VEPR Policy Discussion Note

PD-03

Characteristics of Vietnamese public debt

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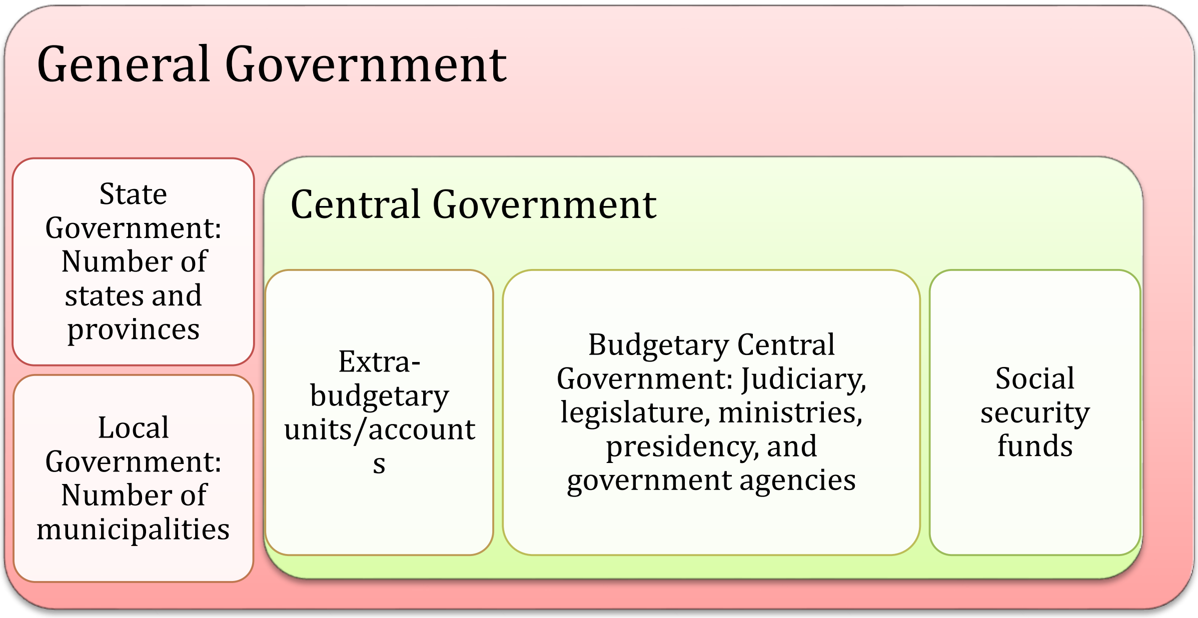
Differences between Vietnamese and IMF's public debt calculation

Although public debt is understood clearly and intuitively to be the state's debt, the calculation method and scope of the public debt are rather different among countries. To ensure the ability to compare and control the public debt vulnerabilities of all countries over the world, The International Monetary Fund (IMF) provided the statistical standard definition of public debt (IMF, 2001). This definition takes into account two basic elements: the institutional coverage and the debt instrument coverage.

Institutional coverage

According to IMF definition, public debt includes the debt of the central government and the local government, in which, central government debt consists of the debt of not only the Budgetary Central Government (Judiciary, legislature, ministries, presidency, and government agencies) but also Extra-budgetary units/accounts (State-owned units perform specific functions such as providing health services, education services, social security… which are controlled and financed by Central government) and Social security funds.



Source: IMF (2001)

As defined in the Law on Public Debt Management in 2009, Viet Nam's public debt comprises of Government debt, Government-guaranteed debt, and the debt of local governments. In comparison with IMF's definition, the institution coverage in Viet Nam's public debt definition does not include extra-budgetary units/accounts (which are guaranteed by Government such as Vietnam Bank for Social Policies (VBSP) and Vietnam Development Bank (VDB)) and social security funds. However, the exclusion of SOEs (Which are not guaranteed by Government) in the institutional coverage is consistent with the convention of the IMF.

Debt Instruments

IMF (2001) issued six different instruments that comprise gross debt:

- Debt securities such as bills, commercial paper, and bonds.
- Loans.
- Other accounts payable such as trade credits and advances and miscellaneous other items due to be paid or received.
- Special Drawing Rights (SDRs) are international reserve assets created by the IMF and allocated to its members to supplement existing reserve assets. The definition of gross debt includes SDRs. However in many countries SDRs are held by central banks and are not included in the debt of the general government.
- Currency and deposits. Currency consists of notes and coins that are of fixed nominal values and are issued or authorized by the central bank or government.
- Insurance, pension and standardized guarantee schemes (IPSGS).

