Domestic Financing vs. Euro bond issuance- the case of Vietnam

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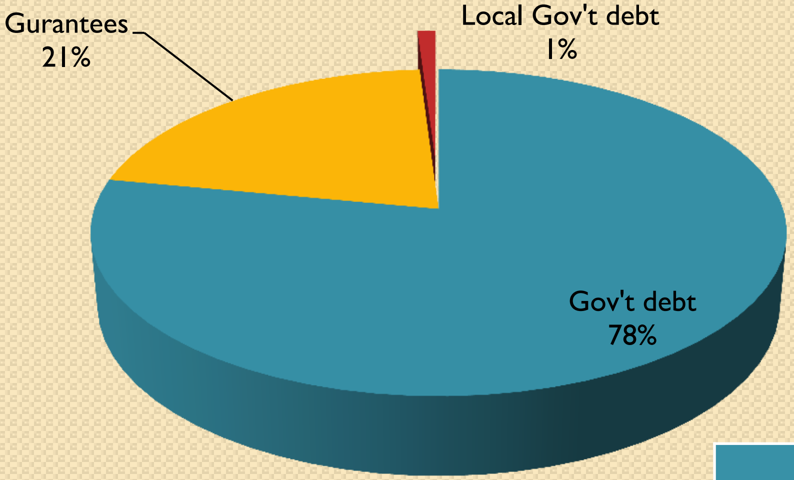
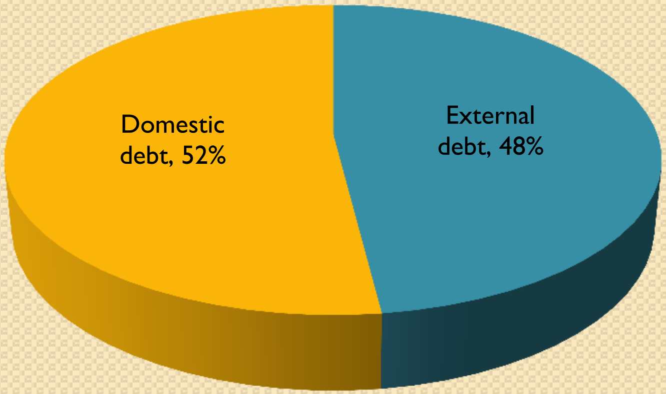
Overview

1. Land area: 331.000 km2
2. Capital: Hanoi
3. Population: 90.4 million
4. GDP per capita: $1,895
5. 2013 macroeconomic indicators:
   - GDP growth: 5.4%
   - Budget deficit/GDP: 5.3%
   - Inflation: 7%
   - Public Debt/GDP: 56.2%
     - O.w: Government Debt: 42.6%

Current public debt portfolio

(as of 31/12/2013, est.)





	USD (Billion)	%GDP	Threshold %GDP
Public debt	95	56.2%	<=65%
- Gov’t debt	72	42.6%	<50%
- Guarantees	21.6	12.8%	
- Local Gov’t debt	1.4	0.8%	

Vietnam sovereign bonds

- The first international bond of Vietnam was the Brady Bond, which was issued in 1998 for restructuring its arrears through Paris Club (amortization repayment schedules).
- The fist time Vietnam came in to international capital market was in 2005. The latest and second time that it came to the capital market was in 2010. Since Vietnam has become middle-income country, Vietnam may need to tap into the international capital market more often.

Issue date	Bond	Amount (USD million)	Tenor (years)	Coupon
Mar 1998	Brady bonds	563	18; 30	3% - 5.5%, floating rate
Oct 2005	VN2016	750	10	6.875%
Jan 2010	VN2020	1,000	10	6.75%

The use of proceeds

By Law, all of the proceeds mobilized from sovereign bond issuance shall be for on-lending

Bond	Amount (USD million)	Beneficiary
VN2016	750	Vinashin
VN2020	300	Vinashin
VN2020	700	Dung Quat oil refinery company

- *Vinashin is a state-owned ship building company.*
- *Dung Quat oil refinery project is was invested by Petro of Vietnam which is also a SOE*

