

Banking Sector

(Neutral)

“Slower, But Leading Indicators Improving”

Banking sector is a NEUTRAL as we expect loans growth to decelerate to 6.8% (we downgraded our forecast in our previous report) in 2016 vs. 8.4% in 2015. Two biggest issues namely lethargic loans growth and tight liquidity may take the spotlight in 2016. Though we expect flat earnings performance for banking sector in 2016 but there are still drivers which could continue to support the banking sector namely 1) improvement in asset quality 2) leaner operating cost. Our Top Picks for banking sector are Public Bank (TP: RM21.38) and BIMB Holdings (TP: RM4.28).

Table 1: May 2016 Summary

Purpose (RM billion)	May-16	Apr-16	May-15	Y-o-Y	M-o-M	Comment
Loans growth	6.2%	6.3%	8.9%	↓	↓	Loans growth weakened by household segment and business segment
Loans Application	8.9%	-6.0%	-2.9%	↑	↑	Still commendable led by household segment
Loans Approval	4.5%	-17.2%	-1.6%	↑	↑	Cautious with the potential default, banks tighyening credit approvals
Loan Disbursement	3.2%	-1.8%	4.9%	↓	↑	Lower approvals led to lower disbursement
Loan Approval Rate	44.0%	42.1%	47.1%	↓	↑	Expect to slow down due to declining HH application
Gross Impaired Loan	1.65%	1.61%	1.59%	↓	↓	At healthy level due to stringent requirement loans selection
Deposits Growth	-0.4%	-1.2%	7.0%	↓	↑	Keen competition to secure low cost deposits to reduce NIM compression
Loan to Deposits	87.7%	87.7%	81.6%	↓	↑	The rising in deposit can cover the deficiency left by loans outstanding, thus maintain healthy LDR
Average Lending (ALR)	4.55%	4.60%	4.61%	↓	↑	The introduction of base rate aided banks ALR to recover
Basel 3 Ratio						
- Total Capital	16.4%	16.4%	15.1%	↑	↓	Well prepared for the Basel III requirements
- CET-1	13.8%	13.8%	13.1%			
- Tier-1	12.9%	12.9%	12.3%			

Source: BNM, M&A Securities

Summary May 2016 Banking Statistics

- Loans growth slipped in May 2016 to 6.2% y-o-y against 6.3% the previous month. Both household (HH) and business loan growth trended south
- HH loan growth touched 6.2%% y-o-y vs. 6.3% y-o-y in April, while business loan growth slowed further to 6.2% y-o-y from 6.3% y-o-y in April.
- Loans applications rebounded strongly to 8.9% y-o-y vs. -6.0% y-o-y in April, underpinned by immense rebound in business segment
- Loans approval followed stronger application in May with a growth of 4.5% vs. -17.2% in April. Strong performance was evidences in business segment.

Our View Loans Growth Outlook in 2016

- We expect soft earnings for banking sector in 2016 with slower macro-economic condition set to weigh on banking sector performance.
- Slower loans growth, tight liquidity, compression in net interest margin (NIM), rising credit cost and softer investment banking activities will be the key theme for banking sector in 2016.
- The reduction in Statutory Reserve Requirement (SRR) from 4% to 3.5% may not bring significant impact given only RM5 billion release into liquidity as compared to RM1,600 billion deposits in circulations. However, we expect the reduction in SRR will assist banks to relieve its cost of funds, albeit only marginally.
- For 2016, we expect a slower loans growth of 6.8% % y-o-y assisted by i) financing from business segment benefiting from the splurge of 1) financing for construction segment 2) continuous SME financing as economy driver 3) the implementation of minimum wages in 1st July 2016

Table 2: Y-o-Y Growth by segment

Purpose (RM billion)	Household			Business		
	May-16	Apr-16	May-15	May-16	Apr-16	May-15
Loans Growth	6.32	6.3%	9.2%	6.2%	6.3%	8.6%
Loans Application	5.4%	0.6%	-9.9%	12.6%	-13.7%	5.9%
Loans Approval	-12.1%	-24.1%	-17.8%	25.2%	-7.4%	30.6%
Loans Disbursement	-0.1%	-9.1%	6.5%	4.5%	1.4%	10.0%

