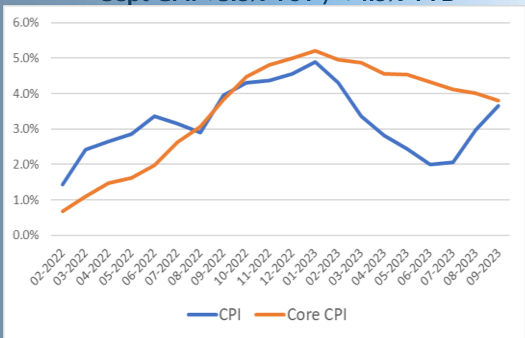
Vietnam Macro

12 October 2023

Sept CPI: +3.8% YoY / +4.5% YTD



What's new?

- 3Q23 GDP growth of +5.3% brings YTD growth to +4.2% YoY. The low end of our 5-6% forecast range is still within sight, we think.
- Inflation has been trending higher in recent months – a key macro risk.
- The US bond rally should help ease some of the pressure on the VND. 10-yr US treasuries are now yielding 4.6%, down from 4.9% last week.

Our View

- The SBV's tightening of interbank liquidity is intended to shore up the VND, not to curtail economic activity.
- The price of capital for the real economy (i.e., state bank deposit rates) is on a downtrend.
- The SBV action was thus an excuse to take profits and does not signal a bear market.
- Inflationary pressures are building for 4Q23-1Q24, possibly offset by VND stability.

Inflation likely to rise into 1Q24

Mission Impossible III: The Final Cut. 3Q23 GDP expanded by +5.3% YoY, bringing YTD growth to +4.2%. This put the original 6.5% growth forecast officially out of reach – which is no major surprise to anyone who has been paying attention. Recent GDP forecast downgrades by multilateral banks have been worse for Vietnam than most countries, but this is an unintended consequence of them clinging to the government's growth targets at the start of the year, rather than any real negative shock.

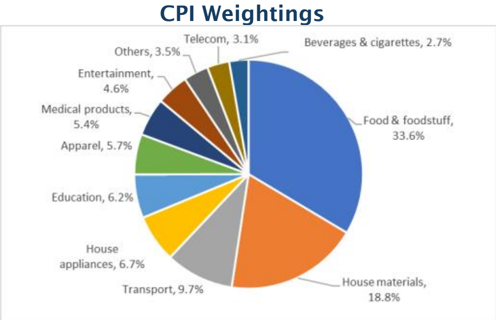
What's good? Retail sales (+2.4% MoM / +7.5% YoY) improved sequentially with support from tourism and other hospitality services. Industrial output continues to exhibit a nascent recovery, or at least light at the end of the tunnel. Credit growth reportedly reached +6.9% YTD in 9M23, up from +5.3% in 8M23. This suggests a surge of new credit in September – which supports our argument that the SBV's tightening action is not meant to cool the real economy. Anecdotally, we are hearing that much of this new credit came in the last week of September.

What's bad? Merchandise exports declined in September (-4.1% MoM / +4.9% YoY) after surging in August, while imports (-0.7% MoM / +1.1% YoY) were similarly sluggish. The manufacturing PMI dropped to just below 50 after August's single-month sojourn into expansion territory. But new orders were up, and regional OEMs (textiles and electronics) indicate that inventory problems are dissipating. We thus remain cautiously optimistic about industrial output heading into 2024. However, we think that rising domestic consumer prices are an increasingly critical risk.

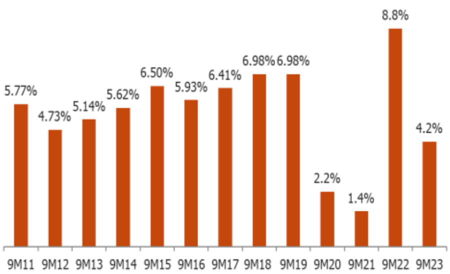
Inflation is back – or at least is back in mind as a key risk. September CPI was up +3.7% YoY (and +3.2% YTD), well below global inflation rates but substantially higher than the +3.0% figure in August and +2.1% in July. We think the risk is to the upside heading into 4Q23-1Q24 given global food and energy price trends. But (as discussed above) the current rally in US treasuries should hopefully offset some of the recent pressure on the VND, which should partly offset price increases for imports.

You can't eat core CPI. In contrast to headline CPI figures, core CPI (+3.8% YoY / +4.5% YTD) has been dropping in recent months. However, food prices (+10.5% YoY / +4.9% YTD) are on a tear, suggesting upside risk for the food & foodstuff subcategory (+2.9% YoY / +3.6% YTD) which represents 34% of the overall CPI basket. In addition, housing & construction materials (+7.3% YoY / +6.7% YTD) – a category that includes electricity, water, and gas – has an 18.8% CPI weighting.

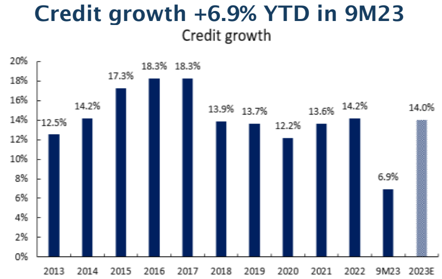
CPI Weightings



GDP +5.3% YoY in 3Q23 / +4.2% in 9M23



Credit growth +6.9% YTD in 9M23



Note: 2023E is the SBV's credit growth target
9M23 data are as at Sep 30, 2023

Sources: *GSO, SBV, FiinPro, various domestic media, Bloomberg, Yuanta Vietnam*

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Inflationary Pressures are Building

Highlights of the GSO data for September – A mixed outlook, as usual.

