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FREIGHT TRANSPORT REPORT

INCLUDES BMI'S FORECASTS

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VIETNAM FREIGHT TRANSPORT REPORT Q3 2011

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CONTENTS

Executive Summary

We maintain our forecast of a good year for Vietnamese freight transport in 2011. Our overall view has two major components: a background of high single-digit growth of the economy on the one hand (albeit at a slower rate than in 2010) and some disparities in the pace of expansion of freight capacity by transport mode on the other. While investment is being channelled into ports and container terminals, for example, officials admit that the rail freight sector is plagued by insufficient track and signalling.

As far as the economy is concerned, the authorities are acting to cool down the pace of growth so as to be able to control inflationary pressures and narrow the foreign trade deficit. While this is forcing a cut-back in some public sector investment projects and therefore slower growth, BMI believes that a short term correction is necessary, and will ultimately be a positive factor on the medium to longer term.

As far as the freight industry is concerned, it is important to note that it is only in the ports and shipping and road haulage sectors that freight tonnage will expand at a faster-than-GDP rate this year. Road haulage will be ahead of GDP by only 0.2 of a percentage point (6.5% vs 6.3%) while the ports sector will be ahead only in some terminals (eg. Saigon New Port). Volume growth across all other transport modes will lag behind GDP: airfreight (+5.3%), followed by rail (+4.8%) and inland waterways (+4.3%)

Headline Industry Data

- The real value of total trade will rise by 11.3% this year, with exports gaining 11.0%, behind import growth of 11.6%

- Total volume handled at SNP (Saigon New Port, also known as Port of Ho Chi Minh City) will rise 7.5% to 21.843mn tonnes this year, while volume at the PDN (Port of Da Nang) will rise 2.8% to 3.29mn tonnes.

- Airfreight will grow by 5.3% this year to 147,910 tonnes.

Key Industry Trends

Jade Cargo Opens Hanoi Route

Netherlands-based Jade Cargo has launched twice-weekly freighter flights to Hanoi via Shanghai, India and Dubai. Executives say they are building the company's Asian network and are encouraged by Vietnamese airfreight exports, particularly in the high-tech sector.

Movement On Long Thanh International Airport

The plan to build a new airport - the country's largest - at Long Thanh has been stuck in the pipeline for years, but now the authorities say work on the US$1.27bn project will start in 2015.

Japanese Interest In Vietnam Ports Surges

The Japanese government, investors, contractors, and shipping lines are all looking to get involved in the

Vietnamese ports and shipping sector. JICA (Japan International Cooperation Agency) is funding the bulk of a JPY140bn (US$1.7bn) new port project at Lach Hyuen in northern Vietnam. Shipping lines MOL and NYK are opening new services to the country. Japan's Kobe Steel says it will build its own US$244-365mn port there to secure iron nugget supplies.

Key Risks To Outlook

The main risk to our freight transport projections is that this year's macro-economic slowdown might be more severe than expected. A potential scenario in which this could happen would be if both domestic inflation and the foreign trade deficit remain much higher than desired, and show no signs of responding to the tightening measures already taken. The authorities could then find themselves forced to take more severe measures, with a consequent negative impact on GDP growth and demand for shipping services.

SWOT Analysis

Vietnam Freight Transport SWOT	
Strengths	▪ Strong domestic growth, coupled with geography (long country, stretching for thousands of kilometres on north-south axis) creates need for long-distance freight haulage. ▪ Recovery of the nation's ports in 2010 is expected to continue over the mid-term. ▪ Vietnam's location on the South China Sea gives the country access to the main inter-Asian shipping routes, as well as access to the developing land transport links with ASEAN countries, allowing the country scope to develop its trade logistics..
Weaknesses	▪ The generally poor state of the road network. Despite new highway construction, only 13.5% of the road network is considered to be in good condition, only 26% has two or more lanes and only 29% is tarred. ▪ Traditionally low investment in rail; although attempts are being made to rectify this, the potential of rail for cost-effective bulk freight is being under-utilised. ▪ Decades of under-investment have left the country with a port infrastructure system that is poor by international standards.
Opportunities	▪ The beginnings of local commercial vehicle production, which will help improve the stock of lorries used by road haulage companies. ▪ Chinese investment could bring about much needed improvements in the rail sector. ▪ Growing international interest in Vietnam as a growth market in box shipping sector.
Threats	▪ Vietnam risks losing out to neighbouring countries if it can't develop its infrastructure to keep up with the pace of demand. ▪ Vietnam is vulnerable to any slowdown in Chinese investment. ▪ A drop in international demand for exports would affect freight transport sector.

Vietnam Political SWOT	
Strengths	▪ Communist Party government appears committed to market-oriented reforms, although specific economic policies will undoubtedly be discussed at 2011 National Congress. One-party system is generally conducive to short-term political stability. ▪ Relations with the US are generally improving, and Washington sees Hanoi as a potential geopolitical ally in South East Asia.
Weaknesses	▪ Corruption among government officials poses a major threat to the legitimacy of the ruling Communist Party. ▪ There is increasing (albeit still limited) public dissatisfaction with the leadership's tight control over political dissent.
Opportunities	▪ The government recognises the threat that corruption poses to its legitimacy, and has acted to clamp down on graft among party officials. ▪ Vietnam has allowed legislators to become more vocal in criticising government policies. This is opening up opportunities for more checks and balances.
Threats	▪ The slowdown in growth in 2009 and 2010 is likely to weigh on public acceptance of the one-party system, and street demonstrations to protest economic conditions could develop into a full-on challenge of undemocractic rule. ▪ Although strong domestic control will ensure little change to political scene in the next few years, over the longer term, the one-party-state will probably be unsustainable.

- Relations with China have deteriorated over the past year due to Beijing's more assertive stance over disputed islands in the South China Sea and domestic criticism of a large Chinese investment into a bauxite mining project in the central highlands, which could potentially cause widescale environmental damage.

Vietnam Economic SWOT	
Strengths	▪ Vietnam has been one of the fastest-growing economies in Asia in recent years, with GDP growth averaging 7.6% annually between 2000 and 2009. ▪ The economic boom has lifted many Vietnamese out of poverty, with the official poverty rate in the country falling from 58% in 1993 to 20% in 2004.
Weaknesses	▪ Vietnam still suffers from substantial trade, current account and fiscal deficits, leaving the economy vulnerable as the global economy continues to suffer in 2010. The fiscal picture is clouded by considerable 'off-the-books' spending. ▪ Heavily managed and weak dong reduces incentives to improve quality of exports, and also serves to keep import costs high, thus contributing to inflationary pressures.
Opportunities	▪ WTO membership has given Vietnam access to both foreign markets and capital, while making Vietnamese enterprises stronger through increased competition. ▪ The government will in spite of current macroeconomic woes, continue to move forward with market reforms, including privatisation of state-owned enterprises, and liberalising the banking sector. ▪ Urbanisation will continue to be a long-term growth driver. The UN forecasts the urban population to rise from 29% of the population to more than 50% by the early 2040s.
Threats	▪ Inflation and deficit concerns have caused some investors to re-assess their hitherto upbeat view of Vietnam. If the government focuses too much on stimulating growth and fails to root out inflationary pressure, it risks prolonging macroeconomic instability, which could lead to a potential crisis. ▪ Prolonged macroeconomic instability could prompt the authorities to put reforms on hold, as they struggle to stabilise the economy.

Vietnam Business Environment SWOT	
Strengths	▪ Large, skilled, low-cost workforce has made Vietnam attractive to foreign investors. ▪ Vietnam's location (proximity to China and South East Asia and good sea links) makes it a good base for foreign companies to export to the rest of Asia, and beyond.
Weaknesses	▪ Vietnam's infrastructure is still weak. Roads, railways and ports are inadequate to cope with the country's economic growth and links with the outside world. ▪ One of the world's most corrupt countries. Its score in Transparency International's 2009 Corruption Perceptions Index was 2.7, 22nd place in the Asia Pacific region.
Opportunities	▪ Vietnam is increasingly attracting investment from key Asian economies, such as Japan, South Korea and Taiwan. This offers possibility of transfer of high-tech skills. ▪ Vietnam is pressing ahead with privatisation of state-owned enterprises and liberalisation of banking sector. This should offer foreign investors new entry points.
Threats	▪ Ongoing trade disputes with the US, and the general threat of American protectionism, which will remain a concern. ▪ Labour unrest remains a lingering threat. A failure by the authorities to boost skills levels could leave Vietnam a second-rate economy for an indefinite period.

Industry Trends And Developments

Multimodal And Logistics

Logwin Boosts Garment Capacity

Luxembourg-based global logistics operator Logwin was in February reported to be expanding its garment logistics facilities in Vietnam owing to an increase in demand in the country's garment manufacturing sector, as well as a significant growth in international air and ocean freight services. The company has planned to transfer its Ho Chi Minh City logistics operations to a new and bigger warehouse container-freight station (CFS) facility that features a modern racking system, which will increase its storage capacity by twofold to 1,000 pallet positions. Additionally, Logwin expanded its warehouse and consolidation facility in Hanoi from 1,000m2 to 2,000m2, and increased its Haiphong Container Freight Station's capacity to 2,000m2. Industry observers believe the expansion will offer an efficient and economical option for customers as well as enable Logwin to capitalise on emerging trade opportunities.

Road

Green Light For Hanoi-Hai Phong Expressway

The Vietnamese government in March announced that the Hanoi-Hai Phong Expressway project is expected to start commercial operations by late 2013-early 2014. The project, involving an estimated investment of VND24trn (US$1.21bn), is being implemented under the build-operate-transfer (BOT) method. Once completed, the project will have six lanes enabling a vehicle speed of 120km per hour, with two lanes for urgent stops. Infrastructure Development and Financial Investment is the main investor for the project, which is divided into 10 main construction and seven supporting bidding packages. The Hanoi-Hai Phong highway construction project received approval from the Vietnam Development Bank (VDB) for a project involving construction of a 105.5km-long expressway, six lanes and road surfacing. Along the highway, two sudden-stop lanes, six intersections, nine large bridges, 21 medium bridges and 22 overhead bridges will also be built.

Moves To Secure Funding For Nghi Son-Bai Vot Expressway

The Nghe An province People's Committee in March submitted a document to the Vietnamese Ministry of Transport requesting that the Mai Linh Group be granted permission to participate in construction of the 94.1km Nghi Son-Bai Vot Expressway. The expressway will have four-six lanes, and will allow vehicles to travel at up to 120km/h. The authority is negotiating with the World Bank to secure US$1bn in loans for the project during 2011-2014, according to Nguyen Hoang, the head of the department of planning and investment under the Ministry of Transport. In March 2010, Vietnam's Prime Minister Nguyen Tan Dung approved VND350trn (US$18.09bn) for the construction and development of the road system in the country. The funds were approved under the development scheme of 2020 and long-term plan until 2030. The plans include development of a North-South road with a total length of 3,262km, construction of seven roads in the north with a total length of 1,099km, construction of three routes with total length of 264km in central and highland areas, and development of seven routes with a total length of 984km in south area.

Air

New Push For Long Thanh International Airport Project

The Vietnamese Ministry of Transport (MoH) asked Prime Minister Nguyen Tan Dung to approve the construction of the Long Thanh International Airport in the southern Dong Nai province. The project involves construction of a US$1.27bn runway system and parking place, as well as a US$1.4bn passenger terminal. Construction work on the project, expected to be the largest international airport in Vietnam, is anticipated to start in 2015. The Vietnamese government has ambitious plans to modernise and expand the country's airport infrastructure, though some, like the Long Thanh international airport, have been in the pipeline for years with little progress made. However, the government's willingness to get projects off the ground provides grounds for optimism. The Ministry of Transport announced in early May 2009 that it would upgrade and expand Vietnam's main airports. Plans include a new international airport in Phu Quoc, Long Thanh, Cam Ranh, Chu Lai, Danang, and Hue. The Noi Bai airport in Hanoi will be expanded, as will the Cat Bi airport in Haiphong.

Upgrade For Pleiku Airport

The Civil Aviation Administration of Vietnam (CAAV) unveiled a new programme to upgrade Pleiku Airport in the Central Highlands province of Gia Lai. The programme, which will run until 2030 and require an estimated investment of more than VND2.2trn (US$105.59mn), will be carried out in two phases. More than VND745bn (US$35.76mn) will be invested before 2020, while the remainder will be spent before 2030. Financing will be raised from different sources, including enterprises and investors, as well as the state budget. The airport is expected to handle more than 330,000 people annually by 2020 and 500,000 passengers by 2030. The transport sector continues to form the majority of infrastructure investment in Vietnam throughout our forecast period, accounting for 70.3% in 2015. Vietnam still suffers from a significant deficit in transportation infrastructure, and we see reason for the Vietnamese government to continue to develop this sub-sector over the medium term. The government has ambitious plans to modernise and expand the country's airport infrastructure.

