RESTRUCTURING FOR A MORE COMPETITIVE VIETNAM

MACROECONOMIC REPORT FOURTH QUARTER AND 2015

INTRODUCTION

Vietnam's economy is entering into major transfers. The transfer is not only between socio-economic planning periods (for 2011-2015 and 2016-2020 respectively), but also from macroeconomic stabilization and growth recovery to further promotion of economic growth and integration. After years of focusing on macroeconomic policies, Vietnam has paid more attention to microeconomic reforms and facilitating the development of business community. The current business environment and economic conditions exhibited major improvements compared to the beginning of 2011 – starting point of Socio-economic Development Plant in 2011-2015. The macroeconomic environment became more stable and sound. The economic recovery appears to be more robust, accompanied by improved confidence of investors, business community and individuals. Policy space for loosening the fiscal and monetary policies has been reduced significantly, implying the need to utilize such space more effectively and focused. International economic integration has significantly broadened economic opportunities, whilst inducing parallel market-oriented reforms in Vietnam.

Looking forward, the economic reforms and integration will be accompanied by challenges, namely: (i) that political will for reforms may not match practical requirements; (ii) inadequate awareness of opportunities, challenges and requirement of practical reforms and international economic integration, as well as the role of State and Government in management; and (iii) ample adjustment costs for selected groups of people and enterprises. To a certain extent, economic reforms in 2011-2015 were slow and not effective as expected. However, this lesson emphasized the need for more fundamental and focused reforms beyond 2015. In this context, the roles and core benefits of business community will form the center of economic reforms and policy adjustment.

The Macroeconomic Report for Q4 of 2015 serves several objectives, including: (i) to update macroeconomic developments and policy changes in Q4 and 2015 with evidence-based analysis and perspectives of experts/Central Institute for Economic Management (CIEM); (ii) to assess the macroeconomic outlook for 2016; (iii) to cover selected economic issues based on quantitative and/or qualitative assessment; and (iv) to propose recommendations on economic reforms (including institutional reforms) and on policy solutions for macroeconomic management in 2016.

During the preparation and finalization of the Report, the authors have received many valuable comments of various experts of CIEM, as well as other Ministries and agencies.

On this occasion, the CIEM would like to thank "Restructuring for More Competitive Vietnam" (RCV) Project for providing financial support to preparation of the Report.

The Team would also dedicate our special thanks to Mr. Raymond Mallon, RCV Project Advisor for valuable and insightful comments.

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All remaining errors, views and opinions presented in the Report are solely of the authors and may not necessary reflecting those of RCV Project and/or CIEM.

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LIST OF ABBREVIATIONS

ADB	Asian Development Bank
AEC	ASEAN Economic Community
AFF	Agriculture – Forestry and Fishery
ASEAN	Association of Southeast Asian Nations
BOJ	Bank of Japan
BOP	Balance of payment
CPI	Consumer Price Index
DB	Doing business
SOE	State-owned Enterprise
ECB	European Central Bank
EPA	Economic Partnership Agreement
EU	European Union
FDI	Foreign Direct Investment
FED	Federal Reserve System
FTA	Free Trade Agreement
GB	Government Bond
GDP	Gross Domestic Product
GSO	General Statistic Office
HNX	Hanoi Stock Exchange
HSBC	The Hong Kong and Shanghai Banking Corporation
IFS	International Financial Statistics
IIF	The Institute of International Finance
IIP	Index of Industrial Production
IMF	International Monetary Fund
MoM	Month on month
M&A	Merge and Acquisition
PBOC	People’s Bank of China
PIMA	Public Investment Management Assessment
PMI	Purchasing Managers Index
PPP	Public Private Partnership
QoQ	Quarter on quarter
RCEP	Regional Comprehensive Economic Partnership
REER	Real Effective Exchange Rate
SBV	State Bank of Vietnam
TPP	Trans-Pacific Partnership
TTIP	Trans-Atlantic Trade and Investment Partnership

USD	US Dollar
VAMC	Vietnam Assets Management Company
VND	Vietnam Dong
WB	World Bank
WEF	World Economic Forum
WTO	World Trade Organization
YoY	Year on year

EXECUTIVE SUMMARY

1. In 2015, the global economy was slowing down and growth recovery was uneven among economies. China's economy exhibited more signs of instability; economic growth in the US continues to recover; Japan's economy showed positive improvements in Q4; European economies remained lackluster. International organizations have continuously loweredd the global economic forecast. Political instability and warfare in Middle East, and influence-targeted competition between large economies has brought about complicated implications and difficult projections.
2. Emerging economies were under stress due to retrieval of foreign capital back to developed countries (US, EU). USD appreciated significantly against other major currencies in Q4/2015. International commodity prices decreased further Q4/2015.
3. The year 2015 witnessed major progresses in trade and investment liberalization. Notably, negotiation of the TPP was concluded in early October 2015. Other FTAs (RCEP and TTIP) have progressed in numerous areas.
4. Vietnam's economic restructuring has gained significant outcomes in all three focal areas, including: public investment, SOEs and credit institutions. Vietnam has also improved significantly some criteria of a market economy (as per the US and EU criteria). However, requirements on economic restructuring and shift of growth paradigm remained essential in: (i) restructuring public investment; (ii) restructuring credit institutions; (iii) Enhancing regional linkages; and (iv) SOE reforms.
5. GDP growth attained 7.06% in Q4/2015 and 6.68% for 2015. This pace was still lower than the average figure for 1990-2006 and equivalent to long-term trend. Consumption and investment were major contributions to the recovery of aggregate demand.
6. Industry and construction were the main driver of economic growth, increasing by 9.6% in 2015. IIP rose by 9.8%. However, growth of industrial sector lack sustainability. PMI varied markedly in Q4/2015. Main risks to further industrial growth include: (i) the slow recovery of global economy, especially the more sluggish growth of China's economy; (ii) lack of concrete policies for stimulating the sector; (iii) immaterial reduction of interest rate; and (iv) increase of labour-related cost in 2016.
7. The value-added of agriculture-forestry and fishery grew by 3.2% in Q4/2015 and of 2.4% in 2015 (YoY), reflecting insignificant improvement over previous years. The service sector rose by 6.7% in Q4/2015 and attained 6.33% for 2015 (YoY). Vietnam's retail market became significantly less attractive. Economic structure by sector hardly changed in Q4/2015.
8. The number of newly registered enterprises increased by 22% and 26.6% (YoY) in Q4 and 2015, respectively. In 2015, 21,506 enterprises came back to business, up by 39.5% (YoY). Manufacturing enterprises had positive

assessment of production and business in late 2015 as well as business tendency in Q1/2016.

9. As of 1 January 2016, total labour force was 54.61 million people. By economic sector, the share of labour in agriculture-forestry and fishery sector was 44.3%; and industry-construction sector accounted for 22.9%. The working-age unemployment rate was 2.31% in 2015, higher than that of 2013-2014. Labour productivity for the whole economy attained VND 79.3 million per labour in 2015, up by 6.4% compared with 2014 and by 23.6% compared with 2010; yet productivity improvement remained lower than the target.

10. CPI went up slightly toward the end of 2015. CPI was up by 0.2% and 0.6% in Q4/2015 (compared to Q3/2015 and end of 2014, respectively). In Q4/2015, only price of transport services decreased, while price indices of other goods and services went up. Inflation risks persist in 2016.

11. VND-denominated deposit rate (for terms shorter than 6 months) was stable and below the ceiling rate imposed by the SBV. In mid-December 2015, the SBV lowered the ceiling on USD-denominated deposit rates of individuals to deepen efforts in the roadmap towards reducing dollarization and to reduce USD hoarding. USD-denominated lending rate remained stable in Q4/2015, and only slightly decreased at joint-stock commercial banks.

12. Outstanding credit increased by about 6.5% in Q4/2015. There remained several challenges to credit management in Q4/2015 and 2015, including (i) pressure on interest rates; (ii) increase in “maturity mismatch”; (iii) high lending rate; and (iv) “credit fragmentation”, which in turn undermined the efficiency of credit allocation. NPL fell to 2.93% by end of September 2015. Total liquidity increased by 3.26% in Q4/2015.

13. The VND/USD exchange rate was more stable in Q4/2015. The SBV effectively dealt with risks and fluctuations in the foreign exchange market in Q4/2015. The new exchange rate mechanism may enable SBV to better consider and respond to more rapid and complicated changes in both domestic and international markets in 2016. REER of Vietnam increased by 0.44% in Q4/2015, implying that Vietnamese goods became cheaper relative to foreign ones.

14. Items of the BOP varied drastically in Q3/2015, with overall deficit of USD 6.6 billion, mainly attributed to the deficit of financial account. Current account surplus attained USD 655 million in Q3/2015, lower than in Q2/2015.

15. Investment activities accelerated in Q4/2015. Gross investment attained VND 450.7 trillion in Q4/2015, and VND 1,367.2 trillion in 2015. The investment to GDP ratios in Q4/2015 and 2015 were 34.1% and 32.9%, respectively. Investment expansion in 2015 was mainly in the foreign-invested sector, and domestic private entities. Registered FDI capital attained USD 5.6 billion in Q4/2015; total figure for 2015 was 12.5% higher than in 2014. Implemented capital of FDI in 2015 went up by 17.4%. Disbursement of state budget and government bonds became more rapid in Q4/2015.

16. Exports attained USD 41.89 billion in Q4/2015 (YoY growth of 4.5%) and USD 162.11 billion in 2015 (YoY growth of 7.9%). Export growth in 2015 was lower than the corresponding figures for 2011-2014, and lower than the target for 2015. Imports were estimated at USD 41.9 billion in Q4/2015, up by 3.5% (YoY). In 2015, imports amounted to USD 165.65 billion, increasing by 12%.
17. Total retail sales of goods and services in Q4/2015 were valued at VND 851.6 trillion, increasing by 6.5% (YoY). The figure for 2015 was VND 3,200 trillion, up by 9.5% (YoY).
18. Budget revenues reached VND 306.7 trillion in Q4/2015, equivalent to 22.9% of GDP. In 2015, budget revenues reached VND 989.7 trillion, 8.6% higher than the planned target and up by 14.6% (YoY). Accumulated budget expenditures (by end of December) were estimated at VND 1,093.7 trillion. The value of newly issued government bonds amounted to VND 101.0 trillion in Q4/2015 and VND 197.4 trillion in 2015.
19. The forecast result shows that YoY economic growth in 2016 may reach 6.82%. Export growth is projected at 10.4%, higher than in 2015. Trade deficit is projected at USD 4.1 billion, mainly due to smaller earnings from crude oil exports. CPI inflation is forecast at 4.37%.
20. The Report analyzes the improvement of Vietnam's competitiveness in 2014-2015. Vietnam's competitiveness in 2015 has significantly improved from that in 2014, gaining 12 places. Vietnam is currently listed in the group of countries in transition from Stage 1 (factor-driven growth) to Stage 2 (efficiency-driven growth). Improved competitiveness in 2015 resulted from various policies to lessen difficulties, and facilitate business activities. Nonetheless, Vietnam's enterprises still encounter several challenges and shortcomings, including (i) high borrowing costs (relative to international capital market); difficulties in diversifying capital sources and accessing credit; competitive non-neutrality between domestic private enterprises and SOEs and/or FDI; prevalence of obstacles and barriers to business activities due to administrative procedures; (ii) Slow improvement of access to credit, changeable policies, inadequate training for labour and lack of professional work attitude; inadequate guidance and support from authorized agencies to domestic private enterprises to better prepare for integration arrangements.
21. The Report also provides detailed analysis of the medium-term investment plan for 2016-2020 with expected positive effects, including (i) gradual resolution of issues related to dual budgeting; (ii) improved preparation of investment projects; (iii) improved likelihood of macroeconomic balances which increases policy space for various agencies; and (iv) publicity and transparency of resource allocation, ultimately helping the restructuring of public investment. Yet actual implementation process faced some difficulties in projecting capital for 2016-2020; reviewing public investment projects; and allocation plan. The Report also discusses potential impacts of medium-term public investment plan on the restructuring of public investment.

22. Vietnam enters the year 2016 with remarkable improvements and optimism. Macroeconomic stability is further enhanced. Economic growth has recovered noticeably from one quarter to another, with ample room for further improvement. Confidence of investors and the business community has become more vivid. A new government apparatus will be established soon, aiming at achieving socio-economic development objectives in line with reforms during 2016-2020. In this context, macroeconomic stabilization has so far served as the initial foundation. Vietnam should quickly implement deeper and broader reforms related to microeconomic foundations and the regulatory system in order to further facilitate business and production activities.

23. The opportunities from integration and domestic economic reforms are significant. The business community and the citizens may believe in Vietnam's potentials during integration process. Yet those potentials would only become prospects and be realized in an appropriate policy environment. This Report re-emphasizes the priority of strengthening microeconomic foundations and reforming economic institutions for a modern market economy. Vietnam should proactively and substantially enhance the business environment via simplification of administrative procedures, reduction of burden to business, market liberalization, business facilitation. The country should also encourage and improve technological capacity for sustainable improvement of productivity. These lines of efforts should be made even before related commitments under economic integration arrangements. The Report also presents detailed recommendations on the conduct of monetary policy, fiscal policy, trade policy, price policy and FDI policy.

I. ECONOMIC CONTEXT IN Q4 AND 2015

1. *Regional and global economic context*

1. In 2015, the global economy was slowing down. Growth recovery was uneven among economies. The weakness of global economy became clearer in Quarter IV of 2015 (Q4/2015). International organizations, including World Bank (WB), International Monetary Fund (IMF), and Asia Development Bank (ADB) have continuously lowered the global economic forecast.[1] Political instability and warfare in Middle East, and influence-targeted competition between large economies has brought about complicated implications and difficult projections.

Table 1: Economic outlook in some major economies

Unit: %

	2015	*2016*	*2017*	*Difference**	
				2016	*2017*
Global GDP (growth rate: %)	3.1	3.4	3.6	- 0.2	- 0.2
Developed countries	1.9	2.1	2.1	- 0.1	- 0.1
USA	*2.5*	*2.6*	*2.6*	*-0.2*	*- 0.2*
Japan	*0.6*	*1.0*	*0.3*	*0.0*	*-0.1*
Euro	*1.5*	*1.7*	*1.7*	*0.1*	*0.0*
Developing and emerging countries	4.0	4.3	4.7	- 0.2	- 0.2
Asia developing countries	6.6	6.3	6.2	- 0.1	-0.1
China	*6.9*	*6.3*	*6.0*	*-0.1*	*-0.1*
ASEAN-5	*4.7*	*4.8*	*5.1*	*-0.1*	*-0.2*
World trade (growth rate: %)	2.6	3.4	4.1	-0.7	-0.5
Non-fuel price (% increase, USD)	-17.4	-9.5	0.4	-4.4	0.1

Source: International Monetary Fund (IMF, January 2016).

Note: * Difference between the forecast as of January 2016 compared to October 2015.

ASEAN-5 includes Indonesia, Malaysia, Philippines, Vietnam and Thailand.

2. China's economy continued to weaken in Q4 in particular and in 2015 in general. Economic growth for 2015 was estimated at 6.9%, the lowest rate for the past decade. Export growth decelerated, leading to weaker balance of trade. Production surplus and unmatched domestic demand have undermined investors' confidence.[2] The year 2015 also witnessed the massive withdrawal of capital away from Chinese market.[3] This requires the People's Bank of

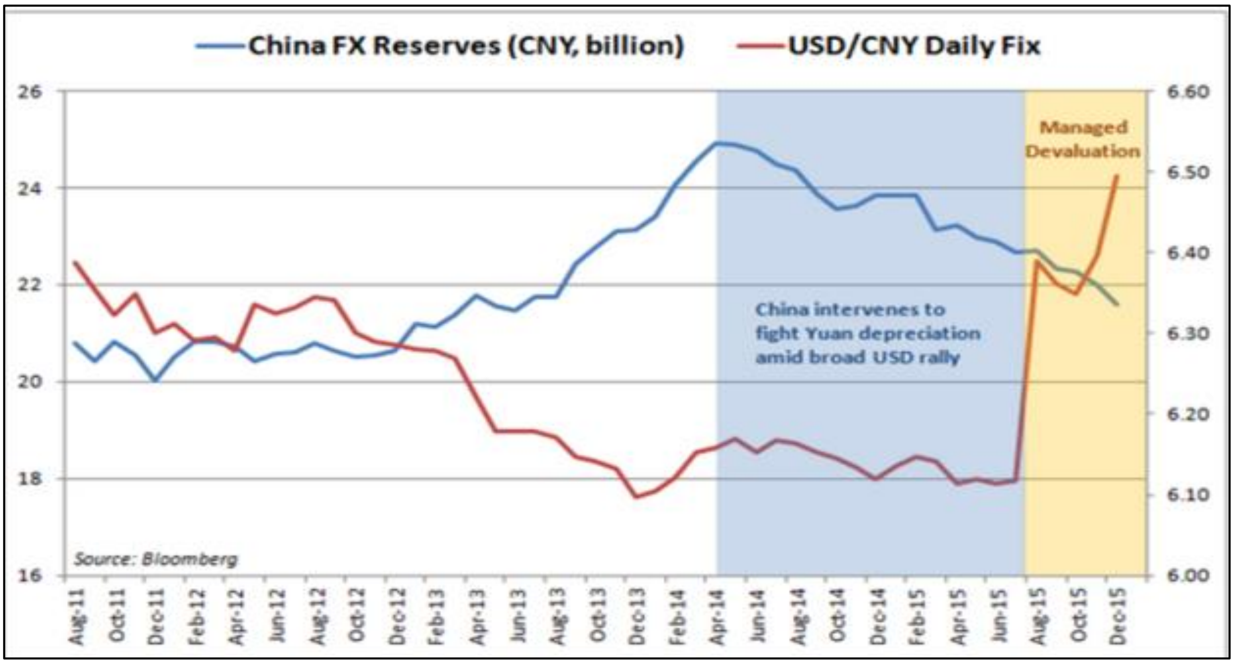
[1] IMF lowered the global economic forecast to 3.1% for 2015 (as compared to July 2015); WB's projection of global economic growth fell from 2.9% to 2.5%. These are the lowest forecasts since the global finanical crisis in 2008-2009. For further references, see various quarterly reports by CIEM.

[2] In November 2015, China's PMI was below 50, exports dropped by 6.8%, foreign reserves decreased by USD 87 billion, and CPI continuously decreased in Q4/2014.

[3] According to Bloomberg's statistics, capital outflows from China amounted to USD 1 trillion from

China to sell foreign reserves,[4] in line with bold measures to adjust the exchange rate regime.[5]

Figure 1: Foreign reserves in China, 2011-2015



Source: Bloomberg.

3. Economic growth in the US continued to recover. GDP growth in Q3/2015 was revised to higher level than initial estimate,[6] largely attributed to more vivid housing construction and business investment. Confidence of both investors and consumers has been strengthened. Consumption increased by 3%, unemployment rate was stable at 5%, domestic consumption went up by 3.2%, sales expanded by 3%, and consumer confidence index maintained at over 90. The Federal Reserves raised interest for the first time after nearly a decade, and left open the opportunity of further rate hikes in 2016.

4. Japan's economy exhibited more positive changes in Q4/2015. GDP growth exceeded 1% in Q3/2015, unemployment rate decreased to 3.1% in October, and PMI was increasing (to 52.4 in October and 52.6 November). However, Japan still encounters material challenges in sustaining these changes. Bank of Japan (BOJ) had to keep both interest rate and the volume of purchase under quantitative easing program unchanged.

5. European economies remained sluggish. GDP of the Eurozone went up only by 0.3% in Q3/2015, slower than in Q2/2015 (0.4%) and being the trough since

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mid-2014 to the end of 2015; the figure for 2015 alone reached about USD 676 billion.

[4] Foreign reserves sold out in Q3/2015 and Q4/2015 was USD 196.1 billion and USD 164.4 billion respectively.

[5] In December 2015, China's foreign reserves dropped sharply by USD 108 trilliion to USD 3.33 trillion.

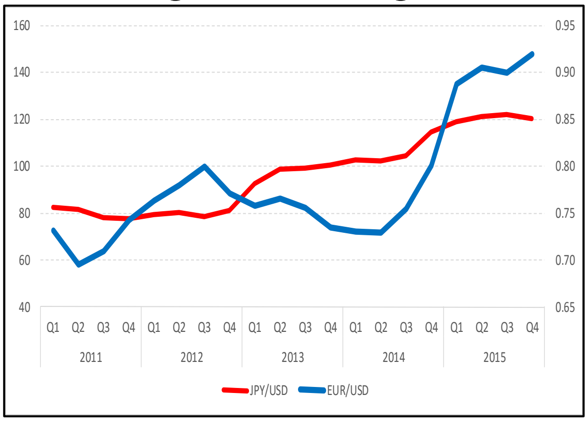
[6] On 24 November 2015, the US Department of Commerce announced that adjusted GDP of Q3/2015 increased by 2.1% (YoY).

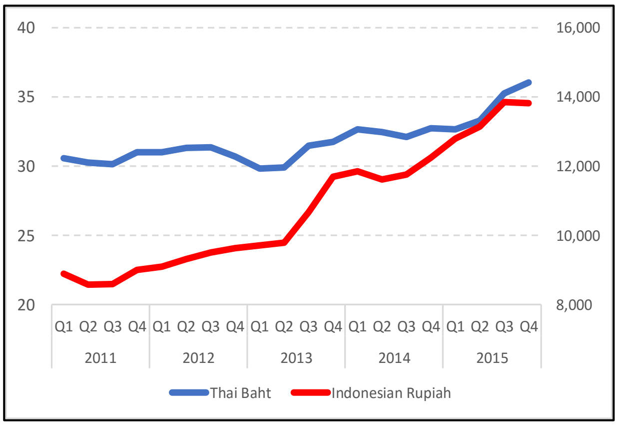
early 2015. Given the insignificant recovery and the depreciation of euro,[7] the European Central Bank (ECB) decided to maintain to basic rate and to decrease deposit rate to -0.3%. Simultaneously, ECB extended the quantitative easing program to facilitate investment and related efforts in inducing economic recovery.

6. Emerging economies were under stress due to smaller inflows of foreign capital. In 2015, capital outflows amounted at USD 735 billion from emerging economies.[8] In addition to China, Brazil and South Africa were largely affected. Capital withdrawn from emerging economies was re-channeled into advanced markets, especially the United States with safer assets. This trend caused the USD to appreciate, and triggered further capital outflows from emerging markets and altered international commodity prices.

7. USD appreciated significantly against other major currencies in Q4/2015. USD index increased by more than 2.5% in the quarter. Other major currencies such as Euro, Japanese Yen continued to depreciate against the USD. The appreciation of USD also affected other Asia currencies such as Thai Baht, Indonesian Rupiah (Figure 2). However, the pace of USD appreciation appeared to decelerate in Q4/2015 compared to previous quarters, particularly since mid-2014.

Figure 2: Exchange rates of major currencies to USD, 2011-2015





Source: International Financial Statistics (IFS).

8. International commodity prices decreased further in Q4/2015. In October 2015, energy prices fell by 43.8%; agricultural prices by 11.3%; food prices by 12.9%; raw materials by 5.7%; and metal by 24.7%[9]. In 2015, price of industrial inputs dropped by 4.1%, fuel by 46.4% and non-fuel basic inputs by 16.9% (Figure 3 and Figure 4). The sharp decrease of commodity price was attributed to: (i) more abundant supply; (ii) appreciation of USD; and (iii) fall in production costs (low price of fuel, reduction of import tarriff under FTA; etc.).

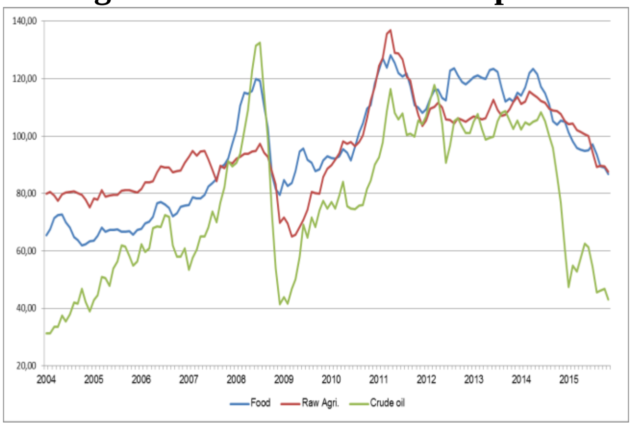
[7] Euro maintained at the lowest rate to USD since 2003.
[8] Source: Report of the Institute of International Finance (IIF), January 2016.
[9] World Bank Commodity Price Data (November 2015).

9. The year 2015 witnessed major progresses in trade and investment liberalization. A myriad of mega Free Trade Agreements (FTA) have concluded or acquired key breakthrough. Notably, negotiation of the Trans Pacific Partnership (TPP) was concluded in early October 2015. ASEAN Economic Community (AEC) was officially established on 31 December 2015, together with the approval of AEC Blueprint by 2025. The United States and EU have achieved progress in negotiating the Trans-Atlantic Trade and Investment Partnership (TTIP) in terms of tariff reduction, services and government procurement.

Figure 3: International gold price

Source: Goldprice.org

Figure 4: Crude oil and food price



Source: IFS.

2. Vietnam's economy: Reform requirements following economic restructuring in 2012-2015

10. Vietnam's economic restructuring has gained significant early outcomes in 2012-2015, in spite of ample space for further improvement. Results can be seen in the three focal areas of restructuring, including: public investment, state-owned enterprises (SOE) and commercial banks.

11. Restructuring of public investment focused on 4 main aspects: (i) Enforcing stricter discipline of public investment; (ii) Legal framework over public investment activities; (iii) Expanding Public Private Partnership; and (iv) Improving efficiency of public investment.

12. Investment efficiency, measured by ICOR, has been improved. According to calculation from GSO statistics, ICOR was 5.9 in 2012, 5.6 in 2013 and 5.18 in 2014. The proportion of investment from state budget was decreased, whilst public investment relied more on resources from borrowings. [10]

13. However, settling outstanding debts in capital construction was hardly sustainable. Violations of regulations over public investment remained popular. Notwithstanding strict public investment discipline in legal documents, it was loosely complied with in practice. The allocation of public investment rested more heavily on political decision rather than project efficiency. The biggest

[10] The share of loans was averaged at 23.2% in 1995-2009, then increased to 36.6% in 2010 and attained an average of 37% during 2011-2014[10].

loopholes in public investment included the mechanism of agencies in charge and public services managed by state sector.

14. In terms of restructuring commercial banks, the Proposal on Restructuring Credit Institutions in 2011-2015 aimed at: (i) enhancing sound operations and capacity of credit institutions; (ii) improving the prudent management and efficiency of credit institutions; and (iii) strengthening disciplines, and market principles in banking activities.
15. The State Bank of Vietnam (SBV) has implemented decisive-but-prudent policies in settling non-performing loans and enhancing sound operations of banking system. Consequently, the non-performing loans of banking system decreased gradually to below 3%. While the statutory Capital Adequacy Ratio (CAR) is set at over 9, CAR of the whole banking system since early 2012 has constantly exceeded 13 (even nearly 15 in 2012).
16. The outcomes of restructuring commercial banks have been remarkable. The banking sector has contributed significantly to macroeconomic stabilization. Key indicators of changes - including smaller inflation, stabilized monetary growth, lower interest rates, and higher foreign reserves – showcased the fundamental improvement due to prudential steps in restructuring commercial banks.
17. With regards to restructuring SOEs, priorities were given to: divestment of non-core activities, enhancing the equitization process, transparency of SOE management activities, standardization of types of SOEs and reforms of corporate governance. The divestment of 5 sensitive sectors, including real estate, securities, banking and finance, insurance and investment fund have achieved initial results.[11].
18. During 2014 and the first eight months of 2015, a total of 234 SOEs (out of 432 SOEs) were equitized, amounting to 54% of the planned figure. After 4 years of implementing the Proposal on Restructuring SOEs, the operational efficiency and competitiveness of SOEs were improved[12]. It can be seen that equitization of SOEs has been re-launched firmly. To some extent, the outcomes so far should receive appreciation, albeit lagging behind original plan.
19. The economic restructuring in association with shifting growth paradigm took place in the period of severe macroeconomic instability. In this context, the

[11] In 2012, divested amount was VND 348 billion with proceedings of VND 356 billion; in 2013, corresponding figures were VND 874 billion and VND 745 billion; in 2014: VND 4,184 billion and VND 4,292 billion. In the first two quarters of 2015: divested amount reached VND 7,522 billion, with proceedings of VND 11,161 billion (or 1.48 times of book value).