Some Positives…

- **3Q23 GDP growth was estimated at +5.33% YoY**, improved from the quarterly YoY growth of 1Q23 (+3.3%) and 2Q23 GDP (+4.14%).
- **This brings 9M23 GDP growth to +4.24% YoY.**
- **It's no surprise if you've been paying attention**, but the consensus has finally concluded that it is impossible to reach the government's original 2023 GDP growth target of 6.5%.
- **Retail spending ticked higher.** Sales of goods and services in September reached VND 524.6tn, up by +2.4% MoM and by +7.5% YoY. Receipts were underpinned by hospitality and catering services.
- **Industrial production continues to exhibit a nascent recovery**, or at least light at the end of the tunnel, fueled by manufacturing.
- **Public investment grew impressively** in September, but reaching the annual target will again be a challenge.

… and Negatives --

- **The manufacturing PMI fell moderately** into contraction territory in September, following the (also moderate) expansion reading of the previous month.
- **But manufacturers report increased new orders**, and especially export orders.
- **International trade paused** in September, but increased export orders suggest stronger momentum toward yearend.
- **No-one is suggesting an imminent boom in global exports** of merchandise, but we continue to believe that the worst has passed for manufacturers.
- **Inflationary pressure is escalating**, putting the government's annual CPI target of <4.5% back into the spotlight.
- **But let's make lemonade** out of this more expensive oil: we continue to see trading opportunities in oil price proxies PVD (BUY), PVS (not rated), and GAS (not rated).

3Q23 recap: Quarterly GDP +5.3%. The GSO reported that GDP in the third quarter of 2023 increased by an estimated 5.33% YoY. This was an improvement on the 2Q23 GDP growth of 4.14% and 1Q23 expansion of 3.30%.

Industry and construction output improved by the most of the three major sectors, increasing by +5.19% YoY (up from just +2.5% YoY in 2Q23).

Agricultural, forestry, and seafood activity increased by 3.72% YoY in 3Q23 (vs. 3.25% in 2Q23). The service sector also looks solid, posting +6.24% YoY growth in 3Q23, up slightly from +6.11% YoY expansion in 2Q23.

The result brings 9M23 GDP growth to +4.24% YoY, up from just 3.72% YoY in 6M23 but still well below the government's original target of +6.5%.

9M23 output of services rose by 6.32% YoY (vs. +6.33% YoY in 6M23), making this sector the key growth driver of Vietnam's economy so far in 2023.

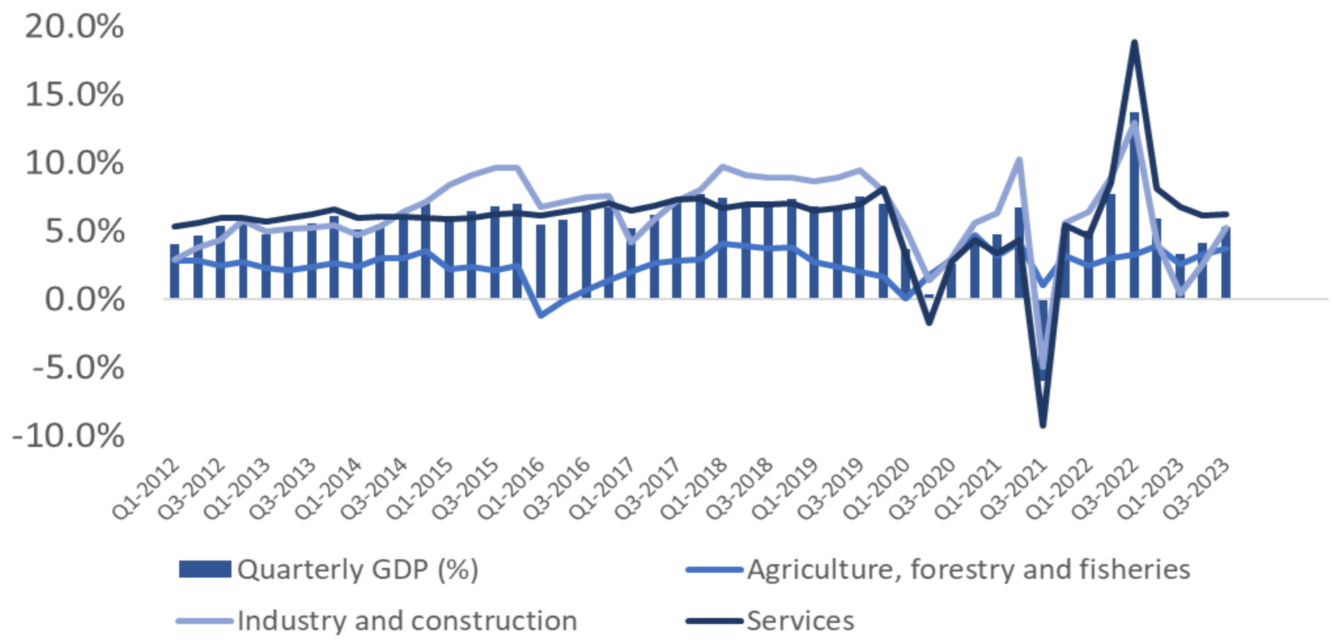
By contrast, 9M23 GDP growth was constrained by industry and construction (+2.41% YoY in 9M23 / + 1.13%YoY in 6M23) and agricultural, forestry and seafood (+3.43% YoY in 9M23 / +3.07% YoY in 6M23).

