INTERNATIONAL MONETARY FUND

IMF Country Report No. 23/338

VIETNAM

September 2023

2023 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR VIETNAM

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2023 IV consultation with Vietnam, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its 2023 consideration of the staff report that concluded the Article IV consultation with Vietnam.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on August 30, 2023, following discussions that ended on June 29, 2023, with the officials of Vietnam on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 25, 2023.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Vietnam.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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International Monetary Fund
Washington, D.C.

PRESS RELEASE

PR23/325

IMF Executive Board Concludes 2023 Article IV Consultation with Vietnam

FOR IMMEDIATE RELEASE

Washington, DC – September 27, 2023: On August 30, 2023, the Executive Board of the International Monetary Fund (IMF) concluded the 2023 Article IV Consultation[1] with Vietnam.

Vietnam experienced a robust post-pandemic economic recovery in 2022 thanks to strong economic fundamentals and prudent public health management during the pandemic. GDP rose by a historically high 8 percent—the highest since the 1990s—driven by strong domestic and external demand. Average inflation was kept at 3.2 percent, well below the (4 percent) inflation target, although price pressures picked up during the year.

The recovery was cut short, however, as strong headwinds hit the economy in late 2022 and during the first half of 2023. Financial stress among real estate developers emerged due to tighter funding conditions, a slowdown in sales, and legal hurdles, while the corporate bond market froze amidst a loss of investor confidence. Exchange rate pressures mounted throughout 2022 as global interest rates rose sharply, and a major domestic bank suffered a deposit run in October 2022 and was placed under the State Bank of Vietnam's control. The economy was further hit by a sharp deterioration in external demand since late 2022, with exports declining by 12 percent in the first half of 2023. Liquidity, foreign exchange, and inflationary pressures have eased, but growth decelerated significantly and is expected to slow to 4.7 percent in 2023—supported by a rebound in exports and expansionary (especially fiscal) policies. Inflation is expected to remain contained below the 4.5 percent ceiling. Vietnam can return to high growth rates over the medium term supported by structural reforms.

Executive Board Assessment[2]

Executive Directors agreed with the thrust of the staff appraisal. They commended the authorities' swift actions to maintain macro-financial stability as the economic recovery from the pandemic faced domestic and external headwinds. They noted that risks remain elevated, and that further efforts are required to safeguard macro-financial stability and deepen reforms to address

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summing up can be found here: http://www.IMF.org/external/np/sec/misc/qualifiers.htm.

vulnerabilities and ensure robust, green, and inclusive growth over the medium term. Continued capacity development will be important to support reforms.

Directors noted that, given ample fiscal space and limited room for monetary policy loosening, fiscal policy should take the lead in supporting economic activity if needed. In this context, Directors welcomed the authorities' plans to speed up the implementation of public investment, which will require tackling bottlenecks, and stressed the importance of expanding social safety nets to support the most vulnerable. Directors recommended strengthening the fiscal framework and budget process and increasing revenue mobilization over the medium term to support the ambitious development agenda.

Directors commended the authorities for effectively containing inflation risks but stressed that monetary policy should continue to be cautious under a complex environment and limited policy space. They welcomed steps toward greater exchange rate flexibility and encouraged continued progress in this area, along with modernizing the monetary policy framework.

Directors underscored the importance of strengthening the resilience of the financial system by bolstering capital buffers, phasing out regulatory forbearance, and addressing rising non-performing loans. They also stressed the need to enhance the authorities' toolkit to prevent and manage banking crises by strengthening the resolution and emergency liquidity frameworks, and welcomed the ongoing revision of the law on credit institutions. Efforts to strengthen bank regulation and supervision should continue.

Directors acknowledged the authorities' swift actions to contain risks in the real estate and corporate bond market. They urged decisive steps to address remaining risks, including by strengthening the insolvency framework, bolstering institutions, and increasing transparency in the corporate bond market.

Directors stressed the importance of structural and climate reforms to achieve sustainable, green, and inclusive growth. Accelerating the transition to upper-middle income status will require further efforts to improve the business environment, step-up critical infrastructure, and invest in human capital. Directors welcomed the latest Power Development Plan and the planned Emissions Trading System to help achieve Vietnam's climate goals and promote energy security. They emphasized the importance of moving ahead with implementation of the strategy and developing the appropriate regulatory framework to promote investment in renewable energy and secure funding for the green transition. Conducting a Climate-Public Investment Management Assessment would be useful.

Directors welcomed the authorities' anti-corruption efforts and emphasized the need to continue strengthening governance, improving the AML/CFT framework, and simplifying regulatory frameworks. Greater efforts in closing data gaps will be important.

The next Article IV Consultation with Vietnam is expected to be held on the standard 12-month cycle.

Vietnam: Selected Economic Indicators, 2019–2024

	2019	2020	2021	2022	Projections 2023	2024
Output						
Real GDP (percent change)	7.4	2.9	2.6	8.0	4.7	5.8
Output Gap (percent of GDP)	0.4	-0.4	-1.9	-0.1	-1.1	-1.1
Prices (percent change)						
CPI (period average)	2.8	3.2	1.8	3.2	3.7	3.5
Core inflation (period average)	2.0	2.3	0.9	2.7	4.2	3.4
Saving and investment (in percent of GDP)						
Gross national saving	35.6	36.3	31.3	33.1	32.4	32.4
Gross investment	32.0	31.9	33.5	33.4	32.1	31.8
Private	26.6	24.9	27.2	27.4	25.5	24.8
Public	5.3	7.0	6.2	6.0	6.6	7.0
State budget finances (in percent of GDP) 1/						
Revenue and grants	19.4	18.4	18.7	19.0	18.4	18.5
Expenditure	19.8	21.3	20.1	18.8	19.6	20.2
Expense	14.5	14.3	13.9	12.8	13.0	13.2
Net acquisition of nonfinancial assets	5.3	7.0	6.2	6.0	6.6	7.0
Net lending (+)/borrowing(-) 2/	-0.4	-2.9	-1.4	0.3	-1.3	-1.7
Public and publicly guaranteed debt (end of period)	40.8	41.1	39.1	35.3	33.6	32.3
Money and credit (percent change, end of period)						
Broad money (M2)	14.8	14.5	10.7	6.2	6.1	6.9
Credit to the economy	12.8	11.6	13.5	14.0	9.0	9.7
Balance of payments (in percent of GDP, unless otherwise indicated)						
Current account balance (including official transfers)	3.7	4.3	-2.2	-0.3	0.2	0.7
Exports f.o.b.	79.6	81.6	90.9	91.4	81.6	80.9
Imports f.o.b.	73.2	72.7	86.7	85.0	75.8	75.1
Capital and financial account 3/	5.7	2.4	8.3	2.3	2.5	1.8
Gross international reserves (in billions of U.S. dollars) 4/	78.5	95.2	109.4	86.7	98.7	110.5
In months of prospective GNFS imports	3.5	3.3	3.5	2.9	3.1	3.1
Total external debt (end of period)	37.0	37.6	37.9	36.2	36.6	36.5
Nominal exchange rate (dong/U.S. dollar, end of period)	23,173	23,098	22,826	23,633	...	...
Memorandum items (current prices):						
GDP (in billions of U.S. dollars)	331.8	346.3	369.7	406.5	438.2	476.9
Per capita GDP (in U.S. dollars)	3,439	3,549	3,753	4,087	4,365	4,707

Sources: Vietnamese authorities; and IMF staff estimates and projections.
1/ Follows the format of the Government Finance Statistics Manual 2001. Large EBFs are outside the state budget but inside the general government (revenue amounting to 6-7 percent of GDP).
2/ Excludes net lending of Vietnam Development Bank and revenue and expenditure of Vietnam Social Security.
3/ Incorporates a projection for negative errors and omissions going forward (i.e. unrecorded imports and short-term capital outflows).
4/ Excludes government deposits.

INTERNATIONAL MONETARY FUND

VIETNAM

STAFF REPORT FOR THE 2023 ARTICLE IV CONSULTATION

July 25, 2023

KEY ISSUES

Context. After a strong post-pandemic recovery, the economy faces strong headwinds. A weaker external environment led to a sizable decline in exports. In addition, amidst high private debt and rising global interest rates, a liquidity crunch distressed highly leveraged sectors (in particular, real estate), the corporate bond came to a halt, and non-performing loans rose. As a result, economic activity decelerated sharply in the first half of 2023. While the government managed to stabilize the markets, risks remain elevated.

Recommendations. Addressing the multiple headwinds affecting the economy calls for a comprehensive, multi-pronged response by the government. In addition, Vietnam should implement far-reaching reforms to meet its ambitious medium- and long-term objectives of sustained high and green economic growth.

- **Monetary policy.** Monetary policy took the lead in responding to the economic deterioration, but there is very limited space for further monetary easing at present. The exchange rate regime should allow for greater flexibility and accompany a modernization of the monetary policy framework to equip it with more market-based tools.
- **Fiscal policy.** Given ample fiscal space, the budget is better placed to take the lead to provide additional support if economic activity proves weaker than expected. The government could scale up social safety nets that would boost growth and protect the most vulnerable households. Over the medium term, further revenue mobilization efforts would bolster social spending and infrastructure investment.
- **Financial sector.** The resilience of the banking system and domestic capital markets should be strengthened, including enhancing the authorities' ability to prevent and manage crises. Upgrading the effectiveness of the debt enforcement and insolvency framework would help deal with corporate debt overhang and reduce risks to the economy and the financial sector.
- **Climate and structural policies.** Achieving the ambitious medium-term growth and climate goals will require accelerating reforms to improve the business environment, critical infrastructure, and human capital.

Approved By
Sanjaya Panth (APD) and Rishi Goyal (SPR)

Discussions took place in Hanoi and Ho Chi Minh City during June 14-29, 2023.The mission comprised Paulo Medas (Head), Federico Díez, Faizaan Kisat, Giacomo Magistretti, Francois Painchaud (all APD), Minke Gort (MCM), Antung A. Liu, Yuan Xiao (both FAD), Nga Ha, and Van Anh Nguyen (both IMF Office in Hanoi). Ryoichi Okuma (APD), Ender Emre and José Garrido (both LEG), and Emanuele Massetti (FAD) joined virtually. Hibah Khan, Mariam Souleyman (both APD), and Hai Hoang (IMF Office in Hanoi) provided superb research, editorial, and logistical assistance, respectively, for the discussions and the preparation of this report.

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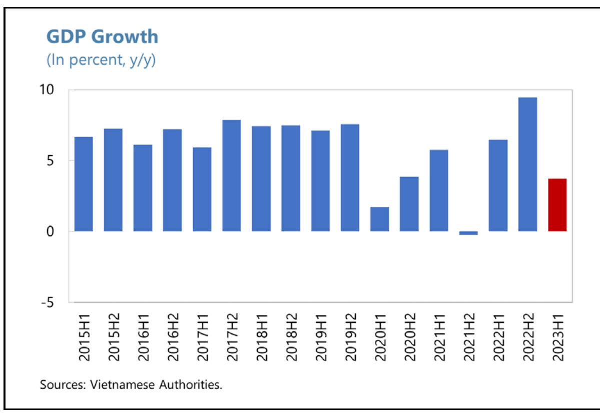
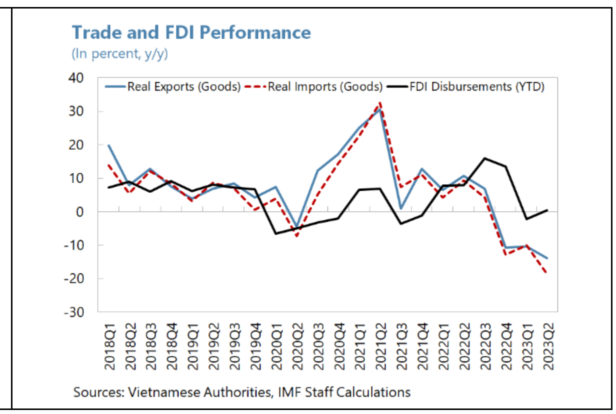
ANNEXES

CONTEXT AND RECENT ECONOMIC DEVELOPMENTS

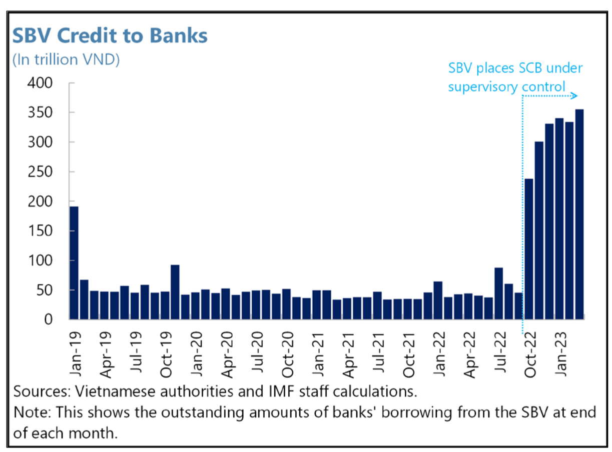
1. Vietnam experienced a strong recovery in 2022. The shift to "living with COVID," along with an impressive vaccination campaign, and strong domestic and foreign demand spurred activity in 2022. GDP grew at the historically high rate of 8 percent. Average annual inflation registered at 3.2 percent; however, price pressures, especially in core items, picked up steadily during the year. Strong external demand early in the year helped reduce the current account deficit to 0.3 percent of GDP.

2. Economic activity deteriorated sharply, however, starting in late 2022 due to domestic and external headwinds. Economic growth slowed to 3.7 percent y-o-y in the first half of 2023, with investment recording one of the worst performances in more than a decade. The unexpected and abrupt deterioration in the outlook was driven by domestic financial distress, turmoil in the real estate sector, and a sharp contraction in exports (12 percent y-o-y in the first 6 months of 2023) due to a decline in foreign demand that has hit the region. On the upside, the labor market displayed some resilience—the unemployment rate remained low, at 2.3 percent in June. However, some manufacturing firms have started to reduce working hours and lay off workers, most of whom are moving to the service sector, often with informal status.



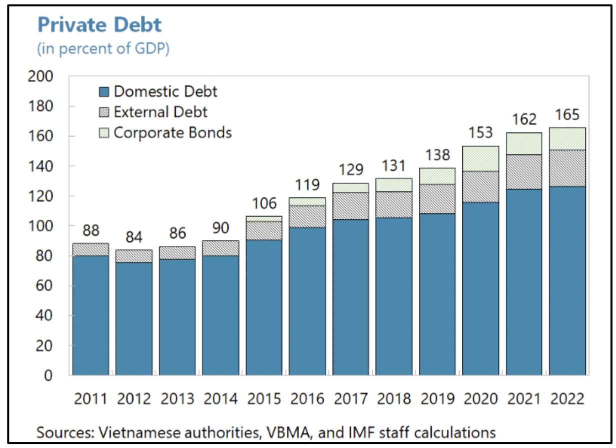


3. Liquidity distress in the FX and financial markets surfaced in late 2022. Pressures on the dong mounted throughout 2022 as global interest rates rose sharply, opening a large gap with domestic rates. Capital outflows, including the sale of FX reserves by the State Bank of Vietnam (SBV) to contain rising FX pressures, contributed to a decline in liquidity in the financial system. In October 2022, Sai Gon Joint Stock Commercial Bank (SCB), the fifth largest bank by assets, suffered a deposit run and was placed under SBV's control. Liquidity in the interbank market deteriorated sharply. However, after



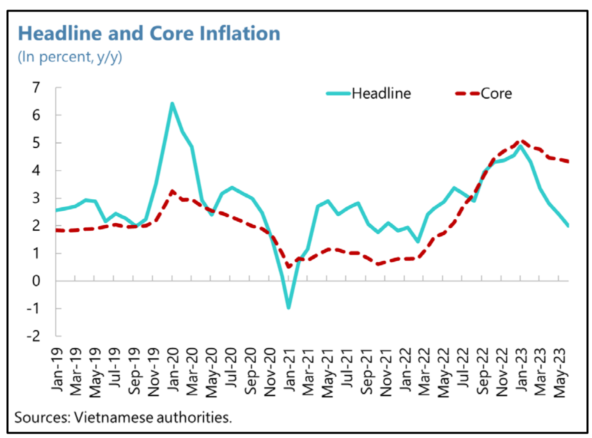
taking control of SCB, the SBV has provided ample liquidity and, by early 2023, liquidity pressures in the banking sector had eased.[1]

4. The turbulence in the real estate and corporate bond markets remains a source of pressure to the economy and the financial sector (Box 1). The liquidity crunch emerged in the context of rising private debt, especially during the low-growth pandemic years. Many real estate developers became highly leveraged in recent years and faced financial distress as interest rates rose and sales declined in late 2022. In addition, the corporate bond market, where real estate represents the largest market share, came to a halt amidst a decline in investor confidence and a crackdown on illegal activities (which also involved real estate issuers). In turn, this aggravated the liquidity squeeze, with a growing number of developers defaulting on bond payments. Furthermore, some banks highly exposed to the real estate market are facing a deterioration in asset quality. The authorities promptly issued a series of regulations aimed at facilitating access to funding and reducing bankruptcy risks in the near term (Text Table 1). While these measures can provide temporary relief, they could create their own risks down the road without further reforms.



Sources: Vietnamese authorities, VBMA, and IMF staff calculations

5. Monetary policy has been nimble, adjusting to contain risks in a fast-changing environment. Like other peer countries facing inflation and exchange rate pressures, the SBV increased its main policy rates in the fall of 2022—the cumulative hike reached 200 basis points. It also raised the 2023 inflation target from 4 to 4.5 percent. After peaking at 4.9 percent in January 2023, headline inflation declined sharply in recent months (down to 2 percent y-o-y in June 2023), while the drop in core inflation was more modest (from 5.2 to 4.3 percent). As the SBV reduced its FX interventions in late 2022, the dong temporarily depreciated but pressures abated following the policy rate hikes. Since March 2023, the SBV has lowered its main policy rates by a cumulative 150-200 basis points to support the faltering economic activity, while the exchange rate has remained stable and modest reserve accumulation has resumed in 2023.



Sources: Vietnamese authorities.

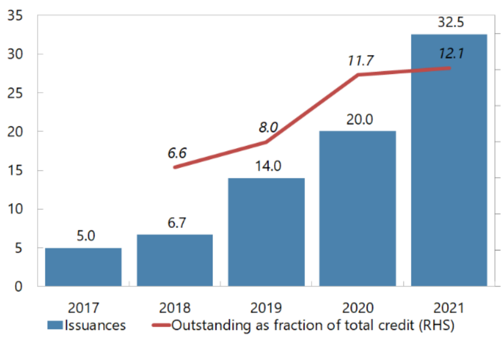
[1] In addition, in June 2023, Vietnam was placed by the Financial Action Task Force (FATF) on its list of jurisdictions under increased monitoring as it works to address strategic deficiencies in its AML-CFT regime.

Box 1. Real Estate Sector and Corporate Bond Market Turbulence

Vietnam's corporate bond market, after expanding at a fast pace over the last 6 years, experienced a sudden stop in issuances starting in late 2022. Outstanding bonds rose from 6.6 to 12 percent of total credit (8.6 to 15 percent of GDP) between 2018 and 2021. However, the market froze in the last quarter of 2022, and market activity remains limited while defaults continue. Bondholders, especially retail investors, are pressuring underwriting banks to buy back bonds.

Corporate Bond Market

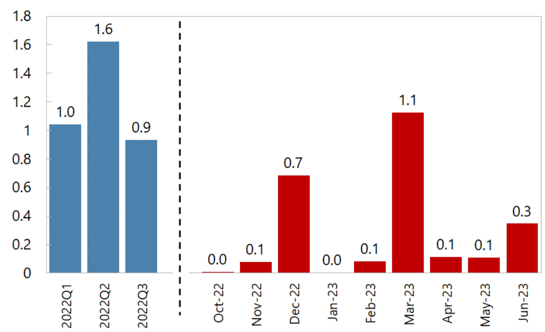
(In billions of US dollars, LHS; in percent, RHS)



Sources: VBMA and IMF staff calculations.

Corporate Bond Issuances 2022-23 1/

(In billions of US dollars)



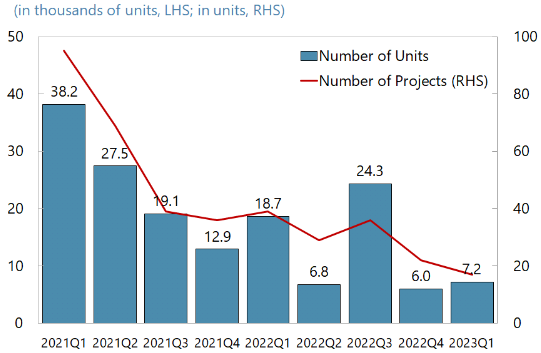
Sources: VBMA and IMF staff calculations.

1/ 2022Q1-Q3 issuance values are monthly averages

Distress among real estate developers increased as funding sources dried up and legal bottlenecks intensified. Real estate transaction activity slowed since late 2022 (after booming in previous quarters), as demand weakened and new projects coming to the market fell due to delays in securing authorizations and land use titles. The delays arose amid heightened uncertainty around how land and construction regulations were being applied, especially given overlapping, unclear, and sometimes inconsistent real estate related laws and regulations. In addition, developers' profitability declined further due to higher financing and other costs, and funding pressures were exacerbated due to the freeze of the bond market. Consequently, 56 developers, including the second largest, defaulted on bond payments in the first 5 months of 2023 (over 70 percent of total defaulted value). Risks remain elevated as a majority of upcoming maturities are for developer issued bonds. In addition, some homebuyers received bridge loans to finance pre-sales and other financial incentives from developers. Rollover risks for these loans have risen due to market uncertainty. On the upside, the market appears to distinguish between developers, with stock prices falling significantly more for those most leveraged. Medium-term prospects for real estate demand also remain promising, given low levels of urbanization and limited supply of affordable housing.

Residential Housing Projects Licensed

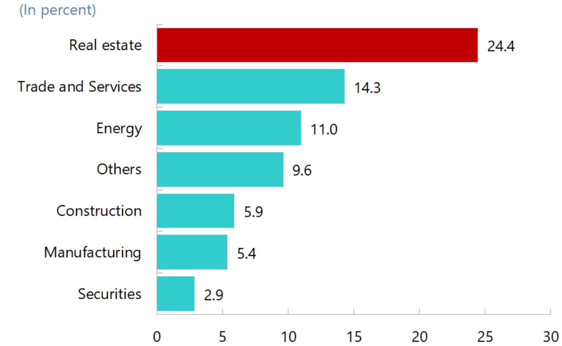
(in thousands of units, LHS; in units, RHS)



Sources: Ministry of Construction

Corporate Bond Default Ratio by Sector 1/

(In percent)



Sources: FiinRatings

1/ As of May 4, 2023.

6. **Fiscal policy was countercyclical in 2022, as spending was kept under control despite rising inflation**. The fiscal position improved to an estimated small surplus in 2022 from a deficit of 1.4 percent of GDP in 2021. While the economic recovery and high oil prices drove revenues higher, with public wages frozen, current spending fell sharply as a share of GDP. Capital spending reached 6 percent of GDP despite a slow start to the investment programs in the 2022-23 Program for Socio-economic Recovery and Development (PRD). Public debt fell to an estimated 35 percent of GDP due to strong nominal GDP growth and an improved primary fiscal balance.

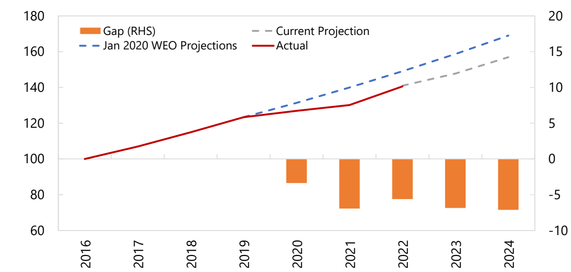
Text Table 1. Vietnam: Measures Addressing the Real Estate and Corporate Bond Market Turbulence

Policy	Date	Main provisions and policy objectives	Potential unintended effects
Circular No. 26/2022/TT-NHNN	December 2022	Enlarging banks' regulatory capacity to lend by including State deposits in the denominator of the regulatory loan to deposit ratio.	Could increase bank liquidity risks if deposits are rapidly withdrawn.
Resolution 33/NQ-CP	March 2023	Easing access to funding to the real estate sector and treating real estate risk in a more differentiated way.	May lead to banks increasing exposure to (non-viable) real estate developers and associated higher risk.
Decree No. 08/2023/ND-CP	March 2023	Deferring some recent regulations (issuer rating obligation and the limitation to professional investors under Decree No. 65/2022) by one year. Allowing deferral of corporate bond maturities by up to two years and the payment of maturing corporate bonds with non-cash assets, subject to bondholders' approval.	Could delay the resolution of problems and the return of confidence, thus undermining medium-term development of the corporate bond market.
Circular No. 02/2023/TT-NHNN	April 2023	Allowing one-year regulatory forbearance on loan classification for loans restructured with financially viable businesses and individuals; banks are required to gradually set aside the required additional provisioning.	Could increase risks to the banking sector by masking actual deterioration in asset quality, while delaying provisioning and NPL workouts.
Circular No. 03/2023/TT-NHNN	April 2023	Allowing banks to purchase corporate bonds they sold within the previous 12 months until end-2023 (previously prohibited).	May pressure banks to repurchase corporate bonds sold to their clients, which could involve taking on larger risks and reduces liquidity.

OUTLOOK AND RISKS

7. Economic growth is projected to bounce back in the second half of the year. After a weak first half, growth in 2023 is expected to accelerate and reach 4.7 percent for the whole year, assuming that the real estate turbulence is contained, and exports and credit growth pick up gradually in the second semester and in 2024. Given the opening up of the output gap, inflation is expected to remain below the 4.5 percent target. The current account balance will improve to a small surplus in 2023, driven partly by a rebound in tourism. Merchandise export and import volumes are expected to decline relative to 2022 due to depressed demand. The exit from the pandemic has been challenging and has left some scarring, but the economy is expected to revert to the pre-COVID growth trajectory over the medium term as reforms are implemented.

GDP Dynamics Pre and Post COVID



Sources: Vietnamese Authorities, IMF Staff Calcualtions.
Notes: GDP is normalized to 100 in 2016. The Jan 2020 WEO line corresponds to GDP projections for 2020-2024 based on the annual growth rates estimated in the January 2020 WEO Update, applied to the 2019 GDP level consistent with the latest GDP revision by the GSO. Gap is the percentage point difference between the Jan 2020 WEO and Current GDP trajectories.

8. Downside risks to growth loom large. Uncertainty surrounding the forecast is high. The main external risk is a deeper and more persistent weakness in external demand. While recently benefitting from some business diversion from China, Vietnam stands to lose from a slowdown in global trade due to geoeconomic fragmentation. Domestic downside risks mostly emanate from a further deterioration of financial conditions, which could damage growth prospects over the medium term (Box 2). Further energy shortages after the episodes in May-June 2023 could harm economic activity and business sentiment. On the upside, a faster than anticipated deployment of public investment may boost growth.

Authorities' Views

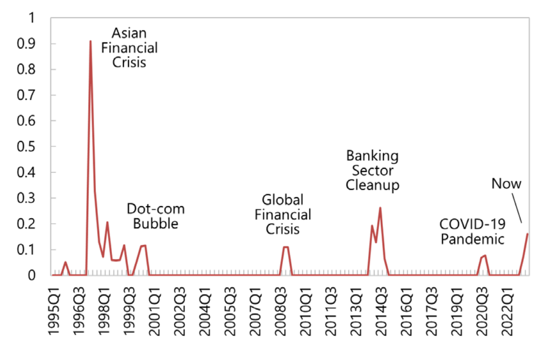
9. The authorities agreed with staff's overall assessment, although they are more optimistic about the rebound in the second half of the year. The authorities are maintaining their 2023 economic growth target of 6-6.5 percent while recognizing that external and domestic risks make achieving that target a harder task. They expect that their economic policy mix and a recovery in external demand will allow for strong growth in the second half of the year. They agreed with staff that inflation pressures have subsided and the SBV is confident the inflation target will be met.

Box 2. Growth Risks from Financial Turbulence

A Financial Stress Index (FSI) shows that turbulence in the markets is increasing but, at present, remains lower than in past distress events. The FSI captures episodes of high credit intermediation costs or disruptions to credit supply, based on text analysis of the Economist Intelligence Unit country reports (Ahir, Dell'Ariccia, Furceri, Papageorgiou, and Qi, forthcoming).[1] The FSI shows the presence of financial distress at the moment. The index is far from the peak reached during the Asian financial crisis, but it is close to the values of 2014, when an attempt to clean up the rising levels of bad debts from banks' balance sheets slowed down credit provision to the economy.

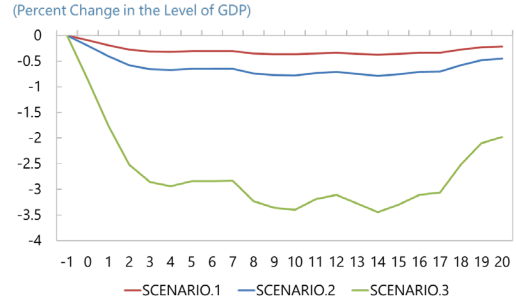
Empirical analysis shows that the impact on economic activity from heightened financial distress could be severe. Using estimates derived in Ahir et al. (forthcoming), an episode of financial turmoil of the intensity (measured by the FSI) experienced in Vietnam in the second quarter of 2023 is estimated to lead to a GDP loss in the order of 0.15 percent in 2023 and around 0.35 percent in every year between 2024 through 2027. If Vietnam's FSI reached the peak value recorded in 2014, the loss of GDP could be around 0.3 percent in 2023 and around 0.7 percent in 2024-2027. Were the FSI to reach the maximum level measured during the Asian financial crisis, GDP would decline by up to 1.4 percent in 2023, and around 3 percent in 2024-2027—losses consistent with an average annual growth in 2023-27 of 5.6 percent, instead of the 6.2 percent projected in this report.

Financial Stress Index – Vietnam



Sources: Ahir et al. (forthcoming), Economist Intelligence Unit, and IMF staff calculations.

Impact of Financial Stress on GDP
(Percent Change in the Level of GDP)



Sources: Ahir et al. (forthcoming) and IMF staff calculations.
Note: In Scenario.1, the FSI increases to the level of 2023Q2; in Scenario.2, to the level observed in 2014Q3; and in Secenario.3, to the level observed in 1997Q3.

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[1] The FSI counts the number of instances in which two keywords jointly appear in a sentence/paragraph of a EIU report, and scales that by the number of words in the report. The keywords are: (i) credit, financial, bank, lending, and fund, and; (ii) crisis, crunch, squeeze, bailout, rescue, tight, contract, and reluctant. Ahir and coauthors build the index for the period 1967Q1-2018Q4, and the Vietnam team extended it to 2023Q2.

