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## Vietnam (Socialist Republic of)

**Primary Credit Analyst:**

KimEng Tan, Singapore (65) 6239-6350; kimeng\_tan@standardandpoors.com

**Secondary Credit Analyst:**

Elena Okorotchenko, Singapore (65) 6239-6375; elena\_okorotchenko@standardandpoors.com

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# Vietnam (Socialist Republic of)

## Major Rating Factors

### Weaknesses:

- A low-income economy
- A risk-laden banking system characterized by a high level of state ownership, rudimentary regulatory regime, and risk management capabilities
- Evolving macroeconomic policy framework

### Strengths:

- Strong economic growth prospects

### Sovereign Credit Rating

*Foreign Currency*

BB/Negative/B

*Local Currency*

BB+/Negative/B

*ASEAN Regional Scale*

axBBB/--/axA-2

## Rationale

The credit ratings on Vietnam reflect the country's low-income economy, developing financial system, and evolving policy framework. These weaknesses increase the vulnerability of the economy to severe shocks that could significantly increase the public financial burden. Healthy economic growth prospects, reinforced by the government's persistent efforts in economic restructuring, partly offset these weaknesses. A modest level of external indebtedness also supports the government's credit quality.

Developments since 2007 highlight the risks associated with Vietnam's credit weaknesses. Strong foreign capital inflow in 2007 and early 2008 was met with inadequate policy responses, which caused credit growth to accelerate from already high levels. By early 2008, this combination had led to clear signs of macroeconomic imbalances as inflation and trade deficit rose steeply.

A strong policy response from the government prevented imbalances from developing into instability. By April 2009, consumer price inflation has receded to below 10% and the trade account was in surplus for the first four months of this year. The politically difficult steps taken to achieve this, as well as the continuing economic reforms implemented over this period, likely reassured investors. Foreign direct investment remained very strong in 2008. Although it has fallen off significantly in 2009, we expect it to rebound as the global economy recovers. These projects are expected to contribute to maintaining Vietnam's trend annual economic growth at about 7%. We forecast growth in 2009 to be lower at 4% because of the global slowdown.

Vietnam's modest net external debtor position, at 2.5% of current account receipts in 2008, also helped prevent more serious damage to the economy. In recent years, foreign investment in Vietnam lifted the level of foreign reserves held by the central bank. We forecast reserves at slightly below US\$24 billion by end 2009. The foreign reserves will continue to provide a useful cushion against future adverse shocks.

The volatility of recent years, however, has weakened the banking sector's balance sheet. Nonperforming loans are expected to rise over the next one to two years, particularly at the newer and smaller banks that had seen the fastest lending growth. If the economic downturn is prolonged, financial pressure will mount to exacerbate asset quality deterioration. The government may have to support the banks to preserve financial stability. This would damage the

sovereign financial position by raising net general government debt significantly above the current level of close to 29% of GDP.

## Outlook

The negative outlook on the ratings reflects the risks to financial stability as banks face an economic slowdown with weakened balance sheets. Without appropriate policy response, the situation could develop into a widespread economic and financial system distress. The credit ratings on the government could be lowered if the probability of this scenario materializing increases. The likelihood of the sovereign rating remaining at the current level could rise on indications that the economy will return to a sustainable growth path and that the financial fallout of economic rebalancing will be confined to a small number of systemically unimportant institutions. This would allow the outlook to revert to stable.

**Table 1**

Socialist Republic of Vietnam's Selected Indicators											
	2003	2004	2005	2006	2007	2008	2009e	2010f	2011f	2012f	Median BB
GDP per capita (\$)	488.9	553.8	636.7	723.5	833.6	1,052.1	1,082.5	1,137.1	1,247.8	1,406.0	3,853.0
Real GDP (% change)	7.3	7.8	8.4	8.2	8.5	6.2	4.0	6.2	6.6	7.5	1.0
Real GDP per capita (% change)	5.8	6.3	7.0	6.8	7.2	5.0	2.7	5.0	5.3	6.1	0.5
General government balance (% of GDP)	(1.8)	(2.7)	5.0	(4.1)	(4.7)	(3.2)	(6.7)	(4.1)	(3.2)	(3.2)	(3.5)
General government debt (% of GDP)	34.0	35.5	37.2	37.5	39.0	34.9	33.2	33.3	32.4	31.5	37.0
Net general government debt (% of GDP)	33.3	29.7	32.1	30.8	31.1	25.1	28.8	29.4	29.0	28.6	30.3
General government interest exp. (% of revenues)	3.6	3.6	3.2	2.8	3.5	4.1	4.4	4.0	4.2	4.1	5.9
Domestic credit to private sector & NFPEs* (% of GDP)	0.0	58.8	65.6	71.2	93.4	90.6	99.1	106.9	115.6	122.5	41.9
Consumer price index (average; % change)	3.2	7.8	8.3	7.4	8.9	24.4	8.3	7.0	6.8	5.3	6.2
Gross ext. financing needs¶ (% of CARs and usable reserves)	N/A	90.0	90.2	88.5	95.0	89.0	82.7	85.4	83.1	81.6	94.8
Current account balance (% of GDP)	(4.9)	(2.0)	(0.9)	(0.3)	(9.8)	(9.3)	(2.1)	(1.4)	(1.5)	(1.8)	(4.1)
Narrow net external debt§ (% of CARs)	N/A	14.4	10.6	2.4	(3.9)	2.5	5.6	1.0	(4.1)	(7.5)	24.9

\*Standard & Poor's estimates that, in a reasonable worst-case economic downturn, gross problematic assets could reach 35%-50% of domestic credit to the private sector and NFPEs; see "Banking Industry Country Risk Assessments", published monthly on RatingsDirect. ¶Gross external financing needs are defined as current account outflows plus short-term debt by remaining maturity. §Narrow net external debt is defined as the stock of foreign and local currency public and private sector borrowings from nonresidents (including nonresident deposits in resident banks) minus liquid nonequity external assets, which include official foreign exchange reserves, other liquid public sector foreign assets, and financial institutions' deposits with and lending to nonresidents. A negative number indicates net external lending. f--Forecast. e--Estimate. NFPEs--Nonfinancial public sector enterprises. CARs--Current account receipts.

## Comparative Analysis

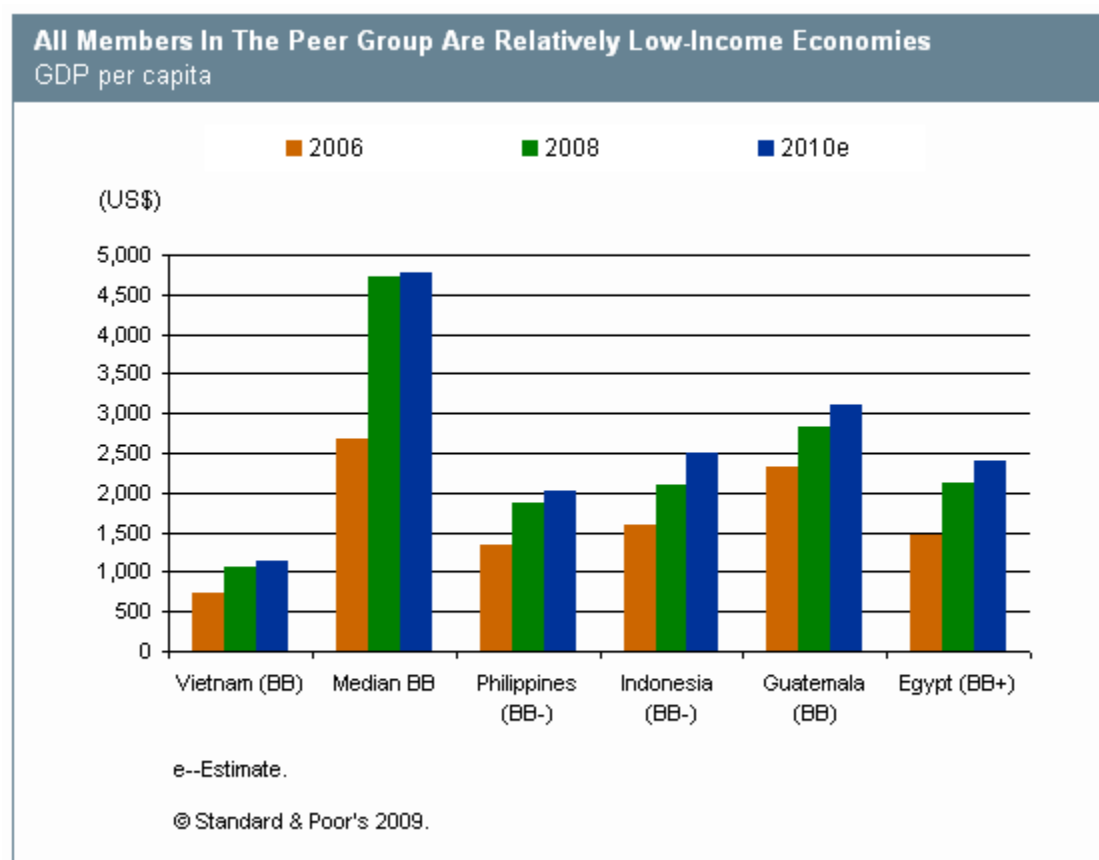
- Lower income level but stronger economic growth prospects than peers
- Lower external vulnerability compared with Indonesia and the Philippines

### Peers are similarly rated sovereigns in large- and medium-size economies

Vietnam's credit attributes are comparable with similarly rated sovereigns that have large- and medium-size economies. These include Egypt (BB+/Stable/B; all ratings herein refer to foreign currency ratings), Guatemala (BB/Stable/B), Indonesia (BB-/Stable/B) and the Philippines (BB-/Stable/B).

All members in the peer group are relatively low-income economies with per capita GDP ranging from US\$1,052 in Vietnam to US\$2,827 in Guatemala (see chart 1). All of them experienced relatively strong economic growth in recent years. For the period 2006-2008, real GDP per capita grew between 2.2% (Guatemala) and 7.0% (Vietnam). The seemingly low figure for Guatemala reflected strong population growth in the period, as overall real GDP grew at almost 5% annually.

