

COMPANY RESULTS

Hong Leong Bank (HLBK MK)

1QFY23: Solid Performance Priced In

Hong Leong Bank reported 1QFY23 earnings that were broadly in line. Despite the solid performance, we are downgrading our call to a HOLD from a BUY with a lower target price of RM23.30 (1.46x FY23F P/B, 11.3% ROE) from RM24.00 on lower NIM outlook and valuation grounds. The stock is trading at its historical mean P/B of 1.30x. Given that our target price implies +1.0SD to its historical mean P/B, we think we have adequately priced in the stock's solid defensive qualities.

RESULTS

- **1QFY23 results: In line.** Hong Leong Bank (HL Bank) reported 1QFY23 earnings of RM981.4m (+14.3% yoy, +8.9% qoq). 1QFY23 earnings were in line, representing 25% of our full year FY23 earnings forecast.
- **YOY.** The group reported a 14.3% yoy increase in 1QFY23 earnings supported by: a) strong 8.8% loans growth, b) 5bp NIM expansion, c) 21% yoy increase in contribution from associate Bank of Chengdu, and d) lower net credit cost of 9bp vs 13bp in 1QFY22. The group also delivered positive operating Jaws with revenue rising 2ppt faster than opex.
- **QOQ.** 1QFY23 earnings rose 8.9% qoq largely due to the absence of the prosperity tax. PBT declined 2.5% qoq on: a) lower contributions from associate Bank of Chengdu (-14.2% qoq), b) +2bp qoq increase in net credit cost, and c) continued weakness in trading income (-38% qoq). This was partially offset by an 8bp qoq increase in NIM.
- **NIM rose 8bp qoq to 2.18%** as the group had optimised its loans to deposit ratio (LDR) with deposits shrinking 0.3% qoq vs loans growth of 0.7% qoq. Management guided for full-year FY23 NIM of 2.14% (FY22: 2.14%) which implies that sequential NIM is likely to taper off from 1QFY23. Inherent in our assumptions is a more conservative 2bp compression for FY23 vs management's expectation of a flattish trend. Management expects a single 25bp OPR hike in 2023.
- **Loans growth remained above industry's growth.** Loans growth remained robust at 8.8% yoy. Loans growth was driven largely by SME (+14.5% yoy), mortgages (+8.4% yoy) and auto loans (+10.1% yoy). We have conservatively pencilled in a 6.3% yoy FY23 loans growth assumption, which is slightly below management's 7.0-7.5% growth guidance.

STOCK IMPACT

- **Targeted assistance loans continued to decline.** Total loans under targeted assistance declined to less than 1.0% of the group's total loans base from 2.6% of gross loans in Jul 22. Retail loans formed the bulk of the loans under repayment assistance and were largely within the mortgage space.

KEY FINANCIALS

Year to 30 Jun (RMm)	2020	2021	2022F	2023F	2024F
Net interest income	2,764	3,458	3,756	3,874	4,028
Non-interest income	1,167	1,090	937	979	1,020
Net profit (rep./act.)	2,495	2,861	3,289	3,760	3,985
Net profit (adj.)	2,495	2,861	3,289	3,760	3,985
EPS (sen)	120.0	137.6	158.2	180.8	191.7
PE (x)	17.4	15.2	13.2	11.5	10.9
P/B (x)	1.6	1.5	1.4	1.3	1.2
Dividend yield (%)	1.7	2.4	2.6	3.0	3.2
Net int margin (%)	1.8	2.0	2.0	2.0	2.0
Cost/income (%)	44.0	38.0	37.5	37.6	37.6
Loan loss cover (%)	141.5	246.6	211.8	142.4	118.5
Consensus net profit	-	-	3,808	4,067	4,414
UOBKH/Consensus (x)	-	-	0.86	0.92	0.90

Source: Hong Leong Bank, Bloomberg, UOB Kay Hian

HOLD

(Downgraded)

Share Price	RM20.88
Target Price	RM23.30
Upside	+11.6%
(Previous TP)	RM24.00

COMPANY DESCRIPTION

This is fourth largest bank in term of asset size focusing on retail banking with presence in China through 20%-owned Bank of Chengdu.

STOCK DATA

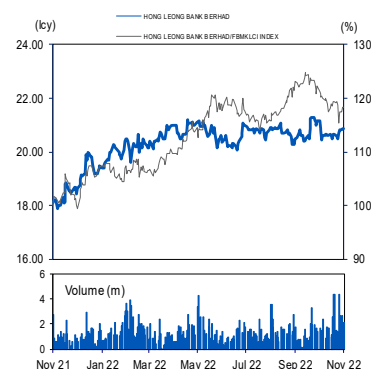
GICS sector	Financials
Bloomberg ticker:	HLBK MK
Shares issued (m):	2,167.7
Market cap (RMm):	45,262.0
Market cap (US\$m):	10,039.7
3-mth avg daily t'over (US\$m):	7.0
Price Performance (%)	

52-week high/low			RM21.30/RM17.86	
1mth	3mth	6mth	1yr	YTD
(1.2)	0.4	(0.6)	14.7	12.1

