Asia-Pacific Research and Training Network on Trade
Working Paper Series, No. 102, May 2011

Impacts of the global economic crisis on foreign trade in lower-income economies in the Greater Mekong Sub-region and policy responses: the case of Vietnam and its implications for Lao PDR and Cambodia

by

Nguyen Manh Hung*
Pham Sy An*

* Nguyen Manh Hung is researcher of the Institute of World Economics and Politics (IWEP), Viet Nam. ** Pham Sy An is researcher of the Viet Nam Institute of Economics (VIES), Viet Nam. This paper was prepared as part of the ARTNeT initiative. The technical support of the United Nations Economic and Social Commission for Asia and the Pacific is gratefully acknowledged. The opinion, figures and estimates are the responsibility of the authors and should not be considered as reflecting the views or carrying the approval of the United Nations, ARTNeT, the Institute of World Economics and Politics or the Viet Nam Institute of Economics. The authors are thankful to Dr. Sailendra Narain, Centre for SME Growth and Development Finance (CESMED) in India, for his valuable comments and suggestions. The authors also are thankful for the valuable input and comments provided by an anonymous referee. Any remaining errors are the responsibility of the authors, who can be contacted at: hungmng@gmail.com, and phamsian@gmail.com

Executive Summary

The outbreak of the global financial crisis, the fluctuation of commodity prices, and the economic slowdown of the major trading partners in 2008 and the early 2009 has brought about one of the most difficult challenges to lower-income economies in the Greater Mekong Subregion (GMS, i.e. Vietnam, Lao PDR and Cambodia) since the Asian financial crisis of 1997-1998. Foreign trade, including both export and import, severely declined, leading to serious contraction of economic growth.

This research seeks to better understand the impacts of the global economic crisis on Vietnam's foreign trade and policy responses, and from this, draw inferences for Lao PDR and Cambodia. To this aim, it asks the following questions:

- To what extent was the foreign trade of Vietnam affected by the global economic crisis?
- What were the policies by the Vietnamese government to arrest and reverse the decline in foreign trade?
- What lessons can the Vietnamese experience offer to Lao PDR and Cambodia?

TABLE OF CONTENTS

LIST OF FIGURES

1. Introduction

The six economies of the Greater Mekong Sub-region (GMS) include Cambodia, Lao PDR, Myanmar, Viet Nam (CLMV), Thailand and China's Yunnan Province. In the recent years, GMS countries have achieved remarkable success in their economic development and integration at both the sub-regional and global level. In 2001, China acceded to the World Trade Organization (WTO), followed by Cambodia in 2004 and Vietnam in 2006. At the same time, a dense web of sub-regional cooperation has been created, including the establishment of development triangles, opening of economic corridors, implementation of cross-border trade facilitation measures, and the acceleration of the completion of the ASEAN Free Trade Area by CLMV on their way toward membership in the ASEAN Economic Community (AEC).

At the same time, trade has been expanding faster than ever in the GMS. During the 1994-2006 period, intra-GMS exports, excluding those to China, grew at an annual average rate of 19% (People's Daily Online, 31/3/2008). From 2002 to 2006, total trade turnover between Cambodia and Thailand increased from US$ 259.88 million to US$ 411.29 million (Chanboreth, 2009). Trade with neighboring economies is especially important for Lao PDR and Myanmar. Lao PDR, for example, being a land-locked country, depends heavily on intra-regional trade, with 45% of its exports going to and 72% of its imports coming from the GMS in 2008. U.S economic sanctions have made Thailand and China Myanmar's two largest trading partners. Myanmar's trade with China, for instance, has grown steadily since the late 1980s, constituting 24% of its total foreign trade in 2008 (Pichai, 2009). In 2008, before the impact of the global economic crisis was fully felt, trade turnover of Vietnam with China, Lao PDR and Cambodia grew at the rates of 37.6%, 35.6% and 27.3% respectively compared to 2007 (MOIT, 2009).

