TAKING STOCK

An Update on Vietnam's Recent Economic Developments

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ACRONYMS AND ABBREVIATIONS

ASEAN	Association of Southeast Asian Nations
CIEM	Central Institute for Economic Management
FDI	Foreign Direct Investment
GDC	General Department of Customs
GDP	Gross Domestic Product
GSO	General Statistics Office
IMF	International Monetary Fund
MOF	Ministry of Finance
MPI	Ministry of Planning and Investment
NPL	Non-Performing Loan
SOCB	State-Owned Commercial Bank
VASS	Vietnam Academy of Social Sciences

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SUMMARY

In late 2007 and early 2008, Vietnam was confronted with the economic overheating resulting from massive capital inflows. Attempts to sterilize these inflows were not able to prevent a boom in banking credit, an acceleration of inflation, a ballooning trade deficit and asset price bubbles. A determined reaction by the government from March 2008 onwards succeeded in stabilizing the economy and reducing the trade deficit to manageable levels. In the second half of 2008, the financial crisis originating in the United States affected foreign demand. The international prices of commodities exported by Vietnam were on a declining trend since the third quarter, export orders for garments and other industrial products collapsed in the fourth quarter, and a slowdown in manufacturing became noticeable. The government reacted swiftly to this second economic shock, shifting gear from stabilization to supporting economic activity in November 2008. Subsequent stimulus measures prevented a collapse of economic activity and might have put the economy on a recovery track.

Nevertheless, 2009 remains a very challenging year. While GDP growth most probably bottomed out in the first quarter, and could pick up in the second half of the year, it will remain several percentage points below Vietnam's potential. On the social front, open unemployment may not have been as large as initially feared, but job losses were common among casual and seasonal workers, and cuts in wages and overtime affected even those who kept their jobs. A good year in agriculture and the recovery in the construction sector may not be enough to offset the impacts. The recovery is also starting to exert pressure on the trade balance, which can be expected to deteriorate in the second half of 2009. Meanwhile, credit is growing rapidly again. Combined with the bottoming out of commodity prices, this may require paying attention to inflation pressures once more. The interest rate subsidy scheme, which played an important role in the initial phase of the stimulus policy, has lost its justification now that credit is flowing again, and could bring back the inefficiencies associated with policy lending. The "143 trillion VND" stimulus package being discussed by the National Assembly may result in a budget deficit that is too large compared with the financing resources available.

With the worst having been avoided and the economy displaying signs of recovery, the question is in which direction to go now. In March 2008, when the government adopted the "eight groups of measures", and in November 2008, at the time of the "five groups of measures", there was a very good reading of the economic situation by the government. Once the figures for the first half of 2009 become available, it might be good to pause and reflect whether sustaining economic activity should remain the single priority, or rather a new balance between the stimulation and stabilization objectives should be established. This macroeconomic debate should not relegate to the backburner the structural reforms which are required to sustain long-term growth and the social measures to mitigate the adverse impacts of economic fluctuations.

THE INTERNATIONAL CONTEXT

The global economic environment deteriorated dramatically over the last year. What began as a collapse of the U.S. sub-prime mortgage market quickly spread through the financial system and turned into one of the sharpest global economic recessions in modern history. The global contraction is affecting both advanced and developing countries (Table 1). Most high-income countries are in deep recession this year with their Gross Domestic Product (GDP) falling on average by 4.5 percent. Among developing economies GDP should ease from 5.8 percent growth in 2008 to 1.2 percent in 2009. Given the weight of industrial countries in worldwide economic activity, global GDP is expected to contract by 3.1 percent. The volume of world trade in goods and services is expected to drop 6.1 percent, with a significantly shaper contraction in the trade volume of manufactured products. Foreign Direct Investment (FDI) inflows are estimated to fall by a third, compared to last year.

Table 1: Global Growth Forecasts

	2008/e	2009/f	2010/f	2011/f
GDP growth				
World	1.9	-3.1	2.0	3.3
High-income countries	0.7	-4.5	1.3	2.4
Euro Area	0.6	-4.5	0.5	1.9
Japan	-0.7	-8.5	1.0	2.0
United States	1.1	-3.0	1.8	2.5
Developing countries	5.8	1.2	4.3	6.0
China	9.0	6.5	7.5	9.5
India	5.5	4.0	7.0	8.0
Russia	5.6	-7.0	3.0	3.5
Exports				
World trade volume	3.6	-9.6	3.8	6.9

Source: World Bank, May 2009

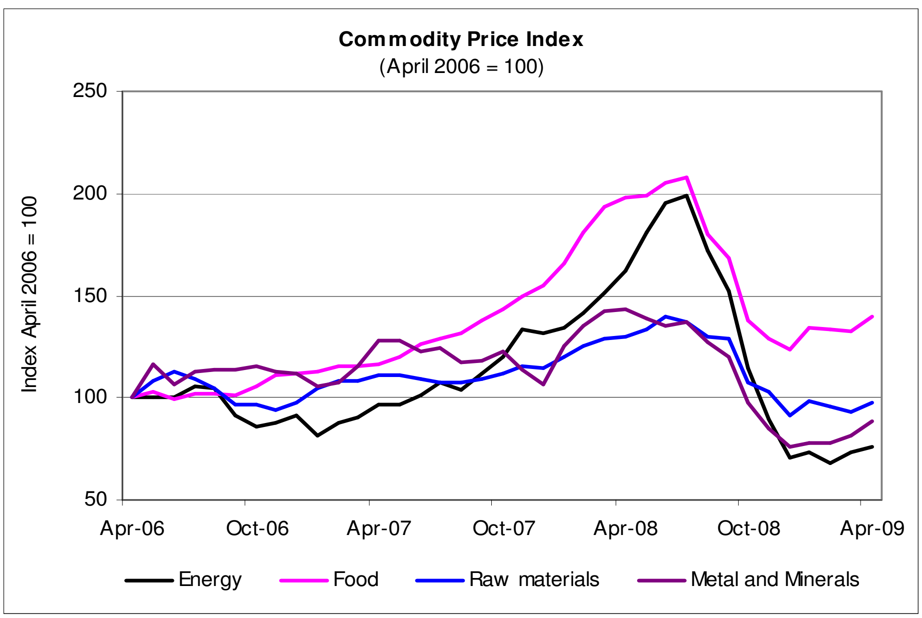
The East Asia region cannot be immune to a shock of this magnitude. But interestingly, there are important disparities (Table 2). High-income countries in East Asia are suffering the most severe contraction in the industrial world. This may be due to their particular insertion in the global economy. Some are trading hubs or major transshipment centers; others are major exporters of capital goods and electronics. At the other end, some countries in East Asia, as well as India, seem to be coping with the crisis better than the average. These countries are exposed to international trade to different degrees, but they have in common their large population, which may increase the effectiveness of domestic stimulus policies.

Table 2: Quarterly GDP Growth of Selected Countries

	Q1-08	Q2-08	Q3-08	Q4-08	Q1-09/e
Hong Kong	7.3	4.3	1.7	-2.5	-7.8
Japan	3.4	-3.5	-2.5	-14.4	-15.2
Singapore	6.7	2.5	0.0	-4.2	-10.1
Malaysia	7.4	6.7	4.7	0.1	-6.2
Thailand	6.0	5.3	3.9	-4.3	-7.1
China	10.6	10.1	9.0	6.8	6.1
India	8.4	8.8	7.9	7.6	5.3
Indonesia	6.2	6.4	6.4	5.2	4.4
Vietnam	7.5	5.7	6.3	5.7	3.1

Source: World Bank. Growth rates are over the same quarter in the previous year.

Figure 1: World Commodity Prices

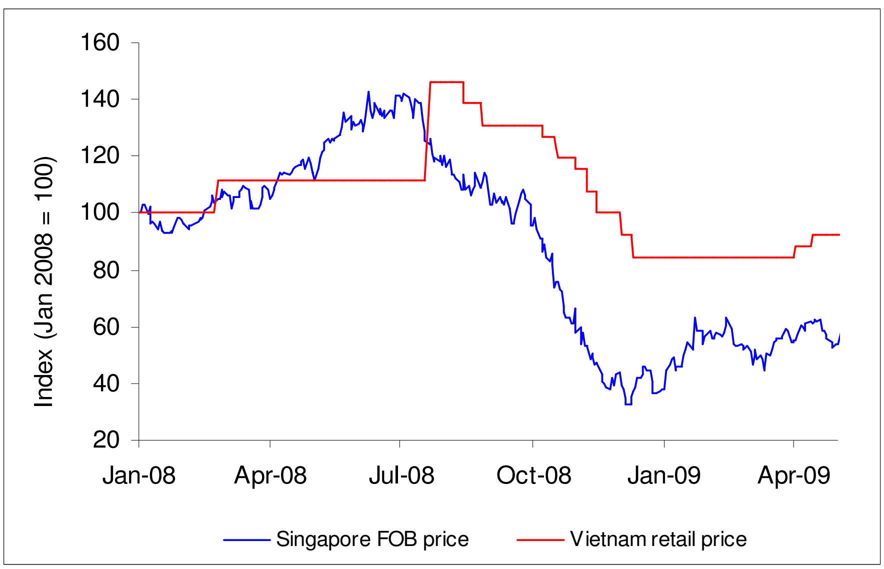


Source: World Bank.

One of the most direct channels through which the global crisis has affected Vietnam has been a precipitous drop in commodity prices (Figure 1). After years on an upward trend, and after a surge during 2007 and part of 2008, the prices of energy, food, raw materials and minerals collapsed in the second half of 2008. In some cases, prices declined by three fourths between the summer and the end of the year. This development was bound to have an impact on a country like Vietnam, which is still to a large extent an exporter of commodities. On the positive side, the fall in food prices led to an ease in inflation rates, whereas the fall in the prices of cement and steel has helped the construction sector rebound.

