

07 September 2017 | Briefing Note

Affin Holdings Berhad

Viewing it in the continuum

INVESTMENT HIGHLIGHTS

- **Management held a briefing yesterday and we believe that the Group is moving in the right direction.**
- **Transformation program has shown to have positive impact in performance.**
- **For example, NIM was stable despite higher funding cost. This was due to ability to better price loans.**
- **Loans mix is getting better.**
- **No real deterioration in asset quality.**
- **No change to forecast.**
- **Reiterate BUY with unchanged TP of RM3.30 PBV of 0.7x.**

Moving in the right direction. We attended the briefing held by management yesterday for an update on the Group. Overall, we believe that the Group' transformation, although on-going, have shown to be bearing fruit and we continue to be optimistic of the sustainability of its earnings growth. Key take away from the briefing are as follows:

- Transformation is continues and in the midst of phase 3.
- Income accretion from transformation program.
- Stable NIM despite higher cost of funding.
- Higher impairments due to restructuring and rescheduling (R&R) of accounts.
- Clear benefit from structure reorganization.

Phase 3 of transformation but are showing results. The management highlighted that its Affinity transformation program have moved to stage 3 which is capabilities building and implementation. As at August 2017, it had completed 12 of the 25 projects initiated. This includes enhancing its IT capabilities, introduction of 7 new organizations which include customer experience, SME & Commercial, data governance and Islamic client solution. A commendable product of the transformation program has led to a shift in mind-set, from focusing on asset building previously to income generation. This also entails looking at source of funding and methodology in pricing of loans. Indeed, we believe that we have seen the product of its transformation program having an impact in its performance in the past quarters.

Reiterate BUY

Unchanged Target Price (TP): RM3.30

RETURN STATS	
Price (6 Sept. 2017)	RM2.56
Target Price	RM3.30
Expected Share Price Return	+28.9%
Expected Dividend Yield	+4.7%
Expected Total Return	+33.6%

STOCK INFO	
KLCI	1,772.48
Bursa / Bloomberg	5185 / AHB MK
Board / Sector	Main / Finance
Syariah Compliant	No
Issued shares (mil)	1,942.9
Market cap. (RM'm)	4,973.9
Price over NA	0.5x
52-wk price Range	RM2.08–RM3.00
Beta against KLCI)	0.86
3-mth Avg Daily Vol	0.24m
3-mth Avg Daily Value	RM0.48m
Major Shareholders	
LTAT	35.42%
Bank of East Asia	23.52%
Boustead Holdings	20.69%

Some banking abbreviations used in this report:

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

Strong operating profit for 1HFY17. Recall, we saw strong PPOP growth of +21.5%yoy to RM417.6m attributable to growth in all of its income segment; NII (+3.6%yoy to RM494.3m), NOII (+49.6%yoy to RM452.4m) and Islamic Banking income (+21.7%yoy to RM151.2m). We were pleasantly surprised to see that NIM improved +6bps yoy to 1.98% despite higher growth in fixed deposits (+22.9%yoy to RM34.4b) as compared to total deposits (+4.2%yoy to RM57.7b) as at 2QFY17. In fact, cost of funds increased +42bps yoy to 3.39% as a result of deposits competition.

Better loans pricing compensated higher cost of fund. The improved NIM was due to better pricing of loans. This stemmed from exiting unprofitable or low margin loans and, policy of implementing hurdle rate in pricing and acceptance of new loans. Hence, we did not see any margin significant margin compression. We like the fact that this was the direct result of its transformation program. The management expects that the transformation will also later lead to lower funding cost as it build its capabilities to secure better priced deposits. Based on current track record, we opine that this expectation can be achieved.

Loans mix getting better. The Group had also began to better its loans mix as part of its transformation programme. The gross loans as at 2QFY17 grew +2.5% year-to-date to RM45.3b or +4.6%yoy when compared with 2QFY16. More importantly, the loans mix were better whereby the loans composition as at 2QFY17 for SMEs and consumer were 7.8% and 47.9% vs. 7.6% and 46.5% as at 4QFY16, respectively. When compared against FY15, SME loans only made up of 0.9% of total gross loans. This leap in contribution was due to having a specialised SME team. Management expect loans to grow faster in 2HFY17 coming from SMEs and corporate segment. We believe that this will lead to better interest income and will not be surprised if NIM improved slightly or at least maintained at current level.

Increased loans impairment due to R&R of accounts but will get better towards end of FY17. The only weakness in the Group 1HFY17 performance was the rise in credit cost and impairments. Net credit cost was +9.0bps yoy higher while GIL ratio went up +9bps yoy to 2.07%. We understand that this was due to R&R of several accounts with majority in the property sector. R&R loans came in at RM296.2m as at 1HFY17 from RM37.0m as at end FY16. However, management expect these accounts to return to performing given that the loans were restructured to realign the borrowers' cash flow with its financing commitments. Since the loans were restructured during 1HFY17, it is possible for the loans to be reclassified in the next 6 month. As such, we could expect for loans impairments and credit cost to trend lower in 2HFY17. Additionally, 100% of the loans are secured, while management do not foresee a real trend of asset quality deterioration.

