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# Singapore Banking Monthly

All eyes on dividend cap review

SINGAPORE | BANKING & FINANCE | UPDATE

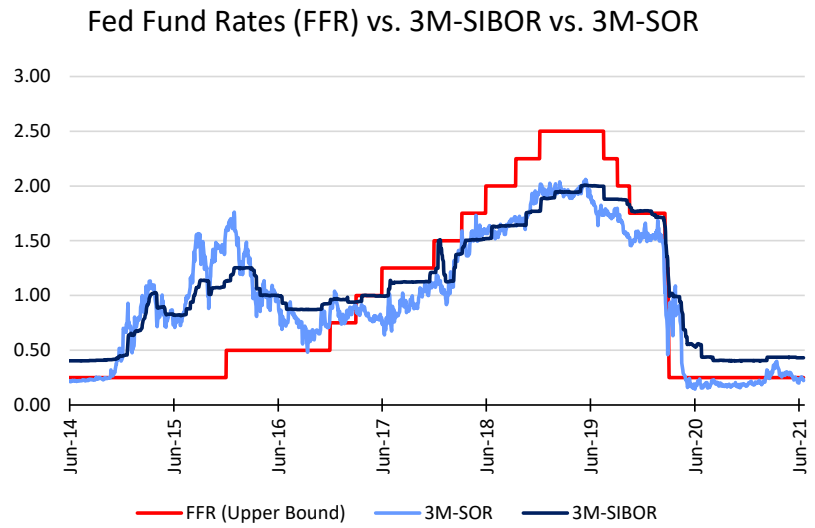
8 July 2021

- Singapore loans were up 0.2% YoY in May. Business loans contracted for ninth straight month by 0.5% YoY. Consumer loans were up for 10th straight month, by 0.3% YoY, aided by housing.
- MAS is assessing whether to extend current dividend restrictions on banks. We continue to see the potential for a removal of the dividend cap.
- **Maintain OVERWEIGHT.** Loans remain on path of recovery on stable interest rates. Catalysts to come from a relaxation of dividend caps on banks. We believe MAS could ease the dividend cap as Singapore banks have kept sufficient capital buffers. We prefer DBS (DBS SP, ACCUMULATE, TP: S$31.40) for sector exposure on account of its wealth-management and investment banking franchises.

### Local lending rates rebounded in June

Interest rates reversed their decline in May, with 3M-SIBOR and 3M-SOR recovering to 0.43% and 0.24% respectively in June as Singapore transitions out of Phase 2 (Heightened Alert). Current 3M-SIBOR is 1bps higher than the 1Q21 average of 0.42%. 3M-SOR is 2 bps lower than its 1Q21 average of 0.26% (Figure 1).

**Figure 1: 3M-SIBOR and SOR see uptick in June**




Source: Bloomberg, PSR

### Stress tests on banks for potential lifting of dividend cap

The MAS is running additional stress tests on the local banks to assess whether it is necessary to extend current dividend restrictions on them. It is in close discussions with the banks on their capital management plans and will be advising them on its position "very shortly".

## Overweight (Maintained)

### DBS Group Holdings

**ACCUMULATE (Maintained)**

| | |
|---|---|
| BLOOMBERG CODE | DBS SP |
| LAST TRADED PRICE | SGD 30.09 |
| FORECAST DIV | SGD 1.17 |
| TARGET PRICE | SGD 31.40 |
| DIVIDEND YIELD | 3.89% |
| TOTAL RETURN | 8.24% |

### Oversea-Chinese Banking Corp

**BUY (Maintained)**

| | |
|---|---|
| BLOOMBERG CODE | OCBC SP |
| LAST TRADED PRICE | SGD 11.89 |
| FORECAST DIV | SGD 0.56 |
| TARGET PRICE | SGD 14.63 |
| DIVIDEND YIELD | 4.71% |
| TOTAL RETURN | 27.75% |

