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CURRENT INFLATION AND SOLUTIONS FOR STABILIZING INFLATION IN VIETNAM

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ABSTRACT

Inflation, a persistent rise in the general price level of goods and services, is one of the key indicators of macroeconomic stability. In Vietnam, inflation management is crucial due to its impact on living standards, business operations, and economic growth. From 2018 to 2023, Vietnam faced varying inflationary pressures caused by both domestic demand fluctuations and global economic changes. This paper provides an overview of the inflation trends during this period, a theoretical framework on inflation, an analysis of Vietnam's current inflationary status, and proposed solutions. Additionally, forecast for 2024 will be discussed.

KEYWORDS:- Inflation, Vietnam, Economic growth.

1. INTRODUCTION

Inflation is one of the most important macroeconomic indicators that reflects the health of an economy. Inflation is a common macroeconomic phenomenon, having profound effects on the economic, political and social aspects of countries during stages of economic development. The cause of inflation in the period 2018-2022 is the sharp increase in food and fuel (gasoline, oil) prices in the world along with the disruption of supply chains due to the impact of the COVID-19 pandemic and conflict between Russia and Ukraine (General Statistics Office, 2022). However, inflation is still within the target range of central banks in the Asia-Pacific region and has not created economic instability in 2021.

In Vietnam, inflation has significant implications for economic growth, business development, and the well-being of citizens. Over the past few years, Vietnam has faced fluctuations in inflation driven by both domestic and international factors. This article explores the current state of inflation in Vietnam, provides a theoretical framework, examines the trends from 2018 to 2023, and proposes solutions for stabilizing inflation, with forecasts for 2024.

2. LITERATURE REVIEW AND THEORETICAL FRAMEWORK

There have been many research projects on inflation around the world. The studies used many different methods; most of them were in groups of countries, with a few studies for one country.

Mundell (1965) and Tobin (1965) describe a proportional relationship between inflation and growth. According to these economists, inflation will reduce the incentive to hold cash and people will shift to holding real assets. This increases investment in the economy and thus promotes economic growth.

Sidrauski (1967) emphasized that reasonably low inflation will make investing more attractive than holding cash because holding cash reduces its value faster than investing. When inflation occurs in the economy, there is always a time lag between the increase in output product prices and the increase in input cost prices, manifested in the lag in wage increases.

Tobin (1972) identified moderate inflation as a lubricant for the economy. Inflation helps manufacturers reduce the real cost of purchasing labor inputs, thereby increasing savings and investment. , encouraging them to expand production scale.

The study by Demirguc-Kunt and Ross Levine (1995) used data on 41 countries from 1986 to 1993 to examine how rising inflation would affect the financial system. Inflation is measured by market size, concentration, market fluctuations, financial institution development and the international impact of inflation. The level of inflation increase is closely related to the development of the banking system and non-bank financial institutions.

For some open economies but exchange rates are not completely flexible, inflation can cause a trade balance deficit. The competitiveness of a country with high inflation will be impaired by its adherence to fixed nominal exchange rates (Hossain & Chowdhury, 1996).

Griffin (1998) believes that to evaluate inflation, it is necessary to evaluate the scale, depth, and liquidity of the market. The research results also agree on the positive relationship between economic growth and inflation measurement variables.

Besides, high inflation also distorts taxes (Romer, 2001), reducing the savings motivation of depositors, and savings are the source of investment. High inflation also causes "shoe wear costs", "menu costs", "confusion and inconvenience" (Vu Kim Dung & Nguyen Van Cong, 2012).

Khan &Senhadji (2001) analyze the threshold effect between inflation and growth using a data set covering 140 countries from the period 1960-1998. Empirical results show that there exists a threshold beyond which inflation causes negative impacts on growth. On the contrary, below the inflation threshold has no impact or positive impact on economic growth. The results also show that this threshold is small for developed countries (1%-3%), compared with developing countries (11%-12% respectively).

Research by James Laurenson (2002) concluded that China's inflation in the period 1995 - 2000 did not really affect economic growth because inflation was not meaningful to improve the innovation process of state-owned companies. And improve China's economic growth. Research also shows that inflation is not related to increase funding for economic reforms in China. Therefore, the function of mobilizing savings and distributing resources is affected by inflation in China.

Charles AmoYartey& Charles Komla Adjasi (2006) studied stock market developments in African countries that affect inflation and economic growth. Research has shown that there is a positive effect of inflation on economic growth in Africa.

