VEPR SINCE 2008

VIET NAM QUARTERLY MACROECONOMIC REPORT

Quarter 4 - 2017

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SUMMARY

- The world economy in Q4 and in 2017 witnessed a steady growth. The US economy continued to expand despite the impact of two major hurricanes Harvey and Irma, which led to the Fed's decision to hike the interest rates in December. EU's economy recovered rapidly with the highest growth rate in recent years, whilst the UK has lost its position as the world's fifth largest economy. In Asia, Japan has continued to face labor shortages as well as population decline. The Chinese economy experienced a slightly lower growth when its government has tried to control the property market and debt risks. ASEAN economies maintained their impressive growth while BRICS countries also witnessed signs of economic rebound.
- The domestic economy, after an abnormal Q3, continued to be reported with even more impressive growth rate of 7.65% (yoy), which contributed to the overall growth rate of 6.81% in 2017, surpassing the National Assembly's target of 6.7%. Agriculture, forestry and fishery and service sectors improved greatly compared to previous years. The number of foreign visitors set a record of nearly 13 million, contributing to the recovery of service sector. The manufacturing witnessed a tremendous growth of 14.4%, being the driving force of the whole industry sector despite the shrink of the mining and quarrying sub-sector due to restructuring. All industrial production indicators grew in Q4.
- The number of new jobs and newly established firms increased considerably again in Q4.
- CPI remained stable in Q4, only increased by 2.6% (yoy) in December while inflation rate of 2017 was 3.53%, met the target of less than 4% assigned by the National Assembly.
- Trade balance saw a surplus of 3 bil. USD in Q4. The trade turnover this year reached 400 bil. USD for the first time in history. Both export and import turnovers showed impressive growth rate of more than 20% (yoy). Total trade surplus in 2017 was reported as 2.7 bil. USD.
- Korea is replacing China to be the country with highest deficit among trading partners with Vietnam.
- Although budget deficit stayed low, it may reflect slow disbursement of public investment. As for expenditure structure, the expenditure for investment and development still accounted for a small proportion (21.3%) compared to current expenditure (70.7%).
- Consumption continued to improve, growing by 10.9% (yoy,ytd) in Q4. Automobile was the commodity with the highest growth rate due to a competition in prices between producers and importers in 2017.
- Total investment capital grew steadily by 12.7% (yoy) in Q4. Investment in private sector witnessed the highest growth rate in both Q4 (17.7%) and the whole year (16.8%) among three sectors of the economy.
- Credit growth rate in 2017 was reported as 18.17%. This rate did not meet the Government's target of 21%. Liquidity of the banking system this year stayed plentiful as the SBV injected a large amount of VND into the economy but not (intentionally) strictly sterilized. Total foreign exchange reserves reached 51.5 bil. USD by the end of 2017.
- In the real estate market, the number of new apartments for sale and transactions increased significantly in both Hanoi and Ho Chi Minh City. The boom in market supply close to the end of the year may signal a declining trend in price in the future.

THE WORLD ECONOMY

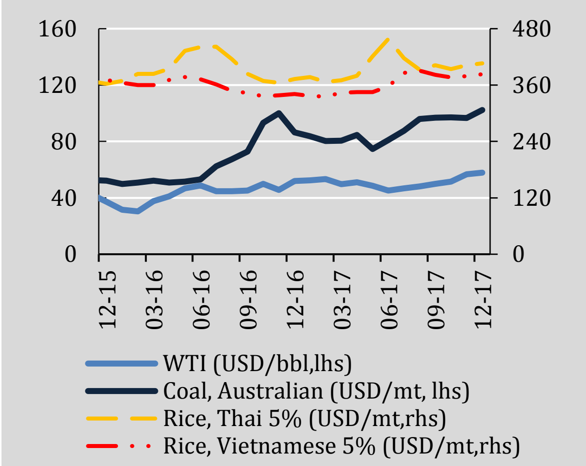
Commodity and asset markets

Commodity markets continued to witness a rebound in energy prices in Q4, while food prices did not fluctuate significantly compared to the previous quarter.

WTI crude oil price rose more sharply than Q3, recovering one-third of value after hitting the bottom in June, reaching an average of 57.9 USD/barrel in December, and increasing by 16.3% and 20.2% compared to the price in September and the average price of Q3 respectively. This was the highest price in the last ten quarters.

Although OPEC and Russia committed to cut production until the end of 2018, oil prices are predicted not to fluctuate wildly in the coming time because these countries' action has been already reflected in current oil prices and not surprised the market any longer. In addition, the fact that the US could increase shale oil production in 2018 also curbs the rise of crude oil prices.

Commodity Prices



Source: The Pink Sheet (WB)

Australian coal price, after witnessing a sharp improvement in Q3, did not change considerably until November, fluctuating around 97 USD/ton. However, the price increased to 102.2 USD/ton in December, setting a record in nearly six years.

Regarding food products, both Vietnam's and Thailand's 5% rice prices did not experience considerable fluctuation compared to Q3. After going down in October, the rice prices recovered in the last two months of 2017 because the supply was affected by natural disasters.

Gold Price and USD Index

Source: Fed, Fxpro

Additionally, increasing rice demand at the end of the year also contributed to the rise of prices. Thailand's and Vietnam's 5% rice prices reached 406 and 383.2 USD/ton, respectively, in December.

The world stock market in Q4 continuously accelerated and set many high records, marking a flourishing year of the global stock market. The MSCI All-Country World Index hit a record high of 513 on last days of 2017, up by 20% from the beginning of the year.

Price of crypto currencies, especially Bitcoin, was extremely volatile in Q4. At the beginning of October, Bitcoin price was 4,000 USD/BTC, peaking at 19,000 USD/BTC in the middle of December. This sharp rise has caused concern about a potential price bubble. Those who possess a large amount of Bitcoin may control the trading market like what happened in the last December when they sold all Bitcoins, causing a sharp fall in price. Bitcoin price during remaining days of the year fluctuated around 14,000 USD/BTC.

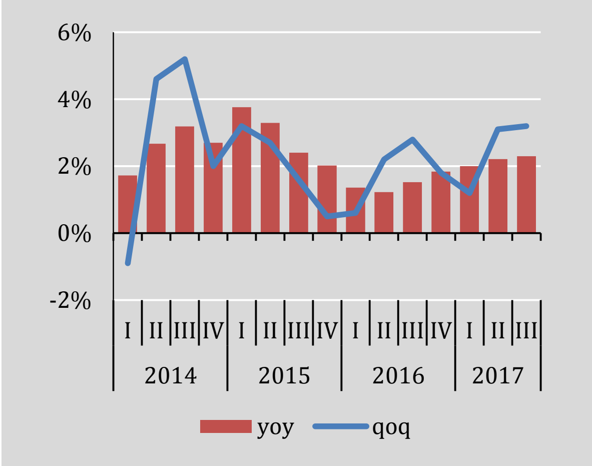
In the asset market, gold price remained stable in October and November, only surpassing 1,300 USD/oz on October 13. The average gold price during these two months was 1,281.3 USD/oz. Gold lost its value in the last month of the year as investors paid all their attention to stock markets and Bitcoin. The lowest price in December was 1,242 USD/oz on December 11. Gold price only rebounded after the Fed's decision to hike the interest rates on December 13.

Meanwhile, the US dollar value recovered slightly in Q4, after reaching the bottom on September 8. The nominal US Dollar Index was stable, fluctuating slightly around 120. By the end of 2017, the dollar lost nearly 7% of value since the beginning of the year, the sharpest decline in more than a decade, although the Fed hiked the interest rates three times during the year. It is due to Trump's attempt to lower the US's trade deficit, making the dollar depreciate against other major currencies.

US economy continued to improve its growth

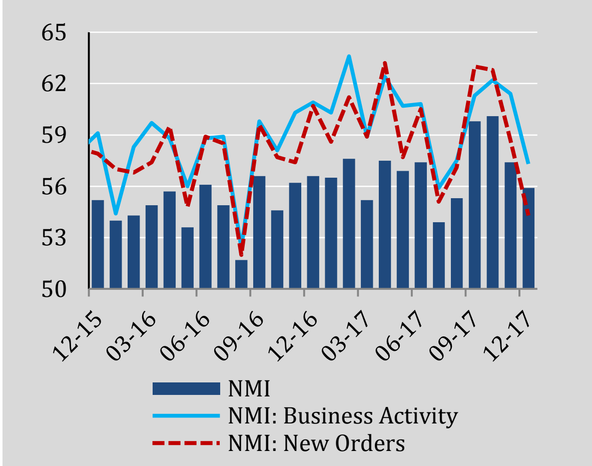
The third estimate released by the US Bureau of Economic Analysis showed that GDP growth rate was 3.2% (qoq) in Q3, 0.1 percentage point lower than the earlier estimate, due to under-expected increase in consumption than the previous estimation. This was the highest quarterly growth rate in nearly three years, contrary to forecasts after the impact of two major hurricanes Harvey and Irma. This positive growth was mainly due to increases in all consumption, investment, federal government spending, and exports.

US Economic Growth (%)



Source: CEIC

US Non Manufacturing Index



Source: CEIC

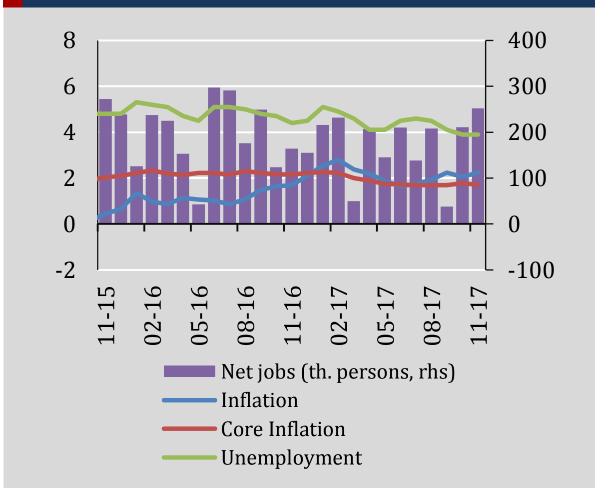
Concerning the service sector, service indicators continued to remain high in October. The NMI rose to 60.1 in October from 59.8 in September. The fact that NMI and sub-indexes declined in the remaining months of the year showed signs of lower growth in the non-manufacturing sector. Specifically, the NMI in December was 55.9 while the two sub-indexes, Business Activity and New Orders, decreased to 57.3 and 54.3 respectively.

