Banking

BNM Financial Stability Review: 2HCY20

OVERWEIGHT

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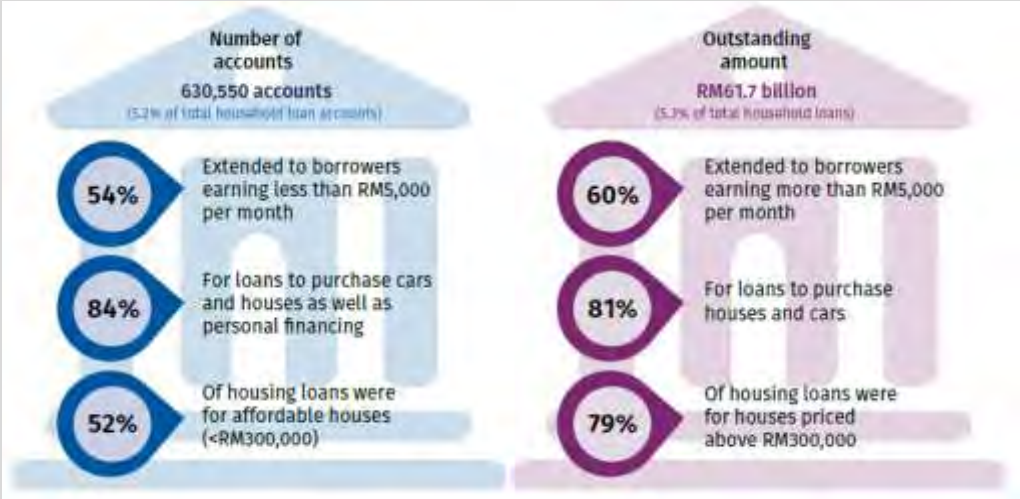
Yesterday, BNM released its Financial Stability Review report for the Second Half 2020. Despite operating in an unprecedented socioeconomic environment, our banking system remains resilient, upheld by strong liquidity management and capital adequacy practices. Going into 2021, BNM expects GDP growth to kick in from the revitalisation of local businesses, economic reopening and boosts from export demand, Covid-19 vaccinations, and supportive government policies. Meanwhile, targeted assistance programs are expected to persist in efforts to keep troubled borrowers afloat. We concur with BNM's optimistic tone, breaking away from the struggles of 2020. We also add that even if loans growth does not pick up alongside GDP, we are still assured that banks will operate in a better cost environment having provided for heavier allowances in 4QCY20 and due to their leaner cost structures from previous reorganisation exercises. We maintain our OVERWEIGHT call on the Banking sector with our preferred picks being: (i) MAYBANK (OP; TP: RM9.10) for its dividend yield potential and entrenched market leading position, and (ii) RHBBANK (OP; TP: RM6.40) for its industry-leading CET-1 reserves which provides strong capital safety in case further tightening is needed.

Sturdy enough to brace the impact. We came away from BNM's analysts briefing for its Financial Stability Review for 2HCY20 feeling reassured that our view of stronger recovery ahead are well founded and could bolster the banking sector in the coming quarters. To sum up the events of 2HCY20, various forms of movement control orders were implemented to navigate the society to curb the spread of Covid-19 while also finding a balance in economic activity. Monetary reliefs were introduced for those economically challenged in addition to the lapse of the Sep 2020 loan moratorium being bridged with assistance programs in the form of payment reduction or deferment. The combined effort is argued to have protected the financial market from further unprecedented volatilities preventing widespread defaults from households and SMEs.

