A PREDICTION OF 2003 INFLATION RATE

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The NA Resolution of socioeconomic targets for 2003 wants to keep the rise in the price index under 5%, but it has increased by 2.5% by the end of April equaling 50% of the target. It's estimated that it will rise slightly in May. In the rest of 2003, may it exceed the limit set forth by the NA?

Growth and inflation rates are two important targets all governments are concerned about. If both of them are high, the economic development will be of less significance. If both are low, the economy suffers a poor spending power. In fact, few economies achieve both of two targets satisfactorily. In macroeconomic management, governments of either developed countries or transition economies have to ensure the growth rate at the expense of the inflation rate if they want to help the economy recover, or ignore the growth rate target and keep the inflation rate low when the economy is too hot.

In Vietnam, if the inflation is high and prolonged, consumers, wage earners and pensioners will suffer because the wage rise will be meaningless if the price index rises accordingly because consumers have to spend more on their needs. However, if there is deflation and the economy doesn't grow, the living standard will reduce.

In the past four months, the price index rose remarkably in January and February, the New Lunar Year, but it fell by 0.6% in March and stayed 0% in April. In the Lunar New Year, the spending increased causing the price index to rise. This happens every year.

On closer examination of rises in prices of goods and services from December 2002 to April 2003, we see that the highest increase was found in pharmaceuticals, 12.2%, The main cause is the fact that Vietnam has to import drugs or raw materials for producing them. Their prices rose on the world market because the euro rose against the dollar and prices of petrochemicals were higher.

The next was building materials with an increase of 3.4%. Besides the fact that the demand for construction service increased, another cause was the increase in the price of imported steel on the world market. Other building materials became dearer because they are imported or made from imported raw materials.

Other goods and services with high increases in their prices were transport and foodstuff because of imported fuel was dearer with the result that the Government had to adjust the retail prices of fuel. At present, the oil price on the world market has reduced but the Government didn't cut the retail prices of fuel and it cut the import duty instead, so the prices are still high in comparison with the past four months. Rises in prices of foodstuff are due to increases in demand on both domestic and foreign markets.

Similarly, the price of gold rose by 5.9% because of changes in the world price and imported gold accounts for 97% of the local market demand.

Thus, we can at first affirm two causes of the remarkable increase in market prices in the first four months of 2003: (1) increases in prices on the world market affect the domestic market, and (2) the demand on the domestic market rises because of pay rises for wage earners and the Government's policy to stimulate the market demand. These are objective factors beyond the will of policy makers.

Under the market mechanism, one usually thinks of the monetary factor as a cause of rises in the price index, but analyses of the economic development in the past few months show nothing for us to worry about.

In the first two months, before the New Lunar Year, the demand for cash increased when the salary and bonuses were paid to laborers, companies made payments to suppliers and the public withdrew money from banks to purchase goods needed for the New Year Day. Thousands of billions were supplied through commercial banks, open market operations, swap dealings, etc. the increase in the money supply was a response to the need for more spending of the public. However, from mid-February till now, thousands of billions were sent to the central banks through open market operations and other channels. As for commercial banks, they kept putting thousands of billions more in T-bills in order to make the best use of bank deposits because these investments have high liquidity. Thus, the circulation of money through banks under the control and supervision of the central bank was smooth and in accordance with principles of the market economy and changes in the market forces. It's also worth noting that interest rate of all kinds (refunding rate, discount rate, open market rate, etc.) increased remarkably in the first months of the year under effects of changes in the supply and demand relation on the money market. This means that the central bank doesn't always meet the demand for cash with the result that commercial banks have to find ways to attract idle money from the public.

In the first months of the year, the money market really became hotter. All commercial banks launched programs to issue bonds and certificates of deposit with attractive interest rate. But their effort aims at restructuring their sources of capital and securing more medium- and long-term capital needed for major development projects. At present, the deposit rate offered by banks stays rather high while bonds are issued in large quantities by commercial banks, Corporation of Oil (Petro bonds) and the Ministry of Finance (Education bonds), etc. They are noticeable signs that make the money market hotter and lead to higher inflation rate in the coming months.

Thus, the monetary factor isn't the main cause of rises in the price index in the first two months of the year but it will play an important role in the time to come. Experience shows that from now till the end of the year, the price index hardly makes any increase and it may fall slightly. If nothing happens unexpectedly, the increase in the price index and the inflation rate will be under the planned limit. It's necessary to keep a close watch on the situation to regulate the money supply to meet the targets of controlling the inflation and growth rates.■