2024 Credit Outlook

Low interest rates and policy measures will support the recovery of domestic operating conditions and dampen the effects of external uncertainties

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» **We expect the credit outlook to improve over the course of 2024, underpinned by low financing costs, improving domestic operating conditions, and a slower pace of new corporate defaults.** The low interest rate environment will drive lower financing costs for borrowers and encourage business expansion. We also expect that the implementation of various government policy measures and changes to the laws and regulations on the property sector will drive stronger investment and domestic consumption. As a result, domestic business conditions will improve and drive stronger sales and operating cash flows for domestic businesses. Debt serviceability will improve, marked by a slowdown in the pace of new loan delinquencies and new corporate bond defaults.

» **Refinancing risks for the property developers will remain high, and partially alleviated by improved access to new financing.** We expect the low interest rate environment, upcoming amendments in property-related laws, and the government's efforts to resolve obstacles to project approval will facilitate new financing for developers in 2024. Nonetheless, refinancing risks for the property developers will remain elevated in 2024 as they cope with high leverage and significant bond maturities. In 2024, property developers have around VND 120 trillion worth of bonds maturing - highest level over the past five years.

» **Weak external demand will continue to dampen prospects of recovery for export-related manufacturing sector.** Retail sales and manufacturing activity in Vietnam's key export markets - U.S. and E.U. – will likely remain weak and weigh on the demand and production activity of Vietnamese export products. On the other hand, we expect business conditions for other domestic business sectors will benefit from low financing costs and government spending. For example, construction and materials sectors will benefit from higher public investment disbursement in 2024, alongside the recovery of new property project development.

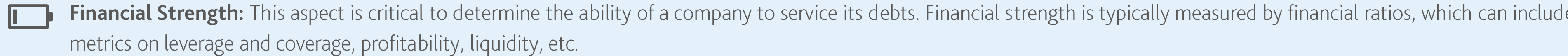
» **Bank asset quality and profitability will improve gradually amid a stronger operating environment and low interest rates.** We expect loan delinquencies to slow as borrowers' debt repayment capability improve amid stronger cash flows and low interest rates. Net interest margins will begin to widen as banks adjust their deposits to lower rates and pick up lending. Stronger profitability will help banks to maintain stable capital. Liquidity will remain stable with banks raising more longer-term bonds to meet stricter short-term funding to the medium and long-term lending ratio (SMLR) requirement.

Credit Outlook: Definition and Assessment Framework

Our Credit Outlook reflects our view of credit conditions in Vietnam over the next 12 months. It captures our view of credit trends and the direction of expected changes in creditworthiness or credit quality of corporate businesses operating in key industry sectors in Vietnam. It also reflects our forward-looking assessment of the abilities of corporate businesses in Vietnam to service and meet their debt obligations.

We denote our credit outlook using three distinct categories, namely ‘Deteriorate’, ‘Improve’ and ‘Stable’.

Our assessment framework is centered around the four key pillars as explained below.



Financial Strength: This aspect is critical to determine the ability of a company to service its debts. Financial strength is typically measured by financial ratios, which can include metrics on leverage and coverage, profitability, liquidity, etc.

A strong financial strength profile is characterized by low leverage, strong and stable profitability, well-matched asset and liability structure, and sufficient cash resources to cover maturing debt repayments.

Business Conditions: We assess business conditions by considering multiple factors that will impact a company’s ability to conduct its business activities, generate sales and cash flow and stay viable.

The factors include the economic outlook, supply and demand dynamics of a company’s product and services, external competition, market sentiment, etc. Strong business conditions will likely enhance the operating prospects of a company, which will bode well on its ability to generate cash flow to meet debt obligations on time.

Policy Measures: We consider how companies will be affected by the government’s policy measures, for example monetary easing, fiscal spending, changes in laws and regulations, etc. We analyze the policy intention and direction, as well as the extent of aid and/or disruption to industry sectors and companies.

Policy measures tend to have a strong influence on both business and financing conditions. Policy measures that are easing in nature are generally positive for business growth. For example, the roll-out of fiscal stimulus, subsidies, changes in laws and regulations may promote business activity.

Financing Conditions: This relates to a company’s ability to access and secure new financing for its business needs or to refinance its outstanding debt. We assess the availability and accessibility of financing, focusing on factors such as overall market cash flow movement, interest rate trends, credit availability, and borrowing conditions.

Easing financing conditions are typically marked by a low interest rate environment, ample liquidity headroom in the banking sector to support lending, good liquidity in the corporate bond market, etc.

2024 Credit Outlook

We expect the credit outlook in Vietnam to improve in 2024, underpinned by improving domestic business conditions, low financing costs, and a slower pace of new corporate defaults

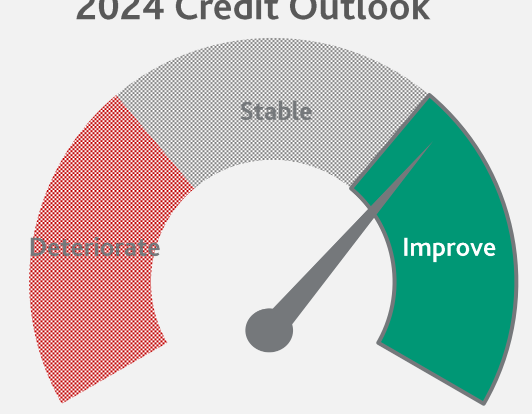
Various government policy support measures including tax cuts, extension of tax payment dates, and boosting public investment in infrastructure will help to lift domestic demand and business activities and offset weakness in external demand. These measures are aimed at achieving the government's GDP growth target of 6.0 – 6.5% for 2024, higher than the 4.2% recorded in the first nine months of 2023.

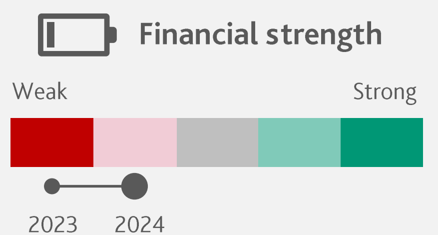
Additionally, the upcoming changes to the legal framework and laws related to the property sector – which experienced a significant downturn and weak sentiment over the past two years - will help to improve business conditions for companies in the property development and ancillary sectors such as construction and materials. The new laws will either ease or resolve key legal obstacles for domestic companies to advance their business activities, improve the market sentiment around the industry and company growth prospects, and support the gradual recovery of their operating cash flows.

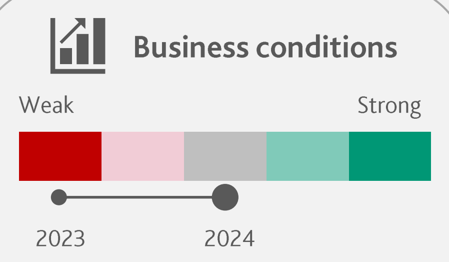
Inflation and currency pressures have been well-managed, and upside risks appear to be well-contained, barring a deeper escalation of geopolitical tensions that may trigger prolonged periods of oil and food price shocks. As such, we expect domestic interest rates to remain at current low levels, which will keep financing costs low for borrowers and bond issuers and support refinancing needs.

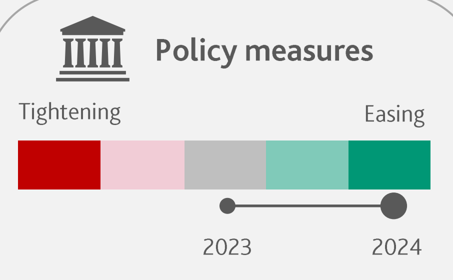
Debt serviceability among highly leveraged corporates especially those in property, construction, and utilities sectors will improve gradually as operating cash flows recover and access to new financing improves. As such, we expect the pace of new loan delinquencies and new corporate bond defaults will slow in 2024.

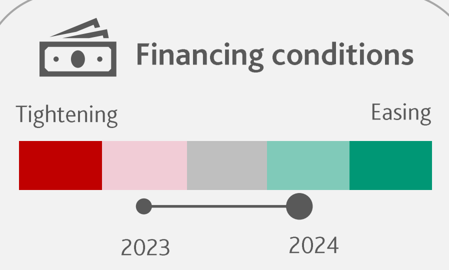
Exhibit 1: Credit Outlook will improve in 2024











Source: Vietnam Investors Service

» **We expect government support measures and changes in major regulations will boost domestic consumption and offset weak external demand**

In 2024, we expect demand from global markets to remain weak due to slowing economic growth, as reflected in weak Manufacturing Purchasing Managers' Index (PMI) data across Vietnam's key export markets (Exhibit 2). This will continue to weigh on Vietnam's export-oriented economy [1].

With the GDP growth rate target of 6.0 – 6.5% in 2024, the government is actively supporting the economy through public spending and tax cuts, which is reflected in the 2024 record high in planned budget spending (Exhibit 3).

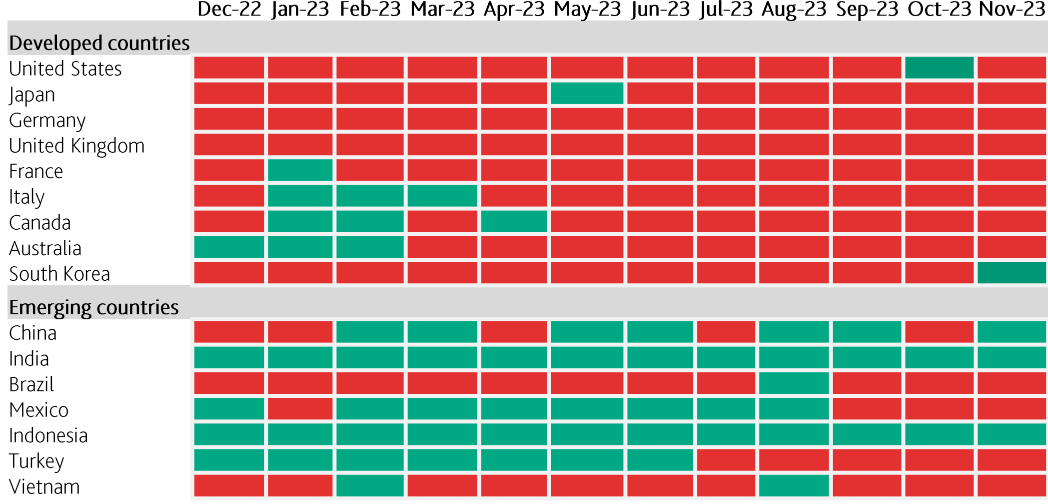
With the public debt level decreasing in recent years, we view that the government will have sufficient headroom to afford the support measures.

In addition, we expect the recent changes to the major regulations such as the revised Law on Real Estate Business, Law on Housing, PDP8, etc. will help improve market sentiment and support business activities in 2024.

The revised laws in the property sector will help accelerate new project approvals, which will aid the developers in accessing new financing, advance their project development and sales, and boost operating cash flow.

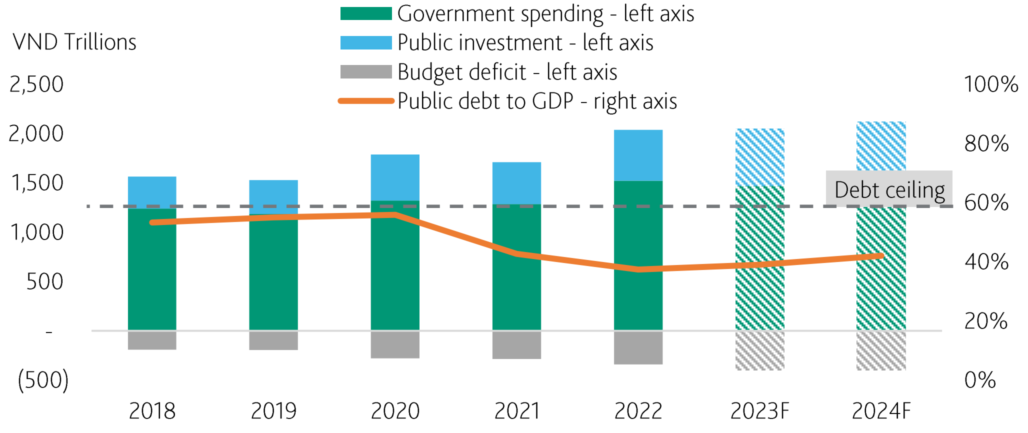
The PDP8 outlines the government's development roadmap for the power sector, and will, over the longer term, help attract new investment to scale the renewable energy sector in Vietnam.

Exhibit 2: Manufacturing Purchasing Managers Index (Red: <50; Green: >=50)



Source: Trading Economics, Vietnam Investors Service

Exhibit 3: Fiscal spending and public investment are at record highs and expected to offset weak external demand



Source: General Statistics Office (GSO), Vietnam Investors Service

[1] Refer to our Credit Insights: Weak external demand will weigh on Vietnam's exports (19 April 2023)

» Low interest rate environment will drive lower financing costs for businesses

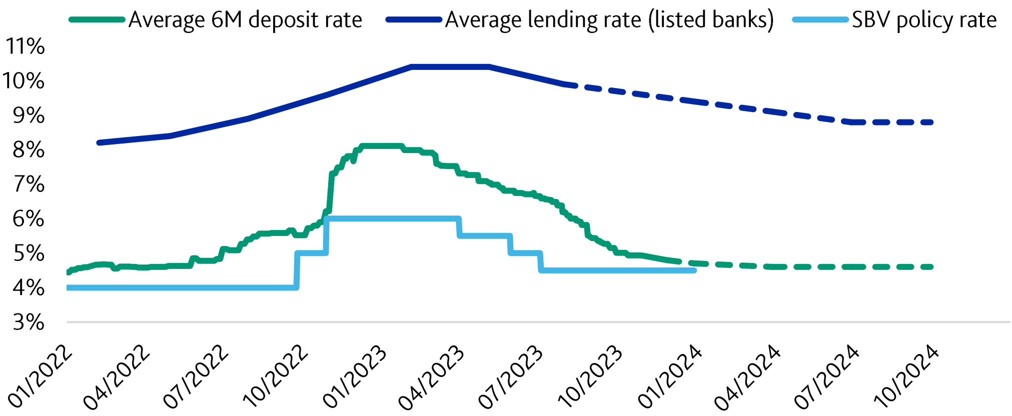
In 2024, we expect deposit rates to remain low and transmit to lower lending rates. Such transmission will lead to lower financing costs and alleviate the debt servicing burden of borrowers and bond issuers (Exhibit 4).

Food prices, which account for a third of headline inflation, will likely remain stable, barring a scenario of a deeper escalation in geopolitical tensions that may trigger prolonged periods of global oil and food price shocks. Vietnam has proven to be relatively resilient to shocks in global food supply and food prices, as it is largely reliant on domestic food supply (Exhibit 5).

Currency pressures have been well-managed; supported by Vietnam's resilient balance of payment position from strong FDI and remittance inflows, recovering foreign exchange reserves, and limited foreign participation in onshore capital markets.

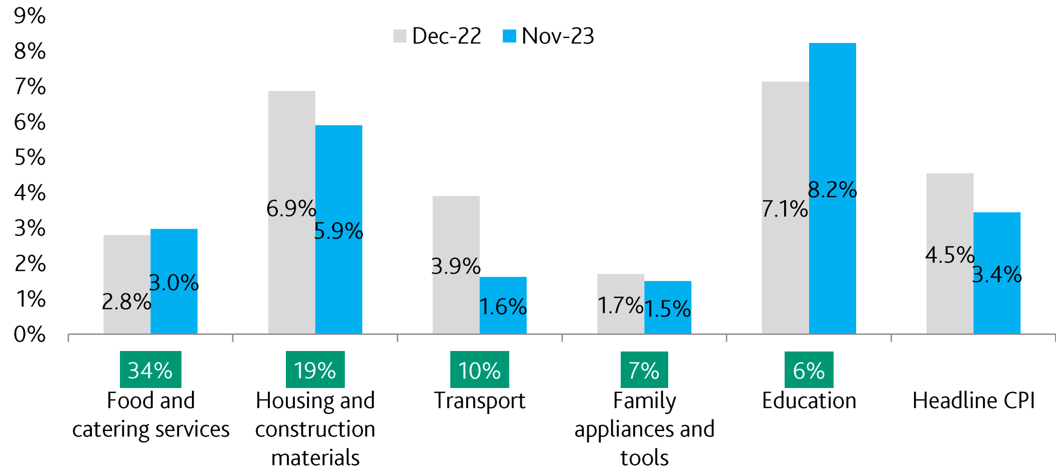
Globally, central banks have either signaled that interest rates have either peaked or that they are close to the end of the monetary tightening cycle. Further easing in global interest rates will add to the stability of the interest rate environment in Vietnam.

Exhibit 4: We expect the low interest rate environment will continue throughout 2024



Note: The average lending rate is annualized, calculated by dividing total interest income from loans by total loans across listed banks.
Source: Bank data, Vietnam Investors Service

Exhibit 5: Food prices driving the headline Consumer Price Index (CPI) will likely remain stable [2]



Note: Numbers in the green box denote the contribution to Headline CPI
Source: GSO, Vietnam Investors Service

[2] Refer to our Credit Insights: Policy rate cut to support economic growth (28 March 2023)

» Credit risks will ease through a slower pace of new defaults across sectors, and supported by more proactive negotiations to extend bond repayment periods

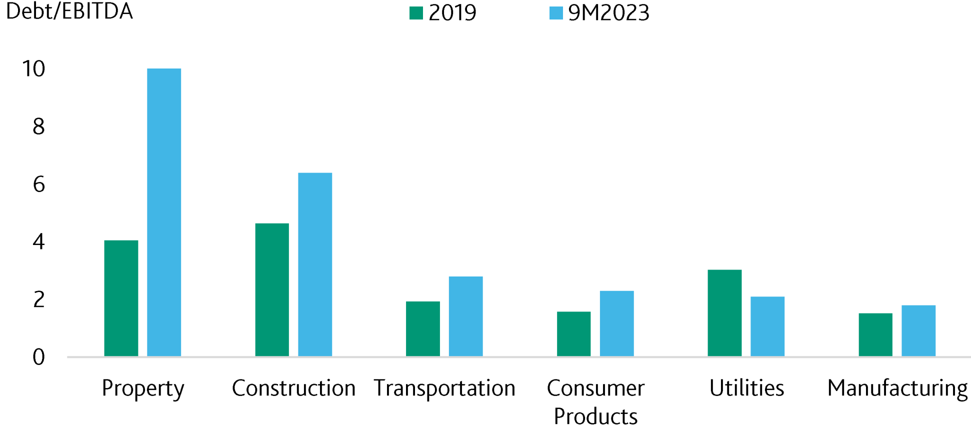
Firms in the property and construction sectors have weak financial strength in general, characterized by high leverage and weak cash resources. On average, property and construction issuers' debt-to-EBITDA ratios as of Q3 2023 are 10.2 times and 6.4 times, respectively, highest among sectors (Exhibit 6).

We observed that the default rate of the corporate bond market has slowed down since Q2 2023, specifically in three main sectors: property, construction, and utilities sector.

We expect debt serviceability among highly leveraged corporates especially those in property, construction, and utilities sectors will improve gradually as operating cash flows recover and access to new financing improves.

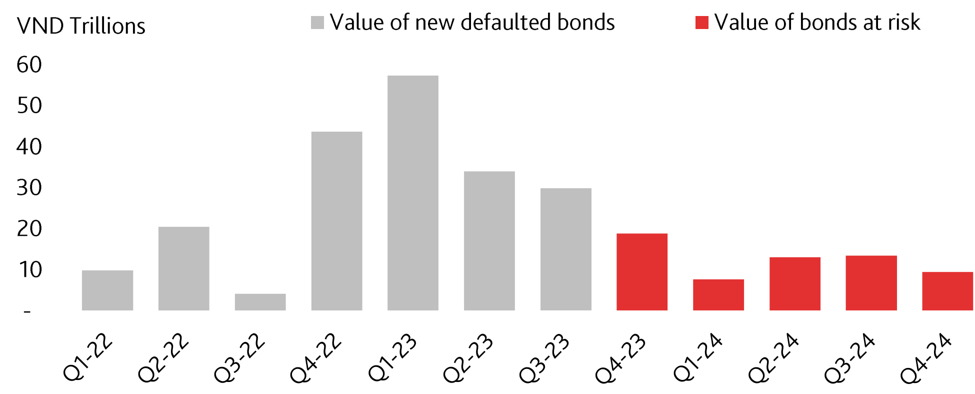
Many defaulted issuers have been proactive in default negotiation, most of which resulted in maturity extension and mostly for a period of over one year [3]. With the gradual improvements in financing and business conditions across sectors in 2024, we expect a slower increase in new bonds at risk [4] in 2024 (Exhibit 7) and slower non-performing loan (NPL) formation rates among banks.

Exhibit 6: Property and construction companies have the highest leverage profiles in Vietnam



Note: VHM is excluded from the calculation of property as it is not representative of sector performance
Source: Company data, Vietnam Investors Service

Exhibit 7: We expect new bond defaults will decline in 2024 [4]



Source: HNX, Vietnam Investors Service

[3] Refer to our Corporate Bond Market Perspective: Proactive negotiations will slow down bond defaults in 2024, marking the start of a new development phase and recovery of bond issuance (10 October 2023)
[4] We assessed bonds at risk of default based on the leverage, profitability, and cash resources of the companies. Refer to our: Corporate Bond Market Perspective: Real estate-related liquidity issues will drive up corporate bond defaults in 2023, new regulations to provide some relief for VND113 trillion of bonds at risk (6 April 2023)

Key drivers of credit conditions for major industry sectors in 2024

Exhibit 8: Most sectors will benefit from policy support and easing financing conditions, while manufacturing and transportation sectors will continue to be challenged by weak external demand

Legend: Improving (green) · Stable (grey) · Deteriorating (red)

Sector	Financial strength	Business conditions	Policy measures	Financing conditions	Key drivers in 2024
Banks	Stable	Stable/Improving	Stable/Improving	Improving	• Slowing formation rate of new problem loans and moderating credit costs • Stronger loan growth and wider net interest margins will boost profitability • Stable liquidity as deposit growth keeps pace with credit growth
Securities	Stable	Stable/Improving	Stable	Stable/Improving	• Improving market sentiment will support higher market trading activity and income • Sizable exposure to corporate bonds pose downside risks • Recent capital raises provide buffer against asset risks and potential losses
Consumers	Stable	Stable	Improving	Stable/Improving	• VAT tax cut and income tax deferral will stimulate consumer demand and spending • Consumer confidence to improve with recovery in operating conditions
Construction & Building materials	Stable/Deteriorating	Stable	Stable/Improving	Stable/Improving	• Benefit from recovery in property market and pick-up in new project development, and disbursement of public investment nationwide • Lower lending rates will support refinancing and debt serviceability
Utilities	Stable/Deteriorating	Stable/Improving	Stable/Improving	Stable/Improving	• Demand for electricity to increase alongside stronger economic and business growth • Increasing retail electricity prices will improve the sector's operating cashflow • PDP8 will attract new investment for the renewable energy sector over time
Property	Deteriorating	Stable/Deteriorating	Stable/Improving	Stable/Improving	• Upcoming changes to laws will boost project approvals and access to new financing • High leverage and weak coverage, as well as significant debt maturities over the next 12 months underpin significant refinancing pressure for many developers
Manufacturing	Stable/Deteriorating	Deteriorating	Stable	Stable/Improving	• Weak demand in key export markets • Lower lending rates will support refinancing and debt serviceability
Transportation	Stable/Deteriorating	Stable	Stable	Stable/Improving	• Weak demand in key export markets • Fuel costs remain high and remain vulnerable to further escalation of geopolitical tensions

Source: Vietnam Investors Service

Property sector's refinancing risk will ease from greater access to new financing

» Refinancing pressure will remain high in 2024 as bond maturities and leverage reach peak levels

Listed developers' short-term debt balance in Q3/2023 reached VND 64.7 trillion, slightly declined compared with 2022 but still 1.6 times larger than 2021. Furthermore, we expect bond maturity in 2024 for the property sector will reach the highest level of over VND 120 trillion (Exhibit 9).

Developers' leverage measured by Debt/EBITDA also peaked in Q3/2023 as the sharp decline in EBITDA outpaced debt reductions. These indicators reflect significant refinancing risks for property developers in 2024 [5].

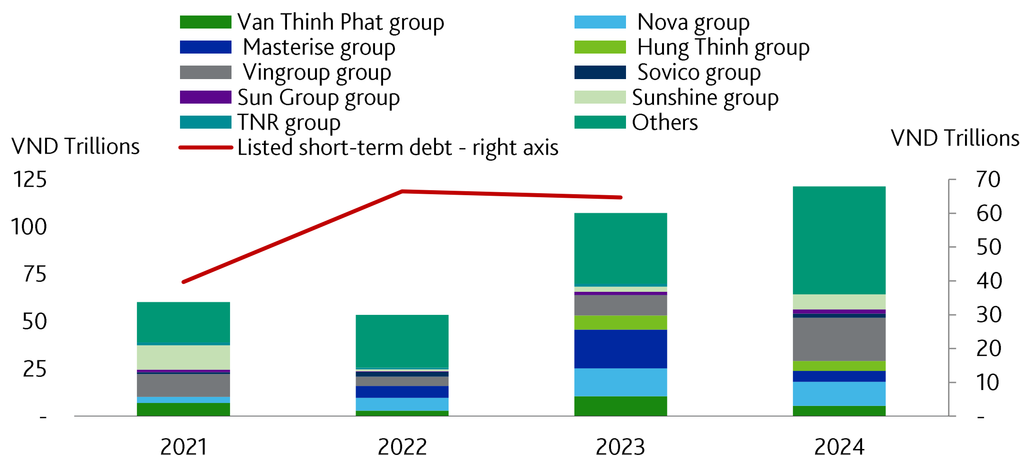
» Broadened access to new financing is critical for the sector to cope with refinancing risk

Privately-owned banks have been providing financing support for developers' projects and debt restructuring, leading to credit to real estate businesses expanding by 22% in 9M2023, offsetting weak mortgage growth (Exhibit 10).

