BANKING

***Maintain* POSITIVE**

FSR 1H23: Interest coverage ratio normalisation continues

KEY INVESTMENT HIGHLIGHTS

- **Business segment: Headwinds continue to plague vulnerable segments – expect smaller SMEs to be affected most**
- **Household segment: Less EPF withdrawals should bode well for financial stability, delinquency rates remain under control**
- **Financial institution resilience: LCR remains healthy amid elevated COF as banks draw from alternative forms of funding – Provisions should be adequate to weather further periods of asset quality stress, especially with capitalisation levels healthy**
- **Maintain POSITIVE call: Stronger NOII, loan and deposit growth should offset potential negative asset quality and provisioning surprises**

Business segment: Headwinds likely to persist. Overall firms-at-risk saw minor uptick – while deteriorations were across the board, real estate segment saw tremendous improvement. Interest-coverage ratio continues to normalise (moving lower) concurrent to OPR hikes.

External headwinds remain bleak: Commodity-and-building-material-related fears (most notably Crude Oil) and labour shortages continue to cast uncertainty over the financial health of businesses in the next couple of quarters. Notably, agriculture SMEs have seen a sharp increase in loans-in-arrears in the last two quarters as CPO conditions are far from ideal.

Household (HH) segment: Motor vehicle, residential mortgages continue to drive debt growth. Unsecured loans were also very in trend. HH debt continued to outpace HH financial assets despite higher financial asset growth rates, following the reduction of EPF withdrawals.

Increases in lower-income group floating rate loans rose relatively sharply, though this was largely within banks' expectations.

Financial Institution resilience: Banks are more than well equipped to handle any major shocks. Asset quality has been kept well under control with writebacks – do expect, however, provisioning downside from more vulnerable smaller banks. The latest BNM banking stats showed continued issues with Islamic FD rates – but Islamic banks should keep in manageable with alternative forms of funding for now.

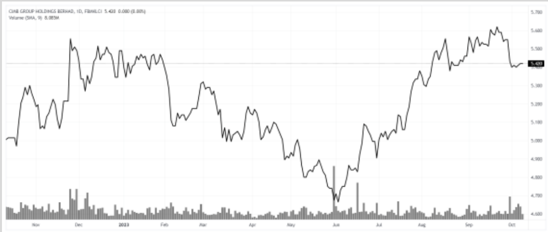
Maintain POSITIVE call. With possible economic headwinds ahead, we expect asset quality issues may persist, though negative effects should affect smaller banks harder than others. Overlay writebacks will likely be limited. Positive drivers should include more impressive NOII, loan and deposit figures in 2HCY23 – while NIM is expected to recover (slowly), end-year deposit competition could put a damper on things.

Top Picks: CIMB (BUY, TP: RM6.43) and **Public Bank (BUY, TP: RM4.76).**

COMPANY IN FOCUS

CIMB
Maintain **BUY |** Unchanged Target price: RM6.43
Price @ 9 October 2023: RM5.42
- Lucrative overseas exposure
- Good OPEX control, following cost restructuring exercise

Share price chart



Public Bank
Maintain **BUY |** Unchanged Target price: RM4.76
Price @ 9 October 2023: RM4.03
- Excellent defensive pick
- Continues to acquire loan and deposit market share.

