CLMV Monitor

Q1 | 2019

SCB
Economic Intelligence Center

CLMV Monitor
Q1 | 2019

The CLMV economy is likely to continue its brisk growth of around 6-7% in 2019. Effects from the global economic slowdown are expected to be limited, thanks to continued inflows of foreign investment in infrastructure construction and factory expansion. Amid rising tension from the US-China trade war, Vietnam is emerging as an FDI safe haven. Many China-based manufacturers have decided on investment relocation to Vietnam to avoid import tariffs from the US and utilize the country's advantages. Seeing brighter prospects going forward, tourism would be another spearhead industry supported by the CLMV governments. China and other Asian countries have been the largest sources of foreign tourists and the number continues to rise. Exports are expected to maintain growth momentum, with strong international demand for CLMV-made products under the preferential trade treatment. Nonetheless, near-term risks come from both external uncertainty and country-specific challenges. These include fluctuations in local currencies, a potential loss of EU preferential trade treatment in response to human rights abuse in Cambodia and Myanmar's Rakhine State, and Vietnam's growth concentration in foreign-invested sectors.

Cambodia

Cambodia's economy will maintain steady growth at 6.8% in 2019 due to strong external demand. Exports is expected to accelerate until the withdrawal of EU's EBA takes effect in August 2020. Tourism activities have grown significantly in recent years and the momentum continues, with China as the largest source of tourist arrivals.

Laos

Laos' economy is expected to achieve higher growth of 7% in 2019-2020, led by electricity exports and the construction sector. However, the continued depreciation of Lao kip and a prolonged trade deficit pose key risks to economic growth and stability.

Myanmar

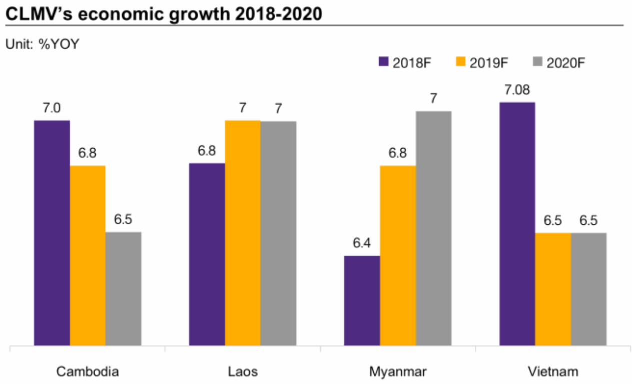
Myanmar's economy is expected to recover to 6.8% in 2019, with robust export growth. Meanwhile, manufacturing and services are expected to grow at around 8%. The possible sanction regarding the Rakhine crisis has added risks to economic growth and development this year and the next.

Vietnam

After achieving 7.08% growth in 2018, the Vietnamese economy is likely to maintain good momentum thanks to FDI inflows from the relocation of China-based manufacturer to avoid higher tariffs from the US. The key challenge to Vietnam is a high growth concentration in the foreign-invested sector, while technology transfers remain low.

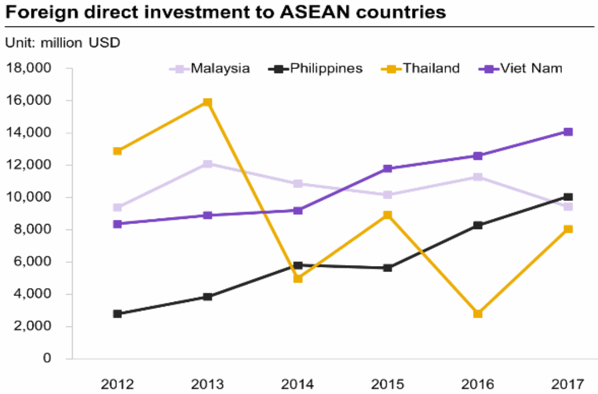
Box: Vietnam emerges as the FDI safe haven amid the trade war

CLMV economies will maintain their robust growth in 2019 and beyond.



Source: IMF WEO October 2018 and Vietnam's GSO

FDI to Vietnam outpaced its ASEAN peers and is likely to continue rising with factory relocation from China-based manufacturers



Source: World Bank and ASEANStats

CAMBODIA

OVERALL ECONOMY

Facts and Figures

Population (2018)	16.45 million
Labor force (2017)	8.9 million
GDP (2017)	22.3 USD billion
GDP per capita (2017)	1,390 USD
GDP by sector (2017)	Agriculture: 25.3%, Industry: 32.8%, Services: 41.9%
Top exports (2017)	Textile 65%, Footwear 11%, Travel goods 3%

Things to watch in 2019

Negative impact of Hard Brexit and EU's EBA withdrawal on Cambodia economy

Development of financial sector to serve increasing financing needs

Macroeconomic update

Economic Outlook

The Cambodia economy will maintain healthy growth of around 6.8% in 2019 as strong external demand continues. In 2018, exports increased 21%YOY, supported by rapid growth in garment and footwear and other emerging products such as travel goods and bicycles. Export growth is expected to remain robust in 2019, particularly in the 2 biggest trading partners with preferential trade treatments, before the EU makes a final decision to withdraw Everything But Arms (EBA) benefits in August 2020. Trade deficit will continue in the medium term due to increasing domestic demand for imports of construction materials, raw materials for manufacturing, vehicles, and food-related products. This, however, is expected to be partially offset by a surplus from foreign direct investment and tourism receipts. The tourism sector has been a new engine of growth in recent years and, in 2018, the Kingdom welcomed 6.2 million international visitors, increasing 11%YOY, of which 2 million were Chinese tourists. With a significant increase in terms of arrivals and spending of Chinese tourists, the government announced 2019 to be the China-Cambodia Cultural and Tourism Year.

Nevertheless, Cambodia now faces the dire prospect of higher tariffs as the risks of the UK's Hard Brexit and the EU's EBA withdrawal have increased. In a Hard Brexit scenario, by which Britain leaves the UK without a deal, duty and quota free access to the UK market under the EBA, granted for least developed countries, will be automatically canceled. Cambodia is expected to suffer the highest losses as the UK is its third largest export market, accounting for 9% of total exports in 2018. Furthermore, the EU began the 18-month process of EBA withdrawal over a deterioration of democracy and respect for human rights in Cambodia. With the EU dominating almost 40% of the Kingdom's exports in 2018 (Figure 1), the loss of access to the EU market would have a devastating impact on the export-oriented manufacturing sector, particularly, garment and footwear (Figure 2). A tariff of 17% will make the garment and footwear sector become less competitive, given already relatively higher production costs to peers. Around 800,000 workers will be at risk of losing their jobs and returning to poverty. The EU has given the Cambodian government 1 year to engage with the EU to improve the situation and avoid having privileges removed. If this fails, the final decision on full or partial withdrawal of the EBA scheme would come into effect in August 2020.

Many actions have been taken by the government to facilitate business. The budget is set for a deficit at 3.3% of GDP in 2019, increasing both current and capital spendings. The fiscal deficit is expected to widen further to 3.7% of GDP by 2023. Amid increasing external uncertainties, the government announced measures to lower operating costs and improve competitiveness for exports, including the elimination of export procedures, cancelation of Certificate of Origin application, and the removal of Kampuchea Shipping Agency and Brokers. It is expected that the government and related ministries will release new sub-decrees and Prakas in pipe line in order to help business.

Figure 1: EU is the Kingdom's largest export market in 2018, followed by US and UK.

Exports by country 2018

Unit: % of total export

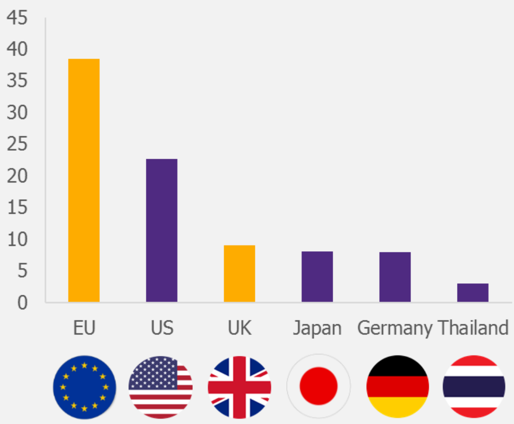
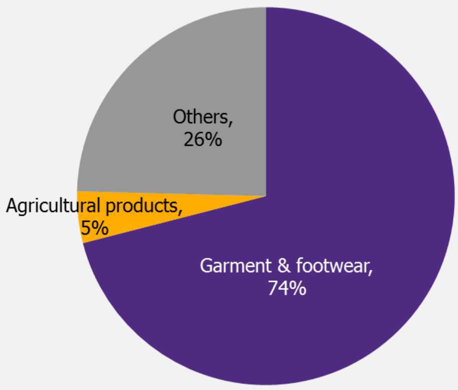


Figure 2: Garment and footwear products have dominated 74% of total exports.

Exports by product 2018

Unit: % of total export



Source: EIC analysis based on data from The National Bank of Cambodia

Financial markets

The financial sector saw a solid growth with continued development. The banking sector expanded with a 19% increase in loans and a 15.3% rise in deposits in 2018. The nonperforming loans ratio also dropped to nearly 1% last year. Later in 2019, the government is set to launch SME bank with an initial capital of USD 100 million to provide financing for small and medium enterprises (SMEs). The new bank will prioritize SMEs linked with ago-business, tourism, tech start-up, and other new economic engines. For the bond market, LOLC (Cambodia) Ltd will introduce a new product, called forex-indexed bond. In addition, the Cambodia Securities Exchange (CSX) market capitalization increased 44%YOY in 2018 and is expected to rise further as the government offers the 3-year 50% reduction in income tax and the elimination of tax debt for listed companies making initial public offerings of equity or debt securities. The continued development of financial products is in line with Cambodia's increasing domestic financing needs.

EIC's view

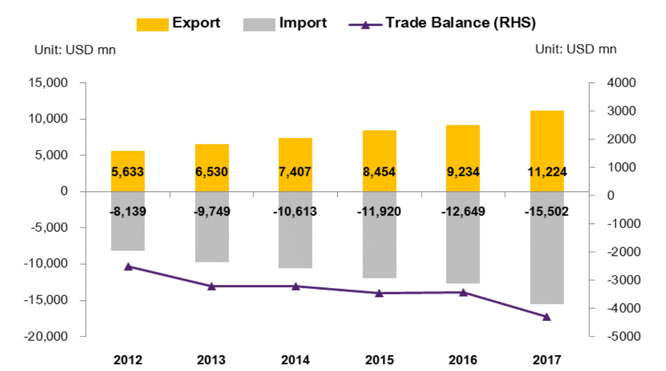
Business activities are promoted by government measures and financial product development. The Cambodian government has implemented a number of measures to support local and foreign investors facing rising challenges from the Hard Brexit or the potential loss of EBA preferential treatment granted by the EU. The government also aims to promote economic diversification and support SMEs in building new economic drivers apart from the garment and footwear sector. These include 6 prioritized industries like ago-business, manufacturing raw materials, and tourism. The financial sector is developing along with solid economic growth. With more variety of financial products available in the market, businesses at any size will be able to obtain a better access to funding. Thailand, as one of the Kingdom's top traders and investors, would also enjoy the better business environment in Cambodia. Opportunities for Thai business will arise in manufacturing and services to support the domestic market, such as, processed food, consumer goods, and tourism services.

Cambodia's Key Indicators

Indicators	Unit	2013	2014	2015	2016	2017	2018E	2019F
Real GDP	% YOY	7.4	7.1	7.0	7.0	6.9	7.3	7.0
Consumer price index	%	4.7	1.0	2.8	3.9	2.2	2.6	2.8
Current account balance	% of GDP	-8.4	-8.5	-8.7	-8.4	-8.0	-10.1	-9.9
Policy rate (end of period)	%	1.3	1.4	1.4	1.4	1.4	1.4	1.4

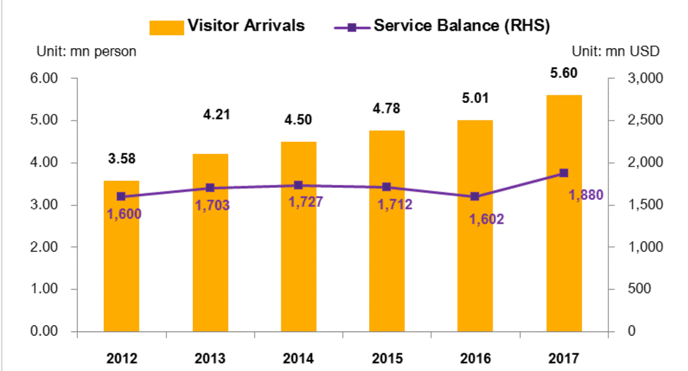
Sources: International Monetary Fund (IMF) and The National Bank of Cambodia

Trade deficits widened due to strong import demand



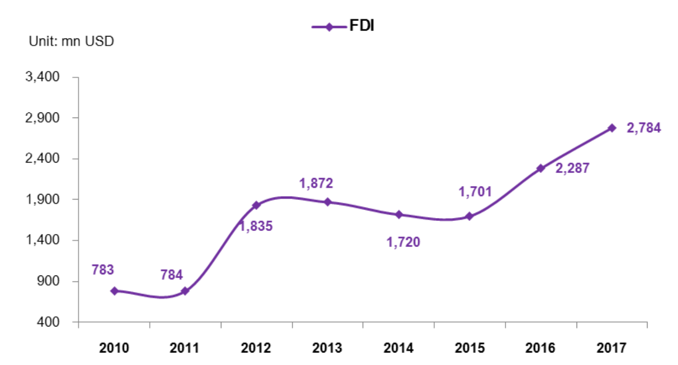
Sources: World Bank

Number of tourism visitors continued to rise



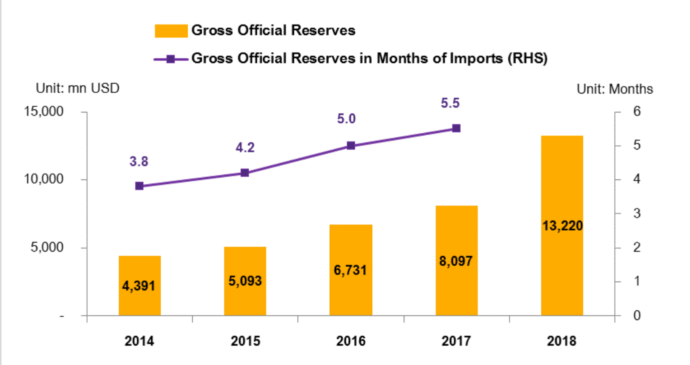
Sources: World Bank and CEIC

Cambodia is among investment-friendly economies



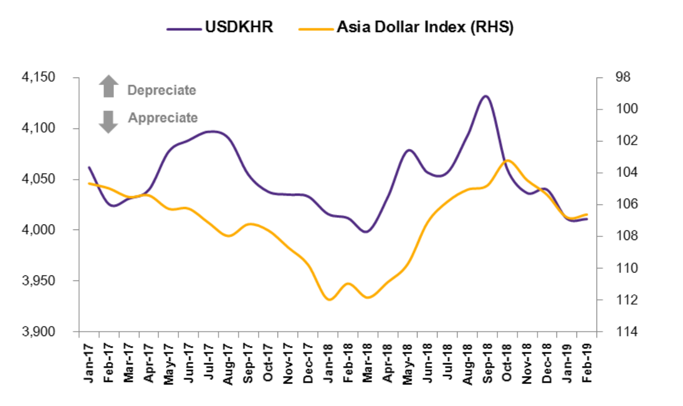
Sources: World Bank

Reserves buffers were higher than a 3-month standard



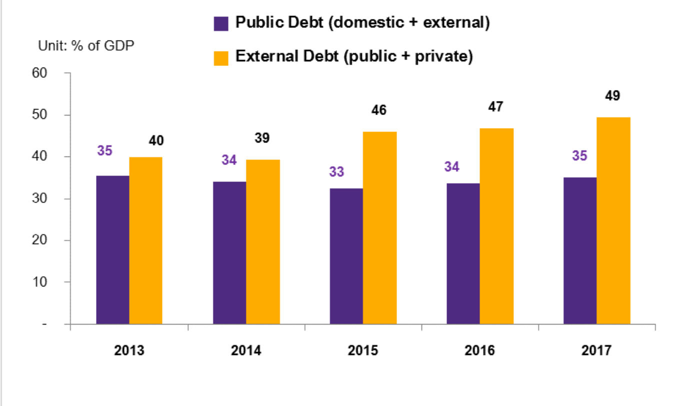
Sources: IMF

KHR has maintained its value around 4,050 per USD



Sources: Bloomberg

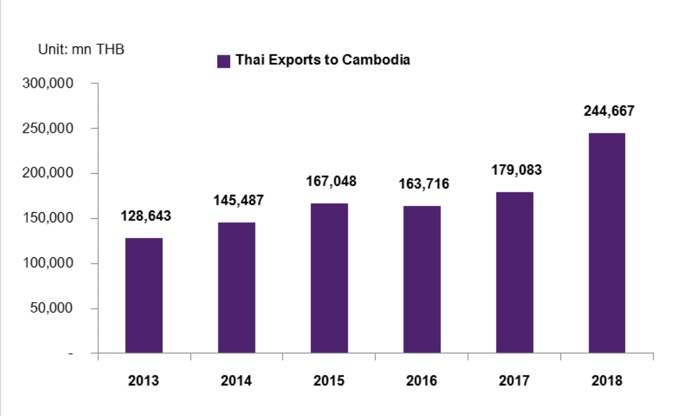
External debt was in manageable level



Sources: International Monetary Fund (IMF) and CEIC

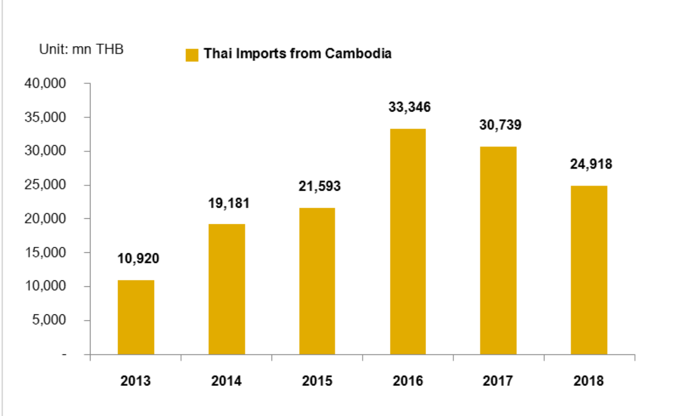
Links with Thai Economy

Exports to Cambodia rose sharply in 2018, moving toward USD 15 billion bilateral trade commitment by 2020



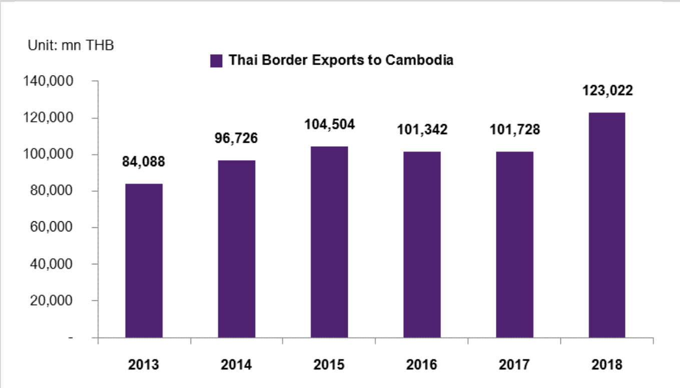
Sources: Thailand's Ministry of Commerce

Imports from Cambodia have grown moderately



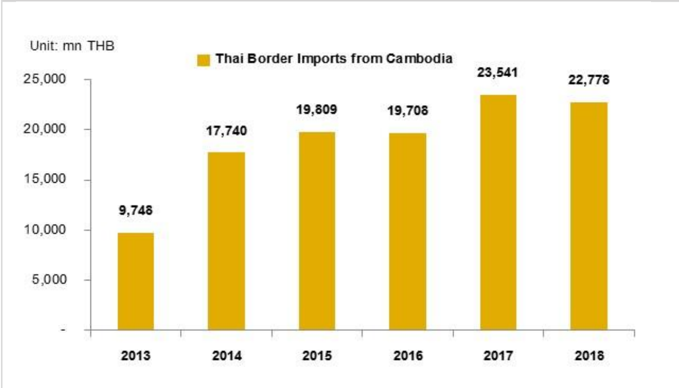
Sources: Thailand's Ministry of Commerce

Thai exports via borders were around half of total exports to Cambodia in 2018



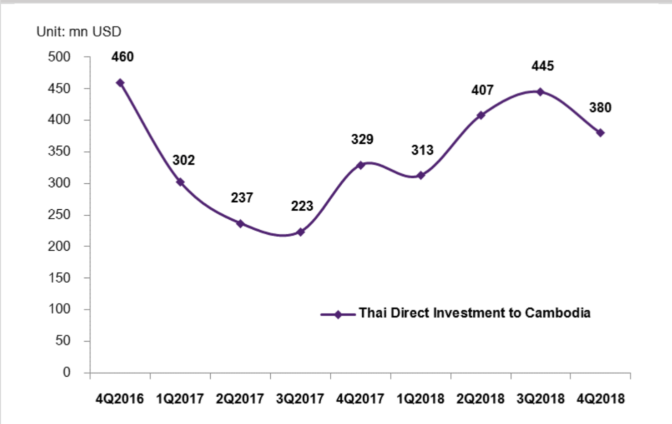
Sources: Thailand's Department of Foreign Trade

Almost all Thai imports from Cambodia in 2018 were through borders.



