Mizuho Flash: Vietnam

Economics & Strategy | Asia ex-Japan

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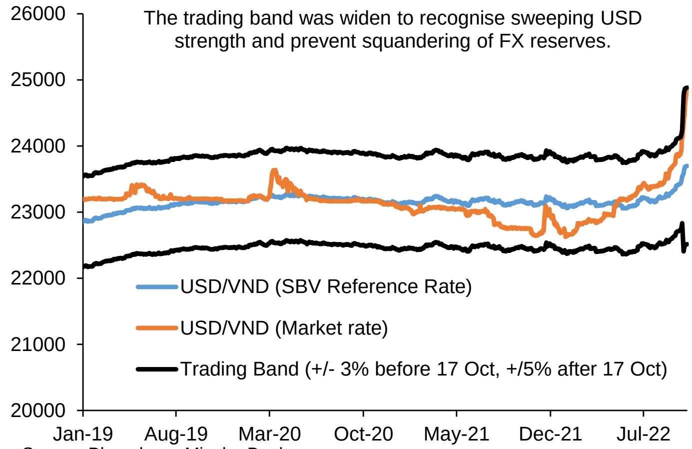
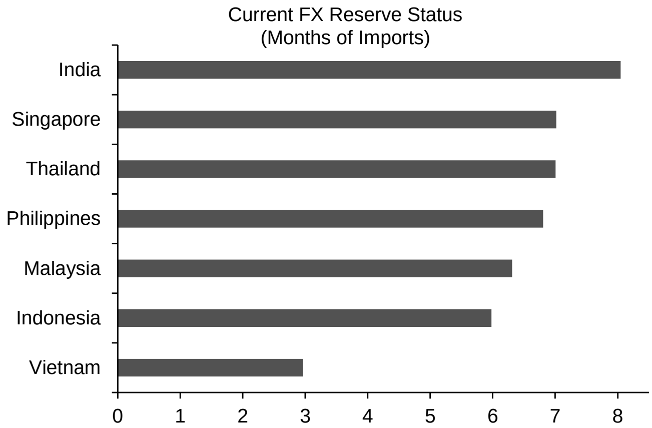
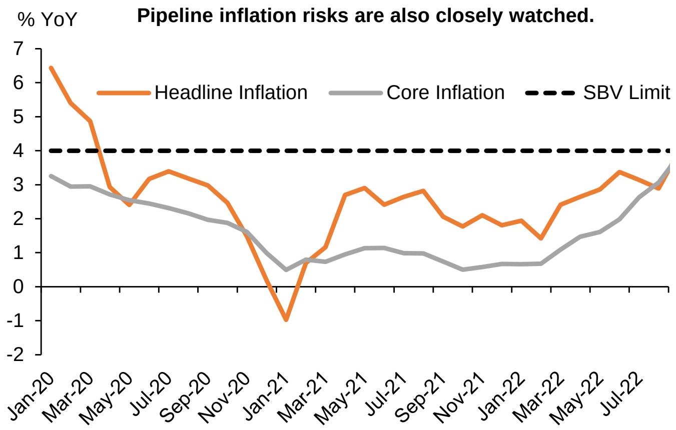
SBV: Restoring Confidence?



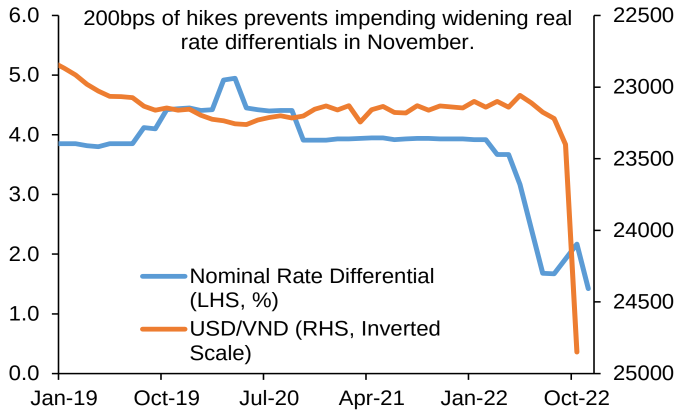
Source: Bloomberg; Mizuho Bank



Source: CEIC; Mizuho Bank



Source: CEIC, Mizuho Bank



Source: CEIC, Mizuho Bank
Note: October's USD/VND taken as of 25 Oct
November's rate differential assumes 75bps Fed hikes & no SBV hike

- The State Bank of Vietnam (SBV) took another emphatic rate hike of **100bps**, raising the refinancing rate from 5% to 6%, which fully **restores the policy rate to pre-pandemic levels.** This move follows from their first rate increase which was also a 100bp hike on 22 September. The need to **prevent macroeconomic instability** and restore confidence in the VND is apparent.

- **<u>The VND and FX reserves</u>**: On 17 October, the SBV widened the USD/VND trading bands* to accommodate broad based USD strength and prevent arbitrary defence of VND levels which may lead to squandering of reserves; ultimately imperilling the very VND stability it aims for.

- Since then, the VND had depreciated 2.9% against the USD, **leaving a 0.2% gap** to the upper bound to start this week, underscoring the USD strength and tells of the immense pressures which FX reserves would have to continue to bear if the narrower limits were defended. While FDI inflows and economic growth remain steady, their **FX reserves position is still a budding one** relative to regional peers as it stands just below 3 months of import cover.

- The threat here is that excessive reserve drawdown to defend the VND will trigger capital outflow risks and **dent years of efforts in building up investor confidence**. **As such, their second 100bps hike is required to further complement their efforts to stabilise the VND, rather than relying**

solely on FX intervention.

- **Fed and Inflation Risks: The pre-emptive need here is two-fold.** The **first** one is in view of the rate differentials with the Fed which is set to widen by at least 75bp next week and consequently add to VND depreciation pressures.

- **Second**, **the SBV also has their attention on pipeline inflation risks,** with the headline and core inflation likely to breach 4% in the coming months as October's inflation print will reveal on 29 October. The government's **upgrade of their inflation target for 2023 to 4.5%** highlights impending inflationary pressures and also reminds of the need for policy flexibility.

- Overall, it is **critical that the SBV shore up confidence in the VND and prevent undue panic from triggering financial and economic instability**. While a current account deficit of US$3.7bn was posted for Q2 2022, **FX reserves** at above US$100bn as of June 2022 **suffice at addressing economic fundamentals**. That said, the issue is that troubling memories of FX instability in previous decades may still haunt markets.

*See Mizuho Chart Speak: SBV-VND: Wider Bands About USD Exceptionalism, Not VND Mercantilism, 17 Oct

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