Navigator

Now, next and how for business

Vietnam report

HSBC

Vietnam

Foreign investments remain key in servicing fast-growing external demand

Surging manufacturing-related foreign direct investments have turned Vietnam into a 'near-shore' production base for East Asian manufacturers. Low wages and an improving business climate should ensure continuation of this trend in the near-term, while the implementation of trade deals such as the CPTPP would give an additional boost to Vietnam's buoyant exports and support diversification into new markets.

Short-Term Snapshot

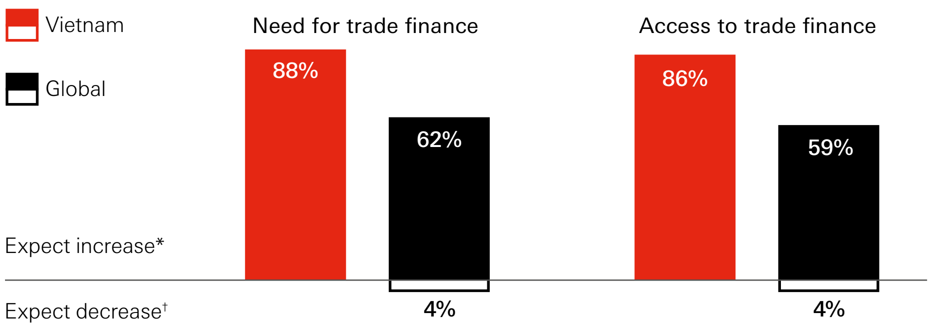
Vietnam's economy remains among the fastest-growing in Southeast Asia. The surge in manufacturing activity in the second half of 2017, helped mostly by FDI-related merchandise exports, looks to have helped Vietnam's economy to grow in excess of 6% for the third year in a row. While goods exports (in US$ terms) jumped an estimated 20% in 2017, we predict services exports grew slightly faster (8%) last year. Looking ahead, Vietnam's low-wage workforce, a rising number of trade agreements, and its improved business climate will likely continue to attract substantial FDI inflows.

Buoyant demand among major global economies such as China, the US and the Eurozone are driving the positive near-term outlook for global trade. Thanks to its high openness to trade and continued attractiveness to foreign manufacturers as a production base, Vietnam is ideally-placed to benefit from this trend. Our survey results reflect these factors: A favourable economic environment and increasing demand for their products are seen as the top growth factors for cross-border trade among Vietnamese companies. Firms are particularly optimistic about the growth outlook in key destinations such as China, Japan and Korea, which currently account for almost 30% of Vietnamese merchandise exports.

Action points for business

- Firms should see the strong demand outlook for Asian economies as an opportunity to expand regional trade linkages and diversify their export markets.
- Attracting foreign investments to the manufacturing sector will remain a key strategy in ensuring firms are able to compete with regional peers. Firms should demonstrate their support for government efforts to improve the business climate and strengthen investor protection.

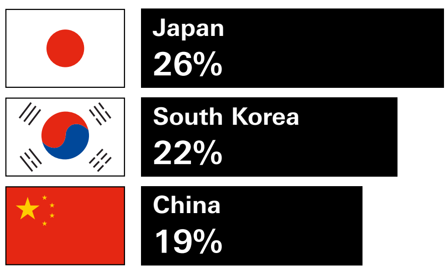
Outlook for trade finance need and access in the next 12 months



*Expect increase = Increase significantly + Increase slightly
†Expect decrease = Decrease significantly + Decrease slightly

Source: TNS Kantar

Which are the top 3 markets where your business will look to expand in the next 3-5 years?



Source: TNS Kantar

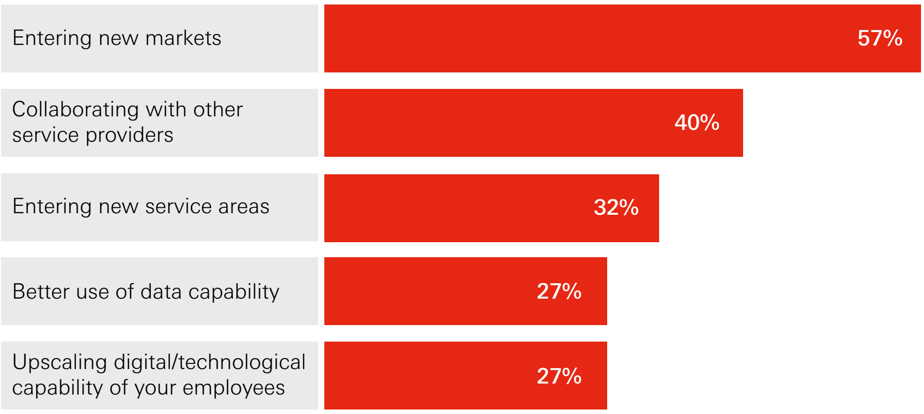
In line with the optimistic trade outlook 88% of surveyed companies report a need for increasing trade finance to meet the rising demand. While some firms feel that high transaction costs and exchange rate volatility could be major obstacles, 86% still believe that their needs will be matched with improved access to finance.

