5th April 2023

Macro Report

ECONOMIC GROWTH Q1/2023 and CRITICAL CHANGES IN MONETARY POLICY

- *Economic growth in Q1/2023 was much lower than expected.*
- *Loosening monetary policy is becoming more apparent.*

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VIETNAM ECONOMY

- Economic growth in Q1/2023 was much lower than expected
- Loosening monetary policy is becoming more apparent

Economic growth in Q1/2023 was much lower than expected

Although we have predicted low economic growth in 2023, the actual data in Q1/2023 was much lower than expected. In the first quarter of the year, GDP growth was only 3.3%. If not considering the time when the economy was negatively impacted by Covid-19 (Q1/2020 and Q3/2021), this is the lowest growth rate since Q1/2009. The slowdown in growth came from one of Vietnam's best growth engines ever, the manufacturing sector fell 0.4% yoy and was the only negative growth rate in the statistical data series if not considering the Q3/2021 period, which was negatively affected by Covid-19. Specifically, the manufacturing and processing industry in March 2023 did not recover as expected and dropped by 1.7% yoy. In Q1/2023, the manufacturing and industrial sector decreased by 2.3% over the same period. Besides, the negative growth sectors in the first quarter included real estate (-0.1% yoy) and healthcare (-1.6% yoy). The construction sector associated with real estate services and public investment was not much better, increasing only about 2.0% yoy, lower than the average growth rate of about 5.5% of this sector in 1Q during the past five years.

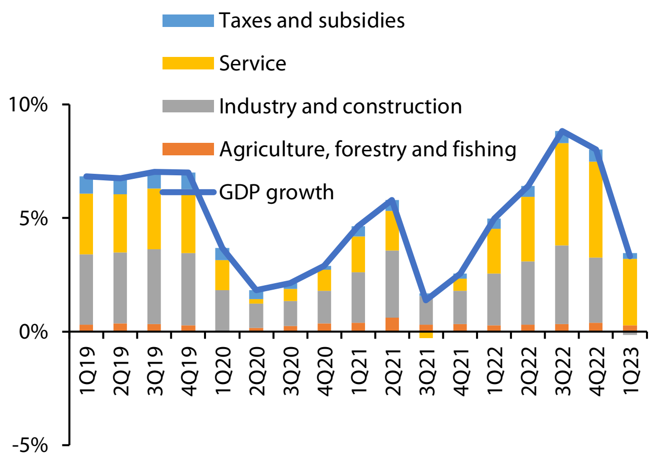
Contrary to the manufacturing sector's decline, the service sector still maintained a growth rate of 6.8% yoy, thanks to the benefits from the low base effects in Q1/2022. Specifically, the growth in retail, accommodation, food and beverage services, entertainment, and administration increased by 8.1-26.0% over the same period. The financial and banking sector alone increased by 7.7% over the same period, lower than the average growth rate of this sector in Q1 in the period of 2020-22 and equal to the average growth rate before Covid-19. The agriculture, forestry, and fishery sectors are the most stable sectors of the economy, maintaining a steady growth rate of 2.5% in Q1/2023.

Figure 1: Vietnam's GDP by economic activity

	1Q22	2Q22	3Q22	4Q22	1Q23	1Q22	2Q22	3Q22	4Q22	1Q23
	% yoy					% pt contribution to GDP				
Real GDP	**5.0**	**7.8**	**13.7**	**5.0**	**3.3**	**5.0**	**7.8**	**13.7**	**5.6**	**3.3**
Agriculture	2.4	3.1	3.7	0.4	2.5	0.3	0.3	0.4	0.5	0.3
Mining	1.2	4.5	6.4	(0.1)	(5.6)	0.0	0.1	0.2	0.2	(0.2)
Manufacturing	7.8	11.1	11.6	1.9	(0.4)	1.8	2.5	2.8	0.7	(0.1)
Construction	2.6	4.9	17.5	0.2	2.0	0.1	0.3	1.2	0.5	0.1
Wholesale & Retail Sales	3.0	8.3	24.9	0.4	8.1	0.3	0.8	1.9	0.6	0.8
Transportation & Storage	7.1	9.5	27.3	0.0	6.8	0.4	0.5	1.3	0.3	0.4
Accommodation & Food	(1.8)	26.6	172.3	(0.3)	26.0	(0.0)	0.5	1.7	0.7	0.6
Financial services	9.8	8.7	9.3	0.6	7.6	0.5	0.4	0.5	0.5	0.4
Real estate	1.8	6.2	11.8	0.0	(0.1)	0.1	0.2	0.4	0.2	(0.0)
Other	4.9	7.2	11.0	1.9	3.9	1.6	2.1	3.2	1.6	1.1

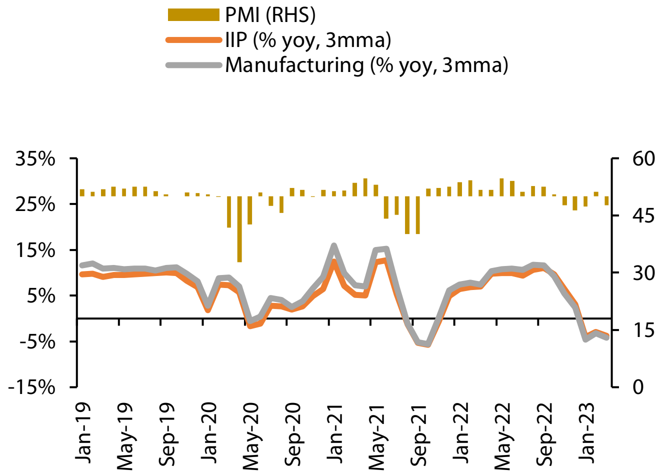
Source: GSO, RongViet Securities

Figure 2: GDP by sector (% yoy)



