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Special Report

Impact Of US Trade Policies: Warning Point For KORUS FTA's Negotiations

At the end of 2016, the United States elected Donald Trump, a non-traditional leader with a tougher style on trading issues than his predecessor, Barack Obama. It has since been reflected in the fact that the US withdrew from the Trans-Pacific Trade Partnership (TPP), renegotiations of NAFTA and KORUS, as well as the implementation of tariffs on imported goods at the beginning of 2018. All of this creates potential "trade wars" between the US and its trading partners.

In this report, we focus on the lessons learned from the renegotiation of the US – South Korea Free Trade Agreement (KORUS FTA) which is seen as a warning point for Vietnam. The country ranks 5th in the list of nations having the largest trade surplus with the US.

There is no doubt that Vietnam is part of a number of countries that benefit from the openness of the US market. South Korean companies play an important role in connecting Vietnam to the rest of the world. South Korean companies have been very large investors in Vietnam. Giants like LG and Samsung have built significant export bases in Vietnam.

Any changes in the KORUS FTA as well as the direction of US trade policies is likely to affect Vietnam in the mid and long term. The US and South Korea are the biggest customers and suppliers of goods to Vietnam.

Bernard Lapointe – Head of Research

bernard.lapointe@vdsc.com.vn

Tu Vu

tu.va@vdsc.com.vn

Thuy Nguyen

thuy.nb@vdsc.com.vn

MAIN CONTENT

THE US NEW TRADE POLICY AND THE 3-PARTY RELATIONSHIP: SOUTH KOREA – VIETNAM – US

- The trade principles of Donald Trump
- South Korea and the United States – Vietnam's two leading partners
- Assessment of the three-party relationship between South Korea – Vietnam – the US

The trade principles of Donald Trump

Since the establishment of the World Trade Organization (WTO) in 1995, global trade is currently experiencing several changes caused by the rise of nationalism and trade protectionism. While the U.K. has decided to leave the European Union, US President's Donald Trump is pursuing a tough commercial policy labelled "American First". The White House implemented many tariffs and started the renegotiation of free trade agreements with close allies after he took office. The renegotiation of the US - Korea Free Trade Agreement (KORUS FTA) is likely to affect Vietnam directly because both countries are among Vietnam's major trading partners.

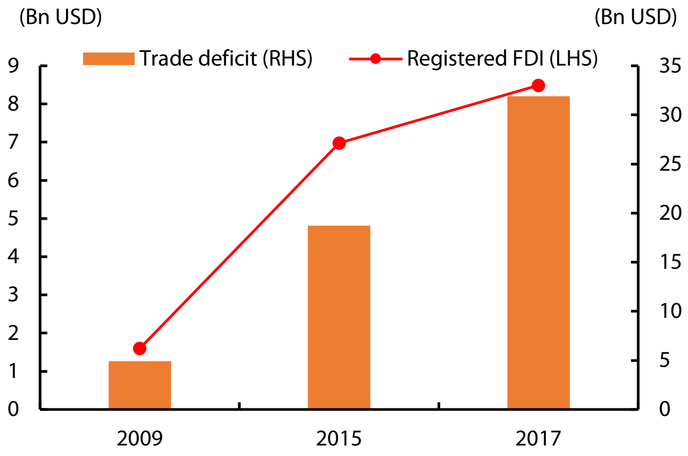
01/2017 03/2017 08/2017 01/2018 03/2018

• Donald Trump took office • The US withdraws from TPP	• Enforcement of anti-dumping laws • US trade deficit causes Trump to re-think its trade policy	• Launch of NAFTA renegotiations • Launch of KORUS FTA renegotiations • Put taxes on large residential washing machine (50%) and solar batteries (30%) imported into the US from all countries	• Put taxes on steel (25%) and aluminum (10%) imported into the US for all countries except Canada and Mexico

South Korea and the United States – Vietnam's two leading partners

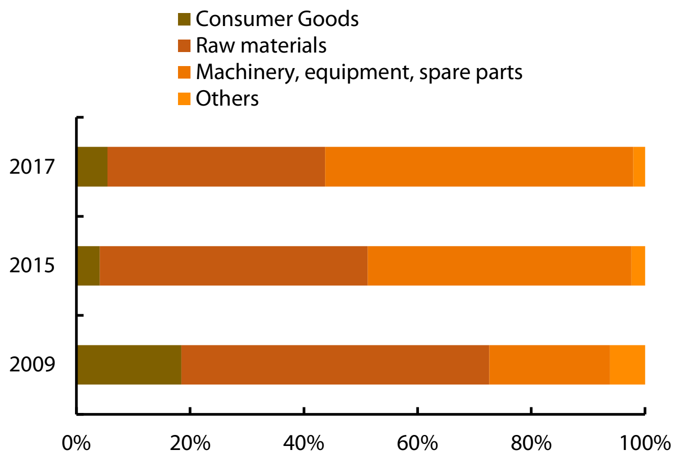
By the end of 2017, Korea surpassed China and became Vietnam's largest supplier of goods. The country's total trade deficit reached nearly USD 31.9 billion, compared with China's USD 22.8 billion. That reflects serious changes in the bilateral relationship between Vietnam and Korea, especially since the South Korea - Vietnam Free Trade Agreement (VKFTA) came into effect in 2015.