**Chart 1**

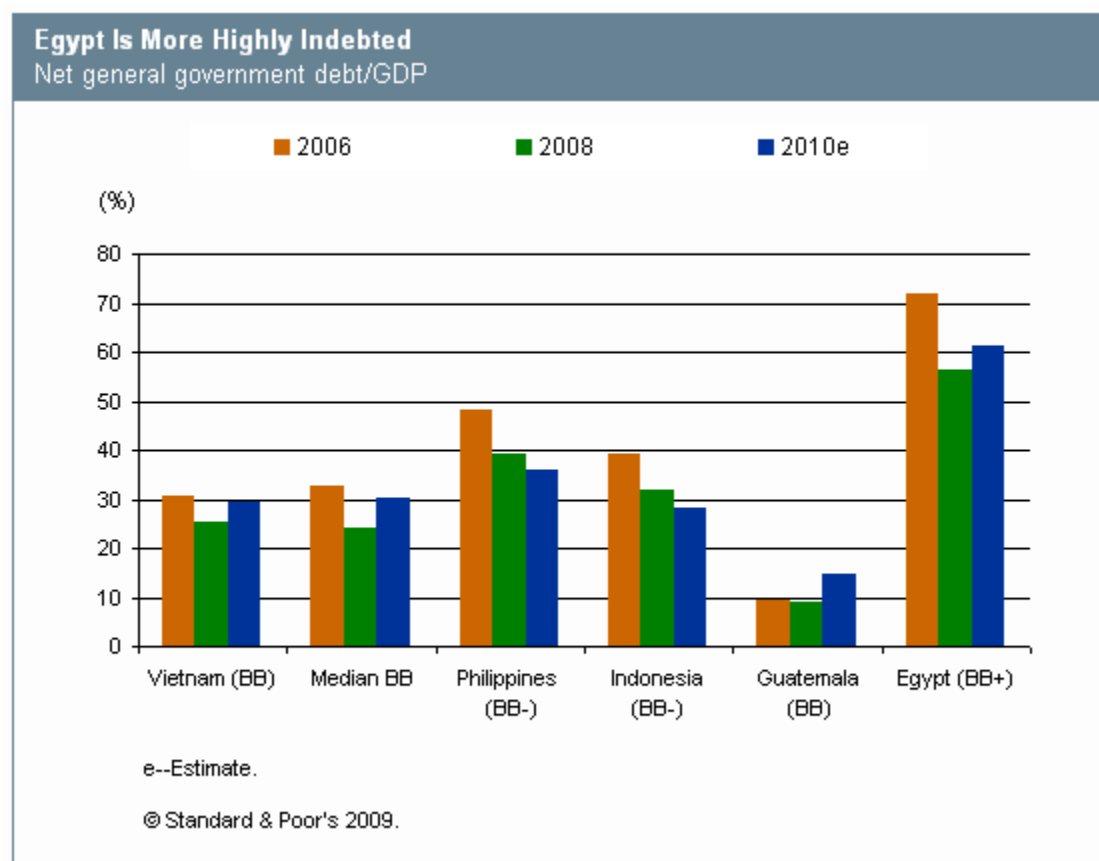


### Healthy external position and economic prospects underpin Egypt's sovereign creditworthiness

General government debt burden in Egypt is heavier than other members of the peer group. With net debt at more than 56% of Egyptian GDP in 2008, the Egyptian government owes significantly more than the Philippines, the next

most highly indebted government (see chart 2). Both governments spent more than 16% of their revenue on interest payments--significantly more than others in the group.

**Chart 2**



A healthy external position and good economic prospects support Egypt's sovereign creditworthiness. Like the Philippines and Indonesia, Egypt had been running current account surpluses in recent years. Moreover, Egypt was the only net external creditor in the peer group at the end of 2008. Growth of the Egyptian economy had also been only slower than Vietnam in recent years. Like in Vietnam, an acceleration of foreign direct investment inflows was an important reason for the strong performance.

### Stronger growth prospects put Vietnam on par with Guatemala...

Similarly rated Guatemala and Vietnam are both small external debtors that have seen current account deficits rising in recent years. A surge in investment was the main reason in Vietnam. A drop in Guatemala's domestic savings rate, due to strong credit growth, joined a pickup in the investment rate as the cause for the widening deficit.

Partly on account of the stronger investment trends in Vietnam, economic growth performance and prospects are stronger than in Guatemala. A lower level of government indebtedness in Guatemala, however, offsets some of its disadvantage in this respect. Moreover, while both are high-inflation economies, macroeconomic volatility in Guatemala has been smaller.

The projected financial institution contingent liability of a post-boom economic scenario is also significantly lower

in Guatemala. The cost to the government of supporting these institutions in this scenario is projected at close to 70% of Vietnam's GDP in 2009. The same estimate for Guatemala is less than 11%.

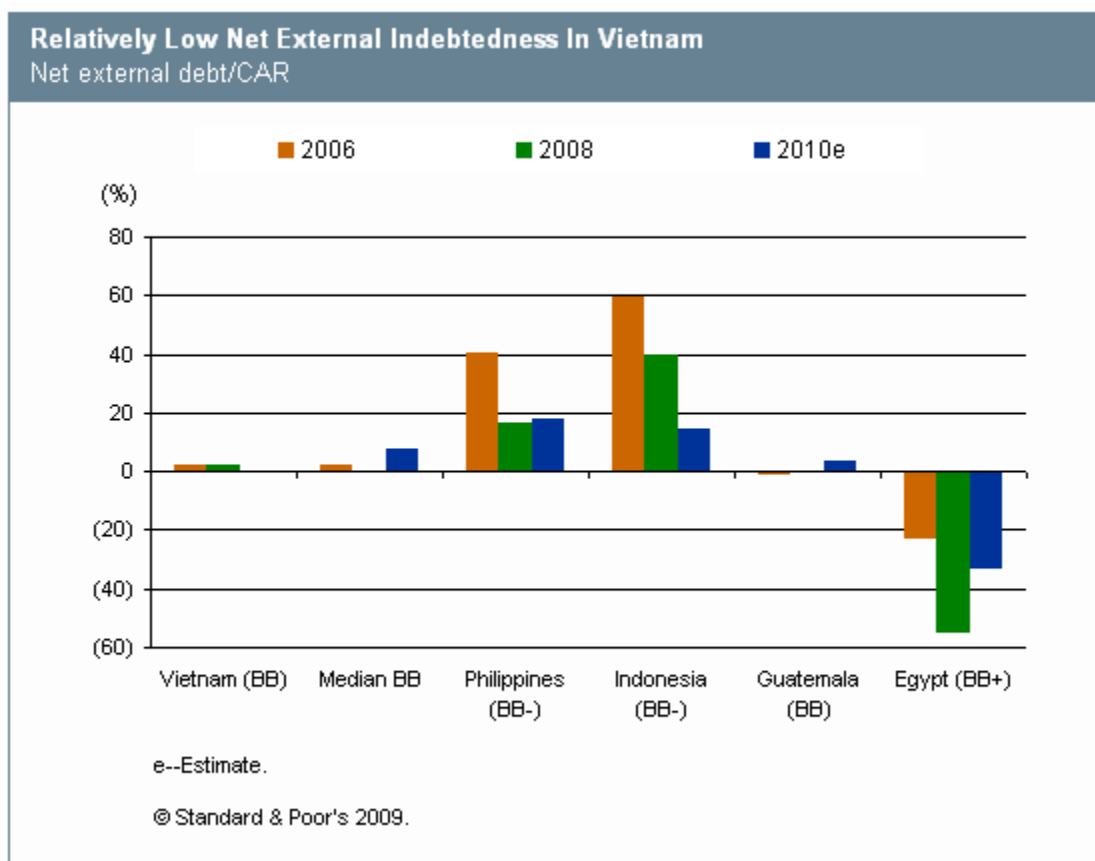
**...and above Indonesia and the Philippines**