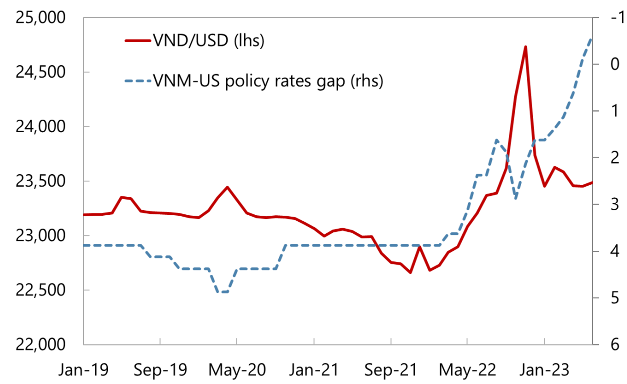
POLICY DISCUSSION

10. **Amid heightened uncertainty, there was broad agreement that the policy priorities should be to restore strong growth and protect financial stability.** Discussions centered around the policy mix, achieving greater balance between monetary and fiscal policies, and the need for a coordinated and comprehensive approach to tackle with greater urgency immediate challenges regarding: (i) the real estate and corporate bond market distress, and (ii) the financial system, given the turmoil stemming from the real estate sector and the rise in non-performing loans due to weak economic activity. Finally, achieving Vietnam's medium-term goals will require executing the ambitious agenda of climate and structural reforms.

A. Monetary and Exchange Rate Policy

11. Monetary policy actions should be cautious given significant underlying risks, while fiscal policy has more flexibility in supporting activity. During the first half of 2023, policy rate cuts were the first line of response to the slowdown—as headline inflation fell well below target, the negative output gap widened, and the dong remained stable, partially thanks to a large trade surplus in the first half of the year. However, further cuts would bring policy rates to historically (pre-COVID) low levels and could reignite disruptive FX dynamics—as global rates are likely to stay high for longer and the large trade surplus of the first half of the year is likely to unwind as the economy strengthens—heightening the risk of exchange rate depreciation passing through to inflation (Annex IV). In addition, with banks facing increasing non-performing loans and high loan-to-deposit ratios, incentivizing credit growth would be risky and likely ineffective. Instead, fiscal policy could take the lead in sustaining demand given the highly leveraged corporates and weak external demand. If inflationary pressures re-emerge, policy rates may need to be increased once again. Conversely, if more generalized financial distress materializes or the economic slowdown proves deeper, further support measures could be needed, which reinforces the need for keeping monetary policy's powder dry for now.

Exchange Rate Movements and Policy Rate Gap
(VND/USD, LHS; policy rate gap in percentage points (reversed), RHS)



Sources: Haver and IMF staff calculations.

12. Greater exchange rate flexibility would help absorb external shocks. The widening of the exchange rate trading band in October 2022 was a positive step. After drawing down reserves to fend off disruptive FX dynamics in 2022, the SBV has been gradually rebuilding its FX reserve buffers given favorable market conditions. Interventions in FX markets should be limited to smooth volatility and not to counter persistent trends. Greater exchange rate flexibility would require lower FX reserve buffers and strengthen the policy rate transmission mechanism.

13. Accelerating modernization of the monetary policy framework would help better manage the different challenges. In recent years, the SBV has worked to improve its forecasting capacity and its monetary policy decision-making process. Further progress could entail introducing an interest rate corridor and improving liquidity forecasting. Monetary policy should gradually move away from tools such as credit growth ceilings and deposit interest rate caps and adopt market-based mechanisms along with appropriate macroprudential measures—for example, by introducing a systemic risk surcharge for domestically important banks, countercyclical buffers, and loan-to-value or debt-to-income limits on borrowers.

Authorities' Views

14. The SBV remains committed to keeping inflation in check and agrees that there is limited space for further monetary loosening. While lower inflation allowed policy rate cuts to support growth, the authorities are aware of the risks of further monetary loosening. Policies are aimed at maintaining macroeconomic stability in the current challenging external environment. The SBV acknowledged that favorable market conditions in the first half of the year have allowed it to start rebuilding foreign exchange reserve buffers. The authorities reiterated that they do not target any level of the VND/USD exchange rate.

B. Fiscal Policy

15. Fiscal policy is expected to become expansionary in 2023-24 to boost domestic demand. The fiscal deficit is projected to reach 1⅓ percent of GDP in 2023. Public wages, frozen since 2019, were set to rise by 20.8 percent in July, with an estimated annual budgetary impact of 1.2 percent of GDP, helping reduce the gap between public and private compensation. Public investment is expected to accelerate. Revenues are expected to fall mainly due to weaker economic activity and lower revenues from oil revenues and land use rights. Temporary tax deferrals, cuts in environmental taxes, and cuts to VAT rates and car registration fees in the second half of 2023 will also provide some relief to firms and households. However, frequent changes to tax rates and excessive use of deferrals add uncertainty to the tax system and can undermine tax collection. Some of the tax cuts are regressive and have negative effects on climate and congestion. Instead, policies could focus on spending to address infrastructure and social needs. Vietnam's medium-term strategy, including fiscal rules, provides a medium-term anchor to ensure sustainable debt.[2]

16. Further fiscal support could be considered, especially if the economic recovery disappoints. Given the slowdown and the constraints faced by monetary policy, going forward, fiscal policy can take a leading role in supporting aggregate demand. For instance, the government could scale up social safety nets—and consider cash transfers to provide swift relief to poorer households. Building on successful fiscal consolidation in recent years, there is fiscal space to provide further support. If the current turmoil proves more damaging to the economy and the financial sector, targeted support could be considered, including to help real estate developers restructure. To contain costs, it is recommended that any support goes through the budget, is temporary, and there are mechanisms in place to control and monitor risk exposure from guarantees or other contingent liabilities.

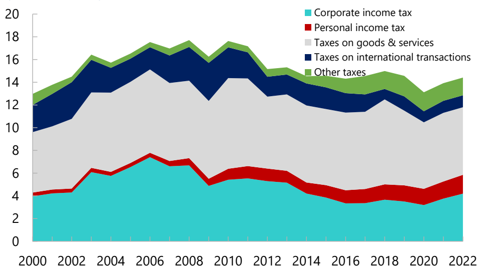
17. Revenue mobilization efforts over the medium term are needed to reverse the trend of tax erosion and create space to bolster social spending and address infrastructure gaps. Tax revenues have been eroded since their peak in the late 2000s, in contrast to trends in regional peers (and despite Vietnam's tax rates being close to peers' average). Implementing the

[2] The strategy for 2021-26 sets a debt ceiling of 60 percent of GDP. In addition, budget deficits (which are based on very conservative revenue projections) need to converge to below 3 percent of GDP.

Tax System Reform Strategy 2021-2030 would help widen the tax base and enhance tax compliance. Reforms could include reducing exemptions and rationalizing preferential regimes for FDI firms, broadening the VAT base, and raising environmental tax and excise duties. The planned introduction of a unified property tax and a land registry would also be important.

Composition of Tax Revenues, 2000-22

(Percent of GDP)

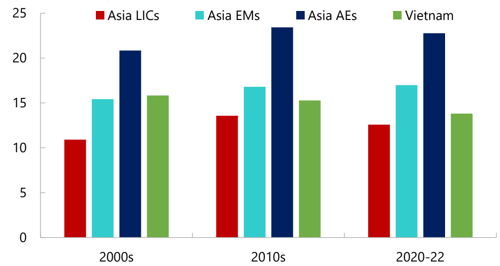


Sources: Vietnamese authorities.

Values for 2000s are based on staff's adjustment of historical GDP to produce a consistent GDP time series and they would be much higher without the adjustment.

Tax Revenues in Asia, 2000-22

(Percent of GDP)



Sources: World Economic Outlook database.

Vietnam's value for 2000s is based on staff's adjustment of historical GDP to produce a consistent GDP time series and it would be much higher without the adjustment.

18. **The adoption of the global minimum corporate tax (GMT) in 2024 will increase tax revenues but will require improvements to the investment climate**. Vietnam could be among those most affected by the GMT—as it has often granted tax incentives to multinational enterprises to attract FDI, including lower income taxes, that will be eroded. The effects of the higher tax can be compensated by improving the business environment, upgrading infrastructure, and enhancing human capital.

19. **Strengthening the fiscal framework and budget processes would increase transparency and enhance the quality and effectiveness of fiscal policy**. The budget process is weakened by overly conservative revenue projections in recent years. A budget based on realistic projections and assessment of risks would allow to better decide on the appropriate fiscal space and level of spending and debt, while increasing transparency. The scope and duration of permitted carryover spending could be more limited and ensure that all spending is integrated in the budget process. It would be important to accelerate efforts to strengthen macro-fiscal capacity (projections, risk assessment, impact of fiscal measures). Conducting expenditure reviews would help identify priorities and improve the quality of expenditures.

Authorities' Views

20. **The authorities reiterated their objective of maintaining macroeconomic stability and confirmed their fiscal structural reform agenda**. They noted that fiscal policy has already played a role in supporting output and are confident that the combined revenue and expenditure measures in 2023 will help boost demand. They agreed there is fiscal space to provide further support if needed given the past successful consolidation efforts that reduced public debt. To reform the tax base and support businesses, they have proposed a revision of several tax laws. The authorities are considering measures that limit the possible negative economic impacts of adopting the GMT that are consistent with international agreements. They cautioned that revenue collection is volatile and prefer to be conservative in the budget.

C. Tackling the Distress in the Real Estate and Corporate Bond Markets

21. Addressing excessive corporate leverage swiftly would help limit the impact of the real estate turmoil and promote a sound corporate bond market. An intergovernmental taskforce is working with local governments to identify and address legal obstacles and administrative delays preventing completion of real estate projects. However, solving the financial distress stemming from the real estate-corporate bond nexus will likely require a more comprehensive response. Unaddressed corporate balance sheet problems, especially among real estate developers, could percolate throughout the economy and the banking system. International experience shows that the lack of an efficient framework to deal with debt overhang cases results in higher costs that take longer to mend.[3] Moreover, ensuring the corporate bond market is a sustainable source of funding for the private sector requires reforms to enhance governance and boost investors' confidence.

22. The necessary deleveraging of high private debt could be made more efficient, and with appropriate burden sharing to not compromise financial stability, by:

- *In the short term*, promoting swift restructuring of viable firms through out-of-court workouts and hybrid solutions for debt restructuring, while liquidating non-viable firms. In addition, if there are concerns regarding completion of ongoing projects deemed critical, the authorities could consider targeted fiscal support subject to adequate safeguards and with appropriate burden sharing between public and private stakeholders. If the real estate turmoil intensifies, the authorities could provide subsidized financing or guarantees to banks for onward lending to viable developers.
- *Over the medium term,* strengthening the effectiveness of the debt enforcement and insolvency framework to deal with debt overhang in real estate and other sectors of the economy (Box 3). A more effective insolvency regime would contribute to a better allocation of resources in the economy and the development of the corporate bond market. Banks have been granted extraordinary powers until end-2023 to seize collateral (Resolution 42), which has helped process their nonperforming loans. However, including such temporary regulation into the Law on Credit Institutions would enshrine unequal treatment of secured creditors and could hinder the establishment of an effective debt enforcement and insolvency framework.

23. Further institutional reforms would help strengthen governance of domestic capital markets and restore investors' confidence. Such reforms include ensuring that investor protection and transparency principles are respected to restore confidence in the corporate bond market and that all investors are treated equally when issuers make use of recently adopted temporary measures. Improving the capacity of rating agencies and making the process for the public listing of bonds less cumbersome would also boost confidence in the bond market and make it a more durable and stable source of funding.

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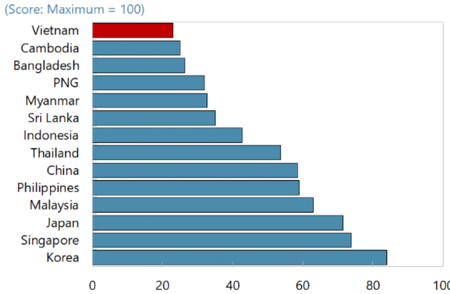
[3] See "Systemic Banking Crises Revisited," IMF WP/18/206.

Box 3. Improving Vietnam's Crisis Preparedness

Vietnam has ample room to improve its preparedness to tackle widespread corporate debt distress. Staff developed a crisis preparedness indicator based on the existence and availability of a set of insolvency and restructuring tools known to be most useful in a debt crisis. The analysis shows several important shortcomings in Vietnam's overall crisis preparedness:

Crisis Preparedness Indicator: Select Asia Pacific Economies
(Score: Maximum = 100)



Sources: Araujo, Juliana, et al. 2022. "Policy Options for Supporting and Restructuring Firms Hit by the COVID-19 Crisis." IMF DP/2022/002, International Monetary Fund.

- Vietnam lacks enhanced mechanisms for ***out-of-court restructuring*** and a legal framework conducive to restructuring. Effective multi-creditor workouts for distressed but viable firms rely on enhanced mechanisms (e.g., a set of principles, master restructuring agreements, and the use of alternative dispute resolution mechanisms) to aid coordinated solutions. An effective debt enforcement regime creates incentives for negotiation, and an enabling framework avoids obstacles in other laws (e.g., tax, banking) to restructurings.

- ***Hybrid restructurings*** are yet to be introduced in Vietnam's framework. They involve limited formal intervention by courts to confirm or facilitate informal restructuring agreements, allowing for quick restructuring, without over-burdening the courts.

- The Vietnamese corporate ***reorganization proceeding*** is largely untested and needs improvements. A debtor in possession reorganization could create appropriate incentives for debtors to seek reorganization. Technical aspects of the stay of creditor actions, the treatment of executory contracts, and post-petition finance could be addressed. Safeguards for dissenting creditors would increase confidence in the process.

- The ***liquidation*** framework does not provide rapid and significant recoveries for creditors. For effectiveness and simplicity, it should allow the possibility of selling the business as a going concern and allow secured creditors to enforce on their collateral. The use of e-auctions and other modern technologies would improve the efficiency of liquidations.

- *S*ome ***institutional*** aspects may be particularly useful in the event of a corporate debt crisis. In Vietnam, the specialization of courts on insolvency matters and the use of modern technology for case management are limited. The regulation of insolvency representatives needs reforms, including on proper qualifications and relevant training.

Specific challenges of the real estate sector accentuate the gaps in crisis-preparedness. Real estate developers can be highly leveraged and exposed to liquidity risk as they invest in land and inventory or face legal obstacles. Uncompleted real estate projects adversely affect banks, investors, and consumers. Some key issues affecting insolvency and creditor rights include the following:

- Prompt enforcement mechanisms minimize the losses of creditors and increase their confidence in real estate collateral. In Vietnam, ***collateral enforcement*** needs strengthening for all economic actors and in all situations under the broader debt enforcement framework.

- Pre-sales can involve fraud and mismanagement risks and buyers may find themselves in the position of unsecured creditors. This may justify the adoption of **protection measures for pre-sales**, either preventive (e.g., mechanisms to allocate sale proceeds for the project) or reactive (e.g., dealing with conflicts between homebuyers and lenders).

- Typically, liquidators can **complete work-in-progress or inventory if that maximizes value**, even if a developer is in liquidation. Additional financing can be provided by existing creditors or a new lender. The challenge is facilitating such financing with adequate priority given existing secured creditors.

Authorities' Views

24. The authorities stressed they are making significant efforts to resolve legal and regulatory bottlenecks in the real estate sector and address social housing needs. A new land law (among other real estate related laws) will be presented to the National Assembly for approval later this year. Affordable housing remains a priority, and the government recently approved a USD 5 billion credit package for social housing projects. On the corporate bond market, the authorities noted there are signs the situation is improving and investors' sentiment has gradually stabilized thanks to the implementation of measures to stabilize the market. In addition, the authorities are working to increase the capacity of rating agencies and researching ways to incentivize institutional investor participation.

D. Protecting Financial Stability

25. SBV acted decisively in 2022 to protect financial stability within the limitations of the existing legal framework; but the real estate turmoil and economic downturn pose increasing risks. SBV took control of SCB in October 2022 using the special control regime and provided it with (secured and unsecured) funding. The authorities also took several ad-hoc measures to support corporates under financial distress due to the problems in the real estate market and deteriorating economic conditions. These included temporary forbearance on bank loans and allowing (unlisted) bond buybacks by banks. These measures imply that more risks will be shifted to the banks amidst an unfavorable environment. Asset quality has been worsening; the combined non-performing loan (NPL) ratio[4] reached 5.5 percent by end-March, and the aggregate loan-to-deposit ratio approached 100 percent (excluding government deposits) as loans have been outgrowing deposits for several years. Some banks are also highly exposed to the ailing real estate sector. Bank capitalization was 11.5 percent at end-2022 and some banks have been actively raising capital, but further efforts may be needed.

26. The stress in 2022 highlights the importance of strengthening cooperation on prevention and management of crises. Establishing a crisis and financial stability monitoring function at the SBV, in consultation with the Ministry of Finance (MOF) in the short term, is critical to improve coordination and information sharing, and should involve all relevant actors. Such a function could include: (i) coordinating the consistent identification and monitoring of weaker banks and defining remedial actions; (ii) estimating losses and resolution costs (including fiscal) and discussing contingency plans; (iii) monitoring forbearance measures and improving bank balance sheet transparency; and (iv) conducting bank solvency and liquidity stress tests to inform on financial stability risks. Data sharing, confidentiality, and developing communication strategies will be critical for the function.

27. The ongoing revision of the Law on Credit Institutions (LCI) is a very timely opportunity to modernize the bank resolution and emergency liquidity frameworks.

[4] This ratio is composed of the NPLs at the banks, restructured loans and impaired loans at VAMC.

Resolving banks has proven to be a complex and overly lengthy process due to constraints in the legal framework. For instance, the SBV is still working on the resolution of banks placed under special control in 2015. As recent experience in Vietnam and other countries shows, bank distress can emerge suddenly. As such, having an effective bank resolution framework that ensures swift action can be taken and contingency plans to enhance crisis preparedness are in place is vital. Similarly, an emergency liquidity framework that makes liquidity available to illiquid but solvent banks against adequate collateral and appropriate pricing is needed.

28. Amendments to the LCI could provide adequate tools and powers to SBV.[5] The LCI could be strengthened by adopting international standards, in particular by: reinforcing the role and responsibilities of SBV (including in the early intervention regime), clarifying decision-making procedures, offering legal protection to SBV staff, and including the option to transfer parts of a bank under special control to a viable bank. It will be important to clearly specify the objectives and the elements of recovery planning, early intervention, and resolution regimes. Caution and adequate safeguards are necessary when requiring other parties (Deposit Insurance of Vietnam, banks) to support the restructuring of a bank put in early intervention, in terms of providing liquidity and loss absorption.

29. The recent setbacks in the banking system also call for additional reforms to strengthen financial sector resilience over the medium term. Priorities include:

- Strengthening bank regulation and supervision. For example, by increasing the operational independence of SBV, improving coordination between relevant institutions, enhancing risk-based supervision, and introducing a framework for consolidated supervision of banking groups.
- Fully disclosing ownerships and related party lending.
- Enhancing securities markets oversight and implementing risk-based supervision of securities markets participants.

30. Non-cash payments in Vietnam are rising rapidly, necessitating an improvement in fintech regulation. Transactions through most non-cash payment channels doubled in 2022 compared to 2021. More than 2.8 million mobile money accounts were opened in 2022, of which 70 percent were in rural, remote, and isolated areas. This development has boosted financial inclusion but has come with an increase in identity theft and fraud, calling for oversight by the SBV. Some of the priority areas include operationalizing the regulatory sandbox, improving the regulatory framework and supervision of payment service providers, and increasing data collection and analysis on all fintech service providers.

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[5] Changes to the LCI include: (i) expanding SBV's powers in early intervention measures (EIM) including the ability to provide special loans; (ii) involving other actors (e.g., DIV) during EIM to support the bank in distress; (iii) introduction of a mechanism to deal with bank runs; (iv) elaboration of the special control regime, dissolution, mergers, DIV payouts and bankruptcy and (v) adding a chapter on bad debts.

Authorities' Views

31. The authorities recognized the risks and are taking measures to address them, while agreeing that reforms to strengthen resilience of the financial sector remain a priority. To this end, SBV has intensified its monitoring of the banks and taken measures to allow banks to deal with rising NPLs. The authorities have established a steering committee to identify further policy options. They are revising the LCI in order to enhance the ability of SBV to intervene in troubled banks and expressed interest in CD to support the process. The authorities intend to make progress on the implementation of the Basel II framework and the development of regulation for the fintech sector.

E. Climate and Structural Policies

32. Achieving the ambitious medium-term growth and climate goals will require accelerating reforms to improve the business environment, critical infrastructure, and human capital. Following a period of high economic growth, building on decades of market-oriented structural reforms, the COVID-19 pandemic posed a severe test to the resilience of the economy. To resume the transition to upper-middle income and, eventually, advanced economy status requires further reforms to sustain growth and manage risks. The economy has faced several challenges. For example, legal uncertainty (e.g., due to complex and sometimes inconsistent laws) is undermining investment. Weaknesses and delays in the implementation of public infrastructure, including to ensure reliable energy supply, also pose a risk. Efforts to promote economic development will also need to align with climate objectives. Further investment in education would help spur productivity and reduce the dual economy.

33. The newly approved Power Development Plan 8 (PDP8) and the planned Emissions Trading System (ETS) have the potential to transform Vietnam's energy sector. The authorities are committed to achieve net-zero emissions by 2050, but Vietnam's power sector is currently highly reliant on coal. The PDP8 and ETS will shift electricity generation to a lower carbon, more sustainable mix, while improving energy security and accessibility. The goal of doubling electricity generation will require large expansions of renewable energy and alleviating current transmission bottlenecks. Renewable energy generation targets under PDP8 are estimated to require investments averaging USD 12 billion per year between 2021 and 2030. Most of this investment is envisaged to be private, which requires a clear legal and regulatory framework that promotes appropriate incentives (including on pricing mechanisms).

34. The planned ETS could be a cost-effective method of achieving emissions reductions targets but will require careful design of accompanying policies (Annex VI). The ETS creates market incentives to promote energy efficiency and shift supply towards more sustainable sources of energy by making carbon-intensive fuels like coal more expensive. The ETS can increase firms' costs, with larger increases in more energy-intensive sectors, and raise energy prices for households. Part of the substantial revenues generated by the ETS can be used to fund measures (such as cash transfers to households) to limit these impacts. The success of the transition will also depend on the ability to scale up renewable energy to replace coal and other carbon-intensive fuels to sustain the economic development goals.

35. The National Strategy for Climate Change until 2050, issued in 2022, is a step in the right direction, but calls for translating principles and strategies into concrete actions and plans. Climate trends and projections indicate macro-critical risks for Vietnam that warrant swift and effective adaptation actions (annex VII). In its 2022 Nationally Determined Contribution, Vietnam made an unconditional commitment to reduce emissions by 15.8 percent below business-as-usual levels by 2030. It also made the commitment to reach Net Zero emissions by 2050. Such measures require investing in capacity to integrate climate change considerations at all levels of governments, including budgeting and fiscal planning. This process can be facilitated by updating Public Financial Management practices to include climate considerations. Mobilizing external funding and private sector involvement, including through the Just Energy Transition Partnership (estimated at USD 15.5 billion), will be key given large needs. Ensuring appropriate financial market regulation would facilitate the issuance of green bonds.

36. Improving the quality of infrastructure investment and social spending is crucial to support the country's development goals and climate agenda. In this context, the Public Investment Law was revised in 2019 and the new Public-Private Partnership Law was issued in 2020, however, progress in implementation of the latter has been slow. Competitive bidding in procurement is planned, but the effectiveness of project selection and appraisal remains to be improved. It would be useful to conduct a Public Investment Management Assessment (PIMA) update together with a Climate-PIMA to identify further reform priorities. Improvements to the social protection system to address incomplete coverage and fragmented delivery are warranted, especially given the high share of informal workers.

37. Product and labor market reforms are crucial to unlock Vietnam's medium-term potential. Reforms aimed at fostering technological diffusion and reducing economic dualism by fostering greater interactions between FDI and domestic firms (e.g., through dense local supplier networks) would boost productivity. Efforts to increase human capital levels and reduce skill mismatches would further improve growth prospects. There is evidence of potentially excessive labor market churning (Annex V), partly underpinned by pervasive informality, which acts as a deterrent for firms to invest in upskilling their workforce.

38. Sustaining the gains in reducing corruption will involve continued efforts to strengthen governance. Indicators of perceived corruption improved significantly following a scaled-up anti-corruption campaign in recent years. However, further efforts could be taken to strengthen governance in several areas, including through the ongoing development of the national database on asset and income. Other reforms include making laws and administrative processes clearer, simpler, and more transparent to provide greater legal certainty, reduce scope for excessive discretion by public officials, and limit red tape. Addressing shortcomings on AML/CFT, including those identified by FAFT, will require, among other actions, increasing risk understanding and risk-based supervision, improving domestic coordination and international cooperation, identifying ultimate beneficial owners, and enacting other amendments to bring the current framework closer to best international practices.

39. Addressing data gaps would increase transparency and help better inform policy making and risk management. On the fiscal front, the lengthy delay in compiling final accounts, sizeable discrepancies, and lack of spending details in the budget reports hamper the timely monitoring and best use of fiscal policy.[6] The magnitude of errors and omissions in the balance of payments in 2022 (over 7 percent of GDP) reduces the ability to assess the external position. Other key weaknesses include the lack of publication of a property price index and related real-estate indicators (reflecting the lack of a land registry), and the absence of data on job vacancies, informal sector-related trackers, and on the international investment position. A unified and collaborative data sharing system between the central and local governments as well as among government agencies is crucial to support comprehensive economic surveillance.

Authorities' Views

40. The authorities reiterated their commitment to climate goals and that structural reforms are key to long-term growth. They agreed that achieving climate goals will be challenging and stressed the need for joint international efforts, including financial and capacity building support. The authorities agreed with the need to improve institutions to support the economic transition towards a developed economy. They noted there are ongoing efforts to address legal uncertainties and ease excessive administrative burdens to improve the business environment and promote economic growth. They welcomed the ongoing Fund support on improving the fiscal statistics but cautioned that it could take time to make the required upgrades to the legislative and IT frameworks. The authorities are committed to improve AML/CFT framework and have developed a government action plan to guide the work.

STAFF APPRAISAL

41. As Vietnam emerges from the effects of COVID-19, it is encouraged to embark on a set of reforms to sustain the high, green, and inclusive economic growth that it aspires to achieve. Economic growth averaged 7 percent between 2014-2019, before slowing to 2.7 percent during the pandemic. The robust rebound in 2022 was disrupted by further external and internal shocks. As the economy develops, Vietnam will need to strengthen institutions further and adopt reforms to make the economy more resilient to shocks and promote its appropriately ambitious development agenda over the medium term.

42. At the current juncture, the policy mix should prioritize consolidating macro-financial stability in the face of the large external and domestic shocks. Further monetary easing and policies to boost credit growth carry risks, reinforcing the need for fiscal

[6] A first step solution is compiling cash budget execution data from the Treasury and Budget Management Information System (TABMIS).

policy to take the lead in supporting economic activity. The SBV was able to both contain inflation pressures and stabilize liquidity in financial markets in a very challenging environment in 2022, and appropriately shifted policies in early 2023 as the economy weakened abruptly and inflation pressures subsided. Going forward, the SBV will have to continue to operate with caution under a complex outlook and limited policy space, especially given the high global interest rates, while risks in the financial system have risen. The exchange rate regime should move towards greater flexibility, along with a modernization of the monetary policy framework.

43. Fiscal policy has ample space available to support growth and the most vulnerable, thanks to prudent policies. In the current environment, fiscal policy can be more effective in promoting domestic demand moving forward, given highly leveraged corporates and weak external demand. However, policy implementation should be stepped up, including by addressing bottlenecks in the public investment cycle. Ramping up social safety nets and cash transfers to the most vulnerable would help sustain more inclusive growth. Strengthening the budget processes would ensure the effectiveness and transparency of fiscal policy. Over the medium term, further efforts are warranted to mobilize revenues to bolster social spending and infrastructure investment.

44. The external sector position is assessed to be stronger than warranted by fundamentals and desirable policies. Structural policies aimed at promoting investment and expanding safety nets would help external rebalancing. However, this assessment is subject to significant uncertainty given the large errors and omissions that emerged in 2022 due to unrecorded capital outflows affecting the balance of payments. FX reserves were assessed at below what standard metrics would suggest as appropriate at end 2022 but the SBV is already rebuilding its buffers.

45. Bold reforms would strengthen the resilience of the financial system and enhance the authorities' ability to prevent and manage crises. As international and domestic events illustrate, financial distress can emerge suddenly. As such, Vietnam should accelerate reforms to protect financial stability. In the short term, these include establishing a crisis and financial stability monitoring function to identify and address risks to financial stability, with the SBV coordinating with the Ministry of Finance. Resolution and emergency liquidity frameworks should be promptly strengthened in line with international standards. To bolster banks' capital buffers, the SBV could consider restricting dividend payments at weaker institutions. In the medium term, the supervisory framework could be further enhanced.

46. Solving the problems in the real estate and corporate bond markets will require further efforts in fostering corporate restructuring and developing efficient insolvency frameworks. There is room for Vietnam to improve in all areas of crisis preparedness and build public trust in its insolvency system. In the short term, the focus should be on deploying out-of-court and hybrid solutions for debt restructuring. Reforms in other areas should be pursued over time. Bolstering institutions, including by strengthening supervision, ensuring investor protection, and increasing transparency would help restore confidence in the corporate bond market.

47. The next step for the ambitious climate agenda would be to swiftly translate goals into specific actions. The implementation of the PDP8 and the ETS will transform Vietnam's energy sector and help achieve both economic development and climate goals. However, it will require enhancing the legal and regulatory framework to promote private investment and develop a compensation scheme for those most impacted during the transition. Funding, including international support, is critical to pursue mitigation and adaptation policies.

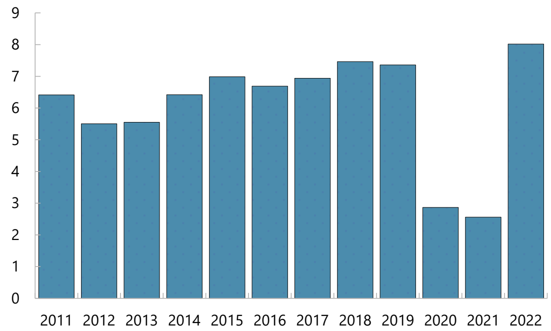
48. Further efforts to enhance anti-corruption frameworks and close gaps in governance and data reliability would be welcome. Despite improvements, strengthening governance is warranted in several areas, including the development of an income and assets national database. Anti-corruption efforts would benefit from greater legal certainty, including through stronger institutions and simplified laws and regulations, and less burdensome administrative procedures. In addition, overcoming data deficiencies, most notably, in fiscal and balance of payments accounts, would improve policy making and the monitoring of risks. It will be important to press ahead with the plans to strengthen the AML/CFT framework.

49. It is recommended that the next Article IV consultation be held on the standard 12-month cycle.

Figure 1. Recent Economic Developments

After two years of subdued activity during the pandemic, the economy rebounded strongly in 2022…

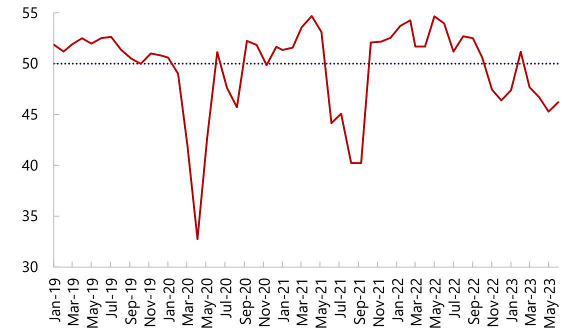
Real GDP Growth
(In percent, y/y)



Sources: Vietnamese authorities.

…but it is currently facing headwinds that started blowing late last year.