The service sector accounted for 43.25% of Vietnam's economic output in 9M23; industry and construction accounted for 36.62%; agriculture, forestry and fishery sector accounted for 11.32%; and taxes minus subsidies accounted for 8.81% of the total.

Based on recent statements, the government now targets 6.0% GDP growth for 2023, slightly down from the original annual target of 6.5%. However, the revised target still looks to be out of reach, in our opinion. By simple math, GDP growth in 4Q23 would have to be +11.28% to reach this target, which would appear to be out of range.

Indeed, even our own more conservative 2023 GDP growth range assumption of 5-6% -- which was well below the government target-hugging Consensus when we published it in 1Q23 -- now appears to be optimistic.

GDP growth expanded by 5.3% in 3Q23, bringing 9M23 growth to 4.2% YoY.



Source: GSO

Industrial production ticked higher again

The recent recovery for industrial production extended into September. This is most clearly evidenced by the industrial production index (IIP), which increased by +0.1% MoM and +5.1% YoY after bottoming out in June. The uptick in industrial output was further demonstrated directly by improved exports and indirectly by strengthened domestic demand.

Overall, our call that June was the bottom for industrial output has held up well. But this doesn't mean that 2H23 will see a boom for manufacturing. New orders have improved off low levels but remain well below trend, so the upcoming holiday season will not go down in history as Vietnam's best.

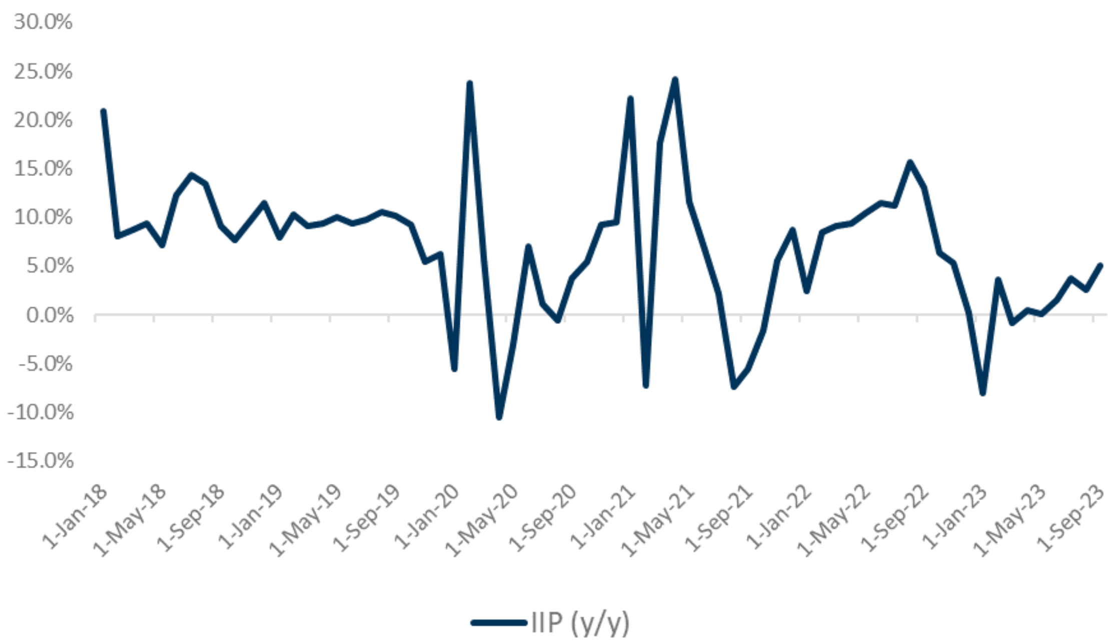
However, inventory problems in end-markets have largely been addressed, and we think the recovery will become clearer in 2024. This view is backed up by our regional coverage of manufacturers including footwear manufacturer Pou Chen (9904 TT, BUY), which is among HCMC's largest private sector employers.

Analyst Jason Tsai expects the footwear manufacturing business to recover as Nike and Adidas' inventory adjustment comes to an end. He expects weak 3Q23 results (which should be baked in) but 4Q23 sales to grow +4.1% YoY. "Amid the ongoing recovery, we expect 2024F sales to increase 12.8% YoY, and EPS to grow 21% YoY".

For further details, please see the following link for Jason's initiation report on Pou Chen, published on September 25: https://research.yuanta-consulting.com.tw/temp/ProductionYT/30758.pdf

Manufacturing output rose by +1.4% MoM and +5.9% YoY in September, higher than the blended IIP result. Key drivers here were production of food (+12.5% YoY), clothing (+13.9% YoY), chemicals (+13.9% YoY), and tobacco (+11.4% YoY). Electricity production increased by +7.9% YoY; and water supply and waste management output rose by +5.8% YoY.

Uptick in industrial output continued in September



Source: GSO

As a result, 9M23 industrial output increased by +1.65% YoY. Our view that 1H23 was the bottom is supported by the positive trend, as IIP declined by -0.75% YoY in 1Q23, before improving in 2Q23 to growth of +0.95% YoY, and following up with 3Q23's positive momentum of +4.57% YoY expansion.

