

Q4 2011

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Q4 2011 [www. businessmonitor. com](http://www.businessmonitor.com) VietnaM agribusiness report INCLUDES BMI'S FORECASTS issn 1759-1740 published by business Monitor international Ltd. VIETNAM AGRIBUSINESS REPORT Q4 2011 INCLUDES 5-YEAR FORECASTS TO 2015 Part of BMI's Industry Report & Forecasts Series Published by: Business Monitor International Copy deadline: September 2011 Business Monitor International 85 Queen Victoria Street London EC4V 4AB UK Tel: +44 (0) 20 7248 0468 Fax: +44 (0) 20 7248 0467 email: [subs@businessmonitor. com](mailto:subs@businessmonitor.com) web: <http://www. businessmonitor. com> © 2011 Business Monitor International. All rights reserved. All information contained in this publication is copyrighted in the name of Business Monitor International, and as such no part of this publication may be reproduced, repackaged, redistributed, resold in whole or in any part, or used in any form or by any means graphic, electronic or mechanical, including photocopying, recording, taping, or by information storage or retrieval, or by any other means, without the express written consent of the publisher. DISCLAIMER All information contained in this publication has been researched and compiled from sources believed to be accurate and reliable at the time of publishing. However, in view of the natural scope for human and/or mechanical error, either at source or during production, Business Monitor International accepts no liability whatsoever for any loss or damage resulting from errors, inaccuracies or omissions affecting any part of the publication. All information is provided without warranty, and Business Monitor International makes no representation of warranty of any kind as to the accuracy or completeness of any information hereto contained. Vietnam Agribusiness Report Q4 2011 © Business Monitor International Ltd Page 2 Vietnam

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Page 4 Vietnam Agribusiness Report Q4 2011 Executive Summary BMI View:

The agriculture industry is very significant for the Vietnamese economy. In fact, Vietnam's agriculture industry (including forestry and aquaculture) contributes to more than 20% of the country's GDP and employs almost half of the country's population. While the country is looking forward to higher agriculture export earnings in 2011, we believe Vietnam will still face strong competition from neighbouring countries' cheap imports, especially for the livestock and dairy sectors. Thus, the government has pledged to invest more than VND20trn (US\$1bn) in the agricultural sector in order to increase the 'value' of its exported products by at least 20% over the next ten years. This would imply lifting the quality of agricultural outputs such as coffee and rice, through better technologies. Key Trends: Corn production growth to 2014/15: 39. 7% to 6. 9mn tonnes. This will be due to current yield immaturity, which means significant gains are still available via this avenue, especially as robust local corn prices provide incentives to farmers. Also an important growth driver will be domestic consumption, especially from the livestock sector. Coffee consumption growth to 2015: 54. 2% to 1. 6mn bags.

This will come as the Ministry of Agriculture and Rural Development (MARD) has said it hopes to boost domestic consumption to 10-15% of the national coffee crop. Poultry production growth to 2014/15: 19. 8% to 419, 000 tonnes. This is because rising incomes will stimulate domestic meat consumption growth (due to diet diversification) and production will increase to keep pace. 2011f Real GDP Growth: 6. 3% (down from 6. 8% in 2010; predicted to average 7. 0% from 2010 until 2015). Consumer Price Inflation: 27% y-o-y in July 2011 (forecast to average 18. 6% in 2011). Industry Developments With the domestic coffee supply crunch expected to persist until the 2011/12 the crop starts to come online in early October, we believe these developments should offer some support to prices in the near term. Coffee exports in June totalled 80, 000 tonnes, 15. 8% lower on a year-on-year basis, and July exports are forecast to reach 55, 000 tonnes, representing a 38. 2% dip from a year ago. A reason for the shortage is the fact that farmers had sold close to 90% of the harvested 2010/11 crop on the back of surging prices at the start of this year, leading to a year-on-year surge of exports by 21. 7% for the first five months of the year. Approximately 40, 000 tonnes of coffee deliveries have already been cancelled for July delivery. According to reports, there is currently about 200, 000 tonnes of coffee, or only © Business Monitor International Ltd Page 5 Vietnam Agribusiness Report Q4 2011 approximately three months' worth of coffee exports currently kept under storage in warehouses in Vietnam. Consumers will be confronted with higher dairy product prices, especially milk powder prices in the medium term. Anecdotal reports in late March 2011 claimed that prices of imported milk products such as milk powder had

risen by 18% on the back of an 8.5% Vietnamese Dong devaluation. According to the report, milk powder products from Abbott products have increased 12-18%, Similac IQ 400-gram box rose by 13% to VND215,000/box, and Similac IQ 900-gram box increased by 12% to VND437,000/box. Foreign milk firms such as Nestlé, FrieslandCampina, 3A and Mead Johnson will also reportedly raise milk powder prices by an average 5-17% starting from March 1. Given the low incomes earned by the average worker, we think these milk price hikes will only place these products further out of reach of the masses and might lead to substitution effects in the short to medium term. While we are largely optimistic about the growth prospects for the livestock industry - we forecast production output of poultry, pork and beef to grow by 19.8%, 15.1% and 52.5% respectively over our five-year forecast period - there are salient downside risks to this outlook. We highlight the three main challenges as high interest rates, a reliance on imports (which causes the livestock industry to be vulnerable to fluctuating input prices) and finally, the fragmented nature of the market. © Business Monitor International Ltd Page 6 Vietnam Agribusiness Report Q4 2011 SWOT Analysis Vietnam Agricultural SWOT Strengths The natural fertility of Vietnam around the Red River Delta in the north and the Mekong River Delta in the south provides the country with a strong agricultural base. Vietnam is the world's second largest exporter of both rice and coffee. It also enjoys relatively high rice yields compared to its regional counterparts. Agricultural productivity has improved considerably since the opening up of the economy in 1986. Weaknesses Much of Vietnam's agriculture is based on small-scale farms with poor yields in comparison to more developed international

competitors. Transportation and production infrastructure is often poor, making getting crops to market difficult and negatively affecting quality.

