SECTOR COMMENT

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Corporate Bond Market Perspective

New regulations will guide stable growth of corporate bonds, but keep new issuances subdued until 2H 2023

The Ministry of Finance of Vietnam implemented new regulations ('Decree No. 65') on private placement corporate bonds on 16 September 2022, after months of consultation with market participants that led to much anticipation of the additional requirements for issuing new private placement bonds.

Decree No. 65 is a big and critical stride to instill greater market discipline, improve the quality of bond issuances and restore investor confidence in the fast-growing private placement market. The new regulation enforces issuers and their intermediary service firms to make more comprehensive and timely disclosures on private placement bond offerings and it defines the legal responsibilities and obligations of issuers and intermediaries.

In addition to more information disclosures, bondholders will benefit from greater clarity on their legal rights and deeper understanding of investment risks. Bondholders will have the right to enforce bond redemptions if bond issuers violate regulations, and more clarity on their legal rights over collateral assets. Professional individual investors will need to self-certify on their eligibility to invest and their understanding of issuers' information disclosures and investment risks. Raising risk awareness and understanding of issuer disclosures are important safeguards to protect investor interests.

Market adjustment to new regulation and tighter financing conditions will defer any meaningful recovery in new bond issuances to 2H 2023. Public bond markets remain intact and can serve to connect corporate bond issuers to a wider pool of investors. The new regulation more clearly restricts retail individual investors to the public bond market which has a more developed regulatory framework and greater information transparency to safeguard investor interests.

VND 62 trillion worth of corporate bonds will mature over the last two months of 2022 and mostly in December. Compared with financial institutions, non-financial corporates with high leverage will face greater need to refinance maturing debt. Barring issuers that may receive bondholders' consent to restructure bond repayment, highly leveraged issuers will likely require support from related companies or other lenders to meet bond repayments.

Decree No. 65 is a big and critical stride to instill greater market discipline, improve the quality of bond issuances and restore investor confidence in the fast-growing private placement market

The Ministry of Finance of Vietnam implemented new regulations ('Decree No. 65') on private placement corporate bonds on 16 September 2022, after months of consultation with market participants. Decree No. 65 serves to amend Decree No. 153 that came into effect in January 2021 to regulate the private placement bond market offerings. Exhibit 1 summarizes the key changes under Decree No. 65.