[12] Equity increased, returns on capital and revenues attained 10 - 15%, contribution to State Budget went up by 27% per annum, accounting to about 30% of State Budget and 32% of GDP. Over 80% of SOEs earned positive profitable and another 11.7% of SOEs incurred loss. YoY growth of equity reached 26% in 2012, 4.1% in 2013; returns on equity was 16.37% (of which respective ROEs of business groups and general corporations were 16.94% and 15.4%). Liabilities/Equity ratio was 1.52 times (respective figures for corporations being 1.46 times, and 1.58 times), which was under the permitted ceiling (3 times).

outcomes achieved so far are hard-earned. Macroeconomic stability continued to be enhanced. The national soundness was strengthened, while the business environment improvement has gained momentum. Market responses to reforms were positive. Economic growth recovery became more robust. Investment efficiency, labour productivity, total factor productivity was much improved. Public investment, and activities of SOEs and commercial banks were more transparent and subject to enhanced supervision. Nonetheless, the efficiency of resource utilization, labour productivity was still modest; the pace of equitization was slow, with low quality. To some extent, the operation mechanism of SOEs in general and the governance of SOEs in particular fail to match with market economy principles.

20. Restructuring programs and proposals of local governments were not closely tailored to respective strengths and competitiveness, whilst overlooking the re-organization of supply chains of competitive products, the alignment between production and sales, and linkages between domestic enterprises and foreign-invested ones to upgrade industrial development and domestic value-added.

21. During 2016-2020, Vietnam still emphasizes on maintaining macroeconomic stability in all four pillars, namely: monetary stability, fiscal stability, market stability and policy stability.

22. The period of 2016-2020 also sees a clear mandate to strengthen awareness and concretize the basic concepts for follow-up reforms, in which the definition of socialist-oriented market economy was a focus.

23. The US and the EU adopted some criteria of a market economy, including (i) The extent to which government intervenes into allocation of resource and in enterprises' decision, either directly or indirectly; (ii) Market distortions due to state's intervention; (iii) Existence of laws and regulations to ensure effective and non-discriminatory corporate governance; (iv) Protection of property rights and market exit right; and (v) Sound financial system, with proper supervision and independent operations.

24. The assessment outcomes, based on aforementioned criteria, are tabulated in Appendix 2. During recent years, Vietnam has implemented drastic economic reforms to improve friendliness to markets and better adaptation to full market economy principles. Still, there remains material intervention of the State on production factor markets, and goods market through the operation of SOEs. Audit and accounting system has not yet followed international standards, therefore it can not create a sound, competitive, and predictable market. The judicial system was still short of independence and effectiveness in enable market disciplines. Business confidence in the legal framework for protecting their legitimate rights and interest is still low.

25. Notwithstanding improvements in the legal framework for bankruptcy and ordered market exit since 2014, it remained defective and failed to create breakthrough in enforcing market exit. Particularly, vast difference persists in applying the bankruptcy principles between SOEs and other enterprises.

Intellectual property rights were well-protected under law, but actual enforcement was weak due to shortage of trained and experienced staff.

26. To ensure fully functioning market, an independent competition authority, with adequate institutional and technical capacity for receiving, investigating cases of anti-dumping, fixing prices and prevention from market entry, etc. becomes mandatory. However, Vietnam Competition Authority and Competition Council appeared to underperform this role in recent years.

27. Economic restructuring and shift of growth paradigm remain an important need, as reflected in the below aspects.

    a. *Restructuring public investment:* To allocate public investment under medium-term investment framework. To improve the supervision and appraisal investment via specialized advisory councils for supervising and appraising agencies. To expand the supervision and appraisal function based on investment efficiency rather than on compliance with investment process. To settle outstanding construction debts more effectively; to strengthen disciplines in the implementation of directives, decisions, decrees and other regulations on public investment and State Budget law.

    b. *Restructuring credit institutions:* To quickly settle the off-balance sheet NPLs so as to pull lending rate down to average rate of developing countries (of about 5% per annum). To promptly universalize the adoption of principles of banking governance under Basel II. To develop exchanges for financial derivatives. To increase the transparency and publicity of SBV in ensuring adequate information dissemination for market participants as well as soundness of financial system.

    c. *Promoting regional linkage:* Regional linkages and industrial clusters are essential to improve business competitiveness in the era of globalization. To improve the approach to strengthen regional linkage, centering on enterprises with the support of State policies. Linkage should come from enterprises themselves; the State only helps minimize risks and costs in establishing regional linkage and industrial clusters.

    d. *SOE reforms:* To accelerate reforms of institutions, governance of SOEs, and State management so that SOEs are fully compliant with market principles and competitive neutrality. To discipline hard budget constraint over SOEs. Equitization process should invite the participation of private sector and foreign investors, so as to avoid cross-ownership among SOEs.

    e. Significant efforts should be made to upgrade quality of human resource and infrastructure - two bottlenecks to Vietnam's economic growth.

II. MACROECONOMIC PERFORMANCE AND OUTLOOK

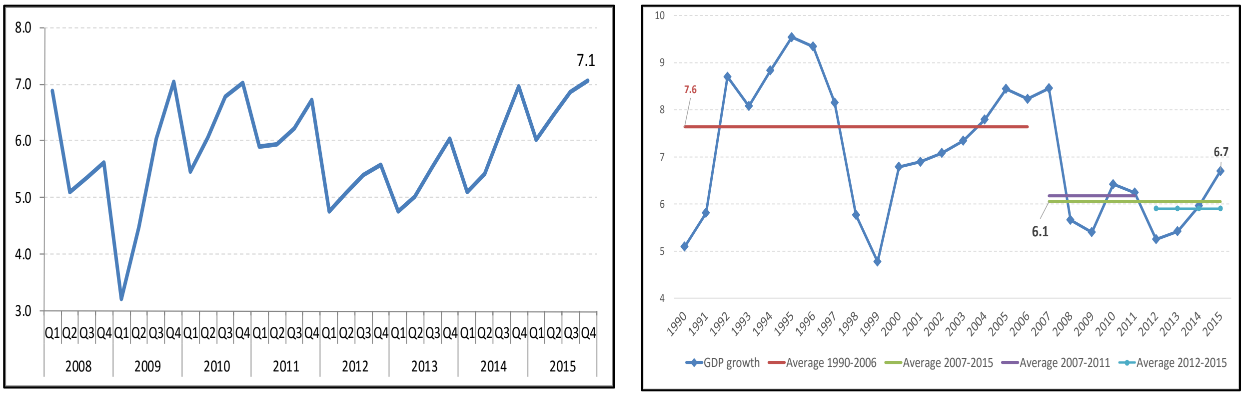
1. Macroeconomic performance in Q4 and 2015

1.1. Real economy

28. Economic growth continues to recover. GDP attained 7.06% in Q4/2015, higher than corresponding quarters of 2011-2014. In 2015, GDP grew by 6.68%, significantly higher than target (6.2%). This figure exceeds the average growth for 2011-2015 (5.91%/year) and for 2007-2015 (6.05%/year). Still, economic growth in 2015 is below the pace in 1990-2006 (averaging 7.6%/year).

Figure 5: GDP growth rate

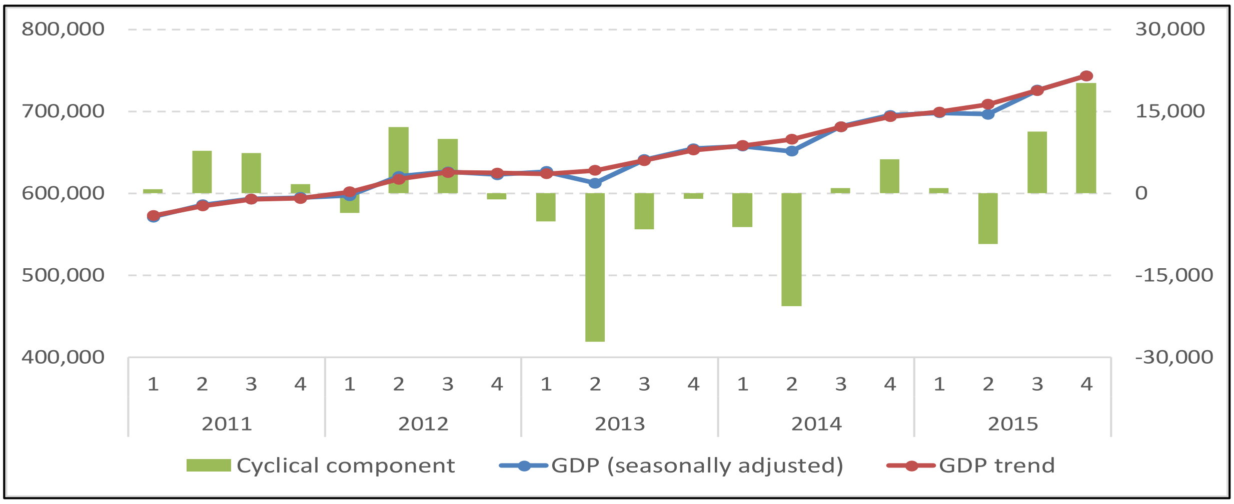
Unit: %



Source: General Statistics Office (GSO).

29. Despite more rapid growth, Vietnam's GDP could barely return to long-term trend (Figure 6). GDP growth is yet to significantly exceed the long-term trend during 2013-2015. From cyclical pattern in 2011-2015, any excess of GDP over long-term trend lack sustainability. As an implication, Vietnam's economy was still short of strong momentum for growth.

Figure 6: Quarterly GDP compared to trend and cycle



Source: Authors' calculation.

Note: The Cyclical component is measured on the right axis (billion VND); other components are reflected on the left axis (billion VND).

30. Consumption and investment were major contributions to the expanded aggregate demand in Q4 and 2015. Final consumption increased by 9.12% (YoY), contributing 10.7 percentage points to overall growth. Gross capital formation grew by 9.04%, contributing 4.6 percentage points. Growth of final consumption and gross capital formation induced an increase in imports; while net imports of goods and services caused overall GDP growth to decrease by 8.6 percentage points. This GDP structure by final expenditure was quite similar to the period of 2006-2009 (Table 2).

Table 2: Contribution of capital formation, final consumption and trade balance of goods and services to GDP growth

Unit: Percentage point

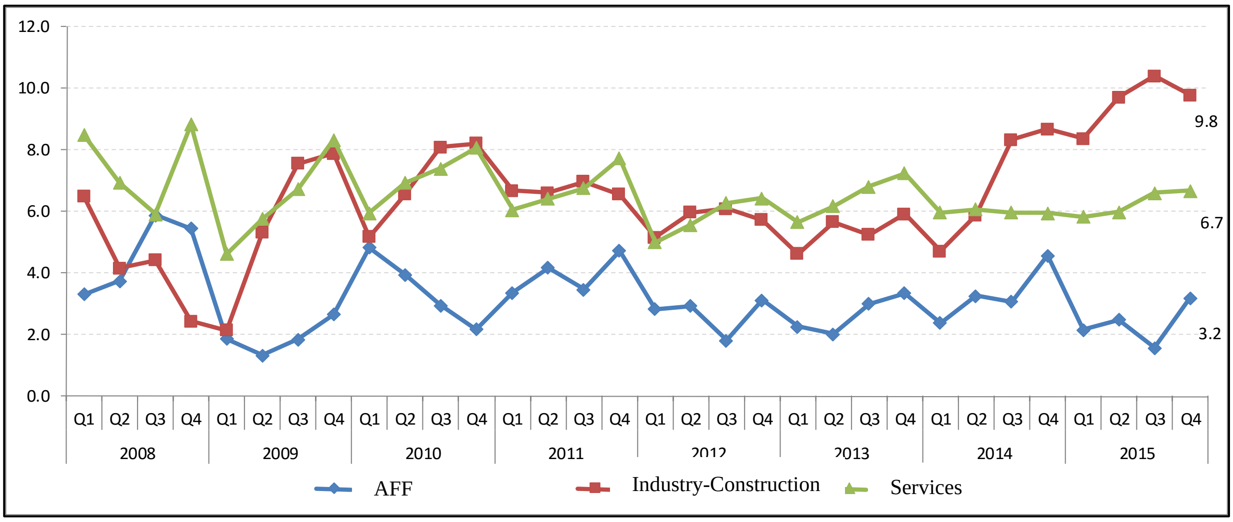
	2006	***2007***	***2008***	***2009***	***2010***	***2013***	***2014***	***2015***
Capital formation	3.31	7.83	2.17	1.50	3.58	1.62	2.9	4.64
Final consumption	5.25	6.80	5.49	1.94	6.06	3.72	4.72	10.66
Trade balance of goods and services	-0.44	-9.95	-2.32	2.10	-0.52	0.08	-1.64	-8.62

Source: GSO.

31. Industry and construction were the main driver of economic growth in Q4 and 2015. Value-added of this sector rose by 9.6% in 2015, much faster than those of agriculture-forestry and fishery, and service sector (Figure 7). The industry sector enjoyed a growth by 9.4%, of which manufacturing sector grew by 10.6%, higher than that of 2013-2014[13]. Value-added of mining and quarrying sector rose by 6.5%. The construction sector experienced YoY growth in value-added of 10.8%, the highest level since 2010.[14]

Figure 7: GDP growth by sector

Unit: %

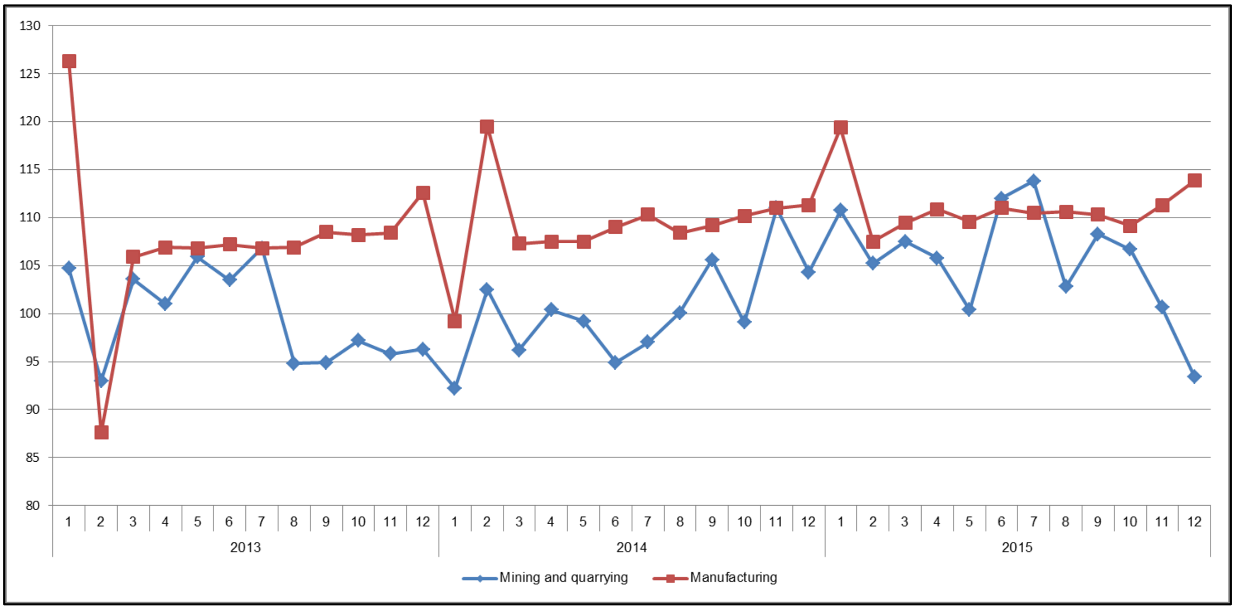


Source: GSO.

[13] Growth figures of manufacturing industry were 7.22% and 7.41% in 2013 and 2014, respectively.
[14] The YoY figures of changes of construction sector: down by 0.26% in 2011, up by 3.66% in 2012; up by 5.84% in 2013; and up by 6.93% in 2014.

32. The Index of Industrial Production (IIP) rose by 9.8% in 2015[15], much higher than the growth of previous years. In December alone, IIP already grew by 9% on YoY basis. Improvement took place in all the 4 sub-sectors in 2015, including: (i) production and distribution of electricity; (ii) manufacturing; (iii) mining and quarrying; and (iv) water supply, waste management and treatment. However, Q4/2015 saw positive growth of manufacturing sub-sector, meanwhile the mining and quarrying sub-sector fell sharply (Figure 8).

Figure 8: Index of Industrial Production, 2013-2015



Source: GSO.

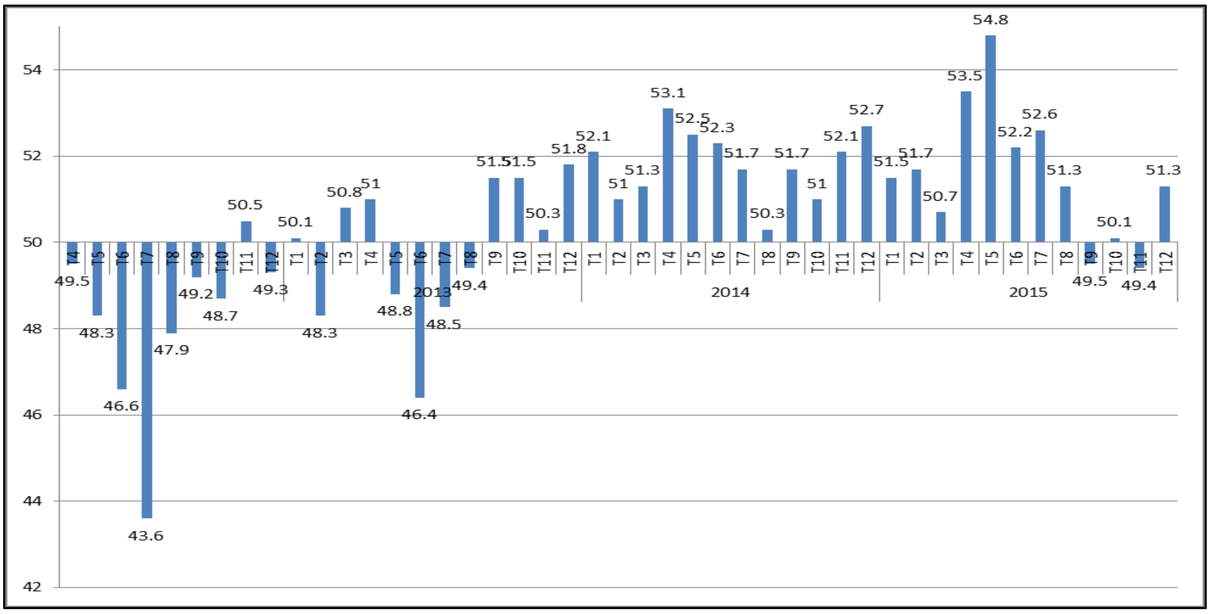
33. Accelerated growth of industrial production was attributed to some factors. *First*, investment and consumption demand was buoyant in the context of economic recovery and Vietnam's preparation ahead of important FTAs.[16] In particular, the more rapid disbursement of public investment and credit in Q4/2015 had significant impacts on industrial sector.[17] *Second*, the prices of materials and inputs went down.[18]

34. The growth of industrial sector was less than robust. PMI lacked stability in Q4/2015, attaining 50.1 in October, falling to 49.4 in November and then recovering to 51.3 in December (Figure 9). The main reasons for this pattern include: (i) the slow recovery of global economy, especially the more sluggish growth of China; (ii) lack of concrete policies for stimulating the industrial sector;[19] (iii) immaterial reduction of interest rates; and (iv) increase of labour-

[15] YoY growth was 9.3% in Q1; Q2: 10.2%; Q3: 9.3%; and Q4: 10%.
[16] Sale of manufacturing sub-sector at the end of 2015 increased by 10.2% (YoY), some industries experienced high increase of sale, including electric products, computers and optical products (49.4%); production of motor vehicles (26.6%); production of metal (22.9%).
[17] See more analysis of the sub-Sections on Monetary movement and Investment.
[18] For example, price of transportation fell by 8.74% in December (YoY) and by 11.92% in 2015; price index of imports dropped by 9.66% in Q4/2015 (YoY). It should be noted that the reduction of tariffs under some FTAs helped lower input costs for industrial production.
[19] For example, the Action Plan was issued for 6 industries in the Industrialization Strategy under Vietnam – Japan collaboration framework by 2020, vision to 2025; however, most of the identified

related costs (such as minimum wage, contribution to social insurance, etc.) in 2016.

Figure 9: Purchasing Manager Index, 2012-2015



Source: Markit, HSBC.

Note: PMI=50 means no month-on-month change.

35. Value-added of agriculture-forestry and fishery (AFF) exhibited YoY growth rates of 3.2% in Q4/2015 and 2.4% in 2015. Despite higher YoY growth rate in Q4/2015, AFF only saw insignificant improvement due to: (i) adverse impacts of weather change; (ii) increasing competition in sale/export of agricultural products, even imported agricultural products; (iii) fall of output prices;[20] and (iv) slow implementation and/or ineffectiveness of supporting policies.

36. The service sector grew by 6.7% in Q4/2015. This growth hardly resembled improvement over other quarters of 2015 as well as Q4s of previous years (Figure 7). For 2015 as a whole, growth of service sector attained 6.33%. Some sub-sectors experienced high growth, such as wholesale and retail trade, repairs of car, motorbike and other motor vehicles (increasing by 9.1%), information and communication (by 8.5%). Meanwhile, tourism still faced difficulties due to: (i) competition from other countries in the region; (ii) reduction of tourists from some key markets due to economic crisis;[21] and (iii) slow improvement of domestic tourism quality and transportation[22].

37. The attractiveness of Vietnam's retail market significantly deteriorated. According to A.T. Kearney (2015), Vietnam no longer showed up in the top 30

measures were yet to be implemented.

[20] Producer price index of agriculture, forestry and fishery went down by 2.43% as compared to 2014.

[21] For example, the number of tourists from Russia fell by 7.1% compared to 2014.

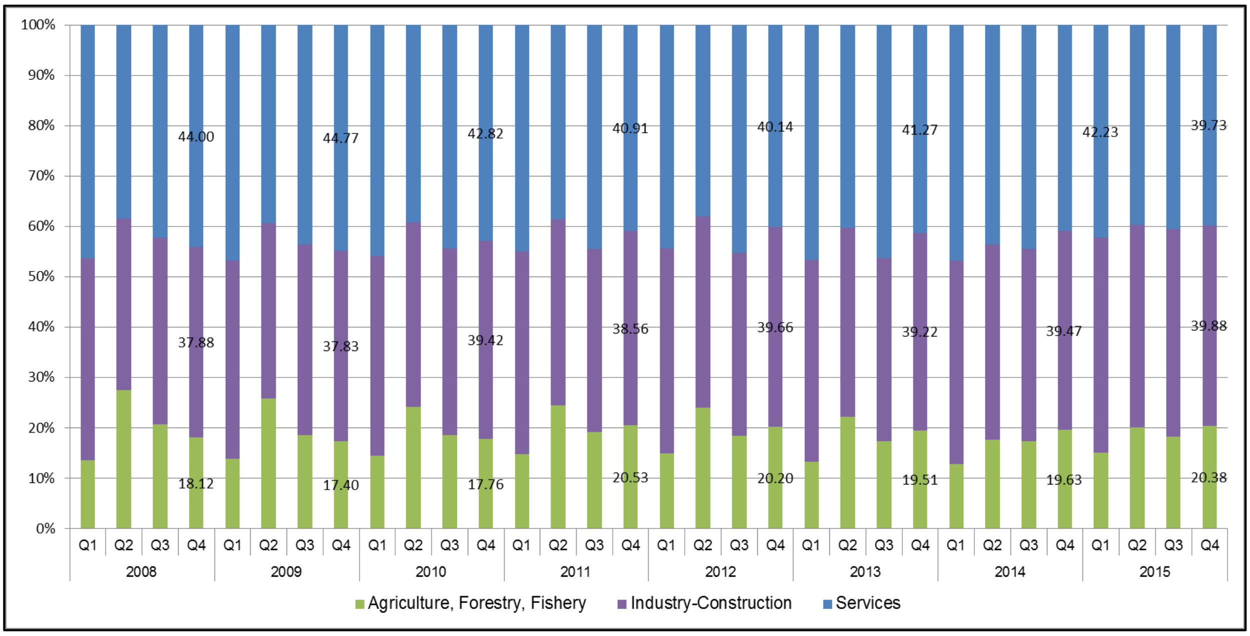
[22] In terms of tourism competitiveness, Vietnam was ranked 75th (out of the 141 countries and territories) by World Economic Forum (WEF, 2015), and remained low in terms of transportation and tourism policies (112th), environmental sustainability (132th).

potential markets for retailing. It should be noted that Vietnam's rank dropped from 4th in 2007 to 14th in 2010 and 28th in 2014.

38. Economic structure by sector had almost no change in Q4/2015. Due to improved growth, industry-construction sector experienced a slight increase in share to 39.9% in Q4/2015 from 39.5% in Q4/2014. The share of agriculture-forestry and fishery rose from 19.6% in Q4/2014 to 20.4% in Q4/2015. Service sector accounted for 39.7% in Q4/2015, decreasing from the level of 42.2% in Q4/2014 (Figure 10).[23]

Figure 10: Quarterly GDP structure, 2008-2015

Unit: %



Source: GSO.

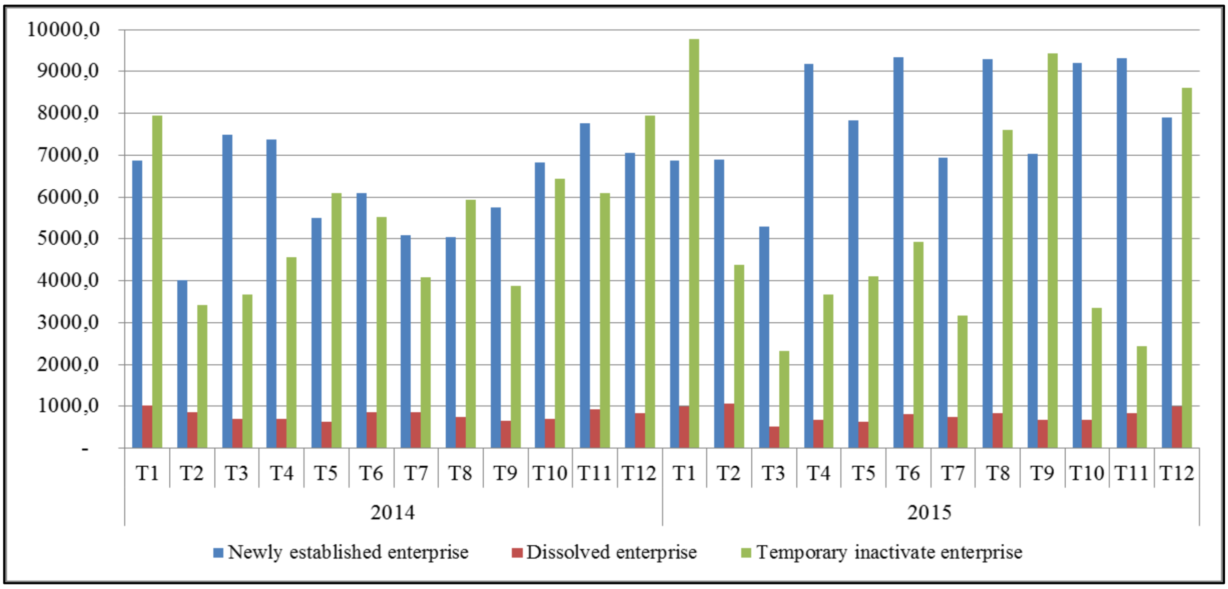
39. 26,407 enterprises were newly registered in Q4/2015, up by 22% (YoY), with total registered capital of VND 180.5 trillion. In Q4, the number of dissolved enterprises was 2,505, up by 1.25% (YoY); the number of inactive enterprises (including those registering inactive status or stopping temporarily before closing tax code or without registration) fell sharply by 29.6% (YoY).