Figure 1: South Korea's FDI and Trade with Vietnam



Source: Customs, GSO, RongViet Securities

Figure 2: Goods imported from South Korea



Source: Customs, RongViet Securities

Notably, Korea became the largest FDI investor in Vietnam. The registered investment in 2017 amounted to nearly USD 8.5 billion. Because of that South Korean and Vietnamese ones are deeply involved in the global supply chain. Imported goods from South Korea such as machinery, equipment tools and spare parts account for 54% of total imports. Most imports serve the processing and manufacturing industries.

Table 1: South Korea's major investment projects in Vietnam (Bn USD)

No.	Projects	Investment Capital	Main products
1	Samsung Electronics HCMC CE Complex (SEHC)	1.4	High-end TV products, production of other consumer electronic products, including washing machines
2	Samsung Electronics Vietnam (SEV)	2.5	Phone & Electronic Equipment, Battery (SDI), Display Screen (SDV), Vacuum Cleaners
3	Samsung Electronics Vietnam THAINGUYEN(SEVT)	5	Telephones & Electronic Devices, Processors & Integrated Circuits
4	Samsung Display Vietnam (SDV)	6.5	Electronic screen OLED, AMOLED
5	LG Display	1.5	Electronic OLED
6	LG Innotek	0.6	Cameras
7	LG Electronics	1.5	Mobile phones, TVs, household electrical appliances, including washing machines

Source: RongViet Securities

Meanwhile, the US is still the largest export for Vietnam as the total sales of goods has increased continuously and stood above USD 41 billion in 2017. According to US Census Bureau, the country recorded a USD 38 billion trade surplus with the US in 2017.

Figure 3: Vietnam – US trade

Source: Customs. RongViet Securities

Figure 4: US trade decifit in 2017

Rank	Countries	Bn USD
1	China	-375.2
2	Mexico	-71.1
3	Japan	-68.8
4	Germany	-64.3
5	Vietnam	-38.3
6	Ireland	-38.1
8	Malaysia	-24.6
10	Korea	-22.9
11	Thailand	-20.4
12	Canada	-17.6

Source: US Census Bureau, RongViet Securities

Assessment of the three-party relationship between South Korea – Vietnam – the US

There is no doubt that Vietnam has entered the global value-added chain. South Korean corporations play an important role in connecting Vietnam to the world. Vietnam's employees, whose salaries remain competitively low, have become the center of many South Korean employers' development plans to export goods to massive consumption markets such as the US and Europe.

South Korea's FDI in Vietnam reached USD 60 billion with over 6,700 projects in operation. For instance, Samsung's manufacturing and exporting expansion contributed to Vietnam's strong GDP growth in the last quarters of 2017.

Therefore, Vietnam is sensitive to changes in the bilateral relationship between South Korea and the US.

A WARNING POINT FOR VIETNAM: KORUS FTA RENEGOTIATION

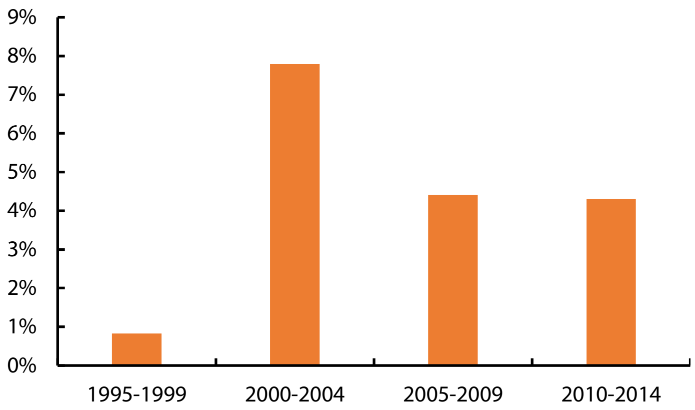
- KORUS FTA – The agreement
- The right time to re-negotiate the KORUS FTA
- A large trade decifit – The main argument of the White House
- Assessment of KORUS FTA renegotiation

KORUS FTA – The agreement

The US – South Korea Free Trade Agreement (KORUS FTA) was signed and entered effect on March 2012 in the context of slowing global trade following the Great Financial Crisis. South Korea's trade growth was only 4% on average during the 2010 – 2014 period, equivalent to the previous 5-year period. It is useful to explain why 10 out of 16 signed FTAs took place during that time.

