

Michael Kokalari, CFA

Chief Economist

MACRO HIGHLIGHTS FROM VINACAPITAL'S 2023 INVESTOR CONFERENCE

VinaCapital held its largest-ever annual investor conference two weeks ago, with investor enthusiasm bolstered by President Biden's visit recent to Vietnam and by the firm's continued solid performance across a variety of asset classes. The economics presentation that opens the conference each year highlights key economic growth drivers that support Vietnam's investment case over the long term and summarizes recent economic developments that tend to drive short-term stock market fluctuations. This year's key points included:

- The elevation of the US-Vietnam diplomatic relationship to a "Comprehensive Strategic Partnership" will drive another wave of FDI investment to Vietnam.
- Vietnam's GDP will likely grow by less than 5% in 2023 due to lower demand for "Made in Vietnam" products.
- Vietnam's central bank hiked interest rates in 2022 to protect the value of the VN Dong, but a stable USD-VND exchange rate in early 2023 facilitated rate cuts, which pushed up the stock market.
- The slowdown in Vietnam's real estate market is completely different than that in China, where the market is massively oversupplied, while Vietnam's housing market is significantly undersupplied.

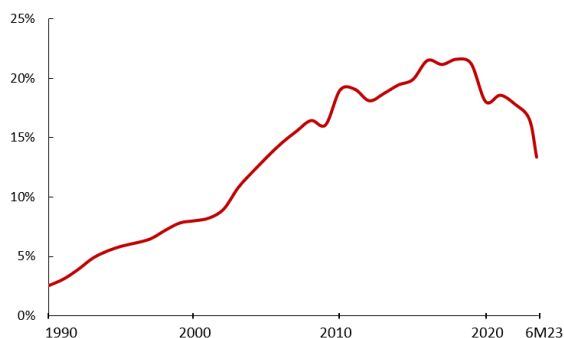
Further to the first point above, in order to convey how important the emergence of a closer US-Vietnam economic relationship is for Vietnam, we noted to investors that hosting the Olympics was a major "economic coming out event" for Japan, Korea, and China; we believe that the new US-Vietnam "Comprehensive Strategic Partnership" could put Vietnam on a path to host the Olympics.

After our investor conference, India announced its intention to submit a bid to host the Olympics in 2036, which reinforces the "economic coming out" rationale for our prediction that Vietnam could submit a bid to host future Olympics. Also, Japan and Vietnam just announced that the two countries would also upgrade their diplomatic relationship to a "Comprehensive Strategic Partnership", which in our view represents another move by Vietnam into the US "friendshoring" orbit.

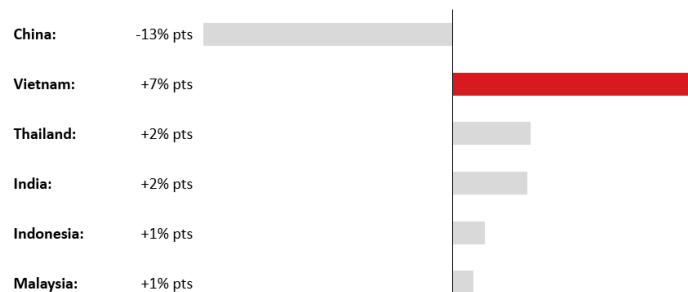
A Monumental Development for Vietnam

The elevation of the US-Vietnam diplomatic relationship to a "Comprehensive Strategic Partnership" represents a major leap forward in the ongoing phenomenon of Vietnam benefitting from a diminution of the US-China economic relationship. As can be seen in the charts below, China's share of US imports fell precipitously in recent years, and Vietnam has been the biggest beneficiary of that decline (along with Mexico).

China's share of U.S. goods imports



Change in share of US imports from Asia, 2018-22



Source: VinaCapital, US Commerce Dept.

The elevation of the US-Vietnam diplomatic relationship will accelerate the dynamics seen in the charts above.