The higher foreign currency sovereign credit rating on Vietnam, compared with Indonesia and the Philippines, is a reflection of its better economic growth prospects and less vulnerable external position. Compared with the Philippines, the Vietnamese government's debt burden is also markedly lower.

Vietnam has experienced stronger real per capita GDP growth in recent years. This was partly due to a strong commitment to improving the investment climate through structural reforms as well as heavy investment spending. In 2004-2008, Vietnam committed an average 39% of GDP to domestic investment. This was significantly more than the 23% in Indonesia and 22% in the Philippines.

Despite a resulting surge in the current account deficit, Vietnam is the smallest net external debtor among the three (see chart 3). In part, this reflects the importance of foreign direct investments in financing capital spending of recent years. Compared to the other two Southeast Asian countries, average maturity of Vietnam's external debt is also much longer. This mirrors the fact that much of these debts are concessionary multilateral or bilateral loans.

**Chart 3**



## Political Environment

- Economic reforms pushed ahead as government responded to economic volatility.
- Corruption remains an issue.

### Structural reforms continue

The Vietnamese government's response to economic overheating in 2008 likely helped it to regain much investor confidence after the turmoil in the first half of the year. Instead of rolling back economic reforms carried out in recent years, as some feared, the government pushed economic liberalization further forward. It also dealt forcefully with macroeconomic imbalances using conventional policy tools.

In the face of evident overheating, the Vietnamese government showed a willingness to take tough measures to stabilize the economy. These included a sharp tightening of monetary and fiscal policies, despite what must have been strong opposition from domestic enterprises. Its decision to temporarily stop issuing new joint-stock bank license in August 2008 was also unlikely to have been well received by the state-owned enterprises (SOE) that had applied for licenses.

As it acted to stabilize the economy, the government had continued its economic liberalization efforts. In line with its World Trade Organization (WTO) commitments, it licensed a number of local subsidiaries for foreign banks. The ownership ceiling of a single foreign party was also lifted to 20% for one of Vietnam's joint-stock banks, above the usual 15%. The 49% limit on foreign ownership of domestic public companies, previously applied only to listed companies, was extended to non-listed companies. A 3% cap on the number of foreign employees working for a company in Vietnam was also removed.

The episode had also led to some improvements in transparency. In an effort to calm uncertainties among investors, the government held a video conference call with investors to answer their queries. Realizing that the lack of information out of the banking sector was a significant concern of foreign investors, the State Bank of Vietnam (SBV) began posting weekly and monthly English-language reports on banking sector developments. Timely data on the state of the banking sector, however, remains absent.

The Vietnam government renewed its anti-corruption drive in 2009. This was in response to a suspension of Japanese official development aid (ODA) in late 2008. The suspension followed the discovery of graft in a Japanese funded ODA project. Japan agreed to resume aid in April 2009 after the Vietnamese government said it would take steps to ensure the proper use of ODA funds. In May, the government issued a resolution launching a national strategy on fighting corruption through to 2020. It also indicated its intention to ratify the United Nations Convention Against Corruption.

Apart from donor pressure, the renewed emphasis on anti-corruption likely also reflects concerns over social stability. Employment opportunities are expected to be significantly reduced by the global recession. With a young and fast-growing labor force, Vietnam could face rising dissatisfaction among its population if unemployment climbs sharply. Perception of official corruption could focus such dissatisfaction on the government and create political instability.

## Structural Reforms Brighten Economic Prospects

- Strong foreign direct investment in 2007 and 2008 contributed to a surge in capital spending.
- Economic growth to remain positive despite the global slowdown.

### A low-income economy that is investing heavily

Although Vietnam is a low-income economy, with per capita GDP expected to reach just US\$1,083 in 2009, heavy investments in recent years are expected to pave the way for strong and sustained economic growth. Capital investment rose to approximately 35% of GDP in 2004-2006, from below 30% in 2000, largely financed by the high domestic savings rate of close to 34% of GDP. In 2007 and 2008, a surge in credit growth and strong foreign direct investment inflows helped push the investment rate toward 45% of GDP.

