

Fixed-income Perspectives

A prolonged period of low rates to arrive

Interbank rates to stay low

Interbank rates in August declined further with a decrease in trading value, reflecting the abundant liquidity in the money market under the sluggish lending market. The main reasons for the drop in interbank rate this month were the slowdown in the first lending market and the low-cost funding environment following reductions in domestic consumption and production. Furthermore, SBV switched from the forward to spot USD-buying in August-early, injecting more liquidity to the money market. We predict interbank rates to remain low next month due to the current slowdown in lending activities and VST's plan to offer short-term loans with a total of VND59tn in 3Q21, especially in September.

Bond yields to find new record lows

In our view, current developments of the yield curve are closely linked to increasingly abundant liquidity conditions in the banking system. This is driving G-bond yields to new record lows in both primary and secondary markets. We believe that a new period of "cheaper money", or lower G-bond yield levels, has just started, and it would likely be continuing for a while, possibly several months, before reversing. As long as credit activity remains subdued and the economy is dealing with stagnation, G-bond yields will continue to dive deeper into the new low-yield territory.

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. The usual silence in OMO

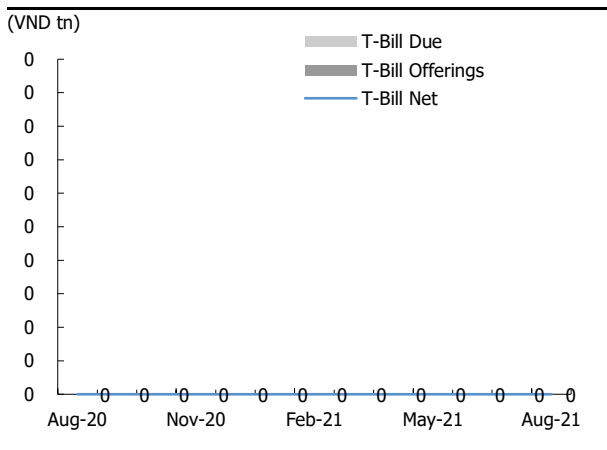
No transaction recorded in the OMO

SBV continued communicating with the banking system via a couple of administrative and directive measures to encourage the banking system to support affected businesses under the widespread infection. On 7th September, SBV issued the circulation 14/2021/TT-NHNN to replace the circulation 03/2021/TT-NHNN, mainly allowing banks to extend the repayment period to 30th June 2022 instead of 31st December 2021. Besides, SBV issued official letter No. 5901/NHNN, requesting the credit institutions to reduce lending rates and fees to share the financial burden with customers affected by the Covid-19 epidemic.

On the other hand, the OMO remained silent this month alongside the excessive liquidity in the money market under the slow growth in lending activities. The current interest rate corridor is still effective when the interest rate applied for collateral loans to commercial banks was unchanged at 2.50% and the overnight rate was approaching the zero level.

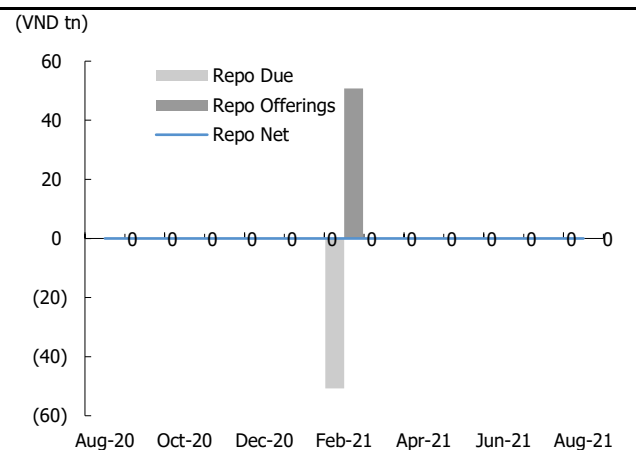
The government was considering ease restrictions gradually in Hochiminh city on 15th September, giving hope for economic activities to return partly to normal. However, enterprises seem to put their new production plans aside and wait to see how the re-opening of the city would be going. Therefore, the financing demand in the first lending market would remain modest, and the short-term liquidity would remain 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 to see how good the re-opening would be.

