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VIETNAM'S REAL ESTATE DEVELOPERS ARE FACING LIQUIDITY ISSUES DESPITE STRONG DEMAND FOR NEW HOUSING

Over the last year, liquidity issues have been mounting for Vietnam's real estate developers, culminating with last week's announcement that Novaland, one of the country's largest developers, missed a payment on one of its outstanding bonds¹. Emerging Markets are notoriously prone to real estate boom and bust cycles, characterized by *overbuilding* of new housing units, but Vietnam's housing market is *undersupplied*; developers' current cash flow problems were not caused by insufficient demand for their products. The demand for new housing units in Vietnam by prospective owner-occupiers vastly outstrips the annual supply of new units,² and mortgage penetration in Vietnam is still modest at around 20%/GDP.

Consequently, the primary problem developers are facing is difficulty rolling-over their outstanding debts, which they need to do in order to complete their outstanding projects and repay loans. This "liquidity gap" problem will likely be solved with Government policies, but not with Government money. Furthermore, we do not expect a significant increase banks NPLs since there is (very) limited room for a drop in Vietnamese housing prices given then enormous discrepancy between the demand and supply of new housing units.

Understanding the Problem – and the Possible Solutions

Real estate developers in Vietnam have been experiencing difficulty accessing credit for months and some are now facing difficulties refinancing their maturing bonds. The problem largely stems from difficulties developers face securing approvals for their projects because banks require proper approvals/documentation in order to extend loans collateralized by those projects. That said: 1) some developers overextended themselves by taking on too many "high end" development projects that are not suitable for emerging middle-class homebuyers, 2) liquidity in Vietnam's banking system is particularly tight at present, and 3) developers are facing structural issues accessing liquidity that we discussed in [this report](#).

¹ <https://www.bloomberg.com/news/articles/2023-02-23/vietnam-property-woes-deepen-as-no-2-firm-delays-bond-payment>

² We (and others) estimate that the number of new housing units being built in Vietnam meets less than half of the annual demand, which is being driven by urbanization, demographics and per-capita GDP growth.

Vietnamese real estate developers do not have access to sufficient long-term funding to support their “land banking” activities. Said differently, the raw land that developers own does not become “bankable” until that land has been rezoned for residential usage and project approvals have been secured. In recent years, developers increasingly met their funding needs with the issuance of two-year corporate bonds that were largely purchased by retail investors as an alternative to bank deposits. However, some developers used the funds from bond issuances for purposes other than those spelled out in the bonds’ prospectuses, prompting some high-profile arrests as well as a crackdown on corporate bond issuance via the new, highly publicized “Decree 65” legislation.

Over the last few weeks, Government officials and industry executives intensified their discussions aimed at solving the issues in Vietnam’s real estate market, resulting in a range of initiatives and proposals, including:

Recent Initiatives	Details
Expedite Approvals on 7 HCMC Projects	<ul style="list-style-type: none">• Preliminary initiative to address obstacles related to project approvals (e.g., auction of land use rights, land-use fee payment, eligibility for sales).
A Government-Backed ~USD10b Credit Package for Developers & Homebuyers	<ul style="list-style-type: none">• Subsidized loans to homebuyers & developers.• Focused on affordable housing.• Funds sourced from 2-3%/GDP liquidity injection by the State Bank of Vietnam.
Temper New Restrictions on the Corporate Bond Market	<ul style="list-style-type: none">• Amendments to Decree 65 that would effectively walk back some new regulations have been under discussion for 3 months.• Current proposals include the ability for bond issuers to delay re-payment by 2 years, and payment-in-kind instead of in cash (i.e., bond investors could potentially be repaid in shares or real estate).

Two weeks ago, Vietnam’s prime minister held a conference on the country’s real estate sector, which was focused on resolving the issues currently impeding Vietnam’s real estate development industry. This meeting was attended by civil servants from various Government ministries, local Government officials, and senior executives from major developers and banks. Additionally, last week, the Vice Chair of HCMC People’s Committee held a widely publicized meeting to review seven HCMC projects that have been delayed due to legal approval/zoning issues – including two projects owned by Novaland.

