

Fixed-income Perspectives

Excess liquidity to set lower-interest-rate environment

ON rate to reduce

Interbank market in June recorded a slight increase in interest rate, providing more evidence that the super-low interest rate environment existing in the pandemic era would be over. Lending costs for loans generally increase for short tenors, including ON and 1-week, while interest rates for longer terms, such as 2-week, 1-month, move in the opposite directions. For July, we predict that the ON rate to reduce due to the slower lending activities and the excessive short-term liquidity in the banking system coming from the government relief package of VND26tn.

Bond yields to find new record lows

Statistics in June pointed out demand for G-bond was gaining steam as the G-bond trading returned to its high level that was seen in late-2020. Increasing demand again helped to push medium-term and long-term yields to nearly their all-time lows, just a few basis points above. However, looking forward to July, we expect that high demand for G-bonds is not likely to persist under the currently low-yield levels, as investors are signaling of being cautious with G-bond investment in the primary market. As a result, we forecast the G-bond yields would remain around the low levels for a while or even increased somewhat.

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KIS leading economic index

(USD bn, %, % QoQ, % YoY)

	1Q20	2Q20	3Q20	4Q20	2019	2020	2021F
GDP	3.82	0.36	2.62	4.48	7.02	2.91	5.94
Trade balance	3.82	1.92	10.72	2.54	10.42	19.01	1.77
CPI	4.87	3.17	2.98	0.19	5.23	3.24	2.41
Discount rate	3.50	3.00	3.00	3.00	4.00	3.00	3.00
VND/USD	23,264	23,206	23,188	23,252	23,231	23,255	23,246
US GDP	(4.80)	(34.20)	NA	7.90	2.3	(5.70)	3.90
China GDP	(6.80)	1.10	NA	6.00	6.10	1.80	8.00

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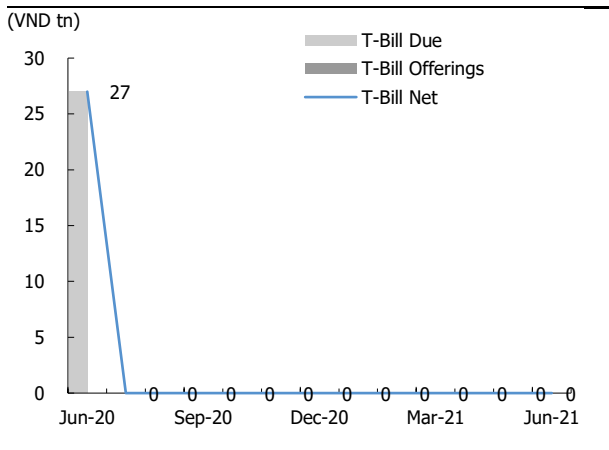
I. OMO records no transactions

No transaction recorded in the OMO

OMO in June recorded further a month with no transaction between SBV and its counterparties when the local outbreak became severe. The stability of the liquidity in the banking system allows the central bank to hold its tools, although the super-low interest rate environment in the money market seems to end. The current interest rate corridor is still effective when the interest rate applied for collateral loans to commercial banks was unchanged at 2.50%, 137bps-higher than the ON value at the end of this month.

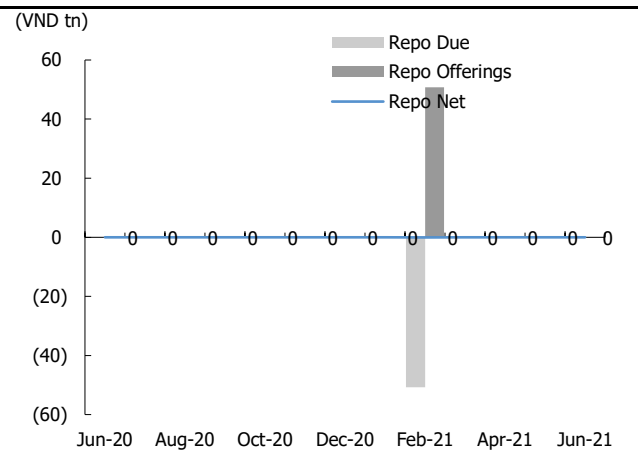
The surging number of infected cases and the new virus variants slow the economic recovery, limiting domestic demand and production to return to the full scale before the pandemic. We forecast that this outbreak would reduce the lending activities in the first lending market and sustain the short-term liquidity to abundant.