Source: GSO, RongViet Securities

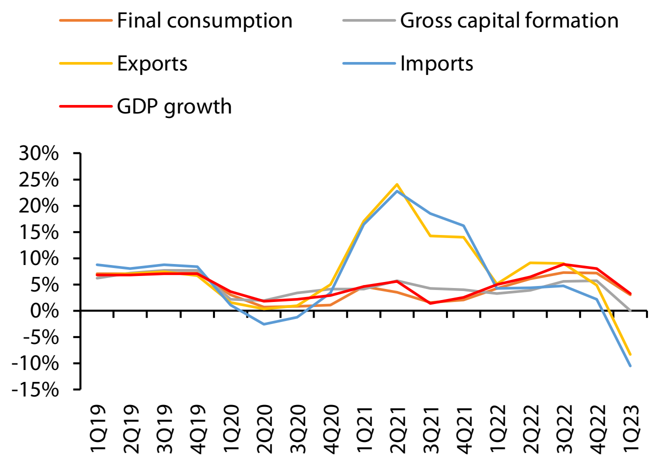
Figure 3: Manufacturing and PMI



Source: GSO, RongViet Securities

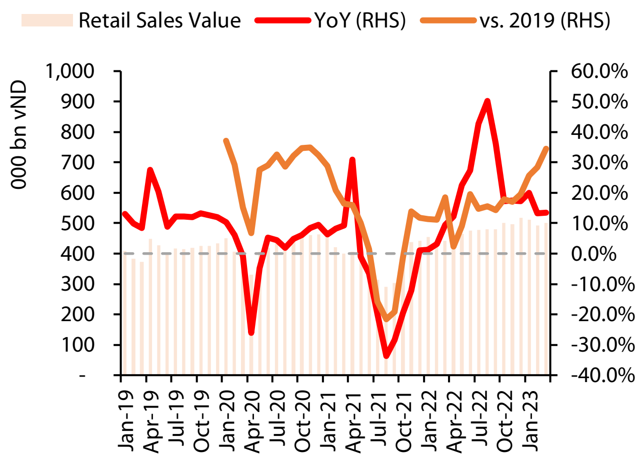
From a usage perspective, the economic growth picture deteriorated significantly. In which, final consumption increased by only 3.0%, equivalent to the increase in Q1/2020 and considerably lower than the average increase of this group without considering the Covid-19 periods. Gross capital formation barely grew in 1Q2023 while the import and export picture softened markedly, which is foreshadowed by the trade growth data. The impact of the decline in external demand on Vietnam is also evident in the GRDP growth of some provinces with sizeable industrial scale and FDI concentration, such as Bac Ninh (-11.9% yoy), Quang Nam (-10.9% yoy), Binh Duong (+1.2% yoy) and Dong Nai (+3.3 % yoy). However, some provinces still recorded better GRDP growth, such as Thai Nguyen (+6.5% yoy), Bac Giang (+8.4% yoy) and Hai Phong (+9.7% yoy). Meanwhile, Ho Chi Minh City, the country's economic growth engine, shows a less optimistic picture when GRDP growth in Q1/2023 is only 0.7% yoy. In which, construction and real estate sectors production decreased by 19%yoy and 16% yoy, respectively, retail accounted for more than 18% of the city's GRDP structure, increasing by only 3.8%. The above developments show that all growth drivers are weakening significantly, partly due to the decline of the FDI and export sectors and primarily due to domestic drivers, such as consumption and investment.

Figure 4: GDP growth by usage (% yoy)



Source: GSO, RongViet Securities

Figure 5: Retail sales growth



Source: GSO, RongViet Securities

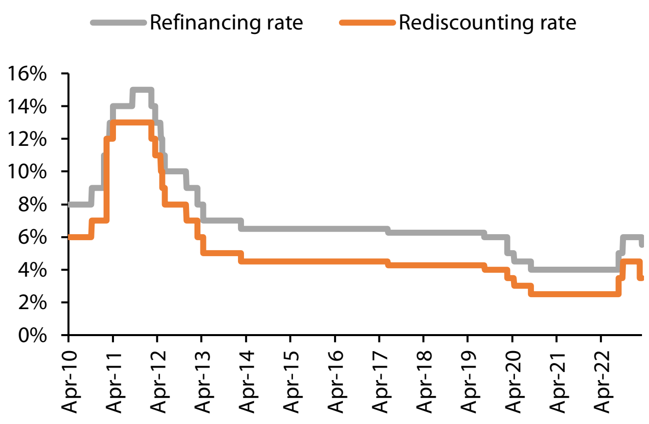
Currently, the Ministry of Planning and Investment still maintains the scenario of GDP growth for the whole year at 6.5% with a growth target of 6.7-7.9% in the remaining quarters. We believe this goal is challenging and unfeasible in the context that the world economy is on the edge of recession, the decline of the real estate market, and domestic consumption is only in the early stage, and the expectations of China's reopening and recovery story are progressing quite slowly. Rong Viet's previous forecast for GDP growth in 2023 is 5.6%. With economic growth in Q1/2023, we revised down our full-year GDP growth forecast to 5.0% based on: 1) improved industrial production in the coming quarters; 2) business and consumer confidence recovered from the second half of 2023 thanks to the easing of monetary policy to support growth; 3) Public investment in the coming quarters is expected to accelerate faster than Q1 and grow by ~20% over the same period. The assumptions for our forecast include: 1) global economic growth will slow down moderately, 2) the interest rate and inflation will cool down, which will boost credit growth and consumer demand, and 3) further policy support.

