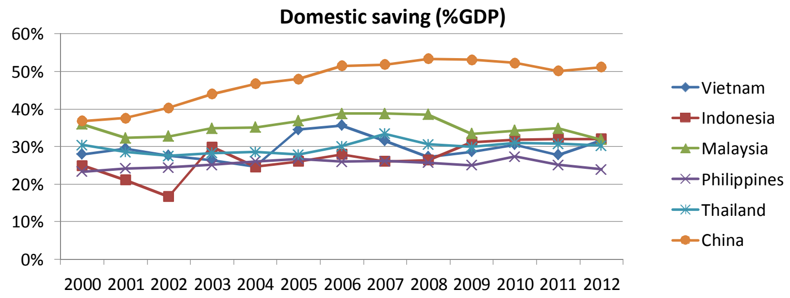
VEPR Finance constraint

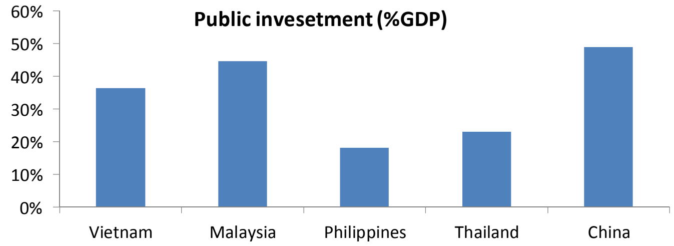
- There is turning point in banks' cash flow, from facing to liquidity crisis to be in excess of liquidity.
- Credit supply doesn't respond to lowering lending rate.

=> *constraint moves from capital supply side to investment demand.*

=> *Capital supply side is currently not a binding constraint, but likely to become whenever the economy return its high growth path.*

VEPR Domestic saving





Source: Author's calculation from data provided by Worldbank

VEPR Domestic saving

- *High public investment/domestic saving is currently not a binding constraint but could be a crucial one whenever the economy returns it high growth path.*

VEPR Financial intermediaries

- Low concentration level in Vietnam banking sector compared to neighboring countries.

  eg, total asset of three largest banks in Vietnam accounts for 35% of market share, compared to India 46%, Indonesia 44%, Malaysia 54%, Philippines 49%, Thailand 54%.
- P/E ratio in banking industry is relatively low, currently about 11.7, whereas retail industry (13.6), tourism and entertainment (26.7), insurance (18.0).

⇒ *No signal of monopoly.*

⇒ *Inefficiency of banks.*

Good Policy, Sound Economy

VEPR Return constraint: Human resource

- Labor force is surplus, more than 70% of labor force works in rural area.
- The quality of labor force in the same level with other developing countries in ASEAN.
- Labor migration is not a popular phenomenon.
- Return of high education is low.

=> *Human resource is not a binding constraint.*

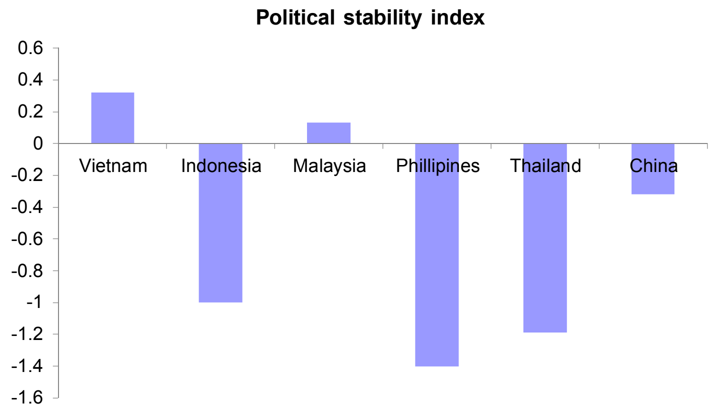
VEPR Return constraint: Infrastructure

- Global competitiveness report 2013-14 , Vietnam is ranked 82nd in infrastructure, comparing to the Philippines (96), Indonesia (61), Malaysia (29), Thailand (47), China (48).
- PCI Province competitiveness report 2013, 85% of foreign investor chose the province which has best infrastructure condition among surveyed places.
- Development gap between well-developed infrastructure area (Hong river delta, East southern zone) and poor infrastructure area (Highland, West northern zone, West southern zone).
- The profitability of transportation BOT projects.

=> *Infrastructure is a binding constraint.*

VEPR Government failures

- *Political and social risks is not a constraint*



Source: Kaufmann, Kraay, and Mastruzzi (2009)

VEPR Cost of doing business

- *Tax level in Vietnam is at a same level with regional developing countries. This is not a growth constraint.*

Source: Author's calculation from data provided by Worldbank

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VEPR Cost of doing business

- Weak property rights and crime are binding constraints.
  - eg, Recent thief in Samsung factory in Bac Ninh.
  - Slow response to riots in Binh Duong and Vung Ang industrial clusters
- Signal: the booming of private safeguard and security companies.

VEPR Cost of doing business

- Corruption in Vietnam is a critical constraint
  - PCI report 2013: 65.8% of foreign investor considers corruption in Vietnam more serious than other surveyed countries.
  - According to Kaufmann et al. (2009), Vietnam's score of corruption control is the lowest in the region.
  - Nguyen and Van Dijk (2012): Corruption affects negatively private companies but does not affect state-owned ones.

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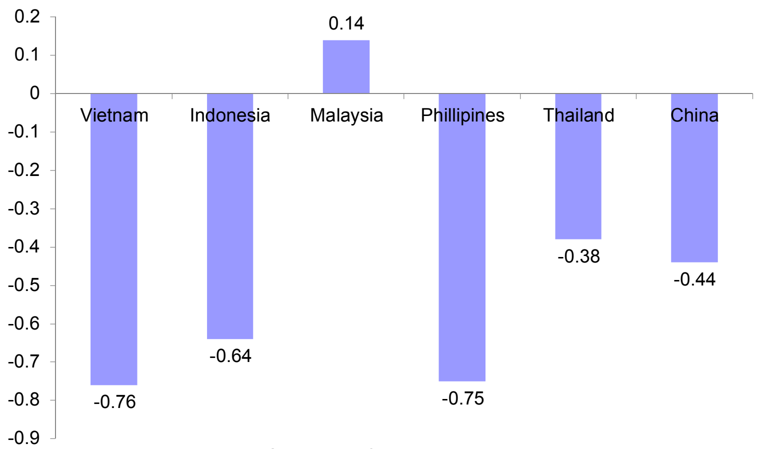
VEPR Cost of doing business

Corruption control index



Source: Kaufmann, Kraay, and Mastruzzi (2009)

VEPR Market failures

- Information and learning externalities: exports is at low level of sophistication and low value added.
- Coordination externalities: less development of supporting industries.