Commodity prices stabilized in the first quarter of 2008, and have more recently been on a recovery path. This upward trend is very clear in the case of oil (Figure 2). After reaching 147 U.S. Dollars per barrel in mid-July 2008, the international price of oil collapsed to 34 U.S. Dollars in mid-February 2009. Vietnam's balance of payments is less affected than other countries by these swings, as its export turnover from crude oil is not too different from its import turnover from gasoline. However, with about 16.4 percent of government revenue coming from oil, the impact on public finance is considerable. The budget plan for 2009 was prepared under the assumption of oil prices at an average of 70 U.S. Dollars per barrel. At 40 U.S. Dollars a barrel, the loss in revenue would have amounted to roughly 27 trillion VND, or roughly 1.5 percent of GDP. But the current oil price is around 60 U.S. Dollars per barrel, and is expected to increase further in the second half of 2009, thus mitigating the fiscal impact.

Figure 2: International versus Domestic Retail Price of Gasoline



Source: Singapore export FOB price is based on the U.S. Department of Energy

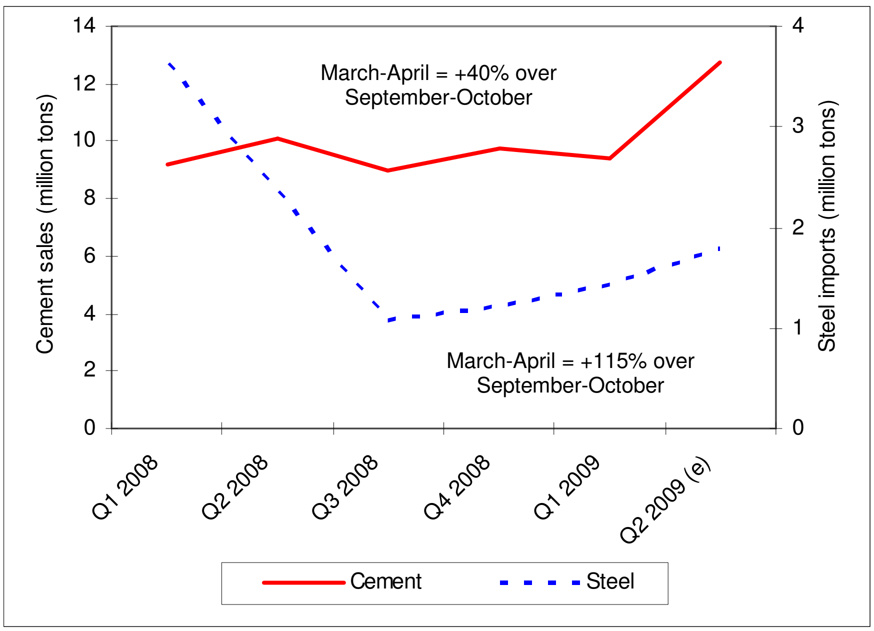
TRENDS IN ECONOMIC ACTIVITY

The global crisis has led to a noticeable slowdown of economic growth in Vietnam. The impact was severe in the first quarter of 2009, when GDP increased by 3.1 percent compared to the same period in 2008. This is more than 4 percentage points below potential (the average for first quarter growth over the last few years has been 7.2

percent). From this perspective, Vietnam may seem to be faring worse than the average developing country. But this is deceiving. The first quarter of 2008 was the peak of the overheating, so that the 3.1 percent growth rate is computed over a quarter with an exceptionally strong performance. Over the rest of the year the comparison will be with weaker quarters in 2008 and this should mechanically increase the growth rate of GDP for 2009 as a whole.

The first quarter of 2009 was also abnormally weak due to heavy rains in the North of the country, leading to an apparent stagnation of agricultural output. In reality, the output of winter-spring rice harvest of the North increased by an encouraging 44.7 percent compared to 2008. Growth in volume was negligible in volume in the South, but there is an ongoing shift to high-quality rice which should be reflected in higher prices. The livestock population has increased by 7 percent year on year, and total output by fisheries is expected to expand by 4.4 percent in 2009. Overall, GDP in agriculture may grow by 3.6 percent for the year as a whole, and given the weight of the sector in total economic activity, this should boost total GDP growth by about 0.6 percentage points compared to the first quarter.

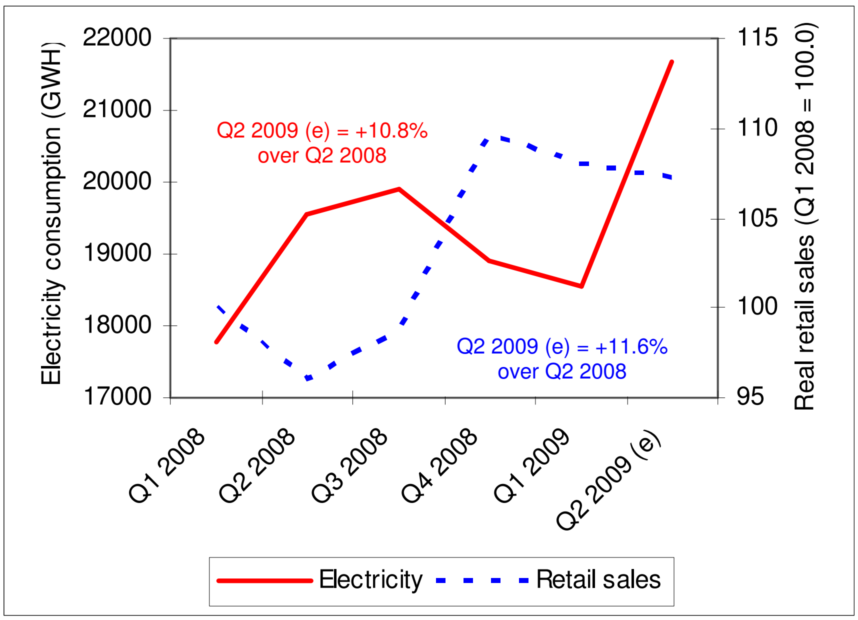
Figure 3: Strong Rebound of Construction



Source: General Statistics Office (GSO) and World Bank estimates

However, the recovery will most probably be led by the construction sector. In 2008, the bursting of the real estate bubble, the escalation of interest rates resulting from the stabilization policy and skyrocketing prices for cement and steel, had led to a decline in the GDP of the construction sector. The figure was modest in absolute terms (0.4 percent) but it was the first time it was negative since the very beginning of the East Asian crisis, a decade ago. Helped by much lower interest rates and a sharp fall in the prices of cement and steel, the construction sector is clearly bouncing back. In the first quarter of 2009, its GDP grew by 6.9 percent. Data on cement sales in the domestic market, and on steel imports, point out to a dramatic increase in construction activity compared to six months ago (Figure 3). On current trends, a strong growth rate can be expected for the sector in 2009. This should also boost results compared to the first quarter.

Figure 4: Resilient Activity in Other Sectors



Source: GSO and World Bank estimates

Other sectors appear to be doing better as well. Electricity consumption increases with household purchasing power and with manufacturing activity, but is not directly influenced by developments in the construction sector. Compared to one year earlier, it had grown by 10.8 percent in the second quarter of 2009. This is below historic rates, but not by a large margin. At 11.6 percent, the growth rate is quite similar for retail sales measured in real terms. This variable does not bear a direct relation with developments in the construction sector either. The retail sales series is somewhat less reliable, as it needs to be deflated by a consumer price and over the last year there was considerable macroeconomic turbulence, making the estimated growth rate sensitive to the price index and the deflation approach used. However, regardless of the approach, growth in real retail sales is substantial (Figure 4). This is confirmed by independent bits of information. For instance, in May 2009 production of air conditioning units increased by 56 percent compared to May 2008. The production of refrigerators grew by 23 percent and that of washing machines by 32 percent.

The main concern is obviously export performance. Commentators often point out that exports account for 70 percent of Vietnam's GDP, implying that their decline could have a devastating effect. This mechanical formulation is misleading, as exports are measured in terms of the value of final products whereas GDP is measured in terms of domestic value added. For instance, the export turnover of rice is similar to that of electronic products, but the domestic value added component of the former is much higher than that of the latter, given the weight of imported inputs. If the export turnover of rice increased by the same percentage as the export turnover of electronic products declined, total export turnover would remain roughly unchanged. However, the domestic value added of exports would increase. Unfortunately, there are no readily available series measuring changes in the domestic value added of exports.

Figures based on export turnover indicate that the impact of the global crisis was large, but not as large as in other countries in the region (Table 3). However, composition effects matter in this case as well. During the first quarter of 2009 Vietnam exported around 2.5 billion U.S. Dollars in gold. This is after being the biggest importer of gold in the world in 2008. In both cases, what was at stake was speculation and portfolio reallocation. The gold rush of 2008 was partly associated with concerns about macroeconomic instability. As those concerns receded, and investment opportunities arose in construction and in the stock market, households sold part of their holdings, artificially inflating export turnover. If gold is excluded, exports declined by 11.6 percent in the first quarter of 2009, which is still better than in other countries in the region, but by a smaller margin.

