KB Securities VIETNAM

Macro Outlook 2021

Out of the woods

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Economic recoveries are boosted with good control of COVID-19

Vietnam GDP growth in 2020 reached the lowest level in the past 20 years, but the recovery of the agricultural and production sectors, especially domestic consumption in 2H2020 served as a silver lining that made Vietnam one of a few countries to record a positive economic growth. The impressive results were achieved thanks to the Government's anti-pandemic efforts, together with appropriate expansionary fiscal and monetary policies, which supported economic growth without rattling inflation and exchange rates.

Below is our forecast about Vietnam's economy in 2021:

1) GDP growth should reach 6.6%, powered by rebounding domestic consumption, manufacturing activities, trade agreements and FDI inflows;

2) Average CPI may be 3.6% for the whole year 2021, under the inflation limit set by the Government;

3) Monetary policy would be at a controlled easing state, with money and credit growth of 14% and 13% respectively. The VND is expected to appreciate in 2021 following the State Bank moves to change foreign currency buying policy and accusations of currency manipulation from the US.

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Executive Summary

Vietnam economy showed signs of post-pandemic recovery in 2H20. Given hopes that the disease will continue to be well controlled in 2021 and the vaccine distribution roadmap becomes clearer in 2H21, GDP should extend its growth momentum. We suppose there are three main growth drivers in 2021, namely the recovery of domestic consumption, the impact of trade agreements and the FDI inflows. The biggest risks include the COVID-19 pandemic and the possibility of the vaccine mass production, tariffs on exports to the US after Vietnam being named as a currency manipulator, and the risk of downgraded credit rating.

Macro stability was focused and maintained throughout 2020 despite the emerging pressure on inflation and exchange rate management. Considering external and objective factors, together with changes in the State Bank's exchange rate management after being accused by the US of currency manipulation, we forecast that the exchange and inflation rates would still be under the control of Government.

Table 1. Vietnam – Macro targets in 2021

			KBSV forecast
	Unit	2020	Jan-21
GDP growth	% YoY	2.91	6.60
Headline CPI	% YoY	3.23	3.60
Credit growth	% YTD	10.14*	13.00
M2 growth	% YTD	12.56*	14.00
Policy rate (refinancing rate)	%/year	4.00	3.50
USD/VND	VND	23,098	22,900

Source: KB Securities Vietnam

* Data as of December 21, 2020

Macro highlights in 2020

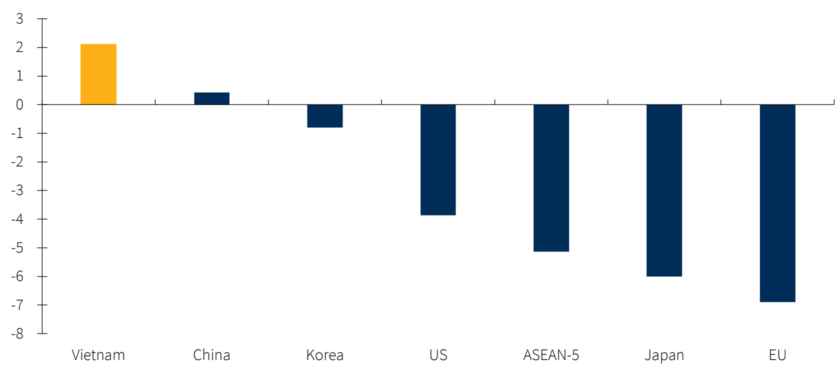
❖ 2020 GDP growth: Better-than-expected recoveries

Vietnam economy rebounded with an unexpected speed thanks to domestic consumption demand, export growth and accelerated public disbursement

Vietnam economy recovered better than expected in the second half of the year, making Vietnam one of a very few countries in the world to log positive GDP growth. Good control of the pandemic while taking advantage of domestic factors (domestic consumption and public investment) and benefits form the (export) value chain is the main key supportive factor to help Vietnam become a bright spot in the region and the world (Figure 1). According to data from the General Statistics Office (GSO), 2020 GDP is estimated to increase 2.9% YoY, reaching 20-year lows. However, 4Q GDP growth is 4.5%, much higher than expected and up sharply from 0.4% and 2.7% in 2Q and 3Q (Figure 2).

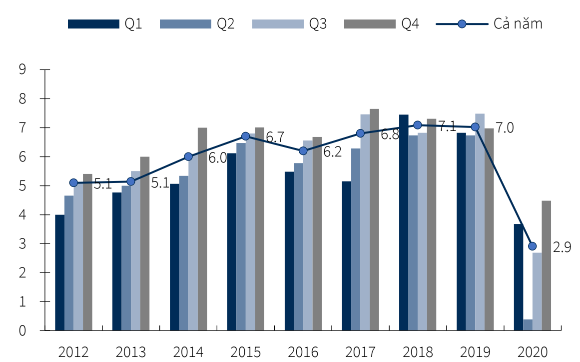
9M20 GDP growth of Vietnam is quite outstanding compared to these countries

Fig 1. Vietnam & its major partners – 9M20 GDP growth (%)



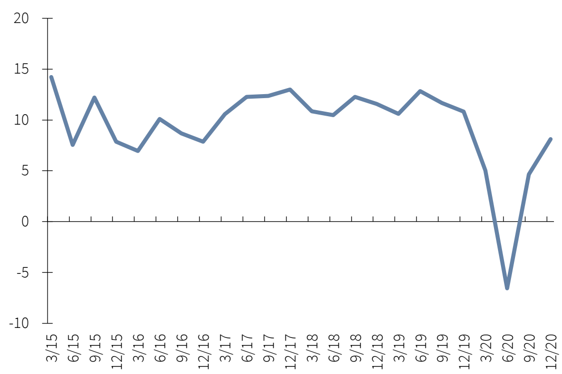
Source: Bloomberg, KB Securities Vietnam
*Note: ASEAN-5: Thailand, Malaysia, Indonesia, Singapore, Philippines

Fig 2. Vietnam – Quarterly GDP growth (%)



Source: General Statistics Office, KB Securities Vietnam

Fig 3. Vietnam – Retailing & services revenue growth (%)



Source: General Statistics Office, KB Securities Vietnam

From the demand side, domestic consumption and FDI growth showed signs of recovery. To be more specific:

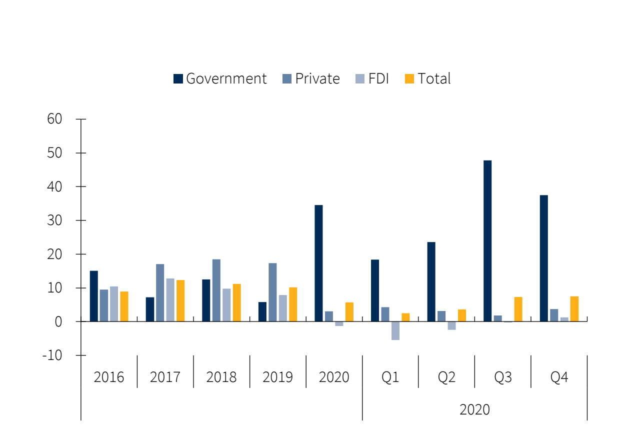
Consumption growth rose again in the last six months of 2020

- Consumption growth in 2020 rose 1.1% YoY, much lower than the average growth of 7.5% in 2015-2019 period mainly due to the heavy impact of the nationwide lockdown by the end of April. It recovered slightly by 1.2% and 1.5% YoY in 3Q and 4Q respectively, in line with the rises in retailing and service revenue growth (up 4.7% and 8.1% YoY in 3Q and 4Q) (Figure 3).

Investment capital from the state budget is a bright spot for investment throughout 2020

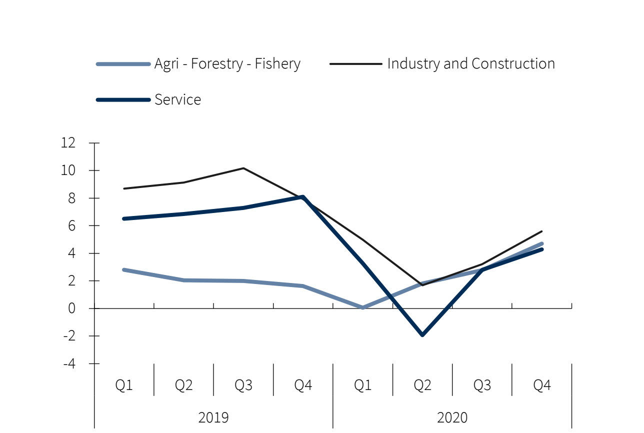
- 2020 social investment capital, despite hitting the lowest growth in the last decade, recovered relatively well in 4Q20, especially in the FDI sector (Figure 4). FDI increased 1.3% in 4Q from a negative growth logged in the three previous quarters. The bright spot for investment in 2020 is the state sector. The capital increase realized from the State budget maintained a positive growth rate in 2020, especially in the second half of the year, reflecting the Government's achievements in promoting public disbursement. Data from the Ministry of Finance indicated that the disbursement progress from the end of July up to now has recorded promising progresses, especially in October and November 2020. 11M20 public disbursement reached 79.3% of the plan, up 34.0% YoY – the highest increase in 2011-2020.

Fig 4. Vietnam – State investment growth (%)



Source: General Statistics Office, KB Securities Vietnam

Fig 5. Vietnam – GDP growth by sectors (%)



Source: General Statistics Office, KB Securities Vietnam

From the supply side, all sectors showed a post-pandemic recovery (Figure 5):

Service sector growth recovered strongly in the second half of the year, focusing on wholesale, retail, finance and banking.

- Service sector picked up 2.3% (up 3.6% in 2H20 alone). The bounceback of domestic consumption demand in the last six months of 2020 strongly boosted wholesale and retail sectors (+5.5%) and finance and banking (+6.9%). Meanwhile, the suspension of flights transporting international visitors to Vietnam has been maintained for more than nine months, which slows down the growth of the hospitality and catering industries (-14.7%), transportation, and warehousing (-1.9%).

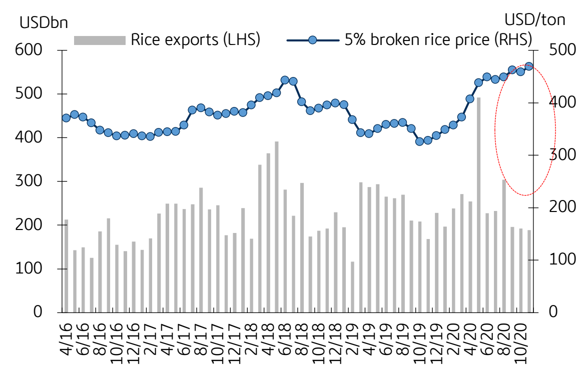
The recovery of fishery and rice exports powered the growth of the agriculture, forestry and fishery sector

- The agriculture, forestry and fishery sector gained 2.9% in 2020 (up 3.9% in 2H20 alone), higher than the growth recorded in 2019. The prices of agricultural and fishery products recovered on strong demand and the newly effective EVFTA (from August 1, 2020), while main competitors such as India are reeling from the Coronavirus pandemic. Specifically, rice prices maintained their eight-year highs for many months, 11M20 rice exports rose 9.7% YoY, and 11M shrimp exports grew strongly by 11.3% YoY (up 34% YoY and 5.2% YoY in the US and EU markets respectively).

The manufacturing and processing industry continued to be the GDP growth force

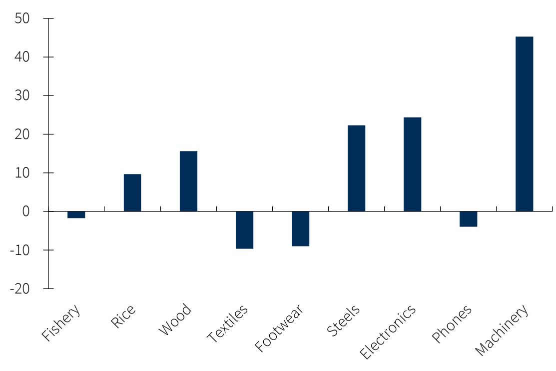
- The industry and construction sector grew 4.0% (4.6% in 2H20 alone). The manufacturing and processing industry continued to be the main driver for GDP growth (contributing 1.3 percentage points), of which the export sectors accounted for a large proportion. Export data showed a deep differentiation among export categories (Figure 7). FDI sector's exports rose 10% YoY as FDI enterprises took advantage of the supply chain relocation and the economic recovery in China. Vietnam's 11M20 export turnover reached USD255 billion, up 5.5% YoY. Export growth of computers and components posted gains by 24.4% YoY, machinery and equipment up 45.2%, timber up 15.5%, iron and steel up 22.3% while weakening global demand hit key export items in previous years, including smartphones and components (down 4.0%), textiles and garments (down 9.7%) and footwear (down 9.0%).

Fig 6. Vietnam – Rice export prices and export turnover (USDmn, USD/ton)



Source: Vietnam Customs, KB Securities Vietnam

Fig 7. Vietnam – Export growth of some key items (%)



Source: Vietnam Customs, KB Securities Vietnam

❖ 2020 inflation: The Government's efforts

Inflation rate was well controlled in 2020, and average CPI was much lower than the limit

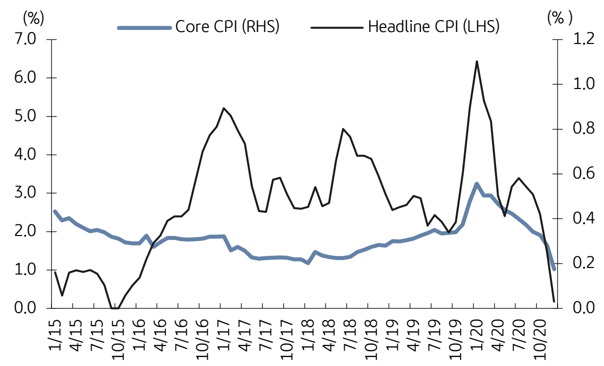
Inflation was well controlled in 2020 thanks to the Government's strict measures despite the increasing pressure from the surge in food prices. Average CPI rose 3.2% YoY, much lower than the limit of 4.0%. Average inflation rate cooled down in 2H20 (Figure 8) from 5.6% in 1Q to only 1.4% in 4Q. Core inflation also slowed down. The average headline inflation was 2.3%, within the range of 2.0% – 2.5% targeted by the Government.

The sharp rise in pork prices and big fall in oil prices are the two powerful factors to 2020 CPI

Main factors affecting CPI in 2020:

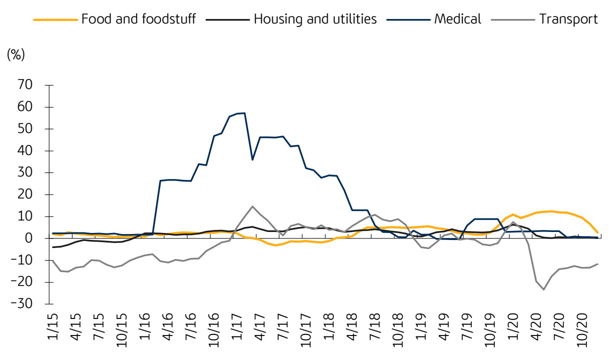
- Food group prices increased 12.3% YoY, mainly due to the 57.2% YoY surge in pork prices, which raised headline CPI by 2.6%;
- Foodstuff group prices picked up 4.5% due to the increase of 5.1% in export rice prices and added 0.2% to the headline CPI;
- Traffic prices dropped by 11.2% due to 23.0% drop in gasoline prices, helping headline CPI slow down by 0.8%.

Fig 8. Vietnam – Core and headline CPI (% YoY)



Source: General Statistics Office, KB Securities Vietnam

Fig 9. Vietnam – Changes in the main CPI groups (%)



Source: General Statistics Office, KB Securities Vietnam

Government made efforts to control inflation as CPI surged in the first six months

The Government successfully kept the inflation rate under the limit despite the spike in pork prices in the first six months of 2020:

- The Government allowed enterprises to import of pork and breeding pigs from Thailand to stabilize domestic pork prices. This helped pork prices lower by 15%.
- The prices of public services were strictly controlled as the Government's request to postpone the increase in base salary in early July alleviated the pressure on healthcare group. In addition, the Government also asked ministries to coordinate so as not to increase prices of State services.

❖ 2020 monetary policy: easing but controlled

Monetary policy with a controlled easing trend

To stimulate credit demand amid the pandemic, the State Bank lowered the policy rates three consecutive times in March, May and October 2020, cut refinancing rates by 150bps, and ceiling deposit rate below six months by 80-100bps. In addition, the State Bank delayed to tighten the ratio of short-term capital for medium and long-term loans for another year so that banks would have to restructure their capital sources right away after they supported enterprises in difficulty of liquidity by reducing lending interest rates and restructuring debts. Vietnam's monetary policies to cushion the economy against the pandemic are less than other regional countries (Table 2) and mainly use resources from commercial banks, hence milder impacts on money supply. We think that these policies are appropriate to current economic conditions and can help avoid bad consequences such as bad debts and asset bubble as in 2009 – 2011.

Table 2. Regional countries – Policies to cope with the Coronavirus pandemic

	Monetary response	Fiscal response
Vietnam	Cut policy rates by 100bps	3.6% GDP
	Ask commercial banks to support COVID-19 19 impacted businesses	
Singapore	Adopt a zero percent annual rate of appreciation of the policy band and reduced the mid-point to the prevailing level of the S$NEER	20.1% GDP
	Ask commercial banks to support COVID-19 19 impacted businesses	
	Announce SGD125 million support package to sustain and strengthen financial services and FinTech capabilities	
	Establish USD 60 billion swap lines with the US Federal Reserve and provide RMB 25 billion of funding to banks in Singapore	
Thailand	Cut policy rate by 75bps	9.6% GDP
	Provide soft loans to financial institutions amounting to THB 500 billion for on-lending to SMEs	
	Establish Corporate Bond Stabilization Fund (BSF) to provide bridge financing of up to THB 400 billion	
	Central bank purchases of government bonds	
Indonesia	Cut policy rate by 125bps	4.4% GDP
	Cut Reverse Required Ratio	
	Increase the maximum duration for repo and reverse repo operations	
	Central bank purchases of primary government bonds	
Malaysia	Cut policy rate by 75 bps	5.0% GDP
	Cut Reverse Required Ratio	
	Liquidity supports worth of 1.3% GDP	

Source: IMF, KB Securities Vietnam

Excess liquidity made interbank interest rates and treasury bond yields at many-year lows

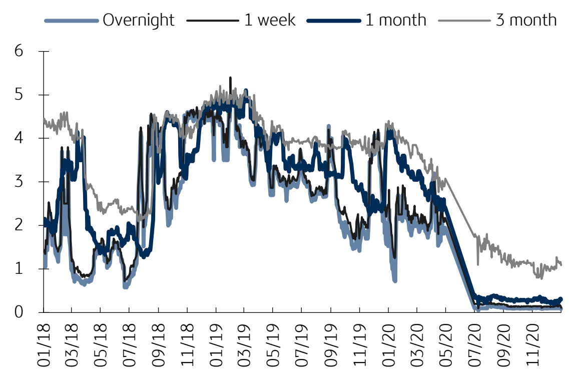
System liquidity in 2020 remained abundant, especially in the last six months with high gap between M2 and credit growth (Table 3). This is mainly due to: 1) lower demand for credit as businesses are facing many Coronavirus-induced difficulties (Credit growth as of December 21, 2020 was 10.1%, lower than the rate of more than 12.4% in the same period in 2019); and 2) the State Bank's foreign currency purchases to accumulate foreign reserves estimated at USD15 billion, equivalent to VND350 trillion of net injection. Excess liquidity has caused interbank interest rates and government bond rates to remain low since May 2020 (Figures 10, 11). As a result, the deposit rate average also dropped sharply by 150 – 300bps. Lending interest rates decreased slightly by 50 – 100bps under the request of the State Bank to support businesses during the pandemic.

Table 3. Vietnam – Demand & supply on the money market

(VNDbn)	31/3/2019	30/6/2019	30/9/2019	31/12/2019	30/3/2020	30/6/20020	30/9/2020	21/12/2020
M2	9,478,157	9,866,810	10,083,289	10,573,725	10,755,572	11,118,423	11,485,845	11,901,785
Growth rate YTD (%)	2.89	7.11	9.46	14.78	1.72	5.15	8.63	12.56
Growth rate QoQ (%)	2.89	4.10	2.19	4.86	1.72	3.37	3.30	3.62
Increase in M2 amount by quarters	266,309	388,653	216,478	490,436	181,847	362,851	367,422	415,940
Credit outstanding balance	7,437,086	7,742,083	7,888,910	8,195,393	8,302,412	8,494,504	8,694,050	9,026,406
Growth rate YTD (%)	3.13	7.36	9.40	13.65	1.31	3.65	6.08	10.14
Growth rate QoQ (%)	3.13	4.10	1.90	3.88	1.31	2.31	2.35	3.82
Increase in lending amount by quarters	225,911	304,997	146,827	306,483	107,019	192,092	199,546	332,356
Annual gap bt. M2 and lending growth	40,398	124,054	193,706	377,659	74,828	245,587	338,635	251,460
Quarterly gap bt. M2 and lending growth	40,398	83,656	69,651	183,953	74,828	170,759	167,876	83,584

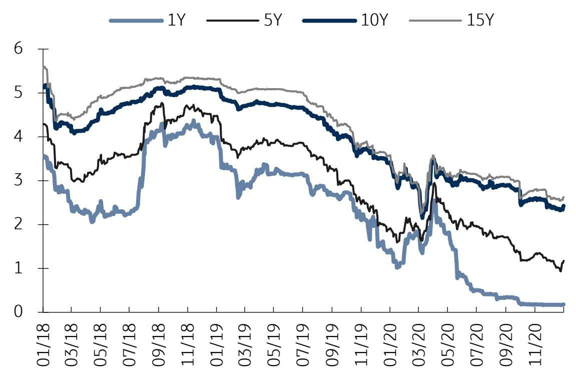
Source: State Bank, KB Securities Vietnam

Fig 10. Vietnam – Interbank interest rates (%)



Source: State Bank, KB Securities Vietnam

Fig 11. Vietnam – Government bond yields (%)



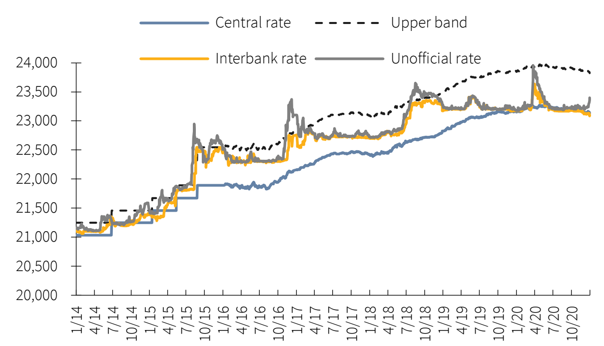
Source: General Statistics Office, KB Securities Vietnam

❖ USD/VND exchange rates: remained stable

The exchange rate was stable in 2020, while NEER and REER plummeted and hit the lowest level in the past three years

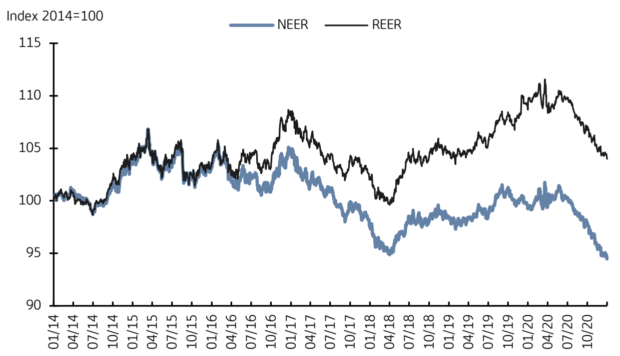
The USD/VND exchange rate after fluctuating strongly in the last two weeks of March turned down for the rest of the year. As of December 31, the central and interbank rates decreased by 0.1% and 0.3% respectively YoY, while the unofficial rate increased by 0.9% YTD. However, the downtrend of the NEER and REER became more obvious in the second half of the year (Figure 13). The NEER fell to the equivalent level in 2017, which means the VND depreciated relatively to the basket of currencies. This boded well for export activities, but also increased the pressure on the State Bank when the Vietnam is named as a currency manipulator.

Fig 12. Vietnam – USD/VND exchange rate (VND)



Source: Bloomberg, KB Securities Vietnam

Fig 13. Vietnam – NEER & REER (points)



Source: Bloomberg, KB Securities Vietnam

The sharp decline of USD in international markets thanks to the Fed's loosening policy helped to maintain the stability of exchange rate in recent years

The main reason for the stable USD/VND exchange rate in 2020 and the devaluation of NEER and REER is the clear downward trend of the USD in international markets. Specifically, after spiking more than 8% between March 9 and March 20, the DXY index has now plummeted to its four-year lows thanks to the Fed's easing monetary policies and fiscal aid packages. In addition, the State Bank proactively bought and increased foreign exchange reserves over the last year, which partly slowed down the decline of the USD/VND exchange rate on the interbank market and helped the VND devaluate against other eight currencies in the basket, especially CNY, EUR, and JPY.

The State Bank changed the policies in managing exchange rates after the US designated Vietnam as a manipulator

As of December 31, 2020, the State Bank stopped listing spot rates at transaction points and buying foreign currencies on spot. From January 4, 2021, the State Bank bought foreign currency for six-month term (instead of three-month term as before) with cancellation at VND23,125/USD. Each credit institution can cancel only once. Previously, the State Bank also lowered the spot rate at transaction points from VND23,175/USD to VND23,125/USD. This is the first move of the SBV after being accused of currency manipulation by the US in mid-December, which can be inferred that:

- Stopping bid rate listing at the Exchanges will remove the "stop button" for the decline of the USD/VND exchange rate on the foreign exchange market.
- Stop buying foreign currencies on spot shows that the State Bank is no longer willing to buy USD to increase FX reserves as before. Commercial banks need to proactively contact the State Bank in case of a large positive foreign currency amount. Furthermore, if there is any proceeding, the spot purchase of USD will most likely take place on a case-by-case basis.
- The expansion of USD buying term to six months with an only cancelation time shows that selling USD with term has become much more difficult while selling USD for spot is limited. In addition, the six-month term will limit the violation of the third criterion of the US Department of Commerce, when the one-way intervention in the foreign exchange market occurs at least six/12 months.

The State Bank can use the difficulty of commercial banks to sell foreign currencies as an evidence to negotiate with the US Department of Commerce, showing that the State Bank has no longer actively intervened in the one-way foreign currency market through the purchase foreign currency to supplement foreign exchange reserves.

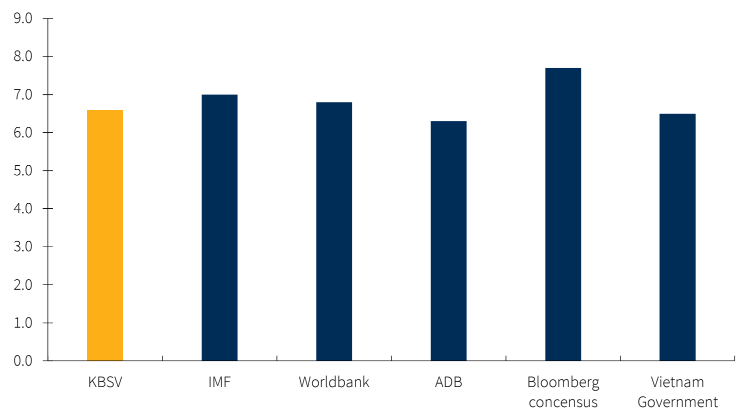
2021E macro outlook

❖ 2021E GDP growth

2021 GDP is expected to reach 6.6%

In 2021, we expect the Government continue to keep COVID-19 pandemic under control. The current vaccine has been distributed in a limited number of developed countries and should be widely passed out to the rest of the world including lower middle-income countries like Vietnam as early as the 2H.2021. Therefore, service, tourism and hospitality industries cannot recover to the pre-pandemic levels right away, and the reopening of international routes will also limit in countries where Coronavirus is well-insulated. With the base scenario above, we forecast that Vietnam's GDP growth in 2021 will reach 6.6%. Factors supporting growth include domestic consumption, recovery in manufacturing activities, FTAs, and the return of FDI inflows. Meanwhile, the risk will come from the additional US tax and credit rating downgrade due to high public debt.

Fig 24. Vietnam – GDP growth forecasts in 2021 (%)

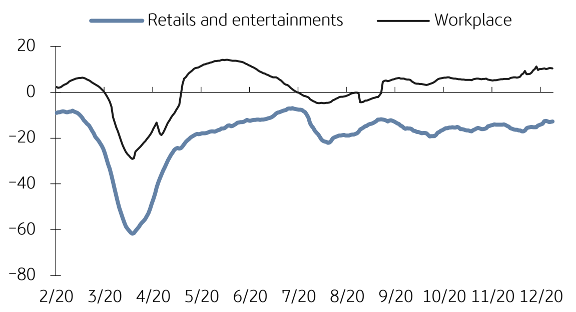


Source: IMF, WB, ADB, Bloomberg, KB Securities Vietnam

Domestic consumption demand is expected to be a growth driver in 2021

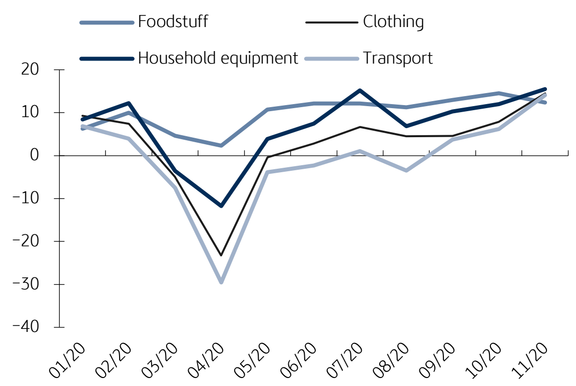
Stable COVID-19 control of the Government is the key to the recovery of domestic demand in 2021. Google's mobility survey (Figure 15) shows the mobility to retail and entertainment, despite not yet recovering to the pre-pandemic levels (partly due to the high YoY levels during Lunar New Year holidays) but has remained a stable uptrend over the past five months. Positive consumer demand as new orders of the consumer goods manufacturing industry in the PMI index continuously increased over the past six months. In addition, retail sales growth increased steadily 2H.2020 across all groups (Figure 16) and we expect consumption to recover to pre-pandemic growth with total retail sales of consumer goods and services growth at 8-9% in 2021E.

Fig 15. Vietnam – Community mobility to retail and entertainment area (%)



Source: Google, KB Securities Vietnam

Fig 16. Vietnam – Growth of retail groups (%)

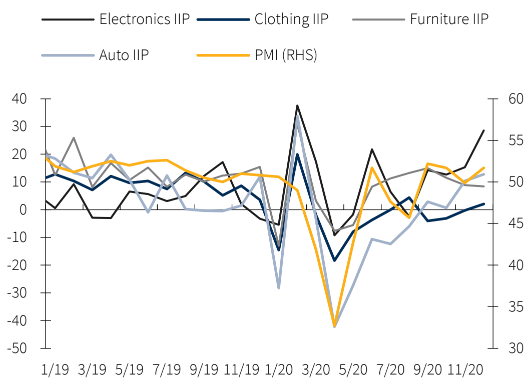


Source: Ministry of Industry & Trade, KB Securities Vietnam

The electronics manufacturing cycle returns globally to support manufacturing and manufacturing

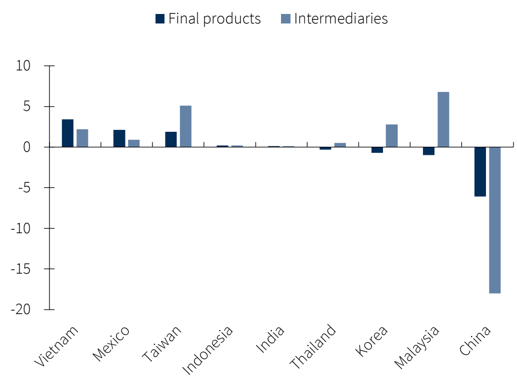
Vietnam's manufacturing and processing activities are on a strong recovery momentum since April 2020. Export data, PMI and IIP show that this recovery is uneven across industry groups, mainly coming from the electronics and components manufacturing sector (Figure 17). The driving force of the electronics manufacturing industry is strong with high demand, reflected in the number of new orders surging over the past several months in key value chain markets such as South Korea, China and Taiwan. Therefore, we expect Vietnam to continue to benefit from the above cycle as it reaffirms its position as the leading manufacturing country in Southeast Asia (Figure 18, Vietnam took market share of electronic products to the US from China with both intermediate and final products).

Fig 17. Vietnam – IP & PMI (%, point)



Source: General Statistics Office, HIS Markit, KB Securities Vietnam

Fig 18. Vietnam – Market share of electronic exports to the US in 2017 – 2019 (percentage point)



Source: ITC, KB Securities Vietnam

FTAs will create a driving force for Vietnam's key exports

The three major FTAs Vietnam signed in the past two years are CTTPP, EVFTA and RCEP. In particular, it is noteworthy that the CTTPP and EVFTA came into force from 2019 and 2020, paving the way for trade activities between Vietnam and the EU, and six partner countries of the CTTPP. EVFTA eliminated nearly 99% of customs duties between the two parties with an eight-year roadmap while CTTPP committed to cut 97% - 100% taxes for Vietnamese goods, depending on each partner with a 16-year roadmap (Table 4). The difference in RCEP is the rules of origin as main partners of Vietnam such as China, South Korea and ASEAN that import raw materials and export goods to RCEP member countries can meet the rules more easily. Therefore, FTAs would serve as an incentive to Vietnam's industries, and the elimination of tariffs will benefit key export industries including mobile phone manufacturing and other electronic products, textiles, footwear, agricultural products (rice and coffee) and fisheries (catfish and shrimp).

Table 4. EVFTA & CTTPP – Tariff lifting roadmap

	Products	Current tariff	Tariff cut schedule
EVFTA	Footwear	8%	0 - 8Y
	Textile	12%	0 - 6Y
	Fisheries	8% (catfish) & 20% (shrimp)	4Y (catfish); Immediate (shrimps)
	Coffee	0% (unroasted); 7.5% (roasted)	Immediate
	Timber	0% (interior); 7% (wooden planks)	6Y
CTTPP	Coffee		Immediate except for Mexico (5-10Y)
	Textile		0 - 4Y (Canada), Immediate (Japan), 16Y (Mexico)
	Timber		Immediate except for Japan (15Y)
	Fisheries		Immediate (Canada, Japan), 3Y(Mexico)
	Footwear		Immediate (Canada), 0-16Y (Japan)

Source: KB Securities Vietnam

FDI inflows in 2021 should be more positive thanks to new FTAs and recoveries in manufacturing activities

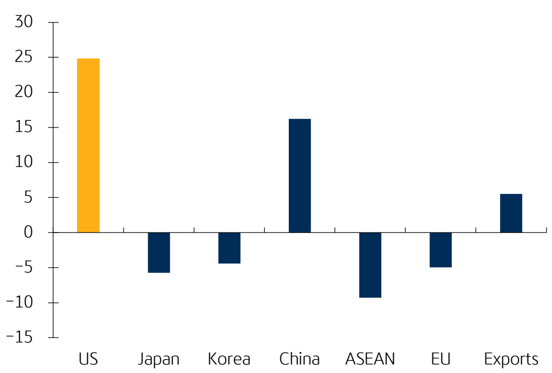
Vietnam expects to attract more FDI inflows despite the fierce competition from ASEAN countries and India. The newly effective CTTPP and EVFTA together with RCEP (coming in to effect from 2H21) gives Vietnam a free-trade advantage over major trading partners. In addition, good control of the Coronavirus pandemic also helps to make a difference between Vietnam and other countries in the region. In 2020, although the travel restriction caused the investment plan to Vietnam to be postponed, the total newly registered FDI in 2020 only slowed by 12.5% YoY and disbursed FDI down by only 2% YoY. This makes the prospect of FDI inflows for 2021 more positive.

On the other hand, we assess the possibility of additional taxation from the US Department of Commerce after investigating Vietnam's trade and the risk of a credit rating downgrade as two risk factors affecting Vietnam's economic growth in the next period:

The risk of being imposed additional taxes full taxes after Vietnam was designated as a currency manipulator

The US Department of Commerce has completed a hearing on a trade investigation under Section 301 of the Commerce Act 1974 regarding the import and use of harvested timber and Vietnam's behavior to undervalue money, adversely affecting the US trade by the end of December 2020. In addition, the move to accuse Vietnam of manipulating money from the US Treasury shows that it is more likely that Vietnam will be subject to additional taxes, or in a worse scenario, full tariffs on goods exports to the US, which is similar to China's case in 2018. The Trump administration will have about two weeks to make a decision whether to impose tariffs on Vietnam before transferring power to the new president. In the worst case, the immediate impact would be on export performance. The US is Vietnam's largest export partner and the rapid growth in exports to the US over the past two years was one of the main drivers of GDP growth during this period.

Fig 19. Vietnam – Export growth to major markets (%)



Source: Vietnam Customs, KB Securities Vietnam

Fig 20. Vietnam – Public debt targets

	2019	2020	2021	2021*	Annual Target
Public debt/GDP	55	56.8	58.6	46.1	< 65%
Government debt/GDP	48	50.8	53.2	41.9	< 54%
External debt/GDP	47.1	47.9			< 50%
Payables/Budget collection	17.4	24.1	27.4		<25%

Source: Ministry of Finance, KB Securities Vietnam
* Reviewed GDP

The risk of credit rating downgrade caused by larger budget deficit and limited ability to solve public loans

Easing fiscal policy in 2020 to cushion the economy against the COVID-19 pandemic caused the budget deficit to rise from 3.4% of GDP in 2019 to 4.2% of GDP in 2020. Repayment obligations vs state budget collection by 2020 was 24% and may exceed 25% of GDP target set by the National Assembly in 2021. In addition, to continue to support economic recovery and pay old loans, it is forecasted that the budget deficit and public debt of Vietnam will remain high in 2021 at 4% and 58 of GDP respectively (for unreviewed GDP). This will increase the risk of a credit rating downgrade, as in December 2019 Moody's lowered Vietnam's outlook to negative with a potential risk of late payment of indirect debt obligations of the Government.

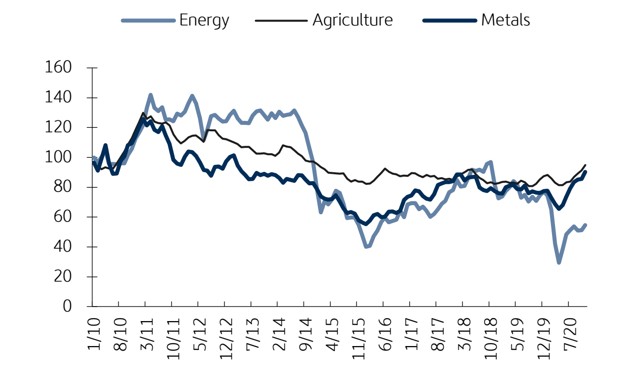
❖ 2021E inflation rate

We project inflation rate in 2021 at 3.6%, with the risk of higher commodity prices and the lag of expansionary monetary-fiscal policy.

Commodity prices, including agricultural and pump prices, are likely to rise as the global economy recovers from COVID-19

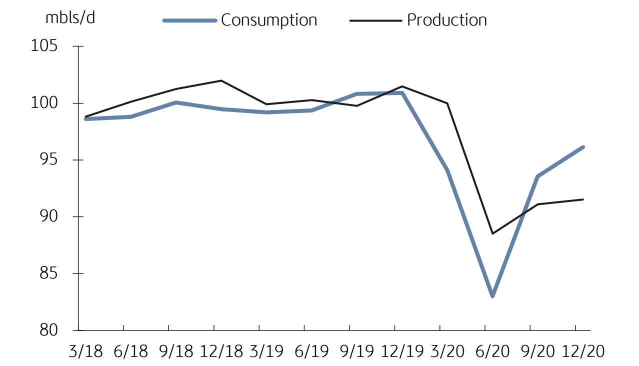
The COVID-19 pandemic changed the supply-demand balance of raw goods in 2020 and made commodity prices plummet. However, commodity prices have strongly recovered since 2H20 (Figure 21), mainly thanks to China's economic strategies. China has boosted importing energy and metals (due to increased investment in infrastructure) and agricultural commodities (to ensure food security). However, if compared with the volatility of food prices in 2011, the price increase in 2H20 is not a concern. In addition, the overall food supply is expected to be sufficient in 2021 as the ratio of total stock to demand has averaged nearly 30% since 2015, up from less than 20% in 2011. Therefore, the World Bank's food price index should gain only 1.5% by 2021 and the impact on inflation in 2021 will need to be followed further, but not as worrying as it was in 2011. The positive point in 2021 is that the prices of pork will no longer spike as it did as the supply has been improved. The government prioritized increasing domestic pork production, after the outbreak of African swine fever. It is estimated that the output of live-weight pork for the whole 2020 will increase 4.4% YoY and maintain the trend until the next year.

Fig 21. Global – Commodity price index (2010=100) (point)



Source: World Bank, KB Securities Vietnam

Fig 22. Global – Demand & supply of crude oil (mn bpd)



Source: International Energy Agency, World Bank, KB Securities Vietnam

Falling inventories lead to a 17% increase in crude oil prices compared to 2020

We expect the oil inventories would be lower in 2021 as demand continues to recover and supply cut agreement of OPEC+ is effective until the end of the year on hopes that the vaccine will be widely distributed in 2H21. Brent oil prices forecast by EIA average USD48.5 per barrel in 2021, up 17% YoY.

Roadmap for raising public service prices has not been updated for 2021

The Government continues to push back the roadmap for price increases of public services in 2021 when the National Assembly approved the Resolution on the State Budget, which decided not to increase base salary for civil servants and officials in 2021. Therefore, prices of health services will not be adjusted. In addition, the roadmap for increasing tuition fees under Decree No. 86/2015 / ND-CP will also end in 2020 and we have not noted the next move by the Government in the 2021-2022 school year. However, with the maintenance of expansionary fiscal and monetary policy in 2020 and 2021, policy lags will put pressure on inflation.

Table 5. Vietnam – Average CPI in 2021E

	Groups	Weights (%)	+/- (%)	Contribution to overall CPI (%)
1	Food and foodstuff			
	Grains	4.46	6	0.27
	Foodstuff	22.60	3	0.68
	Outdoor eating	9.06	7	0.63
2	Beverages and tobacco	3.59	2	0.07
3	Clothing and footwear	6.37	1.5	0.10
4	Housing, water, electricity, gas and other fuels	15.73	5	0.79
5	Furniture, household equipment and maintenance	7.31	1.5	0.11
6	Health	5.04	3	0.15
7	Transport	9.37	5	0.47
8	Communication	2.89	-0.5	-0.01
9	Education	5.99	3	0.18
10	Entertainment	4.29	1	0.04
11	Miscellaneous goods and services	3.30	3	0.10
Total				3.57

Source: KB Securities Vietnam

* Weights calculated for CPI basket in 2021 have changed. We do not have official information from the General Statistics Office, so we still use the weights for the 2016-2020 period

❖ 2021E interest rates

Monetary policy remains loosened, similar to the trend of other major central banks

We believe that the easing monetary policy would be maintained in 2021 to continue supporting businesses and households reeling from the pandemic. It is likely that the State Bank will lower the policy rate again in 1H21 when the consumer price pressure is not too large. M2 growth will increase slightly compared to 2020, expected to reach 14% and be within the average range from 2018. This growth is considered to be enough to be able to provide a large amount of money into the economy (about VND1.5 million) and not put pressure on asset price bubbles. However, the disadvantage in 2021 is that the tools to pump VND through buying foreign currencies are limited. In case of a temporary shortage of liquidity, the SBV will likely to extend the expiry date on OMOs (current term is seven days).

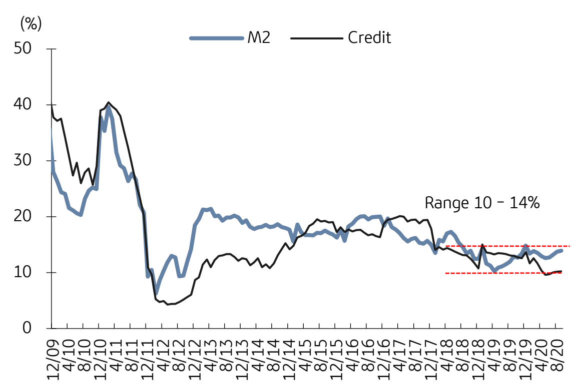
Credit growth should be around 12-14% in 2021

We expect credit growth to continue its recovery momentum in 2021, with an increase of 12-14%, given observing indicators such as the IIP and PMI showed that production activities are gradually recovering amid low lending interest rates maintained for many years thanks to the policy orientation of the State Bank. Credit growth should rebound rapidly in 2H21 if the COVID-19 vaccine is widely distributed across many countries to facilitate manufacturing recovery.

The interest rate level may bottom out in 2020 and 1H21

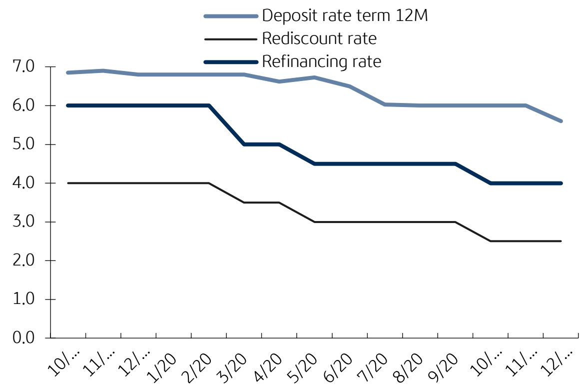
Up to now, the interbank interest rates and the government bond yields have hit the bottom while the deposit interest rates hit 15-year lows. We forecast that the interest rate level will likely bottom out in 1H21 when the State Bank lowers the policy rate one more time and raise it again in 2H21 when: 1) The tools to buy foreign currency are limited and may push up the interest rate level on the market 2; 2) Credit growth in the second half of the year will usually recover rapidly; and 3) The roadmap to tighten the short-term deposit ratio for medium and long-term loans effective in October 2021 will boost the competitiveness of deposits and reverse the trend of declining deposit rates.

Fig 23. Vietnam – M2 and credit growth (%)



Source: State Bank, KB Securities Vietnam

Fig 24. Vietnam – Call and policy rates (%)



Source: State Bank, KB Securities Vietnam

❖ 2021E exchange rates

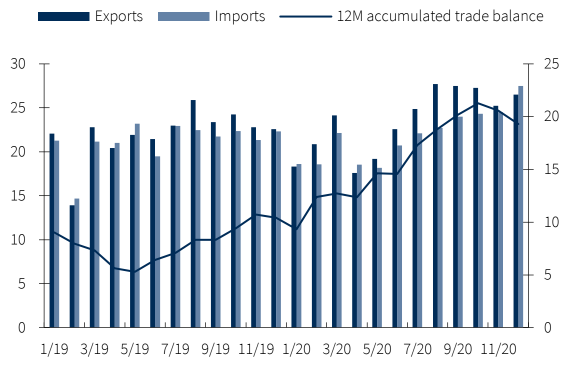
USD/VND exchange rate in 2021 is forecast to decrease slightly

The scenario of VND will appreciate 0.5 – 1% in 2021 – given positive foreign currency supply and USD depreciation along with efforts of the State Bank to remove the label of currency manipulation.

Foreign currency supply should remain positive

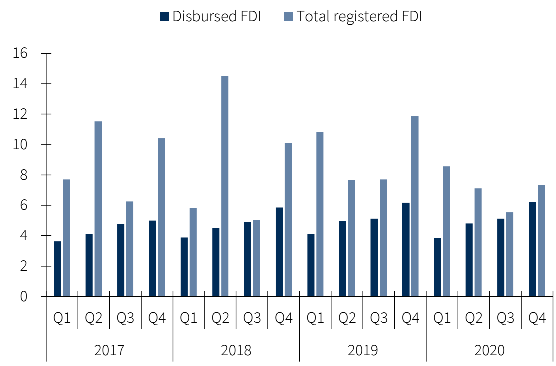
The supply of foreign currency is expected to remain abundant in 2021, when import-export activities and FDI inflows strongly run into Vietnam. The IMF forecasts global trade volumes will increase by around 8% in 2021 and with a growing share of global exports, Vietnam will certainly benefit from the recovery of global trade. FDI disbursement should be positive thanks to the relocation of manufacturing bases and the effectiveness of COVID-19 vaccine.

Fig 25. Vietnam – Trade balance (USDbn)



Source: Vietnam Customs, KB Securities Vietnam

Fig 26. Vietnam – Disbursed and registered FDI (USDbn)



Source: Vietnam Customs, KB Securities Vietnam

The trend of the USD is more inclined to the downside in 2021

The trend of the USD is more inclined to the downside in 2021 thanks to the following signals:

1) The COVID-19 vaccine optimism helps investors shift their attention to risky assets, instead of a haven currency like the US dollar, which causes the demand for USD to fall;

2) The transition of US Government in early 2021 with the takeover of the Democratic administration will increase the likelihood of sustaining expansionary monetary and fiscal policy in the US;

3) The Fed's dovish stance, at least until the end of 2021 and the Fed's shift to medium-inflation targeting means: (a) real interest rates remain negative; (b) steeper yield curve; and (c) a weaker dollar.

VND is under upward pressure from the allegation of "currency manipulation" of the US

The VND will continue to be under appreciation pressure in 2021 as Vietnam still violates all three criteria in May 2021 review period (Table 6). Thus, unless Vietnam negotiates successfully with the US Treasury, the label of currency manipulator would remain. Meanwhile, the State Bank's moves to change the foreign exchange management policy showed that it has been and will no longer actively intervene in the one-way foreign exchange market, and the VND will be regulated according to the supply-demand of the market.

Table 6. Vietnam – Criteria to assess the currency manipulation in 2020

	Goods trade balance with US		Current account		Net FX intervention	
	USD billion	% GDP	USD billion	% GDP	USD billion	Net FX purchase (6 out of 12 months)
Four quarters till 4Q2020*	90.1	33.3%	11	4%	15	Yes
Criteria	20.0			2.0		Yes

Source: KB Securities Vietnam

* Evaluation criteria for the May 2021 evaluation period (from 1Q20 to 4Q20)

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Investment ratings & definitions

Investment Ratings for Stocks
(based on expectations for absolute price gains over the next 6 months)

Buy:	Hold:	Sell:
+15% or more	+15% to -15%	-15% or more

Investment Ratings for Sectors
(based on expectations for absolute price gains over the next 6 months)

Positive:	Neutral:	Negative:
Outperform the market	Perform in line with the market	Underperform the market