MILITARY COMMERCIAL JSB (MBB) - UPDATE

Market Price	Target Price	Dividend Yield	Rating	Sector
VND32,800	VND38,600	1.83%	ADD	FINANCIALS

Outlook – Short term	Outlook – Long term	Valuation
Negative Neutral Positive	Negative Neutral Positive	Negative Neutral Positive

27 February 2018
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We reiterate our ADD recommendation for MBB and raise our target price by 39.4% to VND38,600 due to: 1) a lowering of forecasted provision expenses in FY18 and 2) an increase in the fee income growth forecast for the year. Valuation looks cheap relative to peers.

A plunge in FY18 provision expense will boost earnings growth. In 2017, MBB aggressively provisioned for VAMC bonds to complete all VAMC bonds provisioning obligations. As a result, the bank will not need to book provision for VAMC bonds going forward. Although we model for higher provision expenses for on balance sheet loans, the lack of VAMC provisions in FY18 will reduce total provision expenses. We project that provision expense will fall by 38.4%, facilitating a 56.1% growth in pre-tax profit.

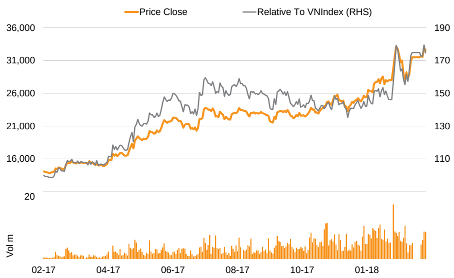
NIM expansion will continue in FY18 but at a slower pace than in FY17. Strong growth of individual loans in FY17 resulted in a 62bps increase in NIM compared to FY16. In 2018, retail lending will remain the strategic priority at MBB and therefore, NIM is projected to increase further. Since MBB has been pushing retail lending for the past three years, growth in the retail loan book will decelerate off a higher base, and thus NIM expansion will temper in pace. We expect NIM to rise by 16bps to touch 4.3% in FY18.

MBB is looking to push fee income through bancassurance and internet/mobile banking. Bancassurance will be a major driver of fee income growth in FY18, as MBB has just started life insurance distribution in 2017 and plans to push this product, going forward. Besides, MBB continues to promote transactions via its internet banking platform and Bankplus – a cooperative mobile banking platform with Viettel – to increase income from payment services and reduce operating cost. We project 40% growth in fee income for FY18.

High loan growth to be supported by sufficient capital and funding. FY17 capital adequacy ratio (CAR) of 12% and loan-to-deposit ratio (LDR) of 73.2% provide headroom for strong loan growth in FY18. We project FY18 loan growth of 18%, which is lower than 22% in FY17, as the State Bank of Vietnam (SBV) has set a lower credit growth target of 17% in 2018, and thus credit quota for banks might be reduced this year. Despite lower loan growth however, MBB can still achieve robust profit thanks to the aforementioned NIM expansion and sharp fall in provision expenses.

MBB still trades at a discount to peers. MBB is trading at a 2.1x current P/B and 1.8x FY18 forward P/B, compared to the corresponding peer averages (ex-VCB) of 2.4x and 2.2x, respectively. We increase our target price to VND38,600, equating to a FY18 P/B of 2.1x.

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	33,100
52w low (VND)	12,867
3m Avg daily volume (shares)	6.4mn
3m Avg daily value (VNDmn)	172,749
Market cap (VNDbn)	59,549
Outstanding shares (m)	1,816
Free float (%)	20
TTM P/E	20.0x
Current P/B	2.1x

Ownership

Viettel	14.75%
SCIC	9.83%
Vietnam Helicopter Corporation	7.84%
Tan Cang Saigon	7.52%
Vietcombank	6.97%
Others	53.09%

Source: VNDIRECT

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net interest income (bn)	7,979	11,219	13,566	15,598
Net interest margin	3.5%	4.1%	4.3%	4.4%
Total operating income (bn)	9,855	13,867	16,742	19,329
Total provision charges (bn)	(2,030)	(3,252)	(2,004)	(2,002)
Net profit (bn)	2,912	3,490	5,454	6,549
Net profit growth	16.7%	19.9%	56.3%	20.1%
Adjusted EPS	1,390	1,642	2,554	3,066
BVPS	14,097	15,516	17,954	20,962
ROAE	12.1%	13.0%	18.0%	18.5%

Source: VNDIRECT

2017 RESULTS – STRONG INCOME GROWTH FACILITATED AGGRESSIVE PROVISIONING

FY17 bottom line fell below our forecasts despite the strong core growth, as there was a sharp rise in provision expenses and a higher cost to income ratio (CIR). Strong growth was posted across major business segments: net interest income increased by 40.6% yoy, net fee income jumped by 65.6% yoy and other non-interest income grew by 27.1% yoy. Provision expenses surged by 60.2% yoy, as MBB looked to speed up bad debt clearing. CIR increased from 42.4% in FY16 to 43.3% in FY17 due to a 41.6% jump in salary expenses as the bank is expanding its headcount to support retail lending growth. FY17 pre-tax profit and net profit reached VND4,616bn and VND3,490bn, translating to 26.4% and 19.9% growth, respectively. MBB fulfilled 107% of its PBT target, but still fell 9% below our forecast due to higher provisioning expenses than we had anticipated.

Figure 1: FY17 business results and performance metrics (VND bn)

	2016	2017	YoY growth
Net interest income	7,979	11,219	40.6%
Non-interest income	1,876	2,648	41.1%
Pre-provision profit	5,681	7,868	38.5%
Provision expenses	-2,030	-3,252	60.2%
Pre-tax profit	3,651	4,616	26.4%
Net profit	2,912	3,490	19.9%
Loan growth	24.2%	22.2%	
Deposit growth	7.3%	13.0%	
Non-performing loans (NPL)	1.3%	1.2%	
Net interest margin (NIM)	3.5%	4.1%	

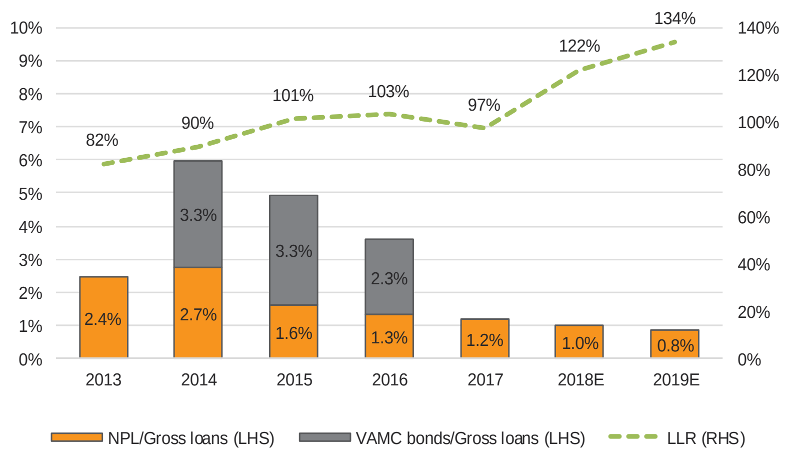
Source: VNDIRECT, Company

Rising NIM fueled net interest income growth. The robust growth in MBB's retail individual loan book (+33.3% yoy) lifted blended asset yields by 47bps. Consequently, MBB's NIM rose from 3.5% in FY16 to 4.1% in FY17. Although FY17 loan growth (22.2% yoy) was lower than FY16 (24.2% yoy), and FY17 deposit growth (13% yoy) was higher than 7.3% yoy growth in FY16, NIM still increased due to rising asset yields.

The bank's fee income growth was driven by income from payment services and the consolidation of the insurance business. Net income from payment services increased by 51.4% yoy, while net income from insurance jumped 2.8 times versus FY16. Insurance income came from Military Insurance Company (MIC), which became a subsidiary of MBB in 4Q16 after MBB increased its stake in MIC from 49.8% to 69.6%. Therefore, income from MIC was consolidated into the bank's financial statements starting 4Q16. On a pro-forma basis (assuming consolidation of MIC results for the entire year of 2016), net fee income growth was still healthy at 18.4% yoy.

The surge in provision expenses was due to higher VAMC provisioning and due to a bid to accelerate write-offs. General provisions booked in FY17 were nearly equal to FY16, but specific provisions booked were more than double the amount of FY16, as MBB wrote-off more bad debt. Due to the large amount of write-offs, the NPL ratio fell from 1.3% in FY16-end to 1.2% in FY17-end. We estimate that MBB booked VND1,600bn worth of provisions for VAMC bonds in 2017, compared with VND1,000bn in 2016, as the bank sped up bad debt clearing. By the end of 2017, MBB had fully provisioned for VAMC bonds, one year earlier than the plan set in its 2017 AGM. MBB is the third bank in the system to have fully provisioned for VAMC bonds. Although provision expenses increased sharply, we view this as a positive for MBB since the bank has now completed the current provisioning cycle.

Figure 2: MBB has good asset quality with low NPL and high LLR



Source: VNDIRECT, Company

2018 FORECAST – IMPRESSIVE EARNINGS GROWTH EXPECTED DUE TO SHARP FALL IN PROVISION EXPENSES

Loan growth will be in line with sector credit growth. We forecast loan growth of 18% in FY18, down from 22% in FY17. SBV has started to tighten credit growth with a credit growth target of 17% for 2018 after two years of 18%-plus growth. As a result, the credit growth quota for each bank might be reduced compared to 2017. We project 13% growth in customer deposits in FY18, same as that in FY17, enabling the bank to maintain a healthy LDR level.

CIR will increase due to retail lending expansion. In order to expand its retail lending business, MBB plans to open 10 new branches in 2018. In addition, we expect a continued expansion of its sales force to boost overall headcounts. We revise up our CIR assumption for FY18 to 45% from 42%, previously.

Provision expense is projected to fall by 38.4% despite higher provisioning for on-balance sheet loans. As MBB fully provisioned for VAMC bonds in FY17, there will be zero VAMC provision expenses in FY18 while we forecast a higher provision expense for on-balance sheet loans. As a result, the loan-loss-coverage ratio (LLR) is projected to improve from 97.3% in FY17 to 122.3% in FY18. However, FY17 provision expense for VAMC bonds accounted for circa 50% of total provision expense, and therefore the absence of VAMC provisions in FY18 will result in a sharp fall in total provision expense.

Stable pre-provision profit growth and lower provision expense will drive 56% earnings growth. FY18 pre-provision profit is forecasted to grow 17%, but a 38% decrease in provision expenses will lead to robust profit growth. FY18 pre-tax profit and net profit are forecasted to grow by 56.1% and 56.3%, respectively.

VALUATION

We use a residual income and target P/B multiple-based approach to value MBB with a weighting of 70% and 30%, respectively. Residual income approach is based on the forecasted earnings and growth of MBB, and factors in the bank's current capital buffer and its business strategy. On the other hand, P/B multiples approach allows us to value MBB relative to other banks and factors in the market sentiment on the banking sector as a whole. However, each bank has distinctly different fundamentals and earnings prospects and, therefore, we only give a 30% weighting to this relative valuation approach.

Figure 3: Valuation

Approach	Weight	Fair value	Contribution
Residual income	70%	38,990	27,293
P/B multiple (at 2.1x)	30%	37,704	11,311
Target price			**38,604**

Source: VNDIRECT

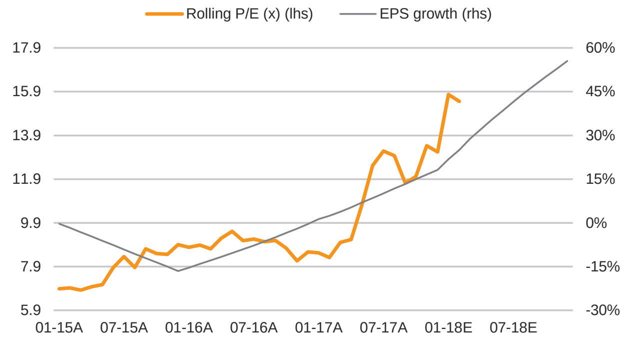
MBB has been re-rated but still trades at discount to peers. We think that MBB deserves higher valuation given high ROE, good asset quality and healthy capital buffer. FY17 ROE was 13%, slightly lower than the peer average of 13.5% but FY18 ROE is forecasted to reach 18% due to robust profit growth. For the P/B multiples approach, we use a target P/B of 2.1x on forecasted 2018 year-end book value per share. Combining the P/B multiple approach and residual income approach, we get a target price of VND38,600. At our target price, FY18's forward P/B works out to 2.1x.

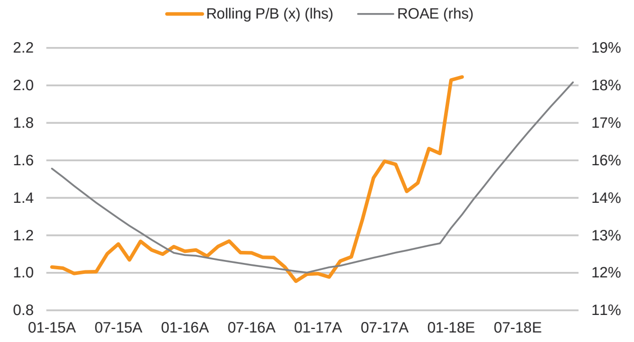
Figure 4: Bank multiples comparison

Banks	Market cap (VND bn)	FY17 ROE %	FY17 ROA %	FY17 P/B	FY17 P/E	FY18E P/B	FY18E P/E
VCB	263,357	17.8%	1.0%	4.9	29.0	4.0	27.8
BID	130,424	15.2%	0.6%	2.8	18.9	2.5	21.3
CTG	119,521	12.0%	0.7%	1.9	16.1	1.7	17.1
ACB	45,746	14.1%	0.8%	3.0	25.5	2.3	11.9
VIB	16,289	12.8%	1.0%	2.0	15.4	2.2	24.0
Average	*115,067*	*14.4%*	*0.8%*	*2.9*	*21.0*	*2.5*	*20.4*
Average-ex VCB	***77,995***	***13.5%***	***0.8%***	***2.4***	***19.0***	***2.2***	***18.6***
MBB	**59,549**	**13.0%**	**1.2%**	**2.1**	**20.0**	**1.8**	**12.8**

Source: VNDIRECT, Bloomberg

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net interest income	**11,219**	**13,566**	**15,598**
Non interest income	**2,648**	**3,176**	**3,731**
Total operating income	**13,867**	**16,742**	**19,329**
Total operating costs	(5,999)	(7,534)	(8,698)
Pre-provision operating profit	**7,868**	**9,208**	**10,631**
Total provision charges	**(3,252)**	**(2,004)**	**(2,002)**
Income from associates & JVs			
Net other income			
Pre-tax profit	**4,616**	**7,204**	**8,629**
Taxation	(1,125)	(1,756)	(2,104)
Profit after tax	**3,490**	**5,448**	**6,525**
Minority interests	0	6	24
Net profit	**3,490**	**5,454**	**6,549**

	12-17A	12-18E	12-19E
Growth rate (yoy)			
Cust deposit growth	13.0%	13.0%	16.0%
Gross cust loan growth	22.2%	18.0%	18.0%
Net interest income growth	40.6%	20.9%	15.0%
Pre provision operating profit growth	38.5%	17.0%	15.5%
Net profit growth	19.9%	56.3%	20.1%
Growth in IEAs	23.3%	11.4%	13.2%
Share value			
Basic EPS (VND)	1,932	3,004	3,607
BVPS (VND)	15,516	17,954	20,962
DPS (VND)	600	600	600
EPS growth	18.2%	55.5%	20.1%

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Gross loans to customers	184,188	217,342	256,464
Loans to banks			
Total gross loans	**184,188**	**217,342**	**256,464**
Securities - total	53,841	54,380	56,555
Other interest earning assets	60,303	60,906	63,342
Total gross IEAs	**298,332**	**332,628**	**376,361**
Total provisions	**(2,486)**	**(3,005)**	**(3,277)**
Net loans to customers	**182,062**	**214,700**	**253,564**
Total net IEAs	**295,847**	**329,622**	**373,083**
Cash and deposits	1,842	1,971	2,109
Total investments	1,077	1,153	1,233
Other assets	15,112	16,170	17,301
Total non-IEAs	**18,031**	**19,293**	**20,644**
Total assets	**313,878**	**348,916**	**393,727**
Customer deposits	220,176	248,799	288,607
Cds outstanding	6,022	6,022	6,022
Customer interest-bearing liabilities	226,198	254,821	294,629
Bank deposits	1,848	1,848	1,848
Broad deposits	228,046	256,669	296,477
Other interest-bearing liabilities	46,398	46,428	46,461
Total IBLs	**274,444**	**303,097**	**342,937**
Deferred tax liability			
Other non-interest bearing liabilities	9,832	11,791	11,302
Total non-IBLs	**9,832**	**11,791**	**11,302**
Total liabilities	**284,277**	**314,888**	**354,240**
Share capital	18,155	18,155	18,155
Additional paid-in capital	0	0	0
Treasury shares			
Retained earnings reserve	5,977	10,404	15,864
Other reserves	4,037	4,037	4,037
Shareholders' equity	**28,170**	**32,596**	**38,056**
Minority interests	1,431	1,431	1,431
Total equity	**29,601**	**34,028**	**39,487**
Total liabilities & equity	**313,878**	**348,916**	**393,727**

Key ratios

	12-17A	12-18E	12-19E
Net interest margin	4.1%	4.3%	4.4%
Cost-income ratio	(43.3%)	(45.0%)	(45.0%)
Reported NPLs / gross cust loans	1.2%	1.0%	0.8%
Reported NPLs / net cust loans	1.2%	1.0%	0.9%
GP charge / average cust loans	1.9%	1.0%	0.8%
Total CAR	12.0%	12.2%	12.3%
Loan deposit ratio	81.4%	85.3%	87.0%
Margins and spreads			
Return on IEAs	7.3%	7.5%	7.7%
Cost of funds	3.5%	3.5%	3.6%
Interest return on average assets	3.9%	4.1%	4.2%
ROAE	13.0%	18.0%	18.5%

Source: VNDIRECT

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

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

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

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