

# Fixed-income Perspectives

## An era of low-interest rates to return

### Interbank rates to lower

Interbank rates in July generally decreased with the rising traded value after an increase streak of 3 months, reflecting the abundant liquidity in the money market under the speedy transmissibility of the new Delta variant. Interest rates were reduced in many tenors except 6-month and 9-month. We predict that interbank rates to reduce further in the next month due to the slowdown in lending activities, VND26tn relief package, and the SBV's switch from forward to spot USD-buying in early August.

### Yield curve to shift to a new low territory

Government bond statistics in July showed that G-bond yields continued to decline further to near record lows. G-bond demand in the primary market saw a slight improvement, although cautiousness is still apparent under a very low-yield environment. Looking forward to August, from our view, more easing banking liquidity conditions combined with weakening credit demand would be a favorable environment for G-bond demand to accelerate. We expect the yield curve to move downward further, in which long-term yields would possibly find new record lows.

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## KIS leading economic index

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

	3Q20	4Q20	1Q21	2Q21	2019	2020	2021F
GDP	2.62	4.48	4.48	6.61	7.02	2.91	5.94
Trade balance	10.72	3.29	2.82	(3.75)	10.42	19.01	1.77
CPI	3.18	1.38	0.30	2.67	5.23	3.24	2.41
Discount rate	3.00	3.00	3.00	3.00	4.00	3.00	3.00
VND/USD	23,188	23,252	23,076	23,020	23,231	23,255	23,246
US GDP	NA	7.90	NA	NA	2.3	(5.70)	3.90
China GDP	NA	6.00	NA	NA	6.10	1.80	8.00

**Y Nguyen**

Y.nt@kisvn.vn

**Tuan Doan**

Tuan.doan@kisvn.vn

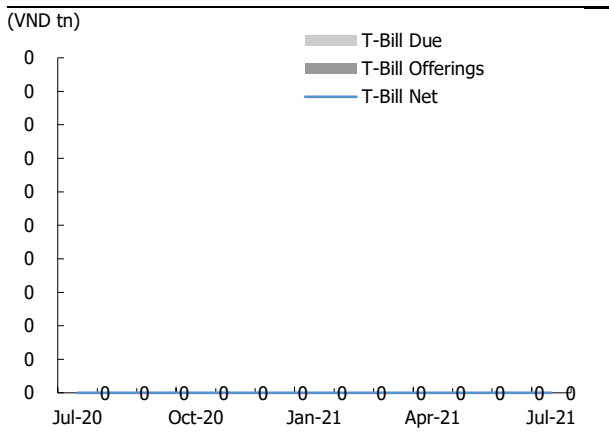
# I. Expectedly silent OMO

**No transaction recorded in the OMO**

July witnessed that SBV introduced a couple of administrative and directive measures to encourage the banking system to support affected businesses under the current outbreak. The open market operations, on the other hand, continued to be quiet when the short-term liquidity still inherently excessive after the Tet season. The current interest rate corridor is still effective when the interest rate applied for collateral loans to commercial banks was unchanged at 2.50%, 153bps-higher than the ON value at the end of this month.

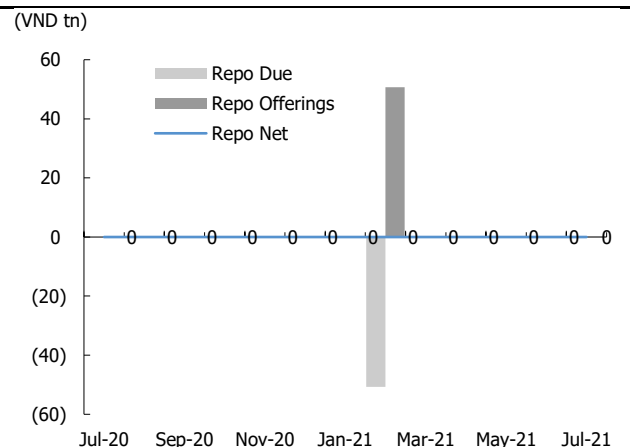
Given the long-lasting strict restrictions to contain the infection in epicenters such as Hochiminh city, Binh Duong, and other southern provinces, domestic consumers and producers were becoming more pessimistic about the income and business prospects. The consequent reduction in aggregate demand and supply would reduce the financing activities in the first lending market and sustain the short-term liquidity to abundant. Hence, we predict that the monetary stance in the next month continued to follow accommodation with the administrative style to prompt commercial banks to share the financial burden with COVID19-affected victims rather than the policy rate cut.

