

SECTOR UPDATE

Banking – Malaysia

Positioning Ahead

The sector has remained resilient despite the headwinds. Initial concerns of modification losses may also be unfounded. Although the sector could remain in consolidation mode in 3Q21, we view any weakness as an opportunity to accumulate as the vaccination rollout gains momentum. The sector's solid capital and liquidity position act as effective shock absorbers, while valuations remain attractive at -1.5SD to historical mean P/B. Maintain OVERWEIGHT. CIMB is our top sector pick.

WHAT'S NEW

- Resilience in face of adversity.** Despite the numerous headwinds, the FBM Finance index has marginally outperformed the FBMKLCI by 3% ytd. But we are cognisant of the fact that the sector could remain in its current consolidation mode in 3Q21 as the number of COVID-19 cases remains elevated, leading to an extended lockdown. However, unlike past lockdowns, the current lockdown is coinciding with a promising COVID-19 vaccination rollout momentum. As such, we continue to believe there is light at the end of the tunnel and the market could be forward-looking in focusing on the eventual reopening of the economy by 4Q21. Consequently, any near-term share price weakness is an opportunity to accumulate, in our view.
- Tackling headwinds from a position of strength.** The banking sector's capital (CET1 ratio) and liquidity position (LCR) remain strong, with sector CET1 hovering at 14.6% and LCR of 152%, which are way above the minimum requirements. System deposit growth at an average of 5% continues to outpace loan growth of 4%. Household balance sheet indicators remain healthy with the household assets-to-debt ratio and household financial assets-to-debt ratio standing at 2.2x and 1.5x respectively. This has helped to underpin a robust 7.4% and 7.7% mortgage and automobile loan growth respectively as at end-May 2021.
- Modification loss from moratorium could potentially be a non-event.** Based on our channel checks, there is a high probability that the recent opt-in moratorium for all borrowers will be based on a similar scheme as the targeted moratorium that has been ongoing since Oct 20. This entails applicants having to sign a new loan agreement, which would result in lower monthly loan instalment payments after the moratorium, but could potentially lead to higher cumulative interest as the loan would have to be stretched by a longer period to reduce the monthly debt obligation. This would essentially result in banks suffering minimal modification losses.

ACTION

- Maintain OVERWEIGHT.** The sector's current consolidation phase provides an excellent opportunity for investors to accumulate on weakness. Current valuations of 1.05x is at -1.5SD to its historical 5-year mean which is attractive. We do not view the current lockdown to have a major upside risk on provisions as banks have by far and large built in sufficient pre-emptive provisions for the vulnerable groups that are more likely to be impacted from the lockdown, while a swifter rollout of COVID-19 vaccine in 2H21 should help to spur economic recovery. As such, we think that the current risk reward balance is attractive which prompts us to retain our OVERWEIGHT recommendation.
- CIMB remains our top sector pick.** Given its strong earnings growth off a low base, attractive valuations, large cap and liquid high beta nature, we continue to believe that the group is best positioned within the sector to benefit from the economic recovery and reopening theme which we expect the market could revisit towards 4Q21 as mass COVID-19 vaccination rollout gains traction. We also like HL Bank and Public Bank given their solid asset quality track record and RHB Bank for its strong capital position and its well balanced growth.

PEER COMPARISON

Company	Ticker	Rec	Share Price (RM)	Target Price (RM)	Market Cap (US\$m)	PE (x)	ROE (%)	P/B (x)	Div (sen)	Div Yield (%)		
						2020	2021F	2022F				
Public Bank	PBK MK	BUY	4.11	4.60	19,158	16.4	14.7	13.7	11.2	1.6	14.5	3.5
CIMB Group	CIMB MK	BUY	4.64	5.10	11,158	31.3	12.2	9.3	6.3	0.7	15.2	3.3
HL Bank	HLBK MK	BUY	18.82	22.30	9,797	13.8	12.1	11.0	10.7	1.3	54.4	2.9
RHB Bank	RHBBANK MK	BUY	5.39	6.35	5,190	8.8	8.5	7.7	9.1	0.8	25.4	4.7
HLFG	HLFG MK	BUY	18.00	20.75	4,950	9.8	9.2	8.7	10.0	0.9	41.3	2.3
Maybank	MAY MK	HOLD	8.11	8.70	22,773	14.1	12.1	10.3	8.8	1.1	53.8	6.6
AMMB	AMM MK	HOLD	2.95	2.90	2,342	9.3	7.6	6.6	8.3	0.6	10.7	3.6
BIMB	BIMB MK	HOLD	3.85	4.75	1,919	9.4	8.5	8.1	12.1	1.0	18.1	4.7
Alliance Bank	ABMB MK	HOLD	2.42	2.38	900	10.5	8.1	7.1	7.3	0.6	9.0	3.7
Affin	ABANK MK	HOLD	1.76	1.60	898	11.1	7.6	7.2	4.7	0.4	7.0	4.0

Source: UOB Kay Hian

OVERWEIGHT (Maintained)

TOP SECTOR PICKS

Company	Rec	Share Price (RM)	Target Price (RM)
Public Bank	BUY	4.11	4.60
CIMB Group	BUY	4.64	5.10
HL Bank	BUY	18.82	22.30
RHB Bank	BUY	5.39	6.35
HLFG	BUY	18.00	20.75

Source: UOB Kay Hian

BANKS' SHARE PRICE PERFORMANCE

Company	Price (RM)	yoy % chg	ytd % chg
CIMB Group	4.64	25.7	7.9
HL Bank	18.82	30.2	3.4
Public Bank	4.11	21.3	(0.2)
HLFG	18.00	37.8	(0.3)
RHB Bank	5.39	10.7	(1.1)
Maybank	8.11	6.4	(4.1)
Affin	1.76	10.0	(4.3)
BIMB	3.85	11.9	(9.6)
Alliance Bank	2.42	12.0	(16.8)
AMMB	2.95	(4.8)	(19.2)

Source: Bloomberg

SECTOR P/B (X)



Source: UOB Kay Hian

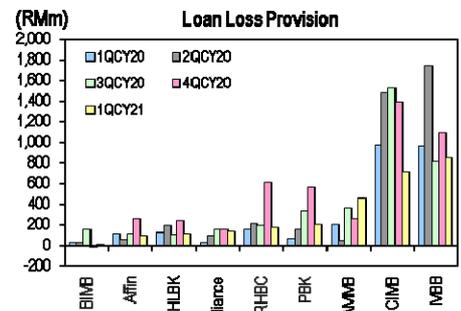
ANALYST(S)