At the first meeting, Prime Minister Pham Minh Chinh criticized developers for focusing on the development of high-end housing rather than on providing reasonably priced units to the market and requested Government agencies “at all levels” to remove obstacles impeding the project approval process. Most Vietnam real estate experts (including VinaCapital’s VinaLiving real estate

team) believe that the slow approval process is the biggest issue currently facing the sector, but many of the country's civil servants are reportedly wary of signing off on new projects³ according to Bloomberg and others.

Addressing Developers' Liquidity Issues

The possibility of two new Government-backed loan packages that would each flow circa USD5 billion of new credit to both developers and homebuyers was raised at the meeting led by the prime minister. In our understanding, the details of these potential new loan programs are still being worked out, but the focus would be on financing the development and purchase of affordable housing, and the programs would likely be administered through state-owned commercial banks (SOCBs), with the funds ultimately provided to the SOCBs directly from Vietnam's central bank.

Next, the Government introduced new regulations on Vietnam's corporate bond market last year that severely impeded developers' ability to re-finance / roll-over maturing corporate bonds. However, protracted discussions on modifications to "Decree 65" that could effectively ease some of those new restrictions have progressed to the point that it now seems possible that developers will be able to repay a significant proportion of their maturing corporate bonds in the form of real estate and/or newly issued shares. Also, the implementation of restrictions on retail investors (who were major buyers of corporate bonds) purchasing newly issued bonds may be delayed by one year.

Tight Liquidity in Vietnam's Banking System

Mortgage rates in Vietnam are currently above 12%, which is too high for some prospective home buyers, while deposit rates at private sector banks are over 8% for 1-year deposits. Investors who would typically purchase apartments to earn an investment yield are instead parking their money in bank deposit accounts. We believe that a circa 2%pts decrease in 6-12 month deposit rates to ~6%, coupled with a 1-2% depreciation in the value of the VN Dong, could prompt savers to move money from bank deposits into rental properties and stocks, but it may be difficult for deposits to drop much in 2023 since credit growth outpaced deposit growth by about 3%pts annually over the last three years, leaving Vietnam's system-wide loan-to-deposit (LDR) ratio (as it would be calculated in most jurisdictions) near 100% at end-2022.

The Government could help lower the system-wide LDR by injecting more liquidity into the economy by: 1) rebuilding the SBV's FX reserves⁴, which could inject circa USD20 billion into the economy this year, 2) funding the above-mentioned circa USD10 billion Government-backed loan packages

³ <https://www.bloomberg.com/news/articles/2023-02-22/-do-nothing-bureaucrats-are-imperiling-vietnam-s-economic-boom>

⁴ The State Bank of Vietnam typically accumulates FX Reserves via "unsterilized" purchases of US Dollars with newly printed VN Dong.

via the SBV's re-financing window, and 3) the Government currently has over USD20 billion of undisbursed infrastructure funds sitting at the central bank and could run down some of that balance in order to meet its target of spending USD30 billion on infrastructure development this year.

Finally, we expect Vietnam's nominal GDP (i.e., including inflation) to grow by about 10% this year, which would likely result in an organic increase of circa USD40 billion of bank deposits this year. If the Government were to inject USD40-50 billion of new liquidity into the country's economy, it is likely that bank deposit growth could outpace system-wide loan growth by circa 3%pts, which would lead to somewhat lower deposit rates in Vietnam (i.e., 13%pts loan growth versus 16% deposit growth).

Conclusions

The long-term prospects for Vietnam's real estate market remain strong. High economic growth is driving robust demand for new housing by the country's growing cohort of emerging middle-class consumers, but the number of new units suitable for those prospective home buyers is far below demand. Despite those favorable supply and demand dynamics, some Vietnamese real estate developers are facing liquidity challenges, primarily due to slow project approvals, so we are encouraged by the Government's recent actions to address these and other issues that developers face.

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