The move towards easing monetary policy is becoming apparent

As our recent Analyst Pinboards mentioned, the SBV quickly reversed monetary policy in March 2023. Firstly, there were twice adjustments to the regulatory interest rates in the middle and at the end of March. Accordingly, the discount and refinancing rates decreased by 100 basis points and 50 basis points, respectively, in the past month. Other-oriented interest rates also fell, such as the ceiling interest rates for demand deposits and 1–6month term deposits decreased by 50 basis points to 0.5%/year and 5.5%/year, respectively; the ceiling of VND short-term lending rates for some priority sectors also reduced by 100 basis points to 4.5%/year.

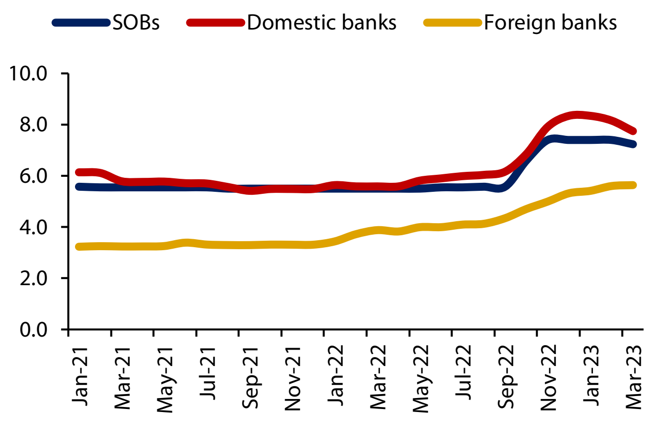
Looking into the interest rate hikes last year, the change in the SBV's regulatory interest rates often followed the market. On the contrary, we expect the recent regulatory interest rate reduction to impact the market interest rate levels significantly. After the decision of the SBV at the beginning of April 2023, commercial banks from the State to the private sector have all reduced deposit interest rates by 0.3-0.8 percentage points. Thus, since the beginning of the year until now, deposit interest rates have decreased relatively sharply by about 0.8-1.2 percentage points, this decrease is equivalent to about ½ of the increase from October to December 2022. According to the SBV, the average lending interest rate for new and old loans at the end of February 2023 was 9.5-11.3%/year, an increase of about 0.5-0.6 percentage points compared to the end of 2022 and 1.1-1.4 percentage points higher than the interest rates levels before October 2022. We expect lending interest rates in the economy to decrease soon based on some reasons: 1) the cooling of deposit rates as a prerequisite for lowering lending rates; 2) system liquidity is abundant, credit demand is weak, lending interest rates will decrease per supply-demand law; 3) a credit package of VND120,000 billion will be implemented from April 1, 2023 with a preferential lending interest rate of 8.2-8.7%/year for developers and buyers of social and worker housing projects and rebuilding old apartments. The expected reduction in lending interest rates is about 0.5 - 1 percentage point, depending on the sector. The ceiling interest rate of 4.5%/year is not much different for the priority sectors, but it is opening a capital channel at a cheaper cost for the real estate sector. The absorption level depends on 1) the dynamism and flexibility of the real estate developers, 2) the risk tolerance/benefit balance of the banks, and 3) a list of projects licensed by the Ministry of Construction.

Figure 6: Refinancing rate and rediscount rate (%/year)



Source: SBV, RongViet Securities

Figure 7: Deposit rates for 12-month term (%/year)



Source: RongViet Securities compiled

As we recognize the inefficiency of implementing the 2% interest rate support package, the SBV is opening more doors to minimize systemic risks and promote growth recovery. For example, the draft amendment to Circular 16 seems to open an opportunity for commercial banks to "reach out" to support the corporate bond market, although we see that the door is not too wide and is accompanied by strict supervision regulations to ensure that there are no additional risks in the future. Or the latest messages of the authorities about the postponement and rescheduling of debts for businesses in difficulty also create more hope, binding that if this policy is issued, it must also carefully consider the dosage and target audience. Regarding the regulation of system liquidity, the SBV also has a consistent liquidity support orientation. According to the SBV's announcement, from the beginning of the year to now, it has bought about $4 billion, equivalent to recovering about 15%-17% of the foreign currency loss in the volatile exchange rate period of 2022. This also means that the SBV net injected about VND94 trillion through foreign currency purchases while implementing a net withdrawal of about VND110 trillion through the issuance of 91-day SBV bills. From the middle to the end of March 2023, the OMO activities stopped entirely due to the sharp drop in interbank interest rates, and commercial banks no longer needed to borrow from the SBV. If this situation continues, from the end of May 2023, a large amount of liquidity (~VND110 trillion) will be pumped into the market due to the maturity of 91-day bills.

Looking at the upcoming policy roadmap, the SBV will likely be consistent with easing monetary policy as the pressures on inflation, exchange rate, and tightening global monetary policy have partly eased. If the risk that many investors are worried about is a global recession, the continued reduction of the regulatory interest rates is probably within the SBV's prediction.

