

# Oversea-Chinese Banking Corp

## Wealth Management Beats but Competition is Heating Up

### SINGAPORE | BANKING | 1Q17 RESULTS

- 1Q17 PATMI of S\$973mn exceeded our estimate by 16%. Insurance and wealth management (WM) surprised on the upside.
- All the growth in 1Q17 came from insurance and WM fee income. A flat 1Q17 net interest income growth was in line with our expectations.
- Maintain "REDUCE" with an unchanged target price of S\$8.48**, based at unchanged 0.95x FY17F book value (excluding preference shares).

#### Results at a glance

| (SGD mn)            | 1Q17         | 1Q16         | y-o-y (%)  | 4Q16         | q-o-q (%)  | Comments                                      |
|---------------------|--------------|--------------|------------|--------------|------------|---|
| Net interest income | 1,272        | 1,307        | -3%        | 1,251        | 2%         | NIMs -13bps y-o-y. Loans +8% y-o-y            |
| Fees & Comm         | 481          | 374          | 29%        | 420          | 15%        | Higher WM fee income q-o-q & y-o-y            |
| Insurance           | 211          | 122          | 73%        | 182          | 16%        | Higher Life Assurance profit q-o-q & y-o-y    |
| Other NII           | 285          | 257          | 11%        | 324          | -12%       | Lumpy net gain from property disposal in 4Q16 |
| <b>Total income</b> | <b>2,249</b> | <b>2,060</b> | <b>9%</b>  | <b>2,177</b> | <b>3%</b>  |   |
| Expenses            | -973         | -923         | 5%         | -981         | -1%        | Barclays WM added 2 percentage points y-o-y   |
| Allowances          | -168         | -167         | 1%         | -305         | -45%       | Lower General Provisions q-o-q and y-o-y      |
| <b>PATMI</b>        | <b>973</b>   | <b>856</b>   | <b>14%</b> | <b>789</b>   | <b>23%</b> |   |

Source: Company, PSR

**Non-interest Income increased 30% y-o-y.** Fee and commission income was up 29% y-o-y, supported by *Investment Banking* (+99% y-o-y) and *Wealth Management* (+70% y-o-y). Profit from insurance was up 111% y-o-y and *net trading income* was up 30% y-o-y. In our OCBC's pre-earnings update report dated 16 Jan 2017, we had expected stronger WM and Life Assurance to support OCBC's total income. But the 22% q-o-q growth from Life Assurance and 37% q-o-q growth from WM had exceeded expectations. Moving ahead, we still expect strong growth from the two segments but we do not expect the same pace of growth to continue as these two segments are largely driven by market conditions and investor sentiments.

**1Q17 Net interest income growth flat y-o-y and q-o-q** as net interest margins declined q-o-q and y-o-y to 1.62%. This was mainly due to tighter margins between non-bank customer loans and deposits partially offset by better returns from money market placements. Excess liquidity was channelled to money market placements thus volumes of these placements were higher q-o-q and y-o-y. But management sees opportunities ahead to shift some of these placements to higher yielding non-bank customer loans to improve net interest income. But we remain cautious on that outlook as the competitive business landscape may crimp some of that potential growth.

11 May 2017

#### Reduce (Maintain)

|                   |           |
|-------------------|-----------|
| LAST TRADED PRICE | SGD 10.46 |
| FORECAST DIV      | SGD 0.36  |
| TARGET PRICE      | SGD 8.48  |
| TOTAL RETURN      | -15.49%   |

#### COMPANY DATA

|                                |               |
|--------------------------------|---------------|
| O/S SHARES (MN) :              | 4,183         |
| MARKET CAP (USD mn / SGD mn) : | 31019 / 43749 |
| 52 - WK HI/LO (SGD) :          | 10.46 / 8.21  |
| 3M Average Daily T/O (mn) :    | 5.52          |

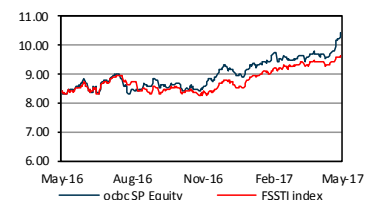
#### MAJOR SHAREHOLDERS (%)

|                                 |        |
|---------------------------------|--------|
| Lee Foundation                  | 4.25%  |
| Selat (Pte) Limited             | 10.81% |
| Aberdeen                        | 4.76%  |
| Singapore Investments (Pte) Ltd | 3.67%  |

#### PRICE PERFORMANCE (%)

|            | 1M TH | 3M TH | 1Y R  |
|------------|-------|-------|-------|
| COMPANY    | 6.5   | 6.3   | 26.3  |
| STI RETURN | 2.73  | 6.71  | 22.68 |