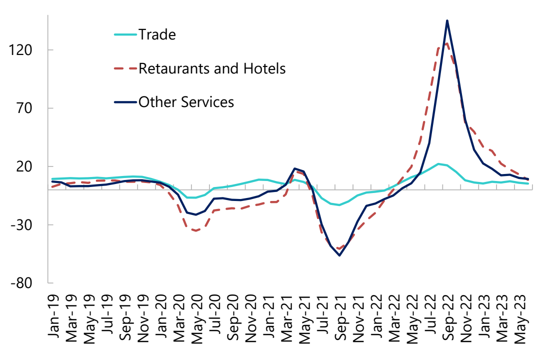
Purchasing Manufacturing Index
(0-100, index)



Sources: Haver.

Domestic demand is still holding up…

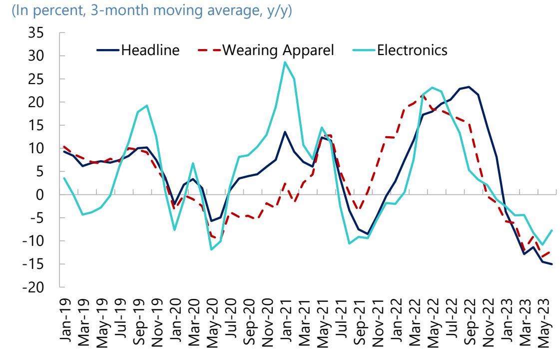
Retail Sales of Trade Goods and Services
(In percent, real, 3-month moving average, y/y)



Sources: Vietnamese authorities.

…but exports are plunging, leading firms to cut back production.

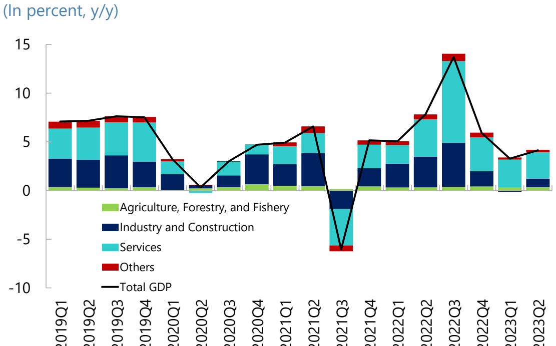
Index of Industrial Production
(In percent, 3-month moving average, y/y)



Sources: Vietnamese authorities.

GDP growth was historically low in 2023H1, with industry having one of the worst performances in over a decade.

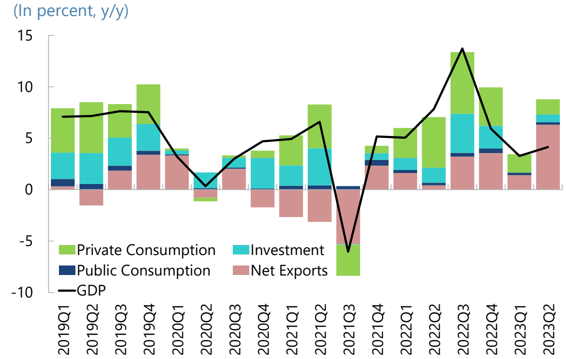
Contributions to Growth, by Economic Activity
(In percent, y/y)



Sources: Vietnamese authorities, IMF staff calculations.

Consumption and investment slowed down while the trade surplus was due to imports declining more than exports.

Contributions to Growth, by Expenditure
(In percent, y/y)



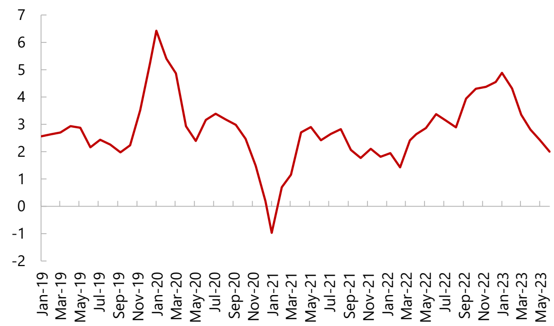
Sources: Vietnamese authorities, IMF staff calculations.

Figure 2. Prices and Wages

Headline inflation is declining fast…

Headline CPI Inflation

(In percent, y/y)

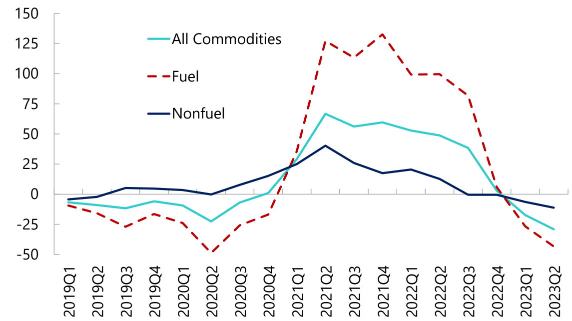


Sources: Vietnamese authorities.

…largely due to a fall in commodity prices, especially fuel.

Global Commodity Price Inflation

(In percent, y/y)

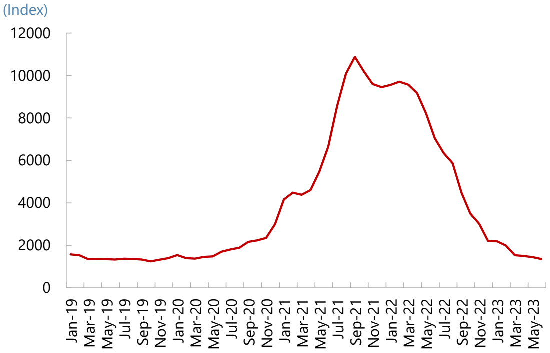


Sources: IMF World Economic Outlook Database.

Lower shipping costs …

Baltic Exchange Freightos Container Index

(Index)

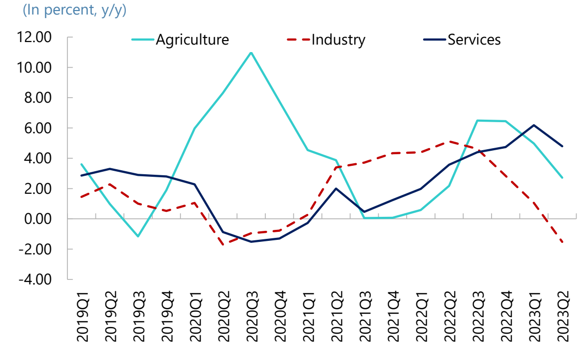


Sources: Haver.

… are also contributing to cool producer prices, especially in manufacturing.

Input Producer Price Inflation

(In percent, y/y)

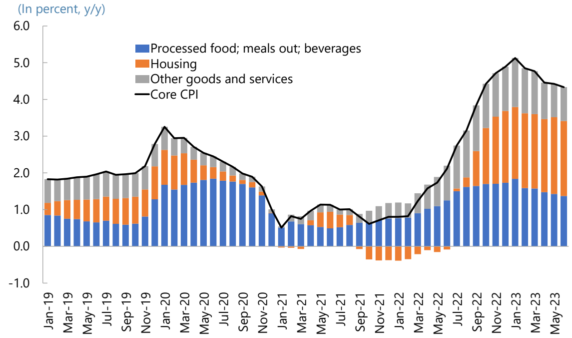


Sources: Haver.

Core inflation is also declining, but more gradually than headline as the price of housing remains elevated.

Core CPI Decomposition

(In percent, y/y)



Sources: Vietnamese authorities and IMF staff calculations.

The labor market remains resilient, but real wages have started to decline as some firms cut down on working hours.

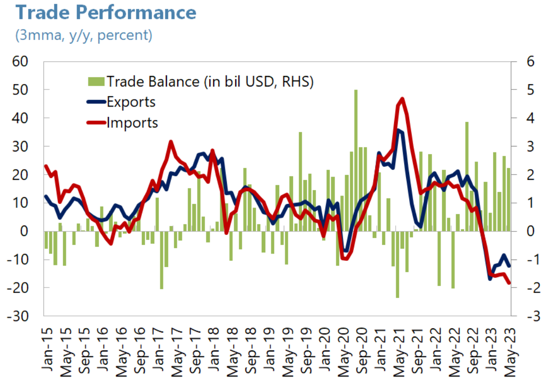
Average Wages and Employment

(In millions)

Sources: Vietnamese authorities and IMF staff calculations.
Notes: Real wages are nominal wages deflated by the CPI, in constant 2019 prices.

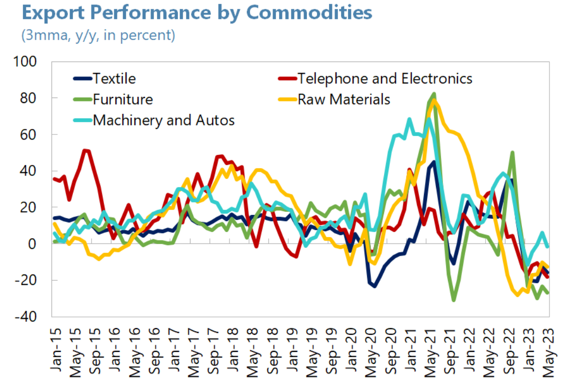
Figure 3. External Sector

Merchandise trade slowed in the first half of 2023…



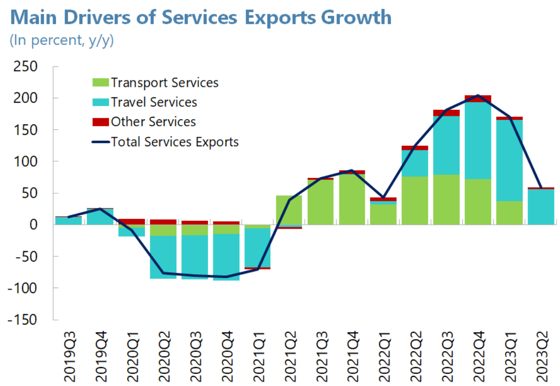
Sources: Vietnamese Authorities, IMF Staff Calculations

… as weak external demand depressed exports, especially of textiles, electronics, and furniture.



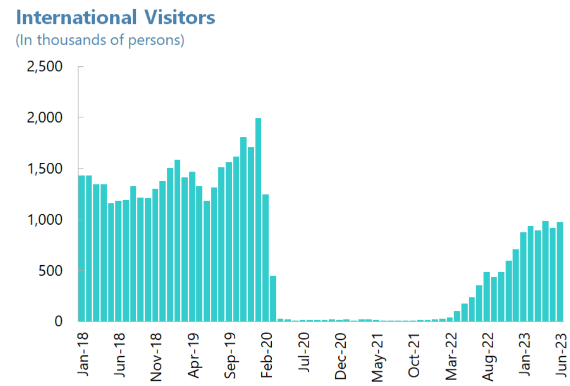
Sources: Vietnamese Authorities, IMF Staff Calculations

Services exports rebounded strongly in 2022 and the first half of 2023…



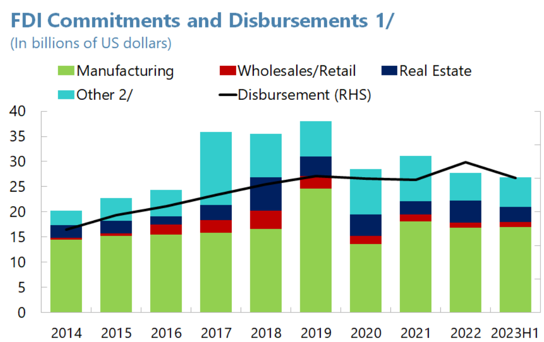
Sources: Vietnamese authorities, IMF staff calculations.

… due to higher tourism, though arrivals still lag pre-pandemic levels.



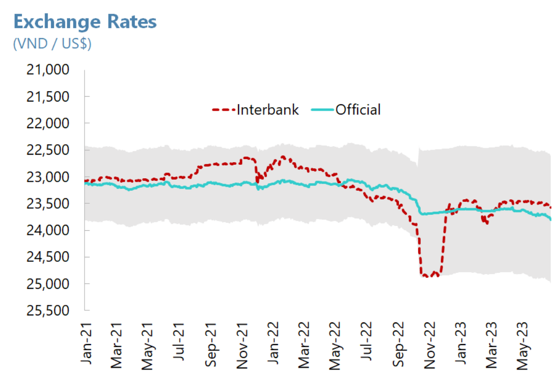
Sources: Haver

FDI commitment and disbursement levels in 2023 fell below recent trends.



Source: Vietnamese authorities; and IMF staff calculations.
1/ 2023H1 data annualized.
2/ Construction, Hotel and Restaurants, Mining, Agricultural, Forestry and Fishery, Electricity, Gas and AC production, and other.

The SBV widened the exchange rate trading band in 2022.



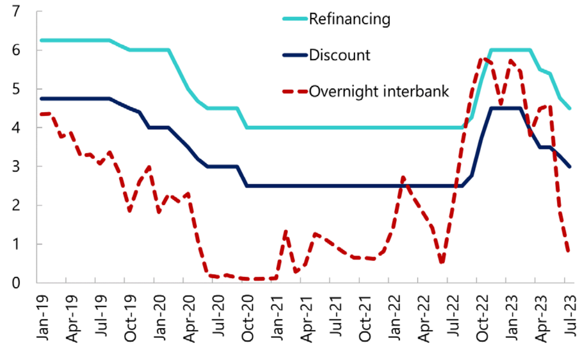
Sources: IMF Staff Calculations
Note: Shaded area indicates the State Bank of Vietnam's exchange rate trading band.

Figure 4. Monetary Sector

Policy rates were tightened in the fall of 2022, but reversed partially since March 2023…

Policy Interest Rates

(Monthly averages, in percent)

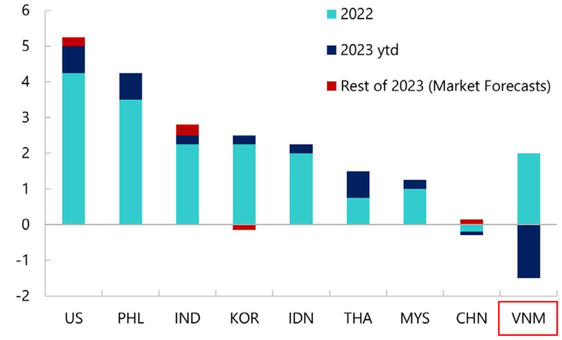


Sources: Vietnamese authorities and IMF staff calculations.

While other countries mostly increased or kept policy rates constant.

Policy Rates Changes in 2022-23: US and Asia

(In percent points change)

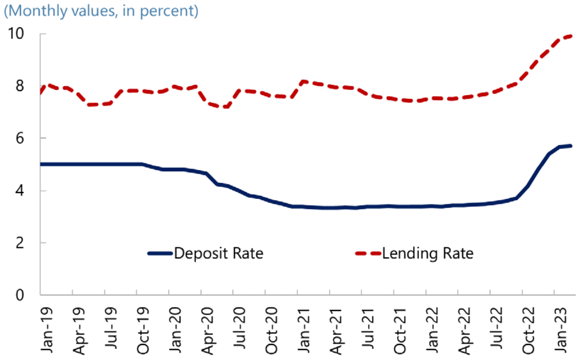


Sources: Haver, Bloomberg, and IMF staff calculations.

Both lending and deposit rates have risen in late 2022 as policy rates were raised.

Lending and Deposit Rates

(Monthly values, in percent)

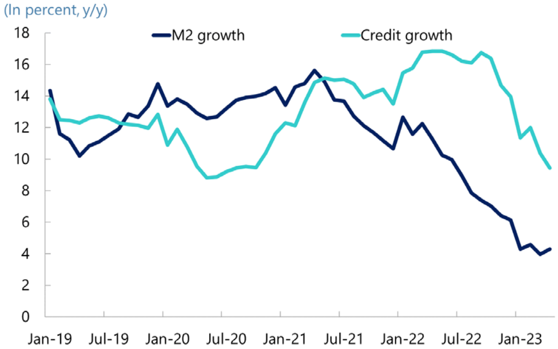


Sources: International Financial Statistics, Vietnamese authorities and IMF staff calculations.

After a strong 2022, credit growth weakened in 2023 while M2 growth has continued declining.

Credit and M2 Growth

(In percent, y/y)

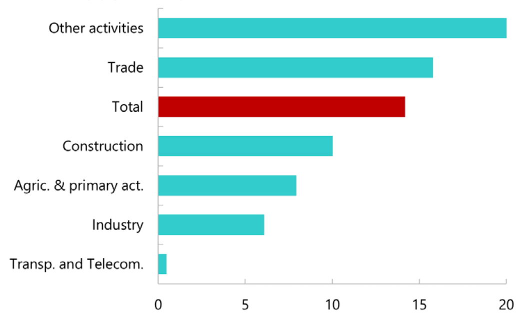


Sources: Vietnamese authorities and IMF staff calculations.

Credit growth in 2022 was concentrated in other activities (including real estate) and trade, due to their strong growth early in the year.

Credit Growth by Sector

(End of 2022, y/y growth, in percent)

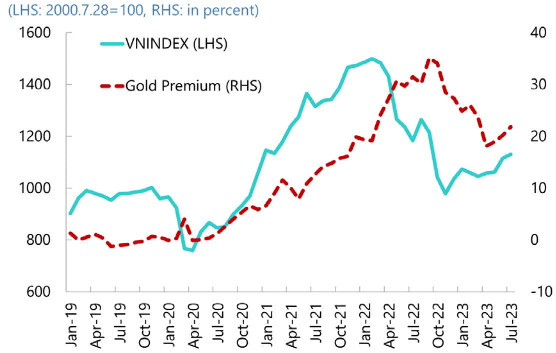


Sources: Vietnamese authorities and IMF staff calculations.

Stock prices peaked out and declined in later 2022 due to uncertainty in global/domestic financial market and real sector.

Stock Market Indices

(LHS: 2000.7.28=100, RHS: in percent)

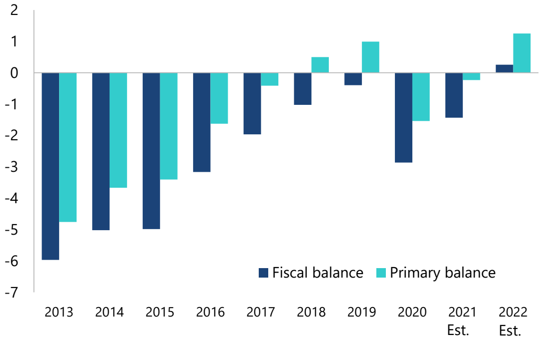


Sources: Vietnamese authorities and IMF staff calculations.

Figure 5. Fiscal Sector

The fiscal position improved in 2022…

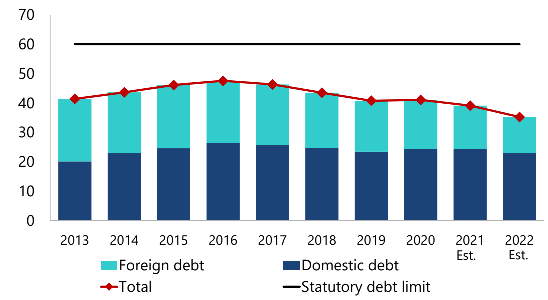
Fiscal Balance
(In percent of GDP)



Sources: Vietnamese authorities; and IMF staff calculations.

…along with strong GDP growth, contributing to a fall in PPG debt ratio.

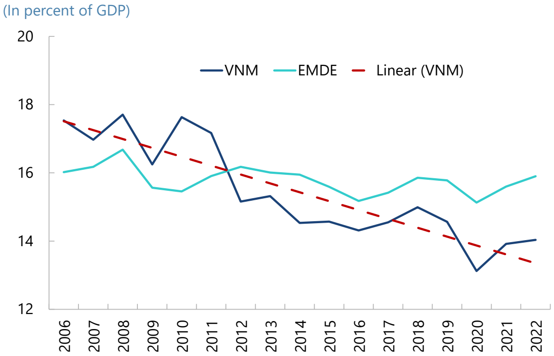
Public and Publicly Guaranteed Debt
(In percent of GDP)



Sources: Vietnamese authorities; and IMF staff calculations.
Note: The formal PPG debt ceiling was revised from 65 to 60 percent of GDP in 2021.

The declining trend in tax revenues needs to be reversed …

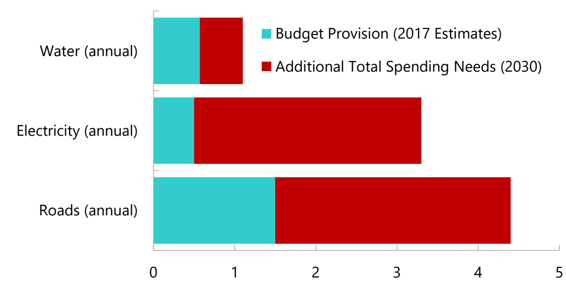
General Government Tax Revenue
(In percent of GDP)



Sources: IMF staff calculations.

…to finance increasing infrastructure and development needs.

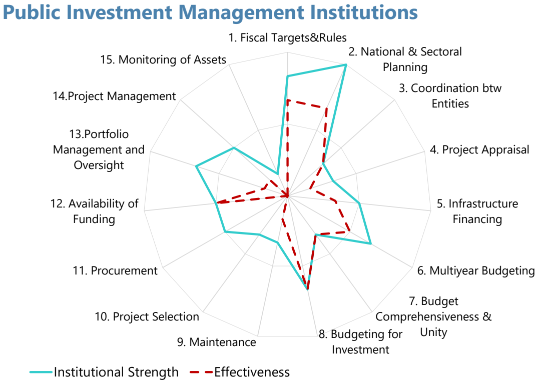
Spending Needs to Achieve Selected SDGs
(additional total spending, in percent of GDP)



Sources: Baum (IMF WP 2020/31).
Notes: Additional spending needs are based on current budget provisions above which spending would need to increase.

Reforms are needed to strengthen public investment management …

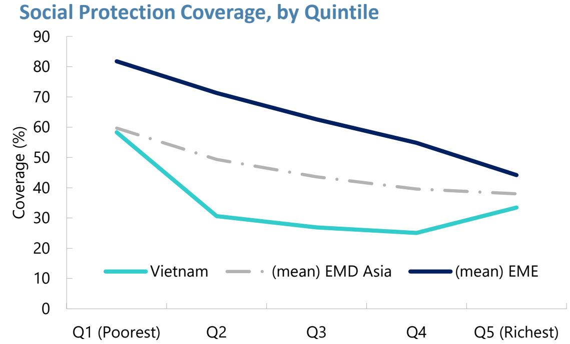
Public Investment Management Institutions



Source: IMF (2018). Vietnam: Public Investment Management Assessment – PIMA.

… and expand coverage of social protection systems.

Social Protection Coverage, by Quintile

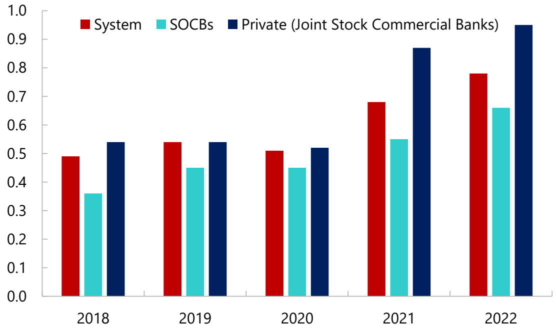


Sources: IMF FAD Social Protection & Labor - Assessment Tool (SPL-AT)

Figure 6. Financial Sector Developments

Bank profitability remained high in 2022, driven by strong credit growth and NIMs.

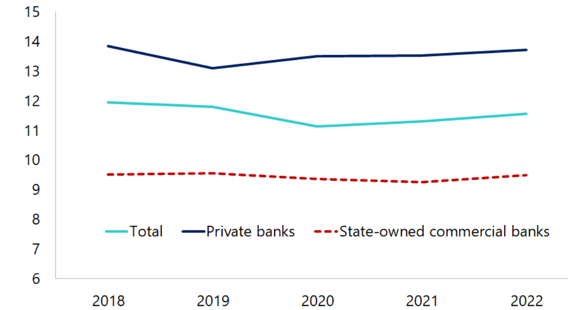
Bank Profitability
(ROA in Q2)



Sources: Haver Analytics and IMF staff calculations.

However, capital adequacy remained weak, especially in SOCBs.

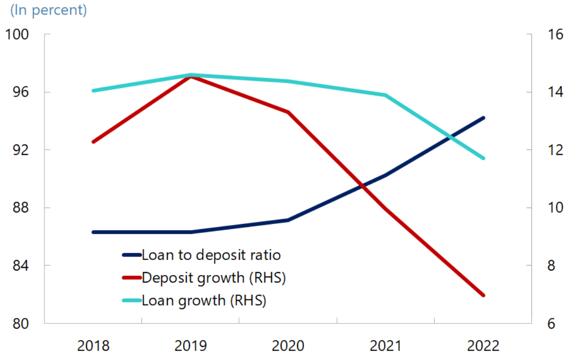
Capital Adequacy Ratios
(In Percent)



Sources: Financial Soundness Indicators, authority's data and IMF staff calculations.

...and liquidity tightened sharply as lending grew faster than deposits.

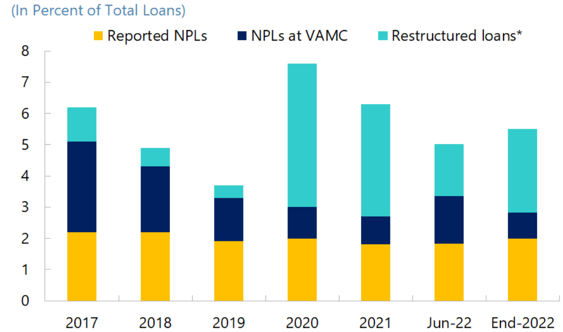
Loan to Deposit Ratio
(In percent)



Sources: Financial Soundness Indicator Database and IMF staff calculations.

NPLs are picking up again since June 2022.

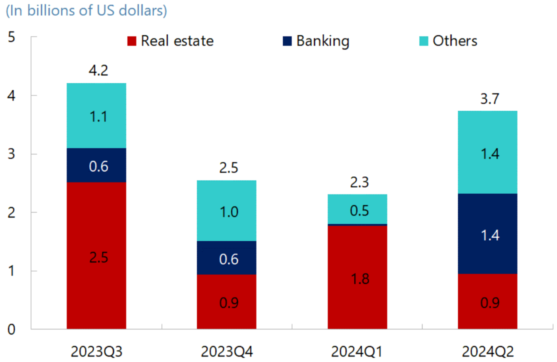
Impaired Assets of Banking System, 2017-2022
(In Percent of Total Loans)



Sources: Financial Soundness Indicators (FSI). 2022 data is from the authorities.
Note: * restructured loans including the legacy restructured loans and covid 19 loan forbearance

Bond defaults could rise further as real estate developer issued bonds form the bulk of upcoming maturities.

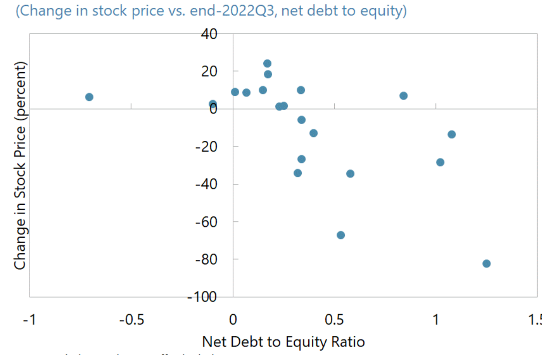
Corporate Bond Market: Scheduled Maturities
(In billions of US dollars)



Sources: VBMA and IMF staff calculations.

Share prices have fallen steeply for the most leveraged developers.

Real Estate Developers: Share Price and Leverage
(Change in stock price vs. end-2022Q3, net debt to equity)



Sources: Capital IQ and IMF staff calculations
Note: Analysis includes top 20 listed real estate developers with reported leverage values.

Table 1. Vietnam: Selected Economic Indicators, 2019–2024

	2019	2020	2021	2022	Projections 2023	Projections 2024
Output						
Real GDP (percent change)	7.4	2.9	2.6	8.0	4.7	5.8
Output Gap (percent of GDP)	0.4	-0.4	-1.9	-0.1	-1.1	-1.1
Prices (percent change)						
CPI (period average)	2.8	3.2	1.8	3.2	3.7	3.5
Core inflation (period average)	2.0	2.3	0.9	2.7	4.2	3.4
Saving and investment (in percent of GDP)						
Gross national saving	35.6	36.3	31.3	33.1	32.4	32.4
Gross investment	32.0	31.9	33.5	33.4	32.1	31.8
Private	26.6	24.9	27.2	27.4	25.5	24.8
Public	5.3	7.0	6.2	6.0	6.6	7.0
State budget finances (in percent of GDP) 1/						
Revenue and grants	19.4	18.4	18.7	19.0	18.4	18.5
Expenditure	19.8	21.3	20.1	18.8	19.6	20.2
Expense	14.5	14.3	13.9	12.8	13.0	13.2
Net acquisition of nonfinancial assets	5.3	7.0	6.2	6.0	6.6	7.0
Net lending (+)/borrowing(-) 2/	-0.4	-2.9	-1.4	0.3	-1.3	-1.7
Public and publicly guaranteed debt (end of period)	40.8	41.1	39.1	35.3	33.6	32.3
Money and credit (percent change, end of period)						
Broad money (M2)	14.8	14.5	10.7	6.2	6.1	6.9
Credit to the economy	12.8	11.6	13.5	14.0	9.0	9.7
Balance of payments (in percent of GDP, unless otherwise indicated)						
Current account balance (including official transfers)	3.7	4.3	-2.2	-0.3	0.2	0.7
Exports f.o.b.	79.6	81.6	90.9	91.4	81.6	80.9
Imports f.o.b.	73.2	72.7	86.7	85.0	75.8	75.1
Capital and financial account 3/	5.7	2.4	8.3	2.3	2.5	1.8
Gross international reserves (in billions of U.S. dollars) 4/	78.5	95.2	109.4	86.7	98.7	110.5
In months of prospective GNFS imports	3.5	3.3	3.5	2.9	3.1	3.1
Total external debt (end of period)	37.0	37.6	37.9	36.2	36.6	36.5
Nominal exchange rate (dong/U.S. dollar, end of period)	23,173	23,098	22,826	23,633	...	...
Memorandum items (current prices):						
GDP (in billions of U.S. dollars)	331.8	346.3	369.7	406.5	438.2	476.9
Per capita GDP (in U.S. dollars)	3,439	3,549	3,753	4,087	4,365	4,707

Sources: Vietnamese authorities; and IMF staff estimates and projections.

1/ Follows the format of the Government Finance Statistics Manual 2001. Large EBFs are outside the state budget but inside the general government (revenue amounting to 6-7 percent of GDP).

2/ Excludes net lending of Vietnam Development Bank and revenue and expenditure of Vietnam Social Security.

3/ Incorporates a projection for negative errors and omissions going forward (i.e. unrecorded imports and short-term capital outfows).

4/ Excludes government deposits.

