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Macro Report

VIETNAM's ECONOMY IN 2M2023: GLOOMY BUT THINGS WILL BE BETTER

- *The industrial sector declined in 2M23 but is expected to recover in the following months.*
- *Retail sales slowed down while inflation cooled down.*
- *Corporate bonds: Risks rising but are anticipated.*

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VIETNAM ECONOMY

- Vietnam's economy in 2M2023: Gloomy but things will be better
- The industrial sector declined in 2M23 but is expected to recover in the following months
- Retail sales slowed down while inflation cooled down
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VIETNAM's ECONOMY IN 2M2023: GLOOMY BUT THINGS WILL BE BETTER

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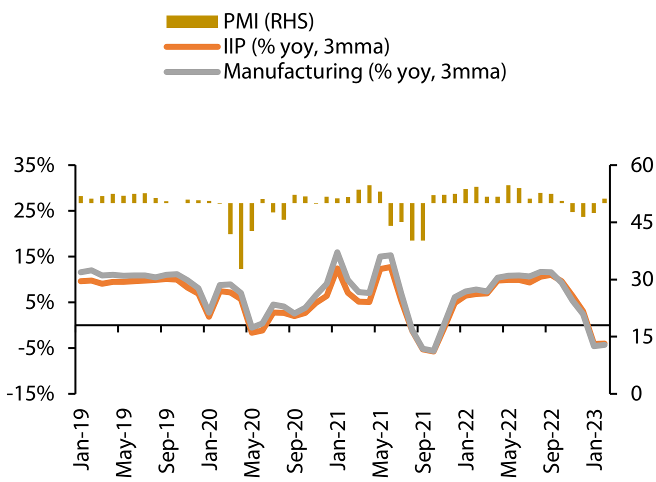
The industrial sector declined in 2M23 but is expected to recover in the following months

According to GSO data, industrial production in Feb was still quite gloomy, with the industrial production index increasing only 3.6% y/y. The industrial production index in Jan adjusted from minus 8% to minus 14.9%. Notably, production activities in the processing and manufacturing industry increased by 3.3% over the same period. In 2M23, industrial production recorded a decrease of 6.3% y/y, marking the first two months period with negative growth during the decade of 2013-23. Most industries had negative changes in the first two months of the year. The ones with substantial declines included textiles and garments, steel, telephones but in contrast, production of petroleum and beer increased sharply compared to the same period in 2022.

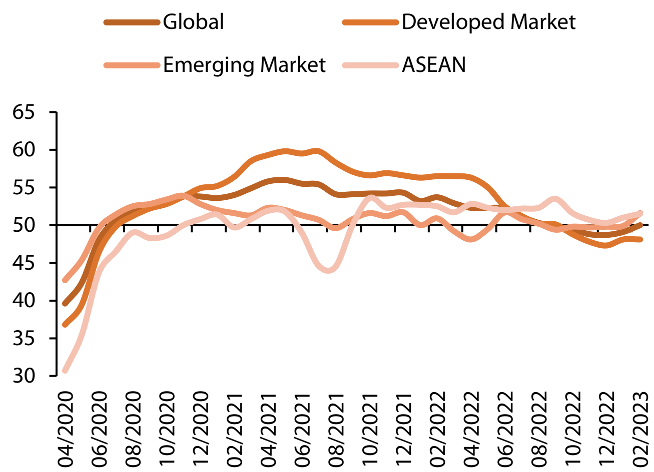
The PMI of Feb 2023 showed that the outlook of industrial production could be positive in the coming months as orders have increased for the first time after four months of decline. Notably, the increase in new orders was the strongest since Aug 2022, and export orders continued to improve for the second consecutive month, showing that global demand for exports is recovering. At the same time, output increased slightly with the focus on investment goods such as machinery and equipment, spare parts, etc. Accordingly, the PMI recovered to 51.2 points from 47.4 points in Jan 2023. The recovery of Vietnam's PMI is also in line with the global PMI, which recovered from 49.1 points in Jan to 50 points in Feb, thanks to China's reopening (per S&P Global). In Feb 2023, China's manufacturing PMI rose to 51.6 points, the highest level since Jun 2022. Nevertheless, it is worth mentioning that the acceleration of China's manufacturing may put more pressure on Vietnam's exports. In Feb 2023, China's New Orders PMI accelerated to 54.1 points, the highest level since September 2017, while export orders reached 52.4 points, the highest level since Mar 2011.

