

SECTOR UPDATE

Banking – Singapore

2Q23 Results Preview: Steady And Sturdy

We forecast that banks' 2Q23 earnings will be powered by strong yoy growth in net interest income, robust net trading income and disciplined cost containment. Asset quality and credit costs remain benign. We forecast net profit of S\$2,466m for DBS (+31% yoy but -4% qoq) and S\$1,722m for OCBC (+16% yoy but -8% qoq). Our top picks are OCBC (BUY/Target: S\$17.50), followed by DBS (BUY/Target: S\$41.50). OCBC provides attractive 2023/24 dividend yield of 5.9%/6.3%. Maintain OVERWEIGHT.

WHAT'S NEW

- UOB will be announcing its 2Q23 results on 27 July, followed by DBS Group Holdings (DBS) on 3 August and Oversea-Chinese Banking Corporation (OCBC) on 4 August.

DBS Group Holdings (DBS SP/BUY/S\$32.74/Target: S\$41.50)

- We forecast net profit to grow 31% yoy but recede 4% qoq to S\$2,466m in 2Q23. The strong yoy growth was powered by NIM expansion and robust non-interest income.
- Benefitting from higher interest rates.** We expect muted loan growth of 0.5% qoq and flat yoy in 2Q23 driven by non-trade corporate loans. We expect residential mortgages to be held back by customer repayments. NIM expanded by 53bp yoy but was stable qoq at 2.11% as higher cost of fixed deposits was offset by a rebound of 3M HIBOR in Hong Kong. We expect net interest income to grow 37% yoy.
- Fees & commission increased 5.5% yoy.** Contribution from wealth management dipped 5% qoq but increased 2% yoy to S\$345m due to a low base. Sentiment remains fragile and investors stayed on the sidelines. Contribution from cards increased 5% yoy due to a continued recovery in business and leisure travel.
- Delivering on cost discipline and efficiency.** Management guided for operating expenses to increase 9-10% and cost-to-income ratio to fall below 40% in 2023. We expect operating expenses to jump 13.7% yoy and cost-to-income ratio to slip lower to 39.3% in 2Q23 (2Q22: 43.9%).
- Asset quality remains benign.** We expect NPL formation to remain benign and NPL ratio to be stable at 1.1%. DBS has accumulated ample management overlay for general provisions of S\$2.1b set aside previously during the COVID-19 pandemic. We expect total provisions of S\$149m and credit cost of 14bp in 2Q23.
- We expect DBS to maintain its quarterly dividend at 42 S cents for 2Q23.
- Our target price of S\$41.50 is based on 1.90x 2023F P/B, derived from Gordon Growth Model (ROE: 17.1%, COE: 9.0%, Growth: 0.0%).

Oversea-Chinese Banking Corporation (OCBC SP/BUY/S\$12.67/Target: S\$17.50)

- We forecast net profit to grow 16% yoy but recede 8% qoq to S\$1,722m for 2Q23. The healthy growth was powered by NIM expansion on a yoy basis, stringent cost discipline and benign asset quality and credit costs.

PEER COMPARISON

| Company | Ticker | Rec | Price @ 19 Jul 23 (\$) | Target Price (\$) | Market Cap (US\$m) | FY | PE 2023F (x) | PE 2024F (x) | P/B 2023F (x) | P/B 2024F (x) | P/POP 2023F (x) | P/POP 2024F (x) | Yield 2023F (%) | Yield 2024F (%) | ROE 2023F (%) | ROE 2024F (%) |
|---------|---------|-----|------------------------|-------------------|--------------------|---------|--------------|--------------|---------------|---------------|-----------------|-----------------|-----------------|-----------------|---------------|---------------|
| DBS | DBS SP | BUY | 32.74 | 41.50 | 63,684 | 12/2022 | 8.8 | 8.7 | 1.49 | 1.37 | 7.2 | 7.1 | 5.2 | 5.6 | 16.7 | 16.0 |
| OCBC | OCBC SP | BUY | 12.67 | 17.50 | 42,951 | 12/2022 | 8.3 | 8.3 | 1.04 | 0.98 | 7.4 | 7.4 | 5.9 | 6.3 | 12.5 | 11.8 |
| UOB# | UOB SP | NR | 28.64 | n.a. | 36,164 | 12/2022 | 8.5 | 8.2 | 1.07 | 1.01 | 6.6 | 6.3 | 5.7 | 6.0 | 12.9 | 12.8 |
| Average | | | | | | | 8.5 | 8.4 | 1.20 | 1.12 | 7.1 | 6.9 | 5.6 | 6.0 | 14.0 | 13.5 |