Jade Cargo Puts Hanoi On Its Airfreight Map

BMI believes that Jade Cargo's decision to open the first airfreight link between Vietnam and Amsterdam will put the company in a strong position to take advantage of growing airfreight volumes in the country, which is fast becoming the factory of Asia. The move is part of Jade Cargo's expansion of its route network in Asia, and flights to Hanoi began on February 27. The service includes two Boeing 747ERF flights per week, flying from the company's hub in Shanghai to Hanoi on Sundays and Thursdays. The service from the city at the Red River Delta area onwards to Amsterdam will include stopovers in Chennai (Madras), India and Dubai. 'Hanoi has evolved into one of Vietnam's major industrial centres', said Gabriela Ahrens, Jade Cargo's executive vice-president, product and sales. 'With our new connections, we are expanding our customised product to accommodate the increased demand ex

Vietnam, especially of the high-tech industry.' Jade Cargo is the only cargo carrier to offer direct connections between Hanoi and Amsterdam. This further strengthens the airline's dense network in South East Asia. Jade Cargo currently serves 25 destinations worldwide from its hubs in Shenzhen, Shanghai and Tianjin in China, with the emphasis on routes to Europe, India and the Middle East. BMI notes that this route will allow Jade to take advantage of both increasing intra-Asia route volumes and the traditional Asia-Europe route - the busiest air cargo route in Europe. BMI predicts Vietnam's airfreight volumes to grow quickly and steadily during our forecast period. Jade Cargo is not alone in recognising the potential of the Vietnam-Europe airfreight route. In 2009 Lufthansa Cargo, the airfreight subsidiary of Deutsche Lufthansa, launched a weekly direct service between Frankfurt and Hanoi, which it is considering doubling in the future to keep up with demand. Vietnam Airlines is planning to increase its flights between Hanoi and Paris, Hanoi and Moscow, and Hanoi and Frankfurt, from late-June 2011, which could potentially mean an increase in the amount of freight carried on the routes. Meanwhile, intra-Asia airfreight has also been attracting increasing investment, with Fedex opening a new office in Hanoi, and announcing a service running Tuesday to Friday between Hanoi and China. BMI notes the US logistics giant has been following a definite strategy of increasing its exposure to Asia. 'The new service enhancement is another testament to FedEx's efforts to provide time-definite and reliable services for customers in Vietnam, and to help them enhance their competitiveness across the Asia Pacific region', said David Cunningham, president of FedEx Asia Pacific. FedEx operates about 10 flights per week between Vietnam and the US, the EU, Japan, China and other Asian markets.

Maritime

Japan Funds Lach Hyuen PPP Port Project

Japan's Overseas Development Assistance (ODA) coordinator Japan International Cooperation Agency (JICA) is set to team up with Japanese companies to construct the JPY140bn (US$1.7bn) Lach Hyuen port project in northern Vietnam. BMI believes that this project highlights the importance of foreign investment in Vietnam's port infrastructure, due to its implications for the country's growth. In April 2012, JICA was due to sign an agreement to provide the bulk of the financing - JPY120bn - for the Lach Hyuen port project. The Japanese companies involved in the project include: trading conglomerate Itochu and shipping companies Nippon Yusen Kabushiki Kaisha (NYK) and Mitsui O.S.K. Lines (MOL), which will invest an additional JPY20bn in the project. The Japanese consortium will form a joint venture (JV) with Vietnamese port operator Vietnam National Shipping Lines . This project will be the first port project under a public private partnership (PPP) framework and construction is expected to begin in 2012. This investment by JICA highlights our growing confidence that Vietnam's port infrastructure will be able to meet the country's trade needs over the long term. The Lach Hyuen port is located just 100km east of Vietnam's capital Hanoi and is expected to eventually replace the nearby Hai Phong port, currently the largest port in the northern region of Vietnam. Hai Phong port is reaching capacity and does not have adequate infrastructure to handle some larger container ships and the Lach Hyuen port expansion will be implemented to address this deficit. The deepwater port will have four container wharves with a loading capacity of about 35mn tonnes a year and facilities capable of handling 100,000 deadweight tonne (DWT) ships.

Sustained Investment In Ports Vital To Vietnam's Growth

We believe that increasing investment in Vietnam's port infrastructure is crucial to Vietnam's economic growth. There are two major factors which are central to our view: Firstly, the export sector is vitally important to Vietnam's economy - we estimate that that it accounted for 76.6% of Vietnam's economy in 2010 - but Vietnam's port infrastructure is ranked just 97 out of 139 countries in a 2010/11 competitiveness report published by the World Economic Forum. Therefore, a continued lack of investment will create major bottlenecks at ports and constrain the country's export led-growth and investment. Secondly, Vietnam is becoming increasingly important, not just to growing Intra-Asian trade, but also on the global stage. An increasing number of shipping companies are choosing Vietnam as their port of call as they ply the East-West trade route. Meanwhile Vietnam's ports are gradually graduating from feeder stop-offs on the major routes to boasting direct services on both the Asia-US and Asia-Europe services. Vietnam's growing importance as part of the global container shipping sector is illustrated by the growth in box throughput at the nation's ports over the last decade. In 2009 (latest available data) total container throughput at the country's ports reached 5.4mn TEUs, up 487% from the 919,264TEUs handled in 1999. Year-on-year (y-o-y) container throughput growth averaged 20% over this period, with the country's ports sector still posting y-o-y volumes increases in 2009, despite the global downturn in trade. Should investment in port infrastructure fail to keep pace with these growing trade volumes, shipping companies might turn to other countries such as Malaysia to meet their infrastructure needs. We believe that the Vietnamese government does not have the fiscal strength to finance the level of investment needed to support its growing trade volumes, thus PPPs will be vitally important in attracting foreign investors to provide financing. At present, there are 23 proposed PPP projects relating to seaport development and services, with twelve of the proposed projects involving seaport construction.

Risk To Outlook

While it has been a long-standing trend for many of the overseas projects that involve Japanese companies to receive financing from the Japanese government, in this case, we are skeptical about the sizeable level of financing provided by the JICA. We have previously highlighted that the environmental disaster currently afflicting Japan could place pressure on the government to redirect funding allocated for international projects towards domestic reconstruction efforts. We have already seen this happening with some projects in Asia and we are concerned that this could happen to the Lach Hyuen port project should Japan's reconstruction bills reach astronomical levels. The transport sector continues to form the majority of infrastructure investment in Vietnam, accounting for 71% in 2015. Vietnam still suffers from a significant deficit in transportation infrastructure, and we see the Vietnamese government continuing to develop this sub-sector over the medium term. This is reflected in our forecast for the value of the transport infrastructure industry to grow by an average of 5.8% y-o-y between 2010 and 2015.

…While Japanese Shipping Lines Compete For Market Share

Major Japanese shipping companies were in February reported to be trying to enhance their market presence in Vietnam in order to capitalise on an increase in demand for shipments of daily necessities and auto parts, according to Nikkei Report. Mitsui OSK Lines (MOL) will deploy Europe-bound container vessels for the first time that will have a handling capacity of 6,500 20-foot equivalent units (TEUs). The vessels will call at a port near Ho Chi Minh City in southern Vietnam. The shipping company will operate 10 such vessels through Vietnam on a weekly basis. Meanwhile, Nippon Yusen KK (NYK) is to launch freight services between Southeast Asian countries in association with state-run Vietnam National Shipping Lines (Vinalines). Kawasaki Kisen Kaisha (K-Line) along with a Vietnamese logistics firm will establish a joint venture in Hanoi in order to operate an international freight forwarding business by sea and air. The venture is also considering establishing a branch in Ho Chi Minh City.

Market Overview

In January 2007 Vietnam officially joined the WTO, an event seen as an important milestone in the country's closer integration into the global economy. WTO membership has helped boost Vietnam's international trade and develop its freight transport capabilities.

Road transport is the most advanced in terms of freight sector privatisation and is the dominant mode for freight, with a market share of around 60% of domestic cargo. There are over 1,050 enterprises registered in the road transport business, which include 16 state-owned enterprises (SOEs), 233 limited liability companies, 350 private companies and 450 joint stock companies. Very few foreign-invested companies are present.

Most road transport companies are of small or medium size, and each company, on average, owns about 50 vehicles. In addition, tens of thousands of individual household businesses exist that operate informally in the road freight sector, and are thus difficult to account for and monitor.

Vietnam has a national road network of 222,179km. Of this, only 42,167km, or 19%, is paved. In addition, recent surveys indicate that approximately 40% of the network is in poor to very poor condition and will require substantial investment even to reach a maintainable condition. The quality of Vietnam's road infrastructure was judged by the World Economic Forum (WEF) to be poor and was ranked 102 out 133 nations surveyed in the WEF 2010 Global Competitiveness Report.

Vietnam's railway transport sector has only one operator, the **Vietnam Railway Corporation** (VRC), established in April 2003 as a state corporation operating railway transport and related services. The government has announced plans to separate the management of rail infrastructure from passenger and cargo services. Vietnam's rail network totals 2,600km (excluding sidings). The network is mixed-gauge, comprising 2,169km of 1.000m gauge and 178km of 1.435m gauge. The network has 1,790 bridges totalling 45km and 11.5km of tunnels. The principal axis is Hanoi-Ho Chi Minh City (1,726km). Other lines emanating from Hanoi are to Hai Phong (102km), Lao Cai (296km) and Dong Dang (162km). Railway infrastructure in Vietnam was ranked 58 out of 114 by the WEF.

There are two principal airlines operating in Vietnam: **Vietnam Airlines** and **Pacific Airlines**. Both are majority state owned, although Australia's **Qantas** is now a minority shareholder in Pacific Airlines. The government has announced plans to build the country's largest airport at Long Thanh in the southern province of Dong Nai, at an estimated cost of US$8bn. The authorities also plan to expand Noi Bai International airport in Hanoi. The three major airports handling freight are located at Ho Chi Minh City, Hanoi and Da Nang, each of which have international connecting flights. Minor airports such as Cat Bi at Haiphong are generally used for domestic flights to the three larger hubs. In 2010, Vietnam's air transport infrastructure was ranked 84/ 133 nations by the WEF.

Vietnam's dense river and canal network provides the country with a highly developed inland waterway system. This is the second-largest sub-sector involved in domestic cargo transport, accounting for 25-30% of total transport volumes. The inland waterway transport sub-sector is managed by two state corporations affiliated to the Ministry of Transport, one SOE affiliated to the Vietnam Inland Waterway Authority, and some enterprises managed by other ministries, operating in support of the power generation, cement and paper industries. In addition, there are about 230 co-operatives and hundreds of inland waterway transport enterprises in the country.

Vietnam's seaport network comprises of many small- and medium-sized entities, with inefficient distribution. Most big ports are located far inside rivers, like Hai Phong and Ho Chi Minh City, with limited depth at the entrance. Some ports are located in big cities, thus making it difficult to connect with other modes of transport for cargo transfer to and from ports, due to traffic congestion. Except for several new or upgraded ports, most have been operating for many years and lack investment and are seriously degraded.

The loading and unloading equipment in some ports is obsolete, leading to low productivity. The average productivity of a Vietnamese port is only 2,500 tonnes/m per wharf, or 40-50% of productivity of other ports in the region.

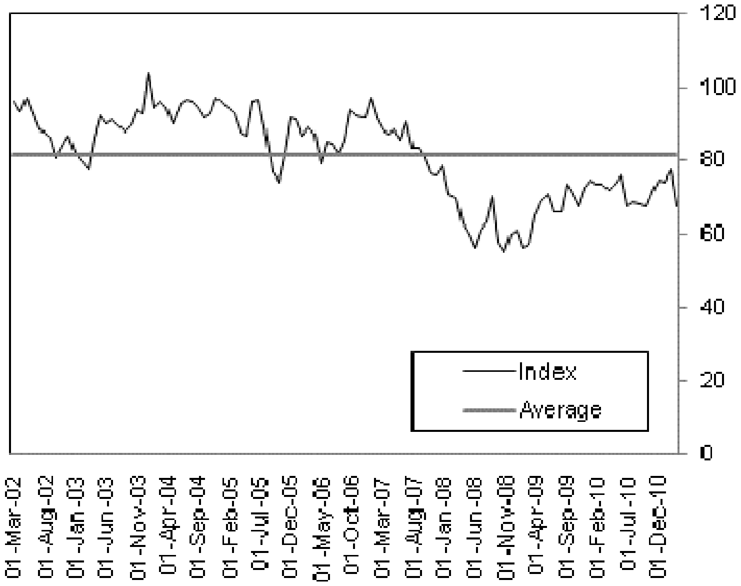
Vietnam's port infrastructure is poor by international standards. The World Economic Forum's 2010 Global Competitiveness Report gives it a score of 3.56, putting it just ahead of the regional underperformer, the Philippines, which scores 2.92, and well behind regional leaders Singapore and Hong Kong. Increasing international interest in Vietnam's port sector on the back of growing intra-Asia trade should help to close the gaps in infrastructure investment.

