

29 November 2018 | 1QFY19 Results Review

Hong Leong Financial Group

Good start to the financial year

INVESTMENT HIGHLIGHTS

- Earnings met expectations
- Strong growth from Hong Leong Bank Bhd
- Insurance division and Hong Leong Capital expanded more robustly
- Interim dividend of 13 sen
- No change to forecast
- Maintain NEUTRAL on HLFG with an adjusted TP of RM20.10 (from RM19.00) based on SOTP valuation

Meeting expectations. HLFG 1QFY19 net profit was within our and consensus' expectations coming in at 23.6% and 24.9% of respective full year estimates. All of its business segment contributed to the earnings growth of +11.1%yoy.

HLB earnings boosted by NOII growth. Strong NOII growth was the main contributor to Hong Leong Bank's (HLB) earnings growth. Its NOII grew +35.4%yoy due to RM72m gains on divestment of joint venture, Sichuan Jincheng Consumer Finance Ltd. Co. While, we understand that this divestment gain was one-off, discounting the gains NOII still grew at solid pace of +10.9%yoy to RM325m. This was supported by +9%yoy to RM52m growth in forex franchise.

Meanwhile, net interest income was weakened due to compression in net interest margin (NIM). This was due to the twin effect of deposit competition and deposit repricing following OPR earlier this year. However, management of HLB expect NIM to recover slightly as it had seen the price of ringgit denominated deposits stabilising, with pressure coming from USD denominated deposits.

On the cost side, HLB's operating expenses was well contained as it grew +3.6%yoy due to higher personnel cost. Cost to income ratio improved to 42% as revenue outpaced expense growth.

Gross loans grew +4.0%yoy to RM129.8b which was led by the +8.0%yoy to RM62.6b in residential mortgages. Deposits expanded +4.0%yoy to RM158.8b. Bulk of the growth came from fixed deposits which grew +4.8%yoy to RM89.3b. However, CASA shrank -3.2%yoy to RM39.7b. This could be the impact from the deposit competition.

Maintain NEUTRAL
Adjusted Target Price (TP): 20.10
(from RM19.00)

RETURN STATS	
Price (28 Nov. 2018)	RM19.20
Target Price	RM20.10
Expected Share Price Return	+4.7%
Expected Dividend Yield	+2.1%
Expected Total Return	+6.8%

STOCK INFO	
KLCI	1,686.55
Bursa / Bloomberg	1082 / HLFG MK
Board / Sector	Main/ Finance
Syariah Compliant	No
Issued shares (mil)	1,145.2m
Market cap (RM'm)	21,988.7
Price over NA	1.2x
52-wk price Range	RM15.40 – RM20.40
Beta (against KLCI)	1.12
3-mth Avg Daily Vol	0.38m
3-mth Avg Daily Value	RM7.31m
Major Shareholders	
Hong Leong Co Malaysia	77.63%
EPF	1.96%
ING Groep NV	1.83%

Insurance division had a strong result. Insurance division (HLAH) had a strong quarter mainly due to Hong Leong Assurance's (HLA) PBT growing +35.5%yoy to RM82.1m. This was supported by significant progress in growing its Non participating and Investment Link new business premiums. Cost remains efficient as HLA's management expense ratio was 6.4%. We understand that the focus for the insurance segment remains on growing and improving the quality of its premium base and growth across multiple distribution channels.

Investment Banking business recovered. The Investment Banking PBT under Hong Leong Capital (HLC) saw an RM4.3m year-on-year increase in 1QFY19 as it posted a PBT of RM22.7m. Its higher PBT mainly contributed by higher non-interest income. On an individual segment basis, investment banking and stockbroking saw higher PBT by RM0.9m (+6.1%yoy) attributed to higher revenue contribution from its Treasury and Markets division. For its fund management and unit trust management, it posted PBT increase of RM2.4m (>100%yoy) mainly due to higher net contribution from management fee income.

FORECAST

We are maintaining our forecasts.