Figure 1. T-bill transaction



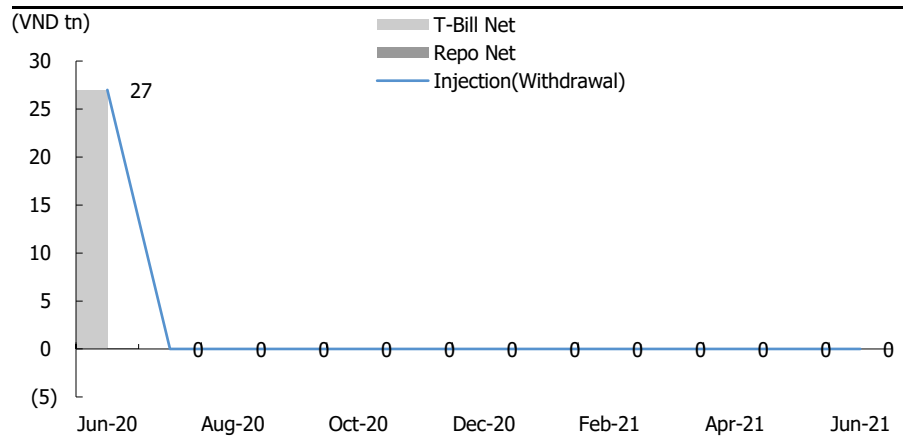
Source: Bloomberg, SBV, KIS

Figure 2. Repo transaction



Source: Bloomberg, SBV, KIS

Figure 3. Net Injection/Withdrawal



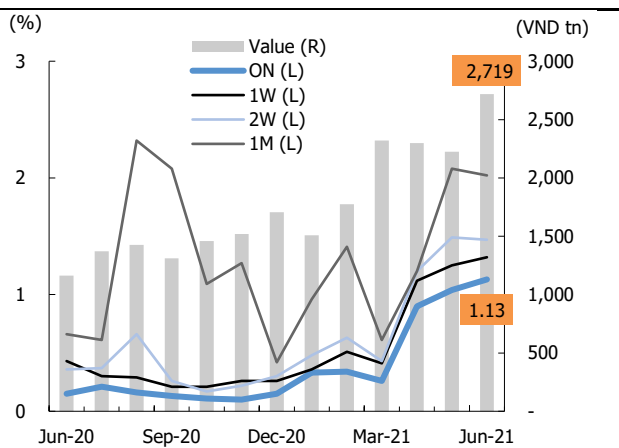
Source: Bloomberg, SBV, KIS

II. Interbank rates to reduce

Interbank market in June recorded a slight increase in interest rate, providing more evidence that the super-low interest rate environment existing in the pandemic era would be over. Lending costs for loans generally increase for short tenors, including ON and 1-week, while interest rates for longer terms, such as 2-week, 1-month, move in the opposite directions. Specifically, ON and 1-week rose to 1.13% and 1.32%, being 9bps-, 7bps-higher than respective rates in previous period. Interest rates for 2-week, 1-month, 6-month, and 9-month loans were 1.47%, 2.02%, 2.48%, and 2.9%, declining by 2bps, 6bps, 52bps, and 18bps compared to May, respectively.

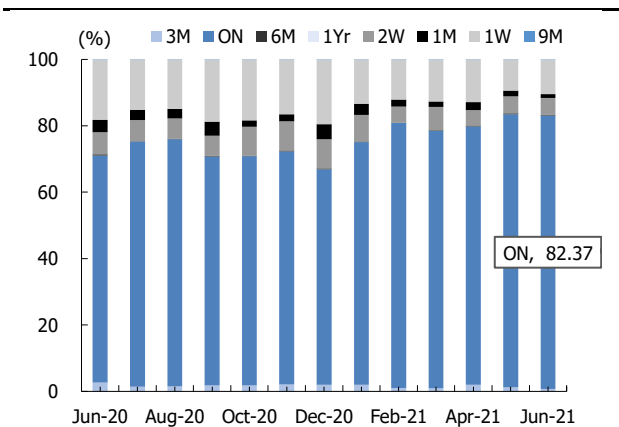
Given the increase in interest rates of short-term loans, the total trading value surged to VND2,718.94tn this month, rising by 22.24% MoM. Banks slightly increase their attention on most liquid loans, including ON and 1-week, as their share increased relative to the remaining tenors. In detail, portions of ON and 1-week increased by 0.11% and 1.04%, climbing to 82.37% and 10.39%, respectively.

Figure 4. Interbank transaction



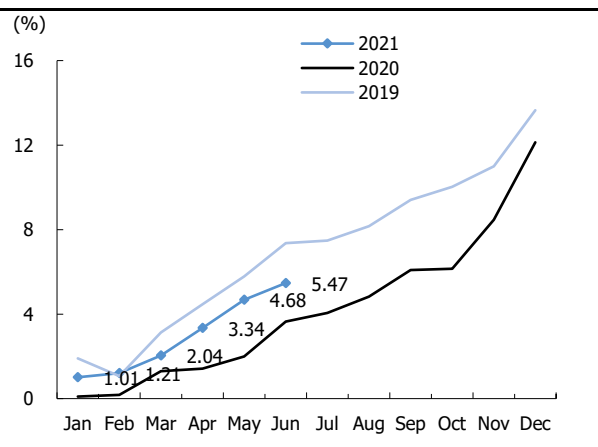
Source: Bloomberg, SBV, KIS

Figure 5. Interbank value by tenors



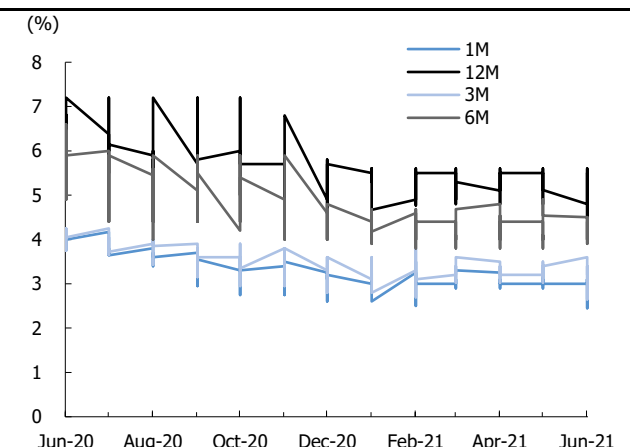
Source: Bloomberg, SBV, KIS

Figure 6. Credit growth by month-of-year



Source: Bloomberg, SBV, KIS

Figure 7. Historical deposit rates



Source: Bloomberg, SBV, KIS

PREDICTION:

There are some reasons allow our team to predict the overnight rate in the money market to reduce in the next month. Firstly, lending activities seems to grow with a slower pace this month and commercial banks continued to mobilize sources with at the low cost, suggesting that the short-term liquidity in the money market would remain abundant. Furthermore, the government has issued the relief package of VND26tn for virus-affected labors to ease the financial burden. We predict that the money would flow from the account of Vietnam state treasury (VST) to resident accounts in the banking system, providing more short-term liquidity for the interbank market in the next month.