Figure 1. T-bill transaction



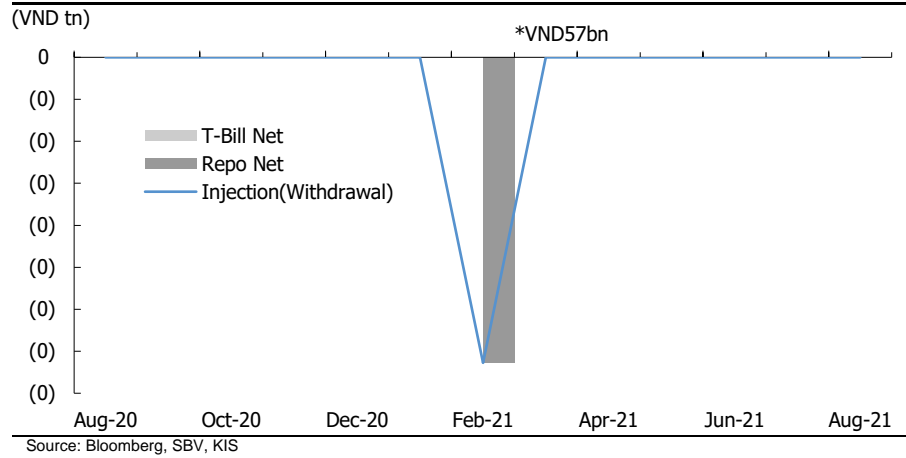
Source: Bloomberg, SBV, KIS

Figure 2. Repo transaction



Source: Bloomberg, SBV, KIS

Figure 3. Net Injection/Withdrawal

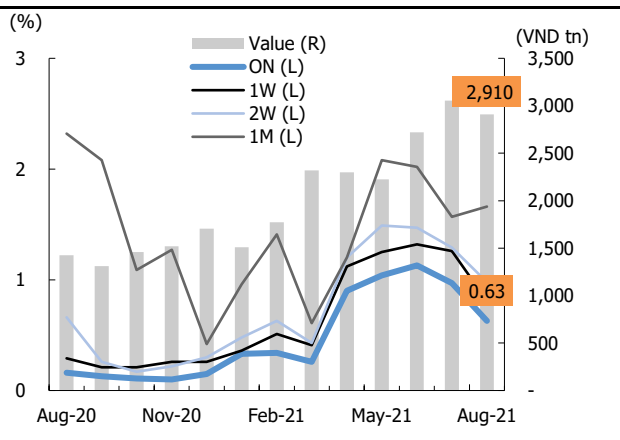


II. Interbank rates to stay low

Interbank rates in August declined further with a decrease in trading value, reflecting the abundant liquidity in the money market under the sluggish lending market. Lending costs of interbank loans declined in the majority of tenors except for 1-month. Specifically, ON, 1-week, 2-week, 3-month, 6-month, and 9-month declined by 34bps, 45bps, 31bps, 19bps, 37bps and 94bps compared to the previous month to post 0.63%, 0.81%, 0.98%, 1.78%, 2.45%, and 2.89%, respectively. On the opposite direction, the interest rate of 1-month loans increased by 9bps to post 1.66% this month.

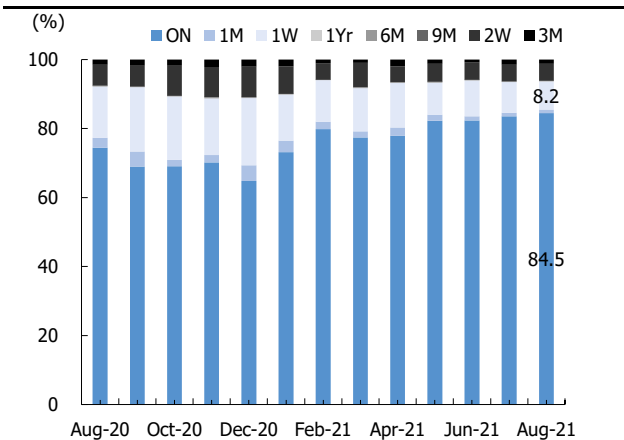
Given the general decrease in interest rates this month, the total trading value reduced slightly, implying that the downward pressure was likely to ease when ON was approaching zero. The total trading value in August was VND2,909.60tn, 4.76%-lower than July. ON loans increased the attention to commercial banks when its share became more significant relative to the remaining tenors and constituted 84.53% of total trading value.