Bonds newly issued by property sector companies also increased considerably by 237% YoY in Q3/2023, strongly bouncing back after experiencing negative growth since Q1/2022.

Developers will continue to seek new financing in 2024, especially when the prolonged property market downturn has limited pre-funding received from homebuyers. We expect the low interest rate environment, upcoming amendments in property-related law, and the government's efforts to resolve obstacles to project approval will facilitate access to new financing for developers in 2024.

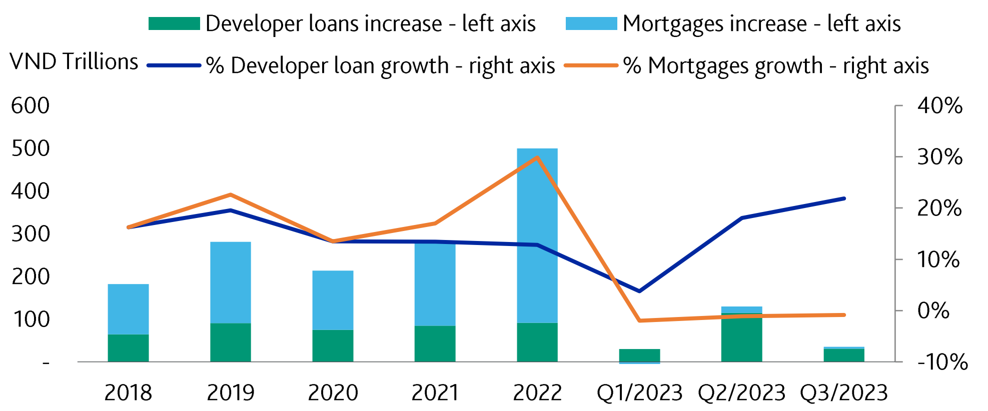
Exhibit 9: Bond maturities remain high in 2024



Note: Bond maturities related to groups are based on our estimation of bond maturities of companies that have linkages to corresponding groups. Listed short-term debt refers to short-term debt of listed developers

Source: Hanoi Stock Exchange (HNX), Vietnam Investors Service

Exhibit 10: Loans to developers increased to offset weak homebuyer's sentiment



Source: SBV, Vietnam Investors Service

[5] Refer to Property sector update: Poor market sentiment led to weak project sales and operating cash flow, access to new financing is key to cope with refinancing risks (20 Nov 2023)

Construction and materials sectors will benefit from public investment, while export-related sectors will continue to face headwinds by weak external demand

» Accelerating public investment and lower financing costs will support the recovery of the construction and materials sector

Based on the government's plan, public investment will increase by 15% in 2024. Therefore, we expect public investment disbursement to keep increasing by at least 10% in 2024, enhancing business conditions for construction and materials sectors, as indicated by growth in steel and cement consumption in Q3/2023 (Exhibit 11). Better business conditions will gradually improve the financial strength of companies in the sector.

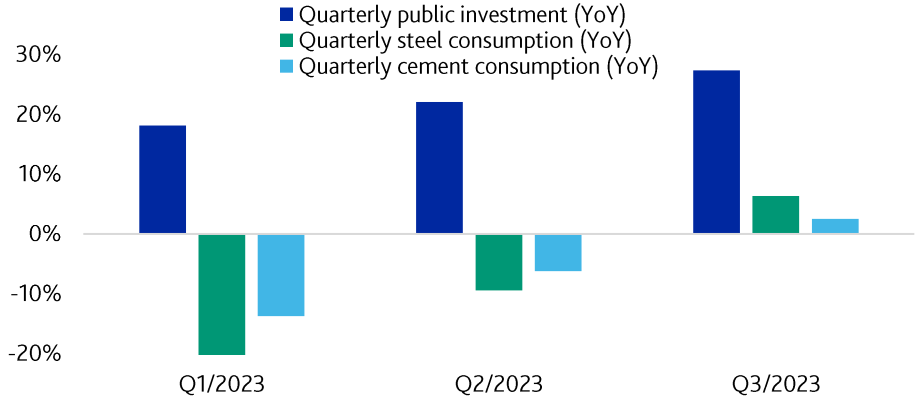
In general, companies in the construction and materials sector have high leverage with Debt/Equity of 2-3 times[6]. Alongside better business conditions, low financing costs will alleviate the sector's debt servicing burden and refinancing needs.

» Weak external demand will likely persist and dampen prospects for Vietnam's export-related sectors

Retail sales in Vietnam's key export markets including the U.S. and E.U remain weak, continuing to weigh on export-related sectors in 2024 (Exhibit 12). PMI indicators of these markets have also been consistently below 50, indicating a gloomy economic outlook and low demand prospect for Vietnam exporting products.

