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VIETNAM INVESTORS SERVICE

Credit Insight:

Policy rate cut to support economic growth

Banks and borrowers will benefit from lower funding costs

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SBV rate cut signals stabilizing domestic inflation, banks will benefit from lower funding costs

» On 14 March 2023, the State Bank of Vietnam (SBV) became the first central bank in Asia to cut policy interest rate this year, reversing its tightening monetary policy stance taken in 2022. This move was after the aggressive rate hikes by the US Federal Reserve (FED) and central banks globally to combat inflation and currency pressures.

» Following SBV decision, rediscount rate was revised down from 4.5% to 3.5% per year and the maximum short-term lending interest rate for certain priority sectors from 5.5% to 5% per year with Decision 313 & 314/QD-NHNN.

» This policy decision was prompted by SBV's intent to support economic growth and stabilize monetary market, on the back of stabilizing domestic inflation and foreign exchange market conditions.

Credits implications:

» We expect funding costs for banks and their borrowers to decline over the course of 2023 as a result of this policy action and SBV's efforts to lower market interest rates and stabilize domestic liquidity. Small banks will benefit most due to their reliance on interbank funding and vulnerability to keen competition for deposit funds.

- Deposit rates and interbank interest rates have since adjusted downwards. Banks are likely to pass on savings from funding cost to borrowers in response to the government's call for lower commercial lending rates to support businesses and the economy. Lower interest rate environment will support credit demand and stability of banking sector liquidity to facilitate access to credit. If and when the deposit rate cap is revised downwards, banks will make more material rate adjustments.

» The recent developments – including FED staying on its course of hiking interest rates and banking sector turmoil in the US and Europe – do not have a material immediate impact on Vietnam's operating environment, due to stable inflation and limited direct exposure to the affected banking markets.

- The recent policy rate cut by SBV contrasts with the policy direction of Fed and other central banks in the region, which are still managing stubborn inflation.

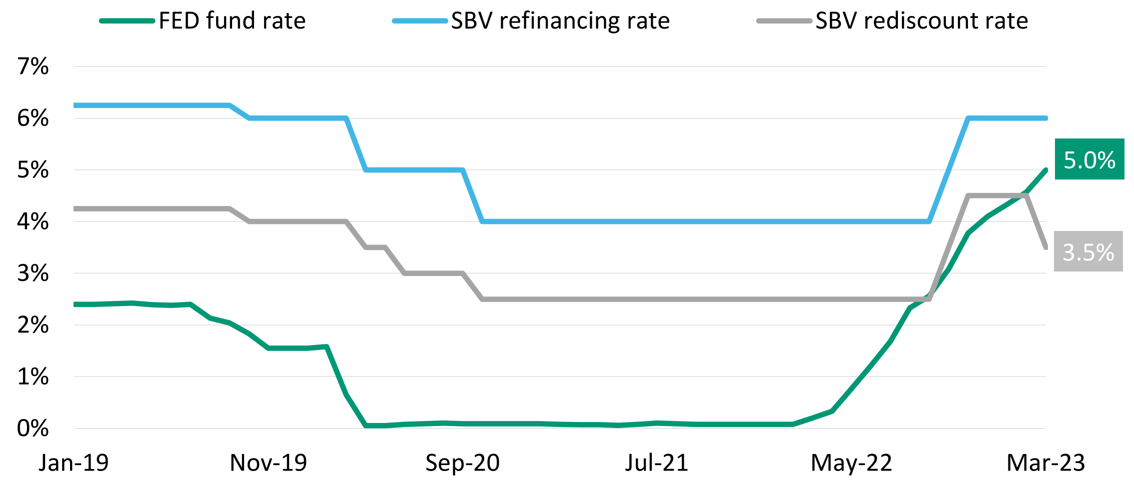
Our baseline expectation:

» In our base case, we expect SBV will continue to strike a balance in containing domestic inflation, stimulating economic growth, liquidity, and maintaining foreign exchange stability. Domestic inflation - mainly driven by the supply-side factors - has been under control. SBV has also been able to utilize various tools to improve money supply and banking sector liquidity and prop up its foreign currency reserves.

