

9 March 2017 | Sector Update

BANKING*Upgrade to POSITIVE****Turning around a corner*****INVESTMENT HIGHLIGHTS**

- **It appears that the banking sector has turned around the corner and we expect any surprises this year will be on the upside**
- **We expect recovery in earnings in most banks and our views are reinforced by the 4QCY16 results which suggest good momentum for CY17**
- **Valuations of banks are depressed at the moment. However, we believe are inching up to its long term averages**
- **We have recently upgraded Maybank to BUY (TP: RM9.40) and continue to like CIMB (BUY, TP: RM5.90) as we expect both these banks to continue its earnings recovery coupled with solid asset growth. Concerns over asset quality are mitigated. We are also favourable due to its regional exposure**
- **We also like Public Bank (BUY, TP: RM22.60) and Hong Leong Bank (BUY, TP: RM15.50) due to its good asset quality and sustained profitability. Our other BUY call is Affin (TP: RM3.30) as its turnaround program showing results**
- **We are sanguine on the prospect of the banks given that Malaysia's economy is expected to rebound this year. Hence, we are upgrading our sector call to POSITIVE**

There seem to be a build-up in optimism lately. We note that there is a lingering sense of optimism on the banking sector lately. Recent statistics and the concluded 4QCY16 results hint that there could be a build-up in momentum into the rest of CY17. We examine the drivers to see if there are any catalysts for the sector going forward.

Banking system loans growth appears to be on an uptrend. Loans growth for the banking system as at Jan'17 grew at a faster pace than the previous six month period at +5.6%yoy to RM1,527b. This suggest that loans growth is continuing to inch higher, a trend which began in Oct'16 (refer to Figure 1).

Businesses are borrowing more. Interestingly, we note that working capital loans uptrend was more pronounced. It grew +6.3%yoy as at Jan'17 from a low of +1.5%yoy as at Aug'16. We take working capital loans as a proxy for overall business borrowing. The acceleration in growth suggests that businesses are more confident of the immediate term prospect. Indeed, RAM Business Confidence Index by RAM Holdings Berhad and RAM Credit Information Sdn Bhd showed that corporates and SMEs are optimistic about the business outlook in 1HCY17 at 56.9 points and 53.2 points respectively.

Loans growth to rebound in CY17. Our economics team are expecting Malaysia's GDP to pick up in CY17. The expected better economic performance will have a positive impact to the banking sector. Hence, we expect loans growth to rebound in CY17. We believe that we have already started to see the green shoots with working capital loans trending higher.

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FIGURE 1: BANKING SYSTEM TOTAL LOANS AND LOANS GROWTH

	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-16	1,447.3	7.7%	2.6%	11.8%	6.1%	10.5%
Feb-16	1,449.9	7.4%	1.8%	11.4%	6.1%	9.8%
Mar-16	1,449.5	6.4%	1.1%	11.0%	7.1%	8.3%
Apr-16	1,447.8	6.3%	1.0%	10.8%	6.6%	8.2%
May-16	1,458.5	6.2%	0.7%	10.6%	5.9%	7.5%
Jun-16	1,465.2	5.6%	0.4%	10.3%	5.7%	5.7%
Jul-16	1,467.3	5.1%	-0.2%	10.1%	5.3%	4.9%
Aug-16	1,472.1	4.2%	-0.3%	10.1%	4.5%	1.5%
Sep-16	1,483.8	4.2%	-0.4%	9.9%	4.6%	2.1%
Oct-16	1,493.4	4.5%	-0.6%	9.5%	4.7%	2.3%
Nov-16	1,507.6	5.3%	-0.8%	9.5%	4.3%	4.4%
Dec-16	1,521.5	5.3%	-1.0%	9.2%	4.6%	5.6%
Jan-17	1,527.9	5.6%	-0.9%	9.1%	4.4%	6.3%

Source: BNM, MIDFR

A similar trend for deposits. Meanwhile, the deposits growth posted as at Jan'17 also suggest a continuation of an upward trend. Deposits grew +3.1%yoy vs. +2.0%yoy as at Dec'16 (Figure 2). Moreover, CASA grew +5.8%yoy with CASA ratio improving +23bps yoy to 26.9%.

FIGURE 2: BANKING SYSTEM TOTAL DEPOSITS and DEPOSITS GROWTH

	Total deposits (RM b)	Growth (yoy)	CASA (RM b)	Growth (yoy)	CASA Ratio
Jan-16	1,636.2	0.1%	429.6	2.1%	26.3%
Feb-16	1,652.7	0.7%	436.7	2.5%	26.4%
Mar-16	1,652.5	-1.0%	423.7	-2.7%	25.6%
Apr-16	1,643.5	-1.2%	417.6	-2.3%	25.4%
May-16	1,655.3	-0.4%	424.2	0.4%	25.6%
Jun-16	1,655.3	-0.8%	433.1	-0.4%	26.2%
Jul-16	1,638.0	1.0%	423.1	1.2%	25.8%
Aug-16	1,640.3	1.0%	425.6	0.6%	25.9%
Sep-16	1,660.5	1.3%	429.1	-0.3%	25.8%
Oct-16	1,670.0	2.6%	432.7	2.8%	25.9%
Nov-16	1,668.1	2.2%	438.9	4.5%	26.3%
Dec-16	1,679.8	2.0%	448.9	5.0%	26.7%
Jan-17	1,687.2	3.1%	454.7	5.8%	26.9%

Source: BNM, MIDFR

Subdued rates competition. It appears that the competition for loans and deposits have not affected pricing. Average lending rate in Jan'17 was +5bps higher from Dec'16, while savings deposit rate fell -1bps. Fixed deposits were generally stable except 12 month deposits which increased by only +2bps mom. We view this as positive as it will ease the pressure on margin compression. If this environment persists, we expect only a slight compression in NIM but overall will be stable in CY17.

Liquidity is still ample, while asset quality stable. It is understandable that we have yet to see faster acceleration of loans growth. We understand that banks have been very cautious in its lending activities to protect asset quality. Indeed, the GIL ratio for the banking system has been steady at around the 1.61% level (Figure 3), while for banks under our coverage it had been stabilising at 1.7%. In addition, LD ratio of 90.6% as at Jan'17 also suggests a need for this cautiousness. However, the deposits growth and especially CASA growth implies that liquidity is ample. In fact, another measure of liquidity which is the Liquidity Coverage Ratio (LCR) shows that banks have sufficient liquidity. The latest LCR (as at Dec'16) was 125%, up +9ppt from Nov'16. Therefore, we opine that banks could well accelerate lending activities should it needs to.

FIGURE 3: BANKING SYSTEM IMPAIRED LOANS RATIO

	Gross Impaired Loans Ratio (%)	Net Impaired Loans Ratio (%)
Jan-16	1.61	1.21
Feb-16	1.64	1.25
Mar-16	1.60	1.21
Apr-16	1.60	1.21
May-16	1.65	1.25
Jun-16	1.66	1.26
Jul-16	1.68	1.29
Aug-16	1.66	1.27
Sep-16	1.65	1.26
Oct-16	1.65	1.25
Nov-16	1.63	1.23
Dec-16	1.61	1.24
Jan-17	1.61	1.22

Source: BNM, MIDFR

Banking earnings momentum in 4QCY16. Based on our observation, there appear to be upward momentum in the earnings of banks under our coverage in 4QCY16. Total normalised earnings in the quarter was +13.3%yoy and +6.7%qoq higher (Figure 4). We noted that this was mostly due to the stellar results from Affin, Maybank and Hong Leong. In general, the strong performance was due to improvement in NIM, controlled OPEX and better than expected loans growth, which moderated increased credit charge-off rate. The +2.7%yoy normalised earnings growth in CY16 was largely contributed by 2HCY16 performance, particularly in 4QCY16.

Expecting better earnings in CY17. We believe that the banking earnings momentum will spill over into CY17. This will be driven by expected better loans growth, stable NIM and lower provisioning given the normalisation of the proactive measures that banks have taken previously.

FIGURE 4: CORE NET PROFIT OF BANKS (RM'm)

	Dec-16 (4QCY16)	Sept-16 (3QCY16)	Dec-15 (4QCY15)	Chg yoy	Chg qoq	12MCY16	12MCY15	Chg yoy
Affin	171.4	139.6	97.4	76.0%	22.7%	564.0	369.3	52.7%
Maybank	2,360.6	1,795.7	1,652.1	42.9%	31.5%	6,743.0	6,835.9	-1.4%
H. Leong	549.9	542.6	475.0	15.8%	1.3%	2,148.9	1,809.1	18.8%
AMMB	313.2	352.6	300.2	4.3%	-11.2%	1,268.8	1,541.4	-17.7%
CIMB	854.4	1,023.2	850.0	0.5%	-16.5%	3,564.2	3,411.0	4.5%
Public	1,482.8	1,238.2	1,492.4	-0.6%	19.8%	5,206.9	5,062.2	2.9%
Alliance	129.7	132.6	135.6	-4.4%	-2.2%	524.6	485.5	8.1%
BIMB	139.5	140.6	161.9	-13.8%	-0.8%	559.0	547.3	2.1%
RHB	261.2	506.0	363.4	-28.1%	-48.4%	1,875.0	1,798.0	4.3%
Total	6,262.7	5,871.1	5,527.9	13.3%	6.7%	22,454.4	21,859.6	2.7%

Source: Various, MIDFR

FIGURE 5: NET INTEREST MARGINS

	Dec-15 (4QCY15)	Mar-16 (1QCY16)	June-16 (2QCY16)	Sept-16 (3QCY16)	Dec-16 (4QCY16)
Affin	2.05%	1.85%	1.99%	2.04%	2.10%
Alliance	2.15%	2.15%	2.16%	2.22%	2.31%
AMMB	1.93%	1.92%	1.94%	1.92%	2.02%
BIMB	2.78%	2.70%	2.77%	2.77%	2.74%
CIMB	2.66%	2.62%	2.63%	2.58%	2.69%
H. Leong	1.96%	1.91%	1.95%	2.01%	2.08%
Maybank	2.29%	2.34%	2.23%	2.22%	2.32%
Public	2.19%	2.20%	2.17%	2.17%	2.22%
RHB	2.15%	2.22%	2.19%	2.15%	2.18%
Average	2.24%	2.21%	2.23%	2.23%	2.30%

Source: Various, MIDFR

FIGURE 6: COST TO INCOME RATIO

	Dec-15 (4QCY15)	Mar-16 (1QCY16)	June-16 (2QCY16)	Sept-16 (3QCY16)	Dec-16 (4QCY16)
Affin	60.3%	63.9%	60.3%	57.2%	55.8%
Alliance	48.4%	54.1%	48.6%	46.5%	46.0%
AMMB	63.5%	68.6%	56.3%	55.0%	60.7%
BIMB	62.2%	58.5%	57.3%	56.6%	59.4%
CIMB	54.7%	57.4%	53.6%	53.2%	51.7%
H. Leong	61.3%	47.1%	45.8%	44.8%	42.5%
Maybank	49.3%	48.4%	48.9%	49.3%	43.3%
Public	30.0%	31.5%	33.1%	33.0%	31.5%
RHB	53.7%	48.2%	50.9%	50.7%	54.3%
Average	53.7%	53.1%	50.5%	49.6%	49.5%

Source: Various, MIDFR

FIGURE 7: GROSS IMPAIRED LOANS RATIO

	Dec-15 (4QCY15)	Mar-16 (1QCY16)	June-16 (2QCY16)	Sept-16 (3QCY16)	Dec-16 (4QCY16)
Affin	1.90%	1.98%	1.98%	2.08%	1.67%
Alliance	1.10%	1.00%	1.00%	0.90%	1.00%
AMMB	1.81%	1.94%	1.69%	1.64%	1.54%
BIMB	1.09%	0.94%	1.05%	1.09%	0.98%
CIMB	3.00%	3.00%	3.20%	3.20%	3.30%
H. Leong	0.86%	0.84%	0.79%	0.84%	0.86%
Maybank	1.86%	2.11%	2.34%	2.22%	2.28%
Public	0.50%	0.50%	0.50%	0.50%	0.50%
RHB	1.88%	1.82%	2.06%	2.25%	2.43%
Average	1.56%	1.57%	1.62%	1.64%	1.62%

Source: Various, MIDFR

FIGURE 8: NET CREDIT CHARGE OFF

	Dec-15 (4QCY15)	Mar-16 (1QCY16)	June-16 (2QCY16)	Sept-16 (3QCY16)	Dec-16 (4QCY16)
Affin	0.28%	0.12%	0.15%	0.34%	0.32%
Alliance	0.07%	0.06%	0.19%	0.17%	0.33%
AMMB	-0.37%	-0.26%	-0.29%	-0.19%	-0.32%
BIMB	0.32%	0.39%	0.33%	0.23%	0.04%
CIMB	0.78%	0.64%	0.79%	0.79%	0.93%
H. Leong	0.20%	0.06%	-0.18%	0.09%	0.09%
Maybank	0.45%	0.75%	0.85%	0.32%	0.54%
Public	-0.15%	0.10%	0.10%	0.13%	-0.05%
RHB	0.63%	0.21%	0.16%	0.38%	0.80%
Average	0.25%	0.23%	0.23%	0.25%	0.30%

Source: Various, MIDFR

Valuation still attractive at this juncture. While banking system statistics and earnings of banks under our coverage showed a rebound, we note that valuation for the banking stocks under our coverage are still depressed. All of the banks are below its 5-year historical average PBV, while a majority are trading below 1 standard deviation. This was probably due to the sluggish macroeconomic performance in the past two years and the concerns regarding asset quality especially from the commodities sector. However, as GDP is expected to rebound in CY17, we expect that valuation of banks will start to normalise.

