

29 September 2022

Financial Services | Banks

Banks

Overweight (Maintained)

Growth In Residential Mortgages To Stay Firm

- **Stay OVERWEIGHT; DBS and OCBC Bank are our Top Picks.** Last week's move by local banks to pull fixed-rate residential mortgages off their shelves suggests that the US Federal Reserve's revised terminal rate of 4.6% in 2023 is generally higher than expected. While the spike in interest rates would likely lead to temporary weakness in the residential property market, we believe underlying demand remains healthy. The drawdown of loans sold in 2021 would also support sustained, albeit moderate, growth in mortgages over the next 12 months.
- **More aggressive than expected rate hikes ahead.** Late last week, United Overseas Bank and DBS announced that they are temporarily ceasing their fixed-rate home loans as they review the interest rates on these packages (Figure 1). This follows the 75bps hike in the federal funds rate (FFR) to 3.25% on 21 Sep. The banks' decision to review the fixed-rate loans, can be attributed to the US Fed's hawkish signalling for more aggressive than expected hikes ahead. US officials forecast rates would reach 4.4% by the end of 2022 and 4.6% in 2023, sharply higher than June's projections of 3.25% and 3.50% respectively.
- **Expect temporary softening in property sales.** In tandem with the rise in FFR, the 3-month compounded Singapore Overnight Rate Average or SORA has risen 173bps YTD to 1.93% currently, with a substantial 140bps increase from 1 Jun 2022 (Figure 2). The spike in interest rates over the short span of four months, in our view, would dampen sentiment and result in a temporary softening in demand for residential property in the immediate term.
- **Underlying demand still firm.** We believe home buyers would adjust to the higher interest rate environment and this should eventually lead to a rebound in sales of residential properties, in particular the mass market residential properties. Underlying demand for owner-occupied homes remains healthy as evident by the 31% QoQ increase in number of private residential units sold in 2Q22, compared to the sharp 39.5% QoQ fall in 1Q22 following the announcement of property cooling measures in mid Dec 2021. Aside, the recovery in unit sales, the Urban Redevelopment Authority or URA reported a healthy 3.5% QoQ rise in residential property prices in 2Q22 (Figure 3), extending the rise in prices of private residential property to nine consecutive quarters.
- **Moderate but sustained, growth in property loans.** Banking system property loans grew 2.3% YTD July 2022 (or 4.0% annualised). This compares favourably against the flattish consumer loans and 1.3% YTD increase in business loans over the same period. We believe banks would chalk moderate, but sustained, increase in residential mortgages over the next 12 months helped by the drawdown of loans for sales booked in 2021. As at end-June 2022, housing loans accounted for 18% of DBS' gross loans, 21% of OCBC's, and 23% of UOB's.
- **NIM expansion to continue.** The US Fed's hawkish stance in Sep 2022 and the revised FFR forecast suggest that banks' NIM would likely expand by a bigger quantum than earlier expected, and a plus for net interest income.
- **Risks.** Downside risk to our investment view would come from a sharp economic downturn that would result in job losses, hurt consumption spending, and impact the property market.

Stocks Covered 3
Rating (Buy/Neutral/Sell): 2 / 1 / 0
Last 12m Earnings Revision Trend: Positive

Top Picks

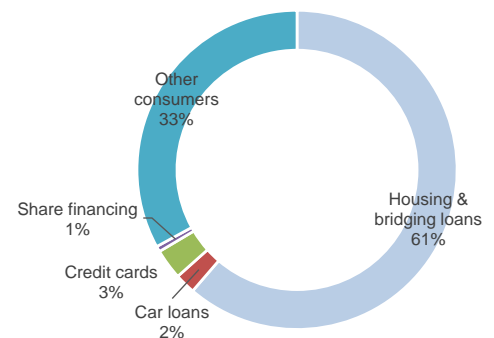
Target Price

DBS (DBS SP) – BUY SGD37.60
OCBC Bank (OCBC SP) – BUY SGD13.90

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Banking system consumer loans, July 2022



Source: Monetary Authority of Singapore, RHB

Company Name	Rating	Target (SGD)	% Upside (Downside)	P/E (x) Dec-23F	P/B (x) Dec-23F	ROAE (%) Dec-23F	Yield (%) Dec-23F
DBS	Buy	37.60	12.2	9.4	1.3	15.0	4.8
OCBC Bank	Buy	13.90	12.9	8.5	0.9	11.4	5.1
United Overseas Bank	Neutral	29.30	6.4	9.0	1.0	11.3	5.1

Source: Company data, RHB

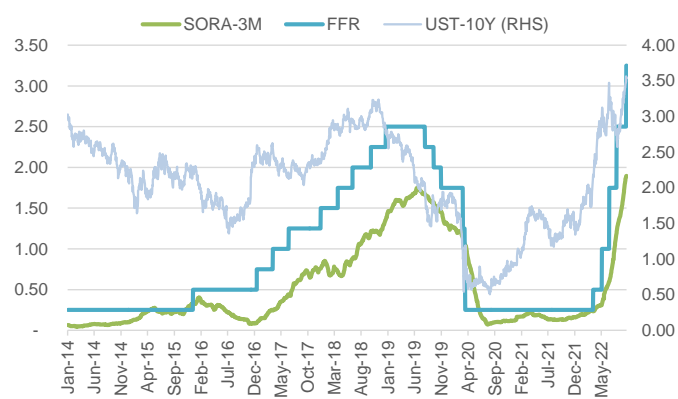
Figure 1: Selected mortgage packages

	DBS			OCBC	UOB	
Fixed-rate packages	2-year fixed 2.75% p.a. (new rates coming soon)	3-year fixed 2.75% p.a. (new rates coming soon)	Two-in-one home loan 50% fixed, 50% floating 40% fixed, 60% floating 30% fixed, 70% floating (still available)	2-year fixed 2.98% p.a.	2-year fixed 2.98% p.a. (stopped temporarily)	3-year fixed 3.08% p.a. (stopped temporarily)
Floating-rate packages (SORA)	2-year lock-in 3-mth compounded SORA + 1% p.a.		2-year lock-in FHR6 + 1.3% p.a.	Year 1 and 2 1-mth/3-mth compounded SORA + 0.98% p.a.	Year 1 and 2 3-mth compounded SORA + 1% p.a.	

Note: FHR6 refers to 6-month fixed deposit rate

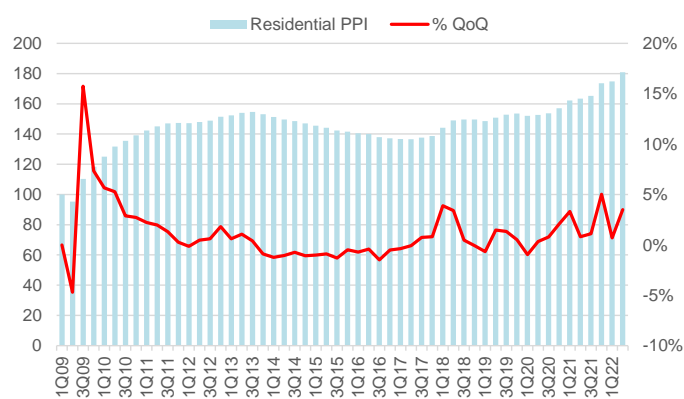
Source: Company websites, RHB

Figure 2: SORA trends higher as FFR spikes



Source: Bloomberg, RHB

Figure 3: Residential Property Price Index, quarterly trend



Source: URA, RHB

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