SECTOR UPDATE

Banking – Malaysia

Lacking Fresh Catalysts

The sector delivered a robust earnings growth of 17% yoy in 2Q23 on lower tax, provisions, and strong non-interest income growth. However, with sector valuations near historical mean and earnings expected to trail the FBMKLCI, we see a fair risk-to-reward balance given the absence of new catalysts. In 2024, we anticipate stable NIM and slowing loan growth. Maintain MARKET WEIGHT. Our two sector top picks are CIMB and Public Bank.

WHAT'S NEW

- **2Q23 sector earnings broadly in line: RHB and Alliance disappointed.** Malaysian banks reported results that were broadly in line, whereby seven out of the nine banks we cover reported in-line earnings. Alliance and RHB disappointed on weaker-than-expected NIM. Maybank and CIMB printed above-average earnings growth (+34-45%), led by smaller bond impairment and strong non-interest income.

- **Earnings flat if we exclude base effect of prosperity tax.** 2Q23 sector earnings grew by 17.0% yoy, primarily due to the absence of the prosperity tax. However, 2Q23 PBT remained relatively unchanged yoy, resulting in a modest 1.7% yoy growth in 1H23 PBT (compared to 11.5% yoy growth in 1H22). On a qoq comparison, a strong 18% growth in non-interest income was balanced out by a 5bp NIM compression, a 45% qoq increase in provisions, and higher operating expenses.

- **Negative yoy operating JAWS.** The sector saw a negative yoy operating JAWS in 2Q22, with opex growing faster at 7.3% compared with revenue growth at 3.8%. The main factor behind this was a 21bp yoy reduction in NIM, which impacted revenue. However, a 27.7% yoy increase in non-interest income, primarily due to stronger trading-related income, helped offset the NIM decline.

- **CIMB was the outright earnings outperformer.** Among the banks, CIMB posted the most robust yoy earnings growth (+38.4% yoy) and revenue growth (+8% yoy), outperforming the sector's earnings growth of 17.0% yoy and revenue growth of 3.8% yoy. This was driven by strong non-interest income growth (+36.9% yoy) and solid cost discipline with opex rising at only 4.6% yoy vs sector's 7.3% yoy growth. Additionally, CIMB achieved a positive operating JAWS, with revenue surpassing opex growth by 4ppt in contrast to the sector's negative operating JAWS.

- **Earnings outlook to lag broader market.** Excluding the impact of the prosperity tax base effect, the sector is projected to achieve a modest 3% earnings growth in 2023, followed by a recovery to 7% in 2024. However, it is worth noting that this lags our 2024 11% earnings growth estimate for the KLCI. There is also potential downside risk in the form of lower-than-expected NIM and higher opex due to IT costs.

MARKET WEIGHT

(Maintained)

TOP SECTOR PICKS

Company	Rec	Target Price (RM)	Share Price (RM)
Public Bank	BUY	5.10	4.25
CIMB Group	BUY	6.00	5.74

Source: UOB Kay Hian

BANKS' 2Q23 RESULTS CORE NET PROFIT

Company	2Q23 (RMm)	yoy % chg	qoq % chg	Results
Affin	113.2	(22.9)	(23.9)	In-line
Alliance	150.5	(29.0)	15.7	Below
AMMB	378.4	(7.8)	(11.6)	In-line
BIMB	136.1	16.2	15.3	In-line
CIMB	1,773.7	38.5	7.8	In-line
HLBK	864.7	(4.7)	(7.0)	In-line
MBB	2,338.6	45.4	3.2	In-line
PBK	1,618.6	14.2	(5.6)	In-line
RHBC	808.7	28.4	6.2	Below

Source: Bloomberg, UOB Kay Hian

BANKS' SHARE PRICE PERFORMANCE

Company	Price (RM)	yoy % chg	ytd % chg
Maybank	9.17	2.7	5.4
Affin	2.07	6.0	2.0
CIMB Group	5.74	6.3	(1.0)
Public Bank	4.25	(8.4)	(1.6)
RHB Bank	5.68	(1.6)	(1.9)
HLFG	18.00	(5.7)	(3.2)
HL Bank	19.80	(5.2)	(3.7)
Alliance Bank	3.40	(8.6)	(7.4)
AMMB	3.67	(9.4)	(11.4)
Bank Islam	2.12	(16.5)	(22.3)

Source: Bloomberg

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PEER COMPARISON

Company	Ticker	Rec	Share Price (RM)	Target Price (RM)	Market Cap (US$m)	PE (x) 2022	PE (x) 2023F	PE (x) 2024F	ROE 2023F (%)	P/B 2023F (x)	Div 2023F (sen)	Div Yield (%)
Public Bank	PBK MK	BUY	4.25	5.10	17,637	12.5	12.3	11.6	13.1	1.6	17.3	4.1
CIMB Group	CIMB MK	BUY	5.74	6.00	13,088	10.9	9.4	8.7	9.8	0.9	30.5	5.3
HLFG	HLFG MK	HOLD	18.00	19.86	4,407	7.4	7.0	6.6	10.7	0.7	50.2	2.8
Maybank	MAY MK	HOLD	9.17	9.00	23,632	12.5	11.3	10.7	10.4	1.2	60.6	6.6
HL Bank	HLBK MK	HOLD	19.80	21.74	9,176	10.8	10.3	9.5	11.3	1.1	67.2	3.4
RHB Bank	RHBBANK MK	HOLD	5.68	6.10	5,205	7.7	8.3	7.9	9.1	0.7	37.5	6.6
AMMB	AMM MK	HOLD	3.67	4.00	2,597	6.6	7.3	6.8	9.0	0.6	22.2	6.1
Alliance Bank	ABMB MK	HOLD	3.40	3.80	1,125	7.8	8.0	7.4	9.5	0.7	21.2	6.2
Affin	ABANK MK	HOLD	2.07	2.14	1,038	23.0	8.0	7.5	4.6	0.4	11.6	5.6
Bank Islam	BIMB MK	HOLD	2.12	1.95	1,027	8.9	9.1	8.9	7.0	0.6	10.5	4.9

Source: Bloomberg, UOB Kay Hian

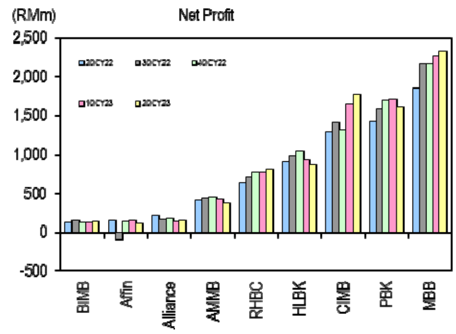
ACTION

- **Maintain MARKET WEIGHT.** We find current sector valuations, at -0.5 SD from the historical mean, fair considering the absence of new catalysts. NIM is predicted to remain flattish, with downside risks, and loan growth is expected to slow down. On the balance, overall, sector dividend yields are attractive, surpassing 5%, and credit costs are anticipated to decrease, albeit at a more modest rate.
- **Top picks.** Public Bank for its high provision buffers providing scope for potential provision write-backs when macroeconomic conditions permit, and CIMB given its strong earnings growth and it being a proxy to potential emerging market inflows.

ESSENTIALS

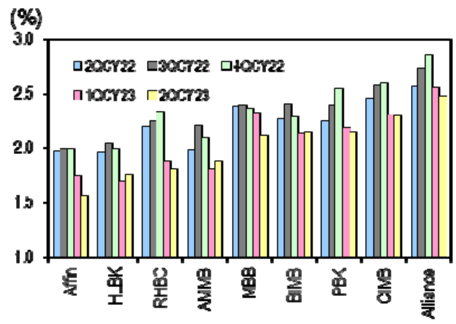
- **Easing NIM compression a silver lining.** Encouragingly, there was an improvement in sequential NIM compression (2Q23: -5bp vs 1Q23: -27bp) on easing deposit competition. Coupled with robust growth in non-interest income, this led to positive qoq operating JAWS in 2Q23. We anticipate a sector-wide NIM compression of 18bp in 2023, and NIM to remain flat in 2024.
- **NIM to remain below pre-pandemic levels.** Despite the Overnight Policy Rate (OPR) having normalised upwards to pre-pandemic levels, the sector's average NIM of 2.04% in 2Q23 remains below the pre-pandemic range of 2.10% to 2.20%. While we anticipate a modest NIM recovery in 4Q23, several factors are expected to limit further improvement into 2024. These include: a) no expected OPR hikes, b) competition in deposits from digital banks, and c) the potential for further normalisation of CASA ratio from 29% to the pre-pandemic average of 26%. Currently, we have factored in a stable NIM trend in 2024 compared to 2023, but due to these factors, there may be a slight downside risk to our 2024 NIM forecast.
- **GIL ratio remains fairly benign.** Aggregate sector GIL ratio for banks under our coverage increased slightly to 1.66% in 2Q23 from 1.63% in 1Q23, after reaching a low of 1.52% in 4Q22. Despite this uptick, 2Q23;s GIL ratio of 1.66% remains relatively low, well below the pre-pandemic level of 1.90%.
- **Partially supported by higher write-offs.** The fairly benign GIL ratio trends can be partially attributed to higher GIL write-offs by a number of banks, notably Maybank, RHB and Alliance. Annualised aggregate sector impaired loans write-off stood at 48bp in 1H23 vs 40bp in 2019.
- **Adequate provision buffers; expecting a slight improvement in credit cost.** Despite the anticipation of a further increase in GIL, we continue to expect a slight decline in sector net credit costs, going from 27bp in 2023 to 25bp in 2024. This expectation is based on the fact that banks have already allocated sufficient pre-emptive provisions. For instance, the aggregate loans loss coverage (LLC) ratio, which includes regulatory reserves for banks in our coverage, currently stands at 142% as of end-2Q23, surpassing pre-pandemic average levels of 117%. Public Bank leads with the highest ratio at 226%.
- **Minimal writebacks factored into our 2024 provisions forecast.** Our 2023/24 sector net credit cost assumptions of 29bp/25bp are near the pre-COVID-19 average of 25bp. This suggests that we have not accounted for a significant reversal in excess provisions even through to 2024, as we prefer a cautious approach due to the delayed effects of interest rate normalization and macroeconomic slowdown on GIL formation. If any reversals occur, we believe Public Bank has the most potential for writebacks given its robust LLC.
- **Loans and deposit growth holding steady but growth to moderate.** 2Q23 sector aggregate loan and deposit growth remained stable at +6.4% yoy (compared to +6.5% in 1Q23) and +5.0% yoy (compared to +4.1% in 1Q23), respectively. Among these categories, the top four banks with the fastest growth rates were Affin, AMMB, HLBank and CIMB, showing increases ranging from 13% to 8%. However, moving forward, we expect loans growth to taper off in 2024 on the back of softer macroeconomic conditions and higher interest rates.

BANKS' NET PROFIT TREND



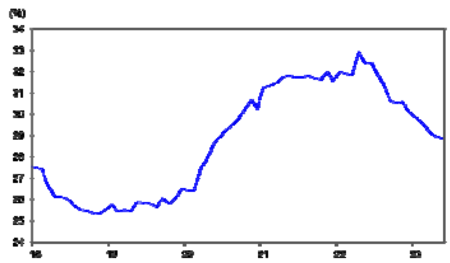
Source: Respective companies, UOB Kay Hian,

BANKS' NIM TRENDS



Source: Respective companies, UOB Kay Hian

SECTOR CASA RATIO



Source: BNM, UOB Kay Hian

SECTOR P/B

Source: Respective companies, UOB Kay Hian

BANKS' FY23 GUIDANCE

Bank	Group loans growth (%)	Deposits growth (%)	ROE (%)	NIM (bp)	Credit cost (bp)	CIR (%)
Affin	10-11	n.a.	n.a.	-15	30	60
Alliance	8-10	n.a.	>10	-14-19	30-35	<48
AMMB	6-7	n.a.	9-10	Below 2%	35	<45
BIMB	7-8	n.a.	7-8	Above 2%	30-40	58
CIMB	6-7	n.a.	10.2-11	-15-20	40-50	<46.5
HLB	6-7	n.a.	~12	1.8-1.9%	~10	<40
Maybank	n.a.	n.a.	10.5-11	c.-25	30-35	<47.5
Public	4-5	4-5	12-13	<-20	<10	n.a.
RHB	4-5	n.a.	11	-34-44	High-teens	<44.6

Source: Respective companies, UOB Kay Hian

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