26 January 2018 | Sector Update

BANKING

***Maintain* POSITIVE**

Short term booster from OPR hike

INVESTMENT HIGHLIGHTS

- **OPR hike of +25bps to 3.25% will have a positive short term boost to banks' margins.**
- **Banks with higher floating rate will benefit the most.**
- **However, margins will subsequently normalise due to deposit rate adjustment.**
- **Potential pressure on loans growth but may be moderate with pipeline appears to be healthy.**
- **We maintain our POSITIVE stance in the banking sector.**

OPR hike of +25bps was within expectations. Bank Negara Malaysia raised the overnight policy rate (OPR) at yesterday Monetary Policy Committee meeting by +25bps to 3.25%. This was in line with our economics team's expectation as industrial and trade activities across major as well as emerging economies remain on upward trajectory. Domestically, positive spill-over effects from external demand and upbeat local economic activities have contributed towards Malaysia's robust economic expansion. Looking ahead, our economics team forecasts GDP growth to remain strong this year, supported with gradual rise in global commodity prices, further market integration, stable labour market and contained inflationary pressure.

Short term boost to margins... We believe that the OPR hike will provide a short term boost to net interest margins (NIM) as there will be a near-immediate adjustment to loans and financing which has a floating rate. The floating rate loans, on average, contribute circa 76.8% of total loans book of banks under our coverage. We note that previous OPR hike had translated into a corresponding increase in Base Lending Rate (or in this case Base Rate) the following month.

...stemming from interest income perspective. We expect that this will not only ease any NIM compression pressure but also lift margins in the near term especially from an interest income perspective. This will strengthen the improvement in NIM that we had observed in 9MCY17 in the majority of the banks under our coverage from better cost funding management. However, we expect NIM to normalise within 2 to 3 quarters due to an increase to the deposits rates, particularly an adjustment to the fixed deposit rates which had been contracted before the OPR hike.

FIGURE 1: BANKS' PERCENTAGE OF FLOATING RATE LOANS & CASA RATIO AS AT END SEPT'17

Banks	Percentage of floating rate loans	CASA ratio
Maybank	70.8%	36.9%
Public	76.9%	30.4%
CIMB	83.5%	36.2%
Hong Leong Bank	76.5%	27.3%
RHB	82.5%	27.1%
AMMB	71.0%	20.8%

Banks	Percentage of floating rate loans	CASA ratio
BIMB	87.9%	33.3%
Alliance Bank	90.3%	37.3%
Affin	63.1%	17.0%
Average	*76.8%*	*32.2%*

Source: Company, MIDFR

Banks with higher floating rate loans will benefit the most. We opine that with a short term boost to NIM, earnings for banks will be positively affected. We estimate an average improvement of +1.5% to the net profit of banks under our coverage when compared against our previous forecast. We expect banks with higher floating rate loans to benefit the most. As such, we believe that Alliance Bank Malaysia Bhd will be a major beneficiary as its floating rate loans comprised of 90.3% of its loans book, the highest amongst its peers. We estimate a rise of circa +3.9% to its FY19 earnings from our previous forecast. Meanwhile, for the regional banks, Maybank and CIMB, the impact on earnings will be +0.8% respectively. This is due to the fact that their loan exposures are more diversified, with domestic loans comprising of 58.1% and 57.0% respectively of its total loans book.

FIGURE 2: ESTIMATED IMPACT OF OPR HIKE ON FY18/19 EARNINGS FORECAST OF BANKS

Banks	FY18/FY19 Net Profit forecast Pre-OPR hike (RM m)	FY18/FY19 Net Profit forecast Post-OPR hike (RM m)	Change
Maybank	7,575	7,639	+0.8%
Public	5,449	5,570	+2.2%
CIMB	4,942	4,984	+0.8%
Hong Leong Bank*	2,410	2,443	+1.4%
RHB	2,107	2,165	+2.8%
AMMB*	1,489	1,522	+2.2%
BIMB	658	670	+1.9%
Alliance Bank*	573	595	+3.9%
Affin	561	574	+2.4%

* denotes impact on FY19 earnings of banks as FYs of these banks end on Mar/June. For the rest, the impact will be on FY18 earnings

Source: MIDFR

Downside risk on loans growth. One of the possible downside risks from the OPR hike will be a slowdown in loans growth, either from lower loans demand or from higher borrowers' rejection rate. Based on our observation, loans applied and approved declined on sequential month basis by -1.5% and -0.9% respectively between June'14 and July'14, the last time there was an OPR hike. However, it subsequently bounced back to register +4.9%mom and +4.3%mom the following month. We expect to see similar trend to occur between Feb'18 and March'18.

But loans pipeline will continue to be robust. We believe that loans pipeline will continue to be robust in 1HCY18. Main driver will be solid demand for borrowing and lending of mortgage loans despite the higher OPR and subsequent Base Rate. Our property analyst expect that there will be a negative impact to property demand in the short term but will subsequently normalise in 2 to 3 month time.

