KB Securities VIETNAM

2H2020 Macro Outlook

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August 7, 2020

Vietnam's 1H20 GDP growth hit the lowest on record since the General Statistics Office started tracking the data. However, the positive growth in 2Q was still appreciated albeit April's nationwide lockdown and COVID-19's strong influence on most economic sectors. This was achieved thanks to the Government's drastic measures in fighting against Coronavirus and loosening monetary and fiscal policies to boost the economy but well control inflation and maintain stable foreign exchange rates.

KBSV's forecast about some key macro indexes in the 2H20:

1) 2020E GDP growth at 3.0% given recoveries in domestic consumption and public disbursement. Production activities are also expected to have bottomed out in April and May and are currently rebounding;

2) Average CPI at 4.0% for the whole 2020E, which is under the inflation target set by the Government;

3) Eased but controlled monetary policies, with money and credit supply of 12% and 10% respectively, to keep USD/VND exchange rate stable at VND23,500 until the end of the year, and keep VND devaluation at a modest decrease of 1.5% compared to the beginning of the year.

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Executive Summary

Vietnam economy has shown signs of recovery since the April nationwide lockdown. We believe these signs would be clearer in the latter half of 2020 thanks to the Government's economic stimulus. Three main growth forces of the economy include rebounding domestic consumption, accelerated public investment and FDI attraction.

Although economic recovery is the first priority, the Government also launched cautious monetary policies to stabilize exchange rates and inflation. Given some external favorable factors, we expect that these two indicators will be under control in the second half of the year.

Table 1. Vietnam – 2020E key macro indicators

			KBSV forecast	
	Unit	1H2020	Old	New
GDP growth	% YoY	1.81	4.5	3.0
Headline CPI	% YoY	4.19	3.5	4.0
Credit growth	% YTD	2.45*	13.0	10.0
M2 growth	% YTD	4.59*	13.0	12.0
Policy rate (refinancing rate)	%/year	4.5	4.5	4.5
USD/VND	VND	23,196	23,750	23,500

Note: *Data as of June 19, 2020
Source: KB Securities Vietnam

GDP growth

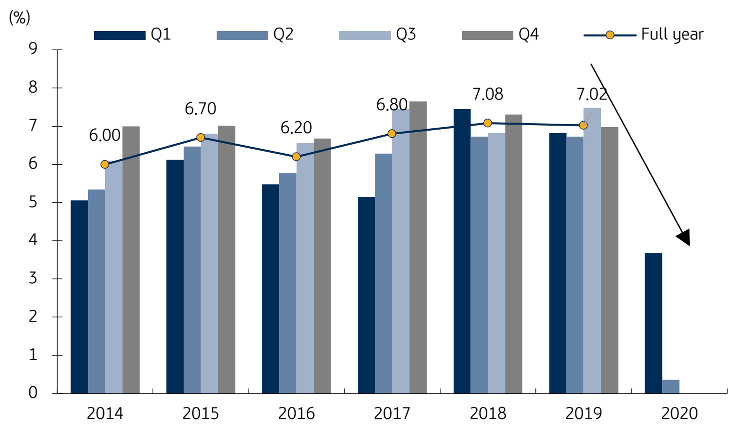
❖ 1H20 GDP growth

1H20 GDP growth hit 30-year lows under the impacts of COVID-19

According to Vietnam General Statistics Office (GSO), Vietnam GDP in the first six months of 2020 rose by a mere of 1.81% YoY, the lowest growth rate on record. On a quarterly basis, 1Q and 2Q growth gained only 3.68% and 0.36% YoY, respectively, much lower than the figure of 6.7% in the same period of 2019 (Figure 1). However, Vietnam has maintained a positive GDP growth in 2Q, which is an encouraging result and attributable to the bounce back in agriculture, manufacturing and retails in June.

2Q GDP growth of most sectors hit hard by COVID-19

Fig 1. Vietnam – Quarterly GDP growth (% YoY)



Source: General Statistics Office, KB Securities Vietnam

On the demand side, COVID-19 hit hard on both consumption and investment, especially from the private sector and FDI in 1H20:

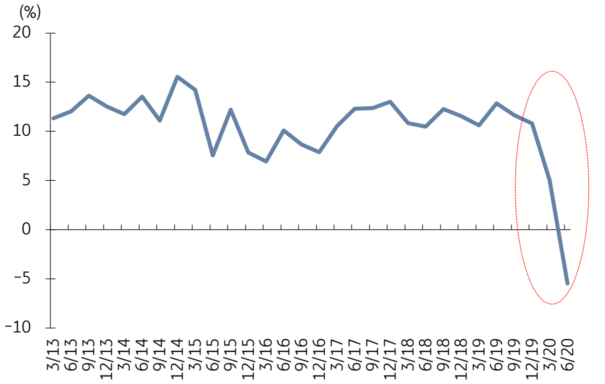
1H20 consumption fell hard from declining consumption during the lockdown

- Consumption in 1H20 posted a modest rise by 0.69% YoY, much lower than the average increase of 7.4% from 2015 to 2019. Remarkably, the nationwide lockdown in April and international flight suspension made 2Q consumption grow by only 0.04% YoY, in line with the 4.6% decline in retailing and service sales (Figure 2).

1H total investment reached the lowest in the last 10 years despite the increase in State investment

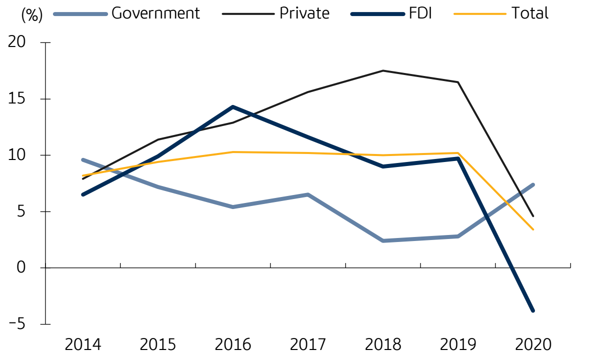
- 1H total social investment hit 10-year lows due to the plunge in investment from private & FDI sectors despite the support from the State sector (Figure 3). Realized capital under the State budget reached the highest in 2016-2020, which bodes well for the public disbursement. Meanwhile, FDI inflows witnessed the deceleration for the first time by 3.8%, and capital from private sector also slowed to 4.6% from 16.5% in 2019.

Fig 2. Vietnam – Retail & service growth (% YoY)



Source: General Statistics Office, KB Securities Vietnam

Fig 3. Vietnam – 1H social investment growth (% YoY)



Source: General Statistics Office, KB Securities Vietnam

On the supply side, COVID-19 hit the service sector the hardest, while industrial and construction sectors were the bright spots:

Service sector was hit the hardest by the Coronavirus

- The service sector inched 0.6% in the first six months (down by 1.8% YoY in 2Q alone due to the social lockdown and border restriction). International tourist traffic to Vietnam fell 55.8% YoY (down 98.6% in 2Q), which hindered the growth of hospitality and catering (down 20.7%), transportation, and warehouse services (down 3.0%).

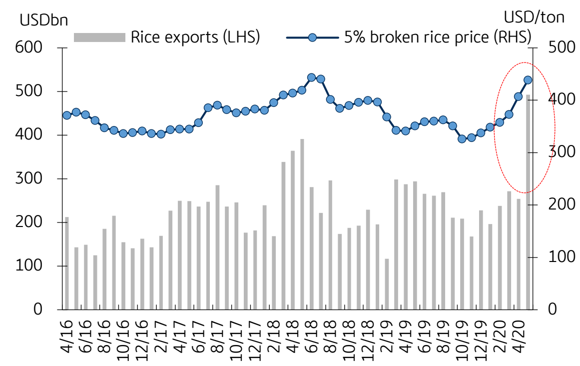
Agriculture, forestry and fishery now make up almost 18% of overall GDP after 2Q's growing contribution

- Agriculture, forestry and fishery grew by 1.2% in 1H (up 1.7% in 2Q alone). Most noteworthy was the significant boost in contribution to overall GDP growth, with the agriculture, forestry and fishery industry sharply increasing to 17.7% of GDP in Q2 from 1Q's 10.1%. Agriculture, in particular, grew by 1.7% YoY in 2Q compared with the 1.2% decrease seen in 1Q. Although the rice output harvested in the winter-spring season was down 3.2% YoY, most of the gains in agriculture can be attributed to rising global food demand, with prices for rice and rice export values at multi-year highs (export prices for 5% broken rice are now the highest in eight years and rice exports reached USD1.03 billion in 2Q or a 22% YoY jump).

The manufacturing industry continues to be the driving force behind GDP growth

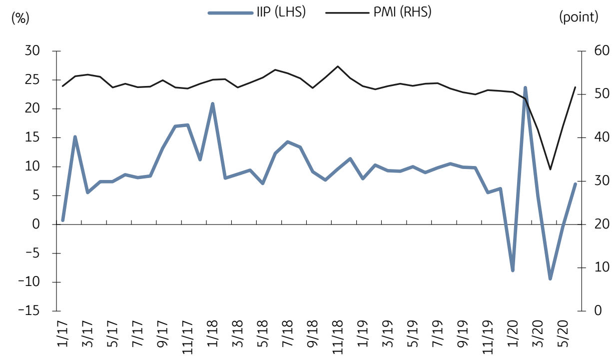
- 1H industry and construction sector gained 3.0% (up 1.4% in 2Q). This performance mainly came from the manufacturing sector that grew by 7.1% in 1Q and 3.2% in 2Q as well as contributing 1.1 percentage points to Vietnam's overall 1H GDP growth. Electronics manufacturing continued to be the forefront in 1H, with the shift to electronics, computers and components (exports for these items rose by 24.2% YoY) from only smart phones like before. Moreover, the pickup in disbursements for public investments in 1H also helped increase the output in raw materials for the construction industry, such as cement (+4% YoY); and steel bars/shaped steel (+12.8% YoY).

Fig 4. Vietnam – Exported prices for 5% broken rice & rice export (USDbn, USD/ton)



Source: General Statistics Office, World Bank, KB Securities Vietnam

Fig 5. Vietnam – IIP & PMI (% YoY, points)



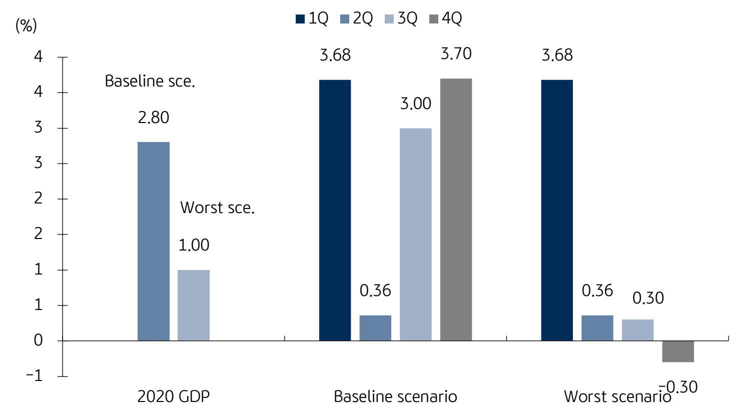
Source: General Statistics Office, World Bank, KB Securities Vietnam

❖ 2020E GDP growth forecast

Lowering 2020E GDP growth forecast to 3.0%

We lower our 2020E GDP growth forecast to 3.0% from 4.5% after reflecting 1H's slowdown due to COVID-19 impacts on Vietnam economy and trade partners. We continue to expect three main drivers to support Vietnam's growth, including: 1) recovery in domestic demand; 2) FDI attraction; and 3) accelerated public investments for the remaining six months of the year.

Fig 6. Vietnam – 2H GDP growth forecast (% YoY)



Source: KB Securities Vietnam

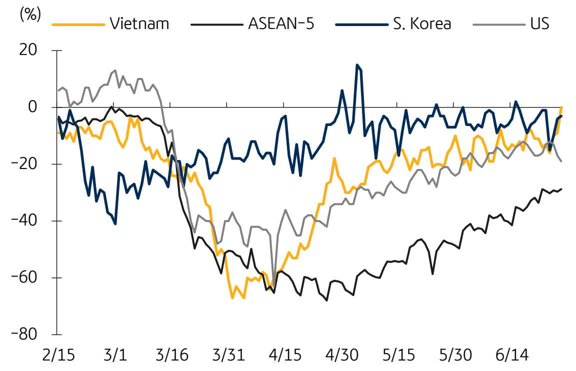
Domestic demand is expected to be the growth force in the next six months of the year

- Vietnam's successful containment of Coronavirus and early lifting lockdown protocols played a key role in boosting domestic consumption. A Google survey showed the mobility for consumption, entertainment, and tourism in Vietnam has bounced back almost near the pre-COVID period (Figure 7). 1Q consumer confidence index maintained high at 126 points, up 1 point vs 4Q19. PMI of the manufacturing sector also rose from May thanks to consumer goods production. We believe these factors would facilitate quick rebound in domestic purchasing power in the near future.

Vietnam expects to attract more FDI flows in 2H20 thanks to the EVFTA and recovered business operations

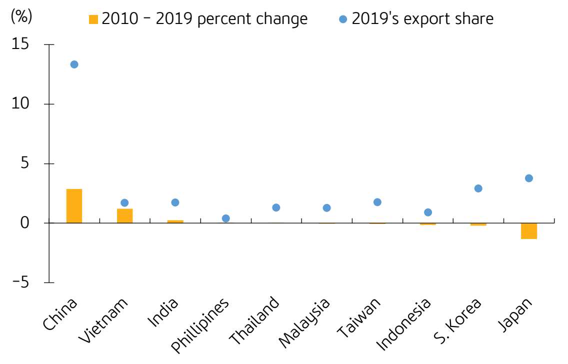
- FDI inflows are expected to achieve impressive progress despite competitive pressure from the ASEAN and India. The newly effective EVFTA from August 1 would create free trade advantages for Vietnam in the EU market, and the good control of COVID-19 would make a big difference between Vietnam and other regional countries. In addition, Vietnam is increasingly gaining share in global exports (Figure 8), which further strengthens its position as the leading manufacturing center in Southeast Asia, thereby attracting larger FDI inflows from China's old partners.

Fig 7. Vietnam – Mobility for shopping and entertainment (%)



Source: Google Mobility, KB Securities Vietnam

Fig 8. Asian countries – Percent of world exports (%)

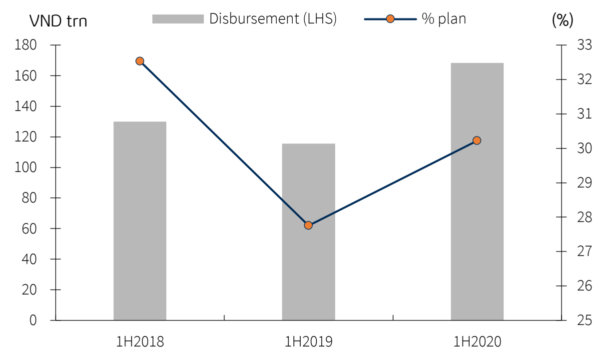


Source: International Trade Centre, KB Securities Vietnam

Public disbursement, especially the North-South highspeed railway project should be the focus in the last six months of the year

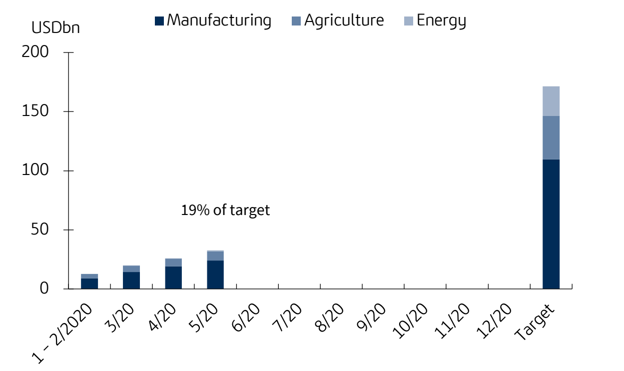
- We expect the disbursement of public investment would be expedited in the 2H of the year. Although 1H disbursed capital only completed 28.94% of full-year plan, this was still a high figure in the last three years (Figure 9). For the 2H20, the Government should accelerate public disbursement with more drastic movements, especially with the North-South highspeed railway. Six out of 11 sub-projects of the railway project were changed from public-private partnership to public investment to be quickly started by 3Q20 instead of 2021 or 2022 as previously planned. In general, this will be an important driving force to boost GDP growth this year, as the Ministry of Planning and Investment forecast if the public disbursement gain 1%, GDP growth will inch by 0.06 percentage points. Thus, if the public disbursement reaches 100% of the 2020E plan (equals to VND700 trillion in capital), GDP will gain 0.42 percentage points.

Fig 9. Vietnam – 1H public disbursement (VND trillion, %)



Source: Ministry of Finance, KB Securities Vietnam

Fig 10. China's progress in importing U.S products



Source: Bloomberg, KB Securities Vietnam

Unpredictable COVID-19 and US-China trade tensions would be the two main Vietnam's economic drivers for the rest of the year:

Falling demand in big export markets and the suspension of international flights are the two obstacles to manufacturing and services in 2H20

- The outbreak beat Vietnam 1H manufacturing sector indirectly through the lack of input materials from China in 1Q, and falling consumption demand in major export markets like the US and EU. This sector would be one of the main risks to 2H GDP growth albeit partly recovered in June, the demand from export markets kept plunging amid complicated developments of Coronavirus. In addition, the suspension of international flights lasting until September would create a sharp decline in revenue from foreign visitors which accounted for 13% of total 2019 GDP.

US-China trade tensions maintained as an unforeseeable driver to Vietnam economic growth

- China's Government have made efforts to tame the tensions with the US by opening its bank card market (with Mastercard's join) and stocking up U.S agricultural products, but the imported volumes were much lower than committed due to the outbreak (Figure 10). Plus, there are so many conflicts such as the US accusation against China for the COVID-19 outbreak and warning to impose sanctions on China for passing cybersecurity laws in Hong Kong made the Sino-US tensions an unpredictable challenge to Vietnam exports in the latter half of the year.

Inflation

❖ 1H20 inflation

Average 1H CPI was still high, but tended to do down

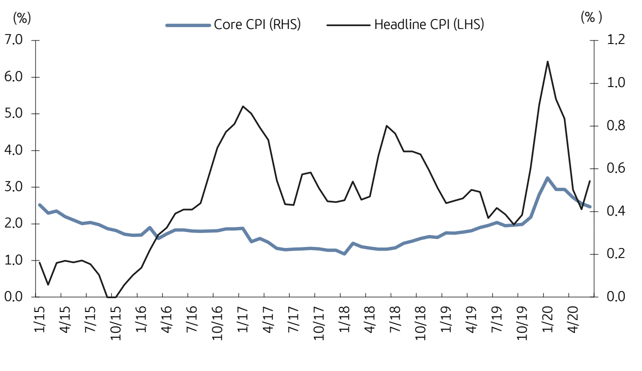
GSO data estimated **average 1H CPI to rise 4.19% YoY, the highest increase in the last three years**, mainly due to the relatively low 2019 base (Figure 11). The good news is that the average CPI in 2Q (2.83%) was just a half of 1Q's (5.56%). Core inflation also tended to decrease, but at a slower pace. The average core inflation in 1H reached 2.82%, of which 1Q and 2Q shares were 3.05% and 2.58% respectively.

The surge in pork prices and the plunge in petrol prices were the two factors affecting six-month CPI

In the first 6 months of 2020, the main factors affecting CPI include:

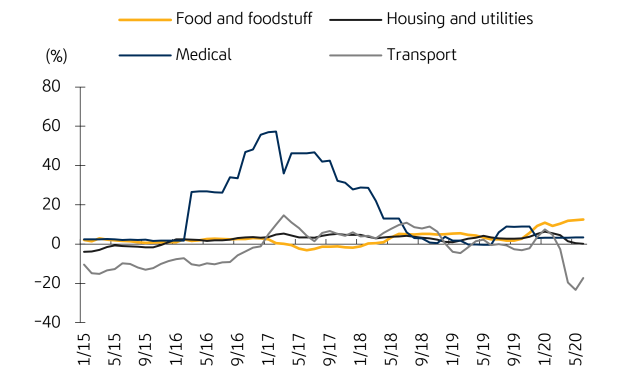
1) Foodstuff prices up 14.28% YoY, mainly due to the 68.2% YoY surge in pork prices, causing headline CPI to increase by 2.86%;
2) Food group increase attributable to the rise in export rice prices, making headline CPI inch 0.15%;
3) Transport group price down by 9.26% owing to a sharp decrease of 19.49% in gasoline prices, helping to lower headline CPI by 0.81%.

Fig 11. Vietnam – Core and headline inflation



Source: General Statistics Office, KB Securities Vietnam

Fig 12. Vietnam – CPI of key sectors (% YoY)



Source: General Statistics Office, KB Securities Vietnam

❖ 2020E inflation forecast

2020E CPI is estimated to reach 3.9-4.0%

We raised our inflation forecast for 2020E to nearly 4.0% from 3.5% previously given hard-to-control pork prices recently despite favorable factors like gasoline and government-administrated service prices:

Pork prices remained a potential risk to 2H CPI

- Pork price movement may be the most unpredictable risk to inflation rate in 2H20. Although pork price base in 4Q19 were high, and the Government prioritized importing living hogs and breeding pigs from Thailand to curb domestic pork prices, we suppose that 2H pork prices should be not lower than VND80,000 per kilogram due to serious supply constraints. Ongoing African swine fever in June would hinder the repopulation in the upcoming period and imports from Thailand have not met domestic demand and not much lower than domestic live-weight hog prices (estimated pork price from Thailand is more than VND80,000 per kilogram).

Petrol prices are far lower than the same period in 2019

- While crude oil prices are quite unforeseeable due to their close relation with politic issues, we maintain our forecast that 2H petrol prices would be lower than the same period last year thanks to: 1) low global crude prices, equal to only two-thirds of the same period, and further declining demand from COVID-19; and 2) abundant Gasoline stabilization fund (VND6,000 billion), raising the possibility for the Government to interfere in oil and gas prices when the world oil prices bounced back sharply.

2H government-administrated service prices would not increase as strongly as in previous year

- Government-administrated service prices including healthcare is not a worrisome factor to inflation in the latter half of 2020 as the Government's postpone of a regular basis salary increase would help remove the increasing pressure. Additionally, given amplifying inflation, the Government would also call for multi-ministry coordination in order not to raise prices of State service in the last six months of the year.

Table 1. 2020E CPI estimates

No.	Groups	Weights (%)	+/- (%)	Contribution to overall CPI (%)
1	Food and foodstuff			
	Grains	4.46	3.00	0.13
	Foodstuff	22.60	12.00	2.71
	Outdoor eating	9.06	7.00	0.63
2	Beverages and tobacco	3.59	1.00	0.04
3	Clothing and footwear	6.37	1.00	0.06
4	Housing, water, electricity, gas and other fuels	15.73	3.00	0.47
5	Furniture, household equipment and maintenance	7.31	1.00	0.07
6	Health	5.04	3.00	0.15
7	Transport	9.37	-7.00	-0.66
8	Communication	2.89	-0.50	-0.01
9	Education	5.99	4.50	0.27
10	Entertainment	4.29	-0.50	-0.02
11	Miscellaneous goods and services	3.30	3.00	0.10
Total				3.95

