

14 January 2020

Financial Services | Banks

DBS (DBS SP)

Neutral (Maintained)

Expect a 4Q19 Sequential NIM Squeeze

Target Price (Return) SGD25.80 (-1%)
Price: SGD26.10
Market Cap: USD49,534m
Avg Daily Turnover (SGD/USD) 229.5m/170.5m

- **Stay NEUTRAL; SGD25.80 TP, 1% downside, 5% yield**, on 1.28x 2020F P/BV. 4Q19 weakness in the SIBOR and Singapore Swap Offer Rate is likely to lead to a sequentially narrower 4Q NIM. Market expectations: 1H20 US federal funds rate (FFR) to be relatively stable. However, the lagged effects of past FFR cuts should still narrow DBS' 2020 NIM. Amongst Singapore banks, its NIM is the most leveraged to changes in the 3-month SIBOR. We forecast NIMs to narrow in the quarters ahead – a negative headwind for earnings.

- **Softer 3-month SIBOR in 4Q19 to narrow NIM.** The 3-month SIBOR averaged 1.80% in 4Q19 (3Q19: 1.92%). This will contribute to softer lending yields and sequentially narrower NIMs. During 3Q19's results release, management guided for 2019 NIM of 1.88% vs 3Q19's 1.90% (our expectation too) and 2020 NIM to be 7bps narrower YoY.

- **Expect marginal sequential 4Q19 loan growth.** DBS had strong home mortgage bookings for primary market transactions in 2Q19 and 3Q19, and some of these could have translated into a sequential rise in 4Q19 home mortgages. Trade and non-trade loans are likely to have expanded sequentially during this period too. We forecast DBS' 2019 loan growth at 3.3%. Management's guidance is for 2020 loan growth to be similar to 2019's.

- **DBS' has high percentage loan exposure to Greater China**, but its focus on lending to Hong Kong corporates investing outside the latter is an offsetting factor. 30% of the bank's loans are to Greater China. This is higher than Oversea-Chinese Banking Corp (OCBC SP, NEUTRAL, TP: SGD11.50) and United Overseas Bank's (UOB SP, BUY, TP: SGD29.50) 25% and 16%. The current developments in Hong Kong are negative for banks with operations there – but DBS is probably insulated. This is because DBS Hong Kong (DBS HK) lends to the larger corporates that mainly use the funding for overseas operations, eg investing in ASEAN. Consequently, DBS HK's asset quality is less correlated with Hong Kong's economic growth.

- **Dividend yield to support share price.** We forecast a 2019 dividend of SGD1.20/share (4.6% yield) – consistent with DBS' 3Q19 quarterly interim one-tier tax-exempt dividend of 30 cents/share.

- **Our TP is based on 1.28x 2020F P/BV.** Our valuation on DBS is based on a long-term ROE assumption of 13.3% vs 9M19's 13.6% – the reduction is attributed to weaker NIMs and increased future competition from digital banks. This yields a 2020F target P/BV of 1.28x, which is close to the 7-year historical average of 1.21x. From this we derive our SGD25.80 TP.

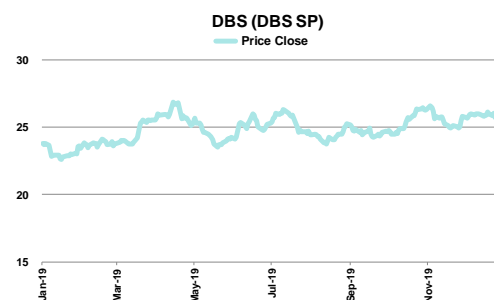
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	0.9	1.1	4.4	1.2	6.2
Relative	(0.0)	(0.1)	0.3	4.4	3.8
52-wk Price low/high (SGD)	23.86 – 28.64				



Source: Bloomberg

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Reported net profit (SGDm)	4,371	5,577	6,407	6,396	6,452
Recurring net profit (SGDm)	4,390	5,625	6,407	6,396	6,452
Recurring net profit gr (%)	3.6	28.1	13.9	(0.2)	0.9
Recurring EPS (SGD)	1.72	2.20	2.50	2.50	2.52
BVPS (SGD)	17.85	18.12	18.89	20.09	21.21
DPS (SGD)	1.43	1.20	1.20	1.30	1.40
Recurring P/E (x)	15.2	11.9	10.4	10.5	10.4
P/B (x)	1.46	1.44	1.38	1.30	1.23
Dividend Yield (%)	5.5	4.6	4.6	5.0	5.4
Return on average equity (%)	9.7	12.1	13.1	12.5	12.0
Return on average assets (%)	0.89	1.05	1.13	1.09	1.07

