A Positive Move

The Government is willing to cope with macroeconomic problems by widening the exchange trading band

With the new trading band, the dong will appreciate more over the U.S. dollar

By Que Anh

As Vietnam has emerged as one of the fastest growth economies in Asia, she cannot avoid macroeconomic mess, including trade imbalance.

A foreign expert from a well-know international audit company based in HCM City said to the *Weekly*, "It is important to note that the current challenges Vietnam is facing are the result of outstanding success in the past few years in pursuing economic reforms and attracting foreign investments, combined with recent developments in the global economy in the wake of the sub-prime crisis in the U.S." Many local economists also shared the same opinion.

According to the statistics by the Ministry of Planning and Investment, the trade deficit in the first two months of the year reached US$4.3 billion, up three times over the same period last year. In 2007, the figure was only US$1.07 billion.

The export turnover reached US$3.8 billion in February, raising that of the first two months to over US$8.7 billion, up 29.2% year-on-year. The import expenditure in February reached US$5.8 billion, making that of the first two months climb up to nearly US$13 billion, up 63.7% year-on-year.

One of the key impacts on the trade balance of any country is the exchange rate of its currency over the dollar. Vietnam dong, since the end of last year, has rapidly appreciated over the dollar. As one of the move to curb inflation, on March 4, the Prime Minister allowed the central bank to widen the trading band to 2% from 0.75%, helping the dong's appreciation to climb. Now, it takes time to see if it will solve economic problems.

Comprehensive measures work

Among policies that have been issued by the Government, some experts said this new one has a positive impact on the economy. Thomas Tobin, president of HSBC Vietnam, said: "The U.S. dollar has depreciated over other currencies, so the new policy is consistent with the weakening of the U.S. economy. In my opinion, this is a positive measure."

The appreciation of the dong over the dollar will make products from overseas cheaper and more competitive than Vietnamese products. Thus, the demand for imported commodities will increase while the demand for local products will decline in line with high inflation, high consumer price index, high input costs and so on. In contrast, Vietnamese products will become more expensive and thus lose its competitiveness in the global market. The trade deficit will climb up as a result.

However, to import products, Vietnam has to pay in dollars. This will on the one hand help return the dollar position back and lower the dong's appreciation as dollars will be in need for international trade. On the other, local companies will face pressure improving their product quality. They can also keep their prices unchanged and increase export volume. The trade deficit as a result will not be much higher.

The depreciation of the dollar does not take place in Vietnam only, but globally. In several countries, it is even higher. Therefore, regarding the bilateral trade between Vietnam and the U.S., Vietnam might suffer larger deficit.

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For the long term, however, this can help if Vietnamese companies are active in looking for other markets where the dong appreciation and their currencies over dollars is quite low.

Theoretically, the appreciation of the dong can create difficulty for foreign investment projects to make disbursement. However, in a recent meeting between HCM City Stock Exchange and 11 fund managers, representatives of these funds are also upbeat on the wider trading band and they said this will not have impacts on their disbursement plans. However, that is just in the short term. In the long term, more policies need to develop. "Whilst the trade balance is an important macroeconomic indicator to watch and the deficit might increase, as long as there is no marked slowdown in the disbursement of foreign direct investment and official development assistance commitments, the balance of payment and external debt situation of the country remains a low level of concern," the expert said.

In addition, the higher appreciation of the dong can partly lower the increase of oil prices, an important input factor. This can help businesses reduce their input costs and output prices, consequently improving their competitiveness.

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concerning governmental compromises in face of adversity. The Government needs to avoid surprise decisions and delayed action in areas where policy adjustments are necessary," the foreign expert said, adding that the Government needs to actively monitor all economic indicators and be ready to take further action.