

BANKING

Downgrade to NEUTRAL

(from POSITIVE)

The worry is on asset quality

KEY INVESTMENT HIGHLIGHTS

- Bank Negara Malaysia announced a 50bp OPR cut yesterday
- Net interest margin compression will continue pressuring net interest income
- Impact muted due to less intense deposits competition
- Loans growth will be sluggish this year
- Worry now is on asset quality
- Earnings and target price revisions to reflect the potential higher credit cost and NIM compression
- We downgrade our stance in the banking sector to NEUTRAL

OPR cut largely expected. Bank Negara Malaysia announced a cut to its Overnight Policy Rate (OPR) of 50bp yesterday. This was relatively anticipated given current situation of Covid-19 pandemic and the expected economic fallout.

Continued margin compression. 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%
<i>Average</i>	79.2%	30.2%

Source: Company, MIDFR

No intense accumulation of fixed deposits. Nevertheless, it could be that banks have not accumulated aggressively on fixed deposits (FD). 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 a downtrend in FD growth since the May-19 OPR cut. Furthermore, with the loan moratorium and the expectation of tepid loans, banks will not have to accumulate deposits to fund the loans growth.

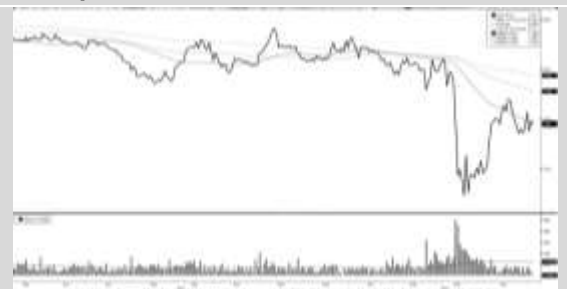
COMPANY IN FOCUS

Malayan Banking Bhd

Maintain **BUY** | Revised Target price: RM8.00
Price @ 5th May 2020: RM7.48

- Likelihood of stable asset quality and credit cost
- Scale and size
- D-SIB bank means support
- Attractive dividend yield

Share price chart



CIMB Group Holdings Bhd

Maintain **BUY** | Unchanged Target price: RM4.30
Price @ 5th May 2020: RM3.43

- Scale and size
- D-SIB bank means support
- Relatively undemanding valuation as it is trading below 1x PBV
- Decent dividend yield

Share price chart



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%	1,003.8	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%	1,000.3	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%	1,006.8	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%	1,011.2	5.3%
Nov-19	1,956.4	2.8%	515.5	5.5%	26.3%	1,001.9	4.0%
Dec-19	1,970.6	3.1%	530.4	6.7%	26.9%	1,002.3	2.8%
Jan-20	1,961.2	2.9%	525.3	5.6%	26.8%	1,004.0	2.5%
Feb-20	1,963.2	2.6%	527.0	5.7%	26.8%	1,008.3	2.2%

Source: Bank Negara Malaysia

Providing support to the economy. In our opinion, the intended effect for the OPR cut is to ensure more disposable income for consumers and reduce cash flow pressure for businesses. With the lower borrowing cost, consumer will pay less for their loans which will translate to more disposable income. It is hoped that this additional income will induce consumer to spend, which is an important factor to reignite the economy. It is also hoped that the OPR cut will induce loans growth.

Loans growth will be sluggish this year. We expect NII could still come under pressure from the NIM compression and the sluggish loans growth this year. Nevertheless, 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.

A time to worry on asset quality. We believe that the concern on NII is somewhat superfluous at the moment given that the Covid-19 will have a far reaching impact to the economy and thus the banking system. In our opinion, the question should be on the asset quality of the banks. The loan moratorium does give breathing space for the consumer as well as the banks, ensuring delinquency kept at bay and gross impaired loans to a minimum. However, since then we have seen extensions to the Movement Control Order (MCO) which will have an impact due to stalled economic activities. In turn this will have an impact to asset quality of banks. The severity will depend on how fast the economy can recover and rebound from the MCO.

No significant spike in credit cost for now but banks may take the opportunity. We believe that another effect of the loan moratorium will be on provisions as previously; the accounts under moratorium will likely be classified as rescheduled & restructured (R&R) accounts which will have to classify as impair, hitting banks' P&L via provisions. However, we believe that BNM will have given leniency to the banks as moratorium accounts will likely not be considered R&R, ensuring that credit cost will not spike up for now. Nevertheless, these credit cost could rise later after the end of the moratorium period. Also, we do not discount banks taking the opportunity to increase its provision levels given the uncertainty of the Covid-19 situation. We have observed this trend in the earnings release of global banks.

Revision to earnings; taking into account OPR cuts and likelihood of higher provisions. We are taking into account of yesterday's 50bp cut in OPR, and another potential 25bp cut. As such, we are factoring an average NIM compression of -20bp for the banks under our coverage. We are also increasing the credit cost of the banks by an average of +12bp. As a result, we are revising our FY20 and FY21 aggregate banking earnings forecast downwards by -15.8% and -9.4% respectively.

Table 3: Aggregate Banking Earnings Revision

	FYE	Pre-adjustment PATAMI (RM m)		Post adjustment PATAMI (RM m)		Percentage change	
		FY20	FY21	FY20	FY21	FY20	FY21
Maybank	Dec	8,392	8,608	7,469	8,180	-11.0%	-5.0%
CIMB*	Dec	5,206	5,565	3,678	4,399	-29.3%	-20.9%
Public	Dec	5,603	5,687	4,890	5,397	-12.7%	-5.1%
RHB	Dec	2,650	2,800	2,191	2,633	-17.3%	-6.0%
Hong Leong	June	2,793	2,943	2,582	2,707	-7.6%	-8.0%
AMMB	Mar	1,401	1,460	1,197	1,383	-14.5%	-5.2%
Alliance	Mar	438	525	348	409	-20.6%	-22.0%
Affin	Dec	516	534	464	486	-10.0%	-9.0%
BIMB	Dec	827	840	601	543	-27.3%	-35.4%
Total		27,826	28,962	23,420	26,248	-15.8%	-9.4%

Source: MIDFR

* **Note: Revision was done on 29 April 2020 during a corporate update report**


Target price and call revision. As a result of the earnings revision, we are also revising the target prices of the banks under our coverage in this report. The only exception is for **CIMB (BUY, TP: RM4.30)** which we had revised last week following a corporate update. The changes are as per the table below:

Table 4: Revision to Recommendation and Target Price of Banks Under Coverage

	Pre-adjustment Recommendation	Post adjustment Recommendation	Pre-adjustment TP (RM)	Post adjustment TP (RM)
Maybank	BUY	BUY	9.55	8.00
CIMB*	BUY	BUY	5.70	4.30
Public	TRADING BUY	TRADING BUY	19.00	17.00
RHB	BUY	BUY	6.30	5.10
Hong Leong	BUY	NEUTRAL	17.00	13.60
AMMB	TRADING BUY	TRADING BUY	4.20	3.60
Alliance	TRADING BUY	NEUTRAL	2.70	2.05
Affin	NEUTRAL	NEUTRAL	1.87	1.55
BIMB	BUY	BUY	5.05	4.05

Source: MIDFR

* **Note: Revision was done on 29 April 2020 during a corporate update report**

Downgrade the sector to NEUTRAL. While we were cautiously optimistic of the banking sector's prospects, we had a change of tune due to the prolonged MCO. We understand that the MCO restrictions have been relaxed slightly but we foresee that it will take some time for the situation to return to normal. All this will have a downside impact to the economy and this will affect the banks through higher credit cost. As such, we are downgrading our sector call to NEUTRAL (from POSITIVE). Our top picks are the three D-SIB banks due to its solid fundamental, scale and size. Also, being systematically important banks will ensure support should there be any stress to asset quality. Hence, we favour **Maybank (BUY, TP: RM8.00), CIMB (BUY, TP: RM4.30)** and **Public Bank (TRADING BUY, TP: RM17.00)**. Additionally, attractive dividend yield will also cushion any downside risk. A re-rating catalyst would be faster than expected recovery of the economy. 

PEER COMPARISON TABLE

	FYE	Rec.	Price @	Target	EPS (sen)		PER		Net DPS		Net Div Yield		BV (RM)		PBV	
			5-May	Price	20	21	20	21	20	21	20	21	20	21	20	21
Maybank	Dec	BUY	7.48	8.00	66	73	11.3	10.3	50	56	6.7	7.5	7.26	7.43	1.0	1.0
Public Bank	Dec	T. BUY	16.06	17.00	126	139	12.7	11.6	70	73	4.4	4.5	11.74	12.25	1.4	1.3
CIMB	Dec	BUY	3.43	4.30	37	44	9.2	7.7	17	22	4.9	6.5	5.62	5.64	0.6	0.6
RHB Bank	Dec	BUY	4.67	5.10	55	66	8.5	7.1	31	31	6.6	6.6	6.42	6.50	0.7	0.7
Hong Leong Bank	Jun	NEUTRAL	13.30	13.60	126	132	10.5	10.1	52	54	3.9	4.1	12.84	12.98	1.0	1.0
AMMB	Mar	T. BUY	2.94	3.60	40	46	7.4	6.4	16	18	5.4	6.2	5.97	6.05	0.5	0.5
Affin Bank	Dec	NEUTRAL	1.53	1.55	24	24	6.3	6.3	5	8	3.3	5.2	4.65	6.75	0.3	0.2
Alliance	Mar	NEUTRAL	1.99	2.05	22	26	8.9	7.5	11	12	5.4	6.0	3.79	3.80	0.5	0.5
BIMB	Dec	BUY	3.22	4.05	34	31	9.4	10.5	12	12	3.7	3.7	3.36	3.51	1.0	0.9
Average					59	65	9.4	8.6	29	32	4.9	5.6	6.85	7.21	0.8	0.8

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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 <i>rise</i> 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 <i>fall</i> 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.