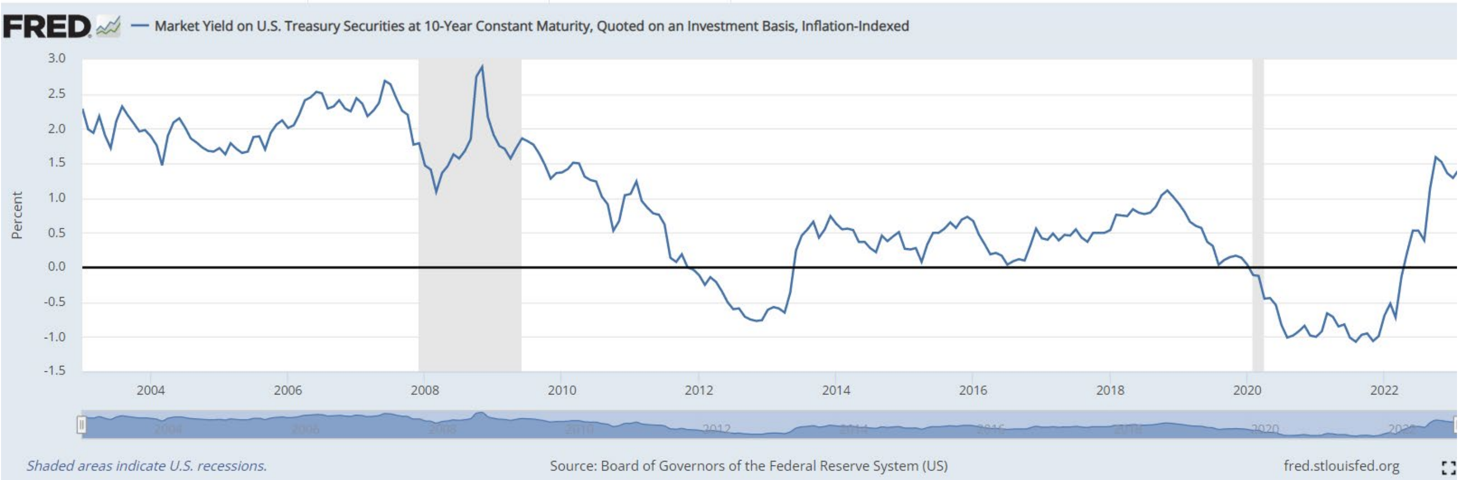
Banking worries

- The US Fed and FDIC[1] have done a terrible job since the 2007-09 financial crisis.
- The Silicon Valley Bank failure may be the beginning of something grimmer.
- The European Central Bank (ECB) hiked the main refinance rate by 50bps in March.
- The US Federal Reserve signaled that there will only be a further rate hike this year.

So far we are not seeing signs of massive stock market panic or volatility yet in the wake of bank failures, so it does seem that the impact can be contained. The US Federal Reserve has taken measures to enhance liquidity provisions for the US banking sector (discount window, bank term funding program) and offered daily currency swaps with central banks elsewhere, which has restored some confidence in the system, even as both the Fed and the European Central Bank have gone ahead to hike rates as focus on inflation remains steadfast. For now, we are not expecting a repeat of the events in 2008 that followed the Lehman Brothers debacle, but more needs to be done probably by central banks to restore financial stability in the coming weeks.

US real interest rates are at a choking point (Figure 1) for the economy and financial markets, hence the yield curve is flattening from an inversion. Corporate earnings are set for their biggest decline from this point while layoffs will accelerate - typical late cycle. The balance of probabilities suggests that the maximum pain in margin contraction, job layoffs and earnings are set to unfold through this quarter and next. **There is unlikely to be any deeper banking problems although delinquencies are likely to rise.**

Figure 8: US real interest rates.



In the US today, if you're a wealthy vulture capitalist with over $250,000 in uninsured deposits at a loosely-regulated bank, the federal government will guarantee that your money is safe in a weekend.

If you're a struggling working person with no health insurance and get cancer, you're on your own.

That's what Martin Luther King Jr called "socialism for the rich and rugged individualism for the poor."

Despite the financial turmoil, the ECB decided for a 50bp hike in March to suffocate inflation pressures. In contrast, China cut its Reserve Requirement Ratio by 25bp as it attempts to exit deflation. Notwithstanding near record US bond volatility, the lack of cross-border contagion into Asia/EM is worth noting since most central banks are by and large finished hiking. The Bank of

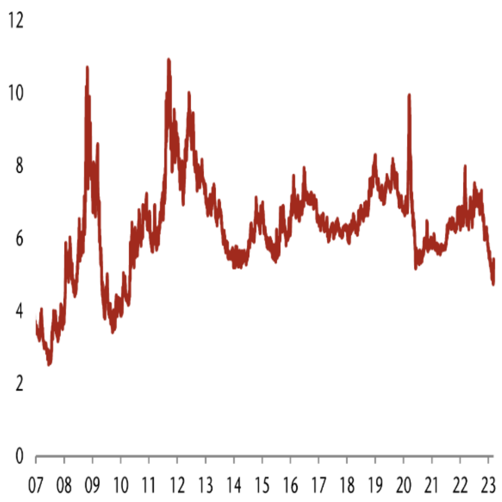
[1] *The Federal Deposit Insurance Corporation is a United States government corporation supplying deposit insurance to depositors in American commercial and savings banks. The FDIC was created by the Banking Act of 1933, enacted during the Great Depression to restore trust in the American banking system.*

Canada said in February that it was done with raising rates. We believe the Swiss Central bank is also done.