The surge in investment threatened macroeconomic stability in Vietnam. This contributed to consumer price inflation escalating above 21% in April 2008, from 10% in late 2007. The trade deficit also rose steeply, leading to a US\$7 billion current account shortfall (9.9% of GDP) in 2007. Together with the worsening global financial conditions, this triggered an outflow of foreign portfolio investments.

A strong policy response from the government helped to stabilize the economy and reduce the trade deficit. By October 2008, the consumer price index began to fall on a month-on-month basis. The trade deficit also shrank sharply. The sharp deceleration in global economic growth reinforced policy measures to rein in the Vietnamese economy. Indeed, the negative impact of external conditions on Vietnam had become the main economic policy focus in late 2008.

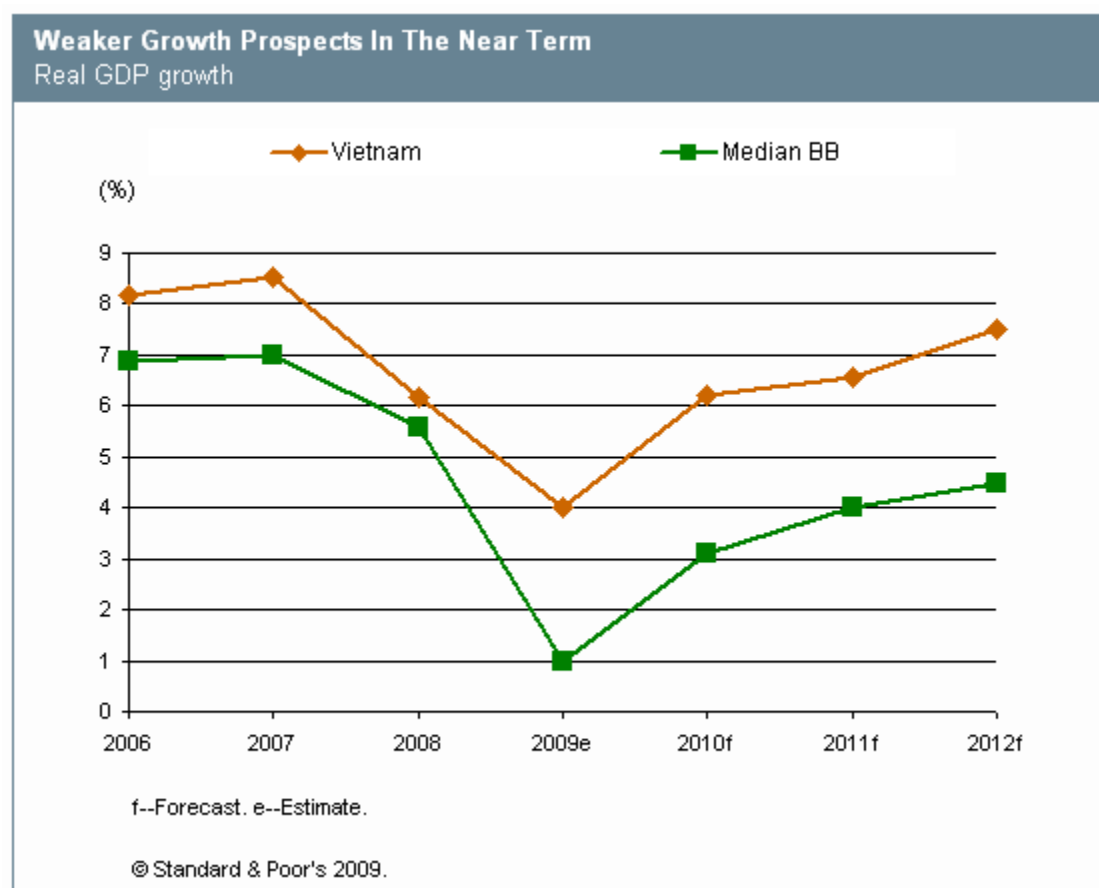
From the fourth quarter of 2008, fiscal and monetary policies were eased rapidly to prevent a steep decline in economic growth. Budgetary funds held back previously to prevent overinvestment were disbursed quickly. Fiscal expenditure and borrowing targets for 2009 were raised significantly. The policy interest rate was also lowered rapidly.

The policy stimulus helped the economy to stage a rebound in the second quarter of 2009. After dipping to 3.1% in the first three months, real GDP growth accelerated from April to record a first half gain of 3.9%. We expect performance in the remainder of 2009 to be less buoyant as growth of private demand slows. Household spending is likely to be more affected by rising unemployment and the implementation of the personal income tax in the second half of the year. Private investment could also slow on fewer starts of FDI projects. For the year, Standard & Poor's Ratings Services forecasts real GDP growth at 4.0%.

Growth in 2010-2011 is forecast at 6%-7% annually on expectations of a gradual capital spending recovery. Exports in the near term will be lifted by the completion of FDI projects committed earlier. However, we expect that uncertainties over the strength of developed economies will persist. This will likely weigh on investor confidence and lead to fewer capacity expansions. Pointing to this, FDI commitments in the first seven months of 2009 fell by more than 81%.

Despite the weaker near-term prospects (see chart 4), we project Vietnam's medium-term trend growth at 7.0%-7.5%. This reflects our expectations that continued economic reforms will help narrow the gap between Vietnam and more developed economies. Specifically, we believe that administrative and bureaucratic impediments faced by the private sector will continue to be reduced gradually.

Chart 4



SOE reforms are also projected to be pushed further in the near future. The effort appeared to have regained momentum recently after slowing equitization of SOEs in recent years. This could be due to the focus on the unproductive use of large tracts of valuable land SOEs own. In June 2009, a new directive by the Prime Minister requires the equitization of all SOEs by July 2010.