Reorganization will bring significant benefit. Management expect that the reorganization of its group structure where Affin Bank Berhad will take over the listing status of Affin Holdings Bhd, to be completed by 1QFY18. Amongst the benefits are the reduction in cost and better capital adequacy. We also believe that shareholders will gain via participating at the bank level, benefitting directly from the result of the transformation program.

Viewing it long term but short term benefit has manifest. We echo the management's view that the Group's prospect should be considered as a long term project as it has yet to fully complete its transformation. However, we believe that the benefits are already showing in the short term. We continue to be encouraged by the Group's future outlook. We believe that the transformation program continues to have an impact in the short term.

FORECAST

We make no change to our FY17 and FY18 forecast.

VALUATION AND RECOMMENDATION

Observing the improvements that the Group have made in the previous few quarters have led us to conclude that the Group is moving in the right direction. We opine that the transformation will leave the Group on a better footing. We also maintain our view that the Group is building its niche and believe that this will ensure future profitability. Taking everything into consideration, we are reiterating our BUY call for the stock, with an unchanged TP of RM3.30 based on pegging our FY18 BVPS forecast to PBV of 0.7x.

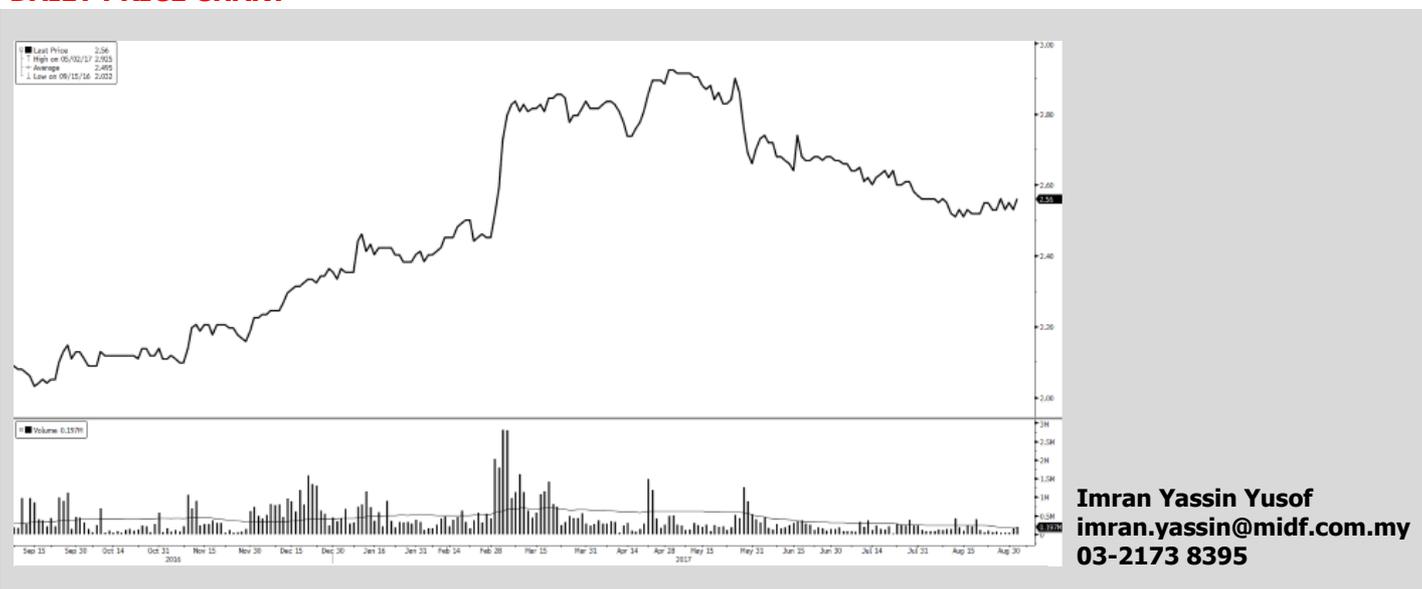


INVESTMENT STATISTICS

FYE Dec	FY15	FY16	FY17F	FY18F
Net Interest income (RM'm)	948	971	1,051	1,143
Islamic Banking income (RM'm)	239	273	299	302
Other income (RM'm)	616	693	703	723
Net/Total income (RM'm)	1,803	1,936	2,054	2,168
Pretax Profit (RM'm)	519	738	794	849
Net Profit (RM'm)	369	564	585	626
EPS (sen)	19	29	30	32
EPS Growth (%)	-0.46	52.6	3.8	6.9
PER (x)	13.5	8.8	8.5	8.0
Net Dividend (sen)	8	11	12	13
Net dividend yield (%)	3.1	4.3	4.7	5.1
Book value per share (sen)	4.26	4.47	4.70	4.90
PBV (x)	0.6	0.6	0.5	0.5
ROE (%)	4.6	5.9	6.4	6.6

Source: Company, MIDFR

DAILY PRICE CHART



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MIDF AMANAH INVESTMENT BANK : GUIDE TO ROMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	<i>Negative</i> total return is expected, by -15% or more, over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >15% 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.