Source: BNM, M&A Securities

Analysis of Banking Sector Operational Metrics

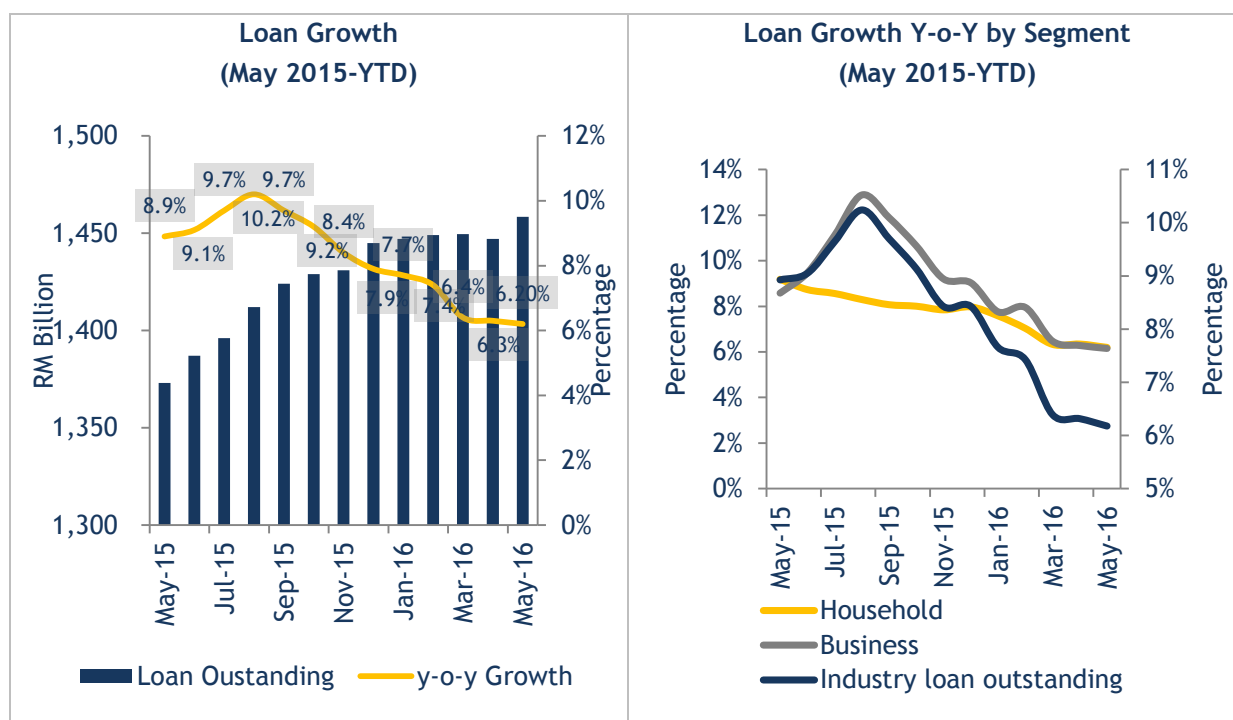
1. Industry loan growth continues to slow

- Loans growth continued to slip in May 2016 to 6.2% y-o-y vs. 6.3% y-o-y in April. Both household (HH) loan growth and business loan growth continued to trend south, with HH loan growth at 6.2% y-o-y vs 6.3% y-o-y in April, while business loan growth slowed further to 6.2% y-o-y from 6.3% y-o-y in April.
- In the HH segment, the slower loan growth was across the board with all purposes declined marginally. The growth was disappointing given May 2015 growth came from small base level (given the full swings impact of GST effect in April 2015). Key sectors reporting slower growth including 1) residential property 10.6% y-o-y vs. 10.8% y-o-y 2) non-residential property 7.6% y-o-y vs. 7.7% y-o-y.
- In business segment, key sectors were still sluggish with the recovery still uncertain at this point until we reach into 2H16 where the award of various construction package is expected to spur business segment. Key sector for May came from 1) real estate of 15% y-o-y 2) mining of 11% y-o-y 3) education of 9% y-o-y.
- Moving forward, we expect HH segment loans growth to continue to moderate due to GST related issue. On the other hand, we expect business segment will continue to grow in steady pace, supporting overall loans growth in 2016.

Table 3: Industry Loans Growth

Purpose (RM billion)	May-16	Apr-16	May-15	M-o-M	Y-o-Y
Purchase of Securities	71,123	70,616	76,165	0.7%	-6.6%
Transport Vehicle	168,175	168,481	167,847	-0.2%	0.2%
Of Which is Passenger Car	159,359	159,713	158,231	-0.2%	0.7%
Residential Property	453,879	450,480	410,429	0.8%	10.6%
Non-Residential Property	201,796	200,944	187,478	0.4%	7.6%
Other Fixed Assets	9,638	9,668	10,567	-0.3%	-8.8%
Personal Use	64,584	64,372	60,969	0.3%	5.9%
Credit Card	35,017	35,009	34,525	0.0%	1.4%
Consumer Durables	140	141	147	-0.7%	-4.7%
Construction	43,861	43,830	39,829	0.1%	10.1%
Working Capital	346,962	342,945	322,888	1.2%	7.5%
Other Purpose	63,339	61,359	62,815	3.2%	0.8%
Total	1,458,516	1,447,844	1,373,659	0.7%	6.2%

Source: BNM, M&A Securities



Source: BNM, M&A Securities

2. Loans Applications “Loans application offers glimpse of rebound in 2H16”

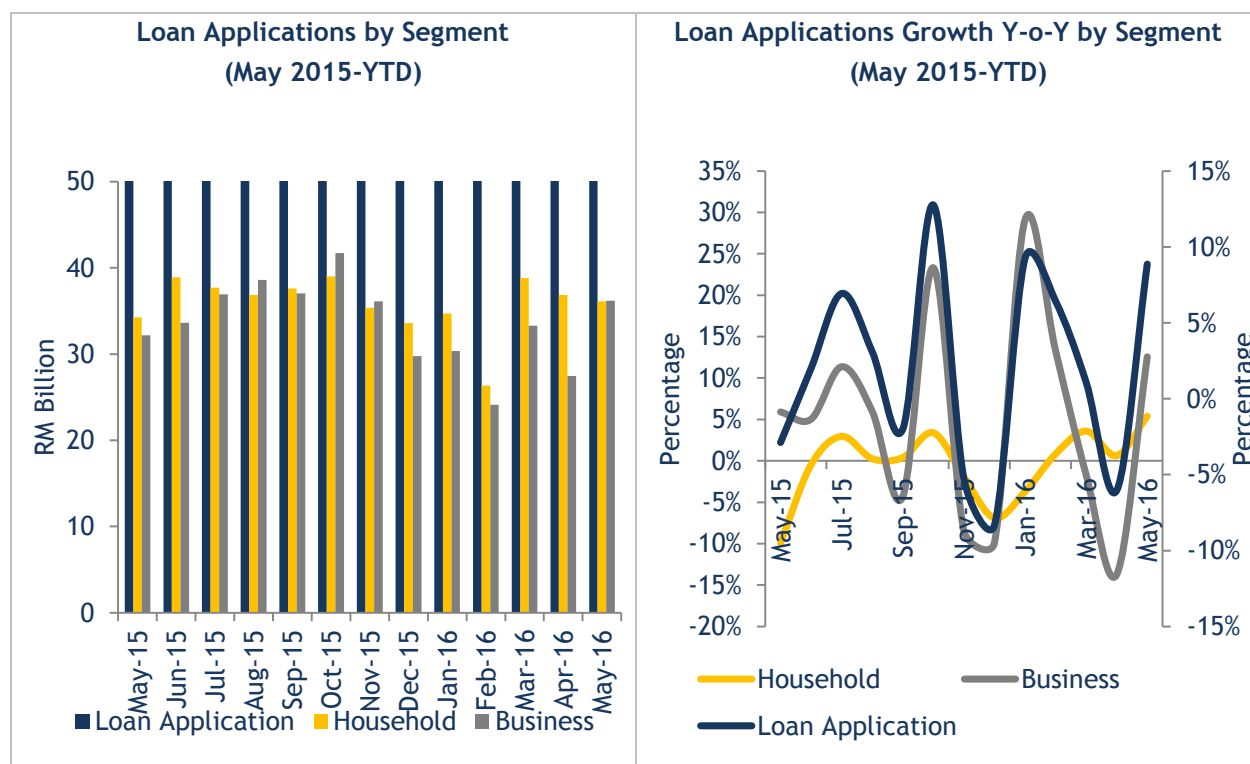
- Loans applications rebounded strongly by 8.9% y-o-y vs. -6.0% y-o-y in April underpinned by immense rebound in business segment
- Business segment grew to 12.6% y-o-y vs. -13.7% y-o-y in April, premised on sector such as 1) transport of 490% y-o-y 2) manufacturing of 23% y-o-y 3) agriculture of 23% y-o-y. We view that manufacturing is signalling recovery, pointing to higher growth in the coming months.
- HH segment application heading north supported from purchase of securities of 39% y-o-y vs. -34% in April. Whilst the rising of base rate by banks recently will ensure HH segment will continue in lethargic mode.

- Moving forward, we expect business loans will make up the deficiency of gap left by HH segment especially in the SME segment, propel by various incentives given by the government for this segment.

Table 5: Industry Loan Applications

Purpose (RM billion)	May-16	Apr-16	May-15	M-o-M	Y-o-Y
Purchase of Securities	2,623	1,900	1,883	38%	39%
Transport Vehicle	6,441	6,745	6,483	-4%	-1%
Of Which is Passenger Car	6,209	6,362	6,177	-2%	1%
Residential Property	18,671	18,225	17,432	2%	7%
Non-Residential Property	7,117	6,348	7,731	12%	-8%
Other Fixed Assets	3,705	505	644	633%	475%
Personal Use	4,481	5,624	5,406	-20%	-17%
Credit Card	4,094	3,890	2,674	5%	53%
Consumer Durables	0	1	17	-93%	-100%
Construction	3,472	1,551	4,183	124%	-17%
Working Capital	19,066	14,873	17,494	28%	9%
Other Purpose	2,655	4,645	2,459	-43%	8%
Total	72,325	64,307	66,405	12.5%	8.9%

Source: BNM, M&A Securities



Source: BNM, M&A Securities

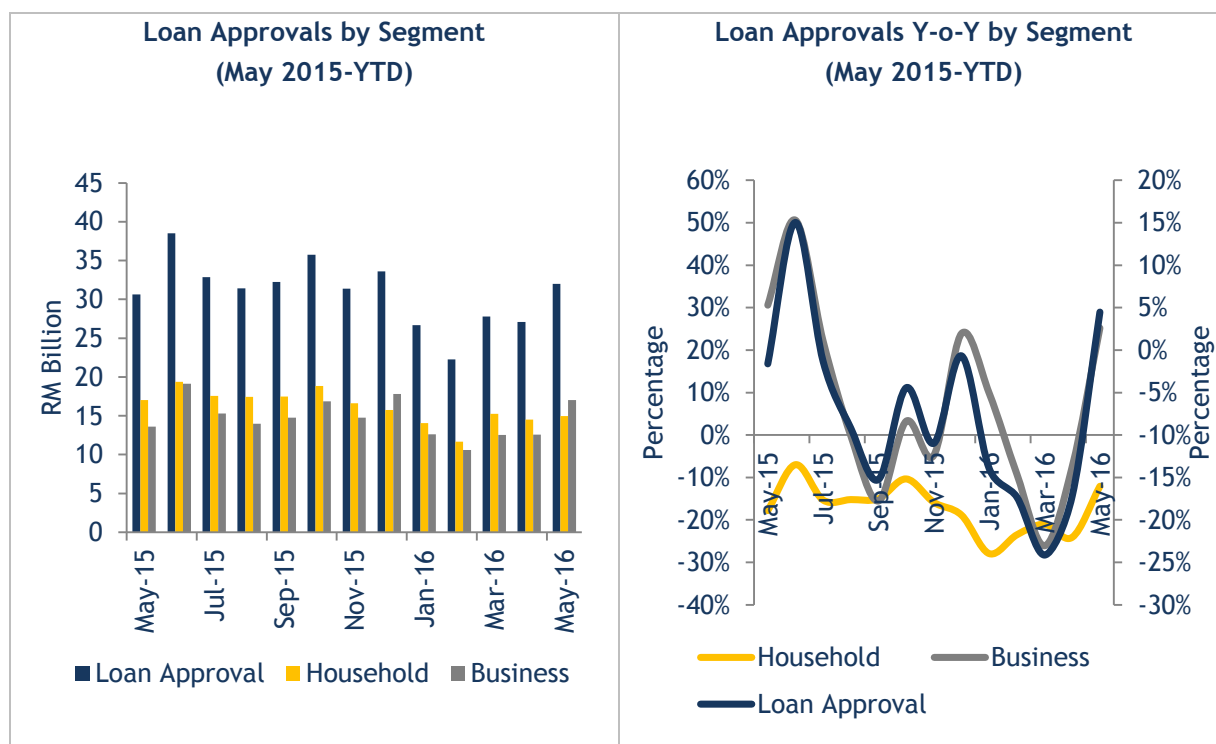
3. Loans Approval “stronger as well”

- Loans approval followed stronger application in May with a growth of 4.5% vs. -17.2% in April, supported by business segment performance.
- Business segment clocked-in stronger approvals of 25.2% y-o-y vs. -7.4% y-o-y in April as construction segment support overall growth of 154% y-o-y vs -55% y-o-y in April.
- In HH segment, there were no signs of recovery spotted in May with all key purposes were still unexciting and poised to drop further in coming months.
- Nevertheless, approvals rate continue to chart at higher level at 44% vs 42% given the rise in approvals. We deem that the approval rate could inch closer to 50% rate in 2016 as banks adjust with their customer credit profiling.

Table 6: Industry Loan Approvals

Purpose (RM billion)	May-16	Apr-16	May-15	M-o-M	Y-o-Y
Purchase of Securities	1,975	1,374	1,323	44%	49%
Transport Vehicle	3,432	3,483	3,860	-1%	-11%
Of Which is Passenger Car	3,145	3,084	3,657	2%	-14%
Residential Property	7,603	7,311	8,561	4%	-11%
Non-Residential Property	2,310	2,331	2,892	-1%	-20%
Other Fixed Assets	320	258	457	24%	-30%
Personal Use	1,382	1,351	1,382	2%	0%
Credit Card	1,487	1,407	1,355	6%	10%
Consumer Durables	0	0	7	1118%	-93%
Construction	2,362	1,052	931	124%	154%
Working Capital	9,309	7,110	8,324	31%	12%
Other Purpose	1,815	1,427	2,211	27%	-18%
Total	31,996	27,104	31,302	18.0%	2.2%

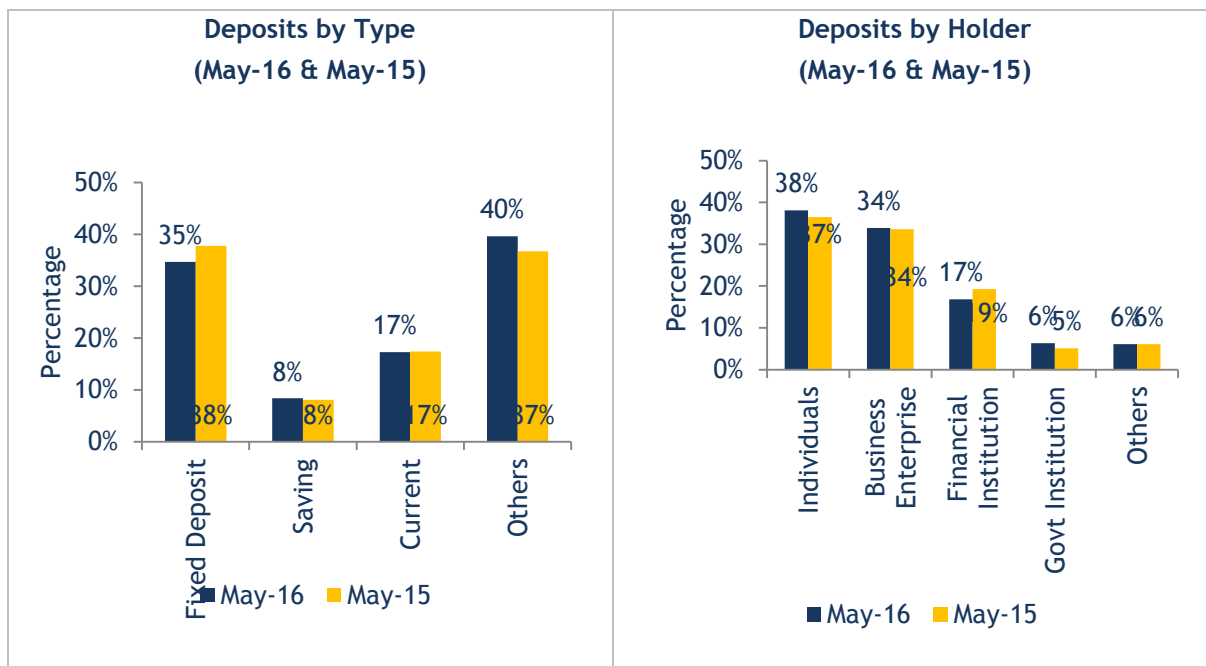
Source: BNM, M&A Securities



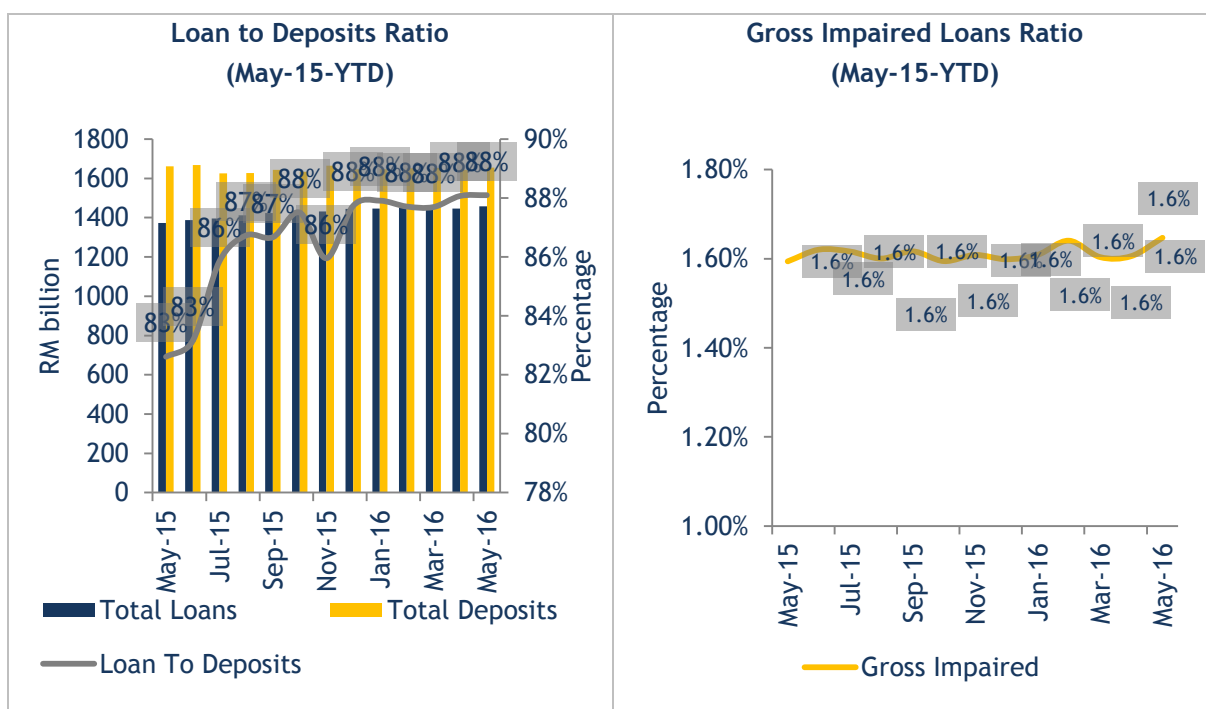
Source: BNM, M&A Securities

4. Deposits “continued negative for second months”

- Total deposits improved marginally from April, however it was still in negative territory. Total deposits eased marginally to 0.4% y-o-y vs. -1.2% in April
- The percentage of current account, savings account (CASA) and excess liquidity to total deposit base stood at 25.6% vs. 25.5% in April.
- The industry’s loan/deposit ratio (LDR) was unchanged at 88.1%, however the situation of tight liquidity still remained in the market.



Source: BNM, M&A Securities



Source: BNM, M&A Securities

5. Gross impaired (GIL) “erode marginally”

Gross impaired ratio fell marginally to 1.65% vs. 1.61% in April aided by GIL in HH segment. Given this, we believe banks will tighten its approval process and will be more selective in due time.