## Infrastructure Building Keeps Government Spending High

- Sharp increase in the budget deficit in 2009

### Fiscal deficit fell in 2008 but strong rebound in 2009 expected

Vietnam's general government deficit fell in 2008 as it reined in spending to cool its overheating economy earlier in the year. Up to September 2008, the government had reported a surplus amounting to 0.7% of annual GDP. However, as global economic conditions worsened dramatically in the final months of 2008, public capital spending was ramped up rapidly. Accounting for both budgetary and off-budget spending (but excluding the operations of the Vietnam Development Bank), the general government deficit amounted to VND48 trillion (3.3% of GDP). This was lower than the VND54.1 trillion (4.7% of GDP) a year earlier.

The deficit reduction reflected mainly lower capital spending. Despite the volatile economic situation, government revenue had risen 20.6% in 2008 (versus a 9.2% gain in 2007). Contributions from the main revenue

sources--corporate income tax, value-added tax, and trade-related taxes--grew strongly in the year. Export and import taxes rose by more than 50%, even as tariffs fell, due to soaring import volume. Current spending, however, rose even faster at 34.1% as the government raised social subsidies by almost 50% partly to offset sharply higher inflation. Total expenditure growth was held down to 16% only due to a 9% cut in capital spending (budgetary capital expenditure and off-budget infrastructure bond financed spending).

In 2009, however, we forecast the deficit to rise to 6.7% of GDP. This reflects both an expectation of weaker economic performance in the year as well as countercyclical measures the government is undertaking. These measures, announced as a VND160 trillion (approximately US\$9 billion) package, included tax reductions and waivers as well as interest subsidies and credit guarantees for SMEs. The additional funds required in 2009 for this package is likely to be significantly less than the amount announced. Funds for projects postponed from 2008, included in the package, are likely to have been raised already. Credit guarantees for SMEs also do not require up-front cash.

### **Need for cash is not matched by new fund raising**

Nevertheless, funds needed to plug the shortfall remains large. However, the government has not been as aggressive about raising funds early in 2009. A number of government bond auctions in the first half of the year resulted in no sale of bonds. Although buyers were reportedly available, the yields they required were higher than the Ministry of Finance's ceiling rate.

The lack of urgency to raise funds is likely explained by the very large deposits that the government maintains at the SBV and the commercial banks. As of October 2008, deposits amounted to VND140 trillion (approximately US\$8 billion). By February 2009, however, government deposits had fallen by more than VND48 trillion. This suggests that a significant part of the stimulus package could be funded by existing government financial resources.

We forecast general government debt to decline to 33.2% of GDP, reflecting its slower growth compared with that of nominal GDP. However, we expect net debt to rise to 28.8% of GDP from 25.1% in 2008. This reflects a large projected decline in government bank deposits and reverses the declining trend of recent years. In 2005-2008, net government debt had fallen as a proportion of GDP. Much of this reduction took place in 2008, when the government reduced its borrowing even as high inflation lifted nominal GDP. At the same time, slow disbursement by government agencies also led to an accumulation of deposits.

### **Sharp exchange rate changes could increase debt burden**

Standard & Poor's projects steady economic growth in the medium term to gradually lower the relative government debt burden. Public investment spending should grow strongly over the foreseeable future. Nevertheless, the size of budget deficits is likely to fall from the unusually high level in 2009. Together with GDP growth, this should keep general government debt at a stable share of GDP. And despite the increasing share of domestic currency debt, which is more costly, interest payments are expected to stay relatively stable as a proportion of government revenue. This assumes slight improvements in revenue collection arising from ongoing tax regime reforms.

An important risk to the Vietnamese government's debt burden comes from a potential sharp depreciation of the dong. A little more than half of existing government debt is denominated in foreign currencies. Despite the concessionary nature of most of these loans, the debt burden on the government could rise sharply if the dong depreciates sharply against other currencies. The government is unable to mitigate this important risk due to the insufficient development of the dong foreign exchange derivative market.

### **Off-budget and contingent liabilities the main fiscal concerns**

Although the official debt level is moderate and interest burden currently low, a significant amount of contingent liabilities, if realized, could threaten fiscal health. The largest of these are the nonperforming loans on the books of the SOCBs, accumulated through years of directed policy lending. Estimated at 2.52% of total loans at the end of June 2009, nonperforming loans are generally considered to be much higher if evaluated according to the standards of more advanced banking systems.

In particular, Vietnam's restructured loans are immediately regarded as performing loans without an observation period. In addition, loans without proper documentations are typically not counted as nonperforming, unlike other banking systems. In a post-boom recession scenario, we estimate that the contingent liability to the government arising from a troubled banking sector could be as high as 69% of GDP.

The risk of the government having to provide significant financial support for the banks has risen over the last few years. In this period, the banking sector has seen very strong credit growth, followed by an abrupt monetary tightening and a global economic slowdown in 2008. From April 2009, loans growth rebounded strongly again. Based on the relatively basic risk assessment and management capabilities of Vietnamese banks, it is possible that nonperforming assets have risen significantly.

While the risks of systemic instability are currently not assessed to be high, the government is likely to have to provide funds to recapitalize the banking system at some point. And if the economic slowdown turns out to be much worse than currently expected, the likelihood of systemic instability will rise and the need for government recapitalization could come sooner.