Source: KB Securities Services

Interest rates

❖ 1H20 interest rates

Table 2. Vietnam – Demand & Supply on the money market

(VNDbn)	31/3/2019	30/6/2019	30/9/2019	31/12/2019	30/3/2020	19/6/2020
M2	9,478,157	9,866,810	10,083,289	10,573,725	10,755,572	11,059,059
Growth rate YTD (%)	2.89	7.11	9.46	14.78	1.72	4.59
Growth rate QoQ (%)	2.89	4.10	2.19	4.86	1.72	2.82
Increase in M2 amount by quarters	266,309	388,653	216,478	490,436	181,847	303,487
Credit outstanding balance	7,437,086	7,742,083	7,888,910	8,195,393	8,302,412	8,396,180
Growth rate YTD (%)	3.13	7.36	9.40	13.65	1.31	2.45
Growth rate QoQ (%)	3.13	4.10	1.90	3.88	1.31	1.13
Increase in lending amount by quarters	225,911	304,997	146,827	306,483	107,019	93,768
Annual gap bt. M2 and lending growth	40,398	124,054	193,706	377,659	74,828	284,547
Quarterly gap bt. M2 and lending growth	40,398	83,656	69,651	183,953	74,828	209,719

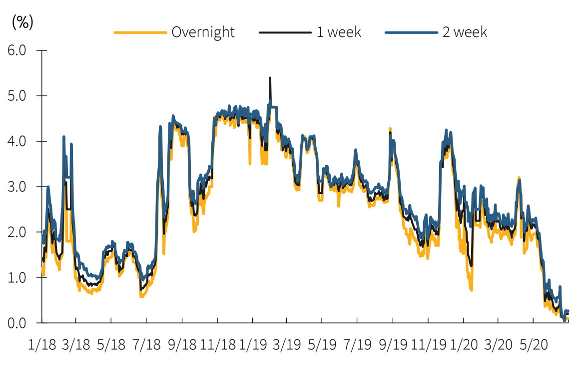
Source: State Bank, KB Securities Vietnam

Excess liquidity pushed interbank interest rates and Treasury bond yields down to many years' bottom

System liquidity in the first six months was ample with the widening difference between credit and M2 (Table 2). This was mainly due to sagging credit demand and businesses' shrinking operations after Coronavirus outbreak.

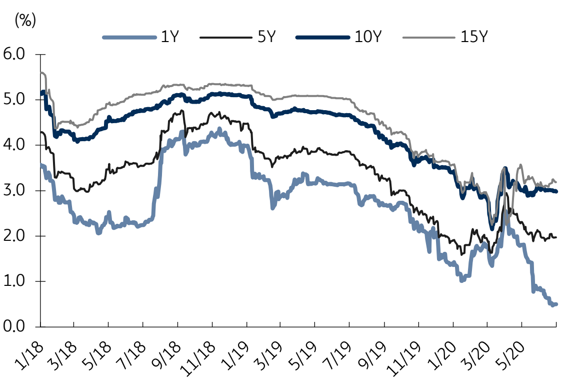
Credit growth as of June 19 was only 2.45% YTD, much lower than 7% over the same period in 2019 while M2 growth was 4.59% YTD. Ample liquidity has brought the interbank interest rates and government bond yield to the lowest level ever (Figures 13, 14).

Fig 13. Vietnam – Interbank interest rates (%)



Source: State Bank, KB Securities Vietnam

Fig 14. Vietnam – Government bond yield (%)



Source: General Statistics Office, KB Securities Vietnam

Easing but well-controlled monetary policies

The State Bank (SBV) lowered policy rates twice in March and May (refinancing rates down 100 bps in total), and cut short-term deposit rate cap and lending rates in priority sectors. In addition, SBV asked commercial banks to support businesses facing liquidity strains by reducing interest rates and rescheduling & restructuring debts. Overall, SBV's monetary policies to cope with the pandemic are not many as compared to other countries in the region (Table 3) and mainly asking supports from commercial banks, hence weaker impacts on money supply than other regional peers. We assess that these policies are relatively appropriate to Vietnam's economic status, which are easing but still under control to avert negative consequences such as inflation, delinquencies and asset price bubbles (such as real estates) as in 2009-2011.

Table 3. Southeast Asian countries – Measures to fight against the COVID-19

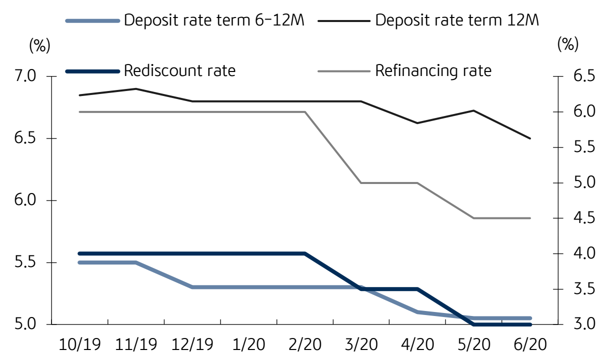
	Monetary response	Fiscal response
Vietnam	Cut policy rates by 100bps	3.6% GDP
	Ask commercial banks to support COVID-19 impacted businesses	
Singapore	Adopt a zero percent annual rate of appreciation of the policy band and reduced the mid-point to the prevailing level of the S$NEER	19.7% GDP
	Ask commercial banks to support COVID-19 impacted businesses	
	Establish USD 60 billion swap lines with the US Federal Reserve	
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 75bps	4.6% GDP
	Cut Reverse Required Ratio	
	Central bank purchases of government bonds	
Malaysia	Cut policy rate by 75 bps	4.3% GDP
	Cut Reverse Required Ratio	
	Liquidity supports worth of 1.3% GDP	

Source: IMF, KB Securities Services

Deposit and lending rates tended to decrease significantly

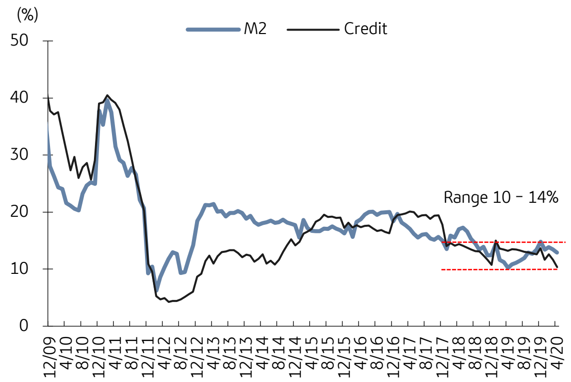
Commercial banks' efforts to offset the reduction in earnings after lending rate cuts to support Covid-19 affected customers pushed deposit rates for terms of over six months down sharply in late 2Q. Long-term deposit rates over six months have dropped by about 50 bps since early this year at most commercial banks amid ample liquidity. Lending interest rates also tended to decrease slightly to support the economy and stayed at 10-year lows.

Fig 15. Vietnam – Average deposit rates (%)



Source: State Bank, KB Securities Vietnam

Fig 3. Vietnam – Credit and M2 growth (% YoY)



Source: State Bank, KB Securities Vietnam

❖ 2020E interest rate forecast

Credit growth in 2020E would be around 10%

We expect credit growth to recover in 2H20 given recovering business operations and low lending rate environment thanks to the SBV's policies. However, credit demand can hardly go back to the normal state before the outbreak, while the risk appetite in large banks became more cautious, reflected in their recently announced business guidance. As a result, we lower our 2020E credit growth forecast from 13% to 10%.

Deposit rates should post modest gains in 2H20 given rebounding credit growth

We believe there are low possibility that the SBV would lower the policy rate one more time for the rest of the year, when inflation pressure is still relatively high and the domestic economic activities has gradually healed. In our baseline scenario, we forecast deposit rates to rise slightly in 2H20 due to: 1) rebounding credit growth; and 2) the roadmap to tighten the short-term deposit ratio used for medium and long-term loans (effective from October 2020), which may raise deposit rate competition and reverse the trend of declining deposit rates.

Exchange rates

❖ 1H20 USD/VND exchange rates

Stable exchange rates in 1H20

The USD/VND exchange rate maintained a stable downtrend throughout 2Q after two last volatile weeks of March. As of June 30, the interbank and unofficial rates inched 0.1% and 0.13% respectively vs late 2019, while the central rate increased 0.3% YTD. Compared to other currencies in the region, VND is considered as a stable currency in the first six months of the year.

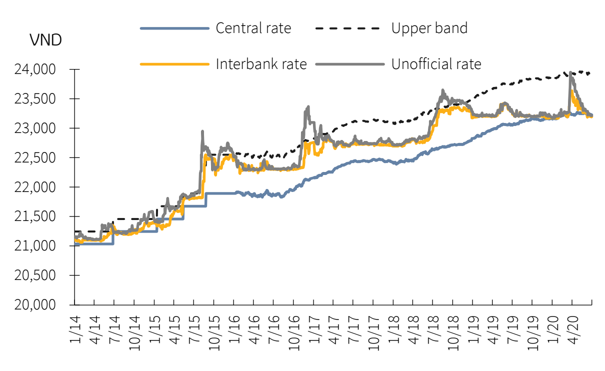
Falling NEER & REER

Similar to the interbank exchange rate movements, NEER and REER tended to went down by the end of 2Q, but are still at many-year highs. This means that the VND still appreciates significantly compared to basket of currencies, which bodes ill for export activities. Meanwhile, the gap between the interbank and the center rate narrowed at the end of 2Q, and the interbank and unofficial rates were lower than the center rate (Figure 17). Therefore, we assess that the pressure of VND devaluation is not significant.

Stabilized USD thanks to Fed's polices to support liquidity, hence stable USD/VND rates

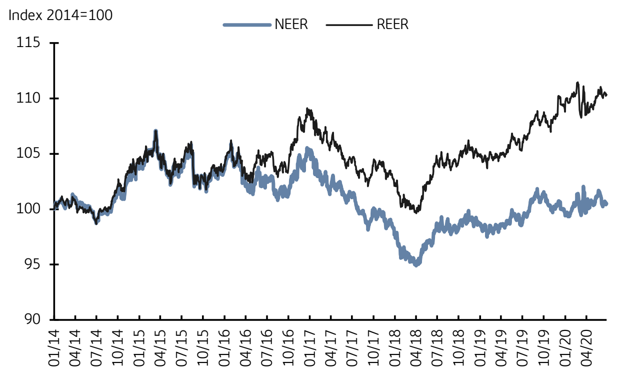
The main factor helped to stabilized 2Q USD/VND exchange rate was the stable USD. Specifically, DXY spiked 8% between March 9 and 20 when investors panicked over COVID-19 but DXY index is now almost back to the same level at the beginning of the year (~ 97 points). This was largely attributable to Fed's easing monetary policies to support the US economy, combined with proactive swap lines with central banks of Japan, UK, EU, Singapore, Korea, etc. to boost USD liquidity. These banks borrowed more than USD440 billion from the Fed's swap lines as of April, which means that the global supply of USD has been supported.

Fig 17. Vietnam – USD/VND exchange rates (%)



Source: Bloomberg, KB Securities Vietnam

Fig 18. Vietnam – NEER & REER (points)



Source: Bloomberg, KB Securities Vietnam

❖ 2020E exchange rate forecast

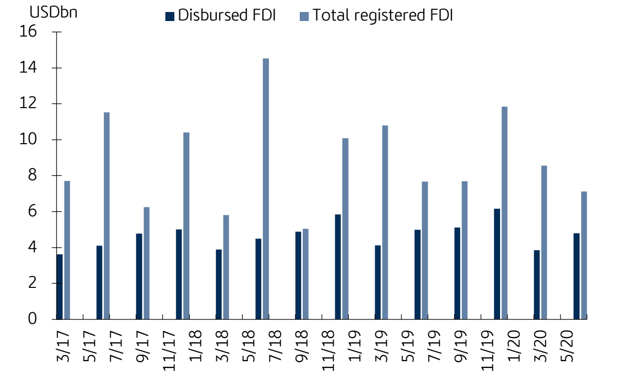
2020E VND depreciation is expected to stay at 1%

We lower the 2020E VND depreciation forecast to 1% from our previous 2.5% thanks to the improvement in USD supply:

Positive FX supply

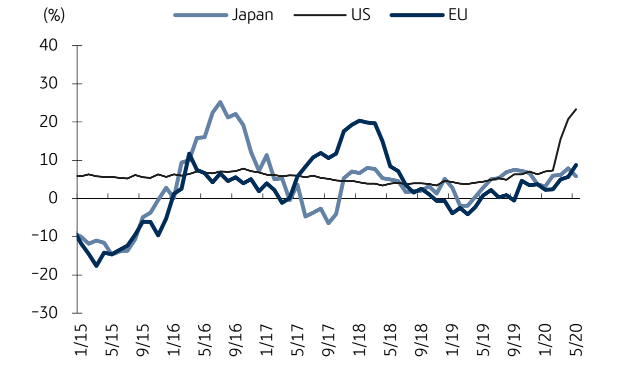
- Foreign currency supply should be abundant in 2H20 given recovery in import-export activities and strong FDI inflows. In fact, contrary to our previous concerns, Vietnam exports in the first six months was still positive, and the trade balance posted at a surplus of USD4 billion. Along with that, statistics also showed that the remittance to Ho Chi Minh City (accounting for 30% of the country's total remittances) was USD2.3 billion, down only 1.9% YoY, which was much better than fears of a sharp drop in remittances due to the outbreak.

Fig 19. Vietnam – Disbursed & registered FDI



Source: Bloomberg, KB Securities Vietnam

Fig 20. Global – Money supply of the US, Japan & EU (%)



Source: Bloomberg, KB Securities Vietnam

DXY would tend to go down in the coming time

- Two factors that favors the lower DXY in 2H 2020 include: 1) The Fed's more generous money injection compared to other countries such as Japan and the EU (Figure 20); and 2) more hopes of GDP growth in other countries given complicated COVID-19 conditions in the U.S. In contrast, there are two main factors causing DXY to increase: 1) Fed's less room to further slash interest rates; 2) US-China trade tensions; and 3) demand for USD following the global second wave of COVID-19.

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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