Fixed-Income Report

1H.2018

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Round-up

- **In 1H.2018, VND 74,581 bn (-40.7% yoy) worth of bond was mobilized. VND 1,307,325bn (+35.5% yoy) was traded on secondary market.**
- Against every market participant's expectation, bond yields ticked down strongly in almost all Q1.2018. Later on, bond yields were under upward pressure. Yield curve shifted downward and became steeper. According to Bloomberg, yields on 1Y, 2Y, 3Y, 5Y, 7Y, 10Y and 15Y terms ended Q2.2018 at 2.338% (-130.2 bps ytd), 2.688% (-121.2 bps ytd), 3.063% (-89.1 bps ytd), 3.65% (-71 bps ytd), 4.155% (-46.5 bps ytd), 4.825% (-37.9 bps ytd), 5.2% (-48.9 bps ytd) respectively.
- The foreign investors net buy approximately VND 2,666 bn in 1H.2018.
- Interbank rates edged up frictionally in Q2.2018. Abundant resources remained in the market. At the end of 1H.2018, ON-3M rates posted at 0.65%, 0.817%, 1.017%, 1.267% and 2.167%.
- From April, SBV turned their position into net-injected through OMO market.

VCBS Commentary 2H.2018

- **At the present, with all factors mentioned above, we believe that upward force on bond yields still remained at least in Q3**. Nevertheless, bond yields will only move upward roughly 50bps depended on tenors. The supporting arguments are as followed: (1) ST is not under pressure to mobilize bonds. (2) Although, no liquidity shortage is expected, and credit growth shall be slower than last year regarding the signal from SBV. (3) Public disbursement may slightly speed up though still behind the schedule. In addition a short-term downward correction, if any, shall occur at the beginning of Q4.

- In the next quarter as well as the remaining time of 2018, **although interbank rate may tick up slightly, liquidity shortage shall not happen**.

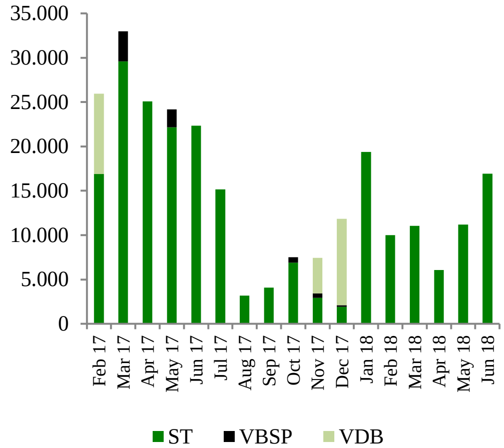
Bond Market

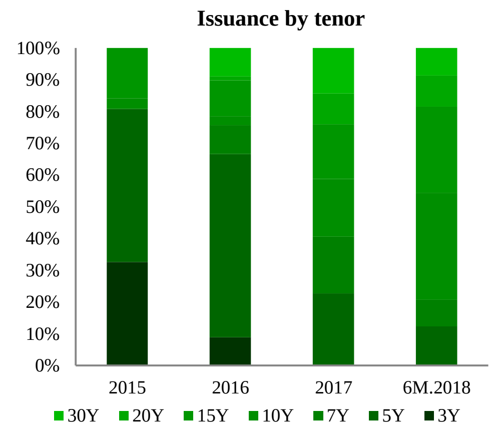
Primary market

Primary market tended to be dovish. ST did not willing to hike winning rates strongly.

In 1H.2018, VND 74,581 bn (-40.7% yoy) worth of bond was mobilized.

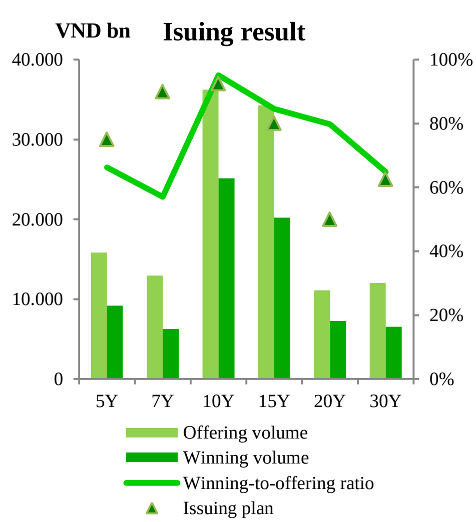
In 1H.2018, VND 74,581 bn (-40.7% yoy) worth of bond was mobilized from the State Treasury (ST). Vietnam Development Bank (VDB) and Vietnam Bank for Social Policies (VBSP) did not successfully mobilize fund in the first half.





