PP14767/09/2012(030761)

Monday, August 10, 2015

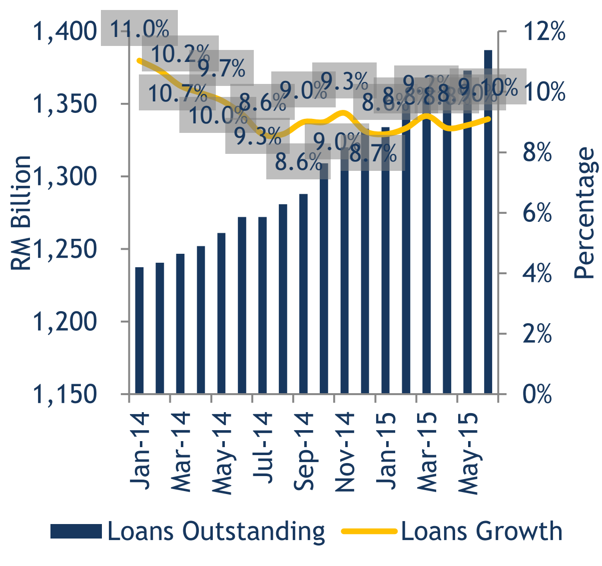
"Cautiously Optimistic on Banks in 2H15"

Banking sector is a NEUTRAL in 2015 as we expect loans growth to hit 9.0% vs. 9.5% in 2014. YTD banking sector loans growth average had reached 8.8%, marginally lower against our expectation and hence, no cause for alarm. Driver to the banking sector loans growth this year includes 1) steady ETP related financing 2) acceleration of re-financing drive towards shariah approved 3) steady equity and debt market performance. Our Top Picks for banking sector are Maybank (TP: RM10.70) and BIMB Holdings (TP: RM4.84).

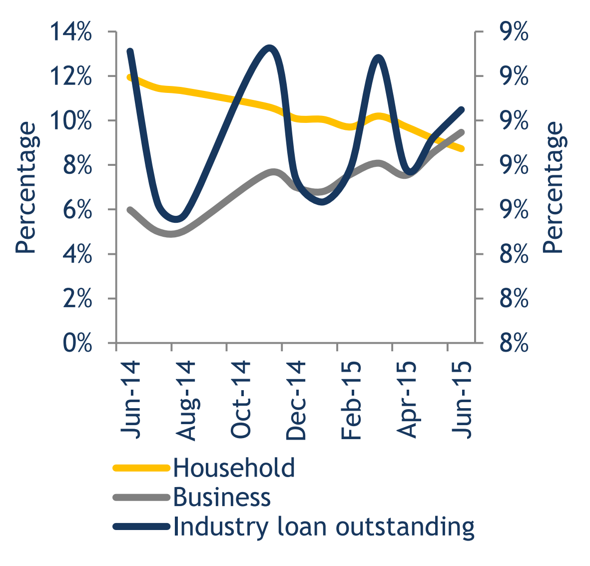
Further bumpy road ahead. Apart from persistent net interest margin (NIM) compression, Malaysia banks are challenged by issues such as slowdown in non-interest income due sluggish capital market activity, rising cost of funds due to intense competition for deposits, higher credit cost due to slow recoveries and higher operating costs due to GST implementation. All these will weigh on banks earnings in 2H15. Concomitantly, we foresee banks will adopt cautious approach to negate the issues.

Loans growth outlook. We see limited opportunity for banks to improve their loans growth performance in 2H15, given the slowdown in residential mortgages from 13-14% in 2014 to 5.1% YTD. To reiterate, we projecta slower loans growth momentum of 9% in 2015, a slight decline from 9.5% in 2014, anchored by business loans to support banks loans growth while we expect a slowdown in household loans (HH) due to myriad of exogenous factors.

