

# Sector Report

Singapore Banking Sector

## Global Macro Strategy

US dollar weakness brings a renewed beginning for Gold

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# Singapore Banking Sector

## Stronger Economy and Higher Dividends Expected

Jeremy Teong  
Phillip Securities Research Pte Ltd  
18 Sept 2017

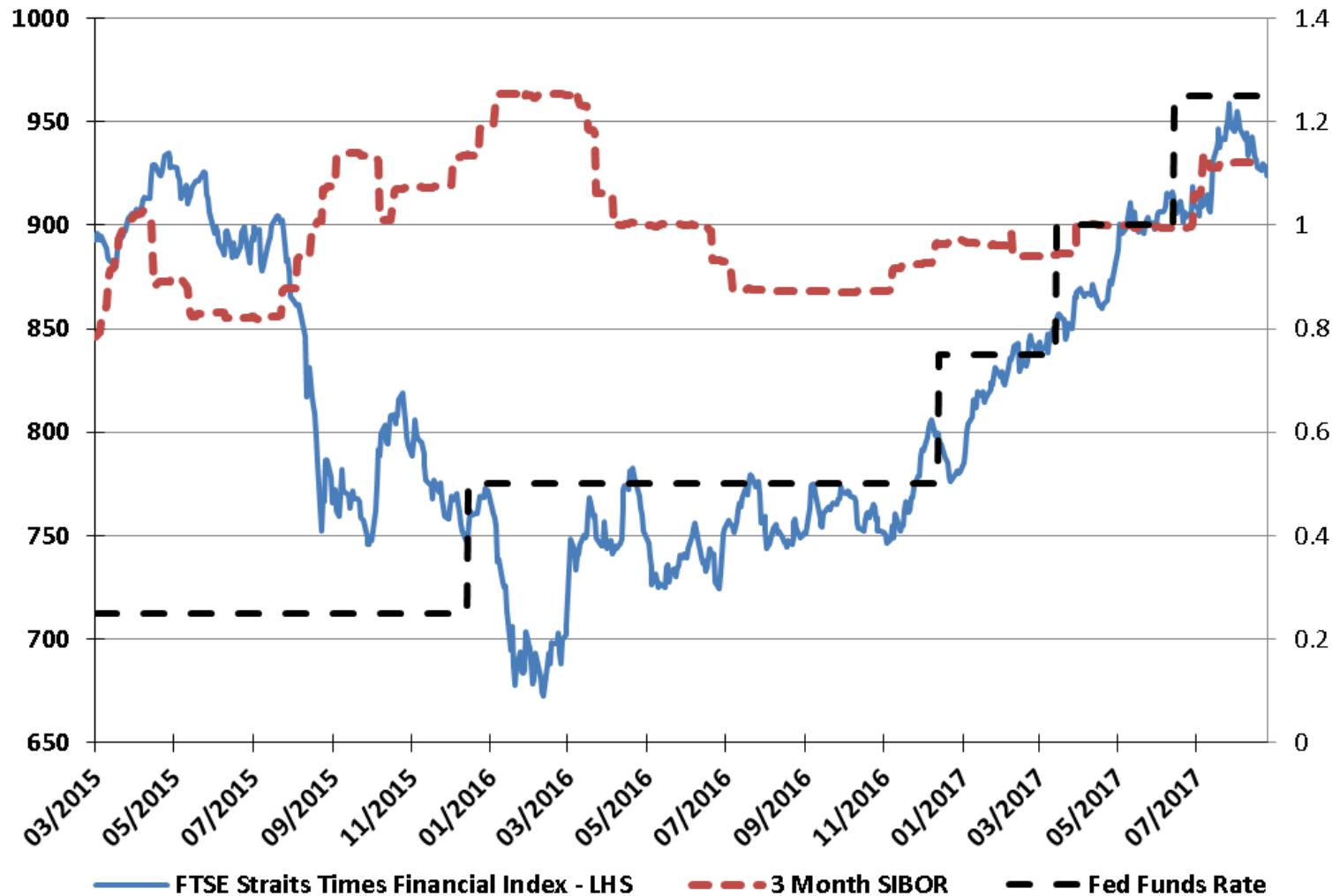
- **Singapore Banking Sector : Upgrade to Neutral from Underweight**
  - Positive loans volume and rate dynamics as economy improves.
  - But competition for Singapore based loans will limit the sensitivity to rising rates
  - Excess capital can be returned to shareholders in the form of dividends as CET 1 is well above requirement and negative EV is forming.
- **DBS**
  - Upgrade to Accumulate from Reduce. TP: S\$21.45, previously S\$17.92
  - Able to compete effectively as it has highest Singapore CASA ratio of 91% and largest deposit base of S\$342.9bn
  - Strong WM franchise with rising yield on AUM. Boosted by acquisition of ANZ WM in 5 Asian markets
- **OCBC**
  - Maintain Neutral. TP: S\$10.81
  - Stronger WM base with acquisition of Barclays and NAB wealth business in Asian markets
  - Product synergies across GEH, Lion Global and BOS. More than 30% contribution to total income. Less pressure to compete on loans
- **UOB**
  - Maintain Reduce. TP: S\$20.18
  - Weakest WM franchise amongst the 3 banks.
  - Lowest overall CASA ratio of 44% and deposit base of S\$260bn.

# A Look at Guidance, Consensus and Results

	1H17 results			FY17e guidance			FY17e Consensus			Commentary
	DBS	OCBC	UOB	DBS	OCBC	UOB	DBS	UOB	OCBC	
<b>Loans growth (YoY)</b>	6.6%	11.4%	7.3%	Mid-Single Digit %	Mid-Single Digit %	Mid-Single Digit %	3.6%	5.1%	3.8%	Actual growth has outperformed guidance and consensus
<b>NIM</b>	1.74%	1.65%	1.74%	c.1.8%	c.1.65%	c.1.7%	1.78%	1.69%	1.73%	Actual NIM is lagging as loans growth outpaces interest rate growth
<b>Allowances</b>	1H17 S\$854mn, forming 82.6% of guidance	-	32bps	FY17e total allowance c.S\$1.03bn (ex Swiber c.S\$400mn)	-	32bps	S\$1.32bn	S\$725mn	S\$724mn (32bps)	Allowances could increase more than expected as oil and gas sector continues to grapple with low cash flow
<b>NPL</b>	Stable since 4Q16			Expect NPLs to stabilise.			NPA ratio higher 14% YoY			Elevated Net NPL formation offset by write-offs may continue to weigh down on coverage ratio