Container Shipping Overview

Lines have posted positive 2010 results and the global economy is recovering, so why is **BMI** still fearful about what the future holds for the container shipping sector? Overcapacity is still not under control, rate declines appear to be worsening and further capacity is due online throughout 2011, which will only exacerbate the situation.

High Gasoline Prices Knock Confidence

University Of Michigan And Thomson Reuters US Consumer Confidence Index



Source: Bloomberg

Improving rates were behind the recovery in container lines' results in 2010. As such, the failure so far in 2011 to increase rates is a bad omen. Volumes, while ticking up, are in most cases still not back to 2008 levels, which is clearly another cause for concern. **BMI** has examined these issues and below we highlight our key views for what this quarter holds for the box shipping sector.

Drivers

Key Views

- US economic growth strengthening in 2011.
- MENA unrest offers downside, with high gasoline prices hitting consumer confidence.
- Positive economic outlook for France and Germany to feed down to increased consumer demand.

The major container shipping demand economies of the US and Europe are looking stronger, with **BMI**'s country risk desk revising up real GDP forecasts across the board for 2011.

US Encourages Consumer Spending

Solid foundations have been laid for economic growth in the US in 2011 with the extension of existing income tax regime and unemployment benefits, along with the cutting of payroll taxes by two percentage points (pp) in a bill approved by Congress on December 16 2010. Following the bill's passage into the statute book **BMI**'s country risk analysts raised our US real GDP growth projections from 2.0% to 3.1% for 2011, and although we do flag slight downside risks to this forecast owing to high energy prices resulting from MENA unrest, the additional income in US consumers' pockets that will result from the extension of unemployment benefits and tax cuts is the major driver of our positive growth outlook for the US economy.

This outlook played out well in February 2011, with retail sales posting their largest gains in four months. However, consumer confidence took a hit in March 2011, with high gasoline prices knocking confidence.

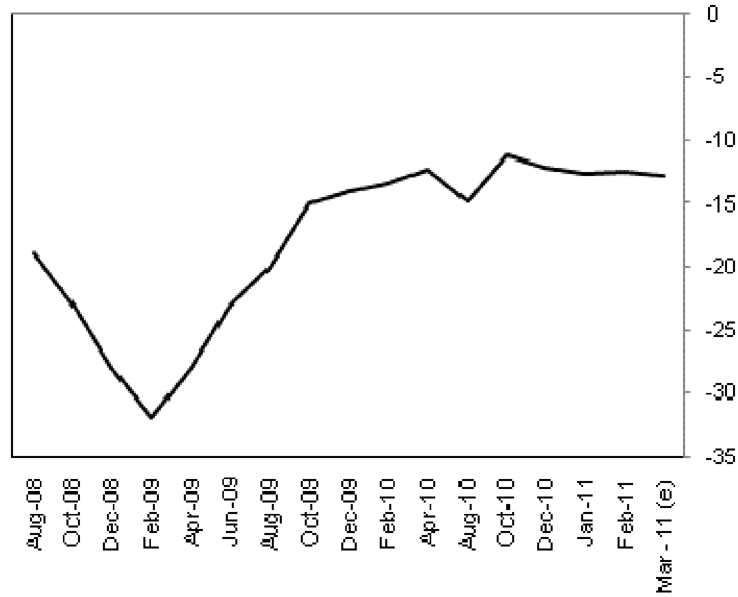
The Thomson Reuters and University of Michigan's consumer sentiment index fell to 68.2 in March, its lowest level since October 2010. Another indicator of US consumer confidence, the Bloomberg Consumer Comfort Index fell to -48.9 on March 20 2011 (last available data) from -48.5 in the previous week, its lowest level since August 2010.

Steady Growth At US Bellwether Ports

The steady recovery in US consumer demand is reflected in throughput volumes for the port of Los Angeles, where year-on-year (y-o-y) box volume growth continues. In January and February (the latest data for 2011 is for January and February, so we will use these months from the previous years for comparative purposes) of 2011 the port of Los Angeles handled 644,282 20-foot equivalent units (TEUs), a y-o-y increase of 12%. 2011 volumes are, however, still 4% below the 671,120TEUs handled in the first two months of 2008, demonstrating that a full recovery has not yet been achieved. We note that the difference in volumes y-o-y is decreasing, though, with the difference between the first two months of 2011 compared to that of 2008 standing at 4%, while in 2009 and 2010 the disparity between 2008 figures was -21% and -14% respectively, showing that the recovery is on the right track.

Plateauing

European Consumer Sentiment, August 2008-March 2010



e = estimate. Source: European Commission's Business and Consumer Survey

Europe Strengthening

In Europe the decline in consumer confidence appears to be plateauing, with the Flash Consumer Confidence Index standing at an average of 12.6% in the first three months of 2011.

Consumer confidence in Europe appears to be strengthening largely on the back of a positive economic outlook for Germany and France, which are currently leading the way in terms of eurozone growth. Real GDP growth in Germany is expected to dip slightly y-o-y in 2011 to a projected 3% following an increase of 3.6% in 2010. Household spending in the country has been pushed up by record low unemployment and higher gross spending.

In France the economy is strengthening, with real GDP set to increase by 1.7% y-o-y following 1.5% growth in 2010. Private consumption has been highlighted by **BMI** as the driver of this growth, but we do note that household spending growth is unlikely to return to pre-downturn levels over the mid term.

European bellwether ports have yet to publish data for 2011.

Bellwethers

Key Views

- Mainland Chinese ports to increase their role in the global box shipping sector to the detriment of traditional Asian transhipment hubs.
- Asia-Europe volumes back to 2008 levels and due to continue strenghtening.
- Trans-Pacific volumes growing, but still not back to 2008 levels.

2010 Container Recovery Lays Foundations For 2011 Growth

According to **BMI** forecasts 2011 is set to be another year of growth at the top five global container ports of Shanghai, Singapore, Hong Kong, Shenzhen and Busan. Our growth projections for the year project a slowdown in year-on-year (y-o-y) growth compared with 2010, which is in line with our forecasts for the global economy. This is hardly surprising considering that 2010 was the rebound year, meaning that growth was from an exceptionally low base. In 2010 the y-o-y growth average of the top five global container ports stood at 15.96%; in 2011 **BMI** predicts average growth at these facilities of 8.44%.

The rise in 2010 throughput after the disastrous 2009 offers a solid foundation for further growth in 2011. The two Chinese ports that feature in the top five, Shanghai and Shenzhen, have both recovered to their pre-downturn box throughput levels, with the ports handling 29mn TEUs and 22.5mn TEUs respectively in 2010 compared with the 28mn TEUs at the port of Shanghai and 24.49mn TEUs at the port of Shenzhen in 2008.

Fifth-placed port of Busan also managed to recover to its pre-downturn level, handling 14.18mn TEUs in 2010 compared with 13.4mn TEUs in 2008.

Asia's two main transhipment hubs, Singapore and Hong Kong, while posting respectable y-o-y growth of 9.8% and 12.10% respectively in 2010, were still off their 2008 levels, Singapore by 5% and Hong Kong by 3.9%.

Shanghai On Top And Shenzhen Gaining On Hong Kong

2010 also marked a shift in dynamics that is set to continue in 2011 and over the mid term. In 2010 the port of Singapore lost its first-place status to the port of Shanghai, with the Singaporean port trailing the Chinese port by 2.1% in terms of total containers handled. The other ports remained in their places: Hong Kong ranked third, the port of Shenzhen fourth and Busan took fifth place. How long these ports will remain in these places, however, is open to debate, with Shenzhen gaining on Hong Kong. In 2009 a throughput difference of 2.7mn TEUs existed between the two ports, in 2010 this had shrunk to 1.03mn TEUs.

Shanghai On Top

Top Five Global Container Ports

Global Rank	Container Port	2010 Container Throughput (TEU)	2010 Container Throughput y-o-y % Change
1	Port of Shanghai	29,050,000.00	16.20
2	Port of Singapore	28,400,000.00	9.80
3	Port of Hong Kong	23,530,000.00	12.10
4	Port of Shenzhen	22,500,000.00	23.30
5	Port of Busan	14,180,000.00	18.40

Source: Port authorities, BMI

BMI believes that the reason for the rise of Chinese ports is twofold. First, China's need for external transhipment hubs is falling, with Chinese goods now shipped from smaller ports to one of the larger domestic facilities, from where goods are shipped to the US or Europe. Lines have noted this change and more and more are offering direct services linking Chinese ports with the US and Europe. The second reason for the rise of Chinese ports over the traditional Asian transhipment hubs is China's growing demand for imported goods, a trend we expect to continue over the mid term as Chinese consumer demand develops.

Shanghai Continues Its Lead In 2011, Gap With Singapore Widens

The port trends identified above have continued in 2011, and this is reflected in January and February 2011 box throughput results for the ports of Shanghai, Singapore, Hong Kong and Shenzhen. The port of Shanghai retains its number-one position with throughput of 4.6mn TEUs in the first two months of 2011. The port of Singapore handled 4.56mn TEUs in January and February.

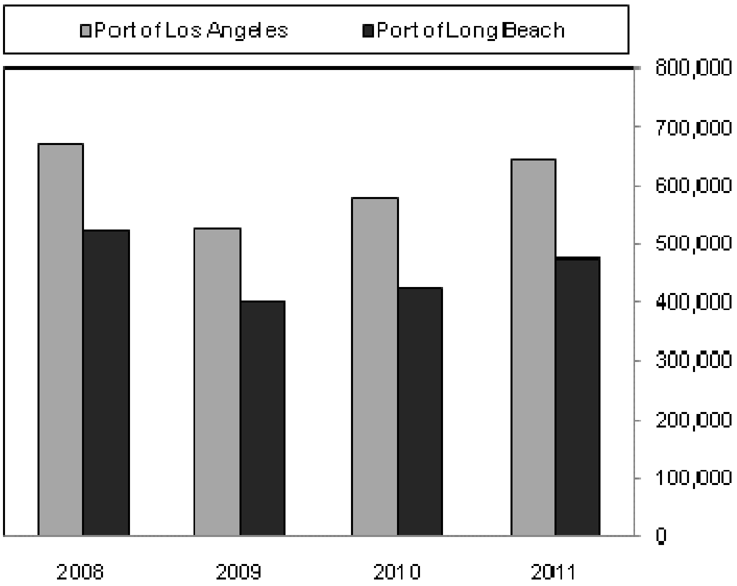
The ports of Shanghai, Shenzhen and Hong Kong posted y-o-y increases of 13%, 3% and 2% respectively in the first two months of 2011, while the port of Singapore's throughput declined by 11%. **BMI** believes that despite this decline at the world's second-largest container port global growth in box volumes will continue in 2011.

Transpacific Volumes Continue To Grow, But Still Off 2008 Levels

Container volumes on transpacific routes appear to be edging up. Inbound container volumes at the ports of Los Angeles and Long Beach (the US west coast box bellwether ports) have risen y-o-y in the first two months of the year, with both facilities seeing y-o-y growth of 12%. Both ports, while recovering, have yet to reclaim pre-downturn levels, with Los Angeles handling 25,838 fewer TEUs in January and February of 2011 than in 2008 and Long Beach trailing its 2008 two-month throughput figure by 48,669TEUs.

Recovering But Not Back To 2008 Levels

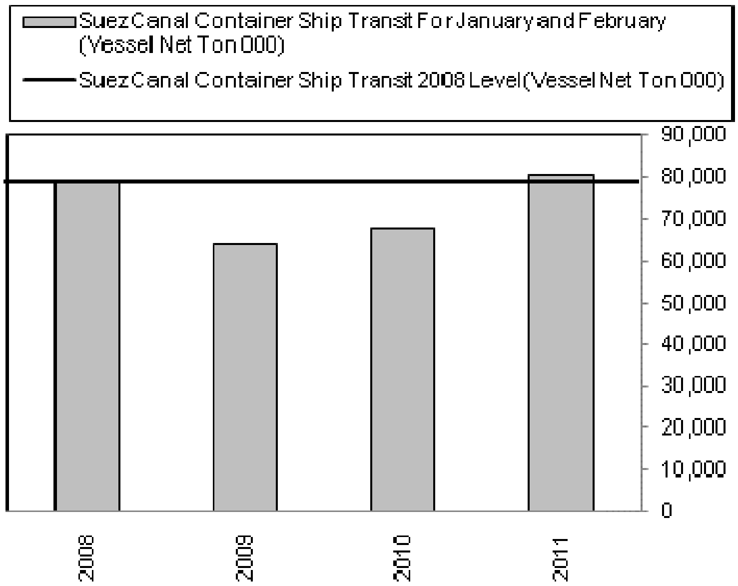
Container Throughput At Ports Of Los Angeles And Long Beach, January And February 2008-2011 (TEU)



Source: Port authorities

Back To Pre-Downturn Levels

Suez Canal Container Ship Transits, January And February 2008-2011 (vessel net '000 tonnes)



Source: Suez Canal Authority

Asia-Europe Back To Pre-Downturn Levels With Larger Vessels In Play

The volume of shipping tonnage passing through the Suez Canal (the main route for the Asia-Europe box ship trade) has increased y-o-y by 18.9%, not only a recovery to the pre-downturn level but an improvement upon it. In January and February 2011 80.4mn net tons of container vessels sailed through the canal compared with 78.7mn net tons in the first two month of 2008.

