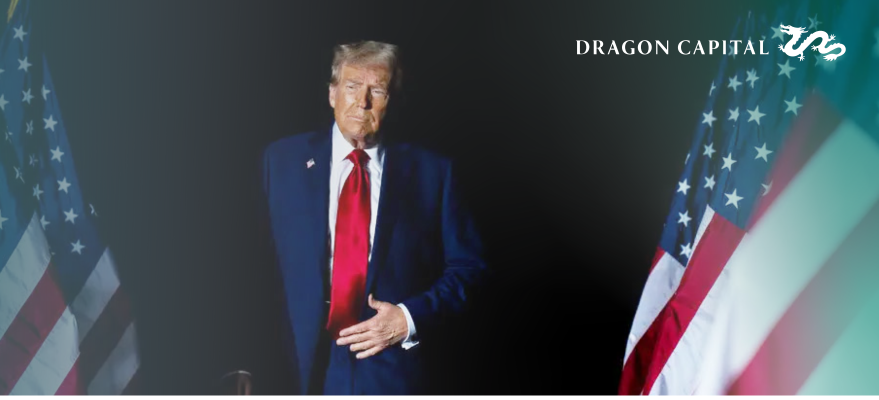
DRAGON CAPITAL



# FLASH NOTE:

# KEY TAKEAWAYS OF TRUMP 2.0 FOR VIETNAMESE MARKETS

Release date: 8 November 2024

In our view, the key takeaways for Vietnamese markets from Trump 2.0 are:

- **Short-Term Impact:** Equity markets are expected to see heightened volatility. However, companies in our coverage are on "watch mode" with no immediate earnings pressures from this event. Export-oriented companies with direct exposure to potential Trump policies hold a limited weight in the VN index, meaning any downside risks from this group are not expected to significantly impact overall market performance. Local sentiment remains more optimistic, as many Vietnamese retail investors view Trump's presidency favourably.

- **Medium-Term Impact:** Market volatility is likely to continue under Trump's administration. But we can divide this into 2 scenarios. In the case of extreme protectionist policies, trade activity will slow, creating secondary earnings pressures. In such a scenario, earnings growth for Vietnamese companies could decelerate from the current 16-18% range to mid-single-digit levels, impacting the broader growth outlook. A more probable scenario involves selective tariffs on specific countries or products, which could ultimately benefit Vietnam through tariff differentials with China.

- Given China's 32% share of global manufacturing versus Vietnam's 2-3%, **increased trade headwinds for China could position Vietnam to capture a larger share of manufacturing and export demand**, much like it did during the previous Trump administration. This trend could further accelerate localisation efforts among Vietnamese manufacturers, enhancing Vietnam's real economy and supporting equity markets as the shift unfolds.

We explore our reasoning on the longer-term impacts below.

## Trump 2.0 and Trade Policy

With Trump's victory we anticipate significant policy shifts with global repercussions over the next four years. Many have argued that a Trump-led administration could pose challenges for export-driven economies, including Vietnam.

In the 2024 campaign, Trump emphasised aggressive trade measures aimed at safeguarding the U.S. economy. Notably:

- 60% tariff on Chinese goods to reduce the trade deficit with China and boost domestic manufacturing; and,

- 10-20% broad tariffs on other nations aimed at protecting U.S. industries from foreign competition.

Whether campaign statements fully translate into policy is both uncertain and subject to the time lag of the transition between administrations as well as the breadth of control & consensus of purpose the GOP ultimately wields over Congress. Nevertheless, the risks arising from more protectionist policies with a uniquely punitive treatment of China appears must be assessed.

## Impact on Equity:

In the three years prior to COVID-19 under Trump's administration, Vietnam's equity market achieved an impressive net profit growth of 19.1%. However, the unpredictability of Trump's policies and public statements heightened market volatility. Despite this, the VN Index delivered a compounded return of about 15% over this period, slightly lagging profit growth due to a discount for volatility.

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Presently, Vietnam's economic and trade outlook remains relatively positive, supported by a pro-growth leadership that could bring more opportunities than risks. On the downside, the potential strengthening of the dollar could extend the foreign selling in emerging markets in favour of U.S. equities. Emerging markets, including Vietnam, may continue to experience valuation discounts, as seen during Trump's first term. Consequently, expected returns in Vietnam's equity market may once again lag earnings growth. While this risk is notable, the valuation of our Top-80 universe of stocks remains at 11.6x based on projected 2024 earnings, compared to the five-year historical average of 13.9x, suggesting limited room for further de-rating due to support from value-minded domestic investors.