40. In 2015, there were 94,754 newly registered enterprises, with total registered capital of VND 601.5 trillion, up by 26.6% in terms of number of enterprises and up by 39.1% in terms of registered capital (YoY). Meanwhile, the additional registered capital contributed a total of VND 851 trillion to total supplementary registered capital to the economy. Estimated number of jobs in newly registered enterprises was 1,471.9 thousand in 2015, increasing by 34.9% (YoY, Figure 11).

41. In 2015, a number of 21,506 enterprises came back to business, up by 39.5% (YoY). This growth was significantly higher than in previous years, showing initial improvement of business confidence.

[23] In this analysis, the shares of sectors do not take into account the distribution of products taxes less subsidies on production.

Figure 11: Selected indicators of enterprises' performance, January 2014-December 2015



Source: Busisness Registration Agency, MPI.

42. The manufacturing enterprises had positive assessment of production and business tendency in late 2015.[24] 42.3% of enterprises expected improved production and business in Q4/2015 than in Q3/2015; 19.5% of enterprises still faced difficulties and 38.2% of enterprises thought that production and business would be stable. In terms of business tendency in Q1/2016, 40.9% of enterprises believed in improved business prospects; 17.7% of enterprises expected more difficulties and 41.4% of enterprises thought that production and business has been stable. Detailed assessment of manufacturing enterprises - on the volume of production output and order, export orders, cost of production, sale prices, inventories and employment – indicated somewhat optimism of the businesses (Figure 12 and Figure 13).

Figure 12: Business tendency (Q4/2015 as compared to Q3/2015)

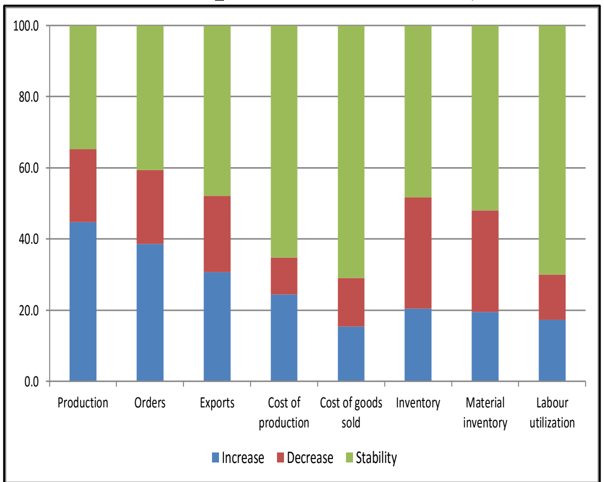
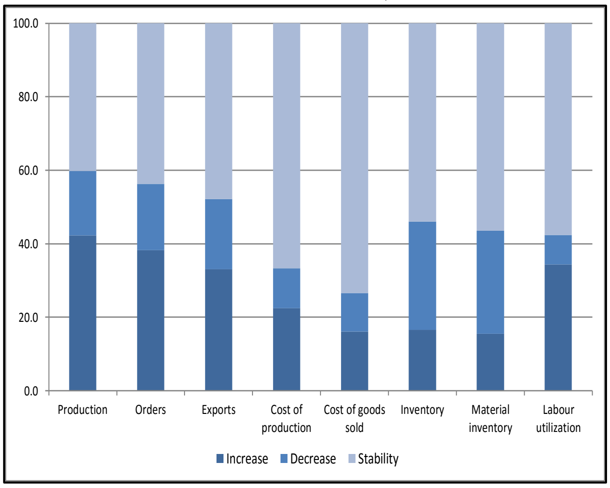


Figure 13: Business tendency (forecast for Q1/2016)



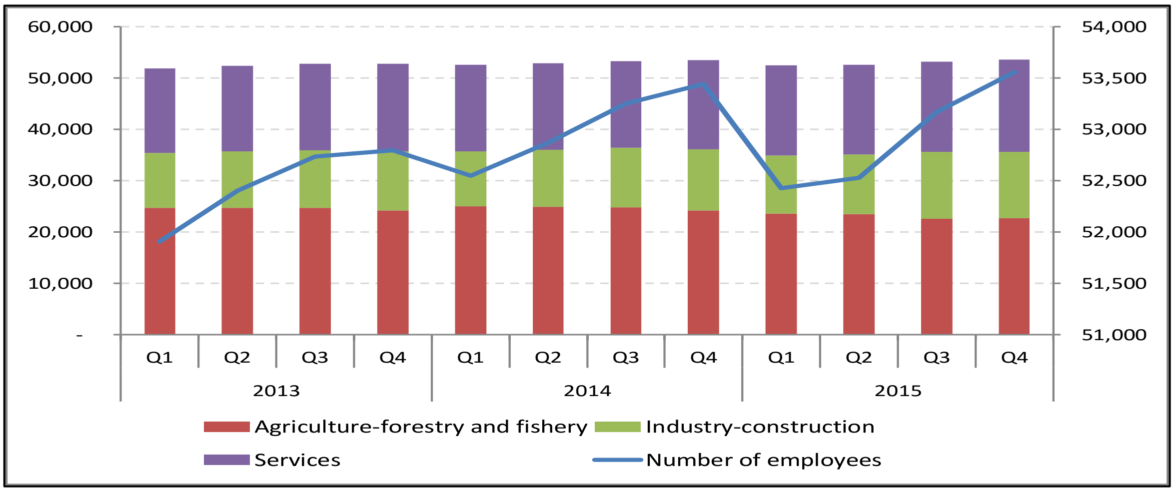
Source: Busisness Registration Agency, MPI.

[24] Results from the business tendency survey by GSO.

43. As of 1 January 2016, total labour force of the country was 54.61 million people, increasing by 185 thousand people (YoY). Male labour accounted for 51.7%; female labour accounted for 48.3%. In 2015, total economically active labour force had 52.9 million people, up by 142 thousand people compared to 2014. The number of employees at the end of each quarter exhibited a positive YoY growth. The share of labour in agriculture-forestry and fishery sector was 44.3%; and industry-construction sector accounted for 22.9%[25] (Figure 14).

Figure 14: Economically active labour force by economic sector, Q1/2013-Q4/2015

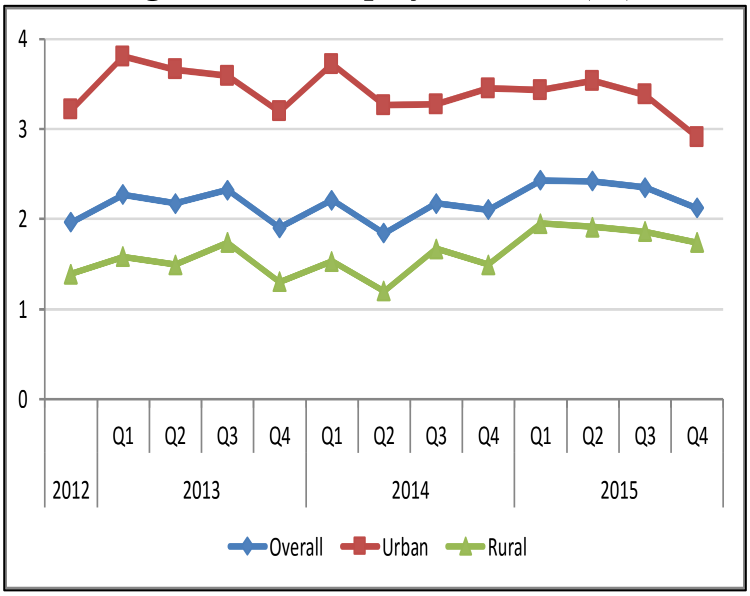
Unit: thousand people



Source: GSO.

44. The working-age unemployment rate was 2.31% in 2015, higher than that of 2013-2014[26], of which the urban unemployment rate was 3.29% and that of rural areas was 1.83%. The recovery of industry-construction was one of major reasons for reducing the urban unemployment rate. The working-age unemployment rate decreased over the quarters[27], largely in the urban area[28] (Figure 15).

Figure 15: Unemployment rate (%)

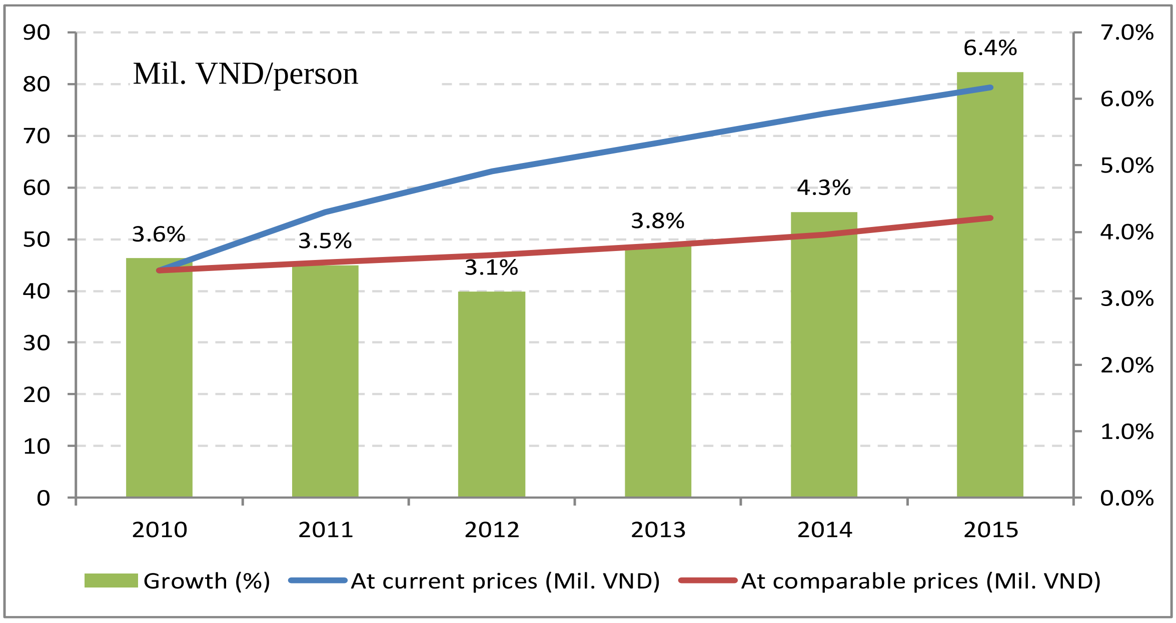


Source: TCTK.

[25] In 2014 it was 46.3%; 21.5% and 32.8% respectively.
[26] Unemployment rate in 2013 and 2014 was 2.13% and 2.1% respectively.
[27] The working-age unemployment rate of Q1 was 2.43%; Q2: 2.42%; Q3: 3.35% and Q4: 2.12%.
[28] Figure for Q1 was 3.43%; Q2: 3.53%; Q3: 3.38%; and Q4: 2.91%.

45. Labour productivity (at current price) attained VND 79.3 million per labour in 2015, rising by 6.4% compared to 2014.[29] On average, labour productivity increased by 3.9% per annum during 2006-2015.[30] However, labour productivity only rose by 23.6% during 2011-2015, lower than the target (up by 29%-32%).[31]

Figure 16: Labour productivity



Source: GSO.

46. Vietnam's labour productivity currently lags far behind other regional countries and remains uneven among industries and sectors. The main reasons include: (i) Slow concretization of economic restructuring by sector (even in agricultural sector); (ii) Existence of "bottlenecks" and "barriers" which prevent labour mobility towards higher productivity industries; (iii) Outdated equipment, machines and technologies, resulting in low labour-augmenting effect; and (iv) Poor management with low efficiency of resource utilization.

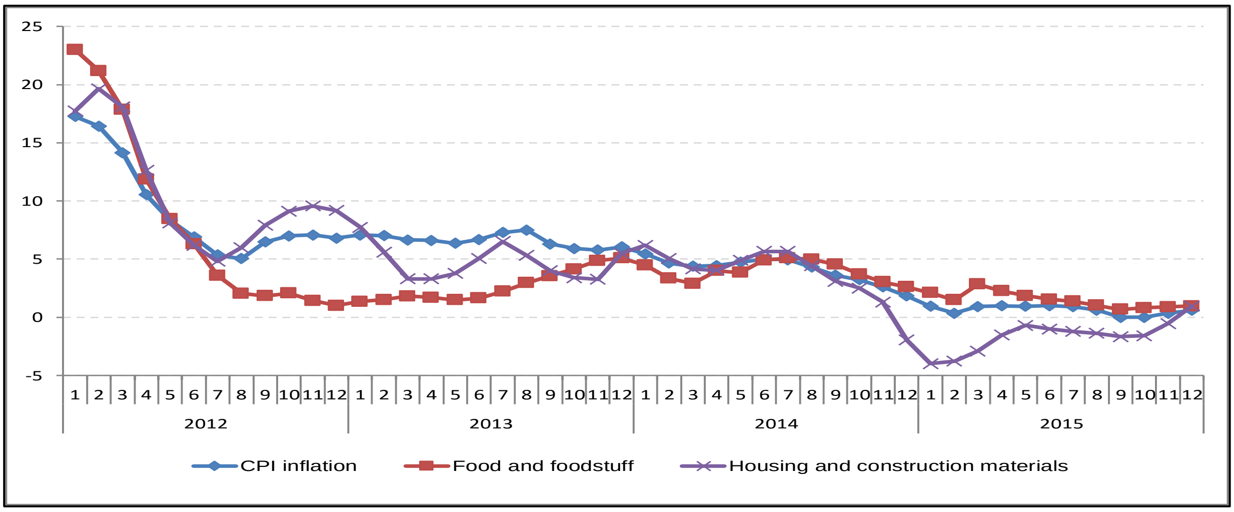
1.2. Inflation

47. Despite two consecutive drops in August and September, the consumer price index (CPI) regained its increase trend in late 2015. CPI went up by 0.11%, 0.07% and 0.02% in October, November and December, respectively (MoM). Overall, CPI was up by 0.2% in Q4 and 0.4% in the first 9 months of 2015. YoY growth of CPI was relatively stable in Q4/2015 (**Error! Reference source not found.**). In 2015, CPI increased by 0.6% and core inflation was 2.05%.

[29] At current prices.
[30] Corresponding growth for 2006-2010 was 3.4%; 2011-2015: 4.2%.
[31] Measured at PPP prices for 2005, labour productivity of Vietnam (in 2014) was equal to only 1/18 of Singapore, 1/6 of Malaysia, 1/3 of Thailand and China, and ½ of Philippines and Indonesia.

Figure 17: YoY inflation, 2012-2015

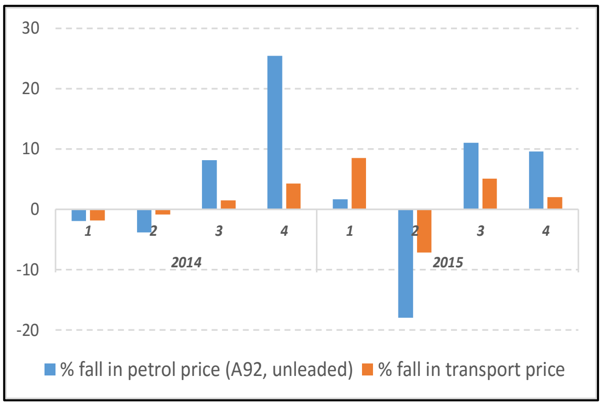
Unit: %

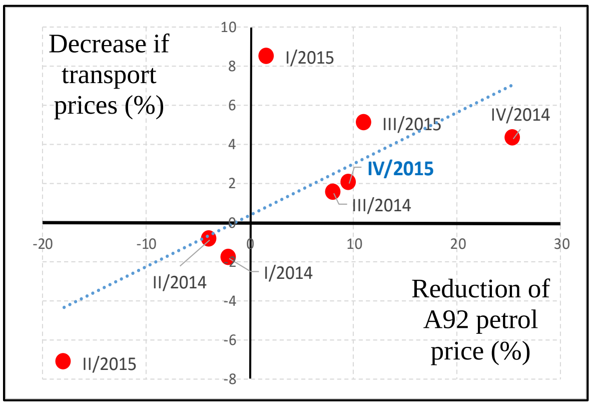


Source: GSO, YoY growth rate.

48. Price decrease in Q4/2015 was mainly related to transport services. Transport price index decreased by nearly 2% in Q4 (compared to Q3), of which respective MoM decreases were 0.05%, 0.38% and 1.53% in October, November and December. This pattern was attributed to continuously adjusted price of petrol in Q4/2015[32], which registered the accumulated decrease of 9.54%[33]. However, the reduction of transport price in Q4/2015 was more modest compared to Q3/2015 and Q4/2014. Besides, the relationship between reduction of petrol price and decreases of transport prices in Q4/2015 exhibited few structural change compared to those since the beginning of 2014 (Figure 18).

Figure 18: Movement of A92 petrol price and transport prices





Source: Authors' compilation.

49. Price indices of almost all other commodities increased in Q4/2015. Food price went up by around 0.06% (compared to the end of Q3/2015), while that of foodstuff rose by 0.46%. For housing and construction materials, price index

[32] In Q4/2015, petrol price was adjusted upward on 3 October, then was adjusted downward on 19 October, 3 and 18 November, 3 and 18 December.
[33] The price of RON A92 petrol in Zone 1 was taken for reference.

was up by 0.8%, mainly attributed to: (i) considerable surge in demand towards the end of 2015; (ii) more supply of housing products; and (iii) disbursement of the preferential credit package of VND 30 trillion.[34]

50. Relatively low inflation in Q4/2015 was attributed to several factors, including: (i) continuous falls in various commodity prices in the world market; (ii) easing of inflationary expectation; (iii) prudential management of total liquidity while the fiscal dominance appeared to be relaxed; and (iv) the VND/USD exchange rate remained stable until late 2015[35].

51. Inflation risks prevail, and related consequences may become more obvious in 2016. Factors that may be attributed to inflation risks in the medium and long-run include: (i) accumulated pressure of budget deficit and public debt, leading to dominance over the conduct of monetary policy; (ii) sharp drop of foreign reserves in the presence of widening trade deficit; (iii) possibility of price increases for some goods and services since the beginning of 2016 (health, electricity, etc.) in the absence of adequate and transparent justification;[36] and (iv) higher production cost due to upward adjustment of minimum salaries,[37] and the change in method of calculating social insurance.

1.3. Monetary movement

52. VND-denominated deposit rate (for terms shorter than 6 months) was stable and below the ceiling rate imposed by the SBV (Table 3). Actual VND-denominated deposit rates in Q4/2015 were almost unchanged compared to Q1/2015 and Q3/2015 (for all terms). However, between mid-November and December 2015, deposit rates tended to hike, albeit below the ceiling rate. Hikes of deposit rates took place initially in joint-stock commercial banks, and then in state-owned commercial banks.

Table 3: VND-denominated deposit rates of commercial banks

Unit: % per year

	Demand deposit	**Term depsit (< 6 months)**	**Term deposit (6-12 months)**	**Term deposit (> 12 months)**
End of December 2014	0.8-1.0	5.0-5.5	5.7-6.8	6.8-7.5
End of March 2015	0.8-1.0	4.5-5.4	5.4-6.5	6.4-7.2
End of September 2015	0.8-1.0	4.5-5.4	5.4-6.5	6.4-7.2
End of December 2015	0.8-1.0	4.5-5.4	5.4-6.5	6.4-7.2

Source: SBV.

[34] By 31 December 2015, total committed amount was VND 26,999 billion (equivalent to 90%), and disbursed value was VND 17,711 billion. As of 30 September 2015, those figures attained VND 20,425 billion and VND 12,293 billion, respectively.

[35] This was an important change since August 2015, because exchange rate management focused largely on actual inflation against target before this milestone.

[36] As a result, prices increase more rapidly and/or easily, while being more rigid on the down side.

[37] The minimum salary by zones was raised on average by 12.4% according to Decree No. 122/2015/ND-CP dated 14 November 2015.

53. In mid-December 2015, the SBV lowered the ceiling on USD-denominated deposit rates of individuals. This attempt followed the downward adjustment of corresponding ceiling on organizations' deposit of USD in September 2015. The main objectives are: (i) to deepen efforts in the roadmap towards reducing dollarization; and (ii) to reduce USD hoarding in the context of increasing rumor about the adjustment of VND/USD exchange rate and/or change in VND/USD exchange rate regime.

54. USD-denominated lending rate remained stable in Q4/2015, and only slightly decreased at joint-stock commercial banks (Table 4). At state-owned commercial banks, the gap between USD-denominated lending and deposit rates was about 2.75-4.25 percentage points for terms of more than 1 year. The gap was higher at joint-stock commercial banks. USD-denominated lending rates hardly decreased due to: (i) grant of foreign-currency-denominated credits only to a few clienteles;[38] (ii) relatively high USD-denominated lending rates in Vietnam, leading to modest effects from interest rate hike in the U.S. – which was made in mid-December 2015; and (iii) attempts to hedge exchange rate fluctuations by commercial banks.

55. In Q4/2015, VND-denominated lending rates were almost unchanged. Modest falls of lending rates in Q4/2015 were attributed to: (i) less abundant liquidity in the context of increasing Government bond issuance; (ii) pressure from interest rate hike by FED[39]; and (iii) higher credit demand in late 2015.

Table 4: Popular lending rates of commercial banks, September-December 2015

Unit: % per year

	Types	Short-term	Medium and long-term
State-owned commercial banks	VND: - Ordinary business and production	6.8-8.8 *(6.8-8.8)*	9.3-10.5 *(9.3-10.5)*
	- Agriculture, rural development, export, SMEs, supporting industries, high-tech enterprises	6.0-7.0 *(6.0-7.0)*	9.0-10.0 *(9.0-10.0)*
	USD:	3.0-4.5 *(3.0-4.5)*	5.5-6.5 *(5.5-6.5)*
Joint-stock commercial banks	VND: - Ordinary business and production	7.8-9.0 *(7.8-9.0)*	10.0-11.0 *(10.0-11.0)*
	- Agriculture, rural development, export, SMEs, supporting industries, high-tech enterprises	7.0 *(7.0)*	10.0-10.5 *(10.0-10.5)*
	USD:	4.5-5.3 *(4.5-5.5)*	6.0-6.5 *(6.0-6.7)*

Source: SBV.

Note: Figures in the brackets are lending rate as of September 2015.

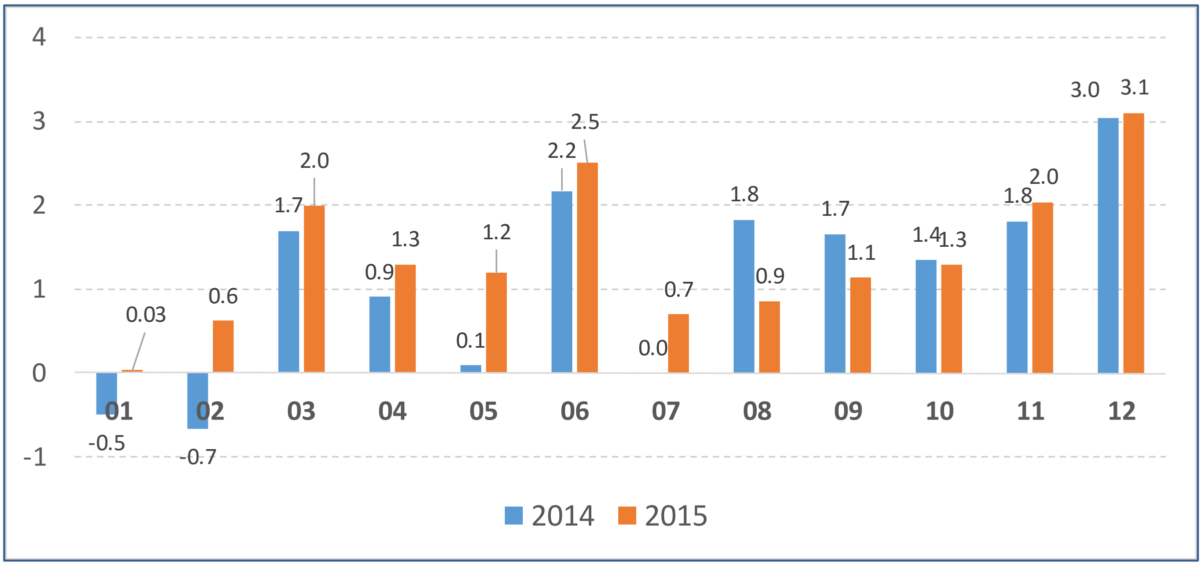
[38] See Macroeconomic Report – Q3/2015.

[39] "Impossible trinity": It is impossible to simultaneously implement pegged exchange rate, free capital flows and independent monetary policy (related to interest rate management) due to interest rate parity.

56. Outstanding credit increased by about 6.5% in Q4/2015 (compared to the end of Q3/2015). MoM credit growth in December 2015 was 3.1%. The development of credit growth in Q4/2015 was relatively similar to that in Q4/2014 (Figure 19). Credit expansion in Q4/2015 considerably outpaced that in previous quarters.[40] In 2015, credit growth was estimated to reach 18%, which hardly became a challenge to the SBV because the credit growth target had been raised to 17% (instead of 13-15% previously).

57. The rapid expansion of outstanding credit in Q4 was attributed to: (i) higher investment demand toward the end of the year and/or attempt to lock in investment opportunities in 2016; (ii) more active extension of credits by commercial banks after reducing NPL ratio to below 3%; (iii) advance borrowing to avoid the possibility of increasing VND-denominated interest rates in 2016; and (iv) accelerated disbursement of some preferential credit packages (such as the VND 30 trillion package for buying social houses, etc.).

Figure 19: MoM credit growth, 2014-2015



Source: Compilations from various sources.

58. There remained several challenges to credit management in Q4/2015 in particular and in 2015 in general. *First*, pressure on interest rates prevails because deposit growth was outpaced by credit at some credit institutions, and because of the possibility of follow-up interest rate hikes in the U.S. Credit to deposit ratio reached very high level in some financial companies, even exceeding 420% (Figure 20). Meanwhile, those companies focused on consumption loans with high real interest rates. *Second*, "maturity mismatch" may become more challenging when part of medium and long-term capital of commercial banks has been poured into Government bonds. *Third,* the management mechanism based on credit targets despite the existence of many preferential credit programs resulted in "credit fragmentation", which in turn undermined the efficiency of credit allocation.

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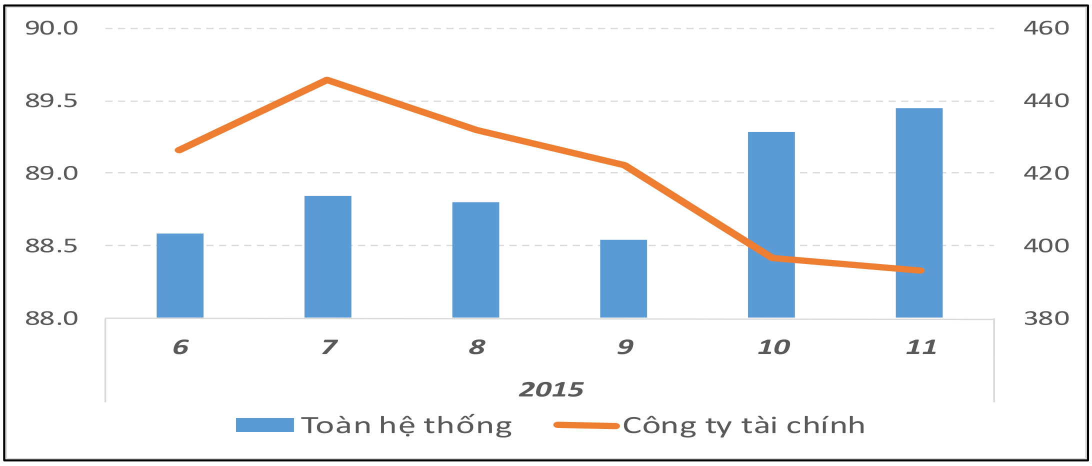
[40] Respective QoQ growth rates of credit outstanding were 2.7%, 5.1% and 2.7% in Q3, Q2 and Q1/2015.