By sector, the composition of the 9M23 IIP was as follows: Output of (1) mining decreased by -3.0% YoY; (2) manufacturing increased by +0.2% YoY; (3) electricity production and distribution increased by +2.6% YoY; and (4) water supply and wastewater treatment industry increased by 4.9%.

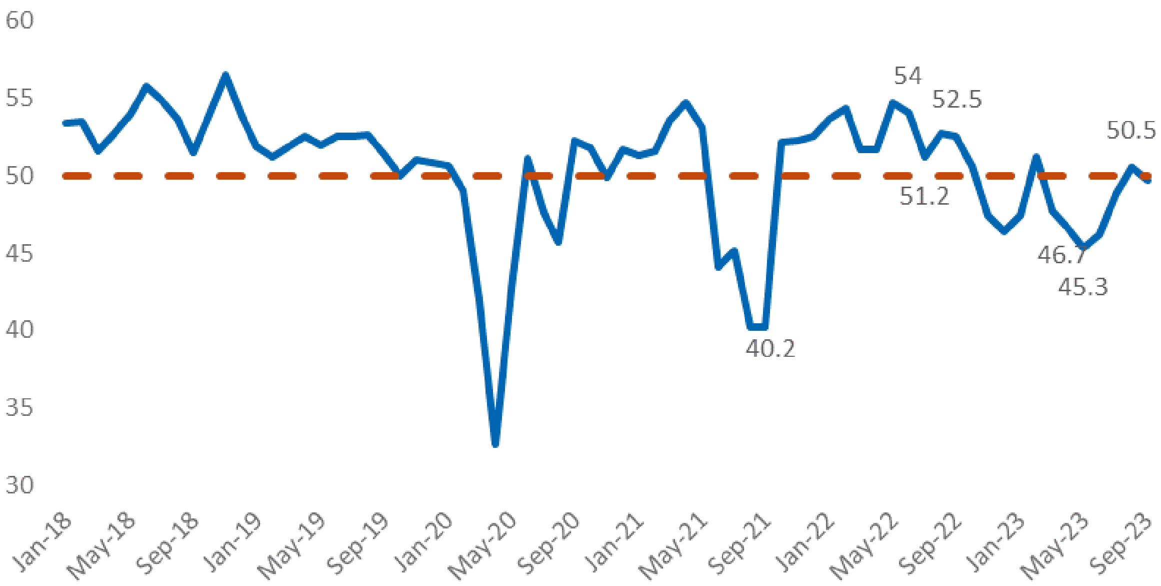
9M23 production of coke & refined petroleum increased by +3.8% YoY; tobacco increased by +9.6% YoY; rubber & plastic products increased by +8.7% YoY; chemicals & chemical products increased by +6.2% YoY; food increased by +5.8% YoY; textiles increased by +3.6% YoY; and electrical equipment increased by +2.8% YoY.

By contrast, production of several industrial segments declined in 9M23: Output of 1) electronic products, computers, and optical products decreased by -2.2% YoY; 2) machinery and equipment production not classified elsewhere decreased by -4.0% YoY; 3) other non-metallic mineral products decreased by -3.4% YoY; 4) wood processing decreased by -3.1% YoY; (5) paper decreased by -3.5% YoY; 6) apparel decreased by -1.5% YoY; 6) other transport equipment decreased by -7.3%; 7) motor vehicles decreased by -5.2% YoY; and mining services decreased by -17.4% YoY.

Manufacturing PMI: Down, but not out -- New orders increased for the second straight month

Business conditions in the manufacturing sector slid marginally in September after indicating expansion in the previous month. S&P Global's September manufacturing PMI returned to negative territory at 49.7 in September, back below the 50.0 no-change mark, following a reading of 50.5 in August. The positive takeaway from the survey is that new orders increased for the second successive month.

The manufacturing PMI in September slid to just below 50 again



Source: GSO

Manufacturers reported increased new orders for the second month in September, and the rate of increase was equal to that of the previous month. Respondents also reported that increased new export orders from other Asian countries were especially strong – even greater than those of the previous month.

Despite the increase in new orders, manufacturers still scaled back production. Total output was thus down MoM from August. However, this decline in output was driven by soft activity among intermediate goods producers, whereas consumer and investment goods producers reported expanding output in September.

Another positive takeaway from the September survey is that manufacturers report increased input purchasing plans to support greater production volumes in the coming months. Materials / parts purchasing plans increased for the second month running in response to new orders, among the survey's respondents.

Foreign trade: A pause in the recovery?

The recovery in merchandise exports has paused after positive August figures. Specifically, September's export turnover of goods reached USD31.41bn, down by -4.1% MoM following a +7.7% MoM increase in August.

9M23 aggregate exports (merchandise only) remain in negative growth territory, but the YoY decline has been exhibiting a slowing pace. YTD merchandise exports in 9M23 declined by -8.2% YoY to reach USD260bn, an improvement from the -10.0% YoY decline of 8M23.

9M23 net exports to the US, the biggest export market by far, fell by -18.0% YoY (a horrible result, but a gradual improvement from the 8M23 decline of -19.1% YoY).

Some 31 items had export turnover in excess of USD 1bn, accounting for 92.2% of total exports in 9M23; while 6 items recorded export turnover in excess of USD 10bn YTD.

