midf RESEARCH

01 June 2018 | 1QFY18 Results Review

RHB Bank Berhad

Strong income growth

***Upgrade to* TRADING BUY**

***Adjusted* Target Price (TP): RM6.00 (from RM5.70)**

INVESTMENT HIGHLIGHTS

- **Strong result but within expectations**
- **Contributed by solid income growth**
- **OPEX expanded drastically**
- **Sturdy domestic loans growth led by mortgage and SMEs**
- **Asset quality improved**
- **No change to forecast**
- **Upgrade to Trading Buy with adjusted TP of RM6.00 (from RM5.70), as we roll over our valuation to FY19**

Strong results within expectations. The Group registered a strong net profit growth of +18.1%yoy to RM590.8m. However, this was within ours and consensus' expectations as it came in at 27.1% and 27.4% of respective full year estimates.

Strong income growth main contributor to earnings growth. NII (including Islamic Banking net fund based income) rose +12.9%yoy to RM1.23b due to positive impact from OPR hike in January 2018. NIM expanded +11bps yoy. Besides the OPR hike, NIM improvement was also due to better funding cost management as CASA grew +14%yoy to RM49.7b. Meanwhile, NOII grew +15.8%yoy to RM534.7m mainly due to higher net forex gain and trading & investment income. Nevertheless, there were also one-off gains of RM131m in the quarter.

Lower provisions was also a contributor. Allowance for loan impairment fell -13.5%yoy as credit cost begin to normalise. This could be due to reduction of exposure in the oil & gas sector where it makes up 3.12% of total gross loans, as compared to 3.21% as at 4QFY17. However, while 1QFY18 saw credit cost below guidance of 30bps, management indicated that it might inch up in the coming quarters.

Positive JAWS but OPEX expanded drastically. OPEX grew +13.5%yoy. While this was matched by total income growth of +14.1%yoy, we are concern by rapid rise in OPEX as any pull back in income may drag earnings down. However, we understand that the reason for the higher than expected OPEX growth was early provisioning of certain personnel cost and IT expenses. Discounting these provisioning, OPEX would have rose by +8 to 9%yoy. As such, OPEX may normalise later in the year.

Modest loans growth due to overseas. Group gross loans expanded +4.3%yoy to RM161.2b as it was moderated by overseas' operation and wholesale banking loans decline of -14.2%yoy to RM14.8b and -1.8%yoy to RM43.6b respectively. However, retail and business banking grew by +11.4%yoy and +8.7%yoy to RM78.5b and RM24.3b respectively. This was lead by mortgage (+16.5yoy to RM48.9b) and SME loans (+9.6%yoy to RM22.4).

RETURN STATS	
Price (31 May 2018)	RM5.34
Target Price	RM6.00
Expected Share Price Return	+12.3%
Expected Dividend Yield	+2.8%
Expected Total Return	**+15.1%**

STOCK INFO	
KLCI	1,740.62
Bursa / Bloomberg	1066 / RHBBANK MK
Board / Sector	Main / Finance
Syariah Compliant	No
Issued shares (mil)	4,010.0
Market cap. (RM'm)	21,413.6
Price over NA	0.9x
52-wk price Range	RM4.71 – RM5.61
Beta (against KLCI)	1.47
3-mth Avg Daily Vol	2.28m
3-mth Avg Daily Value	RM12.11m
Major Shareholders	
EPF	40.70%
Aabar Investment PJS	17.75%
OSK Equity Holdings	10.13%

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
OPEX = Operating Expenses
LLC = Loan Loss Coverage
PPOP = Pre Provision Operating Profit

Domestic lead asset quality improvement. Group GIL ratio as at 1QFY18 fell -10bps yoy to 2.29%, attributable to improvement in its domestic assets. Domestic assets GIL ratio improved -52bps yoy to 1.64%. Comparing on sequential quarter basis, Group GIL ratio had a slight uptick of +6bps qoq but we could ascribe this to impact of MFRS 9. Day One impact saw GIL ratio increased +15bps.