Share price chart

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PEER COMPARISON TABLE

Bank	Rec	Share P* (RM)	Target P (RM)	Upside (%)	Mkt Cap (RM b)	P/E (x) FY23	P/E (x) FY24	P/B (x) FY23	P/B (x) FY24	ROE (%) FY23	ROE (%) FY24	Div Yield (%) FY23	Div Yield (%) FY24
MAY	NEUTRAL	8.80	9.28	5.5	105.3	11.5	10.7	1.2	1.1	10.5	10.9	7.0	7.5
CIMB	BUY	5.42	6.43	18.6	56.5	8.7	8.0	0.9	0.8	10.1	10.3	6.3	6.3
PBK	BUY	4.03	4.76	18.1	78.2	11.0	10.8	1.4	1.3	13.6	12.9	4.6	4.6
RHB	BUY	5.50	6.66	21.1	23.0	7.9	7.3	0.8	0.7	9.9	10.1	6.9	7.3
HLBK	BUY	19.24	22.96	19.3	39.4	9.8	9.2	1.1	1.0	11.3	11.0	3.6	3.8
HLFG	BUY	17.30	23.71	37.1	19.6	7.0	6.5	0.7	0.6	10.0	10.0	2.9	3.1
AMMB	BUY	3.80	3.98	4.7	15.9	8.9	8.4	0.8	0.8	9.5	9.5	4.9	5.3
BIMB	NEUTRAL	2.17	2.04	-6.0	5.2	10.0	9.0	0.7	0.7	7.4	7.7	6.3	6.6
AFFIN	NEUTRAL	2.07	1.71	-17.4	4.5	10.0	7.8	0.4	0.4	4.1	5.1	2.9	3.7
ABMB	BUY	3.34	3.90	16.9	5.2	7.4	6.9	0.7	0.7	10.0	10.2	6.7	7.3
Simple avg (ex-HLFG)						**9.5**	**8.7**	**0.9**	**0.8**	**9.6**	**9.7**	**5.5**	**5.8**
Weighted avg (ex-HLFG)						**10.2**	**9.6**	**1.1**	**1.0**	**11.0**	**11.0**	**5.7**	**6.0**

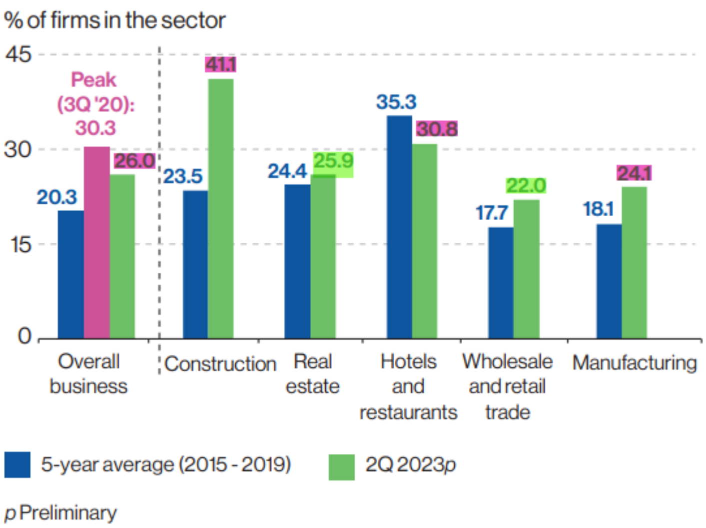
**Closing prices from 09 Oct 2023.*
^AMMB, ABMB, HLBK & HLFG uses FY24F/25F values.

Source: Banks, MIDFR

A. BUSINESS SECTOR CREDIT RISK

Fig 1: Firms-at-risk 1H23…

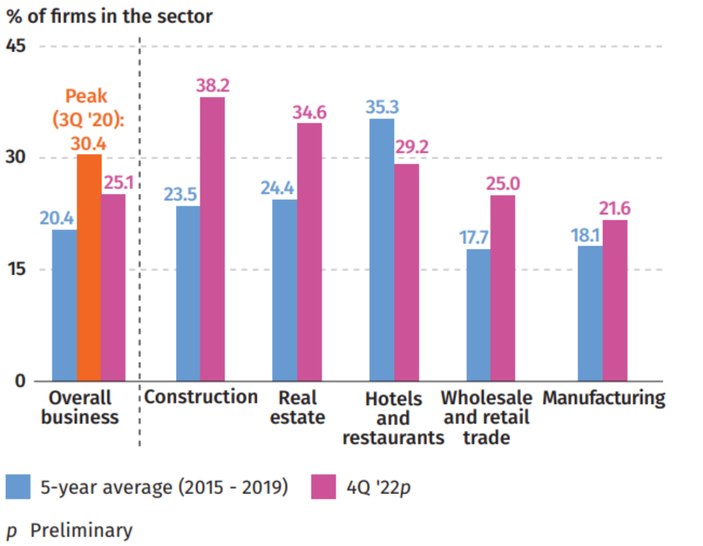
Overall uptick, driven by rising pressure in most sectors…



Source: BNM, MIDFR

Fig 2: … vs 2H22's figures

…but improvements seen in real estate and manufacturing.



