Singapore Industry Focus

Singapore Banks

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DBS Group Research . Equity

1 Apr 2021

What is next for dividends?

- MAS likely to ease its stance on dividend cap imposed as Singapore banks have preserved sufficient capital
- We expect higher dividends for FY21F on gradual relaxation of dividend caps; a two-stage relaxation seems to be a more likely scenario
- Banks may adjust high capital buffers through some special dividends from FY22F, subject to asset quality and corporate actions
- Maintain BUY on OCBC and UOB as recovery plays

MAS likely to ease stance on dividend cap imposed on FY20 dividends as Singapore banks have preserved sufficient capital. In July 2020, the Monetary Authority of Singapore (MAS) called on Singapore banks to cap their total dividends per share at 60% of FY19 levels, for FY2020, while offering the scrip dividend option. This has allowed Singapore banks to preserve sufficient capital to ride through macroeconomic uncertainties. Following the relaxation of dividend restrictions by various central banks going into FY21 on the back of improved visibility for an economic recovery, we expect MAS to also ease its stance for Singapore banks.

We expect higher dividends for FY21F on gradual relaxation of dividend caps; a two-stage relaxation seems to be a more likely scenario. As the targeted loan moratorium under the Extended Support Scheme – Standardised rolls off after Jun 2021, we expect MAS to progressively relax its dividend restrictions for banks. A two-stage relaxation, where Singapore banks would be initially allowed to pay out up to a percentage of their FY21F net profit prior to the complete removal of restrictions, seems to be a more likely scenario. We believe higher dividends are on the horizon as the managements of banks have signalled their willingness and ability to commit to higher dividends in FY21F, subject to MAS guidelines.

Banks may adjust high capital buffers through some special dividends from FY22F, subject to asset quality and corporate actions. As of end-4Q20, Singapore banks' CET1 ratios of 13.9%-15.2% were well above their comfortable operating range of ~13% +/-0.5%. Mathematically, the banks can revert to FY19's dividend policy/payout levels and will still have ample capital buffers within their comfortable range. We believe banks may adjust their high capital buffers via special dividends from FY22F, subject to asset quality and corporate actions at that juncture, as banks navigate through a COVID-19 recovery. Should provisions come within managements' current expectations, we believe there is a case for some special dividends from FY22F.

Maintain BUY on OCBC and UOB as recovery plays. We maintain BUY on OCBC and UOB as recovery plays, as we look towards am earnings recovery led by more stable NIM, higher loan growth, and lower credit costs alongside an uptick in long-end yields.

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STOCKS

	Price S$	Mkt Cap US$m	12-mth Target Price S$	Performance (%) 3 mth	12 mth	Rating
DBS	28.79	54,603	n.a.	15.1	51.5	NR
OCBC Bank	11.75	39,008	12.50	17.9	33.2	BUY
UOB	25.83	32,059	27.60	14.5	28.3	BUY

Source: DBS Bank, Bloomberg Finance L.P.
Closing price as of 31 Mar 2021

Singapore Banks: Forward price-to-book

Source: DBS Bank, Bloomberg Finance L.P

Post dividend cap, Singapore banks preserved sufficient capital to ride through COVID-19 uncertainties. In July 2020, the Monetary Authority of Singapore (MAS) called on Singapore banks to cap total dividends per share at 60% of their FY19 levels, for FY2020, while offering the scrip dividend option. This has allowed Singapore banks to preserve sufficient capital to ride through the macroeconomic uncertainties. As of end-4Q20, Singapore banks' CET1 ratios of 13.9% to 15.2% were well above their comfortable operating range of ~13% +/-0.5%.

Central banks have started to relax dividends restrictions. Increasingly, central banks have started to relax dividend restrictions. We believe that MAS will ease its previous dividend restrictions, where Singapore banks are required to cap their total dividends per share at 60% of FY19 levels, while offering scrip dividends.

Dividends restrictions relaxation

	Previous	New
Thailand	Jun 2020: Commercial banks to temporarily freeze interim dividend payments and suspend buybacks	Nov 2020: Commercial banks allowed to pay dividends not exceeding 2019's payout ratio and 50% of 2020's net profit
United States	Jun 2020: Dividends payments capped at the amount paid in the previous quarter, tied to a formula based on recent earnings	Mar 2021: Restrictions for banks' dividends will end for most banks after June 2021. except for banks that fall below the minimum risk-based requirements in the Fed's stress test
Europe	Mar 2020: Regional lenders to avoid paying cash dividends or any buybacks	Dec 2020: Dividends and share buybacks need to be below 15% of combined profits for the last two years or no higher than 0.2% of CET1 ratio, whichever is lower

Source: Bank of Thailand, European Central Bank, Federal Reserve

Loans under moratorium have started to decline. As the blanket loan moratorium in Singapore rolled off in end-2020, loans under moratorium across the banks have started to decline. For DBS, loans under moratorium declined from 5% as of end-Sep 2020 to 1% as of end-Jan 2021. For OCBC, loans under moratorium declined from 4% as of end-Dec 2020 to 2% as of end-Jan 2021. For UOB, loans under relief are ~90% collateralised and comprised government relief, UOB relief, and ESG loan schemes – making up ~6% of its loan book as of end-Jan 2021 (Dec 2020: ~9%).

As targeted moratoriums start to roll off, we expect increasing NPLs through FY21F. Under the Extended Support Scheme – Standardised, SMEs in targeted sectors are still allowed to defer 80% of principal payments and selected Enterprise Singapore's schemes till 30 Jun 2021. As targeted moratoriums start to roll off, we expect increasing NPLs through FY21F. We expect the NPL ratios for OCBC and UOB to increase to >2% in FY21F, as the recognition of weaker credits takes place on the back of the roll-off of moratoriums for COVID-19-affected sectors like aviation and aerospace, tourism, hospitality, marine and offshore among others. Singapore banks have taken large provisions through FY20 and baring any unexpected credit deterioration through FY21F, we believe the current NPL coverage ratios should support the increasing NPLs ahead.

We expect higher dividends for FY21F on gradual relaxation on dividends; a two-stage relaxation seems to be a more likely scenario. As targeted loan moratorium under the Extended Support Scheme – Standardised rolls off after Jun 2021, we expect MAS to progressively relax its dividend restrictions. We believe higher dividends are on the horizon as the managements of banks have signalled their willingness and ability to commit to dividends that are higher than FY20 levels, subject to MAS guidelines. As we expect NPLs to increase through FY21F while banks continue to assess the full impact of the COVID-19 pandemic, we believe that a full relaxation may not take place. A two-stage relaxation, where Singapore banks would be initially allowed to pay out up to a percentage of their FY21F net profit prior to the complete removal of restrictions, seems to be a more likely scenario.

Singapore Banks: FY19A-20A dividends

	FY19 DPS (Scts)	Div payout ratio (FY19A)	FY20 DPS = 60% of FY19 DPS (Scts)	Div payout ratio (FY20A)
DBS	123	50%	73.8	49%
OCBC	53	46%	31.8	39%
UOB	130	50%	78.0	45%

Source: Companies, DBS Bank

Notes: According to MAS, if a bank has already paid out interim dividends for 1Q2020, the dividend restrictions and the offering of dividends in scrip will be extended for an additional quarter until 1Q2021. The 60% cap will apply to the revised period, but will still be referenced to FY2019.

Prior to COVID-19, dividend policies and stances have differed. Since 2018, Singapore banks have continued to increase their dividend payout ratios. Dividend policies and stances have also differed across banks, with DBS being committed to a fixed dividend policy, while OCBC's dividend payout ratio was below peers – citing defensive and offensive reasons. Scrip dividend was applied at a discount of ~10% up till 2Q19. UOB committed to a higher dividend payout ratio of ~50%, subject to a CET1 ratio of >13.5% and sustainable financial performance.