The Fed hiked the interest rates the third time in the year during Q4. Accordingly, the basic interest rate was raised 0.25% to 1.25%-1.5%. The Fed made this decision after raising the country's economic prospect for the next year. The labor market continued to be strengthened in the last quarter, with the unemployment rate of 3.9%, the lowest in the last 17 years.

Meanwhile, the net number of new jobs, after declining dramatically in September, recovered sharply in Q4, reaching 244 and 228 thousand of new jobs in October and November, respectively.

Inflation continued to recover slightly and kept stable in Q4. Specifically, the headline inflation was 2.23% (yoy) in November. Meanwhile, the core inflation was 1.71%, not yet returned to 2% since Q2.

US Inflation and Unemployment (%, yoy)

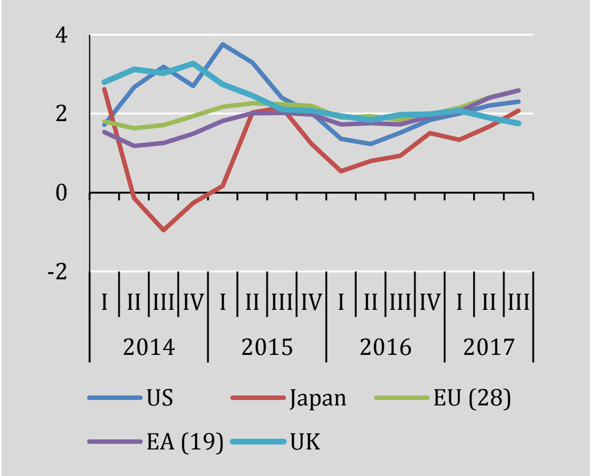


Source: CEIC

Europe continued economic rebound, the UK economy has lost its economic position

The European economy continued to see a robust recovery in Q3, witnessing positive growth rates for four consecutive years, which was the longest growth streak since the global financial crisis. Economic growth of both EU28 and EA19 was 2.59% (yoy) in Q3, the highest rate in more than six years. This recovery led to the ECB's decision to cut down its bond-buying program in Eurozone.

Economic Growth in Selected Advanced Countries (%, yoy)



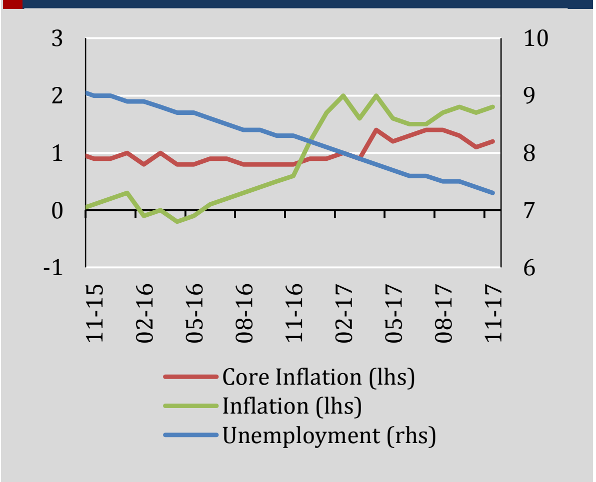
Source: OECD

Marked contribution to economic growth came from the development of production activities. September PMI reached 58.2 which was the highest point in more than six years. PMI in Q4 was even higher, reaching 60.6 in December. This continued to signal positive economic growth of the region in the coming time.

Employment continued to show signs of improvement in Q4. The unemployment rate dropped to 7.3% in November, the lowest rate in nearly nine years. Headline inflation tended to increase slightly in the last months of the year and stayed around 1.7-1.8%. Meanwhile, core inflation declined to 1.2% in November.

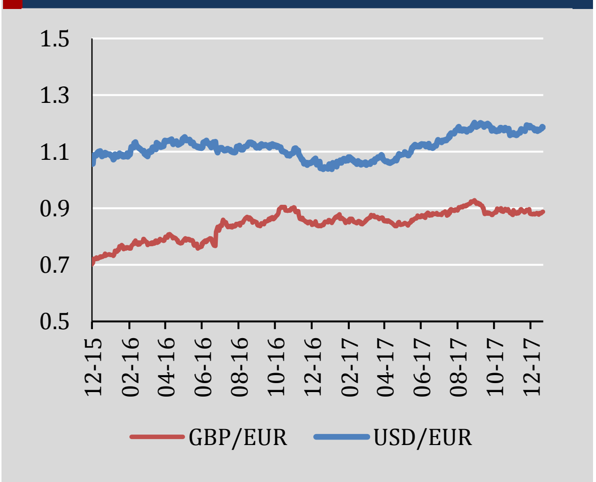
The German economy grew at 2.79% (yoy) in Q3, the highest level in six years. Failed negotiations to build a coalition government in November could trigger a

Inflation and Unemployment in EU28 (%)



Source: OECD

GBP/EUR and USD/EUR exchange rates



Source: BoE

social-political crisis in the largest European economy in the coming time. However, the agreement on January 12 may clear up these doubts.

The Spanish economy in Q3 witnessed a growth rate of 3.14% (yoy). However, the political crisis between Madrid government and the autonomous region of Catalonia since October may slow economic growth in Q4.

The UK economy continued to face difficulties. Economic growth was solely 1.75% (yoy), the lowest rate in four years. The UK has lost its position as the fifth largest economy in the world to France. This decline in economic ranking reflects the UK's economic recession after Brexit.

In case UK and EU cannot reach a new trade agreement, British people will face more difficulties as commodity prices increase.

In the coming time amid uncertainties of the world, the UK economy is expected to face many difficulties. In the latest IMF World Economic Outlook published on October 24, the IMF kept its forecast for its economic growth in 2017 and 2018 at 1.7% and 1.5% respectively.

USD/EUR exchange rate in Q4 was more stable than previous quarters of the year. At the end of the year, the exchange rate was at 1.199 USD/EUR, marking one year the Euro appreciated against the dollar. In 2018, the ECB will likely implement tightening monetary policies.

Japan continued to face demographic and labor problems

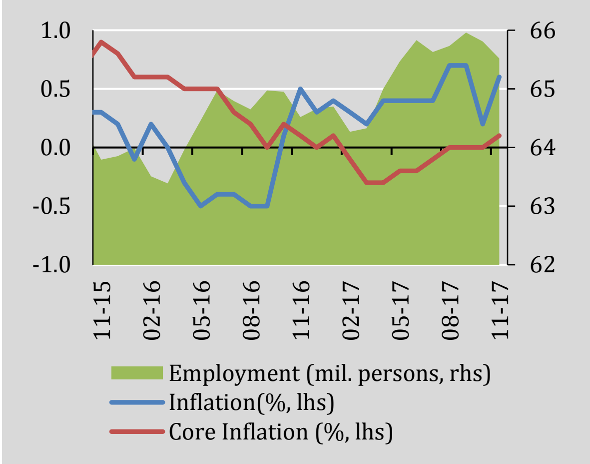
Japan’s economy grew at 0.62% (qoq) in Q3, marking seven consecutive quarters of expanding. This was the longest economic growth streak in more than one decade.

The recovery trend in industrial production has been maintained since the beginning of 2016. In particular, Japan's IPI growth rates were 4.67% and 3.70% in October and November, respectively.

Meanwhile, the service sector showed signs of recovery at the end of the year, with the retail sales index remaining above 100 points.

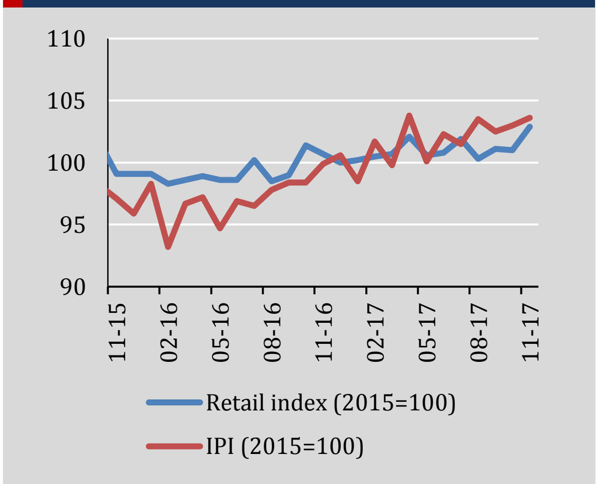
In the labor market, the number of employed workers tended to fall slightly in Q4, reaching 65.81 and 65.52 million in October and November, respectively, lower than Q3 (65.96 million people). The unemployment rate went down slightly to 2.7% in November, the lowest since December 1993. However, the total job offers to applicant ratio was recorded at 1.56 in November, the highest rate in 43 years. This figure, on the one hand, reflects the availability and abundance of job vacancies. On the other hand, it also demonstrates the severe labor shortages Japan has to face. Japan’s population fell sharply in 2017. According to data from Japan’s Ministry of Health, the number of new-born babies in 2017 was the lowest

Japan’s Inflation and Employment rate



Source: CEIC

Japan’s Retail Sales and Industrial Production (seasonally adjusted)



Source: Japan Macro Advisors

Total Wage and Jobs-to-Applicants Ratio in Japan

Source: Japan Macro Advisors

since 1899. The low birth rate combined with the aging population will be major challenges for this country in the future amid increasing labor demand.