Interestingly, export turnover of means-of-transport and components impressively posted +16.5% YoY growth to reach USD 10.3bn and thus this segment joins the group in the table below. We're looking into this now, but an initial educated guess (based on the destination countries – the US, Japan, and Korea) is that it may be related to automobile components that are manufactured / assembled here.

Largest export items in 9M23 recorded substantial decline

	Estimated 9M23 export turnover (USD mn)	YoY growth (% YoY)
Above USD10bn export turnover		
Electronic goods, computers and parts	41,188	-1.7
Mobile phones and parts	39,034	-13.4
Machinery, instrument, accessory	30,642	-10.6
Textiles and garments	25,513	-12.1
Footwear	14,859	-18.2
Means of transport and components	10,259	+16.5

Source: GSO

Similarly, imports posted a sequential pause in the recovery, reaching USD29.12bn in September, down by -0.7% MoM following the August increase of +5.7% MoM.

For 9M23, merchandise imports reached USD 237.99bn, down by -13.8% YoY (improved from -16.2% YoY in 8M23). Some 37 items saw import turnover exceed USD 1bn in 9M23, accounting for 89.7% of total imports in that period.

Two items recorded import turnover in excess of USD 10bn – electronics and machinery, both of which are inputs for downstream export manufacturing. Both items posted substantial declines in YTD imports, as illustrated below. But again, the declines in 9M23 segment imports were substantially lower than those of 8M23.

Electronics, computers and parts remain the largest import products in 9M23

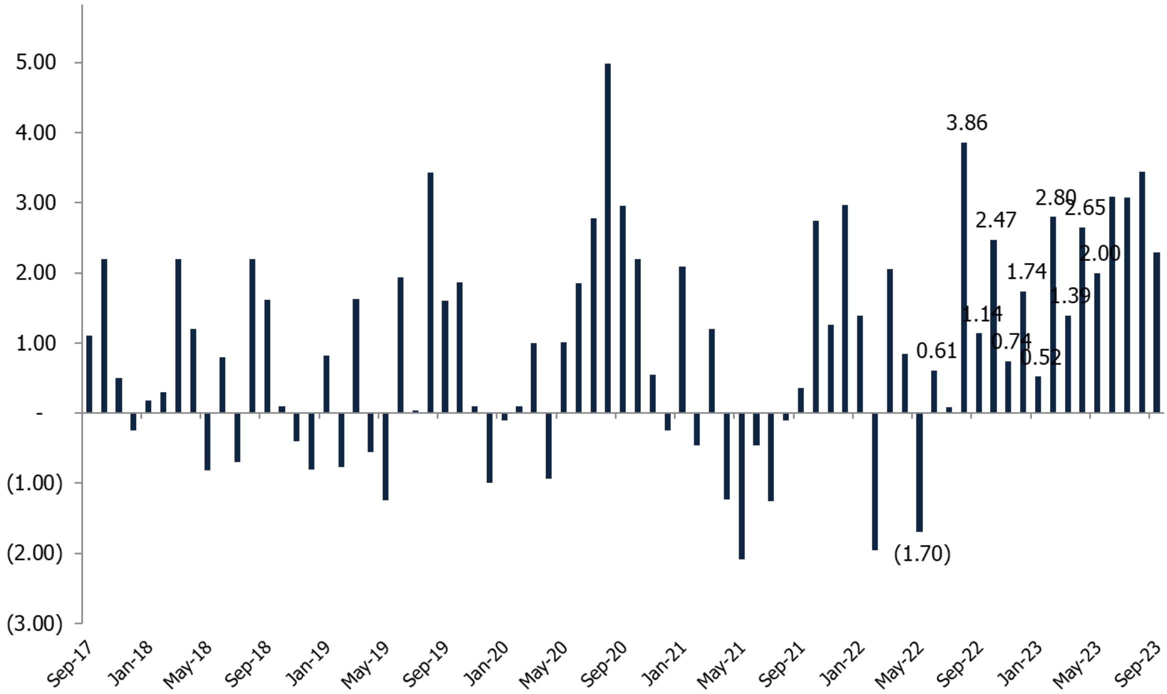
	Estimated 9M23 import turnover (USD mn)	9M23 growth… (% YoY)	*…vs. 8M23 growth (% YoY)*
Above USD10bn export turnover			
Electronics, computers, and parts	63,025	-1.5	*-6.0*
Machinery, instruments, anc accessories	30,569	-11.1	*-13.0*

Source: GSO

Overall, Vietnam recorded a ~USD 15bn total trade surplus, with net merchandise exports (i.e., a surplus) reaching USD 21.7bn (9M22 was +USD6.9bn) while net imports of services (i.e., a deficit) reached 6.7bn.

We continue to expect a clearer recovery picture toward yearend when export demand typically picks up, underpinned by the increase in export orders as highlighted in the recent manufacturing PMI surveys.

Vietnam recorded a merchandise trade surplus of USD 21.68bn in 9M23



Source: GSO

Public investment: Impressive growth but annual budget is a challenge

State investment disbursals reached VND 61.3 tn in September, up +29.1% YoY. According to the GSO, the government at all levels has been emphasizing the disbursal budgeted public investment funds, which led to this impressive YoY growth.

The September figure brought 9M23 public investment to VND415.5 trillion, up by +23.5% YoY (faster than that of 9M22 growth of 20.3% YoY) and fulfilling 57.4% of the government's full-year budget.