Prior to the signed agreement in 2012, there was a US – Korea free trade regime between the two countries that was established in 2007. However, the 2012 agreement went deeper into subjects like security co-operation, sharing of technology and opening of the car market.

Figure 5: South Korea's Trade Growth



Source: Bloomberg, RongViet Securities

Figure 6: Number of FTAs signed by Asia countries

No.	Nation	FTA signed and under negotiation	FTA signed and effective
1	Singapore	35	20
2	India	29	13
3	China	28	17
4	Korea	26	16
5	Japan	23	15
6	Thailandd	23	13
7	Australia	23	12
8	Malaysia	23	14
9	New Zealand	20	11
10	Indonesia	18	9
11	Vietnam	17	10

Source: Bloomberg, RongViet Securities

The right time to re-negotiate KORUS FTA

However, there is an unexpected result for the US in that the trade deficit with South Korea doubled to USD 22.9 billion since 2012.

Historically the issue of "fair trade" was always a problem in prior negotiations with trading partners. Then President George W. Bush signed the KORUS FTA in 2007 but it was not implemented. As a result, Barack Obama required an official renegotiation of KORUS FTA three years later.

2007	2008	2010	2012	2017	2018
KORUS FTA was signed by George Bush but was not implemented	Barack Obama called for a renegotiation of the KORUS FTA	The KORUS FTA renegotiations started	The KORUS FTA's new version was signed	Donald Trump called for a renegotiation of the KORUS FTA	The first renegotiations started on Jan 2018

Meanwhile, protectionism globally is rising. Under the Trump administration, the US government is simultaneously re-negotiating three major free trade agreements, including KORUS FTA and NAFTA.

A huge trade deficit – The main argument of the White House

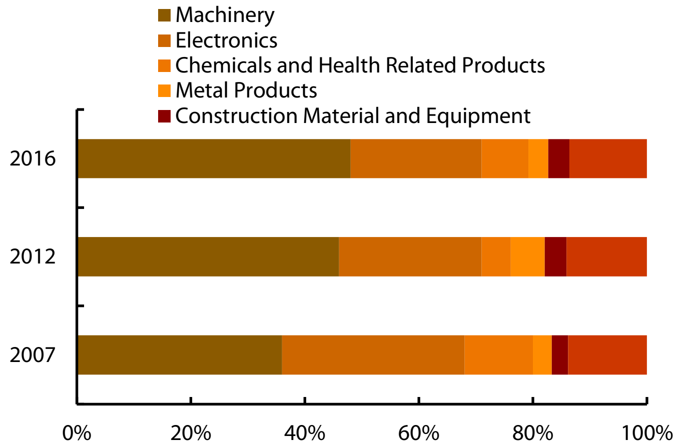
The trade deficit is one of the biggest motivations for the White House to pursue a renegotiation of the KORUS FTA. It nearly doubled to USD 23.7 billion over the period 2012 – 2016 compared with USD 12.1 billion in 2007 – 2011.

Notably, electrical appliances and machinery items are the top US imports from Korea. By 2016, the share of machinery and electronic equipment imports accounted for 48% and 23%, respectively.

Figure 7: US Trade Deficit with South Korea

Source: OEC, RongViet Securities

Figure 8: Goods Imported from South orea



Source: OEC, RongViet Securities

Key points for the increase in the US trade deficit:

South Korea implemented several non-tariff barriers. Notably, the emission standards and safety standards for imported cars. In details:

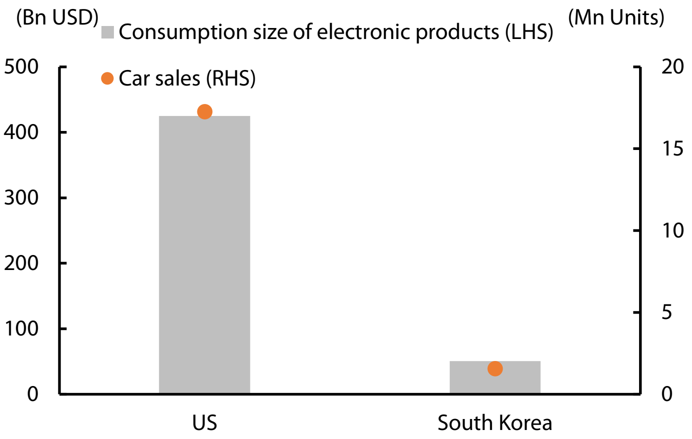
1) Emission standards: By 2015, South Korea's requirements for automobile manufacturers are greenhouse gas emissions of 140 grams per kilometer and fuel consumption of 17 kilometers per liter, equivalent to 40 miles / gallon. According to the US Environmental Agency (EPA), the record for US automobiles is 24.7 miles per gallon for 16MY and is expected to reach 25.2 miles per gallon for 17MY.

