04 September 2018 | Corporate Update

Affin Bank Berhad

Clearly still in transition

Maintain BUY

***Revised* Target Price (TP): RM2.70 (from RM2.90)**

INVESTMENT HIGHLIGHTS

- **Recap, 1HFY18 earnings fell short of expectations due to higher than expected provisions**
- **Provisions due to individual account**
- **NII decline partly due to emphasis on Islamic Banking**
- **Robust loans growth**
- **Deposits growth from fixed deposits. Possibility of further NIM compression**
- **Transition year; Maintain BUY with revised TP of RM2.70 (from RM2.90)**

Key take away – potential earnings recovery in FY19? We met with the management yesterday for the post result briefing. Our key take away from this meeting are:

- Earnings 2QFY18 were affected by the higher provisions stemming from two individual accounts.
- The impaired accounts expected to be rectified by FY19.
- Income and loans growth driven by Islamic Banking side.
- Deposits growth from fixed deposits as competition intensifies in preparation of Net Stable Funding Ratio (NSFR) requirements.

Recall, result fell short of expectation due to provisions. The Group's 1HFY18 net profit was 36.5% and 42.6% of ours and consensus' full year estimates respectively. The variance was due to provisions coming in higher than expected.

Provisions were due to two individual accounts. We understand that the higher provisions were due to two individual accounts in the real estate development and, oil & gas sectors. We were comforted by the fact that it was not a broad base deterioration in asset quality. The loan in the real estate development were classified as impaired due to being R&R, while the oil & gas sector loan were impaired and part of a syndicated loan.

GIL ratio shot up due to these two accounts. GIL ratio was 2.81% as at 2QFY18 vs. 2.54% as at 1QFY18. However, the GIL ratio excluding the R&R accounts would have improved to 2.28% from 2.48% as at 1QFY18.

Resolution of the impaired accounts only next year. The management expects the resolution of the R&R real estate development loan to come in this year or 1QFY19 latest and the oil & gas sector loan in FY19. We opine that this could provide a boost to earnings in FY19 via write backs. For this year, the management is guiding a gross credit cost of 30 to 40bps.

RETURN STATS	
Price (3 September 2018)	RM2.41
Target Price	RM2.70
Expected Share Price Return	+12.0%
Expected Dividend Yield	+2.9%
Expected Total Return	**+14.9%**

STOCK INFO	
KLCI	1,813.58
Bursa / Bloomberg	5185 / ABANK MK
Board / Sector	Main / Finance
Syariah Compliant	No
Issued shares (mil)	1,942.9
Market cap. (RM'm)	4,682.5
Price over NA	0.6x
52-wk price Range	RM2.22–RM2.70
Beta against KLCI)	0.77
3-mth Avg Daily Vol	0.16m
3-mth Avg Daily Value	RM0.40m
Major Shareholders	
LTAT	35.45%
Bank of East Asia	23.52%
Boustead Holdings	20.69%

Some banking abbreviations used in this report:
IA = Individual Impairment Allowance
CA = Collective Impairment Allowance
CI = Cost-Income Ratio
CET1 = Common Equity Tier 1
GIL = Gross Impaired Loan
LD = Loan-Deposit
NII = Net Interest Income
NOII = Non-interest income
NIM = Net Interest margin
CASA = Current and Savings Accounts
IB = Investment Banking
BVPS = Book Value Per Share
LLC = Loan Loss Coverage
OPEX = Operating Expenses
R&R = Restructured and Rescheduled

Lower NII due to Islamic Banking. NII in 1HFY18 fell -13.7%yoy to RM426.3m when compared with Affin Holdings Bhd (AHB; note we compare the "new" with the previous iteration of the banking group). The decline was due to the Group promoting Islamic Banking. As such, Islamic Banking income grew +34.4%yoy to RM203.2m. We understand that the bulk of the loans growth was also from Islamic Banking.

Good growth from fee income but dragged by lower gains in financial instruments. Fee income expanded +13.8%yoy to RM235.3m in 1HFY18. However, overall NOII was dragged by lower gains in financial instruments, which fell -34.4%yoy to RM106.0m.

Focusing on consumer segment having the desired effect. Gross loans as at 2QFY18 grew +5.5%yoy to RM47.8b, mainly driven by household segment. Loans for this segment expanded +11.6%yoy to RM21.5b. This was supported by mortgages which rose +25.0%yoy to RM9.5b. We believe that this is evident that the Group's shift towards increasing the contribution from consumer segment is having the desired effect. The management expects the ratio between consumer to non-consumer loan book to come in to 55:45. As at 2QFY18, it was almost 50:50.

Deposits growth fuelled by fixed deposits. Our only concern is that deposits growth came mostly from fixed deposits (FD). Total deposits from customers expanded to RM52.8b from RM50.9b as at 4QFY17. Meanwhile, FD grew from RM34.3b to RM36.7b (or +7.1%) over the same period. We believe that this will impact NIM in 2HFY18 which would put further pressure on NII. The management have been trying to emphasize CASA growth but we have yet to see the result. This is further difficult given the intensifying deposit competition ahead of NSFR implementation in CY19. We expect that NII will continue to contract but we believe that this will be moderated by the focus to grow SME loans which have higher yields.

FORECAST

We are revising downwards our FY18 and FY19 earnings forecasts by -22.9% and -19.9% to reflect the higher provisions and potential NIM compression.

VALUATION AND RECOMMENDATION

Still in a transition year but expect recovery next year. While we saw earnings for 2QFY18 were a surprisingly weak, we believe that this was due to FY18 being a transition year. However, we believe that there will be a recovery in earnings in FY19 as the Group resolves its asset quality issue. Hence, we are maintaining our BUY call for the stock for now. We are revising our TP to RM2.70 (from RM2.90) as we revised its BVPS following the earnings forecast revision. Our TP is based on pegging FY19 BVPS to PBV of 0.6x.

INVESTMENT STATISTICS

FYE Dec	FY16*	FY17	FY18F	FY19F
Net Interest income (RM'm)	971	855	852	821
Islamic Banking income (RM'm)	273	334	435	521
Other income (RM'm)	693	371	627	611
Net/Total income (RM'm)	1,936	1,560	1,914	1,953
Pretax Profit (RM'm)	738	551	591	724
Net Profit (RM'm)	564	418	454	559
EPS (sen)	29	24	23	29
EPS Growth (%)	52.6	-17.2	-2.7	23.1
PER (x)	8.3	10.0	10.3	8.4
Net Dividend (sen)	11	2.3	7	10
Net dividend yield (%)	4.6	1.0	2.9	4.1
Book value per share (RM)	4.47	4.26	4.46	4.62
PBV (x)	0.5	0.6	0.5	0.5
ROE (%)	6.5	5.1	5.2	6.2

* Based on Affin Holdings Bhd as the financial holding co. of the Group.

Source: Company, MIDFR

DAILY PRICE CHART

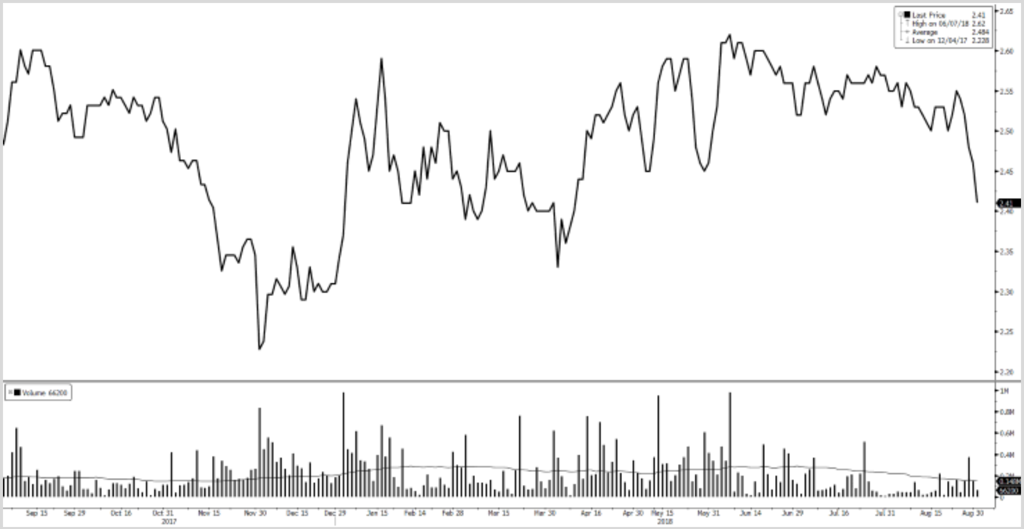

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Table 1: Recap of cumulative results

	Cumulative results				
FYE Dec (RM m)	**ABB Group 1HFY18**	**ABB Group 1HFY17**	**AHB Group 1HFY17**	**Comparison between ABB**	**Comparison between ABB & AHB**
				Yoy (+/- %)	**Yoy (+/- %)**
Net Interest Income	426.3	421.4	494.3	1.2%	-13.7%
Islamic Banking Income	203.2	151.2	151.2	34.4%	34.4%
Non interest income	341.3	125.2	368.3	>100%	-7.3%
Net/Total income	970.8	697.8	1,013.8	39.1%	-4.2%
OPEX	(617.5)	(383.6)	(596.2)	61.0%	3.6%
PPOP	353.3	314.2	417.6	12.5%	-15.4%
Write back/(Provision) for loan losses	(82.6)	(42.4)	(42.3)	94.8%	95.0%
Pre-tax profit	300.7	271.8	360.6	10.6%	-16.6%
Net Profit	(75.7)	(63.4)	(83.2)	19.4%	-9.0%
EPS (sen)	214.8	208.4	268.6	3.0%	-20.0%

Source: Company, MIDFR

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MIDF AMANAH INVESTMENT BANK : GUIDE TO ROMMENDATIONS	
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	*Negative* total return is expected, by -10% or more, 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.