The State Bank of Vietnam doubled its FX trading band to 2% on August 12th, 2015 in response to the CNY devaluation

The State Bank of Vietnam (SBV) has adjusted its FX trading band from 1% to 2% effective from 12th August 2015 in response to the PBOC's record devaluation of CNY earlier this week. This de facto devaluation of a further 1% means VND devaluation can be in reality up to 4% YTD.

On the interbank and free markets, FX rates started to increase sharply after the first CNY devaluation on Tuesday and are trading toward the ceiling of the adjusted band which is set at VND22,106. The SBV's prompt move aims to (i) support Vietnam exports which will face fiercer competition with Chinese goods now being about 5% cheaper, and (ii) help stabilize the FX market which has seen increasing pressure on VND, even before the CNY devaluation.

The Vietnam stock market like elsewhere inevitably got affected; however, at a less-severe-than-expected level so far with the VN-Index retreating 0.24%, 1.44%, 1.65% and 0.88% respectively on the 11th, 12th, 13th and 14th August. Investor's sentiment has been significantly dampened despite on-going progress in FOL theme and improving key macro indicators for the first 7 months. Possible stronger market correction in the coming days or weeks cannot be ruled out when a comprehensive assessment on full impact of the CNY devaluation on Vietnam's economy is made known to the public, coupled with likely sharper correction in global markets. China is currently the biggest trade partner of Vietnam and Vietnam's trade deficit to China was recorded at USD29B last year and USD16.5B in 1H2015.

In addition, high risk on the currency is another big concern to investors. We think with current foreign reserves of USD37B plus 10 tons of gold, the SBV will strive in any way they can to keep any further devaluation, de facto or official, in the remaining months of this year at a minimal level given the ruling Party's Summit will be held early next year. Having said that, if CNY is devalued significantly further in the short term, followed by other currencies (esp. those of Vietnam's export competitors), the SBV's task would be much more difficult.