Meanwhile, inflation was unpredictable in the last quarter. Headline inflation, which remained at 0.7% at the end of Q3, fell back to 0.2% in October before rebounding in November. Core inflation, for the first time since the beginning of the year, kept a positive value of 0.1% in November. This will still pose a challenge for the BOJ if it wants to reach the 2% target by 2019.

One outstanding event in 2017 was the series of fake data scandals in large Japanese corporations such as Kobe Steel and Mitsubishi, etc. These scandals have damaged public confidence in Japanese products and also damaged manufacturing sector of this country.

Chinese economy slightly slowed

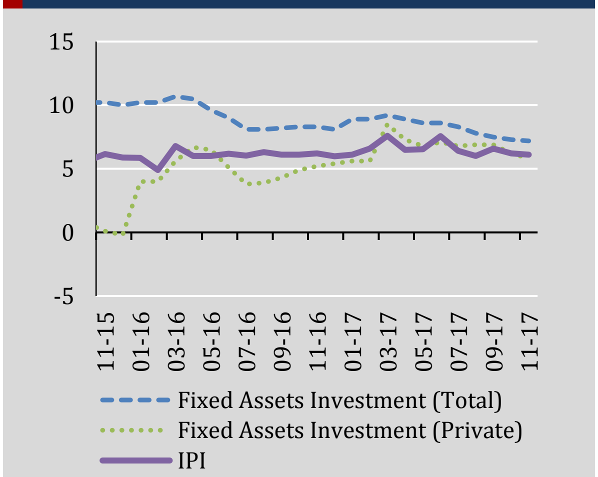
Chinese economy grew at 6.8% (yoy) in Q3, matching analysts' forecast. The second largest economy experienced this slowdown when its government tried to control the property market and mitigate debt risks.

Indicators of industrial production and investment of China together reflect the economic slowdown. Investment growth in the last months of the year decreased significantly. This fact could be explained by Beijing's efforts to control risky lending, which raises the cost of borrowing.

The growth rate of industrial production in the last months of the year declined. Although PMI was still above 50 points, falling slightly to 51.6 in December from 52.4 in September. However, as for the service sector, the NMI index fell slightly in October, before recovering during Q4, reaching 55 points in December.

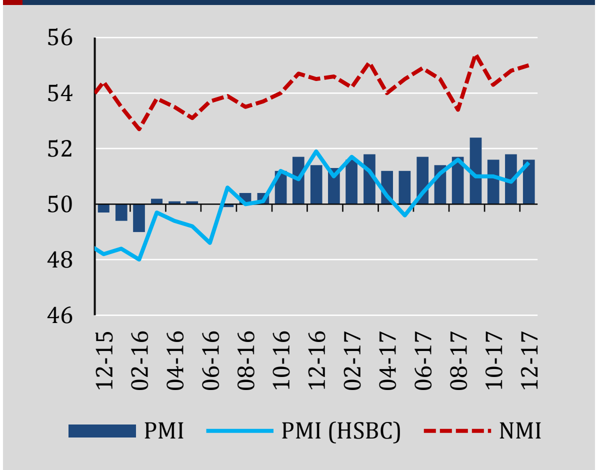
In the foreign exchange market, the CNY/USD rate remained relatively stable at 6.62 CNY/USD. One of the reasons for this stability was that the dollar value did not change much in the last quarter of the year. Stable exchange rate helped the People's Bank of China replenish China's foreign exchange reserves. The reserves in December reached 3,139.9 billion USD.

Fixed Capital Growth & IPI (%, yoy, ytd)



Source: CEIC

China's PMI & NMI



Source: AASTOCKS

China's Exchange Rate and Reserves

Source: FRED, CEIC

This marked the eleventh consecutive month China's foreign exchange reserves has increased after being below 3,000 billion USD in January 2017.

An important socio-political event of China in Q4 was the 19th National Congress of the Communist Party of China. The economy after the Congress will continue to prioritize macro stability rather than nominal values of growth, combined with accelerated reform. The economic reform will aim at the financial and monetary system and state-owned enterprises (SOEs). The priority of financial and monetary reform is to prevent financial risks, especially debt risks. SOEs reform will continue to focus on: (i) promoting mixed ownership and private capital, no privatization; (ii) using state-owned enterprises as the standard to reform ownership; (iii) limiting insolvency, encouraging large-scale mergers. These reform policies will have a substantial impact on the development of China in the near future.

Different growth trends among BRICS economies

The BRICS economies continued to witness different growth trends. While the Chinese economy saw a slowdown, other economies grew better in Q3.

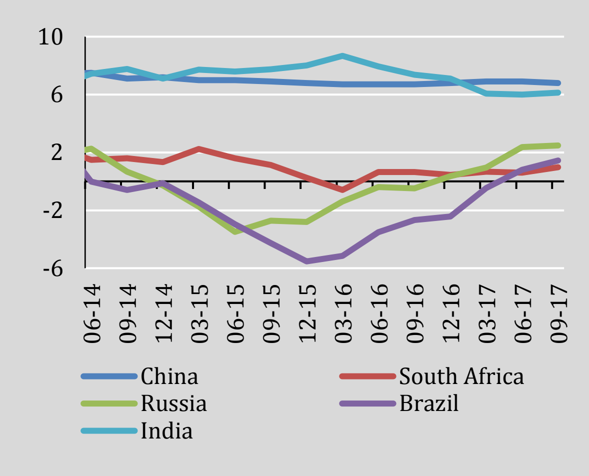
Although the growth rate of Q3 compared to the same quarter of the previous year was at a decent level 2.47%, Russia's growth rate compared to previous quarter declined dramatically, from 1.03% in Q2 to 0.09% in Q3. This fact can be explained by the fact that the economy contracted in Q3/2016 while rebounded in Q2/2017.

Industrial production in the last months of the year declined dramatically. Production growth fell 3.6% (yoy) in November after being 0% in the previous month. The easing monetary policy along with a slight increase in oil prices has been expected to contribute to the recovery of the Russian economy. However, the US sanctions will be an obstacle to this improvement.

Brazilian economy rebounded impressively in Q3 with a growth rate of 1.44% (yoy), nearly double that of the previous quarter. This was also the third consecutive quarter witnessing higher growth rate than previous quarter.

The Indian economy improved slightly in Q3, with a growth rate of 6.13% (yoy). However, this increase shows that the South Asian economy has not recovered strongly after currency swap shock since 2016. Also, businesses and individuals have not been familiar with the new system of goods and services tax yet, which has slowed India's economic growth.

Economic Growth in BRICS (%, yoy)



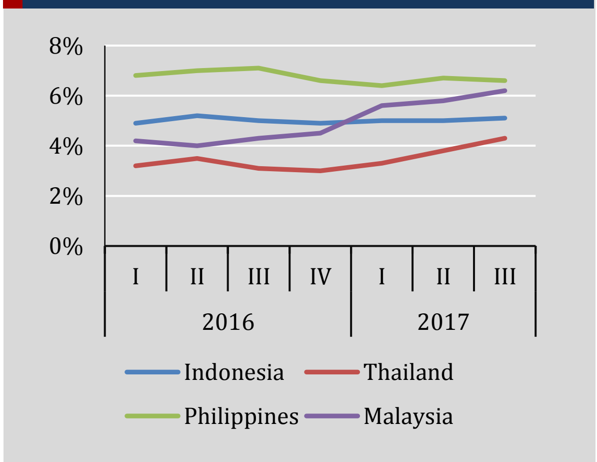
Source: OECD

ASEAN economies continued to grow rapidly

The overall economic growth of the ASEAN countries continued to stay steady in Q3. The growth rate of the region was 5.5% (yoy), much higher than 5% in Q2. This was also the highest growth rate since Q4/2012. In Asian Development Outlook Supplement in December 2017, ADB raised its economic outlook for regional growth to 5.2% for both 2017 and 2018.

Indonesia continued to grow at the average level of 5% (yoy), following the trend since 2014. This economy would reach one trillion dollar soon. Nonetheless, Indonesia is still left behind other regional countries

Economic Growth in ASEAN-4 countries (%, yoy)



Source: OECD

in terms of poverty alleviation, infrastructure system development, etc.

The Thai economy continued to recover in Q3. The growth rate was 4.3% (yoy), the highest in four years. This positive growth came from increases in all exports, private consumption expenditures, government spending, and private investment.

Myanmar has been expected to be the next Vietnam after opening the country in recent years. This country is an attractive destination for foreign investment after many decades of isolation. The Rohingya crisis, however, could prompt the US and Western countries to consider imposing sanctions again, which may make this immature open economy suffer heavily in the near future.