Source: Bloomberg, PSR estimates

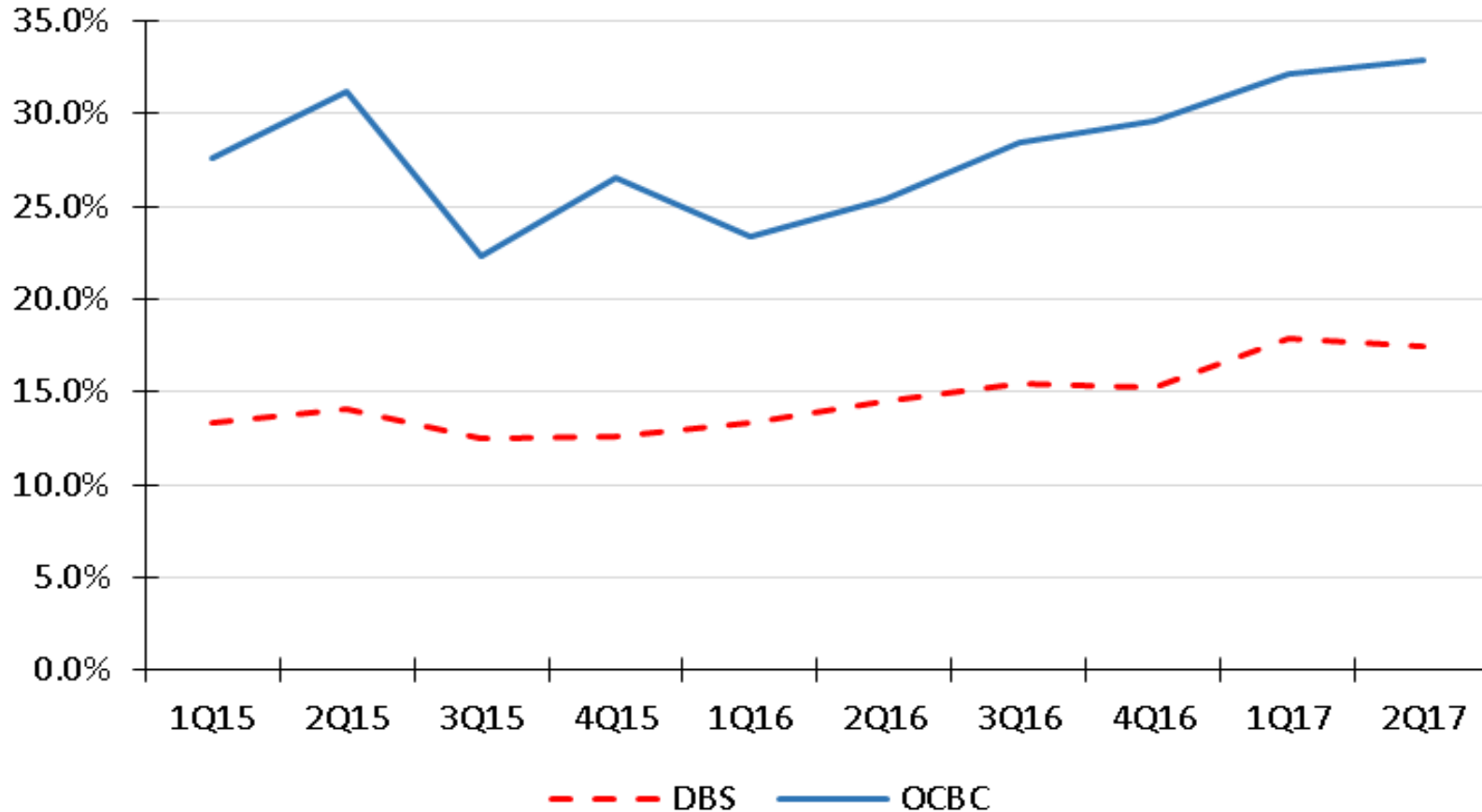
# Banks' Share Price vs SIBOR



- Late 2015 to early 2016, SIBOR rose as economy remains weak.
- Capital outflows during that period.
- Economy improves late Dec 2016 but SIBOR upward movement is more subdued.

Source: Bloomberg, PSR estimates

# WM Income contribution\* to Total Income

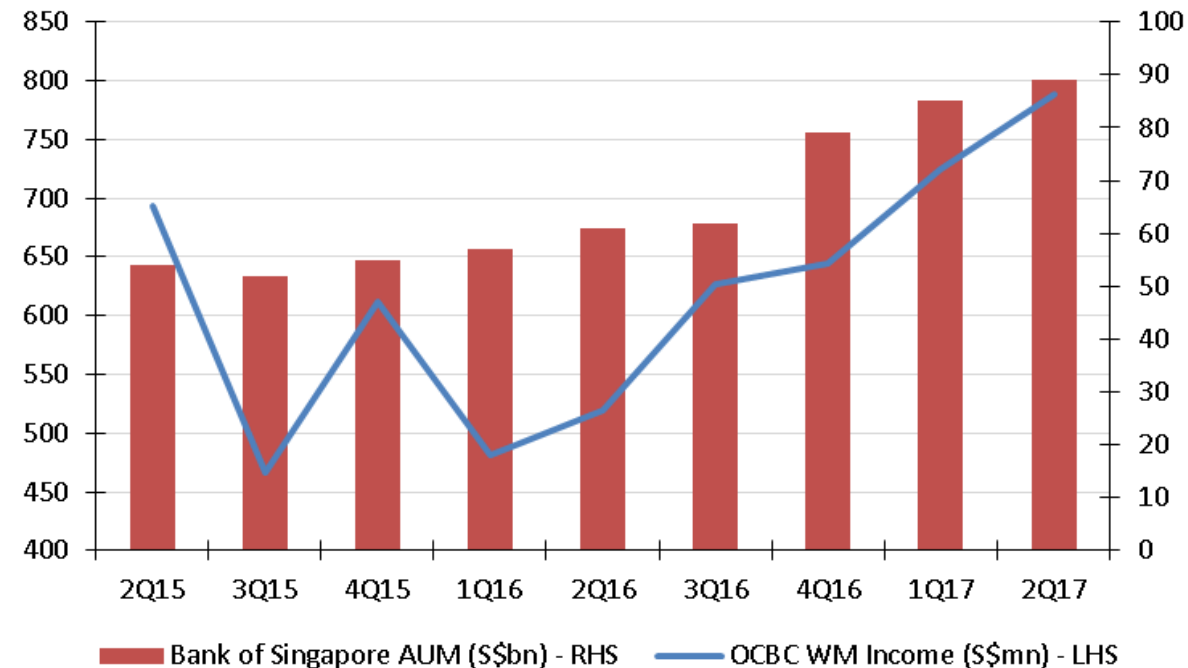
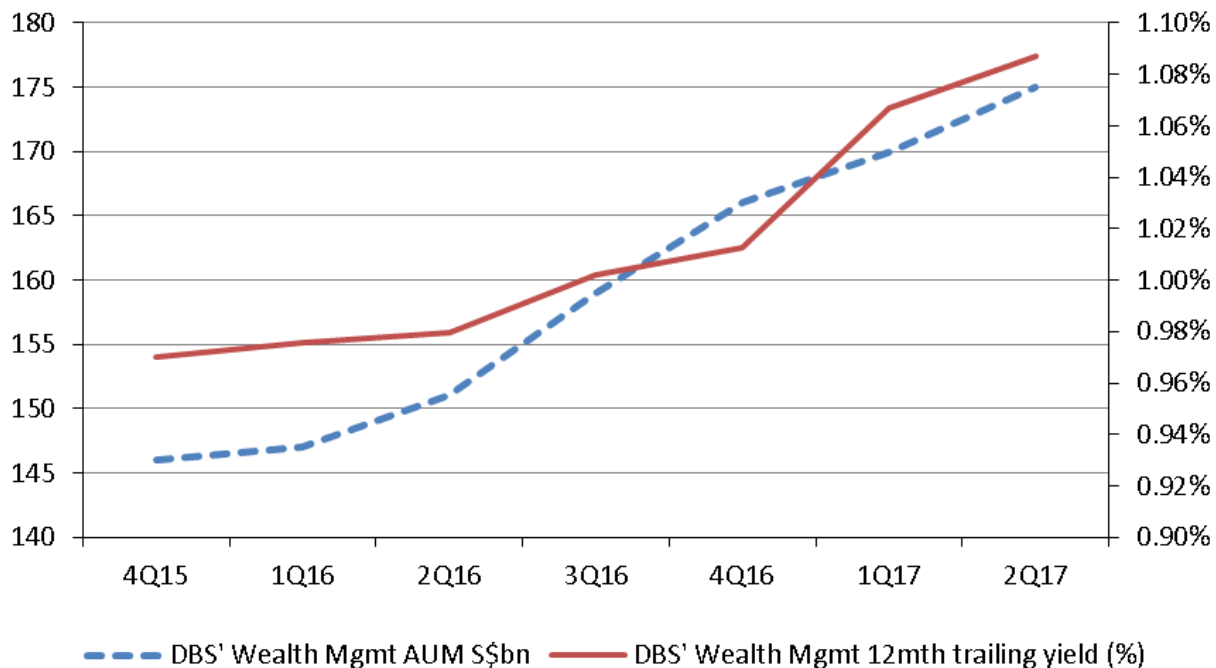


