Public Bank Berhad

(1295 | PBK MK) Financial Services | Finance

Maintain BUY

Trust in their Unit Trust business

***Unchanged* Target Price: RM5.67**

KEY INVESTMENT HIGHLIGHTS

- **Earnings were within our expectations**
- **Maintaining our FY21/FY22/FY23 earnings forecast for now**
- **Core drivers include excellent asset quality and buffers, possible jump in retail SME loan growth, unit trust business capturing market share at rapid rate, foray into ESG initiatives**
- **Key risks include higher OPEX, slower-than-expected loan growth, higher competition quashing unit trust growth**
- **Maintain BUY call with unchanged TP of RM5.67**

Highlights from Public Bank's 2QFY22 quarterly results:

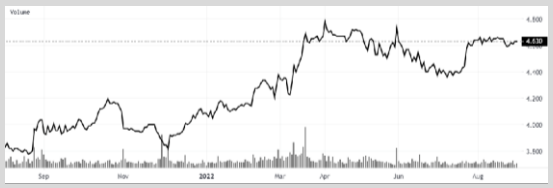
1. PBB's YTD earnings slipped by -3.4%yoy as result of Cukai Makmur and weaker NOII income.
2. RA loans reported an uptick from Apr-22's numbers due to a surge in reapplications.
3. GIL flattish at 0.29%, with improvements in residential mortgages and transport vehicle segments.
4. Total FY22 provisions expected to be at lower end of 10-15bps guidance.
5. 1HFY22's NOII was down -19%, though unit trust business continues to capture retail market share at rapid rate.
6. Slow loan growth: Domestic SME loans reported contraction on a sequential year basis.
7. Deposit growth was similarly muted, growing +3.2%yoy.
8. 1HFY22's OPEX ticks upwards by +3%qoq because of higher admin and marketing costs.
9. Dividend announced: 9.0 sen, implying a payout of 55%.
10. Sustainability targets unveiled for FY22, though still in the rudimentary planning phase.

FINANCIAL SUMMARY

FYE Dec	FY20	FY21	FY22F	FY23F	FY24F
NII (RM m)	8,304	9,793	10,496	10,995	11,463
NOII (RM m)	3,008	2,751	2,955	3,053	3,163
Total income (RM m)	11,312	12,544	12,959	13,509	14,185
PPOP (RM m)	7,403	8,579	8,812	9,186	9,646
Core net profit (RM m)	4,872	5,657	5,869	6,779	7,120
Core EPS (sen)	25.1	29.1	30.2	34.9	36.7
Core P/E (x)	18.4	15.9	15.3	13.3	12.6
Gross DPS (sen)	13.0	15.2	15.1	17.5	18.3
Dividend yield (%)	2.8	3.3	3.3	3.8	4.0
BVPS (RM)	2.4	2.5	2.6	2.8	2.9
P/BV (x)	1.9	1.9	1.8	1.6	1.6
ROE (%)	10.7	11.9	11.9	12.9	12.9

RETURN STATISTICS	
Price @ 29 August 2022 (RM)	4.63
Expected share price return (%)	+22.5
Expected dividend yield (%)	+3.3
Expected total return (%)	**+25.8**

SHARE PRICE CHART



Share price performance (%)	Absolute	Relative
1 month	-0.2	-0.8
3 months	5.9	3.3
12 months	10.8	17.4

KEY STATISTICS	
FBM KLCI	1,501.57
Syariah compliant	No
F4GBM Index	Yes
ESG Grading Band (Star rating)	☆☆☆☆
Issue shares (m)	19410.69
Estimated free float (%)	54.80
Market Capitalisation (RM m)	89,871.50
52-wk price range	RM3.88 - RM4.79
Beta vs FBM KLCI (x)	1.19
Monthly velocity (%)	
Monthly volatility (%)	8.18
3-mth average daily volume (m)	13.31
3-mth average daily value (RM m)	60.45
Top Shareholders (%)	
Consolidated Teh Holdings Sdn Bhd	21.64
Employees Provident Fund Board	15.07
Kumpulan Wang Persaraan Diperbadan	4.10

