30 May 2018 | 1QFY18 Results Review

Malayan Banking Berhad

Driven by strong NOII growth

***Maintain* BUY**

***Adjusted* Target Price (TP): RM11.40 (from RM11.20)**

INVESTMENT HIGHLIGHTS

- **Net profit within expectations**
- **Main growth driver was NOII and flat OPEX**
- **Gross loans and deposits growth was mostly contributed by Malaysia. Singapore and Indonesia also saw growths**
- **Asset quality remains steady**
- **Impact from MFRS 9 not as bad as initially estimated**
- **No change to forecast**
- **Maintain BUY. Adjust our TP to RM11.40 (from RM11.20) as we rollover valuation to FY19, based on PB multiple of 1.6x**

Net profit within expectations. The Group posted 1QFY18 net profit of RM1.87b, a +9.9%yoy growth. This was within ours and consensus' expectations at 23.2% and 22.9% of respective full year estimates.

Solid PPOP growth drove earnings higher. PPOP grew +10.8%yoy, driving the earnings growth. This was due to strong NOII expansion and supported by decent NII increase. NOII grew +12.6%yoy contributed by +20.5%yoy growth to RM1.51b in net earned insurance premiums. This had moderated the flat commission, services charges & fees (-0.4%yoy to RM836m), lower investment & trading income (-52.9%yoy to RM109m) and the swing to unrealised losses in securities & derivatives (-RM281m from RM130m gain). Meanwhile, NII grew +2.9%yoy which was supported by +1.5%yoy growth in gross loans.

Flat OPEX was also a contributor. OPEX was flat as the rise in personnel and marketing expenses (+5.8%yoy and +5.6%yoy to RM1.59b and RM142.8m respectively) was reined in by lower establishment and admin & general cost (-5.2%yoy and -10.6%yoy to RM457.2m and RM588.1m respectively). The declined in establishment cost was due to lower IT expenses while admin & general cost was lower due to absence of MFRS 9 automation cost last year.

Malaysian operation looking robust. As mentioned, gross loans grew only +1.5%yoy to RM493.4b. This was mainly supported by Malaysia where gross loans grew strongly by +6.7%yoy to RM288.9b. However, total international segment (Singapore and Indonesia) gross loans growth declined -5.1%yoy to RM197.2b. This was probably due to currency effect as in local currency terms, gross loans in Singapore and Indonesia grew +5.5%yoy and +2.9%yoy to SGD41.2b and IDR126.2t respectively. Growth in almost all segment contributed to the gross loans expansion in Malaysia. Notably was mortgage and corporate global banking where both makes up 29% of loans book. These grew +8.0%yoy to RM82.4b and +8.8%yoy to RM83.2b respectively.

RETURN STATS	
Price (28 May 2018)	RM10.00
Target Price	RM11.40
Expected Share Price Return	+14.0%
Expected Dividend Yield	+5.8%
Expected Total Return	**+19.8%**

STOCK INFO	
KLCI	1,775.84
Bursa / Bloomberg	1155 / MAY MK
Board / Sector	Main / Finance
Syariah Compliant	No
Issued shares (mil)	10,927.4
Market cap. (RM'm)	109,274.3
Price over NA	1.4x
52-wk price Range	RM9.10 – RM11.08
Beta (against KLCI)	1.03
3-mth Avg Daily Vol	18.14m
3-mth Avg Daily Value	RM191.06m
Major Shareholders	
Skim ASB	34.32%
EPF	11.64%
PNB	7.25%

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
COF = Cost of Funds
IA = Individual Assessment Allowance
YTD = Year-to-date
R&R = Restructuring and Rescheduling

Similarly to deposits and CASA. Reported Group gross deposits grew +47%yoy to RM532.1b, supported by Malaysia which increased +11.5%yoy to RM336.4b, while international segment fell -5.2%yoy to RM197.5b. However, in local currency terms, Singapore and Indonesia deposits grew +3.6%yoy to SGD43.8b and +2.6%yoy to IDR121.0t respectively. For CASA, the reported Group contracted -1.2%yoy to RM187.9b but on a normalised basis, it expanded +1.8%yoy. Malaysia's CASA growth is a slightly concern as it was flattish at +0.8%yoy to RM125.4b.

Asset quality seems steady. GIL ratio improved -3bps yoy to 2.37% and slower sequential quarter formation at +1.4%qoq to RM11.7b as compared to +5.4%qoq as at 1QFY17. This means that asset quality continues to be steady and stable. We opine that the improvement in GIL ratio was supported by asset quality in Indonesia as the GIL ratio there improved -34bps yoy to 4.21%. Meanwhile, GIL ratio in Malaysia and Singapore jumped +9bps yoy to 2.22% and +66bps yoy to 2.34%. For Malaysia, this was due to retail SME and mortgage segment. However, our concern remains in Singapore due to ongoing weakness in the corporate segment. GIL ratio for this segment rose +9bps qoq and +161bps yoy to 4.23% and suggest that there is still weakness in the oil and gas sector. Although the management could not reveal individual cases, we believe that the situation there may deteriorate further in the coming quarters due to a debt reorganization of a utility player. Nevertheless, evaluating as a Group, the asset quality improvement in Indonesia and stable condition in Malaysia will compensate any weakness in Singapore.

MFRS 9 not as bad as we initially thought. The impact of MFRS 9 adoption to CET1, Tier 1 and Total Capital ratios was less than what we have initially estimated. The Day One impact was lowering of these ratios by about -40bps. In comparison, we had estimated an impact of -50bps. Impaired loans were higher as it jumped +32.7% to RM10.96b, but shareholders' equity movement were only reduced by -RM955m to RM72.0b as at 1 January 2018. This was due to utilisation of regulatory reserve to buffer the impact to retained profits. All-in, the impact of MFRS 9 was not as bad as was predicted by many last year.

FORECAST

We are maintaining our forecasts as the result were within expectations.

VALUATION AND RECOMMENDATION

We believe that the Group recorded a very good set of results in 1QFY18. This bode well for the rest of the year. Although, there may be headwinds in term of asset quality and NIM, coupled with the uncertainty in Malaysia following GE14, we believe that the Group will be able to maintain its earnings growth trajectory. We believe that the recent share price retracement have been unwarranted and present a good opportunity for investors to accumulate on the stocks. Hence, we are maintaining our **BUY** call. As we rolling over our valuation to FY19, we are adjusting our TP to RM11.40 (from RM11.20), based on PB multiple of 1.6x.

INVESTMENT STATISTICS

FYE Dec	FY16	FY17	FY18F	FY19F
Net interest income (RM'm)	11,568	12,147	12,699	13,068
Islamic banking income (RM'm)	4,189	4,900	4,634	5,148
Non-interest income (RM'm)	6,506	6,298	7,023	7,622
Total income (RM'm)	22,263	23,345	24,356	25,838
Pretax profit (RM'm)	8,844	10,098	10,558	11,255
Net profit (RM'm)	6,743	7,521	8,070	8,713
Core net profit (RM'm)	6,743	7,521	8,070	8,713
Core EPS (sen)	67.8	72.0	74.9	78.4
PER (x)	14.7	13.9	13.5	12.8
Net dividend (sen)	52	55	58	61
Net dividend yield (%)	5.2	5.5	5.8	6.1
Book value per share (RM)	6.72	6.77	6.90	7.15
PBV (x)	1.5	1.5	1.4	1.4
ROE (%)	10.6	10.3	10.6	10.8

Forecast by MIDFR

DAILY PRICE CHART

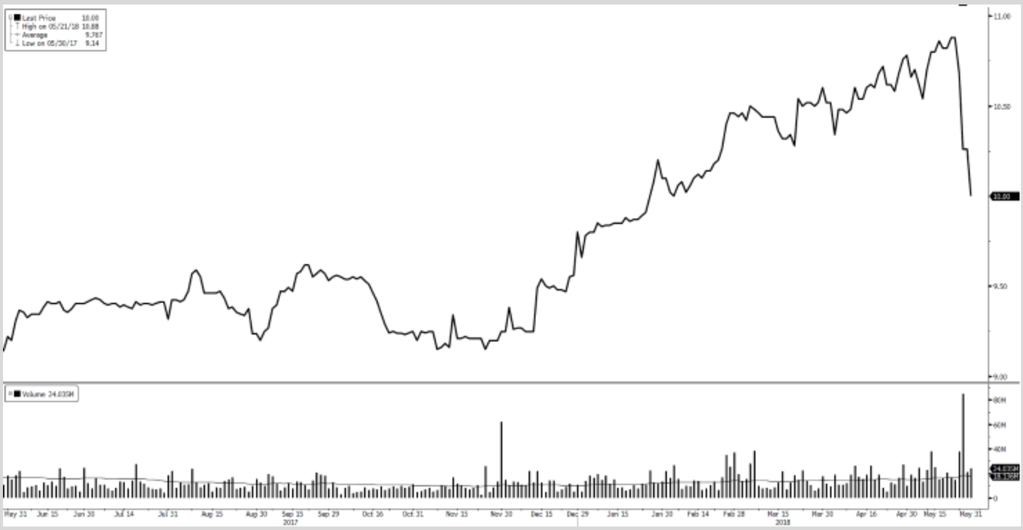

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Table 1: Quarterly results based on reported financials

