

## COMPANY UPDATE

### Public Bank (PBK MK)

Provision Buffers Capable Of Weathering Extreme Stress Conditions

We note that Public Bank has set aside extremely conservative pre-emptive provision buffers that are suited for extreme stress conditions. This places the group in an excellent position to weather the current economic downturn while benefitting from the recovery given ample scope for writebacks. In addition, valuations are attractive (-1SD to historical P/B mean). Maintain BUY with a higher target price of RM5.10 (1.87x 2023F P/B, ROE: 12.9%) from RM4.85 as we roll over our target price to 2023.

#### WHAT'S NEW

- **Repayment assistance expected to edge closer to pre-COVID-19 levels.** We expect Public Bank's domestic loans under repayment assistance (RA) to decline further to an estimated 3-4% of its domestic loans base (RM11b-17b) by 4Q22 vs 6% (RM20.8b) as at end-Jul 22. This is close to the group's pre-COVID-19 average restructuring and rescheduling (R&R) loan level of 1-2% (sector average: 2%).
- **Small percentage of loans under RA impaired.** Impaired RA loans are hovering at a relatively low 0.6% of RA loans, while RA loans that are overdue for more than one month remain stable at 5% of RA loans. As such, loans that are deemed to be potentially vulnerable could equate to only RM500m-700m (0.14-0.20% of total group loans) or a potential rise in group GIL ratio to 0.50% from the current 0.30%. This assumes that 5% of RA loans will be impaired vs the current run rate of only 0.6%.
- **Significant provision buffers built in.** Meanwhile, the group has set aside RM1.7b in pre-emptive provisions, which it has yet to consume vs RM500m-700m in what we have assessed to be vulnerable loans. Assuming a worst-case scenario where 5% of its RA loans are impaired (vs current 0.6%) while assigning a 22% loss given default (LGD) as the loans are largely collateralised against properties, we derive a potential excess provision of RM1.49b-1.55b. This implies a potential 22% accretion to our 2023 earnings forecast assuming a writeback of these assessed excess provisions. However, management remains conservative on its guidance of any potential writebacks for now.
- **Current pre-emptive provisions imply GIL ratio of up to 1.80%.** Should the group be required to consume all of its RM1.7b in pre-emptive provisions, we estimate that this would equate to a potential rise in group GIL ratio from the current 0.30% to 1.80% (six-fold increase in GIL ratio). Clearly, this shows that management has built in extremely conservative provisions buffers that would be akin to an extreme stress scenario. The group's GIL ratio was last at such levels in 2006.

#### KEY FINANCIALS

Year to 31 Dec (RMm)	2020	2021	2022F	2023F	2024F
Net interest income	7,180	8,315	8,671	9,269	9,862
Non-interest income	2,821	2,616	2,494	2,587	2,711
Net profit (rep./act.)	4,872	5,657	5,716	6,798	7,306
Net profit (adj.)	4,872	6,146	5,716	6,798	7,306
EPS (sen)	25.1	31.7	29.4	35.0	37.6
PE (x)	18.3	14.5	15.6	13.1	12.2
P/B (x)	1.9	1.8	1.8	1.7	1.6
Dividend yield (%)	2.8	3.3	3.2	3.8	4.1
Net int margin (%)	2.0	2.2	2.2	2.3	2.3
Cost/income (%)	34.6	31.6	32.4	32.2	31.8
Loan loss cover (%)	227.7	359.7	130.4	170.0	205.9
Consensus net profit	-	-	5,810	6,909	7,352
UOBKH/Consensus (x)	-	-	0.98	0.98	0.99

Source: Public Bank, Bloomberg, UOB Kay Hian

## BUY

(Maintained)

Share Price	RM4.59
Target Price	RM5.10
Upside	+5.7%
(Previous)	RM4.85)

#### COMPANY DESCRIPTION

Public Bank is the third-largest domestic banking group in Malaysia by assets with about 14.8% of system assets and 16.2% of loan market share.

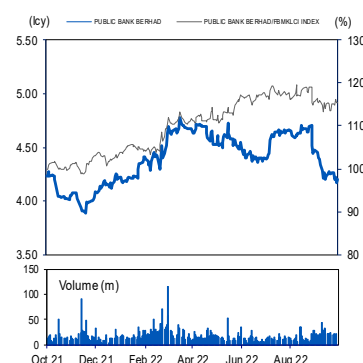
#### STOCK DATA

GICS sector	Financials
Bloomberg ticker:	PBK MK
Shares issued (m):	19,410.7
Market cap (RMm):	89,095.1
Market cap (US\$m):	20,387.9
3-mth avg daily t'over (US\$m):	26.0
<b>Price Performance (%)</b>	
52-week high/low	RM4.78/RM3.88

1mth	3mth	6mth	1yr	YTD
(2.1)	3.1	16.5	7.5	10.3

<b>Major Shareholders</b>	%
Tan Sri Dato' Sri Dr. Teh Hong Piow	21.6
EPF	15.2
-	-
FY22 NAV/Share (RM)	2.59
FY22 CAR Tier-1 (%)	15.12

#### PRICE CHART



Source: Bloomberg

#### ANALYST(S)

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• **Current credit cost assumptions are conservative as they remain above pre-COVID-19 levels.** Despite the very conservative pre-emptive provision buffers that the group has set aside, our 2022/23 net credit cost assumptions of 13bp/10bp respectively remain above its pre-COVID-19 average of 5-7bp. Management has retained its 2022 net credit cost guidance of 10-15bp.

• **Potential upside surprise to our NIM assumptions.** Management has retained its NIM expansion guidance of 8-10bp for 2022. It does not expect any further Overnight Policy Rate (OPR) hike for the rest of 2022, but expects a further 25bp OPR hike for 2023 that will bring OPR to 2.75%. In comparison, we expect two OPR hikes in 2023, which will bring OPR to 3.00% in 2023. Our NIM assumption remains conservative, as we pencil in a modest 2-3bp NIM expansion for 2022-23 vs management's 8-10bp guidance. Inherent in our NIM assumption is a certain degree of intensifying fixed deposit competition and downward normalisation in CASA growth. The group's average fixed deposit re-pricing tenure currently stands at six months. In terms of sensitivity, each 25bp OPR hike is expected to lift group NIM by 2bp and earnings by 1.5%.

• **Healthy loans approval pipeline to sustain current loans growth.** The group registered a commendable 1H22 group loans growth of 5.6%, above our full-year assumption of 4.5% yoy and management's guidance of 4.0-5.0%. Management alluded that loans application and approval pipeline remain healthy, and are sufficient to sustain current above-estimate loans growth momentum for the rest of 2022. Loans growth was supported largely by mortgages (+7.3% yoy) and auto loans (+10.2% yoy), while loans growth for non-residential property remains sluggish at 1.2% yoy.

• **Non-interest income visibility remains uncertain.** Non-interest income declined 15% yoy in 1H22, dragged by lower unit trust (-13% yoy), stockbroking (-51% yoy), trading and investment gains (-50% yoy) but partly offset by a 16% increase in commission and service fees. Moving into 2023, management indicated that wealth management and investment and trading income are likely to remain challenging with minimal opportunities to lock in gains on the fixed income front. Given the above, we do expect some downside risk to our current 2023 non-interest income growth forecast of 3.7%. That said, even if our current 2023 non-interest income growth forecast of 3.7% was to swing to a contraction of 6%, negative impact on our 2023 earnings forecast is a manageable 2.5%. As such, we have left our current non-interest income forecast unchanged for now.

• **2022 outlook.** Management's key 2022 key guidance has remained largely intact: a) loans growth: 4-5%, b) NIM: 5bp, c) net credit cost: 10-15bp, and d) ROE: 11-12%.

## EARNINGS REVISION/RISK

• Unchanged.

## VALUATION/RECOMMENDATION

• **Maintain BUY with a higher target price of RM5.10 (1.87x 2023F P/B, ROE: 12.9%)** which is in line with its historical mean P/B. Rolling forward our target price to 2023, we raise our target price to RM5.10 from RM4.85. Current P/B valuation of 1.55x values the stock at -1SD below its historical P/B mean, which we deem attractive given Public Bank's strong defensive qualities which should gain prominence in the current period of uncertainty. Public Bank also stands to benefit when macroeconomic conditions improve as it has the strongest headroom for potential provision writebacks.

## POTENTIAL EXCESS PROVISIONS ANALYSIS

Public Bank's Total Domestic Loans = RM343.6b

Repayment Assistance (RMm) (A)	Repayment Assistance to Domestic Loans (%)	Repayment Assistance >1 month overdue (%) (B)	Vulnerable Loans (RMm) (A x B)	LGD (%)
13,744	4.0%	5.0%	687.2	22%
10,308	3.0%	5.0%	515.4	22%

Provision required on uncollateralised (assuming 10% uncollateralised) (RMm) (A)	Provisions required on collateralised (assuming 90% collateralised) (RMm) (B)	Total potential assessed provisions required (RMm) (A + B)	Pre-Emptive Provisions Provided (RMm)	Potential Excess Provisions (RMm)
68.7	136.1	204.8	1,700	1,495
51.5	102.0	153.6	1,700	1,546

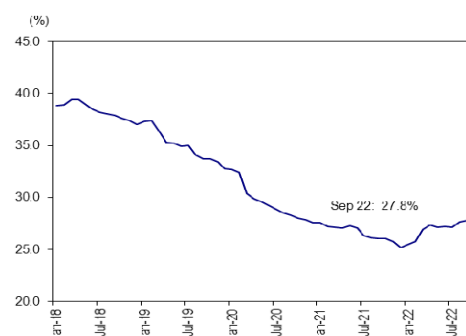
Source: Public Bank, UOB Kay Hian

## KEY ASSUMPTIONS

(%)	2022F	2023F	2024F
Loan Growth	4.5	5.2	5.8
Credit Cost (bp)	13.0	10.0	8.0
ROE	11.4	12.9	13.2

Source: UOB Kay Hian

## FOREIGN SHAREHOLDING



Source: UOB Kay Hian

## P/B BAND



Source: UOB Kay Hian, Bloomberg

## ENVIRONMENTAL, SOCIAL, GOVERNANCE (ESG) UPDATES

<b>Environmental</b> <ul style="list-style-type: none"> <li>Green loan commitment. Launched a campaign in 2020 offering preferential rates for selected energy efficient vehicle (EEV) under its AITAB Hire Purchase-i, to promote the usage of EEVs.</li> <li>Paperless initiative. Moving towards paperless operations with its enhanced Go Green initiatives in its daily operations, such as migrating reports to online verification module, issuing electronic statements and notices as well as introducing electronic signatures (eSignature) in new deposit account openings.</li> </ul>
<b>Social</b> <ul style="list-style-type: none"> <li>Board and upper management gender diversity. Maintained 33% female directors on the Board and 48% for Top and Senior Management.</li> </ul>
<b>Governance</b> <ul style="list-style-type: none"> <li>Non-independent board of directors composition. Composition of Independent Non-Executive Directors (INED) - 55%.</li> </ul>

Source: Public Bank, UOB Kay Hian

### PROFIT & LOSS

Year to 31 Dec (RMm)	2021	2022F	2023F	2024F
Interest income	13,475	13,974	14,783	15,623
Interest expense	(5,160)	(5,303)	(5,514)	(5,761)
Net interest income	8,315	8,671	9,269	9,862
Fees & commissions	2,147	1,932	2,009	2,110
Other income	469	561	578	601
Non-interest income	2,616	2,494	2,587	2,711
Income from islamic banking	1,614	1,694	1,779	1,868
<b>Total income</b>	<b>12,544</b>	<b>12,859</b>	<b>13,635</b>	<b>14,441</b>
Staff costs	(2,896)	(3,041)	(3,230)	(3,391)
Other operating expense	(1,069)	(1,119)	(1,160)	(1,203)
Pre-provision profit	8,579	8,699	9,246	9,847
Loan loss provision	(1,201)	(486)	(394)	(333)
Other provisions	(6)	0	0	0
Associated companies	(5)	(6)	(7)	(7)
Pre-tax profit	7,367	8,207	8,846	9,507
Tax	(1,637)	(2,421)	(1,965)	(2,112)
Minorities	(73)	(69)	(83)	(89)
<b>Net profit</b>	<b>5,657</b>	<b>5,716</b>	<b>6,798</b>	<b>7,306</b>
Net profit (adj.)	6,146	5,716	6,798	7,306

### BALANCE SHEET

Year to 31 Dec (RMm)	2021	2022F	2023F	2024F
Cash with central bank	1,222	11,224	11,807	12,492
Govt treasury bills & securities	22,653	23,106	23,568	24,039
Interbank loans	0	0	0	0
Customer loans	354,052	370,061	390,111	413,547
Investment securities	57,779	62,182	66,888	71,915
Derivative receivables	140	234	327	420
Associates & JVs	115	133	147	162
Fixed assets (incl. prop.)	1,325	1,525	1,725	1,925
Other assets	25,453	25,975	26,976	28,022
<b>Total assets</b>	<b>462,739</b>	<b>494,440</b>	<b>521,549</b>	<b>552,522</b>
Interbank deposits	8,124	6,144	4,646	3,514
Customer deposits	380,394	394,849	410,643	429,122
Derivative payables	254	229	206	185
Debt equivalents	0	0	0	0
Other liabilities	24,542	41,591	51,836	62,711
<b>Total liabilities</b>	<b>413,314</b>	<b>442,813</b>	<b>467,331</b>	<b>495,532</b>
Shareholders' funds	48,163	50,295	52,803	55,487
Minority interest - accumulated	1,263	1,332	1,415	1,503
<b>Total equity &amp; liabilities</b>	<b>462,739</b>	<b>494,440</b>	<b>521,549</b>	<b>552,522</b>

### OPERATING RATIOS

Year to 31 Dec (%)	2021	2022F	2023F	2024F
<b>Capital Adequacy</b>				
Tier-1 CAR	14.6	15.1	15.0	14.9
Total CAR	17.6	17.6	17.4	17.2
Total assets/equity (x)	9.6	9.8	9.9	10.0
Tangible assets/tangible common equity (x)	10.1	10.3	10.4	10.5
<b>Asset Quality</b>				
NPL ratio	0.3	0.8	0.5	0.3
Loan loss coverage	359.7	130.4	170.0	205.9
Loan loss reserve/gross loans	1.1	1.1	0.9	0.7
Increase in NPLs	(11.9)	182.9	(34.5)	(31.9)
Credit cost (bp)	33.7	13.0	10.0	8.0
<b>Liquidity</b>				
Loan/deposit ratio	93.1	93.7	95.0	96.4
Liquid assets/short-term liabilities	6.1	8.6	8.5	8.4
Liquid assets/total assets	5.2	6.9	6.8	6.6

### KEY METRICS

Year to 31 Dec (%)	2021	2022F	2023F	2024F
<b>Growth</b>				
Net interest income, yoy chg	15.8	4.3	6.9	6.4
Fees & commissions, yoy chg	11.3	(10.0)	4.0	5.0
Pre-provision profit, yoy chg	15.9	1.4	6.3	6.5
Net profit, yoy chg	16.1	1.1	18.9	7.5
Net profit (adj.), yoy chg	26.1	(7.0)	18.9	7.5
Customer loans, yoy chg	3.3	4.5	5.4	6.0
Customer deposits, yoy chg	4.0	3.8	4.0	4.5
<b>Profitability</b>				
Net interest margin	2.2	2.2	2.3	2.3
Cost/income ratio	31.6	32.4	32.2	31.8
Adjusted ROA	1.3	1.2	1.3	1.4
Reported ROE	11.9	11.6	13.2	13.5
Adjusted ROE	12.9	11.6	13.2	13.5
<b>Valuation</b>				
P/BV (x)	1.8	1.8	1.7	1.6
P/NTA (x)	1.9	1.9	1.8	1.7
Adjusted P/E (x)	14.5	15.6	13.1	12.2
Dividend Yield	3.3	3.2	3.8	4.1
Payout ratio	52.2	50.0	50.0	50.0

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