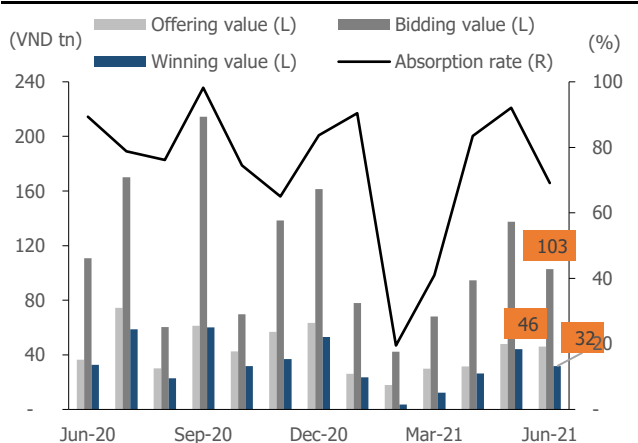
III. Bond yields to find new record lows

Government bond auctions slowed down with limited room in end-2Q21

An acceleration in the government-bond primary market in April and May seems to lose steam in June as the G-bond issuances for some tenors were limited based on the already-issued G-bond issuance plan for 2Q21 by the Ministry of Finance. On the other hand, significant drops in yields also impacted G-bond investors' appetite, in which most G-bond issuances were recorded at yields that are nearly at their record lows.

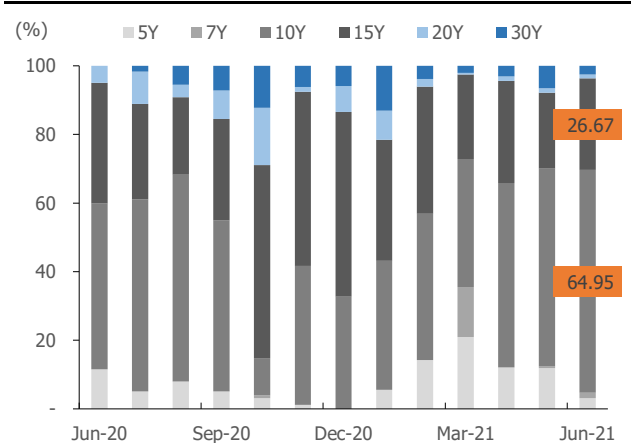
Throughout a total of 18 G-bond auctions, Vietnam State Treasury (VST) offered VND46tn G-bonds, down slightly by 4.17% compared to the prior month, mostly on 10-year and 15-year tenors (accounting for 81.5% of the total offering). From the demand side, the total bidding value recorded just VND102.7tn for all tenors (-25.3% MoM) over VND46tn G-bond offering, and the bid-to-cover ratio for all tenors fell to a 3-month low, at 2.23 times.

Figure 8. Government bond issuance



Source: HNX, KIS

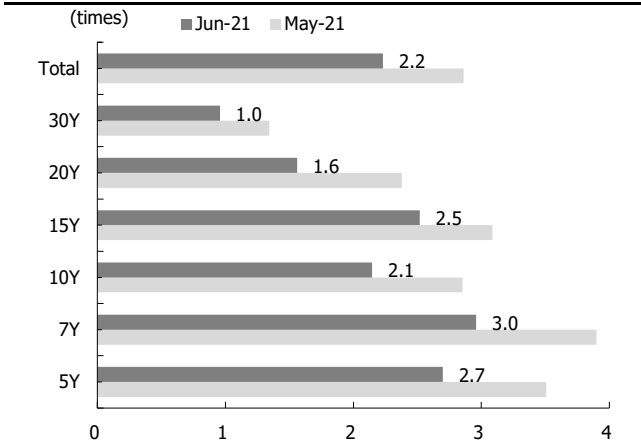
Figure 9. Issuing value by tenors



Source: HNX, KIS

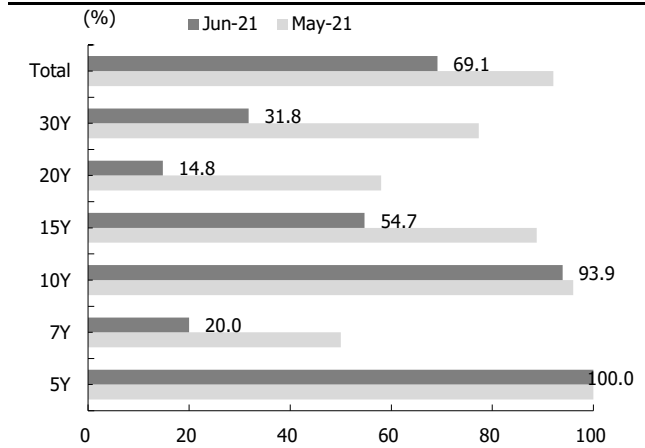
As a result, about VND31.8tn G-bonds were issued with a big discount, decreasing 32.0% compared to a 6-month high in May. The absorption rate also fell to the lowest in 3 months, at 69.1% compared to 83.5% in April and 92.1% in May, in which 5-year and 10-year G-bonds were more attractive to investors relative to other maturities.

Figure 10. Bid-to-cover ratio by tenors



Source: HNX, KIS

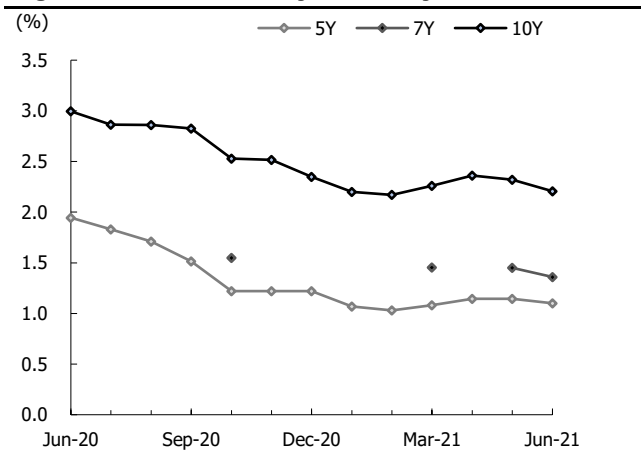
Figure 11. Absorption ratio by tenors



Source: HNX, KIS

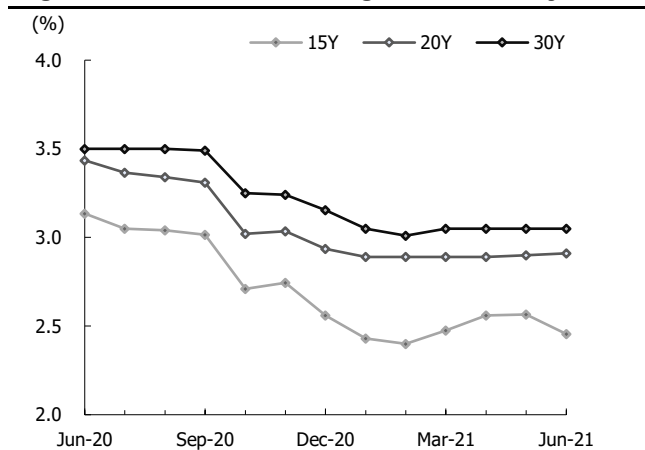
It seemed to be that a marked slowdown in G-bond demand in the auctions was just a consequence of unattractive ask yields from VST. 7-year, 10-year, and 15-year G-bond yields recorded at nearly their bottoms in late-2020, at 1.36%, 2.21%, and 2.46% and losing 9 bps, 12bps, and 12 bps compared to in May. 5-year yield also fell by 4.5 bps to just 1.1%, while 20-year and 30-year yields remained nearly unchanged.

Figure 12. Yields from 5-year to 10-year



Source: HNX, KIS

Figure 13. Yields with tenors greater than 10-years

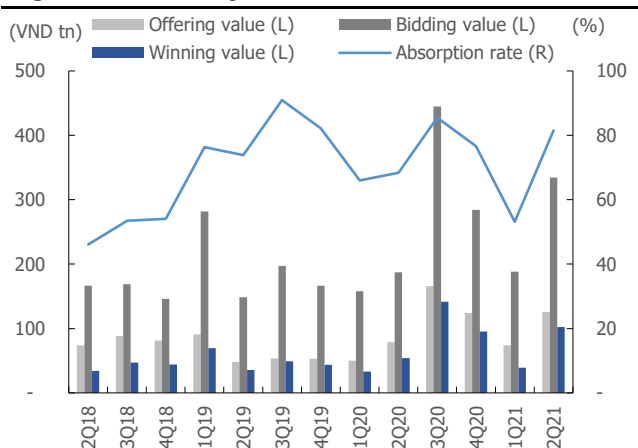


Source: HNX, KIS

Although slowing down in June, 2Q21 was still considered a successful quarter for G-bond auctions, as G-bond demand continued to be strong, which were shown by that most criteria remained nearly at their peaks. About VND125.5tn G-bonds have been offered during this quarter, which is the second-largest level in 5 years and just lower than in 4Q20. Meanwhile, the bidding value posted a total of VND334.7tn, only lower than an all-time peak in 4Q20. Similarly, the issuance value also reached over VND100tn, at VND102.3tn, for a second time

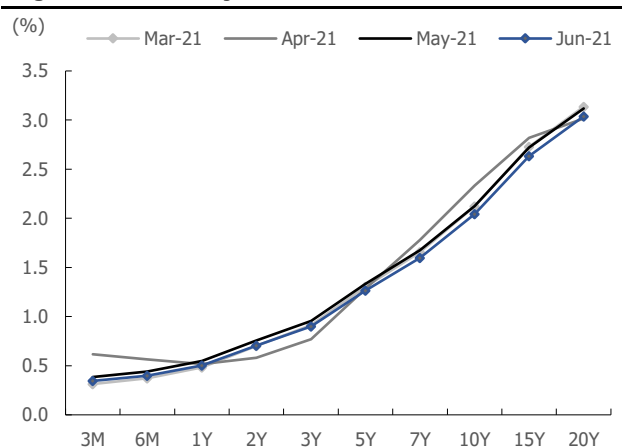
since 3Q16. The absorption ratio achieved more than 80%, at 82%, which was just lower than in 4Q20 since 2020. In the graph below, we also saw that only 10-year G-bonds successfully achieved the issuance plan for 2Q21, 72.1% higher than its target. Meanwhile, 7-year and 20-year G-bonds were far behind their targets, just completing 18.8% and 16.3%, mainly because of unattractive maturity to investors.