- GEH, Lion Global and BOS boost WM share of OCBC's total income.
- DBS has a strong WM franchise from its Treasures, Treasures Private Client and Private Bank.
- UOB does not disclose breakdown
- Strong WM increases banks' value proposition

Source: Company, PSR estimates

\* UOB does not separately disclose their WM income in full detail

# WM Performance

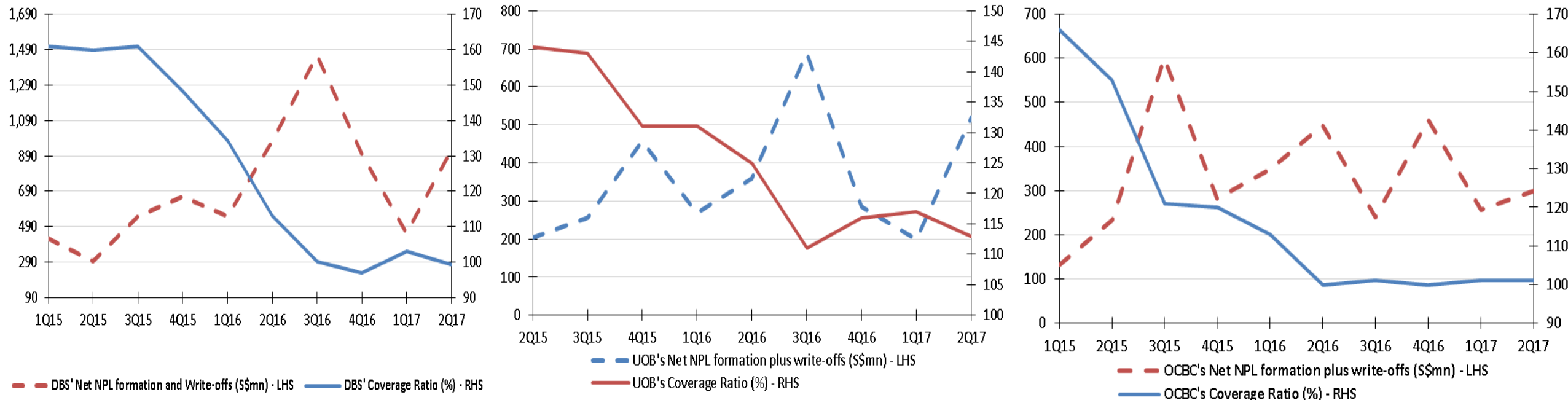


Source: Company, PSR estimates

- DBS's yield on WM AUM is rising along with AUM volume.
- OCBC only discloses BOS AUM (private bank). But income contribution from GEH and Lion Global segments have OCBC's WM income to maintain the lead over it peers
- UOB AUM from Privilege Banking, Privilege Reserve and Private Bank is only S\$99bn as of 2Q17.



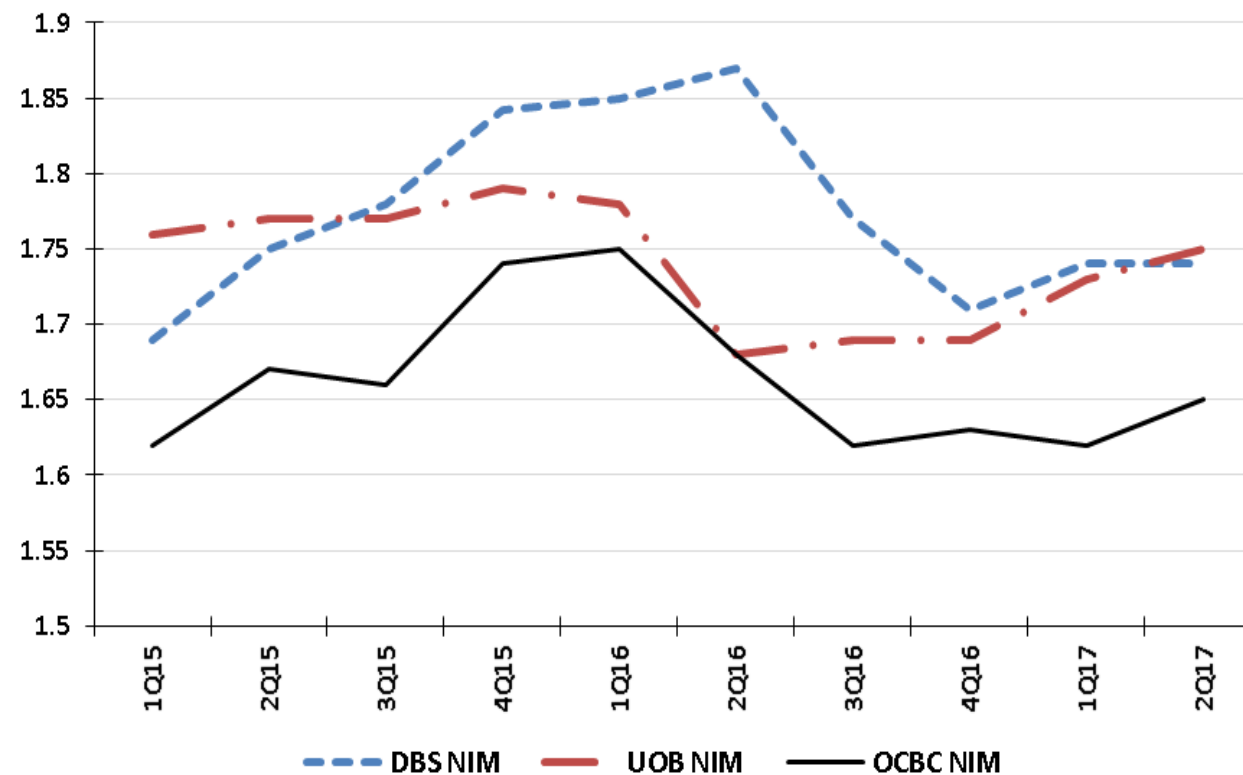
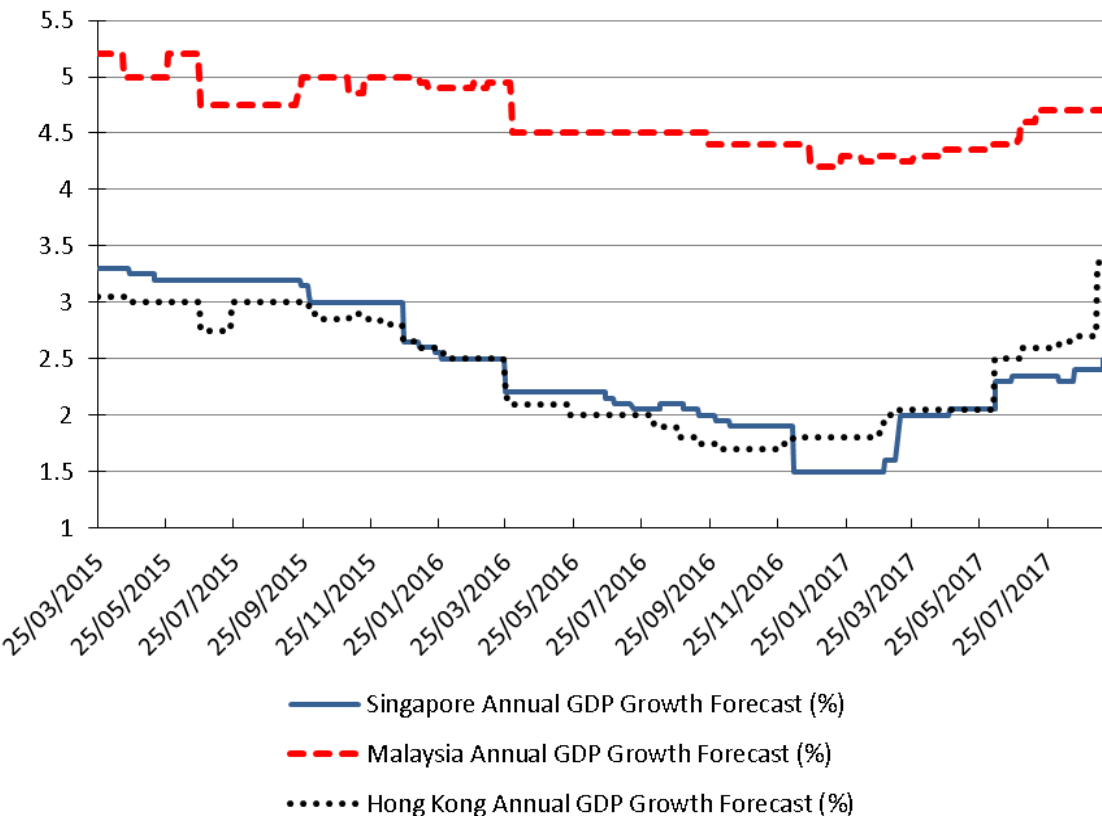
# Low Coverage Ratio remains a Concern



