

14 May 2019

Financial Services | Banks

Banks

Overweight (Maintained)

More Upside For NII Ahead; OVERWEIGHT

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

- Maintain OVERWEIGHT with BUYs on our Top Picks, UOB (TP: SGD30.80) and DBS (TP: SGD30.80).** The two banks, together with OCBC, recently reported 1Q19 net profit, which met our and market expectations. 1Q19 NIM showed some QoQ divergence, with DBS & OCBC recorded a widening whilst UOB saw a 1bp narrowing. Looking ahead, rising lending yields (from lag effects of higher SIBOR) could help widen NIMs. Efficiencies from digitisation is another catalyst to drive banks' earnings higher.
- Expect general trend of NIM widening.** DBS guided for 5-6bps NIM expansion for 2019 (from 2018 level), and OCBC guided for ~5bps widening in 2019, driven by rising lending yields. On the other hand, UOB said its more aggressive fixed deposit expansion led to 1Q19 NIM QoQ narrowing and guided for flat 2019 NIM. We forecast NIM for the three banks to be generally on a mild widening stance going forward.
- Mid-single digit 2019 loan growth forecast for all three banks.** In 1Q19, UOB recorded the strongest 3% sequential loan expansion, whilst DBS and OCBC saw their loans growing <1% QoQ each. Weak housing loans was one key reason for the overall loan softness.
- Wealth management income recorded good sequential expansion.** This came on market sentiment recovery. The recovery was commendable, with DBS hitting a 44% growth, OCBC 52% expansion and UOB's 19% (all sequential growth rates).
- DBS, effective from FY19, will pay quarterly dividends** so as to provide shareholders with a more regular income stream. For 1Q19, DBS declared DPS of SGD0.30. OCBC and UOB did not declare dividends for 1Q19.
- Maintain BUYs on DBS and UOB.** DBS' SGD30.80 TP is pegged to 1.50x 2020F P/BV, which is derived from long-term ROE assumption of 13.8% vs 1Q19's 14%. UOB's SGD30.80 TP is based on 1.29x 2020F P/BV, after we set long-term ROE assumption at 12.5% vs 1Q19's 11.4%. We see NII expansion and lower CIR from digitisation driving ROE over the next few years. Amongst the three banks, DBS should gain the most from the higher Singapore Interbank Offered Rate (SIBOR), whilst UOB is less exposed to Greater China, and therefore, more insulated from the US-China trade developments. On a side note, it is a coincidence that the TPs for both banks are SGD30.80.
- Downside risks to our forecasts** include higher impairment charges, and a fall in the US Federal funds rate, which could dampen NIM.

Top Picks

UOB (UOB SP) – BUY
 DBS (DBS SP) – BUY

Target Price

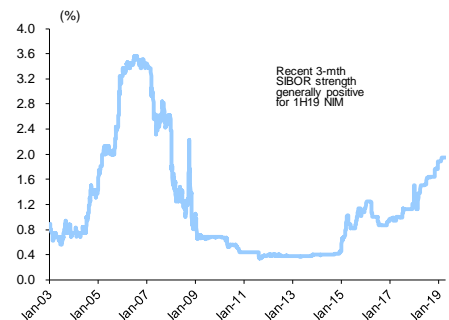
SGD30.80
 SGD30.80

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SIBOR firmness is positive for NIM expansion



Source: Bloomberg

Company Name	Rating	TP (SGD)	% Upside (Downside)	P/E (x) Dec-19F	P/B (x) Dec-19F	Yield (%) Dec-19F
DBS	BUY	30.80	16.0	11.2	1.38	4.5
OCBC	NEUTRAL	12.20	7.1	10.4	1.11	3.9
UOB	BUY	30.80	20.3	10.1	1.14	5.1

Source: Company data, RHB

NIM trend

DBS guides for 5-6bps NIM expansion in 2019. DBS' 1Q19 NIM of 1.88% was 1bp wider QoQ and 5bps wider YoY. Asset yields rose 8bps QoQ, whilst cost of funds climbed 7bps QoQ. Management maintained expectations of 2019 NIM expansion, guiding for a 5-6bps widening from 2018's 1.85%. DBS indicated 60% of loans were repriced in the first year of interest rate (eg SIBOR) rise, but another 40% repriced within the next two years. We forecast DBS' 2019 NIM of 1.9%.

OCBC's QoQ NIM widened the most amongst peers. 1Q19 NIM of 1.76% was 4bps wider QoQ and 9bps wider YoY. The YoY increase was due to higher asset yields and hike in gapping income from money market placements. Loan repricing contributed to the QoQ NIM widening. Management guided for 2019 NIM to be ~5bps wider than 2018's 1.7%, and sees 2Q19 NIM being higher QoQ. We forecast 2019 OCBC NIM of 1.76%.

UOB guided for flat 2019 NIM. 1Q19 NIM of 1.79% was 1bps narrower QoQ and 5bps lower YoY. Sequentially, whilst Singapore NIM was unchanged at 1.49%, Malaysia NIM contracted 2bps to 1.99%. UOB was more aggressive in its fixed deposit expansion due to net stable funding ratio (NSFR), but will likely run off part of it as loans slowed in subsequent months. Management guided for 2019 NIM to be unchanged from 2018's 1.82%, which factors in UOB's intention to defend its mortgage market share amidst competition.

Figure 1: OCBC's 1Q19 NIM widened the most QoQ

Net Interest Margin	DBS	OCBC	UOB
FY16	1.80%	1.67%	1.71%
FY17	1.75%	1.65%	1.77%
1Q18	1.83%	1.67%	1.84%
2Q18	1.85%	1.67%	1.83%
3Q18	1.86%	1.72%	1.81%
4Q18	1.87%	1.72%	1.80%
FY18	1.85%	1.70%	1.82%
1Q19	1.88%	1.76%	1.79%
FY19F	1.90%	1.76%	1.83%
FY20F	1.93%	1.80%	1.85%

Source: Company data, RHB

2019 loan growth guidance of mid-single digit

DBS maintained its Singapore home mortgage market share at 31% despite 1Q19 housing loans declining 1% QoQ. Management guided for SGD1-1.5bn of mortgage growth for 2019 vs SGD1.7bn rise in 2018. The non-trade corporate lending pipeline remains strong. DBS maintained its 2019 loan growth guidance of mid-single digits – our forecast: 5% expansion.

OCBC's 1Q19 loans expanded 0.3% QoQ, with building & construction loans up by a robust 4% QoQ. We forecast 2019 loan growth of 4.5%.

UOB's 2019 loan growth guidance maintained at mid-single digit. With 1Q19 loans having expanded 3% QoQ, loan growth in the subsequent three quarters of 2019 is likely to be muted. Management said that the slowdown of new residential property launches will likely soften its mortgage book. We forecast 2019 loan expansion of 5%.

Figure 2: UOB's loan grew most in 1Q19

Loan QoQ% change	DBS	OCBC	UOB
1Q17	-1.0%	2.1%	1.5%
2Q17	1.5%	1.8%	-0.6%
3Q17	3.7%	1.6%	2.8%
4Q17	2.9%	2.3%	0.9%
1Q18	1.6%	4.1%	2.3%
2Q18	3.0%	2.3%	3.8%
3Q18	0.7%	1.7%	2.2%
4Q18	1.4%	0.5%	2.7%
1Q19	0.6%	0.3%	3.0%

Source: Company data

Figure 3: Management guided for mid-single digit 2019 loan growth

Loan growth (YoY%)	DBS	OCBC	UOB
FY16	6.4%	4.1%	8.9%
FY17	7.2%	8.0%	4.7%
FY18	6.8%	9.0%	11.4%
FY19F	5.0%	4.5%	5.0%
FY20F	5.0%	5.5%	4.5%
FY21F	6.0%	5.8%	5.5%

Source: Company data, RHB

Figure 4: Housing, building & construction are two major loan segments

	DBS	OCBC	UOB
1Q19 L&A Breakdown	100.0%	100.0%	100.0%
- Transportation, Storage & Comms	8.8%	5.3%	4.0%
- Building & Construction	21.7%	21.5%	24.9%
- Manufacturing	11.6%	6.8%	8.7%
- Financial Institutions	6.4%	8.2%	8.6%
- General Commerce	13.3%	13.3%	12.5%
- Professionals & Pte Individuals	9.0%	11.6%	10.8%
- Housing	21.2%	24.6%	25.5%
- Others	8.1%	8.7%	5.0%

Source: Company data

Non-II

DBS' wealth management fees surged QoQ. Wealth management, brokerage, and investment banking fee income fell 12% YoY due to high 1Q18 base from an exceptionally buoyant market sentiment during that period. However, on a sequential basis, wealth management fee income rose 44% from a recovery in market sentiment.

OCBC's wealth management income surged 52% QoQ to SGD921m, driven by higher insurance and private banking income. Bank of Singapore's AUM rose 6% QoQ to USD108bn. We are positive on wealth management income's continued growth going forward.