Statistics on public debt is a precondition for calculating net debt. Net debt is important to any comprehensive analysis of a country's debt, debt sustainability, and fiscal risks. According to IMF (2011), net debt is calculated as gross debt minus the financial assets corresponding to debt instruments.

Thus, compared with IMF's convention, Viet Nam has not made the net public debt calculation. Besides, the debt instrument coverage is less in Viet Nam's definition than in IMF's convention due to excluding: currency and deposits; SDRs; IPSGS; deposits and advances of extra-budgetary units.

It should be noted that there are no regulations on net debt calculation in Viet Nam; therefore, if including the above instruments, the actual public debt would be magnified. The reason is that the current calculation method only refers to the capital mobilization, and does not consider operations using capital. For example, the capital from social security funds can be used to buy government bonds. Thus, if that capital of these organizations is included in public debt, it will be doubly calculated in the public debt. Similarly, when referring to the financial obligations of VBSP and VDB such as deposits, trust funds; we need to consider the financial assets formed from the mobilized capital.

To summarize, the regulations on public debt calculation in Viet Nam shows several differences from international standards, and basically ignores the risks arising from extra-budgetary units but guaranteed by government. Nevertheless, to add the financial obligations of these organizations to the public debt might magnify the actual number. Therefore, the solution which should be achieved is to build a statistical framework on net debt, instead of gross debt, based on international standards. This has important implications for the risk control through constructing indicators for Viet Nam's public debt and comparing these figures with other correspondingly development countries.

Characteristics of Vietnamese public debt

Viet Nam's public debt is at high levels and increasing rapidly

According to official data from the Ministry of Finance, public debt to GDP ratio increased from 51.7% in 2010 to 53.3% in 2010, after declining to 50% in a 2011-2012 period. Public debt rate was estimated about 60.3% of GDP and 64% of GDP in 2014 and 2015, respectively (Phương Nhi, 2015).These numbers were higher than the previously estimated numbers, about 59.6% of GDP, according to "Report on Using of loans and Public debt management", presented by MOF on May 18th, 2015.

However, it should be noted that the method of public debt calculation in Viet Nam reveals several differences from international standards, so there are some significant discrepancies between data published by Government and data calculated by independent organizations. A calculation of the World Bank (WB, 2015) showed that Vietnamese public debt rate was approximately 59.6% of GDP in 2014, lower than official estimates. According to The Economist (2015), public debt is on a downward trend in terms of the ratio to GDP, but increases in total volume (Table 1). In a research conducted by Academy of Policy and Development (APD), the authors indicated that the institution coverage according to the Law on Public Debt Management was narrower than the coverage estimated by international organizations. The public debt calculation proposed by this study, covering loans which government have to pay[1], showed Viet Nam's public debt was about 65.2% of GDP in 2012 (Phạm Huyền, 2014).

Table 1. Public debt in Viet Nam, 2010-2014 (billion VND)

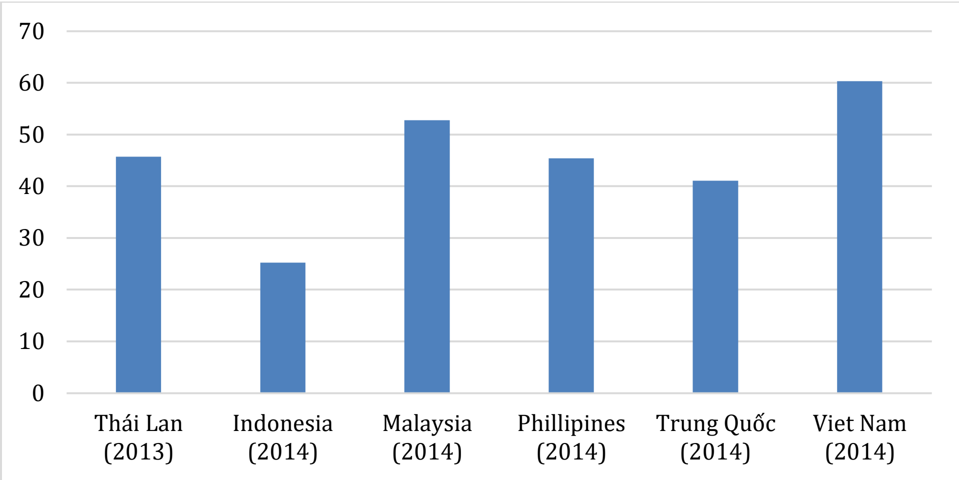
	2010	2011	2012	2013	2014 (estimate)	2015 (forecast)
Gross public debt	1,115,342	1,381,136	1,622,584	1,912,082	2,374,527	2,837,560
Domestic	495.484	598.029	744.521	960.346	1.294.117	1.645.785
(% GDP)	(23.0%)	(21.5%)	(22.9%)	(26.8%)	(32.9%)	(38.2%)
External	619,858	783,107	878,063	951,735	1,080,410	1,191,775
(% GDP)	(28.7%)	(28.2%)	(27.1%)	(26.6%)	(27.4%)	(27.7%)
Public debt to GDP	51.7%	49.7%	50.0%	53.3%	60.3%	65.9%
The Economist	54.0%	53.5%	50.2%	48.9%	47.6%	46.3%

