Initial Rating Public Announcement:

Bac A Commercial Joint Stock Bank ("BAB")

Issuer Credit Rating*: A-

Rating Outlook: Stable

Hanoi, 01 April 2024

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The rating scale used by FiinRatings is the national scale, therefore, it must not be equated with or represented as a rating on the scale used by any other rating agencies.

The rating presented in this announcement is effective from the rating date, until and unless we make any further updates.

This document is prepared in both English and Vietnamese. The English translation is for reference only and the Vietnamese version will prevail in the event of any inconsistency between the English version and the Vietnamese version.

Hanoi, 01 April 2024

FiinRatings is pleased to announce that it has assigned a first-time Long-Term Issuer Credit Rating of **‘A-**’ to Bac A Commercial Joint Stock Bank ("BAB" or "the Bank") with a ‘**stable**’ rating outlook.

RATING SUMMARY

Criteria	Rating points
Banking Anchor	**a-**
Modifiers:	
Business Position	*-1*
Capital & Earnings	*-1*
Risk Position	*+2*
Funding & Liquidity	*+0*
Stand-alone Credit Profile	***a-***
External Support	**+0**
Issuer credit rating	**A-**
Outlook	**Stable**

RATING RATIONALE

The issuer credit rating on BAB of **'A-'** with a **'Stable'** rating outlook reflects our expectation that the Bank's credit profile will be relatively stable over the next 24 months; this is supported by the Bank’s ability to maintain a stable business position, along with the Bank's good risk management capacity. For many years, BAB has a consistent and balanced lending strategy, which focuses on sectors that are less affected by economic fluctuations, such as agriculture, forestry, fisheries and processing and manufacturing industries. In addition, the Bank's funding capability and liquidity position are also expected to remain stable due to sticky/committed individual customers' deposits base as well as a highly liquid investment portfolio, along with an appropriate interbank market trading strategy that has limited risks from the dependence on wholesale funding of BAB.

FiinRatings assigns an anchor rating to the banking industry in Vietnam at '**a-**', reflecting our assessment of the macro environment and industry-specific risks faced by commercial banks operating in Vietnam. In general, despite the pressure on asset quality, FiinRatings expects the credit quality of commercial banks in Vietnam to remain relatively stable in the next 12-24 months, thanks to the Government's supportive policies, as well as expectations of medium-term economic recovery. These drivers will also help reduce difficulties in credit growth, thereby partially improving the profitability of commercial banks. In 2024, FiinRatings also expects that the acceleration in raising tier-2 capital in will support banks improve capital buffers and maintain stable capital sources at reasonable costs, thereby strengthening banks' creditworthiness.

Based on our evaluation of BAB's business scale & scope, which is comparatively smaller and less diverse than the industry norm, we assess the Bank’s business position as 'Moderate'. This could affect the stability of BAB's operations in the medium term. As of 31/12/2023, BAB is categorized among the smaller joint-stock commercial banks in Vietnam, with a relatively modest but stable market share. BAB's market share in terms of Total Assets, Customer Deposits, and Outstanding Loans has consistently accounted for approximately 1.0% of the industry, with minimal annual fluctuations of less than 0.1 percentage points despite market changes over the past 5 years. Despite limited geographical coverage compared to its peers, BAB exhibits business stability, supported by a loyal customer base primarily comprising individual customers, particularly pensioners, who tend to make long-term deposits for asset preservation. This customer base ensures relatively high stability and provides BAB with a solid capital base while minimizing concentration risk and reliance on wholesale funding sources. Additionally, BAB's business stability is expected to be sustained through consistent lending policies targeting sectors less susceptible to economic fluctuations, along with plans to expand its customer base in the medium term. Notably, BAB has directed a significant portion of its lending towards sectors such as agriculture, forestry, processing, and manufacturing, which are deemed lower risk and less sensitive to macroeconomic changes compared to capital-intensive industries like real estate or construction, which faced challenges in the previous 2022-2023 period.

In the Bank's 2024-2025 strategy, BAB's Board of Directors has determined to prioritize lending to high-tech agriculture, and manufacturing, while restricting lending to real estate and securities sectors. FiinRatings assesses that this approach, combined with the expected recovery in import and export activities, will be a primary driver of the Bank's growth in the next 2 years. However, we also view that BAB might face pressure from interest rate competition due to higher funding costs compared to other banks, resulting from its focus on medium and long-term savings deposits. This necessitates maintaining lending interest rates at certain levels to ensure a favorable net interest margin, impacting competitiveness during periods of low demand, such as in 2023, when BAB's credit growth was only 6.1%, which is considerably lower than the system's credit growth of 13.7%.

Moreover, BAB's business diversification remains limited as it heavily relies on lending activities, with non-interest income contributing less to the total operating income compared to the industry average. Over the past five years (2018-2023), income from lending activities has consistently accounted for over 90% of total operating income. Given that BAB's customer base consists mainly of individuals who borrowed for business purposes, demand for other services like credit cards, payments, foreign exchange, and underwriting is relatively low. Additionally, BAB lacks subsidiaries in other fields such as securities, insurance, asset management, or consulting, unlike some other banks. There are no significant plans to expand its portfolio and service system in the upcoming period of 2024-2025 beyond its current operating model.

In terms of products, BAB aims to increase the proportion of loan packages for non-production purposes such as car loans, home purchases, and consumption. However, it's assessed that this product diversification may not substantially impact the Bank's overall loan portfolio in the upcoming period.

We evaluated BAB's Capital Structure and Earnings as 'Moderate', reflecting the Bank's lower capital buffer and profitability compared to the industry average. Despite maintaining a Capital Adequacy Ratio (CAR) higher than the minimum required threshold of 8% set by the State Bank of Vietnam (SBV) during the last 3 years, BAB consistently ranked among the bottom 5 banks who have the lowest CAR ratio in the banking system. While BAB's Tier 1 Capital to Total Assets ratio closely mirrored the industry average from 2015-2022, a significant 22% increase in deposits, outpacing profit and charter capital growth in 2023 led to a decrease in the Tier 1 Capital to Total Assets ratio from 7.6% to 7.1%. We anticipate this ratio to increase to around 7.9% in 2024-2025 due to a decrease in deposits, thanks to abundant medium and long-term capital mobilized in 2023. Additionally, a planned increase in capital of approximately VND 1.400 billion, with VND 896 billion through new issuances, is expected to bolster Tier 1 capital if executed as planned.

FiinRatings assesses BAB's profitability as modest compared to its peers, primarily due to its relatively low net interest margin stemming from high deposit costs and suboptimal operating efficiency. BAB's capital mobilization primarily revolves around term deposits, particularly those exceeding 1 year in tenor. Term deposits contribute about 95% to total deposits, 45% of which have terms longer than 1 year. BAB offers relatively high interest rates compared to other banks to attract medium and long-term savings deposits, prioritizing capital stability and liquidity. Consequently, this approach results in higher funding costs compared to the industry average. Despite offering preferential interest rates for lending to high-tech agricultural and manufacturing sectors, BAB's 2023 average financing costs was at 8.8%, surpassing the industry average of 6.1%. Additionally, the concentration of short-term and medium-term loans for household production contributes to BAB's relatively low Net Interest Margin (NIM) compared to the industry average. BAB's NIM remained at 2%, while the industry average hovered around 3% from 2018-2023. In the short term, BAB's profitability is expected to continue facing challenges related to the economy's limited capacity to absorb capital, which has not fully recovered. Nevertheless, in the medium to long term, we anticipate BAB's profit margin to improve as it leverages long-term capital at a favorable cost in a low-interest rate environment, and as the economy rebounds from a challenging period, leading to increased demand for loans.

In terms of managing operating costs, BAB exhibits a relatively high Cost to Income ratio (CIR), which significantly surpasses the industry average figure. BAB’s CIR ratio in 2023 reached 60.9%, whereas the industry average stood at 31.3%. We anticipate that BAB's CIR ratio, indicative of the Bank's operating efficiency, will continue to exceed the industry average in 2024-2025. Furthermore, BAB's return on total assets (ROA) over the past 5 years has remained stable at around 0.5% to 0.7%, but it remains lower compared to the industry average. This is largely attributed to the low returns from the loan portfolio, as well as the predominantly low-return portfolio held by BAB due to its focus on low-risk asset classes.

BAB's risk position is assessed as "Very strong", underpinned by well-defined and consistently applied risk management practices. The Bank maintains a conservative risk appetite toward both individual and corporate customers, emphasizing a low-risk approach. BAB's track record in managing asset quality consistently surpasses the industry average, reflecting prudent practices. Moreover, BAB faces lower level of potential risks compared its peers, attributed to its less complex business model and emphasis on the lending segment.

