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MASTER'S THESIS

Improving the Management of Non-Performing Loans in Joint Stock Commercial Banks - The Case of the Bank for Investment and Development of Vietnam (BIDV)– Quang Trung Branch

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LIST OF ABBREVIATIONS

Agribank	Vietnam Bank for Agriculture and Rural Development
BIDV	Joint Stock Bank for Investment and Development of Viet Nam
BIDV QT	Joint Stock Bank for Investment and Development of Vietnam – Quang Trung Branch (BIDV Quang Trung)
BOD	Board of Director
BOM	Board of Manager
CEO	Chief Executive Officer
CIC	Credit Information Center
DGD	Deputy General Director
FED	Federal Reserve
GD	General Director
IAS	International Accounting Standards
IPO	Initial public offering
LGD	Loss given default
NPL (NPLs)	Non-performing loan (Non-performing loans)
SBV	State Bank of Vietnam
SWIFT	Society for Worldwide Interbank Financial Telecommunication
UN	United Nations
VCB	Joint Stock Bank for Foreign Trade of Vietnam
Vietinbank	Vietnam Joint Stock Commercial Bank for Industry and Trade
VND	Vietnam Dong
VP	Vice President

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EXECUTIVE SUMMARY

For the last few decades BIDV has consistently remained one of the largest commercial banks in Vietnam – placing itself among the key players in funding and supplying banking services and also serving as an important intermediary for the State Bank's fiscal and monetary policies. Since its inception in April 2005, BIDV – Quang Trung Branch (hereby known as BIDV QT for short) has become one of the largest and the most effective branches in the BIDV system.

In the wake of the global economic downturn at the end of 2012, however, the banking sector was hit hard since most if not all clients were affected to varying degrees. As businesses downsized to stay alive and many individuals going bankrupt, problems started arising for even the most bullet-proof of financial institutions, namely BIDV. Non-performing loans (NPLs) skyrocketed, which had a dual effect: banks' profits started to go down from writing off bad debts and lending came to a halt, thus disrupting the flow of capital in the whole economy. Owing to these factors, BIDV QT has been facing many challenges as its market share shrinks, loyal customers either leave or go out of business. To make matters worse, BIDV QT's credit rating has been downgraded due to the sheer amount of NPL it carries.

As someone who is directly involved at BIDV QT's operations, I decided on the topic of "Improving the Management of Non-performing Loans in Joint Stock Commercial Banks – The Case of the Bank for Investment and Development of Vietnam (BIDV) – Quang Trung Branch" for the final project.

INTRODUCTION

1.1. Problem statement

In the banking sector, credit activities account for most of the bank's total income. However, these activities are inherently risky - especially emerging economies like Vietnam's. Because of many factors, namely a lack of transparency in the information system, underdeveloped risk management processes, and low professionalism among bank officers – the need for a working model of credit risk management is more urgent than ever.

P. Volker, former chairman of FED, once said: "If banks do not have NPLs, it is not business." For all commercial banks, credit risk is a fact of life. Even the world's leading banking institutions cannot escape from NPLs, simply because there are many factors beyond human control. What separates an effective risk management model from an ineffective one is how much controllable risk it can reduce or eliminate altogether.

The biggest challenges commercial banks in Vietnam now face are a weak financial position and an extremely high rate of NPLs per total outstanding loans. The problem here is not only to collect NPLs from previous years quickly but also to prevent NPLs from increasing. Only then can Vietnam's commercial banks get back on their feet financially and remain competitive.

Take an example from BIDV Quang Trung: from the year 2009 to 2012, our cumulative credit growth rate was 35.09% (from 2,524 billion to 3,430 billion VND). At the same time, our NPL ratio shot more than 3-fold, from 1.05% to 3.20%, 1.14 times maximum ratio of 2.8% set by BIDV Headquarter. Our credit activities became much less efficient amid a surge in credit risk and liquidity risk. The aftermath was not just financial – our credit rating was demoted and our brand name suffered.

Therefore, one of our top priorities at BIDV Quang Trung is to standardize risk management practices in the shortest time frame. Managing NPLs in compliance with current international standards will enable commercial banks to provide better products and services at a lower price by allowing a quicker capital turnover rate and of course, a smaller allowance for bad debts, which cuts directly into net profit.

1.2. Research objectives

The core objective of the final project is to find answers for the following research questions:

1. Is management NPL a major factor causing this increase?
2. What can management at BIDV QT do to deal with the current NPL and reduce future NPL?

In an effort to clarify the matters, I used both primary and secondary data from in-depth interview, reports system from internal credit rating and other sources. The research methodology applied during the research is the combination of quantitative and qualitative methods.

After thorough analysis to answer these questions, I have some recommendations to improve the managing NPL at BIDV QT, helping the bank reduce the NPL rate in the coming years.

1.3. Research questions

The above content can be further broken down into the following problems that need an answer to:

1. What are the current policies on managing credit & NPL at BIDV Quang Trung?

2. What caused the surge in NPLs at BIDV Quang Trung?

3. How can BIDV Quang Trung effectively manage its NPL?

4. What are the recommendations for improving managing NPL at BIDV Quang Trung?

1.4. Research methodology

1.4.1. Methodology

The final project uses the Basel Accords as a standard to rate the financial position and income predictability of a bank as well as its credit risk over time. The final project also uses qualitative and quantitative methods to measure and evaluate the related data. The qualitative method is suitable for complex research with intention to provide a deeper understanding and analyze the overall picture. The quantitative techniques are mostly way of measuring the statistic selections to get the results more standardized in comparison with qualitative method.

1.4.2. Data collection

Both primary and secondary data is used for analysis. As the author found out secondary data, even though quite abundant in quantity, was not sufficient for the scope of the research, primary data is also utilized. Primary data is collected through in-depth interviews and discussions with high-ranked bankers. Secondary data included banks' annual reports, financial statements, websites, television, newspapers, government publication, finance journals, banking statistics, books, surveys and industry reports.

1.4.3. Selection

Qualitative interviews do not require a certain way selecting interviewees. However, the main principle is that the selection should be made in the interest of the researcher's aim (Rolf Johansson, 2003). The author sought out people with experience on NPLs and asset management who were willing to provide with sometimes sensitive information. Those include directors, managers of corporate customer department, loan managers, compliance control and inspection managers, officers with many years of experience with handling NPLs *(detail listed in Annex I).*

1.4.4. Interview

The author chose to conduct an in-depth interview which is a crossed method between structured and unstructured interview. It contains both the strict schedule from the structured interview as well as the flexibility and conversation-like discussion from the unstructured interview. The objective of an in-depth interview is to understand thoroughly the reasons causing increasing NPL at BIDV QT. The author followed certain objective but still leave room for other information of interest. The questionnaires which include 12 questions for directors, managers and 11 questions for staff who work at BIDV QT were formulated and constructed in order to avoid asking indistinct formulations, difficult designed questions. There were 20 interviewees which included 1 director, 2 deputy directors, 3 managers, 3 deputy managers, 1 supervisor, 10 officers in the departments of BIDV QT(*with the detail listed in Annex II*).

1.4.5. Methods of conducting interviews

In order to make the primary data representative, the author found it necessary to audio record the interviews. However, being aware of that taping an interview can affect the interviewee as it might make him/her feel uncomfortable (Crane, 2004), the author made it clear that the recording was to be used for academic purpose only. Notes were also taken during the time of interview. Each interview was carefully transcript to prevent information loss through human errors.

1.5. Research scope

The study of this research would enable the researcher to have better understanding of the management of NPL at BIDV QT. In the scope of the final project with limited time and resources, the research focuses only on the credit activities of BIDV QT from 2010 to 2013.

1.6. Research structure

The final project includes three chapters:

Chapter I ***"Theoretical Framework"*** review the relevant theories on managing NPL, giving main ideas and some evaluation.

Chapter II ***"Current status of NPLs management at BIDV QT from"*** provides an overview as well as analysis on managing NPL at BIDV QT.

Chapter III ***"Recommendations to improve the management of NPLs at BIDV QT"*** brings some suggestions to reduce NPL rate and thus increases credit quality.

CHAPTER I: THEORETICAL FRAMEWORK FOR NPL MANAGEMENT IN COMMERCIAL BANKS

I.1. CONCEPT

I.1.1. Definition of credit risk

Credit risk is the risk of property loss resulting from borrowers who are not able to perform part or all of the commitments signed with the bank.

According to the Basel Committee's literature, "Credit risk is the change of net income and the value of capital derived from the loan which is not paid or paid late."

In Vietnam, in accordance with decision No. 493/QD-NHNN dated 22 April 2005 issued by the SBV, "Credit risk is the possibility of losses resulting from the borrower failing to perform its obligations under the commitment."

Credit risk is a major concern for commercial banks because it is associated with their main revenue-generating activity, which is granting credit. Banks are required by laws to accurately analyze borrowers' financial position in order to ensure the loans' collectability.

Credit risk is usually associated with providing credits, which is the largest and most important operation in a commercial bank. In a perfect world, when banks lend out money, they must try to collect and analyze all information related to the borrower, following the standard regulations to ensure the collectability of the loans. However, there are many factors affecting the customers' solvency that neither banks nor anyone else can foresee – the economy, for example. Bank staffs can definitely make human mistakes in judging a project's feasibility. Sometimes, staffs even collude with customers to create false financial analyses. As a rule of thumb, expecting the unexpected is the way of the banking industry. For the scope of this project, we mainly focus on the risks that can be measured.

I.1.2. Indicators of credit risk

- **The indicators:**

Banks are required to minimize financial losses should the event of a default occur. Credit risk can be assessed based on the following main criteria:

- Overdue loans as a percentage of total outstanding loans;
- NPL and NPL rate on total outstanding loans;
- The diversification of outstanding loans
- The collaterals;
- The relationship between the customers and the bank;
- Business environment of the customers' industry.

Banks are recommended to collect as much information as possible regarding the above aspects to ensure the loan's safety.

- **The measures of credit risk**:

Credit risk measures are devised to quantify the risk of losses due to counterparty default. Credit risk is generally broken down into three components:

- ***Default risk:*** is the possibility that a borrower fails pay off all or part of his obligations. There are several criteria as to when a default occurs, such as: missing payment for more than 90 days, filling for bankruptcy, breaking a covenant (which triggers a cross-default for all lenders.) Default risk depends on many factors, both qualitative and quantitative. Borrowers in a weak financial situation, high debt burden, low and/or unstable income have a higher risk of default.

- Qualitative factors such as the state of relevant industries and management quality can also help banks determine the risk level for each customer. Markets with more competition and harsher economic conditions are more likely to result in businesses defaulting. Another factor would be the financial backing that a customer may have access to. A subsidiary that is not doing well financially can receive support from its parent company and therefore less likely to default.
- ***Exposure risk:*** Exposure risk measures the amount at risk when lending to counterparty. The level of exposure risk varies with the types of transactions. For the amortized loans, principal is paid off over time, therefore exposure risk is reduced. For lines of credit, however, the exposure risk is consistent during the life of the contract. For project financing transactions, exposure risk tends to rise from the beginning of the contract, reaching its highest level at the middle stage of project development and declines afterwards. For transactions involving derivatives, exposure risk varies during the life of the contract as market indicators change. Exposure risk is particularly high with these transactions because, as it is well known, derivatives can oftentimes be extremely volatile.
- ***Loss risk:*** The loss risk determines the loss as a fraction of the exposure in the case of default. In the Basel II, this parameter is known as the loss given default which is the amount of funds that is lost by a bank or other financial institution when a borrower defaults on a loan. Academics suggest that there are several methods for calculating the loss given default, but the most frequently used method compares actual total losses to the total potential exposure at the time of default. Of course, most banks don't simply calculate the LGD for one loan. Instead, they review their entire portfolio and determine LGD based on cumulative losses and exposure.

I.2. NPL IN COMMERCIAL BANK

I.2.1. Definition of overdue loan

Overdue loans are loans that customers fail to repay in full on the maturity date of the loan contract. According to Decision No. 493/2005/QD-NHNN dated 22/4/2005 issued by the SBV, overdue loan is understood as "a loan of which a part or all of the principal and/or interest has not been paid." In commercial banks, the level of overdue loans reflects the level of credit risk.

I.2.2. Definition of NPL

- According to international standards

According to the NPL Statistics Division – United Nations, " a loan is considered NPL if interest and/or the principal are overdue more than 90 days; or unpaid interest from more than 90 days was added to the principal, or the payments are overdue less than 90 days, but it is reasonable to suspect the possibility that the loan will be fully paid." Thus, NPL is determined by two factors: (i) expired more than 90 days and (ii) solvency in doubt. This is also the working definition of NPL in the International Accounting Standards (IAS).

- According to Vietnamese standards

Decision No. 493/QD-NHNN dated 22 April 2005 and Decision No. 18/2007 by the SBV dated 25 April 2007 defined NPL very similarly to international standards.

I.2.3. Classifying loans using quantitative and qualitative measures

Banks can classify loans on either a quantitative or qualitative basis. Both methods result in a 5-group classification:

- Group 1: standard loans

- Group 2: loans that require attention
- Group 3: sub-standard loans
- Group 4: loans in doubt
- Group 5: loans at a high risk of being defaulted

Corresponding to each group, the State bank mandates a fixed amount of allowance: 0%, 5%, 20%, 50% and 100%, respectively.

Decision No. 493/QD-NHNN dated 22 April 2005 issued by the SBV regulates: "NPL are loans which are classified in group 3 to 5." The criteria for classifying loans are as followed *(Quotes Article 6, Article 7 of Decision 493/2005/QD-NHNN):*

- **Classification of debt by quantitative methods:**
  - Group 3 (Sub-standard loans) includes loans that are overdue from 91 to 180 days; first-time restructured loans (except for ones already classified into Group 2; loans whose principal and/or interest have been partially waived; and other obligations that are classified in Group 3.
  - Group 4 (Loans in doubt) includes loans that are overdue from 181 days to 360 days; first-time restructured loans that are overdue by less than 90 days from the date of restructuring; loans that have been restructured for the second time; and other obligations that are classified into Group 4.
  - Group 5 (Loans at a high risk of being defaulted) includes loans that are overdue by over 360 days; first-time restructured loans that are overdue by more than 90 days from the date of restructuring; overdue loans that have been restructured for the second time; loans that have been restructured more than two times; classified loans, and other obligations that are classified in Group 5.
- ***Classification of debt by qualitative methods:***
  - Group 3 (Sub-standard loans) include loans of which the possibility of collecting all of principal and interest when they mature is unlikely.
  - Group 4 (Loans in doubt) includes loans at a higher risk of default than Group 3.
  - Group 5 (Loss debt) includes loans that are very likely to be defaulted.

Under both international and Vietnamese standards, NPL is considered to be loans which are overdue for more than 90 days and/or judged to be wholly or partly unrecoverable.

I.2.4. The impact of NPL on the operation of commercial banks

NPL is part of being in the banking business. The trick is how to keep NPL in control and predictable. A higher than expected NPL rate may cause have serious consequences, affecting the banks, the customers, and sometimes in extremely bad cases, the economy:

- **NPL reduces profitability**

Even if an NPL is eventually paid off, this incurs loss for the bank because of the time value of money. Moreover, when NPL incurred, banks must set aside an allowance for bad debts, depending on how long the loans have been overdue. This allowance is taken directly out of net earnings. Handling of NPL can be very expensive too. And in the worse case when an NPL is written off and collaterals sold, very rarely do we see a bank recovering the full amount.

- **NPL hurts the bank's reputation**

Reputation is everything in the banking business. A lowered reputation will surely result in lower deposit and consequently, lower lending. Big customers will steer away from banks without a strong reputation because the fact is, interest rates among the state-owned banks do not differ in any conceivable way, and there are four of them to choose from. Maintaining a good image is one of the top priorities at BIDV, as it is at any other place.

- **NPL can cause insolvency**

Banks, as any other type of business, can go out of business if sustaining losses for too long. However, unlike other businesses, banks build its foundation on customer's trust. Once a bank is seen as "weak", customers may choose to put their money elsewhere, and things can only start going down from there. We have seen examples of hundred years old banks going out of business in a week after the public finds out they had made a bad investment and suffered a big loss. This is because banks keep only around 10% of deposits as reserve – the rest is lent out. Once the public decides their money is not secured, they can rush to withdraw their deposit – effectively making the bank insolvent.

I.3. THE THEORY OF NPL MANAGEMENT IN COMMERCIAL BANK

I.3.1. Definition

Management NPL is not only how to handle NPL when it incurred but also includes developing and implementing the strategies and policies of credit management in banking business in order to achieve safety objectives, efficient and sustainable development. Additionally, it is highly focused on the strengthening of measures to prevent and minimize NPL incurred; along with the handling these incurred NPL in order to match with the goal in each stage of the bank.

I.3.2. The objective of NPL management

The objective of managing NPL in each stage of banking business is different. However, in a general way, the objective of managing NPL in any circumstance for the bank is that it must develop and implement a regulation, policy to classify customers in accordance with each period to restrict the lowest level of risk from the loans without affecting the target profit of the bank.

I.3.3. Basel principles on managing NPL

The Basel Committee issued 17 guidelines on managing NPL, the majority of which deal with ensuring safety and efficiency in credit activities. The principles can be summarized into the following points:

- **Develop a system for credit monitor and management (3 principles)**: in this context, the Basel Committee urges BODs to perform periodical credit risk assessments and to continually develop new strategies and policies as soon as new information emerges. The General Director would then be in charge of enforcing the aforementioned strategies and policies in order to maintain control of NPLs at all levels of the bank's portfolio.
- **Granting "healthy" credits (4 principles)**: as commercial banks usually serve an extremely broad range of customers, they offer many different products tailored to fit the needs of everyone and everything from individuals to international conglomerates. For each of those products, banks must clearly define at least the following criteria: eligibility, amount, duration, other terms and conditions. After that, customers need to go through a filtering process under the form of an internal credit rating system, which, based on each customer's creditworthiness, determines if one is eligible for a loan, and if yes, how much. The procedures should be unified and unambiguous. Aside from the obvious factor of financial position, the role of the credit officer cannot be overlooked.
- **Utilizing information system for credit risk analysis and management (10 principles)**: Banks must have a system by which customers files are continually collected and kept up-to-date. The complexity of this system will depend on each bank's scale of operation. At a minimum, this system should be able to keep up with clients' financial information and

compliance status to quickly detect NPL. The next step can be assigned to either the debt handling department or the marketing department or sometimes, both, depending on the loan itself. The Basel Committee also recommends that banks build a rating system or its assets at risk.

CHAPTER II: CURRENT STATUS OF NPL MANAGEMENT AT BIDV QT

II.1. INTRODUCTION TO BIDV QT

II.1.1. Overview

BIDV QT was established in 2005 after being spun-off from BIDV SGD I. From a humble start with only 700 billion VND in total outstanding loans and a relatively small customer base, the branch has grown exponentially over the years, with outstanding loans shooting almost 10-fold after 8 years. BIDV QT prides itself on having the smallest workforce in relation to net income in the BIDV system. Normally a branch of comparable size and profitability has around 400 employees. At BIDV QT we make do with just over 200, around 80 of whom are directly involved in credit activities.

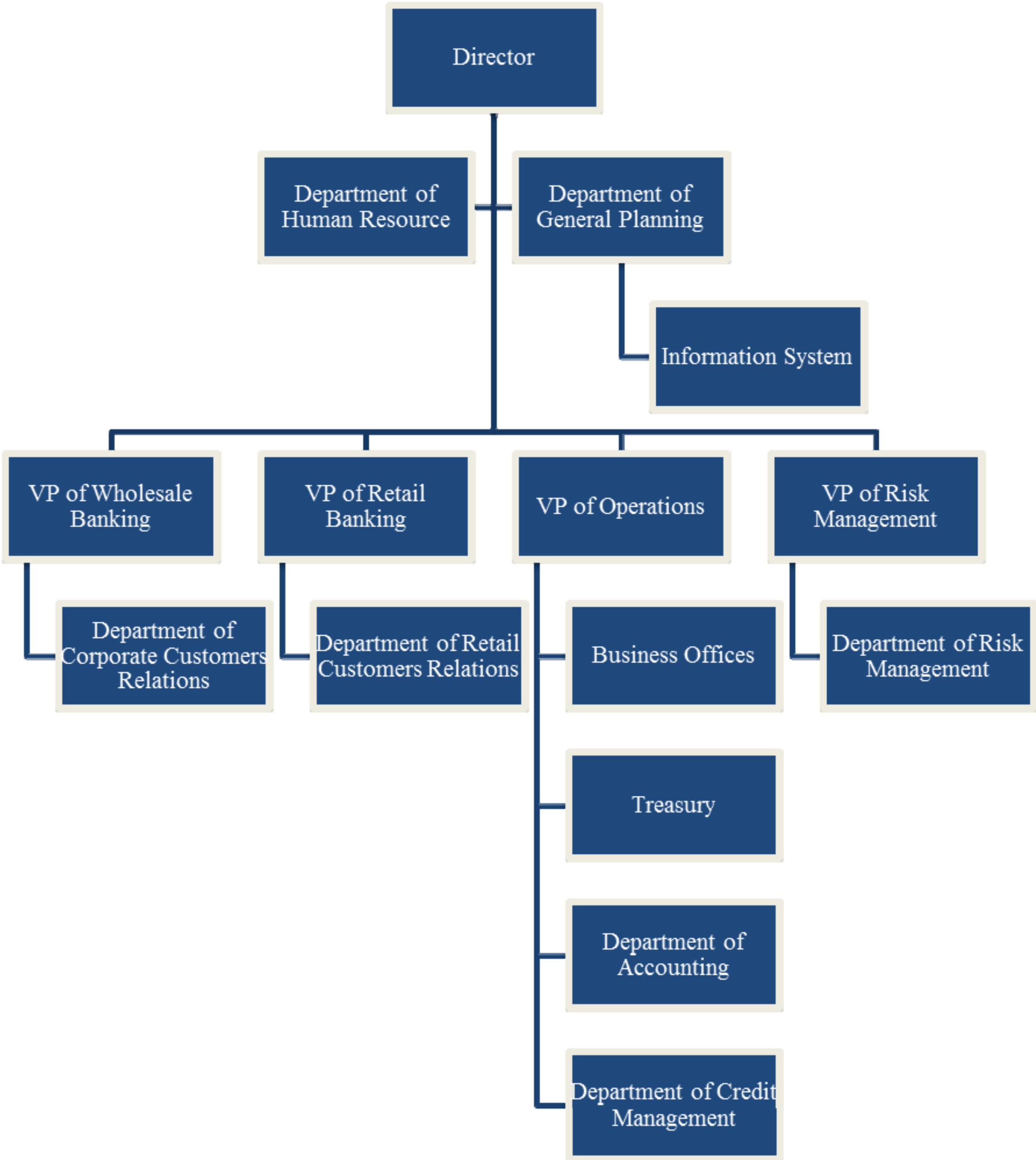
Over the years BIDV QT has built trust and close relationships with many big partners in various industries. Most of the high-profile companies in real estate and construction are BIDV QT's loyal customers. EVN – the biggest state-owned electricity company; VNPT – telecom giant – and Vingroup are all BIDV QT's customers. We also handle cash and provide lines of credit for hundreds of small and medium-sized companies.

For the last few years BIDV QT has consistently placed itself among the top 5 of the biggest branches in BIDV system.

II.1.2. BIDV QT's organization structure

Currently, BIDV QT has 12 specialist departments in headquarters and 7 business offices with a total of 210 employees, 90% of whom hold a bachelor's degree or better.

- **Wholesale banking:**
  - *Department of corporate customers relations*: serves as a focal point of maintain and develop relationships with clients on all aspects of operations. The banking business greatly values trust, therefore a good relationship with customers can sometimes mean the difference between a long-term partnership or no business at all. The department performs general customer evaluation and business analysis, which then will be forwarded to upper management under the form of a report and a proposal.
- **Retail banking:**
  - *Department of retail customers relations*: same as the wholesale department, the retail department builds relationship, albeit with individuals. A large portion of our total deposit comes from the general public. Currently about one fifth of BIDV's total outstanding loans are loans made to individuals. They are an important source of capital and income for any commercial bank. The department also markets and develops specific products for personal use such as personal banking, credit card, debit card, wire transfer, currency exchange, among other things.
- **Supporting departments:**
  - *Department of credit management*: the final step in the credit approval process, this department double-checks for the validity of customers' files, business plans contracts, terms and conditions before cash disbursement. They also archive those files and input them to BIDV QT's database.
  - *Accounting department*: recording banking transactions compliance with accounting principles and regulations, and reporting to BOM, SBV and BIDV headquarter.



<u>Figure 2.0</u>: **BIDV QT's organization**

- *General planning department*: fulfilling synthesize, analysis and business plans development; trading interbank with headquarter, exercising foreign currency with customers; managing and controlling foreign exchange, interest rate to ensure stability in liquidity demand and optimize its fund utilization
- *Information technology department*: managing and maintaining information technology systems related to banking business activities.
- *Risk management department*: testing, monitoring, auditing the compliance with procedures, accounting, foreign exchange, treasury, trade finance, credit, retail service

banking to reduce risk, fraud, error in the key positions as well as activities of the bank.

- *Human resource department*: Recruiting, evaluating, managing and training staff; developing; incentive policies; fulfilling administrative activities of the bank.

II.1.3. BIDV QT's activities from 2010-2013

- **Fund mobilization:**

As of 12/31/2013, the total deposit from customers reached more than 9,277 VND billion, up 12.37% compared to 2012. This is considered as the highest increase since the string of positive deposit growth from 2010 to present. This can be attributed to BIDV's good performance in recent years. The ***table 2.1*** below summarizes the fund mobilization of BIDV QT in the past few years.

Unit: VND Billion

Item	2010	2011	2012	2013	Target	% against 2012	% against targets
Deposits from customers	7,120	7,385	8,256	9,277	9,200	112.37%	100.83%
Total liabilities and equity	7,530	7,740	9,156	10,274	10,200	112.21%	100.73%

(Source: BIDV QT's Financial Statements from 2010 to 2013)

Table 2.1: **Fund mobilization of BIDV QT from 2010 to 2013**

From the start of 2013, the BOD of BIDV drastically assigned the fund mobilization target to all branches and BIDV QT was assigned to reach the target at 9,200 VND billion in fund mobilization in 2013. As of 12/31/2013, this goal has been achieved, exceeding target by 0.83% ***(Figure 2.2)***. BIDV QT's market share has been rising, and total assets reach the highest since 2010.

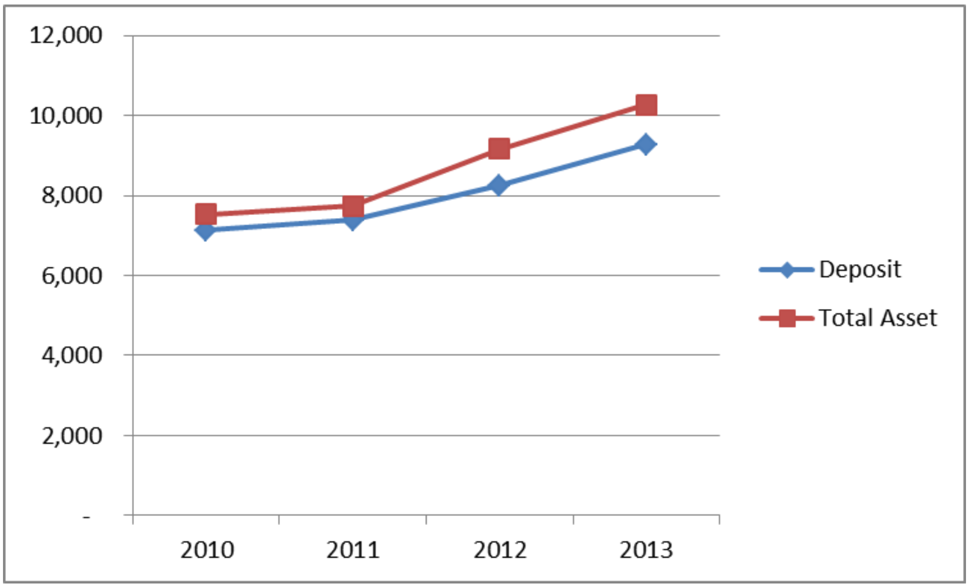


Figure 2.2: **Deposits from customers and Total Asset of BIDV QT 2010-2013**

- **Credit activities:**

From early in 2013, the BOD assigned the target of NPL ratio in the whole system at less than 2%. However, by 09/30/2013, NPL ratio of the whole system was 1.8%, dangerously close to target.

Unit: %

Credit Institution	2011	2012	2013
	NPL rate	**NPL rate**	**NPL rate**
BIDV	**2.57%**	**2.77%**	**1.80%**
Vietinbank	0.75%	1.35%	0.82%
VCB	2.10%	2.25%	3.76%
Agribank	6.00%	5.8%	6.32%
Other Joint stock Banks	0.85%	1.04%	0.62%
Banking system	3.70%	4.08%	3.79%

(Source: Financial Reports)

***Table 2.3*: NPL rate of BIDV against other banks**

From 2011 to 2013, BIDV did not fare the best in terms of NPL management among the largest state-owned banks and other Join stock Banks as a whole. However, by 2013, its NPL rate has dropped well below its level in 2012, showing BIDV's effort in reducing NPL.

Unit: VND Billion

Branch	NPL	NPL rate
BIDV Headquarter	238	3.1%
BIDV Hoan Kiem	201	3.8%
BIDV SGD I	198	2.3%
BIDV South Saigon	205	3.3%
BIDV Tay Ho	142	5.2%
BIDV QT	**239**	**3.6%**
BIDV SGD III	280	3.7%
BIDV Bac Ninh	100	4.0%
BIDV North Hanoi	170	3.2%
BIDV SGD II	245	2.7%

(Source: NPL report in 2013)

***Table 2.4*: 10 branches with highest amount of NPL and NPL ratio as of 12/31/2013**

Throughout the year 2013, BIDV achieved a lower NPL rate than 2012. However, a few branches saw their NPL rate drastically increase. Among those branches, BIDV QT had among the highest amount of NPL, accounting for 3.6% of BIDV's total NPL *(NPL report in BIDV system)*.

- **Financial results:**

As of 12/31/2013, the branch's profit before provision increased to 174 VND billion, while profit after provision was 124 VND billion, up 9.7% compared to 31/12/12. However, in 2013, BIDV QT only set aside 50 VND million for provision and allowance. Details of BIDV QT's financial statements are described in ***Table 2.5***.

Unit: VND Billion

Item	2010	2011	2012	2013
	Amount	Amount	Amount	Amount
Profit before tax before provisions	124	136	153	174
Provisions and allowance for credit risks expense	(5)	(40)	40	50
Profit before tax after provisions	129	176	113	124

(Source: Financial Statements of BIDV QT from 2010 to 2013)

***Table 2.5*: Financial result of BIDV QT from 2010 to 2013**

It can be said that the higher NPL will seriously affect the competitiveness in the banking business. High NPL ratio not only reduces the solvency of banks, decreases efficiency in allocation of asset and liability as well as the liquidity of capital, but also increases the feasible of losing capital as result reducing the profitability of banks, increases level of risk as well as loss of customers' belief for banks. Therefore, managing and reducing NPL ratio can be considered as the most important duties of BIDV QT in this period.

II.2. CURRENT STATUS OF NPL AT BIDV QT 2010-2013

II.2.1. NPL status and loan classification

- **NPL status:**

As of 12/31/2013, total loans of BIDV QT were 6,646 VND billion, up 15.6% compared to 2012. Meanwhile, NPL was 239 VND billion, up 30.0% compared to 2012 and significantly exceeded the goal of 1.80% assigned by the BOD. Detailed figures are provided in ***Table 2.6*** and ***Figure 2.4***.

Unit: VND Billion

Item	2010	2011	2012	2013	+/- against 2012	+/- % against 2012	2013 Target	+/- % against 2013 Target
Loans	3,590	4,329	5,749	6,646	897	115.60%	6,700	99.19%
NPL	54,4	87	184	239	55	130.00%	120	199.17%
NPL rate	1.51%	2.00%	3.20%	3.60%	0.4%	112.50%	1.80%	**200%**

(Source: Financial Statements of BIDV QT from 2010 to 2013)

***Table 2.6*: BIDV QT's NPL from 2010 to 2013**

This high record figure reflected the increase in BIDV QT's market share and its higher liquidity and credit risk. Therefore, the important duty of BIDV QT is to reduce the NPL ratio to get the target. This figure also showed a part of the weakness in the credit risk management, in the quality of disbursement monitoring as well as in the NPL management of BIDV QT.

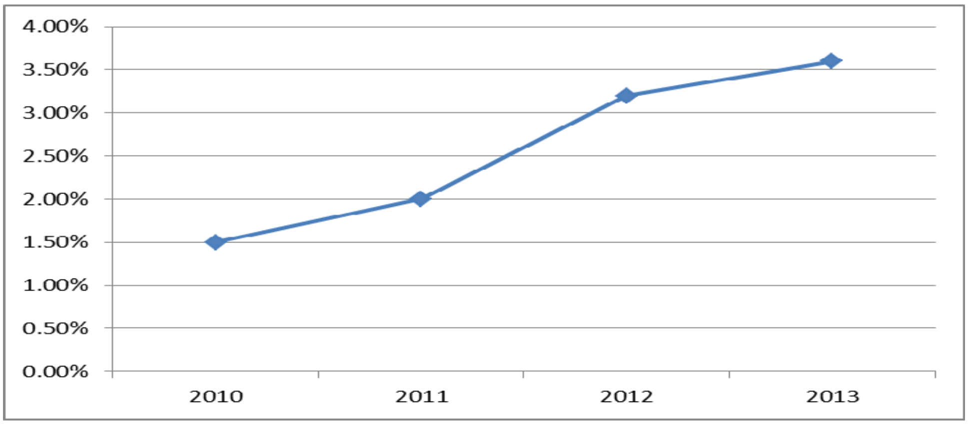


Figure 2.7: **NPL rate curve of BIDV QT from 2010 to 2013**

- **Loan classification:**

BIDV QT implemented loan classification and provisioning risk under Article 6 (for individuals) and Article 7 (for businesses) of Decision No.493/2005/QD-NHNN issued by the SBV since 2006. The internal credit ratings system has been built to ensure a streamlined quality management process from the stage of evaluation, approval to the stage of cash disbursement as well as collateral management. The internal credit rating policy also help the manager control the loan classification, provisioning and use of allowances to handle risk. This set of regulations also helped determine the rights and responsibilities of departments as well as individuals involved in the process. The following ***Table 2.8*** is loan classification results over the years from 2010 to 2013.

Unit: VND Billion

Item	2010		2011		2012		2013	
	Amount	%	Amount	%	Amount	%	Amount	%
Group 1 – Current debt	3,177	88.49%	3,593	83%	4,933	85.80%	5,802	87.30%
Group 2 – Special mentioned debt	359	10%	649	15%	632	11.00%	605	9.10%
Group 3 - Sub-standard debt	30	0.84%	50	1.15%	70	2.28%	140	2.11%
Group 4 – Doubtful debt	20	0.56%	30	0.69%	30	0.72%	79	1.19%
Group 5 – Loss debt	4	0.11%	7	0.16%	6	0.20%	20	0.30%
Total Loans	**3,590**	**100%**	**4,329**	**100%**	**5,749**	**100.00%**	**6,646**	**100.00%**

(Source: Financial Statements of BIDV QT from 2010 to 2013)

Table 2.8: **Loan classification of BIDV QT from 2010 to 2013**

As shown in ***Table 2.8***, in 2011, Group 2 debt reached 15% while NPL accounted for 2% of total loans. In 2012, Group 2 debt decreased to 11% while NPLs reached 3,2% of total loans. As of 12/31/2013, Group 3, 4 and 5 both increased, amounting to the 3.6% NPL rate. Thus, only in four years from 2010 to 12/31/2013, the branch's NPL increased significantly, from 1.51% to 3.6%. With current economic situation which is getting more and more difficult, Group 2's ratio of 9.10% might be a potential risk, which will raise NPL ratio and affect asset quality of the bank when this group change to low credit rating groups.

II.2.2. NPL structure

To better understand the loan structure, as well as the proportion of NPL in each type of loans we further analyzed the types of loan structure in the BIDV QT as below:

- **Loans by time to maturity**

When it comes to time to maturity, loans are divided into three categories: short term, medium term and long term. The data were summarized in ***Table 2.9***. In ***Table 2.9***, from 2010 to 2013, the proportion of short-term loan on total loan of BIDV QT increased, while medium term and long term has a downward trend. Specifically, as of 12/31/2013, short term loans accounted for 46.49% and medium and long term loans accounted for 53.51%.

Unit: VND Billion

Item	2010		2011		2012		2013	
	Amount	%	Amount	%	Amount	%	Amount	%
Short term	1,508	42.01%	1,820	42.04%	2,950	51.31%	3,090	46.49%
Medium to long term	2,082	57.99%	2,509	57.96%	2,799	48.69%	3,556	53.51%
Total	3,590	42.01%	4,329	42.04%	2,950	51.31%	6,646	46.49%

(Source: Financial Statements of BIDV QT from 2010 to 2013)

Table 2.9: **Loan classification by time to maturity of BIDV QT from 2010 to 2013**

However, at that time the interest rates which had maturity from 1 month, 3 months, 6 months or 12 months were the same as 14%. Especially, there was some stress time that the short term interest rate of deposit was higher than the long term interest rate, and the customers tended to deposit in short-term reflecting the illiquidity in banking industry *(Interest rate report of SBV)*. This problem will cause the unbalance in managing assets and liabilities of the bank, increase liquidity gap and liquidity risk, credit risk for BIDV QT.
NPL classified as repayment period is described in the ***Table 2.10***.

Unit: %

Item	2010	2011	2012	12/31/2013
% NPL Short term	47.42%	87.43%	59.20%	68.98%
% NPL Medium term	52.58%	12.57%	7.05%	10.94%
% NPL Long term	0%	0%	33.76%	20.07%

(Source: Financial Statements of BIDV QT from 2010 to 2013)

Table 2.10: **NPL classification by time to maturity of BIDV QT from 2010 to 2013**

As shown in ***Table 2.10***, NPL of BIDV QT from 2010 to 2011 was mainly short and medium term. Since 2012 to 2013, short and medium term NPL fell while long term NPL skyrocketed. As of 12/31/13, BIDV QT's NPL short-term was 68.98%, medium-term was 10.94% and long term was 20.07%. Considering the current economy, the increase in the proportion of long term NPLs reflects a big problem in long term financial capacity. The weakness and inefficiency of cash flow management of the customers, as the result, will affect the credit quality of the bank.

- **Loan classification by business structures:**

When it comes to types of business, loans are divided into five categories of asset such as loans for State owned companies, Limited companies, Joint stock and private companies, Foreign invested enterprises, and for Individuals.

Unit: VND Billion

Item	2010		2011		2012		2013	
	Amount	%	Amount	%	Amount	%	Amount	%
State owned enterprises	215.4	6%	216.45	5%	287.45	5%	265.84	4%
Limited companies	359	10%	519.48	12%	632.39	11%	664.6	10%
Joint stock and private companies	2,405.3	67%	2,943.72	68%	3,794.34	66%	4,585.74	69%
Foreign companies	0	0%	0	0%	0	0%	0	0%
Individuals	610.3	17%	649.35	15%	1034.82	18%	1,129.82	17%
Total Loans	**3,590**	**100%**	**4,329**	**100%**	**5,749**	**100%**	**6,646**	**100%**

(Source: Financial Statements of BIDV QT from 2010 to 2013)

***Table 2.11*: Loan classification by business structure from 2010 to 2013**

As in ***Table 2.11***, in 2013, most loans came from three groups of companies which were limited companies accounting for 10%, Joint stock and private companies accounting for 69%, and Individuals accounting for 17%. State owned enterprises accounted for only 4% while Foreign companies remained at 0%. NPL rate of JSCs was the highest, accounting for 96% of total loans in 2013, followed by Individuals contributing to 2% as described in ***Table 2.12***.

Unit: %

Item	2010	2011	2012	2013
% NPL State owned companies	0.0%	0.0%	2.0%	2.0%
% NPL Limited companies	0.0%	0.0%	0.0%	0.0%
% NPL Joint stock and private companies	99.0%	99.0%	96.3%	96.0%
% NPL Foreign invested enterprises	0.0%	0.0%	0.0%	0.0%
% NPL Individuals	1.0%	1.0%	1.7%	2.0%

(Source: Financial Statements of BIDV QT from 2010 to 2013)

***Table 2.12*: BIDV QT's NPL classification by business structure from 2010 to 2013**

In 2013, NPL for State owned enterprises remained stable, accounting for 2%, while loans for JSCs slightly decreased. This is because State owned enterprises normally have a strong financial backing from the State government, while JSCs have to fight for themselves on the open market. It is in this particular sector that NPLs incur the most.

II.2.3. NPL by industries

2010-2013, outstanding loans and NPLs mostly rest in construction, hotel and restaurant, transportation, and real estate and consulting service. These sectors are strongly affected by the fluctuation of the economy. Details of NPLs for each sector are given in ***Table 2.13***.

Unit: %

Item	2010	2011	2012	2013
Processing and manufacturing	0%	0%	0%	0%
Construction	20%	19%	12%	17%
Trading and service (rice, coffee)	0%	0%	0%	0%
Hotel and restaurant	20%	20%	16%	10%
Transportation	27%	20%	25%	20%
Real estate and consulting service	33%	41%	47%	53%
Community services	0%	0%	0%	0%
Household service	0%	0%	0%	0%
Total	**100%**	**100%**	**100%**	**100%**

(Source: Internal report from 2010 to 12/31/2013)

***Table 2.13*: BIDV QT's NPL classification by industries 2010 to 2013**

Based on data collected from internal credit rating report of BIDV QT and in-depth interviews, I will analyze the macroeconomic risks that affect sectors having high proportion of overdue loans which causes the most difficulties in doing business of the borrowers in BIDV QT. These risks are unfavorable to borrowers in BIDV QT and becoming one of the reasons that cause the NPL to increase, making loans in group 1 and 2 become NPL in the near future.

- **Real Estate and Consulting Service:**
  The economic crisis has caused the demand for real estate (especially high value structures) to significantly decrease. Moreover, the government has issued tight monetary policy and limited credits to non-manufacturing sectors, making it more challenging for investors to pool sufficient capital. As of 12/31/2013, NPL in real estate and consulting service accumulated up to 53%. Potential NPLs from this sector are investments in properties such as Grade A+ properties, 4-5 star hotels and luxury apartments. When real estate market goes down, these segments are the first to be

affected, causing stress on cash flow of investors and making them unable to pay their debts.

- **Construction:**
The capital of construction enterprises primarily derive from the state budget, ODA loans and bank loans. However, the source from the state budget is currently limited due to the government's policy to control inflation; lacking this source, these enterprises will be seriously affected in terms of financial support.
Moreover, these enterprises are likely to use bank loans for improper purposes such as to invest in real estate or other financial instruments. However, they do not analyze and assess the risk of these projects or balance their capital use, resulting in negative cash flow and financial loss.
The enterprises of this sector, especially companies having projects in real estate development, are having big problem as their partners are delaying the payment. As a result, the loans of these companies are more likely to become NPL in the near future.
- **Hotel and restaurant:**
Hotel and restaurant is also another sector severely affected by the economic crisis. The recession has led to the plunge in the consumption and buying power, which means people are now more reluctant to spend on categories other than their basic needs such as hotel and restaurant. Accordingly, the incomes of companies in this industry remarkably drop, bringing about the financial tension in generating profit and paying bank loans. Also, it is foreseen that this situation will continue for at least the next few months, which means the loans of this sector will also be flagged.
- **Transportation:**
Vinaline, one of Vietnam's largest shippers, is BIDV QT's customer. When the financial crisis hit Vietnam in 2010, there was a ripple effect across all industries. The shipping business took a considerable hit when companies could not sell their inventories, thus drastically reducing the demand for large intercontinental ships. This is not only the case with Vinalines but all across Vietnam's shipping industry.

From the above analysis, the author can draw some conclusions for NPL of BIDV QT as below

- NPL ratio was quite high (3.6% by the end 2013) and increased highly, especially in group 4 and group 5 from 2010 to 2013. In addition, loan in group 2 was really high which can easily turn into NPL at anytime, especially in the recession of economic, causing NPL ratio to rise.

- Outstanding loans and NPL in medium-term and long-term tends to increase, which reflects a big problem in long term financial capacity. The weakness and inefficiency of cash flow management of the customers, as the result, will affect the credit quality of BIDV QT.

- Most NPLs come from private and joint stock companies, Individuals, some of which used to be SOEs but recently changed to JSCs in recent years. This situation reflected the limited financial capacity of existing borrowers who have long banking history with BIDV QT.

- Sectors having most NPLs and overdue loans are construction, hotel and restaurant, transportation, real estate and consulting service. The economic crisis has led to a reduced public investment, high inflation and high interest rates, which decrease demand in many industries. As a result, many enterprises were affected and had to face with an even more unfavorable financial situation.

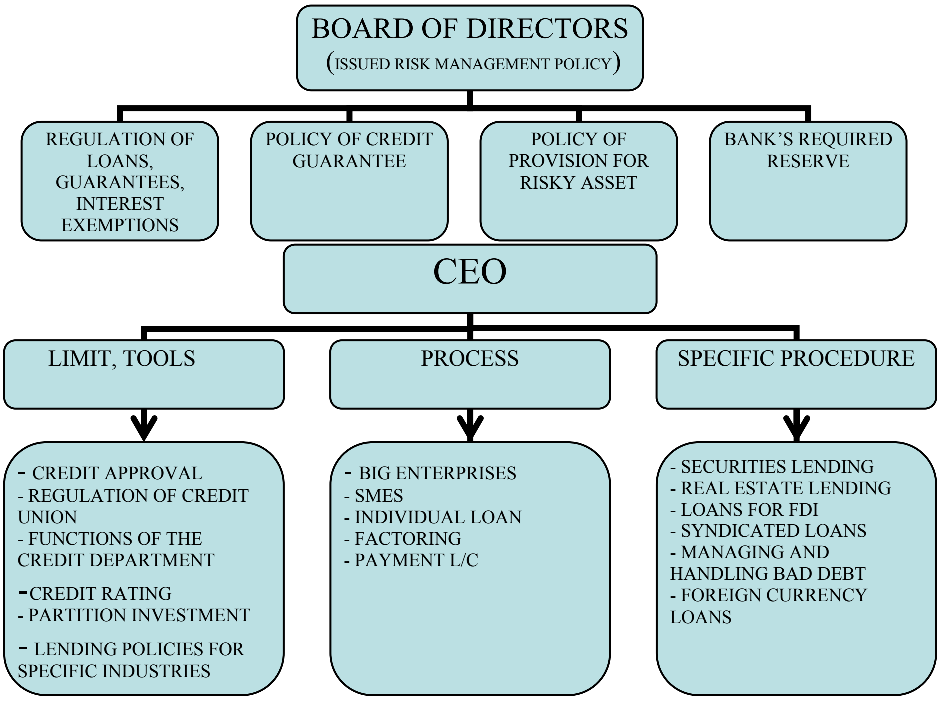
II.3. NPL MANAGEMENT AT BIDV QT DURING 2010 – 2013

II.3.1. Mechanisms for credit management at BIDV QT

- **Regulation of credit activities:**

With the goal of healthy financial status, increasing credit quality, reducing NPL ratio to lowest level, trying to gradually approach the international practice, in recent years, BIDV QT has constantly improve efficiency of credit activities from the stage of granting credit to the stages of inspection and controlling the use of loans, the monitoring process for debt recovery, ensuring the lowest limit of overdue loan, NPL incurred.

To actively control the overdue loan, NPL in recent years, BIDV has developed systems and policies, risk management processes, supporting for the control of increasing in NPL of BIDV. The BOD issued policies regarding lending, guarantee, credit risk management... CEO based on these policies issued the instruments, approved rules, specific procedures for types of loans to the branches in BIDV's system. ***Figure 2.14*** describes the system of documents related to credit activities at BIDV and BIDV QT.



(Source: BIDV's internal policy)

***Figure 2.14*: System of documents governing credit activities at BIDV**

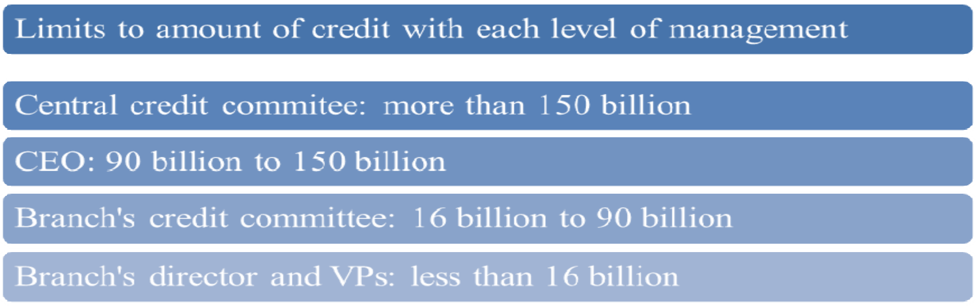
From ***figure 2.14***, the CEO issues credit policies, which outlined the processes for each economic sector based on the business environment and industries' specifics. BIDV QT has complied with the all regulations promulgated by BIDV headquarter. Specifically as follows:

- **The credit approval process at BIDV QT**:

The central credit committee determines the maximum line of credit for one customer. The composition of this committee is generally decided by the CEO himself. At BIDV QT, the

Director appoints the branch's credit council and also takes a role as the chairman of this council.

At BIDV we use a hierarchical system of decision-making whereby each level from branch's deputy director to the Central credit committee (top managers only) have a certain "range" they can work on without having to consult upper levels. This is done to empower lower level managers and also to reduce the burden of bureaucracy. ***Figure 2.15*** elaborates further on this matter. Please note that these figures may vary depending on each client's creditworthiness and depending on the macroeconomic environment.



(Internal credit policy of BIDV)

***Figure 2.15*: Credit authorization at BIDV**

From ***figure 2.15***, the deputy director at BIDV QT can approve a line of credit less than 16 billion VND. When the customers are eligible for more than that amount, the council of credit at BIDV QT will have a meeting for the approval this loan. If the line of credit exceeds 90 billion VND, BIDV QT must forward all required documents to the risk management department at BIDV headquarter for approval. Since 2012, as NPLs at BIDV QT significantly increased, the CEO decided to reduce the maximum amount of credit BIDV QT can grant from 120 billion to 90 billion. This limit can be altered in the future as NPL rate is reduced.

- **Credit granting process at BIDV QT**:

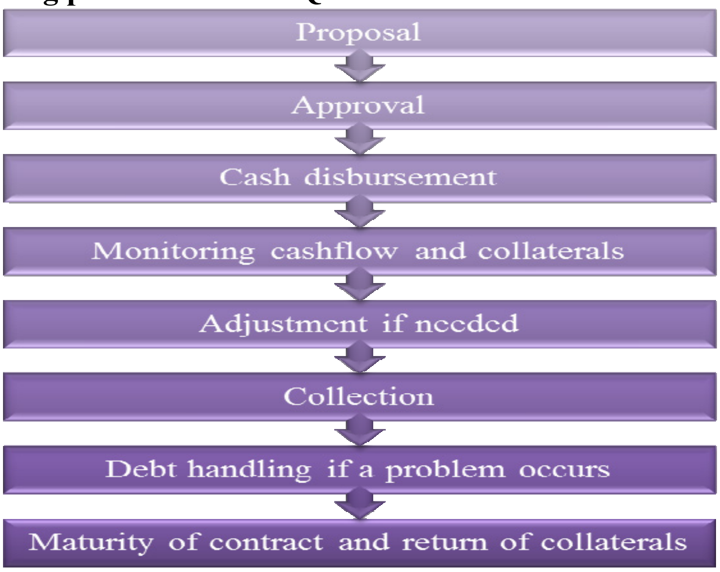


***Figure 2.16*: Credit granting process at BIDV QT**

Credit granting process was developed in compliance with current regulations by the SBV and the relevant government agencies.

Proposal: credit officers (known as customer relations officer) gather all relevant paperwork from customers, using those documents as inputs for further analysis. The customers are wholly responsible before the law for the accuracy of such documents. However, checking for the accuracy of customers' documents is the credit officer's responsibility. Information is fed to BIDV's internal credit rating system, analyzed further by the credit officer himself, who will determine whether or not credit can be granted. If the customer is eligible, the credit officer will write a report and a proposal. Higher-level managers will determine if credit should be granted based on the report and their own subjective opinions.

Approval: after the credit officer finishes evaluating the customer's needs and financial plan, the relevant department conducts risk assessment for the loan in question. At BIDV QT if the loan is sizeable beyond a predetermined amount it has to pass a thorough risk assessment. Based on the proposal and the risk assessment report, the director decides whether the loan will be granted. All legal proceedings after this step are standardized and required by law. Signed documents are carefully grouped and archived as well as input into BIDV QT's database.

Monitoring cash flow: after a full or partial cash disbursement (for lines of credit and project loans), on a periodical basis, the credit officer is responsible for updating relevant information regarding:

- How the customers are using the provided fund ;
- Whether there is any disruption in the customer's cash inflow
- Whether there is any change in the customer's financial plan.

Should the credit officer find any abnormalities regarding the above items, he/she must contact the customers about the problem and report to upper managers in order to devise necessary changes in the loan's terms and conditions.

Monitoring collaterals: for collaterals (including third party assets used as collateral) which are machinery, equipment, buildings, etc…, the credit officer must physically inspect for damages, loss, changes of ownership on a regular basis. In the case of a guarantee contract involving a third party, he/she also has to monitor the financial strength of the guarantor as far as the obligations are concerned.

Adjustment: based on the customers' particular needs and financial positions, the credit terms and conditions may be adjusted.

Collection: customers are notified of the loan's due date at least 10 days prior. If the customers are unable to pay off in time, on a case-by-case basis, the credit officer recommends appropriate measures to his/her superiors.

Debt handling: When a loan becomes overdue, credit monitoring department immediately informs the credit officer to contact the customers to sort things out. Such loans (which are now NPLs) are closely monitored, the customers' credit-worthiness is demoted, additional interests and fees are likely to incur, along with a host of other changes to the loan's terms and conditions. Above all, however, all involved parties must work together to make sure that the overdue loan is paid off as soon as possible.

End of contract: After the loan is paid off in full, the bank releases the hold on assets and returns them to the customers.

The above process has been largely standardized at BIDV QT. The regulations are devised so as to remove as much confusion and ambiguity as possible. Using this streamlined process, BIDV QT is able to grow rapidly despite not having a sizeable workforce.

- **Evaluating customers:**

The internal credit ratings system help BIDV QT assess credit more efficiently while maintaining relatively good control of the credit portfolio. This system takes into consideration even external factors such as economic conditions, regulatory changes and incorporates both financial and non-financial criteria when rating a customer. Around the world banks are constantly in the quest for a more sophisticated system that can essentially act as the eye in the sky for every one of its loans. In the future BIDV needs to further improve its system so as human errors are minimized while the role of objective judgment from staff is not undermined.

- **Customer policies in credit operations:**

BIDV QT qualifies or disqualifies customers using the following criteria:

- Customers must be individuals/organizations eligible for financial transactions. Eligibility is determined by relevant government's regulations.
- Customers must prove their ability to pay off the loans.
- Collaterals must be able to be traded, their ownership status must be unambiguous.
- Duration of the loans must be appropriate with each respective financial product.

Strategic customers with strong financial backings according to BIDV's internal credit rating system will be considered preferred customers who enjoy "special" treatments including, but not limited to, more lenient conditions for granting credit, lower interest and fees, tailored products and services, etc…

- **Policies for collaterals:**

BIDV QT reserves the right to fully decide whether or not it grants credit to customers. The vast majority of loans are secured loans with BIDV putting a hold on collaterals. The conditions for an asset to be used as collaterals are numerous. The most important principles are:

- Collaterals must be under the lawful ownership of the borrowers or a third party involved in the process and;
- Collaterals can be sold/traded with relative ease.

- **Supervision and inspection system at BIDV QT:**

The department of risk management was established at BIDV QT for the purpose of monitoring all internal operations of the bank to assess compliance with policies and procedures and regulations. In theory such operations can be effective in detecting and handling violations. In addition, all staff at management level is also responsible for monitoring and inspection operations within the banking organization.

- **The credit information collection system:**

Currently at BIDV QT, the collection of credit information was performed by client department. The credit officers proactively access customers and deploy, find down necessary information for credit activities and monitor as well as manage the detail, accurate and confidential of this information. Credit information Systems at BIDV QT collected by different credit officers, from various sources. Besides self-collected information, the credit officers were only supported by the central credit information of state banks. This limitation of lacking information had made difficult and less exact for the evaluation and classification credit customers of BIDV QT.

II.3.2. The process of managing and handling NPL at BIDV QT

II.3.2.1. Establishment of loan handling at BIDV QT

In 05/2012, by order of Mr. Le Quang Thanh, director of BIDV QT, a group consist of the director himself, one deputy director and two specialists was to be put in charge of handling bad debts. The handling loan group proactively identifies the right risky loan. The risky loans for customer are one of the characteristics, as followings:

- It was the NPL which was classified under the result of classification and provisions of the BIDV and state banks regulations in each period.
- Loans which had been handled by the provision reserve cannot collect and currently recording in off balance sheet.
- The loan of customers which have not yet been classified as NPL have some signs of risky, as followings:

  - The production of customer's business interrupted, ceased (due to loss of customers, products lose their competitiveness, strikes, continuous losses, the business sector at risk ...)
  - The project of customers face with the difficulty problem as delayed or terminated deployment.
  - Customers use the loan in the wrong purposes which lead unbalance financial status (using short-term capital for long-term investment).
  - Customers are not willing to cooperate (not providing timely reports as required, acts of shirking or hiding information, unwillingness to take all sources of cash flow to pay debt).
  - Customer or the legal representative person, sued, may affect their ability to repay loans.
  - Customers have NPL in other credit institutions.

On the basis of risk assessment for each client, BIDV QT actively applies some remedial measures to collect NPL, as follows:

- (a): Special monitoring. Branches inspected the operations of borrowers frequently, and required the borrowers report their financial statement regularly to grasp the situation.
- (b): Continue to grant credit with stricter conditions such as increase collateral, change the ways to grant credit, or increased controlling the loans.
- (c): Collecting outstanding loans in a gradual manner.
- (d): Requires additional collateral to ensure higher safety for the loans.

- (e): Stop granting credit.
- (f): Reduce interests.
- (g): Restructure
- (h): Require the guarantor to perform the obligation in place of the borrowers
- (i): Sell the collaterals
- (j): Sell the loans
- (k): Request additional collaterals from third parties
- (l): Sue the borrowers
- (m): Other measures permitted by law.

Depending on the level and nature of the NPL, BIDV QT may propose to transfer these loans to the handling loan department of BIDV headquarter. The transferring documents must clearly stating the situation of consumers, content of debt, the measures already taken to handle the loans and the difficulties arising in handling loans and proposing further direction to handle these loans.

The handling loan department of BIDV headquarter is responsible for managing NPL portfolio, monitoring the implementation BIDV QT in making collection of NPL plan and advising for the manager of BIDV QT the new method or process to collect NPL.

The establishment of the handling loan group of BIDV QT showed the determination in handling NPL of the branch. BIDV QT considered that handling NPL is the first key tasks in the business of banking, reform in the way of thinking and doing of the manager of the branches, raise awareness and responsibilities of individuals as well as groups in handling NPL, improving the efficiency of handling NPL at BIDV QT.

II.3.2.2. Risk handling process at BIDV QT

BIDV QT can take any of the above steps to recover the loan. After that, a report will be forwarded to BIDV Headquarters. When all measures have failed except for using the provision to handle the debt, BIDV QT must submit detailed documents to BIDV Headquarter for further instructions. Firstly, the documents of risk handling must have sufficient grounds to prove eligibility to use the above mentioned measures. The submitted documents to the risk management department at BIDV Headquarter must include: the proposal, the minutes of meetings of the credit council clearly showing BIDV QT's solutions to each NPL incurred, the loan contract, the loan collateral reports and other documents related to the disbursement and collection the loans.
Risk handling process of BIDV QT includes three steps:

- Step 1: Credit officers are responsible for background check, research, and analysis in order to propose a list of loans which are eligible to use provision reserve to handle as well as propose the process measures and prepare a proposal submitting to Head quarter.
- Step 2: Managers of the respective department of customer relations review the credit officer's report to before forwarding to the director.
- Step 3: The risk handling council of branch reviewed the short list of loans eligible to be handled by the risk handling committee of BIDV headquarter.

In all cases, the branch shall be fully responsible for the correctness and accuracy of data and records of proposal loans.
After receiving a written acceptance from the risk handling committee of BIDV headquarter, BIDV QT uses specific provision reserve to process credit losses for loans which are no longer to recover. BIDV QT also conducts urgent sale of collateral which are suitable with the agreement between BIDV QT and the borrowers as well as compliance with law and regulations. If the proceeds from the sale of security assets do not offset the credit risk of loans, BIDV QT uses general provision reserve to handle. At that time, BIDV QT shall transfer the debts which have been using provision reserves to handle risk from recording in balance sheet account to record in off balance sheet account and continue to monitor the implementation of schemes for debt recovery.
Before the 15/11 annually, the credit officers make a report to assess the performance of debt handling and the reasons why said NPL has not been paid in the current fiscal year. This also includes a plan by which NPL can be recovered in for the next fiscal years.
For loans deemed unrecoverable, BIDV QT has completed the documents proving that they are in fact unrecoverable and propose to write off these loans out of the balance sheet.
For specific regulations on the steps of risk handling process of BIDV QT as well as the consistent documents and regulations of risk handling in the whole system, the treatments of NPL by using provision reserve were really methodical, scientific, easy to manage as well as control, high initiative created for the branch when the proposed list of bad loans to be treated, to ensure the prescribed by law as well as guidance of BIDV. Thereby, the operation efficiency in processing NPL of BIDV QT also increased, meeting the management needs and requirements of the business of banking.

II.3.3. The application of the measures

Based on the results of periodic loan classification, BIDV QT conducted the review, plans for treatment, recovery of NPL by specific measures. According to the ***Table 2.17***, the measure of special monitoring loans (measure a) and measure of continue to grant credit with sticker conditions (measure b) is the top priority.

Unit: VND million

Measures	2011	2012	2013	Average	%
a	30,501	127,357	161,898	106,585	62.70%
b	25,130	45,084	56,201	42,138	24.79%
c	16,851	0	0	5,617	3.30%
d	0	0	0	0	0.00%
e	1,311	1,336	407	1,018	0.60%
f	828	0	1,673	834	0.49%
g	0	0	0	0	0.00%
h	3,449	9,344	8,646	7,146	4.20%
i	1,856	0	4,652	2,169	1.28%
j	5,088	879	0	1,989	1.17%
k	0	0	0	0	0.00%
l	280	0	702	327	0.19%
m	1,705	0	4,821	2,176	1.28%
Total	**87,000**	**184,000**	**239,000**	**170,000**	**100%**

(Source: Financial Statements of BIDV QT from 2010 to 2013)

***Table 2.17*: Proportion in using handling measures of BIDV QT from 2011 to 2013**

Figure 2.18 shows that measure (a) was used most for collecting NPL of BIDV QT with the rate up to 58.8%, the measure (b) used rather as accounted for 25.4%.

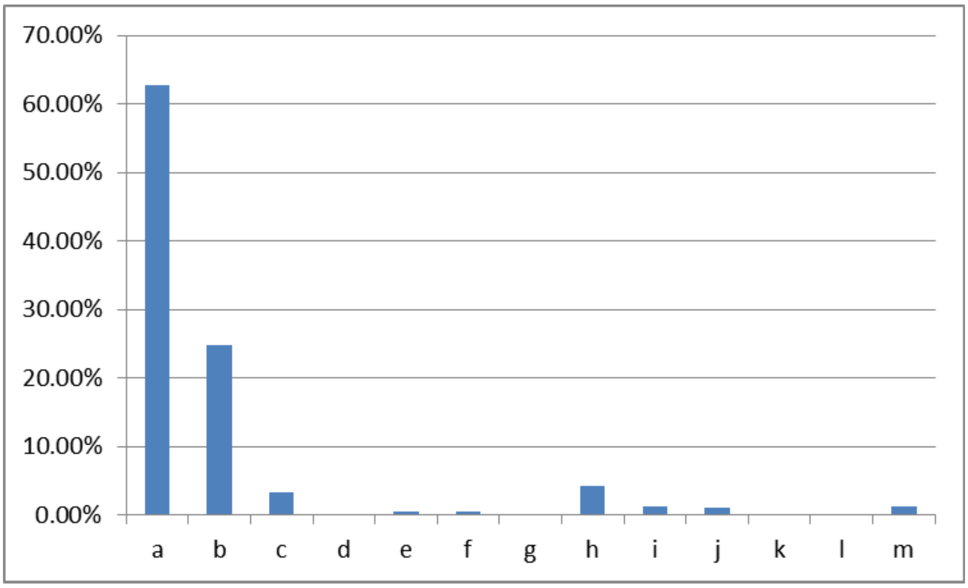


***Figure 2.18*: Proportion in using handling measures of BIDV QT from 2011 to 2013**

Credit officers and client manager at BIDV QT inspected loans more frequently, required the borrowers regularly report their production and business situation in the period, actively reviewed, analyzed and evaluated actual operations of the borrowers (revenue, inventory, accounts receivable...). Credit officers also closely monitor the cash flows of business of borrowers (especially with borrowers opened accounts at the bank) to promptly collect loans. BIDV QT also required additional collateral for the loans from the borrowers to increase security for the bank.

It can be seen that BIDV QT focuses on the application of two methods to handling almost NPL, especially in difficult economic conditions. The borrowers with weak financial capacity cannot afford to pay the loan even though they were closely monitored by the bank. In very bad cases where the collateral has to be sold as a last resort, the result is not pretty. It is not always easy to sell a borrower's assets because of many factors the bank has no control over, most prominently legal problems. The measure of suing the borrowers accounted for only 0.19%.

Other measures such as stop granting credit, interest reduction, selling of debts were also used but with not nearly enough. The measures of handling NPL were not applied diversification which may be one reason why the NPL ratio in current years increases.

II.4 THE REASONS FOR THE INCREASE OF NPL DURING 2010-2013

According to the above analysis and the result of in-depth interview, the reason causing increase of NPL at BIDV QT can classify in three parts:

II.4.1. The reasons from macroeconomic environment

i. ***Global economy.***

By the end of 2013 the developed world has largely gotten out of the recession starting in 2008 and once again in 2012. However, the ripple effect is still felt in the developing world as export, transportation and construction have not fully recovered. The capital market of Vietnam is still in shambles, due in part to the lack of a cash inflow. Large amount of unsold inventory also drives down the price of such assets, further complicating the problems between banks and borrowers, because oftentimes inventory is used as collateral.

ii. High inflation

High inflation makes the input price of electricity, fuel, coal, and minerals increases. The inflation rate of Vietnam in 2011 is 18.13%, this is the second highest rate of inflation in Vietnam over the past 20 years. By the end of 2013 this number has come down to roughly 6%, which is a miracle in itself. But Vietnam is far from stabilizing its price index.

iii. Real estate market downturn

Real estate market downturn has caused serious impact on many related sectors such as steel, cement, and construction, as result creating huge inventories in these sectors. In 2012, inventory of processing industry increased by 23% over the same period of last year, especially some sectors had high increasing rate of inventory such as steel up 32%, cement up 64%, plastic products up 55%, and fertilizer up 56% *(economic report 2012).* This matter forces the market price of these products to go down. Outstanding loans in these sectors of BIDV QT accounted approximate 70% (17% in construction and 53% in real estate) therefore it was much more prone to negative effects from the real estate market.

iv. Tight monetary policy investment

The years 2011 and 2012 saw the government pursuing a low money supply and high interest rate, which at some point reached a record 20%. This is followed by a market collapse which drove interest rate to just 10% in a year, effectively putting a huge strain on borrowers who had to borrow at the peak rate.

II.4.2. The reasons from the borrowers

i. Borrowers have weak financial capacity and are highly dependent on bank capital.

The top 10 borrowers at BIDV QT have an outstanding loan of around 4,300 billion VND, accounting for almost 65% of the branch's outstanding loan. Most of those 10 companies are in the real estate business, which suffered heavily from the market collapse at the end of 2012. Those customers are BIDV QT's long-time partners, so handling NPL for them is a delicate matter at BIDV QT, requiring not only a competent workforce but also enough flexibility to ensure both parties' survival.

ii. Corporate managers lacking both competency and experience

Many otherwise financially sound companies are plagued by poor decision-making. As the Vietnam's economy arguably grows faster than its people can adapt, many top managers struggle to understand new technologies, or to plan a sustainable business strategy. They stick with what did well in the past instead of scrutinizing into details such as cash flow, revenue and risks. Many businesses have gone out this way: top managers overshoot their revenue estimate, borrow way too much for their cash inflow, then become insolvent.

iii. Borrowers invested in too many projects for their financial capacity.

When a business funds its investment in an area it has no expertise in with operating cash flow or borrowed money, it is taking a substantial risk. But when it does so in several industries outside of its own, that is when disaster happens. By 2010, many companies from industries such as manufacturing, exporting, petroleum, and telecommunication poured money into real estate, banking and the stock market using borrowed money. This move greatly inflates those markets, causing the bubble to burst shortly after.

iv. Information provided by borrowers is inaccurate.

Some the financial statements of borrowers are not audited by an independent auditor or the tax authority.

v. Difficulty in selling collaterals

Assets used as to collaterals for the obligations of the borrowers account for roughly 70% of total outstanding loans. It is therefore unlikely that in the event of a default, the bank can fully recover the loan. Furthermore, some loans are secured by machinery, equipment, production lines which are purposely built. Although they are highly valuable to the right party, they are difficult to liquidate. Some loans are mortgages, which, under the Vietnamese property law, cannot be considered the borrowers' property until it has been amortized. Because the borrowers do not technically own the assets, they cannot be registered as collateral. In many cases, a certain building has been operating for years yet the owners cannot register it because he has not paid off his debts.

II.4.3. The reasons from the bank

i. The process of evaluation and approval of credit

- Credit officers have not focused on risk assessment for the group of related companies or the transfer funds between related companies, as result not accurately calculate their own capital needs and working capital cycle, leading inaccurate in approving credit limit for customers. *"Credit officers usually evaluate the effectiveness of the project, and not assess the operations and cash flow in all activities of the company. The projects which are evaluated might be truly good, but the difficulties which come from other activities will affect the repayment capacity of customers*" said Mr. Duong Viet Phuong, corporate customer manager. This can be seen the weakness in evaluation process of client officer at BIDV QT.
- Credit officers have not analyzed the crisis situations in lending decisions, especially in granting credit for long-term projects. In the period of 2005 - 2008, BIDV QT had provided credit to many investment projects in the field of maritime transport, real estate, cement, steel... But at that time, the evaluation only assessed the performance of the projects in normal economic conditions, steady growth without assessing the impact of the crisis-economic factors (including the crisis in the economic cycle) to the ability to pay debts of borrowers.
- Credit officers do not thoroughly evaluate the financial capacity of the borrowers in lending projects. There are many unfinished projects due to lack of capital, forcing the bank increase the lending rate to complete the project or customers borrow other banks, or use short-term capital to invest in long-term projects. This situation will reduce efficiency, increase risk compared with an initial evaluation plan. The credit

officers may also not pay attention to the demand of working capital especially for projects with large capital needs, such as steel, cement, leading to stagnation of production, which affects the efficiency and capacity to repay loan of the borrowers. From talking with Ms. Tong Thi Kieu Oanh, credit officer who manages MERFRIMEX, the author found that, MERFRIMEX had been too ambitious with their project. Borrowing heavily from the bank even before finding a big enough customer base, the company is in deep trouble now that they are unable to borrow anymore, yet their project lacks capital to even take shape and being able to generate revenue. However, when she analyzed before granting credit to the company, she did not carefully evaluate the potential development of these projects and put too much trust in the borrower's risky investments.

ii. The operation, disbursement, management after granting the loan

- The management after granting the loan is not good. The staff do not closely monitor the situation of production and business activities of enterprises in order to detect early signs of risk to have early treatment measures minimize losses. "*Credit officers have not evaluated thoroughly the quality of customer's assets such as receivables, inventory, uncompleted assets, financial investments which have high potential of risk in case the value of customer's asset reduce against market value*", said Ms. Pham Thi Bich Diep, internal auditor. She also pointed that "*the credit officers have not carefully evaluated the credibility factor, the capacity of owner, or the company's leadership. Therefore, there are some cases that the credit officers were provided by inaccurate reports, data and documents, or the borrowers not cooperate in the process of debt recovery*".
- The bank does not properly evaluate the situation of the customer who borrows money from many banks at the same time. The bank has not closely tracked, collected and evaluated sufficient information about the business activities of other projects which were implemented by using other loans not borrowing at BIDV QT. This problem leaded the customers use the loans which borrowed in one bank to pay for other debt in other banks or used for other purposes, or borrowed exceed their capacity to invest in various projects, leading to inefficiency of the business. There are many cases which the borrowers used cash receivable of BIDV QT lending projects to offset the shortage of liquidity for other investment activities without paying the due loans of BIDV QT. *"Working capital requirement of Trung Nam Land in 2010 was 100 billion VND. The company borrows money in five banks and one financial leasing company with total outstanding loan of 150 VND billion. They used the loans which borrowed at BIDV QT to deposit in another bank to benefit from the difference",* said Ms. Nguyen Thi Khanh Ly, deputy manager of the department of corporate customers relations.
- The bank did not regularly update information about market volatility of the commodity. From talking to Mr. Nguyen Duy Anh, credit officer, he said that *"I usually collect the information of the borrower before granting credit. During and after granting, I only collect invoices, contract, other related documents and sometimes update information of the market if there was affected serious to customers". This matter* made them not timely identify risks in the market which can affect borrowers' business, and cannot warn potential risks and consult customers suitable way to reduce losses. BIDV QT also had less periodically reviewed the credit

of investment projects, leading not timely detect the lack of capital, the increasing of the total investment, delayed risks, market volatility, the implementation of credit conventions, or shortages of working capital, which affect the financial performance as well as the borrowers' ability to repay debts.

iii. ***Personnel problems***

- BIDV QT did not controlled and clearly defined responsibilities in the management, prevention and detection of risks and treatment of NPL – especially the risk management department. BIDV QT has not issued regulation to clearly define the obligations and responsibilities as well as sanctions for violation of each staff that makes NPL happen or increase. As of now, most of the responsibility once NPL incurs lies on the customer relations department. Because of the absence of sanctions, the credit officers should not really be responsible for reducing risk and treatment of bad debts in credit activities.
- In addition, there are no separation of functions for credit officers (focused on marketing, customer contact, creation of credit). This limitation reduces the objectivity and accuracy in evaluating the borrowers of BIDV QT, increasing credit risk for the bank.
- The debt handling department is still primitive and is usually tasked with large NPLs. Individuals and small businesses' NPLs are still handled by the credit officers.

iv. ***The application of measures to handle NPL at BIDV QT has not really varied, making the result of recover bad debt low.***

- The main measures to handle NPL are now using as a special monitoring NPL and continue to grant credit with sticker conditions and declining the outstanding loans. Other measures such as requires the guarantor to perform the obligation for the borrowers, stopped granting credit, exemption or reduction of interest to increase the collection of loans, sale of security assets, sale of debt or sue the customer ratio were used with lower ratio against with other handling measures used.
- Other measures such as requires additional collateral to ensure higher safety for the loans as of low percentage of collaterals used to guarantee for the loans, or assign the representative staff of the bank to participate in the management of the operation of the borrowers have not applied yet.

CONCLUSION OF CHAPTER 2

On the basis of the content in Chapter 1, this chapter has analyzed and assessed of the current status of NPL in the credit activities of BIDV QT, and pointed out some reasons causing the increase in NPL of BIDV QT. Analysis of actual situation of management NPL at BIDV QT, the author finds that the main reasons which are causing the increasing NPL of BIDV QT are the weaknesses in evaluation from before granting to during, after granting and collecting loans, especially for the borrower who has NPL at BIDV QT with difficult financial capacity. Therefore, the solutions to improve management NPL are considered the key matters to reduce NPL rate at BIDV QT in the next years.

CHAPTER III: RECOMMENDATION TO IMPROVE THE MANAGEMENT OF NPL AT BIDV QT

III.1. MANAGEMENT'S PROSPECT ON THE FUTURE OF BIDV QT

III.1.1. The objective of BIDV QT in coming years

Taking advantage of technology, brand reputation, BIDV has strived to become a leading bank Vietnam and the Southeastern Asia area. BIDV QT focuses on developing modern banking products, expanding operational network, applying flexible interest policy, developing financial derivatives such as swaps and options. Besides, BIDV QT also shifts to retail services sector, invests and develops e-banking services activities.

BIDV QT should also devise customer policies that catch up with modern trends and practices in the industry, define market segments to provide the appropriate products for the right customers. BIDV QT also gradually develops the brand and culture to further develop their prestige, image and brand name to its customers.

The major goal in the period 2013-2017:

- The average growth rate of total assets is 15-20% per year
- The average credit growth rate is 15-20% per year
- The average growth rate of capital mobilization is 15-20% per year
- Profit after tax increases 20-25% year-on-year
- The ratio of NPL does not exceed 2.2%

III.1.2. The future of managing NPL at BIDV QT

BIDV QT needs to further strengthen the control and management of credit growth, credit quality, NPL, and strives to make enough provision reserve of credit risk in compliance with the regulations of BIDV Headquarter and the SBV.

BIDV QT will restructure customer portfolio following the direction of reducing the number of customers with low rating focusing on potential customers with a stronger financial background. The bank also reviews and monitors the borrowers whose loans belong to group 2 to find the right solutions in time and avoid this group moving into group 3.

In the process of handling NPL of the borrowers, BIDV QT assesses, analyzes the customers' operation as well as their ability and attitude find out the suitable measures for each of them, following these guidelines:

- If the customer is willing to pay from positive the positive cash flow from their business and have feasible plan for repayment, BIDV QT will restructure schedule of payments.
- BIDV QT actively collaborates with customer for selling collaterals in case the customers are willing but unable to pay.
- BIDV QT proactively use measures such as selling debts, interest exemptions complied with regulations, conventions of BIDV Headquarter and BIDV QT to make the handling process quickly and efficiently
- BIDV QT reserves the right to sue customers if they are unwilling to repay the loans.

III. 2. RECOMMENDATION TO IMPROVE THE MANAGEMENT OF NPL AT BIDV QT

III.2.1. Building orientation for credit operations

i. Changing the approach of credit evaluation: assessment should be approached on the macroeconomic level, the whole portfolio level (by sector, a customer group, or the overall of a customer) and the specific transaction levels to limit the investments focusing on high risky sectors, or mainly granting big amount for a customer, customer group.

ii. Building credit portfolio structure (structure for the industry, term structure, the sector and the region) to set up risk-reducing measures. The more diverse a bank's portfolio is, the lower the default risk.

iii. For loans that are likely to turn into NPL, the bank need to actively review and propose financial restructuring options before the loans are overdue.

III.2.2. Enhance the quality of credit evaluation before granting credit, inspection during and after granting the loan.

i. BIDV QT needs enhance the quality of credit evaluation, select customers before granting credit in areas such as assess risks in group of companies related to each other to determine the exact needs of customers and assess the weakness or strength of working capital, receivables, inventory, technology, ability to manage the enterprises as well as the ethics of the leader.

ii. The credit officers need to prepare reports and business plans for clients to define develop or eliminate customers and orientate measures to reduce risk, and set up interest policy consistent with the nature of risk

iii. The credit officers need to focus periodically on checking during and after granting credit in order to detect early signs of risk to minimize the damage to the bank. They also focus on making notebooks to collect and assess information from customers periodic monthly, quarterly in followings matters:

   - Monitoring and managing the forming of asset correspond with granting loans, cash flow of the projects.
   - Assessing customer's loans at other banks.
   - Assessing the quality of inventory, accounts receivable, payable.
   - Monitoring the flow of money, debts, cash flow in the group of relevant customers.
   - Monitoring of collateral formed from the loan, set up management process for inventory rotation.
   - Monitoring, collecting and evaluating information about other projects which are being implemented by the clients
   - Regularly updating information on market fluctuations, industry and business environment of customers
   - Regularly to review and analyze financial statements of borrowers to evaluate the current status of operation of borrowers.

- Regularly actually visit customers: To have a clear picture on the production and business activities of customers. In addition to analyze the financial statements of clients, credit officers need to regularly actually visit customers, which could determine the existence, difficult, the actual status of the customer (the situation of buildings, machinery, equipment, collateral as well as capture the situation production and business customers). Moreover, the trips can also help banks verify the quality and accuracy of financial reports as well as the using loans of the borrowers.

iv. Credit officers must periodically report the result of monitoring and analyzing the risk as well as problem of investment projects to propose overall solutions.

v. Credit officers must also fulfill the conditions of approval and recommendations from BIDV headquarter in order to minimize risks.

vi. Credit officers must also periodically review credit limits for customers, especially the borrowers who are unable to pay loans. In case the customer does not provide financial statements, information on production and business activities, reducing the cooperation in doing business, the credit officers should reduce outstanding loan to explore, collect and evaluate additional information from the borrower.

III.2.3. Improving the structure of credit operations and credit risk management

- Starting from practical demands of credit activities as well as recommendations by the Basel Committee, the departments of customer relations, risk management and risk handling departments must be separated in both operations and authority. Credit risk management should always be independent, while the customer relations department must not participate in credit approval.

- The construction of the line of credit which is based on determining the overall risk (through the implementation of credit rating, industry analysis, the ability to develop customers in the future...) will be made by the credit risk management department which carried out independently to ensure separation of functions. The customer relations department will be responsible for all of the inputs from customers, providing information to the credit risk management division as well as monitoring and inspecting compliance with the loan contract. The separation between the credit marketing division and credit risk management division helps with objectivity and ultimately, safety. Credit risk management division will at the same time cross-check with the customer to detect signs of risks. Credit risk management therefore is a continuous process, from the moment the loan is proposed until it matures.

III.2.4. Devising a reward and discipline system for individuals and groups

BIDV QT has not issued specific regulations on liability and sanctions against individuals and groups causing NPL beyond a certain limit. In many cases, credit officers proposed shady projects with questionable feasibility, subsequently causing a spike in NPL and simply walk away without punishment. Therefore, BIDV QT needs to quickly issue such procedures to hold individuals and groups responsible. Specifically, the regulations issued should follow these principles:

- Fair, objective, transparent;
- Hold upper management partially responsible;

- The rewards and punishments must be carried out in compliance with laws and regulations;
- Incentivize all staff to take part in collecting NPL.

The regulations should clearly state the sanctions imposed on individuals and groups. Specifically as:

- **For individuals:**

The sanctions:

- Criticism.
- Reprimanded and notified within the branch.
- Warning and notified in the system.
- Suspension of work: person responsible for violation must move to another department within the bank and restrain participating in credit activities to focus on collecting NPL within a maximum of six months
- Forced to resign
- Brought to court (in extreme cases)
- Demotion, dismissal

- **For groups:**

- Criticism.
- Warning
- Demotion

Restrict activities: Disciplined groups will be barred from some if not all of operations involving credit activities.

Disciplined cases must be attached to the emulation, appointment, classification and payment in relevant areas.

The splitting of responsibilities for credit staff will ensure fairness in evaluating the quality of work, boosting efficiency as well as creating the of mind for the staff.

III.2.5. Training, developing and standardizing staff capacity related to credit operations

- The bank needs to build up standardized criteria by which an employee's performance can be fairly judged: competency, professional qualifications, practical experience, knowledge, self starter, ability to work independently and in a team, etc…
- The HR department should offer training programs to improve staff's competency. Training must be focused, meaning lower level staff learns to deal with daily tasks, while upper level management learns about planning and organizing. Employees in the debt handling department usually have a tougher job that varies case by case; therefore, they need special attention. Debt collection staff also regularly updated information on the areas concerned the debt collection.
- The reward and discipline policy should be clear-cut based on the quality of work. Fair policies must be are the premises for a high morale and work ethic among employees.

- Employees should be rotated around different departments to deepen their knowledge and experience in different areas. In the long run this will improve their ability to work in teams since they understand the other team members' job better.

III.2.6. Developing an effective information system

BIDV QT should develop a mechanism to exchange information effectively, ensure regular contact, continuous and timely updating of critical information between functions in the operation of credit. Credit risk management can only be successfully by solving the problem of information exchange mechanism. Therefore, the establishment of mechanism must ensure the separation of functions to perform specialized and increasing objectivity without losing the ability to capture and control information of credit risk management division. For this, the key information in the lending process should be periodically and extraordinary updated by the credit officers and forward this information to credit risk management division to analysis, assess the potential risks. In addition, banks should develop information systems and analysis of comprehensive information, supplying accurate, reliable and professional information to concerned division.

By developing new and improved infrastructure, BIDV QT may also diversify its own revenue-generating activities – in other words, reducing its dependence on credit activities. It has been proven in developed countries that retail banking can be a safe and stable source of revenue for commercial banks. Services such as credit card, car payment, foreign exchange, derivative-related services and insurance all benefit from a modern information system. As of 2014, BIDV Headquarter has realized the importance of such operations and has chosen BIDV QT as one of the first branch to open a retail-focus business center whereby retail customers can choose from a great variety of services tailored to fit their individual needs.

III.2.7. Flexibility in handling NPL

III.2.7.1. Improving debt collection practices

Based on the results of the analysis, banks should take appropriate measures to encourage customers to find the funds to repay their debts as quickly as possible, as interest rates for overdue loans are usually rigged at 150% of the normal rates. After detecting signs of NPL incurred, banks should immediately put the borrowers on a special watch list, paying attention customer's cash inflow account which is opened at the bank to collect debt promptly. Banks also need to actively collaborate with customers to devise debt amortization plans. The role of the debt collector cannot be undermined. In order to achieve the desired results, the debt collector must be highly knowledgeable and adaptable to different situation since no two customers are exactly alike.

For debt recovery to achieve the best results, BIDV QT need to build an incentive mechanism for employees and departments who successfully collect NPL. To maximize the value of NPL recovered, BIDV QT should develop reward employees with a bonus as a percentage of the value recovered.

Besides, in case of NPL causing by the deliberate acts of the credit officers, the bank needs to hold such employees accountable fully for the losses.

III.2.7.2.Debt restructuring

Some NPL arose due to extraordinary situations that the borrowers could not foresee. In case the customers are still in business and are still capable of paying off the NPL in later years, the bank may consider restructuring the loans so as to ensure the borrowers' financial solvency. This has a dual effect: as it helps the borrowers stay in business, it also helps the bank recovery an otherwise unrecoverable loan should a bankruptcy occur.

In order to qualify for restructuring, however, borrowers need to provide the bank with proof that temporary insolvency was caused by unforeseeable factors. They also need to devise a feasible debt restructuring plan which at least must include a new business plan and/or additional collateral.

III.2.7.3. Effective use of allowance to handle NPL

To ensure safe operations in the case of risk occurring, BIDV QT must strictly comply with Decision No. 493/2005/QD-NHNN dated April 22, 2005 by the SBV about the Regulation on classification of debts, appropriation, setting up and use of reserves for handling credit risks in banking activities of credit institutions loan classification, provision and use provision reserves to handle NPL and reduce credit risks in banking activities credit institutions and Decision No. 18/2007/QD-NHNN of April 25, 2007, on amendment of and addition to a number of articles of the regulations on classification of debts, and establishment and use of reserves to deal with NPL. As of now, treatment of bad debt by using provision reserve accounts for the largest proportion of the solutions for handling NPLs in commercial banks in Vietnam because this option is always available to banks. However, BIDV QT needs to classify loans so as to truthfully reflect the financial status of the borrowers. Besides, BIDV QT should also raise awareness among debt collectors to recover as much as possible because these loans are added back to the banks' income in later years.

III.2.7.4. Improving handling of collaterals

The inspection and review all credit files is the first required step in process of handling NPLs. BIDV QT should thoroughly review and audit all customer files to add the missing records and detect the new assets which are not mortgaged yet, and ingeniously require the borrower add more collaterals to secure for the loans.

BIDV QT should reassess residual value of the collateral and classify that property on three aspects: the ownership, the legal and the ability to sell products on the market to choose the appropriate form of treatments.

Firstly, for the properties which are easy to sell or transfer in the market and qualified legally, BIDV QT must actively coordinate with customers to sell them in the market in the shortest time to recover debts.

Secondly, for these assets which are qualified legal, but difficult in selling or transferring as of specialization of these properties, BIDV QT has actively cooperated with both clients and relevant agencies or the auctioned centers and public information on the mass media.

III.2.7.5. Selling of NPLs

By participating in the debt market, BIDV QT may sell NPLs for companies specialized in debt collection, who are not under the strict restraints of the banking industry. The proceeds from sales will help BIDV QT process further NPLs, minimizing loss in time and resources.

Selling NPLs has been successfully in other countries such as China and Thailand. Unfortunately, this measure has not generated enough interest in Vietnam as most banks would simply take care of NPLs using allowance.

III.2.8. Recommendations for government's agencies

Economic crisis, high inflation as well as the shrinking investment in the government sector caused demands in many industries to decline. Therefore, the author has some recommendations to the government, the State Bank and relevant ministries as followings:

- The government should have synchronous solutions to finance core industries such as construction, steel and minerals to stabilize input prices, lower interest rates and to keep inventory low.
- The government should use a more lenient and flexible system of regulations governing NPL restructure in this difficult period. The policy must require sufficient documents of clients such as: documents to prove the reasons causing customers unable to repay the loans, a plan to overcome losses in production and business activities, clear, specific, stable, viable and feasible source of repayment plan, ensuring the ability to repay the debt (principal and interest) in full and on time by period proposed restructure. This policy will evaluate the situation, financial capacity of the borrower to determine the right ways for them in the process of reschedule their loans.
- For the banking system, SBV, state audit and inspection of state bank must work closely together to conduct inspections, audit the credit activity, as well as deposit in the banks, to ensure enterprises have access to capital with a reasonable interest rate and feasible projects.

CONCLUSION OF CHAPTER III

Based on the theoretical content in Chapter I, depth analysis of the management of NPL of BIDV QT in Chapter II, Chapter III has studied basic direction of managing NPL in BIDV in the future, and provides some recommendations to improve the effectiveness of NPL management at BIDV QT.

GENERAL CONCLUSIONS

Managing NPL effectively in banking operation to reduce NPL rate and to increase the quality of credit activities and financial capacity is the top priority at BIDV QT, more now than ever before. Based on thorough research and analysis, the main reasons causing increase NPL at BIDV QT are as followed:

- Macroeconomic: economic crisis accompanying with tightening public investment and restricting real estate investment caused demand in many industries decline. High inflation, high interest rates made the financial cost of enterprise increase, and the domestic and foreign market become worsen.
- Borrowers: The borrowers simply borrow too much an too spread-out, effectively increasing the risk for all parties involved. Short-term loans are used for long-term capital investment without a second thought to sustainable growth. In a perfect world those extremely risky investments can pay off hugely to the corporate owners but in this particular case, they do not.
- Banks: customer evaluation was sub-par. Credit officers as well as their superiors either cannot or choose not to foresee the level of risk involved in huge loans with questionable feasibility.

Therefore, to improve managing NPL, reduce NPL ratio, BIDV QT should:

- Have detailed planning aimed for safety in credit operations
- Enhance the quality of credit evaluation before granting credit, inspection during and after granting the loan.
- Improving the organizational structure of credit operations and credit risk management
- Promulgating rules for determining responsibility and penalty for individuals and groups in credit activities
- Training, developing and standardizing staff capacity related to credit operations
- Developing a mechanism to exchange information effectively
- Flexibility in using the measures to handle NPL

As NPL management is a complicated issue, the final project has some limitations which are the collection of primary data. Because of the different and diversified characteristics of the borrowers, the questions and number of interviewees might not enough to represent the whole picture. The reasons causing increase NPL may be subjective and, thus, might not fully reflect the current situation. The further work needs more technical skills and larger scope. Therefore, it is suggested that future researches might extend the scope to the Vietnamese banking sector for a more accurate result.

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APPENDIX 1 - LIST OF INTERVIEWEES

Number	Name	Position/Department
I	**Board of Directors**	
1	Mr. Le Quang Thanh	Director
2	Mr. Le Van Manh	Deputy Director
3	Mrs. Nguyen Thi Minh Huong	Deputy Director
II	**Corporate customer department**	
4	Mr. Duong Viet Phuong	Corporate customer manager
5	Mr. Do Trung Kien	Corporate customer deputy manager
6	Ms. Le Bich Diep	Supervisor
7	Mr. Nguyen Duy Anh	Credit officer
8	Mr. Nguyen Bao Khanh	Credit officer
9	Ms. Uong Thi Hai Yen	Credit officer
10	Ms. Dao Thi Huyen Thuong	Credit officer
11	Ms. Nguyen Thi Mai Phuong	Credit officer
12	Mr. Nguyen Van Dung	Credit officer
III	**Credit management department**	
13	Ms. Pham Thi Phuong Thuy	Manager
14	Mr. Thai Manh Cuong	Deputy Manager
15	Ms. Nguyen Thi Hanh	Officer
16	Ms. Tran Thi Hong Lien	Officer
17	Ms. Le Hien Linh	Officer
IV	**Risk management department**	
18	Mr. Vu Duc Toan	Manager
19	Mr. Dang Tuan Linh	Deputy Manager
20	Ms. Ngo Kieu Nhung	Officer

APPENDIX 2 – LIST OF QUESTIONNAIRE FOR THE IN-DEPTH INTERVIEW

The content of questionnaire is designed and answered for purely research purposes of analyzing the management of NPL at BIDV QT. Responses to this questionnaire will be used to develop general findings and conclusions without specific reference to institutions, clients, except where information may be independently available in the public domain.

A. QUESTIONNAIRE FOR BANKING DIRECTORS AND MANAGERS

1. How many percent of loan in group 2 move to loan in group 3 as of 12/31/2013? Which areas did this situation mainly focus on?
2. Could you please tell me the operation of the production and business of borrowers at BIDV QT in the recent years?
3. What are the current policies on managing credit and NPL at BIDV QT?
4. What are the reasons causing the increasing NPL at BIDV QT?
5. How did you manage and handle to reduce the NPLs? Which methods were considered most effective in handling this problem?
6. What types of security/ collateral do bank require and what is the preferred form used?
7. What proportion of corporate lending is secured?
8. Describe the key problems that exist in the creation, recording and enforcement of security and collateral?
9. What are the organizational structure of a credit recovery group and the process for decision-making? What are the standardized procedures for handling credit recovery at BIDV QT?
10. Which qualification requirements and training process for staff in credit department, especially for staff in a credit recovery group?
11. What steps does your branch follow to verify the integrity and accuracy of information provided by borrowers?
12. What additional changes or recommendations would you propose to improve and strengthen the management of NPL at BIDV QT?

B. QUESTIONNAIRE FOR BANKING STAFFS

1. Have you carefully analyzed the situation of crisis which can negatively affect to the business of borrowers when granting credit to them?
2. What reasons cause the difficulties in doing business of the borrowers?
3. Have you considered the situation of incomplete project due to lack of own capital causing the borrowers use short term liabilities or lending other banks with expensive cost to offset its own capital?
4. In the evaluation process for credit, have you evaluated the quality of customer's assets such as receivables, inventories, assets in progress, and carefully analyzed the ability in management or element of trust of leaders in doing business of the borrowers? Do you analyze the difficulties which may be happened from other activities throughout the company?
5. How often do you inspect using of loans from the borrowers after granting credit? What criteria do you focus on when auditing?
6. Have you regularly monitored and identified the companies related to borrowers as well as tracked the transfer of money, debts, cash flow in the group of customers associated with each other?
7. What type of information do you collect from corporate borrowers to assess business activities and projects being implemented by the customer?

8. How often do you monitor and update information about the volatility of sectors which affect the business of borrowers?
9. Have the financial statements of borrowers audited by third party and certified by the tax authorities yet when the borrowers provided them to the bank?
10. Have BIDV QT had a court official or a lawyer who work part time in the bank to review and monitor the document of the loan yet?
11. How do you feel when you are assigned only to recover bad debt and not involved in providing credit to customers?