Vietnam
Special Report

Vietnamese Banks

Concerns Persist Following H110 Performance

Ratings

Vietnamese banks rated by Fitch:
Vietnam Bank for Agriculture and Rural Development

Individual Rating	E
Support Rating	4

Bank for Investment and Development of Vietnam

Individual Rating	D/E
Support Rating	4

Joint Stock Commercial Bank For Foreign Trade of Vietnam

Individual Rating	D/E
Support Rating	4

Vietnam Joint-Stock Commercial Bank for Industry and Trade

Individual Rating	D/E
Support Rating	4

Asia Commercial Bank (Vietnam)

Individual Rating	D/E
Support Rating	5

Saigon Thuong Tin Commercial Joint Stock Bank

Individual Rating	D
Support Rating	5

Analysts

Mic Kang
+852 2263 9924
mic.kang@fitchratings.com

Jonathan Cornish
+852 2263 9901
jonathan.cornish@fitchratings.com

Related Research

Applicable Criteria

- *Global Financial Institutions Rating Criteria (August 2010)*

Other Research

- *Outlook on Vietnamese Banks (March 2010)*
- *Banks in Asia (Excluding Japan): Outlook for 2010 (2 February 2010)*
- *Vietnamese Banks — Focus on Asset Quality: Three Stress Scenarios (February 2009)*

Executive Summary

Greater optimism surrounded the Vietnamese economy and banking sector in H110, despite the operating environment remaining inherently volatile. Nevertheless, Fitch Ratings is concerned about the sustainability of the domestic banking sector, particularly regarding banks' potentially vulnerable asset quality, limited capitalisation and weakened liquidity position. This is because all the banks are being tested by what the agency considers excessively strong credit growth, which the government is encouraging as a means of facilitating Vietnam's economic growth.

New prudential regulations are due to become effective from 1 October 2010, whereby all banks are supposed to maintain a minimum total capital adequacy ratio (CAR) of 9% and minimum capital of VND3.0trn (around USD160m), and not to lend more than 80% of sum of their deposits and some wholesale funding. Worryingly, Fitch estimates that several of the major banks are either not yet in compliance with the first condition or in danger of breaching it should they continue to extend credit at current rates without raising additional external capital — amounts and timing of which are in many cases uncertain. Many of the country's smaller banks are unlikely to be compliant with either condition. Also, Fitch is of view that some banks face difficulty meeting the new regulatory loans/deposits (LTD) ratio by the cut-off date, as the average regulatory LTD ratio[1] of the rated banks was estimated at above 95% at mid-2010. As such, Fitch doesn't rule out the possibility of either regulatory forbearance on the new prudential regulations for a certain period of time, or refinements which make it easier for the banks to comply.

Although the government is to implement stricter regulations to improve the system's credit profile, it has strongly encouraged the banking sector to expand credit by up to 25% in 2010 to support the country's target of 6.5% GDP growth. While credit growth in H110 stood at 10.5% (around 21% annualised) and is currently lower than the full-year target, Fitch expects credit to expand at a faster pace in H210, meaning that it is on track to record its fourth straight year of growth exceeding GDP by more than 3.0x. That said, the dependence on loan growth is not totally surprising, given that Vietnam does not have a well established local capital market.

With such growth expectations, Fitch considers deterioration in loan performance to be inevitable within the medium term. Average NPLs for rated banks are already estimated to have been around 2.8%[2] at end-H110, with special-mention loans at around 11%. However, the more immediate challenges involve compliance with prudential capital requirements and the avoidance of any further weakening of liquidity. Should competition for deposits intensify, margins will become squeezed, increasing the prospect of banks seeking wholesale funding through debt/hybrid issuance, which adds another risk dimension. Fitch remains concerned about banks' increased exposure to inflationary pressure and market confidence on the VND

[1] Calculated by dividing the sum of customer loans and interbank term deposits/lending by the sum of customer deposits, term deposits from financial institutions, borrowings from domestic non-financial institutions and foreign financial institutions, and certificate of deposits. However, Fitch notes that the final components of the LTD ratio are yet to be decided.

[2] According to Vietnam Accounting Standards (VAS); Fitch estimates that under IFRS they would be at least 1-2x higher in general. There is minimal difference in BIDV's IFRS and VAS loan quality indicators.

arising from excessive foreign-currency loan growth in H110 (27% for the system), given the possibility of further VND devaluation against the USD following a 2.1% devaluation in August 2010.