Table 2. Vietnam: Medium-Term Projections, 2019–2028

	2019	2020	2021	2022	Projections 2023	2024	2025	2026	2027	2028
Output										
Real GDP (percent change)	7.4	2.9	2.6	8.0	4.7	5.8	6.9	6.8	6.8	6.8
Output Gap (percent of GDP)	0.4	-0.4	-1.9	-0.1	-1.1	-1.1	-0.6	-0.4	-0.2	0.0
Prices (percent change)										
CPI (period average)	2.8	3.2	1.8	3.2	3.7	3.5	3.5	3.4	3.4	3.4
CPI (end of period)	5.2	0.2	1.8	4.6	4.1	3.4	3.4	3.4	3.4	3.4
Core inflation (period average)	2.0	2.3	0.9	2.7	4.2	3.4	3.0	2.6	2.5	2.5
Core inflation (end of period)	2.8	1.0	0.8	4.9	3.8	3.2	2.8	2.5	2.5	2.5
Saving and investment (in percent of GDP)										
Gross national saving	35.6	36.3	31.3	33.1	32.4	32.4	32.8	33.2	33.4	33.5
Gross investment	32.0	31.9	33.5	33.4	32.1	31.8	32.0	32.2	32.3	32.4
Private	26.6	24.9	27.2	27.4	25.5	24.8	24.7	24.9	25.0	25.0
Public	5.3	7.0	6.2	6.0	6.6	7.0	7.3	7.3	7.3	7.4
State budget finances (in percent of GDP) 1/										
Revenue and grants	19.4	18.4	18.7	19.0	18.4	18.5	18.8	19.0	19.2	19.4
Of which: Oil revenue	0.7	0.4	0.5	0.8	0.6	0.6	0.5	0.5	0.5	0.6
Expenditure	19.8	21.3	20.1	18.8	19.6	20.2	20.8	21.0	21.3	21.4
Expense	14.5	14.3	13.9	12.8	13.0	13.2	13.5	13.7	14.0	14.0
Net acquisition of nonfinancial assets	5.3	7.0	6.2	6.0	6.6	7.0	7.3	7.3	7.3	7.4
Net lending (+)/borrowing(-) 2/	-0.4	-2.9	-1.4	0.3	-1.3	-1.7	-2.1	-2.1	-2.1	-2.0
Net lending /borrowing including EBFs	0.3	-1.8	-0.5	1.1	-0.5	-1.0	-1.5	-1.7	-1.7	-1.8
Public and publicly guaranteed debt (end of period)	40.8	41.1	39.1	35.3	33.6	32.3	31.3	30.7	30.1	29.5
Money and credit (percent change, end of period)										
Broad money (M2)	14.8	14.5	10.7	6.2	6.1	6.9	7.9	8.5	9.0	9.0
Credit to the economy	12.8	11.6	13.5	14.0	9.0	9.7	10.5	10.5	10.5	10.5
Balance of payments (in percent of GDP, unless otherwise indicated)										
Current account balance (including official transfers)	3.7	4.3	-2.2	-0.3	0.2	0.7	0.8	1.0	1.1	1.1
Exports f.o.b.	79.6	81.6	90.9	91.4	81.6	80.9	82.2	84.4	86.7	89.0
Imports f.o.b.	73.2	72.7	86.7	85.0	75.8	75.1	76.5	78.6	80.9	83.3
Capital and financial account 3/	5.7	2.4	8.3	2.3	2.5	1.8	1.5	1.4	1.4	1.5
Gross international reserves (in billions of U.S. dollars) 4/	78.5	95.2	109.4	86.7	98.7	110.5	122.7	136.3	151.5	168.6
In months of prospective GNFS imports	3.5	3.3	3.5	2.9	3.1	3.1	3.1	3.1	3.1	3.1
Total external debt (end of period)	37.0	37.6	37.9	36.2	36.6	36.5	36.2	35.8	35.4	35.0
Nominal exchange rate (dong/U.S. dollar, end of period)	23,173	23,098	22,826	23,633	...	...	...	...	...	...
Memorandum items (current prices):										
GDP (in billions of U.S. dollars)	331.8	346.3	369.7	406.5	438.2	476.9	520.8	564.8	611.6	662.8
Per capita GDP (in U.S. dollars)	3,439	3,549	3,753	4,087	4,365	4,707	5,097	5,483	5,890	6,334

Sources: Vietnamese authorities; and IMF staff estimates and projections.
1/ Follows the format of the Government Finance Statistics Manual 2001. Large EBFs are outside the state budget but inside the general government (revenue amounting to 6-7 percent of GDP).
2/ Excludes net lending of Vietnam Development Bank and revenue and expenditure of Vietnam Social Security.
3/ Incorporates a projection for negative errors and omissions going forward (i.e. unrecorded imports and short-term capital outfows).
4/ Excludes government deposits.

Table 3. Vietnam: Balance of Payments, 2019–2028

(In billions of U.S. dollars, unless otherwise indicated)

				Prelim.	Projections					
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
Current account balance	12.5	15.1	-8.1	-1.1	1.0	3.2	4.2	5.7	6.6	7.4
Trade balance	21.0	30.7	15.7	25.7	25.4	27.9	29.8	32.2	35.1	38.1
Of which: Oil balance	-3.6	-1.5	-2.1	-6.0	-4.9	-4.7	-4.8	-4.8	-4.9	-5.0
Exports, f.o.b.	264.3	282.6	336.2	371.3	357.5	386.0	428.0	476.4	530.2	590.1
Of which: Oil	2.0	1.6	1.7	2.4	1.9	1.8	1.6	1.5	1.5	1.4
Imports, f.o.b.	243.3	251.9	320.5	345.6	332.1	358.0	398.3	444.2	495.0	551.9
Of which: Oil	5.6	3.1	3.8	8.4	6.8	6.5	6.4	6.4	6.4	6.4
Nonfactor services	-0.9	-10.3	-15.4	-12.6	-10.4	-9.9	-11.1	-12.5	-14.0	-15.8
Receipts	20.4	7.6	5.3	12.9	15.4	17.6	19.1	20.8	22.6	24.5
Payments	21.4	17.9	20.7	25.5	25.8	27.5	30.2	33.3	36.6	40.3
Investment income	-16.8	-14.8	-18.7	-19.7	-20.2	-21.3	-21.8	-22.4	-24.1	-25.9
Receipts	2.2	1.4	1.0	2.3	2.1	2.2	2.3	2.4	2.4	2.3
Payments	19.0	16.2	19.7	22.0	22.2	23.6	24.1	24.8	26.5	28.2
Transfers	9.2	9.5	10.3	5.6	6.2	6.5	7.3	8.4	9.6	11.0
Private (net)	8.7	8.9	9.6	5.0	5.7	6.3	7.2	8.3	9.5	11.0
Official (net)	0.6	0.6	0.7	0.6	0.5	0.2	0.1	0.1	0.0	0.0
Capital and financial account balance	19.0	8.5	30.8	9.5	11.0	8.5	8.0	7.8	8.6	9.7
Direct investment (net)	15.7	15.4	15.3	15.2	14.7	15.5	17.0	18.4	20.0	21.7
Of which: Foreign direct investment in Vietnam	16.1	15.8	15.7	17.9	17.5	18.4	20.1	21.7	23.4	25.3
Portfolio investment	3.0	-1.3	0.3	1.5	0.3	0.4	0.4	0.5	0.5	0.6
Medium- and long-term loans	4.9	2.4	2.8	2.2	2.9	3.4	4.0	3.2	3.2	3.4
Disbursements	13.0	11.5	15.2	15.6	18.7	20.8	22.6	23.7	25.6	27.7
Amortization	8.1	9.1	12.4	13.5	15.8	17.4	18.6	20.5	22.4	24.3
Short-term capital 1/	-4.6	-8.0	12.5	-9.4	-6.9	-10.8	-13.4	-14.2	-15.1	-15.9
Errors and omissions	-8.2	-6.9	-8.4	-31.1	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	23.3	16.6	14.3	-22.7	12.0	11.7	12.2	13.6	15.2	17.1
Memorandum items:										
Gross international reserves 2/	78.5	95.2	109.4	86.7	98.7	110.5	122.7	136.3	151.5	168.6
In months of prospective GNFS imports	3.5	3.3	3.5	2.9	3.1	3.1	3.1	3.1	3.1	3.1
Current account balance (in percent of GDP)	3.8	4.3	-2.2	-0.3	0.2	0.7	0.8	1.0	1.1	1.1
Export value (percent change)	8.4	6.9	18.9	10.5	-3.7	8.0	10.9	11.3	11.3	11.3
Export value (in percent of GDP)	79.6	81.6	90.9	91.4	81.6	80.9	82.2	84.4	86.7	89.0
Import value (percent change)	7.1	3.5	27.2	7.8	-3.9	7.8	11.2	11.5	11.4	11.5
Import value (in percent of GDP)	73.3	72.7	86.7	85.0	75.8	75.1	76.5	78.6	80.9	83.3
External debt	122.7	130.3	140.2	147.2	160.2	174.0	188.5	202.1	216.5	232.0
In percent of GDP 3/	37.0	37.6	37.9	36.2	36.6	36.5	36.2	35.8	35.4	35.0
GDP	331.8	346.3	369.7	406.5	438.2	476.9	520.8	564.8	611.6	662.8

Sources: Vietnamese authorities; and IMF staff estimates and projections.

1/ Incorporates a projection for negative errors and omissions going forward (i.e. unrecorded imports and US dollar currency holdings by residents outside the formal financial sector).

2/ Excludes government deposits.

3/ Uses interbank exchange rate.

Table 4a. Vietnam: Consolidated State Budgetary Operations, 2019-2024 1/

(In trillions of dong)

	2019	2020	2021	Est. 2022	Proj. 2023	Proj. 2024
Total revenue and grants	1496	1479	1587	1810	1914	2124
Tax revenue	1122	1056	1181	1376	1450	1612
Oil revenues	56	32	44	78	63	63
CIT	42	26	32	60	49	49
Natural resource tax	14	6	12	18	15	15
Non-oil tax revenues	1066	1024	1137	1298	1387	1549
PIT	109	115	128	163	178	198
CIT	229	231	286	279	305	340
VAT	363	340	376	445	468	530
Trade	97	79	90	114	112	120
Others	269	259	257	296	324	362
Grants	5	5	17	8	8	8
Other revenue	369	419	389	427	455	504
Expenditure	1527	1710	1708	1786	2044	2316
Expense	1115	1146	1180	1216	1357	1514
Interest	107	106	102	95	97	103
Other expense	1008	1040	1079	1121	1260	1410
Net acquisition of non-financial assets	412	563	528	570	687	803
Net lending (+)/borrowing (-)	-31	-230	-122	24	-131	-192
Net incurrence of liabilities	65	9	-24	60	131	192
Net incurrence of financial liabilities	127	196	53	67	128	189
Domestic	90	165	113	116	127	164
Foreign	37	31	-60	-49	1	25
Disbursement	79	112	-8	61	116	136
Amortization	42	81	53	110	115	111
Net acquisition of financial assets	-62	-187	-77	-7	3	3
of which: Privatization receipts	54	30	4	4	3	3
Statistical discrepancies 2/	-35	221	146	-84	…	…
Memorandum items:						
Net lending/borrowing including VSS	153	-136	-30	117	-39	-103
Net lending/borrowing including EBFs	22	-145	-42	104	-54	-120
Public and publicly guaranteed debt	40.8	41.1	39.1	35.3	33.6	32.3
Primary balance (% GDP)	1.0	-1.5	-0.2	1.3	-0.3	-0.8
Cyclically Adjusted Primary Balance (% potential GDP)	0.9	-1.5	0.1	1.3	-0.1	-0.6
Cyclically Adjusted Non-Oil Primary Balance (% potential GDP)	0.2	-1.8	-0.4	0.4	-0.7	-1.1
Nominal GDP (in trillions of dong)	7707	8044	8480	9513	10412	11466

Sources: Vietnamese authorities; and IMF staff estimates and projections.

1/ Government Finance Statistics 2001 presentation. The baseline projections include assumptions of lower trade-related tax revenue due to international trade agreements, gradual improvements in tax collection, and current plans for SOE equitization/divestment. Figures consolidate central and provincial government accounts, but exclude net lending of Vietnam Development Bank and revenue and expenditure of Vietnam Social Security and other extra-budgetary funds.

2/ Difference between net lending/borrowing and identified below-the-line financing.

Table 4b. Vietnam: Consolidated State Budgetary Operations, 2019-2024 1/

(In percent of GDP, unless otherwise indicated)

	2019	2020	2021	Est. 2022	Proj. 2023	Proj. 2024
Total revenue and grants	19.4	18.4	18.7	19.0	18.4	18.5
Tax revenue	14.6	13.1	13.9	14.5	13.9	14.1
Oil revenues	0.7	0.4	0.5	0.8	0.6	0.6
CIT	0.5	0.3	0.4	0.6	0.5	0.4
Natural resource tax	0.2	0.1	0.1	0.2	0.1	0.1
Non-oil tax revenues	13.8	12.7	13.4	13.6	13.3	13.5
PIT	1.4	1.4	1.5	1.7	1.7	1.7
CIT	3.0	2.9	3.4	2.9	2.9	3.0
VAT	4.7	4.2	4.4	4.7	4.5	4.6
Trade	1.3	1.0	1.1	1.2	1.1	1.0
Others	3.5	3.2	3.0	3.1	3.1	3.2
Grants	0.1	0.1	0.2	0.1	0.1	0.1
Other revenue	4.8	5.2	4.6	4.5	4.4	4.4
Expenditure	19.8	21.3	20.1	18.8	19.6	20.2
Expense	14.5	14.3	13.9	12.8	13.0	13.2
Interest	1.4	1.3	1.2	1.0	0.9	0.9
Other expense	13.1	12.9	12.7	11.8	12.1	12.3
Net acquisition of non-financial assets	5.3	7.0	6.2	6.0	6.6	7.0
Net lending (+)/borrowing (-)	-0.4	-2.9	-1.4	0.3	-1.3	-1.7
Net incurrence of liabilities	0.8	0.1	-0.3	0.6	1.3	1.7
Net incurrence of financial liabilities	1.7	2.4	0.6	0.7	1.2	1.7
Domestic	1.2	2.1	1.3	1.2	1.2	1.4
Foreign	0.5	0.4	-0.7	-0.5	0.0	0.2
Disbursement	1.0	1.4	-0.1	0.6	1.1	1.2
Amortization	0.5	1.0	0.6	1.2	1.1	1.0
Net acquisition of financial assets	-0.8	-2.3	-0.9	-0.1	0.0	0.0
of which: Privatization receipts	0.7	0.4	0.0	0.0	0.0	0.0
Statistical discrepancies 2/	-0.5	2.7	1.7	-0.9	...	...
Memorandum items:						
Net lending/borrowing including VSS	2.0	-1.7	-0.4	1.2	-0.4	-0.9
Net lending/borrowing including EBFs	0.3	-1.8	-0.5	1.1	-0.5	-1.0
Public and publicly guaranteed debt	40.8	41.1	39.1	35.3	33.6	32.3
Primary balance	1.0	-1.5	-0.2	1.3	-0.3	-0.8
Cyclically Adjusted Primary Balance (% potential GDP)	0.9	-1.5	0.1	1.3	-0.1	-0.6
Cyclically Adjusted Non-Oil Primary Balance (% potential GDP)	0.2	-1.8	-0.4	0.4	-0.7	-1.1
Nominal GDP (in trillions of dong)	7,707	8,044	8,480	9,513	10,412	11,466

Sources: Vietnamese authorities; and IMF staff estimates and projections.

1/ Government Finance Statistics 2001 presentation. The baseline projections include assumptions of lower trade-related tax revenue due to international trade agreements, gradual improvements in tax collection, and current plans for SOE equitization/divestment. Figures consolidate central and provincial government accounts, but exclude net lending of Vietnam Development Bank and revenue and expenditure of Vietnam Social Security and other extra-budgetary funds.

2/ Difference between net lending/borrowing and identified below-the-line financing.

Table 5. Vietnam: Monetary Survey, 2019-2024 1/

(In trillions of dong, unless otherwise indicated)

					Proj.	
	2019	2020	2021	2022	2023	2024
Net foreign assets	2,131	2,642	2,737	2,361	2,750	3,164
State Bank of Vietnam (SBV)	1,813	2,199	2,536	2,049	2,379	2,694
Commercial banks	319	443	200	312	371	470
Net domestic assets	8,443	9,469	10,665	11,866	12,351	12,985
Domestic credit	8,583	9,647	10,860	12,103	13,289	14,693
Net claims on government	257	354	312	80	181	313
SBV	-276	-485	-551	-450	…	…
Credit institutions	533	839	863	530	…	…
Credit to the economy	8,326	9,293	10,548	12,023	13,107	14,380
Claims on state-owned enterprises (SOEs)	450	465	443	425	…	…
Claims on other sectors	7,877	8,829	10,105	11,598	…	…
In dong	7,847	8,794	9,966	11,509	…	…
In foreign currency	480	499	583	514	…	…
By state-owned banks (SOCBs)	3,911	4,251	4,731	5,348	…	…
By non-SOCBs	4,415	5,042	5,817	6,675	…	…
Other items net	-140	-178	-195	-237	…	…
Total liquidity (M2)	10,574	12,111	13,402	14,227	15,101	16,149
Dong liquidity	9,718	11,141	12,467	13,193	…	…
Deposits	8,520	9,803	10,947	11,840	…	…
Currency outside banks	1,198	1,338	1,520	1,353	…	…
Foreign currency deposits	856	969	936	1,034	…	…
Memorandum items:						
Reserve money (year-on-year percent change)	24.0	10.0	12.5	-13.1	6.1	6.9
Liquidity (M2; year-on-year percent change)	14.8	14.5	10.7	6.2	6.1	6.9
Currency/deposits (in percent)	12.8	12.4	12.8	10.5	…	…
Credit/deposits (total, in percent)	88.8	86.3	88.8	93.4	…	…
Credit/deposits (dong, in percent)	92	90	91	97	…	…
Credit/deposits (foreign currency, in percent)	56	51	62	50	…	…
Credit to the economy						
Total (in percent of GDP)	108.0	115.5	124.4	126.4	125.9	125.4
Total (year-on-year percent change)	12.8	11.6	13.5	14.0	9.0	9.7
In dong (year-on-year percent change)	13.5	12.1	13.3	15.5	…	…
In FC (year-on-year percent change)	2.5	4.0	16.8	-11.7	…	…
In FC at constant exchange rate (year on year percent change)	1.6	4.6	18.2	-13.9	…	…
To SOEs (year-on-year percent change)	-5.0	3.3	-4.6	-4.0	…	…
To other sectors (year-on-year percent change)	14.1	12.1	14.5	14.8	…	…
To SOEs (percent of total)	5.4	5.0	4.2	3.5	…	…
Nominal GDP (in trillions of dong)	7,707	8,044	8,480	9,513	10,412	11,466

Sources: SBV; and IMF staff estimates and projections.

1/ Includes the SBV and deposit-taking credit institutions.

Table 6. Vietnam: Financial Soundness Indicators, 2018-2022

(In percent)

	2018	2019	2020	2021	2022
Regulatory Capital to Risk-Weighted Assets	11.9	11.8	11.1	11.3	11.5
Regulatory Tier 1 Capital to Risk-Weighted Assets	9.4	9.4	9.5	9.6	10.1
Non-performing Loans Net of Provisions to Capital	9.3	7.5	8.0	4.3	9.1
Non-performing Loans to Total Gross Loans 1/	2.1	1.8	1.9	1.6	1.9
Return on Assets	1.2	1.2	1.2	1.5	1.1
Return on Equity	12.3	12.4	11.9	14.9	13.9
Interest Margin to Gross Income	70.0	68.6	68.7	67.0	70.8
Non-interest Expenses to Gross Income	48.9	47.1	47.4	40.2	42.0
Liquid Assets to Total Assets (Liquid Asset Ratio)	11.3	11.7	11.3	10.3	9.2

Source: Financial Soundness Indicators (FSI)

1/ Excluding restructured and VAMC loans.

Annex I. Progress Against IMF Recommendations

Policies	2022 Article IV Consultations Recommendations	Actions Since 2022 Article IV Consultations
Fiscal Policy	Fiscal policy should strike a balance between providing temporary, targeted support and facilitating economic transformation.	To a large extent, fiscal support in 2022 delivered through the Program for Recovery and Development (PRD) focused on investment in infrastructure and temporary tax cuts. There was more limited spending on housing support, childcare, training and job search assistance.
	Fiscal policies should be agile given fluid economic conditions	The fiscal balance was tighter than expected as the economic recovery in 2022 was stronger than expected at the time of the 2022 Article IV.
	Longer-term spending priorities should promote more inclusive growth.	Vietnam and development partners agreed to a USD15.5 billion Just Energy Transition Partnership. Work on Vietnam's climate change reform plan is underway to achieve net zero emission by 2050. The 2023 budget includes large public investment increases.
	Revenue mobilization efforts are critical to accommodate higher development spending.	The MOF conducted assessments of the implementation of key tax laws (including CIT, Excise, VAT, PIT, environmental tax, land taxes, natural resource tax, export and import tax) and collected comments on amendments of these laws to raise revenue intake over the medium term by strengthening tax administration, especially in e-commerce and digital businesses, broadening VAT base, raising some excise taxes, and amending tax incentives.
	Strengthen public financial management frameworks.	A comprehensive Treasury modernization program is underway, focusing on: budget execution, active cash management, internal audit, re-designing the Charter of Accounts, improving information system. But, weaknesses remain on fiscal accounting and reporting.
	Pension reforms are needed to address unfunded pension liabilities and improve the coverage, adequacy, sustainability, and fairness of pensions.	An ongoing CD assistance on social security fund reform focuses on improving the coverage of pension fund. Training on pension fund modeling is also being conducted to support VSS in forecasting its long-term financial position to ensure its sustainability.
Monetary Policy	Monetary policy should be data dependent, forward looking, and increasingly vigilant of rising inflation risks.	Monetary policy was tightened in second half of 2022 to contain inflation and mitigate exchange rate depreciation pressures. The policy was loosened in early 2023 as headline inflation receded.
	Greater exchange rate flexibility	In October 2022, the FX trading band was widened to +/-5 percent from +/-3 percent.
	Continue to modernize the monetary framework.	The modernization of the monetary policy framework is ongoing, with the SBV enhancing its analytical and forecasting capacity through IMF-supported FPAS TA.

Policies	2022 Article IV Consultations Recommendations	Actions Since 2022 Article IV Consultations
Financial Sector Policies	Close monitoring of risks in the banking sector, and loan classification and provisioning rules should be normalized.	SBV has been closely monitoring risks in the banking sector and acted swiftly to contain contagion from the bank run. Loan classification and provisioning rules have been normalized for loans restructured after January 1, 2023. Full normalization of accounting and provisioning rules will take effect on January 1, 2024.
	Enhance banking sector resilience.	Adoption of Basel II is continuing. The amendments to the law on Credit Institutions are being debated.
	Strengthen the macroprudential framework.	Macro-prudential measures to limit risks from real estate and consumer loans and reduce maturity mismatches were introduced.
	Strengthen AML system	A new AML-CFT law was passed and came into effect in March 2023, but it does not fully address the shortcomings identified. Documents guiding the implementation of the AML-CFT law have also been issued.
	Deepening capital markets	In September 2022, Vietnam revised the rules on corporate bond issuances toward more transparency and limited the participation of small retail investors. However, as the corporate bond market was a facing severe liquidity issues, a March 2023 decree delayed the credit rating requirement and the limits on retail investors to January 1, 2024.
	Harness digital transformation	Vietnam has made progress toward digital transformation in both public service and business. More public services can be provided through the e-government Portal, including tax and customs services, and a national personal identification has been introduced.
Structural policies	Improve further the business environment and reduce corruption.	Vietnam is working on amendments of several economic laws, including: credit institutions, land, real estate business, housing law, and e-commerce. The government is further promoting e-government, reducing regulations and licensing requirements to simplify and improve the business environment.
	Improve the quality of the labor force and reduce skill mismatches	Limited vocational training and job search assistance was undertaken under the PRD.

Annex II. Integration of Capacity Development Assistance in Surveillance

Overview

1. **To achieve its ambitious development objectives, Vietnam needs to continue to modernize its economic institutions**. The IMF and other development partners are actively engaged in their respective areas of expertise and are coordinating regularly.

2. **CD has been well integrated with IMF surveillance**. High-quality CD remains central in strengthening the effective implementation of IMF policy advice and engagements with the authorities. The main surveillance priorities include modernizing policy frameworks, enhancing financial stability, and improving data quality and transparency to help Vietnam transition to the next phase of its development.

3. **Fund CD assistance focuses on Vietnam's ambitious reform agenda**. IMF CD assistance is playing a key role in SBV's plan to modernize its monetary policy framework via the FPAS. A FSSR was undertaken and a broad reform roadmap was design to help enhance financial stability. The IMF stands ready to continue helping the SBV strengthen financial stability. In the field of public finance, the IMF continues to support the authorities' efforts to strengthen treasury management, domestic revenue mobilization, tax administration, and public debt management. IMF technical assistance will also continue to support the authorities' initiatives to improve the coverage, quality, and timeliness of fiscal statistics. Vietnam has also benefitted from IMF TA and capacity building on AML/CFT, central bank digital currency, cybersecurity, pension fund reform, customs modernization, and climate policies.

Table 1. Vietnam: Integrating Fund Surveillance and Capacity Development		
Area	**Surveillance Recommendations**	**Capacity Development Recent Actions/Plans**
Monetary policy	Continue to modernize the monetary policy framework.	Phase 1 on the Forecasting and Policy Analysis System (FPAS) on enhancing analytical and forecasting capacity was successfully completed. Phase II on integration to policy discussion started in April 2022.
Financial Policy	Strengthen the resilience of the banking sector and modernize the macroprudential framework.	A Financial Sector Stability Review was undertaken in 2022 and identified gaps in the financial sector infrastructure, policies, and statistics.
Central bank governance	Strengthen the central bank capacity on internal audit toward more transparence and risk-based management	TA on strengthening SBV internal audit started in August 2022 and aims at developing capacity in the application of risk-based internal auditing.
Tax Policy	Strengthen revenue mobilization by enhancing tax policy	The property tax CD is ongoing.
Tax Administration	Strengthen revenue mobilization by improving tax administration	The Fund continues to work closely with General Taxation Department on the implementation of the Tax System Reform Strategy for 2021-2030. A multiple-year CD program is ongoing with priorities given to further support compliance on risk management and improvement of core tax administration functions.
Treasury management	Improve public financial management and fiscal data, accounting and reporting.	The Vietnam State Treasury received TA on implementation of its Modernization Strategy for 2021-30, including internal audit, improvement of Chart of Accounts and cash management. CD assistance has also been provided in improving quality of financial reports, shortening timing of state budget finalization report and upgrading Treasury's Financial Management Information System.

Table 1. Vietnam: Integrating Fund Surveillance and Capacity Development (Concluded)

Debt management	Improve public debt management, accounting and reporting.	Helped improve public debt management and reporting by providing training on the development of a Medium-Term Debt Strategy, as well as review current institutional arrangements for public debt management. Helped the MOF to assess its legal framework regarding external debt statistics and develop a roadmap for improvement of external debt statistics by currency and residency.
Social Security Fund management	Expanding social security coverage	A potential multi-year CD program with the Vietnam Social Security Fund (VSS) on expanding the social security coverage. Provided training courses to VSS to help project its long-term financial position and distributional features of public pensions.
Customs modernization	Strengthening compliance management and enforcement in Customs	Assisted General Department of Vietnam Customs (GDVC) in strengthening compliance management. Regarding enforcement function, the CD assistance will focus on intelligence, surveillance, and criminal investigation.
Data and statistics	Improve the coverage, quality, transparency, and timeliness of statistics.	TA and training continue in the following areas: transitioning Vietnam's state budget data to Government Financial Statistics Manual 2014 (GFSM 2014) and publishing budget data for 2020-21, in line with GFSM 2014; macroeconomic analysis and forecasting, national accounts, monetary and financial data reporting; and external sector statistics.
AML/CFT	AML/CFT framework and execution should be strengthened in line with the FATF standards to address key country risks.	A multi-year TA program to help resolve gaps has been agreed. The TA program has started with a scoping mission in November 2022
Macroeconomic Framework	Strengthening the capacity of macroeconomic analysis and forecasting.	The scoping mission identified areas of improvement and formulated a multi-year CD action plan.

Annex III. Impact of an Interest Rate Shock on the Corporate Sector in Vietnam[1]

This annex examines the impact of an interest rate shock on the default risk of the non-financial corporate sector in Vietnam. Simulations suggest that a 20 percent increase in borrowing costs could increase the share of firms- and debt-at-risk by 11 and 13 percentage points, respectively. Small and micro firms are most vulnerable to interest rate hikes. Although larger firms can weather the shock better, their high leverage ratios remain a concern.

1. Vietnamese firms were vulnerable to interest rate shocks even prior to the pandemic. The share of debt-at-risk (i.e., the debt of firms with interest coverage ratio, or ICR, less than 1) is used as a metric of firms' debt service capacity.[2] An ICR lower than 1 means that operating earnings are insufficient to cover interest payment obligations, which is taken as a proxy for high default risk. Calculations based on 150 thousand firms in the Orbis database show that 42 percent of firms in 2020 were at risk (ICR<1), a small increase from the 39 percent in 2019. Total debt of these firms stood at 37.3 percent of total corporate debt in Vietnam. This is consistent with Kroeger et al. (2020), who report a share of firm- and debt-at-risk of 33.5 percent and 28.7 percent, respectively, in 2017.[3]

2. Three simulations quantify the impact of interest rate hikes of different magnitude on firms' default risk. The scenarios consider rising firms' interest payments resulting in average borrowing rates increasing by 20 percent (Scenario 1), 40 percent (Scenario 2), and 60 percent (Scenario 3). With a calculated borrowing rate of 6.6 percent on average in 2020 (baseline), the shocks imply borrowing rates of 7.9, 9.2, and 10.6 percent, on average, in the three scenarios.[4]

3. According to the simulation, more than 10 percent of firms (and debt) would be re-classified as high risk due to the interest rate hikes in Scenario 1. A 20 percent rise in borrowing rates would increase the share of firms-at-risk (ICR<1) by 12 percentage points, making 53.2 percent of firms at risk of default. Correspondingly, 49 percent of total debt (an additional 13 percentage points compared to the baseline scenario) would be categorized as risky under Scenario 1. Firms- and debt-at-risk are expected to continue rising if interest rates increase further as in Scenario 2 and Scenario 3, but at a slower pace. This suggests that a non-negligible share of firms is at the edge of

[1] Prepared by Anh Thi Ngoc Nguyen, Federico Díez, and Giacomo Magistretti.

[2] Interest coverage ratio is defined as earnings before tax and interest payment (EBIT) over interest payment.

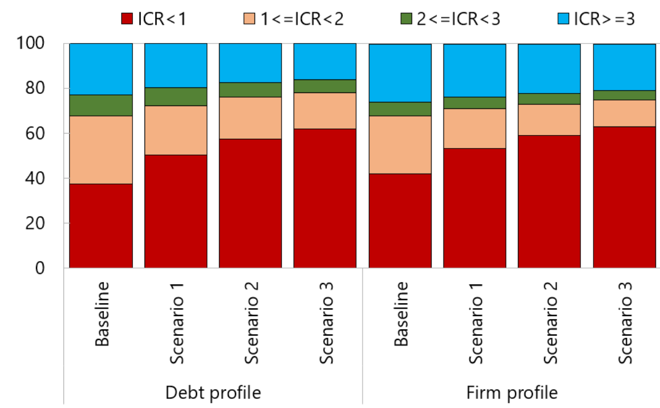
[3] See Thilo Kroeger, Anh Thi Ngoc Nguyen, Yuanyan Sophia Zhang, Pham Dinh Thuy, Nguyen Huy Minh, and Duong Danh Tuan, 2020, "Corporate Vulnerabilities and Implications of COVID-19,", *IMF Working Paper* No.20/260.