Source: Company data, RHB

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Financial Exhibits

Financial model updated on: 2020-01-14

Asia	Financial summary	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Singapore	EPS (SGD)	1.71	2.17	2.49	2.49	2.51
Financials	Core EPS (SGD)	1.72	2.20	2.50	2.50	2.52
DBS	DPS (SGD)	1.43	1.20	1.20	1.30	1.40
DBS SP	BVPS (SGD)	17.85	18.12	18.89	20.09	21.21
NEUTRAL						
	Valuation metrics	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Valuation basis	Recurring P/E (x)	15.2	11.9	10.4	10.5	10.4
GGM.	P/B (x)	1.46	1.44	1.38	1.30	1.23
	Dividend yield (%)	5.5	4.6	4.6	5.0	5.4
Key drivers	Balance sheet (SGDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Our net profit forecast is most sensitive to	Gross loans & advances	327,769	349,645	361,871	374,625	388,199
i. Changes in NIM;	Loan impairment allowances	4,670	4,642	5,483	5,763	6,058
ii. Non-II growth;	Net loans & advances	323,099	345,003	356,388	368,862	382,141
iii. Credit costs.	Total assets	517,711	550,751	580,247	594,588	613,547
	Deposits from customers	373,634	393,785	401,661	419,735	440,722
	Total liabilities	467,909	500,876	528,129	539,309	555,221
Key risks	Shareholders' funds	47,458	49,045	51,121	54,181	57,041
i. Higher impairment charges;	Total equity	49,802	49,875	52,118	55,279	58,326
ii. Weaker NIMs;						
iii. Softer non-II.						
Company Profile	Income statement (SGDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
DBS is the largest Singapore bank by assets. It also has significant Greater China operations.	Net interest income	7,791	8,955	9,716	9,610	9,671
	Non-interest income	4,483	4,228	5,147	5,613	5,914
	Operating income	12,274	13,183	14,863	15,223	15,585
	Overhead expenses	5,205	5,814	6,306	6,584	6,854
	Pre-provision operating profit	7,069	7,369	8,557	8,639	8,731
	Loan impairment allowances	1,894	710	855	940	955
	Other impairment allowances	0	0	0	0	0
	Pretax profit	5,175	6,659	7,702	7,699	7,776
	Reported net profit	4,371	5,577	6,407	6,396	6,452
	Recurring net profit	4,390	5,625	6,407	6,396	6,452
	Profitability	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	ROA (%)	0.89	1.05	1.13	1.09	1.07
	ROE (%)	9.7	12.1	13.1	12.5	12.0
	Yield on IEAs (%)	2.43	2.85	3.02	2.95	2.91
	Cost of funds (%)	0.74	1.07	1.29	1.31	1.30
	Net interest margin (%)	1.75	1.85	1.88	1.81	1.79
	Non-II / Total income (%)	34.7	32.1	34.6	36.9	37.9
	CIR (%)	43.0	44.0	42.4	43.3	44.0
	Credit cost (bps)	60.6	21.3	24.4	25.9	25.4
	PIOP growth (%)	8.5	4.2	16.1	1.0	1.1
	Net profit growth (%)	3.1	27.6	14.9	(0.2)	0.9
	Asset quality	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	Gross impaired loans/Loans (%)	1.7	1.5	1.6	1.6	1.5
	Loan loss coverage ratio (%)	84.7	91.2	90.2	91.6	93.2
	NPL formation (bps)	105	25	40	48	55
	Liquidity	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	Loan growth (%)	7.2	6.8	3.3	3.5	3.6
	Customer deposits growth (%)	7.5	5.4	2.0	4.5	5.0
	LDR (%)	86.5	87.6	88.7	87.9	86.7
	Capital	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	CET1 ratio (%)	14.3	13.9	14.2	14.7	14.9
	Tier-1 ratio (%)	15.1	15.1	15.0	15.1	15.4
	Total capital ratio (%)	15.9	16.9	16.8	16.9	17.1

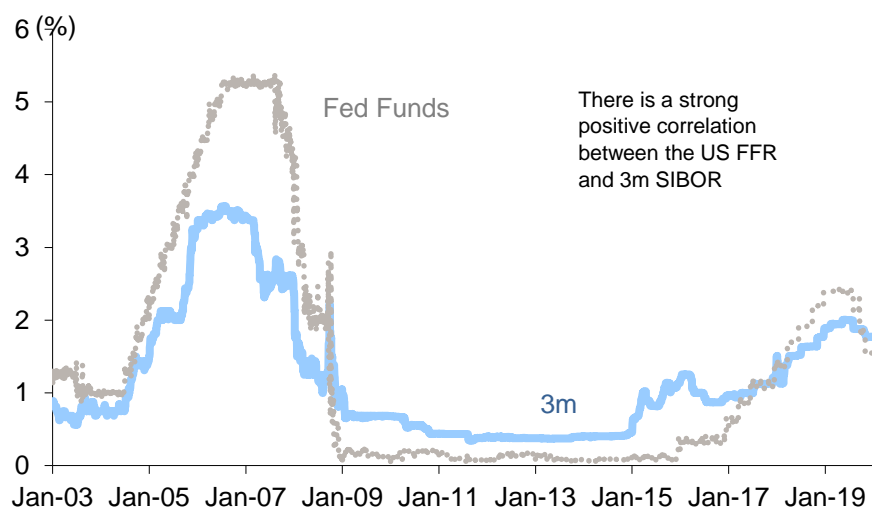
Source: Company data, RHB

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Falling SIBOR To Narrow DBS' NIM

Figure 1: 3-month SIBOR recently fell on weaker FFR



Source: Bloomberg

Figure 2: Sensitivity of net profit to SIBOR changes

	DBS	OCBC	UOB
FY20F net interest income rise for 10bps rise in SIBOR (SGDm)	72.8	42.0	40.9
- net of tax & as % of net profit	0.9%	0.7%	0.8%

Source: RHB

Figure 3: DBS has highest percentage loan exposure to Greater China

3Q19 Loan geographical breakdown (%)	DBS	OCBC	UOB
Singapore	47.0%	41.6%	51.4%
South & SEA	8.3%	N/A	N/A
South-east Asia	N/A	N/A	N/A
- Malaysia	N/A	11.0%	10.7%
- Thailand	N/A	N/A	6.9%
- Indonesia	N/A	7.7%	4.3%
Greater China	30.4%	24.5%	16.3%
- HK	15.9%	12.9%	N/A
Others	14.4%	15.1%	10.4%
Total	100.0%	100.0%	100.0%

Source: Company data

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Figure 4: DBS' financial data

DBS (SGDm)	FY17	FY18	FY19F	FY20F	FY21F
NII	7,791	8,955	9,716	9,610	9,671
Non-II	4,483	4,228	5,147	5,613	5,914
- Fee & commission income	2,622	2,780	3,079	3,432	3,572
- Other operating income	1,861	1,448	2,068	2,181	2,342
Total operating income	12,274	13,183	14,863	15,223	15,585
Operating expenses	(5,205)	(5,814)	(6,306)	(6,584)	(6,854)
Operating profit	7,069	7,369	8,557	8,639	8,731
Provisions	(1,894)	(710)	(855)	(940)	(955)
Pre-tax profit	5,175	6,659	7,702	7,699	7,776
Taxation	(671)	(1,006)	(1,255)	(1,255)	(1,268)
Profit after tax	4,504	5,653	6,447	6,444	6,508
Minorities	(133)	(76)	(40)	(48)	(56)
Net profit	4,371	5,577	6,407	6,396	6,452
EPS (SGD¢)	170.8	217.3	249.4	249.0	251.2
Book value (SGD)	17.85	18.12	18.89	20.09	21.21
Revalued book (SGD)	18.42	18.78	19.54	20.74	21.86
P&L ratios (%)					
ROE (Avg)	9.7	12.1	13.1	12.5	12.0
NIM	1.75	1.85	1.88	1.81	1.79
Net interest income/income	63.5	67.9	65.4	63.1	62.1
Operating expenses/income	42.4	44.1	42.4	43.3	44.0
P&L YoY change (%)					
NII	6.7	14.9	8.5	(1.1)	0.6
Non-II	7.1	(5.7)	21.7	9.1	5.4
Fee & commission income	12.5	6.0	10.8	11.5	4.1
Total income	6.8	7.4	12.7	2.4	2.4
Operating expenses	4.7	11.7	8.5	4.4	4.1
Operating profit	8.5	4.2	16.1	1.0	1.1
Provisions	32.1	(62.5)	20.4	9.9	1.6
Pre-tax profit	1.8	28.7	15.7	(0.0)	1.0
Net profit	3.1	27.6	14.9	(0.2)	0.9
BS data (SGDm)					
Assets	517,711	550,751	580,247	594,588	613,547
Non-bank loans	323,099	345,003	356,388	368,862	382,141
Customer deposit	373,634	393,785	401,661	419,735	440,722
Non-performing assets	6,070	5,684	6,082	6,292	6,502
Cumulative loan loss provisions	5,139	5,181	5,483	5,763	6,058
Balance sheet ratios (%)					
LDR	86.5	87.6	88.7	87.9	86.7
Non-bank loans growth (YoY%)	7.2	6.8	3.3	3.5	3.6
Customer deposit growth (YoY%)	7.5	5.4	2.0	4.5	5.0
Non-bank NPL/non-bank loans	1.7	1.5	1.6	1.6	1.5
LLC	84.7	91.2	90.2	91.6	93.2
Total CAR	15.9	16.9	16.8	16.9	17.1
Tier-1 CAR	15.1	15.1	15.0	15.1	15.4

Source: Company data, RHB

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