The importance of this new, closer relationship cannot be overstated, largely because it means US investment into Vietnam is set to surge. Many readers may be surprised to know that the US – which has the largest economy in the world – currently accounts for less than 3% of Vietnam’s total FDI inflows, versus circa one-half for Korea and Japan. Furthermore, the coming wave of US investment into Vietnam looks set to be dominated by investment into high-tech industries, including semi-conductors, based on the numerous agreements signed during President Biden’s visit to Vietnam in September.

In addition, the elevation of the US-Vietnam relationship cements Vietnam’s position as a member of the “friendshoring” cohort of countries favored by Washington, DC. This cemented status will facilitate continued FDI inflows to Vietnam from companies in other countries around the world that want to sell their products in the US without concerns that their products could be subject to excessive tariffs.

Realpolitik: How to think about the US-Vietnam relationship now

Realpolitik analysis entails a pragmatic, ideology-free examination of how countries' interests motivate their maneuvering in the global arena. For example, increased US-China rivalry played a central role in the US courting Vietnam, but the US motivation to offer Vietnam enhanced economic incentives in exchange for a closer relationship should also be seen as part of a broader US response to the emerging, new multipolar world order.

US policy makers are concerned about a perceived loss of US influence among developing countries, as well as the possibility of a reduction in the use of the US Dollar in global trade. Saudi Arabia’s participation in the new BRICS alliance exacerbated those concerns, given the role that country played over the last 50 years in the current “petrodollar” based global trade paradigm.

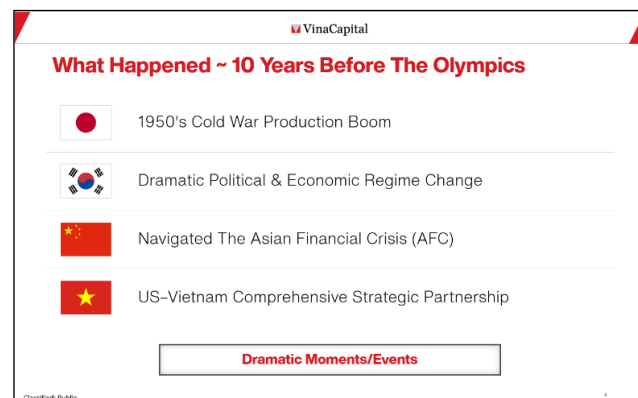
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The US government's efforts to forge closer relations with Vietnam should be viewed as a response to the perceived threat of multipolarity, and this economic upgrade is likely to have a major impact on Vietnam's economic growth trajectory, just as US benevolence played a major role in the economic success of various East Asian nations, including Japan, Korea, and Taiwan.

To be clear, factors like high savings rates, strong work ethics, and a focus on education were important in the rise of the "Asian Tiger" economies, but Washington, DC played a *critical* role in fostering prosperity in countries like Japan and Korea. This strategy was a key component of US Cold War strategy, especially in the 1960s and 1970s, when the US incentivized Japan and Korea to remain firmly in its orbit by offering generous incentives, including unfettered access to the largest consumer market in the world. We do not expect Vietnam to become as close to the US as Japan or Korea are, but when the world's wealthiest country focuses its attention on boosting another nation's prosperity, it historically has been a pivotal turning point with far-reaching implications for that country (in this case, for Vietnam).

Why are we predicting that Vietnam will host the Olympics?

Hosting the Olympics was a major economic milestone for Japan, Korea, China, and certain other countries because it demarcated the transition of these countries from their previous status as "economic backwaters" to peers on the global economic stage. We see parallels between the economic events that preceded these major "coming out" events for each of those three countries, with the recent, US-Vietnam developments discussed above. Those parallels are the basis of our prediction that Vietnam is now on-track to host the Olympics in 20 years.



Specifically, about a decade prior to Japan/Korea/China hosting the Olympics, there were pivotal economic developments that strengthened the already robust growth trajectory of each country. In Japan's case, the Korean War spurred a Japanese industrial production boom during the early 1950s. In Korea's case, the country had already been on a solid growth trajectory, guided by a series of five-

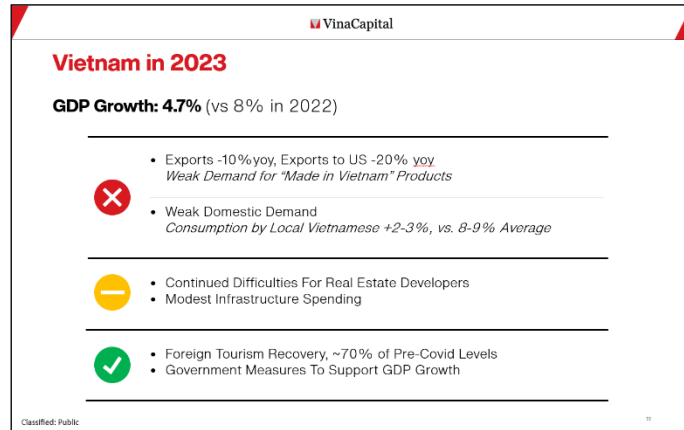
year industrial development plans, when a major economic and political regime change put the country on an even stronger growth trajectory in the 1980s. In China's case, the country's adept handling of the 1997 Asian financial crisis helped instill the confidence of foreign investors to pour massive investments into the country that led up to its hosting the Olympics in 2008. Drawing parallels, we think that the US - Vietnam Comprehensive Strategic Partnership embodies a comparable turning point for Vietnam.

Vietnam's economy in 2023-24

As mentioned at the beginning of this report, the investor conference economic presentation identifies both the long-term drivers that are likely to propel Vietnam's economic growth over the mid-term and the shorter-term economic developments that tend to influence stock prices. Fluctuations in GDP growth are usually the most important short-term economic developments for the stock market because economic growth drives corporate earnings growth.

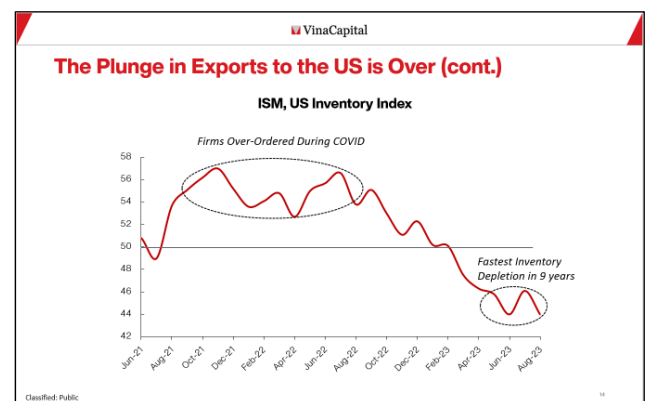
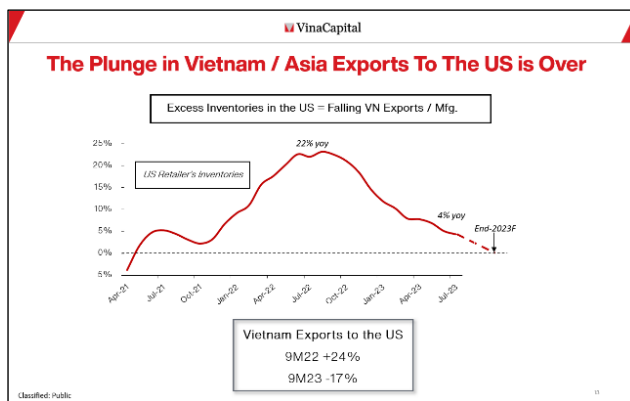
We expect Vietnam's GDP growth to slow from 8% in 2022 to 4.7% in 2023 because:

