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Banks/Vietnam

Impact of Fiscal Measures on Vietnamese Banks' Outlook

Fiscal Stimulus Measures

The most notable fiscal stimulus measure relating to Vietnam's banks is an interest-rate subsidy scheme[1] whereby the government provides 4% of interest expenses on domestic currency loans (eg if the lending rate for a borrower is 10%, the borrower only has to pay 6% as the government pays the 4% balance). The subsidy applies to a wide range of corporate and individual borrowers with subsidised loans being offered by commercial banks, finance companies and the Vietnam Development Bank (VDB, a government policy bank). Whereas this programme was initially limited to short-term working capital loans with a maximum tenor of eight months that matured before end-2009, it was extended in April 2009 to cover loans maturing before 2011 for a maximum period of 24 months. To date, VND255trn in loans has been granted under the subsidy scheme (equal to around 19% of system-wide loans). So far, most of these loans have refinanced existing loans given that Vietnam's system-wide loan growth was quite low in Q109 at just 3%. The annual cost of the 4% subsidy for loans granted so far should be about VND10trn, versus a total budget for the subsidy scheme of VND17trn (USD1bn).

Under another scheme, individuals and corporate clients registered in 61 poor districts are eligible for low interest rate loans from the various major state-owned commercial and policy banks. Under this scheme[2], the central bank (the State Bank of Vietnam or SBV) assumes half of borrowers' interest payments. In addition, VDB offers 12-month interest-free loans to certain weak borrowers suffering in the current environment. The extent to which these schemes have been utilised and their ultimate planned size is not yet known. VDB also guarantees certain SME loans up to a budgeted total of VND200bn (50% utilised to date).[3]

Profitability Outlook

The profitability of Vietnam's banks in FY08 was generally good, reflecting relatively low credit costs (likely benefiting from loan restructuring), good investment income on government bonds and strong 25% loan growth. Net interest margins (NIMs), however, have since come under pressure due to moral suasion on the banks to keep lending rates low and deposit rates high as the authorities are keen to ensure a reasonable level of loan growth amidst the difficult economic environment. From end-2008 to April 2009, the average spread between VND lending and deposit rates narrowed to 2.5% from 3.8%. Nevertheless, margins for state-owned commercial banks should remain satisfactory as they continue to benefit from a material proportion of low-cost government deposits. Lending and deposit rates for banks in Vietnam remain capped at 1.5x the base rate (currently 7.0%; hence maximum lending and deposit rates of 10.5%). Meanwhile, Fitch Ratings expects credit costs to rise notably in future given the very challenging economic environment, with contributing factors being higher inflation and interest rates in 2008, and since then property price weakness, VND depreciation (down 10% against the USD since mid-2008), and lower demand for Vietnam's exports given slower global growth. Declining export orders will chiefly affect the manufacturing sector, and within this sector, SMEs are most exposed. The weakening of the VND is a particular concern, rendering it more expensive for borrowers to service USD loans (around 20% of system-wide loans). Whilst in place, the interest-rate subsidy scheme should however help support loan quality.

Asset Quality

According to Vietnamese Accounting Standards (VAS), system NPLs (loans classified as substandard, doubtful and loss) increased to 2.1% of total loans in 2008 from 1.7% at end-2007, but remained below

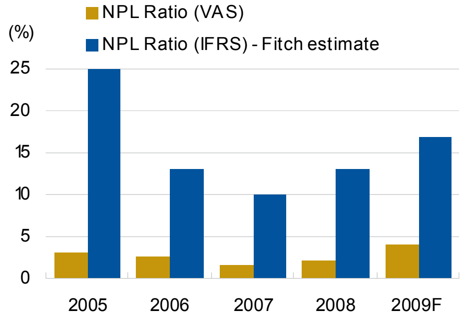
[1] Governed by and detailed in Decision No 131 (23 January 2009), Circular 02 (3 February 2009), Decision No 333 (10 March 2009), Circular 04 (13 March 2009), Decision 443 (4 April 2009), Circular 05 (7 April 2009), Decision 931 (8 April 2009)

[2] Governed by and detailed in Resolution No 30a (27 December 2008) and Circular 06 (9 April 2009)

[3] Governed by and detailed in Decision No 14 (21 January 2009)

the SBV's original estimate of 3.5%. Based on IFRS accounts for the four major state-owned banks, however, and after discussions with market participants, Fitch believes that IFRS NPLs would have stood at around 13% of total loans at end-2008 (see Chart 1). As mentioned, Fitch expects loan quality to come under some pressure in future, as indicated by the high level of IFRS NPLs. Despite the interest-rate subsidy programme, system loan growth in Q109 remained low at about 3% (FY08: 25%). Nevertheless, the SBV has retained its target level of loan growth for 2009 at a relatively high 22%, and expects the focus to be on the agricultural, industry and construction sectors (which accounted for 29%, 26% and 14% of total loans, respectively, at end-2008).

Chart 1: Classified Loans



Source: Fitch, SBV, IMF

Liquidity

During Q109, VND loans increased 3.9% while foreign currency loans grew 2.2%. This was in line with 3.4% deposit growth: 3.3% VND and 3.6% foreign currency. USD liquidity in the banking system eased during Q109 and is now generally adequate, with VND depreciation making borrowers more wary of USD loans, and with VND loans becoming cheaper due to the interest subsidy programme. VND depreciation also makes USD deposits more attractive. In addition, banks have been bringing their offshore USD deposits back onshore under the guidance of the central bank.

In March 2009, the Vietnamese government issued USD230m in bonds (USD100m one-year, USD80m two-year and USD50m three-year bonds with coupons of 3%, 3.2% and 3.6%, respectively) to the domestic market (versus an originally planned USD1bn issue). The central bank guided the commercial banks to actively invest in the issue. A reduction in the interest SBV pays on deposits in excess of required foreign currency reserves to 0.1% from 0.5% on 3 April 2009 also urged the banks to buy the bonds. As the government appears keen to accumulate USD, it is possible that exporters may be persuaded to exchange their USD receipts for VND. Dollarisation in the banking system remains high with 20% of loans and 24% of deposits being in foreign currency, mostly USD. However, these figures may somewhat understate the real level of dollarisation in the country, as many goods and contracts are directly priced in USD.

Capitalisation

Capitalisation in the banking system continued to improve with its capital adequacy ratio (CAR) rising to 9.7% at end-2008 from 8.9% at end-2007, and with all banks meeting the minimum CAR of 8%, except the Vietnam Bank for Agriculture and Rural Development (Agribank, rated Individual 'D/E'), although even it was close to this level. Nevertheless, Fitch still considers the banking system's capitalisation somewhat limited given its significant level of impaired loans (ie under IFRS) and the somewhat weak outlook for loan quality.

Of the two state-owned banks in which 10% stakes have been sold to the public, the Bank for Foreign Trade of Vietnam (December 2007, listing in process, rated Individual 'D') and Vietnam Bank for Industry and Trade (December 2008, rated Individual 'D/E'), neither has yet attracted any strategic foreign minority investors, due to economic uncertainty, as well as differing views on asset quality and pricing. The authorities are instead considering domestic strategic investors, including some of the banks' largest (state-owned) corporate clients; a development that Fitch would view with concern with regard to corporate governance and to enhancing the banks' operations and commerciality. Meanwhile, the Bank for Investment and Development (rated Individual 'D/E') and Mekong Delta Housing Bank are preparing for partial IPOs in 2009, while that for Agribank is likely to be postponed.

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