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Within our and consensus expectations. Public Bank's 1HFY22 core net profit of RM2.82b made up 48% of both our and consensus full-year forecasts respectively. However, earnings slipped by -3.4%yoy, though this was due to elevated tax expenses as result of Cukai Makmur, as well as weaker NOII. Otherwise, PBB reported a far stronger PBT on the back of higher NII and lower loan provisions. Meanwhile, 2QFY22's earnings of RM1.42b rose by +2.4%yoy on the back of lower loan provisioning and stronger NII, offsetting higher OPEX and tax expenses, as well as lower NOII. On a sequential quarter basis, it rose +1.3%qoq mostly due to improved NII.

Repayment assistance (RA) loans. As of July-21, Public Bank saw an uptick in RA loans. Making up 6% of its gross loan portfolio, outstanding RA loans in Jul-22 rose to RM20.8b from Apr-22's RM20.1b. Overall, ~9% of the total RM84.1b of cumulative RA loans made from the beginning of the pandemic applied for further RA programmes. Sizeable re-applications (mostly for PBB's internal R&R programme) outnumbered the newly expired RA loans run-down. A greater proportion of retail businesses reapplied, as compared to consumer loans. Asset quality is still intact, with only 0.6% of active RA loans are classified as impaired. 5% of active RA loans are overdue by >1 month. Reapplying customers are classified under stage 2 loans unless they exhibit more signs of credit weakness.

Asset quality. The Group's GIL ratio remained flattish at 0.29% [1QFY22: 0.29%, 2QFY21: 0.35%]. On a sequential year basis, residential mortgages and transport vehicle loans saw significant improvements in terms of asset quality, whereas commercial properties' GIL ratio remained stable at a low 0.29%. The Group's LLC has risen to 389%, which is the highest within the industry. It benefits from the Group's low GIL base.

Provisioning. PBB reported an NCC of 9bps for the quarter, bringing up 1HFY22's total to 10bps. In 1HFY21, NCC was at the 35bps level. Management maintains their 10-15bps NCC forecast for FY22, though they expect the actual value to be skewed towards the lower end. PBB's cumulative overlays remain at RM1.7b, same as the last quarter.

NIM and NII. 2QFY22's NIM widened to 2.29% [+5bps qoq, +3bps yoy] and averaged 2.26% in 1HFY22, down from 2.27% in 1HFY21. Management increases its NIM guidance, believing that OPR hikes will enable FY22's NIM to be +8-10bps higher than FY21's 2.22%. Further improvements to NIM will be seen in the coming quarters as the benefits of more recent OPR hikes start to kick in. Similarly, NII was up +5.4%qoq and +5.3%yoy. Management did clarify that declines in LCR has no major impact on NIM levels. LCR has dropped to 111% from ~130% in FY21 as result of the withdrawal of some wholesale deposits, the effects of which are temporary. Indeed, LCR has since normalised to 120-130% levels, and this is not expected to impact NIM in any material way.

NOII. 1HFY22 NOII was down -19% as core fee income, forex and investment gains remain lacklustre. Management expects the challenging outlook to persist for the remainder of the year. Unit trust income of RM268m fell -6%qoq, -10%yoy. However, management points out that the loss of income comes from the drop in market value and lower sales volume. Fund size and market share remains constant, with unit holders continuing their regular payments. Note that ~80% of unit trust income stems from management fees, with the remainder from sales. Despite poor performance, the Group's unit trust business continues to capture retail market share at a fast rate, possessing 35.2% as of 1HFY22 [1HFY21: 33.3%].

Loan growth. Gross loans grew at a rate of +4.5%yoy, below the industry average of +5.6%yoy. The Group is maintaining its target for +5.0%yoy loan growth for FY22. PBB continues to take up market share for residential mortgages and hire purchase segment, each growing by +8.4%yoy and +5.6% of loan growth respectively. On the other hand, PBB's domestic SME portfolio is still languishing, falling -2.1%yoy as the Group exercised exceptional caution during the pandemic. Nonetheless, with an improving economic outlook, PBB has reported that new SME loan approvals have seen double digit growth compared to the same period of last year.