Specifically, investment by the central government reached VND 76.4 trillion in 9M23, 57.3% of budget and up by +28.1% YoY. Investment by provincial governments reached VND 339.1 trillion, 57.4% of the annual budget and up by +22.5% YoY.

We think it is unrealistic to expect the authorities to achieve 100% of the annual budget by yearend. However, public investment typically escalates in the second half of the year, so it shouldn't be too challenging to fulfill 80-90% of the annual budget in the last three months of 2023.

This is a critical positive given the need to offset this year's cyclical softness in other areas of the economy, such as manufacturing and consumer spending.

FDI disbursals have been less impressive. Disbursed FDI in 9M23 has reached USD 15.91bn, up by just +2.2% YoY.

We think this is primarily a reflection of global macro uncertainties, and we continue to view Vietnam as a prime beneficiary of "de-risking" of global manufacturing chains away from China.

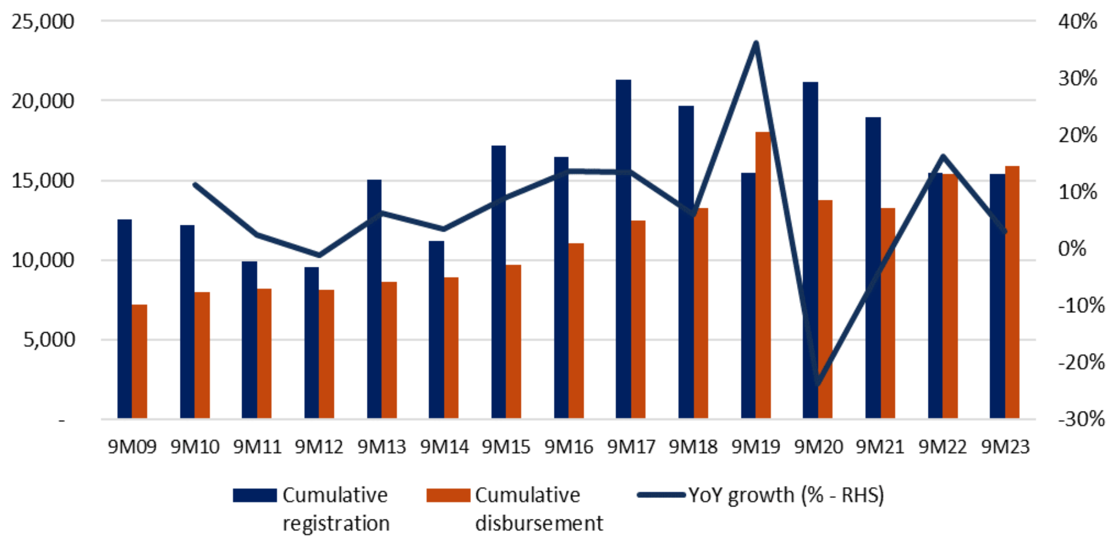
Manufacturing accounts for 82.1% of the 9M23 disbursed FDI, or USD 13.08bn. Property accounts for 4.8% of the FDI mix (USD762.7mn); while gas, hot water, steam, and air-conditioning FDI of USD 1bn, accounts for 6.3% of total disbursed FDI YTD.

Total registered FDI slid by -0.58% YoY to USD15.4bn. Specifically, newly registered FDI reached USD 10.23bn, up by an impressive +44% YoY, whereas additional FDI registrations dropped by -38.0% YoY to just USD 5.15bn.

By (positive) contrast, the number of newly registered FDI projects reached 2,254, up by +66.3% YoY.

Pledged FDI represents promises, not cash injections; but the surge in interest in new projects -- among manufacturers in particular -- indicates that future disbursals are likely to remain strong.

Disbursed FDI recorded positive growth in 9M23



Source: GSO

Retail spending appears to have been solid in September

Consumer demand was solid, albeit not spectacular, in September. Retail sales of goods and services in September reached VND 524.6tn, up by +2.4% MoM and by +7.5% YoY.

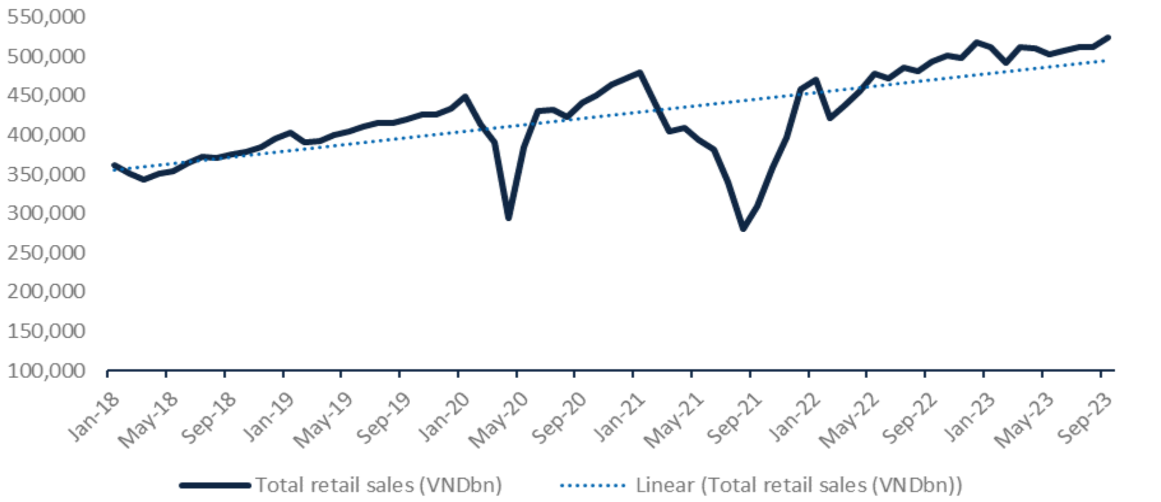
Blended retail sales were underpinned by hospitality and catering services revenue, which grew by +13.7% YoY to reach VND61.1tn (11% of total retail sales) -- driven by the ongoing recovery in international visitor arrivals.