Contrary to the US, in Europe there is no asset-liability mismatch or spillover effects of an asset bubble bursting. Ironically, not only are the economies re-expanding but earnings and target price revisions are some of the best in the world. European banks face neither the aftermath of speculative bubbles popping nor a liquidity crisis resulting from stretched asset-liabilities. Perversely, observing Eurozone labor markets would suggest that the ECB has much more work to do in containing wages and core CPI. The ECB hiked the main refinance rate by 50bp to 3.5% and deposit facility rate to 3%, in a well-telegraphed move. This rate increase comes against the backdrop of emerging stress in the global banking sector, surrounding a handful of regional banks in the US and a big European lender (Credit Suisse). Inflation concerns, nonetheless, took precedence.

European financial conditions have actually been relatively loose. Realized economic data has been better than expected and European earnings are being revised up across a wide range of sectors while equity risk premium as been going down (Figure 2).

Figure 9: Europe ex UK forward equity risk premium (%)



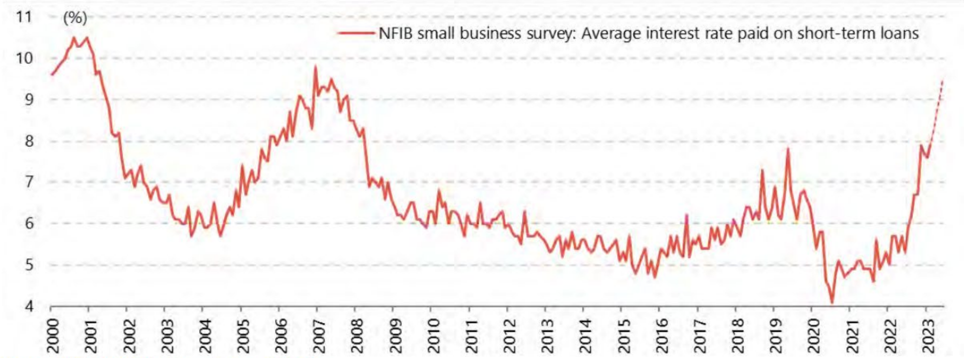
Source: Jefferies

There is the issue of Credit Suisse. But this not new. Credit Suisse's problems are also relatively unique, with a string of major financial losses and scandals that have worried investors and fueled a recent client exodus. Credit Suisse customers – primarily wealthy clients and businesses rather than everyday savers – have been pulling money from the bank for months, leading to more than 111bn Swiss francs (£99.7bn) of outflows late in 2022. It is not immediately clear whether client withdrawals have gathered pace as a result of its plunging share price.

The bank is in the process of a major restructuring plan, meant to stem major losses, which ballooned to 7.3bn Swiss francs (£6.6bn) in 2022, and revive operations hampered by multiple scandals over the past decade involving alleged misconduct, sanctions busting, money laundering and tax evasion.

On the other hand, the interesting point about the three US banks; Silicon Valley Bank, Signature Bank and First Republic , the one missed predictably by most mainstream media, is the hint it provides of the growing mostly unacknowledged financial problems building in the former boom areas of private equity and private lending. This is because these three US banks were unusual as banks because they are so closely interwind with the private equity echo system. The credit boom in the past cycle was in private lending, or shadow financing. But that does not mean that there will be no impact from monetary tightening. Rather in a world if the US enters recession. SVB will be seen as the first hint of the problems to come in private equity, just as the failure of New Century Financial in April 2007 was the first hint of the problems to come in subprime mortgages from monetary tightening. This year will be the year when earnings downgrades hit the stock market if forecast proves to be accurate. This is now the key issue in world financial markets. Then 2024 will be the year when markets will have to deal with the emerging credit problems in the private space.

Figure 10: Small businesses average interest rate paid on short-term loans

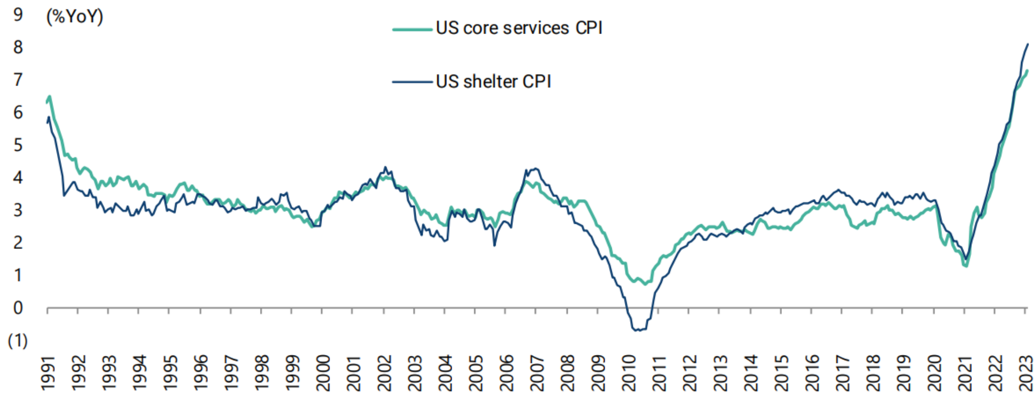


Source: NFIB Small Business Survey, Jefferies

US headline CPI inflation and core CPI inflation slowed from 6.4% y/y and 5.6% y/y, respectively, in January to 6.0% y/y and 5.5% y/y in February, both in line with consensus expectations. Still, the problem for the Fed is that these are still high numbers (Figure 5). That is why 10-yr yields are still high (Figure 4).