Global Economic Prospects(%)

	WEO* (10/2017)			GEP** (1/2018)		
	2016	*2017p*	*2018p*	*2017e*	*2018p*	*2019p*
Global Economy	**3.2**	**3.6 (0.1)**	**3.7 (0.1)**	**3.0 (0.3)**	**3.1 (0.2)**	**2.9 (0.1)**
Advanced countries	**1.7**	**2.2 (0.2)**	**2.0 (0.1)**	**2.3 (0.4)**	**2.2 (0.4)**	**1.9 (0.2)**
US	1.5	2.2 (0.1)	2.3 (0.2)	2.3 (0.2)	2.5 (0.3)	2.2 (0.3)
Euro area	1.8	2.1 (0.2)	1.9 (0.1)	2.4 (0.7)	2.1 (0.6)	1.7 (0.2)
UK	1.8	1.7 (0.0)	1.5 (0.0)	1.7 (0.1)	1.5(0.1)	1.5 (0.0)
Japan	1.0	1.5 (0.2)	0.7 (0.1)	1.7 (0.2)	1.3 (0.3)	0.8 (0.2)
BRICS countries	**4.3**	**4.6 (0.0)**	**4.9 (0.1)**	**4.3 (0.2)**	**4.5 (0.0)**	**4.7 (0.0)**
Russia	-0.2	1.8 (0.4)	1.6 (0.2)	1.7 (0.4)	1.7 (0.3)	1.8 (0.4)
China	6.7	6.8 (0.1)	6.5 (0.1)	6.8 (0.3)	6.4 (0.1)	6.3 (0.0)
India	7.1	6.7 (-0.5)	7.4 (-0.3)	6.7 (-0.5)	7.3 (-0.2)	7.5 (-0.2)
Brazil	-3.6	0.7 (0.4)	1.5 (0.2)	1.0 (0.7)	2.0 (0.2)	2.3 (0.2)
South Africa	0.3	0.7 (-0.3)	1.1 (-0.1)	0.8 (0.2)	1.1 (0.0)	1.7 (-0.3)
ASEAN-5 countries	**4.9**	**5.2**	**5.2**			
Indonesia	5.0	5.2	5.3	5.1	5.3	5.3
Malaysia	4.2	5.4	4.7	5.8	5.2	5.0
Philippines	6.8	6.6	6.9	6.7	6.7	6.7
Thailand	3.2	3.7	3.3	3.5	3.6	3.5
Viet Nam	6.2	6.3	6.3	6.7	6.5	6.5
Laos	6.9	6.8	6.8	6.7	6.6	6.9
Cambodia	7.0	6.9	6.8	6.8	6.9	6.7
Myanmar	6.3	7.5	7.6	6.4	6.7	6.9

Note: Differences from latest forecast in parentheses; e represents estimates; p represents prediction

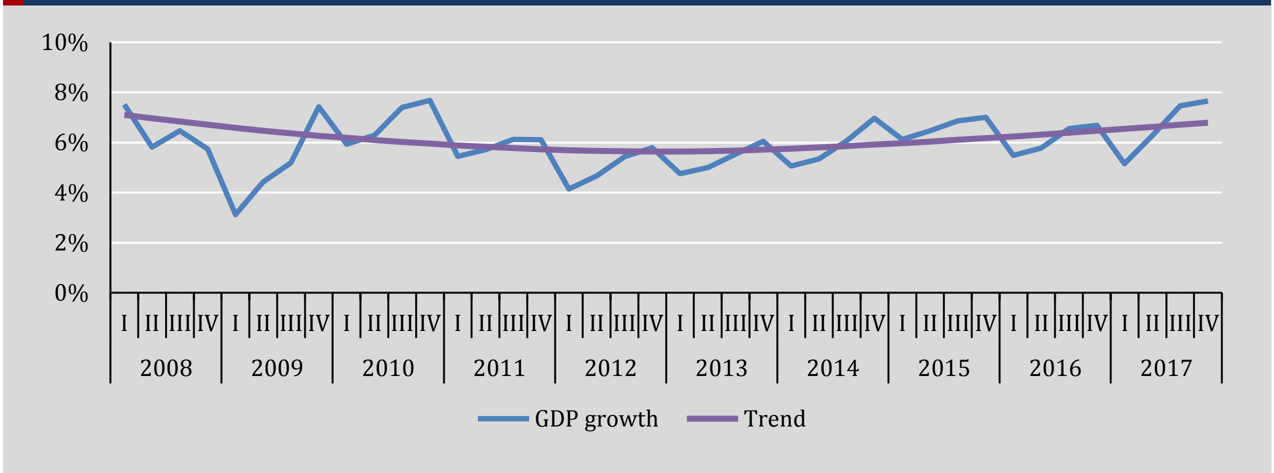
Source: World Economic Outlook (IMF), Global Economic Prospects (WB)

THE VIETNAMESE ECONOMY

Growth-Inflation

Vietnamese economy grew at a rapid rate

Viet Nam Economic Growth (%, yoy)



Source: Calculated from GSO data

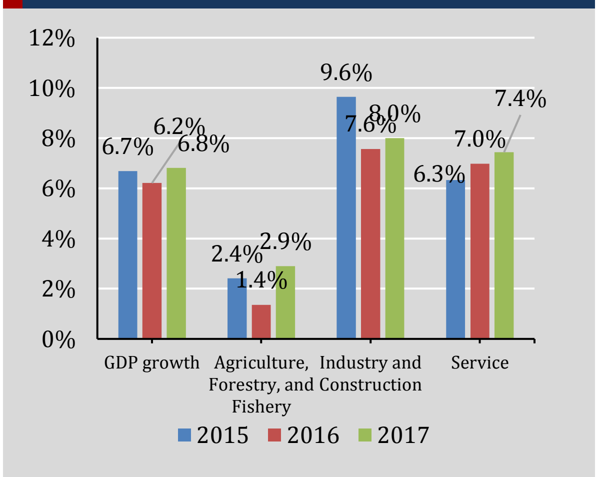
According to the announced data by GSO, Vietnamese economy continued to witness high economic growth in Q4. The growth rate of 7.65% (yoy) was the highest in many years, much higher than the same period of the previous years (2015: 7.01%, 2016: 6.68%). High growth in the second half of the year contributed to the overall GDP growth of 6.81%, surpassing the target 6.7% set by the National Assembly.

The service sector grew at 7.44% (yoy) in 2017, the highest rate since 2011. The sub-sector contributing the most to the overall growth was wholesale and retail with an increase of 8.36% (yoy). Meanwhile, the finance, banking and insurance and the real estate business recorded the highest growth rates for the past 6-7 years, respectively at 8.14% and 4.07% (yoy).

Remarkably, the number of foreign visitors to Vietnam in 2017 hit a record of 12.9 million people, up by 29.1% compared to the previous year.

The agriculture, forestry, and fishery also showed a clear recovery compared to 2016.

Economic Growth of 2017 by sector (%, yoy)



Source: GSO

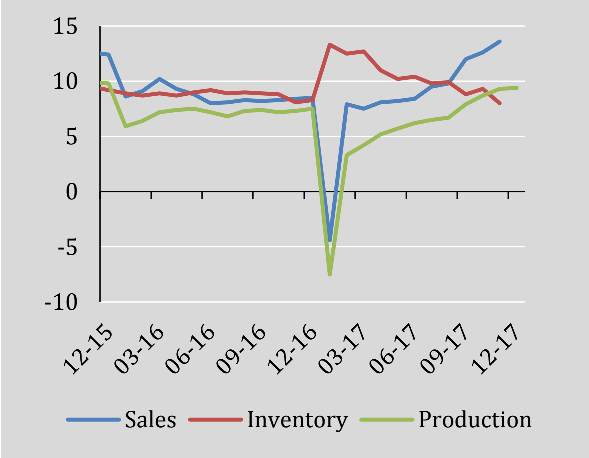
The growth rate of this sector in 2017 was 2.90%, much higher than in 2016 and also higher than the growth rate of 2.41% in 2015. The weather in 2017 was quite favorable for fishery and forestry, which witnessed growth rates of 5.54% and 5.14%, respectively. Particularly, 2017 was a good year for the fishery. Raw pangasius price increased continuously in the last months of the year, reaching the highest price in the past 20 years. However, in a year with a record number of typhoons and floods, the agriculture sector only grew by 2.07%.

Meanwhile, the industrial and construction sector grew at 8.00% (yoy) thanks to two last accelerating quarters of the year, surpassing the growth rate of 7.57% in 2016. The manufacturing industry continued to be the main driving force of economic growth of this sector with a very high growth rate of 14.40%. The mining and quarrying sub-sector continued to decline by 7.10%, the biggest shrinkage since 2011, reflecting the restructuring policies of the Government focusing on more technology-intensive and added-value industries.

All industrial production indicators also revealed improvement in Q4. Industrial production index and consumption index surpassed the average figure in 2016, implying that the reduction at the beginning of the year was only temporary. Specifically, by the end of December, the Industrial production index (IPI) for the whole industry had increased by 9.4% (yoy), the highest rate since 2016. Of which, IPI of the manufacturing jumped by 14.5% (yoy). This is the highest rate of this industry for the past several years.

Consumption index kept improving to reach 13.6% (yoy) by the end of November. Meanwhile, inventory index in Q4 fell slightly, down to 8.0% (yoy) in November.

Selected Industrial Indicators (%, ytd)



Source: GSO

Vietnam Economic Performance Index

Source: VEPR

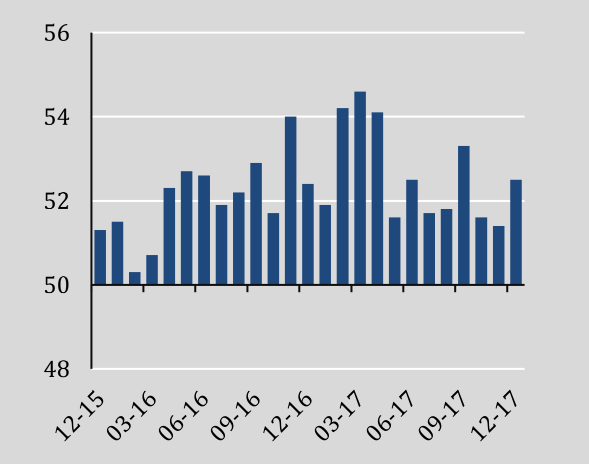
VEPI (Vietnam Economic Performance Index), derived by VEPR using data on electricity, import turnover, credit growth and IPI index, also reflected a high growth rate of the economy in Q4. However, this rate was slightly lower than the announced GDP growth by GSO, as the VEPI always tends to be more stable. Specifically, VEPI in Q4 reached 7.28%, much higher than the previous quarter and the same period in 2016, while the announced GDP growth rate was 7.65%. This came from high import growth of Vietnam in 2017, as well as a recorded level of IPI production index growth in recent years. The gap between VEPI and GDP may raise a question about the announced high GDP growth rate and, therefore, the unification of data. If we use VEPI for Q3 (6.24%) and Q4 (7.28%), the annual growth rate was only 6.41%, lower than 6.81% reported by GSO and not met the target set by the National Assembly. As the growth of other components of VEPI are still moderate, maintaining long-term growth momentum of the whole economy will create more challenges in the future.

