8 May 2019 | Sector Update

BANKING

***Maintain* POSITIVE**

Impact may be muted on surprise OPR cut

INVESTMENT HIGHLIGHTS

- **Surprising OPR cut as we had expected no policy action given the robust domestic spending, continuous pick-up in commodity prices and stable labour market**
- **Margin compression expected in the short term but this will eventually normalise**
- **Banks with higher contribution of floating rate loans to its loans book will be impacted the most**
- **There will be a knee jerk reaction to banking stock prices but there is still value for banking stocks with solid fundamentals**
- **We maintain our POSITIVE stance in the banking sector**

Surprised OPR cut. We are caught by surprised by Bank Negara Malaysia's (BNM) decision to cut the OPR rate by -25bp to 3.00%. The bases for our earlier expectations of no OPR action were the robust domestic spending, continuous pick-up in commodity prices and stable labour market. However, BNM indicated that latest developments point towards moderate economic activity in 1QCY19. This could have prompted the rate cut.

Margin compression in the short term. While we observed the OPR hike providing a short term boost to net interest margin (NIM) last year, there will be a reverse following the OPR cut. This is due to the fact that there will be a near-immediate downward adjustment to loans and financing which has a floating rate. The floating rate loans, on average, contributed circa 78.3% of total loans book of banks under our coverage as at end 2018.

NIM will eventually normalise. While NIM will be impacted by the lower lending rate, as mentioned in our recent thematic report titled "Malaysia's Monetary Policy & the Impact to the Banking Sector", we mentioned that it will normalise within 2 to 3 quarters. This is due to the fact that cost of fund will also decrease, in particular adjustment to the fixed deposit rates which had been contracted before the OPR cut. Also, based on market conditions, banks may not fully translate the full quantum of the OPR cut to borrowers and savers. We observed that previous the OPR cut in 2016 had translated into a decrease of -12bp in Base Lending Rate the following month, instead of -25bp as per the OPR cut then.

NIM impact will not be substantial. We expect the average NIM to come down by -2bp to -3bp for 2019 based on 1 quarter impact of base rate downward revision. However, we noted that several banks have increased its base rate circa end 2018 or 1QCY19 (on average by 10bp). Given the OPR cut, these base rates could revert to last year levels.

Table 1: Banks' Percentage of Floating Rate Loans & Casa Ratio as at end Dec-18

Banks	Percentage of floating rate loans	CASA ratio
Maybank	71.6%	35.1%
Public	77.6%	26.4%
CIMB	84.1%	33.4%
Hong Leong Bank	80.7%	24.8%
RHB	85.7%	25.9%
AMMB	74.3%	20.7%
BIMB	91.0%	30.4%
Alliance Bank	89.9%	38.1%
Affin	67.2%	17.6%
Average	*78.3%*	*30.0%*

Source: Company, MIDFR

Banks with higher floating rate loans will be impacted the most. We expect that earnings for banks will be negatively affected from the short term pressure to NIM. However, it won't to be significant. On average, we estimate a -3.0% decline to the earnings of banks under our coverage compared against our previous forecast. Banks with higher floating rate loans to be impacted the most. We believe that **BIMB Holdings Bhd (BUY, TP: RM4.85)** and **Alliance Bank Malaysia Bhd (BUY, TP: RM4.75)** to see a higher drag to its earnings as its floating rate loans comprised 91.0% and 89.9% of its loans book respectively. Meanwhile, we expect less muted impact for **Maybank (BUY, TP: RM11.40)** due to more geographically diversified loan exposures and **Affin Bank (BUY, TP: RM2.70)** due to less exposure in floating rate loans.

