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Research Update:

Ratings On Vietnam Affirmed At 'BB-/B' With Stable Outlook

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Overview

- Vietnam is a lower middle-income sovereign with vulnerabilities associated with its emerging monetary and fiscal policy framework, banking sector weaknesses, and rising debt burden.
- Its external settings are sound, reflecting rising foreign exchange reserves and a modest external debt burden.
- We are affirming our 'BB-' long-term and 'B' short-term sovereign credit ratings on Vietnam. We are also affirming our 'axBB+/axB' ASEAN regional scale rating on Vietnam.
- The outlook is stable, reflecting our expectation that Vietnam's growth prospects will continue to improve, leading to gains in its key economic, fiscal, external, and monetary credit measures.

Rating Action

On April 29, 2016, Standard & Poor's Ratings Services affirmed its 'BB-' long-term and 'B' short-term sovereign credit ratings on Vietnam. The outlook is stable. At the same time, we affirmed our 'axBB+/axB' ASEAN regional scale rating on Vietnam.

Rationale

The ratings on Vietnam reflect the country's lower middle-income, rising debt burden, banking sector weakness, and the country's emerging institutional settings that hamper policy responsiveness. These strengths are offset by Vietnam's sound external settings that feature adequate foreign exchange reserves and a modest external debt burden.

Vietnam has a lower middle income but comparatively diversified economy; we estimate GDP per capita at about US$2,200 in 2016. Recent improvements in macroeconomic stability have supported strong performance in the sizable foreign-owned and export-focused manufacturing sector (electronics, telephones, and clothing). This strength will likely be offset by weaker domestic activity as the impetus to growth stemming from low household and company sector leverage is hampered by weak banks and government enterprises, and shortfalls in infrastructure. We expect real GDP per capita growth to rise by 5.3% in 2016 (2015: 5.6%) and average 5.2% over 2016-2019, reflecting modest outlooks for Vietnam's trading partners.

Uncertain conditions in export markets and the slow pace in addressing

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government enterprise reforms, fiscal consolidation, and banking sector resolution add downside risks to this growth outlook.

We view the financial and technical assistance Vietnam receives from donors as a rating strength. The government's socio-economic development plans also provide useful policy anchors that have improved macroeconomic stability and the inflationary environment in the past two years. That said, we note that policymaking remains highly centralized and opaque under the one-party system, and the government's ability to develop and implement swift policy responses, if required, is uncertain. Moreover, large fiscal deficits and a sustained rise in Vietnam's debt burden signal a continued delay in fiscal consolidation. Fiscal deficits (including off-budget capital expenditure) have averaged 5.6% of GDP over 2010-2015 and we forecast them to average 5.8% over 2016-2019. We estimate the deficits will underpin a rise in the net general government debt burden to 51.5% of GDP in 2016 and about 55% by 2019.

Vietnam's debt burden may prove higher than we forecast if the shortfall in basic services and infrastructure that feature prominently in its capital spending plans lead to additional borrowings. Other potential constraints on the government's fiscal flexibility are guarantees related to its enterprises that we estimate at 11% of GDP. This percentage may also rise should progress in reforming Vietnam's inefficient government enterprises remain slow or reverse.

While Vietnam's fiscal settings are becoming stretched, its external metrics are adequate. Its current account is likely to remain broadly in balance annually to 2019, reflecting robust manufacturing and services (mainly tourism) exports, large (and rising) remittances, and subdued domestic import demand. Strong foreign direct investment (FDI) in manufacturing, combined with competitive unit labor costs relative to peers (Malaysia, Thailand, and Indonesia) and a large young educated labor market, implies further strength in exports over 2016-2019. Participation in free trade agreements could provide further upside to Vietnam's export earnings. The high capital outflows in 2013 (following the unwinding of gold deposits at commercial banks and announcement of U.S. Federal Reserve tapering) have been offset by large FDI and loan inflows that have contributed to reserves rising to US$34.3 billion by December 2015.