Figure 4. Interbank transaction



Source: Bloomberg, SBV, KIS

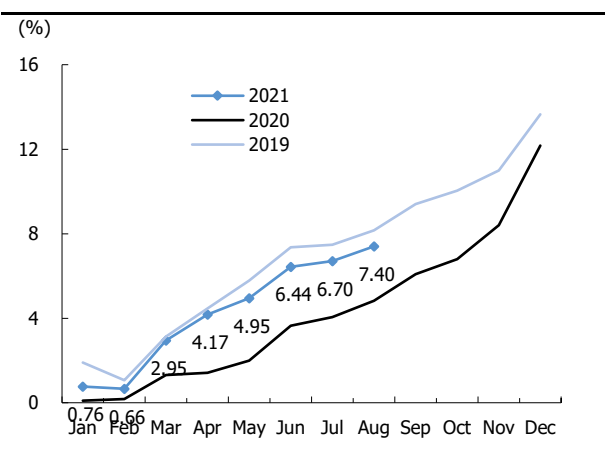
Figure 5. Interbank value by tenors



Source: Bloomberg, SBV, KIS

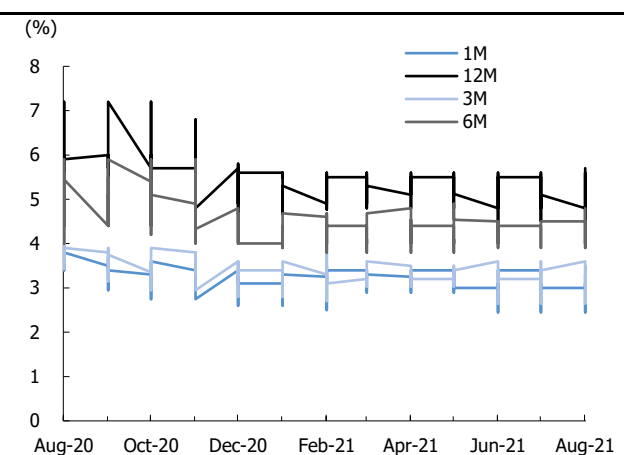
The slowdown in the first lending market and the low-cost funding environment under the reductions of the domestic consumption and production were the main reasons to drop the interbank rates this month. Lending activities remained slowing down this month as the credit growth was 7.40% YTD, recording an insignificant increase in the outstanding loans of the banking system, loosening the short-term liquidity in the money market. Besides, deposit rates stayed low, allowing firms to lend their short-term funds at reasonably low rates. Furthermore, SBV switched from the forward to spot USD-buying in August-early, injecting more liquidity to the money market.

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 remain low in the next month due to several reasons. First, although Hochiminh city authorities drafted the scenario of a partly re-opening the economic activities in September, it seems to be a try-and-error solution with many uncertainties under the complicated infection and slow vaccination. This implies that the production would take several months to operate like the pre-pandemic period entirely. Lending demand, therefore, would slow down further. Second, VST announced to add short-term loans with the total amount of VND59tn in 3Q21 to the money market via repurchase agreements of government bonds, increasing the availability of short-term funds in the banking system and putting downward pressure on the interbank rates in the next month.

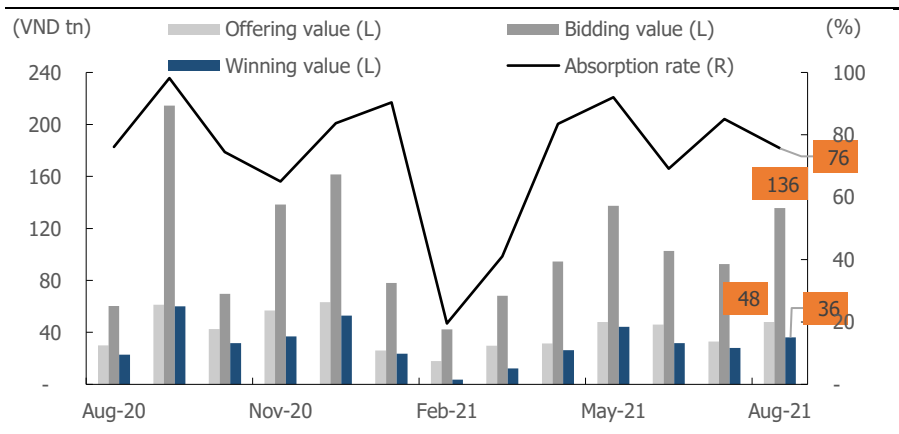
III. Bond yields to enter a new low territory

A booming in G-bond investment activity in the primary market

Unlike other financial markets that are facing enormous pressure from the outbreak's impact, fixed-income markets are re-taking their role as an investment shelter in this uncertain period. It is evident that the government bond markets are benefiting from increasing investment inflows.

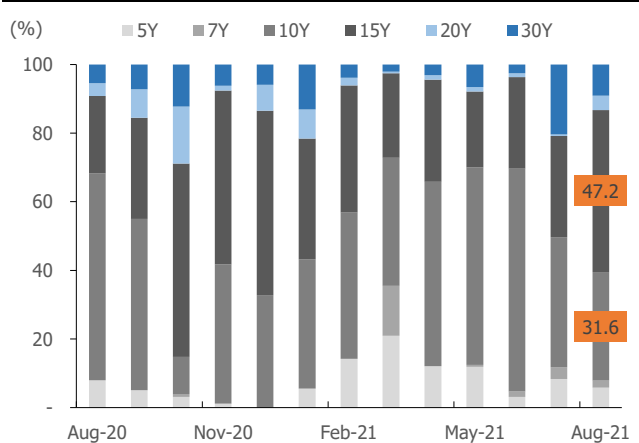
Going into details, 20 government-bond auctions were held in August with about VND47.9tn G-bond amount being offered, which is approximately the highest level in 2021 (only lower than in May with VND48tn G-bond offering) and 45.1% higher than in July. Up to 92.2% of total G-bond offerings were long-term bonds with tenors greater than 10 years, in which 10-year and 15-year G-bonds accounted for about 73.4%. From the demand side, the total registering value also reached nearly its high in 2021, at VND135.7tn and 46.7% higher than in July, translating to a bid-to-offer ratio to its 3-month high of 2.83 times.