#### PRICE VS. STI



Source: Bloomberg, PSR

#### KEY FINANCIALS

| Y/E Dec                      | FY 15 | FY 16 | FY 17F | FY 18F |
|------------------------------|-------|-------|--------|--------|
| Total Operating Inc (SGD mn) | 8,722 | 8,489 | 8,982  | 9,133  |
| Operating Profit (SGD mn)    | 4,472 | 3,879 | 4,288  | 4,543  |
| NPAT, adj.                   | 4,108 | 3,646 | 4,009  | 4,224  |
| EPS (SGD)                    | 0.95  | 0.83  | 0.91   | 0.96   |
| PER, adj. (x)                | 11.0  | 12.6  | 11.5   | 10.9   |
| ROCE (%)                     | 11.6% | 9.6%  | 10.2%  | 10.4%  |

Source: Bloomberg

Valuation Method: 0.95x FY17F P/B

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**Non-Performing Loans (“NPLs”) stable at 1.3% but coverage ratio remains low at 101.1%.** NPLs formation was largely stable across all industries. Oil and Gas NPLs increased by approximately S\$100mn q-o-q to reach S\$1.4bn, representing half of total NPLs of S\$2.81bn. About 37% of the S\$1.4bn NPLs are still serving principal and interest repayments.

Oil and Gas offshore support vessels (“OSV”) sector loans is estimated to be S\$6bn, making up 40% of the total Oil and Gas on-balance sheet exposure of S\$15bn. 22% of the OSV sector loans are in NPL, which is valued at S\$1.32. Therefore NPL from the OSV sector actually make up 94% of the Oil and Gas NPLs. We opine that the stability in NPL formation in the OSV sector was largely due to:

- a) **Deterioration in collateral values of OSVs has decelerated.** Currently, management estimates OSV values have reached 40% to 45% of their original values after most of the deterioration happened in 2016.
- b) **Oil and Gas Customers whose loans have not deteriorated have diversified businesses.** These customers are able to extract cash flow from their non-Oil and Gas related businesses to support their exposure to the Oil and Gas industry. Besides, these companies have also put up additional collateral that are not Oil and Gas related as buffer.

**For now, regional corporate lending leads the loans growth momentum.** We see OCBC strengthening its regional corporate lending as loans to *Financial Institutions, Investment and Holding company* (“FIs”) and *General Commerce* show strong year-on-year (“y-o-y”) and quarter-on-quarter (“q-o-q”) growth (See Table 3.). At the same time, USD loans growth has outpaced SGD loans growth q-o-q and y-o-y corroborating the stronger regional exposure. By geography, half of the q-o-q gross loans growth was contributed by growth of Singapore loans. We believe that the FIs are OCBC’s regional network clients who book loans at the holding company level in Singapore for their overseas regional operations. But we see stiff competition to OCBC’s regional corporate business from at least one large universal bank which is also competing in other similar areas of insurance sales and wealth management. This universal bank has a strong presence in the Pearl River Delta region in China which is also an area of interest for OCBC Wing Hang.

**Housing loans softer.** On the consumer loans space, we saw *Housing loans* decline q-o-q. In our Banking Sector Report in April 2017, we opine that competing for market share in *Housing loans* will drive margins down. So we believe the growth decline is emphatic of OCBC’s reluctance to compete too aggressively. However, in view of stiff competition both in Singapore consumer and regional corporate business, we expect OCBC to tactically rotate between the two segments whenever competition recedes. Therefore, to be ready to capture opportunities, we expect OCBC to aggressively maintain ample deposits for USD and SGD to fund loans. Besides, management also sees deposits as a marker for strong client relationship. So in order to keep customers close and keep funding ample, we expect more upward pressure on funding costs this year.

#### Investment Actions

As expected, we saw unfavourable loans volume and rates dynamics suppressing net interest income growth and these conditions may continue to persist in 2017. But we also expect strong performances by OCBC’s Great Eastern Holdings and OCBC’s Bank of Singapore to support overall performance especially within the Singapore market. But on a less optimistic note, we see strong competition in overseas markets coming from at least one large universal bank that has operations in similar markets and driving similar product strategies as OCBC. **Maintain “REDUCE” with an unchanged target price of S\$8.48**, based on unchanged 0.95x FY17F book value (excluding preference shares).

Table 1. Fee and commission income

| SGD mn                    | 1Q17       | 1Q16       | y-o-y (%)    | 4Q16       | q-o-q (%)    |
|---------------------------|------------|------------|--------------|------------|--------------|
| Brokerage                 | 18         | 17         | 5.9%         | 17         | 5.9%         |
| Wealth management         | 215        | 109        | 97.2%        | 157        | 36.9%        |
| Fund management           | 25         | 34         | -26.5%       | 27         | -7.4%        |
| Credit card               | 35         | 32         | 9.4%         | 40         | -12.5%       |
| Loan-related              | 67         | 72         | -6.9%        | 76         | -11.8%       |
| Trade and remittances     | 52         | 50         | 4.0%         | 55         | -5.5%        |
| Guarantees                | 4          | 4          | 0.0%         | 4          | 0.0%         |
| Investment Banking        | 29         | 14         | 107.1%       | 13         | 123.1%       |
| Service charges           | 27         | 26         | 3.8%         | 22         | 22.7%        |
| Others                    | 9          | 16         | -43.8%       | 9          | 0.0%         |
| <b>Total Fee and Comm</b> | <b>481</b> | <b>374</b> | <b>28.6%</b> | <b>420</b> | <b>14.5%</b> |