[4] By using 2020 data, the latest available year with good coverage at the time of writing, the exercise assumes that debt and profits remained constant since then. If profit growth was higher than debt growth in 2021-22, then the simulations would be an upper bound of the true effect. Conversely, if debt grew faster than profits in 2021-22, which would be consistent with the last five years of pre-pandemic data, then the impact of the shock would be more severe than what is calculated in this annex.

the ICR threshold cutoff, and even a relatively small hike in interest rate would put them in danger of default.

Debt profile and Firm Profile by Scenario

(Based on the categorization of ICR, percent)



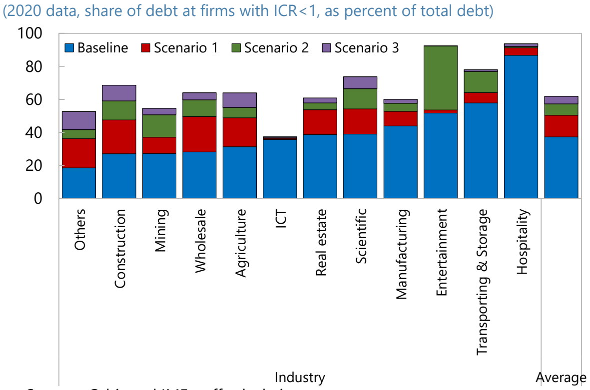
Sources: Orbis and IMF staff calculations.

4. **Smaller firms, and firms in sectors such as construction, wholesale trade, and real estate are most vulnerable to interest rate shocks (Figure 1)**. These industries would likely witness more than 10 percentage point increases in the share of debt at risk under Scenario 1. Small and micro firms would suffer disproportionately from interest shocks, with over 20 percent of debt re-categorized at high risk of default even under a relatively mild increase in borrowing rates.

Figure 1. Vietnam: Simulation Results

Simulation: Debt at Risk by Industry

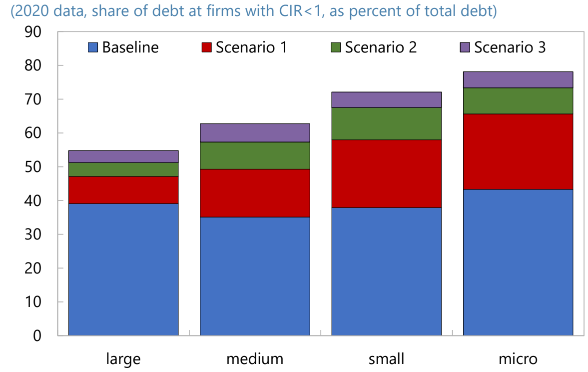
(2020 data, share of debt at firms with ICR<1, as percent of total debt)



Sources: Orbis and IMF staff calculations.

Simulation: Debt at Risk by Firm Size

(2020 data, share of debt at firms with CIR<1, as percent of total debt)

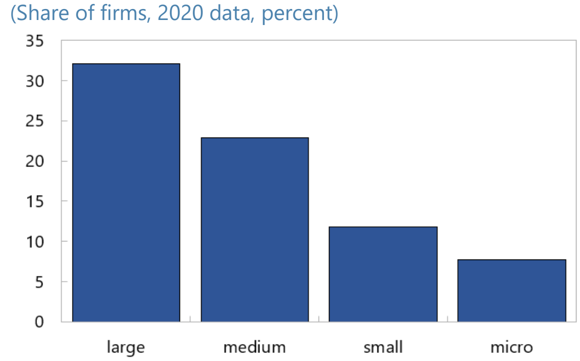


Sources: Orbis and IMF staff calculations.

5. **Some firms, particularly larger firms, have sufficiently high financial revenue to cover their interest payments**. Since firms' financial revenues comprise interest earnings and investment income, higher interest rates could potentially benefit firms holding a high share of interest-bearing assets. In 2020, around 10 percent of firms had positive net interest revenues, defined as the difference between financial income and interest payments. This implies that an increase in interest rates would

Positive Net Interest Revenues by Firm Size

(Share of firms, 2020 data, percent)



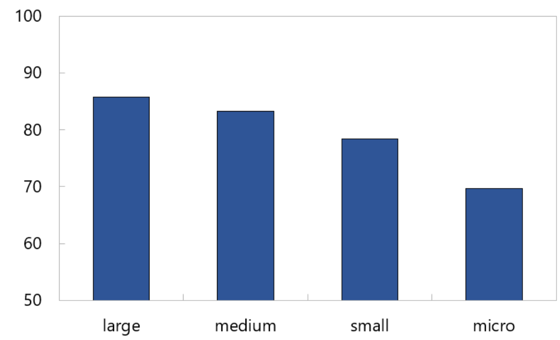
Sources: Orbis and IMF staff calculations.

benefit these firms, at least in terms of their financial activities.[5] Large firms (in terms of employees) would disproportionately benefit, as 32 percent of them had positive net interest revenues compared to only 7 percent of micro firms.

6. However, large firms are also more leveraged, pointing to possible pockets of vulnerability. Large firms have the highest ratios of current liabilities to current assets. This observation partly reflects their greater ability to tap financial markets as compared to smaller firms, which are more likely to rely on retained earnings. That said, in the current context of uncertainty and economic slowdown, some large firms could become more vulnerable to increasing borrowing costs unless their working capital needs are carefully managed.

Leverage Level by Firm Size

(Current liabilities to current assets ratio, 2020 data, percent)



Sources: Orbis and IMF staff calculations.

[5] Interest rate hikes will likely negatively impact operational income, leaving the net effect a priori indeterminate.

Annex IV. Exchange Rate Pass-Through to Inflation in Vietnam[1]

This annex provides two pieces of evidence on the impact of changes in the VND/USD exchange rate (ER) on the CPI in Vietnam. First, it shows the correlation between ER and price changes was substantial during the last major depreciation episode in 2010-11. Second, it estimates an exchange rate pass-through (ERPT) to CPI inflation in ASEAN countries, including Vietnam, of 0.3 percentage points 12 months after a 10 percent change in the ER, increasing to 1.7 in case of depreciations. These findings imply that falls in the value of the dong can have meaningful consequences for inflation.

1. It is challenging to quantify the ERPT in Vietnam based on recent data. Tight regulation of prices of fuel and electricity, limited ER volatility, and low inflation in the past decade prevent an accurate quantification of the ERPT in Vietnam. Mindful of these constraints, the analysis in this annex first documents the co-movement between the ER and inflation in the last major episode of ER depreciation and inflation in 2010-11. Second, it estimates the ERPT in ASEAN countries, an informative benchmark given that Vietnam has an import share in household consumption—a proxy for the preconditions that make the ERPT relevant in a country—of 15 percent, similar to the median among ASEAN countries.[2]

Step 1. Exchange Rate and Inflation in Vietnam

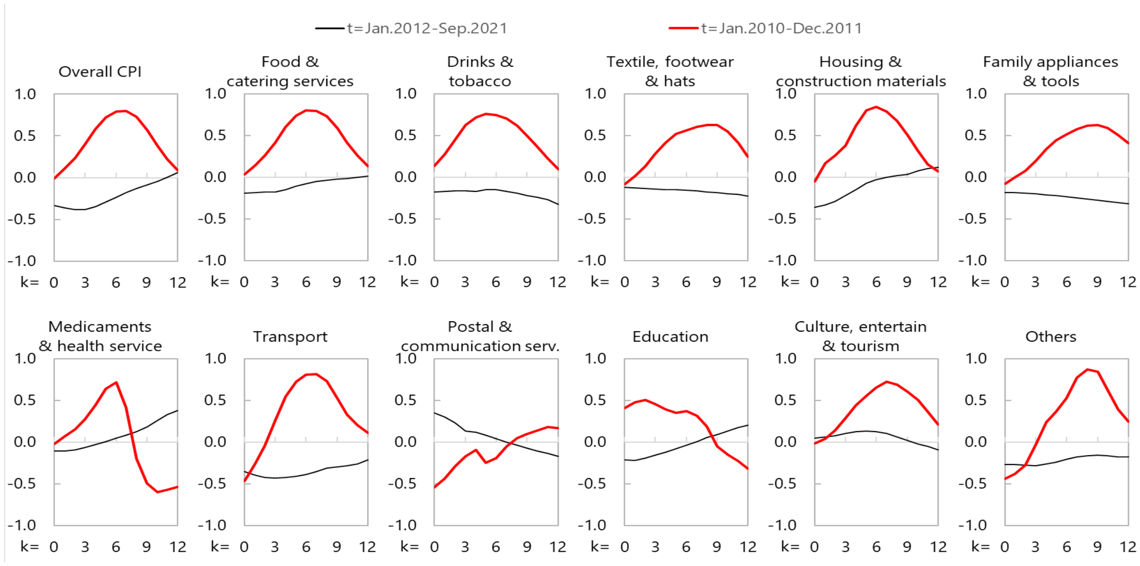
2. Inflation picked up sharply in 2010-11, a few months after sharp ER depreciation. The top-left panel in Figure 1 shows that while there has been no significant co-movement recently, the time-difference correlation between ER depreciation and overall CPI inflation was large and strongly positive during the 2010-11 period, peaking at over 0.8 about six months after the depreciation.[3] The correlation was the highest for transport and housing (including fuel for cooking and electricity)—CPI categories with a direct connection to fuel, a large share of which is imported and priced in dollars—and food and catering services—mostly impacted by a stronger dollar through rising costs of imported fertilizer, animal feed, and transportation.

[1] Prepared by Faizaan Kisat, Giacomo Magistretti, and Ryoichi Okuma.

[2] Estimated from input-output tables published by the Asian Development Bank, the median import share in household consumption is calculated as the share of imported inputs over total inputs into household demand in 2020.

[3] The dong depreciated by about 13 percent against the dollar between January and December 2010.

Figure 1. Vietnam: Correlation between ER and CPI in Vietnam



Source: Vietnam authorities and IMF staff calculations.

Note: Correlations are calculated between the year-on-year percent changes in ER and CPI, with ER leading CPI by k months. The ER is the interbank one (monthly average), a proxy for the actual rate faced by firms and households.

Step 2. Estimating the ERPT for ASEAN Countries

3. **Inflation in ASEAN countries increases by 0.3 percentage points one year after a 10 percent change in the ER, and by 1.7 percent after depreciations**. Local projections are used to trace out impulse responses for the ERPT in ASEAN countries since 2000.[4] The pass-through coefficients can be interpreted as the percent (age point) change in CPI inflation 0–12 months after a percent (age point) change of the exchange rate. In the baseline model, the ERPT is estimated as a 0.3 percentage points increase in inflation after a 10 percent depreciation (Figure 2, left panel).[5] When condensing only depreciation episodes, the ERPT is estimated at 1.7 percent 12 months after a 10 percent ER decline (Figure 2, right panel), substantially larger than the baseline estimate. The ERPT for appreciations is much lower and close to zero up to 3 months after the shock, before turning negative and reaching about -0.9 percent 12 months after a 10 percent ER appreciation. This

[4] The countries in the sample include Brunei (2000-2022), Indonesia (2000-2022), Lao PDR (2000-July 2021), Malaysia (July 2005-2022), Philippines (2000-2022), Singapore (2000-2022), Thailand (2000-2022), and Vietnam (2000-2022). The empirical model estimated follows Caselli and Roitman (2016):

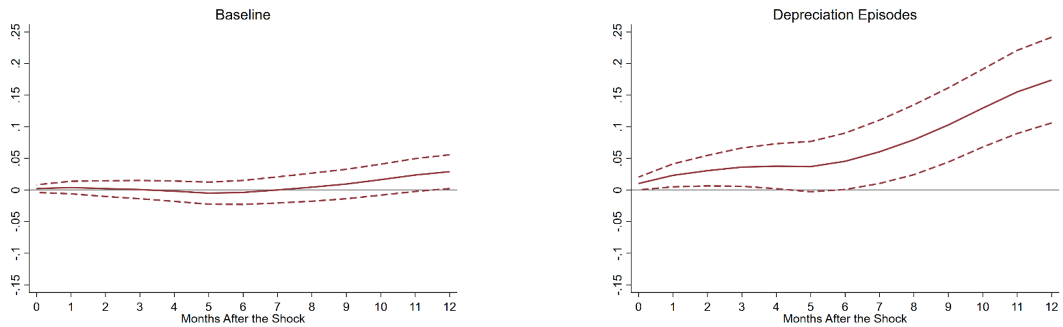
$$\Delta cpi_{i,t+h} = \alpha + \beta_h \Delta ER_{it} + \sum_{s=1}^{p} \rho_s \Delta cpi_{i,t-s} + \sum_{s=1}^{p} \gamma_s \Delta cpi_{i,t-s}^{US} + \mu_i + \varepsilon_{i,t+h}$$

where $\Delta ER_{i,t}$ is the y-o-y percent change in the nominal ER relative to the US dollar in country i at month t (a positive value for $\Delta ER_{i,t}$ represents a depreciation of the local currency). $\Delta cpi_{i,t}$ is the y-o-y percent change in the domestic CPI, and $\Delta cpi_{i,t}^{US}$ is the yoy percent change in the US CPI (a proxy for foreign prices). Both domestic and foreign prices are included with a lag of six periods (i.e., $p = 6$). μ_i are country fixed effects. $\varepsilon_{i,t+h}$ is the error term.

[5] These estimates are in line with the literature. Carriere-Swallow, et al. (2016) estimate an ERPT of around 0.1 for Asian EMs for the period 2003-2015. Similarly, Ha, Stocker and Yilmazkuday (2019) estimate an ERPT of 0.08 for emerging market and developing economies over 1998-2017. Both studies also find a broad-based decline in ERPTs since the late 1990s, in line with the relatively moderate ERPT estimates for our sample period.

asymmetry is consistent with previous studies (Bussiere, 2013), and may be explained by export price rigidities being more binding in case of appreciations than depreciations.

Figure 2. Vietnam: ERPT in ASEAN Countries



Sources: Haver and IMF staff calculations
Note: The figure presents results the β_h coefficients, and associated 95 percent confidence intervals, from estimating the equation in the Appendix, where h denotes the number of months after an exchange rate shock.

4. Monetary policy credibility and lower volatility in ER movements dampen the ERPT. The literature finds that countries with more credible central banks or inflation targeting regimes generally display lower ERPTs (Carriere-Swallow, Gruss, Magud, & Valencia, 2016; Caselli & Roitman, 2016), as producers are less likely to raise prices following bursts of depreciation if they believe that the central bank will promptly act to keep inflation stable after an ER shock. The strong focus on inflation containment of ASEAN countries since the early 2000s (Filardo & Genberg, 2009), including by the SBV with the practice of setting annual inflation targets, may have therefore contributed to the relatively low ERPT values estimated in this annex. Existing studies have also documented larger ERPTs following more severe depreciation episodes, which have been less frequent in ASEAN countries in the sample period relative to other emerging markets outside Asia.

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Annex V. Estimating Worker Flows and Labor Market Dynamism[1]

This annex uses the Vietnamese Labor Force Survey to estimate worker flows and explore the dynamism behind headline labor statistics. While overall employment changed little over the years (except during the pandemic), this masks sizable labor fluidity, with around 4.7 percent of the working-age population changing labor status every quarter. Females, youths, and those less educated are the most likely to change. Furthermore, labor market dynamism comes largely from the informal sector while there seems to be barriers to formalization. There are also signs of excessive churning, which makes it costly for firms to invest in labor training, hindering long-term human capital accumulation.

1. **Vietnam's employment recovery from the pandemic has reinforced long-standing questions about the functioning of the labor market**. While headline employment and unemployment numbers have reverted to pre-pandemic levels, labor-skill mismatches, high levels of labor informality, and lack of adequate training of workers remain a concern (IMF, 2022).

2. **The annex utilizes the Labor Force Survey (LFS) to measure labor mobility in Vietnam**.[2] A panel is constructed with individuals observed at two continuous points in time to measure quarterly labor movement rates, including worker flows, job finding rates, and employment exit rate.[3] Data limitations prevent analyzing overall job switching, but it can identify those who move between self-employment and wage jobs as well as those switching between informal and formal jobs—which allows to gauge the magnitude of worker flows within the employment pool.

3. **Aggregate headline employment and unemployment numbers mask a significant degree of labor market churning**. Aggregate data indicate that employment increased, on average, by 254 thousand (or 0.35 percent of working-age population) each quarter in 2018 while the corresponding figure was 4 thousand (0.01 percent of working-age population) for unemployment. However, using the panel LFS for 2017 and 2018, calculations suggest that about 4.7 percent of the working-age population changed their labor status across employment, unemployment, and inactivity in each quarter (Table 1).

Table 1. Vietnam: Gross Worker Flows in Vietnam

Employment → Unemployment	Employment → Inactivity	Unemployment → Employment	Unemployment → Inactivity	Inactivity → Employment	Inactivity → Unemployment	Total
0.3	1.2	0.5	0.2	2.1	0.3	4.7

Note: Gross worker flows are expressed as a percentage of the population aged 15+.

[1] Prepared by Anh Ngoc Nguyen with inputs from Federico Díez.

[2] The LFS survey is an individual-level representative survey conducted on a quarterly basis, with household groups visited over two continuous quarters before being visited again for another two continuous quarters after 6 months.

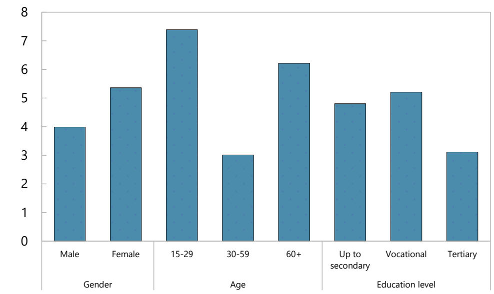
[3] The survey only tracks individuals within a year, and there are almost no continuous data points between years, i.e., in Q4 of the previous year and Q1 of the current year. Therefore, the reported results do not capture labor transitions happening during Q4-Q1 and might suffer from a downward bias as this is the most active period of labor movement.

4. Some demographic groups are more likely to change their labor status:

- *By gender*. Females are more likely to switch labor status: 5.4 percent of working-age females move across employment, unemployment and inactivity within each quarter. The corresponding figure for males is 4 percent.

- *By age*. Youths are the most likely to change their labor status: 7.4 percent of them moves each quarter, while only 3 (6.2) percent of the prime age (older) group change status.

Status-Changing Ratio
(by group, percent)



Sources: Vietnam LFS 2017-18 and IMF staff calculations.

- *By education level*. university graduates or higher tend to stay within their labor status more than those without a tertiary education.

5. Transitions between labor statuses are greatly affected by informality and self-employment—issues that are pervasive in Vietnam.

- **Job-finding rates**. Around 14 percent of the non-employed find a job on a quarterly basis, 88 percent in informal (versus formal) jobs. Roughly 41 percent start as a salaried worker, while 59 are self-employed. Further, the unemployed are more likely to find a job than those inactive,[4] which is in line with the findings by Donovan et al. (2020), that use data from 42 countries. As is typical in developing countries, there is a large share of marginally-attached inactive workers (i.e., who do not actively search for jobs but can easily start working if they happen to find a suitable one). For instance, 18.4 percent of the inactive in Vietnam are marginally-attached, explaining the finding from Table 1 that worker flows between inactivity and employment are much larger than the flows between unemployment and employment. These results also suggest the importance of the inactive as a potential source of labor supply.

- **Employment-exit rates**. Employment-exit rates are estimated to be 1.7 percent. Workers who exit the employment status are mainly self-employed (65 percent) and work informally (87 percent). Upon leaving employment, 25 percent move to the unemployment pool and 75 percent become inactive.

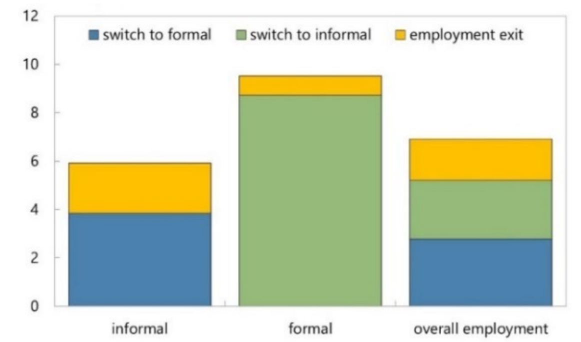
- **Transition rates between self-employment and wage jobs.** The transition rate from self-employment to a wage-earning job is 5 percent, which is rather low relative to peers (Donovan et al 2020). As a large share of self-employed workers in Vietnam work informally with lower wages and limited social protection (Dabla-Norris et al. 2020) than wage workers, this finding could be of concern as it is suggestive of barriers preventing self-employed workers from moving to more secure wage jobs. At the same time, the wage job to self-employment transition rate is 4.8 percent, comparable with peers, and almost cancels out the reverse flow from self-employment to wage jobs.

[4] Among the unemployed, 40 percent found a job within a quarter; this rate is about 11 percent for those inactive.

- **Transition rates for formal-informal work**. Informal work constitutes a large share of total employment, with around 20 percent of workers even in formal firms working informally (Dabla-Norris et al. 2020). The figure shows labor flows as share of total informal, formal, and total employment. Around 6 percent of informal workers change their work status every quarter, either by getting a formal job (3.8 percent) or by exiting from employment (2.1 percent). Further, roughly 10 percent of formal workers change their status quarterly: 8.7 percent get an informal job[5] and 0.8 percent exit employment. Overall, 7 percent of the currently employed either exits employment (1.7 percent) or changes formality status (2.8 percent from informal to formal and 2.4 percent the other way around).

Informal-Formal Transition Rates

(Percentage)



Sources: Vietnam LFS 2017-18 and IMF staff calculations.

6. **The inactive working age population is an important source of labor supply and should be considered as one of key targets for labor market upskilling and training**. While the unemployed have a much higher job-finding rate, the inactivity pool provides three quarters of total new employment given the sizable number of people in the pool.

7. **Labor market churning can affect long term human capital accumulation**. While data limitations preclude an in-depth assessment of job-to-job transitions, transitions between self-employment and wage jobs and between informal and formal work point to excessive churning in the labor market. For instance, the transition rate from a wage job to self-employment is 4.8 percent. Combined with 1.4 percent of wage workers exiting employment, it implies that over 6 percent of wage jobs need to be replaced in a given quarter. Similarly, the formal job exit rate is around 10 percent, so 10 percent of formal jobs need to be re-hired within a quarter. These numbers would be even higher if it were possible to account for workers switching between wage/formal jobs. This high turnover, in turn, creates disincentives for workers and firms to invest in human capital and training, impacting longer term human capital accumulation. As noted in IMF (2022), university-level and vocational-technical skills are under-supplied in Vietnam, and on-the-job skill acquisition does not fill the gap, as few firms provide formal training. Skill mismatches are particularly pronounced for low-skilled and informal workers, reinforcing labor market duality.

8. **Labor fluidity mainly comes from the informal sector, while the formal sector is relatively segmented for the non-employed**. The analysis reveals the presence of bidirectional formal-informal flows within the employment pool. This bidirectional mobility implies a relatively integrated labor market, in line with findings in Dabla-Norris et. al (2020). However, the formal sector is more likely to be segmented and difficult to access for the jobless as flows to the sector

[5] The data suggests that those moving from formal to informal works are less educated, have lower incomes, and are more likely to have worked on the service sector than those staying formal.

from the non-employment pool are limited. Among new workers entering the employment pool, only 12 percent get formal jobs, suggesting that there are barriers that hinder workers from accessing formal jobs. It is also possible that the informal sector serves as a bridge, or "interim training", in which the non-employed first get informal jobs, accumulate experience, and then can move to formal work.

9. These findings point to the need for enhancing active labor policies aimed to address market segmentation and hurdles to finding formal jobs. Improvements in labor training, skill upgrading and job matching for people who are not working are essential. If the segmented formal sector is a result of high costs of hiring, training or firing workers, such that informal jobs are used as a transition mechanism, addressing these distortions would be critical. Overall, both supply and demand side reforms are needed to help remove labor market barriers and facilitate greater labor market dynamism.

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Annex VI. Climate Mitigation: Introducing an Emission Trading System in Vietnam[1]

Achieving net-zero emissions by 2050 will likely require carbon pricing. The government plans to pilot an emission trading system (ETS) in 2025 and make it fully operational by 2028. The ETS will bring many benefits such as on health, pollution, and revenues, while its heterogenous impacts on households and firms could be mitigated through a comprehensive strategy and policy responses during the transition.

1. **Vietnam has committed to mitigating its emissions and shifting away from coal power, including by setting an objective of net-zero emissions by 2050**. Vietnam has historically had very low greenhouse gas (GHG) emissions per capita, but, over the past two decades, it has seen some of the fastest emissions growth rates in the world. From 2000 to 2015, as GDP per capita increased from $390 to $2,000, per capita emissions more than quadrupled. However, the government announced at the 2021 UN Climate Change Conference the intention to achieve net-zero emissions by 2050. Vietnam also committed to end all investment in new coal power generation, scale up deployment of clean power generation, phase out existing coal power by the 2040s, and increase deployment of green technologies.

2. **Achieving net-zero emissions by 2050 in Vietnam would require one of the most ambitious efforts in cutting CO2 emissions among its peers**. A linear emissions pathway to emissions neutrality between 2022 and 2050 would imply reducing GHGs to 333 million tonnes by 2030, a 32 percent reduction relative to 2021 levels, which puts Vietnam among the most ambitious middle-income countries along with Brazil, Mexico, and South Africa in pledging to reduce emissions. In comparison, some middle- and low-income countries (e.g., China, India) currently have non-binding pledges for 2030 (see chart below).

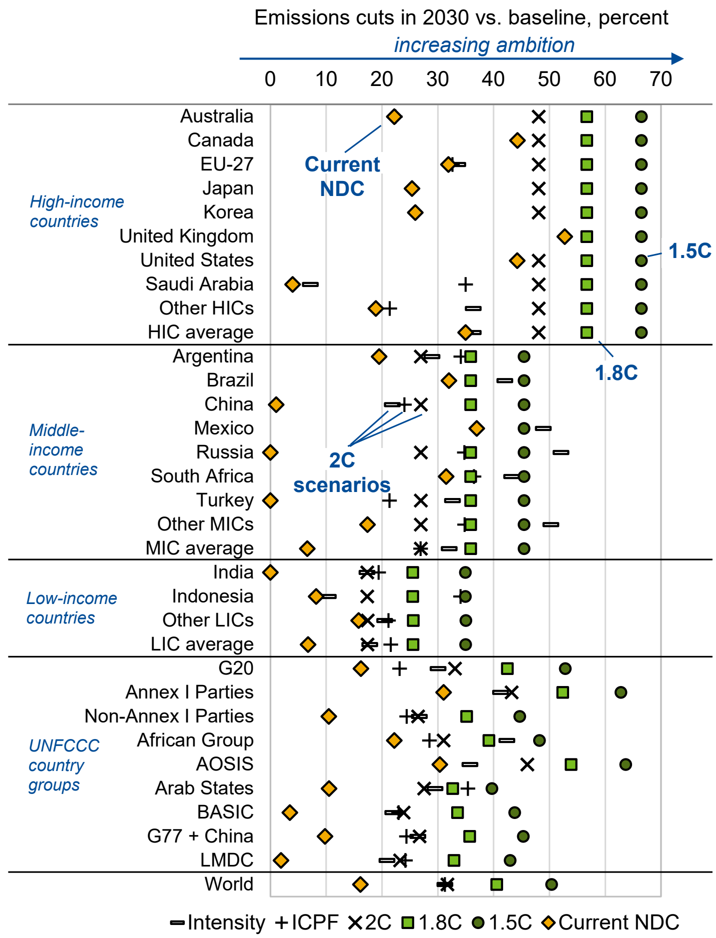
3. **Achieving a substantial emissions reduction will likely require carbon pricing**. The 2020 revised Law on Environmental Protection establishes a mandate for the MOF to design a domestic ETS and a crediting mechanism that encompass a cap, a method of allowance allocation, and domestic and international offsets. The government has decided on an ETS over carbon taxes as the preferred instrument for carbon pricing. A pilot ETS is expected to start by 2025 and to become fully operational by 2028.

[1] Prepared by Antung A. Liu and Yuan Xiao.

Carbon Pricing: Impacts and Responses

4. Pricing carbon would bring many benefits to Vietnam, while its costs could be managed by a gradual introduction and carefully designed accompanying measures. It would help to transition the economy to using more sustainable energy sources, reduce pollution and congestion, benefit the health and quality of living of Vietnamese citizens, generate substantial fiscal revenues that can be invested or spent on public services, and contribute to the global effort to fight climate change. The ETS, through increases in energy costs, would have heterogenous impacts on households and firms, but as the analysis in this annex and international experience show, appropriate policy responses and a good communication strategy would help maximize the net benefits (Box 1).[2] The scenarios below are chosen to illustrate the quantitative implications, but there are many paths to Net Zero by 2050. In fact, many countries use transitional periods to gradually phase in the new policy.

Current and Illustrative CO2 Emissions Cuts for G20 Countries versus 2030 BAU



Source. Black and others (2022).Ax1

5. We examine three scenarios to illustrate the effects of reducing the number of permits that will be available in the ETS along with a coal tax.[3] These three scenarios are presented alongside the Business-As-Usual scenario, where no policies restricting carbon are implemented.[4]

[2] Dabla-Norris et al. (2021).

[3] The quantitative assessment of carbon pricing is based on the Climate Policy Assessment Tool (CPAT). CPAT is a spreadsheet-based model providing projections of fuel use and GHG emissions for the major energy sectors in 188 countries. CPAT, which was developed jointly by IMF and World Bank staff.

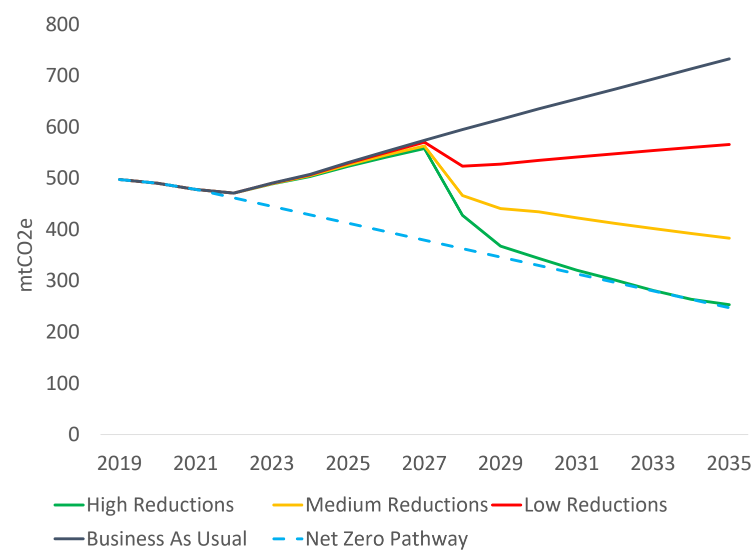
[4] Vietnam's 2022 NDC lists an unconditional emissions target of 781.6 million tons of CO2 equivalent by 2030 and a conditional emissions target of 524.2 million tons. IMF models suggest that these targets will be easy to hit, even under the Business-As Usual scenario. As a result, the 2050 Net Zero target is the focus of this current report.

