ON THE CONTROL OVER FISCAL AMBITIONS

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The world economy thus far has witnessed crises of private debts, public debts, and economic recession in many countries in the America and Europe. For example, the early 2007 saw the collapse of the realty market and then in 2008 the massive bankruptcy of banks (i.e. Lehman Brothers on Sept. 17, 2008), insurers, and automobile companies in the USA leading it to a deep recession. Besides, EB and IMF respectively sponsored around €110 billion and €90 billion so as to tackle public debt crises and budget deficits having taken place in Greece in 2009 and Ireland in 2010. Portugal, Spain, and even France and Italy have also shown signs of fiscal volatility.

Such the aforementioned facts are of course not sufficient to negate the big role of the government in enhancing the economic growth, environmental protection, and securing social welfare. Yet, if we exagerate effects of the government without having a comprehensive look at the cooperation between the government and the private sector throughout these incidents, the market is just a stage for a one-man show. Long-term and uncontrollable dangers will arise from this show of the government. Therefore, this paper aims to discuss the government's ambition in its fiscal policies (fiscal ambition) which sometimes derives from subjective perspectives on the government's role with the result that the government fails to run the national economy and low-income workers or pensioners will inevitably face tax burdens.

After summarizing two schools of economics about fiscal policies, the paper will focus on three sections. The first section considers the rise in public expenditure and budget deficit of governments in EU27 and the USA within the recent period. The second section analyzes Vietnam's fiscal policies from 2004 to 2010. The last section suggests some solutions to control over fiscal ambition in Vietnam, especially the implementation of medium-term expenditure framework.

Keywords: fiscal ambition, public debt, budget deficit, expenditure framework

1. Two schools of economics about effects of fiscal policies on the economy

Neoclassical economics states a fiscal policy is completely impotent, that is, it does not impinge on GDP, employment and real interest rate. Accordingly, budget overspend does not affect the national economy due to the fact that its crowding-out effects cause the reduction in private investors. Thus, if the government does not increase taxes but instead takes out a loan to make up for budget deficit, people must live frugally because they understand that the government will increase taxe rates in the near future to pay interest on governmental loans.

The Keynesian school, however, believes that fiscal policy can reduce fluctuations in aggregate demand. It implies that the government can proactively increase its budget spending (or even budget overspend) when the economy is contracting (see Figure 1a), and tighten its spending when there are signs of inflation (see Figure 1b). Recently, Keynesian theories have been supported by an extreme argument that a

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deep economic recession helps eliminate impotent economic entities, resulting in a healthier economy and society.