**Figure 1. T-bill transaction**



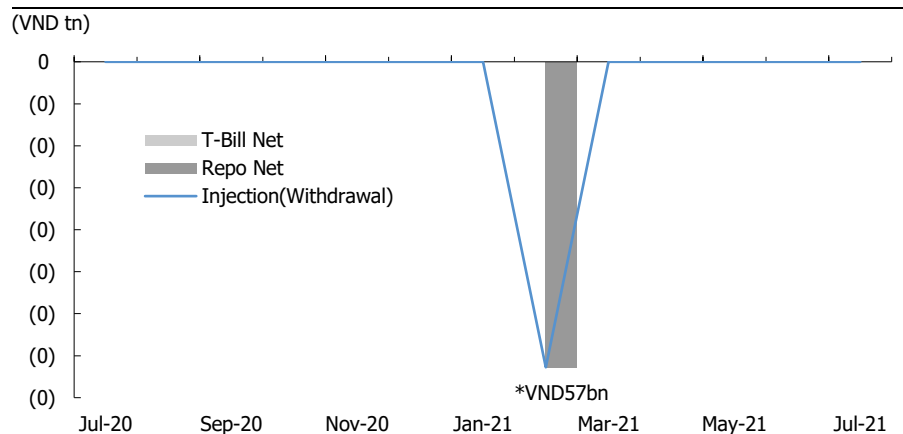
Source: Bloomberg, SBV, KIS

**Figure 2. Repo transaction**



Source: Bloomberg, SBV, KIS

**Figure 3. Net Injection/Withdrawal**



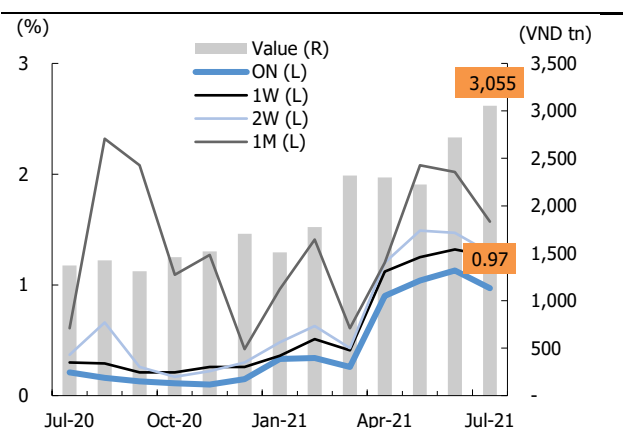
Source: Bloomberg, SBV, KIS

## II. Interbank rates to lower

Interbank rates in July generally decreased with the rising traded value after an increase streak of 3 months, reflecting the abundant liquidity in the money market under the widespread transmissibility of the new Delta variant. Lending costs of loans mostly reduced in many tenors except 6-month and 9-month. Specifically, ON and 1-week, 2-week, 1-month, and 3-month declined by 16bps, 6bps, 18bps, 45bps, and 27bps compared to the previous month, respectively. On the opposite direction, rates of longer-term loans, including 6-month and 9-month, rose by 34bps and 88bps.

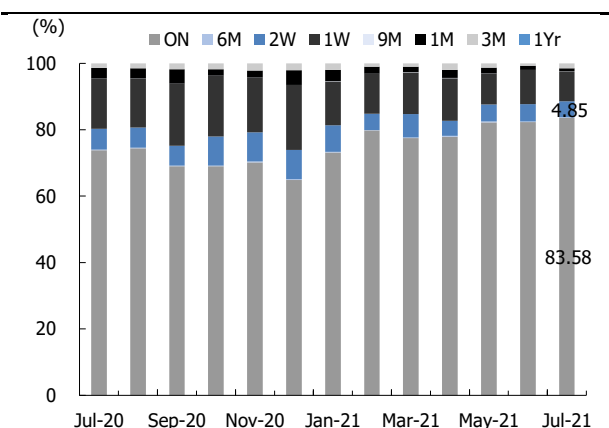
Given the general decrease in interest rates this month, the total trading value climbed up to VND3,054.91tn, 12.36% higher than June. ON loans increased the attention to commercial banks when its share became more significant relative to the remaining tenors and constituted 83.58% of total traded value.

**Figure 4. Interbank transaction**



Source: Bloomberg, SBV, KIS

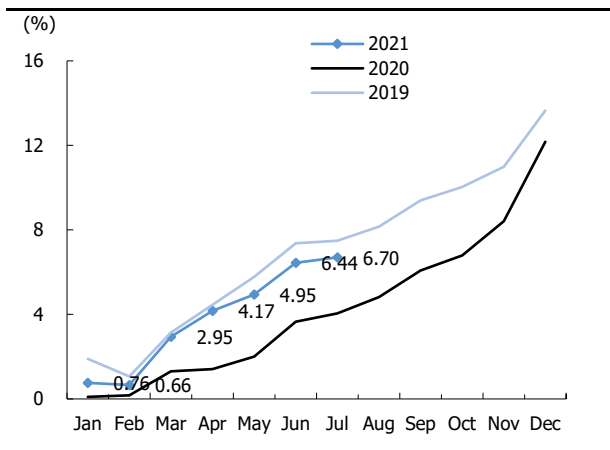
**Figure 5. Interbank value by tenors**



Source: Bloomberg, SBV, KIS

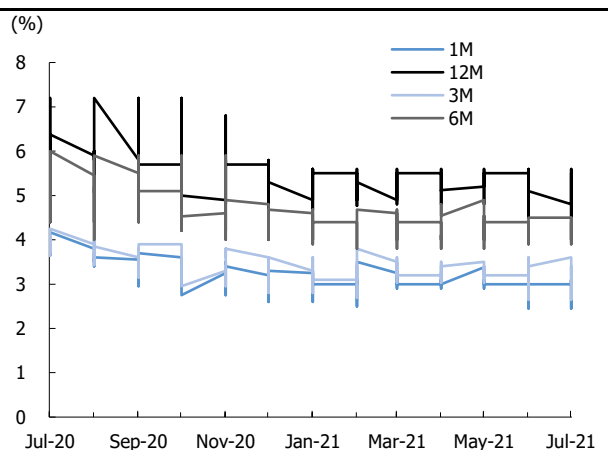
The slowdown in the first lending market and the low-cost funding environment under the reductions of the domestic consumption and production were the main reasons to drop the interbank rates this month. After an impressive acceleration in the disbursement of loans in June, the credit growth this month was 6.70% YTD, recording an insignificant increase in the outstanding loans of the banking system, loosening the short-term liquidity in the money market. Furthermore, deposit rates stayed low, allowing firms to lend their short-term funds at reasonably low rates.