Figure 1: Industrial production index and PMI



Source: GSO, RongViet Securities

Figure 2: Global PMI



Source: Bloomberg, RongViet Securities

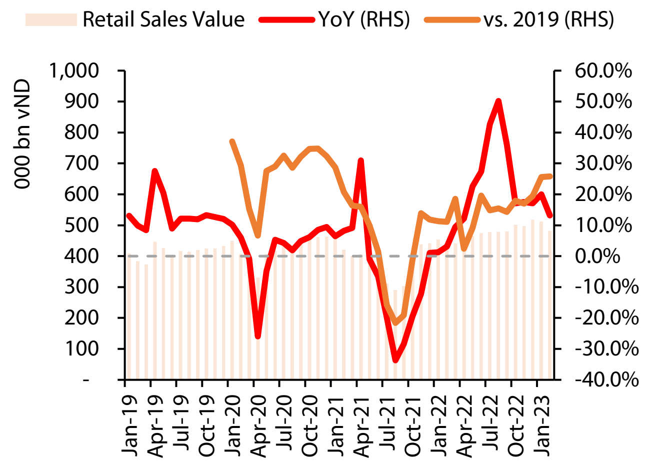
Retail sales slowed down while inflation cooled down

Retail sales of goods and services in Feb 2023 decreased after the Tet holiday's effect, decreasing 6.0% mom, of which retail sales of goods decreased by 6.7%, and retail sales of services were down by 3.3%. Year-on-year, retail sales of goods and services still grew by 13.2%, but this growth was significantly lower than the 20% increase in Jan. This showed that Vietnam's consumption growth rapidly decreased from the peak to average growth when the low-base effect caused by Covid-19 disappeared. After excluding the price factor, retail sales growth is estimated at 9.2% in the first two months, significantly higher than the negative growth of 1.1% in the same period in 2022. Based on this figure, we believe that the domestic consumption sector will still drive GDP growth in the first quarter of 2023.

Regarding product groups, the growth in retail sales of tourism, catering and accommodation services increased the highest, at 124.4% and 31.6%, respectively, over the same period in the first two months of 2023. The third highest growth rate is the textile and garment group, up 18.4% over the same period. Retail sales of food increased by 12.5%, while retail sales of durable goods such as household goods or vehicles grew relatively low, at 4.0% and 3.4%, respectively. International visitors to Vietnam in Feb increased by 7.1% over the previous month, in which visitors from China significantly recovered, 3.5 times higher than in Jan.

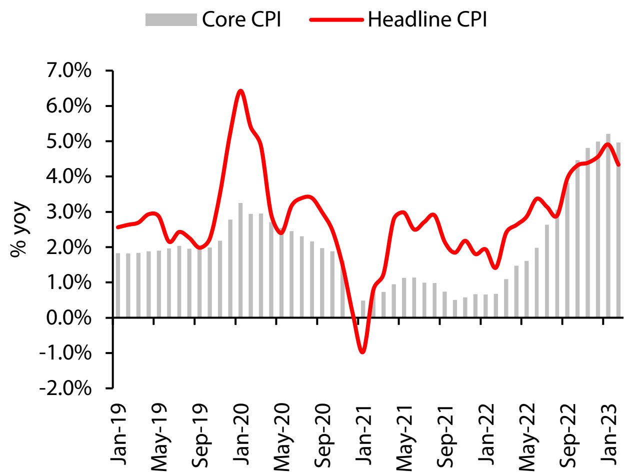
The consumer price index in Feb 2023 showed that Vietnam's inflation may have peaked and will cool down in the following months due to a moderate increase in global commodity prices and the upcoming electricity price increase. The general inflation index increased by 0.45% mom with two main contributors to the CPI: housing & building materials (+1.8% mom) and transportation (+2.1% mom). On the contrary, prices of many consumer goods cooled down after Tet, such as food (-0.17%), beverages (-0.12%) and textiles (-0.08%). Regarding the adjustment of electricity prices, EVN has calculated that if the profit margin of 3% and exchange rate differences in 2019-22 are fully calculated, the electricity price may increase by 15.9-20.3% to 2,162-2,243 VND/kWh. If it is allowed to include the loss in 2022, the average retail price of electricity could increase by 26.2% to 2,357 VND/kWh. Previously, on Feb 3, 2023, the Government announced a new electricity price bracket with a minimum of 1,826.22 VND and a maximum of 2,444.09 VND/kWh, up 13.7% and 28.2%, respectively, compared to the old electricity price bracket. The current average retail price of electricity is 1,864 VND/kWh, only 2.1% higher than the minimum level of the new price bracket. EVN's calculations showed that the pressure to increase electricity prices is relatively high, and the new price bracket is also a premise for the increase in electricity prices. According to Decision 24/2017/QD-TTg on the mechanism to adjust the average retail price of electricity, we expect that there could be a roadmap to adjust the electricity price, the first increase can be from 5-8%, and the adjustment period will be at least six months.

