

# Singapore Company Update

## OCBC

Bloomberg: OCBC SP | Reuters: OCBC.SI

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DBS Group Research . Equity

24 Nov 2020

**BUY** (Upgrade from HOLD)

Last Traded Price (23 Nov 2020): S\$10.11 (STI : 2,848.78)

Price Target 12-mth: S\$11.00 (9% upside) (Prev S\$9.50)

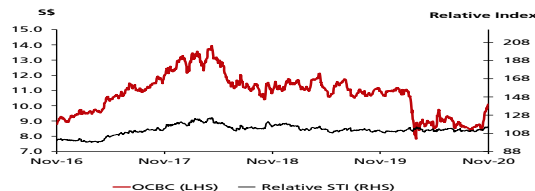
### Analyst

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### What's New

- Current valuations still inexpensive at near 1 SD below its average 15-year forward P/BV
- While OCBC faces ongoing NIM repricing, non-interest income should continue to contribute positively
- Some negatives, including lower net interest income and overhang from asset quality, have been priced in
- Upgrade to BUY, TP S\$11.0

### Price Relative



### Forecasts and Valuation

FY Dec (\$ m)	2019A	2020F	2021F	2022F
Pre-prov. Profit	6,124	5,583	5,430	5,766
Net Profit	4,869	3,267	3,998	4,481
Net Pft (Pre Ex.)	4,869	3,267	3,998	4,481
Net Pft Gth (Pre-ex) (%)	8.4	(32.9)	22.4	12.1
EPS (S cts)	110	74.1	90.7	102
EPS Pre Ex. (S cts)	110	74.1	90.7	102
EPS Gth Pre Ex (%)	4	(33)	22	12
Diluted EPS (S cts)	110	74.1	90.7	102
PE Pre Ex. (X)	9.2	13.6	11.1	9.9
Net DPS (S cts)	53.0	34.1	45.3	50.8
Div Yield (%)	5.2	3.4	4.5	5.0
ROAE Pre Ex. (%)	11.0	6.8	8.0	8.6
ROAE (%)	11.0	6.8	8.0	8.6
ROA (%)	1.0	0.7	0.8	0.9
BV Per Share (S cts)	1,070	1,110	1,155	1,206
P/Book Value (x)	0.9	0.9	0.9	0.8
Earnings Rev (%):		5	1	3
Consensus EPS (S cts):		74.4	94.3	108
Other Broker Recs:		B: 12	S: 1	H: 8

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P.



### Brain Box

(Our NEW Pilot Research Platform) is available to Institutional Investors on Demand. Please contact your DBS Institutional Sales contact for a demonstration.

### Share price to see support

#### Investment Thesis

**Inexpensive valuation; ongoing provisioning provides buffer.**

OCBC's share price has gained >10% since early November, when it was trading near trough valuations. We believe there is further room for OCBC's share price to re-rate amidst expectations of a gradual pick-up in long-end yields, as OCBC is seen as a proxy to economic recovery. OCBC's strong NPA coverage of 109% (2Q20: 101%) and ongoing provisioning of S\$1.8bn as of 9M20 will limit downside risks. While there may be further NIM headwinds into 4Q20 as OCBC's loan book continues to reprice, we believe its strength in non-interest income franchise should continue to contribute positively, providing some income support for FY21F.

**Some negatives have been priced in.** We believe the market has priced in lower net interest income impact into FY21F. As we expect some asset quality deterioration into 2H20 and 1H21, especially when the various moratoriums and reliefs expire, we believe the upside is capped at ~1x P/BV.

**Potential catalysts: Sustained business momentum.** We believe sustained business momentum and broader recovery in macroeconomic sentiments will catalyse the share price.

#### Valuation:

**Upgrade to BUY, TP S\$11.0.** Our revised TP of S\$11.10 is based on the Gordon Growth Model (9% ROE [previously 8%], 3% growth, 9% cost of equity). This is equivalent to ~c. 1x FY21F P/BV that is near 1 SD below its average 15-year forward P/BV multiple. We revise our earnings on better contributions from non-interest income.

#### Where we differ:

We remain conservative over OCBC's income outlook into FY21-22F; we believe that management is likely to continue adopting strict cost discipline to manage its bottom line.

#### Key Risks to Our View:

**Deteriorating asset quality.** A larger-than-expected NPL arising from generic sectors and/or commodity-related exposure, as well as a worse-than-expected COVID-19 pandemic situation globally could unwind expectations of credit cost and NPL declines, and pose risks to earnings. Further, unemployment arising from recession could pose additional risks to mortgages and unsecured consumer lending, among others.

#### At A Glance

Issued Capital (m shrs)	4,473
Mkt. Cap (S\$m/US\$m)	45,224 / 33,661
Major Shareholders (%)	
Selat Pte Ltd	11.8
Free Float (%)	88.2
3m Avg. Daily Val (US\$m)	38.0
GIC Industry : Financial / Banks	



Live more, Bank less

## WHAT'S NEW

### Share price to see support

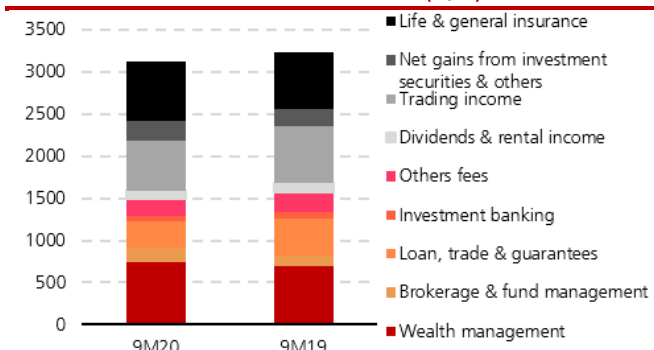
#### Inexpensive valuation; ongoing provisioning provides buffer.

While Hin Leong accounted for most of special allowances across banks in 1Q20, OCBC also took the opportunity in 2Q20 to further write down the remaining offshore support vessel NPLs, resulting in higher special allowances. Management is now guiding for peak NPL ratio and credit costs to come in at the lower end of the 2.5-3.5% range and 100-130bps credit costs through FY20-21F (\$3-3.5bn) previously guided. We believe that OCBC's strong NPA coverage of 109% (2Q20: 101%) and ongoing provisioning of \$1.8bn as of 9M20 will limit downside risks and we expect further provisions to be written in 4Q20 to pave the way for ROE and earnings recovery into FY21F.

**Continued management of cost of deposits.** In the meantime, OCBC continues to manage down cost of deposits. W.e.f. October 2020, its flagship deposit account could see up to a ~17-bp decrease in interest rates for the bulk of its accounts. We believe this should partially mitigate loan yield decline as the loan book continues to reprice into 4Q20 on lower interest rates.

**Support from non-interest income franchise.** There may be further NIM headwinds into 4Q20 as OCBC's loan book continues to reprice. However, we believe the bank's strength in non-interest income franchise should continue to contribute positively, providing some income support for FY21F, alongside good activity levels for wealth management and improved outlook for Great Eastern Holdings.

#### OCBC: Non-interest income breakdown (\$m)



Source: Company, DBS Bank

**Overhang from scrip dividend policy removed.** There have been concerns that OCBC's steep discount (i.e. 10%) on its scrip dividends may signal management's intention of future acquisitions, given that OCBC's strong capital position may not have warranted the discount factor. As management has stated that there are no M&A plans in place, we believe that the overhang may have been removed. Should there be no further M&A plans in place, with the upcoming RWA savings from HKMA's approval of WHB-IRAB transition earliest by end-2020, we believe that excess capital at the end of the credit cycle may be returned to shareholders.

#### Company Background

The OCBC Bank group of businesses (OCBC) comprises a family of companies owned by Singapore's longest-established local bank.

#### Historical PE and PB band



Source: Bloomberg Finance L.P., DBS Bank estimates



Source: Bloomberg Finance L.P., DBS Bank estimates

**Key Assumptions**

FY Dec	2018A	2019A	2020F	2021F	2022F
Gross Loans Growth	8.7	2.7	1.4	3.9	4.8
Customer Deposits Growth	4.1	2.5	6.0	4.0	4.0
Yld. On Earnings Assets	3.2	3.4	2.7	2.6	2.6
Avg Cost Of Funds	1.6	1.7	1.2	1.1	1.1

**Income Statement (\$\$ m)**

FY Dec	2018A	2019A	2020F	2021F	2022F
Net Interest Income	5,890	6,331	5,980	5,819	6,068
Non-Interest Income	3,811	4,540	4,193	4,425	4,642
<b>Operating Income</b>	<b>9,701</b>	<b>10,871</b>	<b>10,173</b>	<b>10,244</b>	<b>10,710</b>
Operating Expenses	(4,316)	(4,747)	(4,590)	(4,814)	(4,945)
<b>Pre-provision Profit</b>	<b>5,385</b>	<b>6,124</b>	<b>5,583</b>	<b>5,430</b>	<b>5,766</b>
Provisions	(288)	(890)	(2,042)	(970)	(713)
Associates	455	566	583	600	618
Exceptionals	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>5,552</b>	<b>5,800</b>	<b>4,125</b>	<b>5,061</b>	<b>5,672</b>
Taxation	(877)	(778)	(652)	(810)	(907)
Minority Interests	(183)	(153)	(206)	(253)	(284)
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>4,492</b>	<b>4,869</b>	<b>3,267</b>	<b>3,998</b>	<b>4,481</b>
Net Profit before Except.	4,492	4,869	3,267	3,998	4,481
<b>Growth (%)</b>					
Net Interest Income Gth	8.6	7.5	(5.5)	(2.7)	4.3
Net Profit Gth bef Except	11.2	8.4	(32.9)	22.4	12.1
<b>Margins, Costs &amp; Efficiency (%)</b>					
Spread	1.6	1.7	1.5	1.5	1.5
Net Interest Margin	1.7	1.8	1.6	1.5	1.5
Cost-to-Income Ratio	44.5	43.7	45.1	47.0	46.2
<b>Business Mix (%)</b>					
Net Int. Inc / Opg Inc.	60.7	58.2	58.8	56.8	56.7
Non-Int. Inc / Opg inc.	39.3	41.8	41.2	43.2	43.3
Fee Inc / Opg Income	20.9	19.5	19.8	21.2	21.9
Oth Non-Int Inc/Opg Inc	18.3	22.2	21.4	22.0	21.5
<b>Profitability (%)</b>					
ROAE Pre Ex.	11.4	11.0	6.8	8.0	8.6
ROAE	11.4	11.0	6.8	8.0	8.6
ROA Pre Ex.	1.0	1.0	0.7	0.8	0.9
ROA	1.0	1.0	0.7	0.8	0.9

Provisions may have peaked in FY20F

Source: Company, DBS Bank

## Quarterly / Interim Income Statement (\$\$ m)

FY Dec	3Q2019	4Q2019	1Q2020	2Q2020	3Q2020
Net Interest Income	1,600	1,610	1,626	1,483	1,421
Non-Interest Income	1,055	1,312	864	1,142	1,118
<b>Operating Income</b>	<b>2,655</b>	<b>2,922</b>	<b>2,490</b>	<b>2,625</b>	<b>2,539</b>
Operating Expenses	(1,158)	(1,292)	(1,135)	(1,107)	(1,124)
<b>Pre-Provision Profit</b>	<b>1,497</b>	<b>1,630</b>	<b>1,355</b>	<b>1,518</b>	<b>1,415</b>
Provisions	(323)	(207)	(657)	(750)	(350)
Associates	156	94	165	163	153
Exceptionals	0	0	0	0	0
<b>Pretax Profit</b>	<b>1,330</b>	<b>1,517</b>	<b>863</b>	<b>931</b>	<b>1,218</b>
Taxation	(139)	(220)	(165)	(201)	(190)
Minority Interests	(19)	(54)	0	0	0
<b>Net Profit</b>	<b>1,172</b>	<b>1,243</b>	<b>698</b>	<b>730</b>	<b>1,028</b>

## Growth (%)

Net Interest Income Gth	0.8	0.6	1.0	(8.8)	(4.2)
Net Profit Gth	(4.2)	6.1	(43.8)	4.6	40.8

## Balance Sheet (\$\$ m)

FY Dec	2018A	2019A	2020F	2021F	2022F
Cash/Bank Balance	18,748	23,201	22,472	20,032	20,833
Government Securities	27,776	28,662	31,528	32,789	34,101
Inter Bank Assets	39,035	35,813	38,268	39,648	41,487
Total Net Loans & Adv.	255,193	262,045	263,917	273,434	286,115
Investment	25,542	28,533	36,948	38,281	40,056
Associates	3,183	3,638	4,221	4,821	5,440
Fixed Assets	4,217	4,467	4,690	4,925	5,171
Goodwill	5,093	4,980	5,160	5,160	5,160
Other Assets	11,889	13,014	13,107	13,580	14,209
Life Ass Fund Inv Assets	76,867	87,338	90,832	93,556	96,363
<b>Total Assets</b>	<b>467,543</b>	<b>491,691</b>	<b>511,144</b>	<b>526,226</b>	<b>548,935</b>
Customer Deposits	295,412	302,851	321,022	333,863	347,217
Inter Bank Deposits	7,576	8,250	15,126	14,390	20,368
Debts/Borrowings	30,272	29,388	23,596	23,596	23,596
Others	15,963	18,153	16,380	17,105	17,959
Minorities	1,255	1,441	1,647	1,900	2,184
Shareholders' Funds	42,137	47,162	48,926	50,925	53,166
Life Ass Fund Liabs	74,928	84,446	84,446	84,446	84,446
<b>Total Liab&amp; S/H's Funds</b>	<b>467,543</b>	<b>491,691</b>	<b>511,144</b>	<b>526,226</b>	<b>548,935</b>

Source: Company, DBS Bank

## Financial Stability Measures (%)

FY Dec	2018A	2019A	2020F	2021F	2022F
<b>Balance Sheet Structure</b>					
Loan-to-Deposit Ratio	86.4	86.5	82.2	81.9	82.4
Net Loans / Total Assets	54.6	53.3	51.6	52.0	52.1
Investment / Total Assets	5.5	5.8	7.2	7.3	7.3
Cust . Dep./Int. Bear. Liab.	88.6	88.9	89.2	89.8	88.8
Interbank Dep / Int. Bear.	2.3	2.4	4.2	3.9	5.2
<b>Asset Quality</b>					
NPL / Total Gross Loans	1.5	1.5	2.0	2.5	1.8
NPL / Total Assets	0.8	0.8	1.0	1.3	1.0
Loan Loss Reserve Coverage	57.4	63.2	80.5	73.7	108.5
Provision Charge-Off Rate	0.1	0.3	0.8	0.3	0.2
<b>Capital Strength</b>					
Total CAR	16.5	16.9	16.4	16.2	16.2
Tier-1 CAR	14.0	14.9	14.5	14.4	14.5

Strong capital ratios

Source: Company, DBS Bank

## Target Price &amp; Ratings History



Note: Share price and Target price are adjusted for corporate actions.

S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	24 Feb 20	10.92	11.50	HOLD
2:	05 Mar 20	10.42	11.00	HOLD
3:	17 Mar 20	8.61	8.60	HOLD
4:	23 Apr 20	8.65	7.90	HOLD
5:	08 May 20	8.88	7.90	HOLD
6:	21 Jul 20	9.21	9.30	HOLD
7:	07 Aug 20	8.72	9.30	HOLD
8:	05 Nov 20	8.93	9.50	HOLD

Source: DBS Bank

Analyst: Rui Wen LIM

DBS Bank recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**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*

Completed Date: 24 Nov 2020 07:34:19 (SGT)

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