- 1) Exports and manufacturing output collapsed this year, driven by a drop in the demand for "Made in Vietnam" products. Vietnam's exports fell nearly 10% yoy in 9M23, driven by a near 20% drop in exports to the US, which is its largest export market, for reasons that are discussed below (US companies over-ordered products from Asia in 2022, although this trend is fortunately nearing its conclusion, heralding an economic recovery for Vietnam next year).
- 2) Domestic consumption growth is nearly flat year-on-year (excluding spending by tourists), versus 8-9% typical growth rates, pre-COVID. Sentiment has been impacted by ongoing challenges in the real estate market that are discussed below, and because the drop in Vietnam's exports prompted layoffs at some foreign direct investment factories (most of Vietnam's exports are produced by FDI companies).
- 3) In contrast to the points above, foreign tourist arrivals recovered to nearly 70% of pre-COVID levels this year, which is supporting Vietnam's 2023 GDP growth. Foreign tourism previously contributed about 10% of Vietnam's GDP pre-COVID but made almost no contribution to the country's economy last year.



We expect Vietnam’s GDP growth to rebound to 6.5% next year, driven by a recovery in exports, which will in-turn be closely accompanied by a rebound in Vietnam’s manufacturing sector output from flat growth in 2023 to 8-9% in 2024, versus the sector’s 12% long-term average growth, pre-COVID.

Our optimism for a manufacturing-driven recovery of Vietnam’s GDP growth in 2024 stems from an analysis of the cause of the sector’s problems in 2023, which was an over-accumulation of inventories by US retailers and other consumer firms in 2022. Inventories surged by more than 20% yoy in late-2022, as can be seen in the chart below, because firms over-ordered during the COVID supply-chain disruptions of 2021, and because expectations of a post-COVID spending boom did not materialize as retailers and other consumer companies had expected.



Instead of purchasing more products when COVID lockdowns were lifted, consumers splurged on services such as travelling and eating out. Consequently, US firms have been working through this excess inventory throughout 2023, with inventory depletion at the fastest pace in almost 10 years; this has been the main factor weighing on Vietnam’s exports and manufacturing output this year. However, a plethora of anecdotal and high-frequency economic data in the US and in Vietnam

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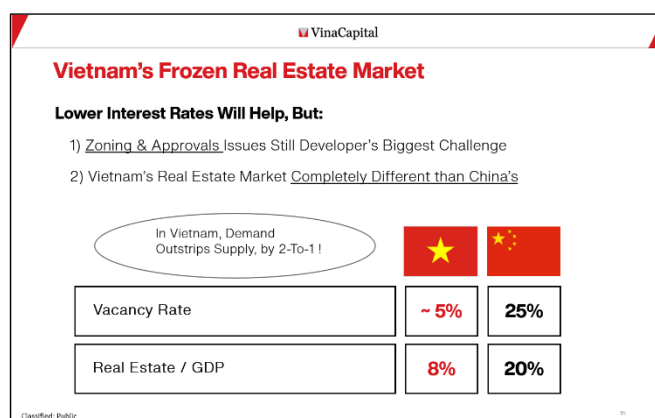
indicates that this phenomenon is now coming to an end, which is the basis for the belief that orders and output from factories in Vietnam are now recovering.

Vietnam's frozen real estate market

The number of housing units for sale in HCMC and Hanoi fell by about 50% yoy in 9M23, while the volume of new housing purchases in China fell by nearly 10% yoy during the same period, after having plunged nearly 25% last year, measured in floor space terms. Some investors (and newspaper journalists) worry that Vietnam is now experiencing the aftermath of a real estate bubble that will drag on the country's economic growth over the next few years.

However, the situation in Vietnam's real estate market is completely different than China's. Unlike in China, where there is an enormous oversupply of empty housing units, Vietnam's real estate market is fundamentally healthy, albeit suffering from severe short-term headwinds.

