

19 April 2024

Financial Services | Banks

Public Bank (PBK MK)

Buy (from Neutral)

Time For Quality, Defensive Names To Shine?

- **Upgrade to BUY from Neutral, new MYR4.80 TP from MYR4.70, 16% upside with c.5% FY24F yield.** We believe recent events such as the escalation of tensions in the Middle East and shift in US Federal Funds (FFR) rate expectations, coupled with the upcoming US presidential election will likely lead to increased market volatility. Amid such a scenario, we are tactically upgrading our call for Public Bank as we see room for a big-cap, defensive, quality name in investors' portfolios to tide through the volatility. Fundamentally, the group's growth prospects have not changed, in our view.
- **Five reasons for our upgrade:** i) Earnings safety. PBK's domestic-driven earnings with stable drivers offer investors good earnings predictability; ii) the stock's underperformance vs FBM KLCI by 9% YTD. Focus could turn to laggards as volatility rises; iii) valuations – PBK is trading at 11.6x 2024F PE and 1.4x 2024F P/BV, ie close to the mid-point of -1SD and -2SD levels; iv) low foreign shareholding – this is now at 25.4% vs the recent multi-year low of 25.1% at end-Oct 2023; and v) it being a liquid, big-cap stock.
- **Loan demand – so far, so good on the consumer front.** PBK had guided for 2024 loan growth of 5-6%, with key drivers being housing loans (c. 6%), auto (5-6%) and SME (mid-single digit rate). We understand that growth for mortgages is holding up well, backed by a solid approval pipeline that is up c.7% YoY at end-2023. Meanwhile, auto loans have been well supported by the robust TIV YTD (2M TIV: +13% YoY), but management was unsure how long this can be sustained. PBK thinks the demand for big-ticket items has been partly buoyed by improved sentiment, as well as factors such as pent-up demand for properties. For SMEs, PBK is now more comfortable to grow the segment at a faster clip (2023 SME loan growth: +1% YoY) but stressed this would not be at the expense of asset quality.
- **NIM pressure – a slow burn?** New mortgage rates remain competitively priced in the market, at 3.8-4%. Similarly, given that most banks are focused on the SME segment, PBK said pricing in this segment has also been competitive. However, the impact to yields and NIMs will not be immediate but, instead, felt over time unlike deposit price competition. That said, deposit price discipline seems to have held up. PBK had reduced its promotional and board fixed deposit (FD) rates by 5-10bps in March and saw some peers similarly lower their FD rates. PBK guided for a stable-to-single-digit NIM squeeze, which it has kept to for now.
- **Asset quality – domestic segment still holding up** while the Hong Kong book has stabilised. That said, there has been some uptick in GIL from Vietnam, but the book there is small. While asset quality has remained intact, the recent global situation is likely to push back any potential provision writebacks.
- **Earnings forecasts broadly retained.** However, we raise our TP to MYR4.80 from MYR4.70 after ascribing a new 2% ESG premium (vs 2% discount previously) following an update to our ESG scorecard post-release of PBK's Sustainability Report 2023.

Forecasts and Valuation	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Reported net profit (MYRm)	6,119	6,649	6,920	7,237	7,525
Net profit growth (%)	8.2	8.7	4.1	4.6	4.0
Recurring net profit (MYRm)	6,119	6,649	6,920	7,237	7,525
Recurring EPS (MYR)	0.32	0.34	0.36	0.37	0.39
BVPS (MYR)	2.59	2.82	2.98	3.15	3.32
DPS (MYR)	0.17	0.19	0.20	0.21	0.22
Recurring P/E (x)	13.13	12.09	11.61	11.10	10.68
P/B (x)	1.60	1.47	1.39	1.31	1.25
Dividend Yield (%)	4.1	4.6	4.8	5.1	5.3
Return on average equity (%)	12.4	12.7	12.3	12.2	12.0

Source: Company data, RHB

Target Price (Return):	MYR4.80 (+16%)
Price (Market Cap):	MYR4.14 (USD16,843m)
ESG score:	3.1 (out of 4)
Avg Daily Turnover (MYR/USD)	74.6m/13.6m

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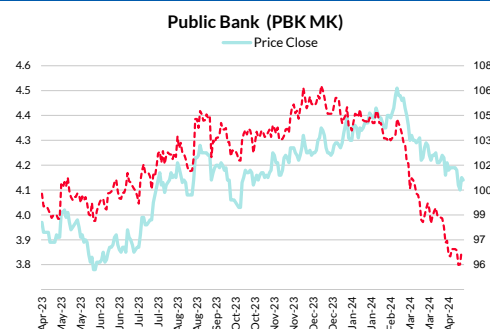