Figure 3: Vietnam's retail sales



Source: GSO, RongViet Securities

Figure 4: Vietnam's inflation



Source: GSO, RongViet Securities

Corporate bonds: risks rising but are anticipated

As we mentioned in our Analyst Pinboard dated 27/02/2023, the SBV withdrew a large amount of money from the banking system last month, approximately VND198 trillion. Of which, about VND83.2 trillion of SBV bills have a term of 91 days, meaning a large amount of money has been withdrawn from the banking system and is expected to be pumped back in the second half of May 2023. The SBV's supply management in the past month stemmed from several reasons, including 1) low credit growth at the beginning of the year, 2) a sharp drop in overnight interbank lending rates and 3) the SBV's regulation to respond to the Fed's interest rate hikes, and likely due to 4) a preparation to deal with the pressure of maturing corporate bonds from the end of May 2023.

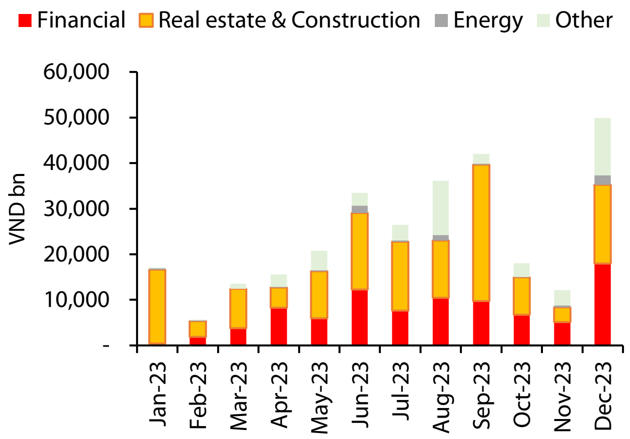
According to our estimates, the size of maturing corporate bonds in 2023 is estimated at VND290 trillion, and debt repayment pressure will fall in May-Sep 2023 and Dec 2023. Particularly for the real estate and construction sectors, the size of corporate bonds maturing in 2023 is about VND145 trillion, of which the debt repayment pressure is about VND85 trillion during the peak period from May-Sep 2023. In the first two months of 2023, the issuance of corporate bonds was quite bleak, with only Son Kim Land and Phan Vu Investment JSC being two successful issuers with a total issuance value of VND500 billion and VND110 billion, respectively, with interest rates of 13.5%/year and 10.5%/year, respectively.

The scale of early redemption of corporate bonds in the first two months of the year was about VND15 trillion, up about 56% over the same period. However, the early redemption of corporate bonds has slowed down somewhat compared to the second half of 2022. The total value of corporate bonds bought back before maturity from the beginning of 2022 to now is VND235 trillion, of which 48% was in the financial group (banking, securities, financial services, ~VND112 trillion dong) and 30% belongs to the real estate and construction group (~VND70 trillion).

The default risk of corporate bonds has become more evident in recent times. In the first two months of 2023, about VND22.8 trillion of corporate bonds matured. However, statistics of HNX show that there are about 13 enterprises that are late in paying bond principal and interest with an issued size of nearly VND3.8 trillion. Accumulated from Sep 2022, more than 60 enterprises announced late payment of interest and bond principal, mainly focusing on real estate and construction businesses. Since the financial capacity and business situation of the Real estate & Construction group has not improved, the problem of violations in debt repayment obligations to bondholders will likely increase soon. However, the default risk is expected to be concentrated in the real estate and construction sectors.

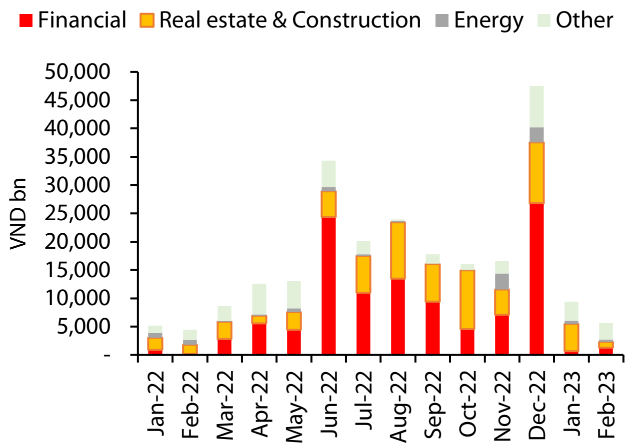
In sum, the problem of the corporate bond market for investors is no longer new. We believe that more issuers could not fulfil their obligations to bondholders is a predictable development. In addition, although the problematic nature of the corporate bond market has yet to be removed, we expect that this risk will not be exaggerated as businesses have solutions to negotiate and arrange with bondholders after Decree 65 was amended. Additionally, the size of maturing corporate bonds has decreased thanks to early bond redemption activities, and the risk of insolvency is at a predictable level. The size of maturing corporate bonds of real estate & construction groups accounted for about 1.2% of the credit of the whole system. The risk of insolvency spreading to bank loans of real estate & construction enterprises and other fields is also a matter of concern. However, the probability and impact of these risks are not clear at the moment.