Figure 11: US 10-yr yields. %

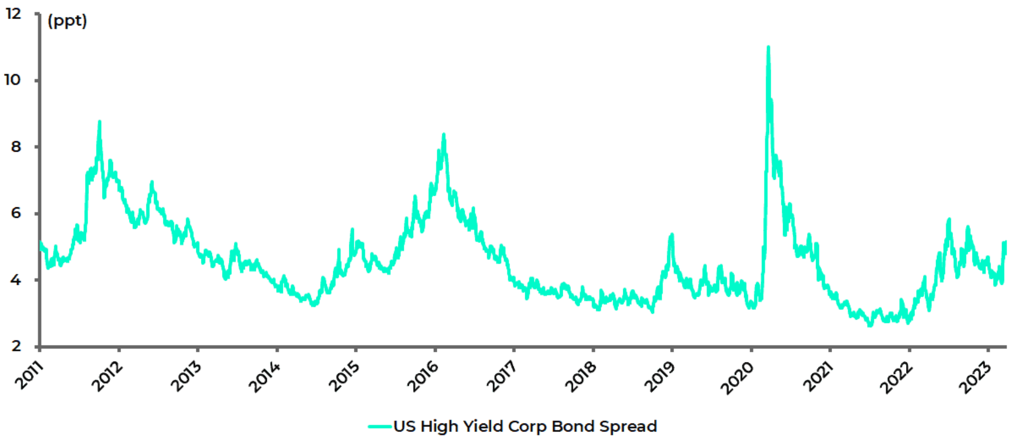
Figure 12: US core services CPI and shelter CPI inflation



Source : US BLS

The US high-yield corporate bond spread rose from 271bp in late December 2021 to a recent high of 583bp in July 2022 and is now 516bp, though up from 389bp in early March (Figure 6).

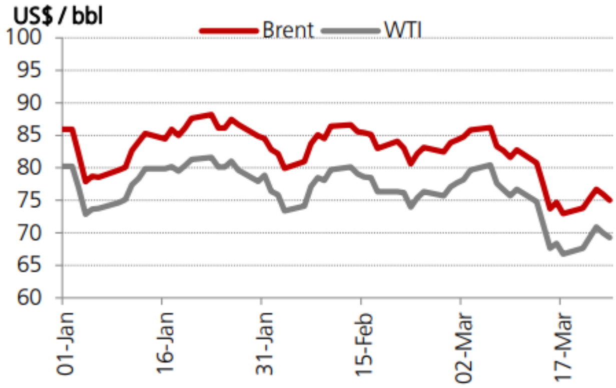
Figure 13: US high yield corporate bond spread over 10-yr Treasuries



Source: Grizzle.com

Brent crude oil prices dipped to a low of US$73/bbl recently, before recovering to around US$76/bbl as we write, down 12%-16% from US$86/bbl levels earlier in March. This is on the back of the recent banking crisis in the US and Europe, which saw confidence sapping and fund flows pulling out from risk on trades. Given that the fundamentals for the oil market do not seem to have changed meaningfully in the light of mid-sized bank runs in the US and the forced takeover of Credit Suisse, we would like to believe that the dip in oil prices is more of a blip at the moment rather than a sustained move below US$80/bbl (Figure 7). As financial markets stabilize, we reckon oil prices should gradually recover to where they were.

Figure 14: Oil prices 2023 ytd, US$ per barrel



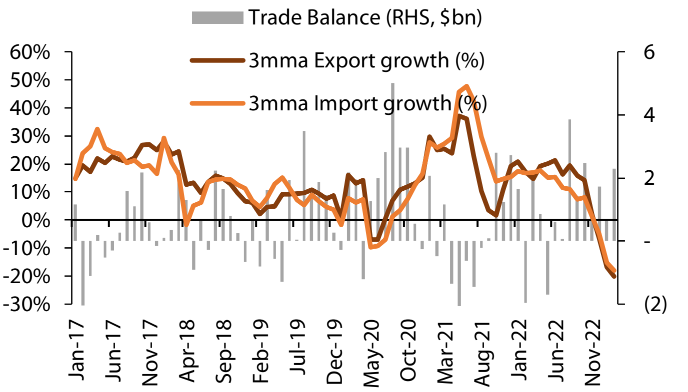
Source: DBS

<u>Bottom line:</u>

- The US has the difficult policy position of banks tightening credit spreads, high positive real rates, drawing deposits out of the banking system and an entire inverted yield curve that is lower than the Fed Funds rate – a classic overtightening.
- Meanwhile, Europe is experiencing strong PMIs and positive sales revisions with the ECB yet to quench the latent wage inflation – a typical nominal GDP boom is playing out.
- Japan is hesitating on dealing with inflation worried that a deflationary defeat will be snatched from the jaws of a reflationary victory.
- China is in the throes of a series of policy U-turns with the real estate's three red lines being relaxed, the economy reopening hastily from its zero-Covid policy and rapprochement towards the private sector. Mainland monetary policy needs to be on the back foot to make sure the velocity of money rises.

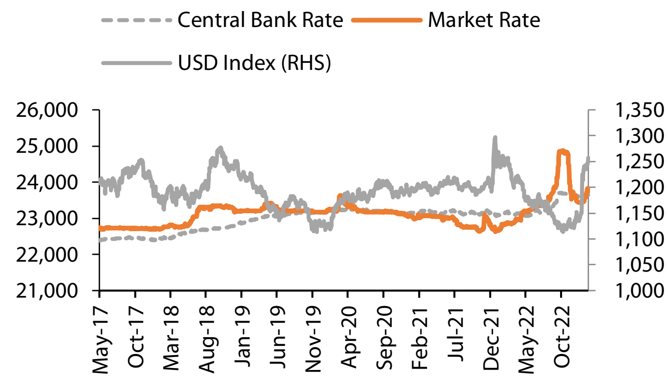
VIETNAM ECONOMIC INDICATORS IN MARCH 2023

Trade balance



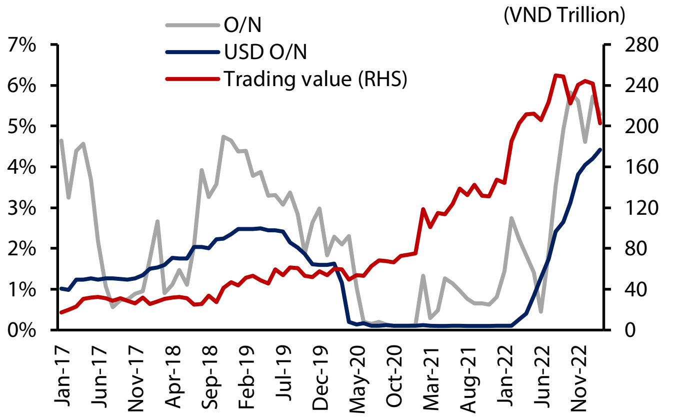
Source: GSO, Rong Viet Securities

USDVND exchange rate



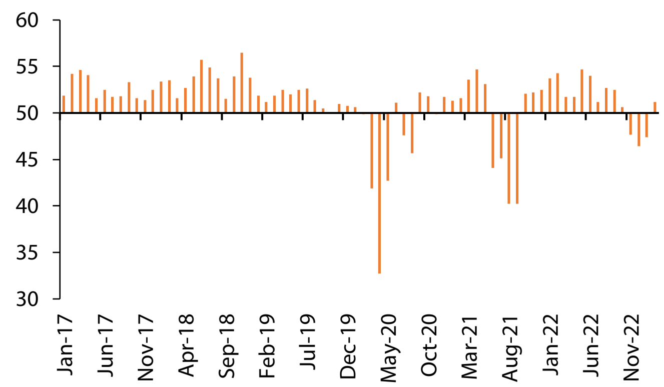
Source: SBV, Bloomberg, Rong Viet Securities

Interbank interest rate (%/year)



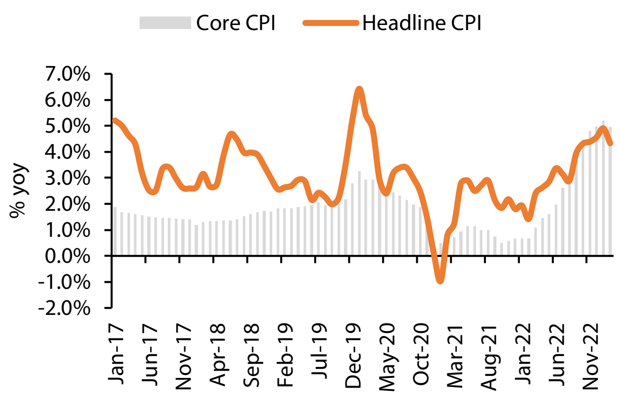
Source: SBV, Rong Viet Securities

Vietnam PMI



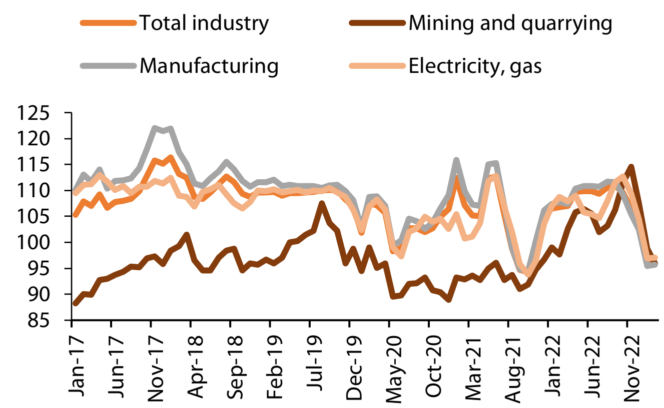
Source: IHS Markit, Rong Viet Securities

Vietnam CPI



Source: GSO, Rong Viet Securities

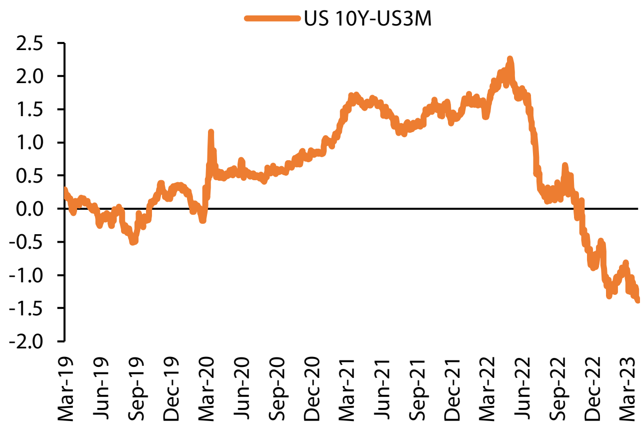
3-month MA Industrial Production Indices