Foreign currency debts guaranteed by the government are another source of contingent liabilities. As at September 2008, this stood at US\$2.9 billion. These loans are mostly foreign commercial bank borrowings of large SOEs in the transport and power sectors. Yet another fiscal concern is the arrears arising from off-budget infrastructure projects. Reviews of public expenditure reveal significant transport development spending that had not been budgeted for, and which had been financed by arrears due to contractors (usually SOEs) who in turn borrowed from SOCBs. Although an earlier estimate of such arrears was 1.5% of GDP, part of this could already be captured as nonperforming loans of the SOCBs.

### **High Inflation Expectations Limit Impact Of Monetary Easing**

- Monetary easing began from the final quarter of 2008
- Inflationary expectations remain high to limit the effectiveness of lower policy interest rates

### **Banks' net interest margins squeezed by regulatory ceiling on interest rates**

In early 2008, as imbalances threaten to destabilize the economy, the SBV began to reassert direct control over interest rates in the country. Prior to February 2008, commercial banks were free to set deposit and lending rates according to market conditions and their funding positions. By May, however, they were required to set lending and deposit rates at no higher than 1.5x the SBV's prime interest rate. From August, even interbank lending rates were similarly restricted.

With inflation showing signs of moderation and economic uncertainties rising, the SBV began using its new powers to engineer a reduction in borrowing costs. The central bank began lowering its policy interest rates, from October 2008 when it peaked at 14%, to 7% by February 2009. At the same time, reserve requirements were also lowered to

release more liquidity to the commercial banks. The SBV also offered to buy back compulsory bills that it had earlier sold to banks to mop up excess liquidity in the money markets. The relief to borrowers, however, is a lot less than one would expect, given the rapid easing of monetary policy.

Banks had continued to be selective in making new loans in early 2009. In part, this reflected a more conservative attitude among lenders in a weak economic environment. A number of banks were also constrained by balance sheets that had been weakened by the volatility of the past two years. However, a domestic liquidity shortage was also an important reason for banks' reluctance to lend. Banks continue to face difficulties attracting deposits at interest rates below the 10.5% ceiling implied by the SBV's 7% prime interest rate. This is possibly related to still-high inflation expectations.

With their lending rates similarly restricted at the same level, banks face low positive or even negative margins on their loans. This naturally reduced their eagerness to lend. As a result, bank lending grew by a relatively weak 2.67% in the first quarter of 2009. Only when the government's interest rate subsidy scheme began to show its impact in April did lending grow more robustly. For 2009, we forecast that bank lending will grow by 24%.

Foreign currency liquidity was better than in the domestic currency money markets. U.S. dollar deposit rates fell continually from late 2008 into early 2009 as deposit growth outpaced that of Vietnamese dong deposits in the period. Demand for U.S. dollar loans, however, was relatively weak in the period. In taking advantage of these trends, the Vietnamese government sold about US\$230 million of debt at low costs in March 2009. The government reportedly aimed to raise up to US\$1 billion from bond issuances in the domestic market in 2009. However, the weak demand for its offerings in late August suggests that this target is unlikely to be met. The low interest rate that the government was willing to pay (3.9% for the three-year tranche) did little to attract investor interest.

## External Finances

- Risks posed by external imbalances eased by early 2009 as the current account returned to balance
- Large current account deficit in 2008 financed mainly by foreign direct investments and net official borrowing, leaving foreign exchange reserves little changed

### Current account deficit to fall sharply in 2009

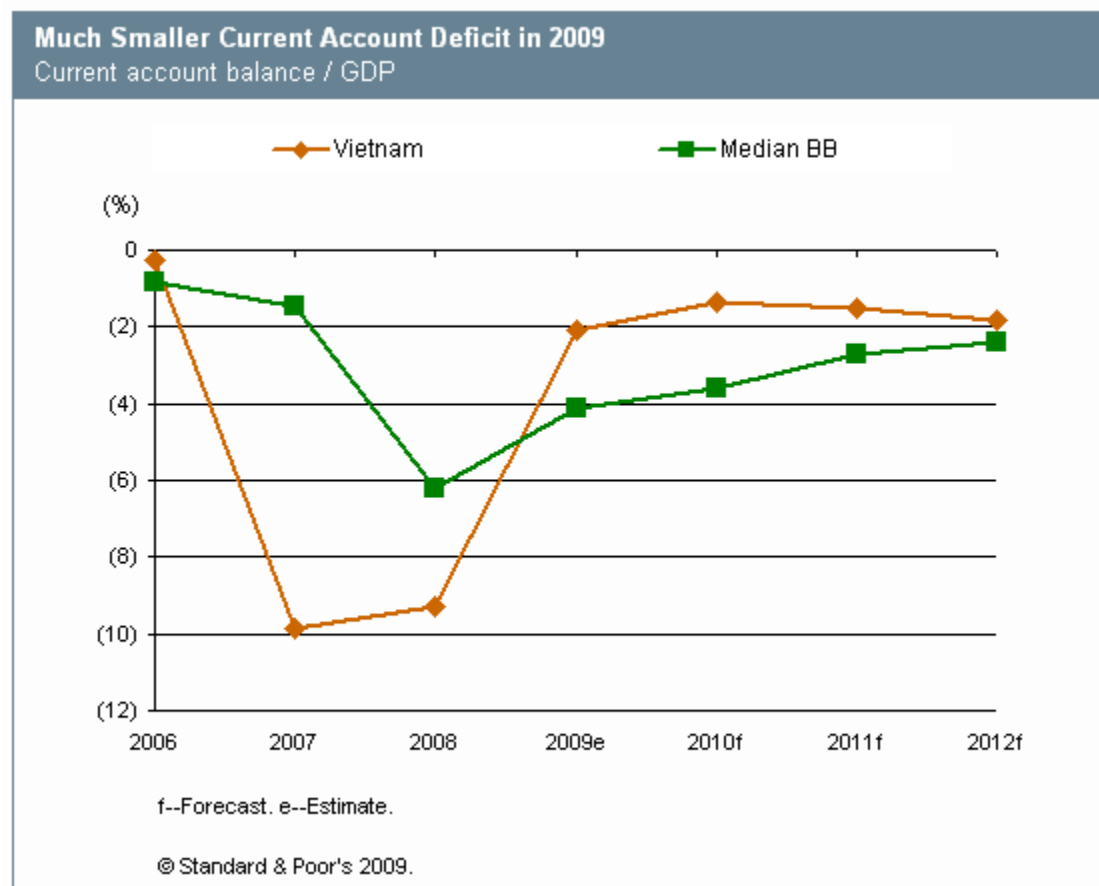
Vietnam's current account deficit tumbled from late 2008 and likely turned into a surplus in early 2009. The current account deficit remained high at close to 10% of GDP in 2008, after a similar shortage in 2007, due to a surge in imports that accompanied strong capital investment. This gap closed significantly in late 2008 due to the government's efforts to restore macroeconomic balance. The intensifying global economic slowdown had also dampened investment demand.

