

VIET NAM ECONOMIC REPORT 2017
OUTLOOK FOR 2018

(Viet Nam Association of Securities Business – VASB)

October 2017

WORLD ECONOMY

- US: Fed Holds Firm in September
- EU: Waits for Decision on QE in October
- China: 19th Party Congress to Focus on Macro Policies and Reforms

The global economy witnessed a recovery of economic growth in 2017, with advanced economies benefiting from easing monetary policies and tightening labor market while emerging economies gained thanks to strong global trade and resilient dynamic in China. Going forward to the end of the year, we think investors will put their focus on the guidance of central banks in advanced economies in order to get a clearer picture about how the coming changes in monetary policy could drive economic growth and capital flow.

US: Fed Holds Firm in September

At the September FOMC meeting, the Fed maintained its target for the federal funds rate between 1.00% and 1.25%, as widely expected by the market. The FOMC also made a first move in unwinding its balance sheet in October. In details, the Fed will gradually cease reinvestment of maturing holdings, capping them at USD10 billion a month in US Treasury bonds and mortgage-backed securities. These levels are expected to be raised at three-month intervals until they reach USD30 billion and USD20 billion, respectively. Compared to its massive USD4.5 trillion balance sheet, the pace of unwinding is slow, which is in line with the dovish tone of most of the FOMC members.

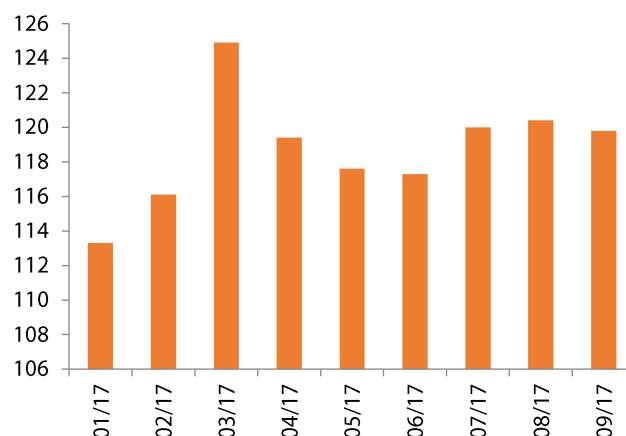
Regarding US economic environment, hurricanes affected negatively the consumption but manufacturing sector remained strong in Q3. The Conference Board's consumer confidence index eased from a revised 120.4 points in August (previously reported: 122.9 points) to 119.8 points in September as the effects of Hurricanes Harvey and Irma heavily weighed on consumer confidence in Texas and Florida. Meanwhile, ISM manufacturing index continued to soar to 13 year high of 60.8 in September, which signals a solid pace of growth in the manufacturing sector. At the end of September, President Trump proposed details of his tax plan. Based on early analysis of this proposal, many analysts expect its passage is going to be politically difficult because it would likely to add more to the budget deficit of the US economy.

Figure 1: US ISM PMI



Source: Bloomberg

Figure 2: US consumer index



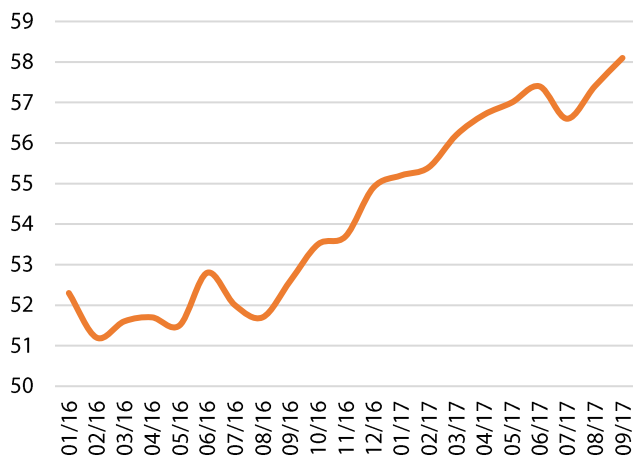
Source: Bloomberg

EU: Waits for Decision on QE in October

Similar to the Fed, the ECB decided to keep interest rates unchanged at its September meeting and made no changes to its bond-buying program. In addition, this central bank reiterated that it planned to continue with its monthly asset purchases of EUR60 billion until the end of December. However, there is a likely announcement of tapering in October, as expected by the market.

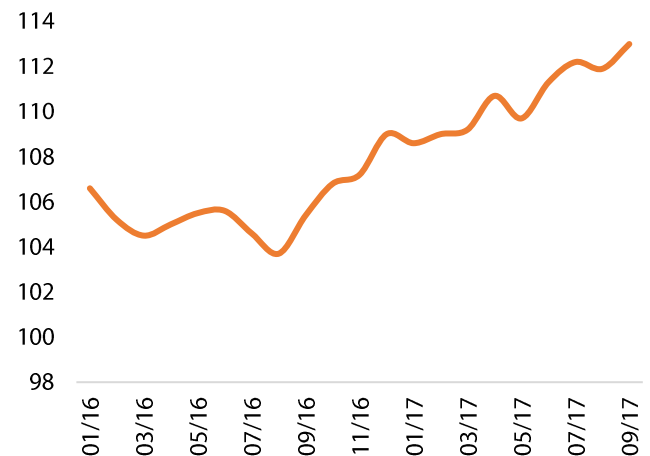
We believe a backdrop of strengthening economic momentum in the Eurozone is giving the ECB some room to maneuver its tightening policy. In August, inflation edged up to 1.5%, rising from July's 1.3%. Furthermore, average inflation inched up to 1.3%, a multi-year high. However, core inflation remained at 1.3%. Leading indicators also suggested healthy manufacturing and services sectors. Accordingly, the Eurozone manufacturing condition was at 6.5-year high in September, came in at 58.1, up from August's 57.4. The composite PMI index that tracks both services and manufacturing came in at 56.7, well above the 55.7 in August. Besides, the economic sentiment index also recorded the best result since July 2007, increased from August's 111.9 to 113.

Figure 3: EU PMI



Source: Bloomberg

Figure 4: EU economic sentiment

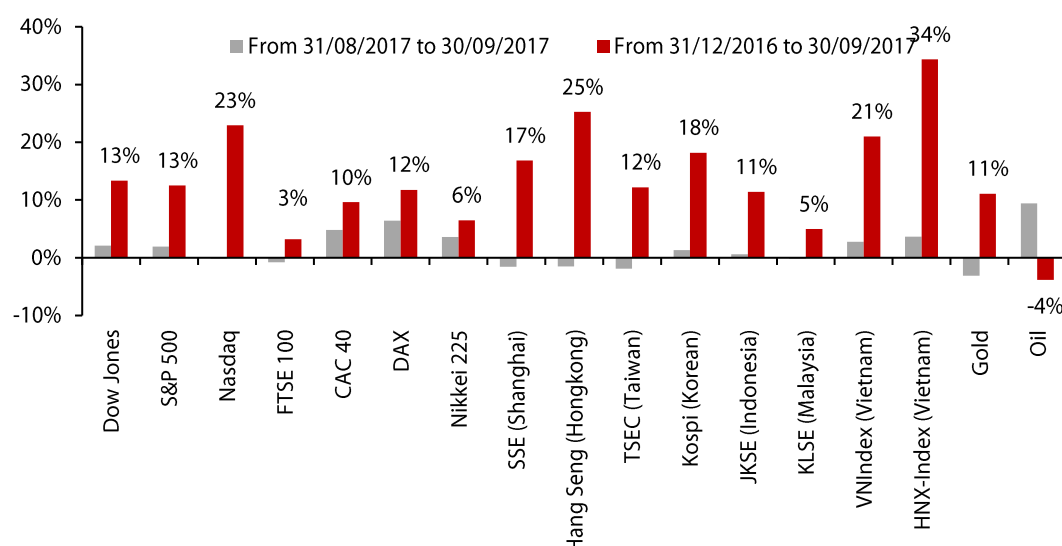


Source: Bloomberg

China: 19th Party Congress 2017 to Focus on Macro Policies and Reforms

The China's 19 Party Congress will begin on 18 October, setting the policy agenda for the next five years. According to HSBC, the top priority is to keep growth above 6.5% in order to hit the target of doubling GDP and income by 2020 from 2010 levels. In addition, other key items include implementing structural reforms to lift private sector productivity and potential growth; containing systemic risks by deleveraging SOEs' debt and making growth greener.

