

# Hong Leong Bank Bhd

(5819 | HLBK MK) Financial Services | Finance

## Earnings pullback within expectations

### KEY INVESTMENT HIGHLIGHTS

- **Decline in 3QFY20 net profit but results were within expectations**
- **Lower income dragged 3QFY20 earnings**
- **Higher provisions due to ECL buffers**
- **Strong loans growth despite challenging environment**
- **Uptick in GIL ratio, quarter-on-quarter basis**
- **No change to FY20/FY21/FY22 earnings forecast**
- **Maintain NEUTRAL with unchanged TP of RM13.60**

**Within expectations.** Hong Leong Bank (HLB) reported lower earnings in 3QFY20. This resulted in marginal decline of -0.7%yoy in its 9MFY20 net profit. However, this was within ours and consensus expectation coming in at 74.5% and 75.8% of respective full year estimates.

**Lower performance in 3QFY20 dragged net profit.** PPOP in 9MFY20 grew +4.9%yoy due to performance in 1HFY20 as 3QFY20 PPOP fell -7.2%yoy. NII in 3QFY20 came in lower by -2.1%yoy due to NIM compression of -16bp yoy following from the OPR cuts in the quarter. However, strong loans growth moderated this impact.

**NOII growth from trading income.** NOII in 9MFY20 grew +6.2%yoy. This was driven by trading & investment income expansion of +29.0%yoy to RM334m.

**Higher provisions due to ECL buffers.** Provisions increased in 3QFY20 with credit cost going up +34bp yoy. This was due to ECL buffers of RM65m set aside to take into account the effect of Covid-19 pandemic and the movement control order (MCO). We expect to see the full impact in 4QFY20. Management expects credit cost to rise within the next 6 month between 10-13bp and on a stress scenario, 25bp.

**Strong loans growth despite the challenging environment.** Gross loans expanded +6.6%yoy to RM142.4b as at 3QFY20. Major drivers were residential properties, domestic business enterprise and surprisingly in Singapore. These grew +8.9%yoy to RM71.8b, +4.6%yoy to RM40.5b and +14.2%yoy to RM5.6b respectively. In terms of business enterprise segment, the key contributors were SME and community SME banking as it expanded +1.7%yoy to RM21.2b and +33.5%yoy to RM7.1b respectively.

**Uptick in GIL ratio.** HLB's GIL ratio saw another uptick on a sequential quarter basis. GIL ratio went up +14bp qoq to 0.98%. However, we consider this to be still very manageable and the management expect it to normalize in 4QFY20.

**Good pickup in CASA.** Deposits grew +3.0%yoy to RM167.9b. CASA saw good growth with +11.8%yoy to RM44.3b outpacing FD growth of +3.9%yoy to RM95.6b. This could be due to depositors ensuring sufficient cashflows.

**No revision in earnings forecast.** As the results were within our expectations, we are maintaining our FY20/FY21/FY22 earnings forecast.

## Maintain NEUTRAL

### Unchanged Target Price: RM13.60

#### RETURN STATISTICS

|  |             |
|--|-------------|
| Price @ 29 <sup>th</sup> May 2020 (RM) | 13.60       |
| Expected share price return (%)        | +0.0        |
| Expected dividend yield (%)            | +3.5        |
| <b>Expected total return (%)</b>       | <b>+3.5</b> |

#### SHARE PRICE CHART




| Share price performance (%) | Absolute | Relative |
|-----------------------------|----------|----------|
| 1 month                     | 2.3      | -2.3     |
| 3 months                    | 1.0      | -10.5    |
| 12 months                   | -28.4    | -19.8    |

#### KEY STATISTICS

|                                  |                 |
|----------------------------------|-----------------|
| FBM KLCI                         | 1473.25         |
| Syariah compliant                | No              |
| Issue shares (m)                 | 2046.43         |
| Estimated free float (%)         | 22.63           |
| Market Capitalisation (RM'm)     | 29480.96        |
| 52-wk price range                | RM11.7 - RM19.5 |
| Beta vs FBM KLCI (x)             | 1.04            |
| Monthly velocity (%)             | 0.00            |
| Monthly volatility (%)           | 8.30            |
| 3-mth average daily volume (m)   | 1.32            |
| 3-mth average daily value (RM'm) | 17.85           |
| Top Shareholders (%)             |                 |
| Employees Provident Fund Board   | 61.82           |
| OSK Holdings Bhd                 | 11.27           |
| Associated PNB Funds             | 1.85            |

