VIETNAM INVESTORS SERVICE

SECTOR COMMENT

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Banking Sector

New Credit Institution Law will strengthen risk governance among banks and empower the regulator to act swiftly to maintain financial sector stability

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On 18 January 2024, the National Assembly passed the amended Law on Credit Institutions. The new law will serve to reduce banks' exposure to large borrowers and large shareholders. These new measures will help to enhance risk governance and business practices among banks and support their asset quality. In addition, the new law now includes detailed and clearer guidelines on the regulator's powers to intervene and address issues swiftly and effectively in ailing banks, for example, those facing deposit runs. These guidelines provide greater clarity and certainty over the regulatory actions that can be taken to resolve weak banks and maintain stability of the financial sector.

Lower credit concentration and stricter shareholder ownership and stricter disclosure requirements reflect the regulator's intent to enhance bank risk governance and business practices. Under the new law, credit exposure to single borrowers and their related parties – based on the new and expanded definition of related parties – are limited to 10-15% of total capital, down from 15-25% previously. Local institutional shareholders and their related parties may only hold up to 10-15% in equity stake, down from 15-20% previously. These stricter measures will serve to limit the linkages between banks and large corporate groups that often go beyond the regulatory limits, and urge banks to strengthen internal risk governance and lending practices.

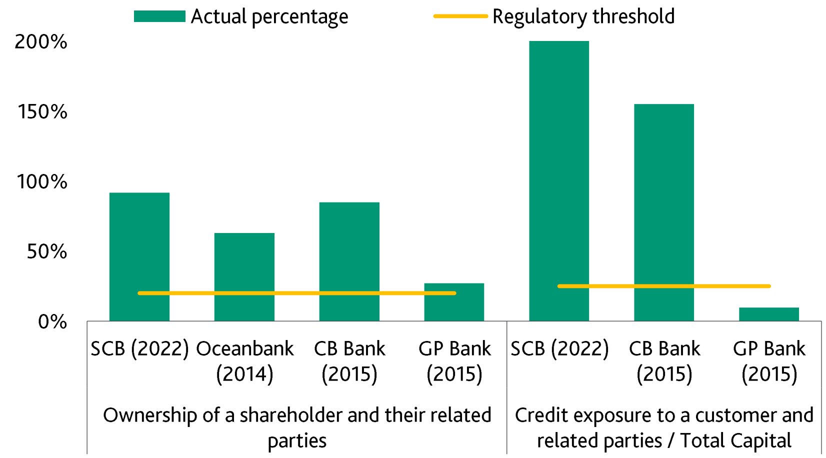
Clearer and detailed guidelines on the regulator's powers to resolve ailing banks are positive to facilitate swift and timely intervention by the regulator to address issues in weak banks and maintain financial sector stability. The new guidelines include specific criteria related to a bank's solvency and liquidity position that will warrant early intervention by the regulator. In addition, the guidelines provide more clarity on the regulator's powers to resolve banks that are placed under special control.

The new law provides banks with a proper legal framework to support future debt recovery efforts. The new law incorporates many of the new mechanisms used by banks to manage bad debt and improve recoveries in recent years, including the buying and selling of bad debts and collaterals, implemented under Resolution 42 that expired in December 2023. On a negative note, banks will not have the legal rights to seize collateral under the new law and debt recovery through the court process will take a longer time.

Lower credit concentration and stricter shareholder ownership and stricter disclosure requirements reflect the regulator's intent to enhance bank risk governance and business practices.

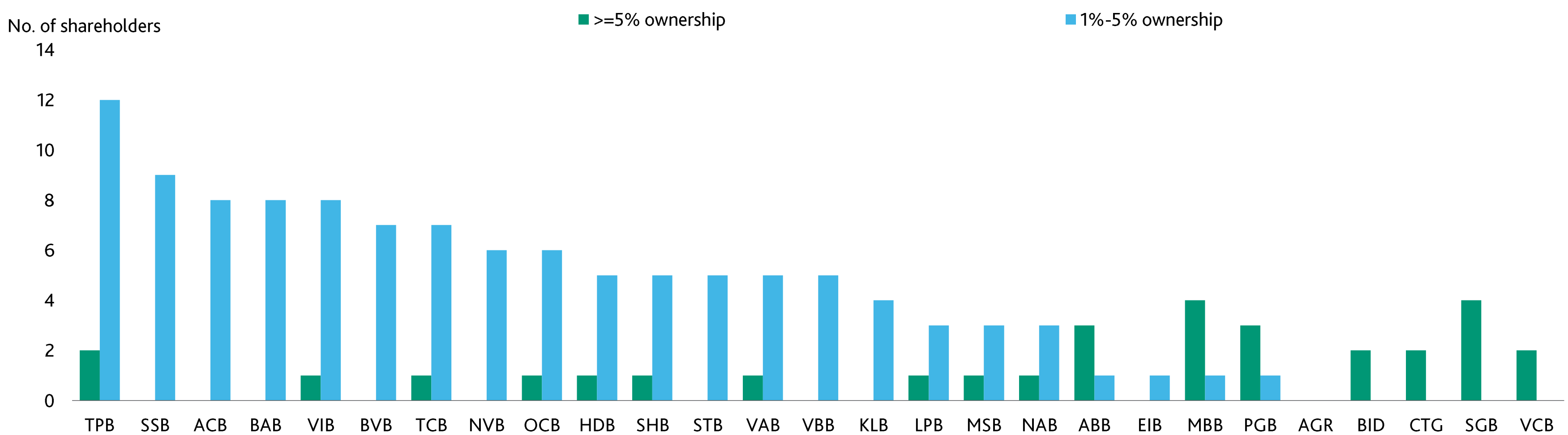
Recent incidents of banks that faced financial troubles reflect the linkages between banks and large corporate groups that often go beyond the regulatory limits (Exhibit 1). Under the new law, credit exposure to single borrowers and their related parties – based on the new and expanded definition of related parties – are limited to 10-15% of total capital, down from 15-25% previously. Local institutional shareholders and their related parties may only hold up to 10-15% in equity stake, down from 15-20% previously. Moreover, shareholders owning from 1% charter capital are required to disclose information, down from 5% previously (Exhibit 2). These stricter measures will serve to limit the linkages between banks and large corporate groups similar to the cases in the past and urge credit institutions to strengthen internal risk governance and lending practices (Exhibit 3).