Figure 5: Performance of some global markets in September



Source: Bloomberg, RongViet Research

Most of the world stock market indexes closed the month higher.

In US, Dow Jones, S&P 500 and Nasdaq gained slightly in September. FED meeting did not affect much the investors' sentiment. FED decided to hold the rate unchanged at 1–1.25%. Twelve out of 16 FOMC members predicted that another rate hike would take place in December. Market players tended to forecast such decision. Besides, FED will proceed cutting off its balance sheet from October 2017.

European markets saw Germany's election of Angela Merkel as Chancellor for the fourth term. Such result supported the market; at least, the EU will not have more anxiety on "EU quitting". Besides, Mario Draghi of ECB showed the market expectation to reduce the QE in October. ECB also increased its forecast for the GDP growth of EU in 2017 from the previous 1.9% to 2.2%, the best growth rate since 2007. Some major indexes such as DAX and CAC 40 increased but FTSE 100 of Britain decreased due to political and economic uncertainties.

In the Asian region, North Korea's missile tests once again shook the world. However, the Asian stock markets did not react negatively. Most of the indexes still moved forward in September. However, SSE, Hang Seng and TSEC indexes dropped as S&P downgraded China's Sovereign Credit Rating. Last May, Moody also downgraded China. Therefore, although the Chinese economy still showed decent growth, investors are in fact worried about the real estate bubble and its shadow banking system.

Oil price saw beautiful gain in September, thanks to the positive cut down on information. However, it is still 3% lower than last year.

VIETNAM MACRO OUTLOOK

- 2017: Profound Evidence of FDI-Driven Economy
 - State to Speed Up SOE Equitization and Divestment in Final Quarter
-

After nine months of 2017, we think it is time to talk about the economy picture for the whole year. In this part of the Strategy Report, we focus on some highlights under the context of strong performance in the economy as well as a desire of the Government to complete the divestment plan in the final quarter of the year. Besides, the sixth meeting of the 12th Communist Party of Vietnam Central Committee opened on 04 October, is expected to focus its efforts on reforming the country's political system. This issue is addressed by many investors so we expect there will be not any surprises to market during the period of this meeting.

2017: Profound Evidence of FDI-Driven Economy

As we can see in the macro review part, it is important to highlight that the significant rise of GDP in 2017 has been mainly driven by manufacturing. In which, the strong investment of FDI sector has benefited manufacturing activities which have seen their weight in GDP growth increasing in 2017. In 2016, the manufacturing sector represented nearly 29.5% of the GDP. In the first three quarters of 2017, it was more than 33.6%.

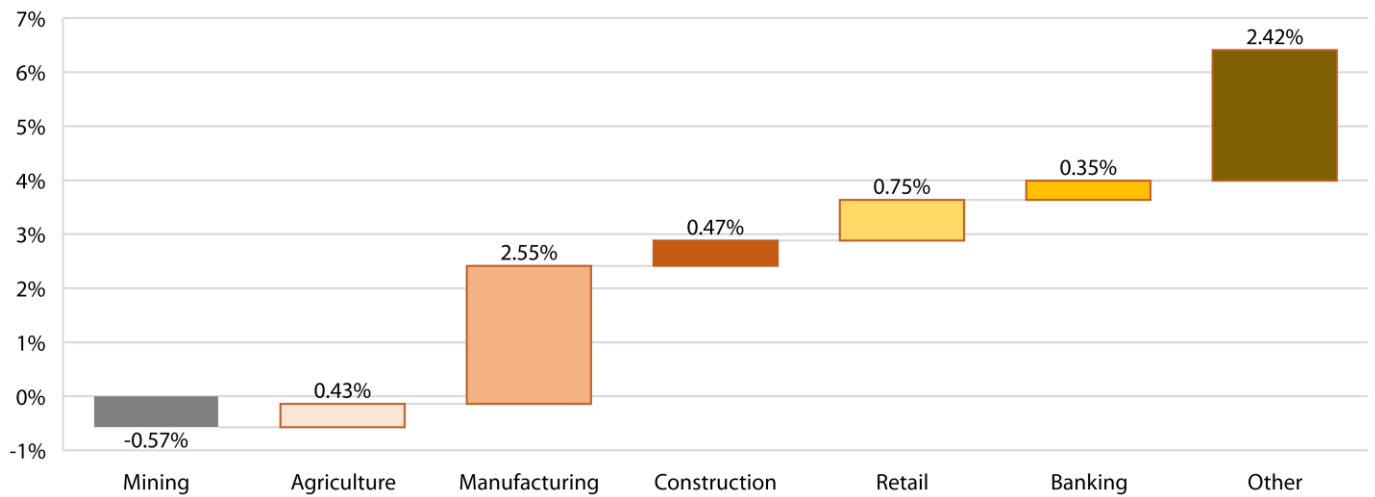
Positive disbursed FDI during the last two years also draw a bright picture for manufacturing activities. Based on these reasons, we expect the strength of manufacturing to persist into next year. Continuing investment in FDI sector also bode well for output growth of construction and domestic building materials sector. However, the growth momentum slowed down in Q3 due to heavy rainy season. Construction sector gained 8.3%YoY in nine months of 2017, declined slightly from a gain of 8.5% in H1 2017. In the first nine months, steel and cement production increased 21.2%YoY and 8.3%YoY, respectively. In Q4, construction activities will be strengthen, we think the recovery of real estate sector plus easing monetary policy could support the outlook of sectors relating to construction next year.

Apart from FDI sector, sectors have seen significant output growth over the past nine months are fishery (+9.4% YoY), fishery feeds (+9.6%), fresh milk (+8.3% YoY), power milk (+9.2% YoY), natural fiber (+16.8%YoY), clothes (+8.7%YoY), urea (+15.9%YoY) and NPK fertilizer (+12.9%YoY). These gains are bound up with the recovery of agriculture sector, textile, fishery exports and strong consumer confidence in Vietnam. The EU-Vietnam FTA will become effective in 2018, this will give more opportunities for Vietnam domestic exporters in textile and fishery sectors. Meanwhile, we think the Government's supports in hi-tech agriculture needs time to show its effectiveness. As a result, agriculture sector might contribute insignificant to GDP growth next year.

Besides, the positive economic environment is bolstering consumer goods industry, banking and real estate activities. The retail, accommodation and catering services sectors combined increased by 8.4%YoY, contributed 17.3% to GDP growth. In the first three quarters of 2017, banking and real estate industry grew 7.89%YoY and 3.99%YoY, respectively, which were higher than the same period of last year. Backed by higher middle-class population, we expect consumer goods, tourism, catering services sectors continue to be healthy in the long-term. At the same time, the recovery of banking and real estate sectors will benefit from the banking reform and strong economic growth.

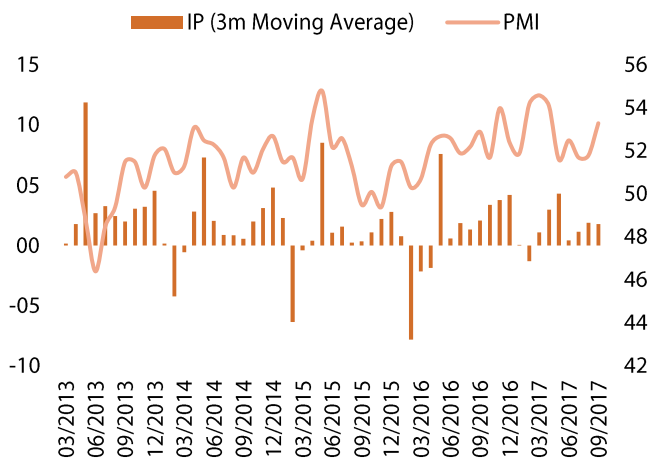
In general, we believe the continued strength of FDI sector should be important drivers for future economic development. Meanwhile, other sectors in the economy will benefit from foreign investment and the support from the Government to upgrade economic growth model. The biggest risk to the economic growth is the lack of interest of foreign investors in Vietnam, not what the number of GDP growth is. However, we think this scenario is not going to happen in the medium term.