Figure 8. Government bond issuance



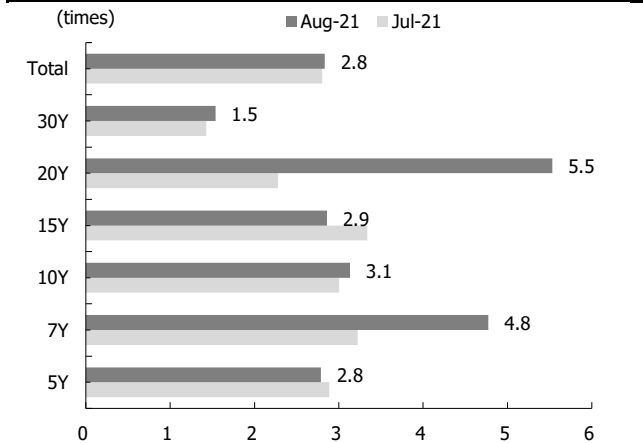
Source: Bloomberg, SBV, KIS

Figure 9. Issuing value by tenors



Source: HNX, KIS

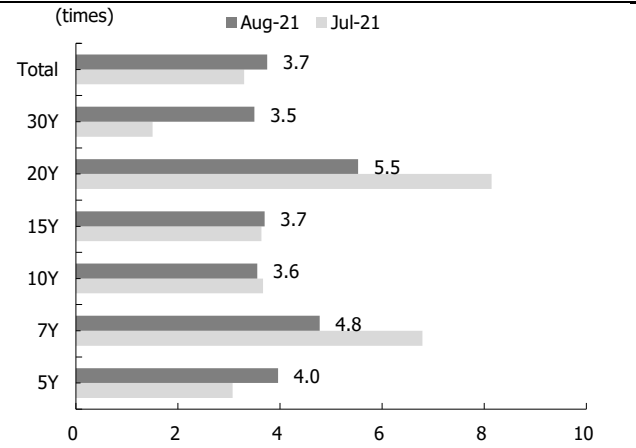
Figure 10. Bid-to-offer ratio



Source: HNX, KIS

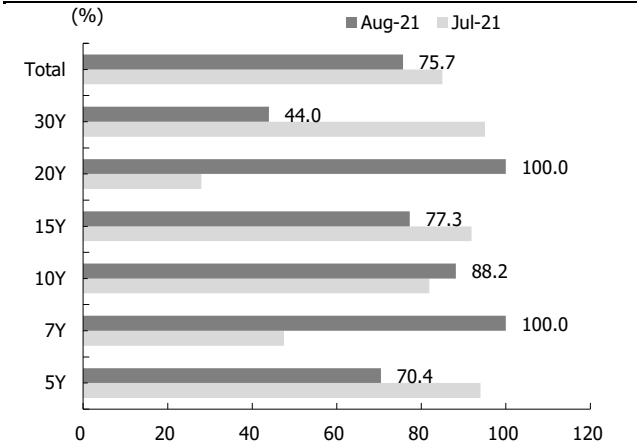
Under improved G-bond demand and expanding G-bond supply, about VND36.2tn were successfully issued, the second-highest level in 2021 and increasing 29.1% MoM, with 10-year and 15-year G-bond issuance accounting for nearly 80% of total issuance. At the same time, the bid-to-cover ratio improved to a 5-month high of 3.75 times, while the absorption ratio also remained high at 75.7%

Figure 11. Bid-to-cover ratio by tenors



Source: HNX, KIS

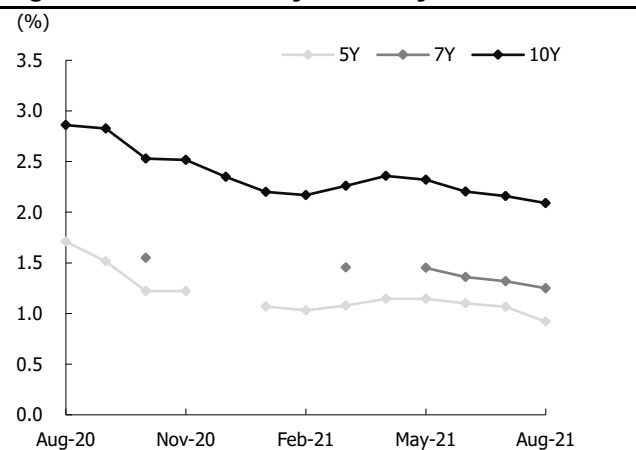
Figure 12. Absorption ratio by tenors



Source: HNX, KIS

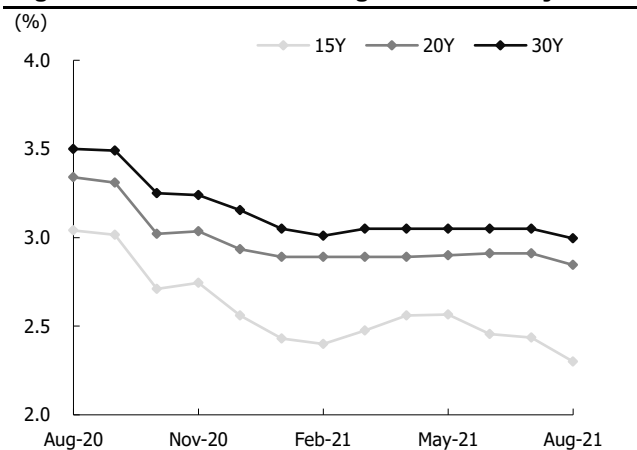
It is noticeable that G-bond yields for all tenors found their new record lows in August, in which 5-year yield dropped below 1% for the first time, and 10-year yield reached close to just 2%. More specifically, medium-term 5-year and 7-year yields were down by 14.5 bps and 7 bps from July to 0.92% and 1.25%. Long-term yields, including 10-year, 15-year, 20-year, and 30-year also dropped by 7 bps, 13.5 bps, 6.5 bps, and 5.5 bps to 2.09%, 2.30%, 2.85%, and 3.00%, respectively.

