VIETNAM

STRONG PERFORMANCES

The Covid-19 epidemic was well controlled last year and lockdown was swiftly eased. Productive activity has rebounded vigorously since May, notably driven by a solid recovery in exports. Fiscal support measures have been moderate, primarily based on the accelerated implementation of already-planned investment projects. In the end, economic growth and macroeconomic balances were only moderately and temporarily affected in 2020. However, there remains a weak link in the economy: banks are insufficiently capitalised while corporates, especially state-owned enterprises, are excessively indebted. Some of these institutions could be severely weakened when monetary support measures come to an end in 2021.

HEALTH CRISIS CONTAINED

Vietnam posted economic growth of 2.9% in 2020, making it one of the strongest performers in the world. The Covid-19 epidemic was particularly well-managed, thanks to strict case-tracking. Lockdown measures were introduced gradually from the end of January, building up to a strict lockdown, that lasted just three weeks, in April. These restrictions were gradually phased out from the end of April, with adjustments then made in certain provinces, depending on the health situation. As a result, after it slowed to 0.4% year-on-year (y/y) in Q2 2020, real GDP growth bounced back to 2.7% in Q3 and 4.5% in Q4. Mobility indicators have now returned to close to normal levels. Yet international tourism continues to be banned.

By mid-January, Vietnam had had only 1,515 Covid-19 cases and 35 deaths for a population of 98 million. A clinical trial of a locally produced vaccine began last month, and the first delivery of European vaccines has just been announced.

FORECASTS

	2019	2020e	2021e	2022e
Real GDP growth (%)	7.0	2.9	7.0	6.9
Inflation (CPI, year average, %)	2.8	3.2	3.5	3.9
Budget balance / GDP (%)	-3.3	-6.0	-4.5	-4.0
General government debt / GDP (%)	43.4	46.9	46.9	46.4
Current account balance / GDP (%)	3.8	3.2	3.5	3.8
External debt / GDP (%)	35.6	36.3	34.4	32.0
Forex reserves (USD bn)	78.3	90.0	103.0	115.0
Forex reserves, in months of imports	3.6	4.0	4.1	4.1
Exchange rate VND/USD (year end)	23 170	23 150	23 070	23 000

TABLE 1

e: ESTIMATE & FORECASTS
SOURCE: BNP PARIBAS ECONOMIQUE RESEARCH

EXPORTS: A SOLID DRIVER OF ECONOMIC GROWTH

The Covid-19 shock hit a very buoyant economy, which had grown by an average of 7% per year between 2015 and 2019, and still enjoyed growth of 7% y/y in Q4 2019. This momentum was fuelled in particular by the export-oriented manufacturing sector, which has attracted substantial Foreign Direct Investment (FDI) and gradually moved up the value chain. Exports of goods accounted for 80% of nominal GDP in 2019, from 64% in 2014. They now consist primarily of phones, computers and other electronic goods[1], for which global demand has surged since the beginning of the health crisis. As a result, exports have been a solid driver of the economic growth rebound after the shock in S1 2020 (chart 1). After a 7% y/y contraction in Q2, exports have bounced back rapidly, posting growth of 6.5% over the full year (vs. 8.4% in 2019). Vietnam further strengthened its world market share, accounting for 1.6% of global exports in the first nine months of 2020 (from 1.4% in 2019 and 0.8% in 2014).

The export sector has proved able to adapt to changes in global demand in 2020. Moreover, it has also taken advantage of Sino-American tensions over the past three years, via the substitution of certain Chinese products by Vietnamese products and the relocation of factories to Vietnam[2]. These trends are likely to persist in 2021 and 2022, with the country well-placed to attract investors and continue to expand its export base. One dark cloud on the horizon, however, emerged in December, when the US officially designated Vietnam as a 'currency manipulator'[3]. This decision could result in a degree of tension with the US, which is the destination for around a quarter of Vietnamese exports.

STRONG PERFORMANCE OF VIETNAMESE EXPORTS

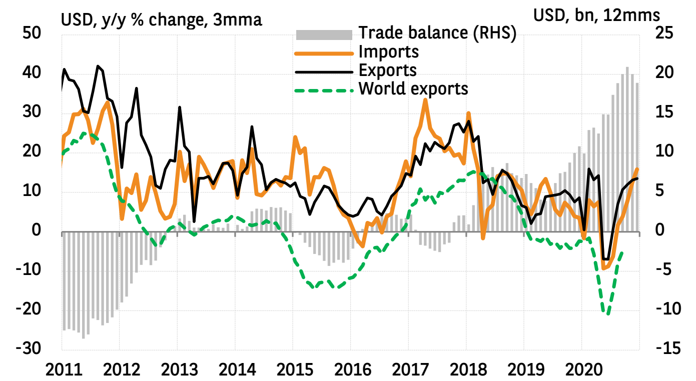

CHART 1

SOURCE: GENERAL STATISTICS OFFICE

1 In 2019, phones and components accounted for one-fifth of Vietnam's exports (vs. 16% in 2014), and other electronic and IT goods for 14% (vs. 8% in 2014). Textile and shoes remained at 19% of the total, whilst oil, agricultural and fisheries products declined to less than 8% from 20% in 2014. Foreign groups produced two-thirds of the goods exported, a share that has fallen slightly over the past three years.
2 One recent example is Apple, which began to assemble some of its products in Vietnam in May 2020.
3 This decision is the consequence of a bilateral trade surplus of more than USD 20 bn, Vietnam's current account surplus of more than 2% of GDP and forex market interventions of more than 2% of GDP.

