VIETNAM INVESTORS SERVICE

Banking Sector Outlook

Slower operating conditions to weaken profitability, liquidity to stabilize with mid-sized and small banks most at risk

Updated with 2022 full year financials

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28 FEBRUARY 2023

Key Takeaways

Asset risks and credit costs will rise from deteriorating operating conditions
Problem loan formation will increase from weaker business cash flows, higher interest rates and operating costs, and refinancing difficulties in the corporate bond market. Credit exposures to export-oriented and manufacturing, real estate and construction are vulnerable to higher credit costs.

Net interest margins will contract following recent policy rate hikes
Mix of competitive and regulatory pressures will drive up deposit rates more than lending rates. Coupled with weakening credit demand, net interest margins will contract and more significantly for small banks with weak funding and tight liquidity.

Non-lending income growth will decelerate from unfavorable market conditions
Capital market-related and bancassurance fees will shrink from weak sentiment and lower cross-selling. Trading gains will diminish from higher interest rate and prolonged market volatility.

Capital levels will remain stable and weak by regional standards
Weaker profitability will hamper the ability to generate capital internally, while slower credit growth alleviate some pressure on capital. Tier 2 subordinated bonds will help to supplement bank capital needs.

Liquidity will remain tight, with mid-sized and small banks most at risk
Funding costs will remain elevated from sluggish deposit growth, keen competition among banks and risk aversion in the interbank market. Regulatory support will play an important role to stabilize banking system liquidity. Mid-sized and small banks with heavy reliance on short-term market fund are most at risk.

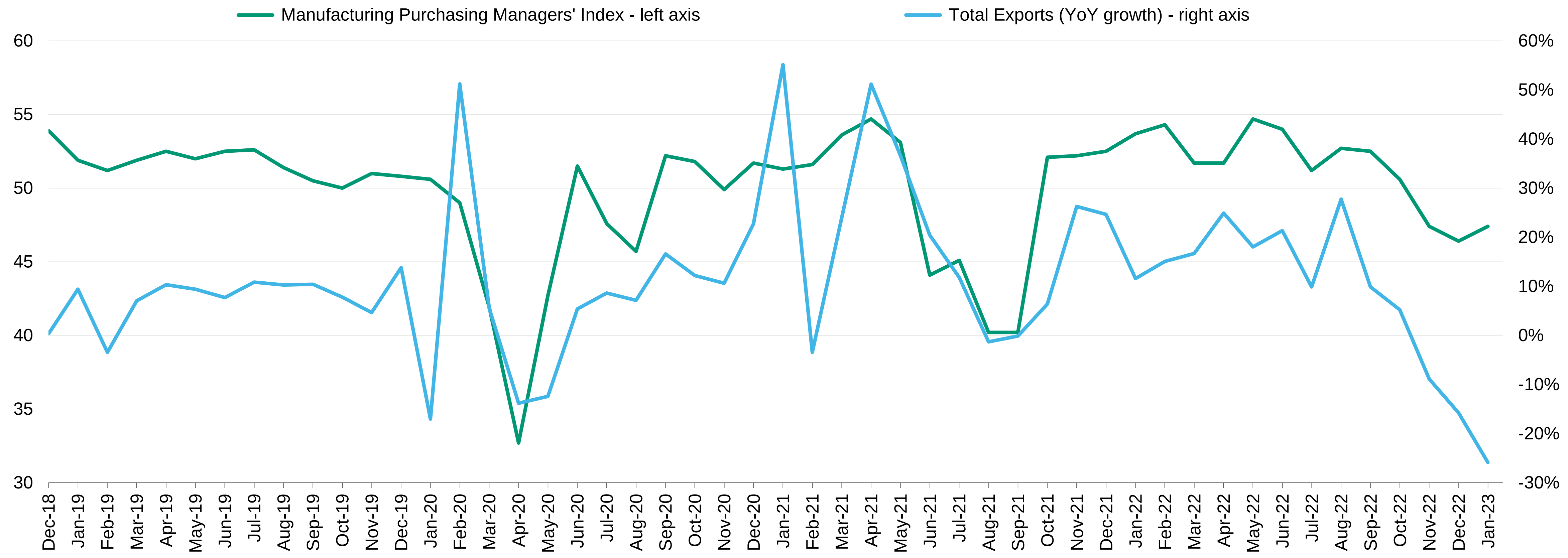
1

Bank operating conditions to deteriorate in 2023

Slowing manufacturing activity and exports

Economic growth is set to slow, and global trade to moderate from softer consumer demand

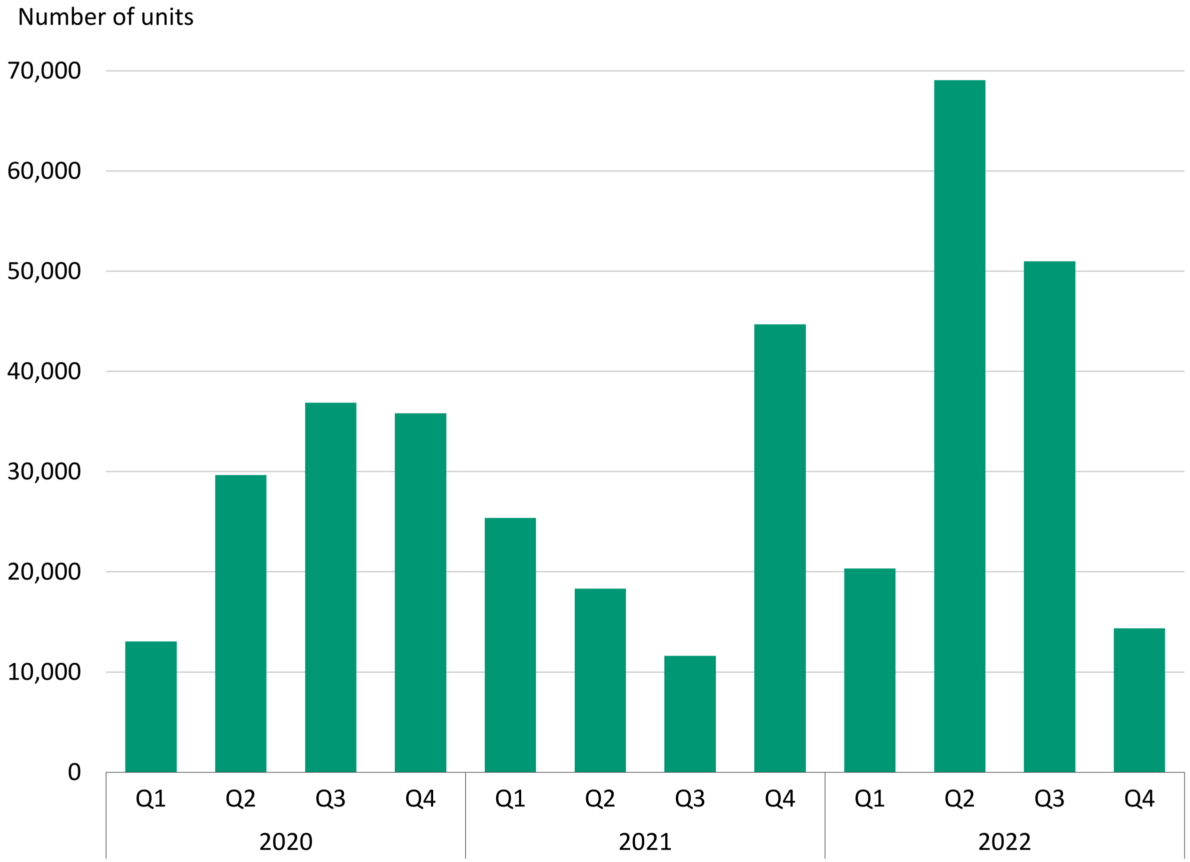
Purchasing Managers' Index vs Total Exports