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



Source: HNX, KIS

Figure 14. Yields with tenors greater than 10-years

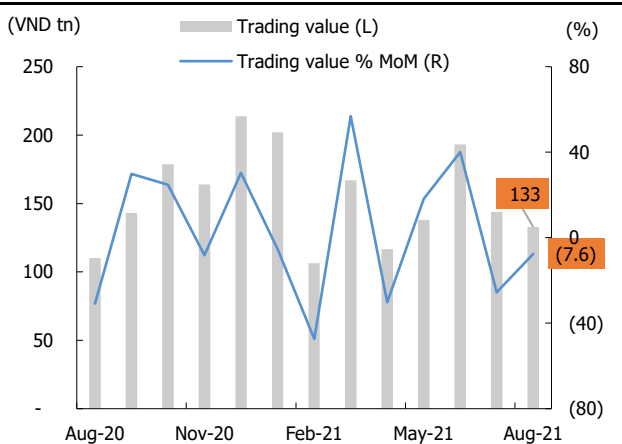


Source: HNX, KIS

G-bond trading value hit a 3-month low with a slowdown in medium-term bond trading

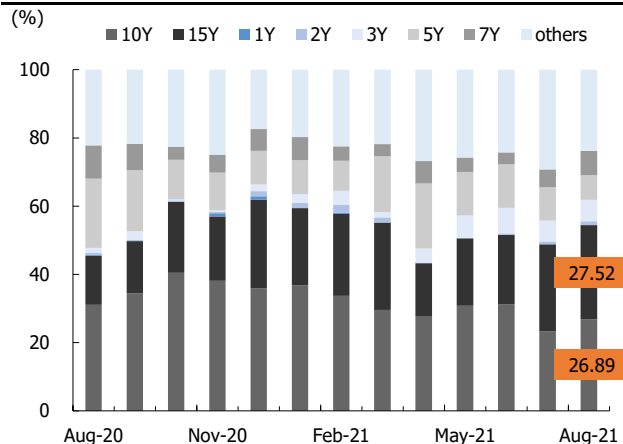
In contrast to a booming in the primary G-bond market, G-bond trading activity was slowing down somewhat in the secondary market, down by 25.6% MoM to just VND132.8tn. The G-bond trading structure was also changing markedly in August with a larger proportion of long-term bonds, in which 10-year and 15-year G-bonds accounted for the largest shares of 26.9% and 27.5% of total trading value.

Figure 15. Trading value



Source: HNX, KIS

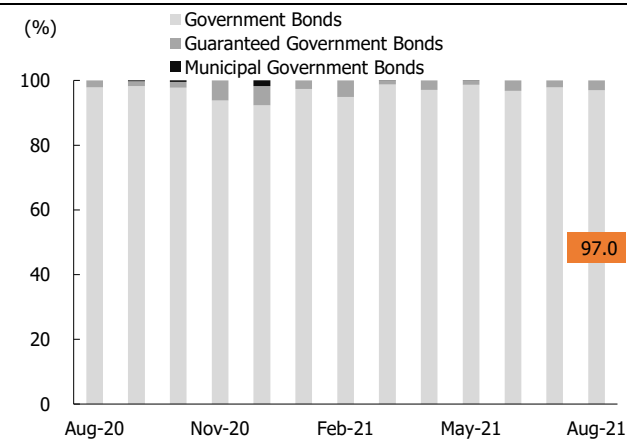
Figure 16. Trading value by tenor



Source: HNX, KIS

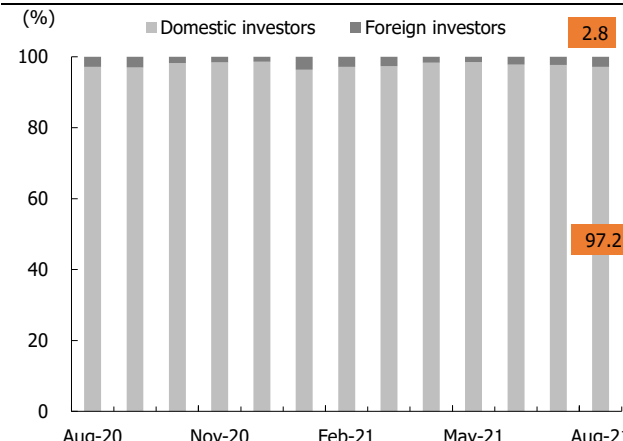
By bond type, 97.0% of the total trading value (VND128.9tn) was from government bonds, while government-guaranteed bonds accounted for 3.0% of the total trading value (VND4.0tn). Regarding investor types, domestic investors made up 97.2% of total trading value, the remaining 2.8% was from foreign investors.

