Vietnam markets update

Getting up to speed on investing in Vietnam's local capital markets

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Authors:

Amber Rabinov
Economist, International
+61 3 9273 4853
Amber.Rabinov@anz.com

Amy Auster
Head of International Economics
+61 3 9273 5417
Amy.Auster@anz.com

Our Vision:

For Economics@ANZ to be the most respected, sought-after and commercially valued source of economics research and information on Australia, New Zealand, the Pacific and Asia.

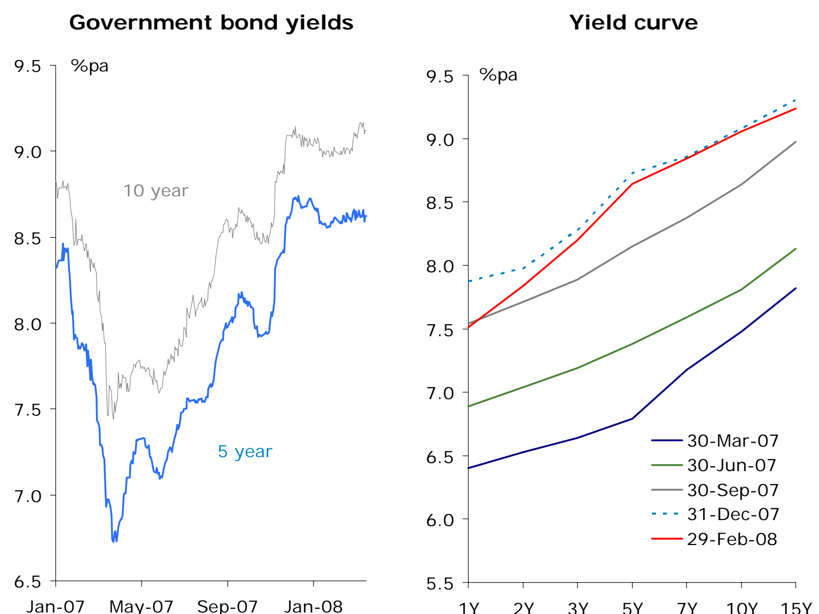
There is no doubt that Vietnam represents a compelling investment story. It is the newest tiger in the Asian compound, growing at a fast clip and drawing in ever-increasing trade and investment flows from around the world.

The year 2006 was a stellar one for Vietnam investors. The stock market more than doubled in value, and issuance in the bond market took off in an environment of declining yields. The year 2007 was more difficult. The stock market rose and fell through the year, though it ended up 23% for the year as a whole. Bond yields began rising in mid-year, spurred on by worsening data on the inflation front. Since the start of 2008, the equity market has fallen by 34% - wiping off all the gains of last year and turning in the worst performance in East Asia – while bond yields have remained near recent highs.

What is in store for 2008? We remain bullish on Vietnam as a long-term investment opportunity. Our expectation is that growth will soften this year, as it must in order to bring inflation under control. It should be a time for further reform, particularly in the area of monetary policy so as to ensure that price stability going forward. Assuming that the global economy does not enter a prolonged downturn, Vietnam should weather this storm and be set for further gains in asset prices as inflation begins to decline later this year. Demand for bonds, in particular, should remain strong – buoyed by the attractive yields on this BB-credit country.

To get up to date on the Vietnam story and informed about how to become involved, we offer the 2008 Vietnam market primer.

Figure 1: It's been a big year in the bond market



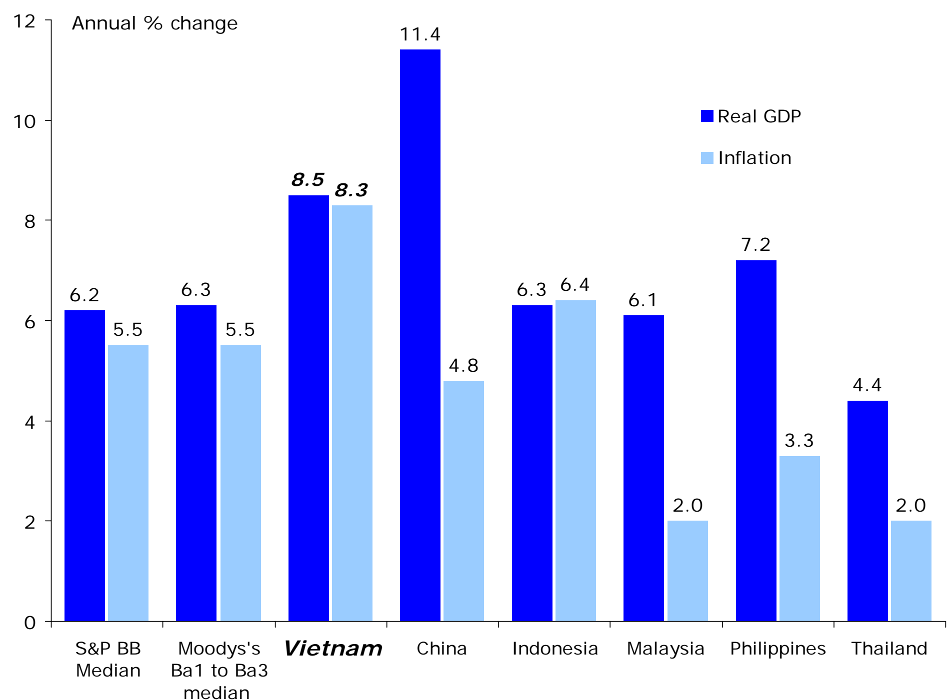
Source: Bloomberg

Economics brief

An attractive long-term Asia play

The rise of Vietnam is a powerful investment story. This country of 84 million people – the third most populous country in East Asia – has been transformed from a largely agrarian economy to an industrialised one in just a few decades. Since 1999 alone, the industry and construction sector has expanded at an average rate of 10.3% per annum to represent 42% of GDP by 2007 (up from 35% of GDP in 1999). As a comparison, the agriculture forestry and fishery sector has grown at an average annual rate of 3.8% over the same time period and its share of GDP has fallen to 18% in 2007 from 23% in 1999, despite the fact that this sector accounts for over half of Vietnam's total employment. By growing at a respectable average rate of 7.1% since 1999, the services sector has remained around 41% of GDP.

Figure 2: Real GDP Growth & Inflation in 2007



Source: S&P, Moody's, General Statistics Office, IMF, Economics@ANZ

Since 2000, the Vietnamese government has stepped up the pace of economic liberalisation. The country has managed to achieve real GDP growth of over 7½% per annum on average over this period, a performance second to only China. Going forward, strong growth is expected to continue, and given Vietnam's entry into the World Trade Organization (WTO) in 2007, the government will continue with reforms over coming years.

