**ECONOMIST’S NOTE** **November 10, 2023** **VinaCapital**

**Michael Kokalari, CFA** Chief Economist  
 **Linh Vu** Head of Research

### **THE VN-INDEX’S RECENT 16% CORRECTION**

The VN-Index sold off by 16% from mid-September until end-October, before recovering somewhat since the end of last week, despite the fact that the country’s economy is now recovering from its slowdown at the beginning of this year. The sell-off was driven by three key factors:

1. The **depreciation of the VN Dong**, which prompted concerns that the State Bank of Vietnam (SBV) would significantly tighten monetary policy, and also prompted some selling by foreign investors.
2. The announcement of **Vingroup’s USD250m convertible bond**, which is exchangeable into Vinhomes shares, and which is discussed below (VIC and VHM account for about 10% of the VN-Index).
3. **Margin calls** by local securities companies, plus rumors of a clampdown on certain unofficial sources of margin lending that appear to have prompted an unwinding of highly leveraged speculative positions on October 17th.

In addition to the three Vietnam-specific factors outlined above, the 60 bp increase in 10Y US Treasury yields from mid-September to end-October plus geopolitical issues also weighed on emerging market stock markets, with the MSCI-EM Index falling 5% from mid-September to end-October. However, the VNI significantly underperformed its regional EM peers as can be seen below, making it clear that concerns about the SBV and VIC/VHM drove the sell-off. Additionally, Q3 earnings have generally been lackluster, which also weighed on investor sentiment to some extent.

### **Charts**

**Left: The VN-Index has lost most its gains YTD** Chart of VN-Index with callouts:

* Sep 25: SBV tightens monetary policy in response to 3% VNĐ depreciation
* Oct 4: Apparent acceleration of stock margin liquidation
* Oct 16: Vingroup CB/VIC issue

**Right: VN-Index Underperformed Regional EM Peers Since Mid-Sep** Line graph comparing:

* VN-Index (declined more)
* EM Peers (THA, PHI, PDR, MYM)

Finally, further to #1 above, the circa 4% YTD depreciation in the value of the VN Dong as of end-October was driven by a 6–7% increase in the US Dollar/DXY index from mid-July to early-October, coupled with the fact that the SBV’s aggressive rate cuts in H1 left short-term interest rates in Vietnam a record 500bps below short-term USD interest rates. The USD-VND exchange rate depreciated by 0.7% on August 15th, which was its biggest daily depreciation in nearly one year; this ultimately prompted the SBV to modestly tighten monetary policy. Note that the SBV typically

(*Text cuts off at page bottom*)

Acts to prevent annual depreciations in the value of Vietnam’s currency by more than 3%, and it had depreciated by about 3% in late-September.

Specifically, the SBV drained nearly **USD9 billion worth of VN Dong** from the country’s money market from **September 21st until end-October**, but it **did not hike policy interest rates** to protect the currency – in contrast to the recent, unexpected policy rate hikes in the Philippines and Indonesia (although the currencies of Vietnam’s regional peers depreciated by about 2%pts more than the VND did from mid-September to end-October). The possibility that the SBV would significantly tighten monetary policy – or even hike policy rates – was probably the biggest factor weighing on the stock market during the correction because the **fall in deposit rates** was one of the main drivers of the increase in the market earlier this year, prompting investors to channel maturing 6-month deposits into the stock market, which we discussed in this report. In addition, **VN Dong depreciation weighed on foreign investors’ sentiment** toward Vietnamese stocks.

The fact that the **USD-VND exchange rate has stabilized** at current levels for the past several weeks without the SBV having to resort to rate hikes, together with the fact that the rally in the **US Dollar appears to be running out of steam** – especially after last week’s weak employment and ISM/PMI numbers – makes us confident that the SBV will not hike rates in the months ahead. We expect the USD-VND exchange rate to finish 2024 with a **circa 3% depreciation**, with the currency supported by a **surge in Vietnam’s trade surplus** from 3% of GDP in 2023 to 7% in 2024. That expectation is reinforced by the sudden **~1% appreciation** in the value of the VN Dong over the last few days, bringing the YTD depreciation in the value of Vietnam’s currency **back to 3%**.

### **Vincom and Vinhomes**

The share price of **Vingroup (VIC)**, Vietnam’s largest conglomerate, surged by about **40% from end-July to mid-August** in the lead-up to the **listing of the company’s EV subsidiary in the US** (on August 15th). Investors then **sold/took profits** on VIC and its **Vinhomes (VHM)** real estate development subsidiary, which can be seen in the charts below. This drove a **4.4% decline in the VN-Index** on August 18th.

**[Charts: Share Price Movements]**

* **Left: Vingroup’s (VIC) Share Price in 2023**
  + Arrow label: *Share Price Surging in the Lead-up to Vinfast’s IPO*
  + Trend shows rise from ~40,000 to ~75,000, then a decline into November.
* **Right: Vinhomes’ (VHM) Share Price in 2023**
  + Arrow label: *Sell-off Driven by New CB/EB*
  + Trend shows fluctuations with decline after August.

In late-October, VIC announced a USD250 million convertible/exchangeable bond that is redeemable in shares of the company’s VHM real estate development subsidiary at a conversion price of VND 51,635 – 53,880 per share. The share price of VHM dropped by more than 10% around the time that the new CB, which pays a 10% coupon and matures in 2028, was announced on October 26ᵗʰ, as can be seen in the chart above, on the right. That drop in-turn weighed on investors’ sentiment towards VIC somewhat, as can be seen in the chart above on the left.