Major Shareholders

	%
Hong Leong Financial Group Berhad	61.8
Employees Provident Fund Board	9.2
-	-
FY23 NAV/Share (RM)	15.99
FY23 CAR Tier-1 (%)	14.45

PRICE CHART



Source: Bloomberg

ANALYST(S)

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- **GIL remained benign.** Asset quality remained benign with GIL ratio remaining stable at 0.49% in 1QFY23 while loans loss coverage ratio was also stable at 212%.
- **Robust provision buffers built in.** Given the robust provision buffers, management indicated that no further management overlays will be required for now. Management has narrowed the range of it FY23 net credit cost guidance to 10bp from 10-15bp. This is broadly in line with our 10bp assumption. The group's stock of pre-emptive provision remains unchanged at RM629m in 1QFY23.
- **Strong performance from Bank of Chengdu.** 1QFY23 contribution from Bank of Chengdu grew 21% yoy. The strong growth was underpinned by 31% loans growth and lower credit cost as GIL ratio declined by 25bp yoy to 0.81%. Loans loss coverage ratio was also robust at 498%.
- **FY23 guidance.** Management's key FY23 guidance are as follows: a) 10bp net credit cost, b) GIL ratio to remain below 0.75%, c) above industry loans growth of 7-7.5%, d) cost-to-income ratio of 36%, and e) ROE of above 12%. Management's FY23 guidance is slightly more optimistic than our assumptions as we have pencilled in a more conservative loans growth of 6.3% and NIM compression of 2bp vs management's flattish guidance. Assuming if management were to achieve its FY23 guidance there could be 4% upside to our FY23 earning assumption.

KEY ASSUMPTIONS

(%)	2023F	2024F	2025F
Loan Growth	6.5	6.9	6.8
Credit Cost (bp)	10.0	10.0	9.0
ROE	11.3	11.1	11.2

Source: Sunway, UOB Kay Hian

ENVIRONMENTAL, SOCIAL, GOVERNANCE (ESG)

<ul style="list-style-type: none"> • Environmental <ul style="list-style-type: none"> - Carbon emission commitment. To reduce Scope 1 and 2 emissions by 40-50% by 2031. - Raising market share for hybrid vehicle financing. HLBank's market share for hybrid vehicle financing rose to 9% in 2021, comprising 2.8% of the group's outstanding HP loans. • Social <ul style="list-style-type: none"> - Gender diversity. Females comprise 40% of the group's upper management. • Governance <ul style="list-style-type: none"> - Non-independent board of directors composition. Composition of Independent Non-Executive Directors (INED) – 55%.

Source: UOB Kay Hian

EARNINGS REVISION/RISK

- We trim our FY23-25 earnings by 2-3% to factor in slower loans growth and NIM outlook.

VALUATION/RECOMMENDATION

- **Downgrade to HOLD with a lower target price of RM23.30 (11.3% ROE and 1.46x FY23F PBV) from RM24.00 post earnings adjustment.** The stock is currently trading at 1.30x FY23 P/B which is in line with its eight-year historical mean P/B. Our target price implies close to a +1.0SD above its eight-year historical mean P/B which we think has adequately priced in the stock's solid defensive qualities. As such, we take opportunity to downgrade the stock to a HOLD largely on valuation grounds.

1QFY23 RESULTS

Profit & Loss (RMm)	1QFY23	1QFY22	yoy % chg	4QFY22	qoq % chg	Remarks
Net Interest Income	989.6	918.8	7.7	928.6	6.6	Higher NIM from OPR hike
Islamic Banking	251.5	208.1	20.9	239.3	5.1	
Fees & Commissions	155.5	147.6	5.4	154.5	0.7	
Trading income	102.5	118.5	(13.5)	164.9	(37.8)	
Other income	0.8	-13.0	(105.9)	11.2	(93.2)	
Total Income	1,499.9	1,380.0	8.7	1,498.4	0.1	
Operating Expenses	(540.6)	(507.2)	6.6	(560.1)	(3.5)	
PPOP	959.4	872.7	9.9	938.3	2.2	
Provisions	(37.2)	(48.6)	(23.4)	(29.8)	24.9	9bp net credit cost
Associate	265.0	218.0	21.6	308.8	(14.2)	
PBT	1,187.1	1,042.1	13.9	1,217.3	(2.5)	
Net profit	981.4	858.3	14.3	907.6	8.1	In line
EPS (sen)	45.3	39.6	14.3	41.9	8.1	
DPS (sen)	0.0	0.0	n.a.	37.0	n.a.	
BVPS (RM)	15.21	14.37	5.8	15.13	0.5	
Financial Ratios (%)	1QFY23	1QFY22	yoy chg (ppt)	4QFY22	qoq chg (ppt)	
NIM	2.18	2.13	0.05	2.10	0.08	
Loan Growth, yoy	8.8	5.2	3.6	7.9	0.8	
Deposit Growth, yoy	9.0	4.6	4.4	8.4	0.6	
Loan/Deposit Ratio	86.8	84.0	(0.1)	83.3	0.7	
Cost/Income Ratio	36.0	36.8	(0.7)	37.4	(1.3)	
ROE	12.6	11.7	1.0	11.8	0.8	
NPL Ratio	0.5	0.5	0.0	0.5	0.0	
Credit Costs (bp)	8.9	12.5	(3.7)	7.2	1.7	
Loan Loss Coverage	282.0	309.0	(27.0)	282.0	0.0	
CET-1 CAR	12.9	13.0	(0.1)	13.4	(0.5)	