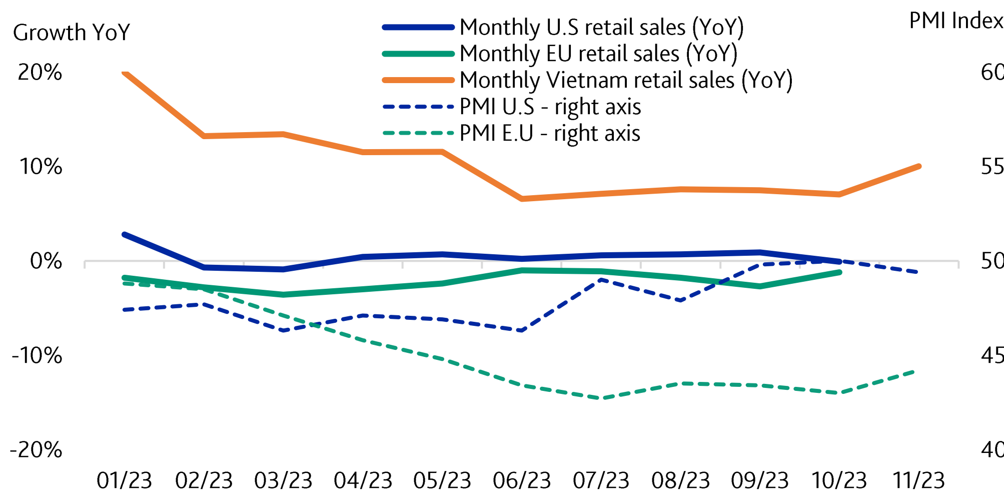
In contrast, the growth outlook for companies that focus on the domestic market is more positive as we expect consumer sentiment and spending to improve in 2024. For 2024, we expect annual retail sales to grow by 5-10%.

Exhibit 11: Strong public investment will support credit improvement of construction and materials sectors



Source: GSO, Vietnam Investors Service

Exhibit 12: Resilient domestic retail sales compared with sluggish in key exporting markets



Source: Trading Economics, GSO, Vietnam Investors Service

[6] As of Q3/2023 aggregated from listed companies

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Bank asset quality and profitability will gradually recover amid a stronger operating environment and low interest rates

» **NPL formation rate will slow down as borrowers' debt repayment capability improves amid stronger operating conditions and low interest rates environment**

We expect the sector's NPL formation rate to slow as borrowers' debt repayment capability improves amid stronger operating conditions and low interest rates (Exhibit 13). Most State-owned banks (SOBs) and ACB will lead the sector's recovery in asset quality, driven by their large, diversified corporate customer base and prudent lending practice[7].

Despite slower NPL formation rates, banks' sizeable exposure to sectors at risk such as property-related sector, and manufacturing (30% and 18% of total credit as of end-Jun 2023 respectively) continue to pose latent risks. Loan restructuring picked up since the introduction of Circular 02 in April 2023; restructured loans made up 1% of total banking sector loans as end-August 2023 and were not classified as NPLs.

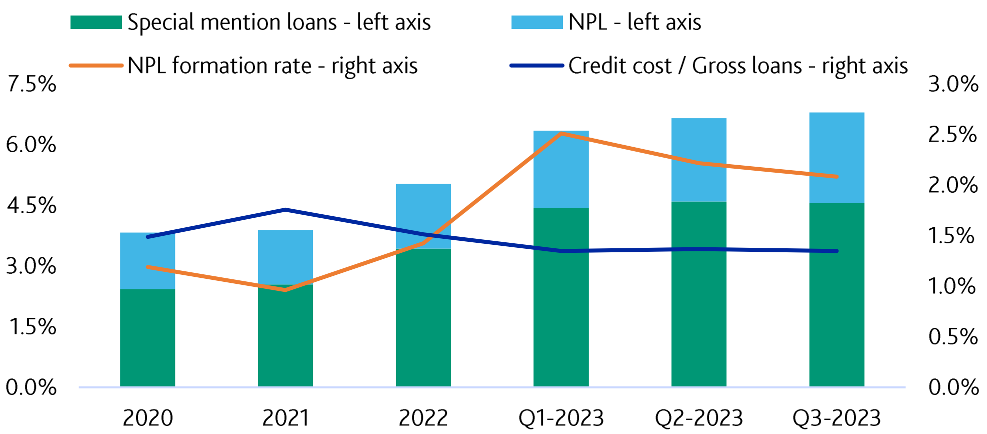
» **Profitability to gradually recover given a wider NIM and pickup credit demand amid the economic recovery**

We expect profitability to gradually recover in 2024 driven by a wider NIM with deposits adjusting quicker to lower rates than loans and credit demand picking up amid the economic recovery (Exhibit 14).

As high-cost deposits raised post-rate hikes in Q4/2022 mature and the growth in current account and savings account (CASA) deposits pick up amid low interest rate environment, banks' funding costs will adjust substantially to lower rates.

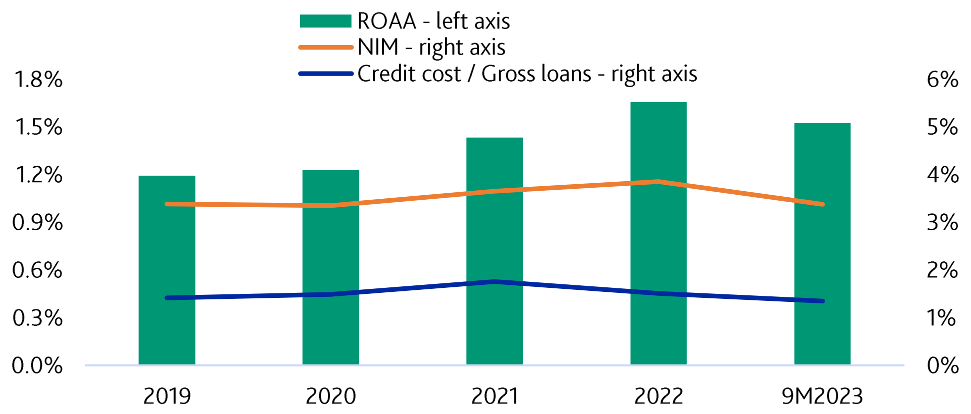
In addition, improving credit demand amid the economic recovery will enhance banks' lending yields.

Exhibit 13: NPL formation rate to slow down



Source: Company data, Vietnam Investors Service

Exhibit 14: ROAA will recover given wider NIM and pickup credit demand



Source: Company data, Vietnam Investors Service

[7] Refer to our Baking sector update: 9M2023 profits fell from the 2022 peak but recovery is within sight as net interest and margin pick up (13 Nov 2023)

» Loss absorption buffer will recover modestly as improved bank profits will help strengthen their capital

Improving profitability will moderately strengthen banks' capital and loss-absorption buffer against downside risks.

However, the sector's capital level will remain weak (Exhibit 15) with only a few meaningful capital raises by several privately owned banks (POBs). Meanwhile, other SOBs will take a longer time to obtain the necessary approvals, which drives up the issuance of subordinated bonds (tier 2 capital) to supplement their capital requirements.

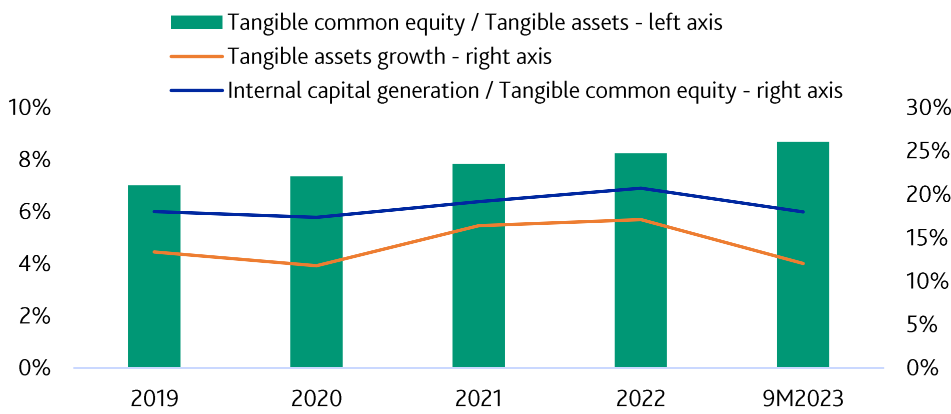
In addition, declining loan loss coverage given asset deterioration during 9M2023 results in a weak loss buffer, especially for small POBs. Loan loss reserve for POBs declined to a 5-year low (55% on average as of end-September 2023, much lower than the sector average of 93%).

» Liquidity will remain stable as deposit catches up with credit growth

We expect the liquidity position to be stable given stronger deposit growth to keep pace with the credit growth as corporate cash flow recovers alongside improved business conditions (Exhibit 16). The sector's loan-to-customer deposit ratio (LDR) held steady at 101% as of 9M2023.

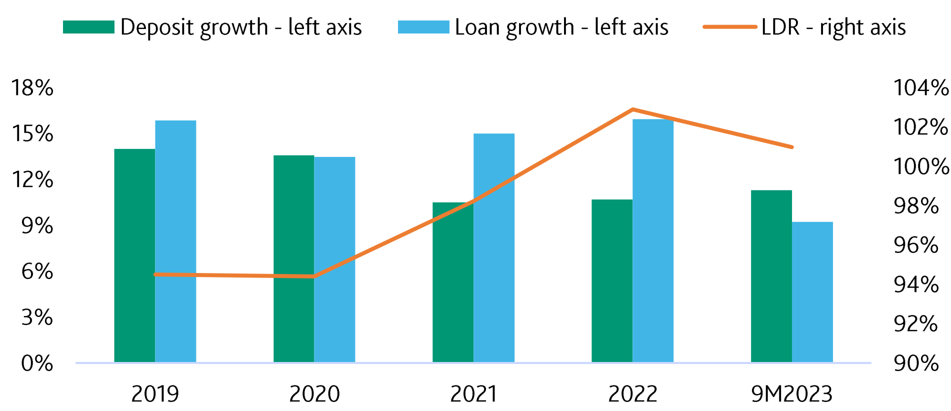
In addition, banks will increase their funding stability from long-term bond issuance to meet the stricter short-term funding to the medium and long-term lending ratio (SMLR) requirement. Given that the SMLR's regulatory limit decreased to 30% from October 2023, several private banks focusing on long-term lending are actively raising long-term bonds to meet pickup credit demand and comply with SMLR.

Exhibit 15: The sector's capital level will remain weak



Source: Company data, Vietnam Investors Service

Exhibit 16: Liquidity is improving as the higher deposit growth catches up with slow credit growth



Source: Company data, Vietnam Investors Service

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