**Figure 6. Credit growth by month-of-year**



Source: Bloomberg, SBV, KIS

**Figure 7. Historical deposit rates**



Source: Bloomberg, SBV, KIS

**PREDICTION:**

We predict that interest rates to reduce further in the next month due to the following reasons: Firstly, lending activity is growing at a slower pace than previous month under the strict restrictions in southern economic centers such as Hochiminh city, Binh Duong, and Dong Nai in the context of the low-cost funding of commercial banks, suggesting that the short-term liquidity in the money market would remain abundant. Secondly, the government has issued the relief package of VND26tn for virus-affected employees to ease the financial burden.

We predict that the money would flow from the Vietnam state treasury (VST) account to resident accounts in the banking system, providing more short-term liquidity for the interbank market in the next month. Furthermore, SBV switched from the forward to spot USD-buying in August-early, injecting more liquidity to the money market in the short term.

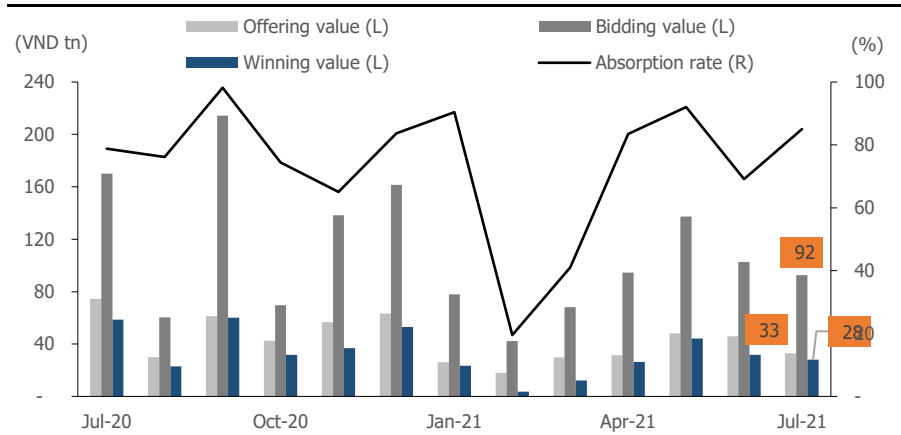
**III. Yield curve to shift to a new low territory**

**Government bond auctions slowed down at the beginning of 3Q21**

There has been a significant slowdown in the primary bond market at the beginning of the third quarter. Banks are still showing cautiousness in bond investment in the context that government bond yields are remaining extremely low, but the demand for G-bond sees some improvement in July compared to June.

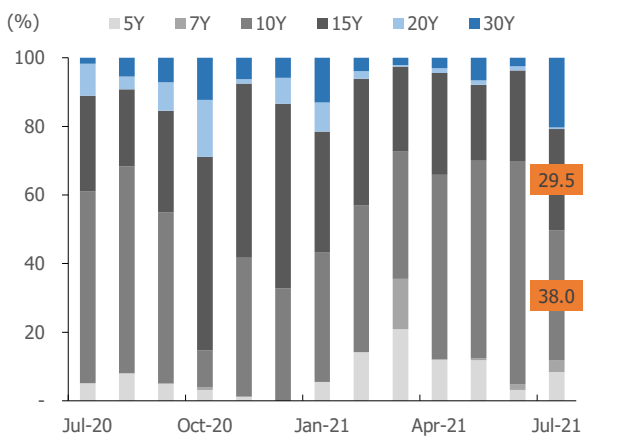
July recorded only 16 government bond auctions with VND33tn G-bond amount being offered, which is a 3-month low and down by 28.3% from last month. More than 86% of total G-bond offers are long-term bonds with maturities greater than 10 years, in which 10-year and 15-year G-bonds were offered the most with VND13tn and VND9tn, equal to 66.7% of total G-bond offering. We saw a modest improvement of G-bond demand in the month as the total bidding value reached VND92.5tn over VND33tn offering, down by 9.9% MoM. As a result, the bid-to-offer ratio improved markedly from 2.23 times in June to 2.80 times.