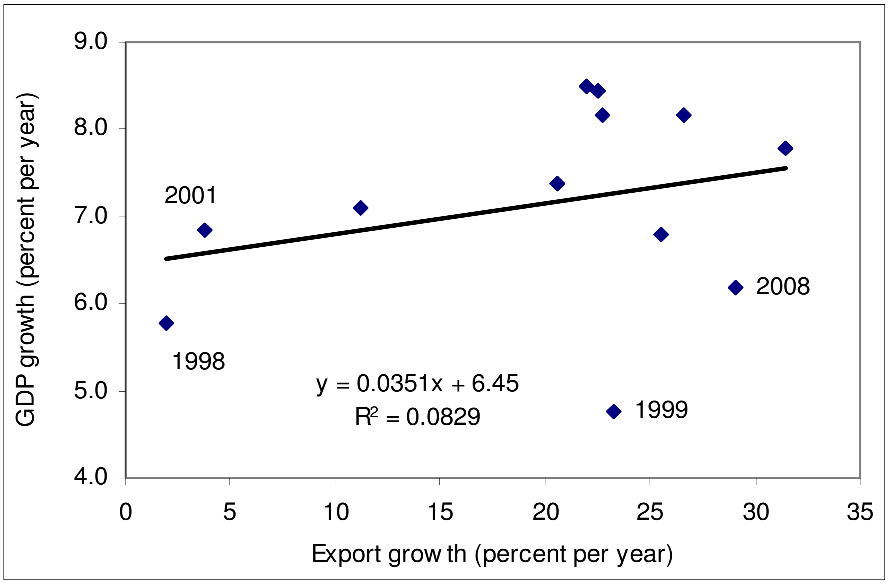
Table 3: Exports Hold Better than Elsewhere

	2007	2008	Q1-2009
Japan	10.0	9.5	-60.0
Philippines	7.1	-2.9	-36.8
Indonesia	13.2	20.0	-32.0
Malaysia	9.7	13.3	-28.9
Korea	14.1	13.8	-24.9
Thailand	16.5	15.7	-23.2
Singapore	10.1	12.9	-20.6
China	25.7	17.3	-19.7
Vietnam	21.9	29.1	7.4

Source: World Bank, General Department of Customs (GDC), and GSO

The question is then how much the deceleration or decline in export turnover will affect GDP growth in 2009. The answer critically depends on what will happen to other components of aggregate demand, hence on the effectiveness of the stimulus package. If the experience of previous years can serve as guidance, the impact can be substantially dampened. Over the last decade, there have been years with dismal growth in exports turnover, but still a decent performance in terms of GDP growth, and years with solid growth in exports turnover but relatively low GDP growth rates (Figure 5).

Figure 5: The Impact from Exports is not Mechanical



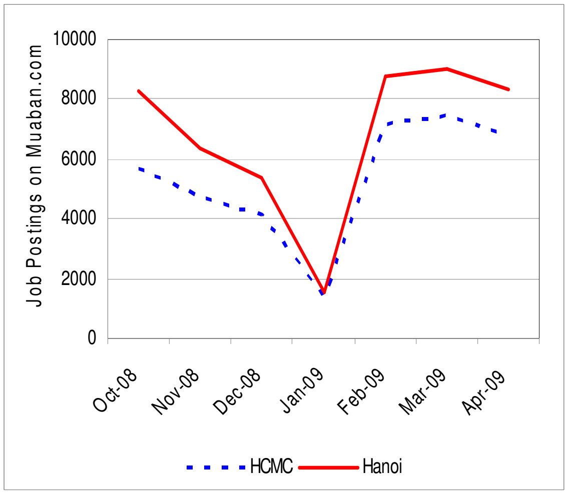
Source: GSO and World Bank estimates

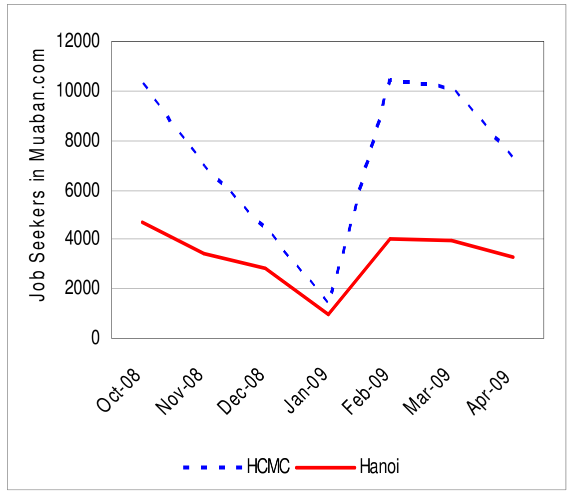
THE SOCIAL IMPACT OF THE SLOWDOWN

Assessing the social impact of the growth slowdown is difficult in the absence of a reliable and timely labor force survey. There is abundant anecdotal evidence of increased hardship, especially in industrial parks and in handicraft villages. But the plural of anecdote is not data, and some of the figures on job losses reported by local authorities, business associations and civil society organizations do not appear to be entirely reliable. A systematic effort to compile evidence from various sources suggests a more mixed picture than is generally accepted. Overall, it appears that underemployment has been more common than open unemployment. There are also disparities across various segments of the labor market and a clear heterogeneity of impacts across enterprises and across provinces.

Based on electronic advertisements in a popular website, the market for semi-skilled and skilled workers recovered well after the Tet break (Figure 6). Until then, there was a noticeable drop in both job offers by employers and job seeking ads by individuals. But both series bounced back strongly in March 2009. By April, there were more job offers and fewer job seeking ads than in October 2008. The change in the relative number of job offers and job seeking ads suggests a gradual tightening of the labor market for the semi-skilled and the skilled in recent months (Figure 7).

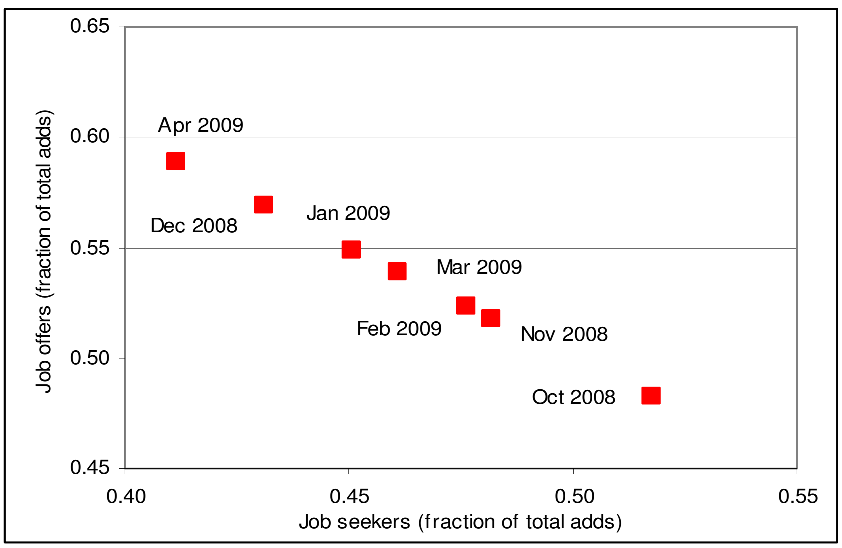
Figure 6: Job Offers and Job Seekers in Urban Markets





Source: World Bank, based on data from muaban.com.

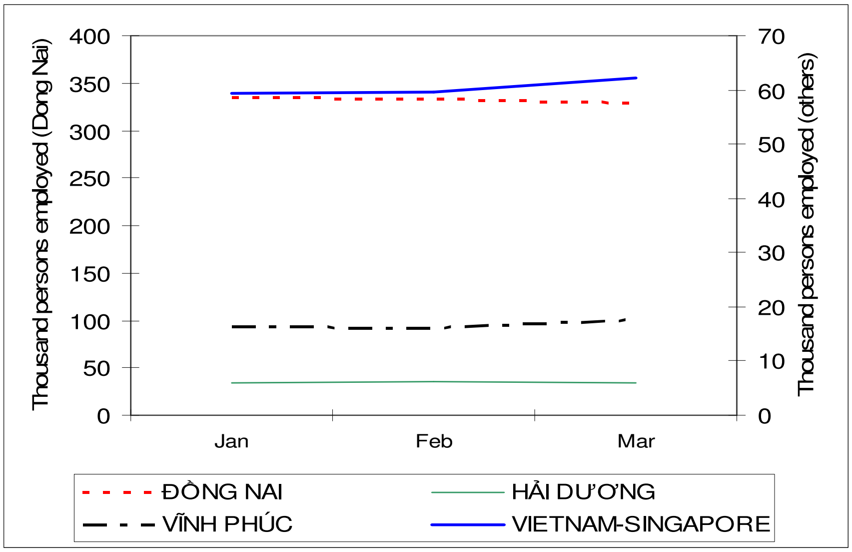
Figure 7: A Rudimentary Beveridge Curve



Source: World Bank, based on data from muaban.com.

The overall picture is altogether different in industrial parks, where the work force is generally less skilled. Industrial parks serve as the platform for a large share of manufacturing exports, so that they should feel the impact of the global crisis more directly than the rest of the economy. An ongoing survey aimed at strengthening their monitoring, conducted by the Central Institute for Economic Management (CIEM) with support from the World Bank, is informative in this respect. Aggregate data at the industrial park level, available for the Dong Nai, Hai Duong and Vinh Phuc provinces, as well as for the Vietnam-Singapore Industrial Park, suggest a stability of total employment (Figure 8). However, the employment figures reported to CIEM are likely to be based on workers registered with social security, and not to include casual and seasonal workers. There are grounds to believe that this is the group that suffered most.

Figure 8: Deceiving Employment Stability in Industrial Parks



Source: CIEM (2009; work in progress).

Even for the group of workers captured in the CIEM report, disaggregated data indicates more heterogeneity in impacts at the enterprise level than suggested by the aggregates. By May 2009, survey response rates at the enterprise level had exceeded one quarter in Hai Phong (59 percent), Hai Duong (65 percent), Vinh Phuc (81 percent), and Ba Ria Vung Tau (26 percent). Those responses reveal that a majority of enterprises is doing relatively well, but a significant minority has been adversely hit (Table 4). Similarly, there is a considerable diversity across provinces. Some of them, like Ba Ria-Vung Tau, seem relatively immune to the slowdown whereas others, such as Hai Phong, appear to be much more severely impacted (Table 5).