2) Safety standards and regulations for domestic industrial production: US automakers can export only 25,000 vehicles per year Korea and will cost USD 75 million if the US manufacturers want to change products to conform to South Korea's safety standards.

Meanwhile, the difference in market size is what we want to emphasize on. Looking at the auto market, sales in the US reached over 17 million units in 2017, which was 11 times more than the number of cars sold in the South Korean market. Similarly, sales of electronic products in the US market reached over USD 425 billion in 2017 compared with only USD 50.5 billion in South Korea.

Finally, the rise of South Korean manufacturers has been satisfying American consumers. According to Customer Reports, South Korea contributed 9 out of 10 best-selling TVs in the US with two big names, Samsung and LG. Meanwhile, car brands from Korea are also gaining credibility among the US users.

Figure 9: Market size



Source: RongViet Securities

Figure 10: 10 samples of TV satisfied American consumers

Rank	Companies	Products	Grade	Origin
1	LG	OLED55E6	84	Korea
2	LG	65EF9500	81	Korea
2	Samsung	65JS9500	81	Korea
4	LG	55EG9100	80	Korea
5	Sony	65X930C	79	Japan
6	LG	55EF9500	78	Korea
6	LG	55EG9600	78	Korea
6	Samsung	55KS8000	78	Korea
9	Samsung	65KS8500	77	Korea
10	Samsung	65JS900	76	Korea

Source: Consumer Reports, RongViet Securities

A warning point for Vietnam

We believe that the renegotiation of KORUS FTA highlights the rigid trade principles of the White House. The third renegotiations ended in mid-March when both of parties concentrated on cars and spare parts, steels imports from South Korea.

According to the US administration there are two critical points related to the KORUS FTA:

1. Improve US export opportunities and facilitate more balanced, two-way trade. The Administration is seeking a resolution of outstanding implementation issues and a rebalancing of commitments on tariffs for a ‘reciprocal and mutually advantageous agreement’.
2. The Administration’s objectives include eliminating non-tariff barriers to exports of US-made motor vehicles and motor vehicle parts.

Therefore, any changes in KORUS FTA as well as the trade policies are likely to affect strongly Vietnam.

IMPACT OF THE US TRADE POLICY ON VIETNAM

- Changes in Vietnam's foreign policy
- Investment flows into Vietnam
- Vietnam trade policy

Changes in Vietnam's foreign policy

Resuming the process of negotiating the Vietnam - US Framework Agreement on Trade and Investment (TIFA)

We argued that the renegotiation of KORUS FTA as well as NAFTA is a testament of what the White House is about. Withdrawing from the TPP has showed the preference for bilateral trade agreements. The Office of the US Trade Representative has confirmed its willingness to launch trade talks with Japan and four other countries in the Trans-Pacific Partnership on Transparent and Comprehensive Progress (CPTPP). It shows that Vietnam needs to change its foreign policies with the United States in the context of "trade wars". Therefore, coming back to the US-Vietnam Trade and Investment Framework Agreement (TIFA) is necessary when the US remains the partner that has a large trade deficit with Vietnam.

TIFA was signed in 2007 when both sides agreed to set up a bilateral cooperation council to facilitate cooperation on major policies. Moreover, recommendations of businesses from both sides were also considered.

TIFA is considered as an extension of the Vietnam-US Bilateral Trade Agreement (BTA) with the aim of promoting trade and investment between the two countries. Signing this agreement has marked a new milestone for bilateral cooperation between Vietnam and the United States. However, the negotiation process has been suspended since 2011 as Vietnamese leaders focused on pursuing the Transpacific Partner Agreement (TPP).

6/2007	11/2010	2011	01/2017	03/2017
TIFA was signed	Vietnam participated in TPP negotiations as a fully qualified member	TIFA enforcement was suspended	The US officially withdrew from the TPP	Vietnam and the US agreed to resume TIFA meetings

Promoting cooperation with strategic partners and the EU-Vietnam Free Trade Agreement (EVFTA) negotiation

Vietnam is trying to promote relations with strategic partners. According to an assessment by the World Bank, the economic benefits of Vietnam after joining CPTPP will come mainly from new markets such as Canada, Mexico, Australia, etc. Besides, we noted the efforts of Vietnamese diplomatic missions to resume negotiations of the EU-Vietnam Free Trade Agreement (EVFTA). In February, Prime Minister Nguyen Xuan Phuc signed Decision No. 213 / QD-TTg approving the project "Strengthening bilateral trade and investment cooperation between Vietnam and other strategic partner countries" to promote and diversify the export market of the country.

Table 2: Strategic partners of Vietnam

No.	Name	Year signed	No.	Name	Year signed
			7	Philippines	2015
1	Japan	2009	8	Australia	2018
2	South Korea	2009	9	Spain	2009
3	Thailand	2013	10	England	2010
4	Singapore	2013	11	France	2013
5	Indonesia	2013	12	Italy	2013
6	Malaysia	2015	13	Germany*	2011

Source: RongViet Securities

Note: On 22 September, Germany suspended its strategic partnership with Vietnam.

Over the last recent years, we have noted that Vietnamese diplomatic missions have been continuously dispatched to promote trade liberalization. It has been reflected in the schedule of meetings of Vietnam over 2017-2018.

1/2017	4/2017	5/2017	7/2017	8/2017	11/2017	3/2018
China	Hungary Sweden	The United States	German Netherlands	Thailand Indonesia	Singapore Philippines	India Australia*

Source: RongViet Securities

Note: On 15/09/2018, Vietnam and Australia formally signed a declaration establishing a strategic partnership

Investment flows into Vietnam

The US government is trying to attract foreign capital flows via measures to reduce corporate income tax, increased import tariffs, etc. These actions can cause corporations and investors to consider their investment plans in Vietnam. South Korean companies (42 of them) announced that they would invest a total of USD 17.3 billion into the US over the next four years.

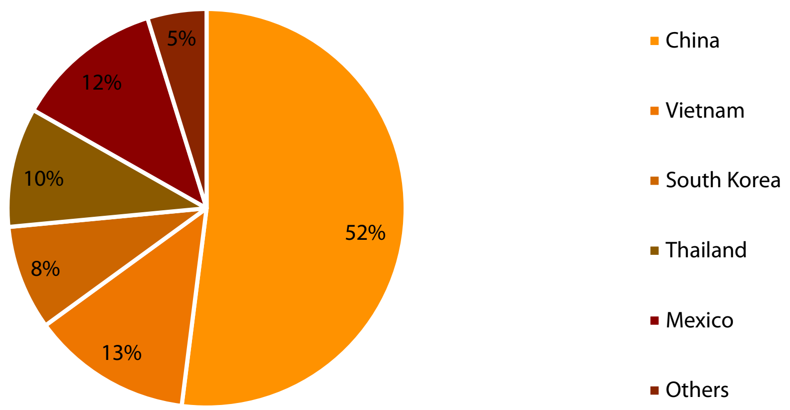
Table 3: Some Korean investment projects into the US (Bn USD)

Company	Investment (Bn USD)	Project	Location
Samsung Electronics Co.	1.9	Production of semiconductors Production of home appliances, including washing machines	Texas, South Carolina
Hyundai Motor Co. Kia Motors Corp.	3.1	Car manufacturing	Montgomery, Alabama Georgia
Lottle Chemical	3.1	Petrochemical facility	Louisiana
LG Electronics	0.3	Manufacture of washing machines	Tennessee

Source: RongViet Securities

In the above list, we emphasize the large corporations that have strong economic ties with Vietnam such as Samsung, LG or potential investors Hyundai Motor. Specifically, Samsung said it would spend USD 1.5 billion on a semiconductors factory in Texas. Samsung has never had a factory in the United States since the 1990s after shutting down a major TV factory. In addition, Samsung said it would invest USD 380 million to build a home appliance factory, including industrial washing machines, in Southern California. Currently, besides China, Vietnam is the second largest exporter of industrial washing machines to the United States, accounting for 13% of total import value of this item, equivalent to USD 180 million in 2016.

Figure 11: Industrial washing machine imported into the USD, capacity> 10 kg



Source: OEC, RongViet Securities

Meanwhile, Hyundai Motor and Kia, two potential investors in Vietnam, have announced that they would invest USD 3.1 billion to the US. Their investment capital will increase by 50% compared to the amount invested in the previous five years.

Outcome:

We believe that despite that investment flows will continue to pour into Vietnam.

1) The shift of investments from China to ASEAN countries

Vietnam and other ASEAN countries are gradually replacing China as the world factory because of the advantage of labor cost and important geopolitical issues. Besides the US market, commodities produced in Vietnam are also sent towards large markets such as China, ASEAN and Europe. In addition, policy changes in China made Korean food and retail businesses come to Vietnam. Notably, CJ Cheiljedang, a Korean food corporation, will invest KRW 70 billion to build a food processing plant in Ho Chi Minh City.

Table 4: Outstanding M&A deals in 2017 (Mn USD)