In short, China experienced a classic EM, real estate "boom & bust" cycle in which banks over-lend at the peak of the market, which pushes prices into the stratosphere and leads to the development of too many housing units. Vietnam experienced a similar real estate boom & bust bubble that bottomed out around 2012, but the country has *not* experienced a proper real estate bubble since then. It is also certainly *not* in the aftermath of a bubble now, which is reflected by the fact that the country's vacancy rate is still quite modest and far below China's, as can be seen below.



The reality is that Vietnam is not producing nearly enough new housing units to meet the growing demand from the burgeoning middle-class population in need of affordable housing (i.e., residences priced at around USD1,500 per square meter that cater to the needs of ordinary consumers).

The primary bottleneck that developers are currently facing to build more apartment buildings/housing units centers around Vietnam's cumbersome zoning and approvals process, which has been especially hindered in recent years by various dynamics within the government. In addition,

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the need for developers to finance their land acquisition/land-banking activities and construction of their projects also contributed to the slowdown in development activity.

The especially high level of interest rates in Vietnam (until recently) made it expensive for developers to finance the construction of their projects, and their inability to secure proper zoning and approvals for the projects from the Government has made it impossible for them to borrow at any cost since because banks do not want to lend to projects without proper approvals.

Finally, we note that there have been some recent intensified efforts within the Government to remove/reduce the obstacles developers have been facing in attaining the approvals needed to proceed with certain specific projects. Those efforts by senior Government officials stem in part from the fact that the slowdown in Vietnam's real estate development activity has dampened consumer sentiment in Vietnam, which in turn has weighed on consumption.

However, real estate development only makes a modest contribution to Vietnam's GDP, so: 1) slower real estate development activity is not the primary factor depressing Vietnam's GDP growth this year (especially because development activity was already slow last year), and 2) the sluggish real estate sector has had much less of an impact on Vietnam's GDP growth than it has in China because real estate development represents a much bigger slice of that country's economy (as can be seen above).

Macro Stability: Foreign exchange rate and interest rates

Vietnamese policymakers appear to be aiming to maintain a stable USD-VND exchange rate to foster a stable macro-economic environment that is conducive to steady GDP growth and to help attract FDI inflows. While not an officially stated policy, the actions of the State Bank of Vietnam (SBV) suggest an aversion to allowing the currency to depreciate by more than 2-3% annually. Monitoring the country's money and foreign exchange markets closely reveals that when the currency approaches this threshold, the central bank typically acts to maintain stability.

In late 2022, the value of the US Dollar/DXY Index surged nearly 20% YTD, prompting the SBV to aggressively hike interest rates. This move was clearly aimed at stabilizing the VN Dong: inflation was just 3% at that time and the SBV's actions helped limit VN Dong depreciation to 3% last year.

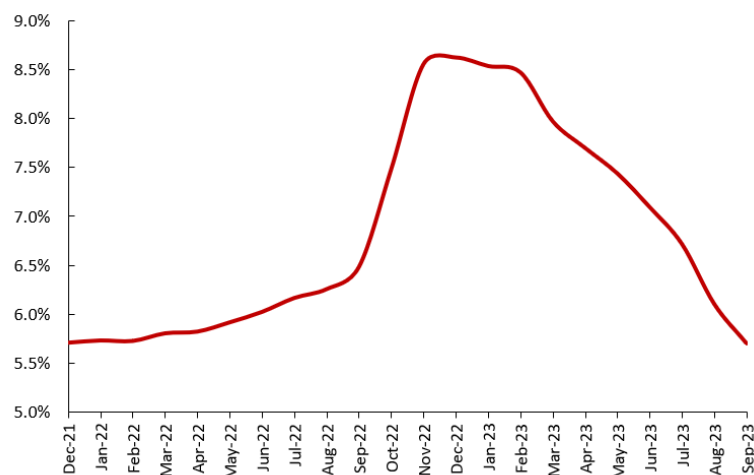
In 2023, Vietnam's GDP growth slowed for reasons discussed above, which prompted the central bank to aggressively cut interest rates. Those aggressive rate cuts were enabled by a stable USD-VND exchange rate in 1H23, which was in turn largely attributable to a surge in Vietnam's trade surplus to circa 7% of GDP this year.

That said, Vietnam's central bank has slashed policy interest rates at a time when the Fed has been persistently hiking rates, so short-term interest rates in Vietnam are now a remarkable 400 bps below USD interest rates (i.e., circa 5% for short-term USD interest rates versus 1% for short-term VND interest rates), which caused the VN Dong to depreciate by about 3% again this year. Once again,

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the SBV stepped up its actions to protect the value of the VND as this depreciation approached the 3%-level).

Average 12M Deposit Rates

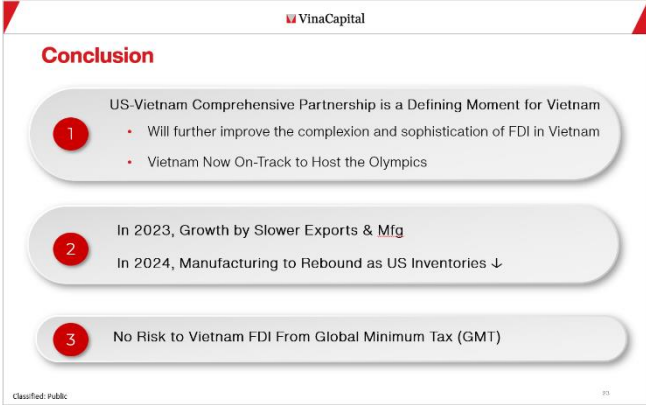


Finally, the surge in deposit interest rates in Vietnam last year prompted many retail investors to sell stocks and place their funds in banks due to the attractive interest rates on offer. However, interest rates have declined precipitously this year in the wake of the SBV's rate cuts. Consequently, many investors reinvested the proceeds of their maturing 6-month deposits (which were particularly popular) back into the stock market, which is one of the main factors that has contributed to the VN-Index's rise of 10% YTD as of the publication of this report.

Conclusions

The elevation of the US-Vietnam diplomatic relationship to a "Comprehensive Strategic Partnership" holds significant implications that are underestimated by many. It should prompt an enormous inflow of new investment from the US into Vietnam (the US currently only represents around 3% of Vietnam's FDI inflows), but also encourage continued investment from companies in other countries given that this move cements Vietnam's status as a "friendshoring" country in the US orbit.

That said, in the near-term, Vietnam's close economic relationship with the US has actually hurt its GDP growth because the US is Vietnam's largest export market and inventory destocking by US companies depressed the demand for "Made in Vietnam" goods this year, although we see signs of a robust recovery in exports and manufacturing next year.



Conclusion

US-Vietnam Comprehensive Partnership is a Defining Moment for Vietnam

- 1 Will further improve the complexion and sophistication of FDI in Vietnam
 - Vietnam Now On-Track to Host the Olympics
- 2 In 2023, Growth by Slower Exports & Mfg
 - In 2024, Manufacturing to Rebound as US Inventories ↓
- 3 No Risk to Vietnam FDI From Global Minimum Tax (GMT)

Classified: Public

Finally, note that in addition to the points discussed in this report, the conclusion slide to our Investor Conference presentation shown above includes an additional point about the potential implementation of a global minimum tax (GMT) regime in Vietnam. We did not discuss GMT in this report because the possible implementation of GMT in Vietnam will be covered in our next insights report. Long-story-short, we believe concerns that GMT could impede FDI inflows to Vietnam are unfounded for a variety of reasons, including the near certainty that Vietnam's Government (like many other EM governments) is likely to find ways to provide other incentives to companies in order to offset potential increases in corporate tax rates in Vietnam.

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