Loans Growth
(Jan 2013-YTD)



Loan Growths Y-o-Y by Segment
(Jun 2014-YTD)



Source: BNM, M&A Securities

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Table 1: Y-o-Y Gross Loan Growth

Company	Year Ended	Sep-13	Dec-13	Mar-14	Jun-14	Sept-14	Dec-14	Mar-13	Mgt Guidance
AFG	March	12.6%	12.8%	14.1%	15.2%	15.5%	16.2%	14.7%	11%-12%
AMMB	March	6.2%	6.1%	5.3%	1.5%	0.9%	-2.1%	1.6%	7.0%
CIMB	Dec	13.7%	12.6%	11.9%	8.1%	9.8%	13.2%	12.4%	14.0%
Maybank	Dec	12.0%	13.7%	13.5%	12.6%	14.3%	13.4%	14.3%	13.0%
PBK	June	12.0%	13.7%	13.5%	12.6%	9.8%	10.8%	11.7%	10%-11%
RHB Cap	Dec	13.9%	9.2%	11.2%	13.0%	11.9%	17%	13.7%	12.0%

Source: Bursa Malaysia, M&A Securities

Persistent NIM compression. For 1H15, we witnessed Malaysia banks reported an average net interest margin (NIM) compression of -10bps to 2.20% vs. -7bps in 4Q14 due to higher cost of funds. This was due to intense competition for retail deposits and the situations are expected to continue due to new regulation of Bank Negara's Liquidity Coverage Ratio. As a result, we witnessed that banks are skewing their deposit composition to meet the LCR requirement to more retail deposits. Additionally, we foresee banks are deserting their loan-to-deposit ratio to the extent of 89% in average, due to inability to grow deposit to higher base. The only bank reported a q-o-q increase in NIM was Maybank, with a commendable 6bps improvement to 2.26%, due in large part to an improvement in funding mix.

Table 2: Net Interest Margin

	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	q-o-q chg
AFG	2.17%	2.11%	2.27%	2.25%	1.85%	-40bps
AMMB	2.77%	2.45%	2.54%	2.38%	2.33%	-5bps
BIMB	3.55%	2.88%	2.81%	2.86%	2.85%	-1bps
CIMB	2.85%	2.90%	2.82%	2.79%	2.65%	-14bps
Maybank	2.37%	2.35%	2.31%	2.20%	2.26%	+6bps
Public Bank	2.28%	2.20%	2.29%	2.20%	2.15%	-5bps
RHB Capital	2.33%	2.29%	2.29%	2.26%	2.22%	-4bps

Source: Various, M&A Securities

Reflecting GST impact. Despite some banks have released their CY1H15 result, we foresee that 1H15 result will witness the transition period where banks have to adjust to a number of factors including the GST implementation including back-end system, compliance and slowdown of consumer consumption. This in line with our moderate view of 9% loans growth in banking system to reflect the slowdown in HH loans especially in hire purchase segment. For the 2-3 past years, residential mortgages were the key driver of the industry's loans growth, contributing 35-47% to the industry's incremental loans in 2014. More pertinently, the introduction of cooling measures by central bank has dampened the property transaction.

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Table 3: Cost to Income

	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15
AFG	48.4%	44.9%	44.8%	44.7%	51.8%
AMMB	42.5%	49.8%	44.2%	49.8%	50.7%
BIMB	57.1%	56.0%	55.4%	54.3%	52%
CIMB	56.8%	58.9%	57.6%	63.2%	58.1%
Maybank	48.9%	46.6%	50.3%	50.7%	49.9%
Public Bank	31.8%	31.7%	28.9%	28.1%	31.0%
RHB Capital	53.6%	55.2%	51.1%	58.9%	54.3%

Source: Various, M&A Securities

Pressure on cost to income. The recent 1Q15 results suggested that the trend of higher overheads cost due to seasonally bonus payment to the staff. Nevertheless, the potential drop in earnings due to slowdown in both net interest and non-interest income suggest that banks cost to income (CTI) will trend higher, above the average of 53%. While we think the situation may not last, we believe some banks may ease the pressure by offering mutual separation scheme (MSS) as happened to CIMB. In CIMB case, CIMB offered Malaysia and Indonesia operation MSS, resulting 4,000 employees taking the offer costing RM443 million. While for Maybank, the recent adjustment in union collective agreement will have an impact to staff cost.