Figure 5: Breakdown of maturing corporate bonds



Source: VBMA, RongViet Securities

Figure 6: Breakdown of early redemption corporate bonds

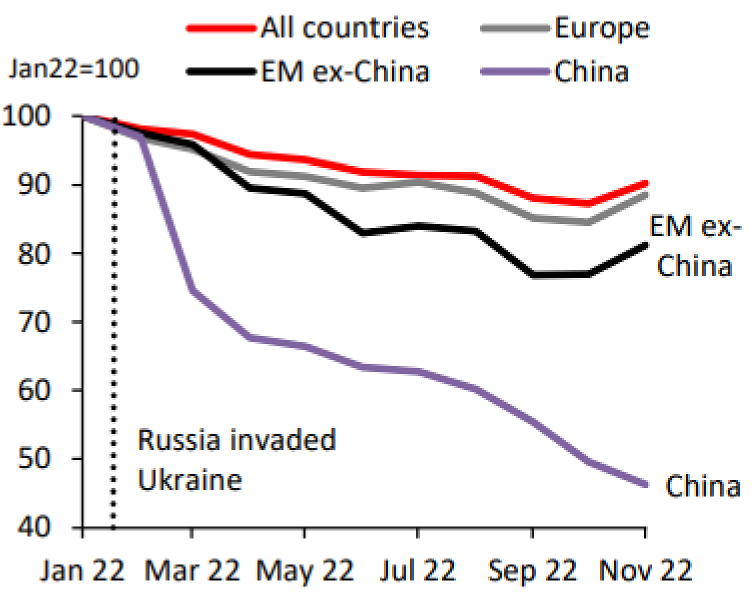


Source: HNX, RongViet Securities

Global bonds

Post Russia's invasion of Ukraine, US investors' holdings of China bonds have shown a rapid decline (Figure 1). The reduction in US investors' Renminbi (RMB) bond holdings is proportionally much larger than reductions of EM and European bond holdings. This suggests that RMB bond outflows are not just impacted by market risk, commodity supply chain risk or yields, but they have become susceptible to political risk.

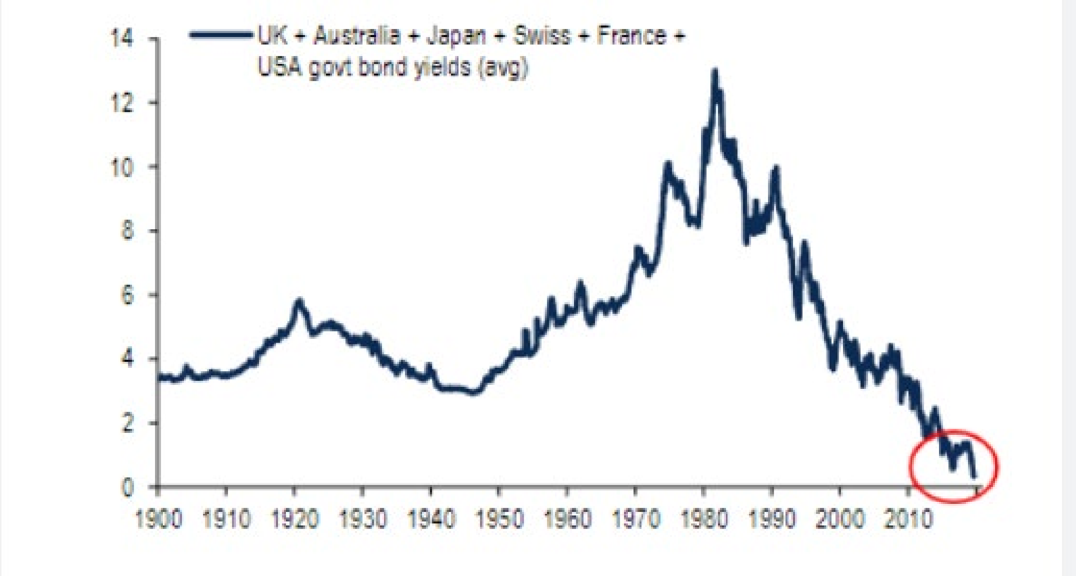
Figure 7: US investors' holdings of foreign bonds (Jan 2022= 100, USD)