### Trump 1.0

During the first Trump administration, three significant actions stood out in the context of Vietnam–U.S. bilateral trade:

**1. Illegal-transshipment Investigations on Timber:**

In October 2017, The U.S. initiated Section 301 Trade Act investigations on Vietnam's imported timber, particularly potential illegal transshipment from China to avoid tariffs. This raised concerns that U.S. tariffs could be imposed on Vietnam's wooden exports after the investigations. The investigation lasted through the end of Trump's term and into Biden's presidency. In 2021 USTR determined that Vietnamese timber exports were not in violation, and no tariff was imposed. Nevertheless, this example highlights how the perception of transshipment represents an area of acute sensitivity.

**2. Tariffs on Steel and Aluminium:**

In March 2018, the U.S. imposed a 25% tariff on steel and a 10% tariff on aluminium imports from various countries, including the EU, Canada, Mexico, Australia, Brazil, South Korea, and Vietnam. Recently, President Biden extended this tariff rate until 2025. Tariffs as a tool for protecting the interests of U.S. commodity producers remained consistent across both administrations and there is no foreseeable case for this to change.

**3. Currency Manipulation:**

In 2020, a U.S. Treasury report concluded that Vietnam met the criteria for currency manipulation. As a result, the U.S. Treasury labelled Vietnam a currency manipulator in its December 2020 report, though no tariffs were imposed on Vietnamese exports and the U.S. ultimately removed Vietnam from the currency manipulator list in 2021. The uncertainty created during the period of review, however, highlights the risk that even suspicion rather than outright sanction can be a source of disruption.

## Trump 2.0

Trump's campaign statements on tariffs, if enacted into policy, could have negative impacts on exporting nations, including Vietnam. Bilateral trade between Vietnam and the U.S. has grown substantially over the past two administrations, rising from $50 billion in 2016 to $110 billion in 2023, a near 120% increase over eight years. It is important to note that U.S.–Vietnam relations have evolved significantly since Trump's first term. The two countries have elevated their relationship to the highest diplomatic level of Comprehensive Strategic Partners (CSP), with commitments to cooperation across numerous fields. Nevertheless, we believe the following risks remain:

- **Trade investigation:**

  Vietnam has a substantial trade surplus with the U.S., placing it among the top four countries with the largest trade surpluses. Combined with a steady increase in Chinese FDI and a doubling of Vietnam's imports from China in recent years, this has led to concerns about potential trade investigations into transshipment practices. Vietnam's Ministry of Industry and Trade has disclosed that several Vietnamese exports are on a watchlist for possible trade defence measures, origin fraud, and illegal transshipment investigations. Notably, four products[ii], including solar panels, totalled $10.6 billion and accounted for nearly 11.5% of Vietnam's exports to the U.S. in 2023. Concentrated export categories of this type are at risk of drawing scrutiny and sanction.

- **Currency Manipulation Allegations:**

  Since 2019, Vietnam has consistently asserted that it does not use exchange rate policies to gain a competitive advantage in international trade, but the U.S. Treasury's June 2024 report once again placed Vietnam on its monitoring list.

  We believe that the likelihood of Vietnam being labelled as a currency manipulator is low as the Vietnamese government has been acting to prevent currency devaluation to defray the importing of inflation and preserve domestic consumption rather than to achieve a pricing benefit in trade. Since 2022, the State Bank of Vietnam has spent over $20 billion in reserves to stabilise the VND, underscoring its commitment to currency stability. Vietnam's current account balance stands at 5.8% of GDP, while its bilateral trade surplus with the U.S. reached $103 billion. This provides scope for Vietnam to counter concerns on currency manipulation by narrowing the trade surplus – a point upon which we will expand in the next section.

- **0-20% Broad-Based Tariffs on All Exporters:**

  Imposing broad-based tariffs on all countries is less likely, as the U.S. is a consumption-driven market with an annual trade deficit of around $600 billion. Such tariffs would significantly raise domestic prices of imported goods, impacting American consumer spending. Even if these tariffs were applied to all countries, Vietnam could retain a competitive edge due to its comparative advantages including geographic location, low labour costs, and its network of free trade agreements. Ultimately, while protectionist rhetoric plays well during an election cycle, the realities of structurally higher prices are likely less politically tenable in practise. Consequently, the translation of rhetoric into policy may prove to be selective.