At this point, we will remind readers that the biggest investors in CBs globally are so-called CB arbitrage funds that buy CBs and short-sell shares against the bonds they hold. Short selling stocks onshore in Vietnam is illegal, but in theory if CB arb funds bought the entire USD250 million bond issue, then they would have needed to sell about USD175 million worth of VHM shares to hedge their positions, according to Bloomberg’s CB pricing model.

That said, hedge selling by CB arb funds tends to be temporary, occurring primarily in-and-around the time that the fund buys what it perceives as “cheap” convertible bonds (with the “cheapness” of the CB assessed based on the implied volatility based on the price of the bond versus the actual volatility of the stock on the market). The net result of all of the above is that VIC’s share price is now below where it was before the surge in the lead-up to the Vinfast listing and VHM’s share price is trading at the lowest level since its IPO five years ago.

### **Margin Calls**

Securities firms in Vietnam had been reducing the amount of stock margin lending they extended to retail investors from early-September, prompted by concerns about the possibility of tighter monetary policy in Vietnam, plus other increasing risks. However, in addition to those margin calls by licensed securities firms, there was “unverified information” of an inspection of one particular source of margin lending by regulators that resulted in the rapid liquidity of some leveraged, speculative positions at the end of the trading day on October 17th, which was another factor that depressed stock prices in October.

### **No Help From Q3 Earnings**

Most companies listed on the stock market have already reported their Q3 earnings, and the results have disappointed somewhat, missing expectations by nearly 10% on average. This further dampened investors’ sentiment, although we do not believe this was one of the primary factors that depressed the stock market in recent weeks.

Also, we note that companies reported a fairly wide range of results. Banks and consumer companies disappointed because of weak credit growth and weak consumption growth by local Vietnamese consumers – which is essentially flat this year, versus 8–9% typical growth. Meanwhile, the earnings of energy and materials companies surged, partly due to the low base effect from their depressed earnings last year.

Such earnings dispersion gives active stock pickers like VinaCapital ample opportunity to outperform the broader index. The earnings of VVF, VinaCapital’s UCITS fund, grew by **36%** versus a circa **6% decline** in the earnings of the broader index, thanks in part to stellar earnings growth in some of the fund’s top holdings (e.g., 35% yoy at Sacombank and 60% yoy at Quang Ngai Sugar).

### **Reasons to be Positive: Cheap Valuation & Earnings Rebound**

We expect EPS earnings growth to rebound to **35% yoy in 4Q23** and **20% in 2024** largely because the sharp slowdown in Vietnam’s economy earlier this year has clearly ended, evidenced by a rebound in GDP growth from **3.3% yoy in Q1** to **4.1% in Q2** and **5.3% in Q3**. The main factor weighing on Vietnam’s economy had been a slowdown in exports to the US, but high-frequency economic data for October confirmed our recent assertions that Vietnam’s manufacturing activity and exports are now recovering, reinforcing our expectation that GDP growth will rebound to **6.5% next year**.

Despite those clear signs of a recovery in Vietnam’s economy, at the bottom of the sell-off valuation of the VN-Index on both a forward P/E and P/B basis fell to a level that was as cheap as it had been only twice in the past 10 years. Furthermore, Vietnam’s stock market trading volume more than halved from USD1.3 billion before the sell-off to USD500 million in late-October. Stock market technicians characterize reduced selling enthusiasm during a sharp market decline as a likely sign that the market will enjoy a robust rebound once the factors causing the sell-off abate, which helps explain the fairly strong performance of the market at the end of last week.

### **Conclusions**

Vietnam’s stock market sold off aggressively from mid-September until the end of October, driven by a confluence of global and local factors. In our view the most important local factor that drove the market down were concerns that the State Bank of Vietnam would significantly tighten monetary policy in Vietnam to support the USD-VND exchange rate – including the possibility of interest rate hikes in Vietnam. For that reason, we were happy to see a modest appreciation in the value of the VN Dong, recently (the VND has now depreciated by **3% YTD**).

Other Vietnam-specific factors weighing on the market included selling of VHM and VIC shares, related to the Vingroup’s issue of a USD250 million convertible/exchangeable bond and the liquidation of stock margin positions by securities firms. From our point of view, all of these transient negative factors have already abated or are easing, and the prospects for higher Vietnamese stock prices in the months ahead are supported by rebounding earnings growth, a rebounding economy, and the market’s cheap valuation./.

### **Disclaimer**

© 2023 VinaCapital Fund Management JSC (VCFM). All rights reserved. This report has been prepared and is being issued by VCFM or one of its affiliates for distribution in Vietnam and overseas. The information herein is based on sources believed to be reliable. With the exception of information about VCFM, VCFM makes no representation about the accuracy of such information. Opinions, estimates, and projections expressed in this report represent the current views of the author at the date of publication only. They do not necessarily reflect the opinions of VCFM and are subject to change without notice. VCFM has no obligation to update, amend or in any way modify this report or otherwise notify a reader in the event that any of the subject matter or opinion, projections or estimates contained within it change or become inaccurate.

Neither the information nor any opinion expressed in this report are an offer, or an invitation to make an offer, to buy or to sell any securities or any option, futures, or other derivative instruments in any securities. Nor should it be construed as an advertisement for any financial instruments. This research report is prepared for general circulation and for general information only. It does not have regard to the specific investment objectives, financial situation or particular needs of any person who may receive or read this report. Investors should note that the prices of securities fluctuate and may rise and fall. Past performance, if any, is no guide to the future.

Financial instruments discussed in this report, if any, may not be suitable for all investors. Investors must make their own financial decisions based on their particular financial situation and investment objectives. This report may not be copied, reproduced, published, or redistributed by any person for any purpose without the express permission of VCFM in writing. Please cite sources when quoting.