

DBS GROUP HOLDINGS LTD

Major Spring Cleaning before FY18



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SINGAPORE | BANKING | 3Q17 RESULTS

- 3Q17 PATMI of S\$0.8bn missed our estimate by 38.5%.
- The downside surprise came from lumpy accelerated provisions of S\$815mn.
- NII is driven by stronger growth in loans volume.
- Strong momentum in WM and IB fee income
- Maintain "BUY" rating with a higher target price of S\$26.83 (previous TP S\$25.70) based on Gordon Growth Model.**

Results at a glance

(SGD mn)	3Q17	3Q16	YoY (%)	2Q17	QoQ (%)	Comments
NII	1,975	1,815	8.8%	1,888	4.6%	NIMs -4bps YoY, loans +8.5% YoY
Net Fees & Comm	685	614	11.6%	636	7.7%	Higher WM and IB YoY.
Other Non-II	399	500	-20.2%	400	-0.2%	Lower Net Trading Income and absence of one-off gains YoY
Total Income	3,059	2,929	4.4%	2,924	4.6%	
Expenses	1,278	1,199	6.6%	1,282	-0.3%	Higher expenses in line with higher total income
Allowance	815	436	86.9%	304	168.1%	Accelerated recognition of residual weak O&G supports services exposure.
Net Profit	840	1,102	-23.8%	1,161	-27.6%	

Source: Company, PSR

The Positives

+ Strong WM. 3Q17 WM income was S\$546mn (+21% YoY) supported by investment products (+19% YoY). WM AUM increased to S\$195bn in 3Q17 compared to S\$175bn in 2Q17. S\$15bn came from the ANZ integration and S\$5bn from the DBS WM franchise.

+ IBG Cash/SFS income 35% higher YoY. Higher volumes of cash management deposits and digital capabilities contributed to stronger IBG Cash/SFS income in 3Q17. Cash management deposits grew 7% YoY to reach S\$134bn and the digital capabilities helped DBS IBG capture new clients.

+ Stronger NII is driven by broad-based strong loans growth and higher yields. Loans growth was 8.5% higher YoY led by YoY double-digit percentage growth in Manufacturing, Building & Construction and Housing loans. Yields were also higher YoY for Customer non-trade loans, Trade assets and Interbank loans.

+ Strong IB performance. IB grew 18.5% YoY as debt capital markets were strong in 3Q17 and were supported by advisory fees from One Belt and One Road projects.

The Negatives

- S\$815mn net allowance taken in a move to accelerate recognition of residual weak O&G support service exposure. SP expense in the 3Q17 was S\$1,665mn offset by a write back of S\$850mn from GP to result in the net allowance of S\$815mn expensed in the profit & loss line. This was in line with the recognition of S\$1.7bn new O&G NPA this quarter. In 2Q17 the O&G NPA was c.S\$1.4bn so with the additional S\$1.7bn recognised, the total O&G NPA is now at c.S\$3bn thus making up 57% of higher risk O&G exposure of S\$5.3bn. The heavy SP expensed this quarter increased the total SP allowance to S\$2.5bn from S\$1.3bn in 2Q17. Of the total SP allowance, S\$1.5bn is used to cover the O&G NPA of S\$3bn.

	GP movement	SP movement	O&G New NPA
3Q17	-S\$850mn	+S\$1,665mn	+S\$1.7bn

Source: Company, PSR

Buy (Maintain)

LAST TRADED PRICE	SGD 22.79
FORECAST DIV	SGD 0.66
TARGET PRICE	SGD 26.83
TOTAL RETURN	20.62%

COMPANY DATA

BLOOMBERG TICKER	DBS SP
O/S SHARES (MN) :	2,558
MARKET CAP (USD mn / SGD mn) :	42733 / 58288
52 - WK HI/LO (SGD) :	23.14 / 14.96
3M Average Daily T/O (mn) :	4.22

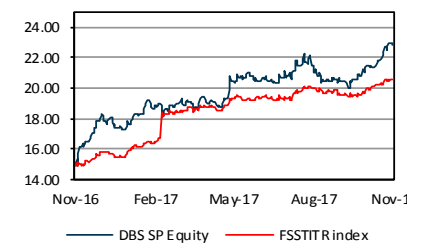
MAJOR SHAREHOLDERS (%)

Temasek Holdings Pte Ltd	29.35%
Vanguard Group	2.23%
Norges Bank Investment Management	2.02%
BlackRock	1.29%

PRICE PERFORMANCE (%)

	1M TH	3M TH	1Y R
COMPANY	8.7	5.7	58.4
STIRETURN	4.30	1.90	24.83

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec	FY 15	FY 16	FY 17e	FY 18e
Total Inc (SGDmn)	10,923	11,489	12,200	12,960
Op Profit (SGDmn)	5,280	5,083	5,151	6,820
NPAT (SGDmn)	4,567	4,360	4,504	5,889
EPS (SGD)	1.71	1.73	1.52	2.23
PER, (X)	11.7	10.3	14.5	10.2
P/BV, (X)	1.3	1.0	1.3	1.2
DPS (SGD)	0.60	0.60	0.66	0.68
ROE, (%)	11.4%	10.4%	9.1%	12.1%

Source: Bloomberg, Company, PSR

Valuation Method:

Gordon Growth Model (ERP: 6.7%, g: 2%)

Jeremy Teong (+65 6212 1863)

Investment Analyst

jeremyteongfh@phillip.com.sg

- Less likely for a special dividend as excess GP is moved to SP through profit and loss line before FRS 109 implementation. The FRS 109 that will be implemented on 1 Jan 2018 will require banks to maintain their GP allowance of not less than 1% of its loans and receivables net of collaterals after deducting individual impairment provisions made. Any excess of that 1% will be transferred to either retained earnings or to a Non-distributable RLAR. The RLAR is a mechanism that cannot be released to profit and loss but is recognised as Tier 2 capital and serves to absorb unexpected deterioration of assets. The implication is GP cannot be utilised in the profit and loss line under the FRS 109 to help smoothen out any volatility in provision expense. Therefore by releasing S\$850mn of GP to SP, DBS could reduce its GP ratio from 1.4% to 0.9% through the profit and loss line and provide as much as possible for the existing O&G exposure before the implementation of the FRS 109. We argue that this move would effectively take away the potential for the excess GP to be transferred to retained earnings for distribution as special dividends.

List of Abbreviations

WM – Wealth Management
IBG – Institutional Banking Group
CBG – Consumer Banking Group
NII – Net Interest Income
NIM – Net Interest Margin
LDR – Loan to Deposit Ratio
NPL – Non-performing Loans
CASA – Current Account, Savings Account
IB – Investment Banking
O&G – Oil and Gas
SP – specific provisions
GP – general provisions
AUM – Asset Under Management

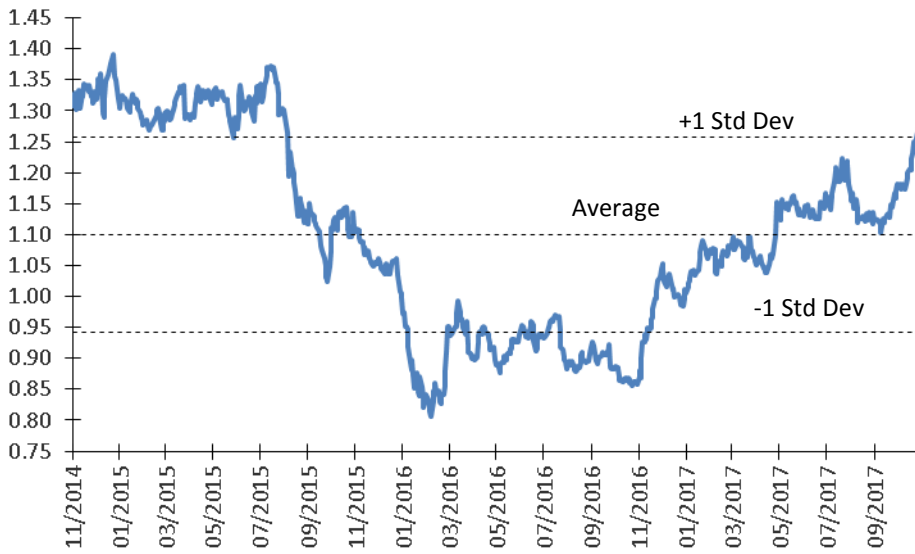
Outlook

Owing to the aggressive recognition of NPA and net allowance expensed, we revise our FY17e net income growth to 3.1% in line with management guidance. Our previous FY17e net income growth estimate was 20.5%. Specific provisions could remain elevated in 4Q17 following the move to clean up as much O&G exposure as possible. Nonetheless, this would pave the way for FY18's total credit cost to be lower than the through cycle level of 27bps. Underlying loan growth for this year and the next is 7% to 8%, higher than the mid-single-digit percentage guided at the beginning of this year. In all, we see the move to spring clean the O&G exposure as a preparation for a much stronger performance in FY18.

Valuation: Gordon Growth Model

Item	Description	Value
R _f	Risk-free rate	2.0%
E	Equity-risk premium	6.7%
B	Beta	1.085
COE	Cost of Equity	9.3%
ROE	FY18e Return on Equity	12.1%
g	Terminal growth rate	2.0%
(ROE-g)	FY18e Target Price to Book	1.39
(COE-g)		
	FY18e BVPS, S\$	19.30
	FY18e Valuation, S\$	26.83

3-Year Historical Price-to-Book



Investment Actions

Maintain “BUY” rating with a higher target price of S\$26.83 (previous TP S\$25.70) based on Gordon Growth Model.

Table 1. Fee and commission income

SGD mn	3Q17	3Q16	YoY (%)	2Q17	QoQ (%)
Brokerage	39	39	0.0%	38	2.6%
Investment banking	64	54	18.5%	41	56.1%
Transaction Services	154	147	4.8%	154	0.0%
Loan related	100	110	-9.1%	104	-3.8%
Cards	139	123	13.0%	130	6.9%
Others	20	28	-28.6%	19	5.3%
Wealth management	272	201	35.3%	245	11.0%
Fee and comm expense	(103)	(88)	NM	(95)	NM
Total	685	614	11.6%	636	7.7%

Wealth management the stand-out performer

Table 2. Other non-interest income

SGD mn	3Q17	3Q16	YoY (%)	2Q17	QoQ (%)
Net trading income	265	338	-21.6%	295	-10.2%
Net income on Fin Inv	120	103	16.5%	95	26.3%
Net gain on fixed assets	-	41	NM	-	NM
Others (inc. rental and assoc)	14	18	-22.2%	10	40.0%
Total other non int Inc	399	500	-20.2%	400	-0.2%

Less investment gains

Table 3. Loans by Industries

SGD mn	3Q17	3Q16	YoY (%)	2Q17	QoQ (%)
Manufacturing	33,563	30,872	8.7%	32,771	2.4%
Building & construction	62,502	55,881	11.8%	60,546	3.2%
Housing loans	69,956	62,692	11.6%	64,850	7.9%
General commerce	50,792	45,559	11.5%	48,692	4.3%
Tpt, storage & comms	29,307	28,591	2.5%	30,411	-3.6%
Fls, invt & holding co	15,605	15,525	0.5%	14,768	5.7%
Professionals & Pri inv	28,039	24,663	13.7%	25,312	10.8%
Others	29,071	30,034	-3.2%	30,072	-3.3%
Total loans	318,835	293,817	8.5%	307,422	3.7%

Real Estate related loans leading the group

Table 4. Loans by currencies

SGD mn	3Q17	3Q16	YoY (%)	2Q17	QoQ (%)
Singapore dollar	132,144	121,203	9.0%	126,378	4.6%
US dollar	100,678	95,509	5.4%	101,206	-0.5%
Hong Kong dollar	36,932	33,415	10.5%	34,389	7.4%
Chinese yuan	10,340	12,296	-15.9%	10,127	2.1%
Others	38,741	31,394	23.4%	35,322	9.7%
Total loans	318,835	293,817	8.5%	307,422	3.7%

Table 5. Revenue by Business segments

SGD mn	3Q17	3Q16	YoY (%)	2Q17	QoQ (%)
Consumer/Priv Banking	1,174	1,106	6.1%	1,140	3.0%
Institutional Banking	1,327	1,310	1.3%	1,298	2.2%
Treasury	211	287	-26.5%	258	-18.2%
Others	347	226	53.5%	228	52.2%
Total Revenue	3,059	2,929	4.4%	2,924	4.6%

Table 6. Revenue by Geographical segments

SGD mn	3Q17	3Q16	YoY (%)	2Q17	QoQ (%)
Singapore	2,025	1,889	7.2%	1,923	5.3%
Hong Kong	563	566	-0.5%	536	5.0%
Rest of Greater China	213	208	2.4%	208	2.4%
South and SE Asia	168	188	-10.6%	168	0.0%
Rest of the world	90	78	15.4%	89	1.1%
Total Revenue	3,059	2,929	4.4%	2,924	4.6%

Source (Tables 1-6): Company, PSR

Figure 1. Net interest margin

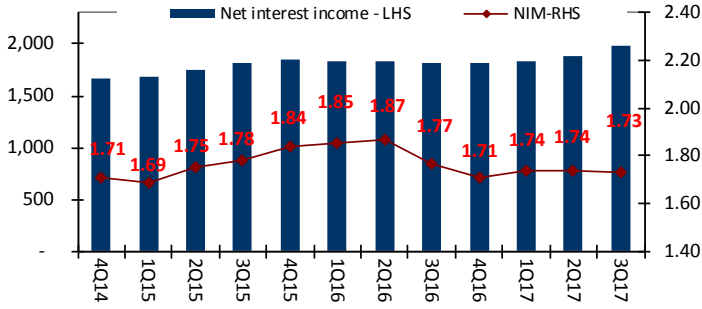


Figure 2. NonII/Total Income

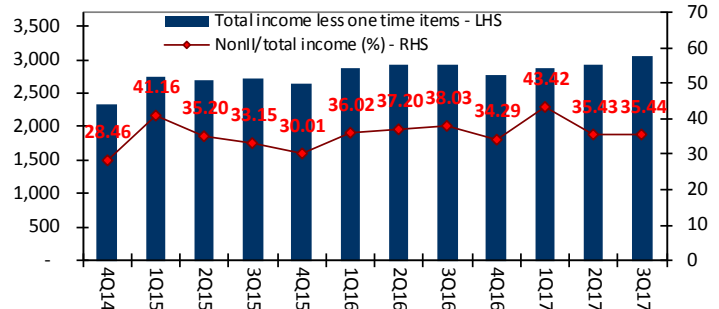


Figure 3. Efficiency ratio

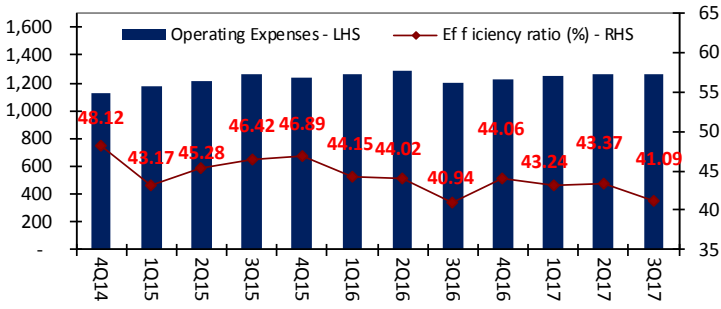


Figure 4. Net profit margin

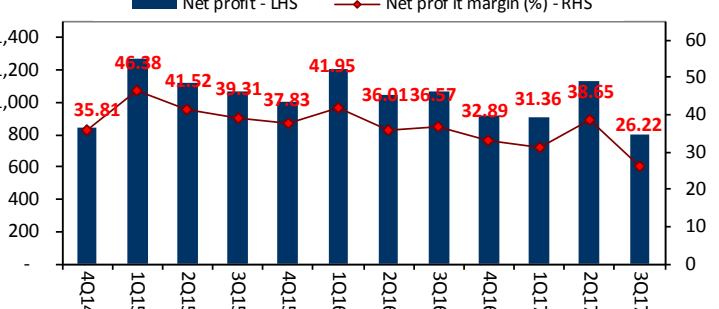


Figure 5. Deposits, Loans, LDR

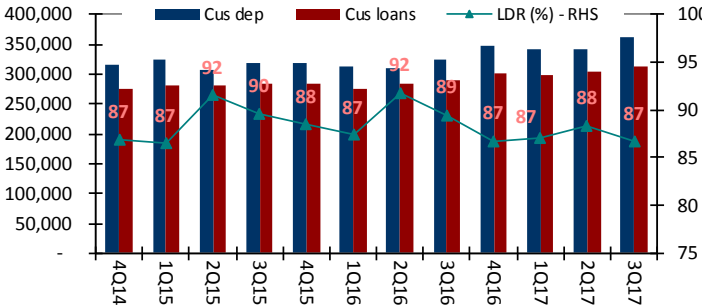


Figure 6. NPA, NPL

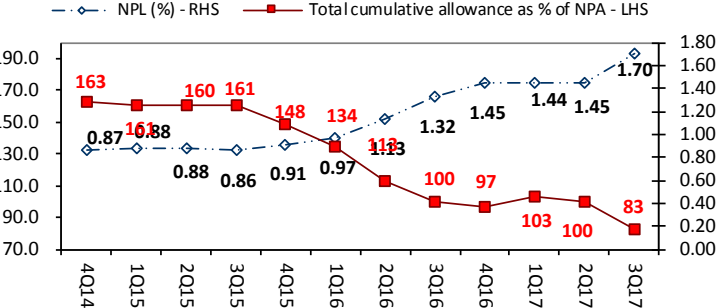


Figure 7. Growth in selected asset items

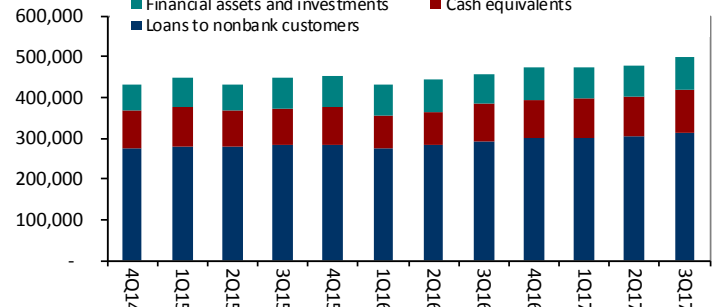


Figure 8. CAR

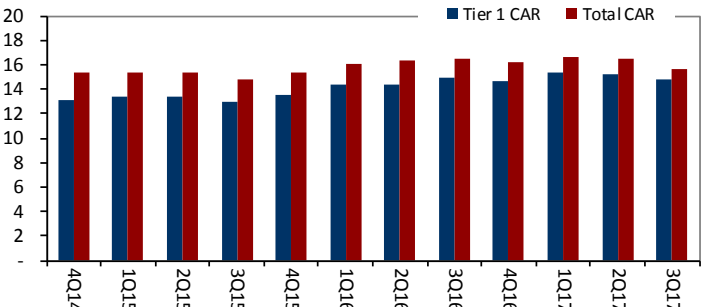


Figure 9. ROE and ROA

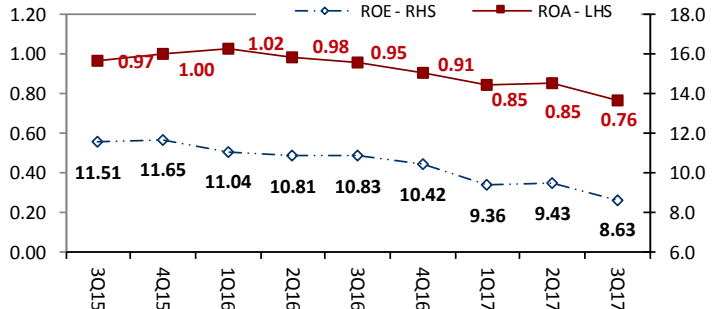


Figure 10. EPS and NBV

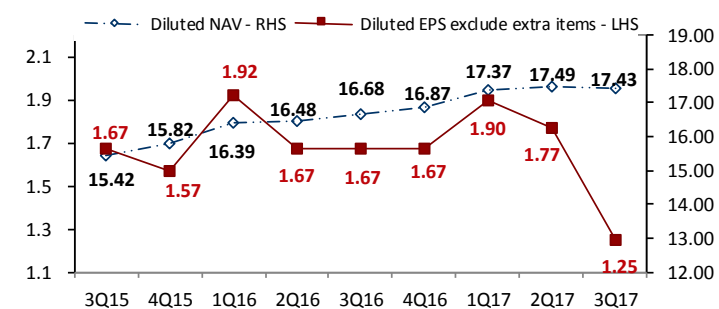


Figure 11. Profit before tax by geographical segment

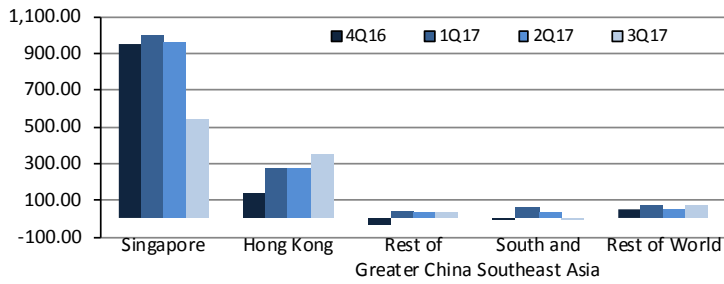


Figure 12. Profit before tax by Geographical segment breakdown

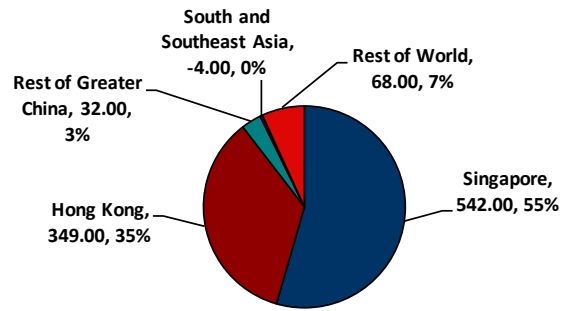


Figure 13. Profit before tax by business segment

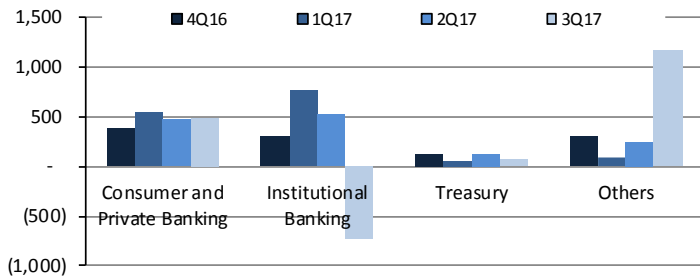


Figure 14. Net interest income trend

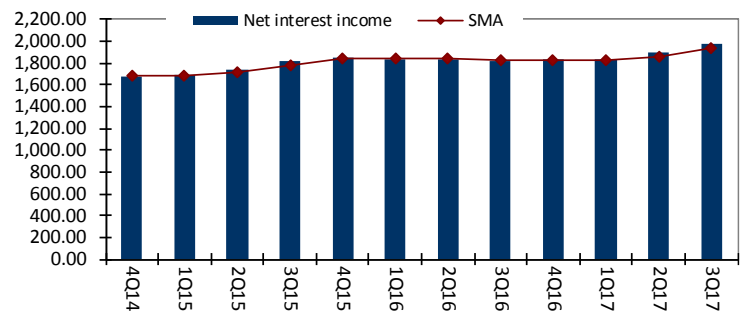


Figure 15. Fee and Commission trend

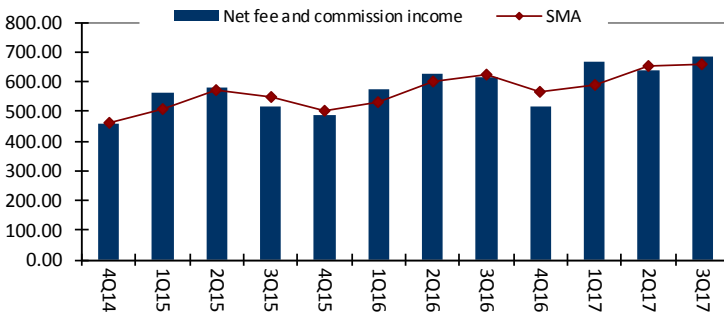
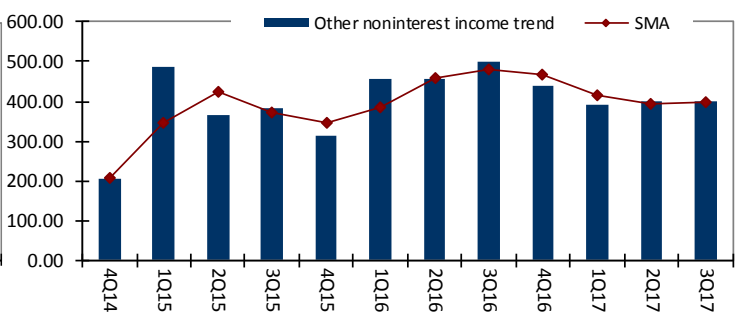


Figure 16. Other noninterest income trend



Financials

Income Statement

Y/E Dec, SGD mn	FY14	FY15	FY16	FY17e	FY18e
Net Interest Income	6,321	7,100	7,305	7,715	8,391
Fees and Commission	2,027	2,144	2,331	2,533	2,898
Other Non interest income	1,468	1,679	1,853	1,952	1,671
Total income	9,816	10,923	11,489	12,200	12,960
Operating expenses	4,330	4,900	4,972	5,084	5,296
Provisions	667	743	1,434	1,965	845
Operating profit	4,819	5,280	5,083	5,151	6,820
Associates & JVs	79	14	0	0	0
Profit Before Tax	4,898	5,294	5,083	5,151	6,820
Taxation	713	727	723	647	931
Profit After Tax	4,185	4,567	4,360	4,504	5,889
Non-controlling Interest	139	113	122	136	137
Net Income, reported	4,046	4,454	4,238	4,368	5,752
Net Income, adj.	3,848	4,318	4,238	4,018	5,752

Per share data (SGD)

Y/E Dec, SGD mn	FY14	FY15	FY16	FY17e	FY18e
EPS, reported	1.63	1.71	1.73	1.52	2.23
DPS	0.58	0.60	0.60	0.66	0.68
BVPS	14.44	15.49	16.61	17.74	19.30

Supplementary items

Y/E Dec, SGD mn	FY14	FY15	FY16	FY17e	FY18e
CET1 CAR (%)	13.1%	13.5%	14.1%	13.6%	13.6%
Tier 1 CAR (%)	13.1%	13.5%	14.7%	14.2%	14.2%
Total CAR (%)	15.3%	15.4%	16.2%	15.6%	15.5%

Balance Sheet

Y/E Dec, SGD mn	FY14	FY15	FY16	FY17e	FY18e
Cash and bal with central banks	19,517	18,829	26,840	22,780	20,039
Due from banks	42,263	38,285	30,018	33,020	33,020
Govt, Bank & Corp Sec & T Bills	67,457	74,574	78,818	98,936	105,955
Derivatives	16,995	23,631	25,757	16,651	11,082
Goodwill and intangibles	5,117	5,117	5,117	5,166	5,166
Property and other fixed assets	1,485	1,547	1,572	1,263	1,758
Loans to non-bank customers	275,588	283,289	301,516	319,701	343,197
JV and Associates	995	1,000	890	882	919
Other assets	11,249	11,562	11,042	12,268	11,135
Total Assets	440,666	457,834	481,570	510,667	532,271
Due to banks	16,176	18,251	15,915	22,920	22,920
Deposits from customers	317,173	320,134	347,446	365,132	387,848
Derivatives	18,755	22,145	24,497	16,651	11,082
Other liabilities	11,728	12,404	15,895	19,753	19,829
Other debt securities	31,963	38,078	27,745	35,514	35,514
Subordinated term debts	4,665	4,026	3,102	1,147	1,147
Total liabilities	400,460	415,038	434,600	461,117	478,340
Shareholder's equity	37,708	40,374	44,609	47,175	51,568
Non-controlling interest	2,498	2,422	2,361	2,375	2,362
Total Equity	40,206	42,796	46,970	49,550	53,931

Valuation Ratios

Y/E Dec, SGD mn	FY14	FY15	FY16	FY17e	FY18e
P/E (X), avg	11.8	11.7	10.3	14.5	10.2
P/B (X), avg	1.3	1.3	1.0	1.3	1.2
Dividend Yield (%)	3.3%	3.1%	3.5%	2.9%	3.0%

Growth & Margins (%)

Growth					
Net interest income	13.5%	12.3%	2.9%	5.6%	1.9%
Net Fee and Comm Inc	7.5%	5.8%	8.7%	8.7%	2.7%
Total income	7.9%	11.3%	5.2%	6.2%	1.8%
Profit before tax	9.3%	9.6%	-3.7%	1.3%	4.4%
Net income, reported	10.2%	10.1%	-4.8%	3.1%	4.6%
Net income, adj.	9.9%	12.2%	-1.9%	-5.2%	4.6%

Margins

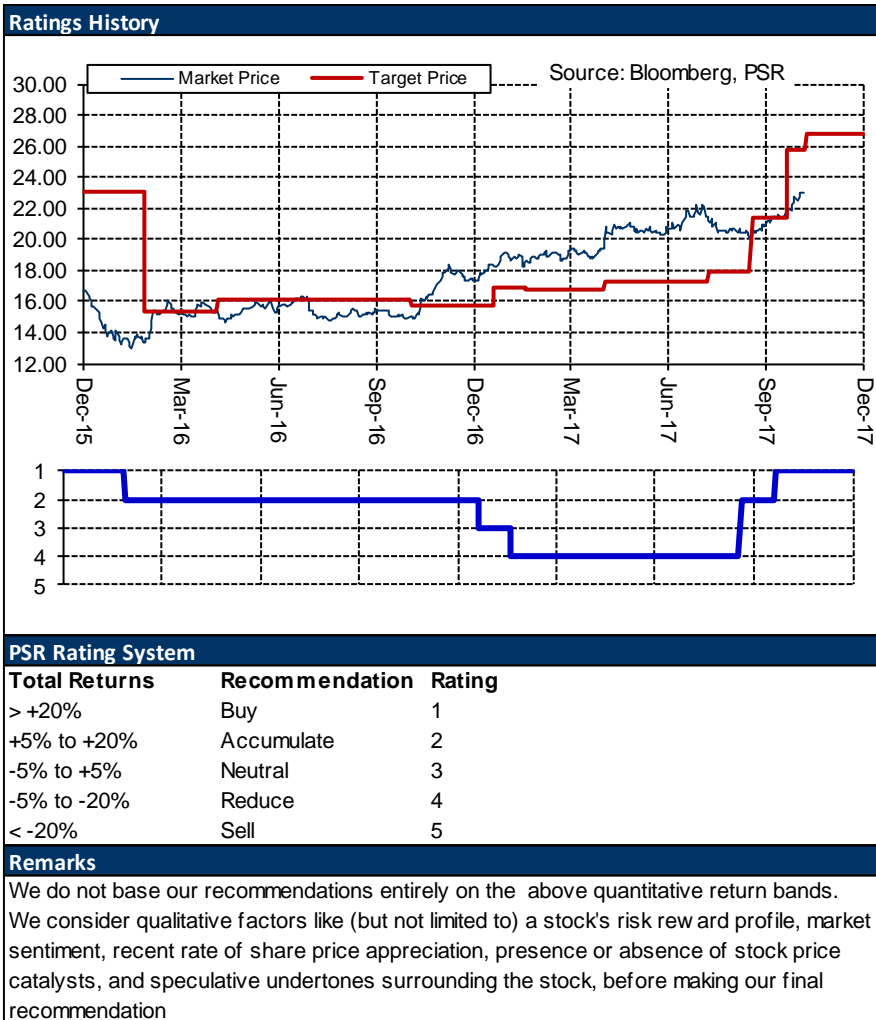
Net interest margin	1.71%	1.84%	1.71%	1.77%	1.78%
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Key Ratios (%)

ROE	10.9%	11.3%	10.4%	9.1%	12.1%
ROA	0.9%	1.0%	0.9%	0.8%	1.1%
RORWA	1.5%	1.6%	1.5%	1.4%	1.8%
Non-interest/total income ratio	35.6%	35.0%	36.4%	36.8%	35.3%
Cost/income ratio	44.1%	44.9%	43.3%	41.7%	40.9%
Loan/deposit ratio	86.9%	88.5%	86.8%	87.6%	88.5%
NPL ratio	0.87	0.91	1.45	1.71	1.50

Source: Company, PSR

*Forward multiples & yields based on current market price; historical multiples & yields based on historical market price.



