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Alliance Financial Group Bhd

“Short Term Pain for Long Term Gain”

Results Review

- Actual vs. expectations.** Alliance Financial Group Berhad (AFG) 3M16 net profit of RM122 million (-7% y-o-y) came in line with ours and consensus estimates respectively, accounting 22% and 21.5% of ours and consensus full year net profit forecast. Note that earnings were hit by higher allowance for losses amounting RM17.1 million in 3M16 on the back of higher collective provision booked amounting to RM17.4 million (RM15.5 million in 3M15) as well as slower recoveries booked.
- Dividend.** No dividend declared in this quarter.
- Topline vs. Bottom line.** AFG net income reached RM344 million (+2% y-o-y) fuelled by higher contribution from net-interest income of RM208 million (+9%) on the back of higher interest from loans (+14.4% y-o-y). Growth in net interest income was well offset by operating expenses that jumped commendably by 4% y-o-y to RM167 million. Despite disappointment in bottomline, pre-provision income was still at healthier level of RM177 million (+1% y-o-y).
- Short term pain for loans growth.** Loans growth (gross) grew moderately by 1.1% y-o-y in 3M16. The result is highly contradicted with AFG’s higher-than-industry loans growth in the past. This could emanate from AFG’s efforts to focus on risk adjusted return-focus more on selected profitable loan rather than on quantity driven. Moving forward, management has guided slower loans growth of 8%-9% in FY16. YTD loans growth touched 0.3%.

Wednesday, August 19, 2015

BUY (TP: RM4.70)

Current Price (RM)	RM3.66
New Fair Value (RM)	RM4.70
Previous Fair Value (RM)	RM4.90
Previous Recommend.	BUY
Upside To Fair Value	28.4%
Dividend Yield (FY16)	6%

Stock Code

Bloomberg	AFG MK
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Stock & Market Data

Listing	MAIN MARKET	
Sector	Banking	
Shariah Compliance	No	
Issued Shares (mn)	1,548.1	
Market Cap (RM mn)	5,666	
YTD Chg In Share Price	-22%	
Beta (x)	1.07	
52-week Hi/Lo (RM)	RM5.07	RM3.59
3M Average Volume (shrs)	1.25 mill	
Estimated Free Float	54.6%	

Major Shareholders

Vertical Theme Sdn Bhd	29.06%
EPF	17.31%
Malaysia Focus Inv.	4.75%

Market Access

- **Improving liquidity position.** One of AFG risk adjusted returns focus is to further improve liquidity position despite intensified competition to secure low cost deposit. Despite total deposits dropping by 4% y-o-y derailed by weakening fixed deposit that shed by 34.4% y-o-y, however, this was largely within the management expectation to reduce the dependency on fixed deposits in view of slower loans growth. That said, AFG is now eyeing to grow CASA deposits to relieve its cost of funds. Note that CASA position improved to 34.5% vs. 33.6% in 4Q15. Loan-to-deposit (LDR) stood at 85% vs. 82.8% in 4Q15, signalling slower loans growth.
- **Asset quality improving further.** Gross NPL continued to decline both in absolute and percentage terms with gross NPL ratio to 1.0% from 1.02% in 12M15. On the back of lower recoveries and higher collective allowances, however, credit costs were slower at 7bps in 1Q16. Loans loss coverage rose to 105.4% vs 102.7% at end-March 2015.
- **Net interest margin (NIM) relieved marginally.** Driven by risk adjusted return effort, NIM returned to positive territory by 1bps to 2.16%. Moving forward, AFG efforts could lead NIM to stay at positive territory as AFG is planning to focus on higher yielding loans such as consumer segment (personal loans, credit card) and SME segment. Meanwhile, growth in mortgages, auto hire purchase and commercial property lending are expected to be reined.
- **Outlook.** We are surprised with the management decision to skew its loans composition into higher yielding loans. That said, AFG's robust double-digit loans growth in the past will not be sustainable in view of reducing selected household loans. Meanwhile on SME front, management still believe stable outlook for the segment given its effort to focus on underserved small-sized segment. However, we are cautious on its loans loss provision as management had indicated collective allowance to maintain at 1.2% of loans book and hence, it will may slice its net profit further.
- **Change to forecast.** We imputed lower loans growth of 9% y-o-y and hence, came up with lower interest income. In that, we have cut our earnings assumption by 0.7% in FY16. Given this, FY16 and FY17 earnings are expected to grow by 1.6% and 11% respectively driven by 1) low risk as 50% of SME are collateralized business 2) benefit from OPR hike (if any) as more than 90% of variable rate forms its loans portfolio 3) migrating into higher yielding loans segment (contradict with previous para).
- **Valuation & recommendation.** We reduce our TP on AFG to RM4.70 based on 3-year average P/BV of 1.88x on lower loans growth target, but we maintain BUY call on AFG. Rerating catalyst for the stock could emanate from i) lower-than-expected provision allowance ii) higher-than-expected LDR to assist loans growth iii) new M&A deal.

