



# NPL Asia

Issue 9 | May 2008

Welcome to the first edition for 2008 of *NPL Asia*, our newsletter on the Asian non-performing loan (NPL) market. Since our last issue in March last year, we have seen a mix of trends. China continued to be slow, but other markets proved very active, most notably Thailand, with four of its banks selling NPLs worth over US\$1 billion in the last quarter alone. Taiwan continued the trend of multiple sales, with Malaysia and India also hosting multiple sales. Vietnam is a new entrant, and certainly worth following in the next few years. To date there has been little activity there in portfolio sales but interest is strong and opportunities for single credit deals appear to be increasing.

On balance, the Asian NPL market in 2008 is expected to be active and at the time of writing there are at least four ongoing sales in the region. Clearly, one of the big questions in 2008 will be how the United States' financial woes affect NPL sales/distressed deal activity. The impact is in fact likely to be minimal, as the appetite for distressed deals in Asia remains strong in terms of both portfolio and single deals.

The information contained in *NPL Asia* has been obtained from numerous sources in the market and is believed to be accurate at the time of going to print. We trust you will continue to find this publication useful and welcome any comments you may have.

## NPL Sellers in 2007

<b>China:</b>	China Orient, Cinda, Great Wall, Huarong
<b>India:</b>	UCO Bank, Arcil, Bank of Baroda
<b>Malaysia:</b>	Maybank, Alliance, Ambank
<b>Philippines:</b>	Philippine National Bank
<b>Taiwan:</b>	Land Bank of Taiwan, Taishin International Bank, China United Trust & Investment Bank, Hua Nan Commercial Bank, Chinese Bank, Bank of Taiwan
<b>Thailand:</b>	Bank of Ayudhya, Exim Bank, KBank, Siam Commercial Bank, TMB Bank
<b>Vietnam:</b>	Agribank

## Another slow year

As we predicted in our last issue, 2007 was a pretty flat year for foreign investors in the China NPL market, with reported outstanding principal balance (OPB) sales totalling only US\$3 billion. We can only surmise as to why sales to foreign investors have never really been as big as first anticipated for China. Is it simply because the asking prices of the asset management companies (AMCs) are too high? Or is it because the AMCs are focusing elsewhere as they start preparing for a life after NPLs? Whatever the reasons, reported NPL sales to foreign investors in 2007 were down compared to 2006, and indeed down compared to the last four years. The result: an apparent exodus of experienced investors (Citigroup, Mellon, UBS, Clearwater, Orix) and only one new entrant (Societe General) to replace them. If deal activity remains low in 2008, one can only expect that more investors will head for greener pastures. But, as outlined below, we remain cautiously optimistic that government pressure on the AMCs and other factors could lead to increased sales activity in 2008.

Buyer	Seller	Location	OPB (RMB billion)	OPB (US\$ million)	Total (US\$ million)	Date
CarVal	China Orient	Jiangsu	1.0	129		Oct-07
	Huarong	Guangdong	6.6	881	1,010	Jun-07
DAC	China Orient	Shanxi	1.5	205		Jul-07
	China Orient	Jilin	1.0	140		Jun-07
	China Orient	Jiangsu	1.0	133		Jun-07
	China Orient	Jiangsu	0.4	60		Dec-07
	China Orient	Hebei	0.2	32		Dec-07
	Cinda	Hebei	0.6	82		Oct-07
	Cinda	Jiangsu	0.1	17		Mar-07
Caylon/ DAC	Great Wall	Heilongjiang	0.7	93		May-07
	China Orient	Guangdong	0.4	55	817	Dec-07
Bank of America	Undisclosed	Guangzhou	2.0	268		May-07
	Undisclosed	Shanghai	1.0	134	402	Jun-07
DB Zwiir	China Orient	Guangxi	2.6	350	350	Jan-07
Avenue Asia	China Orient	Liaoning	1.6	218	218	Jun-07
PPF	China Orient	Inner Mongolia	1.0	140	140	Jun-07
	China Orient	Chongqing	0.7	95		Jan-07
Societe Generale	Cinda	Dongguan	0.3	40	135	Dec-07
<b>Total</b>			<b>22.9</b>		<b>3,072</b>	

Note: In addition to the above, GE Comm Finance and Corstone are both rumoured to be attempting to close deals signed in 2007.