Not much impact to MFRS 9 implementation. Day One impact of MFRS 9 implementation saw fully loaded CET1 ratio reduction of only -20bps to 13.7%. Other impact included increase of RM1.36 in allowance for impaired loans, regulatory reserves reduction of RM1.12b and decrease of retained earnings by RM123m only.

Committed to 5-year strategy. Recall, after conclusion of IGNITE 2017, the Group has embarked on a new 5-year strategy with three key thrusts, namely Funding the Group Journey, Invest to Win in the medium term and Transform the Organisation. The new strategy is named FIT22. Amongst the target segments are continuation of Affluent and Mass Affluent market, SMEs, Mid Caps and Large Caps. One aspect of FIT22 is its digitization of the Group. As we have previously stated, we opine that this could lead to additional OPEX in the next 2-3 years time as the Group invest on IT infrastructure and talent acquisition amongst others. However, we opine that these investments can be seen as necessary as the Group need to boost its performance going forward.

FORECAST

We are maintaining our forecast.

VALUATION AND RECOMMENDATION

The Group had a solid start to the year. We were pleasantly surprised by the strength of income growth in the quarter. We expect the boost to NIM in 1QFY18 to taper off as the effect of the OPR hike wears out and deposits priced higher. This could bring pressure to income and subsequently PPOP should OPEX growth trajectory remains high. Nevertheless, we expect that OPEX will normalise given that the Group were front loading some of the expenses in 1QFY18. We believe that this good performance will likely be an impetus for investors to revisit the stock. Hence, we are upgrading our call to **TRADING BUY** (from NEUTRAL) with an adjusted **TP of RM6.00** (from RM5.70) as we roll our our valuation to FY19. Our TP is based on pegging its FY19 BVPS to 0.95x which is its 5-year average PBV.

INVESTMENT STATISTICS

FYE Dec	FY16	FY17	FY18F	FY19F
Net interest income (RM'm)	3,453	3,522	3,892	4,139
Other operating income (RM'm)	1,763	1,780	1,778	1,800
Islamic Banking income (RM'm)	977	1,085	1,031	1,083
Total income (RM'm)	6,193	6,387	6,702	7,021
Pretax profit (RM'm)	2,232	2,558	2,837	3,027
Net profit (RM'm)	1,682	1,950	2,174	2,322
Core Net profit (RM'm)	1,875	1,950	2,174	2,322
Core EPS (sen)	43.6	48.6	54.2	57.9
EPS growth (%)	-34.8	11.5	11.5	6.8
PER (x)	12.2	11.0	9.8	9.2
Net dividend (sen)	12	15.0	15.0	17.0
Net dividend yield (%)	2.2	2.8	2.8	3.2
Book value per share (RM)	5.42	5.77	6.01	6.41
PBV (x)	1.0	0.9	0.9	0.8
ROE (%)	8.5	8.7	9.0	9.0