Source: HNX, VCBS

When it comes to tenor, we come up with some highlight in 1H.2018: Long-term bond (10Y, 15Y) accounted for the largest portion. It should be note that these are main tenors that special members (Vietnam Social Security-VSS and Deposit Insurance of Vietnam-DIV) enter the most. It seemed that risk exposure of market participants to 20Y and 30Y came to limit especially for banks. Till now, percentage completion of annual issue plan was a little bit behind the schedule. However, issuing pressure did not huge as bond matured in 2018 decrease strongly. Average issuance tenor in 1H.2018 was 13.21, which was slightly higher than 13.03 year recorded in 2017.



Tenor	2018 Plan	1H. 2018 plan	Issued in 1H. 2018	% completion 2018 plan
< 5Y	20,000			
5Y	30,000	17,000	9,184	30.6%
7Y	36,000	17,000	6,250	17.4%
10Y	37,000	27,000	25,150	68.0%
15Y	32,000	24,000	20,209	63.2%
20Y	20,000	11,000	7,265	36.3%
30Y	25,000	14,000	6,523	26.1%
Total	**200,000**	**110,000**	**74,581**	**37.3%**

Source: HNX, VCBS

After forming its trough in Q1.2018, Winning rate was under upward pressure. Nevertheless, no issuing pressure recorded in this period. ST was unwilling to tick up rate offered. Therefore, the winning rates at the end of Q2.2018 nowhere far from Q1's level at 2.97% (+13 bps qoq; -155 bps ytd); 3.43% (+3 bps qoq;-148 bps ytd); 4.37% (+14 bps qoq;- 108 bps ytd); 4.7% (+30 bps qoq;- 135 bps qoq); 5.1% (+10 bps qoq; -72 bps ytd) and 5.42 (+0 bps qoq; -68 bps ytd) for 5Y, 7Y, 10Y, 15Y, 20Y and 30Y tenors, respectively. A great gap was formed between primary and secondary market.

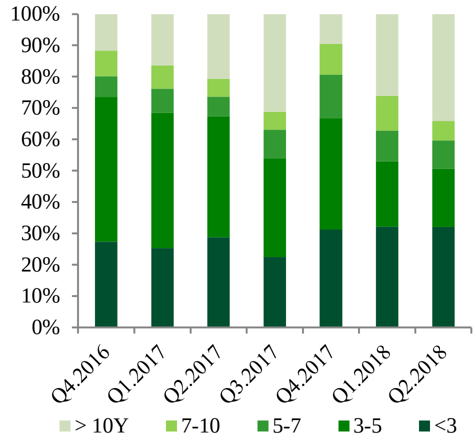
Macro updates:

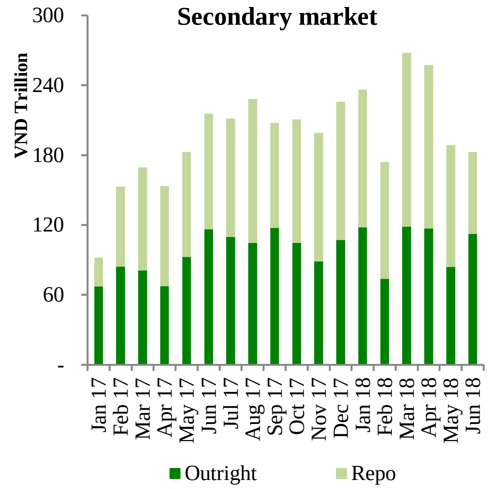
- Socio-economic state in the first 6 months tremendous change in term of growth. GDP growth in the first half of 2018 was 7.08%- highest level since 2010. **GDP growth in the second quarter of 2018 was 6.79%, which put and end to the cycle of higher growth quarter by quarter** (note that GDP growth in Q1 was 7.45%). We believe that these figures somehow ease recent concern about chance that monetary policy shall became less loosen compared to the same period.
- CPI in June kept surging by 0.61% mom, which equivalent to a 4.67% yoy. Meanwhile, core inflation in June 2018 increased by 0.1% over the previous month and went up by 1.37% from the same period last year. Pork price and gasoline price was the main driver of upward force to CPI with gain contribution of 0.34% and 0.1% respectively).These two factors are still the unpredictable ones which preventing Government from completing 4% inflation target in 2018. However, a 4% inflation this year is still within reach as Government can regulate price of public services. Nevertheless, it means inflation pressure will be huge for 2019. We expect that CPI in July may increase 0.3%-0.4%, which equivalent to 4.86%-4.97% yoy.
- According to GSO, the credit growth in the first half of 2018 was 6.35% ytd. It should be noted that this figure in 2017 was 7.54%. Also this growth was also lower than deposit growth. In addition, money supply M2 also grew faster than credit growth. These figures indicated abundant resources still available on banking system especially given the fact that (i) Public fund disbursement is still behind the schedule and (2) State Treasury still remained a huge amount of deposits in commercial banks.
- On the worldwide market, in June's FOMC, FED decided to raise interest rates for the second time in 2018. In addition, two more interest-liftings was also on the table for the remaining time of 2018. These days, spotlight was on trade war between US and China. However, we did not speak highly chance that tension will keep heating up for long time.
- Reference exchange rates and the exchange rated quoted by commercial banks ticked up and moved the same direction due to a temporary intermission in the supply of foreign currencies banknotes not only in Vietnam but also in the whole world. VCBS believe that short-term upward pressure on exchange rates still exists. However, there is still probability that VND devaluation in 2018 shall volatile in a band from 2%-2.5%, which is comparatively lower than regional countries.

