

29 August 2018 | 4QFY18 Results Review

Hong Leong Bank Berhad

Solid PPOP growth

INVESTMENT HIGHLIGHTS

- **Net profit within expectations.**
- **Earnings growth led by income growth.**
- **Margin compression in 4QFY18.**
- **Loans growth was decent supported by mortgages.**
- **Deposits growth disappointing but good CASA momentum.**
- **Dividend of 32 sen bringing full year dividend to 48 sen.**
- **No revision to FY19 forecasts.**
- **Maintain NEUTRAL with unchanged TP of RM18.85, pegging its FY19 BVPS to 1.5x, which is its 5-year historical average.**

Net profit within expectations. Hong Leong Bank Berhad (HLB) posted FY18 net profit growth that was within ours and consensus' expectations coming in at 101.4% and 102.2% of respective estimates. The strong growth of +23.0%yoy was due to solid income growth and absence of tax impact which affected FY17 that amounted to RM102m. Excluding this tax impact, earnings grew +17.4%yoy.

Income led by NOII and Islamic Banking. NOII grew +12.4%yoy supported by growth in trading & investment income of +46.0%yoy to RM623m. This included gains from sale of Visa shares, which we believe was one-off. For NII, it was led by Islamic Banking which expanded +17.4%yoy to RM646.0m. Meanwhile, conventional NII grew +1.4%yoy to RM2.89b due to contraction in 4QFY18 of -5.3%yoy to RM690.4m.

Margin compression in 4QFY18. The fall in NII in 4QFY18 was the result of margin compression. NIM fell by -7bps qoq and -11bps yoy to 2.03% due to deposits re-priced higher following OPR hike earlier this year. However, FY18 NIM improved +1bps yoy to 2.1%. The management expects NIM to remain above 2% in FY19.

Lowest CI in 6 years. HLB seems to be reaping the benefit of its digitization program as CI came in at 42.6%, the lowest in the past 6 years. OPEX grew by +2.6%yoy with the major contributor being IT investments which grew +11.2%yoy to RM164.3m. Of this, digitization related cost amounted to RM97m. Personnel cost fell marginally by -0.5%yoy to RM1.11b on lower headcount.

Loans growth within target. Gross loans grew +3.1%yoy to RM129.1b. The main driver was residential properties loans which grew +7.9%yoy to RM61.4b. SME loans was almost flat at +0.5%yoy to RM20.5b but we understand that Group SME segment saw good traction. The gross loans growth was moderated by decline in auto loans and unsecured loans which fell -8.8%yoy to RM16.9b and -4.0%yoy to RM5.6b respectively.

Maintain NEUTRAL
Unchanged Target Price (TP): RM18.85

RETURN STATS	
Price (28 August 2018)	RM20.30
Target Price	RM18.85
Expected Share Price Return	-7.1%
Expected Dividend Yield	+2.4%
Expected Total Return	-4.8%

STOCK INFO	
KLCI	1,826.90
Bursa / Bloomberg	5819 / HLBK MK
Board / Sector	Main / Finance
Syariah Compliant	No
Issued shares (mil)	2,045.6
Market cap. (RM'm)	41,525.7
Price over NA	1.7x
52-wk price Range	RM14.90 - RM20.30
Beta (against KLCI)	0.89
3-mth Avg Daily Vol	1.10m
3-mth Avg Daily Value	RM20.72m
Major Shareholders	
Hong Leong Financial Group	65.66%
EPF	12.85%

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

Disappointing deposits growth but good CASA momentum. Total deposits grew +1.4%yoy to RM157.4b as business enterprise segment fell -0.9%yoy to RM62.7b. However, it was lifted by good CASA momentum. CASA grew +6.3%yoy to RM41.2b. Meanwhile, fixed deposits were flat at +0.3%yoy to RM88.2b. This partly explains the improved NIM in FY18.


Dividend within expectations. HLB announced a final dividend of 32 sen. This brings the full year dividend to 48 sen which is within our expectations.

FY19 targets achievable. 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%. We do not foresee any difficulties in the management achieving these targets except for NIM which we believe could face some pressure.

FORECAST

We maintaining our FY19 forecast.

