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**LOOKING AHEAD AT 2024**

After a challenging 2023, all indications are that 2024 should be a stronger year for Vietnam's economy, driven by a rebound in the manufacturing sector and an improvement in consumer sentiment. In addition, the plunge in interest rates throughout 2023 should help boost the real estate market after having helped support the stock market last year. In 2024, we expect:

* **GDP growth to increase** from 5.1% last year to 6-6.5% this year driven by a recovery in Vietnam's exports, which fell 4% in 2023, to 7% growth in 2024. The demand for "Made in Vietnam" products – especially for consumer electronics – from consumers in the US/EU has already started to recover and is likely to accelerate as 2024 progresses.
* **Domestic consumption growth to recover**. Consumption by local Vietnamese (excluding tourists) was nearly flat last year, partly because sentiment was depressed by layoffs in the manufacturing sector and issues in the real estate market, but consumption already started recovering in late-2023 as factories began rehiring workers and the Government took steps to address issues in the real estate market.
* The VN-Index (VNI) **earnings to increase 10-15%**, driven by 18% earnings growth in the Banking sector (which has a 37% weighting in the VNI) and by 33% earnings growth in the Consumer sector (14% weighting), both of which reflect our expectations for faster growth in domestic consumption, and faster credit growth this year.

Further to that last point, the VNI ended 2023 up 12.2% (and up 9.3% in USD terms) after having been up as much as 24% YTD in early-September before USD-VND depreciation prompted the State Bank of Vietnam (SBV) to tighten monetary policy somewhat - which sent stock prices tumbling. However, the value of the VND is likely to be fairly stable this year as pressures on Vietnam's currency are more balanced now than in 2022-23.

A stable USD-VND exchange rate means that interest rates will also remain stable, since most of the 2022-23 fluctuations in VND interest rates was linked to the USD-VND exchange rate. Lower interest rates and lower interest rate volatility help support Vietnam's economic growth via credit creation, making loans more accessible and affordable to businesses, prospective home buyers, and consumers.

Finally, Vietnam's position in the world's evolving geopolitical landscape, coupled with the country's existing appeals to investors helped propel a 32% increase in registered FDI last year to USD 37 billion (9%/GDP) despite concerns about the recent implementation of the Global Minimum Tax (GMT) regime, which is discussed below. Vietnam was the only country that both Joe Biden and Xi Jinping visited in 2023, prompting the *Wall Street Journal* to publish an article titled "Why Everyone Wants to be Vietnam's Friend".

**Vietnam's GDP Growth to Accelerate in 2024**

We expect Vietnam's GDP growth to reach 6.5% in 2024 due to several factors, including:

1. **Manufacturing output** growth is likely to recover from less than 4% in 2023 to 8-9% in 2024, which is still below pre-COVID growth levels because of the weakening US/global economy (most products manufactured in Vietnam are exported, especially to the US).
2. **Interest rates** in Vietnam will likely remain lower and less volatile than over the last two years, which will support the economy in a number of ways, including encouraging consumption and credit growth.
3. **Consumption** is likely to see a modest acceleration, supported by #1 and #2 above, although real retail sales growth is only likely to accelerate slightly in 2024, and most likely later in the year.

Further to that last point, Vietnam's GDP growth fell from 8% during its post-COVID reopening boom in 2022 to 5.1% last year, a drop that was roughly equally attributable to plunges in industrial production/manufacturing and in the services sector/domestic consumption. While we expect a healthy rebound in manufacturing activity, we do not expect a big increase in the growth of consumption. That's because a surge in foreign tourist arrivals last year boosted consumption last year – which will not be repeated this year.

The number of tourists visiting Vietnam from countries other than China (which previously accounted for about one-third of total tourist arrivals) has almost fully recovered to pre-COVID levels. There is a possibility that Chinese tourist arrivals (which only reached 30% of pre-COVID levels last year) will continue to recover in 2024, but consumer sentiment in China currently languishes at similar levels as during the country's COVID lockdowns as the country deals with a wide range of structural economic issues.

**Key Projections for 2024**

|  | **2023** | **2024F** | **Pre-COVID Average\*** |
| --- | --- | --- | --- |
| GDP | 5.1% | 6.0 - 6.5% | 7.0% |
| Real Retail Sales | 7.1% | 7.5% | 9.0% |
| Manufacturing | 3.6% | 8.0% | 12.0% |
| Export Growth | -4.4% | +7.0% | 12.0% |
| VND Depreciation | 2.7% | 0.0% | 1.6% |

*Source: GSO, Bloomberg, VinaCapital* *Average over 2016-19*

The main risk to our moderately positive outlook is the possibility of a "hard landing" in the US economy, causing demand for "Made in Vietnam" products to plunge. The value of the US Dollar would likely soar in such a scenario (as it typically does) driven by "safe haven" buying, which would limit the ability of Vietnamese policy makers to respond to a slowing Vietnamese economy by slashing VND interest rates (Vietnamese policy makers have repeatedly shown their resolve to defend the value of the VN Dong in recent years).

That said, the Vietnamese Government would have ample ability to respond to such a crisis with massive fiscal stimulus, including a surge in infrastructure spending. In early 2023, the Government guided its intention to increase infrastructure spending by about 50% to about USD 30 billion, or ~7%/GDP last year, up from 4%/GDP in 2022. It is very likely that part of the reason the Government intended to ramp up infrastructure was to offset the predictable hit to the economy from the slowing global demand for "Made in Vietnam" products.

Early indications are that infrastructure spending increased to around USD 25 billion (or to 6% of 2023 GDP), and that the Government plans a similar level (USD 25b) of spending this year. Critically, the Government's past prudence permits it to significantly ramp up spending if it wanted to. The State Treasury of Vietnam reportedly has over USD 30 billion of undisbursed funds deposited in the country's banks¹ – most of which was earmarked for infrastructure projects in past years but did not get spent – and the Government debt-to-GDP ratio is below 40%, which is very low compared to most EM and DM countries around the world.

Finally, the Government implemented a few minor measures to boost the economy last year, including a temporary cut in the country's VAT rate from 10% to 8% and a cut in the environmental tax on petrol; these measures probably only equated to total of about 0.5% of GDP, although a planned increase in public sector salaries next year will probably equate to another circa 1%/GDP of stimulus to the economy. All of that said, we again believe the Government could do much more to support the economy if it needed to.

**Vietnam's Exports and Manufacturing Are Rebounding**

In 2023, a plunge in Vietnam's manufacturing output and exports were the biggest drags on the economy, just as we predicted in our "Looking Ahead at 2023" report, which was a non-consensus call at that time. However, Vietnam's longest streak of falling exports in over a decade has already bottomed out and export growth is likely to accelerate to some degree throughout 2024.

Global export orders are poised to start expanding again because the inventories of US retailers and other consumer facing firms look likely to end 2023 down about 5-7% year-on-year, according to recent earnings calls of firms like Walmart, Target, Best Buy, Nike and others. Inventories of US retailers had surged by well over 20% yoy in late-2022 and the resulting destocking efforts is reflected in the plunge in global export orders that can be seen in the chart below.

Inventory depletion in 2023 explains why Vietnam's overall exports deteriorated from 11% growth in 2022 to a 4% drop in 2023. With exports equating to over 80% of GDP, a swing of that magnitude has a major impact on GDP growth. We only expect a modest rebound in exports to the US this year, partly because US credit card debt surged ~40% over the last two years, which is constraining US consumers' capabilities to continue purchasing "Made in Vietnam" products and which helps explains why 2023 holiday spending in the US was reportedly tepid².

**Electronics Exports Already Rebounding**

Computers and electronics exports are already rebounding, although exports of smartphones and low value garment products are still falling (note that each of those three product categories accounted for about 15% of Vietnam's total exports last year). Sales of PCs and other "work from home" products plunged post-COVID, but users have started upgrading to computers that are sufficiently powerful to run AI applications.³ This helps explain why market research firm Canalys expects global PC sales to rebound from a 12% drop in 2023 to nearly 10% growth in 2024.

In contrast, global smartphone sales are only likely to improve from a 3.5% drop in 2023 to 3.8% growth in 2024 according to IDC. Smartphone sales resumed growing for the first time in two years in late-2023 (by about 5% year-on-year), but unlike PCs, for which there is a compelling reason for users to upgrade, consumers do not see sufficiently compelling reasons to upgrade their smartphones.

The net result of all of the above is that *"the tech sector has bottomed out...led by consumer electronics replacement demand"* as Standard Chartered noted in its 2024 global strategy report. Standard Chartered also observed that electronics exports tend to lead overall export recovery/growth in Asia, which bodes well for Vietnam's overall exports in 2024, while JP Morgan's 2024 strategy report highlighted the resulting rebound in Asia-wide tech manufacturing output, which bodes well for GDP growth.

Additionally, we note that Vietnam's imports of the electronic components used to manufacture computers and consumer electronics is surging, which is a reliable leading indicator that companies are ramping up to fulfill the orders in their pipelines.

Finally, garment and footwear exports have not started recovering yet because: 1) demand from US consumers remains weak (Target's CEO noted that some US consumers put off buying winter clothes last year until the weather actually turned cold); 2) some production is relocating to countries with cheaper wages (especially Bangladesh); and 3) some production is moving out of Asia entirely to minimize the possibility that any of the cotton or other raw material inputs were sourced from China.⁴,⁵

All of that said, the overseas customers of garment and footwear factories in Vietnam have generally guided those local firms to expect an increase in orders this year, according to our industry contacts. However, those Vietnamese factory managers also lament that their customers have essentially been giving them small lot and/or last-minute orders rather than the pipeline of 6-12 months' work as they had in the past.

**Domestic Consumption Recovery**

In 2023, consumer spending in Vietnam was depressed by layoffs in the manufacturing sector - which affected lower-income consumers - and by the country's "frozen" real estate market – which affected middle- and upper-income consumers, although this weakness was largely offset by a surge in foreign tourist arrivals. The number of foreign tourists visiting Vietnam leapt from 20% of pre-COVID levels in 2022 to 70% in 2023, accounting for most of the country's 7.1% real retail sales growth last year.⁶ Consequently, we estimate that the growth of spending by local Vietnamese consumers (excluding tourists) was nearly flat last year. That said, consumer spending and sentiment in Vietnam both bottomed in mid-2023, as can be seen below.

One reason sentiment and spending started recovering in the middle of last year is that the employment picture started improving around that time. In early-2023, highly publicized factory layoffs were a major drag on spending and sentiment, but the pace of layoffs slowed by mid-2023; the layoffs were a direct consequence of the drop in exports, which had also slowed by then, and by late-2023, firms resumed hiring workers.

Specifically, factories started expanding their workforces in October, after having laid off workers for most of the year according to S&P Global's PMI survey for Vietnam. Consequently, industrial employment expanded by nearly 1% month-on-month in October according to the General Statistics Office (GSO) and by the end of the year, industrial employment had fully recovered (i.e., it was essentially unchanged yoy). That said, wages grew by less than 5% yoy, which is lower than Vietnam's typical 7-10% yoy factory wage growth, reflecting weak conditions in the labor market.

Consumer sentiment and spending got a further boost in late-2023 from the nascent thawing of the country's "frozen" real estate market. The highly publicized slowdown in Vietnam's real estate market negatively impacted consumer sentiment to a degree that is out of proportion to the reality of the issues that the market actually faces. Consequently, a modest thawing could disproportionately boost consumer sentiment this year.

**Other Factors Influencing Consumption in Vietnam**

The temporary surge of interest rates shown on the first page of this report weighed on home prices, which in-turn dampened consumer sentiment, but lower mortgage interest rates/monthly payments will also free up money for homeowners to spend on purchases (mortgage rates in Vietnam are floating and linked to banks' deposit rates).

That said, last year's temporary spike in savings rates generated windfall income for savers - some of which got spent in the economy (a similar phenomenon helps explain the surprising strength of the US economy last year). Consequently, it is difficult to disentangle the impact of last year's temporary surge in interest rates on consumption in Vietnam, although lower rates will make it easier for consumers to finance purchases of "big ticket" items which should support consumption this year (outstanding consumer loans growth was very weak in 2023).

Finally, the labour and real estate markets were not the only influences on consumer spending last year – we focused on these factors because they had the biggest impact. For example, the Government's temporary reduction in the VAT rate from 10% to 8% also supported spending, but we do not believe that cut was big enough to significantly influence consumer behaviour.

**Understanding the Issues in Vietnam's Real Estate Market**

In a typical real estate "boom and bust" cycle, banks lend too much money to property speculators and real estate developers, which results in the market becoming vastly oversupplied with new housing units. At some point, the supply of credit dries up, crashing both real estate prices and property development activity. The market then languishes for years as it digests the existing oversupply of empty housing units.

This is *not* what is currently happening in Vietnam. Real estate development activity ground to a halt *not* because there is an oversupply of empty housing units; Vietnam's vacancy rate is below 5%.

**Vietnam is Not in the Aftermath of a Bubble**

Property development activity in Vietnam ground to a halt because of a confluence of legal and regulatory issues that make it very difficult to get new projects approved as well as certain market inefficiencies in financing the development of greenfield property projects. Critically, property prices in Vietnam have *not* crashed since the demand for new housing units outstrips supply by a factor of 2-to-1.

That said, the prices of some selected properties have dropped, especially if the homeowner not yet received a proper legal title from the developer, which in-turn is because the developer had not attained proper permissions to proceed with the project from the outset. Also, the prices of some properties that are poorly located or in geographies oversaturated with new housing units have dropped after having increased too much during what was admittedly a slightly frothy market in 2021 and early-2022.

**Overly Negative Sentiment**

Consumers and homeowners in Vietnam are peripherally aware of issues in the real estate market, and they occasionally read sensationalist headlines that property prices are plunging, prompting a reflexive reaction to limit their spending. But those sensationalist headlines do not reflect the reality of Vietnam's real estate market.