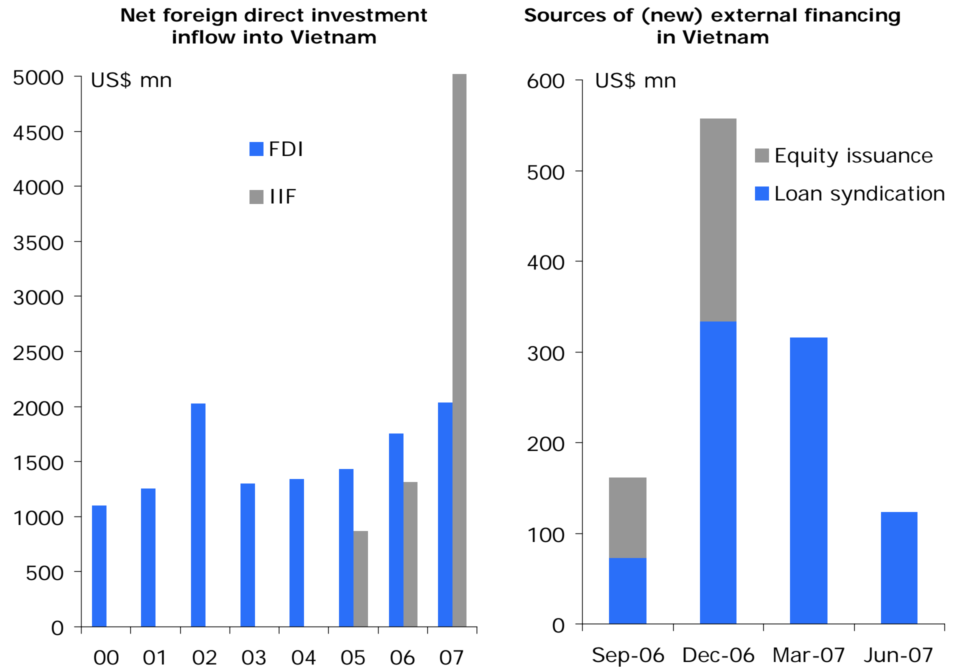
The opening of the economy to trade and investment flows has generated substantial inflows of foreign capital. Foreign direct investment is robust, with Vietnam rated the world's sixth most attractive location for FDI in 2007-09[1]. FDI commitments for new and existing projects reached US$20.3 bn in 2007 – just over 30% of GDP – although actual FDI flows are estimated at US$2.0 bn. The expansion of Vietnam's manufacturing capacity has attracted global multinationals to set up production in the country, apparel retailers Adidas and Nike, and chemical company ICI (manufacturer of the Dulux brand of paints).

Foreign inflows have also surged into the domestic capital markets thanks to the development of the bond market and growth of the equity market via initial public offerings of state owned enterprises (SOEs). The capitalisation of the Ho

[1] UNCTAD, *World Investment Prospects Survey*, 2007.

Chi Minh City stock exchange has risen from VND30 tr (US$2 bn or 3% of GDP) in June 2006 to a peak of VND373 tr (US$23 bn, or 37% of GDP) in November 2007, prior to the recent correction. According to local reports, share offerings could total more than US$1 bn in 2008[2].

Figure 3: Foreign capital is flowing quickly into Vietnam – and is now dominated by FII *



*FII is portfolio investment flows

Source: IMF, CEIC, Global Insight

Vietnam compares favourably to peers

From a country risk point of view, Vietnam compares favourably to its peers in many regards. Our 2007 report, "*Rating Vietnam: Solidly BB*" reviews the key factors supporting Vietnam's BB rating, and the below table compares key economic indicators in Vietnam to those of its similarly-rated peers.

As can be seen from the table below, Vietnam is still a poor country relative to its peers, but enjoys a higher growth rate and a comparable level of government debt relative to other BB-rated economies. With real GDP per capita of less than a third of its peers, Vietnam has considerably more upside potential in relation to its development potential, with much investment still needed, particularly infrastructure. However, the budget deficit of the government of Vietnam considerably exceeds the median of its peers, as does the current account deficit. The ability of the government to push forward investment to induce growth will be constrained; productivity gains and private sector investment are required.

Moody's agrees that Vietnam's credit strengths include a high rate of GDP growth, WTO membership and permanent normal trade relations status with the US, and substantial financial support from official aid programs. Credit challenges for Vietnam include the containment of government debt, the effectiveness of monetary and credit policy, timely implementation of state-owned enterprise and bank reforms, transparency and governance deficiencies, and relatively low per-capita income.

[2] Dow Jones, 'Foreigners allowed to use dollar funds to pay for IPOs' 25 February 2008.

Figure 4: Selected economic indicators

	2005	2006	2007e	S&P BB Median 2007e	Moody's Ba1 to Ba3 Median
GDP per capita (US$)	636	723	833	3,018	3,541
Real GDP (% change)	8.4	8.2	8.5	6.2	6.3
Real GDP per capita (% change)	7.0	6.8	6.9	4.9	na
General government balance (% of GDP)	-5.9	-3.8	-6.9	-1.3	-2.0
General government debt (% of GDP)	34.9	33.9	35.9	40.2	40.2
Current account balance (% of GDP)	-0.9	-0.3	-3.2	-2.0	-4.0

Source: S&P, Moody's, General Statistics Office, IMF, Economics@ANZ

Our key concern from a sovereign risk point of view is Vietnam's "twin deficits". It is one of the only economies in East Asia that has featured both a current account deficit and a fiscal deficit (using IMF's standard definition of the fiscal position) over the past few years. The budget deficit is estimated to have reached 6.9% of GDP in 2007 and is expected to remain above 6% of GDP this year, according to the IMF's recent Article IV report. Tax reform – including a new personal income tax to be introduced in January 2009 – should help to expand and stabilise tax revenue, while the continued strength in the price of oil will bolster government coffers.

Nonetheless, expenditure levels are high and are likely contributing to Vietnam's present high rate of growth. We also believe that loose fiscal policy is contributing to the major short-term and long-term risk facing Vietnam – inflation.

Inflation is the key near term and medium term risk

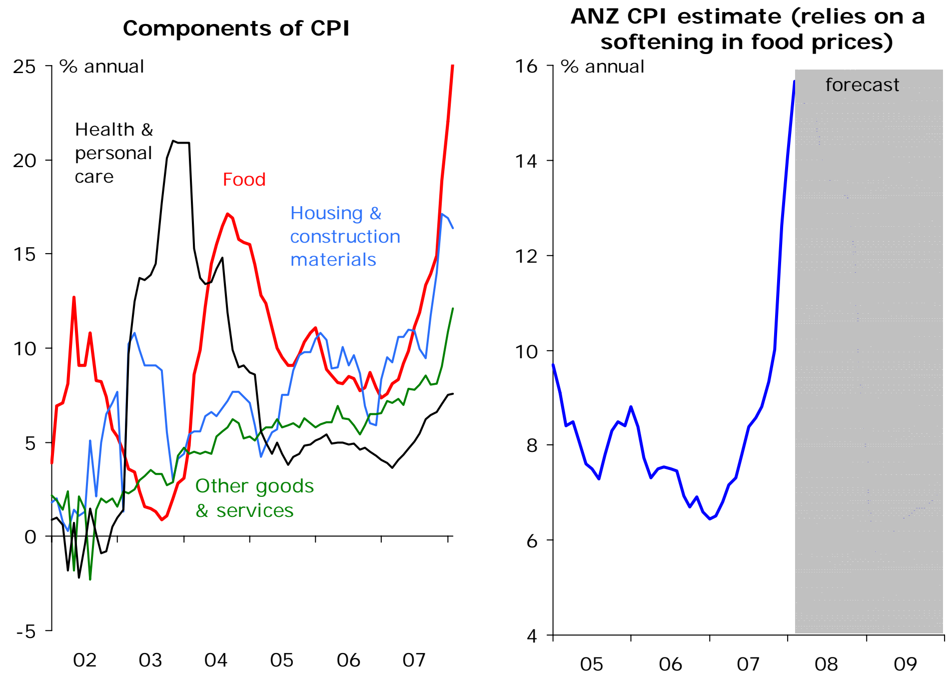
While Vietnam's long-term prospects are attractive, the immediate road ahead is throwing up a few speed bumps. Most recently, inflation has become problematic in Asia's newest tiger, and the relatively undeveloped state of policy tools to maintain price stability is posing a major challenge to the government and to asset prices.