Source: PwC research; amounts confirmed with buyers.

Please note that this information is not intended to be a full list of all sales, but rather a selection of some publicly known sales that PwC is aware of.

While the AMCs sometimes seem preoccupied with business tie-ups with commercial partners and transforming themselves into investment banks, rather than with disposing of their stockpile of NPLs, it is very likely that they will have an opportunity to acquire even more of these loans. The Agricultural Bank of China (ABC), the last of the 'big four' state-owned commercial banks to restructure, needs to unload approximately US\$100 billion of its NPLs as it readies for an initial public offering (IPO) in 2009–10. Sources indicate that approximately US\$60 billion of these loans are Category IV (doubtful) loans and the rest Category V (loss) loans. Great Wall AMC is favoured to receive the Category V loans. The Category IV loans will be sold to the highest bidder via an auction among the four AMCs, who will have to borrow from China's central bank, the PBOC, to pay for them. The good news for investors is that this transfer could cause the AMCs to step up their disposal efforts as they will soon be under pressure to repay at least the interest on the monies borrowed from the PBOC to finance their acquisitions.

## More reasons sales will pick up in 2008–09

In addition to looming interest payments to the PBOC relating to the ABC's NPL acquisitions, the AMCs will face other pressures that may encourage them to increase the pace of their NPL disposals. When the AMCs were established in 1999 to acquire the NPLs from the four (then insolvent) state-owned banks, they issued bonds to finance the purchases. While it is unclear whether all of the AMCs are current with their interest payments, the bonds mature in 2009 and 2010, so payment will have to be dealt with. It is possible this maturity date will be extended; however, the day will come when the bonds will be payable and it is unlikely that the AMCs will have the means in the short term to meet their repayment obligations. In this case, the Ministry of Finance (MOF) will have to step in to make the payments on behalf of the AMCs. We believe the MOF will begin applying pressure on the AMCs to raise as much capital as they can towards the bonds' repayment. This will likely trigger an increase in loan disposals.

## NPL numbers may increase further

The AMCs hold a significant number of NPLs – enough to last them for several years at the current rate of disposals. But while the China Banking Regulatory Commission (CBRC) regularly announces declining NPL ratios at the country's commercial banks, the fact remains that there are approximately US\$175 billion of NPLs in the banking system that are not held by the AMCs<sup>1</sup>. We believe this level could increase substantially in the next two years due to any one or a combination of the following factors:

- Cash flow problems for Chinese businesses, particularly exporters, stemming from the US subprime crisis
- An increase in (government-controlled) interest rates due to measures to curb excessive growth and inflation
- Fall-out from companies that have misused borrowings to speculate in China's (now) declining stock market and property markets.

<sup>1</sup> CBRC website

The combination of new NPLs being transferred to the AMCs as a result of the ABC IPO with new NPLs possibly being created in the banking system has revived rumours that the banks will finally be able to bypass the AMCs and sell NPLs directly to investors. Should this occur the AMCs will, for the first time, face some stiff competition from the banks. Many of the banks will have more recent NPLs to sell, which will be more appealing to investors than the older NPLs held by the AMCs. This could cause the AMCs to lower their asking prices, which would lead to a pick up in the pace of dispositions in the months before the banks get the official go ahead.

## India

### Slow momentum in transactions and reforms

Looking back on 2007, the first half of the last financial year (ending March 2008) did not see much activity in NPL auctions other than a secondary auction by Asset Reconstruction Company (India) Limited ('ARCIL'); however, action picked up significantly in the second half. As at March 2008, seven banks reportedly approached the market with NPL portfolios totalling Rs 25 billion (US\$605 million). While ARCIL and Bank of Baroda (advised by PwC) successfully completed transactions, most of the other transactions did not succeed largely due to gaps in value expectations. Other issues affecting the success of these transactions included portfolio packaging, allowing cherry picking, issues with the sale process and sale and purchase agreement (SPA) concerns.

The last financial year also saw IFCI Ltd, an Indian term lending institution, inviting offers for a strategic equity stake. IFCI Ltd is the oldest financial institution in the country. Over the past five years, IFCI Ltd has operated as a 'bad bank', focusing on resolving its NPLs. Unfortunately, the transaction did not proceed, again mainly due to value expectation gap and control-related issues.