Figure 6: Contribution to GDP growth by sector in nine months of 2017



Source: GSO, RongViet Research

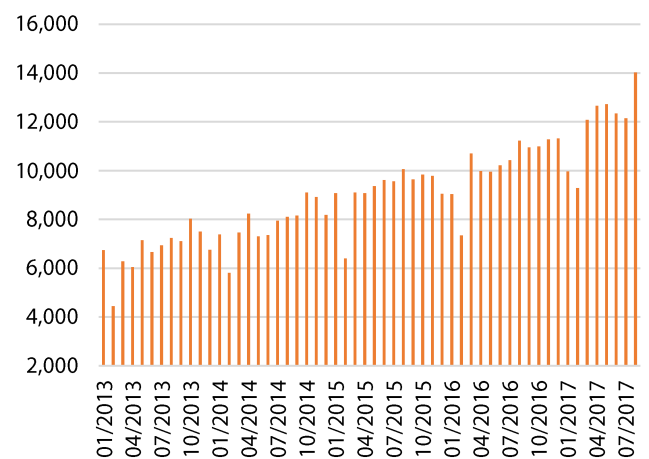
Figure 7: Industrial production movement (2013–2017)



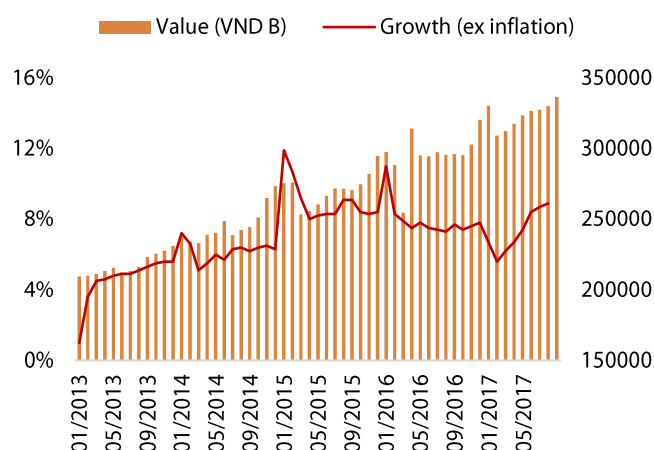
Source: GSO

Figure 8: FDI export (2013–2017)

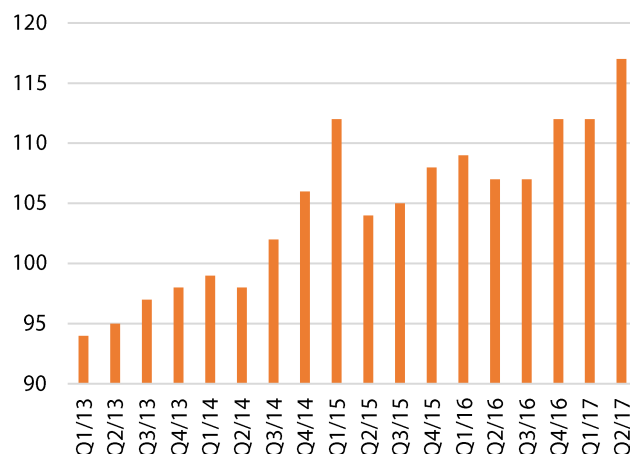
(USD millions)



Source: Customs

Figure 9: Retail sales (2013–2017)

Source: GSO

Figure 10: Vietnam Consumer Confidence (2013–2017)

Source: Nielsen

State to Speed Up SOE Equitization and Divestment in Final Quarter

The recent report from the Corporate Finance Department showed the improvement in SOEs reform progress of equitization in Vietnam. In the first nine months of 2017, the authorities approved for equitization of 34 SOEs. This number is lower than that of last year, however, they are big corporations with actual valuation of VND80,636 billion, of which the actual value of State capital was VND20,811 billion. According to equitization plans, the registered capital of these companies was VND25,837 billion, including VND12,646 billion held by the State, VND7,941 billion to strategic investors, VND205 billion to their employees, VND20 billion to trade unions, and VND5,060 billion from the public via auction. Among these companies, 11 companies completed their IPO plans, most notably names are:

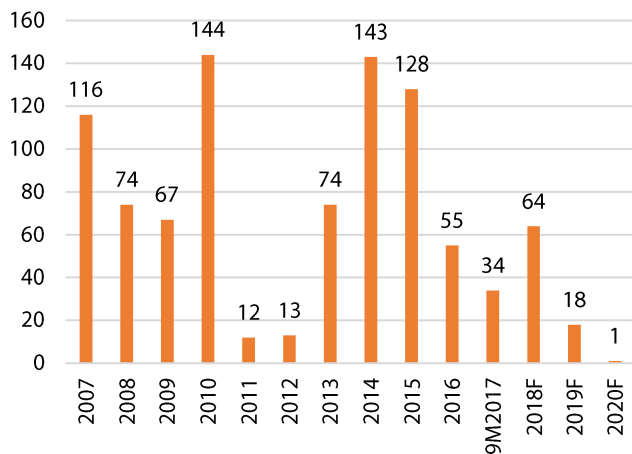
- Investment and Industrial Development Corporation (Becamex IDC) (Charter capital: VND13.17 trillion): in June, the Government has allowed the company to go public by issuing shares to spur its capital, with the State stake to be kept unchanged at 51%.
- Song Da Corporation (Charter capital: VND4,500 billion): revised its IPO plan in the beginning of October. To be specific, the company will sell 200 million shares to the public (~48.82% of its charter capital) instead of 30% of its charter capital in the approved plan.
- Vietnam Urban and Industrial Zone Development Investment Corporation (IDICO) (Charter capital: VND3,000 billion): the company offered 55.3 million shares for sale, equaling a 18.44% stake, with the initial price of VND18,000 in the beginning of October. The average winning price is VND23,940.
- Thanh Le Import-Export (Thalexim) (Charter capital: VND2,366 billion): official IPOed in the end of October with the initial price of VND10,600; offering volume: 11.83 million shares, equaling a 5% stake.

In August, the Government announced the approval process of the equitization plan set for 2017–2020. 18 SOEs had their equitization plans approved by the end of August, completed 14% of the target of 127 SOEs in 2017–2020 period. According to MoF, the Government could complete 86.4% of the 2017 plan (38 SOEs). In addition, we think the equitization progress of many big corporations will be slow due to complex ownership and management structures of those corporations, in addition, some of them also have unclear financial and debt obligations which should be transparent before the IPO.

Most recently, the State has announced it will push up the sale of stakes in Sabeco and Habeco, the two largest beer manufacturers in Vietnam, where the state holds 89.6% and 81.8% of charter capital, respectively. This campaign began in the end of 2016, however, the progress of State divestment from these two companies is still sluggish. According to the Government guidance,

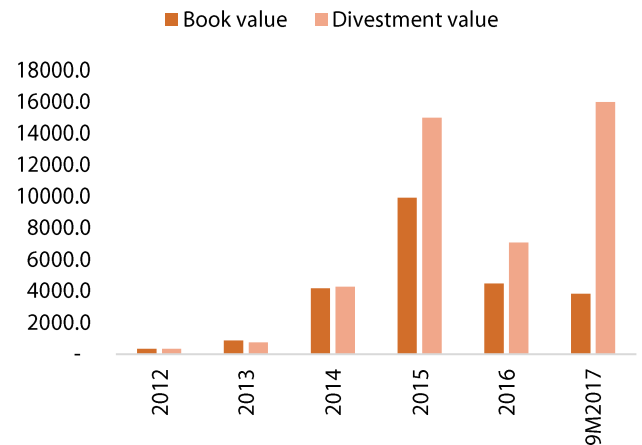
the goal for the State divestment is VND60,000 billion in 2017. By the end of September, the State divested VND3,636 billion and earned VND15,998 billion (including the value divested in 2016 but recorded in 2017). Particularly, it divested VND105 billion from companies in sensitive areas and earned VND105 billion. The divestiture value in other companies was VND2,210 billion and the sale value was VND3,463 billion. SCIC sold State interests worth VND1,522 billion in 28 companies for VND12,428 billion (it sold its partial interests in Vinamilk with a book value of VND783.7 billion in 2016 for VND11,286.4 billion). It showed that Vinamilk was a big deal of the State divestment in the nine months of 2017 and the divestment process should speed up in the final quarter to complete the whole year plan. In our view, the main aim of pushing the State divestment process is to complete the target of budget revenue which will help to narrow budget deficit this year.