- *High Reductions Scenario:* the quantity of ETS permits is reduced sufficiently to establish Vietnam on the linear path to Net Zero by 2050. The ETS permits are combined with a $US 10 per gigajoule (GJ) tax on coal (see Table 1.) This coal excise tax shifts more of the increase in price to coal and away from other energy resources.[5]

- *Medium Reductions Scenario:* permits are reduced sufficiently to bring Vietnam two-thirds of the way to the linear path to Net Zero. A $US 6 per GJ excise tax on coal is required in this scenario.

- *Low Reductions scenario:* permits are reduced to bring Vietnam one-thirds of the way to the linear path to Net Zero. In this scenario, a $US 2 per GJ excise tax on coal is required.

Emissions Permits by Scenario



Source: IMF Staff using CPAT.

6. The model assumes that limiting the number of carbon emissions permits and taxing coal will result in a broader set of changes to the economy. As the prices of carbon-intensive sources of energy like coal and gasoline rise, households and firms are incentivized to become more energy efficient, reducing the quantity of energy demanded. Renewable sources of energy like solar power or wind power will become more economical and should expand as a result.

[5] Our policy scenarios include a coal tax because of Vietnam's heavy reliance on coal and the government's intention to shift away from coal power. Coal accounted for about 30 percent of installed capacity, 59 percent of electricity generation, and 71 percent of CO2 emissions in 2020.

Box 1. The International Experience on Carbon Pricing

To date, 70 carbon pricing initiatives in 47 countries have been implemented, covering 23% of global greenhouse gas initiatives in 2022. Carbon pricing, which includes both carbon taxes and emissions trading systems (ETSs) have been implemented in each country in the European Union (EU), China, South Korea, New Zealand, and areas of the U.S.

Prices on carbon vary widely, with most countries pricing emissions in the range of US$20 through US$100 per ton. The most widely used price, from the EU's ETS, was US $83 per ton in 2022. Empirical evidence has consistently found that pricing carbon has resulted in large cuts of emissions (e.g., Bayer and Aklin 2020).

The evidence on the effect of carbon prices on GDP is still emerging. Previously, most macroeconomic models have predicted that a price on carbon will negatively affect economic growth, especially if revenues are not used to invest in other growth-promoting initiatives such as cutting taxes and investing in infrastructure. However, a nascent empirical literature on the experience of countries with carbon prices suggests that the actual effect on GDP has been near zero (Andersson, 2019, Metcalf & Stock, forthcoming). The reasons for the difference between the ex-ante and ex-post literatures are not yet understood.

Many countries adopting an ETS use transitional periods to gradually phase in the new policy. For example, the first two phases of the European Union's ETS lasted between 2005 and 2012. During these phases, the EU targeted a reduction in emissions of 7% from 2005 levels. To further decrease the burden on firms, most allowances were given to firms for free during the first phase. Prices of emissions permits were low during much of these first two phases, limiting the effectiveness of the ETS in reducing emissions. Later ETS systems such as that in California and in New Zealand enacted a price floor, a minimum level by which permits could be bought and sold, to ensure that their policies would be effective in reducing emissions.

To help maintain competitiveness, the EU passed legislation enacting a Carbon Border Adjustment Mechanism (CBAM), expected to enter into force in October 2023. The CBAM will require importers of goods from 5 emission-intensive, trade-exposed sectors to purchase permits based on the carbon intensity of their goods; these permits will be priced at the same level as EU ETS permits. A CBAM is intended to reduce the competitive advantage of importers over domestic producers; firms in jurisdictions without their own carbon price will be most affected.

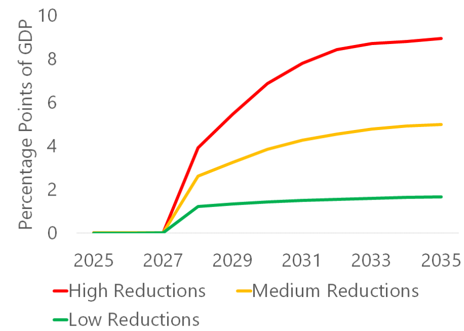
Countries have used the revenues generated on environmental spending, tax cuts, direct transfers, and reducing the deficit. Most countries raise under 1% of GDP in new revenues, with only Uruguay, Bulgaria, Estonia, and Poland reaping revenues higher than that threshold. Spending has also varied widely. Environmental economists have long encouraged governments to use revenues to cut taxes or enact household transfers[1.] Carbon tax revenues have often been used to enact tax cuts, while ETS permit auction revenue has most often been legally earmarked for new initiatives like environmental spending (Marten & van Dender, 2019).

[1] For example, when Iran eliminated fuel subsidies, it also enacted an unconditional cash transfer to households intended to maintain household purchasing power.

7. As expected, pricing carbon will have significant effects on the costs of energy. Depending on the scenario, the price of permits will vary and the number of permits will be reduced. One of the largest sources of energy in Vietnam is oil; its price will rise 96%, 33%, or 7% by 2030 under the high, medium, or low reductions scenarios respectively. Electricity prices will rise by 80%, 50%, or 20% under these scenarios. Because each scenario couples Vietnam's ETS with an excise tax on coal, the largest price increases are reserved for this energy source: coal prices are expected to rise by 443%, 207%, or 60% under each scenario.

8. However, the ETS will also generate substantial revenues for Vietnam, beyond cutting emissions. As the figure illustrates, if emissions permits from Vietnam's ETS are fully auctioned, they can generate substantial revenues. The High Reductions, Medium Reductions, and Low Reductions scenarios are projected to generate new fiscal revenues in the amount of 6.9%, 3.9%, and 1.4% of GDP respectively in 2030. These new revenues are annual and can be used to help achieve Vietnam's development goals and mitigate the impacts of higher energy costs on households and firms.

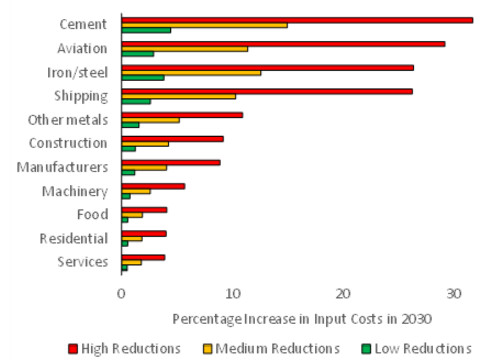
Annual Revenues from Pricing Carbon by Scenario, 2030



Source: IMF Staff using CPAT
Notes: Calculations account for erosion of revenue from pre-existing fuel taxes.

9. In addition to these new fiscal revenues, pricing carbon is expected to produce major co-benefits for Vietnam. Transport co-benefits are realized when higher prices on gasoline and diesel result in less driving of private vehicles and more usage of public transportation decreasing road congestion. Air pollution co-benefits (e.g., reduced deaths from improved air quality) are realized when airborne pollutants in coal, such as sulfur dioxide and particulate matter, are decreased as coal is replaced in Vietnam's energy systems. Liu and Xiao (2023) find that these co-benefits could total 4.5%, 3.0%, or 1.5% of GDP in the High Reductions, Medium Reductions, and Low Reductions scenarios.

Cost Increases for Most-Affected Vietnam Industries



Source: IMF staff calculations.

10. Price increases to energy will have a significant impact on costs for Vietnamese industrial firms. Because the ETS is expected to be phased in between 2028 and 2030, the cost of energy will rise quickly for firms, with larger cost increases for more energy-intensive sectors of the economy. Price increases will be passed through the economy. For example, the price of iron and steel will rise, increasing the costs for purchasers of those products such as construction firms and shipping companies. These increases in price could result in two competitiveness disadvantages if other countries do not enact similar measures. First, domestic producers will be at a cost disadvantage in the domestic market if they pay a price for emissions while foreign producers do not. Second, domestic exporters will be at a disadvantage in foreign markets if they must pay a price for emissions that emitters in other countries do not. The degree of these effects depends on progress in other countries—this is one of the reasons it is critical to have global efforts to address climate change.

Table 1. Vietnam: Energy Price Increases Under Reductions Scenarios, 2030

Fuel	Unit	Baseline price	High Reductions Scenario	Medium Reductions Scenario	Low Reductions Scenario
Gasoline	US$ per liter	0.84	1.15	0.95	0.86
Diesel	US$ per liter	0.65	1.00	0.77	0.68
LPG	US$ per liter	0.73	0.95	0.80	0.74
Kerosene	US$ per liter	0.56	0.88	0.67	0.58
Oil	US$ per barrel	56.9	111.8	75.9	61.1
Coal	US$ per gigajoule (GJ)	4.75	25.8	14.58	7.60
Natural gas	US$ per gigajoule (GJ)	8.89	15.42	11.15	9.39
Electricity	US$ per kwh	0.10	0.18	0.15	0.12

Source. IMF staff using CPAT.

11. To address the issue of competitiveness, a variety of options could be considered. Because rises in energy prices will increase costs to exporters while giving an advantage to importers, the issue of export competitiveness is likely to be important in Vietnam. To address competitiveness, Vietnam might consider a Border Cost Adjustment, where exporters are refunded for the price paid for permits as goods cross the border. The EU is currently enacting a Carbon Border Adjustment Mechanism, and a BCA in Vietnam would ensure that it keep carbon revenues when exporting to the EU. However, this is a complex framework that requires building significant capacity. It might also consider exempting export-dependent, energy-intensive sectors from the ETS, as many countries have done for at least a few years after a new ETS.

12. Several complementary policy tools could address the issue of leakage. Leakage can occur if firms leave Vietnam because costs have risen too much. Vietnam could consider giving incumbent firms free allowances, as was done in Korea, New Zealand, and the EU. Alternatively, Vietnam could use a Tradeable Permit System in some industries, as was done in China and Canada. Finally, Vietnam could consider recycling ETS revenues, returning funds to trade-exposed firms in the form of lump sum transfers, tax cuts, or output-based rebates. When deciding on the approach will need to consider the different trade-offs, including the use of ETS revenues as discussed below.

13. The ETS needs to be accompanied by other policies to help households during the transition.[6] The effect of the High Reductions scenario on household consumption is displayed in the first panel of Figure 1.[7] While increases in the cost of electricity and of gasoline reduce

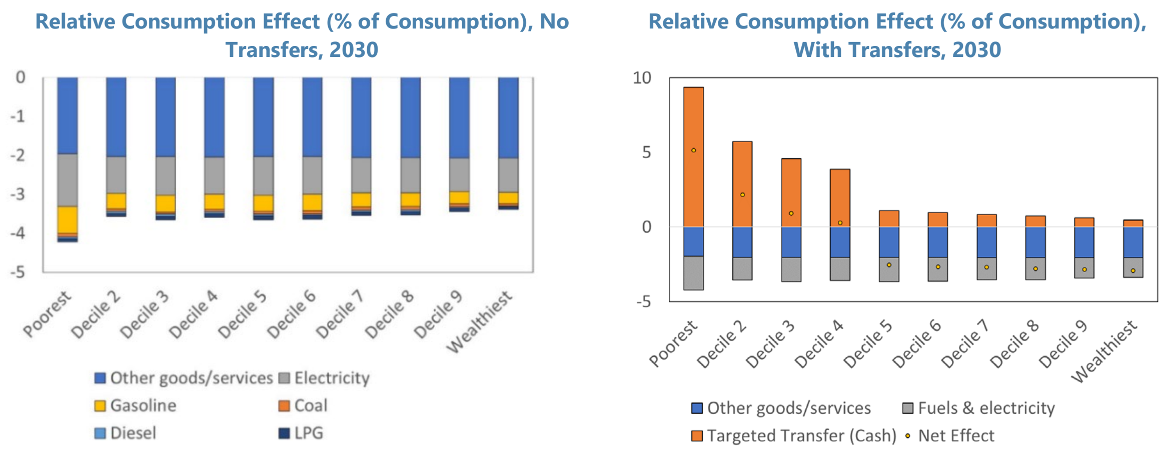
[6] The ETS will have the effect of increasing coal prices, negatively impacting the coal mining industry. ETS revenues could also be deployed for transition assistance for displaced workers from affected industries.

[7] To analyze the effect of carbon pricing on Vietnamese households, we begin by analyzing their patterns of consumption from the Vietnam Household Livings Standards Survey of 2016. After dividing households into deciles, we then analyze the energy intensity of the bundles of consumption for each of these deciles.

household consumption, increases in prices of other goods consumed have the largest negative impact. Because poorer households spend larger fractions of their incomes on energy, they are most hurt by rises in energy prices. An ETS with no accompanying reforms is regressive and is likely to be unpopular.

14. The simulation suggests that targeted transfers using revenues from the ETS could leave the poorest households better off, more than compensating for increases in energy prices. Using revenues for targeted transfers and public investment could make the policy both progressive while also boosting consumption for the poorest households. More generally, it can also reduce any potential negative impact on growth—e.g., high quality public investment gives a boost to domestic demand and can contribute to rising productivity. As an example, in the second graph of Figure 1, we apply 30 percent of carbon pricing revenues in targeted transfers for the bottom 40 percent of households. On net, the bottom two deciles of households are left better off by this set of policies, while impact on the next two deciles is near zero. Using a larger proportion of revenues on transfer would yield even larger benefits for the poorest households. This accompanying reform reverses the regressivity of an ETS, as also found for other Asian countries.[8] When policies raising energy prices are accompanied with progressivity-boosting transfers, they are much more likely to be popular with Vietnamese households.

Figure 1. Vietnam: Burden on Households from Medium Reductions Scenario, 2030



Source: IMF staff calculations using CPAT.

Note: Panels show relative to consumption impact of the carbon price on consumption deciles before (left) and after (right) revenue recycling. Revenue recycling assumes 30 percent of carbon pricing revenues are used for targeted transfers.

[8] Dabla-Norris et al. (2021).

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Annex VII. Climate Change Risks and Efficient Adaptation[1]

Climate change poses macro-critical risks, especially from sea-level rise, but adaptation can be highly effective. With many competing needs the government would benefit from focusing on adaptations with positive externalities, market reforms to facilitate efficient private adaptation, and welfare measures to make adaptation equitable. Cost-benefit analysis can play an important role in helping collect, aggregate, and compare information on adaptation projects.

1. Vietnam is becoming more vulnerable to climate change as it experiences higher temperatures and sea-level rise. Average annual temperature has oscillated until approximately the 1980s, when a clear upward trend starts (Figure 1). In the period 1985-2014, average annual temperature in Vietnam was approximately 0.3 to 0.4 °C higher than its historical norm. The number of days with maximum daily temperature above 35 °C has also significantly increased. Vietnam's long coastline and heavily populated low-lying regions make it highly vulnerable to sea level rise, especially along the Mekong delta (World Bank CCDR, 2022). There is instead no discernible nation-wide trend in total annual precipitation (Figure 1), in the number of days with heavy precipitations, and in the number of consecutive dry days (World Bank CCKP).

2. Temperature and sea-level will continue to rise, while changes in precipitations and weather extremes are more uncertain but can potentially cause large losses. Climate models project additional warming of 0.8 °C in 2030 relative to the 1985-2014 period under all emission scenarios (Figure ***2***). Temperature is projected to increase between 1.2 and 1.4 °C in 2050 (Table 1). In 2070, the temperature is likely to further increase even with large global emission reductions (Paris scenario)—at present trends, temperature is expected to increase by 1.8 °C in 2070, and by 2.1 °C in a High emission scenario. In 2050 sea-level rise is expected to increase by an additional 22 to 26 cm. The consensus among models shows an increase in total annual precipitation in all emission scenarios, but not larger than normal interannual variability (Figure 2). Projections of changes in extreme rainfall and dry periods are also very uncertain (World Bank CCKP). Tropical cyclones periodically affect Vietnam causing large losses. While uncertainty about changes in frequency and intensity of tropical cyclones is large, the upward trend in tropical cyclones observed in recent years is expected to continue with medium confidence (IPCC, 2021).

3. In this context, Vietnam would greatly benefit from adapting to increasing temperature and to additional sea-level rise, and from monitoring risks from precipitation changes and tropical cyclones. Higher temperature throughout the year has the potential to cause productivity losses across the economy, but especially in agriculture. Higher ocean temperature and acidification may negatively impact fishery sector. Sea-level rise and a potential increase in the frequency and/or intensity of tropical cyclones will amplify risks along the coastline. While scenarios of temperature and sea-level rise change indicate robust trends that can be used to plan incremental adaptation measures, uncertainty around scenarios suggest focusing on win-win measures that reduce present risks and can turn to be beneficial under a wide range of scenarios.

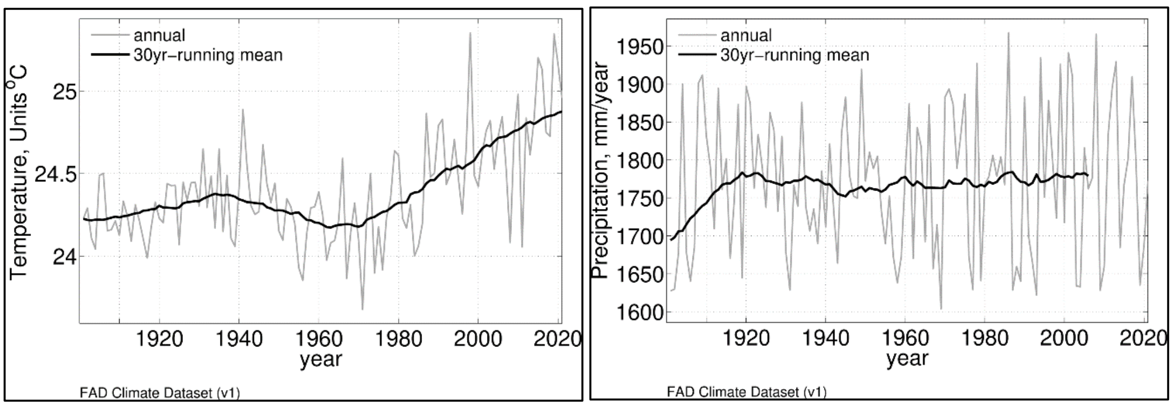
[1] Prepared by Emanuele Massetti.

For example, projects that enhance efficient water use or effective storm water management have both immediate benefits and will be useful under a wide range of future scenarios. Enhancing preparedness against tropical cyclones will be beneficial even if future risks will not change noticeably.

4. With many competing needs, the government must carefully allocate resources across all possible uses, including adaptation to climate change, while considering the distributional effects of its programs. This requires (1) concentrating government efforts and resources in key areas, and (2) collecting information on how effective spending is across alternative programs and how spending affects distinct groups in society (Bellon and Massetti, 2022).

Figure 1. Vietnam: Average Annual Timeseries for the Period (1900-2021)

(left) temperature (°C), (right) precipitation (mm/year).



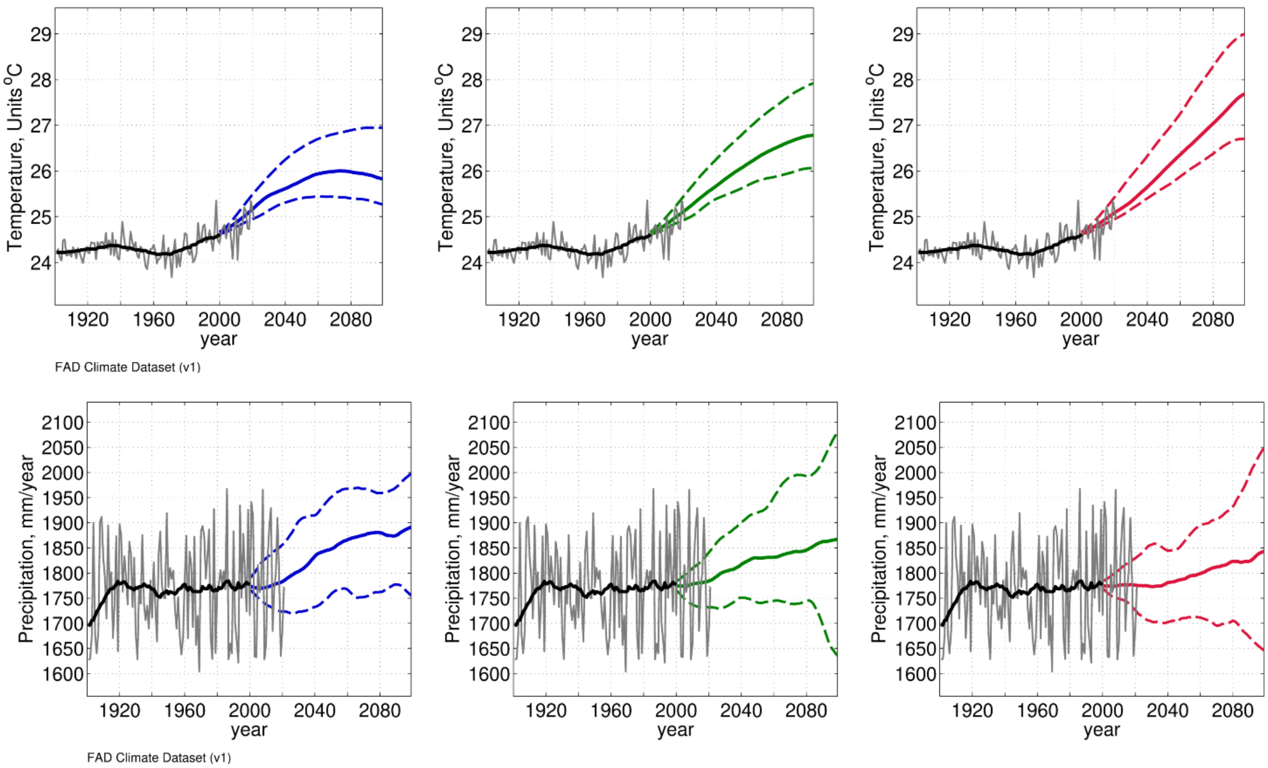
Notes: The solid line displays the 30-year average centered around each 30-year period.

Source: FADCP Climate Dataset (Massetti and Tagklis, 2023), using CRU data (Harris et al., 2020).

Figure 2. Vietnam: Time Series of Average Annual Temperature (ºc), and Total Annual Precipitation

(Mm/Year).

Paris (SSP1-2.6)	*Present Trends* (SSP2-4.5)	*High* (SSP3-7.0)



Notes: The gray line describes historical mean annual temperature/precipitation based on observations (CRU). The black line describes the 30-year moving average of historical data centered around each 30-year period. Colored lines represent the median and the 80 percent range of temperature anomalies (10th and 90th percentiles) added to the CRU value(thick black line in the year 2000. SSP1-2.6 scenario is in line with the Paris goal to keep global mean temperature increase below 2 ºC with respect to pre-industrial times. SSP2-4.5 represents continuation of present trends. SSP3-7.0 is a high emission scenario.

Source: FADCP Climate Dataset (Massetti and Tagklis, 2023), using CRU data (Harris et al., 2020), and CMIP6 data (Copernicus Climate Change Service, Climate Data Store, (2021): CMIP6 climate projections).

Table 1. Vietnam: Summary Table of Temperature Historical Observations and Projections (°C)

	1985-2014 (level)	1931-1960 (change)	1961-1990 (change)	2030 (2015-2044)	2050 (2035-2064)	2070 (2055-2084)
Paris SSP1-2.6				(0.5,**0.8**,1.3)	(0.8,**1.2**,1.9)	(0.8,**1.4**,2.2)
Present Trends SSP2-4.5	24.6	-0.3	-0.4	(0.5,**0.8**,1.4)	(0.9,**1.3**,2.0)	(1.2,**1.8**,2.6)
High SSP3-7.0				(0.6,**0.8**,1.4)	(1.0,**1.4**,2.2)	(1.5,**2.1**,3.2)

Notes: 1985-2014 average temperature is used as the benchmark to measure observed and projected temperature change. Future projectsions indicate the 10th, 50th, and 90th percentile of the range of all climate models. The 50th percentile is the "consensus" estimate.
Source: FADCP Climate Dataset (Massetti and Tagklis, 2023), using CRU data (Harris et al., 2020), and CMIP6 data (Copernicus Climate Change Service, Climate Data Store, 2021).

5. **Governments can prioritize adaptation policies with positive externalities, by removing the market imperfections and policies that hinder efficient private adaptation, and by ensuring a just transition**. Individuals and firms have strong incentives to adapt because many adaptation benefits tend to be local and private. However, there is a clear role for government intervention when adaptation has large externalities (Bellon and Massetti, 2022), for example:

- Some market imperfections pertain to the nature of the adaptation goods themselves. For example, markets invest suboptimally in adaptations with large positive externalities and public goods, such as information about climate change, emergency preparedness plans, seawalls, basic research in new materials, and technologies to cope with higher temperature.
- In many instances, resilience depends on networks, such as a system of dikes, a water network, or a transportation network. As adaptation in each part of a network has impacts on the rest of the network that may not be captured, private adaptation will tend to be underprovided.
- The extent of needed cooperation for adaptation projects depends on the extent of the externality that is addressed by the project. As risks grow in scope and complexity, cooperation might be needed at the national or even the international level, for example to manage floods in transnational rivers. In general, the optimal distribution of responsibilities across levels of government also depends on the existing allocation of responsibilities.
- Other market imperfections affect the broad functioning of the economy and make adaptation to climate change inefficient. For example, a poor business environment and inefficient credit markets hamper opportunities for farmers to invest in new capital to grow crops that are more suitable to the new climate.
- Moral hazard may cause insufficient investment in adaptation if consumers, firms, and local government expect central governments to provide relief. Governments can implement regulations that minimize risk taking. Examples include zoning that prohibits construction in flood zones, building codes, and mandatory insurance.

- The government may also consider correcting market distortions resulting from their own policies. For example, subsidies to inputs can lead to inefficient use. Of particular concern is subsidized water use, which may worsen water scarcity problems due to climate change. Barriers to international trade also prevent efficient climate-change-induced reallocation of capital, land use, and other resources to maximize their productivity.

6. Cost-benefit analysis (CBA) can play an important role in helping collect, aggregate, and compare information on adaptation projects. What to do, when, how, and at what cost ultimately relies on ethical choices that should reflect the preferences of each society. However, cost-benefit analysis (CBA), complemented by analysis and correction of distributional impacts, can help decision makers maximize overall social welfare by avoiding wasting scarce resources. CBA should be applied to adaptation as well as to all other development programs in a consistent manner (Bellon and Massetti, 2022). Competing programs should be ranked using CBA and only programs with the highest ranking should be financed**.** By consistently investing in projects with the highest returns, governments can maximize the impact of their spending. This means, for example, saving the largest number of lives, providing access to education to the largest number of children, ensuring that the largest possible number of people are above the poverty line, and boosting long-term growth (Bellon and Massetti, 2022).

7. Compensation might be more efficient than investments in adaptation to achieve society's equity preferences. Full protection of all assets and populations at risks may be very expensive in some cases and as a result adaptation projects may have a negative NPV. While there can be specific reasons to warrant investment even with a negative NPV, the authorities should consider if it is possible to support the affected population in alternative ways. This can take the form of relocation subsidies or other forms of supports with less stringent conditionality (Bellon and Massetti, 2022).

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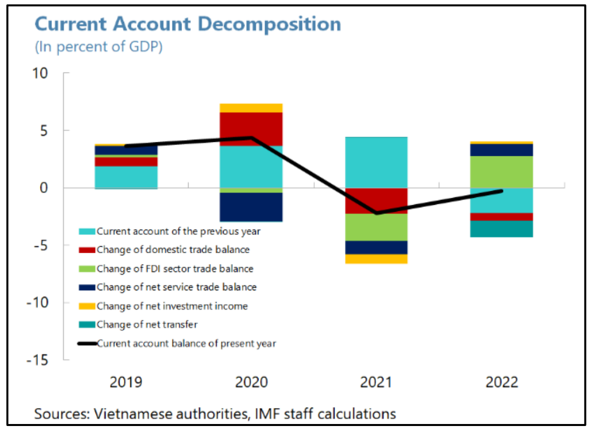
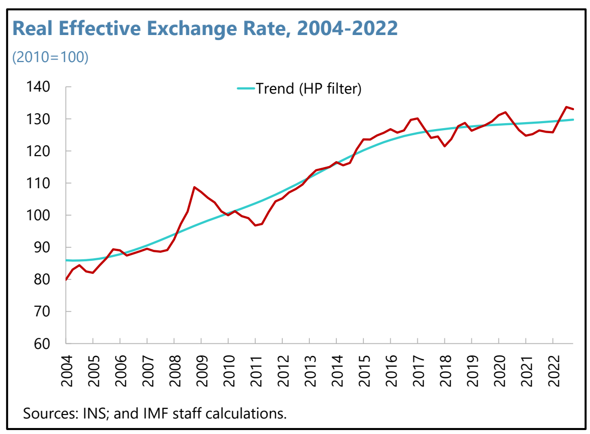
Annex VIII. External Sector Assessment

Vietnam's external position in 2022 was assessed to be stronger than the level implied by medium-term fundamentals and desirable policies. The current account balance (CAB) registered a deficit of 0.3 percent of GDP. The CAB is expected to improve further in 2023 as a result of China's reopening, subdued domestic demand, and a pick-up in net transfers. Policies geared towards promoting investment, including a stronger rollout of public investment, and strengthening of safety nets would support external rebalancing.



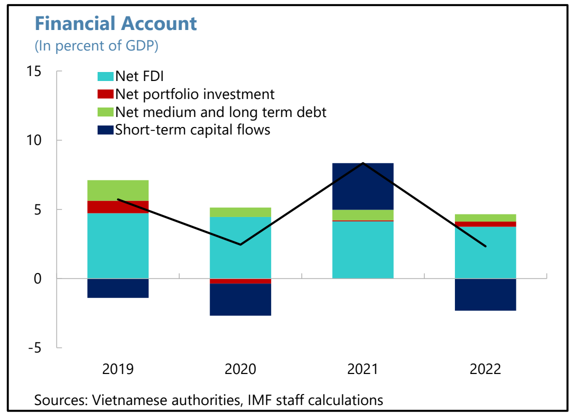
1. **The CA improved noticeably from a deficit of 2.2 percent of GDP in 2021 to a deficit of 0.3 percent in 2022, following a higher merchandise trade surplus and a rebound in services exports**. Vietnam's post-pandemic recovery boosted both domestic and FDI-related trade activity during the first nine months of 2022. However, merchandise trade declined in the last quarter as external and domestic headwinds arose, dampening FDI imports in particular. Additionally, an increase in tourist arrivals boosted services exports, which in 2022 were roughly 2.5 times higher than their 2021 levels. These factors increased the trade balance (including services) from 0.1 percent of GDP in 2021 to 3.2 percent in 2022. Net transfers fell by nearly 50 percent in 2022, due to higher remittance outflows.

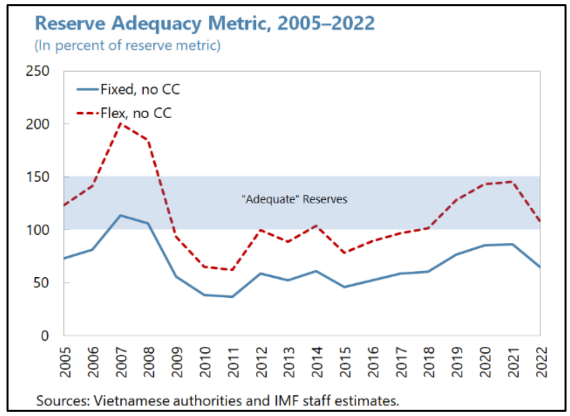


2. **The real effective exchange rate (REER) appreciated during the first three quarters of 2022 before stabilizing in the remainder of the year**. REER movements mirrored the trends in the nominal effective exchange rate (NEER). The depreciation of the dong versus the US dollar was more muted than that in Vietnam's other major trading partners (EU, China) until the end of 2022Q3, driving up Vietnam's NEER. As depreciation pressures on the dong came to bear in 2022Q4, the REER depreciated slightly, though it ended the year up 5.6 percent versus the end-2021 level.