**Figure 8. Government bond issuance**



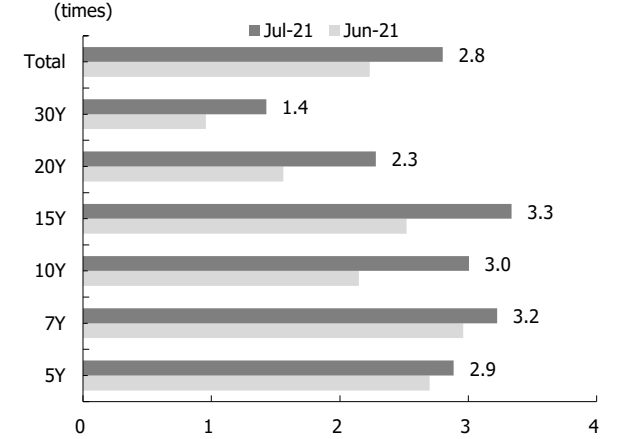
Source: HNX, KIS

**Figure 9. Issuing value by tenors**



Source: HNX, KIS

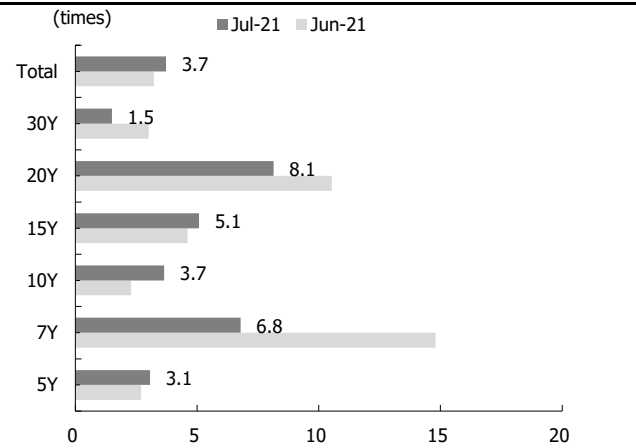
**Figure 10. Bid-to-offer ratio**



Source: HNX, KIS

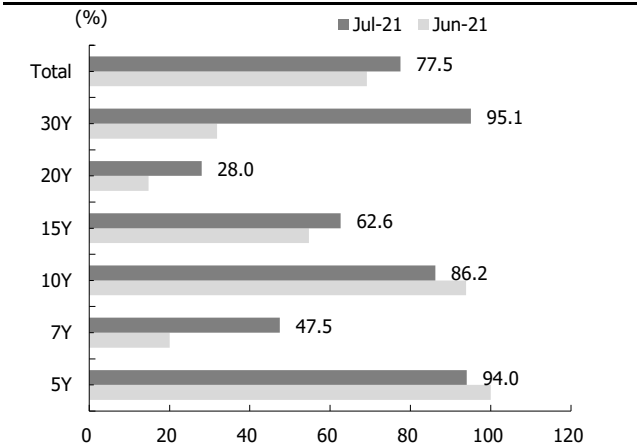
On the other hand, about VND28.1tn G-bonds were successfully issued in July, which is the lowest level since May, down by 11.8% MoM. G-bonds from 10-year to 30-year tenors accounted for more than 88% of total G-bond issuing, while 10-year and 15-year G-bonds made up 38.0% and 29.5% of total issuing. Furthermore, the bid-to-cover ratio improved at a 3-month high of 3.3 times, while the absorption rate also recovered to a 2-month high of 85.0%, significantly higher than in June.

**Figure 11. Bid-to-cover ratio by tenors**



Source: HNX, KIS

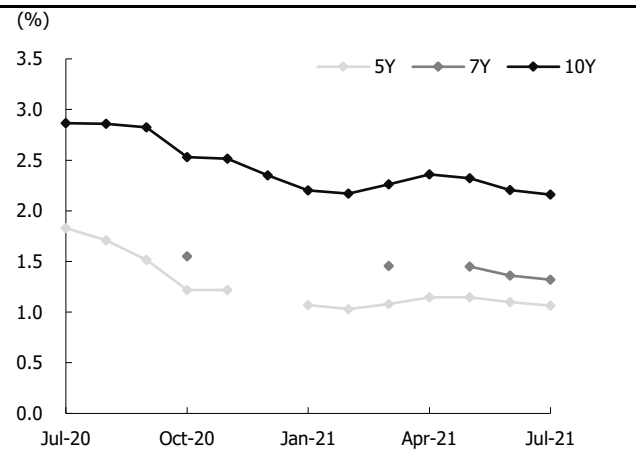
**Figure 12. Absorption ratio by tenors**



Source: HNX, KIS

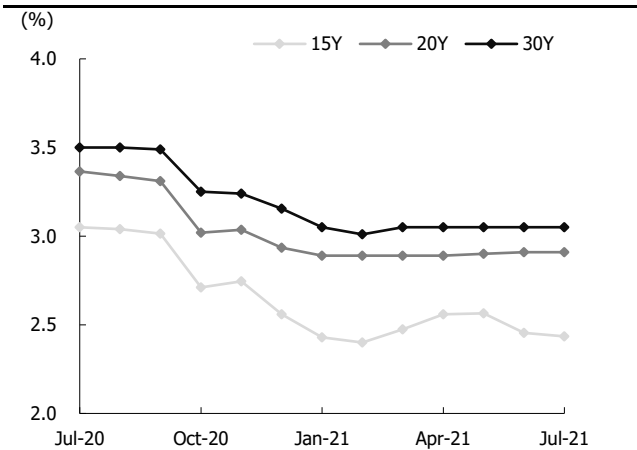
Under improving demand for G-bonds, bond yields continued to drop modestly in the month and reached new record lows or nearly there for most tenors. More specifically, average 10-year G-bond yield set up an all-time low of just 2.16%, down by 4.5 bps than in June's level, while 15-year yield dropped slightly by 2 bps to 2.44%, which is just 4 bps higher than its historic low. Similarly, 5-year and 7-year yields continued to decline by 3.5 bps and 4 bps to 1.07% and 1.32%, while long-term 20-year and 30-year yields remained unchanged at 2.91% and 3.05%.