This may translate to better loans growth in CY18. We believe that loans growth will be below expectations in CY17 despite the strong domestic economic performance. However, we understand that there may be a lag effect. With our economics team expecting continuing solid GDP performance this year and a healthy loans pipeline, we expect that loans growth will pick up in CY18. The loans applied and approval will provide a steady loans pipeline at least in 1QCY18. As such, we maintain our expectations of a loans growth of 6%yoy for CY18.

OPR to remain at 3.25% in CY18. Our economics team's baseline view is for one rate hike in CY18. The hike is seen as a step to normalise the degree of monetary accommodation rather than the beginning of tightening cycle. Hence, this would moderate any downward pressure on loans growth.

Maintain POSITIVE. With the expected boost to the earnings of banks under our coverage, we maintain our POSITIVE stance for the banking sector. We note that the share price performance of banking stocks this past week may indicate that investors have already factored in the OPR hike. Nevertheless, we believe that there is still upside given that we believe the main investment premised of the banking sector is not just based on the OPR hike but also on continuing loans growth. We believe that the continued domestic economic performance in CY18 and stable employment environment will drive loans growth.

Adjustment to earnings forecast and target price. We are also adjusting our FY18/FY19 earnings forecast for the banks under our coverage as per Figure 3 above to reflect the increased lending rate and deposits rate. Our rationale for not adjusting earlier was due to the uncertainty of the timing of the OPR hike. Since the hike came in Jan'18, banks with December financial year end could relatively account the impact in full. With the adjustment to earnings forecast, we are also adjusting our target price as per Figure 3 below. However, we are not adjusting our BUY calls which are Maybank, CIMB, Public Bank, Affin, Alliance and BIMB. For Maybank and CIMB, our BUY call is due to the expectations of continued earnings recovery coupled with solid asset growth and it regional exposure. As for Public Bank, we like its good asset quality and sustained profitability. Meanwhile for Affin and Alliance, our call is premised upon its turnaround program showing results, and for BIMB, we expect its operations to continue to be robust.

FIGURE 3: TARGET PRICE ADJUSTMENT FOR BANKING STOCKS UNDER COVERAGE

Banks	Target price (RM)	
	Previous	Post earnings adjustment
Maybank	10.30	10.30
Public	23.30	23.50
CIMB	7.17	7.17
Hong Leong Bank	15.70	15.72
RHB	5.20	5.22
AMMB	4.35	4.40
BIMB	5.00	5.03
Alliance Bank	4.65	4.69
Affin	2.90	2.91

FIGURE 4: PEER COMPARISON FOR MALAYSIAN BANKING STOCKS

	Rec.	Price @ 25/1 (RM)	TP (RM)	EPS (sen)		PER (x)		Net DPS (sen)		Net Div Yield (%)		BV (RM)		PBV (x)	
				17	18	17	18	17	18	17	18	17	18	17	18
Maybank	BUY	10.00	10.30	69.8	70.9	14.3	14.1	55.0	56.0	5.5	5.6	6.8	7.1	1.5	1.4
Public Bank	BUY	21.20	23.50	137.9	144.2	15.4	14.7	60.0	62.0	2.8	2.9	9.3	9.8	2.3	2.2
CIMB	BUY	7.02	7.17	47.0	53.2	14.9	13.2	26.0	30.0	3.7	4.3	5.2	5.5	1.3	1.3
RHB Bank	NEUTRAL	5.40	5.22	48.3	54.0	11.2	10.0	12.0	13.0	2.2	2.4	5.6	5.8	1.0	0.9
Hong Leong*	NEUTRAL	18.14	15.72**	117.6	119.5	15.4	15.2	47.0	47.0	2.6	2.6	11.2	11.3	1.6	1.6
AMMB*	NEUTRAL	4.80	4.40	46.8	49.5	10.3	9.7	17.0	18.0	3.5	3.8	5.5	5.8	0.9	0.8
Affin	BUY	2.53	2.91	26.0	29.5	9.7	8.6	12.0	13.0	4.7	5.1	4.7	4.8	0.5	0.5
Alliance*	BUY	4.26	4.69	35.2	38.9	12.1	11.0	19.0	20.0	3.7	4.4	3.5	3.7	1.2	1.2
BIMB	BUY	4.06	5.03	38.9	42.2	10.4	9.6	14.4	15.5	3.5	3.8	2.7	3.0	1.5	1.4
Average				**63.1**	**66.9**	**12.6**	**11.8**	**29.2**	**30.5**	**3.6**	**3.9**	**6.1**	**6.3**	**1.3**	**1.3**

* denotes investment statistics of FY18 and FY19 as FYs of these banks end on Mar/June.
** under review

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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.