Banking

Hawkish Headache

POSITIVE (Maintain)

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HIGHLIGHTS

- **Possible US interest rate hikes could provide downside to non-fee income, but if OPR and other regional interest rates follow in a similar direction, we should see some NIM benefit.**
- **Expect a weak 2QCY26 results season and several negative guidance revisions. Downward pressure comes from continual exacerbation of deposit competition, heavier provisioning due to persistent geopolitical tensions (even though asset quality worries are not that concerning), and minimal room for further dividend upside this quarter. However, we expect these headwinds to dial down by CY26.**
- **Also, a strong local economy seems to be buoying domestic loan growth for now, which we would argue is the best thing the banking sector has going for itself.**
- **Maintain POSITIVE call: 2QCY26 may be a tough results season, but we are confident that the sector's outlook will brighten soon after.**

Sector Verdict

The sector has its share of headwinds, but we think fears may be overblown. CY26's profitability may come in weaker, but asset growth prospects and dividend yields are intact.

Core Themes

1. ▲ **Core beneficiary of emerging market inflows.** Our robust economic growth outlook, excellent dividend yields, superior asset quality, and high capitalisation levels give our banks a more defensive nature, making them an attractive pick.
2. ▲ **Dividend outlook remains extremely bright.** Capital ratios remain elevated, and the Basel transition is capital accretive in most cases. Some banks have already announced special dividends, though we don't expect many positive surprises in the coming quarter.
3. ▲ **Expect fee income to drive the topline, though non-fee income could see some normalisation.** Wealth management, bancassurance, and debt capital markets are major drivers. Forex volatility aside, the stabilisation of interest rates should result in some moderation in investment income – hence, expect normalisation from CY25's strong result. A Fed rate hike could further adversely affect investment income (but provide a positive offset via forex gains).
4. ▲ **Loan growth is ramping up.** So far, banking stats suggest that loan growth is performing better than expected – particularly the business loan segment. Banks with large international exposure may find it more difficult: Despite solid pipelines, currency fluctuations may crimp the loan growth of these banks.
5. ► **Liquidity is getting tighter.** CASA growth remains strong, and non-deposit funding is still a very attractive option. Despite this, we get a sense that banks were not expecting such strong loan demand – as a result, an ongoing scramble for deposits is elevating FD rates.
6. ► **Fairly optimistic on NIMs, but deposit competition may cause negative surprises.** Some banks are positive on NIM, premised on further FD release. Several banks also see limited room for further optimisation, especially as deposit competition ramps up sharply (and we are not expecting any OPR hikes this year, despite the Fed's hawkish stance). On the asset side, expect more aggressive loan rebalancing, favouring higher-yielding business loans.
7. ► **Rising cost pressures may pressure OPEX.** While we expect further tech efficiencies to come online, some banks are still investing heavily in tech and business expansion. Expect sharp OPEX growth among rapidly expanding smaller banks (and MAY).
8. ▼ **Minimal asset quality issues ahead – but provisions are a different issue.** Middle East tensions have all but abated, but oil prices have improved significantly from pre-MOU highs (even during recent skirmishes). Also, heightened cost pressures will take some time to abate as supply chains normalise. So far only a few banks have sounded alarm bells for asset quality – but do not expect anything overly severe. However, since geopolitical volatility is here to stay, expect large overlay allocations in subsequent quarters.

COMPANY *IN FOCUS*

HL Bank

Maintain BUY | Target Price: RM30.50
Price @ 14 July 2026: RM22.24

- Loan growth is very high for a mid-sized bank.
- Defensive pick: Asset quality and provisioning remain the industry's best.
- Sharp NOII growth persists from regional offerings. "Low-hanging fruit" is still close.

SHARE PRICE CHART



ABMB

Maintain BUY | Target Price: RM5.92
Price @ 14 July 2026: RM4.82

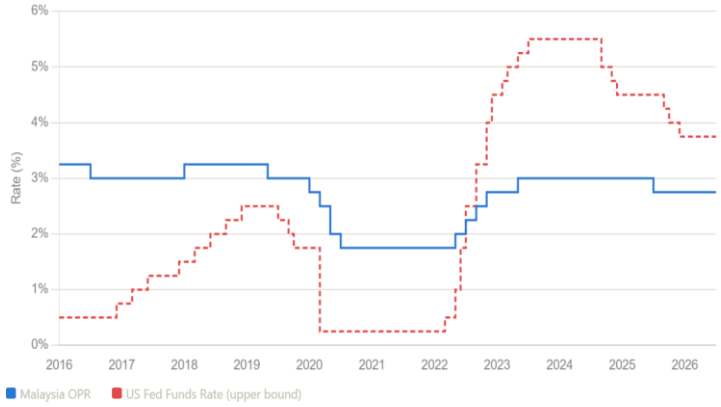
- Extremely high loan growth and market share capture to continue.
- Expect lower cost pressure, as the brunt of costs was frontloaded in the beginning stages of ACCELER8.
- Fee income is ramping up, particularly from the wealth management end.

SHARE PRICE CHART



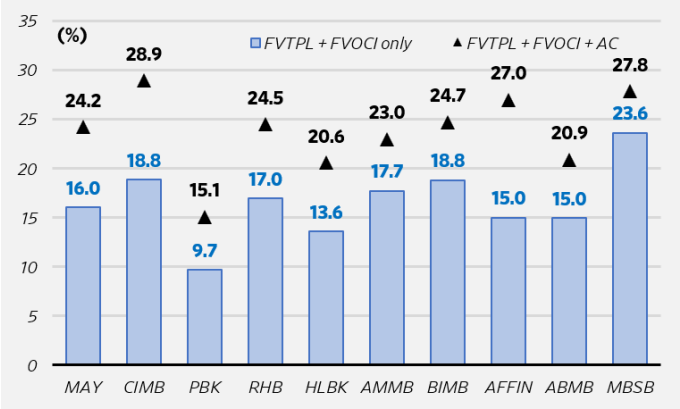
Possible interest rate hikes in the US are not good for the non-fee income component of NOII. The prolonged war in the Middle East is driving up inflation in the US. Judging by the hawkish nature of the latest Fed statement, we could see sharp Fed Funds Rate (FFR) hikes to combat it. Other countries will attempt to preserve their currency by following suit. Interest rate hikes tend to be bad for investment income as they cause bond prices to fall, though we could see a potential forex-related windfall. **CIMB** and **AFFIN** have a particularly heavy reliance on their investment books.

Fig 1: OPR vs Fed Fund Rate



Source: Trading Economics, MBSBR

Fig 2: Investment Book as % of total assets



Source: Banks, MBSBR

Fig 3: Quarterly NOII Breakdown



Source: Banks, MBSBR

FFR hikes may not necessarily translate to OPR hikes – but if it does, expect some boost to NIM. Whether or not BNM decides to hike the OPR remains a different issue, as BNM usually prevents the OPR from shifting as sharply as the FFR. Recall that Malaysia was one of the few countries that maintained a very low OPR during the pandemic era, with an extremely large interest rate differential and was hit by a sharp deterioration in the MYR. Even if an OPR hike happens, we are not expecting it to move up too steep a quantum. Our house view does not forecast an OPR hike in CY26. An OPR hike provides NIM uplift, with **AMMB, BIMB** and **PBK** expected to see the most benefit to earnings. As regional markets such as Singapore and Indonesia will likely follow the FFR's movements more closely, banks with larger regional exposure (namely **MAY** and **CIMB**) could potentially see some benefit as well (though note that the pass-on mechanism in Indonesia is not as efficient, which complicates the NIM uplift process).

FIG 4: +25bps OPR hike impact on NIM

Banks	Full-year NIM Impact (bps)	Minimum FY27 Core NP uplift*
MAY	2 – 3	0.8%
CIMB	2 – 3	0.8%
PBK	4	1.5%
RHB	3 – 4	1.4%
HLBK	3 – 4	1.0%
AMMB	5	2.2%
BIMB	3	1.5%
AFFIN	1 – 3	0.6%
ABMB	2 – 2.5	0.9%

**For AMMB and ABMB, we use FY28 figures.*
Source: Banks, MBSBR

We are expecting a lacklustre 2QCY26 results season for several reasons:

1. **Expect several negative guidance revisions.** The main threats come from the NIM and NCC downside possibilities. Expect negative revisions to metrics such as ROE, NIM and NCC, and possibly CIR (given the cost inflation is expected to persist, while topline sees impact from elevated COF). Recall that in the last result season, most banks were not expecting the Middle East war to persist this long – and even then, they were already warning of possible negative revisions in 2QCY26. Indirectly, the ongoing Middle East war could bode poorly for non-fee income prospects: It exacerbates global inflation, which could lead to rate hikes across the world (a scenario bad for investment income).

FIG 5: Guidance from the 1QCY25 Results season

	P/L Statement			Balance Sheet			Asset Quality	
Bank	ROE	NIM	Cost /Inc. ratio	Loan growth	CASA ratio	Div payout	GIL ratio	NCC (bps)
MAY	>11.8	2.05 - 2.10 (from 2.05)	<49	4 - 5 (CC)		~72		20
CIMB	11.0 - 11.5	2.08 - 2.18 (from 2.13)	<47	Asset: 5 - 7 (CC) Loans (Unofficial): Mid-single-digit		55 + Special div		25 - 35
PBK	12.0 - 13.0	Mid single-digit squeeze (from 2.15)		4 - 5		60 + Special div		Single digit
RHB	10.8 - 11.0	1.83 - 1.86 (from 1.80)	45.5 - 46.0	5 - 6	>30	50 - 60	1.35 - 1.40	13 - 14
HLBK	11.5 - 12.0	1.80 - 1.90 (from 1.90)	39	6 - 7	>32		<0.65	<10
AMMB	>10	Stable for now (from 1.98)		To match GDP				<21
BIMB	>7.0	2.07 - 2.10 (from 2.07)	64 - 65	7 - 9		60	<1.1	28 - 33
AFFIN	5.0 PBT: RM850m	1.55 (from 1.45)	67	10	31	40 - 60	1.80	
ABMB	10.0 - 10.5	2.28 - 2.35 (from 2.34)	47.5 - 48.5	7.5 - 10.0 (includes assets)		40 - 50		27 - 32
MBSB	5 - 6	2.0 (from 1.95)	<53	7 - 8		80 - 90	4.0 - 5.0	40 - 50

Source: Banks, MBSBR

2. **Domestic loan growth is coming in above expectations, but it may be causing a liquidity crunch. This is intensifying deposit competition, raising the likelihood of negative NIM surprises.** The loan growth is driven by business loans. We do not think it is fair to solely attribute the surge in working capital loans to cost inflation; Purchasing Managers Index (PMI) data is up (a positive indicator of economic expansion), and exports came well above expectations (signifying possible frontloading by international buyers, trying to lock in products before further price increases)**.** There is some speculation that a sizeable chunk of the loans is data centre related. Whatever it is, it's doing a good job buoying loan growth in a time when multiple companies are delaying projects to wait out the cost inflation.

   The deposit competition during the last results season was bad enough; anecdotal evidence suggests that it has only been exacerbated since then – which puts pressure on pre-existing NIM guidance. We do not think the current deposit competition is irrational; domestic loan growth (particularly on the non-household end, as implied by BNM's stats) came in much stronger than expected – the banks' response is to scramble for liquidity. We are more optimistic on a longer-term outlook – the upsurge in business loans is good for asset yield optimisation. Also, we should see stability on the OPR front: MPC's recent statements suggest that a change is unlikely for the time being – even in the event the US hikes rates (in response to the inflation caused by the prolonged conflict). In the event of sharp global interest rate hikes, also expect a downside to the investment income component of non-fee income.

FIG: NIM Commentary

Banks	NIM guidance	1QCY26 Qtr's NIMs	Additional notes
MAY	2.05 – 2.10 (from 2.05)	2.14	► NIMs will be attempted to be kept stable. There are both opportunities for upside and downside.
CIMB	2.08 – 2.18 (from 2.05)	2.08	▲ NIM compression has bottomed out in various geographies. NIAGA may be a wildcard: Despite the recent hefty rate hike in ID, asset yields and FD rates don't translate as cleanly – hence, impact may not necessarily be positive.
PBK	Mid-single-digit squeeze (from 2.15)	2.11	▼ Among the worst guidance in the industry, with further compressions expected. Both declining loan yields and ongoing deposit competition exacerbate this decline.
RHB	1.80 – 1.90 (from 2.05)	1.86	▲ Very optimistic outlook, with expansion expected, from ongoing CASA accumulation and asset/liability measures.
HLBK	1.80 – 1.90 (from 2.05)	1.84	▲ NIM recovery is happening slower than expected (hence this quarter's NIM expansion was rather limited) – but at least NIM is expected to see further expansion.
AMMB	Stable for now (from 1.98)	1.97	► Stable at least for the next quarter. Admittedly limited room for further short-term optimisation, apart from alternative funding methods.
BIMB	2.07 – 2.10 (from 2.07)	2.06	▲ Expects further expansion or at least stabilisation, driven by both FD repricing and rising asset yields from portfolio revamp. Note, however, the Group has negatively tweaked its FY26 guidance this results season.
AFFIN	1.55 (from 1.45)	1.54	▼ NIM may have peaked this quarter, and compression is likely. Management acknowledges the challenging COF situation and is repricing its loan yields upwards to compensate.
ABMB	2.28 – 2.35 (from 2.34)	2.31	▼ High likelihood of compression – the Group has no issue with taking in pricier deposits as short-term funding of its high loan growth requirements.

Source: Banks, MBSBR

3. **The prime cause of share price overhang is the threat of further large overlays. This may remain, even though oil prices have eased up.** We expect banks to be prudent considering ongoing geopolitical volatility, so prepare for large overlays and possible negative revisions to NCC guidance this quarter, given that US-Iran tensions could not be resolved by Jun-26. More importantly, there is little indication that skirmishes within the Middle East region will end anytime soon, implying that heightened geopolitical tensions are here to stay. This drags out the share overhang, reducing the chances of a full-blown KLFIN rally before results season. The constant Middle East flare-ups also increase the incidence of US indices tanking – which usually results in Malaysian indices following suit. The market would benefit from clearer guidance on the NCC outlook for subsequent quarters, but unless the Middle East conflict wraps up anytime soon, we think the uncertainty is here to stay.

   Provisioning aside, the chances of significant asset quality deterioration have reduced drastically post-signing of the memorandum of understanding (MOU) between both countries. This is because WTI oil prices have improved to the 65-75 USD/Bbl range since the two countries agreed to the MOU on 15 Jun 2026 – though it has spiked up once again after the latest conflict (which we don't think is sustainable, anyway). The current prices remain under the >90 USD/Bbl range seen during the war – and well below the >100 USD/Bbl price range most banks input as "worst-case scenario" in their stress test models. We doubt it will return to those highs (or at least remain there for too long). Cost inflation may linger a little while longer but is certainly not as bad as once feared.

FIG 6: WTI Crude Oil prices (USD/Bbl)



Source: Trading Economics, MBSBR

4. **Only slight dividend upside this quarter, though only among two banks.** We are not expecting too many dividend upside surprises, as Basel implementation takes place on 1 July 2026, past the cutoff date for excess capital release to be reflected in 2QCY26's dividends (**PBK** has explicitly mentioned that its first special dividend issuance will be in 4QCY26). However, there's a possibility that **CIMB** may issue special dividends this quarter – it mentioned its intention to frontload special dividends to achieve ROE targets more quickly. There's a slim chance that **HLBK** could see an increase in dividend payout in its effort to maintain competitive dividend yields despite having rather tight capital – its Basel transition is expected to increase the CET1 ratio by +60bps. Smaller banks have indicated there is little room for dividend surprises, even more so given the need to allocate capital for the recent surge in loan growth. We think dividend surprises, if any, will likely happen in subsequent quarters.

FIG 7: Dividend Commentary

Banks	Basel Impact (bps)	Additional notes
MAY	**Neutral to slightly -ve (FY27)**	▲ Dividends will remain close to ~70% levels for now.
CIMB	**Mild uplift**	▲ Special dividend worth RM2.0b announced in FY25 (until FY27), separate from standard 55% payout. Management has no qualms about front-loading dividends to achieve FY26 ROE targets.
PBK	**+100**	▲ Special dividend announced, separate from standard 60% payout. RM3.5b from Basel changes to be spread across FY26-FY28. Possibly some extra from LPI's PBK share disposal proceeds. However, management guides that the first special dividend will only be issued in 4QCY26.
RHB	**+100 (FY28)**	▲ While the Group adheres to a standard payout of 60%, it will increase it slightly in years of better performance to get rid of excess capital.
HLBK	**+60**	▲ The Group intends to improve dividend payout to maintain competitive dividend yields. However, capital is a bit tight, and loan growth is rather strong.
AMMB	**Neutral/ +ve**	► Management did not commit to any specific dividend payout guidance.
BIMB	**+35-40**	► No upside expected to current 60% guidance – situation is not ideal, and capital is tight.
AFFIN	**+10-30 +200 (FY29)**	▲ In FY29, we could see a special dividend announced as AFFIN transitions to the IRB approach. This is estimated to release 200bps worth of capital.
ABMB	**+30-37**	► Expect dividend payout to remain at the lower end of 40-50% guidance. A raise back to the 50% level will only happen after the macroeconomic situation recovers.

Source: Banks, MBSBR

Maintain POSITIVE call. (Our comprehensive list of sector drivers is on the first page.)

Top downside risks include:

1. Disruptions to economic growth, which could lead to slower asset growth and asset quality issues.
2. An exacerbation in deposit competition, which will compress NIMs.
3. A prolonged Middle East conflict, which could lead to further asset quality flare-ups and instances of higher provisioning.

Top Picks: HL Bank (BUY, TP: RM30.50) and **ABMB (BUY, TP: RM5.92).**

PEER COMPARISON

Bank	Call	Share P	Target P	Upside	Mkt Cap	FY	P/B	ROE	LTG	COE	P/E (x)		P/B (x)		ROE (%)		Div Yield (%)	
	^Top Pick	(RM)	(RM)	(%)	(RM b)	Basis	(x)	(%)	(%)	(%)	FY26	FY27	FY26	FY27	FY26	FY27	FY26	FY27
MAY	BUY	11.00	12.01	9.2	133.0	FY27F	1.44	10.9	3.0	8.5	12.8	12.3	1.37	1.32	10.9	10.9	5.6	5.8
CIMB	BUY	7.77	9.29	19.6	83.1	FY27F	1.33	10.9	4.0	9.2	10.7	10.3	1.15	1.11	10.8	10.9	6.0	6.2
PBK	NEUTRAL	5.05	4.96	-1.8	97.5	FY27F	1.50	12.1	3.5	9.2	13.7	12.9	1.58	1.53	11.7	12.1	5.5	5.8
RHB	BUY	8.44	9.17	8.6	37.0	FY27F	1.08	9.4	4.0	9.0	11.0	10.8	1.04	0.99	9.6	9.4	5.4	5.5
HLBK	^BUY	22.24	30.50	37.2	45.6	FY27F	1.42	11.1	4.0	9.0	10.2	9.6	1.10	1.04	11.1	11.1	4.6	4.9
AMMB	BUY	6.57	7.63	16.1	21.7	FY27F	1.12	9.5	4.0	8.9	10.3	10.1	0.96	0.93	9.5	9.3	5.3	5.4
BIMB	NEUTRAL	2.13	2.30	8.0	4.8	FY27F	0.64	6.9	4.0	8.5	9.1	8.8	0.62	0.59	6.6	6.9	6.5	6.8
AFFIN	NEUTRAL	2.25	2.39	6.0	5.8	FY27F	0.47	4.8	3.0	6.8	10.4	9.4	0.46	0.44	4.5	4.8	3.9	4.2
ABMB	^BUY	4.82	5.92	22.8	8.3	FY27F	1.09	9.8	5.0	9.4	9.3	8.9	0.89	0.83	9.8	9.6	4.4	4.6
Total Weighted avg											11.9	11.4	1.27	1.22	10.7	10.8	5.5	5.7
Large-Cap	MAY, CIMB, PBK										12.5	12.0	1.38	1.33	11.1	11.3	5.7	5.9
Mid-Cap	RHB, HLBK, AMMB										10.5	10.1	1.05	1.00	10.2	10.1	5.0	5.2
Small-Cap	BIMB, AFFIN, ABMB										9.6	9.0	0.69	0.65	7.4	7.5	4.8	5.0

**Closing prices from 14 Jul 2026.*
**AMMB and ABMB use FY27F/28F values. ~HL Bank & HL FG uses FY23F/24F values.*

Pecking Order: [HLBK & ABMB] > [AMMB & CIMB] > [MAY & RHB] > [AFFIN & BIMB] > [PBK]

Source: MBSBR

Income Statement	Balance Sheet	Valuations & Sector
Core NP – Core Net Profit	LCR – Liquidity Coverage ratio	ROE – Return on Equity
PPOP – Pre-Provisioning Operating Profit	L/D ratio – Loan/Deposit ratio	GGM – Gordon Growth Model
NII – Net Interest Income	CASA – Current & Savings accounts	P/BV – Price to Book Value
NIM – Net Interest Margin	FD – Fixed Deposits	BVPS – Book Value per Share
COF – Cost of Funds	GIL – Gross Impaired Loans	BNM – Bank Negara Malaysia
NOII – Non-Interest Income	NIL – Net Impaired Loans	OPR – Overnight Policy Rate
MTM – Mark to Market	LLC – Loan Loss Coverage	SRR – Statutory Reserve Requirement
CIR – Cost to Income Ratio	NCC – Net Credit Costs	SBR – Standardised Base Rate
OPEX – Operational Expenses	GCC – Gross Credit Costs	ALR – Average Lending Rate
	CET 1 – Common Equity Tier 1	

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MBSB INVESTMENT BANK: GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	The stock price is expected to rise by >10% within 3 months after a Trading Buy rating has been assigned due to positive news flow.
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	The stock price is expected to fall by >10% within 3 months after a Trading Sell rating has been assigned due to negative news flow.

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