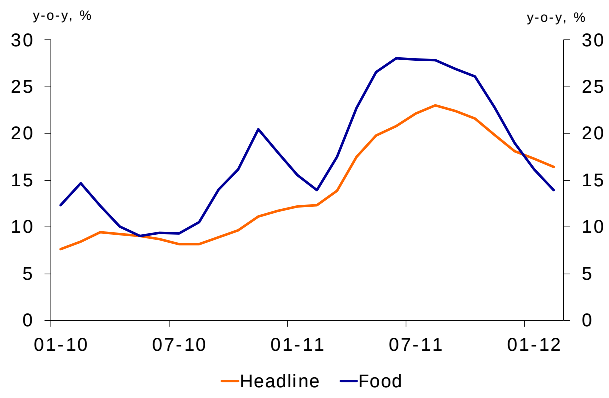
Macro Comment 12/20

Vietnam: Stay on course

After experiencing somewhat of an economic rollercoaster ride in 2011, inflation in Vietnam is finally easing. Nonetheless, Vietnam's economic situation remains vulnerable and the government should make sure it stays on course.

Inflation is easing



Source: Reuters EcoWin

The Vietnamese economy has been on a rollercoaster ride last year. Inflation rose rapidly, economic confidence fell to a low and the currency (dong) had to be devaluated to prevent a balance of payments crisis. This prompted the government to shift away from its usual focus on strong GDP growth towards maintaining, or rather achieving, economic stability. Real GDP growth had averaged 7.1% a year between 2000 and 2010, but fell to 5.9% in 2011. For this year, real GDP growth is estimated at 5.8% while the Vietnamese government is aiming for 6%. The policy shift seems to be working out for the better. After peaking at 23% y-o-y in 2011, inflation started to ease. In February this year, inflation had fallen to 16.4% as particularly the rise in food prices decelerated. Good news, as lower inflation will boost confidence in the economy and the currency. Although still relatively high when compared to other countries in the region, the decrease of inflation was sufficient for the State Bank of Vietnam (the central bank) to start easing monetary policy for the first time in three years. The refinancing rate was lowered by 100bps to 14%, the discount rate was lowered by 100bps as well to 12%. This monetary easing should give the economy a boost, which will help to achieve the government's 2012 growth target.

However, we are not fully convinced that authorities aren't too soon to act. Inflation, although expected to ease further in the coming months, remains in double-digit territory. In addition, the rate cut will increase stress on the external liquidity front. The exact strength of Vietnam's external liquidity is difficult to estimate, as figures on the level of FX-reserves have not been published since October last year. Even if a recent central bank statement - claiming that FX-reserves have increased by 20% since the start of the year - is true, the stock of FX-reserves will still amount to only roughly 2 months of imports, which is low. We fear that the government's quest for growth, in fact, persists and that the rate cut decision was, at least in part, influenced by it. The urge to stimulate growth should be contained though. Instead, Vietnamese authorities should keep their head cool and continue to focus on maintaining economic stability. This will bring back confidence among investors and consumers, which will also boost growth, but in a more sustainable manner.

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