## Results Review - Alliance Financial Group Bhd

Table 1: Peers Comparison

Company	Year Ended	Price (RM)	EPS (RM)		P/E (x)		P/B (X)		ROE (%)	Div Yield (%)	TP (RM)	Call
			FY15	FY16	FY15	FY16	FY15	FY16				
AFG	March	3.66	0.4	0.4	12.7	12.0	1.7	1.6	14.3	1.9	4.70	Buy
AMMB	March	5.00	0.6	0.6	11.0	11.0	1.4	1.3	14.1	4.5	6.80	Buy
BIMB	Dec	4.06	0.3	0.4	11.7	11.3	1.8	2.0	16.0	5.8	4.84	Buy
CIMB	Dec	4.94	0.5	0.6	12.1	10.4	1.3	1.5	9.2	3.5	6.10	Buy
Maybank	Dec	8.43	0.7	0.8	12.6	11.9	1.5	1.5	13.6	6.2	10.70	Buy
RHB Cap	Dec	6.52	0.8	0.9	9.7	9.1	1.1	1.1	11.5	1.3	8.35	Buy
Public Bank	Dec	17.96	1.2	1.3	15.3	14.2	2.6	2.8	18.7	2.9	21.70	Buy
Affin	Dec	2.27	0.3	0.3	9.0	8.5	0.7	0.7	7.8	5.1	NR	NR
MBSB	Dec	1.37	0.2	0.3	9.1	8.4	1.2	1.1	29.6	2.3	NR	NR
STMB	Dec	3.60	NA	NA	NA	NA	NA	NA	24.3	6.6	NR	NR
HL Bank	June	12.82	1.2	1.3	12.0	11.2	1.6	1.5	14.7	2.9	NR	NR
Average			0.6	0.7	11.5	10.8	1.5	1.5	15.8	3.9		

Source: Bloomberg, M&amp;A Securities

Table 2: Financial Summary

YE: March (RM million)	1Q16	4Q15	1Q15	y-o-y	q-o-q	3M16	3M15	y-o-y
Gross Interest income	464	432	423	10%	7%	464	423	10%
Interest expense	(256)	(246)	(224)	14%	4%	(256)	(224)	14%
Net interest income	208	186	200	4%	12%	208	200	4%
Islamic banking income	59	58	54	9%	1%	59	54	9%
Fee and commission income	70	70	74	-5%	1%	70	74	-5%
Fee and commission expense	(28)	(28)	(28)	0%	0%	(28)	(28)	0%
Investment income	24	15	33	-27%	61%	24	33	-27%
Other income	11	5	3	227%	146%	11	3	227%
Net income	344	306	337	2%	13%	344	337	2%
Operating expenses	(167)	(165)	(162)	4%	1%	(167)	(162)	4%
Pre-provision income	177	141	175	1%	26%	177	175	1%
Allowance loan loss	(17)	(17)	(2)	877%	-2%	(17)	(2)	877%
Impairment	1	2	-	0	-56%	1	-	0
Operating profit	161	125	173	-7%	29%	161	173	-7%
Associate	0	0	-	0	5050%	0	-	0
PBT	161	125	173	-7%	29%	161	173	-7%
Taxation	(39)	(31)	(43)	-9%	23%	(39)	(43)	-9%
PAT	122	93	131	-7%	31%	122	131	-7%
EPS	7.9	6.0	8.4	-7%	31%	7.9	8.4	-7%
<u>Margin</u>								
NII Margin	60%	61%	59%			60%	59%	
NOII Margin	23%	20%	25%			23%	25%	
PPOP Margin	51%	46%	52%			51%	52%	
PBT Margin	47%	41%	51%			47%	51%	
PAT Margin	35%	30%	39%			35%	39%	

