Strong economic growth in Vietnam will help open up opportunities in a variety of sectors outside of manufacturing over the coming years, although the business environment remains challenging. Structural factors, including rapidly rising incomes, major urbanisation and an ageing population, will underpin expansion in three sectors in particular – construction, electricity transmission and distribution, and health care.

The rapid pace of Vietnam's economic growth is creating avenues for investment in a range of sectors. Real GDP growth, which stood at around 6.6% in 2014–18, will average 6.5% over 2019–23, according to IMF forecasts, outpacing both China (5.9%) and the emerging market average (4.8%).

Corporate interest in Vietnam has surged and foreign direct investment (FDI) inflows grew at an annual average rate of 12% over 2014–18 to reach $15.5bn.[1]This has turned Vietnam into the eighth-largest recipient of FDI in the emerging world, as classified by the UN.

FDI has thus far been concentrated in Vietnam's booming manufacturing export sector. Exports from the sector have grown at an average annual rate of 22.4% over the past ten years, effectively doubling every three years from $32bn in 2009 to $244bn in 2018.[2]

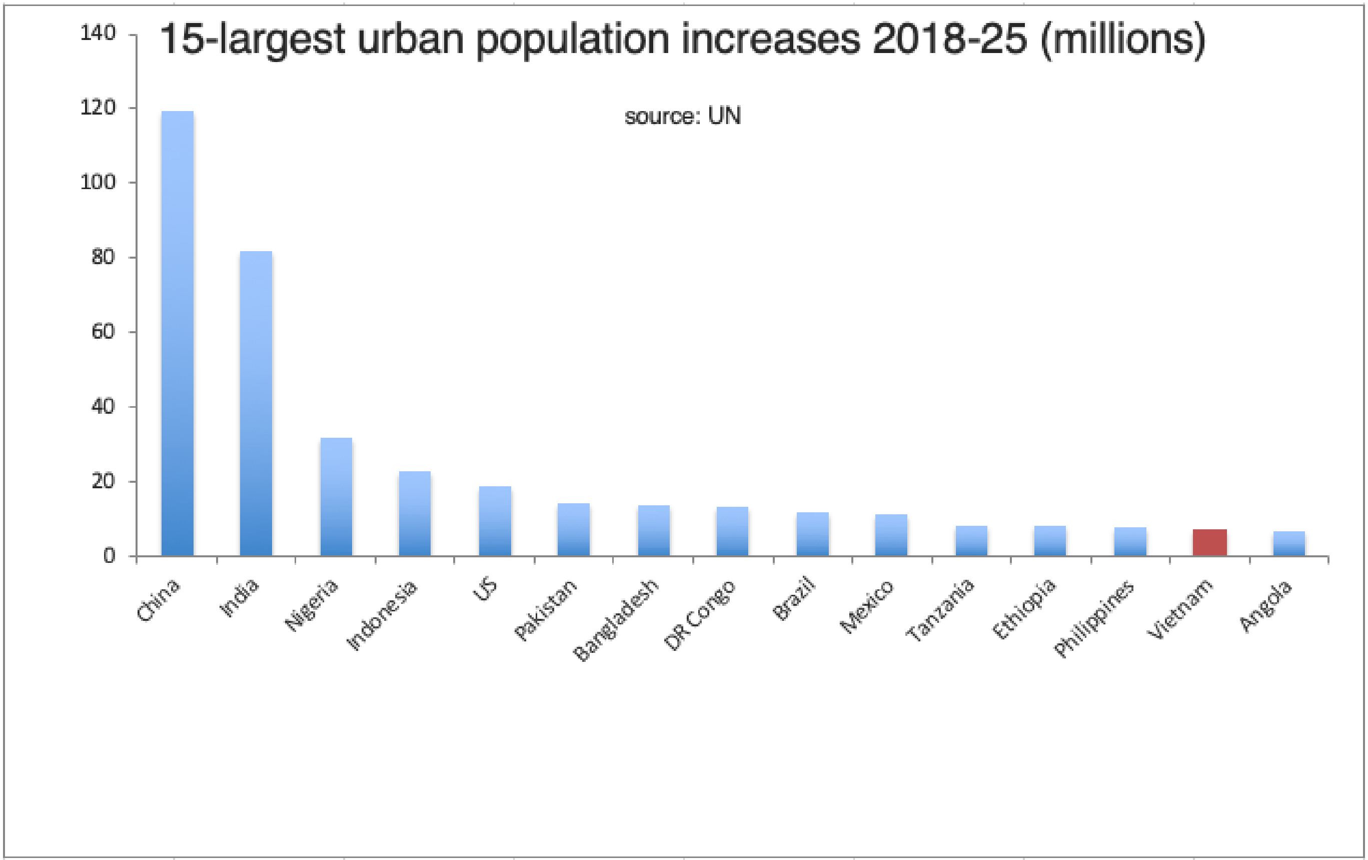
Three of the most promising sectors outside of manufacturing are construction, electricity transmission & distribution and health care. The following structural drivers will contribute to growth in these industries by boosting demand:

Surging household incomes Per capita income will rise by almost half from $2,551 in 2018 to $3,646 in 2023[3]

Major urbanisation The share of the population living in urban areas is expected to rise from 33.8% in 2015 to 40.9% in 2025. This would imply an additional 5.3m urban residents[4]

Rapidly ageing population The IMF expects the share of over-60s in the total population to double over the next 25 years

Privatisation State owned enterprises accounted for around 35% of the economy in 2018[5]The government intends to steadily reduce this share through privatisations in the coming years



Construction to create short- and long-term opportunities

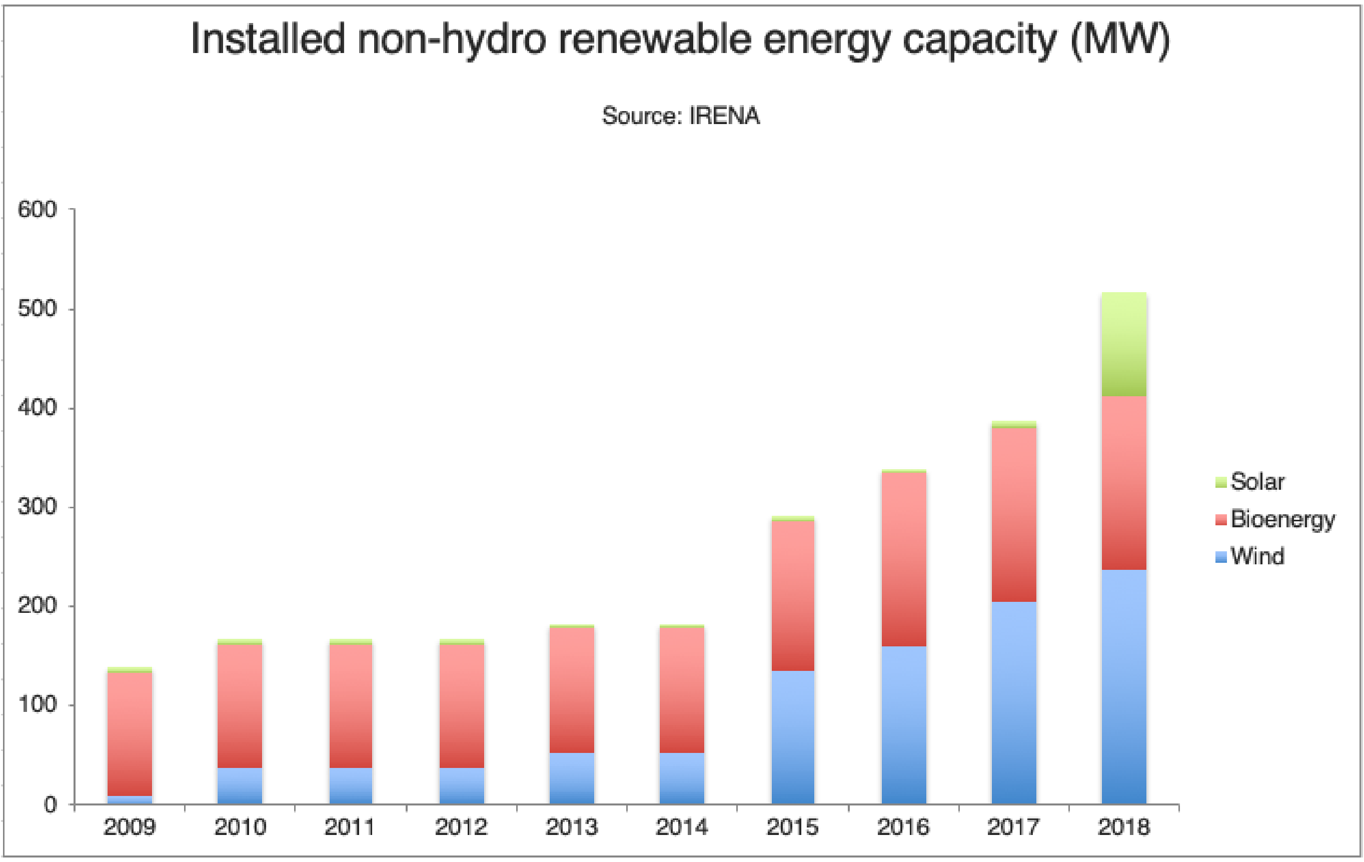
The government has ambitious infrastructure targets and there is already a healthy construction sector pipeline. This will create opportunities for private sector firms, as budgetary constraints force the government to fund an increasing share of infrastructure expenditure through public-private partnerships (PPPs). Authorities are drafting new legislation to limit the risk faced by private firms engaged in these partnerships, for instance by providing revenue guarantees. The Asian Development Bank estimated the value of PPP infrastructure investment in Vietnam at $12.8bn, or 5.7% of the economy in 2017.