Secondary Market

Market was extremely active in Q1 and became laggard in Q2.

VND 1,307,325bn (+35.5% yoy) was traded on secondary market.





Source: HNX, VCBS

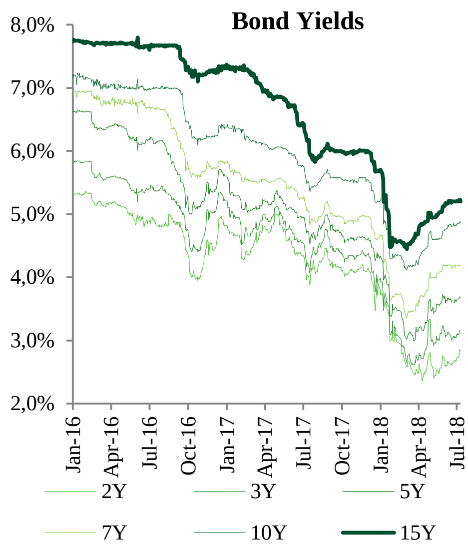
In 1H.2018 VND 1,307,325bn (+35.5% yoy) was traded on secondary market. In detail, outright values increased significantly to VND 624,131 bn (+22.54 yoy) while repo activities jumped to VND 683,194 bn (+49.53% yoy). Outright trading was very active in Q1 thank to ample liquidity in the banking system. However, outright activities cooled down in Q2. In terms of maturity, 1-5year bonds accounted for more than 50% of total outright trading volume and remained the most liquid on the market. Meanwhile, transactions at longer tenors (more than 10 years) accounted for 30%. Repo activity also rocketed in the first quarter in the context of low level of interbank rates.

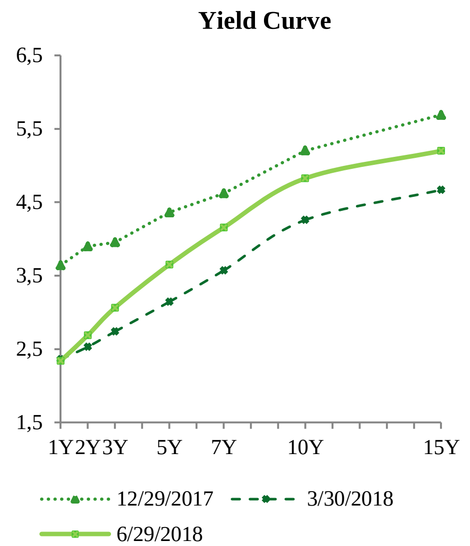
Against every market participant's expectation, bond yields ticked down strongly in almost all Q1.2018. Later on, bond yields were under upward pressure. Yield curve shifted downward and became steeper. According to Bloomberg, yields on 1Y, 2Y, 3Y, 5Y, 7Y, 10Y and 15Y terms ended Q2.2018 at 2.338% (-130.2 bps ytd), 2.688% (-121.2 bps ytd), 3.063% (-89.1 bps ytd), 3.65% (-71 bps ytd), 4.155% (-46.5 bps ytd), 4.825% (-37.9 bps ytd), 5.2% (-48.9 bps ytd) respectively.

Remarkably, the upward pressure in bond yields can be explained by the following reasons: (1) Rising concerns caused by macroeconomic factor changes (i) higher CPI, which may threaten a 4% target for 2018; (ii) concern about chance that a more tighten policy shall be applied; (iii) interest swap between USD and VND went below zero in the context of US 10Y bond kept surging and exceed 3% threshold- a psychological level; (2) There were times in Q2, the amount of ST's deposit in commercial banks temporary decreased.

For the second half of 2018, we speak highly chance that bond yield will move upward slightly. A short-term downward correction if any shall occur at the beginning of Q4.

At the present, with all factors mentioned above, we believe that upward force on bond yields still remained at least in Q3. Nevertheless, bond yields will only move upward roughly 50bps depended on tenors. The supporting arguments are as followed: (1) ST is not under pressure to mobilize bonds. (2) Although, no liquidity shortage is expected, and credit growth shall be slower than last year regarding the signal from SBV. (3) Public disbursement may slightly speed up though still behind the schedule.



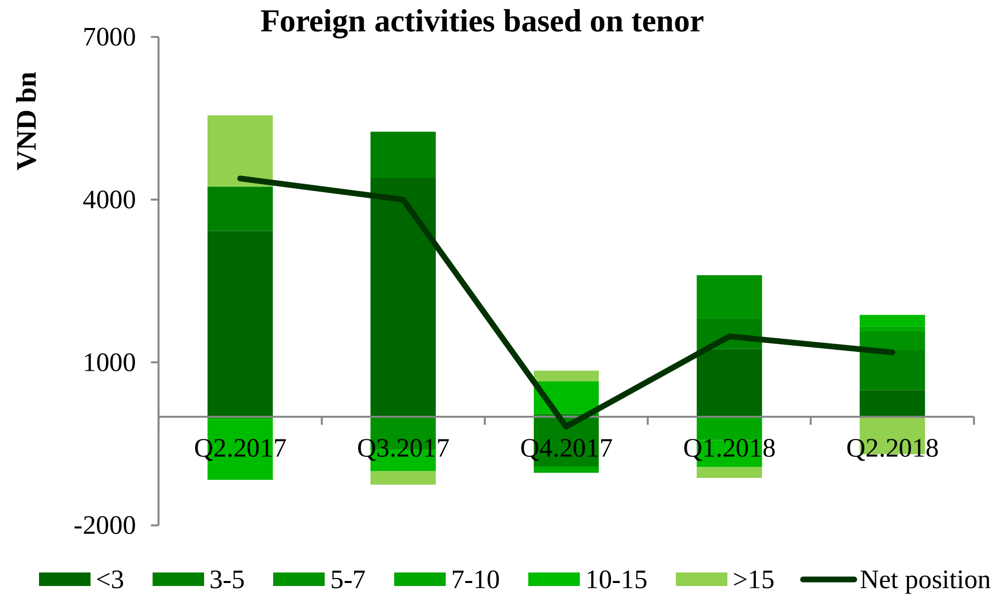


Source: Bloomberg, VCBS

We expect that a short-term downward correction if any shall occur at the beginning of Q4 because: (1) We anticipate that CPI growth in term of yoy will cool down and go below 4% threshold at the end of Q3. (2) Tension around worldwide matters may be released especially trade war between US and China. Demand for bonds did not change especially regarding the growth of insurance companies.

The foreign investors net buy approximately VND 2,666 bn in 1H.2018.

The foreign investors net buy approximately VND 2,666 bn. In 1H.2018, foreign though still recorded the net bought value in bond market, their trading size of the foreign was quite small to overall market and tended to shrink. In addition, in Q2, Foreign tended to sold long-term bond (10-15Y) and only purchased short-term bond to avoid risks because uncertainty rising fast this period.