Figure 14. Quarterly G-bond issuance



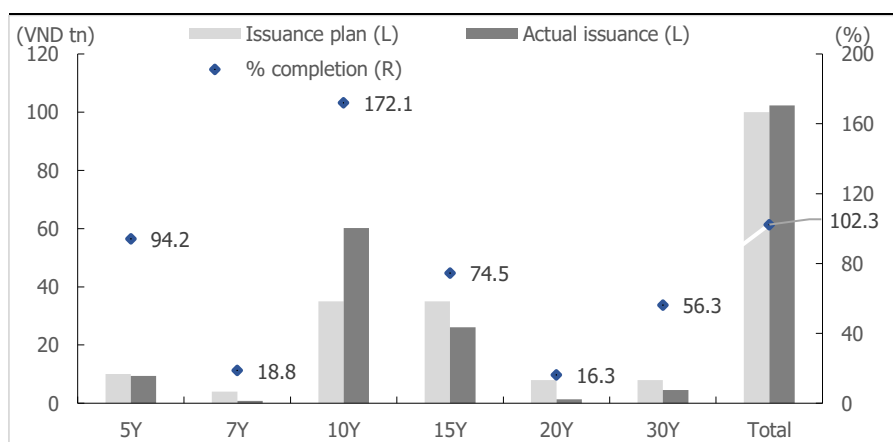
Source: HNX, KIS

Figure 15. G-bond yield movement in 2Q21



Source: HNX, KIS

Figure 16. G-bond actual issuance versus plan in 2Q21

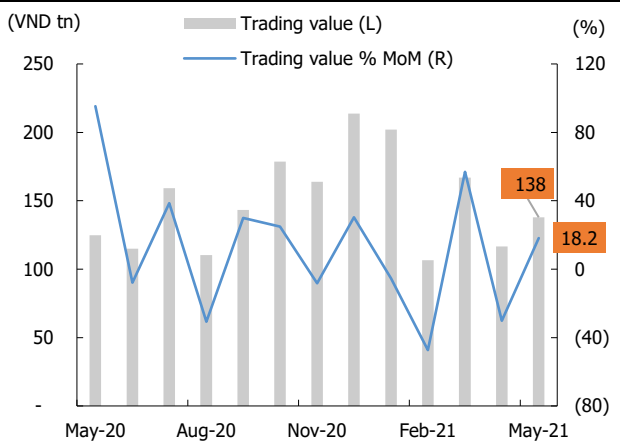


Source: Bloomberg, SBV, KIS

***G-bond trading accelerated
nearly its all-time peak***

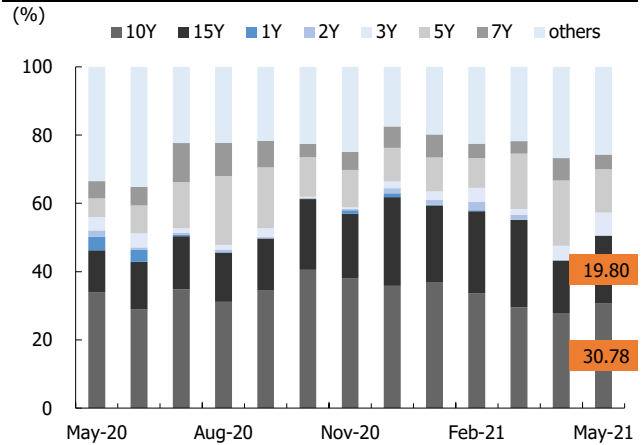
In the secondary market, data pointed out that demand for G-bond was gaining steam as the G-bond trading returned to its high level that was seen in late-2020. Total trading value accelerated to nearly an all-time peak in December 2020, at VND193.1tn and up 40.1% compared to May, marking a second month with fast-paced growth. 60% of trading activity concentrated on long-term G-bonds with maturities greater than 10 years, while about 28% was from medium-term G-bond trading (with maturities between 5 years and less than 10 years). Less than 10% of the G-bond was coming from short-term G-bonds, mostly on 3-year G-bond.

Figure 17. Trading value



Source: HNX, KIS

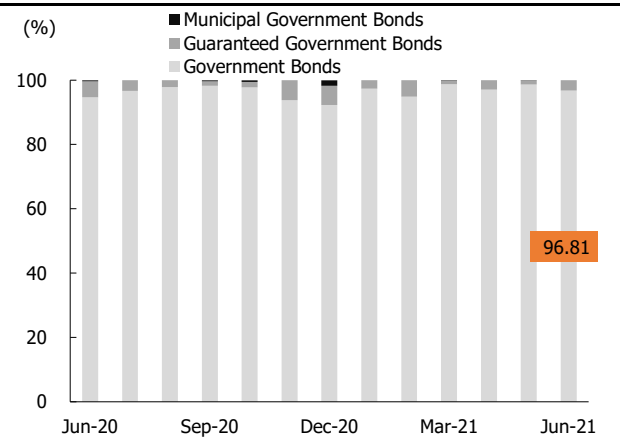
Figure 18. Trading value by tenor



Source: HNX, KIS

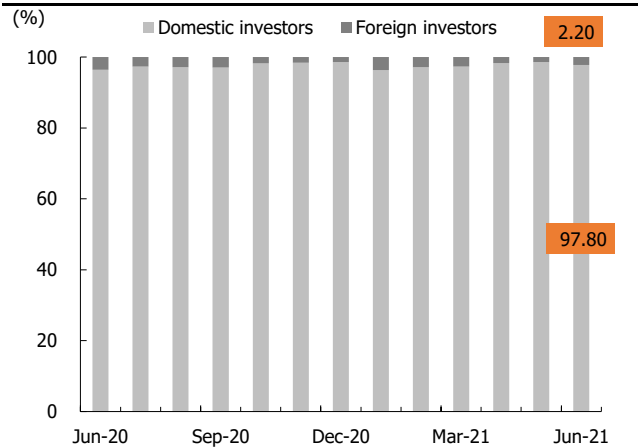
By bond type, 96.8% of the total trading value (VND186.9tn) was from government bonds, while government-guaranteed bonds accounted for just 3.2% of the total trading value (VND6.2tn). Regarding investor types, domestic investors made up 97.8% of total trading value, the remaining 2.2% was from foreign investors.

Figure 19. Trading value by bond type



Source: HNX, KIS

Figure 20. Trading value by investor



Source: HNX, KIS

Increasing demand pressures on mid-term and long-term yields

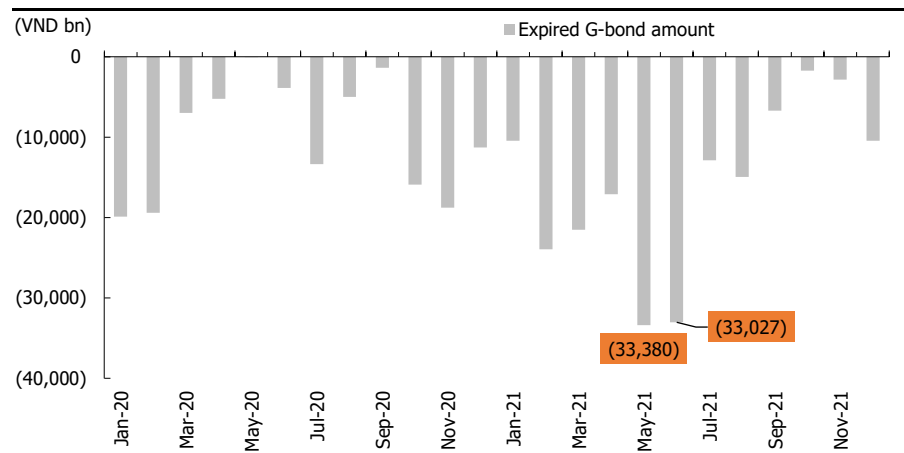
Under G-bond demand recovering to its peak, G-bond yields from short-term, medium-term to long-term maturities were being put significant downward pressure, and the latter dropped even faster. Overall, the G-bond yield curve was shifted downward from both its left tail and long tail. From our viewpoint, some potential factors were behind the downward shift in the yield curve this month.

Firstly, developments in the interbank market showed that previously tightening conditions in the banking system seemed to ease in June. From our source, term deposit from Vietnam State Treasury was back to the banking system in early June and mitigated pressure from limited banking excess liquidity. As a result, short-term bond yields with maturities less than years, which we found are highly correlated to changes in interbank lending rates, dropped somewhat by the end-June. 3-month, 6-month, 1-year, 2-year, and 3-year G-bond yields

fell about from 4bps to 6 bps to 0.35%, 0.40%, 0.50%, 0.70%, and 0.90%, respectively.

Secondly, a great amount of G-bonds expired in June, which we estimated about VND33.0tn, created a considerable demand for G-bonds to cover an equivalent amount. Besides, inflation fears in previous months have been faded away faster than anticipated as CPI was somewhat muted in contrast to most investors' expectations. A wounded economy impacted by ongoing COVID-19 outbreaks is also a favorable environment for G-bonds, as the financial markets tend to rely on safe-haven G-bonds in an uncertain time.

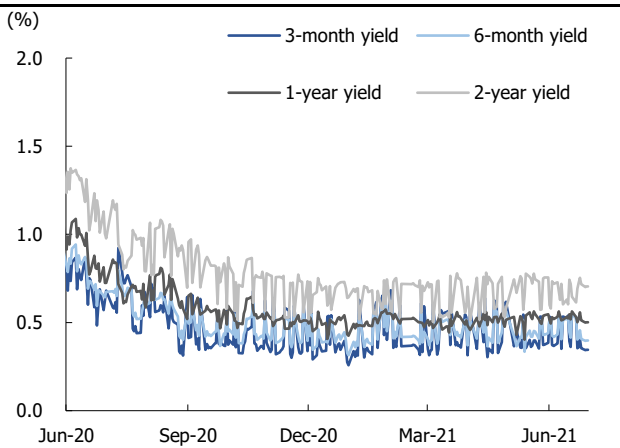
Figure 21. Estimated monthly expired G-bond amount



