Vietnam Prosperity Joint Stock Commercial Bank (VPB: HOSE)

MARKET PERFORM – 1Y Price Target: VND 25,020

Current price: VND 22,800

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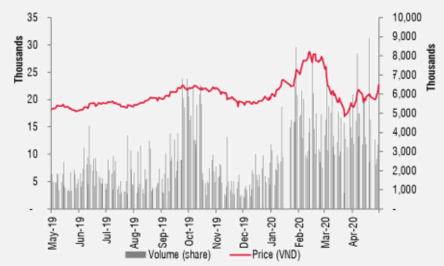
FINANCIALS - VIETNAM

AM NOTE

Key figures

Market cap (USD mn)	2,377
Market cap (VND bn)	55,581
Outstanding shares (mn)	2,438
52W high/low (VND 1,000)	29.3/16
Average 3M volume (share)	4,425,895
Average 3M value (USD mn)	4.30
Average 3M value (VND bn)	100.49
Foreign ownership (%)	29.38
State ownership (%)	0

VPB Price & Trading Volume



Source: Bloomberg

Company Snapshot

Vietnam Prosperity JSC Bank (VPB) was founded in Aug 1993 with a charter capital of VND 20bn. This Hanoi-based bank is ranked among the top private banks in Vietnam in terms of scale and profitability. It comprised 2.7% of total assets in the Vietnam banking system, and 2.6% of the total credit market in 2016 with a network of 51 branches and 163 transaction offices. VPB delivered the highest profitability among listed banks with a 2016 ROAE of 25.7%.

Management expects flat 2020 profit

What's new?

VPB held an analyst meeting on May 5th 2020, which provided us with useful information on the current situation of the bank, as well as its FY2020 prospects.

Change in loan disbursement policy

VPB will reduce its exposure to the 3 hardest hit segments that the Bank services; micro-SME, hospitality, and consumer finance. Since the 3rd week of March, VPB has applied credit tightening measures to mitigate potential losses, particularly in these segments. Specifically, the bank will take action to halt new lending to new bank clients, and focus on low-risk existing customers that operate in industries which are not impacted by the pandemic. These measures are to be applicable for 3 months. The initial results for such change was a higher growth in secured loans (+11.5% YTD) as compared to unsecured loans (-0.5% YTD) at the end of 1Q 2020.

Support to clients

VPB has been restructuring loans for clients impacted by Covid-19, as according to Circular 01. Up to Apr 29th, the bank had restructured loans for 11,895 customers (1.8% of total bank customers), with an outstanding loan balance of VND 11.8 tn (5% of total lending portfolio). The restructuring period is to last for 3 months, and the bank expects 70-80% of their impacted clients to recover if the pandemic can be controlled by the end of 2Q 2020, which looks likely (at least in the case within Vietnam).

According to management, VPB has gone through its peak time in terms of restructuring applications. In the worst case, they believe that total restructured loans would not exceed 6-7% of total outstanding loans.

2020 guidance

VPB has considered different scenarios regarding the development of Covid-19 and the bank's operations. Accordingly, for the scenario where the pandemic becomes contained by 2Q 2020, the parent bank and FeCredit is expected to post a respective VND 6.71 tn (+15.5% YoY) and VND 3.5 tn (-21.9% YoY) pretax profit. This translates into a consolidated pretax profit of VND 10.214 tn, down by -1.1% YoY. For the best and worst case, pretax profit would exhibit a bidirectional variance within ± a 10-15% range of the base case target. Initially, VPB set a 25-30% YoY growth of pretax profit for the parent bank, and a 40% YoY PBT growth for FeCredit.

What's the impact

As the meeting has shed some light on the size of the impacted loan book as well as the bank's recent approach toward lending, we revise our earnings estimate accordingly. Our pretax forecast for VPB is VND 9.626 tn (-6.9% YoY) for 2020, and VND 11.257 tn (+16.9% YoY) for 2021.

What we recommend

With the new estimates, the ROE of the parent bank is projected to be 16% for 2020, which leads us to apply a target P/B ratio of 1x. For FeCredit, the residual income model and P/B method resulted in a valuation equivalent to a P/B ratio of 1.68x. On a consolidated basis, our revised 1-year target price for the VPB stock is VND 25,020. As our target price offers +9.7% upside potential from current levels, we therefore reiterate our Market Perform rating. The key upside surprise to our call outside our immediate expectations would be an earlier-than-expected containment of Covid-19 (before the end of Q2 both within Vietnam and at least regionally), and a better recovery rate in relation to restructured loans. The key downside risk to our call would be a prolonged pandemic situation, which would trend down our estimates potentially lower than the aforementioned forecasts.

Other updates

Management also provided rationale for recent announcements that the Bank has made recently. For background information, VPB recently issued a document seeking shareholder approval for various measures, including: (1) a share buy-back of up to 5% outstanding shares, (2) a foreign ownership limit (FOL) lock at 15% from the current level of 22.77% and (3) a buy-back of $300 mn worth of international bonds issued in July 2019.

The share repurchase was rationalized to shareholders to be in their best interest, and would not be a move to impact the capital strength of VPB. According to VPB estimates, the buyback (worth a total of VND 1.5 tn based on current market price) would reduce CAR by 34 bps to roughly 10.8%. Meanwhile, management essentially stated that the downward adjustment in the FOL would somehow create more room for strategic investors in the future.

Under our point of view, while the buyback might provide certain support to the stock price, we do not appreciate it in term of the bank's capital strength and longer-term market capitalization viability. This concern is particularly a sticking point at this juncture of time uncertainty reigns in general among global markets.

Estimates revision

For 2020, pretax profit is estimated at VND 9.626 tn (-6.9% YoY), which rests on the following rationale and assumptions:

The parent bank

- **Loan growth of 14.3% YoY** (vs. 16.8% in our previous estimate)

- **NIM to be revised down by 32 bps to 4.5%.** Specifically, loan yield is expected to be reduced by 70 bps, while the deposit rate is expected to be clipped by 25 bps. We noticed that VPB had already trimmed deposit rates for various terms by roughly 40 bps in 1Q 2020, but then boosted them upward by 20 bps in April. We believe that in order to maintain decent funding, deposit rates might be kept at competitive levels. Thus, they are not expected to tumble to as great a degree as lending rates.

- **The ratio of NPLs before write-offs we expect to surge by roughly 2.7%.** It could be inferred that approx. 20-30% (VND 2.3 - 3.5 tn) of restructured loans might not be recoverable. As the restructuring period the bank has applied is for a 3-month with no interest waiver or reduction, we may witness a surge in the bank's NPL ratio in later periods by roughly 1% to 1.6%.

  For a bit of background, the average increase in the NPL ratio before write-offs in the last 5 years was approx. 1.6% to 2.7% of outstanding loans. Hence, we expect roughly VND 6.2 to 6.4 tn in new NPLs to be incurred during the year. We expect the bank will aggressively pursue write-off activities to bring the NPL ratio to below 3% at year-end, which will in turn lead to soaring provision expenses in 2H 2020. If we assume that VPB might accept provision coverage to go down to 45% (or provision after recovery at 69%), we then expect provision expenses to rise by +9.8% YoY, or +37% YoY if we exclude the provision for VAMC bonds in 2019.

- TOI is projected to be VND 18.375 tn (+4.8% YoY)

- We maintain operating expenses as the same per bank guidance, as we believe it would be able to curb expenses to that extent.

FeCredit

- **Loan growth of 2.8%.** Given the new loan disbursement policy resulting in modest levels of new loan disbursement, we think FeCredit might focus on collection activities instead. Hence, a target loan book at relatively the same level as at the end of 1Q 2020 appears to be reasonable. As such, the new bank client portion of the loan book is expected to decrease by -10% YoY, while cross-sales/top-up are to decline by -5% YoY. Credit card is expected to be the key engine, with +60% YoY growth.

- **Average lending rate to decline by -157 bps,** due to a change in product mix as well as the settlement offer and restructuring offer provided to clients. Of note, the settlement offer is made to clients with more than 6 equal monthly installments paid. Accordingly, clients would receive certain incentives (no pre-payment penalty fees, interest reduction) if they are able to settle the loan earlier than originally scheduled. The restructuring offer enables clients to be able to defer their payments for a 3 month period.