Figure 17. Trading value by bond type



Source: HNX, KIS

Figure 18. Trading value by investor



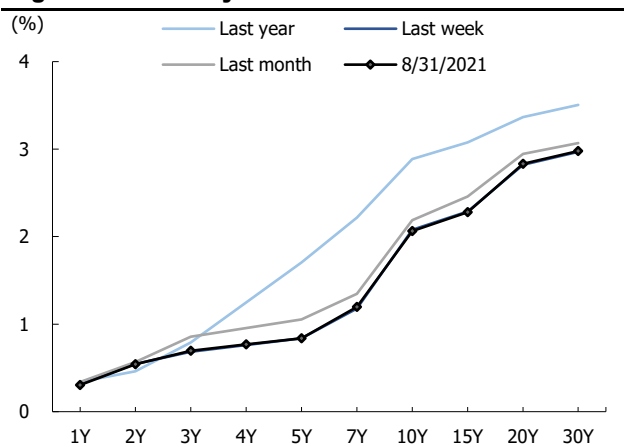
Source: HNX, KIS

G-bond yields for all tenors set new record lows

In our view, current developments of the yield curve were closely linked to increasingly abundant liquidity conditions in the banking system. In a time of many uncertainties, deteriorated business conditions, and lack of investment opportunities, excess liquidity just found its way towards safe-and-sound G-bonds. The result is that G-bond yields were under massive pressure in this exceptional period.

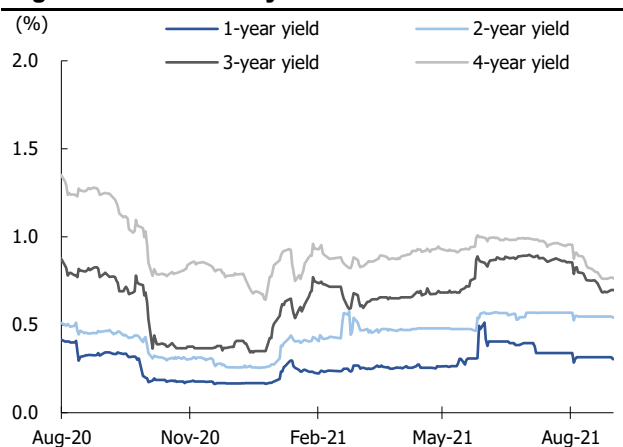
Overall, the whole yield curve was shifted downward in the month, in which the curve went down faster towards its right tail, meaning longer-maturity G-bond yield dropped faster than short-term yields. To be more specific, very short-term yields, including 1-year and 2-year maturities, declined about 3.4 bps and 2.6 bps to 0.31% and 0.54%. Meanwhile, 3-year and 4-year yields dropped up to 15.9 bps and 18.9 bps to just 0.70% and 0.77%.

Figure 19. G-bond yield curve



Source: HNX, VBMA, KIS

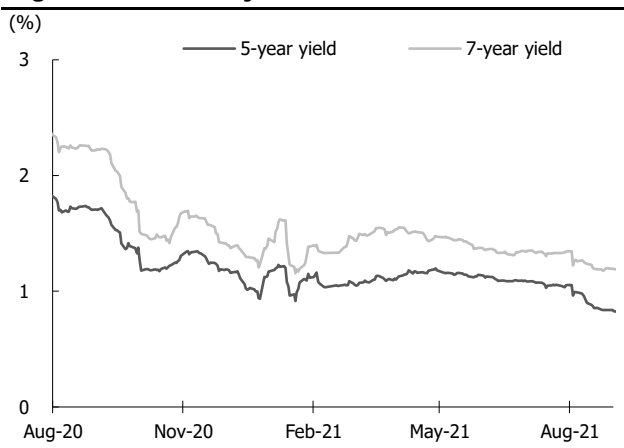
Figure 20. Short-term yields



Source: HNX, VBMA, KIS

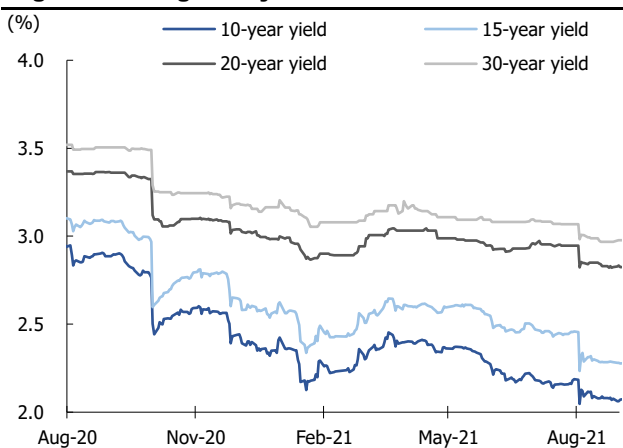
In the middle of yield curve, 5-year and 7-year yields fell the most by 21.8 bps and 15.1 bps to 0.84% and 1.20%. A right tail of the curve with long-term yields was also down by 2-digit points. 10-year and 15-year yields fell further by 12.4 bps and 17.7 bps to 2.06% and 2.28%, while 20-year and 30-year yields dropped 11.3 bps and 9.1 bps to 2.83% and 2.98%.