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**Valuation and recommendation.** We observed that the impact of Covid-19 and MCO have already made an impact to 3QFY20 earnings despite the MCO only starting on 18<sup>th</sup> March. We expect to see further weakness to its performance in 4QFY20. However, we opine that loans growth may provide some moderation to the impact. Also, asset quality seems stable and GIL ratio appears manageable at current juncture. Taking everything into consideration, we are maintaining our **NEUTRAL** call for the stock with unchanged **TP of RM13.60**. Our TP is based on pegging its FY21 BVPS to 1.1x PBV. 

## INVESTMENT STATISTICS

| Financial year ending 30 June<br>(in RM'm, unless otherwise stated) | 2018A | 2019A | 2020E | 2021F | 2022F |
|---|-------|-------|-------|-------|-------|
| Net interest income (RM'm)  | 2,893 | 2,764 | 2,792 | 3,043 | 3,244 |
| Islamic banking income (RM'm)                                       | 646   | 707   | 693   | 714   | 735   |
| Non-interest income (RM'm)  | 1,300 | 1,254 | 1,330 | 1,414 | 1,441 |
| Total income (RM'm)   | 4,840 | 4,726 | 4,815 | 5,171 | 5,421 |
| Pretax profit (RM'm)  | 3,246 | 3,186 | 3,265 | 3,420 | 3,678 |
| Net profit  | 2,638 | 2,665 | 2,586 | 2,709 | 2,913 |
| Core Net profit (RM'm)  | 2,638 | 2,665 | 2,586 | 2,709 | 2,913 |
| Core EPS (sen)  | 128.7 | 130.0 | 126.4 | 132.4 | 142.4 |
| PER (x)   | 10.6  | 10.5  | 10.8  | 10.3  | 9.6   |
| Net Dividend (sen)  | 48    | 50    | 48    | 49    | 51    |
| Net Dividend Yield (%)  | 3.5   | 3.7   | 3.5   | 3.6   | 3.8   |
| Book value per share (sen)  | 11.68 | 12.45 | 12.89 | 12.96 | 13.51 |
| PBV (x)   | 1.2   | 1.1   | 1.1   | 1.0   | 1.0   |
| ROE (%)   | 11.3  | 10.8  | 10.0  | 10.2  | 10.8  |

Source: Company, MIDFR

### Some banking abbreviations used in this report:

CI = Cost to Income  
 CET1 = Common Equity Tier 1  
 GIL = Gross Impaired Loan  
 LD = Loan-Deposit  
 NII = Net Interest Income  
 NOII = Non-interest income  
 NIM = Net Interest margin  
 CASA = Current and Savings Accounts  
 COF = Cost of Funds  
 IB = Investment Banking  
 LLC = Loan Loss Coverage  
 PPOP = Pre-Provisioning Operating Profit  
 FVTPL = Fair Value Through Profit Or Loss  
 OPEX = Operating Expenses  
 OPR = Overnight Policy Rate

**Table 1: Quarterly & Cumulative results (base on reported financials)**

| FYE June (RM m)                        | Quarterly results |        |        |             |             | Cumulative results |         |             |
|--|-------------------|--------|--------|-------------|-------------|--------------------|---------|-------------|
|  | 3QFY20            | 2QFY20 | 3QFY19 | Yoy (+/- %) | Qoq (+/- %) | 9MFY20             | 9MFY19* | Yoy (+/- %) |
| Net Interest Income                    | 839               | 912    | 857    | -2.1%       | -8.0%       | 2,632              | 2,574   | 2.3%        |
| Non-interest Income                    | 290               | 326    | 309    | -6.3%       | -11.0%      | 949                | 894     | 6.2%        |
| Net/Total income                       | 1,129             | 1,238  | 1,166  | -3.2%       | -8.8%       | 3,582              | 3,468   | 3.3%        |
| OPEX                                   | (534)             | (527)  | (533)  | 0.2%        | 1.3%        | (1,583)            | (1,562) | 1.3%        |
| PPOP                                   | 595               | 711    | 641    | -7.2%       | -16.3%      | 1,999              | 1,906   | 4.9%        |
| Write back/(Provision) for loan losses | (124)             | (21)   | (4)    | >100%       | >100%       | (136)              | 35      | <-100%      |
| Share of profit from associate and JV  | 166               | 167    | 141    | 17.5%       | -0.6%       | 478                | 421     | 13.5%       |
| Pre-tax profit                         | 637               | 857    | 779    | -18.2%      | -25.7%      | 2,341              | 2,363   | -0.9%       |
| Net Profit                             | 535               | 702    | 634    | -15.6%      | -23.8%      | 1,925              | 1,938   | -0.7%       |

