

# Is Vietnamese Economic Growth Hot?

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## 1. From a WB survey of developing economies

Recently, some people have argued that the Vietnamese economic growth was hot. They said that Vietnam, as an economy in transition with a low starting point was experiencing wide fluctuations in the foreign exchange and monetary markets that were signs of a hot economic growth. In my opinion, such an argument lacks scientific and practical grounds. It isn't easy to determine whether the economic growth is hot or not. Because governments of many countries will take action when an economy is considered as hot in order to bring it under control again. If the Vietnamese economic growth is hot, the SBV will certainly increase the interest rate to make it cooler. A hot economic growth will lead to a bubble economy that can burst any time. The 1997 financial crisis in Asia was a good example of the failure to realize hot signs of the economic growth. How

Table 1: Macroeconomic achievements in periods of huge capital inflow

Nation	Period of capital inflow	Annual growth rate (%)	Annual Inflation rate (%)	Current account (a)	Average REER (b)
Argentina	1991-1994	9.1	-801.1	1.8	91.7
Brazil	1992-1995	3.1	-93.5	0.6	7.4
Chile	1989-1995	5.7	-4.1	-4.9	-25.5
Colombia	1992-1995	1.6	-4.8	4.9	14.7
Hungary	1993-1995	7.5	-5.5	9.8	18.9
India	1992-1995	-0.7	0.1	-1.2	-30.8
Indonesia	1990-1995	2.2	1.3	0.2	-29.4
Korea	1991-1995	-2.5	0.8	5.0	4.4
Malaysia	1989-1995	4.0	1.4	2.9	-24.5
Mexico	1989-1994	2.9	3-74.4	7.1	20.0
Morocco	1990-1995	-3.3	0.1	0.1	-6.5
Pakistan	1992-1995	-2.3	1.7	0.9	-9.0
Peru	1990-1995	3.3	-79.1	1.4	120.9
Philippines	1989-1995	2.2	-3.1	0.7	-10.7
Poland	1992-1995	8.5	-146.7	3.9	37.9
Sri Lanka	1991-1995	2.0	-2.2	-0.2	0.6
Thailand	1988-1995	3.9	-1.1	2.3	-18.9
Tunisia	1992-1995	0.5	-2.2	3.7	0.6
Turkey	1992-1993	1.4	5.0	1.4	1.0
Venezuela	1992-1993	-5.0	-2.7	14.6	9.8
Vietnam <sup>(c)</sup>	1999-2003	7.0	4.0	3.5	100

(a) as % of the GDP. The minus symbol means an improvement in the balance of payments on current account.

(b) Percentage of change in the real effective exchange rate. A plus means a rise in prices.

(c) Numerical data calculated here are based on official statistics and IMF data about the VND real exchange rate. According to our calculation, the index of real exchange rate to the value of 100 equals its equilibrium in 1999

can we identify an economic growth as hot?

Researchers from the World Bank have publi-

cized their initial conclusions after studying four variables: high growth rate, huge deficit in the

balance of payments on current account, accelerated inflation and high real effective exchange rate.

A hotly developing economy usually involves high growth rates and accelerated rates of inflation. Countries included in the Table 1 didn't revealed systematic patterns of the accelerated inflation, worsened balance of payments on current account and increased real exchange rate. With each variable, half of surveyed countries obtained results that could be seen as too hot. In addition, in each country, all four indicators didn't change in the direction usually found in a hotly developing economy. For example, one country





had higher growth rate but its inflation rate was lower. Moreover, no variable proves to be too hot among countries that received the biggest capital inflow. Mentioning this fact, we wanted to say that it's dangerous when the government had no instrument and method for inspecting the hot growth and taking measures in time to deal with it, because we would become too assured when thinking the Vietnamese inflation rate was too low to lead to the hot growth: The inflation rate has been under 4% and the growth rate 7% as

something unwanted and caused deficits in the balance of payments on current account. Thirteen countries in the survey have succeeded in reducing the inflation rate during the period of capital inflow. Five of them have obtained great reductions.

Great capital inflows didn't certainly lead to increases in the real exchange rate because only 12 countries experienced such increases in the periods of capital inflow. In this group there was no Southeast Asian countries while seven South American countries saw their

surveyed countries reduced their deficits and Chile could only keep a curb on its deficit.

The real exchange rate and balance of payments on current account tended to change in the same direction. Most countries that experienced great increases in the real exchange rate also witnessed great deficits in the balance of payments on current account.

Thus, all surveyed countries have avoided symptoms of the hot economy. With four countries obtaining very high growth rates and one coun-

change rate tended to lead to deceleration of the inflation rate.

## 2. To the Vietnamese economic growth

Above analyses allow us to say that, two out of four variables (overestimated real exchange rate and huge deficit in the balance of payments on current account) could be used by the Vietnamese government to inspect for signs of hot development when Vietnam is receiving capital inflows and trying to integrate into the world economy. Thus, we didn't agree with the argument that acceleration in the inflation in developing economies always reflected the hot development, although it is an important indicator of this situation. According to our calculation based on data publicized by the IMF, the index of the real exchange of the VND up to 2003 is 100 if we take 1999 as the base year, that is, the VND is priced in parity with currencies of our trading partners. In spite of such a real exchange rate, the IMF predicts that the deficit in the balance of payments on current account in the coming years will rise to some 4% of the Vietnamese GDP, higher than deficits of surveyed countries. This isn't a surprise in economies in transition like Vietnam. However, the Vietnam's inflation rate is low and the Vietnamese government is considered by the IMF as good at controlling the inflation, we think that the economic development in Vietnam isn't hot, especially when the real exchange rate returns to its equilibrium, not to mention the fact that the interest rate in Vietnam tends to lower like interest rates all over the world. However, falls in the interest rates are signs of a recession of the world economy that will certainly affect Vietnam's economic growth. ■



required by the National Assembly for years.

Of countries with the highest growth rates, there were Argentina, Hungary, Peru and Poland: two economies in transition and two experiencing changes in its macroeconomic policies. In these countries, high growth rates and huge capital inflows interacted with a third factor: changes in economic policies. This explained why they faced highly decelerated inflation in this period. Experience shows that the accelerated inflation could be seen as a direct symptom of the hotly economic growth because it is

real exchange rates increase considerably, especially Argentina, Colombia, Mexico and Peru. In addition, increases in the real exchange rate apparently didn't lead to acceleration of the inflation rate. Of 12 countries where increases in the real exchange rate were registered, two countries witnessed their inflation rate reduced. This was apparent in Argentina, Mexico and Peru.

Unlike the inflation, the deficit in the balance of payments on current account could be affected by the capital inflow. In periods of great capital inflow, only three among 20 sur-

veyed countries (Brazil) suffering hyperinflation, factors behind these facts were unusual, visible and not attributable to increases in the capital inflow. Great increases in the inflation – the most visible sign of the hot growth – was almost absent in these countries, although the inflation pressure was on the increase in East Asian recipients of foreign capital. In many countries, increases in the real exchange rate seemed to originate from policies on the exchange rate, not from the capital inflow. This remark was supported by the fact that increases in the real ex-