VIETNAM INVESTORS SERVICE

SECTOR OUTLOOK

19 MARCH 2024

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Banking Sector

Outlook improving as stronger operating conditions and low interest rates lower asset risks and boost profitability

After enduring a year of economic slowdown and rise in non-performing loans (NPL) in 2023, we expect bank profitability to strengthen in 2024 as stronger domestic operating conditions and low interest rates drive improvements in borrower debt serviceability and asset quality. The sector's return on average assets (ROAA) will improve from wider net interest margins (NIM) and stronger loan growth and support capital generation. In addition, funding and liquid resources will remain steady as deposit growth keeps pace with credit growth and banks increase longer-term funding.

NPL formation rate will slow as borrower debt repayment capability improves amid stronger domestic operating conditions and low interest rates. Various government policies and regulation changes to boost investment and domestic consumption will come into effect and help drive business activity and stronger operating cash flows for domestic businesses. Low interest rates will alleviate the repayment burden and improve debt serviceability for retail and SMEs borrowers. We expect the sector-average non-performing loan (NPL) ratio will decline to 1.7%-1.8% in 2024 from a 5-year high of 1.9% in 2023. The pace of loan restructuring (~1.2% of total loans) will stabilize. Asset risk from real estate exposures will continue to stabilize as developers obtain the necessary legal approvals to commence project development and gain access to financing. Nonetheless, high leverage and slow recovery in cash flows for developers embroiled in legal issues and/or speculative projects will continue to be a key risk to bank asset quality.

Profitability will improve from wider NIM and stronger loan growth. In 2024, we expect sector average ROAA will increase marginally to 1.7% in 2024 from 1.6% in 2023 as NIMs widen by 20-30 basis points from the prior year to around 3.8%. Most banks will be able to re-price deposits at lower rates quicker than loans. Loan growth will increase to 14-15%, driven by credit demand from domestic trade, manufacturing, and real estate developers. Non-interest income growth will be modest, driven mainly by settlement services, offsetting weak sentiment in bancassurance products and lower investment income. Credit costs will remain high as banks replenish their provision coverage from trough levels in 2023, especially mid-sized and small banks.

Loss absorption buffer will remain stable as internal capital generation improves to support business growth. Even as profits improve to support provisioning and replenish capital, we expect bank capital levels to remain broadly flat in 2024. Only a few banks have announced capital-raising plans. Overall, the banking sector's capital adequacy ratio will remain weak at around 11-12%. Provisioning coverage for mid-sized and small banks will remain lower than sector average as they will take longer to raise provisioning levels following severe asset quality deterioration in 2023.

Funding and liquid resources will remain stable as deposit growth keeps pace with credit growth and banks increase longer-term funding. We expect banks' deposit growth will be supported by stronger corporates' cash flows alongside improved business conditions. Moreover, banks will actively seek new long-term bond funding to maintain short-term funding to medium and long-term loan ratios (SMLR) below the 30% threshold.

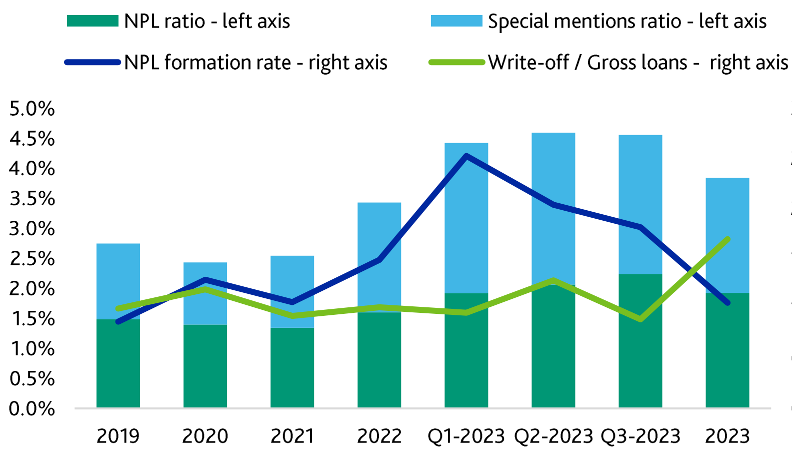
Exhibit 1: Banking Sector - Credit Outlook Improving for 2024 and Key Drivers