Source: HNX, KIS

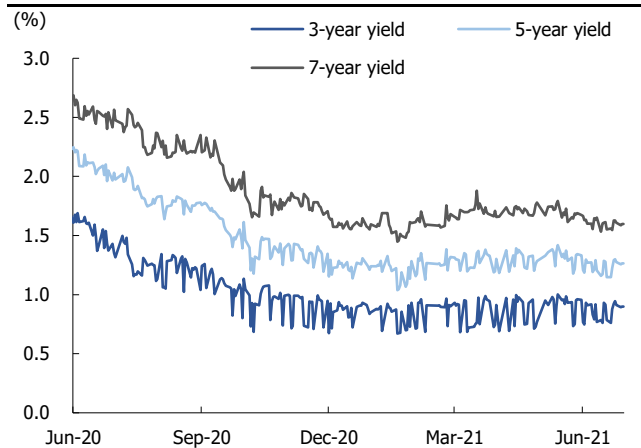
As a result, both medium-term and long-term yields also fell significantly and ended close to their troughs by the end-June. For medium-term G-bonds, 5-year and 7-year yields dropped by 6.8 bps and 7.6 bps to 1.26% and 1.60%. In the meantime, long-term 10-year, 15-year, and 20-year yields also decreased about 8.4 bps, 8.7 bps, and 8.0 bps to 2.04%, 2.63%, and 3.04%, respectively. Most noticeably, those yields were just a few basis points above their all-time lows and in the downward trend since April.

Figure 22. Short-term yields



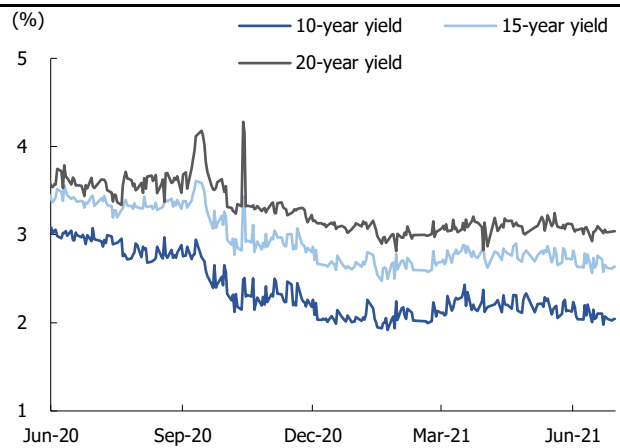
Source: HNX, VBMA, KIS

Figure 23. Mid-term yields



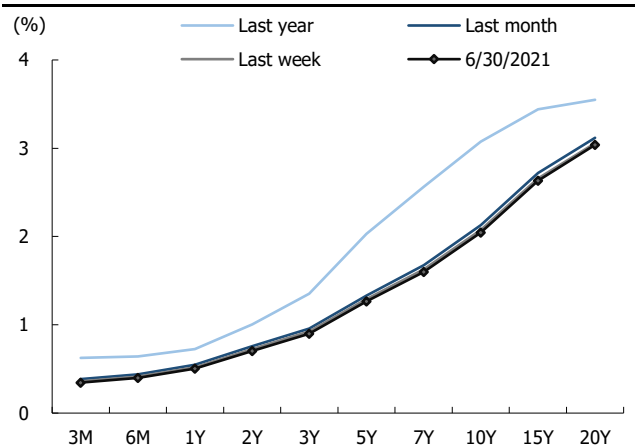
Source: HNX, VBMA, KIS

Figure 24. Long-term yields



Source: HNX, VBMA, KIS

Figure 25. G-bond yield curve



Source: HNX, VBMA, KIS

PREDICTION:

Several important points have been derived from the developments in fixed-income markets in June. First, as G-bond yields dropped considerably in the primary market, investors are signaling a decreasing demand for G-bonds. This means that the prevailing low levels in G-bonds are not likely attractive, and investors are not willing to pay any prices for their investment on G-bonds. Furthermore, as expired G-bonds were already at peaks in May and June, investors will not in pressure to purchase the government bonds in the coming months. As a result, we expect that high demand for G-bonds would not likely be sustainable in the currently low-yield environment, which in turn would ease downward pressure on medium-term and long-term yields.

Besides, in July, nearly VND100tn would be poured back to the banking system via several USD-purchasing forward contracts expired. We expect that this huge VND inflows back to banks would set a new low-interest-rate level in the interbank market like in 2H20, and pushed short-term G-bonds down in July.

IV. USD recovery hit a 5-year high

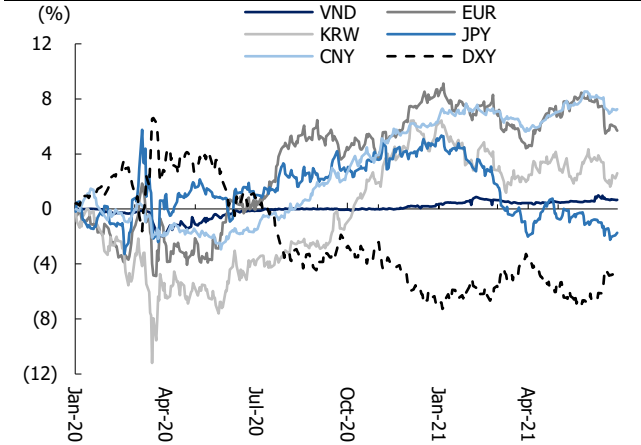
USD fast recovery pushed pressure on other currencies

After a previously two-month plunge under increasing inflation pressure, June marked the best month for USD in more than 5 years since late-2016, as the currency of the global largest economy appreciated impressively thanks to a faster-than-expected post-crisis economic recovery. By end-June, the benchmark DXY index, which measures USD value, improved by 2.47% compared to May. A big gain in USD put significant downward pressure on other currencies in our watchlist.

All four currencies in our watchlist, whose countries are large trade partners with Vietnam, saw considerable depreciation against the greenback. After two consecutive months of outperforming USD, those currencies EUR, KRW, and CNY fell significantly against USD. EUR suffered the biggest loss in the quarter with a 2.46% depreciation, while KRW and CNY lost about 1.38% MoM and 1.36% MoM against USD. Meanwhile, JPY continued to be left behind as it recorded a loss for a 5th MoM reduction over 6 months, by 0.73% MoM.

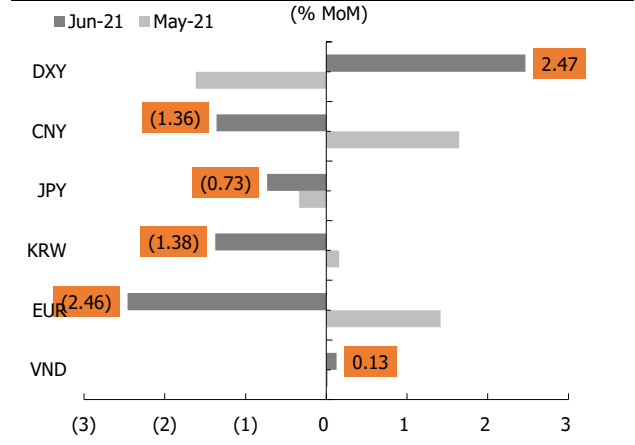
Regarding VND, under SBV adjusting its USD-purchasing price to be higher in early June, VND also saw upward pressure in the interbank market. VND marked three consecutive months appreciating against the greenback, albeit slightly by about 0.13% MoM.

Figure 26. Movements of VND, USD, CNY, KRW, JPY, and EUR



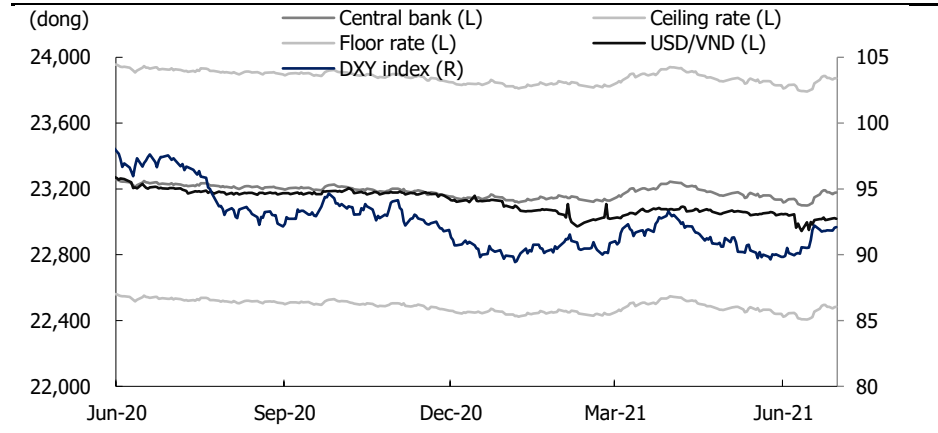
Source: Bloomberg, KIS

Figure 27. Monthly changes in VND, USD, CNY, KRW, JPY, and EUR



Source: Bloomberg, KIS

Figure 28. USD/VND rate and DXY index



Source: Bloomberg, KIS

Macro scorecard

(USD bn, USD, %, % YoY)

	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	3Q20	4Q20	1Q21	2Q21	2017	2018	2019	2020
Real GDP growth			4.48				2.62	4.48	4.65	6.61	6.81	7.08	7.03	2.91
Registered FDI	2.02	3.44	4.67	2.12	1.74	1.28	5.54	7.32	10.13	5.14	35.88	35.47	38.02	28.53
GDP per capita											2,353	2,551	2,730	
Unemployment rate											2.21	2.21	2.25	2.48
Export	28.55	20.20	29.65	26.55	26.00	26.50	79.74	80.15	77.34	79.23	215.1	243.5	263.6	282.7
Import	26.46	20.66	28.46	27.78	28.00	27.50	69.02	76.86	75.32	83.50	213.2	236.7	254.4	263.0
Export growth	55.13	(3.77)	22.89	51.00	35.51	17.28	10.61	15.14	21.76	33.50	21.82	13.19	8.16	7.02
Import growth	41.32	9.75	28.48	49.95	54.05	33.49	3.74	16.43	26.17	45.68	21.85	11.01	7.41	3.81
Inflation	(0.97)	0.70	1.16	1.16	2.90	2.41	3.81	3.24	0.30	1.23	3.53	3.54	2.79	3.24
USD/VND	23,049	23,018	23,076	23,053	23,048	23,020	23,184	23,126	23,076	23,020	22,698	23,175	23,173	23,126
Credit growth							6.10	10.14			18.24	13.89	13.70	10.14
10Y gov't bond	2.03	2.13	2.40	2.36	2.27	2.04	2.65	2.01	2.40	2.04	5.14	5.07	3.37	2.01

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