

LIENVIET POST BANK (LPB) - UPDATE

Market Price VND9,400	Target Price VND12,200	Dividend Yield 10.6%	Rating ADD	Sector FINANCIALS
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Outlook – Short term



Outlook – Long term



Valuation



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Key changes in the report

- FY19F net profit is reduced by 8%
- Target price is reduced to VND12,200

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	17,143
52w low (VND)	8,476
3m Avg daily volume (shares)	0.9mn
3m Avg daily value (VNDmn)	8,340
Market cap (VNDbn)	8,347
Outstanding shares (m)	888
Free float (%)	20
TTM P/E (x)	8.6
Current P/B (x)	0.7

Ownership

Vietnam Post	11.5%
H.T.H Ltd. Co.	4.5%
Mr.Nguyen Duc Huong	4.5%
Others	79.5%

Source: VNDIRECT

A rise in funding costs and higher provision expense on the back of soaring bad debt hampered net profit growth in FY18.

Higher funding costs led to a 48bp net interest margin (NIM) compression in FY18, although asset yields improved on retail lending expansion. The surge in funding costs was driven by: 1) a fall in demand deposits by 37.3% yoy as fast network expansion helped LPB to raise ample deposits from individuals who prefer term deposits; 2) issuance of nearly VND4,000bn long-term valuable papers to reduce the ratio of short-term funds used for medium/long-term loans. As a result, FY18 net interest income (NII) declined by 4.0% yoy, despite 18.5% yoy loan growth.

Loss in non-interest income (Non-II) widened from -VND124bn in FY17 to -VND141bn in FY18, due to provision for investment securities on a choppy stock market and higher expense incurred in this business. Net fee income, however, rose 128.5% yoy in FY18 as LPB raised service fees in Jun 2018. As NII fell and non-II recorded bigger losses, total operating income (TOI) reduced 4.4% yoy in FY18.

Operating expense (opex) ticked up 8.4% yoy and provision expense increased 18.5% yoy as bad debt spiked. The rise in opex was driven by network expansion. Opex increased slightly in FY18 because headcount only rose 10.0% in FY18 compared to FY17 when LPB actively recruited new staff (headcount rose 43.3% in FY17) to prepare for network expansion. Provision expense increased 18.5% yoy as the non-performing loan (NPL) ratio spiked from 1.1% at end-FY17 to 1.4% at end-FY18. We believe that the rise in bad debt was partially due to a new regulation effective Aug 2018 prohibiting banks from purchasing corporate bonds issued for debt restructuring.

Target price reduced from VND12,900 to VND12,200 due to lower profit forecast for FY19F. FY18 net profit reached VND960bn (-29.8% yoy), fulfilling 93% of our forecast. With a higher NPL ratio, we increase provision expense assumptions for FY19F as we expect LPB will ramp up write-offs to reduce bad debt. We expect profit growth to recover in FY19F as the rise in funding costs will moderate, asset yields will increase due to retail lending at new transaction offices and the rise in the NPL ratio is unlikely to be as steep as seen in FY18. LPB currently trades at 36.1% discount versus regional peers in term of FY19F P/B, although FY19F ROE is projected to be 11.0% lower than peers. We therefore believe that LPB is trading below fair value and maintain our Add call in the stock.

Financial summary (VND)	12-16A	12-17A	12-18A	12-19E
Net interest income (bn)	4,024	5,227	5,020	5,705
Net interest margin	3.5%	3.6%	3.1%	3.2%
Total operating income (bn)	3,872	5,103	4,879	5,653
Total provision charges (bn)	(492)	(522)	(618)	(703)
Net profit (bn)	1,063	1,368	960	1,099
Net profit growth	203.8%	28.7%	(29.8%)	14.5%
Adjusted EPS	1,397	1,657	1,095	1,104
BVPS	11,588	12,451	12,954	13,012
ROAE	13.3%	15.4%	9.8%	10.1%

Source: VNDIRECT

2018 RECAP: A RISE IN FUNDING COSTS AND PROVISION EXPENSE HAMPERED PROFIT GROWTH

Figure 1: Results comparison (VNDbn, unless otherwise noted)

Profit & Loss Statement	4QFY17	4QFY18	%yoy	FY17	FY18	%yoy	FY18 forecast	%FY18 forecast	Comments
Net interest income	1,324	1,429	8%	5,227	5,020	-4%	5,224	96%	Slightly below our forecast as FY18 actual NIM (3.1%) was lower than our forecast (3.2%) because funding costs rose faster than our expectations.
Non-interest income	25	(23)	n/m	(124)	(141)	14%	(352)	n/m	Better result than our forecast thanks to higher fee income growth than our projection, driven by an increase in service charges in Jun 2018. In addition, LPB incurred less expenses on other activities than our forecast.
Operating revenue	1,349	1,406	4%	5,103	4,879	-4%	4,872	100%	In line with our forecast.
Operating expenses	(974)	(940)	-3%	(2,813)	(3,048)	8%	(3,069)	99%	
Pre-provision profit	375	465	24%	2,290	1,831	-20%	1,803	102%	
Provision expenses	(40)	(267)	562%	(522)	(618)	19%	(469)	132%	Above our forecast as NPL surged in FY18. As a result, credit cost was higher than our forecast.
Pretax profit	334	199	-41%	1,768	1,213	-31%	1,333	91%	Below our forecast due to large provision expense.
Net profit	242	134	-45%	1,368	960	-30%	1,032	93%	

Source: VNDIRECT, COMPANY REPORT

2019 OUTLOOK: A BETTER YEAR AHEAD

FY18 profit was hampered by a big drop in NIM and higher provision expense due to the surge in bad debt. There were some headwinds for LPB in FY18, including both internal issues at the bank and stricter regulations from the State Bank of Vietnam (SBV). We expect a recovery in FY19F based on the following considerations:

- Fast network expansion attracted ample deposits from individual customers, who prefer term deposits. As a result, the current account and savings account rate declined from 28.6% in FY17 to 18.4% in FY18. On the other hand, lending at new transaction offices has yet to catch up with fund mobilisation. As a result, funding costs increases were unmatched by the increase in asset yields, leading to a fall in NIM. We expect lending will improve at the new transaction offices in FY19F, driven by retail lending, which will lead to a rise in asset yields, thereby supporting interest income growth.
- SBV's tightening of credit hurt LPB's interest income in 1H18. In mid-FY18, SBV announced that it would not lift the credit quota for banks. As a result, 1H18 loan growth only reached 13.8% versus end-FY17, close to the credit quota of 14.0%. Meanwhile deposit growth touched 14.1% versus end-FY17, as LPB raised deposits to prepare for the lending high season towards year-end, despite a low loan-to-deposit ratio of 71.8% at end-1H18, in order to meet its aggressive targets for 22% credit growth for the year. As SBV tightened credit growth, LPB aggressively reduced deposits in the last two quarters of FY18, but the strong mobilisation in 1H18 hurt interest income, nonetheless. Going into FY19F, SBV remains cautious on credit growth. We therefore expect LPB to grow the deposit base more conservatively and more in line with credit growth.

- In FY18, LPB issued nearly VND4,000bn in long-term valuable papers to reduce its ratio of short-term funds used for medium/long-term loans. LPB reduced this ratio below 40% in FY18, satisfying the new regulation which took effect in Jan 2019. We do not expect the same amount of valuable paper issuance this year and therefore do not expect funding costs to rise as fast as it did last year.
- NPL ratio spiked from 1.1% at end-FY17 to 1.4% at end-FY18. We believe it was impacted by a new regulation effective Aug 2018 which prohibits banks from purchasing corporate bonds issued as part of a debt restructuring exercise. Although we see bad debt is rising due to the expansion in retail lending, the surge in bad debt last year was largely driven by a change in regulations. Although this has impacted all banks, LPB has had lower provision buffers and weaker pre-provision operating profit than many of its peers and therefore has not been able to write off bad debt as aggressively. We believe that the pace of bad debt increases will cool in FY19F.

Figure 2: Earnings revision (VND bn, unless otherwise noted)

Profit & Loss Statement	2018A	2019F		Change	Comments
		Old forecasts	New forecasts		
Net interest income	5,020	5,988	5,705	-5%	As funding costs increased faster than our expectation, we revise down FY19F NIM assumption by 11bp versus previous forecast.
Non-interest income	(141)	(204)	(52)	n/m	We increase non-interest income forecast as fee income growth was better than projection and LPB was able to control miscellaneous expenses better than it did in the past.
Operating revenue	4,879	5,784	5,653	-2%	
Operating expenses	(3,048)	(3,702)	(3,561)	-4%	LPB upgraded a lot of postal transaction offices to bank transaction offices in FY18 and the cost-to-income ratio (CIR) reached 62.5% in FY18. We expect the same pace of network expansion in FY19F and thus lower our CIR forecast for FY19F from 64.0% previously to 63.0%.
Pre-provision profit	1,831	2,082	2,091	0%	
Provision expenses	(618)	(530)	(703)	32%	As NPL increased sharply in FY18, we lift our provision expense forecast for FY19F as we expect LPB will ramp up provisioning to write-off bad debt, in order to maintain NPL ratio at 1.4% and loan-loss-reserves at 86.9% in FY19F.
Pretax profit	1,213	1,552	1,389	-11%	
Net profit	960	1,201	1,099	-8%	

Source: VNDIRECT

VALUATION

We reduce our target price by 6% to VND12,200 on higher provision expense assumptions as NPL surged in FY18. Our target price is based on residual income valuation (70% weighting, COE: 14.7%, LTG: 3.0%) and P/B multiple valuation (30% weighting, target P/B of 1.0x in FY19F). LPB's stock price has been weak due to poor performance in FY18. Currently, LPB trades at a 36.1% discount versus regional peers in terms of FY19F P/B, while LPB's FY19F ROE is projected at 10.1%, slightly lower than the peer average ROE of 11.4% forecasted for the same period. Due to lower ROE, we apply a target P/B of 1.0x for FY19F book value per share, which is 11.3% discount versus peer's average FY19F P/B. We believe LPB's profit growth will recover in FY19F. Our target price corresponds to a FY19F P/B of 0.9x.

Figure 3: Our target price calculation

Approach	Weighting	Fair value (VND/share)	Contribution (VND/share)
Residual income	70%	11,863	8,304
P/B multiple (at 1.0x FY19F P/B)	30%	13,012	3,904
Target price (VND/share)			12,208
Target price (VND/share, rounded)			12,200

Source: VNDIRECT

Figure 4: Residual income valuation, based on our estimates

Key assumptions	2019E	2020E	2021E	2022E	2023E	Terminal
Risk free rate	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Equity risk premium	11.0%	11.0%	11.0%	11.0%	11.0%	11.0%
Beta	0.9	0.9	0.9	0.9	0.9	0.9
Cost of equity	14.7%	14.7%	14.7%	14.7%	14.7%	14.7%
Long-term growth rate						3.0%
<i>(in VND bn, otherwise noted)</i>						
Opening shareholder's equity	10,201					
PV of RI (5 years)	(483)					
PV of Terminal value	818					
Implied Equity value	10,536					
No. of outstanding shares (m shares)	888.1					
Implied value per share (VND/share)	11,863					

Source: VNDIRECT

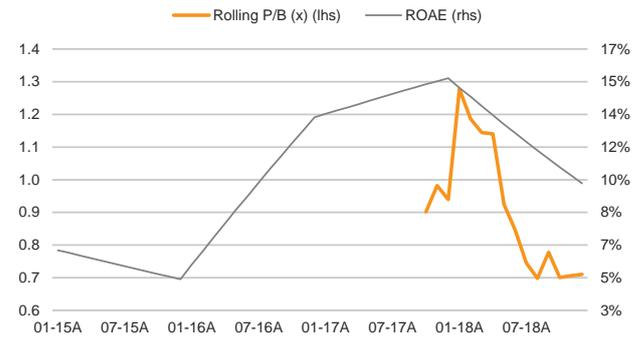
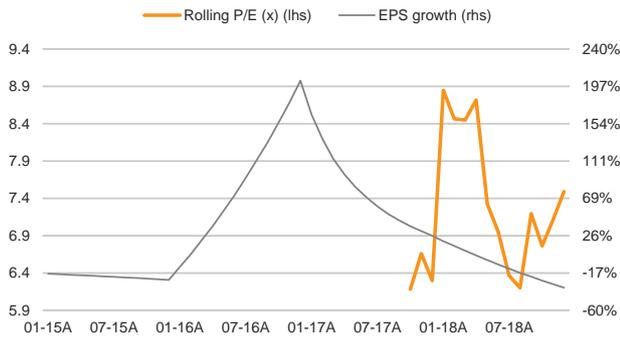
Figure 5: Banks multiple comparison

Banks	Countries	Bloomberg code	Market cap (US\$m)	TTM ROA (%)	TTM ROE (%)	ROE FY19F (%)	Current P/B (x)	TTM P/E (x)	FY19F P/B (x)	FY19F P/E (x)
Federal Bank	India	FB IN	2,599	0.8%	9.6%	11.8%	1.4	15.3	1.3	11.5
Bank Permata	Indonesia	BNLI IJ	2,182	0.4%	3.1%	3.9%	1.4	45.7	1.3	35.2
Asia Commercial Joint Stock Bank	Vietnam	ACB VN	1,688	1.7%	27.7%	24.8%	1.8	12.9	1.5	10.0
Alliance Bank Malaysia Berhad	Malaysia	ABMB MK	1,576	1.1%	10.4%	10.7%	1.1	11.1	1.1	10.3
Affin Bank Berhad	Malaysia	ABANK MK	1,093	0.7%	5.9%	5.6%	0.5	8.7	0.4	8.3
Average				0.9%	11.4%	11.4%	1.2	18.8	1.1	15.1
LienViet Post Bank	Vietnam	LPB VN	363	0.6%	9.8%	10.1%	0.7	8.6	0.7	8.5