We expect Vietnam to remain in an external asset position, shown by its narrow net external debt (the ratio of gross external debt less official reserves and financial sector external assets to current account receipts [CARs]) averaging close to zero over 2016-2019. External liquidity (measured by the ratio of gross external financing needs to CARs and usable reserves) will also remain a sound 92% on average over the period. We do not envisage a marked deterioration in Vietnam's external financing stemming from a reduction in disbursements from donors, or from a shift in foreign direct investments or portfolio equity investments.

Other factors that mitigate risks associated with Vietnam's international liabilities include a very low reliance on external savings by Vietnam's combined bank and company sectors, as well as the low and mainly long-term and concessional nature of the government's external borrowings.

Vietnam's banks benefit from being in an external net asset position with limited linkages to global markets. That said, system stability is hampered by high nonperforming assets and cross-ownership, connected lending, and heavy exposure to Vietnam's weak property market. Capital adequacy is reportedly above the 9% regulatory minimum but unclear loan classification and provisioning, and government policies directed at the resolution of distressed banks through the Vietnam Asset Management Co. (VAMC) weigh on a fuller assessment of the condition and outlook for Vietnam's financial system. Our Bank Industry Credit Risk Assessment for Vietnam is '9' (with '1' being the highest assessment and '10' being the lowest).

We regard the State Bank of Vietnam's ability to support sustainable economic growth while attenuating economic or financial shocks to be constrained. This reflects its limited independence; ability to coordinate monetary policies with fiscal, economic, and development policies; use of market-orientated instruments to conduct policy; and record in maintaining low inflation. In our opinion, greater exchange rate flexibility and use of inflation targeting, combined with a deeper and more diversified financial and capital market, may facilitate a more effective monetary policy framework and improved credit metrics.

Outlook

The stable outlook reflects our expectation that Vietnam's growth prospects will continue to improve, leading to gains in its key economic, fiscal, external, and monetary credit measures.

This outlook assumes progress on growth-enhancing improvements over the next three to five years.

We may lower the ratings if:
- Vietnam's banks weaken further, or
- Government debt rises significantly, either because of fiscal loosening or support for Vietnamese banks.

We may raise our ratings if the reform program of Vietnam's government results in substantially better growth, fiscal outturns, and bank system resolution than we currently expect, such that net general government debt falls below 30% of GDP and net external debt remains low. We consider this scenario unlikely over the next year, however.

Key Statistics

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Socialist Republic of Vietnam - Selected Indicators										
	2010	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**
ECONOMIC INDICATORS (%)										
Nominal GDP (bil. LC)	2,157,828	2,779,880	3,245,419	3,584,262	3,937,856	4,193,289	4,546,615	4,944,390	5,334,957	5,835,696
Nominal GDP (bil. $)	116	136	156	171	186	193	206	222	239	262
GDP per capita (000s $)	1.3	1.5	1.8	1.9	2.1	2.1	2.2	2.4	2.5	2.7
Real GDP growth	6.4	6.2	5.2	5.4	6.0	6.7	6.3	6.2	6.2	6.2
Real GDP per capita growth	5.3	5.1	4.1	4.3	4.9	5.6	5.2	5.1	5.1	5.1
Real investment growth	10.9	(7.8)	1.9	5.3	9.3	7.2	6.7	6.0	5.9	6.0
Investment/GDP	35.7	31.9	26.1	26.2	24.7	27.3	27.7	28.7	29.3	29.0
Savings/GDP	32.0	32.0	32.1	30.8	29.7	28.6	28.2	28.6	29.5	29.5
Exports/GDP	68.7	78.0	79.8	83.4	86.6	100.7	115.1	124.2	138.7	152.5
Real exports growth	6.8	4.4	4.7	1.6	8.6	18.2	16.9	12.1	13.4	13.5
Unemployment rate	4.3	3.6	3.2	3.6	3.4	2.4	2.4	2.4	2.4	2.4
EXTERNAL INDICATORS (%)										
Current account balance/GDP	(3.7)	0.2	6.1	4.5	5.0	1.3	0.5	(0.1)	0.2	0.6
Current account balance/CARs	(4.9)	0.2	7.1	5.1	5.4	1.2	0.4	(0.1)	0.2	0.3
Trade balance/GDP	(4.4)	(0.3)	6.4	5.1	6.5	3.1	3.1	3.0	3.7	4.3
Net FDI/GDP	6.1	4.8	4.6	4.1	4.3	4.1	4.1	4.1	4.1	4.1
Net portfolio equity inflow/GDP	2.0	1.0	0.8	0.8	0.1	1.0	0.6	0.6	0.6	0.6
Gross external financing needs/CARs plus usable reserves	95.5	97.4	91.4	88.1	88.7	90.7	90.6	90.9	92.0	93.0
Narrow net external debt/CARs	28.6	26.3	18.6	15.9	8.6	3.5	1.1	(0.2)	(1.5)	(2.6)
Net external liabilities/CARs	94.6	83.8	74.6	70.0	61.6	51.4	44.5	40.5	35.4	30.9
Short-term external debt by remaining maturity/CARs	8.4	8.2	7.9	8.0	7.5	6.6	5.3	4.5	3.4	2.7
Reserves/CAPs (months)	2.1	1.3	1.3	2.1	1.9	2.0	1.9	1.8	1.5	1.2
FISCAL INDICATORS (%, General government)										
Balance/GDP	(2.8)	(1.1)	(6.8)	(7.4)	(6.1)	(6.5)	(6.4)	(5.8)	(5.5)	(5.3)
Change in debt/GDP	10.3	9.3	8.9	8.6	8.0	7.1	6.4	5.8	5.5	5.3
Primary balance/GDP	(1.6)	0.0	(5.5)	(5.8)	(4.5)	(5)	(4.3)	(3.6)	(3.2)	(3)
Revenue/GDP	27.3	25.9	22.6	23.1	21.9	22.1	21.7	22.0	22.2	22.2
Expenditures/GDP	30.0	26.9	29.4	30.5	28.0	28.7	28.1	27.8	27.7	27.5
Interest /revenues	4.3	4.1	5.9	6.8	7.7	7.0	10.0	10.1	10.5	10.5

Socialist Republic of Vietnam - Selected Indicators (cont.)	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Debt/GDP	49.3	47.6	49.7	53.6	56.8	60.4	62.2	63.0	63.9	63.7
Debt/Revenue	180.8	183.9	219.7	232.2	259.2	273.3	287.1	286.4	288.4	286.7
Net debt/GDP	46.1	44.7	47.1	50.9	54.5	58.1	59.8	60.5	61.6	61.6
Liquid assets/GDP	3.2	2.9	2.5	2.8	2.3	2.3	2.4	2.5	2.3	2.1
MONETARY INDICATORS (%)										
CPI growth	8.9	18.7	9.1	6.6	4.1	0.6	1.3	2.3	2.9	3.4
GDP deflator growth	12.1	21.3	10.9	4.8	3.7	(0.2)	2.0	2.4	1.6	3.0
Exchange rate, year-end (LC/$)	18,932.0	20,828.0	20,828.0	21,036.0	21,246.0	21,890.0	22,296.0	22,296.0	22,296.0	22,296.0
Banks' claims on resident non-gov't sector growth	32.4	14.3	8.8	12.7	13.5	16.0	16.0	16.0	16.0	16.0
Banks' claims on resident non-gov't sector/GDP	114.7	101.8	94.8	96.8	100.0	108.9	116.6	124.3	133.7	141.7
Foreign currency share of claims by banks on residents	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Foreign currency share of residents' bank deposits	18.0	16.8	13.4	13.9	12.4	12.4	12.4	12.4	12.4	12.4
Real effective exchange rate growth	(4.2)	(0.7)	8.5	7.8	3.7	10.3	N/A	N/A	N/A	N/A

Savings is defined as investment plus the current account surplus (deficit). Investment is defined as expenditure on capital goods, including plant, equipment, and housing, plus the change in inventories. Banks are other depository corporations other than the central bank, whose liabilities are included in the national definition of broad money. Gross external financing needs are defined as current account payments plus short-term external debt at the end of the prior year plus nonresident deposits at the end of the prior year plus long-term external debt maturing within the year. Narrow net external debt is defined as the stock of foreign and local currency public- and private- sector borrowings from nonresidents minus official reserves minus public-sector liquid assets held by nonresidents minus financial-sector loans to, deposits with, or investments in nonresident entities. A negative number indicates net external lending. LC--Local currency. CARs--Current account receipts. FDI--Foreign direct investment. CAPs--Current account payments. The data and ratios above result from Standard & Poor's own calculations, drawing on national as well as international sources, reflecting Standard & Poor's independent view on the timeliness, coverage, accuracy, credibility, and usability of available information.

Ratings Score Snapshot

Socialist Republic of Vietnam - Ratings Score Snapshot	
Key rating factors	
Institutional assessment	Weakness
Economic assessment	Weakness
External assessment	Strength
Fiscal assessment: flexibility and performance	Neutral
Fiscal assessment: debt burden	Neutral
Monetary assessment	Weakness

Socialist Republic of Vietnam - Ratings Score Snapshot (cont.)

Standard & Poor's analysis of sovereign creditworthiness rests on its assessment and scoring of five key rating factors: (i) institutional assessment; (ii) economic assessment; (iii) external assessment; (iv) the average of fiscal flexibility and performance, and debt burden; and (v) monetary assessment. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). Section V.B of Standard & Poor's "Sovereign Rating Methodology," published on Dec. 23, 2014 , summarizes how the various factors are combined to derive the sovereign foreign currency rating, while section V.C details how the scores are derived. The ratings score snapshot summarizes whether we consider that the individual rating factors listed in our methodology constitute a strength or a weakness to the sovereign credit profile, or whether we consider them to be neutral. The concepts of "strength", "neutral", or "weakness" are absolute, rather than in relation to sovereigns in a given rating category. Therefore, highly rated sovereigns will typically display more strengths, and lower rated sovereigns more weaknesses. In accordance with Standard & Poor's sovereign ratings methodology, a change in assessment of the aforementioned factors does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the assessments.

Related Criteria And Research

Related Criteria

- Standard & Poor's National And Regional Scale Mapping Tables, Jan. 19, 2016
- National And Regional Scale Credit Ratings, Sept. 22, 2014
- Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers, May 7, 2013
- Sovereign Rating Methodology, Dec. 23, 2014
- Methodology: Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009

Related Research

- Asia-Pacific Sector Outlook 2Q 2016: Net Negative Bias Inches Up To 9%, April 18, 2016
- Corporate And Government Ratings That Exceed The Sovereign Rating, April 15, 2016
- Sovereign Risk Indicators at http://spratings.com/sri
- Asia-Pacific Credit Outlook 2Q 2016: Downgrade Momentum Will Continue, April 12, 2016
- Sovereign Ratings Score Snapshot, April 4, 2016
- Banking Industry Country Risk Assessment Update: March 2016, March 23, 2016
- Emerging Markets Sovereign Debt Report 2016: Borrowing Is Pointing Up This Year, Feb. 29, 2016
- Global Sovereign Debt Report 2016: Borrowing To Drop By 2% To US$6.7 Trillion, Feb. 29, 2016
- Asia-Pacific Sovereign Debt Report 2016: Borrowing Of US$2.5 Trillion Is Likely This Year, Feb. 29, 2016

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee agreed that all key rating factors were unchanged.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Ratings Affirmed

Vietnam (Socialist Republic of)	
Sovereign Credit Rating	BB-/Stable/B
ASEAN Regional Scale	axBB+/--/axB
Senior Unsecured	BB-
Commercial Paper	B

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.