\* Excluding one-off gain on divestment of joint venture of RM90 mil in 9MFY19

**Table 2: Financial Ratios**

| Financial Ratios (%)        | 3QFY20 | 2QFY20 | 3QFY19 | Yoy (+/- ppts) | Qoq (+/- ppts) | 9MFY20 | 9MFY19* | Yoy (+/- ppts) |
|-----------------------------|--------|--------|--------|----------------|----------------|--------|---------|----------------|
| CET1 <sup>^</sup>           | 12.9   | 13.1   | 12.6   | 0.3            | -0.2           | 12.9   | 12.6    | 0.3            |
| Tier 1 Capital <sup>^</sup> | 13.5   | 13.7   | 13.6   | -0.1           | -0.2           | 13.5   | 13.6    | -0.1           |
| Total Capital <sup>^</sup>  | 15.7   | 15.9   | 16.4   | -0.7           | -0.2           | 15.7   | 16.4    | -0.7           |
| NIM                         | 1.84   | 2.04   | 2.00   | -0.16          | -0.20          | 1.97   | 1.98    | -0.01          |
| GIL                         | 0.98   | 0.84   | 0.8    | 0.18           | 0.14           | 0.98   | 0.8     | 0.18           |
| Loan loss Coverage          | 91     | 103    | 116    | -25            | -12            | 91     | 116     | -25            |
| Credit charge-off           | 0.35   | 0.05   | 0.01   | 0.34           | 0.3            | 0.13   | -0.05   | 0.18           |
| Cost to income              | 47.3   | 42.6   | 45.0   | 2.3            | 4.7            | 47.3   | 45.0    | 2.3            |
| Net LD                      | 84.8   | 84.6   | 82.0   | 2.8            | 0.2            | 84.8   | 82.0    | 2.8            |
| ROEA                        | 8.2    | 10.8   | 10.3   | -2.1           | -2.6           | 9.9    | 10.6    | -0.7           |

<sup>^</sup>After deducting proposed dividend

\* Excluding one-off gain on divestment of joint venture of RM90 mil in 9MFY19

**Table 3: PBT by key segments (based on reported financials)**

| PBT (RM m)                           | 9MFY20  | 9MFY19  | Yoy (+/- %) |
|--------------------------------------|---------|---------|-------------|
| Personal Financial Services          | 853.4   | 846.0   | 0.9%        |
| Business and Corporate Banking       | 584.4   | 613.5   | -4.7%       |
| Global Markets                       | 405.7   | 268.4   | 51.2%       |
| International Banking                | (29.3)  | 28.4    | <-100%      |
| Others and Inter-Segment Elimination | 48.6    | 275.2   | -82.4%      |
| Total segment profit before tax      | 1,862.4 | 2,031.6 | -8.3%       |

Source: Company, MIDFR

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### MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

#### STOCK RECOMMENDATIONS

|                     |  |
|---------------------|--|
| <b>BUY</b>          | Total return is expected to be >10% over the next 12 months.   |
| <b>TRADING BUY</b>  | Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.  |
| <b>NEUTRAL</b>      | Total return is expected to be between -10% and +10% over the next 12 months.  |
| <b>SELL</b>         | Total return is expected to be <10% over the next 12 months.   |
| <b>TRADING SELL</b> | Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow. |

#### SECTOR RECOMMENDATIONS

|                 |  |
|-----------------|--|
| <b>POSITIVE</b> | The sector is expected to outperform the overall market over the next 12 months.   |
| <b>NEUTRAL</b>  | The sector is to perform in line with the overall market over the next 12 months.  |
| <b>NEGATIVE</b> | The sector is expected to underperform the overall market over the next 12 months. |