Source: Company, PSR estimates

- Offshore O&G have been languishing for a long time. Write-offs can become elevated as recovery prospects remain poor.
- Though NPLs appear stable, coverage ratio is at a historical low.
- Taken together, Singapore banks have to respond to any elevated NPLs and write-offs at any given quarter.
- Ability to raise PPOP at any given quarter to raise provisions
- Positive loan volume and rate dynamics will help.

# Tailwind of Stronger GDP growth



Source: Bloomberg, Company, PSR estimates

- Stronger GDP forecast across Singapore banks' key markets supports loans growth and positive volume and rate dynamics.
- Expect NIMs expansion to be subdued as loans growth will be the main driver of NII.

# Loans Growth and NII



Source: Company, PSR estimates

- Loans growth has been driving NII after 2H16
- Recall SIBOR was rose quickly from 3Q15 to 1Q16 then declined in 2H16.
- OCBC shows greatest sensitivity to SIBOR. OCBC has about 40% of its Singapore based loans is priced in SIBOR.
- Pass through of higher interest rates to be crimped by competition especially in the property sector.

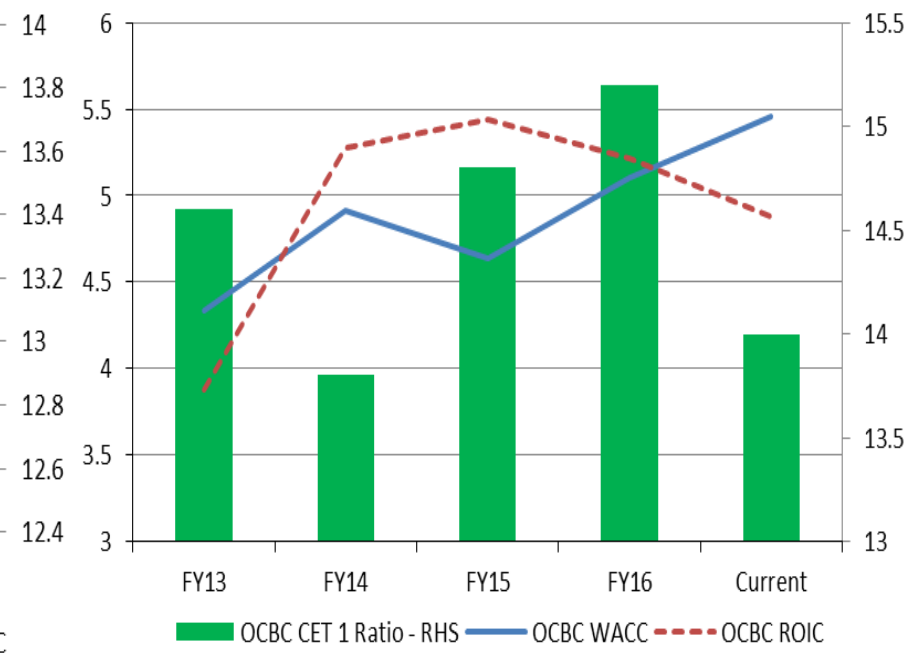
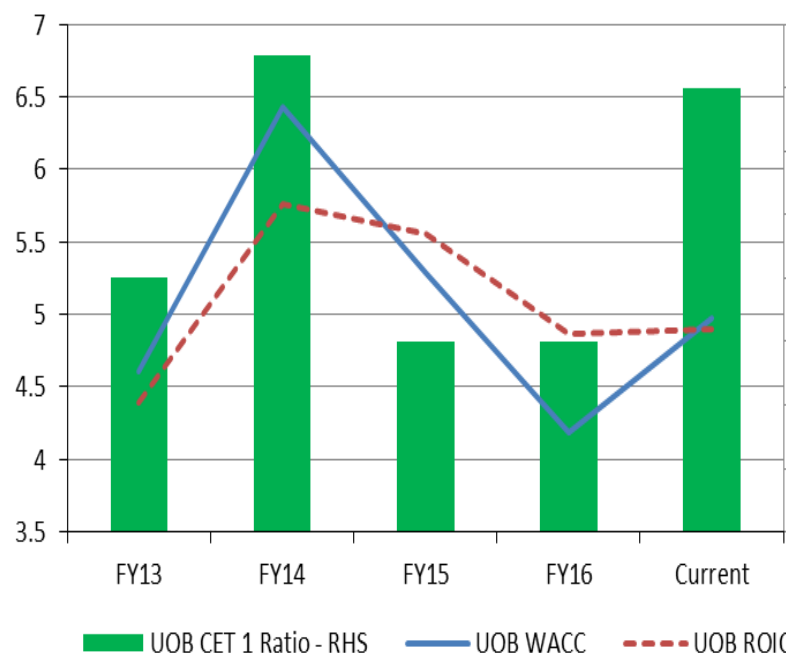
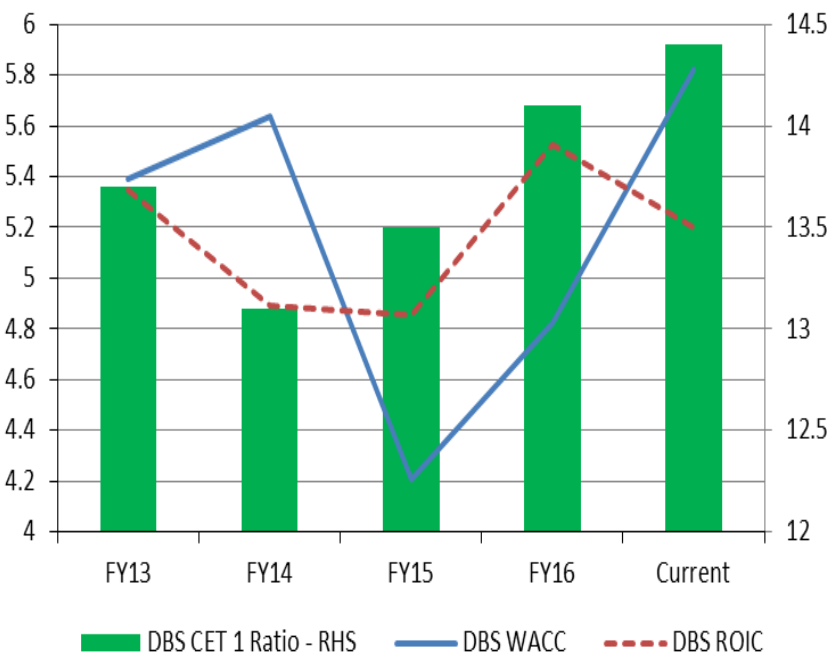
# Singapore Home Loans becoming less Sensitive to Benchmark Rates

	BOC	UOB	OCBC	DBS	MayBank
Before Dec 2016	2-year fixed rate at 1.4%	2-year fixed rate at 1.8%	2-year fixed rate at 2.38%	3-year fixed rate at 1.88%. Removed the 5-year fixed rate at 1.99%.	Removed the 2-year 1.6% fixed rate in Nov 2016
Sept 2017	2-year fixed rate at year 1: 1.48%, year 2: 1.58%	2-year fixed rate at 1.48%	2-year fixed rate at 2.38%	3-year fixed rate at 1.68%	2-year fixed rate at year 1: 1.48%, year 2: 1.58%

Source: Straits Times, Moneysmart.sg

- Singapore home loans make up 15% to 20% of Singapore banks gross loans
- DBS introduced FHR packages in 2014 and currently do not offer SIBOR pegged mortgage loans. Take up rate for FHR package is c.90%.
- DBS, UOB, HSBC and BOC have recently rolled out 3 year fixed rate at 1.68% despite SIBOR is on a rising trend.

# Excess Capital Build Up and Negative EV

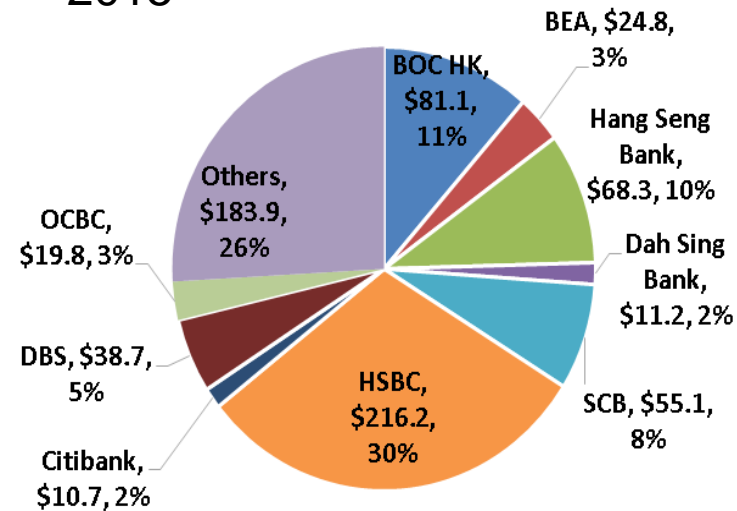


Source: Bloomberg, Company, PSR estimates

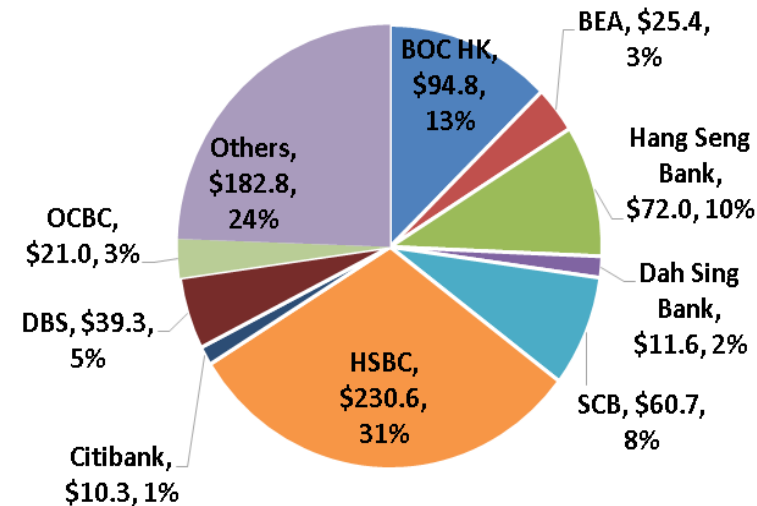
- CET 1 regulatory hurdle is 6.5%. Singapore banks CET 1 ratio at c.14%.
- As NIMs are expected to remain subdued, ROIC growth outlook may also be weak
- Capital that cannot be deployed to improve ROIC above WACC should be returned to shareholders.

# Hong Kong Domestic Loans Market Share

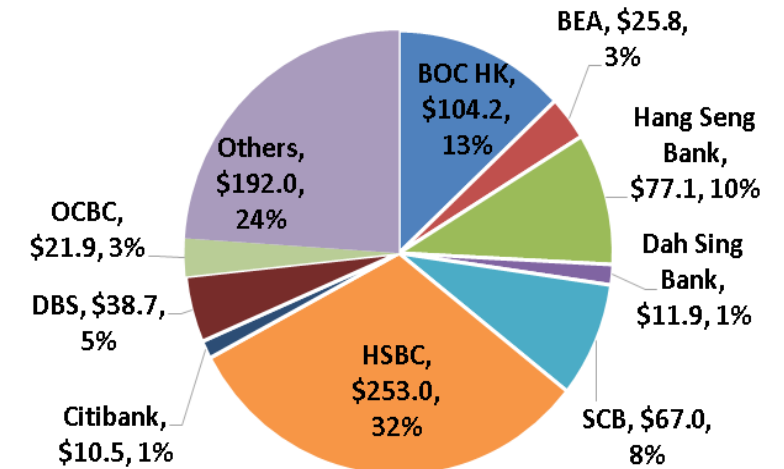
2015



2016



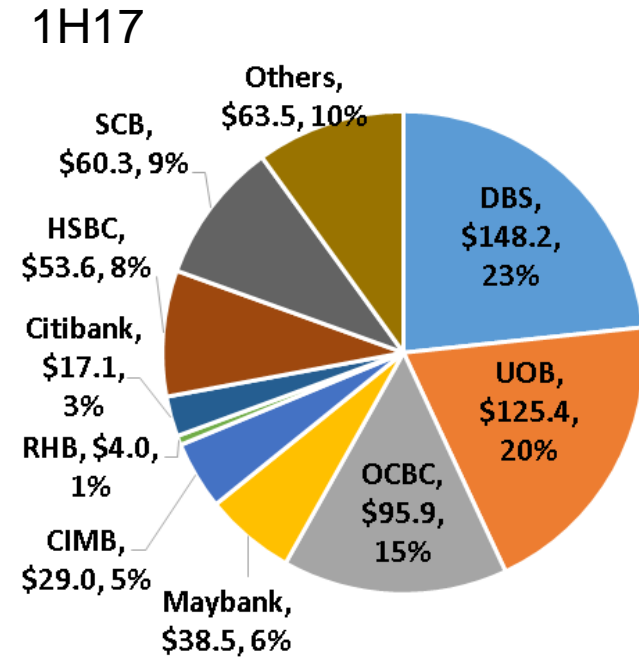
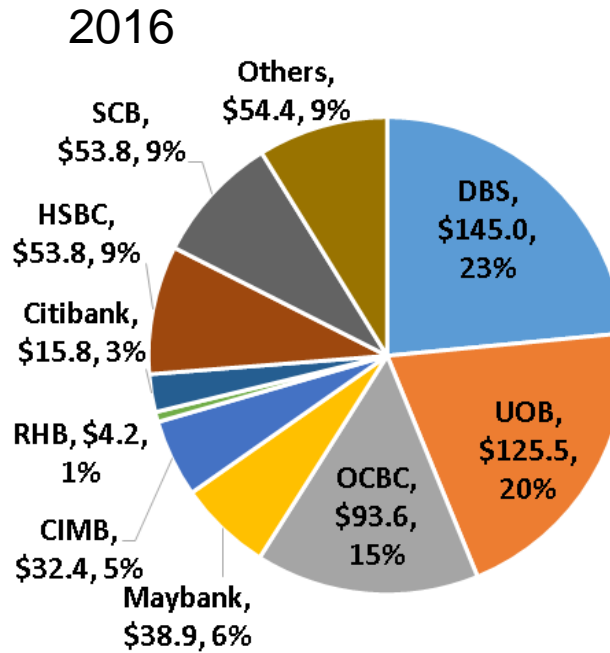
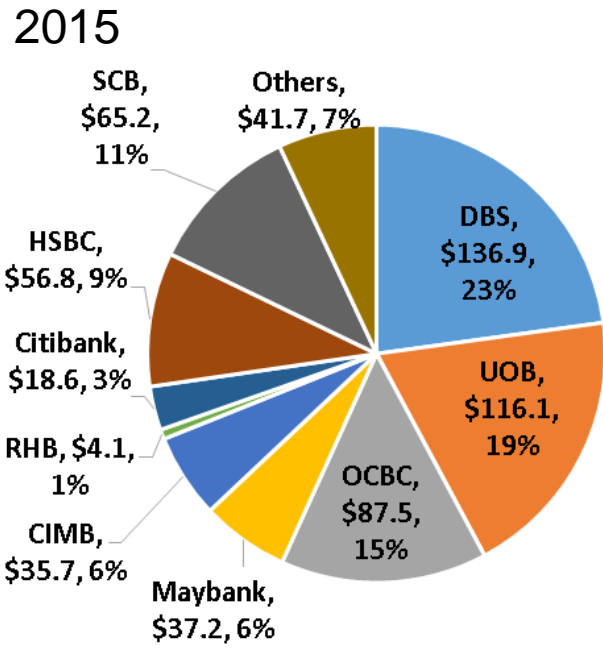
1H17