Figure 21. Mid-term yields



Source: HNX, VBMA, KIS

Figure 22. Long-term yields



Source: HNX, VBMA, KIS

PREDICTION:

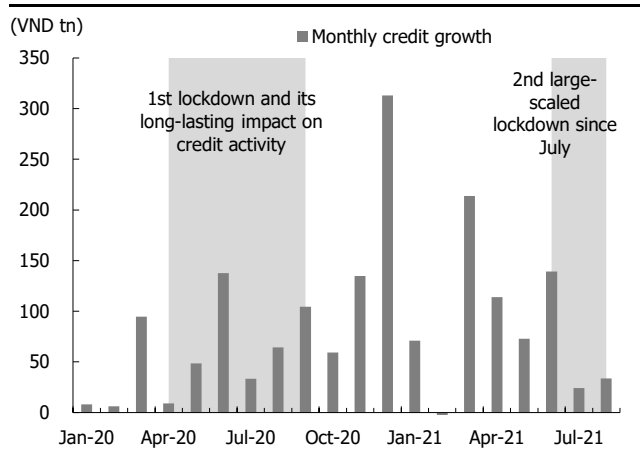
In our view, the current outbreak is considered a turning point towards a new prolonged period of low yields, which already started in June and accelerated in August. The fixed-income market is in a similar situation that is already experienced in the first lockdown last year. Firstly, an era of cheap money has come back with interbank rates and G-bond yields suddenly plunging along with the worsening pandemic situation. Credit activity has also been freezing during the first months of the pandemic, which is the main cause of a free fall in interest rate levels.

Figure 23. Interest rate levels during the pandemic



Source: HNX, VBMA, Bloomberg, KIS

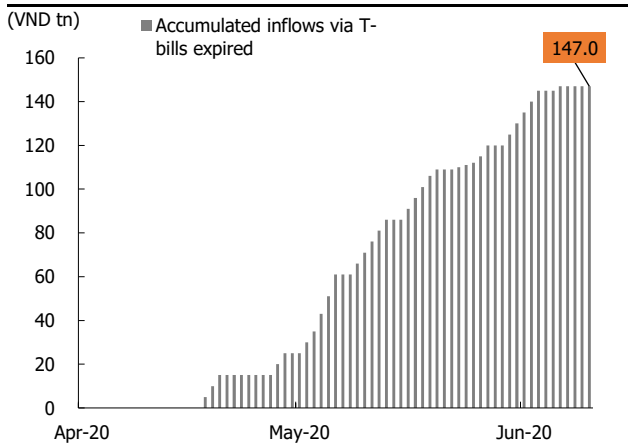
Figure 24. Credit activity during the pandemic



Source: SBV, KIS

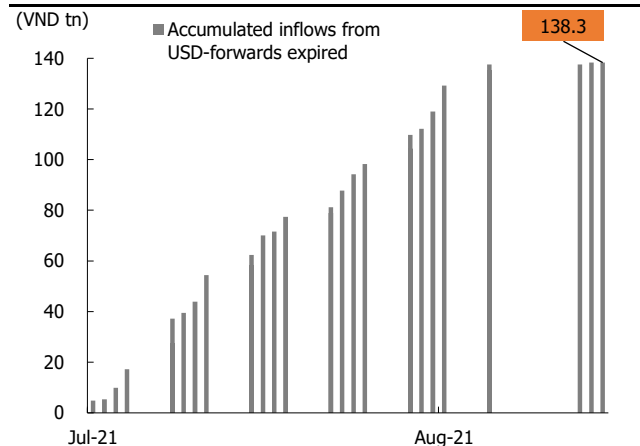
Secondly, Vietnam state bank has also created a new wave of liquidity into the banking system in different ways. While there were a hundred VND trillions flowing into banking liquidity via OMO operations, this time has also witnessed an equivalent amount of VND entering the system through USD-purchasing activity from SBV.

Figure 25. New liquidity inflows in the 1st lockdown



Source: HNX, Bloomberg, KIS

Figure 26. New liquidity inflows in this lockdown



Source: KIS estimates

We believe that a new period of “cheaper money”, or lower G-bond yield levels, has just started, and it would likely be continuing for a while, possibly several months, before reversing. How long it would last would depend significantly on the economic recovery in a re-opening phase. As long as credit activity remains subdued and the economy is dealing with stagnation, G-bond yields would continue to dive deeper into the low-yield territory.

IV. VND reaches a 40-month high

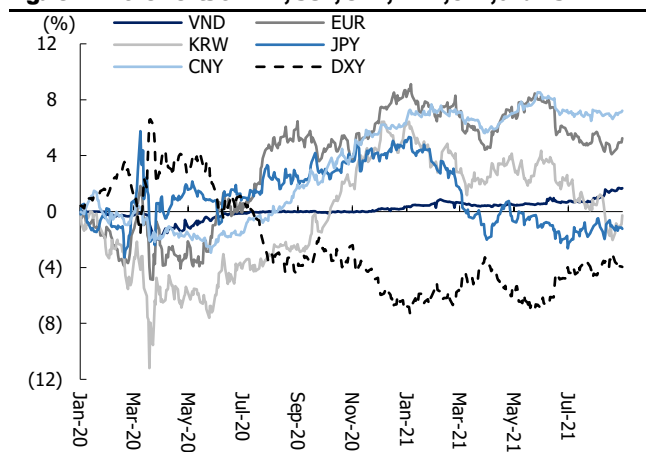
A 5-month straight increase pushes VND to the highest in more than 3 years

After a modest correction in end-July, USD continued to accelerate with an outlook of higher U.S. interest rate levels as Fed is planning for a tapering in the later months of 2021. By the end-August, DXY index, which measures USD value, increased by 0.49% MoM, and it sometimes reached its several-month high just before Fed’s Jackson Hole event.

