Vietnam Prosperity Joint-Stock Commercial Bank (VPB: HSX)

Wait for signals from asset quality

KB Securities

FULL REPORT
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INVESTMENT HIGHLIGHT

Maintain the No.1 position on the potential consumer credit market

The consumer credit market addressing "black credit" issues in many localities still has a lot of development room as it has only taken 2.4% of GDP and 1.8% of total outstanding loans, quite low compared to those in developed countries. In addition, total consumer credit is only about 26% of GDP, also much lower than other developed and developing markets. However, the growth rate will slow down after the initial strong growth penetration. Although the competition will be increasingly fierce, we believe that FE Credit will still maintain its No. 1 position thanks to its large business scale, database and standardized deployment procedures.

Promote business activities at the parent bank, focusing on developing digital banking individual customers

The business operations in the parent company will be boosted while the conditions for credit growth in FE Credit is being gradually controlled. The strategic segment is still retailing, which focuses on guaranteed consumer lending and SME lending, but with higher risk appetite. Additionally, VPB is also one of few digital banks which have many products creating a large amount of added value for customers such as VPDream, YOlO, products for priority customers. The bank also applied digital standards in payment activities and commercial financing.

However, asset quality issues after a quick growing period will play a decisive role in VPB valuation

Despite having a big potential of development, VPB has been under the pressure of high provision cost after strong growing period and not very tight lending conditions. Considering VPB's high troubled assets/total outstanding loan ratio (12.4% by the end of the 1Q/2019), we suppose that it will take 1 – 2 years for the bank to handle all of these assets, which will strongly affect business performance and capital base. Therefore, in the short term, we recommend to **HOLD** VPB shares. This recommendation can be changed in case there are more improvements in asset quality of the bank.

Hold

Target price (1Y)	20,000VND
Up/Down	8.1%
Current price (14/05/2019)	18,500VNĐ
Target price	20,500VNĐ
Market cap	45,450 tỷ VNĐ (1.95 tỷ USD)

Exchange rate on 14/05/2019: 1USD= 23,250 VND

Trading data	
Outstanding share volume	2,456,748,366
10-session average trading volume	1,597,336
% foreign ownership	22.72%
Cash dividend	0 VND/cp

% price change

(%)	1M	3M	6M	12M
VPB	-4.79%	-6.44%	-7.35%	-39.1%
VN-INDEX	-2.2%	7.14%	9.77%	-9.12%

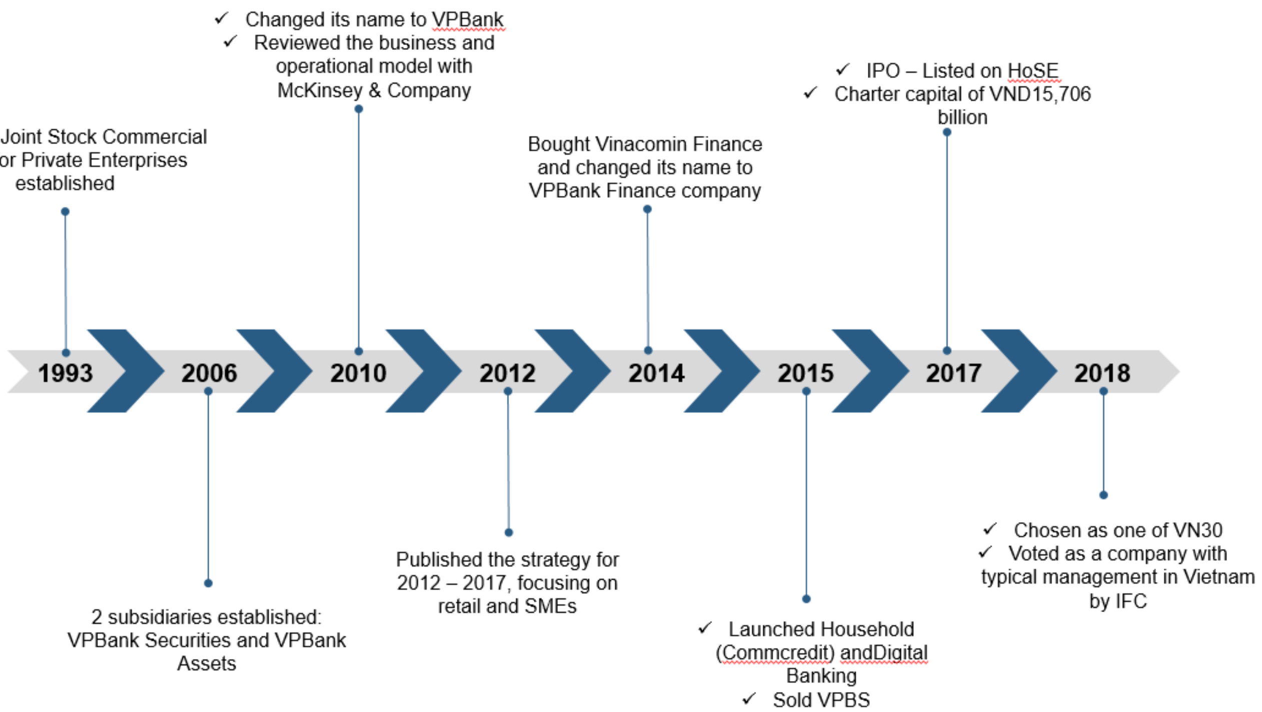
Forecast revenue and valuation

	2018A	2019F	2020F	2021F
NII (bil VND)	24,702	28,602	31,384	34,769
Growth rate (%)	19.8	15.8	9.7	10.8
Total operating income (VND bn)	31,086	35,114	37,928	42,977
CIR (%)	34.2	34.7	36.1	34.5
Net profit (VND bn)	9,199	9,476	9,165	12,383
Growth speed (%)	13.15	3.01	-3.28	35.11
EPS (VND thousand)	2,908	2,996	2,898	3,915
BVPS (VND thousand)	13,735	16,611	21,166	24,942
P/B	1.35	1.11	0.87	0.74

Source: Fiinpro, KBSV

OVERVIEW

Shape 0: History of development



Source: VPB; KBSV Research

The size of the balance sheet (only compared to those of listed banks)

By the end of 2018, the total assets of VPB reached VND323,291 billion, ranking 7th in the banking system, gaining two levels compared to that in 2016. After the bank's IPO was successful in 2017, the current charter capital is VND25,300 billion, ranking 5th after three state-owned banks and TCB (previously VPB ranked 9th in the whole sector), but the gap between VPB and the above mentioned banks is still big. EBT of VPB in 2018 was VND9,199 billion, which helped to maintain the ranking of the bank in Top 4 banks with highest EBT for three years. However, VPB was ranked 4th in partly because Vietinbank had to make a large provision, putting negative impacts on its profit.

Business scale

According to the data in 2018, VPB have been operating with one head office in Hanoi, 221 branches and transactions offices, 83 centers and Hubs SME, with roughly 650 ATM/CDMs. The number of staff by the end of 2018 in VPB was 27,429 people, gaining 15.1% over the previous year.

Credit and mobilization market share (Figure 1)

As we estimated at the end of 2018, held about 4.6% and 3.7% credit and mobilization market share, which are average in private joint stock commercial banks in Vietnam. However, in the strategic segment of unsecured consumer lending, with about VND 53,000 billion of outstanding loans at the end of 2018, FE Credit – a subsidiary of VPB accounted for about 50% of the market share.

Credit ratings

In 2018, VPB's BCA was upgraded from B2 to B1, and from positive to stable outlook. Counterparty Risk Assessment (CRA) was also raised from B1 to Ba3; and Corporate Family Rating (CFR) of FE Credit was upgraded from B2 to B1 with a stable outlook.

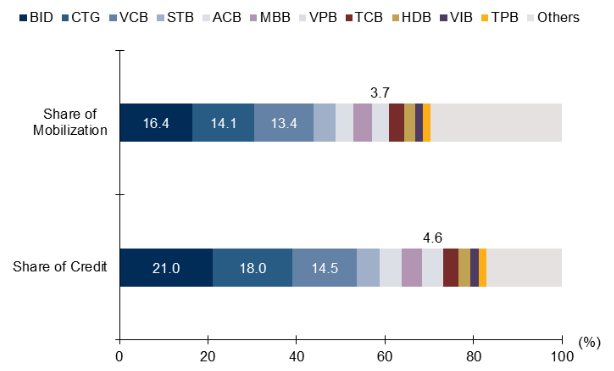
Ownership structure (Figure 2)

Chairman Ngo Chi Dung and associates have owned about 30% of the bank's shares. Foreign ownership in VPB is currently kept at 22.72%, 7.28% lower that the ceiling rate allowed by the SBV (30%). We suppose that many private joint stock commercial banks have locked foreign room at a lower ceiling rate to leave room for capital raising in the future when the demand increases. Another difference in VPB's ownership structure compared to many other private banks is the absence of a strategic partner.

Operating model (Table 1)

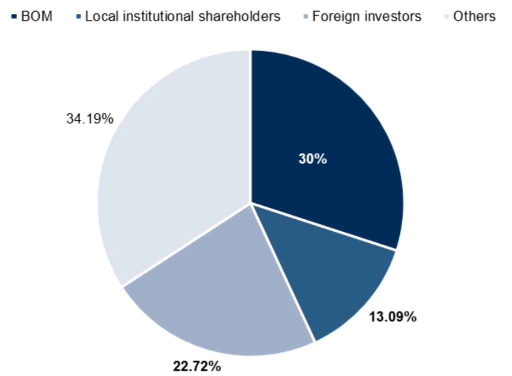
After VPB sold VPBS subsidiary in 2015, the bank has only two subsidiaries left, which are FE Credit and VPB AMC. In particular, FE Credit operates in consumer credit which is one of the core strategies of VPB from the past.

Figure 1: Credit and mobilization market share



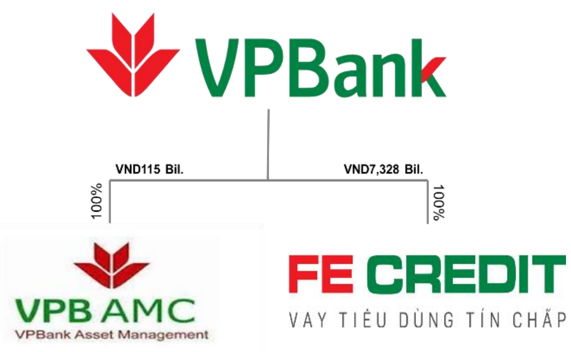
Source: SBV; Banks' financial statements; KBSV Research

Figure 2: VPB's ownership structure



Source: VPB; KBSV Research

Shape 1: VPB operating model



Source: VPB; KBSV Research

BUSINESS MODEL

Credit structure

In general, consolidated credit structure has more potential risks than the average. Unsecured consumer credit at FE Credit accounted for 23% of total consolidated outstanding loan

If including both corporate and VAMC bonds, the current outstanding loan proportion of FE Credit accounted for 23%. Most of which was unsecured loans with relaxed lending criteria, and high risks aiming at borrowers whose average incomes range from 3 – 7 million per month. These loans are valued at under VND 100 million (VND20 million on average), and borrowed by provinces surrounding large cities, with increasing consumption demand.

