Vietnam’s Economic Outlook

The Vietnamese economy has recovered from a three-year soft patch. After dropping to its slowest pace in 13 years in 2012, growth has been on an upward trend and ended 2015 at a five-year high of over 7%. Given the strong momentum going into 2016, the economy is expected to continue growing at an impressive rate of around 6.8% this year, up slightly from 6.68% in 2015 and 6% in 2014.

A strong recovery in the property market is the main driver behind Vietnam’s economic rebound. Growth took a dive in 2011 following a burst in the nation’s housing market bubble, which developed after the government’s massive stimulus spending during the 2008-09 financial crisis. In an effort to improve conditions in the property market and spur growth, the government has cut interest rates several times and purchased around $8 billion of banks’ nonperforming loans. These efforts have alleviated the burden of debt and lifted credit growth in the economy.

The property market has also benefited from new laws allowing foreign investors to purchase Vietnamese real estate and fully own some of the nation’s locally listed companies. These new laws have caused foreign investment, which accounts for 20% of the Vietnamese economy, to surge to a record high. Although commercial real estate sales are experiencing the strongest gains, accounting for half of last year’s total foreign investment, activity is also picking up in the residential market. Meanwhile, domestic buyers are also rushing in to purchase homes before a potential spike in prices caused by the influx of foreign buyers. As a result, home sales in 2015 almost doubled compared to 2014 levels.
Foreign investment is expected to strengthen further this year as a result of a slew of recent trade deals, including a new pact with South Korea, the nation’s top foreign investor. Vietnam is also a participant in the massive Trans-Pacific Partnership (TPP), a 12-country trade deal that includes the U.S. and Japan. Although negotiations of the TPP’s terms concluded at the end of last year, the agreement still needs to be ratified by most countries’ legislatures. If finalized, the TPP will be the largest trade deal in the region’s history and allow Vietnam to trade tariff-free with countries that make up around 20% of world trade. In addition to these significant trade deals, Vietnam is also a member of the newly-established ASEAN Economic Community (AEC), which aims to further free trade and investment in the region.

Not surprisingly, these trade deals and partnerships are expected to have a very positive impact on Vietnam’s foreign investment and trade this year. Exports are also expected to benefit from the State Bank of Vietnam’s recent shift toward a more market-based currency, which involves updating the dong’s fixed reference rate on a daily basis and widening its trading band from 1% to 3%. The move is expected to alleviate sudden shifts in the dong, which has experienced downward pressure over the last year due to the strengthening dollar. The weaker dong will continue to increase the price-competitiveness of Vietnamese goods and support robust exports growth in the near term.

Meanwhile, despite the weaker dong, imports are also growing at a solid rate; rising production is increasing firms’ demand for intermediate goods imports, while improving economic conditions have increased the demand for consumer goods imports. This trend is expected to continue in the near term as domestic demand strengthens following the government’s efforts to lift foreign investment and liberalize trade.
Domestic demand will also continue to be supported by the nation’s very low inflation. Owing largely to declining oil prices, Vietnam’s inflation rate dropped to its lowest rate in 14 years in 2015 to 0.6%. As a result, the policy rate has remained at 6.5% since March 2015 and changes are not expected in the near term given the favorable economic conditions and benign inflation.

The low inflation rate has lifted domestic purchasing power and driven consumption and investment to grow at their fastest rates since 2010. Although this trend is expected to continue in the near term, inflationary pressures will likely increase slightly this year as a result of a low base-effect and higher imported inflation caused by a weaker dong.

Overall, we see that the Vietnamese economy has recovered nicely from its previous soft patch. The slowdown was primarily the result of a crash in the nation’s housing market, which has since experienced a strong rebound due to the government’s efforts to lift credit growth and attract foreign investment. As a result of a slew of recent trade deals with key partners, including the U.S., Japan, and South Korea, rising foreign investment and exports will continue to be main drivers of economic growth in the near term. Meanwhile, domestic demand will also continue to strengthen, as consumers and firms benefit from improving economic conditions and low inflation. The economy is expected to gain steam and grow by around 6.8% this year.