» Barring any significant fund outflows from emerging markets and Vietnam that may be triggered by future rate hikes globally, we expect SBV to stay on its course to maintain a flexible and accommodative monetary policy stance.

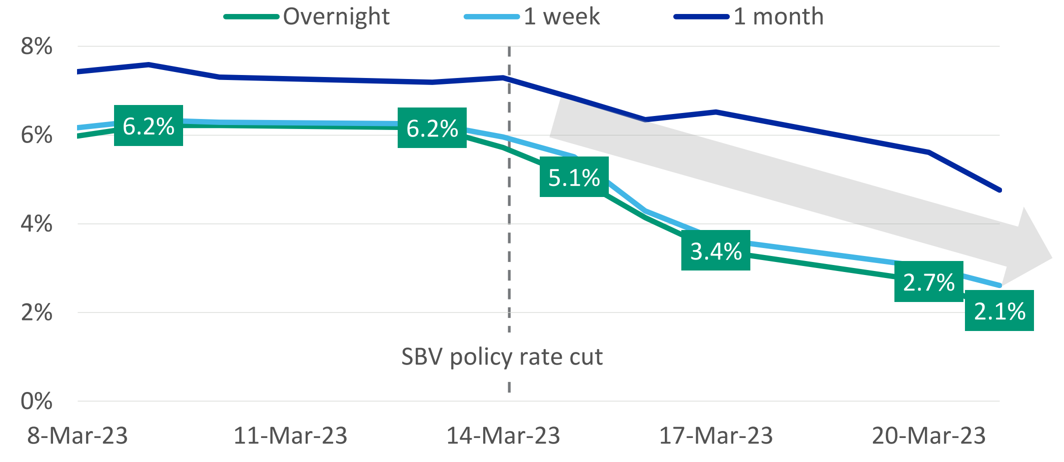
Small banks will benefit most from lower funding costs