Source: Government Report no. 221/BC-CP on May 18th, 2015, The Economist (2015) and Authors' forecast for 2015

[1]The authors from APD recommended to add 4 instruments to public debt in Viet Nam, including debt payments of local and central governments, VBSP, VDB; the costs for bad debt disposal, insurance debts; and losses due to foreign exchange rate fluctuations. However, these suggestions are not consistent with international standards and tend to be biased due to skipping financial assets formed from these added items.

Regarding to the ratio to GDP, gross public debt in Viet Nam accounted for 60% of GDP in 2014, the highest level in comparison with other developing countries (Figure 1)[2]. It can be seen that most of these countries controlled their public debt around 40-50% of GDP, especially, Indonesia had a very low public debt ratio, at 25% of GDP. Although the ratios of public debt to GDP of Viet Nam were still below the threshold of 90%, which was calculated by Reinhart, C. M., Reinhart, V. R. and Rogoff, K. S. (2012), this threshold was calculated for countries with developed financial markets. In developing countries such as Viet Nam, the optimum ratio could be much lower.

Figure 1: Public debt/GDP ratio (%)



Source: Government Report no. 221/BC-CP on May 18th, 2015 and Trading economics

Public debt is mainly Government debt

Government debt accounted for the relatively steady rate in gross public debt, about 79% in a 2010-2013 period (BTC, 2014). This percentage tends to increase slightly, partly because Government has restricted the guaranteed loans since 2013 with Decision No. 689/QD-TTg. The Government wants to reduce the burden of debt which increased rapidly in a long period, but was not used for the right purpose. Nevertheless, loans guaranteed by Government increased significantly from 226 trillion VND in 2010 to 452 trillion VND in 2014. not only to fund national key projects, government-guaranteed loans were also supposed to be largely used for "restructuring the domestic debt and external debt of general companies and state

[2]Due to differences between Viet Nam's pubic debt calculation and the world's, we compared official data of Vietnamese public debt with government debt (including bonds, bills and bilateral government or government-guaranteed loans) data of other regional countries.

own groups, and government-guaranteed debt of VDB and VBSP" (Ngọc Lan, 2014). For example, in 2013, Viet Nam issued government-guaranteed bonds to restructure the foreign loan worth $600 million of Vinashin. This might have been going on in 2014.

Table 2. Public debt by source, 2010-2014 (billion VND)

	2010	2011	2012	2013	2014	2015
Government debt	889,389	1,092,761	1,279,484	1,515,968	1,922,721	2,340,574
(yoy growth rate)		(↑23%)	(↑17%)	(↑18%)	(↑27%)	(↑22%)
% gross public debt	79.7%	79.1%	78.9%	79.3%	81.0%	82.5%
Government-guaranteed debt	225,953	288,375	343,099	396,113	451,806	496,986
(yoy growth rate)		(↑28%)	(↑19%)	(↑15%)	(↑14%)	(↑10%)
% gross public debt	20.3%	20.9%	21.1%	20.7%	19.0%	17.5%

Source: MOF (2014), authors' calculation for 2014 and 2015.