Source: HL Bank, UOB Kay Hian

PROFIT & LOSS

Year to 30 Jun (RMm)	2021	2022F	2023F	2024F
Interest income	5,557	5,723	6,271	6,592
Interest expense	(2,099)	(1,967)	(2,397)	(2,565)
Net interest income	3,458	3,756	3,874	4,028
Fees & commissions	570	610	628	659
Other income	519	328	351	361
Non-interest income	1,090	937	979	1,020
Income from islamic banking	919	905	995	1,105
Total income	5,467	5,598	5,848	6,152
Staff costs	(1,192)	(1,154)	(1,211)	(1,296)
Other operating expense	(886)	(945)	(990)	(1,016)
Pre-provision profit	3,389	3,499	3,646	3,840
Loan loss provision	(654)	(164)	(179)	(190)
Other provisions	(0)	1	3	4
Associated companies	736	1,030	1,154	1,246
Pre-tax profit	3,471	4,367	4,625	4,901
Tax	(610)	(1,078)	(865)	(916)
Minorities	0	0	0	0
Net profit	2,861	3,289	3,760	3,985
Net profit (adj.)	2,861	3,289	3,760	3,985

OPERATING RATIOS

Year to 30 Jun (%)	2021	2022F	2023F	2024F
Capital Adequacy				
Tier-1 CAR	13.5	13.4	14.5	15.1
Total CAR	16.2	16.7	13.7	14.5
Total assets/equity (x)	8.0	8.2	8.2	8.2
Tangible assets/tangible common equity (x)	8.6	8.7	8.7	8.6
Asset Quality				
NPL ratio	0.5	0.5	0.7	0.8
Loan loss coverage	246.6	211.8	142.4	118.5
Loan loss reserve/gross loans	1.1	1.0	1.0	1.0
Increase in NPLs	(19.4)	14.3	58.0	17.5
Credit cost (bp)	42.0	9.7	10.0	10.0
Liquidity				
Loan/deposit ratio	83.5	83.3	84.3	85.2
Liquid assets/short-term liabilities	22.2	16.9	18.1	17.9
Liquid assets/total assets	18.4	13.7	14.3	14.0

BALANCE SHEET

Year to 30 Jun (RMm)	2021	2022F	2023F	2024F
Cash with central bank	494	521	3,576	3,791
Govt treasury bills & securities	42,697	33,441	34,778	36,170
Interbank loans	487	843	885	929
Customer loans	154,071	166,488	176,978	187,747
Investment securities	23,635	32,358	33,815	35,336
Derivative receivables	1,005	1,863	1,863	1,863
Associates & JVs	5,502	6,455	6,455	6,455
Fixed assets (incl. prop.)	1,413	1,322	1,375	1,430
Other assets	7,827	11,040	14,770	18,651
Total assets	237,129	254,331	274,496	292,373
Interbank deposits	12,130	6,322	6,702	7,104
Customer deposits	184,435	199,961	209,959	220,457
Derivative payables	910	1,737	1,876	2,026
Debt equivalents	2,309	3,218	3,213	3,212
Other liabilities	7,887	12,105	19,444	23,823
Total liabilities	207,670	223,342	241,194	256,621
Shareholders' funds	29,459	30,989	33,302	35,750
Minority interest - accumulated	0	0	0	0
Total equity & liabilities	237,129	254,331	274,496	292,373

KEY METRICS

Year to 30 Jun (%)	2021	2022F	2023F	2024F
Growth				
Net interest income, yoy chg	25.1	8.6	3.1	4.0
Fees & commissions, yoy chg	9.6	6.9	3.0	5.0
Pre-provision profit, yoy chg	26.7	3.3	4.2	5.3
Net profit, yoy chg	14.7	15.0	14.3	6.0
Net profit (adj.), yoy chg	14.7	15.0	14.3	6.0
Customer loans, yoy chg	6.5	8.1	6.3	6.1
Customer deposits, yoy chg	6.1	8.4	5.0	5.0
Profitability				
Net interest margin	2.0	2.0	2.0	2.0
Cost/income ratio	38.0	37.5	37.6	37.6
Adjusted ROA	1.2	1.3	1.4	1.4
Reported ROE	10.1	10.9	11.7	11.5
Adjusted ROE	10.1	10.9	11.7	11.5
Valuation				
P/BV (x)	1.5	1.4	1.3	1.2
P/NTA (x)	1.6	1.5	1.4	1.3
Adjusted P/E (x)	15.2	13.2	11.5	10.9
Dividend Yield	2.4	2.6	3.0	3.2
Payout ratio	36.3	34.8	35.0	35.0

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