

5 July 2019

Banks

Limited Impact Expected From Softer GDP

Financial Services | Banks

Overweight (Maintained)

Stocks Covered 3
Ratings (Buy/Neutral/Sell): 2 / 1 / 0
Last 12m Earnings Neutral

- **Maintain OVERWEIGHT with BUYs on our Top Picks UOB and DBS.** Market expectations of softer 2019 GDP growth for Singapore and cut in US Federal Funds Rate (FFR) in 2H19 could dampen investors' appetite for Singapore banks. However, with economic recovery likely in 2020, we remain bullish on the sector.
- **Cut in RHB's forecast for Singapore's GDP growth to have limited impact on banks' earnings.** Our RHB economists had, in early July, cut Singapore's 2019 GDP forecast to 1.8% from 2.5%, amidst further weakening of domestic and external indicators. Slower 2019 GDP growth is a negative for Singapore banks. However, with 2020 GDP growth forecasted to pick up to 2.5%, we believe the impact on banks' earnings will be limited.
- **Possible FFR cut in 2H19 may narrow NIM.** Market expectations are for the US FFR to be cut in 2H19. This could lead to subsequent softness in the 3-month SIBOR (from 2% now and 2Q19's average of 1.98%), given its high correlation with the US FFR. With a time lag of about a quarter, the banks' NIM may narrow. Our sensitivity analysis suggests that any decline in SIBOR would impact DBS' net profit the most vs its peers.

Figure 1: Earnings sensitivity to SIBOR changes

	DBS	OCBC	UOB
FY20F net interest income rise for every 10bps increase in the SIBOR (SGDm)	72.8	43.3	41.3
Net of tax & as % of net profit	0.9%	0.7%	0.8%

Source: RHB

- **Impact from digital bank licences appears to be muted.** The Monetary Authority of Singapore (MAS) recently announced that it will issue up to five digital bank licences, of which two will be full digital bank licences. This will introduce more competition, although digitisation efforts (both past and future) of the three Singapore banks under our coverage should equip them to face this new challenge.
- **Lower CIR from digitisation a positive for banks.** Our TP for DBS of SGD30.80 is pegged to 2020F P/BV of 1.5x, and is derived from our long-term ROE assumption of 13.8% vs 1Q19's 14%. Our TP for UOB of SGD30.80 is based on 2020F P/BV of 1.29x, based on our long-term ROE assumption of 12.5% vs 1Q19's 11.4%.
- **Despite the possible peaking of NIMs in 2H19/1H20, we see NII expansion.** In addition, lower CIR from digitisation should drive ROEs over the next few years. Among the three banks, DBS should gain the most from a higher SIBOR over the near term, although any subsequent fall in the FFR would be negative for DBS. UOB is less exposed to Greater China, and therefore, more insulated from the US-China trade developments.
- **Downside risks to our forecasts** include higher impairment charges, and a sharper fall in the US FFR, which could dampen NIM.

Top Picks

UOB (UOB SP) – BUY
DBS (DBS SP) – BUY

Target Price

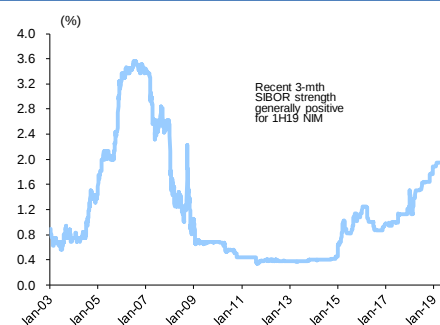
SGD30.80
SGD30.80

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SIBOR firmness in 1H19 positive for NIM



Source: Bloomberg

Company	Rating	TP (SGD)	% Upside (Downside)	P/E (x) Dec-19F	P/BV (x) Dec-19F	Yield (%) Dec-19F
DBS	BUY	30.80	18.2	11.0	1.35	4.6
OCBC	NEUTRAL	12.20	6.2	10.4	1.12	3.8
UOB	BUY	30.80	16.4	10.4	1.17	4.9

Source: Company data, RHB

Figure 2: Peer valuation

		DBS	OCBC	UOB
Price @ 4 Jul 2019	(SGD)	26.06	11.49	26.47
Mkt Cap	(SGD)	66,588	49,563	44,157
	(USD)	49,106	36,551	32,564
P/E (x)	Historical	11.7	10.6	10.9
	Current	10.8	10.3	10.6
	Forward	10.3	9.7	10.1
P/BV	(x)	1.31	1.11	1.20
ROE	(%)	11.5	11.1	11.3
ROA	(%)	1.1	1.0	1.1
Yield	(%)	4.6	3.7	3.8
YTD total return	(%)	13.7	4.0	10.7
1-month total return	(%)	7.4	8.1	10.3
3-month total return	(%)	0.3	0.7	2.9
6-month total return	(%)	15.7	4.8	11.5
1-year total return	(%)	4.6	3.4	2.0

Source: Bloomberg data

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