Trade in services are substantially outweighed by cross-border flow in goods – in 2016, services contributed only 4% to the increase in total exports (in US$ terms). And while exporters are generally optimistic about the near-term outlook for services trade, only around half of the surveyed companies indicate this is an important source of export revenue.

Tourism is projected to remain the key sector among services (currently accounting for more than 60% of total services exports), thanks to rising incomes and living costs in neighbouring countries.

Continued investment inflows and strong external demand momentum should continue to boost Vietnam's manufacturing industry.

How do you plan to grow your services business?



Source: TNS Kantar

Trade Policy Developments

Vietnam's accession to the Association of South-East Asian Nations (ASEAN) in 1995 and its WTO membership (2007) have driven a step-change in its relations with the wider world. Export volumes have grown at double-digit annual rates consistently for the past 20 years, except during the global financial crisis. Although future trade agreements are not explicitly factored into our forecast, Vietnam is clearly well-placed to gain most from future initiatives, such as the recently signed CPTPP and the Regional Comprehensive Economic Partnership (RCEP).

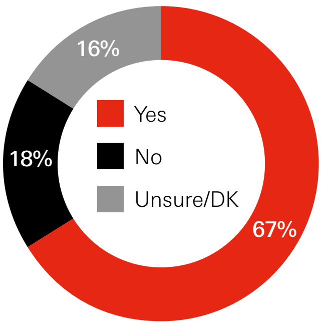
Vietnamese companies are justifiably upbeat about both ongoing and new trade agreements. Deepening cooperation amongst ASEAN economies is seen as the most relevant development in this respect for Vietnam. Around three-quarters (74%) of survey respondents indicate the ASEAN Vision 2025 would further help grow their exports, while 63% are convinced CPTPP would boost their trade prospects.

> Businesses are confident new trade deals will have positive impact on growth.

Action points for business

- Firms are advised to support pro-trade government initiatives such as RCEP and ASEAN Vision 2025, to ensure Vietnam remains an attractive location for growth-enhancing foreign direct investments in the region.
- Businesses should make sure they understand the implications of upcoming trade initiatives such as "Belt and Road" and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), to make sure they are in a good position to seize the benefits from planned infrastructure investments and higher connectivity.

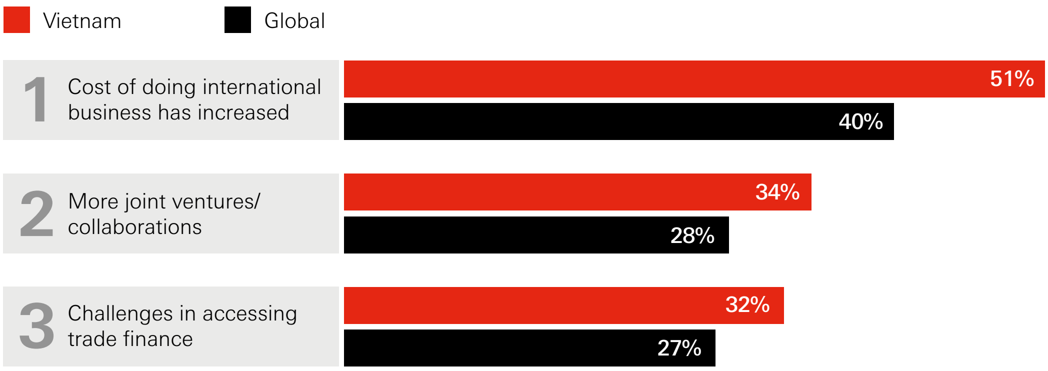
Are governments becoming more protective of their domestic business?