Engineering, procurement and construction firms will benefit from substantial investment in industrial and residential infrastructure. Major projects approved in 2018 include more than $2bn of South Korean investment into a polypropylene factory and two electronics factories, and Japanese investment in the construction of a $4.1bn “smart” residential township in Hanoi. The flagship transport project is the $58.7bn Hanoi-Ho Chi Minh City high-speed rail project.

Rapid urbanisation will also boost demand for firms specialising in operating urban infrastructure, such as water and waste systems. For instance, only about 10% of wastewater in the country is currently treated and the government plans to vastly increase this share over the coming years.

Electrical grid will need both expansion and sophistication

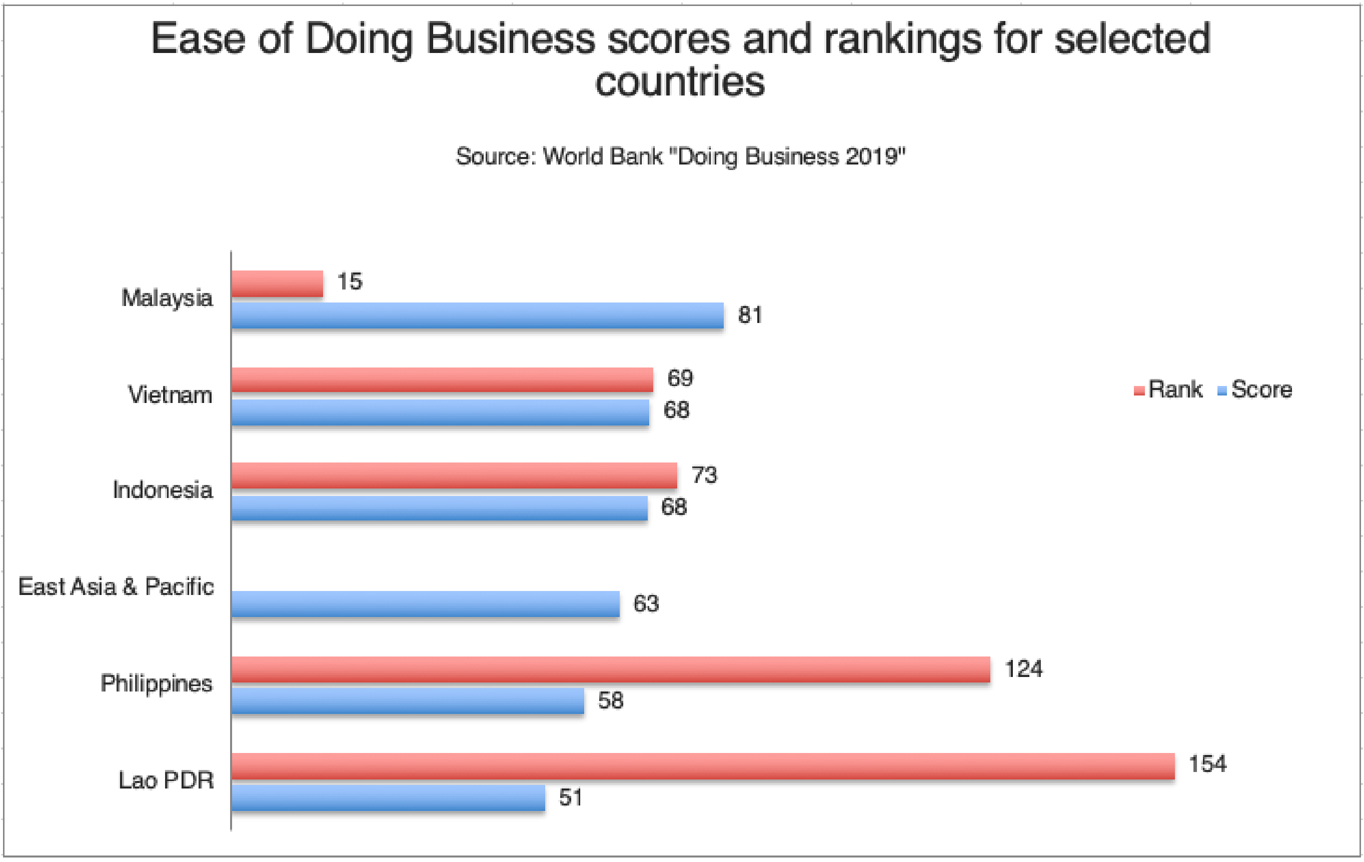
Surging investment in power generation will require major expansion and modernisation of the electrical grid over the next decade. The EIA estimates that 17% of total electricity generated was lost during transmission and distribution in 2016, illustrating existing inefficiency.[6]The current Power Development Plan (PDP) sets out $37bn of investment into the electricity grid over 2016–30, with $10bn to be spent by 2020. Aside from extending the grid to connect new urban and industrial areas, sophistication of the grid will be necessary in order to integrate surging sources of intermittent renewable power such as wind and solar. The PDP aims to increase the share of renewable sources in total electricity generation to 7% in 2020 and more than 10% in 2030.[7]