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VEPR Major constraints

- Macroeconomic instability, economic agents' loss of confidence in the future and management orientation are constraints for long-term investment
- Weak property rights and high corruption are major constraints to growth
- Infrastructure, especially transportation network, is binding constraint. Energy infrastructure is a vital constraint in medium- and long-term rather than in short term.
- Inefficiency of financial intermediary and over public investment could prevent the economy from returning its high growth path.

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Major constraints

- Market failures are binding constraints, especially in major ones such as labor, education, energy, input production, etc. markets.
- The lack of skilled and high-quality laborers is a constraint for economic growth. This is because of the failure of both the low-level and high-level education and training systems.
- The creativity and innovation of the economy are very limited. This is because of the failure of the state to protect intellectual properties and industrial secrets, the lack of an environment to encourage learning, researching, and independent thinking.

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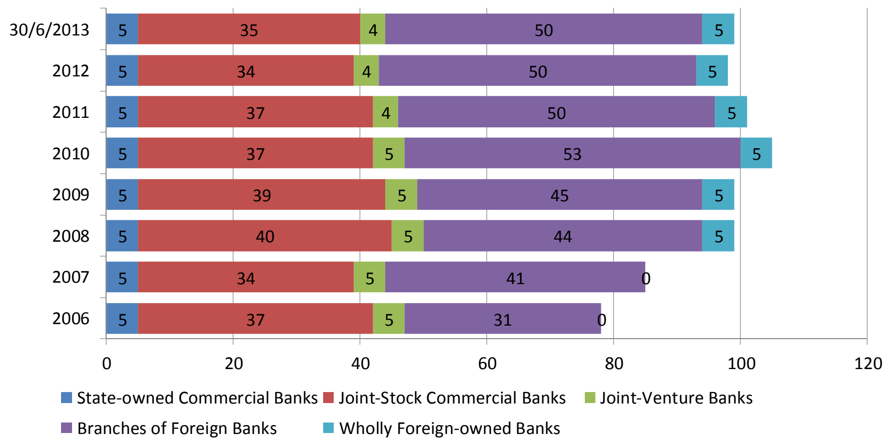
Chapter 4: A Financial Assessment for Vietnam's Banking System using Financial Soundness Indicators

Nguyen Duc Thanh, Ph.D.
Vu Minh Long

VEPR Main Contents

- The development of Vietnam's banking system
- An introduction to Financial Soundness Indicators (FSIs)
- A financial assessment for Vietnam's banking system using FSIs
  - Constraints for the calculation of FSIs in Vietnam
  - An analysis on calculated FSIs for Vietnam's banking system

VEPR Vietnam's banking system



Source: SBV's website

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VEPR Vietnam's banking system

Domestic credit provided by financial sector in selected countries, 2000-2010 (% GDP)

	2000	2005	2010
Lower middle income countries	50,57	49,91	58,73
Low & middle income countries	66,82	74,38	92,23
High income countries	174,87	181,12	197,45
China	119,67	134,30	146,28
India	51,19	58,36	71,94
Indonesia	60,68	46,20	36,39
Vietnam	32,57	65,40	124,66
Uganda	12,20	8,64	17,10
South Africa	152,46	185,89	191,66
Russia	24,93	22,12	37,45
Brazil	71,86	74,48	96,26

Source: World Bank (2013)

VEPR Financial Soundness Indicators (FSIs)

- FSIs are indicators of the current financial health and soundness of the financial institutions in a country, and of their corporate and household counterparts.
- FSIs include both aggregated individual institution data and indicators that are representative of the markets in which the financial institution operate. FSIs are calculated and disseminated for the purpose of supporting macroprudential analysis. This is the assessment and surveillance of the strengths and vulnerabilities of financial systems, with the objective of enhancing financial stability and, in particular, limiting the likelihood of failure of the financial system.
- There are core and encouraged sets of FSIs. The core indicators are normally applied by most countries, while the encouraged ones are applied according to countries' specific characteristics.

VEPR Capital-based indicators

- Regulatory capital to risk-weighted assets (CAR)
- Capital to assets
- Return on equity (ROE)
- Nonperforming net of provisions to capital

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Asset-based indicators

- Liquid assets to total assets
- Customer deposits to total loans
- Return on assets (ROA)
- Nonperforming loans to total gross loans

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Non-performing loans to total gross loans

Nonperforming Loans to Total Gross Loans of selected banks, 2008-2012 (%)

	BIDV	VCB	Vietin Bank	Exim bank	STB	Techcom Bank	MBB
2008	2.71%	4.61%	1.81%	4.71%	0.60%	2.52%	1.92%
2009	2.82%	2.47%	0.61%	1.83%	0.64%	2.49%	1.73%
2010	2.71%	2.83%	0.66%	1.42%	0.54%	2.29%	1.35%
2011	2.96%	2.03%	0.75%	1.61%	0.58%	2.83%	1.61%
2012	2.92%	2.40%	1.47%	1.32%	2.05%	2.70%	1.86%

	DongA Bank	HD Bank	KienLong Bank	LienViet PostBank	MDB	NaVi Bank	Ocean Bank	PG Bank	PNB	SHB
2008	2.55%	1.93%	0.59%		0.80%	2.91%	1.44%	1.42%	2.31%	1.89%
2009	1.33%	1.10%	1.17%	0.28%	2.93%	2.45%	1.61%	1.23%	2.33%	2.79%
2010	1.60%	0.83%	1.11%	0.42%	1.26%	2.24%	1.67%	1.42%	1.84%	1.40%
2011	1.69%	2.36%	2.77%	2.14%	2.08%	2.92%	2.08%	2.06%	2.32%	2.23%
2012	3.95%	4.34%	2.93%	2.71%		5.64%	3.52%	8.44%	3.02%	8.83%

Source: Author's calculation from banks' financial statements

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Income and expense-based indicators

- Interest margin to gross income
- Trading income to total income
- Noninterest expenses to gross income
- Personnel expenses to noninterest expenses

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Personnel expenses to non-interest expenses

Personnel expenses to noninterest expenses of selected banks, 2008-2012 (%)

	Agri bank	BIDV	VCB	Vietin Bank	ACB	Exim bank	STB	Techcom Bank	MBB	MSB	VP Bank	Average
2008	54.72%	60.03%	47.02%	59.44%	43.45%	46.91%			42.13%	42.78%	41.61%	**53.15%**
2009	51.98%	66.32%	56.78%	56.69%	47.06%	50.55%	45.61%	50.21%	45.88%	48.76%	43.53%	**53.25%**
2010	54.73%	60.62%	56.87%	57.55%	44.94%	53.01%	52.55%	47.52%	45.23%	45.26%	44.00%	**53.36%**
2011	56.78%	63.51%	55.94%	54.80%	50.02%	55.03%	57.28%	56.27%	43.82%	46.06%	52.80%	**53.07%**
2012		49.93%	55.75%	52.87%	44.13%	48.73%	51.35%	42.14%	52.90%	43.89%	42.41%	**47.80%**
	AB Bank	**BaoViet Bank**	**DongA Bank**	**HD Bank**	**LienViet PostBank**	**MDB**	**NaVi Bank**	**Ocean Bank**	**PG Bank**	**PNB**	**SHB**	**VietCapital Bank**
2008	37.48%	41.27%	38.18%	51.80%	44.47%	55.70%	44.11%	36.36%	37.68%	57.43%	44.82%	56.02%
2009	40.44%	41.19%	38.52%	45.87%	34.32%	61.75%	47.70%	39.29%	46.96%	53.59%	42.17%	57.15%
2010	42.61%	41.85%	37.47%	48.08%	32.70%	58.01%	44.47%	40.61%	45.84%	50.69%	41.18%	51.22%
2011	42.30%	38.50%	48.61%	44.95%	38.61%	64.45%	49.31%	33.05%	44.36%	47.02%	45.38%	43.07%
2012		36.71%	41.63%	37.90%		55.87%	37.67%	36.80%	39.64%	55.12%	43.60%	41.57%