## What are Vietnam's Options?

Given these potential risks, Vietnam may consider proactive measures to safeguard its economic interests by addressing U.S. concerns:

- **Narrow the trade surplus with the U.S.:**

  Vietnam could expand imports from the U.S. to help reduce the trade surplus. Potential imports include aircraft, Liquefied Natural Gas (LNG), defence, and, services. During Trump's first term, Vietnam and the U.S. engaged in extensive discussions on energy imports, particularly LNG. Trump's return to office may increase external pressure on Vietnam to finalise outstanding legal frameworks and accelerate the integration of LNG into its national energy portfolio.

- **Reduce Transshipment flow of Chinese products:**

  Vietnam is currently conducting anti-dumping investigations on hot-rolled coil (HRC) and galvanised steel imports from China and South Korea, with possible tariffs on these products by early 2025. This action underscores Vietnam's commitment to mitigating the risk of becoming a transshipment hub for steel products, which could pose risks to its overall position as an exporter.

- **Trade Agreement Negotiation:**

  Establishing a bilateral trade agreement could provide a formal mechanism for resolving trade disputes and reaffirm Vietnam's stance against acting as a transshipment hub for Chinese goods. These negotiations could include specific commitments on rules of origin and localisation in key export sectors, helping Vietnam avoid stringent trade remedies. While trade agreements are on option upon the table, they will be unlikely to be a priority for a protectionist America and so we believe this to only be likely as a medium to long term remedy.

## Impacts over the Longer Term:

China holds a massive 32% share of global manufacturing, while Vietnam currently captures just 2-3%. As Trump 2.0 likely increase China's trade headwinds, other nations stand to gain as an alternative if for no other reason than the inevitable implementation lag & consumer price impact of America homeshoring manufacturing. Vietnam is positioned to benefit from the continuing shift of supply chains and manufacturing hubs, much like it did during the previous Trump administration. Still, with this opportunity comes the likelihood of intensified scrutiny on Vietnamese goods, a trend that could play out over the medium term. The initial impact may be most pronounced for FDI firms with ties to China, particularly those at risk of transshipment concerns. Overall, we believe that the net impact of new opportunities – even with additional scrutiny – remains in Vietnam's favour.

Vietnam is expected to respond proactively, leveraging its experience with similar challenges to take targeted and pre-emptive steps. This environment could even create momentum for Vietnam to drive significant policy shifts. Ideally, Vietnam might reach an agreement with the U.S. to clarify rules of origin and address concerns around transshipment, supporting local suppliers and increasing localisation rates. Accelerated localisation represents multiple benefits to the Vietnamese economy in diversification & depth, with the ultimate being the capacity to repurpose OEM manufacturing capability into direct-to-consumer sales enabling more of the margin in products to be captured locally.

While the outcome of the U.S. election may pose short-term challenges for Vietnam, the long-term impact could prove favourable. As it is too soon to draw any firm conclusions, we will continue to update you on impacts as policy and its timetable becomes certain.

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Exceeding $20 billion in trade surplus with the U.S. within 12 months;
A current account surplus over 2% of GDP across four quarters; and,
Net purchases of foreign currency in at least 8 out of 12 months, totalling at least 2% of an economy's GDP, representing one sided intervention.

Solar Panels: Solar panels were among the first products targeted by U.S. tariffs on Chinese goods. Since then, Vietnam's solar panel exports to the U.S. have reached over $4.4 billion in 2023, marking a nearly 400% increase from 2019 and accounting for 26.5% of the U.S. market for these products. While the U.S. Department of Commerce (DOC) has repeatedly proposed additional tariffs on Vietnamese solar panels, President Biden rejected this proposal in 2023.

Wooden Products: Vietnamese wood products under scrutiny represent nearly $5.3 billion out of the $8 billion in total wood exports to the U.S. The DOC investigated several cases to determine whether Vietnamesecompanies use Chinese parts in their products once again highlighting transhipment risks.

Washing Machines: Vietnam's washing machine exports to the U.S. reached $440 million in 2023, an increase of over 300% compared to previous years.

Electric Bicycles: Exports to the U.S. totalled $50.8 million in 2023.

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