This trend extended into early 2009. In the first four months of the year, Vietnam's trade account showed a US\$800 million surplus. By June, however, it had returned to a year-to-date deficit amounting to US\$2.1 billion. In part, this reflected the fall in gold exports from the early months of the year. The early 2009 surge in gold export was likely the reversal of speculative purchases made in the previous year, when residents purchased gold amid the uncertain economic environment.

For 2009, we project the annual trade deficit at close to US\$4 billion. The smaller trade deficit forecast, compared with US\$18 billion a year earlier, will help to keep the current account closer to balance. We expect the 2009 annual current account to shrink to 2.1% of GDP from almost 11% in 2008 (see chart 5). As in earlier years, this reflects

the partial offset of the trade deficit by remittance inflows.

**Chart 5**



### FDI inflows covered much of external deficits in recent years

Similar to the situation in 2007, the current account deficit in 2008 was largely plugged by strong net direct investment flows. In fact, the surge in imports to the levels in 2007-2008 was largely due to strong foreign direct investment inflows. In 2007, capital spending by the foreign invested sector almost doubled from a year earlier to VND129 trillion. This rose further to VND192 trillion in 2008. Over these two years, the sector's share of capital spending in Vietnam rose to 31.4% from 16.2%.

Foreign investment in Vietnamese financial securities almost ground to a halt in 2008. Net portfolio investment inflows slowed to US\$110 million from more than US\$6.2 billion just a year earlier. This decline coincided with a drop of approximately US\$1 billion in medium- and long-term official net borrowing as well as significant unidentified capital outflows.

The capital outflow was reflected in a US\$2.5 billion negative balance in the balance of payments errors and omissions account. A US\$1.8 billion increase in short-term borrowing (mainly from bilateral sources), however, made up for the shortfall resulting from these developments. Consequently, Vietnam's foreign exchange reserves managed to rise marginally to US\$24.2 billion at the end of 2008.

## External indebtedness to be little changed against GDP

We expect gross external indebtedness to rise to US\$33.2 billion in 2009 from US\$32.0 billion in 2008. Relative to GDP, we forecast external debt to be little changed from 2008 at 35%. While direct investment inflows are likely to slow in the year, the decline in the current account deficit is projected to be even larger. Consequently, net debt inflows will fall even more steeply.

The government will remain the largest external debtor in the country, followed by foreign invested firms that borrow from their parent companies. Much of the government's foreign debts are in the form of bilateral or multilateral official development aid (ODA). Reflecting the very long maturity of such lending, average maturity of the government's debt is forecast at 27 years at the end of 2009.

<b>Ratings Detail</b> (As Of September 15, 2009)*		
<b>Vietnam (Socialist Republic of)</b>		
Sovereign Credit Rating		
<i>Foreign Currency</i>		BB/Negative/B
<i>Local Currency</i>		BB+/Negative/B
<i>ASEAN Regional Scale</i>		axBBB/--/axA-2
Commercial Paper		
<i>Local Currency</i>		B
Senior Unsecured (4 Issues)		BB
Senior Unsecured (254 Issues)		BB+
<b>Sovereign Credit Ratings History</b>		
02-May-2008	<i>Foreign Currency</i>	BB/Negative/B
07-Sep-2006		BB/Stable/B
18-Oct-2005		BB-/Positive/B
02-May-2008	<i>Local Currency</i>	BB+/Negative/B
07-Sep-2006		BB+/Stable/B
18-Oct-2005		BB/Positive/B
17-Aug-2009	<i>ASEAN Regional Scale</i>	axBBB/--/axA-2
<b>Default History</b>		
Restructured last outstanding bilateral debt to Algeria, June 2005.		
Distressed rescheduling of US\$850 million of commercial loans to the London Club group of creditors concluded with Brady Bonds issuance, March 1998.		
Restructured official debt with Paris Club creditors in 1993 and Russian ruble debt in September 2000.		
<b>Population</b>		87.2 million
<b>Per Capita GDP</b>		US\$1,083
<b>Current Government</b>		
General Secretary Nong Duc Manh is the head of the Communist Party of Vietnam.		
Prime Minister Nguyen Tan Dung is the head of government.		
President Nguyen Minh Triet is the head of state.		
<b>Election Schedule</b>		
Not applicable.		

\*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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