Table 4: Diverse Impacts across Enterprises

Variable	Down by more than 10 percent	Down by less than 10 percent	Stable	Up by less than 10 percent	Up by more than 10 percent	Total
Turnover	10.3	10.3	4.4	23.5	51.5	100
Exports	20.6	6.4	7.9	15.9	49.2	100
Imports	25.0	5.4	5.4	5.4	58.9	100
Domestic sales	13.7	3.9	11.8	15.7	54.9	100
Taxes	2.5	0.0	5.0	20.0	72.5	100
Employment	1.8	31.6	10.5	28.1	28.1	100

Source: CIEM (2009; work in progress).

Table 5: Diverse Impacts across Provinces

Province	Down by more than 10 percent	Down by less than 10 percent	Stable	Up by less than 10 percent	Up by more than 10 percent	Total
Hai Phong	0.0	45.0	15.0	20.0	20.0	100
Vinh Phuc	0.0	30.8	0.0	38.5	30.8	100
Hai Duong	10.0	30.0	20.0	30.0	10.0	100
Ba Ria-VungTau	0.0	14.3	7.1	28.6	50.0	100

Source: CIEM (2009; work in progress). The table is based on changes in employment.

Perhaps the biggest diversity of impacts is among individual workers and households. The most reliable information in this respect comes from a rapid impact assessment exercise conducted by the Vietnamese Academy of Social Sciences (VASS), with support from the World Bank and participation by civil society organizations. Rapid impact assessments take the form of structured focus group discussions with workers. They were conducted in Hanoi's spot labor markets (chợ lao động), in handicraft villages and in one industrial park in February and March 2009, and in several other industrial parks and in rural areas in April 2009.

These rapid assessments are too rich to be summarized under the form of just a few stylized facts. However, several patterns emerge. On the positive side, major adverse effects such as falling into poverty, facing food shortages, having to pull children out of school or to sell land, or becoming homeless, were relatively uncommon. On the negative side, there were numerous job losses, frequent reductions in working hours and wages, reduced remittances, and more reliance on informal sector jobs.

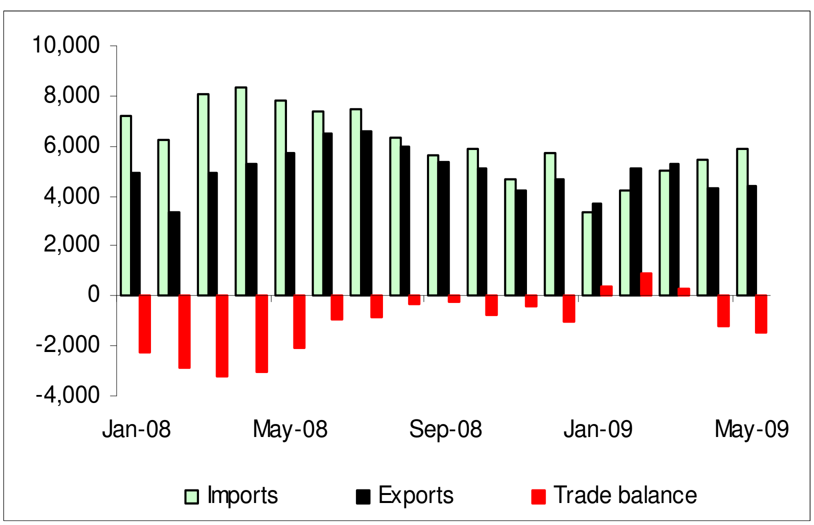
Job losses were widespread in industrial parks in late 2008 and early 2009. But few took the form of open layoffs. Non-renewals of contracts and incentives for voluntary departures were more common. Job losses were frequent among seasonal workers, and those on short-term contracts. Many enterprises in industrial parks noted difficulties in complying with social insurance and the new system of unemployment insurance. Even in the enterprises that reported a recovery in production, workers were often offered regular hours and shifts only, with no overtime. Lack or scarcity of overtime pay forced workers to cut on expenses, especially in Ho Chi Minh City and surrounding areas, due to the high cost of living. Remittances to families staying in rural areas suffered as a result. But permanent return to rural areas was less common than anecdotes suggest, as if the migration process was irreversible by now. Those who did return faced more difficulties than is generally acknowledged.

THE BALANCE OF PAYMENTS

In 2008 the deficit of the current account of the balance of payments had reached 11.9 percent of GDP, above any reasonable comfort level. This was to a large extent due to an unusually large trade imbalance, close to 2.3 billion U.S. Dollars per month in the first quarter of the year. In reality, the deficit was not as unsustainable as the figures suggest. In Vietnam, FDI inflows are associated with large imports of capital goods; because the inflows were massive, the import turnover was unusually large too. But in this case, imports and the resources to finance them go together. Another important component of imports is the purchase of intermediate inputs by export processing activities. In this case, current imports are paid for by future exports. However, the trade deficit of early 2008 was dramatically amplified by a surge in imports of consumption goods, including luxury goods such as cosmetics and expensive cars.

In a way, because of the stabilization policies of 2008, the Vietnamese economy is in a better position to weather the global crisis than it would have been a year earlier. At the beginning of 2009, the balance of trade was roughly in equilibrium. Over the first quarter of 2009, exports had increased or decreased modestly compared to the same period in 2008; depending on whether gold is included or excluded. Meanwhile, imports had declined by roughly 41.3 percent (Figure 9). In part, their decline reflected a more active trade policy, possibly at the limits of what WTO commitments allow. But it was also the result of deeper macroeconomic forces. The drop in FDI inflows, the decline in export demand and the slowdown in economic growth did all contribute to the fall in key components of import turnover.

Figure 9: A more Manageable Trade Deficit



Source: GSO

As economic activity start to recover, some reversal of the trend is already noticeable in trade data for April and May. Import turnover has started to pick up again, and the trade deficit can be expected to widen during the remaining of 2009. But the same fundamental reasons that prevented the 2008 deficit from becoming unsustainable should be at play in 2009.

Meanwhile, export turnover is down across most items (Table 6). The only positive note concerns rice, with sales abroad up by 20 percent compared to the previous year. Given that many rice farmers are close to the poverty line, the good performance of the sector should help mitigate adverse social impacts from the slowdown. Other results are mixed at best. For instance, it is interesting to see that the sharp decline in exports of footwear is not matched by a similar decline in the case of garments. Given that many of those involved in seafood production are poor or near-poor, it is also encouraging to see that seafood exports have not declined as much as those of other sectors.

Table 6: Export Values Fall for Most Items

	2008 (US$ million)	Growth (in percent, year on year)		
		2008	5M-2008	5M-2009
Total export earnings	62,685	29.1	27.2	-6.8
Crude oil	10,357	22.0	45.5	-44.0
Non-oil	52,328	30.6	23.5	1.8
Rice	2,894	94.3	94.1	20.2
Other agricultural commodities	5,505	17.2	4.0	-19.5
Seafood	4,510	19.8	11.6	-9.1
Coal	1,388	38.8	34.9	-20.7
Garment	9,120	17.7	19.0	-1.8
Footwear	4,768	19.4	13.4	-10.1
Electronics and computers	2,638	22.5	25.2	-8.0
Handicraft (including gold)	1,363	65.1	3.2	772.6
Wood products	2,829	17.7	20.8	-19.8
Other	17,312	44.3	32.9	-12.2

Source: GSO

Export turnover is down for most of Vietnam's traditional markets (Table 6). In 2008, the United States, the European Union, Japan, China and the Association of Southeast Asian Nations (ASEAN) accounted together for more than three fourths of sales abroad. In the first quarter of 2009, exports to all these markets had declined, some times substantially. But total non-oil exports declined by substantially less, due to the rapid growth in sales to the rest of the world. Vietnamese exporters have been especially active trying to win markets over in Latin America and the Middle East. As a consequence of this dynamism, in the first quarter of 2009, export turnover to these two regions had grown by nearly 14 percent compared to the same period in 2008.

Table 7: Traditional Export Markets Are Down

	2006	2007	2008	Q1-2009
China	8.3	7.7	7.5	6.3
Japan	14.3	12.6	12.2	9.6
ASEAN	11.6	12.5	14.0	10.7
EU	21.1	21.4	19.4	16.6
US	21.3	23.2	20.8	17.5
Rest of the World	23.3	22.5	26.1	39.1

Source: GSO. Share of Vietnam non-oil exports by main market.

Less information is available at this point on other key components of the balance of payments. It is expected that remittances will decline, although by how much is controversial. In other East Asian countries, remittances originate in migrant workers who support the consumption of the families they left behind. Many of those migrants are seeing their livelihoods at risk in the current global crisis, and remittances can be expected to suffer accordingly. In Vietnam, on the other hand, remittances are to a large extent associated with an ageing overseas community which is relatively prosperous and is by now investing back in the country, some times in connection with retirement plans. Therefore, the inflow of remittances could decline by less than in other countries in the region.

Some information is available on FDI projects, although its presentation is not fully consistent with the measurement criteria used when constructing the balance of payments. In Vietnam, FDI approvals reflect mainly an intention by a foreign investor, or the taking of an option on land. FDI implementation captures actual spending, combining both capital inflows from abroad and the mobilization of domestic resources (for instance, under the form of borrowing from local commercial banks). However, from a balance of payments perspective, it is only the inflows from abroad that matter. FDI implementation figures are thus closer to the balance of payments measure than FDI approvals. But they are still higher.