Source: CEIC, DBS

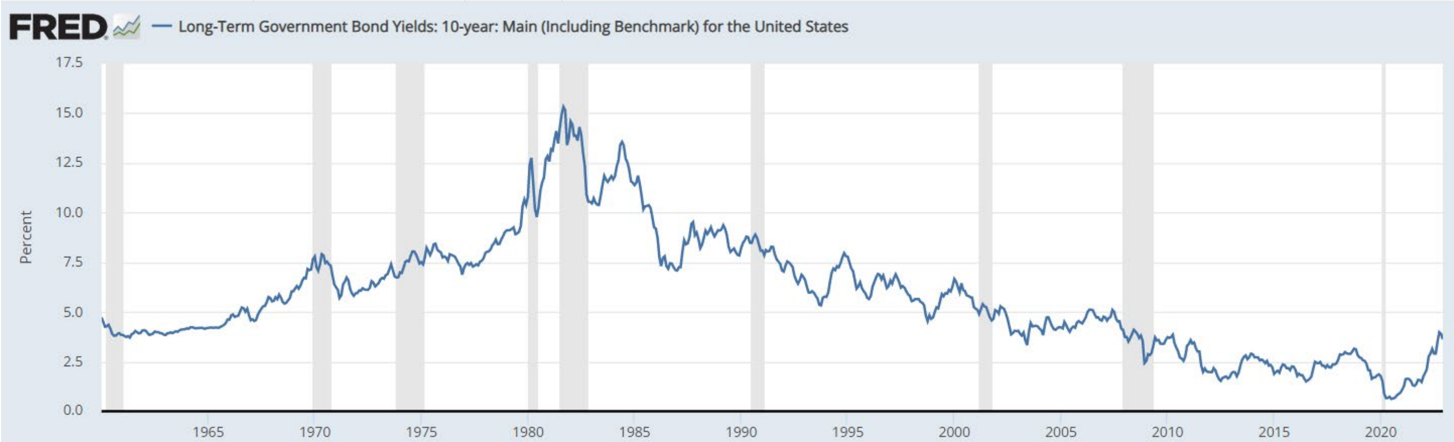
Recently, global bond yields have decreased but have probably bottomed out (Figures 2 & 3).

Figure 8: Global bond yields, %



Source: BofA Merrill Lynch Global Investment Strategy, Bloomberg, Global Financial Data

Figure 9: US 10-year bond yields, %



Source: Federal Reserve Bank of St. Louis

Bond yields are suddenly big news again. Because bonds are generally less well understood by investors than stocks, many people don’t know whether this is a good or bad thing.

On the surface, rising yields sound positive in that holders of bonds get paid more. But in an era of soaring inflation and economic turbulence, nothing is quite what it seems.

A stock’s yield is a function of the price and moves in opposite directions – a falling share price will push the yield higher and vice versa. And it’s the same with bonds, where yields and prices move around hourly and daily.

The "fixed" part of "fixed income" refers to the coupon and not the yield – if I buy a government bond with a five-year maturity, I will get the same amount of money back as income over that period, but the price and the yield of that bond will fluctuate over those five years. I will, of course, receive my original investment back if I hold it for five years. And that’s a big appeal for bond investors over shares, where capital security is by no means guaranteed.

Should I Buy Bonds Now?

There’s a big "if" implied in buying bonds, though. Issuers, whether governments (local/national) or companies, need to stay in business or not default on their debt to keep paying investors income. There’s a world of difference between buying a bond issued by the Switzerland government, which has the highest "AAA" credit rating from S&P, and, say, a new technology company trying to raise money.

Whichever entity sells you the bond wants to keep paying you back but may not be able to because it runs into financial trouble. This is less likely for sovereign governments, especially ones that control their own currencies, but it does happen, especially in emerging markets.

At the time of writing, Switzerland’s 10-year bond yields 1.29% but Brazil’s yields 12%. The market’s not saying that Brazil is about to default on its debt, but that this is more likely than Switzerland doing so (the yield difference also takes into account interest rates and inflation, of which more later).

The Eurozone debt crisis may be a distant memory for many investors, but it provided a textbook case of high yields flagging up risk. Greek debt yielded nearly 30% at one point – and the country did default on its debt, going to the International Monetary Fund for a bailout. (Greece’s 10-year bond currently yields around 4.75%). Investors at that yield will either have been very brave or very foolish.

As well as compensating investors for the higher risks, high yields can flag up a big case of buyer beware. That’s definitely the case in the corporate bond market, where companies with worse credit ratings (issuing “junk bonds”) need to offer higher yields to tempt investors to take on the higher risk. In good economic conditions, defaults are generally low, and markets can overprice risk, to the benefit of yield hunters.

Yields go up because investors sell bonds, pushing down their prices. That can highlight a loss of confidence in the issuer's economic or corporate strategy.

As well as risk, government bond yields also tell us about inflation and interest rate expectations. We are now living in a high-inflation era. Interest rates have been rising sharply, particularly in the US, where the Federal Reserve has been hiking aggressively.

In economic history, periods of rising inflation are expected to be bad for bonds: new issues of debt have to offer higher yields to compete with other "risk-free" assets like cash. And rising interest rates mean bond yields can look uncompetitive very quickly.

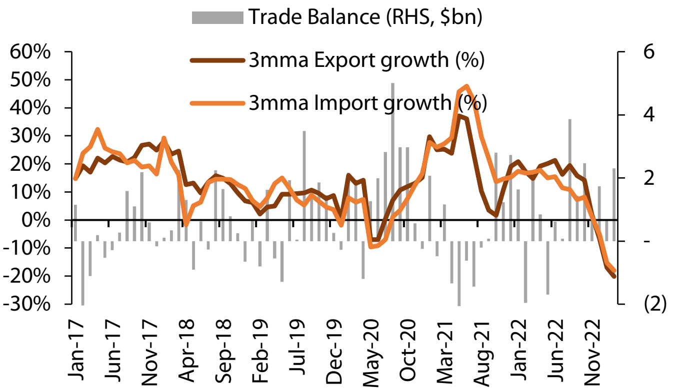
Where does this leave investors, savers and mortgage holders? Clearly, we have ve moved away from the unusual era when investors were effectively paying governments to own their bonds. German and Japanese debt offered negative interest rates at one point. That period was not a great one to be a new bond buyer. Prices were elevated and yields were low.

Because of their predictable cash flows and lower risk profile – especially for the likes of Switzerland – they are meant to offer some element of safety in volatile times.

In the March 2020 Covid-19 crash, these bonds were in high demand as "safe havens". Investors were willing to overlook the tiny or negative yield just to own a more secure asset. In that case yields were a very secondary consideration to the investment proposition – investors bought bonds despite the yields rather than because of them.