Profitability of the rated banks in 2009 was generally comparable with 2008 despite much stronger loan growth. H110 results suggest that 2010 net income should remain broadly similar to that achieved in 2009. ROAA is just adequate across the portfolio of rated banks (where the average was 1.3% and 1.1% for H110 and 2009, respectively). State-owned banks, including Vietnam Bank for Agricultural and Rural Development (Agribank) and Vietnam Joint-Stock Commercial Bank for Industry and Trade (Vietinbank), stand out as the weakest, having reported an ROAA of just 0.5% in H110 (2009: 0.42% and 1.18%, respectively). The banks therefore have only a modest cushion to absorb any meaningful rise in problem loans. Any losses would likely compound their capital adequacy problems as their capital is also modest, bearing in mind the vulnerability of profitability to higher credit costs and the current/expected pace of credit growth.

Fitch therefore remains of the view that the credit profile of the Vietnamese banking sector is broadly weak, and this is reflected in the low Individual Ratings across the rated portfolio.

Profitability — Margin Pressure

Table 1. Profitability of Rated Banks

	Operating profit[a] (% of average assets)				Net income (% of average assets)			
(VAS)	H110[b]	2009	2008	2007	H110[b]	2009	2008	2007
Total (six banks)	**2.02**	**2.06**	**2.68**	**3.07**	**1.26**	**1.10**	**1.05**	**1.13**
Agribank	1.06	1.74	2.82	3.17	0.53	0.42	0.59	0.58
BIDV	2.12	2.25	2.41	3.36	1.49	1.13	0.98	0.95
Vietinbank	1.12	1.77	2.10	2.57	0.47	1.18	1.00	0.76
Vietcombank	2.53	2.43	3.14	2.72	1.70	1.65	1.26	1.43
ACB	1.67	2.20	3.27	3.44	1.17	1.61	2.32	2.71
Sacombank	2.33	2.67	2.06	3.81	1.55	1.94	1.43	3.13

[a] Excluding impairment charges
[b] Unaudited
Source: Fitch

Banks' profitability appeared quite satisfactory in H110, but considering the risks pertaining to the local banking sector, it was only adequate by international standards. In H110, the estimated average margin[3] of Fitch-rated banks held firm at around 3% (3.02% in 2009), while loan loss provisions were low on the back of strong loan growth and the interest subsidy programme. However, the profitability of rated banks came under pressure, with their operating ROAA declining to 2.02% in H110 (annualised) from 2.06% in 2009 (2008: 2.68%) on account of them having paid higher deposit rates to mobilise funds for supporting the excessively strong credit growth. Given competition for fund mobilisation, the banks were unable to fully pass higher funding costs on to borrowers in H110, although this was somewhat offset by lower provisioning charges. While the average ROAA of the six banks (based on net income) appeared to have improved to 1.26% in H110, Fitch believes this may not be sustained, especially if the banks set aside higher provisioning at year-end.

Fitch expects the banks' profitability to remain under pressure in H210 and 2011. While they have cut both lending and deposit rates since Q210, in line with the government's guidelines, the former are likely to decline more than the latter, given ongoing high competition for deposits, which would be further intensified by the new regulatory LTD ratio. In addition, Fitch expects provisioning charges to

[3] Margin is defined by net interest income divided by earnings assets

increase at some stage, given sustained weak underlying loan quality and excessive loan growth, which the agency believes has allowed borrowers with weak/marginal credit profiles to remain in operation, despite their leverage being estimated to have risen.

Loan Growth — Still Excessive, Albeit Moderating

By end-H110, credit growth had decelerated to around 10.5% (since end-2009; annualised rate of around 22%), accounting for 42% of the government's credit growth target of 25% yoy for 2010 (2009: 37.7%). This was mainly due to lower loan demand as effective borrowing rates increased following the removal of interest rate caps (12% pa previously) for medium- and long-term loans in February 2010 and for short-term loans in April 2010. Interest rates for VND loans reportedly rose by 2%-3% to 14%-18% pa after the removal of the caps, as the banks were able to charge negotiable rates above the previous effective borrowing rates (which were a combination of the cap and various fees). Loan demand was further hit by a cut in the interest subsidy to 2% (since March 2010) from 4% and still subdued economies in the US and Europe.