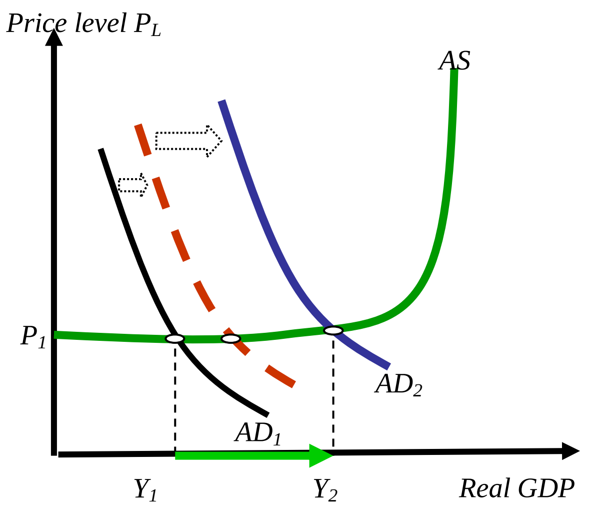

Figure 1a: Open fiscal policy

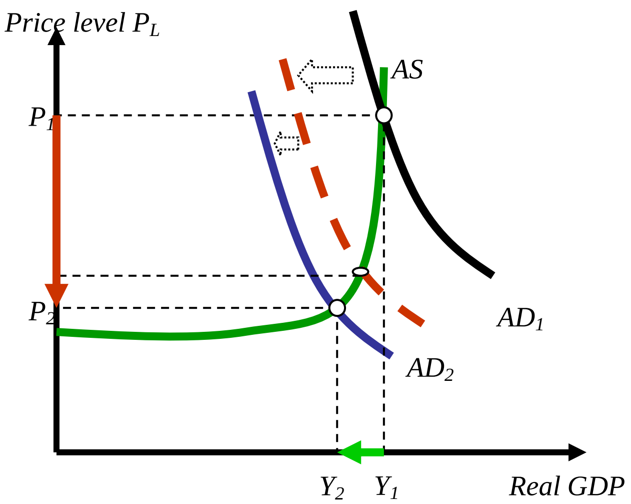

Figure 1b: Constrained fiscal policy

2. Fiscal deficit and public debts in some countries in the period 2005-2010

The ratios of budget spending to GDP in the USA and some West European countries are among the highest in the world. During the past five years, this ratio in the USA has incessantly risen from 21.2% in 2005 up to 25.9% in 2009. The governmental spending in the EU27, in 2009 alone, reached 50.8%, whereas the budget income was just some 44% of GDP. Among EU members, Portugal, Ireland, Italy, Greece, and Spain (PIIGS group) have shown a tremendous public expenditure and the expansion of governmental spending over time (see Table 1).

Table 1: Ratio of governmental spending to GDP (%)

	2005	2006	2007	2008	2009
EU					50.8
Spain	25.0	24.9	25.1	26.4	
Germany	31.3	30.1	28.9	28.7	
Ireland	30.7	30.9	32.1	37.2	
Austria	40.2	39.7	38.8	38.4	
Italy	39.2	39.6	39.3	40.3	
Netherlands	39.3	40.4	40.2	40.5	
Belgium	44.4	41.1	41.0	42.5	
United Kingdom	41.2	40.3	40.1	42.7	
Portugal	43.3	42.2	41.6	42.9	
France	45.8	45.1	44.4	44.7	
Greece	41.8	40.8	42.4	46.4	
Asia					
Bangladesh	9.4	9.7	10.1	10.9	
Singapore	12.8	13.4	12.4	14.5	
India	14.9	15.1	15.3	15.4	
Philippines	17.9	17.5	17.2	17.0	
Thailand	16.4	16.1	17.6	18.2	
Sri Lanka	20.2	21.1	20.0	19.2	
Korea, Rep.	19.7	20.5	20.1	20.0	
Others					
Canada	18.0	17.6	17.8	17.7	
United States	21.2	21.1	21.4	23.0	25.9
Brazil		25	24.2	24.1	
Australia	25.7	25	24.5	24.4	

Source: IMF, WB, OECD retrieved from http://data.worldbank.org/indicator/GC.XPN.TOTL.GD.ZS/countries

The rise in public expenditure forces governments to resort to budget deficit. Accordingly, budget deficit has crossed the border of a country to spread out to the world. Table 2 shows budget deficits in Europe, Asia, and America in 2005-2010. In 2009 alone, the whole EU did suffer a deficit of 6.8% as compared to the 2.3% in the previous year; and no EU members could attain a budget surplus. Particularly, in countries with public debt crisis, budget deficit rose rapidly (double) and public debts represented over 90% of GDP, making governments insolvent.

Table 2: Ratio of budget deficit to GDP in some countries in 2005-2010

	2005	2006	2007	2008	2009	2010
EU				- 2.3	-6.8	
Greece	-5.3	-3.1	-4.0	-7.8	-15.4	
Ireland	1.4	2.8	0.5	-7.0	-14.4	-32.0
United Kingdom	-2.9	-2.6	-2.6	-4.7	-11.4	
Spain	1.3	2.0	2.4	-2.0	-11.1	
Portugal	-5.8	-4.0	-2.6	-2.7	-9.3	
France	-2.8	-2.1	-2.3	-3.0	-7.5	
Italy	-3.5	-2.1	-1.6	-2.5	-5.3	
Belgium	-2.7	0.3	-0.6	-1.1	-6.0	
Austria	-1.9	-1.7	-0.9	-0.7	-3.0	
Germany	-2.3	-1.2	-0.3	-0.2	-3.0	
Asia						
Sri Lanka	-7.0	-6.9	-6.5	-6.6		
India	-3.2	-2.2	-1.0	-1.5		
Philippines	-3.0	-1.3	-1.5	-1.3		
Bangladesh	-1.1	-1.4	-1.3	-1.0		
America						
United States	-2.8	-1.8	-2.2	-5.4	-9.9	-10.2
Brazil		-2.9	-1.9	-1.2		