Figure 11: Number of privatized SOEs (2007–2020F)



Source: MoF

Figure 12: Divestment value (2012–2017)
(VND billions)



Source: MoF

Q3 2017 Vietnam Macro Review: A Quarter of Goldilocks

GDP Growth Spikes in Q3

According to GSO, the economy grew a bit faster than previously estimated in the second quarter, up 6.28%. Meanwhile, GDP growth continued to robustly rise in Q3, recording its quickest pace in more than six years, up 7.46% QoQ. In the first three quarters of 2017, GDP growth expanded 6.41%, which is higher than our expectation for the whole year.

Assessment: Excluding the negative growth factor in GDP (mining), economic growth in the first three quarters of 2017 was around 7.5%. It is an impressive result compared to other countries in the world. A breakdown of data showed that manufacturing contributed to more than one-third of overall growth, but it should be noted that things happened better than expected, thanks to the FDI sector. Based on the Q3 2017 results, there is no doubt that the government could achieve a GDP growth target of 6.7% in 2017.

Inflation recovered

Average CPI for nine months of 2017 increased by 3.79% YoY. Headline inflation recovered in Q3 2017 due to the increase of public goods and services prices. In addition, a marked acceleration in transportation, construction materials and accommodation was recorded in that period. Even if there was a recovery in headline inflation, core inflation remained stable at 1.45%, lower than its level at the beginning of the year.

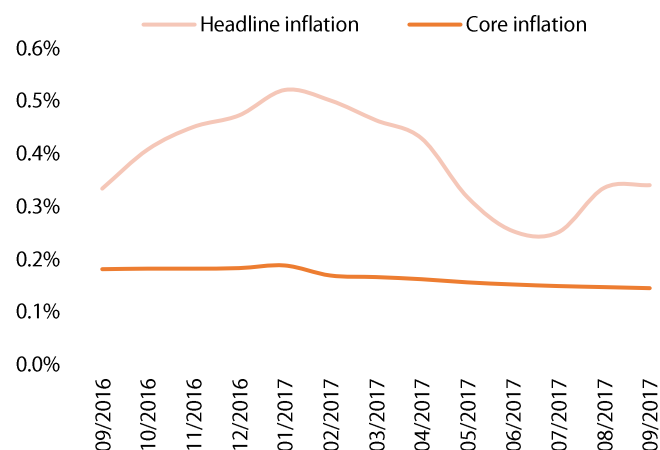
Assessment: At the moment, we see inflation rate showing little upside pressure. Although healthcare services will be hiked twice in 33 provinces in Vietnam for the rest of the year, we think there will be no significant impact on the overall inflation. It could be said that Vietnam has been in a good year, in which the economy is expanding quickly, at the same time, inflation is under control.

Figure 13: Quarterly GDP growth



Source: GSO

Figure 14: Headline and core inflation



Source: GSO

Disbursed FDI improved in September

According to the MPI, Vietnam lured USD25.4 billion in FDI in the first nine months of 2017, up 34.4%YoY. Most projects licensed in nine months include infrastructure projects (thermal power plants and natural gas pipeline) while Samsung Display continued to invest another USD2.5 billion in Vietnam to boost capacity. Notably, the pace of capital disbursement improved dramatically in September. As of September 20, USD12.5 billion of FDI was disbursed, resulting to a rise of 13.4%YoY.

Assessment: It is clear that the investment environment in Vietnam are becoming increasingly attractive in the eyes of direct investors. In the Global Competitiveness Report (2017–2018) by the World Economic Forum (WEF), Vietnam has gained five places in rank, from 60th in 2016 to 55th in 2017 among 137 countries. Accordingly, Vietnam’s competitiveness is significantly driven by its market size. Even with the withdrawal of the US from the TPP, Vietnam’s export remains robust thanks to strong FDI investment.

Consumption continues to drive growth

In Q3 2017, retail sales continued to hit 11.8% YoY, supported by stronger tourism demand and local spending. To be specific, revenue from tourism services recorded a gain of 21.5% YoY while that from retail goods was 11.1% YoY. Thanks to low inflation, retail sales growth (adjusted for inflation) was 9.2%YoY in nine months of 2017, the highest level since March 2015.

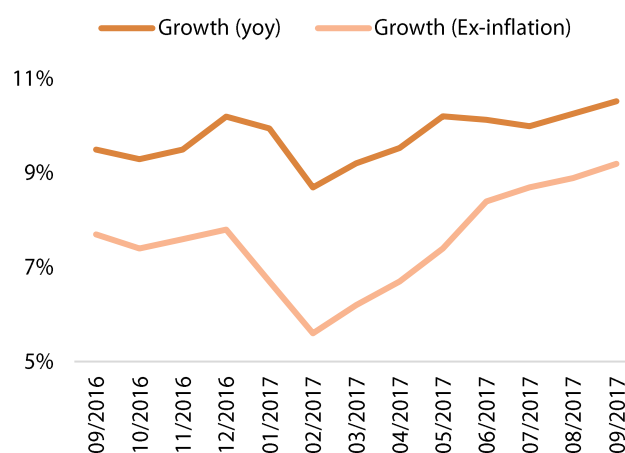
Assessment: It can be said that the positive economic environment is bolstering consumer confidence. According to the latest report of Nielsen, Vietnam consumers are among the top five of the world’s most confident consumers in Q2 2017 with an index score of 117, up five places compared to the end of last year. We think this trend will continue in the final quarter of the year, which will benefit overall consumption in the near term.

Figure 15: FDI capital inflow (USD millions)



Source: GSO

Figure 16: Retail sales growth



Source: GSO

Loan growth steadied in Q3 2017

According to GSO, credit growth was 11.02%YTD as of 20 September 2017. This growth has steadied compared to the data as of the end of August (11.5%YTD). Due to the different statistic periods, we do not think credit growth has slowed down, but basically, we think there was not much growth momentum in credit in Q3 2017. This was also in line with the low overnight cost of borrowing among commercial banks. During Q3 2017, the average overnight interbank rate was around 0.78% per year, which was much lower than the average of 3.4% in Q2.

Assessment: In the middle of Q3, the Prime Minister called for 21% credit growth for 2017. According to our estimates, to achieve this goal, the banking system needs to inject nearly VND500,000 billion into the economy. We think it is infeasible to achieve that expansion in credit base. However, the base scenario for credit growth in 2017 could be 19–20%, which is expected to support the economic growth in the medium term.

Bond issuance declined in Q3 2017

In Q3 2017, the State Treasury raised VND22,435 billion out of the VND38,000 billion offered. The winning ratio plummeted to 54% from 85% in the second quarter. Although there was a steep decline in the government bond issuance in Q3, as of the end of September, the State Treasury completed 81% of the whole year target.

Assessment: In the first nine months of 2017, the government had successfully extended the average maturity of the government debt portfolio. The average of the bonds sold was 18.02 years, a spectacular increase from 8.71 years in 2016. In addition, the average coupon also went down slightly compared to last year. We suppose these movements are good signals for the public debt issue as well as the economic health.

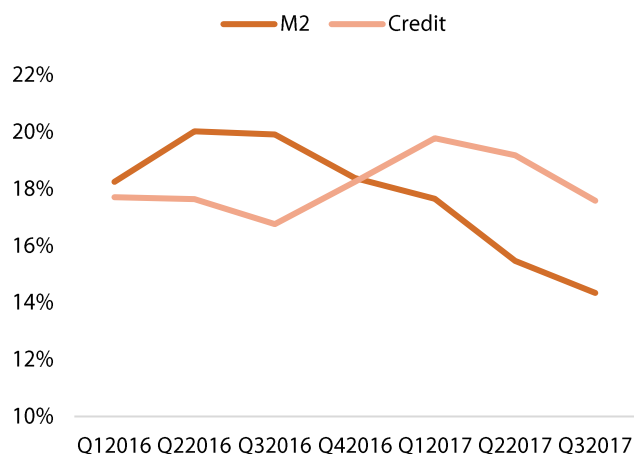
Budget investment expenditure falling short of target

Based on the data provided by GSO, the budget revenue for the nine months presented an increase of 18.2% YoY, fulfilled 64.9% the annual target. In which, external collection (import and export revenue) soared significantly (+38.2%YoY), thanks to the recovery of trade. Domestic collection rose 15.2%YoY mainly due to the improvement of the private sector.

