

4 August 2022

Financial Services | Banks

OCBC Bank (OCBC SP)

Buy (Maintained)

1H22: Robust NIM Expansion, Benign Credit Cost

Target Price (Return): SGD13.90 (+16%)
 Price (Market Cap): SGD12.00 (USD39,072m)
 ESG score: 3.10 (out of 4)
 Avg Daily Turnover (SGD/USD) 66.3m/47.5m

- **Stay BUY and SGD13.90 TP, 16% upside and c.5% yield.** OCBC Bank's 1H22 results were broadly in line. More positive guidance on NIM and credit costs were tempered by our expectation of weaker non-Il, resulting in modest earnings upgrade. Still, we like that asset quality remains resilient, while exposure to China's troubled real estate sector is small, with no stress detected. Valuation is compelling, with P/BV of <1.0x vs improving ROEs of 10-12%.
- **1H22 within expectations.** Net profit of SGD2.84bn (+7% YoY) was at 53% and 52% of our and Street FY22F earnings. Reported ROAE rose to 11% (FY21: 9.6%). CET-1 stayed healthy, although lower at 14.9% (1Q22: 15.2%). A cash DPS of 28 SG cents was declared (1H21: SGD0.25), representing a 44% payout. In 2Q22, PIOP rose 13% QoQ, boosted mainly by the 13% QoQ jump in NII and moderate 4% QoQ rise in opex that lowered CIR to 43.5% (1Q22: 45.6%). Bottomline growth was moderated by the 64% QoQ increase in loan provisions, with loan credit cost at 8bps (1Q22: 6bps).
- **FY22 loan growth target tempered.** Management remains positive on FY22 outlook. Still, cognisant that headwinds from the Russia-Ukraine war, supply chain disruptions and recessionary risk have dented investor sentiment, loan growth guidance is tweaked to mid-single digit (from high-to-mid single digit). In our view, this is achievable given YTD-June growth of 3% or 6% annualised.
- **Sustained NIM in 2H22.** NIM expanded 26bps QoQ in 2Q22, a positive surprise with faster transmission of rising interest rates to improved asset yields. Notwithstanding the sharp increases in interest rates since mid-June, management expects NIM to stay at 2Q22 level of 1.81%. The guidance is conservative as management expects a further shift in CASA deposits to fixed deposits, while competition for fixed deposits would also push funding costs higher.
- **No asset quality stress.** Non-performing assets (NPA) fell 8% QoQ, helped by recoveries (namely oil & gas NPLs) and an upgrade of accounts in Malaysia and Indonesia where borrowers exited relief assistance. This lowered NPL ratio to 1.3% (1Q22: 1.4%), while NPA coverage is a higher 99% (1Q22: 91%). OCBC has c.SGD2.0bn exposure to China's real estate sector. With most borrowers being network clients, and exposure to uncompleted projects small, management does not see any structural concerns. Credit cost guidance remains conservative (lower end of 20-25bps) as external headwinds may mean normalised provisions, and the need for additional overlays in 2H22.
- **Earnings and TP.** Our FY22F-24F earnings are raised by 3-4%. Assumptions of better NIM and lower credit cost are partly offset by downward revision in non-Il (Figure 3). Our unchanged SGD13.90 TP is based on an GGM-derived intrinsic value of SGD13.61 and a 2% ESG premium, based on our in-house ESG methodology (Figure 4).

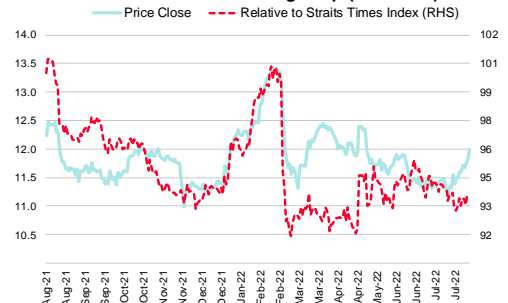
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	5.2	6.1	(3.2)	(6.3)	(2.1)
Relative	1.5	1.5	0.3	(4.0)	(5.0)
52-wk Price low/high (SGD)	11.0 – 13.4				

Oversea-Chinese Banking Corp (OCBC SP)



Source: Bloomberg

Overall ESG Score: 3.10 (out of 4)

E: GOOD

OCBC has a sustainability framework that aligns the bank's approach to creating a positive social and environmental impact in line with the global sustainable development agenda. It has a responsible lending framework, and is working towards enhancing the integration of climate-related considerations into its ESG Risk Assessment processes by 2022. In 2020, OCBC developed a new Responsible Investing Policy to integrate ESG considerations into the bank's investment decisions. It aims to build a sustainable finance portfolio of SGD50bn by 2025 (2021: SGD34bn).

