# BANKING

**Maintain POSITIVE**

## 2H21 Financial Stability Review

### KEY INVESTMENT HIGHLIGHTS

- **Financial ratios for businesses have shown steady improvement**
- **Business loans currently make up 24.6% of R&R loans. This was driven largely by SME applications in 2H21**
- **Similarly, household loan take-up rates for repayment assistance rose with PEMULIH and URUS introductions**
- **Banking sector maintains its high liquidity with superb LCR and NSFR ratios**
- **We maintain our POSITIVE stance. In spite of headwinds, the banking sector can look forward to pre-emptive provisioning writebacks in 2023**

**BNM released its 2H21 Financial Stability Review (FSR) yesterday.** Here are some highlights from the review.

**Asset Quality – Businesses**

Following the loosening of containment measures in 2H21, firms have shown marked signs of recovery. Most notably, firms in the construction, manufacturing, restaurants and recreational activities sectors, as well as firms that successfully pivoted towards greater digitalisation of operations.

**Financial ratios for businesses.** Encouragingly, financial ratios (pertaining to debt-servicing capabilities) showed steady improvement in 4Q21 (vs. 2Q21), as demonstrated in the following (Exhibit 1&2):

- Operational margin of 7.6x [2Q21: 7.2x]
- Debt-to-equity ratio of 21.8x [2Q21: 22.2x]
- Interest coverage ratio of 7.5x [2Q21: 6.7x]
- Cash to short-term debt ratio of 1.4x [2Q21: 1.4x]

Other points to note:

- **Larger firms** generally remained financially resilient, with larger financial buffers, diversified revenue streams and higher capacity to roll out cost-efficiency measures.
- **SMEs** make up the highest number of firms benefitting from repayment assistance (RA) – they make up 95% of business loan accounts approved for R&R.
- **As of Dec-21, overall business loans make up 24.6% of R&R loans.** [Jun-21: 18.9%]. This was largely driven by the sharp increase of SME loans under R&R programmes to 36.5% [Jun-21: 21.6%], mostly due to increased volume of R&R applications during 2H21 by SMEs in vulnerable sectors (Exhibit 3). In contrast Non-SME contributions to R&R loans remained stable at 17.7% [Jun-21: 17.2%].

**COMPANY IN FOCUS**

**Maybank**
Maintain **BUY** | Unchanged Target price: RM9.47
Price @ 30th March 2022: RM8.88
- High dividend yields
- Industry leader
- Sizeable foreign operations

**Share price chart**

**Public Bank**
Maintain **BUY** | Unchanged Target price: RM5.10
Price @ 30th March 2022: RM4.65
- Superior asset quality
- Resilience towards higher bond yields
- Large headroom for provision writebacks

**Share price chart**

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- **Potential commercial real estate (CRE) sector issues.** BNM notes possible issues with recent structural trends reducing CRE demand (via vacancy and rental rates) and subsequently posing risks to the balance sheets of financial institutions. A sharp and protracted slowdown in CRE activity could have an indirect impact on other industries.

  However, BNM sees limited impact from the above. Linkages between CRE sector and the financial system are significantly lower in Malaysia relative to other countries – credit exposures to CRE sector comprise only of 7.8% of local total banking system assets, in part due to the banks' cautiousness towards the sector.

## Asset Quality – Household

**HH debt-to GDP ratio declines.** Dec-21: 89.0% [Jun-21: 89.6%], though still on the higher end compared to regional economies (Exhibit 4). Household (HH) debt was driven primarily by housing mortgages, largely due to incentives under the Home Ownership Campaign.

Take-up rate of RA in Dec-21 rose sharply, given the introduction of the PEMULIH and URUS programme. It rose to 30% of HH loan accounts & 35.7% of outstanding loan exposures. [Jun-21: 12.8% & 16.0% respectively].

**Some notes on residential mortgages:**

- Residential mortgage to total HH debt ratio rises: 58% [Dec-19: 55%]. (Exhibit 5)
- Growth in housing loans taken by owner-occupiers (+7.4%yoy) continues to outpace that by HH investors (+5.7%yoy). (HH investors refer to individual borrower with more than one housing loan).
- Median debt service ratios (DSRs) of newly-approved and outstanding HH loans maintained at 44% and 35% respectively [Jun-21: 44% and 35%].
- Median loan-to-value (LTV) ratio of outstanding housing loans fell to 65.2% in Dec-21 [Mar-20: 66.5%] – At this comfortable rate, it provides ample buffers for borrowers against a steep correction in house prices.