- **NPL ratio to sit at 6% by year-end.** Although the NPL ratio at the end of 1Q 2020 was 4.43%, we believe that after the restructuring period, it would soar significantly. Assuming a recovery rate of 50% on the restructured loans, approx. 1.5% in additional NPLs will likely be added up in 2H2020.

- **Credit costs after recovery, hence, is expected to rise to 15%** (vs. 13% in 2019). This assumption falls within the higher end of the spectrum. According to management, if the company applies sales reduction measures, lifetime losses of the products would range from 2.3% to 16.2% - altered from the previous 2.7% to 21%. Lifetime loss of the product is the percentage of the loan which is not recoverable during the whole term.

The primary gap between our estimate and the bank's target lies in the details of provisioning expenses, as we expect VPB could rack up more provisions as an extra buffer during the year. The corporate bond portfolio of the banks could also pose inherent risk if the situation gets worse.

For 2021, we expect VPB to post VND 11.256 tn in pretax profit, up by +16.9% YoY, in which the parent bank would attain +19.3% YoY PBT growth to VND 7.6 tn, while FeCredit could record +12.2% YoY in PBT growth, to VND 3.6 tn. Key assumptions for the above estimate are as follows:

- Credit growth of 15.3% of the parent bank; 12.8% for FeCredit.

- NIM to be expanded by 42 bps from a low base in 2020 to 8.87%. This is still lower than the equivalent of 2019 (9.32%), as the loan book has been restructured toward lower risk segments with lower yields.

- The increase of NPLs before write-offs is assumed to be modest at +5% YoY (vs. +20% YoY in 2020) due to tightening credit measures taken in 2020. The NPL ratio of the parent bank and FeCredit, hence, would be 2.78% and 6%. Credit costs are projected to be 5.75%, which is -10 bps lower than the equivalent of 2020.

APPENDIX: ANNUAL FINANCIAL STATEMENTS

VND Million	2017	2018	2019	2020F	2021F
Balance Sheet					
+ Cash on hand, gold and gemstones	2,574,284	1,855,473	2,459,321	3,641,853	2,960,897
+ Balances with the SBV	6,460,795	10,828,571	3,454,138	9,153,978	9,783,890
+ Balances with and loans to other CIs	17,520,025	16,571,491	20,097,552	21,730,630	24,718,303
+ Trading securities	1,424,854	4,202,413	1,566,592	1,719,157	1,891,983
+ Derivatives and other financial assets	-	-	-	-	-
+ Loans and advances to customers	179,518,809	218,395,223	253,099,865	281,896,895	323,061,893
+ Investment securities	53,558,049	51,926,416	68,729,363	73,880,579	79,486,526
+ Long-term investments	152,506	190,654	174,134	174,134	174,134
+ Fixed assets	808,486	1,963,096	1,922,972	2,661,843	3,716,367
+ Investment property	-	-	-	-	-
+ Other assets	15,734,506	17,357,782	25,709,899	27,607,245	30,223,329
Total Assets	**277,752,314**	**323,291,119**	**377,213,836**	**422,466,315**	**476,017,322**
+ Amounts due to the Government and the SBV	26,015	3,781,343	19,492	2,184,358	1,636,425
+ Deposits and borrowings from other CIs	33,200,418	54,231,451	50,867,989	56,847,030	56,374,663
+ Deposits from customers	133,550,812	170,850,871	213,949,567	240,261,325	275,706,601
+ Derivatives and other financial liabilities	160,469	18,571	45,670	50,287	50,287
+ Financed funds, trust funds and borrowings from other credit institutions	3,899,364	329,649	291,823	291,823	291,823
+ Valuable papers issued	66,104,605	48,658,036	57,599,723	61,957,060	70,171,458
+ Other liabilities	11,114,921	10,671,129	12,222,063	13,588,309	15,341,667
Total Liabilities	**248,056,604**	**288,541,050**	**334,996,327**	**375,180,193**	**419,572,924**
+ Capital	21,572,335	24,096,960	23,296,370	23,296,370	23,296,370
+ Reserves	1,337,409	-	-	1,222,774	1,222,774
+ Foreign exchange differences	-	-	-	-	-
+ Asset revaluation differences	-	-	-	-	-
+ Retained earnings	4,565,110	5,187,230	11,812,568	18,212,855	25,817,389
Total Shareholders' Equity	**29,695,710**	**34,750,069**	**42,217,509**	**50,086,307**	**59,244,582**
Minority Interests	-	-	-	-	-
Total Liabilities, Shareholders' Equity & Minority Interest	**277,752,314**	**323,291,119**	**377,213,836**	**425,266,499**	**478,817,506**
Growth					
Deposit	15.8%	9.9%	23.7%	11.3%	14.4%
Credit	23.9%	17.3%	17.6%	11.4%	14.6%
Total assets	21.4%	16.4%	16.7%	12.0%	12.7%
Shareholders' Equity	72.9%	17.0%	21.5%	18.6%	18.3%
Net interest income	35.9%	19.8%	23.4%	4.5%	12.1%
Operating income	48.4%	24.2%	17.0%	2.6%	13.5%
Operating expense	34.3%	19.5%	16.0%	-4.5%	12.7%
Profit before tax	64.9%	13.1%	12.3%	-6.9%	16.9%
Profit after tax	63.7%	14.2%	12.4%	-6.9%	18.9%
Valuation					
P/E	14.54	6.51	5.97	6.41	5.39
P/B	2.17	1.43	1.17	0.99	0.83
BVPS (VND)	18,907	13,735	17,318	20,546	24,303

Source: Company, SSI Research

VND Million	2017	2018	2019	2020F	2021F
Income Statement					
Net interest income	20,614,426	24,701,575	30,492,344	31,879,310	35,724,473
Non-interest income	4,411,665	6,384,088	5,863,161	5,409,798	6,580,098
TOTAL OPERATING INCOME	**25,026,091**	**31,085,663**	**36,355,505**	**37,289,108**	**42,304,571**
Operating expenses	(8,894,970)	(10,633,924)	(12,334,010)	(11,773,999)	(13,275,063)
Pre-provision operating profit	**16,131,121**	**20,451,739**	**24,021,495**	**25,515,109**	**29,029,508**
Provision expense	(8,001,058)	(11,253,231)	(13,687,625)	(15,889,292)	(17,772,561)
PROFIT BEFORE TAX	**8,130,063**	**9,198,508**	**10,333,870**	**9,625,817**	**11,256,946**
Corporate Income Tax	(1,689,296)	(1,842,940)	(2,065,840)	(1,925,163)	(2,098,671)
PROFIT AFTER TAX	**6,440,767**	**7,355,568**	**8,268,030**	**7,700,654**	**9,158,275**
Net profit attributable to the minority interest	(146,439)	-	-	-	-
NET PROFIT ATTRIBUTABLE TO PARENTS' SHAREHOLDERS	**6,294,328**	**7,355,568**	**8,268,030**	**7,700,654**	**9,158,275**
EPS (VND)	2,820	3,025	3,392	3,159	3,757
Capitalization					
Capital adequacy ratio - CAR (Basel II in 2019F-2020F)	14.6%	11.9%	**11.0%**	**10.0%**	**9.5%**
Equity/Total assets	10.7%	10.7%	11.2%	11.9%	12.4%
Equity/Loans to customers	16.3%	15.7%	16.4%	17.5%	18.1%
Assets quality					
NPL ratio	2.89%	3.21%	3.13%	3.24%	3.15%
Provision coverage ratio	50.8%	45.9%	46.4%	41.3%	42.1%
Management					
Cost to income ratio - CIR	35.5%	34.2%	33.9%	31.6%	31.4%
Net operating profit per employee	1,050	1,133	1,353	1,239	1,255
Profit before tax per employee	341	335	385	320	334
Net operating profit per branch/transaction office	115,328	138,775	160,156	159,355	180,789
Profit before tax per branch/transaction office	37,466	41,065	45,524	41,136	48,107
Earnings					
Net interest margin - NIM	8.76%	8.79%	9.32%	8.57%	9.10%
Non-interest income/Net operating profit	17.6%	20.5%	16.1%	14.5%	15.6%
ROA - average balance	2.5%	2.4%	2.4%	1.9%	2.0%
ROE - average balance	27.5%	22.8%	21.5%	16.7%	16.8%
Liquidity					
Loans to deposits ratio - Pure LDR	98.5%	105.1%	99.9%	100.1%	100.2%

Source: Company, SSI Research

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