Quarterly results						Comments
FYE Dec (RM m)	**1QFY18**	**4QFY17**	**1QFY17**	**Yoy**	**Qoq**	
NII*	4,237.9	4,161.3	4,117.9	2.9%	1.8%	Supported by gross loans growth of 1.5%yoy.
NOII*	1,589.9	1,895.2	1,412.1	12.6%	-16.1%	Due to strong growth in net earned insurance premium (+20.5%yoy to RM1.51b). Moderated flat commission, service charges and fees (-0.4%yoy to RM839m), and lower investment & trading income (-52.9%yoy to RM109m) and the swing to unrealised losses in securities & derivatives (-RM281m from RM130m gain).
Net income	5,827.8	6,056.4	5,530.0	5.4%	-3.8%	
OPEX	(2,778.8)	(2,922.8)	(2,779.3)	0.0%	-4.9%	Higher personnel and marketing expenses (+5.8%yoy and +5.6%yoy to RM1.59b and RM142.8m respectively) was reined in by lower establishment and admin & general cost (-5.2%yoy and -10.6%yoy to RM457.2m and RM588.1m respectively).
PPOP	3,048.9	3,133.6	2,750.6	10.8%	-2.7%	
Net impairment losses	(500.8)	(239.7)	(542.8)	-7.7%	108.9%	Lower when compare to IA and CA in 1QFY17.
Pre-tax profit	2,556.7	2,926.1	2,249.1	13.7%	-12.6%	
Taxation	(657.2)	(675.1)	(504.0)	30.4%	-2.7%	
Net Profit	1,871.0	2,132.1	1,702.8	9.9%	-12.2%	
EPS (sen)	17.3	19.9	16.7	3.6%	-13.1%	

*Includes a portion of Islamic Banking income

Table 2: Financial ratios by quarter

Financial Ratios (%)	1QFY18	4QFY17	1QFY17	Yoy (+/- ppts)	Qoq (+/- ppts)	Comments
CET1*	13.7	14.2	13.0	0.7	-0.5	Lower quarter-on-quarter due to MFRS 9.
Tier 1*	15.4	15.9	14.7	0.7	-0.5	
Total Capital*	18.5	18.8	18.5	0.0	-0.3	
GIL ratio	2.37	2.34	2.40	-0.03	0.03	Higher quarter-on-quarter due to MFRS 9 due to judgemental triggers.
NIL ratio	1.20	1.58	1.70	-0.50	-0.38	
Loan loss Coverage	87.8	71.5	71.2	16.6	16.3	
Credit charge-off	0.41	0.16	0.45	-0.04	0.25	
NIM	2.39	2.30	2.43	-0.04	0.09	Compression in Indonesia. Higher on sequential quarter basis due to Malaysia's OPR hike in January.
CI	47.6	48.2	50.1	-2.5	-0.6	
LD ratio	92.5	93.8	95.7	-3.2	-1.3	
ROEA	10.5	12.4	10.0	0.5	-1.9	

**Group Capital Ratios based on 85% take up rate for DRP*

Table 3: Contribution to PBT by business segments and ratios based on reported financials

Cumulative results				Comments
PBT by business segments (RM m)	**1QFY18**	**1QFY17**	**Yoy (+/- %)**	
Community Financial Services	1,396.0	1,206.2	15.7%	Mainly due to lower allowances for impairment losses on loans, advances, financing and other debts, lower overhead expenses, higher NII and income from IBS operations, and higher NOII.
Corporate Banking & Global Markets	1,040.7	1,177.4	-11.6%	Due to higher allowances for impairment losses on loans, advances, financing and other debts, lower share of profits in associates and joint ventures, lower NII and income from IBS operations and higher OPEX. This was offset by higher writeback for impairment losses on financial investments and other financial assets and higher NOII.
Investment Banking	155.3	63.9	143.1%	Higher NOII and NII and income from IBS operations and higher writeback for impairment losses on loans, advances, financing and other debts.
Group Asset Management	(40.0)	26.1	-253.0%	Lower NOII and and higher allowances for impairment losses on financial investments and other financial assets.
Group Insurance & Takaful	108.8	176.7	-38.4%	Lower NOII and higher OPEX and higher allowances for impairment losses on loans, advances, financing and other debts.
PBT contribution by geographies (%)				
	1QFY18	**1QFY17**	**Yoy +/- ppts**	
Malaysia	63.4	69.5	-6.1	
Indonesia	5.5	8.7	-3.2	
Singapore	20.3	9.0	11.3	
Others	10.8	12.8	-2	

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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 *rise* 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	*Negative* total return is expected, by -10% or more, over the next 12 months.
TRADING SELL	Stock price is expected to *fall* 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.