### United Overseas Bank Limited

**ACCUMULATE (Maintained)**

| | |
|---|---|
| BLOOMBERG CODE | UOB SP |
| LAST TRADED PRICE | SGD 25.93 |
| FORECAST DIV | SGD 1.20 |
| TARGET PRICE | SGD 28.70 |
| DIVIDEND YIELD | 4.63% |
| TOTAL RETURN | 15.31% |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List of Abbreviations:
NIM – Net Interest Margin
SIBOR – Singapore Interbank Offer Rate
SOR – Swap Offer Rate
HIBOR – Hong Kong Interbank Offer Rate
DBU – Domestic Business Units
DDAV – Derivatives Daily Average Volume
SDAV – Securities Daily Average Value

We believe MAS will lift its dividend cap as banks had made significant provisions in FY2020. Earlier concerns that defaults among weaker corporates could strain their capital ratios have not materialised. Systemically-important domestic banks have CET-1 ratio at over 14%, which are higher than their pre-COVID levels. With total allowance coverage over 30% above MAS' regulatory limit, we believe the central bank could lift its dividend cap.

**Figure 2: Bank's key operating metrics in 1Q21**

| 1Q21 vs. 4Q20 | DBS | OCBC | UOB |
|---|---|---|---|
| NIM (vs. 4Q20) | 1.49% (unchanged) | 1.56% (unchanged) | 1.53% (unchanged) |
| NII | +2% | - | +1% |
| Net fees & commissions | +28% | +13% | +22% |
| General provisions (S$) | (190) mn | 9 mn | 130 mn |
| NPL ratio | 1.5% | 1.5% | 1.5% |
| NPA coverage | 109% | 118% | 112% |
| Common Equity Tier-1 | 14.3% | 15.3% | 15.3% |

Source: Company, PSR

## Snail's pace loans growth

Domestic loans growth rose 0.2% YoY in May, tracking below our expected range of 2% – 3% for 2021 but still above our expectations as concerns over loans growth slowing from Singapore's move into Phase 2 (Heightened Alert) did not materialise.

Business loans contracted by 0.5% YoY in May, for the ninth straight month even though business loans picked up for the month. Loans to the building and construction segment, the single largest business segment was up marginally by 0.1% for the second straight month to S$152.37bn, while loans to manufacturing reversed the decline in April to register a 5.1% gain.

Consumer loans were up 0.3% YoY in May for the 10th straight month, aided by strong loan demand in the housing segment. Housing loans, which make up three-quarters of consumer lending, extended their growth streak for the ninth straight month, up 2.6% YoY to S$205.1bn for the month.

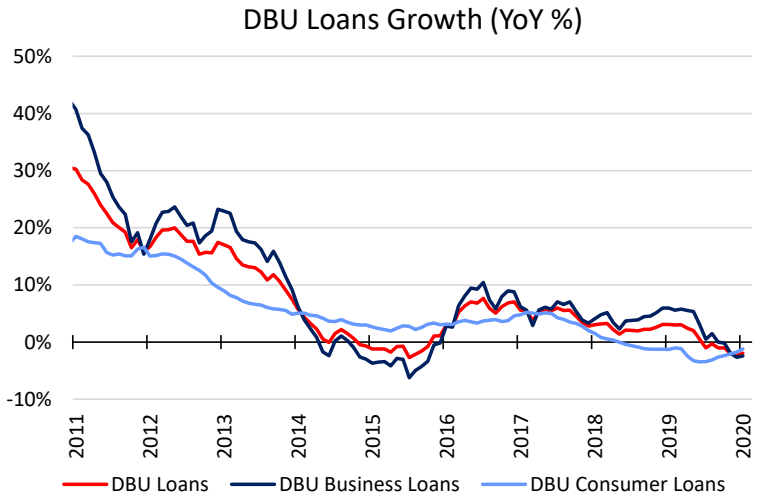
Overall loans through the domestic banking unit – which captures lending in all currencies but reflects mainly Singapore-dollar lending - rose for the seventh consecutive month. They were up 0.2% in May to S$693.7bn, up from the 0.1% increase in April.

**Figure 3: YTD loans growth**

| 2021 | Loans growth (MoM) |
|---|---|
| May | 0.22% |
| April | 0.14% |
| March | 0.65% |
| February | 0.46% |
| January | 0.72% |

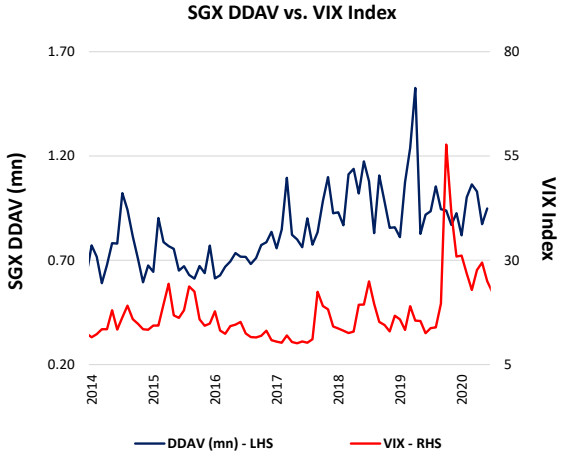
Source: MAS, PSR

**Figure 4: Domestic loans growth remained in low single-digits**




Source: MAS, PSR

**Figure 5: Correlation of DDAV and VIX Index**




Source: SGX, Bloomberg, PSR

### Volatility fell as Singapore exited Phase 2 (Heightened Alert)

SDAV fell 31% YoY to $1,192mn in June (Figure 6), as Singapore eased COVID-19 restrictions and exited Phase 2 (Heightened Alert). In May, derivatives traded on the SGX rose 6% YoY to 18.1mn contracts.

**Figure 6: YTD SDAV and DDAV performance**

| | SDAV ($mn) | YoY (+/-) | DDAV (mn) | YoY (+/-) |
|---|---|---|---|---|
| June | 1,192 | -31% | - | - |
| May | 1,579 | +5% | 0.95 | +3% |
| April | 1,267 | -10% | 0.87 | +6% |
| March | 1,633 | -26% | 1.03 | -33% |
| February | 1,357 | -1% | 1.06 | -14% |
| January | 1,485 | +22% | 1.00 | -7% |

Source: SGX, Bloomberg, PSR

VIX averaged 17.0 in June, down from 19.8 in the previous month as new COVID-19 community cases sent it lower. DDAV will likely fall in June, as trading volume had declined to a year-low.

Trading in SGX's suite of pan-Asia benchmark equity derivatives climbed 8% YoY to 13 million contracts. FTSE Taiwan Index Futures, launched in July 2020, advanced 28% MoM to a four month high of 1.8mn.

**Figure 7: Turnover of top five equity index futures contracts up YoY**

| No. of contracts | May-20 | May-21 | YoY (+/-) |
|---|---|---|---|
| FTSE China A50 Index Futures | 6,111,234 | 6,923,961 | +13.3% |
| Nifty 50 Index Futures | 1,999,875 | 2,037,095 | +1.9% |
| MSCI Taiwan Index Futures | 1,494,470 | 0 | +20.8% |
| FTSE Taiwan Index Futures | 0 | 1,805,071 | |
| Nikkei 225 Index Futures | 1,446,649 | 1,099,192 | -24.0% |
| MSCI Singapore Index Futures | 840,412 | 1,045,254 | +24.4% |
| **Sub-total** | **11,892,640** | **12,910,573** | **+8.6%** |

Source: SGX, Bloomberg, PSR

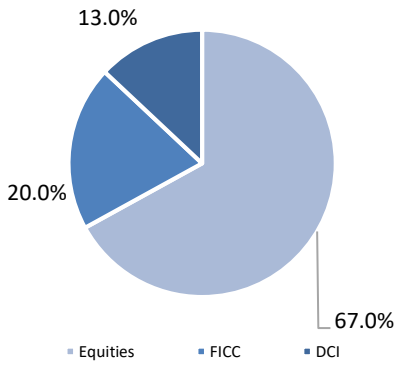
Foreign exchange (FX) traded on the SGX increased 2% YoY to 2mn contracts in May. China's economic rebound had led to strong institutional demand for risk-management of the renminbi (RMB). Reflecting this, SGX's USD/CNH Futures jumped 20% YoY to 869,101 contracts. Month-end open interest in this contract, the world's most widely-traded international RMB futures, leapt almost 32% YoY to US$9.6bn.

### SGX taking multi-asset business to next level

SGX is focusing on building a multi-asset exchange, widening its partnerships and networks and growing its international presence. During its recent Analysts' Day, it detailed its plan to strengthen its core businesses and invest in its next leg of growth.

Growth pipeline includes M&A targets that will augment its offerings, accelerate the growth of Scientific Beta and build an integrated forex marketplace to increase revenue contributions from the current 6%. The exchange has also set aside S$55mn – S$60mn in capex for modernising its systems architecture, digitalising and investing in its forex and fixed-income businesses.

**Figure 8: SGX 1H21 revenue**




Source: Company, PSR

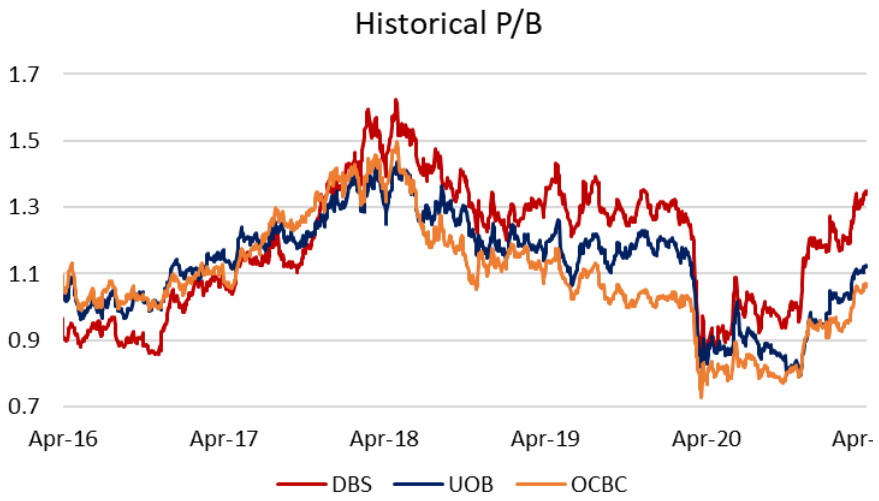
### Investment Action

**Maintain OVERWEIGHT.** Despite the run-up in their share prices in 1H21, we remain positive on banks. The banks have traded above 1.4x P/B over the last five year and are currently close-to or below our P/B targets. Our forward targets are supported by improving ROEs as allowances reverse in FY21e. With total allowance coverage being over 30% above the MAS' regulatory limit, we believe there is further room for GP reversions in 2021. This would boost earnings.

We also believe the MAS will ease the dividend cap imposed on Singapore banks in 2020 as they have kept sufficient capital buffers. Capital ratios of 14.3 - 15.3% are higher than the MAS' ideal operating range of 12.5 – 13.5%. This is supportive of a resumption of pre-COVID dividend payouts once dividend restrictions are removed. We believe the banks could pay out special dividends to adjust their high capital buffers.

For sector exposure, prefer DBS. DBS is expected to benefit more from improving market conditions with its wealth-management and investment banking businesses which could drive record earnings in FY21e.

**Figure 9: Banks' 5-year historical P/B**




Source: Bloomberg, PSR

**Figure 10: Banks' target P/B**

| | DBS | OCBC | UOB |
|---|---|---|---|
| High<br>Low | 1.62<br>0.81 | 1.50<br>0.73 | 1.43<br>0.79 |
| 5-year average | 1.17 | 1.09 | 1.12 |
| Current | 1.35 | 1.06 | 1.12 |
| Forward target | 1.36 | 1.27 | 1.17 |
| TP (S$) | 31.40 | 14.63 | 28.70 |

Source: Bloomberg, PSR

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