Source: HKMA, Company Reports, PSR estimates

- DBS and OCBC experienced compressed NIM as low HIBOR impacted their HIBOR pegged loans.
- HSBC and BOC grew their loans at a fast pace in 1H17.
- HSBC poses strong competition not just in Hong Kong but also in the Pearl River Delta region where it is ramping up its presence aggressively.

# Singapore Domestic Loans Market Share



Source: MAS, Company Reports, PSR estimates

- DBS and OCBC grow their market share of loans because of the acquisition of ANZ wealth business in five Asian markets by DBS; Barclays and NAB Asian wealth business by OCBC.
- DBS and OCBC strong wealth management franchise will help improve scale and synergy.

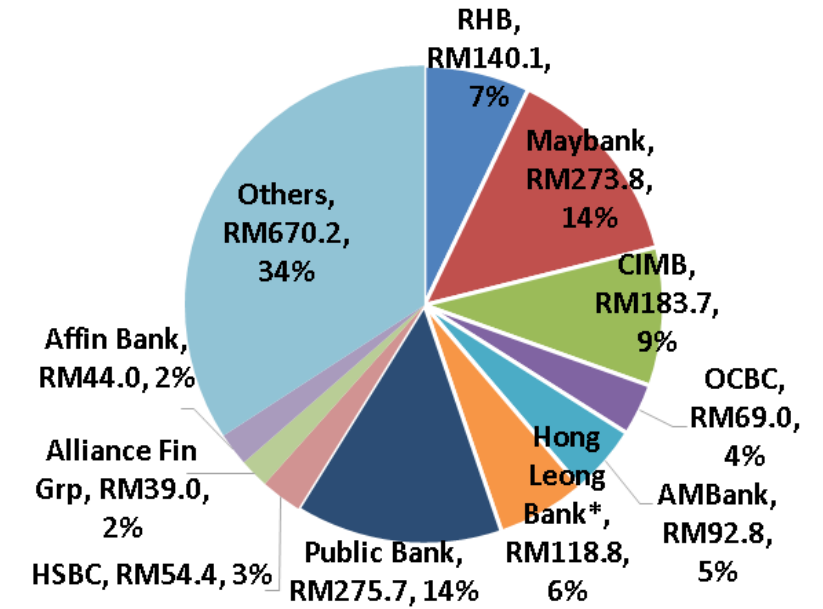
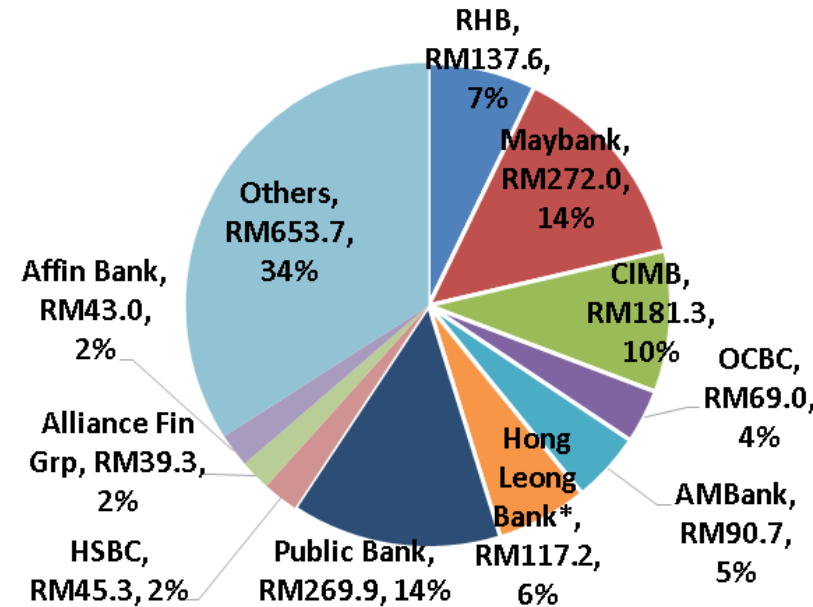
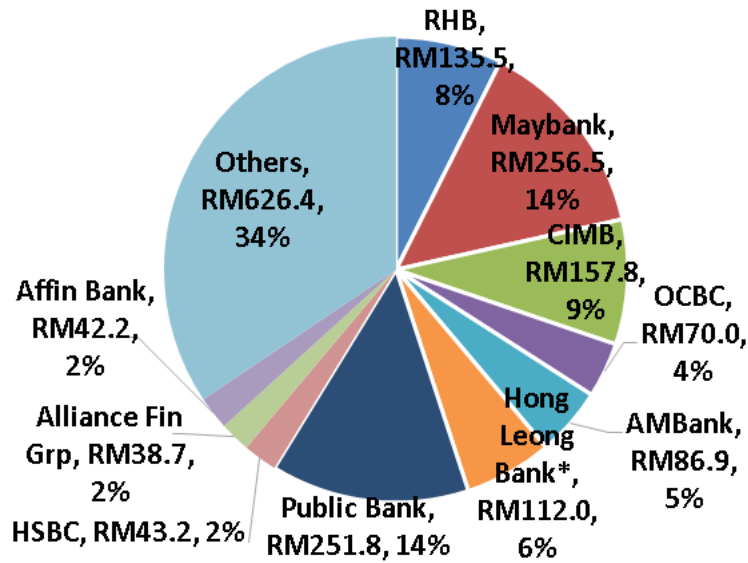


# Malaysia Domestic Loans Market Share

2015

2016

1H17



Source: BNM, Company Reports, PSR estimates

- Potential mergers of the top Malaysian banks had failed to go through (CIMB and RHB in 2015; RHB and AmBank in 2017).
- Malaysian market remains fragmented and we expect competition to be more volatile.

\* Estimates using geographical breakdown information from FYE June 2015 and 2016 annual report.



# Peer Comparison across Key Markets

Ticker	Name	Div Yield (%)	ROA (%)	ROE (%)	P/E (x)	P/B (x)	NIM (%)	Non-Performing Assets to Total Loans (%)	Total Loans to Total Deposits (%)	Total Loans 1Y Growth (%)
<b>Singapore</b>										
DBS SP Equity	DBS	3.04	0.95	10.10	12	1.1	1.74	1.6	89.7	6.6
OCBC SP Equity	OCBC	3.26	1.21	11.90	12	1.2	1.67	1.3	86.5	11.3
UOB SP Equity	UOB	2.95	0.99	10.30	13	1.2	1.78	1.6	87.6	7.3
<b>Simple Average</b>		<b>3.08</b>	<b>1.05</b>	<b>10.77</b>	<b>12</b>	<b>1.2</b>	<b>1.73</b>	<b>1.5</b>	<b>87.9</b>	<b>8.4</b>
<b>Malaysia</b>										
MAY MK Equity	MayBank	5.52	1.02	11.17	13	1.4	1.88	2.5	99.2	6.4
PBK MK Equity	Public Bank	2.86	1.38	15.60	15	2.2	2.06	0.5	94.1	5.3
CIMB MK Equity	CIMB	2.96	0.86	9.30	14	1.3	2.58	3.2	93.0	8.2
HLBK MK Equity	Hong Leong Bank	2.91	1.11	9.79	15	1.4	1.79	1.0	80.6	3.8
RHBBANK MK Equity	RHB Bank	2.38	0.77	8.09	12	0.9	1.72	2.3	94.4	3.2
AMM MK Equity	AM Bank	4.10	1.00	8.36	10	0.8	1.45	1.9	99.8	6.6
AFG MK Equity	Alliance Financial Grp	4.27	0.94	10.24	11	1.1	1.71	1.1	88.3	1.3
AHB MK Equity	Affin Holdings	3.56	0.81	6.56	9	0.6	1.67	2.0	89.9	1.9
<b>Simple Average</b>		<b>3.57</b>	<b>0.99</b>	<b>9.89</b>	<b>12</b>	<b>1.2</b>	<b>1.86</b>	<b>1.8</b>	<b>92.4</b>	<b>4.6</b>
<b>Hong Kong</b>										
2356 HK Equity	Dah Sing Banking Grp	2.28	1.17	10.23	10	1.0	2.04	1.3	74.0	3.3
2388 HK Equity	BOC Hong Kong	3.02	1.20	12.87	15	1.7	1.65	0.2	69.0	11.9
11 HK Equity	Hang Seng Bank	3.51	1.33	13.23	19	2.5	1.84	0.5	73.5	9.6
23 HK Equity	Bank of East Asia	2.70	1.02	8.91	31	1.1	1.73	1.6	82.1	3.7
<b>Simple Average</b>		<b>2.88</b>	<b>1.18</b>	<b>11.31</b>	<b>19</b>	<b>1.6</b>	<b>1.82</b>	<b>0.9</b>	<b>74.6</b>	<b>7.1</b>
<b>London</b>										
HSBA LN Equity	HSBC	5.48	0.12	1.35	87	1.0	1.17	1.7	70.7	3.4
STAN LN Equity	Standard Chartered	0.00	0.07	0.20	316	0.6	1.63	3.6	69.4	0.9

# Global Macro Strategy

## US dollar weakness brings a renewed beginning for Gold

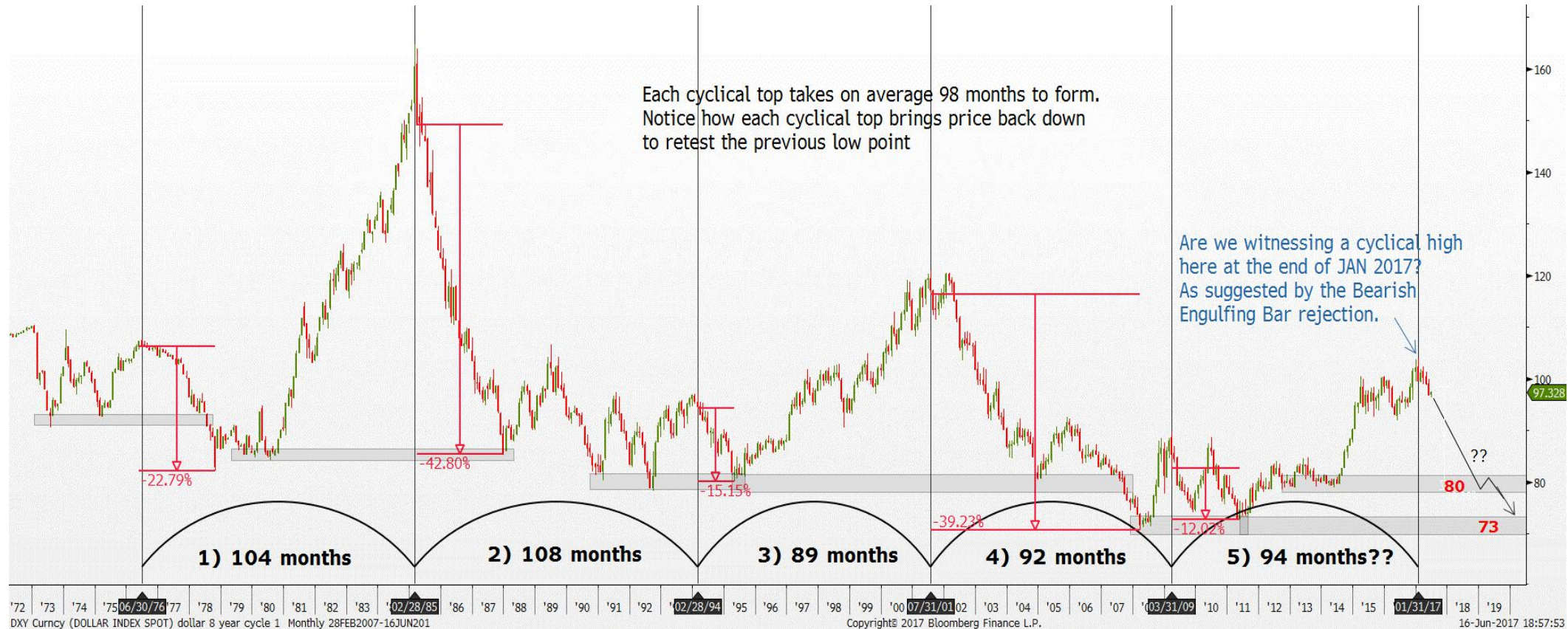
Pei Sai Teng

Phillip Securities Research Pte Ltd

18 September 2017

# Dollar hit cycle top, 30% downside to go

- Base on a previous technical analysis report, our house view is for dollar to head lower
- Our fundamental studies support this thesis



Source: Bloomberg

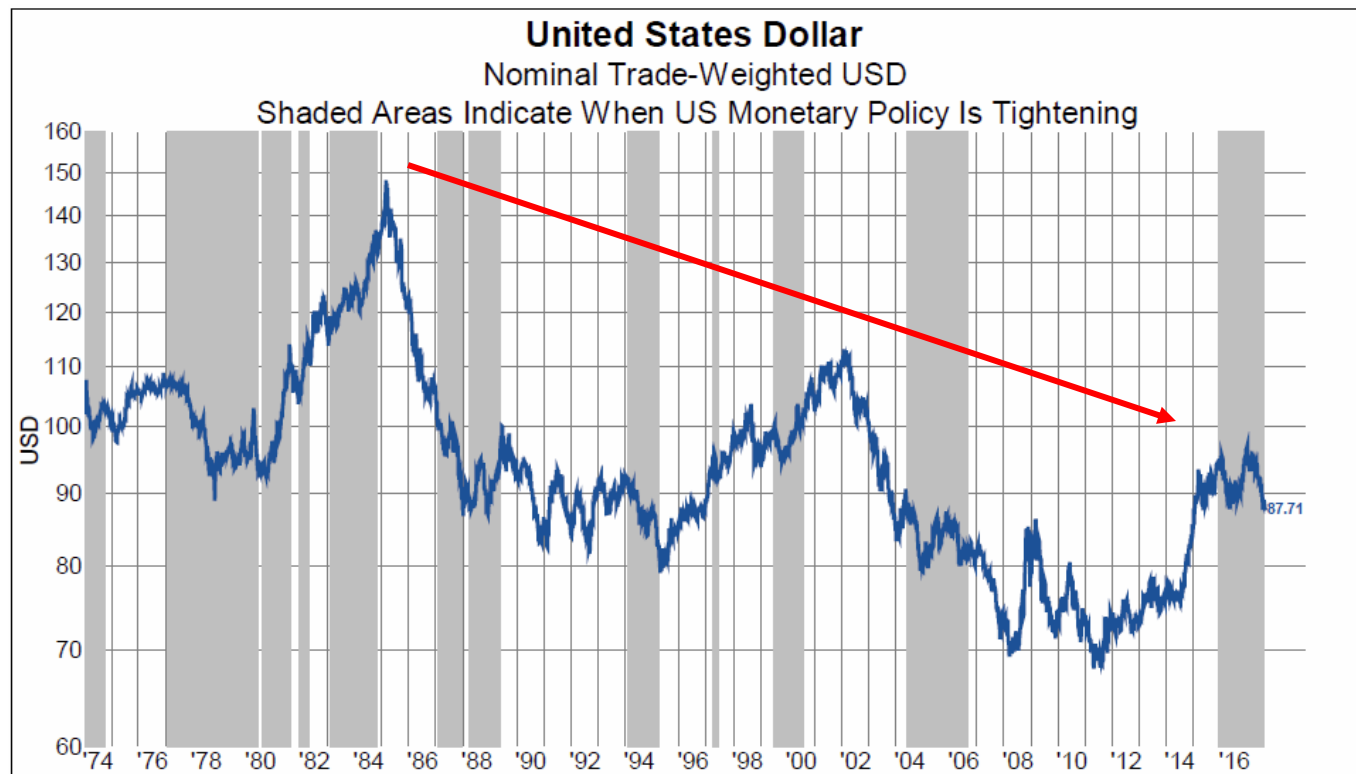
# Dollar weakness renews Bull run in Gold

