

31 May 2018 | 3QFY18 Results Review

Hong Leong Financial Group

Surprised by associate's result

Maintain NEUTRAL

Adjusted Target Price (TP): 19.00
(from RM18.70)

INVESTMENT HIGHLIGHTS

- **Net profit for 9MFY18 was above expectations**
- **Hong Leong Bank Bhd remains a key driver**
- **HLB earnings driven by associate Bank of Chengdu**
- **Interim dividend of 27 sen**
- **Tweaking our FY18 and FY19 forecast upwards by +5.9 and +8.3% respectively**
- **Maintain NEUTRAL on HLFG with an adjusted TP of RM19.00 (from RM18.70) based on SOTP valuation**

HLFG 9MFY18 exceeded expectations. HLFG reported 9MFY18 net profit of RM1.45b, which was above ours and consensus' expectations coming in at 81.8% and 81.6% of respective full year estimates. The variance was due to better than expected contribution from HLB's associate, Bank of Chengdu (BOC).

Strong results from BOC drove HLB earnings. Contribution from BOC to HLB's earnings grew +67.3%yoy to RM404.4m. Meanwhile, the consolidated share of results from BOC to the Group saw growth of +53.9%yoy to RM450m. This was due to the robust operating income and improving asset quality

Besides that, Islamic banking was particularly strong as well, with income expanding +18.7%yoy to RM483.3m.

Meanwhile, HLB's OPEX grew +3.9%yoy with personnel cost being contained, remaining flat at RM835.5m. Main cost item continue to be IT expenses where it rose +11.3%yoy to RM122.7m as the Group continue to investment in digitisation.

However, HLB's gross loans growth continues to be much lower than expected with +1.6%yoy to RM125.4b. Mortgages and SME loans remains robust but auto loans continued its downtrend. In addition, there were also corporate repayments in the quarter.

Deposits for HLB was also equally disappointing as it grew by only +1.3%yoy to RM154.2b as at 9MFY18. Business enterprise was flat. However, we were pleased to see solid CASA expansion.

HLB's asset quality continues to be sound, with overall GIL ratio improving by +4bps yoy to 0.84% as at 3QFY18.

RETURN STATS

Price (30 May 2018)	RM18.50
Target Price	RM19.00
Expected Share Price Return	+2.7%
Expected Dividend Yield	+2.1%
Expected Total Return	+4.8%

STOCK INFO

KLCI	1,719.28
Bursa / Bloomberg	1082 / HLFG MK
Board / Sector	Main/ Finance
Syariah Compliant	No
Issued shares (mil)	1,145.2m
Market cap (RM'm)	21,187.0
Price over NA	1.2x
52-wk price Range	RM15.40 - RM19.70
Beta (against KLCI)	1.03
3-mth Avg Daily Vol	0.20m
3-mth Avg Daily Value	RM3.86m
Major Shareholders	
Hong Leong Co Malaysia	77.47%
EPF	1.92%
ING Groep NV	1.83%


Turnaround from contraction to growth for insurance division. Insurance division PBT manage to halt the contraction in 3QFY18 as it was able to record growth of +3.9%yoy to RM202.1m. Comparatively, 1HFY18 PBT fell -16.2%yoy. The turnaround was due to higher revenue.

Investment Banking business under Hong Leong Cap (HLC) continue trend lower. The Investment Banking PBT under Hong Leong Cap (HLC) fell -11.6%yoy to RM58.0m. This continued from the -6.4%yoy decline to RM37.4m seen in 1HFY18. The drag came from investment banking and stockbroking.

FORECAST

We are tweaking our FY18 and FY19 forecast upwards by +5.9% and +8.3% respectively to take into account the performance of HLB.

VALUATION

We opine that the Group continues to be driven by the performance of HLB. Although, HLB's prospect remain stable, we believe that the lower than expected loans growth may be a dampener going into FY19. However, this will be moderated by the performance of Bank of Chengdu. With no immediate catalyst to the Group's earnings, we are maintaining our NEUTRAL call. We are revising our TP to RM19.00 (from RM18.70) due to adjustment made to HLB's 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	25,721		65.7%	1.5	Base on forecast for FY19	25,362	22.09
HLC	745	30/6/17	81.3%	1.5	Audited FY17 result	909	0.79
Insurance companies under HLA Holdings							
HLA	1,572	30/6/17	70.00%	1.5	Audited FY17 result	1,651	1.82
MSIG	2,609	30/6/17	30.00%	1.5	Interim FY17 result	1,174	1.3
HLMSIG Takaful	81	30/6/17	65.00%	1.5	Audited FY17 result	79	0.09
SOP Valuation						29,174	25.41
Holding company discount				25%		(7,362)	(6.41)
SOP Valuation after holding company discount						21,812	
No of shares (Mil)						1,148	
Target Price (TP)						19.00	

INVESTMENT STATISTICS

FYE 30 June (RM'Mil)	FY16	FY17	FY18F	FY19F
Net Interest Income	2,641	2,822	3,122	3,341
Income from Islamic Banking	467	550	726	741
Non interest income	1,435	1,663	1,737	1,898
Net/total income	4,543	5,035	5,585	5,980
Pre-provisioning operating profit	2,259	2,812	3,218	3,452
Profit before tax	2,565	3,090	3,617	3,959
Profit after tax	1,359	1,507	1,881	2,143
EPS (sen)	123.2	131.8	163.9	186.7
EPS Growth (%)	-20.2	7.0	24.4	13.9
PER (x)	15.0	12.2	11.3	9.9
Net Dividend (sen)	38	38	38	39
Dividend yield (%)	2.1	2.4	2.1	2.1
Book Value Per Share (RM)	13.91	14.52	15.17	16.65
PBV (x)	1.3	1.1	1.2	1.1
ROE (%)	8.9	9.9	10.8	11.2