Deposit growth. Group deposit growth grew at a muted pace of +3.2%yoy. Domestic deposits grew by +3.5%yoy. CASA growth picked up pace to of +10.8%yoy, while the Group's Loan/Deposit ratio currently stands at 93.7%.

Cost efficiency. Operating expenses (OPEX) rose by +2.8%qoq in 2QFY22, on the back of higher admin and marketing costs. On a sequential year basis, 1HFY22's OPEX rose by +4.4%yoy despite lower marketing spend as result of higher personnel, establishment, and admin costs.

PBB reported a weaker cost/income ratio (CIR) of 33.5% in 1HFY22 [1HFY21: 31.6%], as result of higher OPEX and weaker NOII costs dragging the income base.

Capital ratios. The Group's CET-1 ratio remains stable, resting at a comfortable 14.1%.

Sustainability targets. PBB unveiled some of its sustainability targets and initiatives for 1HFY22, listed in Exhibit 3 and 4. PBB seems to be slightly behind the curve in terms of ESG practices, being well in the rudimentary planning phase. We do highlight PBB's commitment to finance energy efficient vehicles: In its goal to mobilise RM40b in ESG-friendly financing by 2025, RM25b of these will be for energy efficient vehicles.

Dividend announced. PBB announced a gross DPS of 9.0sen, which translates to a dividend payout of 55%. This translates to a dividend yield of 3.3% in FY22.

Earnings maintained. As results were within expectations, we make no changes to our earnings forecast.

Key risks. Key risks to earnings include (1) An inability to maintain lower costs, considering higher revenue spend and fixed costs as the economy reopens, (2) Lower-than-expected loan growth, especially in the retail SME segment, (3) Contraction in unit trust fund size and loss in retail market share, given higher competition.

Valuation and recommendation. We are optimistic on Public Bank's long-term prospects for several reasons: (1) Excellent asset quality and buffers reduce the possibility of unwelcome credit cost surprises, (2) Retail SME loan growth could see a huge jump in 2HFY22, (3) PBB's unit trust continues to steadily capture retail market share, set to benefit as markets revert to a more accommodative state, (4) Foray into sustainability practices could see PBB becomes more attractive as a viable ESG alternative within the industry. Thus, we maintain our **BUY** call with an unchanged **TP of RM5.67**, as we peg its FY23 BVPS to a unchanged P/BV of 2.0x. (GGM assumptions: FY23 ROE of 12.9%, LTG of 3.5% and COE of 8.1%.)

EXHIBIT 1: QUARTERLY RESULTS

FYE Dec (RM m)	2QFY22	1QFY22	2QFY21	Yoy (%)	Qoq (%)	1HFY22	1HFY21	Yoy (%)
Net interest income	2,218	2,104	2,107	5.3%	5.4%	4,322	4,180	3.4%
Islamic banking income	415	401	405	2.4%	3.5%	816	838	-2.7%
Non-interest income	545	642	682	-20.1%	-15.1%	1,187	1,403	-15.4%
Net income	**3,177**	**3,147**	**3,194**	**-0.5%**	**1.0%**	**6,325**	**6,421**	**-1.5%**
OPEX	(1,073)	(1,043)	(1,001)	7.2%	2.8%	(2,116)	(2,028)	4.3%
PPOP	**2,105**	**2,104**	**2,193**	**-4.0%**	**0.0%**	**4,209**	**4,393**	**-4.2%**
Loan provisions	(80)	(100)	(396)	-79.8%	-19.9%	(180)	(594)	-69.8%
Other provisions	(3)	(2)	1	n.m.	n.m.	(5)	(0)	n.m.
JV & Associates	0	(2)	(3)	n.m.	n.m.	(1)	(4)	n.m.
Profit before tax	**2,023**	**2,000**	**1,795**	**12.7%**	**1.1%**	**4,023**	**3,794**	**6.0%**
Tax	(591)	(587)	(394)	50.1%	0.6%	(1,179)	(844)	39.7%
NCI	(15)	(14)	(17)	-15.0%	2.3%	(29)	(36)	-20.8%
Reported net profit	**1,417**	**1,399**	**1,384**	**2.4%**	**1.3%**	**2,816**	**2,914**	**-3.4%**
Core net profit	**1,417**	**1,399**	**1,384**	**2.4%**	**1.3%**	**2,816**	**2,914**	**-3.4%**
Total NII	**2,615**	**2,490**	**2,473**	**5.7%**	**5.0%**	**5,105**	**4,916**	**3.8%**
Total NOII	**562**	**657**	**721**	**-22.0%**	**-14.4%**	**1,220**	**1,505**	**-18.9%**
Gross DPS (sen)	**8.0**	**-**	**7.5**	**n.m.**	**n.m.**	**8.0**	**7.5**	**n.m.**
Core EPS (sen)	**7.3**	**7.2**	**7.1**	**2.4%**	**1.3%**	**14.5**	**15.0**	**-3.4%**
Gross loans	367,965	362,732	352,071	4.5%	1.4%			
Gross impaired loans	1,066	1,061	1,242	-14.2%	0.5%			
Customer deposits	388,252	384,752	375,152	3.5%	0.9%			
CASA	123,495	120,177	111,505	10.8%	2.8%			