Note: may not total 100% due to rounding

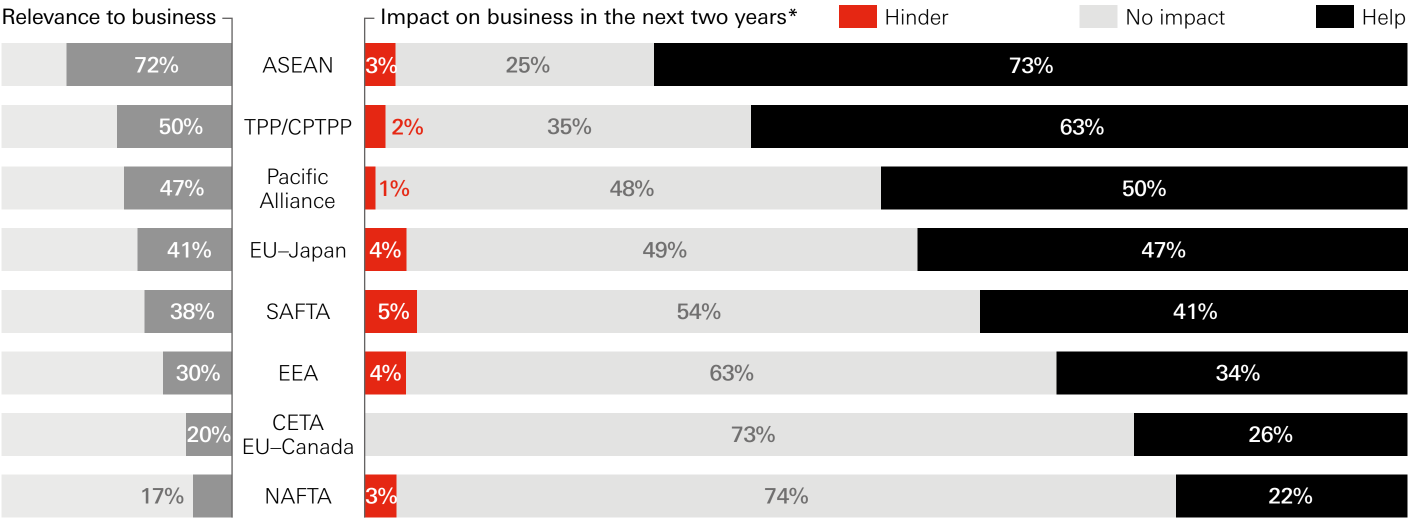
Source: TNS Kantar

Top 3 impacts of protective policies on my business



Source: TNS Kantar

Relevance and impact of trade agreements



Source: TNS Kantar

*May not total 100% due to rounding

Long-Term Outlook for Trade

Vietnam is well positioned to enjoy high growth in trade and investment beyond the near-term – provided it can continue to successfully leverage its key competitive advantages in the region, which are its skilled and low-wage workforce and its openness to trade.

According to our baseline projection, which assumes the status quo in trade policy is maintained, Vietnamese merchandise exports (in US$ terms) will grow at an average 10% per year from 2021-30, while services exports will increase at 7% per annum over the same period. As a result, total exports will stand US$750 billion in 2030 – four times higher than in 2016. In terms of structural developments, we expect FDI-related ICT exports to retaining its top position among goods flows, and tourism to continue dominating services exports.

New trade policy initiatives within ASEAN, as well as RCEP and CPTPP, could provide an additional boost to trade. However, the high exposure to regional demand and reliance on the ICT sector also mean there are downside risks associated with potential disruption to these flows.

US and China to drive demand for manufactured products
Vietnam's industry has been boosted by foreign investments in recent years, enabling a structural shift toward higher-value manufacturing such as electronics and machinery. With its abundant and low-wage labour force and high openness to trade, it continues to be attractive to foreign investors, predominantly from East Asia, who use it as a regional base for production and final assembly.

We expect electronics-related goods, which account for 27% of goods exports, to remain the key driver over the long-term, contributing almost a third to the overall increase in merchandise exports to 2030, followed by clothing and apparel (20%). We also expect investment inflows to help Vietnam become more competitive in the region – it is projected to outperform Bangladesh and India in key sectors such as textiles and ICT.