Budget expenditure reached nearly VND851 trillion, fulfilled 61.2% of the annual plan. Expenditures for development investment were recorded at VND153 trillion, even though it increased by 17.5% but fulfilled only 42.8% of the annual plan.

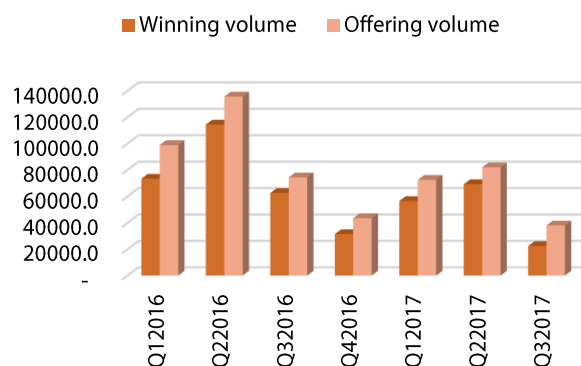
Assessment: Domestic collection from the FDI sector is not in line with the economic growth rate of 6.4% in the first nine months, reaching VND111.4 trillion (+2.8%YoY). Meanwhile, the improvement of the private sector has helped CIT from non state-owned companies and PIT collection rise. Because of debt

Figure 17: Loan vs M2 growth (YoY)



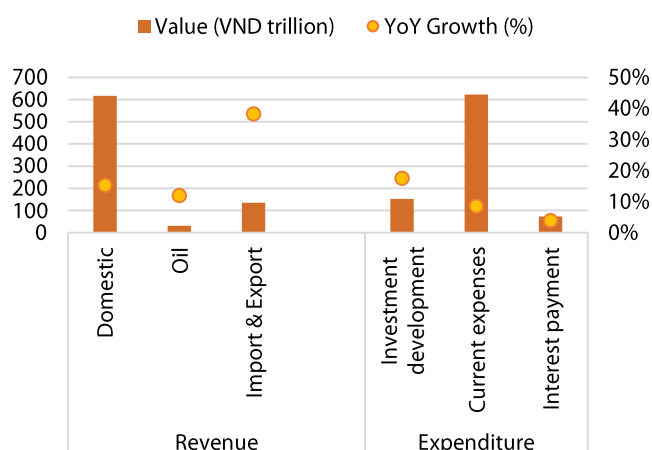
Source: GSO, SBV

Figure 18: Bond issuance (quarterly)



Source: HNX

Figure 19: Budget revenue and expenditure



Source: GSO

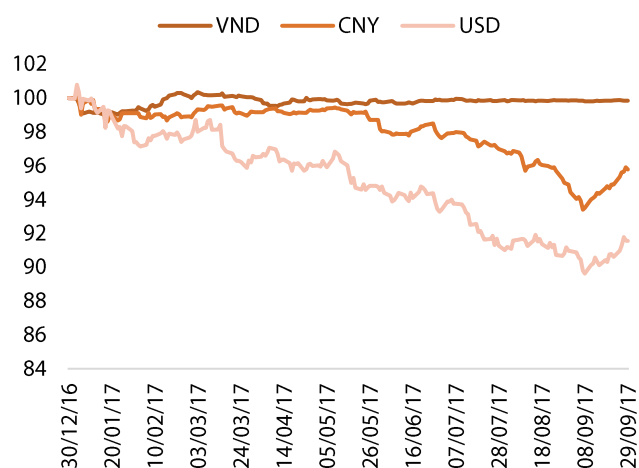
and interest payment burden plus constraints in budget disbursements, the support of fiscal policy to economic growth is still weak at the moment.

No fluctuation in exchange rate

USD/VND exchange rate has been remarkably stable this year despite the 1.4% (YTD) depreciation in official mid-rate in the first nine months of 2017. In year-to-date terms, USD/VND has been trading within a tight range of -1%–0.36% since the beginning of the year.

Assessment: Actually, because of the high dependence on the FDI sector in terms of trade activities, Vietnam does not need a firm exchange rate to curb import prices or a weaker currency to boost export competitiveness. CPI inflation eased to 3.4% (YoY) in September from the year's high of 5.2% in January. Exports expanded a healthy 23.2% (YTD) in the first nine months of the year. Our end-2017 forecast for USD/VND is 22,770.

Figure 20: Exchange rate movement



Source: Bloomberg

2018 OUTLOOK OF VIET NAM'S ECONOMY

The 2018 macro plan points to 6.5-6.7% GDP growth, inflation will be below 4% and trade growth will be in a range of 7-8%. Meanwhile, the fiscal deficit and investment to GDP will be 3.7% and 33-34%, respectively. Based on this prudent plan, we think **policy makers put stability as the top priority in 2018**. Other priorities are (1) accelerating SOE reforms, especially IPOs progress; (2) further promoting the private sector to upgrade growth driver; and (3) solving a problem of slow public investment growth.

- In the near term, we think **strong FDI investment is a solution to boost economic growth**. According to our estimates, FDI sector contributes about 20% of GDP, nearly a quarter of total investment, two-thirds of total exports and millions of direct and indirect jobs. In addition, FDI commitments accelerated in 2017, reflecting positive investor sentiment about Vietnam's long-term economic potential. As a result, the development of FDI sector will have a positive impact on the capital stock, production capacity, income and spending spillovers to the rest of the economy.
- Besides, **the Government is working to make the private sector the main engine of growth** through removing the barriers to the development of private manufacturing firms and SMEs and providing more conducive business environment (credit access, land, tax, other legacy issues). There has been cutbacks in SOE capital formation as long as improvements of private investment in recent years. However, we think there will be a long way in improving private sector efficiency and its contribution to growth. Due to the limited fiscal space, greater private participation in infrastructure projects is underway.
- **SOE reform, which is the hardest part of all reforms**, is currently still far from certain. Historical experience suggests that an adverse growth shock may be needed to get things really moving. Vietnam has executed about 20% of 44/135 IPOs/divestment planned for 2017, suggesting a large rollover to 2018. There are also 64/181 IPOs/divestments planned for next year.

In 2018, **we have little to worry about on the inflation front**. Headline inflation has averaged just below 4% so far in 2017, while core inflation also remains low. Although policy makers have a formal inflation target of 4%, we think they will pay more attention to the core rather than the headline rate to guide the market in monetary policy. We expect slow recovery in oil prices to help to keep a lid on underlying price pressures, and for core inflation to average just 2% in 2018, a rate which policy makers are likely to be comfortable with.

On policies, we believe **policy makers will continue to be supportive, appropriate demand support and structural reforms are needed to reinforce growth momentum**. Monetary policy should remain accommodative, given that inflation is in line with the Government's target. Meanwhile, policy makers should start rebuild fiscal space by implementing fiscal consolidation plans. Structural reforms are needed to help reduce external imbalances and vulnerabilities and promote more sustainable growth. Regarding to exchange rate management, we believe the SBV will improve the normal operation as well as prepare for a more exchange rate flexibility in 2018.