FIGURE 9: HISTORICAL AND CURRENT PRICE TO BOOK

	PBV (x)		
	5-YEAR AVERAGE	1 STD. DEV. BELOW	CURRENT
Affin	0.7	0.6	0.6
Alliance	1.5	1.3	1.2
AMMB	1.4	1.0	0.9
BIMB	1.8	1.6	1.7
CIMB	1.5	1.1	1.0
H. Leong	1.7	1.4	1.2
Maybank	1.7	1.4	1.3
Public	2.8	2.4	2.1
RHB	1.1	0.9	0.9

Source: Various, MIDFR

All pointing towards better performance, upgrade to POSITIVE. We believe that the increasing optimism in the banking sector is not without merit. Major metrics for banks are showing promising signs of improvement. In our opinion, the banking sector has turned around a corner and we expect better performance in CY17, driven by higher loans growth and stable margins. This is in-line with our economics team's expectation of improved GDP, with private consumption and investment on an upward trajectory. Furthermore, valuation remains attractive at current juncture. Therefore, we are upgrading our view of the banking sector to **POSITIVE** (from NEUTRAL).


Reiterate BUY calls for CIMB, Maybank, Public Bank, Hong Leong and Affin. We continue to like CIMB (BUY, TP: RM5.90) and have recently upgraded Maybank to BUY (TP: RM9.40), as we expect both these banks to continue its earnings recovery coupled with solid asset growth. Concerns over asset quality are mitigated. We are also favourable due to its regional exposure. We also like Public Bank (BUY, TP: RM22.60) and Hong Leong Bank (BUY, TP: RM15.50) due to its good asset quality and sustained profitability. Our other BUY call is Affin as its turnaround program showing results. We are also revising our TP of Affin to RM3.30 (from RM2.85) as we peg its FY17 BVPS to 0.7x (previously 0.6x), which is its 5-year historical average. We believe that this fair given that Affin have been showing remarkable improvements resulting from its transformation program. 

FIGURE 10: PEER COMPARISON FOR MALAYSIAN BANKING STOCKS

	Rec.	Price @ 9 Mar (RM)	TP (RM)	EPS (sen)		PER (x)		Net DPS (sen)		Net Div Yield (%)		BV (RM)		PBV (x)	
				16	17	16	17	16	17	16	17	16	17	16	17
Maybank	BUY	8.83	9.40	67.8	69.9	13.0	12.6	52.0	55.0	5.9	6.2	6.7	6.8	1.3	1.3
Public Bank	BUY	19.20	22.60	134.8	137.9	14.2	13.9	58.0	60.0	3.0	3.1	8.9	9.3	2.2	2.1
CIMB	BUY	5.37	5.90	41.0	45.5	13.1	11.8	20.0	18.0	3.7	3.4	5.0	5.3	1.1	1.0
RHB Bank	NEUTRAL	5.19	5.15	43.6	48.4	11.9	10.7	12.0	13.0	2.3	2.5	5.4	5.6	1.0	0.9
Hong Leong	BUY	13.40	15.50	99.1	112.2	13.5	11.9	41.0	41.0	3.1	3.1	10.3	10.9	1.3	1.2
AMMB	NEUTRAL	4.99	4.55	45.1	45.0	11.1	11.1	15.5	16.0	3.1	3.2	5.0	5.3	1.0	0.9
Affin	BUY	2.88	3.30	29.0	30.0	9.9	9.6	3.0	12.0	1.0	4.2	4.5	4.7	0.6	0.6
AFG	NEUTRAL	4.08	4.05	34.2	36.0	11.9	11.3	14.5	18.0	3.6	4.4	3.1	3.3	1.3	1.2
BIMB	NEUTRAL	4.42	4.35	35.3	38.9	12.5	11.4	13.0	14.4	2.9	3.3	2.4	2.6	1.8	1.7
Average				35.3	38.9	12.5	11.4	13.0	14.4	2.9	3.3	2.4	2.6	1.8	1.7

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	Total return is expected to be <-15% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >15% 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.