

CREDIT QUALITY AT VIETNAM STATE CAPITAL COMMERCIAL BANKS

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Abstract: *This article studies the current status of credit quality of Vietnamese state-owned commercial banks in the period 2018-2022. Based on the application of fundamental theory on credit quality of commercial banks, the article aims to analyze the current status of credit quality of commercial banks with state capital in Vietnam. From there, propose appropriate solutions to improve the credit quality of Vietnamese state-owned commercial banks.*

• Keywords: *credit quality, state-owned commercial banks, bad debt.*

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1. Basic issues about credit quality of commercial banks

a. Bank credit concept

Bank credit is a borrowing relationship between a bank and a customer, in which the bank transfers to the customer the right to use an amount of value (in the form of goods or currency) under certain conditions and for a certain period of time. certain period of time that the two parties have agreed upon based on the principle of refund.

b. Perspectives on credit quality of commercial banks

For commercial banks: “Credit quality is a term that reflects whether a commercial bank’s credit activities are good or not. It is made up of two factors: safety level and profitability.” of banks due to credit activities.”

Credit quality is reflected in the goals of growth, safety and profitability of business capital in accordance with planned goals and legal regulations in each period. Attract many customers while still ensuring credit principles. Specifically:

- Level of capital safety: To ensure the safety of loan capital and the safety of capital, it is required that before granting credit to borrowers, commercial banks must carefully consider their legal capacity and capacity. Financial strength, ability to meet loan conditions, capital use plan of the borrower... At the same time, the bank must evaluate the creditworthiness of the borrower. If the borrower’s creditworthiness is low, it means the risk is high, which means low credit quality.

- Level of profitability: credit activities must be effective, which means banks must collect principal and interest when lending. Therefore, minimizing bad debts while bringing profits to the bank, helping the bank expand its scale and operating network...

For customers, credit quality is reflected in the fact that the bank’s services satisfy customer needs, the amount of money the bank lends must have reasonable interest rates and terms, and simple procedures. Convenient, attracts many customers but still ensures credit principles.

2. Current status of credit quality of commercial banks with Vietnamese State capital

a. Overview of commercial banks with state capital in Vietnam

Currently, the system of credit institutions in Vietnam includes 7 commercial banks with dominant State capital, including: Agribank, Vietinbank, Vietcombank, BIDV, Limited Liability Bank, a member of Global Petroleum. Ocean One Member Limited Liability Bank and Construction One Member Limited Liability Bank. Including 3 banks: Global Petroleum Bank Limited, One member Ocean Bank Limited, One Member Construction Bank Limited is undergoing merger procedures. and merge. In this article, the author surveys and evaluates the factors (macro, micro) affecting the business performance of the four largest banks in Vietnam: Agribank, Vietinbank, Vietcombank and BIDV.

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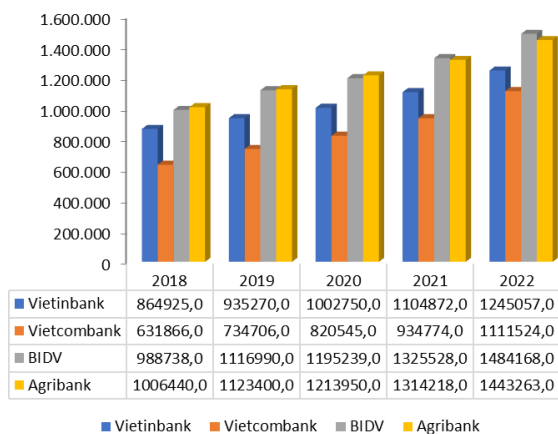
b. Current status of credit quality of commercial banks with state capital in Vietnam

** Credit balance and growth of credit balance of commercial banks with Vietnamese State capital*

Total outstanding credit is an indicator that reflects the amount of money allocated by commercial banks with State capital to the economy at a time. Total outstanding debt includes short-term, medium-term and long-term loan balance. Low total outstanding debt shows that the bank’s credit activities are weak, the bank’s inability to expand its customers, its poor marketing ability, and low staff qualifications... However, this indicator If high, the loan quality is not necessarily good, bad debt is likely to occur. However, if total outstanding debt increases continuously over the years, it shows an increasing trend in credit quality. Specifically, outstanding credit debt of commercial banks with state capital is as shown in Figure 1 below:

From 2018 to 2022, outstanding loans of commercial banks with state capital increased every year, higher than the average increase in credit growth of the entire banking system, the highest in 2020 was an increase of 17.05 % compared to 2019. In 2021 compared to 2002, the lowest credit growth in the past 5 years is 2.23%.

Figure 1: Credit balance of commercial banks with Vietnamese State capita (Billion VND)



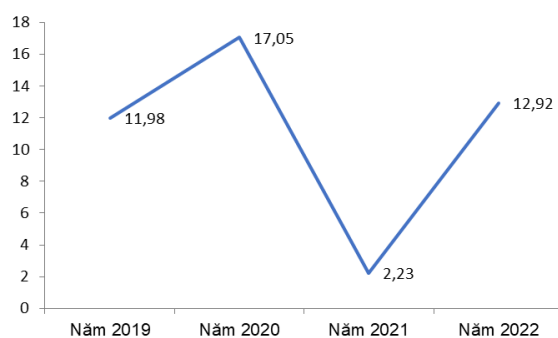
** Credit growth rate of commercial banks with Vietnamese State capital*

The average credit growth rate of commercial banks with state capital from financial reports over the years is shown in Figure 2.

Regarding growth rate, from 2018 to 2022 it can be said that commercial banks with state capital in Vietnam have a steady growth rate. In 2022 compared to 2018 it is 51.31%. If considering the growth rate of

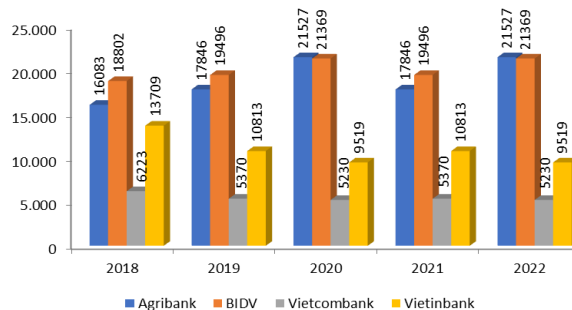
each bank, Vietcombank achieved the highest growth rate of 75.19%, BIDV 50.10%, Vietinbank 43.9%; and Agribank is 43.4%. In 2018, Vietcombank’s customer loans only reached 631,866 billion VND, but by 2022 this number will reach 1,111,524 billion VND, an increase of 75.92%, of which growth in 2022 compared to 2021 will reach the highest level of 18.9%, in 2020 compared to 2019, the lowest rate was 11.68%. Similarly, for BIDV, the average growth rate over 5 years is 11.51%, the growth rate of next year compared to the previous year from 2022 to 2018 is: 11.96%, 10.90% respectively. %, 10.21%, 12.97% Thus, growth in 2021 compared to 2020 is 10.90%, the lowest growth rate in the period 2018 to 2022. But in 2019 compared to 2018, growth is at a high level at most 12.97%. Likewise, the average growth rate over 5 years of Vietinbank and Agribank also reached about 10%.

Figure 2: Average credit growth rate of Vietnamese state-owned commercial banks from 2018-2022 (%)



** Bad debt ratio of commercial banks with Vietnamese State capital*

Figure 3: Bad debt of Vietnamese state-owned commercial banks from 2018-2022 (Billion VND)

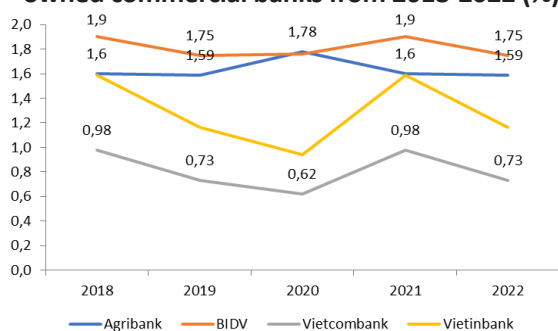


Source: Annual reports of Vietnamese state-owned commercial banks (2018-2022)

Bad debt ratio is an important financial indicator evaluating the credit quality of Vietnamese commercial banks. Once a commercial bank has a high bad debt

ratio, it proves that credit activities in general and lending in particular are of low quality and high risk, thereby requiring a review of all credit activities. However, bad debt is an unavoidable problem in credit activities, it is important for banks to maintain it at an acceptable level. According to the World Bank, this rate is acceptable at less than 5%, good at 1-3%. In the period from 2018 to 2022, the bad debt ratio of Vietnamese state-owned commercial banks averaged 1.38%, smaller than the allowed level of 3%.

Figure 4: Bad debt ratio of Vietnamese state-owned commercial banks from 2018-2022 (%)



Source: Annual reports of Vietnamese state-owned commercial banks (2018-2022)

According to statistical data on the financial statements of Vietnamese state-owned commercial banks in 2022, although economic sectors are heavily affected by the epidemic and the banking and finance industry is not an exception. But in general, the bad debt ratio of most Vietnamese state-owned commercial banks has decreased, except for BIDV and Agribank.

As of December 31, 2022, commercial banks with Vietnamese state capital all controlled the bad debt ratio below 3%. However, the absolute number of bad debts of Vietnamese state-owned commercial banks increased while the bad debt ratio decreased, the reason the growth rate of outstanding loans increased higher than bad debt. In 2022, state-owned banks will well control the bad debt ratio below 3%. Specifically, Vietcombank and Vietinbank are the two with bad debt ratios below 1%. Vietcombank's bad debt ratio of 0.62% in 2020 is also a low level in this bank's history. Meanwhile, VietinBank had 0.94% remaining in 2020. In addition, in 2020, VietinBank also settled all bad debts at the Asset Management Company (VAMC), the loan bad debt coverage ratio and On-balance sheet bonds have also improved, increasing to 130% compared to 1.16% in 2019 and is the lowest bad debt ratio in the period 2015-2020. BIDV's bad debt ratio in 2020 was 1.76%, a decrease compared

to 2019. The bad debt ratio of Bidv and Agribank in 2020 increased compared to 2019 but the increase was not significant because these are banks operated by BIDV. The state-dominated business has healthy business operations and a big brand nationwide. All banks have customer portfolios that have performed well over the past many years.

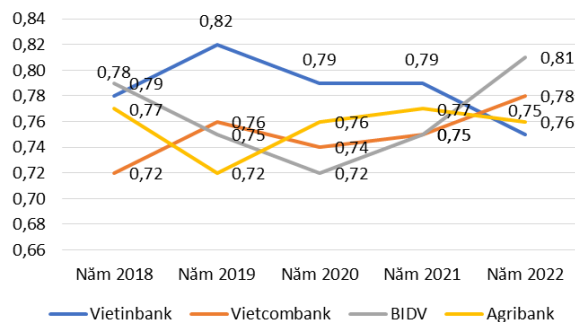
What is worth noting for Vietnamese state-owned commercial banks in 2020 is that although the bad debt ratio almost decreased, debt that needs attention (group 2 debt) increased, especially Vietcombank increased by 70%. This is also a matter of concern because if customers continue to be unable to repay their debts, these debts will move from group 2 to the bad debt group. In addition, group 5 debt tended to increase sharply compared to previous years during the study period. Typically in the case of BIDV, group 5 debt increased by more than 5,000 billion VND, to 16,525 billion VND, equivalent to an increase of 46% compared to the beginning of the year. In addition, although the bad debt ratio at Vietnamese state-owned commercial banks has been at a low level for many years, that bad debt figure does not fully reflect reality, because many debts are restructured. The debt repayment deadline according to Circular 01/2020/TT-NHNN is essentially bad debt.

In 2020, commercial banks with state capital in Vietnam also made a very large amount of provision for risk reserve funds to cope with the problem of bad debt and this expense was partly used for banks to The company will write off bad debts in the fourth quarter of 2020, aiming to reduce the bad debt ratio for the whole year. Another part is for banks to make provisions for bad debts that may form in the future, when restructuring regulations keep the same debt group to support customers affected by the Covid epidemic according to Circular 01/2020/TT-NHNN expires. Specifically, the debt restructured and the repayment term according to this circular in 2020 is VND 355,000 billion, accounting for about 4% of the total outstanding debt of the economy. Therefore, if only 50% of restructured debt becomes bad debt, the bad debt ratio of the whole system will increase to 4%. The general move of banks is to make early provisions for risks in 2020 as a solution to reduce pressure on potential difficulties and challenges in the future while the epidemic is still prolonged and not yet under control. However, this solution creates another problem: it will be difficult for banks to lower lending interest rates. Invisibly, part of the cost of handling bad debt falls on the borrower.

*** Income from credit activities and income ratio from credit activities of commercial banks with Vietnamese state capital**

Income from credit activities of Vietnamese state-owned commercial banks in the period from 2018 to 2022 is shown in Figure 5 below:

Figure 5: Ratio of income from credit activities of Vietnamese state-owned commercial banks in the period 2018-2022 (%)



Source: Annual reports of Vietnamese state-owned commercial banks (2018-2022)

Risk provisioning is a measure to handle bad debts and control credit quality of Vietnamese state-owned commercial banks, which has had a great impact on the bank's profit results. Banks with good credit quality and low bad debt ratios will not face much pressure in making provisions, causing a big impact on profits. For every bad debt recovered, the bank will record the entire amount of provision as profit.

Banks' profits have tended to increase sharply in recent years, but at the same time, bad debts still occur. Thus, banks still have to spend money on risk provisions. BIDV is the bank with the largest risk provision expense in 2018. Although bad debt decreased compared to the beginning of the year, the bad debt volume at BIDV is still the largest in the system. There are 2 banks out of 4 banks with Vietnamese State capital whose risk provision costs during the period accounted for half of net profit from business activities such as: BIDV, VietinBank.

The nature of risk provisioning costs is to reserve an amount of money for problem loans to improve credit quality. Therefore, the cost of the provision will be taken from the bank's profits and deducted from current income before calculating corporate income tax. An increase in provision costs means that the size of banks' taxable profits will decrease, and less tax will be payable. However, when each dollar of bad debt is processed and recovered, the provision amount will be accounted directly into extraordinary income. Therefore, at many banks,

provision costs will come back and increase taxable profits in the future.

However, shareholders will be interested in whether the bank's profits are high to push up the stock market price. On the other hand, if profits increase, shareholders will receive more dividends. Therefore, making risk provisions for shareholders is a burden. Many bad debts originate from basic investments, outstanding debts from the state budget are difficult to handle, typically debts from 12 loss-making projects of the industry and trade sector. Therefore, the need for banks to set up risk provisions will be a burden not only for the bank but also affect the interests of shareholders.

c. Assessing the credit quality of Vietnamese state-owned commercial banks

*** Limit**

- *Financial resources for bad debt handling process are limited*

To successfully handle bad debt, strong financial resources are needed to speed up the process of handling bad debt. Accordingly, it is necessary to have financial plans to directly and completely buy bad debts from banks, transfer the money to buy bad debts to banks to stabilize business, and strengthen VAMC's bad debt handling activities through restructuring, selling to investors at market price, handling collateral, liquidating collateral...

- *Requirements to increase capital for commercial banks with state capital still face difficulties*

In the context of state budget overspending, the Government's stance is not to use state budget money to restructure commercial banks in general as well as commercial banks with Vietnamese state capital in particular and handle debt. bad debt, while the ability of credit institutions to mobilize social resources for restructuring and handling bad debt is still limited. Therefore, increasing capital for banks, especially commercial banks with Vietnamese state capital, faces many difficulties due to the provisions of the State Budget Law and the Law on Management and Use of State Capital. investing in production and business at enterprises, Decree No. 91/2015/ND-CP does not allow State-owned commercial banks to retain profits, after setting up payable/payable funds to the State; At the same time, Resolution No. 25/2016/QH14 dated November 9, 2016 of the National Assembly on the National 5-year financial plan for the period 2016-2020 also clearly stipulates that the increase in charter capital for State-owned commercial banks is not use state budget.

- State-owned commercial banks are having difficulty handling bad debts. Specifically:

+ Bad debts are mainly handled with risk provisions and special bonds, while measures to thoroughly handle bad debts through handling collateral and debt repayment by borrowers are still at a low level. Therefore, the effectiveness and thoroughness in handling bad debts is limited. Bad debts still exist when the lender and the borrower have not yet terminated and settled the rights and obligations related to the debt. Promoting the handling of bad debts by risk provisions and selling debts to VAMC to receive special bonds as in the past has significantly affected the health and safety of the bank's operations, because of all the risks and Bad debt handling costs are borne by the bank. Risk provision costs and special bond provisions continue to increase in the coming years, which will limit banks' business results and ability to increase charter capital if bad debts are not thoroughly handled. according to market mechanism

+ The bank also faces difficulties in using risk provisions to handle bad debts because according to the process, the bank must apply debt recovery measures from customers first, even considering the customer's conditions. Customers apply support measures (restructuring repayment terms, loan structure...) to improve customers' financial capacity, increase customers' ability to repay debt, and then can Use risk provisions, sell collateral to recover debt to handle bad debts in group 5 or debts of customers who are dissolved, bankrupt, missing, or dead.

+ Customers' debt repayment ability is still limited due to production and business difficulties; Some customers are sluggish, have poor debt repayment awareness, and do not cooperate with banks in handling collateral to repay debt; Customers use capital for improper purposes

+ The seizure of collateral is still facing difficulties due to customers not cooperating in handing over assets; The authorities (People's Committee, police agency, etc.) have not coordinated and actively participated in supporting to solve difficulties for the bank; Communication difficulties during the process of confiscating assets in the spirit of Resolution 42.

* Cause of limitation

- Most commercial banks with Vietnamese state capital often find it difficult to increase capital because they are controlled by the State

- Some senior bank managers are not fully aware and pursue immediate benefits, affecting credit quality.

- The weak management capacity of some banks combined with competitive pressure to develop credit market share leads to the risk of reducing standards in the credit process.

3. Some solutions to improve credit quality of Vietnamese state-owned commercial banks

a. Effectively control asset scale and credit growth rate

First, commercial banks with state capital need to increase the scale and quality of assets, especially profitable assets. Interest-bearing assets are the basis of interest income, which is the most important source of income for commercial banks in Vietnam today. Therefore, commercial banks need to simplify the lending process, improve appraisal capabilities to shorten loan processing time, but must strictly manage loans to ensure loan quality. At the same time, commercial banks with state capital need to focus on priority growth industries, on good quality businesses in industry groups such as post and telecommunications, pharmaceuticals, and medical equipment.

Second, establishing an optimal asset portfolio combined with diversifying the asset portfolio structure helps banks distribute risks and ensure safety. More specifically, it is possible to restructure loan assets into less risky and potential areas such as agriculture, forestry - fishery, and industries serving essential needs, industries and fields associated with technology. information and reduce the proportion of outstanding non-productive debt; Promote foreign exchange trading activities or investment in Government bonds. For commercial banks with state capital, which are medium and small sized banks: restructure customer loan portfolios, reduce loans to state-owned enterprises with low business results and no collateral assets. , increase lending to private enterprises, small and medium enterprises. At the same time, commercial banks must periodically evaluate their customer portfolio to predict long-term risks. Thereby, there are policies to reduce outstanding loans for customer groups, reducing possible future risks for the bank..

b. Limit credit risk

The optimal solution that needs to be done immediately is that commercial banks with Vietnamese State capital need strong solutions to limit credit risks, specifically:

Firstly, strengthen supervision of loans through regulations requiring review of all debts, full objective assessment of customers' ability to repay debt, debt

collection sources to control debts, loans and limit credit risks.

Second, improve the ability to identify and detect credit risks for prevention. Potential credit risks can come from customers or from the bank itself. On the basis of credit risk signs, the departments responsible for risk management according to the scope of their duties provide assessments, comments, and suggestions to the directly responsible department for solutions, timely handling. Consider risk management by unit and centralized management by region. Currently, all banks have a Risk Management Division and each region has a risk monitoring and supervision department, and each business unit has a risk management department. However, it is necessary to closely monitor the operational situation and detect risk factors for the Regional Risk Management Department, and report to the Unit Head.

Third, effectively handle problem debts and limit the emergence of problem debts and bad debts.

For overdue debts, banks need to clarify the customer's business situation. Banks should establish a Working Group to handle bad debt, consider each customer with bad debt, and find ways to solve it through support and financial consulting for businesses with bad debt so that they can have a plan to restore business and operate effectively again, thereby fulfilling debt repayment obligations. In case the customer has the ability to restore production, repay debt and wishes to cooperate, the bank can restructure the debt for the customer. Banks can lend them additional loans in cases where the cause affecting their ability to repay debt and operate is due to lack of capital. Lending ensures capital recovery, helping customers overcome difficulties. Based on the customer's business plan, demonstrate the ability to repay when due after restructuring their debt. This requires banks to closely monitor customers' debts and activities after restructuring. At the same time, the bank has appropriate debt restructuring solutions such as being able to convert part of the principal debt into medium-term bonds; Convert overdue debt and bad debt into shares if it is found that after restructuring, the enterprise has the ability to survive and develop.

c. Limit the rate of marginal interest income

According to the results of the above research model, increasing NIM will increase turnover. Specifically, when the loan interest rate is high, that is, the NIM is high, it can cause the borrower to not be able to fulfill the terms committed in the loan

contract or part of the principal and interest cannot be paid on time, especially in terms of Economic conditions are unstable, business profitability is lower than bank lending interest rates. At the same time, marginal interest income is determined by dividing net interest income by total earning assets. Therefore, when net interest income is high, it proves that the bank lends a lot, leading to high risk, and bad debt is one of the main causes of credit risk and then the bank must make provisions, many risks. The solution for commercial banks with state capital is to offer diverse preferential interest rates applicable to each customer and each customer segment. Commercial banks need to proactively build lending programs with reasonable interest rates, diversify credit products, and develop a balanced consumer loan product package to meet the needs of legitimate life, of customers in order to limit black credit, consider extending debt, adjusting debt repayment terms when customers encounter difficulties due to legitimate reasons and cannot repay debt on time, helping customers not to borrow at high interest rates to pay off debt, bank term.

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