**Figure 13. Yields from 5-year to 10-year**



Source: HNX, KIS

**Figure 14. Yields with tenors greater than 10-years**



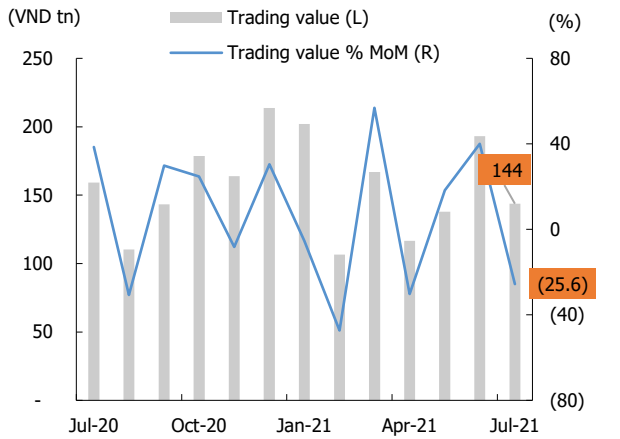
Source: HNX, KIS

**G-bond trading activities returned to quiet mood in a low-yield environment**

G-bond trading in the secondary market slowed down markedly from a high in June as the total trading value reduced by more than 25% MoM to just VND143.7tn. More than a half of total trading value was from long-term g-bonds with tenors greater than 10 years, in which 10-year and 15-year G-bonds accounted for the largest shares of about 23.3% and 25.5% of total trading value. On the other side, mid-term G-bonds with maturities from 5 years to 10 years and short-term bonds with maturities less than 5 years made up about 31.0% and 11.6%.

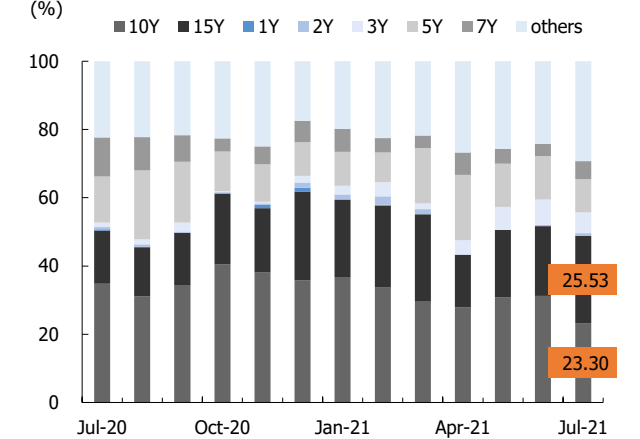
A possible reason for the slowdown in G-bond trading is that the amount of G-bonds expired in the month declined strongly compared to May and June. In other words, G-bond investors felt less pressure to purchase bonds than in the previous months when bond yields continued to be less attractive.

**Figure 15. Trading value**



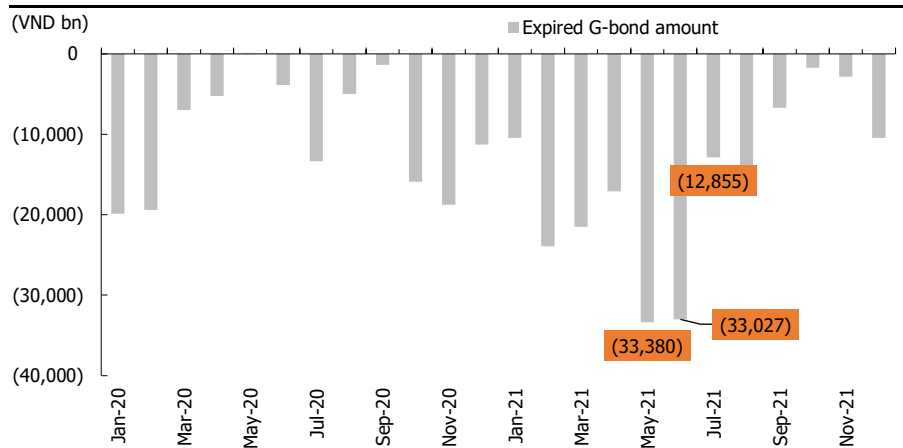
Source: HNX, KIS

**Figure 16. Trading value by tenor**



Source: HNX, KIS

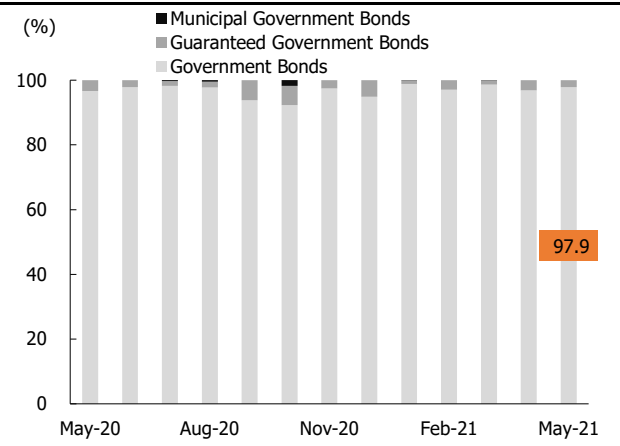
**Figure 17. Estimates of monthly government bonds expired**