The basis of Vietnam's current inflation problem is twofold. First, there are structural elements pushing inflation forward, including strong growth and high domestic liquidity. Secondly, the development of the macroeconomic policy framework – specifically, the coordination and effectiveness of fiscal and monetary policy – is relatively immature. These two factors have combined to push inflation in Vietnam to above 15% per annum as at February 2008.

On the economic front, rapid growth appears to be pushing Vietnam's capacity to satisfy domestic demand. Real GDP growth has exceeded the government's target for the past few years, and the government has again raised its target for GDP growth this year to 9% from 8½% in 2007. While productivity gains are contributing to real GDP growth, capacity constraints are now emerging in parts of the labour market, in hard infrastructure and in energy.

Although available data are insufficient to analyse the extent of capacity constraints, we do know that the average monthly income for workers in the state sector accelerated last year, from annual growth of 10.8% in 2006 to 12.8% in 2007. Higher wage inflation is a sure sign of a tight labour market – the key cause of structural inflation – and workers in the private sector are likely to have experienced an even greater degree of wage inflation. Accelerating retail sales growth – up 20% per annum on average over the past three years – also shows how rising incomes are spurring rapid increases in domestic demand.

Figure 5: Inflation - not all food



Source: CEIC, Bloomberg and Economics@ANZ

In addition to structural inflation, the economy has been flush with liquidity – which, all else being equal, will encourage inflation. System data are only available with a long lag, but as of June 2007 it appears that base money (measured by M2) was rising at an annual rate of 42.7%, and the IMF estimates full year growth of 37%, after rising by around 30% per annum in each of the previous three years. It is not surprising that credit growth in this environment has also been above 25% for each of the past four years.

Capacity constraints and high liquidity conditions have fuelled inflation, which has risen from a rate of 6.5% through the year to January 2007 to 14.1% in January 2008 and 15.7% in February 2008. The global phenomenon of rising food prices has hit hard: Vietnamese food prices rose 25.2% over the year to February 2008 from a rate of 7.4% at the start of 2007. Food comprises over 40% of the CPI basket. The boom in the real estate sector has caused housing and construction materials prices to soar 16.4% over the year to February 2008, while energy prices have pushed transport and communications costs up and medical products and health care prices have also increased.

Fiscal policy may have well added to the incipient causes of inflation in Vietnam, as the government's expenditure on major projects would have accelerated the demand for building materials. While there is no doubt that Vietnam needs to build more capacity in hard infrastructure, the widening trade deficit is evidence of the pressures that this rapid build is putting on the economy. A tightening of fiscal policy has been under discussion, but would need to be implemented soon in order to have a significant impact on inflation this year.

Vietnam's approach to monetary policy

Complicating the outlook for inflation is the fact that management of monetary policy is undergoing a transformation in Vietnam. The efficiency of this process has significant implications for asset prices in the local market. The following section details the recent history of monetary policy management and our expectations as to how State Bank of Vietnam's (SBV's) approach to monetary policy and inflation may change going forward.

Historic focus on managing the exchange rate

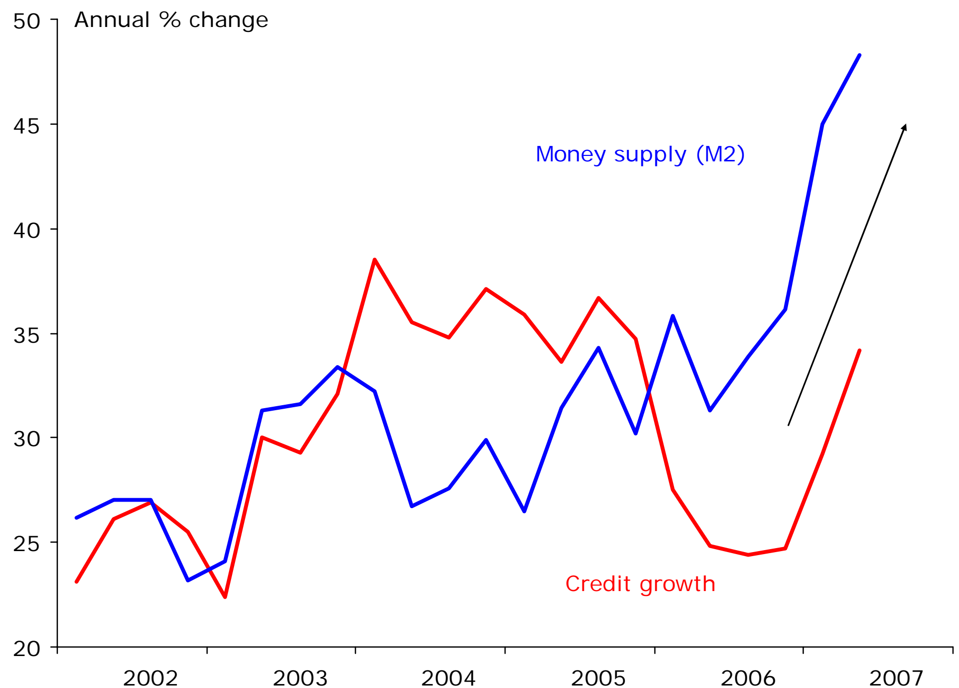
Historically, Vietnam's financial system could be characterised as heavily regulated to cross border capital flows, while also being highly dollarised, as

more than 30% of the deposit base was denominated in foreign currency. Monetary policy was set through control of the exchange rate, as a way to influence the price of imported goods. Vietnam's imports are equivalent to more than 80% of GDP – of which a high percentage is energy and intermediate goods – making the price of imported goods quite important for the economy.

As part of Vietnam's process of economic liberalisation and reform, the government has progressively liberalised the capital account to allow more funds to flow into and out of the economy for trade and investment purposes. The result of Vietnam's very strong growth prospects and open capital account has been massive capital inflows.

While the rate of foreign capital inflows into the Vietnamese economy accelerated at a rapid rate over the past three years, the central bank maintained a weak dong policy, originally set up in the 1980s to promote export competitiveness. Over the past few years, this policy combined with massive foreign capital inflows has seen a rapid build-up of liquidity in the local market. In the past several months, the SBV appears to have recognised the need to shift its policy objectives and implementation, and has started to adjust policy accordingly.