Health care to benefit from structural uptick in government spending

A rapidly ageing population will drive a significant increase in health care spending in Vietnam over the coming decade. The provision of adequate social and health services will increasingly be a priority for the government as it attempts to prevent pressure growing for political liberalisation as the economy matures. Public sector spending will grow strongly, with the government looking to implement a comprehensive national health insurance scheme by 2025.

There is also scope for expansion of the private health care sector. The Ministry of Health estimates that residents currently spend $2bn annually on travel abroad for medical services, reflecting huge potential for domestic private health care sales growth.



Risks to continued business reform

Continued pro-investment reforms will be required in order to attract the FDI necessary to sustain rapid economic growth.

The operating environment for foreign firms remains challenging, despite significant reforms over the past decade. Transparency International ranks Vietnam 117th for corruption, while the country's overall position on the World Bank's "Doing Business" report has stalled at 69th in the past two years, held back in part by particularly weak scores for starting a business, paying taxes and resolving insolvency. In reflection of these challenges, the government is currently drafting a new FDI Attraction Strategy for 2020–30 in partnership with the World Bank.

Vietnam business environment rankings				
Measure	**Position**	**Total countries**	**Year**	**Source**
Competitiveness	77	140	2018	World Economic Forum Competitiveness Index
Corruption	117	180	2018	Transparency International Corruption perceptions Index
Ease of doing business	69	190	2019	World Bank "Doing Business" report
Innovation	45	126	2018	Global Innovation Index

Political instability is the greatest risk to this reform trajectory. Although one-party rule in Vietnam increases the chance of policy continuity in the near term, it arguably raises risk of political volatility in the longer term. The state will likely gradually face stronger local pushback against its current centralised and corporatist political model, which prioritises the interests of the industrial sector. Issues such as corruption, environmental degradation and competition from foreign firms are potential flashpoints for political protest over the next decade.

Not only could reform stall, but the business environment could become more challenging as more populist policies are adopted. Such a scenario would threaten existing pro-investment measures, such as tax breaks for foreign firms, free trade agreements and generous allocation of land to industrial development.

John Davies is an economist with a special interest in emerging markets, global trade and heavy industry. He is the co-founder of research and analysis firm, North Shore Analysis.

Sources:
[1] Energy Information Administration, International Energy Statistics Database

[2] Ministry of Industry and Trade

[3] UN World Urbanization Prospects 2018

[4] Export.gov

[5] UNCTAD

[6] IMF World Economic Outlook, April 2019

[7] UNCTAD

Featured Image © Shutterstock.com