We estimate that Vietnam's current account surplus was 3.2% of GDP in 2020, from 3.8% in 2019. The increase in the trade surplus was partly offset by the deterioration of the balance in services (collapse in tourism) and a drop in workers' remittances. Despite the reduction in foreign capital inflows, Vietnam continued to accumulate foreign exchange reserves, which reached USD 89 billion in September, meaning that they cover more than four months of imports of goods and services. The dong has appreciated slightly against the dollar since mid-2020.

A MODEST SLOWDOWN IN DOMESTIC DEMAND

In 2020, the manufacturing sector grew by 5.8%, down from 11.3% in 2019, and the service sector grew by 2.3% vs. 7.3% in 2019. Although sectors linked to tourism (6% of GDP) continued to struggle, services activities that depend on domestic demand have either held steady during the lockdown (IT & communications, healthcare) or recovered well since May (most notably in the retail sector). In fact, after a contraction during the lockdown period (-27% y/y in April), retail sales volumes have rebounded once lockdown was loosened, and posted a small decline of less than 1% in 2020.

Vietnam's labour market and households have been hit less hard than those of other countries in the region by the Covid-19 shock, given the rapid recovery in productive activity from Q2 2020. According to the World Bank, only 3% of workers lost their jobs last year because of the pandemic. Nevertheless, 33% of households suffered a reduction in income (compared to 79% in Indonesia for example), inequality increased, and the financial support provided by government proved to be weaker than expected. Meanwhile, households have benefited from slower inflation in consumer prices (1.4% y/y in Q4 2020 vs. 3.7% y/y in Q4 2019).

Private consumption growth stood at 0.6% in 2020, down from 7.4% in 2019. It is likely to rebound vigorously over the coming months, but not to return to pre-crisis levels in 2021. The slowdown in investment was much more modest (4.1% in 2020 vs. 7.9% in 2019). On the one hand, the loss of vigour in private investment was contained, notably thanks to the still strong prospects for exports. In particular, FDI has proved more resilient in Vietnam than in the rest of the region. According to balance of payments data, FDI inflows dropped by only 4% y/y over the first nine months of 2020 and had already regained their Q3 2019 levels in Q3 2020. On the other hand, public investment was stepped up last year. The accelerated implementation of investment projects (most of which were already under way or in the planning stage) represented the biggest share of the fiscal support package. Whilst total government spending increased by 8% y/y in the first nine months of 2020, investment spending (a quarter of the total) rose by 40%.

A TEMPORARY SHOCK TO PUBLIC FINANCES

Public finances had been consolidated over the five years prior to the Covid-19 crisis, leaving the government a small degree of latitude to absorb the shock and support activity. Thanks to greater discipline in managing expenditure, the partial privatisation of some state-owned enterprises and strong economic growth, the government registered a steady reduction in its deficit from 2014 to 2019 (from 5% of GDP to 3.3%) and a reduction in its debt between 2016 to 2019 (from 47.6% of GDP to 43.4% according to IMF data). This positive trend was interrupted last year, but this interruption is expected to prove only temporary.

MONETARY SUPPORT

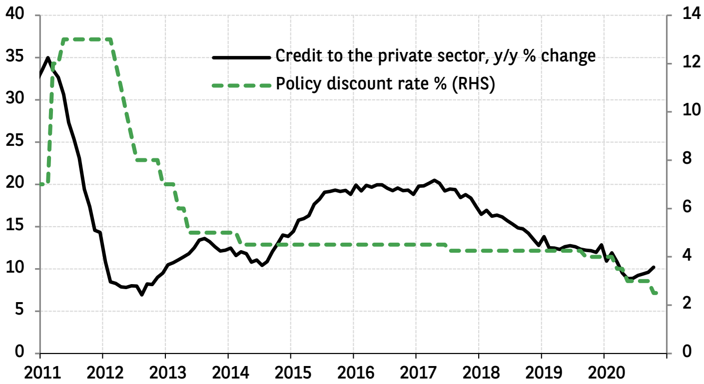

CHART 2 SOURCE: STATE BANK OF VIETNAM, IMF

The fiscal support package was modest – estimated at around 3% of GDP – and the fiscal deficit is unlikely to have exceeded 6% of GDP in 2020. It is projected to decline from 2021.

The government has been able to cover its financing requirements without difficulty, both on the local bond market and by using its fiscal reserves. Government debt remains moderately high, estimated at nearly 47% of GDP at end-2020 (from 43% in 2019, according to IMF data). It is projected to stabilise in 2021.

A MAJOR TEST FOR THE BANKING SECTOR

There is a major weak link in the Vietnamese economy: banks are undercapitalised and lack a buffer to protect them from shocks, while corporates, particularly in the public sector, are excessively indebted (credit to the economy represented 145% of GDP in 2020).

Some of these institutions could therefore find themselves severely weakened, in turn creating a threat to public finances. Granted, the performance of the banking sector improved in 2018-2019, notably thanks to a strengthening of the regulatory framework, a more solid funding base and an improved quality of new loans. In addition, since the beginning of the health crisis, the easing of monetary conditions (through interest rate cuts, liquidity injections and a loosening of macro-prudential rules) and the support provided to banks and their customers (rescheduling of loans) have helped reduce the pressure (chart 2). However, some corporates have been weakened and are experiencing cash-flow constraints, particularly those in the tourism and transport sectors. Non-performing loans on bank loan books have started to increase. This trend is likely to accelerate when support measures are phased out over the course of 2021. Against this background, certain small private banks, lacking capital and stable sources of funding, could face significant difficulties.

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