Source: HNX, KIS estimate

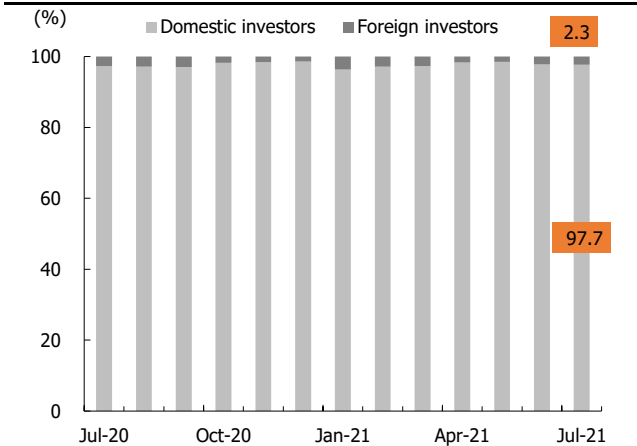
By bond type, 97.9% of the total trading value (VND140.7tn) was from government bonds, while government-guaranteed bonds accounted for 2.1% of the total trading value (VND3.0tn). Regarding investor types, domestic investors made up 97.7% of total trading value, the remaining 2.3% was from foreign investors.

**Figure 18. Trading value by bond type**



Source: HNX, KIS

**Figure 19. Trading value by investor**



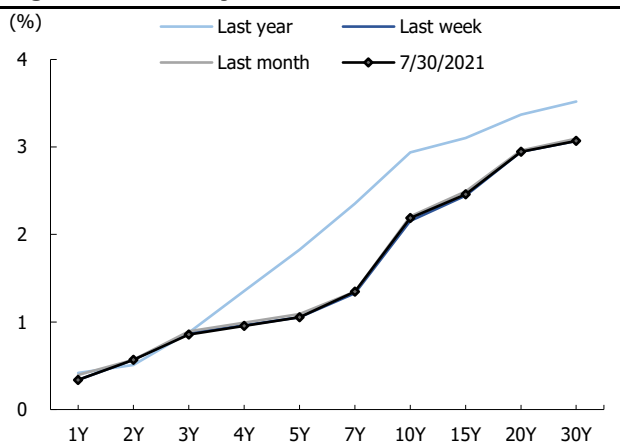
Source: HNX, KIS

***G-bond yields are on the way to find new record lows***

From our view, improved liquidity conditions in the banking system were the main force in driving G-bonds down further in July, although the downward pressure was limited in the context that G-bond yield levels were near historic lows and inflation was picking up.

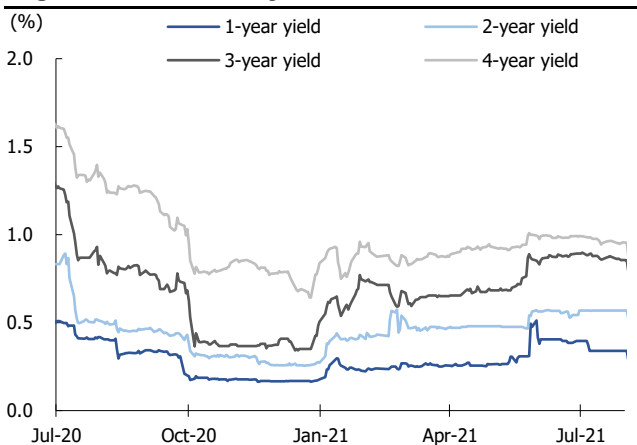
Firstly, liquidity conditions in the interbank market continued to ease further in July, illustrated by downward-drifting interbank rates. As a result, short-term G-bond yields, which we found are highly correlated to interbank rates both statistically and economically, dropped the most in July. More specifically, 1-year, 2-year, 3-year, and 4-year yields declined by 5.6 bps, 0.1 bps, 3.7 bps, and 3.6 bps to 0.34%, 0.57%, 0.76%, and 0.96%.

**Figure 20. G-bond yield curve**



Source: HNX, VBMA, KIS

**Figure 21. Short-term yields**

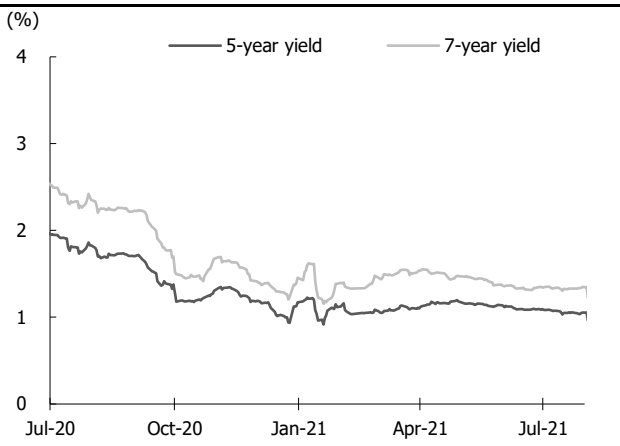


Source: HNX, VBMA, KIS

Regarding mid-term bonds from 5-year to less than 10-year tenors, we also saw downward pressure on those yields, albeit to a lesser extent than on short-term yields. 5-year yield fell by nearly 4 bps to 1.06%, which was a few points away from its record lows in December 2020 – January 2021. 7-year yields remained unchanged at 1.35%. For long-term yields, a several-month downward trend continued in the month since late March. 10-year, 15-year, 20-year, and 30-year yields dropped further by 1.9 bps, 3.5 bps, 1.2 bps, and 2.6 bps, to 2.19%, 2.46%, 2.95%, and 3.07%, respectively.

