

29 November 2018 | 1QFY19 Results Review

Hong Leong Bank Berhad

Boosted by gains in NOII

Maintain NEUTRAL

Adjusted Target Price (TP): RM20.30
(from RM18.85)

INVESTMENT HIGHLIGHTS

- Earnings in line
- Strong NOII growth
- NIM compression continued in 1QFY19
- Mortgage supported loans growth
- No revision to FY19 forecasts
- Maintain NEUTRAL with adjusted TP of RM20.30 (from RM18.85) as we roll over our valuation to FY20

Earnings within expectations. Hong Leong Bank Berhad (HLB) posted 1QFY19 earnings that were in line with ours and consensus' expectations. It came in at 25.4% and 25.5% of respective full year estimates. The robust +10.6%yoy earnings growth was supported by strong NOII expansion.

Strong NOII expansion due to divestment gains. NOII grew +35.4%yoy due to RM72m gains on divestment of joint venture, Sichuan Jincheng Consumer Finance Ltd. Co. Post completion of the divestment exercise, HLB retained interest of 12% and recognized the company as an associate. However, we understand that this divestment gain was one-off. Nevertheless, discounting this gain, NOII would still have a solid growth of +10.9%yoy to RM325m. This was supported by +9%yoy to RM52m growth in forex franchise.

Margin compression continued to affect NII. NII fell -3.8%yoy as NIM compression continued in 1QFY19. NIM fell -5bps qoq and -15bps yoy on the twin effect of deposit competition and deposit repricing following OPR earlier this year. However, management expect NIM to recover slightly as it had seen the price of ringgit denominated deposits stabilising, with pressure coming from USD denominated deposits.

Decent loans growth... Gross loans grew +4.0%yoy to RM129.8b. We believe that this had moderated the impact of NIM compression as NII rose +0.8%qoq. The gross loans growth was led by the +8.0%yoy to RM62.6b in residential mortgages. Meanwhile, business enterprise loans grew +3.5%yoy to RM36.3b. While HLB's gross loans expanded lower than system loans growth, management expect that there will be a pick up later in FY19. We understand that businesses are currently cautious in drawing down approved loans.

...matched by deposits growth. Deposits expanded +4.0%yoy to RM158.8b. Bulk of the growth came from fixed deposits which grew +4.8%yoy to RM89.3b. Meanwhile, CASA shrank -3.2%yoy to RM39.7b. This could be the impact from the deposit competition.

RETURN STATS	
Price (28 Nov. 2018)	RM20.68
Target Price	RM20.30
Expected Share Price Return	-1.8%
Expected Dividend Yield	+2.3%
Expected Total Return	+0.5%

STOCK INFO	
KLCI	1,686.55
Bursa / Bloomberg	5819 / HLBK MK
Board / Sector	Main / Finance
Syariah Compliant	No
Issued shares (mil)	2,045.6
Market cap. (RM'm)	42,303.0
Price over NA	1.8x
52-wk price Range	RM15.14 - RM21.26
Beta (against KLCI)	0.86
3-mth Avg Daily Vol	1.27m
3-mth Avg Daily Value	RM25.93m
Major Shareholders	
Hong Leong Financial Group	65.51%
EPF	12.56%

Some banking abbreviations used in this report:

CI = Cost-Income Ratio
 CET1 = Common Equity Tier 1
 GIL = Gross Impaired Loan
 LDR = Loan-Deposit Ratio
 NII = Net Interest Income
 NOII = Non-interest income
 NIM = Net Interest margin
 CASA = Current and Savings Accounts
 COF = Cost of Funds
 PPOP = Pre-provisioning Operating Profit
 LLC = Loan Loss Coverage
 JV = Joint Venture with BOC in a Consumer Finance Company in China
 BOC = Bank of Chengdu

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Asset quality remains solid. GIL ratio improved -17bps yoy and -6bps qoq to 0.81%. The management does not expect pressure from any particular segment.

Most of FY19 targets on track. Recall, the management guided the following; (1) gross loans growth to be in line with industry, (2) LDR of circa 82%, (3) NIM of above 2%, (4) NOII ratio of above 27%, (5) CI of below 43%, (6) GIL of below 1% and (7) ROE of circa 11%. At the moment, HLB missed its gross loans and NIM target. However, it is still early days. We do not foresee any difficulties in the management achieving these targets except for NIM which we believe could still face some pressure.

FORECAST

We maintaining our FY19 and FY20 forecast.