6. Capital remains strong

Overall, capital ratios were stable in May, including the industry’s CET1 ratio of 12.9%. Tier 1 fell 10 bps to 13.8% while total capital of 16.4%. Mostly banks saw their common equity tier 1 (CET1) ratio regressed. The drop is to increase their risk weighted asset from the previous quarter but overall the banks’ CET1 ratio is still comfortably above the Basel III regulatory requirements of 7%. Basel III is expected to be enforced by 2019 and we believe no further capital raising exercise is required by the banks.

Conclusion and Recommendations

2016 may see banks report flat earnings due to the slowdown in macro-economic conditions that will set to influence banks performance. Among banking sector challenges include 1) flat loans growth 2) tight liquidity 3) margin compression 4) rising credit cost and 5) challenging macroeconomic conditions which may continue to plague the banking industry. Banking sector is **NEUTRAL** in 2016 with 2 banks emerge as our **Top Pick** namely Public Bank (TP: RM21.38) and BIMB Holdings (TP: RM4.28).

Table 6: Loans Growth Y-o-Y

Company	Year Ended	Sept-14	Dec-14	Mar-15	Jun-15	Sept-15	Dec-15	Mar-16
AFG	March	14.9%	16.3%	14.7%	12.5%	10.2%	8.5%	4.9%
AMMB	March	0.9%	0.7%	-1.6%	-2.2%	0.1%	-0.7%	0.1%
CIMB	Dec	9.3%	12.8%	12.5%	16.1%	19.3%	12.5%	7.1%
Maybank	Dec	13.8%	13.3%	14.2%	15.6%	20.1%	12.3%	5.7%
PBK	June	10.2%	10.8%	11.7%	11.5%	12.9%	11.6%	9.5%
RHB Cap	Dec	12.0%	17.0%	13.7%	9.2%	11.4%	6.3%	4.3%

Source: Bursa Malaysia, M&A Securities

Sector Update: Banking May 2016 Statistics

Table 7: Peers Comparison

Company	YE	Price (RM)	EPS (RM)		P/E (x)		P/B (X)		ROE (%)	Div Yield (%)	TP (RM)	Call
			FY16	FY17	FY16	FY17	FY16	FY17				
AFG	Mac	4.06	0.3	0.4	11.7	11.2	1.3	1.3	10.8	2.0	4.00	Hold
AMMB	Mac	4.40	0.4	0.4	10.3	10.2	0.9	0.9	10.7	4.5	4.80	Hold
BIMB	Dec	4.01	0.4	0.4	10.3	9.8	1.7	1.5	17.2	3.3	4.28	Hold
CIMB	Dec	4.37	0.5	0.5	10.4	9.2	1.0	0.9	7.3	2.9	4.75	Hold
Maybank	Dec	8.27	0.7	0.7	12.9	12.3	1.4	1.3	11.9	6.4	9.10	Hold
RHB Bank	Dec	5.12	0.6	0.6	9.8	9.2	0.8	0.8	7.2	1.0	5.80	Hold
Public Bank	Dec	19.14	1.3	1.4	14.8	14.0	2.3	2.0	17.1	3.0	21.38	Buy
Affin	Dec	2.24	0.2	0.3	9.8	9.0	0.6	0.5	4.5	1.3	NR	NR
MBSB	Dec	1.14	0.1	0.1	11.0	11.2	0.8	0.8	5.4	7.5	NR	NR
STMB	Dec	3.86	0.2	0.2	20.1	17.8	5.0	NA	24.5	1.8	NR	NR
HL Bank	Jun	13.40	1.0	1.1	13.3	12.5	1.3	1.3	11.1	3.0	NR	NR
Average			0.6	0.7	12.8	11.4	1.5	1.1	11.1	3.9		

Source: Bloomberg, M&A Securities

M&A Securities

STOCK RECOMMENDATIONS

BUY	Share price is expected to be $\geq +10\%$ over the next 12 months.
TRADING BUY	Share price is expected to be $\geq +10\%$ within 3-months due to positive newsflow.
HOLD	Share price is expected to be between -10% and $+10\%$ over the next 12 months.
SELL	Share price is expected to be $\geq -10\%$ over the next 12 months.

SECTOR RECOMMENDATIONS

OVERWEIGHT	The sector is expected to outperform the FBM KLCI over the next 12 months.
NEUTRAL	The sector is expected to perform in line with the FBM KLCI over the next 12 months.
UNDERWEIGHT	The sector is expected to underperform the FBM KLCI over the next 12 months.

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