Source: BNM, MIDFR

Fig 3: SME Loans-in-Arrears for Selected Sectors

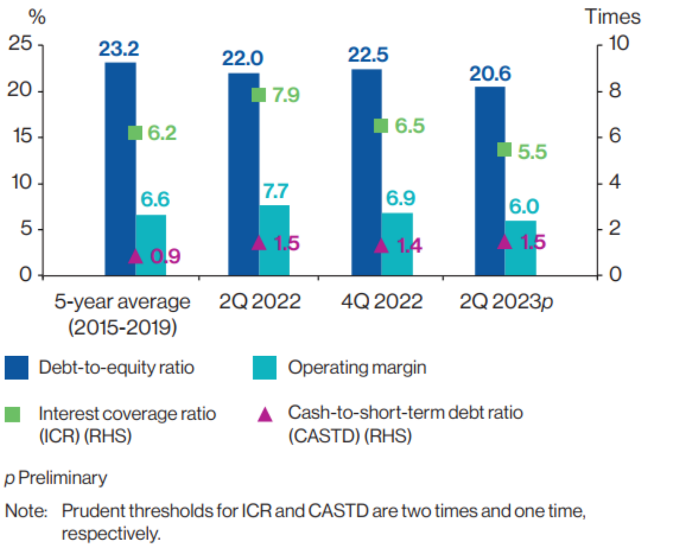
Sector	Outstanding Loans (% of total banking system loans)	Loans-in-Arrears[1] (% of SME loans to the sector) Dec 2022	Jun 2023
Wholesale and retail trade	5.1	1.5	1.8
Retail food and beverages	*0.1*	*0.7*	*1.6*
Construction	2.1	3.8	4.5
Agriculture	0.5	2.3	6.2

[1] Refers to loans with 3 months or more in-arrears, equivalent to more than 90 days past due.

Source: BNM, MIDFR

Fig 4: Key Financial Performance Indicators

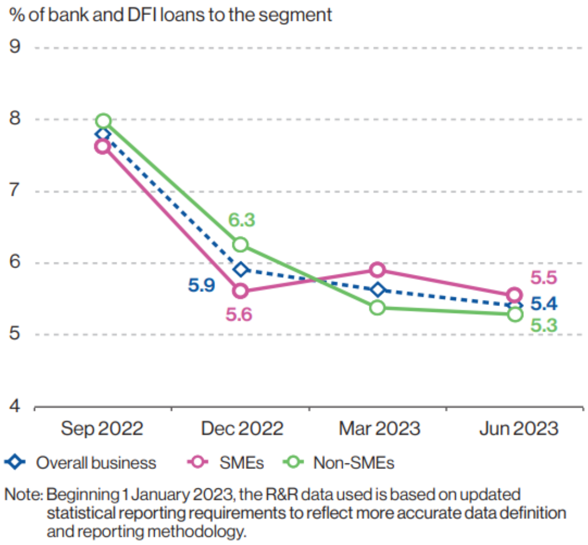
While still well above the prudent threshold, ICR has shown a sharp decline, with heavier pressure skewed towards smaller firms. Also reflected in lower operating margin.



Source: BNM, MIDFR

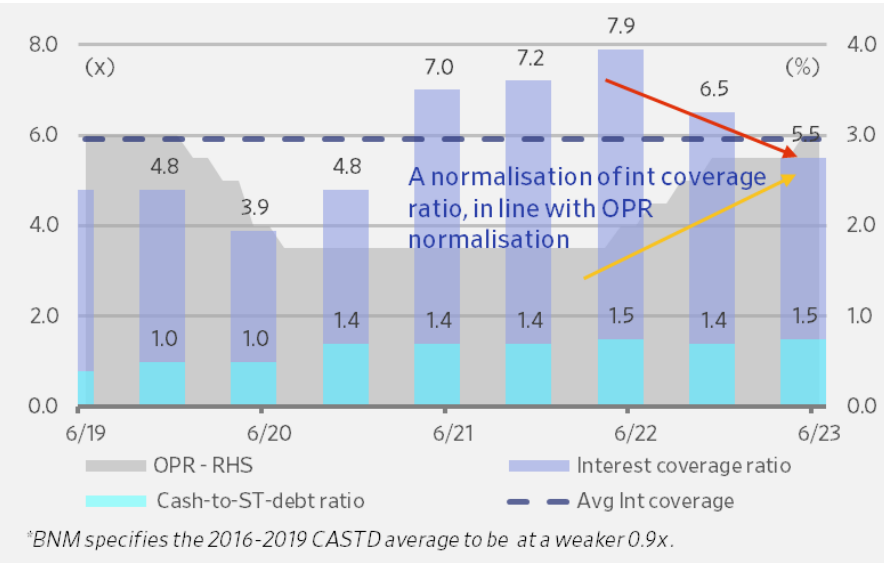
Fig 5: Share of R&R Loans by Segment

Unsurprisingly, SMEs continue to trickle out of R&R programmes with minimal reenrollment (0.1% of total SME loans).



