

# The Real Effective Exchange Rate and Vietnamese Trade Performance in the Period 1992-2014

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**ABSTRACT:** This paper investigates whether the conduct of exchange rate policies in Vietnam has been conducive to the preservation of external competitiveness over the 1992-2014 period. Two main analysis methods are employed: descriptive analysis and econometric analysis. The co-integration technique is applied to investigate the relationship between the real effective exchange rate (REER) and trade performance. The results of the econometric analysis indicate that there exists a long-run relationship between REER and exports as well as imports. In the meantime, REER generally showed an appreciating trend. This suggests that the conduct of exchange rate policies tended to contribute to the deterioration in the country's external competitiveness over the studied period, thus leading to the persistent trade deficit in the past. Overall, the findings suggest that monitoring the equilibrium real exchange rate and adjusting misalignment in time appears to be a crucial tool for the authorities to ensure the external balance for the economy.

**KEYWORDS:** Exchange rate regime, real effective exchange rate, REER and NEER, trade balance.

## 1. Introduction

The exchange rate is an important macroeconomic variable in any open economy. It can exert considerable influence on inflation, trading performance, financial stability and the functioning of the foreign exchange market (Ho & McCauley, 2003). Countries in the world have adopted different exchange rate regimes for objectives as diverse as inflation control, volatility reduction, and compet-

itiveness improvement (Friedan, Ghezzi and Stein, 2001). In Vietnam, however, the exchange rate only started to become central to economic policy-making in the late 1980s, when embarking on the transitional path from the central planning economy to a market-oriented one.

Despite the many changes implemented in the exchange rate setting arrangements, administrative mechanisms have been

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