## Banking sector stability

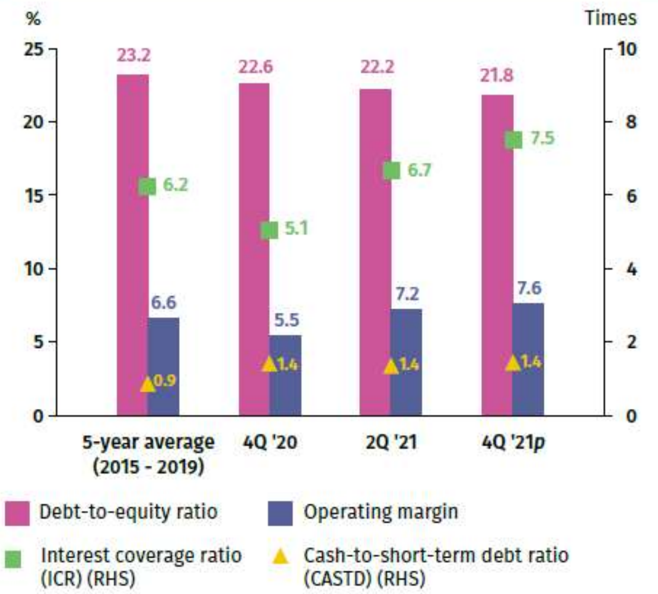
The banking sector has stayed resilient, thanks to ample capital and liquidity buffers:

- Robust aggregate LCR of 162% [Jun-21: 150%]. (Exhibit 6). This reflects excess deposits being channeled into high-quality liquid assets (gov bonds, BNM placements).
- Solid aggregate NSFR of 116.4% -- all banks met minimum NSFR requirement of 100.0% in Sep-21.

**Maintain POSITIVE.** All in all, recovery seems to have progressed at a decent rate. Banks are expected to weather through a deterioration in asset quality in the coming quarters with adequate loan loss coverage and capital ratios. Despite headwinds, we still favour the banking sector for mainly for reduced credit costs in 2022, improved structural performance and potential pre-emptive provisioning writebacks in 2023. Our top picks include **Public Bank (BUY, TP: RM5.10)** and **Maybank (BUY, TP: RM9.47)**.

## EXHIBIT 1

Chart 1.4: Business Sector – Key Financial Performance Indicators



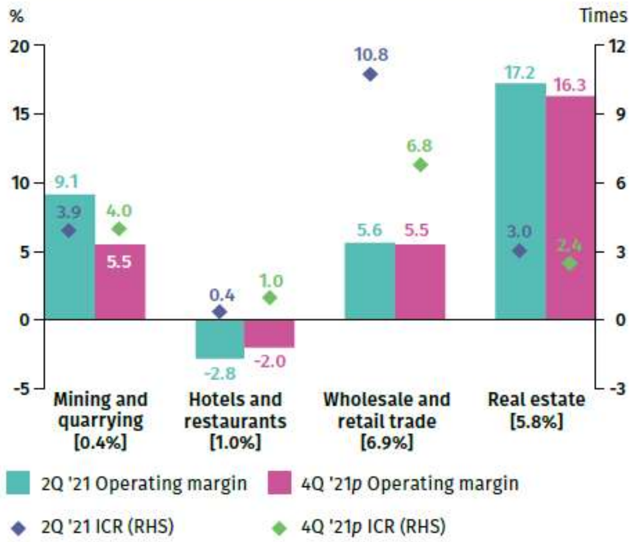

*p* Preliminary

Note: Prudent thresholds for ICR and CASTD are two times and one time, respectively.

*Source: BNM, S&P Capital IQ, MIDFR*

## EXHIBIT 2

Chart 1.5: Business Sector – Operating Margin and Debt-servicing Capacity Indicators for Selected Sectors



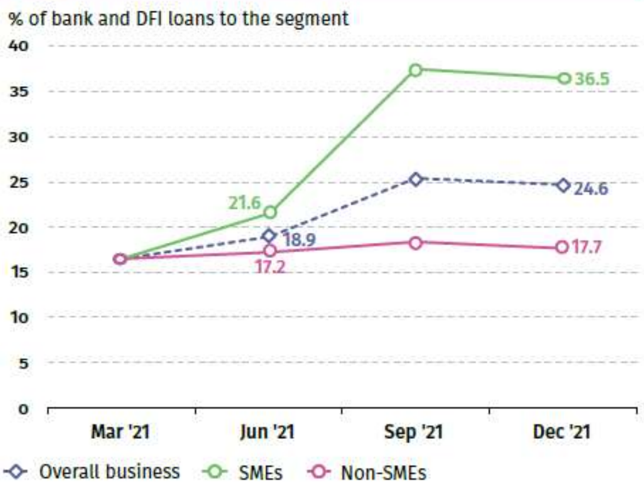

*p* Preliminary

Note: 1. Prudent threshold for ICR is two times.
2. [...%] refers to loans to the sector as a share of total banking system loans.

*Source: BNM, S&P Capital IQ, MIDFR*

## EXHIBIT 3

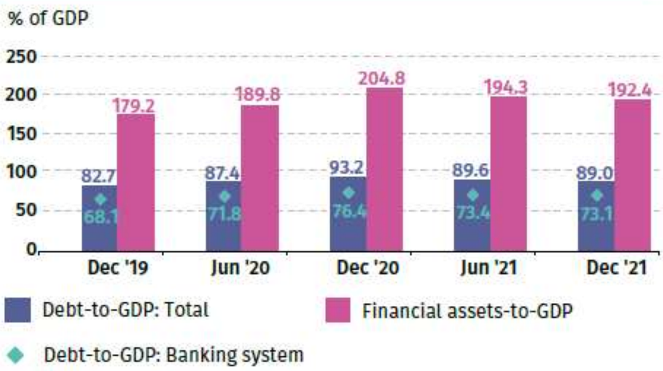
Chart 1.6: Business Sector – Share of R&R Loans by Segment




*Source: BNM, MIDFR*

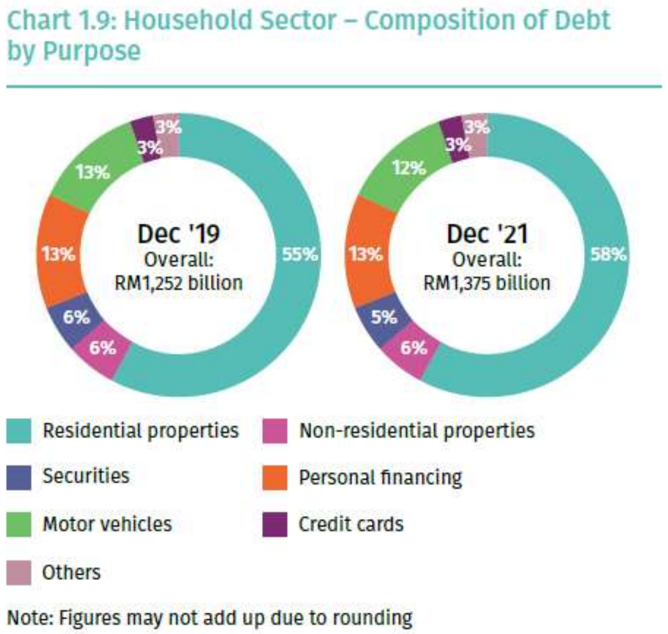
## EXHIBIT 4

Chart 1.11: Household Sector – Key Ratios



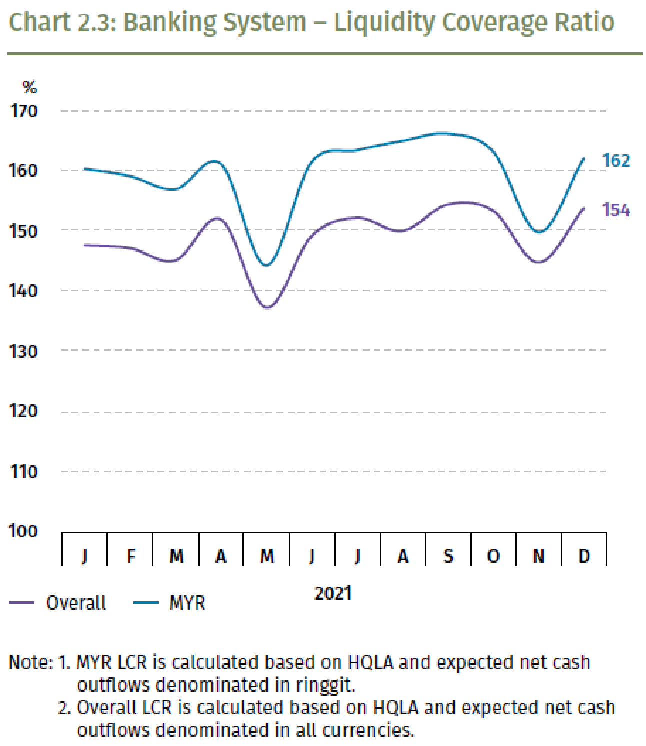

*Source: BNM, Bursa, DoSM, EPF, SC, MIDFR*

## EXHIBIT 5




*Source: BNM, MIDFR*

## EXHIBIT 6




*Source: BNM, MIDFR*

## 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. |
| **ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell** | |
| ☆☆☆☆ | Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell |
| ☆☆☆ | Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell |
| ☆☆ | Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell |
| ☆ | Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell |

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology