

China / Hong Kong Company Update

Hang Seng Bank

Bloomberg: 11 HK EQUITY | Reuters: 0011.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

28 Feb 2024

HOLD

Last Traded Price (27 Feb 2024): HK\$89.75 (HSI: 16,791)
Price Target 12-mth: HK\$97.00 (8% upside) (Prev HK\$116.0)

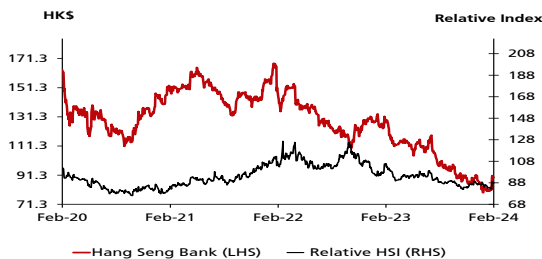
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What's New

- FY23 results in line; net profit increased 58% y-o-y to HK\$17.8bn
- Following de-risking strategy, NPL ratio stabilized at 2.83% in FY23, down 2bps h-o-h
- We expect credit costs to drop 5-20bps in FY24/25F from c.70bps in FY23, but remain more conservative than consensus
- Maintain HOLD with TP revised down to HK\$97 with higher ECL charge assumptions

Price Relative



Forecasts and Valuation

FY Dec (HK\$ m)	2023A	2024F	2025F	2026F
Pre-prov. Profit	26,198	25,620	26,026	26,482
Pre-prov. Profit Gth	34	(2)	2	2
Pretax Profit	20,105	19,972	20,518	21,688
Net Profit	17,848	17,785	18,272	19,313
EPS (HK\$)	9.24	9.21	9.46	10.00
EPS Gth (%)	70	0	3	6
PE (X)	9.7	9.7	9.5	9.0
DPS (HK\$)	6.43	6.41	6.59	6.98
Div Yield (%)	7.2	7.1	7.3	7.8
BV Per Share (HK\$)	87.04	89.47	91.97	94.62
P/Book Value (x)	1.0	1.0	1.0	0.9
ROAE (%)	10.9	10.4	10.4	10.7
ROAE (ex-exceptional)	10.9	10.4	10.4	10.7
ROA (%)	1.01	1.03	1.01	1.02

Earnings Rev (%)	(7)	(12)	New
Consensus EPS (HK\$)	9.96	9.66	10.19
Other Broker Recs:	B:3	S:1	H:9

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

De-risking strategy highlights asset quality

Investment Thesis

De-risking strategy showing positive progress. Following its cautious strategy in balance sheet expansion, Hang Seng Bank (HSB) saw an c.7% y-o-y decline in its gross loan balance by the end-Dec '23 to HK\$874bn. Its China CRE exposure dropped by 33% y-o-y to HK\$34.7bn by end-Dec '23. As a result of its de-risking progress, its NPL ratio by the end of FY23 dropped 2bps h-o-h to 2.83%. The bank expects lower credit costs going ahead.

Expect flattish y-o-y earnings for FY24/25F, as the Fed Fund rate is expected to begin the downturn cycle in 2H24F. We expect more NIM downward pressure 2H24 onwards while loan volume growth turns to low-single-digits y-o-y in FY24-26F as 1) recovering loan demand with lower interest rate with our expectation for HK loan growth at 2% y-o-y in 2024; and 2) de-risk for China CRE has been partly done. On the cost side, we expect operating efficiency to carry on with cost-to-income ratio remaining below 40% in FY24/25F.

More conservative than consensus on ECL charge. We are less concerned on HSB's China CRE exposure and asset quality than previously. However, uncertainties on China macro-economics in 2024 remain. We expect credit cost to be c.50-65bps between FY24-26F (vs. c.70bps for FY23), higher than the consensus expectation of 25-46bps. Our FY24/25F earnings assumptions are thus 5% lower than consensus.

Maintain HOLD with TP revised down to HK\$97, with earnings revised down by 11-12% for FY24/25F mainly due to more conservative views on ECL charges. China CRE showed weaker-than-expected performance since our last update, and China economy uncertainties remain, despite a soft-landing scenario as the base case. Our TP is based on the DDM model with assumptions of 13% (prev. 15%) ROE, 3% growth, and 12% cost of equity. Our TP implies a 1.1x forward P/BV, below -1SD of its five-year average.