Newly established firms and new jobs increased again

Although GDP grew at a higher rate, the Purchasing Managers' Index (PMI) showed a downward trend in Q4 compared to September. PMI fell from 53.3 in September to 51.6 and 51.4 in October and November respectively, before rebounding in December, reaching 52.5 points. Accordingly, the PMI Index also recorded 25 consecutive months of the manufacturing's expansion, showing a positive signal of business prospects in the manufacturing sector.

The Ease of Doing Business Index (EDBI) of Vietnam announced by World Bank also saw steady improvement. Accordingly, the ranking of Vietnam has risen to 82th out of 190 countries and is expected to increase to 68th in 2018. This improvement has come from many different factors including increased reliable power supply by rolling out a Supervisory Control and Data Acquisition (SCADA) automatic energy management system, strengthened accessibility to credit for businesses by broadening the scope of assets that can be used as collateral, upgraded automated cargo clearance system to facilitate import and export, etc.

Viet Nam's PMI



Source: HSBC, Nikkei

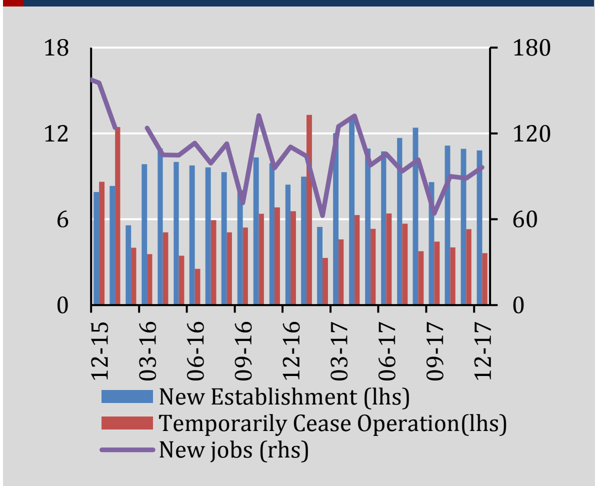
The survey on the business trend of manufacturing and processing enterprises conducted by the GSO also showed positive figures. Of all the surveyed enterprises, 44.8% rated their business performance in Q4 better than Q3. This rate was higher than the previous quarter (41.55) and the same quarter of the previous year (41.2%). Meanwhile, only 18.7% rated worse.

Regarding business activities, after September (the seventh month of the Lunar calendar) with only 8,610 newly established enterprises, this figure rose markedly again in Q4 with an average of 10,964 per month.

For the whole year, there were 126,859 newly established enterprises, 15.2% higher than 2016, with registered capital of 1,295.9 trillion VND, up by 45.4%. The average registered capital per enterprise increased significantly by 26.2% and reached 10.2 billion per enterprise. In addition, the number of enterprises temporarily ceasing operation in 2017 was 60,553 enterprises, down by 0.2% compared with 2016.

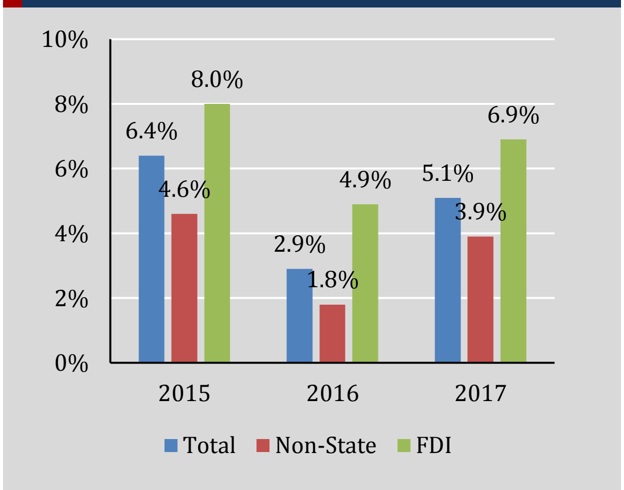
Newly created jobs also rebounded again in Q4 from 64 thousand in September. On average, there were 91.6 thousand new jobs created per month in Q4. As of December 1, 2017, the number of employees working in enterprises increased by 5.1% over the same period in 2016. Regarding economic sector, the number of employees in public sector continued to decline by 0.7 %, while that of the FDI sector recorded a high growth rate of 6.9%. This shows that the FDI sector continues to be the key driver of industrial recovery as well as exports.

Enterprise Operations (th. unit, th. persons)



Source: GSO

Labor Growth in Industry Sector (%)



Source: GSO

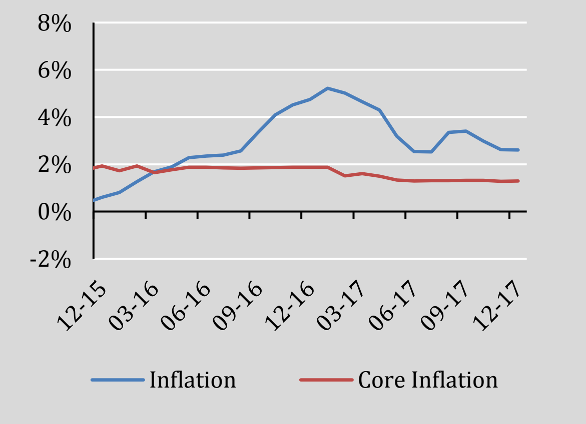
Inflation remained stable in Q4, core inflation for the whole year stayed low

After rising in August and September, headline inflation declined in Q4 and stayed below 3% in the whole quarter. December CPI rose only by 2.60% over the same period of the previous year. Thus, the average CPI in 2017 increased by 3.53%, meeting the target of less than 4% set by the National Assembly. In general, headline inflation in 2017 remained low, mainly due to the sharp decline in food prices in the first half of the year because of the pig oversupply crisis. Prices increased in August and September due to seasonal factors, then fell back again. This was in stark contrast with the upward trend of 2016.

At the end of the year, CPI only rose by 2.60% over the same period of the previous year. Meanwhile, core inflation remained stable around 1.3% since May, creating more space for monetary policy.

The primary cause of low inflation in 2017, besides a sharp drop in food prices in the first half of the year, also came from the tight monetary policy, reflected by the downward trend of core inflation. This created an opportunity for price adjustments of basic public services not been completed yet in 2016. Specifically,

Inflation and Core Inflation (%, yoy)



Source: GSO

many provinces increased the price of medical services for those without insurance cards, causing the price of this service group increased 27.79% compared to 2016. Along with that, the price of education services rose sharply in August and September, causing the price index of this group to rise by 7.29%. After petrol price adjustments, the price index of transportation group in December also increased by 6.04% over the same period of the previous year.

Fluctuation in the core inflation rate also reflects the prudent money supply control by the SBV. For the whole year, total means of payment was estimated to increase by 14.19% over the end of 2016, a lower rate compared to two previous years (2015: 14.91%; 2016: 16.47%).

Macroeconomic balances

Trade surplus with recorded levels of import and export turnover

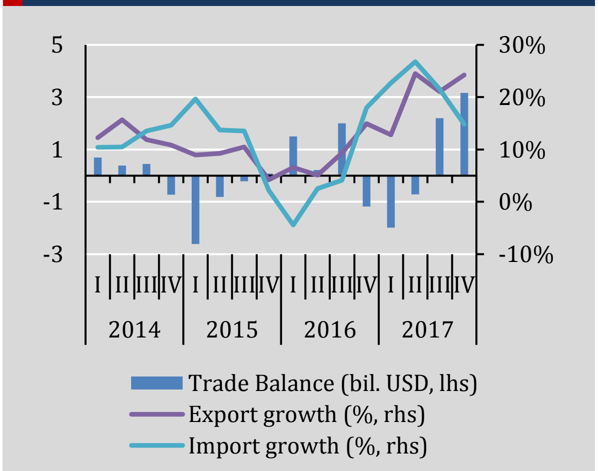
Trade continued to grow dramatically in Q4. Specifically, export and import turnovers grew by 24.2% and 14.8% (yoy) respectively. Following the trend from the previous quarter, Q4 recorded a trade surplus of 3.17 billion USD, the highest in many years.

By the end of December, export turnover was estimated to reach 213.77 billion USD, with an increase of 21.2% compared to the previous year, as global demand increased due to steady economic growth. In particular, exports still come mainly from FDI enterprises. Exports from this economic sector reached 155.24 billion USD, accounting for 72.6% of total exports and up by 23% over the same period of 2016. Domestic exports also improved sharply by 16.2%.

Import turnover also grew at a high rate of 20.8% over the same period last year and reached 211.1 billion USD. Imports of major commodities recorded high growth rates, such as electronics, computers and components reaching 37.5 billion USD (up by 34.4%) and machinery, equipment, tools and spare parts reaching 33.6 billion (up by 17.9%).

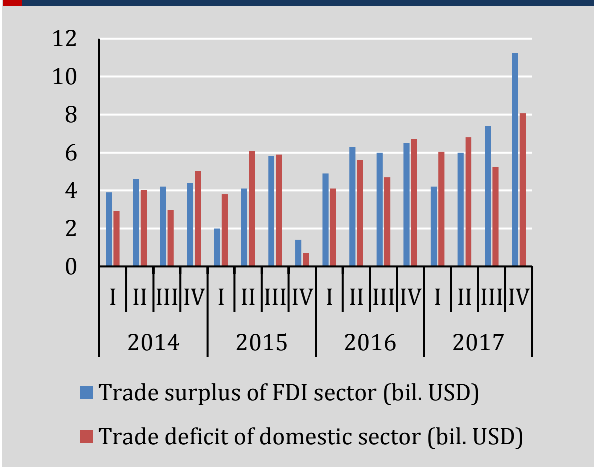
By types of goods, exports of major commodities in 2017 increased sharply compared to the previous year. Phones and components were still the top export commodities, gaining 45.1 billion USD, up by 31.4%, mainly from the FDI sector. Apparel and electronics, computers, and components also accounted for substantial shares in the export structure, both reaching 25.9 billion USD. In one favorable

Trade Balance and Growth



Source: CEIC, GSO

Trade Balance by Sector



Source: CEIC, GSO

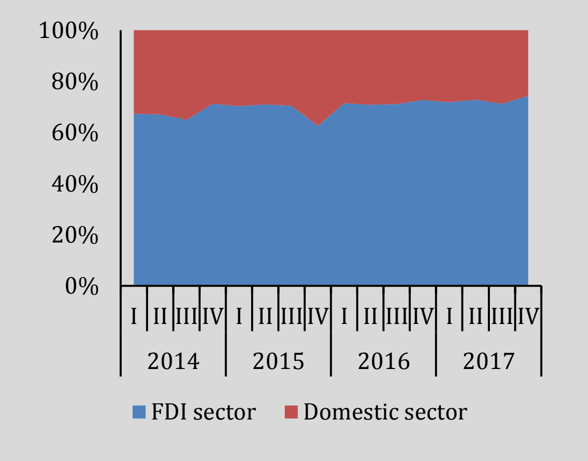
year for fishery and forestry, these two sub-sectors also contributed 8.4 and 7.6 billion dollars respectively to total export turnover.

