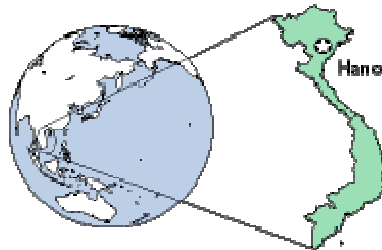


COUNTRY REVIEW

Vietnam



14 July 2011

ANALYST: David Atkinson

EULER HERMES COUNTRY RISK GRADE: D

EULER HERMES COUNTRY RISK LEVEL: HIGH

Country Risk Grades are on a scale of AA, A, BB, B, C, D

Country Risk Levels are on a scale of LOW, MEDIUM, SENSITIVE, HIGH

ECONOMIC STRUCTURE

Country Profile	
Capital city:	Hanoi
Population:	89.03 mn (2010)
GDP:	USD 104630 mn (2010)
Currency:	Dong (VND)
Form of state:	One Party State (Communist)
Head of government:	Prime minister Nguyen Tan Dung
Next elections:	July 2011 Presidential (indirect) May 2016 Legislative

Major Industries (% of GDP at market prices, 2009)	Global Assumptions	2010	2011	
Agriculture	22.0%	Real GDP grth (% yr/yr) *	3.3	2.9
Industry	39.3%	Inflation (% av) *	1.2	1.4
Manufacturing	20.3%	Dated Brent (USD/b)	80	110
Services	38.8%	* World		

Main Exports (% of total, 2010)	Main Imports (% of total, 2010)		
Textiles	15.6%	Machinery & equipment	16.1%
Crude oil & products	8.7%	Steel	7.3%
Shoes	7.1%	Petroleum	6.8%
Seafood	6.9%	Fabrics	6.4%
Electronics	5.0%	Electronics	6.2%

Basic indicators

Selected economic indicators	2008	2009	2010	2011f	2012f
Nominal GDP (USD mn)	87,470	92,440	104,630	112,290	128,330
Population (mn)	87.47	88.07	89.03	90.96	92.89
GDP per capita (USD)	1,000	1,050	1,175	1,234	1,382
Real GDP growth (% yr/yr)	6.2	5.3	6.8	5.5	5.8
Inflation (% eop)	20.0	6.5	11.8	15.5	8.0
Fiscal balance (% of GDP)	-1.2	-4.6	-2.8	-2.3	-2.3
Current account balance (% of GDP)	-12.3	-6.6	-3.8	-4.7	-4.4
External debt/GDP (%)	33	40	40	40	38
External debt/Exports of goods & services (%)	37	53	48	44	41
Interest payments/Exports of goods & services (%)	2	2	1	1	1
Foreign exchange reserves (USD mn)	23,890	16,447	12,467	12,220	12,000
Import cover (months)	3.4	2.7	1.7	1.4	1.2
Exchange rate assumption, COP:USD (av)	16,977	17,941	18,932	20,744	22,000
f: CRU central forecast					

Sources: National, IMF, World Bank, Euler Hermes

Political Stability

The Communist Party (CP) operates a one-party state where serious organised opposition is not permitted. The party dominates, with the government, military and bureaucracy all subordinate to it. The transition from a centrally planned to market-based economy (*Doi Moi*) begun in the late 1980s has made considerable progress, but favours gradualism over shock therapy in order to maintain one-party control.

It is not clear where the authorities see the ultimate limit of state-ownership, but there is an inherent tension between the continued incorporation of liberal economic policies and the maintenance of tight political control, which may become more apparent in the longer-term as real incomes rise further. Necessary change in the economic structure is likely to require an equally adaptive, evolutionary political structure to maintain stability, but the risk is that the leadership will put one-party control first and fail to keep pace with the demands of economic reality.

Effective power is vested in the 14 man politburo of the Communist Party Central Committee with a triumvirate of General Secretary of the Communist party, the President and the Prime Minister at its head. The 11th party congress in January 2011 re-appointed PM Nguyen Tran Dung, a move which points to policy continuity (economic liberalisation with a strong line on one-party control). General Secretary Nong Duc Manh and President Nguyen Minh Triet were replaced as they had reached retirement age. The new General Secretary is Nguyen Phu Trong. Truong Tan Sang, who was nominated as the next president, will be confirmed formally in a National Assembly vote on 25 July. Direct elections for the National Assembly were held in May 2011, which the Communist Party won with 458 of the 500 seats and 91.6% of the vote.

There is a regular dialogue with the IMF and other IFIs and a bilateral donor group provides ongoing financial support. However, the leadership is likely to be very reluctant to seek formal IMF support for their efforts to deal with current problems.

Internationally, relations with the US and China have improved in recent years (Vietnam has fought a war with both in the modern era), though there is scope for periodic tension with the US over human rights issues and with China over sovereignty issues. Vietnam is a member of the Association of South East Asian Nations (ASEAN).