Table: Key economic indicators

	2014	2015	2016	2017F	2018F
ECONOMIC GROWTH	5.98%	6.68%	6.21%	6.70%	6.60%
TRADE BALANCE (USD B)	+1.5	-4.1	+1.5	+1.8	+1.8
EXPORT GROWTH	11.6%	8.1%	9.0%	21.0%	13.5%
IMPORT GROWTH	15.9%	12.0%	5.3%	21.0%	14.0%
INFLATION	1.9%	0.6%	4.7%	4.0%	4.0%
REFINANCING RATE	6.5%	6.5%	6.5%	6.25%	6.25%
M2 GROWTH	16.0%	14.5%	18.4%	15.0%	16.0%

CREDIT GROWTH	12.6%	17.3%	18.3%	20.0%	18.0%
BUDGET DEFICIT/GDP	4.7%	4.6%	3.9%	3.5%	3.5%
EXCHANGE RATE	21,405	22,540	22,790	22,750	23,000

Source: RongViet Research

CHALLENGES OF VIETNAM ECONOMIC

1. High public debt: a constraint for economic growth

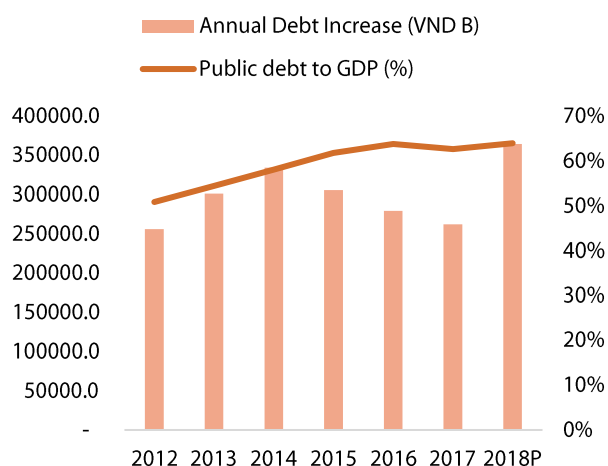
- The Government estimates that Vietnam's public debt burden is 62.6%GDP as of end-2017, declining from 63.7%GDP in 2016. While the public debt to GDP ratio is decreasing, the absolute amount is still rising (+9.1% compared to end-2016). Under the current plan, public debt to GDP would rise to 63.9% in 2018 and the Government faces challenges in controlling budget deficit in the next few years.
- **Vietnam's public debt has been rising 1.5 times higher than the economic growth** in the past five year and now nears its ceiling of 65%GDP. However, the country's financial sustainability is generally neutral compared to other countries in region at present (Table: ASEAN sustainability matrix). Thus, we believe that the current concern is that **the high level of debt-to-GDP ratio acts a drag on economy growth** because the debt burden refrains the Government to invest in public infrastructure.

Table: ASEAN sustainability matrix

% GDP	Short-term external debt	External debt	Household debt	Loan to Deposit Ratio	Public debt
Thailand	14.0	34.0	81.0	110.0	47.8
Phillipines	5.0	26.0	7.0	67.0	44
Vietnam	7.0	39.0	na	92.0	62.6
Indonesia	5.0	37.0	10.0	93.0	31.1
Malaysia	29.0	74.0	89.0	85.0	54.3

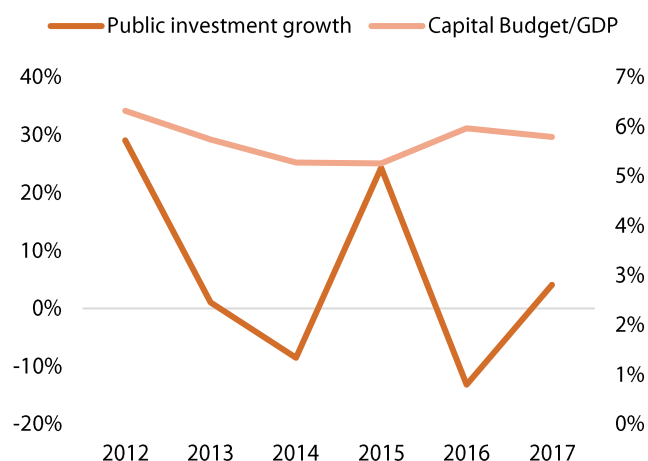
Source: HSBC, RongViet Research

Figure: Public debt to GDP ratio and incremental debt



Source: GSO, RongViet Research

Figure: Public investment



Source: GSO, RongViet Research

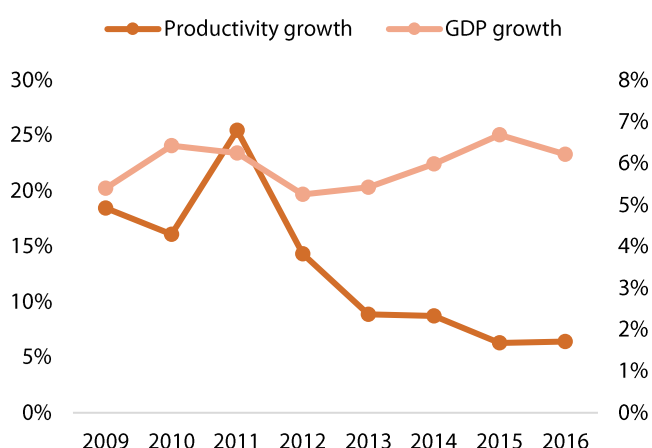
- The Government called for scaling down the state sector and expediting the privatization and divestment of state capital in recent years, which aimed to mobilize resources for infrastructure development. In addition, SOE equitization could be a reliable source of funding for fiscal budget. However, **slow progress in implementing SOE reform is posing risks to medium-term growth prospects**.
- Vietnam aims to equitize 137 additional SOEs in 2017-2020, divestment from SOEs will bring USD11 billion to finance development investment. In nine months of 2017, the Government has executed about 20% of IPOs/divestments planned for 2017, suggesting a large rollover to 2018. There are also 64/181

IPOs/divestments planned for next year. It can be seen that the main challenge to SOE reform is that many remaining companies are large with complex ownership and management structures, in addition, some of them also have unclear financial and debt obligations which are difficult to be solved.

2. Low productivity growth is a concern for long term prospects

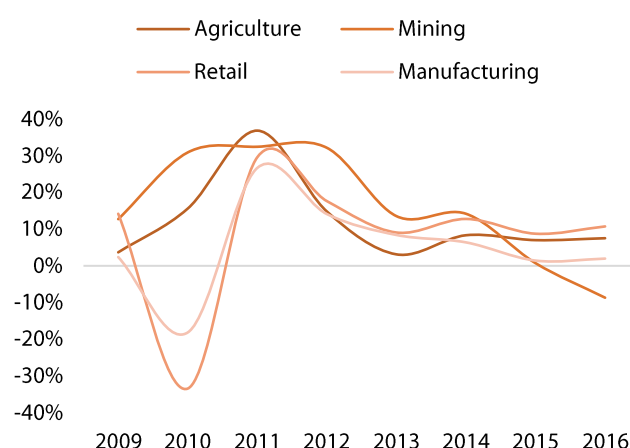
- **Contrary to the recovery of GDP growth, Vietnam has experienced a productivity growth slowdown since 2011.** Data showed that the strong performance of manufacturing sector might not be supportive for boosting productivity growth. Over the past five years, output in the manufacturing industry has grown at comparable annual rates of about 9.2%, while the labor productivity in this sector has expanded at a more modest rate of 6.4%. The fact that productivity growth of manufacturing industry slowed to just 1.4% and 2% in 2015 and 2016, respectively.

Figure: Vietnam productivity growth vs. GDP growth



Source: GSO, RongViet Research

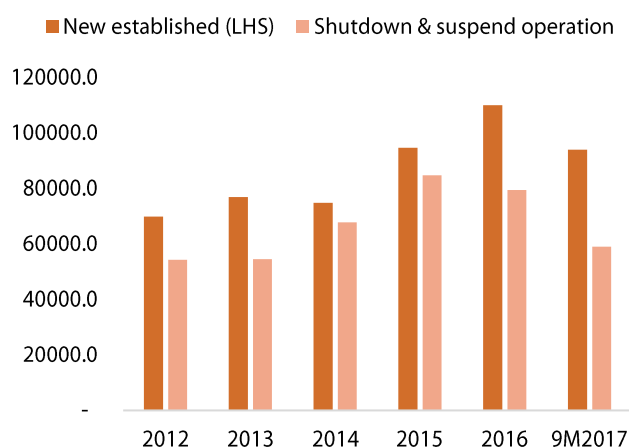
Figure: Sector-Level labor productivity growth



Source: GSO, RongViet Research

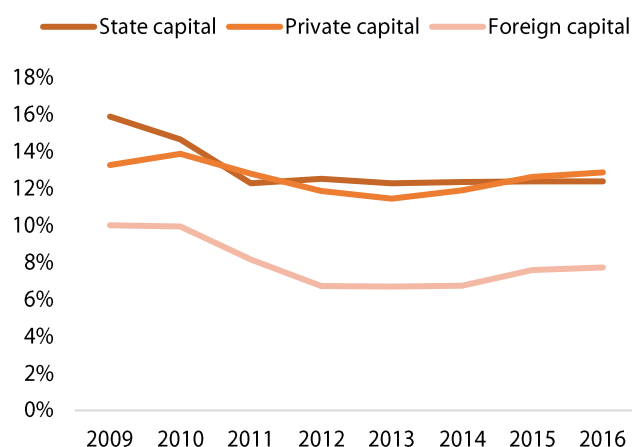
- There is a recovery in private sector business activities, investment and business confidence in recent two years. In addition, the Government asserts the role of the private economy as an important driving force of economic growth in the long term. However, we think **there has been a lot of obstacles for private businesses to grow and eventually make it to the top.**
- The Vietnam 2035 Report shows that the productivity and competitiveness of Vietnamese private sector are decreasing. In addition, Vietnamese firms are engaged in the global/regional production network but with weak positions in the global/regional value chains.
- The low quality growth of the private sector can be attributed to many factors, including (1) the weak framework responsible for ensuring private property rights, free and fair competition, (2) Difficult access to production factors (land, capital, information, infrastructure and labour), and (3) Matters are not helped by the weak capacity of private firms in terms of legal and market savvy, development vision and networking, not to mention weak corporate governance and culture.