Meanwhile, imports soared in materials for manufacturing and processing industry, reaching 192.9 billion USD, accounting for 91.4% of import turnover. Of which, imports of machinery, equipment and spare parts reached 33.6 billion USD (up by 17.9%) while such figures for electronics, computers and their components, and phones and their components were 37.5 billion USD (up by 34.4%) and 16.2 billion USD (up by 53.2%) respectively.

The two last quarters contributed to the total trade surplus of 2.7 billion USD in 2017. Regarding economic sectors, the FDI sector recorded a trade surplus of 28.84 billion in 2017, while the domestic sector suffered a trade deficit of 26.14 billion. This situation continued to show the dependence of trade as well as the growth of the entire economy on the FDI sector and to raise doubts about long-term prospects for the quality and sustainability of Vietnam's economic growth.

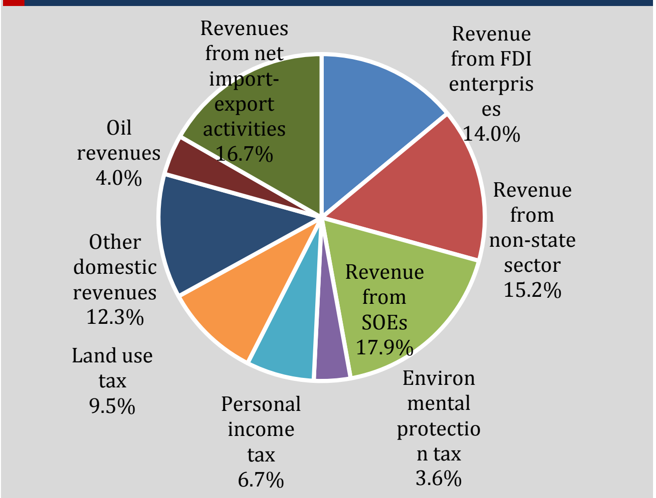
By partners, the US continued to be the biggest export market of Vietnam with 41.5 billion USD, followed by EU and China with 38.3 and 35.3 billion USD, respectively. Meanwhile, in terms of imports, although China was still the largest import market of Vietnam with 58.5 billion USD (up by 16.9%), South Korea replaced China as the largest trade deficit partner of Vietnam with 31.8 billion USD. This continues to show that FDI inflows from Korea are growing thanks to FDI enterprises from this country, especially Samsung, which mainly import materials from the home country. The shift of trade deficit from China to Korea- a country with higher technology capability- will continue to open opportunities and challenges for Vietnam in advancing its technology by adjusting and applying imported products in the context of the Industry 4.0.

Exports by Sector



Source: CEIC, GSO

Structure of Budget Revenue in 2017



Source: GSO

Budget deficit decreased slightly, but revenue collection and expenditure disbursement were behind schedule

According to the National Financial Supervisory Commission of Vietnam, the budget deficit in 2017 was 3.5%, the lowest in the past four years. However, the low deficit was partly due to the slow disbursement of public investment. Divestment from SOEs (such as Sabeco) also contributed to the low budget deficit.

By December 15, 2017, total state budget revenue was only 1,104 trillion VND, about 91.1% of the plan. Of which, domestic revenue was 871.1 trillion VND, about 88% of the plan and accounting for 78.9% of total revenue. In revenue structure, revenue from crude oil and trade remained almost unchanged compared to 2016 (4.0% and 16.7% respectively), much lower than previous years, due to the impact from the price of crude oil and other necessities. In order to raise revenue, the government had to continue to collect from other revenue sources, especially from land use tax (9.5%).

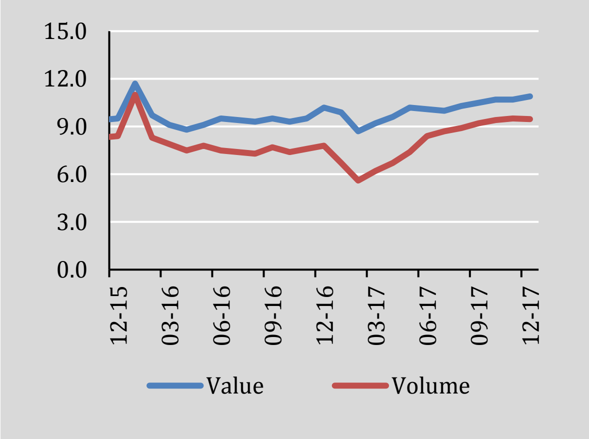
In the context of no improvement in revenue, state budget expenditure has always been a burden due to the bulky state apparatus. By December 15, 2017, total state budget expenditures reached 1,219.5 trillion VND, resulting in the budget deficit of 115.5 trillion VND. Recurrent expenditures remained high at 862.6 trillion VND, accounting for 70.7% of total expenditure. Meanwhile, development investment was only 259.5 trillion VND, accounting for 21.3% of total expenditure and only 72.6% of the plan.

This, on the one hand, showed slow disbursement of development investment capital. On the other hand, this situation continued to reflect the imbalance of total expenditure as long-term growth resources such as public investment are much more limited than short-term needs such as recurrent expenditure.

Consumption kept improving, investment growth still relied heavily on the FDI sector

The announced data showed that consumption continued to improve in Q4, contributing to a good year for retail and consumption. Total retail sales of goods and services for the whole year were estimated at 3,934.2 trillion VND, up by 10.9% (yoy), higher than previous years (2015: 9.8%,

Retail Growth (%, ytd, yoy)



Source: GSO

2016: 10.1%). In addition, consumption was substantially enhanced in terms of quantity with the growth rate of 9.2% (yoy), excluding price factor. Of which, the automobile sales had the highest growth rate (14%) in 2017 due to a competition in prices between producers and importers. Precious stones, precious metals (13.2%) and construction materials (12.8%) also witnessed high growth rates in the year.

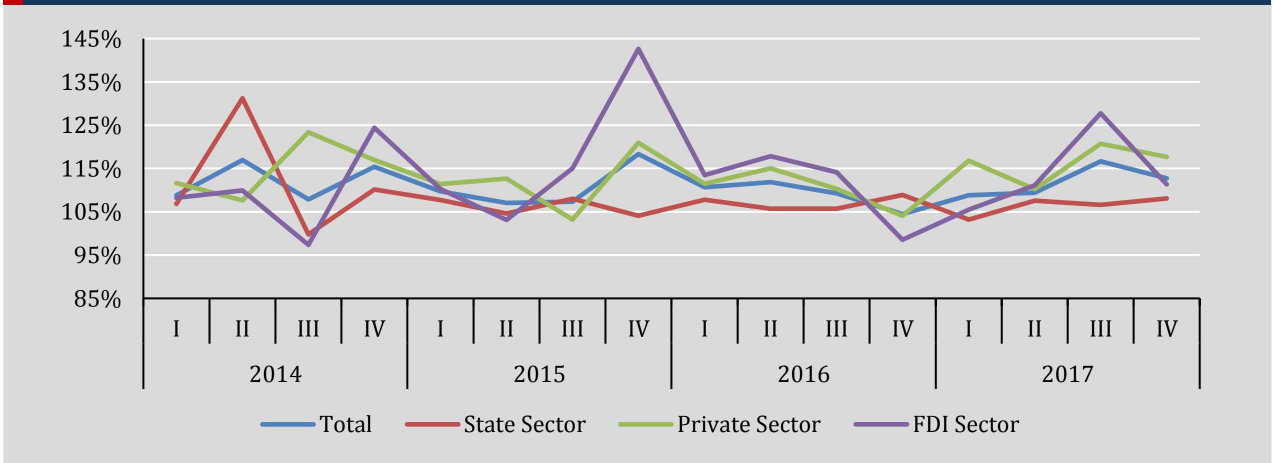
Meanwhile, total capital investment continued to recover slightly. Total implemented capital in Q4 was estimated at 538.7 trillion VND, about 112.7% over the same period of the previous year, just below the growth rate of Q3/2017 during the last two years. The private sector was the most invested sector in terms of both volume and growth, reaching 225.9 trillion VND, up by 17.7% (yoy). In the last quarter of the year, investment growth in the FDI sector declined by more than half compared to the previous quarter, only by 11.3% compared to 27.7% in Q3, although the amount of investment capital of 119.7 trillion VND was the highest level in many years.

Regarding foreign investment inflows, disbursed FDI capital was 5 billion USD, up only by 4.6% over the same period of the previous year. For the whole year, the total disbursed FDI reached 17.5 billion USD and up by 10.8% (yoy).

Meanwhile, after a sharp drop in Q3, the newly registered capital increased nearly three times in Q4 and reached 6.72 billion USD, up by 67.1% (yoy) with 747 newly registered projects. For the whole year, newly registered capital reached 21.28 billion USD, with a total of 2,591 newly registered projects. More than one-third of these projects (932 projects) were in the manufacturing industry, which had a very high growth rate and was a major driving force of the economy.