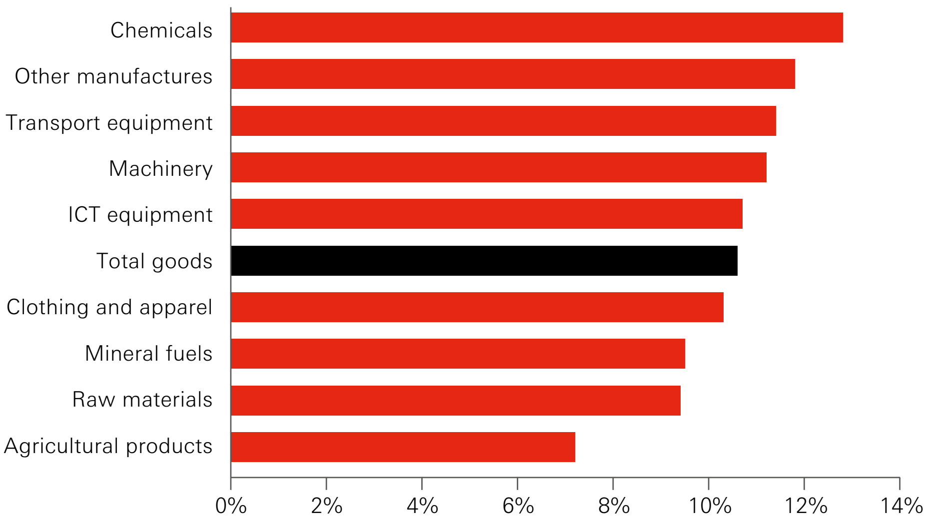
In addition, high-tech goods such as industrial machinery and precision instruments will slowly gain share, reflecting a gradual move up the value chain and spill-over of technology and skills from foreign direct investments.

Action points for business

- Firms should continue seeking opportunities to engage in the supply chain for higher-cost producers elsewhere. This can range from supplying inputs to offering IT and other business support services - a fast-growing market that has considerable potential for growth in Vietnam.
- Businesses should also lobby for trade facilitation policy and necessary trade infrastructure investments to cater for the projected increase in global demand.
- Tourism firms should ask themselves why they lag behind competitors in Thailand and Malaysia. Asian incomes are rising, tourism is gaining importance and Vietnamese firms need to ensure they benefit.

ICT and clothing will remain the dominant export sectors …

Exports of goods by sector, 2017-30 (average annual growth)



Source: Oxford Economics

Top 5 Hotlist destinations of goods exports

Rank	2016	2030
1	USA	USA
2	China	China
3	Japan	Korea
4	Korea	Japan
5	Hong Kong	UAE

Note: Ranking among the 24 trade partners covered in the forecast

Source: Oxford Economics

Demand from the US and China will likely remain crucial in the future. Between 2017 and 2030, these two economies combined are projected to contribute 35% of the overall increase in goods exports. The US will retain its top spot as the single most important export destination over the forecast period to 2030. However, while the US is by far the most important market for the Vietnamese textiles industry, sucking in almost 50% of all clothing exports, demand from Asian economies is more balanced across sectors, with 30% of ICT-related goods and 25% of clothing exports going to regional peers – offering more diverse growth potential in higher-value sectors.

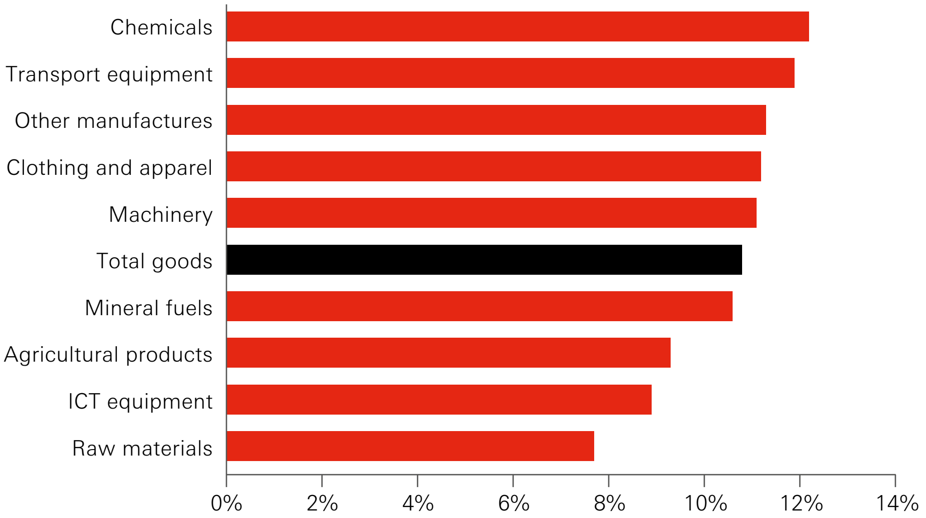
…boosted by demand from its two key destination markets, US and China.