Notably, the GSO reported the number of international arrivals to Vietnam in September reached 1 million, up +13.4% MoM and +2.4 times higher YoY.

This improvement in international arrivals may have been helped by the mid-August easing of certain restrictive tourist visa policies that had been rather confusingly put into place after COVID. In any case, this is an encouraging trend for retail sales for the remainder of 2H23 and beyond, in our view.

Merchandise receipts rose by +7.4% YoY in September (down marginally from +7.5% YoY in August) to reach VND 402.4tn, representing 78% of total retail sales.

Retail sales growth remains solid



Source: GSO

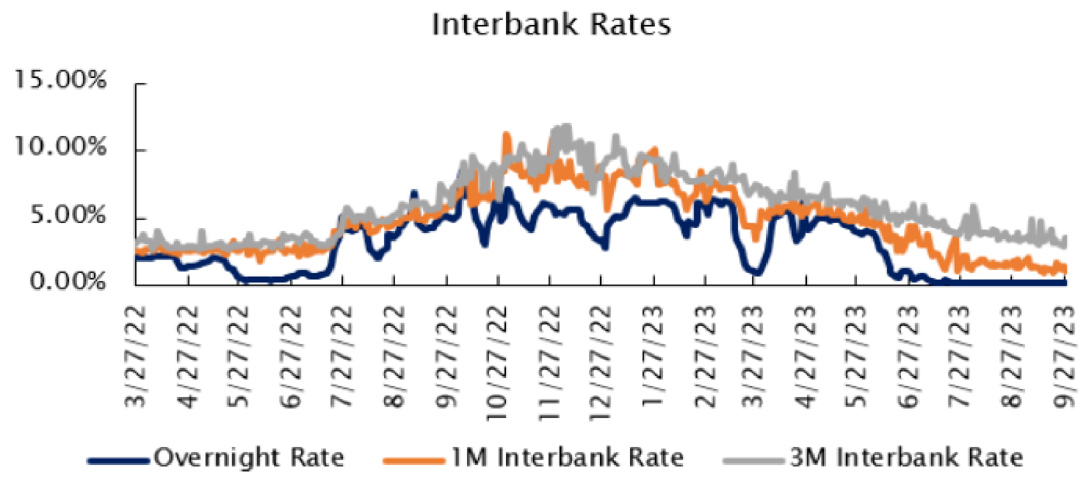
As a result, total retail sales (i.e., goods and services) rose by 10.0% YoY in 9M23 (for real growth of +7.7% YoY) to reach VND4,044 trillion (USD169 billion). This was driven in part by +16.0% YoY growth in hospitality and catering receipts, which reached VND 500.1tn to account for 12% of the total retail sales.

The GSO estimates that revenue from tourism and travel in 9M23 reached VND26.5 tn, +47.7% higher than that of the same period last year. But this only accounts for 0.6% of total retail sales – this rather low figure is due to the classification system, as tourist spending in stores / restaurants etc. is not included in the official data on tourism industry receipts.

In addition, retail sales of goods in 9M23 reached an estimated VND 3,572 tn, up +8.4% YoY (real growth +7.0%), according to the GSO. Cultural and educational product receipts increased by +12.8% YoY; food spending increased by +11.4% YoY; and spending on garments increased by +7.8% YoY.

Retail sales have benefited from relaxed fiscal and monetary policies. The 2ppt VAT cut that took effect on July 1st should lift consumer sentiment in theory, but it may take a bit of time to fully trigger retail sales. In addition, the SBV has encouraged commercial banks to reduce lending rates following a series of policies rates cut since Mar 2023. Latest update: VCB has reduced its deposit interest rate by 20bps to the record low 5.3%, even lower than in the Covid time.

State bank deposit rates are the basis for floating loan interest rates, so the drop in deposit rates will eventually have a positive impact on spending power of consumers, including middle-class mortgage borrowers. The new policies should be supportive of demand and retail sales going forward.



Source: SBV

However, a near-term headwind is that the ability to continue cutting interest rates might be hit by inflationary pressures that are now starting to re-emerge, driven by the rebound in food and global energy / fuel costs and exacerbated by the recent softness in the Vietnam dong.

Inflationary pressure is escalating (in line with our call)

According to the GSO, domestic petrol and rice prices surged in accordance with global prices, driving the CPI up by +1.08% MoM and by +3.66% YoY -- substantially higher than the 2.96% YoY CPI increase in August. This is in line with our concerns expressed in last month's macro roundup, in which we discussed our expectations for oil and food prices to present upside risk to the CPI figures into yearend.

