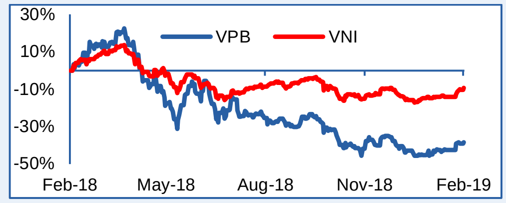
VPBank (VPB) [BUY +31.0%]

Update Report

			2018	2019F	2020F	2021F
Industry:	**Banking**					
Report Date:	**February 26, 2019**					
Current Price:	VND21,300	PPOP y/y	26.8%	14.0%	9.2%	9.5%
Current Target Price:	VND27,900	NPAT y/y	14.2%	19.0%	8.1%	20.7%
Previous Target Price:	VND27,500	NIM	8.8%	8.9%	8.7%	8.5%
		NPL	3.5%	3.7%	3.9%	3.9%
Upside to TP:	+31.0%	CIR	34.2%	35.0%	35.0%	35.0%
Dividend Yield:	0.0%	Div/Sh (VND)	0	0	0	0
TSR:	+31.0%	P/B	1.5x	1.1x	1.0x	0.8x



			VPB	Peers	VNI
Market Cap:	$2.2bn				
Foreign Room	$0mn	P/E (ttm)	7.0x	10.6x	16.6x
ADTV30D	$2.6mn	P/B (curr)	1.5x	1.7x	2.6x
State Ownership	0%	ROE	22.8%	18.8%	15.5%
Outstanding Shares	2.457 bn	ROA	2.4%	1.5%	2.5%
Fully Diluted Shares	2.457 bn				

Company Overview

Vietnam Prosperity Joint Stock Commercial Bank is a Vietnam-based commercial bank with two fully owned subsidiaries: an asset management company (VPBank AMC) and a consumer finance company (FE Credit). VPB derived c.50% of its consolidated NPAT-MI from FE Credit in 2018.

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Q1 FEC loan growth key to affirming 2019 growth trend

- We lift our TP by 1.5% to VND27,900 and maintain our BUY rating with a projected TSR of 31.0% as we revise up our 2019/2020/2021 earnings forecasts by 6%/2%/4%, respectively. Our 2019 net profit forecast is VND8.7tn (USD380mn, +19% YoY).
- We increase our projections on NII forecasts for 2019/2020/2021 by 4%/5%/6%, respectively, due to the delivery of higher-than-expected loan growth at both the parent bank and FE Credit (FEC) in Q4 2018 and our view of FEC's net yield expansion in 2019. Consolidated 2019 NIM to increase 10 bps to 8.9%.
- We hold our 2019 consolidated loan growth forecast at 13.8% YoY with FEC's book growing 10% YoY for the time being.
- 2018 ROE stood at 22.8% against a sector median of 18.8%, and we expect ROE to maintain at around 18% in the medium term. VPB's valuation is compelling at a TTM P/B of 1.5x compared to the sector median at 1.7x, in our view.

Fortunes of consumer finance subsidiary continue to hem in outlook for consolidated bank. The consumer finance market must now contend with the presence of Shinhan Bank and Lotte Card. Add to this our observation that both HD Saison (HDS) and FE Credit (FEC) saw loan yield compression accelerate in 2018 relative to 2017 as measured by absolute point drop, even if one calculates annual yields using a quarterly geometric return method (-8.8 pts relative to -7.9 pts for HDS and -4.2 pts relative to -1.1 pts for FEC, respectively). Using this same measure, the drop at HDS in 2018 is more than double that of FEC, leading us to the inference that yield pressure was greatest in the non-cash loan segment given FEC has c 83% of its loan book in cash or credit card loans at the end of 2018. On a positive note, our observation of funding cost and OPEX trends at HDS and FEC leads us to the conclusion that yield compression will level off in 2019.

State of competition prompts restraint, but strong loan growth in Q1 2019 on top of strong Q4 2018 growth will dispel disappointment in 9M 2018 and trigger a positive catalyst for VPB, in our view. The degree of difficulty of FEC growing its loan book strongly after adding 14 ppts of growth in Q4 2018 is high. Its YE2018 loan book of USD2.3bn is 496% larger than HDS. We believe that a loan growth of close to 5% QoQ in Q1 2019 would be a good achievement and trigger our positive view that FEC has the business model to keep competition at bay.

We expect consolidated NFI, including FX, to grow by 30% YoY in 2019. Management sees less need for acquiring customers at FEC in 2019, evidenced by predominantly cash loan driven growth in Q4 2018, rather than consumer durable loans. We expect the drag from FEC's commission expenses paid to retailers to slow, lifting consolidated NFI growth in 2019.

