

OCBC Bank (OCBC SP)

Improving transparency

Good ESG disclosure levels. Could be better. BUY

OCBC scores a 70 in our enhanced ESG 2.0 methodology - this is above average. The Group is executing on its green financing targets strongly and scores well on workplace inclusivity and diversity. However, we believe OCBC's score could be significantly enhanced by increasing transparency on its Net Zero target and pathways to get there. Also detailed quantifications on operational environmental impacts are needed. Improving NIMs together with increasing North-South capital and wealth flows should support OCBC's earnings momentum going forward, we believe. Maintain BUY.

Strong Green-financing & management diversity

OCBC has successfully deployed SGD34bn of sustainable financing, making good progress on its SGD50bn by 2025 target. It has also set targets to reaching carbon neutrality from its operations by 2022. Contrastingly, there is limited disclosure on the Group's intended pathway towards Net Zero or a timeline. Separately, on workforce inclusivity, it is notable that women make up 58% of the total compared to our global comparison, HSBC (5 HK, HKD40.30, NR). Importantly, the proportion of women in senior management stands at 39% vs. 32% for HSBC. However, diversity at the Board level is lower with just 25% women, while proportion of independent directors are also lower than global comparisons.

Notable headroom for greater disclosure levels

We believe more disclosures are needed in areas such as waste and recycling. Similarly, there is limited disclosures on senior management rewards structures for achieving ESG targets. Clarity here would be critical for transparency on the Group's overall sustainability strategy, in our view. Concurrently, there is limited details on OCBC's pathway to capture financed emissions. Improved disclosures here could result in a higher ESG scoring, in our view.

Margins set to further improve. Maintain BUY.

We expect the strong NIM improvement momentum delivered in 1H22 to flow through to 2H22 as Fed rate hikes get further baked in. At the same time, the Group's gearing towards North-South supply chain and wealth flows gives it earnings visibility. China re-opening could be a near term upside catalyst. Asset quality remains benign so far, but slowing macro conditions increasing provisioning costs need to be watched. Maintain BUY.

FYE Dec (SGD m)	FY20A	FY21A	FY22E	FY23E	FY24E
Operating income	10,139	10,596	12,058	13,152	13,860
Pre-provision profit	5,596	5,729	6,527	7,156	7,431
Core net profit	3,586	4,858	5,813	6,493	6,798
Core EPS (SGD)	0.8	1.1	1.3	1.4	1.5
Core EPS growth (%)	(27.5)	34.9	19.7	11.7	4.7
Net DPS (SGD)	0.3	0.5	0.6	0.7	0.7
Core P/E (x)	12.6	10.5	9.2	8.3	7.9
P/BV (x)	0.9	1.0	1.0	0.9	0.8
Net dividend yield (%)	3.2	4.6	4.9	5.9	6.2
Book value (SGD)	11.09	11.72	12.53	13.37	14.24
ROAE (%)	7.6	9.7	10.9	11.4	11.2
ROAA (%)	0.7	0.9	1.0	1.1	1.1
Consensus net profit	-	-	5,739	6,439	6,751
MKE vs. Consensus (%)	-	-	1.3	0.8	0.7

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BUY

Share Price	SGD 11.93
12m Price Target	SGD 14.39 (+21%)
Previous Price Target	SGD 14.39

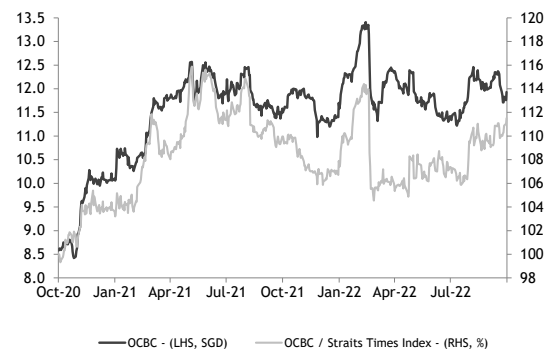
Statistics

52w high/low (SGD)	13.41/10.98
3m avg turnover (USDm)	43.7
Free float (%)	72.3
Issued shares (m)	4,257
Market capitalisation	SGD50.8B
	USD35.6B

Major shareholders:

LEE FAMILY /OCBC/	21.9%
Lee Foundation	4.3%
The Vanguard Group, Inc.	2.1%

Price Performance



	-1M	-3M	-12M
Absolute (%)	(0)	4	3
Relative to index (%)	3	5	2

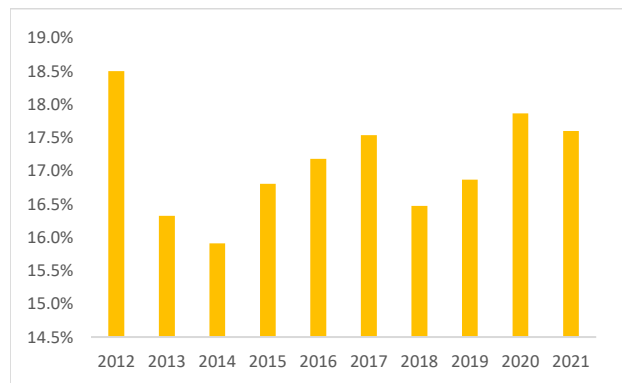
Source: FactSet

ESG@MAYBANK IBG
Tear Sheet Insert

Value Proposition

- Second-largest Singapore bank by assets. Present in Malaysia, Indonesia and Greater China.
- Acquired ING’s Asia Private Bank and Barclays’s wealth units in HK and Singapore to build up wealth management.
- 87.8%-owned subsidiary Great Eastern is a leader in Singapore life insurance.
- Bought Wing Hang Bank (WHB) in HK in 2014 to strengthen its presence in Pearl River Delta. Execution risks remain due to fierce competition
- Strongest capital levels amongst the local banks

Capital adequacy ratio (%)

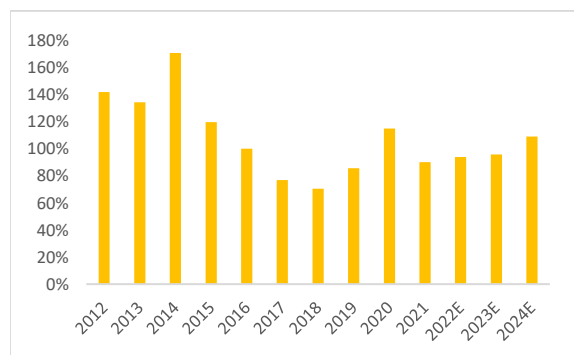


Source: Company

Financial Metrics

- We expect loan growth to slow from 8% YoY in 2021 to 7% YoY in 2022E as regional macro conditions slow
- Higher interest rates should see NIMs expanding 25bps YoY in 2022E and a further 9bps YoY in 2023E
- Costs could remain elevated with CIR reaching 45.6% in 2023E from higher staff and IT spend
- NPLs could remain at 1.5% levels in the medium term as asset growth and asset quality balance out

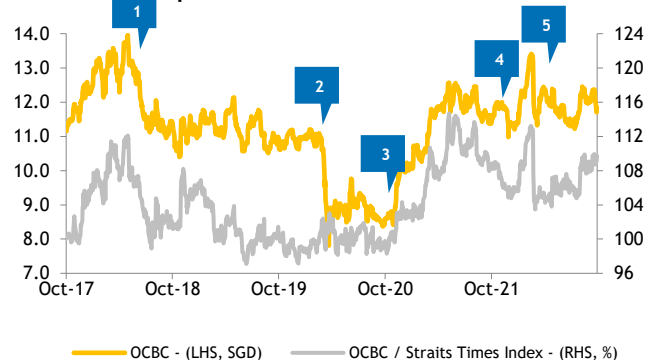
Provisioning cover to stay at comfortable levels



Source: Company

Price Drivers

Historical share price trend



Source: Company, Maybank IBG Research

1. Fears of US-China trade war and loan growth decline from property cooling measure
2. Start of the Covid-19 pandemic
3. Vaccine optimism driven recovery
4. Fed rate hike expectations
5. Rising inflation, rates driven worries on growth

Swing Factors

Upside

- Faster than expected improvements in equity & debt markets should drive insurance and trading gains
- Regional market share opportunities for USD funding
- Accretive acquisitions in the banking, wealth or insurance space in focus markets

Downside

- Increasing macro-volatility resulting in faster than expected asset quality and investment holding declines
- Potential IT system breakdowns or cyberattacks leading to regulatory sanctions
- New Covid variants and lockdowns in key markets

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Risk Rating & Score ¹	27.1
Score Momentum ²	-4.5
Last Updated	03 Oct 2022
Controversy Score ³ (Updated: 03 Oct 2022)	2

Business Model & Industry Issues

- The nature of OCBC’s business of lending and investments exposes it to multiple risks including environmental, social, money laundering, corruption through its clients. Target for sustainable financing commitment established at SGD50bn by 2025, while 60% of incremental loans in 2021 were classified as sustainable finance
- The industry is facing rising cyber-security and data protection threats as more and more banking goes online - especially accelerated by COVID-19 lockdowns. OCBC has had several service disruption issues in the past 10-years (2011 & 2018) due to IT infrastructure failures and faced issues handling SMS phishing scams in 2021
- OCBC has significant private banking and wealth management business exposes through its Bank of Singapore franchise as well as its Great Eastern Insurance subsidiary, which may lead to product governance, business ethics risks.
- We believe OCBC displays no exceptional risks not typical for a large, regional bank for ESG.

Material E issues

- Potential contagion risks from lending & investment to sectors with ESG issues. OCBC does not provide specific public disclosure on exposure to coal, palm oil, but total commodities exposure is 4% of loans, O&G 4%. Have adopted the Poseidon Principles to drive emissions reductions in shipping portfolios
- Committed to no new coal mining, brown coal, offensive weapons and exploitative labour funding
- OCBC has developed sector specific policies for ESG risk assessment and management. These policies cover all industries identified as ‘high risk’ by ABS Responsible Financing Guidelines.
- OCBC has set a target to achieve operational carbon neutrality by 2022 for its own emissions

Material S issues

- Potential financial inclusion risks. OCBC has developed inclusion products for the young, youth and elderly. However, there is limited information on how the group is tackling the under-banked, migrant workers and other socially vulnerable groups
- Increasing digitalisation as a response to financial inclusion. 60% of new secured consumer loans are approved digitally and all SME accounts are opened digitally (vs. 40% in 2020)
- Employee diversity and equal opportunity risks. Female employees make up 58% of the workforce. While women comprise 39% of leadership roles, only 33% are in senior management
- >75% of wealth management recommended funds carry a minimum BB MSCI ESG rating
- OCBC has a whistleblowing program to escalate employee concerns

Key G metrics and issues

- Regulators in Hong Kong found against OCBC in a mis-selling case in 2016 in its private banking arm. The mis-selling occurred before the entity was acquired by OCBC in 2009
- OCBC has not had any material accounting & tax, lobbying & public policy, sanctions related, data privacy or security controversies in the past 5-yers
- Given the breadth of products offered and the large wealth and PB franchise, fair dealing risks cannot be ignored. The group has a Fair Dealing monitoring program that measure quantitative and qualitative aspects of its performance. OCBC has also set up a Board Level Ethics and Conduct committee
- Significant investments in technology for systems and business integration as well as online banking opens it to material cyber-security risks. The group has developed a framework of policies and practices under corporate risk governance to tackle these issues. Nevertheless, the group has had 2 major digital infrastructure related incidents in the past 10-years
- The Group had SGD330m of additional capital (0.2% CAR) being imposed in 2Q22 by MAS for deficiencies in mitigating risks from SMS phishing scams in 2021
- Corporate Governance Risks. 75% of Board composition is Independent Directors. Gender diversity is low with 25% of female Board representation. In the Management committee this is 25%
- OCBC is a signatory to the UN Global Compact. It produces a sustainability report as part of its Annual Report. The report has been prepared under the ESG standards of SGX, GRI, and the recommendations of TCFD

¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company’s exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company’s enterprise value, respectively, from ESG-driven financial impacts. ²**Score Momentum** - indicates changes to the company’s score since the last update - a **negative** integer indicates a company’s improving risk score; a **positive** integer indicates a deterioration. ³**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

Quantitative parameters (Score: 78)						
	Particulars	Unit	2019	2020	2021	HSBC (2021)
E	Scope 1 GHG emissions	tCO2e	N/A	N/A	237	22,000
	Scope 2 GHG emissions	tCO2e	71,361	65,188	61,375	307,000
	Total	tCO2e	N/A	N/A	61,612	329,000
	Scope 3 GHG emissions	tCO2e	N/A	N/A	278	12,000
	Total	tCO2e	N/A	N/A	61,890	341,000
	GHG intensity (Scope 1 and 2)	kgCO2e/emp	N/A	N/A	2,017	1,470
	Energy consumption	MWh	123,042	114,887	109,790	833,000
	Water consumption	m3	591,936	507,510	407,051	1,594,000
	Printing paper from eco-friendly sources	tons	N/A	N/A	N/A	N/A
	Total waste generated	tons	N/A	N/A	N/A	13,000
Cases of environmental non-compliance	number	0	0	0	N/A	
S	% of women in workforce	%	59.0%	59.0%	58.0%	52.0%
	% of women in senior management roles	%	24.0%	39.0%	39.0%	32.0%
	Policy, data & framework breaches	number	0	0	0	0
	Average training hours per employee	hours	44.2	33.9	45.1	26.3
	Non-compliance concerning fair dealing outcomes	number	0	0	0	N/A
G	MD/CEO salary as % of reported net profit	%	0.23%	0.24%	0.21%	0.04%
	Board salary as % of reported net profit	%	0.08%	0.11%	0.08%	0.05%
	Independent directors on the Board	%	64%	64%	75%	85%
	Female directors on the Board	%	18%	18%	25%	38%

Qualitative Parameters (Score: 50)	
a) is there an ESG policy in place and whether there is a standalone ESG committee or is it part of a risk committee?	<i>No. It is part of the Risk Committee. However, there is a Sustainability Council chaired by the CEO that supports the Board</i>
b) is the senior management salary linked to fulfilling ESG targets?	<i>Not disclosed</i>
c) Does the company follow the task force of climate related disclosures (TCFD) framework for ESG reporting?	<i>Yes</i>
e) Does the company have a mechanism to capture Scope 3 emissions - which parameters are captured?	<i>Currently OCBC is capturing parameters including business air travel. It is planning to expand expand Scope 3 coverage to align with industry best practices. However, there is no disclosure on when it plans to capture financed emissions.</i>
f) What are the 2-3 key carbon mitigation/water/waste management strategies adopted by the company?	<i>It is implementing Green Mark certifications for its building operations and data centres. Similarly, it is reducing water consumption through installing water efficient fittings and aligning for BCA Green Mark standards</i>
g) Does carbon offset form part of the net zero/carbon neutrality target of the company?	<i>No. But it has indicated of plans to do so going forward</i>

Target (Score: 75)		
Particulars	Target	Achieved
SGD50bn Sustainable financing target by 2025	50bn	34bn
Carbon neutral operations by 2022	0	N/A
Integration of climate-related considerations in to ESG Risk Assessments by 2022 in alignment with TCFD and MAS		
Help 1m vulnerable individuals by 2023 in core markets from a 2017 baseline	1m	N/A
Impact		
NA		
Overall score: 70		
As per our ESG matrix, OCBC (OCBC SP) has an overall score of 70.		

ESG score	Weights	Scores	Final Score
Quantitative	50%	78	39
Qualitative	25%	50	13
Target	25%	75	19
Total			70

OCBC displays a reasonably high degree of transparency in its ESG disclosures. Its overall impact on 'E' has the potential to be higher with more transparent disclosures on waste disposal as well as Scope 3 financed emissions. Strong progress has been made meeting sustainability financing targets. However, we believe disclosures on alignment of senior management rewards towards ESG outcomes is critical going forward.

Appendix 1

Methodology of our proprietary ESG scoring

We have evaluated the ESG ratings based on quantitative, qualitative and ESG targets. We assign a score for each of these three parameters. The overall rating is based on the weighted average of the scores: quantitative (50%), qualitative (25%) and ESG target (25%). For the quantitative, qualitative and ESG target, the sub-parameters are assigned a score - '0' for data not available, '+1' for improving trajectory, positive change, 'Yes', better than peers or a positive number if historical is not available and '-1' for declining trajectory, negative change, 'No', lower than peers or a negative number. The total of the scores of all sub-parameters is divided by the total number of sub-parameter to receive the final score of that segment. The inputs of each sub-parameters may be different for different industries depending on the key areas to monitor for each industry. A company should achieve a minimum score of 50 for an average ESG rating.

FYE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Key Metrics					
Core P/E (x)	12.6	10.5	9.2	8.3	7.9
Core FD P/E (x)	12.6	10.5	9.2	8.3	7.9
P/BV (x)	0.9	1.0	1.0	0.9	0.8
P/NTA (x)	1.0	1.1	1.0	1.0	0.9
Net dividend yield (%)	3.2	4.6	4.9	5.9	6.2
INCOME STATEMENT (SGD m)					
Interest income	9,143.0	7,425.0	10,114.2	12,194.4	13,601.7
Interest expense	(3,177.0)	(1,570.0)	(2,822.4)	(4,025.9)	(4,952.5)
Net interest income	5,966.0	5,855.0	7,291.8	8,168.5	8,649.2
Net insurance income	899.0	1,334.0	1,307.3	1,372.7	1,441.3
Net fees and commission	2,003.0	2,245.0	2,334.8	2,451.5	2,574.1
Other income	1,271.0	1,162.0	1,124.0	1,158.9	1,195.1
Total non-interest income	4,173.0	4,741.0	4,766.1	4,983.1	5,210.6
Operating income	10,139.0	10,596.0	12,057.9	13,151.6	13,859.8
Staff costs	(2,748.0)	(3,028.0)	(3,542.8)	(3,897.0)	(4,208.8)
Other operating expenses	(1,795.0)	(1,839.0)	(1,988.2)	(2,098.8)	(2,220.2)
Operating expenses	(4,543.0)	(4,867.0)	(5,530.9)	(5,995.8)	(6,429.0)
Pre-provision profit	5,596.0	5,729.0	6,527.0	7,155.8	7,430.7
Loan impairment allowances	(2,043.0)	(873.0)	(510.2)	(659.9)	(691.8)
Other allowances	0.0	0.0	0.0	0.0	0.0
Associates & JV income	612.0	824.0	865.2	995.0	1,094.5
Pretax profit	4,165.0	5,680.0	6,882.0	7,490.9	7,833.4
Income tax	(437.0)	(648.0)	(894.7)	(824.0)	(861.7)
Minorities	(142.0)	(174.0)	(174.0)	(174.0)	(174.0)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	3,586.0	4,858.0	5,813.3	6,492.9	6,797.7
Core net profit	3,586.0	4,858.0	5,813.3	6,492.9	6,797.7
Preferred Dividends	(40.0)	0.0	0.0	0.0	0.0
BALANCE SHEET (SGD m)					
Cash & deposits with banks	59,341.0	53,381.0	62,992.2	67,852.4	74,361.6
Sec. under resale agreements	0.0	0.0	0.0	0.0	0.0
Derivatives financial assets	15,223.0	9,267.0	9,359.7	9,453.3	9,453.3
Dealing securities	0.0	0.0	0.0	0.0	0.0
Available-for-sale securities	0.0	0.0	0.0	0.0	0.0
Investment securities	66,434.0	71,286.0	71,813.9	75,477.6	75,124.3
Loans & advances	263,538.0	286,281.0	304,910.5	327,045.8	353,215.9
Central bank deposits	0.0	0.0	0.0	0.0	0.0
Investment in associates/JVs	4,633.0	6,170.0	6,170.0	6,170.0	6,170.0
Insurance assets	0.0	0.0	0.0	0.0	0.0
Fixed assets	4,380.0	4,307.0	4,235.2	4,164.6	4,095.2
Intangible assets	4,837.0	4,774.0	4,774.0	4,774.0	4,774.0
Other assets	103,009.0	106,721.0	112,057.1	113,177.6	114,309.4
Total assets	521,395.0	542,187.0	576,312.6	608,115.3	641,503.7
Deposits from customers	314,907.0	342,395.0	371,186.1	397,414.4	425,734.2
Deposits from banks & FIs	9,586.0	8,239.0	9,062.9	9,969.2	10,168.6
Derivatives financial instruments	15,516.0	9,070.0	9,070.0	9,070.0	9,070.0
Subordinated debt	3,145.0	2,730.0	2,730.0	2,730.0	2,730.0
Other securities in issue	0.0	0.0	0.0	0.0	0.0
Other borrowings	21,210.0	17,385.0	18,254.3	19,167.0	20,125.3
Insurance liabilities	0.0	0.0	0.0	0.0	0.0
Other liabilities	105,855.0	108,030.0	108,030.0	108,030.0	108,030.0
Total liabilities	470,219.0	487,849.0	518,333.3	546,380.6	575,858.1
Share capital	17,833.0	18,040.0	18,040.0	18,040.0	18,040.0
Reserves	30,591.0	33,425.0	37,066.3	40,821.7	44,732.6
Shareholders' funds	48,424.0	51,465.0	55,106.3	58,861.7	62,772.6
Preference shares	1,198.0	1,198.0	1,198.0	1,198.0	1,198.0
Minority interest	1,554.0	1,675.0	1,675.0	1,675.0	1,675.0
Total equity	51,176.0	54,338.0	57,979.3	61,734.7	65,645.6
Total liabilities & equity	521,395.0	542,187.0	576,312.6	608,115.3	641,503.7

FYE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Key Ratios					
Growth (%)					
Net interest income	(5.8)	(1.9)	24.5	12.0	5.9
Non-interest income	(8.1)	13.6	0.5	4.6	4.6
Operating expenses	(4.3)	7.1	13.6	8.4	7.2
Pre-provision profit	(8.6)	2.4	13.9	9.6	3.8
Core net profit	(26.4)	35.5	19.7	11.7	4.7
Gross loans	0.9	8.4	6.6	7.3	8.1
Customer deposits	4.0	8.7	8.4	7.1	7.1
Total assets	6.0	4.0	6.3	5.5	5.5
Profitability (%)					
Non-int. income/Total income	41.2	44.7	39.5	37.9	37.6
Average lending yields	2.38	1.86	2.38	2.68	2.80
Average cost of funds	0.92	0.44	0.73	0.97	1.12
Net interest margin	1.55	1.46	1.71	1.80	1.78
Net income margin	35.37	45.85	48.21	49.37	49.05
Cost/income	44.8	45.9	45.9	45.6	46.4
Liquidity (%)					
Loans/customer deposits	83.7	83.6	82.1	82.3	83.0
Asset quality (%)					
Net NPL	0.1	0.3	0.2	0.1	(0.1)
Gross NPL	1.5	1.5	1.5	1.5	1.4
Net NPF	0.0	0.0	0.0	0.0	0.0
(SP+GP)/average gross loans	0.8	0.3	0.2	0.2	0.2
Loan loss coverage	114.8	90.0	93.7	95.6	109.0
Capital adequacy (%)					
CET1	15.2	15.5	15.5	14.4	14.2
Tier 1 capital	15.8	16.0	16.1	14.9	14.7
Risk-weighted capital	17.9	17.6	17.5	16.2	15.9
Returns (%)					
ROAE	7.6	9.7	10.9	11.4	11.2
ROAA	0.7	0.9	1.0	1.1	1.1
Shareholders equity/assets	9.3	9.5	9.6	9.7	9.8

Source: Company; Maybank IBG Research

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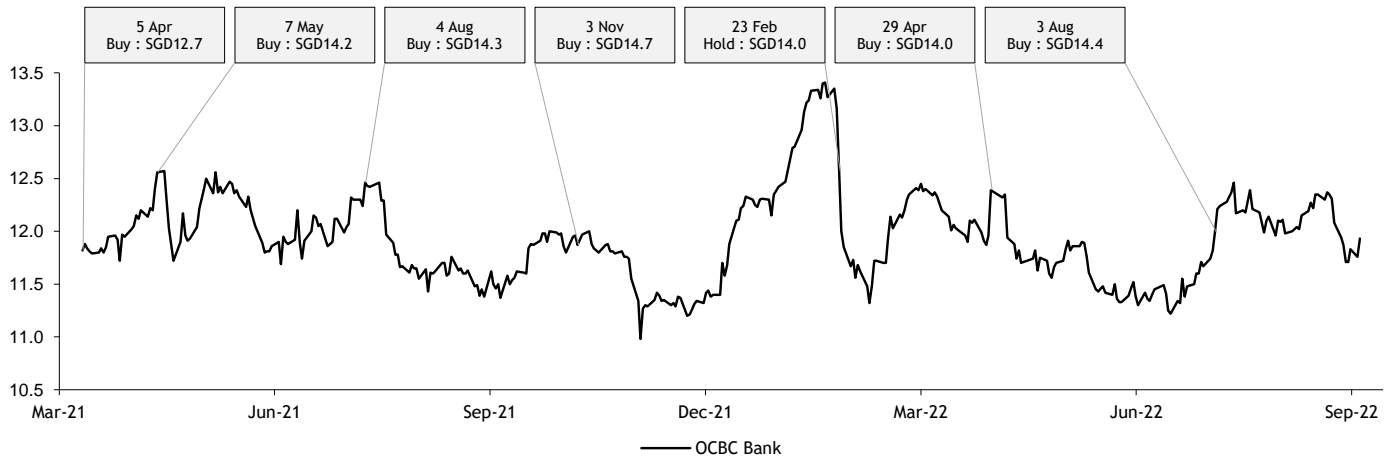
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