We assess that BAB continues to maintain asset quality and manage credit costs more effectively than the overall industry level, even in challenging business environments. Over the period of 2019-2023, BAB maintained an average annual loan growth rate of 7.2%, which is lower than the industry average of approximately 15%. Despite this, BAB consistently managed to maintain the problematic loan ratio (including Group 2 loans and Non-performing loans) under control, with a very low Non-Performing Loan (NPL). Although there was an increase in the NPL ratio in 2023, similar with the industry trend, BAB still achieved the lowest NPL ratio in the banking sector as of 31/12/2023 (standing at 0.92%, remarkably lower than the industry median of 2.3%). Additionally, BAB's non performing loans are primarily concentrated in auto loan products, as the sector is significantly impacted by unfavourable change in market conditions, resulting in the decrease in borrowers’ incomes; consequently auto loans witnessed a sharp decline while non-performing loans in this segment roughly maintained. FiinRatings expects that the economic situation in 2024 will not exhibit immediate and significant positive changes, especially in the fields of auto loans and real estate; this will lead to limited improvement in asset quality. Consequently, FiinRatings anticipates a slight increase in BAB's NPL ratio, which is expected to remain within the range of 1.0% to 1.4% in 2024-2025. This assessment is based on our expectation that BAB's management will continue to effectively handle and collect bad debts/problem debts, alongside the expiration of Circular 02/2023/TT-NHNN on June 30, 2024.

In terms of provisioning, BAB consistently maintains a significantly higher bad debt coverage ratio compared to the industry average, and the Bank’s provisions tend to increase in tandem with industry trends, especially since 2020 when the SBV issued regulations which provide guidance for loan restructuring in response to the Covid-19 pandemic. As of 31/12/2023, BAB's bad debt coverage ratio was at 131.0% (2022: 203.8%; 2021: 161.8%), and surpassed the industry average of 63.7% (2022: 68.9%; 2021: 60.9%). This ratio aligns with the leading group of private banks and those with highly profitable asset portfolios. Provision expenses (or credit cost) increased by 35.7% year-on-year, in line with the growth rate of the problematic loan group. However, debt recovered after provision processing declined by 34.0% compared to the previous year, amounting to VND 93 billion. Additionally, BAB's provision expense ratio increased to 0.2% (2022: 0.1%; 2021: 0.3%). FiinRatings anticipates that this ratio will remain within the 0.2-0.3% range between 2024 and 2025.

BAB's risk policies and management procedures are well-defined and consistent, incorporating standard risk control processes such as limit systems, risk measurement and reporting information systems, and regular reviews of internal audit and control systems. The Bank has developed expected loss models, internal credit rating systems, early warning systems, and action plans to monitor risks. BAB has long-established and clearly identified the Bank's risk appetite. Furthermore, BAB's risk management practices are deemed appropriate for the Bank's business model, thereby help mitigate risks and ensure a relatively sustainable operational orientation. Additionally, BAB establishes, assesses, and monitors material risks and key indicators of risk appetite, including indicators of capital adequacy ratio, liquidity safety, credit safety, and bad debt safety, with specific risk management strategies tailored to each type of material risk.

We assess that BAB's development of a comprehensive credit policy, which focused on lending to government-encouraged sectors with low risk and volatility, while restricting lending to highly volatile sectors like real estate, has significantly strengthened the Bank's risk position. BAB maintains a balanced loan portfolio, with processing and manufacturing accounting for 37% loan book, and agriculture, forestry, and fisheries accounting for 18% its loan book.

The remaining sectors are fairly distributed, which minimize concentration risk. With a loan portfolio predominantly composed of individual customers (65.5% of total outstanding loans in 2023), largely from target industry groups, BAB demonstrates risk dispersion in its lending activities. The 20 largest corporate customers are in processing, manufacturing, and agriculture industries; they account for 22% of BAB's total outstanding loans. These are reputable industry players with good credit quality, integrated into BAB's typical lending value chain. Moreover, BAB serves as an investment advisory unit for clients in these industries, enabling a comprehensive understanding of their business activities and close monitoring of cash flow.

Regarding credit risk management of related parties, BAB's outstanding loans to TH Group and TH branded customers amounted to VND 5,800 billion, which accounted for 5.8% of total outstanding loans as of 31/12/2023. TH branded customers largely consist of TH Group's suppliers, exhibiting improved business performance, especially post-Covid-19, based on financial data from the past 3 years. Approximately half of the total debt of these businesses is held by BAB, indicating their access to alternative sources of financing besides BAB. To enhance management efficiency, supervise lending activities, and mitigate risks for related customer groups, BAB has implemented credit risk limit warnings for these customers, all of which are currently classified as 'current / standard loans' (Group 1) on CIC.

BAB's funding and liquidity profile is evaluated as 'Adequate', attributed to the Bank's stable capital structure and its strong reliance on an actively engaged retail clientele. BAB demonstrates a robust ability to meet capital requirements through various stable sources, including customer deposits, equity, interbank long-term loans, and other long-term debt, surpassing the industry average. This is evident in BAB's stable funding ratio (FiinRatings adjusted), which showed a slight downward trend from 2019-2023 and reached 100.1% at the end of 2023; yet this figure of BAB remains higher than the industry average (98.8% as of YE2023). Furthermore, BAB consistently maintains an Net Stable Funding Ratio, which exceeds 100% according to Basel III standards. Even during a liquidity pressure period in the interbank market from 4Q2022 to 1Q2023, BAB ensures its funding stability by focusing on network expansion and implementing policies to attract long-term deposits (over 12 months), alongside with increased investments in Government bonds and highly liquid securities. The Bank's funding base is supported by a steady influx of customer deposits, particularly from the retail segment. Over the past five years (2019 – 2023), BAB's ratio of customer deposits to total funding has consistently ranged from 76.2% to 84.4%, aligning with the industry average of 65% to 70%. Notably, medium and long-term deposits increased by 14% by the end of 2023 compared to 2022, driven by customer deposit attraction programs and optimization of advantages from the value chain and TH-branded ecosystem. BAB maintains this customer deposit ratio fairly stable, mainly due to its business model, which focuses on less volatile sectors with low off-balance sheet items and a highly liquid portfolio of valuable securities. Although equity only accounts for a small proportion (approximately 7.7-8.2%) of total funding, BAB prioritizes increasing equity to enhance financial capacity, ensures meeting capital adequacy requirement and other operational safety indicators.

BAB's average funding cost in the recent 5-year period (2019-2023) is relatively high compared to the average level of banks due to the relatively low CASA. However, since mid-2023, the Bank has continuously reduced deposit rates. By March 2024, BAB's deposit interest rates for terms were equivalent to the industry average. With good liquidity position, stable customer deposits combined with strong interest rate reduction policies from the second quarter of 2023 until now, BAB's funding costs in 2024 - 2025 are expected to gradually decrease to an appropriate threshold, approaching the industry average..

In the coming time of 2024-2025, BAB plans to closely follow market developments to manage funding and lending interest rates flexibly, promptly, and in line with the Bank's objectives and operational strategy; also to ensure the balance of Funding Source – Funding Use, to be competitive enough to attract customers, to optimize NIM, and to achieve efficiency for the Bank. At the same time, the Bank also implemented new Fund Transfer Pricing Management (FTP) projects to promote CASA funding as well as the target tenors of the management policy. In our base case projection, FiinRatings assumes that BAB will successfully infuse new equity of about VND 900 billion, based on the bank's history and capital increase plan. According to this scenario, FiinRatings believes that BAB will maintain a stable funding ratio at a higher level in comparison to the average level of banks in the period of 2024-2025.

During the late 2022 to early 2023 period, the interbank market experienced liquidity stress, with several banks facing liquidity shortages, and interest rates consistently remaining high. Some banks were also impacted by the corporate bond crisis and faced credit limit reductions in the Interbank market due to liquidity risk concerns. However, amidst this challenging environment, BAB maintained a relatively favorable liquidity position, with financial metrics in the “safe” range, and suffered minimal impact from unsecured credit limits. BAB remained unaffected by the corporate bond crisis and had abundant capital during this period, reflected in significant idle funds invested in valuable securities and utilized in the Interbank market. In addition to maintaining its liquidity status, BAB implemented additional measures to ensure liquidity safety, including strengthening partnerships, expanding unsecured credit lines in the secondary market, utilizing valuable securities portfolios as liquidity buffers, and assessing and temporarily reducing credit limits with banks showing signs of potential risks since the 1H2022. BAB also restricted the utilization of unsecured sources in the Interbank market to further safeguard liquidity.

Overall, we observe improvements in BAB's funding ability, characterized by a tendency to increase more stable funding sources, which in turn generates momentum for credit growth while ensuring liquidity. Even in our stress test scenario, BAB appears to be able to maintain stable capital and liquidity, as evidenced by the stable funding ratio consistently exceeding 100% and the ratio of broad liquid assets to short-term wholesale funding consistently surpassing 1.0 times. Furthermore, BAB's funding structure characteristics and diversification strategies aimed at reducing dependence on wholesale capital are factors we will continue to monitor and update in BAB's credit profile.

OUTLOOK, UPGRADE & DOWNGRADE SCENARIOS

The 'Stable' outlook for BAB reflects our expectation that the Bank will maintain the rating score for the next 24 months.

Upgrade Scenario:

Factors that could, individually or collectively, lead to review for positive rating action or upgrade for BAB:

- The Bank succeeded in expanding its customer base; credit growth averaged or higher than the banking system during the same period and the Bank was able to maintain this growth sustainably, without changing the current risk position; and
- Net interest margins and capital buffers improved (reflected by NIM and CAR being on par with the industry average) and stayed around 3.4% for NIM and 12% for CAR, respectively.

Downgrade Scenario:

Factors that could, individually or collectively, lead to review for negative rating action or downgrade:

- BAB's business position is weakened (reflected by the Bank’s market share) due to failure to maintain existing customer base, weak credit growth compared to previous years;
- Asset quality has deteriorated due to the Bank's expansion, changes in lending strategies to high-risk industries or significant investments in low-liquidity assets or restructured liabilities that continue to increase sharply along with poor debt recovery. Weakening asset quality will be reflected in non-performing loans and problematic loans figures.
- Liquidity position and funding abilities go through difficulties, reflected by the decline in important indicators such as stable funding ratio, broad liquid asset ratio, loan-to-deposit ratio; and
- Pressure from higher funding cost, as well as from continuously rising operating cost compared to current.

RATING METHODOLOGY

The rating methodology explains FiinRatings' approach to assessing the credit risk of companies in Vietnam. This methodology is intended as general guidance to help companies, investors, and other market participants to understand how FiinRatings looks at quantitative and qualitative factors significant in explaining rating outcomes in general and specific for each sector that we cover.

In addition, certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please follow the link below for the Rating Methodology and Related Criteria:

- Rating methodology for banks in Vietnam

Or refer to the following link for more details on the general ranking methodology:

- General Rating methodology

CREDIT RATING HISTORY

Company Name	Type	Publication date	Rank	Prospect
Bac A Commercial Joint Stock Bank	Issuer Rating – Initial	01 April 2024	A-	Stable

RATING SCALE AND DEFINITION

We employ below rating scale in assigning ratings for all issuers across industries and sectors that we cover in Vietnam. The rating scale used by FiinRatings is the national scale, therefore, it must not be equated with or represented as a rating on the scale used by any other rating agencies.

Definition and interpretation	Rating scale
Group 1: **Extremely strong** capacity to meet financial obligations.	**AAA**
Group 2: **Very strong** capacity to meet financial obligations.	**AA+**
	AA
	AA-
Group 3: **Strong capacity** to meet financial obligations but somewhat susceptible to adverse economic conditions and changes in circumstances.	**A+**
	A
	A-
Group 4: **Adequate capacity** to meet financial commitments but more vulnerable to adverse developments and economic conditions.	**BBB+**
	BBB
	BBB-
Group 5: **Moderate capacity** to meet financial obligations but less vulnerable than other speculative issuers.	**BB+**
	BB
	BB-
Group 6: **Weak capacity** to meet financial obligations. Sensitive to business, financial and economic conditions. High risk.	**B+**
	B
	B-
Group 7: **Very weak** capability or very likely to get into default. Very sensitive to business, financial and economic conditions. Substantial risk.	**CCC+**
	CCC
	CCC-
	CC
	C
Group 8: **Default**. Payments on an obligation are not made on the date due or the issuer becomes insolvent. The 'D' rating also will be used upon the filing of a bankruptcy petition or the taking of similar action.	**SD, D**

OWNERSHIP DISCLOSURE AND STATEMENTS

At the time of the publication, the following information is provided as required by current regulations and as a part of our compliance policies in providing credit ratings:

- BAB's percentage of equity ownership at FiinRatings: none**
- FiinRatings' percentage of equity ownership at BAB: none
- FiinRatings' other employee percentage of equity ownership at BAB: none
- BAB's investment value of bond(s) issued by FiinRatings: none
- FiinRatings' investment value of bond(s) issued by BAB: none
- BAB's investment value of other debt instruments issued by FiinRatings: none
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FIINRATINGS JOINT STOCK COMPANY

Public Credit Rating Announcement No.: 01-C31-2024

Nguyen Quang Thuan, FCCA

Chief Executive Officer

Hanoi, 01 April 2024

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