Source: BNM, MIDFR

Fig 6: Debt serviceability ratios of businesses

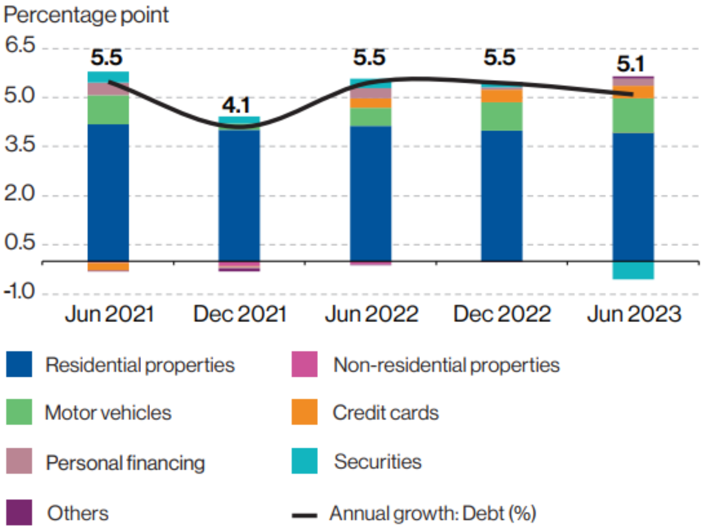


Source: BNM, MIDFR

B. HOUSEHOLD SEGMENT CREDIT RISK

Fig 7: Annual Growth of Debt

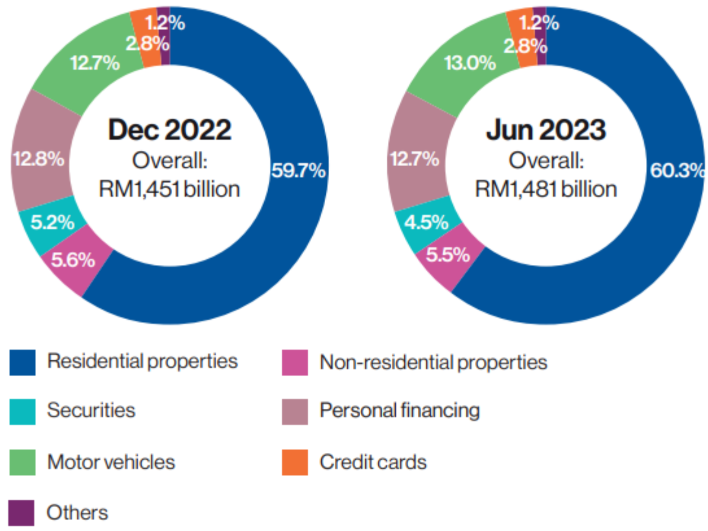
Overall growth was more muted at 5.1%. Unsecured lending and motor vehicle loan growth are very strong this period. Securities show sizeable shrinkage.



Source: BNM, MIDFR

Fig 8: Composition of debt by Purpose

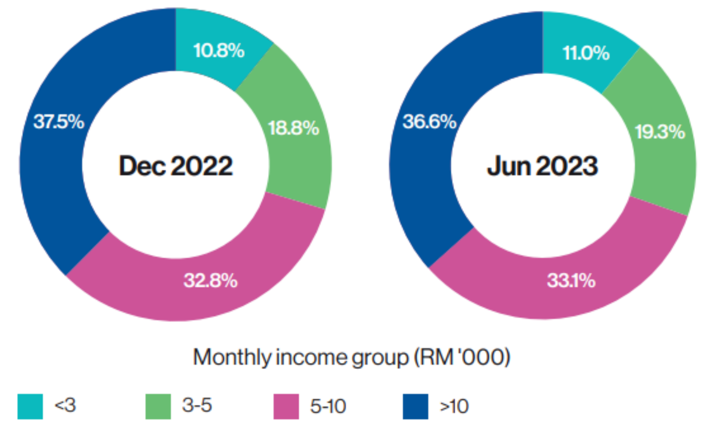
Residential properties and motor vehicles fill up the void left by reduced Securities-related debt.