SBV partially unwinds its rate hikes in 2H 2022



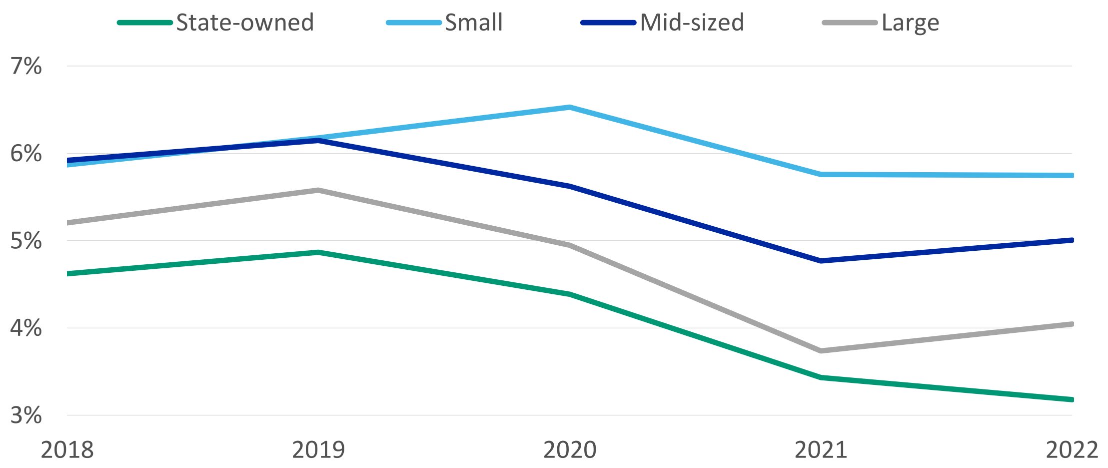
Source: FED, SBV

Interbank rates had fallen since policy rate cut



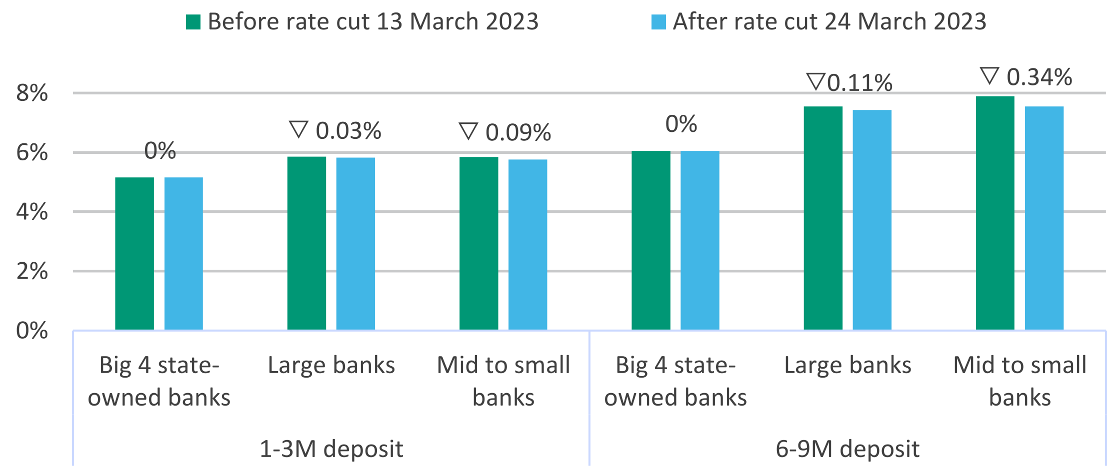
Source: Vietnam Investors Service

Small banks with weak deposit franchise & high funding costs will benefit most



Source: Vietnam Investors Service

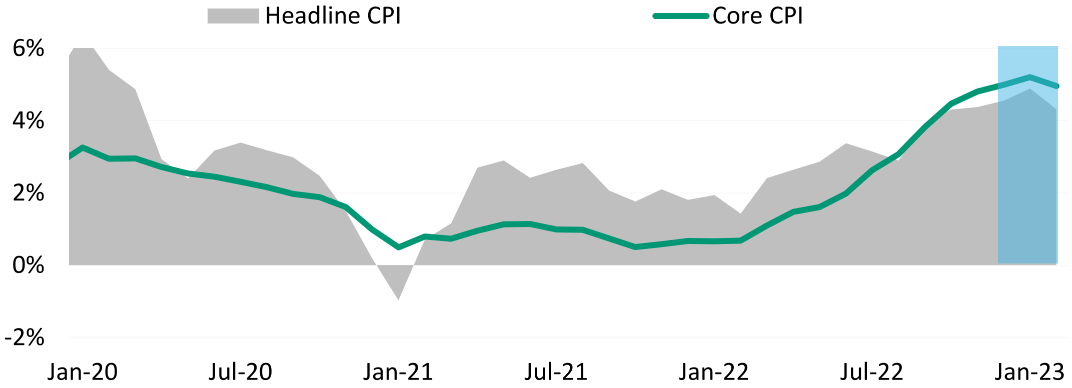
Deposit rates have declined more substantially for smaller banks



Source: SBV, bank quoted rates, Vietnam Investors Service

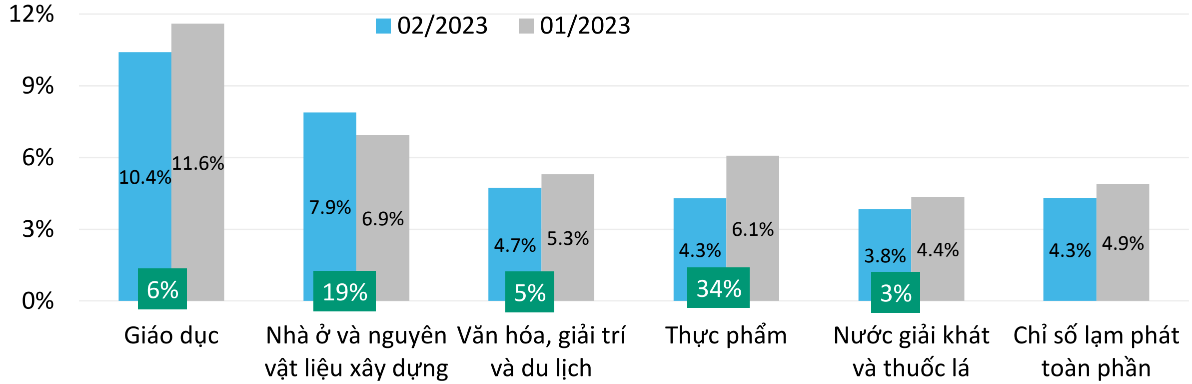
SBV will remain vigilant of regional fund flows that may impact FX stability