3. **The financial account declined in 2022 driven by short-term capital flows**. Commercial banks repaid offshore debt and more deposits were placed abroad due to a widening interest rate differential (prior to the SBV's rate hike in fall 2022). FDI levels remained stable during the year and medium-term external borrowing was in line with previous years

4. Gross international reserves fell by 21 percent (USD 22.7 billion) in 2022. The authorities used FX interventions to counter depreciation pressures against the dong and stabilize the FX market, after a period of steady reserve accumulation between 2017-21. As of 2022 year-end, reserves stood at USD 86.7 billion, equivalent to 2.3 times short-term external debt and 65 percent of the Assessing Reserve Adequacy (ARA) metric under a fixed exchange rate regime. Reserve levels were at 107 percent of the metric under a flexible exchange rate. Staff assesses the end-2022 reserve levels to be moderately below adequacy, as the exchange rate regime is in between fixed and floating, and expects reserves to reach adequate levels again in 2023.





5. Vietnam's external position in 2022 is assessed to be stronger than warranted by fundamentals and desirable policies. Based on the current account model, the CA gap is estimated at 3.4 percent of GDP. The gap reflects both policy and unexplained factors. Some policy gaps have opposing signs: fiscal policy increased the gap by 1.3 percent of GDP (reflecting the tighter stance than in the rest of the world) while FXI interacted with capital controls reduced the gap by 2.2 percent (reflecting the drawdown in reserves along with the relatively closed financial account). Structural factors, not accounted by the model (like informality and weak social safety nets that lead to precautionary saving), also contributed to the gap. In addition, the large errors and omissions increase the uncertainty surrounding the assessment as the current account balance may have been more negative than reported, reducing the gap. The CA model implies a REER gap of -5 percent (applying an elasticity of 0.7). Instead, the EBA REER models suggest a gap of 16.2-21.4 percent, highlighting the significant uncertainty surrounding an exchange rate assessment.

EBA Model Estimates for 2022 (in percent of GDP) 1/

CA model	
CA-Actual	**-0.3**
Cyclical contributions (from model) (-)	-1.3
Adjusted CA	**1.0**
CA Norm (from model) 2/	**-2.4**
Standard Error	0.6
CA Gap	**3.4**
o/w Relative policy gap	-1.5
o/w fiscal policy gap	1.3
o/w FXI*KC gap	-2.2
REER Gap	
CA-implied	**-5.0**
Elasticity	0.7
REER-Index Model	**21.4**
REER-Level Model	**16.2**

1/ Vietnam transitioned from EBA-lite to EBA in 2022.
2/ Cyclically adjusted, including multilateral consistency adjustments.

Annex IX. Debt Sustainability Analysis

Figure 1. Vietnam: Risk of Sovereign Stress

Horizon	Mechanical signal	Final assessment	Comments
Overall	...	Low	The overall risk of sovereign stress is low, reflecting a relatively low level of vulnerability in the medium-term horizon and a low to moderate level of vulnerability in the long term.
Near term 1/			
Medium term	Low	Low	Medium-term risks are assessed as low, reflecting a stable fiscal outlook and low amortization need. The fanchart analysis suggests that baseline projections are reasonable and the public debt will be on a downward trajectory. GFN analysis indicates that financing needs are trending downward. Tighter global financing conditions remain a risk.
Fanchart	Low	...	
GFN	Low	...	
Stress test	...	...	
Long term	...	Moderate	Long-term risks are low to moderate as aging-related expenditures on health and social security as well on climate spending feed into debt dynamics, which will increase debt and GFN without policy actions. The government is aware of these risks and policy measures are envisaged, such as revenue mobilization, pension reforms, and galvanizing private sector support.
Sustainability assessment 2/	Not required for surveillance countries	Not required for surveillance countries	
Debt stabilization in the baseline			Yes

DSA summary assessment

Commentary: Vietnam is at a low overall risk of sovereign stress. The public debt continued to fall since 2020 and is projected to further decline, and medium-term risks as analyzed by the DSA are also low. Over the longer run, Vietnam should maintain fiscal prudency and continue with reforms to strengthen the authorities' debt management institutions to tackle any long-term risks arising from population aging and climate change.

Source: Fund staff.

Note: The risk of sovereign stress is a broader concept than debt sustainability. Unsustainable debt can only be resolved through exceptional measures (such as debt restructuring). In contrast, a sovereign can face stress without its debt necessarily being unsustainable, and there can be various measures—that do not involve a debt restructuring—to remedy such a situation, such as fiscal adjustment and new financing.

1/ The near-term assessment is not applicable in cases where there is a disbursing IMF arrangement. In surveillance-only cases or in cases with precautionary IMF arrangements, the near-term assessment is performed but not published.

2/ A debt sustainability assessment is optional for surveillance-only cases and mandatory in cases where there is a Fund arrangement. The mechanical signal of the debt sustainability assessment is deleted before publication. In surveillance-only cases or cases with IMF arrangements with normal access, the qualifier indicating probability of sustainable debt ("with high probability" or "but not with high probability") is deleted before publication.

Figure 2. Vietnam: Debt Coverage and Disclosures

1. Debt coverage in the DSA: 1/

CG	GG	NFPS	CPS	Other	Comments

1a. If central government, are non-central government entities insignificant? n.a.

2. Subsectors included in the chosen coverage in (1) above:

					Subsectors captured in the baseline	Inclusion	Comments
CPS	NFPS	GG: expected	CG	1	Budgetary central government	Yes	
				2	Extra budgetary funds (EBFs)	No	Not applicable
				3	Social security funds (SSFs)	No	(see commentary below)
				4	State governments	Yes	
				5	Local governments	Yes	
				6	Public nonfinancial corporations	No	
				7	Central bank	No	
				8	Other public financial corporations	No	

3. Instrument coverage:

Currency & deposits	Loans	Debt securities	Oth acct. payable 2/	IPSGSs 3/

4. Accounting principles:

Basis of recording		Valuation of debt stock		
Non-cash basis 4/	Cash basis	Nominal value 5/	Face value 6/	Market value 7/

5. Debt consolidation across sectors:

Consolidated	Non-consolidated

Color code: chosen coverage; Missing from recommended coverage; Not applicable

Reporting on intra-government debt holdings

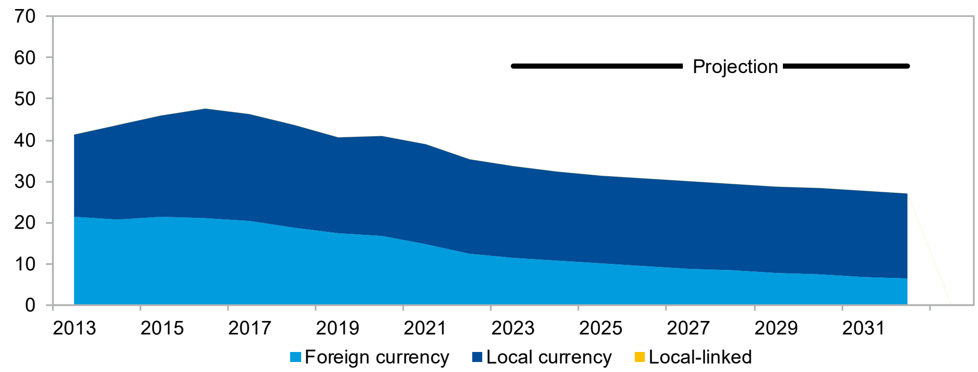
						Holder / Issuer	Budget. central govt	Extra-budget. funds	Social security funds	State govt.	Local govt.	Nonfin. pub. corp.	Central bank	Oth. pub. fin corp	Total
CPS	NFPS	GG: expected	CG	1		Budget. central govt									0
				2		Extra-budget. funds									0
				3		Social security funds									0
				4		State govt.									0
				5		Local govt.									0
				6		Nonfin pub. corp.									0
				7		Central bank									0
				8		Oth. pub. fin. corp									0
						Total	0	0	0	0	0	0	0	0	0

1/ CG=Central government; GG=General government; NFPS=Nonfinancial public sector; PS=Public sector.
2/ Stock of arrears could be used as a proxy in the absence of accrual data on other accounts payable.
3/ Insurance, Pension, and Standardized Guarantee Schemes, typically including government employee pension liabilities.
4/ Includes accrual recording, commitment basis, due for payment, etc.
5/ Nominal value at any moment in time is the amount the debtor owes to the creditor. It reflects the value of the instrument at creation and subsequent economic flows (such as transactions, exchange rate, and other valuation changes other than market price changes, and other volume changes).
6/ The face value of a debt instrument is the undiscounted amount of principal to be paid at (or before) maturity.
7/ Market value of debt instruments is the value as if they were acquired in market transactions on the balance sheet reporting date (reference date). Only traded debt securities have observed market values.

Commentary: Public debt of the Vietnam Social Security (VSS) is not included in Vietnam's definition of public debt. With cross-debt holdings of about 10 percent of GDP, its inclusion would currently reduce public debt by the same amount.

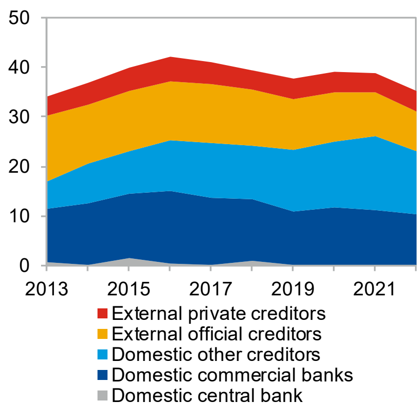
Figure 3. Vietnam: Public Debt Structure Indicators

(Debt by currency (percent of GDP))



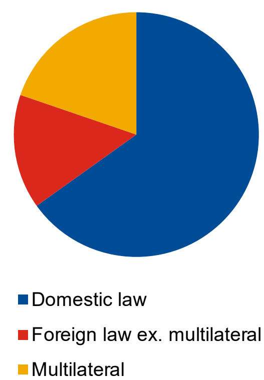
Note: The perimeter shown is general government.

Public debt by holder (percent of GDP)



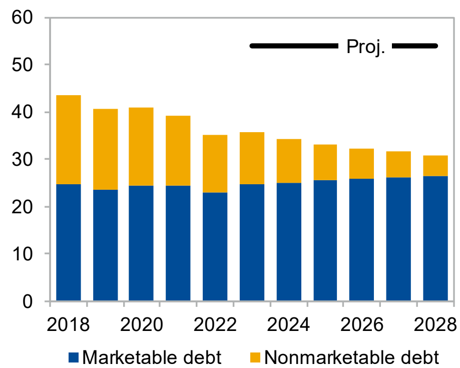
Note: The perimeter shown is general government.

Public debt by governing law, 2022 (percent)



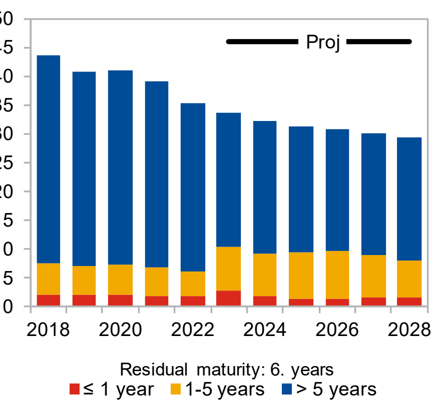
Note: The perimeter shown is general government.

Debt by instruments (percent of GDP)



Note: The perimeter shown is general government.

Public debt by maturity (percent of GDP)



Note: The perimeter shown is general government.

Commentary: Debt has been increasingly held by domestic commercial banks and nonbank financial institutions. The share of foreign currency debt is projected to decline as the government favors domestic financing for the budget, with gradual decay of nonmarketable debt.

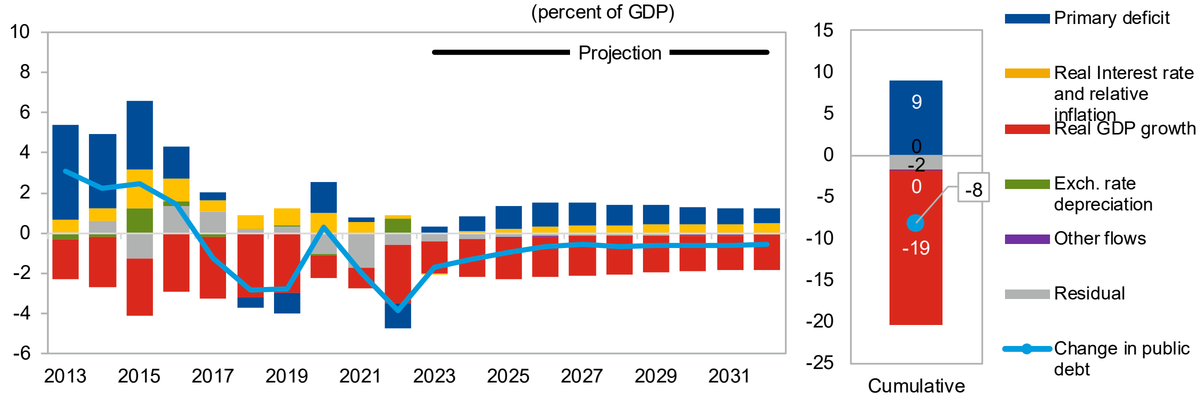
Figure 4. Vietnam: Baseline Scenario

(Percent of GDP unless indicated otherwise)

	Actual	Medium-term projection						Extended projection			
	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
Public debt	35.3	33.6	32.3	31.3	30.7	30.1	29.5	28.9	28.2	27.6	27.1
Change in public debt	-3.9	-1.7	-1.3	-0.9	-0.6	-0.6	-0.7	-0.6	-0.6	-0.6	-0.6
Contribution of identified flows	-3.3	-1.3	-1.0	-0.7	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5
Primary deficit	-1.3	0.3	0.8	1.2	1.2	1.1	1.0	1.0	0.8	0.8	0.8
Noninterest revenues	19.0	18.4	18.5	18.8	19.0	19.2	19.4	19.5	19.6	19.6	19.7
Noninterest expenditures	17.8	18.7	19.3	19.9	20.2	20.4	20.5	20.5	20.5	20.5	20.5
Automatic debt dynamics	-2.0	-1.6	-1.8	-1.9	-1.7	-1.6	-1.6	-1.4	-1.4	-1.3	-1.2
Real interest rate and relative inflation	0.2	0.0	0.1	0.2	0.3	0.4	0.4	0.4	0.4	0.5	0.5
Real interest rate	-0.3	-0.5	-0.3	-0.1	0.0	0.1	0.1	0.2	0.2	0.3	0.3
Relative inflation	0.5	0.5	0.4	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2
Real growth rate	-2.9	-1.6	-1.8	-2.1	-2.0	-2.0	-1.9	-1.8	-1.8	-1.8	-1.7
Real exchange rate	0.7	…	…	…	…	…	…	…	…	…	…
Other identified flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other transactions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Contribution of residual	-0.6	-0.4	-0.3	-0.2	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Gross financing needs	2.1	3.4	4.2	3.6	3.4	3.3	3.4	3.4	3.5	3.4	2.7
of which: debt service	3.4	3.0	3.4	2.5	2.2	2.1	2.3	2.4	2.7	2.6	1.9
Local currency	2.5	1.8	2.3	1.6	1.4	1.4	1.6	1.8	2.1	2.0	1.4
Foreign currency	0.9	1.3	1.1	0.8	0.8	0.7	0.7	0.6	0.6	0.6	0.5
Memo:											
Real GDP growth (percent)	8.0	4.7	5.8	6.9	6.8	6.8	6.8	6.7	6.6	6.6	6.6
Inflation (GDP deflator; percent)	3.9	4.5	4.1	3.5	2.9	2.8	2.9	2.7	2.7	2.7	2.7
Nominal GDP growth (percent)	12.2	9.5	10.1	10.7	10.0	9.8	9.9	9.6	9.6	9.6	9.6
Effective interest rate (percent)	2.9	2.9	3.0	3.0	3.1	3.3	3.4	3.5	3.6	3.8	4.0

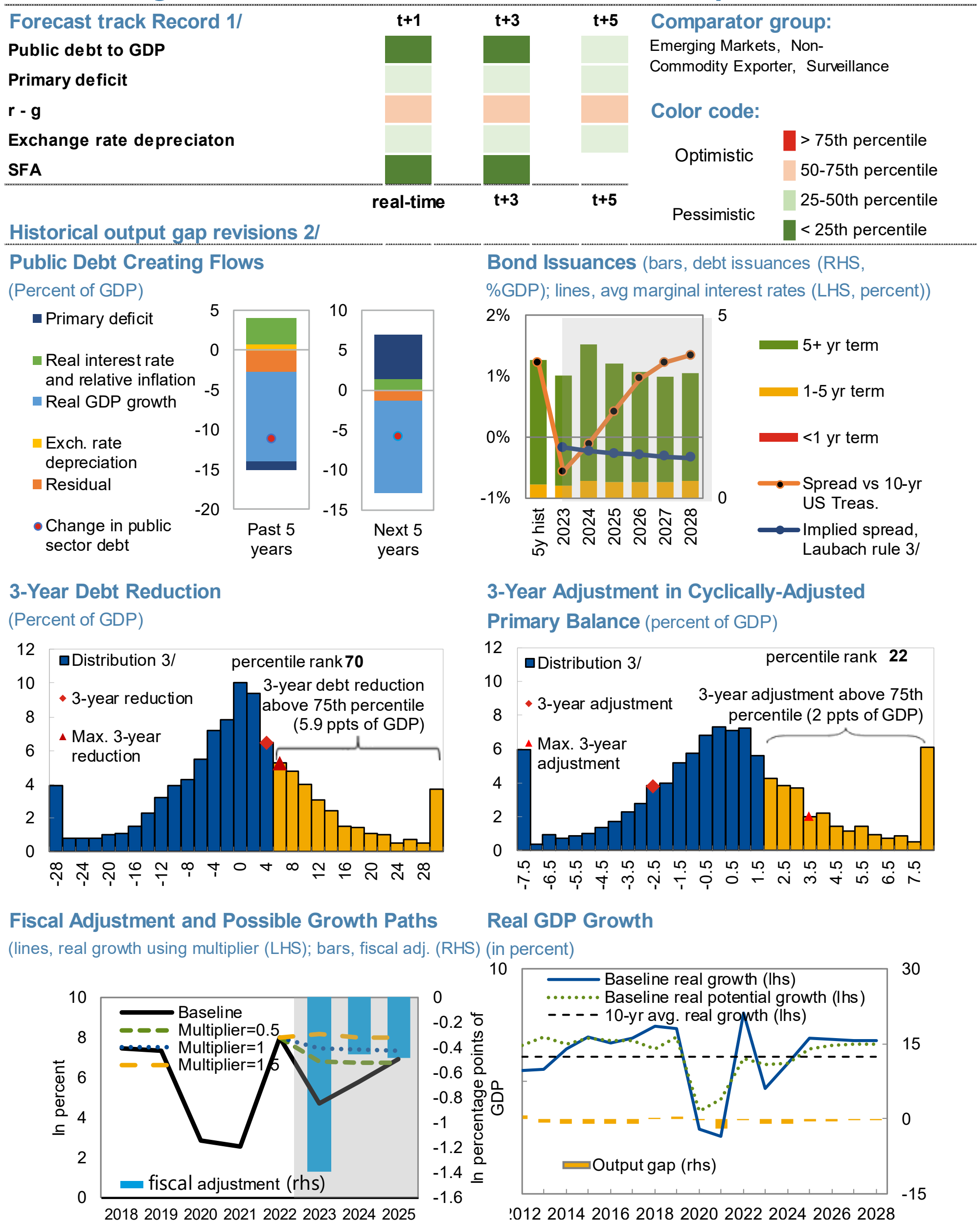
Contribution to change in public debt

(percent of GDP)



Staff commentary: Public debt is projected to gradually decline, reflecting expectations of a narrowing of primary deficits and strong GDP growth amid stable economic conditions. Continued revenue mobilization and spending prudency will help lower the primary deficit to around 1 percent of GDP in the medium term. After a weaker performance owing to lackluster external demand in 2023, growth is expected to recover to the potential annual rate of 6.8 percent in the medium term, together with a projected inflation of 3.1 percent, helping to keep the debt-to-GDP ratio in check.

Figure 5. Vietnam: Realism of Baseline Assumptions



Commentary: Realism analysis does not point to major concerns as past forecasts appear to be conservative and the projections are well within norms. The primary deficit is projected to become the main driver of debt creation as the generally tight fiscal policy in the past few years loosens.

Source : IMF Staff.

1/ Projections made in the October and April WEO vintage.

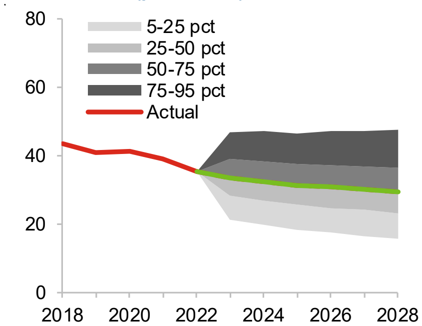
2/ Calculated as the percentile rank of the country's output gap revisions (defined as the difference between real time/period ahead estimates and final estimates in the latest October WEO) in the total distribution of revisions across the data sample.

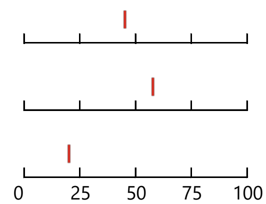
3/ The Laubach (2009) rule is a linear rule assuming bond spreads increase by about 4 bps in response to a 1 ppt increase in the projected debt-to-GDP ratio.

Figure 6. Vietnam: Medium-Term Risk Assessment

	Value	Contrib 1/	Percentile in peer group 2/
Debt fanchart module			
Fanchart width *(percent of GDP)*	32.1	0.5	
Probability of debt non-stabilizaiton *(percent)*	32.1	0.3	
Terminal debt-to-GDP x institutions index	18.0	0.4	
Debt fanchart index (DFI)		1.1	
Risk signal: 3/		Low	

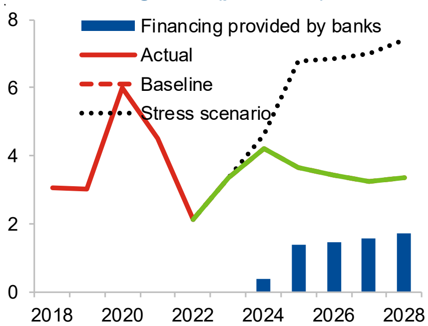
Final fanchart (pct of GDP)

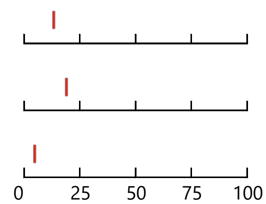




	Value	Contrib 1/	Percentile in peer group 2/
Gross financing needs (GFN) module			
Average baseline GFN *(percent of GDP)*	3.5	1.2	
Banks' claims on the ger govt *(pct bank assets)*	5.7	1.8	
Chg. In banks' claims in stress *(pct banks' assets)*	0.7	0.2	
GFN financeability index (GFI)		3.3	
Risk signal: 4/		Low	

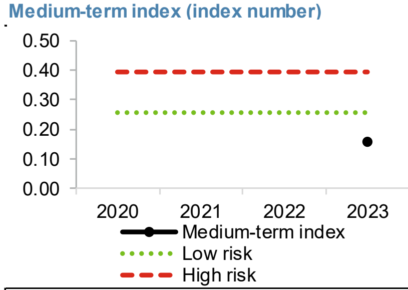
Gross financing needs (pct of GDP)





Banking crisis | Commodity prices | Exchange rate | Contingent liab. | Natural disaster

Medium-term index (index number)



Medium-term risk analysis

	Value	Weight	Contribution
Debt fanchart index (normalized)	0.3	0.5	0.1
GFN finaceability index (normalized)	0.1	0.5	0.0
Medium-term index	0.2		
Risk signal: 5/	Low		
Final assessment:	Low		

Prob. of missed crisis, 2023-2028, if stress not predicted: 0.0 pct.

Prob. of false alarms, 2023-2028, if stress predicted: 65.9 pct.

According to the debt fanchart and GFN modules, debt remains stable in the medium term and the gross financing needs remains low. The medium-term index point to low risk. The stress scenario for FX depreciation does not change these results as FX debt is relatively small.

Source: IMF staff estimates and projections.

1/ See Annex IV of IMF, 2022, Staff Guidance Note on the Sovereign Risk and Debt Sustainability Framework for details on index calculation.

2/ The comparison group is emerging markets, non-commodity exporter, surveillance.

3/ The signal is low risk if the DFI is below 1.13; high risk if the DFI is above 2.08; and otherwise, it is moderate risk.

4/ The signal is low risk if the GFI is below 7.6; high risk if the DFI is above 17.9; and otherwise, it is moderate risk.

5/ The signal is low risk if the GFI is below 0.26; high risk if the DFI is above 0.40; and otherwise, it is moderate risk.

Figure 7. Vietnam: Long-Term Risk Analysis

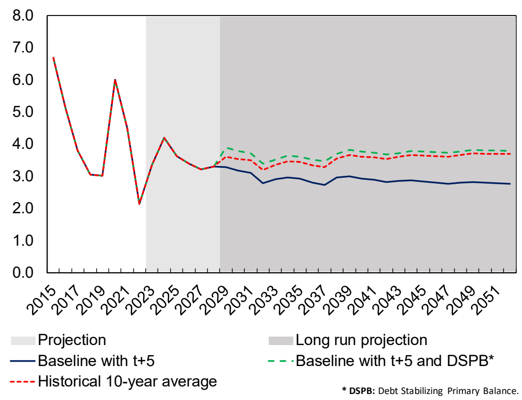
Large Amortization Trigger

Projection	Variable	Risk Indication
Medium-term extrapolation	GFN-to-GDP ratio	
	Amortization-to-GDP ratio	
	Amortization	
Medium-term extrapolation with debt stabilizing primary balance	GFN-to-GDP ratio	
	Amortization-to-GDP ratio	
	Amortization	
Historical average assumptions	GFN-to-GDP ratio	
	Amortization-to-GDP ratio	
	Amortization	

Overall Risk Indication	

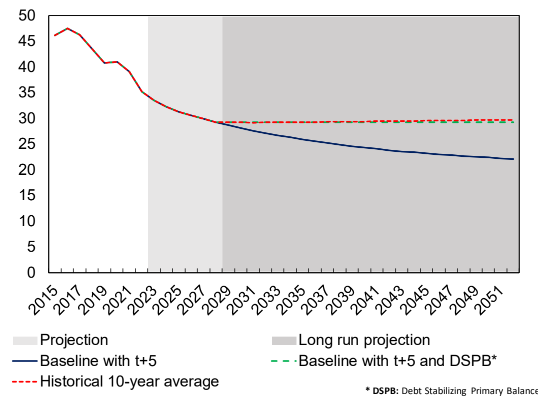
Alternative Baseline Long-term Projections

GFN-to-GDP ratio



* DSPB: Debt Stabilizing Primary Balance.

Total public debt-to-GDP ratio



* DSPB: Debt Stabilizing Primary Balance.

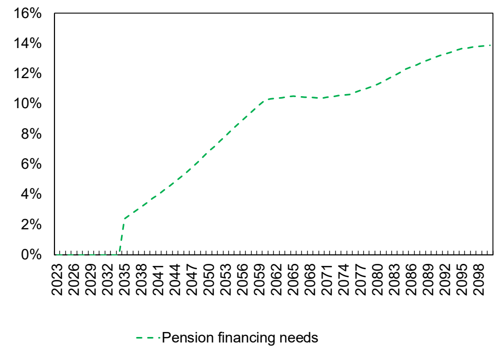
Commentary: Long-term debt is broadly stable and remain relatively low under alternative assumptions. The "Historical 10-year average" and "t+5 and DSPB" scenarios show somewhat higher financing needs.

Figure 7. Vietnam: Long-Term Risk Analysis (Continued)

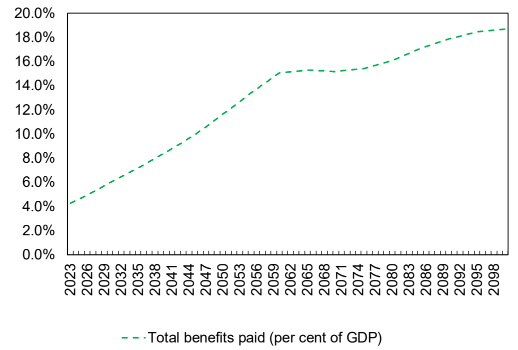
Demographics: Pension

Permanent adjustment needed in the pension system (pp of GDP per year)	To keep pension assets positive for:		
	30 years	50 years	Until 2100
	3.74%	7.70%	10.73%

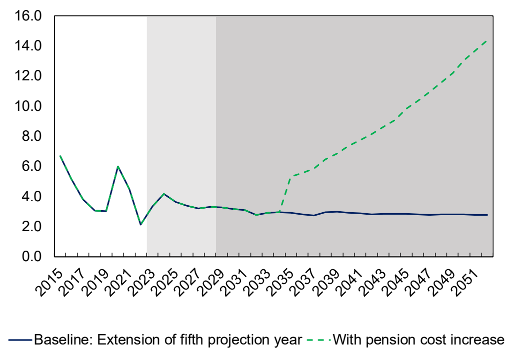
Pension Financing Needs



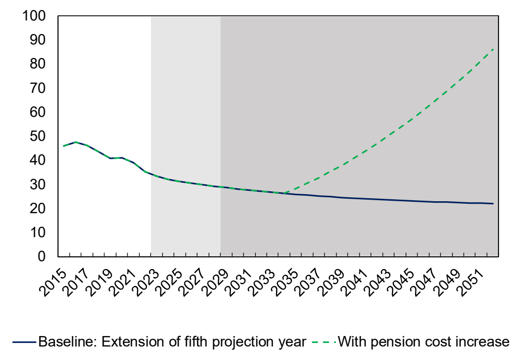
Total benefits paid



GFN-to-GDP ratio



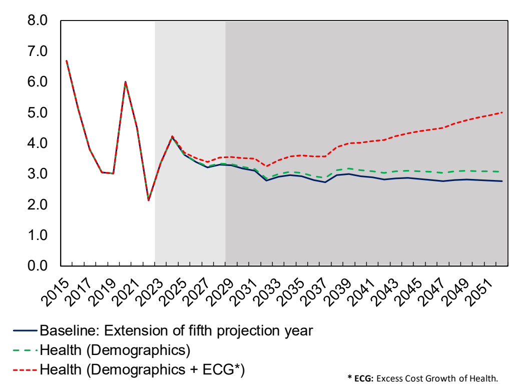
Total public debt-to-GDP ratio



Commentary: Population aging is expected to increase pension cost significantly after 2035 in the absence of reforms. The government is aware of the pressure from population aging and is expected to implement pension reforms and revenue mobilization to meet the challenge.