Table 2: Estimated Impact of OPR Cut on FY19/20 Earnings Forecast of Banks

Banks	FY19/FY20 Net Profit forecast Pre-OPR cut (RM m)	FY19/FY20 Net Profit forecast Post-OPR cut (RM m)	Change
Maybank	8,591	8,377	-2.5%
Public	5,701	5,564	-2.4%
CIMB	4,991	4,822	-3.4%
Hong Leong Bank*	2,927	2,819	-3.7%
RHB	2,500	2,399	-4.1%
AMMB*	1,401	1,360	-2.9%
BIMB	687	659	-4.1%
Alliance Bank*	609	575	-5.6%
Affin	559	549	-1.8%

* denotes impact on FY20 earnings of banks as FYs of these banks end on Mar/June. For the rest, the impact will be on FY19 earnings

Source: MIDFR

Potential booster for loans growth. One of the possible upside from any OPR cut will be a boost to loans growth due to higher loans demand. This could be due to borrowers taking advantage of the better rates. However, we do not believe that the steep upswing in loans demand as loan affordability will continue to be a determinant. Hence, we are maintaining our loans growth expectations of 4.7%.

Manoeuvring a potential OPR cut. We believe that there are still room for an investor to manoeuvre despite the OPR cut. We believe that investors could consider banks with low exposure in floating rate in its loans book, have a geographically diversified loans book and offer solid dividend yield. Applying these criteria, we opine that Maybank is a good candidate. We have a **BUY** call with **TP of RM11.40** for **Maybank**.

Maintain POSITIVE. We maintain our cautious optimism for the banking sector this year. As we mentioned, we believe that banks will be able to continue its earnings momentum at current juncture despite the pressure on margin. This is due to continued loans growth. Meanwhile, stable asset quality will contain banks' provision levels. We expect there will be a knee jerk reaction to the share prices of banking stocks under our coverage. However, we believe there is an opportunity for investors to pick on banking stocks which have solid fundamentals. Therefore, our top picks for this sector are; (1) **Maybank (BUY, TP: RM11.40)** as we expect the impact of the OPR cut to be muted and its dividend yield of circa 6% will limit any downside risk, (2) **CIMB (BUY, TP: RM7.55)** on the recovery of its Indonesian operation and value play, and (3) **Public Bank (BUY, TP: RM27.15**) due to its solid asset quality.

Table 3: PEER COMPARISON FOR MALAYSIAN BANKING STOCKS

	Rec.	Price @ 7/5 (RM)	TP (RM)	EPS (sen)		PER (x)		Net DPS (sen)		Net Div Yield (%)		BV (RM)		PBV (x)	
				18	19	18	19	18	19	18	19	18	19	18	19
Maybank	BUY	8.99	11.40	75.9	74.3	11.8	12.1	59.0	59.0	6.6	6.6	7.1	7.3	1.3	1.2
Public Bank	BUY	22.48	27.15	147.6	147.4	15.2	15.3	72.0	73.0	3.2	3.2	11.2	11.9	2.0	1.9
CIMB	BUY	5.20	7.55	50.0	47.3	10.4	11.0	26.0	25.0	5.0	4.8	5.6	5.7	0.9	0.9
RHB Bank	BUY	5.69	6.10	62.4	64.9	9.1	8.8	20.0	20.0	3.5	3.5	6.3	6.5	0.9	0.9
Hong Leong	NEUTRAL	19.80	20.30	135.8	137.8	14.6	14.4	49.0	50.0	2.5	2.5	12.5	13.4	1.6	1.5
AMMB	NEUTRAL	4.44	4.50	45.4	45.2	9.8	9.8	18.0	18.0	4.1	4.1	5.6	5.8	0.8	0.8
Affin	BUY	2.17	2.70	29.0	28.5	7.5	7.6	5.0	7.0	2.3	3.2	4.7	4.8	0.5	0.4
Alliance	BUY	3.94	4.75	37.0	37.6	10.6	10.5	17.0	18.5	3.7	4.4	3.6	3.7	1.1	1.1
BIMB	BUY	4.58	4.85	42.0	40.6	10.9	11.3	16.0	18.0	3.5	3.9	3.2	3.5	1.4	1.3
Average				**69.5**	**69.3**	**11.1**	**11.2**	**31.3**	**32.1**	**3.8**	**4.0**	**6.6**	**6.9**	**1.2**	**1.1**

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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.