Macroeconomic Review
2013

Report No. 01/2013

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2012 – A year in review

Global economy

Global growth has remained subdued through 2012 and the international outlook remains tepid. The global economy is expected to continue making a cautious recovery over the coming years, with a strong contribution from Asia. A euro area close to or in recession, and sluggish growth in the United States and other major advanced economies are all providing headwinds to against growth in developing economies like Vietnam. While global policy responses commencing in late 2011 have substantially lowered immediate short-term risks, it appears the global economy remains in the midst of an impasse, with further policy intervention establishing credible long-term fiscal strategies still necessary to ensure a return to more stable growth. Notwithstanding these pressures, if the global economic and financial momentum of late 2012 is sustained, the global economy is expected to see much healthier growth in 2013 (Figure 1).

Figure 1: Growth in selected economies


Events in the euro area remain a key downside risk to the world economy. Although activity in Europe has ceased to contract at an alarming rate, thanks in part to measures adopted in late 2012, growth prospects remain weak. General consensus suggests this weak demand is expected to extend well into 2013, consistent with indicators of poor sentiment and stubbornly high
unemployment rates. While the adjustment of structural imbalances has begun, much more will be needed to ensure long-term sustainability in the euro area. Against this background of deleveraging, fiscal consolidation and weakening global trade, prospects for a sustained recovery in Europe not surprisingly, remain uncertain. The OECD in its October 2012 Economic Outlook expects the euro area to remain in or near recession until well into 2013 (Table 1).

**Table 1: Global growth estimates**

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<thead>
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In the US, growth remains moderate, providing welcoming news for one of Vietnam’s largest export destinations. Consumer sentiment has improved, reflecting a gradual pick-up in the labor market and better conditions in the housing market. Encouragingly, monetary policy is expected to remain highly accommodative for as long as the unemployment rate remains above 6½ per cent. However, there is still considerable uncertainty surrounding ongoing fiscal debt negotiations in early 2013. If unresolved, there is a very real prospect of the US tipping into recession and potentially triggering another major global financial shock.

While the outlook for the euro area and US continue to be tepid, growth prospects for the emerging market economies of Asia remain the key driver of overall global growth. Growth in China appears to have stabilized albeit, at a slightly lower than previously expected rate, and inflation remains contained. Looking ahead, ongoing fiscal support for infrastructure and improved conditions in the residential property market has positioned China for what appears to
be a robust growth. Continued growth in China is expected to support demand for commodities and activity in East Asia.

The news is more mixed in Japan. While the Japanese economy appears to be contracting, in part, due to the economic consequences arising from territorial disputes with China, recent indicators of sentiment have improved on the back of the recent election result. There are now hopes the new government will follow through with a more substantial recovery plan in what is still one Vietnam’s largest trading partners. For the lower-income economies in the region, growth is expected to remain close to trend.

Overall, global growth estimated by the World Bank in its January 2013 Global Economic Prospects report will be around 2.3 percent in 2013 and 2.4 per cent in 2014, slightly below trend. Abstracting from the GFC years, this will represent the slowest rate in global growth in almost a decade. The IMF in a January 2013 update of its World Economic Outlook remains more optimistic, with growth in 2013 and 2014 estimated to be 3.5 and 4.1 per cent, respectively.

**Financial markets**

Global financial markets posted only moderate gains in 2012, consistent with slow global economic growth. After rallying in early 2012, global financial market’s appetite for risk declined markedly as a consequence of the ongoing euro area sovereign debt crisis. Since August, however, aggregate financial conditions have improved and there has been a marked decline in volatility, consistent with the declining perceptions of adverse risk. Global markets have remained relatively steady, reflecting the more positive stream of policy announcements and economic news stemming from the major economies. Further down the track, sovereign debt issues in the euro area and US are likely to remain key risks for financial markets in 2013.

The euro area’s continued sovereign debt crisis, particularly evident during the middle of 2012 continued to be reflected in global financial markets. In particular, sovereign bond yields issued by some of the most troubled euro area countries and declining equity prices, especially among European banks were the subject of numerous headlines. Since August, there has been a marked improvement in global financial markets, largely reflecting the European Central Bank’s Outright Monetary Transactions announcement to preserve the euro area monetary union. As a result, money market rates, credit default swap rates, and bond yields have eased together with an improvement in equity markets. Equity prices in the euro area rose 5.8% over 2012.

In the US, recent conditions have improved in virtually all financial market sectors. Credit growth remains solid, consistent with an accommodative monetary stance and equity prices have rallied over the latter half of 2012, to be at their highest level in five years (Figure 2).
Across the Pacific, Japan remains a relatively safe refuge for capital inflows, in part, due to the ongoing events in Europe. However, this safe-haven status has proven to be a double-edged sword. On the one hand, government bond yields remain at near-record lows, enabling easy financing for Japan’s already high public debt. On the other, the continual inflow of capital has maintained upward pressure on the Yen, thus hampering an already weak exports sector. Compounding these existing pressures will unfolding ramifications of Japan’s newly announced inflation target of 2%.

Financial market conditions in emerging Asia have also improved recently. While past performance, of course, is not a guarantee of future performance, capital investment in the Southeast Asian giants of China and India remains solid. Consistent with the performance of the financial markets, equity prices in the region, reflected through the broader S&P Emerging Asia Pacific Index have grown by around 17% over 2012.

In contrast to these more developed Asian markets, activity in Vietnam’s financial markets remain largely unpredictable, with the VN Index growing by around 9% over 2012 (Figure 3). Domestic loans in Vietnam have continued to grow at a relatively modest pace in recent quarters, despite a downturn in business credit.
Overall, along with the renewed vigor by the United States’ Fed and Bank of Japan to engage in further quantitative easing, the price of risk worldwide has rescinded. However, market confidence remains fragile, and ongoing concerns about regarding European banks’ solvency or the resolution of the US’ fiscal negotiations have yet to dissipate, particularly in the context of soft global demand.

**The Vietnamese economy**

**Aggregate output**

Against this soft global backdrop, the fundamentals of the Vietnamese economy remain strong and the outlook remains positive. GDP grew by 5.03% in 2012 (Figure 4 and 5), driven by solid growth in services (6.42%), industry and construction (4.52%) and modest growth in agriculture, forestry and fisheries (2.72%). While the global environment has moderated growth in Vietnam to some extent, the soft growth outcome in 2012 was mostly a self-inflicted consequence of inflation-curbing policy in second half of 2011. With the effects of earlier intervention largely complete, demand is expected to strengthen over the next year and inflation is expected to be contained. However, strong growth is not guaranteed. Continued structural reform remains necessary with fiscal prudence, improved governance and human-capital investment all forming essential ingredients for maintaining strong growth. GDP growth for Vietnam is projected to lift to around 6 per cent in 2013. Consistent with trends over the past decade, the services and
industry and construction sector will continue to become increasingly important drivers of growth.

Figure 4: Growth in real and nominal GDP

![Figure 4: Growth in real and nominal GDP]

Source: General Statistics Office, CEIC data and DEPOCEN.

Figure 5: Industry contribution to real GDP growth

![Figure 5: Industry contribution to real GDP growth]

Source: General Statistics Office, CEIC data and DEPOCEN.

Production

Agriculture, forestry and fisheries

The agriculture, forestry and fisheries sector grew by 2.72% in 2012, driven by strong growth in forestry (up 6.4%), fishery (up 4.5%) and a slight increase in agriculture (up 2.8%). Overall, this sector contributed 0.44 percentage points to GDP growth in 2012. Abstracting from the global recession, growth in 2012 represented the slowest pace in over a decade. Looking ahead, a recovery in growth is expected from this sector, with long-run trend forecasts of around 3-3½% per year.

1) Agriculture
Total rice production in 2012 grew around 3% in 2012, to reach an annual estimated output of 43.7 million tons. The increase in rice production was due to a combined increase in cultivated area (1.3%) and higher productivity (1.6%).

Live-weight meat production in 2012 was estimated to have reached 4.3 million tons, an increase of 2.5% on 2011. The increase was driven by growth in buffalo meat (0.8%), beef (2.4%), pork by 2% and poultry (4.8%).

2) Forestry

The forestry sector has seen rapid growth in recent years. 2012 continued this trend, with growth in decentralized planted trees rising by rose 0.3%; cultivation areas rising 34.8% and areas under protection rising by 12.6%. Total damaged areas are now estimated to be 3,225 ha, a decline of 18% compared to 2011.

3) Fisheries

Fisheries production in 2012 reached 5,732,900 tons, representing an increase of 5.2% on 2011. The increase was mainly driven by strong growth in total fish production (up 5.3%), with a small contribution from shrimp production (up 0.3%).

Aquaculture production in 2012 reached 3,110,700 tons, a rise of 6.1% on 2011. The increase was driven by a 6.5% rise in fish production, offset by a small decline in shrimp production of 1%.

Industry and construction

2012 was another soft year for the industry and construction sector, with growth of around 4.5% (Figure 7). Perhaps worryingly, the past two years have represented the slowest growth in over a decade. 2012’s Industrial Production Index (an aggregate measure of industries such as manufacturing, mining and utilities) rose 4.8% from 2011, of which mining and quarrying rose 3.5%, manufacturing by 4.5%, power and gas by 12.3%, and water supply and waste management by 8.4%. Should 2013 and 2014 see a repeat performance of 4% annual growth rates, real GDP could be lower by as much as 1 percentage point per year. As such, concerted effort by government is needed to ensure a return to long-run average growth rates of around 6% per year.
Services grew by 6.4% in 2012, a pace that was slightly the long-run average growth of 7½ per cent. In the context of a turbulent 2012, however, the services sector remains a star performer in the Vietnamese economy, driving much needed economic growth. Indeed, growth in services has remained broad-based for much of the past decade and is expected to continue through 2013 (Figure 8).

4) Total retail sales
As estimated, 2012’s total retail sales of consumer goods and services rose 16% from 2011 (if the factor of inflation were excluded, it would be 6.2%), of which the state economic sector took 12.3% and decreased by 1.2%; the non-state economic sector took 84.8% and increased by 18.4%; the FDI sector took 2.9% and increased by 34.7%. Considering by business sector, trade business took 77.1% of the total and rose 15.2%; hotel and restaurant 11.8% and by 17.2%; service 10.1% and by 19.6%; tourist 1% and by 28.1% respectively.

5) Transport
Passenger transport in 2012 rose 12.2%. By transport category, land transport was estimated to rise 13.4% followed by rail transport (up 2%). These increases were offset by declines in river transportation (down 3.4%), sea (down 2.4%) and air transportation (down 0.2%).
Total cargo transport was estimated to increase by 9.5% in 2012. The result was driven by a strengthening domestic transport sector (up 10.4%), offset slightly by weakness in overseas cargo transport (down 12.4%). By transport category, land and river cargo increased by 11.5% and 6.8% respectively while falls were evident in sea transport, down 14%, and rail transport, down 3.9%.

6) Postal and communication services
2012’s new telephone subscribers reached 12.5 million, rose 5.5% from last year, including 16,500 desk telephone subscribers, equaling 33.4% from 2011 and 12.5 million mobile phone subscribers, rose 5.8%. The number of telephone subscribers over the country as late December 2012 was at an estimation of 136.6 million, rose 2.7% from last year’s same period, including 14.9 million desk telephone subscribers, reduced 2.9% and 121.7 million mobile phone subscribers, reduced 2.9%.
subscribers, rose 3.5%. The number of new broadband internet subscribers in 2012 was 355,600. As of late December, total internet subscribers over the country were at an estimation of 4.3 million, rose 5.4% from last year’s same period. 2012’s total postal and communicational service net income was at an estimation of 179.9 trillion dongs rose 7.6% from 2011.

7) Tourism and travel
The international tourism and travel sector remains strong, with an estimated 6,647,700 people visiting Vietnam in 2012, a rise of 9.5% from last year. The strong result was driven by across the board increases in tourism (4,170,900 arrivals, up 7.3%), business (1,166,000 arrivals, up 16.2%) or visiting relatives (1,150,900 arrivals, up 14.3%).

![Figure 8: Growth in the services sector](image)

Source: General Statistics Office, CEIC data and DEPOCEN.

External demand

Exports
Despite the global turbulence of 2012, Vietnamese exports continued to surge, quadrupling over the past decade. The growth, in part, reflects Vietnam’s increasing competitiveness in the global economy. The value of goods exports in 2012 reached around 114.6 billion USD, an 18.3% increase from 2011. The increase was almost entirely driven by growth in FDI. In 2012, FDI increased by 31.2% to reach 72.3 billion USD (a 17.7 percentage point contribution to growth) while the domestic sector increased by a mere 1.3% to reach 42.3 billion USD (contributing 0.6 percentage points to growth).

Exports of heavy industrial and mineral goods reached an estimated 51.7 billion USD, a rise of 49.9%. Growth in this category was mainly confined to strength in exports of telephones and components. Agricultural and forestry exports rose to 17.7 billion USD, with growth of 18% in line with overall exports. By destination, the EU overtook the US in 2012 to become Vietnam’s largest export partner. Exports to the EU rose by 22.5% to reach an estimated 20.3 billion USD, or around 18% of total exports turnover.

Services exports in 2012 reached an estimated 9.4 billion USD, rising 6.3% compared to 2011. The fastest growth came from the tourism sector which grew by 18% to reach 6.6 billion USD. The largest fall was in the transport sector, falling by 15.5% to 2.1 billion USD.

Imports
The value of goods imports in 2012 grew to 114.3 billion USD, an increase of 7.1% from 2011. Excluding the 2009 global recession, this was the slowest growth in imports since 2001. The increase was almost driven by growth in FDI. In 2012, FDI increased by 23.5% to reach 60.3 billion USD while the domestic sector decreased by a 6.7% to reach 54 billion USD (contributing 0.6 percentage points to growth).

Imports of intermediate goods (means of production) grew by around 10% in 2012, reaching an estimated 106.5 billion USD. This was driven by greater demand for machinery and equipment and assembly goods imports. In contrast, imports of raw materials fell by around 2%. By destination, China remains by far, Vietnam’s major source of imports. With growth of imports from China rising by 17.6% in 2012 and accounting for 28.9 billion USD, Vietnam’s share of imports from China rose to 25.3%. Growth in imports from South Korea (up 18.4%), Japan (up 12.2%) and EU (13.3%) also grew.

Services imports grew by 5.7% in 2012 to reach 12.5 billion USD. The largest sectors contributing to this growth was the transport services sector (up 6%, 8.7 billion USD) and tourism (up 8.5 per cent, 1.9 per cent).

Overall, Vietnam recorded a small trade surplus of 284 million USD in the year to 2012 (Figure 9), the first since 1993. The result was driven by a significant trade surplus of 12 billion USD in FDI (72.3 billion USD in exports, 60.3 billion USD in imports) and offset by a trade deficit in the domestic sector of 11.7 billion USD (42.3 billion USD in exports, 54 billion USD in imports). The services balance was also in deficit, reaching 3.1 billion USD (9.4 billion USD exports, 12.5 billion USD imports). Looking ahead, domestic development of Vietnam’s economy and a recovery in global markets suggest growth in Vietnam’s trade will continue to be strong through 2013.

**Figure 9: Industry contribution to real GDP growth**

![Chart showing Industry contribution to real GDP growth](source: General Statistics Office, CEIC data and DEPOCEN)

**Consumer prices**

The outlook for inflation remains uncertain. After a volatile 2011, inflation moderated considerably in 2012. 2012’s average CPI rose 9.21%, slightly below the State Bank’s target of 10%. The fall in the inflation rate from the highs of 2011 was mainly a consequence of easing food and transportation cost pressures (Figure 10). Since January 2013, monthly inflation has increased 1.25%, following an increase of 0.3% in December. In year-on-year terms, inflation has grown at 7.07%, slight up from 6.8% in December 2012. While inflation has indeed moderated over 2012, the longevity of this period of moderation is not clear.
In 2012, the fastest growing consumer price categories were for health, (up 17.4%) education (up 17.1%) and meals and drinking outside (a category of food, up 13.8%). The slowest growing categories include post and telecommunications (down 1.1%), food (up only 3.5%) and culture, sport and entertainment (up 5.6%). Although inflation appears to have moderated over recent periods, one worrying trend shown in the previous figure has been the steady increase in health and personal care prices since mid-2012. When coupled with the potential for more food-related price increases, inflation in 2013 could well return to previous highs. As a result, the Government’s target inflation rate of 8% remains an ambitious.

Risks and Outlook

Since late-2011, short-term risks to the global economy have been alleviated. As a result, 2012 saw an ongoing, albeit staggered recovery. While 2012 was a somewhat turbulent year, recent global economic indicators have been generally positive and downside risks have subsided. The United States had temporarily avoided falling off their “fiscal cliff”, while earlier policy measures in Europe and recently announced policies by the new Japanese government have improved global market conditions. Data from China has continued to indicate stabilizing growth.

With the many of the dangers of 2012 now consigned to history, the central expectation among many global institutions is for an improvement in global economic growth for 2013. The focus in Europe and the US will now turn to whether the extent of ongoing fiscal consolidation will prove too effective in hampering medium-term growth.

In Vietnam, the simultaneous recovery among a number of significant trade partners is providing a significant upside risk to Vietnam’s economic growth. In an environment where price volatility has been largely controlled, Vietnam is expected to grow slightly faster than the 5% growth recorded in 2012, off the back of an improving external sector. Although pre-global recession growth rates are unlikely to be achieved, real growth is expected to be around 6% in 2013 and 2014 (Table 2). The projected growth in real GDP is based on a simple 5-year moving average growth of each production sector. While this represents a rather crude approach, overall growth of 6% (rounded to the nearest ½ of a percentages point) is consistent with the IMF’s October
2012 WEO growth rate of 5.9 per cent and 6.4 per cent for 2013 and 2014 respectively. More importantly, in the context of a growth global recession for Vietnam, the 5-year average represents a reasonable growth expectation, especially after such a subdued 2012 outcome. By contrast, the outlook for CPI inflation in 2013 and 2014 is slightly higher than the Government’s more ambitious 8% target and reflects broader trends over the past 5 years (further discussed in Box A).

Table 2: Vietnam growth estimates

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(a) Year-average growth unless otherwise indicated.
(b) Year-on-year to December.

Source: GSO and DEPOCEN.

While external risks have improved, domestic risks to Vietnam remain unchanged and largely, on the downside. Like much of the past decade, continued global and regional integration will continue benefitted growth over much of the past decade. However, this increased integration has also led to greater vulnerabilities to global capital shocks. Indeed, the Vietnamese banking system remains underdeveloped, raising questions about their ability to withstand shocks from abroad. Efforts must also be made to address overleveraged and underperforming state-owned enterprises. Without continued progress in the development of domestic capital markets, the prospect of a global downturn triggering another episode of macroeconomic instability remains very real.
Box A: Income growth and price dynamics

The value of any economic transaction within a given period is typically measured as the product of the quantity produced or sold, and a unit price of the good or service. Nominal GDP for example simply the sum of all individual transactions within a period and any change in GDP over time is due to a combination of changes in volumes and prices. The former is often referred to as real growth while the latter reflects inflationary impacts. While growth in real GDP is regularly touted as a measure of improving living standards, fiscal obligations ensure that governments must also be equally mindful of growth in nominal GDP.

Price effects are usually measured in two ways. The ratio of nominal GDP to real GDP, known as the GDP deflator, measures the overall change in the price of all output relative to a base year. The more commonly used measure of inflation the consumer price index (CPI). The CPI is a measure based on a representative basket of only consumer goods and services. Though a narrower indicator, it is easily measurable and less prone to revision therefore the most common inflation measure targeted by governments. The difference between the two measures in practice is not large (Figure A1).

While the two price measures regularly align for most developed countries due to the size of the household sector, this phenomenon is unusually striking for emerging Vietnam. Nevertheless, in the context of the National Assembly’s recent 5½% GDP growth and 8% CPI growth target for 2013, this relationship suggests nominal GDP growth of 2013 will be around 13½%, a growth rate not achieved since the early 2000s (Figure A2).

Taking a more cautious approach, therefore, we believe inflation in 2013 is likely to be higher than the official target. To be consistent with real growth of around 5-6%, inflation would need to be around 10 per cent over the coming year, resulting in nominal GDP growth of around 16%.

Figure A1: CPI and the GDP deflator growth

Source: GSO, IMF data (via CEIC) and DEPOCEN.

Figure A2: Nominal GDP growth

Source: GSO and DEPOCEN.

The National Assembly’s implied target of 13½% nominal growth is indeed a challenging goal, particularly given the heightened volatility since the global recession. In a world where foreign investors are increasingly sensitive to Vietnam’s domestic macroeconomic conditions, the consequences of over applying the monetary policy brakes to slow inflation could be immense.

While the two price measures regularly align for most developed countries due to the size of the household sector, this phenomenon is unusually striking for emerging Vietnam. Nevertheless, in the context of the National Assembly’s recent 5½% GDP growth and 8% CPI growth target for 2013, this relationship suggests nominal GDP growth of 2013 will be around 13½%, a growth rate not achieved since the early 2000s (Figure A2).
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