Forecast by MIDFR

DAILY PRICE CHART

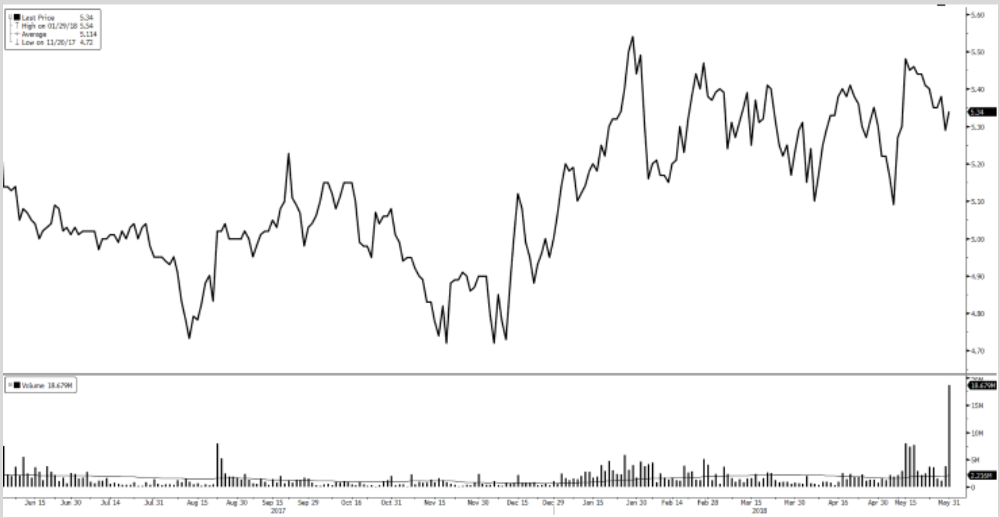

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Table 1: Quarterly results (base on reported financials)

Quarterly results						Comments
FYE Dec (RM m)	**1QFY18**	**4QFY17**	**1QFY17**	**Yoy (+/- %)**	**Qoq (+/- %)**	
Net Interest Income	928.9	892.2	851.6	9.1%	4.1%	Strong improvement in NIM.
Other Operating Income	566.7	520.2	448.1	26.5%	8.9%	Trading and investment gains and mark-to-market gains from investment in PE fund.
Islamic Banking Income	273.8	255.2	255.8	7.0%	7.3%	
Net/Total Income	1,769.4	1,667.6	1,555.4	13.8%	6.1%	
OPEX	(863.0)	(847.4)	(761.2)	13.4%	1.8%	Provisioning of HR cost and IT expenses.
PPOP	906.4	820.2	794.2	14.1%	10.5%	
Write back/(Provision) for loan losses & other assets	(114.5)	(218.4)	(136.0)	-15.8%	-47.6%	Normalising credit cost.
Pre-tax profit	791.9	601.9	658.3	20.3%	31.6%	
Taxation	(200.9)	(139.8)	(156.7)	28.2%	43.7%	
Net Profit	590.8	460.1	500.3	18.1%	28.4%	

Table 2: Financial Ratios

Financial Ratios (%)	1QFY18	4QFY17	1QFY17	Yoy (+/-ppts)	Qoq (+/-ppts)	Comments
CET1	13.5	13.9	13.2	0.3	-0.4	
CCR	13.7	14.2	13.5	0.2	-0.5	
RWCR	16.7	17.2	17.0	-0.3	-0.5	
GIL	2.29	2.23	2.39	-0.10	0.06	
Credit charge-off	0.26	0.29	0.35	-0.09	-0.03	
NIM	2.28	2.17	2.17	0.11	0.11	Impact from OPR hike.
Loan loss Coverage	107.4	101.6	77.7	29.7	5.8	
CI ratio	48.8	50.8	48.9	-0.2	-2.0	
Net LDR	93.1	95.3	91.8	1.3	-2.2	
ROEA	10.4	7.9	9.1	1.3	2.5	

Table 3: PBT by key segments (based on reported financials)

PBT (RM m)	1QFY18	1QFY17	Yoy (+/- %)	Comments
Corporate and Investment Banking	173.8	156.2	11.3%	Higher non-fund based and net fund based income.
Retail Banking	225.2	257.5	-12.5%	Higher OPEX and higher ECL
Business Banking	89.4	88.1	1.5%	Higher net funding income and lower ECL
Treasury	342.0	302.8	12.9%	Higher net forex gain and trading & investment gain.
Group International Business	52.8	(12.3)	>100%	Lower impairment and higher NOII.
Support center & others	(91.3)	(134.0)	-31.9%	
Share of results of JV	(9.0)	96.0	-109.4%	
Group PBT	791.9	658.3	20.3%	

Source: Company, MIDFR

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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.