Keith Wee Teck Keong
+603 2147 1981
keithwee@uobkayhian.com

ESSENTIALS

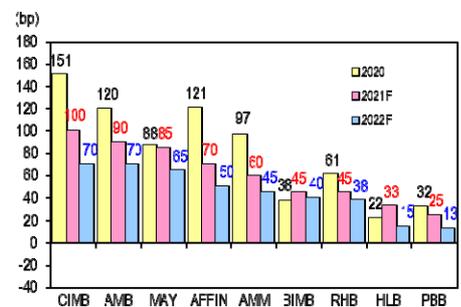
- GIL ratio will continue to lag.** The system gross impaired loans (GIL) ratio remained stable at 1.59% in May 21. Given the reimplementation of the loan moratorium for all borrowers (opt-in model) for a six-month period, the GIL ratio will remain benign for the rest of 2021 before rising from 2022 onwards.
- Targeted assistance level to rise but likely to remain at a manageable level.** As of end-1Q21, the overall sector take-up rate for the targeted loans assistance stood at 13-15%. Given the recent loan moratorium, we expect this to increase but is likely to remain significantly below the 85% average take-up rate during the auto moratorium programme in 2020 given the opt-in nature of the current moratorium. Taking into account the ongoing lockdown and the impact on vulnerable groups, most banks have guided that the level of targeted loan assistance may only rise upward to 20%. This assumes that only borrowers that require it would apply.
- Adequate pre-emptive provisions factored in despite lockdown.** Banks have by far and large made pre-emptive provisions in 2020 for vulnerable groups given the protracted nature of the ongoing pandemic. Our current pre-emptive provision assumptions for the banks in general implies that the system GIL ratio could rise 3.5x to 5.5%. Taking into account the relatively high pre-emptive credit cost that banking sector has already built in (2020: 82bp, 2021: 65bp (f) vs pre-COVID-19 average: 30bp p.a.) and much swifter rollout of COVID-19 vaccination, we make no changes to our credit cost outlook for 2021 despite the ongoing lockdown. We are expecting 147bp cumulative sector net credit cost over 2020-21 which is already higher than the 100-120bp range derived from the respective bank's guidance.
- Credit cost to chart a gradual decline well into 2023.** The sector's net credit cost was at 60bp in 1Q21. Although it is likely to rise closer to 70bp in the following quarters, we believe that it is likely to remain below the 82bp level registered in 2020. As such, we expect net credit cost to continue declining to 65bp and 40bp in 2021 and 2022 respectively and eventually to pre-COVID-19 level of 30bp in 2023. We believe that sector's net credit cost may have reached its peak in 4Q20 (100bp) as banks have by far and large taken the opportunity to pre-emptively front-load the bulk of the provisions that may be required for the vulnerable groups impacted by the lockdowns.
- Sustained recovery in earnings well into 2022.** On the back of a continued decline in net credit cost (off a high base) coupled with a stable NIM outlook and gradual improvement in loan growth, we expect the sector to register a robust 24% and 15% earnings growth in 2021 and 2022 respectively. Fee income growth is also likely to remain vibrant on the back of elevated brokerage and wealth management income coupled with improved transaction fee income as economic activities recover. However, revenue growth would be slightly tempered by rising bond yields and its impact on lower treasury income gains where we have assumed a contraction in trading income in 2021 and 2022. Taking a longer-term view, the prospects of a gradual interest rate normalisation in 2022-23 could help fuel NIM recovery.
- A case to support faster-than-expected normalisation of dividends?** The banking system's CET1 ratio had strengthened to 14.6% as at end-Apr 21 vs the pre-COVID-19 average level of 14.0% (2019) despite the negative impact from the surge in pre-emptive credit cost and Day 1 Modification losses as the overall sector had remained profitable.
- Current dividend yields attractive vs historical levels.** Taking a longer-term investment horizon, the average dividend yield for the sector into 2022 is now hovering at a commendable 5.3% vs its historical average of 4.5%. Meanwhile, the current implied 2021 yield of 4.0% is broadly in line with historical levels despite earnings being impacted by still elevated provisions. Our 2021 dividend payout ratio assumptions remain conservative, at 40% (2019: 48%).
- Public Bank and Maybank have normalised dividend payouts to pre-COVID-19 levels.** Public Bank and Maybank have normalised their dividend payout ratios to pre-COVID-19 levels in 2020. As credit cost is expected to subside gradually in 2021 and with an improved economic recovery outlook in 4Q21, in tandem with the much faster pace of the mass vaccination rollout in 2H21, we think more banks that are able to satisfy BNM's stress test may follow suit in potentially normalising their dividend payout ratios closer to pre-COVID-19 levels at an earlier-than-expected stage.
- NIM to remain relatively stable even with another potential rate cut.** Even if BNM were to cut the overnight policy rate (OPR) by an additional 25bp in 2H21 to further buffer the potential downside risk on the economy from the current lockdown, we expect NIM to remain flattish. This is because of the strong CASA growth and re-pricing of fixed deposits in 1Q21 from the OPR cut in Jul 20, thereby partially cushioning the impact of another OPR cut. Moving into 2H21, assuming OPR remains unchanged, we no longer expect any further sequential improvement in NIM as deposit re-pricing had been completed in 1Q21 while CASA growth could begin to moderate downwards in 4Q21 as economic activities gain momentum on improved vaccination.

QUARTERLY LOAN LOSS



Source: Respective companies, UOB Kay Hian.

CREDIT COST ASSUMPTIONS



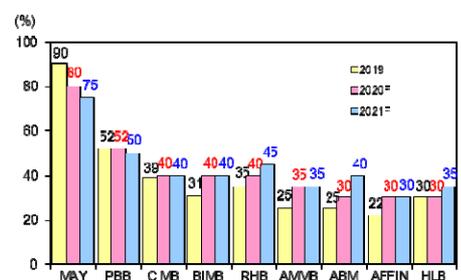
Source: Respective companies, UOB Kay Hian.

DIVIDEND YIELDS

	2021 Dividend Yield (%)	2022 Div Yield (%)	10-Year mean Div yield (%)
Maybank	6.6	7.2	7.1
RHB Bank	4.7	5.8	4.8
BMB	4.7	4.9	4.3
AMMB	3.6	5.7	4.0
Alliance	3.5	5.3	4.6
Public Bank	3.5	3.6	4.4
CIMB	3.3	4.3	4.4
HL Bank	2.2	2.9	3.3
Average	4.0	5.3	4.5

Source: Respective companies, UOB Kay Hian.

DIVIDEND PAYOUT RATIO ASSUMPTIONS



Source: Respective companies, UOB Kay Hian.

Disclosures/Disclaimers

This report is prepared by UOB Kay Hian Private Limited ("UOBKH"), which is a holder of a capital markets services licence and an exempt financial adviser in Singapore.

This report is provided for information only and is not an offer or a solicitation to deal in securities or to enter into any legal relations, nor an advice or a recommendation with respect to such securities.

This report is prepared for general circulation. It does not have regard to the specific investment objectives, financial situation and the particular needs of any recipient hereof. Advice should be sought from a financial adviser regarding the suitability of the investment product, taking into account the specific investment objectives, financial situation or particular needs of any person in receipt of the recommendation, before the person makes a commitment to purchase the investment product.

This report is confidential. This report may not be published, circulated, reproduced or distributed in whole or in part by any recipient of this report to any other person without the prior written consent of UOBKH. This report is not directed to or intended for distribution to or use by any person or any entity who is a citizen or resident of or located in any locality, state, country or any other jurisdiction as UOBKH may determine in its absolute discretion, where the distribution, publication, availability or use of this report would be contrary to applicable law or would subject UOBKH and its connected persons (as defined in the Financial Advisers Act, Chapter 110 of Singapore) to any registration, licensing or other requirements within such jurisdiction.

The information or views in the report ("Information") has been obtained or derived from sources believed by UOBKH to be reliable. However, UOBKH makes no representation as to the accuracy or completeness of such sources or the Information and UOBKH accepts no liability whatsoever for any loss or damage arising from the use of or reliance on the Information. UOBKH and its connected persons may have issued other reports expressing views different from the Information and all views expressed in all reports of UOBKH and its connected persons are subject to change without notice. UOBKH reserves the right to act upon or use the Information at any time, including before its publication herein.

Except as otherwise indicated below, (1) UOBKH, its connected persons and its officers, employees and representatives may, to the extent permitted by law, transact with, perform or provide broking, underwriting, corporate finance-related or other services for or solicit business from, the subject corporation(s) referred to in this report; (2) UOBKH, its connected persons and its officers, employees and representatives may also, to the extent permitted by law, transact with, perform or provide broking or other services for or solicit business from, other persons in respect of dealings in the securities referred to in this report or other investments related thereto; (3) the officers, employees and representatives of UOBKH may also serve on the board of directors or in trustee positions with the subject corporation(s) referred to in this report. (All of the foregoing is hereafter referred to as the "Subject Business"); and (4) UOBKH may otherwise have an interest (including a proprietary interest) in the subject corporation(s) referred to in this report.

As of the date of this report, no analyst responsible for any of the content in this report has any proprietary position or material interest in the securities of the corporation(s) which are referred to in the content they respectively author or are otherwise responsible for.

IMPORTANT DISCLOSURES FOR U.S. PERSONS

This research report was prepared by UOBKH, a company authorized, as noted above, to engage in securities activities in Singapore. UOBKH is not a registered broker-dealer in the United States and, therefore, is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. This research report is provided for distribution by UOBKH (whether directly or through its US registered broker dealer affiliate named below) to "major U.S. institutional investors" in reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act"). All US persons that receive this document by way of distribution from or which they regard as being from UOBKH by their acceptance thereof represent and agree that they are a major institutional investor and understand the risks involved in executing transactions in securities.

Any U.S. recipient of this research report wishing to effect any transaction to buy or sell securities or related financial instruments based on the information provided in this research report should do so only through UOB Kay Hian (U.S.) Inc ("UOBKHUS"), a registered broker-dealer in the United States. Under no circumstances should any recipient of this research report effect any transaction to buy or sell securities or related financial instruments through UOBKH.

UOBKHUS accepts responsibility for the contents of this research report, subject to the terms set out below, to the extent that it is delivered to and intended to be received by a U.S. person other than a major U.S. institutional investor.

The analyst whose name appears in this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA") and may not be an associated person of UOBKHUS and, therefore, may not be subject to applicable restrictions under FINRA Rules on communications with a subject company, public appearances and trading securities held by a research analyst account.

Analyst Certification/Regulation AC

Each research analyst of UOBKH who produced this report hereby certifies that (1) the views expressed in this report accurately reflect his/her personal views about all of the subject corporation(s) and securities in this report; (2) the report was produced independently by him/her; (3) he/she does not carry out, whether for himself/herself or on behalf of UOBKH or any other person, any of the Subject Business involving any of the subject corporation(s) or securities referred to in this report; and (4) he/she has not received and will not receive any compensation that is directly or indirectly related or linked to the recommendations or views expressed in this report or to any sales, trading, dealing or corporate finance advisory services or transaction in respect of the securities in this report. However, the compensation received by each such research analyst is based upon various factors, including UOBKH's total revenues, a portion of which are generated from UOBKH's business of dealing in securities.

Reports are distributed in the respective countries by the respective entities and are subject to the additional restrictions listed in the following table.

General	This report is not intended for distribution, publication to or use by any person or entity who is a citizen or resident of or located in any country or jurisdiction where the distribution, publication or use of this report would be contrary to applicable law or regulation.
Hong Kong	This report is distributed in Hong Kong by UOB Kay Hian (Hong Kong) Limited ("UOBKHHK"), which is regulated by the Securities and Futures Commission of Hong Kong. Neither the analyst(s) preparing this report nor his associate, has trading and financial interest and relevant relationship specified under Para. 16.4 of Code of Conduct in the listed corporation covered in this report. UOBKHHK does not have financial interests and business relationship specified under Para. 16.5 of Code of Conduct with the listed corporation covered in this report. Where the report is distributed in Hong Kong and contains research analyses or reports from a foreign research house, please note: (i) recipients of the analyses or reports are to contact UOBKHHK (and not the relevant foreign research house) in Hong Kong in respect of any matters arising from, or in connection with, the analysis or report; and (ii) to the extent that the analyses or reports are delivered to and intended to be received by any person in Hong Kong who is not a professional investor, or institutional investor, UOBKHHK accepts legal responsibility for the contents of the analyses or reports only to the extent required by law.
Indonesia	This report is distributed in Indonesia by PT UOB Kay Hian Sekuritas, which is regulated by Financial Services Authority of Indonesia ("OJK"). Where the report is distributed in Indonesia and contains research analyses or reports from a foreign research house, please note recipients of the analyses or reports are to contact PT UOBKH (and not the relevant foreign research house) in Indonesia in respect of any matters arising from, or in connection with, the analysis or report.
Malaysia	Where the report is distributed in Malaysia and contains research analyses or reports from a foreign research house, the recipients of the analyses or reports are to contact UOBKHM (and not the relevant foreign research house) in Malaysia, at +603-21471988, in respect of any matters arising from, or in connection with, the analysis or report as UOBKHM is the registered person under CMSA to distribute any research analyses in Malaysia.
Singapore	This report is distributed in Singapore by UOB Kay Hian Private Limited ("UOBKH"), which is a holder of a capital markets services licence and an exempt financial adviser regulated by the Monetary Authority of Singapore. Where the report is distributed in Singapore and contains research analyses or reports from a foreign research house, please note: (i) recipients of the analyses or reports are to contact UOBKH (and not the relevant foreign research house) in Singapore in respect of any matters arising from, or in connection with, the analysis or report; and (ii) to the extent that the analyses or reports are delivered to and intended to be received by any person in Singapore who is not an accredited investor, expert investor or institutional investor, UOBKH accepts legal responsibility for the contents of the analyses or reports only to the extent required by law.
Thailand	This report is distributed in Thailand by UOB Kay Hian Securities (Thailand) Public Company Limited, which is regulated by the Securities and Exchange Commission of Thailand.
United Kingdom	This report is being distributed in the UK by UOB Kay Hian (U.K.) Limited, which is an authorised person in the meaning of the Financial Services and Markets Act and is regulated by The Financial Conduct Authority. Research distributed in the UK is intended only for institutional clients.
United States of America ('U.S.')	This report cannot be distributed into the U.S. or to any U.S. person or entity except in compliance with applicable U.S. laws and regulations. It is being distributed in the U.S. by UOB Kay Hian (US) Inc, which accepts responsibility for its contents. Any U.S. person or entity receiving this report and wishing to effect transactions in any securities referred to in the report should contact UOB Kay Hian (US) Inc. directly.

Copyright 2021, UOB Kay Hian Pte Ltd. All rights reserved.

<http://research.uobkayhian.com>

RCB Regn. No. 197000447W