Source: HNX,VCBS

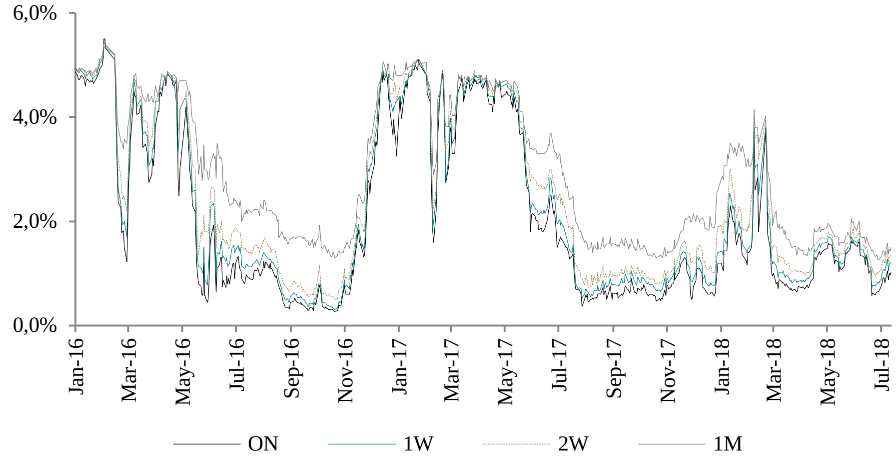
From 2H.2018, a faster procedure of tightening policy of FED has been recorded. This fact one way or another may impact the inflows to emerging markets like Vietnam. However, we believe that it will not hurt bond market much as foreign only accounted for roughly 5% trading value in secondary market. Also demand for bonds is still there, it is the problem of an unreasonable price, which prevented the foreign from investing in Bond market. Overall, with the above expectation of bond yields level, foreign trading on bond market shall be quiet.

INTEREST RATE

Interbank rates edged up frictionally in Q2.2018. Abundant resources remained in the market.

Interbank Rates

Interbank rates **settled stably at a low level in almost all Q1.2018.** The fact that interbank rate being at a low level allowed banks to make full use of this source to fund their bond trading. **Later on, in Q2, the average level of interbank edged up fractionally.** In details, at the end of 1H.2018, ON-3M rates posted at 0.65%, 0.817%, 1.017%, 1.267% and 2.167%.



Source: Bloomberg, VCBS

We believe that a slight higher in interbank rate in Q2 can be explained as followed: (1) Recently, there was concern about monetary inflation in the context of phenomenal growth in CPI in May and even June. It means, ST will less willing to keep huge amount of deposits in commercial banks. (2) Additionally, the purchase of foreign currencies by SBV was narrowed down because (i) less favorable condition while exchange rate edged up; (ii) Import raised at a slower pace and foreign currencies reserve logged in comfort zone of 12-15 week of import.

Nevertheless, a liquidity shortage did not happen because (1) Credit growth was slower than the same period and also slower than deposits growth rates; (2) Fund disbursement was sluggish. Till now only 13% value of bond mobilized in 2018 was cashed out. Hence, ST still have to remained certain deposit amount in commercial banks.

For the remaining time of 2018, although interbank rate may tick up slightly, liquidity shortage shall not happen.

In the next quarter as well as the remaining time of 2018, **although interbank rate may tick up slightly, liquidity shortage shall not happen**. First, (1) the disbursement of public investment may still behind the schedule. Besides, (2) although credit growth was slower than the same period last year, the recent upward force on exchange rate means some market participants can make full use of FX market to seek for profit. To sum up, we project a slight higher interbank rates for the second half of 2018.

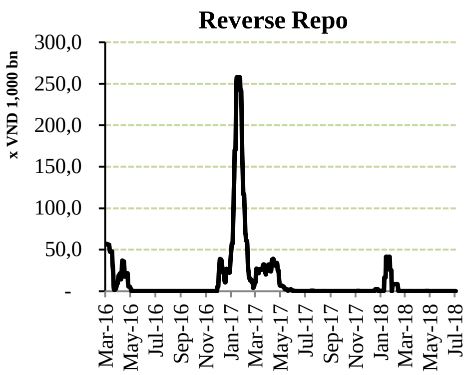
Open Market Operation

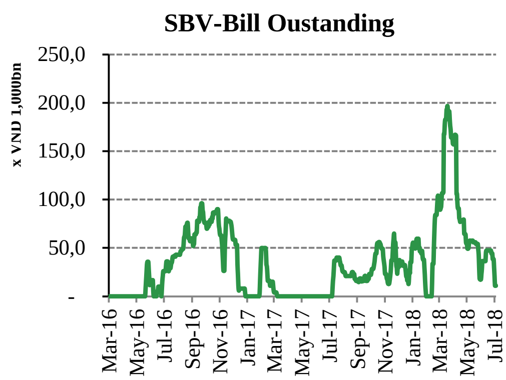
From April, SBV turned their position into net-injected through OMO market.

Not long after downward repo rate adjustment in Q1, repo rate rebounded to 5% in May Also from April, liquidity in the banking system was no longer too abundant. Hence, **SBV turned their position into net-injected through OMO market.** This was also the time, we experienced a higher rate applied for SBV-bills from 0.9% to 1.2% in 5th June and from 1.2% to 1.25% in 21st June for 28- day Bill.

In general, SBV net injected VND 143,810 in Q2.2018. In the first half of 2018, SBV net withdrew VND 31,266 bn.

In 2H.2018, same approach will be recorded by SBV. In detail, they may keep using Bills to absorb liquidity, cause by the forward buying foreign currencies contract. When it comes to reverse repo, SBV shall not need it much because we project no liquidity shortage.





Source: Bloomberg, VCBS

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APPENDICES

Primary Market

Month	ST Bond							VDB	VBSP	Other	
	Issued Volume	5 Y	7Y	10Y	15Y	20Y	30Y	Issued Volume	Issued Volume	Issued Volume	Issued Volume
17-Jun	22,348	4.9	5.19	5.65	6.25	6.55	7.1	0	0	0	22,348
17-Jul	15,170	4.48	4.8	5.38	5.75	5.82	6.22	0	0	0	15,170
17-Aug	3,179	4.6	4.8	5.38	5.75	N/A	6.1	0	0	0	3,179
17-Sep	4,086	4.65	4.85	5.4	N/A	N/A	6.1	0	0	0	4,086
17-Oct	6,910	4.5	4.85	5.42	N/A	N/A	N/A	0	600	0	7,510
17-Nov	2,931	4.52	4.88	5.42	5.75	5.82	6.1	4,000	500	0	7,431
17-Dec	1,900	4.52	N/A	5.28	N/A	N/A	N/A	9,745	208	0	11,853
18-Jan	19,365	4.3	4.35	4.38	4.5	5.2	5.4	0	0	0	19,365
18-Feb	10,015	3.05	3.4	4.2	4.4	N/A	N/A	0	0	0	10,015
18- Mar	11,028	2.97	3.43	N/A	4.4	5.1	5.42	0	0	0	11,028
18-April	6,055	2.97	3.43	4,1	4.47	5.12	5.42	0	0	0	6,055
18- May	11,178	3	N/A	4.26	4.6	5.14	N/A	0	0	0	11,178
18- June	**16,940**	**3.1**	**N/A**	**4.37**	**4.7**	**5.2**	**N/A**	**0**	**0**	**0**	**16,940**

Secondary Market

	Bonds		ST-bills		Total
Month	Outright	Repo	Outright	Repo	
May-17	92.439	90.118	-	-	182.557
June-17	116,510	99,280	-	-	215,790
July-17	109,831	101,694	-	-	211,525
Aug-17	104,593	112,190	-	-	216.783
Sep-17	117,431	90,153	-	-	207,584
Oct-17	104,614	106,158	-	-	210,772
Nov-17	88,676	110,552	-	-	199,228
17-Dec	107,063	118,739	-	-	225,802
18-Jan	118,223	118,127	-	-	236,350
18-Feb	73,893	100,365	-	-	174,285
18- Mar	118,614	149,163	-	-	267,777
18-April	117,127	140,244	-	-	257,371
18- May	83,940	104,896	-	-	188,836
18-June	**112,344**	**70,399**	**-**	**-**	**182,733**

Open Market Operation

Month	Reverse Repo				Outright (SBV Bills)			
	Due	Offer	Balance	Outstanding	Due	Offer	Balance	Outstanding
May-17	51,145	24,459	(29,686)	1,314	0	0	0	0
June-17	2,766	1,452	(1,314)	0	0	0	0	0
July-17	0	506	506	506	45,000	85,000	40,000	40,000
Aug-17	0	0	0	0	125,996	110,997	(15,000)	25,000
Sep-17	0	0	0	0	78,425	69,424	-9,000	16,000
Oct-17	0	0	0	0	75,299	113,300	38,000	54,000
Nov-17	223	223	0	0	72,205	83,105	10,900	64,900
17-Dec	169	2,435	2,266	2,266	159,441	110,941	-48,500	16,400
18-Jan	3,260	42,309	39,048	41,314	167,106	197,705	30,600	47,000
18-Feb	49,780	8,466	(41,314)	0	59,000	90,600	31,600	78,600
18- Mar	31	31	0	0	84,100	196,710	112,610	191,210
18-April	2	2	0	0	191,210	78,500	(112,630)	78,580
18-May	170	170	0	0	80,280	55,840	(24,440)	54,140
18- June	**0**	**0**	**0**	**0**	**54,140**	**47,400**	**(6,740)**	**47,400**

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