One notable FDI project in the last quarter was the BOT Van Phong 1 project, with the total registered capital of 2.58 billion USD,

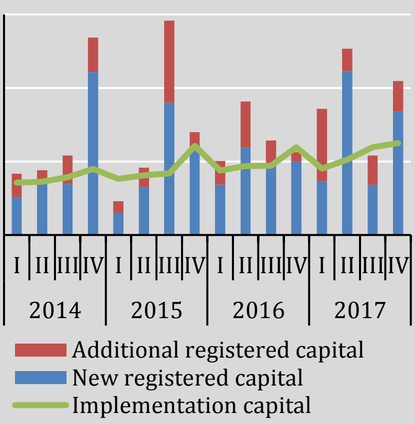
Total Social Investment (Compared to Corresponding Period of the Previous Year)



Source: Calculated from GSO data

invested by Sumitomo Corporation of Japan. This project, together with other large projects, helped Japan to be the top foreign investor in Vietnam in 2017 with 9.11 billion USD, accounting for 25.4% of total FDI. South Korea ranked second with 8.49 billion USD, of which 2.5 billion was supplemented to Samsung Display Vietnam project. Singapore ranked third with 5.31 billion USD.

Foreign Direct Investment (bil. USD)



Source: MPI

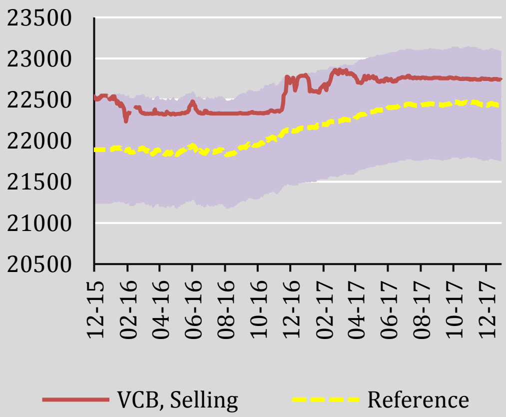
The monetary and financial markets

The forex market remained stable for the whole year

Nominal exchange rate continued to maintain stability in Q4. In general, the VND/USD exchange rate did not change much throughout 2017. Thanks to the low inflation rate, the abundant foreign currency supply, and the devaluation of the dollar, the impact on the exchange rate was even reversed. As a result, both the reference exchange rate and the spot exchange rate at commercial banks did not fluctuate greatly during the second half of the year. As of December 29, 2017, the reference rate announced by the SBV was 22,425 VND/USD, only rising by 1.2% compared to the beginning of the year. Meanwhile, the selling rate at Vietcombank was almost unchanged, only fluctuating around 22,745 VND/USD.

Monetary policy in 2017 continued to be implemented strictly although the SBV has made many statements showing a tendency to loosen. The positive balance of payments allowed the SBV to buy foreign currencies continuously throughout the year, helping foreign exchange reserves reach 51.5 billion USD (over 2.7 months of imports), as announced by the Deputy Governor Nguyen Thi Hong in the last meeting of the year. The abundance of foreign currency helped reduce the pressure on VND. Therefore, the SBV has had more space to lower interest rates to boost the economy.

Nominal Exchange Rate (VND/USD)



Source: VEPR

Liquidity was abundant, while credit growth was under target

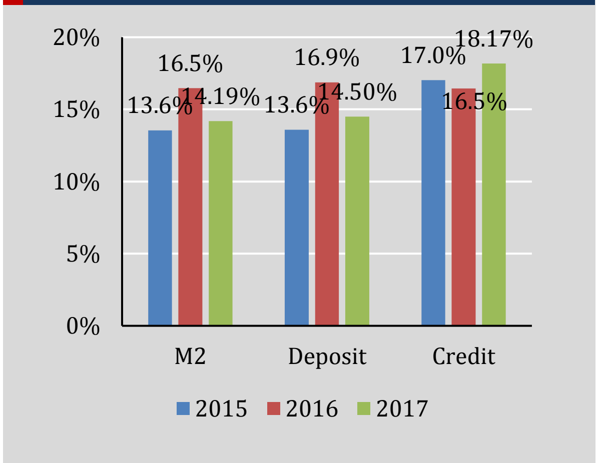
According to data announced by GSO, as of December 20, 2017, credit growth was 16.96% compared to December 2016, almost the same as the two previous years (2015: 17.02%; 2016: 16.46%). However, according to Tran Van Tan, the Deputy Head of the SBV's Credit Department of Economic Sectors, credit growth for the whole year 2017 was 18.17%. This growth rate still did not meet the target of 21% set by the Government.

In addition, in 2017, deposit growth was 14.50%, lower than the rate of 16.88% over the same period of 2016. Thus, credit growth rate was 2.46% higher than deposit growth rate. However, the liquidity of the banking system in 2017 was still abundant thanks to the SBV's actions of purchasing of 7.5 billion USD throughout the year and only contracting the money supply of nearly 31 trillion VND through the treasury bill auction channel.

The deposit rates were kept stable throughout the year. Long-term VND deposit rates over 12 months were around 6.4-7.2%.

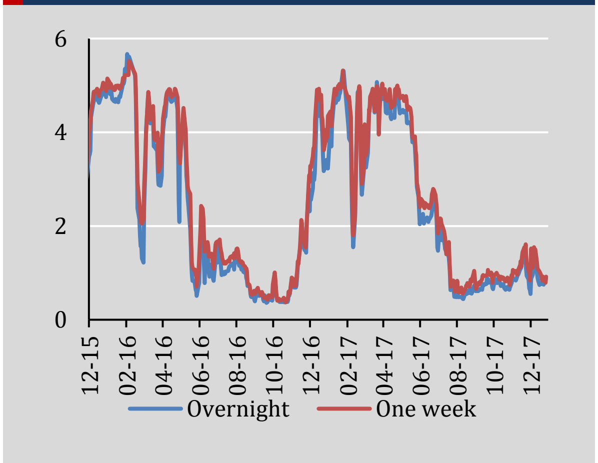
A notable event in 2017 was that the SBV issued Decision No. 1424/QD-NHNN, effective from July 10, 2017, to cut the benchmark interest rates by 0.25%/year and to reduce the lending interest rate by 0.5% for many economic sectors in the favorable context of low inflation in 2017. Rediscount and refinancing rates fell to 4.25% and 6.25%, respectively. Accordingly, all banks adjusted interest rates to create opportunities for enterprises to access capital and reduce borrowing costs, which would boost production and business activities. The stable liquidity of

Growth of M2, Deposit, and Credit, 2015-2017



Source: GSO

Interbank Offered Rate (%)



Source: CEIC

the banking system helped to keep interest rates low in the interbank market in 2017. Although interest rates fluctuated with a slight upward trend in Q4, the overnight and one-week rates were still low at 0.88% and 1.06% on average, respectively.

Credit in 2017 mostly flowed into industry and trade activities, which accounted for 78.4% of total credit. This partly explains the impressive growth in the manufacturing and service sectors. However, in the December report of the National Financial Supervisory Commission, Vietnam's credit at the end of 2017 was around 135% of GDP, higher than other countries with similar level of development. This rate is roughly equal to the level of the previous unstable period, thus posing threats to the financial balance of the banking system. Although money supply growth was lower than 2016 by two percentage points, the M2/GDP ratio in 2017 still reached 165%, much higher than the 146% in 2016. This suggests that the SBV needs to be prudent with money supply growth as it is likely to lead to an outbreak of inflation in the coming time when the lag impact of monetary policy affects the economy.

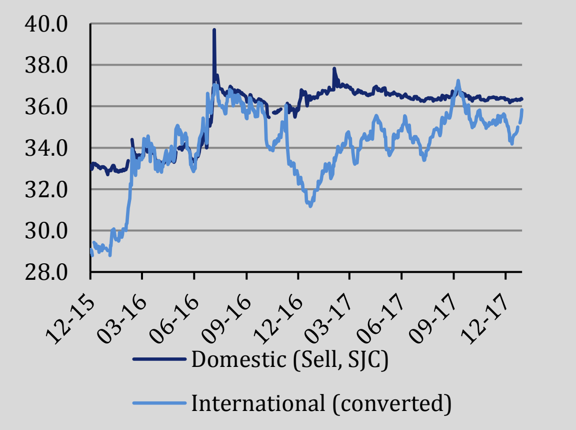
The asset market

Domestic gold price continued to remain stable

Gold price in the last quarter of the year continued the trend of the whole year. While the domestic gold price remained steady, the world price wildly fluctuated. In 2017, the domestic and world prices had been very close in the first half of September, around 36.6 million VND/tael, before uncertainties of the world market widened the price gap during the end of the year.

In the first half of December when world gold was not attractive to investors, the price gap increased, reaching more than 2.12 million VND/tael on December 12, the highest difference in Q4. World gold only rebounded after the Fed's decision to hike interest rates on December 13, bringing the world price closer to the domestic price. The domestic price was only 0.5 million VND/tael higher than the world price on the last trading day of the year, December 29.

Gold Price (mil. VND/tael)



Source: SJC, Fxpro

Real estate market remained active at the end of the year

The apartment market in the last quarter of the year was active in both Hanoi and Ho Chi Minh City, with a boom in both supply and sales. In both markets, the intermediate and low-end segments were still dominant in transactions.

According to data from JLL Vietnam, in Hanoi market, the total new apartment supply for sale in Q4 reached 9,400 units, up by 56.7% (qoq) yet only up by 2.1% (yoy). Of which, mid and low-end apartments accounted for 80.4%. Meanwhile, the numwber of successful transactions also rose sharply from 6,500 in Q3, to 9,800 in Q4, up by 50.8% (qoq).

