SACOMBANK (STB VN)

A turnaround story for the long haul

BUY

Current price (01-08-19): VND 11,350

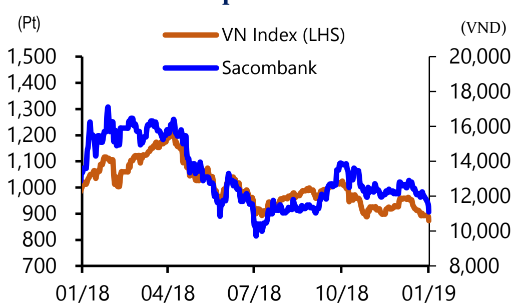
Target price: VND 14,049

Upside: 23.8%

Our view: STB has been a sector laggard due to its substantial legacy NPLs. But a restructuring is under way, and we view the bank as a turnaround play given its solid underlying operations, as reflected in strong expected pre-provisioning operating profit (PPoP) growth. Admittedly, the story is not without risks, and capital pressure is a key investor concern. But the bank's low LDR, broad retail footprint, and solid PPOP growth highlight its strong underlying potential. We think that there is value here, and we initiate coverage on STB with a BUY recommendation.

52-week Price Range (VND)	Market Capitalization	FY19E Dividend Yield	Remaining Foreign Room	Free-float (shares)	Avg. Trading Volume-3 month (shares)
VND 9,670-17,300	**USD 890 mn**	**0.0%**	**11.0%**	**1,695 mn**	**5.9 mn**

Price performance



Event catalysts

- Operational turnaround as legacy bad debt problems are resolved and underlying business continues to improve.
- Management's real estate expertise supports confidence in NPL restructuring.
- LDR is lower than peers and well below the regulatory cap, implying NIM outperformance vs the sector.

Risks to our call

- Potential equity dilution due to legacy NPLs and Basel 2.
- Barriers to bad debt recoveries (e.g., asset selling price and bidding procedures).
- Funding franchise is not very strong for a retail bank, and improving this may be tough.

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Company profile: STB is Vietnam's 6th largest bank by assets with 4.83% market share as at 3Q18. It operates a primarily retail- and SME-focused business. A merger with the former Southern Bank in 2015 resulted in substantial asset quality woes, a challenge that the Bank's management is now addressing with strong support from government policy.

Stock data	
VN Stock Index	887
Market Cap.(USD mn)	890
Outstanding Shares(mn)	1,804
52-week High(VND)	17,300
52-week Low(VND)	9,670
Avg. Trading Volume 1 day(mn)	3.7

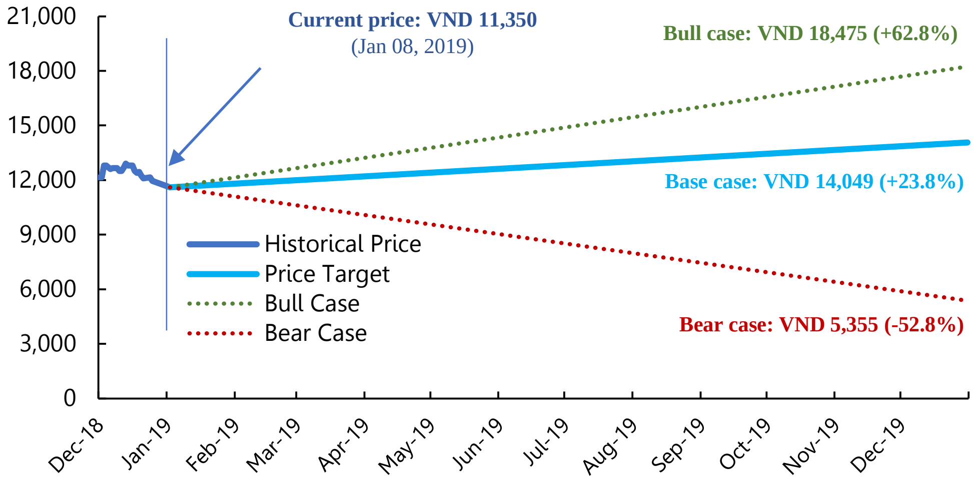
Stock performance (%)		
Absolute performance	1M	-9.5
	6M	10.1
	12M	-21.3
Relative to VNIndex	1M	-2.0
	6M	13.4
	12M	-8.0

Source: Bloomberg

Valuation is cheap (admittedly, for a reason)... STB's stock trades at 1.1x 3Q18A P/TBV, far below the sector average of 2.0x. In our view, the reason for the valuation discount vs peers should be obvious: STB's high level of legacy NPLs, which we peg at VND82.3 trillion or 20.3% of assets. However, we believe the stock could rerate as positive signs of its restructuring emerge. Our 12-month price target of VND14,049 implies 1.2x 2018E P/TBV, which we view as reasonable given the bank's long-term roadmap to improved returns. In short, we believe the stock offers value here.

… but underlying business operations are improving. We forecast PPoP CAGR of 35.1% in 2017-20E, with PPoP / clean-book assets to almost double from 2017A to reach 1.49% in 2020E. In our view, topline growth and PPOP ROA are better indicators of STB's underlying business strength than net profit, which we assume will compressed by the NPL overhang during our forecast horizon. That said, STB could surprise on the upside if the NPL restructuring proceeds more rapidly and effectively than we assume in our model – and management's real estate acumen suggests that it might.

Capital is the key risk. STB's NPL prudential restructuring plan implies gradual loss recognition based on topline profitability in the next several years. We view this workout as entirely appropriate from a prudential perspective. But investors could face equity dilution if a one-off recapitalization were adopted, which necessitates an assessment of the potential risk. A reasonably prudent set of assumptions – 20-30% legacy NPL write-offs and new shares issued at 1.4-1.5x P/TBV – would imply 36-48% dilution if the bank were recapitalized to achieve an 8% CET1 ratio, based on our estimates.



Source: Bloomberg, Yuanta Vietnam Research estimates

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Key Scenario Metrics

Scenarios	Assumptions	
Target Price: VND14,049 (+23.8%)	Our target price based on residual income model. Cost of equity: 12.15% (with 0.2% annual reduction); Final year ROTCE: 11.0%	
Bull case: VND18,475 (62.8%) *Sharp turnaround*	2019E adjusted EPS (*): VND 1,053 2019E Fee income: VND 3,717 bn 2019E Provision costs: VND 1,889 bn	2019E Net interest income: VND 8,023 bn 2019E adjusted CIR (*): 65.6% 2019E P/TBV: 1.46x
Base case: VND14,049 (+23.8%) *Steady turnaround*	2019E adjusted EPS (*): VND 847 2019E Fee income: VND 3,380 bn 2019E Provision costs: VND 1,933 bn	2019E Net interest income: VND 7,821 bn 2019E adjusted CIR (*): 67.6% 2019E P/TBV: 1.13x
Bear case: VND5,355 (-52.8%) *Failed turnaround*	2019E adjusted EPS (*): VND 464 2019E Fee income: VND 2,784 bn 2019E Provision costs: VND 2,061 bn	2019E Net interest income: VND 6,344 bn 2019E adjusted CIR (*): 68.4% 2019E P/TBV: 0.44x

(*) adjusted for bonus and welfare

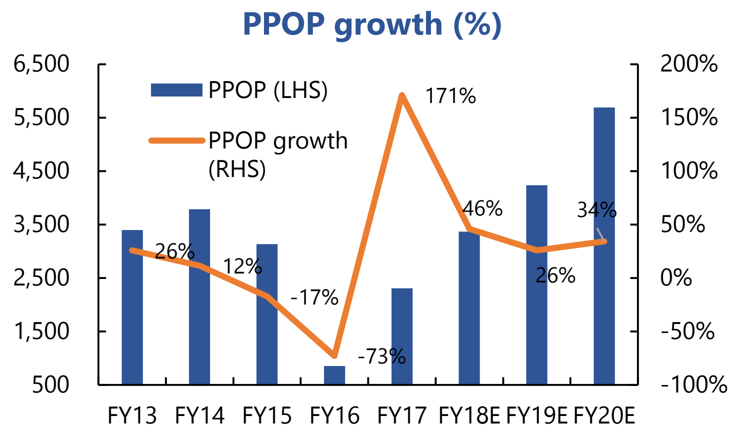
INVESTMENT THESIS

STB's stock valuation reflects its substantial exposure to legacy NPLs

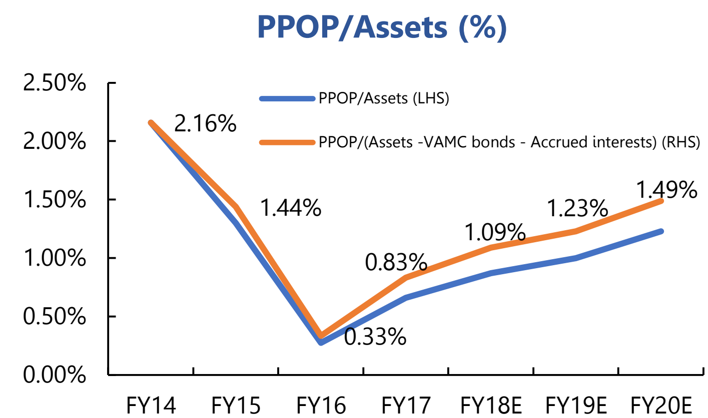
Valuation is cheap (admittedly, for a reason) ... STB trades at a 3Q18A P/TBV ratio of 1.12x, well below the peer average of 1.97x. In our view, the reason for the valuation gap with the rest of the sector should be obvious: STB is in a restructuring phase and will have to recognize substantial provisioning for its high level of NPLs, which are mostly a legacy of the 2015 Southern Bank merger. However, we believe the stock could rerate as positive signs of the restructuring emerge.

But its underlying operations are solid, and we expect PPoP CAGR of 35.1% in 2017A-20E

.. but the underlying business operations are improving. Business efficiency has improved remarkably since 2016, and growth in pre-provisioning operating profit (PPoP) should remain solid. In our view, topline PPoP growth is a better indicator of the strength of the bank's underlying business than net profit, which we assume will continue to be flattened by provisioning for legacy assets. Topline growth should be driven by improving NIMs as the Bank's very low LDR rises toward the regulatory cap, higher consumer banking fee income as the bank better leverages its attractive retail franchise, and improved efficiencies as management shakes off the effects of the 2015 merger with Southern Bank. Despite the legacy NPL issues, we thus see STB's underlying business as very solid and a key attractive feature of the stock. As a result, we forecast PPoP CAGR of 35.1% in 2017-20E, with PPoP / average clean-book assets (i.e., adjusting out the legacy bad debt from total assets) rising from 0.83% to reach 1.49% in 2020E.



Source: Company Data, Yuanta Vietnam Research estimates



Source: Company Data, Yuanta Vietnam Research estimates

Although we expect bottom line ROA to remain constricted by the NPL overhang, management's real estate background suggests that the NPL problem can be worked out.

Admittedly, PPoP does not fully capture the return that investors can expect to receive in the next several years, which (assuming no recapitalization) will be limited by the ongoing NPL overhang. The bank's overall net profitability is still rather low (with ROA of 0.33% and ROE of 5.6% in 3Q18), but even so, we think this will improve as STB continues to resolve NPLs. In 2017, the Bank resolved about VND 19.6 tn (USD 840 mn) of NPLs, and it has said it would handle another VND 15 tn (USD 640 mn) of NPLs in 2018.

Sacombank brought in Chairman Duong Cong Minh to execute the restructuring. Mr. Minh is the former head of Him Lam Corp, a property firm. We think this was the right move given that most of STB's NPL collateral comprises real estate assets. As the former Chairman of LienVietPostBank, he also has a depth of experience in banking. Such a degree of real estate and banking experience for the key decision-maker at STB bolsters our confidence in the bank's ability to resolve its legacy assets and to successfully implement its restructuring. It is still early days, but the VND 19 trillion of NPLs resolved in 2017 suggests that such confidence is deserved, in our view.

Under its restructuring plan, the State Bank of Vietnam has allowed STB to resolve NPLs over 10 years (i.e., from 2017 to 2026). However, STB plans to complete the restructuring ahead of that schedule, in just 3-5 years. Although it is still early days, this indicates STB's strong commitment toward resolving this issue, in our view. But the legacy NPL issue also elicits what we see as the key risk for investors in STB – capital requirements and the possibility of dilution.

Capital is the key risk given the incipient requirements of Basel 2 and the bank's massive legacy asset problems. We have made no assumptions for dilution in our valuation model, instead assuming a steady muddle-through approach in which the bank amortizes part of its legacy bad debt throughout our forecast horizon. However, investors could also be presented with a recapitalization as a means of restructuring the bank.

Equity dilution risk would be limited to 4-7% to bring our estimated CET1 ratio up to 8%, but this is without considering the NPL overhang.

We go into greater detail in the "Investment Risks" section below. But assuming a prudent 8% CET1 ratio (vs an estimated 7% currently), we reckon the bank would have to issue VND1.7 trillion in new shares just to achieve this level as at 2018E, without any other balance sheet considerations. Depending on the issuance price, we reckon this would result in 4-7% equity dilution, which is not really cause for concern (especially given that a few years of earnings retention could reasonably be expected to achieve the same CET1 level).

But perhaps the deeper risk lies in the recoverability of STB's actual level of non-performing assets. Problem assets total VND82.3 trillion as at 4Q18 if we include the VND4.9 tn in recognized category 2-5 NPLs *(net of specific provisions)*, VND37.7 tn in VAMC bonds *(net of provisions)*, VND19.8 tn in accrued interest, and VND19.9 tn net receivables (which mostly comprises NPLs as well). That total figure represents 20.3% of total 2018E assets and 3.3x 2018E shareholders' equity.

The figure below represents the total capital that we reckon would be needed to achieve a CET1 ratio of 8% based on a range of legacy bad debt loss assumptions from 0% to 100%.

Sensitivity analysis of NPL losses to total capital raising (unit: VND bn)

% Total NPLs loss	0%	10.0%	20.0%	30.0%	40.0%	50.0%	60.0%	70.0%	80.0%	90.0%	100.0%
Capital Raising	1,712	9,939	18,165	26,392	34,619	42,846	51,072	59,299	67,526	75,752	83,979

Assuming a 20-30% loss on total NPLs, the bank would require additional capital of VND18-26 tn

Exactly how much of this will have to be written off is difficult to determine. In our view, it would be unreasonable to assume 100% losses on these assets given 1) they have already been partially provisioned against, 2) overall collateral values are likely to be higher now than when the asset was created, and 3) the bank's key decision makers have deep property market experience and thus should be able to handle NPLs efficiently. This should potentially suggest eventual recoveries, but we believe a more reasonable loss assumption should be around 20-30%, implying an additional capital requirement of VND18-26 trillion. However, the eventual losses are clearly uncertain, and we therefore provide the dilution sensitivities for as much as 100% write-offs of the legacy assets (please see the "Risks" section for details).

Estimating the potential dilution risk also requires a discussion of the price of the new capital. At the stock's current price, writing off 30% of legacy bad debt and raising CET1 to 8% would require equity dilution of roughly 55% to current shareholders. We therefore do not see issuing shares at the current valuation as a particularly attractive option. However, a case can be made for raising capital at a higher-than-market price. Typically, such a transaction would also involve changes in the composition of management. Clearly this is all speculative, but STB offers an attractive foundation for retail banking growth, which could be attractive for a strategic investor.

Again, we go into greater detail in the "Risks" section, but the table below indicates the estimated dilution to current shareholders of a recapitalization to 8% CET1 based on legacy asset loss assumptions of zero to 100% (the Y column) and the valuation at which the new capital is issued (the X column), based on whether or not a strategic shareholder premium is part of the price. A reasonable combination of assumptions (i.e., 20-30% losses on legacy assets and new capital issuance valuation of 1.4-1.5x P/TBV) which would imply c. 36-48% dilution. Caveat emptor, but we think the stock's current valuation has more than priced in such an outcome.

Sensitivity analysis of share ownership dilution risk (unit: %)

	Price of newly issued shares	12,000	14,000	16,000	18,000	20,000	22,000	24,000	26,000
	P/TBV of newly issued shares	1.02x	1.18x	1.35x	1.52x	1.69x	1.86x	2.03x	2.20x
Loss on Legacy Bad Debts	0%	7%	6%	6%	5%	5%	4%	4%	4%
	10%	31%	28%	26%	23%	22%	20%	19%	17%
	20%	46%	42%	39%	36%	33%	31%	30%	28%
	30%	55%	51%	48%	45%	42%	40%	38%	36%
	40%	62%	58%	55%	52%	49%	47%	44%	42%
	50%	66%	63%	60%	57%	54%	52%	50%	48%
	60%	70%	67%	64%	61%	59%	56%	54%	52%
	70%	73%	70%	67%	65%	62%	60%	58%	56%
	80%	76%	73%	70%	68%	65%	63%	61%	59%
	90%	78%	75%	72%	70%	68%	66%	64%	62%
	100%	80%	77%	74%	72%	70%	68%	66%	64%

Source: Yuanta Vietnam Research estimates

PATH TO DOUBLE-DIGIT ROTCE

1) Despite the many obstacles to NPL resolution, we believe that STB will be successful with its restructuring, with ROTCE to climb once provisioning normalizes. In our view, Vietnam's banks are on track to resolving their bad loan issues given:

- **A favorable macroeconomic environment** (i.e., solid GDP growth and a strong property market),
- **VAMC provides a mechanism to recover** bad loans.

- **Resolution 42/2017/QH14 allows banks to more actively manage NPLs** via rapid repossession of collateral.

Admittedly the legal mechanism is not perfect, but these policies clearly indicate the Government's strong commitment to resolving Vietnam's estimated USD 20 bn of NPLs, equivalent to about 10% of total GDP. Clearly NPLs are not specific to any particular bank, but rather a national issue that needs to be resolved to ensure macroeconomic stability. Total loans in the banking system account for more than 120% of Vietnam's real GDP, a level that is 2 to 3 times that of comparable ASEAN countries. Thus, a high rate of NPLs are a major concern, not just for the banking system but for overall national financial security.

Thus, we believe that the Government will work to help banks clear bad debts efficiently. One such policy could be the establishment of a market to sell bad debt, preferably with the participation of domestic and foreign investors.

Sensitivities: What if VAMC bonds were interest earning assets?

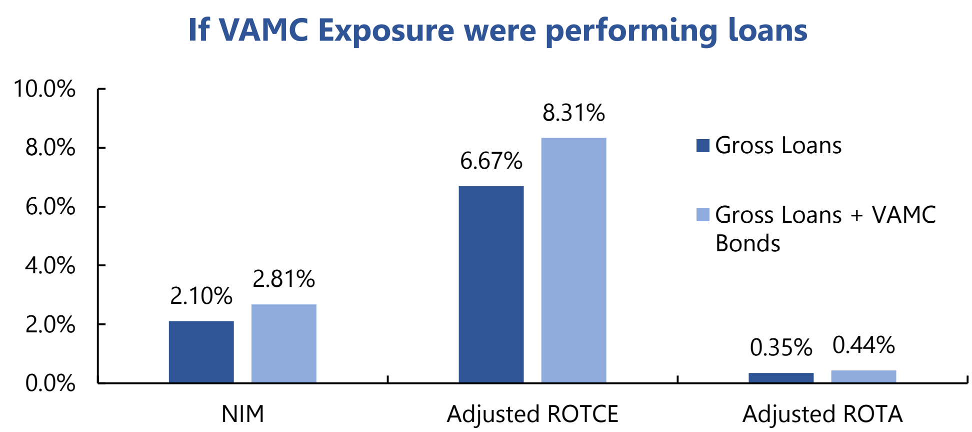
We make the following assumptions for 2018E:

Gross Loans	*Net VAMC Bonds*	*Average loans yield*	*LDR Regulatory Cap*
VND 255.4 tn	*VND 37.7 tn*	*9.1%*	*80%*

STB transferred VND 40.2 tn (USD 1.7 bn) in gross NPLs to the VAMC in exchange for on-balance sheet special bonds that represent about 10% of the bank's total assets as of **4Q18**. The bank must provision for the VAMC bonds over ten years, but any recovery value from the transferred NPLs should be returned to the bank. This suggests potential writebacks in the years ahead, although we prefer to see this as a call option rather than a sure thing.

VAMC exposure earns no interest. If these funds were instead allocated to loans, NIM and ROA would be far higher. Again, this reflects the potential for improved profitability once the NPL overhang is removed.

If we assume that the VND 37.7 tn NPLs (net of provisioning) that STB sold to VAMC were recouped in 2018 and the resulting free funds were shifted into gross loans (with no change in total assets, deposits, or other balance sheet items) with a maximum LDR of 80%, total 2018E gross loans would be VND 288.3 tn, which is 13% higher than our assumption. Assuming that the new loans were issued at the loan book's average yield (9.1%), NIM would increase from 2.10% to 2.81%, adjusted ROTA from 0.35% to 0.44%, and adjusted ROTCE from 6.67% to 8.31%.



Source: Yuanta Vietnam Research estimates

Our point is not that this is likely to occur, but rather that bad debt is clearly the biggest headwind to STB's profitability and stock price. Thus, investors should closely observe the progress of its restructuring.

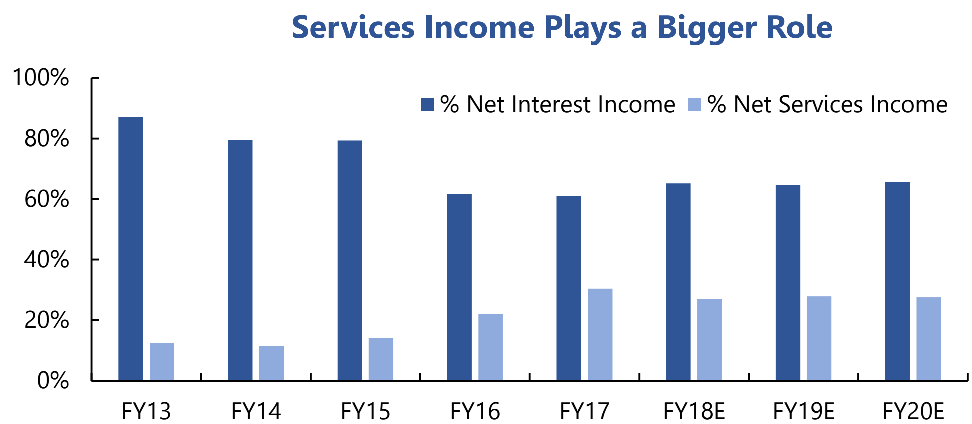
Our view is that the NPLs will be successfully worked out for the aforementioned reasons – macroeconomic and policy trends are positive. Thus, we view STB stock's as a play on an operational turnaround.

Net fee income account for 27.5% of total revenues on average in the 2018-20E

2) Fee income to reduce earnings volatility

Aside from NPL resolution, boosting fee income is another goal of the Bank to improve its ROTCE over the long term. We expect net fee revenues to account for 27.5% of total revenues on average in the 2018-20E period, up from 22.1% in 2015-17A. Despite its well-publicized problems, STB has a very strong branch network and large retail customer base (see page 11 of the 2017 annual report for details). We therefore believe that the Bank's outlook is strong for consumer banking fees, including segment such as:

- **Card transaction fees** and other card-related fees. STB ranks third highest in Vietnam in terms of Visa transactions.
- **Other retail-focused fee-based services** such as internet and mobile banking, and
- **Bancassurance**, where STB has tied up with Dai-Ichi Life.



Source: Company Data, Yuanta Vietnam Research estimates

LDR (69.7% in 3Q18) is well below other listed banks on average in the same period (88.4%), implying NIM outperformance going forward.

3) STB has more room than its peers to expand loan growth by boosting LDR

- **LDR was 69.7% as of 3Q18, well below the regulatory cap of 80%**. By contrast, most other banks have already reached or exceeded the regulatory limit of 80% for non-state commercial banks and 90% for state commercial banks. Current average LDR of listed banks is 88.4% and that of listed non-state banks is 87.5%, suggesting limited room to push LDRs higher among competitor banks. We see this as a key attractive feature for STB, given that it has room to increase its LDR, and thus also improve its NIM, going forward.
- **Higher LDR = Higher profitability.** The tables below present our sensitivity analysis of the Bank's LDR to its NIM, ROE, and ROA. (In this exercise, LDR increases from our initial assumptions to the regulatory cap of 80%, whereas other numbers remained unchanged.)

	FY18E	FY19E	FY20E
Current LDR assumptions	70.0%	74.0%	77.0%
NIM	2.10%	2.18%	2.42%
Adjusted ROTCE	6.67%	7.05%	8.93%
Adjusted ROTA	0.35%	0.36%	0.46%

	FY18E	FY19E	FY20E
Regulatory cap LDR	80.0%	80.0%	80.0%
NIM	2.47%	2.74%	2.74%
Adjusted ROTCE	7.52%	9.02%	9.98%
Adjusted ROTA	0.40%	0.48%	0.53%

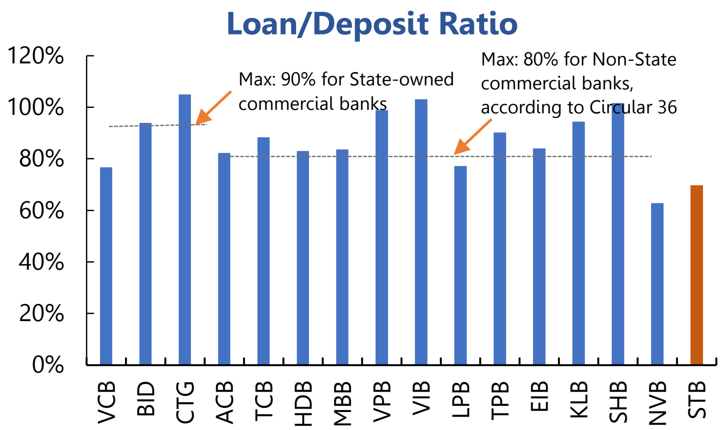
Source: Yuanta Vietnam Research estimates

Not surprisingly, NIM, ROE, and ROA improve significantly when LDR increases from our base case assumptions of 70% in FY18E, 74% in FY19E, and 77% in FY20E to 80% for all three years. The higher LDR also boosts the implied fair value by about 4.0% to VND 14,612 (+28.7% vs. the current level) compared to our base fair value of VND 14,049 (+23.8% vs. the current stock price).

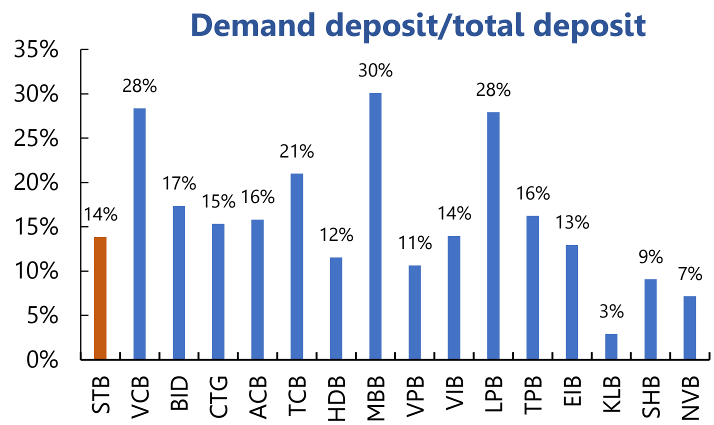
- An increased LDR is not just an academic exercise. **Banks that are undergoing restructuring such as STB are likely to be allowed higher loan growth rates** from the

SBV than other banks, in our view. Again, this could be an advantage for STB to increase its NIMs that is not enjoyed by all of its peers.

- **Rising interest rates would be a mixed bag** for STB. Demand deposits account for about 14% of total deposits, which is close to average among its peers. We believe that a 50 bps increase in rates would result in 5% higher net interest income in 2019E.
- **Risk: deposit costs might also increase** substantially along with demand for capital in 2019, given that the cap on short-term capital used for medium-to-long term loans will decrease from 45% in 2018 to 40%.



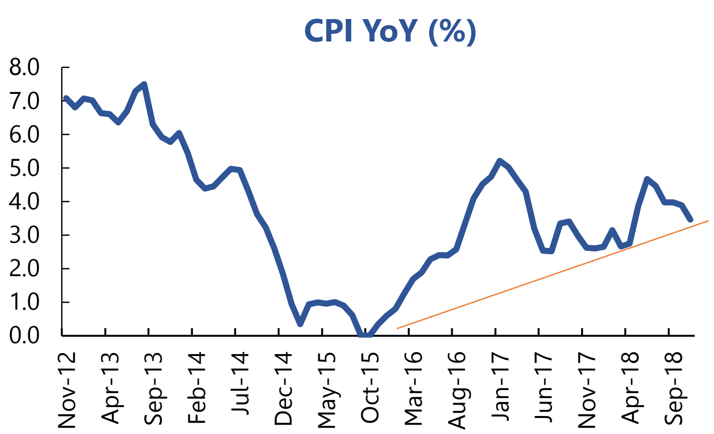
Source: Bloomberg



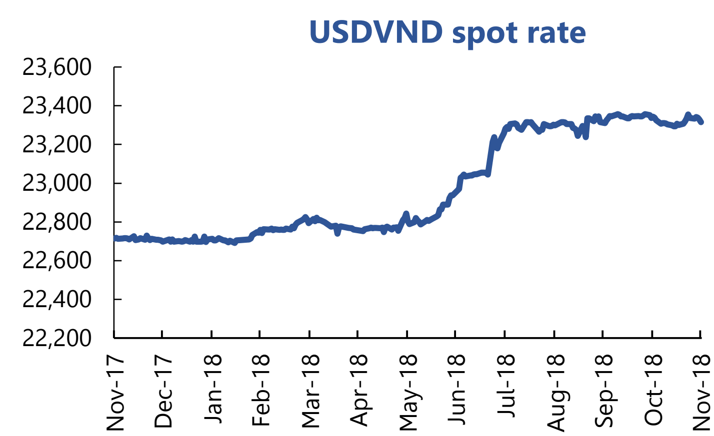
Source: Bloomberg

Interest rates to increase in 2019? As illustrated by the charts below, inflation has been on the rise and the USDVND spot rate has increased nearly 3% in 2018. Interbank Offered Rates in 1H18 were relatively low and persistently decreasing. However, liquidity tightened in the second half, which has boosted interbank rates sharply.

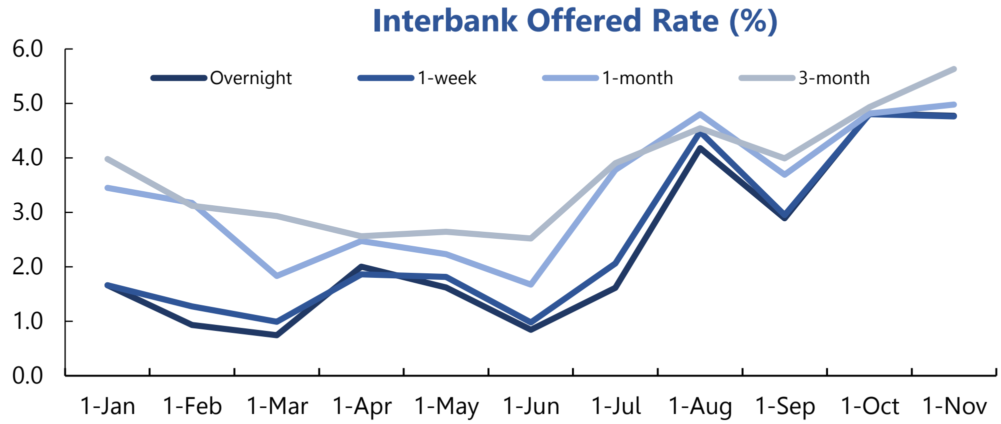
Inflation could increase going forward due to several push factors, such as the new environmental tax rate on fuel (increasing from VND 3,000 per liter to VND 4,000 per liter from 01/01/2019), higher medical services fees, commodity price shocks, and Dong devaluation. Thus, rates might be raised to keep inflation in check.



Source: Bloomberg



Source: Bloomberg

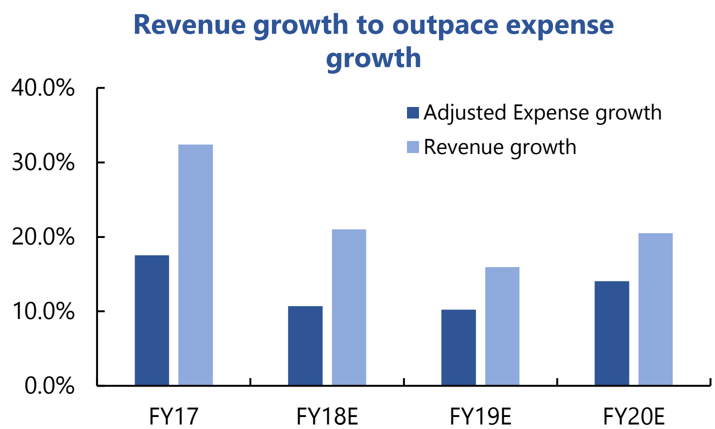


Source: State Bank of Vietnam (SBV)

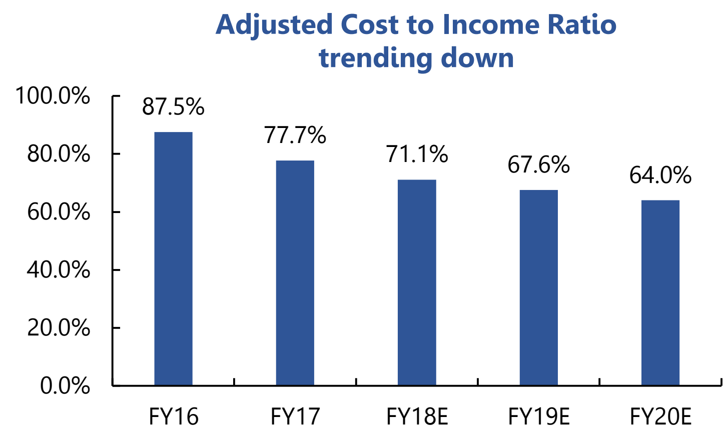
4) Operating expense improvement

We expect CIR to decline to 71.1% in 2018E and 67.6% in 2019E

- We expect expenses to increase as the Bank improves its IT infrastructure and operations to adapt Basel II, increase its fee-based revenues. However, we expect a positive JAWS ratio as revenue growth outpaces expense growth – driving positive operating leverage. We expect the efficiency ratio to continue to improve from the nadir of 87.5% in 2016 and 77.7% in 2017 (which we attribute to the Southern Bank merger) to 71.1% in 2018E and 67.6% in 2019E.
- STB is not a cost-cutting story. Nevertheless, we believe management will successfully keep expenses in check while growing revenue.



Source: Company, Yuanta Vietnam Research estimates



Source: Company, Yuanta Vietnam Research estimates

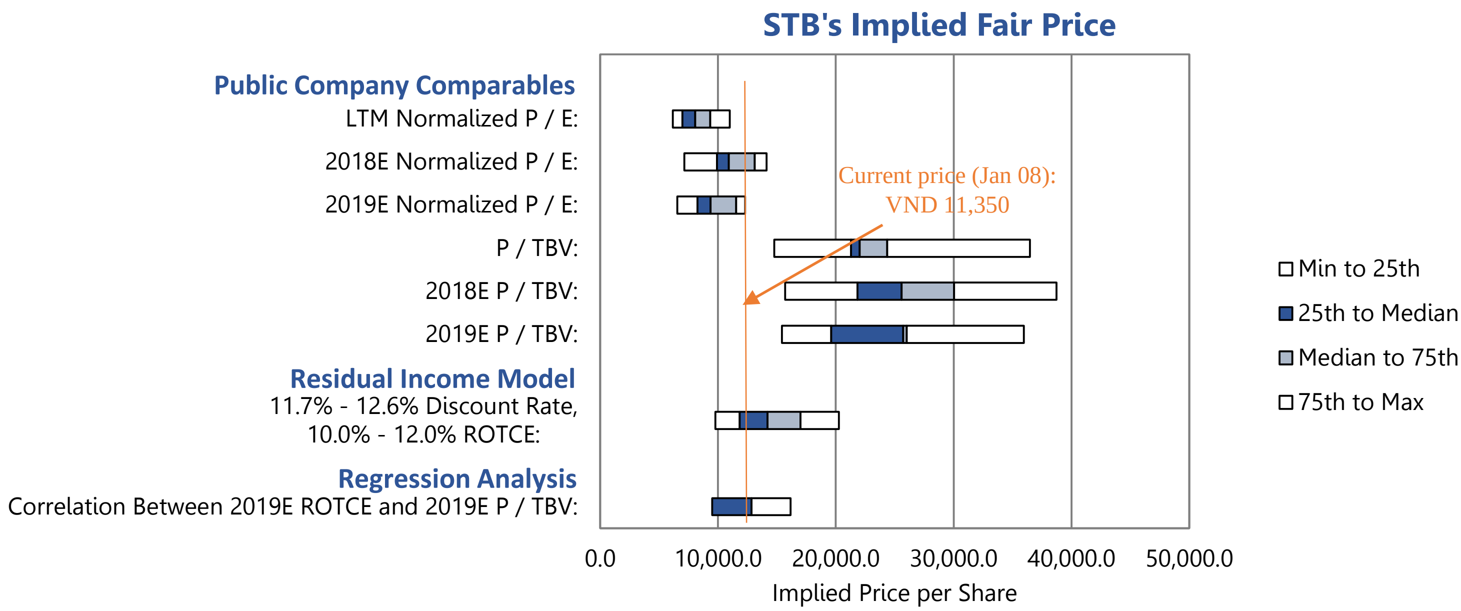
VALUATION

Target price: VND14,049 (23.8%), implying P/TBV of 1.2x for 2018E and 1.13x for 2019E

We apply three valuation methodologies to formulate our target price for STB. Our preferred method for STB is the residual income (excess return) model, which generates our target price of VND 14,049, implying P/TBV multiples of 1.20x for 2018E and 1.13x for 2019E and PERs of 18.72x for 2018E and 16.58x for 2019E. The dividend discount model (DDM) valuation is problematic given that STB has not paid a dividend for the past few years given its capital requirements and ongoing restructuring. We have penciled in a small (5%) payout ratio on 2019E earnings attributable to shareholders in line with management guidance, but we remain skeptical about the bank's actual ability to meet even this modest expectation. A DDM approach is thus problematic, and also tends to undervalue the stock, in our view. We also use public comparable banks in Vietnam, and look at the implied P/TBV multiples generated from a regression analysis.

STB's fair value estimate using our "Base Case" assumptions.

As shown below, STB's share price is lower than the implied fair value range generated from the residual income approach, listed comparables method, and regression analysis. STB has a relatively low P/TBV multiple, which might suggest undervaluation. However, the Bank is in a restructuring process and its reported equity value masks the underlying asset quality problems.



Source: Yuanta Vietnam Research estimates

Residual Income (Excess Return) Model

We believe that the Residual Income Model is a more suitable approach than the Dividend Discount Model given that the Bank currently pays no dividend.

We split the model into 3 phases, with Phase 1 corresponding to high dividend issuance growth in the first five years, Phase 2 corresponding to slowing dividend growth in the five years after that, and Phase 3 corresponding to a stabilized payout ratio in the fives after phase 2.

Residual Income = ROCE * Average Equity – Cost of Equity * Average Equity.

We make the following assumptions:

- **Cost of equity** starts at 12.15% and falls to 10.15% in the final year to reflect reduced risk (and reduced potential returns) as STB grows.
- **ROTCE** in the second stage (Years 6-12) starts at 14% and then falls gradually to reach 11% in the third stage (Years 13-15).
- **Assets growth** in the second stage (Years 6-12) starts at 10% and declines gradually to reach 7% in the third stage (Years 13-15).
- **Dividend payout ratio** increases from 5.0% on FY19E earnings to 20% in FY22E. It then rises to 50% in FY27E, and remains stable thereafter.

Implied Value of Equity:	
Terminal Net Income Growth Rate:	6.0%
Projected Net Income 1 Year After Period:	7,190.9
Residual Income Terminal Value:	13,428.7
(+) Current Common Shareholders' Equity:	23,780.9
(+) PV of Residual Income Terminal Value:	3,644.0
(+) Sum of PV of Residual Income:	(2,084.8)
Implied Equity Value:	**25,340.2**
% of Implied Value from PV of TV:	*14.4%*
Implied Share Price:	**14,049**
Current Share Price:	11,350
Premium / (Discount) to Current:	**23.8%**

Sensitivity Table

Terminal Return on Common Equity:	Initial Cost of Equity (Declines by 0.20% Annually in Phases 2 and 3):										
	11.00%	11.15%	11.40%	11.65%	11.90%	**12.15%**	12.40%	12.65%	12.90%	13.15%	13.40%
13.0%	30,342	28,480	25,745	23,388	21,337	**19,549**	17,954	16,531	15,256	14,106	13,064
12.5%	28,141	26,418	23,887	21,705	19,804	**18,148**	16,667	15,347	14,163	13,094	12,125
12.0%	25,969	24,384	22,053	20,043	18,292	**16,764**	15,398	14,178	13,083	12,095	11,197
11.5%	23,824	22,375	20,244	18,404	16,799	**15,398**	14,144	13,024	12,018	11,108	10,282
11.0%	**21,708**	**20,393**	**18,457**	**16,785**	**15,325**	**14,050**	**12,907**	**11,885**	**10,966**	**10,134**	**9,378**
10.5%	19,620	18,437	16,695	15,188	13,871	**12,719**	11,686	10,761	9,928	9,173	8,486
10.0%	17,559	16,507	14,955	13,611	12,435	**11,405**	10,480	9,651	8,903	8,224	7,605
9.5%	15,526	14,602	13,239	12,056	11,019	**10,110**	9,291	8,556	7,892	7,288	6,736
9.0%	13,520	12,723	11,545	10,521	9,622	**8,831**	8,118	7,476	6,894	6,364	5,878

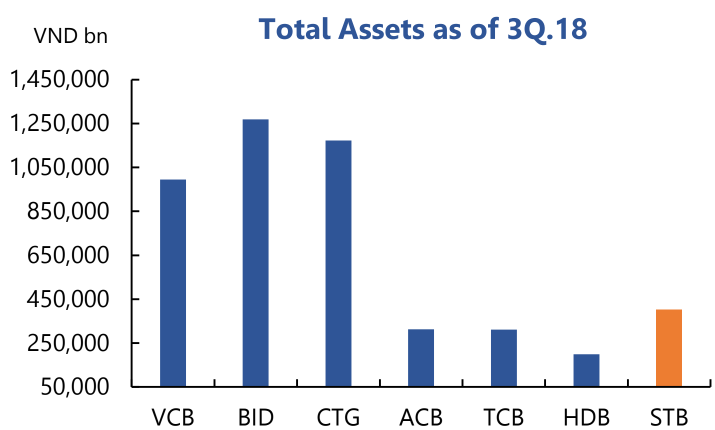
Listed Bank Comparables

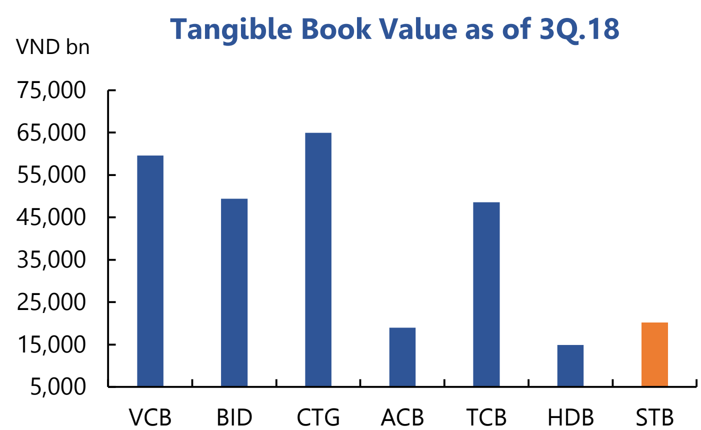
We apply the following criteria to determine comparable banks.

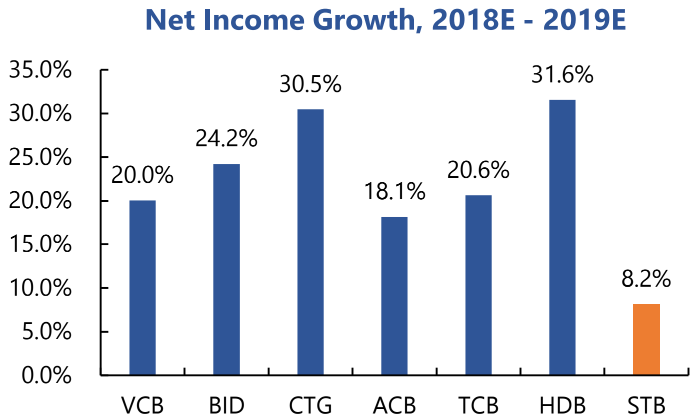
- **Industry**: Banks in Vietnam
- **Financials**: Total Assets from VND 210 tn to 1,150 tn (USD 9 bn to 50 bn)

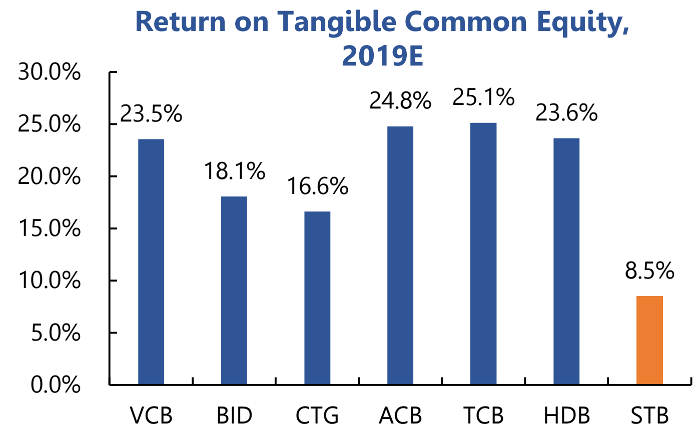
A comparison with peers indicates that STB's 3Q.18A P/TBV multiple is 1.12x, which is well below that of the sector (1.97x), but its unadjusted ROTCE is likewise far below the median. STB's unadjusted ROTCE in 3Q17-18A was 6.74%, and we forecast this to rise to 8.4% in 2018E and 8.5% in 2019E. Despite the expected improvement, the Bank's profitability is still far below the sector median unadjusted ROTCE of 18.2% in the past four quarters, and Bloomberg consensus of 20.6% in 2018E and 23.6% in 2019E.

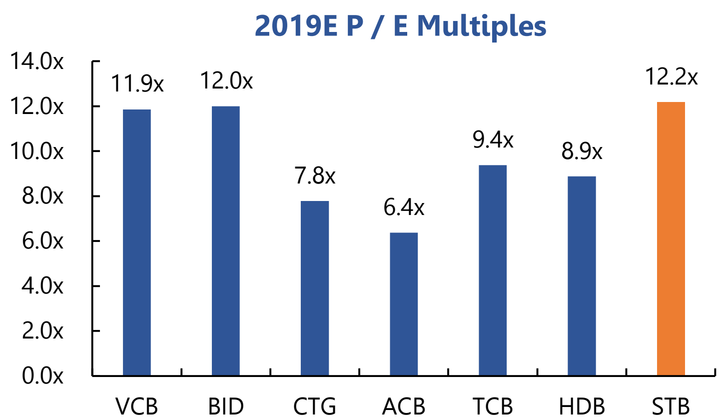
Comparable Public Banks – Key Financial Metrics

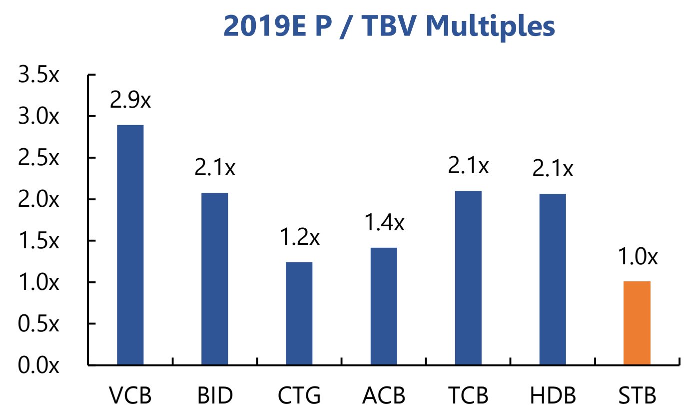












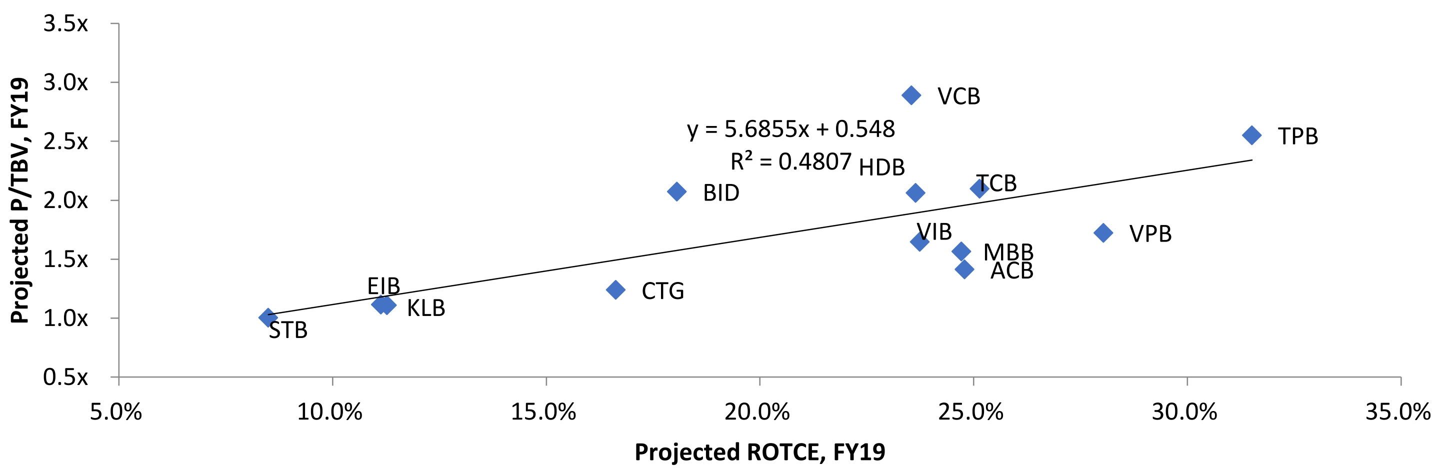
Source: Yuanta Vietnam Research estimates, Bloomberg, Fiinpro

Regression Analysis

We also ran a regression analysis to determine the relationship between FY19E ROTCE and P/TBV for a broad set of public commercial banks in Vietnam. We then use this relationship to estimate the implied FY19E P/TBV multiple and implied Equity value.

Here is the result of the regression:

The Regression analysis gives an implied share price of about VND 12,816.



Source: Yuanta Vietnam Research estimates, Bloomberg

Base case: +23.8%

Bull case: + 62.8%

Bear case: -52.8%

Valuation Conclusions

As noted above, we see the Residual Income Model as most appropriate for estimating STB's fair value. On this basis, the stock is currently undervalued by about 23.8% under our Base case, and about 62.8% in the Bullish case (final year ROE of 11.5%). In the Bearish case (final year ROE of 9%), the stock price is overvalued by about 52.8%.

We view our Base case as reasonably conservative, which is appropriate given uncertainties over STB's restructuring. We also view the Bullish case as more likely to occur than the Bear case, given the favorable macro environment and Government support for the restructuring.

In our view, banks are seeing a turning point after years of concerted clean-up efforts – and investors have been waiting for this turning point for years. We see this as an attractive opportunity to benefit from an undervalued turnaround story, and we thus initiate with an Overweight.

We believe every valuation has a story behind it. A solid company's story might be rosy – but often its market valuation more than reflects this. Sacombank's story is admittedly not rosy, but management understands the problems and is taking actions to fix them. Thus, we believe that STB is a good, albeit speculative, investment. Investors should approach the idea with open eyes and should be cognizant of the risks.

INVESTMENT RISKS

Biggest risks are the legacy bad debt handling progress & capital pressures

Risk 1) The biggest risk for the Company and stock price is the progress of its legacy NPL resolution. Delays in handling NPLs that have been transferred to the VAMC could continue to impact earnings and the share price performance. Whereas Resolution 42/2017/QH14 should help banks to resolve their bad debts, certain real-world frictions remain and need to be addressed. This includes issues related to the mechanism for asset sales, the bidding process, and – of course – the selling price. Analysts and investors should closely monitor the progress of NPL resolution to gauge the potential for STB's stock price. Also, as noted above, STB's asset quality woes are a legacy of the Southern Bank merger. We are positive on the bank's ongoing operations and do not anticipate a substantial increase in new NPL formation; but if this were to occur, it would obviously be a negative for sentiment and the share price.

Capital and liquidity pressures. STB could face pressure related to its capital levels as it must ensure that it complies with the Basel II requirements by 2019. An average loan growth is about 14-15% per annual, short-term funding used for medium-to-long term loans will reduce from 45% in 2018 to 40% in 2019, and risk weighted assets for real estate loans will increase from 200% in 2018 to 250% in 2019. Thus, with this capital pressure and NPLs, STB is not likely to pay dividend on 2018E earnings (and it may not do so on 2019E earnings either).

Below is the sensitivity analysis of newly issued shares with the following assumptions:

- 2018E's tangible common equity tier 1 (CET1): VND 21.3 tn
- CET1 ratio: We assume that STB will maintain CET1 ratio at 8%
- Total amount of legacy bad debts is about **VND 82.3 tn** as at 4Q.18 (including net internal NPLs (category 2-5) VND 4.9 tn, net VAMC bonds VND 37.7 tn, accrued interests VND 19.8 tn, and net receivable that are NPAs VND 19.9 tn)
- Newly issued shares range from 699 mn to 2,199 mn shares, *corresponding with assumptions of 20% to 30% loss on legacy bad debts and VND 12,000 (P/TBV: 1.02x) to VND 26,000 (P/TBV: 2.20x) on prices of newly issued shares.*

Sensitivity analysis of newly issued shares (unit: million shares)

Loss on Legacy Bad	Price of newly issued shares	12,000	14,000	16,000	18,000	20,000	22,000	24,000	26,000
	P/TBV of newly issued shares	1.02x	1.18x	1.35x	1.52x	1.69x	1.86x	2.03x	2.20x
	0%	143	122	107	95	86	78	71	66
	10%	828	710	621	552	497	452	414	382
	20%	1,514	1,298	1,135	1,009	908	826	757	699
	30%	2,199	1,885	1,650	1,466	1,320	1,200	1,100	1,015
	40%	2,885	2,473	2,164	1,923	1,731	1,574	1,442	1,331
	50%	3,570	3,060	2,678	2,380	2,142	1,948	1,785	1,648
	60%	4,256	3,648	3,192	2,837	2,554	2,321	2,128	1,964
	70%	4,942	4,236	3,706	3,294	2,965	2,695	2,471	2,281
	80%	5,627	4,823	4,220	3,751	3,376	3,069	2,814	2,597
	90%	6,313	5,411	4,735	4,208	3,788	3,443	3,156	2,914
	100%	6,998	5,999	5,249	4,666	4,199	3,817	3,499	3,230

Source: Yuanta Vietnam Research estimates

Below is the total capital that needs to be raised corresponding to different assumptions on legacy bad debts loss - ranging from 0% to 100%, to maintain CET1 ratio at 8%.

Sensitivity analysis of total capital raising (unit: VND bn)

% Total NPLs loss	0%	10.0%	20.0%	30.0%	40.0%	50.0%	60.0%	70.0%	80.0%	90.0%	100.0%
Capital Raising	1,712	9,939	18,165	26,392	34,619	42,846	51,072	59,299	67,526	75,752	83,979

We expect the percentage loss on legacy bad debts in the base case is 20% to 30% and 100% in the worst case. We believe that 20-30% loss on the base case is more likely to happen than the worst case because most NPLs have collaterals. Correspondingly, the total capital that might need to be raised ranges from VND18 tn to VND26 tn.

Below is the sensitivity analysis of share ownership dilution risk (%):

- Current share outstanding: 1,804 mn
- Share ownership dilution risk ranges from 28% to 55%, *corresponding with assumptions of 20% to 30% loss on legacy bad debts and VND 12,000 to VND 26,000 on prices of newly issued shares.*

Sensitivity analysis of share ownership dilution risk (unit: %)

Loss on Legacy Bad Debts	Price of newly issued shares	12,000	14,000	16,000	18,000	20,000	22,000	24,000	26,000
	P/TBV of newly issued shares	1.02x	1.18x	1.35x	1.52x	1.69x	1.86x	2.03x	2.20x
	0%	7%	6%	6%	5%	5%	4%	4%	4%
	10%	31%	28%	26%	23%	22%	20%	19%	17%
	20%	46%	42%	39%	36%	33%	31%	30%	28%
	30%	55%	51%	48%	45%	42%	40%	38%	36%
	40%	62%	58%	55%	52%	49%	47%	44%	42%
	50%	66%	63%	60%	57%	54%	52%	50%	48%
	60%	70%	67%	64%	61%	59%	56%	54%	52%
	70%	73%	70%	67%	65%	62%	60%	58%	56%
	80%	76%	73%	70%	68%	65%	63%	61%	59%
	90%	78%	75%	72%	70%	68%	66%	64%	62%
	100%	80%	77%	74%	72%	70%	68%	66%	64%

Source: Yuanta Vietnam Research estimates

Below are the newly estimated fair prices corresponding with newly issued shares:

- Original estimated fair value: VND 14,049
- Estimated equity value: VND 25.3 tn
- New fair prices range from VND 6,330 to VND 10,127, *with the assumptions of 20% to 30% loss on legacy bad debts and VND 12,000 to VND 26,000 on prices of newly issued shares.*

Sensitivity analysis of newly estimated fair prices (unit: VND)

	Price of newly issued shares	12,000	14,000	16,000	18,000	20,000	22,000	24,000	26,000
	P/TBV of newly issued shares	1.02x	1.18x	1.35x	1.52x	1.69x	1.86x	2.03x	2.20x
Loss on Legacy Bad Debts	0%	13,020	13,157	13,263	13,346	13,413	13,468	13,515	13,555
	10%	9,628	10,081	10,450	10,756	11,015	11,235	11,426	11,592
	20%	7,638	8,171	8,622	9,009	9,344	9,637	9,896	10,127
	30%	6,330	6,869	7,338	7,750	8,113	8,437	8,728	8,990
	40%	5,405	5,926	6,387	6,799	7,169	7,503	7,806	8,083
	50%	4,715	5,210	5,654	6,057	6,422	6,755	7,061	7,342
	60%	4,182	4,648	5,072	5,460	5,816	6,143	6,445	6,725
	70%	3,757	4,196	4,599	4,971	5,314	5,632	5,928	6,204
	80%	3,410	3,824	4,207	4,562	4,892	5,200	5,488	5,758
	90%	3,122	3,512	3,876	4,215	4,532	4,830	5,109	5,372
	100%	2,879	3,248	3,593	3,917	4,222	4,508	4,779	5,034

Source: Yuanta Vietnam Research estimates

Risk 2) Barriers to bad debt recoveries.

Despite supportive government policies such as Resolution No. 42 to help banks accelerate the resolution of legacy NPLs, numerous barriers to implementation still stand in the way. These include issues related to the asset sale mechanism, the bidding process, and – of course – the selling price. Moreover, most of STB's real estate collateral assets are very large in value. Finding investors to purchase these assets might be difficult, and the bank might have to accept installment payments over many years. Such arrangements also pose credit and counterparty risks.

However, we remain confident about STB's ability to overcome these hurdles given favorable government policy and support, as well as management's strong real estate acumen.

Risk 3) Funding franchise is not strong for a retail bank, and improving this may be tough. Demand deposits represent 14.5% of total deposits, which is just slightly below the 15% median of listed banks. This is relatively weak for a retail- and business-banking focused bank like STB. Increasing this may be difficult given the strong competition and probable higher interest rate environment (which could further bolster the attractiveness of time deposits). However, we see increasing the CASA ratio as a potential upside driver for STB, especially if it is able to leverage its payments and overall SME business.

Risk 4) 4Q18 earnings could be hit by lumpy provisioning. Under its restructuring plan STB has committed to amortize its VAMC exposure over ten years. Moreover, management has stated its intention to handle the problem within 3-5 years. We expect the need to provision more heavily in 4Q18E, which would be a repeat of 2017 (4Q17 represented 72% of full-year provisioning in 2017) unless there is a substantial recovery of NPLs in the year.

BUSINESS OPERATIONS

Key focus: Progress of NPL workout

3Q.18 Results: Sacombank [STB] reported mixed Q318A results. Net interest income of VND 2,070 bn grew 22.1% YoY growth, while pre-provisioning operating profit (PPOP) of VND 982 bn was up 66.7% YoY. However, profit before tax was hit by lumpy provisioning in the 3Q.18 to reach only VND 318 bn, down 29.3% YoY. STB appears to have accelerated provisioning for NPLs as its PPOP increased – which is in line with its mandate to provision legacy assets based on its profitability.

STB is guiding for PBT VND2,2tn in PBT in 2018E. This suggests low provisioning in 4Q18, which implies recoveries on legacy assets.

FY18 Guidance: STB has guided 2018 PBT to increase by 47% YoY to reach VND 2,200 bn, which is higher than its initial target of 23% YoY growth. The Bank would have to book low provisions in 4Q18 to record such high PBT, in our view. This would imply substantial recoveries on legacy assets, in our view.

The bank targets loan growth of about 14% YoY (vs. its initial target of 13%), deposit growth of about 12% YoY (below its initial target of 18% YoY), and total operating income of about +21% YoY.

We forecast net interest income of VND 6,787 bn (+28.6% YoY), fee income of VND 2,822 bn (+7.6% YoY). Net interest margin (NIM) of 2.10% (vs 1.84% in 2017), and operating costs of VND 7,069 bn (+11.6% YoY).

According to the restructuring plan approved by the SBV, STB has flexibility in provisioning VAMC bonds and accrued interests based on its financial ability during the period 2015-2025. However, we expect STB to continue increasing provisions for loans losses and VAMC bonds to about VND 1,238 bn (+51.6% YoY) given the increased PPOP.

We forecast reported net income at VND 1,704 bn (+44.3% YoY). However, we also assume a 20% management bonus of VND 59.1 bn and another VND 292 bn in bonus & welfare fund payments in 2018. These "below the line" items are really operating costs, in our view. Thus, we forecast net income attributable to common shareholders of VND 1,354 bn (+69.6% YoY) in 2018, equivalent to adjusted EPS of VND 751.

In addition, STB has about 81.56 million treasury shares with total value at VND 750.9 bn, which is equivalent to an initial investment cost at VND 9,200/share. At the current share price at VND 11,950, STB could recognize about VND 196 bn in additional share premium if this occurs, which would also improve its regulatory capital ratios.

Ongoing NPL workout is a key trend to watch. In 2017, STB resolved VND 19,665 bn (USD 840 mn) of NPLs (including VND 15,365 bn under the restructuring plan). Specifically, the Bank liquidated VND 2,786 bn of collateral, selling VND 2,608 bn of debt at market price and collecting VND 14,271 bn of bad debts sold to VAMC and other receivables. Provisioning and the allocation of accrued interest in 2017 exceeded 35.1% of the restructuring plan's objectives for that year.

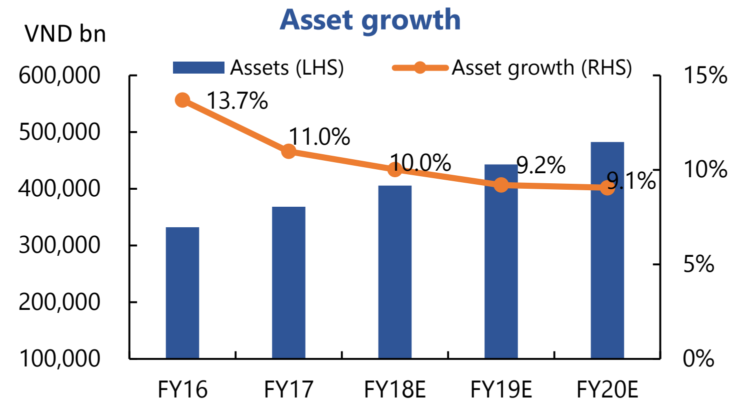
STB sold three industrial parks in Long An province to Him Lam in 2017 at VND 9,200 bn. However, under the terms of the deal, STB received only VND 920 bn as a deposit and another VND 8,280 bn will be paid over the next 7 years as an installment payment, with annual interest of 7.5% to be paid on the principal. We view such an outcome positively overall, although such an installment payment methodology also poses a risk for STB (i.e., in terms of its ability to collect).

STB has indicated that it will take drastic measures to shorten the bad debt workout process with the goal of recovering VND 15 tn (USD 640 mn) of bad debt in 2018E. However, the road ahead is a long one, and we think that STB's ability to pay a dividend is highly at risk until the restructuring progress is complete, which *ceteris paribus* is likely to last at least another three years.

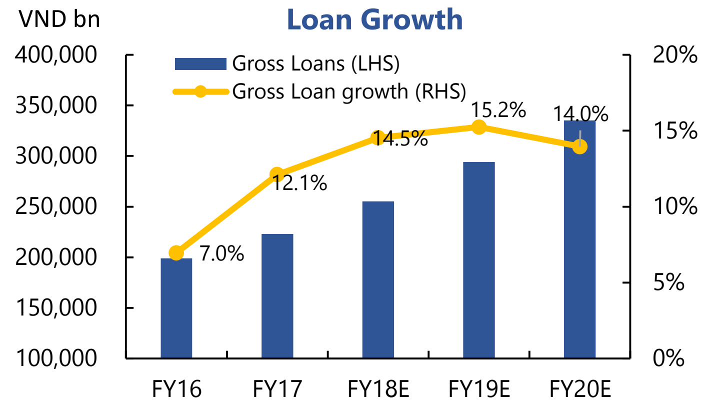
Loan growth

Loan growth: 14.6% on average in the 2018-20E

Following the painful Southern Bank merger, loan growth decelerated in 2016 (7% YoY vs. industry average of 18.7% YoY) and 2017 (12.1% YoY vs. 18.2% YoY) as the Bank has focused on resolving bad debts that resulted from the merger. However, the growth rate has improved to reach 13.6% YTD in 3Q18A, higher than the 11.0% YTD average growth rate of STB's listed peers, according to FiinPro. Sacombank's credit growth target from the SBV is about 14% in 2018E. Given STB's low LDR and government policy allowing higher-than-average loan growth for banks that have acquired weak peers, we expect the loan growth to average 14.6% in 2018-20E.



Source: Company Data, Yuanta Vietnam Research estimates



Source: Company Data, Yuanta Vietnam Research estimates

Deposit growth: 10.4% on average in the 2018-20E

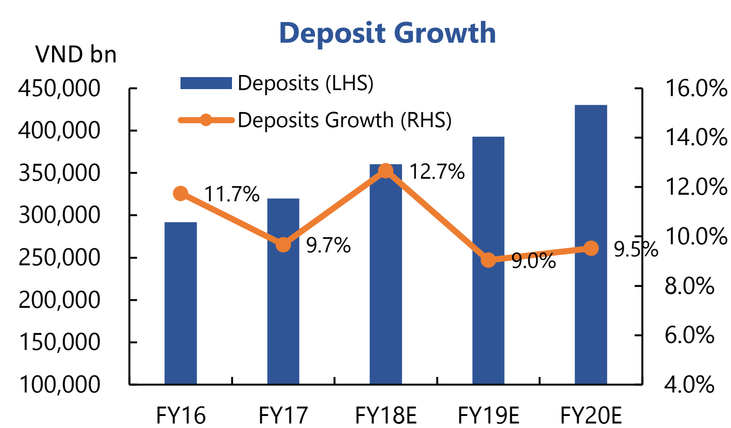
Deposit growth

In line with asset growth, STB's deposit growth increased slightly from 2016A (11.7% YoY) to 3Q18A (14.3% YoY). We estimate deposit growth to average 10.4% YoY in 2018-20E. Time deposits account for 85.5% of the bank's total deposits as of 3Q.18; while, demand deposits represent 14.5%, which is just slightly below the median of listed banks (15%). Total demand deposits of STB (VND 51.9 tn) ranked 5th place among listed banks in terms of absolute value, just behind VCB (VND 216.7 tn), BID (VND 157.6 tn), CTG (VND 113.7 tn), and MBB (VND 76.4 tn).

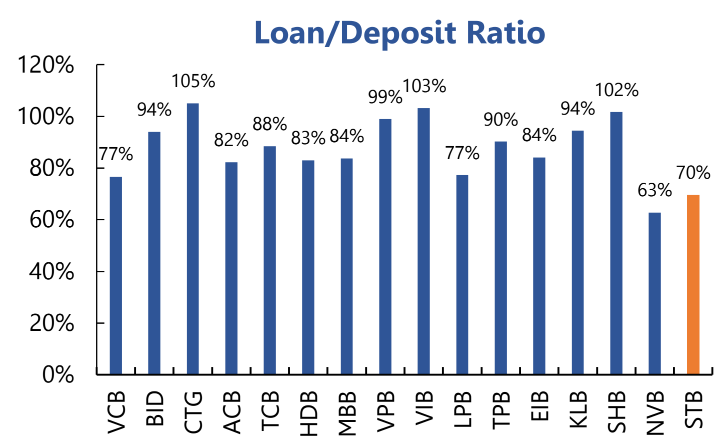
We expect LDR to approach regulatory limit of 80%

Loan/deposit ratio (LDR) is below the average of its peers

Loan to deposit ratio has been flat at around 70% since 2016, which is lower than that listed bank average of 88.4%. In large part, this is a reflection of the large balance sheet items that are not earning interest (i.e., the VAMC exposure and interest receivables, which represent non-performing assets). In other words, the Bank is earning less than it would if its asset quality were normalized. Additionally, STB has been in a restructuring period which has also impacted the acceleration of loan growth. However, in the longer term, it also means that STB has a longer runway to increase LDR and boost NIM compared to other banks, the LDRs of which have typically already reached or exceeded the regulatory limit (80% for non-state commercial banks and 90% for state-owned commercial banks).



Source: Company Data, Yuanta Vietnam Research estimates



Source: Bloomberg

Net interest margin (NIM) has improved

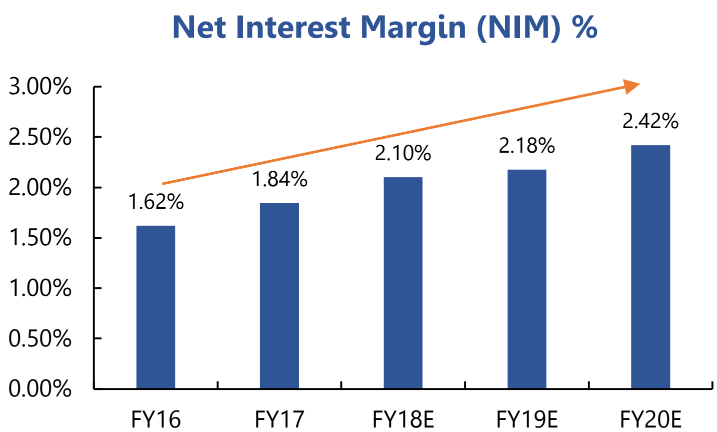
NIM is approximately 1.82%, lower than the NIMs of listed peers which average 3.18% as of 3Q.18. However, STB's NIM has improved meaningfully from 1.44% in 2016 to nearly 1.82% as of 3Q18, and we expect it to reach 2.23% on average in 2018-20E as LDR ramps up and more of the bank's capital is appropriated to interest-earning assets.

Fee income to play a more significant role

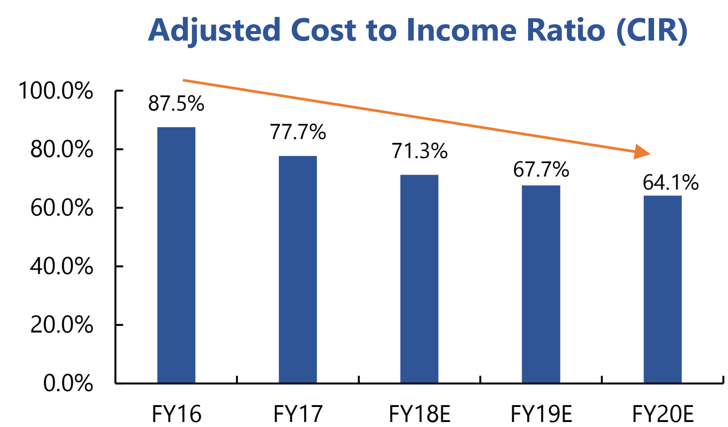
Net non-interest income has increasingly become a revenue growth driver for the Bank. Non-interest income accounted for 38.9% of total revenues in 2017A, with client services revenue alone accounting for about 30.3% of total revenues. We expect net non-interest income and especially fee income to continue increasing its contribution to the total net revenue, growing by 19.5% CAGR in 2018-20E and accounting for 27.5% of total revenues on average in the same period. This should help the Bank to smooth earnings amidst the potential interest rate volatility; moreover, it is a key ROE driver given the limited additional capital commitment to this type of business.

Cost to Income ratio (CIR): High, but falling

STB's cost to income ratio (CIR) is relatively high at 67.5% vs the peer average of 42% as of 3Q18A. However, we attribute this performance largely to the effects of Southern Bank merger. STB's CIR averaged 53% in 2010-14, prior to the merger. Moreover, the bank's efficiency has improved substantially since 2016, with adjusted CIR falling from 87.5% (2016) to 77.7% (2017). We expect this to decline to 67.6% on average in 2018-20E.



Source: Company Data, Yuanta Vietnam Research estimates



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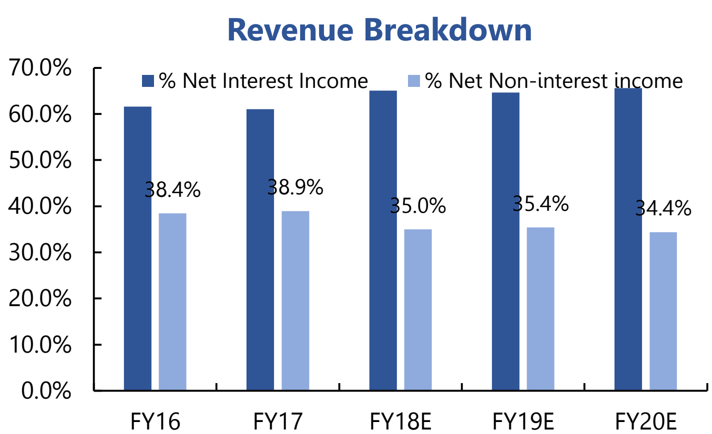

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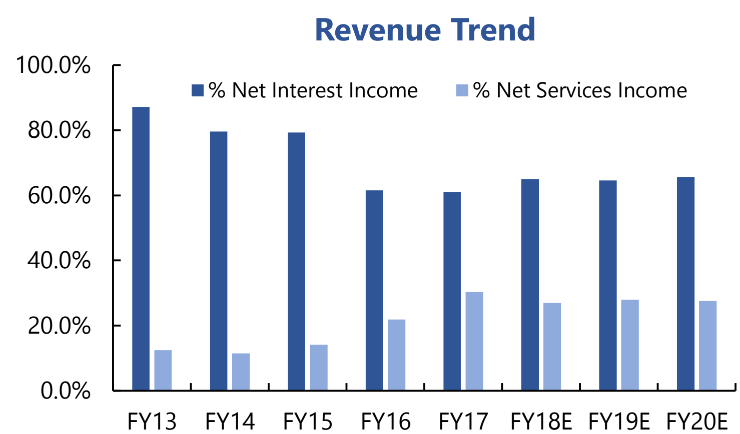


Source: Company Data, Yuanta Vietnam Research estimates

Credit quality: Weak, but improving

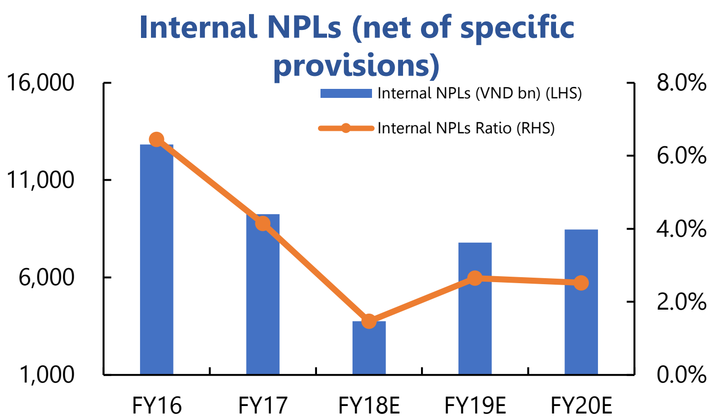
The restructuring is under way, but admittedly there is still a long road ahead. Non-performing loans (NPLs) (net of category 3-5) ratio declined considerably from 2016 (6.5%) to only 1.5% as of 4Q18. However, this does not include bad debts that sold to the VAMC, which were a net VND 37.7 tn (USD 1.6 bn) as of 4Q18A. Including the VAMC assets would raise the NPL ratio to 12.9% as of 4Q18A (extremely high, obviously, but down from 15.8% in 2016A and 16.3% in 2017A). In addition, if including accrued interests of about VND19.8 tn and net receivables that are NPAs VND19.9 tn, the total NPL ratio could increase to 24.1% as of 4Q18A, decreasing from 25.7% in 2016A. For this exercise, we consider the legacy bad debt to be loans (NPLs) both for the numerator and the denominator, resulting in NPL percentages that are slightly below the numbers we have seen reported in the media. Presumably the media are only adding the NPLs to the numerator. Under the restructuring plan, the State Bank of Vietnam allows STB to resolve its NPLs over 10 years; however, STB aims to handle in 3 to 5 years.

STB's asset/equity ratio has increased from 14.9x in 2016A to 16.9x in 3Q18A, which is quite high. This is partly due to high accounts receivable, especially accrued interest, which mostly consists of bad debt. Accrued interest/asset ratio of Sacombank stands at 5.94%, which is far higher than the average of its peers (1.29%); however, this line too has improved since 2016 (7.63%).

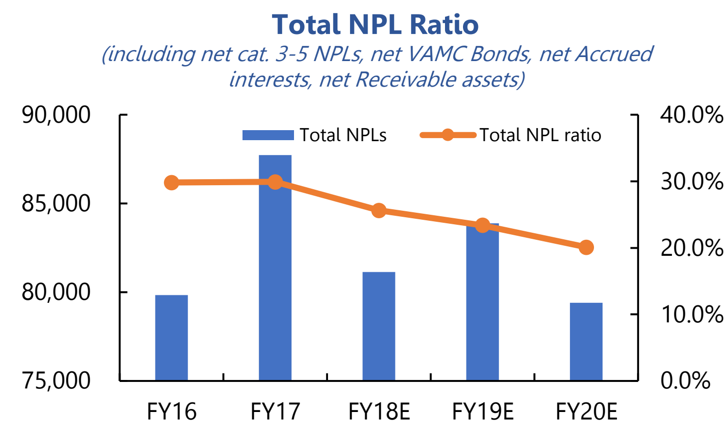
Category 2-5 NPLs have fallen substantially from VND 16.34 tn (USD 701 mn) in 2016A to VND 6.6 tn (USD 280 mn) in 4Q18A, a decrease of 59.5% in that timeframe.

Real estate properties that STB is offering for bid

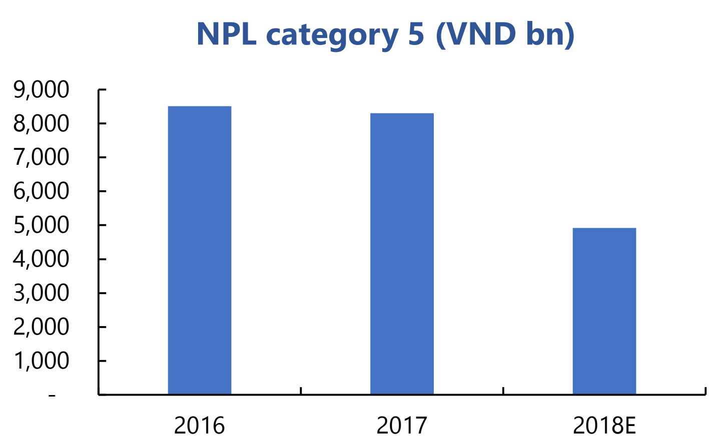
Properties	Location	Area (m2)	Bidding value (VND bn)
Phong Phu Industrial Zone	Binh Chanh, HCMC	1,340,000	7,600
Binh Tri Dong Residential Area	Binh Tan, HCMC	534,124	6,698
Residential Area	Long Binh, District 9, HCMC	164,950	1,815
Residential Area	Binh Thuy, Can Tho Province	602,225	4,565
61-63A Nam Ky Khoi Nghia	District 1, HCMC	800	811
Manufacturing land	Tan Phu District, HCMC	6,327	413
36/70 D2 street	Binh Thanh District, HCMC	6,382	447



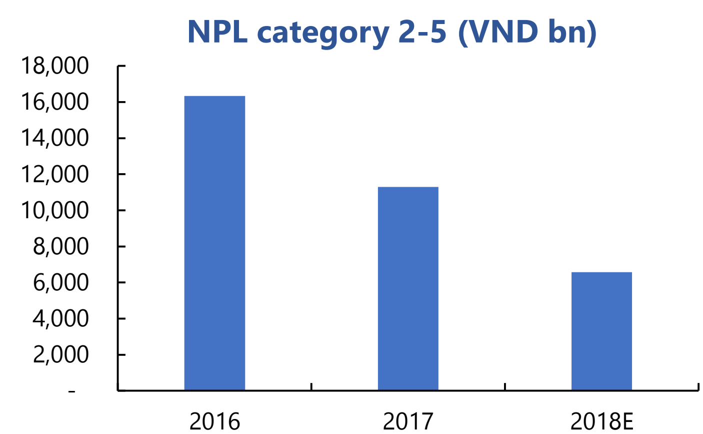
Source: Company Data, Yuanta Vietnam Research estimates



Source: Company Data, Yuanta Vietnam Research estimates



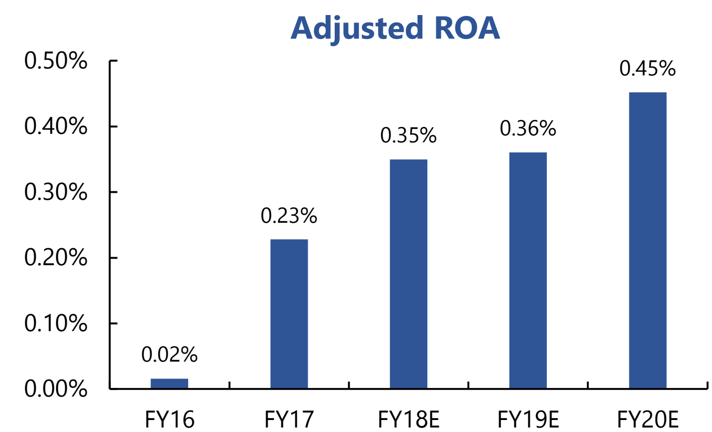
Source: Company Data, Yuanta Vietnam Research estimates



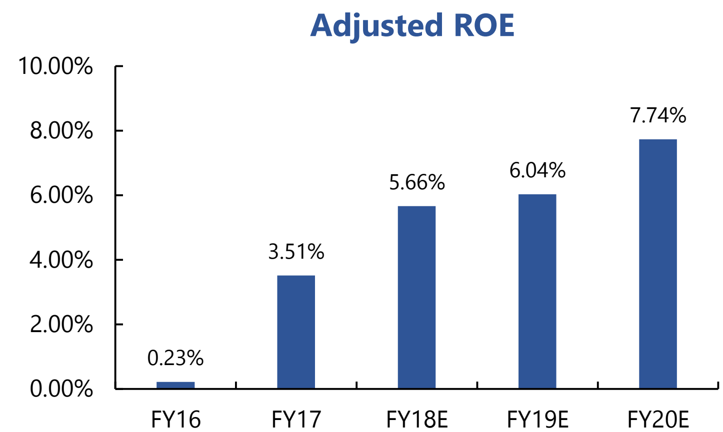
Source: Company Data, Yuanta Vietnam Research estimates

Overall, profitability is constrained, but on the rebound

As the Company focuses on restructuring and putting down significant amount of provisions for bad loans, reported return on assets and return on equity are relatively low, 0.34% and 5.65% respectively as of 3Q.18. These are much lower than that of its peers, which are approximately 1.35% and 17.69% respectively *(data from FiinPro)*. However, things have improved remarkably since 2016, **adjusted** ROA and ROE has jumped from 0.02% and 0.23% in 2016A to 0.23% and 3.51% in 2017A, respectively. We estimate average adjusted ROA and ROE to reach 0.39% and 6.48% in 2018-20E.



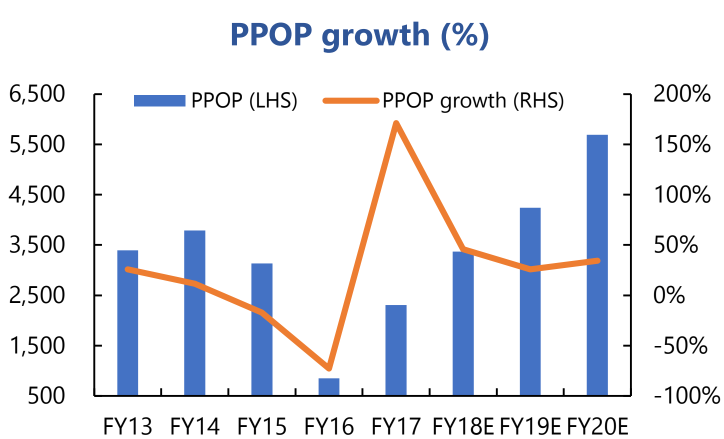
Source: Company Data, Yuanta Vietnam Research estimates



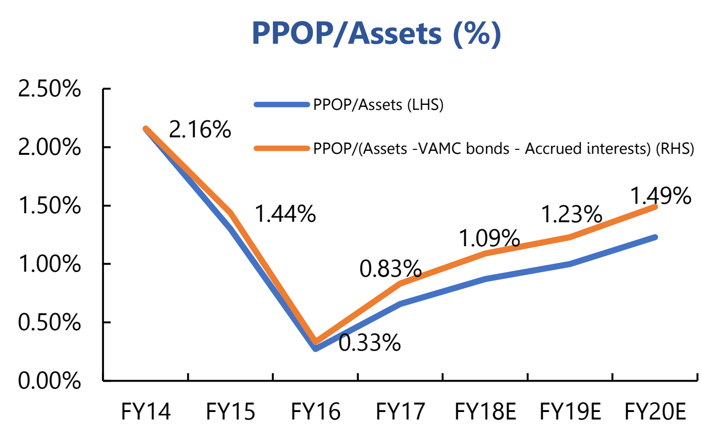
Source: Company Data, Yuanta Vietnam Research estimates

Underlying business is still solid

Given that net income growth will be limited by the need for provisioning against legacy assets, we view the trends in pre-provisioning operating profit (PPOP) as a superior indicator of the profitability of the underlying business. PPOP posted significant growth in 2017 (+171% YoY) after a sharp decline in the past two years due to the merger with Southern Bank. We expect the strong growth to continue, with PPOP to expand 46% in 2018E and 30% on average in 2019-20E. PPOP/assets recovered steadily from 0.27% in 2016 to 0.66% in 2017. Excluding the legacy VAMC bonds and other NPLs, PPOP/adjusted assets would increase from 0.33% in 2016 to 0.83% in 2017. We expect the latter number to increase to 1.09% in 2018E, 1.23% in 2019E and 1.49% in 2020E.



Source: Company Data, Yuanta Vietnam Research estimates

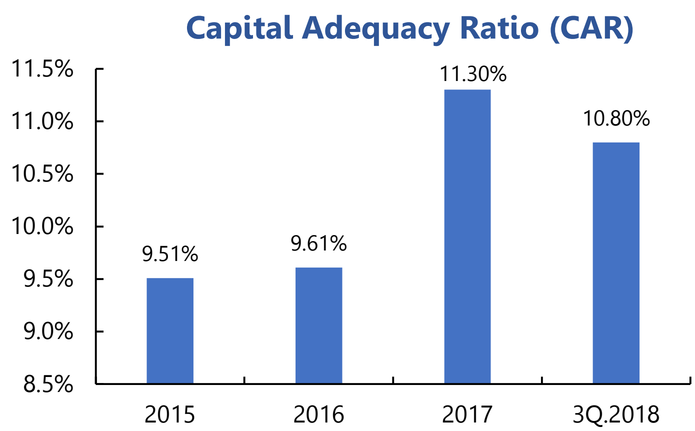


Source: Company Data, Yuanta Vietnam Research estimates

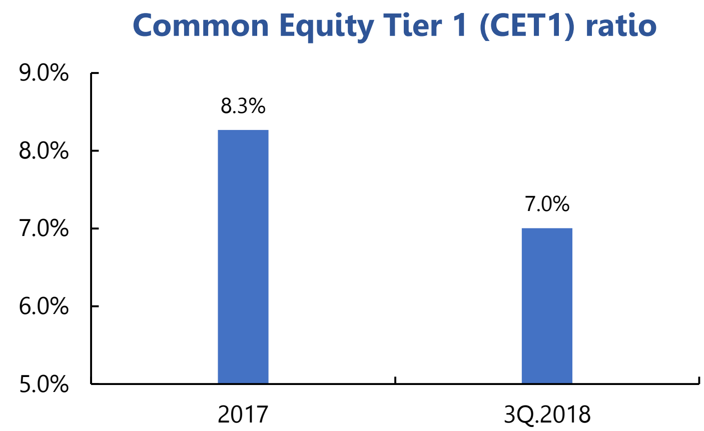
Reported CAR appears adequate for B-2, but capital remains a concern

STB's CAR of 11.3% as at 2017A and 10.8% as at 3Q18A was above the Basel II minimum of 8%. We estimate the bank's Common Equity Tier 1 (CET1) ratio was at 8.3% in 2017A and 7.0% in 3Q18A, which is also higher than the minimum requirement under Basel III (i.e., 4.5% by 2019). However, the bank's assets to equity ratio has increased from 14.9x in 2016A to 16.9x in 3Q18A, which is quite high. This is partly due to its high level of accounts receivable, especially accrued interest (i.e., mostly bad debt).

Thus, we believe that capital requirements could be a risk for investors, especially under a strict CAR calculation of Basel II to be adopted by 2019. Thus, the Bank might need to decrease its leverage by increasing its capital (preferably Common Equity Tier 1 capital, in our view) to ensure adequate safety. In any case, given the low CAR level and the bank's ongoing restructuring, we do not expect the Bank to pay a dividend on 2018E earnings and the issue may impair its ability to pay a dividend in subsequent years as well (although we have penciled in a modest 5% payout on 2019E earnings).



Source: Company Data, Bloomberg



Source: Company Data, Yuanta Vietnam Research estimates

COMPANY BACKGROUND

SaiGon Thuong Tin Commercial Joint Stock Bank (STB) is a private commercial bank that specialized in SME lending. In 2015, the Bank merged with Southern Bank, becoming the top 5 largest commercial banks in terms of total assets, shareholder equity, and networks. 2017 was the first year that Sacombank proceed with the Restructuring Program approved by the State Bank after merging with Southern Bank. The Bank's development strategy will continue to base on retail business, focusing strongly on "quality" instead of "quantity". The main goals in the next few years concentrate on handling bad debts (or Non-performing loans- NPLs), raising capital and improving business operations to adapt Basel II accords.

Sacombank was founded in 1991, which was one of the first commercial bank that was established in Ho Chi Minh City (HCMC). It operates a primarily retail banking business with a wide branch network across Vietnam and also has branches in Laos and Cambodia. A merger with the former Southern Bank in 2015 resulted in substantial asset quality woes, a challenge that management is now addressing with strong support from government policy.

Loans are the heart of the Bank. Sacombank's business model, just like many other banks in Vietnam, is a prototypical bank. Loans are the heart of the Bank. As of 3Q.18, 61.8% of Sacombank's assets are loans, followed by securities investments at 19.5% (this includes VND 40.2 tn or about 10% of assets in zero-interest VAMC bonds). Deposits are the main component of the Bank's liabilities, with deposit/liabilities ratio is 94%.

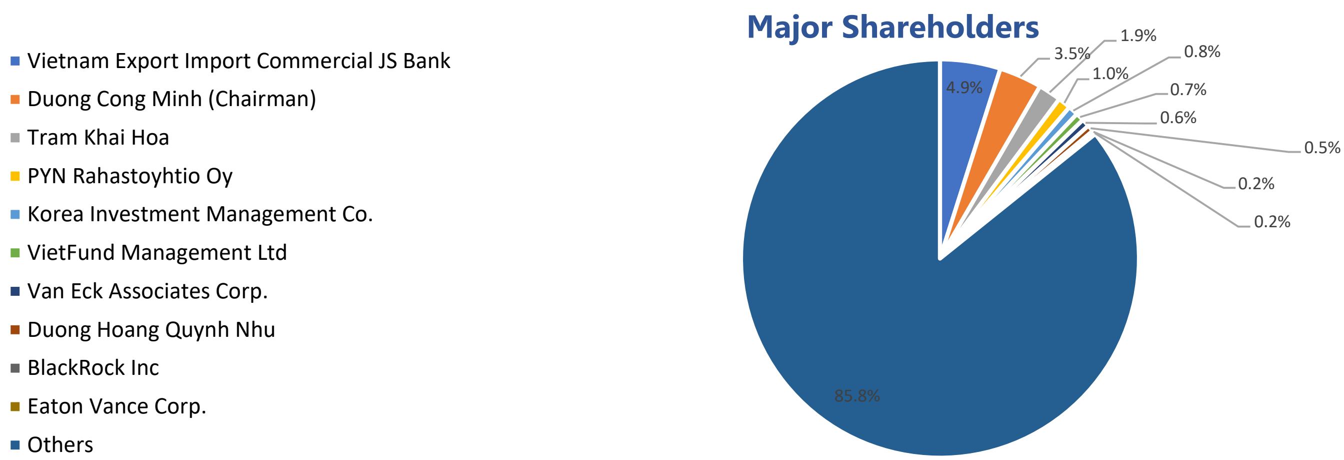
Sacombank went public in 2006, and the stock price is currently traded at VND 11,950 per share. Its market cap is about VND 21.5 tn (USD 920 mn). Its TTM P/TBV multiple is about 1.12x against medians of 1.97x for our set of comparable banks (Vietcombank (VCB), BIDV Bank (BID), Vietinbank (CTG), Asia Commercial Bank (ACB), Techcombank (TCB), and HDBank (HDB)). These multiples are based on our estimates and consensus data from Bloomberg for the companies and do not reflect adjustments for excess or deficit capital.

Sacombank was in the top 3 with highest card transaction volume presented by Visa, a leading bank in deploying touchtech payment, and top 3 with highest volume of card transactions in Vietnam in 2017.

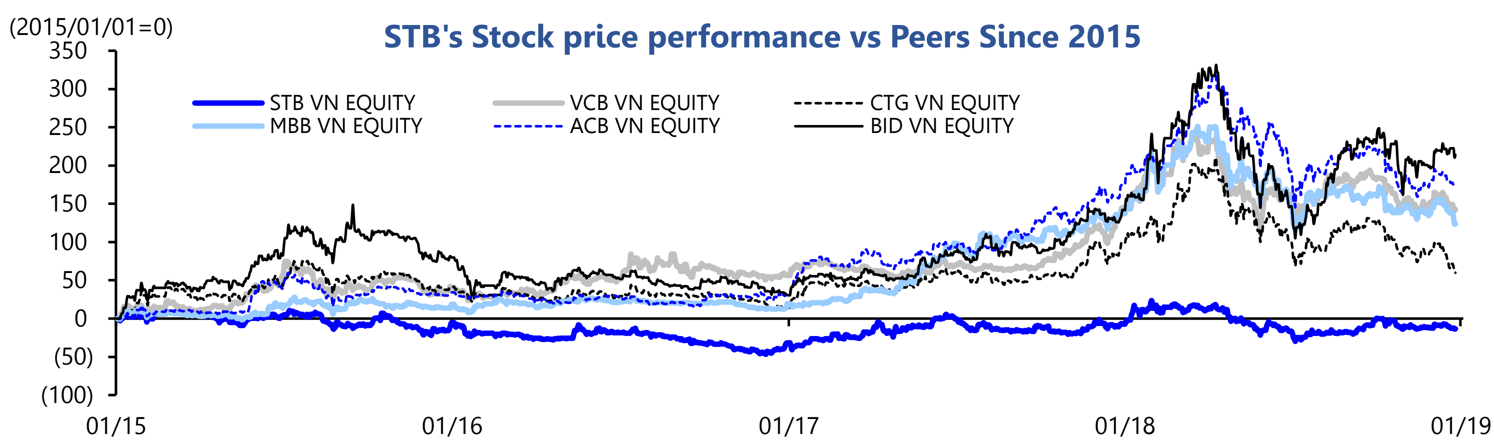
In 2018, Sacombank was awarded by International Card Organization JCB (Japan) as the leading bank in card spending, in card revenue growth, in the number of issued cards, and in the new issued cards. It was also awarded as the Outstanding E-banking by Vietnam Banking Association (VNBA) and IDG group. As of now, STB has more than 1.3 million people using internet banking services, and more than 1.1 million people using mobile banking services, with total transaction value of VND 110 tn monthly. Total customer is about 4.3 million customers in all branches and it currently has the largest networks with 566 branches and offices in Vietnam and Lao.

In 2018-2020, Sacombank aims to improve infrastructure to promote retail business and revenue from services to contribute to the overall profitability of the Bank. We expect services income to contribute 27.5% on average to the total operating income in 2018-20E, reducing exposure to loan growth.

Cashless payment will dominate the payment system in the future, and effective e-banking service like STB will gain significant market share. Bancassurance business also contribute a big portion to the total fee and commission incomes as demand to buy insurances to hedge against any unpredictable events. Sacombank and Dai-ichi Life Insurance Vietnam Company signed an exclusive insurance agency contract in 2017 with a 20-year term, which is considered the longest deal in the Bancassurance field in Vietnam.



Source: Bloomberg



Source: Bloomberg

Balance Sheet (Quarterly) (VND bn)	3Q.17A	4Q.17A	1Q.18A	2Q.18A	3Q.18A	4Q.18E	QoQ %	YoY %
Cash and equivalents:	16,039	9,213	17,296	17,555	19,725	10,451	*-47.0%*	*13.4%*
Loans and Advances to Banks:	2,164	7,375	5,236	6,813	1,856	7,741	*317.1%*	*5.0%*
ST & Long-Term Investments:	74,766	73,438	76,811	79,094	78,823	78,398	*-0.5%*	*6.8%*
Gross Loans:	223,016	222,947	229,441	246,691	253,392	255,367	*0.8%*	*14.5%*
(-) Specific Provisions:	825	1,046	1,178	1,336	1,761	1,192	*-32.3%*	*14.0%*
(-) General Provisions:	1,704	1,732	1,669	1,790	2,083	1,915	*-8.0%*	*10.6%*
Total provisions:	2,529	2,778	2,847	3,126	3,844	3,108	*-19.2%*	*11.9%*
Net Loans:	220,487	220,169	226,594	243,565	249,548	252,260	*1.1%*	*14.6%*
Property, Plant and Equipment (PP&E):	4,470	4,475	4,515	4,518	4,500	4,698	*4.4%*	*5.0%*
Intangible Assets:	3,598	3,626	3,620	3,633	3,609	3,626	*0.5%*	*0.0%*
Other Assets:	41,964	50,385	47,180	45,507	45,541	48,131	*5.7%*	*-4.5%*
Total Assets:	**363,488**	**368,681**	**381,252**	**400,685**	**403,602**	**405,379**	***0.4%***	***10.0%***
Deposits:	312,561	319,860	339,235	355,860	357,220	360,371	*0.9%*	*12.7%*
Due to Banks:	15,491	12,880	5,633	4,188	4,650	12,880	*177%*	*0%*
Subordinated Notes:	5,717	5,601	5,565	8,185	8,121	8,120	*0.0%*	*45%*
Investment Trust; Derivatives & others:	46	91	91	101	89	104	*16.9%*	*14.5%*
Other Liabilities:	6,890	7,020	7,059	8,702	9,743	(686)	*-107%*	*-110%*
Total Liabilities:	**340,705**	**345,452**	**357,583**	**377,036**	**379,823**	**380,789**	***0.3%***	***10.2%***
Share Capital & Share Premium:	18,167	18,167	18,167	18,167	18,167	18,167	*0.0%*	*0.0%*
Reserves:	2,519	2,550	2,550	2,719	2,719	2,784	*2.4%*	*9.2%*
Retained Earnings:	1,918	2,277	2,688	2,501	2,664	3,640	*36.6%*	*59.9%*
Others:	179	234	266	262	231	0	*-100%*	*-100%*
Total Equity:	**22,783**	**23,228**	**23,671**	**23,649**	**23,781**	**24,590**	***3.4%***	***5.9%***
Total Liabilities & Equity:	**363,488**	**368,680**	**381,254**	**400,685**	**403,604**	**405,379**	***0.4%***	***10.0%***

Income Statement (Quarterly) (VND bn)	3Q.17A	4Q.17A	1Q.18A	2Q.18A	3Q.18A	4Q.18E	QoQ %	YoY %
Net Interest Income	1,696	1,519	1,672	1,781	2,070	1,264	*-38.9%*	*-16.8%*
Interest Income	5,852	5,775	6,046	6,385	6,910	5,947	*-13.9%*	*3.0%*
Interest Expense	4,156	4,256	4,374	4,604	4,840	4,683	*-3.2%*	*10.0%*
Non-Interest Income	541	1,526	671	887	875	1,217	*39.1%*	*-20.3%*
Net Fee and Commission income:	456	1,328	544	589	626	1,063	*69.8%*	*-19.9%*
Other Income	85	198	127	298	249	154	*-38.2%*	*-22.4%*
Total Operating Income	2,237	3,045	2,343	2,668	2,945	2,481	*-15.8%*	*-18.5%*
Total Operating Costs	1,648	1,988	1,759	1,744	1,963	1,603	*-18.3%*	*-19.4%*
Pre-Provision Profit	589	1,057	584	924	982	878	*-10.6%*	*-17.0%*
Cummulated Pre-Provision Profit	*1,251*	*2,308*	*584*	*1,508*	*2,490*	*3,368*	*35.3%*	*45.9%*
Provisions	139	592	81	433	664	60	*-91.0%*	*-89.9%*
Profit Before Tax	450	466	503	491	318	819	*157.5%*	*75.8%*
Income Tax	143	55	107	121	155	43	*-72.3%*	*-22.2%*
Net Profit	307	411	396	370	163	775	*375.5%*	*88.8%*
Cummulated net profit	*771*	*1,182*	*396*	*766*	*929*	*1,704*	*83.4%*	*44.2%*

Selected Calculated Ratios (Quarterly)	3Q.17A	4Q.17A	1Q.18A	2Q.18A	3Q.18A	4Q.18E
GROWTH PROJECTIONS						
Quarterly (QoQ %)						
Net interest income	67.8%	-10.4%	10.1%	6.5%	16.2%	-38.9%
Non-interest Income	-18.6%	182.1%	-56.0%	32.2%	-1.4%	39.1%
Operating costs	24.6%	20.6%	-11.5%	-0.9%	12.6%	-18.3%
Provision	59.8%	325.6%	-86.3%	434.6%	53.3%	-91.0%
Pre-provision profit	66.9%	79.5%	-44.8%	58.2%	6.3%	-10.6%
Net profit	21.3%	33.7%	-3.5%	-6.6%	-55.9%	375.7%
Assets	2.1%	1.4%	3.4%	5.1%	0.7%	0.4%
Yearly (YoY %)						
Net interest income	77.2%	16.0%	58.9%	76.2%	22.1%	-16.8%
Non-interest Income	-21.7%	109.9%	5.7%	33.4%	61.7%	-20.3%
Other Income	-75.3%	-37.6%	-49.6%	43.3%	192.9%	-22.4%
Operating costs	8.8%	43.8%	27.6%	31.8%	19.1%	-19.4%
Provision	-357.4%	-16.4%	-8200.0%	397.7%	377.7%	-89.9%
Pre-provision profit	342.9%	61.8%	89.0%	161.8%	66.7%	-16.9%
Net profit	104.7%	-735.8%	87.7%	46.2%	-46.9%	88.9%
Assets	13.6%	10.6%	10.7%	12.6%	11.0%	10.0%
ASSET ANALYSIS						
Net interest income / average IEAs (NIM) (Quarterly)	0.57%	0.50%	0.54%	0.55%	0.62%	0.37%
Net interest income / average IEAs (NIM) (TTM)	1.79%	1.81%	1.95%	2.11%	2.21%	2.08%
Earning assets to total assets	82.5%	82.4%	81.7%	83.0%	82.8%	84.2%
Average loans to average earning assets	74.5%	73.9%	73.5%	73.9%	75.0%	75.3%
LOAN ANALYSIS						
Loan growth (QoQ %)	2.0%	0.0%	2.9%	7.5%	2.7%	0.8%
Loan growth (YoY %)	14.3%	12.1%	11.2%	12.9%	13.6%	14.5%
DEPOSIT ANALYSIS						
Deposit growth (QoQ %)	-1.4%	2.3%	6.1%	4.9%	0.4%	0.9%
Deposit growth (YoY %)	9.5%	9.8%	11.9%	12.2%	14.3%	12.7%
Deposits to Interest Bearing Liabilities	92.7%	93.2%	96.5%	96.9%	94.4%	94.8%
LIQUIDITY						
LDR	71.4%	69.7%	67.6%	69.3%	70.9%	70.9%
ASSET QUALITY						
NPL ratio	5.95%	4.16%	4.01%	3.70%	3.18%	3.16%
General Provisions to net loans	0.77%	0.79%	0.74%	0.74%	0.83%	0.76%
SPREAD ANALYSIS						
Interest rate received on Average IEA	1.97%	1.91%	1.97%	1.98%	2.07%	1.76%
Interest rate paid on Average IBL	1.23%	1.24%	1.24%	1.25%	1.28%	1.23%
Interest rate spread	0.74%	0.67%	0.72%	0.73%	0.79%	0.53%
OTHER INCOME						
Non-interest income to total income	24.2%	50.1%	28.6%	33.2%	29.7%	49.1%
Fees to non-interest income	84.3%	87.0%	81.1%	66.4%	71.5%	87.3%
Fees to total income	20.4%	43.6%	23.2%	22.1%	21.3%	42.8%
OPERATING EFFICIENCY						
Cost to income ratio	74%	65%	75%	65%	67%	65%
PROFITABILITY						
ROA	0.09%	0.11%	0.11%	0.09%	0.04%	0.19%
ROE	1.36%	1.78%	1.69%	1.56%	0.69%	3.21%
Pre-provision ROE	2.60%	4.60%	2.49%	3.91%	4.14%	3.63%
Pre-provision ROA	0.16%	0.29%	0.16%	0.24%	0.24%	0.22%

Income Statement (Annually)	Units:	Historical FY16A	Historical FY17A	Projected FY18E	Projected FY19E	Projected FY20E
Net Interest Income:						
(+) Interest Income:	VND bn	17,868	**21,534**	25,288	28,641	32,707
(-) Interest Expense:	VND bn	(13,848)	(16,256)	(18,501)	(20,821)	(23,128)
Total Net Interest Income:	VND bn	**4,021**	**5,278**	**6,787**	**7,821**	**9,579**
Total Net Non-Interest Income:	VND bn	**2,509**	**3,367**	**2,822**	**3,380**	**4,030**
Revenue (Net Operating Income):	VND bn	**6,530**	**8,645**	**10,437**	**12,105**	**14,594**
Total Non-Interest Expenses:	VND bn	**(5,678)**	**(6,337)**	**(7,069)**	**(7,868)**	**(8,907)**
Pre-provisioning Operating Income:	VND bn	**852**	**2,308**	**3,368**	**4,237**	**5,688**
(-) Provisions for Credit Losses:	VND bn	(419)	**(401)**	(455)	(521)	(631)
(-) Provision for debts sold to VAMC & others	VND bn	(277)	(416)	(783)	(1,410)	(1,904)
Total Provisions:	VND bn	(696)	(817)	(1,238)	(1,931)	(2,535)
Pre-Tax Income:	VND bn	**156**	**1,492**	**2,131**	**2,304**	**3,154**
(-) Income Tax Expense / (+) Tax Benefit:	VND bn	(67)	**(310)**	(426)	(461)	(631)
Reported Net Income:	VND bn	**89**	**1,182**	**1,704**	**1,843**	**2,523**
Attributable Net Income to Common:	VND bn	**50**	**798**	**1,354**	**1,528**	**2,092**
Adjusted Earnings Per Share (EPS):	*VND / Share*	*28*	*443*	*751*	*847*	*1,160*
Dividend Per Share (DPS):	*VND / share*			*0*	*0*	*42.36*
Dividend Yield (%)	*%*			*0*	*0*	*0.37%*

Balance Sheet (Annually)	Units:	Historical FY16A	Historical FY17A	Projected FY18E	Projected FY19E	Projected FY20E
Cash and Balances at Central Banks:	VND bn	14,827	**9,215**	10,451	11,396	12,481
Loans and Advances to Banks:	VND bn	2,484	**7,372**	7,741	8,128	8,534
Investment Securities - Available for Sale:	VND bn	66,395	**74,060**	78,375	74,459	70,933
Derivative Financial Instruments:	VND bn	15	**20**	23	25	27
Gross Loans:	VND bn	**198,860**	**222,947**	**255,367**	**294,286**	**335,361**
(-) Allowance for Loan Losses:	VND bn	(2,432)	**(2,749)**	(3,108)	(3,493)	(3,965)
Net Loans:	VND bn	**196,428**	**220,198**	**252,260**	**290,794**	**331,396**
Property, Plant and Equipment (PP&E):	VND bn	4,504	**4,475**	4,698	4,933	5,180
Intangible Assets:	VND bn	3,446	**3,626**	3,626	3,626	3,626
Accrued interests:	VND bn	25,336	**24,742**	23,446	22,064	20,594
Deferred tax:	VND bn	106	**74**	74	74	74
Other Assets:	VND bn	18,481	**24,686**	24,686	27,154	29,870
TOTAL ASSETS:	VND bn	**332,023**	**368,469**	**405,379**	**442,653**	**482,716**
Deposits:	VND bn	291,653	**319,860**	360,371	392,964	430,384
Due to Banks:	VND bn	11,884	**12,880**	12,881	12,881	12,881
Subordinated Notes:	VND bn	1	**5,601**	8,120	8,120	8,120
Investment Trust; Derivatives & others:	VND bn	1,404	**91**	104	120	137
Other Liabilities:	VND bn	4,889	**6,800**	(686)	2,526	3,166
Total Liabilities:	VND bn	**309,831**	**345,233**	**380,789**	**416,611**	**454,687**
Share Capital & Share Premium:	VND bn	18,167	**18,167**	18,167	18,167	18,167
Reserves:	VND bn	2,684	**2,784**	2,784	2,784	2,784
Retained Earnings:	VND bn	1,341	**2,286**	3,640	5,092	7,079
Total Equity:	VND bn	**22,192**	**23,236**	**24,590**	**26,042**	**28,029**
TOTAL LIABILITIES & EQUITY:	VND bn	**332,023**	**368,469**	**405,379**	**442,653**	**482,716**

APPENDIX I: TERMS FOR PROVISION OF REPORT, DISCLAIMERS AND DISCLOSURES

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Ratings	Total expected return within the next 12 months
BUY	Above 20%
HOLD	Between -20% to +20%
SELL	Below 20%

BUY: We have a positive outlook on the stock based on our expected absolute or relative return over the investment period. Our thesis is based on our analysis of the company's outlook, financial performance, catalysts, valuation and risk profile. We recommend investors add to their position.
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HOLD-Underperform: In our view, the stock's fundamentals are relatively less attractive than peers at the current price. Our thesis is based on our analysis of the company's outlook, financial performance, catalysts, valuation and risk profile.
SELL: We have a negative outlook on the stock based on our expected absolute or relative return over the investment period. Our thesis is based on our analysis of the company's outlook, financial performance, catalysts, valuation and risk profile. We recommend investors reduce their position.
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