The outbreak of the global financial crisis, fluctuations in oil, food, and other commodity prices, and the economic slowdown of the major trading partners in 2008 and early 2009 has brought about one of the most difficult challenges to the GMS economies since the Asian financial crisis of 1997-1998. The most important impact channel, exports, was severely decreased, leading to a serious contraction of economic growth. Among the lower income economies of the GMS, in 2009, the export volume of Vietnam fell 9.7%, contributing to a further decline of the economic growth rate from 6.18% in 2008 to 5.32% in 2009 (General Statistics Office, Annual Report 2009). Cambodian total exports showed a sharp decline of 18% compared to 2008, and the growth rate fell to 2.1% from 6.6% in 2008 (The Mirror, 21/1/2010). The relatively closed economy of Lao PDR also experienced a fall in its growth rate from 7.2% in 2008 to 6.4% in 2009 because of heavy drop in the price of its major export items. (Vientiane Times, 25/1/2010)

The above governments took important steps on both fiscal and monetary policy in response to the impacts of the crisis: Stimulus packages were launched; central banks reduced interest rates; fiscal authorities adopted expansionary policies; taxes were cut; and targeted cash transfers were made. These varied from country to country depending on their fiscal capabilities, but at least a few of these measures were taken in every case. Moreover, it became a popular view during the period of external economic turbulence that the more open is the economy, the more severe the impact. The adverse effects of the global economic crisis on foreign trade and economic growth have ushered in calls for the export-oriented developing economies to rebalance their growth sources by choosing their domestic market for their own production (Kawai, 2009; Kuroda, 2009; Nag, 2009). Although this idea is correct and indeed timely, it may unconsciously provide a rationale for an increase in protectionism and the return to past import-substitution trade policies in these countries in the aftermath of the crisis.

This research seeks to better understand the impacts of the global economic crisis on Vietnam's foreign trade and policy responses, and from this, draw conclusions for Lao PDR and Cambodia. To this aim, it asks the following questions:

- To what extent was foreign trade of Vietnam affected by the global economic crisis?
- What were the policies by the Vietnamese government to arrest and reverse the decline in foreign trade?
- What lessons can Vietnam offer to Lao PDR and Cambodia for mutual advantages?

The rest of this paper is organized into **5** sections. The following section provides an overview of the impacts of the global financial crisis upon the Vietnamese economy, and discusses some key literature on the impact of the crisis on Vietnamese foreign trade. Section 3 analyzes the impacts of the crisis upon Vietnam's foreign trade in more detail. Section 4 reviews several policy responses of the Vietnamese Government. Section 5 discusses some important policy implications for Vietnam, Lao PDR and Cambodia.

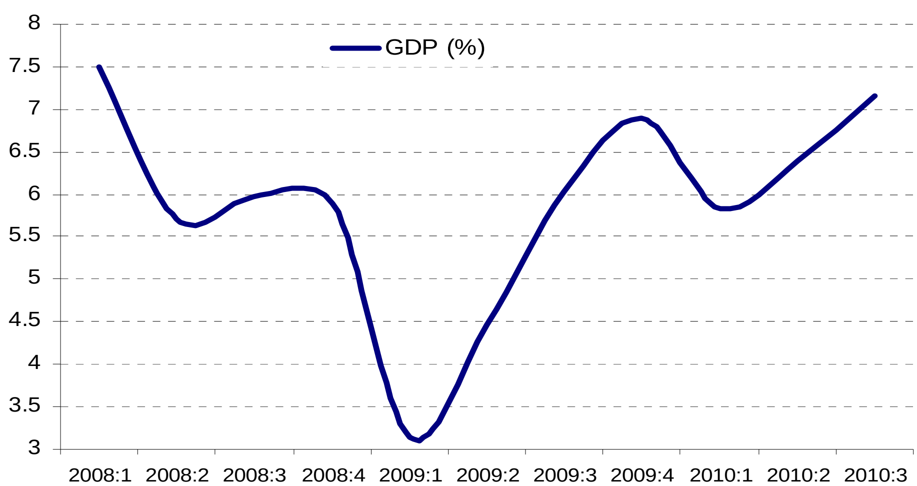
2. Overview of the Impact of the Global Economic Crisis on the Vietnamese Economy and Literature Review

