18 March 2020

Impacts of new regulations of interest rates on the banking sector

Summary

The State Bank of Vietnam (SBV) has recently issued new policy rates effective as of March 17, 2020, as highlighted in the table below. The new regulations aim in general to reduce the funding cost of banks, and increase interest payments to banks' deposits at the SBV. This is to better facilitate the decrease in lending interest rates to better support the economy. This new policy of SBV is in line with our forecast on deposit/lending rate trend for the whole year 202: In our base case scenario, we forecast for deposit interest rate to reduce 70 bps YoY. Lending interest rates will be reduced 50 bps YoY, with the exception for the special clients, who are negatively affected by the epidemic, for whom the decline will be from 150 bps YoY.

Table: Policy rates

No.	Items	Current regulations	Previous regulations	Difference (bps)
	Commercial banks to customers			
	Caps on deposit interest rates			
1	- Demand deposits and deposits under 1 mo.-term	**0.50%**	0.80%	(30)
2	- Deposits with terms from 1 mo. to 6 mo.	**4.75%**	5.00%	(25)
	Cap on lending interest rates			
3	- Short-term lending in VND to 6 priority sectors	**5.50%**	6.00%	(50)
	The central bank to commercial banks, fixed rate			
4	- OMO reverse repo lending rate	**3.50%**	4.00%	(50)
5	- Discount lending rate	**3.50%**	4.00%	(50)
6	- Refinancing rate	**5.00%**	6.00%	(100)
7	- Interbank clearing lending rate	**6.00%**	7.00%	(100)
8	- Interest rates payable to required reserve in VND	**1.00%**	0.80%	20
	The central bank fixed rate to the VDB, VBSP, people's credit funds, micro finance institutions,			
9	- Interest rates payable to deposits in VND	**1.00%**	0.80%	20

Source: The State Bank of Vietnam, SSI Research

Note: VDB: the Vietnam Development Bank, VBSP: Vietnam Bank for Social Policy

1. Impact of lower rate offered by commercial banks to customers

The lower caps on deposit rates (applicable to demand deposits and less than 6-month term deposits) and lending rates (applicable to short-term lending in VND to six priority sectors as regulated by the government) are expected to have immediate direct impacts on market rates.

We have reviewed deposit rates across different banks, and note that state-owned banks (Agribank, BIDV, VCB, and CTG) and commercial bank TCB have trended downwards previously, and have fallen to under the new imposed caps. Therefore, we don't expect the new caps to have much impact on these banks. Instead, deposit rates of most top Tier-2 banks are now higher than the new caps, and will be subsequently reduced to suit the new regulations.

Table: Impacts of new caps on deposit rates

Bank	Current short-term deposit rate (Mar. 16, 2020)	Decrease in deposit expenses in 2020 (VND bn)
ACB	<1M: 0.8%. 1M - 5M: 5%. 6M: 6.5%	471
BID	Demand: 0.1%. 1M-2M: 4.3%. 3M-5M: 4.8%	
CTG	Demand: 0.1%. 1M-2M: 4.3%. 3M-5M: 4.8%	
HDB	<1M: 0.7%-0.8%. 1M - 5M: 5%. 6M: 6.8%	146
LPB	<1M: 0.8%. 1M-2M: 4.9% 3M-5M: 5%. 6M: 6.1%	159
MBB	<1M: 0.8%. 1M: 4.8%. 2M - 5M: 5%. 6M: 6.4%	411
TCB	Demand: 0.1%. 1M-5M: 4.1%	
TPB	Demand: 0.6%. 1M-5M: 4.75% - 4.95%	28
VCB	Demand: 0.1%. 7-14D: 0.5%. 1M-2M: 4.3%. 3M: 4.8%. 6M: 5.3%	
VIB	<1M: 0.8%. 1M - 5M: 5%	119
VPB	<1M: 0.8%. 1M - 2M: 4.5%. 3M-5M: 4.6%. 6M: 6.9%	171

Source: SSI Research

In detail, we expect that the downward adjustment of offered deposit rates as laid out above would translate into reduction of the funding cost of banks in 2020, such as ACB (VND 471 bn), MBB (VND 411 bn), VPB (VND 171 bn), etc in our estimate. On the other hand, VCB, BID, CTG and TCB (among others) could continue to enjoy the much lower cost for demand deposits, because their advantages in payroll and payment services would likely be enough to retain their CASA clients.

Moreover, deposits will be directed towards longer-term for banks to improve their operation ratios in compliance with the current regulations.

As the difference in deposit rates will be narrowed down among Tier-3 banks and the rest, banks with better creditworthiness and/or better financial health will likely attract more depositors, similar to the situation in 2011. In that case, we expect the interbank lending business of Tier 1 and top Tier-2 banks to thrive.

In the meantime, the new cap on short-term lending interest rates to six priority sectors will not have significant impact on these sectors. State-owned commercial banks (SOCBs) are known to have the largest credit balance of this kind. In 2019, Agribank, BID and VCB cut these lending interest rates three times to only 5% p.a., which is already lower than the new cap of 5.5% p.a. On the contrary, this rate is currently 6% p.a. at CTG, and should be thus reduced by 50 bps immediately.

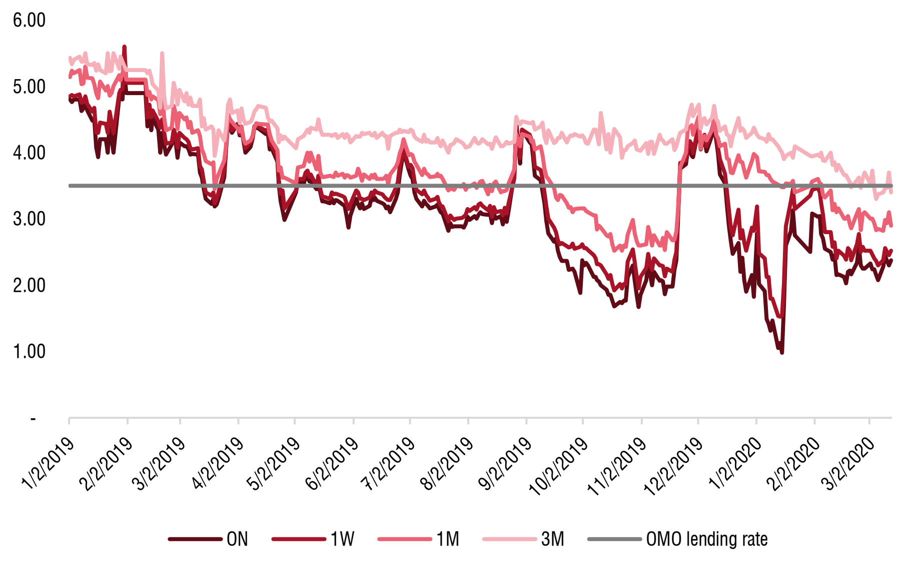
2. Of rates between the SBV and commercial banks

To support commercial banks in the lowering of lending interest rates and the restructuring of loan payments, the SBV has raised deposit interest rates of various types of credit institutions at the SBV (Items No. 8&9). We estimate total required reserves of the sector at VND 164 tn, equivalent to 1.86% of total deposits in 2019. The +20 bps increase in interest rates applied to required reserves in VND would directly bring about an additional VND 247 bn of interest income to the sector in 2020. We believe the total deposits of the VDB, the VBSP, the people's credit funds, and various microfinance institutions at the SBV are significant in scale.

Regarding the rate of lending by the SBV to commercial banks (Items No. 4-7), impacts would be indirect, as there is little demand for SBV lending lines at the moment amidst abundant liquidity in the system. These rates will instead act as caps for interbank interest rates.

Interbank rates have trended downwards recently, and we expect them to stay below 3.5% during the remainder of 2020. This expectation applies to even the 3 month term. This may one way or another lead to NIM contraction in the interbank market business.

Interbank rate



Source: Bloomberg, SSI Research

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HO CHI MINH CITY
Floor 18th, Office Tower 2, Saigon Centre, 67 Le Loi Street, Ben Nghe Ward, District 1, Ho Chi Minh City
Tel: (84-28) 3636 3688
Fax: (84-28) 3636 3668
Email: info@ssi.com.vn

HANOI
1C Ngo Quyen Street, Ha Noi City
Tel: (84-24) 3936 6321
Fax: (84-24) 3936 6311
Email: info@ssi.com.vn

4. CONTACT INFORMATION

Research & Advisory Center

Linh Nguyen

Research Manager

☎ Tel: (84-24) 3936 6321 ext. 679

linhntt1@ssi.com.vn

Ha Nguyen

Research Manager

☎ Tel: (84-24) 3936 6321 ext. 680

hant4@ssi.com.vn

Phuong Hoang

Deputy Managing Director,

Head of Research & Advisory Center

phuonghv@ssi.com.vn

Hung Pham

Associate Director

hungpl@ssi.com.vn