VALUATION AND RECOMMENDATION

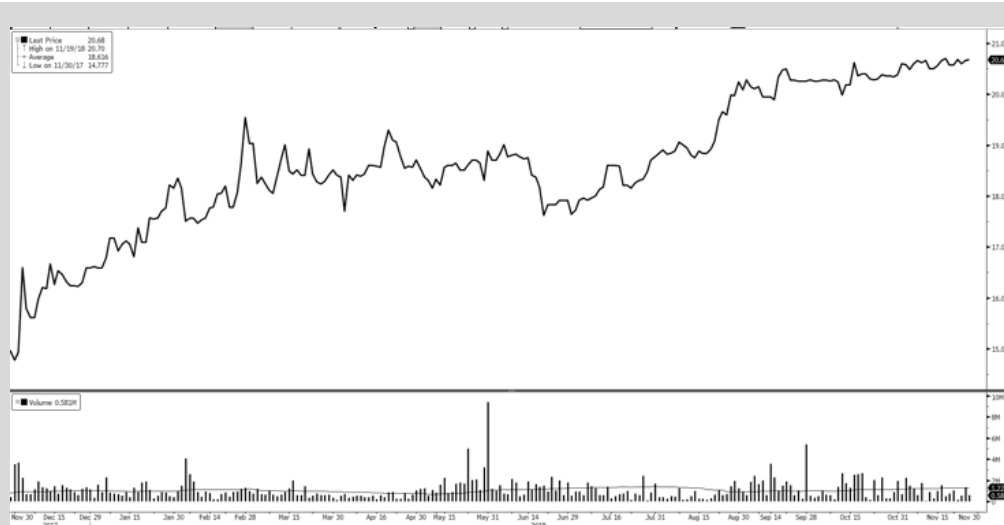
HLB had a strong start to its financial year. However, we opine that this was largely contributed by the divestment gain, and this was one-off in nature. Going forward, we believe that pressure of a NIM compression, and thus NII, will remain prevalent albeit not at a detrimental level. In addition, we expect its NOII growth will be able to moderate any impact from weakness in NII. As such, we maintain our NEUTRAL call for the stock with an adjusted TP of RM20.30 (from RM18.85) as we roll over our valuation to FY20. Our TP is based on pegging its FY20 BVPS to PBV of 1.5x which is its 5-year historical average PBV. 

INVESTMENT STATISTICS

FYE June	FY17	FY18	FY19F	FY20F
Net interest income (RM'm)	2,854	2,893	3,211	3,430
Islamic banking income (RM'm)	550	646	673	741
Non-interest income (RM'm)	1,146	1,300	1,274	1,330
Total income (RM'm)	4,551	4,840	5,158	5,501
Pretax profit (RM'm)	2,748	3,246	3,517	3,695
Net profit (RM'm)	2,145	2,638	2,778	2,927
Core net profit (RM'm)	2,247	2,638	2,778	2,927
Core EPS (sen)	109.9	128.7	135.8	143.1
PER (x)	18.8	16.1	15.2	14.5
Net dividend (sen)	45	48	49	50
Net dividend yield (%)	2.2	2.3	2.4	2.4
Book value per share (RM)	11.09	11.68	12.52	13.42
PBV (x)	1.9	1.8	1.7	1.5
ROE (%)	9.8	11.3	11.2	11.0

Forecast by MIDFR

DAILY PRICE CHART



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Table 1: Quaterly results

Quarterly results						Comments
FYE June (RM m)	1Q19	4Q18	1Q18	Yoy (+/- %)	Qoq (+/- %)	
Net Interest Income	852	846	886	-3.8%	0.8%	NIM compression of -15bps yoy. Nevertheless, improved quarter-on-quarter basis due to stable loans growth
Non-interest Income	397	331	293	35.4%	20.0%	Gains of RM72m on divestment of joint venture
Net/Total income	1,249	1,176	1,179	6.0%	6.2%	
OPEX	(525)	(511)	(507)	3.6%	3.0%	Higher personnel expenses
PPOP	724	665	671	7.9%	8.8%	
Write back/(Provision) for loan losses	(20)	(5)	(43)	-54.9%	>100%	
Share of profit from associate and JV	147	117	152	-3.6%	25.2%	
Pre-tax profit	851	778	780	9.1%	9.5%	
Net Profit	707	626	639	10.6%	12.9%	
EPS (sen)	34.4	30.6	31.2	10.3%	12.4%	

Table 2: Quaterly financial ratios based on normalised financials

Financial Ratios (%)	1Q19	4Q18	1Q18	Yoy (+/- ppts)	Qoq (+/- ppts)	Comments
CET1*	12.4	12.6	12.9	-0.5	-0.2	
Tier 1 Capital*	13.1	13.3	13.3	-0.2	-0.2	
Total Capital*	16.1	16.3	15.3	0.8	-0.2	
NIM	1.98	2.03	2.13	-0.15	-0.05	Due to repricing of deposits and deposit competition
GIL	0.81	0.87	0.98	-0.17	-0.06	Vs. industry: 1.51%
Loan loss Coverage	128	89	96	32	39	Vs. industry: 97%
Credit charge-off	0.06	0.03	0.14	-0.08	0.03	
Cost to income	42.0	43.5	43.0	-1.0	-1.4	
Net LD	81.7	82.0	81	0.7	-0.3	Vs. industry: 90.5%
ROEA	11.7	10.6	11.1	0.6	1.1	

*Group ratios after deducting proposed dividend

Table 3: Comparison of pretax profits by business segments (RM'Mil) based on reported numbers

Business segments	1QFY19	1QFY18	Change (%)	Comments
Personal Financial Services	266.8	282.8	-5.6%	Attributable to lower income and higher OPEX
Business and Corporate Banking	209.9	200.1	4.9%	Higher income and lower allowance for impairment losses on loans, advances and financing
Global Markets	102.7	106.2	-3.3%	Higher income, higher OPEX and impairment losses on bonds & interbank assets with MFRS9 implementation
International Banking	3.2	15.6	-79.4%	Contributed by lower total income, higher OPEX, higher allowance for impairment losses on loans, advances and financing and lower share of profit from associated company in China
Others and Inter-Segment Elimination	121.6	23.4	>100%	
Total segment profit before tax	704.3	628.1	12.1%	

Source: Company

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> 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	<i>Negative</i> total return is expected, by -10% or more, over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> 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.