Figure 6: Growth in credit and the money supply ticked up in 2007



Source: CEIC

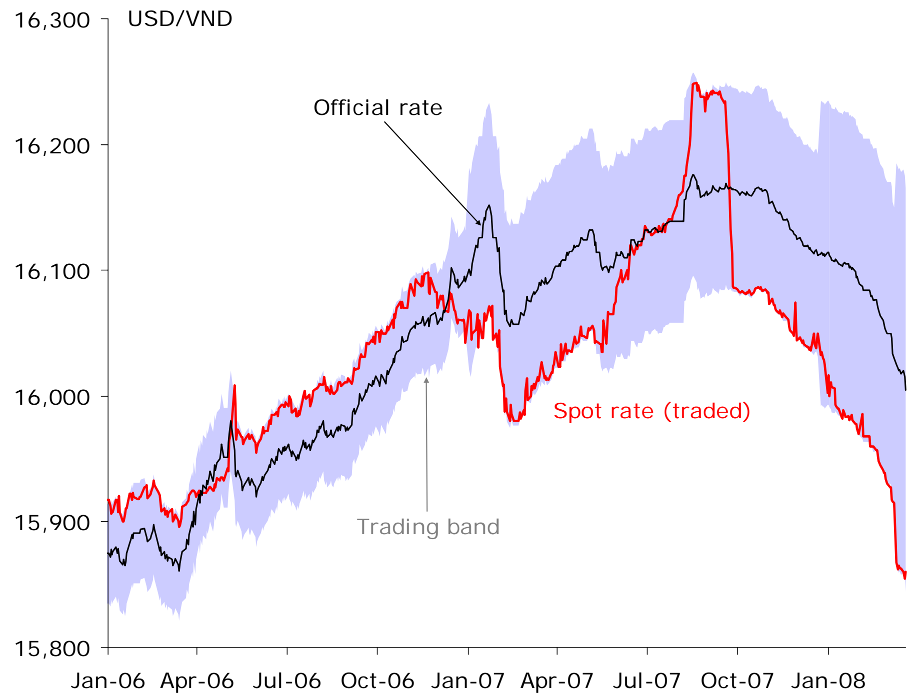
A modern approach to monetary policy by the SBV would entail moving toward a focus on interest rates rather than on the US dollar / Vietnamese dong exchange rate as an anchor for inflation expectations. This process, however, takes time and its implementation is complicated by the fact that the SBV is not an independent body with a sole mandate to maintain price stability in the economy.

Dong has begun to appreciate, and this will accelerate

As a first step, the SBV has abandoned its policy of targeting a very slight nominal depreciation of the dong against the US dollar on an annual basis. The dong trades within a band that is set by the SBV, and the SBV intervenes heavily in the market. The SBV has widened the band within which the dong trades three times over the past fourteen months: at the end of 2006 (to plus or minus 0.5%), again in December 2007 (to plus or minus 0.75%), and once more in March 2008, such that the daily USD/VND spot rate can now fluctuate in a range of plus or minus 1% from a rate set each morning by the Bank, versus a range of plus or minus 0.25% set between 2002 and 2005. On 4 March 2008,

the Deputy Prime Minister issued a directive on behalf of Prime Minister Nguyen Tan Dung to the SBV to widen dollar-dong trading band to plus or minus 2% from the official rate set by the SBV each morning. The timing of this change is yet to be confirmed, with the SBV and government yet to discuss the details of the proposed change.[3] The dong has appreciated to around VND/USD 15,860 at the time of writing, the strongest the currency has traded at since mid 2005.

Figure 7: USD/VND – recent movements



Source: Bloomberg, Reuters and Economics@ANZ

We expect the pace of dong appreciation to accelerate in the first half of 2008, and are forecast a rate of USD/VND15,500 by June 2008, and USD/VND15,345 by December 2008. Accelerated appreciation will help tame the price of imported goods, although the impact will not be all that significant given that the rate of appreciation is still quite slow.

The currencies of all of Vietnam's major trade partners have appreciated against the US dollar over the past six months. Indeed, there is arguably far more room for the currency to appreciate. According to our currency forecasts, despite the expected appreciation of the dong against the US dollar for 2008, the dong is expected to depreciate by more than 5% on a nominal basis against the euro, the yen, the renminbi and the Singapore dollar over the course of 2008.

Observers such as the IMF have argued that this is a propitious time for a move toward a more flexible exchange rate, which among other things would encourage the development of a derivatives market such that market participants could hedge currency risk and ultimately reduce their vulnerability to exchange rate volatility. However, thus far the Vietnamese authorities have emphasised their desire for a stable exchange rate over a flexible one.

Liquidity tightening measures are having greater impact

In addition to shifting the exchange rate regime, the authorities have implemented other measures to reduce the build-up in system liquidity. These are having a far greater impact on the financial system and capital markets in Vietnam than the exchange rate movement, and we expect this dynamic to continue for at least several months.

[3] In the days following this announcement, the SBV widened the dollar-dong trading band to plus or minus 1%. At the time of writing, no further news regarding the widening of the trading band to plus or minus 2% has been reported.

First, the SBV raised interest rates in January, encompassing the base lending rate (from 8.25% to 8.75%), the discount rate (from 4.5% to 6%), and the refinance rate (from 6.5% to 7.5%). It subsequently raised the reserve requirements for credit institutions. For dong and foreign currency deposits up to one year (including demand deposits), the compulsory reserve rate is now 11% versus 10% previously, with the reserve rate on deposits of more than 12 months raised to 5% from 4%.[4] The authorities also acted to cool asset prices by changing lending restrictions for securities investment from 3% of total loans outstanding to 20% of charter capital, which limits the potential growth in volumes for such investment credit.

In response to the acceleration in inflation and higher cost of funds, the yield on 5-year government bonds has risen from 7.95% as of October 2007 to 8.6% at present, while the 10-year government bond yield has risen from 8.47% to 9.0% over the same period. Meanwhile, the equity market has declined by around 30% since the start of this year (see below).

In a further effort to tighten liquidity, a proposal was floated in late February to require all commercial banks (state-run, joint-stock banks and some foreign banks) to participate in a one-year government bond issue at 7.8% (below the rate of inflation but above current yields) on 17 March. The bond issue is meant to drain approximately US$1.3 bn (VND20.3 tr) from the market, equivalent to 1¾% of total GDP in 2007. The announcement was followed by rapid increases in deposit rates to the level of 11-12% and a huge spike in overnight interest rates. While rates have since eased, it does seem that the days of flush liquidity are coming to an end.

Dollarisation still an issue

Although the SBV is on the road to shifting its inflation anchor away from the USD/VND exchange rate and toward benchmark interest rates, that transition is not yet complete. One issue in particular for Vietnam is the degree of "dollarisation" in the financial system, with foreign currency-denominated deposits still representing around 24% of total deposits (according to the latest June 2007 data). Although this is down from a peak of 45% in September 2001, the extent of dollarisation still has the ability to interfere with the transmission of monetary policy to the economy. Allowing for a faster rate of dong appreciation against the US dollar as well as higher nominal interest rates is appropriate for Vietnam's present rate of growth and inflation, and would also encourage the de-dollarisation process to ultimately make monetary policy more effective.

However, the squeeze on liquidity that is creating a shortage of both foreign currency and dong – and a factor in the falling equity market – led the government to announce that Prime Minister Nguyen Tan Dung has approved a Ministry of Finance proposal to allow foreign investors to use US dollars to pay for IPOs due to the lack of sufficient available dong. Separately, it was also reported that special permission was granted to a global bank to pay US$217mn in US dollars for a 10% stake in PetroVietnam Finance Corp, instead of making the payment in dong, as is normally required by law.[5]

Our forecast

Going forward, we expect:

- Accelerated appreciation of the currency from around USD/VND15,930 at present to around USD/VND15,500 by mid year and USD/VND 15,350 by the end of 2008. This represents a nominal appreciation of 4.2% against the US dollar for 2008 versus an appreciation of 0.2% over 2007 and a depreciation of 0.87% over 2006.

[4] In March 2008 the government requested the SBV to consider increasing bank reserve requirements further in order to reduce liquidity, although no news of such action has been reported at the time of writing.

[5] Amy Kazmin, 'Vietnam's currency crisis causes headaches,' *Financial Times*, 26 February 2008. Foreign companies are also finding it a challenge to convert much smaller amounts of foreign currency into local currency to pay for staff salaries, for example.