Price as of 13 Mar 2019

Source: CGS-CIMB RESEARCH, VNDIRECT

Valuation



Income statement

(VNDbn)	12-17A	12-18A	12-19E
Net interest income	5,227	5,020	5,705
Non interest income	(124)	(141)	(52)
Total operating income	5,103	4,879	5,653
Total operating costs	(2,813)	(3,048)	(3,561)
Pre-provision operating profit	2,290	1,831	2,091
Total provision charges	(522)	(618)	(703)
Income from associates & JVs			
Net other income			
Pre-tax profit	1,768	1,213	1,389
Tax expense	(400)	(253)	(290)
Profit after tax	1,368	960	1,099
Minority interest	0	0	0
Net profit	1,368	960	1,099

Balance sheet

(VNDbn)	12-17A	12-18A	12-19E
Gross loans to customers	100,621	119,193	137,072
Loans to banks			
Total gross loans	100,621	119,193	137,072
Securities - total	32,650	36,356	40,988
Other interest earning assets	23,292	11,429	12,574
Total gross IEAs	156,563	166,978	190,635
Total provisions	(2,015)	(2,173)	(2,513)
Net loans to customers	99,392	117,710	135,387
Total net IEAs	154,548	164,806	188,122
Cash and deposits	893	1,664	1,764
Total investments	325	325	344
Other assets	7,668	8,300	8,798
Total non-IEAs	8,886	10,289	10,906
Total assets	163,434	175,095	199,028
Customer deposits	128,275	124,948	144,940
Cds outstanding	6,157	10,120	10,120
Customer interest-bearing liabilities	134,433	135,068	155,060
Bank deposits	1,332	7,345	7,712
Broad deposits	135,764	142,413	162,772
Other interest-bearing liabilities	14,709	17,602	19,740
Total IBLs	150,473	160,015	182,512
Deferred tax liability			
Other non-interest bearing liabilities	3,577	4,878	4,960
Total non-IBLs	3,577	4,878	4,960
Total liabilities	154,050	164,894	187,471
Share capital	6,460	7,500	8,881
Additional paid-in capital	0	0	0
Treasury shares			
Retained earnings reserve	1,794	1,432	1,407
Other reserves	1,129	1,268	1,268
Shareholders' equity	9,383	10,201	11,557
Minority interest	0	0	0
Total equity	9,383	10,201	11,557
Total liabilities & equity	163,434	175,095	199,028

	12-17A	12-18A	12-19E
Growth rate (yoy)			
Cust deposit growth	15.6%	(2.6%)	16.0%
Gross cust loan growth	26.3%	18.5%	15.0%
Net interest income growth	29.9%	(4.0%)	13.6%
Pre provision operating profit growth	24.4%	(20.0%)	14.2%
Net profit growth	28.7%	(29.8%)	14.5%
Growth in IEAs	15.8%	6.6%	14.1%
Share value			
Basic EPS (VND)	1,858	1,228	1,238
BVPS (VND)	12,451	12,954	13,012
DPS (VND)	1,000	1,000	600
EPS growth	25.7%	(33.9%)	0.8%

Key ratios

	12-17A	12-18A	12-19E
Net interest margin	3.6%	3.1%	3.2%
Cost-income ratio	(55.1%)	(62.5%)	(63.0%)
Reported NPLs / gross cust loans	1.1%	1.4%	1.4%
Reported NPLs / net cust loans	1.1%	1.4%	1.4%
GP charge / average cust loans	0.6%	0.6%	0.5%
Total CAR	10.3%	10.0%	10.1%
Loan deposit ratio	74.8%	88.2%	88.4%
Margins and spreads			
Return on IEAs	7.9%	8.6%	8.7%
Cost of funds	4.5%	5.7%	5.7%
Interest return on average assets	3.4%	3.0%	3.0%
ROAE	15.4%	9.8%	10.1%

Source: VNDIRECT

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Definition:

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- Hold The stock's total return is expected to be between negative 10% and positive 15% over the next 12 months.
- Reduce The stock's total return is expected to fall below negative 10% over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings

Definition:

- Overweight An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
- Neutral A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
- Underweight An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

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- Neutral A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
- Underweight An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.

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