Post COVID-19, Singapore banks signalled willingness and ability to commit to higher dividends; big-ticket M&A may not be on the horizon. We believe that uncertainties, especially for regional emerging countries, may still linger on in view of the various expiry timeframes for debt moratoriums. As such, big ticket M&A may not be on the horizon for Singapore banks that may prefer to grow regionally via digital channels.

According to OCBC, management maintains that there are no M&A plans at the moment due to the murky visibility. Management also does not wish to undertake an M&A in a deteriorating market, where resources are required to manage its current portfolios, despite its previous stance on keeping capital buffers for offensive and defensive reasons. Management believes that some capital buffers are necessary for organic growth across ASEAN.

Banks may adjust high capital buffers through some special dividends from FY22F, subject to asset quality and corporate actions. Mathematically, the banks can revert to FY19's dividend policy/payout levels and will still have ample capital buffers that are above their comfortable range. We believe banks may adjust high capital buffers through special dividends from 2H22F, subject to asset quality and corporate actions at that juncture, as banks navigate through a COVID-19 recovery. Should provisions come within managements' current expectations, we believe there is a case for some special dividends from FY22F, though banks may also wish to keep some of the excess capital to deploy for growth. Higher dividend payout policies post-FY21F may also be an avenue to distribute excess capital.

Exploring theoretical dividend payouts while maintaining CET1 ratio of ~13.5%. Our dividend payout estimates for OCBC and UOB are depicted in the following table. To arrive at a more realistic special dividends payout situation, we took into account adjustments for final 4Q20 dividend payout, RWA growth of ~8% taking into account management loan growth targets and some credit deterioration due to higher NPLs in FY21F.

Singapore Banks: Theoretical dividend payouts

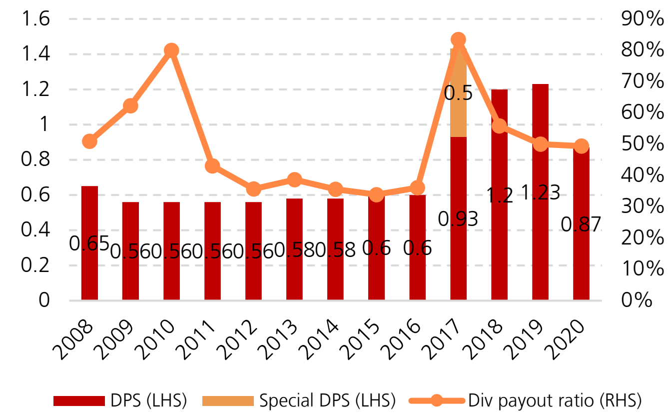
	FY21F net profit ($m)	FY21F RWA ($m)	FY20A CET1 ratio	Excess capital (S$m)*	Excess capital (S$ per share)	Assume 50% dividend payout ratio for FY21F (S$ per share)	Implied dividend yield (FY21F)	Excess capital for FY22F (S$ per share)
OCBC	4,303	235,597	15.2%	4,992	1.12	0.48	4.0%	0.63
UOB	3,655	243,476	14.7%	3,364	2.01	1.09	4.2%	0.92

* excess capital above CET1 ratio assumed to be 13.5% in FY21

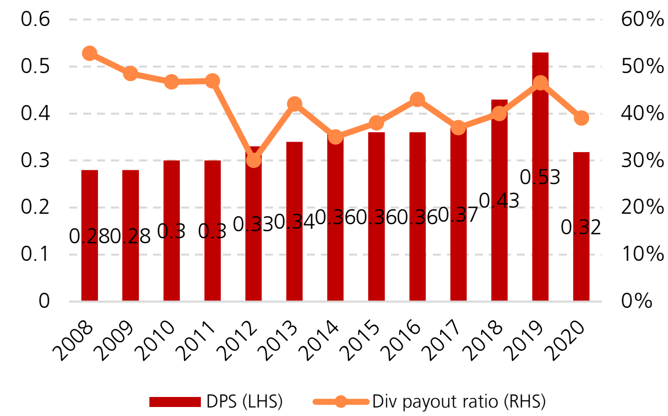
Source: Companies, DBS Bank

Singapore Banks: Dividends

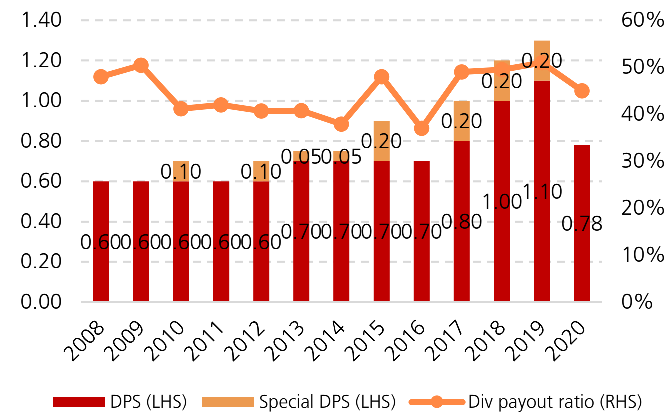
DBS



OCBC



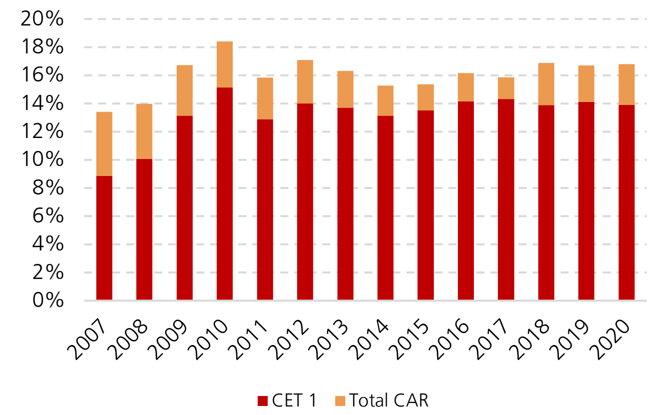
UOB



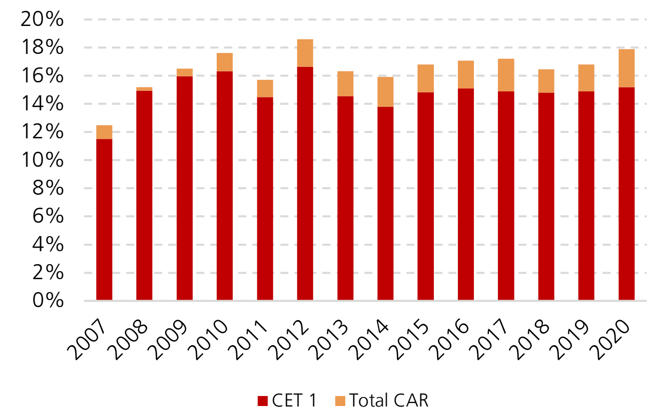
Source: Companies, DBS Bank

Singapore Banks: Capital ratios

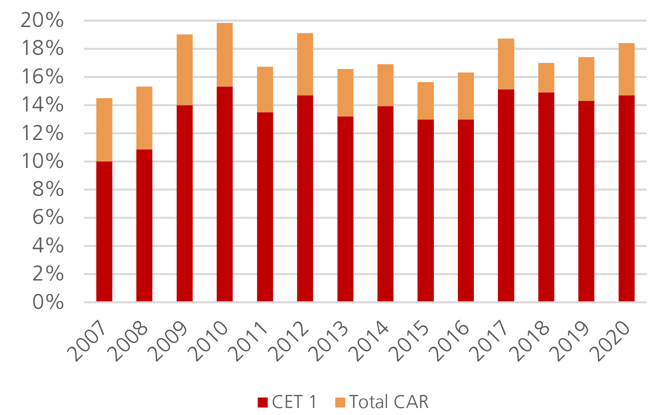
DBS



OCBC



UOB



Source: Companies, DBS Bank

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BUY (>15% total return over the next 12 months for small caps, >10% for large caps)
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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 Bank unless otherwise specified.

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