Table 2. Loan Growth of Rated Banks

	Amount (VNDtrn)		Loan growth rate (%), yoy			% of loans in total assets	
(VAS)	Jun 10[a]	Dec 09	Jun 10[a]	Dec 09	Dec 08	Jun 10[a]	Dec 09
GDP	**855.2[b]**	**1,645.5[b]**	**6.1[c]**	**5.3[c]**	**6.3[c]**	**n.a.**	**n.a.**
Total gross loans (six banks)	**1,097.1**	**1,001.3**	**19.0**	**31.9**	**16.6**	**65.1**	**65.5**
Agribank	389.7	368.1	7.4	25.0	17.0	75.6	76.5
BIDV	227.4	206.4	20.0	28.2	22.0	67.6	69.9
Vietinbank	187.1	163.2	35.3	35.1	18.2	63.5	66.9
Vietcombank	147.9	141.6	12.7	25.6	15.5	59.7	55.4
ACB	72.4	62.4	41.9	79.0	9.5	40.9	37.1
Sacombank	67.6	59.7	37.3	70.4	-1.0	59.6	57.4

[a] Unaudited
[b] Nominal GDP
[c] Real GDP growth rate
Source: Fitch

Nevertheless, credit growth remains high, particularly compared with Vietnam's economic growth (GDP growth of 6.1% yoy in H110; target rate for 2010 of 6.5%), although this is partly due to Vietnam not having a fully functional domestic capital market. The Fitch-rated state-owned banks (except Agribank and Joint Stock Commercial Bank For Foreign Trade of Vietnam (Vietcombank)) reported 20%-plus yoy loan growth in H110, while the two private banks (Asia Commercial Bank (Vietnam) (ACB) and Saigon Thuong Tin Commercial Joint Stock Bank (Sacombank)) have outgrown the state-owned banks and the system as a whole since 2007 (except for 2008). In particular, growth in the system's foreign-currency loans (mostly USD loans) was exceptionally high at around 27% in H110 on account of exporters (ie not just importers) being permitted to borrow in USD. On the other hand, VND loans posted just 5% growth over the same period as the interest rate differential between VND loans and USD loans (7%-8% pa) widened. This resulted in corporates borrowing more USD as a cap on USD deposit rates[4] (1% pa) was set up in February 2010. Prior to the cap, USD corporate deposit rates were around 4%. Fitch notes that the rapid USD loan growth in H110 increased the vulnerability of banks' liquidity and loan quality to inflationary pressure and market confidence on VND.

The government has encouraged the banks to grow their loans further in H210 to achieve the 2010 credit growth target and ultimately boost Vietnam's economic

[4] Vietnamese banks' lending rates are closely correlated with deposit rates. The banks generally pass changes in deposit rates on to borrowers, although competition for deposits sometimes limits their ability to do so.

growth. To facilitate this, the state-owned banks and joint stock banks cut their normal lending rates to around 14% pa and less than 15% pa, respectively, in July 2010. They also agreed to reduce deposit rates (including promotional packages) to 11.0%-11.5% pa from July 2010[5] (from 11.5%-11.7% pa). In addition, reserve requirements for loans to the agricultural sector are to be lowered to 1.5% from 3%, for banks[6] with more than 40% loan exposure to the sector, to increase funding supply to that sector. Fitch expects these measures to spur credit growth in the system for the rest of 2010, although full-year growth is likely to be slightly lower than the government's target of 25% yoy. While the new prudential regulations may slow the system's credit growth somewhat, Fitch is of the view that they would further intensify competition for fund mobilisation amongst banks. Meanwhile, the agency notes that most Vietnamese banks plan to expand VND loans in H210 at the expense of USD loans, given the lack of USD funds to support USD loan growth following substantial use of available sources for USD mobilisation.

While the pace of credit growth in 2010 remains below that of 2009, Fitch considers the target to be aggressive. Apart from the immediate weakening of liquidity and capitalisation, this will likely give rise to deterioration in underlying loan quality. In particular, Fitch sees some risk from the banks' aggressive expansion of USD loans in H110 (noting a 2.1% devaluation of the VND against the USD in August 2010), which may trigger a further devaluation of the VND.

Non-state-owned corporates accounted for 41% of the rated banks' loan books at end-2009, while 23% and 30% of loans were lent to state-owned corporates/joint stock companies and individuals, respectively. By industry, manufacturing & processing, trading/services & others, and retail accounted for 22%, 26%, and 30% of the banks' loan books, respectively. Construction (12%) was another major area where the banks (particularly Bank for Investment and Development of Vietnam (BIDV)) extended loans. Fitch believes the loan mix at mid-2010 was similar to that at end-2009, although some loans may have been used for non-production-related activities[7], noting that it is difficult to monitor where funds ultimately go. The agency estimates that foreign-currency loans accounted for more than 25% (on average) of the banks' loans books at mid-2010 (end-2009: 16%), due to rapid USD loan growth.

Loan Quality/Loan Composition – Overstated and Weak

On the face of it, loan quality has remained adequate, with the banks' estimated average NPL ratio manageable standing at around 2.8% at mid-2010 (2.65% at end-2009), based on VAS. However, Fitch notes that the banks' underlying loan quality remains weak, having been well masked by high loan growth. Fitch also notes that reported NPL ratios and coverage for most of the banks are generally understated, as overdue date-focused loan classification is common under VAS. Fitch estimates that the NPL ratio under IFRS would be at least 1-2x higher than that reported under VAS. However, the deviation between the two accounting standards at BIDV is minimal, which explains the much higher credibility on the banks' loan classification, compared with most other state-owned banks, including Agribank, Vietinbank and Vietcombank, and the two private banks (ACB and Sacombank), which do not produce IFRS-based financial statements.

[5] Deposit rates will be further reduced by late September 2010 to 10.2%-10.5%.

[6] Of the six Vietnamese banks rated by Fitch, Agribank is currently the only one that could benefit from the new prudential regulations.

[7] Anecdotal evidence suggests there could be cases where corporates borrow USD loans and simultaneously deposit them at banks after conversion to VND to enjoy the interest differential between USD loans (5%-7% pa) and VND deposits (around 11%), as well as corporates in non-construction sectors using borrowed funds to purchase properties for investment purposes.

Table 3. Loan Quality and Coverage

(VAS)	NPL ratio (%)			SML ratio (%)			NPL coverage (%)	
	Jun 10[a]	Dec 09	Dec 08	Jun 10a	Dec 09	Dec 08	Jun 10a	Dec 09
Total (six banks)	2.80[b]	2.65	3.14	n.a.	10.17	9.64	n.a.	71.39
Agribank	n.a.[c]	4.15	3.25	n.a.	15.90	11.36	n.a.	41.66
BIDV	2.92	2.98	4.02	14.33	16.05	21.14	83.57	87.81
Vietinbank	0.99	0.61	1.81	1.27	1.02	3.29	123.51	154.97
Vietcombank	4.15	2.47	4.61	15.87	5.67	2.71	79.02	132.22
ACB	0.37	0.41	0.89	0.52	0.58	1.14	224.94	197.11
Sacombank	0.62	0.64	0.59	0.76	0.17	0.37	149.92	134.25

[a] Unaudited
[b] estimated
[c] Agribank's loan classification at mid-2010 is not available.
Source: Fitch

Fitch expects asset quality to remain under pressure in H210 and 2011, particularly given the high possibility of the banks' special-mention loans (even current loans) becoming NPLs[8]. This is due to the inherently volatile economic environment, prolonged slow demand in the US and Europe, a potential further devaluation of the VND against the USD (following August 2010's 2.1% devaluation), and as economic stimulus measures are withdrawn.

In addition, Fitch expects the banks' asset quality to be negatively affected by their likely exposure to the troubled state-owned Vietnam Shipbuilding Industry Group (Vinashin; estimated total debts of USD4.2bn equivalent). The reported exposure of Agribank, Vietcombank, Vietinbank, ACB, and Sacombank to Vinashin ranges from nil to 18% of equity at end-July 2010. BIDV has not yet disclosed its exposure level. In fact, Fitch would not rule out the actual exposure being larger than the reported exposure, noting that the substantial gab between the aggregate reported exposure of the rated banks and the system's total exposure to Vinashin.

Fitch believes that banks may have engaged in loan forbearance (which, if this is the case, would not be unique to Vietnam), but the agency acknowledges that it is unable to quantify whether and to what extent this may be the case. The banks believe they make appropriate commercial assessments with respect to the risk associated with each individual loan. With capital positions generally modest, the downside to classifying loans more stringently (which is the case under IFRS) is that many banks would find themselves even more challenged to maintain appropriate capital levels, if not in breach of prudential regulations.

Funding & Liquidity – High Exposure to Market Volatility

Deposits remain a major funding source for Vietnamese banks (around 70% of total liabilities for the rated banks), with the rest sourced from borrowings from the State Bank of Vietnam and the government, interbank borrowings, other debts and certificates of deposits. Of deposits, the VND accounted for around 80%, with the rest denominated in foreign currencies (mostly USD). However, Fitch notes that the banks' deposits are generally less sticky, given that more than 40% come from corporates. The agency also notes that depositors are very sensitive to confidence on the VND and deposits rates in general, resulting in high deposit rate-based competition amongst banks.