From this data it would appear that volumes on the Asia-Europe route have fully recovered. Another interesting trend from the Suez Canal data series is that although the net tonnage of box vessels increased in January and February 2011 compared with the first two months of 2008, the actual number of box ships passing through the canal fell. In the first two months of 2008 some 1,368 container vessels sailed through the canal, down to 1,149 vessels in the first two months of 2011, highlighting a trend in the container sector for ultra-large container vessels. Ships of 14,000TEUs and over have over the past three years come online, and are being used on the Asia-Europe trade route, leading to an increase in vessel size, but not an increase in the number of vessels.

Rates

Key Views

- Planned rate increases unlikely to hold with more capacity due online.
- Idling expected to increase in order to bring overcapacity under control.
- Slow-steaming to continue.

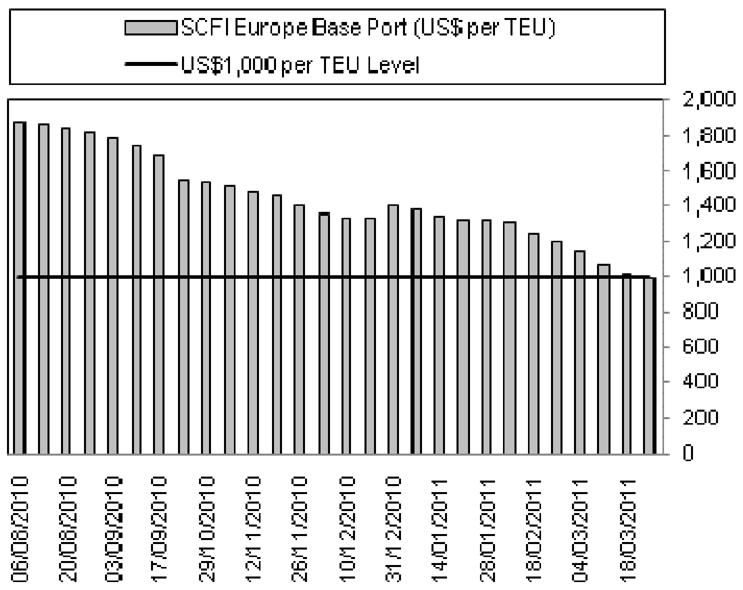
Overcapacity Continues

Although container volumes are continuing to recover many lines are starting to fear for their bottom lines once more, as despite the uptick in volumes rates continue to plummet.

Asia-Europe is one of the worst-hit routes, with rates falling below US$1,000 per 20-foot equivalent unit (TEU) for the week ending March 28 2011 (most recent data at the time of writing). This is the first time in 20 months that rates on the route have dipped below US$1,000. The last time rates fell below

Dipping Below 1,000

SCFI Europe (base port index), August 2010-March 2011 (US$ per TEU)

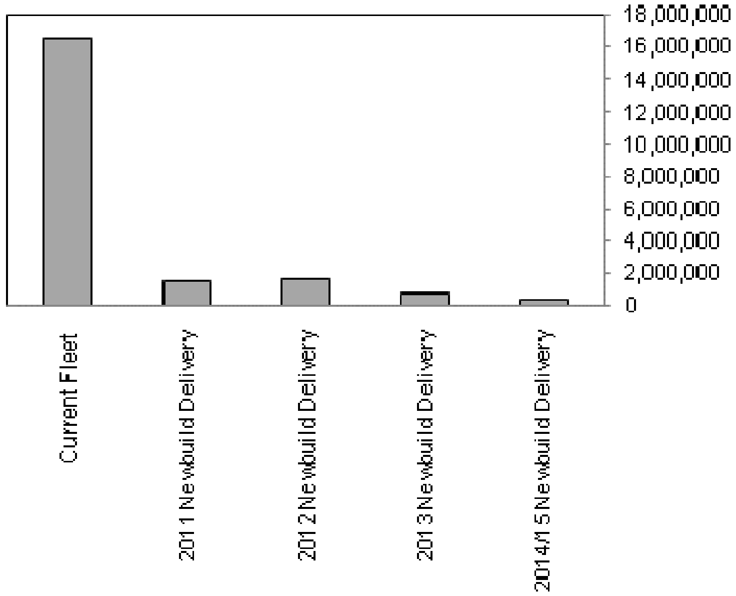


Europe Base Port= Hamburg/Antwerp/Felixstowe/Le Havre. Source: SCFI this level was in March 2009 in the midst of the downturn, when a price war broke out between lines. This time round the decline is due to overcapacity in the market and the inability of lines to force through rate increases.

BMI notes that rates on the route have been declining steadily for the past few months. Since August 2010 rates on the Asia-Europe trade route have declined by an average of 2% per week. Rates have also been declining and the transpacific, with the Shanghai Containerised Freight Index on this route dipping to US$1,608 per 40-foot equivalent unit (FEU) for the week ending March 28 2011. The average decline of over the past seven months has been 2% week-on-week (w-o-w).

Adding To Overcapacity

Newbuild Delivery Schedule (TEU)



Source: Lloyd's List Intelligence

The issue of overcapacity is unlikely to iron itself out in the next 12 months, as a further 1.4mn TEUs of capacity are due online in 2011 on top of the 115.5mn TEUs currently active in the box shipping sector.

Get Hiking

The most obvious tactic for lines to combat the decline, increasing shipping rates, was attempted in January 2011 and failed. Another slew of rate increases on the Asia-Europe trade route was set for April 2011

The chances of an industry-wide rate increase succeeding, however, are already being questioned. **BMI** asserts that little has changed since the beginning of the year when the last slew of rate increases failed to hold and so fears they won't be able to be pushed through in April 2011. Line may therefore have to wait until the peak season in July, but once again we note lines failed to push through the traditional peak season surcharges last year due to overcapacity in the sector.

The increase in transpacific rates is due in May 2011, with TSA members mulling increases of between US$200 and US$400 per TEU. The rate increases will be part of spring contract negotiations, and lines will no doubt be hoping that a concerted effort by TSA members will ensure the rises stick.

Slow-Steaming, Lay-Up Or Quit

If rate rises do not work and lines are forced to turn to other means to manage capacity, **BMI** believes that slow-steaming will be employed along with the idling of vessels. In the worst case we believe lines may start trying to decrease their exposure, but this is very much a last-ditch strategy as it will lose clients, and lines may struggle to win them back if they decide to re-launch services in the future.

It should be noted that one line has already chosen this strategy. In March 2011 Chile's **Compania Suramericana de Vapores** (CSAV) dropped its one Asia-US East Coast (USEC) link. CSAV's decision to abandon the route is, in **BMI**'s view, down to overcapacity on the route, which is driving rates down and therefore making it unprofitable, rather than any reflection on demand for containers to USEC ports. **BMI** notes that rates on the Asia-USEC route have indeed been falling. According to the Shanghai Containerised Freight Index (SCFI) rates on the route over the past seven months have averaged a w-o-w decline of 1%. For the week ending March 25 2011 (last data update) the average cost of shipping an FEU from Shanghai to USEC base port (New York, Savannah, Norfolk, Charleston) stood at US$2,819.

Although CSAV's peers also have to operate within these unfavourable conditions, we doubt that a trend for dropping this service will emerge. We believe that CSAV's decision to leave this trade route, rather than weather it out until the environment improves, is a result of the company's uncertain financial outlook. The company's new chairman has warned of negative results for the first quarter of 2011, with Que Pasa reporting earlier in March that losses of US$50mn had already been incurred by CSAV since the start of 2011.

Players

Key Views

- Lines facing a return to the red if rate drop isn't reversed.
- Market wide expansion into intra-Asia routes is set to continue.

Lines Back In The Black, But For How Long?

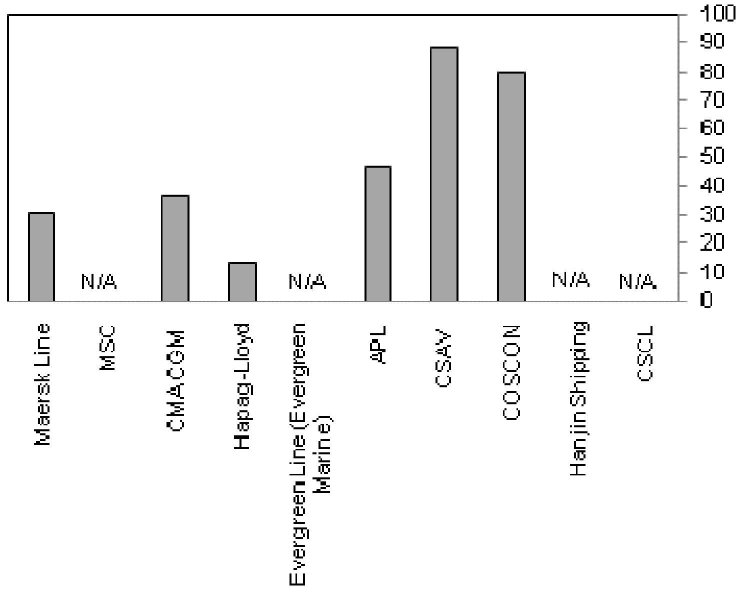
Chilean shipping company Compañía Sud Americana de Vapores (CSAV) is not the only line that will have concerns about its bottom line amid falling box rates. The extent to which shipping lines are reliant on periods of higher rates to ensure profit was highlighted in 2010, when massive year-on-year (y-o-y) increases in rates, rather than the y-o-y uptick in volumes, led many lines to return to profit.

A look at two major box operators illustrates this dynamic. In 2010 **Maersk Line**'s rates increased by 29% y-o-y, while volumes grew by just 5% y-o-y; the story was similar at **Hapag-Lloyd**, where rates increased by 24.8% but volumes rose by just 6.7%. Overall the companies' revenues increased by 30.65% and 87.9% respectively in 2010. This reliance on rate increases, rather than volume growth to drive up revenues is obviously a worry for companies in 2011, as rates are tracking lower and volumes have remained static. This combination leads **BMI** to question what companies will have to do to protect their bottom lines if rates cannot be pushed higher and volumes remain static.

The one bright spot on **BMI**'s medium-term view for container carriers is the intra-Asia trade route. Using Maersk Line's 2010 results to once again highlight our argument, we note that the route saw the largest y-o-y volume increase in 2010 of all the routes operated by Maersk, recording 37% growth. Unlike on the traditional big-money routes, growth on this route was driven by volumes, as rates on the trade route increased by just 19%.

Recovery

Key Players' Revenue – % Change Between 2009 And 2010



na = not available. Source: BMI

*For further container line information, including company strategy outlooks and financials please see **BMI** Shipping's company profiles.*

Industry Forecast

Macroeconomic

Slightly Slower Growth In 2011

Economic growth will continue support the Vietnamese freight transport sector this year. However, it is clear that the government, concerned over rising inflation and the size of the trade deficit, is applying the economic policy brakes, by cutting public spending and tightening interest rates. Investment in public projects is being cut back by VND50trn (US$2.4bn), while the State Bank of Vietnam (SBV) tightened interest rates in February and again in April. Some of this domestic tightening may be offset by greater exports - encouraged by a currency devaluation in February - but we believe the net effect is deflationary on the short term. BMI also believes that tackling inflation now is a positive move for the country's medium term economic future: in other words, that the current correction is necessary. As a result of our analysis, BMI now forecasts 2011 GDP growth of 6.3% (down from 6.8% in 2010). Our outlook for 2012 is for growth to accelerate again to 7.2%. In the five years to 2015 we expect growth to average 7.0% per annum, confirming Vietnam as one of the faster-growing economies in Southeast Asia.

Road Freight

High Single Digit Growth

Since our last report we have maintained our forecast for road haulage. In 2011 we now see a growth rate of 6.9% to 36.84bn tonnes per kilometre (bntkm). Thereafter road freight growth will continue expanding vigorously, averaging 7.4% per annum in the five years to 2015. This rate will exceed the average for GDP growth, a pattern consistent with this stage of Vietnam's industrialisation process.