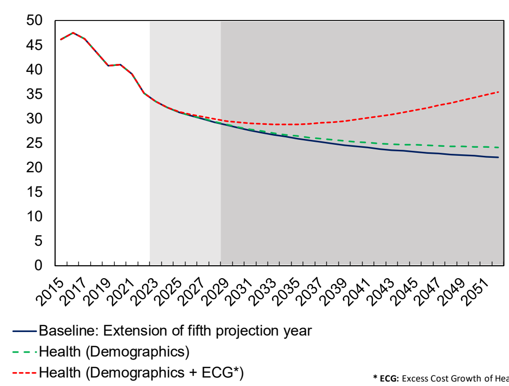
Demographics: Health

GFN-to-GDP ratio



* ECG: Excess Cost Growth of Health.

Total public debt-to-GDP ratio



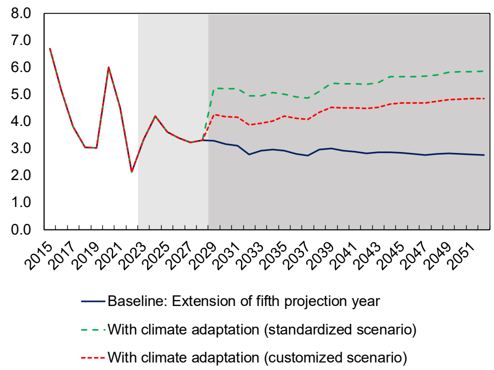
* ECG: Excess Cost Growth of Health.

Commentary: In the long term, the health spending need is rising. It could be managed if the government devotes enough gains from its efforts to mobilize tax revenues to health spending and implement structural reforms to improve spending efficiency.

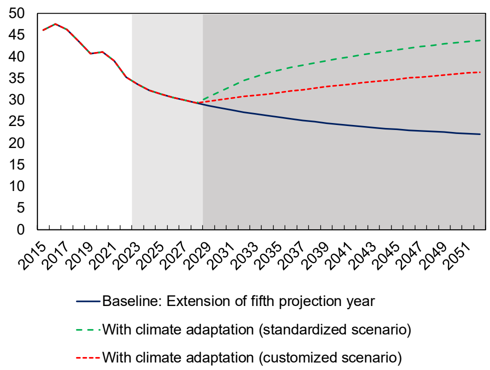
Figure 7. Vietnam: Long-Term Risk Analysis (Concluded)

Climate Change: Adaptation

GFN-to-GDP ratio



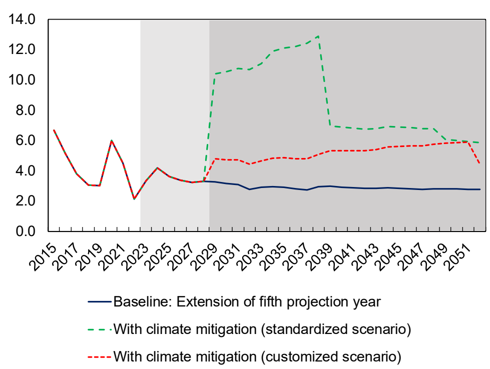
Total public debt-to-GDP ratio



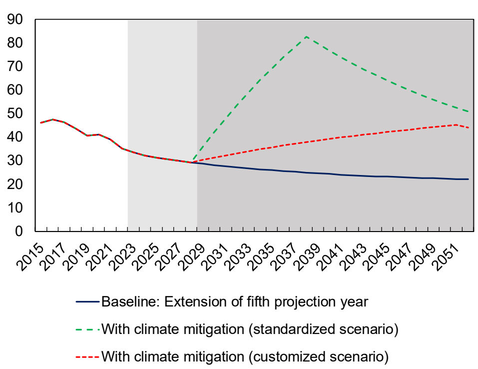
Commentary: Investments to address climate adaptation will increase the long-term financing need. However, the government's planned ETS is expected to generate significant revenues which could be used to finance climate adaptation. The government is also committed to prioritizing investment toward climate adaptation.

Climate Change: Mitigation

GFN-to-GDP ratio



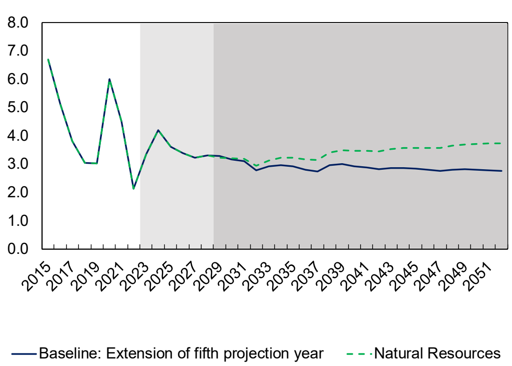
Total public debt-to-GDP ratio



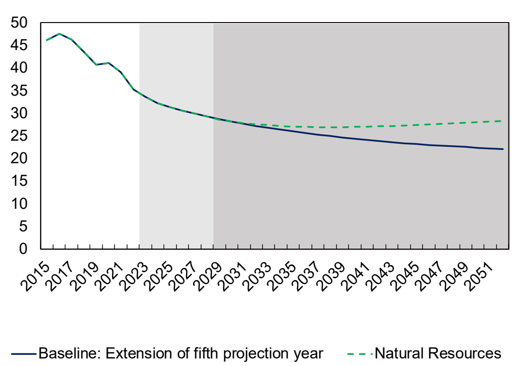
Commentary: In the absence of measures, the mitigation spending need is high in the standardized scenario. However, the government's planned ETS will operate starting 2028 which will help reduce the spending need and generate significant revenues which could be used on shifting toward renewable energy.

Natural Resources

GFN-to-GDP ratio



Total public debt-to-GDP ratio



Commentary: Vietnam is an oil producer. In the absence of new discoveries, the exhaustion of the oil reserves in the long run would have negative impacts on the GFN and public debt, but as the natural resource sector constituted less than 3 percent of GDP in 2022, the sector's influence on public debt is small.

Annex X. Risk Assessment Matrix

Risk	Likelihood of Risk	Time Horizon	Impact if realized	Policy Response
		External Risks		
Intensification of regional conflict(s).	***High*** **Downside**: Escalation of the war in Ukraine or other regional conflicts and resulting economic sanctions disrupt trade (e.g., energy, food, tourism, and/or critical supply chain components), remittances, refugee flows, FDI and financial flows, and payment systems.	***ST, MT***	***High*** Higher commodity prices, extended supply chain disruptions, tighter financial conditions, lower global demand, and less trade.	• Provide targeted policy support. • Allow greater exchange rate flexibility. • Accelerate structural reforms and improve business environment. • Diversify sourcing of intermediate goods.
Abrupt global slowdown or recession.	***Medium*** **Downside**: Global and idiosyncratic risk factors combine to cause a synchronized sharp growth downturn, with recessions in some countries, adverse spillovers through trade and financial channels, and markets fragmentation.	***ST***	***High*** Lower exports, tourism, and FDI.	• Provide targeted policy support. • Allow greater exchange rate flexibility. • Facilitate reallocation of resources through structural reforms. • Diversify sourcing of intermediate goods.
Deepening geo-economic fragmentation.	***High*** **Downside/upside:** Broader and deeper conflict(s) and weakened international cooperation lead to a more rapid reconfiguration of trade and FDI, supply disruptions, technological and payments systems fragmentation, rising input costs, financial instability, a fracturing of international monetary and financial systems, and lower potential growth.	***ST/MT***	***Medium*** Supply disruptions and weaker confidence adversely affect economic activity globally. However, Vietnam may continue benefiting from trade diversion.	• Allow greater exchange rate flexibility. • Accelerate structural reforms and improve business environment
Monetary policy miscalibration.	***Medium*** **Downside**: Amid high economic uncertainty and volatility, major central banks slow monetary policy tightening or pivot to loosen monetary policy stance prematurely, de-anchoring inflation expectations and triggering a wage-price spiral in tight labor markets.	***ST, MT***	***High/Medium*** Tighter global financial conditions, lower capital inflows; increase inflationary pressure.	• Allow greater exchange rate flexibility. • Tighten monetary policy when economic situation allows. • Agile and more targeted fiscal policy
Systemic financial instability.	***Medium*** **Downside:** Sharp swings in real interest rates, risk premia, and assets repricing amid economic slowdowns and policy shifts trigger insolvencies in countries with weak banks or non-bank financial institutions, causing markets dislocations and adverse cross-border spillovers.	***ST, MT***	***Medium*** Lower external demand and tighter global financial conditions.	• Allow greater exchange rate flexibility. • Tighten monetary policy when economic situation allows. • Closely monitor financial stability risks. • Provide targeted policy support.

		Domestic Risks		
Slowdown in credit to the economy.	***High*** **Downside:** A deepening of the current ongoing real estate and corporate bond markets turmoil could adversely affect banks, including some that could become distressed.	***ST, MT***	***Medium*** Reduced economic activity accompanied by tighter financial conditions as credit risks increase.	• Establish a crisis monitoring function to address short-term risks to financial stability. • Urgently modernize the bank resolution and the emergency liquidity frameworks • Contagion from troubled real estate developers should be prevented to avoid posing risks to financial stability. • Over time, strengthen bank regulation, supervision and resolution frameworks, establish a well-functioning corporate bond market and firm insolvency framework.
Slow and inconsistent policy Implementation.	***Medium*** **Downside:** coordination and capacity issues hamper implementation of the stimulus and create policy uncertainties.	***ST, MT***	***Medium*** Hampers labor reallocation and fuels supply disruptions; weak stimulus implementation slows recovery.	• Enhance policy coordination and reduce regulatory and other barriers • Clearly communicate harmonized policies and consistent application nationally.
Debt overhang and liquidity constraints.	***Medium*** **Downside**: businesses and households deplete buffers, propagating balance sheet stress.	***ST, MT***	***Medium*** Slows recovery threatens financial stability.	• Target support to viable firms and vulnerable households. • Closely monitor asset quality, enhance provisioning, and rebuild capital buffers.
Climate change.	***High*** **Downside:** Vietnam is amongst the most vulnerable yet least ready/able to adapt.	***ST, MT***	***High*** By 2100, climate change could severely impact more than 12 percent of the population and reduce growth by 10 percent.	• Address both climate mitigation and adaptation. • Lower the intensity of fossil fuels • Provide stronger incentives through taxation of fossil fuels • Invest in climate resilient infrastructure. • Improve capacity to adapt technological change.

"L" =Low; "M" =Medium; "H" =High. The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly

INTERNATIONAL MONETARY FUND

VIETNAM

July 25, 2023

STAFF REPORT FOR THE 2023 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

Asia and Pacific Department
(In consultation with other departments)

CONTENTS

FUND RELATIONS

(As of June 30, 2023)

Membership Status

Joined: September 21, 1956; Article VIII

General Resources Account

	SDR Million	Percent of Quota
Quota	1,153.10	100.00
Fund holdings of currency	1,153.10	100.00
Reserve position in Fund	0.01	0.00

SDR Department

	SDR Million	Percent Allocation
Net cumulative allocation	1,419.99	100.00
Holdings	1,403.61	98.85

Outstanding Purchases and Loans: None

Latest Financial Arrangements

In millions of SDRs

Type	Date of Arrangement	Expiration Date	Amount Approved	Amount Drawn
ECF[1]	04/13/2001	04/12/2004	290.00	124.20
ECF[1]	11/11/1994	11/10/1997	362.40	241.60
Stand-By	10/06/1993	11/11/1994	145.00	108.80

[1] Formally PRGF.

Projected Payments to Fund

In millions of SDRs (based on existing use of resources and present holdings of SDRs)

	Forthcoming				
	2023	2024	2025	2026	2027
Principal					
Charges/interest	0.32	0.67	0. 67	0.67	0.67
Total	**0.32**	**0.67**	**0.67**	**0.67**	**0.67**

Exchange Rate Arrangement

The de facto exchange rate arrangement was reclassified to stabilized from crawl-like. The de jure arrangement is managed floating. The State Bank of Vietnam (SBV) is gradually increasing exchange-rate flexibility. In August 2015 it widened the VND/USD trading band to +/-3 percent from +/-1 percent while devaluing the central parity by one percent. SBV further widened its trading band to +/-5 percent from +/-3 percent in October 2022. In January 2016 it announced the VND/USD rate would be adjusted daily rate based on (i) the previous day's weighted average dong/USD exchange rate; (ii) a weighted average of movements in dong exchange rates vis-à-vis seven other important trading partners' currencies; and (iii) domestic macroeconomic conditions.

Vietnam has accepted the obligations under Article VIII, Section 2(a), 3, and 4 of the IMF's Articles of Agreement and maintains an exchange system free of multiple currency practices and restrictions on the making of payments and transfers for current international transactions, except for those exchange restrictions imposed for security reasons of which Vietnam has notified the IMF pursuant to Executive Board Decision No. 144- (52/51), 8/14/52.

Article IV Consultations

Vietnam is on a 12-month consultation cycle. The previous Article IV consultation was held hybrid during March 9-23, 2022, and was concluded by the Executive Board on June 6, 2022.

Technical Assistance

In recent years, Vietnam has received technical assistance (TA) in the areas of statistics (government finance, external sector, price, and national accounts), reserve management, debt management, tax administration, fiscal risks, liberalization of capital controls on external debt, foreign exchange management, and forecasting and policy analysis system (FPAS). The IMF-World Bank Financial Sector Assessment Program was undertaken during 2012–13.

In 2019, the IMF's Institute for Capacity Development (ICD) started a multi-year TA on FPAS. In 2021, Phase I of FPAS TA on modelling capacity was successfully completed and Phase II on structured policy discussion started in April 2022.

In 2022 and 2023, the IMF's Fiscal Affairs Department and the Capacity Development Center of Thailand (CDOT) have provided TA on tax administration and compliance risk management, strengthening Vietnam Treasury's cash management, internal audit, and chart of accounts. TA and training were also provided for the formulation of medium-term debt strategy, debt management institutional arrangement, custom modernization, and pension fund modeling. The IMF's Monetary and Capital Markets Department (MCM) started a multi-year project on strengthening the SBV Internal Audit in Aug 2022. The IMF's Legal Department (LEG) started a multi-year project to help SBV and relevant government agencies strengthen AML/CFT legal frameworks and risk-based AML supervision in November 2022. The IMF's Statistics Department (STA) provided TA on Government Finance Statistics (with CDOT), and National Accounts. CDOT provided TA on external sector statistics in coordination with STA. In April 2023, STA provided a TA to help the SBV transition to the new FSIs compiling format. A scoping mission for a Financial Sector Stability Review (FSSR) took place in 2021, with a full FSSR finalized in June 2023. The FSSR report was approved by the SBV management.

In 2023, ICD started a new multi-year CD on macroeconomic framework to strengthen the capacity of macroeconomic analysis and forecasting of the Ministry of Planning and Investment.

Resident Representative

Mr. François Painchaud is the Resident Representative for Vietnam and Lao P.D.R., based in Hanoi, since June 2019. Mr. Jochen Schmittmann will replace Mr. Painchaud in late August 2023.

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS

World Bank: http://www.worldbank.org/en/country/vietnam

Asian Development Bank: https://www.adb.org/countries/vietnam/main

MAIN WEBSITES OF DATA

State Bank of Vietnam (www.sbv.gov.vn)

Exchange rates

Interest rates

Balance of payments

Credit to the economy

Financial Soundness Indicators

Money Market Operation

Ministry of Finance (www.mof.gov.vn)

Government budget

Customs data

Public Debt Bulletin

Ministry of Planning and Investment (www.mpi.gov.vn)

Public Investment

Foreign Direct Investment

Business registration

General Statistics Office of Vietnam (www.gso.gov.vn)

Price Indices

National accounts

Population and Employment

Investment and Construction

Socioeconomic information

Exports and Imports

STATISTICAL ISSUES

(As of June 29, 2023)

Assessment of Data Adequacy for Surveillance

General: Data provision is broadly adequate for surveillance, although some shortcomings remain where further efforts are needed. In particular, improving the quality of the balance of payments and the timely collection fiscal accounts are a priority. Other areas include national accounts and the financial sector.

National accounts: The General Statistics Office (GSO) provides quarterly and annual data on GDP by type of economic activity and by expenditure (both in current and constant prices), and monthly and annual data on external trade, industrial output, retail sales, and prices. Improving the quality of Quarterly National Accounts (QNA) estimates should be accorded priority, in particular to compile discrete and independent quarterly GDP, using consistent data sources and methods. Currently, the GSO produces cumulative QNA estimates for the first three quarters of the year and the fourth quarter estimate is a residual. The compilation of national and provincial estimates is centralized at the GSO. The National Accounts base year is 2010. Vietnam plans to use 2020 (a year impacted by COVID 19) as the new benchmark year and employ chain-linking volume measures which will help to preserve the structure of national accounts components for each year of the new GDP series. However, finalization of the national account rebase could be delayed to 2024. STA has provided TA for the benchmarking exercise, with a focus on better incorporating non-observed activities, including informal activities, as well as the development of supply and use tables (SUTs) and input-output tables (IOTs).

Prices statistics: The CPI methodology is broadly in line with international standards. Monthly CPIs are released on a timely basis by the end of the reference month. The current CPI weights (2019) were calculated based on the Household Living Standards and CPI weight survey conducted in 2018. The CPI basket is also scheduled to be updated in 2024. Monthly producer and trade price indices are published quarterly. STA TA to support sampling and data collection improvements for services producer price indexes was also conducted. New residential property price indexes were developed by the GSO, although limited availability of administrative source data has delayed progress and publication. Indexes based on data obtained through web scraping were designed but compilation faces challenges mainly due to absence of reliable data.

Government finance statistics: Government operations data reflect the consolidated operations of the state budget, which cover all four levels of government (central, provincial, district, and commune). However, data exclude quasi fiscal activities of the central bank (and state-owned enterprises (SOEs)), and extra-budgetary funds, among which are the Social Security Fund, and the Sinking Fund (for repayment of on-lent funds), for which data are not compiled/disseminated on a regular basis. Compilation is on a cash basis for final annual data but varies for provisional data depending on their source. As a result, government financing data, in particular government cash and domestic financing cannot be reconciled as reported in the fiscal accounts. Moreover, a process of final budget accounts production that takes up to 18 months, the lack of granular recurrent expenditure data by economic classifications, and typically large revisions in the budget outcomes between the 1st/ 2nd budget estimate and final accounts to reflect carryover complicate policy making and timely assessments of the fiscal policy stance. The World Bank and the IMF have recommended improving the coverage of fiscal data and aligning definitions with the *GFSM 2014*. The authorities provided GFSM 2014 consistent data for 2003-2019 based on final budget account, supported by the CDOT.

Monetary and financial statistics: The SBV reports monetary data for the central bank, monetary survey and other depository corporations to STA with monthly periodicity, although using old report forms with very limited information. STA has encouraged the SBV to develop a reporting scheme providing a comprehensive breakdown of data by counterparties and by currency of transaction, which would facilitate the migration to the standardized report forms (SRFs). In October 2018, the SBV informed STA of its action plan to complete the migration to the SRFs by end-May 2019, which is still in progress. The SBV reports data on some key series and indicators of the Financial Access Survey (FAS), including the two indicators of the U.N. Sustainable Development Goals. Vietnam reports 10 of the 12 core financial soundness indicators (FSIs), 7 of the 13 additional FSIs for deposit takers, and one FSI for real estate markets—on a semi-annual basis—for posting on the IMF's FSI website with a 12-month lag. Vietnam has informed STA that it continues to provide FSIs in old format through 2021 and would follow the recommendation of the recent STA TA and apply the new compilation method for 2022 FSIs in July 2023. The new IMF compilation method was introduced with relevant sectoral financial statements (consolidated balance sheet and income statement data) and additional underlying series for the compilation of the new FSIs.

External sector statistics: Starting from 2013 data, the authorities are reporting balance of payments in BPM6 format. Weaknesses persist in the compilation of external sector position statistics—international investment position (IIP) statistics, external debt statistics, and Coordinated Direct Investment Survey (CDIS). While more comprehensive data on external debt flows and positions have become available with recent improvements, capacity constraints prevent the compilation of an overall measure of Vietnam's gross external debt position. Improved BOP compilation data is in needed, especially to narrow the large Errors and Omissions. The annual foreign direct investment survey was last undertaken for 2015 reference year and has been discontinued thereafter. New administrative data sources have been explored to compile direct investment positions. CDOT is helping Vietnam improve the compilation and dissemination of the IIP as well as the compilation of comprehensive external debt statistics, the Coordinated Direct Investment Survey (CDIS), and the reserves data template.

Data Standards and Quality

Vietnam participates in the enhanced General Data Dissemination System (e-GDDS) and launched a National Summary Data Page (NSDP) in July 2019. No data ROSC are available.

Table 1. Vietnam: Common Indicators Required for Surveillance
(As of July 1, 2023)

	Date of Latest Observation	Date Received	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]
Exchange Rates	June 2023	06/28/2023	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	March 2022	5/24/2023	M	M	N/A
Reserve/Base Money	March 2023	6/07/2023	M	M	N/A
Broad Money	March 2023	6/19/2023	M	M	N/A
Central Bank Balance Sheet	Mar 2023	6/07/2023	M	M	N/A
Consolidated Balance Sheet of the Banking System	Mar 2023	6/19/2023	M	M	N/A
Interest Rates[3]	Apr 2023	6/05/2023	M	M	M
Consumer Price Index	June 2023	6/29/2023	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[4]—General Government[5]	March 2023	April 2023	Q	Q	Q
Stocks of Central Government and Central Government-Guaranteed Debt[6]	December 022	June 2023	A	A	Semi-Annual
External Current Account Balance	Q1 2023	6/01/2023	Q	Q	Q
Exports and Imports of Goods and Services[7]	May 2023	6/29/2023	M	M	M
GDP/GNP	Q2 2023	6/29/2023	Q	Q	Q
Gross External Debt	December 2022	June 2023	A	A	A
International Investment Position[8]	...	...	N/A	N/A	N/A

[1]Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); and Not Available (N/A).
[2]Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency, but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
[3]Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[4]Foreign, domestic bank, and domestic nonbank financing.
[5]The general government consists of the central government (budgetary funds, extra-budgetary funds, and social security funds) and state and local governments.
[6]Including currency and maturity composition.
[7]Services data available on an annual basis.
[8]Includes external gross financial asset and liability positions vis-à-vis nonresidents.

Statement by Mr. Anwar and Mr. Hendrayadi on Vietnam
August 30, 2023

On behalf of the Vietnamese authorities, we express our gratitude to the IMF mission team led by Mr. Paulo Medas for the constructive and open policy discussions during the 2023 Article IV consultation. The authorities hold the ongoing engagement by the team in high regard.

Our authorities broadly concur with the staff's assessment and policy recommendations. They underscore the significant importance of maintaining macroeconomic stability to consolidate the recovery and foster sustainable and inclusive growth. Simultaneously, policy priorities revolve around rebuilding policy buffers, ensuring macroeconomic and financial stability, managing inflationary pressures, and mitigating slower growth. In response to macroeconomic developments, fiscal and monetary policies will continue to be proactive, preemptive, and flexible.

The Vietnamese economy demonstrated remarkable resilience amidst global uncertainties, owing to prudent and pragmatic policies. Vietnam's economy managed to achieve a historically high growth rate of 8% in 2022, surpassing that of regional economies and many emerging markets, supported by heightened global demand and recovery in the tourism sector. Going forward, Vietnam's economy is projected to sustain robust growth, albeit at a more moderate pace due to anticipated global growth moderation. The authorities' economic projections largely align with the staff's forecasts, albeit with a more optimistic outlook. The authorities anticipate a strong recovery in the latter half of 2023, supported by sustained external demand and a policy mix to counter potential slowdown risks. Macroeconomic stability remains intact, with inflation expected to remain below the 4.5% target in 2023, accompanied by an improving current account balance.

Monetary and Exchange Rate Policy

Monetary policy, executed judiciously, has effectively managed inflation dynamics and risks to broader macroeconomic stability. In late 2022, the State Bank of Vietnam (SBV) decisively increased interest rates to proactively contain inflation risks, maintain stability, and safeguard the banking system. This strategy proved effective, resulting in a decline in inflation by early 2023 and a return to the target range, and contributing to enhanced financial stability. Core inflation, reflecting underlying demand pressures, has also receded. In anticipation of potential risks of future economic slowdown influenced by global factors that could impact macroeconomic stability, the SBV adopted a preemptive and front-loaded approach, easing monetary policy through interest rate cuts to stay ahead of potential challenges. This relaxation could alleviate the burden on small and micro firms. This relaxation of monetary policy will be complemented by fiscal stimulus and sectoral policies within the context of the national economic policy mix to mitigate the risks of an economic slowdown.

Exchange rate policy prioritizes flexibility to preserve the role of the exchange rate as a shock absorber and to maintain orderly market functioning. In October 2022, the exchange rate trading band was further widened to allow greater exchange rate flexibility and help absorb external shocks, following similar measures in previous years. Foreign exchange interventions were conducted to manage excessive volatility, without targeting specific exchange rate levels. Following the disruptive foreign exchange dynamics at the end of 2022, foreign exchange reserves increased supported by improved external conditions and positive investor’s confidence in Vietnam's economic prospects.

The SBV continues to modernize the monetary policy framework with the support of IMF technical assistance. The SBV has enhanced its forecasting capabilities and strengthened the monetary policy decision-making process. This modernization will progress incrementally and is aligned with efforts to enhance institutional capacity and resources, strengthen domestic regulations, and improve policy coordination. The augmentation of monetary policy tools will be undertaken, considering overall preparedness and the prevailing operating environment.

Fiscal Policy

Fiscal policy is disciplined and a follows a conservative approach, with a view on its impact over the medium- to long-term horizon. Fiscal consolidation is undertaken gradually and prudently, as reflected in the phasing out of pandemic-related measures and transitioning to more targeted policies while considering their implications on economic recovery. Public debt has decreased to 35% of GDP, supported by an improved fiscal balance and strong nominal GDP growth. Government-guaranteed debt continues to decrease as more state-owned enterprises (SOEs) gain access to market financing without government guarantees.

To mitigate the risks of potential economic slowdown, fiscal policy will play a counter-cyclical role through more expansionary measures, aligning with monetary policy. There is ample room for additional fiscal support if circumstances require it, given the successful prior fiscal consolidation efforts and debt reduction. The fiscal position has improved, and there is considerable room to utilize debt securities. Current public debt (including debt of affiliated institutions guaranteed by the government) remains below the National Assembly's 50% debt threshold. Nonetheless, the authorities will exercise prudence and opt for a conservative approach, considering the variability in revenue collection.

The authorities are confident that the expenditure measures in 2023 will support demand. Public wages have been raised by 20.8% after being frozen since 2019, with a well-contained budget impact. Efforts to better target and expand social safety nets continue, particularly focusing on the most vulnerable groups, with technical assistance from the IMF and World Bank. Initiatives to expedite the realization of public investments are also ongoing, to be accomplished through enhanced capacity of implementing officials and streamlined bureaucracy while upholding good governance practices.

The tax reform strategy moving forward aims to strike a balance between sustainable revenue generation and creating a more conducive business environment. Revisions to tax laws have been proposed to revamp the tax base and support businesses. Once approved, the new tax law will be cascaded into regulations at both central and provincial levels before full implementation of the new tax regime.

Financial Sector Policy

The SBV has taken swift and decisive measures to address liquidity challenges in late 2002 due to internal and external pressures. Globally, rising interest rates have widened the gap with domestic interest rates, leading to capital outflows. Domestically, there was negative sentiment arising from turbulence in the real estate and corporate bond markets. To mitigate their impact on the banking sector and broader financial system stability, the SBV swiftly injected liquidity into the interbank market. The liquidity situation has gradually improved, with the banking system currently maintaining sufficient liquidity.

The SBV has also implemented several temporary and targeted measures to support financially distressed corporations, responding to issues in the real estate market and deteriorating economic conditions. These policies have been gradually unwound to mitigate the risk of moral hazard and prevent the emergence of non-viable firms. Certain measures will remain in effect until mid-2024 but are limited in scope, specifically targeting well-performing companies facing production and business challenges due to recent financial stress.

The authorities remain committed to exploring further policy options to mitigate deteriorating credit quality. Mitigating the risk of credit quality deterioration, especially in the real estate sector, involves enhanced supervision and measures for banks to manage non-performing loans (NPLs) while adhering to prudential principles. Credit to the real estate sector continues to be selective, particularly for low-risk ventures, including support for financing government affordable housing initiatives that aim to assist vulnerable households.

Moving forward, authorities acknowledge that reforms are pivotal to promote an efficient, robust, and resilient financial sector that sustainably supports economic development. In this regard, the authorities highly value the Article IV consultation's focus on strengthening the financial sector, particularly on enhancing the effectiveness of debt enforcement and insolvency frameworks and improving crisis preparedness. Recommendations, especially those pertaining to enhancing the legal framework and institutional capacity, have been well-received and will be progressively implemented. The ongoing revision of the Law on Credit Institutions is a step toward expediting structural reforms in the financial sector.

Significant efforts have been made to enhance the credibility and investors' confidence in the bond market. These efforts include the issuance of Vietnamese Government decrees that provides further clarity on investor status, issuance purposes, and principles for utilizing bond capital. Market infrastructure will be reinforced with the involvement of rating agencies. Moreover, consumer education efforts will be intensified and expanded as a preventive measure.

Structural Policies

The authorities remain resolute in their commitment to accelerate structural reforms to achieve sustainable and inclusive growth and facilitate the transition to a more developed economy. They highlight ongoing efforts to address legal uncertainties and reduce excessive administrative burdens, aimed at enhancing the business environment and fostering economic expansion.

Efforts to enhance data quality and availability are ongoing and are being gradually implemented. Necessary upgrades to legislative and IT frameworks to enhance data quality and availability need to be planned and sequenced appropriately, considering the involvement of various agencies and the need to amend several statistical provisions. The technical assistance received from the IMF is highly valued, and the authorities remain committed to its implementation. While awaiting a more robust regulatory data framework, authorities are diligently preparing various datasets that adhere to international standards, serving both Article IV consultations and domestic requirements.

The authorities remain committed to enhancing governance and strengthening the Anti-Money Laundering and Counter Financing of Terrorism (AML/CFT) framework. Ongoing efforts to accelerate the implementation of AML/CFT measures aligned with FATF standards will be expedited. They recognize the need for stronger engagement to gain buy-in from the various stakeholders involved. Efforts also encompass revising various existing legal provisions to accommodate AML/CFT-related measures.

Vietnam has formulated a comprehensive national strategy for climate adaptation and mitigation, in line with COP26 commitments. This involves concerted action across various ministries and state institutions and the development of enabling regulations. In this regard, the IMF's technical assistance on the implementation of the Emission Trading System (ETS) is welcomed. The authorities would also appreciate technical assistance on other non-price measures that are more feasible for near-term implementation.

Conclusion

Vietnam's economy is poised to continue growing at a reasonably healthy pace, supported by the coherent blend of prudent and pragmatic policy measures. Going forward, the policy direction will remain proactive and adaptable, factoring in the dynamics of external and domestic risks. Policies will take into consideration the characteristics of the Vietnamese economy, which heavily depends on external demand.

The Vietnamese authorities reiterate their strong commitment to pursue structural reforms to achieve sustainable and inclusive growth. The modernization of the legal and institutional framework is progressing, and efforts are ongoing to strengthen governance, AMLF/CFT, and address climate risks. Technical assistance from the IMF and other international organizations are of immense value and is highly appreciated. Looking ahead, the realization of this ambitious structural reform agenda necessitates meticulous planning, prioritization, and phased implementation, considering the available resources, to yield optimal benefits for Vietnam.