Figure: Business Activities



Source: GSO, RongViet Research

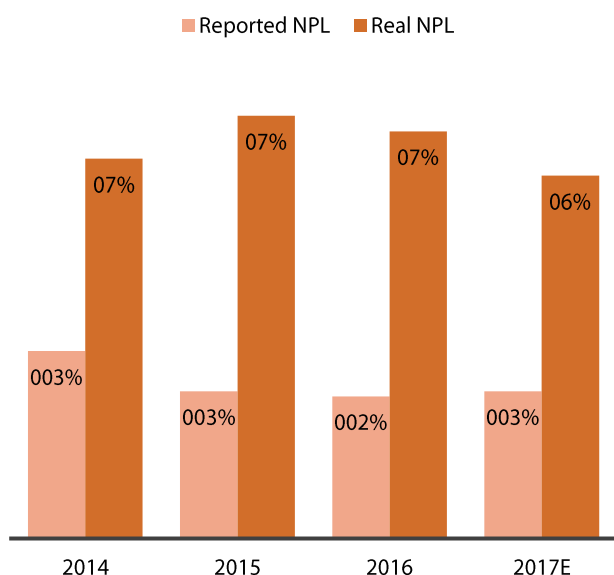
Figure: Sector-level investment to GDP ratio



Source: GSO, RongViet Research

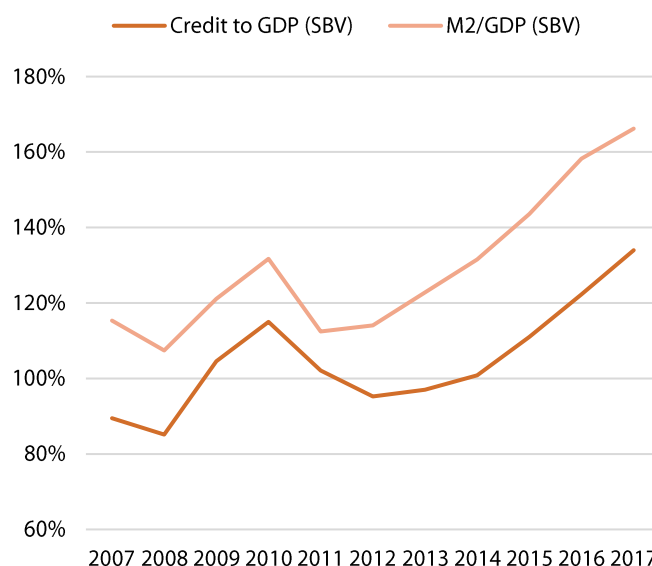
- **Delays in addressing lingering NPL problems could hinder productivity growth** by preventing the reallocation of resources. Since 2013, the Vietnam Asset Management Company (VAMC) has reclaimed over VND301 trillion of bad debts from 42 credit institutions. Albeit meaningful progress has been achieved this year thanks to the resolution 42 on settling bad debts, the VAMC has resolved only 20% of the bad debt purchased. In addition, Vietnam's credit-to-GDP ratio is now close to levels reached during previous periods of macroeconomic instability, as a result, a heavy reliance on bank loans for growth remains a source of concern for future bad debts.

Figure: NPL ratio



Source: SBV, RongViet Research

Figure: Credit and M2 Expansion



Source: GSO, RongViet Research

3. External environment creates great financial instability

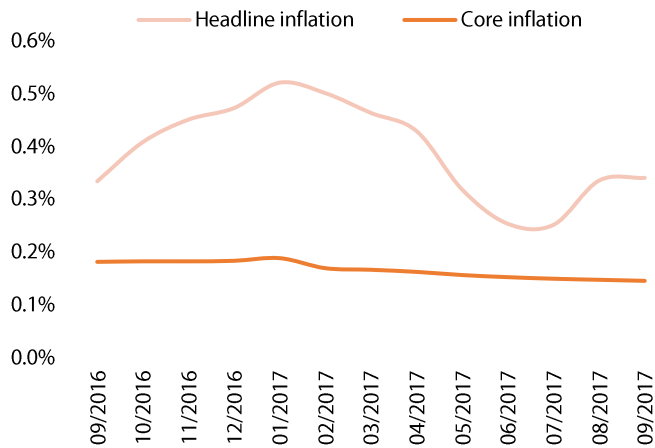
- In 2017, China's economy seems to be holding up relatively well with growth drivers looking to be more boardly based. With credit expansion softening, we expect the economy to cool next year, but China could

pilot a soft landing. However, Vietnam must carefully watch the Chinese situation because the development of China's economy and RMB may pose potential problems for Vietnam. At the moment, China is moving to a more flexible currency system. If the transition is smooth, there should be no great difficulty for Vietnam.

- Central banks have made financial stability possible in recent years. But their monetary policies have now reached their limits, and it is difficult to expect more easing. At present, market believes the Fed was very cautious in raising its rates and will be able to do so without too much damage to the financial market. If the Fed makes a mistake, it will be necessary to bet on a sharp drop in equities, and on a contagion especially in emerging markets.