Contact Information (Singapore Research Team)

Head of Research

Paul Chew – paulchewkl@phillip.com.sg

Research Operations Officer

Mohamed Amiruddin – amiruddin@phillip.com.sg

Consumer | Healthcare

Soh Lin Sin – sohls@phillip.com.sg

Oil & Gas | Energy

Chen Guangzhi – chengz@phillip.com.sg

Macro

Pei Sai Teng – peist@phillip.com.sg

Transport | REITs (Industrial)

Richard Leow, CFTe, FRM -
richardleowwt@phillip.com.sg

REITs (Commercial, Retail, Healthcare) | Property

Dehong Tan – tandh@phillip.com.sg

Technical Analysis

Jeremy Ng – jeremyngch@phillip.com.sg

Banking and Finance

Jeremy Teong – jeremyteongfh@phillip.com.sg

US Equity

Ho Kang Wei – hokw@phillip.com.sg

Contact Information (Regional Member Companies)

SINGAPORE

Phillip Securities Pte Ltd

Raffles City Tower
250, North Bridge Road #06-00
Singapore 179101
Tel +65 6533 6001
Fax +65 6535 6631
Website: www.poems.com.sg

MALAYSIA

Phillip Capital Management Sdn Bhd

B-3-6 Block B Level 3 Megan Avenue II,
No. 12, Jalan Yap Kwan Seng, 50450
Kuala Lumpur
Tel +603 2162 8841
Fax +603 2166 5099
Website: www.poems.com.my

HONG KONG

Phillip Securities (HK) Ltd

11/F United Centre 95 Queensway
Hong Kong
Tel +852 2277 6600
Fax +852 2868 5307
Websites: www.phillip.com.hk

JAPAN

Phillip Securities Japan, Ltd.

4-2 Nihonbashi Kabuto-cho Chuo-ku,
Tokyo 103-0026
Tel +81-3 3666 2101
Fax +81-3 3666 6090
Website: www.phillip.co.jp

INDONESIA

PT Phillip Securities Indonesia

ANZ Tower Level 23B,
Jl Jend Sudirman Kav 33A
Jakarta 10220 – Indonesia
Tel +62-21 5790 0800
Fax +62-21 5790 0809
Website: www.phillip.co.id

CHINA

Phillip Financial Advisory (Shanghai) Co Ltd

No 550 Yan An East Road,
Ocean Tower Unit 2318,
Postal code 200001
Tel +86-21 5169 9200
Fax +86-21 6351 2940
Website: www.phillip.com.cn

THAILAND

Phillip Securities (Thailand) Public Co. Ltd

15th Floor, Vorawat Building,
849 Silom Road, Silom, Bangrak,
Bangkok 10500 Thailand
Tel +66-2 6351700 / 22680999
Fax +66-2 22680921
Website www.phillip.co.th

FRANCE

King & Shaxson Capital Limited

3rd Floor, 35 Rue de la Bienfaisance 75008
Paris France
Tel +33-1 45633100
Fax +33-1 45636017
Website: www.kingandshaxson.com

UNITED KINGDOM

King & Shaxson Capital Limited

6th Floor, Candlewick House,
120 Cannon Street,
London, EC4N 6AS
Tel +44-20 7426 5950
Fax +44-20 7626 1757
Website: www.kingandshaxson.com

UNITED STATES

Phillip Capital Inc

141 W Jackson Blvd Ste 3050
The Chicago Board of Trade Building
Chicago, IL 60604 USA
Tel +1-312 356 9000
Fax +1-312 356 9005
Website: www.phillipusa.com

AUSTRALIA

Phillip Capital Limited

Level 10, 330 Collins Street
Melbourne, Victoria 3000, Australia
Tel +61-03 9629 8288
Fax +61-03 9629 8882
Website: www.phillipcapital.com.au

SRI LANKA

Asha Phillip Securities Limited

2nd Floor, Lakshmans Building,
No. 321, Galle Road,
Colombo 03, Sri Lanka
Tel: (94) 11 2429 100
Fax: (94) 11 2429 199
Website: www.ashaphillip.net

INDIA

PhillipCapital (India) Private Limited

No.1, 18th Floor, Urmi Estate
95, Ganpatrao Kadam Marg
Lower Parel West, Mumbai 400-013
Maharashtra, India
Tel: +91-22-2300 2999 / Fax: +91-22-2300 2969
Website: www.phillipcapital.in

TURKEY

PhillipCapital Menkul Degerler

Dr. Cemil Bengü Cad. Hak Is Merkezi
No. 2 Kat. 6A Caglayan
34403 Istanbul, Turkey
Tel: 0212 296 84 84
Fax: 0212 233 69 29
Website: www.phillipcapital.com.tr

DUBAI

Phillip Futures DMCC

Member of the Dubai Gold and
Commodities Exchange (DGCX)
Unit No 601, Plot No 58, White Crown Bldg,
Sheikh Zayed Road, P.O.Box 212291
Dubai-UAE
Tel: +971-4-3325052 / Fax: + 971-4-3328895

CAMBODIA

Phillip Bank Plc

Ground Floor of B-Office Centre,#61-64,
Norodom Blvd Corner Street 306,Sangkat
Boeung Keng Kang 1, Khan Chamkamorn,
Phnom Penh, Cambodia
Tel: 855 (0) 7796 6151/855 (0) 1620 0769
Website: www.phillipbank.com.kh

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