- Sideways or upward movement of bond yields, with yields on 5-year government bonds unlikely to fall below 8.5% again this year. Fundamentally, a discount rate of 6% and average annual inflation of no less than 7% suggests 5-year bonds yields should be above 10%. Demand will continue to depress yields, but a rally is unlikely.
- Ongoing tight liquidity. Now that a reduction in liquidity has been achieved, the system will need to face some deleveraging. Some consolidation in the banking system may be required.

2008 forecasts

Our forecast is for the rate of growth in Vietnam to slow this year, albeit to a still fast clip of 8%. The slowdown will be driven by tighter liquidity and falling credit growth out of the banking system, while there may also be a tightening of fiscal policy. This is essentially the end of the business cycle for Vietnam; a time to pause and regather after more than five years of extremely strong growth.

Although concerns about inflation are expected to persist for the coming three to six months, we do anticipate a light at the end of the tunnel toward year-end. Our forecast is for annual inflation to ease from 15.7% in February to 9.7% by December this year, for several reasons. First, we expect oil prices to decline from present record highs in the second half of this year, and are forecasting a year-end price for West Texas Intermediate (WTI) of US$80/bbl. Falling oil prices will bring relief not just to energy users, but also to the global trend in food inflation that has posed a significant problem in Vietnam. We also expect the stronger pace of currency appreciation to help dampen imported inflation, and for retailers to look to modify price rises as the domestic economy slows down. Finally, the annual rate of inflation should temper with the base effect.

There are two key risks to our forecast, and both present a downside risk to growth. The first is that the global environment remains overwhelmingly negative, such that foreign investment flows into Vietnam begin to reverse. The Vietnamese economy has benefited mightily from foreign capital inflows, and would similarly suffer in the other direction upon their reversal. The second key risk is that inflation does not moderate as we anticipate, and the central bank either must cause growth to slow precipitously, or adopt regulations that would ultimately lead to distortions in the economy.

The table below presents our macroeconomic forecasts for Vietnam.

Figure 8: Economic forecasts

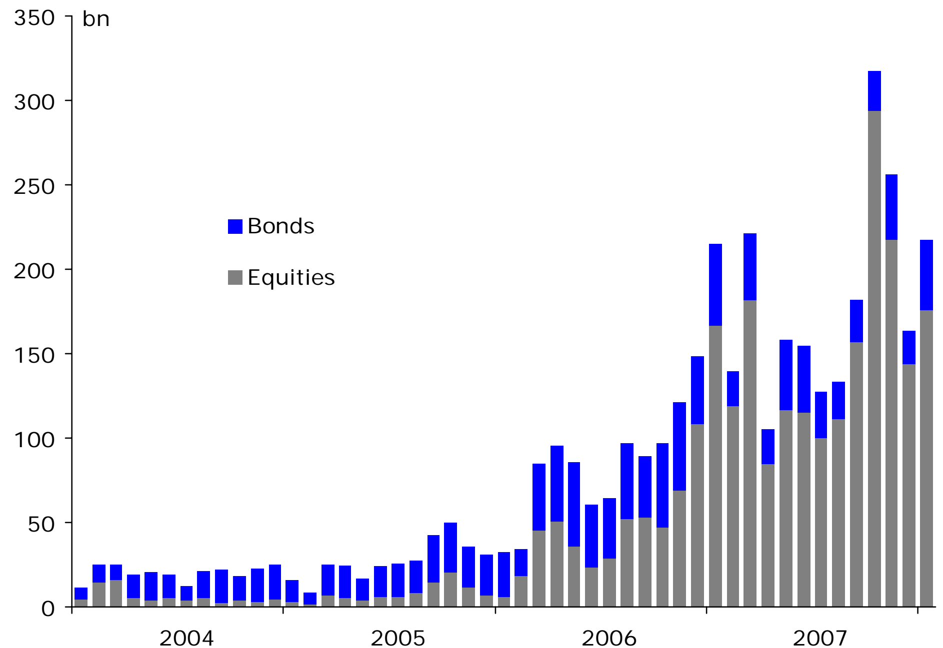
	2006	2007e	2008f	2009f
Nominal GDP (US$ bn)	60.9	71.1	86.6	98.4
Real GDP growth (%)	8.2	8.5	8.0	7.5
Inflation (%)	7.4	8.3	13.8	6.6
Exports (%)	22.9	22.2	19.1	16.2
Imports (%)	20.4	37.0	19.0	16.0
Industrial production (%)	18.0	16.7	16.0	16.5
Current account (% of GDP)	-0.3	-3.2	-3.2	-3.5
FX reserves (US$ bn)	13.4	20.0	31.0	35.0
VND/USD (period end value)	16,056	16,017	15,345	15,500

Source: IMF, Economics@ANZ

Capital markets

The rise of Vietnam as the next dynamic growth story of Asia has coincided with the rapid growth of its domestic capital markets. Vietnam's equity market capitalisation has grown from a miniscule US$470 mn at the end of 2003 (or 1.3% of GDP) to US$9.4 bn (15.4% of GDP) at the end of 2006 and US$24.9 bn (35% of GDP) at the end of 2007.

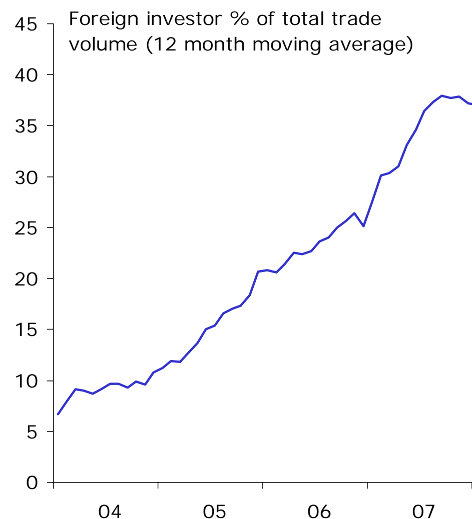
Figure 9: Rising capitalisation and trading volumes in HCMC

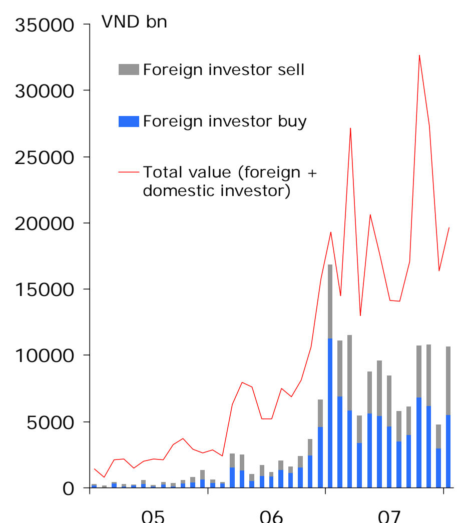


Source: CEIC

Foreign investors are an increasingly important part of this market, now representing 40% of the total trading volume in the HCMC stock exchange. Foreigners also represent a significant share of holders of outstanding bonds, with the IMF estimating that foreigners held around 55% of outstanding government bonds in 2007. The chart below highlights the volume of foreign activity in the equity market in recent years. While the equity market has gained a lot of popular attention, the growth of the bond market has also been important.