Ten of the 11 items in the CPI baskets posted increases in prices in September, notably:

- Transport (9.56% of the basket) rose by +1.21% MoM as petrol prices rose by 3.54% MoM.
- Housing materials (18.82% of the CPI basket) rose by +1.12% MoM, as gas prices increased by 8.37% MoM and water prices rose by 2.83% MoM.
- Food (33.56% of the CPI basket) rose by +0.73% MoM, as rice prices rose +4.23% MoM due to global supply constraints following the +4.4% MoM increase in the previous month. In addition, meat prices rose by 0.96% MoM.

By contrast, only one of the 11 items in the CPI basket posted reduced prices in August:

- Telecom (3.14% of the CPI basket) prices decreased by -0.23% MoM due to cratering smartphone prices.

No change to our view about upside risks for CPI toward the yearend. The government is likely to achieve its annual CPI target (i.e., an average of 4.5%) given that the 9M23 CPI run rate is just 3.16%. However, we still think that inflation should be considered as a key macroeconomic risk, for several reasons:

1) **Oil prices hit an 11-month high in September.** Brent crude reached USD 95 per barrel in late September before cooling off to ~USD 90 per barrel in October 3, still +2.86% MoM . As discussed last month, **we continue to see trading opportunities in oil price beneficiaries such as PVD (BUY), PVS (Not rated), and GAS (Not rated),** which all have high share price correlations with oil prices.

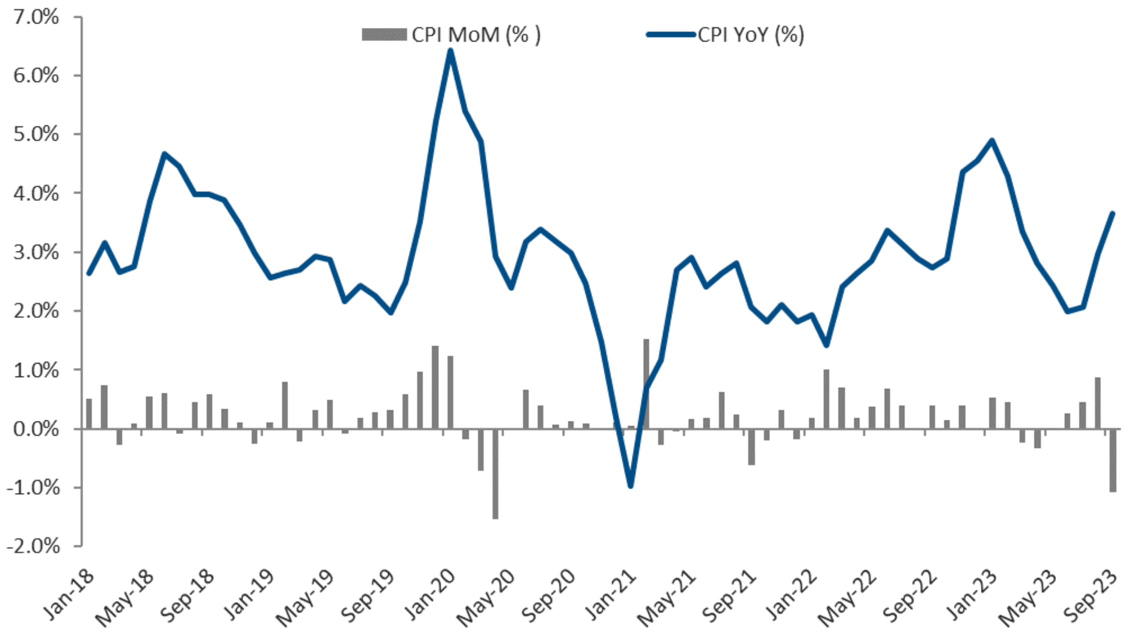
2) **Rice prices are steaming!** Rice futures are trading around USD16 per hundredweight (100 pounds), not far from an over three-month high of USD16.8 hit on September 5th, amid concerns of limited supplies due to unfavorable weather conditions and export restrictions.

   Asian countries, which account for 90% of global rice cultivation and consumption, are facing reduced output due to exacerbated weather conditions from global warming, compounded by an earlier-than-usual El Niño.

3) **VND weakness means even higher LCY prices for imports**. Only about one-third of imports are for the domestic economy, but a soft VND is especially impactful for energy and fuel prices, which obviously have a direct impact on CPI but ultimately feed through to higher prices elsewhere (due to increased shipping costs, etc).

   The real interest rate differential driven by "higher-for-longer" USD rates is likely to keep the pressure on the VND and to constrain the SBV's monetary policy flexibility going forward, in our view.

Consumer price inflation is picking up



Source: GSO

Appendix A: Important Disclosures

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BUY: We have a positive outlook on the stock based on our expected absolute or relative return over the investment period. Our thesis is based on our analysis of the company's outlook, financial performance, catalysts, valuation and risk profile. We recommend investors add to their position.
HOLD-Outperform: In our view, the stock's fundamentals are relatively more attractive than peers at the current price. Our thesis is based on our analysis of the company's outlook, financial performance, catalysts, valuation and risk profile.
HOLD-Underperform: In our view, the stock's fundamentals are relatively less attractive than peers at the current price. Our thesis is based on our analysis of the company's outlook, financial performance, catalysts, valuation and risk profile.
SELL: We have a negative outlook on the stock based on our expected absolute or relative return over the investment period. Our thesis is based on our analysis of the company's outlook, financial performance, catalysts, valuation and risk profile. We recommend investors reduce their position.
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