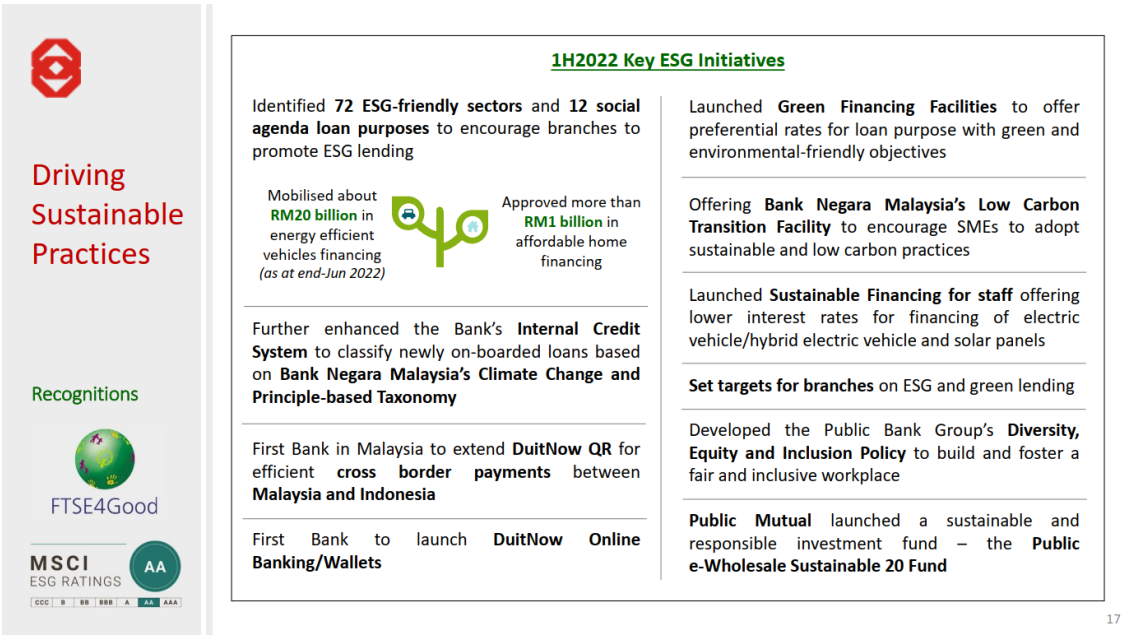
Source: Public Bank, MIDFR

EXHIBIT 2: QUARTERLY FINANCIAL RATIOS

Financial Ratios (%)	2QFY22	1QFY22	2QFY21	Yoy (+/- ppts)	Qoq (+/- ppts)	1HFY22	1HFY21	Yoy (+/- ppts)
NIM (Reported)	**2.29**	**2.24**	**2.26**	**0.03**	**0.05**	**2.26**	**2.27**	**-0.01**
NOII/Total income	17.7	20.9	22.6	-4.9	-3.2	19.3	23.4	-4.2
ROE (Ann.)	**11.2**	**11.7**	**11.7**	**-0.5**	**-0.4**	**11.2**	**12.3**	**-1.2**
Cost-to-income ratio	33.8	33.2	31.3	2.4	0.6	33.5	31.6	1.9
Net credit costs (Ann.) (bps)	9	11	45	-36	-2	10	34	-24
GIL ratio	0.29	0.29	0.35	-0.06	0.00			
Loan loss coverage	388.8	382.5	275.1	113.7	6.3			
L/D ratio	93.7	93.2	92.9	0.8	0.5			
CET1	14.1	14.3	14.3	-0.2	-0.2			
Tier-1	14.2	14.4	14.3	-0.2	-0.2			
Total Capital	17.2	17.5	17.5	-0.2	-0.2			

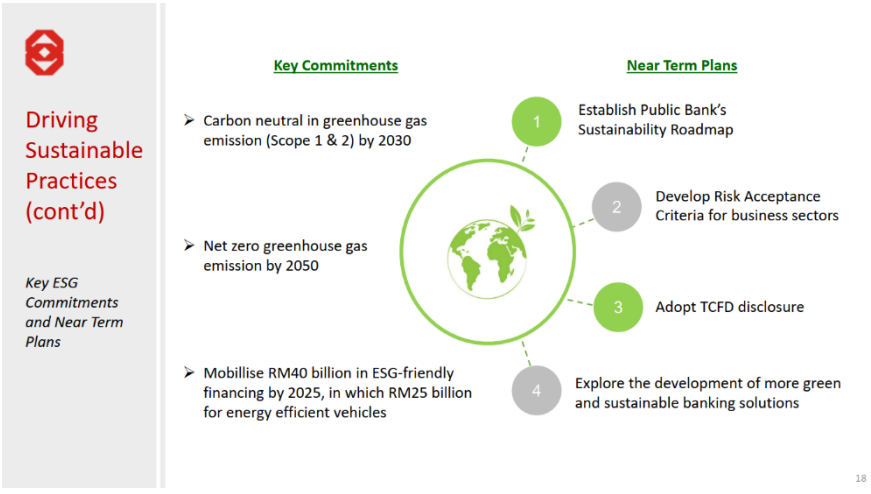
Source: Public Bank, MIDFR

EXHIBIT 3: Key ESG Initiatives



Source: Public Bank, MIDFR

EXHIBIT 4: ESG Key Commitments and Near-term Plans



Source: Public Bank, MIDFR

INVESTMENT STATISTICS

INCOME STATEMENT

FYE Dec (RM m)	FY20	FY21	FY22F	FY23F	FY24F
Interest income	14,184	13,475	14,936	16,391	17,905
Interest expense	(7,004)	(5,160)	(5,980)	(7,012)	(8,123)
Net interest income	**7,180**	**8,315**	**8,956**	**9,379**	**9,782**
Islamic banking income	1,311	1,614	1,710	1,796	1,868
Other operating income	2,821	2,616	2,293	2,335	2,536
Total income	**11,312**	**12,544**	**12,959**	**13,509**	**14,185**
OPEX	(3,909)	(3,965)	(4,147)	(4,323)	(4,539)
PPOP	**7,403**	**8,579**	**8,812**	**9,186**	**9,646**
Loan allowances	(1,106)	(1,201)	(440)	(460)	(480)
Other allowances	(14)	(6)	(11)	9	9
JV & Associates	2	(5)	5	5	5
Pretax profit	**6,285**	**7,367**	**8,367**	**8,741**	**9,180**
Taxation and zakat	(1,353)	(1,637)	(2,426)	(1,879)	(1,974)
NCI	(61)	(73)	(71)	(82)	(86)
Reported net profit	**4,872**	**5,657**	**5,869**	**6,779**	**7,120**
Core net profit	**4,872**	**5,657**	**5,869**	**6,779**	**7,120**
Total NII	8,304	9,793	10,496	10,995	11,463
Total NOII	3,008	2,751	2,955	3,053	3,163