Figure 10: Foreign participation in Vietnam's domestic securities market has grown significantly, but has levelled off since late 2007



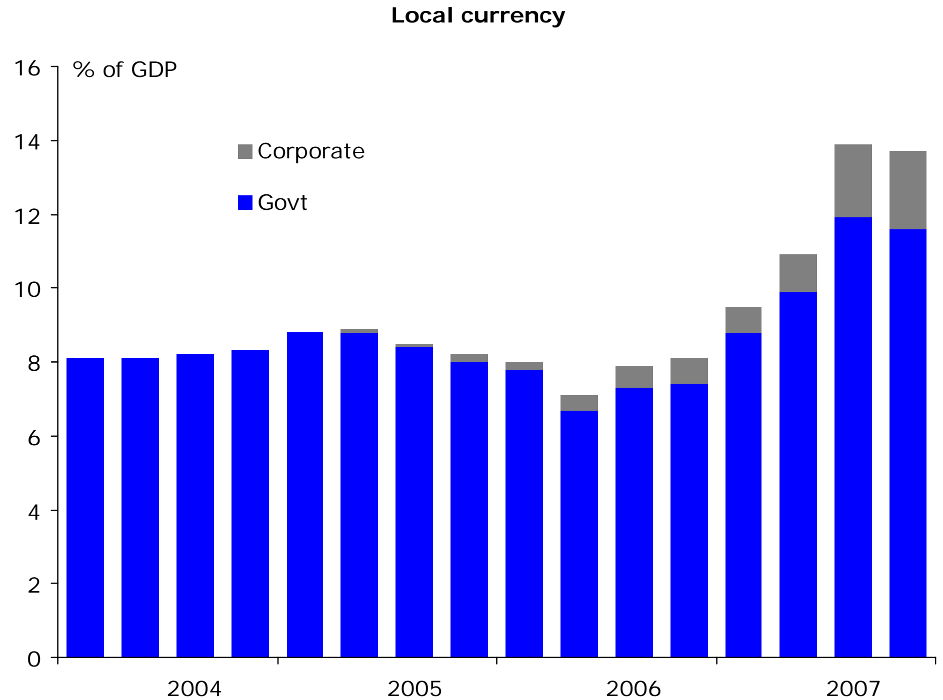


Source: CEIC, Economics@ANZ

Bond market

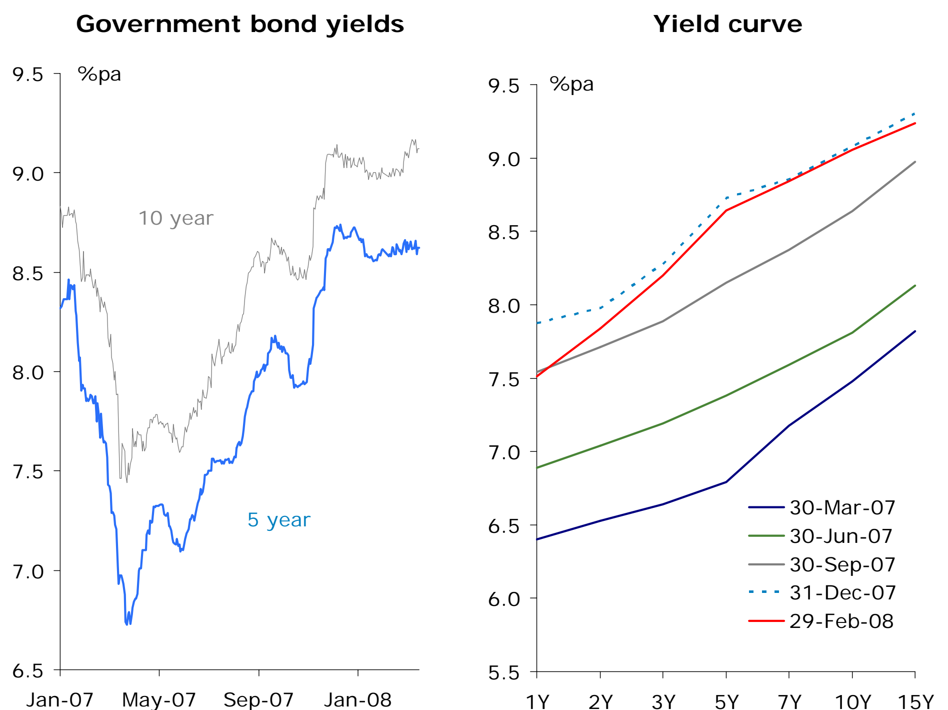
Vietnam's debt market is dominated by government securities, with maturities of less than one year right through to fifteen years. Treasury bill, government bond and corporate bond markets are open to both onshore as offshore investors. The stock of outstanding debt has risen significantly, from less than 8% of GDP in 2006 to about 14% of GDP (US$9.6 bn) at present.

Figure 11: Bonds outstanding in the Vietnamese market



Source: Asia Development Bank

Figure 12: Yields responding to inflation pressures



Source: Bloomberg

The performance of bonds has been mixed. Yields declined in the first half of last year, but subsequently rose in response to rising inflation concerns. Since December 2007, yields have settled, with the falling equity market perhaps boosting demand.

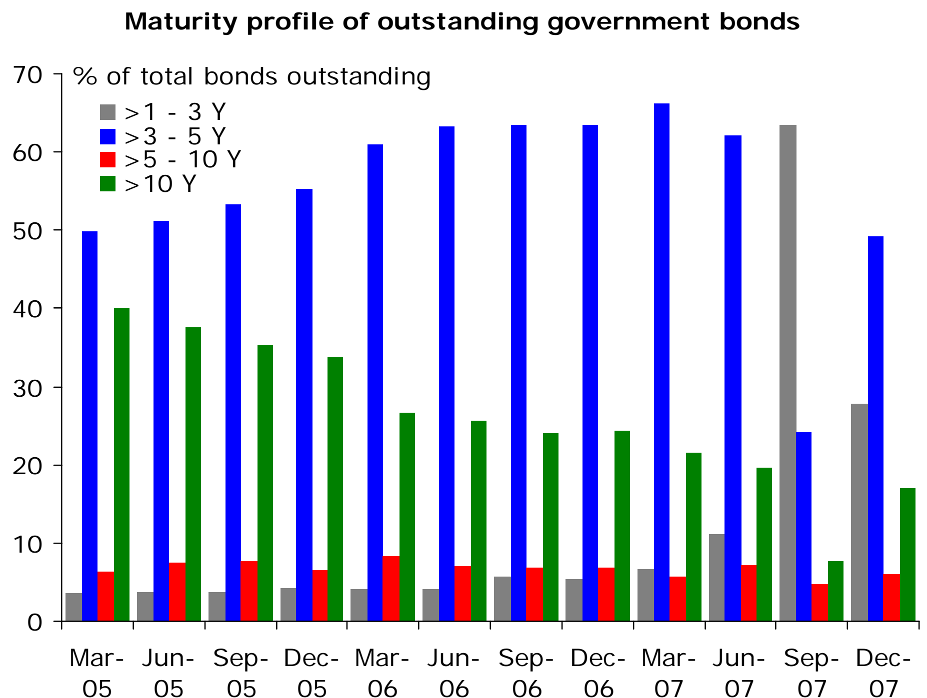
Despite the rise in yields, offshore demand for Vietnam government bonds has also remained strong in light of the attractive yields to be had on sovereign, BB-rated paper.

Government debt

There are two issuers of Vietnamese government bonds: the Vietnam Development Bank and the State Treasury. Since July 2006, all VND-denominated government bonds have been listed.