Our survey shows Vietnamese exporters are aware of these opportunities, with Japan, Korea and China seen as the most important growth markets for exports. Our forecast supports this view, reflecting the strong regional supply-chain linkages in manufacturing industries. Participation in new trade deals such as RCEP and CPTPP could help diversify the mix of destinations and exported products further.

Machinery and parts for assembly continue to be sourced from abroad
Much like exports, the composition of imports reflects Vietnam's structural shift to providing a regional base for industrial production and final assembly. Industrial machinery, which is required both for development of production capacity as well as trade infrastructure, accounted for 24% of goods imports in 2016 (based on imports from the 24 trading partners analysed this report), up from 18% in 2010. Assuming continued foreign investments into Vietnamese production plants, we forecast machinery to contribute around a quarter of the increase in imports from 2017-30.

Other inputs for assembly, such as parts for ICT equipment and wood & textile manufactures, will also remain important drivers of trade, accounting for a further 20% of the projected increase in merchandise imports until 2030. Overall, manufactured goods will account for over half of all imported products through to 2020 and beyond, but final goods will likely become more important in this mix, as domestic demand increasingly benefits from foreign investments and buoyant trade.

Imports of goods by sector, 2017-30 (average annual growth)



Source: Oxford Economics

Top 5 Hotlist origins of goods imports

Rank	2016	2030
1	China	China
2	Korea	Korea
3	Japan	India
4	Singapore	Singapore
5	USA	Japan

Note: Ranking among the 24 trade partners covered in the forecast

Source: Oxford Economics

The composition of Vietnam's trading partners illustrates the close supply chain linkages in South-East Asia – China, Korea, Japan and Singapore all feature among the most important import origins, with China occupying the top spot through to 2030. Chinese and Korean imports can be mainly attributed to electronics and textiles manufacturing in Vietnam – the two economies account for 68% of all ICT-related goods and 90% of supplies for the clothing industry, and this trend is set to continue over the forecast horizon, with Korea gradually gaining share from China.

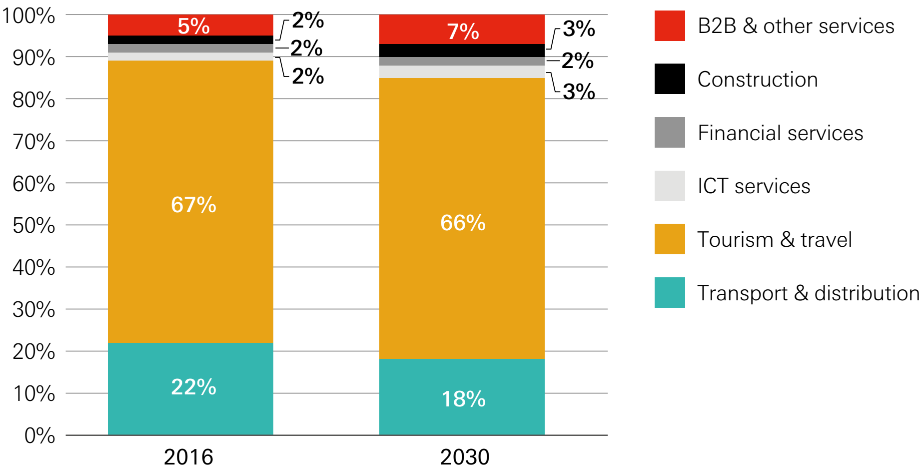
East Asian economies set to remain crucial suppliers of parts & materials for assembly.

Despite the relevance of East Asian suppliers, imports from India and European economies are the fastest growing in the near-term. Purchases from India will remain the fastest growing out to 2030, making it the third most important supplier for Vietnam in 2030, and ongoing bilateral negotiations between Vietnam and India on trade and investment could provide a further boost to cross-border flows between the two countries.

Services likely to benefit from expanding goods trade, but with potential for faster growth

Although exports are largely dominated by merchandise trade, the outlook for services also bears considerable potential, thanks to the improving business climate – the World Bank now ranks Vietnam 68th out of 190 countries, an improvement of 14 from the previous year – and rising incomes in key markets like China and ASEAN.