Exhibit 1
Key enhancements to the regulatory framework under Decree No. 65

	Transparency	Accountability
Issuers	» To specify purpose of bond, details of issuer's investment program/project/debt to be restructured » For secured bonds: To provide details of collateral assets (asset type, valuation, legal status, registration of security interest, priority of claim of bondholders, etc.) » To disclose an expanded list of financial indicators on issuer's capital structure, outstanding debt and bonds, liquidity and profitability ratios » To disclose any regulatory violation prior to bond issuance; administrative penalties for violating relevant laws » To disclose changes to bond terms, bondholder representative; compulsory redemption of bonds » To provide plan and schedule for use of idle bond proceeds » To disclose offering results to bondholders and Stock Exchange within 5 days (from 10days); updates on issuer's financial status between offering waves	» Documentary evidence of no prior default of bond repayment » Provide an assessment of own financial status and solvency to repay debts » Half-year and annual audited reports on use of proceeds from outstanding bonds » Report on fulfillment of commitments to bondholders » Obtain bank confirmation of account opening and receipt of adequate funds from bond issue; underwriting and brokerage firms' written confirmation of transfer of bond proceeds to issuer account » Obtain credit rating and disclose credit rating results (if applicable); requirements are same as public bond issuance
Service Providers	» Bondholders' representative to report to State Securities Commission (SSC) and Stock Exchange on a quarterly and annual basis, and whenever the issuer is found to have committed violations » Banks licensed to provide brokerage services to report to State Bank of Vietnam » Vietnam Securities Depository Corporation (VSDC) to report to SSC on registration, depositing, ownership transfer, and structure of bondholders	» Must not be related persons of the issuer » Must assume legal responsibility for services provided; in case of violations, liable to administrative penalties or criminal prosecution » Bondholder representatives must have service contracts with issuers for bonds sold to individual investors » Counseling on bond offering dossiers: certify that bond offering and offering dossier fulfill all relevant legal requirements prior to bond offering; do not include false or misleading information » Bidding, underwriting, brokerage service providers: only distribute bonds to eligible professional investors that are certified; do not confuse and mislead investors; to confirm transfer of bond proceeds to issuer's account
State and Regulatory agencies	Stock Exchange » Ensure adequate and timely disclosure of information and reporting by issuers, bidding, underwriting and brokerage service providers » Publish more information on corporate bonds issuance, including financial indicators of bond issuers, ad hoc information updates, credit ratings of issuers, issuers that fail to fulfill bond repayment obligations or other commitments to bond holders such as use of bond proceeds for prescribed purposes, compulsory bond redemptions	State Securities Commission » Regulate receipt, reporting and disclosure of information on Stock Exchange, trading of corporate bonds » Supervise VSDC's registration, depositing, payment and transfer of ownership » Supervise services provided by securities companies » Conduct inspection of the Stock Exchange, VSDC, service providers and issuers in case of violations to the relevant laws State Bank of Vietnam » Supervise banks licensed to provide brokerage service Ministry of Finance » Supervise audit and valuation service providers involved in privately placed corporate bond issuances Relevant Ministries and Regulatory Authorities » To inspect and supervise offering, trading and provision of related services on corporate bonds

Source: Ministry of Finance, Vietnam Investors Service

Under Decree No. 65, issuers need to disclose an expanded set of standard, pertinent information for private placement bond issuances to bond investors on a timely basis throughout the duration of the bond. This requirement will address the opacity of the private placement market. Importantly, it enforces issuers to assess the feasibility of bond financing plans, to be accountable for the legitimacy and accuracy of their assertions to investors, the usage of bond proceeds and the repayment of borrowed monies.

The decree also reinforces the roles and responsibilities of intermediary service firms involved in bond issuances, their legal obligations, and the regulatory stance to deal with violations. In addition, it strengthens the supervisory framework for various state agencies and authorities to manage institutions and service providers under their charge.

Decree No. 65 is a big and critical stride to instill greater accountability among key stakeholders for their role in the bond issuance process, enhance information transparency and quality of issued bonds, and restore market confidence in the fast-growing private placement bond market and its role as a reliable financing channel for businesses.

The recent alleged misconduct and misappropriation of bond proceeds by entities linked to Tan Hoang Minh Group and Van Thinh Phat Holdings Group revealed the lack of due care exercised by parties involved in bond issuances and the lack of ready information to assess issuer and investment risks. Multiple securities brokerage firms were sanctioned by the State Securities Commission in September 2022 for failing to disclose required and accurate information in bond offering documents.

These developments surfaced after a period of very strong growth in private placement bonds beginning in 2020 and increasing concern by regulatory authorities that corporate bonds were mis-sold to individual investors who do not adequately understand the risks of bond investments.

In addition to more information disclosures, bondholders will benefit from greater clarity on their legal rights and deeper understanding of investment risks

The decree strengthens the legal safeguards for bondholders and enhances the market infrastructure for bondholders and prospective bond investors to make better investment decisions.