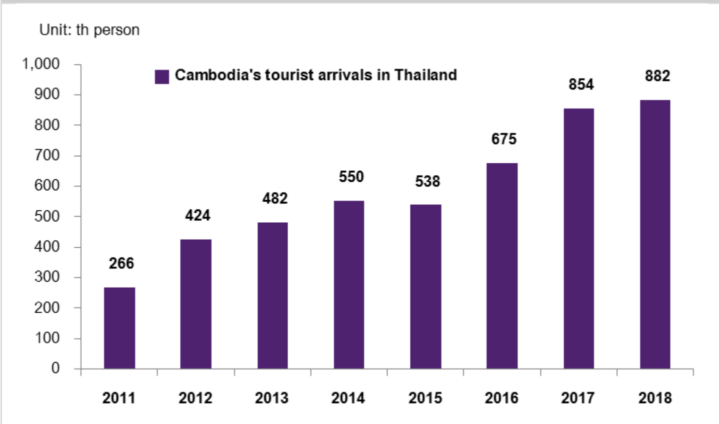
Sources: Thailand's Department of Foreign Trade

Thai direct investment in Cambodia has been growing to achieve a double investment value by 2020



Sources: Bank of Thailand

Despite a gradual improvement, the number of Cambodian traveling to Thailand remained small in 2018



Sources: Thailand's Department of Tourism

LAOS

OVERALL ECONOMY

Facts and Figures

Population (2017)	7.13 million
Labor force (2017)	3.6 million
GDP (2017)	17.15 USD billion
GDP per capita (2017)	2,568 USD
GDP by sector (2017)	Agriculture: 20.9%, Industry: 33.2%, Services: 39.1%
Top exports (2017)	Electricity 24%, Copper 20%, Electrical product 12%

Things to watch in 2019

Effect of "Visit Laos-China 2019" campaign on tourism sector

A continued depreciation of Lao kip value

Macroeconomic update

Economic Outlook

Laos' robust economic growth is likely to continue in 2019-2020. The IMF expects the Laos economy to expand by 7% in 2019 and 2020. Electricity exports and the construction sector are the two key growth drivers. Major construction projects in the pipeline include the China-Laos railway, hydropower work, and infrastructure in special economic zones. Electronics manufacturing is yet another rising star, with an expanding share in exports. During 2010-2017, the average growth of electronics exports was 65% per year, surpassing that of electricity at 41%. Such positive prospects have encouraged overseas investment in the sector. In February, Japanese optical product manufacturer Hoya Corporation invested over USD 300 million to build a new hard disk drive memory disk production factory in Vientiane. In addition, a "Visit Laos-China Year 2019" tourism campaign will be another boost to the Lao economy this year.

Laos has cut import tariffs for 8,536 goods from ASEAN members to zero. These account for 89% of entitled lists under the ASEAN Trade in Goods Agreement (ATIGA). Initially, Laos entered the ATIGA framework in 2015, but was able to prolong its tariff reduction due date until the end of 2018 with its status as a newer ASEAN member and as a least developed nation. Tariff cuts are favorable for Lao consumers, since more than 50% of products in the market are imported, mostly from Thailand. With the recent fall in the value of the Lao kip against the Thai baht, tariff waivers will help keep the price of goods under control while keeping inflation at a low level.

The three key risks to Laos' economy in 2019 are a continued depreciation of the Lao kip, a prolonged trade deficit, and China's economic slowdown. First, the kip has been weakening on the back of the Fed rate hike and confidence loss among EMs. As of February 2019, the value of the kip fell by 3.5% against the US dollar and Thai baht when compared to the same period last year. This continued depreciation will weigh on Laos' external debt repayment as they are denominated by the US dollar. Second, rising import demand – especially from construction projects – will keep dragging out the trade deficit during 2019-2020. The prolonged deficit may lead to depleting foreign reserves, which are currently low and able to cover only around one month of imports. Third, China's economic slowdown poses a significant risk to Laos' FDI and exports since China is the nation's top investor and export market. Approximately 77% of Laos' FDI in 2017 was from China alone, while shipments to China accounted for 33% of total Laos' exports during the first ten months of 2018.

EIC's view

Laos' tourism sector will see brighter prospects in 2019. The "Visit Laos Year 2018" campaign last year was hit by natural disasters, which resulted in the number of arrivals falling behind a 5-million-tourist target. Around 4.1 million foreigners visited Laos in 2018 based on a primary estimation by the Lao government. The figure, however, was 6% higher than that of 2017, signaling a potential rebound in coming years. **In 2019, the Lao government will join hands with China and launch a "Visit Laos-China Year 2019" campaign** aiming to promote tourism between both countries. The program could be a major driver for Laos' tourism segment as Chinese visitors to the country have been rising in recent years.

Chinese tourists ranked 3rd in the number of inbound visitors to Laos in 2017, following those from Thailand and Vietnam, but growth was compelling. While arrivals from Thailand and Vietnam have slowed, **the number of Chinese tourists surged 17%YOY in 2017 and their share of total tourists in Laos also expanded to 17%** -- up from 6% in 2010. The figure is set to continue growing thanks to a rising number of Freely Independent Travelers (FIT) and tourists from the New Tier 1 cities. Not only in numbers, but tourism incomes will also see an upswing. Based on Thailand's tourism statistics, **Chinese visitors are among the top spenders**, with expenditure per head at USD 193 per day, higher than ASEAN and European tourists, who spent USD 162 and USD 125 on average.

Laos' tourism sector presents a business opportunity for Thai investors, with a rosy growth outlook, especially from Chinese arrivals and abundant natural resources which provide huge potential for developing new natural tourism sites. **The sector is also backed by a government that provides generous investment incentives, since the country is still in need of improved hospitality services and transport infrastructure.** Thai businesses with expertise in tourism services and acquainted with Chinese tourists will be the competitive players in this market. **Nevertheless, key challenges to investors are a scarce labor force and a less favorable business environment.** Based on the World Bank's Doing Business Report 2019, Laos' rank in ease of doing business dropped thirteen places to 154 compared to the previous year.

Figure 3: Laos has seen an increase in Chinese arrivals, both in number and share to total visitors.

Number of tourism arrivals to Laos

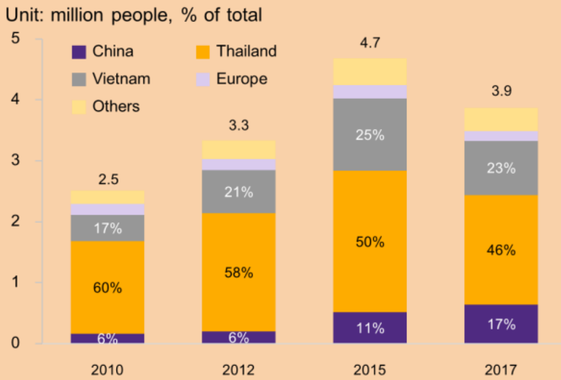


Figure 4: Chinese tourists were the top spenders, based on Thailand's statistics.

Thailand's tourism receipts, 2017

Country of origin	Length of stay (days)	Spending per head (USD/day)
China	8	193
ASEAN	6	162
Europe	17	125
The Americas	15	147
South Asia	8	171
Oceania	14	166
Middle East	13	191
Africa	13	173

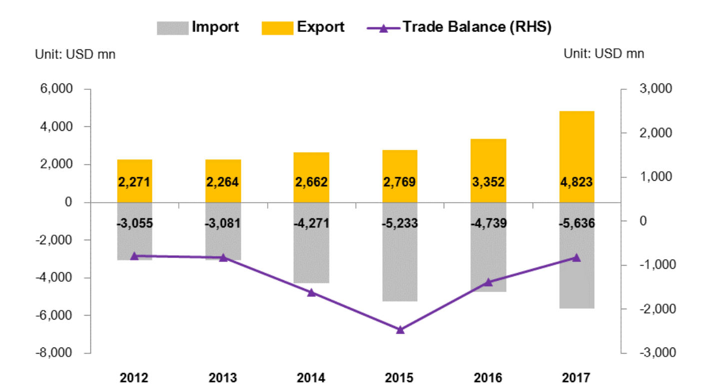
Source: EIC analysis based on data from Lao Statistics Bureau, Thailand's Department of Tourism, and CEIC

Laos' Key Indicators

Domestic Demand	Unit	2013	2014	2015	2016	2017	2018E	2019F
Real GDP	% YOY	8.0	7.6	7.3	7.0	6.9	6.8	7.0
Consumer price index	%	6.7	2.4	0.9	2.5	0.1	2.6	2.9
Current account balance	% of GDP	-28.4	-20.0	-18.0	-13.0	-12.1	-13.9	-12.3
Policy rate (end of period)	%	5.0	5.0	4.5	4.3	4.0	4.0	-

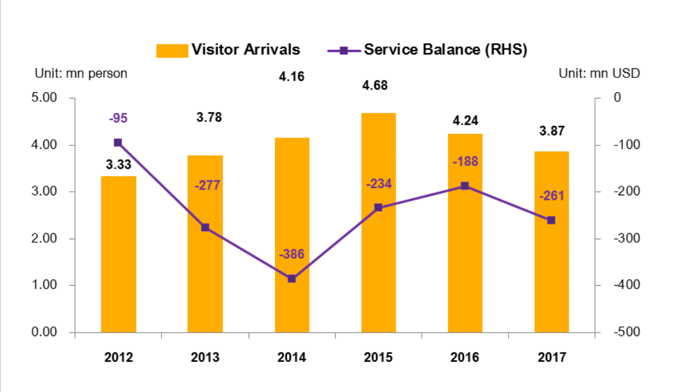
Sources: International Monetary Fund (IMF) and Bank of the Lao PDR

Trade balance improved thanks to surging exports



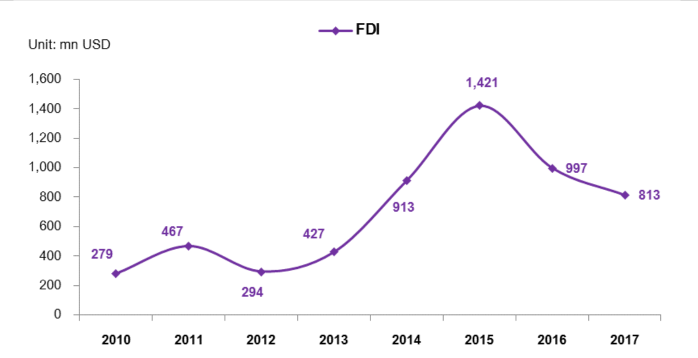
Sources: World Bank

Tourism visitors dropped during the past 2 years



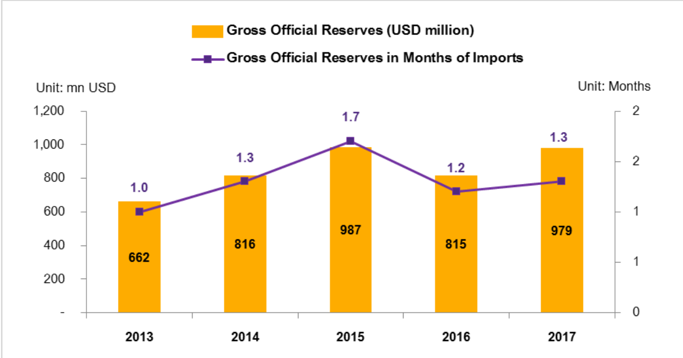
Sources: World Bank and CEIC

FDI fell but remained robust led by Chinese investment



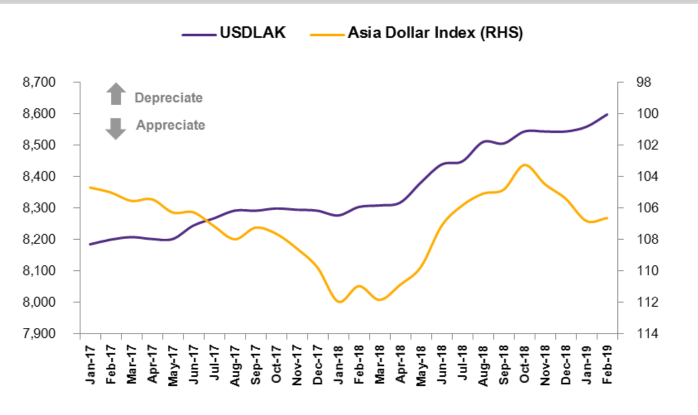
Sources: World Bank

Low foreign reserves intensified external vulnerability



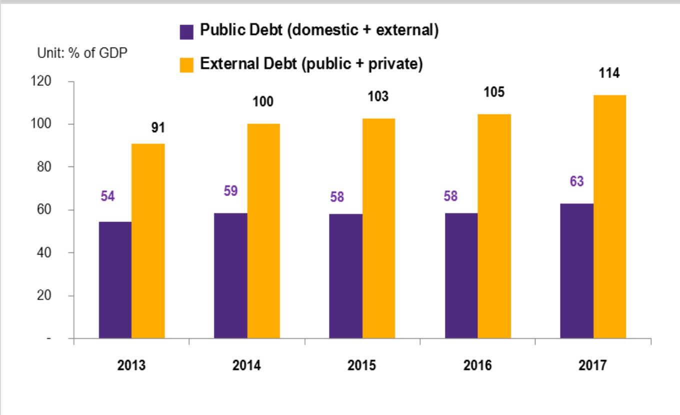
Sources: IMF

LAK is depreciating as USD strengthens



Sources: Bloomberg

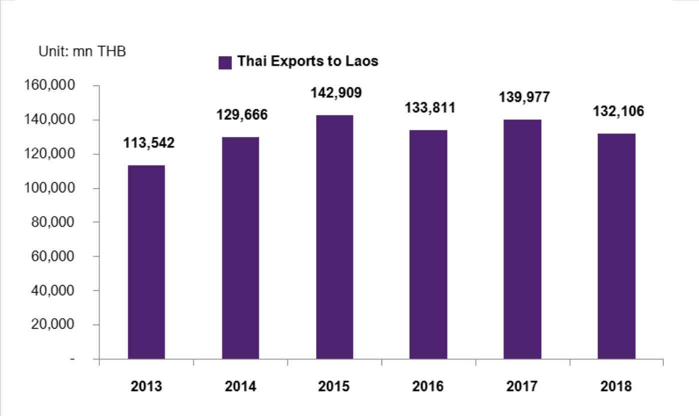
High external debt level is a major risk to Laos



Sources: International Monetary Fund (IMF) and CEIC

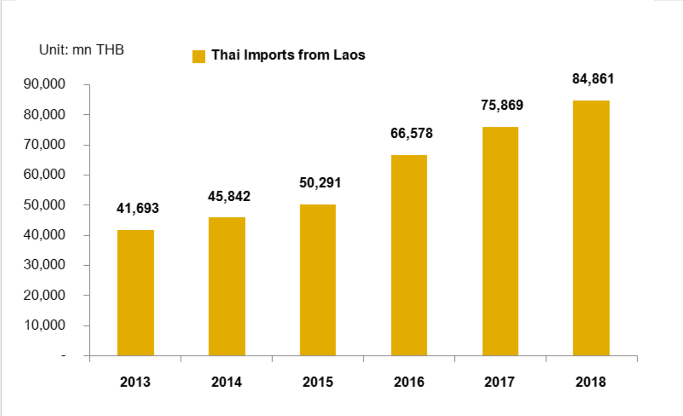
Links with Thai Economy

Exports to Laos slowed in 2018, dragged by industrial products and auto parts



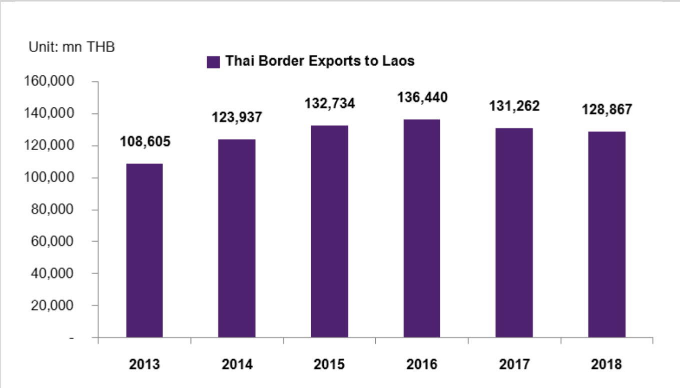
Sources: Thailand's Ministry of Commerce

Imports from Laos continued to rise thanks to a surge in imports of electronics parts



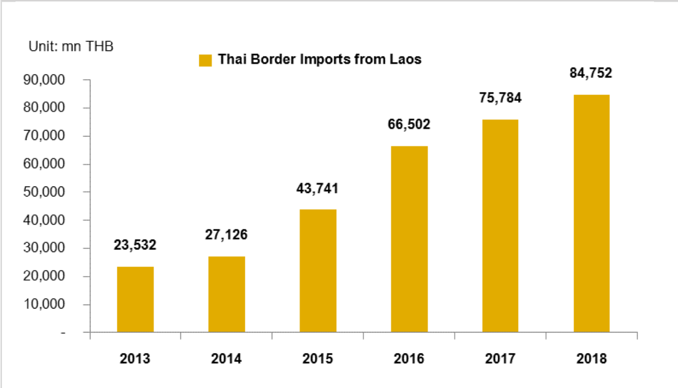
Sources: Thailand's Ministry of Commerce

Border exports accounted for about 98% of total Thai exports to Laos



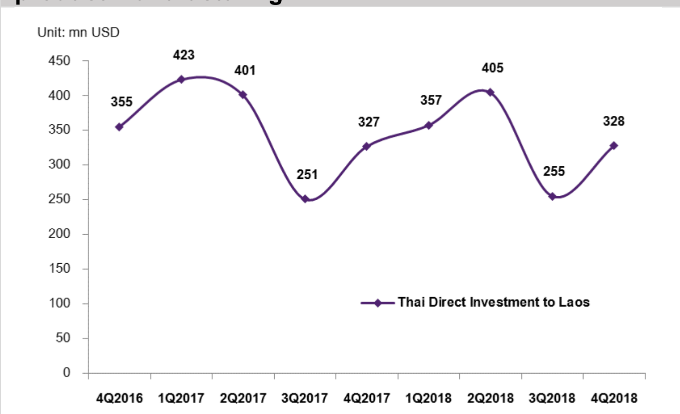
Sources: Thailand's Department of Foreign Trade

Expanding border imports were led by electricity and copper products



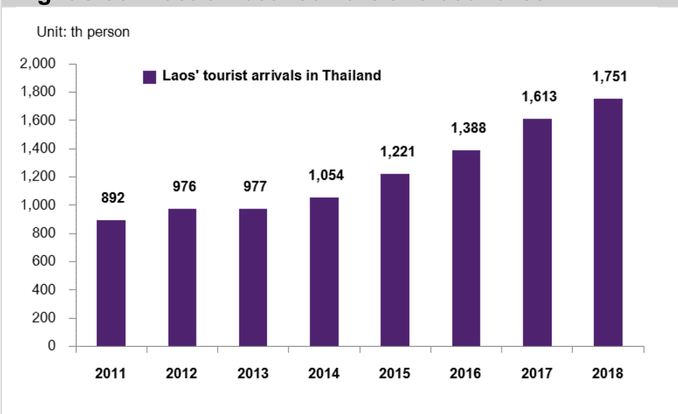
Sources: Thailand's Department of Foreign Trade

TDI in 2018 is driven by financial services and food product manufacturing



Sources: Bank of Thailand

Lao tourists in Thailand have been rising, thanks to more flight's connection between the two countries



Sources: Thailand's Department of Tourism

MYANMAR

OVERALL ECONOMY

Facts and Figures

Population (2017)	55.12 million
Labor force (2017)	22.3 million
GDP (2017)	66.96 USD billion
GDP per capita (2017)	1,272 USD
GDP by sector (2017)	Agriculture: 24.8%, Industry: 35.4%, Services: 39.9%
Top exports (2017)	Oil & Gas 27%, Textile 14%, Cereal 10%

Things to watch in 2019

Government huge investment spending to improve business infrastructure and environment

Banking and financial sector development

Macroeconomic update

Economic Outlook

Myanmar's economy is expected to recover to 6.8% in 2019 from 6.4% in 2018. Export-oriented manufacturing, the biggest part of the industrial sector, is expected to grow at around 8.2%. Services sector growth will moderate slightly to 7.6%, dragged down by poor performance in tourism-related businesses, including hotels, restaurants, and transportation. A deceleration in foreign direct investment (FDI) could be seen as FDI inflow during the 6-month transition period (April-September 2018) was much below the target and FDI commitments fell more than 50%YOY at the beginning of 2019. However, robust export growth will be the key economic driver. Exports in the last quarter of 2018 rose 26%YOY, supported by higher garment exports to the EU, while imports of capital and consumer goods fell following MMK depreciation and rising import prices. As a result, the trade deficit narrowed to USD 300 million, the lowest level in 5 years.

Business confidence dropped to a 3-year low as domestic uncertainties built up. Based on EuroCham's survey in December 2018, the majority of foreign firms operating in Myanmar (81%) were more pessimistic about the economic outlook. Protectionism and nationalism were considered the greatest obstacles for business, followed by a lack of skilled workers and poor infrastructure. Furthermore, the impacts of the Rakhine crisis have also become evident, particularly in the recent shortfall in FDI and stagnant tourist arrivals from western countries. The violation of human rights in Rakhine State has triggered a review for a possible withdrawal of the Everything But Arms (EBA) benefit granted by the EU, which would have a significant impact on exports, especially garment and footwear and other labor-intensive products with more than a 50% share of total exports to the EU in 2016. A full withdrawal of EBA will put Myanmar at a competitive disadvantage, due to higher tariffs. The risk of Myanmar losing EBA benefits from the EU have increased following the EU decision to impose tariffs on Indica rice from Myanmar in January 2018.

The government doubled the fiscal deficit to 6% of GDP in FY2018/19, with ambitious plans to maintain high economic growth and attract more FDI over the medium term.

Public spending has shifted toward more investments in infrastructure development, particularly in transportation and energy, as well as improving social welfare in education and healthcare. Efforts have been made in developing essential infrastructures and supporting key industries, such as, garment, manufacturing, real estate, and services to improve business environment. The goal is to attract more than USD 200 billion investment from both local and foreign investors under the 20-year Myanmar Investment Promotion Plan (MIPP). The government expects that with this plan, Myanmar will be able to maintain its rapid expansion and achieve the middle-income status in the medium term. Nevertheless, policy execution has become a big challenge as the capital budget was underspent by over 20% in the previous fiscal year and economic reforms have long been delayed.

Financial markets

The Central Bank of Myanmar (CBM) has implemented a number of measures since the beginning of 2019, aiming to further develop the financial sector and support economic activities. Many efforts have been seen in the development of the banking sector, through introducing new products and services. Starting in January, local banks have been allowed to allocate up to 5% of their total loan portfolios towards mortgage loans not exceeding 3 years. Mortgages that extend beyond 3-year period must be submitted to the CBM for approval. Later in February, Myanmar banks have been permitted to extend credit to all businesses without the need for collateral at a maximum lending rate of 16% per year, while the current interest rates for loans without collateral offered by non-bank institutions range from 24% to 36% per year. Moreover, the Myanmar Credit Bureau is expected to officially begin operation this year. These measures will, therefore increase access to credit by retail and SMEs customers and improve bank profitability and risk-pricing capability.

The insurance sector has finally been liberalized after a long awaited 6 years. Since 2013, 11 local insurers have been granted licenses, while 14 foreign insurers were only allowed to set up representative offices in Myanmar. According to the Ministry of Planning and Finance (MOPF)'s announcement No.1/2019, foreign insurance providers have now been given the green light to operate in the domestic market with 2 options, by allowing; 1) Not more than 3 licenses for foreign life insurers to operate as 100% wholly owned subsidiaries and 2) Foreign life insurers and non-life insurers with representative offices in Myanmar to form joint ventures with local counterparts. The MOPF expects 6 to 8 joint venture insurance firms joining the market in 2019, of which, 4 local insurers have already completed joint ventures with foreign firms. The move will not only increase the regionally lowest rate of insurance penetration at 0.1% of GDP, but also significantly promote the domestic capital market as insurance providers are big investors in government bonds. Once given licenses, insurance companies will be required to buy government bonds for at least 30% of their capital.

The CBM has responded to MMK volatility with several key measures, moving toward a flexible exchange rate regime and exchange rate market development. The US Fed rate hikes, coupled with stagnant FDI and tourism inflows, has pressured MMK to sharply depreciate by 19%YTD, reaching its peak of 1620 against the US dollar (USD) in late-September 2018. To date, MMK has gradually improved to levels of around 1,520-1,550 against USD in response to the CBM's measures, including the removal of a +/- 0.8% trading band around the daily reference rate, introduction of a USD swap facility with private banks, and a crackdown on informal currency trading in September last year. Continuing in early 2019, the CBM announced a new calculation for the reference exchange rate to a "market-based" weighted average rate in line with the international practices and granted official remittance licenses to authorized money changers to curb illegal trade of foreign currencies. The CBM's steps toward flexible exchange rate regime will increase MMK volatility in the short-term, given Myanmar's small foreign exchange rate market and a shortage of USD, but are expected to help Myanmar respond to both internal and external uncertainties in the future.

EIC's view

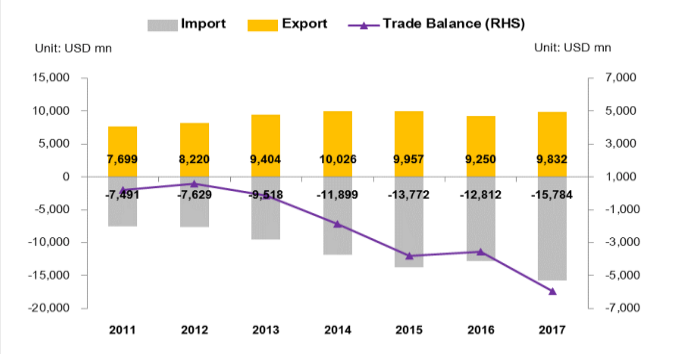
Amid uncertainties regarding EBA withdrawal, business opportunities in the Myanmar domestic market still shine. A sharp depreciation of MMK directly increased prices for imported goods, leading to a lessening Myanmar's import demand last year. At the same time, Myanmar wants to reduce reliance on imports from neighboring countries and transform the economy to be market-oriented. Thai investors should consider expanding production and sales to Myanmar rather than just exporting. We could also provide the Myanmar domestic market with a wide range of higher-value consumer products, capital goods, and services, given Myanmar's limited production capacity. Processed food & beverage, clothing, and other fast-moving consumer goods have strong potential growth due to rising per capita income and the liberalization of the wholesale and retail sector. The need for construction materials and machinery is rising following public and private infrastructure projects, a booming real estate market, and the development of the manufacturing industry. Education is one of a few services that is 100% opened to foreign investors, as Myanmar aims to increase the supply of skilled labors. Logistics services growth looks promising following more economic activities across the country in the near future. Recent development in the banking and financial sectors will also support business activities in Myanmar. Newly introduced banking products, such as loan without collateral, will increase the chances of small and medium enterprises to expand their businesses. Though many sectors remain restricted, EIC expects Myanmar to gradually open its doors and allow more foreign participation in its domestic market.

Myanmar's Key Indicators

Domestic Demand	Unit	2013	2014	2015	2016	2017	2018E	2019F
Real GDP	% YOY	8.4	8.0	7.0	5.9	6.8	6.4	6.8
Consumer price index	%	6.4	6.1	8.4	7.0	5.4	6.3	5.9
Current account balance	% of GDP	-4.9	-2.2	-5.1	-3.9	-4.3	-5.3	-5.7
Policy rate (end of period)	%	10	10	10	10	10	10	10

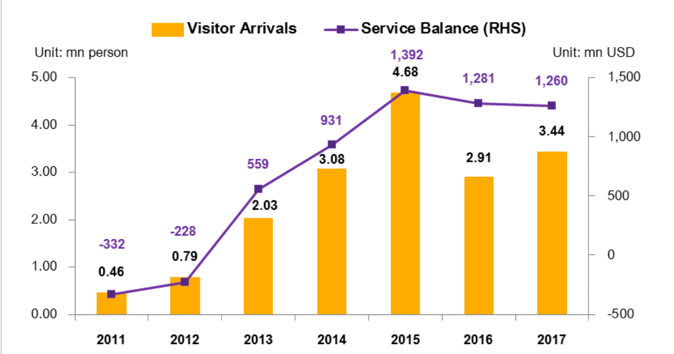
Sources: International Monetary Fund (IMF) and The Central Bank of Myanmar

Trade deficits deepened as imports continued to rise



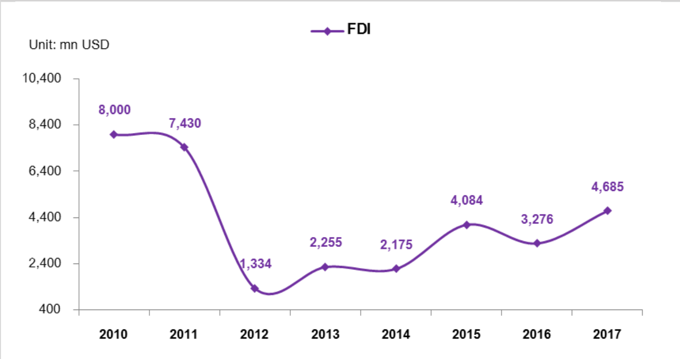
Sources: World Bank

Tourist arrivals fell especially from the western regions



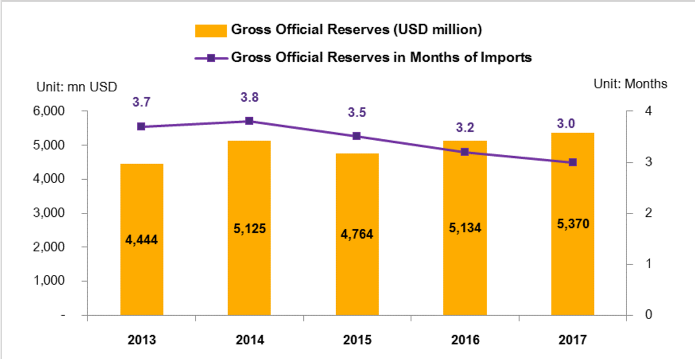
Sources: World Bank and CEIC

Stagnant FDI inflow due to Rohingya crisis



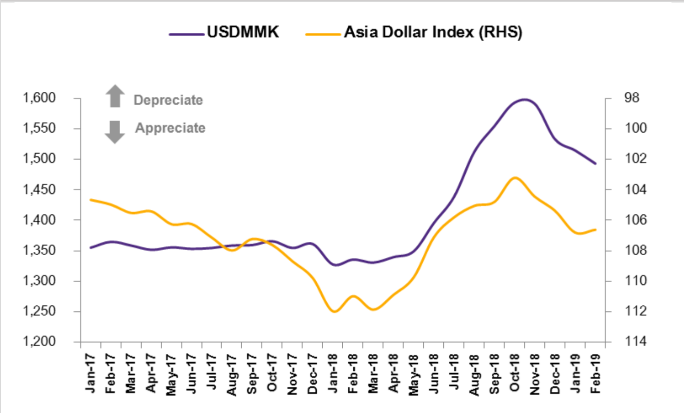
Sources: World Bank

Foreign reserves provided sufficient economic buffers



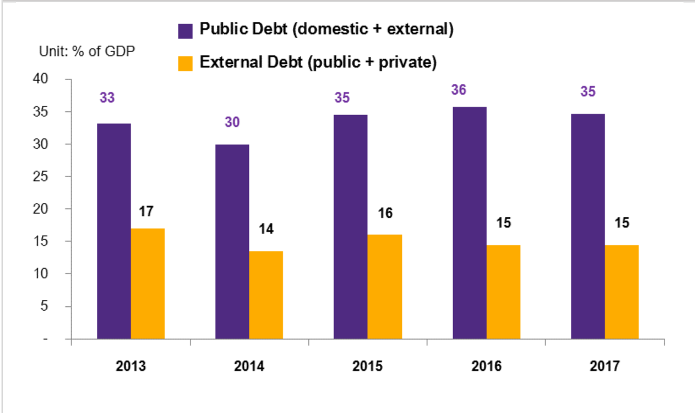
Sources: IMF

Sharp decline of MMK intensified economic vulnerability



Sources: Bloomberg

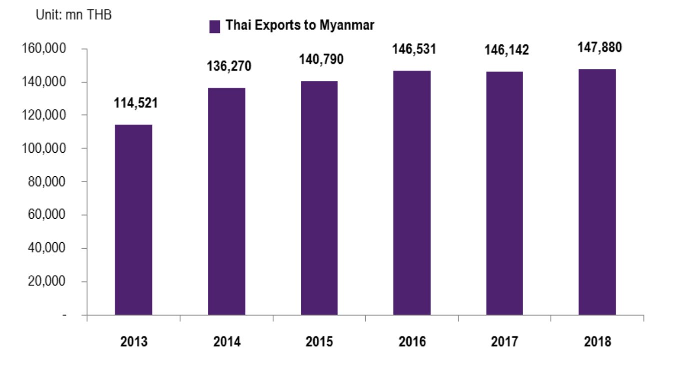
External debt remained low



Sources: International Monetary Fund (IMF) and CEIC

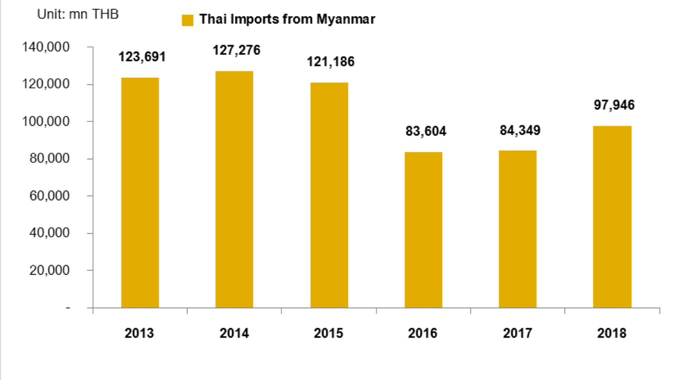
Links with Thai Economy

Thai exports to Myanmar marginally increased in 2018, due to a weaker domestic demand