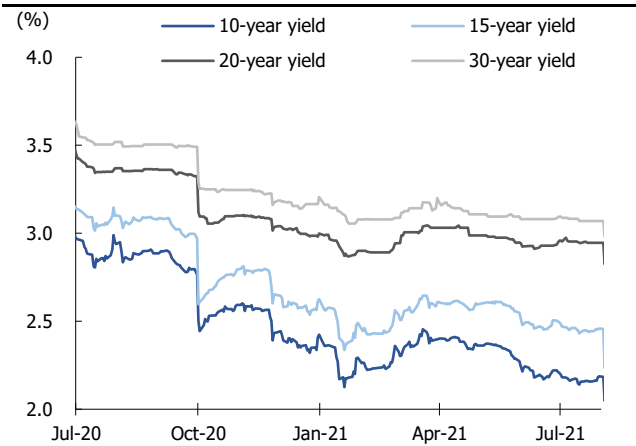


**Figure 22. Mid-term yields**



Source: HNX, VBMA, KIS

**Figure 23. Long-term yields**



Source: HNX, VBMA, KIS

### PREDICTION:

In the first half of August, there are important changes in VND supply conditions that would make significant impacts on the government bond market in the coming months. Firstly, under worsening economic conditions due to the COVID-19 outbreak, banking lending activity would likely be dampened similarly to what already happened since April last year. More abundant banking liquidity combined with weakening credit demand, as a result, would be a favorable environment for G-bond demand to accelerate.

Besides, a part of VND inflows would be poured back into the banking system via SBV's USD-purchasing 6-month forward contracts being expired in August, estimated worth nearly USD2bn. Furthermore, SBV changing its USD-purchasing approach to spot purchasing from 11th August will create new and constant VND inflows into the banking system, and we believe this would make fixed-income markets return to a low-interest-rate environment like last year.

Looking forward to August, we expect the G-bond yield curve would be shifting downward further. We also expect long-term yields to see greater downward pressure under abundant liquidity conditions, and some of them would likely set new all-time lows.

## IV. VND increase hits a one-year high

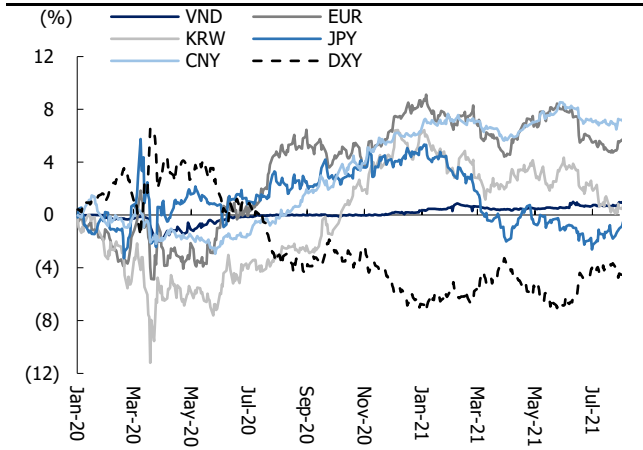
***VND saw the largest appreciation against USD since a year ago***

An impressive economic recovery in the U.S continued to help USD remain at a high level in July after its 5-year record increase in the previous month. By end-July, the benchmark DXY index, which measures USD value, adjusted slightly by 0.28% compared to a 5-year record increase in June.

In our currency watchlist, including four currencies EUR, KRW, JPY, and CNY of our large trade partners, KRW saw the largest reduction of 2.1% MoM against the greenback. It marked the second month of strong depreciation in that currency as the Korean economy is battling the worst COVID-19 outbreak with the Delta variant. EUR and CNY also marked another reduction for the two consecutive months under strong USD recovery, although the depreciation

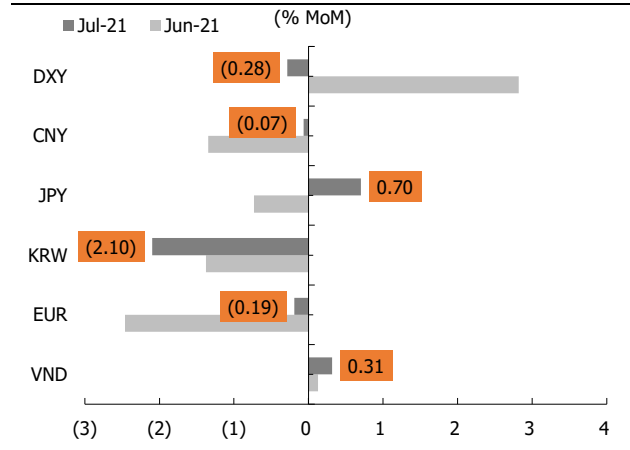
levels were modest. More specifically, EUR and CNY loss by about 0.19% MoM and 0.07% compared to USD. On the contrary, JPY posted the first increase of about 0.70% MoM since May.

**Figure 24. Movements of VND, USD, CNY, KRW, JPY, and EUR**



Source: Bloomberg, KIS

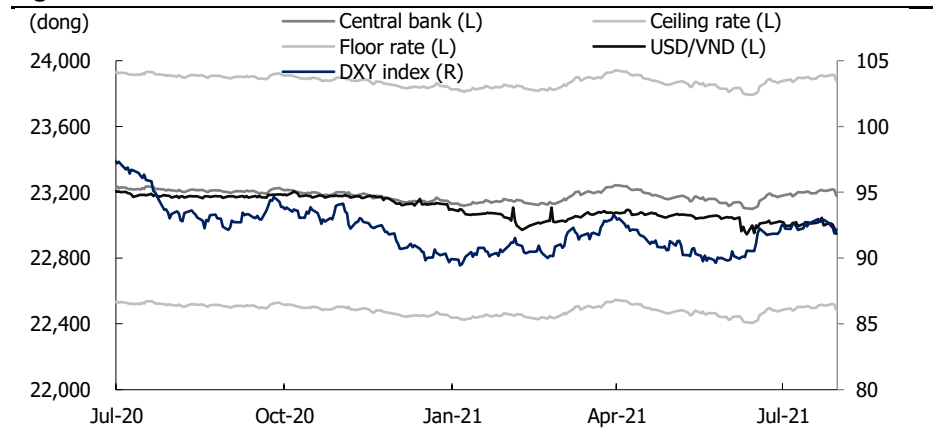
**Figure 25. Monthly changes in VND, USD, CNY, KRW, JPY, and EUR**



Source: Bloomberg, KIS

The spotlight in the month was coming from our domestic currency, as VND appreciated by about 0.31% MoM against USD, which is the largest increase since a year ago.

**Figure 26. USD/VND rate and DXY index**



Source: Bloomberg, KIS

**PREDICTION:**

There is an important change in SBV's approach in purchasing USD in early August that, from our viewpoint, would impact strongly the VND/USD rate in the interbank market. The state bank has adjusted its USD-purchase rate to 22,750 dong from 22,975 dong, which is the largest reduction for many years. SBV's USD-purchase price is considered as a benchmark for USD-purchase price in the foreign exchange market, and this possibly signals for VND appreciation in the near term

## Macro scorecard

(USD bn, USD, %, % YoY)

	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	3Q20	4Q20	1Q21	2Q21	2017	2018	2019	2020
Real GDP growth		4.48			6.61		2.62	4.48	4.65	6.61	6.81	7.08	7.03	2.91
Registered FDI	3.44	4.67	2.12	1.74	1.28	1.45	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	20.20	29.65	26.55	26.19	27.20	27.00	79.74	80.15	77.34	79.23	215.1	243.5	263.6	282.7
Import	20.66	28.46	27.78	28.27	27.66	28.70	69.02	76.86	75.32	83.50	213.2	236.7	254.4	263.0
Export growth	(3.77)	22.89	51.00	36.52	20.56	8.55	10.61	15.14	21.76	33.50	21.82	13.19	8.16	7.02
Import growth	9.75	28.48	49.95	55.52	33.54	29.88	3.74	16.43	26.17	45.68	21.85	11.01	7.41	3.81
Inflation	0.70	1.16	1.16	2.90	2.41	2.64	3.81	3.24	0.30	1.23	3.53	3.54	2.79	3.24
USD/VND	23,018	23,076	23,053	23,048	23,020	22,947	23,184	23,126	23,076	23,020	22,698	23,175	23,173	23,126
Credit growth	1.21	2.04	3.34				6.10	10.14			18.24	13.89	13.70	10.14
10Y gov't bond	2.13	2.40	2.36	2.27	2.04	2.06	2.65	2.01	2.40	2.04	5.14	5.07	3.37	2.01

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#### **VIET NAM**

JAE HEUNG LEE, Business Director (jhlee@kisvn.vn +8428 3914 8585 - 1466)  
UYEN LAM, Head of Institutional Brokerage (uyen.lh@kisvn.vn +8428 3914 8585 - 1444)  
KIS Vietnam Securities Corporation  
3rd floor, 180-192 Nguyen Cong Tru, Nguyen Thai Binh Ward, District 1, Ho Chi Minh City.  
Fax: 8428 3821-6898

#### **SOUTH KOREA**

YEONG KEUN JOO, Managing Director, Head of International Business Division (ykjoo@truefriend.com, +822 3276 5157)  
PAUL CHUNG, Sales Trading (pchung@truefriend.com +822 3276 5843)  
27-1 Yoido-dong, Youngdeungpo-ku, Seoul 150-745, Korea  
Toll free: US 1 866 258 2552 HK 800 964 464 SG 800 8211 320  
Fax: 822 3276 5681~3  
Telex: K2296

#### **NEW YORK**

DONG KIM, Managing Director (dkim@kisamerica.com +1 212 314 0681)  
HOON SULL, Head of Sales (hoonsull@kisamerica.com +1 212 314 0686)  
Korea Investment & Securities America, Inc.  
1350 Avenue of the Americas, Suite 1110  
New York, NY 10019  
Fax: 1 212 314 0699

#### **HONG KONG**

GREGORY KIM, Managing Director, Head of HK Sales (greg.kim @kisasia.com +852 2530 8915)  
Korea Investment & Securities Asia, Ltd.  
Suite 2220, Jardine House  
1 Connaught Place, Central, Hong Kong  
Fax: 852-2530-1516

#### **SINGAPORE**

ALEX JUN, Managing Director, Head of Singapore Sales (alex@kisasia.com.sg +65 6501 5602)  
CHARLES AN, Sales (alex.jun@kisasia.com.sg +65 6501 5601)  
Korea Investment & Securities Singapore Pte Ltd  
1 Raffles Place, #43-04, One Raffles Place  
Singapore 048616  
Fax: 65 6501 5617

#### **LONDON**

Min Suk Key, Managing Director (peterkey@kiseurope.com +44 207 065 2766)  
Korea Investment & Securities Europe, Ltd.  
2nd Floor, 35-39 Moorgate  
London EC2R 6AR  
Fax: 44-207-236-4811

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