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VIETNAM'S GOVERNMENT HAS A PLAN TO BOOST ECONOMIC GROWTH

Vietnam's GDP growth slowed from 8% in 2022 to just 3.3% in Q1 2023, prompting the Government to launch several initiatives to boost the country's growth. These include tax cuts, monetary stimulus, and administrative measures aimed at easing the current difficult conditions in the real estate market, which we discussed in our previous reports and webinars¹. The details of these and other initiatives are discussed below; the key points are that the Government is proactively addressing the current growth slowdown and has ample fiscal resources to counter any continued growth headwinds (Vietnam's government debt-to-GDP ratio was just 40% at the end of 2022).

We are confident that policymakers can counter the growth slowdown, and that Vietnam's economic growth will rebound in the second half of 2023 for reasons discussed below – although it's unlikely that the Government can achieve its 6.5% GDP growth target this year. Stock markets typically climb in advance of economic recoveries, so the Government's mounting resolve to support economic growth, coupled with the fact Vietnamese stocks are currently trading at a near 10-year low valuation, make now an auspicious time to invest in Vietnamese stocks, in our view.

The Government's Recent Measures to Support Economic Growth

	Note
11-March-23	The Central Government Directs Relevant Ministries and the SBV to Ease Difficulties in Real Estate Market.
14-March-23	The SBV Cuts the Discount Rate by 100bp to 3.5%.
14-March-23	The Prime Minister Directs Relevant Ministries to Accelerate Public Infrastructure Spending.
27-March-23	The SBV Proposes to Relax Certain Conditions for Credit Institutions to Purchase Corporate Bonds.
31-March-23	The SBV Cuts the Deposit Rate Cap on 1-6 Month Deposits by -50bp to 5.5%, and Cut the Refinancing Rate by -50bp to 5.5%.
03-April-23	The Central Government Provides Guidance to Relevant Authorities to Address Legal Bottlenecks for Real Estate Market.
17-April-23	The Ministry of Finance Proposes to Cut Vietnam's VAT tax rate from 10% to 8% during H2.

¹ <https://vinacapital.com/wp-content/uploads/2023/03/20230203-VinaCapital-Insights-Vietnams-Real-Estate-Developers-are-Facing-Liquidity-Issues-Despite-Strong-Demand-for-New-Housing.pdf>

The current slowdown in Vietnam's economic growth is being caused by a drop in demand for "Made in Vietnam" products from US consumers, although orders at FDI factories in Vietnam are likely to recover in H2, which should help drive an economic rebound later this year. Manufacturing contributes nearly one-quarter of Vietnam's GDP and output contracted slightly in 1Q23 versus 9% growth in 2022, because most products produced in Vietnam are exported to the US and other developed countries. Note that Vietnam's international trade accounts for a higher percentage of the country's GDP than in any other nation in modern history (excluding city-states like Hong Kong and Singapore), so weaker demand in the rest of the world weighs fairly heavily on Vietnam's economy.

Specifically, Vietnam's exports fell 12% yoy in Q1, driven by a 20% drop in exports to the US. Meanwhile, inventories at US retailers and other consumer-facing firms such as Nike and Lululemon are now contracting, which is why we expect FDI factories' order books to start recovering later this year (inventory growth at US retailers peaked at over 20% yoy in late-2022, is currently around 10%, and looks likely to fall to 0% year-on-year growth in H2, which should prompt a resumption of order growth for FDI factories in Vietnam).

Finally, domestic consumption in Vietnam continues to grow at a healthy pace and consumer confidence has remained remarkably resilient despite the steep slowdown in GDP growth. That is partly because the number of people who are employed grew by over 2% yoy in Q1, which more than twice the country's population growth rate and we estimate that wages are up over 7% yoy, far outpacing CPI inflation which is just over 3%. In addition, foreign tourist arrivals rocketed to over 60% of pre-COVID levels in Q1, despite the fact that Chinese tourists have not yet returned to the country en masse - which is another reason we expect Vietnam's economic growth to recover in H2.

Measures to Support Growth

This week, Vietnam's Ministry of Finance (MOF) finalized a plan to cut Vietnam's VAT tax rate from 10% to 8% in 2H23, which will equate to about USD1.5 billion of stimulus for Vietnam's USD450 billion economy. The Government will also allow companies and individuals 3-6-month delays in the payment of various taxes. Last month, the State Bank of Vietnam (SBV) cut policy rates in Vietnam by 50-100bps, including a 50bp reduction in the re-financing rate (which is the most important policy rate in Vietnam) to 5.5%, and a 50bp reduction in the maximum interest rates banks are allowed to pay savers on deposits of up to 6 months to 5.5%.