Inflation started to decline towards government's 4.5% target



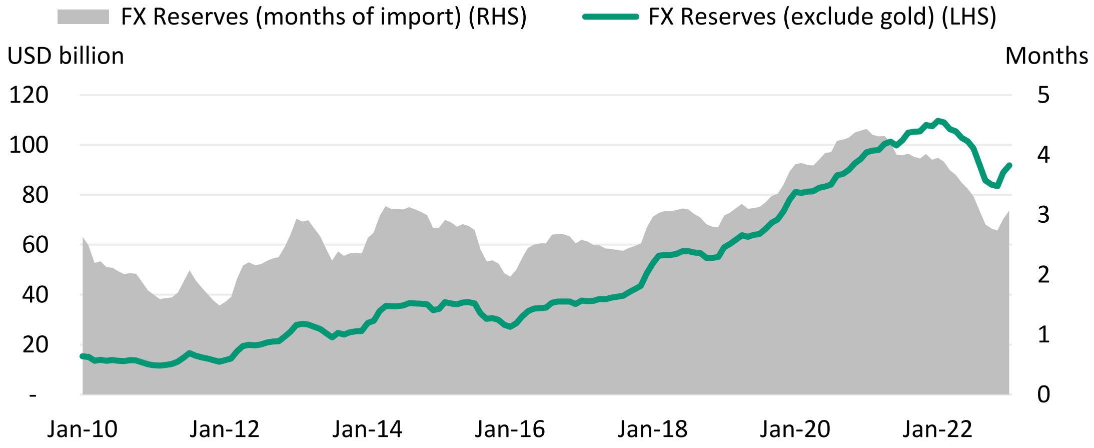
Source: GSO, Vietnam Investors Service

Higher housing and construction materials price will drive the headline CPI



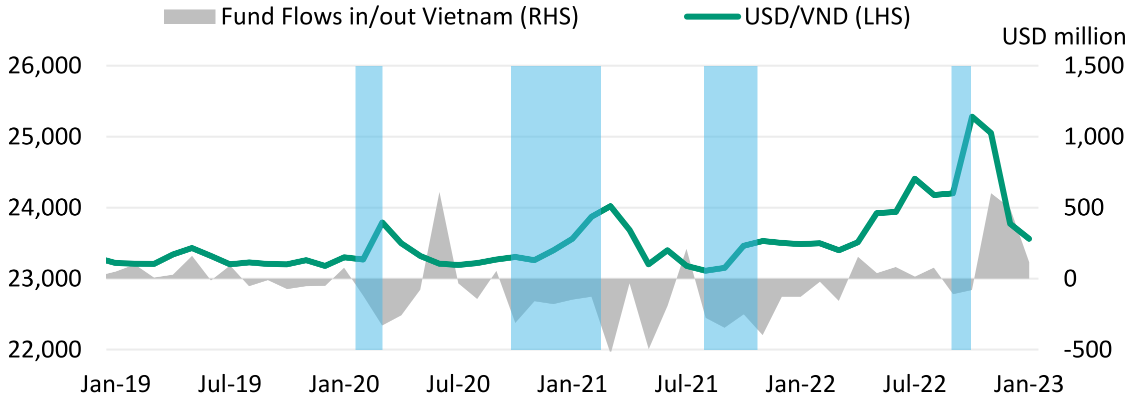
Note: Numbers in the green box denote the contribution to Headline CPI
Source: General Statistics Office (GSO), Vietnam Investors Service

Foreign reserves have recovered since December 2022



Source: CEIC, GSO, Vietnam Investors Service

Future fund outflows may trigger downside risks to FX stability



Source: The Institute of International Finance (IIF), Vietnam Investors Service

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