Economic Stability

Overheating in 2007 and 2008, which necessitated policy tightening, was followed by the global financial crisis that threatened a sharp growth slowdown. The authorities, however, in responding to these swings have found it difficult to achieve a desired minimum growth rate without high inflation, exacerbated by two surges in global food prices, and pressure on the external balance. Policymaking has been erratic and largely reactive, lagging events, as growth has taken precedence. Consequently, with a managed exchange rate foreign exchange reserves have fallen to low levels and there have been successive exchange rate devaluations. Following the 11th party congress earlier this year policy measures have been taken to address the drain on foreign exchange reserves and there has been some progress. There is some risk, however, that, again fearing a too sharp slowdown in growth (and the social impact) the authorities will switch back too soon to expansionary policies.

Economic transition has followed a similar pattern to that of China—early liberalisation of agriculture followed by gradual reduction of the state's role in industry and finance. Shock treatment has been generally eschewed. Vietnam is classified as a lower-middle income by the World Bank. Annual average growth of real per capita GDP was a strong 5.5% during 2001-10, as real GDP grew by an annual average 7.3% in the same period. Total exports as a share of GDP have risen dramatically from 7% of GDP in 1986 to 68% in 2009. Industry and services are the main drivers of growth, reflecting expansion of the private sector. Oil output is declining, but remains an important source of export earnings (9%) and government revenues. Garments and footwear account for 23% of exports

Real GDP slowed from 8.5% in 2007 to 6.2% in 2008 and 5.3% in 2009, before recovering to 6.8% in 2010, as stimulatory fiscal and monetary policies boosted domestic demand. In H1 2011 growth slowed to 5.6% yr/yr and full year 2011 and 2012 are likely to be in the 5.5-6.0% range, though the risks are to the downside.

Inflation has been relatively high and volatile in recent years. Consumer prices accelerated to 22.2% yr/yr in July 2011, driven by strong credit growth, delayed withdrawal of stimulus measures, exchange rate devaluation and the surge in global food and energy prices. With prospectively more stable global food and commodity prices inflation should begin to ease, but could still be around 19% at end-2011 and relatively high in 2012, though the rate could dip below 10% by year-end.

The fiscal deficit widened to 4.8% of GDP in 2009 from 1.2% in 2008, based on Ministry of Finance data, as the authorities provided a fiscal stimulus and spending rose sharply as a proportion of GDP. In 2010 the deficit narrowed 2.9% of GDP. Based on World Bank and IMF figures, which include off-budget expenditures, however, the deficit was a much larger 9.0% of GDP in 2009 and 6.4% in 2010. Stabilisation measures introduced in early 2011, if fully implemented, would reduce the wider deficit to 3.9% of GDP according to World Bank and IMF projections.

Policy interest rates have been raised during H1 2011, with the refinancing rate rising from a recent low of 7% in October 2010 to 14%, but real interest rates remain negative. Also, another key rate, however, was cut in early July, which at best provides mixed signals on policy intentions. Reserve requirements have also been raised. Credit growth targets have also been lowered to 20% (39% and 33% respectively in 2009 and 2010) and the target for M2 is 15-16%. Data from the State Bank of Vietnam (central bank) suggest that growth was below target in H1 (7% over the six months to end-June). The exchange rate was devalued by 9.3% in February in 2011 and the trading range was narrowed to +/-1%, which followed a series of smaller devaluations in 2010.

The banking system remains opaque and state-owned banks still dominate, though the private sector is increasing. In its latest report to the Consultative Group the World Bank noted that "the asset quality of bank portfolios remain an ongoing concern". In late 2010 the state-owned Venashin shipping group defaulted, raising questions over lending to SOEs and the ability of the authorities to deal with potential problems, eroding confidence in the banking system.

The current account deficit ballooned to 12.3% of GDP in 2008 before narrowing to 6.6% in 2009 and 3.8% in 2010, as imports were constrained by lower domestic demand growth and devaluation. Exports fell in 2009 but recovered strongly in 2010. The past two months (June-July) have shown an improvement in the trade deficit, nevertheless, the current account deficit will probably be wider at 4.7% of GDP in 2011 overall, before narrowing slightly in 2012 (as a proportion of GDP). The current account deficit is more than fully covered by net FDI flows, though FDI has fallen and may not recover fully to previous levels. Despite this position, FX reserves fell from USD23.9bn at end-2008 to USD12.2bn in March 2011, providing cover of less than 1.5 months' imports and only 70-80% of external payments due in 2011-12. M2 is also relatively high compared with FX reserves. However, bi-lateral donor aid support has been strong and should be maintained if the authorities continue to adopt appropriate policies, but even though Vietnam has good technical support relations with the IFIs, it may be reluctant to go to the IMF unless it really has no alternative.

The ratio of external debt to GDP at 40% is relatively high, but external debt as a proportion of exports of goods and services is more moderate at 44% and interest payments at 1% of exports of goods and services are low.

Structural Business Environment

The Structural Business Environment is below average in our assessment.

Based on data and definitions from the World Bank's 2011 Doing Business Survey, Starting a Business, Closing a Business and Paying Taxes were weaker areas, ranking below average, and Protecting Investors was particularly weak. The World Bank Institute's Governance Research Indicator puts Regulatory Quality, Control of Corruption and Rule of Law all below average for the East Asia Region.

David Atkinson

London: +44 (0)20 7860 2807

Charts