S: GOOD

OCBC aims to maintain a balanced gender mix across its workforce, with 42% of women in leadership positions by 2022. In 2020, women accounted for 59% of total employees, 39% in leadership positions, and 20% in the board of directors. OCBC is active in talent management, and places health, safety and wellbeing of staff at the top of its priorities as an employer.

G: EXCELLENT

OCBC is proactive in its approach to ensure resilience against risks of cyber-attacks, data breaches, fraud and money laundering. That said, a highly sophisticated phishing scam in Dec 2021 has highlighted the need for enhanced security measures.

Forecasts and Valuation	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Reported net profit (SGDm)	3,586	4,858	5,520	6,496	7,063
Net profit growth (%)	(26.4)	35.5	13.6	17.7	8.7
Recurring net profit (SGDm)	3,586	4,858	5,520	6,496	7,063
Recurring EPS (SGD)	0.81	1.09	1.23	1.45	1.58
BVPS (SGD)	11.09	11.72	12.36	13.18	14.07
DPS (SGD)	0.32	0.53	0.58	0.63	0.68
Recurring P/E (x)	14.84	11.04	9.72	8.26	7.59
P/B (x)	1.08	1.02	0.97	0.91	0.85
Dividend Yield (%)	2.6	4.4	4.8	5.3	5.7
Return on average equity (%)	7.4	9.5	10.3	11.4	12.4

Source: Company data, RHB

Financial Exhibits

Asia	Financial summary (SGD)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Singapore	EPS	0.81	1.09	1.23	1.45	1.58
Financial Services	Recurring EPS	0.81	1.09	1.23	1.45	1.58
OCBC Bank	DPS	0.32	0.53	0.58	0.63	0.68
OCBC SP	BVPS	11.09	11.72	12.36	13.18	14.07
Buy						
	Valuation metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Recurring P/E (x)	14.84	11.04	9.72	8.26	7.59
	P/B (x)	1.1	1.0	1.0	0.9	0.9
	Dividend Yield (%)	2.6	4.4	4.8	5.3	5.7
	Income statement (SGDm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Interest income	9,143	7,425	8,655	11,150	11,981
	Interest expense	(3,177)	(1,570)	(1,930)	(3,650)	(3,930)
	Net interest income	5,966	5,855	6,725	7,500	8,051
	Non interest income	4,173	4,741	4,604	5,015	5,329
	Total operating income	10,139	10,596	11,329	12,514	13,380
	Overheads	(4,543)	(4,867)	(5,060)	(5,408)	(5,708)
	Pre-provision operating profit	5,596	5,729	6,268	7,106	7,672
	Loan impairment allowances	(2,009)	(867)	(578)	(517)	(503)
	Other impairment allowances	(34)	(6)	(7)	(7)	(6)
	Income from associates	612	824	1,000	1,050	1,103
	Pre-tax profit	4,165	5,680	6,683	7,632	8,265
	Taxation	(437)	(648)	(968)	(916)	(967)
	Minority interests	(142)	(174)	(195)	(220)	(235)
	Reported net profit	3,586	4,858	5,520	6,496	7,063
	Recurring net profit	3,586	4,858	5,520	6,496	7,063
	Profitability ratios	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Return on average assets (%)	0.7	0.9	1.0	1.1	1.2
	Return on average equity (%)	7.4	9.5	10.3	11.4	12.4
	Return on IEAs (%)	2.6	2.1	2.3	2.8	3.0
	Cost of funds (%)	1.0	0.5	0.6	1.0	1.1
	Net interest spread (%)	1.6	1.6	1.7	1.8	1.9
	Net interest margin (%)	1.7	1.6	1.8	1.9	2.0
	Non-interest income / total income (%)	41.2	44.7	40.6	40.1	39.8
	Cost to income ratio (%)	44.8	45.9	44.7	43.2	42.7
	Credit cost (bps)	75.5	31.5	19.8	16.8	16.3
	Balance sheet (SGDm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Total gross loans	267,240	289,716	305,940	324,297	342,133
	Other interest earning assets	88,930	87,217	94,855	99,121	104,040
	Total gross IEAs	356,170	376,933	400,795	423,418	446,173
	Total provisions	(4,596)	(3,904)	(4,200)	(4,500)	(4,650)
	Net loans to customers	262,644	285,812	301,740	319,797	337,483
	Total net IEAs	351,574	373,029	396,595	418,918	441,523
	Total non-IEAs	169,821	169,158	177,400	186,379	195,206
	Total assets	521,395	542,187	573,995	605,297	636,729
	Customer deposits	314,907	342,395	361,227	382,900	402,811
	Other interest-bearing liabilities	9,586	8,239	13,200	13,596	13,949
	Total IBLs	324,493	350,634	374,427	396,496	416,761
	Total non-IBLs	145,726	137,215	142,298	147,802	154,898
	Total liabilities	470,219	487,849	516,725	544,299	571,658
	Share capital	19,031	19,238	19,238	19,238	19,238
	Shareholders' equity	49,622	52,663	55,512	59,178	63,186
	Minority interests	1,554	1,675	1,759	1,820	1,884
	Asset quality and capital	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Reported NPLs / gross cust loans (%)	1.5	1.5	1.4	1.4	1.4
	Total provisions / reported NPLs (%)	117.3	92.6	101.7	99.1	98.8
	CET-1 ratio (%)	15.8	16.0	15.6	15.7	16.2
	Tier-1 ratio (%)	15.8	16.0	15.6	15.7	16.2
	Total capital ratio (%)	17.9	17.6	17.0	17.0	17.5

Source: Company data, RHB

Results At a Glance

Figure 1: OCBC – summary of 2Q22 and 1H22 results

FYE 31 Dec (SGDm)	2Q21	1Q22	2Q22	QoQ (%)	YoY (%)	1H21	1H22	YoY (%)	Comments: 1H22 vs 1H21
Net interest income	1,461	1,503	1,700	13	16	2,902	3,203	10	Healthy YoY growth as NIM expanded 6bps YoY and loan growth of 8% YoY.
<i>NIM (%) – reported</i>	1.58%	1.55%	1.81%			1.57%	1.63%		NIM expanded mainly on improved asset yields.
Non-interest income	1,111	1,140	1,179	3	6	2,584	2,319	-10	
Net fee & commission income	563	522	477	-9	-15	1,148	999	-13	Down YoY as wealth management income fell 23% YoY, and brokerage & fund management income declined 16% YoY. These offset the 7% YoY rise in fees from loan, trade guarantees and remittances.
Income from insurance	254	330	423	28	67	724	753	4	Up YoY on higher operating profit and MTM gains in insurance funds.
Other non-interest income	294	288	279	-3	-5	712	567	-20	Down YoY on lower trading income (-7% YoY) and net loss of SGD18m from investment securities (1H21: 103m gain).
<i>Non-ll/total income (%)</i>	43.2%	43.1%	41.0%			47.1%	42.0%		
Operating income	2,572	2,643	2,879	9	12	5,486	5,522	1	
Overhead expenses	(1,138)	(1,205)	(1,253)	4	10	(2,287)	(2,458)	7	
<i>CIR (%)</i>	44.2%	45.6%	43.5%			41.7%	44.5%		
PIOP	1,434	1,438	1,626	13	13	3,199	3,064	-4	
Impairments charges	(257)	(69)	(99)	43	-61	(444)	(168)	-62	
<i>Annualised credit cost (bps)</i>	38	10	14			29	8		Annualised credit cost is materially lower than guidance of 20-25bps.
Operating profit	1,177	1,369	1,527	12	30	2,755	2,896	5	
Associates	213.0	254.0	245.0	-4		422.0	499.0		
Pre-tax profit	1,390	1,623	1,772	9	27	3,177	3,395	7	
Tax	(181)	(241)	(234)			(413)	(475)		
<i>Effective tax rate (%)</i>	13.0%	14.8%	13.2%			13.0%	14.0%		
Minorities	(49)	(26)	(57)	119	16	(103)	(83)	-19	
Net profit	1,160	1,356	1,481	9	28	2,661	2,837	7	
Other key data and ratios									
Gross loans	274,794	294,000	297,920	1	8				YTD growth of 3% or 6% annualised vs guidance of mid-to-high single digit growth;
Customer deposits	316,776	348,265	348,821	0	10				YTD growth of 2% or 4% annualised. CASA deposits dipped 2% YTD, lowering CASA ratio to 60.9% vs 63.3% in 4Q21.
Gross NPLs	3,991	4,189	3,849	-8	-4				Down QoQ as recoveries and loan upgrades offset new NPA formation.
Total assets	521,131	552,787	554,862	0	6				
Shareholders' funds	51,773	53,094	52,821	-1	2				
ROAA (%) - reported	1.11	1.23	1.31			1.27	1.27		
ROAE (%) - reported	9.3	10.6	11.5			10.8	11.0		
LDR (%)	85.6	83.3	84.4						
GIL ratio	1.49	1.46	1.29						
Loan loss coverage	103.8	90.7	101.6						
CET-1 ratio (%)	16.06	15.20	14.93						
Total capital ratio (%)	18.4	17.2	17.5						

Source: Company data, RHB

Management guidance

Figure 2: OCBC – management guidance and financial targets

	FY21 Actual	1H22 Achieved	FY22 Guidance	Comments
Loan growth	+8% YoY	+8% YoY	Mid-single digit (from mid-to-high single digit)	Management toned down loan growth guidance given the moderation in demand as sentiment is dampened by the macroeconomic headwinds.
NIM	1.54%	1.63%	1.81% in 2H22 (from 1.55-1.58%)	Guidance raised to reflect the rise in interest rates. While acknowledging that NIM could trend higher in 2H22, management conservatively guides that NIM would be unchanged at 2Q22's exit NIM of 1.81% would be sustained. A 100bps rise in interest rates would lift NII by SGD670m and NIM by 18bps.
Credit cost	29bps FY20-21: 96bps	7bps	Low end of 20-25bps guidance	This is refined from an earlier guidance of 20-25bps. Management expects recoveries and upgrade of accounts seen in 2Q22 would not be sustained in 2H22. The still challenging environment may also mean normalised provisions and the need for additional overlays.

Source: Company data, RHB

Revisions to earnings estimates

Our FY22F-24F earnings are raised by 3-4% as we pencilled in the following revisions:

- Higher NIM given the faster and sharper rise in interest rates;
- Lower credit costs;
- Lower non-II with continued weakness in financial markets expected to impact wealth fees and capital market related income.

We have also raised DPS estimates, taking into account the higher payout ratio in 1H22.

Figure 3: OCBC – revisions to earnings forecasts

FYE Dec	Previous FY22F	Previous FY23F	Previous FY24F	Revised FY22F	Revised FY23F	New FY24F	% Change FY22F	% Change FY23F	% Change FY24F
(SGDm)									
Net interest income	6,388	7,059	7,491	6,725	7,500	8,051	5%	6%	7%
Non-interest income	4,901	5,252	5,580	4,604	5,015	5,329	-6%	-5%	-5%
Operating expenses	(5,028)	(5,259)	(5,487)	(4,956)	(5,303)	(5,603)	-1%	1%	2%
PIOP	6,261	7,052	7,585	6,372	7,211	7,777	2%	2%	3%
Provision expenses	(762)	(716)	(734)	(689)	(629)	(614)	-10%	-12%	-16%
Pretax profit	6,519	7,407	7,975	6,683	7,632	8,265	3%	3%	4%
Net profit	5,318	6,335	6,807	5,454	6,496	7,063	3%	3%	4%
EPS (SGD)	1.18	1.40	1.51	1.21	1.44	1.56	3%	3%	4%
DPS (SGD)	0.53	0.60	0.62	0.58	0.63	0.68	9%	5%	10%
Loan growth (%)	7.5	6.5	5.5	5.6	6.0	5.5			
NIM (%)	1.64	1.71	1.72	1.73	1.82	1.85			
CIR (%)	44.5	42.7	42.0	43.8	42.4	41.9			
Credit cost (bps)	22	19	18	19	16	15			

Source: Company data, RHB

Valuation and TP

Our TP is unchanged at SGD13.90, based on an intrinsic value of SGD13.61, with a 2% ESG premium applied, based on RHB’s in-house ESG methodology.

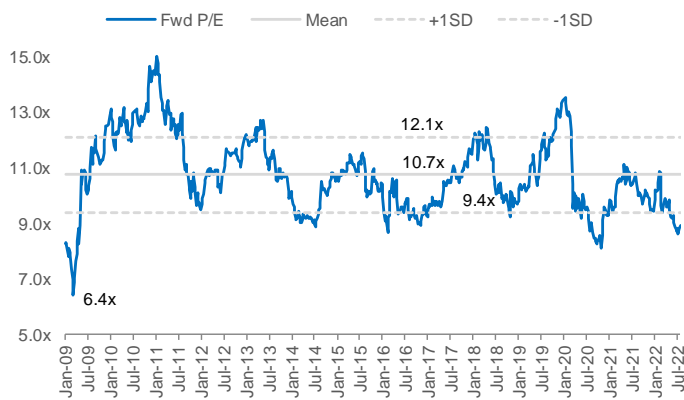
The intrinsic value is based on the GGM-derived P/BV of 1.05x, which is close to its historical mean of 1.1x.

Figure 4: OCBC – GGM valuation

Cost of equity (COE) computation:		Sustainable ROE (%)	10.50
Risk free rate (%)	2.65	COE (%)	10.11
Equity premium (%)	7.35	Long-term growth (g)	3.00
Beta (x)	1.02	Implied P/BV (x)	1.05
Cost of equity - CAPM (%)	10.11	Rolling 12-mth forward BVPS	SGD12.90
		Intrinsic value	SGD13.61
ESG premium/(discount) (%)	2.0	ESG premium/(discount)	SGD0.27
		TP (rounded)	SGD13.90

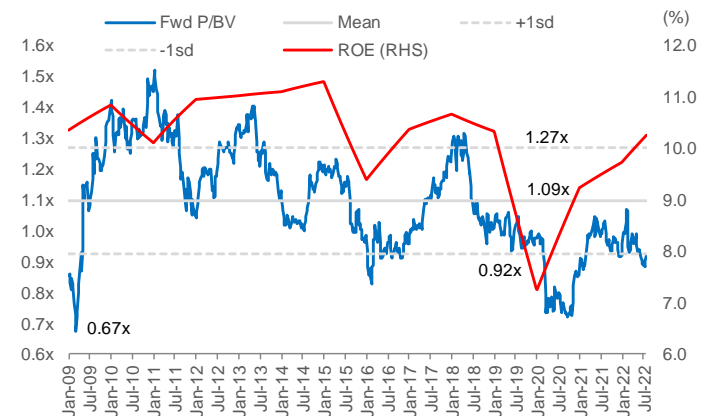
Source: Company data, RHB

Figure 5: OCBC’s 12-month forward consensus P/E



Source: Bloomberg, RHB

Figure 6: OCBC’s 12-month forward consensus P/BV



Source: Bloomberg, RHB

Recommendation Chart

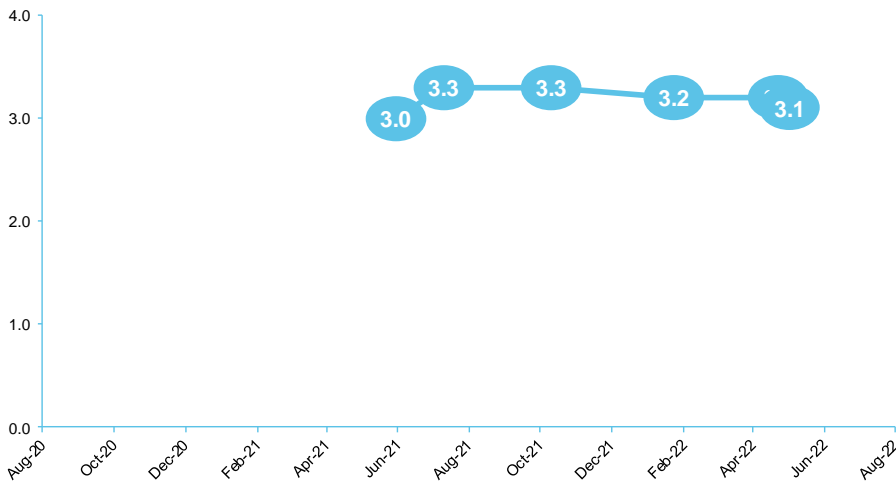


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-05-03	Buy	13.9	12.4
2022-02-24	Buy	14.4	12.0
2022-01-24	Buy	14.8	12.3
2021-11-04	Buy	15.1	11.9
2021-08-05	Buy	14.3	12.4
2021-05-09	Buy	14.3	12.6
2021-04-09	Buy	13.3	11.8
2021-02-25	Buy	12.5	11.1
2020-11-06	Neutral	9.5	8.9
2020-08-10	Neutral	8.7	8.7
2020-05-08	Neutral	8.7	8.9
2020-04-22	Neutral	9.0	8.6
2020-03-17	Neutral	9.6	8.6
2020-02-23	Neutral	11.2	11.0
2019-11-05	Neutral	11.5	11.1

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
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