In normal economic situations, money supply increases faster than real output, causing inflation. Increasing the money supply aims to maintain high growth rates over a long period of time. However, when the imbalance between the money supply growth rate and GDP growth rate is large, inflationary pressure begins to appear. On the other hand, investing in building more schools, educational facilities, research institutes, increasing salaries for staff, building factories, enterprises... will contribute to improving the quality of human resources and qualifications. Science and technology, meeting infrastructure conditions to serve economic development requirements.

Inflation, commonly defined as the general rise in prices, can occur due to various factors. Economists generally categorize inflation into three types:

- Demand-pull inflation: This happens when aggregate demand in the economy surpasses aggregate supply. Increased consumer demand drives prices higher as businesses struggle to keep up with demand.
- Cost-push inflation: This type of inflation occurs when the cost of production increases. Factors such as rising wages, raw material prices, and energy costs lead businesses to raise prices to cover their expenses.
- Built-in inflation: Also known as wage-price inflation, this occurs when workers demand higher wages to keep up with rising prices, and businesses raise prices further in response to higher labor costs.

The Phillips Curve theory postulates a short-term inverse relationship between inflation and unemployment, suggesting that lower unemployment might come with higher inflation and vice versa (Friedman, 1968). However, Vietnam’s inflation dynamics are affected by both domestic factors, such as rising consumer demand, and external factors, including global supply chain disruptions and energy price volatility.

3. INFLATION TRENDS IN VIETNAM (2018-2023)

Vietnam’s inflation from 2018 to 2023 has followed a variable path, influenced by a range of economic conditions:

- 2018: Inflation reached 3.54%, driven by higher global oil prices and increases in food prices domestically. The government aimed to keep inflation below 4%, and managed to do so through monetary and fiscal interventions (General Statistics Office [GSO], 2019).
- 2019: Inflation eased to 2.79% as global energy prices stabilized, and Vietnam's economy grew steadily. Government efforts to maintain macroeconomic stability helped keep inflation under control (GSO, 2020).
- 2020: Due to the global COVID-19 pandemic, inflation climbed to 3.23%. Supply chain disruptions and increased healthcare spending contributed to rising costs, though reduced demand offset some price hikes (World Bank, 2021).
- 2021: Inflation fell to 1.84%, largely due to reduced demand during the pandemic. Lockdowns and decreased economic activity kept inflation low, although the government remained cautious about inflation risks as the economy began to recover (GSO, 2021).
- 2022: Inflation rose again to 3.15%, driven by a surge in global energy prices and the impact of geopolitical events, particularly the Russia-Ukraine conflict. The conflict led to disruptions in oil and food supplies, which affected global prices (International Monetary Fund [IMF], 2022).
- 2023: As of mid-2023, inflation stood at 3.2%. Domestic demand picked up as the economy recovered from the pandemic, and inflationary pressures from global energy markets persisted. The government and the State Bank of Vietnam (SBV) employed various measures to keep inflation under control, including interest rate hikes and fiscal tightening (SBV, 2023).

4. CURRENT SITUATION AND CHALLENGES IN CONTROLLING INFLATION

In 2023, inflation remains a pressing concern for Vietnam, driven by both external and internal factors. Some key challenges include:

- Rising Global Commodity Prices: Vietnam's dependence on global markets makes it susceptible to external shocks, particularly rising global energy and commodity prices. Vietnam relies heavily on imports of fuel and raw materials. Global price increases, particularly in energy markets, have resulted in cost-push inflation domestically. Geopolitical tensions, such as the Russia-Ukraine conflict, have added further instability to these prices.
- Domestic Demand Growth: With the economy recovering from the pandemic, domestic consumption has risen, which has led to demand-pull inflation. Rising wages and increased spending on goods and services have contributed to inflationary pressures.This is particularly evident in urban areas, where rising wages and improved living standards are fueling higher demand for goods and services.
- Supply Chain Disruptions: Although the worst of the COVID-19 pandemic is over, global supply chains have not fully recovered. Continued disruptions in logistics and production have affected the availability of certain goods, pushing up prices.
- Production Costs: Higher costs for raw materials, fuel, and labor have increased the cost of production for many industries. Businesses, facing increased production costs, have passed these on to consumers in the form of higher prices, which contributes to inflation (World Bank, 2023).

5. MEASURES TO CONTROL INFLATION IN VIETNAM

The Vietnamese government has implemented several measures to manage inflation, focusing on both monetary and fiscal policies:

- Monetary Policy Adjustments: The SBV has actively used interest rates to control inflation. By raising interest rates, the SBV aims to reduce credit growth and consumer spending, which helps ease inflationary pressures. Additionally, the SBV has employed open market operations to manage liquidity and stabilize the economy (SBV, 2023).

- Exchange Rate Management: Stabilizing the Vietnamese dong (VND) is essential to controlling imported inflation. The SBV closely monitors and manages the exchange rate to prevent fluctuations that could drive up the costs of imports, particularly energy and other essential goods (IMF, 2022).
- Fiscal Policies: The government has adopted a cautious fiscal stance, avoiding excessive spending that could fuel inflation. In particular, Vietnam has been cautious with public investment projects and has implemented tax policies to keep inflation in check. For example, the government has provided subsidies and tax relief for essential goods such as fuel and staple foods (Ministry of Finance, 2023).
- Price Stabilization Programs: Vietnam has implemented price stabilization policies for essential goods like gasoline, rice, and other staples to prevent sharp price increases, particularly during periods of high inflation. These programs include subsidies for vulnerable groups and maintaining strategic reserves to mitigate supply shortages (GSO, 2023).

6. FORECAST FOR 2024

Looking forward, inflation in Vietnam is expected to remain under pressure, though forecasts suggest it will stay within manageable levels. According to the World Bank and IMF, inflation in Vietnam is projected to average between 3.5% and 3.8% in 2024.

Vietnam's annual inflation rate edged up to 4.44% in May, nearing the government's target ceiling of 4.5% for the year and a potential challenge to efforts to boost credit growth to drive activity. Consumer had risen 4.4% in April from a year earlier, and rose 3.25% in 2023.Vietnam is targeting economic growth of 6.0%-6.5% this year, faster than an expansion of 5.05% last year. The central bank, the State Bank of Vietnam, is aiming for credit growth of 15% to help meet the growth goal, but banks have struggled to increase their lending this year. Banks as of May 10 had risen 1.95% from the end of last year, state media cited the central bank. Several factors will influence inflation trends in the coming year:

- Global Energy Prices: If global energy markets stabilize, this could ease some of the inflationary pressures. However, any renewed geopolitical tensions or supply chain disruptions could push prices higher.
- Domestic Demand: With continued economic recovery, domestic consumption is expected to rise. This may place additional pressure on prices, particularly in sectors such as housing, services, and food. This will require careful balancing by the government and the SBV to manage inflation while supporting growth.
- Supply Chain Resilience: Vietnam is investing in strengthening its domestic supply chains, which should help mitigate inflationary pressures caused by global disruptions. However, it will take time for these investments to fully materialize (World Bank, 2023).

7. SOLUTIONS FOR STABILIZING INFLATION

To ensure inflation remains stable in the medium and long term, Vietnam can implement the following measures:

- Flexible Monetary Policies: The SBV should continue to monitor inflationary pressures and adjust interest rates as needed. Transparent communication of monetary policy decisions will help guide market expectations and keep inflation stable.

- Improving Energy Independence: Reducing reliance on imported energy is crucial. Investments in renewable energy sources, such as solar and wind power, will help shield Vietnam from global energy price shocks and stabilize domestic energy costs.
- Enhancing Productivity: Boosting productivity in key sectors like agriculture, manufacturing, and services can help reduce inflationary pressures by lowering production costs. Government support for technological innovation and workforce training will be vital in achieving this.
- Strengthening Domestic Supply Chains: Vietnam should prioritize building more resilient domestic supply chains, particularly in key industries like agriculture and manufacturing. This will help reduce dependence on global markets and protect the country from external supply chain disruptions.

8. CONCLUSION

Inflation remains a significant challenge for Vietnam as the country navigates both domestic economic recovery and global economic uncertainty. From 2018 to 2023, inflation has been influenced by rising global commodity prices, domestic demand growth, and supply chain disruptions. While the government and the SBV have implemented effective measures to manage inflation, further efforts will be needed to ensure long-term stability. By adopting flexible monetary policies, investing in energy independence, and strengthening domestic supply chains, Vietnam can stabilize inflation and support sustainable economic growth in the coming years.

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