Source: BNM, MIDFR

Fig 9: Composition of Banking Debt by Income Group

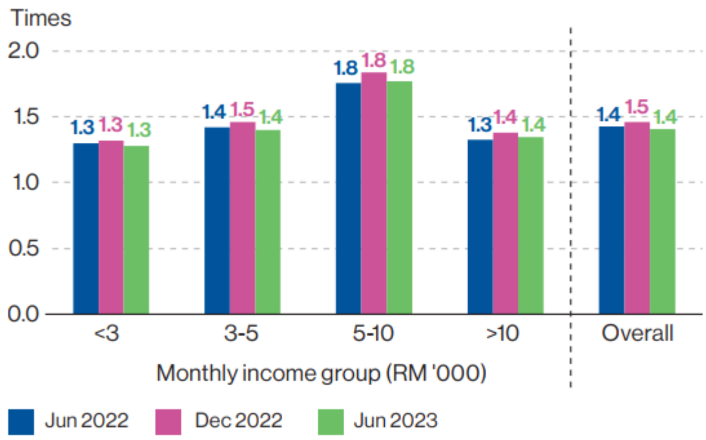
The bulk of growth is coming from 3-5 and 5-10 categories.



Source: BNM, MIDFR

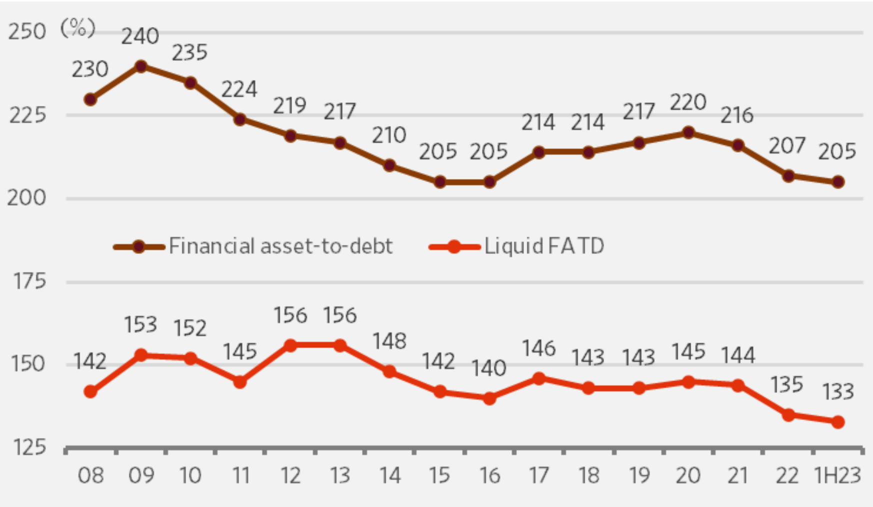
Fig 10: Median Debt-to-Income Ratios by Income Group

Remains relatively stable.



Source: BNM, MIDFR

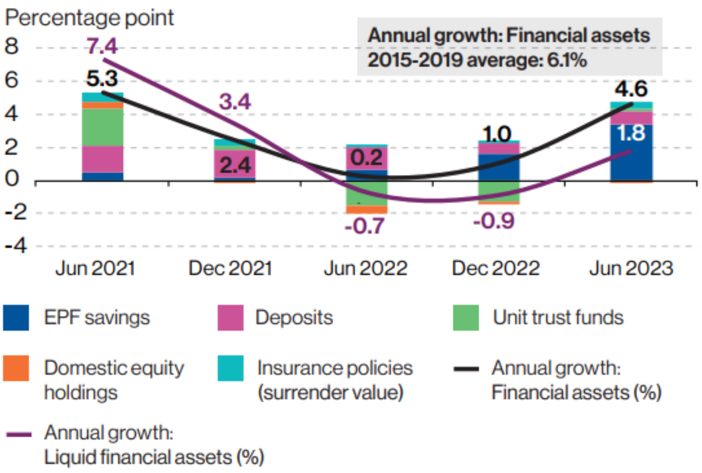
Fig 11: Household Financial asset-to-debt ratios



Source: BNM, MIDFR

Fig 12: Annual Growth of Financial Assets

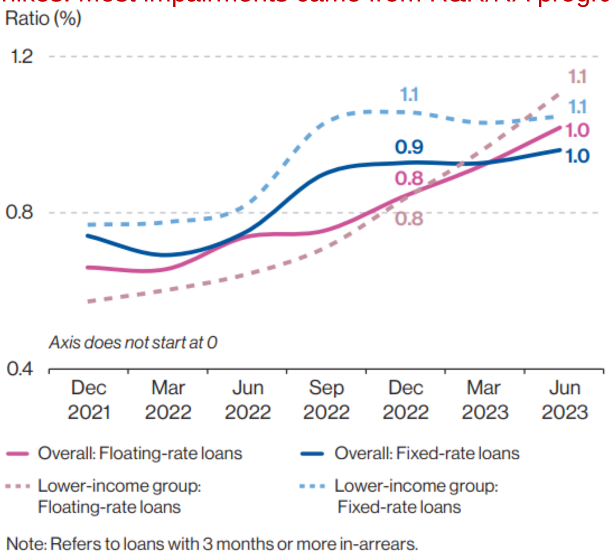
Financial Assets saw good growth this time around, as EPF withdrawals have reduced.



Source: BNM, MIDFR

Fig 13: MIA-3 Ratio by Floating/Fixed rate loans.

As expected, lower-income borrowers of floating-rate loans are feeling a bit more of a pinch than others, given the OPR hikes. Most impairments came from R&R/RA programmes.

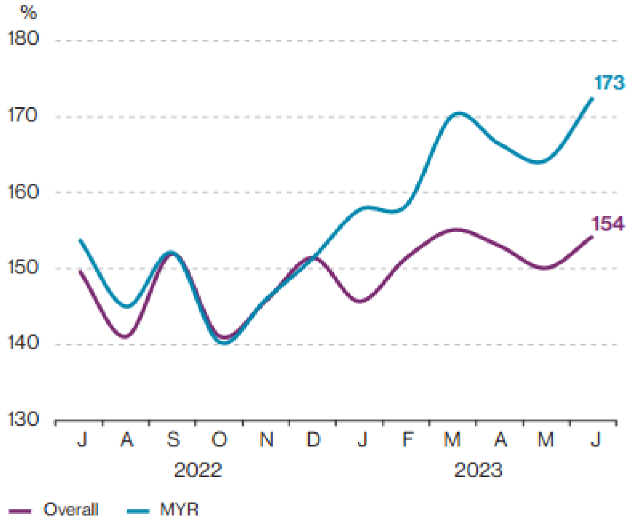


Source: BNM, MIDFR

C. FINANCIAL INSTIUTION RESILIENCE

Fig 14: System Liquidity Coverage Ratio

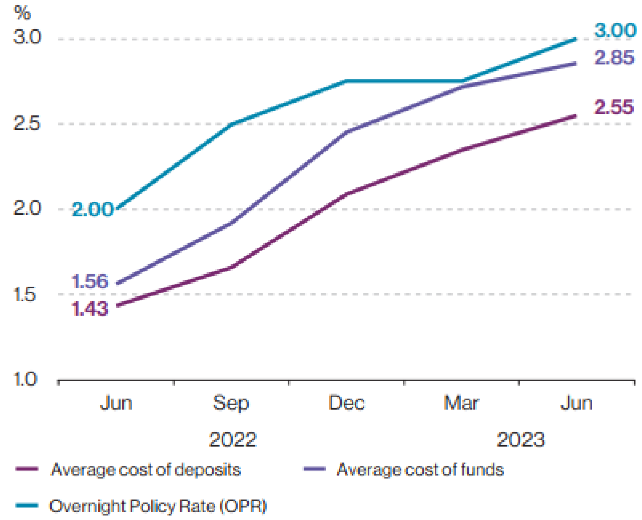
LCR remains highly elevated as banks draw down on repo-related funding amid higher cost of funds.