Source: General Statistics Office of Vietnam (GSO), S&P Global

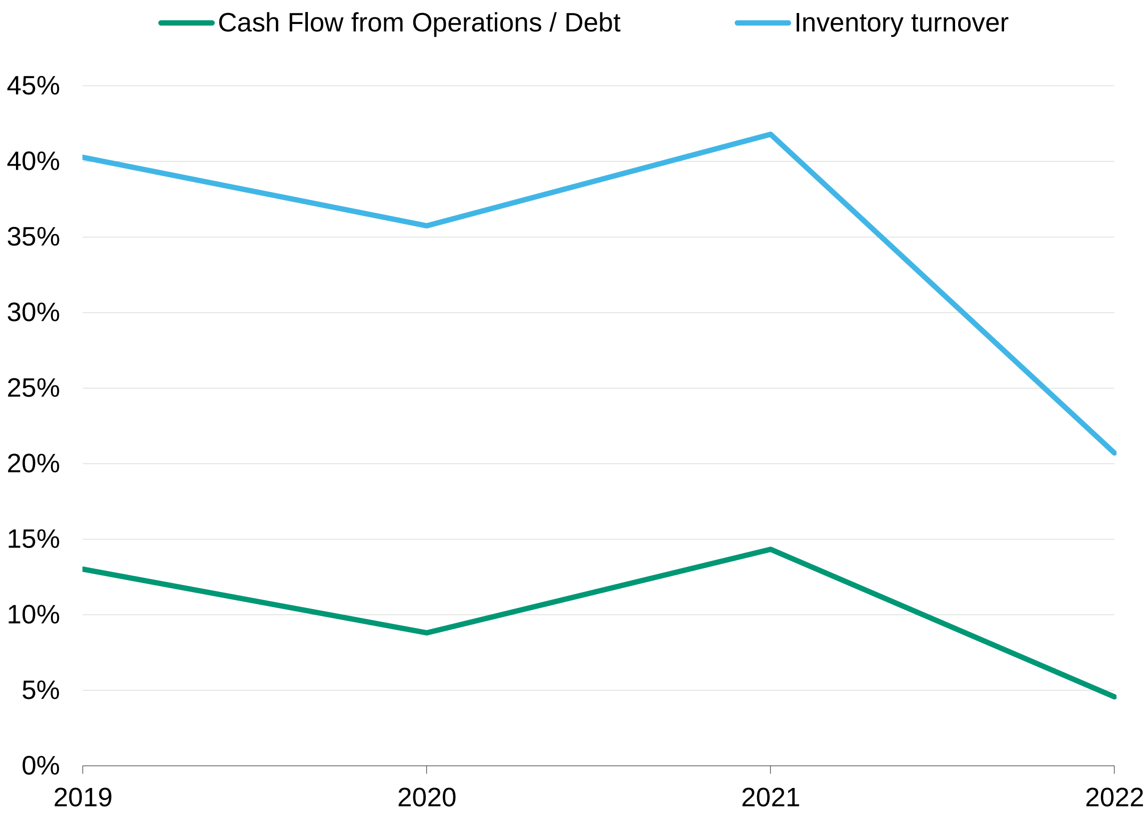
Weak buyer sentiment and liquidity stress weigh on real estate developers’ sales and cash flows

Real estate sale transaction volume



Source: Ministry of Construction, Vietnam Investors Service

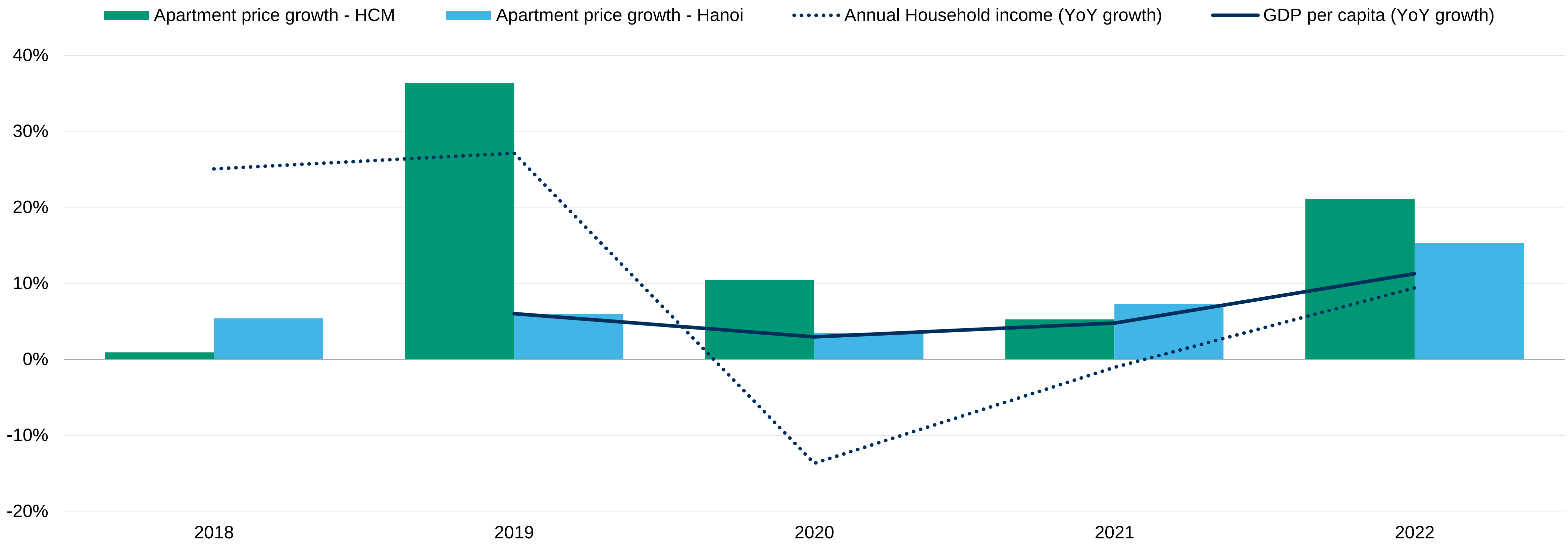
Inventory turnover and cash flows of top 20 real estate developers



Source: Vietnam Investors Service

Rising household borrower leverage as housing price growth far outpaced income growth

