

SECTOR UPDATE

Banking – Singapore

Resiliency That Defies Gravity

The Fed has signalled another two rate hikes of 25bp each to bring Fed Funds Rate to 5.50% by end-23. Core inflation is receding very gradually and we expect interest rates to stay elevated till mid-24. 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 0.99x. We also like DBS (Target: S\$41.50) for excellence in execution and consistently delivering good results. Maintain OVERWEIGHT.

WHAT'S NEW

- 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. We expect interest rates to stay elevated till mid-24.
- US economy stays resilient despite the series of rate hikes.** The US economy has weathered higher interest rates, tightening of liquidity and fallout from the collapse of three regional banks. Labour market remains too tight with unemployment rate still low at 3.6% in Jun 23, near the historical low of 3.4% recorded in Apr 23. Lately, new single-family home sales and new construction activities have also surged in May 23.
- Sensitivity analysis.** We conducted a sensitivity analysis for the impact on 2025 financial performance, including net profit, ROE, DPS and dividend yield, from: a) fluctuation of Fed Funds Rate and NIM, and b) potential slowdown/recession and the resultant hit on credit costs. Assuming Fed Funds Rate at 5.50%, a deterioration of credit costs from 20bp to 90bp would cause DBS' and OCBC's net profit to drop 25.1% and 24.7% respectively. Assuming credit costs at 20bp, a cut in Fed Funds Rate from 5.50% to 4.50% would cause DBS' and OCBC's net profit to drop 6.1% and 5.1% respectively.
- Asset quality – Withstood test from COVID-19 pandemic.** The three Singapore banks have weathered the COVID-19 pandemic with NPL ratio deteriorating on average by just 0.1ppt. DBS' and OCBC's NPL ratios have slipped 0.2ppt to a similar 1.1% over the past three quarters. Banks have ample management overlays for general provisions amounting to about S\$2,100m for DBS, S\$1,000m for OCBC and S\$1,400m for UOB.
- Capital adequacy – Among the safest in the world.** OCBC has the highest CET-1 CAR at 15.9% as of Mar 23, followed by DBS at 14.4%, far exceeding the minimum requirement of 9%. DBS is ranked 12th safest on a worldwide basis by Global Finance, followed by OCBC at 13th. Within Asia, the three Singapore banks are recognised as the top 3 safest ahead of banks in South Korea, Taiwan and Hong Kong.

Click [here](#) for Blue Top dated 12 Jul 23

PEER COMPARISON

Company	Ticker	Rec	Price @ 10 Jul 23 (S\$)	Target Price (S\$)	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	30.91	41.50	59,288	12/2022	8.4	8.1	1.41	1.30	6.9	6.6	5.5	5.9	16.6	16.2
OCBC	OCBC SP	BUY	12.09	17.50	40,414	12/2022	7.8	7.8	0.99	0.93	7.0	6.9	6.2	6.6	12.6	12.0
UOB#	UOB SP	NR	27.40	n.a.	34,121	12/2022	8.2	7.8	1.02	0.96	6.3	6.0	5.9	6.2	12.9	12.9
Average							8.1	7.9	1.14	1.06	6.7	6.5	5.9	6.2	14.0	13.7

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

OVERWEIGHT

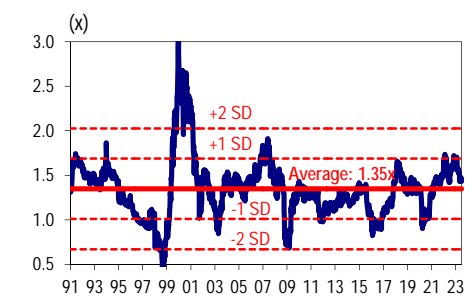
(Maintained)

SECTOR PICKS

Company	Rec	Share Price (S\$)	Target Price (S\$)
DBS	BUY	30.91	41.50
OCBC	BUY	12.09	17.50

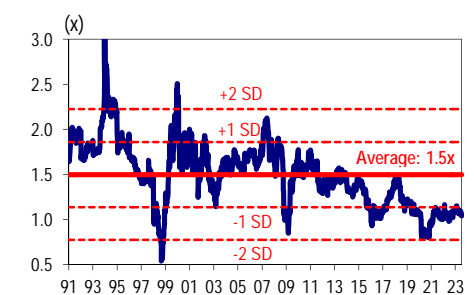
Source: UOB Kay Hian

P/B – DBS



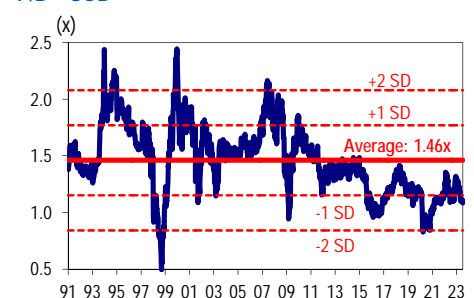
Source: UOB Kay Hian

P/B – OCBC



Source: UOB Kay Hian

P/B – UOB



Source: UOB Kay Hian

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ACTION

- **Maintain OVERWEIGHT.** Banks provide attractive value proposition with low P/B of 1.14x, low PE of 8.1x and sustainably high yield of 5.9% 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 0.99x. We also like DBS (Target: S\$41.50) for excellence in execution and consistently delivering good results.

PROJECTED DPS AND DIVIDEND PAYOUT RATIOS

	DBS			OCBC			UOB#		
Price (S\$)	30.91			12.09			27.40		
Year to 31 Dec	FY22	FY23F	FY24F	FY22	FY23F	FY24F	FY22	FY23F	FY24F
EPS (S c)	315	368	382	127	154	156	269	336	352
DPS (S c)	200	171	182	68	75	80	135	163	171
Payout Ratio (%)	63.5	46.5	47.7	53.5	48.7	51.4	50.1	48.4	48.6
Dividend Yield (%)	6.5	5.5	5.9	5.6	6.2	6.6	4.9	5.9	6.2

Based on consensus estimate
Source: UOB Kay Hian

ASSUMPTION CHANGES

- We trimmed our 2025 net profit forecast for DBS by 7% due to rate cuts of 100bp in 2H24 and credit costs of 31bp (previous: 22bp). 2025 DPS and dividend yield remain attractive at S\$1.88 and 6.1% respectively.

KEY ASSUMPTIONS – DBS

	2021	2022	2023F	2024F	2025F
Loan Growth (%)	9.9	1.3	3.4	4.9	4.9
NIM (%)	1.45	1.75	2.12	2.09	1.98
Fees, % Chg	15.2	(12.3)	15.4	9.1	7.6
NPL Ratio (%)	1.27	1.13	1.25	1.30	1.32
Credit Costs (bp)	0.6	5.4	20.3	22.1	30.7
Net Profit (S\$m)	6,802	8,262	9,579	9,936	9,703
% Chg	44.1	21.5	15.9	3.7	(2.4)

Source: UOB Kay Hian

- We trimmed our 2025 net profit forecast for OCBC by 7% due to rate cuts of 100bp in 2H24 and credit costs of 32bp (previous: 23bp). 2025 DPS and dividend yield remain attractive at S\$0.80 and 6.6% respectively.

KEY ASSUMPTIONS – OCBC

	2021	2022	2023F	2024F	2025F
Loan Growth (%)	8.6	1.8	4.0	4.4	4.8
NIM (%)	1.55	1.91	2.24	2.19	2.08
Fees, % Chg	12.0	(17.6)	1.5	5.8	6.2
NPL Ratio (%)	1.45	1.15	1.33	1.43	1.42
Credit Costs (bp)	31.3	20.0	20.3	22.5	31.8
Net Profit (S\$m)	4,858	5,748	6,910	6,984	6,855
% Chg	35.4	18.3	20.2	1.1	(1.8)

Source: UOB Kay Hian

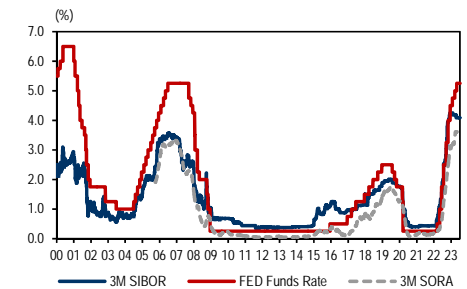
SECTOR CATALYSTS

- 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

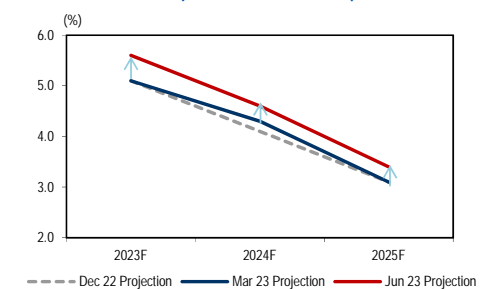
- Escalation of the Russia-Ukraine war beyond Ukraine.
- Geopolitical tension and trade conflict between the US, EU and China.

US FED FUNDS RATE VS 3M SIBOR



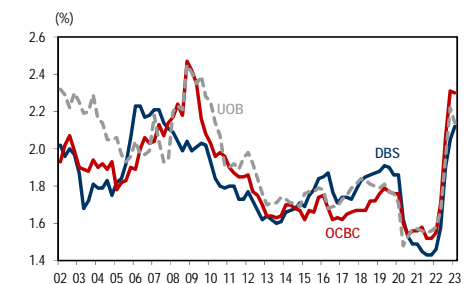
Source: Bloomberg

FED'S DOT PLOT (JUN 23 VS MAR 23)



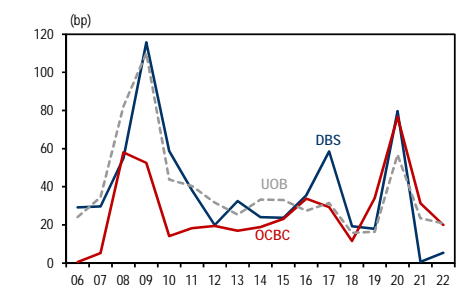
Source: Bloomberg

NET INTEREST MARGIN (NIM)



Source: Respective banks

CREDIT COSTS



Source: Respective banks

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