Key Risks

Upside risk: Higher-than-expected growth recovery in China CRE.

Downside risk: HK loan demand growth being weaker-than-expected and further asset quality deterioration.

At A Glance

Issued Capital (m shrs)	1,912
Mkt Cap (HKm/US\$m)	171,602 / 21,932
Major Shareholders (%)	
HSBC Holdings PLC	62.1
Free Float (%)	37.9
3m Avg. Daily Val. (US\$m)	17.9
GICS Industry: Financials / Banks	

Hang Seng Bank

WHAT'S NEW

Highlights in operating efficiency and asset quality

FY23 results in line

Hang Seng Bank reported FY23 profit to shareholders at HK\$17.8bn (58% y-o-y growth), in line with the market expectation of c.HK\$17bn for FY23. Revenue increased by 18.9% y-o-y to HK\$40.8bn. NIM increased by 55bps y-o-y to 2.30% and NII increased by 26% y-o-y to HK\$32.3bn. Gross loan balance by the end of FY23 dropped by c.7.5% y-o-y to HK\$874bn, in line with the overall HK loan trend. ROE increased to 11.3% in FY23 from 7.2% in FY22.

Key highlights of the results

Major positives in results include 1) asset quality, with NPL ratio of 2.83% vs 2.85% by 1H23 and 2.56% at FY22 year end, showing a stabilization trend better than market expectation, as its de-risking from China CRE strategy is showing positive progress; 2) operating efficiency, with cost-to-income ratio having dropped from 40.1% in FY22 to 35.8% in FY23 mainly due to strong revenue side in the high-interest environment and continuous digitalization efforts; and 3) shareholder returns, as HSB reported a strong CET-1 ratio at 18.1%. Management is actively considering additional shareholder distributions.

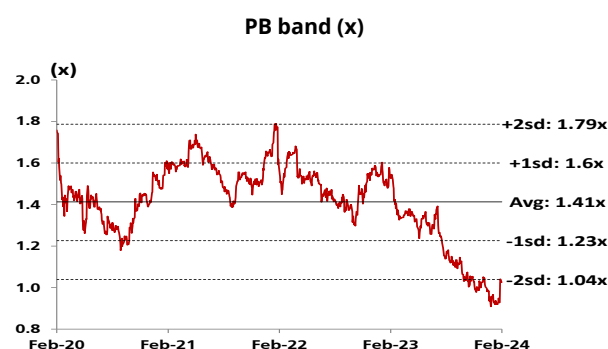
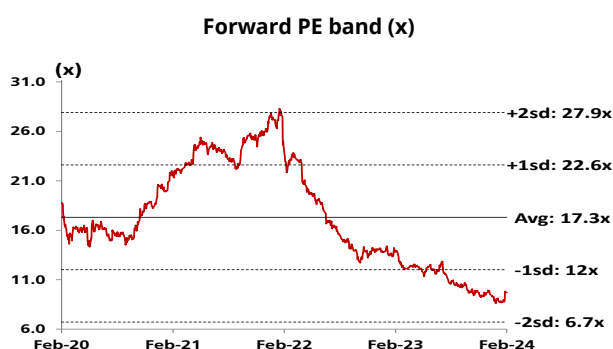
Outlook:

We expect NIM to hold up high in 1H24 with more downward pressure in 2H24. In 1H24, we see headwinds such as weaker HIBOR and continuous time deposit migration, while the positive side is that the time deposit rate in HK is not that high when the deposit competition is less intense. On the non-NII side, we expect HSB to continue to grow in the cross-border businesses. The fee income related to capital market may also follow when interest rate begins to cut. We revised down our ECL charges estimation to reflect a relatively conservative view on China/HK macroeconomy. Still, we expect lower credit costs in FY24/25F vs. FY23, following the banks' de-risking efforts.

Company Background

Founded in 1922, Hang Seng Bank (HSB) is one of the largest banks in Hong Kong by asset size, and is a principal member of the HSBC Group. Its subsidiary, Hang Seng Bank (China) Limited, operates a network of 46 branches around China. As of FY23, HSB had HK\$1.7tr in assets and HK\$847bn in loans.

Historical PE and PB band



Source: Thomson Reuters, DBS HK

Hang Seng Bank

Key Assumptions

FY Dec	2022A	2023A	2024F	2025F	2026F
NIM (%)	1.75	2.30	2.27	2.17	2.07
Loan growth (%)	(6)	(7)	3	6	5
Cost-to-income (%)	43	36	36	37	37
Credit cost (%)	0.8	0.7	0.7	0.6	0.5
Customer Deposits Growth (%)	2	(8)	5	5	5
Yld. On Earnings Assets (%)	2.01	3.53	3.43	3.27	3.16
Avg Cost Of Funds (%)	0.64	1.99	1.94	1.84	1.79

Source: Company, DBS HK

Income Statement (HK\$ m)

FY Dec	2022A	2023A	2024F	2025F	2026F
Net Interest Income	25,551	32,295	30,944	30,299	29,492
Non-Interest Income	8,848	8,527	9,270	10,733	12,331
Operating Income	34,399	40,822	40,214	41,032	41,823
Operating Expenses	(14,778)	(14,624)	(14,595)	(15,006)	(15,341)
Pre-provision Profit	19,621	26,198	25,620	26,026	26,482
Provisions	(7,705)	(6,252)	(5,841)	(5,701)	(4,987)
Associates	(10)	193	193	193	193
Exceptionals	(108)	(34)	0	0	0
Pre-tax Profit	11,798	20,105	19,972	20,518	21,688
Taxation	(1,288)	(2,267)	(2,197)	(2,257)	(2,386)
Minority Interests	14	10	10	10	11
Preference Dividend	0	0	0	0	0
Net Profit	10,524	17,848	17,785	18,272	19,313
Net Profit bef Except	10,632	17,882	17,785	18,272	19,313

Growth (%)

Net Interest Income Gth	7.26	26.39	(4.18)	(2.08)	(2.66)
Net Profit Gth	(24.61)	69.59	(0.35)	2.74	5.70

Margins, Costs & Efficiency (%)

Spread	1.37	1.54	1.50	1.43	1.37
Net Interest Margin	1.75	2.30	2.27	2.17	2.07
Cost-to-Income Ratio	43.0	35.8	36.3	36.6	36.7

Business Mix (%)

Net Int. Inc / Opg Inc.	74.3	79.1	76.9	73.8	70.5
Non-Int. Inc / Opg inc.	25.7	20.9	23.1	26.2	29.5
Fee Inc / Opg Income	15.2	12.1	13.1	14.0	14.9
Oth Non-Int Inc/Opg Inc	10.5	8.8	10.0	12.2	14.6

Profitability (%)

ROAE Pre Ex.	6.2	10.9	10.4	10.4	10.7
ROAE	6.1	10.9	10.4	10.4	10.7
ROA Pre Ex.	0.6	1.0	1.0	1.0	1.0
ROA	0.6	1.0	1.0	1.0	1.0

Source: Company, DBS HK

Interim Income Statement (HK\$ m)

FY Dec	2H2021	1H2022	2H2022	1H2023	2H2023
Net Interest Income	11,939	10,692	14,859	15,191	17,104
Non-Interest Income	3,917	4,717	4,131	4,749	3,778
Operating Income	15,856	15,409	18,990	19,940	20,882
Operating Expenses	(5,483)	(6,816)	(7,962)	(7,156)	(7,468)
Pre-Provision Profit	10,373	8,593	11,028	12,784	13,414
Provisions	(2,478)	(2,102)	(5,603)	(1,926)	(4,326)
Associates	36	(35)	25	104	89
Exceptionals	43	(59)	(49)	(1)	(33)
Pretax Profit	7,974	6,397	5,401	10,961	9,144
Taxation	(902)	(900)	(388)	(1,139)	(1,128)
Minority Interests	8	8	6	5	5
Net Profit	7,080	5,505	5,019	9,827	8,021

Growth (%)

Net Interest Income Gth	(1.4)	(10.0)	24.5	42.1	15.1
Net Profit Gth	(14.3)	(37.2)	(29.1)	78.5	59.8

Source: Company, DBS HK

Balance Sheet (HK\$ m)

FY Dec	2022A	2023A	2024F	2025F	2026F
Cash/Bank Balance	17,609	10,564	11,092	11,647	12,229
Government Securities	0	0	0	0	0
Inter Bank Assets	104,567	113,958	99,412	86,199	70,793
Total Net Loans & Adv.	931,334	860,406	884,084	932,414	977,175
Investment	703,789	621,641	673,761	691,864	710,468
Associates	2,256	2,363	2,556	2,749	2,942
Fixed Assets	39,496	39,075	41,029	43,080	45,234
Goodwill	3,894	4,335	4,682	5,056	5,461
Other Assets	51,501	39,752	55,417	82,992	120,059
Total Assets	1,854,446	1,692,094	1,772,033	1,856,002	1,944,362
Customer Deposits	1,249,486	1,153,062	1,210,715	1,271,251	1,334,813
Inter Bank Deposits	16,509	32,474	34,098	35,803	37,593
Debts/Borrowings	93,379	9,857	10,054	10,255	10,460
Others	182,700	161,253	168,659	176,575	185,042
Minorities	65	53	53	53	53
Shareholders' Funds	159,933	168,131	172,827	177,656	182,772
Total Liab& S/H's Funds	1,854,446	1,692,094	1,772,033	1,856,002	1,944,362

Source: Company, DBS HK

Hang Seng Bank

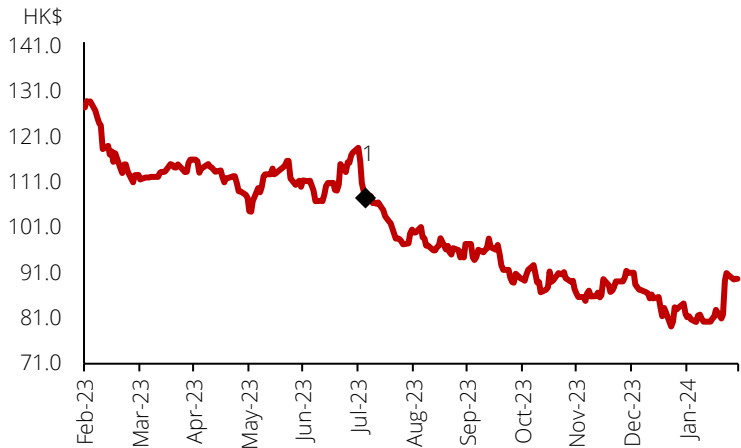
Financial Stability Measures (%)

FY Dec	2022A	2023A	2024F	2025F	2026F
Balance Sheet Structure					
Loan-to-Deposit Ratio	75.6	75.8	74.2	74.7	74.7
Net Loans / Total Assets	50.2	50.8	49.9	50.2	50.3
Investment / Total Assets	38.0	36.7	38.0	37.3	36.5
Cust. Dep./Int. Bear. Liab.	86.9	84.5	92.7	92.9	93.1
Interbank Dep / Int. Bear.	1.1	2.4	2.6	2.6	2.6
Asset Quality					
NPL / Total Gross Loans	2.6	2.8	2.8	2.6	2.5
NPL / Total Assets	1.3	1.5	1.4	1.3	1.3
Loan Loss Reserve Coverage	55.3	55.1	57.7	71.7	81.1
Provision Charge-Off Rate	0.8	0.7	0.7	0.6	0.5
Capital Strength					
Total CAR	18.1	21.4	21.9	22.4	22.6
Tier-1 CAR	16.8	19.9	19.6	19.4	19.2

Source: Company, DBS HK

Hang Seng Bank

Target Price & Ratings 12-mth History



S.No.	Date	Closing Price	Target Price	Rating
1	4-Aug-23	HK\$109.00	HK\$116.00	HOLD

Source: DBS HK

Analyst: Manyi Lu

Ken Shih

Iris GAO

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STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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Sources for all charts and tables are DBS HK unless otherwise specified.

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