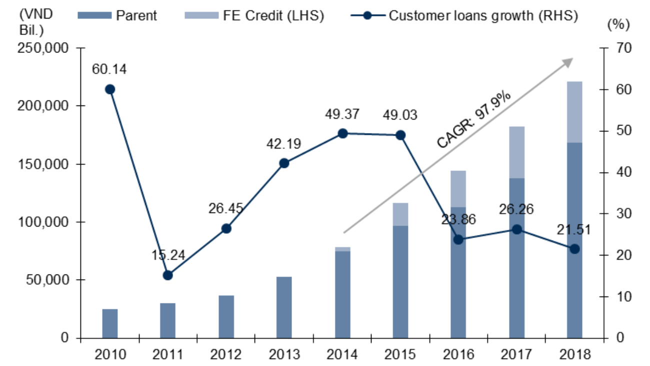
Riskier model is followed by better interest rates (the average NIM was about 27% compared to 3 – 4% of an ordinary collateral loans). Total unsecured loans account for 35% consolidated loans balance, which means 12% (about VND 26,600 Bil. in definite term) of unsecured loans belong to parent's loans book. According to our research, this segment has been also developed towards retailing (accounting for 31%), but in mid-end segment, with a monthly income from VND10 million to VND20 million. 19% of the rest retailing (about VND42,000 billion) mainly includes mortgage loans to buy houses and cars, and credit cards.

In addition, VPB also operates in three other segments including:

- **Corporte customers (31%):** This group is divided into two small groups, which are CMB (with a revenue per year from VND400 – VND1,600 billion) and CIB (with a revenue per year of over VND1,600 billion). The main products are working capital loan and project investment.
- **SMEs (13%):** Focus on Micro SMEs with a revenue of under VND400 billion per year.
- **CommCredit (2%):** This is a group of small businesses operating in the locality, with a revenue ranging from VND0.1 to VND2.5 billion per year, and without business license. This segment was established in July 2015 and only reached breakeven in 2018.

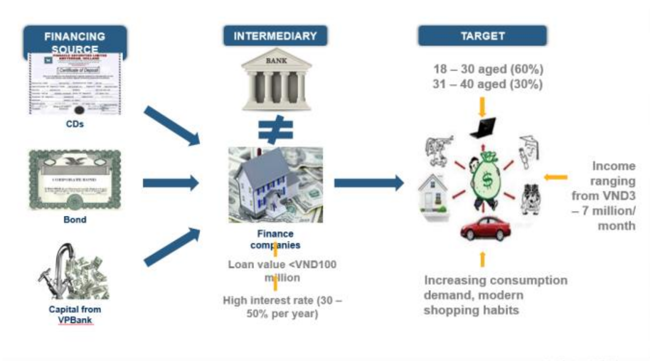
In terms of TOI structure, FE Credit's revenue accounts for 52%, although it only contributes 23% to total credit. In addition, retail customer group; corporate customers; SMEs and CommCredit accounted for 18%; 20%; 6% and 4% of TOI in2018.

Figure 3: VPB credit structure (consolidated)



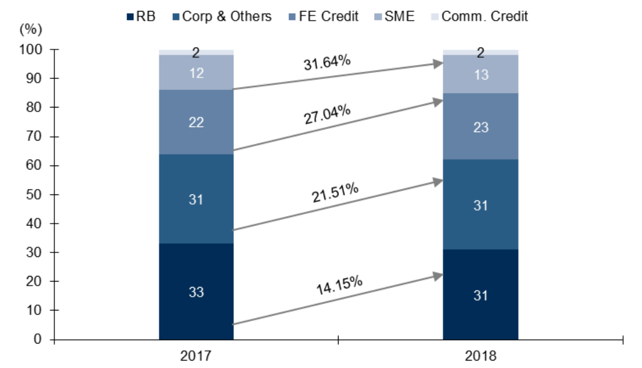
Source: VPB; KBSV Research

Shape 2: Business model of a finance company



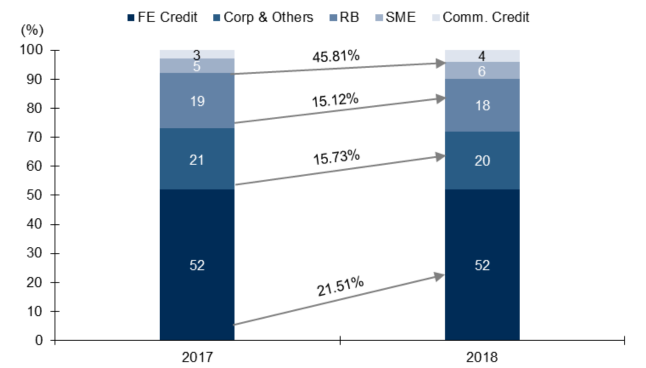
Source: KBSV Research

Figure 4: Credit structure by customer segment (including both corporate and VAMC bonds)



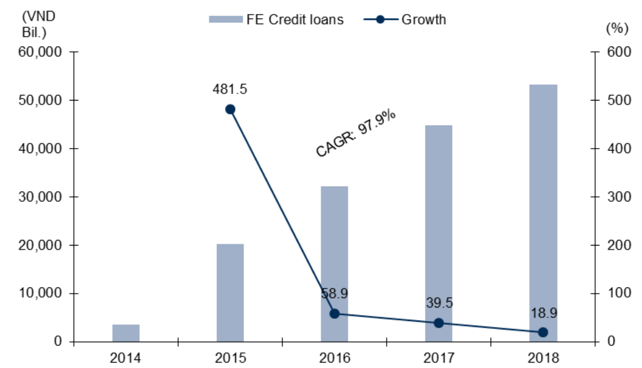
Source: VPB; KBSV Research

Figure 5: Operating income structure



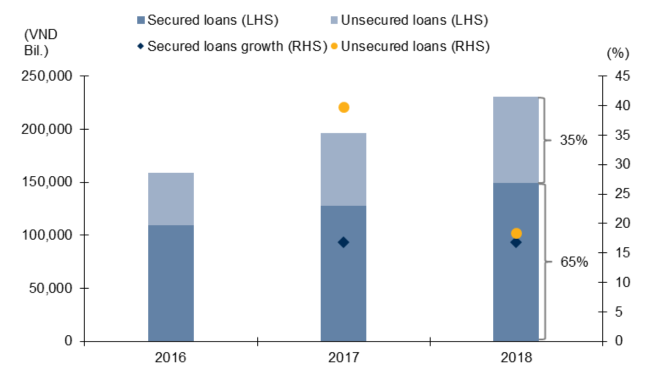
Source: VPB; KBSV Research

Figure 6: FE Credit growth



Source: VPB; KBSV Research

Figure 7: Credit structure by secured assets



Source: VPB; KBSV Research

Mobilization structure

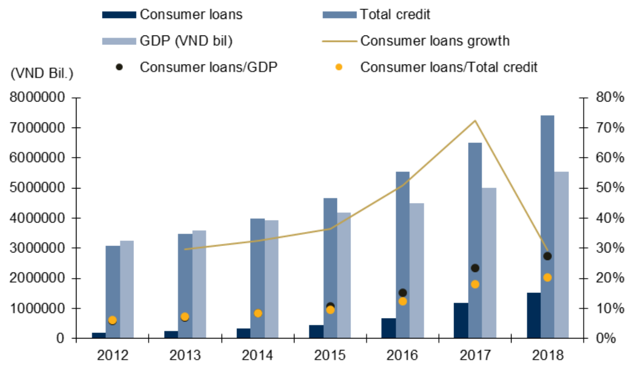
Typical mobilization structure with high proportion from CDs of mid term and long term

Due to VPB's characteristic credit operation, the mobilization structure is also quite different compared to that in other banks. The weight of valuable papers has been increasing since FE Credit was effective (2014), reaching 17.5% by the end of 2018, quadrupled the sector's average. The reason is that SBV required finance companies not to mobilize from citizens as in commerce banks, so FE Credit has to mobilize from other sources, which are Bank CDs in particular. Mobilization objects are corporates with idle money, the cost is about 10-12%/year and the term is mostly short to medium term (less than 3 years). In addition, the parent bank also has quite high deposits from Bank CDs (VND 10,000 billion in 2018, a sharp decrease from VND 27,500 billion in 2017).

Regarding mobilization structure by terms, VPB does not have strong advantages in CASA. It can be seen that banks with large CASA all have their own large and strong corporate customer ecosystem. Therefore, in the near future, VPB is not likely to compete with other banks on this market. VPB are focusing on mobilization from citizens, with a surge of 36% in 2018. In addition to the strong competition in short term deposit interests, the bank has consciously enhanced the service quality, trading system and technology to keep private customers.

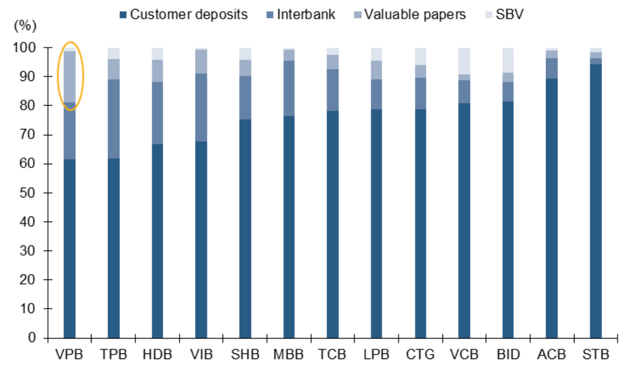
Additionally, VPB's high interbank mobilization rates partly shows the high liquidity pressure on the bank in some periods as the market tier 1 is not really stable.