Opportunities Since the opening up of the economy in 1986, allowing more private involvement in agriculture, yields have improved dramatically and look set to continue doing so over our forecast period to 2013. Vietnam's fast-growing population of over 80mn provides a large market for agro-food products. With BMI forecasting Vietnamese GDP per capita to grow rapidly over our forecast period to 2015, consumers will have more money to spend on food, spurring growth in agricultural production.

Threats Poor knowledge of good farming practices and hygiene standards leaves Vietnamese agriculture open to disease outbreaks of the kind that have plagued the livestock industry in recent years. The rising population and increasing industrialisation of the economy will increase competition for land use, curtailing the area available for expansion of agriculture.

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Political SWOT

Strengths The Communist Party of Vietnam remains committed to market-oriented reforms and we do not expect major shifts in policy direction over the next five years. The one-party system is generally conducive to short-term political stability. Relations with the US have witnessed a marked improvement, 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 within the one-party system. Threats Macroeconomic instabilities in 2010 and 2011 are 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 undemocratic rule. Although strong domestic control will ensure little change to Vietnam's 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 recent years 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. © Business Monitor International Ltd Page 8 Vietnam Agribusiness Report Q4 2011 Vietnam Economic SWOT Strengths Vietnam has been one of the fastest-growing economies in Asia in recent years, with GDP growth averaging 7. 2% annually between 2000 and 2010. 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 to global economic uncertainties in 2011. The fiscal deficit is dominated by substantial spending on social subsidies that could be difficult to withdraw. The heavily-managed and weak dong currency reduces incentives to improve quality of exports, and also serves to keep import costs high, thus contributing to inflationary

pressures. Opportunities W TO 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 the 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. © Business Monitor International Ltd Page 9 Vietnam Agribusiness Report Q4 2011 Vietnam Business Environment SWOT Strengths Vietnam has a large, skilled and low-cost workforce, that has made the country attractive to foreign investors. Vietnam's location - its proximity to China and South East Asia, and its 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. Vietnam remains one of the world's most corrupt countries. Its score in Transparency International's 2010 Corruption Perceptions Index was 2.7, placing it in 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 the possibility of the transfer of high-tech skills and knowhow. Vietnam is pressing ahead with the privatisation of state-owned enterprises and the liberalisation of the 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. © Business Monitor International Ltd Page 10 Vietnam Agribusiness Report Q4 2011 Supply Demand Analysis Vietnam Sugar Outlook BMI Supply View: Vietnam's sugar industry suffers from a lack of technological advancement and investment as a result of cheap imports and competition from higher quality, more efficient producers. The area harvested for sugar reached a 40-year high of 320, 000 hectares in 2001/02, but has not returned to that level in subsequent seasons. To mitigate the fall in area planted, sugarcane yields have increased by 21% from 1997/98 to 2007/08. For 2010/11 we expect production to grow by a marginal 0. 3% year-on-year. Over the forecast period, we expect sugar production to increase by 4. 9% to 1. 2mn tonnes, driven by stronger domestic demand and an increase in yields. Despite this, the country will likely remain a net sugar importer, as demand is expected to outstrip supply. The US Department of Agriculture forecasts sugar imports into Vietnam to rise again in 2011/12 to 1. 5mn tonnes, after a fall to 1. 4mn tonnes in 2010/11. BMI Demand View: Increasing the country's import dependency, Vietnamese sugar consumption is forecast to continue climbing 14. 3% to 2015 to reach 1. 7mn tonnes. We therefore maintain our bullish

Vietnamese economic growth outlook for the medium term. This positive outlook is bolstered by the robust sales figures for sugar confectionary and soft drinks of 41. 3% and 53. 6% growth (in local currency terms) respectively over our forecast period. Table: Vietnam Sugar Production & Consumption, 2010-2015

Year	2010	2011	2012	2013	2014	2015
Sugar Production, '000 tonnes	1, 119. 0	1, 2	122. 7	1, 133. 6	1, 145. 8	1, 159. 2
Sugar Consumption, '000 tonnes	1, 122. 7	1, 133. 6	1, 145. 8	1, 159. 2	1, 174. 0	1, 492. 7
Sugar Production, '000 tonnes	1, 535. 2	1, 574. 0	1, 615. 2	1, 658. 9	1, 705. 4	

Notes: BMI forecasts. In all instances year indicates data for harvest year ending that calendar year i. e. 2011 = 2010-11; Sources: USDA, BMI. Full Potential Not Yet Realised The industry is now in a state of transition as international agreements are forcing Vietnam to cut protection. Under the ASEAN Free Trade Area (AFTA) agreement, Vietnam has to reduce tariffs on sugar imports from ASEAN members to a maximum of 5% by 2011. This will expose the country to imports from Thailand, a major sugar exporter. Tariffs on imports from other countries will also have to be reduced by 2011 in line with the government's commitments to the WTO. The government has been trying to increase efficiency in the sector to prepare it for greater integration with the world economy by encouraging farmers to plant high-yielding cane varieties and improving the