BALANCE SHEET

FYE Dec (RM m)	FY20	FY21	FY22F	FY23F	FY24F
Cash and ST funds	19,698	17,531	18,061	17,935	17,780
Investment securities	77,735	80,431	82,654	85,693	90,230
Net loans	342,803	354,052	371,996	388,983	405,768
Other IEAs	203	-	-	-	-
Non-IEAs	10,818	10,725	10,843	21,608	22,168
Total assets	**451,257**	**462,739**	**483,554**	**514,219**	**535,946**
Customer & bank deposits	376,613	388,518	406,717	425,014	442,647
Other IBLs	17,896	17,688	16,546	15,297	14,056
Non-IBLs	8,321	7,108	8,748	17,424	22,340
Total liabilities	**402,830**	**413,314**	**432,011**	**457,734**	**479,043**
Share capital	9,418	9,418	9,418	9,418	9,418
Reserves & retained profit	37,831	38,745	40,819	45,636	46,043
Shareholders' funds	**47,248**	**48,163**	**50,237**	**55,054**	**55,461**
NCI	1,178	1,263	1,306	1,431	1,442
Total equity	**48,427**	**49,425**	**51,543**	**56,485**	**56,903**
Total liabilities & equity	**451,257**	**462,739**	**483,554**	**514,219**	**535,946**
Total IEAs	440,439	452,014	472,711	492,611	513,778
Total IBLs	394,509	406,206	423,263	440,310	456,703
Gross loans	345,651	358,027	374,996	391,483	408,068
CASA	105,600	118,001	122,063	126,946	132,024

FINANCIAL RATIOS

FYE Dec (RM m)	FY20	FY21	FY22F	FY23F	FY24F
Interest (%)					
NIM	1.95	2.22	2.27	2.28	2.28
Return on IEAs	3.32	3.02	3.23	3.40	3.56
Cost of funds	1.81	1.29	1.44	1.62	1.81
Net interest spread	1.51	1.73	1.79	1.77	1.75
Profitability (%)					
ROE	10.7	11.9	11.9	12.9	12.9
ROA	1.1	1.2	1.2	1.4	1.4
NOII/Total income	26.6	21.9	22.8	22.6	22.3
Effective tax rate	21.5	22.2	29.0	21.5	21.5
Liquidity & Efficiency (%)					
Cost-to-income ratio	34.6	31.6	32.0	32.0	32.0
Loan/Deposit ratio	93.7	93.1	93.4	93.4	93.6
CASA ratio	28.9	31.0	30.6	30.5	30.4
Asset Quality (%)					
GIL ratio	0.36	0.31	0.42	0.37	0.33
NIL ratio	0.29	0.24	0.28	0.00	0.00
LLC ratio	227.7	360.7	189.0	172.1	170.5
LLC (incl. reserves)	325.1	383.2	206.3	266.8	276.7
Gross credit cost (bps)	39	40	18	18	18
Net credit cost (bps)	33	34	12	12	12
% Floating rate loans	21.9	21.4	21.0	21.0	21.0
% Domestic loans	93.7	93.5	93.5	93.5	93.5
Capital (%)					
CET 1	14.8	15.0	14.8	14.5	14.2
Tier 1 capital	14.8	15.0	14.8	14.5	14.2
Total capital	17.9	18.2	17.9	17.3	17.0
Growth (%)					
Total NII	(3.5)	17.9	7.2	4.8	4.3
Total NOII	20.7	(8.5)	7.4	3.3	3.6
Core net profit	(11.6)	16.1	3.8	15.5	5.0
Gross loans	0.0	0.0	0.0	0.0	0.0
Customer deposits	3.5	4.0	4.7	4.5	4.2
CASA	18.9	11.7	3.4	4.0	4.0
Valuation metrics					
Core EPS (sen)	25.1	29.1	30.2	34.9	36.7
Gross DPS (sen)	13.0	15.2	15.1	17.5	18.3
Div payout ratio (%)	51.8	52.2	50.0	50.0	50.0
BVPS (RM)	2.4	2.5	2.6	2.8	2.9
Core P/E (x)	18.4	15.9	15.3	13.3	12.6
Dividend yield (%)	2.8	3.3	3.3	3.8	4.0
P/BV (x)	1.9	1.9	1.8	1.6	1.6

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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.
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