BANKING

***Maintain* NEUTRAL**

NIM compression will be minimal from this OPR cut

KEY INVESTMENT HIGHLIGHTS

- **Bank Negara Malaysia announced a 25bp OPR cut yesterday**
- **Net interest margin compression will likely be muted this time around**
- **Benign deposits competition and depositors preferring CASA**
- **Loans growth will be sluggish this year**
- **All eyes will be on asset quality especially post loan moratorium**
- **We maintain our NEUTRAL stance in the banking sector**

OPR cut largely expected. Bank Negara Malaysia (BNM) announced another cut to its Overnight Policy Rate (OPR) of 25bp yesterday. This latest move by BNM was widely anticipated by our economics team and consensus given current situation of Covid-19 pandemic and the expected economic fallout. We have already imputed this cut to our earnings forecast for the banks under our coverage.

Normally there would be margin compression… In normal circumstance, 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. Floating rate loans, on average, contributed circa 79.3% of total loans book of banks under our coverage as at end March-20.

…but impact this time around will likely be minimal. Nevertheless, we opine that the impact of this OPR cut to banks' NIM will likely be muted. This is due to: (1) the OPR cut was widely expected and banks would have adjusted its pricing and strategy accordingly, (2) relaxation of regulatory requirements such as the Liquidity Coverage Ratio and Net Stable Funding Ratio which mean there is less need for banks to fight for deposits, and (3) depositors may be unwilling to lock in deposits for longer term and prefer CASA for now.

No intense accumulation of fixed deposits. 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.

Unwilling to lock in deposits. Recall, the total system deposits grew at +2.7%yoy as at May CY20. CASA grew at faster pace of +13.7%yoy from +12.6%yoy while fixed deposits contracted for the third consecutive month. It fell -1.3%yoy to RM984.3b. We believe that this suggest that depositors were reluctant to tie-up their cash flows and the desire to maintain liquidity given the uncertain conditions as a result of Covid-19.

COMPANY IN FOCUS

Malayan Banking Bhd
Maintain **BUY |** Revised Target price: RM8.20
Price @ 7th July 2020: RM7.82

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

Share price chart

BIMB Holdings Bhd
Maintain **BUY |** Unchanged Target price: RM4.25
Price @ 7th July 2020: RM3.52

- Stable asset quality
- Stable borrowers' profile
- Strong loans growth

Share price chart

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

FIGURE 1: BANKS' PERCENTAGE OF FLOATING RATE LOANS & CASA RATIO AS AT END MARCH-20

Banks	Percentage of floating rate loans	CASA ratio
Maybank	72.1%	36.8%
Public	78.6%	25.4%
CIMB	83.9%	37.3%
Hong Leong Bank	82.1%	26.4%
RHB	89.4%	27.4%
AMMB	76.4%	25.5%
BIMB	91.3%	36.5%
Alliance Bank	83.3%	37.4%
Affin	72.3%	18.0%
Average	79.3%	31.7%

Source: Company, MIDFR

FIGURE 2: BANKING SYSTEM TOTAL DEPOSITS and DEPOSITS GROWTH

	Total deposits (RM b)	Growth (yoy)	CASA (RM b)	Growth (yoy)	CASA Ratio
Jan-19	1,906.2	7.4%	497.6	0.9%	26.1%
Feb-19	1,914.3	7.7%	498.4	1.5%	26.0%
Mar-19	1,927.4	6.6%	500.7	2.7%	26.0%
Apr-19	1,940.6	5.2%	499.8	2.8%	25.8%
May-19	1,943.0	5.3%	508.0	4.6%	26.1%
Jun-19	1,937.5	4.7%	506.6	4.4%	26.1%
Jul-19	1,944.5	4.8%	507.4	5.3%	26.1%
Aug-19	1,948.8	4.5%	506.7	5.2%	26.0%
Sep-19	1,952.7	4.2%	514.2	6.5%	26.3%
Oct-19	1,963.8	3.9%	512.4	5.5%	26.1%
Nov-19	1,956.4	2.8%	515.5	5.5%	26.3%
Dec-19	1,970.6	3.1%	530.4	6.7%	26.9%
Jan-20	1,961.2	2.9%	525.3	5.6%	26.8%
Feb-20	1,963.2	2.6%	527.0	5.7%	26.8%
Mar-20	1,968.2	2.1%	552.3	10.3%	28.1%
Apr-20	1,985.7	2.3%	562.5	12.6%	28.3%
May-20	1,996.0	2.7%	577.4	13.7%	28.9%

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. The banking system loans growth has been robust thus far. As at May-20, loans growth came in at 3.9%yoy to RM1.79t. However, we believe that this was due to lack of repayments stemming from the loan moratorium. Going forward, loans growth could come under pressure after the end of the loan moratorium period, and repayments restarts. In our opinion, there will be less demand for loans given the uncertain economic conditions and consumer shift towards necessities from discretionary spending. Nevertheless, the pent-up consumption during the RMCO period could carry the loans growth in 2HCY20. In tandem with the GDP performance, we are estimating a loans growth of 2% for CY20.

All eyes 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 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.

Provisions will weigh down banks' earnings. 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. We have observed that banks' earnings in 1QCY20 saw year-on-year contraction due to higher provisions as banks' take into account the macro economic factors stemming from the impact of Covid-19. Bear in mind, we saw only circa 2 weeks of MCO in 1QCY20. Therefore, we expect earnings will continue to be weighed by elevated provisions.

Asset quality expected to deteriorate post loan moratorium. We believe the other effect of the ending of the loan moratorium in 2HCY20 will be on asset quality. We expect gross impaired loans (GIL) ratio to spike up post loan moratorium. While economic recovery is currently underway, we opine that it is too short of time period for some businesses to regenerate the loss of income during the MCO. This will be in tandem with the increase in provisions.

Maintain NEUTRAL. We maintain our **NEUTRAL** stance as we expect the various forms MCO will have an impact to the economy. This will have an impact to loans growth and asset quality. Also, we foresee that it will take some time for the situation to return to normal. However, we do not foresee exacerbated stress to the banking sector as it face current headwinds on a position of strength. Our top picks are **Maybank (BUY, TP: RM8.20)** due to its solid fundamental, scale and size. Also, being systematically important banks will ensure support should there be any stress to asset quality. Also, we favour **BIMB (BUY, TP: RM4.25)** due to its asset quality which we expect to be stable on account of its borrower's profile. A re-rating catalyst would be faster than expected recovery of the economy.

PEER COMPARISON TABLE

	FYE	Rec.	Price @ 7-Jul	Target Price	EPS (sen)		PER		Net DPS		Net Div Yield		BV (RM)		PBV	
					20	21	20	21	20	21	20	21	20	21	20	21
Maybank	Dec	BUY	7.82	8.20	61	66	12.9	11.8	36	43	4.6	5.5	7.36	7.50	1.1	1.0
Public Bank	Dec	BUY	17.40	17.20	127	141	13.7	12.4	74	73	4.3	4.2	11.75	12.27	1.5	1.4
CIMB	Dec	T. BUY	3.70	3.95	24	36	15.4	10.3	12	18	3.2	4.9	5.62	5.66	0.7	0.7
RHB Bank	Dec	BUY	4.98	5.25	54	64	9.3	7.8	22	25	4.4	5.0	6.42	6.56	0.8	0.8
Hong Leong Bank	Jun	NEUTRAL	14.46	13.60	126	132	11.4	10.9	48	49	3.3	3.4	12.89	12.96	1.1	1.1
AMMB	Mar	T. BUY	3.20	3.60	45	42	7.2	7.6	13	15	4.2	4.7	6.18	6.23	0.5	0.5
Affin Bank	Dec	NEUTRAL	1.57	1.65	24	24	6.5	6.5	5	5	3.2	3.2	4.66	4.79	0.3	0.3
Alliance	Mar	NEUTRAL	2.20	2.05	27	26	8.0	8.3	6	9	2.7	4.2	3.87	3.92	0.6	0.6
BIMB	Dec	BUY	3.52	4.25	43	44	8.3	8.0	19	20	5.4	5.7	3.73	3.88	0.9	0.9
Average					**59**	**64**	**10.3**	**9.3**	**26**	**29**	**3.9**	**4.5**	**6.94**	**7.09**	**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 *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.