Table 2. Other non-interest income

| SGD mn                         | 1Q17       | 1Q16       | y-o-y (%)    | 4Q16       | q-o-q (%)     |
|--------------------------------|------------|------------|--------------|------------|---------------|
| Net trading income             | 158        | 122        | 29.5%        | 122        | 29.5%         |
| Net gain on Invt securities    | 65         | 59         | 10.2%        | 54         | 20.4%         |
| Disposal of properties         | 24         | 21         | 14.3%        | 82         | -70.7%        |
| Others                         | 2          | 21         | -90.5%       | 26         | -92.3%        |
| <b>Total other non int Inc</b> | <b>249</b> | <b>223</b> | <b>11.7%</b> | <b>284</b> | <b>-12.3%</b> |

Table 3. Loans by Industries

| SGD mn                    | 1Q17           | 1Q16           | y-o-y (%)   | 4Q16           | q-o-q (%)   |
|---------------------------|----------------|----------------|-------------|----------------|-------------|
| Agri, mining & quarrying  | 7,582          | 7,578          | 0.1%        | 8,974          | -15.5%      |
| Manufacturing             | 13,185         | 12,881         | 2.4%        | 12,697         | 3.8%        |
| Building and construction | 35,742         | 34,838         | 2.6%        | 35,632         | 0.3%        |
| Housing loans             | 60,027         | 57,455         | 4.5%        | 60,149         | -0.2%       |
| General commerce          | 26,366         | 23,641         | 11.5%       | 25,348         | 4.0%        |
| Tpt, storage & comms      | 12,016         | 11,344         | 5.9%        | 11,520         | 4.3%        |
| FIs, invt & holding co    | 33,225         | 26,848         | 23.8%       | 30,491         | 9.0%        |
| Professionals & Pri inv   | 26,956         | 23,195         | 16.2%       | 26,396         | 2.1%        |
| Others                    | 9,704          | 10,301         | -5.8%       | 8,945          | 8.5%        |
| <b>Total loans</b>        | <b>224,803</b> | <b>208,081</b> | <b>8.0%</b> | <b>220,152</b> | <b>2.1%</b> |

Table 4. Loans by currencies

| SGD mn             | 1Q17           | 1Q16           | y-o-y (%)   | 4Q16           | q-o-q (%)   |
|--------------------|----------------|----------------|-------------|----------------|-------------|
| Singapore dollar   | 83,069         | 81,220         | 2.3%        | 81,260         | 2.2%        |
| US dollar          | 59,828         | 45,543         | 31.4%       | 56,576         | 5.7%        |
| Malaysian ringgit  | 20,264         | 22,285         | -9.1%       | 20,552         | -1.4%       |
| Indonesian rupiah  | 7,350          | 6,523          | 12.7%       | 7,486          | -1.8%       |
| Others             | 19,587         | 17,414         | 12.5%       | 18,757         | 4.4%        |
| Hong Kong Dollar   | 29,561         | 27,920         | 5.9%        | 30,339         | -2.6%       |
| Renminbi           | 5,144          | 7,176          | -28.3%      | 5,182          | -0.7%       |
| <b>Total loans</b> | <b>224,803</b> | <b>208,081</b> | <b>8.0%</b> | <b>220,152</b> | <b>2.1%</b> |

Table 5. Operating profit by Business segments

| SGD mn                               | 1Q17         | 1Q16       | y-o-y (%)    | 4Q16       | q-o-q (%)    |
|--------------------------------------|--------------|------------|--------------|------------|--------------|
| Global Consumer/ Private Banking     | 313          | 253        | 23.7%        | 257        | 21.8%        |
| Global Corporate/ Investment Banking | 356          | 507        | -29.8%       | 230        | 54.8%        |
| Global Treasury and Markets          | 109          | 118        | -7.6%        | 77         | 41.6%        |
| Insurance                            | 237          | 106        | 123.6%       | 222        | 6.8%         |
| OCBC Wing Hang                       | 85           | 74         | 14.9%        | 106        | -19.8%       |
| Others                               | (18)         | (112)      | nm           | (25)       | nm           |
| <b>Total Profit</b>                  | <b>1,082</b> | <b>946</b> | <b>14.4%</b> | <b>867</b> | <b>24.8%</b> |

Strong q-o-q and y-o-y growth seen in FIs, Invt & holding co and General commerce loan segments.

US dollar loans show strongest q-o-q growth, corroborating a stronger regional exposure.

Global corporate and investment banking is showing signs of recovery as OCBC strengthens its regional corporate lending.

Table 6. Profit before tax by Geographical segments

| SGD mn             | 1Q17         | 1Q16         | y-o-y (%)   | 4Q16         | q-o-q (%)   |
|--------------------|--------------|--------------|-------------|--------------|-------------|
| Singapore          | 629          | 575          | 9.4%        | 463          | 35.9%       |
| Malaysia           | 311          | 315          | -1.3%       | 341          | -8.8%       |
| Indonesia          | 197          | 177          | 11.3%       | 189          | 4.2%        |
| Greater China      | 289          | 304          | -4.9%       | 312          | -7.4%       |
| Other Asia Pacific | 38           | 32           | 18.8%       | 35           | 8.6%        |
| Rest of the World  | 47           | 32           | 46.9%       | 39           | 20.5%       |
| <b>Total NPBT</b>  | <b>1,511</b> | <b>1,435</b> | <b>5.3%</b> | <b>1,379</b> | <b>9.6%</b> |

Source (tables 1-6): Company, Phillip Securities Research

Fig 1: Net interest margin

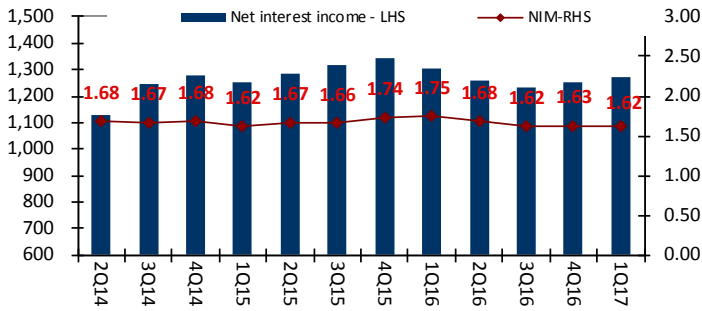


Fig 2: NonII/Total revenue

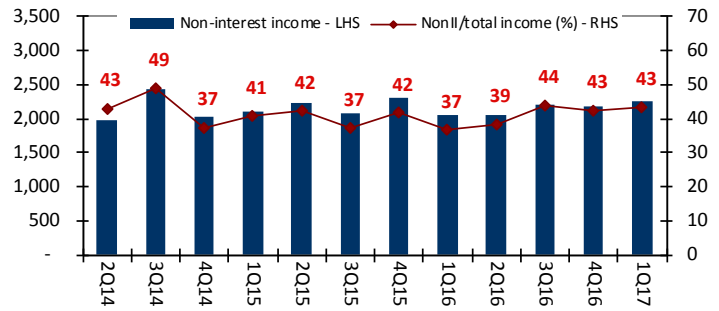


Fig 3: Efficiency ratio

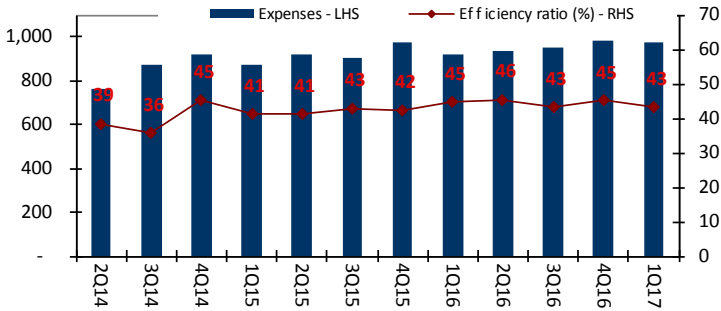


Fig 4: Net profit margin

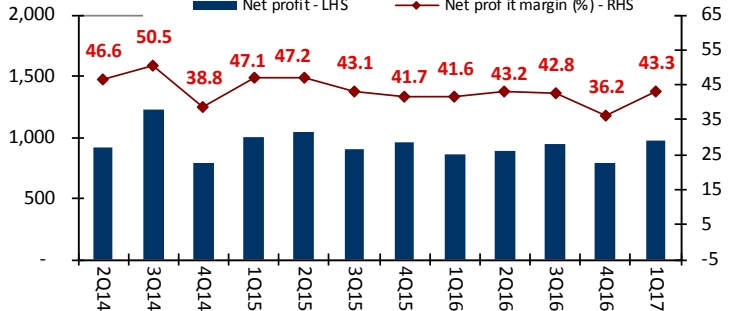


Fig 5: Deposits, Loans, LDR

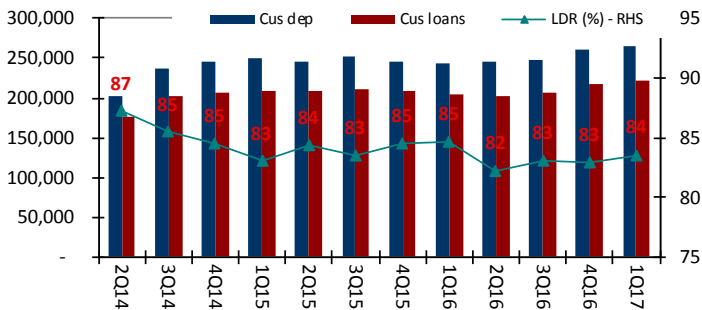


Fig 6: NPA, NPL

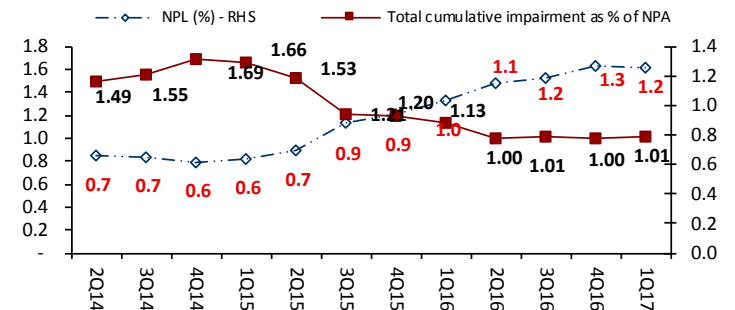


Fig 7: Growth in selected asset items

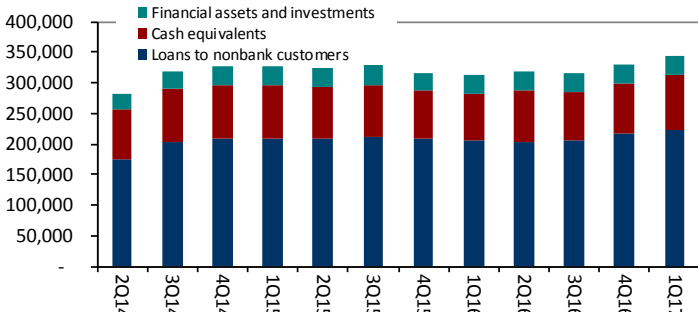


Fig 8: CAR

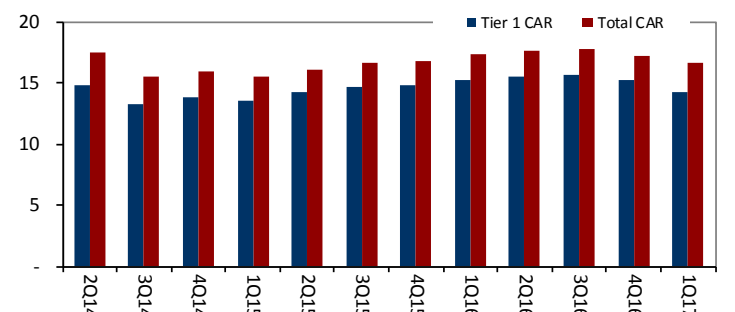


Fig 9: ROE and ROA

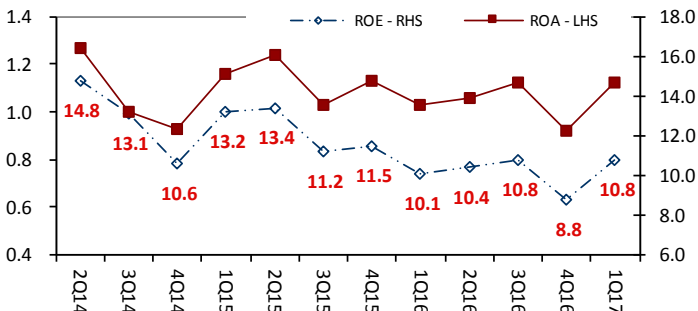


Fig 10: EPS and NBV

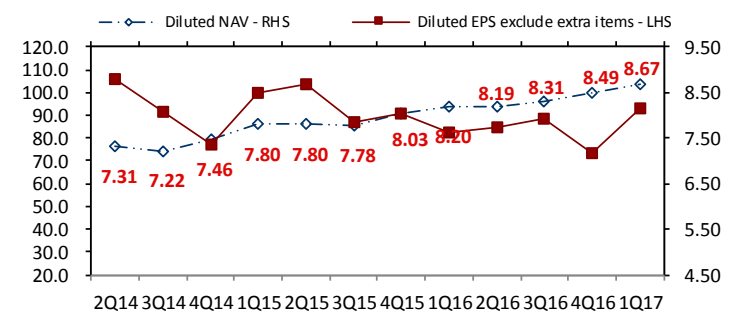


Fig 11: Profit before tax by geographical segment

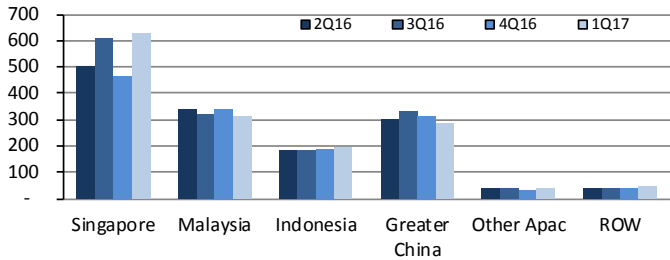


Fig 12: Geo segment breakdown

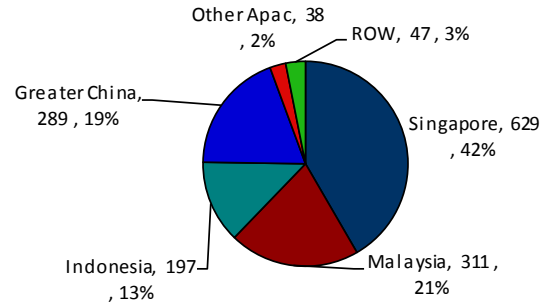


Fig 13: Operating profit by Business segment

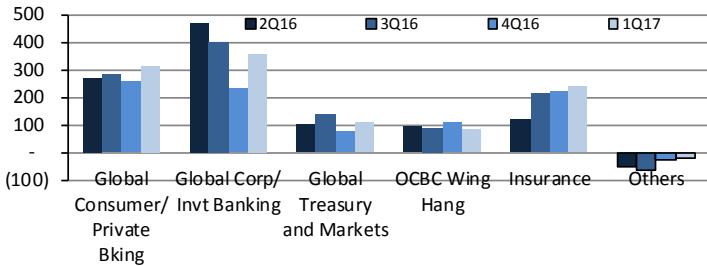


Fig 14: Net interest income trend

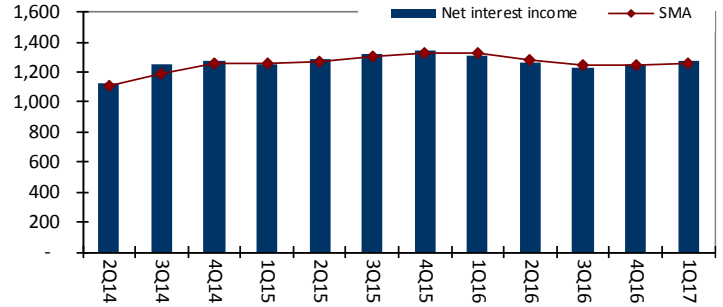


Fig 15: Fee and Commission trend

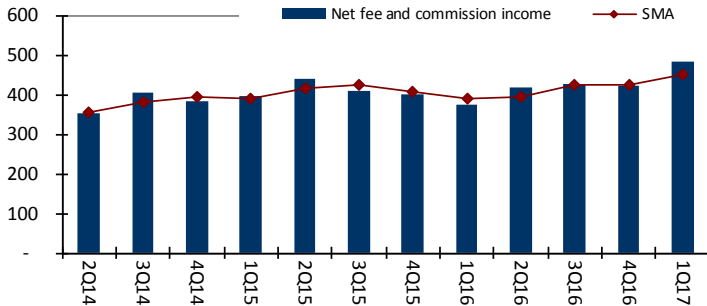


Fig 16: Other noninterest income trend

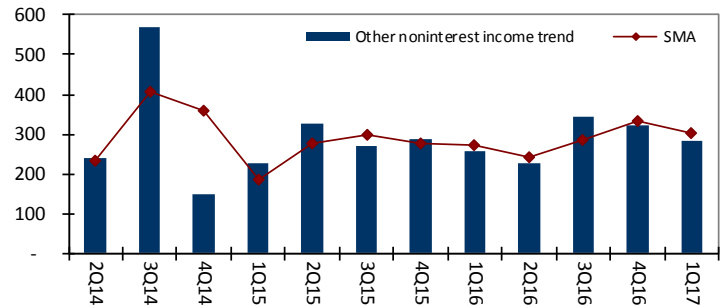
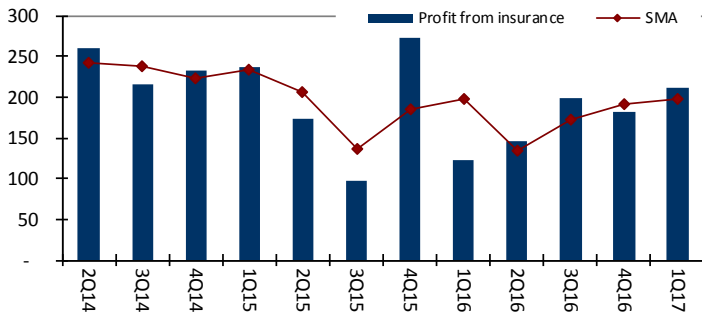


Fig 17: Profit from insurance



## Financials

### Income Statement

| Y/E Dec, SGD mn               | FY14         | FY15         | FY16         | FY17F        | FY18F        |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|
| Net Interest Income           | 4,736        | 5,189        | 5,052        | 5,157        | 5,233        |
| Fees and Commission           | 1,496        | 1,655        | 1,638        | 1,884        | 1,948        |
| Other Non interest income     | 2,109        | 1,878        | 1,799        | 1,941        | 1,952        |
| <b>Total operating income</b> | <b>8,341</b> | <b>8,722</b> | <b>8,489</b> | <b>8,982</b> | <b>9,133</b> |
| Operating expenses            | 3,258        | 3,665        | 3,789        | 3,902        | 3,931        |
| Provisions                    | 432          | 585          | 821          | 793          | 659          |
| <b>Operating profit</b>       | <b>4,651</b> | <b>4,472</b> | <b>3,879</b> | <b>4,288</b> | <b>4,543</b> |
| Associates & JVs              | 113          | 353          | 396          | 396          | 396          |
| <b>Profit Before Tax</b>      | <b>4,764</b> | <b>4,825</b> | <b>4,275</b> | <b>4,684</b> | <b>4,939</b> |
| Taxation                      | 687          | 717          | 629          | 675          | 715          |
| <b>Profit After Tax</b>       | <b>4,077</b> | <b>4,108</b> | <b>3,646</b> | <b>4,009</b> | <b>4,224</b> |
| Non-controlling Interest      | 233          | 205          | 173          | 211          | 222          |
| <b>Net Income, reported</b>   | <b>3,844</b> | <b>3,903</b> | <b>3,473</b> | <b>3,798</b> | <b>4,002</b> |
| <b>Net Income, adj.</b>       | <b>3,844</b> | <b>3,903</b> | <b>3,473</b> | <b>3,796</b> | <b>4,002</b> |

### Per share data (SGD)

| Y/E Dec, SGD mn | FY14 | FY15 | FY16 | FY17F | FY18F |
|-----------------|------|------|------|-------|-------|
| EPS, reported   | 1.02 | 1.00 | 0.87 | 0.96  | 1.01  |
| EPS, adj.       | 0.96 | 0.95 | 0.83 | 0.91  | 0.96  |
| DPS             | 0.36 | 0.36 | 0.36 | 0.36  | 0.36  |
| BVPS            | 7.46 | 8.15 | 8.61 | 8.93  | 9.26  |

### Supplementary items

| Y/E Dec, SGD mn | FY14  | FY15  | FY16  | FY17F | FY18F |
|-----------------|-------|-------|-------|-------|-------|
| CET1 CAR (%)    | 13.8% | 14.8% | 14.7% | 13.6% | 12.8% |
| Tier 1 CAR (%)  | 13.8% | 14.8% | 15.2% | 14.5% | 13.6% |
| Total CAR (%)   | 15.9% | 16.8% | 17.2% | 16.6% | 15.5% |

### Balance Sheet

| Y/E Dec, SGD mn              | FY14           | FY15           | FY16           | FY17F          | FY18F          |
|------------------------------|----------------|----------------|----------------|----------------|----------------|
| Cash bal with central banks  | 25,314         | 21,180         | 16,559         | 26,201         | 32,643         |
| Due from banks               | 41,220         | 35,791         | 39,801         | 42,939         | 40,669         |
| Debt and equity securities   | 23,466         | 22,786         | 23,157         | 23,113         | 23,345         |
| Loans and bills receivable   | 207,535        | 208,218        | 216,830        | 224,986        | 230,648        |
| Life Assur. Fund Inv. Assets | 57,286         | 56,983         | 61,973         | 63,832         | 65,747         |
| Others                       | 46,405         | 45,232         | 51,564         | 49,063         | 49,620         |
| <b>Total Assets</b>          | <b>401,226</b> | <b>390,190</b> | <b>409,884</b> | <b>430,134</b> | <b>442,672</b> |
| Due to banks                 | 20,503         | 12,048         | 10,740         | 12,123         | 12,244         |
| Due to non-bank customers    | 245,519        | 246,277        | 261,486        | 273,568        | 281,797        |
| Life Assur. Fund Liabilities | 57,224         | 56,994         | 61,962         | 63,821         | 65,735         |
| Debts issued                 | 28,859         | 23,479         | 19,947         | 22,869         | 23,098         |
| Others                       | 14,936         | 14,282         | 16,107         | 16,584         | 17,075         |
| <b>Total liabilities</b>     | <b>367,041</b> | <b>353,080</b> | <b>370,242</b> | <b>388,965</b> | <b>399,950</b> |
| Shareholder's equity         | 31,097         | 34,553         | 37,007         | 38,323         | 39,654         |
| Non-controlling interest     | 3,088          | 2,558          | 2,635          | 2,846          | 3,068          |
| <b>Total Equity</b>          | <b>34,185</b>  | <b>37,111</b>  | <b>39,642</b>  | <b>41,169</b>  | <b>42,722</b>  |

### Valuation Ratios

| Y/E Dec, SGD mn    | FY14 | FY15 | FY16 | FY17F | FY18F |
|--------------------|------|------|------|-------|-------|
| P/E (X), adj.      | 10.1 | 11.0 | 12.6 | 11.5  | 10.9  |
| P/B (X)            | 1.3  | 1.1  | 1.05 | 1.17  | 1.13  |
| Dividend Yield (%) | 3.7% | 4.1% | 4.0% | 3.8%  | 3.8%  |

### Growth & Margins (%)

|                                | FY14  | FY15  | FY16   | FY17F | FY18F |
|--------------------------------|-------|-------|--------|-------|-------|
| <b>Growth</b>                  |       |       |        |       |       |
| Net interest income            | 22.0% | 9.6%  | -2.6%  | 2.1%  | 1.5%  |
| Non interest income            | 31.6% | -2.0% | -2.7%  | 11.3% | 1.9%  |
| Pre provision operating profit | 26.0% | 4.6%  | -2.7%  | 5.8%  | 1.7%  |
| Operating income               | 32.4% | -3.8% | -13.3% | 10.5% | 6.0%  |
| Net income, reported           | 38.9% | 1.5%  | -11.0% | 9.3%  | 5.4%  |
| Net income, adj                | 38.9% | 1.5%  | -11.0% | 9.3%  | 5.4%  |

### Margins

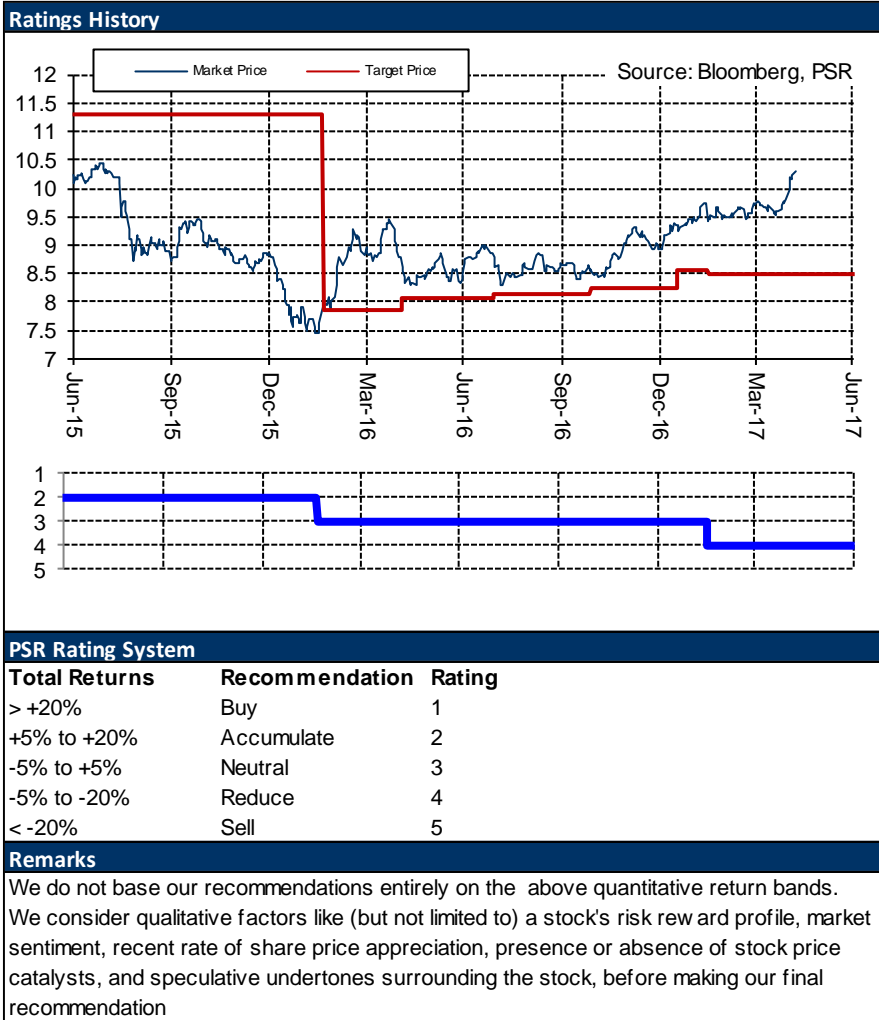
|                     | FY14  | FY15  | FY16  | FY17F | FY18F |
|---------------------|-------|-------|-------|-------|-------|
| Net interest margin | 1.68% | 1.67% | 1.67% | 1.60% | 1.59% |

### Key Ratios (%)

|                                 | FY14  | FY15  | FY16  | FY17F | FY18F |
|---------------------------------|-------|-------|-------|-------|-------|
| ROE                             | 12.9% | 11.6% | 9.6%  | 10.2% | 10.4% |
| ROA                             | 1.1%  | 1.2%  | 1.0%  | 1.0%  | 1.0%  |
| RORWA                           | 2.0%  | 2.0%  | 1.8%  | 1.7%  | 1.6%  |
| Non-interest/total income ratio | 43.2% | 40.5% | 40.5% | 42.6% | 42.7% |
| Cost/income ratio               | 39.1% | 42.0% | 44.6% | 43.4% | 43.0% |
| Loan/deposit ratio              | 84.5% | 84.5% | 82.9% | 82.2% | 81.8% |
| NPL ratio                       | 0.61  | 0.93  | 1.26  | 1.31  | 1.30  |

Source: Company, Phillip Securities Research (Singapore) Estimates

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





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