Exhibit 2
Decree 65 strengthens bondholder rights and safeguards

Category	Details
Legal Rights	» Bond buyers have legal right to obtain adequate information from issuers and bond sellers prior to investment » Bondholder resolutions to be approved by at least 65% of votes, including for changes to bond terms » Bondholders' representative must be appointed to represent rights and interests of bondholders; may be replaced if approved by ≥ 65% of bondholders » Compulsory redemption by bondholders if issuer commits violation or fails to commit to issuance plan, and violations cannot be remedied; or ≥ 65% of bondholders do not approve of remedial measures
Bond Settlement	» Bond issued to be distributed to investors within 30 days (from 90 days) from date of information disclosure » Total duration for bonds issued in multiple waves to not exceed 6 months (from 12 months) » Bonds must be registered and deposited at Vietnam Securities Depository Corporation before being traded or transferring ownership
Risk Awareness	» Higher qualification criteria for professional individual investors: Investment holding ≥VND2 billion over 6-month period Investor to sign self-certification of compliance with Decree requirements, assume responsibility of own investment » Par value of bond increased to VND100 million, from VND100,000 » Bond buyers not allowed to sell bonds or make joint investment in bonds with investors that are not professional investors

Source: Ministry of Finance, Vietnam Investors Service

Under Decree No. 65, bondholders have the legal right to enforce bond redemptions if bond issuers violate regulations or fail to commit to their issuance plans. Bondholders will have access to more information disclosures to assess and monitor the risks of their investments, including their legal rights over collateral assets.

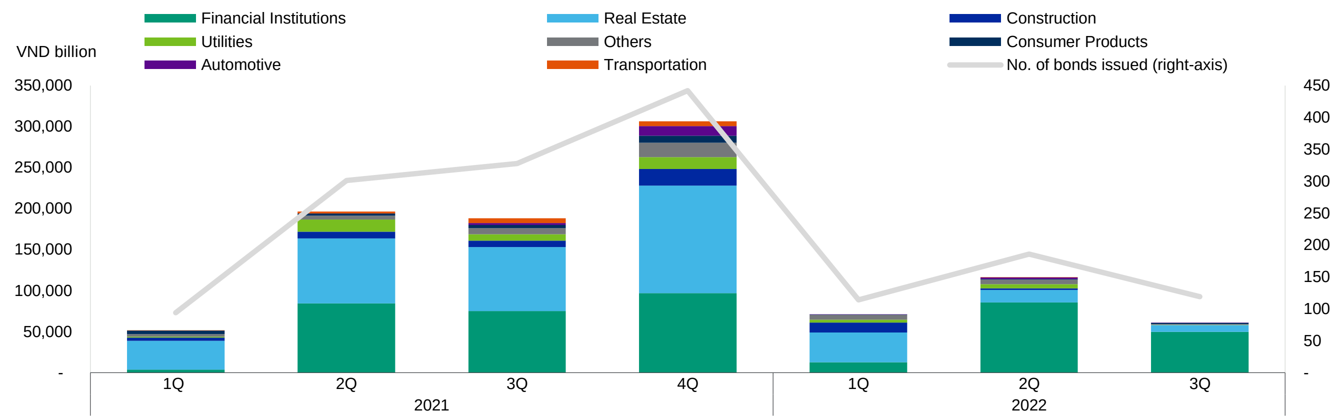
Bondholders can also refer to certifications by service firms – including representative of bondholders, counseling service providers, bidding, underwriting and brokerage service providers – to get assurance on bond issuer's compliance with requirements under relevant laws.

Professional individual bond investors need to self-certify their eligibility to invest and their understanding of bond issuers' information disclosures and the associated investment risks. This is an important safeguard to increase investors' awareness and motivation to use all available information for their investment decisions. For bonds requiring credit ratings, bondholders can utilize ratings to assess relative risks, the suitability of the bonds for their risk tolerance, and the adequacy of the risk premiums.

Market adjustment to new requirements and tighter financing conditions will defer any meaningful recovery in bond issuances to 2H 2023. Public bond markets remain intact and can serve to connect corporate bond issuers to a wider pool of investors

New bond issuances declined substantially over the first nine months in 2022, driven in part by market uncertainty prior to the release of Decree 65 and risk aversion sparked by the recent criminal and regulatory actions taken against bond issuers and their service providers. Accessing liquidity in the primary bond market is a key concern for companies seeking new funding or refinancing of maturing debt obligations.

Exhibit 3
Substantial year-on-year decline in total bond issuances in 2022



Source: Hanoi Stock Exchange, Vietnam Investors Service

Amid higher interest rates and financing costs that will likely dampen bond issuance plans, bond issuers and service providers will need to adjust to additional administrative and compliance costs and a longer roadmap to launch new private placement bonds. Any meaningful pick-up in bond issuances will likely occur in 2H 2023 at the earliest.

Decree 65 closes the significant gap in the documentary requirements for bond offerings between the public and the private placement markets. It also more clearly guides retail individual investors to the public bond market, which has a more-developed issuance and supervision framework that provides stronger safeguards for bondholders.

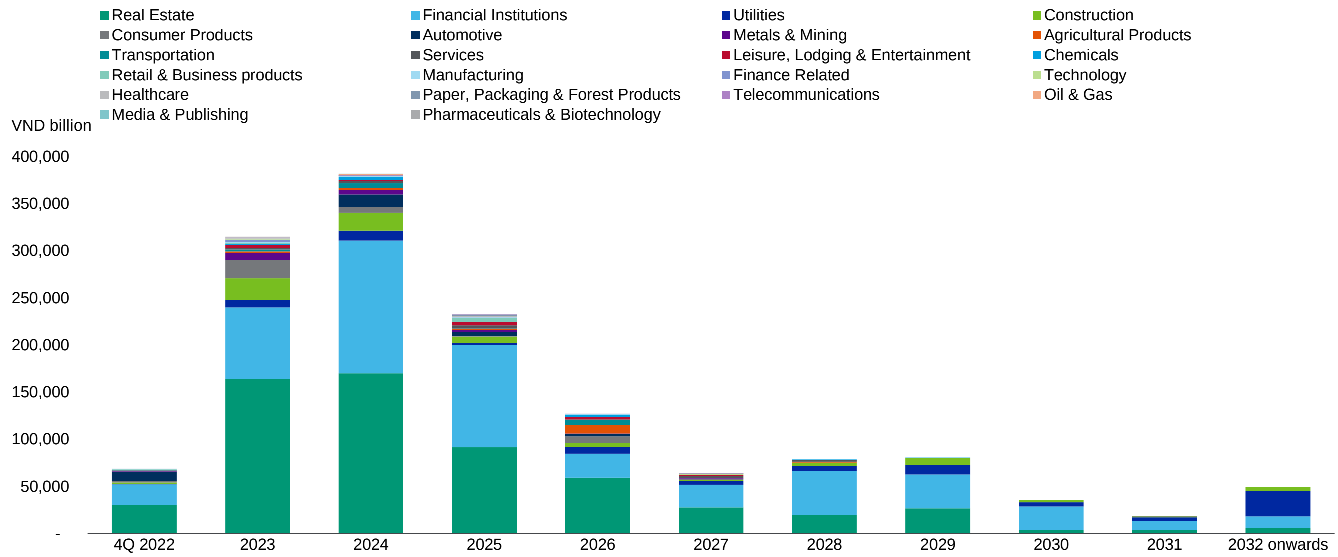
We expect more corporate bond issuers to seek financing in the public bond market to access the strong demand by retail individuals for high-yielding investments.

According to data released by Hanoi Stock Exchange, individual investors were among the largest investor group for bonds and held 31% of total outstanding corporate bonds in the first nine months of 2022, second only to credit institutions (44%). As individual wealth creation increases with income levels, the demand for bonds offered in the public bond market among retail investors will increase over time.

VND 62 trillion worth of corporate bonds will mature over the last two months of 2022 and mostly in December. Compared with financial institutions, non-financial corporates with high leverage will face greater need to refinance maturing debt

A total of VND62 trillion worth of corporate bonds issued by over 70 companies will mature in November and December 2022. The maturity wall will increase over the next two years (Exhibit 4), and this points to an increasing number of bond issuers needing to either manage cash flows to make bond repayments or plan to refinance bond funding ahead of maturity. Around 80% of total bonds maturing in 2023-2024 are attributable to bonds issued by financial institutions and real estate companies in the private placement market over the past three years with tenors of mostly between one to three years.

Exhibit 4
Outstanding corporate bonds maturing will increase and peak in 2024



Source: Hanoi Stock Exchange, Vietnam Investors Service

We expect refinancing risks will remain elevated at least until the end of 2022. Tighter financing conditions and heightened market risk aversion will create challenges for corporations to access liquidity in the primary bond market.

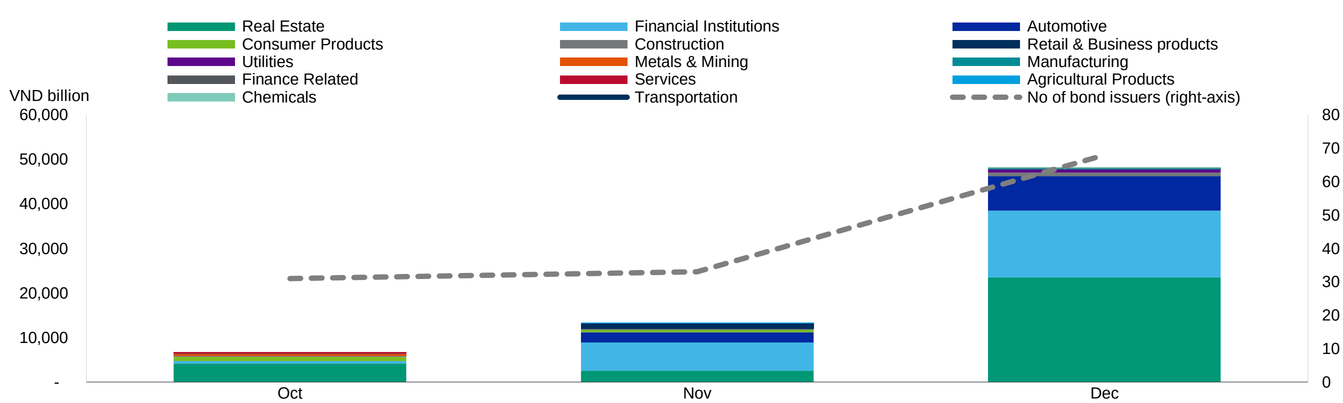
Recently, several bond issuers had notified bondholders of their intention to defer the repayment of upcoming interest or principal amount for their maturing bonds. We view this development to be a recurring theme to watch for as more bonds become due for principal repayment over the next few quarters.

For the companies with bonds maturing in November – December 2022, around a quarter of them are financial institutions including commercial banks, finance companies and securities firms; remaining companies are non-financial companies, mostly in the real estate sector.

Non-financial Corporates

We expect issuers to have increasing difficulty rolling over their existing bonds given the tight market liquidity and such companies will need to repay their bond obligations with maturities concentrated in December 2022.

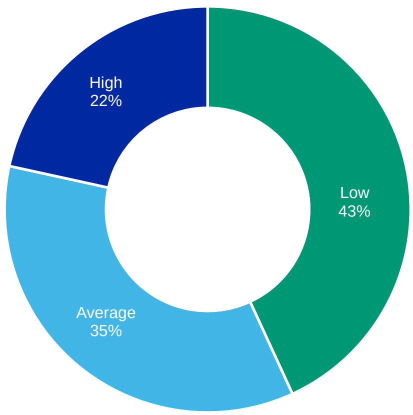
Exhibit 5
Bond maturities concentrated in December 2022