Factors	Outlook	Key drivers
Operating Environment	Improving	• Low-interest rate environment drives lower financing costs for businesses • Improving operating cash flows for domestic businesses from stronger investment and domestic consumption following the implementation of various government policies such as VAT cut, income tax deferral, and public investment disbursement • Gradual improvement in housing demand and supply driven by accelerating project approvals, new real estate legal framework, and low lending rate
Asset Quality	Improving	• Lower NPL ratio (1.7%-1.8%, down from 5-year high of 1.9% in 2023) and slower pace of loan restructuring (1.2% of total loans in October 2023) • Improving debt serviceability from stronger operating cash flows for domestic business, and lower repayment burden for retail and SMEs borrowers due to low interest rates • Stabilized asset risk from real estate exposures given developers' improved legal approvals and financing access, but high leverage and slow recovery in cash flows for developers embroiled in legal issues and/or speculative projects will continue to be a key risk
Profitability	Improving	• ROAA will increase marginally to 1.7% in 2024 from 1.6% in 2023 • NIM will expand by 20-30 basis points to around 3.8% as banks re-price deposits to lower rates quicker than loans, and stronger loan growth of 14%-15% driven by credit demand from domestic trade, manufacturing, and real estate developers • Non-interest income growth will be modest, driven mainly by settlement services, offsetting weak sentiment in bancassurance products and lower investment income • Credit costs will remain high as banks replenish their provision coverage from trough level in 2023, especially for mid-sized and small banks
Loss Absorption Buffer	Stable	• Profits improve to support the provisioning and replenish capital required for business growth • Only few banks have announced capital-raising plans • Overall, the banking sector's capital adequacy ratio will remain weak at around 11-12%
Funding & Liquid Resources	Stable	• Banks' deposit growth will be supported by stronger corporates' cash flows alongside improved business conditions • Banks will actively seek long-term bond funding to maintain SMLR below the 30% threshold

Source: Vietnam Investors Service

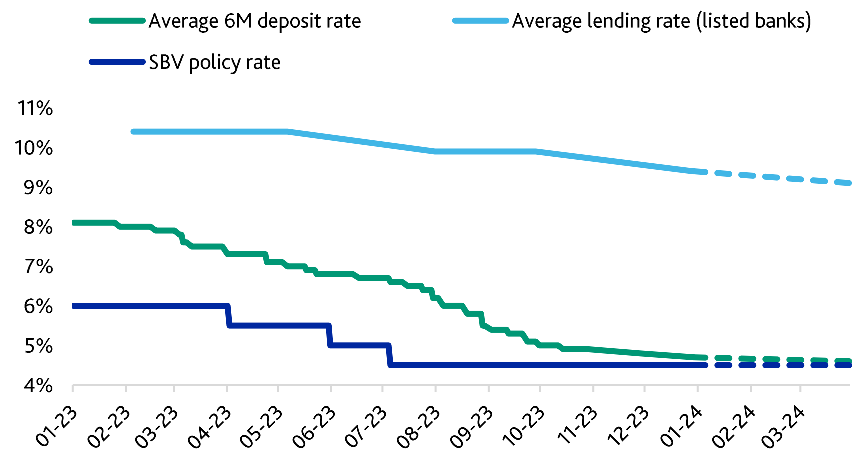
NPL formation rate will slow as borrower debt repayment capability improves amid stronger domestic operating conditions and low-interest rates

Exhibit 1: We expect NPL ratio will decline in 2024 given the improvement in customers' debt serviceability



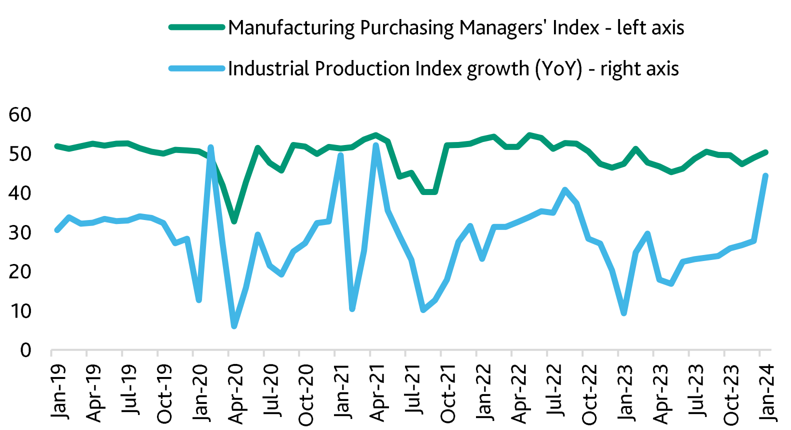
Source: Bank data, Vietnam Investors Service
Note: Sector numbers include 27 listed banks

Exhibit 2: The declining lending rate will support borrowers' debt serviceability, especially for highly leveraged retail and SMEs