2018 recap: Loan growth jumps in Q4

Figure 1: VPB's consolidated 2018 results

	2017	2018	YoY	% of VCSC's previous 2018F	VCSC comments
Net interest income	20,625	24,702	19.8%	100%	Consolidated and standalone NII increased by 19.8% and 17.1% YoY, respectively. 2018 NIM remained at 8.8% (consolidated) and 4.6% (standalone). Consolidated NII to TOI stood at 79% (vs 82% in 2017), mainly due to lack of loan growth at FEC during 9M 2018.
Net fee income*	1,290	1,509	17.0%	87%	The standalone bank saw a 75% YoY increase in 2018 NFI, including FX, offsetting lackluster insurance services growth (-11% YoY) and high customer acquisition expenses at FEC in 2018 (the parent's fee expenses growth was 6.9% YoY vs 26% growth at the consolidated level). Consolidated NFI saw 17% YoY growth during the same period.
Total NOII	4,399	6,384	45.1%	115%	Total NOII surpassed our 2018 forecast, mainly due to a boost in recovery income from written-off debt (**Figure 9**). 2018 recovery income grew 242% YoY at the standalone bank and 173% YoY at FEC, equivalent to 30% of 2018 write-offs.
OPEX	(8,895)	(10,634)	19.5%	97%	
PPOP	16,128	20,452	26.8%	105%	
Provision expenses	(8,002)	(11,253)	40.6%	107%	Consolidated net write-offs (add back recovery) to gross loans as of YE2018 stood at 3.4% vs 4.4% in H1 2018 and 3.0% in 2017 (**Figure 10**). 2018 provision expenses to gross loans stood at 5.1% (-40 bps vs annualized H1 2018 and +70 bps vs 2017). Management expects risk costs to trend down in 2019.
Net profit	6,438	7,356	14.2%	105%	
NIM	8.80%	8.83%	3 bps		NIMs bounced back in Q4 at the consolidated and standalone banks with 29-bp and 15-bp QoQ increases, respectively, due to a strong boost in retail at the parent and consumer finance loans at FEC.
Interest-earning asset yields	14.56%	14.40%	-16 bps		
Cost of funds	6.13%	6.05%	-8 bps		
CASA ratio**	15.0%	13.7%	-1.3 ppts		
Customer deposits in foreign currencies growth	-28.0%	9.2%	37 ppts		2018 customer deposits in foreign currencies (mostly USD) accounted for 3.4% of total deposits.
CIR	35.5%	34.2%	-1.3 ppts		Staff costs occupied 57% of total consolidated OPEX.
NPL	3.39%	3.51%	11 bps		
Loan growth (YTD)	26.3%	21.2%	-5.1 ppts		FEC recorded 19% loan growth YoY in 2018, mainly disbursed in Q4.
Deposit growth (YTD)	7.9%	27.9%	20 ppts		

Source: VPB & VCSC, units are in VND bn unless otherwise stated - *Net fee income includes FX gains, **CASA volume included demand and margin deposits.

2019 outlook: Balancing growth and credit quality

Figure 2: VCSC's 2019 forecasts

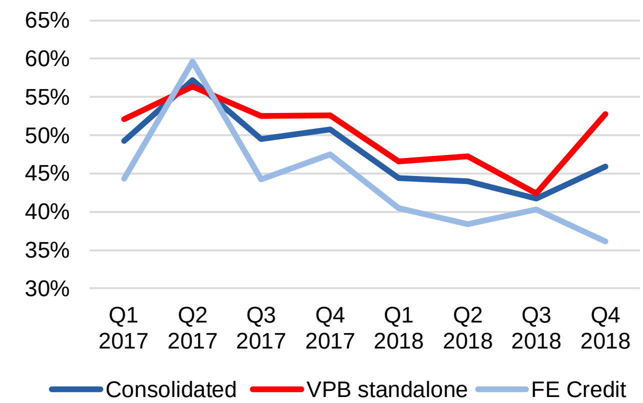
	2018	2019F old	2019F new	2019F new vs 2018	VCSC comments on 2019 forecasts
Net interest income	24,702	27,686	28,745	16.4%	We lift our 2019 NII forecast by 4% and project a faster pace of growth than loan growth in 2019 due to higher-than-expected loan disbursement at both the standalone bank and FEC in Q4 2018.
Net fee income*	1,509	2,289	1,969	30.5%	We maintain our positive outlook on the standalone bank's fee income growth, driven by banking and bancassurance services. Also, we expect the drag from FEC to slow from its high expense base and after spending 9M 2018 acquiring customers. However, we lower our 2019 NFI forecast by 14% as fees from bancassurance at FEC did not show signs of improvement.
Total NOII	6,384	6,576	7,111	11.4%	**Figure 9** illustrates the concerted efforts of VPB, including FEC, in boosting the recovery of written-off debt. We forecast recovery income from written-off debt to grow by 8% YoY in 2019. Our 2019 normalized total non-interest income (NOII) growth forecast, excluding a second tranche of bancassurance upfront in 2018, is 27.3% YoY.
PPOP	20,452	21,928	23,306	14.0%	
Provision expenses	(11,253)	(11,540)	(12,364)	9.9%	
Net profit	7,356	8,230	8,750	19.0%	
NIM	8.83%	8.81%	8.94%	10 bps	We expect consolidated NIM to increase by 10 bps YoY in 2019, mainly due to FEC's loan disbursement in Q4 2018.
Interest-earning asset yields	14.40%	14.33%	14.47%	7 bps	
Cost of funds	6.05%	6.17%	6.03%	-2 bps	
CASA ratio**	13.7%	17.0%	14.7%	1.0 ppts	
CIR	34.2%	36.0%	35.0%	0.8 ppts	
NPL	3.51%	3.90%	3.74%	23 bps	
Gross loans	221,460	236,290	252,016	13.8%	We retain our conservative view on 2019 loan growth for now with an assumption of better-managed credit quality to control provision charges. We forecast 13.8% YoY consolidated loan growth in 2019 with the loan book at the standalone bank and FEC growing at 15% and 10%, respectively.
Customer deposits	170,851	185,903	198,187	16.0%	
Valuable papers	48,658	61,081	53,524	10.0%	
Total assets	323,308	356,068	370,018	14.4%	
Total equity	34,750	42,030	46,703	34.4%	
ROAE	22.8%	21.6%	21.5%	-1.3 ppts	
ROAA	2.4%	2.5%	2.5%	0.1 ppts	
Regulated LDR	81.0%	79.1%	81.7%	0.7 ppts	