The data available as of May 2009 show that FDI approvals have declined by an astounding three quarters (Table 8). This is a combination of a near collapse in the number of new projects, and some expansion in the capital of existing projects. Anecdotal evidence suggests that FDI enterprises already operating in Vietnam, much the same as domestic investors, are taking advantage of low interest rates and low construction costs to charge ahead with expansions that were planned anyway. Because of this, implemented FDI has declined by much less than approved FDI. However, not all the implemented FDI is bound to show as inflows in the balance of payments. FDI projects operating locally may be borrowing from local banks, which should reduce their reliance on funding from abroad.

Table 8: New FDI Projects Down, Old Ones Up

	Amount (US$ billion)	Change (percent, yoy)
Approved capital	6.7	-76.3
Newly registered projects	2.7	-89.2
Number of projects	256	-60.5
Capital increased from existing projects	4.0	27.5
Implemented capital	2.8	-29.1

Source: The Ministry of Planning and Investment (MPI). Data accumulated figures, January 1 to May 20, 2009.

Patchy information on remittances, FDI inflows and other international capital movements makes it difficult to produce a reliable forecast of the balance of payments. However, based on the available information, a current account deficit in the order of 5 percent of GDP is not unrealistic. On the capital account side, apart from the expected decline in FDI inflows, it is worth mentioning the massive capital outflow expected for the year as whole. Most (if not all) of this outflow took place earlier in 2009, as foreign investors were selling their government bonds and trying to liquidate their stock market shares. Given how "thin" financial markets in Vietnam are, foreign investors ended up selling their assets for far less than they had paid in the first place.

Table 9: A Large Current Account Deficit

US$ million	2009/e
Current account balance	-4,622
Trade balance	-5,552
Non-factor services	-595
Investment income	-3,275
Transfers	4,800
Financial account balance	1,950
FDI investment	4,500
Medium and long-term loans	1,450
Other capital	-4,000
Overall balance	-2,672
Change in reserves (- increases)	2,672
Current account as percent of GDP	-5.0

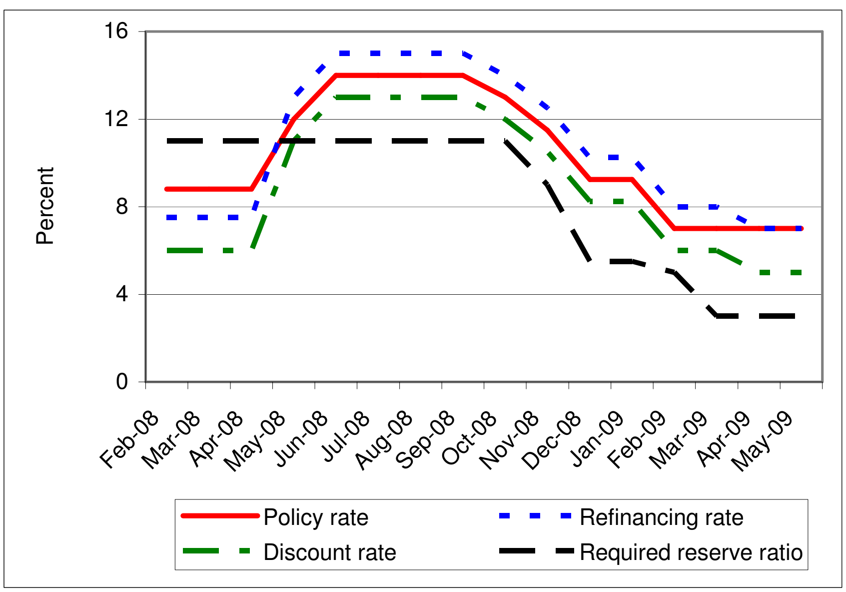
Source: World Bank estimates

THE FINANCIAL SECTOR

Banks' excessively cautious stance towards risk, and the associated drying up of credit, were among the reasons why the downturn was so severe in industrial countries in late 2008 and early 2009. The main problem then was not a lack of liquidity, as the central banks of those countries had massively injected money into their economies. The problem was rather the fact that banks were channeling their liquidity towards safe placements such as government bonds, or simply sitting on their money. In Vietnam there was barely any growth in credit in the first few months of 2009, but at least there was no contraction. As in industrial countries, the State Bank of Vietnam (SBV) greatly relaxed monetary policy from November onwards, confirming a trend cautiously initiated in June. But the first phase of the interest rate subsidy scheme might have played a more important role in keeping credit flowing during the first quarter of 2009.

Monetary policy was loosened through a combination of measures. Among them were reductions in key policy rates and cuts in the required reserve ratio (Figure 10). The SBV also purchased back the large compulsory bond it had placed in March 2008, when the priority was to address the overheating of the economy. The impact of these measures on monetary aggregates was enhanced through further moves towards a more flexible exchange rate. The flotation band for the dollar was widened to +/-5 percent in March 2009, from +/-3 percent in November 2008, +/-2 percent in June and barely +/-1 percent in March. These moves followed a 3 percent devaluation of the reference exchange rate in December 2008.

Figure 10: A Relaxation of Monetary Policy

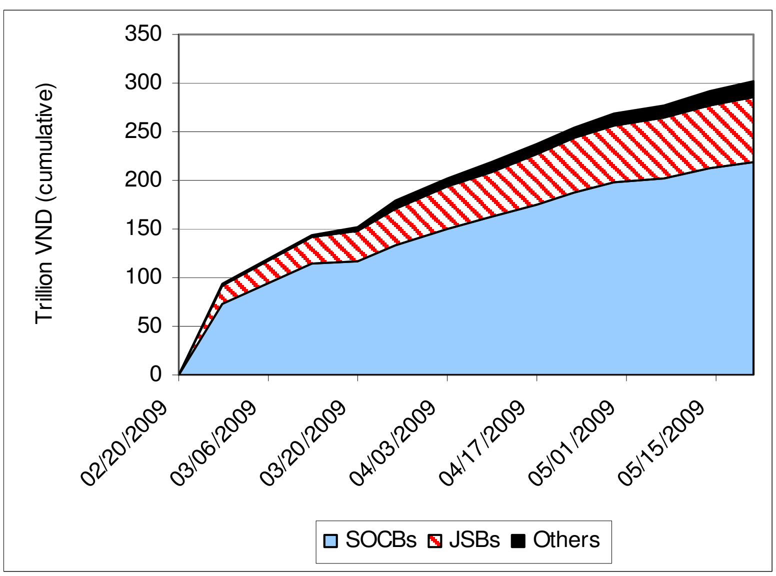


Source: SBV.

The first phase of the interest rate subsidy scheme, in turn, amounted to a large-scale refinancing of enterprise debts. Re-financing was not formally allowed by the scheme, whose explicit aim was to provide funding for working capital to enterprises with viable plans. The subsidy offered was 4 percentage points, and it could not last for more than nine months. In practice, however, borrowing for working capital allowed enterprises to use their turnover to pay back debts they had contracted when interest rates were very high, in some cases as high as 21 percent. With the rapid disinflation that took place in the second half of 2008, those debts had become exceedingly burdensome, raising the prospect of a rapid increase in the share of non-performing loans (NPLs) and potentially affecting the stability of the banking system.

Because the first phase of the interest rate subsidy scheme was associated with a massive restructuring of debts, total credit did not grow much during the first quarter of 2009. Loans benefitting from the scheme amounted to roughly 200 trillion VND by end-March 2009, but total outstanding loans grew by only 6 percent since the end of 2008 (Figure 11). By end-May, state-owned commercial banks (SOCBs) were responsible for 72 percent of the credit issued under the scheme, suggesting an element of moral suasion in the banks' decision to participate. But suasion was probably less relevant in the case of borrowers, as the private sector accounted for a remarkable 79 percent of the lending volume.

Figure 11: Lending under the Interest Rate Subsidy Scheme

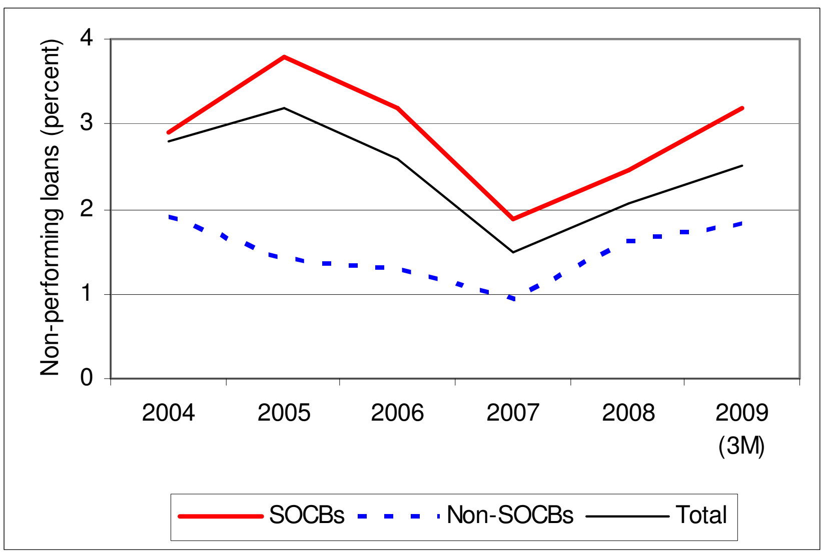


Source: SBV.

Re-financing enterprise debts contracted at high interest rates has been common in rapid disinflation episodes. In the mid-1980s, a salient feature of so-called "heterodox" stabilization packages, such as those adopted by Argentina and Israel, was to reduce the interest rates of outstanding loans administratively, so as to avoid massive bankruptcies. The Vietnamese subsidy scheme was in a way better than those administrative measures. There was no blanket reduction of interest rates: in order to apply to subsidized credit, enterprises needed to have a viable business plan. This might have limited the rolling over of loans in the case of enterprises which were bound to fail anyway. On the banks' side, the subsidy only benefitted them if they actually lent under the scheme. And this was a probably a way to keep credit flowing at a time when the natural instinct of banks could have been to simply sit on their money and wait, as they did in industrial countries.

