Maybank IB Research

Banks

Malaysia

RHB Bank (RHBBANK MK)

Credit cost guidance still intact

BUY

Share Price	MYR 5.36
12m Price Target	MYR 6.30 (+18%)
Previous Price Target	*MYR 6.30*

Buffers to our forecasts

While an uptick in loans under targeted relief assistance is to be expected amid the current second lockdown, management is comfortable with its credit cost guidance for now and we have, in fact, maintained higher credit cost assumptions, thus providing some buffer to our earnings forecasts. We maintain a BUY on RHB with an unchanged TP of MYR6.30 (CY22E PBV: 0.9x; ROE: 8.5%).

Some uptick in TRA expected but credit cost intact

Amid a second lockdown, management is seeing a tick-up in consumer and SME loan applications for Targeted Relief Assistance (TRA). Recall, outstanding loans under TRA accounted for 10% of total loans as at end-Mar 2021. Nevertheless, management believes that its credit cost guidance of 30bp for FY21 is comfortable. There is buffer to our earnings forecasts, we feel, for we have assumed a higher credit cost of 45bps for FY21, 33bps for FY22.

Other targets maintained

Managing potential marked-to-market (MTM) investment losses from potentially higher bond yields is the challenge for banks this year. Todate, RHB has monetized some of its FVOCI gains to buffer against such losses. We have nevertheless taken a cautious view and assumed a 13% YoY decline in non-interest income (NOII) this year. Management's other targets are maintained and they include i) loan growth of 4-5% (MKE: 4%); ii) NIM of 2.06% (MKE: 2.06%), iii) expense growth <5% (MKE: 4.2%) and ROE of 9% (MKE: 8.3%). Imputing a lower credit cost of 30bps (in line with mgt's target) would raise our FY21 net profit by 9% and yield an ROE of 9%.

Hoping for a higher dividend payout

Separately, having priced its dividend reinvestment plan (DRP) at MYR4.61, which is an attractive 10% discount to VWAP, we think the take-up rate should be decent. This should lend some optimism to possibly a higher dividend payout this year (35% in FY20 vs 50% in FY19; MKE: 40% in FY21E).

FYE Dec (MYR m)	FY19A	FY20A	FY21E	FY22E	FY23E
Operating income	7,058	7,186	7,395	7,513	7,856
Pre-provision profit	3,670	3,799	3,928	3,962	4,221
Core net profit	2,527	2,186	2,299	2,473	2,662
Core EPS (MYR)	0.63	0.55	0.57	0.62	0.66
Core EPS growth (%)	9.6	(13.5)	5.1	7.6	7.6
Net DPS (MYR)	0.31	0.18	0.23	0.25	0.27
Core P/E (x)	9.2	10.0	9.4	8.7	8.1
P/BV (x)	0.9	0.8	0.8	0.7	0.7
Net dividend yield (%)	5.4	3.2	4.3	4.6	5.0
Book value (MYR)	6.43	6.74	7.08	7.45	7.85
ROAE (%)	10.3	8.3	8.3	8.5	8.7
ROAA (%)	1.0	0.8	0.8	0.8	0.9
Consensus net profit	-	-	2,498	2,795	3,014
MKE vs. Consensus (%)	-	-	(8.0)	(11.5)	(11.7)

Company Description

RHB Capital provides integrated financial services such as commercial banking, Islamic banking, investment banking, and stock broking, among others.

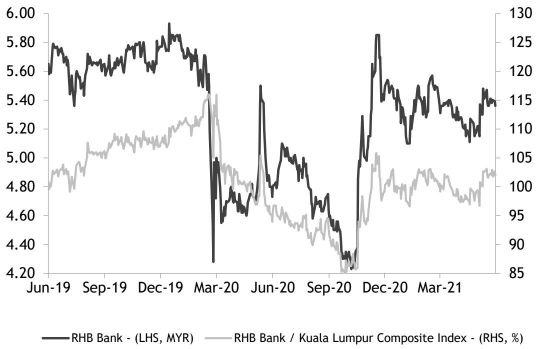
Statistics

52w high/low (MYR)	5.85/4.23
3m avg turnover (USDm)	3.5
Free float (%)	42.1
Issued shares (m)	4,010
Market capitalisation	MYR21.5B
	USD5.2B

Major shareholders:

Employees Provident Fund	41.9%
OSK Holdings Bhd.	10.1%
Kumpulan Wang Persaraan	6.0%

Price Performance



	-1M	-3M	-12M
Absolute (%)	4	(1)	12
Relative to index (%)	3	2	7

Source: FactSet

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Risk Rating & Score[1]	27.0
Score Momentum[2]	-2.6
Last Updated	06 May 2021
Controversy Score[3] (Updated: 01 Apr 2021)	2

Business Model & Industry Issues

- RHB Bank has the highest CET1 ratios among its domestic peers at 15.6% at the group level and 14.3% at the bank level as at end-Mar 2021. These ratios place the bank in a strong position to weather through the presently volatile economic environment both domestically and abroad.
- The banking sector is one of the transmission mechanisms for government stimulus programs under COVID-19 relief schemes, with an ongoing loan moratorium for the unemployed and reduced instalment payments for individuals that have suffered pay cuts. The Pemerkasa Plus plan, as announced in May 2021, extended this targeted repayment assistance programme (TRA) to B40 borrowers under Bantuan Sara Hidup/Bantuan Prihatin Rakyat, micro-enterprises with loan facilities <MYR150,000 and SMEs not permitted to operate during the MCO period. The TRA elevates social priorities over shareholders returns in the near term.
- RHB Bank displays no exceptional risks not typical of a large bank for ESG. The group's earnings are principally driven by its domestic operations, while regional contributions are relatively insignificant at this stage (<5%). This domestic concentration reduces its overall environment and corporate governance issues, in our view.

Material E issues

- RHB Bank is a constituent of FTSE4Good Bursa Malaysia and it has an MSCI ESG rating of AA. In 2020, it obtained an S&P Global ESG Score of 43/100, recording a +20-point improvement from 2019.
- Under its Green Financing commitment, RM3.1 billion was extended as at December 2020 to support green activities through lending, investment, advisory and capital market activities. It is committed to extending MYR5b by 2025 to support green activities and the transition to a low-carbon and climate resilient economy.
- RHB Bank was the Principal Adviser, Lead Manager and Lead Arranger for the issuance of Malaysia's 1st ever ESG-related Unrated Perpetual Sukuk of up to RM500 million.
- The Group recorded a 38% reduction in GHG emissions intensity per employee in 2020 compared to 2016.
- As at end-Mar 2021, the group's loan portfolio comprised a 2.3% exposure to palm oil, 2.3% O&G and 1% coal.

Material S issues

- The Board of Directors comprised 3 females (33%) and 7 males as at end-Dec 2020. Females comprised 59% of its total workforce in 2020.
- As at Dec 2020, total transactions via its digital channels increased to 75.5%. Internet banking registered an increase in customer penetration rate to 54% from 46.9% in 2019 and mobile banking increased to 22% from 16.6%.
- 85.7% of all customers use non-OTC channels, including Cards and ATM usage.
- In 2020, 61.3% of SME unsecured loans were acquired via SME online financing.
- The bank achieved an Employee Engagement Score of 92% in 2020, an improvement from 90% in 2019.

Key G metrics and issues

- RHB Bank has not had any material accounting & tax, lobbying & public policy, sanctions related, data privacy or security controversies in the past 5 years.
- RHB's BOD comprises 1 executive director/Managing Director, 1 non-independent non-executive Chairman, 6 independent non-executive directors and 2 non-independent non-executive directors as at end-2019.
- The Managing Director's remuneration was MYR4.1m in FY20, representing 0.2% of the group's pretax profit.
- The group discloses the remuneration of each individual Director in its annual report.
- IT expenses amounted to MYR271.9m in FY20 representing 8.0% of total operating expenses.
- RHB Bank is audited by PricewaterhouseCoopers, the world's second largest network of professional firms. PwC has been, at the very least, their auditors over the past 10 years.
- The EPF is a major shareholder of the group with a 41.0% stake as at 17 Jun 2021, which does imply that RHB Bank is a Government-linked company. Previous attempts been made to reduce this shareholding through potential M&As have since fallen through but this does not preclude future attempts at doing so.
- On 18 June 2021, RHB Bank said it had discovered an error in the issuance of current account e-statements sent via email to a number of customers, due to a technical issue at its external service partner. This affected less than 0.5% of its total retail customer base and the problem was swiftly addressed.

[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).

Uptick in requests for targeted repayment assistance (TRA)

Investors will recall that as at the end of March 2021, total loans approved under targeted repayment assistance (TRA) accounted for 15% of total loans. However, total loans outstanding under TRA was a lower 10% of total loans, due to the resumption of loan servicing for some of these accounts.

Retail loans approved under TRA totalled MYR16.5b (17% of total retail loans), but the outstanding was just MYR8.3b (9% of total retail loans). Of the MYR8.3b, loans under moratorium versus loans under reduced instalments were about 50:50.

For provisioning purposes, loans under moratorium are classified under Stage 2 and provided for accordingly, while provisions against loans under reduced instalments are dependent on the staging of such loans when they first entered into payment assistance.

With the current second lockdown, and the PEMERKASA Plus programme which extends the financial assistance to the B40 and micro-SMEs, there has been an uptick in consumer loan applications for TRA.

B40 loans totalled MYR14.4b end-Mar 2021, accounting for 15% of total retail loans. Of this sum, MYR4.8b (33% of total B40 loans) was under TRA as at end-Mar 2021, representing about 58% of total retail loans under TRA.

Commercial banking delinquency was 3.9% of outstanding amount under TRA as at end-Mar 2021. To note that delinquent accounts are not necessarily impaired loans but are mainly loans with some delays in repayments. Management is seeing an increase in SMEs applying for TRA.

Credit cost guidance maintained

Overall, the percentage of loans under TRA is expected to rise but management is comfortable with its credit cost guidance of 30bps for FY21 and believes that it is adequate despite the anticipated increase in applications. This compares against a credit cost of 58bps in FY20. Our forecasts assume a more conservative credit cost of 45bps for FY21 and 33bps for FY22.

Some mod loss to be expected still, offset by mod gain

RHB reported a modification (mod) loss of MYR37m in 1Q21, but this was offset by a mod gain of MYR33m. The bank expects to continue recording mod losses as applications come in for TRA, but these will be largely offset by mod gains.

Loan growth target of 4-5% still holds

Management maintains its loan growth target of 4-5% for FY21 against an annualized rate of 4.4% in 1Q21. SME loan growth has thus far been supported by loan disbursements under the various relief schemes announced last year. There is the likelihood that SME lending may taper off in the absence of these relief schemes, in our view, but economic recovery in 2H21 could prompt stronger loan demand. Consumer lending remains stable at this juncture. Our forecasts assume an FY21 loan growth of 4%.

Softer NIMs ahead

Net interest margin (NIM) was 2.16% in 1Q21 versus 1.96% (2.06% excluding mod loss) in FY20. The improvement in NIM has been driven by the repricing of deposits and proactive funding cost management. However, the bulk of fixed deposits had repriced by March 2021 while CASA growth is expected to taper off as consumer spending improves alongside the economic recovery. As such, management expects a tapering off of NIMs in the coming quarters and maintains its NIM target of 2.06% in FY21. The house view is for no interest rate changes this year. Our forecasts incorporate management's 2.06% NIM assumption for FY21.

Supporting non-interest income

One of the group's strategies in combating the rise in bond yields and the corresponding marked-to-market (MTM) losses on investments, has been to accelerate the monetization of the FVOCI reserves. FVOCI reserves stood at MYR776m end-Mar 2021 versus MYR1.86b end-Dec 2020. We expect the monetization programme to continue into 2Q21, with gains on investment disposals buffering MTM losses if any. It is envisaged that 2H21 could see the yield curves move up and management will look to rebuild the investment portfolio then. Our forecasts assume a 13% YoY decline in NOII this year.

Managing expenses

In 1Q21, operating expenses picked up 8% YoY with personnel expenses up 10% YoY and marketing expenses jumping 27% YoY. The latter was led by better sales which led to higher commissions being paid. Cost management is an important area of focus and the aim is still to keep cost growth at less than 5% in FY21. Our forecasts assume a 4.2% growth in FY21 operating expenses.

e-statement error

Pertaining to the recent issue of e-statements having been sent to the wrong customers, management points out that the error was detected early and affected just 0.5% of customers. The error was on the part of its third-party service provider, and the issue was swiftly addressed.

Participating in digital banking

Management views its recent MOU to joint venture on a 40:60 basis with Boost Holdings (Axiata's 75.4% subsidiary) as a strategic move. This move will allow the bank to tap into a relatively separate market segment (of the under-served population), while over the long term, there is the possibility of referral work from the digital to the conventional bank as income levels rise and demand increases for more sophisticated products.

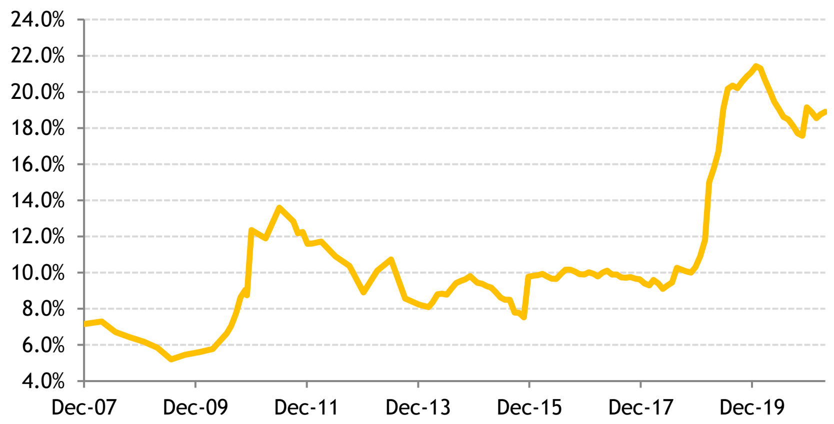
External estimates would indicate that the capital requirement for the digital bank over time could be about MYR500m, of which RHB's portion would be about MYR200m. However, to note that the initial capital requirement is just MYR100m, of which RHB's portion would be MYR40m.

Take-up for DRP likely to be decent

CET1 15.6% end-Mar 2021, 14.3% at the bank level. There will be a further 27bps improvement in CET1 from disposal of RHB Securities Singapore, to be accounted for in 2Q21. RHB's capital levels are comfortably above its minimum ICAAP levels.

Management had previously said that it would study the take-up rate for its maiden dividend reinvestment plan (DRP) before deciding on whether it would raise its dividend payout (35% in FY20 versus 50% in FY19). Given that the DRP price of RHB's final DPS of 7.65sen was fixed at MYR4.61 or an attractive 10% discount to VWAP, the take-up rate should have been quite strong, in our view, which would be a positive. We have assumed a payout ratio of 40% in FY21.

Foreign shareholding in RHB Bank (18.90% end-Apr 2021)

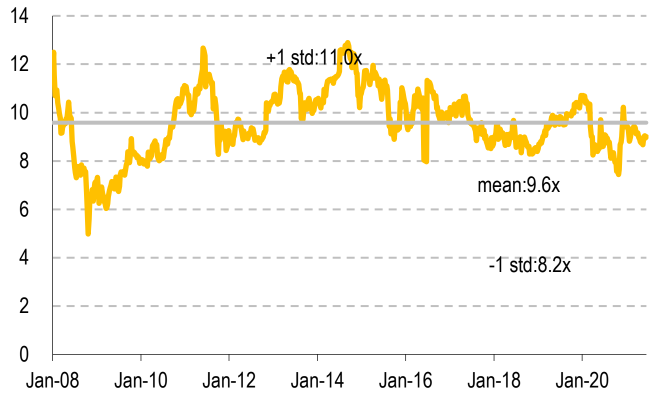


Source: Bank

Risk statement

As the fourth largest domestic financial institution in Malaysia in terms of asset size, any economic slowdown in the country would have a knock-on effect on the group's operating performance and hence potentially our estimates, rating, and target price. Volatility in the O&G sector could result in asset quality issues for both its Malaysia and Singapore loan exposures.

One-year forward rolling PER (x)



Source: Bloomberg, Maybank KE

One-year forward rolling P/BV (x)

Source: Bloomberg, Maybank KE

FYE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Key Metrics					
Core P/E (x)	9.2	10.0	9.4	8.7	8.1
Core FD P/E (x)	9.2	10.0	9.4	8.7	8.1
P/BV (x)	0.9	0.8	0.8	0.7	0.7
P/NTA (x)	1.0	0.9	0.9	0.8	0.8
Net dividend yield (%)	5.4	3.2	4.3	4.6	5.0
INCOME STATEMENT (MYR m)					
Interest income	8,088.8	6,569.4	8,590.3	8,846.9	9,094.1
Interest expense	(4,486.3)	(3,226.0)	(5,030.5)	(5,136.8)	(5,334.8)
Net interest income	**3,602.5**	**3,343.4**	**3,559.8**	**3,710.1**	**3,759.3**
Islamic banking income	1,614.5	1,665.7	1,865.5	2,089.4	2,340.1
Net insurance income	193.0	216.5	227.3	238.7	250.6
Net fees and commission	896.8	1,027.7	1,058.6	1,090.3	1,123.0
Other income	750.7	932.5	683.8	384.1	383.4
Total non-interest income	**1,840.5**	**2,176.7**	**1,969.7**	**1,713.0**	**1,757.0**
Operating income	**7,057.5**	**7,185.7**	**7,395.0**	**7,512.6**	**7,856.5**
Staff costs	(2,013.1)	(2,041.6)	(2,102.8)	(2,165.9)	(2,230.9)
Other operating expenses	(1,374.3)	(1,345.1)	(1,364.6)	(1,384.3)	(1,404.4)
Operating expenses	**(3,387.3)**	**(3,386.7)**	**(3,467.4)**	**(3,550.2)**	**(3,635.3)**
Pre-provision profit	**3,670.2**	**3,799.0**	**3,927.6**	**3,962.3**	**4,221.2**
Loan impairment allowances	(275.8)	(1,145.1)	(856.6)	(658.5)	(664.9)
Other allowances	0.0	(9.5)	0.0	0.0	0.0
Associates & JV income	(0.0)	0.0	0.0	0.0	0.0
Pretax profit	**3,394.3**	**2,644.4**	**3,071.0**	**3,303.8**	**3,556.4**
Income tax	(862.3)	(639.9)	(767.8)	(826.0)	(889.1)
Minorities	(5.4)	(6.6)	(4.6)	(5.0)	(5.3)
Discontinued operations	(44.2)	34.7	0.0	0.0	0.0
Reported net profit	**2,482.4**	**2,032.5**	**2,298.7**	**2,472.9**	**2,661.9**
Core net profit	**2,526.7**	**2,186.2**	**2,298.7**	**2,472.9**	**2,661.9**
BALANCE SHEET (MYR m)					
Cash & deposits with banks	12,723.6	14,973.7	15,722.4	16,508.5	17,334.0
Sec. under resale agreements	0.0	0.0	0.0	0.0	0.0
Derivatives financial assets	0.0	0.0	0.0	0.0	0.0
Dealing securities	4,623.4	4,462.1	4,685.2	4,919.5	5,165.4
Available-for-sale securities	54,054.7	58,908.5	64,799.4	69,983.3	75,582.0
Investment securities	0.0	0.0	0.0	0.0	0.0
Loans & advances	173,236.7	182,424.9	189,595.1	197,178.9	205,066.1
Central bank deposits	4,549.3	612.7	5,661.9	5,884.2	6,115.3
Investment in associates/JVs	9.5	0.0	0.0	0.0	0.0
Insurance assets	0.0	0.0	0.0	0.0	0.0
Fixed assets	1,104.1	1,163.2	1,186.4	1,210.1	1,234.3
Intangible assets	3,284.0	3,290.4	3,290.4	3,290.4	3,290.4
Other assets	4,007.2	5,314.5	5,426.0	5,542.0	5,662.5
Total assets	**257,592.5**	**271,150.0**	**290,366.9**	**304,517.1**	**319,450.1**
Deposits from customers	190,555.2	203,470.8	211,609.6	220,074.0	228,877.0
Deposits from banks & FIs	21,539.3	21,035.2	21,876.6	22,751.7	23,661.7
Derivatives financial instruments	0.0	0.0	0.0	0.0	0.0
Subordinated debt	2,724.2	2,718.7	2,718.7	2,718.7	2,718.7
Other securities in issue	3,296.8	3,545.2	4,145.2	4,145.2	4,145.2
Other borrowings	6,878.8	4,785.5	4,985.4	5,195.2	5,415.5
Insurance liabilities	0.0	0.0	0.0	0.0	0.0
Other liabilities	6,787.3	8,538.0	16,591.5	19,703.8	23,101.0
Total liabilities	**231,781.7**	**244,093.4**	**261,927.0**	**274,588.5**	**287,919.1**
Share capital	6,994.1	6,994.1	6,994.1	6,994.1	6,994.1
Reserves	18,781.3	20,029.7	21,408.4	22,892.2	24,489.3
Shareholders' funds	25,775.4	27,023.8	28,402.5	29,886.3	31,483.4
Preference shares	0.0	0.0	0.0	0.0	0.0
Minority interest	35.4	32.7	37.3	42.3	47.6
Total equity	25,810.8	27,056.6	28,439.8	29,928.5	31,531.0
Total liabilities & equity	**257,592.5**	**271,150.0**	**290,366.9**	**304,517.1**	**319,450.1**

FYE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Key Ratios					
Growth (%)					
Net interest income	(1.4)	(7.2)	6.5	4.2	1.3
Non-interest income	6.9	18.3	(9.5)	(13.0)	2.6
Operating expenses	0.9	(0.0)	2.4	2.4	2.4
Pre-provision profit	6.4	3.5	3.4	0.9	6.5
Core net profit	9.6	(13.5)	5.1	7.6	7.6
Gross loans	4.3	5.6	4.0	4.0	4.0
Customer deposits	6.5	6.8	4.0	4.0	4.0
Total assets	5.9	5.3	7.1	4.9	4.9
Profitability (%)					
Non-int. income/Total income	26.1	30.3	26.6	22.8	22.4
Average lending yields	4.09	3.26	3.90	3.88	3.86
Average cost of funds	2.47	1.73	2.69	2.68	2.68
Net interest margin	2.20	1.98	2.03	2.06	2.06
Cost/income	48.0	47.1	46.9	47.3	46.3
Liquidity (%)					
Loans/customer deposits	90.9	89.7	89.6	89.6	89.6
Asset quality (%)					
Net NPL	1.1	0.9	1.3	1.3	1.3
Gross NPL	2.0	1.7	2.3	2.3	2.3
(SP+GP)/average gross loans	0.2	0.6	0.5	0.3	0.3
Loan loss coverage	84.5	115.9	89.0	89.0	89.0
Capital adequacy (%)					
CET1	16.3	16.2	16.0	16.2	16.4
Tier 1 capital	16.3	16.2	16.2	16.4	16.6
Risk-weighted capital	18.6	18.4	18.2	18.3	18.4
Returns (%)					
ROAE	10.3	8.3	8.3	8.5	8.7
ROAA	1.0	0.8	0.8	0.8	0.9
Shareholders equity/assets	10.0	10.0	9.8	9.8	9.9

Source: Company; Maybank

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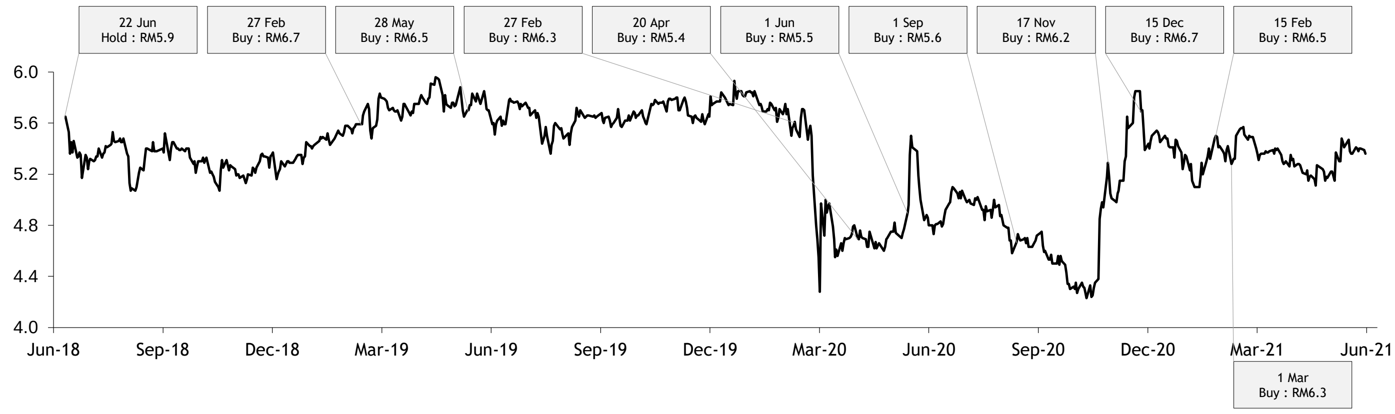

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