Many economists initially insisted that the spillover effects of the US sub-prime mortgage crisis on the developing economies in Asia would be limited (Kawai, 2008). For the case of Vietnam, there was a reason to believe in this resilience because Vietnam's financial institutions were less exposed to the US sub-prime mortgage and structured financial products in other developed economies. Nonetheless, by the mid-2008, all optimism disappeared. The global crisis magnified the downturn cycle that Vietnamese economy had been experiencing since the end of 2007.

After its WTO accession, Vietnam experienced a surge in foreign investment, together with a boom in the stock exchange and the real estate sector. Rapid economic growth however became overheated, peaking in Q4 of 2007 at the cost of high inflation, which averaged 12.63% for the whole year. A contraction phase occurred in Q1 and Q2 of 2008. A soft landing of the economy did not happen in 2008, and its prospects were spoiled by the global economic recession.

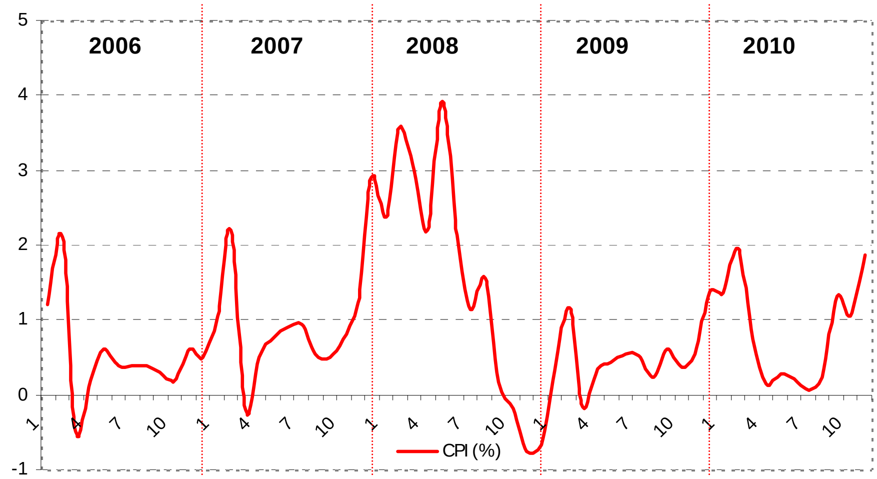
Figure 1 shows that the growth rate reached its trough in Q1 of 2009 at 3.14%, before picking up gradually to 4.46%, 6.04% and 6.9% in the consecutive quarters. The average economic growth rate in 2009 was 5.32% (GSO, 2009). Together with the world economy, the Vietnamese economy showed signs of recovery in 2010. The GDP growth rate moved up from 5.83% in Q1 and 6.4% in Q2 and 7.18% in Q3 of 2010 compared to the same period of 2009.

Figure 1: GDP Growth Rate by Quarter, 2008:1-2010:3



Source: General Statistics Office, 2010. Monthly Reports.

Figure 2: Monthly Inflation Rates



Source: General Statistics Office, 2010. Monthly Reports.

The inflation rate increased dramatically in the first half of 2008, reaching above 20% for the whole year. The increase in food commodity prices (20% in 2007 and 30% in 2008) contributed to the rise in inflation. The economic growth rate also fell from 8.6% in 2007 to 6.2% in 2008. An April 2009 study by the Ministry of Labor, Invalid and Social Affairs estimated that some 400,000-500,000 workers lost their jobs in 2009 as economic growth slowed further (laodong.com, 9/4/2009).

Figure 3: Some Key Indicators of the Vietnamese Economy, 2005 - 2010