Profile of Accounts Under Loan Moratorium



Source: BNM Financial Stability Review 2H20

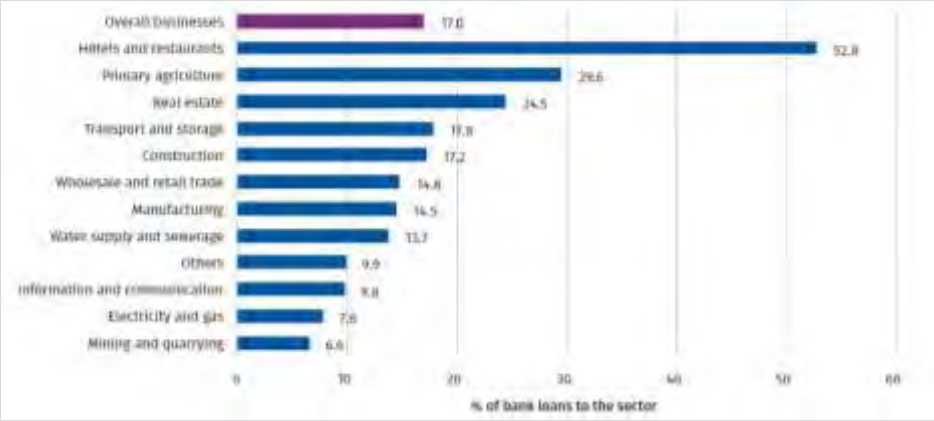
2HCY20 household debt-to-GDP at an all-time high of 93.3%. This was skewed by plunging GDP, no thanks to movement controls implemented since March 2020. Despite this, household debt continued to register some growth, albeit at a much slower pace, as households take advantage of the low interest rate environment for large discretionary purposes (i.e. residential property, motor vehicles) with the loan moratorium also keeping loan bases high by delaying potential defaults. 1HCY20 household debt-to-debt ratio was also toppish at 87.5% for the same reason.

(Refer to our concurrently released report "Banking: February 2021 Statistics" for further information regarding the monthly loan statistics)

Growth-enabled. For 2021, BNM expressed that a 6.0-7.5% GDP growth is not unreasonable, supported by progressive reopening of local business activities and loosening of movement controls, resurgence of export demand (particularly from the global technology upcycle), vaccination efforts and continued assistance from government initiatives to stimulate spending. Operationally speaking, we believe that banks should register better earnings growth even if GDP growth does not translate to better loans growth. This is premised on operating cost of banks remaining relatively lighter having invested in digitalisation and right-sizing in the prior year. Additionally, impairments are also anticipated to be less burdensome from frontloading of provisions in 4QCY20 and lower credit risk across most economic sectors.

Risks still exists, but more moderately. Heavy credit risk was a major concern from the previous chokehold on economic activity. As of Dec 2020, the banking system registered an annualised credit cost of 78 bps from a mere 8 bps in Dec 2019. Key sectors, such as construction and manufacturing are expected to pick up with national infrastructure projects and higher production, elevating cash flow and debt payment concerns. While certain sectors are expected to remain somewhat affected (i.e. aviation, tourism, retail), we opine that credit risks for 2021 is well contained with debt-servicing capacity for the overall business sector already improved to 4.1x in 2HCY20 as opposed to 3.9x in 1HCY20. On the flipside, the total loan loss coverage as of Feb 2021 registered at 107.4% (from 80.0% in Feb 2020).

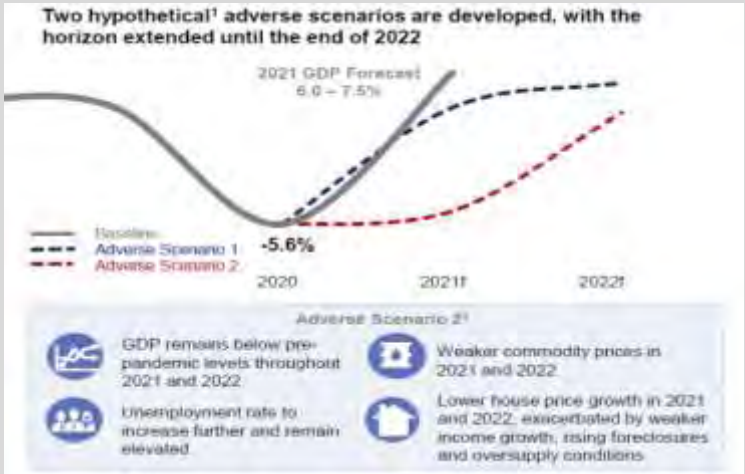
Share of R&R Loans by Sector



Source: BNM Financial Stability Review 2H20

Stressed and tested. To build confidence in the financial system, BNM conducted a stress test to gauge the effects of a weaker-than-expected GDP. From this test, it was derived that capital ratios for the banks would arrive at close to 16.8-17.0% in both scenarios (from 18.5% in Dec 2020), which is deemed adequate in the face of another prolonged economic slowdown.

BNM 2021 Stress Test Scenarios



Notes:

1Two hypothetical adverse scenarios were applied covering a 2-year horizon till end 2022, with adverse scenario 2 being the more severe of the two scenarios projected.

2 The economic scenarios do not represent the Bank's actual expectations for economic trajectory but rather, have been developed specifically for stress test purpose. These scenarios are not likely to materialise.

Source: BNM Financial Stability Review 2H20

Maintain OVERWEIGHT on the banking sector. While near-term prospects appear dim, we believe sentiment would encounter a kneejerk effect when decent economic recovery is posted. The rolling out of vaccination efforts would ultimately translate to less restrictive movement controls until we are able to make do without them all together. Additionally, we do not expect further OPR cuts for the year but welcome any hikes as it would enable better pricing opportunities for banks and also boost sentiment. Additionally, we do not anticipate further provisioning to be worrisome given that most banks have frontloaded their books during 4QCY20. In terms of stock picks, we like **MAYBANK (OP; TP: RM9.10)** for its industry-leading yield (7-8%) and high dividend-to-ROE spread amongst its peers. On the note of economic recovery, being the market share leader in domestic loans, MAYBANK could be poised to experience accelerated loans growth given its brand equity and outreach. Meanwhile, we also like **RHBBANK (OP; TP: RM6.40)** for its leading CET-1 ratio of 16.2%. This should enable enables greater allowance to implement capital management strategies. Additionally, RHBBANK offers the next best dividend returns of 4-5% amongst the rest of its conventional peers (2-4%).

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Appendix

Biannual Snapshot: Household Sector

Chart 1.14: Household Sector – Annual Growth of Debt

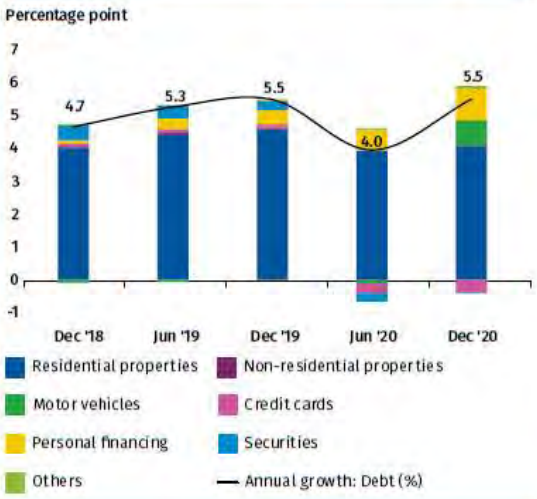


Chart 1.15: Household Sector – Key Ratios

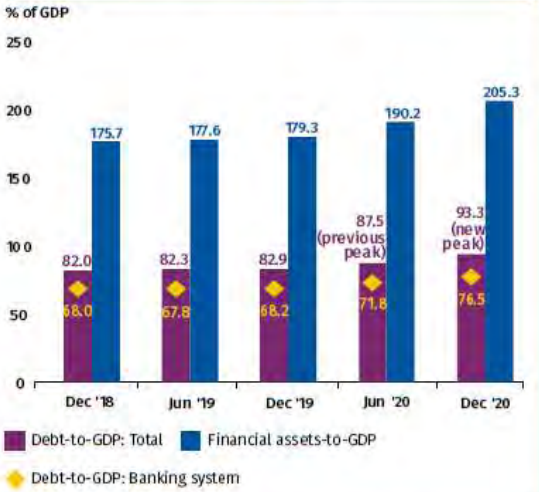


Chart 1.16: Household Sector – Annual Growth of Financial Assets

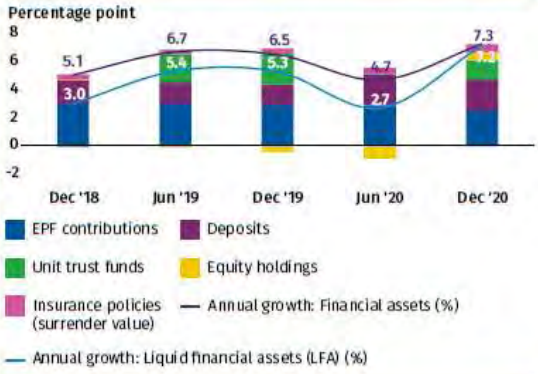


Chart 1.17: Household Sector – Leverage and LFA-to-Debt Ratios

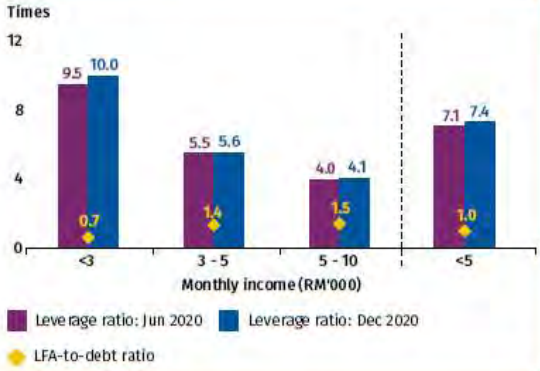


Chart 1.18: Household Sector – Debt by Monthly Income Group

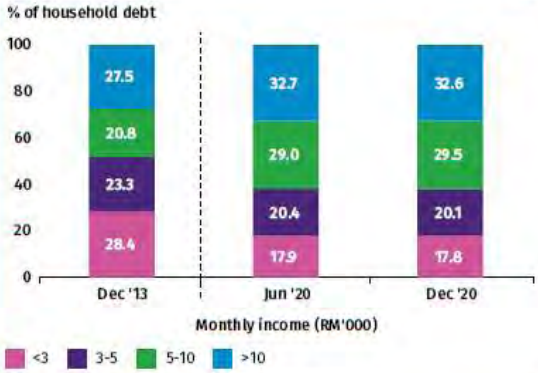
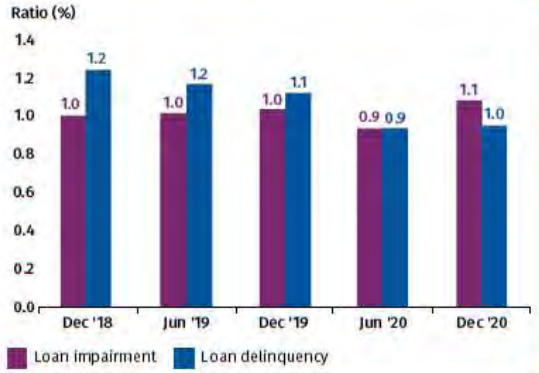


Chart 1.19: Household Sector – Loan Impairment and Delinquency Ratios in the Banking System



Source: Bank Negara Malaysia, Bursa Malaysia Berhad, Department of Statistics, Malaysia, Employees Provident Fund and Securities Commission Malaysia

Source: BNM Financial Stability Review 2H20

Biannual Snapshot: Property Markets

Chart 1.20: Property Market – Housing Transactions

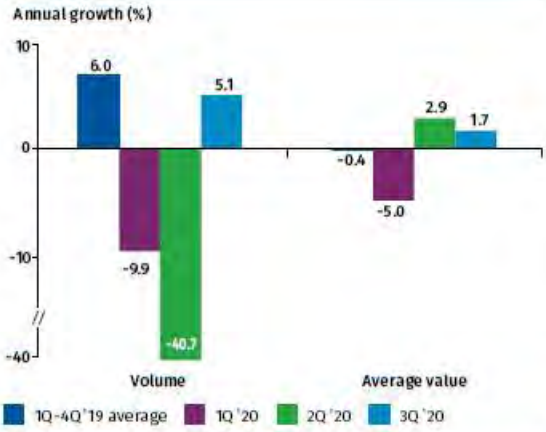


Chart 1.21: Property Market – Volume of Housing Loan Applications by Price Segment

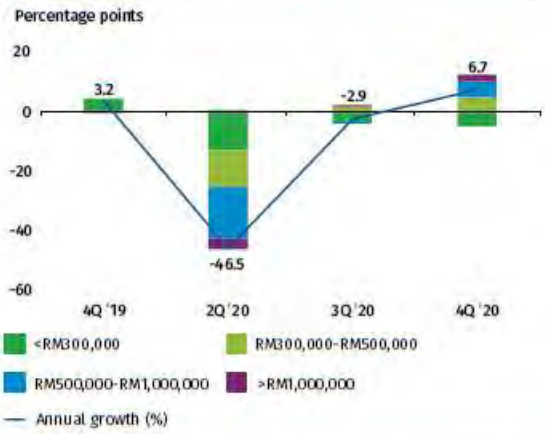


Chart 1.22: Property Market – Occupancy Rate for Hotels and Vacancy Rates for Office and Retail Space

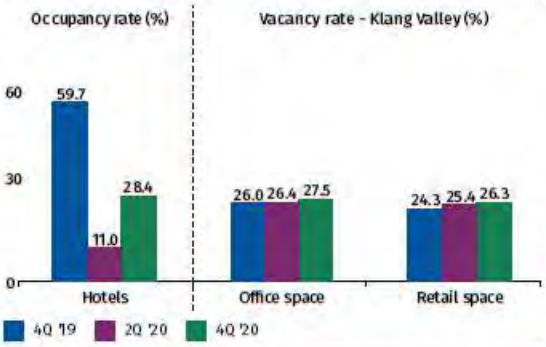


Chart 1.23: Property Market – Rentals for Prime Office and Retail Space in Kuala Lumpur

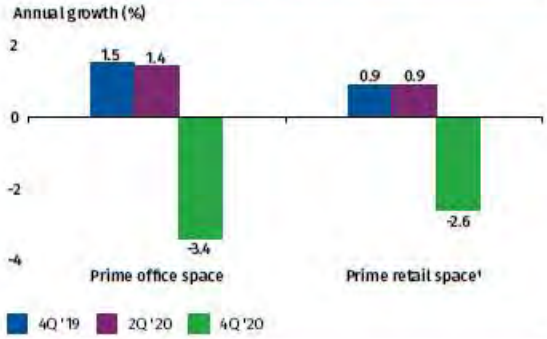
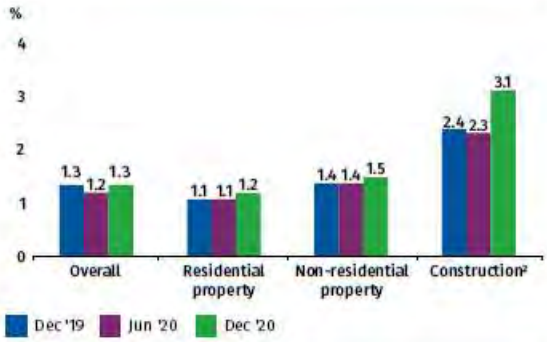


Chart 1.24: Property Market – Banking System's Exposure to Vulnerable Segments in the Property Market

Chart 1.25: Property Market – Loan Impairment Ratios by Segment



Note: 1. Average rents of the most prominent shops in major shopping complexes
2. Construction loans for residential and non-residential property, and working capital for firms in the real estate sector

Source: Bank Negara Malaysia, Jones Lang Wootton, Knight Frank, Malaysian Association of Hotels, Malaysia Tourism Promotion Board, National Property Information Centre (NAPIC) and Savills Malaysia

Source: BNM Financial Stability Review 2H20

Biannual Snapshot: Banking Sector

Chart 2.8: Banking System – Gross Impaired Loans Ratio

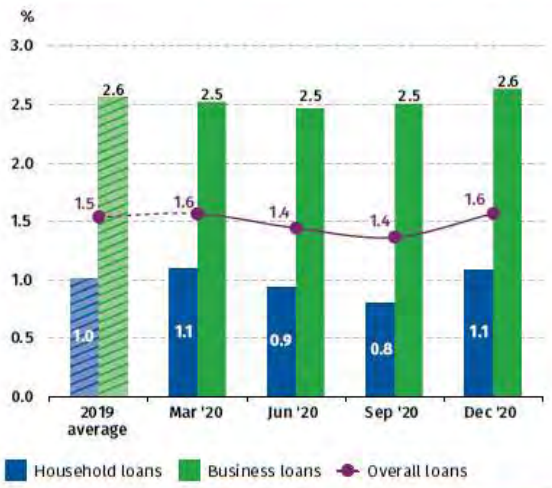


Chart 2.9: Banking System – Provisions

Chart 2.10: Banking System – Annualised Credit Cost Ratio

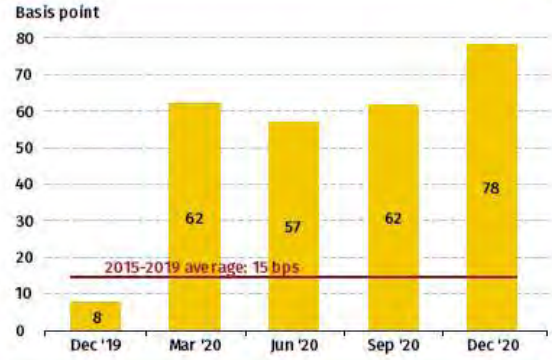


Chart 2.11: Banking System – Income, Cost and Profit before Tax

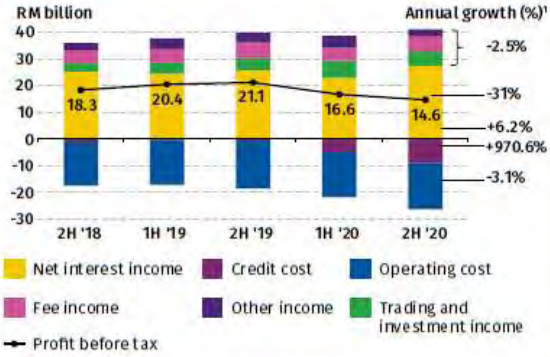


Chart 2.12: Banking System – Interest Margin and Average Cost of Deposits

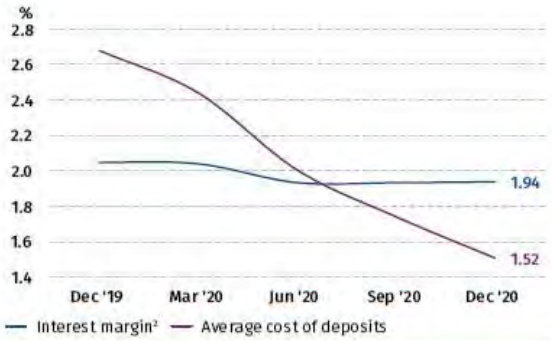


Chart 2.13: Banking System – Profitability

Note: 1. Annual growth computed based on figures for 2H 2019 and 2H 2020
2. Interest margin is the difference between interest rates at which banks extend financing and interest rates banks pay for funding, including deposits

Source: Bank Negara Malaysia

Source: BNM Financial Stability Review 2H20

Peer Table Comparison

Name	Last Price (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net DivYld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
Stocks Under Coverage																	
AFFIN BANK BHD	1.73	3,598.0	N	12/2021	-4.6%	2.7%	46.5%	11.2%	15.6	10.7	9.6	0.4	0.4	3.5%	2.9%	1.40	UP
ALLIANCE BANK MALAYSIA BHD	2.65	4,102.5	N	03/2021	-10.1%	-6.4%	-14.7%	34.8%	9.7	11.3	8.4	0.7	0.7	5.9%	2.3%	2.50	MP
AMMB HOLDINGS BHD	2.93	8,813.8	N	03/2021	-10.9%	4.6%	-205.4%	190.0%	6.6	N.A.	6.9	0.5	0.5	-7.9%	0.0%	3.05	MP
BIMB HOLDINGS BHD	4.23	7,840.9	Y	12/2021	7.6%	3.9%	6.1%	0.8%	11.0	10.3	10.3	1.2	1.1	11.5%	3.3%	5.25	OP
CIMB GROUP HOLDINGS BHD	4.34	43,065.7	N	12/2021	-9.3%	-0.3%	-73.8%	176.0%	9.4	36.1	13.1	0.8	0.8	2.1%	1.1%	3.60	UP
HONG LEONG BANK BHD	18.70	40,536.3	N	06/2021	14.8%	9.6%	14.3%	6.3%	15.3	13.4	12.6	1.4	1.3	10.1%	1.9%	18.50	MP
MALAYAN BANKING BHD	8.25	94,165.5	N	12/2022	-4.7%	2.8%	8.8%	19.7%	13.6	12.5	10.5	1.1	1.1	8.7%	6.8%	9.10	OP
MALAYSIA BUILDING SOCIETY BHD	0.660	4,603.8	N	12/2021	66.6%	3.0%	173.9%	14.4%	16.7	6.1	5.3	0.5	0.5	8.1%	4.5%	0.820	OP
PUBLIC BANK BHD	4.20	81,524.9	N	12/2021	1.4%	2.3%	15.6%	3.1%	16.7	14.5	14.0	1.7	1.6	11.6%	3.3%	4.55	OP
RHB BANK BHD	5.37	21,533.9	N	12/2021	-6.6%	-2.6%	-18.1%	16.0%	8.7	10.6	9.1	0.8	0.8	7.7%	3.3%	6.40	OP
Simple Average					**4.4%**	**2.0%**	**-4.7%**	**47.2%**	**12.3**	**13.9**	**10.0**	**0.9**	**0.9**	**6.1%**	**2.9%**		

Source: Kenanga Research

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Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

******Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.***

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