VALUATION

In our opinion, HLB continues to drive the Group's performance. We expect that HLB will continue to deliver on its earnings potential. However, we note that there may be some drag in terms of its net interest income and the margin compression. We believe that this will be moderated by the insurance division as it plays a supporting role given its commendable growth. Therefore, we are maintaining our NEUTRAL call with an adjusted TP to RM20.10 (from RM19.00) as we roll over HLB's valuation to FY20, which affected our SOTP valuation.



SOTP Valuation

Companies	Shareholder fund (RM'Mil)	As of	Equity Stake (%)	Book Value Multiple (X)	Basis	Valuation (RM'Mil)	RNAV per share (RM)
HLB	27,454		65.7%	1.5	Base on forecast for FY20	27,070	23.58
HLC	766	30/6/18	81.3%	1.4	Unaudited FY18 result	872	0.76
Insurance companies under HLA Holdings							
HLA	2,163	30/6/18	70.0%	1.4	Audited FY17 result	2,120	1.85
MSIG	2,957	30/6/18	30.0%	1.4	Interim FY17 result	1,242	1.08
HLMSIG Takaful	80	31/12/17	65.0%	1.4	Audited FY17 result	73	0.06
SOP Valuation						31,377	27.33
Holding company discount				25%		(8,299)	(7.23)
SOTP Valuation after holding company discount						23,078	
No of shares (Mil)						1,148	
Target Price (TP)						20.10	

INVESTMENT STATISTICS

FYE 30 June (RM'Mil)	FY17	FY18	FY19F	FY20F
Net Interest Income	2,822	2,871	3,235	3,460
Income from Islamic Banking	550	646	673	741
Non interest income	1,663	1,834	1,904	2,068
Net/total income	5,035	5,351	5,812	6,269
Pre-provisioning operating profit	2,812	3,056	3,446	3,743
Profit before tax	3,090	3,579	3,962	4,192
Profit after tax	1,507	1,907	2,144	2,269
EPS (sen)	131.8	166.8	186.9	197.7
EPS Growth (%)	7.0	26.6	12.0	5.8
PER (x)	14.6	11.5	10.3	9.7
Net Dividend (sen)	38	40	41	42
Dividend yield (%)	2.0	2.1	2.1	2.2
Book Value Per Share (RM)	14.52	15.55	16.88	18.42
PBV (x)	1.3	1.2	1.1	1.0
ROE (%)	9.1	10.7	11.1	10.7

Source: MIDFR, Company

DAILY PRICE CHART

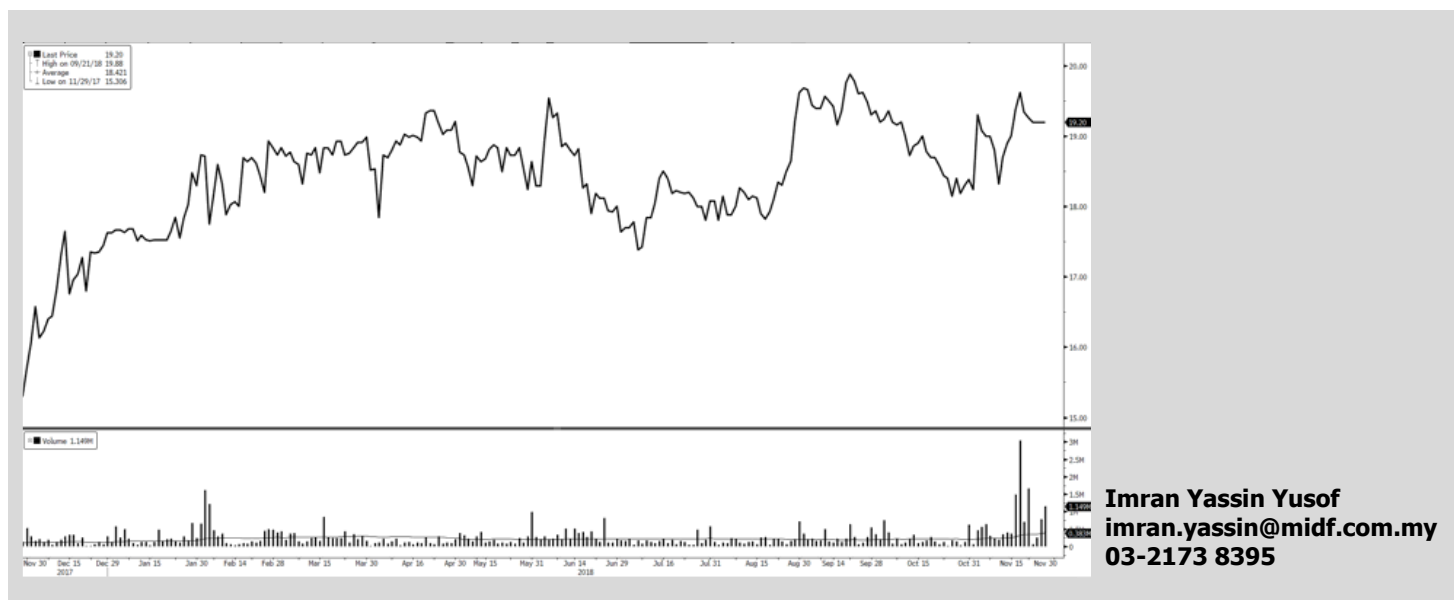


Table 1: Quarterly results

Quarterly results					
FYE June (RM m)	1Q19	4Q18	1Q18	Yoy (+/- %)	Qoq (+/- %)
Net Interest Income	691	690	729	-5.2%	0.2%
Islamic Banking Income	171	163	160	7.0%	5.1%
Non interest Income	521	467	390	33.5%	11.5%
Net/Total income	1,383	1,320	1,279	8.2%	4.8%
OPEX	(592)	(572)	(558)	6.0%	3.4%
PPOP	792	748	721	9.9%	5.8%
Write back/(Provision) for loan losses	(20)	(12)	(44)	-54.6%	66.7%
Share of results from associate & JV	157	135	164	-3.9%	16.9%
Pre-tax profit	929	871	840	10.5%	6.7%
Net Profit	506	454	455	11.1%	11.3%
EPS (sen)	44.2	39.7	39.8	11.1%	11.3%

Source: Company

Table 2: PBT of key segments (RM'm)

Business segments	1QFY19	1QFY18	Change (%)	Comments
Commercial Banking (HLB)	704	628	12.1%	Contributed by higher revenue and lower allowance for impairment losses on loans. This offset the higher operating expenses
Investment Banking	23	18	23.7%	Higher contribution from investment banking, stock broking and assets management
Insurance (HLA)	72	49	45.8%	Higher life fund surplus, lower allowance for impairment losses on securities and higher revenue

Source: Company

MIDF RESEARCH is part of MIDF Amanah Investment Bank Berhad (23878 - X).

(Bank Pelaburan)

(A Participating Organisation of Bursa Malaysia Securities Berhad)

DISCLOSURES AND DISCLAIMER

This report has been prepared by MIDF AMANAH INVESTMENT BANK BERHAD (23878-X). It is for distribution only under such circumstances as may be permitted by applicable law.

Readers should be fully aware that this report is for information purposes only. The opinions contained in this report are based on information obtained or derived from sources that we believe are reliable. MIDF AMANAH INVESTMENT BANK BERHAD makes no representation or warranty, expressed or implied, as to the accuracy, completeness or reliability of the information contained therein and it should not be relied upon as such.

This report is not, and should not be construed as, an offer to buy or sell any securities or other financial instruments. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. All opinions and estimates are subject to change without notice. The research analysts will initiate, update and cease coverage solely at the discretion of MIDF AMANAH INVESTMENT BANK BERHAD.

The directors, employees and representatives of MIDF AMANAH INVESTMENT BANK BERHAD may have interest in any of the securities mentioned and may benefit from the information herein. Members of the MIDF Group and their affiliates may provide services to any company and affiliates of such companies whose securities are mentioned herein. This document may not be reproduced, distributed or published in any form or for any purpose.

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.