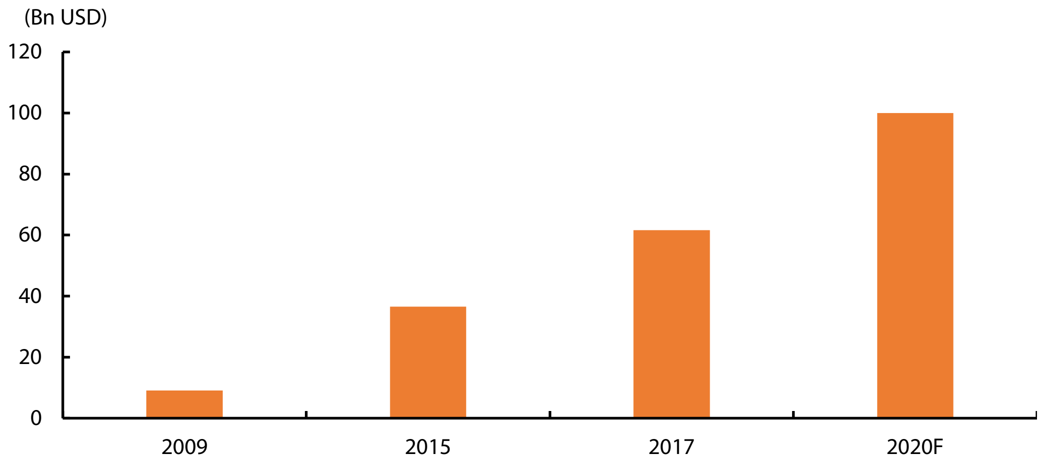
No.	Buyer	Seller	Ratio	Value	Sector
1	Daesang Corp – Korea	Duc Viet Food Joint Stock Company – Vietnam	100%	32	Food
2	Earth Chemical – Japan	A My Gia Joint Stock Company - Vietnam	100%	80	Chemistry
3	Shinhan Bank Viet Nam	Prudential Financial Limited Company	100%	151	Finance
4	SCG Joint Stock Company - Vietnam	Vietnam Construction Materials Joint Stock Company	100%	156	Construction Materials
5	Captial Land - Singapore	Twin Peak Development	100%	52	Real Estate

Source: MAF, RongViet Securities

2) Vietnam is the center of South Korea's "new south wind" policy

Undeniably, the bilateral relationship between Vietnam and Korea has been becoming closer day by day. The three-day visit of South Korean President Moon Jae-in in Vietnam once again reaffirmed the position of Vietnam as the center of South Korea's "new south wind" policy. Notably, the two countries agreed to promote two-way bilateral trade of USD 100 billion by 2020, higher by 62% compared to 2017 (USD 62 billion). It implies that two-way trade average growth will be 17% over the next three years. As mentioned in part 1, South Korea has surpassed China and became Vietnam's largest supplier.

Figure 12: Total trade value of Vietnam - Korea



Source: Customs. RongViet Securities

Particularly noteworthy are direct investment activities in the banking, finance, logistics, retail sectors as well as M&A deals.

According to Mobile World, 6 out of 10 Samsung products occupy the top spot in the top earning products. South Korean subsidies are continuing to expand their operations in Vietnam.

In addition, a typical M&A deal is Samsung SDS and logistics services firm, Minh Phuong logistics group in order to develope supply chain of Samsung and expand further to the logistics market with a size of USD 22 billion per year in Vietnam. Previously, this company also established a joint venture with Air Logistics Joint Stock Company (ALS) to manage the cargo terminal at Noi Bai airport.

After huge investments from Chaebol such as Samsung. LG. ... we expect the satellite enterprises of these groups will continue to invest and expand their production in Vietnam. Although there are many views that the appearance of Korean satellite businesses will directly compete with Vietnamese supporting industries. However, we think it is also an opportunity for Vietnam to upgrade our technology and management experience.

Table 5: Korean manufacturers invested in Vietnam as Samsung suppliers (Mn USD)

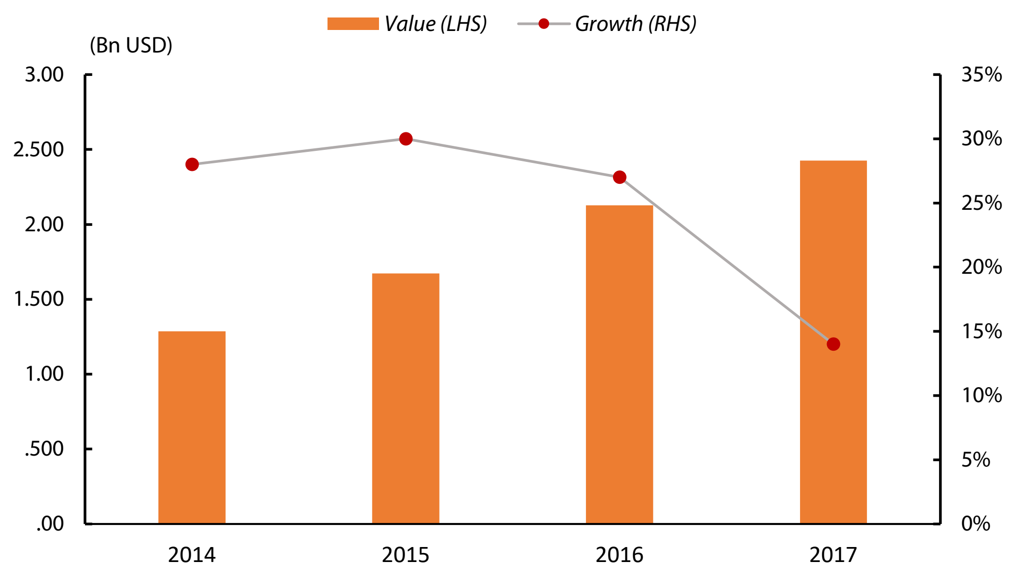
No.	Project	Location	Activities	Investment
1	Young Sung Precision	Bac Giang	Manufacturing and processing mobile phone covers, electronic components	0.4
2	Hamiflexible Vina	Hai Phong	Production of electronic components for household products	5
3	Heasung Vina	Vinh Phuc	Cameras for mobile phones	72
4	Haehwa	Phu Tho	Cameras for mobile phones	4
5	New - Hanam	Ho Chi Minh city	Washing machine motors, refrigerators, air conditioners and vacuum cleaners	74
6	INTOPS	Ho Chi Minh city	Production of electronic components and information technology	80

Source: RongViet Securities

Vietnam's foreign trade

We argue that protectionism will negatively affect the foreign trade of Vietnam. The most typical example is the US tariffs on washing machines. Specifically, the US will levy a 20% tax on 1.2 million large household washing machines and a 50% tax on products surpassing the upper limit (in terms of size). By the third year, the tax rates will be 16% and 40%.

Figure 13: Vietnam's exports of machinery, equipment, tools and spare parts to the US



Source: OEC, RongViet Securities

Meanwhile, Samsung Electronics and LG Electronics, who account for more than 25% of total washing machine exported to the US in 2017, are bigplayers in Vietnam and affected by the US tax policy. These two companies have already invested in two large home appliances manufacturing plants, including washing machines, in Vietnam such as Samsung's CE Complex (Ho Chi Minh City) and LG Electronics (Hai Phong). The export growth rate of machinery, equipment and parts was 14% in 2017, which is the lowest level in recent years.

Meanwhile, in the case of solar panels, the first-year tax rate is 30% and down to 15% from the fourth year onwards. According to the International Trade Commission, Vietnam provided 9% of solar panels to the US market last year. Recently, First Solar confirmed that it would restart its investments in Vietnam and raise to USD 830 million. The project has been revived after being delayed since 2011 due to supply-demand imbalances of solar panels.

Opinion:

In general, we cannot deny the growing trade tensions. After President Trump signed the decision to levy taxes on Chinese goods, China immediately imposed a tariff on USD 3 billion on products imported from the United States. Boeing and soybean are the two most obvious targets. However, we think that trade barriers are likely more politically motivated than anything else. The main purpose is to create advantages in bilateral trade negotiations between the United States and other countries.

Regarding recent tariffs, Trump seemed to choose the safest solution with an estimated impact of USD 9 billion on a 25% tax on steel and 10% on aluminum among three options proposed by US Commerce Secretary Wilbur Ross. Major trade partners such as Argentina, Australia, Brazil, South Korea, Canada, Mexico and EU are temporarily exempted until May 2018 before they will renegotiate to decide on long-term exemption.

Table 6: Proposed taxes on steel and aluminum

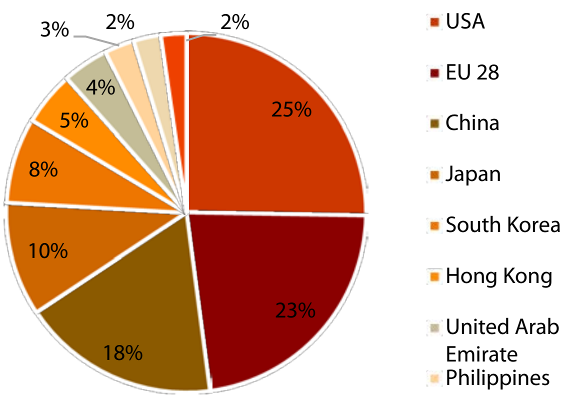
No.	Three Options Proposed by US Commerce Secretary, Wilbur Ross
1	24% and 8% tariffs on all steel and aluminum imports
2	53% tariff on steel imports from 12 countries, including Brazil, China and Russia. 24% tariff on aluminum imports from China, Hong Kong, Russia, Venezuela and Vietnam.
3	Set quotas for imports of aluminum and steel from all countries. Specifically, the quotas for steel and aluminum respectively were 63% and 86.7% of imports last year.