VALUATION AND RECOMMENDATION

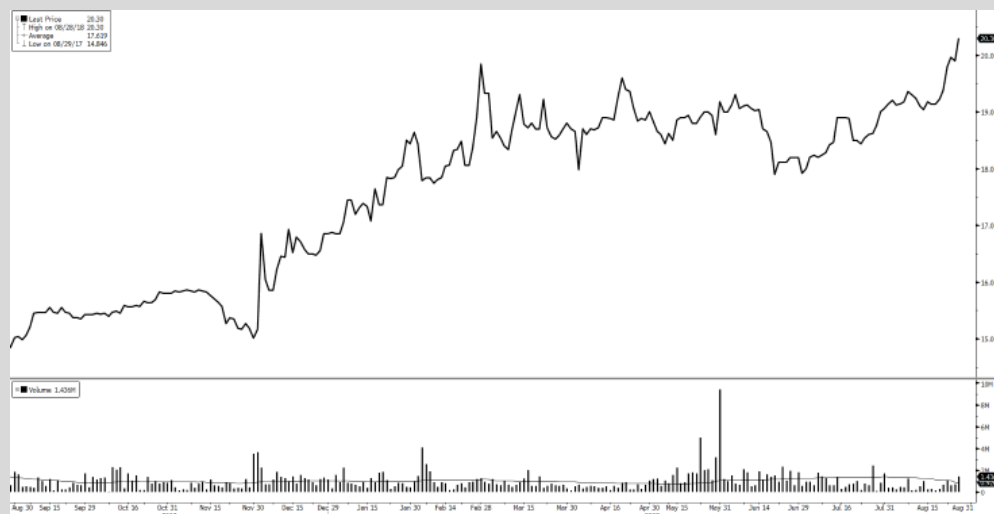
HLB ended the year strongly with strong income growth and well contained OPEX. However, we opine that there could be some pressure in NII going forward judging by the decline in conventional NII in 4QFY18 coupled by the drop in NIM. In addition, we believe the strong results were tempered by the disappointing growth in terms of loans and deposits. However, we believe that earnings momentum will continue in FY19. Nevertheless, we believe that this have been priced in. As such, we maintain our NEUTRAL call for the stock with unchanged TP of RM18.85. Our TP is based on pegging its FY19 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	3,216	3,435
Islamic banking income (RM'm)	550	646	673	741
Non-interest income (RM'm)	1,146	1,300	1,273	1,332
Total income (RM'm)	4,551	4,840	5,163	5,507
Pretax profit (RM'm)	2,748	3,246	3,514	3,699
Net profit (RM'm)	2,145	2,638	2,776	2,922
Core net profit (RM'm)	2,247	2,638	2,776	2,922
Core EPS (sen)	109.9	128.7	135.8	143.0
PER (x)	18.5	15.8	15.0	14.2
Net dividend (sen)	45	48	49	50
Net dividend yield (%)	2.2	2.4	2.4	2.5
Book value per share (RM)	11.09	11.68	12.58	13.43
PBV (x)	1.8	1.7	1.6	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)	4Q18	3Q18	4Q17	Yoy (+/- %)	Qoq (+/- %)	
Net Interest Income	846	867	864	-2.1%	-2.5%	NIM compression of -11bps yoy.
Non-interest Income	331	389	288	14.8%	-15.0%	
Net/Total income	1,176	1,256	1,152	2.1%	-6.3%	
OPEX	(511)	(527)	(516)	-0.9%	-3.0%	Lower headcount.
PPOP	665	729	636	4.5%	-8.8%	
Write back/(Provision) for loan losses	(5)	(11)	(60)	-91.7%	-53.1%	Write back in IA.
Share of profit from associate and JV	117	137	105	11.4%	-14.2%	
Pre-tax profit	778	855	680	14.4%	-9.1%	
Net Profit	626	690	483	29.6%	-9.3%	Normalised growth (excluding one-off tax impact in 4QFY17) was +7.1%yoy.
EPS (sen)	30.6	33.7	23.6	29.7%	-9.2%	

Table 2: Quaterly financial ratios based on normalised financials

Financial Ratios (%)	4Q18	3Q18	4Q17	Yoy (+/- ppts)	Qoq (+/- ppts)	Comments
CET1*	12.6	12.0	13.3	-0.7	0.6	
Tier 1 Capital*	13.3	12.7	13.7	-0.4	0.6	
Total Capital*	16.3	15.3	15.8	0.5	1.0	
NIM	2.03	2.10	2.14	-0.11	-0.07	Due to repricing of deposits
GIL	0.87	0.84	0.96	-0.09	0.03	Vs. industry: 1.58%
Loan loss Coverage	89	96	96	-7	-7	Vs. industry: 95%
Credit charge-off	0.03	0.04	0.21	-0.18	-0.01	
Cost to income	43.5	42.0	44.8	-1.3	1.5	
Net LD	82.0	81.3	80.6	1.4	0.7	Vs. industry: 91.3%
ROEA	10.6	11.9	10.4	0.2	-1.3	

*Group ratios after deducting proposed dividend

Table 3: Normalised cumulative results and ratios

Cumulative results & ratios				Comments
FYE June (RM m)	FY18	FY17	Yoy	
NII	3,495	3,355	4.2%	Contributed by strong Islamic banking income and NIM improvement.
NOII	1,344	1,196	12.4%	Due to higher trading and investment income.
Net/Total Income	4,840	4,551	6.4%	
OPEX	(2,060)	(2,008)	2.6%	Higher IT expenses for digitization but moderated by lower personnel cost stemming from lower headcount.
PPOP	2,779	2,543	9.3%	
Writeback/ (Provision) for loan losses	(70)	(159)	-56.0%	Due to lower IA.
Share of profit from associate and JV	537	364	47.5%	Strong showing from BOC.
Pre-tax profit	3,246	2,748	18.1%	
Net Profit	2,638	2,145	23.0%	
EPS (sen)	128.7	104.8	22.8%	
	FY18	FY17	(+/-ppts)	
ROE (%)	11.3	10.3	1.0	
CI ratio (%)	42.6	44.1	-1.5	
Credit charge-off	0.06	0.13	-0.07	
NIM	2.10	2.09	0.01	

Table 4: Comparison of pretax profits by business segments (RM'Mil) based on reported numbers

Business segments	FY18	FY17	Change (%)	Comments
Personal Financial Services	1,118.6	1,119.9	-0.1%	Higher OPEX offset by higher income and lower provisions.
Business and Corporate Banking	830.8	718.4	15.6%	Higher income and lower provisions.
Global Markets	468.2	405.9	15.3%	Higher income and lower OPEX.
International Banking	53.1	36.2	46.5%	Higher share of profit from BOC and lower provisions.
Others and Inter-Segment Elimination	239.0	103.8	>100%	
Total segment profit before tax	2,709.6	2,384.2	13.6%	

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.