Source: BNM, MIDFR

Fig 15: Avg Cost of Deposits, Avg Cost of Funds, OPR

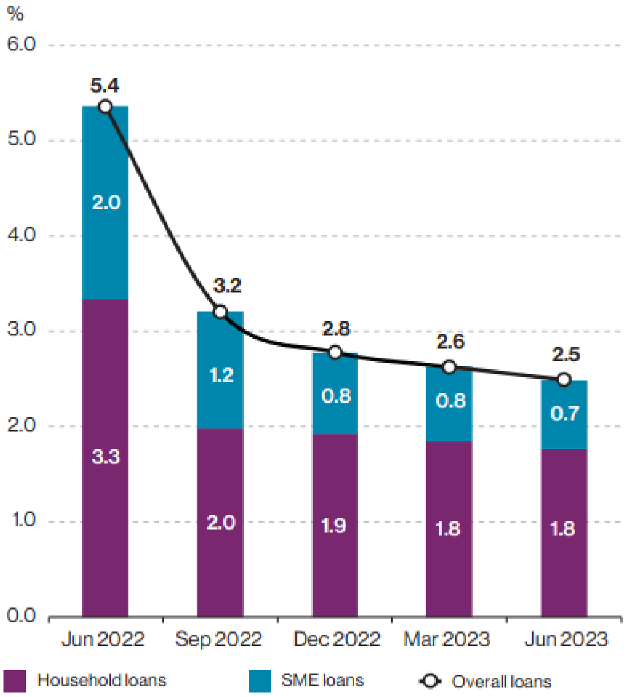
Be wary that smaller banks and Islamic banks see more pressure in this aspect



Source: BNM, MIDFR

Fig 16: % Loans under Repayment Assistance

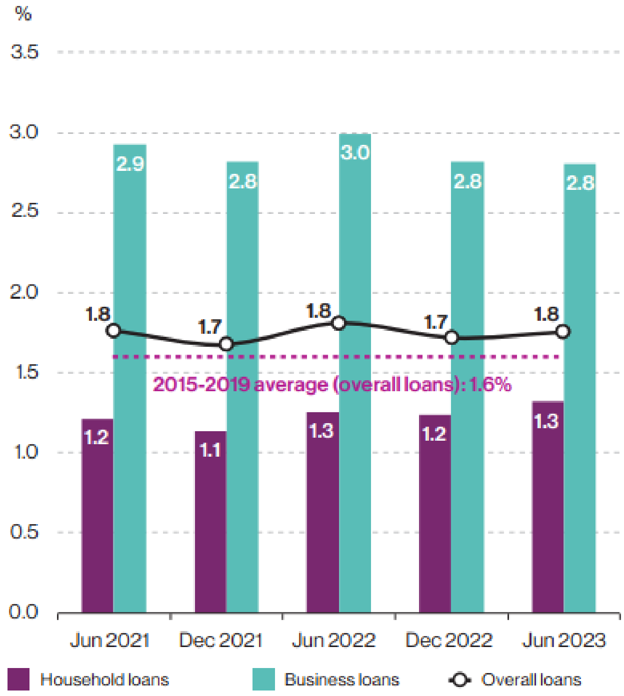
The good news is that reapplication rates are very low.



Source: BNM, MIDFR

Fig 17: GIL ratio

GIL ratio has been kept in check with heavy writedowns – but expect continued R&R impairments in future quarters.



Source: BNM, MIDFR

BNM hasn't made any changes to its previous Stress testing. We restate the highlights here:

Fig 18: BNM's stress testing verdict (Unchanged from 2H22)

STRESS TESTING	
Scenario 1 (AS1)	**Temporary but severe disruption:** V-shaped recovery in 2024 before normalisation.
Scenario 1 (AS2)	**Less severe but prolonged disruption:** Negative GDP growth in 2023 and 2024.
Impaired loans	Dec-22: 2.1%
AS1	Peak at 7.7% in Dec-25
AS2	Peak at 6.9% in Dec-25
CET 1	Dec-22: 14.6%
AS1	Trough at 12.5% in Dec-23
AS2	Trough at 12.8% in Dec-25
Total capital	Dec-22: 18.7%
AS1	Trough at 16.3% in Dec-25
AS2	Trough at 16.7% in Dec-23

Source: BNM, 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	Total return is expected to be <-10% 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.
ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell	
☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology