

# ■ Vietnam

| UOB Economics Projections  | 2006 | 2007 | 2008F | 2009F |
|----------------------------|------|------|-------|-------|
| GDP                        | 8.2  | 8.5  | 6.3   | 6.0   |
| CPI (average, y/y)         | 7.4  | 8.3  | 23.7  | 12.5  |
| Current account (% of GDP) | -0.3 | -9.6 | -13.0 | -11.0 |
| Fiscal balance (% of GDP)  | -1.8 | -1.8 | -1.9  | -2.1  |

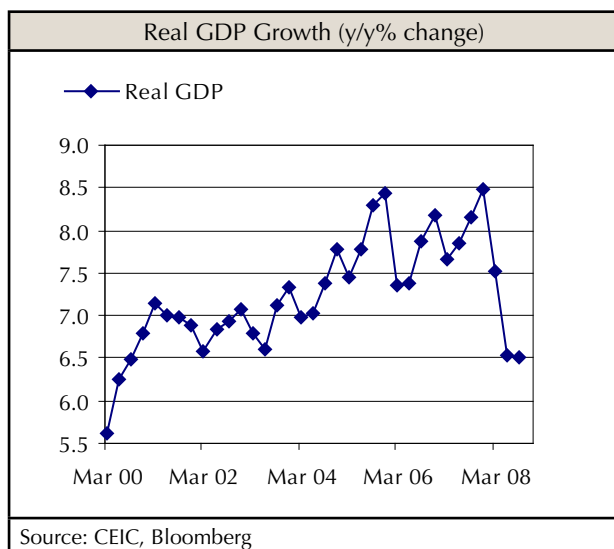
While the economy has remained resilient so far, we expect slowing growth to set in for the coming quarters. We have lowered our GDP growth forecast for Vietnam to 6.3% this year from 7.0% previously and foresee the growth rate to continue to ease to 6.0% in 2009.

Inflation is likely to moderate further, well into next year, as food prices moderate and supplies increase. Overall, we expect inflation to average around 23.7% this year, against govt's expectation of 25%.

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## Moderating Economic Growth Ahead

Vietnam's economy grew 6.5% y/y in 3Q08, similar to the pace in 1H this year but a sharp slowdown from the 8.2% y/y growth clocked in the same period of last year. Industry & Construction sector, accounting for 41.7% of GDP grew 7.1% y/y in 3Q08 slowing from 10.1% y/y in the same period of 2007. Construction alone contracted 0.3% y/y vs 11.1% y/y expansion during Jan-Sept 2007 as a result of the rising cost of raw materials. Companies also faced difficulties in acquiring capital due to the high interest rates.



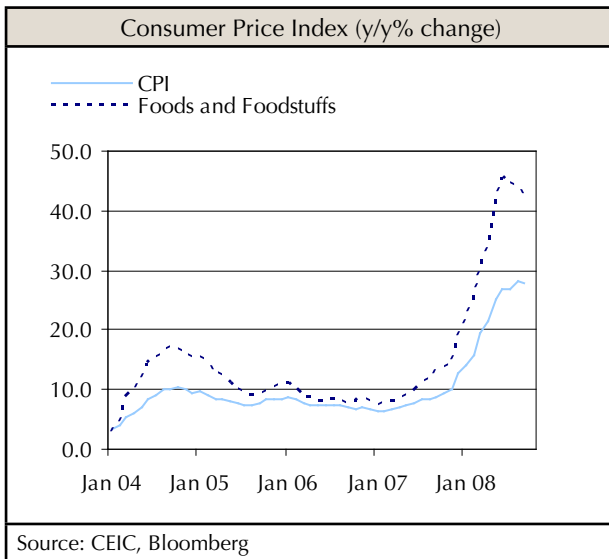
Services sector moderated to 7.2% y/y in the past nine months compared to previous year reading of 8.6% in the same period. Businesses in the Hotels and Restaurants industry also take a dip and fell 8.9% y/y in 3Q08, partly due to higher inflation crimping consumer spending. Meanwhile, the Agriculture, Forestry & Fishery sector grew 3.8% y/y contributed by the better-than-expected rice harvest this year.

While the economy has remained resilient so far, we expect slowing growth to set in for the coming quarters. We have lowered our GDP growth forecast for Vietnam to 6.3% this year from 7.0% previously and foresee the growth rate to continue to ease to 6.0% in 2009. Meanwhile, the govt is forecasting GDP growth of 7.0% this year vs initial expectation of 9% and 7.5% next year, which appears to be a little optimistic given the external uncertainties.