In our currency watchlist, including four currencies EUR, KRW, JPY, and CNY of our large trade partners, KRW and EUR continued their reductions for the third month, by 0.79% and 0.28% compared to end-July. Furthermore, only in the June-August period, KRW and EUR fell by up to 4.21% and 2.92% of their values against the greenback. JPY also fell slightly by 0.20% MoM this month, while CNY was almost unchanged against USD.

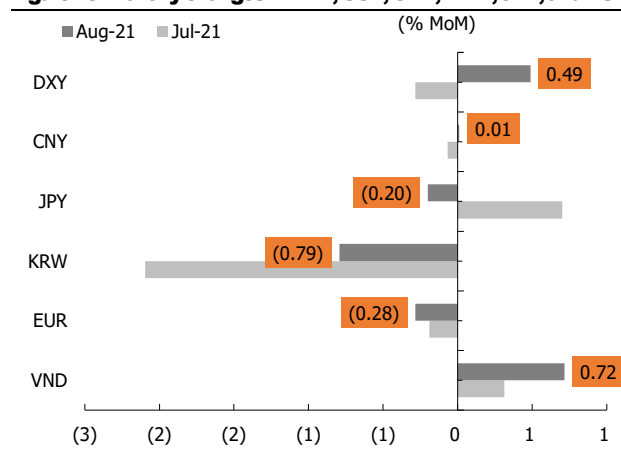
Following a recent signal for VND appreciation from Vietnam state bank, VND recorded the monthly largest gain of 0.72% MoM since April last year, which is also the fifth-month consecutive increase. Based on the interbank VND/USD rate, with a several-month appreciation, VND reached its highest value against USD for about 40 months since May 20.

Figure 27. Movements of VND, USD, CNY, KRW, JPY, and EUR



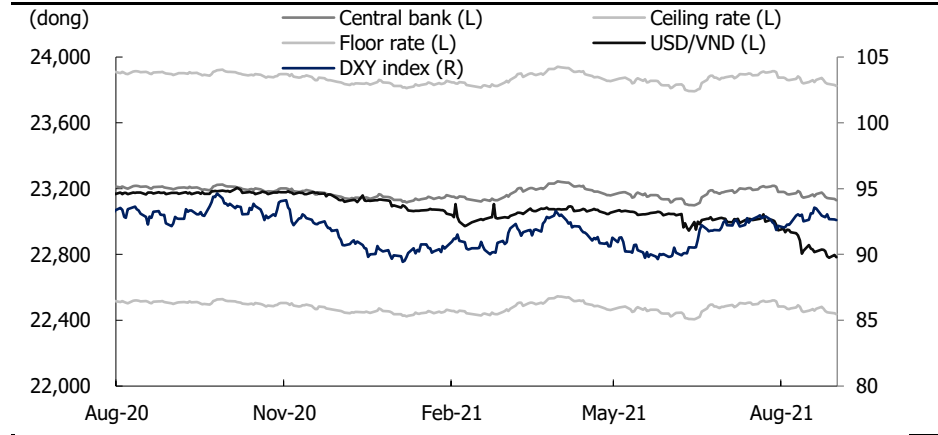
Source: Bloomberg, KIS

Figure 28. Monthly changes in VND, USD, CNY, KRW, JPY, and EUR



Source: Bloomberg, KIS

Figure 29. USD/VND rate and DXY index



Source: Bloomberg, KIS

Macro scorecard

(USD bn, USD, %, % YoY)

	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-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	4.67	2.12	1.74	1.28	1.45	2.40	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	29.65	26.55	26.19	27.20	27.87	26.20	79.74	80.15	77.34	79.23	215.1	243.5	263.6	282.7
Import	28.46	27.78	28.27	27.66	29.11	27.50	69.02	76.86	75.32	83.50	213.2	236.7	254.4	263.0
Export growth	22.89	51.00	36.52	20.56	12.03	(5.42)	10.61	15.14	21.76	33.50	21.82	13.19	8.16	7.02
Import growth	28.48	49.95	55.52	33.54	31.75	21.06	3.74	16.43	26.17	45.68	21.85	11.01	7.41	3.81
Inflation	1.16	1.16	2.90	2.41	2.64	2.82	3.81	3.24	0.30	1.23	3.53	3.54	2.79	3.24
USD/VND	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	2.95	4.17	4.95	6.44	6.70		6.10	10.14			18.24	13.89	13.70	10.14
10Y gov't bond	2.40	2.36	2.27	2.04	2.06	2.07	2.65	2.01	2.40	2.04	5.14	5.07	3.37	2.01

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