Figure 20: Credit-to-deposit ratio (%)

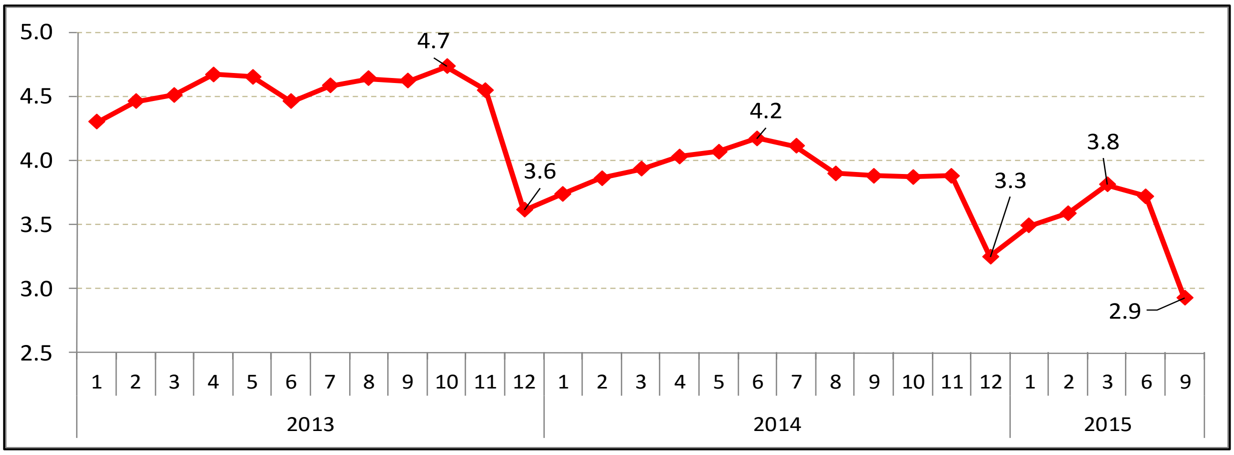


Source: SBV.

59. According to SBV statistics, NPL ratio continues to fall. By the end of September 2015, NPL ratio reported by credit institutions attained 2.93% (Figure 21). As such, the reduction of NPL basically achieved the target (below 3% by 30 September 2015). In 2015, Vietnam Assets Management Company (VAMC) bought VND 111 trillion of NPL principals, of which nearly VND 20 trillion had been bought in Q4. Interest rate on acquired VND-denominated NPLs was 9.6% per annum, while that of USD-denominated and EUR-denominated NPLs was 4.3% per annum and 5.4% per annum, respectively. VAMC also issued more than VND 110 trillion of special bonds.

Figure 21: NPL of credit institutions, 2013-2015

Unit: %

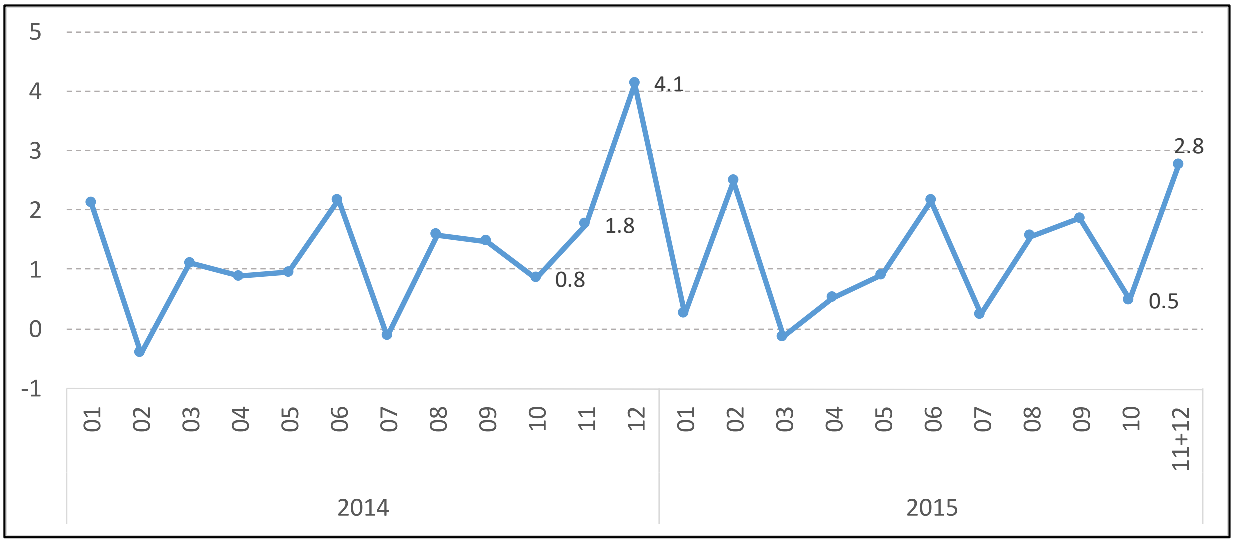


Source: SBV.

60. Total liquidity grew by 3.26% in Q4/2015 (compared to the end of Q3/2015), which was below the figures of Q3/2015 (3.70%) and Q4/2014 (6.85%). As of mid-December 2015, total liquidity was nearly 13.6% higher than that at the end of 2014. In Q4/2015, the SBV had flexible management of liquidity in order to support Government bond issuance and credit growth. Meanwhile, pressure on inflation is modest because the falling prices in international market has been transmitted to the domestic market.

Figure 22: Growth rate of total liquidity, 2014-2015

Unit: %



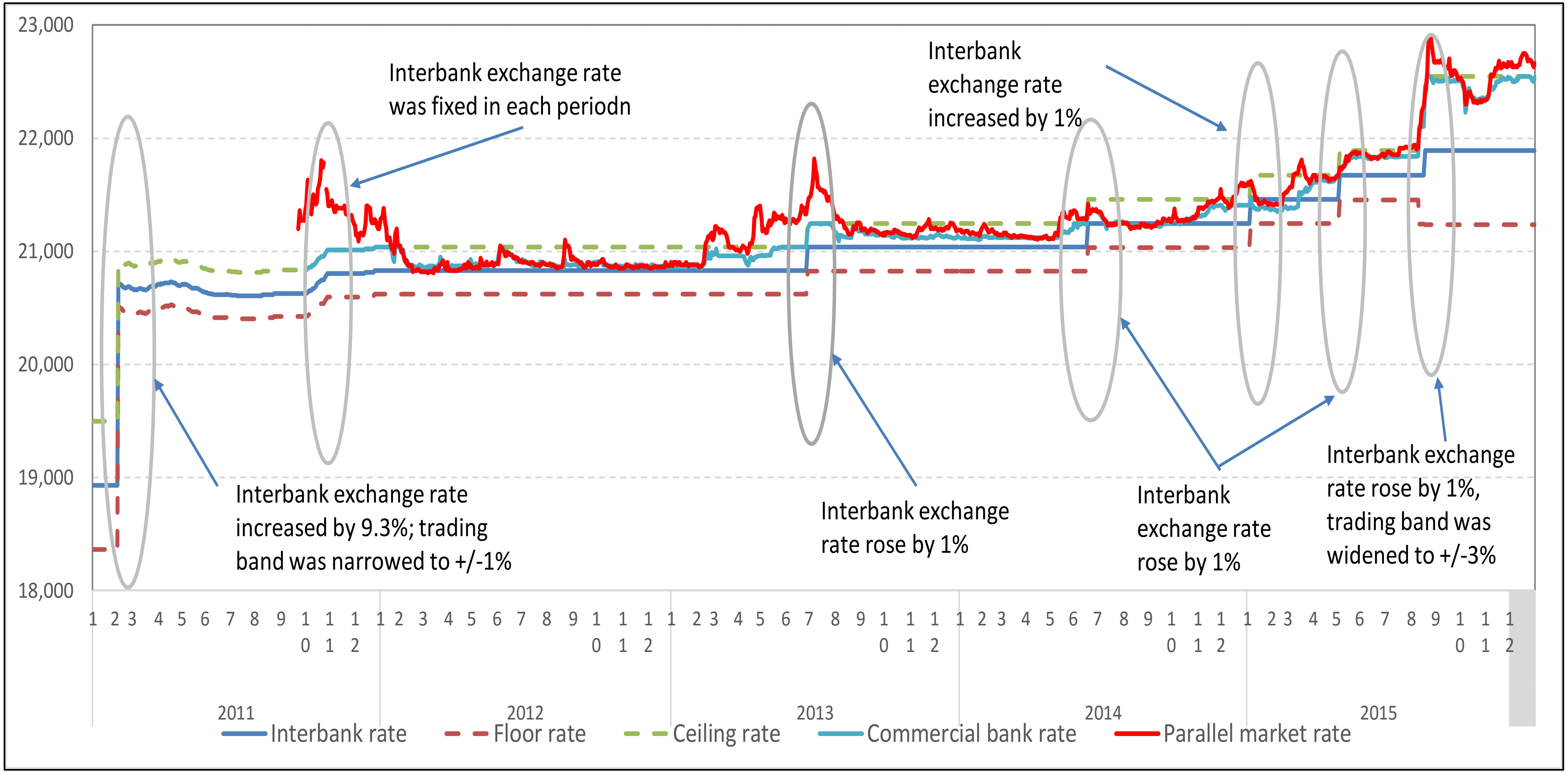
Source: Compilation from various sources.

61. The VND/USD exchange rate was more stable in Q4/2015 (Figure 23). In Q4/2015, the average interbank VND/USD exchange rate was fixed at 21,890. Meanwhile, the VND/USD exchange rate at both commercial banks and the parallel market decreased continuously in the first week of October, then slightly increased before being stable and close to the permitted ceiling since mid-November. Between mid-November and the end of December 2015, the parallel exchange rate usually stayed above that at commercial banks. However, the foreign exchange market hardly underwent stresses.

    a. The upward trend of VND/USD exchange rate during October-November 2015 was largely due to market expectation and adjustment around the timing of possible interest rate hike by the FED – including the appreciation of USD in the international market. Exchange rate was hardly exposed to pressure from trade balance because Vietnam had trade surplus during this period.

    b. The evolvement of exchange rate between mid-November and December 2015 originated from: (i) market expectation of further appreciation of USD internationally after the interest rate hike in mid-December 2015; (ii) market rumor about the possibility of adjusting VND/USD interbank exchange rate in early 2016, even though the SBV *had not* delivered any message on exchange rate mechanism for 2016.

Figure 23: VND/USD exchange rate, 2011-2015



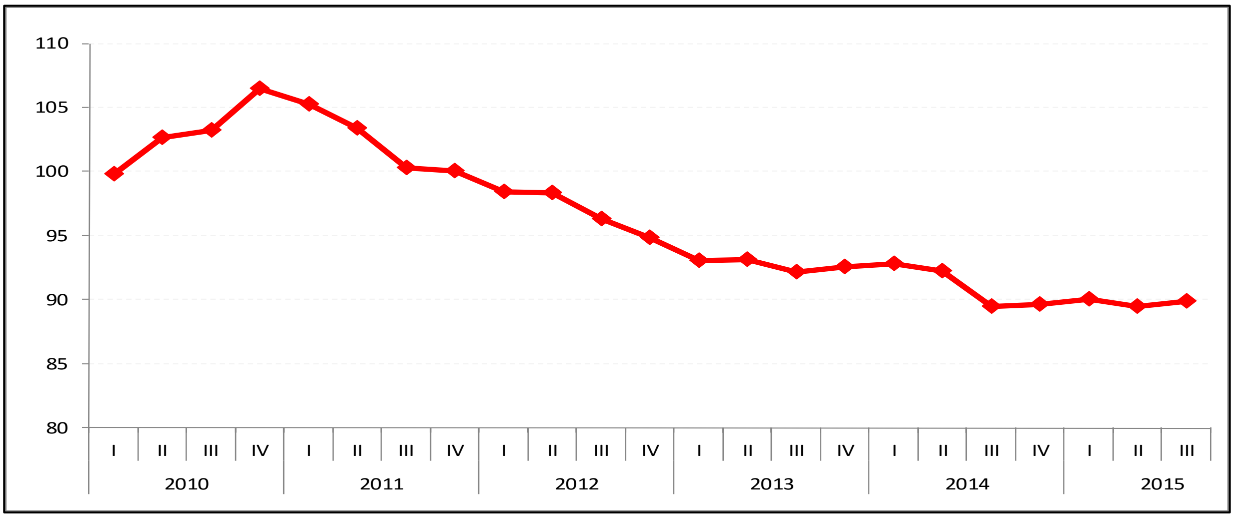
Source: VNDirect.

62. In general, the SBV effectively dealt with risks and fluctuations in the foreign exchange market in Q4/2015. Bold measures to reduce hoarding USD by individuals and organizations began to take effect. Information dissemination to the market has been close and frequent, aiming to guide the market prior to change in exchange rate regime. The new exchange rate regime[41] - arguably more flexible – may enable the SBV to better consider and respond to rapid and complicated changes in both domestic and international markets in 2016.

63. The conduct of exchange rate policy still encounters several challenges. *First*, more flexible mechanism based on daily developments and some other factors (both formally and informally) requires a larger and more complicated workload for the SBV. *Second*, monetary policy still has to serve a range of final[42] and intermediate objectives, of which the extent of exchange rate change only constitutes an intermediate one[43]. *Third*, the USD continues to appreciate and the withdrawal of capital from developing markets is yet to stop, leading to significant risks and consequences to Vietnam. *Finally*, the SBV has to seek balance between exchange rate stabilization and increasing foreign reserves.

64. As of Q4/2015, the real effective exchange rate (REER) of Vietnam increased by 0.44% compared with Q3/2015 and 0.46% compared with Q4/2014. Thus, Vietnamese goods became cheaper relative to foreign ones, though the real depreciation was modest (Figure 24). Efforts to stabilize VND/USD exchange rate have also weakened the competitiveness of Vietnamese goods in the context of the USD appreciating significantly against many other currencies.

Figure 24: Real Effective Exchange Rate (REER)



Source: Authors' calculation.

Note: Q1/2012=100. REER is calculated using trade data with 20 biggest trading partners and CPI statistics. Data for Q4/2015 is estimated; a higher REER implies that Vietnamese goods are relatively cheaper than foreign ones.

[41] Since 1 January 2016, the SBV announces the central rate daily before market opens, depending on 3 main factors: volatility of the 8-currency basket of Vietnam's major trading partners, foreign currency supply and demand, and macroeconomic balances.
[42] Such as GDP growth and inflation.
[43] Together with growth rates of outstanding credit and total liquidity.

65. Items of the balance of payment (BOP) varied drastically in Q3/2015. Overall BOP deficit was USD 6.6 billion in Q3/2015, despite consecutive surpluses of USD 2.7 billion and USD 555 million in the first two quarters of 2015. BOP deficit in Q3/2015 was attributed to the deficit of financial account, in particular other investment (net) with deficit of USD 7.3 billion. Meanwhile, current account surplus attained only USD 655 million in Q3/2015, i.e. below that in Q2/2015.

Table 5: Balance of Payment, Q1-Q3/2015

Unit: Million USD

	Q1	*Q2*	*Q3*
A. Current Account	**-1,341**	**691**	**655**
Goods (net)	-31	1,756	2,446
Services (net)	-830	-1,270	-1,194
Investment income (primary, net)	-2,418	-1,855	-2,550
Current transfer (primary, net)	1,938	2,060	1,953
B. Capital Account	**0**	**0**	**0**
Current Account + Capital Account	-1,341	691	655
C. Financial Account	**3,804**	**1,772**	**-5,250**
Direct investment (net)	1,974	2,118	2,158
Indirect investment (net)	-53	160	-79
Other investment (net)	1,883	-506	-7,329
D. Errors and omissions	**199**	**-1,908**	**-1,999**
E. Overall balance	**2,662**	**555**	**-6,594**
F. Reserves and related items	**-2,662**	**-555**	**6,594**

Source: SBV.

1.4. Investment

66. Investment activities accelerated in Q4/2015. Gross investment attained VND 450.7 trillion in Q4/2015, higher than that in Q2/2015 and Q3/2015 (Table 6). The figure reached VND 1,367.2 trillion in 2015, 12% higher than in 2014. In real terms, investment increased by 11.3% in 2015.

Table 6: **Gross investment, current prices**

Unit: Trillion VND

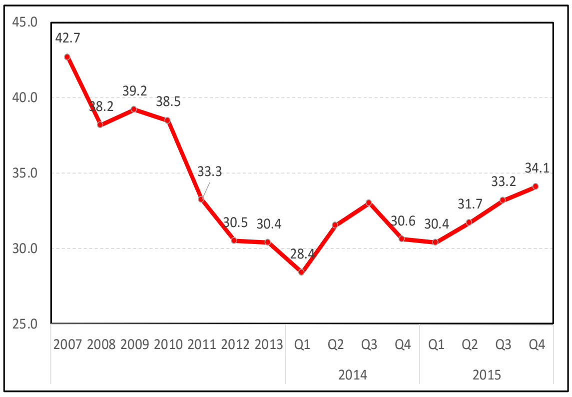
	2015 plan	Q2/2015	Q3/2015	Q4/2015	2015	Growth rate (%)
TOTAL	**1,343**	**302.6**	**360.87**	**450.7**	**1,367.2**	**12.0**
State budget investment	203	55.0	60.5	68.1	220.4	**6.1**
Government bonds	85	15.9	17.4	18.9	61.7	**-1.3**
State credit	60	14.3	16.1	18.5	62.5	**11.8**
Borrowings from other sources (by the State sector)	90	18.1	24.1	31.5	86.8	**8.8**
Investment by SOEs (Equity)	90	15.9	17.5	21.4	66.9	**10.6**
Investment by individuals and private sector	520	108.6	146.8	179.5	529.6	**13.0**
FDI	290	69.7	72.1	104.6	318.1	**19.9**
Other sources	25	4.5	6.3	8.2	21.2	**3.9**

Source: GSO.

67. The investment to GDP ratio was 34.1% in Q4/2015, higher than in previous quarters of 2015 and in Q4/2014 (Figure 25). The overall figure for 2015 attained 32.9%, exceeding that in 2014 (31.2%), albeit far smaller than in the period of 2007-2010. Notably, investment by domestic private sector and FDI enterprises rose considerably.

Figure 25: **Investment/GDP ratio**

Unit: %



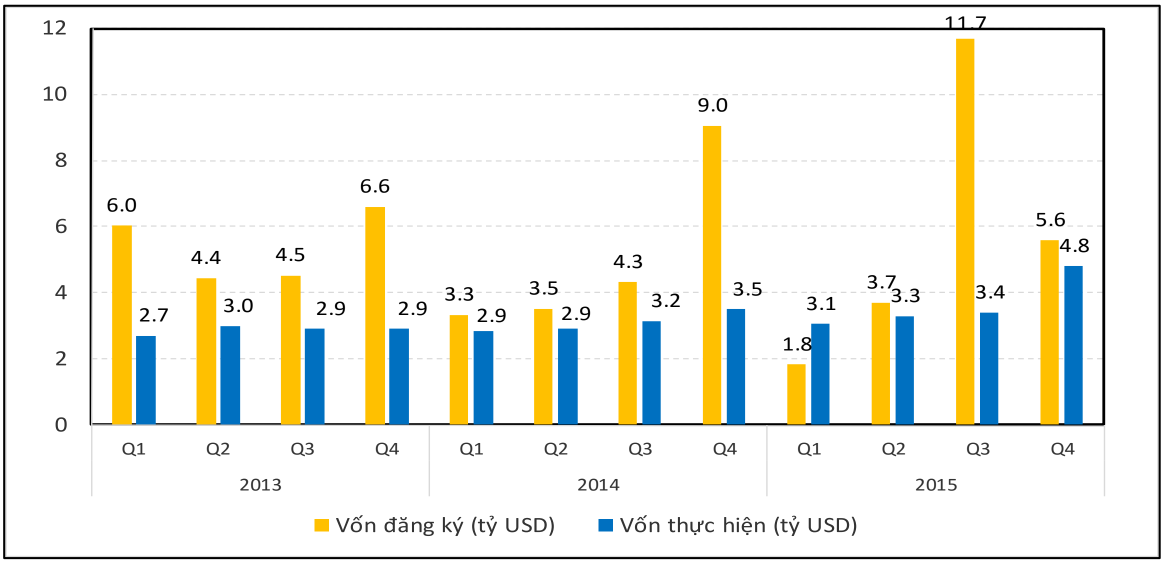
Source: GSO.

68. Investment expansion in 2015 was mainly by the foreign-invested sector (investment of which increased by 19.9%) and domestic private sector (by 13%). Implemented capital of both sectors in Q4/2015 increased from previous quarters (Table 6). Investment by domestic private sector in Q4/2015 went up by nearly 17.9% (YoY) while that by FDI reached 36.7%.

69. Registered FDI capital attained USD 5.6 billion in Q4/2015, representing a drop from those in Q3/2015 and Q4s of 2013 and 2014 (Figure 26). However, implemented capital amounted to USD 4.8 billion in Q4/2015, the unprecedented level in any single quarter. In 2015, the FDI sector had 2,013 newly-licensed projects with total registered and supplemented capital of USD 22.76 billion, increasing by 12.5% (YoY). Implemented capital of FDI in 2015 was estimated at USD 14.5 billion, up by 17.4% (YoY).

Figure 26: FDI attraction to Vietnam

Unit: Billion USD



Source: GSO.

70. The manufacturing sector received the biggest volume of FDI capital, with total registered and supplemented capital in Q4/2015 and 2015 of USD 3.9 billion and USD 15.2 billion, respectively. In 2015, the sector accounted for 66.9% of total newly-registered and supplemented capital. The corresponding share of electricity, gas, steam and air conditioning supply was 12.4%; real estate: 10.5%; and other sectors: 10.2%.

71. By scale of newly-registered FDI projects, electricity, gas, steam and air conditioning supply took the leading position with average capital of USD 350.2 million per project; followed by real estate (USD 63.1 million per project). The manufacturing sector stood at the third place with average newly-registered capital of USD 9.3 million per project. This modest figure is less than a concern, because: (i) more capital can be registered and supplemented depending on actual project progress; and (ii) the presence of more small- and medium-sized FDI enterprises, which is suitable to the current operations of value chains led by big corporations in Vietnam.

72. In 2015, Korea was the biggest investor to Vietnam with 702 newly-licensed projects and 260 supplemented projects, and total newly-registered and supplemented capital of USD 6.72 billion (or 29.6% of registered FDI capital). Increasing investment from Korea was partly induced by Vietnam-Korea FTA – which took effect since 20 December 2015 as the negotiation, signing and ratification of the FTA was accelerated by both countries. Malaysia ranked 2nd with total capital of USD 2.47 billion, or 10.9% of total registered capital; Japan was in the third place with total capital of USD 1.84 billion, or 8.1% of total registered capital; Taiwan took the 4th position with corresponding figures of USD 1.39 billion and 6.1%, respectively.

73. Higher investment by private and FDI sector in Q4/2015 in particular and 2015 in general was induced by some main reasons, namely: (i) more robust

recovery of economic growth in Vietnam; (ii) efforts to improve business environment and liberalize the market (including real estate); (iii) More rapid extension of credit when the crowding-out effect of public investment became less profound; and (iv) efforts to grasp opportunities from signed and pending FTAs of Vietnam (namely FTAs with Korea, EU or TPP, etc.)

74. Disbursement of state budget investment was accelerated toward the end of 2015. In Q4/2015, investment from State Budget amounted to VND 68.1 trillion (at current prices), representing a YoY growth of 12.4%. For 2015 as a whole, the corresponding growth rate was only 6.1%.

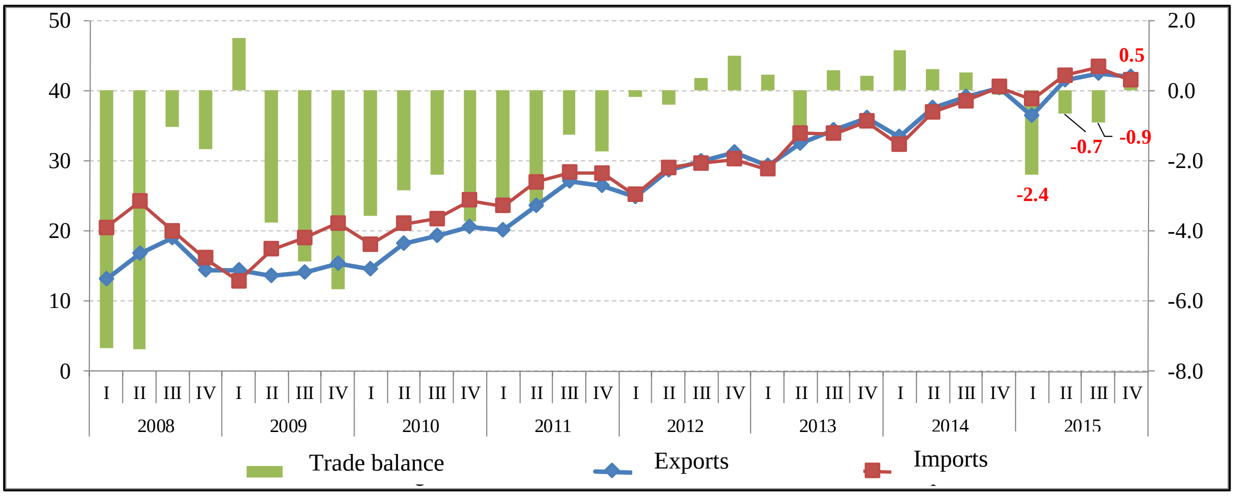
75. Disbursement of Government bonds increased sharply in Q4/2015 (relative to early quarters of 2015), but was below Q4/2014 (VND 20 trillion). Still, overall disbursement of Government bonds in 2015 even fell by 1.3% compared to 2014. Such a fall was mainly attributed to modest issuance of Government bonds in the first 10 months of 2015 due to: (i) unfavorable conditions to issue Government bonds in international markets; (ii) requirement to issue Government bonds with term to maturity of at least 5 years (which was relaxed in November 2015); and (iii) targeting bank liquidity for production. Besides, low disbursement of Government bonds was caused by: (i) a large share of Government bonds being issued for debt rollover; and (ii) time costs associated with procedures and regulations related to Government bond issuance.

1.5. Trade

76. Exports attained USD 41.89 billion in Q4/2015, or 1.3% lower than Q3/2015 (Figure 27). On YoY basis, exports in Q4/2015 grew by USD 1.81 billion or 4.5%. Total exports in 2015 reached USD 162.11 billion, up by 7.9% (YoY). Export growth rate was lower than the corresponding figures of 2011-2014, and lower than the target for 2015 (10%). The average growth of export was 17.6% per annum during 2011-2015 (Figure 28).