Figure 8: Mobilization structure by products



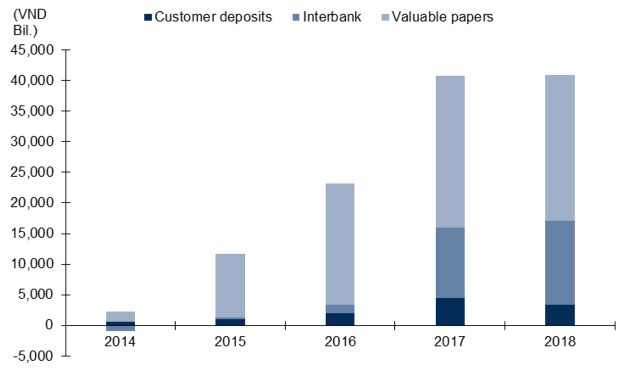
Source: VPB; KBSV Research

Figure 9: A comparison of mobilization structures



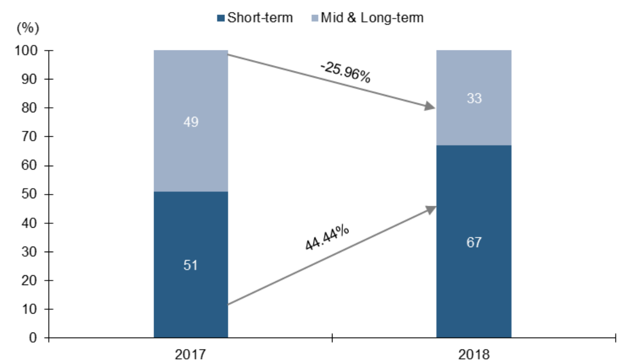
Source: VPB; KBSV Research

Figure 10: FE Credit mobilization structure



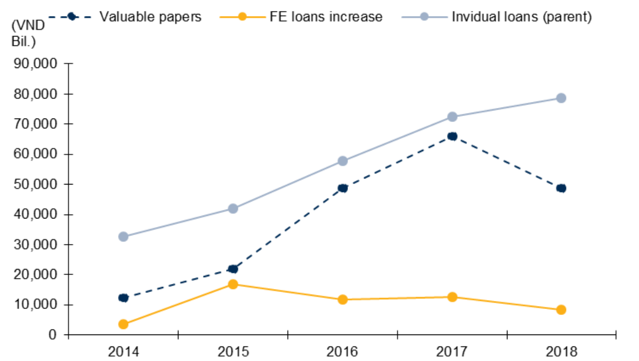
Source: VPB; KBSV Research

Figure 11: Mobilization structure by terms



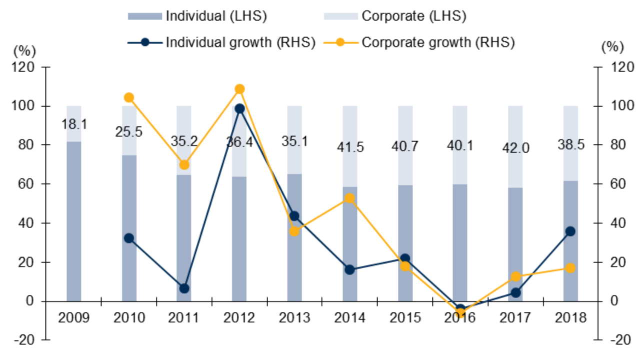
Source: VPB; KBSV Research

Figure 12: Comparison between FE Credit credit and mobilization structure



Source: VPB; KBSV Research

Figure 13: Comparison of mobilization structure by objects



Source: VPB; KBSV Research

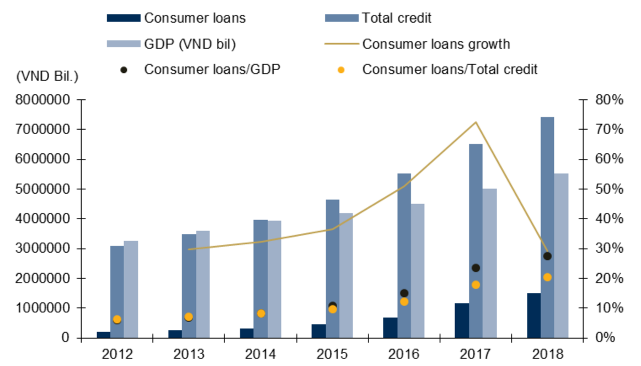
INVESTMENT HIGHLIGHT

Unsecured consumer credit will continue to have a positive growth despite a slowdown

The foundation of unsecured consumer credit with the main purpose of minimizing the "black credit" market, especially in rural area. According to SBV's data and our research, unsecured consumer credit in 2017 in Vietnam accounted for 2.4% GDP, equal to 1.8% total outstanding loans. The official data of 2018 has not been released yet, but we estimate that the two above ratios just inched up from 2 – 5 bps, which means that the market almost did not expand last year. We suppose there are two reasons: 1) More tightening management from the SBV after the booming growth in the past three years; 2) The market absorption showed signs of a standstill.

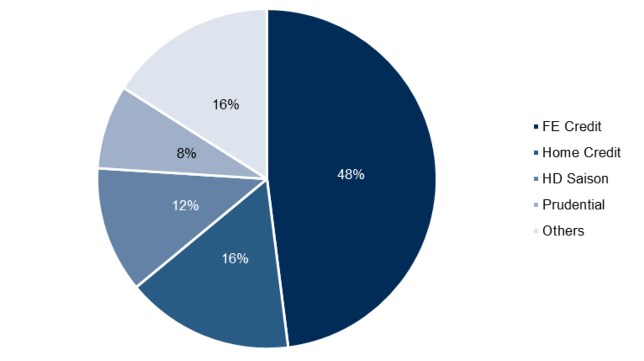
When these above ratios are compared with those in developed markets based on some other criteria such as total consumer credit/GDP ratio (about 26% in 2018), or household credit/GDP ratio (about 60% in 2018), these ratios are still low, which means that the room for development is still large Nevertheless, considering the slowdown in recent years, we believe that the speed of unsecured consumer credit growth in 2019 – 2022 will significantly decrease compared to that in 2014 – 2018, from over 60% to 15 – 30%, depending on each scenario.

Figure 14: Consumer credit growth in Vietnam



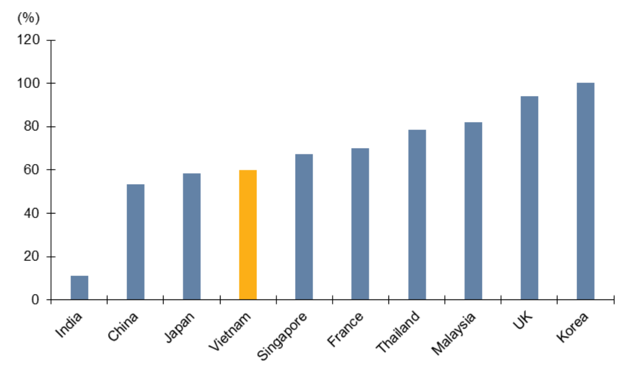
Source: VPB; KBSV Research

Figure 15: Consumer credit market share in 2017



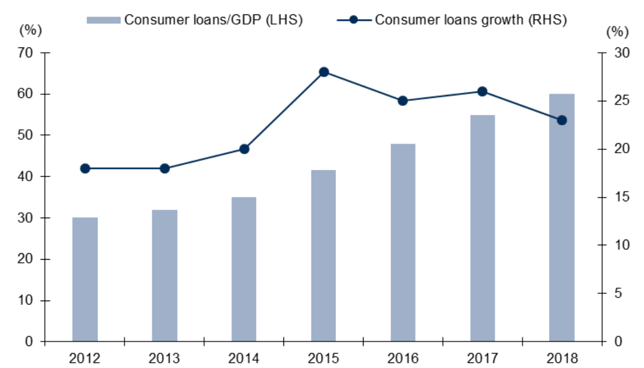
Source: Stoxplus; KBSV Research

Figure 16: Penetration rate of credit for households



Source: KBSV Research; Statista

Figure 17: The growth of credit for households in Vietnam



Source: KBSV Research

FE Credit will continue to maintain the No. 1 position on consumer

Although there has been no official data, with the strong attempts exerted by other competitors and the slowdown in FE Credit, we suppose that the

credit in the future

unsecured market share of FE Credit is only 40%, falling from 50% in the previous two years. The two big competitors against FE Credit are HD Saison and Home Credit, in 2018, some other competitors such as MCredit and some other foreign funded finance companies also saw strong development.

The three main products of consumer credit are cash loans, loans for shopping (electronics, motorbikes, etc.) and credit cards. In particular, the product that is most focused by the companies are cash loans, accounting for 80% in FE Credit, 50% in Home Credit and Mcredit, and about 45% in HD Saison. Therefore, it can be seen that cash lending is the key product that help FE Credit achieve its current position.

The current biggest competitive advantage of FE Credit is its economy of scale, good brand awareness helps increase customer accessibility and reduce operating costs of a lender. As other companies have not focused on rural areas, we believe that this advantage has been benefit the bank on these markets from the past to the future. Meanwhile, the competition in large cities will become increasingly fierce, and the market share will soon be divided to competitors.

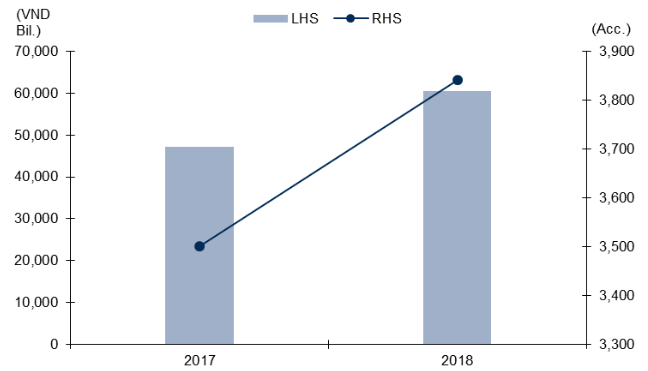
Potential business model, but the risk management procedure is questionable

With more than VND53,270 billion outstanding loans and over 3,800 active accounts late 2018, average loan value/loan number of FE Credit was from VND15 – 20 million. The average interest rate was estimated at 35% per year, which was quite high, but due to the equated monthly installment, the amount (both principal and interest) that customers had to pay each month was around VND1.5 – 2 million. This is a very high cost, but still acceptable, in exchange for current spending needs. We believe that this business model can be expanded because black credit in the localities is still very large, however, keeping a long-term customer (borrowing more than 1 time) is quite challenging at the above cost.

In the first phase of market penetration, FE Credit has chosen a rapid expansion strategy to gain market share, in order to gain the advantage of recognition and economy by scale, accompanied by a somewhat easier lending procedures, and less standardized risk management. However, in this second phase, it will be very difficult for FE Credit to maintain that direction, due to 3 reasons: 1) The economy enters the end of the cycle; 2) FE Credit scale is relatively large; 3) Many official competitors (finance companies) have gradually enhanced their competitiveness.

