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FISCAL DEFICITS AND GROWTH IN VIETNAM: RETHINKING THE TRADE-OFF IN A TRANSITIONAL ECONOMY

DÉFICES FISCAIS E CRESCIMENTO NO VIETNÃ: REPENSANDO O TRADE-OFF EM UMA ECONOMIA EM TRANSIÇÃO

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Abstract
This study explores the relationship between fiscal deficits and economic growth in Vietnam over the period 2000-2024. Drawing on modern macroeconomic theory and prior empirical research, the analysis employs a Vector Error Correction Model (VECM) using time series data from the World Bank to examine how fiscal deficits and current account balances affect real GDP growth. The results indicate a long-run cointegration among the variables, suggesting a stable equilibrium relationship. In the short run, fiscal deficits exert a negative influence on economic growth, although the effect is statistically insignificant. In the long run, fiscal deficits appear to have no measurable impact on growth, challenging conventional views on the deficit-growth trade-off in transitional economies. Based on these findings, the study recommends strengthening fiscal discipline, improving the efficiency of public expenditure, and adopting policies that promote sustainable economic development. The research contributes to the broader discourse on fiscal sustainability and offers practical insights for policymakers navigating Vietnam's evolving economic landscape.

Keywords: Fiscal Deficit. Economic Growth. VECM Model. Current Account Balance.

Resumo
Este estudo explora a relação entre déficits fiscais e crescimento econômico no Vietnã no período de 2000 a 2024. Com base na teoria macroeconômica moderna e em pesquisas empíricas anteriores, a análise emprega um Modelo de Correção de Erros Vetoriais (VECM) utilizando dados de séries temporais do Banco Mundial para examinar como os déficits fiscais e os saldos em conta corrente afetam o crescimento real do PIB. Os resultados indicam uma cointegração de longo prazo entre as variáveis, sugerindo uma relação de equilíbrio estável. No curto prazo, os déficits fiscais exercem uma influência negativa sobre o crescimento econômico, embora o efeito seja estatisticamente insignificante. No longo prazo, os déficits fiscais parecem não ter impacto mensurável sobre o crescimento, desafiando as visões convencionais sobre o trade-off déficit-crescimento em economias em transição. Com base nessas descobertas, o estudo recomenda o fortalecimento da disciplina fiscal, a melhoria da eficiência dos gastos públicos e a adoção de políticas que promovam o desenvolvimento econômico sustentável. A pesquisa contribui para o discurso mais amplo sobre sustentabilidade fiscal e oferece insights práticos para formuladores de políticas que navegam no cenário econômico em evolução do Vietnã.

Palavras-chave: *Déficit Fiscal. Crescimento Econômico. Modelo VECM. Saldo da Conta Corrente.*

1 INTRODUCTION

In recent decades, fiscal deficits have emerged as one of the most pressing macroeconomic concerns in many developing countries, including Vietnam. Simply put, a fiscal deficit occurs when government expenditures exceed budget revenues over a given period. This phenomenon not only serves as an indicator of public financial management efficiency but also has far-reaching implications for key macroeconomic variables such as interest rates, private investment, inflation, the balance of payments, and, most notably, economic growth.

From a theoretical perspective, different schools of economic thought offer contrasting views on the relationship between fiscal deficits and economic growth. Keynesian economists argue that fiscal deficits can play a constructive role in stimulating aggregate demand, particularly during periods of economic downturn. In contrast, classical and neoclassical economists emphasize the crowding-out effect, suggesting that budget deficits lead to higher interest rates, which in turn reduce private investment and hinder growth. Meanwhile, the Ricardian Equivalence theory posits that individuals anticipate future tax increases to offset current deficits, thereby adjusting their consumption behavior in a way that neutralizes the impact of fiscal policy.

Following the initiation of economic reforms in 1986, Vietnam has witnessed remarkable structural transformation. Vietnam's economy has undergone a profound transformation from a centrally planned system to a socialist-oriented market economy. Throughout this transition, fiscal policy has played an increasingly critical role in regulating economic cycles and promoting growth. However, Vietnam's budget deficit has remained persistently high over the years. According to data from the Ministry of Finance of Vietnam (2025), the deficit has shown a rising trend, particularly evident after 2020. The period from 2020 to 2024 recorded elevated deficit levels, reflecting the impact of the COVID-19 pandemic and the expansionary fiscal measures adopted to support economic recovery. In 2024, the deficit was estimated at approximately VND 200 trillion, significantly higher than in the 2010-2015 period. This situation poses challenges for public expenditure control and may exert upward pressure on interest rates, reduce the effectiveness of private investment, and threaten macroeconomic stability.

In the context of Vietnam's pursuit of green and sustainable growth, alongside its deepening integration into the global economy, evaluating the impact of fiscal deficits on

economic growth has become a pressing requirement, both theoretically and practically. From a theoretical standpoint, this study contributes to testing economic hypotheses within the specific conditions of a developing economy, where financial markets remain underdeveloped and regulatory mechanisms are still evolving. On the practical side, the findings offer empirical evidence to inform policymakers in designing sound fiscal strategies that ensure budget sustainability and foster long-term economic growth. Moreover, this research seeks to address a gap in the current academic literature, where quantitative studies on the relationship between fiscal deficits and economic growth in Vietnam remain limited, particularly those employing modern econometric techniques. A deeper analysis of this relationship not only enhances understanding of the direct and indirect effects of fiscal deficits but also opens new avenues for evaluating the effectiveness of fiscal policy in developing countries.

2 LITERATURE REVIEW

The impact of fiscal deficits on economic growth remains a deeply contested issue in economics. Clearly, there is no consensus among economists regarding this relationship. Drawing on the concepts proposed by Keynes (2015), it is argued that high fiscal deficits are not necessarily abnormal for developing economies, as governments often use deficit spending to sustain high levels of aggregate domestic demand, thereby promoting growth and employment.

High fiscal deficits may contribute to capital accumulation and economic expansion (Chandrasekhar, 2022; Gllogjani & Balaj, 2021; Murty & Soumya, 2007). Proponents of the Keynesian approach suggest that increased fiscal deficits particularly through public investment in infrastructure can stimulate private sector growth. Accordingly, expanding public investment within a coherent policy framework may generate sufficient momentum to encourage large-scale private investment, ultimately leading to overall economic growth. This phenomenon is commonly referred to as the "positive crowding-in" effect of fiscal deficits.

In contrast to Keynesian perspectives, classical and neoclassical economic theories argue that elevated fiscal deficits especially those driven by increased public investment may crowd out private investment and dampen overall economic activity. This crowding-out effect operates through multiple channels. First, government borrowing to

finance persistent deficits raises interest rates, thereby discouraging private investment (Makin, 2018). Second, public expenditure increases aggregate consumption, which reduces national savings and further elevates interest rates (Bailey, 1995; Mawejje & Odhiambo, 2020). In a closed economy, this dynamic leads to a contraction in private sector investment and output. In open economies, increased public investment may attract foreign capital inflows, causing real exchange rate appreciation. This appreciation reduces net exports and weakens economic performance (Kappler et al., 2013; Makin, 2018). The macroeconomic effects of large exchange rate adjustments are particularly pronounced in developing countries, where export growth slows and current account balances deteriorate. Empirical evidence from OECD countries shows that public investment can have either crowding-in or crowding-out effects depending on fiscal conditions and country-specific factors (Afonso & St. Aubyn, 2019). Moreover, the effectiveness of fiscal policy is contingent on the economy's proximity to full capacity. When operating near full employment, additional public spending may simply reallocate resources rather than stimulate output (Cavallo et al., 2017). In developing countries, deficit financing poses additional risks. It may lead to inflation, currency depreciation, and unsustainable debt levels, especially when financed through external borrowing (Hussain & Haque, 2017; Tanzi, 1989). These macroeconomic vulnerabilities underscore the importance of prudent fiscal management and institutional quality in mitigating the adverse effects of fiscal deficits.

The effectiveness of fiscal expansion has been increasingly questioned in contexts characterized by large budget deficits and high public debt-to-GDP ratios (Sundaram & Yermack, 2007; Sundararajan & Thakur, 1980). Critics argue that beyond the well-known crowding-out effect where public investment displaces private investment government spending may also be less efficient than the private investment it replaces, even when such spending is directed toward capital formation (Afonso & St. Aubyn, 2019; Trabelsi & Boujelbene, 2024).

Empirical evidence suggests that public investment efficiency varies significantly across countries, and in many developing economies, increased government expenditure has failed to yield proportional growth benefits due to inefficiencies in allocation and implementation (Makin, 2018; Mawejje & Odhiambo, 2020). Moreover, when fiscal expansion is financed through debt, especially in economies with already high debt burdens, it may lead to macroeconomic instability, including rising interest rates,

inflationary pressures, and exchange rate volatility (Bozatli et al., 2024; Ramu et al., 2018).

Recent studies also highlight that fiscal consolidation, when carefully designed to protect productive public investment, can mitigate short-term contractionary effects and even promote long-term growth (Ardanaz et al., 2024). In contrast, indiscriminate cuts to public investment during austerity periods may exacerbate economic downturns and reduce private sector confidence. In light of these findings, controlling fiscal deficits and improving the efficiency of public spending are seen as critical for sustaining long-term economic growth, particularly in economies facing structural debt challenges (Özmen & Mutascu, 2024; Rebelo, 1991).

Empirical studies have shown that efforts to stimulate aggregate demand through increased public consumption may result in the crowding out of both private consumption and private investment, without generating sustained positive effects on output growth. Moreover, public investment in the productive sectors appears to exert a negative influence on private investment. However, government spending on infrastructure tends to produce a positive crowding-in effect, encouraging private investment. Importantly, the magnitude of the fiscal deficit plays a critical role in this dynamic. The positive impact of public infrastructure investment on private investment is more likely to occur when the deficit is either stable or declining. Although perspectives on the crowding-out phenomenon vary, analysts at the Reserve Bank of India (RBI) largely agree that excessive government consumption expenditure particularly on wages, debt waivers, and subsidies has a detrimental effect on economic growth. This issue reflects the political economy of public spending and the quality of fiscal adjustment.

A distinct perspective from the classical, neoclassical, and Keynesian schools is offered by the Neo-Ricardian theory, as articulated by (Näslund, 1978). This framework posits that increases in public investment exert a neutral effect on the economy. Rational economic agents are assumed to adjust their spending behavior in response to changes in government expenditure, thereby neutralizing any real impact on output or aggregate savings.

However, the empirical support for Ricardian equivalence remains limited and inconclusive. Studies such as Ball et al. (1998) and Ball and Mankiw (1995) suggest that the theoretical neutrality proposed by Ricardian models does not consistently hold in practice. In the case of India, empirical findings tend to support both neoclassical and

Keynesian interpretations, indicating that the effects of fiscal policy are context-dependent and complex. As a result, drawing definitive policy conclusions remains challenging.

An alternative perspective suggests that while governments may need to increase public spending to stimulate economic activity, it is equally important to maintain fiscal discipline to avoid adverse macroeconomic consequences. According to several analysts, the recent trend of expansionary fiscal policy cannot be sustained indefinitely. There is a growing consensus that the upcoming budget should include a well-defined **exit strategy** to ensure fiscal sustainability, enhance the flexibility of monetary policy, improve the efficiency of public expenditure, and mitigate upward pressure on interest rates (Kumar & Kumar, 2010; Rangarajan, 2009; Rao, 2009).

Another line of argument warns that focusing solely on the headline fiscal deficit may be misleading. Off-budget liabilities and contingent fiscal risks such as hidden debt obligations and quasi-fiscal activities can pose significant threats to macroeconomic stability if not properly accounted for (Adam & Bevan, 2005; Bennett et al., 2004; Petrie et al., 2013). Shifting debt obligations off the official budget without reducing systemic risk does little to improve the overall fiscal outlook. To achieve fiscal stability, policymakers must adopt a comprehensive approach that goes beyond primary balance targets. This includes optimizing the composition of public spending between consumption and investment, designing efficient tax systems, and managing borrowing prudently (Claeys et al., 2010; Rangarajan, 2009; Singh & Srinivasan, 2004). The quality of fiscal adjustment particularly the efficiency and productivity of public expenditure plays a crucial role in determining long-term growth outcomes.

Table 1. Summary of key studies on fiscal deficit and economic growth

Author(s) (Year)	Country/Region	Methodology	Main Findings
Acharya et al. (2025)	China	Empirical analysis using banking sector data	Fiscal deficits intensify deposit competition and foster the expansion of shadow banking.
Adam and Bevan (2005)	Developing countries	Panel econometric analysis	Persistent fiscal deficits are associated with lower economic growth, particularly in low-income nations.
Alagidede et al. (2018)	Ghana	Fiscal optimization modeling	Fiscal deficits may support growth if managed prudently, but excessive deficits

			undermine economic performance.
Ali (2019)	India	Time series econometric analysis	Fiscal deficits exert a negative long-term effect on economic growth.
Amaegberi and Krokeyi (2024)	Nigeria	Econometric investigation	Fiscal deficits diminish economic efficiency and constrain growth.
Hussain and Haque (2017)	Bangladesh	ARDL time series model	Fiscal deficits adversely affect economic growth.
Kryeziu and Hoxha (2021)	Kosovo	Empirical analysis	Fiscal deficits are found to impede economic growth.
Kumar et al. (2025)	India	Empirical study	Large fiscal deficits are linked to reduced economic growth.
Matti (2024)	Pakistan & Afghanistan	Empirical analysis	Fiscal deficits negatively influence economic growth in both countries.
Muinga et al. (2024)	East African Community	Econometric modeling	Fiscal deficits are detrimental to regional economic growth.
Obed et al. (2024)	Iraq	Empirical analysis	Fiscal deficits have a negative impact on economic growth.

Source: Author's compilation.

Table 1 synthesizes a range of empirical studies investigating the relationship between fiscal deficits and economic growth across diverse national contexts. The methodologies adopted in these studies are predominantly empirical, including panel data analysis, time series econometric models (such as ARDL), and fiscal optimization approaches. Such methodological variety reflects the multifaceted nature of the topic and the need for context-specific analysis.

The findings reported in the table are not uniform. While the majority of studies such as those by Adam and Bevan (2005), Ali (2019), Hussain and Haque (2017), and Kumar et al. (2025) identify a negative association between persistent fiscal deficits and economic growth, some research highlights that well-managed deficits, particularly when directed toward productive investment, may support growth in certain circumstances e.g., (Alagidede et al., 2018). Furthermore, Acharya et al. (2025) provide evidence that fiscal deficits can influence financial sector dynamics, such as deposit competition and shadow banking.

Overall, the table underscores the importance of considering country-specific factors, including fiscal management quality, the effectiveness of public expenditure, and the

mechanisms used to finance deficits. These insights form a valuable basis for identifying research gaps and guiding future empirical work, particularly in the context of Vietnam.

3 METHODOLOGY

3.1 Econometric model

This study employs time series data spanning the period from 2000 to 2024. Secondary data were obtained from the World Bank database. Building upon prior research and established economic theories, the proposed empirical model is specified as follows:

$$GROW_t = f(FD_t, CA_t) \quad (1)$$

Where:

- $GROW_t$ (dependent variable) denotes the real GDP growth rate (measured in percentage), serving as a proxy for economic growth (Chikalipah & Makina, 2019; Khan et al., 2020; Tung, 2018).
- FD_t represents the fiscal deficit (measured in trillion VND).
- CA_t (control variable) refers to the current account balance (measured in billion USD).

3.2 Vector Error Correction Model (VECM)

According to George et al. (2008), in time series analysis, applying a VAR model to integrated series may lead to spurious regression results. To address this issue, two commonly recommended approaches are: (i) estimating the VAR model using differenced data, or (ii) employing the Vector Error Correction Model (VECM). In practice, the VECM is often preferred as it captures long-run relationships and yields more efficient parameter estimates. The VECM implementation procedure can be summarized as follows: Test for stationarity of the time series data; Estimate the

unrestricted VAR(p) model; Determine the optimal lag length using information criteria such as AIC (Akaike Information Criterion), SIC (Schwarz Information Criterion), and HQC (Hannan-Quinn Criterion); Specify the VECM model in the following form:

$$\Delta y_t = \Pi y_{t-1} + \sum_{i=1}^{k} \Gamma_i \Delta y_{t-1} + \mu + \varepsilon_t \qquad (2)$$

In this specification:

- y_t is an (n×1) vector of endogenous variables,
- μ is an (n×1) vector of constants,
- Γ_i denotes the short-run coefficient matrices,
- ε_t is an (n×1) vector of white noise error terms,
- and Π represents the long-run coefficient matrix.

Method 1: Trace test

The statistical hypotheses are:

$H_0 : \text{rank}(\Pi) \leq r$ (The number of cointegrating vectors is less than or equal to r)

$H_1 : \text{rank}(\Pi) > r$ (The number of cointegrating vectors is greater than r)

The test statistic is given by

$$\lambda_{\text{trace}}(r) = -T \sum_{i=r+1}^{n} \ln(1 - \hat{\lambda}_i) \qquad (3)$$

Where

- r denotes the number of cointegrating vectors,
- $\prod$ denotes Matrix of non-zero eigenvalues
- T is sample size
- $\hat{\lambda}_i$ denotes the estimated value of the ith eigenvalue
- n is the total number of eigenvalues, and the test statistic follows a chi-square distribution χ^2

Method 2: Maximum eigenvalue test

The statistical hypotheses are:

$H_0 : \text{rank}(\Pi) = r$ (The number of cointegrating vectors is equal to r)

$H_1 : \text{rank}(\Pi) = r + 1$ (The number of cointegrating vectors is equal to r + 1)

The test statistic is given by

$$\lambda_{\text{trace}}(r, r+1) = -T \sum_{i=r+1}^{n} \ln(1 - \hat{\lambda}_{i+1}) \qquad (4)$$

In empirical applications, the results of the Trace test and the Maximum Eigenvalue test are often consistent with each other.

4 RESULTS AND DISCUSSIONS

4.1 Data description

Descriptive statistics provide an overview of the dataset used in this study. Table 2 summarizes the variables collected over a 25-year period (2000-2024). The variable $GROW_t$, representing the real GDP growth rate, has an average value of approximately 6.33% during the study period. The range from 2.6% to 8.4% indicates a relatively stable economic growth, with a low standard deviation (1.37), suggesting minimal year-to-year fluctuations.

The variable FD_t, which captures the fiscal deficit, shows a negative average value (-96,965.66 billion VND), reflecting a persistent budget deficit over most of the period. The large standard deviation (102,770.50) and the wide range from -266,810 to +64,541.87 indicate substantial volatility, possibly driven by economic shocks or shifts in fiscal policy.

The variable CA_t, representing the current account balance, has a small positive mean (2.85 billion USD), suggesting a slight surplus trend. However, the high standard deviation (9.54) and the minimum value of -10.787 reveal that significant deficits

occurred in some years, while the maximum value of 28.047 points to periods of strong trade surplus or large capital inflows.

Table 2. Descriptive statistics

Variable	Obsevation	Mean	Standard deviation	Min	Max
GROWt	25	6.328	1.374	2.6	8.4
FD_t	25	-96,965.66	102,770.50	-266,810	64,541.87
CA_t	25	2.848	9.542	-10.787	28.047

Source(s): Author's Calculation Using Stata 17.

Franses and Kleibergen (1996) argue that most time series are not integrated at order I(0). Therefore, prior to conducting any analysis, it is essential to test whether the series are stationary. The stationarity of time series data plays a critical role in determining the validity and efficiency of the estimation methods employed. If the series are non-stationary, the assumptions underlying the Ordinary Least Squares (OLS) method are violated, rendering conventional statistical tests such as the t-test and F-test invalid (Brooks, 2021). To assess stationarity, two widely used approaches are the Dickey and Fuller (1979) test and the Phillips and Perron (1986) test. These tests help identify the presence of unit roots and determine the appropriate transformation of the data before model estimation.

Table 3. Results of unit root tests

Variable	Level form		First differenced	
	ADF	PP	ADF	PP
$GROW_t$	-2.473	-2.640	-3.831^{***}	-3.774^{**}
FD_t	-3.357	-3.326	-6.391^{***}	-7.057^{***}
CA_t	-2.453	-2.415	-4.571^{***}	-4.597^{***}

**** p<0.01, ** p<0.05, * p<0.1.*

Source(s): Author's Calculation Using Stata 17.

The results presented in Table 3 report the stationarity tests conducted using both the Augmented Dickey-Fuller (ADF) and Phillips-Perron (PP) methods. Based on the original (level) series, all time series variables are found to be non-stationary. However, after first differencing, the results indicate that all variables become stationary, suggesting that they are integrated of order one, I(1).

4.2 Johansen cointegration test

The Johansen cointegration test, developed by Johansen (1988), is a multivariate approach used to determine the presence and number of cointegrating relationships among non-stationary time series variables. Unlike the Engle and Granger (1987) method, which is limited to bivariate analysis, the Johansen procedure allows for testing multiple cointegrating vectors within a Vector Error Correction Model (VECM) framework.

Table 4. Results of the Johansen Cointegration Test
Method 1: Matrix trace

Hypothesis			**Trace**	**0.05**
H_0	**H_1**	**Eigenvalue**	**Statistic**	**Critical Value**
r=0	r >=1	.	33.8971	29.68
r<=1	r >=2	0.72771	3.9762*	15.41
r<=2	r>=3	0.14772	0.2999	3.76
Method 2: Maximum eigenvalue				
Hypothesis			**Eigenvalue**	**0.05**
H_0	**H_1**	**Eigenvalue**	**Statistic**	**Critical Value**
r=0	r =1	.	29.9208	20.97
r<=1	r =2	0.72771	3.6764*	14.07
r<=2	r=3	0.14772	0.2999	3.00

**** p<0.01, ** p<0.05, * p<0.1.*
Source(s): Author's Calculation Using Stata 17.

Table 4 presents the results of the Johansen cointegration test using both the Trace and Maximum Eigenvalue approaches. Under the null hypothesis H_0: r<=1 both test statistics Trace and Maximum Eigenvalue are found to be lower than the critical value at the 5% significance level. Consequently, the null hypothesis cannot be rejected, indicating the presence of one cointegrating vector in the model. Corresponding to the number of cointegrating vectors, the following cointegration equations are derived from the estimated Vector Error Correction Model (VECM)

Table 5. Estimation results of the VECM Model

Dependent variable: $\Delta GROW_t$	**Coefficient**	**Standard deviaton**	**Z**	**P>|Z|**
Adjustment Coefficient				
EC_{t-1}	-0.5461	0.1810	-3.02	0.003***
Short-run				
$\Delta GROW_{t-1}$	0.5693	0.2383	2.3900	0.0170**
ΔFD_{t-1}	-5.37e-06	2.97e-06	-1.81	0.071*
ΔCA_{t-1}	-0.0042	0.0364	-0.1200	0.9080

Cons	-0.2933	0.2438	-1.2000	0.2290
Long-run				
FD_t	2.54e-06	-1.20	-1.2	0.229
CA_t	0.0399859	3.39	3.39	0.001***
Cons	-7.280473			
Diagnostic tests				
R^2	0.8909			0.0000
JB	0.5473			0.0748
LM test	0.8143			0.5697
Vecstable				Stable

JB Test (Jarque-Bera Test): Tests whether the residuals follow a normal distribution. LM Test (Lagrange Multiplier Test): Checks for the presence of autocorrelation in the residuals. Vecstable Test: Examines the stability of the VECM model by verifying whether all eigenvalues lie within the unit circle.

**** p<0.01, ** p<0.05, * p<0.1.*

Source(s): Author's Calculation Using Stata 17.

The estimated results from the VECM model (Table 5) reveal the short- and long-term effects of independent variables on the dependent variable. In the short run, with a one-year lag, real GDP growth in the following year is influenced by its own value from the previous year. The coefficient is 0.5693, positive and statistically significant at the 5% level. This implies that, holding other factors constant, a one-unit increase in real GDP growth in the preceding year leads to an average increase of approximately 0.5693 units in the subsequent year.

Similarly, the study confirms that fiscal deficits have a negative short-term impact on economic growth, although the effect is relatively minor. The coefficient is -5.37e-06, statistically significant at the 10% level. This can be explained by the fact that rising fiscal deficits tend to increase pressure on macroeconomic variables such as interest rates, private investment, and market expectations. When government spending exceeds revenue, borrowing is often required to finance the deficit, which can push interest rates upward. Higher interest rates reduce access to capital for the private sector, thereby dampening investment and production. Moreover, large deficits may undermine confidence in fiscal stability, affecting consumer and investor sentiment. In a developing economy like Vietnam, where public spending efficiency remains limited, expansionary fiscal policy does not yield strong short-term growth effects.

On the other hand, the current account balance (CAt) does not show a statistically significant impact on real GDP growth in the short run, as indicated by the VECM results. This can be interpreted through both theoretical and practical lenses. First, the current account reflects the gap between national savings and investment, encompassing trade in goods and services, income flows, and international transfers. These components often

exhibit delayed effects on domestic production and consumption. For instance, a trade surplus may not immediately translate into growth if firms do not reinvest or if capital flows are not efficiently allocated. Second, short-term economic dynamics may be dominated by cyclical factors such as fiscal and monetary policy, market sentiment, or external shocks (e.g., oil price fluctuations, global interest rate changes), which can obscure the influence of the current account on GDP growth. Third, in developing economies like Vietnam, the current account tends to be volatile due to reliance on raw material exports, remittances, and short-term capital flows. These fluctuations may be temporary and not indicative of sustainable growth trends. Therefore, the lack of a significant short-term effect of the current account on real GDP growth is consistent with modern macroeconomic theory, especially in contexts where the components of CAt have not been effectively transformed into domestic growth drivers.

In the long run, the study finds no significant impact of fiscal deficits on real GDP, which may be attributed to the effective allocation of public spending toward productive investments, particularly in infrastructure and education. Such investments are likely to enhance productivity and support long-term growth. Additionally, factors such as foreign direct investment (FDI), exports, and institutional reforms appear to play a more prominent role in driving economic expansion, thereby offsetting the adverse effects of budget deficits. Conversely, the current account balance shows a statistically significant positive effect on real GDP growth in the long term (with the coefficient of CAt equal to 0.0399859 at the 1% significance level). This suggests that current account surpluses reflect the economy's ability to attract resources through exports, remittances, and foreign investment, contributing to capital accumulation and production expansion. When these capital inflows are channeled into infrastructure, technology, and productive capacity, they foster sustainable growth. Moreover, a stable current account helps maintain exchange rate stability, reduces inflationary pressures and public debt risks, and creates a favorable macroeconomic environment for fiscal and monetary policy.

Given Vietnam's open economy, export orientation, and reliance on FDI, it is highly sensitive to global cyclical factors. Therefore, in the long term, the current account balance serves as a key indicator of economic resilience and health, with a direct influence on real GDP growth. Furthermore, the adjustment speed toward equilibrium after each cycle of the GROWt variable is captured by the error correction coefficient (ECt-1). As shown in Table 5, the ECt-1 coefficient is negative and statistically significant at the 1%

level. This implies that when real GDP deviates from its equilibrium level due to macroeconomic shocks, it tends to adjust by approximately 54.61% in the following year. The negative and significant coefficient reflects the inherent stability of real GDP growth, suggesting that despite short-term fiscal shocks, the economy possesses a self-correcting mechanism that supports long-term growth trajectories.

The findings of this study indicate that fiscal deficits have a negative impact on economic growth in the short term, although the effect is relatively modest, and no significant long-term influence is observed. This outcome aligns with previous research, such as Kumar et al. (2025) and Muinga et al. (2024), which argue that public spending, if inefficient, fails to promote sustained growth. However, this study adds empirical evidence within the context of Vietnam a developing economy characterized by unique budget structures and public investment efficiency. The absence of a long-term effect may suggest that public expenditures have been directed toward productive sectors such as infrastructure, education, and technology, thereby offsetting initial adverse impacts. Moreover, the positive role of the current account balance in the long run underscores the importance of exports, remittances, and international capital flows in driving economic growth.

From a theoretical perspective, the findings support the Keynesian view in the short run, while leaning toward Ricardian Equivalence in the long run. Practically, the results provide scientific evidence for policymakers in designing medium-term fiscal strategies that enhance public spending efficiency and maintain macroeconomic stability. This represents a meaningful contribution in the context of Vietnam's dual challenge: sustaining growth while ensuring fiscal discipline.

5 CONCLUSION

This study sheds light on the relationship between fiscal deficits and economic growth in Vietnam over the period 2000-2024, utilizing the Vector Error Correction Model (VECM) and a series of econometric tests. The results indicate the presence of a long-run cointegration relationship among the variables, particularly between fiscal deficits and real GDP growth. In the short run, fiscal deficits exert a negative impact on economic growth, although the magnitude of the effect is relatively modest. In contrast, long-run dynamics reveal that macroeconomic factors such as the current account balance

have a more pronounced influence on growth, reflecting the structural characteristics of the Vietnamese economy, an economy shaped by cyclical fluctuations and fiscal policy interventions.

From a policy perspective, the findings of this study offer several important implications. First, maintaining fiscal deficits at a reasonable level is essential to avoid upward pressure on interest rates and private investment, while ensuring the sustainability of public finances. Second, public expenditure should be restructured to enhance efficiency, particularly by prioritizing investments in sectors capable of generating "positive crowding-out" effects, such as infrastructure, education, and technology. Third, a clear medium-term fiscal strategy is needed one that balances macroeconomic stability with growth objectives and avoids prolonged fiscal expansion that could destabilize the budget. In the context of Vietnam's growing challenges including population aging, climate change, and deepening global economic integration controlling the budget deficit is not merely a technical financial requirement but also a matter of political economy. The government must strengthen budget transparency, improve public debt management, and enhance spending efficiency to ensure stable and sustainable economic growth. In conclusion, this study confirms that fiscal deficits do affect Vietnam's economic growth, particularly in the short term. However, this impact can be mitigated through well-designed and effective fiscal policies that are oriented toward long-term development. These insights provide a critical foundation for shaping future fiscal strategies aimed at achieving sustainable and stable economic growth.

From a policy standpoint, the short-run findings suggest that fiscal deficits exert a mildly negative impact on economic growth, primarily through upward pressure on interest rates and reduced private investment. This underscores the importance of maintaining fiscal discipline to mitigate macroeconomic risks. Additionally, the study reveals that the current account balance has a positive long-term effect on growth, highlighting the role of international capital flows and export performance in driving production. Accordingly, fiscal policy should be designed to support sectors with strong spillover potential such as infrastructure, education, and technology while ensuring budget sustainability. The absence of a significant long-term effect of fiscal deficits further implies that the efficiency of public spending may offset adverse impacts, emphasizing the need for greater transparency and effectiveness in budget allocation. These findings carry theoretical relevance by testing economic hypotheses within the

Vietnamese context, and practical value in guiding the formulation of medium-term fiscal strategies aligned with the goals of stable and sustainable growth.

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Authors' Contribution

Both authors contributed equally to the development of this article.

Data availability

All datasets relevant to this study's findings are fully available within the article.

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