Figure 27: Quarterly exports, imports and trade balance, 2008-2015

Unit: Billion USD



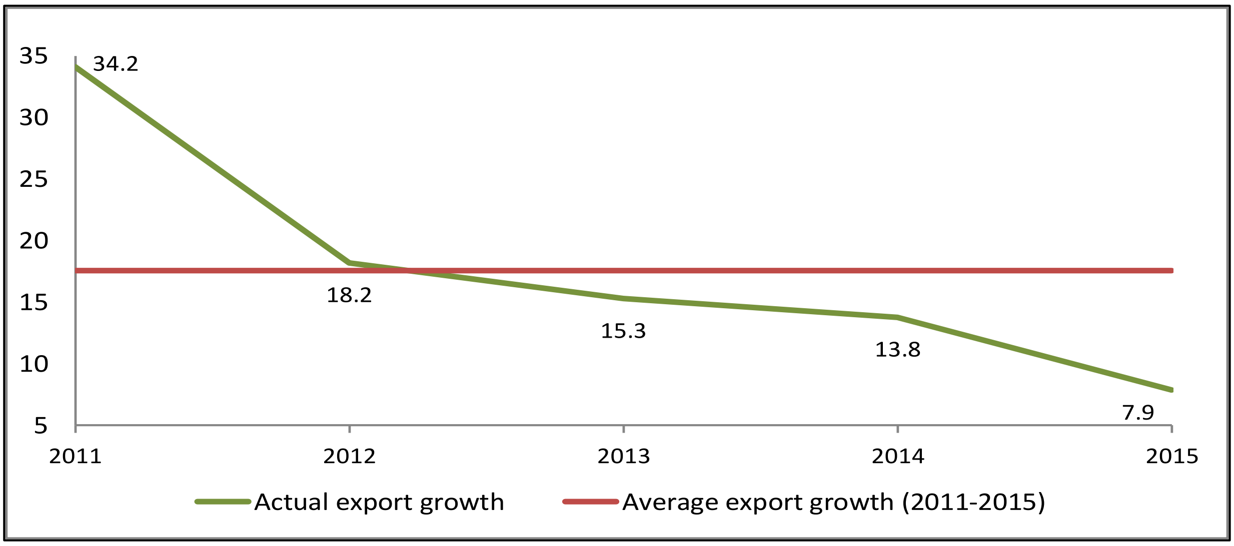
Source: GSO.

77. FDI sector accounted for lion's shares in Vietnam's exports. The figure was 68.4% in Q4 and 68.2% in 2015 respectively. However, YoY export growth of FDI sector decelerated to only 9.6% in Q4/2015, remarkably lower than the figure for the first 9 months of 2015 (20.8%). In 2015, exports of this sector increased by 17.7% (YoY), contributing 11.1 percentage points to the overall export growth.

78. Exports by domestic firms attained USD 13.2 billion in Q4 and USD 51.5 billion in 2015. On YoY basis, exports of this sector even fell by 6.7% Q4/2015. In 2015, exports of domestic firms dropped by 8.43%, leading to a decline in overall export growth rate by 3.2 percentage points.

Figure 28: Annual and average export growth rates, 2011-2015

Unit: %



Source: General Department of Customs.

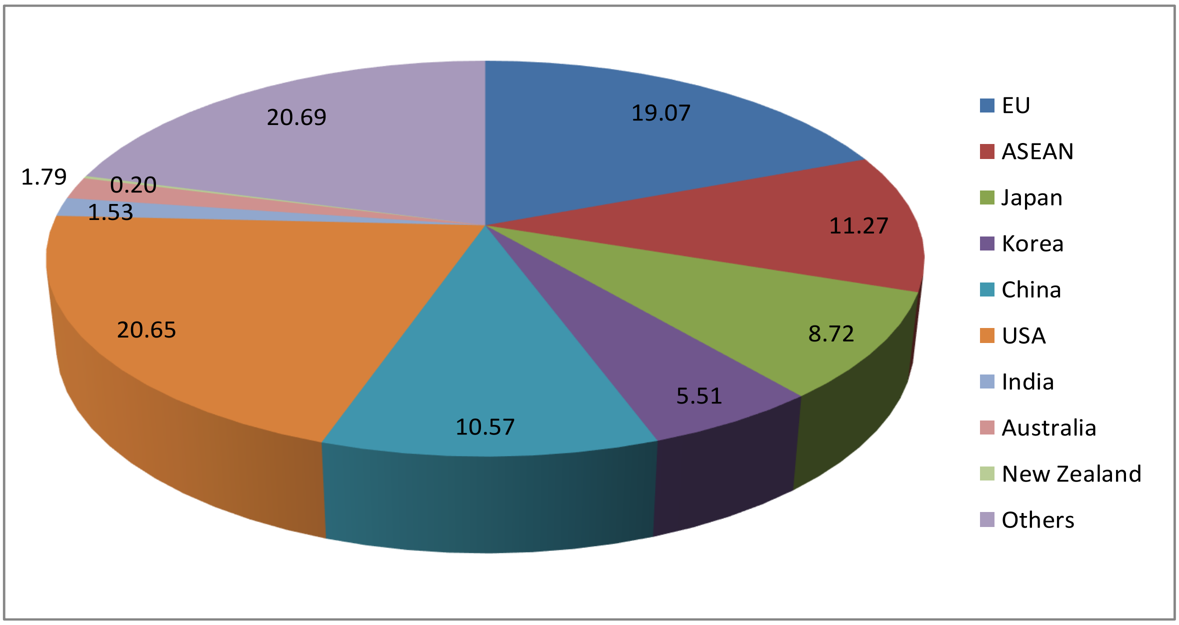
79. Exports of many commodities attained considerably high growth rate in 2015, notably telephones and components (USD 30.2 billion, increasing by 27.9% - YoY), computers, electronic products and components (USD 15.6 billion, 36.5% - YoY) and garment and textiles (USD 22.8 billion, 9.1% - YoY). Other key products experienced drops in exports in 2015. In particular, exports of crude oil decreased by 48.5%, coffee by 24.8%, aquatic products by 16.0%, iron and steel by 15.6% and rubber by 13.9%.

80. Price and/or export volume of many products dropped sharply in 2015. Export price indices of some key commodities went down significantly in 2015, on average by 3.8%. Particularly, export price of crude oil decreased by 53%, gasoline: 49.8%; rubber: 24.1%; coal: 10.0%; rice: 8.1%; coffee: 6.4%; fruits and vegetables: 3.4%; aquatic products: 2.5%; ores and other minerals: 2.4%; etc. Export volume decreased for a number of agricultural products: coffee by 24.8%; rice: 4.5%; tea: 6.6%; coal: 66.2%; crude oil: 48.5%; and fertilizers: 25.2%, etc.

81. Modest expansion of exports in Q4 and 2015 could be attributed to some key factors, including: (i) slow recovery of the global economy, (ii) appreciation of

USD weakening Vietnam's products competitiveness (whereas VND/USD exchange rate was quite stable in Q4); (iii) prices of many products in international market decreased sharply, (iv) some export products were subject to anti-dumping investigation, anti-dumping duties[44]; and (v) inadequate preparation to take advantages of new FTAs in 2015 (such as FTAs with Eurasian Economic Union or with South Korea).

Figure 29: Exports to major trading partners in 2015 (%)



Source: General Department of Customs.

82. The export structure hardly changed in 2015. The USA remained the biggest export market of Vietnam, accounting for USD 33.5 billion or 20.6% of total exports. The EU ranked 2nd, accounting for 19.1% of Vietnam's exports in 2015. ASEAN followed with the share of 11.27%. The shares of China, Japan and Korea were 10.53%, 8.72% and 5.51%, respectively.

83. Imports were estimated at USD 41.9 billion in Q4/2015, increasing by 3.5% (YoY). For 2015, total imports attained USD 165.65 billion, growing by 12%. In real terms, imports grew by 18.89% in 2015, higher than in 2014 (13.2%). During 2011-2015, the average annual growth rate of imports was 14.3%.

84. The FDI sector also accounted for a major share in imports, albeit smaller than its share in total exports. In Q4/2015, import value of the FDI sector was USD 23.87 billion, or 56.95% of total imports. However, such an import value only increased by 1.7% (YoY), which was remarkably slower than in the first 9 months (20.8%). In 2015, imports of the FDI sector was about USD 97.3 billion, increasing by 15.5% and being equivalent to 58.7% of total imports.

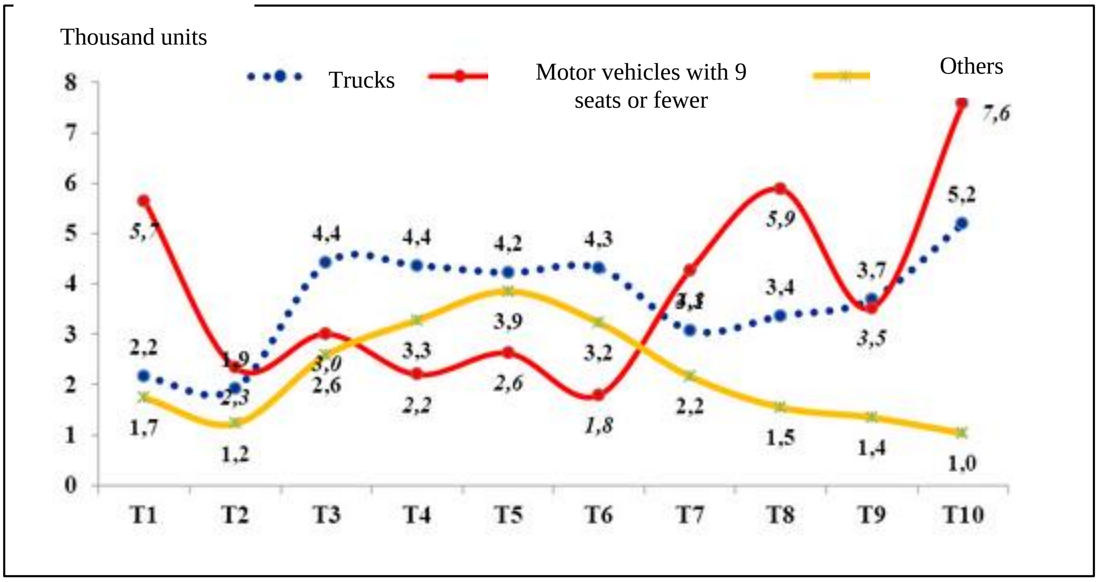
[44] For example, India initiated anti-dumping investigation on AA batteries imported from Vietnam on October 20th 2015; the USA started anti-dumping investigation on carbon rolled steel pipes imported from Vietnam on November 24th 2015, etc. Regarding anti-dumping duties, on December 24th 2015, Canada announced the final conclusion on the re-investigation case related to OCTG pipe products imported from some countries, including Vietnam, and imposed an anti-dumping duty of 37.4%.

85. In Q4/2015, import value of domestic firms attained USD 18 billion, or 43.0% of total imports. The corresponding YoY growth rate of imports was 6.6%. In 2015, the domestic sector imported USD 68.39 billion in value, up by 7.5% (YoY).

86. Imports in 2015 mainly comprised of production means and inputs. Import value of such products amounted to USD 151.2 billion, increasing by 12.3% and accounting for 91.3% of total imports. Imports of some products grew significantly, such as computers and electronic components (rising by 24.2%), telephones and components (25.4%), machinery and spare parts (23.1%). Imports of consumer goods were estimated at USD 14.4 billion, increasing by 10.4% and accounting for 8.7% (declining by 0.2 percentage point).

87. In Q4/2015, the number of imported CBU cars was 41.96 thousand, rising by 15.16 thousand or 56.57% (YoY). In October 2015, the amount of imported automobiles with 9 seats or fewer reached 7.58 thousand – the highest since January 2010, increasing by 115% (MoM), accounting for 55% of total imported CBU cars in the month.

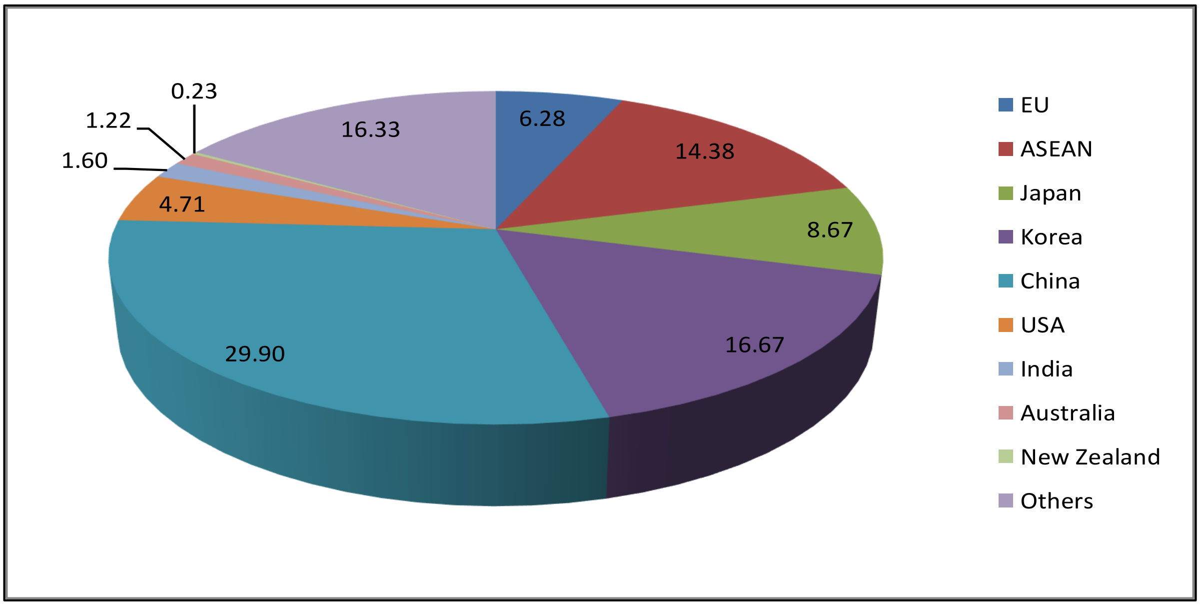
Figure 30: Monthly imports of CBU cars, 2015



Source: General Department of Customs.

88. China continued to be largest source of imports for Vietnam in 2015. Imports from this market amounted to USD 49.3 billion, increasing by 12.9%, accounting for approximately 29.9% of total imports. South Korea ranked 2nd with imports of USD 27.6 billion, up by 26.88%, and accounting for 16.67%. The shares of ASEAN, Japan and EU were 14.38%, 8.67% and 6.28%, respectively.

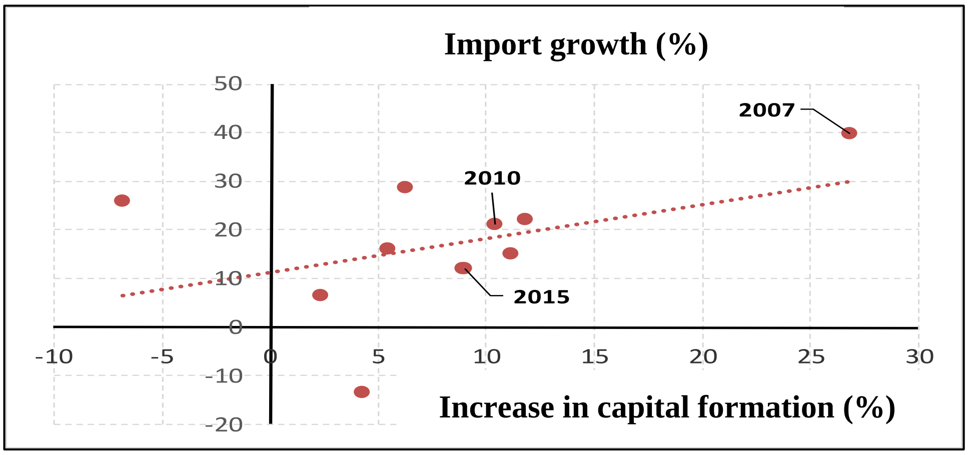
Figure 31: Imports from major trading partners, 2015 (%)



Source: General Department of Customs.

89. Import growth in 2015 was affected by some key factors, including: (i) restrictions of foreign-currency-denominated credits only to some areas; (ii) eases of international commodity prices; (iii) attempts to lock in benefits from some FTAs (especially Vietnam-Korea FTA); and (iv) economic recovery which induced higher demand for investment and imports. Notably, the pervasiveness from investment to imports seemed smaller in 2015 than in previous years (Figure 32).

Figure 32: Growth rate of gross capital formation and imports (%)

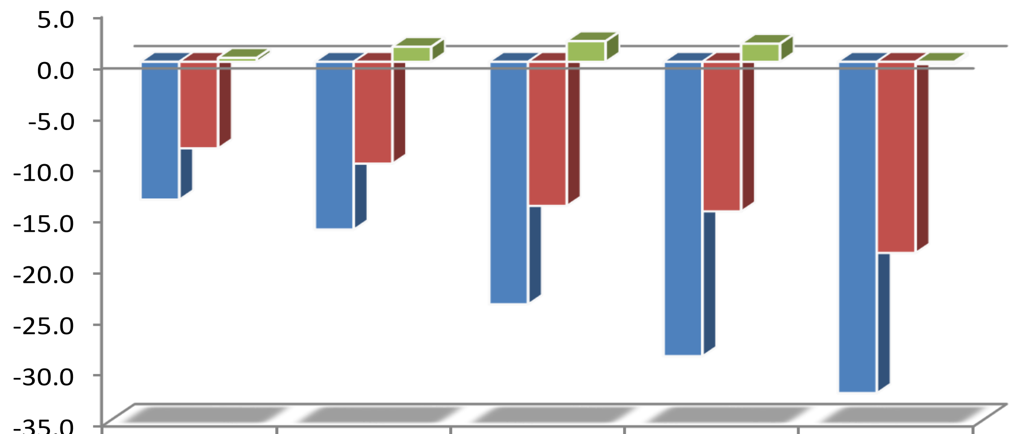


Source: GSO.

90. Trade deficit in Q4/2015 was estimated at USD 500 million. Overall trade balance was in deficit of approximately USD 3.4 billion. This deficit was noticeable since it followed 3 years of consecutive trade surpluses (2012-2014, Figure 27). Trade deficit accounted for 2.18% of exports in 2015, which was below the target of 5%. During 2011-2015, the average trade deficit amounted to USD 2.1 billion per year.

91. Vietnam mainly had trade surplus with the USA and EU. Meanwhile, trade deficit of Vietnam with other major markets tended to increase. In particular, trade deficit with China was estimated at USD 32.4 billion, increasing by 11.8% (YoY); South Korea: USD 18.7 billion, increasing by 27.8%; ASEAN: USD 5.5 billion, growing by 41.9%. Notably, Vietnam ran a trade deficit of about USD 230 million with Japan in 2015, after years of surpluses.

Figure 33: Trade deficit of Vietnam with major markets (billion USD)



	2011	2012	2013	2014	2015
China	-13.5	-16.4	-23.7	-28.8	-32.4
Korea	-8.5	-10.0	-14.1	-14.6	-18.7
Japan	0.4	1.5	2.0	1.8	-0.2

Source: General Department of Customs and GSO.

92. The FDI sector had trade surplus of USD 13.3 billion in 2015, growing by 36.8% (YoY). Meanwhile, trade deficit in 2015 was largely sourced from the domestic sector, with deficit of USD 16.8 billion. This deficit was more than twice the average figure for 2011-2015 (about USD 7.2 billion per year). Trade deficit of domestic sector tended to increase over the quarters, from USD 3.2 billion in Q1/2015 to USD 4.8 billion in Q4/2015. Trade deficit of domestic firms in Q4/2015 was also higher than in Q4/2014 (USD 2.7 billion). The expansion of trade deficit of domestic firms may imply: (i) deterioration of such firms' competitiveness; (ii) lower positions with less added value of such firms in the value chain.

93. Deeper economic integration requires domestic enterprises to seriously rethink their participation in the export value chain.

   a. The traditional approach is to import materials and inputs from foreign markets for export-oriented processing. This method is quick and easy; however domestic firms will receive low profits. As such, this method mainly works for enterprises at initial development stages.

   b. The second approach is to import materials and inputs from FTA-partner countries with appropriate rules of origin (ROO; for example, ASEAN Economic Community with cumulative rules of origin). Then, domestic enterprises are able to take advantage of preferential import tariffs when exporting to suitable FTA partners. Vietnam has participated in many FTAs which created diverse opportunities for enterprises. However, enterprises still face with some challenges in: (i) managing the sources of imported inputs to satisfy ROO requirements; (ii) minimizing costs related to time and procedures; and (iii) formulating a roadmap to maintain competitiveness and upgrade positions in the value chain.

c. The third approach – which is more complex and challenging – is to develop domestic supporting industries for own production of Vietnamese and FDI enterprises. With sufficiently developed supporting industries, Vietnam may take advantage of opportunities from various FTAs. This is a long-term roadmap that requires tremendous determination and efforts of domestic enterprises. Developing partnership with nations and/or enterprises that possess advanced technology and value chain management capacity will help shorten the time for such a roadmap.

94. Total retail sales of goods and services in Q4/2015 amounted to VND 851.6 trillion, increasing by 6.5% (YoY). Meanwhile, retail sales of goods reached VND 663.6 trillion, growing by 10.8% (YoY). Noticeably, revenues from accommodation, food and beverage services attained VND 93.2 trillion, decreasing by 0.1% (YoY). Revenues of tourism service were at VND 7.9 trillion, increasing by 18.6% (YoY). This increase was notably, given that Vietnam's tourism was under hardship and required numerous stimulus measures in 2015.

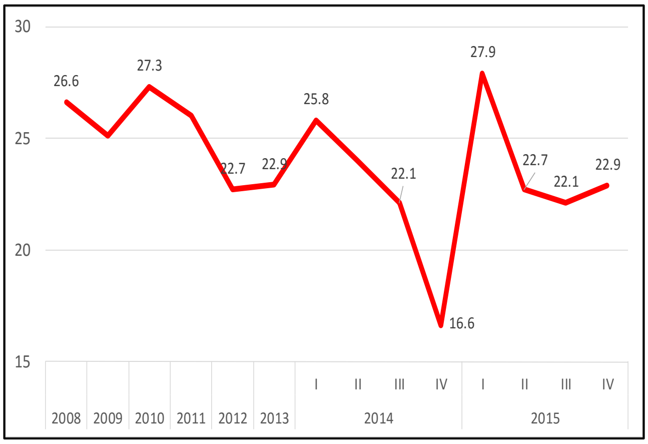
95. Total retail sales of goods and services was VND 3,200 trillion in 2015, up by 9.5% (YoY). Excluding the price factor, the growth rate attained 8.4%, higher than in 2014 (8.1%). Retail sales of goods amounted to VND 2,500 trillion, accounting for 76.2% of total retail sales and increasing by 10.6% (YoY). Revenues from accommodation, food and beverage service were estimated at VND 372.2 trillion in 2015, accounting for 11.5% of total retail sales and rising by 5.2% (YoY).

1.6. <u>Budget revenues and expenditures</u>

96. Budget revenues reached VND 306.7 trillion in Q4/2015, or 22.9% of GDP (Figure 34). This amount was relatively high compared to Q3/2015 (VND 236.9 trillion) as well as Q4/2014 (VND 227.5 trillion). Budget revenues in Q4 were equal to 33.7% of planned figure for 2015.

Figure 34: Budget revenues to GDP ratio

Unit: %



Source: Authors' calculation.

97. Domestic revenues accounted for 74.7% of total budget revenues in Q4/2015. This share was lower than Q1/2015 (76.6%), but much higher than Q2/2015 (70.9%) and Q3/2015 (74.4%). The corresponding share of revenues from exports and imports was 21.1% in Q4/2015, higher than the first 9 months of 2015 (18.1%). Meanwhile, revenues from crude oil only contributed 3.8% to budget revenues in Q4/2015, much lower than the first 9 months (7.6%)

98. In 2015, budget revenues reached VND 989.7 trillion, 8.6% higher than the planned target and up by 14.6% (YoY). However, revenues tended to increase more rapidly toward the end of 2015. By November 2015, budget revenues were only VND 860.1 trillion, equivalent to 94.4% of planned figure. The corresponding figure as of 18 December 2015 was VND 927.5 trillion. Underlying the difficulties of budget revenues in 2015 were: (i) phasing out of many import tariff lines under Vietnam's FTA commitments; and (ii) falls of import prices (especially for oil and petroleum products).

99. Accumulated budget expenditures (excluding repayment of debt principal) were estimated at VND 1,093.7 trillion by 18 December 2015. Budget expenditures attained nearly VND 324.0 trillion in Q4/2015, or 28.2% of the planned figure. Expansion of budget expenditures in Q4/2015 (compared to previous quarters) was attributed to: (i) improved resource availability for budget expenditures (from issuing government bonds, collection of revenues, etc.); (ii) smaller repayment of principal (about VND 10.8 trillion, compared to VND 33.6 trillion in Q3/2015); and (iii) weak disciplines over current expenditures (the figure was VND 236.3 trillion in Q4/2015, and VND 878.8 trillion for 2015, or 13.1% higher than the planned figure[45]).

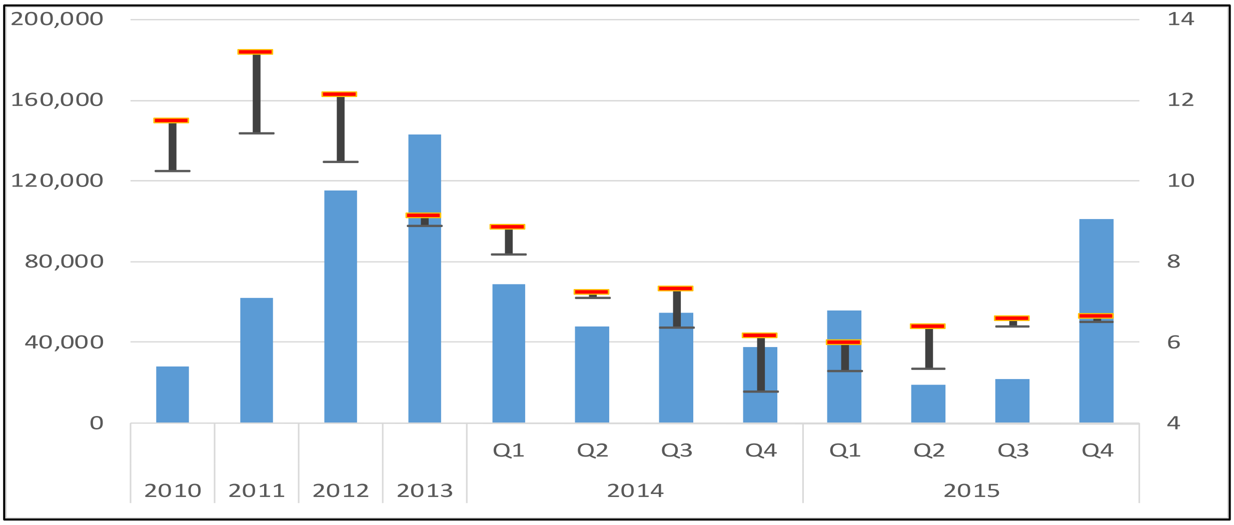
100. The value of newly issued government bonds amounted to VND 101.0 trillion in Q4/2015. The figure was only nearly VND 13.0 trillion in October, then increased significantly in November and December with total value of VND 88.0 trillion. The value of government bonds issued in Q4/2015 already exceeded cumulated figure for the first 3 quarters of 2015, representing an YoY increase by 2.67 times. Government bonds with 3 years to maturity accounted for 63.9% of issued value in Q4/2015 (corresponding figure for December was 80.9%). In 2015, value of newly issued government bonds attained VND 197.4 trillion, decreasing by 5.5% (YoY).

101. Interest rate for successful bids of government bonds (with 5-year terms to maturity) ranged between 6.53-6.55% p.a in Q4/2015. This range was similar to Q3/2015, and slightly increased relative to Q2/2015 (5.35-6.4% p.a., **Error! Reference source not found.**). Interest rate for successful bids of government bonds (with 3 year terms to maturity) ranged between 5.74%-5.9% p.a in Q4/2015, much lower than the corresponding rate of 5-year government bonds. The permission to issue government bonds with terms to maturity of between 3 and 5 years seemed to ease the borrowing costs for the Budget.

[45] Planned figures in Decision No. 3137/QD-BTC on December 10th 2014 of the Minister of Finance on publicizing State budget plan for 2015 (total current expenditures was VND 777 trillion, including VND 10 trillion for salary reform).