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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(3.5)	(3.5)	(4.0)	(0.7)	4.0
Relative	(9.4)	(2.6)	(8.1)	(7.2)	(3.5)
52-wk Price low/high (MYR)				3.78	4.51



Source: Bloomberg

Overall ESG Score: 3.1 (out of 4)

E: GOOD

Total emissions in 2023 eased 3% YoY due to a reduction in Scope 3 emissions relating to employee commuting. PBK's commitments include achieving a carbon-neutral position by 2030, and net-zero carbon by 2050. It has mobilised MYR54bn of sustainable finance since 2020, which includes MYR38bn for energy-efficient vehicle financing, MYR8bn for affordable homes financing, MYR5bn of corporate loans and MYR2bn under green financing facilities.

S: EXCELLENT

PBK offers affordable rates to first-time homebuyers under its PB First Home Loan initiative. It embraces gender diversity, with 49% of women in at the senior management level and 44% of women in the Board of Directors. It has a low staff attrition rate of 9.5%.

G: EXCELLENT

It has not had any material data security or privacy issues over the past few years. The Board of Directors is decently diverse, with well-defined roles and responsibilities for each member. Board members, senior management, and employees undergo training on matters of compliance, good governance and banking best practices.

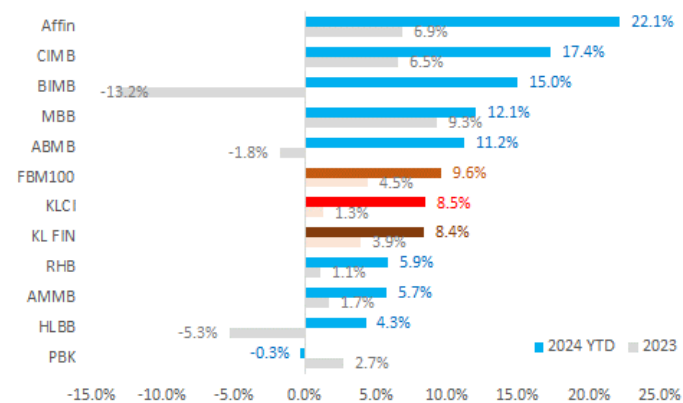
Financial Exhibits

Asia	Financial summary (MYR)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Malaysia	EPS	0.32	0.34	0.36	0.37	0.39
Financial Services	Recurring EPS	0.32	0.34	0.36	0.37	0.39
Public Bank	DPS	0.17	0.19	0.20	0.21	0.22
PBK MK	BVPS	2.59	2.82	2.98	3.15	3.32
Buy						
Valuation basis	Valuation metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
GGM-derived intrinsic value with an ESG overlay. Key GGM assumptions are:	Recurring P/E (x)	13.13	12.09	11.61	11.10	10.68
i. COE of 9.0%;	P/B (x)	1.6	1.5	1.4	1.3	1.2
ii. ROE of 12.25%;	Dividend Yield (%)	4.1	4.6	4.8	5.1	5.3
iii. 3.5% long-term growth.						
Key drivers	Income statement (MYRm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Our earnings are most sensitive to changes in:	Interest income	18,229	22,083	22,946	24,035	25,089
i. net interest margin;	Interest expense	(7,205)	(11,467)	(11,983)	(12,624)	(13,242)
ii. credit cost;	Net interest income	11,024	10,617	10,963	11,412	11,848
iii. non-interest income growth.	Non interest income	2,414	2,476	2,690	2,851	2,994
	Total operating income	13,438	13,093	13,654	14,263	14,842
	Overheads	(4,235)	(4,415)	(4,591)	(4,775)	(4,966)
	Pre-provision operating profit	9,203	8,678	9,062	9,488	9,876
	Loan impairment allowances	(366)	(157)	(210)	(230)	(248)
	Other impairment allowances	(13)	(1)	-	-	-
	Income from associates	7	19	20	20	20
	Pre-tax profit	8,831	8,539	8,872	9,278	9,648