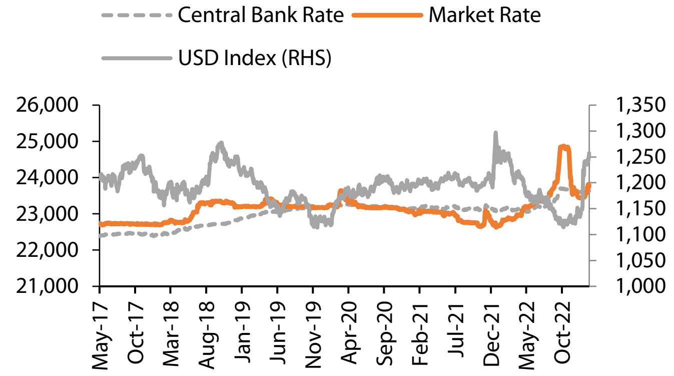
VIETNAM ECONOMIC INDICATORS IN FEB 2023

Trade balance



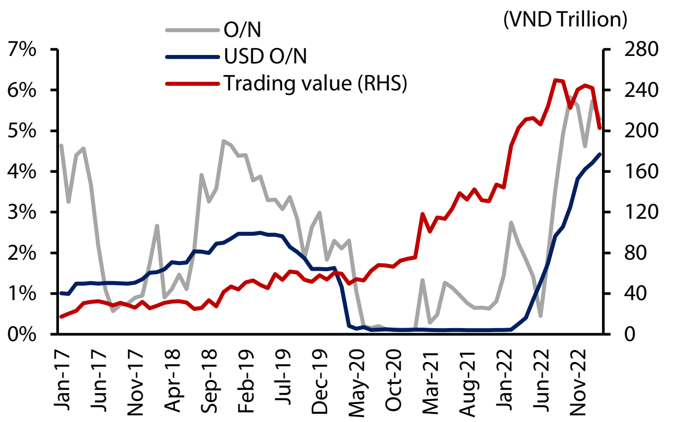
Source: GSO, RongViet Securities

USDVND exchange rate



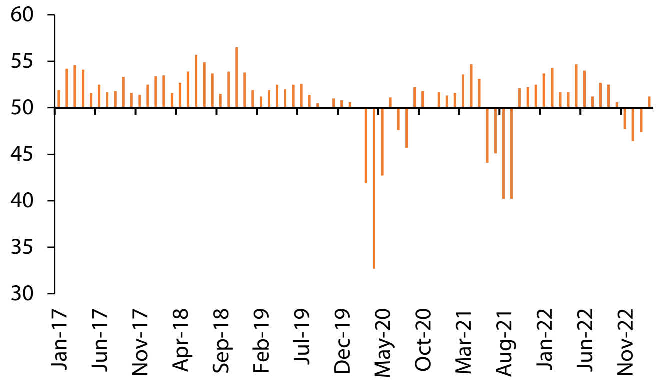
Source: SBV, Bloomberg, RongViet Securities

Interbank interest rate (%/year)



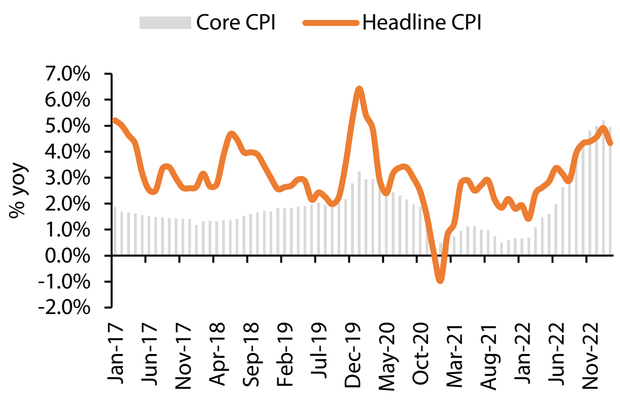
Source: SBV, RongViet Securities

Vietnam PMI



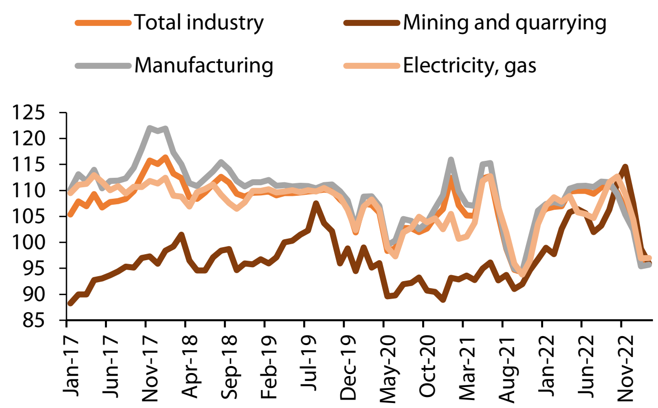
Source: IHS Markit, RongViet Securities

Vietnam CPI



Source: GSO, RongViet Securities

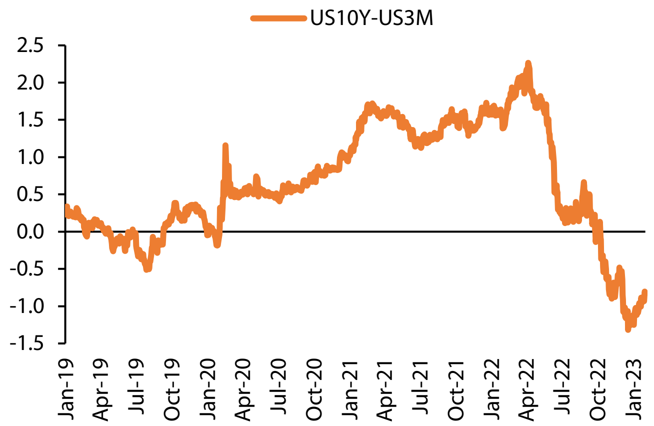
3-month MA Industrial Production Indices



Source: GSO, RongViet Securities

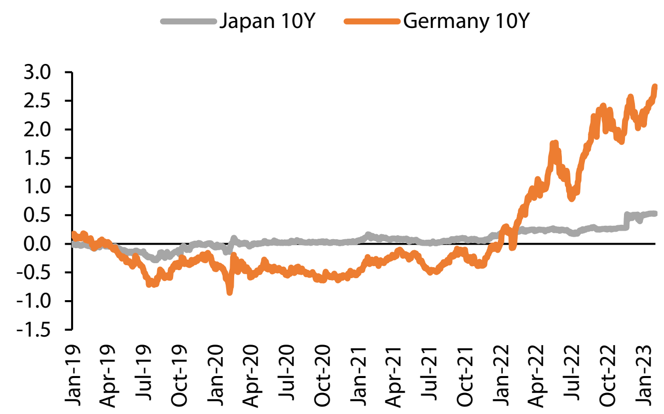
GLOBAL ECONOMIC INDICATORS IN FEBRUARY

US G-Bond yields gap (%/year)



