

22 April 2022

Financial Services | Banks

Bank Neo Commerce (BBYB IJ)

Buy

Digital Bank With Strongest Growth; Initiate BUY

- **Initiate BUY with a combined valuation per user and GGM-based IDR3,100 TP, 67% upside.** Our TP implies 4.1x-4.7x FY22-23F P/BV. Given Bank Neo Commerce's huge customer base, it should monetise digital loans easier vs peers. It intends to launch a digital lending unit and distribute IDR10-12trn in loans in 2022 (total loans as of Dec 2021: IDR4.3trn). Total deposits have more than doubled in the last one year, with digital deposits accounting for 53% of the total. Key risks: Inflation that may dampen loan demand, and also NPLs from digital lending spiking upwards.
- **The largest user base, to offer digital lending products.** BBYB is one of the fastest growing digital banks in the country. It owns Indonesia's most downloaded digital banking app, Neo+, which surpassed 20m users since the app's launch in Mar 2021. It had 15.8m registered users in February, with 8.5m accounts already funded. This large number of active and funded users should make it easier for BBYB to acquire digital loan customers.
- **Rapid deposit growth.** BBYB's initial strategy was to acquire customers by luring them with attractive deposit interest rates. This led to deposits more than doubling to IDR8.8trn as of Jan 2022 (Jan 2021: IDR3.8trn), with digital deposits accounting for 53% of the total. Meanwhile, the bank's customer acquisition cost remains lower than the market average, at USD4.00-5.00 per user (vs the market's USD7.00-10.00), despite its aggressive marketing strategy. This year, its growth strategy is more targeted, and focused towards increasing deposits from existing customers while also uplifting its monthly transaction volumes.
- **To launch Neo-loan in May.** BBYB plans to distribute IDR10-12trn in loans in 2022, of which the majority will come from digital lending. BBYB is gradually reducing its conventional pension loan exposure, and channelling loans to fintech companies and also through digital loans. Last November, the bank teamed up with Akulaku to launch its first digital loan product, DanaCicil, a cash-installment programme. Digital loans – which offer higher yields – are expected to account for 40-50% of loan disbursements.
- **Rights issue to boost capital, and a new strategic partner.** BBYB announced that it plans to issue up to 5bn new shares (53% of existing share base) in a rights offering in May, with the proceeds going toward strengthening core capital, credit disbursement, and other operational activities. Note that Akulaku gradually increased its stake in BBYB as the rights issue drew near.
- **Valuation.** We combined the GGM and valuation per user methods (with equal weighting) to derive our TP, using the following assumptions: Beta of 1.07x, risk premium of 4%, risk-free rate of 7%, and sustainable ROE of 15%. Also, the average valuation per user of its peers is at USD829.00.

Target Price (Return): IDR3,100 (+64%)
Price (Market Cap): IDR1,890 (USD1,239m)
ESG score: 3.00 (out of 4)
Avg Daily Turnover (IDR/USD) 121,860m/8.49m

Analysts

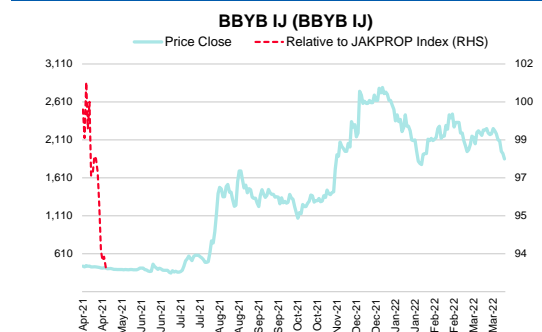
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(28.1)	(12.9)	(10.4)	48.5	330.5
Relative	(28.1)	(12.9)	(10.4)	48.5	329.4
52-wk Price low/high (IDR)				357 – 2,800	



Source: Bloomberg

Forecasts and Valuation	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Reported net profit (IDRb)	16	16	(234)	(306)	(108)
Net profit growth (%)	-	1.1	(1,578.6)	30.6	(64.7)
Recurring net profit (IDRb)	17	17	(233)	(304)	(106)
Recurring EPS (IDR)	3.27	2.84	(32.21)	(32.27)	(9.21)
BVPS (IDR)	160.11	167.07	415.49	742.53	648.64
DPS (IDR)	na	na	na	na	na
Recurring P/E (x)	578.79	666.35	na	na	na
P/B (x)	11.80	11.31	4.55	2.55	2.91
Dividend Yield (%)	na	na	na	na	na
Return on average equity (%)	2.1	1.6	(10.6)	(5.4)	(1.4)

Source: Company data, RHB

Overall ESG Score: 3.00 (out of 4)

E: GOOD

BBYB has applied the principle of responsibility to society and environment, and continuously carrying out CSR activities to participate in sustainable development.

S: GOOD

During the pandemic, company has provided personal protective equipment to health workers in carrying out their duties. More importantly, maintaining a healthy and safe working environments for its employees.

G: GOOD

Bank Neo Commerce is categorized into Rank 3 (BUKU III) or "quite good" in good corporate governance. The implementation weakness was on the fulfillment of BNC management, which management is committed to continuously improve.

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Financial Exhibits

Asia Indonesia Financial Services Bank Neo Commerce BBYB IJ Buy	Financial summary (IDR)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	EPS	2.95	2.62	(32.40)	(32.43)	(9.37)
	Recurring EPS	3.27	2.84	(32.21)	(32.27)	(9.21)
	BVPS	160.11	167.07	415.49	742.53	648.64
Valuation basis GGM with Beta of 1.92x, risk premium of 4%, risk-free rate of 6%, and sustainable ROE of 19%. Combined with valuation per customer method with a global average of USD975.00/customer.	Valuation metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Recurring P/E (x)	578.79	666.35	na	na	na
	P/B (x)	11.8	11.3	4.5	2.5	2.9
	Dividend Yield (%)	na	na	na	na	na
Key drivers i. Rapid user growth; ii. Release of digital lending products; iii. Additional transactional features.	Income statement (IDRb)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Interest income	532	435	722	1,023	1,464
	Interest expense	(316)	(277)	(413)	(621)	(717)
	Net interest income	216	158	310	403	746
Key risks i. Weaker purchasing power may dampen consumer loan demand; ii. Higher NPL from digital lending; iii. Competition from digital banks and fintech.	Non interest income	183	87	34	44	57
	Total operating income	398	245	344	446	803
	Overheads	(213)	(203)	(365)	(431)	(522)
	Pre-provision operating profit	185	43	(21)	15	281
Company Profile Bank Neo Commerce (BBYB IJ) was founded in 1989 as Bank Yudha Bhakti by the Ministry of Defence. The company shares were then acquired by Akulaku Silvr through a capital increase without pre-emptive rights by Akulaku Silvr (PMTHMETD), and began its transformation into a digital bank in 2019.	Loan impairment allowances	(164)	(1)	(206)	(303)	(337)
	Other impairment allowances	(2)	(25)	(31)	(50)	(62)
	Other exceptional items	(2)	(1)	(2)	(2)	(2)
	Pre-tax profit	18	16	(260)	(340)	(120)
	Taxation	(2)	0	25	34	12
	Reported net profit	16	16	(234)	(306)	(108)
	Recurring net profit	17	17	(233)	(304)	(106)
	Profitability ratios	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Return on average assets (%)	0.3	0.3	(2.9)	(2.2)	(0.6)
	Return on average equity (%)	2.1	1.6	(10.6)	(5.4)	(1.4)
	Return on IEAs (%)	11.6	9.1	9.8	7.6	8.0
	Cost of funds (%)	7.9	6.6	7.3	7.4	6.5
	Net interest spread (%)	3.7	2.5	2.5	0.2	1.4
	Net interest margin (%)	4.7	3.3	4.2	3.0	4.1
	Non-interest income / total income (%)	45.8	35.4	9.9	9.8	7.0
	Cost to income ratio (%)	53.5	82.7	106.1	96.6	65.0
	Credit cost (bps)	422	2	500	500	400
	Balance sheet (IDRb)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total gross loans	3,829	3,665	4,582	7,540	9,294
	Other interest earning assets	887	1,185	5,268	9,707	10,281
	Total gross IEAs	4,716	4,850	9,850	17,246	19,575
	Total provisions	(168)	(103)	(151)	(268)	(386)
	Net loans to customers	3,661	3,563	4,431	7,272	8,908
	Total net IEAs	4,548	4,747	9,699	16,978	19,189
	Total non-IEAs	577	674	781	904	1,046
	Total assets	5,124	5,421	10,480	17,882	20,235
	Customer deposits	4,066	3,943	6,749	9,474	11,951
	Other interest-bearing liabilities	84	321	305	289	275
	Total IBLs	4,150	4,264	7,054	9,763	12,226
	Total non-IBLs	28	36	35	33	31
	Total liabilities	4,178	4,301	7,088	9,796	12,257
	Share capital	868	1,017	3,522	8,522	8,522
	Shareholders' equity	909	1,071	3,341	8,035	7,927
	Asset quality and capital	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Reported NPLs / gross cust loans (%)	4.3	4.1	6.1	5.5	4.0
	Total provisions / reported NPLs (%)	259.2	356.3	242.2	229.3	358.0
	CET-1 ratio (%)	15.6	16.1	68.6	121.6	99.9
	Tier-1 ratio (%)	28.3	31.8	77.0	122.6	99.8
	Total capital ratio (%)	28.3	31.8	77.0	122.6	99.8

Source: Company data, RHB

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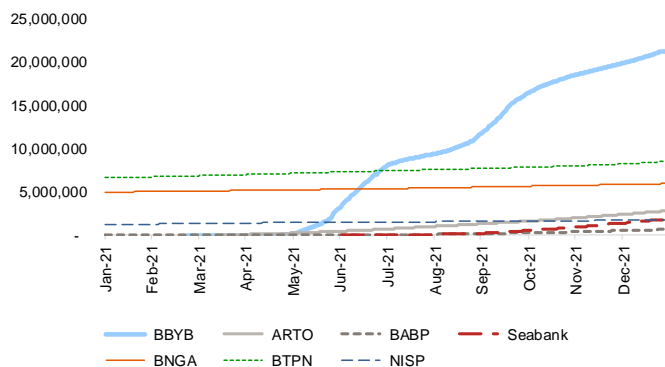
Investment Thesis

Rapid user growth

BBYB is one of the country's fastest growing digital banks. Since the company launched its new digital app, Neo+, in March 2021, total downloads have surpassed those of the incumbent digital banking apps, reaching more than 20m. In February, there were 15.8m registered users, with 8.5m accounts already funded.

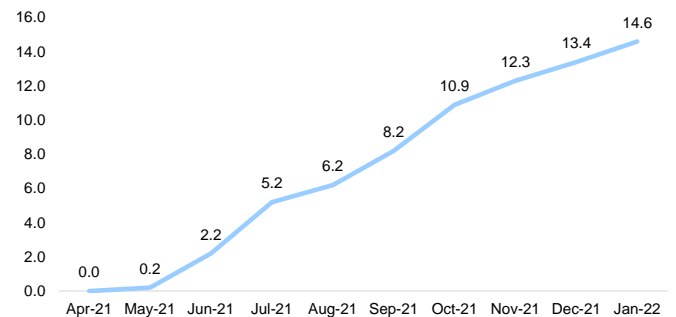
The user acquisition strategy has been effective, with an attractive deposit rate of up to 8% pa. Additionally, it has a referral programme that rewards IDR25,000 for each new customer. The majority of new users are organic. During our meeting, management said that just 10% of Neo+ users are Akulaku clients. In 2022, the business plans to add another 15m customers, and increase consumer stickiness with additional services.

Figure 1: Total downloads are outgrowing incumbent apps



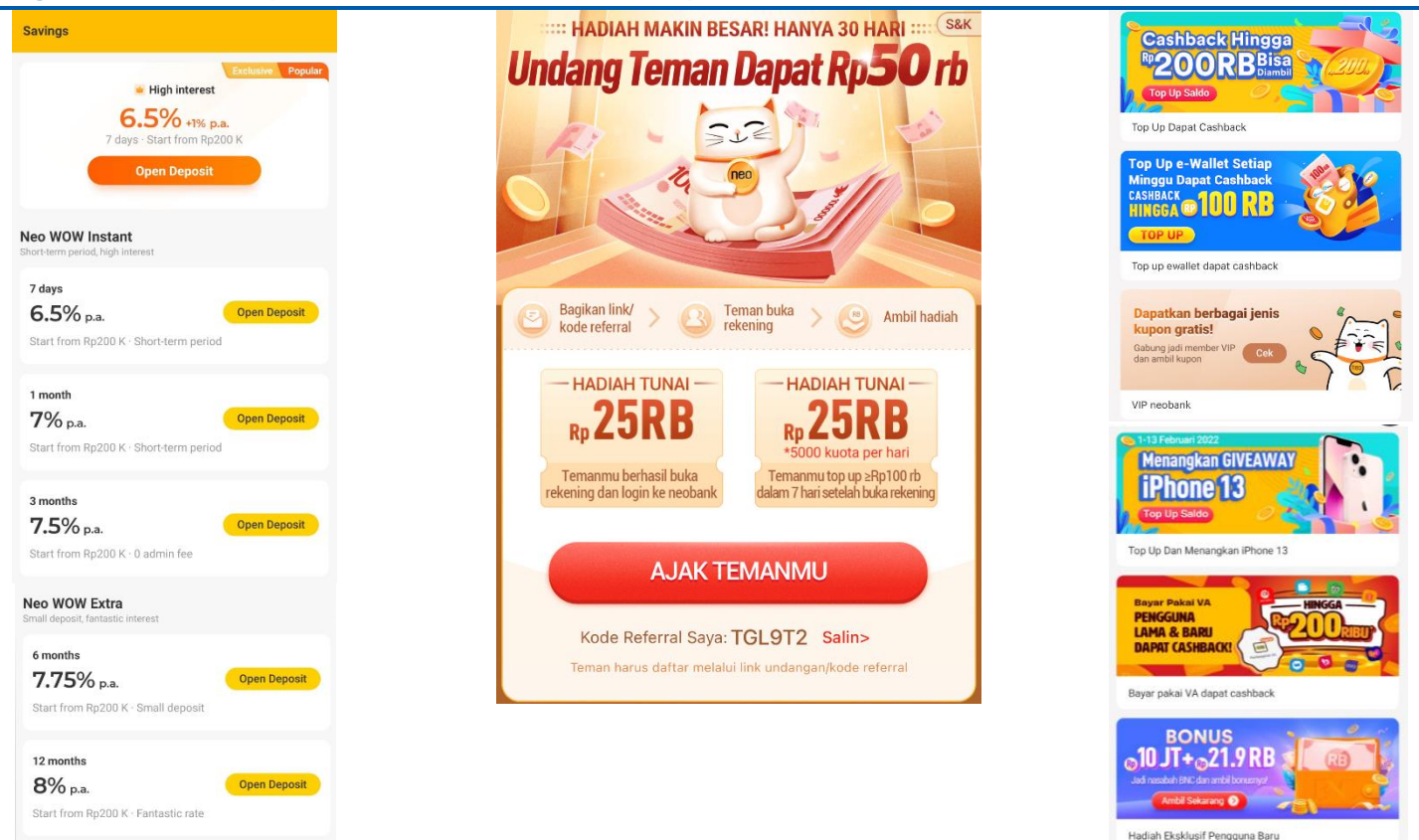
Source: App Annie, RHB

Figure 2: Neo+ registered users (m)



Source: Company data, RHB

Figure 3: Attractive deposit rates, referral bonus and other promotions



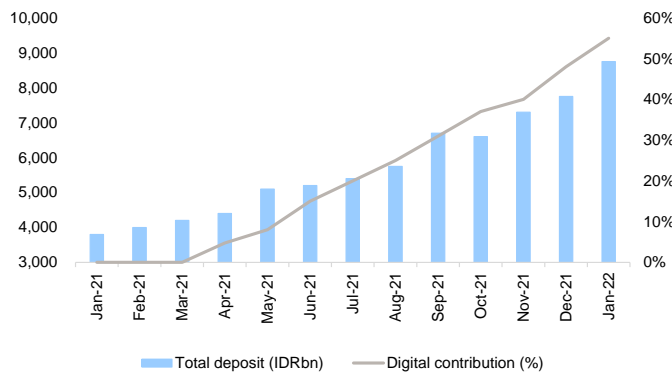
Source: Company data, RHB

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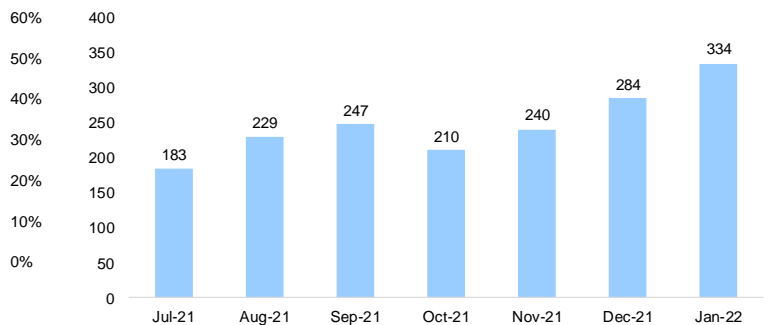
In Jan 2022, BBYB's total deposits had more than doubled to IDR8.8trn (Jan 2021: IDR3.8trn), with digital deposits accounting for 53% of the total. To increase the average deposit per user, the company launched a "VIP Membership" campaign in December, offering a free upgrade to active members who raise their balance above IDR500k. Despite its aggressive marketing strategy, BBYB's customer acquisition cost remains lower than the market average, at USD4.00-5.00 per user. Nonetheless, we believe this year's strategy is more targeted and focused, with the goal of increasing deposits from existing customers while also increasing monthly transaction volume.