102. The issuance of government bonds in Q4/2015 received boost from: (i) permission from the National Assembly regarding the diversification of terms to maturity (allowing terms of between 3 and 5 years); (ii) appropriate management of liquidity by the SBV to support bond issuance. Notably, the interest rate on government bonds with 3 years to maturity was relatively lower than commercial banks' demand (the offered interest rate ranged between 5.65-7.0% p.a).

Figure 35: Government Bond issuance, 2010-2015



Source: HNX.

Note: The column diagram demonstrates the value of Government bond issuance (billion VND), measured on the left axis. The line graph demonstrates the range of interest rates of successful bids (%/p.a., 5-year terms to maturity), reference to the right axis.

103. The management of State Budget in 2015 presented valuable lessons for upcoming years. *First*, the control of budget expenditures in general and regular expenditures in particular remains essential; however, such control only works in the presence of strong determination of all levels of authority. *Second*, the role of business community, especially private enterprises, should be more thoroughly recognized. In this regard, the collection of budget revenues should only be in the extent to which resources and incentives are still retained for enterprises to reinvest and/or expand their production and business. *Third*, the budget-related tasks should be fulfilled right from the beginning of the year, rather than being left until the last months/quarters. *Finally*, international economic integration and the slow global economic recovery require Vietnam to revisit the roles of revenues from crude oil and from exports-imports. The increase of domestic revenues is hardly avoidable, but it needs to be justified concretely in terms of necessity and efficiency of its use.

2. *Macroeconomic Outlook*

104. A forecast scenario is specified for Vietnam in "business as usual" conditions in 2016, in line with the expectation of the global economic recovery and domestic economic development. GDP growth in partner countries is projected

at 3.4% in 2016[46]. US inflation may reach 1.0%[47]. Export prices of agricultural products may decline by 2.0%[48]. The international crude oil price may fall by 17.6% compared to the average export prices of 2015[49]. For Vietnam, the nominal VND/USD exchange rate is increased by 4%. Total liquidity increases by 20%. Outstanding credit increases by 16%. Import prices go down by 2%. Population increases by 1.04% and employment by 1.4%. The export volume of crude oil is assumed the same as in 2015. REER is assumed to increase by 1%. On the balance of payment, Government transfers increase by 5%, while (net) private transfers increase by 10% compared to 2015. The implemented capital of FDI rises by 10% compared to 2015, when investors believe in the improved economic prospects for Vietnam and when anticipate opportunities from newly-signed FTAs (TPP, EU-Vietnam FTA, Vietnam-Korea FTA, etc. Investment from State budget and Government bonds will be VND 254.95 trillion and VND 100 trillion, respectively. As an assumption, investment capital will be evenly disbursed throughout 2016.

105. YoY economic growth in 2016 is projected at 6.82% (Table 7). Export growth may reach 10.4%, higher than that of 2015. Trade deficit is projected at USD 4.1 billion, mainly due to the smaller earnings from crude oil exports. CPI will increase by approximately 4.37%.

Table 7: Projection of macroeconomic indicators, 2016

Unit: %

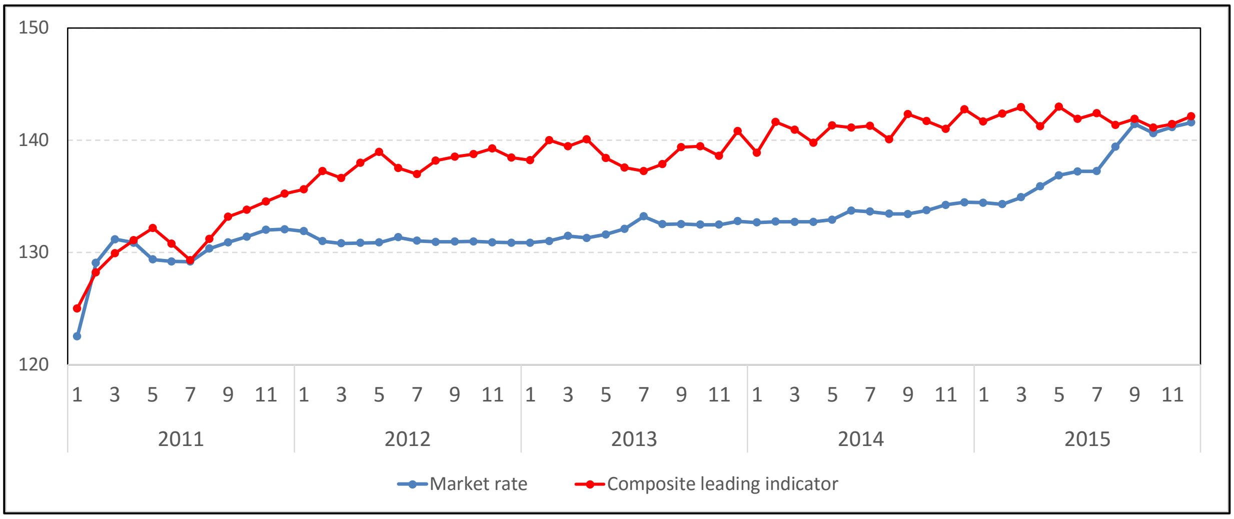
GDP growth rate (YoY)	6.82
Inflation	4.37
Export growth	10.4
Trade balance *(bil. USD)*	-4.1

Source: CIEM's projection from macroeconometric model using quarterly data.

106. Other important indicators concern the volatility of VND/USD exchange rate and the pressure on the foreign exchange market (Figure 36). CIEM's leading indicator of exchange rate shows no substantial change (over 3%) at the most recent time, implying that the exchange rate of commercial banks will be stable in the first 6 months of 2016 (with a probability of 94.4%). Accordingly, REER continues to support Vietnam's export, in the absence of major shock and/or disturbance of exchange rate policy to macroeconomic stability.

[46] IMF forecast (January 2016).
[47] OECD forecast (2015). https://data.oecd.org/price/inflation-forecast.htm [Accessed time: 20/1/2016].
[48] EIU forecast (January 2016).
[49] IMF forecast (2016).

Figure 36: Leading indicator of exchange rate



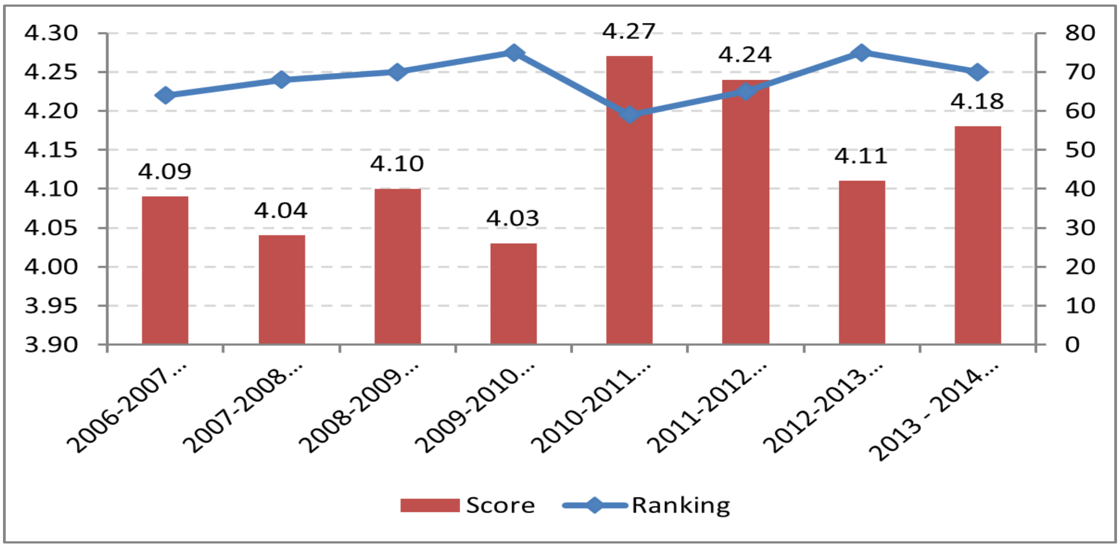
Source: Authors' calculation.

III. SELECTED ECONOMIC ISSUES

1. Vietnam's competitiveness: Improvements and challenges in 2014 -2015

107. According to the Global Competitiveness Report 2015-2016[50] of the World Economic Forum, Vietnam has significantly improved competitiveness in 2015, up by 12 ranks (from 68 out of 144 to 56 out of 140), the most rapid increase ever. The competitiveness has been continuously improved since 2012 (Figure 37). Vietnam is currently among the countries in transition from Stage 1 (factor-driven growth; in 2014[51]) to Stage 2 (efficiency-driven growth)[52] as its GDP per capita already exceeded USD 2,000[53].

Figure 37: Ranking and competitiveness indices of Vietnam during 2007-2015

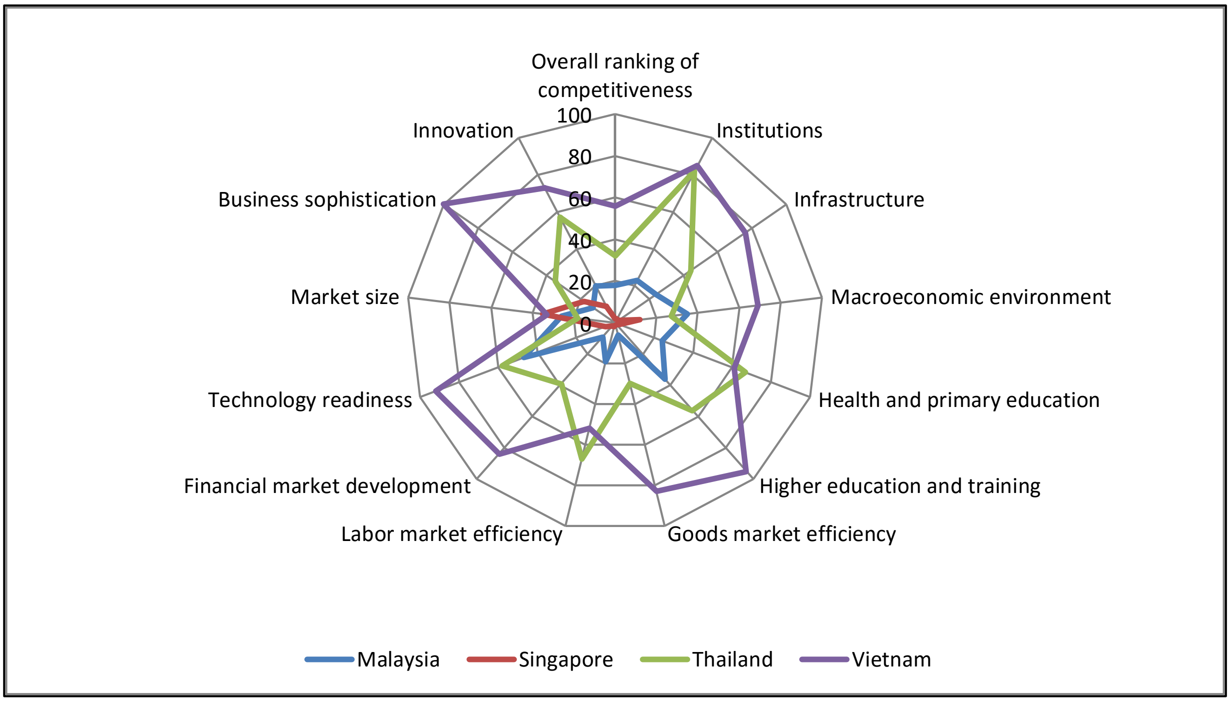


Source: WEF.

108. Among ASEAN, Vietnam ranked 6th after Singapore (2nd), Malaysia (18th), Thailand (32nd), Indonesia (37th) and Philippines (47th) and remained in the upper half of the overall Global Competitiveness rankings. Despite crisis with ringgit devaluation, Malaysia still moved up by 2 ranks to the 18th. Thailand inched down by 1 rank to the 32nd; Indonesia down by 3 to 37th while Philippines up by 5 to 47th. Singapore remained the second most competitive globally, just only after Switzerland. Despite most rapid improvements, Vietnam still lags far behind top ASEAN performers in almost all indicators (Figure 38).

[50] Published September/2015.
[51] Weights to rank Competitiveness of the countries in Stage 1: Basic requirements (60%), efficiency enhancers (35%) , and innovation and sophistication factors (5%).
[52] Weights to rank the competitiveness of countries in transition from Stage 1 to Stage 2: basic requirements (58.9%), efficiency enhancers (35.8%) and innovation and sophistication factors (5.3%)
[53] GDP per capital of Vietnam achieves USD 2,053

Figure 38: Ranking of competitiveness of Vietnam and some ASEAN members



Source: WEF.

109. According to the World Economic Forum rankings in 2015, nine out of twelve indexes of Vietnam have been improved; one remained unchanged in terms of both ranking and score (Health and primary education) and two other indexes fell in rankings (Table 8). Vietnam has improved most rapidly in Innovation (up by 14 ranks), Institutions, and Technological readiness (both up by 7 ranks). The country also progressed in terms of Macroeconomic environment, Financial market development, and Business sophistication (all up by 6 ranks); Infrastructure (up by 5) and Higher education and training (up by 1). Despite higher rankings in Macroeconomic environment, Business sophistication, and Financial market development, the scores of these indexes have not been improved; that of Financial market development even declined. This is technically because scores of certain countries decreased even more rapidly. Meanwhile, Vietnam's scores of "Goods market efficiency" and "Labor market efficiency" do not change, but the rankings decreased due to outperformance of other countries.

110. The World Economic Forum defines competitiveness of a country as the set of 12 pillars, they are in turn organised in three sub-indexes. Vietnam is in the transition process (from Stage 1 to Stage 2); thus, weight of Basic requirements is still the highest (58.9%), followed by Efficiency enhancers (35.8%) and Innovation and sophistication factors (5.3%). In 2015, performance of Vietnam in Basic requirements has slightly improved (score rises from 4.4 to 4.5 and ranking increases by 7 places); while two other groups saw no progress in terms of score but gained in the rankings (Table 8).

Table 8: Ranking and scores of Vietnam in 2014 and 2015

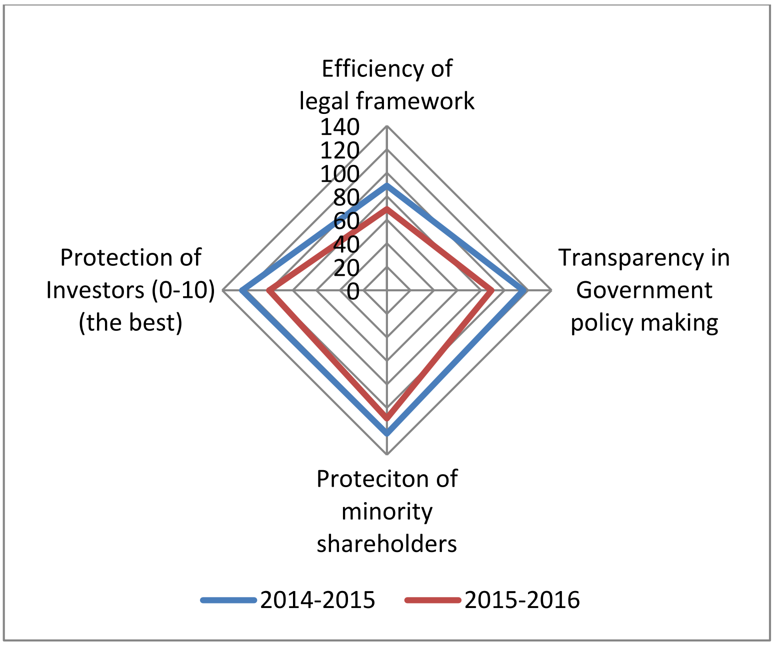
Global Competitiveness Report		2014-2015		2015-2016		Changes increase (+). decrease (-)	
Number of economies covered		144 countries		140 countries			
Scores measured on a 1 to 7 scale; "*" do not measure on a 1 to 7		*Rank*	*Score*	*Rank*	*Score*	*Rank*	*Score*
	The Competitiveness Index	**68**	**4.2**	**56**	**4.3**	**12**	**0.1**
A.	***Basic requirements***	***79***	***4.4***	***72***	***4.5***	***7***	***0.1***
1	Institutions	92	3.5	85	3.7	**7**	**0.2**
2	Infrastructure	81	3.7	76	3.8	**5**	**0.1**
3	Macroeconomic environment	75	4.7	69	4.7	**6**	**0.0**
4	Health and primary education	61	5.9	61	5.9	**0**	**0.0**
B.	***Efficiency enhancers***	***74***	***4.0***	***70***	***4.0***	***4***	***0.0***
5	Higher education and training	96	3.7	95	3.8	**1**	**0.1**
6	Goods market efficiency	78	4.2	83	4.2	**-5**	**0.0**
7	Labor market efficiency	49	4.4	52	4.4	**-3**	**0.0**
8	Financial market development	90	3.8	84	3.7	**6**	**-0.1**
9	Technology readiness	99	3.1	92	3.3	**7**	**0.2**
10	Market size	34	4.7	33	4.8	**1**	**0.1**
C.	***Innovation and sophistication factors***	***98***	***3.4***	***88***	***3.4***	***10***	***0.0***
11	Business sophistication	106	3.6	100	3.6	**6**	**0.0**
12	Innovation	87	3.1	73	3.2	**14**	**0.1**

Source: WEF.

111. Detailed analysis on major sub-indicators under Basic requirements and Efficiency Enhancers:

a. Vietnam moved up in Institutions (by 7 ranks) thanks to improvement in 20 out of 21 sub-indices. However, Vietnam still ranked rather low (85 out of 140). Vietnam has improved in “Efficiency of legal framework in settling disputes” (up by 20 ranks), “Transparency in Government policymaking” (up by 27), “Protection of minority shareholders” (up by 23) (**Error! Reference source not found.**). There were also improvements in “Protection of investors” and “Protection of minority shareholders” thanks to the new regulations in the Enterprise Law 2014 and the Investment Law 2014.

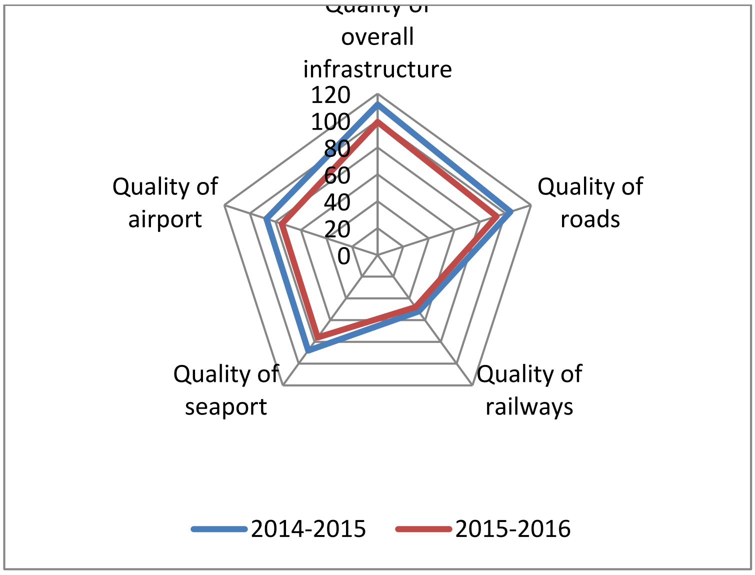
Figure 39: Ranking of institution pillar



Source: WEF.

b. Infrastructure gains 7 places to 76th with most sub-indexes in this pillar improving (except “Fixed telephone line/100 people”). There were significant improvements in Quality of roads, railways, air transport and overall infrastructure scores (Figure 40). However, most of these indexes remain less than half the overall GCI rankings.

Figure 40: Ranking of Infrastructure Pillar



Source: WEF.

c. “Macroeconomic Environment” is up 6 places (from 75th to 69th), mainly thanks to slower. However, due to increase in public debts and a decline in the country’s credit rating, the improvement of this pillar remains modest.

d. "Goods Market Efficiency" is at 83th place, a fall of 5 places compared to 2014, although the overall score remains unchanged. Almost all sub-indicators in this pillar are in the lower halt of the overall GCI rankings. Out of 8 sub-indicators for this pillar, 5 improved and 3 fell. Notably, the total profit tax (% profits) in Vietnam has significantly increased to 40.8%, from 35.2% (in GCI 2014-2015, published in 2014). Consequently, this indicator fell 25 places. The "No. of procedures to start a business" and "No. days to start a business" have not improved. the positive reforms in the 2014 Enterprise Law have not recognized in this GCR. Of the 7 foreign competition sub-indexes, 4 improved, while 3 fell. The "Business impact of FDI rules" dropped 26 places and "Burden of custom procedures" declined by 9 places (Table 9).

Table 9: Ranking and scores of Good Market Efficiency Pillar of Vietnam, 2014-2015

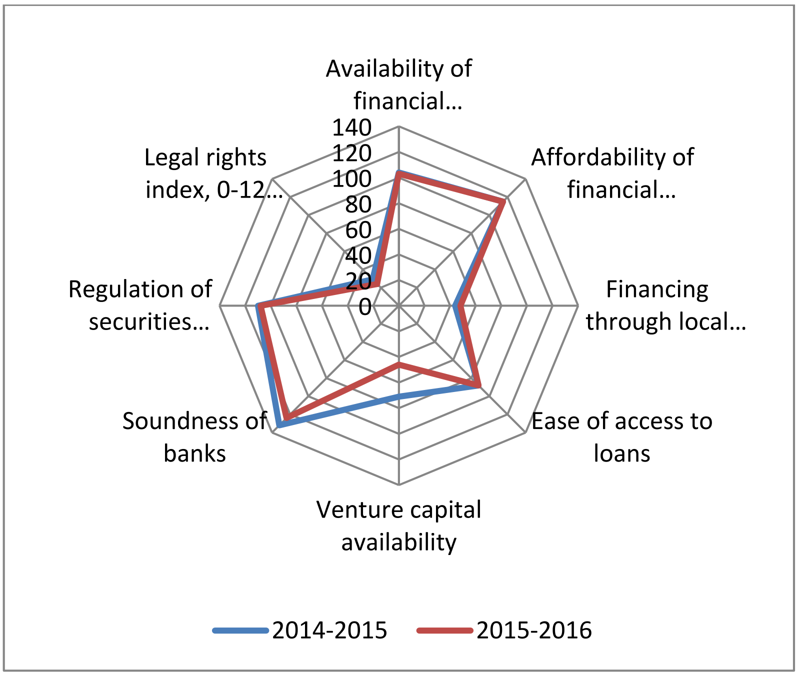
The Global Competitiveness Report		**2014-2015**		**2015-2016**		**Changes; increase (+), decrease (-)**	
Number of economies covered		144 countries		140 countries			
Point (1-7); "*"		*Ranking*	*Score*	*Ranking*	*Score*	*Ranking*	*Score*
A	***Competition***						
1	*Local competition*						
	Intensity of local competition	65	5.1	71	5.0	**-6**	**-0.1**
	Extent of market dominance	69	3.7	64	3.8	**5**	**0.1**
	Effectiveness of anti-monopoly policy	87	3.9	77	3.7	**10**	**-0.2**
	Effect of taxation on incentives to invest	93	3.5	69	3.6	**24**	**0.1**
	Total tax rate % profits *	61	35.2	86	40.8	**-25**	**5.6**
	No. procedures to start a business *	118	10.0	116	10.0	**2**	**0.0**
	No. days to start a business *	118	34.0	119	34.0	**-1**	**0.0**
	Agricultural policy costs	56	3.9	50	4.0	**6**	**0.1**
2	*Foreign competition*						
	Prevalence of non-tariff barriers	91	4.3	100	4.1	**-9**	**-0.2**
	Trade tariff, % duty	83	6.8	86	7.4	**-3**	**0.6**
	Prevalence of foreign ownership	103	4.1	93	4.2	**10**	**0.1**
	Business impact of rules on FDI	37	4.7	63	4.6	**-26**	**-0.1**
	Burden of customs procedures	94	3.6	90	3.6	**4**	**0.0**
	Imports as a percentage of GDP (%)*	16	85.1	13	87.9	**3**	**2.8**
B	***Quality of demand requirements***						
	Degree of customer orientation	105	4.1	102	4.1	**3**	**0.0**
	Buyer sophistication	85	3.3	70	3.4	**15**	**0.1**

Source: WEF.

e. “Labor market efficiency” lost 3 places (to 52th) due to a 22 place decline in productivity, and 3 place decline in “Reliance on professional management”.

f. “Financial market development” improved 6 places (from 90th to 84th) with 5 (out of 8) indicators improving, 2 unchanged, and 1 declining. “Venture capital availability” jumped 25 places; but “Financing through local equity market” fell 4 places (Figure 41).

Figure 41: Ranking and score of financial market development pillar



Source: WEF.

g. The “Innovation” pillar had the most notable improvement, up 14 places (from 87th, to 73rd). This resulted from improvements in “Capacity for innovation”, “Corporate R&D spending” and “No of scientist and engineers”. “Government procurement of advanced technology products” gains 6 places despite no change in the indicator score.

112. The consecutive improvement in Vietnam’s competitiveness ranking is evidence of its serious efforts to join international market and revise its policies and administrative procedures to improve the business environment. Since becoming an official member of WTO on 11 January 2007, Vietnam has signed 8 FTAs; and many bilateral trade and investment agreements with countries like India, Netherlands, United States, Indonesia, and Germany. By 2015, Vietnam had signed the largest number of FTAs. Vietnam is also the first country in the ASEAN to negotiate a Free Trade Agreement with the EU (in August, 2015); substantially completed TPP negotiations with 11 partners on October 2015; jointly implemented the ASEAN Economic Community on 31 December 2015 with other ASEAN member countries. Participation in the international market requires both management agencies and enterprises to change in order to satisfy international standards and improve their competitiveness.

113. Improvements in competitiveness in 2015 resulted from Vietnamese Government actions to resolve bottlenecks and promote business activities. The Government issued two Resolutions No. 19 (18 March 2014, and 12 March 2015) on improving the business environment and strengthening competitiveness; developed and revised key business laws (Enterprise Law, Investment Law and Bankruptcy Law) to better reflect international good practices; focused to a comprehensive reform of regulations on business conditions and import-export requirements ; issued Resolution No. 59/NQ-CP (7 August 2015) on implementation of the Enterprise Law and the Investment Law; approved measures to improve efficiency and effectiveness of professional clearance of import-export goods under Decision 2026/QD-TTg.

114. Business environment is an essential factor to assess the competitiveness of an economy. The World Bank's Doing Business (DB) Report 2016[54] concluded that Vietnam's business environment improved 3 places in 2015, from 93rd to 90th out of 189 economies, improving its DB score by 1.75 points (from 60.35 points to 60.10 point in distance to frontier (DTF) [55]) (Table 10).

Table 10: Ranking and scores of Vietnam's business environment in 2014 and 2015 (according to the assessment of World Bank)

	Indicators	Ranking (out of 189 economies			DTF points		
		DB 2015[56]	**DB 2016**[57]	Difference (+/-)	**DB 2015**	**DB 2016**	Difference (+/-)
	Business environment	**93**	**90**	**3**	**60.35**	**62.10**	**1.75**
1	Starting a business	125	119	6	77.68	81.25	3.57
2	Dealing with construction permits	12	12	0	82.33	82.21	-0.12
3	Getting electricity	130	108	22	56.91	63.34	6.43
4	Registering property	58	58	0	70.60	70.60	0.00
5	Getting credit	36	28	8	65.00	70.00	5.00
6	Protecting minority investors	121	122	-1	45.00	45.00	0.00
7	Paying taxes	172	168	4	43.61	45.41	1.80
8	Trading across borders	98	99	-1	67.15	67.15	0.00
9	Enforcing contracts	74	74	0	60.22	60.22	0.00
10	Resolving insolvency	125	123	2	35.02	35.83	0.81

Source: WB.