A number of different government securities are issued: Treasury bonds; central project bonds; foreign currency bonds; government-guaranteed bonds; and municipal bonds. Bonds are issued in two, three, five, seven, ten and fifteen year terms, with the majority being five-year terms. We estimate that the government issued VND50 tr worth of debt, and believe issuances in 2008 will be at this level or higher. While banks tend to dominate and be the largest investors in the five-year bond market, insurance companies tend to focus on the longer-term bonds.

Figure 13: Three to five year bonds remain the market favourites



Source: Asia Development Bank

Corporate debt

Corporate bond issuance in Vietnam has enjoyed superb growth since the first issuance in September 2003 by PetroVietnam, and is one of the fastest growing fixed income markets in Asia. The market has grown from around VND9 tr (US$560 mn) in 2006 to over VND36 tr (US$2.2 bn) in 2007. Listed VND corporate bonds tend to issue fixed rate bonds with senior unsecured collateral. Only two of the early issuances by Electricity of Vietnam in 2005 and 2006 used a floating rate coupon. In the current market, the majority of corporate bond issues in Vietnam remain unlisted as the listing process is both lengthy and costly. Moreover, it is not a prerequisite for bonds to be listed in the VND corporate bond market.

Appendix – market details[6]

Government debt

State Treasury bonds enjoy higher liquidity than VDB bonds, and therefore tend to be more popular with foreign investors. State Treasury bonds are issued via auction or underwriting, with two auction and two underwriting sessions generally held per month. To participate in auction sessions, banks must obtain membership as a primary VND government bond dealer.[7] Offshore investors can participate in primary issuances through authorised onshore dealers. Settlement is T+1/2 and listing takes approximately two weeks from the trade date. Prior to listing, bonds cannot be traded, and are only transferred to the custodian accounts of offshore investors once they are listed. To participate in underwriting sessions, investors can leave orders with participating dealers. The method for allocations depends on market conditions, and can be on a pro rata or a purely pricing basis; settlement is T+1/2 and the same rules for listing apply as in the case of auctioned bonds.

While the stock of outstanding government debt is rising, the secondary market is still catching up. The traded volume of bonds on the Ho Chi Minh City (HCMC) Securities Trading Centre has declined since the beginning 2007, in stark contrast to the ever-climbing volume of equities traded. This is mainly due to the fact that the size of the bond issues tend to be small. Most investors tend to hold onto bonds after their purchase.

The government of Vietnam launched its single global bond in October 2005. Launched in the US, the US$750 mn issue carried a coupon of 7.25% and was six times oversubscribed, with interest predominantly coming from banks and insurance companies in Asia (38% of total demand), the US (32%) and the EU (32%).

Corporate debt

Listed VND corporate bonds may be traded in the secondary market on either the Hanoi Security Trading Centre or HCMC Stock Exchange. However, secondary trading of corporate bonds is very underdeveloped and as such there is not sufficiently liquidity in the market to allow for the estimation of corporate bond yield curves. Corporate bonds do not tend to be rated by the major credit agencies. Only the Bank for Investment and Development of Vietnam (BIDV) is rated by Moody's, which upgraded BIDV's long-term debt a rating to Ba2 (stable) in May 2006 from Ba1.

In 2005 and 2006, the major issuers of corporate debt were Electricity of Vietnam (total debt issued of VND3.7 tr) and the Bank for Investment and Development of Vietnam (VND4.5 tr). In 2007, the number of corporate bond issuers multiplied rapidly. However, no corporate bonds have been issued since late December 2007 due to tight liquidity and market disruption generated by the uncertainty surrounding future monetary policy actions by the SBV in its attempts to rein in inflation.

To participate in primary VND non-listed corporate bond offerings, offshore investors must have an approved capital account by the SBV, and can subsequently receive an allocation along with the bond purchase agreement (BPA). The BPA is prepared by the underwriter, and is executed one day prior to the settlement date. Settlement is usually T+5.

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[6] The information in this section has largely been prepared by Shaun Horton, Analyst FI Origination and Pham Duong Hieu, Senior Manager FI Sales.

[7] ANZ has primary dealer status for State Treasury auctions.

Figure 14: Significant Vietnam Corporate Bond Issuances - 2007

Issuer name	Amount (VND bn)	Coupon	Issue date	Maturity	Type	Collateral
Vietnam Shipbuilding Industry Group	500	10	05/01/2007	05/01/2012	Straight	Senior unsecured
Vietnam Shipbuilding Industry Group	1000	10.5	18/01/2007	18/01/2017	Straight	Senior unsecured
Vietnam Machinery Installation Group	500	9.6	05/03/2007	05/03/2012	Straight	Senior unsecured
Vietnam Shipbuilding Industry Group	3000	9	13/04/2007	13/04/2017	Straight	Senior unsecured
Vietnam Steel Corp	400	9.5	10/05/2007	10/05/2012	Straight	Senior unsecured
Vietnam Machinery Installation Corp	1000	9.2	06/06/2007	06/06/2017	Straight	Senior unsecured
Ho Chi Minh Infrastructure Investment JSC (CII)	500	10.3	09/07/2007	09/07/2014	Straight	Senior unsecured
Bank for investment and Development of Vietnam	3000	8.15	23/07/2007	23/07/2012	Straight	Senior unsecured
Vietnam Technological and Commercial Joint Stock Bank	1750	8.6	31/08/2007	31/08/2012	Straight	Senior unsubord.
Vietnam Shipbuilding Industry Group	3000	9.4	20/09/2007	20/09/2017	Straight	Senior unsecured
Thang Long Securities	300	9	22/09/2007	22/09/2009	Straight	Senior unsecured
Asia Commercial Bank Vietnam	2250	8.6	25/09/2007	25/09/2012	Straight	Unsubord.
Vietnam Electricity Construction JSC (VNECO)	500	10.05	28/09/2007	28/09/2012	Straight	Senior unsecured
Vincom JSC	1000	10.3	22/10/2007	22/10/2012	Straight	Senior unsecured
Sacomreal	500	9.8	31/10/2007	31/10/2012	Straight	Senior unsecured
Thang Long Securities	200	9	27/11/2007	27/11/2009	Straight	Senior unsecured
Vietnam Expressway Highway Development and Investment Co.	400	9	28/11/2007	28/11/2022	Straight	Govt guarantee
Saigon Commercial Bank	1400	8.5	2/12/2007	5/12/2009	Convertible	Senior unsubord.
Sacomreal	500	10	10/12/2007	10/12/2012	Straight	Senior unsecured
Vinacomin	1500	9.5	11/12/2007	11/12/2017	Straight	Senior unsecured
Vinacomin	1500	9.5	11/12/2007	11/12/2017	Straight	Senior unsecured
SATRA	1000	9.6	15/12/2007	15/12/2012	Straight	Senior unsecured
Asia Commercial Bank Vietnam	1920	8.7	20/12/2007	20/12/2010	Straight	Senior unsubord.
Minh Phu Seafood	200	9.98	21/12/2007	21/12/2012	Straight	Senior unsecured

Source: ANZ

Tax implications

For offshore investors, bond holders are required to pay withholding tax of 0.1% on both principal and coupon (at any coupon rate). When selling bonds, there is also a 0.1% withholding tax on the settlement amount. There is no corporate income tax for offshore investors.

Foreign exchange market at a glance

As in Vietnam's bond and capital markets, the foreign exchange (FX) market is quite limited, with restrictions applying to onshore trading in spot, forward FX, FX swaps and FX options. Offshore trading in forward FX and FX swaps is permitted if the party has an investment in Vietnam. Trading of non-deliverable forwards is not permitted in Vietnam.