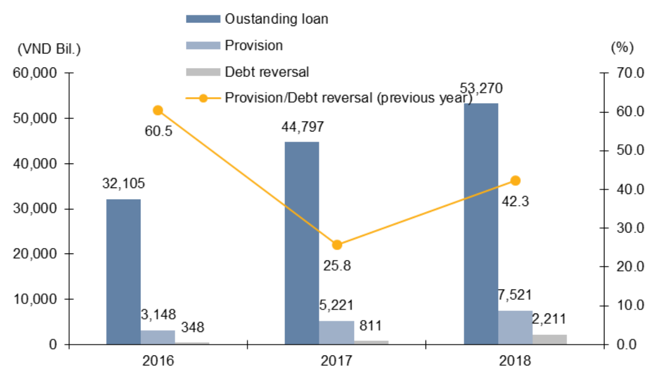
To sum up, although FE Credit still holds the No. 1 position and leaves many competitors far behind, we believe that the growth and market share of FE Credit will decrease slightly in the coming years as the SBV tightens its management and the opponents continue to boost lending more. We believe that FE Credit can grow outstanding loans from 10-20% per year from 2019-2022, based on different scenarios.

Figure 18: Lending criteria of FE Credit



Source: VPB; KBSV Research

Figure 19: Provision and debt reversals of FE Credit



Source: VPB; KBSV Research

Business operation in the parent bank is still stable

Customer outstanding loans in the parent bank late 2018 was VND168,190 billion, in which there was about VND26,600 billion of unsecured loans. We suppose NPLs of this segment were 6% (equal to FE Credit), the total remaining loans will have 2.6% of NPLs. In general, this is a high level compared to others in the sector, which showed that VPB has higher risk appetite than other banks, even in the traditional banking segment.

In addition, NIM of the parent bank was also among Top 3 of the sector (after MBB). However, the different point is that VPB achieved high NIM thanks to high average lending yield (9.5% in 2018), while MBB or TCB have advantages in low input capital. VPB has a high yield thanks to the high allocation for micro enterprises, mortgage lending, and CommCredit. In particular, CommCredit is a strategic segment in the parent bank, but because of its low proportion (2%) and the impact on the whole bank is insignificant, so we will not analyze this segment specifically.

We believe that when Vietnam economy still maintain the positive growth, business performance of VPB will still be ensured due to high risk appetite.

Digitalization is more focused and developed

VPB is stimulating technical application in business activities and operations. There are three particular products:

1) Priority customers, developing products that create added value for high-end individual customers, such as VPBank Diamond's financial management, consulting and services;

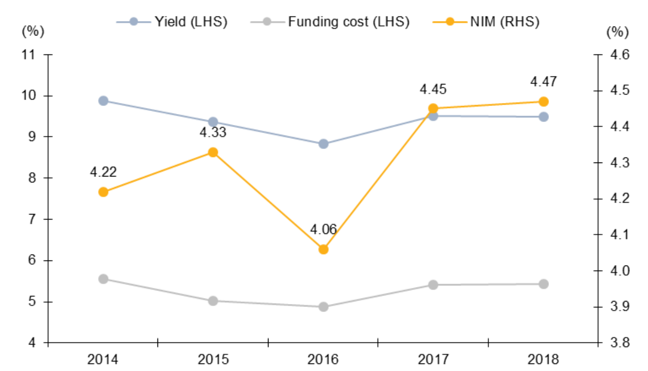
2) Card digitalization, with outstanding product YOLO, aiming to create convenience, shorten the time of customers' transactions (VPB's number of active credit cards until the end of 2018 was 416,000 cards, gaining 40.7% yoy, accounting for 10.4% market share, trading value reached USD1,548 million, up 86.8% yoy, accounting for 18% market share). VPB's proportion of transactions via electronic banking channel reached 93% in 2018;

3) FE Credit, with the advantage of database, is stimulating digitalization with the main purpose on improving customer experience and risk management. Big Data and AI database are being developed well and we expect that FE Credit will become the pioneer in applying the above

technology thanks to available strengths.

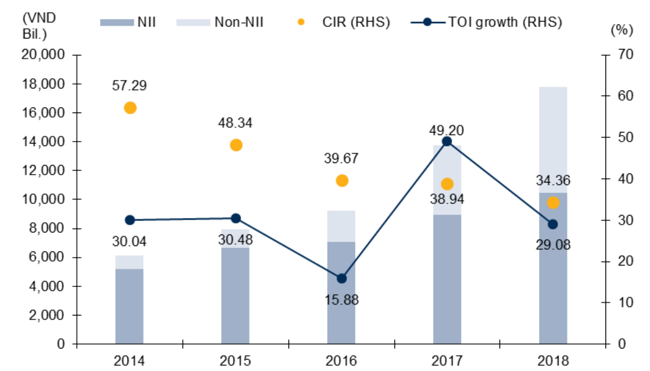
Furthermore, VPB is also one of the leading banks in cooperating with fintechs to search for new products that can support the bank (via start-up ecosystem).

Figure 20: NIM at the parent bank



Source: VPB; KBSV Research

Figure 21: Business performance at the parent bank

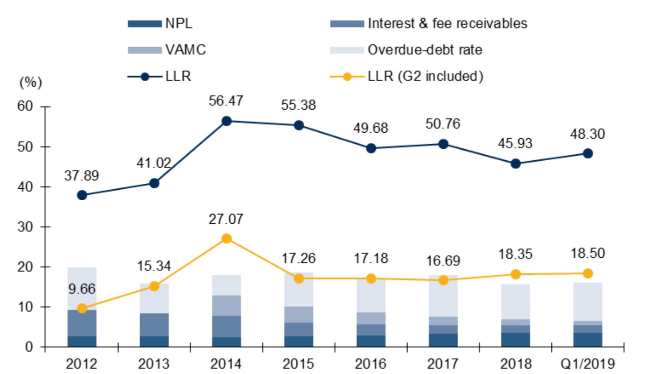


Source: VPB; KBSV Research

However, asset quality adversely affects investment decisions in the next 1-2 years

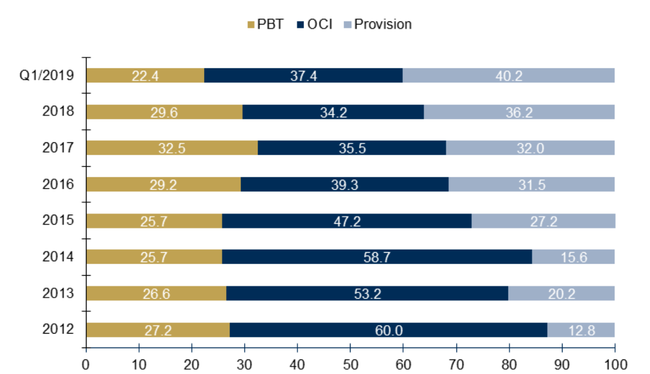
It can be clearly seen that the total problematic asset/total outstanding loan ratio of VPB is the highest level in the sector, while LLR is much lower. This is gradually showing the pressure on the bank's business results in both recent years and the coming years, as the cost of provision escalates. With about 1.42% of VAMC, 3.5% of NPL, 5.26% of Group 2 debt and 1.95% of receivable interest, we believe that the pressure will remain at least for two more years, or even longer if the bank does not have more drastic provision in the short term.

Figure 22: Consolidated asset quality



Source: VPB; KBSV Research

Figure 23: Consolidated EBT structure



Source: VPB; KBSV Research

FINANCIAL ANALYSIS

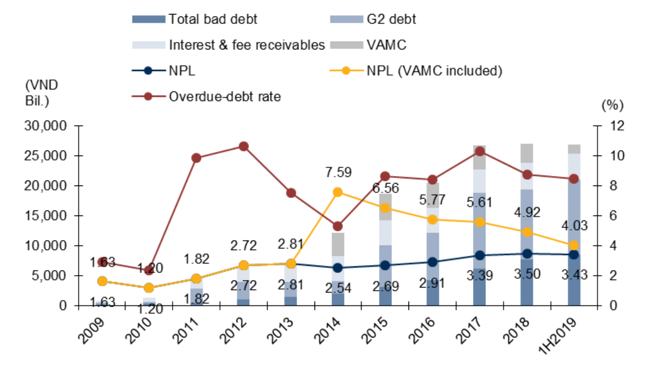
Asset quality

Highest problematic assets/total outstanding loan ratio in the sector due to high-risk business model

NPLs and overdue debts of VCB are currently the highest among listed banks, at 3.51% and 5.27% by the end of 2018. The main reason is the riskier business orientation compared to the average in both FE Credit and the parent bank. NPLs and overdue debts are 5.98% and 16.1% at FE Credit, 3% and 6.71% at the parent bank, which are much higher than the sector's average. There have not been many clues saying these ratios will be improved in a short term, except when VPB has more drastic provision measures than in the past.

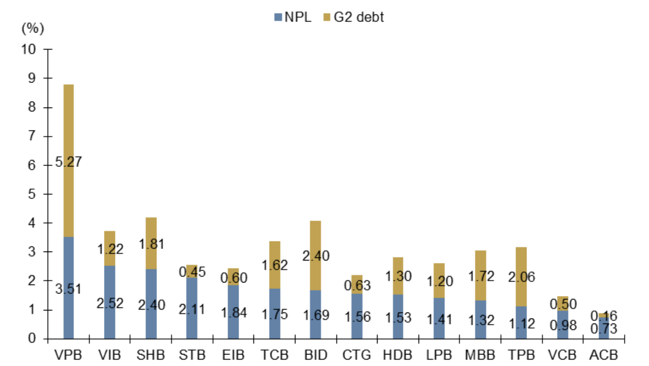
VAMC bonds at the end of 2019 was VND3,161 billion (about 1.42% total outstanding loans.) This is a quite high level, but the good point is the volume of this bond plunged for the first time in 2014, which shows that there is no new debt arising at VAMC. VPB's plan will bring this amount of VAMC bond back to internal market in 2019 to resolve, so NPLs may be affected this year.

Figure 24: Troubled assets in VPB



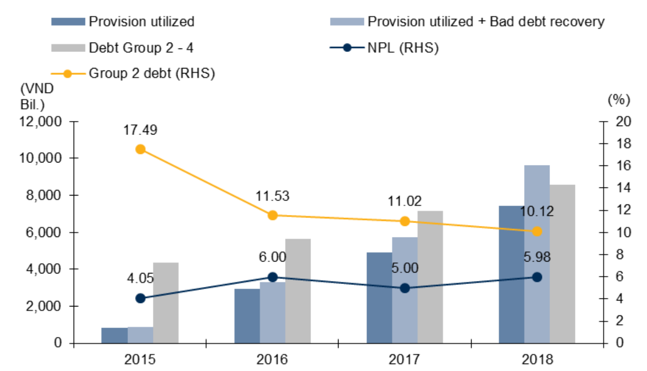
Source: VPB; KBSV Research

Figure 25: Comparison of bad debts among banks



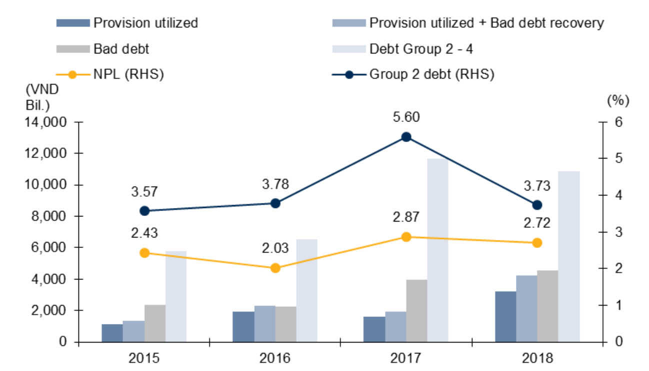
Source: Banks' financial statements; KBSV Research

Figure 26: Asset quality of FE Credit



Source: VPB; KBSV Research

Figure 27: Asset quality of the parent bank

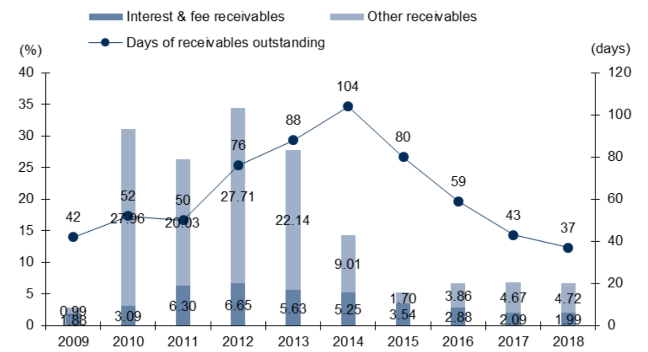


Source: VPB; KBSV Research

The next item to note is other assets. In particular, interest and fee receivables continued to achieve improvements when the number of days payable outstanding is only 37 days (lower than the industry average). However, the risk is increasing again in other receivables, currently accounting for 4.72% of outstanding loans, increasing in the last three years and not being announced clearly.

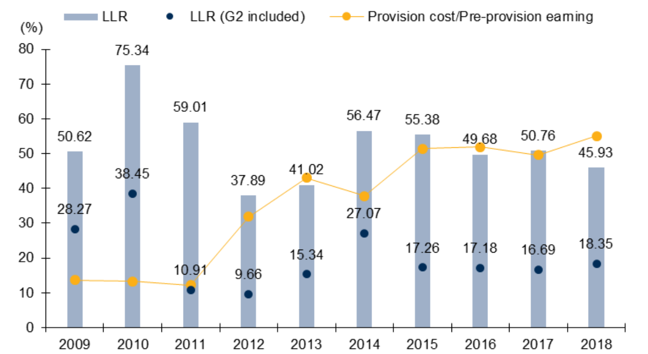
Finally, in terms of provision, in 2018, the total used provisions and recovered bad debts at FE Credit were VND 1,000 billion higher than of total debt from group 2 - 4. This showed that the bank became more prudent, and was also an opportunity to record a large amount of debt reversals in the future. About the parent bank, we have similar assumption that the provision and reversal compared to problematic debt are being improved, and more prudent, but we are still concerned about the large group 2 debt, focusing on the retail segment, and the bank does not have enough provision for this item, which may put pressure on the cost of provision the coming years.

Figure 28: Receivable movements



Source: VPB; KBSV Research

Figure 29: Provision and bad debt recovery



Source: VPB; KBSV Research

Capital Adequacy Ratio (CAR)

CAR was kept at a high level (according to Basel II), but did not totally reflect current risks at FE Credit

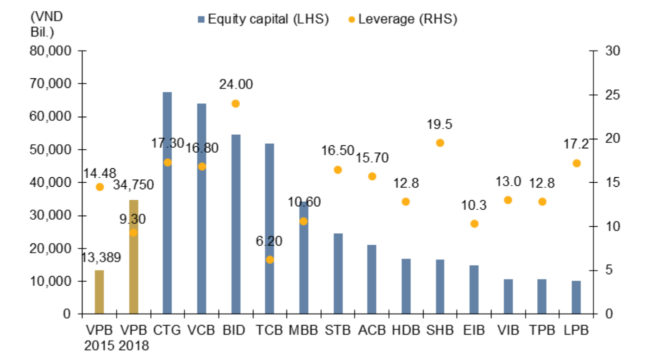
CARs according to the Circular No.36 and Basel II of VPB by the end of Q1/2019 were 13% and 11.1% respectively. Based on these CARs, there are two points:

1) CAR of VPB is currently at a safe level, even when compared to the average of the banking system or the minimum requirements, which showed that VPB has a good capital base. We believe that a big factor that helps VCB has maintained its CAR at the second lowest of the sector (9.3x at the end of 2018), but still achieved high profitability was quick capital turnover of unsecured lending.

2) However, this high ratio may be resulted from the fact that there has not been specific regulations on the calculation risk ratio for VPB's lending model. At the moment, VPB has advantages compared to other banks as it has a relatively low risk ratio thanks to the highly fragmented unsecured credit with other banks. We think that this is true, but only with stricter lending conditions and procedures.

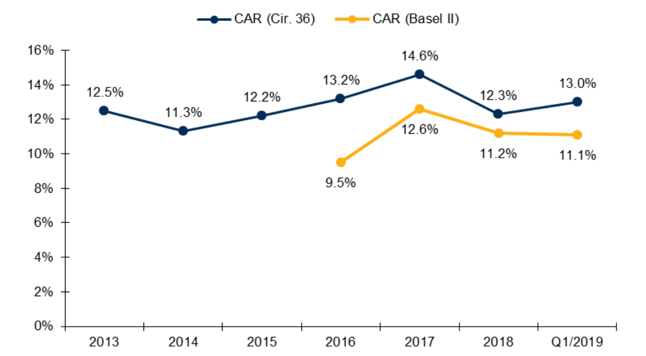
To sum up, the current CAR of the bank does not reflect VPB's risks totally especially in FE Credit, but this ratio is quite safe to be considered in overall.

Figure 30: Owner equity and leverage



Source: Banks' financial statements; KBSV Research

Figure 31: CAR of VPB



Source: VPB; KBSV Research

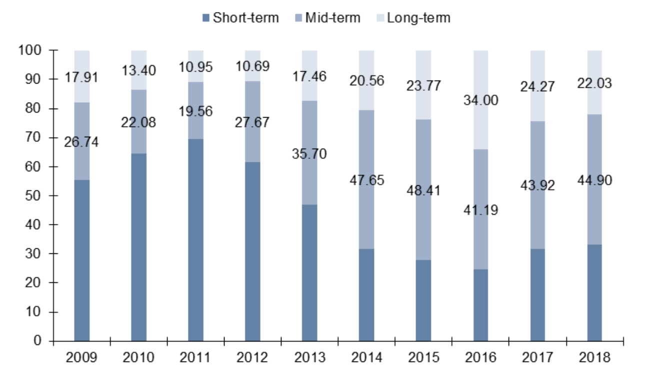
Liquidity

In general, LDR will be ensured and does not have any strong pressure in the short term

Like other ratios, LDR of VPB is also different from others in the banking system due to special business model at FE Credit (LDR is roughly at 100%). However, LDR in the parent bank is still safe, about 71.4% by the end of 2018. Furthermore, we believe that the risk level to VPB compared with other banks based on LDR needs to be adjusted. Accordingly, most of mobilized amount for unsecured lending had mid-terms to long-terms, which is different from short-term lending at commercial banks. Although this would cost more (offset by high lending rates) but more stable, so LDR may be higher to optimize profits.)

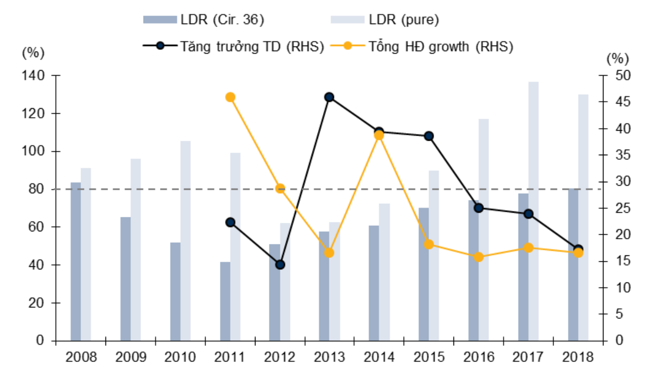
The ratio of assets with good liquidity on VPB's total mobilization, despite falling sharply from 52% in 2017 to 39.5% in 2018, but is at a safe level compared to the system average, equivalent to two other banks, MBB and ACB.

Figure 32: Lending structure by term



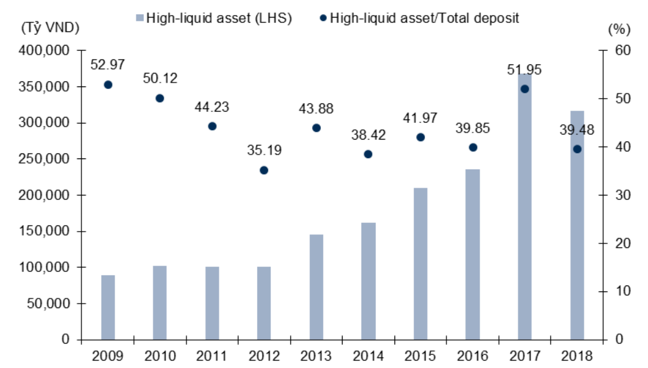
Source: VPB; KBSV Research

Figure 33: LDR movements



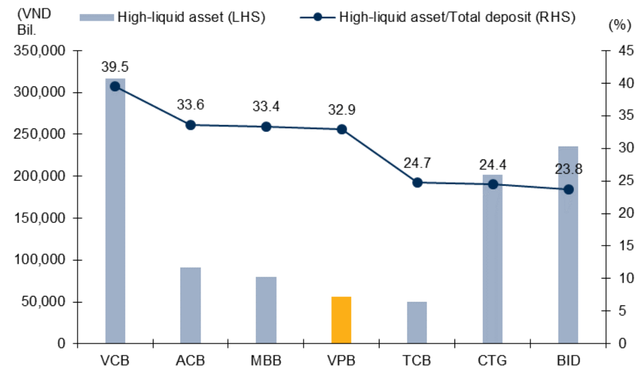
Source: VPB; KBSV Research

Figure 34: Assets with good LDR



Source: VPB; KBSV Research

Figure 35: Comparison of assets with good LDR at banks



Source: Banks' financial statements; KBSV Research

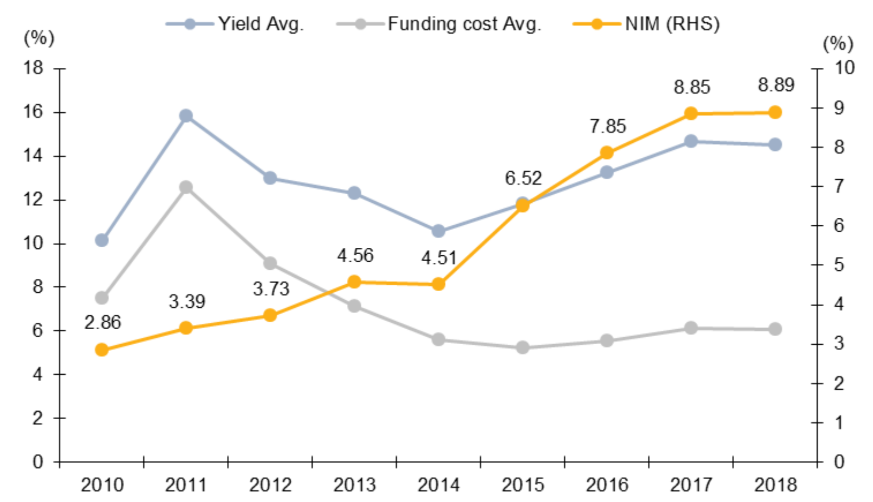
Profitability

NIM of VPB was the highest in the banking sector thanks to high lending yield at FE Credit, but this yield growth tends to slow down as consumer credit was controlled

FE Credit has been expanding its scale since 2014, which helped NIM continuously increase. By the end of 2018, VPB's NIM was 8.95%, superior to all other banks. The main contribution comes from the very high NIM of FE Credit, although it is on the decline but still up to about 34.4% in 2018.

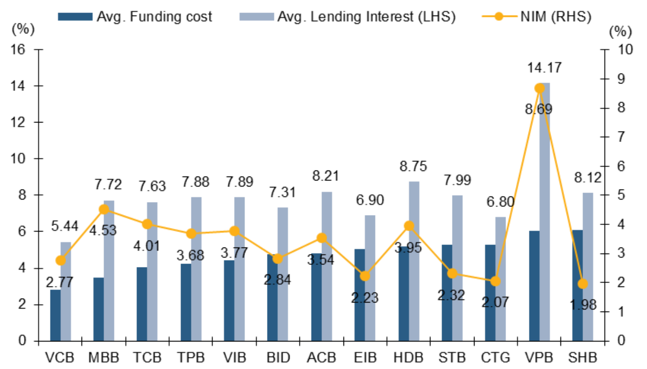
However, 2018 was the first year when VPB saw NIM only increasing slightly, because the output yield almost went flat after gaining for 3 consecutive previous years. This is the main reason for the deceleration of consumer credit and increasing competition with more competitors.

Figure 36: Movements of NIM, yield average, and funding cost average



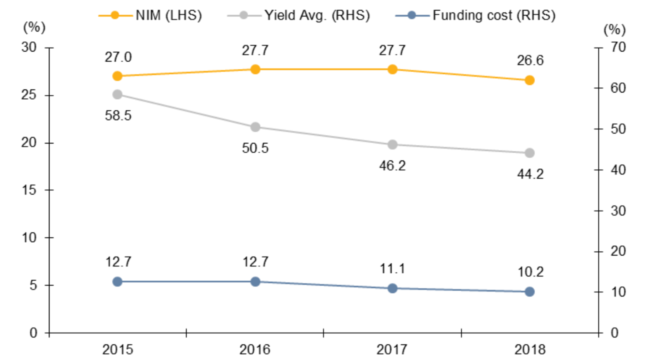
Source: VPB; KBSV Research

Figure 37: Comparison between NIM, yield average, and funding cost average



Source: Banks' financial statements; KBSV Research

Figure 38: NIM movements at FE Credit



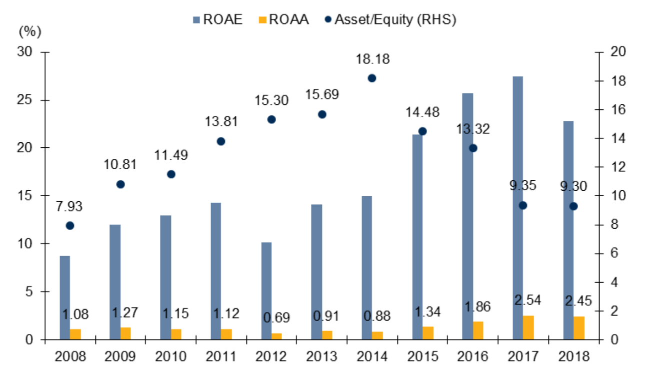
Source: VPB; KBSV Research

The pressure from provision cost has a strong impact on profitability

After a period of growth along with relatively low provision cost, ROA and ROE have continuously climbed (used to reach over 27%), VPB's profitability has started to show signs of a decline when growth momentum narrowed, while large cost of provision gradually appeared. ROA dropped sharply from 2.54% in 2017 to only 2.21% in Q1/2019, causing ROE to decrease from 27.5% to 19.7%.

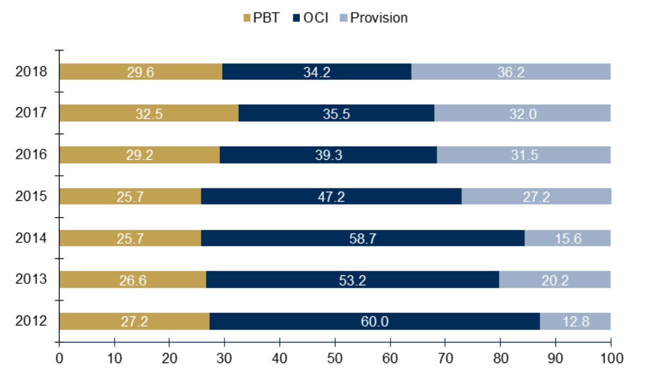
Although VPB still has a lot of room to expand credit when leverage is still low, but under tougher market conditions and requires accelerating problematic asset handling, we believe that profitability of VPB will not be improved in the next two years.

Figure 39: EBT structure



Source: VPB; KBSV Research

Figure 40: EBT structure



Source: VPB; KBSV Research

Updated business performance in and 1Q/2019

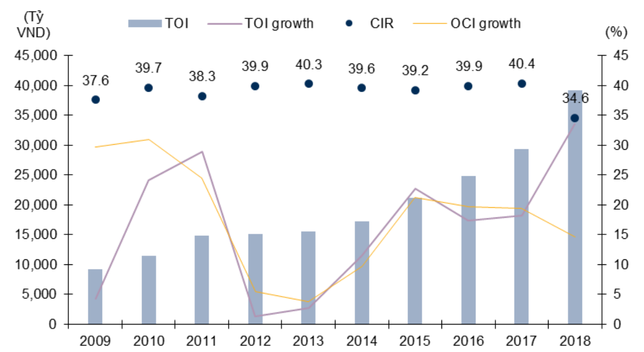
VPB More tightening control of consumer credit by the SBV and the pressure from provision continued to affect VPB business performance

At the end of Q1/2019 (compared to the end of 2018): Total credit increased by 6.8% with over 35% (about VND 6,000 billion) from enterprises, more than two times higher than the sector's credit growth (3.2%). This growth was significantly supported by the parent bank with an increase of 8% yoy. Customer mobilization in Q1/2019 rose by 10.1% but total mobilization fell slightly by 1% due to the absence of SBV loans and reduction of debt on the market 2.

Regarding FE Credit, although the total outstanding loan only inched up from VND53,270 billion at the end of the year to VND54,662 billion, the total disbursed amount was still quite positive, which reached roughly VND17,000 billion (gaining 22% QoQ and equal to the level in Q4/2018) with about 80% for available customers. NII hit VND3,821 billion, climbing 16% QoQ, TOI was VND4,187 billion, up by 13% QoQ, but EBT was only VND764 billion, decreasing 17.5% YoY due to surging provision cost.

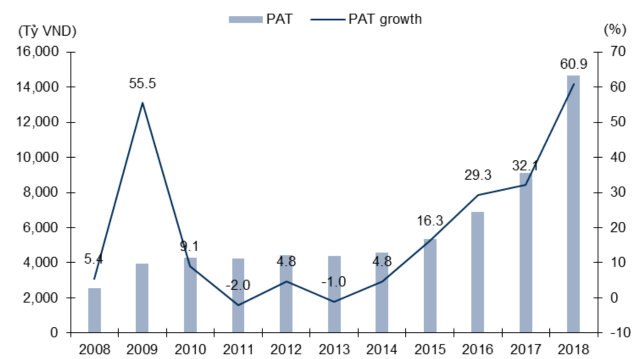
To sum up, compared to Q1/2018, interest income increased by 16.9% but NII increased only 12.6%, indicating that the pressure on NIM is growing. Non-NII decreased by 28% against Q1/2018 because there was no extraordinary income from divestment of subsidiaries, so TOI only increased slightly by 3.95%. However, on the basis of relative comparison, TOI still increased by over 15%. CIR also went up from 34.2% in 2018 to 37.4% because of the above reasons. Provision cost/pre-provision cost increased sharply from 55% to 64.3% in Q1/2019 due to a sharp increase in the cost of provision at both the parent bank and FE credit, as well as speeding up the VAMC process. We think this trend will remain in the remaining quarters of 2019 and will significantly affect the bank's earnings this year.

Figure 41: Some momentum indicators of VPB



Source: VPB; KBSV Research

Figure 42: NPAT changes



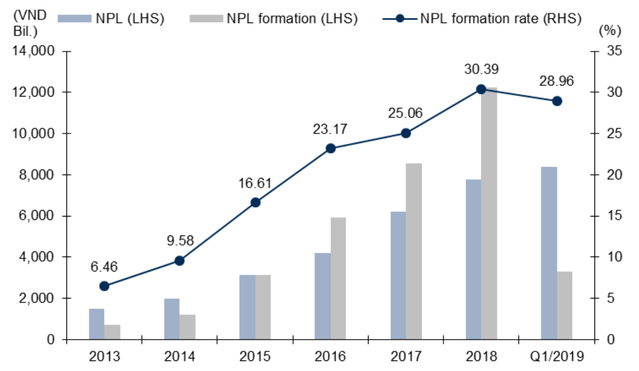
Source: VPB; KBSV Research

The proportion of VAMC has been decreased since 2018, which are positive signs. At the end of Q1/2019, VPB provisioned nearly enough of the year target for VAMC, but we think that the bank will continue to boost the provision in the coming quarters as well as in 2020 to definitely resolve this item.

Meanwhile, the remaining items including bad debt and debt group 2 have not shown a clear improvement, this will also put a great pressure on the cost of provision in the coming time.