Table: Road Freight, 2008-2015

	2008	2009	2010	2011f	2012f	2013f	2014f	2015f
'000 tonnes	455,898.40	494,649.80	563,406.12	599,863.21	641,689.03	688,531.87	738,564.31	789,140.46
– % change y-o-y	13.02	8.50	13.90	6.47	6.97	7.30	7.27	6.85
mn tonnes/ km	27,968.00	30,261.40	34,467.73	36,840.47	39,562.62	42,611.29	45,867.56	49,182.10
– % change y-o-y	13.47	8.20	13.90	6.88	7.39	7.71	7.64	7.23

f = BMI forecast. Source: General Statistics Office of Vietnam

Rail Freight

Waiting For New Investment

Rail freight carried is set to experience a slowdown in 2011, with growth of 4.7% to 3.893bntkms. Average annual growth over the next five years will be 5.2%, below overall economic growth. This suggests that Vietnam's poor track infrastructure and signalling system is limiting the potential for this freight transport mode. In volume terms freight carried by rail will recover by 4.8% in 2011 to 8.187mn tonnes. Chinese-backed rail investment projects for Vietnam present upside risks to our forecasts.

Table: Rail Freight, 2008-2015

	2008	2009	2010	2011f	2012f	2013f	2014f	2015f
Rail freight, '000 tonnes	8,481.10	8,068.10	7,809.92	8,187.28	8,620.20	9,105.06	9,622.93	10,199.06
– % change y-o-y	-6.29	-4.87	-3.20	4.83	5.29	5.62	5.69	5.99
Rail freight, mn tonnes/km	4,170.90	3,805.10	3,717.58	3,893.05	4,094.36	4,319.82	4,560.63	4,799.43
– % change y-o-y	7.43	-8.77	-2.30	4.72	5.17	5.51	5.57	5.24

f = BMI forecast. Source: General Statistics Office of Vietnam

Air Freight

Growing At 5%+

In terms of air cargo volume, **BMI** sees growth of 5.3% to 147,910 tonnes in 2011, compared with growth of 2.1% in 2010. In the medium term, the 2011-2015 forecast period, tonnage growth will average 5.9%, just below the country's general rate of economic expansion. In terms of freight carried (volume x distance) we expect to see growth of 4.9% in 2011 to 327.73mntkms, a recovery from 2010's contraction of 1.3%.

Table: Air Freight, 2008-2015

	2008	2009	2010e	2011f	2012f	2013f	2014f	2015f
Air freight, '000 tonnes	131.40	137.60	140.54	147.91	156.38	165.85	175.98	187.56
– % change y-o-y	1.39	4.72	2.13	5.25	5.72	6.06	6.10	6.58
Air freight, mn tonnes/km	295.60	316.60	312.48	327.73	345.23	364.83	385.76	408.23
– % change y-o-y	5.61	7.10	-1.30	4.88	5.34	5.68	5.74	5.82

e/f = BMI estimate/forecast. Source: General Statistics Office of Vietnam

Maritime And Inland Waterways

Saigon New Port To See Strong Volume Growth

BMI maintains our projection of strong growth in 2011 volume handled at the Port of Ho Chi Minh City (also known as SNP, Saigon New Port), up by 7.45% to 21.84mn tonnes, after the 6.22% rate estimated in 2010. We believe medium term growth will be vigorous, with the annual average over the 2010-2015 period coming out at 8.0%, one percentage point above the general growth rate of the Vietnamese economy. At Da Nang Port (DNP) we see 2011's volume increasing by 2.8% to 3.29mn tonnes. Average growth of volume at DNP across the forecast period will however, be 3.4%, below the general GDP growth rate (this reflects capacity limitations at this port). .

SNP is expected to see 4.4% container handling growth to 2.89mn 20-foot equivalent units (TEUs) in 2011, following an estimated growth of 13.89% in 2010. The DNP will see growth of 7.09% to 79,252 TEUs. SNP will experience medium-term (2011-2015) average annual box handling growth of 5.6%; while for DNP the figure will be a somewhat higher at 7.9%.

Table: Maritime Freight – Throughput, 2008-2015 (‘000 tonnes)

	2008	2009	2010e	2011f	2012f	2013f	2014f	2015f
Port of Ho Chi Minh City (Saigon New)	20,180.00	19,140.00	20,329.57	21,843.71	23,581.42	25,564.47	27,691.79	29,920.83
– % change y-o-y	-21.17	-5.15	6.22	7.45	7.96	8.41	8.32	8.05
Port of Da Nang	2742.26	3132.00	3204.35	3292.86	3394.43	3510.34	3634.68	3778.43
– % change y-o-y	0.19	14.21	2.31	2.76	3.08	3.41	3.54	3.95

e/f = BMI estimate/forecast. Source: Port authorities

Table: Inland Waterway Freight, 2008-2015

	2008	2009	2010	2011f	2012f	2013f	2014f	2015f
‘000 tonnes	133,028.00	135,688.40	142,201.44	148,378.09	155,960.44	164,659.38	174,401.76	184,807.51
– % change y-o-y	-1.67	2.00	4.80	4.34	5.11	5.58	5.92	5.97
Mn tonnes km	24,869.00	25,365.20	25,593.49	26,752.09	28,084.60	29,568.40	31,159.70	32,622.02
– % change y-o-y	11.84	2.00	0.90	4.53	4.98	5.28	5.38	4.69

f = BMI forecast. Source: General Statistics Office of Vietnam

Trade Overview

Forecast Remains At 11.3% Growth In Real Terms

In real terms Vietnam's total trade (imports + exports) will grow by 11.3% in 2011. Over our forecast period, up to 2015, exports will grow at an average per annum rate of 8.6%, ahead of imports at 7.5%. In real terms we expect imports to grow by 11.6% and exports to grow by 11% in 2011. In nominal terms, in 2011, imports will gain 20.8% to US$105.8bn, while exports will grow 20.2% to US$93.8bn.

Vietnam's principal export commodities are crude oil and manufactured goods. The country's main imports are machinery and equipment. Vietnam's main export partners are the US, Japan, Australia, China and Germany. The country's main sources for imports are China, Singapore, Japan, South Korea and Thailand. Vietnam's geographic position on the South China Sea allows the country access to the main transpacific and intra-Asian shipping routes, enabling the country to meet its trading needs.

Table: Trade Overview, 2008-2015

Real	**2008**	**2009e**	**2010e**	**2011f**	**2012f**	**2013f**	**2014f**	**2015f**
Imports, real growth, % y-o-y	11.92	-13.81	17.90	11.60	6.50	6.50	6.50	6.50
Exports, real growth, % y-o-y	10.85	-15.00	21.00	11.00	8.00	8.00	8.00	8.00
Total trade, real growth, % y-o-y	11.38	-14.40	19.45	11.30	7.25	7.25	7.25	7.25
Nominal								
Imports, US$bn	83.60	73.00	87.57	105.80	119.99	138.98	160.32	184.19
- % change y-o-y	26.71	-12.68	19.97	20.81	13.42	15.82	15.35	14.89
Exports, US$bn	69.95	63.39	78.05	93.78	107.87	126.69	148.20	172.67
- % change y-o-y	27.88	-9.38	23.12	20.16	15.01	17.45	16.98	16.51
Total trade, US$bn	153.55	136.39	165.62	199.58	227.86	265.67	308.52	356.85
- % change y-o-y	27.24	-11.18	21.43	20.51	14.17	16.59	16.13	15.67

e/f = BMI estimate/forecast. Source: General Statistics Office of Vietnam, BMI

Table: Key Trade Indicators, 2008-2015 (US$mn and % change y-o-y)

	2008	2009e	2010e	2011f	2012f	2013f	2014f	2015f
Agricultural raw materials								
Imports	2,415.93	2,215.20	2,720.81	3,263.67	3,749.39	4,398.80	5,140.79	5,984.65
– % change	24.45	-8.31	22.82	19.95	14.88	17.32	16.87	16.42
Exports	2,416.63	2,099.17	2,563.83	3,144.87	3,597.38	4,202.61	4,882.84	5,643.75
– % change	30.15	-13.14	22.14	22.66	14.39	16.82	16.19	15.58
Ores and metals								
Exports	553.33	437.13	546.13	663.16	767.87	907.88	1,067.84	1,249.76
– % change	47.72	-21.00	24.94	21.43	15.79	18.23	17.62	17.04
Imports	2,824.71	2,649.93	3,247.65	3,995.07	4,577.15	5,355.69	6,230.71	7,209.50
– % change	6.42	-6.19	22.56	23.01	14.57	17.01	16.34	15.71
Iron and steel								
Exports	411.02	442.56	558.23	682.43	793.55	942.13	1,111.88	1,304.95
– % change	-20.82	7.67	26.14	22.25	16.28	18.72	18.02	17.36
Imports	4,946.04	5,304.42	6,418.02	7,810.54	8,895.01	10,345.49	11,975.73	13,799.32
– % change	-14.85	7.25	20.99	21.70	13.88	16.31	15.76	15.23
Manufactured goods								
Exports	32,534.78	28,748.03	35,341.47	42,420.77	48,754.91	57,223.68	66,899.77	77,904.34
– % change	23.16	-11.64	22.94	20.03	14.93	17.37	16.91	16.45
Imports	54,527.27	47,929.54	57,491.36	69,448.13	78,759.83	91,214.30	105,212.22	120,870.30
– % change	24.31	-12.10	19.95	20.80	13.41	15.81	15.35	14.88
Fuel								
Exports	14,833.69	12,788.78	15,696.53	18,818.55	21,611.94	25,346.72	29,613.94	34,467.03
– % change	47.44	-13.79	22.74	19.89	14.84	17.28	16.84	16.39
Imports	13,811.07	11,047.46	13,527.95	16,629.74	19,045.35	22,276.25	25,907.55	29,969.52
– % change	57.95	-20.01	22.45	22.93	14.53	16.96	16.30	15.68

e/f = estimate/forecast. Source: BMI

Table: Vietnam's Main Import Partners, 2002-2009 (US$mn)

	2002	2003	2004	2005	2006	2007	2008	2009
Mainland China	2,158.84	3,138.55	4,595.10	5,899.70	7,391.30	12,710.00	15,652.10	16,441.00
Japan	2,504.65	2,982.06	3,552.60	4,074.10	4,702.10	6,188.90	na	7,468.09
South Korea	2,279.60	2,625.44	3,359.40	3,594.10	3,908.40	5,340.40	7,066.30	6,976.36
Thailand	955.24	1,282.19	1,858.60	2,374.10	3,034.40	3,744.20	4,905.60	4,514.07
Singapore	2,533.49	2,875.82	3,618.40	4,482.30	6,273.90	7,613.70	9,392.50	4,248.36

na = not available/applicable. Source: IMF's Direction of Trade Statistics

Table: Vietnam's Main Export Partners, 2002-2009 (US$mn)

	2002	2003	2004	2005	2006	2007	2008	2009
United States	2,453.15	3,939.56	5,024.80	5,924.00	7,845.10	10,104.50	11,868.50	11,355.80
Japan	2,436.96	2,908.60	3,542.10	4,340.30	5,240.10	6,090.00	8,537.90	6,291.81
Mainland China	1,518.33	1,883.12	2,899.10	3,228.10	3,242.80	3,646.10	4,535.70	4,909.03
Switzerland	66.67	74.67	120.20	103.90	155.70	236.90	516.90	2,486.49
Australia	1,328.33	1,420.86	1,884.70	2,722.80	3,744.70	3,802.20	4,225.20	2,276.72

Source: IMF's Direction of Trade Statistics

Political Outlook

Domestic Politics

National Congress Unlikely To See Shift In Expansionary Focus

We reiterate our view that Vietnam's 11th National Congress is unlikely to result in a major shift in the country's policy direction over the next five years. Prime Minister Nguyen Tan Dung is set to retain his post for another term, and this suggests that the CPV's stance on economic reforms will continue over the coming years. Vietnam's socio-economic targets for 2011 indicate an increased focus towards achieving macroeconomic stability and controlling inflation. Nonetheless, the National Assembly's real GDP growth target of 7.5% in 2011 remains overly ambitious in light of overheating pressures in the economy.

Vietnam's 11th National Congress, which is scheduled to conclude on January 19, will decide on the new leadership of the Communist Party of Vietnam (CPV) over the next five years. Key political figures including State President Nguyen Minh Triet and Party General Secretary Nong Duc Manh will retire due to the age ceiling of 65 for members seeking re-election. There has been no indication by the government as to who are the most likely candidates to assume the leadership of the CPV. However, it is widely expected that National Assembly Chairman Nguyen Phu Trong will replace Nong Duc Manh as Party General Secretary. This suggests that Prime Minister Nguyen Tan Dung is set to retain his post for another term. Having survived a no-confidence vote in November - due to criticism of the handling of the near bankrupt state-owned shipbuilding company Vinashin - we see this as an indication that PM Nguyen Tan Dung's popularity and his influence within the National Assembly remain strong. As such, PM Nguyen Tan Dung's stance on economic reforms is expected to continue over the coming years. The National Congress will also approve draft documents on national development and Vietnam's political framework, which are expected to reaffirm the socialist orientation of the country.

No Change To Policy Direction

We have previously highlighted our view that the direction of Vietnam's economic policies would remain largely unchanged in spite of a reshuffle of key political figures within the politburo. We argued that the CPV's economic policies would continue to centre on opening the economy to foreign competition, addressing corruption, promoting trade and upgrading the country's infrastructure and technology. The theme of the National Congress also remains dedicated towards continuing the ‘Doi Moi’ (renovation) process of market-oriented reforms, as the congress reiterates its commitment to become a fully industrialised economy by 2020. Despite the socialist rhetoric that we expect to come out of this congress, Vietnam will continue to move in the direction of a market-based economy. We regard this as a positive development that will provide support for our bullish long-term economic outlook for Vietnam.

Calling For A Balance To Growth

The National Assembly is targeting real GDP growth of 7.5% for 2011, which in our opinion remains overly ambitious in light of overheating pressures in the economy. Vietnam continues to struggle with mounting inflationary pressures, persistent trade deficits and deteriorating confidence in the domestic currency. We see these short-term macroeconomic problems as key challenges for the government in 2011. Given that the government is set to pursue economic growth at the expense of higher inflation and larger trade and fiscal deficits, we believe that this would eventually backfire on the economy's growth. As such, we are maintaining a relatively subdued real GDP growth forecast of 6.3% in 2011. Highlighting our concerns that the government remains too narrowly focused on economic growth, Minister of Planning and Investment Vo Hong Phuc warned during the congress that the government needs to pay more attention to the sustainability of development and reassess Vietnam's model of growth. He added that it is necessary to seek a balance between speed and quality of the country's development.

Vietnam's socio-economic targets for 2011 indicate an increased focus towards achieving macroeconomic stability and controlling inflation. We believe this could be due to growing concerns among members of the National Assembly towards mounting inflationary pressures in recent months. The CPV's new leadership will be assessed by the National Assembly based on Vietnam's socio-economic performance in the coming years. This suggest that failure to address mounting inflationary pressures and macroeconomic instability - which is partly a result of the CPV's expansionary policies in recent years - will put the CPV's leadership in a difficult position over the coming years. Indeed, we see the National Assembly's role as an effective check against government policies, and we believe this will help impose accountability on the CPV's policy decisions over the coming years.

Foreign Policy

Strained Relations With China Set To Stay

We anticipate further efforts by Hanoi to deepen ties with Washington and the Association of South East Asian Nations (ASEAN) as a counterbalance against Beijing's growing political clout and military presence in the region. A persistent bilateral trade deficit with China will continue to strain relations as policymakers in Hanoi begin to recognise the threat of losing bargaining power in trade negotiations with China.

Vietnam is struggling to catch up with China's growing economic and political influence in the region. Bilateral relations should remain in a delicate situation over the coming years as Vietnam continues to strengthen ties with US and Russia in a bid to counter Beijing's political clout. Relations have also been strained in recent years as China has expanded its military presence in the disputed Paracel and Spratly Islands in the South China Sea. On the economic front, concerns over a growing trade deficit with China have resurfaced as policymakers in Hanoi begin to recognise the threat of losing bargaining power in trade negotiations with China.

Countering Beijing's Influence

We anticipate further efforts by Hanoi to deepen ties with Washington over the coming years, as Vietnam lean towards the pro-US camp that already includes some of its ASEAN peers such as Indonesia and Thailand. From our perspective, China's growing influence in the region and its expanding military presence in the South China Sea will continue to play a key role in aligning the political interests of Hanoi and Washington. Indeed, we saw a marked improvement in Vietnam-US relations in 2010 as the two countries made a series of symbolic moves in boosting bilateral ties:

In March 2010, the US signed a memorandum of understanding on nuclear cooperation with Vietnam and accelerated negotiations to complete a deal that would allow for the exchange of know-how and cooperation in civilian nuclear technology. Unsurprisingly, the deal came under heavy criticism from China that the US is applying double-standards in its nuclear policies by extending more favourable terms to Vietnam as compared to other deals with emerging nuclear nations such as the United Arab Emirates.

US Secretary of State Hillary Clinton also made two visits to Hanoi in 2010-in July for the ASEAN regional forum and in October for the ASEAN and East Asia summit—during which she made a point of reaffirming the importance of bilateral relations between the two countries. The USS Lassen, which docked in Vietnam in 2009 was also viewed a symbolic move by the two countries to strengthen bilateral ties.

Lagging Behind In An Arms Race With China

The revelation of a Chinese stealth fighter jet in the final stages of development in January 2011 is expected to reignite Vietnam's concerns over China's ambitions to modernize its military. More importantly, the pace of China's progress in developing its military capabilities has come as a surprise to Washington. US Defense Secretary Robert Gates commented during a visit to Beijing that China may be ahead in the development of the aircraft than US intelligence had previously predicted. China's military expansion in recent years has prompted Vietnam to respond by upgrading its own military capabilities. Back in December 2009, Vietnam signed a series of major arms deals with Russia that included six Kilo-class submarines and 20 Su-30 fighter-bombers. The deals amounted to around US$2.6bn, the biggest since Moscow pulled its remaining military interests out of Vietnam at the end of the Cold War about 20 years ago. Judging from Vietnam's response to China's growing military presence in previous years, we note that the recent revelation of China's stealth fighter jet could potentially spark another round of arms deals between Vietnam and Russia.

Relations Strained By A Persistent Deficit

Vietnam is increasingly concerned over its persistent bilateral trade deficit with China, which has amounted to more than 10% of GDP in recent years. We also argue that Vietnam will continue to lean towards ASEAN as a counterbalance to China's growing economic influence. Government efforts to narrow the trade deficit with China have been largely unsuccessful in recent years and policymakers are putting the blame on a depressed Chinese yuan that is keeping prices of Chinese exports artificially low. Nonetheless, China remains strong on its stance of allowing the currency to appreciate gradually, undermining Vietnam's efforts to bring the trade deficit back in balance.

While Vietnamese exporters struggle to compete with cheap Chinese exports, bilateral trade is expected to grow at a robust pace over the coming years. Hanoi is beginning to recognise the threat of becoming overly dependent on imports of intermediate goods from China. In contrast, China's economy is considerably less dependent on trade with Vietnam. Hanoi is slowly losing its bargaining power in terms of trade negotiations with Beijing, in our view. Indeed, the growing reliance on China imports has already attracted a degree of attention at the Communist Party of Vietnam's 11th National Congress that was held in January 2011.

Going forward, we expect the issue of a persistent trade deficit with China to dominate Hanoi's engagement with Beijing on economic negotiations. South East Asia's plan to establish an ASEAN Economic Community by 2015 could potentially serve as a collective bargaining tool against China, in our view. As such, we expect Vietnam to continue to show support for ASEAN's efforts to promote intra-regional trade and investment.

Long-Term Political Outlook

Key Political Challenges Over The Coming Decade

We believe that Vietnam's biggest political question over the coming decade is whether one-party rule under the Communist Party of Vietnam (CPV) will face growing calls for democratisation, as was the case in other major Southeast Asian countries. While our core scenario envisages the CPV transforming itself into a technocratic administration, it faces major economic challenges which if mismanaged could lead to widespread unrest. On the foreign policy front, we expect an increasingly powerful China to drive Vietnam further into the camp of Asian nations with close relations with the US.

Although Vietnam is a politically stable country, we view the ruling Communist Party of Vietnam's (CPV) monopoly on political power as unsustainable over the long term. One of the CPV's biggest challenges will be managing Vietnam's transformation into a more pluralistic society over the coming decade and beyond. Indeed, the CPV's strict control of the media and political opinion is already cracking, with a growing number of internet bloggers becoming increasingly critical of government policy.

Challenges And Threats To Stability

Inflation And Devaluation As Drivers Of Discontent

As in neighbouring China, economic growth has brought sizeable material gains for the majority of the population. However, the Vietnamese government's loose fiscal and monetary policies have led to high levels of inflation and repeated devaluations of the dong in recent years, which have eroded the real value of wages and savings. A failure to contain inflation at a reasonable level and uphold the real value of the dong could undermine confidence in the regime.

Divisions Within The Communist Party

High inflation and devaluation have opened schisms within the CPV leadership between proponents of continued economic reform and a more conservative wing which believes that a deceleration or even reversal of reform policies would benefit macroeconomic stability.

Ethnic And Regional Tensions

Vietnam is relatively homogenous, with ethnic Viet comprising almost 90% of the population. Ethnic minorities in the Central Highlands have previously objected to government policies promoting migration of ethnic Viet into the highland region. While protests have died down, they could emerge in future. A potential spark could be the Chinese-financed bauxite mining project in Lam Dong and Dak Nong provinces, which is currently causing widespread environmental damage and thus raising ire among the local population.

There are also continued cultural differences between the population of the Red River Delta around the capital Hanoi in the north and the population of the Mekong Delta in the south, where Ho Chi Minh City (formerly Saigon, the ex-capital of South Vietnam) remains the commercial capital. While the general perception is that northerners are more supportive of socialist rule and the southerners more inclined to support continued economic reform, a strong concept of national unity nevertheless exists in both parts of the country.

Demands For increased Religious Rights

One of the most concerted challenges against the CPV in recent years has come from Catholics wishing for a stronger recognition of their right to worship in what is still a nominally atheist country. Hanoi has ceded to pressure from the US to allow a higher degree of religious freedom, but is wary of the Catholic Church becoming a rallying point of political opposition, as was the case in Communist Poland and the Philippines during the Marcos dictatorship. The Vietnamese government has thus slapped heavy sentences on Catholic activists who have extended their fight to encompass increased political freedom.

Relations With China

Relations with China have become increasingly strained in recent years as Beijing has expanded its economic, political and military influence southwards. The main point of contention is the conflicting territorial claims for the Paracel and Spratly Islands in the South China Sea. Vietnam's relations with China have also been strained by the large bilateral trade deficit it runs with its northern neighbour, which amounts to more than 10% of GDP, and criticism of a Chinese-financed bauxite mining project in the central highlands.

That said, the regimes in Beijing and Hanoi share the same ideological base and political system, and contacts between their respective Politburos have served to decrease tension between them. Nonetheless, we believe Vietnam will seek increasingly close relations with the US - and potentially India and Japan - in the defence sphere, as a hedge against China's rising power in the region.

Vietnam's long-term political risk rating of 52.8/100 is weighed down by a score of 27.6 in the 'characteristics of polity' subcomponent. This is due to the limited independence of the judiciary, the ban on political parties other than the CPV and severe limitations on the media and civil society. While these factors may presage stability in the short term, the experience of other Southeast Asian nations shows that rising wealth and development later lead to calls for political liberalisation. We have thus drawn up three scenarios for Vietnam's political future:

Scenarios For Political Change

Core Scenario: CPV Turns Into A Technocratic Regime

Our core scenario is for the CPV to shift increasingly towards a technocratic form of government aimed at maintaining high economic growth levels and an acceptable distribution of wealth across the population. Ambitious young Vietnamese are already joining the CPV as a career path and as a means to serve their country rather than because of ideological convictions. We thus foresee a continuation of economic reforms in spite of the criticism emanating from older more traditionally-minded party members. However, intermittent periods of harsh repression against pro-democracy activists and other government critics are a strong indication that political liberalisation is not in the offing.

Best Case Scenario: Gradual Political Liberalisation

Our best-case scenario is the above scenario combined with a gradual move towards political liberalisation involving an expanded role for the National Assembly, greater scope for differing opinion within the CPV, increased political competition at elections, and greater media freedom. This scenario would see Vietnam moving from a one-party system towards a dominant-party system of the kind seen in neighbouring Cambodia, Malaysia and Singapore, where elections are held but only the ruling party has a realistic chance of winning them. Looking even further beyond the horizon, the experiences of South Korea, Taiwan, and Japan have shown that even dominant-party systems eventually give way to opposition rule. However, in Vietnam's case this may be more than a decade away.

Worst-Case Scenario: Mass Unrest And Violent Suppression

Our worst-case scenario involves severe policy missteps that lead to a period of prolonged economic upheaval with high unemployment and rapid inflation eroding wealth. This would significantly strengthen the case for regime change, as advocated by the pro-democracy movement. Faced with widespread street protests and an all-out challenge to one-party rule, we believe that at least part of the CPV leadership would support a crackdown on demonstrators by security forces in order to stay in power. A violent suppression of street protests as seen in Beijing in 1989 and in Myanmar in 2007 could easily result in a number of deaths and the imposition of sanctions by the international community. If so, Vietnam would likely face not only diplomatic isolation but also economic weakness as exports and foreign direct investment tumble.

Macroeconomic Outlook

Real GDP Growth Revised Upward But To Remain Subdued In 2011

Our view that infrastructure investment would provide support for Vietnam's economic growth in 2010 has played out well. Vietnam's real GDP growth came in at a better-than-expected 6.8% in 2010, led by a strong performance in the construction sector. Going into 2011, we expect domestic demand to remain robust on the back of rising wages and improving consumer sentiment. However, we expect import growth to continue to outpace that of exports in 2011. In light of a better-than-expected Q410 result and our global team's recent upgrade on the US economy, we are revising our real GDP growth forecast upwards from 5.5% to 6.3% in 2011.

In line with our view that investment in infrastructure would continue to provide support for Vietnam's economic growth, real GDP growth came in at a better-than-expected 7.2% y-o-y in Q410, led by robust growth in the construction sector. The latest Q410 figure effectively translates into real GDP growth of 6.8% for 2010, surpassing the Vietnamese government's target of 6.7%. According to data published by the General Statistics Office (GSO), the construction sector grew by 10.1% in 2010 while the electricity, gas and water sector also saw double-digit growth of 11.3%. On the other hand, floods across the region in recent months led to a disappointing 2.5% growth in the agricultural sector. Going into 2011, we expect the construction sector to continue to outperform the manufacturing and agricultural sectors.

From our perspective, the latest figures highlight the fact that expansionary economic policies dictated by the National Assembly continue to have a significant influence on the structure of Vietnam's economic growth in 2010. We believe this will continue to be the case in 2011 as the government remains focused on upgrading Vietnam's infrastructure and raising electricity production to support the country's economic growth. Despite our positive outlook for infrastructure investment though, we continue to see overheating pressures that should prevent growth from reaching the government's 7.5% target in 2011.

Slow Recovery In Manufacturing Sector

Looking at industrial production growth, we have seen a slow and steady rise from 14.5% y-o-y in October to 16.3% in December. Given that industrial production data has traditionally served as a reliable indicator of the performance of the manufacturing sector, we remain optimistic that the recovery in the manufacturing sector remains on track. That said, we believe that the performance of the sector will increasingly rely on demand from Asia rather than the US and Eurozone in 2011. The manufacturing sector grew by 8.4% in 2010, far from the sector's pre-crisis growth of 12.4% in 2007. Indeed, we see economic uncertainties in the US and EU as a reason behind the slow recovery in the manufacturing sector. We believe 2011 will be a challenging year for the manufacturing sector due to below trend economic growth in the US, and tightening efforts in China in light of inflationary pressures. However, an improved outlook for the US economy will nonetheless have a positive impact on exports. As such, we are revising our real GDP growth forecast upwards from 5.5% to 6.3% in 2011.

High Lending Rates Threatens Investment Growth

Aggressive economic policies by the Vietnamese government have led to mounting inflationary pressures in recent months. Consumer price inflation (CPI) accelerated from 7.6% y-o-y in January to 11.8% in December, averaging 9.2% for 2010. This contributed to a rise in production costs and higher lending rates for businesses. We expect lending rates, which are currently in the range of 14.0-17% to remain elevated and to put a damper on gross fixed capital formation (GFCF) growth in 2011. Furthermore, rising production costs are likely to lead to lower profit margins for businesses, lowering the incentive for businesses to invest in expanding operations. Accordingly, we are forecasting a subdued 7.0% growth in private investments in 2011.

Table: Vietnam – Economic Activity, 2008-2015

	2008	2009	2010	2011f	2012f	2013f	2014	2015
Nominal GDP, VNDbn [1]	1,485,038	1,658,389	1,953,223	2,326,854	2,641,667	2,985,463	3,358,614	3,761,092
– US$bn [1]	89.8	92.8	101.9	117.8	133.8	155.1	179.1	206.1
Real GDP growth, % y-o-y [1]	6.3	5.3	6.8	6.3	7.2	7.2	7.2	7.2
GDP per capita, US$ [1]	1,041	1,063	1,153	1,320	1,483	1,703	1,948	2,220
Population, mn [2]	86.2	87.3e	88.4e	89.3	90.2	91.1	92.0	92.8
Industrial production index, % y-o-y, average [1]	13.6	6.7	14.0e	10.0	15.0	16.0	17.0	16.0
Unemployment, % of labour force, end of period [1]	4.7	6.0	5.0e	6.0	5.0	5.0	5.0	5.0

f = BMI forecast. Source: [1] General Statistics Office; [2] World Bank, BMI

Strong Performance In Spite Of Growing Trade Deficit

Despite a widening trade deficit of US$3.8bn in Q410, compared to US$2.2bn in Q310, Vietnam's economy managed to grow by 20.4% q-o-q in Q410. Although we acknowledge that seasonal factors were largely responsible for the spike in domestic demand - historical data shows the final quarter in previous years seeing a significant spike in domestic demand - we believe private consumption will remain robust in the coming months. Judging from the better-than-expected performance in domestic demand in Q410, we believe consumer sentiment will continue to improve and this in turn supports our view that private consumption will remain strong in 2011. Rising wages in Vietnam is also likely to support consumer spending in the coming months.

We believe that robust private consumption will result in import growth outpacing export growth and a deteriorating trade deficit in 2011. The recent rise in crude oil prices represents a threat to the trade deficit as Vietnam remains a significant net importer of refined crude. Should crude prices continue to rise in the coming months, we expect this to have a negative impact on the trade deficit and real GDP growth. We are maintaining our forecast for the trade deficit to widen from an estimated 7.0% of GDP in 2010 to 8.0% of GDP in 2011. Accordingly, we see this as a reason for our subdued real GDP growth forecast of 6.3% in 2011.

Company Profiles

Vietnam National Shipping Lines (Vinalines)

Strengths	▪ Diversified fleet operating in the areas of dry bulk, container and oil transport ▪ Largest commercial shipping line in Vietnam
Weaknesses	▪ Does not play a role on the major Asia-Europe routes, despite Vietnam developing as a direct port of call on these routes.
Opportunities	▪ Exposure to Vietnam, which is expanding its role in the global box market and it fast becoming a mainstay port of call on Asia-Europe services. ▪ Potential to increase its intra-Asia role and well placed to be chosen as partner on these services by the bigger lines.
Threats	▪ While Vietnam has invested heavily in the port network the logistic supply chain could be let down by the landside freight network, which will have a negative impact on operators in the country.

Company Overview

Vinalines is Vietnam's largest commercial shipping line established in 1996. The line caters for domestic trade in Vietnam and also offers intra-Asia services.

The company also boasts a port operating division which is the largest in Vietnam with the company controlling and managing ports in the areas of Quang Ninh, Hai Phong, Da Nang, Ho Chi Minh and Can Tho.

Strategy

Vinalines 14 shipping companies over a diverse fleet, which while it is dominated by dry bulk vessels, boasts container ships, oil and product oil vessels.

As of the end of Q210 (last published data) Vinalines fleet consisted of 150 vessels with a capacity of 3.1mn dwt. The line is looking to expand, with a mid term plan to increase the line's capacity to 6-7mn dwt by 2010. The plan centres on increasing the proportion of specialised vessels such as box ships or oil tankers.

In order to achieve this, the line is seeking to spend US$2bn on ordering new ships from Vietnamese yards seeking state funding for the plan. Vinalines has in fact ended up expanding its fleet quicker than it first planned with the shipping line taking on 36 vessels from the debt laden Vietnamese shipbuilder Vinashin in July 2010. Vinaline's chairman, Duong Chi Dung, stated at the time that up to two-thirds of the acquired vessels cannot be used currently as they fail to meet technical requirements. He estimated that the company will need to spend US$26mn to repair the vessels and purchase insurance cover. Dung stated that he expects some financial aid from the government for the project.

Vinalines services the trade needs of Vietnam's domestic shipping market but also has exposure to the intra-Asia trade lane joining forces with NYK in December 2010 to launch a Thailand-Vietnam-Singapore (TVS) service providing a 1,100TEU vessel for the service.

BMI believes that Vinalines presence on the intra-Asia trade route will increase, with major lines looking to expand into the route and Vinalines well placed to play a role in partnering

	with these big lines on the route. Vinalines is increasing it contacts in container sector partnering with a number of the majors on container terminal projects in Vietnam.
Latest Activity	Vinalines joint container terminal venture with CMA CGM and Saigon Port, the Cai Mep International Terminal (CMIT) has been launched and has already cemented its position as a terminal to watch receiving the 11,500TEU CMA CGM Columba in March 2011. Vinalines is increasing its role in Vietnam's container terminal sector and is doing so with some of the major box lines, the carrier, along with MOL, NYK and Itochu Corporation are to develop two wharves at the port of Haiphong.

Vietnam Airlines Cargo

Strengths	▪ Vietnam Airlines Cargo is the main air cargo provider in Vietnam
Weaknesses	▪ Unlike its peers Vietnam Airlines Cargo does not have a freighter fleet and is reliant on using the belly hold of its parent company's planes.
Opportunities	▪ The air carrier is well placed to benefit from Vietnam's growing role in the trade sector, the country has flooded money into the development of the country's port sector, but BMI believes aviation also stands to benefit.
Threats	▪ While the sector has recovered well the outlook for global air freight remains volatile especially with oil prices at their current high levels.

Company Overview

Vietnam Airlines Cargo's parent Vietnam Airlines began operations in 1956 serving the domestic market. In 1993 it was established as Vietnam's national carrier.

Vietnam Airlines Cargo's operations are concentrated in Asia, with the carrier still catering to the domestic market. The airline operates its cargo business by transporting goods in the belly's of its passenger planes.

Strategy

Operating out of hubs in Hanoi and Ho Chi Minh City, Vietnam Airlines Cargo has developed a route network both domestically and internationally. Within Vietnam the carrier lands at 18 domestic airports. The carrier is heavily Asia focused with three freight flights to neighbouring Thailand and routes servicing China, Hong Kong, Japan, South Korea, Taiwan, Philippines, Malaysia and Indonesia. Thereby allowing the air freight carrier to cater for all five of Vietnam's top five import partners.

The carriers expansion into China offers a launch pad for further services to other Chinese airports.

Vietnam Airlines Cargo has also developed routes to Australia with freight connections to Melbourne and Sydney.

Further afield Vietnam Airlines Cargo offers cargo links to three destinations in Europe, Paris Frankfurt and Moscow.

Vietnam Airlines Cargo is able to utilise the cargo capacity of the belly holds of its parent company's passenger planes.

Latest Activity

Older Planes To Be Checked

Aircraft belonging to Vietnam Airlines Cargo's parent Vietnam Airlines along with like other airlines in Vietnam are set to have their older aircraft checked following a decision by the Civil Aviation Authority of Vietnam to implement inspections on old, but operating aircraft in Vietnam. The planned inspections follow holes being noticed on the fuselage on a series of Boeing 737-300 in the US.

Vinatrans

Strengths	▪ Vinatrans is a diversified logistics company, offering a wide variety of services.
Weaknesses	▪ The company is exposed to all of the weaknesses of state owned companies, such as inefficiency and underfunding.
Opportunities	▪ **BMI** has identified intra-Asia trade as a market to watch, as consumer demand in the traditional markets of the US and Europe remains sluggish.
	▪ Vietnam is part of the ASEAN 5. As such, it should see an uptick in trade as a result of the group's FTA with China.
Threats	▪ Rising fuel prices pose a threat to logistics companies' profit margins.
	▪ The rate of economic growth in Vietnam has far outpaced the country's infrastructure. Road, railways and ports are all badly in need of upgrades.

Company Overview

Vinatrans is a state-owned Vietnamese freight forwarding company, providing door-to-door logistics worldwide and a number of related services. These include airfreight and sea freight forwarding (including customs clearance, cargo surveying, insurance, air consolidation for inbound and export cargoes, and exhibition or project handling), shipping (including chartering, husbandry, crewing, and brokerage services) and warehousing/cold storage provision.

The company is 100% owned by the Vietnamese Ministry of Trade and acts as an agent for several foreign organisations including BAX Global, Hapag-Lloyd Container, Zim Israel Navigation Company and Panalpina. The firm's warehousing and storage facilities in Vietnam include a 2,500m2 Container Freight Station (CFS) for sea and air cargo, a joint venture cold storage facility of 2,800m2 run by Vinatrans and Konoike Transport Company of Japan, 40,000m2 of covered warehousing and 50,000m2 of open storage.