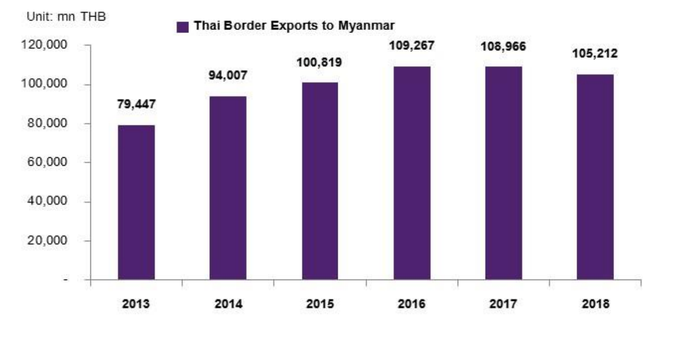
Sources: Thailand's Ministry of Commerce

Thai imports from Myanmar saw robust growth following a larger imported natural gas and other raw materials



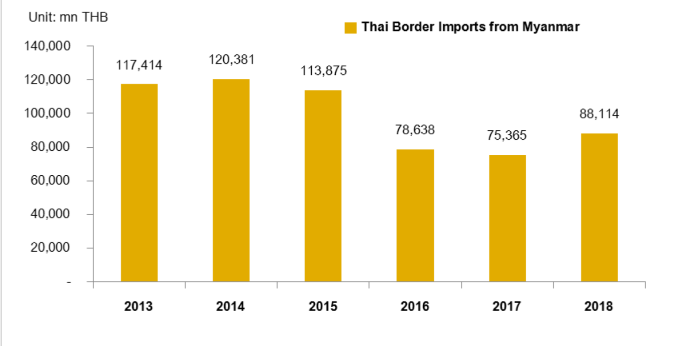
Sources: Thailand's Ministry of Commerce

Thai exports through 2 major borders dropped in 2018



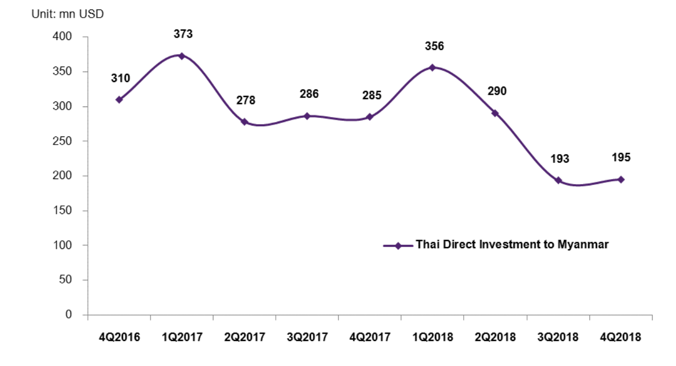
Sources: Thailand's Department of Foreign Trade

Thai import activities in 2018 improved in all Myanmar borders



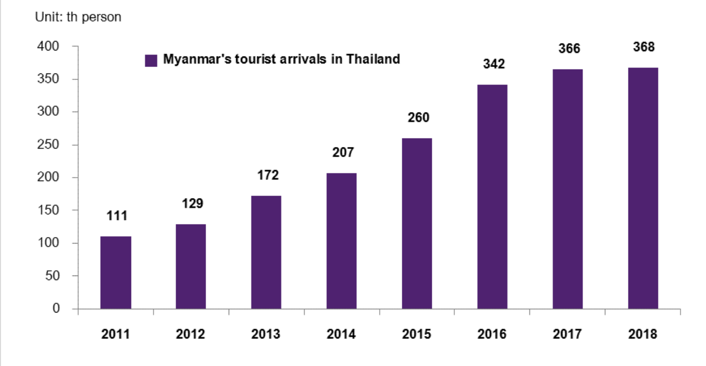
Sources: Thailand's Department of Foreign Trade

Thai direct investment in Myanmar dropped significantly from the beginning of 2018



Sources: Bank of Thailand

The number of Myanmar tourists has been less than 1% of total foreign tourists in Thailand.



Sources: Thailand's Department of Tourism

VIETNAM

OVERALL ECONOMY

Facts and Figures

Population (2017)	96.16 million
Labor force (2017)	56.46 million
GDP (2017)	215.93 USD billion
GDP per capita (2017)	2,306 USD
GDP by sector (2017)	Agriculture: 16%, Industry: 33%, Services: 41%
Top exports (2017)	Electronic products 39%, Garments and footwears 19%

Things to watch in 2019

EU-Vietnam FTA enforcement by the 1st half of 2019

China-based manufacturer relocation to Vietnam

Macroeconomic update

Economic Outlook

Vietnam's economy expanded 7.08% in 2018, the fastest growth in 11 years. All major sectors recorded notable growth, buoyed by the manufacturing, construction, and wholesale-retail sectors, which rose 13%, 9.2%, and 8.5%, respectively. The tourism industry also saw a bright outlook with the number of international arrivals surging by 20%. Vietnam's rosy economic growth will continue in 2019 thanks to FDI inflows, particularly in construction and factory expansion. During the first two months of 2019, FDI to Vietnam was about 200% higher than the same period last year. Manufacturing remained the top sector, attracting 82% of total FDI. This trend will continue, as Vietnam has become a potential regional manufacturing base, especially for electronics and high-tech industries. The Vietnamese government targets GDP growth at 6.6%-6.8% and inflation below 4% for this year.

Nevertheless, the challenge to Vietnam is a concentration of growth in foreign-invested industry, while technology transfers to local enterprises remain low. In 2018, 70% of Vietnam's total exports were dominated by foreign-invested companies. The sector also saw average export growth of 22% per year during 2010-2018, compared to 8% from the domestic sector. To enhance the capacity of Vietnamese firms, the government recently launched a directive supporting technology transfer and development from overseas. Prioritized sectors include IT, electronics, hi-tech agriculture, and healthcare. Meanwhile, CPTPP enforcement is pressuring Vietnam to speed up the SOE privatization process, which has been sluggish to date.

Financial markets

The State Bank of Vietnam (SBV) extended the foreign currency lending period and is preparing to rate all financial institutions in the country as a part of risk management. Earlier in 2018, the SBV called for strict controls on foreign-currency loans and a limit on lending until the end of 2018. The regulation initially aims to curb USD speculation and dollarization in the country. However, the bank later decided to extend the deadline to March 31 for short-term loans and September 30 for medium- to long-term loans. Rising trade tension and the need to accommodate local exporters are the main reasons behind the move. In addition, the SBV will start ranking financial companies in Vietnam based on performance and soundness. The ratings will include all commercial banks, credit institutions, financial leasing firms, cooperative banks, and foreign bank branches. However, ratings results will not be publicized as the SBV decide to use outcomes only for internal risk speculation.

Law & Regulation

Following active legal implementation in 2018, Vietnam is set to continue at a similar pace this year with developments in laws on investment, employment, and securities. The amended investment law will notably ease conditions for foreign businesses. Key amendments include (1) The PM's approval is no longer required for investment projects with capital over VND 5 trillion; and (2) The proposed removal of 19 conditional business restricted from foreign investors, such as logistics services and franchising. Meanwhile, the revised labor code will broaden its worker protection, particularly in overtime hours and pay, as well as extend the retirement age to 60-62. Both amended laws are expected to be passed in October 2019 and would take effect by 2021. In addition, Vietnam's Finance Ministry has proposed a draft Law on Securities which will lift foreign ownership caps for public companies, except those in conditional sectors. The draft law is scheduled to be enforced by 2020.

EIC's view

Foreign companies hit by the US-China trade war are eying factory relocation to Vietnam. Known as a manufacturing base, particularly for electronics products, Vietnam has been the top destination for China-based manufacturers seeking to avoid higher US tariffs. (Read more in Box: Vietnam emerges as the FDI safe haven amid the trade war)

SOE divestment is another rising opportunity for Thai investors. In past decades, privatization of state-owned enterprises (SOE) has been the top priority for the Vietnamese government to better manage loss-making firms and find new sources of state revenue. Under the current plan, 406 SOEs are listed for divestment by 2020. Examples of SOEs already selling some of their shares to foreign investors are Sabeco and Vietnam Airlines. Sabeco is the state-owned brewery, holding an approximately 40% market share in Vietnam's beer market. Some 53.9% of its shares were acquired by ThaiBev in 2017. Vietnam Airlines (VNA) sold 8.8% of its stake to Japan's ANA Holdings and plans to vend other 35.16% to the public this year.

Major SOE equitization deals

SOEs		Sector/ description	Capital (million USD)	% of share to divest
1	MobiFone	Telecom operator	600	35-50%
2	Saigon Trading Group (SATRA)	Retail distributor, supermarket chain	180	50%
3	PV Power	Electricity provider	655.3	50%
4	PV Oil	Petroleum trading and distribution company	205	50%
5	Vicem	Cement manufacturer	570	50%
6	Song Da Corporation	Hydropower contractor	190	50%
7	Ben Thanh Group	Tourism, commerce and property	53.6	50%
8	Saigon tourist Co. Ltd.	Tourism	162	50%
9	Vietnam Rubber Group	Rubber manufacturer	1,189.4	35-50%
10	EVN Corporation 1/2/3	Holding company for power plants	Total 1,242	50%

Source: Vietnamese SOE Equitization Report by Allens, March 2017

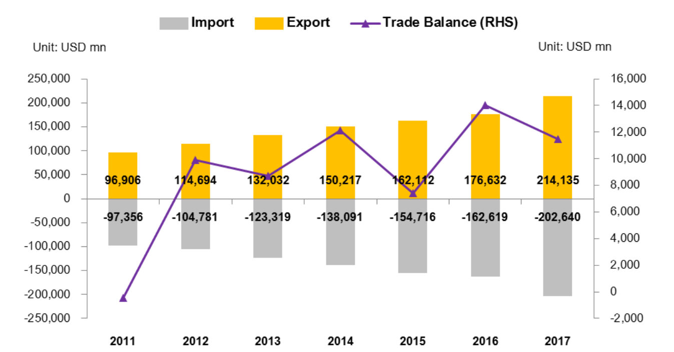
Key advantage of acquiring SOE stakes is that the companies already have a presence in the Vietnamese market -- some even have a wide consumer base such as VinaFood, VinaMilk, and MobiFone. This is an **appealing opportunity for new investors,** since earning market share and consumer interest is a crucial step in doing business in Vietnam but to do so is quite challenging. **Nevertheless, major obstacles to investors include unfair stake valuation and a slow ownership transfer process.** To improve this situation, the Vietnamese government has implemented several directives providing clearer conditions, frameworks, and schedules for SOE privatization.

Vietnam's Key Indicators

Domestic Demand	Unit	2013	2014	2015	2016	2017	2018E	2019F
Real GDP	% YOY	5.4	6.0	6.7	6.2	6.8	6.6	6.5
Consumer price index	%	6.0	1.8	0.6	4.7	2.6	4	4
Current account balance	% of GDP	4.5	4.9	-0.1	2.9	2.5	2.2	2.0
Policy rate (end of period)	%	7.0	6.5	6.5	6.5	6.25	6.25	-

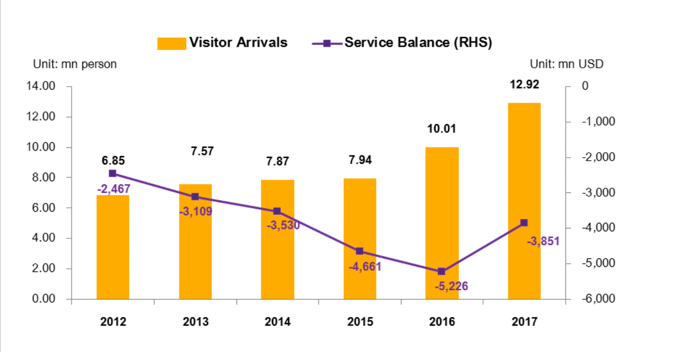
Sources: International Monetary Fund (IMF) and The State Bank of Vietnam

Trade surplus continued with rising export demand



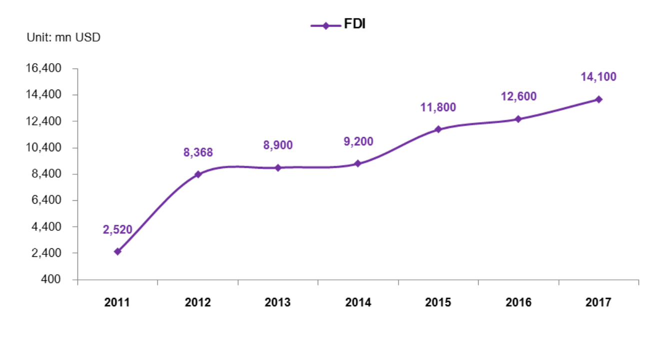
Sources: World Bank

Tourism helped lifting service balance



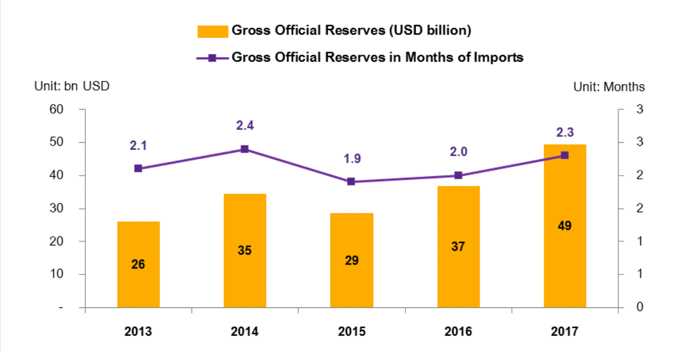
Sources: World Bank and CEIC

FDI is on the rise, concentrated in manufacturing



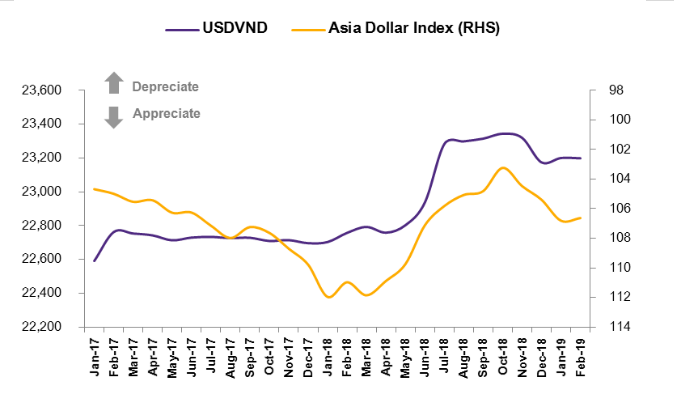
Sources: World Bank

Reserves buffers are lower than a 3-month standard



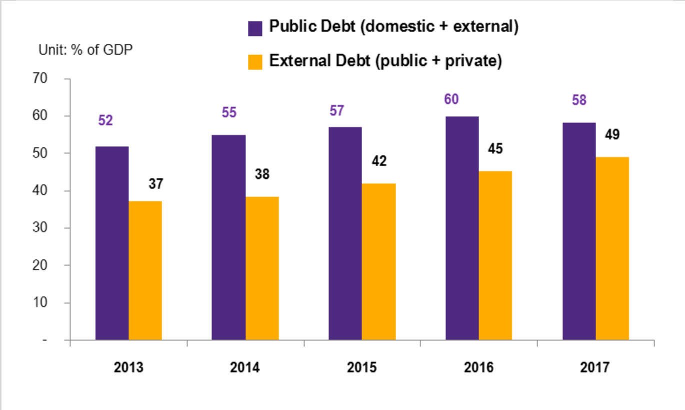
Sources: IMF

VND moves in line with Asian currencies



Sources: Bloomberg

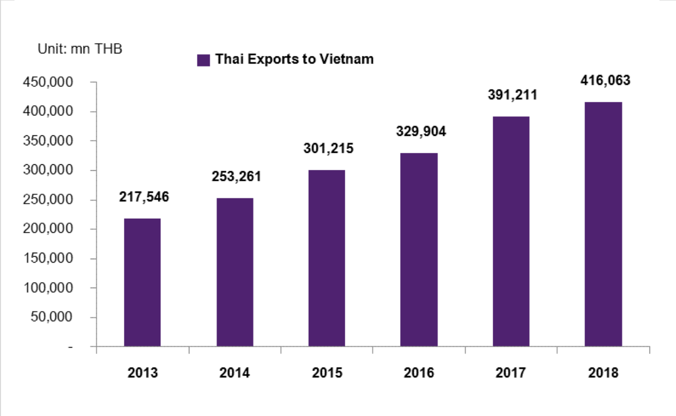
Country debt are relatively high, comparing to peers



Sources: International Monetary Fund (IMF) and CEIC

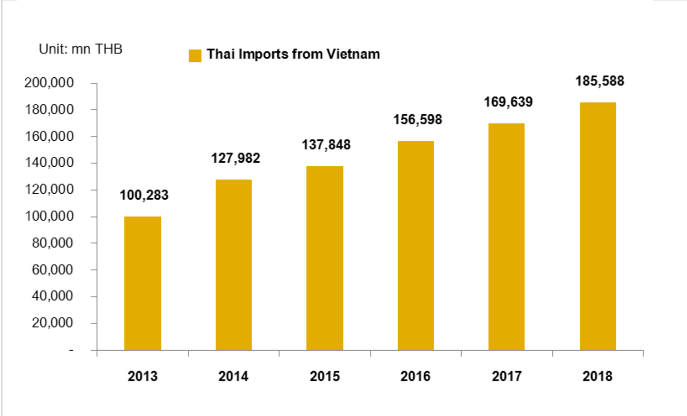
Links with Thai Economy

Exports to Vietnam continued rising, driven by auto parts, refined oil and polyethylene resin



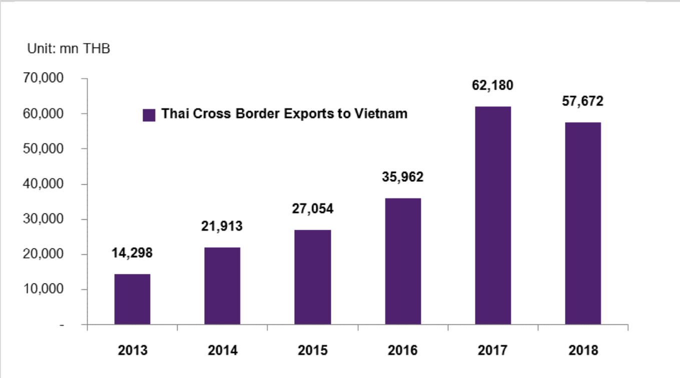
Sources: Thailand's Ministry of Commerce

Telephones, crude petroleum oil, and electronics parts are among major imported products from Vietnam



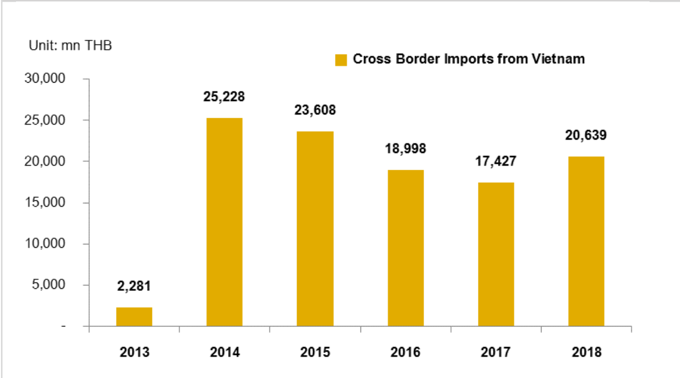
Sources: Thailand's Ministry of Commerce

Border exports slightly dropped in 2018, but fruits exports saw a rapid growth especially frozen durian



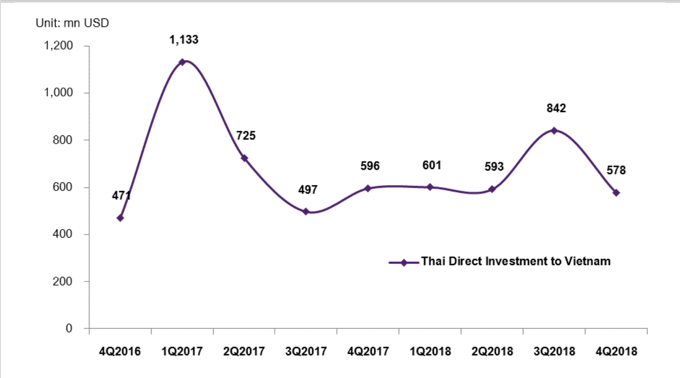
Sources: Thailand's Department of Foreign Trade

Cross Border Imports recorded an 18%YOY growth in 2018, led by imports of electrical part and plant product



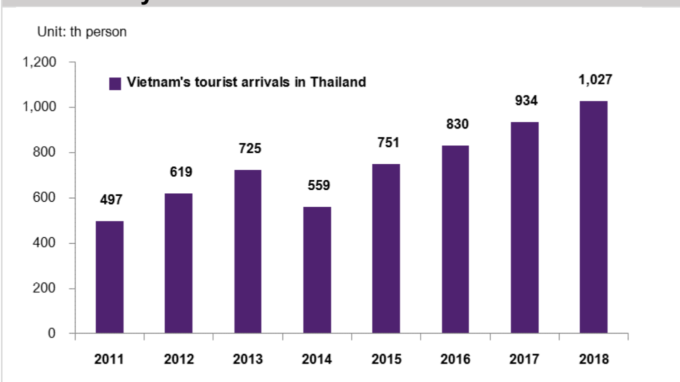
Sources: Thailand's Department of Foreign Trade

TDI to Vietnam has been concentrated in manufacturing and financial services



Sources: Bank of Thailand

Tourists from Vietnam has been rising particularly travelers by air



Sources: Thailand's Department of Tourism

BOX

Vietnam emerges as the FDI safe haven amid the trade war

The relocation of manufacturing-based production from China to Vietnam has gathered momentum, fueled by continued Chinese wage hikes and an ongoing trade war between the US and China. Trade tensions between the world's two biggest economies have caused uncertainty in global trade, dampening exports from the countries facing the tariffs. Particularly, global manufacturing hub China and countries integrated in its supply chain saw a slowdown in exports. The threat of high tariffs forced manufacturers based in China to consider the most cost-effective strategies by shifting their production elsewhere to avoid impacts from the trade conflict. **Geographically and economically, Vietnam is seen as a potential candidate for an export production base.**

Apart from its geographic proximity to China and tax privileges, **one of Vietnam's competitive advantages in attracting investment is its relatively cheap labor force compared to China and its ASEAN neighbors**. The recent 2019 minimum wage hikes in Vietnam resulted in new monthly minimum wages ranging from USD 126 to USD 180 across different regions. However, Vietnamese minimum wages are still 38%-54% of those in China, whose minimum wages in some leading cities in Guangdong, known as a manufacturing-oriented province, now exceed USD 330 per month. Meanwhile, minimum wages of around USD 275 in Malaysia and USD 288 in Thailand are also higher than those in Vietnam. In addition, **Vietnam's demography is in a good position**. According to UN, the population in Vietnam is estimated to be around 96 million people, with about 70% of population between 15 and 64 years old in 2019.