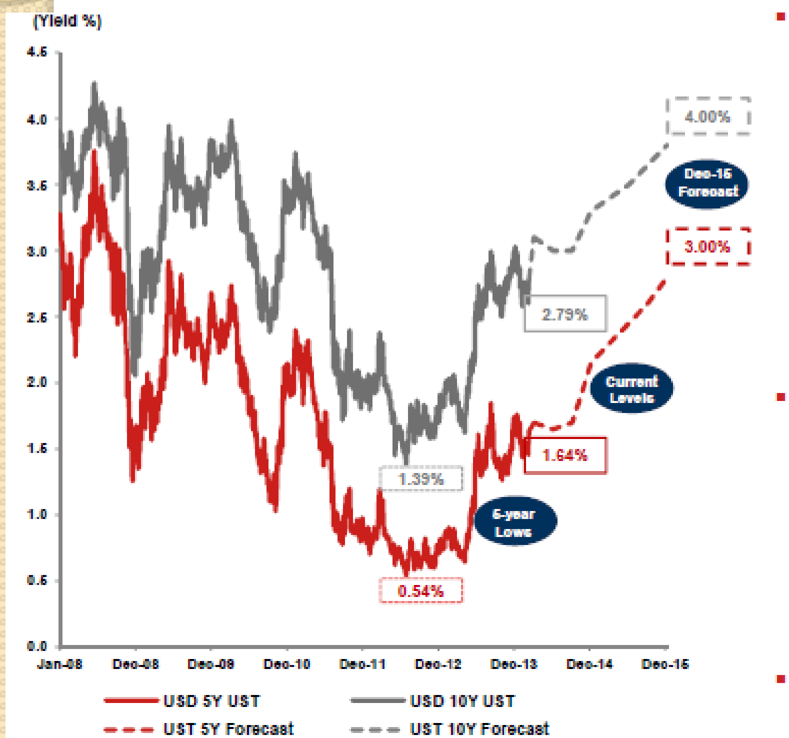
While the refinery project was the story of success, Vinashin was not the case. Vinashin deferred its first interest repayment on 2011 and is deemed of not being able to fulfill its payment obligation when the bond due in 2016.

→ ***The Government will have to use its own resource for bond repayment.***

Refinancing sovereign bonds

LM exercise with a new Euro bond

UST yields have stayed at low levels but all forecast is on the rise.



Source: Bloomberg as of Mar 21,,2014 and Nomura's forecast rates

Investors' appetite for emerging market bonds remains high

Issuers	Issue date	Tenor	Amount (in millions of US$)	Over-subscription	Coupon
Philippines (Baa3/BBB-)	Jan 2012	25	1,500	5.7x	5%
Zambia (B+)	Mar 2012	10	750	15.8x	5.625%
Mongolia (BB-/B+)	May 2012	5, 10	1,500	10x	5.125%
Sri Lanka (B1/B+)	Jul 2012	10	1,000	10x	5.875%
Indonesia (Baa3/BB+)	Apr 2013	30	1,500	4.2x	4.625%
Rwanda (B/B)	Apr 2013	10	400	8.25x	6.875%
Gabonese (BB-/BB-)	Dec 2013	10	1,500	2x	6.375%
Indonesia (Baa3/BB+)	Jan 2014	30	2,000	NA	6.75%

Source: www.reuter.com

Refinancing sovereign bonds (Cont.)

The credit story of Vietnam has been improved with number of efforts in structural reforms

- Vietnam's economy has been stable after a long period of overheating with stable exchange rate and low inflation over the past 2 years;
- Banking sectors and SOE structural reforms remained the Government's top priorities.
- Vietnam remains one of the fastest growing, most attractive investment destinations in the world.

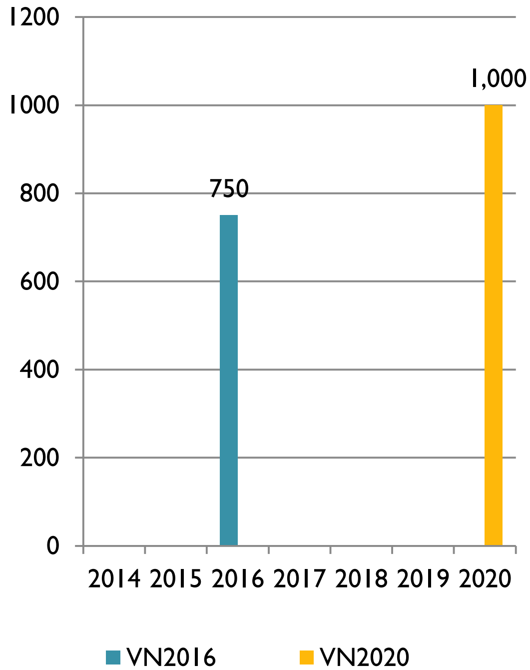
Challenges:

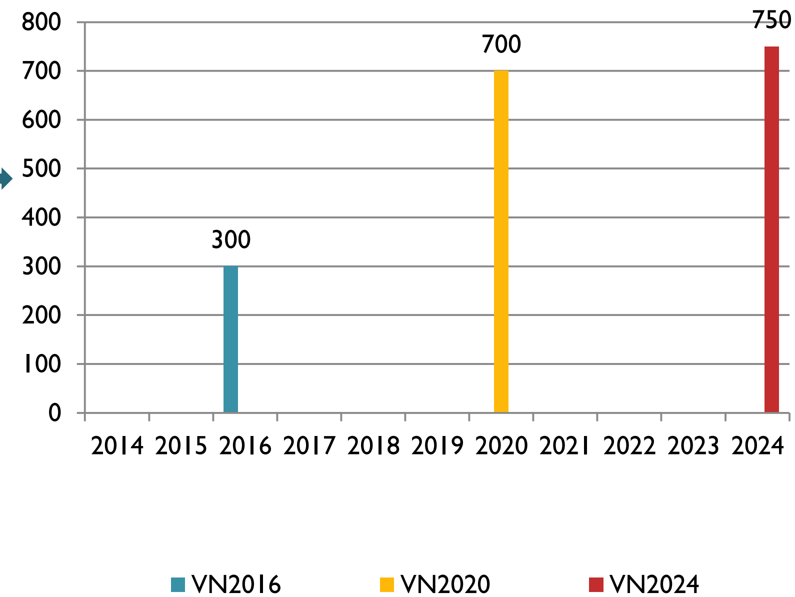
- Complicated documentations and too much internal procedures
- Negative perspective from public at the 2 previous issuances due to its tie with Vinashin collapse.

Refinancing sovereign bonds (Cont.)

Alternative 1: LM exercise with a new Euro bond

- Issue a USD 750 million 10 year bond with a target of exchange USD450 million for VN2016 and exchange USD 300 million for VN2020. The Government will have a smoother debt repayment profile.





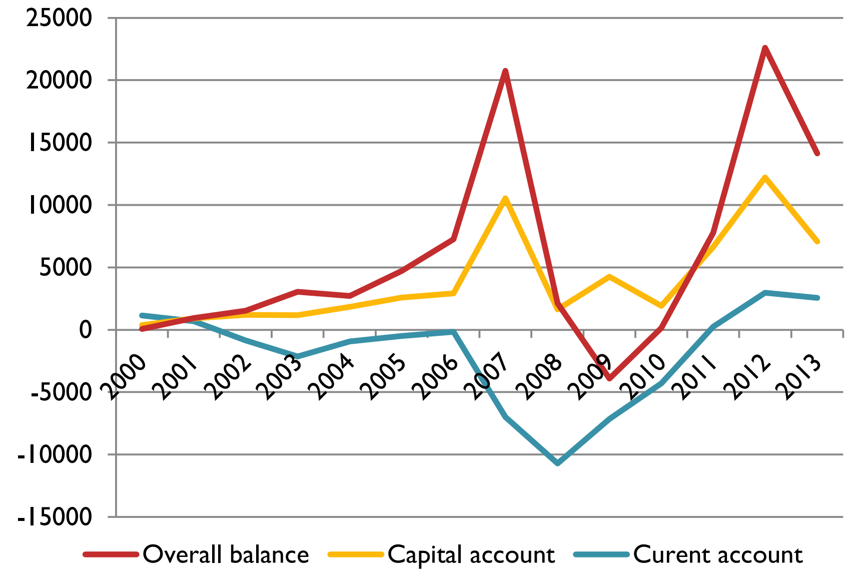
Refinancing sovereign bonds (cont.)

- **Alternative 2: Issue USD denominated bond domestically**

- With the return of economic stability, Vietnam's BoP has been improved.

- Economic slow down made credit going down significantly (6.8% in 2013 vs. more than 30% before 2011)

- Commercial banks may find investment in $ denominated government bond as a safe channel.



Difficulties:

- Against anti-dollarization policy pursuing by SBV, who has been maintained low USD deposit rate for a long time;

- Commercial Banks and other financial institutions do not have long term resource to invest into long term bonds;

- The last mobilization of USD denominated bond in 2009 was not success, with low participation and low maturity (mostly 3 years and 24% plan achievable)

Cross countries experiences

- **Set up Sinking Fund:** UK, the Philippines and India have good experiences of accumulating a fund to have resource available to repay their debts. However, it may be costly due to carrying cost.

- **Issue foreign currency denominated bond domestically:** Some countries have successfully issued foreign currency denominated bonds domestically such as Peru, Columbia, Paraguay and the Philippines. However, it has not been very common recently, and not success with Vietnam.

- **Engage in liability management operations:** includes exchanging or buying back the existing bonds. Indonesia, Philippines, Turkey, Brazil and Gabon have actively engaged in these operations and achieved targets of extending the average debt maturity profile, reduce ongoing debt services by taking advantage of low yields.

Debt manager considerations

Both options have pros and cons . After careful consideration, DMO of Vietnam decided to conduct its LM exercise with sovereign bond issuance, based on the following merits:

-Pro-long current sovereign bonds given difficulties in state budget allocation for principal repayment in 2016; while current public debt ration wont be affect.

- Create new low benchmark for Government yield curve, given QE of US on the way of ending.

- The new yield is expected lower than lending rate of external guaranteed projects (8%/year)

- Improve chance of rating upgrade by proactive debt management

- Paving way for Vietnam corporation accessing capital market with lower costs (in 2012, Vietinbank issued with coupon of 11.625%, in 2013, Vin Group issued with coupon of 8.25%, both for 5 year bond).

Policy considerations

- There should be a careful consideration associated risks with another Euro bond issue including exchange rate and rollover risks as well as its affects to the public debt burden.
- It is necessary to design an appropriate medium term debt management strategy including comprehensive analysis of market and refinancing risks.
- Debt managers should be authorized to carry on proactive debt management such as liability management, hedging… operations within an approved scheme instead of waiting for approvals for each of individual transactions.
- Other economic shall be entitled to issue bonds by themselves on their own credit standing to avoid credit risk impacting the Government's budget.

Thank you!