Banking

OVERWEIGHT
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Riding on Sustained Demand

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We maintain our OVERWEIGHT call on the sector. Global recessionary concerns continue to press market sentiment, though we believe it open up opportunities in the banking space. Recent performance of 2QCY22 GDP (+8.9%) and Aug 2022 exports (+48% YoY) are highly supportive of growth prospects and demand for business loans. While this may taper down in 2023, we anticipate a continuing OPR up-cycle (two additional 25 bps hikes to 3.00% by 1QCY23) to cushion banking NIMs. For 4QCY22, we seek to pick names which are firmly positioned to benefit from the abovementioned boons, narrowing to those with: (i) a high growth SME-financing mix on better general economic performance, and (ii) optimal funds profile (i.e. low fixed-rate financing with high CASA mix). For the large cap banks, we highlight CIMB (OP; TP: RM6.35) which has also demonstrated defensive performance in NOII, contrary to most other banks thanks to its regional operations. MAYBANK (OP; TP: RM11.05) is still preferred for its dividend yield safety (7-8%). For the smaller banks, we look towards ABMB (OP; TP: RM4.20) which we awarded a higher ESG-rating thanks to its commendable green financing book. Fundamentally, the bank commands ROEs and dividend yields comparable to its larger cap peers.

OPR trajectory could be reaching its end. Approaching 4QCY22, we anticipate one last 25bps OPR hike in November. We do not anticipate BNM to be as aggressive as the US Fed following another 75 bps increase to the Fed Funds Rate (3.00-3.25%) in its September meeting as local inflation concerns are not as severe as abroad. While we do see gradual recovery to the supply chain and boosts to our overall economic output, developments in the Russia-Ukraine war could further press macro conditions, but we do not believe it would have as strong an impact as it did during the early days in Feb 2022.

Optimising tailwinds at hand. With the prospects at hand, we anticipate our newly revised GDP growth expectation of 6.7% to be met by a significant return in SME sector which was the most affected sector during past MCOs. Banking corporates also share similar sentiment with key loans growth strategies aimed at enabling SMEs to expand. Service sectors such as hospitality, retail and tourism are likely to be at the forefront. We identified the smaller cap banks (ABMB, AMBANK, and BIMB) to have a stronger SME identity which may solidify their position when this segment kicks off. Meanwhile, **in a rising rate environment,** it is more like that the banks with the greatest re-pricing power could capitalise on the introduction of higher rates. This would constitute having: (i) a low fixed rate financing mix, and/or (ii) a higher CASA-to-deposit ratio. Notably, BIMB and RHBBANK appear to have the highest variable loans rate profile while ABMB, CIMB and MAYBANK stand tall with CASA.

Loans and deposits profile of banks as of 2QCY22

	Large Cap Banks					Small Cap Banks				
2QCY22	**CIMB**	**HLBANK**	**MAYBANK**	**PBBANK**	**RHBBANK**	**ABMB**	**AFFIN**	**AMBANK**	**BIMB**	**MBSB**
Gross loans (RM'm)	394,307	168,234	575,332	367,965	204,926	46,098	55,429	120,126	60,700	36,838
Domestic SME proportion	13%	18%	13%	19%	15%	33%	17%	21%	20%	8%
Fixed rate financing %	19%	17%	27%	22%	12%	18%	25%	20%	8%	47%
Customer deposits (RM'm)	420,937	195,227	608,155	388,252	225,942	48,651	64,452	121,393	54,891	32,993
CASA-to-deposit %	44%	34%	45%	32%	29%	50%	21%	33%	36%	5%
Total assets (RM'm)	652,993	254,331	923,380	478,813	299,653	63,129	86,677	178,553	83,030	50,854
Shareholders' equity (RM'm)	60,323	30,989	84,698	49,098	27,428	6,325	10,098	17,017	6,669	8,556
Peer Loans Market Share	19.4%	8.3%	28.3%	18.1%	10.1%	2.3%	2.7%	5.9%	3.0%	1.8%
Peer Deposits Market Share	19.5%	9.0%	28.1%	18.0%	10.5%	2.3%	3.0%	5.6%	2.5%	1.5%
Loans growth (CY-YoY)	6.8%	8.0%	6.2%	4.5%	7.3%	6.7%	15.0%	3.9%	8.0%	2.8%
Deposits growth (CY-YoY)	3.0%	6.8%	4.9%	3.5%	4.8%	4.0%	19.8%	6.4%	11.6%	-7.5%