Source: GSO, Rong Viet Securities

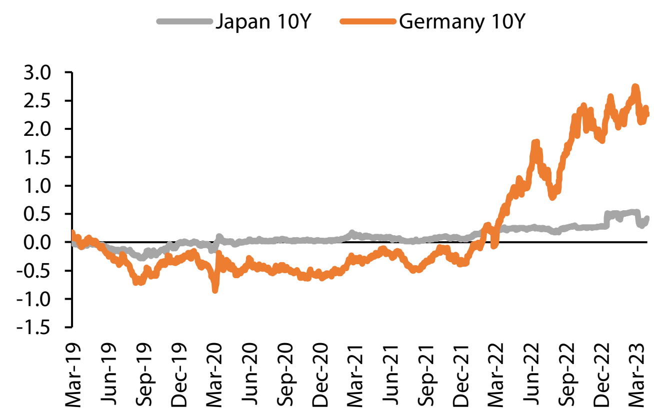
GLOBAL ECONOMIC INDICATORS IN MARCH

US G-Bond yields gap (%/year)



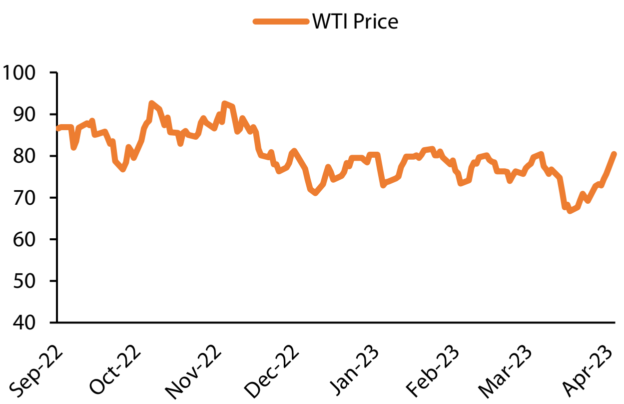
Source: Bloomberg, Rong Viet Securities

Germany and Japan 10Y G-Bond yields (%/year)



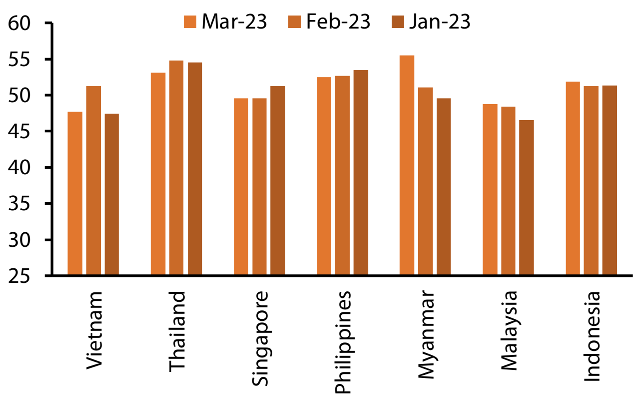
Source: Bloomberg, Rong Viet Securities

WTI crude oil price (USD/barrel)



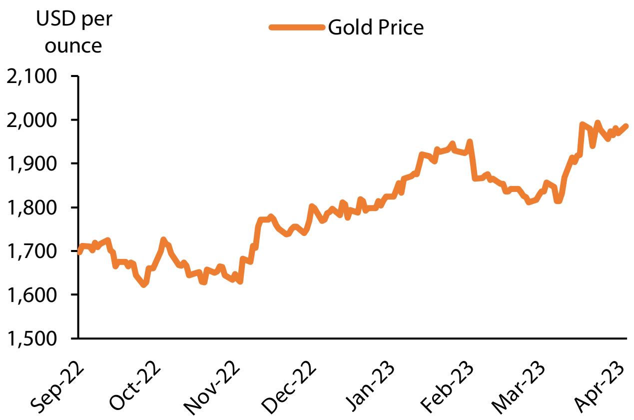
Source: Bloomberg, Rong Viet Securities

ASEAN's PMI



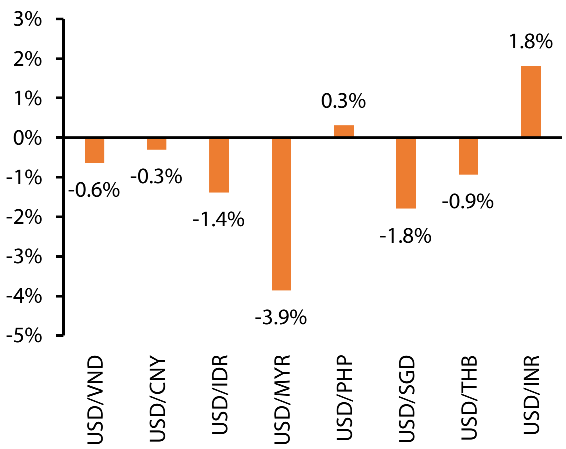
Source: Markit Economics, Rong Viet Securities

Gold prices (US$/ounce)



Source: Bloomberg, Rong Viet Securities

FX rates (%, YTD)



Source: Bloomberg, Rong Viet Securities

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