Source: IMF, WB, OECD, and EU as retrieved from http://data.worldbank.org/indicator/ and http://epp.eurostat.ec.europa.eu/cache/

Besides, in order to avoid the domino effect made by the collapse of the USA realty market in 2007, governments and multilateral organizations have incessantly released fiscal rescue or demand stimulating packages in hope of pulling economies out of recession. This raises the budget deficit and the ratio of public debts to GDP. The 2009 public debt ratio of EU did shoot up 74% from 61.8% of the year 2008; and that of PIIGS group was the highest. In 2010, the ratio of public debts to GDP in Greece and Italy was the highest in the EU (see Table 3). In the same year, Vietnam's public debt ratio to GDP did exceed the threshold of 50% reaching the 42nd place in the world and 1st position in the Southeast Asia, and the credit rating for long-term loans in local/foreign currency and for foreign-currency bonds fell to B+ from BB- by Fitch.

Table 3: The ratio of public debts to GDP in some countries in 2010

Rank	Country	%
1	Japan	225.8
5	Greece	144.0
6	Iceland	123.8
8	Italy	118.1
9	Singapore	102.4
10	Belgium	98.6
11	Ireland	94.2
13	Sri Lanka	86.7
14	France	83.5
15	Portugal	83.2
19	Germany	78.8
23	United Kingdom	76.5
25	Austria	70.4
26	Netherlands	64.6
27	Spain	63.4
31	Brazil	60.8
34	World	59.3
37	United States	58.9
42	Vietnam	56.7
43	Philippines	56.5
45	India	55.9
49	Malaysia	53.1

51	Argentina	50.3
52	Pakistan	49.9
55	Norway	47.7
56	Denmark	46.6
58	Finland	45.4
62	Thailand	42.3

Source: (https://www.cia.gov/library/publications/the-world-factbook/rankorder/2186rank.html

In sum, it is possible to summarize causes of economic recession in the USA and EU as follows:

- Governments employed the open fiscal and monetary policy without any prudential supervision, causing their budget deficit to reach a record high.

- The collapse of realty market in the world caused by speculators had cornered the market, and local people were over-optimistic about the future of the economy as well as from the strong backup of the credit system.

- Governments did not stringently control the operation of intermediate financial institutions (i.e. banks, insurers, and investing companies, etc.). As Alan Blinder from Princeton University put it, FED did not try its best in prudential supervision which is supposed to be a function of a central bank.

- Some countries (i.e. Greece) concealed stats about national accounts; others even did not accept the fact of being in fiscal crisis, expecting supports from international organizations (i.e. Ireland).

3. Vietnam's fiscal operation over the period 2004-2010

Many expenditures related to Vietnam's fiscal policy, if compared to Greece and Ireland, have not been at risk. Being a transition economy with a small-cap private sector that lacks capital and state-of-the-art technologies, Vietnam's government must invest in keynote projects (such as traffic networks, power generation, and essential industrial facilities, etc.) so as to pave the way for industrialization and modernization. Nonetheless, the rapid expansion of public expenditure, if not strictly controlled, might put the economy at risk.

The government's fiscal ambition is evident in: (1) a rise in regular expenditures, (2) budget deficit lasting in 10 consecutive years, (3) many over VND10,000 billion worth of keynote projects and the birth of national target programs, and (4) the continuous rise in public debts.

a. Regular expenditures are rising in both absolute value and ratio:

Regular expenditures have been rising both in level and percentage. The ratio of regular spending soared to 64.7% in 2010 from the 47.9% in 2004. The 2005/2004 growth rate was 22.5% which then climbed to 35.6% in 2010/2009 (see Figure 2).

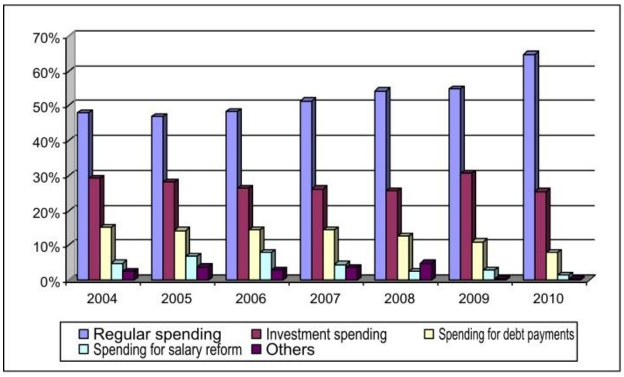

Figure 2: Budget expenditures in 2004-2010

Source: Vietnam's Ministry of Finance

b. Constant budget deficit:

Over the past twelve consecutive years, budget expenditures have been larger than budget income and shown an upward trend. Figure 3 reveals budget expenditures and income from 2004 (when the Law on State Budget 2002 came into effect) to 2010.

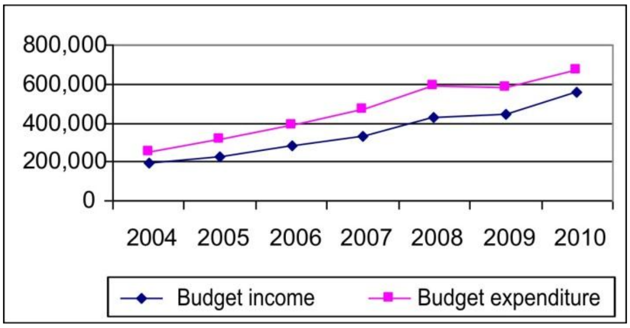

Figure 3: Budget income and expenditure in 2004-2010

Source: Vietnam's Ministry of Finance

Together with the budget deficit, there are two rather unusual fiscal phenomena.

- ***Firstly***, the local budget surplus is on the rise. If we merely take the relationship between obligatory budget spending and budget incomes into account, the central budget will definitely not be in deficit. The deficit in central budget derives from financial supports for local budgets. In the period 2004-2010 alone, such the financial supports represented 37.2% of the total national budget spending. The local budget surplus in the same period equaled 33% of the national budget deficit.

- ***Secondly***, balances carried forward are growing. There are two types of balances: (1) balance carried over from salary and payroll reforms, and (2) spending from funds of the current year brought forward for balancing the account in the next year and the balance carried down serving as obligatory expenditures. These balances represent a percentage increase from 2004 to 2009 (i.e. 13.85%, 16.20%, 20.12%, 18.91%, and 23.35% respectively).

c. The birth of many over VND10 trillion keynote projects and national target programs:

Since the national project of 500kV North-South Power Transmission Line was officially commenced on April 5, 1992, Vietnam has been implementing many other heavily-invested projects (see Table 4).

Table 4: Heavily-invested projects

Projects	Real cost	Estimate
Cà Mau Gas-Power-Fertilizer	US$2.2bn	
Bà Rịa-Vũng Tàu Gas-Power-Fertilizer		US$6bn
Dung Quất Refinery	US$3.1bn	US$2.5bn
Sơn La Hydroelectric Plant		US$1.5bn
Hồ Chí Minh Highway		US$2.5bn
Hà Nội – Hải Phòng Highway		VND24 trillion, commenced in 2009
TP HCM – Long Thành – Dầu Giây Highway		VND18,884 billion, commenced in 2009
Nội Bài – Lào Cai Highway		VND19,984 billion, commenced in 2009

Source: Vietnam's Ministry of Planning and Investment

Vietnam's government has recently become concerned with projects whose invested capital is larger than 1% GDP. For example, the government has surveyed and planned many large projects worth billions of US dollars; however, they have not been implemented due to controversial opinions. It is possible to exemplify some like North-South High-Speed Rail estimated to be worth about US$56.3 billion, two US$14-billion nuclear power stations, Đăk Nông Bauxite Project costing US$2 billion, and US$5-billion Long Thành International Terminal, etc. Such projects require abundant resources, and if the execution takes longer than expected, it can raise the real cost.

Additionally, Vietnam has had 15 national target programs up to 2011, namely (1) Employment, (2) Poverty Alleviation, (3) Fresh Water and Environmental Hygiene in Vietnam Rural, (4) Healthcare, (5) Population and Family Planning, (6) Food Hygiene and Safety, (7) Culture, (8) Education and Training, (9) Drug Prevention, (10) Crime Prevention, (11) Economical and Effective Use of Power, (12) Climate Change Adaptation, (13) Modern Rural Vietnam, (14) HIV/AIDS Prevention, and (15) Information Service in Remote Areas. The costs of national target programs ~~is~~ are not as large as that of major projects but the ability to control their performance is not fully attended to.

d. An incessant rise in public debts:

As ranked by CIA, Vietnam's public debts reached 52% in 2009 and climbed to 56.7% in 2010. If we just consider government's foreign debts and government-sponsored foreign debts, the figure constantly rose from US$9.41 billion in 2002 to USD29 billion in June 2010, amounting to roughly 30% GDP (see Figure 4).

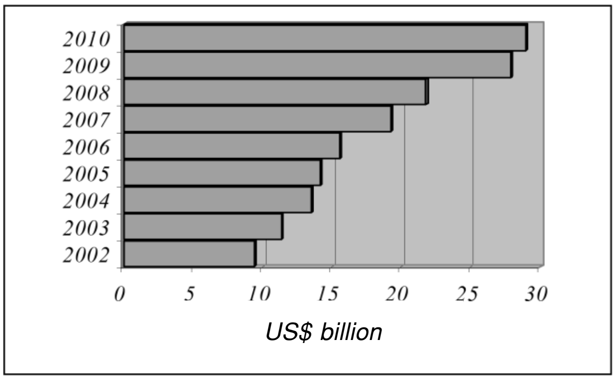

Figure 4: Total government's foreign debts and government-sponsored foreign debts

(US$ billion)

Source: Debt Bulletin No.1-6, Dept. of Debt Management and External Finance, Ministry of Finance.

The rise in foreign debts and devaluation of local currency, if not stringently controlled and effectively employed, will definitely generate a burden of enormous principal and interest payments on next generations.

In sum, if fiscal ambition is not strictly controlled and an appropriate spending routine is not worked out, it is possible that:

- The private sector can hardly gain access to credit sources in the long run, and thereby hindering its development. Thus, to enhance the performance of the private sector, the government is forced to increase its investment; yet then the private sector might be overwhelmed by public sector and become weaker. This vicious circle is also worrisome.

- The government itself has difficulties in accessing to international credit sources when its credit rating falls to B+.

- The national budget is too small to finance projects punctually, and thereby extending the implementation term and raising the real costs.

- The output efficiency of major projects (such as Long Thành International Terminal, North-South High-Speed Rail, etc.) is hard to gauge. The output of national target programs is unclear.

4. Recommendations

In order to control fiscal ambition, besides basic remedies employed by the Ministry of Finance such as tight fiscal and monetary policies, the followings are worth considering:

- The nationwide implementation of medium-term expenditure framework should be at the fore.

- The development of the private sector should be facilitated by public-private partnership. Enhancing the role of the private sector may stimulate the sustainable economic growth and generate jobs.

- Impose taxes on individual property as soon as possible and perfect provisions on personal income tax with a view to: (1) soothing away dependence of budget on incomes from crude oil and customs duties, and (2) broadening the tax base with low elasticity and bridging the gap between budget income and expenditures.

- Reduce and gradually eliminate the practice of using the government as the intermediary in obtaining foreign loans for state-owned enterprises.

- Besides, the government synchronously implements non-fiscal remedies such as controlling the realty market, supervising the operation of intermediate financial institutions, etc.

The medium-term expenditure framework is not a new fiscal tool and it has been employed by many countries in EU and other continents. This tool has recently been piloted in Vietnam. In 2006 and 2008, the Ministry of Finance released two circulars that instructed six ministries (i.e. Ministries of Finance, Planning and Investment, Education and Training, Public Health, Agriculture and Rural Development, and Transportation) and three regions (HCMC, Bình Dương Province, and Vĩnh Long Province) to experiment the medium-term financial plan and the medium-term expenditure plan for the period 2009-2011. However, there has not been any report or assessment of this scheme so far.

The medium-term expenditure framework, as mentioned above, is a fiscal tool. It is a system of criteria that controls expenditures of the central government and local authorities as well as those on national target programs within the terms of three to five years. It is woven into the medium-term fiscal framework and medium-term budget framework (see Figure 5).

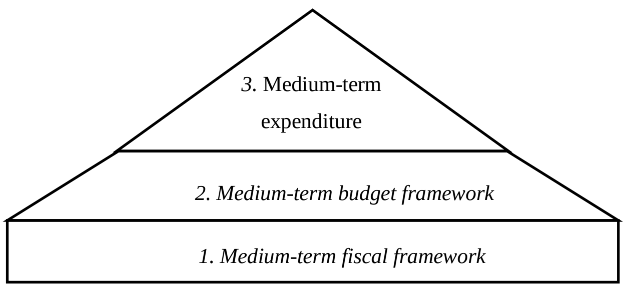

Figure 5: The medium-term expenditure framework is the specification of the medium-term fiscal framework

The medium-term fiscal framework is a set of objectives that are put forth in the fiscal policy and financial plan of the medium-term macroeconomic framework. This is also the first step towards a medium-term expenditure framework. The medium-term fiscal framework establishes fiscal constraints such as the ratio of budget expenditures to GDP, the ratio of budget income to GDP, the ratio of budget deficit to GDP, the ratio of public debt to GDP, the ratio of financial aids to GDP, annual growth rate of total spending, capacity of exploiting income sources, loans, long and medium-term fiscal commitments, socioeconomic development goals, and warnings of contingent debts, etc. These constraints are determined for the period of three to five years and budget-related decisions shall not exceed such limits. In sum, the objective here is to establish macro-fiscal disciplines for the allocation of resources.

The medium-term budget framework is an evolutionary step of the medium-term fiscal framework on the ground of developing budget estimates for each beneficiary unit. It aims at allocating resources based on priorities of national strategies to maximize effectiveness of budget expenditures and allocation of resources and keep the allocations within limits of medium-term fiscal framework. In sum, state budget beneficiary units still receive regular estimates on their budget without exceeding fiscal stringent constraints. In fact, the medium-term-budget framework is the most basic form of the medium-term expenditure framework.

The medium-term expenditure framework is the perfection of the medium-term budget framework via the modification of budget elements on the ground of operation and performance. It is reasonable to state that the aim of medium-term expenditure framework is the effectiveness of utilizing public resources in the government's operation, especially in supplying better public services (resources allocation effectiveness). Therefore, the medium-term expenditure framework can be deemed as a framework of policy and strategic spending of the government in which ministers enjoy more rights to allocate and utilize resources. A medium-term expenditure framework includes competence of resources as calculated from the top down, cost estimates for the current and three to five years later as per applicable policies, and eventually the balance between costs and current financial resources.

In the long run, the medium-term expenditure framework is a good tool to help the government and local authorities control fiscal ambitions. The successful implementation of medium-term expenditure framework depends heavily on the aid of institutional regime and the government's determination.

5. Conclusion

The government, more than anyone else, is competent enough to lead other economic entities to four macroeconomic goals namely economic growth, job creation, inflation control, and natural environmental protection. The government should think more objectively of its economic role and have a more flexible perspective on the public-private partnership. The reform of fiscal institutions and establishment of fiscal rules will help the government retain a more effective collaboration with the private sector. Any tardiness at the present time can prove expensive in the future■

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