115. In 2015, the WB recognised that Vietnam had improved in 5 out of 10 DB indicators. They were:

[54] Published in October 2015.
[55] Distance to Frontier (DTF), measuring from 0 to 100 (%).
[56] Published in October/2014.
[57] Published in October/2015.

a. *Starting a business* rises by 6 places (and 3.57 points) due to a decline in time to complete procedures. As the DB Report 2016 (published October 2015) did not reflect the positive changes in the Enterprise Law 2014[58], Vietnam's performance in this indicator should improve in the next report.

b. *Getting electricity* recorded the best improvement in terms of both score (up 6.44 points) and ranking (up by 22 places), reflecting efforts to reduce the time needed to connect to the electricity grid (from 115 to 59 days). However, this indicator remains in the lower haft of the overall ranking.

c. *Getting credit* also improved (up 5 points, and 8 places) thanks to reforms to regulations to better ensure the rights of debtors in accessing credit information and wider scope of provided information.

d. *Paying taxes and social insurance* improved 4 places (from 172nd to 168th) thank to cutting 48 hours in time needed to pay taxes, and 62 hours of time to pay social insurances. As with "Starting a business", some reforms in tax policies and tax administrative procedures implemented in 2015 were not recognised in this Report, but will be reflected in the next edition.

e. *Resolving insolvency* remains low (123/189 economies) despite positive reforms towards a modern approach under the Law of Business Bankruptcy 2014 that helped improve this indicator by 2 places.

116. However, there remain five indicators where there has been no progress or a deterioration. Specifically, (i) the time to complete all formalities to get a construction permits actually increased by 52 days (from 114 to 166 days) - the only indicator that fell in 2015; (ii) An additional procedure is not required to "Register property" (up from 4 to 5 procedures), and score on the quality of land administrative procedures is low; (iii) improvements made in "Protecting minority investors" under the Enterprise Law 2014 were not in effect when the survey was conducted and were not reflected in this report; (iv) Trading across borders fell by 1 place due to weakness in management; and (v) Enforcing contracts did not changes in either ranking or score.

117. Vietnam introduced more reforms in 2015 than any of the ASEAN 4 countries, and its business environment ranking improved while the ranking of Malaysia, Philippines and Thailand declined; Singapore remains one of the best performing economies (Table 11). Vietnam's better performance resulted from the actions by the government agencies[59] under Resolution No. 19 (18 March 2014, and 12 March 2015) to improve the business environment and strengthen competitiveness. The regulatory reforms implemented under Resolution 19 have been recognised and highly appreciated by the business community. A Business Associations and

[58] Since the amended Enterprise Law in 2014 took effect after the World Bank survey.

[59] Including: Ministry of Planning and Investment, Ministry of Finance, State Bank of Vietnam, Vietnam Social Security, and Electricity Vietnam.

Cooperative Affiliation[60] survey found that the reforms receiving the most positive assessments were: starting a business (84%); paying taxes (75%), and customs (68%).

Table 11: Ranking and score of business environment of Vietnam and ASEAN 4

Economies	Rankings (out of 189 economies)			Point DTF		
	DB 2015	**DB 2016**	Changes increase (+), decrease (-)	**DB 2015**	**DB 2016**	Changes increase (+), decrease (-)
Malaysia	17	18	-1	79.13	79.08	-0.05
Philippines	97	103	-6	59.94	60.07	0.13
Singapore	1	1	0	87.34	87.34	0.00
Thailand	46	49	-3	71.33	71.42	0.09
Vietnam	**93**	**90**	**3**	**60.35**	**62.10**	**1.75**

Source: WB.

118. International organisations recognize that Vietnam's business environment and competitiveness significant improved in most areas in 2015. Despite consecutive climbs in rankings since 2012, Vietnam is still ranked relatively low in the overall ranking. Some areas have not progressed, or have even declined, including Goods market efficiency (Intensity local competition, total tax rates, non-tariff barriers; business impacts of FDU rules); pay and productivity; financing through local equity market; dealing with construction permits; and registering property.

119. Vietnam is ranked at 75 out of 141 countries in the Travel and Tourism Competitiveness Index[61] 2015, up by 5 places compared with 2013 (80/140) but its score fell (from 4 points to 3.6 points[62]). Performance in 7/14 indicators fell in 2015, while for 3/14 indicators the rankings improved, but scores fell (Table 12).

120. Vietnam has not exploited efficiently its comparative advantage in tourism. While travel and tourism competitiveness improved in 2015, Vietnam's ranking dropped and remains at the low of the overall rankings. Vietnam has not paid adequate attention to improving the following areas: prioritisation of travel & tourism (119/141); environment protection (indicator fell 72 places); and cultural resources (fell by 5 places, and 1.3 points, from 4.1 to 2.8 points).

[60] It is the joint program to monitor and supervise between 6 agencies and organisations: Vietnamese Fatherland Front, Ministry of Finance. VCCI, Vietnam Cooperative Alliance, SME Association, Vietnam Young Enterpreneurs to implement Resolution 19 in Taxes and Customs (published in December 2015).

[61] Travel and Tourism Competitiveness Index – TTCI is conducted by the World Economic Forum every 2 years, which measures factors and policies to promote the development of sustainable tourism, in order to contribute to improved competitiveness of one country. This index is measured on the base of 14 pillars (include 83 sub-indexes) divided into 4 groups.

[62] Score ranges from 1 – 7 (the best).

Table 12: Ranking of Vietnam's Travel and Toursim Competitiveness

	Global Travel and Tourism Competitiveness Report	2013		2015		Change increase (+), decrease (-)	
	Number of economies covers	140 countries		141 countries			
	Point 1-7 (7 is the best)	*Ranking*	*Point*	*Ranking*	*Point*	*Ranking*	*Point*
	The Travel and Tourism Competitiveness Index	**80**	**4.0**	**75**	**3.6**	**5**	**-0.4**
1	Business environment	60	4.6	66	4.4	**-6**	**-0.2**
2	Safety and Security	128	3.8	75	5.3	**53**	**1.5**
3	Health and Hygiene	81	4.5	83	5.0	**-2**	**0.5**
4	Human Resources and Labour Market	77	4.8	55	4.7	**22**	**-0.1**
5	ICT Readiness	68	3.2	97	3.4	**-29**	**0.2**
6	Prioritization of Travel & Tourism	110	3.6	119	3.7	**-9**	**0.1**
7	International Openness	108	4.3	89	2.7	**19**	**-1.6**
8	Price Competitiveness	18	5.1	22	5.3	**-4**	**0.2**
9	Environment sustainability	60	4.3	132	3.2	**-72**	**-1.1**
10	Air Transport Infrastructure	79	2.8	68	2.7	**11**	**-0.1**
11	Ground and Port Infrastructure	98	3.0	87	3.1	**11**	**0.1**
12	Tourism Service Infrastructure	112	2.2	105	2.9	**7**	**0.7**
13	Natural Resources	50	4.0	40	3.6	**10**	**-0.4**
14	Cultural Resources and Business Travel	28	4.1	33	2.8	**-5**	**-1.3**

Source: WEF.

Challenges to business environment and competitivness

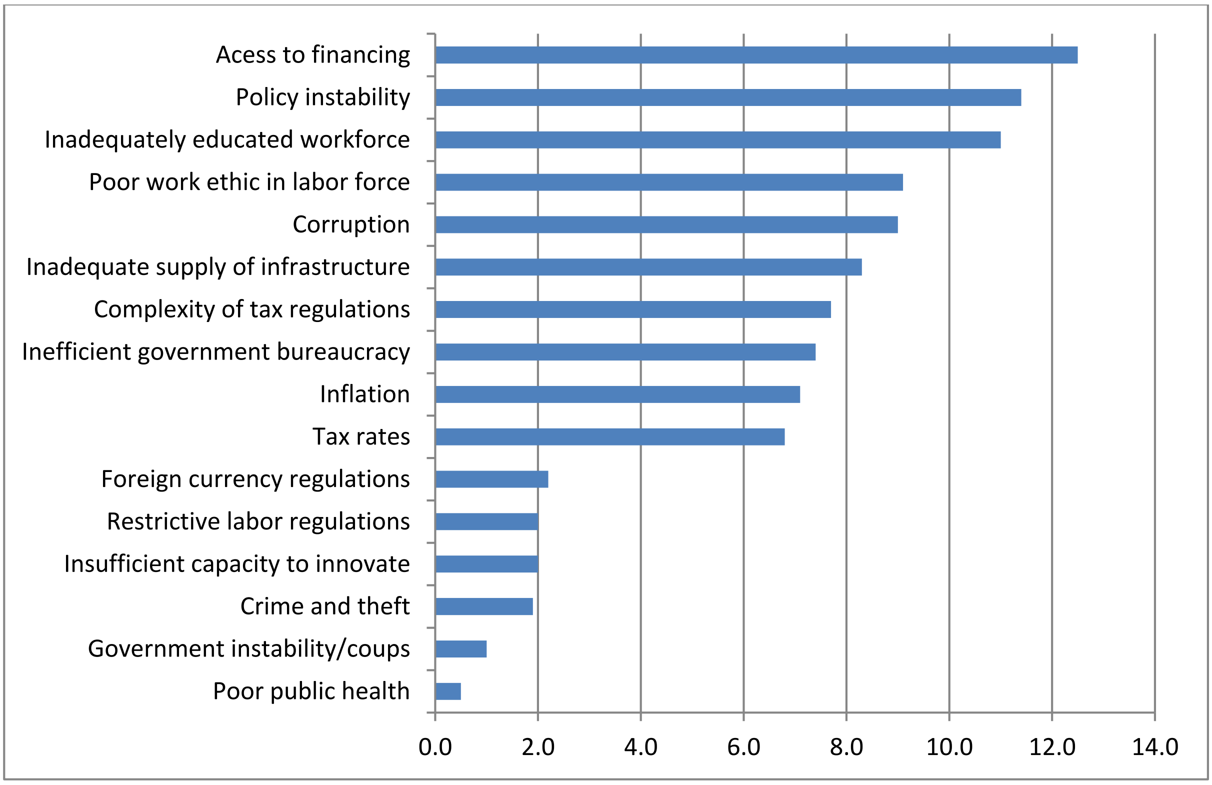
121. Despite improvements in business environment and competitivness in 2015, Vietnam's business community still face several difficulties and problems, including:

a. Local capital costs are still high compared to average international level; most domestic business are unable to diversify and access capital sources; the "playing ground" for domestic private sector, SOEs and FDI enterprises remains unfair; and there continue to be many barriers and administrative procedures that impose unnecessary burdens on business activities.

b. WEF surveys[63] show that access to financing; policy instability; inadequately educated workforce, and poor labour force work ethic are the most problematic factors for doing business in Vietnam (Figure 42).

[63] The Global Competitiveness Report 2015-2016

Figure 42: Most problematic issues in doing business



Source: WEF.

c. *External market and integration:* The business community, in particular the domestic private sector, has not received necessary and useful support and guidance from the management agencies to improve enterprises' preparation and their capacity to take advantage of international economic integration.

2. *Medium-term investment plan: Implications and challenges for economic restructuring.*

122. Vietnam is preparing medium-term public investment plan for 2016-2020 under the Investment Law No. 67/2014/QH13[64] at all levels of authority - including national level, ministries and ministerial agencies, and local authorities. This plan presents a significant change in approach to public investment management. Some anticipated positive impacts are as follows:

a. To gradually overcome the inherent shortcomings of dual budgeting, also known as the relative separation between management of current expenditures (by Ministry of Finance) and management of investment (by Ministry of Planning and Investment), including: (1) widespread and excessive investment; (2) weak linkage between public investment and budget availability (leading to increasing public debt); (3) inadequate consideration of long-term impacts of public investment projects on the increase of current expenditures (such as costs for maintenance and

[64] Investment Law was passed by the National Assembly on June 28th 2014 and took effect as of January 1st 2015.

operation after the completion of projects); and (4) inappropriate balance between current and investment expenditures, between investment on physical and social infrastructure.

b. To gradually overcome low-quality preparation of investment projects by requiring the approval their investment and improving the procedures of appraisal and selection. The Public Investment Management Law regulated that all public investment projects must be in prioritized order (Article 52) and approved of their investment directions (Article 55) prior to being listed in the medium-term public investment plan. Of which, the process of project approval with several stages and the participation of various stakeholders enable better project preparation and help ensure the quality as well as efficiency in project implementation.

c. To ensure major macroeconomic balance, and better inform ministries, agencies and local governments of possible resource availability during the 5-year plan so as to make efficient investment decisions. Investment planning in medium-term will also ensure adequate allocation of fund for approved projects, avoiding the failure to mobilize funds for projects as in the past years.

d. To enhance the publicity and transparency in allocating public investment, promoting restructuring of public investment.

123. With regard to IMF framework of Public Investment Management Assessment (PIMA), the issuance and implementation of medium-term investment plan would improve 5 out of 15 criteria of PIMA, including:

a. Criterion 1: Enhancing budget disciplines.

b. Criterion 2: Establishing the national and sectoral public investment plans.

c. Criterion 3: Enhancing the collaboration between central and local governments in managing public investment.

d. Criterion 4: Contributing to transparent framework for the selection, supervision and management of Public-Private Partnerships (PPP).

e. Criterion 5: Preparing medium-term budget plan.

f. Criterion 6: Strengthening the comprehensiveness and consensus of state budget, avoiding dual budgeting and separation between current expenditures budgeting and investment budgeting.

124. International experiences showed that the planning of medium-term public investment has been easier than actual enforcement. According to a recent IMF assessment on public investment efficiency, developing countries have surprisingly better scores than developed counterparts in terms of medium-term budget planning and public investment planning, whilst lagging behind in terms of enforcement, selection and appraisal of projects, and allocation of funds. As a result, the efficiency of public investment in developed countries is 30% higher than in

developing ones[65]. To improve public investment efficiency, it is also necessary to have good institutions, appropriate people, right tools and adequate incentives, rather than just well-prepared medium-term public investment plans[66].

125. As legal documents regulating medium-term public investment plans have just come into effect[67], it is too early to conclude and assess the impacts of such plans. However, the recent planning of medium-term public investment has encountered several shortcomings and obstacles, leading to slow approval, ineffective and inefficient implementation as well as affecting the outcomes of public investment restructuring.

Legal documents governing the planning of medium-term public investment for 2016-2020

126. In addition to Public Investment Management Law, state agencies have issued many legal normative documents and regulations to guide the planning of medium-term public investment. The key documents (in chronological order of issuance) include:

- Directive No. 23/CT-TTg dated 5 August 2014 by the Prime Minister regulating the planning of medium-term public investment for 2016-2020;
- Document No. 5318/BKHDT-TH of MPI dated 15 August 2014 regulating the planning of medium-term public investment for 2016-2020;
- Document No. 63/TB-VPCP of Office of Government dated 16 February 2015 announcing Prime Minister Nguyen Tan Dung's conclusion at the meeting on the planning of medium-term public investment for 2016-2020;
- Document No. 1100/BKHDT-TH of MPI dated 27 February 2015 on supplementary guidance for the planning of medium-term public investment for 2016-2020;
- Resolution No. 1023/NQ-UBTVQH13 of Standing Committee of the National Assembly dated 28 August 2015 and Decision No. 40/2015/QD-TTg of Prime Minister dated 14 September 2015 issuing principles, criteria and norms for the allocation of development investment capital from state budget for 2016-2020;
- Decree No. 77/2015/ND-CP of the Government dated 10 September 2015 regulating the medium-term and annual plans of public investment;
- Document No. 8123/BKHDT-TH of MPI dated 23 October 2015 on the medium-term public investment plan for 2016-2020 and the investment plan for 2016, with notice of the delay of National Assembly in approving the Report on National medium-term public investment plan for 2016-2020 (tentatively by March 2016);

[65] IMF, 2015, Making Public Investment More Efficiency.
[66] Hart T., Krause P., 2015, Bricks and Dollards: Improving Public Investment in Infrastructure.
[67] Decree No. 77/2015/ND-CP on the annual medium-term public investment plan was issued on Sep 10th 2015 and took effect as of Nov 1st 2015.

- Document No. 10638/BKHDT-TH of MPI dated 30 November 2015 on the approval schedule of socio-economic development plan, medium-term public investment plan for 2016-2020 and capital allocation in 2016 for newly started projects, which stipulates that ministries, agencies, and local governments only approve their medium-term public investment plans for 2016-2020 after the approval of national plan.

127. The afore-mentioned documents have created a regulatory and administrative framework for the planning of medium-term public investment nationwide. However, some important documents were issued after the predetermined deadlines[68]; many documents regulating and dealing with certain practical situations, leading to entanglement for planning stakeholders.

Difficulties and obstacles in the preparation of medium-term plan

128. Difficulties and obstacles exist in each and every stage of the planning process. Upon *identifying estimated capital for 2016-2020*, it is the first time that all ministries, agencies and localities (including 3 levels of province, district and commune) participate in planning all sources of funding during 2016-2020; therefore, they encountered a lot of obstacles and difficulties, which primarily lied in the calculation and estimation of funding for medium-term public investment. Meanwhile, Vietnam has no medium-term state budget plan, thus the medium-term public investment plan has not been comprehensively considered and linked with public finance and medium-term budget revenues and expenditures. This may present a risk of collapse for medium-term public investment plans at all levels.

129. At the central level, total demand for development and investment, proposed by ministries, agencies and localities, during 2016-2020 was estimated at VND 3,710 trillion, 19 times larger than planned figure for 2015 and 2.2 times larger than mobilization plan for 2016-2020 (estimated at VND 1,679 trillion).[69]

    a. In 2016-2020, state budget (including ODA) may only suffice for repayment of basic construction debts, payment for advanced items, reciprocal contribution to ODA projects and payment for unfinished projects in 2011-2015.

    b. The demand of new investment capital (about VND 1,586 trillion) has not yet met by any source. Therefore, Vietnam may have difficulty starting new public investment projects in 2016-2020.

130. At the local level, despite guiding documents on calculating and estimating available resources for public investment in 2016-2020, actual process still encountered several difficulties:

    a. Under the guidelines, the planned investment from Central budget allocated for ministries, agencies and localities increase by 10% p.a

[68] For instance, the Decree on planning medium-term public investment or legal documents regulating the principles, criteria and norms for the allocation of investment capital.

[69] Report No. 524/BC-CP dated October 17th 2015 by the Government to members of the XIII National Assembly on the Implementation of development investment plan for 2011-2015 and projected medium-term public investment plan for 2016-2020.

during 2016-2020 (compared to 2015 plan). In fact, given large demand for investment capital of ministries, agencies and localities, the growth rate of 10% p.a can hardly suffice. Besides, the bottom-up approach itself creates difficulty for higher authority in allocating funding based on proposed demand.

b. It is difficult to estimate the sources of capital that are subject to uncertainty, such as revenues from granting certificates of land use rights; proceedings from issuing government bonds due to unavailability of issuance plan in 2016-2020; State credit for development investment which depends on accessibility of each locality; ODA and concessional loans which rely on commitments and agreements of donors, etc.

c. The slow issuance of rules, principles, criteria and norms for allocating development investment capital from budget for 2016-2020 and the delay in targeted programs also create difficulties and obstacles for local governments[70].

131. At the stage of reviewing public investment projects, several difficulties also arise.

a. The Public Investment Management Law and other related guiding documents require ministries, agencies and localities to determine the outstanding debt of capital construction by 31 December 2014; and there must be no newly accrued construction debt since 1 January 2015. This strict regulation was essential to prevent the widespread increase of basic construction debt. Nonetheless, the actual volume of basic construction debt was already large enough to exert pressures on medium-term public investment plans for 2016-2020 of ministries, agencies and localities.

b. The review of project also showed a large number of projects being brought forward to 2016. In addition to eligible projects listed in the medium-term public investment plan for 2016-2010, a lot of projects have no clear follow-up plans due to incompleteness, insufficient progress after past extension or rescheduling, even with temporarily technical stop. There is no clear solution for unfinished projects that fail to be qualified for listing in the medium-term public investment plan. Besides, many projects were approved for implementation, but had no plan for funding; these projects have then to undergo another approval process which is time-consuming and costly.

c. Due to the amendment of principles for allocating funds to national targeted programs in 2016-2020 under Resolution No. 1023/NQ-UBTVQH13 and Decision No. 40/2015-QD-TTg, unfinished projects in 2011-2015 are not qualified for support in 2016-2020. This creates more pressure for local budget which has already been limited.

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[70] Only until August 28th 2015, did the Standing committee of the National Assembly issue Resolution No. 1023/NQ-UBTVQH13 and on September 14th 2015, the Prime Minister issued Decision 40/2015/QD-TTg regulating principles, criteria and norms for state budget development investment capital allocation for 2016-2020.

132. In the stage of allocation, main difficulties include:

a. No specific instructions on preparing investment guidelines and priorities. Upon selecting new investment projects for inclusion in the plan, various ministries, agencies and localities encountered difficulties due to the absence of consistent and feasible criteria for assessing and ranking projects. Some methodologies remain simple and mainly rely on qualitative assessment, even personal judgement, which prevents the selection of best projects.

b. Targeted support from the central budget (100% support) is only applicable to projects of category B or higher[71] (under Resolution No. 1023/NQ-UBTVQH13 and Decision 40/2015/QD-TTg). This restriction, however, has been questioned by localities as the number of Category-B projects is small (even 0), while category-C projects are dominant but receive no support. Some local governments have to adjust their directions for larger investment scale (to fit with threshold of Category-B projects). Consequently, this potentially causes investment wastages.

c. The priority order in allocation of fund, under Resolution No. 1023/NQ-UBTVQH13 and Decision 40/2015/QD-TTg, is as follow:

+ 1st priority: settlement of outstanding construction debts and repayment of advancement;

+ 2nd priority: Finished projects which receive insufficient funds;

+ 3rd priority: ODA reciprocal contribution and State capital for PPP;

+ 4th priority: Brought-forward projects;

+ 5th priority: Newly started projects.

The local governments were then concerned about having no newly started projects in 2016-2020 because of inability to mobilize funding, eventually affecting socio-economic development targets. Besides, for some localities, PPP remains relatively new and PPP planning takes time.

d. Regarding newly started projects, Article 55 of the Public Investment Management Law stipulates that only projects with approved investment guidelines can be listed in the medium-term public investment plan for allotted funding. Nonetheless, the time available for preparing and approving investment guidelines of newly started projects in 2016-2020 is quite short. At the local level, provincial People's Councils only meet twice a year; therefore, getting approval from People's Councils is hardly possible in the absence of quick submission. In fact, as of 31 October 2015, some provinces had no project approved by the provincial People's Councils.

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[71] These are large or key projects, with significant spillover impacts and inducement of local socio-economic developments, or inter-provincial and inter-regional projects.

Potential impacts of medium-term public investment plan on the restructuring of public investment.

Positive impacts

133. This plan of medium-term public investment under State budget has been the first of its kind, providing a comprehensive overview of public investment and capital mobilization for 2016-2020, especially availability of funds for settling outstanding construction debts, repayment for advancement, and reciprocal contribution to ODA at all levels.

134. Medium-term public investment planning enables ministries, agencies, and localities to know exactly the available funds for medium-term investment, so that they can actively allocate and make efficient use within 5 years. This ensures prompt implementation of projects and avoids shortage of funds from Central budget.

135. Discipling approval of investment guidelines prior to fund allocation - under Public Investment Management Law (Article 55) - has significantly changed the mindset of all line authorities and localities on the importance of preparation, particularly of investment guideline. At the central level, some particularly important projects have received guidance from leaders. The discretion in preparing proposals and approving investment guidelines has diminished remarkably. For example, in Vinh Phuc, the Department of Planning and Investment issued Document No. 391/SKHDT-TD dated 20 March 2015 guiding the formulation, appraisal and approval of investment intentions and decision, which clearly identifies authorized agency, process, procedures, profiles, etc. This lays an important first foundation for ensuring quality and efficiency of projects.

136. The 5-year allocation plan enhances publicity, transparency and responsibility of all line authorities and agencies in approving, deciding, allocating and mobilizing funds for investment, preventing corruption and wastages. As an evidence, various ministries and agencies argued against including some investment projects with guidance of Party and State leaders in the medium-term public investment plan because of excessive capital requirement.

137. Rules and disciplines in public investment management are strengthened. Strict implementation of medium-term public investment plan can help fundamentally settle outstanding construction debts and excessive advancement. According to the Public Investment Management Law, the line authorities and localities need to determine the amount of outstanding construction debts as of 31 December 2014, and no debts could be incurred beyond that time. Simultaneously, priority is given in the medium-term public investment plan to repay all these debts. Recently, various ministries, agencies and localities have dedicated efforts to significantly reduce outstanding debts.

138. The fragmentation and dispersion of investment gradually diminish. The medium-term public investment plan focused on national targeted programs, significant

national programs, prioritized programs[72]. The numbers of targeted programs have been reduced from 16 to 2 (at national level) and from 63 to 21 (at sub-national level). For new projects, the Central budget only fully finances projects of category B or higher.

Challenges in realizing positive effects

139. The afore-mentioned challenges and problems will significantly affect the restructuring of public investment, reflected in following aspects:

a. The structure of public investment in 2016-2020 hardly change due to shortage of funds for new projects. Many ministries and localities still incurred sizeable construction debts and advancement, and large number of unfinished projects such as Ministry of Transport, Phu Tho, Ninh Binh, Ha Tinh, Binh Thuan, etc. and will thus have no funds for newly started projects. Moreover, the allocation mainly relies on the implemented investment in the past (with annual growth of 10%; total investment for 2016-2020 is estimated at 6.72 times of that in 2015). Therefore, investment structure in 2016-2020 only varies insignificantly. Restructuring of public investment - in terms of capital, projects and priority - will be hardly implemented in 2016-2020.

b. The medium-term public investment plan still fails to thoroughly address the problem of "dual budgeting". The coordination between current expenditure planning and development investment planning remains problematic in certain aspects as follows:

- Medium-term public investment plan is yet to rely on the medium-term budget plan.
- Medium-term public investment plan is yet to take full account of impacts on current expenditures (such as post-investment maintenance and operation).
- Limited coordination and information sharing during the planning of mid-term public investment between Finance agencies and Planning and Investment counterparts.

c. In the absence of fundamental change in project appraisal and selection, public investment efficiency will hardly be improved. The shortage of standards in identifying investment guidance and evaluation criteria undermines the preparation, appraisal and approval of projects, and these may be no more than costly administrative procedures for related partners. Similarly, the provisions under Article 52 of the Public Investment Management Law on priority of public investment projects can hardly work.

[72] Including nuclear power project in Ninh Thuan, Son La hydropower project, Lai Chau Hydropower Project, Long Thanh Airport Project, Ho Chi Minh road project and a project to improve and upgrade Highway 1A.

d. Estimating the availability of funds for public investment in 2016-2020, especially those without sufficient predictability, is no easy task, which may necessitate amendment of the medium-term public investment plan. This issue can also undermine the process and outcomes of restructuring public investment.

e. The process of planning medium-term public investment still indicates excessive reliance on the higher-level state budget. Therefore, the awareness and modality of public investment management in general and public investment restructuring in particular may hardly improve in the near future.

f. Good quality and effective medium-term public investment plan for 2016-2020 requires the determination, bold measures, responsibility and close alignment with the Public Investment Management Law and related under-law guiding documents by ministries and agencies. The line authorities and localities still need to actively implement the relevant investment plans and related supporting measures, especially in building capacity for staffs.

IV. RECOMMENDATIONS

140. Vietnam enters the year 2016 with remarkable improvements and optimism. Macroeconomic stability is further enhanced. Economic growth has recovered noticeably from one quarter to another, with ample room for further improvement. Confidence of investors and the business community has become more vivid. A new government apparatus will be established soon, aiming at achieving socio-economic development objectives in line with reforms during 2016-2020. In this context, macroeconomic stabilization has so far served as the initial foundation. Vietnam should quickly implement deeper and broader reforms related to microeconomic foundations and the regulatory system in order to further facilitate business and production activities.

141. International integration process continues to deepen. Vietnam signed and implemented important FTAs with Korea and Eurasian Economic Union in 2015. The AEC was established in late 2015. The conclusion of negotiations of Vietnam-EU FTA and TPP – with expected ratification in 2016 – would mark a turning point in Vietnam's restructuring process. Accordingly, economic liberalization and international integration will not only help enhance access to foreign markets and resources. Instead, deeper commitments to liberalize trade and investment – even behind the borders – toward common high-quality, consistent and business-friendly rules of game would induce fundamental market-oriented reforms in Vietnam. These commitments are accompanied with various challenges and uncertainties; yet the benefits from prompt reforms and meeting requirements of major markets (such as the EU, the USA and Japan) are vast.

142. The opportunities from integration and domestic economic reforms are significant, but require efforts to materialize. The business community and the citizens may believe in Vietnam's potentials during integration process; yet those potentials would only become prospects and be realized in an appropriate policy environment. More specifically, the policy framework must undergo clear and relevant changes that are consistent with international commitments and development aspirations of Vietnam. At the same time, such policy framework must embody friendliness, encouragement and promotion of innovation, creativity and development of business community.

143. This Report re-emphasizes the priority of strengthening microeconomic foundations and reforming economic institutions for a modern market economy. Vietnam should proactively and substantially enhance the business environment via simplification of administrative procedures, reduction of burden to business, market liberalization, business facilitation. The country should also encourage and improve technological capacity for sustainable improvement of productivity. These lines of efforts should be made even before related commitments under economic integration arrangements.

1. Recommendations on further reforms of microeconomic foundations

144. Identify targets and priorities in addressing institutional and structural bottlenecks to promote economic restructuring and the shift of growth paradigm, aiming at

improving competitiveness. Concretize roles of the State and the market, and the State-market interactions in a modern economy.

145. Effectively implement fundamental laws of market economy, namely the Civil Code; the (amended) Law on Legal Normative Documents; the (amended) Law on the Organization of the Government; the (amended) State Budget Law; etc.

146. Effectively implement new regulations and laws, including (amended) Enterprise Law; (amended) Investment Law; Law on Personal Income Tax; Law on Value-Added Tax; Law on Special Sale Tax; Law on Natural Resource Tax; Law on Tax Management; etc.

147. Promote business environment reforms, aiming at facilitating production-business activities in line with Resolutions No. 19

    a. Study and examine methods to evaluate and rank competitiveness of international organizations; then identify specific measures to strengthen and increase rankings of improved indicators; prevent falls in ranking and quickly improve rankings of remaining indicators. Study and learn from international best practices of improving business environment and competitiveness.

    b. Improve regulations on business conditions to facilitate activities of enterprises, in line with international practices and requirements of economic integration. This will help improve competitiveness at enterprise, sectoral and economy levels.

    c. Concretize the need for comprehensively improving regulations on sectoral management of exported and imported goods. The key measures related to sectoral management include: (i) removal of unnecessary regulatory burden; reduction of objectives subject to sectoral management; reduction of documents, procedures and costs to implement related administrative procedures; (ii) application of IT, linking government agencies with customs; online provision of public administrative services; and (iii) shift to ex post control and risk-based management.

    d. Improve competitiveness of tourism and travel services to take advantage of the long coastal line with various natural landscapes and cultural heritages.

148. Review commitments under concluded or pending FTAs and international treaties of Vietnam in order to make relevant internalization attempts.

    a. Further review and develop a roadmap to reduce discriminatory and differential treatments (e.g., access to land and credit, Government procurement, etc.) that affect competitive neutrality between SOEs and private sector.

    b. Strengthen institutional and technical capacity of Vietnam Competition Authority (VCA) to ensure competitive neutrality between private firms and SOEs, and at the same time effectively deal with competition cases and trade remedies in line with international integration commitments.

c. Examine requirements on international regulatory cooperation to enhance capacity and adjust regulations in line with commitments.

d. Consult the business community, laborers and other social groups to appropriately prepare for FTAs and other international treaties.

149. State authorities should disseminate information on signed and pending FTAs of Vietnam to enterprises; support and instruct enterprises to participate in the integration process in order to realize opportunities, and to turn challenges into opportunities.

150. Appreciate and encourage domestic enterprises' dynamism, creativity and innovation, for instance: examine opportunities from FTAs; capacity to satisfy ROO requirements and participate in the value chain; capacity to study and cooperate with foreign firms; etc.

2. Recommendations of macroeconomic policies

* *Monetary policy:*

151. Assign highest priority to restructuring commercial banks and improving NPLs. Develop plan and targets for resolving NPLs in the coming years.

152. Consider phasing out of administrative targets related to monetary policy. Monetary policy should focus on stabilizing inflation (or core inflation) for a sufficient long period, accompanied with exchange rate management. Such objectives as the growth rates of outstanding credit and total liquidity should receive relatively less attention.

153. Avoid administrative push for reducing lending rate, due to the inherent pressure from further interest rate hikes by FED in 2016.

154. Consider phasing out of preferential credits for selected sectors or provinces. Disbursement of preferential credit should be accompanied with strengthening supervision and regulatory capacity in order to minimize distortions.

155. Closely monitor USD-denominated deposits in commercial banks, and in the BOP, to make suitable adjustments.

156. Regularly disseminate information on exchange rate management to the market. Monitor and reduce foreign-currency hoarding in entities and commercial banks. (Period-specific) Exchange rate stabilization remains important, but the US interest rate and USD price index should also be taken into consideration.

157. Flexibly manage liquidity of commercial banks to support credit activities, the issuance of Government bonds; provide for and respond to volatility of indirect investment flows (particularly when FED considers interest rate hike).

158. Efforts to restrain the participation of commercial banks in GB issuance will not be effective if fiscal policy remains dominant and, more fundamentally, if reducing state budget expenditures is under weak discipline.

** Fiscal policy:*

159. Conduct fiscal policy more prudently to reduce dominance over monetary policy. Seriously consider the sustainability of state budget deficit and public debts, crowding out effect on private sector, vulnerability of state budget expenditures in the context of integration, trade-off between economic growth and inflation, etc.

160. Consider minimizing petrol fees and taxes to support production-business activities of the private sector.

161. Reducing current expenditures will be effective only if actual number of staff under public payroll decreases. In the long run, a fixed state budget expenditure should be allocated to some specific activities of the public sector (instead of hiring regular staff first, then finding jobs and paying salary to them).

162. Ensure strict fiscal discipline and public investment management. Improving the efficiency of public investment appraisal and coordination is essential till 2020. The medium-term investment plan for 2016-2020 should avoid rapid disbursement of public investment projects during 2016-2017. This does not restrict new projects, even mega ones, but less necessary and less effective project(s) should be terminated.

163. Consider and announce medium and long-term plan to cut public debt. The options may be to gradually increase debt repayment, or allocate more (effective) investment resources in the medium term before dedicating resources for debt payment in the longer-term.

164. Develop and publicize feasible, specific and measurable indicators to evaluate the efficiency of public investment projects, particularly those that use Government bonds.

165. Consider, avoid further relaxing requirements on terms to maturity of newly issued Government bonds.

** Trade policy*

166. Quickly complete negotiations of, sign, ratify and enforce important FTAs to enhance effectiveness and benefits of FTAs. Harmonize commitments and related technical requirements (particular those related to ROO and agriculture). Improve institutions related to such areas as intellectual property rights, labour, environment, SPS, etc., facilitate the negotiation and implementation of trade and investment agreements.

167. Enhance awareness, information dissemination and consultation of the business community on content, opportunities and challenges, capacity to take advantage of trade and investment from signed and pending FTAs with the EU, TPP, Korea, the Eurasian Economic Union, AEC, etc. Effectively consult the business community during the negotiation of and preparation process for implementing TPP, RCEP and AEC.

168. Cooperate with partners to sign mutual recognition agreements, publicize requirements and technical barriers imposed on imported-exported goods, etc.

Facilitate trade across border; focus on infrastructure development, particularly transport infrastructure, seaports, airports, etc. Promote the connection of sectoral procedures to the national single window.

169. Enhance capacity of competition management, anti-subsidies, anti-dumping; settle trade disputes and issues of market management; and simultaneously provide legal support to enterprises. Consider participation in some international conventions to simplify procedures and paperwork for enterprises.

** Price policy*

170. Price reforms should not be restricted to amending direct management (frequency and extent of adjustment) of some products whose prices are controlled by the State (such as petrol, electricity, healthcare services, education). Instead, Vietnam needs more transparent efforts and accountability to enhance market competition and monitor cost structure and/or increase product quality. Avoid raising prices of those products and services during times of low inflation.

171. Consider keeping electricity price unchanged, so that the enterprises can take advantage of lower petrol price and stable inflation to recover business-production activities. Consider prompt electricity subsidy to help mitigate adverse impacts on poor households and targeted beneficiaries.

** FDI policy*

172. Encourage FDI projects to important sectors and industries in line with development priorities of Vietnam. FDI policy should be consistent with a more focused approach to industrial development, depending on advantages of each area and locality.

173. Promote investment from multinational corporations and enterprises in related supporting industries. Provide guiding information to domestic enterprises in order to prepare and cooperate with FDI enterprises.

174. Ensure disciplines in developing and managing plans. Avoid overuse of plans to realize existing investment ideas. Negotiate with foreign investors to ensure appropriate projects in line with industrial plans, international commitments, national security and defense.

175. Effectively consult FDI enterprises on related policy adjustments (including increasing minimum salary) to avoid exposure to dispute settlement under international treaties.

176. Develop human resources - particularly technical, skilled and high qualified workforce - to proactively receive transfers of technology and management know-how.

177. Ensure that FDI implementation relies more on foreign capital (i.e. disbursement via BOP) instead of domestic capital source.

3. Other related recommendations

178. Macroeconomic policy coordination exhibited early and significant improvements; yet room for further improvement prevails. Regularly review the effectiveness of

previous measures, adjustment requirements, etc. More serious attention should be placed on long-term issues, instead of mere temporary or technical issues.

179. Improving quality and accountability of statistical data remains an urgent requirement, particularly the consistency of statistical data on growth, production, investment and imports-exports. Institutionalize the development of indicators of economic cycle, inflation expectation, business and consumer confidence./.

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APPENDICES

Appendix 1: Policy adjustments in Q4/2015 and in 2015.

Serial No.	Content	Changes till the end of December 2015
1	Economic restructuring	1.1. Restructuring SOEs • Enterprise Law No. 68/2014/QH13 dated 26 November 2014 (taking effect from 1 July 2015) • Law on Managing and Using State Capital in Production and Business, No. 69/2014/QH13 dated 26 November 2014 (taking effect from 1 July 2015) • Document No. 1821/NHNN-TTGSNH dated 25 March 2015 on withdrawing SOEs' capital in joint stock credit institutions • Announcement No. 389/TB-VPCP on conclusion by Deputy Prime Minister Vu Van Ninh at the online conference on promoting SOE reform in 2015 (27 November 2015), which aimed at reviewing the SOE reform in the first 10 months of 2015 and setting objectives for the remaining 2 months of 2015. • Decree No. 60/2015/ND-CP dated 26 June 2015 on amending and supplementing a number of articles of the Decree No. 58/2012/ND-CP dated 20 July 2012 on stipulating in detail and guiding the implementation of a number of articles of the Securities Law and the Law on amending and supplementing a number of articles of Securities Law (taking effect from 1 September 2015) • Circular No. 129/2015/TT-BTC dated 24 August 2015 on guiding sequences and procedures for financial settlement to newly establish, reorganize and dissolve 1-member limited liability company owned by the State and 1 member limited liability company that is subsidiary of other 1 member limited liability company owned by the State (taking effect from 5 October 2015) • Decree No. 81/2015/ND-CP dated 18 September 2015 on information disclosure by SOEs (taking effect from 1 November 2015) • Decree on investing state capital to enterprises and managing, utilizing capital and assets in enterprises (draft) • Decree No. 87/2015/ND-CP dated 6 October 2015 on monitoring investment of state capital to enterprises; monitoring financial situation, evaluating operation results and publicizing financial condition of SOEs and state-invested enterprises (taking effect from 1 December 2015) • Circular No. 200/2015/TT-BTC dated 15 December 2015 guiding some contents related to supervision of state investment to enterprises, financial supervision, evaluation of operation results and dissemination of financial information of SOEs and State-invested enterprises.

		• Decision No. 41/2015/QD-TTg (dated 15 September 2015) on public and transparent selling share by batch to investors by State enterprises and corporations 1.2. Restructuring of the banking system and credit institutions • Circular No. 36/2015/TT-NHNN dated December 31, 2015 of the State Bank of Vietnam on restructuring of credit institutions through merger, acquisition, transformation of legal status that are imposed on related commercial banks, financial companies, individuals and organizations. • Circular No. 30/2015/TT-NHNN dated 25 December 2015 of the State Bank of Vietnam on regulations on issuing licenses, organization and operation of non-bank credit institutions • Circular No. 23/2015/TT-NHNN dated 04 December 2015 of the State Bank of Vietnam on amending, supplementing a number of articles of the Decree No. 581/2003/QD-NHNN dated 09 June 2003 of the State Bank Governor • Circular No. 18/2015/TT-NHNN dated 22 October 2015 of the State Bank of Vietnam regulating refinancing loans on the basis of special bonds of Vietnam Asset Management Company for Vietnamese Credit Institutions • Circular No. 33/2015/TT-NHNN dated 31 December 2015 regulating prudential ratio of micro financial institutions. 1.3. Power sector restructuring • Decision No. 14318/QD-BTC (taking effect from 25 December 2015) approving the project on restructuring Vietnam's power sector to support industrialization-modernization and sustainable development toward 2020, vision to 2030. The objectives are to attract investment capital from all types of domestic and foreign economic ownerships; reduce State investment; improve legal framework in order to promote competitiveness of the power sector; ensure stable and enough electricity supply at reasonable prices; encourage the development of clean and renewable energy; etc. • Circular No. 51/2015/TT-BCT dated 29 December 2015 of MOIT on amending and supplementing some articles of Circular No. 30/2014/TT-BCT dated 02 October 2014 of the Minister of Trade and Industry regulating methodology to set electricity price, procedures and sequences to check electricity trading contracts. 1.4. Agricultural sector restructuring • Directive No. 26/CT-TTg (dated 06 October 2015) on accelerating the implementation of the project on agricultural sector reform, aiming at improving added value and sustainable development. Main focuses are production innovation via strengthening coordination and linkage within the value chain, from production to consumption between farmers, collectives, coordination with enterprises, in which enterprises play the vital role. To guide and support farmers to establish new-style of

		collectives and production groups; to implement drastic measures in order to create favorable environment to encourage enterprises invest to agriculture, rural development and participation in chain association. • Announcement No. 10312/TB-BNN-VP dated 21 December 2015 on instructions of Minister Cao Duc Phat on promoting researches and policy recommendations to serve agriculture sector restructuring, aiming at improving added value and sustainable development.
2	Resolving NPLs	• Circular No. 14/2015/TT-NHNN dated 28 August 2015 on amending, supplementing a number of Circular No. 19/2013/TT-NHNN dated 06 September 2013 on providing the purchase, sale and handling of nonperforming loans by VAMC.
3	Stabilizing foreign exchange market	- In the context of strong appreciation of the USD against VND and other major foreign currencies, the SBV lowered USD-denominated deposit rate to 0% by Decision No. 2589/QĐ-NHNN dated 17 December 2015 in order to restrict the phenomenon of hoarding USD. - In line with the guiding from the SBV on fighting against dollarization, the SBV's Governor Nguyen Van Binh recommended that in the coming period, fees will be imposed on foreign-currency deposit, and central exchange rate will be changed frequently to prevent speculation phenomenon[73].
4	Restructuring public investment	• Law on Public Investment Management, No. 49/2014/QH13 dated 18 June 2014 (taking effect from 1 January 2015) • Decree No. 136/2015/ND-CP dated 31 December 2015 guiding the implementation of some articles of the Law on Public Investment • Document No. 10638/BKHDT-TH dated 30 November 2015 of MPI regarding schedule to approve the socio-economic development plan and medium-term investment plan for the 5-year-term of 2016-2020 and capital allocation for new projects in 2016. • Circular No. 39/2015/TT-BNNPTNT dated 20 October 2015 of MARD regulating the selection of investors for construction projects using public investment under the management of MARD. • Decree No. 77/2015/NĐ-CP dated 10 September 2015 of the Government on annual and medium-term public investment plan • Decree No. 15/2015/ND-CP dated 14 February 2015 on investment in the form of public-private investment (PPP) (taking effect from 10 April 2015) • Decree No. 84/2015/ND-CP dated 30 September 2015 on investment monitoring and evaluation, which replaces Decree No. 113/2009/NĐ-CP (taking effect from 20 November 2015) • Decree No. 87/2015/ND-CP dated 6 October 2015 on monitoring investment of state capital to enterprises; monitoring financial situation, evaluating operation results and publicizing financial

[73] http://cafef.vn/tai-chinh-ngan-hang/thong-doc-nguyen-van-binh-gui-ngoai-te-se-phai-tra-phi-20151228075609559.chn

		condition of SOEs and state-invested enterprises (taking effect from 1 December 2015) • Circular No. 38/2015/TT-BCT dated 30 October 2015 detailing some issues related to PPP investment under the management of MOIT. • Decree on managing Official Development Assistance capital (ODA) and preferential borrowings from foreign donors. (Draft)
5	Trade	- To be well prepared for international integration, the Prime Minister signed Decision No. 2528/QD-TTg dated 31 December 2015 on approving the Plan to implement and propose participation into treaties of the UN and ILO in labor – social areas in the period of 2016-2020 - Besides, several legal documents were issued to stabilize domestic and international trade, fight against smuggling and counterfeit, etc. • Document No. 13688/BCT-QLTT dated 31 December 2015 of MOIT on strengthening the management of MOIT, aiming at market and price stabilization and preventing smuggling, trade fraud and counterfeit during the Lunar New Year 2016. • Document No. 12415/TCHQ-GSQL dated 31 December 2015 of the General Department of Customs on implementing Decision No. 52/2015/QĐ-TTg dated 20 October 2015 of the Prime Minister on regulating border trade with neighboring countries. • Circular No. 216/2015/TT-BTC of the MOF guiding import-export tariff to implement bilateral trade agreement between the Social Republic of Vietnam and the People's Democratic Republic of Laos. • Circular No. 56/2015/TT-BCT dated 31 December 2015 of the MOIT regulating import by quota at the import tariff of 0% imposed on goods from the People's Democratic Republic of Laos • Circular No. 54/2015/TT-BCT dated 30 December 2015 of the MOIT regulating the list of goods to be traded and exchanged of residents at border areas. • Circular No. 53/2015/TT-BCT dated 30 December 2015 of the MOIT detailing the registration of imported, temporary import-re-export goods by foreign contractors in construction sector in Vietnam. • Circular No. 52/2015/TT-BCT dated 30 December 2015 of the MOIT regulating details of the trading of goods across borders in accordance with Decision No. 52/2015/QĐ-TTg dated 20 October 2010 of the Prime Minister on managing trade across borders with neighboring countries. • Decision No. 2770/QĐ-BTC dated 25 December 2015 of the MOF on introducing new/replaced/removed/unchanged administrative regulations related to customs procedures under the State management of the MOF.

Appendix 2: Evaluation of the market level of Vietnam's economy

	Criteria	Completion	Outstanding issue	Remarks
1	**Intervention of government in allocating resources and decision-making of enterprises**	**Met the standards of a market economy since 2010, according to the evaluation of EU delegation for ensuring the benefits of FDI enterprises). However, SOEs still have more competitive advantages than other sectors. Should take further reforms on economic institutions.**		
1.1	Price control	Gradually liberalize commodities under price controls such as gasoline, water, telecommunications, telephone based on market principles; exports control consistent with common practices: rice, wood and minerals.	Electricity tariff has not yet been competitive.	Has not yet reached the level of a market economy.
1.2	SOEs and the development of private sector	Gradually reduce the role of the state-owned sector; develop domestic private sector.		Already reached the level of a market economy.
1.3	A level playing field	Expand rights to do business, improve administrative procedures: Enterprise Law 2005, Investment Law 2005, (amended) Enterprise Law 2014, (amended) Investment Law 2014 are highly recognized and appreciated.		Creating a level “playing field” for different types of enterprises.
2	**Market distortions by state sector**	**Market distortions still exist despite some reforms of the state sector.**		
2.1	Impacts of SOEs	SOE restructuring has lessened impacts of SOEs on business environment.	The result of SOEs restructuring is still limited; no solution yet on economic activities of military sector.	Not yet equal competition between SOEs and other enterprises.
2.2	Land market	Land Law 2013 has shown remarkable improvement, basically resolving distortions of	Still imposing compensation to people; the rights of using agricultural lands are still limited; cannot accurately determine land	Land market still shows some problems.

		land market.	prices owned by SOEs; foreign investors have not been transferred the land-use rights, only have right to rent lands.	
2.3	Non-cash transactions	Almost get rid of barter transactions and non-cash transaction.	In agriculture, the implementation of land accumulation is a kind of non-cash transaction in land market.	Still exists monetary transaction in agriculture.
3	**Legal regulations ensuring the efficient and non-discriminative corporate governance**	**The accounting and auditing system has not met international standards, do not create a sound competition, order operation and predictability of economy. The judicial system lacks independence and effectiveness to ensure the market disciplines. Businesses lack confidence in the judicial system to protect their legitimate interests.**		
3.1	Accounting and auditing system	Building accounting and auditing policies: Amended Accounting Law in 2015, Independent Audit Law in 2012; State Audit Law in 2015; Vietnam's Independent audit sector has made significant progress.	The financial statements have low reliability; Accounting standards have not incorporated new international standards; the coverage of state audit is low;	Lack of effectiveness in enforcing accounting and auditing law, leading to common price transfer of FDI and large domestic enterprises.
3.2	Investor protection	Investor protection indicator increased thanks to the amended Enterprise Law 2014. The score reached 6.2 and ranks 52th (World Bank)		Minority investor protection indicator was similar to other economies in the region.
4	**Protection of intellectual property rights and the right to exit from market**	**Intellectual property rights are well protected in terms of the law, but enforcement is very weak due to lack of experienced and qualified staffs. In spite of significant progress since 2014, the insolvency and ordered exit from the market is still defective and fail to create breakthrough.**		
4.1	The judicial system		The reliability of enterprises on the judicial system remains low; enterprises rarely choose resolving dispute under court regimes. Ranking of legitimate state function (rule of law) by WB is -0.3/2.5; Ranking of Heritage for the integrity of the judicial system of Vietnam is 7/10	The judicial system in Vietnam is not effective enough to ensure that market rules are respected, the right to own property is protected effectively and

				contractual commitments are followed.
4.2	Bankruptcy	The amendment of bankruptcy law in 2014 overcame most of limitations of the bankruptcy law in 1993 and 2004.	The implication that SOEs are protected by the State and rescued when falling into bankruptcy created inequalities for non-state enterprises; the purchase of commercial banks at the price of 0 by the SBV eliminated entire responsibilities of related parties for causing losses, allowed managers/major shareholders to limit their losses before transferring their banks to the SBV which created inequalities for minority shareholders.	Inequalities in SOEs protection and treatment of bankrupt banks.
4.3	Protection of intellectual property rights	Vietnam has fully approved the conventions on the protection of IPR.	The enforcement of IPR regulation is poor due to lack of experienced human resource; Businesses are less likely to use the legal system to protect their IPR.	Do not fully protect IPR.
4.4	Protection of Competition	Competition Law in 2005; the establishment of Competitive Authority of Vietnam under the Ministry of Industry and Trade which have investigation function and National Competitive Council which have a function of judiciary.	Roles of Competitive Authority of Vietnam and National Competitive Council have been quite lackluster in recent years, while the phenomena of collusion, price fixing, preventing market entry are quite clear.	Have not protected competition.
5	Sound financial system, which is fully-supervised and independently operated.	Vietnam remains a strict state control on financial system. The State Bank of Vietnam not only plays a role of market surveillance but also has a role of market dealer. This is strongly influenced by the previous non-market one-tier banking system.		
5.1	Banking system		Vietnam financial market is still strongly influenced by a system of state-owned commercial banks - SBV holds dominant shares. Foreign investment is limited to invest in banks at 30% of charter capital, which is contrary to the principle of free-	The independence of Vietnam's banking system is very weak.

			market access.	
5.2	Banking system restructuring		The mechanism of handling bad debts through VAMC is not efficient and lacks transparency; the banking system pushed the entire burden of bad debt resolution to borrowers and depositors.	Restructuring the banking system is not effective.
5.3	SBV		SBV not only conducts the monetary policy and supervision of the banking system, but also directly intervenes in the business activities of commercial banks.	Do not meet the principles of two-tier banking system in a market economy.
5.4	Currency conversion		Foreign currency transactions in the parallel market, in principles, are not legally recognized, which creates additional risks and injustices for people participating in this market, and advantages for those who are able to access formal foreign exchanges.	Converting currencies is not free.

Source: Authors' compilation.

Appendix 3: Macroeconomic statistics

	Unit	*2010*	*2011*	*2012*	*2013*				*2014*				*2015*			
					I	***II***	***III***	***IV***	***I***	***II***	***III***	***IV***	***I***	***II***	***III***	***IV***
GDP growth																
Overall	%	6.4	6.2	5.2	4.8	5.0	5.5	6.0	5.0	5.4	6.4	6.8	6.0	6.5	6.8	7.0
Trade																
Growth rate of exports	%	26.5	34.2	18.2	17.5	13.6	14.8	15.6	12.2	15.7	13.6	11.6	8.8	10.6	9.2	4.5
- *FDI sector*	*%*	*41.2*	*40.3*	*33.7*	*27.9*	*28.4*	*26.2*	*23.6*	*18.2*	*16.1*	*37.5*	*28.3*	*18.7*	*21.5*	*22.0*	*9.6*
Growth rate of imports	%	21.3	25.8	6.6	14.8	17.0	14.2	18.0	10.4	10.5	14.0	13.7	20.1	14.2	11.6	3.3
- *FDI sector*	*%*	*41.8*	*32.1*	*22.7*	*26.1*	*25.9*	*25.4*	*19.9*	*14.6*	*7.3*	*8.2*	*24.3*	*27.1*	*20.3*	*18.4*	*1.7*
Exports /GDP	%	63.4	72.6	73.5	89.1	81.4	79.7	65.1	92.8	86.6	82.5	67.7	96.3	92.8	87.0	69.7
Money																
M2 growth (YoY)	%	33.3	12.1	18.5	3.8	3.4	2.8	7.7	2.8	4.1	2.9	6.7	2.4	3.6	3.7	3.3
Credit growth (YoY)	%	32.4	14.3	8.9	1.2	3.5	2.1	5.3	0.5	3.2	3.5	6.3	2.7	5.1	2.7	6.5
Interbank VND/USD exchange rate (average)	Dong	18630	20532	20828	20828	20831	21036	21036	21036	21063	21246	21246	21446	21593	21773	21890
Investment																
Investment/GDP	%	38.5	33.3	30.5	29.6	29.6	33.8	33.2	28.4	31.5	33.0	30.6	30.4	31.7	33.2	33.6
Implemented FDI capital	Bil. USD	11.0	11.0	10.0	2.7	3.0	2.9	2.9	2.9	2.9	3.2	3.5	3.1	3.3	3.4	4.8
Other indicators																
Inflation (YoY)	%	11.8	18.1	6.8	6.6	6.7	6.3	6.0	4.4	5.0	3.6	1.8	0.9	1.0	0.4	0.6
State budget deficit/GDP	%	5.5	4.9	5.4	5.4	5.0	5.3	4.7	4.9	4.6	5.3	7.3	4.6	6.4	3.9	-
Current account	Bil. USD	-4.3	0.2	9.1	2.6	1.3	3.5	1.7	2.7	2.7	2.8	0.8	-1.3	0.7	0.7	-
Balance of payment	Bil. USD	-1.8	1.2	11.9	3.0	-3.3	-0.8	1.7	7.9	2.2	0.9	-2.6	2.7	0.6	-6.6	-

Source: Authors' compilation.