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Q4 2011 mechanisation of cane production. In 2007, the government presented a plan for the development of the sector to 2010 and further to 2020. The plan aimed for annual production of 1. 5mn tonnes of sugar from 1. 9mn tonnes of sugar cane by 2010. Obviously this was not met. The plan had envisioned 300, 000 hectares (ha) planted to sugarcane and yields of 65

tonnes/ha. Average yields are still some way off this level and cane production in 2009 is estimated at around only 10mn tonnes, though it stood at 12.1mn tonnes in 2008. By 2020, the plan is aiming for production of 2.1mn tonnes to be achieved through increasing cane yields and the sugar content of cane. To achieve these ambitious aims the government has put a moratorium on the building of new mills so that technology in existing mills can be improved. Provincial authorities will assist mills in organising the zones where their cane will come from and assist in improving farming practices. Financially, the government has committed to investing in importing and propagating new cane varieties and improving infrastructure such as reservoirs and irrigation canals. While government support for the sector is encouraging, we believe it will struggle to produce enough sugar for domestic consumption. Once tariffs are lowered by 2011, it is likely that the government will have to support the sector by other means to keep production on course, as it is unlikely that Vietnamese-produced sugar will be able to compete with imports by then. French shipping service company Bourbon SA has recently sold off its 69% stake in local sugar company Sucrerie de Bourbon Tay Ninh to a group of Vietnamese investors for EUR34mn (USD483mn). BMI believes that as the company is now in the hands of local producers, there could be more incentive to improve efficiencies and strengthen the falling revenues of the company.

Table:
Vietnam Sugar Production & Consumption, 2006-2011

	2006	2007	2008	2009	2010	2011
Sugar Production, '000 tonnes	930.0	1,210.0	1,100.0	1,220.0	1,000.0	1,119.0
Sugar Consumption, '000 tonnes	1,122.7	1,300.0	1,300.0	1,400.0	1,450.0	1,492.7

Notes: BMI forecasts. In

all instances year indicates data for harvest year ending that calendar year i. e. 2011 = 2010-11; Sources: USDA, BMI. Risks To Outlook Risks to consumption growth remain. We have factored in the effects of monetary tightening on spending on non-essential food and drink purchases, such as soft drinks and confectionery (both of which fell by 4% y-o-y in 2009), but were this reduction to be exacerbated by a secondary slowdown in the Vietnamese economy - perhaps due to reduced investment as a result of sluggish US and eurozone growth - our sugar consumption forecasts are unlikely to be achieved. © Business Monitor International Ltd Page 12

Vietnam Agribusiness Report Q4 2011 If government support for sugar production proves ineffective and mill owners are not able to increase profitability, the sector could struggle when import tariffs on sugar are reduced in 2012. Though it is not our core scenario, this could possibly see output fall later in our forecast period. © Business Monitor International Ltd Page 13

Vietnam Agribusiness Report Q4 2011 Vietnam Livestock Outlook BMI Supply View: Within the Vietnamese livestock industry, pig farming is by far the most significant sector, with pork production comprising about two thirds of total meat production in 2010/11. For 2010/11, we expect poultry production to grow by a healthy 3.0% year-on-year to 360,600 tonnes. Beef and veal and pork production should also grow by 8.7% and 2.5% to reach 307,000 tonnes and 1.9mn tonnes respectively. Despite going through hard times over recent years with disease outbreaks, soaring input costs and competition from cheap imports, we expect Vietnam's livestock production to see strong growth, led by pork production, over the medium term. This is because rising incomes will stimulate domestic meat consumption growth

(due to diet diversification) and production will increase to keep pace. That said, we foresee the country to continue being a net importer of livestock over our forecast period. We further elaborate on the challenges facing the sector below. As a result, we expect poultry production to rise by 19. 8% to 419, 300 tonnes over our forecast period to 2014/15 and for pork production to grow 15. 1% from its 2010 level to 2. 2mn tonnes over the same period. The country will still remain reliant on pork imports to satiate demand. Beef production will remain the least significant of Vietnam's livestock sectors, but will also see good growth over our forecast period, with production expected to rise by 52. 6% to 430, 700 tonnes. BMI Demand View: Meat consumption in Vietnam has risen significantly over the last decade, with percapita consumption rising by 86% from 1999 to 2009 to reach 28kg per year. Once again, buoyed by strong income as well as population growth, we see healthy demand growth for livestock over the forecast period to 2015. Poultry consumption will see the strongest growth at 54. 9% to 895, 000 tonnes, while pork (from a higher base) and beef consumption will increase by 15. 4% and 41. 5% respectively. Indeed, we foresee pork consumption to reach 2. 2mn tonnes, while beef consumption will reach 766, 800 tonnes. BMI foresees pork consumption to continue being the dominant meat consumed, comprising more than 60% of total meat consumed. Indeed, a household survey done in 2010 revealed that 40% of household meat expenditure comprised of pork, with preference given to fresh pork, as compared to chilled or processed meat. Table: Vietnam Poultry Production & Consumption, 2010-2015

	2010	2011f	2012f	2013f	2014f	2015f
Poultry Production, '000 tonnes	350. 00	419. 30	419. 30	419. 30	419. 30	419. 30
Poultry Consumption, '000 tonnes	360. 00	360. 00	360. 00	360. 00	360. 00	360. 00