Source: Author's calculation from banks' financial statements

VEPR Incalculable core indicators

- Regulatory capital to risk-weighted assets
- Regulatory Tier I capital to risk-weighted assets
- Net open position in foreign exchange to capital
- Sectoral distribution of loans to total loans

VEPR Overall assessment of the banking system's soundness

- The capital adequacy ratio was always higher the 8% minimum requirement of the Basel Committee, and even well above the 9% minimum requirement of the State Bank of Vietnam. However, the asset quality has not remained secure recently because of high nonperforming loans.
- The indicators measuring earnings and profitability all decreased, despite impressive growth in the past .
- The indicators measuring liquidity also showed a decreasing trend.

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Chapter 5:
International Economic Integration: Behind the Expectations of Vietnam

Nguyen Hong Son, Assoc. Prof. Ph.D.
Nguyen Anh Thu, Ph.D.
Nguyen Tien Dung, Ph.D.
Ha Van Hoi, Assoc. Prof. Ph.D.

VEPR Main Contents

- International economic integration of Vietnam and internal constraints
- Trans-Pacific Partnership Agreement (TPP): Big opportunities and challenges.
- ASEAN Economic Community and Vietnam's participation.
- Policy Implications

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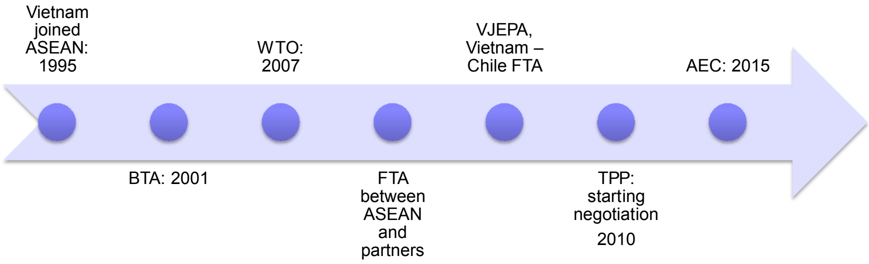
International Integration of Vietnam: the process started in 1995



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Achievements of economic integration

- In 2013, total import-export turnover reached 263.47 billion USD, more than 2.3 times higher than in 2007.
- Economic integration attracted a big amount of FDI, creating motivations for economic growth in Vietnam.

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VEPR Internal constraints

- Vietnam have a revealed comparative advantage (RCA) in the labor-intensive or natural-resource-based products such as agro-forestry and fishery products and garments.

→ Risk of "trade liberalization trap".

- High non-tariff barriers to Vietnam's exports.

VEPR Internal constraints

- Low FDI performance
  - FDI focuses primarily on the areas of assembly with low added value, low level of technology transfer and spillover to other economic areas.
- Do not take advantage of integration opportunities for domestic reform
  - Reform state-owned enterprises slowly.
  - Make the commitment to integration, but not effective for domestic reform.

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Internal constraints

- According to the ranking of world governance indicators (WGI), Vietnam belongs to low ranking group
  - The lowest are component indicators: "Voice and accountability" and "quality of law"
- From 2005 to date, the index of economic freedom (IEF) of Vietnam are approximately at 50, which is the boundary between the "repressed" economy and "almost no freedom“ economy.

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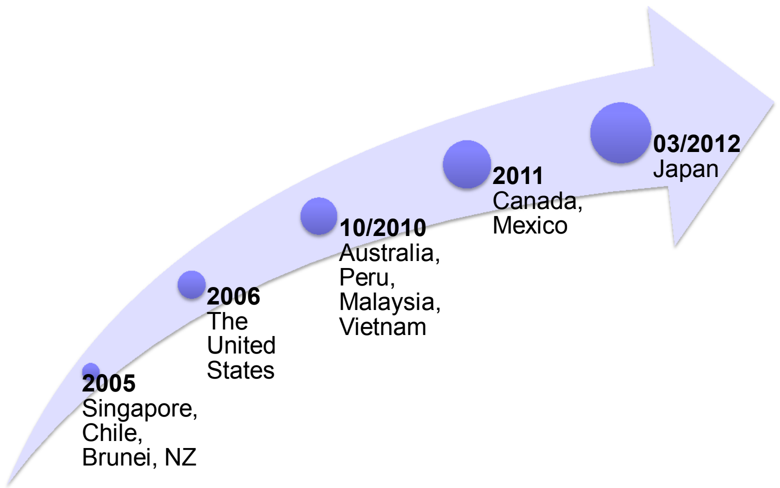
TPP formation



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The TPP Agreement: "21st Century FTA"

Negotiation Issues	Outline of the TPP Agreement
*** Trade and Investment Liberalization** - The removal of tariffs - Non-tariff barriers - Sensitive products - Liberalization of trade in services - Investment Liberalization - Special treatment for developing countries	- Market access for goods - Textile and apparel - Rule of origin - Technical barriers - SPS - Trade remedies - Custom - Cross-border services - Telecommunication - Financial Services - Temporary entry - Investment - Cooperation - Competition policies - Labor
Negotiation on Rules **New and Cross-cutting Issues**	- Environment - Government procurement - Intellectual Property rights - E-commerce - Legal issues

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Trade Relations between Vietnam and TPP members

- TPP is one of the largest FTAs that Vietnam has been participating in so far.
- TPP covers Vietnam's largest export markets (The U.S. and Japan).
- TPP covers major investing countries in Vietnam such as Japan, Malaysia, Singapore, and the U.S.
- Export of Vietnam to TPP countries has declining trend recently.
- Vietnam exports more to TPP members than it imports from these countries.

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Trade Relations between Vietnam and TPP members

- Major exports to TPP members include agricultural products and labor-intensive products.
  - TPP is the largest markets for Vietnam's labor-intensive manufacturing products (garment and footwear).
  - TPP is also the largest markets for Vietnam's agriculture and fishery products.
  - Amongst the TPP members, the U.S. is the largest market for Vietnam's agricultural and labor-intensive manufacturing products.