[8] Fitch estimates that additional equity of around VND100trn (versus the six banks' total equity of VND120trn at mid-2010) would be needed for the six banks to cover all NPLs and SMLs (under VAS), while maintaining an average equity-to-asset ratio of 7% (versus a ratio of around 7% at mid-2010).

Table 4. Liquidity and Deposit Composition

	LTD ratio			Deposit mix at end-2009	
(%)	Jun 10[a]	Dec 09	Dec 08	Retail	Corporates/others
Total (six banks)	**99.4**	**101.7**	**89.0**	**53.4**[b]	**46.6**[b]
Agribank	106.7	110.9	98.2	n.a.	n.a.
BIDV	99.9	110.2	98.5	39.6	60.4
Vietinbank	120.6	109.9	99.3	53.1	46.9
Vietcombank	84.0	83.8	71.8	45.5	54.5
ACB	73.6	71.7	54.2	81.9	18.1
Sacombank	89.9	98.6	75.9	77.9	22.1

Note: Official development assistance and state-directed/planning loans are included in the LTD ratio. Fitch estimates that the LTD ratio without these loans would be slightly lower.
[a] Unaudited
[b] Excluding Agribank
Source: Fitch

Banks' liquidity deteriorated substantially in the 18 months to mid-2010, due to continued excessive credit growth. The average LTD ratio (per Fitch's calculations) among the rated banks increased to 99% at mid-2010 (102% at end-2009) from 89% at end-2008. While ACB's LTD ratio was still lower than that of the other banks, Fitch notes that its strong desire to expand its market share of loans could weaken the ratio. The agency expects an increasing possibility of banks funding their excessive credit growth through more wholesale channels, given that funding mobilisation should lag credit growth. If and when this happens, there would be an increased risk concerning refinancing should the banks not strengthen their financial positions and liquidity, and the banks' profitability would be further pressured by rising interest in bond issuance for both VND and USD. Such refinancing risk would potentially be magnified the shorter the terms of funding, although Fitch believes the banks would initially target long-term funding. Furthermore, Fitch notes that rising wholesale funding (particularly through short-term funding) would lead banks' exposure to market volatility and confidence on VND to rise notably.

Fitch estimates the foreign-currency LTD ratio of the rated banks to have been around 120% at mid-2010, following rapid growth in foreign-currency loans. This contrasts with a decline in foreign-currency deposits following the setting of the cap on USD deposits in February 2010. Given this, Fitch is concerned about banks' liquidity becoming more vulnerable to inflationary pressure in Vietnam. Any weakening of market confidence on the value of the VND against the USD may shift medium- and long-term deposits to short-term deposits, with VND deposits also withdrawn from the system and converted into USD/gold.

From 1 October 2010, banks are supposed to not lend more than 80% of the sum of their deposits and some wholesale funding under the new prudential regulations. Although how the regulations would be implemented remains to be seen, Fitch is of the view that the new regulations will lead to higher competition for deposits, particularly noting that the average LTD ratio (based on the initial regulatory definition) was estimated at around 98% for the rated banks (around 100% for state-owned banks and around 80% for private banks).

Capitalisation – A Very Limited Cushion in General

Table 5. Capital Ratio

	CAR (%)			Equity-to-asset ratio (%)		
(VAS)	Jun 10[a]	Dec 09	Dec 08	Jun 10[a]	Dec 09	Dec 08
Total (six banks)	**8.0-10.9**	**5.0-11.4**	**6.3-12.4**	**6.57**	**5.68**	**7.06**
Agribank	8.19[b]	4.97[b]	6.26[b]	6.44	4.13	4.44
BIDV	10.89	9.53	8.90	7.04	5.95	5.47
Vietinbank	8.00	8.46	12.02	5.63	5.24	6.37
Vietcombank	8.45[c]	8.22	9.25	7.00	6.58	6.33
ACB	9.00	9.73	12.44	5.63	6.02	7.37
Sacombank	9.41[c]	11.41	12.16	8.74	10.35	11.34

[a] Unaudited
[b] Agribank's CAR ratios are based on initially advised ones. Fitch will review Agribank's CAR ratios upon detailed information on new CAR ratios provided by the bank, given that it advised that its CAR ratios are much higher than those included above.
[c] The CARs of Vietcombank and Sacombank after taking newly issued shares in Q310 are estimated at 10.0% and 11.5% (based on risk-weighted assets at mid-2010, respectively. However, Fitch expects the banks' CAR to remain under pressure, given the strong loan growth target. Source: Fitch

Despite the excessively strong credit growth, most of the rated banks managed to maintain their CAR above the current regulatory minimum of 8% at mid-2010, albeit only just. Agribank and BIDV were recapitalised through government capital injections of VND10.2trn (29% of equity at end-2009) and VND5.3trn (23%), respectively, in Q110. However, the former bank (with a CAR of 8.19% at mid-2010) still has marginal capacity for growth and therefore will be dependent upon internal capital generation/retention and raising further external capital. Meanwhile, Vietinbank is on the current benchmark CAR of 8%, so it too remains constrained in meeting growth targets while remaining compliant with minimum regulatory capital ratios.

ACB's capital benefited from its largest shareholder, Standard Chartered Bank, and other existing shareholders converting convertible bonds of VND1.3trn (13% of its end-2009 equity) into equity in 2009, while Sacombank increased its capital by issuing new shares and selling treasury shares (14% and 5% of its end-2009 equity, respectively). Meanwhile, most banks retained their earnings by issuing shares rather than cash dividends to existing shareholders. However, in Fitch's opinion, the banks' current capital level and earnings retention are still insufficient to cushion against higher credit costs, particularly if credit growth remains excessive. Also, Fitch is of view that the banks will continue to face downward pressure on their CARs, due to strong loan growth (including rapid expansion of FC loans in H110, which remains potentially vulnerable to further VND devaluation), and an upward adjustment in risk asset weight to 250% from 100% for real estate and stock loans.

That said, Fitch notes that most banks in the system have been planning to raise capital to meet new prudential regulations of a minimum CAR of 9% and minimum capital of VND3trn (around USD160m), through the issuance of new shares to local and foreign investors, additional capital injections from the government (in the case of state-owned banks) and through debt issuance (including subordinated debt). The new regulations are due to come into effect from 1 October 2010.

In this regard, Agribank has proposed an additional capital injection, while BIDV has been seeking strategic investor(s) and an initial public offering to achieve a target CAR of more than 10% under VAS. Vietinbank is reportedly in discussions with Nova Scotia and International Finance Corporation to sell new shares. Vietcombank has been planning to issue more shares to the domestic capital market to recapitalise itself, following its new share issue in August 2010 (VND1.12trn or 6% of equity at mid-2010). ACB plans to raise equity capital of VND1.6trn (16% of equity at mid-2010) and issue 10-year subordinated bonds (VND3trn) by end-October 2010. Sacombank is reported to have raised its equity capital by 17% in Q310 through issue of new shares to its existing shareholders, while Fitch believes it could consider further capital raising initiatives in 2010-2011 to accommodate any significant growth ambitions.

Other banks' capital-raising plans have not been reported. Some could try to raise capital through the domestic capital market, however how and when the banks will recapitalise remains uncertain, given that the Vietnamese capital market is not large enough to absorb all the new shares from the banks. Moreover, Fitch believes that few banks in the system (other than the rated banks) are close to finalising capital-raising plans despite the fast-approaching cut-off date.

In Fitch's view, three possible scenarios are likely: (i) the proposed regulations will be amended; (ii) the Bank of Vietnam will grant banks a time extension to become compliant; or (iii) the Bank of Vietnam will show forbearance. With regards to the last of these scenarios, there are recent precedents involving state-owned banks Agribank (which had a CAR ratio of below the current regulatory minimum of 8% in 2008 and 2009[9]) and Vietcombank (whose CAR ratio was at 7.60% at end-March 2010).

Although there are examples of external capital having been raised over the past year, the process has often been slow and there is limited capacity for the domestic market to absorb the supply of capital required to fully and sustainably meet new regulatory requirements. The larger banks rated by Fitch are best placed to tap available sources, which include foreign investors (most likely foreign banks — which the agency believes could be a positive for the credit profiles of the rated domestic banks). However, to the extent that any capital is raised domestically, it would only serve to limit the prospects for small domestic banks to raise such capital. One of the options available to local banks is to merge, but this seems rather unlikely (at least in the near term) given the fast-approaching regulatory cut-off date (of 30 September 2010) and the lack of news on banks making headway in merger discussions. Moreover, Fitch believes that family-run banks would often have difficulty merging and integrating their operations without confronting cultural differences. Therefore, the most likely scenario is that the government will force smaller banks to merge into larger ones.

[9] Agribank has advised that its CAR ratio was above 8% at end-2009 without proper explanation. Fitch will review the bank's historical CAR ratios based on an auditor's opinion, which is to be provided by the bank.