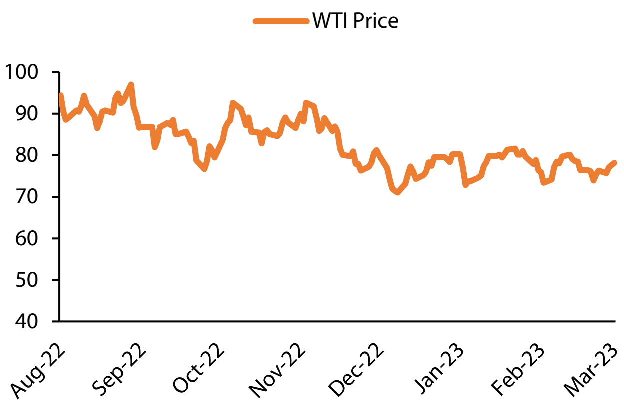
Source: Bloomberg, RongViet Securities

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



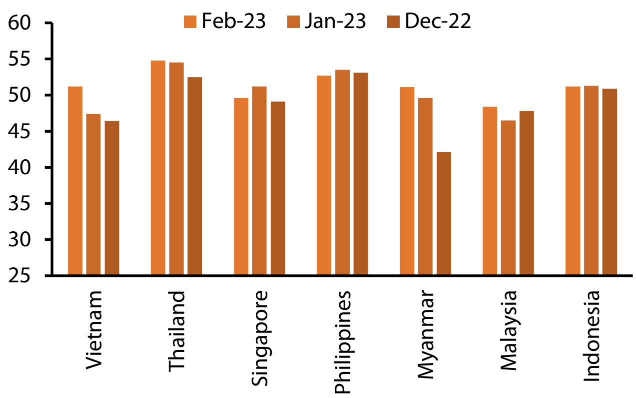
Source: Bloomberg, RongViet Securities

WTI crude oil price (USD/barrel)



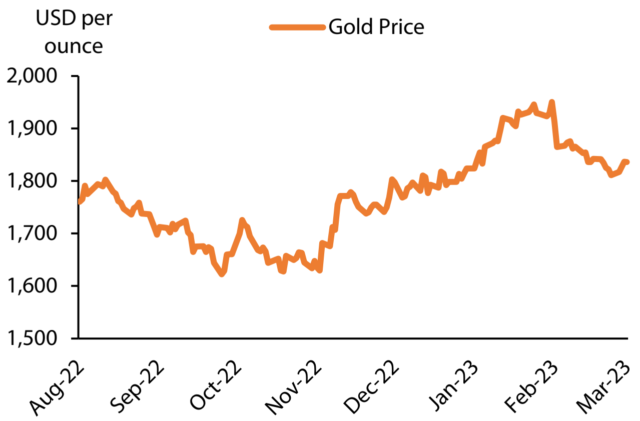
Source: Bloomberg, RongViet Securities

ASEAN's PMI



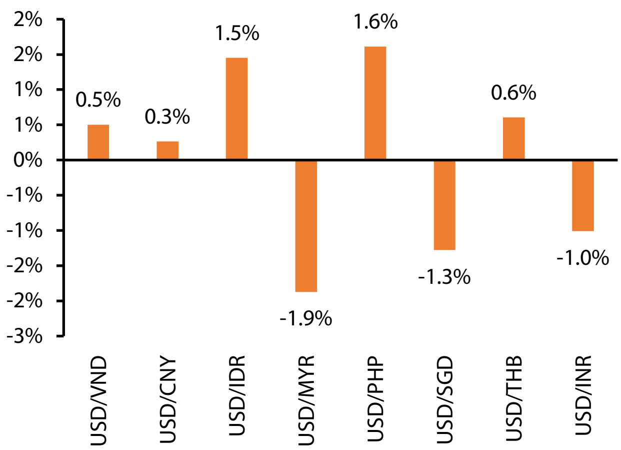
Source: Markit Economics, RongViet Securities

Gold prices (US$/ounce)



Source: Bloomberg, RongViet Securities

FX rates (%, YTD)



Source: Bloomberg, RongViet Securities

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