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Trade Relations between Vietnam and TPP members

- Vietnam's imports from TPP members mainly consists of machinery and equipments, and production materials.
- In 2012, imports of food and agricultural products from TPP members amounted to 3 billions U.S. dollars, accounting for 36% of total agricultural imports.
  - Major food and agricultural products imported from TPP members are cereals, meat, dairies, and fisheries.
  - Most of the imported food and agricultural products are supplied by Australia, New Zealand, the U.S. and Canada.

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Two-way Trade Between Vietnam and TPP Members, 2013

	Value (Millions USD)		Composition (%)	
	2007	2013	2007	2013
A. Exports				
Total Exports	48561	132135	100.00	100.00
Exports to TPP	24816	51572	51.10	39.03
Of which:				
The U.S.	10105	23869	20.81	18.06
Canada	539	1547	1.11	1.17
Mexico	360	890	0.74	0.67
Chile	47	219	0.10	0.17
Peru	17	-	0.03	-
New Zealand	68	274	0.14	0.21
Australia	3802	3514	7.83	2.66
Japan	6090	13651	12.54	10.33
Malaysia	1555	4926	3.20	3.73
Singapores	2234	2662	4.60	2.01
Brunei	-	18	-	0.01
B. Imports				
Total Imports	62765	132125	100.00	100.00
Imports to TPP	19603	30172	31.23	22.84
trong đo				
The U.S.	1701	5232	2.71	3.96
Canada	287	406	0.46	0.31
Mexico	59	115	0.09	0.09
Chile	110	315	0.18	0.24
Peru	48	43	0.08	0.03
New Zealand	246	449	0.39	0.34
Australia	1059	1587	1.69	1.20
Japan	6189	11612	9.86	8.79
Malaysia	2290	4104	3.65	3.11
Singapores	7614	5703	12.13	4.32
Brunei	-	607	-	0.46

Source: GSO

Trade Relations between Vietnam and TPP members

- Vietnam's trade structure shows a high degree of complementarity with that of other TPP members.
- Vietnam has a revealed comparative advantage (RCA) in:
  - Food and agricultural products (rice, fruits and vegetables, tea and coffee, rubber, aquacultural products, and wood).
  - Minerals (coal, crude oil).
  - Labor-intensive manufacturing products (furniture, garment, footwear).
  - Consumer electronics (telecommunication equipments, office equipments and parts).
- Most of TPP members do not possess a revealed comparative advantage in consumer electronics, garment, textile and footwear.

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The RCA Index for TPP Members, 2012

SITC	65	75	76	82	84	85	88
	Textile yam, fabrics	Office machine and parts	Telecom. equipments and parts	Furniture	Garment	Footwear	Photographic equipment
Vietnam	2.09	1.06	3.19	3.42	3.45	5.30	10.08
Japan	0.60	0.67	0.7	0.18	0.01	0.03	0.01
Singapore	0.12	1.85	0.78	0.06	0.33	0.14	0.12
Malaysia	0.49	2.16	1.38	1.26	0.07	0.84	0.10
Brunei	0.00	0.01	0.07	0.00	0.00	0.02	0.00
Australia	0.06	0.13	0.1	0.04	0.04	0.04	0.03
New Zealand	0.44	0.09	0.13	0.20	0.08	0.21	0.13
The U.S.	0.53	0.95	0.78	0.54	0.21	0.15	0.11
Canada	0.27	0.17	0.31	0.94	0.11	0.12	0.08
Mexico	0.37	1.64	2.69	1.72	0.12	0.50	0.22
Chile	0.16	0.03	0.06	0.06	0.15	0.22	0.24
Peru	0.66	0.01	0.01	0.06	0.06	1.48	0.08

Source: Calculated by author based on UNComtrade database

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The Potential Costs and Benefits of The TPP Agreement

- The TPP trade liberalization would expand market for Vietnam's exports, and for exports of labor-intensive manufacturing products in particular.
  - The significant benefits of TPP trade liberalization can be expected because of the large size of the TPP market and trade complementarity between Vietnam and other members.
  - Tariff have remained at relatively high levels for several manufacturing products including garment and textile, suggesting a substantial benefit of the tariff removal.
- The removal of tariffs and non-tariff barriers would stimulate foreign investment into Vietnam's exporting industries, thus further enhancing the benefit of trade liberalization.

The Potential Costs and Benefits of The TPP Agreement

- However, the benefit of the tariff removal could be eroded by the new trade barriers, including:
  - The possible application of the strict rule of origin (yearn forward).
  - Other possible trade barriers include the special safeguard measures or a long scheduling of tariff reductions.
- Manufacturing sectors will be negatively affected by TPP (e.g. livestock, dairy products, and services sectors).
  - Opening agricultural markets may negatively affect the livestock sector and efforts to diversify the structure of agricultural production and to develop rural areas.

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The Potential Costs and Benefits of The TPP Agreement

- The TPP aims to be a landmark, 21st century trade agreement.
  - The TPP has a broad and complex framework, covering traditional issues of trade and investment liberalization, as well as new and cross-cutting trade issues.
  - Vietnam may be required to adjust domestic policies and regulations in various areas such as competition, custom, state enterprises, government procurement, labor regulations, and intellectual property rights.

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The Potential Costs and Benefits of The TPP Agreement

MFN Tariff Rates on Garment and Footwear

	Textile	Garment	Footwear
Japan	5.5	9.2	12.9
Singapore	0	0	0
Malaysia	10.6	15.9	14
Australia	6.8	15.4	5.5
New Zealand	2	12	3.3
The U.S.	8	11.7	3.9
Canada	6.6	16.9	5.3
Mexico	12	35	15.2
Chile	6	6	6
Peru	12.9	17	6.7

Sources: WTO Tariff Database

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ASEAN ECONOMIC COMMUNITY

STRATEGIC SCHEDULE OF THE AEC BLUEPRINT (2008-2015)

Pillar 1
Single Market & Production Base

- Free flow of goods
- Free flow of services
- Free flow of investment
- Freer flow of capital
- Free flow of skilled labor
- Priority Integration Sectors
- Food, agriculture and forestry

Pillar 2
Competitive Economic Region

- Competition policy
- Consumer protection
- Intellectual property rights
- Infrastructure development
- Taxation
- E-Commerce

Pillar 3
Equitable Economic Development

- SME development
- Initiative for ASEAN Integration

Pillar 4
Integration into the Global Economy

- Coherent approach towards external economic relations
- Enhanced participation in global supply networks

VEPR Score card

VEPR Free flows of goods

- One key instrument of integration so far in ASEAN is removal of tariffs and non-tariffs barriers under CEPT/ATIGA.
  - 7 priority sectors: agriculture, automobile, electronics, fishery, rubber products, textile and garment, wood products.
- Vietnam commits to
  - Cut down all applied tariffs to 0% for all products traded among ASEAN by 2015 .
    - Reverses 7% of tariff lines until 2018.
    - Except for Sensitive List (SL), High Sensitive List (HSL) and General Exclusion List.

VEPR Free flows of goods

- Tariff reduction under AFTA (CEPT - ATIGA)
  - Average tariff ASEAN-6: 0.05%
  - Average tariff CLMV: 2.61%
  - Average tariff Vietnam: 1.88% in 2012; 1.77% in 2013 and 1.69% in 2014
- Customs reforms and other trade facilitation measures
  - E-customs procedures
  - Vietnam's National Single Window
  - Simplify the process of issuing license and certificates

VEPR Free flows of services

- AFAS (ASEAN Framework Agreement on Services) in 1995 -> the newest package AFAS 8.
- 5 priority service sectors
- Other special sector: financial services
- Remove Mode 1, 2; reduce Mode 3 and set parameter Mode 4.
- MRA: Mutual Recognition Agreements (MRAs)

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The scope of Vietnam's services commitments in AFAS 8

No.	Sector	**The number of sub-sectors under WTO rules**	**The number of sub-sectors Vietnam commit to WTO**	**The number of sub-sectors committed in AFAS 7**	**The number of sub-sectors committed in AFAS 8**
1	Business service	46	26	21	25
2	Communication service	24	19	20	20
3	Contruction service	5	5	5	5
4	Distribution service	5	4	4	4
5	Education service	5	4	4	4
6	Environment service	4	3	3	4
7	Financial service	17	16	16	16
8	Medical service	4	2	3	4
9	Tourism service	4	2	3	3
10	Entertainment, culture and sport services	5	2	2	2
11	Transport service	36	17	14	24

Source: Synthesis of authors from the Commitments of Vietnam service in GATS, AFAS 7 and AFAS 8

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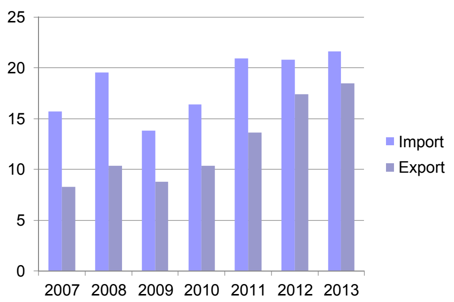
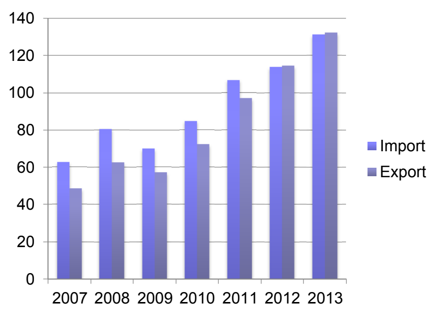
Trade and investment between Vietnam and ASEAN countries

Import export of Vietnam-ASEAN in 2007-2012, *Billion USD*



Import-Export of Vietnam – world in 2007-2012, *Billion USD*



Source: UNComtrade and General Department of Vietnam Customs

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Trade and investment relation of Vietnam and ASEAN countries

- The proportion of intra-trade in ASEAN accounted for only 25% of the total trade volume of the region.
- Major trade partners are Thailand, Singapore and Malaysia
  - Vietnam always has a relatively large trade deficit with ASEAN, especially with Thailand and Singapore. The trade surplus is most pronounced with Cambodia.
- Vietnam shows its high comparative advantage in fisheries, cereals, coffee, tea, rubber, wood, furniture, bags and travel goods, clothing and footwear.
- ASEAN countries have similar comparative advantage, except for furniture, but China has comparative advantage for this item.

→ *Vietnam has quite similar comparative advantages to the ASEAN countries → high level of competition.*

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Import – export between Vietnam – ASEAN

	Value (Millions USD)		Composition (%)	
A, Exports	2007	2013	2007	2013
Total Exports	48.56	132.2		
Exports to ASEAN countries	8.11	18.47	100	100
Brunei	N/A	0.02	N/A	0.09
Cambodia	1.04	2.93	12.84	15.84
Indonesia	1.15	2.45	14.22	13.29
Lao PDR	0.11	0.46	1.35	2.48
Malaysia	1.55	4.93	19.17	26.67
Myanmar	0.02	0.23	0.27	1.23
Philippines	0.97	1.70	11.90	9.18
Singapores	2.23	2.66	27.55	14.41
Thailand	1.03	3.19	12.70	17.29
B. Imports				
Total Imports	62.76	131.3		
Imports to ASEAN countries	15.91	21.64	100	100
Brunei	N/A	0.61	N/A	2.80
Cambodia	0.21	0.50	1.29	2.33
Indonesia	1.35	2.37	8.51	10.97
Lao PDR	0.21	0.67	1.33	3.09
Malaysia	2.29	4.10	14.39	18.97
Myanmar	0.08	0.12	0.47	0.57
Philippines	0.41	0.95	2.60	4.40
Singapores	7.61	5.70	47.86	26.35
Thailand	3.74	6.31	23.53	29.17

Source: UNComtrade and General Department of Vietnam Customs

VEPR RCA of Vietnam, ASEAN and China

SITC	Description	Brunei	Indonesia	Cambodia	Malaysia	Philippines	Singapore	Thailand	Vietnam	China
3	Fish and fish preparations	0.03	2.64	0.03	0.50	2.18	0.12	5.00	7.36	1.22
4	Cereals and cereal preparations	0.01	0.18	1.58	0.44	0.26	0.32	2.22	3.10	0.06
5	Fruit and vegetables	0.00	0.33	0.10	0.16	2.53	0.06	1.60	2.04	0.74
7	Coffee, tea, cocoa, spices & manufacs. Thereof	0.00	3.15	0.02	1.29	0.03	0.47	0.24	7.16	0.19
23	Crude rubber including synthetic and reclaimed	0.00	11.02	5.57	3.18	0.31	0.31	10.58	5.75	0.11
32	Coal, coke and briquettes	0.00	16.43	0.01	0.02	0.38	0.00	0.00	1.28	0.12
61	Leather, lthr. Manufs., nes & dressed fur skins	0.00	0.56	0.18	0.06	0.10	0.22	1.37	2.23	1.01
62	Rubber manufactures, nes	0.06	1.35	0.01	1.42	0.74	0.28	3.60	1.03	1.13
63	Wood and cork manufactures excluding furniture	0.01	3.67	0.05	2.71	10.70	0.07	1.11	2.80	1.39
65	Textile yarn, fabrics, made up articles, etc.	0.00	1.45	0.35	0.47	0.20	0.12	0.94	1.96	2.76
72	Electrical machinery, apparatus and appliances	0.04	0.45	0.05	2.25	3.45	2.41	1.10	1.69	1.99
82	Furniture	0.00	0.98	0.24	1.21	0.36	0.06	0.53	3.28	2.83
83	Travel goods, handbags and similar articles	0.00	0.36	0.30	0.08	0.39	0.36	0.44	3.73	4.09
84	Clothing	0.02	1.72	23.36	0.85	1.38	0.14	0.82	5.40	3.29

VEPR Trade complementary index of Vietnam with ASEAN countries

Partner	2006	2007	2008	2009	2010	2011	2012
Thailand	44.64	45.34	50.75	49.19	48.83	52.06	52.91
Singapore	42.04	45.63	47.38	45.02	44.57	47.34	53.07
Malaysia	34.21	37.06	42.69	41.58	47.47	53.99	58.19
Philippines	N/A	43.49	51.78	47.33	47.08	58.07	56.23
Cambodia	32.71	33.72	37.87	42.5	40.86	43.13	39.5
Indonesia	N/A	N/A	N/A	N/A	48.49	50.54	48.72

Source: Calculated by author based on UNComtrade database

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Trade and investment relation of Vietnam and ASEAN countries

- In the total net worth of FDI into ASEAN, intra - investment accounted for a modest proportion of about 19%.
- Vietnam ranked No. 5, attracted 8% of total FDI in ASEAN in the period of 2007-2012 .
- Vietnam receives a large amount of FDI from both ASEAN countries and non-member countries.
- FDI contributes to the growth of Vietnam in general and contribute to build the comparative advantage of exports (e.g. items of telecommunications equipment having high RCA thanks to FDI).

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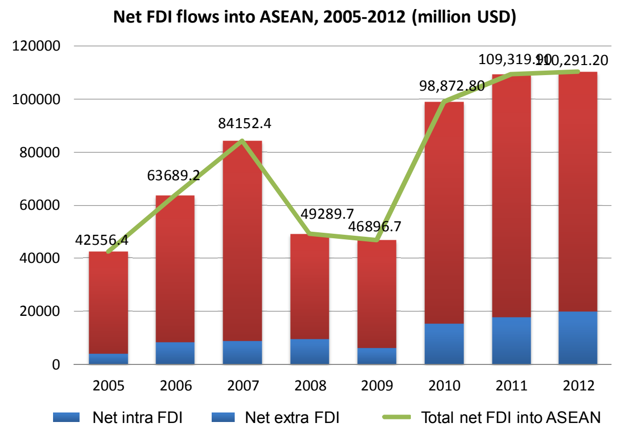
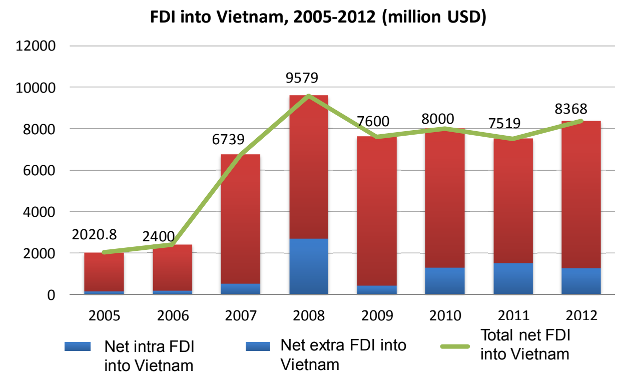
Trade and investment relation of Vietnam and ASEAN countries



Source: FDI ASEAN Database by 30.10.2013

Trade and investment relation of Vietnam and ASEAN countries



Source: FDI ASEAN Database by 30.10.2013

AEC: Some issues to be considered

- Cooperation and competition in ASEAN
  - Vietnam and ASEAN countries tend to compete in both exporting and attracting foreign investment.
  - AEC is moving towards a "single market and production base", i.e. making a connectivity in ASEAN, establishing production networks in the region, ASEAN enterprises will participate in this network and allocate resources in an optimal way.
- The view of Vietnamese business on AEC
  - Vietnam enterprises have very limited awareness of the AEC.
  - The businesses almost recognize the benefits of market access, export growth, which are relatively limited in AEC.
  - They do not see the long term benefits of the connectivity in "single market and production base" in AEC.

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Policy implications

- Vietnam needs to assess its comparative advantage, finding a position in the regional and global production networks.
  - Government should consider policy supporting research and development, design activities to promote added value for exports.
- There should be a comprehensive and unified view of the opportunities and challenges of integration from government to businesses.
- It is necessary to consider the effectiveness of law enforcement in order to take advantage of the institutional reform of the integration process.

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Policy implications (cont.)

- For TPP
  - Commitments to intellectual property, state enterprises, and public procurement may require changes in policy and legislation in the country.
  - There should be deep research on the issues being negotiated in TPP and their impact on the economy, including the market size, intellectual property, labor, environment, investment, and related issues.
  - Vietnam should take full advantage of the developing country status under the TPP negotiation. Commitments on rules and market opening should be made and scheduled appropriately to allow domestic industries to adjust.

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Policy implications (cont.)

- For AEC
  - Government should develop an effective mechanism to raise businesses' awareness of the AEC, especially on the long-term benefits that AEC brings.
  - Be better prepared for the migration of skilled labor in ASEAN after 2015 through two major tasks.
    - Firstly, construct and improve regulations and standards to be recognized as "ASEAN skilled labor" in the fields that ASEAN signed MRAs.
    - Secondly, promote education and training human resources, especially in the priority areas of ASEAN, by promoting cooperation with universities in ASEAN.

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Conclusion

- Moving from static comparative advantage to dynamic competitive advantage, avoiding the "trap of trade liberalization"
- Leveraging FDI to participate in global production networks
- Integration is an opportunity for institutional reform and economic restructuring

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Chapter 6:
Vietnam's Choices of Energy Policies

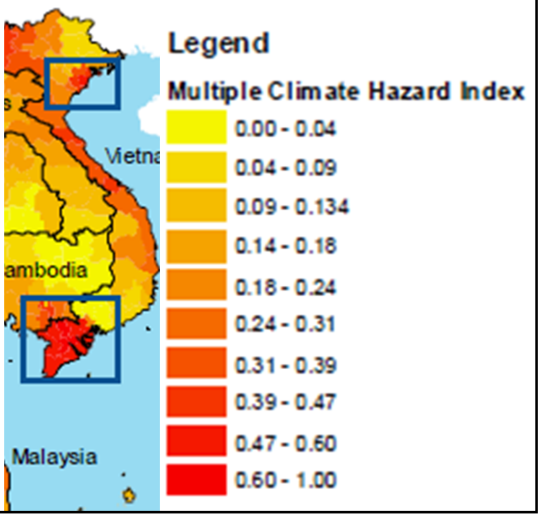
Phil Smith, MSc.