The SBV sets ceiling and floor rates for the USD/VND spot rate, as well as for forward rates. There are no restrictions on other foreign currency rates versus the dong in either the spot or forward markets. The minimum tenor in the forward market is three days, and the maximum tenor is 365 days. No documentation is required to convert portfolio investment into dong, nor to repatriate capital.

The onshore money market is liquid, but it is not available to offshore participants. Interest rate trading is very limited, with forward rate agreements and interest rate options unavailable, and the markets for interest rate swaps and cross currency swaps very illiquid.

The table on the following page summarises various features of the markets.

Figure 15: Features of Vietnam's markets

Instrument	Onshore	Offshore
Spot	• SBV announces daily official USD/VND rate • Trading band set at +/- 0.75% versus setting rate • Other spot FCY/VCD exchange rate is decided by banks • Sales of VND versus foreign currency must be supported by required documentation • FX fee is not allowed	Very limited non-deliverable market
Outright Forward	• Sales of VND must be supported by authorised business purpose • Contracts only allowed between three and 365 days • The forward or swap USD exchange rate shall not exceed the rate determined by (i) the spot USD exchange rate at the day of forward or swap agreement (ii) difference between VND base rate announced by SBV and US Fed funds target rate (iii) period of the agreement • FX fee is not allowed	Very limited non-deliverable market
FX Swap	• As per outright forward but individuals may not enter into FX Swap transactions • The forward or swap USD exchange rate shall not exceed the rate determined by (i) the spot USD exchange rate at the day of forward or swap agreement (ii) difference between VND base rate announced by SBV and US Fed funds target rate (iii) period of the agreement	None
Non-Deliverable Forward	• Not applicable	Growing offshore market on VND NDF/NDS
FX Options	• Only small number of banks have licence to do VND options • Very few deals have been written • Strike price cannot exceed outright forward rate for same tenor • There is no limitation on non-VND CCY options	None
Money Market	• Liquid short term interbank market up to three months • Market hardly trades above three months	Not available
SBV Bills	• Issued regularly by the SBV • Tenors up to one year	No limitation on participation of offshore investors
Government Bonds	• Largest issuers of debt are National and Local Govt debt securities • Govt bonds are issued mainly by State Treasury and the Vietnam Development Bank (VDB) • Market beginning to develop in bonds issued by state owned enterprises	No limitation on participation of offshore investors
Corporate Bonds	• Corporate bond market limited and approval must be gained from SSC for SOE • Currently none on issue • Secondary market limited but has grown significantly in the last two years	Purchase and sale of securities by foreign investors is limited and must be conducted via securities companies
Forward Rate Agreements	• No VND FRAs	No access
Interest Rate Swaps	• Market in infancy stage	Need approval from regulators
Interest Rate Options	• None written onshore	Need approval from regulators
Cross Currency Swaps	• Market in infancy stage	Need approval from regulators

Source: ANZ

Contacts

ANZ Research

Saul Eslake Chief Economist +61 3 9273 6251 Saul.Eslake@anz.com	**Fiona Allen** Business Manager +61 3 9273 6224 Fiona.Allen@anz.com			
Tony Pearson Head of Australian Economics +61 3 9273 5083 Tony.Pearson@anz.com	**Mark Rodrigues** Senior Economist, Australia +61 3 9273 6286 Mark.Rodrigues@anz.com	**Riki Polygenis** Economist, Australia +61 3 9273 4060 Riki.Polygenis@anz.com	**Dr. Alex Joiner** Economist, Australia +61 3 9273 6123 Alex.Joiner@anz.com	
Julie Toth Senior Economist, Industry +61 3 9273 6252 Julie.Toth@anz.com	**Wain Yuen** Economist, Industry +61 3 9273 6295 Wain.Yuen@anz.com			
Amy Auster Head of International Economics +61 3 9273 5417 Amy.Auster@anz.com	**Jasmine Robinson** Senior Economist, International +61 3 9273 6289 Jasmine.Robinson@anz.com	**Amber Rabinov** Economist, International +61 3 9273 4853 Amber.Rabinov@anz.com		
Paul Braddick Head of Financial System Analysis +61 3 9273 5987 Paul.Braddick@anz.com	**Ange Montalti** Senior Economist, Financial System Analysis +61 3 9273 6288 Ange.Montalti@anz.com	**Dr. Alex Joiner** Economist, Financial System Analysis +61 3 9273 6123 Alex.Joiner@anz.com	**Stephanie Wayne** Research Analyst, Financial System Analysis +61 3 9273 4075 Stephanie.Wayne@anz.com	
Warren Hogan Head of Markets Research +61 2 9227 1562 Warren.Hogan@anz.com	**Katie Dean** Senior Economist, Markets +61 3 9273 1381 Katie.Dean@anz.com			

ANZ Markets

Warren Hogan Head of Markets Research +61 2 9227 1562 Warren.Hogan@anz.com	**Sally Auld** Senior Interest Rate Strategist +61 2 9227 1809 Sally.Auld@anz.com	**Tony Morriss** Senior Currency Strategist +61 2 9226 6757 Anthony.Morriss@anz.com	**Mark Pervan** Senior Commodity Strategist +61 3 9273 3716 Mark.Pervan@anz.com	**Katie Dean** Senior Economist, Markets +61 3 9273 1381 Katie.Dean@anz.com
David Croy Strategist +44 20 7378 2070 croyd@anz.com	**Patricia Gacis** Market Strategist +61 2 9227 1272 Patricia.Gacis@anz.com			

Research & Information Services

Mary Yaxley Head of Research & Information Services +61 3 9273 6265 Mary.Yaxley@anz.com	**Marilla Rough** Senior Information Officer +61 3 9273 6263 Marilla.Rough@anz.com	**Manesha Jayasuriya** Information Officer +61 3 9273 4121 Manesha.Jayasuriya@anz.com

ANZ New Zealand

Cameron Bagrie Chief Economist +64 4 802 2212 bagriec@anz.com	**Khoon Goh** Senior Economist +64 4 802 2357 gohk@anz.com	**Philip Borkin** Economist +64 4 802 2199 borkinp@anz.com
Sean Comber Economist +64 4 802 2286 combers@anz.com	**Steve Edwards** Economist +64 4 802 2217 edwards1@anz.com	**Kevin Wilson** Rural Economist +64 4 802 2361 Kevin.Wilson@nbnz.co.nz

Important Notice

Australia and New Zealand Banking Group Limited is represented in:

AUSTRALIA by:

Australia and New Zealand Banking Group Limited ABN 11 005 357 522

10th Floor 100 Queen Street, Melbourne 3000, Australia

Telephone +61 3 9273 6224 Fax +61 3 9273 5711

UNITED KINGDOM by:

Australia and New Zealand Banking Group Limited

ABN 11 005 357 522

40 Bank Street, Canary Wharf, London, E14 5EJ, United Kingdom

Telephone +44 20 3229 2121 Fax +44 20 7378 2378

UNITED STATES OF AMERICA by:

ANZ Securities, Inc. (Member of NASD and SIPC)

6th Floor 1177 Avenue of the Americas

New York, NY 10036, United States of America

Tel: +1 212 801 9160 Fax: +1 212 801 9163

NEW ZEALAND by:

ANZ National Bank Limited

Level 7, 1-9 Victoria Street, Wellington, New Zealand

Telephone +64 4 802 2000

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