## Inflationary Pressures Remain Dominant

Against 8.3% in 2007, inflation surged to an average of 22.9% y/y in the first nine months of 2008. However, there were signs that inflation in Vietnam has peaked. Consumer prices rose 27.9% y/y in September, slowing from 28.3% in August as a result of lower food prices. Accounting for 43% of the CPI basket, food prices was at 42.7% y/y compared with 44.1% y/y in August. Meanwhile, govt's close supervision on businesses (preventing

## ■ Vietnam



unreasonable price adjustments) should help stabilize prices. In addition, global food prices have been declining on increased supplies, easing inflation in countries like Vietnam, which relies on agriculture for the bulk of its economy.

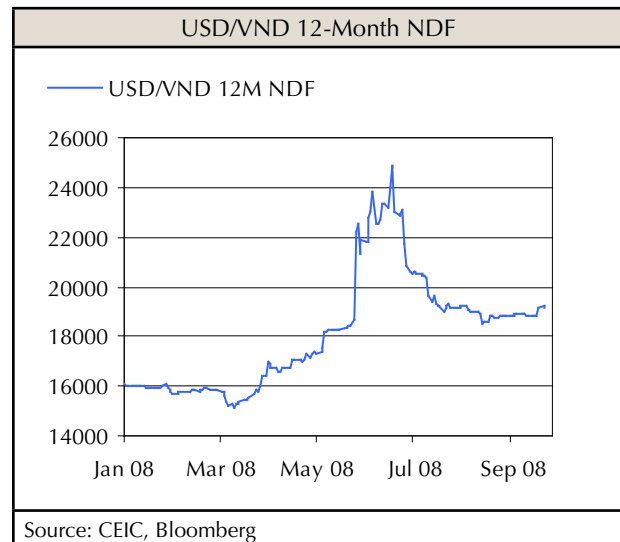
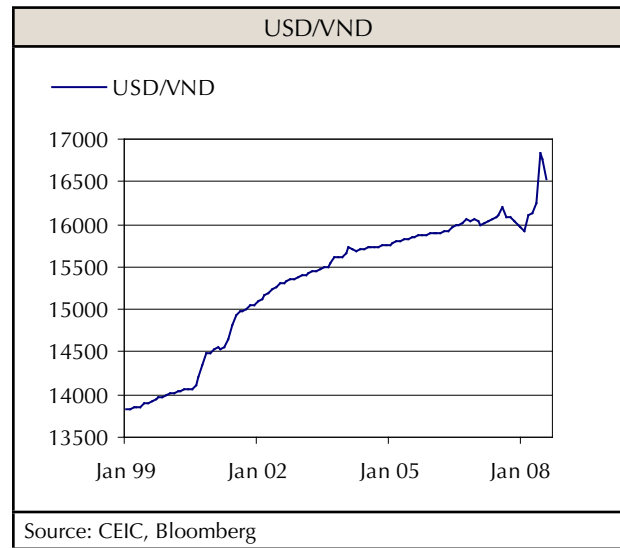
Going forward, inflation is likely to moderate further, well into next year. Overall, we expect inflation to average around 23.7% this year, against gov't expectation of 25%. The gov't is targeting at single-digit inflation rate by end 2009 or beginning 2010.

### SBV Maintained Tight Monetary Policy

The State Bank of Vietnam (SBV) continued to reiterate its tight monetary policy stance in view of inflationary pressures and had raised key interest rate three times this year (last hike - 11 June) to 14%. This is likely to be the SBV's last rate hike of the year. Gov't's ruling is that interbank rates are not allowed to exceed 150% of the key interest rates -- which means banks can loan at up to 21% per year, given current key rate of 14%. In addition, limiting credit growth at 30% for 2008 as compared with a growth rate of 54% last year, which triggered the surge in the country's inflation. We expect the central bank to keep to a tightening credit policy till end of the year as inflation still remains elevated.

### More FX Stabilization

On 11 June 2008, the government implemented a one-off 2% devaluation of the VND, to bring official exchange rates closer to black-market rates and widened the trading band to  $\pm 2\%$  (as widely-expected) on 27 June. Against 19,400/USD in June, VND is now trading around 16,620/USD in the black-market, as compared to



16,580/USD in the official market (24 September 2008). A few months back, market was expecting a reminiscence of Thailand in 1997, when the fall of Thai baht became the catalyst for the Asian economic crisis. Markets were worried that the dong would devalue in a manner similar to that of Thailand in 1997. At one point in June this year, the 12-month NDF priced in a major dong devaluation of as much as 50%, but has since eased to 13.7% in August. While there are still speculative pressures on the currency, we are doubtful of any major dong devaluation as:

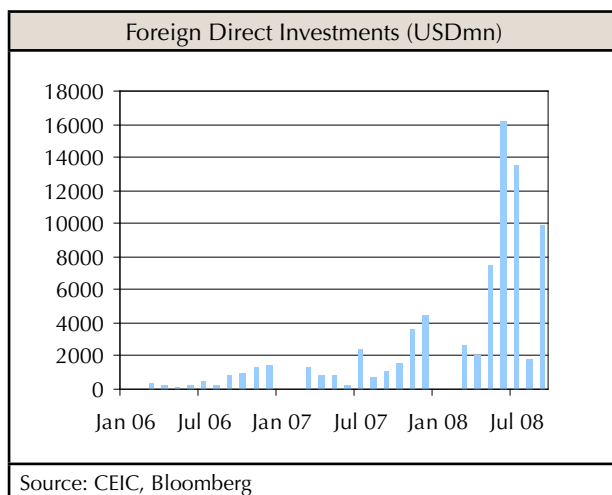
- Containing inflation is still the government's priority and there would be concern that the sharp dong depreciation would escalate inflation which could lead to renewed downward pressure on the currency.

## ■ Vietnam

- The country's foreign exchange reserves have improved significantly over the years to USD21.9bn end September 2008 from USD3.4bn in 2000.
- Like the RMB, VND is a "tightly controlled" currency. Any impact from the NDF on the cash market will be limited.

### Sustained FDI Inflows

The sustained FDI inflows has also provided some relief on the currency as well as supporting the country to achieve a balanced external account. Vietnam attracted USD57.1bn in FDI over the past nine months, much higher than the projected amount of USD50bn for the whole year. Attracting the biggest investment is the industry & construction sector with investors pouring in as much as USD32.3bn during the first nine months of 2008 while the service sector attracted overseas investment of USD23.7bn in the same period.

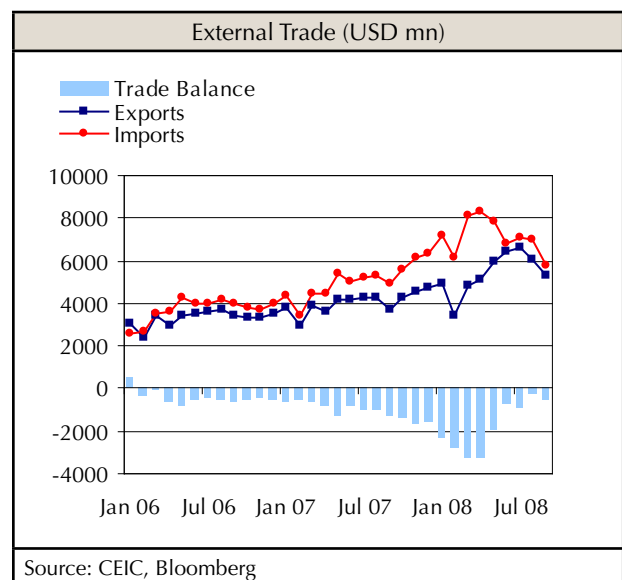


Recently, Malaysia has also registered to invest USD14.8bn for 37 projects (including the licensed USD9.8bn steel project) in Vietnam while Korea has also poured additional capital of USD192.7mn into their existing projects in the country.

While the strong FDI inflows might help the country to achieve a balanced external account, however, there are concerns over the FDI inflows into sector such as the property and steel industry. Given that projects in these industries would trigger demands for equipments and materials for such developments, escalating import growth which could lead to renewed pressure on the trade deficit.

### Government to Keep Close Watch on the Trade Balance

The country's trade deficit widened to USD15.8bn in the past nine months, doubled the figure (USD7.9bn) in the same period last year. However, in the month of September, Vietnam's trade deficit moderated to USD-500mn, the lowest figure recorded in 2008 compared with USD954mn in August. Against a monthly average of USD2.4bn between January and June 2008, the trade deficit was also under USD1bn for both August and September. This is line with the government's target to curb monthly trade shortfalls to under USD1bn in 2H08. Vietnam also revised 2008 trade forecast downwards, from under USD20bn to USD18.5-19.5bn.



Meanwhile, exports continued to perform well, rising 39.3% y/y to USD48.6bn in the first nine months of the year led by exports of rice, rising 71.5% y/y in September followed by crude oil reaching 30.4% y/y while textile & garments came in at 29.1% y/y.

The tightened monetary policy as well as measures to reduce imports adopted by the government has cut import growth from 77.8% y/y in April this year to 51.4% y/y in September. Imports for the past nine months reached USD64.7bn. The Ministry of Industry and Trade (MoIT) raised significant taxes which include the import taxes, the special consumption tax and value added tax as well as restricting imports of luxury goods since August. The government has also applied automatic licensing on imported goods which are under strict inspection and reducing the progress of investments along with cutting down on public spending.