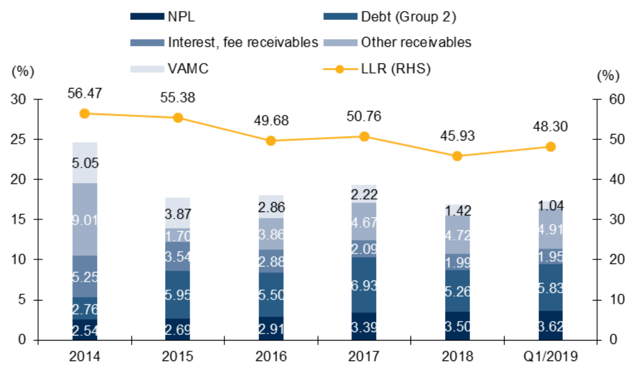
The new NPL ratio has decreased slightly in Q1/2019 after continuously increasing since 2014 but for the whole year, the reason for the bad debt formation rate at FE Credit decreased while the parent bank still increased strongly. However, we believe that this ratio will continue to increase throughout the year, because the amount of debt in group 2 is still quite large and there is no sign of reduction. There is also a positive point that the provision rate tends to increase more strongly, we believe that if VPB is more aggressive in provisioning in the next 1-2 years, it will help reduce considerable pressure for the future.

Figure 43: NPL and NPL formation rate



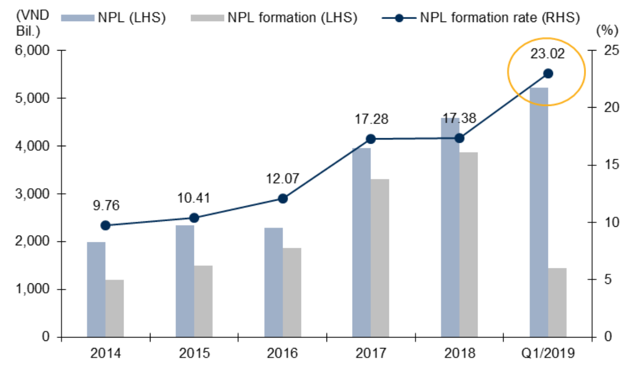
Source: VPB; KBSV Research

Figure 44: Asset quality by Q1/2019



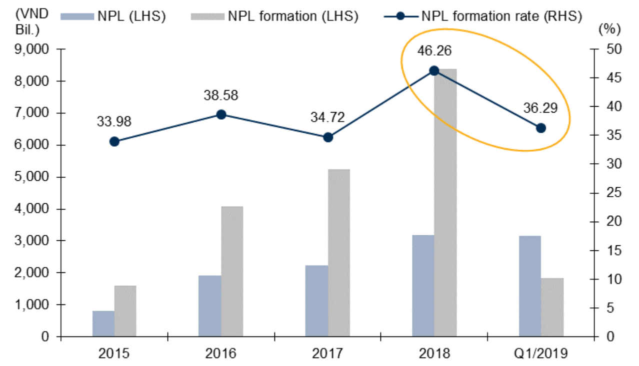
Source: VPB; KBSV Research

Figure 45: NPL and NPL formation rate at the parent bank



Source: VPB; KBSV Research

Figure 46: NPL and NPL formation rate at FE Credit



Source: VPB; KBSV Research

2019 FORECAST BUSINESS PERFORMANCE & VALUATION

2019 Forecast business performance

Based on the forecast saying that Vietnam's macroeconomic situation will continue to be stable, we believe that credit growth of VPB in 2019 will be 15%, equivalent to the target assigned by the SBV. Consolidated customer credit growth will reach 12.8%, the rest may come from corporate bonds. Credit growth of FE Credit is likely to be limited at 12%, lower than other smaller companies in the same sector such as HD Saison, Home Credit or MCredit.

NIM will go down slightly by 8bps in 2019

After staying flat in 2018, NIM is supposed to keep decreasing slightly by 8bps in 2018 due to slow growth of FE Credit and higher competition affecting lending rates. In the next two years, it is likely that NIM will be significantly reduced due to economic cycle factors. However, after that, NIM may increase again when the economy recovers.

Non-NII will still stay as high as the level in the same period last year although there is no extraordinary profit anymore

In 2019, VPB will no longer have one-off profits from its exclusive insurance contracts like in the previous two years. In addition, we do not make any assumption for incomes from debt selling due to insufficient information. Although we did not include these two extraordinary profits, we believe that Non-NII will still be high as in 2018 thanks to two main factors: 1) Service profit maintained a good growth thanks to payment and insurance services; 2) Expectation of debt recovery interest is high, based on prudent provision moves in previous years and improvements in bad debt recovery activities. In previous year, VPB sold bad debt recovery rights, which is likely to be repeated in 2019.

In short, our forecast on Non-NII will increase slightly by 2% compared to that in 2018.

CIR may be adjusted to rise slightly compared to that in 2018

We believe that the expansion of staff size will slow down at FE Credit and the parent bank when the bank has gained advantages in scale, and introduced new technologies. Since then, the expansion of OPEX will be better controlled. However, due to the adjustment for the extraordinary profit in 2017 and 2018, CIR is likely to increase slightly to 34.7% in 2019 and 36.1% in 2020.

The pressure on provision cost will still increase

Although there are positive signs in the VAMC item in the past, the pressure of provision cost will still be quite high in the next 2-3 years when the debt formation rate is increasing rapidly, especially in FE Credit.

We forecast the provision expense/pre-provision ratio of 2019 and 2020 will hit 58.7% and 62.2% respectively. This will be the biggest impact on VPB's short to medium-term business results.

Based on our assumptions, we expect that EBT of VPB in 2019 will reach VND 9,476 billion, increasing slightly by 3% yoy and nearly equal to the profit plan of 2019 of the bank’s BOM of VND 9,500 billion. ROE will continue to decline to 19.8%. BVPS forward 2019 may reach VND16,611 per share in case there is no issuance of capital raise this year.

Valuation

We used two valuation methods of P/B and Residual Income Model (RI) to find out the reasonable price for VPB shares.

With the above assumptions, P/B forward in 2019 = 1.11x; P/B trailing = 1.35x, which is the 1st and 2nd lowest among Vietnamese banks we choose to compare. VPB has gone through a period of booming growth (P/E valuation phase can be used), now is the time when the bank is focusing on restructuring its assets, improving capital base and developing new business model on digital technology platform. Although the valuation is relatively low even when compared to the Vietnamese market or other banks in similar markets, asset quality and new growth motivation are not clear enough, which makes VPB's target valuation not be improved in the short term.

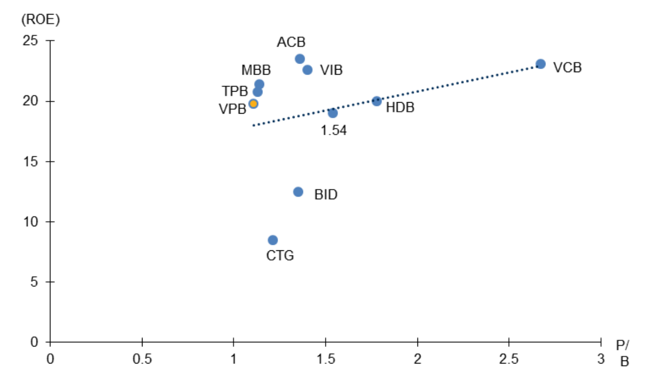
We suggest that 1-year P/B target of VPB should be 1.2x, 12.4% decreasing compared to the level of (-1 SD of the past P/B average) due to asset quality issues, equivalent to the price for the next 1 year at about VND 20,000 per share, 8.1% higher than the market price at the time of valuation. At the moment, we do not put the P/E valuation into the recommendation.

Table 1: Valuation indexes of some banks in Vietnam

Ticker	Name	Mkt Cap (VND)	ROE (%)	P/B trailing	P/B forward	P/E trailing	P/E leading	Diluted EPS (5Y Avg. growth %)
ACB VN	ASIA COMMERCIAL BANK	39,785	27.73	1.77	1.36	7.25	5.94	35.2
MBB VN	MILITARY COMMERCIAL JCB	48,080	19.41	1.42	1.14	7.84	5.92	7.13
TCB VN	VIETNAM TECHNOLOGICAL & COMM. BANK	94,583	21.53	1.86	1.54	11.37	9.03	26.7
BID VN	BANK FOR INVT. & DEVP OF VIETNAM JSC	127,518	14.6	2.17	1.35	17.33	20.49	8.89
HDB VN	HDBANK	31,196	20.3	2.00	1.78	10.98	10.31	6.48
TPB VN	TIEN PHONG COMMERCIAL JSB	18,075	20.8	1.70	1.13	7.97	6.36	25.12
VIB VN	VIETNAM INTERNATIONAL JSB	14,881	22.6	1.37	1.40	7.16	6.22	8.83
CTG VN	VIETNAM JSCB FOR INDUSTRY & TRADE	87,128	8.3	1.24	1.21	7.16	16.78	-1.34
VCB VN	BANK FOR FOREIGN TRADE OF VIETNAM JSC	250,720	25.18	3.55	2.67	15.46	13.38	16.6
VPB VN	VIETNAM PROSPERITY JSB BANK	55,277	22.8	1.35	1.11	6.36	6.17	10.52
Average		**76,724**	**20.33**	**1.84**	**1.47**	**9.89**	**10.06**	**14.41**

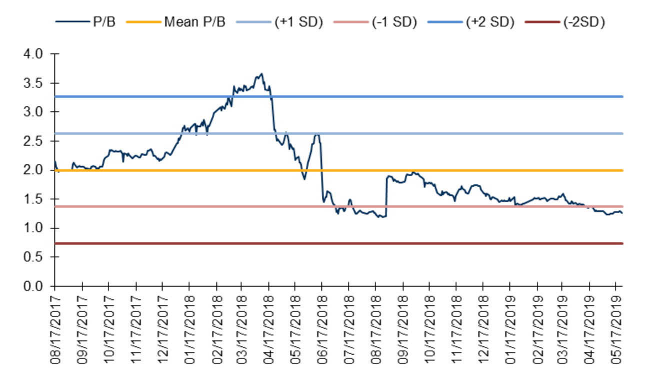
Source: Bloomberg; KBSV Research

Figure 47: Comparison of valuation forward 2019



Source: VPB; KBSV Research

Figure 48: History of P/B valuation of VPB



Source: VPB; KBSV Research

However, based on the viewpoint if VPB strongly sets provision in the next 1-2 years, resolving weak assets totally, it will then have a positive impact on business results in the future. Applying the 3-period surplus profit method, we set a valuation of VND 25,400 / share, 37.3% higher than the market price at the time of valuation. However, to expect this target price as we mentioned, it will take 1-2 years, after VPB resolves problematic property, and reflects the impacts from economic cycle.