Table 4: Credit Costs

	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15
AFG	-0.22%	0.02%	-0.08%	0.31%	0.19%
AMMB	0.29%	0.37%	0.02%	-0.26%	-0.27%
CIMB	0.19%	0.24%	0.56%	1.43%	0.8%
Maybank	0.23%	0.17%	0.07%	-0.03%	0.24%
Public Bank	0.15%	0.11%	0.08%	0.10%	0.12%
RHB Capital	0.17%	0.05%	0.28%	0.12%	0.14%

Source: Various, M&A Securities

Credit costs and provision to trend higher. Although banks' asset quality was stable in 2015 (6M15 gross impaired loans ratio: 1.73% vs. 6M14: 1.85%), we believe the industry is bracing for another stage of higher credit cost due to: (i) implementation if 1.2% minimum collective allowance and regulatory reserve buffer (ii) GST implementation that could weigh on banks asset quality (iii) the lack of recoveries for bad legacy business.

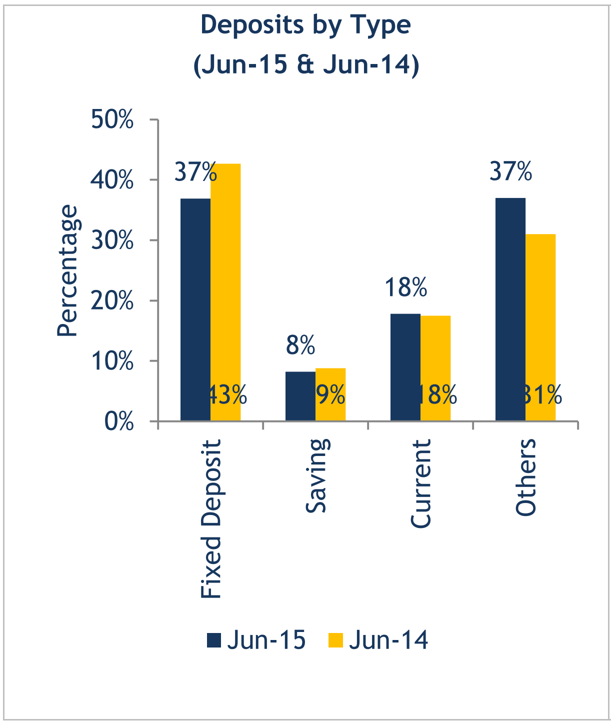
Table 5: Non Interest Income

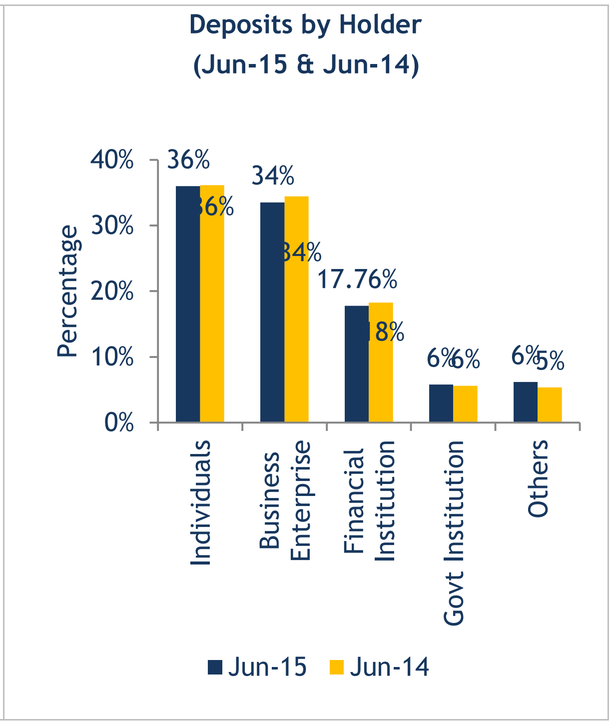
	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	q-o-q chg
AFG	11.76%	13.9%	17.1%	13.0%	13.0%	0bps
AMMB	16.3%	15.4%	14.9%	15.8%	15.7%	-1bps
CIMB	14.2%	13.3%	12.9%	13.9%	14.4%	+5bps
Maybank	17.7%	20.1%	21.1%	21.0%	18.8%	-22bps
Public Bank	15.6%	16.5%	15.8%	15.8%	16.3%	+5bps
RHB Capital	21.9%	20.7%	23.1%	27.0%	20.9%	-61bps

Source: Various, M&A Securities

Non-interest income to remains murky. 1H15 saw only minute IPO transaction, with only 2 companies made their presence in Bursa Malaysia, namely Malakoff Bhd and Sunway Construction Bhd, accumulating total funds of RM4.3 billion with several big names e.g. 1MDB,Iskandar Waterfront held back their intention to go for listing due to rough market environment. The muted IPO market has dampened non-interest income performance for most banks which already under pressure due to lower stockbroking income, resulting from cautious view approach as a result of US' intention to raise interest rate policy.

Liquidity position. Deposits growing were stable with the average loan/deposit ratio (LDR) for the banks marginally lower at 89.0% end-Mar 2015 from 89.7% end-Dec 2014. Customer deposits grew at an impressive pace of 11% y-o-y, slightly below from y-o-y loan growth. However, we foresee that the growth in deposits not mirroring the liquidity position as the new deposits secured were from business segment, rather than individual segment, reflecting a tough deposits taking competitions.





Conclusion and Recommendations

2015 will see banks slower but steady earnings due to the slow down in HH segment that account for about 50 % of banking system loans growth. However, we foresee this situation could improve at the back of a pickup in lending from business loans linked to financing of ETP-related projects and also refinancing activities by listed companies from conventional debts to shariah-compliant instruments. Banking sector is a **NEUTRAL** in 2015 with 2 banks emerge as our **Top Pick** namely Maybank (TP: RM10.70) and BIMB Holdings (TP: RM4.84).

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Market Access

Table 6: 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	3.99	0.4	0.4	12.7	12.0	1.7	1.6	14.3	1.9	5.05	Buy
AMMB	March	5.52	0.6	0.6	11.0	11.0	1.4	1.3	14.1	4.5	6.80	Buy
BIMB	Dec	4.11	0.3	0.4	11.7	11.3	1.8	2.0	16.0	5.8	4.84	Buy
CIMB	Dec	5.30	0.5	0.6	12.1	10.4	1.3	1.5	9.2	3.5	6.10	Buy
Maybank	Dec	8.96	0.7	0.8	12.6	11.9	1.5	1.5	13.6	6.2	10.70	Buy
RHB Cap	Dec	7.30	0.8	0.9	9.7	9.1	1.1	1.1	11.5	1.3	8.35	Buy
Public Bank	Dec	19.08	1.2	1.3	15.3	14.2	2.6	2.8	18.7	2.9	21.70	Buy
Affin	Dec	2.50	0.3	0.3	9.0	8.5	0.7	0.7	7.8	5.1	NR	NR
MBSB	Dec	1.68	0.2	0.3	9.1	8.4	1.2	1.1	29.6	2.3	NR	NR
STMB	Dec	3.92	NA	NA	NA	NA	NA	NA	24.3	6.6	NR	NR
HL Bank	June	13.40	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: BNM, M&A Securities

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M&A Securities

STOCK RECOMMENDATIONS

BUY	*Share price is expected to be ≥+10% over the next 12 months.*
TRADING BUY	*Share price is expected to be ≥+10% within 3-months due to positive newsflow.*
HOLD	*Share price is expected to be between -10% and +10% over the next 12 months.*
SELL	*Share price is expected to be ≥-10% over the next 12 months.*

SECTOR RECOMMENDATIONS

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

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