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Singapore Banks

Push Release

POSITIVE [Unchanged]

Banks

Singapore

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The case for write-backs is becoming stronger

The US banks are aggressively reversing 2020 provisions as economic growth takes off and COVID-related asset quality fears fail to materialize. Strengthening growth and good progress in vaccinations offer a supportive backdrop for Singapore banks to do the same. Fresh infections regionally makes timing hard to predict, but just matching the average US pace of write-backs could add 15-18% to 2021E earnings. Improved NIMs, stronger loan growth, rising non-interest income and falling provisions should set the sector for faster earnings momentum in 2Q21. We prefer OCBC and DBS for the strongest coupling to these drivers, while also offering the highest probability for earlier provision write-backs.

Upside risks from reserve releases…

US banks are reporting strong 2Q21 results. Reserve write-backs have contributed a large share of the beats and on average 40% of provisions taken in 2020 have been released so far, we estimate. Managements claim this is driven by faster than expected US economic recovery and the absence of pandemic-induced asset quality issues. This has positive read-throughs for Singapore banks. Vaccinations are progressing well with herd immunity on track for 4Q21. GDP is forecasted to expand by 6.8% in 2021E – the highest pace of growth since 2010 driven by strong external demand. Concurrently, new NPL formation as a proportion of loans have fallen by a third in 1Q21 vs. 2020, and NPL upgrades have doubled during the same period. This is a conducive environment for provisions write-backs.

…potential to add 15-18% to EPS

Assuming the Singapore banks release 40% of provisions taken in 2020 (to match the US average), we estimate it could add 15-18% to 2021E earnings. We expect DBS to lead releases (it has already written back SGD190m of general provisions in 1Q21) followed by OCBC, given greater exposure to North Asia where recovery is strongly underway. UOB has the largest theoretical potential for releases - its GP+RLAR is 74% of NPLs vs. 63% for DBS. Yet, rising COVID cases & fresh lockdowns in ASEAN (22% of loan book) may drive UOB to take a relatively more cautious approach, in our view.

Expect strengthening momentum in 2Q21. Positive

The US banks reported rising opex, particularly employee costs in 1H21. Similar trends are likely for Singapore banks as business activities rise, but borders remain closed creating bottlenecks in labour availability. While we estimate opex to rise 8% YoY in 2021E, we think the risks here are on the upside. Nevertheless, stabilizing NIMs, improved loan growth and higher non-interest income from wealth and loan related fees together with falling provisions should drive earnings momentum higher in 2Q21. Our preferred picks ahead of results (OCBC, UOB 4 Aug, DBS 5 Aug) are OCBC and DBS for stronger PPOP growth from North Asia together with lower provisions. Potential increases in dividends, now that the MAS dividend cap has expired, is a further upside risk.

Stock	Bloomberg code	Mkt cap (USD'm)	Rating	Price (LC)	TP (LC)	Upside (%)	P/E (x) 21E	P/E (x) 22E	P/B (x) 21E	P/B (x) 22E	Div yld (%) 21E	Div yld (%) 22E
DBS Group	DBS SP	57,178	Buy	30.21	33.71	12	11.5	10.5	1.3	1.2	3.6	4.7
OCBC	OCBC SP	39,864	Buy	12.12	14.17	17	10.9	9.7	1.0	1.0	3.9	5.1
UOB	UOB SP	32,182	Buy	26.01	29.34	13	10.7	9.5	1.0	1.0	4.6	5.2

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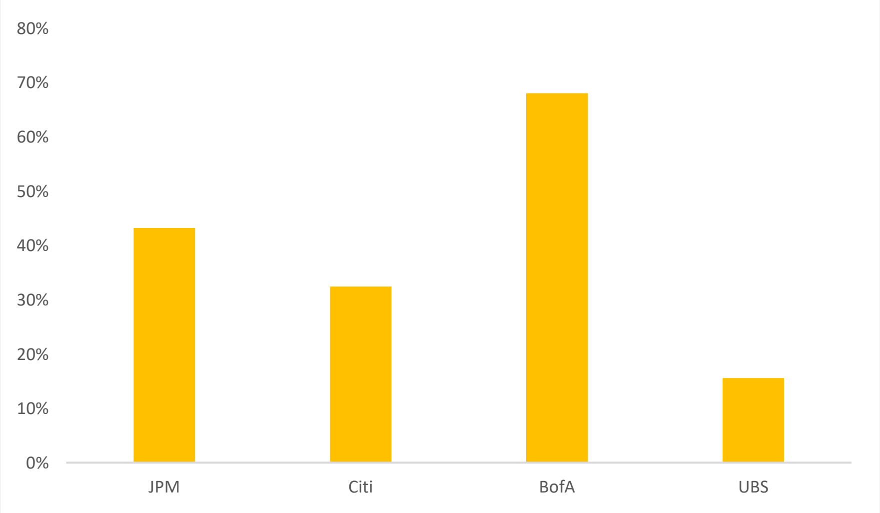
Upside risks to Reserve releases

US banks are reporting strong 2Q21 results. Reserve write-backs have contributed a large share of the beats and on average 40% of provisions taken in 2020 have been released so far, we estimate.

Bank of America (BAC US, USD38.46, Not Rated) has reversed back nearly 70% of the provisions it took in 2020, while JP Morgan (JPM US, USD149.71, Not Rated) has written back 43%. For most European banks, 2Q21 results are still pending, but UBS (UBSG SW, SFR14.46. Not Rated) has already written back 16% of 2020 credit charges despite a slower rate of recovery than the US.

Fig 1: US/EU banks: 1H21 credit reserve releases for loans as a percentage of total credit costs taken during 2020



Source: Company data, Maybank Kim Eng

In all cases, Managements claim write-backs are being catalyzed by faster than expected economic recovery and the absence of pandemic-induced asset quality issues.

This has positive read-throughs for Singapore banks, in our view. Vaccinations are progressing well (49% of the population is fully vaccinated) with herd immunity on track for 4Q21, or earlier.

MKE's macroeconomics team is forecasting GDP to expand by 6.8% in 2021E – the highest pace of growth since 2010 driven by strong external demand.

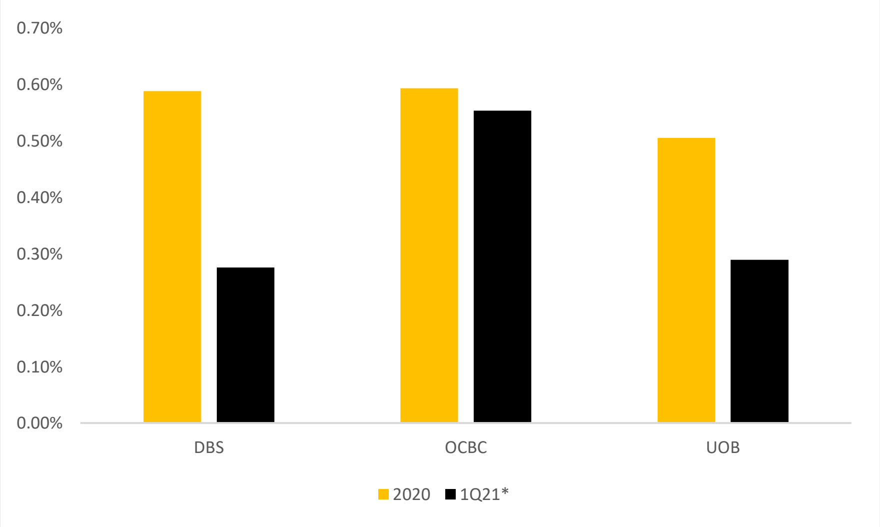
Fig 2: Singapore macro forecasts

	2017	2018	2019	2020	2021E	2022E
Real GDP (%)	4.5	3.5	1.3	-5.4	6.8	3.5
Private Consumption (%)	3.1	4.0	3.3	-14.1	6.1	3.8
Government Consumption (%)	3.1	3.2	3.4	12.6	-2.2	3.4
Gross Fixed Capital Formation (%)	5.4	-4.3	1.2	-13.7	8.8	5.5
Exports of Goods & Services (%)	7.1	7.7	0.1	-4.3	5.8	4.4
Imports of Goods & Services (%)	7.8	7.5	0.2	-7.1	5.6	5.0
Current Account Balance (% of GDP)	17.3	15.4	14.3	17.6	16.5	17.0
Fiscal Balance (% of GDP)	2.3	0.7	-0.3	-13.9	-2.2	0.5
Inflation Rate (%, period average)	0.6	0.4	0.6	-0.2	1.8	1.4
Unemployment Rate (%, period average)	2.2	2.1	2.3	3.0	2.7	2.4
Exchange Rate (per USD, end-period)	1.3	1.36	1.35	1.32	1.32	1.29
3M SIBOR (% p.a., end-period)	1.5	1.89	1.77	0.41	0.45	0.45

Source: Factset, Maybank Kim Eng

Concurrently, new NPL formation as a proportion of loans have fallen by a third in 1Q21 vs. 2020. For DBS and UOB, new NPL formation fell by nearly half during this period, while OCBC has seen a slower fall from their Malaysia exposure.

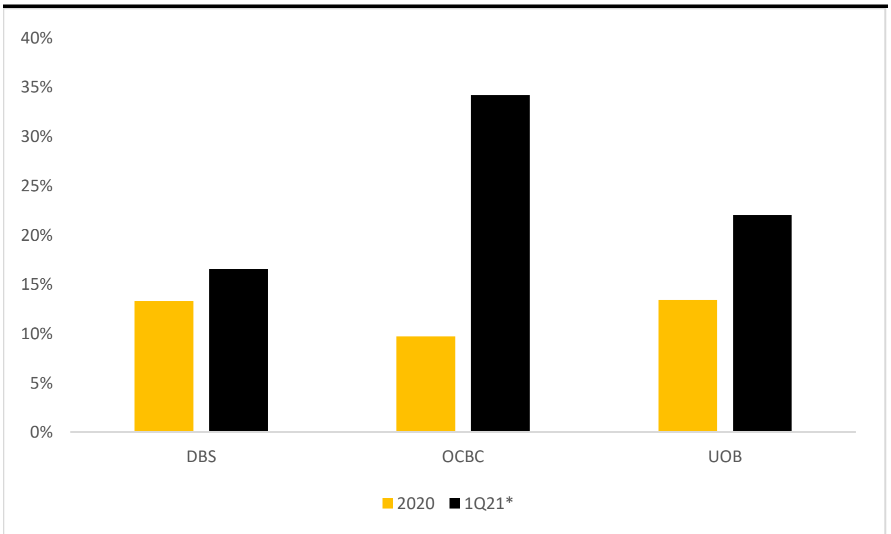
Fig 3: New NPA formation as a percentage of total loans



** Annualized*
Source: Maybank Kim Eng

NPL upgrades have doubled during the same period. Particularly for OCBC, NPL upgrades have tripled between 2020 and 1Q21. This pace is likely to accelerate as North Asian recovery takes shape.

Fig 4: Upgrades, settlements and recoveries as a percentage of NPLs



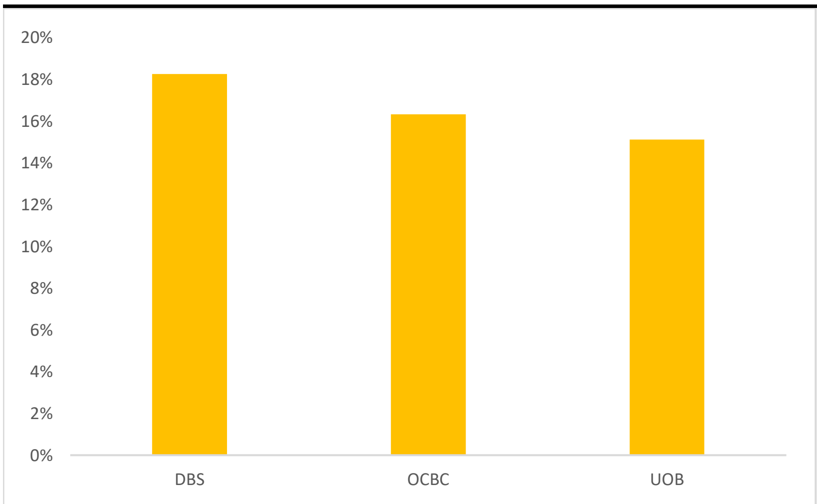
** Annualized*
Source: Maybank Kim Eng

We believe the improved economic outlook regionally together with better than expected asset quality creates a conducive environment for provisions write-backs going forward.

Potential for EPS upside

On average, the US/EU banks have so far released 40% of the provisions taken during 2020. All things equal, assuming the Singapore banks release 40% of provisions taken in 2020, we estimate it could add 15-18% to 2021E earnings.

Fig 5: 2021E EPS upside from writing-back 40% of 2020 credit charges



Source: Company data, Maybank Kim Eng

We expect DBS to lead releases (it has already written back SGD190m of general provisions in 1Q21) followed by OCBC, given their greater exposure to North Asia where recovery is strongly underway.

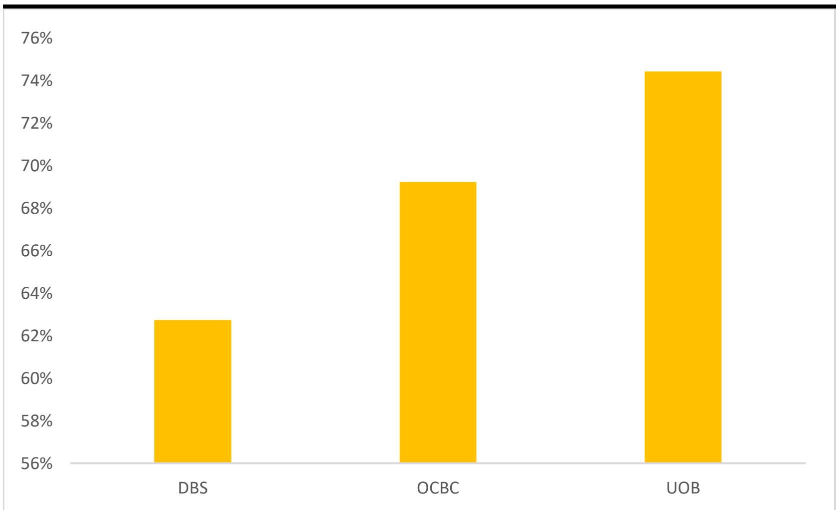
Fig 6: Credit charges taken by Singapore banks 2020

	Net Credit Charges Taken in 2020 (SGDm)	40% write-back (SGDm)
DBS	3,066	1,221
OCBC	2,043	813
UOB	1,554	619

Source: Company data, Maybank Kim Eng

UOB has the largest theoretical potential for releases - its General Provisions plus RLAR is 74% of NPLs vs. 63% for DBS.

Fig 7: General Provisions + RLAR as a percentage of NPLs 1Q21



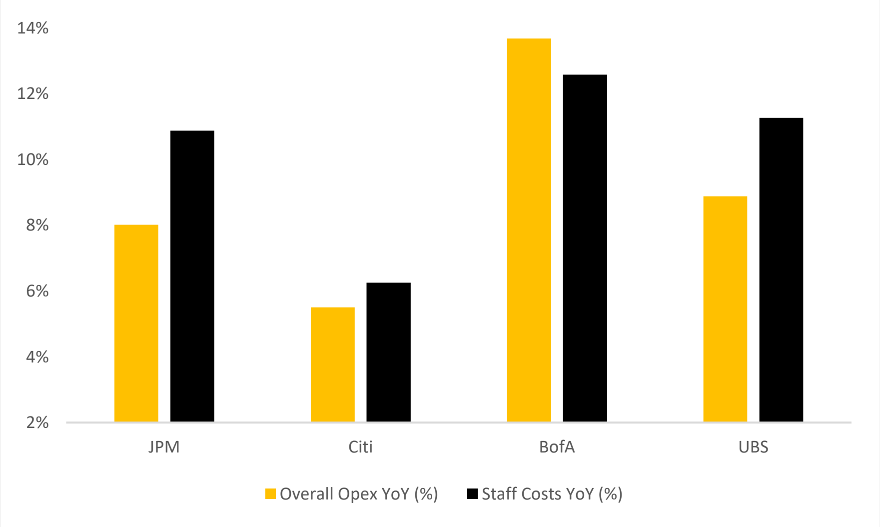
Source: Company data, Maybank Kim Eng

Yet, rising COVID cases & fresh lockdowns in ASEAN (22% of loan book) may drive UOB to take a relatively more cautious approach, in our view.

Expect strengthening momentum in 2Q21

The US banks reported rising opex, particularly employee costs in 1H21. Similar trends are likely for Singapore banks, as business activities rise, but borders remain closed creating bottlenecks in labour availability.

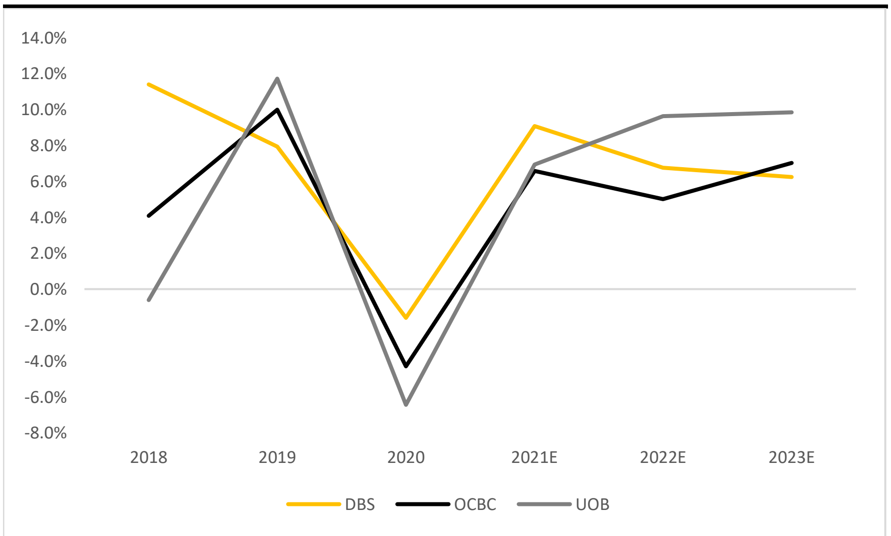
Fig 8: US/EU banks 1H20 vs. 1H21 opex increase YoY (%)



Source: Company data, Maybank Kim Eng

While we estimate opex to rise 8% YoY in 2021E, we think the risks here are on the upside. Additional digitalization expenses as the sector calibrates customer touchpoints to incorporate more online interactions post-COVID, could also catalyse higher costs, in our view.

Fig 9: Opex growth YoY (%)



Source: Maybank Kim Eng

Nevertheless, stabilizing NIMs, improved loan growth and higher non-interest income from wealth and loan related fees together with falling provisions should drive earnings momentum higher in 2Q21.

Our preferred picks ahead of 1H21 results (OCBC, UOB reporting on 4 Aug, DBS 5 Aug) are OCBC and DBS for stronger PPOP growth from North Asia together with lower provisions.

Fig 10: Singapore banks key assumptions and 2Q21E expectations

SGDm	DBS			UOB			OCBC		
	2020	2021E	y-o-y (%)	2020	2021E	y-o-y (%)	2020	2021E	y-o-y (%)
Net Interest Income	9,076	9,002	-1%	6,036	6,487	7%	5,966	6,072	2%
Non-Interest Income	5,516	6,142	11%	3,141	3,607	15%	4,173	4,840	16%
Total Income	14,592	15,144	4%	9,177	10,095	10%	10,139	10,912	8%
PPOP	8,434	8,427	0%	4,993	5,620	13%	5,596	6,070	8%
Allowances for credit and other losses	(3,066)	(749)	-76%	(1,554)	(763)	-51%	(2,043)	(746)	-63%
PBT	5,368	7,678	43%	3,537	4,955	40%	4,165	6,028	45%
Net Profit	4,756	6,718	41%	2,931	4,106	40%	3,728	5,124	37%
Core-Profit	4,721	6,683	42%	2,915	4,090	40%	3,586	4,982	39%
EPS	1.85	2.62	42%	1.73	2.43	40%	0.80	1.11	39%
Net Loans	371,171	401,637	8%	277,201	299,713	8%	263,538	278,686	6%
Total Deposits	464,850	485,468	4%	324,598	344,073	6%	314,907	326,032	4%
CAR	16.8%	16.9%	0.08%	18.4%	17.4%	-0.95%	17.9%	17.5%	-0.41%
	2Q20	2Q21E	y-o-y (%)	2Q20	2Q21E	y-o-y (%)	2Q20	2Q21E	y-o-y (%)
Core-Profit	1,247	1,558	25%	703	1,027	46%	730	1,160	59%

Source: Company data, Maybank Kim Eng

Globally, banking regulators have been easing dividend and other capital return restrictions imposed during 2020. The MAS dividend caps introduced during the start of the COVID pandemic have also expired, but guidance for the future are yet to be relieved. We believe, there is potential for relaxation, although a full lifting is unlikely given the regional COVID re-opening uncertainty. Nevertheless, any relaxation should drive upgrades to dividend yields, which should be a positive catalyst for the sector, in our view.

Fig 11: Regulatory dividend guidance changes in 2021

Regulators	New Dividend Guidance	Date of Announcement
Australian Prudential Regulation Authority	Approved higher bank dividend payments at the start of 2021, following the COVID-19 restriction for banks to cap shareholder payouts at 50% of profits.	15-Dec-20
Banco Central do Brasil	Following caps in 2020 restricting banks for paying more than the mandatory minimums of dividends established by law, banks are now able to distribute the higher of 30% of net profit or mandatory minimums since January 2021	10-Feb-21
Reserve Bank of India	Following a ban on dividend payments in FY21, banks may pay dividend from the profits for FY21, subject to the quantum of dividends being not more than 50% of the amount determined as per the dividend payout ratio prescribed	23-Apr-21
South Korea Financial Supervisory Service and Financial Services Commission	Has lifted the 20% dividend cap imposed during the Pandemic effective July 2021	25-Jun-21
US Federal Reserve	Following stress-tests in June 2021, the Fed has removed all restrictions on capital payouts	29-Jun-21
European Central Bank	ECB is scrapping dividend caps and share buybacks effective from 3Q21	1-Jul-21
Bank of England, UK	BoE has scrapped all dividend restrictions as of July 2021 following a partial easing in December 2020	13-Jul-21

Source: Media reports, Maybank Kim Eng

Appendix A: SG Banks Operating Summary

Fig 12: SG banks operating summary

	DBS	UOB	OCBC
Total Income (SGDm)			
2018	13,183	9,116	9,701
2019	14,544	10,030	10,871
2020	14,592	9,177	10,139
2021E	15,144	10,095	10,912
2022E	16,242	10,951	11,603
2023E	17,800	11,938	12,599
PPOP (SGDm)			
2018	7,385	5,113	5,385
2019	8,286	5,558	6,124
2020	8,434	4,993	5,596
2021E	8,427	5,620	6,070
2022E	9,071	6,046	6,519
2023E	10,181	6,551	7,158
Core-Net Profit (SGDm)			
2018	5,625	4,008	4,492
2019	6,391	4,343	4,869
2020	4,721	2,915	3,586
2021E	6,683	4,090	4,982
2022E	7,319	4,633	5,581
2023E	8,365	5,102	6,366
Core EPS growth y-o-y (%)			
2018	38%	18%	11%
2019	14%	8%	8%
2020	-26%	-33%	-26%
2021E	42%	40%	39%
2022E	10%	13%	12%
2023E	14%	10%	14%
Gross Loan growth y-o-y (%)			
2018	6.7%	10.9%	8.6%
2019	3.7%	2.7%	2.7%
2020	4.2%	4.7%	0.9%
2021E	8.0%	8.0%	5.8%
2022E	6.7%	6.9%	7.1%
2023E	5.8%	4.8%	7.8%
Net Interest Margin (%)			
2018	1.80%	1.75%	1.63%
2019	1.83%	1.74%	1.70%
2020	1.61%	1.53%	1.55%
2021E	1.51%	1.55%	1.55%
2022E	1.59%	1.58%	1.59%
2023E	1.70%	1.64%	1.67%
Gross NPL (%)			
2018	1.5%	1.5%	1.5%
2019	1.5%	1.5%	1.5%
2020	1.6%	1.6%	1.5%
2021E	1.6%	1.6%	1.6%
2022E	1.5%	1.5%	1.5%
2023E	1.4%	1.5%	1.5%
CET1 (%)			
2018	13.9%	13.9%	14.0%
2019	14.1%	14.3%	14.9%
2020	13.9%	14.7%	15.2%
2021E	14.0%	14.3%	15.0%
2022E	13.9%	13.7%	14.7%
2023E	14.0%	13.6%	14.2%

Source: Company data, Maybank Kim Eng

Appendix B: Singapore Banks Valuation Summary

Fig 13: Singapore Banks Valuation Summary

	DBS	UOB	OCBC
Ticker	DBS SP	UOB SP	OCBC SP
Market Cap (SGDm)	63,852	37,789	45,008
Share Price (SGD)	30.21	26.01	12.12
Target Price (SGD)	33.71	29.34	14.17
Upside/Downside (%)	12%	13%	17%
Recommendation	BUY	BUY	BUY
PE (x)			
2018	13.8	10.8	11.5
2019	12.1	10.0	11.0
2020	16.3	15.0	15.1
2021E	11.5	10.7	10.9
2022E	10.5	9.5	9.7
2023E	9.2	8.6	8.5
PB (x)			
2018	1.58	1.15	1.22
2019	1.51	1.09	1.13
2020	1.41	1.07	1.09
2021E	1.32	1.02	1.03
2022E	1.24	0.97	0.98
2023E	1.16	0.91	0.93
ROE (%)			
2018	11.7%	10.8%	11.1%
2019	12.8%	11.2%	10.9%
2020	8.9%	7.2%	7.4%
2021E	11.8%	9.8%	9.8%
2022E	12.1%	10.5%	10.4%
2023E	13.0%	11.0%	11.2%
ROA (%)			
2018	1.1%	1.1%	1.0%
2019	1.1%	1.1%	1.0%
2020	0.8%	0.7%	0.7%
2021E	1.0%	0.9%	0.9%
2022E	1.1%	1.0%	1.0%
2023E	1.2%	1.0%	1.1%
Dividend yield (%)			
2018	4.0%	4.6%	3.5%
2019	4.1%	5.0%	4.4%
2020	2.9%	3.0%	2.6%
2021E	3.6%	4.6%	3.9%
2022E	4.7%	5.2%	5.1%
2023E	5.3%	5.8%	5.8%

Source: Factset, Maybank Kim Eng

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