VEPR Electricity Production

- Consumption 140,000 GWh (2014e)
  - Growing 14% pa
- Capacity 41 GWe
  - 30% Hydro
  - 20% Gas
  - 40% Coal
  - Renewables 0.06%
- Transmission losses >4,000 GWh

VEPR Consequences of Increasing Reliance on Coal

- Climate Change
  - Mekong and Red River Deltas
- Balance of Payments



VEPR Energy Security (VEPR Model)

- Oil depleted 2029 Coal low 2030.
- Gas secure but limited exploitation.
- National electricity shortage 2024
  - It is too late to invest in renewables to avoid this shortage, imported coal and oil is the only option.
  - It is not too late to plan investment in renewables for long term security.

VEPR Nuclear

- Phuoc Dinh 1 and 2 Nuclear Power Plants (Ninh Thuan Province)
- 4 * 1,000 MWe

$mn	Nuclear					
	Costs Low			Costs High		
MW	1000e	1400e	2000e	1000e	1400e	2000e
Capital Costs	1,000	1,400	2,000	4,000	5,600	8,000
Annual Operating Costs	29	40	57	40	56	80
Decommissioning Costs	52	73	104	400	560	800

VEPR Nuclear

Nuclear $mn	Costs Low/Revenue High			Costs High/Revenue Low		
MW	1000e	1400e	2000e	1000e	1400e	2000e
Capital	1,000	1,400	2,000	4,000	5,600	8,000
Interest	6,600	9,240	13,200	51,520	72,128	103,040
Operations and Maintenance	1,720	2,408	3,440	2,000	2,800	4,000
Remediation	52	73	104	400	560	800
Total Costs	8,372	11,721	16,744	53,920	75,488	107,840
Revenue	43,336	60,670	86,671	16,097	22,535	32,193
Discounted IRR	6.96	6.96	6.96	-1.40	-1.40	-1.40

VEPR Nuclear

Average Costs and Revenue $mn	Nuclear		
MW	1000e	1400e	2000e
Capital	2,500	3,500	5,000
Interest	29,824	41,754	59,648
Operations and Maintenance	1,860	2,604	3,720
Remediation	226	316	452
Total Costs	31,910	44,674	63,820
Revenue	29,716	41,603	59,432
Discounted IRR	-0.12	-0.12	-0.12

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VEPR Geothermal

- 300 Geothermal Fields
- 1,400MW
- Could develop 400MW by 2020

$mn	Geothermal					
	Costs Low			Costs High		
MW	20	50	100	20	50	100
Capital Costs	43	61	111	74	102	146
Annual Operating Costs	0.4	1.0	2.0	0.6	1.5	3.0

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Geothermal

Geothermal $mn	Costs Low/Revenue High			Costs High/Revenue Low		
MW	20	50	100	20	50	100
Capital	43	61	111	74	102	146
Interest	150	213	388	511	704	1,007
Operations and Maintenance	12	30	60	15	38	75
Total Costs	162	243	448	526	741	1,082
Revenue	433	1,083	2,167	161	402	805
Discounted IRR	5.58	11.52	12.79	-2.78	-1.83	-1.03

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Geothermal

Average Costs and Revenue $mn	Geothermal		
MW	20	50	100
Capital	58	81	128
Interest	305	425	670
Operations and Maintenance	14	34	68
Remediation	-	-	-
Total Costs	318	459	738
Revenue	297	743	1,486
Discounted IRR	-0.24	2.21	3.62

VEPR Mini Hydro

- Mini hydro low impact means of generation

$mn	Mini Hydro					
	Costs Low			Costs High		
MW	0.1	0.25	1	0.1	0.25	1
Capital Costs	0.25	0.50	0.02	0.40	0.80	3.20
Annual Operating Costs	0.01	0.02	0.03	0.02	0.03	0.06

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VEPR Mini Hydro

Mini Hydro $mn	Costs Low/Revenue High			Costs High/Revenue Low		
MW	0.1	0.25	1	0.1	0.25	1
Capital	0.25	0.50	2.00	0.40	0.80	3.20
Interest	0.78	1.55	6.20	2.39	4.78	19.14
Operations and Maintenance	0.23	0.45	0.90	0.38	0.75	1.50
Total Costs	1.00	2.00	7.10	2.77	5.53	20.64
Revenue	1.68	4.19	16.76	0.35	0.88	3.53
Discounted IRR	2.25	3.65	4.54	-3.49	-3.36	-3.32

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Mini Hydro

Average Costs and Revenue	Mini Hydro		
MW	0.1	0.25	1
Capital	0.33	0.65	1.61
Interest	1.88	3.76	9.30
Operations and Maintenance	0.30	0.60	1.20
Total Costs	2.18	4.36	10.50
Revenue	1.01	2.54	8.05
Discounted IRR	-1.91	-1.49	-0.83

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Biomass

- 8 GW from rice husk, sugarcane, cassava, wood and animal waste by 2020.

Smn	Gasification					
	Costs Low			Costs High		
MW	50	100	150	50	100	150
Capital Costs	50	100	150	80	160	240
Annual Operating Costs	5	10	15	10	20	30

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Biomass - Gasification

Gasification $mn	Costs Low/Revenue High			Costs High/Revenue Low		
MW	50	100	150	50	100	150
Capital	50	100	150	80	160	240
Interest	155	310	465	478	957	1,435
Operations and Maintenance	150	300	450	250	500	750
Total Costs	305	610	915	728	1,457	2,185
Revenue	838	1,676	2,514	265	529	794
Discounted IRR	5.83	5.83	5.83	-2.55	-2.55	-2.55

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Biomass - Gasification

Average Costs and Revenue $mn	Gasification		
MW	50	100	150
Capital	65	130	195
Interest	376	751	1127
Operations and Maintenance	200	400	600
Total Costs	576	1,151	1,727
Revenue	551	1,103	1,654
Discounted IRR	-0.15	-0.15	-0.15

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VEPR Biomass – Anaerobic Digestion

$mn	Anaerobic Digestion					
	Costs Low			Costs High		
MW	2.5	5	10	2.5	5	10
Capital Costs	2.5	5	10	7.5	15	30
Annual Operating Costs	0.13	0.25	0.50	0.33	0.66	1.33

Anaerobic Digestion $mn	Costs Low/Revenue High			Costs High/Revenue Low		
MW	2.5	5	10	2.5	5	10
Capital	2.5	5	10	7.5	15	30
Interest	7.75	15.5	31	44.85	89.7	179.4
Operations and Maintenance	3.75	7.50	15.00	8.25	16.50	33.25
Total Costs	11.50	23.00	46.00	53.10	106.20	212.65
Revenue	62.70	125.40	250.80	19.40	38.81	77.62
Discounted IRR	14.84	14.84	14.84	-2.54	-2.54	-2.54

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VEPR Biomass - Anaerobic Digestion

Average Costs and Revenue	Anaerobic Digestion		
MW	2.5	5	10
Capital	5	10	20
Interest	29	58	116
Operations and Maintenance	6.00	12.00	24.13
Total Costs	34.89	69.78	139.69
Revenue	41.05	82.10	164.21
Discounted IRR	0.63	0.63	0.63

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Wind

- 1,000GW of potential wind capacity.
- 12GW of wind power by 2020
  - Binh Thuan, 30MW last year with.
  - Further 41 wind power projects in the country.
  - Bac Lieu Province 56GWh offshore wind turbines.