	Taxation	(2,661)	(1,884)	(1,952)	(2,041)	(2,123)
	Minority interests	(50)	(6)	-	-	-
	Reported net profit	6,119	6,649	6,920	7,237	7,525
	Recurring net profit	6,119	6,649	6,920	7,237	7,525
Key risks						
Downside risks include:	Profitability ratios	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
i. weaker-than-expected NIMs;	Return on average assets (%)	1.3	1.3	1.3	1.3	1.3
ii. sharper-than-expected deterioration in asset quality;	Return on average equity (%)	12.4	12.7	12.3	12.2	12.0
iii. weaker-than-expected non-interest income.	Return on IEAs (%)	3.9	4.5	4.5	4.5	4.5
	Cost of funds (%)	1.7	2.6	2.7	2.7	2.7
	Net interest spread (%)	2.2	1.9	1.8	1.8	1.8
	Net interest margin (%)	2.4	2.2	2.1	2.1	2.1
	Non-interest income / total income (%)	18.0	18.9	19.7	20.0	20.2
	Cost to income ratio (%)	31.5	33.7	33.6	33.5	33.5
	Credit cost (bps)	9.95	4.04	5.12	5.31	5.47
Company Profile	Balance sheet (MYRm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Public Bank is Malaysia's third largest banking group by assets. The group also has overseas operations in Cambodia, Vietnam, Laos and Hong Kong.	Total gross loans	376,892	398,997	422,630	443,507	463,235
	Other interest earning assets	103,158	97,860	101,991	106,301	110,799
	Total gross IEAs	480,050	496,856	524,621	549,808	574,034
	Total provisions	(4,309)	(4,247)	(4,314)	(4,407)	(4,524)
	Net loans to customers	372,583	394,750	418,317	439,100	458,711
	Total net IEAs	475,741	492,610	520,307	545,401	569,510
	Total non-IEAs	17,522	17,988	16,821	17,445	17,770
	Total assets	493,263	510,598	537,128	562,846	587,281
	Customer deposits	394,719	412,897	435,606	457,387	477,969
	Other interest-bearing liabilities	32,889	26,956	27,184	27,384	27,478
	Total IBLs	427,608	439,853	462,790	484,771	505,447
	Total non-IBLs	14,129	14,365	14,788	15,233	15,700
	Total liabilities	441,737	454,218	477,578	500,003	521,148
	Share capital	9,418	9,418	9,418	9,418	9,418
	Shareholders' equity	50,179	54,674	57,844	61,137	64,427
	Minority interests	1,347	1,706	1,706	1,706	1,706
	Asset quality and capital	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Reported NPLs / gross cust loans (%)	0.4	0.6	0.6	0.6	0.6
	Total provisions / reported NPLs (%)	272.0	181.8	170.1	165.6	169.8
	CET-1 ratio (%)	14.7	14.7	15.2	15.4	15.6
	Tier-1 ratio (%)	14.8	14.7	15.2	15.4	15.6
	Total capital ratio (%)	17.8	17.6	18.0	18.1	18.2

Source: Company data, RHB

Reasons For Our Tactical Call Upgrade

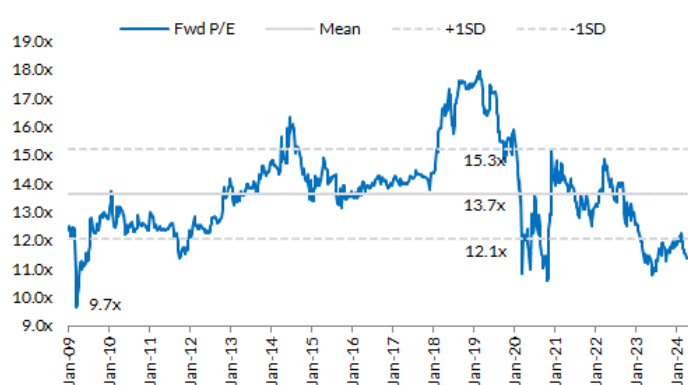
Figure 1: PBK has been a laggard YTD – the potential reason being the muted ROE it sees ahead ,due to income growth pressures



Note: Data as at 12 Apr 2024

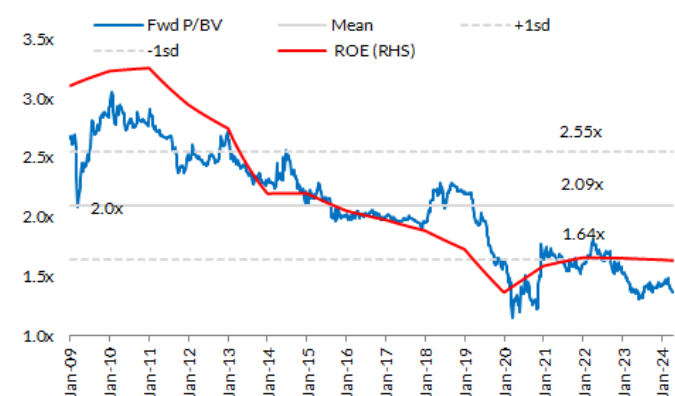
Source: Bloomberg, RHB

Figure 2: Consequently, valuations have stayed depressed, with both the 12-month forward consensus P/E ...