In April 2009 the interest rate subsidy scheme was extended, from working capital to investments and from nine months to two years. The justification of this second phase of the subsidy scheme is more questionable. Banking credit was flowing again by then. More importantly, subsidizing investments has much in common with "policy lending", which had been taken out of commercial banks into specialized financial institutions several years ago, as part of a broader effort to reform the financial sector. Policy lending is vulnerable to favoritism, may result in an inefficient allocation of resources and could eventually affect the quality of bank portfolios.

Figure 12: Non-Performing Loans Increase Again

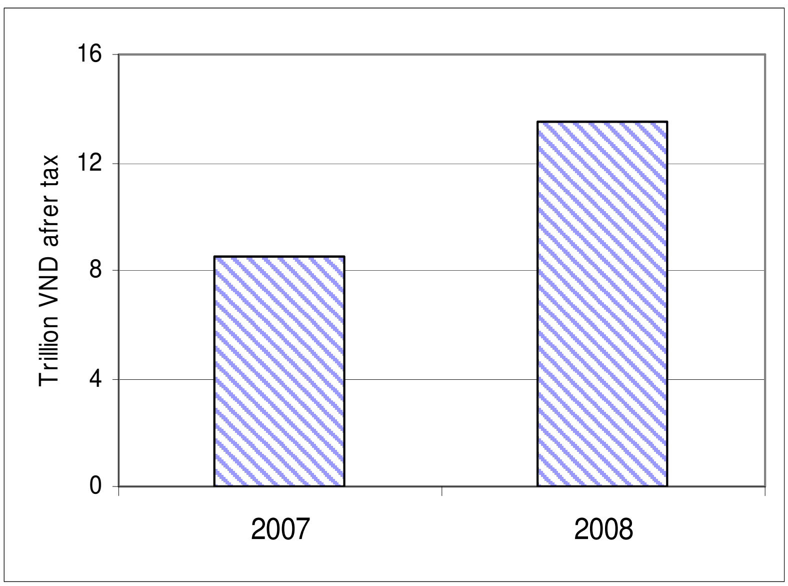


Source: SBV.

There are already some indications of an increase in the share of NPLs (Figure 12). They come after several years during which the efforts by SOCBs to clean up their portfolios in preparation for equitization had resulted in an overall improvement in the quality of lending. In the aftermath of a determined stabilization program and a global crisis, some deterioration in the quality of loans could be expected. The available NPL estimates rely on quantitative indicators. Specifically, a loan is classified as an NPL if it has been rolled over or its service is overdue by 90 days or more. More reliable figures would require assessing the solvability of borrowers. But those assessments are difficult to make in a country whose market institutions are still being developed. Higher figures are mentioned by rating agencies; for instance, Fitch recently estimated the share of NPLs at 13 percent. But quantitative estimates like those compiled by SBV at least provide some comparability over time.

Despite the increase in the share of NPLs, the banking sector of Vietnam remains in relatively good health. In 2008 the profitability of banks was generally good, reflecting relatively low credit costs and a strong growth in the volume of lending. Profitability was also boosted by sizeable capital gains on government bonds, which many banks purchased when foreign investors fled Vietnam in the first half of 2008, at a time when interest rates were high. These capital gains offset the impact of relatively low net interest margins (Figure 13). In 2009, the profitability of the banking system can be expected to benefit from the interest rate subsidy scheme.

Figure 13: Improved Bank Profits

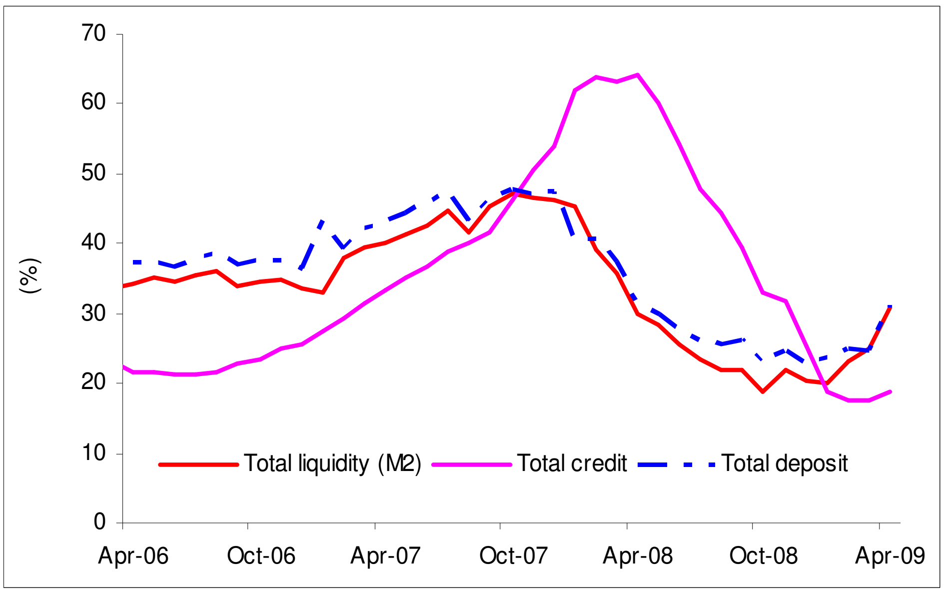


Source: World Bank, based on data from 25 commercial banks.

The relatively good health of the banking system is also the result of an active stance by monetary authorities. During the stabilization phase, when the bursting of the real estate bubble and high interest rates prompted concerns about the situation of smaller banks, the SBV upgraded its supervision efforts considerably and raised minimum capital requirements. By the end of 2008 all commercial banks, including the nine small joint stock banks that seemed most vulnerable, had met the new requirements. This process is bound to continue, with the minimum charter capital set at 3 trillion VND by end 2009. Banks which fail to meet this requirement will be forced to merge with larger banks, or will have their business licenses revoked. In preparation for this possibility, SBV has already drafted a circular on bank mergers and acquisitions.

The loosening of monetary policy and the second phase of the interest rate subsidy scheme are by now leading to rapid growth in key monetary aggregates (Figure 14). So far, this is not resulting in an acceleration of inflation. If anything, the stabilization program of early 2008 and the collapse of commodity prices later in the year have brought all standard inflation indicators down (Figure 15). In May, the consumer price index rose by only 0.44 percent on month, or 5.6 percent on year. Single-digit figures for annual inflation are at hand for 2009, confirming the success of the government's approach to stabilization. But price stability should not be taken for granted. As monetary aggregates are growing again, and commodity prices have most probably bottomed out, inflation may start picking up again in the second half of 2009.

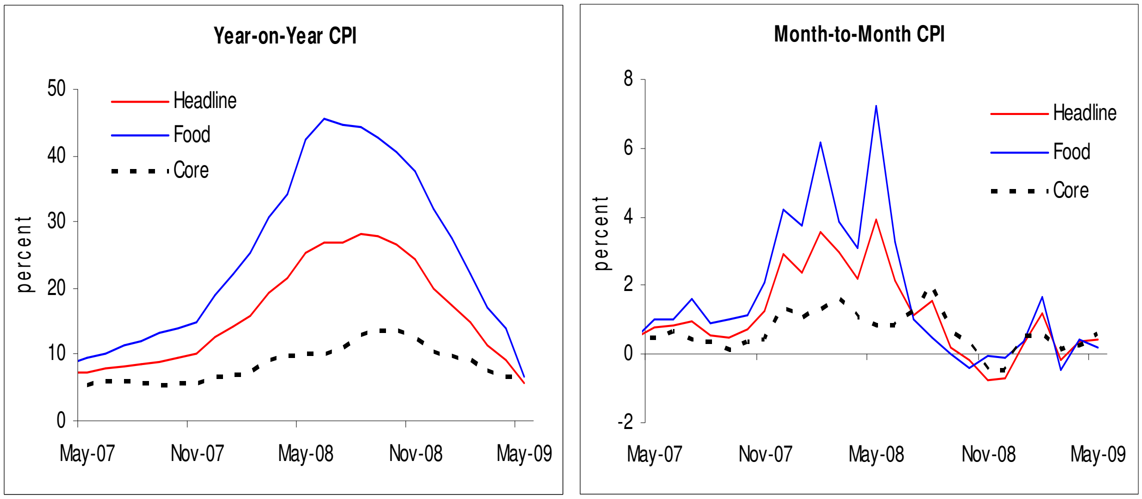
Figure 14: The End of the Stabilization Phase



Source: IMF and World Bank estimates based on SBV data.

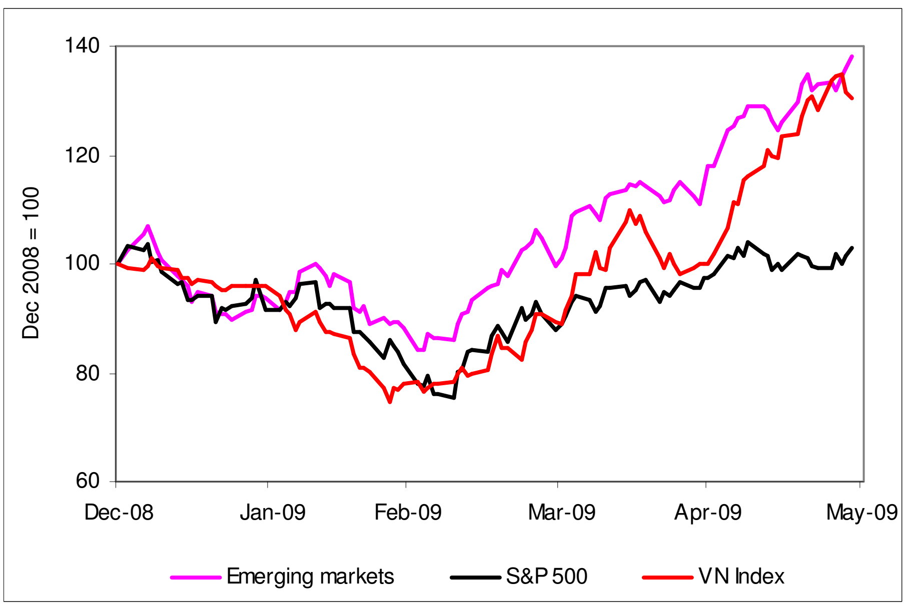
Upward pressures are also apparent in the stock market. Due to the small size of the float portion of shares and the limited volume of transactions, share prices are highly sensitive to market sentiment in Vietnam. The stabilization program of early 2008, with its impact on credit and economic activity, had led to a dramatic decline in the VN Index. The trend was reinforced by share sales by foreign investors. As a result of all these forces, Vietnam had the worst performing stock market in the world in 2008, with the VN Index falling by an astounding 67.3 percent. In 2009, a looser monetary policy and more upbeat expectations on economic activity are leading to a reversal of the trend. As of end-May 2009, the VN index had gained 81 percent since it bottomed out in February 2009, and 35 percent since the beginning of the year, making the stock market of Vietnam the best performing in the world (Figure 16). While this recovery is a welcome development and opens up the possibility to revitalize the equitization process, it also raises concerns about its sustainability.

Figure 15: Inflation Down to Single Digits



Source: GSO and World Bank Estimates

Figure 16: A Strong Stock Market Rebound



Source: HOSE, MSCI and Standard and Poor's

THE STIMULUS PACKAGE

Sustaining economic growth during the remaining of 2009 will require a stronger reliance on domestic demand. In line with policy responses elsewhere, the budget plan that was adopted by the National Assembly at the end of 2008, in the wake of "the five groups of measures", already entailed a substantial increase in the overall budget deficit. But other stimulus policies were adopted in early 2009 and yet others are being considered for approval at present.

Based on international criteria, the planned deficit for 2009 reached 8.3 percent of GDP, against 4.5 percent in 2008. These figures are not strictly comparable to those discussed in Vietnam's public debate, for several reasons. First, under international criteria, "off-budget" items are to be included in the estimation of the deficit. In Vietnam's case, some of those items are "off-budget" only in name, as they are subject to the same approval procedures and the same public financial management rules as "on-budget" items. Other "off-budget" items, such as spending funded by the Vietnam Development Bank, are more quasi-fiscal in nature. Second, Vietnam treats the amortization of public debt as government expenditure, whereas the international practice is to consider it as a financing item (actually, as a reduction in the available financing). Last but not least, the estimate depends of the GDP forecast for the year, and in times of turbulence different organizations have different views in this respect.

With all these caveats in mind, increasing the overall budget deficit from 4.5 to 8.3 percent of GDP reflects a clearly expansionary stance. Admittedly, the expected change in the overall budget deficit is only a rudimentary measure of the size of the stimulus package. The economic slowdown, by itself, creates the illusion of an expansion. This is because tax revenue is highly dependent on GDP growth, implying that deficits are mechanically larger during economic downturns. Still, based on the simple budget deficit metric, the budget plan of late 2008 put the Vietnamese stimulus package in the top tier of the regional comparison (Table 10).

Table 10: Stimulus Packages across Countries

Country	Percent of GDP
China	12.0
Malaysia	9.3
Singapore	8.0
Philippines	1.8
Korea	6.8
Thailand	1.1
Vietnam	8.3

Source: National authorities, Bloomberg, Factiva and World Bank.

Since then, several additional stimulus polices were adopted or announced, creating some confusion and prompting understandable concern about potentially unsustainable government spending. A series of measures were adopted in the first quarter of 2009. For the sake of clarity, in what follows they are identified as "first round of measures". Subsequently, several other measures were submitted for consideration to line ministries or, more recently, to the National Assembly. Many of those measures, together with all those already adopted in the first quarter of 2009, were regrouped by MPI into a single, comprehensive document popularly know as the "143 trillion VND plan".

Given that 143 trillion VND amounts to roughly 8.7 percent of the expected GDP for 2009, the MPI plan has led to considerable anxiety. Adding 8.7 percent of GDP to the overall budget deficit of 8.3 percent implied by the budget plan approved in late 2008 yields 17 percent. If this were correct, the stimulus package of Vietnam would be in a altogether different league compared to those of other countries. It is therefore important to have clarity as to what has been approved already, what is under consideration by line ministries and by the National Assembly, and what are the financing implications of the policy decisions that will be made in the coming weeks.

Table 11: Costing the First Round of Measures

Stimulus package components approved or committed so far	
Revenue item	**Trillion VND**
• Reduction of CIT for small and medium enterprises, from Q4-2008 to Q4-2009, both inclusive	3.0
• Deferred CIT payment for six subsectors during nine months of 2009. Revenue is not foregone	(7.3)
• Deferred PIT payment during five months of 2009. Revenue is not foregone	(6.1)
• 50 percent reduction in VAT payments for selected goods and sectors, including imports	7.2
Total revenue foregone	10.2
Expenditure item	**Trillion VND**
• Subsidized interest rate scheme, two phases combined. SBV to bear the cost for now, although it may eventually impact on the budget	(17.0)
• Additional off-budget spending	8.0
• Tet bonus (200,000 VND per poor person, up to 1,000,000 VND per poor household). Based on actual spending	1.7
• Support to 61 poorest districts (each of the provinces to receive an advance of 25 billion VND)	1.5
• Housing support for the poor (around 0.5 million rural households to receive 7.2 million VND each)	3.6
• Support for low income civil servants (about 0.9 million civil servants to receive 360,000 VND each)	0.4
Total additional expenditure	15.2

Source: Based on data from the International Monetary Fund (IMF), the Ministry of Finance (MOF), and SBV. Figures are in parentheses indicate deferred (as opposed to foregone) revenue or expenditures not falling on the budget.

Before undertaking this exercise, it is important to emphasize several points. First, the "143 trillion VND plan" contains a considerable amount of duplication. Some of the items listed in it were part of the first round of measures; others were included in the budget plan approved in late 2008. Second, the "143 trillion VND plan" combines measures resulting in lower tax revenue with measures leading to higher spending and measures aiming at raising more resources. While adding the contribution of the first two to the budget deficit makes sense, the third set of measures represents a financing item, not a source of additional deficits. Last but not least, some of the measures included in the "143 trillion VND plan" certainly have a cost to society, but it is not clear that their cost will fall on the 2009 budget.

The first round of measures included a series of exemptions and deferrals of tax payments. Only the former should be considered when assessing the budget implications, as the latter are going to be paid by households and enterprises, only a few months later. However, it is worth noting that the government has proposed to the National Assembly to exempt the PIT payments deferred for the first six months of this year. Deferred CIT payments could also result in a revenue loss this year. If these payments were only collected in 2010, they should be recorded as a reduction in revenue too, since these resources would not be available to cover expenditures in this year. The first round of measures also included the interest rate subsidy scheme. Initially, there was considerably uncertainty regarding the cost of this scheme; gradually, the debate has shifted to who should bear it. For now, it is clear that it will fall on SBV's shoulders and will not be directly paid for by the budget. However, depending on how it is financed by SBV it could become a fiscal liability in the next months or years. Last but not least, the first round of measures included additional off-budget spending and a series of social spending items. Taken altogether, these measures amount to a loss of revenue by roughly 10.2 trillion VND and additional spending by about 15.2 trillion (Table 11).

Assessing the "143 trillion VND plan" is more demanding due to the only partially detailed way in which it is presented. Therefore, different commentators may come to different interpretations of it, and all those interpretations should be taken with a dose of caution. It seems clear that the "143 trillion VND plan" does not entail any additional loss of revenue compared to the first round of measures. It may however imply an increase of 43.3 trillion VND in government expenditures, compared to the first round of measures. And it foresees an additional 31.1 trillion in financing (Table 12).

CAN IT BE AFFORDED AND HOW?

Vietnam has some fiscal space to finance a fiscal stimulus package. A debt sustainability analysis completed after the budget plan for 2009 was announced suggests that the country's position is robust, even taking the global financial crisis into account. The total public debt, external and domestic, was estimated to stand at 47.5 percent of GDP at end of 2008. Nearly two-thirds of this debt is on highly concessional terms. Stress tests show that the main risks for debt management would be a large (30 percent) and sustained depreciation of the VND, and an unexpected large borrowing by Government on non-concessional terms, two shocks which seem unlikely at this point. In spite of the large increase in the overall budget deficit implied by the budget plan for 2009, public debt was expected to peak at 50.7 percent of GDP by 2012.

Table 12: What is Additional in the "143 Trillion VND" Plan?