Source: VCSC, units are in VND bn unless otherwise stated – *Net fee income includes FX gains, **CASA volume included demand and margin deposits

NPL ratio trended down in Q4 2018 after a spike during 9M 2018, credit quality improvement in 2019 could ease provision charges to gross loans

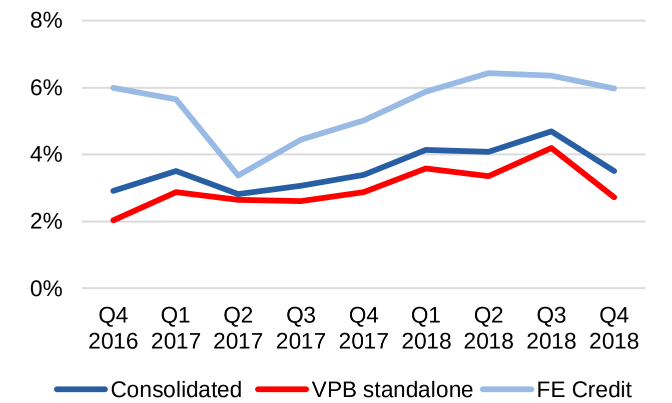
The consolidated NPL ratio dropped to 3.5% (-119 bps QoQ and +11 bps YoY) in Q4 2018. Consolidated group 2 loans also dropped 6.6% QoQ and 4.3% YoY in Q4, indicating improvement in credit quality after a cut in alternative sources (loan disbursement via third parties). **Figure 4** shows a positive signal in the NPL trend at both the parent and FEC. Management sees provision charges dropping in 2019. However, a strong boost in loan growth in Q4 2018 needs a quality validation in Q1 2019's financial results. We hold our conservative forecast for 2019 provision expenses to gross loans at 4.9% (vs 5.1% in 2018).

Figure 3: Loan loss reserve ratio



Source: VPB

Figure 4: NPL ratio

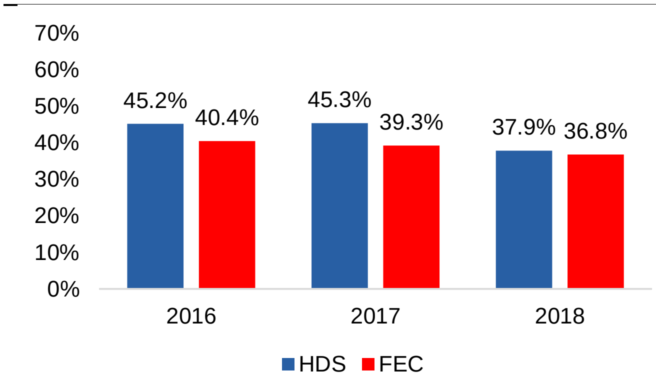


Source: VPB

The net yield compression at FEC has potential to level off in 2019

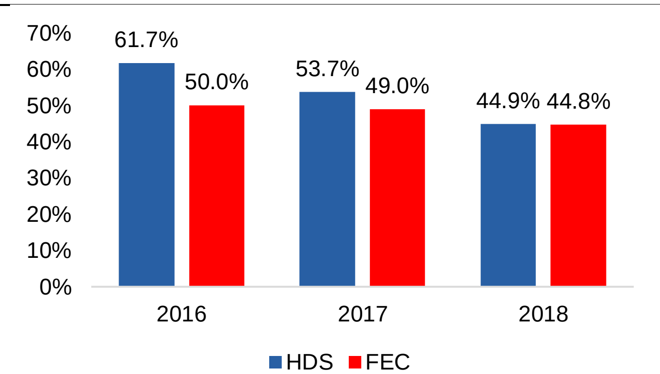
Both FEC and HDS's loan yield dropped in 2018 by 4.2 ppts and 8.8 ppts, respectively, using the quarterly geometric method. The drop at HDS in 2018 is more than double than that of FEC. Given the cash loan focus at FEC vs sales finance focus (including consumer durables and two-wheeler loans) at HDS, we see the yield pressure was more on the non-cash loan side.

Figure 5: HDS and FEC's loan yields comparison (using average annual loan balances)



Source: HDB, VPB, VCSC

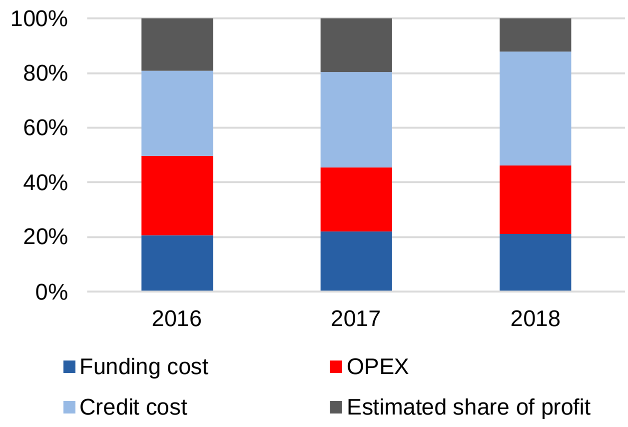
Figure 6: HDS and FEC's loan yields comparison (using quarterly geometric method)



Source: HDB, VPB, VCSC

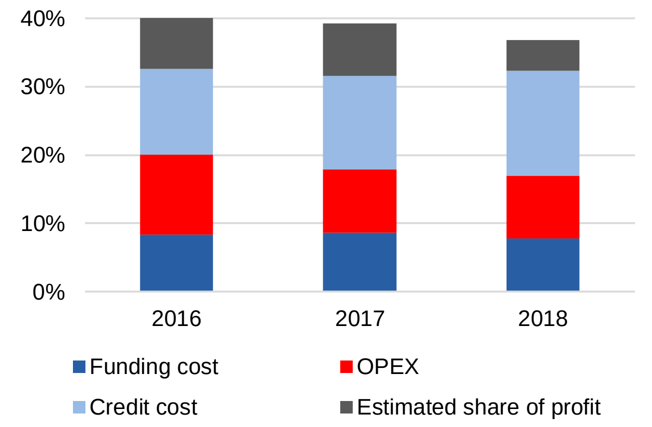
Loan yield at FEC compressed in 2018 either due to an alternative sources cut or intensifying competition in the consumer finance field. However, **Figure 7** illustrates that FEC has balanced out its OPEX (25% of interest income) and funding costs (21% of interest income).

Figure 7: Estimated share of profit in interest income of FEC



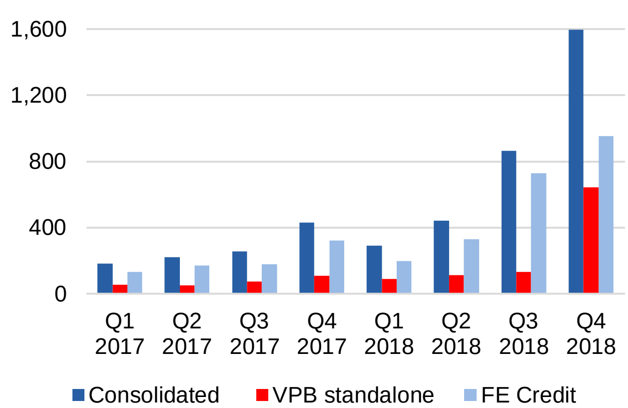
Source: VPB, VCSC

Figure 8: Estimated share of profit in loan yield of FEC



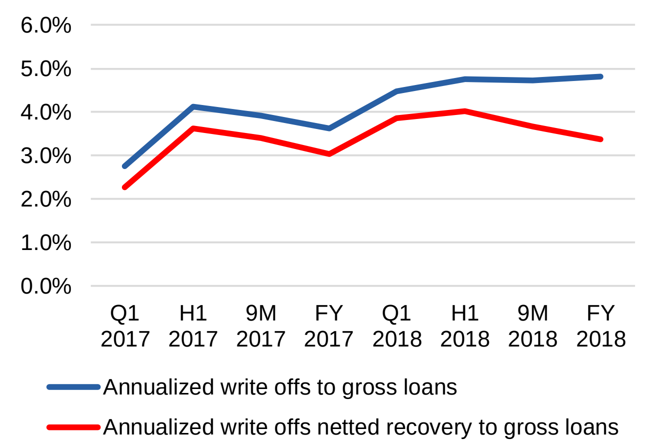
Source: VPB, VCSC

Figure 9: Income from recovery of written-off debt (VND bn) (non-cumulative)