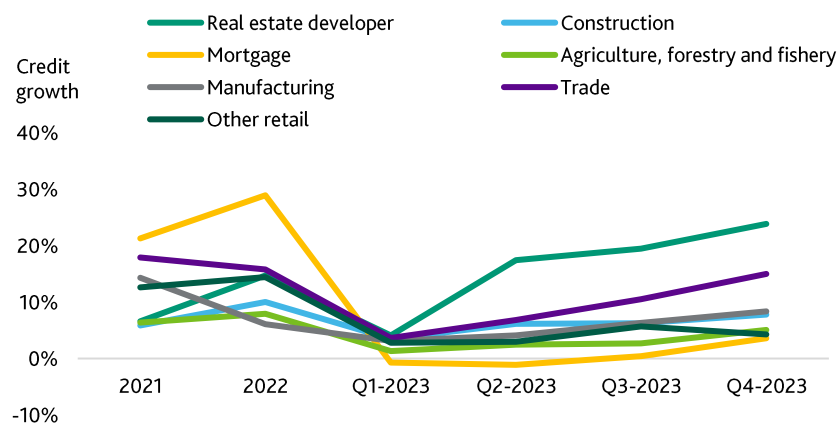
Source: Bank data, Vietnam Investors Service
Note: The average lending rate is annualized, calculated by dividing total interest income from loans by total loans across listed banks.

Exhibit 3: Various government policies and regulation changes will drive business activity and stronger operating cash flows for domestic businesses



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

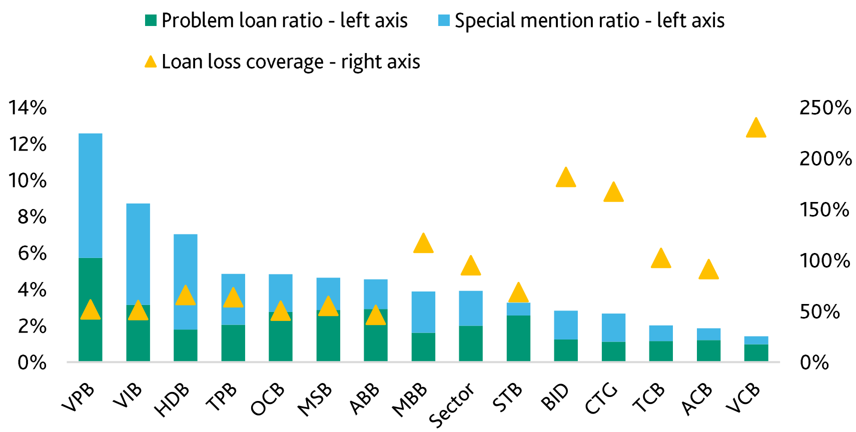
Exhibit 4: Corporate businesses will drive credit growth while retail mortgages will gradually pick up



Source: Ministry of Construction, State Bank of Vietnam (SBV), Vietnam Investors Service
Note: The 2023 credit growth were year-to-date (YTD) data

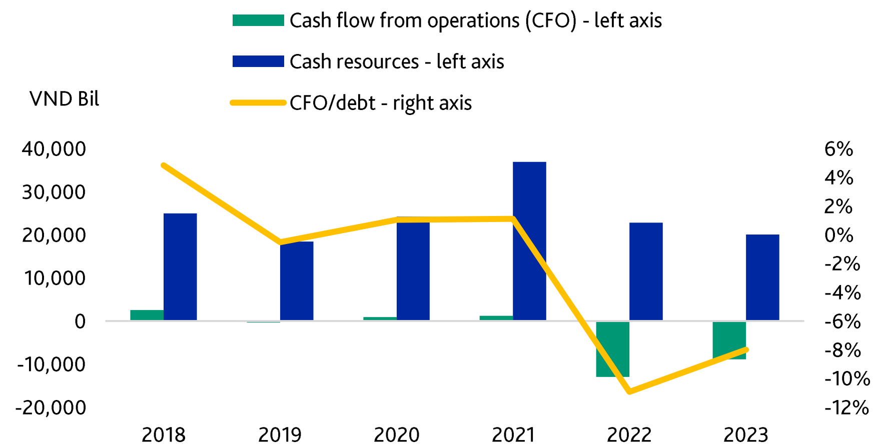
Asset risk from real estate exposures will stabilize given developers' improved legal approvals and financing access, while weak developers embroiled in legal issues and/or speculative projects will continue to be a key risk to some banks' asset quality

Exhibit 5: State-owned banks (SOBs) and ACB showed stronger asset quality resilience than industry peers



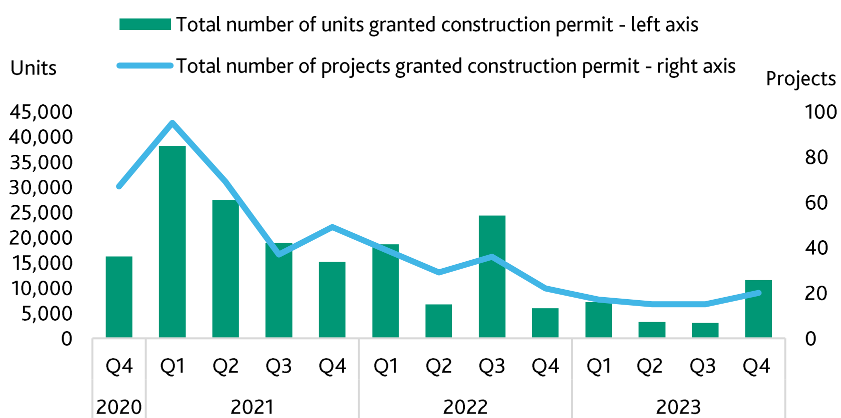
Source: Bank data, Vietnam Investors Service
Note: Problem loans consist of non-performing loans and VAMC bonds

Exhibit 6: Cash flows of real estate developers remained at a weak level



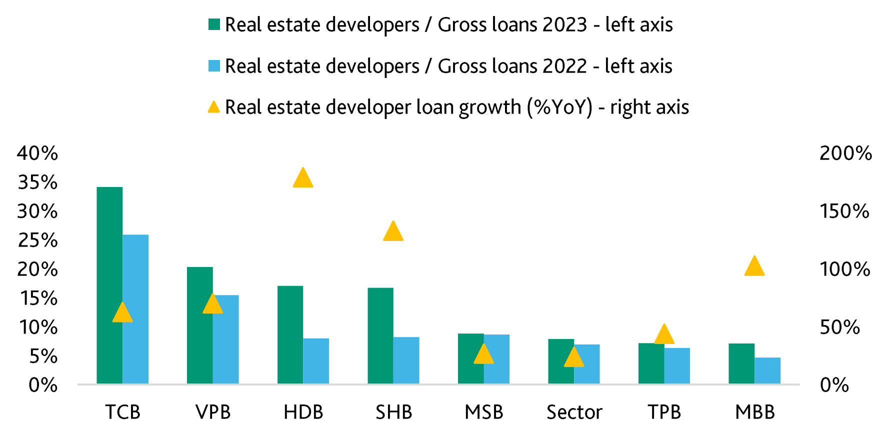
Source: Company data, Vietnam Investors Service
Note: Vinhomes is excluded from the calculation as it is not representative of sector performance
Sector data was based on the top 30 residential property companies by revenue

Exhibit 7: Projects obtaining construction permits increased in Q4-2023



Source: Ministry of Construction, Vietnam Investors Service

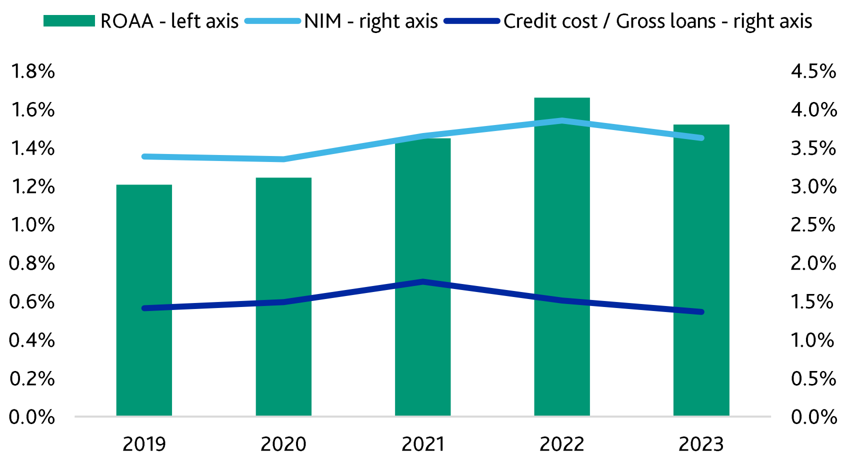
Exhibit 8: Several POBs increased their loan exposure to real estate developers



Source: Bank data, Vietnam Investors Service

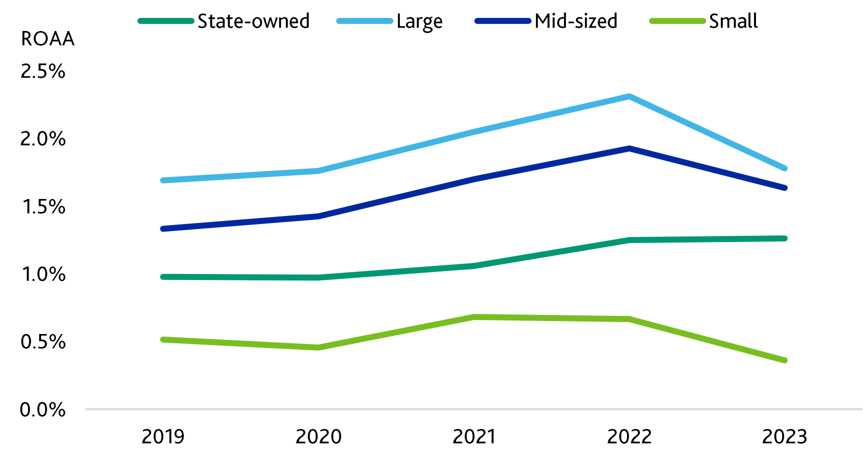
Profitability will improve from wider NIM, and stronger loan growth

Exhibit 9: Sector's ROAA will improve driven by wider NIM and stronger loan growth



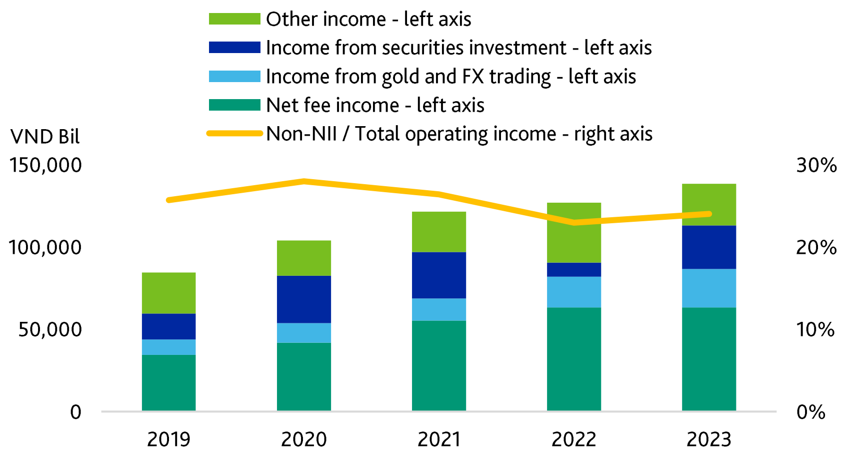
Source: Bank data, Vietnam Investors Service
Note: Sector numbers include 27 listed banks

Exhibit 10: SOBs will maintain more stable profitability due to resilient NIM and lower credit cost pressure



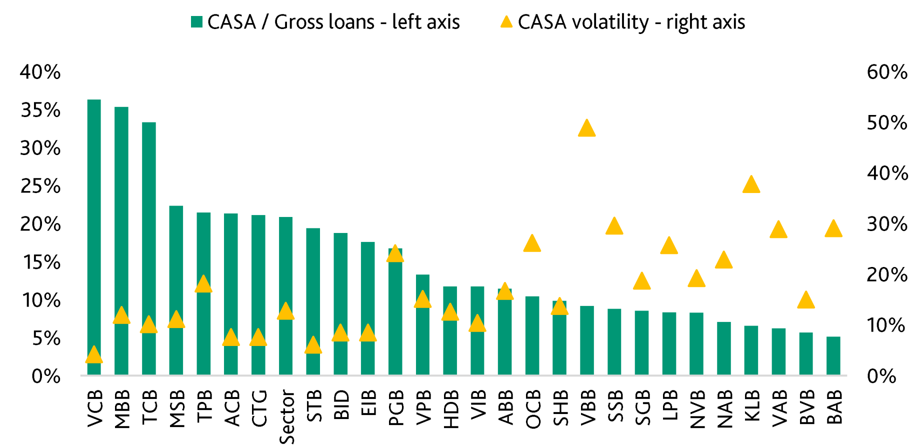
Source: Bank data, Vietnam Investors Service
Note: Refer to the Appendix for the full name of banks

Exhibit 11: Non-interest income is expected to improve slightly, mainly driven by settlement income



Source: Bank data, Vietnam Investors Service
Note: Sector numbers include 27 listed banks

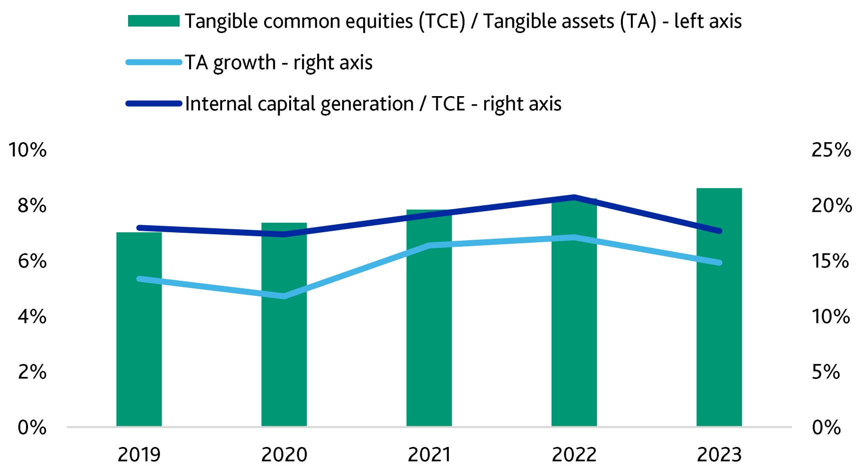
Exhibit 12: SOBs and several large POBs with strong CASA base and low volatility will experience stronger improvements in funding costs



Source: Bank data, Vietnam Investors Service
Note: Refer to the Appendix for the full name of banks
CASA volatility reflects the standard deviation of quarterly changes in CASA balance over 5 years

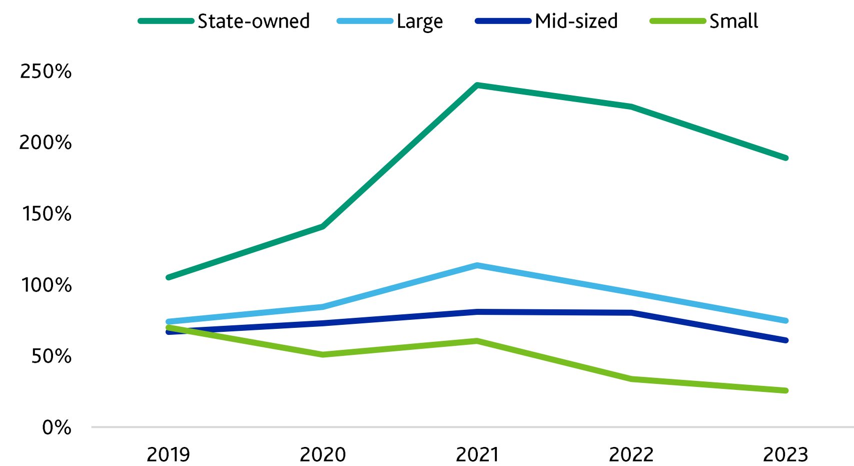
The loss absorption buffer will remain stable as internal capital generation improves to support business growth

Exhibit 13: The banking sector's capital level is expected to improve modestly driven by internal capital generation recovery



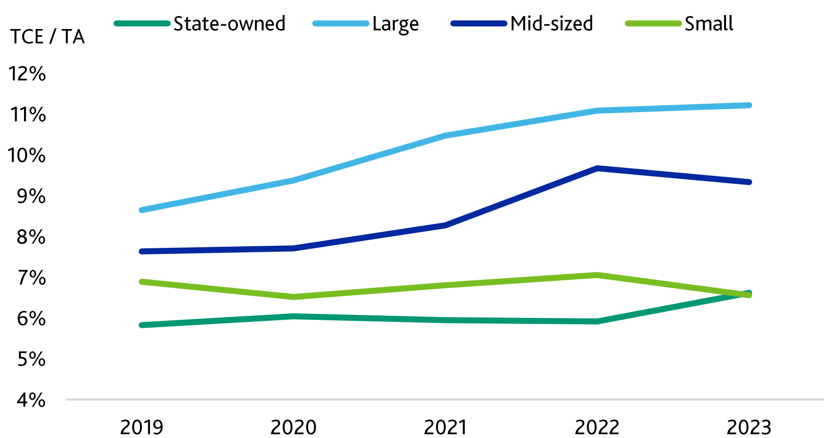
Source: Bank data, Vietnam Investors Service
Note: Sector numbers include 27 listed banks

Exhibit 14: SOBs' coverage will drive the sector's recovery while small and mid-sized POBs will take more time to recover from 2023's trough level



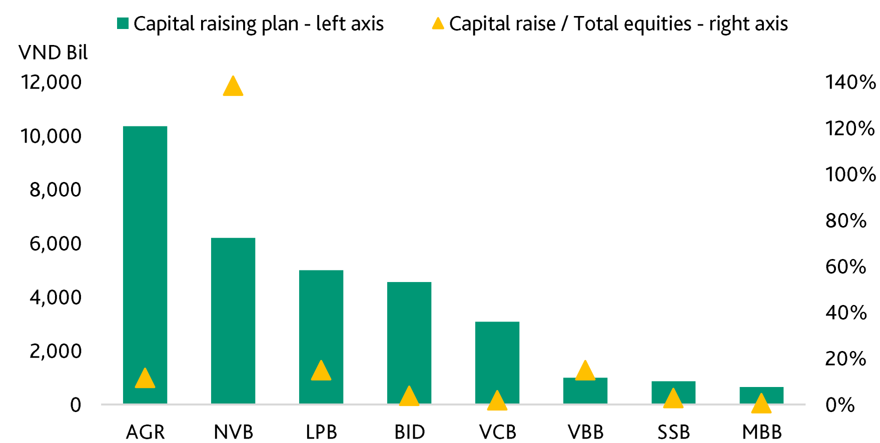
Source: Bank data, Vietnam Investors Service
Note: Refer to the Appendix for the full name of banks

Exhibit 15: SOBs' capital level will improve at a faster pace given a more stable income compared to small POBs



Source: Bank data, Vietnam Investors Service
Note: Refer to the Appendix for the full name of banks

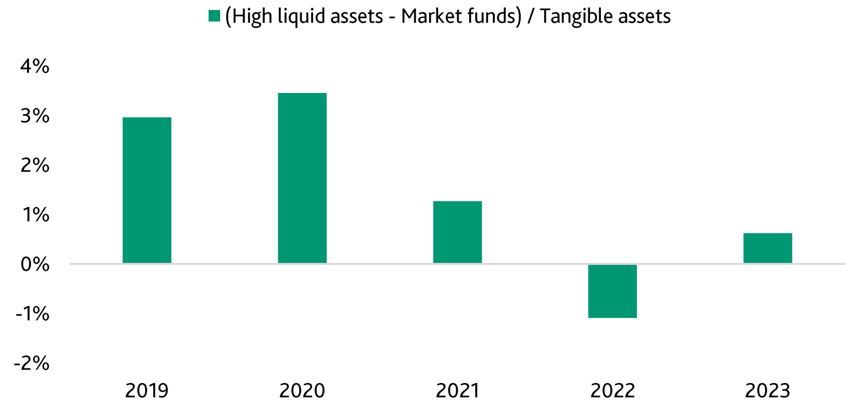
Exhibit 16: Only a few banks announced plans to raise new capital in 2024



Source: Bank data, Vietnam Investors Service
Note: AGR refer to Vietnam Bank for Agriculture and Rural Development; full names of other listed banks refer to the Appendix

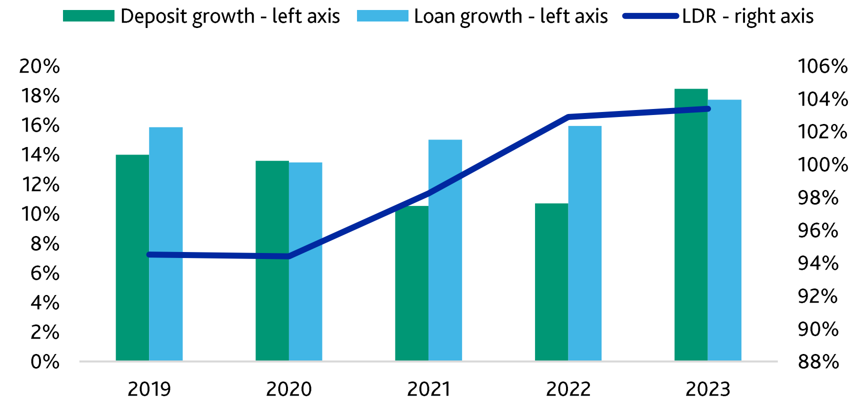
Funding and liquid resources will remain stable as deposit growth keeps pace with credit growth and banks increase longer-term funding

Exhibit 17: The banking sector's liquidity improved from the trough in 2022



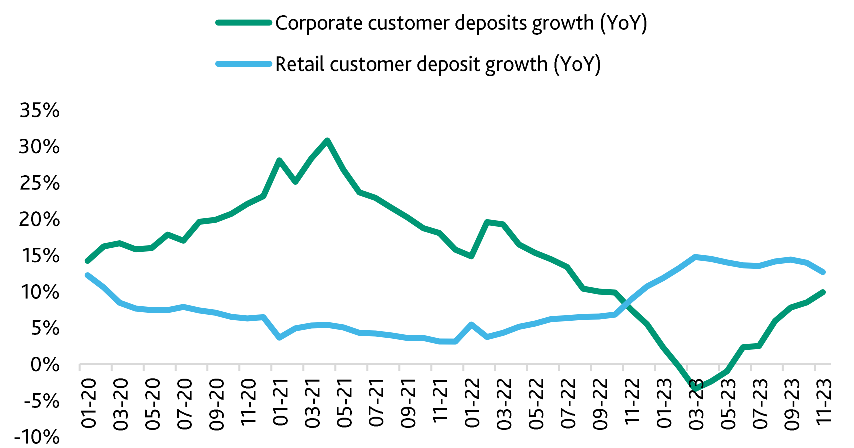
Source: Bank data, Vietnam Investors Service
Note: High liquid assets consist of cash, balance at the SBV, interbank deposit and lending, and government bonds. Market funds consist of the State Treasury's deposits, deposits and borrowings from other credit institutions, grants and trusted funds, and valuable papers issued.

Exhibit 18: Loan to deposit ratio (LDR) will stabilize driven by corporate deposit recovery aligning with the credit demand pick-up



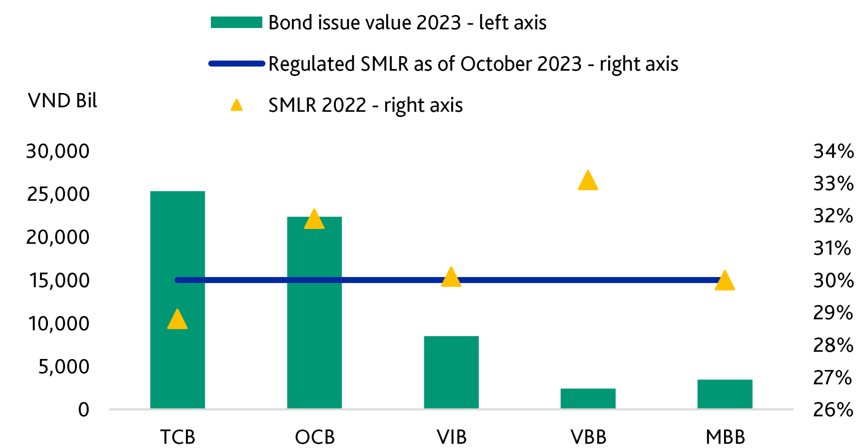
Source: Bank data, Vietnam Investors Service
Note: Sector numbers include 27 listed banks

Exhibit 19: Banks' deposits will be supported by stronger corporates' cash flows alongside improved business conditions



Source: State Bank of Vietnam (SBV), Vietnam Investors Service

Exhibit 20: Banks will long-term funding to maintain SMLR below the regulated threshold



Source: Hanoi Stock Exchange (HNX), Bank data, Vietnam Investors Service
Note: Refer to the Appendix for the full name of banks

APPENDIX

List of 27 listed banks

The banks included in our analysis are as follows:

Nº	Short name	Full name	Classification
1	ABB	An Binh Commercial Joint Stock Bank	Small
2	ACB	Asia Commercial Joint-Stock Bank	Large
3	BAB	Bac A Commercial Joint Stock Bank	Small
4	BID	Joint Stock Commercial Bank for Investment and Development of Vietnam	State-owned
5	BVB	Viet Capital Commercial Joint Stock Bank	Small
6	CTG	Vietnam Joint-Stock Commercial Bank for Industry and Trade	State-owned
7	EIB	Vietnam Export Import Commercial Joint Stock Bank	Mid-sized
8	HDB	Ho Chi Minh City Development Joint Stock Commercial Bank	Mid-sized
9	KLB	Kien Long Commercial Joint Stock Bank	Small
10	LPB	Lien Viet Post Joint Stock Commercial Bank	Mid-sized
11	MBB	Military Commercial Joint Stock Bank	Large
12	MSB	Vietnam Maritime Commercial Joint Stock Bank	Mid-sized
13	NAB	Nam A Commercial Joint Stock Bank	Mid-sized
14	NVB	National Citizen Commercial Joint Stock Bank	Small
15	OCB	Orient Commercial Joint Stock Bank	Mid-sized
16	PGB	Petrolimex Group Commercial Joint Stock Bank	Small
17	SGB	Saigon Bank for Industry and Trade	Small
18	SHB	Saigon - Hanoi Commercial Joint Stock Bank	Large
19	SSB	Southeast Asia Commercial Joint Stock Bank	Mid-sized
20	STB	Saigon Thuong Tin Commercial Joint Stock Bank	Large
21	TCB	Vietnam Technological and Commercial Joint-Stock Bank	Large
22	TPB	Tien Phong Commercial Joint Stock Bank	Mid-sized
23	VAB	Vietnam Asia Commercial Joint Stock Bank	Small
24	VBB	Vietnam Thuong Tin Joint Stock Commercial Bank	Small
25	VCB	Joint Stock Commercial Bank for Foreign Trade of Vietnam	State-owned
26	VIB	Vietnam International Commercial Joint Stock Bank	Mid-sized
27	VPB	Vietnam Prosperity Joint Stock Commercial Bank	Large