Source: Bursa Malaysia, M&amp;A Securities

Table 3: Financial Forecast

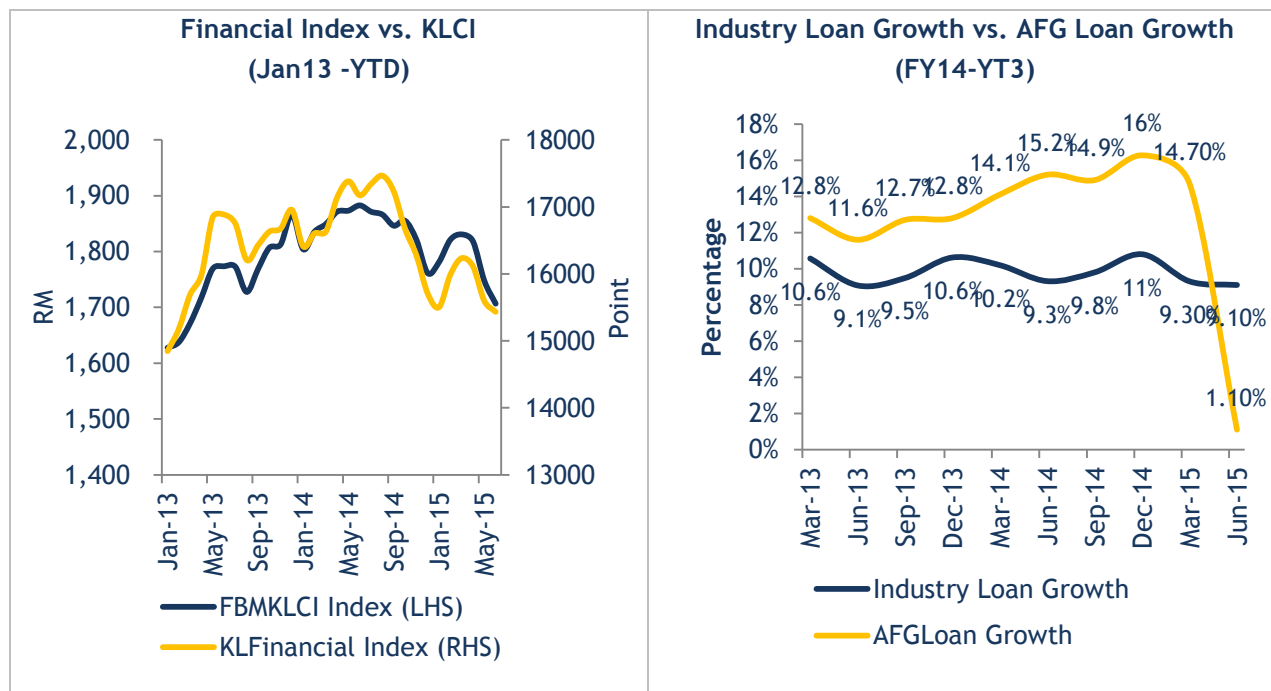
Y/E: March (RM'mil)	FY13	FY14	FY15	FY16F	FY17F
Net interest income	730	779	821	810	873
Islamic banking income	242	211	225	239	249
Fee and commission income	267	314	309	357	380
Fee and commission expense	(92)	(104)	(114)	(135)	(155)
Investment income	117	104	87	109	111
Other income	69	45	55	55	60
Net income	1,333	1,349	1,383	1,435	1,518
Operating expenses	(639)	(628)	(647)	(654)	(679)
Pre-provision income	694	721	736	781	840
Allowance loan loss	25	14	(40)	(71)	(47)
Impairment	0	15	7	8	8
Operating profit	719	749	703	718	801
Associate	(5)	0	0	0	0
PBT	714	749	703	718	801
Taxation	(176)	(186)	(172)	(178)	(199)
PAT	538	564	531	540	602
EPS (sen)	35.3	37.2	34.8	34.9	38.9
Dividend - sen	16.6	29.5	15.4	23	23
Dividend payment (RMm)	257	457	238	356	356
PER (x)	13.5	12.6	13.3	11.9	10.7
BV	1.96	2.25	2.42	2.54	2.76
P/BV	2.4	2.1	1.9	1.6	1.5