Sectoral shares in total services exports



Source: Oxford Economics

Top 5 Hotlist destinations of services exports

Rank	2016	2030
1	Japan	China
2	China	USA
3	USA	Japan
4	Singapore	Singapore
5	Australia	Australia

Note: Ranking among the 23 trade partners covered in the forecast

Source: Oxford Economics

Overall, services exports will likely remain concentrated in tourism and, to a lesser extent, transportation, which will benefit both from steadily increasing visitor numbers and healthy growth in merchandise trade. These sectors combined are projected to contribute more than 80% to the overall increase in services exports (in US$ terms), which are forecast to grow at an annual average of 8% until 2030, in the long term.

Despite its importance for total service exports, tourism in Vietnam is still dwarfed by regional competitors Thailand, Malaysia and Indonesia. Given its tourist attractions and favourable climate, improvements in marketing and tourism infrastructure could unlock substantially faster growth in travel-related services exports for Vietnam.

> Additional investments could unlock high growth potential in the tourism sector.

While Japan, China and the US are currently Vietnam's most important markets and will remain so until 2030, services are much more diversified across destination markets than goods exports. The top three markets only have a combined share of 22%, and this will fall to 21% by 2030 as other destinations in Asia and the Middle East gain more share, reflecting increasing incomes therefore opportunities for Vietnam's tourism industry.

Cross-border services flows to India are projected to be the fastest growing in our forecast, expanding at 11% per year to 2030, followed by China which will see imports from Vietnam growing at 10% in the long term. This reflects the growing share of regional markets in Vietnamese merchandise trade, which is often bundled with transport and business services. And new trade deals could provide an extra boost – exporting firms seem particularly optimistic about growth in services revenue when it comes to participation in new trade deals.

About the HSBC Navigator

The HSBC Navigator presents a blend of survey evidence, policy analysis, and economic modelling to generate unique and timely insights into the changing landscape for global trade.

The business survey is a quantitative indicator of the short-term outlook for global trade. The survey, which is the largest of its kind, is conducted on behalf of HSBC by Kantar TNS. It is compiled from responses by decision-makers at over 6,000 businesses – from small and mid-market to large corporations – across a broad range of industry sectors in 26 markets. Interviewees were polled on a range of questions including expectations around future growth in trade, trade finance needs, attitudes toward trade policy developments and strategic business plans.

The survey represents a timely source of information on the fast-evolving trade environment. And it can provide a useful contextual setting for interpreting developments in official data. In this way, economists at Oxford Economics are able to blend insights from the survey with their own analysis and modelling of developments in trade.

Oxford Economics has tailored a unique service for HSBC which forecasts bilateral trade in goods and services, in part based on HSBC's own analysis and forecasts of the world economy. A top-down approach is employed, with Oxford Economics' suite of models used to ensure consistency between HSBC's forecasts for economic growth and exchange rates in key countries and the more granular projections for bilateral trade flows presented here.

Oxford Economics employs a global modelling framework, with headline bilateral trade forecasts constructed as a function of demand in the destination market and the exporter's competitiveness (as measured by unit labour costs in nominal USD terms). Exports, imports and trade balances are identified, with both historical estimates and forecasts for the periods 2017-20 and 2021-30.

These headline bilateral trade forecasts for goods and services are also disaggregated by sector, using Oxford Economics' Industry forecasts to inform future production trends and taking into account the historic relationship between output and exports in each sector, by market:

- For trade in goods, sectors are classified according to the UN's Standard International Trade Classifications (SITC) system at the two-digit level and grouped into 30 sector headings.
- For trade in services, we identify five broad sectors: B2B and other services, tourism & travel, transport & distribution, financial services, ICT services and construction.

Drawing on the Kantar TNS survey results and Oxford Economics' long-term forecasts, Oxford Economics produces in consultation with HSBC a global report and specific reports on the following 23 markets: Argentina, Australia, Bangladesh, Canada, China, Egypt, France, Germany, Hong Kong, India, Indonesia, Ireland, Japan, Malaysia, Mexico, Poland, Saudi Arabia, Singapore, Turkey, UAE, UK, USA and Vietnam. The analysis of trade in goods also includes trade with Brazil and Korea for a total sample of 25 key trading markets; for trade in services the analysis also includes Korea for a total sample of 24 key trading markets.

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