60 376. 70 392. 10 406. 40 419. 30 577. 90 628. 50 695. 20 762. 40 829. 20 895. 00 1 Notes: BMI forecasts. Sources: USDA, BMI. © Business Monitor International Ltd Page 14 Vietnam Agribusiness Report Q4 2011 Table: Vietnam Pork Production & Consumption, 2010-2015 2010 Pork Production, '000 tonnes Pork Consumption, '000 tonnes f 2013f 2014f 2015f 1, 930. 95 2, 005. 76 2, 065. 36 2, 119. 86 2, 168. 70 1, 918. 83 1 2012f 1, 884. 40 1 2011f 1, 958. 38 2, 027. 46 2, 093. 24 2, 155. 34 2, 213. 33 1 Notes: BMI forecasts. Sources: USDA, BMI. Table: Vietnam Beef & Veal Production & Consumption, 2010-2015 2010 Beef & Veal Production, '000 tonnes Beef & Veal Consumption, '000 tonnes f 1 2012f 2013f 2014f 2015f 282. 30 1 2011f 307. 00 336. 00 364. 60 396. 10 430. 70 542. 00 568. 20 619. 20 669. 60 718. 90 766. 80 1 Notes: BMI forecasts. Sources: USDA, BMI. Livestock Industry Faces Crucial Challenges In Medium Term The Vietnam's commercial animal feed sector has grown at an annual rate of about 16% between 2005 and 2009, according to the Ministry of Agriculture and Rural Development. This reflects the strong growth in livestock production in the country. We estimate that poultry and beef production grew 8. 7%, 17. 6% and 28. 3% respectively during the same period, boosted by consolidation of the industry and increased industrial production of meat. This year alone, the livestock industry aims to raise its production value by 7. 5-8%, and at the same time, increase the ratio of livestock production from the current 28% to 30% of Vietnam's total agricultural output. While we are largely optimistic about the growth prospects for this industry - we forecast production output of poultry, pork and beef to grow by 19. 8%, 15. 1% and 52. 5% respectively over our five-year forecast period - there are salient downside risks to this

outlook. We highlight the three main challenges as high interest rates, a reliance on imports (which causes the livestock industry to be vulnerable to fluctuating input prices), and finally, the fragmented nature of the market. © Business Monitor International Ltd Page 15 Vietnam Agribusiness Report Q4 2011 Growing Poultry Deficit Vietnam - Selected Livestock Estimates, 000 tonnes Source: BMI High Interest Rates Push Loans Out of Reach For Farmers Although it is mandatory for local banks to prioritise agricultural loans as ordered by the central bank, the higher cost of loans this year led farmers to put off borrowing to expand their farms. According to reports, many pig farmers were badly in need of capital, but the banks had yet to provide them any support, while they had to cope with rising input costs. This year alone, the State Bank of Vietnam has hiked interest rates five times, almost doubling the rate from 7.5% early this year to the level of 14% as of mid-September. Agriculture loans are between 16.0% and 21.5%, which are still considerably higher than previous years. For example, branches of the Vietnam Bank for Agriculture and Rural Development in some Mekong Delta provinces have also announced lending rates of 18-19.5% a year for agricultural households. With farmers being squeezed by rising input costs, higher interest rates are likely to curb expansion of domestic farms and place a strain on pork production in the short-to-medium term, especially after the foot-and-mouth disease and blue ear disease epidemics, which significantly damaged the pork industry in 2009 and 2010. Nevertheless, given BMI's expectations for monetary easing to come in H112 (see 'Inflationary Pressures Remain Stubborn But Disinflation View Still In Play', August 29), lower policy rates in 2012 could mitigate some of the production

constraints faced by livestock farmers in 2011. Reliance On Imports Increases Vulnerability To Price Fluctuations Given that the dependency on imports of grains is expected to continue growing over the long term, this dynamic makes local livestock farmers highly vulnerable to fluctuations in international grain prices, © Business Monitor International Ltd Page 16

Vietnam Agribusiness Report Q4 2011 which contributes 70% in producing animal feed. Import dependency for corn, for example, rose from 5. 2% in 2005 to 19. 0% in 2010. According to the Vietnam Animal Husbandry Department, animal feed manufacturers have increased their prices up to a dozen times since early 2011, pushing current prices 40% higher year-on-year. Higher animal feed costs, coupled with a shortage in output, have pushed the prices of live pigs up by 70% to 100% since the start of 2011, costing VND64, 000-70, 000/kg. With consumption of meat growing steadily in Vietnam as incomes rise, we also expect imports of grain for animal feed to continue increasing. Unless the government boosts domestic production of these grains or improves storage conditions, the country should remain largely vulnerable to grain price fluctuations in the coming years. Increasing Domestic Feed Production Vietnam - Imports of Soybean, Soymeal & Corn Feed, 000 tonnes Source: USDA, BMI Fragmented Domestic Feed Industry Disadvantages Local Companies To Foreign Players The domestic livestock industry is made up of mainly small-scale or backyard farm operations, which have poor hygiene standards and are susceptible to epidemics. The Vietnamese livestock sector is constantly plagued by disease outbreaks due to a lack of proper sanitation facilities in farms and meat production facilities. Since 2009, the country's livestock sector has experienced multiple rounds

of avian influenza, H5N1 bird flu virus, foot-and-mouth disease and porcine reproductive respiratory syndrome, also known as blue ear disease. Disease outbreaks will constantly feature as a challenge to the industry as long as it remains fragmented and low in technology and health standards. © Business Monitor International Ltd Page 17 Vietnam Agribusiness Report Q4 2011 The fragmented nature of the industry has thus resulted in foreign companies, with their sophisticated and larger scale production facilities, dominating livestock production in Vietnam. In the poultry sector, for example, the three main companies dominating the landscape are China-based CP Vietnam Livestock Corporation, Indonesia-based Japfa and Malaysian company Emivest, supplying around 6mn chickens to the domestic market monthly, leaving hundreds of domestic firms to compete for the remaining market share. Changing Meat Consumption Trends Vietnam - Livestock Consumption By % Source: BMI It is estimated that approximately 20 of the foreign-owned feed companies control almost 70% of the Vietnamese animal feed industry and similar significant shares in the poultry and pork industry. According to reports, 30% of domestic firms have been forced out of the animal feed business as a result. Another advantage that foreign firms enjoy in the sector is that they are not subject to the high lending costs that local farmers have to pay. Being able to rely on their parent companies also allows these foreign players to dig into deep pockets and purchase raw materials at lower costs in foreign currencies. H5N1 Virus Mutation Renders Vaccination Ineffective According to reports, a 'new type' of H5N1 bird flu virus has been found circulating the northern, coastal, and central regions. The Animal Health Department has, since 2010, been vaccinating animals found with the H5N1

virus but recent post-vaccination results suggest that the disease has mutated such that the vaccine has been rendered ineffective. Given the small area in which the disease has been reported, we do not think that the outbreak will spread to a national level though a prolonged outbreak should increased imports of the meat in the medium term. © Business Monitor International Ltd Page 18 Vietnam Agribusiness Report Q4 2011 Diseases Make Their Way Through Livestock Sector Poultry In common with many countries in the region, Vietnam battled with repeated Outbreaks of highly pathogenic avian influenza (HPAI) in the first few months of 2009.

Occurrences were reported across the country and by the end of March, three people had died of the disease. While the hot season in May should have seen a fall in outbreaks, the wide geographic spread of the disease was worrying. At the end of June, Vietnam was still not completely free of the disease, though most of the country had passed the 21-day period without infection to be declared clear. An outbreak in the northern province of Quang Ninh at the end of June saw 500 birds die and another 1, 300 culled. In mid-July, this was the only province yet to be declared avian flu free. With the start of the cool season in November, HPAI returned to Vietnam after being absent since June following the first incident in the northern province of Lai Chau which saw the culling of almost 2, 000 birds. Outbreaks continued across the country through December. Unless effective measures can be put in place to stop the return of the disease every cool season, it will continue to be a major threat to the country's poultry producers. International help has been offered with the FAO pledging US\$7mn to help the country improve preparedness. However, efforts are being hampered by the opaque nature of

officialdom in the country with reports of government vets exaggerating the number of animals vaccinated to claim vaccination fees. The prevalence of small-scale 'backyard' poultry producers also makes implementing an effective system difficult. Indeed, the flu is continuing to hurt farmers, as six separate outbreaks were reported in August 2010, leading to the deaths of over 6, 000 birds. Cattle & Hogs After experiencing a round of foot-mouth disease outbreak amongst the poultry population in H109, the same disease made a comeback in December 2010 and is still present at the time of this writing. In all, a total of 18, 500 animals (mostly cattle) have been vaccinated to prevent the disease from spreading and reports of infected animals have emerged in 19 cities and provinces across the nation, with a total of approximately 700 buffaloes, cows and pigs reportedly affected. Vietnam's pork sector is no stranger to disease either. Since the start of 2010 to October, as many as 105, 023 pigs had been infected with the Blue Ear Disease (porcine reproductive respiratory syndrome; PRRS) with the government slaughtering almost half of them to prevent further spreading. To aid the farmers, the government gave out approximately US\$1. 30 per animal lost. Despite this, the disease has spread to 21 other provinces in a month (mostly in southern areas of the country), including Dong Nai and Binh Phuoc, Nghe An, Cao Bang, Soc Trang, Quang Tri, Tien Giang, Lao Cai, Long An, Binh Duong, Bac Lieu, Quang Nam, Dong Nai, Binh Phuoc and Da Nang. Indeed, the spread of the disease has prompted local authorities to label the disease a pandemic. In an effort to stop

© Business Monitor International Ltd Page 19 Vietnam Agribusiness Report Q4 2011 the advance of the disease, local authorities have urged farmers to slaughter sick pigs

immediately. The authorities have also called for tighter transport restrictions to keep the disease contained.

Table: Vietnam Poultry Production & Consumption, 2006-2011

	2006	2007	2008	2009	2010	2011
Poultry Production, '000 tonnes	344.00	350.00	340.00	350.00	360.60	370.00
Poultry Consumption, '000 tonnes	460.00	545.00	530.00	577.90	628.50	628.50

Table: Vietnam Pork Production & Consumption, 2006-2011

	2006	2007	2008	2009	2010	2011
Pork Production, '000 tonnes	1,713.00	1,832.00	1,850.00	1,850.00	1,884.40	1,930.95
Pork Consumption, '000 tonnes	1,731.00	1,855.00	1,880.00	1,894.00	1,918.83	1,958.38

Table: Vietnam Beef & Veal Production & Consumption, 2006-2011

	2006	2007	2008	2009	2010	2011
Beef & Veal Production, '000 tonnes	230.00	240.00	250.00	260.00	282.30	307.00
Beef & Veal Consumption, '000 tonnes	258.00	329.00	448.00	509.00	542.00	568.20

Notes: BMI forecasts. Sources: USDA, BMI.

Risks To Outlook Disease poses a major downside risk to our forecasts for livestock production in Vietnam. It is a particular risk for our poultry and pork output forecasts, although it could also affect our beef sector outlook. A reduction in consumer spending, as a result of the return to more normal fiscal and monetary policy could adversely affect livestock consumption growth. Prolonged demand sluggishness would also weigh on production growth, removing as it would one of the key incentives currently available to domestic production.

Competition from cheap imports remains a risk to Vietnamese livestock farmers. Efficiency improvements are being made - as demonstrated by our robust production forecasts - and yet this risk might only be fully realised

beyond 2012 once government intervention is reduced. © Business Monitor International Ltd Page 20 Vietnam Agribusiness Report Q4 2011 An upside production risk is continued government investment. If the sector continues to get investment from the government, the ensuing efficiency increases could pose upside risks to our forecasts. © Business Monitor International Ltd Page 21 Vietnam Agribusiness Report Q4 2011 Vietnam Coffee Outlook BMI Supply View: Vietnam's coffee sector has grown significantly over the last 20 years, with yields doubling, while the area planted has expanded from 42, 000 hectares to over 509, 000. Vietnam is the world's biggest producer of robusta coffee, with more than 95% of its coffee output consisting of the cheaper bean and only around 2-3% of production devoted to the premium Arabica variety. The Vietnamese coffee market year runs from October to September, and harvesting takes place between November to February. With the 2010/11 coffee harvest season over, we now turn our attention to the 2011/12 crop, for which BMI forecasts a 9. 0% year-on-year (y-o-y) increase in production to 21. 0mn bags. The main driver for this bullish forecast will be higher yields, as higher local prices encourage farmers to re-invest profits from the previous crop to improve the next harvest. Local coffee prices have risen by more than 100% yo-y at the time of this writing. As a result, farmers are reportedly beginning to purchase more fertiliser and farming equipment such as water pumps. However, bringing new land into cultivation will be restricted, as according to the Vietnam Coffee and Cocoa Association (Vicofa), new seedlings and new land are limited. There is a high likelihood that yields could push past 2010/11 yields of 2. 1 tonnes/hectare. Out to 2014/15, we expect production growth of 27. 5% to 24. 3mn bags as the

Vietnamese government endeavours to increase the replanting of coffee trees. However, in mid-2009, farmers were still investing in expanding the area under production rather than replanting existing trees. Work on replacing trees, many of which are more than 20 years old, will improve disease resistance and thus yields in the long term. Another growth driver will be export opportunities, given that Vietnam is also the world's largest exporter of robusta coffee. While the newly-approved national coffee stockpiling scheme is aimed to smooth out domestic price fluctuations in the coffee market over the long run and ensure a steady supply of coffee beans, we note that the results of the program have not shown any indication of its success since its implementation in January. BMI Demand View: Vietnam's population is predicted to grow by 5. 0% from 2010-2015 and its GDP is forecast to rise at an average rate of 7. 2% annually to the end of the forecast period. As GDP and population rise, spending on food and drink items like coffee should also increase. Increasing urbanisation and the spread of Western-style coffee shops should add to this trend. Indeed, coffee consumption grew impressively by 41. 4% from 0. 58kg/capita in 2006 to 0. 82kg/capita in 2009, one of the highest growth rates out of all coffee-exporting countries over the period. We predict that consumption will rise 8. 0% in 2011 to 1. 1 bags. That said, we note that coffee consumption growth comes from a relatively low base and we foresee 54. 2% growth to reach 1. 6mn bags over our forecast period to 2015. The Ministry of Agriculture and Rural Development (MARD) has said it hopes to boost domestic consumption to 10-15% of the national coffee crop. We do not believe this will be achieved in our

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Report Q4 2011 forecast period, but the existence of such a sizeable target underlines the apparent potential of domestic consumption. Table: Vietnam Coffee Production & Consumption, 2010-2015

	2010	2011f	2012f	2013f	2014f	2015f
Coffee Production, '000 60kg bags	19,083.70	19,282.87	21,019.26	22,050.02	23,151.20	24,327.87
Coffee Consumption, '000 60kg bags	1,017.19	1,102.57	1,207.85	1,320.30	1,440.42	1,568.78

Notes: BMI forecasts. In all instances year indicates data for harvest year ending that calendar year i. e. 2011 = 2008-09; Sources: USDA, Vietnam Coffee and Cocoa Association, BMI. USDA, BMI. Vietnamese Coffee Export Contract Cancellations Keep Market Tight With the domestic coffee supply crunch expected to persist until the 2011/12 crop starts to come online in early October, we believe these developments should offer some support to prices in the near term. Coffee exports in June totalled 80,000 tonnes, 15.8% lower on a year-on-year basis, and July exports are estimated to have reached 55,000 tonnes, representing a 38.2% dip from a year ago. A reason for the shortage is the fact that farmers had sold close to 90% of the harvested 2010/11 crop on the back of surging prices at the start of 2011, leading to a year-on-year surge of exports by 21.7% for the first five months of the year. Approximately 40,000 tonnes of coffee deliveries have already been cancelled for July delivery. According to reports, there is about 200,000 tonnes of coffee, or only approximately three months' worth of coffee exports currently kept under storage in warehouses in Vietnam. Vietnam contributes to about 15% of all global (mainly robusta) coffee production. While Vietnamese coffee exports are seasonally lower in Q2 and Q3, we note that exports of the commodity in June and July have fallen below the five-

year average, underscoring the severe scarcity of the bean in the local market. This development, coupled with our recent downgrade of the Indonesian coffee crop (see 'Lower Indonesian Coffee Output To Tighten Robusta Export Markets', July 21), should keep the robusta coffee market tight and could serve to restrain recent moderation in global coffee prices. Looking ahead, we maintain our forecast for the 2011/12 coffee crop to post strong growth of 9. 0% to reach 21. 1mn tonnes. Despite expectations of a bumper crop, we do not rule out the possibility of a replay of this export crunch next year. This is so as domestic prices are still prone to fluctuations, and as farmers are heavily leveraged, sharp swings in prices (as was the case this year) could lead to another situation where farmers sell off more of their crops than they should before the next harvest. Coffee Hoarding Causing Delay In Shipments, Likely to Support Prices Thinning Vietnamese coffee stocks could keep global coffee prices supported in the short term after having sold off considerably in recent trading. According to reports, about 100, 000 tonnes of coffee shipments due for May delivery have been delayed due to shortages of domestic supply. This represents approximately 10% of the country's total coffee exports, based on last year's overall export volume. © Business Monitor International Ltd Page 23 Vietnam Agribusiness Report Q4 2011 A reason for the shortage is because farmers reportedly sold close to 90% of the harvested 2010/11 crop on the back of surging prices at the start of 2011, leading to a year-on-year surge of exports 21. 7% for the first five months of this year. Domestic hoarding of remaining coffee stocks is a major reason for the lack of supplies for exports. F. O. Licht reports that an alleged 2. 5-4. 1mn 60kg bags (150, 000-246, 000 tonnes) are being

withheld by 'rich farmers' in anticipation of higher prices. As a result of these, local exporters have turned to purchasing beans from foreign trading houses at a premium. There are also fears that these developments could have led to a dearth in coffee exports in June and July to between 65, 000 tonnes and 80, 000 tonnes per month. Coffee exports for those two months came in at 100, 000 tonnes and 95, 000 tonnes respectively in 2010. Given that Vietnam contributes to about 15% of all global coffee production, a significant fall in robusta shipments out of Vietnam should be supportive of international coffee prices in the near term. We note that the correlation between Vietnamese domestic coffee prices in Dak Lak, a major coffee-growing region, and LIFEE Robusta coffee prices broke down considerably, with the Dak Lak/LIFEE Robusta ratio recently reaching a peak. We believe that these dynamics should provide upside risk to our currently bearish view on global coffee prices.

Increasing Foreign Competition According to Vicofa, local exporters are facing increasing competition from foreign players in securing coffee bean stocks to be shipped out of the country. Larger foreign players are currently allowed to invest only in cultivating, processing and preserving coffee for export, as well as 'the transfer of advanced technology'. However, anecdotal evidence suggests that these companies have also been setting up unofficial networks to buy coffee stocks for export, thus depriving local exporters of coffee bean supply. BMI believes that any measure to curb such activity will only be a temporary solution. The fragmented structure of the industry results in local companies being less competitive than larger foreign companies in terms of economies of scale and the ability to take out business loans. We believe a greater consolidation

of the local industry and better development of networks between exporters and farmers is needed, especially once the coffee market eventually opens up to foreign wholesalers in accordance with World Trade Organisation commitments. © Business Monitor International Ltd Page 24 Vietnam Agribusiness Report Q4 2011 Vietnam Catching Up Brazil, Colombia, Indonesia, And Vietnam % Of Global Coffee Exports Note: f = forecast, Source: USDA Domestic Demand Could Soar But Poor Business Landscape Undermines Potential While the vast majority of Vietnam's coffee will be destined for the export market for a long time to come, we expect domestic consumption to rise rapidly in the coming years. A 2009 survey by the Policy and Strategy Institute on Agriculture and Rural Development on coffee drinking habits in Hanoi and Ho Chi Minh City clearly reinforces this trend. Results showed that coffee consumption was highest among the young and the well-educated living in urban areas and lowest among the elderly and in rural areas. Consumption was also far higher in the south than in the north. The US Department of Agriculture has also noted that 'domestic consumption has been increasing due to the effective marketing strategies of domestic coffee companies.' Having said that, BMI notes that other factors undermine this otherwise positive picture. © Business Monitor International Ltd Page 25 Vietnam Agribusiness Report Q4 2011 Table: Vietnam Coffee Production & Consumption, 2006-2011

	2006	2007	2008	2009	2010	2011f
Coffee Production, '000 60kg bags	16,335.00	19,500.00	18,000.00	16,980.00	19,083.70	19,282.87
Coffee Consumption, '000 60kg bags	1,216.33	1,500.00	1,800.00	1,950.00	1,017.19	1,102.57

Notes: BMI forecasts. In all instances year indicates data for harvest year ending that calendar

year i. e. 2011 = 2 3 2008-09; Sources: USDA, Vietnam Coffee and Cocoa Association, BMI. USDA, BMI. Risks To Outlook Higher lending rates could be a downside risk to crop yield improvements. According to a report by the State Bank of Vietnam, the financing rates for agriculture and rural areas increased by 14. 5%-17. 0% per year in 2010. However, we do not think that this is a significant downside risk because the agriculture sector traditionally receives a significant amount of government support, and lending to the agriculture sector is considered relatively low risk compared with other sectors. Indeed, credit tightening should only limit farmer investment to a small extent. With Vietnam's coffee industry so dependent on exports, our forecasts for production will be heavily dependent on world demand and prices for robusta coffee. BMI is expecting prices to remain relatively high over the medium term, but should further demand weakness - or indeed global oversupply - cause prices to come in lower than expected, production could undershoot our growth forecast. While Vietnam's coffee consumption forecast indicates significant growth, it is coming from a low base. This highlights the fact that despite government efforts to lift local consumption, coffee remains a luxury, discretionary item. Its status leaves it exposed to any period of reduced consumer confidence resulting from government monetary normalisation or a secondary economic slowdown. Such a scenario would likely see our consumption growth forecast missed. © Business Monitor International Ltd Page 26 Vietnam Agribusiness Report Q4 2011 Vietnam Dairy Outlook BMI Supply View: Vietnamese dairy consumption has expanded significantly in the last 15 years, driven by relatively large increases in domestic consumption, as well as rising incomes which have

fostered increased milk consumption. In fact, per-capita milk consumption in Vietnam has virtually doubled between 2000 and 2009 to 12kg per person per year. Despite this increase, the country remains below the regional average of 65kg. Though there has been an increase in milk production over the years, the country produces neither cheese nor butter. Condensed milk and yoghurt are also highly popular dairy products in the country. We expect the country to be increasingly reliant on dairy imports to meet its domestic needs. In 2010/11 we foresee milk production growth of 7. 2% to reach 315, 500 tonnes. Out to 2014/15, we are forecasting Vietnamese fluid milk production growth of 39. 5% to 410, 700 tonnes. Dramatic increases in cattle numbers and increased public and private sector investment, in an effort to reduce the country's growing import dependency, will be the main boost to strong growth. Commercialisation will also play a key role, as larger, more efficient farms come to play a greater part in total milk production. A sustained period of high global milk prices - thanks to rising global demand and supply sluggishness - will also prove production-supportive and encourage producers to be more long-term in their approach to cattle farming. Finally, the sector should benefit from the continued increase in yields, which have been rising over the last decade by almost 130% and should continue to do so given the new private investments in the sector.

BMI Demand View: Vietnamese dairy consumption growth will remain strong over our forecast period to 2015. Strong economic growth will filter through into rising disposable incomes, pushing up demand for non-essential foodstuffs. Through to 2015, we expect fluid milk consumption growth of 31. 4% to 238, 600 tonnes, while demand for butter, cheese and whole milk

powder will soar 73. 1%, 192. 9% and 3. 1% respectively, albeit from a far lower base. Increased urbanisation, increased home ownership of Western goods and the ongoing spread of modern, organised retail will all prove supportive of strong dairy consumption growth, even if the forecast higher global dairy prices limits the growth outlook to some extent. Indeed, BMI's forecasts for GDP per capita growth of 114% from US\$1, 160 in 2010 to US\$2, 484 in 2015 serves to reinforce our bullish outlook. Table: Vietnam

Milk Production & Consumption, 2010-2015 2010 Milk Production, '000

tonnes Liquid Milk Consumption, '000 tonnes f 3 2011f 2012f 2013f 2014f

2015f 294. 4 1, 2 315. 5 339. 6 363. 4 387. 2 410. 7 181. 6 190. 7 198. 3

209. 7 223. 8 238. 6 1 Notes: BMI forecasts. In all instances year indicates

data for harvest year ending that calendar year i. e. 2011 = 2 3 2008-09;

Sources: General Statistics Office of Vietnam, BMI. FAPRI, BMI. © Business

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Table: Vietnam Butter Production & Consumption, 2010-2015 2010 2012f

2013f 2014f 2015f 0. 0 0. 0 0. 0 0. 0 0. 0 0. 0 11. 7 12. 8 14. 4 16. 2 18. 1 20.

3 2010 Butter Production, '000 tonnes 2011f 2011f 2012f 2013f 2014f 2015f

0. 0 0. 0 0. 0 0. 0 0. 0 0. 0 4. 4 5. 3 6. 7 8. 3 10. 3 12. 8 1 Butter

Consumption, '000 tonnes f 1 1 Notes: BMI forecasts. Sources: FAPRI, BMI.

Table: Vietnam Cheese Production & Consumption, 2010-2015 Cheese

Production, '000 tonnes 1 Cheese Consumption, '000 tonnes f 1 1 Notes: BMI

forecasts. Sources: FAPRI, BMI. Table: Vietnam Whole Milk Powder Production

& Consumption, 2010-2015 2010 Whole Milk Powder Production, '000 tonnes

Whole Milk Powder Consumption, '000 tonnes f 1 2012f 2013f 2014f 2015f 0.

0 1 2011f 0. 0 0. 0 0. 0 0. 0 0. 0 33. 2 34. 8 34. 6 34. 4 34. 3 34. 2 1 Notes:

BMI forecasts. Sources: FAPRI, BMI. Consumers Struggling With High Milk Prices Consumers will be confronted with higher dairy product prices, especially milk powder prices in the medium term. Anecdotal reports in late March 2011 claimed that prices of imported milk products such as milk powder had risen by 18% on the back of an 8.5% Vietnamese Dong devaluation. Accor