Exhibit 1: Some troubled banks' exposure to large borrowers and large shareholders were much higher than regulatory thresholds



Source: People's Procuratorate of the Supreme, Vietnam Investors Service
Note: SCB's credit exposure to a customer and related parties/Total Capital is 3218%

Exhibit 2: Bank shareholders with 1% or more ownership are now required to disclose ownership information, compared with 5% or more previously



Source: Widata, Vietnam Investors Service

Exhibit 3: Stricter requirements on credit concentration, shareholder ownership and disclosure

Content	Prior to New Law	Key changes in New Law	Implications
Definition of related parties	➢ For individuals: including spouses, parents, children, brothers, and sisters ➢ For organizations: including subsidiaries of the organization	➢ For individuals: extending to more family members including spouse family (all in-laws), grandparents, uncles, aunts, nephews, nieces, adoptive parents and children, stepchildren, half-brothers/sisters ➢ For organizations: including subsidiaries of the subsidiaries of the organization	Lower exposure to large shareholders by a broader definition of related parties
Shareholder disclosure requirement	➢ Relevant law from 5% equity stake	➢ From 1% equity stake	Enhance transparency
Domestic ownership limits	➢ 15% for an institutional shareholder ➢ 20% for a shareholder and related parties	➢ 10% for an institutional shareholder ➢ 15% for a shareholder and related parties	Limit the linkage between banks and large related corporate groups
Credit exposure limits	➢ 15% for a single borrower ➢ 25% for a single borrower and related parties	➢ 10% for a single borrower ➢ 15% for a single borrower and related parties	

Source: Law on Credit Institutions 2024, Vietnam Investors Service

Clearer and detailed guidelines on the regulator's powers to resolve ailing banks are positive to facilitate swift and timely intervention by the regulator to address issues in weak banks and maintain financial sector stability.

The new guidelines include specific criteria related to a bank's solvency and liquidity position that will warrant early intervention by the regulator (Exhibit 4). In addition, the guidelines provide more clarity on the regulator's powers to resolve banks that are placed under special control.

Exhibit 4: Clearer and detailed guidelines on the regulator's powers to address issues in weak banks through early intervention and special control

Key content	Prior to New Law	Key changes in New Law	Implications
Criteria to trigger early intervention/special control	➢ No mention of deposit run and accumulated loss	➢ Add deposit run and risk to financial stability ➢ For early intervention: (i) add 15% accumulated loss to charter capital and reserve funds and failure for CAR, and (ii) tighten existing criteria such as 30 consecutive days of failure to maintain solvency ratio, down from 3 consecutive months	Allows the SBV to intervene earlier to support weak banks and maintain financial stability
Guidelines on regulator's power to resolve credit institutions			
1. Requirements for banks under early intervention	➢ No mention	➢ Specific requirements on enhancing capital, high liquid assets, cost management, risk management, and corporate governance ➢ Restrictions to dividends, share transferring, risky business activities, credit growth, and prudential limits	Clearer guidelines on the SBV's power allow swifter actions
2. Remedial plan	➢ General guidance to the SBV and weak banks	➢ Add detailed stipulation on the role of banks in proposing the plan and the SBV in reviewing and supervising	
3. Special loans	➢ General guidance to the SBV	➢ Detailed authorization to the SBV and the Government based on impact, interest rate and collaterals	
4. Supporting measures for weak banks	➢ No mention	➢ Allow a roadmap to comply with prudential ratios ➢ Allow banks to exceed ownership limit during remedial plan ➢ Lower provisioning if accumulated loss >50% chattered capital with disclosure ➢ Extend timeline for releasing accrued interest up to 5 years if approved by the SBV, and up to 10 years if approved by the Government	More SBV's measures to support weak banks
5. Supporting measures for banks participating in mandatory transferring	➢ Less regulatory forbearance to supporting banks	Add: ➢ Regulatory forbearance on prudential ratios (e.g. -50% reserve ratio) and excluding credit exposure to weak banks in calculating prudential ratios ➢ Liquidity support from SBV refinancing, long-term bond issuance to deposit insurance ➢ Clearer legal framework in supporting transferred banks	Allow extra regulatory forbearance for the SBV to apply to supporting banks