Strategy

BMI has been following the trend of increasing investment in the Vietnamese port sector as the country establishes itself as a centre of production, particularly for the textile industry. We caution, however, that as many factories are situated inland, investment in the supply chain as a whole, including road, air, rail and storage, will be needed to deal with increasing demand. Having declined by 10% year-on-year in 2009 2010 once more saw increased growth for Vietnamese exports. The volume of imports and exports is forecast to grow by 20% in 2011.

According to the Civil Aviation Authority of Vietnam, air freight to and from Vietnam increased by 37% y-o-y to reach 340,000 tonnes in 2010. As such, we see growth opportunities for Vinatrans in the sector. We note that several air cargo carriers have already spotted the potential in the market. Chinese carrier **Jade Cargo** has recently opened the first airfreight link between Vietnam and Amsterdam. In 2009 **Lufthansa Cargo**, the airfreight subsidiary of **Deutsche Lufthansa**, launched a weekly direct service between Frankfurt and Hanoi, which it is considering doubling in the future to keep up with demand. Vietnam Airlines is planning to increase its flights between Hanoi and Paris, Hanoi and Moscow, and Hanoi and Frankfurt, from late-June 2011, which could potentially mean an increase in the amount of freight carried on the routes.

Financials

Vinatrans has reported consolidated earnings results for the second quarter and first half of 2010. In the second quarter, the company made a net profit of VND5.06bn on revenues of VND 109.42bn, versus VND 3.42bn and VND62.99bn in the same period of 2009. The company made a net profit of VND9.94bn in the first half of this year, down 14.16% from a year earlier. Net revenues, however, rose 44.05% on year to VND189.08bn during the period. Its six-month earnings per share (EPS) was VND 1,816, compared to VND2,117 in the same period last year. This year, the company targets a pre-tax profit of VND23bn on revenues of VND 300bn. The company targets a dividend payout equivalent to VND1,500 per share for the year 2010.

Latest Activity

Viffas Voices Fears Logistics Companies Too Small

According to the Vietnam Freight Forwarders Association (Viffas) Vietnam now has more than 1000 enterprises which provide logistics services, most of which, about 600-700 enterprises, are located in Ho Chi Minh City. Commenting on the capabilities of the enterprises, Mai Xuan Thieu, Head of the Vietnam Logistics Institute said the majority of enterprises have a modest capital of VND1-1.5bn.

As a result, the majority of their work is as agents for multinational groups. Thieu said that Vietnamese enterprises are not capable of providing enough transport services throughout Vietnamese territory with competitive costs. Currently, Vietnamese companies only can meet 25% of the total domestic demand. BMI believes this is a cause for concern, given that we expect the country's trade volumes to continue growing.

Vietnam Petroleum Transport Company (VIPCO)

Strengths

- 60% of the company's fleet is employed by Petrolimex
- The company boasts a relatively young fleet
- The company has diversified away from operating in a single sector, with a real estate arm.

Weaknesses

- The company only operates in one shipping sector.

Opportunities

- The company plans to expand its fleet.

Threats

- Vietnam's reliance on imported refined products is decreasing as the country brings online more refining capacity, which could negatively affect VIPCO. In the longer term Vietnam's refining capacity could allow the state to export.

Company Overview

The Vietnam Petroleum Transport Joint Stock Company (VIPCO) offers maritime transport for petroleum products. The company has a diversified portfolio and along with units which support its product tanker fleet such as its port operations and freight forwarding services the company is also engaged in real estate.

Strategy

VIPCO's has developed a fleet of 6 product tankers with a total capacity of 176,111 dead weight tonne (dwt). The fleet is relatively young with an average age of 16 years. VIPCO has a fleet expansion strategy in place and is prepared to invest in either via newbuilds or purchasing tankers under the age of ten years. The company plans to boost its fleet to 200,000dwt.

VIPCO's employment strategy for its tankers divides the fleet's employment up with 60% of the fleet meeting the transport needs of the Vietnam National Petroleum Corporation (Petrolimex) the other 40% of the fleet is charted to other consignees.

Via its connection with VNPC the company is able to cater for Vietnam's oil sector, while the country boasts estimated oil reserves of 4.6bn barrels, the country imports refined products.

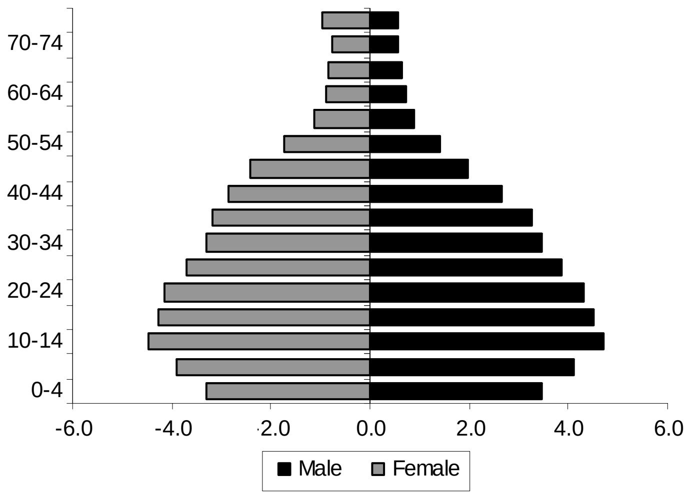
The company's shipping unit is complimented by its petrochemical terminal's sector.

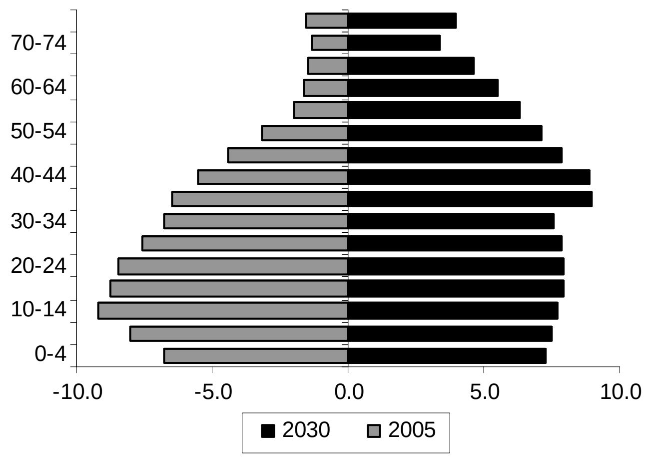
Latest Activity

VIPCO stands to benefit from a deal signed between Petrolimex and SK Energy in February 2011. The contract will see the South Korean firm supply Petrolimex with 900,000cbm of RON 92 gasoline and diesel oil in 2011.

Country Snapshot: Vietnam Demographic Data

Section 1: Population





Source: UN Population Division

Table: Demographic Indicators, 2005-2030

	2005	2010f	2020f	2030f
Dependent population, % of total	34.1	29.9	30.4	31.2
Dependent population, total, '000	28,318	26,225	30,950	34,499
Active population, % of total	65.8	70.0	69.5	68.7
Active population, total, '000	54,650	61,263	70,706	75,927
Youth population*, % of total	28.8	25.0	23.4	20.3
Youth population*, total, '000	23,972	21,887	23,807	22,508
Pensionable population, % of total	5.2	4.9	7.0	10.8
Pensionable population, total, '000	4,346	4,338	7,143	11,991

*f = forecast. * Youth = under 15. Source: UN Population Division*

Table: Rural/Urban Breakdown, 2005-2030

	2005	2010f	2020f	2030f
Urban population, % of total	26.7	29.4	34.7	41.8
Rural population, % of total	73.3	70.6	65.3	58.2
Urban population, total, ‘000	22,509	26,395	35230	46,123
Rural population, total, ‘000	61,729	63,323	66426	64,306
Total population, '000	84,238	89,718	101,656	110,429

f = forecast. Source: UN Population Division

Section 2: Education And Healthcare

Table: Education, 2002-2005

	2002/03	2004/05
Gross enrolment, primary	98	93
Gross enrolment, secondary	73	75
Gross enrolment, tertiary	10	16
Adult literacy, male, %	na	93.9
Adult literacy, female, %	na	86.9

Gross enrolment is the number of pupils enrolled in a given level of education regardless of age expressed as a percentage of the population in the theoretical age group for that level of education. na = not available. Source: UNESCO

Table: Vital Statistics, 2005-2030

	2005	2010f	2020f	2030f
Life expectancy at birth, males (years)	68.4	69.9	74.2	75.8
Life expectancy at birth, females (years)	72.4	73.9	78.4	80.0

Life expectancy estimated at 2005. f = forecast. Source: UNESCO

Section 3: Labour Market And Spending Power

Table: Employment Indicators, 1999-2004

	1999	2000	2001	2002	2003	2004
Employment, '000	38,120	38,368	39,000	40,162	41,176	42,316
– % change y-o-y	3.1	0.6	1.6	2.9	2.5	2.7
– male	19,029	19,292	19,744	20,356	20,959	21,649
– female	19,091	19,076	19,257	19,807	20,217	20,666
— female, % of total	50.0	49.7	49.3	49.3	49.1	48.8
Unemployment, '000	909	886	1,107	871	949	926
– male	439	468	458	398	402	410
– female	470	418	650	473	547	517
– unemployment rate, %	2.3	2.2	2.7	2.1	2.2	2.1

Source: ILO

Table: Consumer Expenditure, 2000-2012 (US$)

	2000	2007e	2008f	2009f	2010f	2012f
Consumer expenditure per capita	110	265	301	368	386	427
Poorest 20%, expenditure per capita	49	119	136	166	174	192
Richest 20%, expenditure per capita	243	587	668	815	855	946
Richest 10%, expenditure per capita	316	763	868	1,060	1,112	1,230
Middle 60%, expenditure per capita	85	206	235	286	301	332
Purchasing power parity						
Consumer expenditure per capita	556	1,196	1,297	na	na	na
Poorest 20%, expenditure per capita	250	538	583	na	na	na
Richest 20%, expenditure per capita	1,231	2,649	2,872	na	na	na
Richest 10%, expenditure per capita	1,600	3,444	3,734	na	na	na
Middle 60%, expenditure per capita	433	931	1,009	na	na	na

e/f = BMI estimate/forecast. na = not available. Source: World Bank, Country data; BMI calculation

BMI Methodology

How We Generate Our Industry Forecasts

BMI's industry forecasts are generated using the best-practice techniques of time-series modelling. The precise form of time-series model we use varies from industry to industry, in each case being determined, as per standard practice, by the prevailing features of the industry data being examined. For example, data for some industries may be particularly prone to seasonality, i.e. seasonal trends. In other industries, there may be pronounced non-linearity, whereby large recessions, for example, may occur more frequently than cyclical booms.

Our approach varies from industry to industry. Common to our analysis of every industry, is the use of vector autoregressions. Vector autoregressions allow us to forecast a variable using more than the variable's own history as explanatory information. For example, when forecasting oil prices, we can include information about oil consumption, supply and capacity.

When forecasting for some of our industry sub-component variables, however, using a variable's own history is often the most desirable method of analysis. Such single-variable analysis is called univariate modelling. We use the most common and versatile form of univariate models: the autoregressive moving average model (ARMA).

In some cases, ARMA techniques are inappropriate because there is insufficient historic data or data quality is poor. In such cases, we use either traditional decomposition methods or smoothing methods as a basis for analysis and forecasting.

It must be remembered that human intervention plays a necessary and desirable part of all our industry forecasting techniques. Intimate knowledge of the data and industry ensures we spot structural breaks, anomalous data, turning points and seasonal features where a purely mechanical forecasting process would not.

Transport Industry

There are a number of principal criteria that drive our forecasts for each transport variable:

GDP Growth
As transport activity is heavily influenced by real GDP growth, this factor is examined to ascertain its relationship with overall trade volumes. Projected GDP growth is calculated using **BMI**'s own macroeconomic and demographic forecasts.

Real Trade Volumes
The sum of imports and exports plays a particularly important role in developing countries with a small

domestic industrial sector. In particular, the focus is on goods, as services do not employ transport. The volumes are forecast based on the following criteria:

- Trends manifested through historical data;
- The impact of future step changes to the economy (such as future membership of the EU or some other regional body).

Port Traffic

Port traffic levels act as a ‘second opinion’ on trade volumes. However, this check needs to be used with caution as trade values and volumes do not always move over time in the same way.

Market Share

The market share of each mode (road, rail, inland waterway, coastal shipping) for future years is based upon:

- Trends in historical modal split data;
- Evidence of government policy favouring one or more modes over others;
- Government and or private sector investment plans in specific modes.

Sources

Sources used in transport reports include local transport ministries, officially released company results and figures, established think tanks and institutes and donor agencies such as the World Bank and the Asian Development Bank.