UOB's 1Q19 wealth management income saw 19% QoQ growth, as the stabilisation of macroeconomic outlook led to improved customer confidence. Management guided for 2019 wealth management income growth of c.5%. The sequential doubling of net trading income is another key contributor to non-ll expansion.

Figure 5: Fee & commissions showed 1Q19 sequential recovery

Fee & Commissions QoQ % change	DBS	OCBC	UOB
1Q17	29.1%	14.5%	-17.3%
2Q17	-4.4%	2.3%	2.1%
3Q17	7.7%	-0.8%	6.5%
4Q17	-7.2%	0.6%	6.7%
1Q18	17.0%	9.2%	1.6%
2Q18	-5.1%	-3.4%	-3.7%
3Q18	-1.6%	-3.1%	-2.8%
4Q18	-8.6%	-5.6%	-3.3%
1Q19	15.0%	4.4%	2.4%

Source: Company data

Expenses

DBS 1Q19 CIR was stable vs 1Q18. 1Q19 expenses rose 7% YoY, driven mainly by a 9% increase in staff costs. Total income expansion led to stable CIR.

OCBC recorded a sharp improvement in 1Q19 CIR, as total income rose a strong 15% YoY whilst expenses rose a milder 6%.

UOB management guided for CIR to be c.44% for 2019. 1Q19 CIR was 44.6% vs 1Q18's 44.2% as total expenses rose 9% YoY due to higher performance-related staff costs and IT-related expenses.

Figure 6: We expect CIR to fall in 2019 (vs 2018)

CIR (%)	DBS	OCBC	UOB
FY17	43.0%	42.4%	43.7%
1Q18	41.6%	44.2%	44.2%
2Q18	44.3%	41.9%	43.6%
3Q18	43.9%	42.0%	43.4%
4Q18	46.3%	45.9%	44.4%
FY18	44.0%	43.4%	43.9%
1Q19	42.2%	40.9%	44.6%
FY19F	42.7%	42.8%	43.8%

Source: Company data, RHB

Allowances

OCBC's 1Q19 specific credit cost of 32bps was sharply higher than 1Q18's 2bps. The majority of 1Q19 allowances were for loans to oil and gas support vessels and services (ie OSVs), which were already classified as NPLs. Despite the recovery in fuel oil prices, the OSV sector did not see a corresponding increase in vessel employment or rise in charter rates.

Figure 7: Higher 1Q19 SP credit cost for OCBC

SP credit cost (bps)	DBS	OCBC	UOB
FY16	38	23	45
FY17	72	62	61
1Q18	20	2	12
2Q18	12	5	11
3Q18	21	14	15
4Q18	25	34	22
FY18	19	14	15
1Q19	15	32	13

Source: Company data

Dividend

Effective from FY19, DBS will pay dividends four times a year instead of two – this is to provide shareholders with more regular income streams. For 1Q19, DBS declared DPS of SGD0.30.

Both OCBC and UOB did not declare dividends for 1Q19.

ROE trend

Our long-term DBS ROE assumption is 13.8%. 1Q19 ROE was at 14% – the highest in more than a decade. It was even higher than 1Q18's 13.1%. Management guided that a 13% short-term ROE may be likely. We have assumed 13.8% long-term ROE, as we factor in gains from DBS' digitisation efforts.

Our long-term OCBC ROE assumption is 12%. 1Q19 ROE was at 12%, as there were significant gains from net trading income. We do not assume these gains can be sustained. On the other hand, digitisation efforts should help to improve efficiency. Overall, we have assumed long-term ROE of 12%.

Our long-term UOB ROE assumption is 12.5%. 1Q19 ROE was at 11.4%. We have assumed 12.5% long-term ROE, as we factor in gains from digitisation efforts.

Valuation

Figure 8: Peer valuation

Name		DBS	OCBC	UOB
Price @	10-May-19	26.55	11.39	25.61
Local	Curr	SGD	SGD	SGD
Mkt Cap (\$m)	(SGD)	67,922	48,438	42,706
	(USD)	49,844	35,546	31,339
PE (x)	Hist	11.9	10.5	10.5
	Curr	10.9	10.2	10.2
	Fwd	10.1	9.4	9.5
P/BV	(x)	1.31	1.09	1.14
ROE	(%)	11.5	11.1	11.3
ROA	(%)	1.1	1.0	1.1
Yield	(%)	4.5	3.8	3.9
YTD TR	(%)	14.5	3.1	7.1
1-m TR	(%)	0.6	(0.9)	(1.0)
3-m TR	(%)	11.6	1.1	4.2
6-m TR	(%)	14.3	1.3	6.7
1-y TR	(%)	(3.8)	(8.7)	(7.6)

Source: Bloomberg data

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