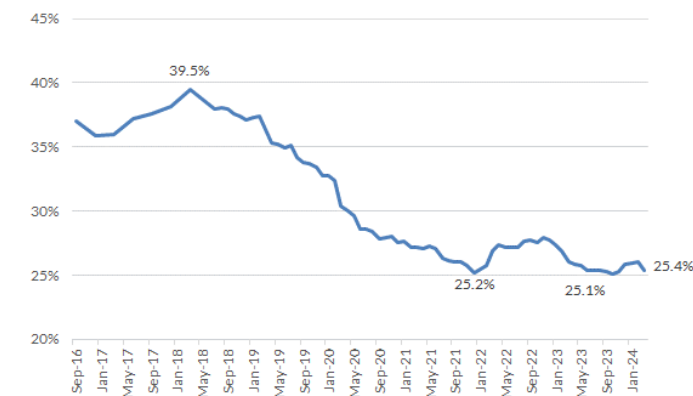
Source: Bloomberg, RHB

Figure 3... and 12-month forward consensus P/BV being at the mid-point between the -1SD and -2SD levels



Source: Bloomberg, RHB

Figure 4: PBK's current foreign shareholding level is also depressed, but appears to be stabilising. This could help cushion it against further selling pressure from foreign institutional investors



Source: Bloomberg, RHB

Revisions to estimates

We have fine-tuned our model for PBK, although the impact is insignificant. Our key assumptions on loans growth, NIM and credit cost are largely retained.

Figure 5: Revisions to our forecasts

	Previous FY24F	Previous FY25F	Previous FY26F	Revised FY24F	Revised FY25F	Revised FY26F	% Change FY24F	% Change FY25F	% Change FY26F
FYE Dec (MYRm)									
Net fund based income	10,984	11,383	11,763	10,963	11,412	11,848	-0.2%	0.3%	0.7%
Net fee based income	2,690	2,851	2,994	2,690	2,851	2,994	0.0%	0.0%	0.0%
Operating expenses	-4,591	-4,775	-4,966	-4,591	-4,775	-4,966	0.0%	0.0%	0.0%
PIOP	9,083	9,459	9,791	9,062	9,488	9,876	-0.2%	0.3%	0.9%
Impairment charges	-210	-230	-248	-210	-230	-248	0.0%	0.0%	0.0%
Pretax profit	8,893	9,249	9,563	8,872	9,278	9,648	-0.2%	0.3%	0.9%
Net profit	6,936	7,214	7,459	6,920	7,237	7,525	-0.2%	0.3%	0.9%
EPS (MYR)	0.36	0.37	0.38	0.36	0.37	0.39	-0.2%	0.3%	0.9%
DPS (MYR)	0.20	0.21	0.22	0.20	0.21	0.22	0.0%	0.0%	0.0%
Loan growth (%)	6.0	5.0	4.5	6.0	5.0	4.5			
NIM (%)	2.17	2.14	2.11	2.16	2.14	2.13			
CIR (%)	33.6	33.5	33.7	33.6	33.5	33.5			
Credit cost (bps)	5	5	5	5	5	5			

Source: Company data, RHB

Valuation and TP

All in, we raise our TP to MYR4.80 from MYR4.70. We tone down our sustainable ROE assumption to 12.25% from 12.5% for now, given potential sustained pressures on asset yields, which could spill over to NIMs as well. Consequently, our GGM-derived P/BV drops to 1.58x from 1.63x while our intrinsic value decreases to MYR4.71 (from MYR4.84).

The reduction in intrinsic value, however, is more than compensated by the revision to PBK's ESG score to 3.1 out of 4 from 2.9, which is above the country median of 3. This is post its recently released Sustainability Report 2023, with a key improvement in disclosure being the maiden reporting of financed emissions from its loan portfolio. This lead to it deserving a new 2% ESG premium applied to our intrinsic value, vs a 2% discount previously.

Figure 6: PBK – GGM valuation with ESG overlay

Cost of equity (COE) computation:		Sustainable ROE (%)	12.25
Risk free rate (%)	4.0	COE (%)	9.0
Equity premium (%)	5.2	Long-term growth (g)	3.5
Beta (x)	1.0	Implied P/BV (x)	1.58
Cost of equity - CAPM (%)	9.0	BVPS – 12-mth rolling forward	MYR2.98
		Intrinsic value	MYR4.71
ESG premium/(discount) (%)	2.0	ESG premium/(discount)	MYR0.09
		TP (rounded)	MYR4.80

Source: Company data, RHB

Emissions And ESG

Trend analysis

Public Bank's greenhouse gas emissions ticked down slightly YoY on a reduction in emissions relating to employee travel.

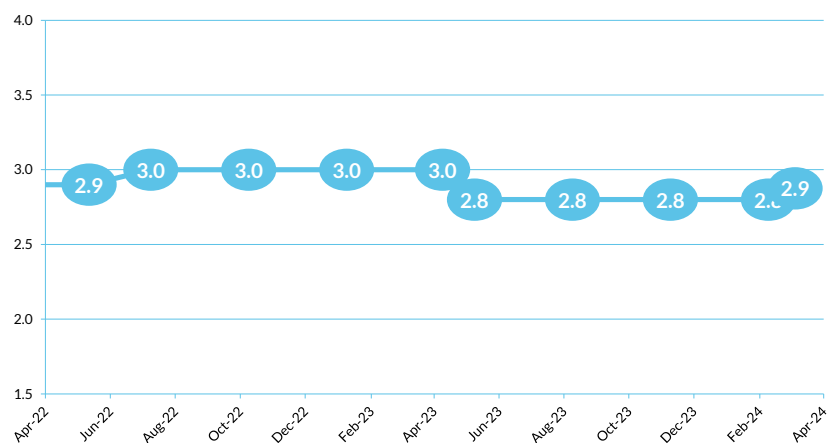
Emissions (tCO2e)	Dec-21	Dec-22	Dec-23
Scope 1	551	2,460	na
Scope 2	61,318	61,211	na
Scope 3	1,041	26,236	na
Total emissions	62,910	89,907	na

Source: Company data, RHB

Latest ESG-Related Developments

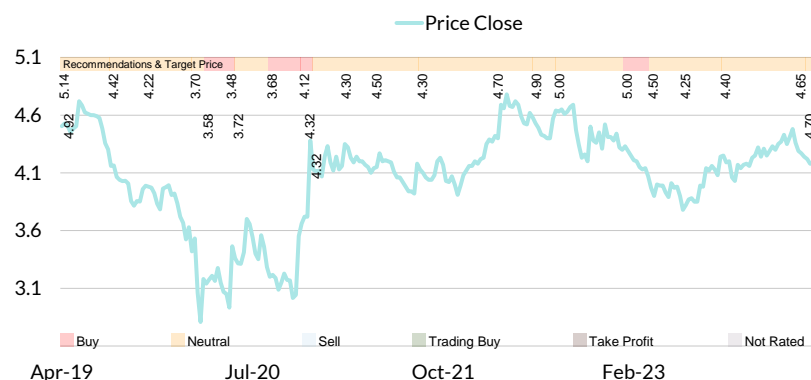
- **Raising sustainability commitments:** Public Bank raised its sustainable finance target to MYR100bn by 2030, from MYR48bn by 2025.
- **Government Guarantee Scheme Madani:** Public Bank is a participant of the Government's Government Guarantee Scheme Madani (GGSM), a scheme for extending government-guaranteed financing to SMEs with a focus on the high technology, agriculture, manufacturing and tourism sectors.
- **Financed emissions:** It has started to measure financed emissions from 81% of total loans, both domestic and overseas.

ESG Rating History



Source: RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2024-03-21	Neutral	4.70	4.22
2024-02-29	Neutral	4.65	4.40
2024-02-19	Neutral	4.40	4.43
2023-11-29	Neutral	4.40	4.24
2023-08-29	Neutral	4.40	4.14
2023-05-26	Neutral	4.25	3.90
2023-03-08	Neutral	4.50	4.11
2023-02-28	Buy	5.00	4.13
2023-01-04	Buy	5.00	4.28
2022-08-29	Neutral	5.00	4.63
2022-07-25	Neutral	5.00	4.62
2022-05-30	Neutral	4.90	4.59
2022-02-27	Neutral	4.70	4.37
2021-11-29	Neutral	4.30	3.96
2021-08-29	Neutral	4.30	4.18

Source: RHB, Bloomberg

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