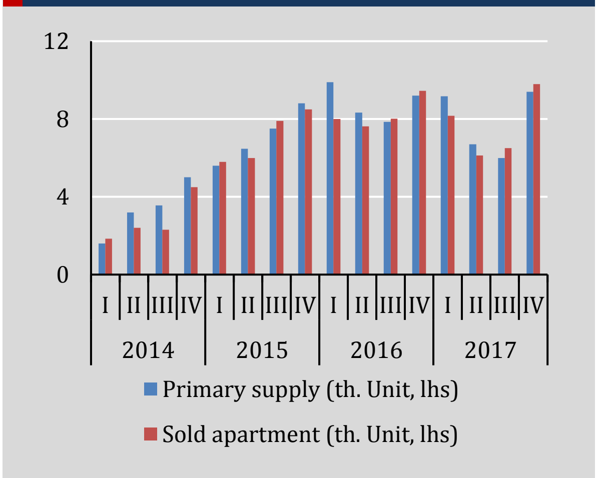
Similarly, Ho Chi Minh city witnessed a surge in both apartment supply and successful transactions, reaching 15,193 units (up by 29.4% qoq, 71.2% yoy) and 16,181 units (up by 25.2% qoq and 78.0% yoy) respectively. Of which, the number of intermediate apartments reached 6,847, accounting for 42.3% of transactions in this market.

High demand for intermediate and low-end segments contributed to a price increase in the primary market with an average of 2-3% compared to Q3. In contrast, the secondary market witnessed a price drop at 0.5% in Q4 due to the abundance of supply.

Real estate sector still attracted new foreign investors. According to data from Foreign Investment Agency of the Ministry of Planning and Investment, for the whole year, the newly registered capital in this sector reached 2.239 billion USD, accounting for 10.5% of the total newly registered capital, ranking third place after manufacturing sector and production and distribution of electricity, gas, water and air conditioning sector.

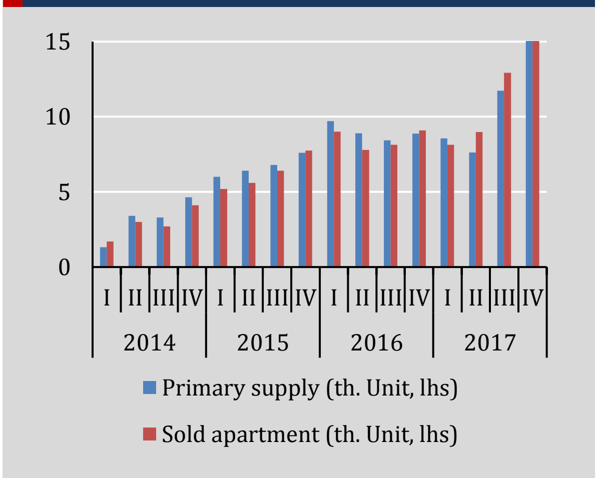
However, with the abundance of the apartment supply and credit, it is important to consider the likelihood of a price drop in the coming time when monetary policy becomes more prudent.

Hanoi's Apartment for Sale



Source: JLL Viet Nam

HCMC's Apartment for Sale



Source: JLL Viet Nam

PROSPECT FOR THE ECONOMY IN 2018 AND POLICY NOTES

2017 can be considered as a successful year of Vietnam's economy because this was the first time Vietnam fulfilled and surpassed 13 socio-economic targets set by the National Assembly. In particular, GDP growth rate was 6.81%, above the target of 6.7%, although at the beginning of the year, domestic and international experts and organizations, did not share optimistic expectations about the economy.

The massive trade surplus of FDI sector contributed significantly to the favorable balance of trade of the whole economy. On the other hand, this fact may pose a question about the sustainability of the domestic economy when it relies heavily on the FDI sector.

Contrary to forecasts of high inflation in the last quarter of the year due to the adjustment of prices of goods such as health, education, and gasoline, Q4 inflation remained stable. This reflects the flexible and prudent monetary policy of the SBV, as well as the efforts of all authorities to control market prices.

The positive balance of payments (3.4% GDP) helped the SBV to replenish its foreign exchange reserves. This created more policy space for the SBV to continue implementing easing monetary policy, lower interest rates to support economic growth. However, this continues to pose a challenge for the SBV to strictly control and sterilize this amount of foreign currencies to curb inflation and maintain macroeconomic stability in the coming time.

The stock market has grown sharply, along with the general trend around the world. The VNIndex reached the recorded level of nearly 1000 points at the end of the year, among the top five growing stock markets in the world. The market has created favorable conditions for equitization and divestment from SOEs. The equitization process has taken place in 2017 in large SOEs and is expected to continue to accelerate in 2018 when the Government has issued Decree No. 126/2017/ND-CP effective from January 1, 2018, to remove obstacles in the process of equitization of these enterprises.

The Ease of Doing Business Index (EDBI) of Vietnam announced by World Bank saw steady improvement. After rising eight levels from 2016 to 2017, Vietnam's business climate ranking for 2017-2018 continued to jump 14 levels, reflecting positive results of macroeconomic stability, and administrative and investment climate reforms. This promotes the active development of the private sector and the FDI sector, contributing to high economic growth of Vietnam.

The successful organization of APEC 2017, as well as the commitment on CPTPP agreement, opens many opportunities and challenges for the economy in the future. Tariff barriers once removed will help Vietnamese commodities to penetrate more easily to the CPTPP market. However, in the opposite direction, foreign commodities will also flow into Vietnam, creating greater challenges in improving production efficiency as well as product quality for domestic firms.

Macroeconomic stability and institutional reforms aimed at improving the investment environment are expected to continue to be effective and more supportive for business activities. 2018. However, many inherent problems of the economy which have not been resolved thoroughly will remain a drag on the economy.

Firstly, economic growth still have not come from increasing labor productivity. Vietnam's labor productivity remains low compared to other countries in the neighboring region, only 1/14 of Singapore's, 1/6 of Malaysia's and one-third of Thailand's. If there are no comprehensive measures to boost labor productivity in the near future, in the context of dwindling away demographic dividend, it is unlikely that Vietnam will be able to maintain its current growth momentum. In addition, the advantage of cheap labor will no longer be available due to the impact of Industry 4.0. In the context of depletion of natural resources, continuous decline in the production of the mining and quarrying industry, not-yet breakthroughs in the manufacturing industry, and vulnerable agriculture sector from natural disasters and climate change, the growth pressure for 2018 would be a real challenge.

Growth-Inflation forecast 2018

The 14th National Assembly's forth session passed the Resolution No. 48/2017/QH14 and set some key economic development targets in 2018 as follows:

	2018
GDP growth rate (%)	6.5-6.7%
Export turnover growth (%)	7-8%
Trade deficit/Total export turnover ratio (%)	<3%
CPI (%)	4%
Total social development investment capital (% GDP)	33-34%

Source: Resolution No. 48/2017/QH14

VEPR research team believe that such targets in 2018 are achievable in the current favorable context.

Given this situation, we forecast economic growth rate and inflation as follows:

Growth- Inflation in 2018 (%, yoy)

	Economic Growth	**Inflation**
Q1	6.02	4.14
Q2	6.41	4.41
Q3	7.08	4.69
Q4	7.27	4.03
2018	6.65	

Source: VEPR

Secondly, high budget deficit and public debt will continue to be a severe problem hindering the economy. While public investment is limited, recurrent expenditures still remain high, creating a burden on the state budget. In the context when international organizations and foreign donors will no longer provide ODA preferential loans and only offer loans with higher interest rates, Vietnam will need to use more internal resources as driving forces for growth. The government also need to take drastic measures to tighten current expenditures such as policies for personnel streamlining, restructuring the apparatus, limiting expenditures for mass organizations, and divesting and equitizing SOEs like recently.

Thirdly, the increasing dependence of Vietnam's economy on the world economy and the FDI sector also creates many uncertainties for the economy, especially in the context of the world economy in 2018 facing many geopolitical risks and the trade protectionism of major economies as well as the rapid change of science and technology in the world.

Note: Long-term and structural policies will be discussed in other policy reports of VEPR.

Abbreviations

BoJ	Bank of Japan
BoE	Bank of England
BSC	BIDV Securities Company
CNY	Chinese Yuan
ECB	European Central Bank
FDI	Foreign Direct Investment
FED	Federal Reserve
FIE	Foreign invested enterprises
FMCG	Fast Moving Consumption Goods
GDP	Gross Domestic Product
GSO	General Statistics Office
HSCB	Hong Kong Shanghai Commercial Bank
LHS	left hand side
IMF	International Monetary Fund
MOLISA	Ministry of Labor, Invalid and Social Affairs
MOIT	Ministry of Industry and Trade
mom	month-on-month
MPI	Ministry of Planning and Investment
OECD	Organization for Economic Co-operation and Development
PMI	Purchasing Manager Index
qoq	quarter-on-quarter
RHS	right hand side
SBV	State Bank of Viet Nam
UN	United Nations
USD	the United State dollar
VAMC	Viet Nam Asset Management Company
VCB	Viet Nam Bank of Foreign Trade
VND	Vietnamese currency
WB	World Bank
yoy	year-on-year
ytd	year-to-date

Disclosure appendix

Author's Certification

The following author who are primarily responsible for this report, certify that the opinion on the subject or issues and/or any other views or forecasts expressed herein accurately reflect their personal views and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendations or views contained in this research report: Nguyễn Đức Thành, Vũ Minh Long, Nguyễn Hoàng Hiệp (VEPR Macroeconomic Research Team).

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Additional disclosures

This report is dated as January 16, 2018. All data included in this report are dated December 31, 2017 unless otherwise indicated in the report.

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CONTACT US

Viet Nam Institute for Economic and Policy Research
University of Economics and Business, Viet Nam National University, Ha Noi

Address:	Room 707, E4 Building 144 Xuan Thuy strt, Cau Giay dist Ha Noi, Viet Nam
Tel:	(84-24) 3 754 7506 - 704/714
Fax:	(84-24) 3 754 9921
Email:	info@vepr.org.vn
Website:	www.vepr.org.vn