Table 2: Valuation results according to RIM

VND Bil.		2019F	2020F	2021F	2022F	2023F
PAT		7,581.00	7,332.00	9,906.00	10,490.90	12,919.50
Residual income		2,469.26	1,149.98	2,028.80	1,208.60	2,147.97
Cost of Capital R	14.71%					
g	5.00%					
Terminal value	23,227.28					
Total present value (PV)	64,127.55					
VPB instrinsic value (VND/share)	**25,347.2**					

Source: KBSV Research

INVESTMENT VIEWPOINT

We are still positive about consumer credit growth in the long term, based on low penetration rate compared to other developing countries and very high non-bank credit demand in Vietnam. Although the competition will become much fiercer due to some new competitors, FE Credit still maintains its No.1 position thanks to the strong competitive advantage of large operating scale, customer base, and good ability to operate in a large scale. Increasing focus on risk management based on available data analyzing technology and database, we believe that asset quality of FE Credit will be gradually improved, and enhance trust.

Additionally, the parent bank, VPB also showed its ability to operate business stably, with the main focus on retail credit, SMEs lending and private consumption (buying houses, cars, and credit card). Digital banking activities are being focused to improve usability and create more added value for customers. We evaluate VPB as one of the banks doing the best in this section.

Considering cyclical factors, we think that banks will be affected in general. However, the level of impact on VPB will not be much stronger than the case of no cyclical factors, thanks to the dispersion and fragmentation in loans of and FE Credit. Besides, good capital base (high CAR and low leverage) will also partly guarantee the bank against the shocks of the economy.

Finally, from an investment viewpoint, although the bank has a relatively low P/B valuation in the banking sector in Vietnam, we believe that in the next 1-2 years, VPB will still cannot get a better valuation, because the amount of problematic assets to be handled is still quite large, thereby adversely affecting the business results of the bank. In the short term, we can expect positive impacts from VPB's successful mobilization of capital through the issuance of bonds on the international market. In the long term, if VPB performs well in the asset settlement in the coming time, we think that VPB's valuation will be much better, as shown in the surplus profit valuation method. We recommend to **HOLD** VPB shares at the current market price.

APPENDIX

Balance Sheet

(VND Bil.)	2015	2016	2017	2018
TOTAL ASSETS	193,876.43	228,770.92	277,752.31	323,291.12
Cash and precious metals	1,632.43	1,727.36	2,574.28	1,855.47
Balances with the SBV	2,261.50	2,982.59	6,460.80	10,828.57
Placements with and loans to other credit institutions	14,599.68	9,388.91	17,520.03	16,571.49
Balances with other credit institutions	8,729.75	4,089.18	15,218.72	15,337.63
Loans to other credit institutions	5,870.66	5,300.46	2,302.04	1,233.86
Allowance for balances with and loans to other credit	-0.73	-0.73	-0.73	0.00
Trading securities, net	2,043.65	2,952.21	1,424.85	4,202.41
Trading securities	2,046.74	2,953.77	1,424.85	4,240.74
Less: Provision for diminution in value of trading secu	-3.09	-1.56	0.00	-38.33
Derivatives and other financial assets	0.00	0.00	0.00	0.00
Loans and advances to customers, net	115,062.47	142,583.25	179,518.81	218,395.22
Loans and advances to customers	116,804.25	144,673.21	182,666.21	221,962.00
Less: Provision for losses on loans and advances to	-1,741.77	-2,089.96	-3,147.40	-3,566.77
Debts purchase	0.00	0.00	0.00	0.00
Debts purchase	0.00	0.00	0.00	0.00
Allowance for losses on debts purchase	193,876.43	228,770.92	277,752.31	323,291.12
Investment securities	47,729.48	55,339.99	53,558.05	51,926.42
Available-for-sales securities	43,950.62	51,948.66	50,384.79	49,417.16
Held-to-maturity securities	4,520.64	4,136.20	4,151.13	3,564.93
Less: Provision for diminution in value of investment s	-741.78	-744.87	-977.87	-1,055.67
Investment in other entities and long term investments	383.19	1,389.79	328.78	329.65
Investment in subsidiaries	0.00	0.00	0.00	0.00
Investment in associate companies	0.00	0.00	0.00	0.00
Investments in joint-venture	0.00	0.00	0.00	0.00
Investments in associates	0.00	0.00	0.00	0.00
Other Long-term investments	322.98	299.37	194.60	227.60
Provision for long-term investments	-0.47	-76.44	-42.10	-36.95
Fixed assets	509.57	624.20	808.49	1,963.10
Investment properties	27.60	27.16	0.00	0.00
Other assets	9,687.54	12,922.33	15,734.51	17,357.78
Receivables	1,985.97	5,588.81	8,539.53	10,482.28
Accrued interest and fee receivables	4,133.76	4,165.58	3,812.02	4,427.77
LIABILITIES AND SHAREHOLDER"S EQUITY				
Total liabilities	180,487.51	211,593.39	248,056.60	288,541.05
Due to Gov and Loans from SBV	4,821.06	1,103.69	26.02	3,781.34
Deposits and Loans from other credit institutions	17,764.43	28,835.90	38,063.85	54,231.45
Deposits from other credit institutions	9,603.16	13,437.11	7,834.38	21,145.19
Loans from other credit institutions	8,161.27	15,398.79	30,229.47	33,086.26
Deposits from customers	130,270.67	123,787.57	133,550.81	170,850.87
Derivatives and other financial liabilities	131.76	191.33	160.47	18.57
Funds received from Gov, international and other inst	383.19	1,389.79	328.78	329.65
Convertible bonds/CDs and other valuable papers is	21,859.94	48,650.53	66,104.61	48,658.04
Other liabilities	5,256.45	7,634.60	9,822.08	10,671.13
Shareholder"s equity	13,388.92	17,177.53	29,695.71	34,750.07
Capital	9,345.33	10,469.86	21,572.34	24,096.96
Charter capital	8,056.47	9,181.00	15,706.23	25,299.68
Fund for basic construction	0.00	0.00	0.00	0.00
Share premium	1,288.86	1,288.86	5,866.11	1,289.00
Treasury shares	0.00	0.00	0.00	-2,491.72
Preferred shares	0.00	0.00	0.00	0.00
Other capitals	0.00	0.00	0.00	0.00
Reserves	1,324.78	2,950.19	3,558.27	5,465.88
Foreign currency difference reserve	0.00	0.00	0.00	0.00
Difference upon assets revaluation	0.00	0.00	0.00	0.00
Retained Earnings	2,718.82	3,757.47	4,565.11	5,187.23
OFF BALANCE SHEET				
Contingent liabilities	16,250.59	17,953.89	11,594.42	0.00
Letters of credit (L/C)	6,326.99	6,356.32	0.00	13,880.64
Credit guarantee	9,923.61	11,597.57	11,594.42	0.00
Credit commitments	43,637.95	41,998.30	92,812.14	13,860.02

Income Statement

(VND Bil.)	2015	2016	2017	2018
Interest and Similar Income	18,758.80	25,631.12	34,133.37	40,280.21
Interest and Similar Expenses	-8,405.36	-10,463.26	-13,518.95	-15,578.64
Net Interest Income	10,353.44	15,167.86	20,614.43	24,701.58
Fees and Commission income	1,597.31	2,114.83	3,210.07	3,818.80
Fees and Commission expenses	-712.65	-1,261.91	-1,748.53	-2,206.30
Net Fee and Commission Income	884.67	852.93	1,461.54	1,612.50
Net gain/(loss) from foreign currency and gold dealin	-290.47	-318.96	-158.84	-103.75
Net gain/(loss) from trading of trading securities	44.59	-149.38	179.64	-56.82
Net gain/(loss) from disposal of investment securitie	27.97	91.87	339.48	250.06
Other incomes	957.36	1,450.89	3,208.78	5,363.87
Other expenses	-82.29	-232.32	-672.50	-682.61
Net Other income/(expenses)	875.07	1,218.57	2,536.28	4,681.26
Dividends income	171.05	0.87	53.57	0.85
Total operating income	12,066.31	16,863.76	25,026.09	31,085.66
General and Admin expenses	-5,692.47	-6,621.35	-8,894.97	-10,633.92
Operating Profit Before Provision for Credit Losses	6,373.84	10,242.41	16,131.12	20,451.74
Provision for credit losses	-3,277.64	-5,313.09	-8,001.06	-11,253.23
Profit before tax	3,096.20	4,929.31	8,130.06	9,198.51
Corporate income tax - current	-700.60	-994.27	-1,689.30	-1,842.94
Corporate income tax - deferred	0.26	0.00	0.00	0.00
Corporate income tax	-700.33	-994.27	-1,689.30	-1,842.94
Net profit for the year	2,395.87	3,935.05	6,440.77	7,355.57
Minority interest	0.00	0.00	0.00	0.00
Attributable to parent company	2,395.87	3,935.05	6,440.77	7,355.57
Basic EPS attributable to the equity holders (VND)	3,072.00	4,485.00	4,564.00	3,025.00

Financial summary

	2015	2016	2017	2018
NII	10,353	15,168	20,614	24,702
TOI	12,066	16,864	25,026	31,086
Protfit after tax	2,396	3,935	6,441	7,356
Total Asset	193,876	228,771	277,752	323,291
Shareholder"s equity	13,389	17,178	29,696	34,750
Loans and advances to customers	116,804	144,673	182,666	221,962
Deposits from customers	130,271	123,788	133,551	170,851
Profitability				
NIM	6.52%	7.85%	8.85%	8.89%
Average Lending Interest	15.20%	16.00%	17.60%	17.10%
Average Funding Cost	4.90%	4.80%	5.10%	5.10%
ROAA	1.34%	1.86%	2.54%	2.45%
ROAE	21.42%	25.75%	27.48%	22.83%
Leverage ratio	14.5	13.3	9.4	9.3
Asset Quality				
NPL	2.69%	2.91%	3.39%	3.50%
LLR	55.38%	49.68%	50.76%	45.93%
LDR	70.20%	74.10%	77.80%	80.40%
Overdue debt rate	5.95%	5.50%	6.93%	5.26%
Provision cost/Pre-provision profit	51.42%	51.87%	49.60%	55.02%
Capital Adequacy				
CAR	12.20%	13.20%	14.60%	12.30%
Shareholder"s equity/Total Asset	6.91%	7.51%	10.70%	10.75%
Liquidity				
LDR	70.20%	74.10%	77.80%	80.40%
Customers loans/Deposits from Customers	89.66%	116.87%	136.78%	129.92%
Operating Efficiency				
CIR	47.2%	39.3%	35.5%	34.2%
Valuation Metrics				
BVPS	16,619	18,710	18,907	13,735
EPS	2,974	4,286	4,101	2,908
P/B	1.56	1.49	1.42	1.42
P/E	15.03	13.81	12.27	7.70

Source: Fiinpro, KBSV

Investment portfolio recommendations

Buy: +15% or more

Hold: between +15% and -15%

Sell: -15% or less

DISCLAIMER

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