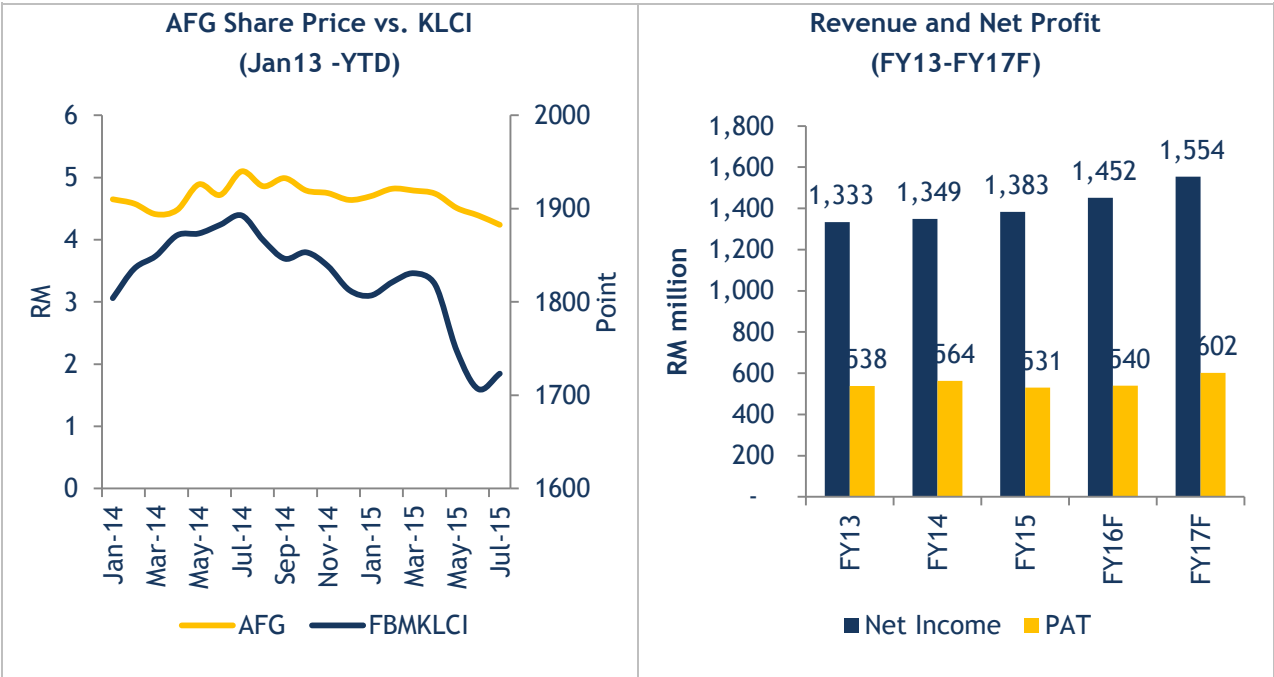
Source: Bursa Malaysia, M&amp;A Securities

Table 4: Operational Ratio

Y/E: Dec (RM'mil)	FY13	FY14	FY15	FY16F	FY17F
<b>Growth</b>					
NII	9%	7%	7%	3%	10%
NOII	-1%	20%	5%	1%	3%
Operating expenses	8%	-2%	2%	2%	4%
PPOP	6%	4%	8%	4%	10%
Core earnings	7%	5%	-4%	6%	14%
Gross loans	11%	13%	14%	10%	10%
Customer deposits	20%	14%	12%	9%	8%
	14%	10%	10%	10%	8%
<b>Profitability</b>					
NOII/Total income	9%	8%	9%	9%	9%
Average Lending Yield	4.2%	4.5%	4.5%	4.4%	3.9%
Average Cost of funds	0.0%	0.0%	2.4%	2.4%	2.4%
NII	35%	34%	34%	33%	32%
Cost/income	16%	17%	29%	27%	27%
<b>Asset Quality</b>					
Net NPL	1.7%	1.2%	1.0%	1.1%	1.0%
Gross NPL	2.2%	1.6%	1.4%	1.4%	1.4%
SP+GP/Gross Loans	0.1%	0.1%	0.3%	0.2%	0.1%
<b>Return</b>					
ROA	1.2%	1.2%	1.0%	1.0%	1.1%
ROE	13.3%	13.5%	11.5%	11.4%	12.0%

Source: Bursa Malaysia, M&amp;A Securities





Source: Bloomberg, M&A Securities

# M&A Securities

## STOCK RECOMMENDATIONS

<b>BUY</b>	Share price is expected to be $\geq +10\%$ over the next 12 months.
<b>TRADING BUY</b>	Share price is expected to be $\geq +10\%$ within 3-months due to positive newsflow.
<b>HOLD</b>	Share price is expected to be between $-10\%$ and $+10\%$ over the next 12 months.
<b>SELL</b>	Share price is expected to be $\geq -10\%$ over the next 12 months.

## SECTOR RECOMMENDATIONS

<b>OVERWEIGHT</b>	The sector is expected to outperform the FBM KLCI over the next 12 months.
<b>NEUTRAL</b>	The sector is expected to perform in line with the FBM KLCI over the next 12 months.
<b>UNDERWEIGHT</b>	The sector is expected to underperform the FBM KLCI over the next 12 months.

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