Apartment price growth vs household income growth



Source: GSO, Jones Lang LaSalle, Vietnam Investors Service

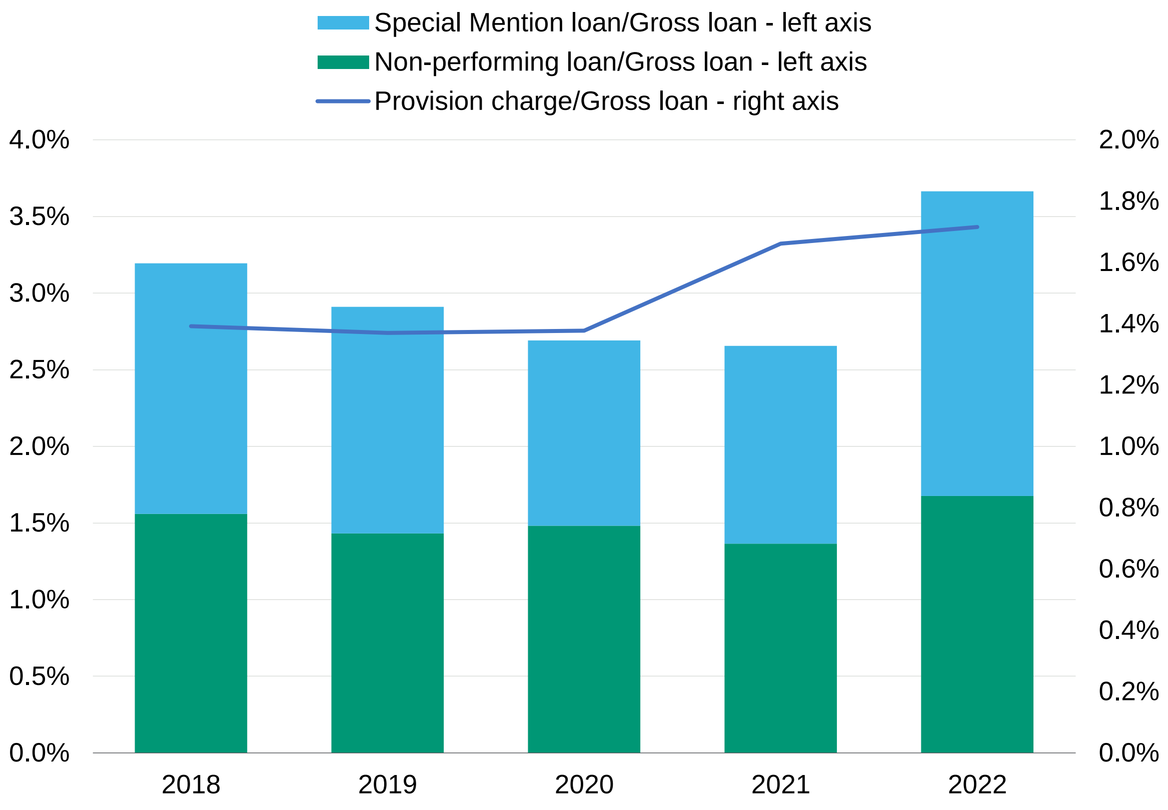
2

Asset risks and credit costs will rise

Problem loan formation will increase

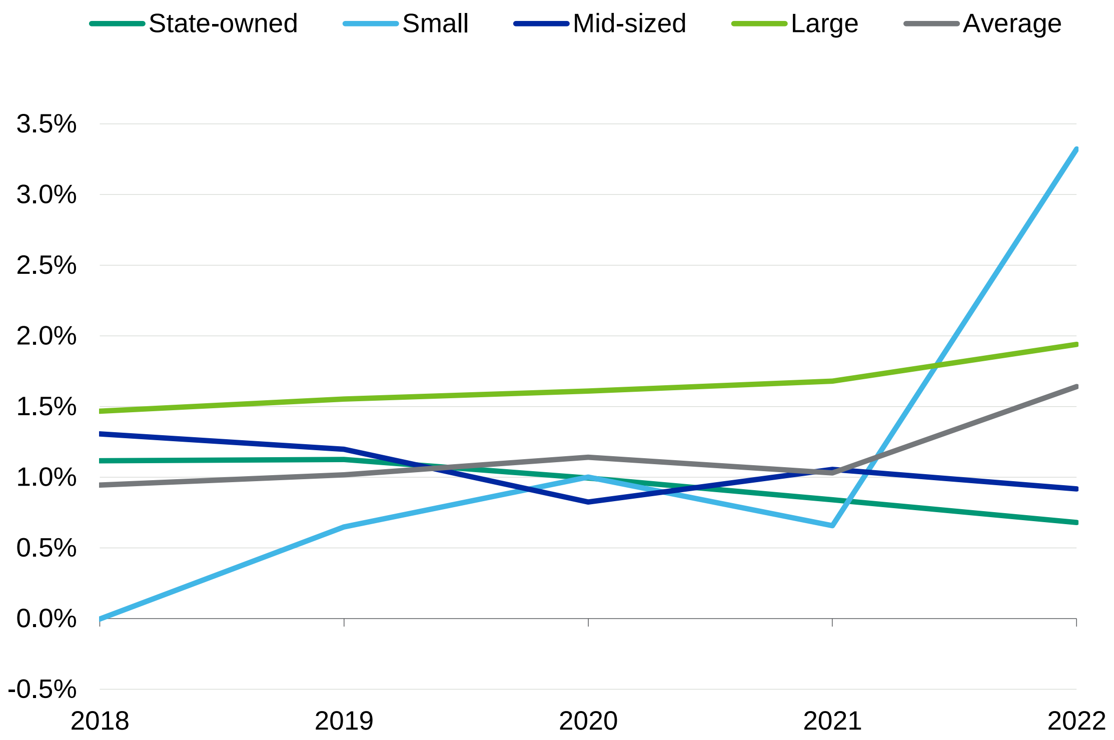
Weaker business cash flows, higher interest rates and operating costs, and refinancing difficulties in corporate bond market weigh on borrower debt repayment

Problem loans and credit costs



Source: Bank data, Vietnam Investors Service

NPL formation rate

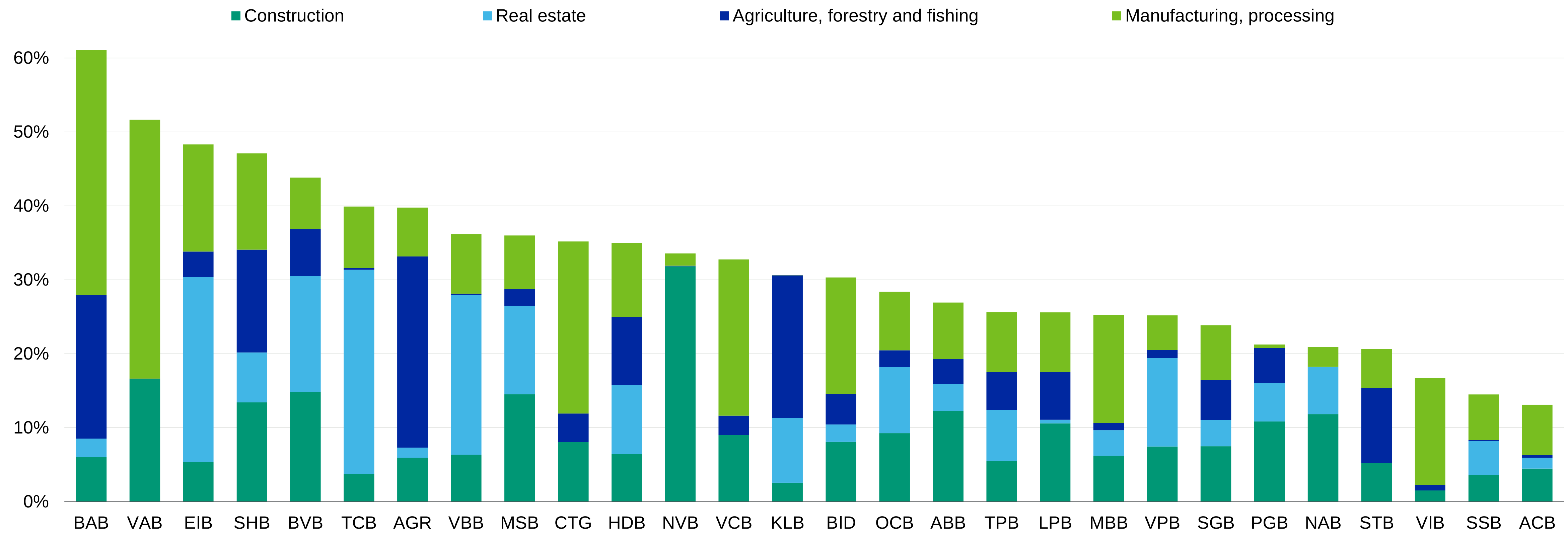


Source: Bank data, Vietnam Investors Service

Banks have material exposure to sectors at risk…

Export-oriented and manufacturing, real estate and construction are most vulnerable to increases in credit costs

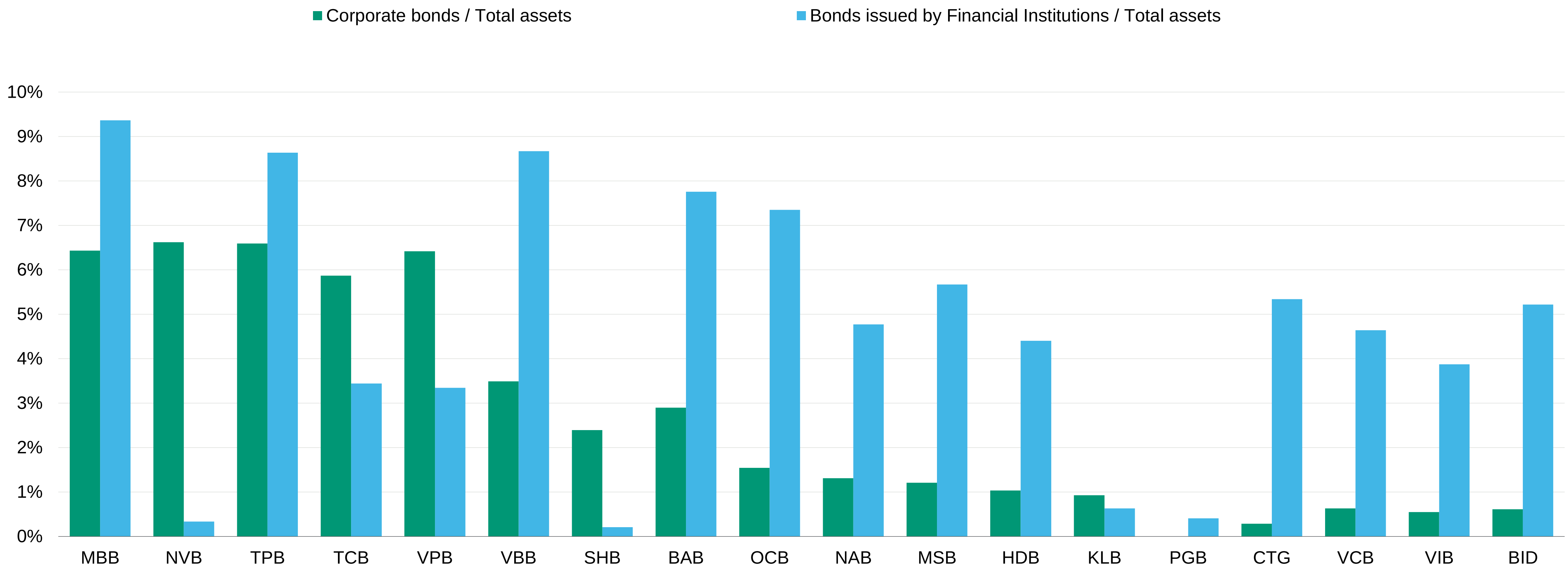
Percentage of total loans as of end-2021



.Source: Bank data, Vietnam Investors Service

…but limited exposure to corporate bonds

Bonds issued by non-financial corporates are less than 2% of total banking system assets

