BANKING

Maintain POSITIVE

Surprise timing of a cut

KEY INVESTMENT HIGHLIGHTS

- **Bank Negara Malaysia announced another 25bp OPR cut yesterday**
- **NIM compression is a given. Furthermore, normalisation could take slightly longer (by 2 quarters) than previously anticipated**
- **Banks could have already anticipated the rate cuts and would have likely manoeuvred early. There is a possibility that banks did not fervently accumulate fixed deposits given the timing of the second OPR cut this year**
- **NOII growth from treasury activities could moderate the impact**
- **This OPR cut would have already been priced in but banks remains undervalued**
- **We maintain our POSITIVE stance in the banking sector**

Timing of the OPR cut was a surprise. Bank Negara Malaysia announced another cut to its Overnight Policy Rate (OPR) of 25bp yesterday, bringing the OPR to 2.50%. While we had expected another OPR cut to follow the reduction in Jan-20, we expect it would have been in May-20. Nevertheless, magnitude of the cut was as per our economics team's expectation.

OPR cut is more pre-emptive. We believe that the OPR was not a signal of any imminent recession. Our economics team expect that GDP will continue to grow this year, albeit at a slower pace when compared against last year. In our view, the second OPR cut was a pre-emptive measure to stimulate growth against the backdrop of the intensifying of the Covid-19 outbreak.

Margin compression is a given. An OPR cut will have a negative impact to banks' earnings from downward pressure in net interest income (NII) due to net interest margin (NIM) compression. This is due to the fact that there will be a near-immediate downward adjustment to loans and financing which has a floating rate, while term deposits (such as fixed deposits) are re-priced after maturity. The floating rate loans, on average, contributed circa 79.2% of total loans book of banks under our coverage as at end December 2019.

Table 1: Banks' Percentage of Floating Rate Loans & Casa Ratio as at end December-19

Banks	Percentage of floating rate loans	CASA ratio
Maybank	71.9%	34.4%
Public	78.4%	25.1%
CIMB	84.8%	35.1%
Hong Leong Bank	81.8%	26.1%
RHB	88.6%	25.7%
AMMB	75.8%	23.4%
BIMB	90.7%	33.4%
Alliance Bank	83.0%	37.5%
Affin	71.5%	19.1%
Average	79.2%	30.2%

Source: Company, MIDFR

COMPANY IN FOCUS

Malayan Banking Bhd
Maintain **BUY |** Unchanged Target price: RM9.55
Price @ 3rd March 2020 : RM8.41

- Low exposure to floating rate which should moderate OPR cut impact
- It has scale and size
- Attractive dividend yield of circa 6%

Share price chart

CIMB Group Holdings Bhd
Maintain **BUY |** Unchanged Target price: RM5.70
Price @ 3rd March 2020 : RM4.50

- Earning recovery in Indonesia and Thailand
- Robust net income
- Relatively undemanding valuation
- Decent dividend yield of circa 5%

Share price chart

ANALYST
Imran Yassin Yusof
imran.yassin@midf.com.my
03 -2173 8395

Possibility of no intense accumulation of fixed deposits. Nevertheless, it could be that banks have not yet accumulated aggressively on fixed deposits (FD) given the short time period between OPR cuts. In our opinion, banks would have positioned itself due to expectation of another OPR cut after the May-19 OPR reduction. In fact, we observed that FD growth have been on a downtrend since the May-19 OPR cut.

Table 2: Banking System Deposits by Type

	Total deposits (RM b)	Growth (yoy)	CASA (RM b)	Growth (yoy)	CASA Ratio	FD (RM b)	Growth (yoy)
Jan-19	1,906.2	7.4%	497.6	0.9%	26.1%	979.4	11.8%
Feb-19	1,914.3	7.7%	498.4	1.5%	26.0%	986.6	11.9%
Mar-19	1,927.4	6.6%	500.7	2.7%	26.0%	994.6	11.2%
Apr-19	1,940.6	5.2%	499.8	2.8%	25.8%	1003.8	8.3%
May-19	1,943.0	5.3%	508.0	4.6%	26.1%	997.3	7.9%
Jun-19	1,937.5	4.7%	506.6	4.4%	26.1%	1000.3	7.7%
Jul-19	1,944.5	4.8%	507.4	5.3%	26.1%	999.2	6.6%
Aug-19	1,948.8	4.5%	506.7	5.2%	26.0%	1006.8	5.9%
Sep-19	1,952.7	4.2%	514.2	6.5%	26.3%	1013.1	5.9%
Oct-19	1,963.8	3.9%	512.4	5.5%	26.1%	1011.2	5.3%
Nov-19	1,956.4	2.8%	515.5	5.5%	26.3%	1001.9	4.0%
Dec-19	1,970.6	3.1%	530.4	6.7%	26.9%	1002.3	2.8%
Jan-20	1,961.2	2.9%	525.3	5.6%	26.8%	1004.0	2.5%

Source: Bank Negara Malaysia

In addition, less fervent deposits competition will likely continue. The requirement to meet the Net Stable Funding Ratio (NSFR) as prescribed by BNM played a key factor in banks accumulating deposits in CY18 and early parts of CY19. We understand that all the banks under our coverage have complied with the NSFR requirement. As such, we opine that banks will be less keen to fight aggressively for deposits. Consequently, we expect there will not be undue deposits competition in CY20.

Normalisation could be slightly longer than expected. With the earlier OPR cut in Jan-20, we had expected the possibility of NIM recovery in one quarter. However, since there are now two successive OPR cuts, we expect that NIM normalisation could take longer. We opine that it could take 2 quarters before NIM would normalise. We estimate the impact of a 25bp OPR cut will reduce NIM by 5bp on average. This may translate to an average circa 3% downward impact to earnings estimate for the year. With another 25bp OPR cut yesterday, NIM could compress on average 10bp or circa 6% to earnings estimate. However, this is predicated that the OPR reduction was a surprise one. Since the Jan-20 OPR cut may have been largely anticipated the impact could be muted. Furthermore, we posit that banks may have also anticipated a second OPR cut this year. In combination of the possibility of slower pace of FD accumulation, impact of the OPR cuts could be subdued still. All-in, we expect the final impact will be circa 5bp compression to NIM for FY20.

Loans growth will be sluggish this year. We expect NII could still come under pressure as loans growth could be sluggish this year. This is predicated upon the cautiousness and disruption caused by the Covid-19 outbreak, especially on businesses. The banking system loans also continued to be on a downtrend.

Table 3: Banking System Loans by Selective Purpose

	Total loans (RM b)	Growth (yoy)	Growth (yoy) on selected loans purpose			
			Purchase of passenger cars	Purchase of residential property	Personal use	Working capital
Jan-19	1,711.1	7.5%	-0.2%	8.2%	37.0%	5.8%
Feb-19	1,708.5	7.0%	-0.5%	7.9%	36.4%	5.5%
Mar-19	1,715.0	7.0%	-0.3%	7.9%	35.6%	4.7%
Apr-19	1,715.7	4.5%	-0.5%	7.1%	3.4%	3.0%
May-19	1,721.9	4.5%	0.2%	7.3%	3.3%	3.3%
Jun-19	1,728.4	4.2%	-0.3%	7.1%	4.2%	2.3%
Jul-19	1,728.8	3.9%	-0.8%	7.0%	2.9%	1.6%
Aug-19	1,739.0	3.9%	-1.6%	7.1%	2.8%	2.1%
Sep-19	1,747.5	3.8%	-1.7%	7.2%	2.8%	1.6%
Oct-19	1,751.7	3.7%	-1.5%	7.2%	2.7%	1.3%
Nov-19	1,759.1	3.7%	-1.2%	7.3%	2.8%	1.3%
Dec-19	1,771.6	3.9%	-1.0%	7.3%	3.1%	1.0%
Jan-20	1,770.5	3.5%	-0.8%	7.2%	3.0%	-0.4%

Source: Bank Negara Malaysia

NOII could moderate the impact. We expect that the pressure to NII could be moderated by robust growth of non-interest income (NOII), due to treasury activities. Based on the CY19 earnings review of banks under our coverage, we noted a trend of strong NOII growth. We observed Malaysia Government bond yields have fallen and this could portend similar trend this year.

Already imputed the impact of a second OPR cut. We are not making any adjustments to our earnings forecast for banks under our coverage. This is due to the fact that we have already imputed another OPR cut this year and made adjustments during our recent review of banks' earnings.

Banks continue to be undervalued. In our opinion, the impact of this OPR cut have also been fully priced in earlier given the price reaction of banking stocks under our coverage. Nevertheless, we view that banking stocks in general are relatively still undervalued. Majority of the banks are trading below its 5-year historical average. We opine that this is unjustified given that in our view, banks have thus far managed to navigate the headwinds the sector had faced and will likely continue to do so.

Monitoring asset quality. One metrics that could be affecting banks' valuation is asset quality. This could be due the potential impact of the Covid-19 outbreak. Also, with the slowing economic growth, banks would have to make some judgmental provisioning. Yet, we observed that bank's asset quality have been stable so far. Furthermore, there are some leeway given to banks, as we understand that rescheduled and restructuring of SME accounts do not have to be classified as impaired.

Cautiously optimistic, maintain POSITIVE for now. Based on the ability of banks in general to navigate the headwinds it faced, we opine that banking stocks are undeservedly undervalued currently. Hence, we are cautiously optimistic and maintain our POSITIVE stance at the moment. However, we are cognizant of the potential headwinds this year coming from the risk to asset quality. Not to mention the increase volatility of share price performance. Therefore, our top picks for this sector will banks with scale and size or the potential to maintain its earnings momentum. These are **Maybank (BUY, TP: RM9.55)**, **CIMB (BUY, TP: RM5.70)** and **RHB Bank (BUY, TP: RM6.30)**. Good dividends yields will be an added bonus.

PEER COMPARISON TABLE

	FYE	Rec.	Price @ 3/3/20	Target Price	EPS (sen)		PER		Net DPS		Net Div Yield		BV		PBV	
					20	21	20	21	20	21	20	21	20	21	20	21
Maybank	Dec	BUY	8.41	9.55	71.6	71.2	11.7	11.8	56.0	56.0	6.7	6.7	7.3	7.6	1.1	1.1
Public Bank	Dec	T. BUY	17.76	19.00	144.3	146.5	12.3	12.1	73.0	73.0	4.1	4.1	11.9	12.5	1.5	1.4
CIMB	Dec	BUY	4.50	5.70	51.0	52.0	8.8	8.7	26.0	26.0	5.8	5.8	5.7	5.9	0.8	0.8
RHB Bank	Dec	BUY	5.64	6.30	66.1	69.8	8.5	8.1	31.0	31.0	5.5	5.5	6.5	6.6	0.9	0.9
Hong Leong	Jun	BUY	15.60	17.00	136.6	143.9	11.4	10.8	52.0	54.0	3.3	3.5	12.9	13.2	1.2	1.2
AMMB	Mar	T. BUY	3.63	4.20	46.6	48.5	7.8	7.5	22.0	24.0	6.1	6.6	6.0	6.1	0.6	0.6
Affin	Dec	NEUTRAL	1.78	1.87	27.0	27.0	6.6	6.6	7.0	8.0	3.9	4.5	4.7	4.8	0.4	0.4
Alliance	Mar	T. BUY	2.23	2.70	28.6	34.3	7.8	6.5	14.5	17.0	6.5	7.6	3.9	3.9	0.6	0.6
BIMB	Dec	BUY	3.73	5.05	50.5	51.3	7.4	7.3	18.0	18.0	4.8	4.8	3.5	3.8	1.1	1.0
Average					**69.1**	**71.6**	**9.2**	**8.8**	**33.3**	**34.1**	**5.2**	**5.5**	**6.9**	**7.2**	**0.9**	**0.9**

DISCLOSURES AND DISCLAIMER

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.
SECTOR RECOMMENDATIONS	
POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.