Of particular interest is the NPL auction by ARCIL mentioned above, which was the first instance of ARCIL selling NPL portfolios through the auction process. ARCIL aggregated the financial stakes of different banks and financial institutions, and carried out financial/ business restructuring (where possible). Based on the resulting cash flow streams, it also invited distressed debt investors to acquire the NPL portfolio. Demand for cash by the originating lenders, who had received security receipts (pass-through instruments) in consideration for transferring their NPLs to ARCIL a few years ago, was reportedly a factor leading to this secondary auction by ARCIL. To compete with other NPL investors making upfront cash payments to selling banks, ARCIL raised a US\$65 million fund from eligible, largely domestic, investors. ARCIL will act as an investment manager to this fund.

The last financial year also saw the first retail NPL acquisition (mortgages) by ARCIL from a private sector bank. Recent macroeconomic developments in India, including an increase in interest rates, have affected retail borrowers' paying capacity, and we may see increased action in retail NPLs.

On the investor front, there has been no change in the government's guidelines on foreign investment in the equity share capital of asset reconstruction companies (ARCs) or in security receipts issued by trusts set up by these ARCs. This has, in effect, limited foreign participation in NPL deals, especially NPL portfolio auctions by banks. The regulatory requirements have, on the one hand, limited competition. On the other hand, the

limited number of eligible investors has effectively created 'closed auctions', giving a greater level of comfort to existing bidders. At the same time, India's Reserve Bank has granted registration to new ARCs, taking the number of operational ARCs to seven.

Looking at single credit deals, while the number of distressed debt transactions has been lower, most special situation investors have widened their definition of special situations. Subsequently, the distinction between private equity houses, distressed debt funds, special situation funds and venture funds has become blurred. A couple of recent transactions have included provision of growth capital to companies who were not able to raise the required funds through traditional banking channels. We also saw increased interest in real estate projects from these special situation investors. Foreign investors such as Citigroup, Clearwater, ADM Capital, JP Morgan Chase, Spinnaker, WL Ross, Lehman Brothers, Cargill, Avenue and JC Flower have been active in India.

### Outlook

We see continued activity in the portfolio space. We also see public sector banks as well as ARCIL bringing NPL portfolios to the market. In addition, we expect an increasing number of retail NPL transactions. Further, several regulatory obstacles are in the process of being removed, pricing benchmarks are evolving and, as a result, there continues to be increased investor interest in India. Going forward, India's NPL market is expected to continue to offer significant investment opportunities.

## Malaysia

### Not all are on board yet

The last 12 months saw a modest level of selling activity by local banks and locally incorporated foreign banks (LIFBs).

The country's first portfolio sale by auction, following the issuance of the NPL Sale Guidelines by the Central Bank in December 2005, was completed in 2007. The sale was undertaken by Malayan Banking Berhad ('Maybank') in two tranches. The total OPB was RM 424.8 million (US\$134.3 million).

Soon after, a second local bank disposed of a portfolio of NPLs in two tranches for RM 440 million (US\$139.1 million). A couple of LIFBs sold smaller portfolios while other local banks sold single loans. These deals were done through either a competitive bid or a bilateral negotiated process. Maybank finished the year by selling a second portfolio of secured retail loans.

At least four NPL portfolio sales of corporate and retail loans are planned for the first half of 2008. At the time of writing, the second largest bank group in the country, CIMB Bank, had just launched its first portfolio sale of corporate loans.

Notwithstanding the increased level of interest among the banks, it would be fair to say, given the NPL Sale Guidelines are over two years old, that the number of transactions has not been very significant.

In our view, one of the reasons for the apparent reluctance of local banks to sell is their belief that the price offered by would-be buyers would not do justice to the underlying value of the loans or, more precisely, their collateral. Many banks believe they can recover higher value by managing the NPLs inhouse. However, there are signs that banks are beginning to realise that

the cost of holding on to NPLs exceeds the perceived benefits, in terms of both the carrying costs and the deterioration in selling prices.

Still, the Malaysian market may prove to be the hot spot in the Asia Pacific region in the months to come. Interest levels of distressed debt investors remain high. The situation at the moment is one where there are more buyers than sellers. Anticipating an increase in transactions, several NPL investors have set up local offices to manage the distressed debts they purchased and scope out new deals. This is in spite of the relatively long delays involved in closing transactions caused by the local regulatory process.

Of late, a number of banks (both local and LIFBs) have tested the market with small portfolio sales. Perhaps some had been waiting for benchmark prices to emerge before setting off on the sale process. Others could realise that selling NPLs may be an expedient way of reducing the NPL ratio when loan growth becomes challenging. The fact that the two largest bank groups have taken the sale route should provide a lead for other banks to follow.

## Philippines

With the expiry of the Special Purpose Vehicle (SPV) Act in May 2008, the Philippines' central bank, the Bangko Sentral ng Pilipinas ('BSP'), anticipates banks will sell bad assets amounting to approximately Php 70 billion (US\$1.6 billion) under the SPV Act. This is lower than the central bank's target of Php 100 billion (US\$2.3 billion) from SPV sales. It was initially approved and implemented in April 2004 for two years but was extended until May 2008 to give banks and other financial institutions (FIs) more time to enjoy the incentives. The SPV Act applied to the following types of transactions:

1. Transfer of NPLs by an FI to an SPV
2. Transfer of real and other properties acquired (ROPA) by an FI to an SPV
3. 'Dation in payment' (*dacion en pago*) of NPLs by a borrower to an FI
4. Dation in payment of NPLs by a third party, on behalf of the borrower, to an FI
5. Transfer of NPLs (secured by a real estate mortgage on a residential unit) by an FI to an individual
6. Transfer of ROPA (e.g. single family residential unit) by FI to an individual.

Any of these transactions may be exempt from documentary stamp tax, capital gains tax, creditable withholding income tax, value-added tax and gross receipts tax. The transactions may also be entitled to a 50% reduction on the applicable mortgage registration and transfer fees, filing fees for any foreclosures and land registration fees.

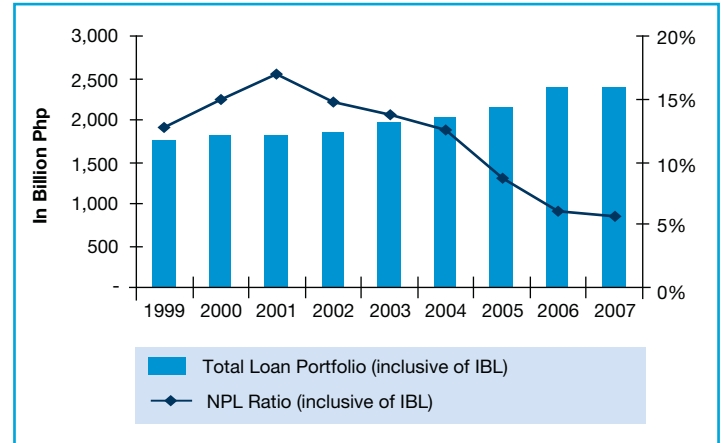
During the period of the SPV Act, NPL ratios have reduced from approximately 14% in 2004 to just over 5% in 2007, as a percentage of the total loan portfolio. The graph below plots the NPL ratios of all banks against the total loan portfolio from 1999 until the first half of 2007.

As at August 2007, bad loans of universal and commercial banks had dropped to 5.3% (Php 103.3 billion/US\$2.4 billion) of the total loan portfolio, compared to 7.2% a year earlier. On the other

hand, the sector's ROPA to gross assets ratio improved to 3.6% in August from 4.5% a year earlier. The thrift (savings) banking industry's NPL ratio as at August 2007 was only slightly better at 9.1% compared to the previous year's rate of 9.7%.

Based on a report by BSP, non-performing assets (NPAs) for the entire banking industry as at 30 June 2007 totalled Php 326.1 billion (US\$7.7 billion), 37% below the levels of 30 June 2002. Of the Php 193.9 billion (US\$4.6 billion) of NPAs sold during this period, Php 32.0 billion is accounted for by NPAs sold under the extended SPV Act.

### NPL Ratio Against Total Loan Portfolio, All Banks



Source: Bangko Sentral ng Pilipinas

Note: 2007 data refers to the second quarter of 2007, while for the other years, the December balances were used.

### Expectations for 2008

Local banks and government financial institutions are planning to sell NPAs totalling Php 62.4 billion (US\$1.4 billion) in 2008. Details of the NPAs are as follows:

- United Coconut Planters Bank will sell Php 6.3 billion (US\$0.1 billion) of NPLs and about Php 13.8 billion (US\$0.3 billion) of ROPA.
- Land Bank of the Philippines will sell about Php 4.6 billion (US\$0.1 billion) of NPLs and NPAs under the SPV Act through a public auction.
- Allied Bank Corporation intends to sell an estimated Php 5.0 billion (US\$0.1 billion) of ROPA to a joint venture partner under the SPV Act.
- Philippine National Bank will sell Php 1.3 billion (US\$0.03 billion) of NPLs and Php 2.7 (US\$0.06 billion) of ROPA under the SPV law.
- Pag-ibig Fund intends to sell Php 21.6 billion (US\$0.5 billion) of NPLs and Php 5.7 billion (US\$0.1 billion) of ROPA.
- Development Bank of the Philippines will sell Php 1.4 billion (US\$0.03 billion) of NPLs and Php 0.5 billion (US\$0.01 billion) of ROPA.

However, of the Php 62.4 billion (US\$1.4 billion) of NPAs to be sold, only Php 33.6 billion (US\$0.8 billion) is accounted for by universal and commercial banks. We expect that an additional Php 26.0 billion (US\$0.6 billion) of NPAs will be sold to achieve the BSP's target of bringing down the NPL ratio for Philippine banks to the pre-1997 financial crisis level of 4%.

## Implications of Basel II implementation for banks with large NPL ratios

The current capital adequacy framework of the BSP closely follows the guidelines set by the Basel Committee. Banks are mandated to maintain a minimum capital level in order to hedge against credit, market and operational risks. The capital level is computed by following prescribed risk weights for assets. NPLs are among the items with the highest risk weights.

With the BSP's announcement to adopt Basel II guidelines from July 2007, new sets of risk weights were assigned for bank assets. In particular, NPLs made for housing purposes were assigned a risk weight of 100%, while all other NPLs were assigned a risk weight of 150% starting 2007.<sup>2</sup>

NPL ratios declined. This may be merely a reflection of the larger banks' efforts to clean up their balance sheets, with many of the smaller banks yet to clean up their balance sheets.

## Taiwan

### A changing banking scene

After its cash card and credit card NPL crisis, Taiwan's banking industry has continued to evolve. NPL sales increased in 2007, due partly to the restructuring of distressed banks (see below). As at the end of October 2007, the sale of NPLs in Taiwan by public auction amounted to NT \$117.5 billion (US\$3.6 billion). This compared to NPL sales totalling NT \$87 billion (US\$2.9 billion) in 2006. Taiwan's NPL market grew by 35% in the first 10 months of 2007. Three quasi-government banks and three distressed banks generated most of these NPL sales for the 10-month period, accounting for 55% and 45% of sales respectively.

To strengthen the competitiveness of local banks, the Financial Supervisory Commission restarted the 'second-stage' financial reform. Its intention was to trigger more financial sector consolidations, especially for government-controlled banks. In August, the Executive Yuan announced it would establish the Taiwan Financial Holding Company, planning to merge the government-owned Bank of Taiwan, Land Bank of Taiwan and Export-Import Bank into one entity. Furthermore, the government plans to gradually sell its shares in some of the banks, such as First FHC, Huan Nan FHC, Taiwan Cooperative Bank and Taiwan Business Bank. The government's initiatives have led these government-controlled banks to prepare for consolidation through disposal of their NPLs, by either internal write-off or public auctions.

Bank of Taiwan completed its first NPL sale in September, disposing of a portfolio totalling NT \$32 billion (US\$1.0 billion). Hua Nan Bank also disposed of a NT \$15 billion (US\$0.5 billion) NPL portfolio in the second half of 2007. In addition, TCB held another NPL portfolio sale for NT \$40 billion (US\$1.3 billion) in December to lower its overdue ratio of 2.44%, a level that was slightly higher than other government-controlled banks. The TCB NPL sale was estimated to be the largest in 2007.

### Continued resolution of distressed banks

Under the Banking Act, the government may assign officials to assume control of a bank's operation if it fails to pay its liabilities when due or risks damage to depositors' interests due to obvious adverse changes in its business or financial status.

No.	Seller	Approximate Size		Asset Type	Buyer	Financial Advisor
		NT\$ Billion	US\$ Million			
1	Land Bank of Taiwan	9.66	297	Corporate & Individual	Orix, Taiwan	PwC
	Land Bank of Taiwan	9.31	286	Corporate & Individual and REO	Mega AMC and Huan-Nan AMC	
2	Taitung Business Bank (Tranche A)	5.02	154	Corporate & Individual	Orix, Taiwan	PwC
	Taitung Business Bank (Tranche B)	4.31	132	Consumer Loan	Liang-Jing Co.	
	Taitung Business Bank (Tranche C)	4.29	132	Consumer Loan	Liang-Jing Co.	
3	Chinese Bank (Tranche A)	13.98	429	Corporate & Individual	GE Capital	PwC
	Chinese Bank (Tranche B)	3.70	114	Credit Cards loan	Yangtze AMC	
	Chinese Bank (Tranche C)	3.70	114	Consumer Loan	Yangtze AMC	
4	Bank of Taiwan (Tranche A)	15.90	488	Corporate & Individual	Yong Sheng AM	PwC
	Bank of Taiwan (Tranche B)	16.00	491	Corporate & Individual	TAMCO	
5	China United Trust & Investment Co.	17.00	522	Corporate & Individual	GE Capital	PwC
6	Hua-Nan Commercial Bank	14.60	448	Corporate & Individual	TAMCO	E&Y

Source: Information collected by PwC

Please note that this information is not intended to be a full list of all sales, but rather a selection of some publicly known sales that PwC is aware of.

In 2007, the Financial Supervisory Commission (FSC) took over the management of five distressed banks and completed NPL public auctions for four of them – Taitung Business Bank, Chinese Bank, China United Trust & Investment Corporation, and BOWA Bank. On 31 January 2008, the FSC also took over Asia Trust & Investment Corporation, which had been on the FSC's watch list for years. We expect its NPL auction to be held in early July. There is another bank under FSC's observation as target for takeover if the bank cannot improve its levels of capitalization within a designated period of time.

<sup>2</sup> <http://www.bsp.gov.ph/downloads/Regulations/C280Amended.pdf>

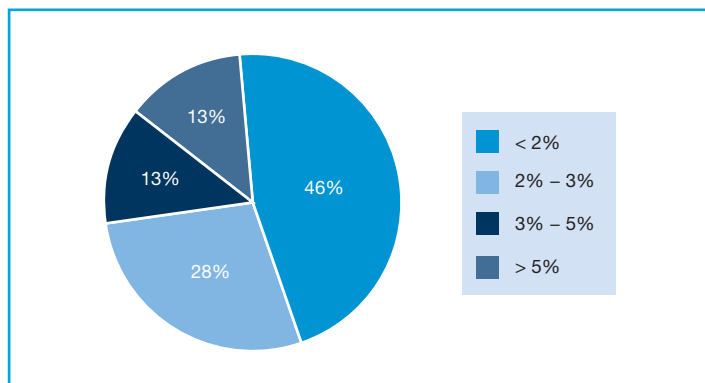
<http://www.bsp.gov.ph/regulations/implementation.asp>

BSP Unveils Basel II Implementing Guidelines, 08.09.2006, <http://www.bsp.gov.ph/publications/media.asp?id=999>

## What's next?

On the sell side, the consolidation of financial institutions in Taiwan and resolution of distressed banks will continue to be catalysts for new NPL sales in 2008. On the buy side, Orix Taiwan, GE Capital, Shinsei Bank and TAMCO are still very actively bidding. Also, new participants, such as Standard Bank, Fubon AMC and Yungta AMC have made an appearance in a couple of sales and are expected to participate in the future NPL market, indicating the potential of the NPL market in Taiwan. However, after six years of effort, most of the financial institutions have lowered their overdue ratio below 3%, with an average ratio of 2.16% in September 2007. If the economy doesn't change dramatically, large volumes of NPL sales such as those of the past five years are not expected in the future. Moreover, the resolution of distressed banks will likely culminate in 2008 unless a more aggressive policy is applied.

## Overdue Ratio of Local Banks in Taiwan



Source: Banking Bureau, Financial Supervisory Commission

## Thailand

### Back in Business

After a number of years of little or no NPL portfolio activity, 2007 turned out to be one of the busiest years of NPL activity in Thailand since the Asian Economic Crisis of a decade earlier. Five banks held multiple tranche public auctions, including one bank (Siam Commercial Bank or SCB) holding multiple auctions. There were also a number of attempted bilateral deals, with market rumours reporting mixed results, as well as a number of single credit transactions.

While the typical sales process in Thailand has yet to follow other Asian countries (ie the use of paper-based data rooms and at times limited due diligence periods), all sales in 2007 attracted wide interest. Of the five banks to hold public auctions, four banks appointed external advisors to help conduct the sales. Outlined below is a summary of known 2007 sales.

While there was much talk of what effect the Capitals Control Act, the military coup of 2006 and the elections held in late 2007 would have on the Thailand economy, the commercial reality was very much 'business as usual'. As a result, investor interest in Thailand remains high, although deals – especially single credit deals – still remain challenging due to bank price expectations. The property sector continues to be very active, although this sector also represents the most likely opportunity for single credit/private equity type plays.

Seller	Tranche	OPB THB billions	OPB USD millions	Date	Buyer
TMB	Tranche A	5.6	170.0	Mar-07	Negotiations ongoing
	Tranche B	4.1	125.0	Mar-07	Negotiations ongoing
Exim Bank	Tranche A	4.2	127.0	Nov-07	SAM
	Tranche B	4.5	135.0	Nov-07	SAM
K Bank	Tranche A	7.9	240.0	Dec-07	Standard Bank
	Tranche B	6.4	193.9	Dec-07	Morgan Stanley
BAY	Tranche A	6.2	187.9	Dec-07	Negotiations ongoing
	Tranche B	3.7	112.1	Oct-07	Lehmans
	Tranche C	4.8	145.5	Mar-07	Did not sell
SCB*	SME/Retail Tranche	3.5	106.1	Nov-07	SAM
	SME/Retail Tranche	5.9	178.8	Aug-07	Lehmans
	SME Tranche	4.3	138.0	Mar-08	Morgan Stanley**
	SME Tranche	4.1	132.0	Mar-08	Morgan Stanley**
		<b>65.2</b>	<b>1,991.2</b>		

\* SCB also offered a number of corporate accounts, however these are rumoured to have sold poorly or not at all

\*\* Rumoured and not confirmed

Source: PwC market research

Please note that this information is not intended to be a full list of all sales, but rather a selection of some publicly known sales that PwC is aware of.

2007 also saw further foreign bank acquisitions, namely ING's acquisition of a 30%+ stake in TMB. Banks with large foreign shareholders now include TMB (ING and DBS), BAY (GE) and Bank Thai (Newbridge).

The key factor that may impact sales in 2008 is the current credit crunch resulting from the US subprime crisis. However, independent research by PwC indicates that appetite for Thai distressed debt (and in indeed Asian distressed debt) remains high. Still, pricing will likely be affected, as the cost of debt and/or required returns is now higher.

How this will ultimately effect Thai transactions only time will tell. Thai banks, perhaps riding on the successful outcomes of the 2007 sales, are continuing to plan sales in 2008, with market rumours indicating that at least four banks will go to market this year with upwards of Thb 40 billion (approx US\$1.25 billion) of NPLs.

What is becoming more apparent though is that both sellers and buyers prefer to conduct NPL sale transactions via a local AMC. Those buyers submitting conditional bids subject to AMC formation are likely to find their bids rejected outright in favour of those buyers who already have their own AMC or have affiliation deals with existing AMCs.

Other opportunities likely to arise in Thailand in 2008 include the property sector, where perhaps the first effects of the tightening of credit policies are being felt, which in turn may affect other industries such as steel and cement. A number of banks holding equity positions as a result of debt/equity swaps may also look to divest these holdings. For more strategic plays, the FIDF will also be selling its equity positions in a number of banks including Bank Thai (of which Newbridge and Marathon already have stakes), Siam City Bank and Krung Thai Bank. In summary, the

activity of 2007 looks set to continue in 2008. According to the Bank of Thailand, as at December 2007 gross NPLs represented 7.81% of total loans (commercial banks registered in Thailand), or Thb 442 billion (approx US\$14 billion). The Bank of Thailand defines gross NPLs as the outstanding amount of loans classified as substandard, doubtful, doubtful of loss, and loss.<sup>3</sup>

## Vietnam

### Strong economic growth but few immediate NPL opportunities

With its high economic growth rates, favourable demographics and recent entry into WTO, Vietnam is attracting significant interest from foreign investors. It is also a market in transition – moving from a managed/centralised economy to one based on market principles.

This is all bringing increased opportunities, but looking specifically at the NPL market, is Vietnam becoming an attractive proposition? We believe the answer is ‘not yet’. However, the situation could change quickly.

### Low level of NPLs

There is uncertainty over the ‘true’ levels of NPLs in the Vietnam’s banking system. Official estimates by the State Bank of Vietnam (‘SBV’) of NPL levels were around 3% as at the end of 2006 – a relatively low figure, particularly when compared to other countries in the region. However, while no official figures are published for NPLs, market rumours suggest that current levels may be closer to 15%, if not higher.

The reason for disparity in levels lies in the quality of the loan assessment and classification system applied by the banks under the SBV’s regulations. There is a view that many of the loans currently classified as performing would qualify as NPLs, if assessed under international standards. The basis adopted by Vietnamese banks assesses overdue status based on a customer’s repayment history rather than an assessment of a debtor’s ability to repay based on qualitative measures.

### Compelling reasons for a higher NPL ratio?

Despite the lack of detailed analysis, there are some compelling arguments supporting a higher ratio:

- **Practical application.** Within the overall NPL ratio of 3%, one bank, BIDV, was reporting NPL levels closer to 9% at 31 December 2006. We understand that this higher ratio reflects management’s policy to attempt to report a ‘true’ NPL figure. BIDV engaged independent advisors to assess its loans based on international standards and the result was the higher NPL ratio.
- **Rescheduling.** It is well documented that many loans have been ‘rescheduled’, that is, capital repayment dates have been deferred. Under international standards such loans are likely to be captured as NPLs – even more so if the interest payments are being funded by further borrowings.

- **IFRS financials.** State-owned commercial banks (SOCBs) that have prepared financial statements using International Financial Reporting Standards disclosed NPL ratios far higher than the number disclosed under Vietnamese Accounting Standards.

In addition, a significant number of loans have been written off by SOCBs and this further distorts the NPL position.

Finally, Vietnam’s strong growth and positive economic outlook also cloud the issue. More specifically, loan books have been growing at around 25–30% per annum over the last few years and concerns are being voiced over the credit quality of the new loans.

### Low activity levels

Given the low level of disclosed NPLs, there is, as might be expected, little loan resolution or trading activity being generated.

The lack of NPLs is also an issue for Vietnam’s national AMC – the Debt and Asset Trading Company (‘DATC’). DATC was established a number of years ago with a mandate to help resolve Vietnam’s NPLs. However, it currently finds itself with little to do. While there is some evidence that activity is on the increase – DATC recently acquired US\$4.8 million of loans from Agribank, one of Vietnam’s larger state-owned banks – it would be fair to say that transactions of this size are still few and far between.

There are a number of legal impediments that will need to be removed before private sector entities can operate effectively in the secondary debt market.

### In summary – watch and wait

The potential size of Vietnam’s NPL market and the nature and scale of resolution and trading activity could be significant. In addition, with many state owned enterprises – including banks – going through corporatisation (and in so doing attracting overseas strategic investors), a clearer picture of the NPL situation and underlying market values will start to emerge. If there is also a recognition of the growing NPL burden, there is likely to be a greater will to resolve the overall problem. This in turn will increase the activity levels for DATC and the wider NPL market.

However, given the uncertainty over NPL levels, coupled with its emerging market status, we view Vietnam in the “watch and wait category”.

<sup>3</sup> Bank of Thailand website

# Our Contacts

Across Asia we have experienced partners and directors who can assist you with your NPL-related needs. In addition, PwC has a dedicated international NPL group that can act as an overall coordinator for worldwide NPL mandates and opportunity identification. Through this group, both buyers and sellers of NPLs can receive consistent and seamless service across the world, integrated with country-specific knowledge and expertise.

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