Source: Bloomberg, UOB Kay Hian #Based on consensus estimate

OVERWEIGHT

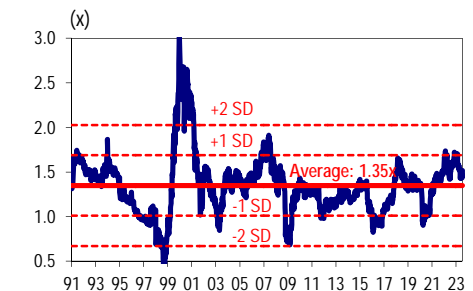
(Maintained)

SECTOR PICKS

| Company | Rec | Share Price (\$) | Target Price (\$) |
|---------|-----|------------------|-------------------|
| DBS | BUY | 32.74 | 41.50 |
| OCBC | BUY | 12.67 | 17.50 |

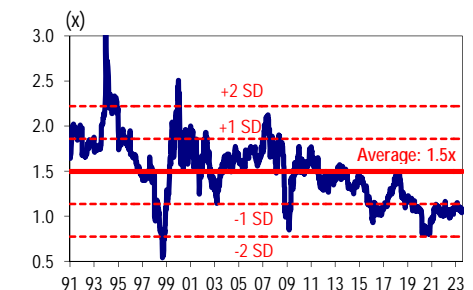
Source: UOB Kay Hian

P/B – DBS



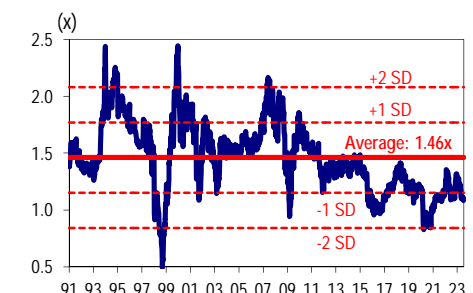
Source: UOB Kay Hian

P/B – OCBC



Source: UOB Kay Hian

P/B – UOB



Source: UOB Kay Hian

ANALYST(S)

Jonathan Koh, CFA, MSc Econ
+65 6590 6620
jonathankoh@uobkayhian.com

- **Strong growth in net interest income.** We expect loan growth to be muted at 0.2% qoq and flat on a yoy basis in 2Q23 as corporate customers are cautious on business expansion. We expect NIM to expand by 53bp yoy but compress 6bp qoq to 2.24% as cost of fixed deposits is re-priced higher. Net interest income is expected to grow by a sizeable 35% yoy.
- **Contribution from wealth management remains soft.** We expect fee income to dip 4% yoy in 2Q23. Contribution from wealth management is expected to be lacklustre and decline 12% yoy as market sentiment remains fragile. Loans and trade-related fees are expected to be stable.
- **Stable contributions from insurance without swings from mark-to-market.** We expect contribution from the insurance business at a normalised level of S\$230m in 2Q23. The adoption of SFRS(I) 17 has moved mark-to-market for insurance assets and liabilities to fair value through other comprehensive income (direct to balance sheet), which stabilise and lower the fluctuation of Great Eastern's contribution to OCBC's profit & loss going forward.
- **Asset quality remains stable.** We expect NPL ratio to be stable at 1.1%. OCBC has conducted a review of its macro-economic variable (MEV) model for general provisions in 2Q23. We have factored in credit costs of 20bp in 2Q23, which is at the top-end of management's guidance of 15-20bp for 2023.
- Our target price of S\$17.50 is based on 1.43x 2023F P/B, derived from the Gordon Growth Model (ROE: 12.9%, COE: 9.0%, Growth: 0.0%).

ACTION

- **Higher interest rates for a longer time frame.** The Fed kept interest rates unchanged at the FOMC meeting on 14 Jun 23 but signalled more upcoming rate hikes. The dot plot indicates another two rate hikes of 25bp each to bring Fed Funds Rate to 5.50% by end-23. Fed chairman Jerome Powell said he does not anticipate core inflation to return to the Fed's target of 2% until 2025, which suggests that interest rates could stay higher for a longer time frame.
- **Banks as proxy to growth in ASEAN countries.** ASEAN countries have a large combined population of 680m and account for about 8% of global exports. Many multinational companies have adopted the China +1 strategy and plan to set up alternative production facilities within the ASEAN region. Malaysia, Thailand, Indonesia and Vietnam are seeing growth in Foreign Direct Investments. OCBC and UOB benefit from the reorientation of supply chain due to their extensive network within ASEAN countries.
- **Maintain OVERWEIGHT.** Banks provide attractive value proposition with low P/B of 1.20x, low PE of 8.5x and sustainably high yield of 5.6% for 2023. Our top BUY pick is OCBC (Target: S\$17.50) for its new dividend policy with payout ratio at 50%, focus on ASEAN and defensively low P/B of 1.04x. We like DBS (Target: S\$41.50) due to its excellence in execution and it consistently delivering good results.

PROJECTED DPS AND DIVIDEND PAYOUT RATIOS

| | DBS | | | OCBC | | | UOB# | | |
|--------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Price (S\$) | 32.74 | | | 12.67 | | | 28.64 | | |
| Year to 31 Dec | FY22 | FY23F | FY24F | FY22 | FY23F | FY24F | FY22 | FY23F | FY24F |
| EPS (S c) | 315 | 372 | 377 | 127 | 153 | 153 | 269 | 336 | 351 |
| DPS (S c) | 200 | 171 | 182 | 68 | 75 | 80 | 135 | 163 | 172 |
| Payout Ratio (%) | 63.5 | 45.9 | 48.3 | 53.5 | 48.9 | 52.3 | 50.1 | 48.6 | 48.9 |
| Dividend Yield (%) | 6.1 | 5.2 | 5.6 | 5.4 | 5.9 | 6.3 | 4.7 | 5.7 | 6.0 |

Based on consensus estimate
Source: UOB Kay Hian

PROFIT & LOSS-FORECAST FOR DBS (2023)

| Profit & Loss (\$m) | 2023F | 2022 | yoy % chg | 1Q23 | qoq % chg |
|---------------------------|---------|---------|-----------|---------|-----------|
| Net Interest Income | 3,361 | 2,454 | 37.0 | 3,271 | 2.7 |
| Fees & Commissions | 810 | 768 | 5.5 | 851 | -4.8 |
| Other Non-Interest Income | 620 | 571 | 8.6 | 814 | -23.8 |
| Total Income | 4,791 | 3,793 | 26.3 | 4,936 | -2.9 |
| Operating Expenses | (1,885) | (1,658) | 13.7 | (1,882) | 0.1 |
| PPoP | 2,906 | 2,135 | 36.1 | 3,054 | -4.8 |
| Provisions | (149) | (45) | 230.5 | (161) | -7.6 |
| Associates | 55 | 65 | n.m. | 63 | -12.7 |
| PBT | 2,812 | 2,155 | 30.5 | 2,956 | -4.9 |
| Net Profit | 2,466 | 1,882 | 31.0 | 2,571 | -4.1 |
| EPS (S cents) | 94.7 | 70.0 | 35.3 | 100.5 | -5.8 |
| DPS (S cents) | 42.0 | 36.0 | 16.7 | 42.0 | 0.0 |
| BVPS (S\$) | 21.01 | 20.78 | 1.1 | 21.41 | -1.9 |

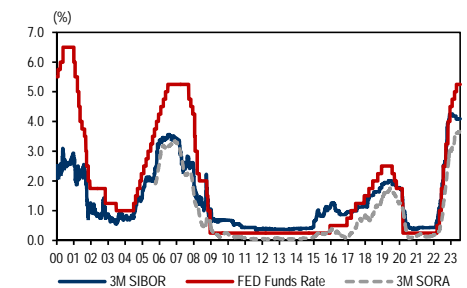
Source: UOB Kay Hian

PROFIT & LOSS-FORECAST FOR OCBC (2023)

| Profit & Loss (\$m) | 2023F | 2022 | yoy % chg | 1Q23 | qoq % chg |
|---------------------------|---------|---------|-----------|---------|-----------|
| Net Interest Income | 2,290 | 1,700 | 34.7 | 2,338 | -2.1 |
| Fees & Commissions | 457 | 477 | -4.3 | 453 | 0.8 |
| Insurance | 230 | 423 | -45.6 | 238 | -3.4 |
| Net Trading Income | 180 | 267 | -32.6 | 251 | -28.3 |
| Other Non-Interest Income | 60 | 12 | 400.0 | 70 | -14.3 |
| Total Income | 3,217 | 2,879 | 11.7 | 3,350 | -4.0 |
| Operating Expenses | (1,279) | (1,279) | 0.0 | (1,269) | 0.8 |
| PPoP | 1,937 | 1,600 | 21.1 | 2,081 | -6.9 |
| Provisions | (147) | (72) | 104.6 | (110) | 33.9 |
| Associates | 262 | 245 | 7.0 | 260 | 0.8 |
| PBT | 2,052 | 1,773 | 15.7 | 2,231 | -8.0 |
| Net Profit | 1,722 | 1,481 | 16.3 | 1,879 | -8.3 |
| EPS (S cents) | 38.4 | 32.8 | 17.2 | 42.0 | -8.6 |
| DPS (S cents) | 35.0 | 28.0 | 25.0 | 0.0 | n.m. |
| BVPS (S\$) | 11.83 | 11.37 | 4.1 | 11.58 | 2.2 |

Source: UOB Kay Hian

US FED FUNDS RATE VS 3M SIBOR AND 3M SORA



Source: Bloomberg

ASSUMPTION CHANGES

- We forecast earnings growth of 17.3% for DBS in 2023.

KEY ASSUMPTIONS – DBS

| | 2021 | 2022 | 2023F | 2024F | 2025F |
|-------------------|-------|--------|-------|-------|--------|
| Loan Growth (%) | 9.9 | 1.3 | 3.1 | 4.9 | 4.9 |
| NIM (%) | 1.45 | 1.75 | 2.12 | 2.09 | 1.99 |
| Fees, % Chg | 15.2 | (12.3) | 12.7 | 10.5 | 7.6 |
| NPL Ratio (%) | 1.27 | 1.13 | 1.25 | 1.31 | 1.33 |
| Credit Costs (bp) | 0.6 | 5.4 | 18.3 | 22.1 | 22.1 |
| Net Profit (\$m) | 6,802 | 8,262 | 9,695 | 9,820 | 10,008 |
| % Chg | 44.1 | 21.5 | 17.3 | 1.3 | 1.9 |

Source: UOB Kay Hian

- We forecast earnings growth of 19.6% for OCBC in 2023.

KEY ASSUMPTIONS – OCBC

| | 2021 | 2022 | 2023F | 2024F | 2025F |
|-------------------|-------|--------|-------|-------|-------|
| Loan Growth (%) | 8.6 | 1.8 | 1.8 | 4.4 | 4.8 |
| NIM (%) | 1.55 | 1.91 | 2.23 | 2.16 | 2.06 |
| Fees, % Chg | 12.0 | (17.6) | 1.2 | 5.8 | 6.2 |
| NPL Ratio (%) | 1.45 | 1.15 | 1.36 | 1.46 | 1.45 |
| Credit Costs (bp) | 31.3 | 20.0 | 19.7 | 22.5 | 23.3 |
| Net Profit (\$m) | 4,858 | 5,748 | 6,876 | 6,864 | 6,966 |
| % Chg | 35.4 | 18.3 | 19.6 | (0.2) | 1.5 |

Source: UOB Kay Hian

SECTOR CATALYSTS

- Economic recovery driven by the reopening and easing of COVID-19 restrictions, including the ongoing reopening in China.
- Banks reviewing their dividend policy and paying more dividends.

RISKS

- Escalation of the Russia-Ukraine war beyond Ukraine.
- Geopolitical tension and trade conflict between the US, EU and China.

3M LIBOR AND 3M HIBOR



Source: Bloomberg

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