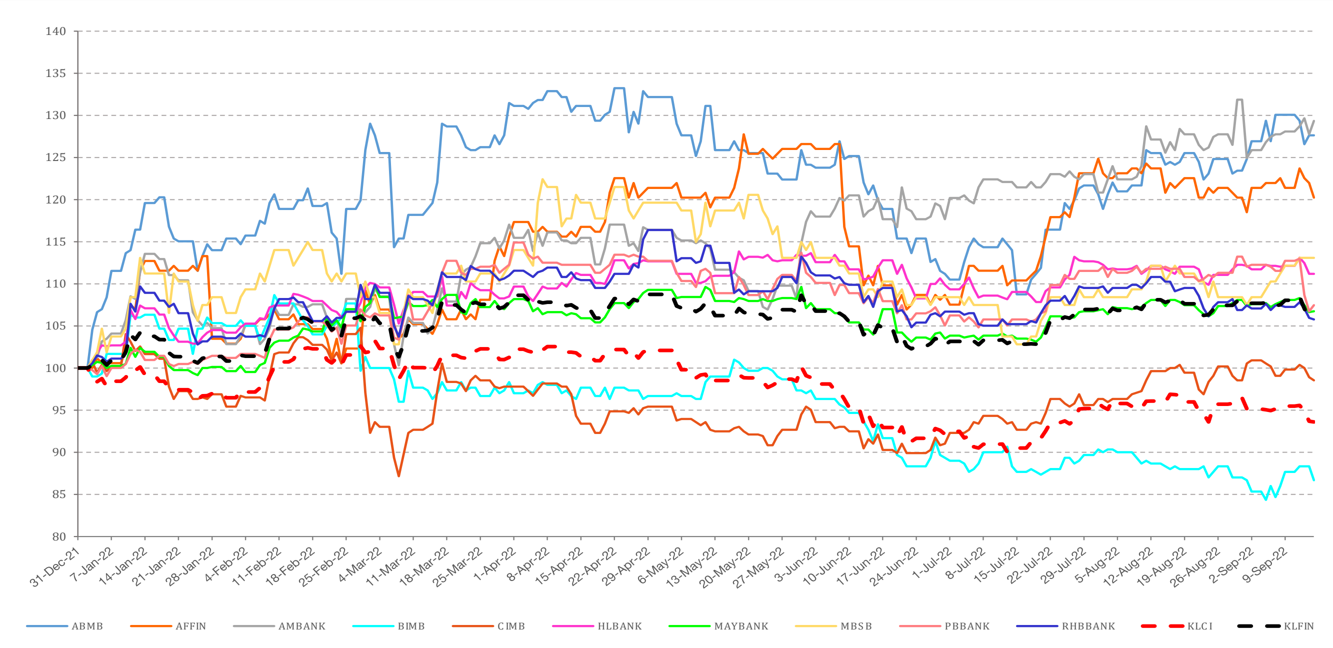
Source: Kenanga, Companies

(refer to the overleaf for further commentary on industry fundamentals)

Maintain OVERWEIGHT on the banking sector. The investment thesis for the banking sector's resiliency remains affirmed and we believe additional attention could be given to names which demonstrate stronger performance thanks to the factors mentioned above. On top of the industry-wide boons of: (i) progressive write-backs of Covid-19 loan provisions, and (ii) earnings-surge post-prosperity tax in CY23, we feature our large cap Top Picks for 4QCY22 - **CIMB (OP; TP: RM6.35)** which is expected to command defensive NOII numbers as trading performances are supported by its regional arm, whereas peers are expected to still report diminishing returns. It also helps that CIMB was recently awarded a 4-star ESG rating by us for its sustainable financing efforts. **MAYBANK (OP; TP: RM11.05)** continues to be a favourite for dividends (7-8% yield) for those concerned with capital safety amidst ongoing uncertainties. Meanwhile, we like **ABMB (OP; TP: RM4.20)** amongst the small cap banks for being the leader in SME profiling as well as its considerable CASA mix. The stock's fundamentals are also comparatively better than its larger cap peers in terms of ROE (10%) and dividend yields (6%).

Strength in banking stocks still holding up. We gather that the overall investment sentiment has been bogged down by ongoing macro concerns, which could be further amplified by developing unrest in certain regions, possibly allaying the mending of supply chain issues. Additionally, the rise in US Fed rates and recessionary concerns may cause foreign investors to exit less critical positions. That said, the banks are likely firmly positioned against the abovementioned headwinds as they are still poised to benefit from persisting loans growth tractions while benefitting from the OPR up-cycle to further cement profit margins. Only BIMB has yet to perform above index owing to earnings disappointments amidst untimely defaults from large corporate accounts and subsequent earnings misses.

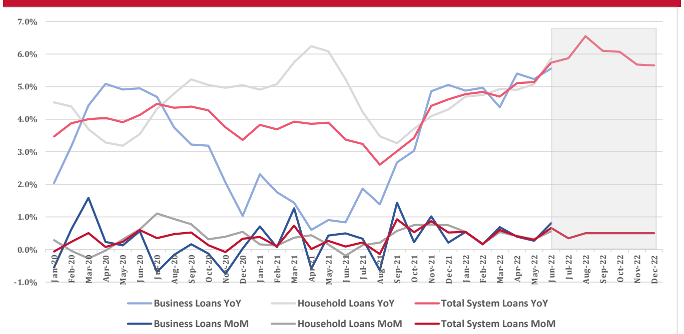
YTD Performance of Banking Stocks against the KLCI and Bursa Finance Index (KLFIN)



* as of our cut-off date at 15 Sep 2022
Source: Bloomberg

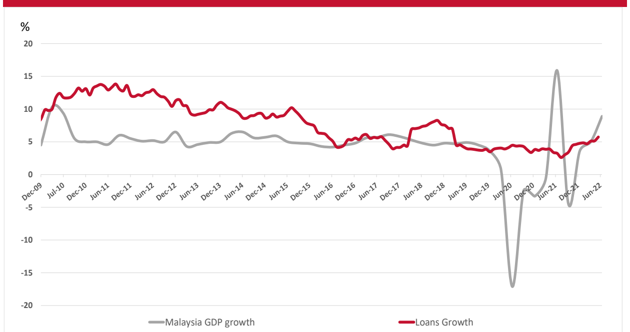
5.5-6.0% industry loans growth target firmly in line with GDP. July 2022 reported a 5.9% YoY system loans growth, which warranted us to upgrade our initial CY22 expectations from 5.0-5.5% to 5.5-6.0%. The recently reported 2QCY22 GDP growth of 8.9% further cements our view that our local economy is regaining its health and should translate to a higher demand for loans going forward. Albeit, there should be some easing in 4QCY22 as production bottlenecks ease but all this would justify our in-house 2022 GDP forecast of 5.7%. We anticipate the forerunners in the coming months to be business loans as working capital needs are expected to increase to cope with the growing economic output regardless of increasing OPR. Household loans may step back in meeting existing loan commitments while retailers may opt to capitalise on higher savings rates, instead.

YoY and MoM Loans Growth and Projection



Source: Kenanga

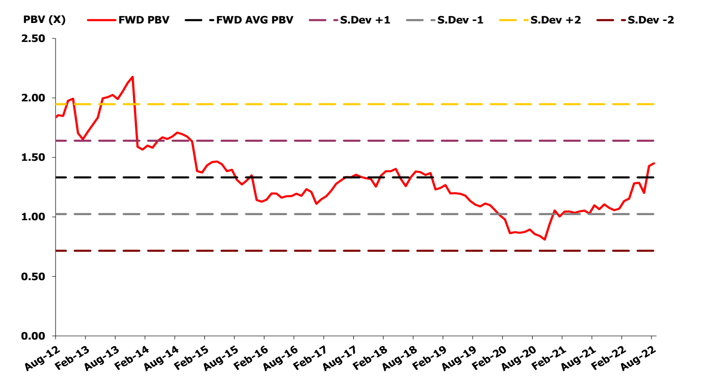
GDP and Loans Growth Trajectory



Source: Kenanga

Banking valuations are relatively inexpensive. Arising from the Covid-19 pandemic, the equities market saw a sell-down stemming from the first lockdown in March 2020 which is now seen to be normalising. The banking sector trended similarly but had enjoyed a quicker recovery in sentiment thanks to tailwinds from: (i) sustained loans growth, (ii) rising OPR expectations, and (iii) better-than-expected asset quality. We anticipate these merits to persist, now with the addition of bumper earnings in CY2023 as profits normalise from CY2022 one-off prosperity tax. In spite of this, we gathered that the banking sector's Fwd. PBV valuations are still fairly undemanding, closely trailing its 10-year mean. We anticipate valuations to only rise further in the coming periods as dividend prospects materialise from year-end reporting, barring unexpected macro developments.

10-year Fwd PBV Standard Deviation lingering at mean levels

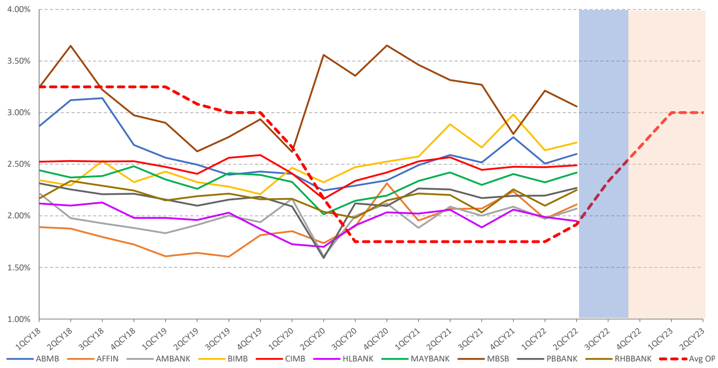


Source: Kenanga

Reaping OPR up-cycle. The plateauing of NIMs has expectedly ceased following the first OPR hike in May 2022, as the banks now have greater room for up-pricing loans books while rebalancing fixed deposit rates. CASA ratios could possibly taper down as fixed deposit products become more attractive, but it should still be outpaced by higher loan charges on average. That said, an outlier would be MBSB which would see further erosion as its high proportion of fixed financing products has nullified re-pricing opportunities. Meanwhile, other banks are guiding for an annualised NIMs expansion of 2-4 bps for each subsequent 25 bps hike.

Recall that we anticipated one further rate hike in BNM's November MPC meeting followed by another in the January or March 2023 meeting before steadying OPR at 3.00%.

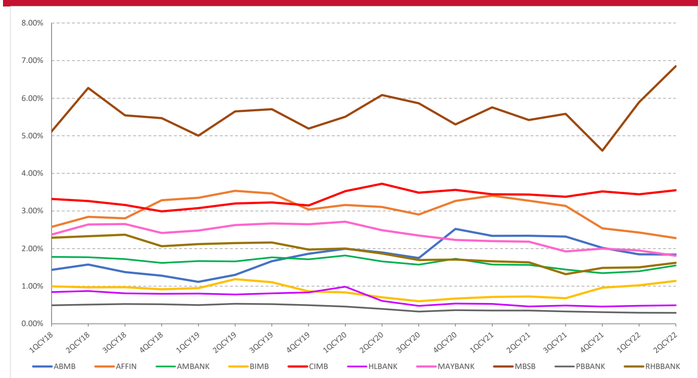
Est. Annualised NIMs



Note:
1. Blue bar indicates announced OPR yet to be reflected into reported earnings
2. Orange bar indicates our in-house OPR expectations in the coming periods
Source: Kenanga

Bump in GIL is not a concern. Sector-wide, GIL ratios did see an uptick during the 2QCY22 reporting season. However, we do not believe this would transpire to higher levels as we see it to be a normalisation of rates post-repayment assistance. Certain banks have notably been able to bring their GIL to more respectable levels and are expected to maintain similar asset quality as we do not anticipate further on-boarding of higher-risked assets. Notable performers are HLBANK and PBBANK which are amongst the industry lowest at 0.5% and 0.3%, respectively.

Est. GIL trends (1QCY18-2QCY22)



Source: Kenanga

Peer Table Comparison

Name	Rating	Last Price asa of 15 Sep 2022 (RM)	Target Price (RM)	Upside (%)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE (%)	Net. Div. (sen)	Net Div Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
Stocks Under Coverage																	
AFFIN BANK BHD	OP	2.12	2.45	15.6%	4,690.1	N	12/2022	28.0	35.7	12.3%	27.5%	7.6	5.9	0.4	5.9%	11.0	5.2%
ALLIANCE BANK MALAYSIA BHD	OP	3.72	4.20	12.9%	5,759.0	N	03/2023	44.8	51.0	21.0%	13.8%	8.3	7.3	0.9	10.5%	22.0	5.9%
AMMB HOLDINGS BHD	OP	4.05	4.75	17.3%	13,412.5	N	03/2023	49.8	54.2	9.4%	8.8%	8.1	7.5	0.7	9.5%	16.0	4.0%
BANK ISLAM MALAYSIA BHD	MP	2.58	2.45	-5.0%	5,560.6	Y	12/2022	19.5	24.4	-9.2%	23.0%	13.2	10.6	1.0	7.3%	9.7	3.8%
CIMB GROUP HOLDINGS BHD	OP	5.40	6.35	12.0%	56,561.0	N	12/2022	52.2	65.9	12.6%	26.2%	10.3	8.2	0.9	8.7%	26.0	4.8%
HONG LEONG BANK BHD	OP	20.86	23.35	11.9%	45,218.6	N	06/2023	194.3	201.5	21.0%	3.7%	10.7	10.4	1.3	12.3%	70.0	3.4%
MALAYAN BANKING BHD	OP	8.95	11.05	23.5%	107,131.6	N	12/2022	73.3	90.7	5.2%	23.7%	12.2	9.9	1.2	9.8%	60.0	6.7%
MALAYSIA BUILDING SOCIETY BHD	UP	0.595	0.505	-15.1%	4,267.0	N	12/2022	7.1	9.9	16.5%	39.3%	8.4	6.0	0.5	5.8%	3.5	5.9%
PUBLIC BANK BHD	MP	4.64	4.65	0.2%	90,065.6	N	12/2022	29.5	37.5	1.3%	26.9%	15.7	12.4	1.8	11.6%	15.5	3.3%
RHB BANK BHD	OP	5.77	7.00	21.3%	24,303.7	N	12/2022	65.4	78.7	-5.6%	20.3%	8.8	7.3	0.8	9.2%	32.0	5.5%
Simple Average										**8.4%**	**21.3%**	**10.3**	**8.5**	**0.9**	**9.1%**		**4.8%**

Source: Kenanga Research

Gordon Growth Model Inputs

Name	Cost of Equity (%)	Terminal growth (%)	Sustainable ROE (%)	Fair value P/BV (x)	Applied CY23E BVPS (RM)	Additional Remarks	TP (RM)	Call
ABMB	11.0	3.00	10.0	0.88	4.57	+5% ESG Premium	4.20	OP
AFFIN	11.3	3.00	7.0	0.48	5.08		2.45	OP
AMBANK	10.7	3.50	9.5	0.84	5.69		4.75	OP
BIMB	10.0	3.00	9.0	0.85	2.88		2.45	MP
CIMB	11.0	3.00	10.5	0.94	6.47	+5% ESG Premium	6.35	OP
HLBANK	9.7	3.50	12.0	1.37	17.02		23.35	OP
MAYBANK	9.7	3.25	12.5	1.43	7.70		11.05	OP
MBSB	12.0	3.00	6.5	0.39	1.30		0.505	UP
PBBANK	9.7	4.00	13.0	1.58	2.82	+5% ESG Premium	4.65	MP
RHBBANK	10.7	3.00	10.0	0.91	7.67		7.00	OP

Source: Kenanga Research

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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