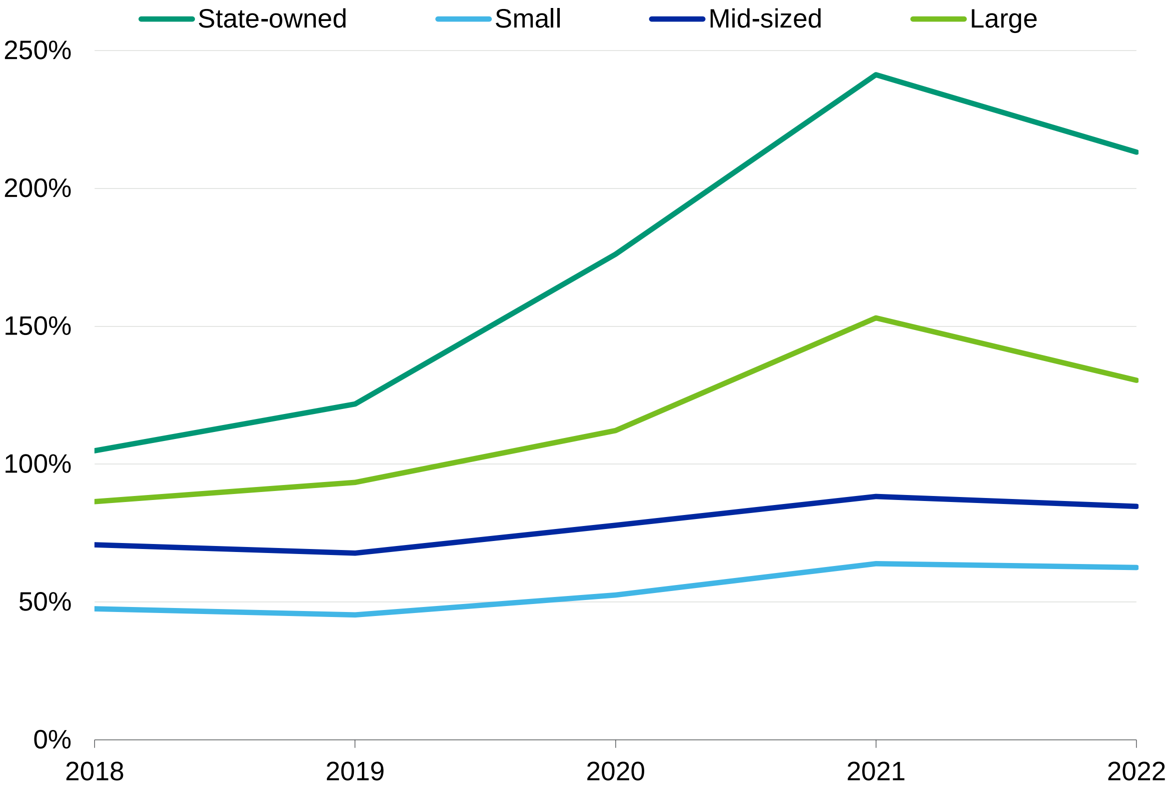


Note: Data as of end of 2022.

Source: Bank data, Vietnam Investors Service

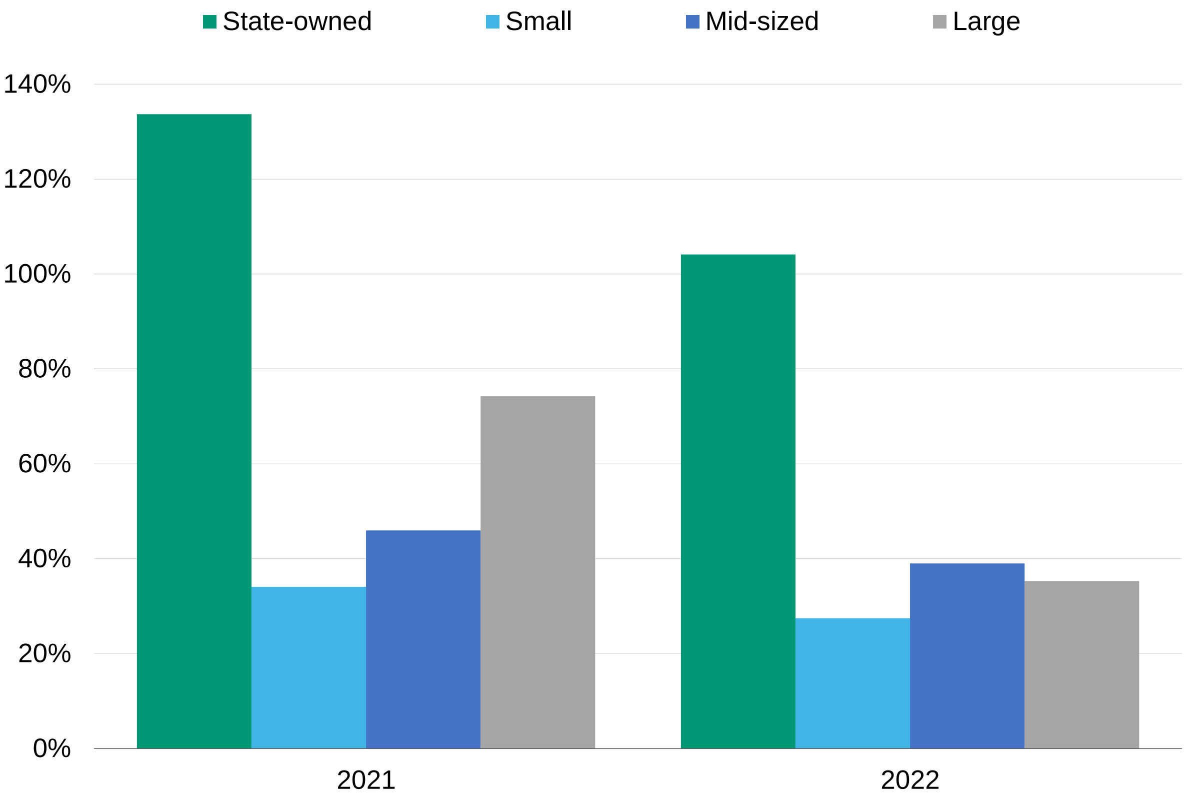
Loan loss coverage has improved but remains low for small and mid-sized banks

Loan loss coverage ratios by group of banks



Source: Bank data, Vietnam Investors Service

Loan loss coverage ratios for non-performing and special mention loans by group of banks



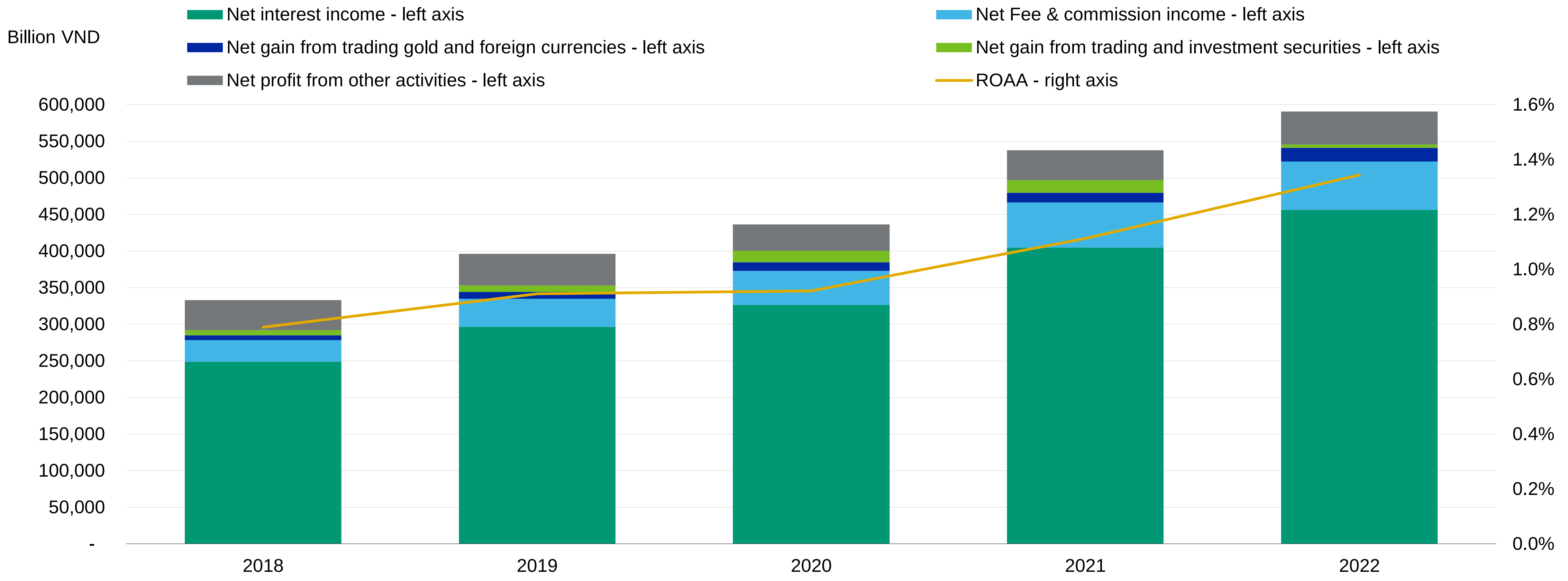
Source: Bank data, Vietnam Investors Service

3

Profitability will moderate from 2022 peak levels

Revenue growth from key sources will decline from weakening operating conditions

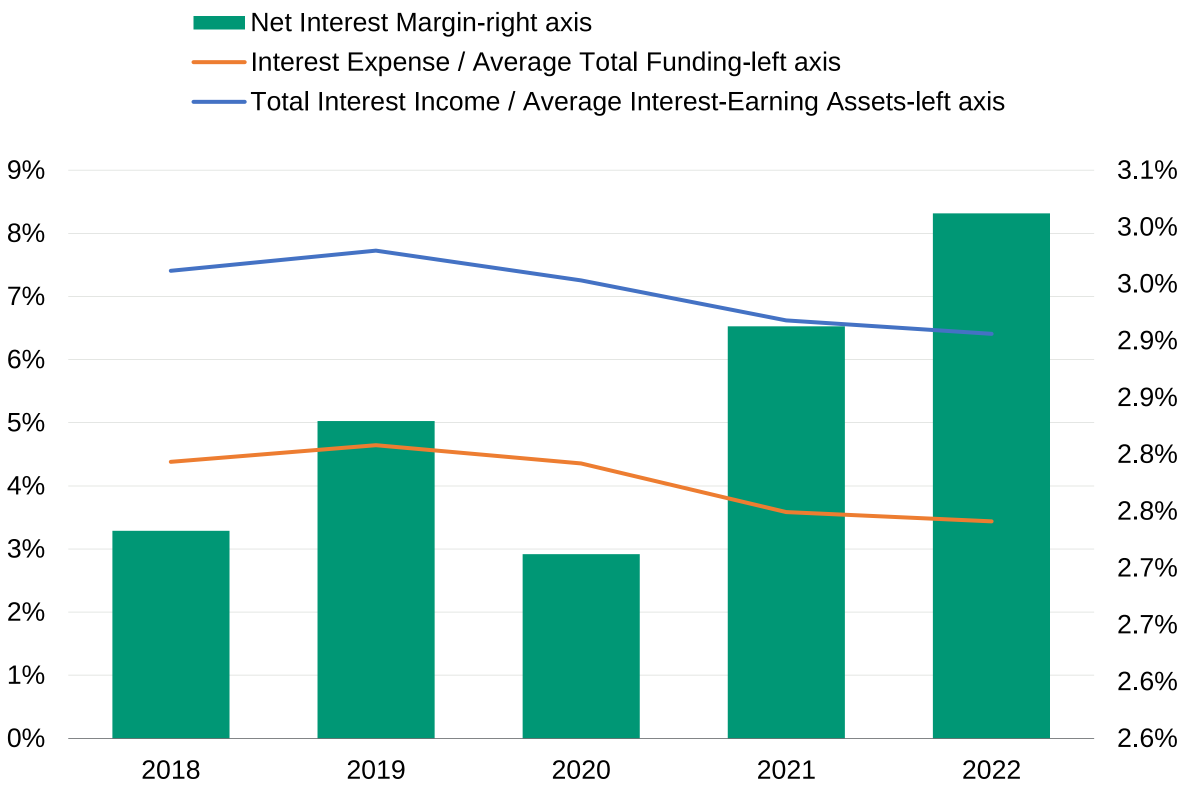
Revenue structure and return on average assets



.Source: Bank data, Vietnam Investors Service

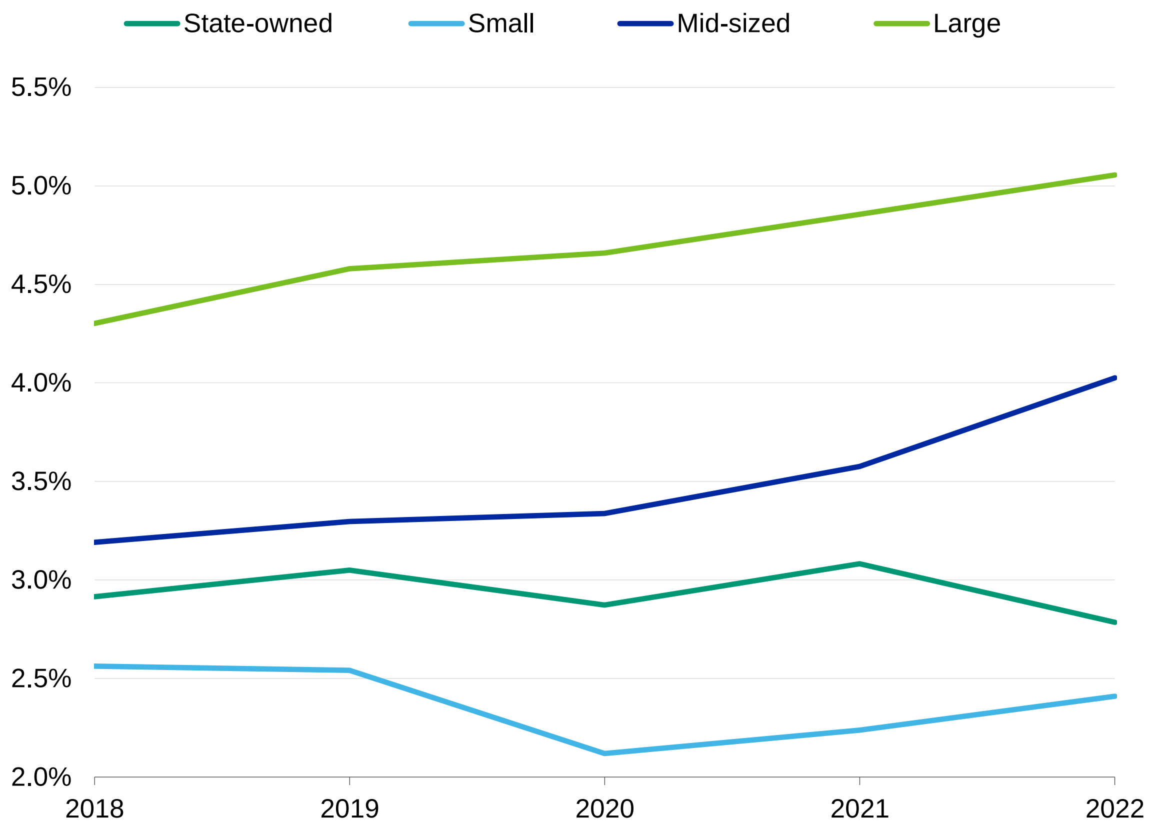
Net interest margins set to narrow as deposit costs increase more rapidly than lending yields

Net interest margins



Source: Bank data, Vietnam Investors Service

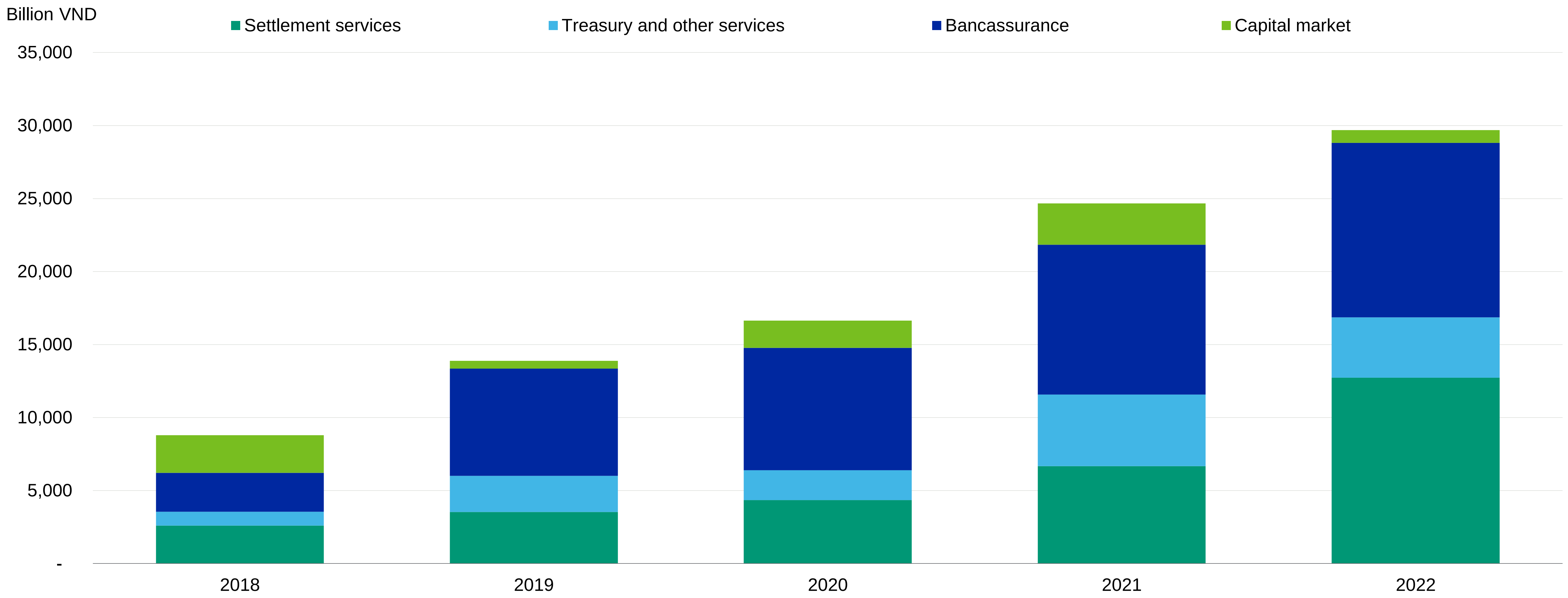
Net interest margins by group of banks



Source: Bank data, Vietnam Investors Service

Capital market-related and bancassurance income will shrink from weak market sentiment

Breakdown of non-lending income



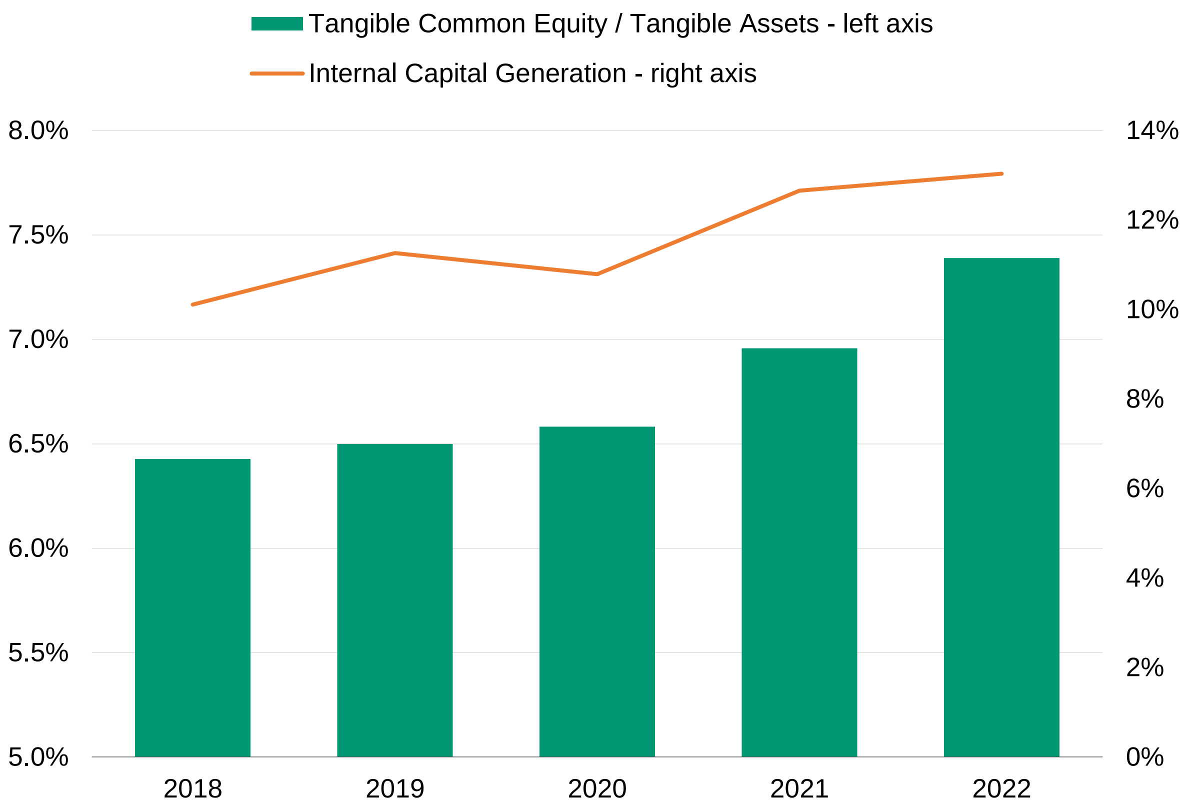
.Source: Bank data, Vietnam Investors Service

4

Capital levels will remain stable and weak by regional standards

Internal capital generation to weaken and weigh on bank capital levels in 2023

Internal capital generation



Source: Bank data, Vietnam Investors Service

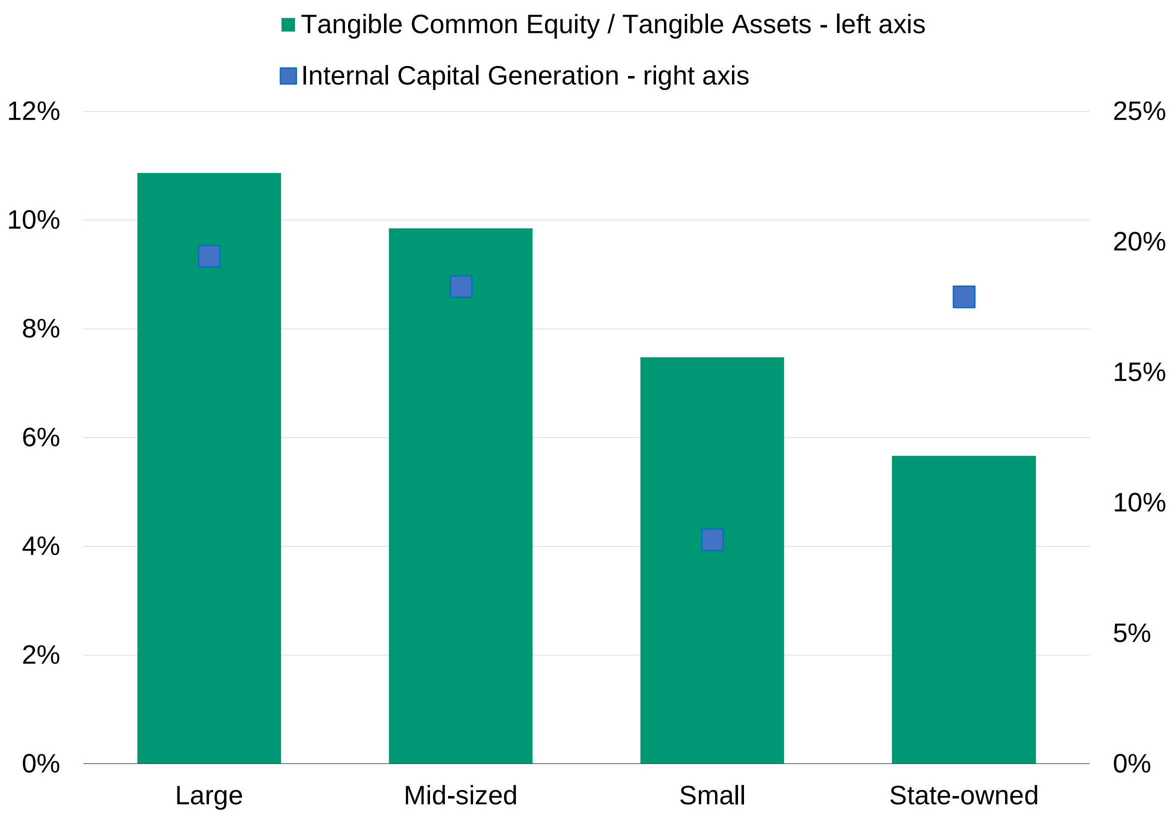
Aggregate tangible common equity to risk-weighted assets as of Q3 2022

Note: Data as of 2021 for Singapore and Philippines, Q2/2022 for Malaysia and Thailand