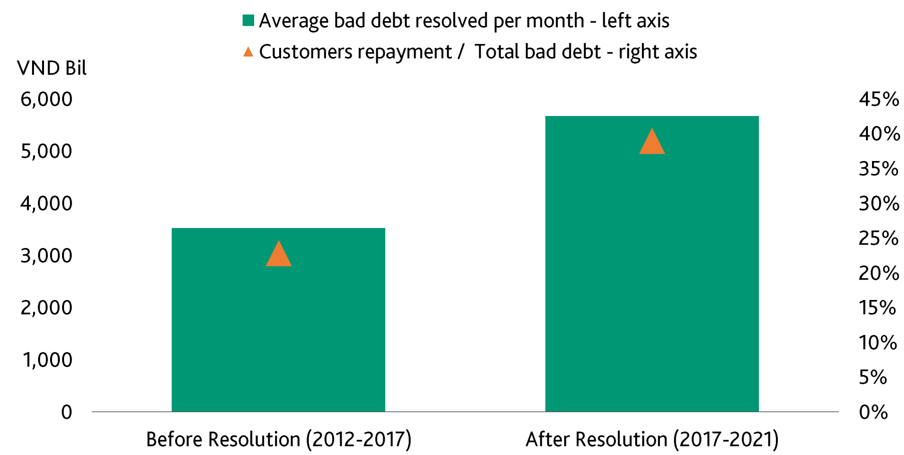
Source: Law on Credit Institutions 2024, Vietnam Investors Service

The new law provides banks with a proper legal framework to support future debt recovery efforts.

The new law incorporates many of the new mechanisms used by banks to manage bad debt and improve recoveries in recent years, including the buying and selling of bad debts and collaterals, implemented under Resolution 42 that expired in December 2023 (Exhibit 5).

On a negative note, debt collection may take a longer time as banks will not have the legal right to seize collateral under the new law and have to rely on the borrowers' collaboration and the court decision.

Exhibit 5: Banks improved recoveries in bad debt through Resolution 42 framework introduced in 2017



Source: Ministry of Jurisdiction, Vietnam Investors Service

APPENDIX

List of banks

The banks included in our analysis are as follows (in order of A-Z):

	Short name	Full name	Classification
1	ABB	An Binh Commercial Joint Stock Bank	Small
2	ACB	Asia Commercial Joint-Stock Bank	Large
3	AGR	Vietnam Bank For Agriculture And Rural Development	SOCB
4	BAB	Bac A Commercial Joint Stock Bank	Small
5	BID	Joint Stock Commercial Bank for Investment and Development of Vietnam	SOCB
6	BVB	Viet Capital Commercial Joint Stock Bank	Small
7	CTG	Vietnam Joint-Stock Commercial Bank for Industry and Trade	SOCB
8	EIB	Vietnam Commercial Joint Stock Export Import Bank	Mid-sized
9	HDB	Ho Chi Minh City Development Joint Stock Commercial Bank	Mid-sized
10	KLB	Kien Long Commercial Joint Stock Bank	Small
11	LPB	Lien Viet Post Joint Stock Commercial Bank	Mid-sized
12	MBB	Military Commercial Joint Stock Bank	Large
13	MSB	Vietnam Maritime Commercial Joint Stock Bank	Mid-sized
14	NAB	Nam A Commercial Joint Stock Bank	Mid-sized
15	NVB	National Citizen Commercial Joint Stock Bank	Small
16	OCB	Orient Commercial Joint Stock Bank	Mid-sized
17	PGB	Petrolimex Group Commercial Joint Stock Bank	Small
18	SGB	Saigon Bank for Industry and Trade	Small
19	SHB	Saigon - Hanoi Commercial Joint Stock Bank	Large
20	SSB	Southeast Asia Commercial Joint Stock Bank	Mid-sized
21	STB	Saigon Thuong Tin Commercial Joint Stock Bank	Large
22	TCB	Vietnam Technological and Commercial Joint-Stock Bank	Large
23	TPB	Tien Phong Commercial Joint Stock Bank	Mid-sized
24	VAB	Vietnam Asia Commercial Joint Stock Bank	Small
25	VBB	Vietnam Thuong Tin Joint Stock Commercial Bank	Small
26	VCB	Joint Stock Commercial Bank for Foreign Trade of Vietnam	SOCB
27	VIB	Vietnam International Commercial Joint Stock Bank	Mid-sized
28	VPB	Vietnam Prosperity Joint Stock Commercial Bank	Large

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This publication does not announce a credit rating action.