Source: MIDFR, Company

DAILY PRICE CHART

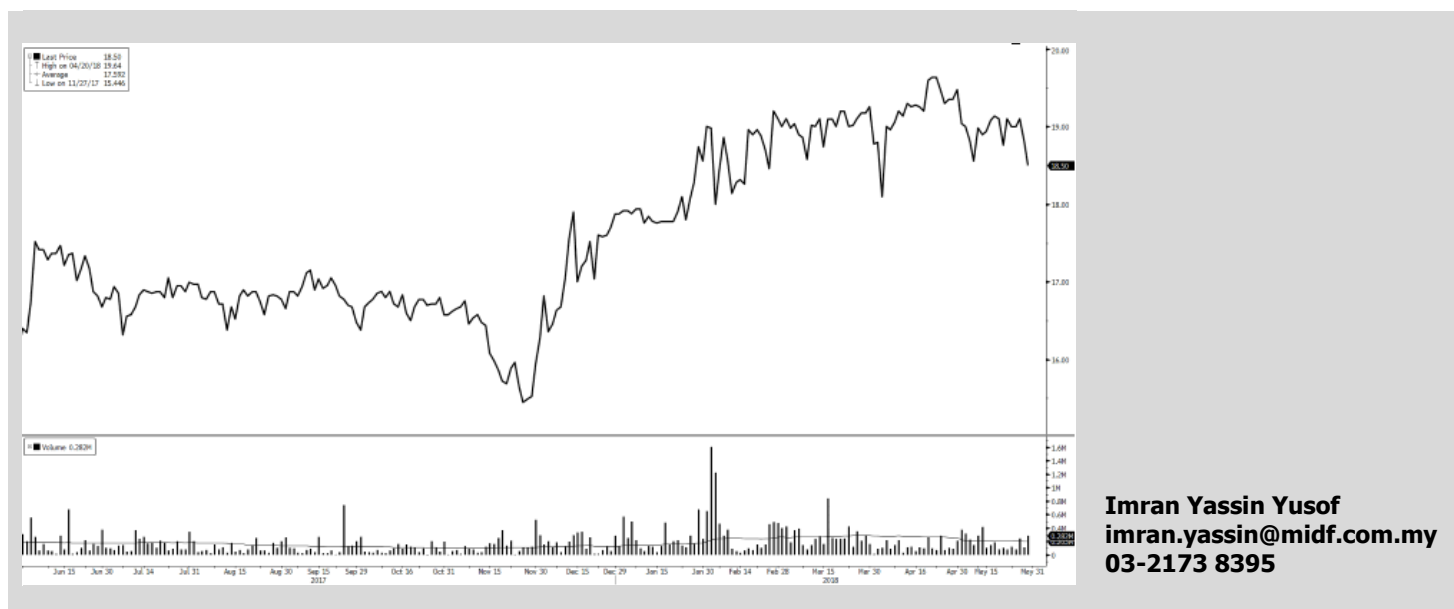


Table 1: Quarterly results

Quarterly results					
FYE June (RM m)	3Q18	2Q18	3Q17	Yoy (+/- %)	Qoq (+/- %)
Net Interest Income	706	747	719	-1.9%	-5.5%
Islamic Banking Income	167	157	139	19.7%	6.3%
Non interest Income	514	463	367	40.0%	11.1%
Net/Total income	1,386	1,366	1,226	13.1%	1.5%
OPEX	(593)	(572)	(553)	7.2%	3.5%
PPOP	794	794	673	18.0%	0.0%
Write back/(Provision) for loan losses	(11)	(10)	(43)	-74.4%	9.7%
Share of results from associate	155	136	129	19.5%	13.5%
Share of results from JV	5	5	5	11.5%	9.8%
Pre-tax profit	943	925	764	23.4%	2.0%
Net Profit	503	495	419	20.0%	1.5%
EPS (sen)	43.9	44.3	36.6	19.9%	-0.9%

Source: Company

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

Business segments	9MFY18	9MFY17	Change (%)	Comments
Commercial Banking (HLB)	2,049	1,810	13.2%	Strong showing from BOC.
Investment Banking	58	66	-11.6%	Drag by Investment Banking and Stockbroking.
Insurance (HLA)	202	195	3.9%	Higher revenue.

Table 3: Comparison of cumulative results and ratios (RM'Mil)

Cumulative results & ratios				
FYE June (RM m)	9MFY18	9MFY17	Yoy	
Net Interest Income	2,181	2,105	3.6%	
Islamic Banking Income	483	407	18.7%	
Non Interest Income	1,367	1,249	9.4%	
Net/Total Income	4,031	3,761	7.2%	
OPEX	(1,723)	(1,651)	4.4%	
PPOP	2,308	2,110	9.4%	
Writeback/(Provision) for loan losses	(65)	(98)	-33.2%	
Share of results from associate, BOC	450	292	53.9%	
Share of results from JV	15	17	-10.5%	
Pre-tax profit	2,708	2,322	16.6%	
Taxation and zakat	1,453	1,248	16.4%	
Net Profit	127.1	109.1	16.5%	
EPS (sen)	2,181	2,105	3.6%	
			(+/-ppts)	
ROE (%)	11.2	10.3	0.9	
CI ratio (%)	42.7	43.9	-1.2	

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.