Another strength of Vietnam as an export production base is its excellent network of trade agreements. A total of 13 Free trade agreements have been signed, and another three are under negotiation. This means that Vietnamese exports to significant parts of the world are free from tariffs, offering opportunities for manufacturers relocating in Vietnam to sell to more partners at minimized cost. Vietnam's major FTAs include the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), which came into effect at the beginning of 2019, and the EU-Vietnam Free Trade Agreement (EVFTA) awaiting ratification this year. Eliminating tariffs for goods traded between members, CPTPP and EVFTA would open opportunities for investors who aim to access CPTPP members around the Pacific Rim and EU markets.

Recent trends show empirical evidences of investment relocation in Vietnam. Amid a trade war between the US and China, foreign investment in Vietnam has been strong. Actual FDI inflows increased by 9.1%YOY in 2018, reaching USD 19.1 billion, and grew 9.2%MOM in January 2019. Some 57.8% of accumulated FDI flew into the manufacturing and processing sector, supporting the further establishment of Vietnam as a main manufacturing hub (Figure 5 and 6). **Meanwhile, some businesses have diversified their US-exporting production to Vietnam,** especially manufacturers of products subject to US tariffs on electronics, furniture, and apparel (Figure 7). According to PWC's APEC CEO Survey 2018, Vietnam was among the top APEC economies for planned increases in cross-border investment.

Figure 5: FDI to Vietnam outpaced its ASEAN peers and is likely to continue rising

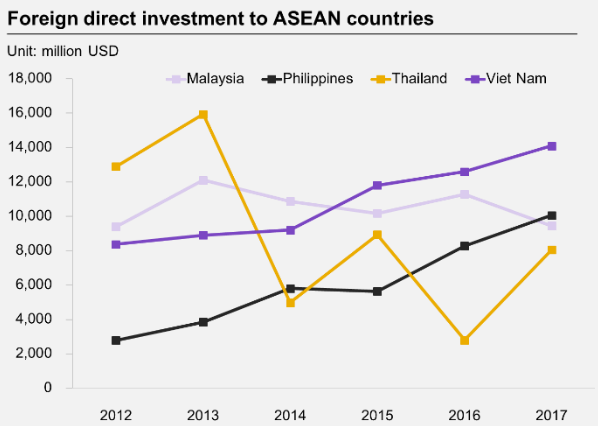
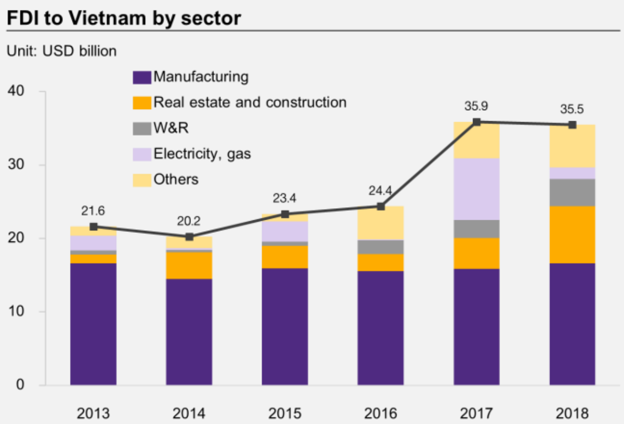


Figure 6: FDI to Vietnam mainly concentrated in manufacturing sector



Source: EIC analysis based on data from World Bank, ASEANStats, Vietnam's Foreign Investment Agency, and CEIC

Figure 7: Some manufacturers in China announced investment relocation plans to Vietnam to mitigate risks caused by the Trade War

Companies	Nationality	Products	Information
Tapestry Inc.	American	Handbag	Expand its production in Vietnam
Sintai	Chinese	Furniture	Shift 20% of its production to Vietnam
Man Wah Holdings	Hong Kong	Furniture	Acquired new plant in Vietnam in November 2018
Zhejiang Hailide New Material	Chinese	Polyester	Invested in the new plant in Vietnam
Second Generation (BeBop and Gypsies & Moondust lables)	American	Junior wears	Shift part of its production to Vietnam
Yokowo	Japanese	Automotive antenna components	Shift its production to Vietnam and anticipate to complete a relocation of production in 2019
HL Corp.	Chinese	Bike parts	Shift part of its production to Vietnam
Hon Hai Precision (Foxconn Technology Group)	Taiwanese	iPhone assembler	Acquired land in Vietnam industrial park in January 2019
GoerTek	Chinese	Wireless earphones for Apple	Shift its production to Vietnam
Key Tronic	American	Electronic products	Invest in the new plant in Vietnam and anticipate to open the Vietnam factory in July 2019

Source: EIC analysis based on data from several presses (as of February 27, 2019)

Nevertheless, investment relocation in Vietnam might be constrained by a skilled labor shortage. Navigos Group, operator of Vietnam's biggest job portal, reported that Vietnam was under pressure by recruitment demands at the senior management level, particularly from FDI companies in the electronics industry in the fourth quarter of 2018. In fact, the shortage of medium and high skilled personnel is nothing new in Vietnam. A labor force survey conducted by the General Statistic Office of Vietnam (GSO) in the first quarter of 2018 revealed that skilled laborers accounted for only 21% of the total labor force. This may be one of the biggest obstacles for Vietnam making the most of investment relocation.

In summary, **Vietnam has emerged as an attractive investment destination for foreign investors,** particularly during the ongoing trade tension between the US and China. This is due to **its low labor costs and a strong network of free trade agreements** that allow businesses relocating to Vietnam to conduct cost-effective strategies and access global major markets. This case study **highlights the importance of the country's competitiveness,** to which Thailand should pay attention in order to attract foreign investment in the future.

Main author

YUNYONG THAICHAROEN, PH.D.
Chief Economist and
First Executive Vice President
Economic Intelligence Center

Yunyong Thaicharoen is a First Executive Vice President of the Economic Intelligence Centre (EIC), a strategic unit of Siam Commercial Bank Public Company Limited (SCB). Prior to joining SCB, Yunyong was a Director at the Monetary Policy Department, Monetary Policy Group, Bank of Thailand which oversees overall monetary policy analyses and recommendations on interest rate, exchange rate, and capital flow policies. He also held the position of Director of the Capital Market Research Institute at the Stock Exchange of Thailand.

Yunyong is an expert on macroeconomics, monetary policy, and capital market. He frequently gives lectures to public seminars, as well as to organisations both domestically and abroad. Yunyong is also a special instructor at various academic institutions.

Yunyong holds a doctorate in economics, specialising in monetary policy and international economics, and a bachelor's degree in economics from Massachusetts Institute of Technology (MIT) under a scholarship from the Bank of Thailand.

THANAPOL SRITHANPONG, PH.D.
Senior Economist

Contact :
thanapol.srithanpong@scb.co.th

JIRAMON SUTHEERACHART
Analyst

Contact :
jiramon.sutheerachart@scb.co.th

KUNYARUK NAIYARAKSAREE
Analyst

Contact :
kunyarak.naiyaraksaree@scb.co.th

SUPAWADEE CHINGNAWAN
Management Associate

Contact :
supawadee.chingnawan@scb.co.th

Economic Intelligence Center (EIC)

E-mail: eic@scb.co.th Tel: +66 (2) 544 2953

Yunyong Thaicharoen, PH.D.
Chief Economist and FEVP
yunyong.thaicharoen@scb.co.th

Economic and Financial Market Research

Krasae rangsipol
krasae.rangsipol@scb.co.th

Panundorn Aruneeniramarn
Panundorn.aruneeniramarn@scb.co.th

Thanapol Srithanpong, PH.D.
thanapol.srithanpong@scb.co.th

Wachirawat Banchuen
wachirawat.banchuen@scb.co.th

Kunyaruk Naiyaraksaree
kunyaruk.naiyaraksaree@scb.co.th

Jiramon Sutheerachart
jiramon.sutheerachart @scb.co.th

Jirayu Photirat
jirayu.photirat@scb.co.th

Chinnachod Thaerapanyaporn
chinnachod.thaerapanyaporn@scb.co.th

Pangubon Amnueysit
pangubon.amnueysit@scb.co.th

Pongsakorn Srisakawkul
pongsakorn.srisakawkul@scb.co.th

Export Cluster

Chotika Chummee
chotika.chummee@scb.co.th

Kriskorn Trachoo
kriskorn.trachoo@scb.co.th

Kamonchanok Klainok
kamonchanok.klainok@scb.co.th

Kanyarat Kanjanavisut
kanyarat.kanjanavisut@scb.co.th

Nantapong Pantaweesak
Nantapong.pantaweesak@scb.co.th

Service Cluster

Vithan Charoenphon
Head of Service Cluster
vithan.charoenphon@scb.co.th

Pranida Syamananda
pranida.syamananda@scb.co.th

Nopphamas Houbjaruen
Nopphamas.houbjaruen@scb.co.th

Pullawat Pitigraisorn
pullawat.pitigraisorn@scb.co.th

Pattharapon Yuttharsaknukul
Pattharapon.yuttharsaknukul@scb.co.th

Infrastructure Cluster

Supree Srisamran, PH.D.
supree.srisamran@scb.co.th

Kamonmarn Jaenglom
kamonmarn.jaenglom@scb.co.th

Kanit Umsakul
kanit.umsakul@scb.co.th

Punyapob Tantipidok
punyapob.tantipidok@scb.co.th

Nawaporn Komolsuradej
nawaporn.komolsuradej@scb.co.th

Olan Aeovithayasupon
olan.aeovithayasupon@scb.co.th

Energy and Resources Cluster

Sivalai Khantachavana
sivalai.khantachavana@scb.co.th

Pimjai Hoontrakul
pimjai.hoontrakul@scb.co.th

Nantapong Pantaweesak
nantapong.pantaweesak@scb.co.th

Nattanan Apinunwattanakul
nattanan.apinunwattanakul@scb.co.th

Puthita Yamchinda
puthita.yamchinda@scb.co.th

Apinya Aksornkij
apinya.aksornkij@scb.co.th

Business Advisory

Nithi Kaveevivitchai
nithi.kaveevivitchai@scb.co.th

Pattarawadee Rattanasiwakoon
pattarawadee.rattanasiwakoon@scb.co.th

Phatranij Eamsiri
phatranij.eamsiri@scb.co.th

Knowledge Management & Networking

Phanumard Lueangaram
phanumard.lueangaram@scb.co.th

Krilerk Vallopsiri
krilerk.vallopsiri@scb.co.th

Piyanuch Phiolueang
piyanuch.phiolueang@scb.co.th

Poomisak Kumprasert
poomisak.kumprasert@scb.co.th

Wanitcha Nateesuwan
wanitcha.nateesuwan@scb.co.th

Worawan Wannaprapan
worawan.wannaprapan@scb.co.th

Sorodda Upamai
sorodda.upamai@scb.co.th