Figure 4: Deposit growth after digitalisation



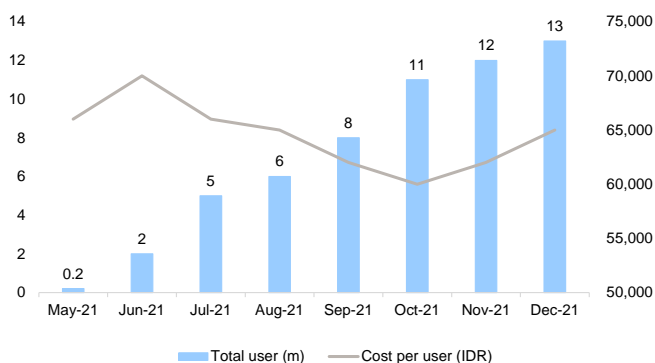
Source: Company data, RHB

Figure 5: Average deposits per registered digital user (IDRk)



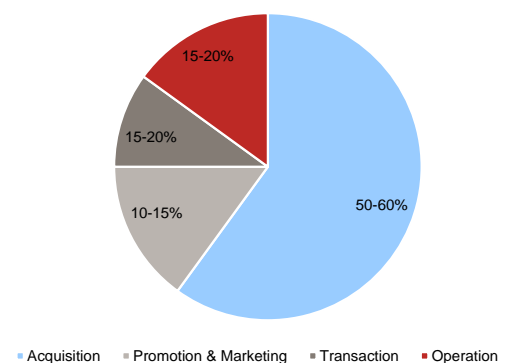
Source: Company data, RHB

Figure 6: Customer acquisition costs from May to Dec 2022F



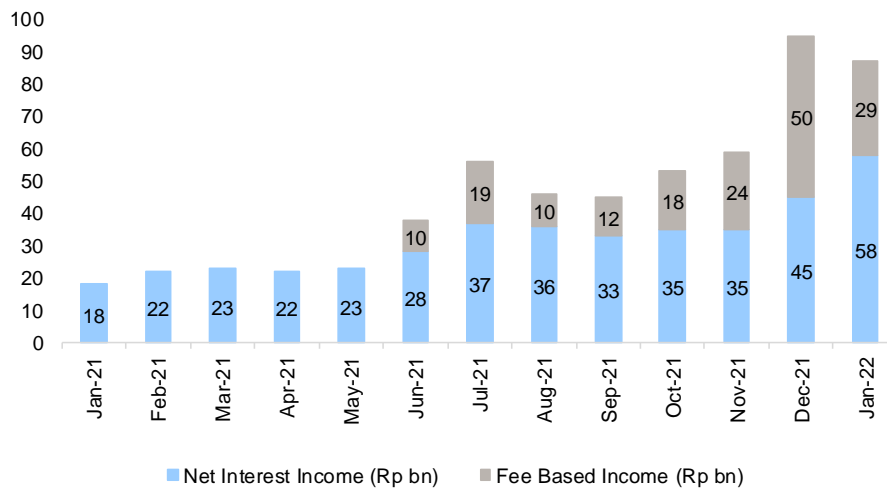
Source: Company data, RHB

Figure 7: Cost breakdown



Source: Company data, RHB

Since the launch of Neo+, BBYB's fee-based income has grown significantly – the majority of this comes from ATM fee income. As BBYB is aggressively acquiring new customers through attractive deposit rates, people have also begun using its app for transactions like inter-bank transfers and also cash withdrawals. This has positively impacts its fee income contributions. Moreover, as bank expands its services to include wealth management, open-banking partnership, insurance, we believe such contributions are set to grow even further.

Figure 8: Growing net interest income and fee-based income

Source: Company data, RHB

New features aimed at increasing transaction volume

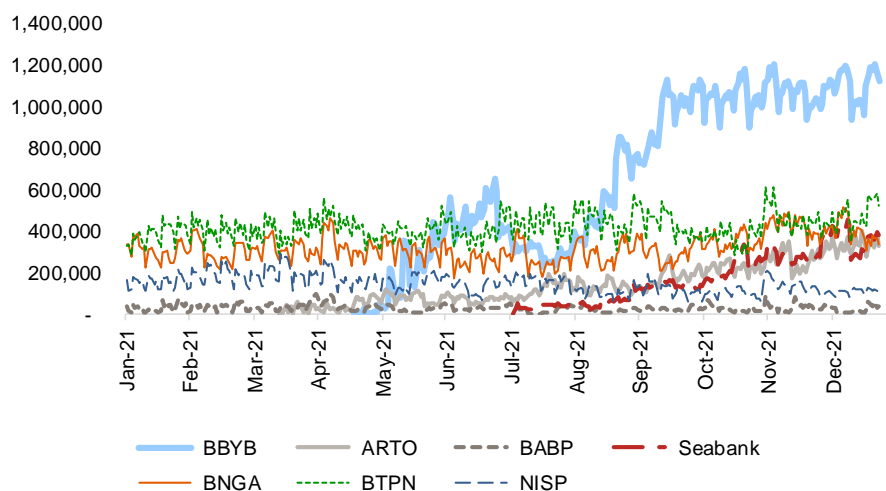
Beyond attracting new users, the company's goal for this year is to boost Neo+'s stickiness with existing users. To begin with, BBYB offers gaming features that reward players with coins that can be traded for discounts, additional deposit interest, and other incentives. Again, Neo+ daily active users have outpaced prior digital applications, surpassing 1m daily users. Additionally, it was the most engaging banking app in the country, with an average daily usage duration of six minutes per user.

In January, the bank processed almost 25m transactions involving interbank transfers, bill payments, virtual accounts, and Neo transfers. In 2022, it intends to increase its services as follows:

- i. Payment: Indonesian Quick Response Code Standard (QRIS), rapid payments (debit card, virtual account), and a variety of services such as e-commerce, travel, and medical care;
- ii. Wealth management products: securities accounts (RDN), mutual funds, stocks, insurance, and bonds;
- iii. Digital loans: instalment payments, instant cash, and Buy Now Pay Later (BNPL).

We believe that when more features become available, transaction volume will certainly increase. Currently, the corporation subsidises interbank transfer fees, which can be levied to clients due to their increased reliance on the Neo+ app, in our opinion.

Figure 9: Daily active users



Source: App Annie, RHB

Revenue generation from a huge user base

In 2022, BBYB intends to distribute IDR10-12trn in loans, of which the majority should come via digital lending — through the launch of three lending products:

- i. Monthly cash installments: 2-24 months;
- ii. Instant cash: up to a 2-month tenure;
- iii. BNPL.

Compared to other companies that give digital loans, BBYB has the largest user base. This should better enable the bank to distribute its own digital loan products.

Figure 10: Changes in the distribution between loan segments

	Then	Now	Plan	Indicative yield
Channeling	20-30%	30-40%	20-30%	15-20%
Pension	55-65%	30-40%	0-10%	12-13%
Digital Loan	0%	10-20%	40-50%	30-70%
SME	15-25%	10-15%	10-20%	13-18%

Source: Company data, RHB

◆ BBYB has increased its focus on higher-yield segments, digital loans and channeling, while reducing its emphasis on the pension loan segment.

BBYB has been steadily lowering its historical loan exposure by transferring it to digital loans and channeling those with a higher yield. In November, it launched its first digital loan product through Akulaku, DanaCecil, a cash instalment programme. The loan amount ranges from IDR500K to IDR15m, with monthly interest rates ranging 2.48% to 6.25%. Management intends for digital loans to account for 40-50% of loan disbursements.

While using the Neo+ app, a cash-instalment product was soft-launched to a select group of prioritised consumers. In 2Q22, the company aims to disburse digital financing to 300-400k consumers with an average transaction value of IDR2-5m. The primary objective is to give digital loans to at least 30% of the company's total subscribers.

Synergies with Akulaku

Akulaku became an investor in BBYB for the first time in early 2019, when it acquired 8.9% of BBYB shares from Gozco Capital for IDR338 per share, implying a total transaction value of IDR158bn. Then, Akulaku gradually increased its stake in BBYB to 25.44%, largely via a rights issue and in the secondary market.

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BBYB plans to issue up to 5bn new shares in a rights offering in May, with the proceeds going toward strengthening core capital, credit disbursement, and other operational activities, the Indonesian digital lender announced in a stock exchange filing.

We believe there should be positive synergies for both BBYB and Akulaku. First, it can increase the loan channeling to Akulaku, especially as Akulaku Finance Indonesia has reintroduced the BNPL service solution or the Shopping Now Pay Later concept, rebranding it as Akulaku PayLater. Second, Akulaku users can also apply for cash instalments or instant cash loans to BBYB. Today, only 10-15% of Akulaku customers are using Neo+ apps, and BBYB can further tap into Akulaku users. Note that, Akulaku is South-East Asia's leading consumer financial platform. Furthermore, this fintech company is dedicated to providing financial services ranging from instalment shopping on online platforms such as marketplaces to credit card processing. Akulaku's strength is its extensive Indonesian merchants partnership.

Figure 11: Akulaku key merchants



Source: Akulaku, RHB

Moving up to KBMI 2 through rights issue

Company has scheduled a rights issue (RI) in 1H22, with targeted proceeds of IDR5trn that will bring its equity to IDR7.6trn. With this corporate action, BBYB will fulfil the required capital based on the new Financial Services Authority (OJK) regulation, and move up in classification to Bank Classification (KBMI) 2, with capital ranging IDR6-14trn.

Figure 12: Historical rights issue exercises

Year	New shares (bn)	Price per share (IDR)	Proceed (IDRbn)	Equity post-RI (IDRbn)
2016	1.509	125	189	643
2018	0.47	338	159	600
2019	0.5	300	150	946
2020	0.832	300	250	1121
2021	1.927	1300	2505	2588
2022	TBA	TBA	5000	7588

Source: Company data, RHB

Local competition

The main fully digital banking competitors for BBYB are Bank Raya Indonesia (AGRO IJ), Bank Jago (ARTO IJ), Bank Aladin Syariah (BANK). However, the pie is large and their target segment is differentiated. BANK is targeting *shariah* financing customers for *hajj* pilgrims, while AGRO is tapping into BRILink agents and BRI ecosystem first. Meanwhile, ARTO already has its own ecosystem with Gojek drivers and Tokopedia customers. In the meantime, BBYB already has its own customer base, and is further expanding to the millennial market – as proven by the strong growth of its user numbers. Also, BBYB has one of the most attractive valuations among its peers.

In the past few months, there was pressure on the digital banking sector, which we believe was impacted by two factors:

- Most digital banks are likely to book losses in FY21F, as the main strategy is to acquire new users;
- Old-economy sectors are distributing dividends, which are attractive to accumulate for 1H22.

However, with the recent rally on the old economy, we believe digital banks provide more attractive upside, as the development on the features is still on-going. Furthermore, the digital banking sector is expected to start booking profit in 2023-2024.

Figure 13: Peer comparison (FY22F)

No	Name	Ticker	Rating	Price (IDR)	Target price (IDR)	Upside (%)	Market cap. (USDbn)	P/E (x)	P/BV (x)	ROE (%)
1	Bank Neo Commerce	BBYB IJ	BUY	2,110	3,100	46.9	1.3	(65.1)	2.8	(5.4)
2	Bank Raya Indonesia	AGRO IJ	BUY	1,160	4,900	322.4	1.7	162.5	6.2	4.7
3	Bank Jago	ARTO IJ	N/A	13,800	N/A	N/A	12.5	656.1	23.2	3.2
4	Bank Aladin Syariah	BANK IJ	N/A	2,230	N/A	N/A	2.0	(317.2)	28.2	N/A

Source: Company data, RHB

Valuation

Our valuation combines a Gordon Growth Model (GGM) approach and that of a valuation per customer basis, compared to other digital banks worldwide. While BBYB has the strongest user growth nationally, we believe it will start to monetise its user base this year, through the lending products. Moreover, being a part of Akulaku – which has experience in the digital lending business – BBYB should be able to utilise its credit scoring to manage NPL well.

GGM calculation

For GGM methodology, our main assumptions are a risk premium at 4%, risk-free rate of 7%, beta of 1.11x, dividend payout ratio of 30%, and a sustainable ROE of 15%. We expect the bank to cut its marketing cost and pare down losses in 2023. Starting in 2014, we expect company to start booking profit and paying dividends in 2025.

Figure 14: Gordon Growth Model details

Risk premium	4%										
Risk free rate	7%										
Beta	1.07										
CoE	11%										
Payout ratio	30%										
Sustainable ROE	15%										
Sustainable growth, g	11%										
	2022F	2023F	2024F	2025F	2026F	2027F	2028F	2029F	2030F	2031F	2032F
	0	1	2	3	4	5	6	7	8	9	10
DPS (IDR/share)	-	-	-	5	10	17	25	30	35	41	49
Discount factor (x)	1.00	0.90	0.81	0.73	0.65	0.59	0.53	0.47	0.43	0.38	0.34
NPV of dividends	95										
Terminal value	6,933										
NPV of terminal value	2,381										
Target Price	2,476										

Source: Company data, RHB

Valuation per customer

For the valuation per customer method, we assume that from a total of 25m target users in 2023, at least c.30-40% are active ones. After new transactional features are added, people can use Neo+ not only for deposits, but also for transactions.

We calculated the average valuation per customers of digital banks worldwide, and found a value of USD829.00/user. With an estimated 7.5m active users, we value BBYB at IDR3,000/user.

Figure 15: Valuation per customer

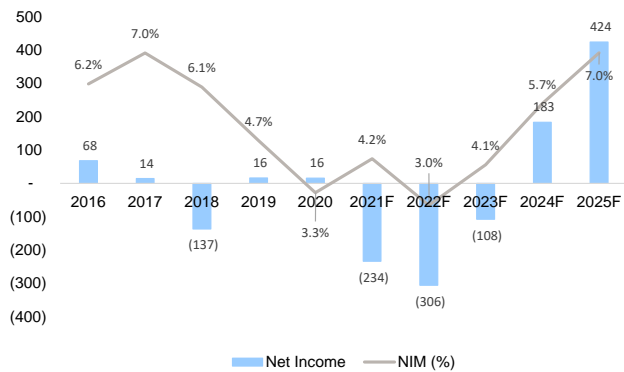
	Number of users (m)	Valuation (USDbn)	Valuation/user (USD)
Jago*	15.0	13.1	873
Raya*	10.0	1.8	182
Revolut	15.5	33.0	2,129
Monzo	5.0	4.5	900
Nu Bank	48.1	28.1	584
Kakao	17.4	19.9	1,144
Webank	200.0	21.0	105
N26	7.0	9.0	1,286
Chime	13.0	25.0	1,923
Starling Bank	2.5	1.5	600
Wise Bank	12.0	11.0	917
Paytm Payment Bank	60.0	25.0	417
Rakuten	11.0	2.6	236
Tinkoff	20.0	6.3	315
Average Value per user (USD)			829
BBYB expected active users (m)			7.5
BBYB Valuation (IDRbn)			88,322
TP from Valuation per user			3,775
TP from DDM			2,476
Average TP			3,100

Source: Company data, RHB

Financial Outlook

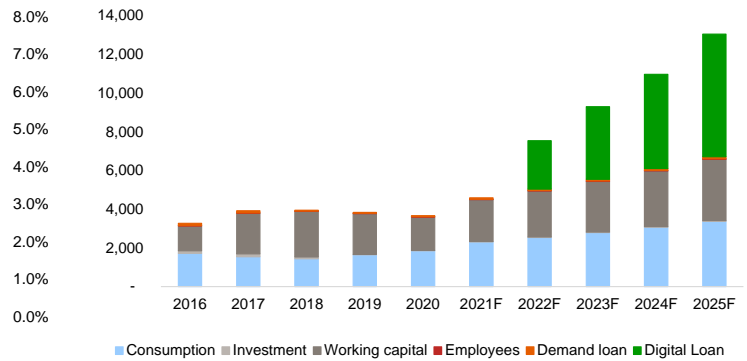
In 2022, we expect BBYB to maintain its aggressive strategy to acquire new users, by giving referral incentives, subsidising inter-bank transfer fees, and other coupons. Thereafter, it is likely to book profit from 2024 onwards, boosted by digital lending and a reduction in acquisition cost.