Source: VPB, VCSC

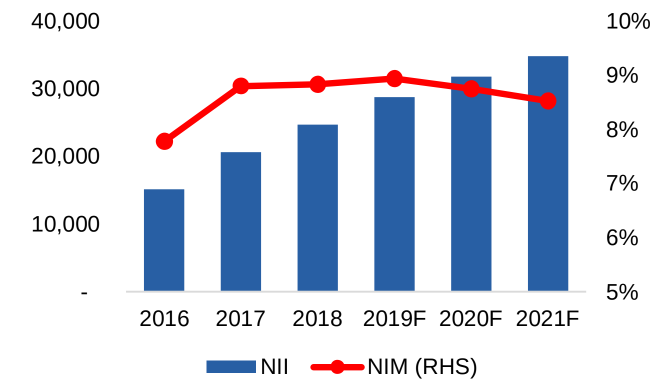
Figure 10: Pure write-offs vs write-offs netting recovery over gross loans (consolidated)



Source: VPB, VCSC – incremental numbers within a year

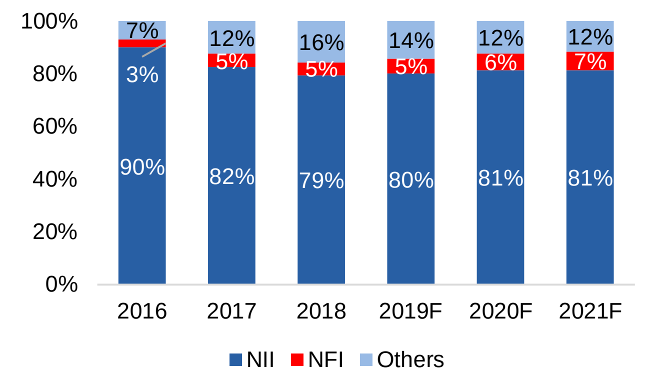
Key figures of VPB

Figure 11: NIM (%) and NII (VND bn) (2016-2021F)



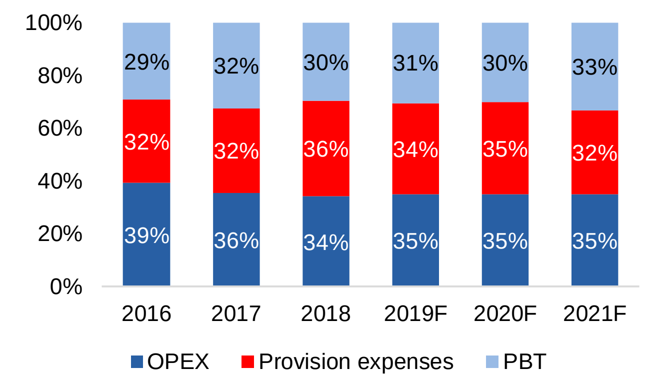
Source: VPB, VCSC

Figure 12: TOI components (2016-2021F)



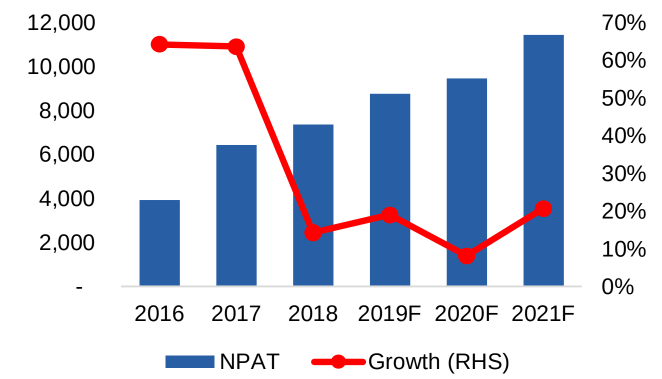
Source: VPB, VCSC

Figure 13: OPEX, provision expenses and PBT as % of TOI (2016-2021F)



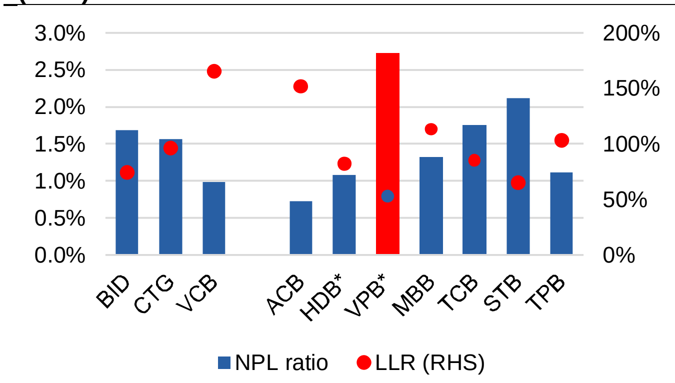
Source: VPB, VCSC

Figure 14: NPAT (VND bn) and growth (%) (2016-2021F)



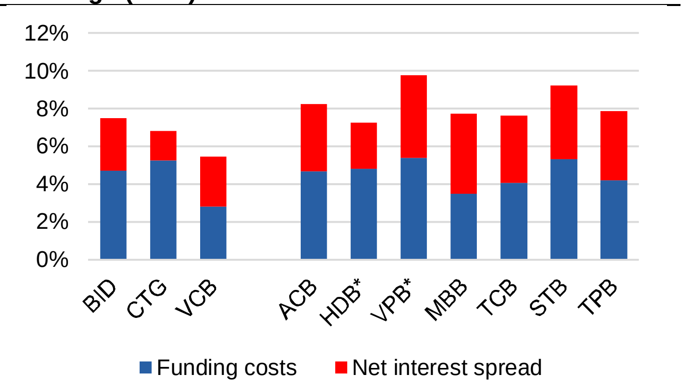
Source: VPB, VCSC

Figure 15: NPL ratio and LLR of banks under coverage (2018)



Source: Company data, VCSC – * standalone bank only

Figure 16: Interest-earning asset yields of banks under coverage (2018)



Source: Company data, VCSC - * standalone bank only

Valuation

We utilize two valuation methodologies in estimating our target price, assigning equal weighting for the residual income method and implied multiples. Our target price is VND27,900/share.

Figure 17: Cost of equity

Cost of equity	
Risk free rate	4.5%
Beta	1.0
Market Risk Premium	8.4%
Cost of equity	12.9%

Source: VCSC

Figure 18: Valuation summary

Method	Fair value	Weighting	Contribution
Residual income	66,934 (USD2.91bn)	50%	33,467
Target P/B @ 1.5x 2019F	70,054 (USD3.05bn)	50%	35,027
Composite valuation			**68,494 (USD3.02bn)**
Number of shares outstanding (bn)			2.457
Target price (VND)			**27,900**
Upside			31.0%
Dividend yield			0.0%
TSR			31.0%
2019F P/B at TP			1.47x
RATING			**BUY**

Source: VCSC, units are in VND bn unless otherwise stated

Figure 19: Residual income model

Residual income	2018F	2019F	2020F	2021F	2022F
ROE (Beginning period equity)	25.2%	20.3%	20.5%	18.7%	17.4%
COE	12.9%	12.9%	12.9%	12.9%	12.9%
Terminal Economic Margin (TEM)	12.3%	7.4%	7.6%	5.8%	4.5%
Equity value (Beginning period)	34,750	46,703	55,597	66,330	78,017
Residual income	4,267	3,437	4,246	3,877	3,496
PV of residual income	3,780	2,697	2,951	2,386	1,906
Sum PV of RI			13,719		
PV of terminal value (2.0% perpetual growth)			18,464		
Beginning EV (YE2018)			34,750		
Fair equity value			**66,934**		
Number of shares outstanding (bn)			2.457		
Fair value per share (VND)			**27,245**		

Source: VCSC, units are in VND bn unless otherwise stated

We assume a 2% perpetual growth rate for VPB, aligning our modelling with HDB. We apply a 1-ppt lower rate relative to other banks in our coverage as half of VPB's consolidated earnings is derived from FEC (2018) and in our view, the consumer finance sector will face increasing pressure in the future.

Comparable peers

Our observation suggests that VPB on average traded in line to the peer median trailing P/B in the past twelve months. VPB is currently traded at a discount of 12% compared to the peer median trailing P/B of 1.7x.

VPB is chasing for unsecured retail and SME loans which yield high return metrics with 2018 ROE at 22.8% against a domestic peer median at 18.8%. Operating under well-capitalized conditions at 9.3x leverage vs the peer median at 12.8x, VPB's ROAA is toward the high end in 2018. We forecast a net income CAGR of 13% during 2018-2023 with sustainable ROE of 18% due to a conservative FEC loan growth forecast of 10% CAGR during the same period. Taken together, we put the bank at a 2019F target P/B of 1.5x.

Figure 20: Bloomberg consensus forecasts for Vietnamese banks

Bloomberg Ticker	Market Cap. (USD bn)	P/E			P/B			ROE			ROA	Equity Multiplier	NPL
		2018	2019F	2020F	2018	2019F	2020F	2018	2019F	2020F	TTM	2018	2018
ACB VN	1.63	7.40	6.88	6.41	1.81	1.38	1.23	27.7%	24.9%	21.3%	1.67%	15.7	0.73%
BID VN	5.01	15.08	16.97	9.74	2.15	1.68	1.30	15.08	14.5%	17.2%	0.59%	24.0	1.69%
CTG VN	3.31	14.32	15.23	7.34	1.16	1.05	0.92	14.32	9.2%	14.4%	0.48%	17.3	1.56%
MBB VN	2.05	7.78	6.82	5.79	1.39	1.26	1.06	7.78	20.4%	20.3%	1.81%	10.6	1.32%
VCB VN	9.45	14.40	16.48	13.74	3.30	2.75	2.36	14.40	21.7%	21.8%	1.39%	16.8	0.98%
STB VN	1.00	13.10	13.35	9.41	0.95	0.88	0.79	13.10	7.7%	10.3%	0.46%	16.5	2.11%
HDB VN	1.26	10.74	10.86	14.27	1.95	1.73	1.34	10.74	20.3%	17.6%	1.40%	12.8	1.53%
TCB VN	4.15	11.04	9.81	7.92	1.86	1.57	1.33	11.04	17.2%	17.8%	2.87%	6.2	1.75%
TPB VN	0.77	9.68	6.83	5.13	1.71	1.11	1.17	9.68	18.0%	19.7%	1.39%	12.8	1.12%
Median		**11.04**	**10.86**	**7.92**	**1.71**	**1.26**	**1.17**	**20.1%**	**18.0%**	**17.8%**	**1.40%**	**12.8**	**1.56%**
VPB VN	**2.24**	**7.06**	**6.27**	**5.45**	**1.51**	**1.14**	**1.03**	**7.06**	**21.5%**	**20.7%**	**2.45%**	**9.3**	**3.51%**

Source: Bloomberg as on 2/22/2019

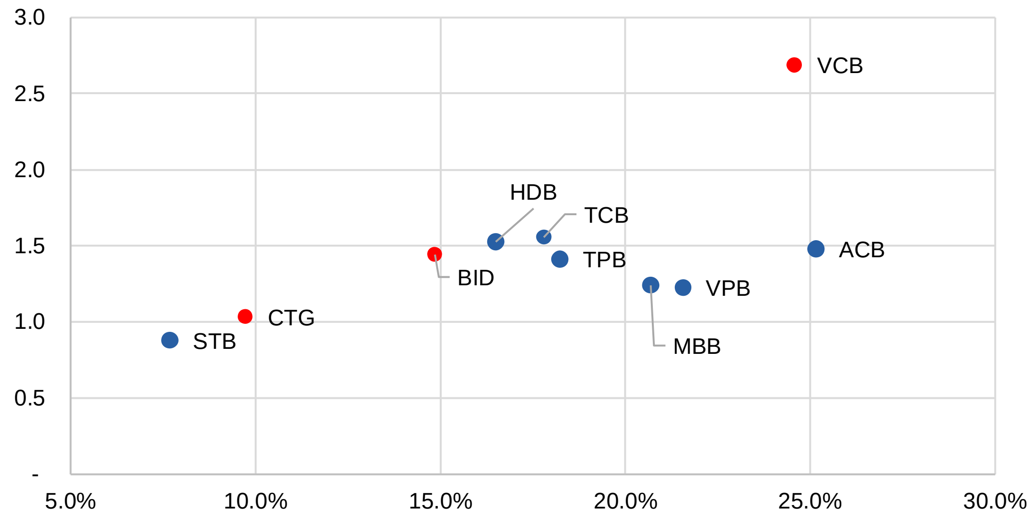
Figure 21: Sensitivity analysis of our 2019F P/B for VPB in relation to ROE derived from Gordon growth model and terminal growth rate, ceteris paribus.

		2019F ROE				
		17.5%	**19.5%**	**21.5%**	**23.5%**	**25.5%**
Terminal growth (g)	**1.0%**	1.39	1.55	1.72	1.89	2.06
	1.5%	1.40	1.58	1.75	1.93	2.10
	2.0%	1.42	1.60	1.79	1.97	2.15
	2.5%	1.44	1.63	1.83	2.02	2.21
	3.0%	1.46	1.67	1.87	2.07	2.27
	3.5%	1.49	1.70	1.91	2.13	2.34

Source: VCSC

The above sensitivity matrix illustrates a fair value P/B multiple for VPB at 1.79x using the Gordon Growth Model with ROE of 21.5% (our 2019F), cost of equity at 12.9% (**Figure 17**) and terminal growth of 2.0%. Our target price at a 1.47x 2019 projected P/B (**Figure 18**) is 17% lower than the P/B multiple derived from Gordon Growth Model because the business model is dependent largely on interest income from unsecured loans. While having a strong position on the market in this segment, (1) an intensifying competition could press down yields and/or (2) a spike in NPLs could lead to substantial provision charges, dragging ROE projections.

Figure 22: Vietnam banks P/B (x-axis) and ROE (y-axis) (2019F)



Source: VCSC

Risk to our positive view and forecasts: VPB may fail to meet our NPL ratio and earnings expectations either due to its failure to execute on its business model regarding high-yield businesses, failure to continue growing its retail franchise/digital banking or a macro-driven banking crisis that leads to a new cycle of NPLs.

Financial Statements

P&L (VND bn)	2018	2019F	2020F	2021F
Interest inc.	40,280	46,541	52,223	57,929
Interest exp.	(15,579)	(17,796)	(20,385)	(23,073)
Net interest inc.	**24,702**	**28,745**	**31,838**	**34,857**
Fee & commission inc.	1,612	2,062	2,578	3,128
Other non-interest inc.	4,772	5,049	4,738	4,880
Total non-interest inc.	6,384	7,111	7,315	8,007
Total operating inc.	**31,086**	**35,856**	**39,153**	**42,864**
Non-interest exp.	(10,634)	(12,550)	(13,704)	(15,002)
Other G&A exp.	-	-	-	-
Total operating exp.	(10,634)	(12,550)	(13,704)	(15,002)
PPOP	**20,452**	**23,306**	**25,450**	**27,862**
Provision exp.	(11,253)	(12,364)	(13,617)	(13,583)
Other inc./exp.	-	-	-	-
Pre-tax profit	**9,199**	**10,943**	**11,832**	**14,279**
Taxes	(1,843)	(2,192)	(2,371)	(2,861)
Net profit	**7,356**	**8,750**	**9,462**	**11,418**
Minorities/pref divs	-	-	-	-
Attributable net profit	**7,356**	**8,750**	**9,462**	**11,418**
Adj shares, wt avg (mn)	2,433	2,457	2,457	2,457
EPS (VND)	3,024	3,562	3,851	4,648
DPS (VND)	-	-	-	-

BS (VND bn)	2018	2019F	2020F	2021F
Cash & equivalents	1,855	2,865	3,266	3,637
Balances with SBV	10,829	5,183	5,374	6,034
Due from FIs	16,571	18,229	20,052	22,057
ST investments	53,066	65,894	72,306	79,347
Net customer loans	217,893	247,266	281,267	315,936
HTM	3,565	2,309	1,921	1,599
Long term investments	191	162	154	146
Property & equipment	1,963	2,061	2,164	2,273
Other assets	17,375	26,048	30,075	32,033
Total assets	**323,308**	**370,018**	**416,579**	**463,062**
	-	-	-	-
Borrowings from SBV	3,781	3,306	3,768	4,196
IB deposits & borrowings	54,231	56,943	59,790	62,780
Other borrowed funds	330	346	363	382
Customer deposits	170,851	198,187	227,915	255,265
Other financial int.	19	-	-	-
Valuable papers	48,658	53,524	57,806	62,430
Other liabilities	10,688	11,009	11,339	11,680
Shareholders' equity	34,750	46,703	55,597	66,330
MI	-	-	-	-
Liabilities & equity	**323,308**	**370,018**	**416,579**	**463,062**

RATIOS (%)	2018	2019F	2020F	2021F
Growth				
Loan growth	21.2	13.8	13.8	12.3
Deposit growth	27.9	16.0	15.0	12.0
TOI growth	24.2	15.3	9.2	9.5
PPOP growth	26.8	14.0	9.2	9.5
NPAT growth	14.2	19.0	8.1	20.7
Asset quality				
Group 2 / loans	5.27	5.27	5.27	5.27
NPL ratio	3.51	3.74	3.94	3.94
LLR	45.9	50.4	49.7	49.7
Provision exp. / loans	5.08	4.91	4.75	4.21
Liquidity				
CAR under BASEL I	13.2	14.9	15.2	15.8
Regulated LDR	81.0	81.7	83.1	83.1

RATIOS (%)	2018	2019F	2020F	2021F
Profitability				
NIM	8.83	8.94	8.75	8.52
Int-earning asset yields	14.40	14.47	14.34	14.17
Funding costs	6.05	6.03	6.16	6.28
CIR	34.2	35.0	35.0	35.0
ROE decomposition				
Pre-provision NIM	8.22	8.29	8.10	7.93
Provisions	-3.74	-3.57	-3.46	-3.09
Post-provision NIM	4.47	4.73	4.63	4.84
Non-Interest inc.	2.12	2.05	1.86	1.82
Operating exp.	-3.54	-3.62	-3.48	-3.41
Taxes	-0.61	-0.63	-0.60	-0.65
ROAA	2.45	2.52	2.41	2.60
Equity Mult. (x)	9.3	8.5	7.7	7.2
ROAE	22.8	21.5	18.5	18.7

Source: Company data, VCSC

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MARKET PERFORM	If the projected TSR is between -10% and 10%
UNDERPERFORM	If the projected TSR is between -10% and -20%
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