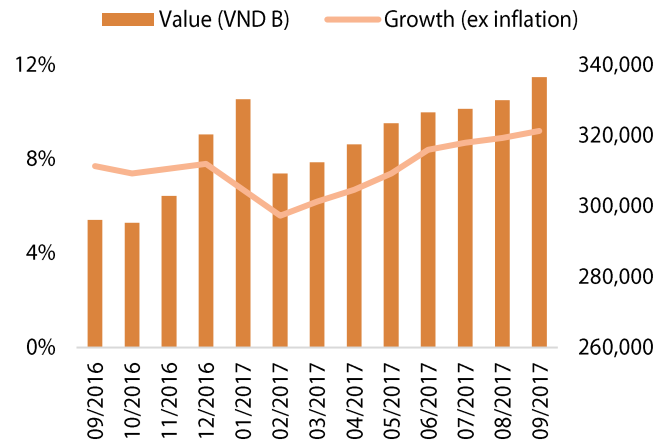
MACRO WATCH IN SEPTEMBER

Stable inflation



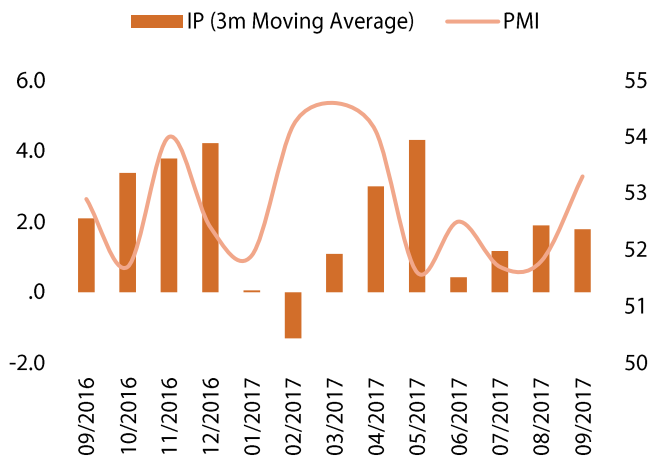
Source: GSO, RongViet Research

Continuous improving in retail sales



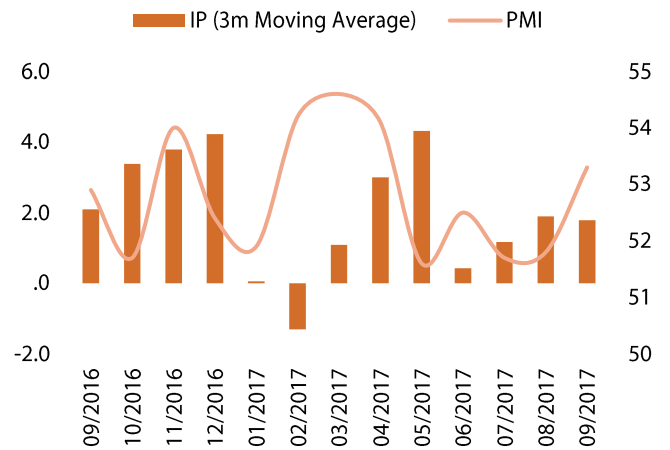
Source: GSO, RongViet Research

PMI increased sharply in September



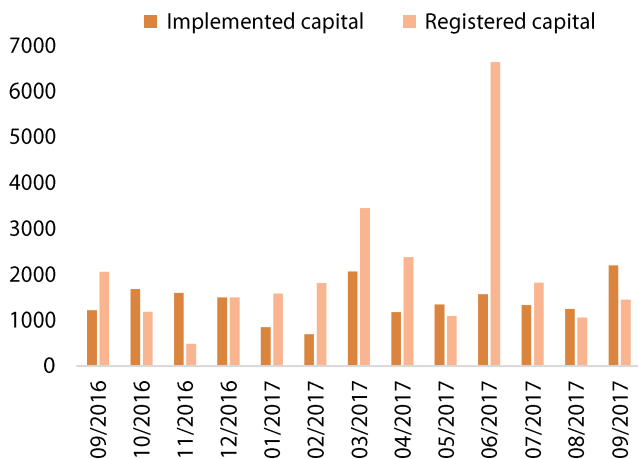
Source: GSO, RongViet Research

Trade growth steadied



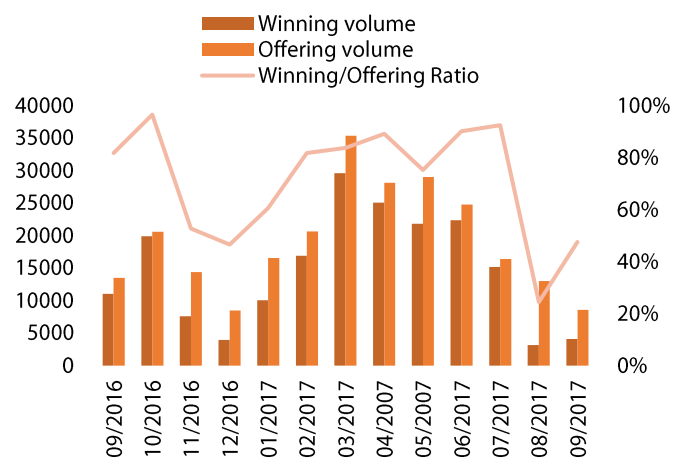
Source: GSO, RongViet Research

Improved disbursed foreign capital



Source: FII, RongViet Research

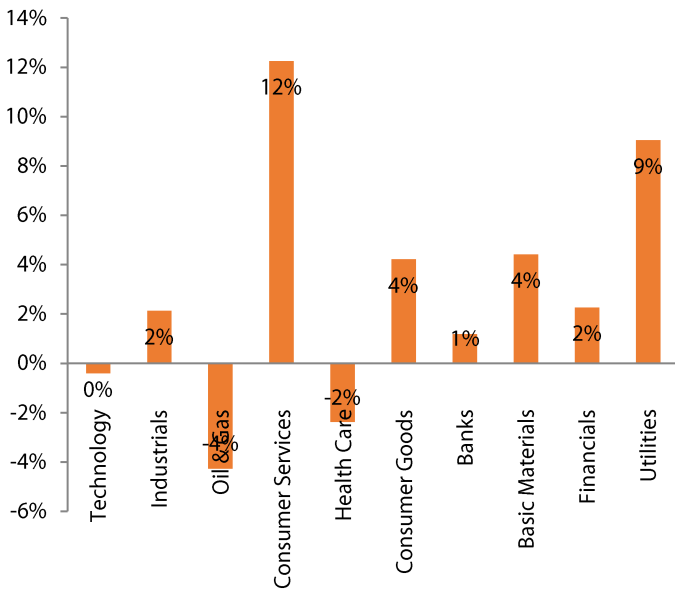
Winning volume decreased sharply in Q3



Source: VBMA, RongViet Research

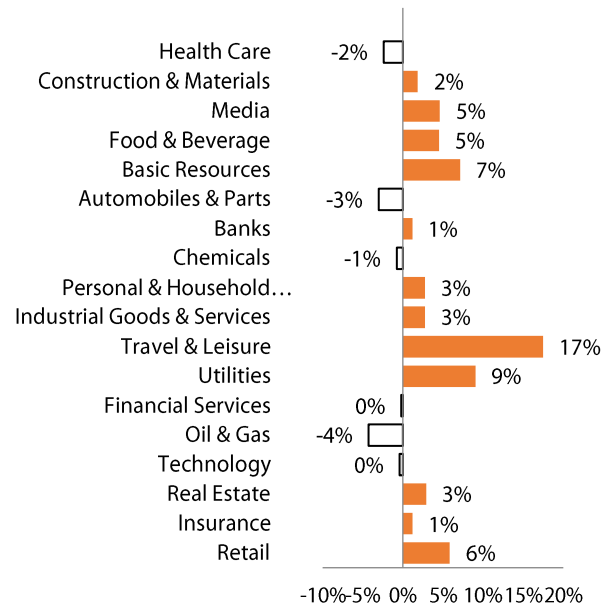
INDUSTRY INDEX

Level 1 industry movement



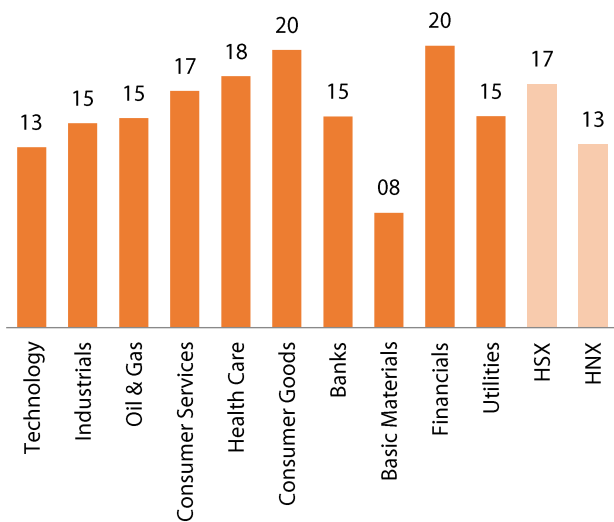
Source: RongViet Research

Level 2 industry movement



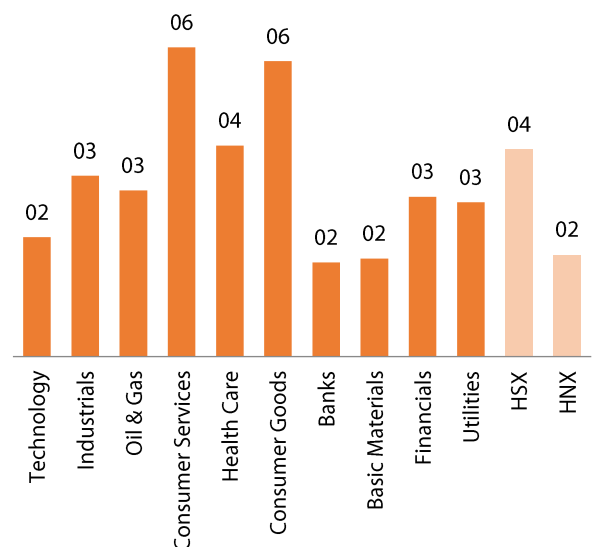
Source: RongViet Research

Industry PE comparison



Source: RongViet Research

Industry PB comparison



Source: RongViet Research