Figure 16: Net income and NIM



Source: Company data, RHB

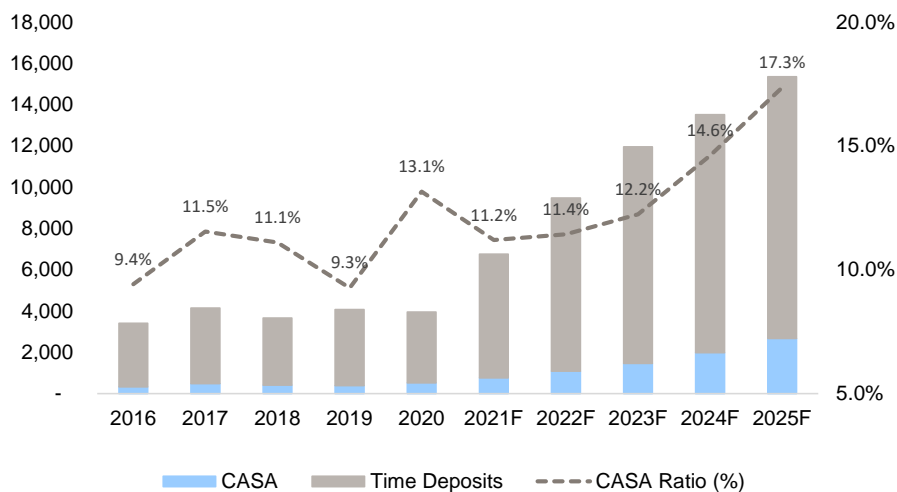
Figure 17: Loan composition



Source: Company data, RHB

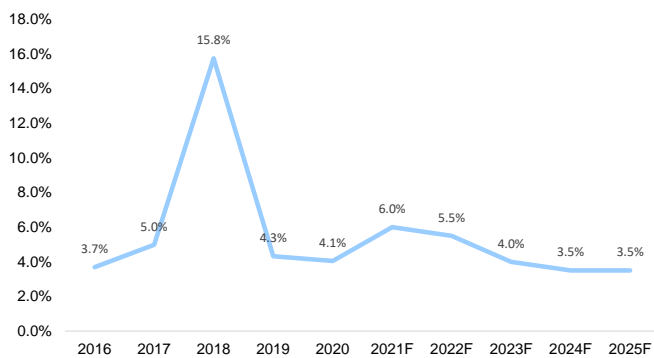
BBYB's total deposit growth is driven by the convenience of Neo+ and its attractive deposit rates. With additional transactional features such as QRIS, Virtual Account, and RDN, we expect its CASA ratio to begin improving.

Figure 18: Total deposits



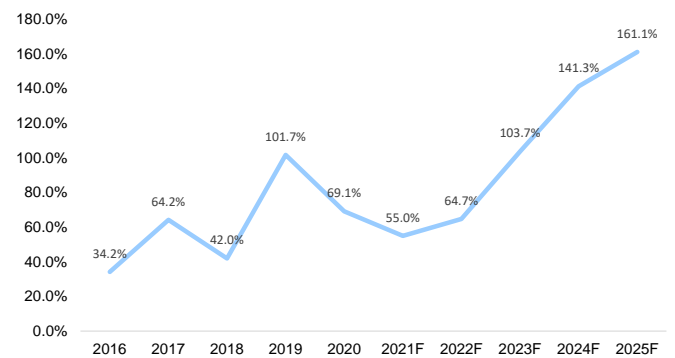
Source: Company data, RHB

Figure 19: NPL trend



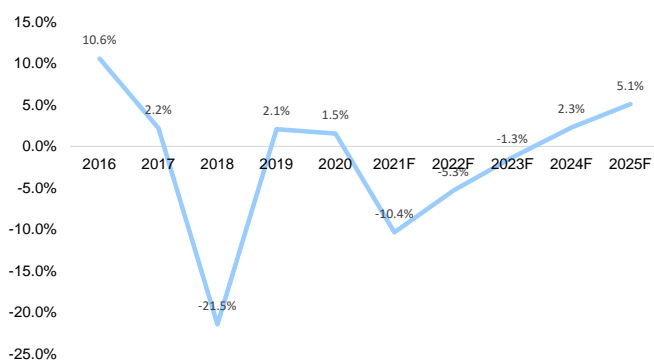
Source: Company data, RHB

Figure 20: NPL coverage trend



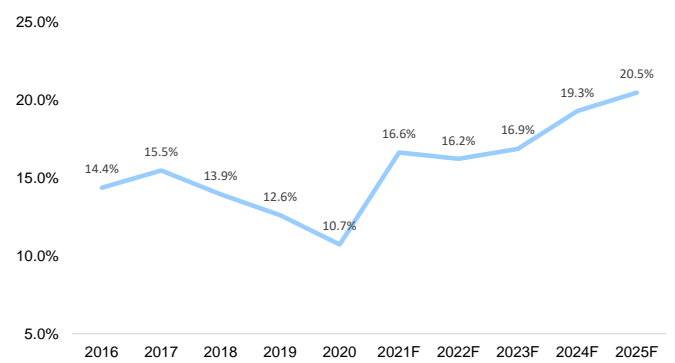
Source: Company data, RHB

Figure 21: ROE trend



Source: Company data, RHB

Figure 22: Blended loan yield



Source: Company data, RHB

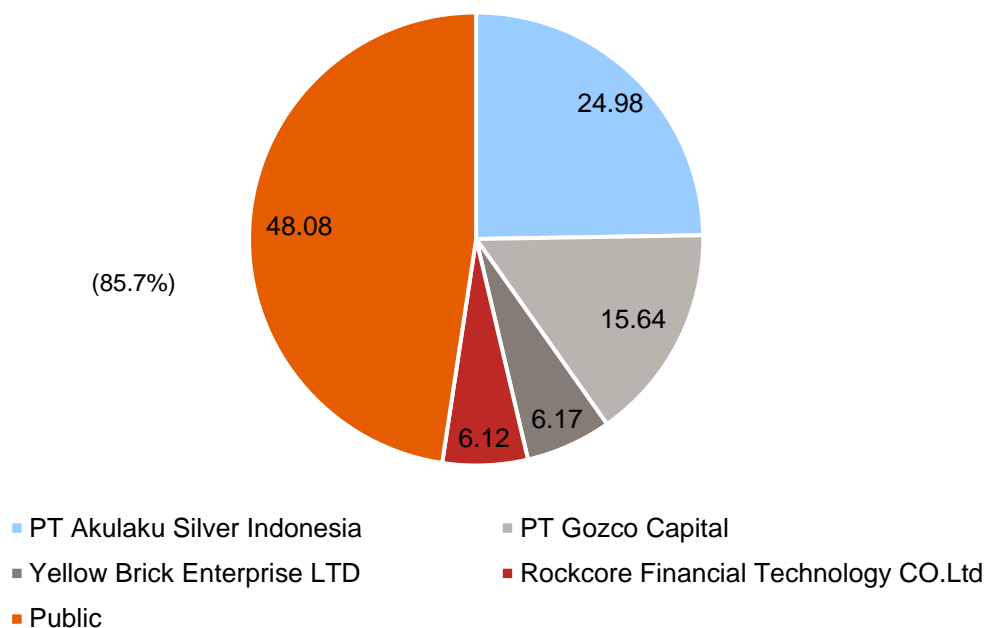
Company Background

BBYB was founded in 1989 as Bank Yudha Bhakti by the Ministry of Defense, Perum ASABRI, Pepabri, and other developers as Bank Yudha Bhakti. The bank is in the "A" category, which means it did not require government assistance during the 1997 monetary crisis.

BBYB was publicly traded on the Indonesia Stock Exchange in 2015. Its shares were then acquired by Akulaku Silvr through a capital increase without pre-emptive rights by Akulaku Silvr (PMTHMETD). Later in 2020, the company conducted another right issue, bringing BBYB to BUKU II with core capital exceeding IDR1trn. It was also rebranded as Bank Neo Commerce.

BBYB began its transformation into a digital bank in 2019, with the help of Akulaku Silvr, and successfully launched a new mobile banking app called Neo+.