Source: Moody's Investors Service

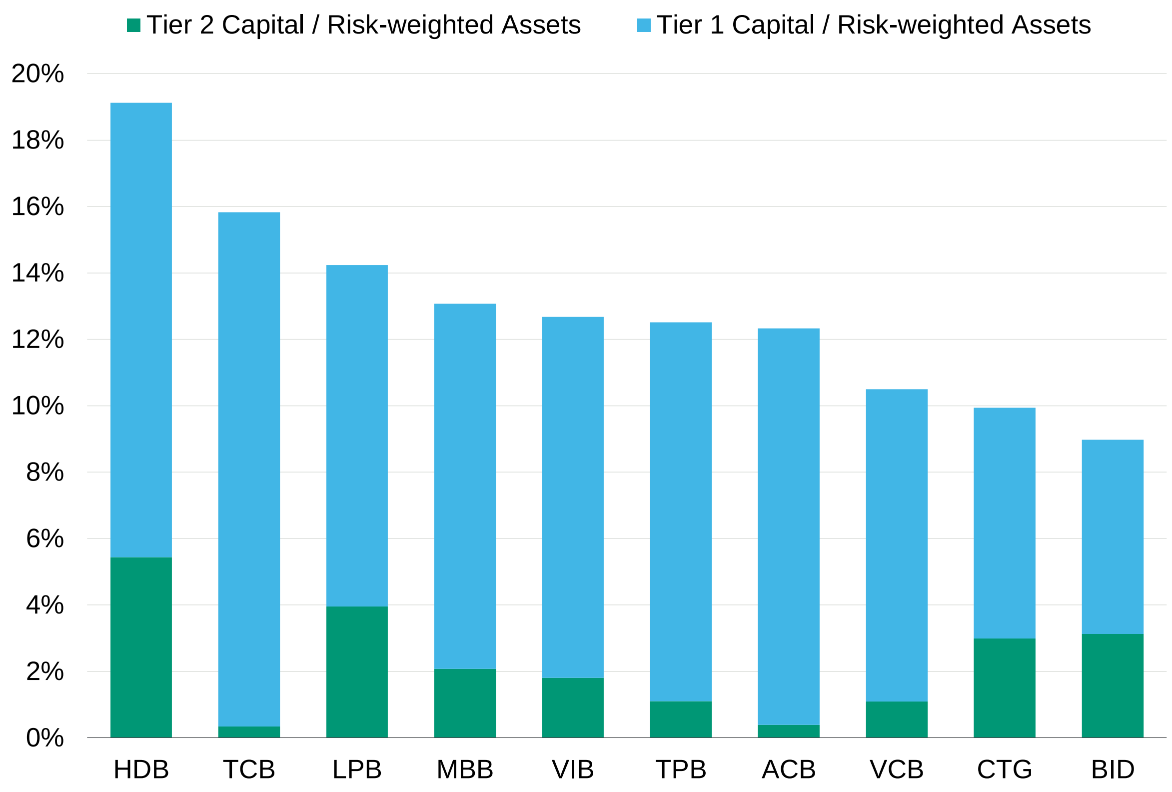
Tier 2 subordinated bonds help to supplement bank capital needs

Capital adequacy ratios by group of banks as of 31 December 2022



Source: Bank data, Vietnam Investors Service

Tier 1 and 2 capital ratios as of 30 June 2022



Source: Bank data, Vietnam Investors Service

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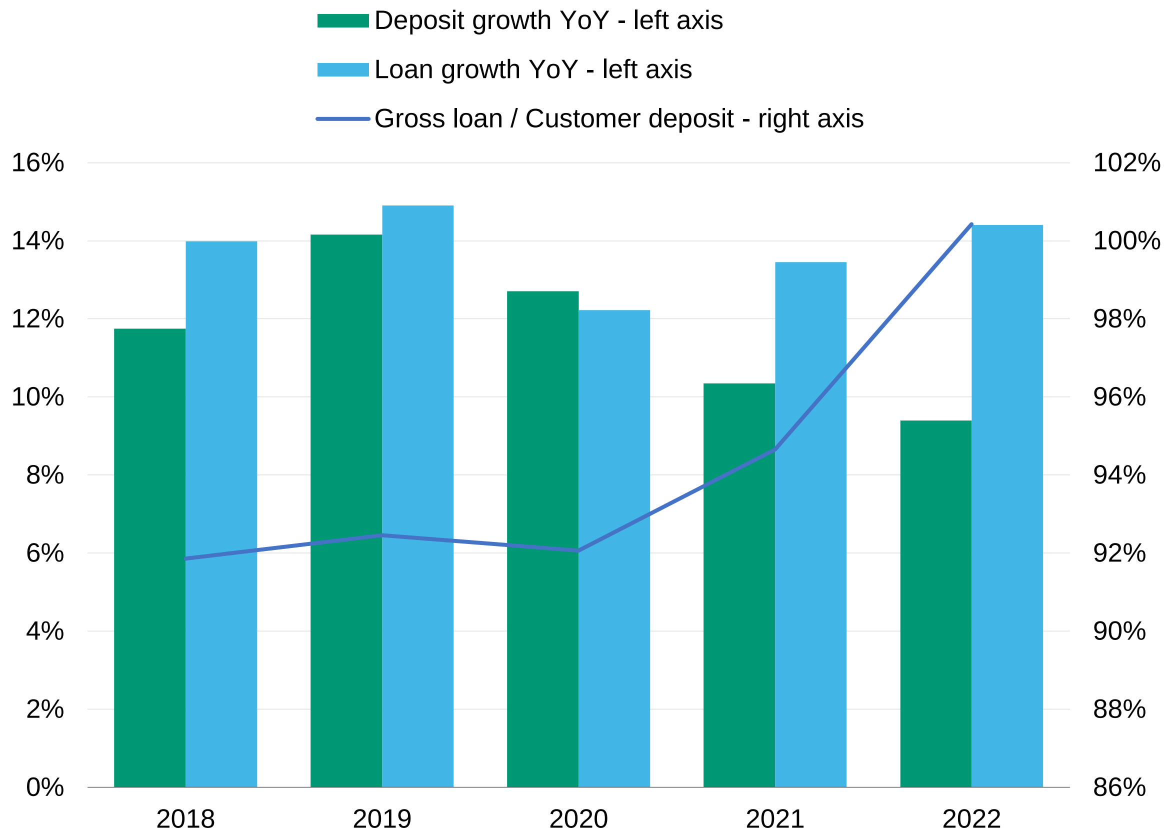
Liquidity will stabilize but remain tight, with mid-sized and small banks most at risk

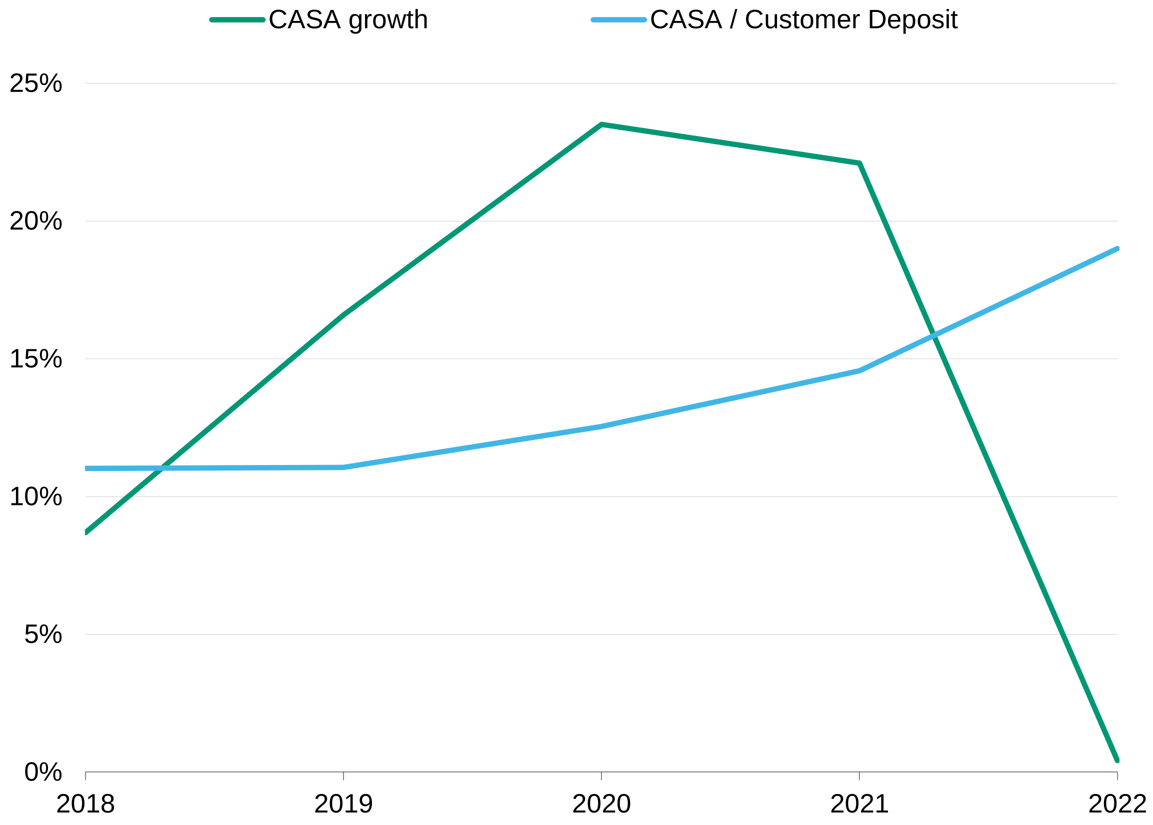
Weaker corporate cash flows and tight monetary policy stance will weigh on deposit growth

Deposit growth vs loan growth



Source: Bank data, Vietnam Investors Service

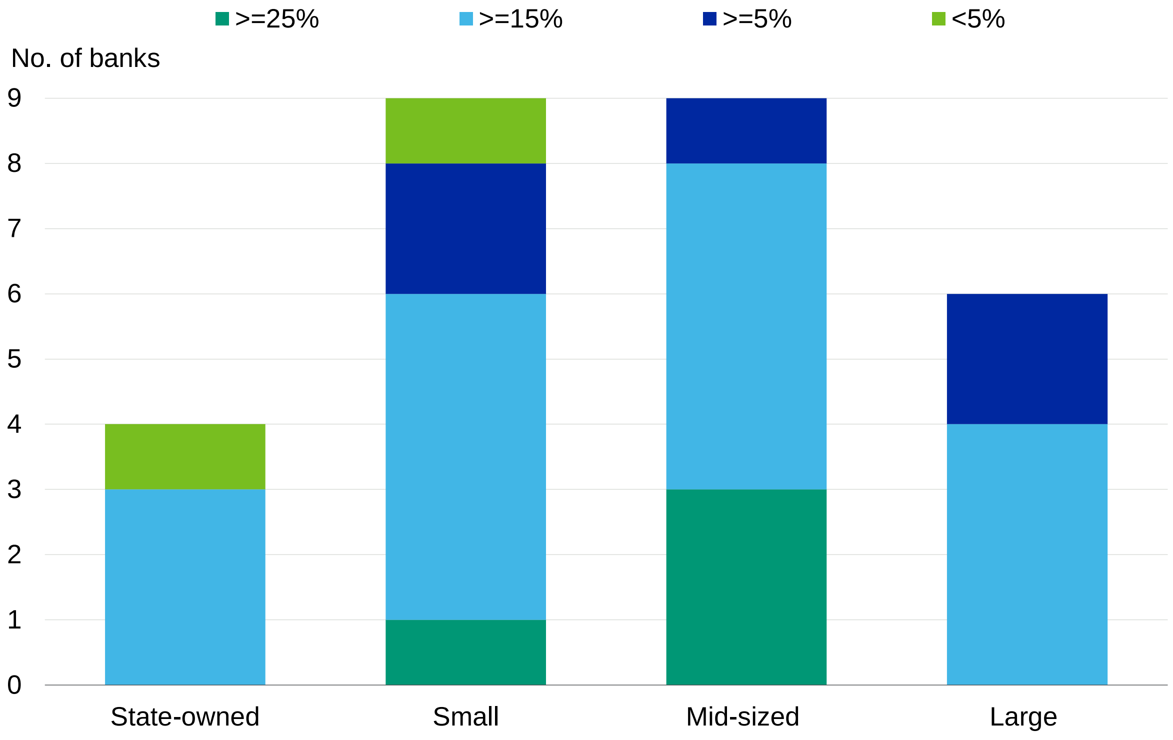
CASA deposits shrank in 2022



Source: Bank data, Vietnam Investors Service

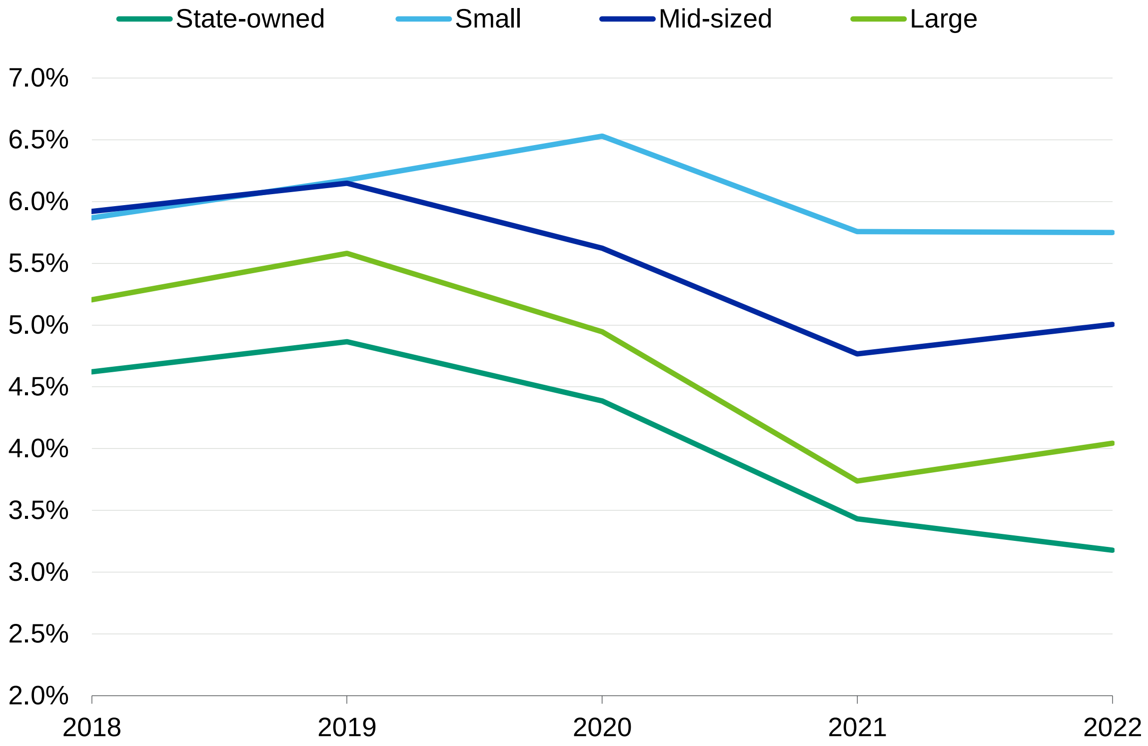
Mid-sized and small banks rely heavily on market funding and offer higher rates to secure deposits

Market funds as a percentage of tangible assets by group of banks



Source: Bank data, Vietnam Investors Service

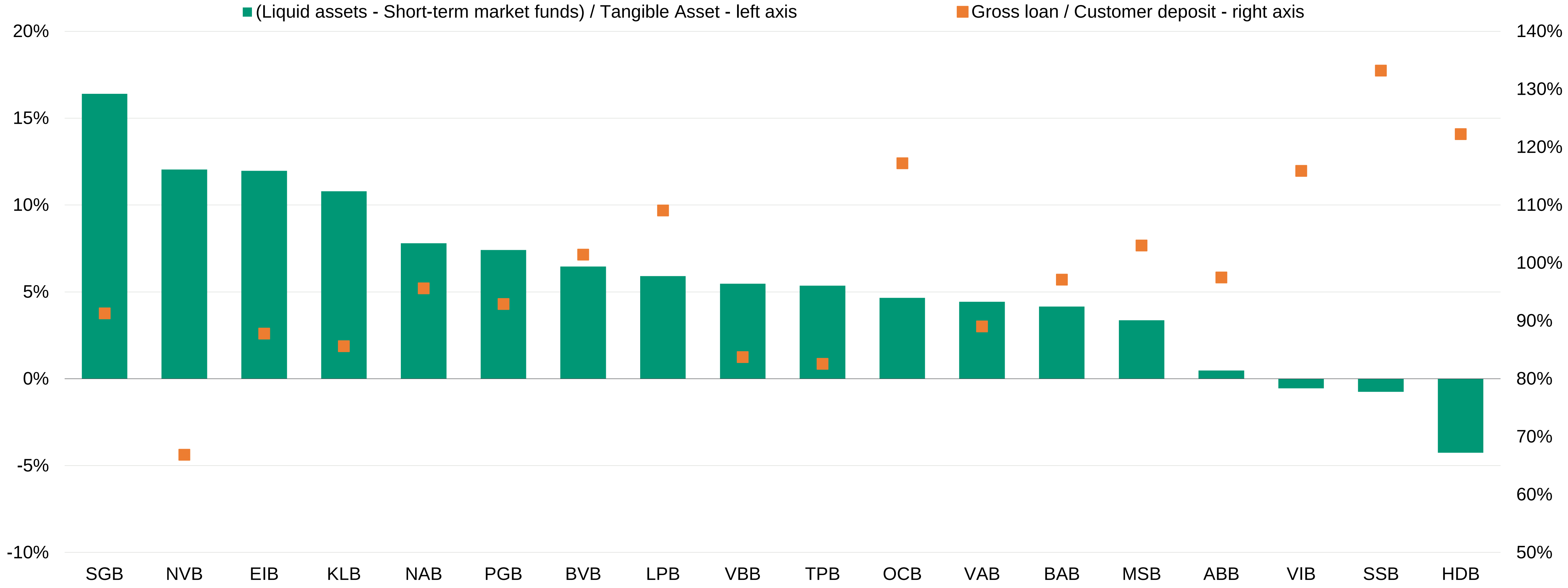
Deposit funding costs by group of banks



Source: Bank data, Vietnam Investors Service

Banks with high loan-to-deposit ratio and low liquid asset buffer are most at risk

Loan-to-deposit ratios and liquid asset buffer



.Source: Bank data, Vietnam Investors Service

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