Domestic debt is greater than external debt

The share of domestic debt in gross public debt tended to increase from 44.4% in 2010 to 54.5% in 2014. This partly stemmed from the drop in credit demand in this period. The lower credit demand caused redundant capital in banking system, leading to the issuance of Government bonds with lower interest rates. Because of the large share of domestic debt, risks of public debt crisis has not been dangerous though the public debt to GDP ratio has already been relatively high. Nevertheless, domestic debt also caused negative impacts on the economy such as raising interest rates, narrowing capital flows for private sector, and inflationary pressures.

Remarkably, the trend in public debt structure might be reversed in the next period when credit demand recovers and issuance of domestic bonds becomes less attractive. Recently, Government proposed issuances of international bonds worth 3 billion USD in total to restructure domestic debts during a 2015-2016 period.

Table 3. Public debt structure, 2010-2014 (% of gross public debt)

	2010	2011	2012	2013	2014	2015*
Domestic debt	44.4%	43.3%	45.9%	50.2%	54.5%	58%
External debt	55.6%	56.7%	54.1%	49.8%	45.5%	42%

Source: MOF (2014) and (*) author's calculation

Another characteristic which could reduce the risks of debt crisis in Viet Nam is that the external debt mainly came from ODA. Foreign bonds only accounted for approximately 6% of total external debt in 2013 (Table 4). ODA loans are usually funds in long periods at low interest rates, thus, payment pressure is lower than international bond issuances.

Table 4. Selected government debt indicators, 2010-2014 (% GDP)

	2010	2011	2012	2013	2014
Domestic government bond	13.5%	12.7%	15.4%	16.5%	21.76%
Domestic government debt	16.6%	15.3%	17.0%	21.0%	-
Foreign government bond	2.3%	2.0%	1.5%	1.3%	0.8%
External government debt	24.6%	24.0%	22.4%	21.3%	-

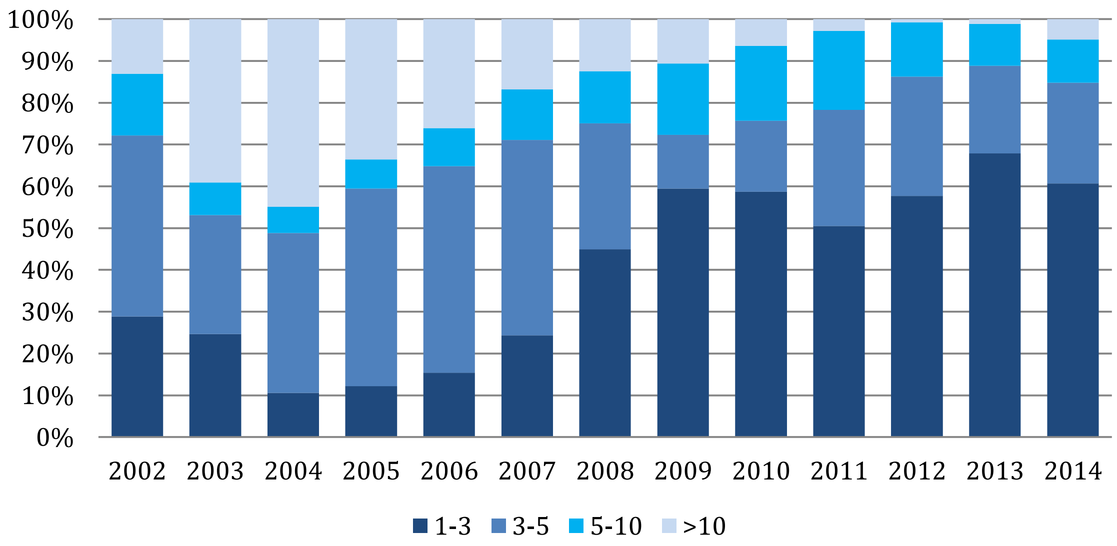
Source: ADB (2015), BTC (2014).

Huge pressure on debt payment due to short-term domestic bonds

Due to the underdevelopment of the financial market and macroeconomic risks, government bonds were primarily issued in under 5-year maturities. Average maturity of newly issued bonds was 2.97 years in 2012. After that, long-term bonds were promoted to be issued more, however, short-term bonds still accounted for 60% of total government bonds, 25% were medium-term bonds, and 15% were long-term bonds at the end of 2014 (Figure 2).

Facing with this problem, National Assembly issued Resolution No. 78/2014/QH13 to limit government bonds under 5-year maturities from 2015. However, the demand for long-term bonds is still very low. The rate of government bond issuance was lower than the plan in which Ministry of Finance would implement the goal of increasing the average maturity up to 6.8 years in 2014 (Table 5).

Figure 2. Government bonds by remaining time to maturity date (% total outstanding)



Source: ADB Bonds (2015)

Table 5. Selected indicators of Government bond issuance

	2012	2013	2014	2015*
Volume (trillion VND)	144	182	330	250*
Average interest rate	9.8%	7.79%	6.62%	
Average maturity (year)	2.97	3.21	4.85	6.8*

Source: Phương Nhi (2015). Data for 2015 relied on government bond issuance plan (MOF)

The principal amount was 62.6 trillion VND, in which 62.5 trillion VND was paid from state budget in 2010. By 2013, total principal amount doubled (125.8 trillion VND), while the budgetary expenditure for this payment just reached 55.6 trillion VND. Therefore, the volume of rollover was 70.2 trillion VND in 2013 (Table 6) and was expanded to 77 trillion VND in 2014[3]. The primary reason is that majority of bonds have been issued in a very short maturity since 2009, from 1 to 3 years. The maturity dates of these bonds have been starting in 2011; therefore, total principal payment has increased rapidly. The appearance of some kinds of short-term bills (3-6 month of maturity) also increased the amount of principal payment.

Table 6: Public debt payment using budgetary expenditure, 2010-2014 (bil. VND)

		2010	2011	2012	2013	2014[a]	2015[b]
Debt payment from budgetary expenditure	Principle	62,516	63,440	55,405	55,570	50,691	*65,060*
	Interest	25,400	29,786	39,884	*48,130*	*68,059*	*83,410*
	Total	**87,916**	**93,226**	**98,850**	**109,654**	***118,750***	***148,470***
Debt service payment	Principle	62,602	78,450	110,548	125,818		
	Interest	24,503	32,184	43,837	59,996		
	Total	**87,105**	**110,634**	**154,386**	**185,814**		
Payment obligation	Direct payments/ Budget revenue	17.6%	15.6%	14.6%	15.2%	*13.8%*	*16,1%*
Interest payment/Budget revenue		4,3%	4.1%	5.4%	6.5%	8.0%	9.2%
Interest payment/Budget expenditure		3,2%	4.2%	5.1%	5.2%	6.7%	7.7%

Note: a –Estimation for year 2014 (1st time). b -plan for 2015

Source: authors' calculation CEIC database and MOF (2014)

Besides, interest payment also accounted for a large proportion of budget expenditure. Compared to total expenditure, interest payment increased rapidly, from 3.2% in 2010 to 6.7% in 2013. In terms of volume, interest payment increased by 2.6 times in a 2010-2014 period. The payment was only lower than education expenditure (17.3%),

[3] Press release on the Government meeting, October, 2014 (http://vpcp.chinhphu.vn/Home/Thong-cao-bao-chi-cua-Phien-hop-Chinh-phu-thuong-ky-thang-102014-ve-no-cong/201410/14700.vgp accessed 02/08/2015)

pension and social securities (10.8%), and general public administration (9.7%), but dominated other kinds of current expenditure. Expenditure for interest payment was often at a high level, forecasted up to 9.2% in 2015. This is eroding the budget for development investment, as a direct result of high public debt ratio.

Conclusion and policy recommendations

In this policy discussion note, we analysed the differences between Viet Nam's public debt calculation and international standards. Basically, Vietnamese current statistics on public debt does not incur risks from extra-budgetary units/accounts and social security funds. We recommend that it is necessary for public debt statistics in Viet Nam to meet international standards in order to control the risks of public debt.

Because of large share of domestic debt, the risk of sovereign debt crisis has not been theoretically dangerous. However, domestic public debt also caused certainly negative impacts on the economy such as raising interest rates, affecting on private investment, and inflationary pressures in medium-term.

It is more important that we believe the negative impacts of public debt should be basically understood as the cumulative risks of undisciplined fiscal policy and inefficient public investment. The public debt ceiling should be considered as a tight constraint in order to enhance efficiency of fiscal policy, besides the meaning of safety threshold to prevent a debt crisis in the future. For this reason, maintaining the fixed public debt ceiling is necessary to control medium-term risks. Rather than lifting the debt ceiling, we suggest to implement the strong measures to bring and maintain public debt at an acceptable threshold.

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Disclosure appendix

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