Stimulus package components in the "US$8 billion" MPI plan (figures in trillion VND)		
Revenue item	**MPI**	**World Bank**
• Combination of measures related to rebates and payment delays on CIT, PIT and VAT. Already included in the first phase of the stimulus package	28.0	(10.2)
Total revenue foregone	28.0	0.0
Expenditure item	**MPI**	**World Bank**
• Advancing the implementation of critically important projects from 2010. In practice, resources will be reallocated from projects with poor implementation	37.2	14.9
• Subsidized interest rate schemes, two phases combined. Already included in the first phase of the stimulus package	17.0	(17.0)
• Other spending, mainly on social safety net, including the Tet bonus. Already included in the first phase of the stimulus package	7.2	(7.2)
• Investments to be financed on revenue brought forward from the 2008 budget. However, 14.1 trillion VND in carry-overs were already included in the November 2008 budget plan	22.5	8.4
• Issuance of additional off-budget domestic bonds. However, only 20 trillion VND are to finance additional expenditure. The other 7.7 trillion represent additional finance	27.7	20.0
Total additional expenditures	83.9	43.3
Financing item	**MPI**	**World Bank**
• Suspending the recovery of advances made in 2008 for investments not implemented. This amounts to an authorization to draw upon deposits	3.4	3.4
• Issuance of additional off-budget domestic bonds for investment	27.7	27.7
Total additional financing	31.1	31.1

Source: Based on data from IMF, MOF, and SBV. Figures in parentheses were not part of the first round of measures or did not fall on the budget

The main constraint to support the active fiscal stance of the government stems from finance rather than from debt sustainability. The budget plan for 2009 foresaw the issuance of a second sovereign bond, which is unlikely in the current global context. On the positive side, tax revenue forecasts are now higher than they were at end-2008, Meanwhile the first round of measures already approved and the additional measures for consideration which were included in the “143 trillion VND plan” amount, combined, to 10.2 trillion VND in lost government revenue and 58.5 trillion VND in additional government spending. Therefore, if all the pending measures were approved, total financing needs would climb from 136.5 trillion VND in late 2008 to 197.1 trillion by mid-2009 (Table 13). This represents roughly 12.1 percent of GDP and the deficit could be even larger depending on how the interest rate subsidy scheme is financed.

Table 13: A Revised Budget Plan for 2009

Deficit according to budget plan as of November 2008	**Trillion VND**
a. Total revenue (tax, non-tax, and grants)	389.9
b. Total on-budget expenditure (recurrent and capital)	456.6
c. Other expenditure (VDB lending, ODA on-lending, off-budget investment)	69.8
d. Overall fiscal balance (=a-b-c)	-136.5
e. Overall balance in percent of GDP (depends on nominal GDP forecast)	-8.3
Adjustment to budget plan as of May 2009	**Trillion VND**
f. Change in estimated revenue (independent of stimulus package)	8.1
g. Revenue foregone (first round of stimulus measures)	10.2
h. Revenue foregone (second round of stimulus measures)	0.0
i. Additional spending (first round of stimulus measures)	15.2
j. Additional spending (second round of stimulus measures)	43.3
k. Adjusted overall fiscal balance (=d+f-g-h-i-j)	-197.1
l. Adjusted overall balance in percent of GDP	-12.0

Source: World Bank based on data from IMF, MOF, and SBV

While running a large stimulus program is a defensible response to the fall in export demand, an excessively large deficit could run the risk of crowding out the private sector more than supporting it. Equally important, a budget plan not including appropriate financing could end up affecting investor confidence. At present, if all the measures in the “143 trillion VND plan” were approved, the financing shortfall could amount to 29.5 trillion VND, or roughly 1.8 percent of GDP (Table 14).

In practice, Vietnam has often reconciled the availability of resources with financing needs through a pragmatic execution of the budget. One of the main remaining weaknesses of public financial management in Vietnam is actually the usually large gap between budget plan and budget execution. Government expenditure usually falls short of the plan due to implementation delays. On average, during the period 2004-2008 actual expenditures have been 18.9 percent lower than planned. Similarly, government revenue usually exceeds the plan, with the average gap during 2004-2008 amounting to

15.5 percent. Last but not least, bond issuances are often under-subscribed, and are some times completed in subsequent years.

Table 14: A Partial Financing Plan So Far

Budget plan as of November 2008	Trillion VND
a. Financing needs as of November 2008	136.5
b. Financing gap as of November 2008	0.0
Revised budget plan as of May 2009 if US$8 billion package is approved	**Trillion VND**
c. Financing needs as of May 2009	197.1
d. Additional financing sources as of May 2009	31.1
e. Financing gap as of May 2009 (=c-a-d)	29.5
f. Financing gap as of May 2009 (in percent of GDP)	1.8

Source: World Bank, based on data from IMF and MOF.

It should also be noted that the government of Vietnam keeps unusually large cash holdings, under the form of deposits in SOCBs. In industrial countries, governments do not tend to hold more than 1 percent of GDP in cash. But the government of Vietnam has about 86 trillion VND in bank deposits. In case of need, the balance could be brought down to about one month of government spending, or roughly 48 trillion VND. Therefore the problem is not so much to bridge a temporary gap as it is to mobilize the necessary resources to support the stimulus policy.

The real issues to address at this point are: how big the stimulus package should be, and how it should be financed? These are not trivial questions. At a time when there are clear signs of a recovery, and the period of low inflation and depressed asset markets may be ending, an excessively large budget deficit may not be warranted. And with markets still being uncertain, a stimulus package lacking adequate financing could create unnecessary anxiety. For all these reasons, the measures proposed in the "143 trillion VND plan" which are still up for approval should be considered with caution.

POLICIES LOOKING FORWARD

The government of Vietnam can be commended for its swift response to the global crisis of late 2008. The policy reaction was timely and determined, as had been the response to the overheating of late 2007 and early 2008. It is clear that sustaining economic activity in the face of a drop in exports requires supporting other components of aggregate demand. There is also consensus about the importance of fiscal policy to confront the global downturn. But engineering a substantial increase in public spending takes time, as shown by the still ongoing debates on the stimulus package, which may only translate into higher government spending later in 2009. From this perspective, in early 2009 it was urgent to respond with other tools. In retrospect, it appears that the government of Vietnam chose an effective mix through its first round of stimulus measures.

The rapid loosening of monetary policy, together with the first phase of the interest rate subsidy scheme and exemptions and deferrals of tax payments succeeded in preventing a more severe economic downturn. The first phase of the interest rate subsidy might have kept credit flowing to the economy, at a time when banks could have preferred to sit on their liquidity and avoid taking risks. It allowed the refinancing of enterprise debts contracted at very high interest rates, which could have led to numerous defaults in a context of rapid disinflation. And it boosted the profits of commercial banks, at a time when the deterioration in the quality of their portfolios and thin interest rate margins could have made them vulnerable.

Preventing a collapse in economic activity was also critical to mitigate the social impacts of the global crisis. Vietnam does not have modern social insurance mechanisms yet, and relying on cash transfers is fraught with implementation problems, as shown by the experience with the Tet bonus. From this perspective, sustaining job opportunities remains the most effective social policy response.

The economic developments of early 2009 also confirmed the resilience of the Vietnamese economy. While workers and households have undoubtedly suffered, macroeconomic performance was better than in many other countries, in the region and elsewhere. This performance owes to the stimulus policies adopted by the government, but it also reflects solid initial conditions. The demographic transition is rapidly expanding the working age population, and new entrants into the labor force tend to be more skilled than the average worker. Together with the exceptionally high investment rates of the last few years, this accumulation of factors of production leads to a substantial growth potential. The Vietnamese economy is also less vulnerable to massive insolvencies than those of other countries. Households do not hold much debt and enterprises are not highly leveraged. A flexible labor market mitigates impacts, as under-employment is more common than unemployment. And the Vietnamese have a remarkable entrepreneurial capacity, as shown by the rapid reorientation of exports towards new markets.

With the worst having been avoided and the economy displaying signs of recovery, the question is in which direction to go now. In March 2008, when the government adopted the "eight groups of measures", and in November 2008, at the time of the "five groups of measures", there was a very good reading of the economic situation by the government. Once the figures for the first half of 2009 become available, it might be good to pause and reflect whether sustaining economic activity should remain the single priority, or rather a new balance between the stimulation and stabilization objectives should be established.

For now, the debate around the "143 trillion VND plan" shows a continued determination to boost economic growth. However, there is a risk that several of the measures in it will only lead to an actual increase in public spending much later in the year, when commodity prices may already be higher and export demand might have bottomed out. There are also risks in embracing a stimulus package that is too large compared to the available financing resources. While the donor community is keen to help and bring more rapidly-disbursing ODA, there are constraints on how much domestic finance can be raised, as shown by the recent experience with bond issuances.

There are also indications that upward price pressures are resurfacing, both for goods and services and for assets. In an economy as open as the Vietnamese, increases in the international prices of food and oil have a very direct impact on the CPI. The stock market is also going through a strong rally. This has led to a self-reinforcing cycle of upbeat expectations, growing demand for shares, and an ever higher VN Index. The construction sector is clearly bouncing back. In a country where the urban population grows by about one million people per year, a construction boom could push property prices up again.

While striking the right balance between stimulus and stability becomes more pressing, the macroeconomic debate should not relegate other key policy reform agendas to the backburner. There is a need to support economic activity and to preserve stability, and the government should strike the right balance between them. But there are also key structural reforms which are required to sustain long-term growth. And more can be done on the social front, in order to identify and mitigate the adverse impacts of economic fluctuations. All these objectives can actually be reconciled under the form of a practical set of policy recommendations (Box 1).

Box 1: Some Practical Recommendations

- Phase out the interest rate subsidy scheme, especially for investments; clarify how the scheme will be financed.
- Avoid an excessively loose monetary stance, setting a target for credit growth that is consistent with price stability.
- Finalize the second round of the stimulus package, with emphasis on critically important investments and adequate financing.
- Improve the clarity of budget planning and narrow the gaps between budget plan and execution.
- Strengthen public investment processes, addressing the weaknesses exposed during the overheating phase.
- Speed up ODA disbursements, so as to support the stimulus package and shore up the balance of payments
- Improve the quality of banking supervision and the monitoring of international capital flows.
- Continue the reform of the public sector and revitalize the equitization of large enterprises and banks.
- Improve the monitoring of social impacts through the introduction of regular labor force surveys.
- Improve the quality of "poor households lists" and provide adequate funding for programs supporting the poor.