Source: Hanoi Stock Exchange, Vietnam Investors Service

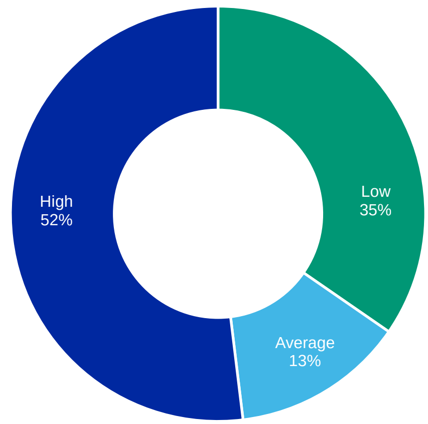
For the non-financial corporates with bond maturing in November – December 2022, we assess that a substantial portion of companies have high leverage profiles as shown in Exhibits 6 and 7. In this assessment, high leverage is characterized by Debt/Equity of 4x or higher and/or Debt/EBITDA of 7x or higher. Much of the high leverage resulted from bond issuances over the past three years. For several companies, issuance sizes were way in excess of their capital levels.

Exhibit 6
Debt/Equity profile
By proportion of companies



Source: Vietnam Investors Service

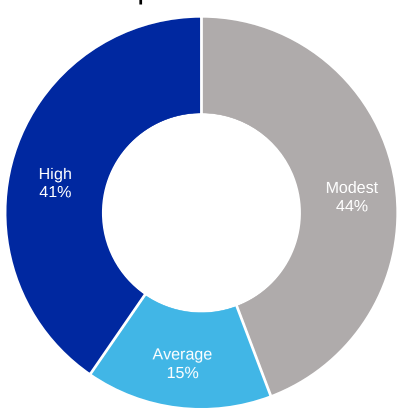
Exhibit 7
Debt/EBITDA profile
By proportion of companies



Source: Vietnam Investors Service

We expect debt restructuring for these companies to refinance maturing bonds under Decree No. 65 to be challenging, and these companies will need to rely on existing cash flow and resources (Exhibit 8) or financial support from other lenders or related companies to repay debt.

Exhibit 8
Sufficiency of cash resources to cover repayment of bonds maturing in November – December 2022
By proportion of companies

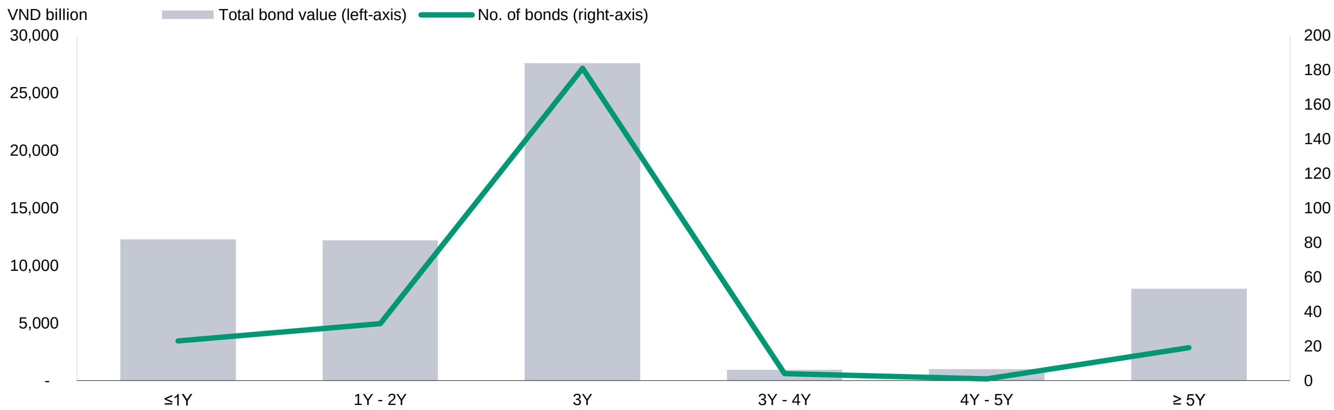


Source: Vietnam Investors Service
Note: Cash resources refer to estimated cash balance and cash flow from operations.

Many of the real estate-related issuers are unlisted subsidiaries of the large real estate developer groups in Vietnam established to primarily undertake investment and development in new real estate projects. Cash flow management is crucial for these companies over the course of the project development, which typically takes five years or more to complete.

A significant portion of the bonds issued by these companies were issued in 2020-2021 with maturities of three years or less (Exhibit 9), which they will need to roll over or refinance with alternative sources to fund their long-term projects.

Exhibit 9
Majority of bonds issued by financial institutions and corporates maturing in 4Q 2022 have original issuing tenors of 3 years or less



Source: Hanoi Stock Exchange, Vietnam Investors Service

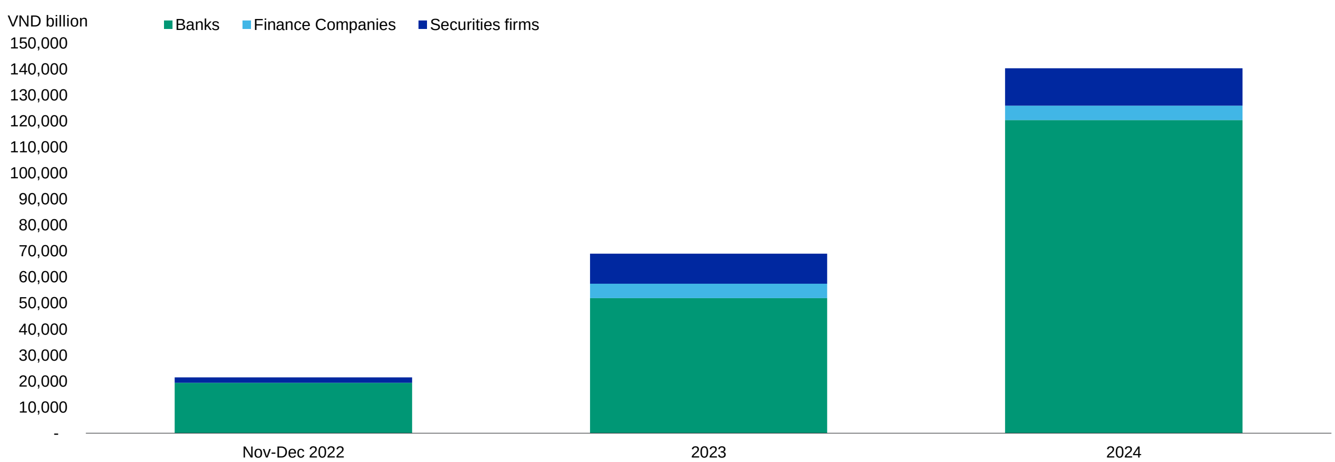
High reliance on short-term financing with little or low predictability of incoming cash flows reflects weak financial policy and exposes companies to refinancing risks and potential liquidity challenges.

Majority of the maturing bonds were issued on an unsecured basis. Despite the high-risk profile of the bond issuers, we note that a significant portion of the real estate-related bonds were distributed to retail individual investors that may not fully understand the financing standing of these issuers or unable to adequately assess the issuers' ability to repay.

Financial Institutions

For the financial institutions, total value of bonds maturing will increase over the next three years, mostly attributable to commercial banks (Exhibit 10).

Exhibit 10
Total outstanding bonds maturing for financial institutions will increase



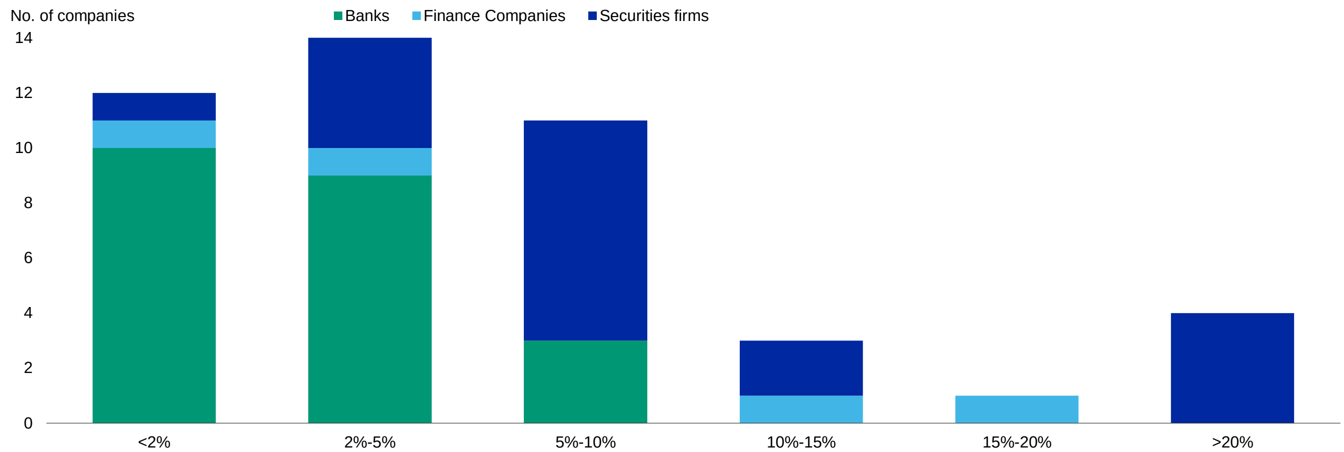
Source: Hanoi Stock Exchange, Vietnam Investors Service

Compared with non-financial corporates, we view liquidity and refinancing risks for the financial institutions to be manageable, underpinned by the regulated nature of their businesses. As shown in Exhibit 11, maturing bonds over the next three years amount to no more than 10% of total assets for majority of the financial institutions.

Commercial banks in Vietnam are primarily funded by customer deposits, and bond funding is typically used to match-fund longer-dated credit exposures and supplement capital needs. According to the State Bank of Vietnam, the average loan-to-deposit ratio for banking system is 82% (for state-owned banks) and 72% (for joint stock commercial banks) as at the end of June 2022, and banks maintain adequate stock of liquid assets in the form of cash and government securities.

The use of short-term funding for medium- and long-term loans is constrained by regulation. At end-June 2022, the average ratio for short term funding is 29% (for state-owned banks) and 27% (for joint stock commercial banks), below the regulatory limit of 34%.

Exhibit 11
Majority of financial institutions have maturing bonds (up to 2024) not exceeding 10% of total assets



Source: Company data, Vietnam Investors Service

For securities firms, bonds issued in recent years have supported their balance sheet-intensive business growth such as proprietary trading and investments and margin lending. Apart from several small firms, majority have maturing bonds totaling no more than 10% of total assets and sufficient liquid assets to tackle potential refinancing issues.

Firms with substantial amount of bonds maturing may need to scale back new business and balance sheet growth if they are unable to replace maturing bonds with new funding. Such business adjustment will add pressure to the firms' weakening profitability amid the roil in domestic equity and bond markets. For 9M 2022, majority of the securities firms reported year-on-year declines in revenue and net income.

On the asset-side, commercial banks and securities firms have sizable investments in corporate bonds that pose potential asset risks. According to the State Bank of Vietnam, the total value of corporate bonds held by credit institutions was VND274 trillion at the end of 2021, with majority held by Vietnam's largest commercial banks.

Circular 16 was implemented in November 2021 to limit credit institutions' investment in corporate bonds. Among the 15 largest commercial banks by assets, only a handful have corporate bonds making up over 5% of total credit exposures.

Majority of securities firms have corporate bond investments not exceeding 10% of total assets.

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