In addition to those concrete steps to boost growth, the Government also walked back some new regulations that were introduced in late 2022 to impose stricter conditions on the issuance of corporate bonds. Vietnam's central Government also directed its ministries to address various administrative bottlenecks that are impeding real estate development and infrastructure projects. The tax cuts and policy interest rate cut are the most concrete actions the Government took to

support growth, but these administrative measures could potentially have a much bigger impact on economic growth.

Real estate development, which accounts for nearly 10% of Vietnam's GDP, has essentially ground to a halt, largely because of the difficulties developers are having obtaining the approvals required to proceed with their projects. Some of the micro-level issues that the Government's recent actions seek to address include bottlenecks entailed in converting agricultural land for use in residential real estate projects and delays in the appraisal of land values for the determination of land-use/conversion fees payable to the Government.

The Government also launched a USD5.1 billion subsidized loan package to support the development of over one million new affordable housing units (subsidized loans will be provided to both developers and home buyers via the state-owned commercial banks) and established a new working group to review and remove obstacles developers encounter in progressing their development projects. Further to that last point, the Government also established a working group to accelerate disbursement of public investment projects this year; it aims to increase infrastructure spending by about 40% in 2023 (to USD30 billion) but infrastructure spending increased by less than 20% yoy in Q1.

Finally, in addition to the administrative measures above, the Government also provided guidance intended to make it easier for banks to restructure loans extended to real estate developers, as well as to other borrowers, although the details of these proposed forbearance measures are still being hashed out².

Monetary Policy Easing

The interest rates that banks pay savers in Vietnam increased by over 200bps in 2022 to over 8% for 12-month deposits as of end-2022, although one-year deposit rates had climbed to above 9.5% at their peak in late-2022. This surge in deposit rates is an additional source of difficulties for the real estate market, compounding the administrative issues mentioned above that are impeding real estate development projects. Mortgage rates in Vietnam are linked to long-term deposit rates, and higher deposit rates encourage savers to park their money in the bank rather than seek out other investments (such real estate and/or investing in the stock market).

We believe that a 200bp drop in the average level of 12-month deposit rates from the levels at the beginning of this year (to circa 6%), would help drive a recovery in Vietnam's real estate market and would support Vietnamese businesses in general. The SBV's 50-100bp policy rate cut has put some downward pressure on long-term deposit rates – which have fallen by about 50bps YTD – but

² <https://theinvestor.vn/struggling-property-developers-entitled-to-debt-repayment-rescheduling-d4055.html>

for deposit rates to fall significantly further, liquidity in Vietnam's banking system will need to improve significantly.

Credit growth in Vietnam has outstripped deposit growth by about 3%pts annually over the last year, which has pushed up banks' loan-to-deposit ratios to unacceptably high levels and prompting banks to increase the interest rates they pay savers in order to raise deposits. The Government is addressing this liquidity shortage in a few ways, the most important of which is by purchasing US Dollars from commercial banks to increase its FX reserves.

We expect the SBV to purchase about USD25 billion of FX reserves this year, which would inject significant liquidity into the banking system and would likely boost Vietnam's system-wide deposit growth by 4%pts this year, *ceteris paribus*, because the central bank typically purchases USD from the country's commercial banks with newly printed VN Dong. In short, the SBV's purchases of FX reserves, coupled with the other measures the Government is taking to ease liquidity in the banking sector are even more important monetary easing measures than the SBV's policy rate cuts last month.

Finally, we mentioned above that the SBV cut the maximum allowable interest rate on 6-month deposits by 50bps last month. The interest rates on short term deposits in Vietnam had already peaked in late-2022, and the March policy rate cut will put additional downward pressure on those deposit interest rates. Consequently, there will be many bank deposits maturing in Q2 and Q3 and savers will essentially face a choice of rolling over their deposits at lower interest rates or plowing that money into the stock market (the vast majority of time deposits in Vietnam are 3-month and 6-month deposits).

Conclusions

GDP growth in Vietnam slowed precipitously in Q1 as consumers in the US and other developed markets bought fewer "Made in Vietnam" products. This was exacerbated by the on-going slowdown in the country's real estate market, although a rebound in foreign tourist arrivals is mitigating the negative impact of these two burdens on Vietnam's growth this year.

The Government has taken a series of initiatives to address the country's slowing growth, the most concrete of which are tax cuts and interest rate cuts, but administrative measures that are intended to ease bottlenecks impeding real estate development and infrastructure projects could have an even bigger impact to support growth in 2023 and beyond.

The Government's initiative to address disappointing Q1 GDP growth, coupled with the fact that FDI factories' orders are likely to accelerate in H2, leads us to expect a rebound in GDP growth in the second half of this year. The fact that stock markets tend to start climbing in advance of economic rebounds, coupled with the fact that the VN-Index is trading at around a 10-year low valuation, leads us to believe that now could be an ideal time for investors to selectively purchase Vietnamese

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stocks. We are encouraged to see that foreign investors have been net buyers YTD, so there are already some investors that are recognizing the attractiveness of the current entry point for Vietnamese stocks.

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