Source: RongViet Securities

We believe that Vietnam's trade growth prospects are very bright. The country has free trade agreements with most of ASEAN and Northeast Asia. Recently, EVFTA has been restarted after more than a year of delay. It is expected that EVFTA will be signed by the end of 2018. We emphasize that the EU 28 is the second largest export market for Vietnamese products. To speed up the negotiation and signing of EVFTA, we note some key points. including:

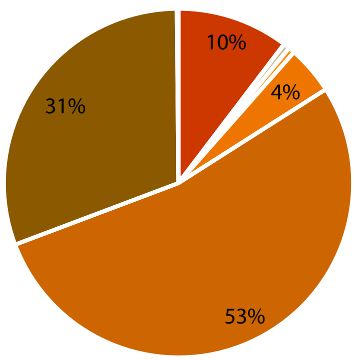
- The EVFTA is split into two separate ones: the Free Trade Agreement and the Investment Protection (IP) Agreement.
- In May, the EU will evaluate Vietnam's efforts to improve the legal framework and combat illegal fishing before removing sanctions put on Vietnam's seafood exports.

Figure 14: Major importers from Vietnam



Source: Eurostat, RongViet Securities

Figure 15: EU-Vietnam trade according to SITC classification



Source: Eurostat, RongViet Securities

Table 7: Table SITC for Figure 15

Item	Color	Label	Item	Color	Label
			S5		Chemicals and related products
S0		Food and live animals (10%)	S6		Produced goods are classified by materials
S1		Drinks and cigarettes (4%)	S7		Machinery and equipment transport (53%)
S2		Raw materials, except crude oil	S8		Mixed products (31%)
S3		Mineral materials, lubricants and related products	S9		Commodities
S4		Animal and vegetable oils, fats and beeswax	Others		Others

ANALYSIS & INVESTMENT ADVISORY DEPARTMENT

Bernard Lapointe
Head of Research
bernard.lapointe@vdsc.com.vn
+ 84 28 62992006 (1525)

Lam Nguyen
Senior Strategist
lam.ntp@vdsc.com.vn
+ 84 28 6299 2006 (1313)
- Banking
- Conglomerates

Thien Bui
Senior Analyst
thien.bv@vdsc.com.vn
+ 84 28 6299 2006 (1321)
- Market Strategy
- Financial Services
- Personal Goods

Hieu Nguyen
Senior Analyst
hieu.nd@vdsc.com.vn
+ 84 28 6299 2006 (1514)
- Market Strategy
- Pharmaceuticals
- Aviation

Duong Lai
Senior Analyst
duong.ld@vdsc.com.vn
+ 84 28 6299 2006 (1522)
- Real Estate
- Building Materials

Vu Tran
Senior Analyst
vu.thx@vdsc.com.vn
+ 84 28 6299 2006 (1518)
- Oil & Gas
- Food & Beverage

Trinh Nguyen
Analyst
trinh.nh@vdsc.com.vn
+ 84 28 6299 2006 (1331)
- Steel
- Construction
- Technology

Quang Vo
Analyst
quang.vv@vdsc.com.vn
+ 84 28 6299 2006 (1517)
- Market Strategy
- Basic Materials
- Personal Goods

Son Phan
Analyst
son.pnt@vdsc.com.vn
+ 84 28 6299 2006 (1519)
- Utilities
- Natural Rubber

Tu Vu
Analyst
tu.va@vdsc.com.vn
+ 84 28 6299 2006 (1511)
- Macroeconomics

Son Tran
Analyst
son.tt@vdsc.com.vn
+ 84 28 6299 2006 (1527)
- Market Strategy
- Retails
- Consumer chemicals

Thuy Nguyen
Analyst
thuy.nb@vdsc.com.vn
+ 84 28 6299 2006 (1528)
- Macroeconomics

Tung Do
Analyst
tung.dt@vdsc.com.vn
+ 84 28 6299 2006 (1521)
- Logistics
- Aviation

Thu Pham
Analyst
thu.pa@vdsc.com.vn
+ 84 28 6299 2006 (1520)
- Industrial Real Estate

Thao Dang
Analyst
thao.dtp@vdsc.com.vn
+ 84 28 6299 2006 (1529)
- Food & Beverage

Tam Pham
Analyst
tam.ptt@vdsc.com.vn
+ 84 28 6299 2006 (1530)
- Fishery

Ha Tran
Assistant
ha.ttn@vdsc.com.vn
+ 84 28 6299 2006 (1526)

RONG VIET SECURITIES CORPORATION

Floor 1-2-3-4, Viet Dragon Tower,

141 Nguyen Du St. - Dist 1 – HCMC

Tel: (84 28) 6299 2006

Fax: (84 28) 6291 7986

Email: info@vdsc.com.vn

Website: www.vdsc.com.vn

Hanoi Branch

2C Thai Phien St., Hai Ba Trung Dist, Hanoi

Tel: (84 24) 6288 2006

Fax: (84 24) 6288 2008

Can Tho Branch

95-97-99 Vo Van Tan – Ninh Kieu - Can Tho

Tel: (84 292) 381 7578

Fax: (84 292) 381 8387

Nha Trang Branch

50Bis Yersin St, Nha Trang

Tel: (84 258) 382 0006

Fax: (84 258) 382 0008

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