$mn	Wind					
	Costs Low			Costs High		
MW	1	10	100	1	10	100
Capital Costs	2	13	100	3	16	125
Annual Operating Costs	0.01	0.05	0.50	0.01	0.10	1.00

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Wind

Wind $mn	Costs Low/Revenue High			Costs High/Revenue Low		
MW	1	10	100	1	10	100
Capital	2	13	100	3	16	125
Interest	3	26	210	15	96	748
Operations and Maintenance	0	1	10	0	3	25
Total Costs	3	27	220	15	98	773
Revenue	7	67	670	4	41	407
Discounted IRR	5.31	7.30	10.24	-2.93	-2.34	-1.89

Average Costs and Revenue $mn	Wind		
MW	1	10	100
Capital	2	14	113
Interest	10	69	545
Operations and Maintenance	0	2	18
Total Costs	10	71	563
Revenue	5	54	539
Discounted IRR	-1.62	-0.85	-0.15

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Solar

- Muang Giang.
- Long An and in Ho Chi Minh City Factories.
- Mostly used for heating water, rather than electricity generation.

$mn	Solar					
	Costs Low			Costs High		
MW	1	5	10	1	5	10
Capital Costs	2	4	6	4	8	12
Annual Operating Costs	0.05	0.10	0.20	0.08	0.16	0.25

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Solar

Solar $mn	Costs Low/Revenue High			Costs High/Revenue Low		
MW	1	5	10	1	5	10
Capital	2	4	6	4	8	12
Interest	4	8	13	24	48	72
Operations and Maintenance	1	2	4	2	4	6
Total Costs	5	10	17	26	52	78
Revenue	4	19	39	1	4	7
Discounted IRR	-1.34	4.14	6.75	-3.89	-3.72	-3.63

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Average Costs and Revenue $mn	Solar		
MW	1	5	10
Capital	3	6	9
Interest	16	32	49
Operations and Maintenance	2	3	5
Total Costs	18	35	54
Revenue	2	11	23
Discounted IRR	-3.11	-2.43	-2.03

VEPR Discussion

- State subsidizes electricity as a part of its macro-economic policy to control inflation.
- Investment in renewables would require generous published feed-in tariffs.
- Impact on consumers.
- Impact of removing subsidies on export orientated businesses (e.g. garments).
- Impact of renewables in stimulating high value added industries.

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Chapter 7: VIETNAM ECONOMIC PROSPECTS 2014 AND POLICY IMPLICATIONS

Nguyen Duc Thanh, Ph.D.

VEPR Vietnam Economic Prospects 2014

Year	2010	2011	2012	2013	2014 Scenario 1	2014 Scenario 2
Growth (%)	6.42	6.24	5.25	5.42	4.15	4.88
Inflation (%)	11.75	18.90	6.81	6.04	4.76	5.51

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Short-term issues

- Giving priority to growth recovery, enterprise revitalization policies and monetary policies for macroeconomic stabilization. Macroeconomic stabilization is always the solid premise for other fundamental policies.
- Since expected inflation might be less than 6%, along with banks' excess liquidity, SBV can continue to put pressure on decreasing deposit rates. However, it should be careful not to disrupt the capital market when real deposit rates become.
- For real estates market, it is necessary not to lengthen the adjustment process by supporting packages or impractical methods, which create false expectations on this market. The best method is to help the market to self-adjust its prices (cutting down prices).
- Exchange rate policies should not be focused on short-term adjustment for the second half of the year (2-3% increase). They should be focused on a stable future in order to promote domestic production. After a period of sea tension with China, exchange rates should be adjusted since we do not have many opportunities of favorable macroeconomic conditions.

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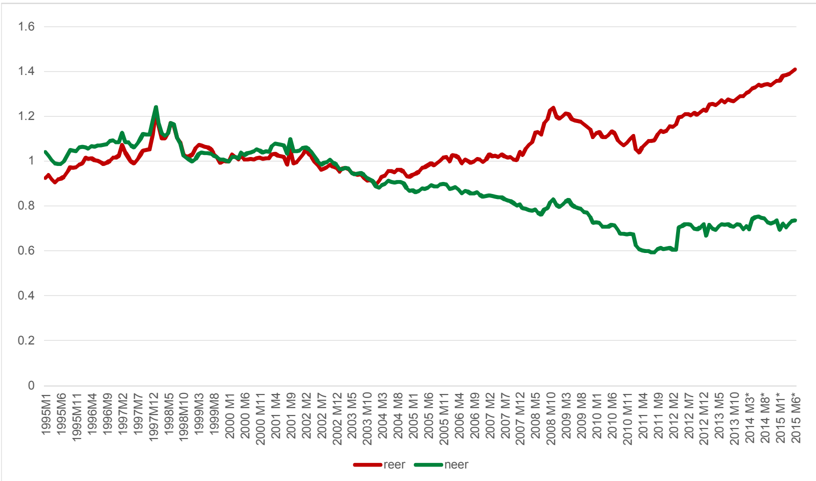
NEER and REER to 2015



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Fundamental issues

- Disposal of bad debts: it is necessary to create a market for trading debts and a mechanism to allow domestic and international investors to enter the market;
- Privatization of state-owned enterprises, following the Prime Minister's speech in the beginning of the year, to improve government's budget position and at the same time to restructure the economy;
- Besides benefits from exports, the risks of the development trends as Vietnam further integrates into the international commitments with higher degree of free trade (ACFTA, TPP, other FTAs) should be paid more attention. Institutional reforms and an improvement in business environment are keys to successful integration;
- Streamlining central and local personnels to control current budget expenditure;
- Improve commitment to a roadmap of reforms and restructuring the economy; need to focus and to avoid dispersion that takes time and take away opportunities;
- More practical, clear, and effective industrial policy;
- Actively restructure the labor market to improve labor quality and skills.

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Policy recommendations

- Focusing on changing the economic model, economic growth path and ideology in governing the economy. The recent period of economic recession has showed many lessons. Along with disputes with China, the needs for reforms and decreasing dependence become clearer;
- Identifying strategic partners like Japan, Korea, Australia, India and ASEAN to construct long-term cooperation and decrease dependence on China;
- Policies to support enterprises and recover the economy in the short-term, giving priority to improve the business environment and competitiveness rather than short-term stimulation policies and populist statements (like in the real-estate market);
- Promoting the economy's productivity in medium and long-term by focusing on institutional reforms toward a market economy to allocate resources more efficiently;
- Focusing on resources allocation and the creation of investment mechanism to support production in the agricultural sector. Specifically, the marine economy needs to be supported directly (in repairing and supplying materials) to fishermen. Fishing ships should be supported in logistics by national vessels.

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Sincere thanks!

Q&A?

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