Figure 23: BBYB's ownership structure






Source: Company data, RHB

Figure 24: Company milestones

Year	Description
1989	Bank Yudha Bhakti was officially established.
2015	Became a public company by listing its shares on the Indonesia Stock Exchange.
2019	Akulaku become a shareholder in BBYB. Increased the issued / paid-up capital of the company as a result of the capital increase without pre-emptive rights (PMTHMETD).
2020	Changed its name to Bank Neo Commerce. Became a Commercial Bank Business Group (BUKU) II with a core capital of over IDR1trn.
2021	Neo+ mobile banking app launched




Source: Company data, RHB

Figure 25: Board of Commissioners

Name	Position	Description
 <p>Supriyadi</p>	President Commissioner / Independent Commissioner	<p>Served as President Commissioner since 19 Feb 2020. Obtained a Bachelor's degree in Civil Law from UII, Yogyakarta (1987) and Masters of Management from the International Management University of Indonesia, Jakarta (2001).</p> <p>Previously, he was the Head of Bank Rakyat Indonesia's (BRI) Corporate Secretariat Division (Apr 2014-Sep 2015), BRI Regional Leader Jakarta (Oct 2015-Feb 2017), and Director of Consumer Banking at Bank Tabungan Negara (Mar 2017-Sep 2019).</p>
 <p>Tjandra Mindharta Gozali</p>	Commissioner	<p>Served as Independent Commissioner since 9 Apr 2021. Obtained a Bachelor's degree in Economics from the University of Pembangunan, Jakarta and a Masters of Management Degree from Trisakti University.</p> <p>He is also an Independent Commissioner at Pelindo Investama. Previously, he was Commissioner at Maritim Learning Indonesia Harbour (Jan-Jul 2020). He has been the Chairman Of Infobank Institute since May 2015.</p>
 <p>Pamitra Wineka</p>	Commissioner	<p>Served as an Independent Commissioner since 9 Apr 2021. He obtained a Bachelor's degree from Al-Azhar University Cairo, Egypt then a Master of Science degree from the University of Indonesia.</p> <p>He previously served as a special staff member in the Ministry of Youth and Sports (2015-2017), and was an expert consultant in Ministry of Maritime Affairs and Fisheries (2019-2020).</p>

Source: Company

Figure 26: Board of Directors

Name	Position	Description
 Tjandra Gunawan	President Director	<p>His professional career began as an auditor at KPMG Siddharta Siddharta & Harsono from Oct 1994 to May 2000, with his last position as Audit Supervisor. Then in Jun 2000, his career in finance and banking began, with a position as Manager, Head Office Reporting & Analyst at Citibank NA.</p>
 Aditya Wahy Windarwo	Director	<p>Obtained a Bachelor of Economics degree from Universitas Indonesia in 2002, and Master of Science from University of Colorado in 2002. He began his career as a mutual fund specialist in Manulife Asset Management Indonesia in 2005, and entered the banking industry in 2005 as Investment Product Manager at Citibank.</p> <p>He was also Head of Retail Product Management & Digital Banking at Bank Mega in 2014-2019. Thereafter, he was Head of Wealth Management, Retail Liability & Customer Segment Head at Bank Permata in 2019-2021.</p>
 Ricko Irwanto	Compliance Director	<p>Obtained a Bachelor of Engineering from Sriwijaya University in 1994 and Master's degree from STIE IPWI in 1999. He began his professional career as Customer Relations Manager at Bank Bali in 1996, and was promoted as Head of Operational Development and Improvement. He was also held a position of Operational Risk Management Head at Bank Pertama. His latest position prior to joining the company was Compliance Director at Bank MNC International from 2019 to 2021.</p>

Source: Company data, RHB

Industry Overview

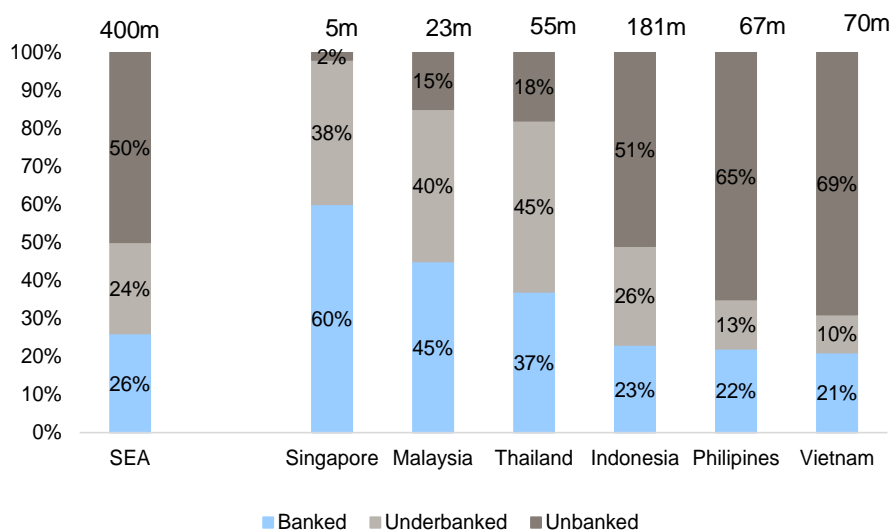
Big unbanked population points to great growth potential

We believe there is huge growth potential for digital banks in Indonesia, since around 139m people in the country are not well-served by existing banks – and of these, 92m are still unbanked. Meanwhile, Indonesia has the third-largest number of internet users in the Asia-Pacific – this means its 203m internet users could have access to digital bank platforms.

About half the population of Indonesia is 30 years old or younger. Boston Consulting (BCG) estimates that Indonesia's middle class will grow by 1.3x from 2019 to 2024. The country – which also has the biggest population in South-East Asia – has a growing appetite for digital financial services, and digital transactions have increased by 30-50% pa over 2015-2018. As of end-2019, Indonesia had the second highest e-payment penetration in South-East Asia, next to Singapore.

According to Bain & Company, around 92m Indonesian people still do not have access to banks (unbanked), and around 47m do not have good access to banking services. Hence, the growth potential for digital banks is huge – since there are about 139m people who have not been served optimally by existing banks, due to the limited access to physical banks and other conventional bank limitations.

Figure 27: Percentage of underbanked and unbanked population in South-East Asia (2018)

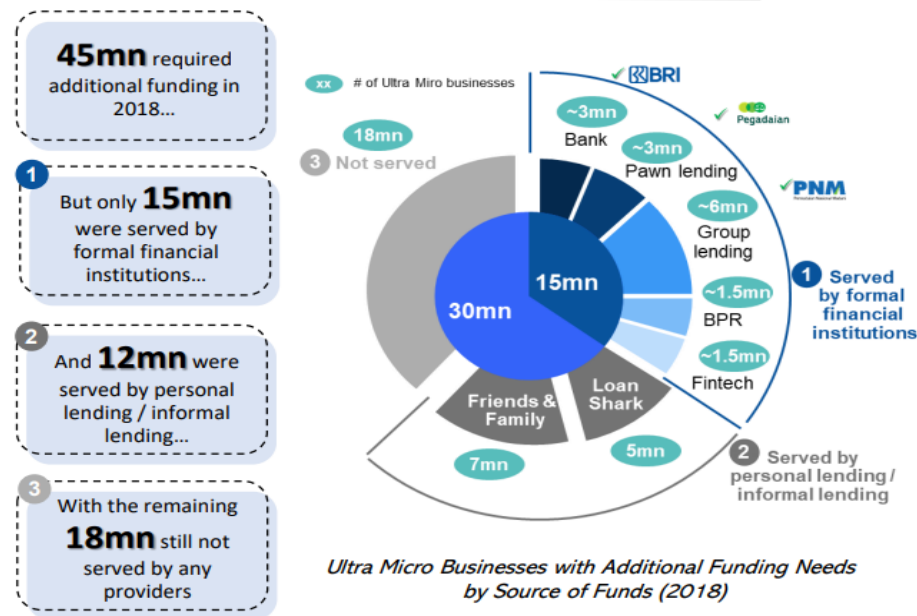


♦ The majority of Indonesians remain underbanked or unbanked (77% of total population)

Source: Bain, RHB

This is in line with Bank Rakyat Indonesia's (BBRI IJ, BUY, TP: IDR5,500) study, which found that around 30m of its potential customers have not been well-served by the bank. Around 18m potential customers have not been contacted at all by any financial providers, and around 12m potential customers' financing are served by personal and informal lenders. While larger conventional banks are focused on acquiring high net worth individual and corporate customers, smaller digital banks are more agile in adapting to capture the untapped market of customers with uncertain lifetime value.

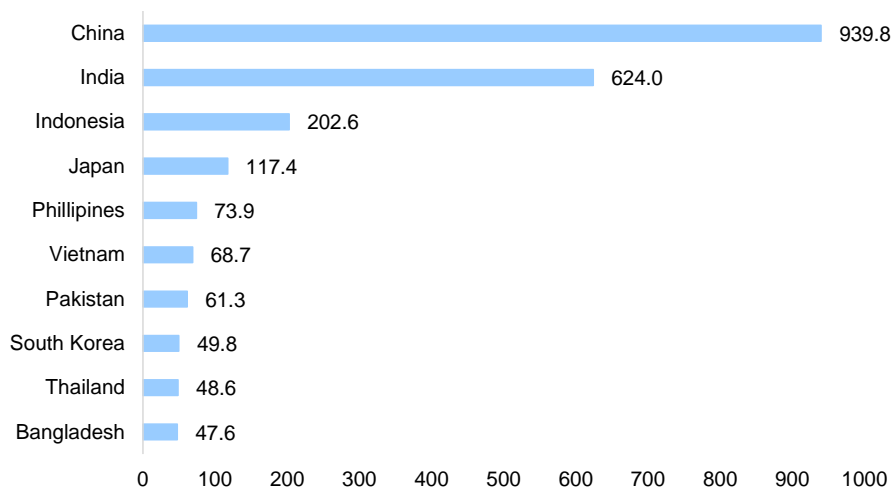
Figure 28: Potential market for digital bank funding



♦ The digital banks' untapped funding market comes up to about 30m people. Of this, 12m are served by personal/informal lenders, and 18m are not served at all

Source: BBRI, RHB

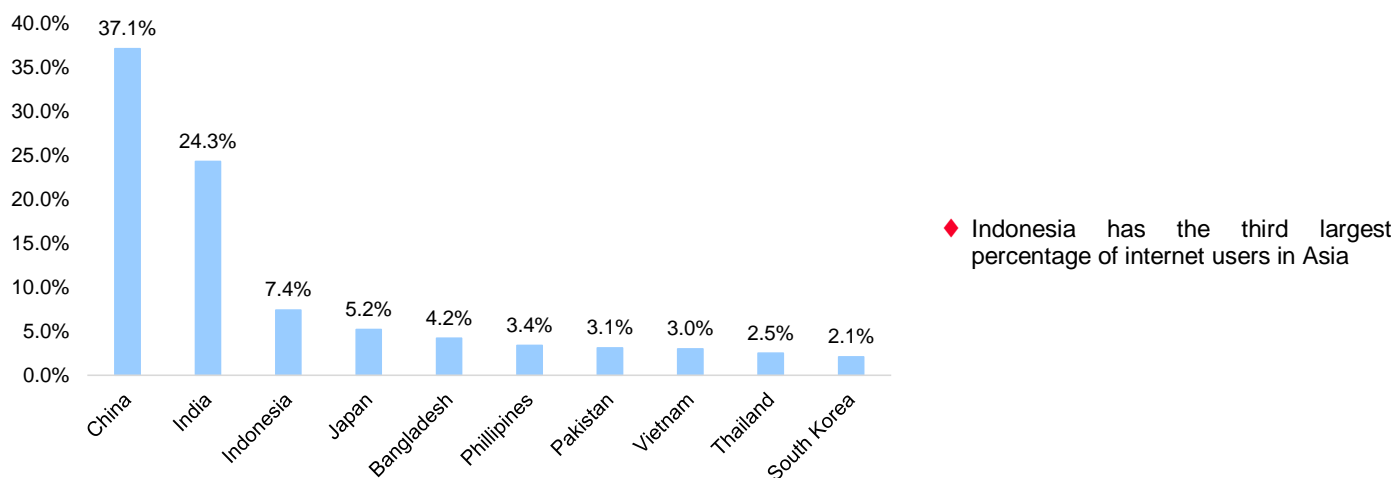
Figure 29: Top 10 internet users in Asia-Pacific as of Jan 2021 (m)



♦ Indonesia has the third largest population of internet users in Asia Pacific, with 202.6m users

Source: Statista, RHB

Figure 30: Asian countries with the biggest percentage of internet users as of May 2020



Source: Statista, RHB

Financial Services Authority (OJK) guidelines

We believe that relaxation of the OJK's digital banking guidelines for foreign shareholders of an Indonesian digital bank effectively lowered the barriers to entry into the sector, thereby engendering healthy competition. This will provide opportunities for collaboration between established international players and local challengers that are trying to penetrate the market.

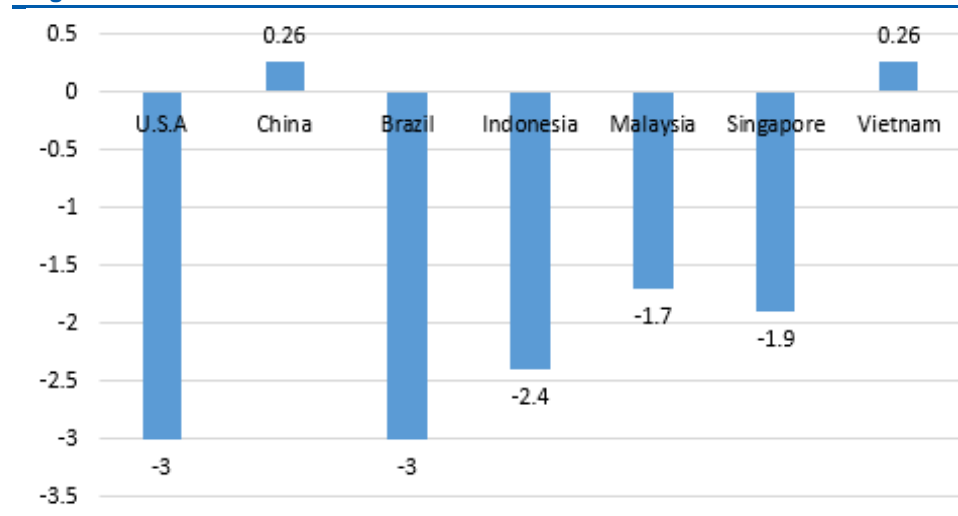
Collaborations are already taking place in the sector, at the time of writing. Shopee, the e-commerce arm of Singapore's Sea Group, acquired Bank Kesejahteraan Ekonomi in February, and intends to transform it into the digital bank, SeaBank. Bank Neo Commerce, and its digital bank Neobank, have Indonesian fintech, Akulaku (which in turn has China's Ant Group as an investor) as their controlling shareholder. These will certainly not be the last of the collaborations, as Malaysian banks BIMB (BIMB MK, BUY, TP: MYR3.70) and AMMB (AMM MK, BUY, TP: MYR3.90) have also declared their interest in exploring digital opportunities in the country.

The regulations also commit to making it more convenient for banks to obtain permits for new services – what could have taken 60 days before is now capped at a maximum of 14 days. Further, basic services such as savings and transfers no longer require permits. Instead, the OJK only requires the banks to report the said services to them. Banks are also required to submit a strategic 5-year plan to the regulator.

On the other hand, the OJK requires digital banks to have a minimum paid-up capital of IDR10trn, which is significantly higher than most of its regional peers. Malaysia, for instance, requires a minimum paid-up capital of only RM100m (IDR339bn) unimpaired by losses during the first 3-5 years, after which the amount increases to RM300m (IDR1.02trn). We infer that this may have been done to encourage more partnerships between local and international banks and fintech firms, in order to leverage upon each other's financial as well as technical capabilities.

A new age of banking

One key reason for the increasing popularity of digital over conventional banks is the difference in cost structure. As digital banks do not operate brick-and-mortar branches, costs will consist of more variable than fixed elements. This provides an advantage to digital banks, as the increase in fixed costs associated with growth need not be exponentially high. Commercial banks around the world have already started to shut down some of their branches and are moving online. According to the International Monetary Fund (IMF) and MomentumWorks, between 2015 and 2020, Indonesia recorded a -2.4% growth in commercial bank branches per 100,000 adults.

Figure 31: Growth rates of commercial bank branches

Source: IMF, Momentum Works, RHB

Another significant difference between digital and conventional banks is the application of big data. More often than not, digital banks possess the appropriate integrated infrastructure to collect and store customer/operational data, due to the use of higher-quality mobile applications. This data is then used to design better products and risk models, as well as improve operational efficiency and customer targeting. For instance, Bank Jago (ARTO IJ, NR), part-owned by GoTo (formed by the partnership of Indonesian unicorns Gojek and Tokopedia), offers interest rates of 0.5% and 3.5% on spending and saving pocket accounts. These rates are higher than those offered by Indonesia's bigger banks, and effectively encourage price competition in the sector.

These differences allow digital banks to access an expanded customer base, often in the traditionally "high-risk" segments. Also, by carefully curating a convenient and meaningful customer journey, these banks can hope to enjoy customer loyalty in time. Eventually, digital banks will be able to serve customers with more targeted products, aided by their ever-growing data bank, which in turn could lead to a growth in interest margins – in China, as of 4Q20, the average NIM among digital banks was 3.7%, compared to 2.4% among conventional banks.

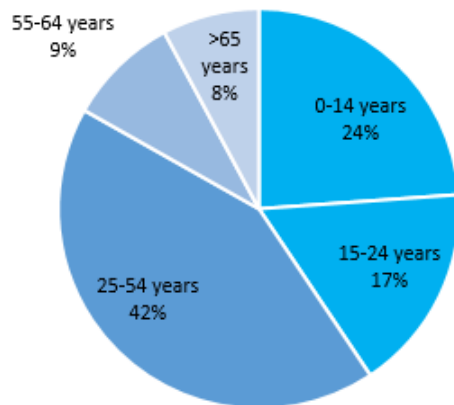
There is also a distinction between the decision-making drivers of conventional and digital banks. While conventional banks tend to focus on maximising profit, digital banks have their eyes set on maximising growth, measured using less conventional metrics such as daily average users (DAU) and monthly average users (MAU). As digital banks, at their core, are internet companies first and banks second, a larger consumer base allows the bank access to more data, which opens up more cross-selling/up-selling opportunities. However, we remain cognisant of the potential change in business direction towards profit-seeking, as digital banks slowly capitalise on economies of scale over time.

These differences outline why digital banking may appeal to an entirely different market demographic than in previous generations – a market mainly consisting of internet-savvy youths.

Indonesian demographics and why digital banking might work

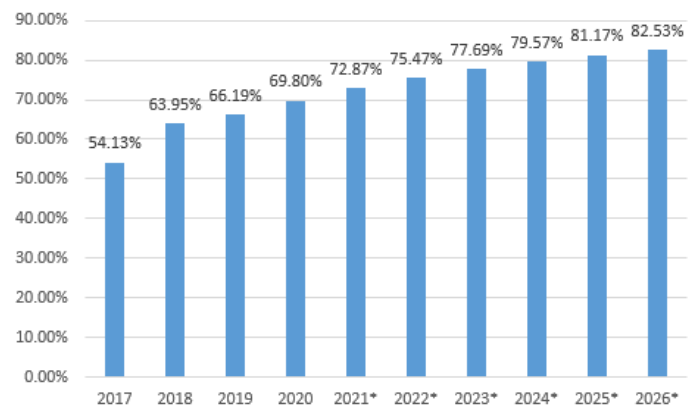
Indonesia currently houses over 275m people, making it the fourth most populous nation in the world. Almost 41% of these 275m people are aged 24 or under, a fact reflected in the relative digital savviness of the average Indonesian. While internet penetration in the country was only at 69.8% as at end 2020, a report by Nikkei Asia in Jan 2019 stated that 76% of Indonesian internet users were making purchases online each month, and this was before the days of the pandemic. Digital banking app downloads also grew 7% in 2020. However, it is worth noting that only 61% of Indonesians have a bank account, while only 6% of adults possess a credit card.

Figure 32: Population of Indonesians by age



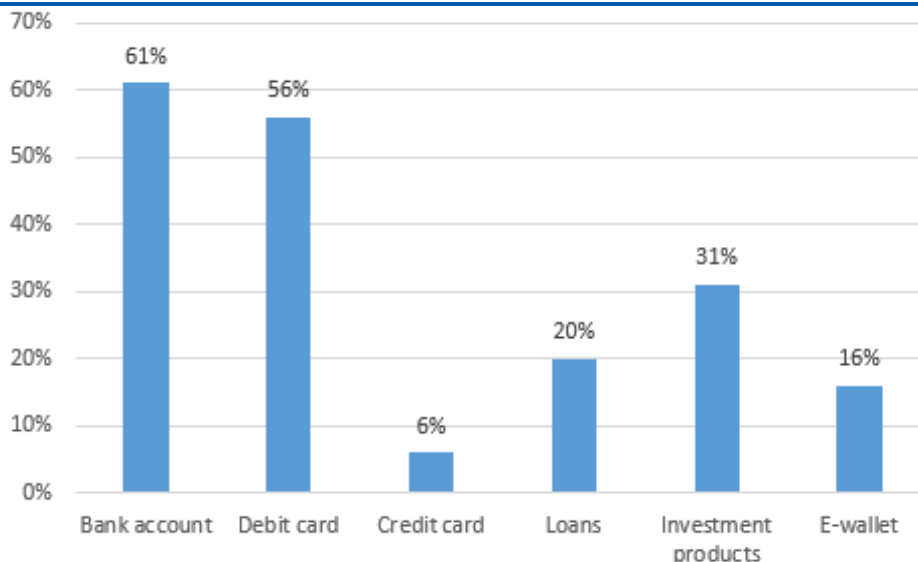
Source: CIA World, Facebook, RHB

Figure 33: Internet penetration rate in Indonesia



Source: Statista, RHB

Figure 34: Use of commercial banking products in Indonesia



Source: Momentum Works, RHB

Indonesians' general proximity to technology is an encouraging factor for digital banks' consumer banking operations. Banks can expand their reach by making basic banking services accessible simply via mobile phone. Forming partnerships with fintech outfits such as e-commerce and digital wallet companies provide convenience to customers who are already active users of the fintech products. One example of such a partnership is between Bank Jago and GoTo, which allows the former access to Gojek's entire driver fleet as well as Tokopedia's SME vendors and customers, while making Jago's banking services available on the Gojek app.

While having a strong focus on the consumer banking segment, the lending side should also be a point of consideration. For the next few years, we expect digital banks to be paying particular attention to SME, retail consumer and B2B customers. On top of that, some banks, including Bank Jago, are exploring a partnership lending business model – lending to established partners after a thorough due diligence is conducted. In the near future, we also anticipate digital banks' wealth management and *shariah* compliant products to grow.

Major categories of digital banks

Digital banks in Indonesia are divided into three major categories:

- i. Conventional supported;
- ii. Tech-player backed;
- iii. Independent.

Digital banks supported by large conventional banks have a strong offline and online presence, with the ability to utilise the latter's office branches. The synergy with their respective holding companies will allow them to operate efficiently and access existing customers for swift growth, like BLU and AGRO

Digital banks acquired by giant tech players – ARTO, Seabank, Bank Bumi Arta (BNBA IJ, NR), BBYB, and Bank Bisnis Internasional (BBSI IJ, NR) – already have ecosystems, and will be able to integrate their banking systems with the e-commerce applications. Moreover, they can access the user database and analyse their customers' credit scores with high accuracy.

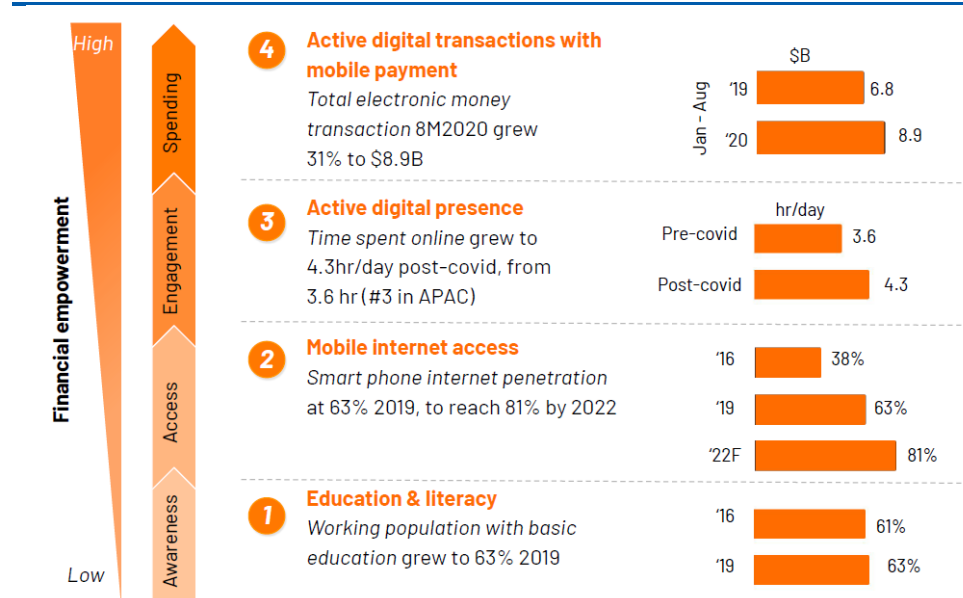
However, we believe independent digital banks will likely face the most challenges compared to digital banks in the other two categories, as customer acquisition and maintenance cost can be higher.

Fintech development paved the road for digital banking

The financial technology boom that began in 2015 created a better landscape for digital financial services in Indonesia. More than 150 fintech start-ups were founded in 2016, growing 78% YoY, and in 2019, there were 249 fintech companies.

In 2016, more than 17.4m credit cards were issued, and in 2017, digital payment total transactions reached USD18m – indicating the level of trust in the security of digital financial services in Indonesia. Increasing digital transactions have been supported by the growth of e-commerce and food delivery services via online platforms. The emergence of COVID-19 further accelerated the digital adoption in Indonesia.

Figure 35: Digital awareness, access, active engagement and adoption



Source: Momentum Works, RHB

Sector risks

The conflict between Russia and Ukraine has caused commodity prices to skyrocket, and is likely to cause the consumer price index to increase. As digital banking targets the untapped market, it may dampen the purchasing power of low- and middle-income segments, potentially dragging the demand for consumer loans. Moreover, NPL may also spike up in a post-pandemic environment.

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-04-21			

Source: RHB, Bloomberg

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