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- Contrary to market expectation, we believe that the **US Dollar (USD) will continue to weaken in the months ahead.**
  - Debt overhang in the private sector will limit future economic growth via credit expansion
  - Debt ceiling impasse might cause potential re-rating of U.S. Treasuries from major credit rating agency
  
- A weakening dollar is positive for Gold. We believe **Gold will continue to rally past its 2016 high.**
  - Positive net Inflows into Gold-backed ETFs for 2016 and 2017 suggests stronger interest from investors
  - Central Banks are accumulating gold as part of their foreign currencies reserve, highlight the significant of gold as a storage of value.

# Tightening monetary policies doesn't mean strong USD

- During period of monetary tightening (indicated by the shaded area in the chart), USD does not necessary strengthen.
- In fact, we find the USD correlates more with aggregate saving rate and confidence in the current administration.



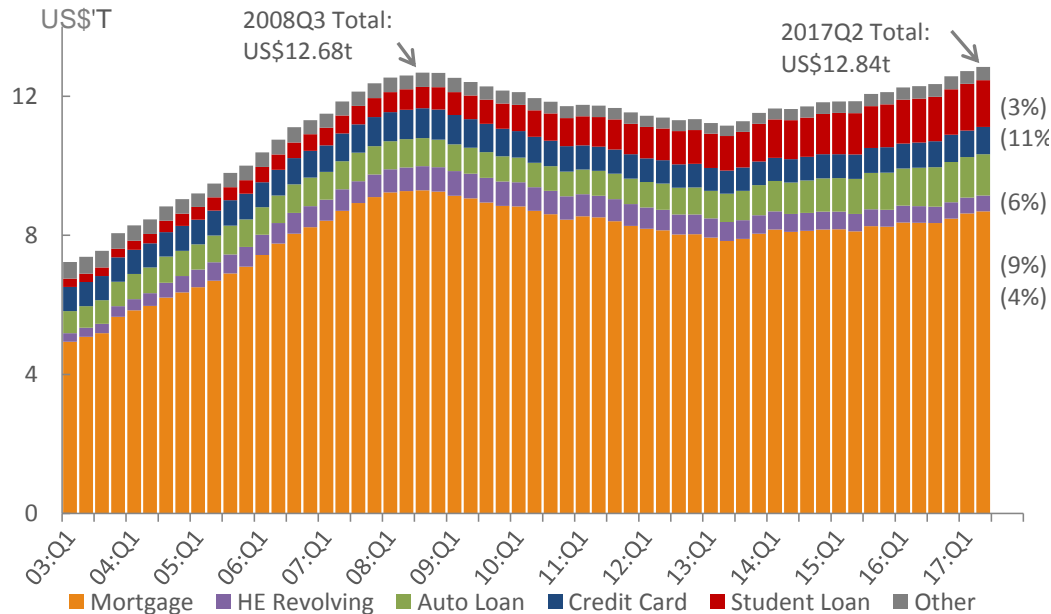
Source: Knowledge Leaders Capital, LLC



# Main weakness to Dollar lies in the loss of confidence

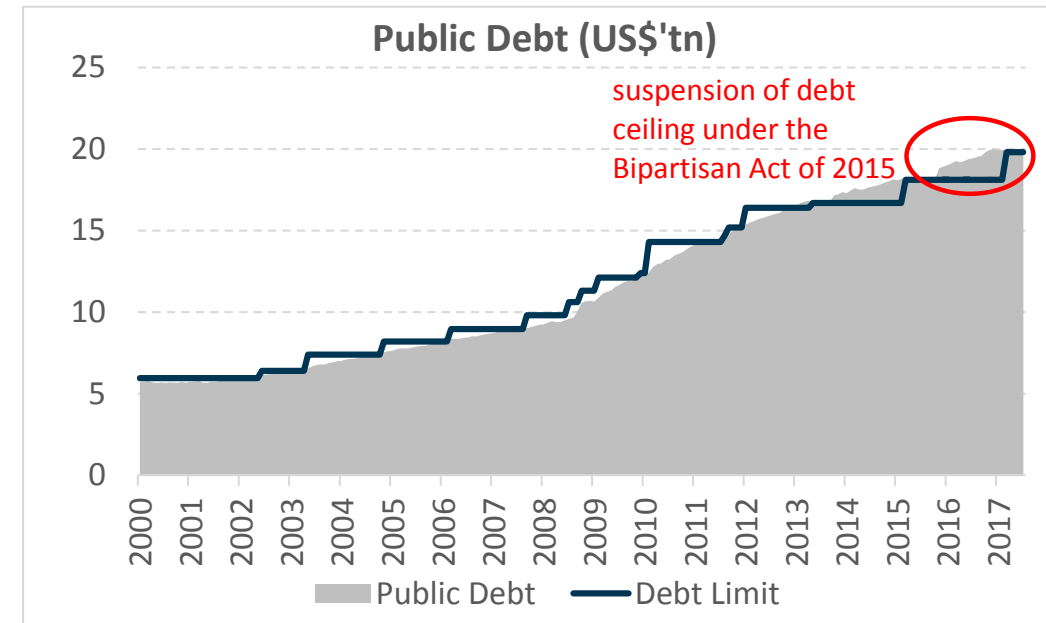
- As of today, U.S. has never been more leveraged than any point in their history.
- The private household debt and the national public debt are at record high, easily surpassing the historical high of the Great Financial Crisis (GFC) in 2008.

## Total Household Debt back above 2008 high



Source: New York Fed Consumer Credit Panel/Equifax

## National Debt is now above US\$20T



Source: CEIC, Bureau of the Fiscal Service, PSR

# An Overleverage economy weighs down on USD

## Household Debt

- **Debt overhang for America Household**
- Non-housing debts such as Auto loan debt, student loan debt and credit card debt have reached unprecedented record size.
- However, unlike mortgage loans these unsecured debts have no salvage value in time of default.
- This debt overhang handicapped the U.S. economy from expanding through further credit expansion.

## National Debt

- **Debt ceiling impasse incur potential downgrade woe**
- Debt ceiling negotiation postponed till December.
- Moody's threaten to downgrade credit rating of U.S. Treasuries if a bill was not pass to raise the debt ceiling.
- If Moody's were to downgrade, they will be the second largest credit agency to downgrade U.S. Treasuries after Standard & Poor's credit rating agency.

# Trump's Administration remains unsettled

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- The stability of a nation can usually be inferred from the political party in power.
- The current presidential administration remains unsettled with high turnover of prominent posts.
- Failure in keeping up with campaign promises
  - Lost the vote to repeal and replace the Affordable Care Act
  - No Mexico wall
  - No Tax reform proposed
- Ongoing Special Counsel Investigation on the link between Trump's 2016 presidential campaign
- In which, the worst case scenario could see a possible impeachment



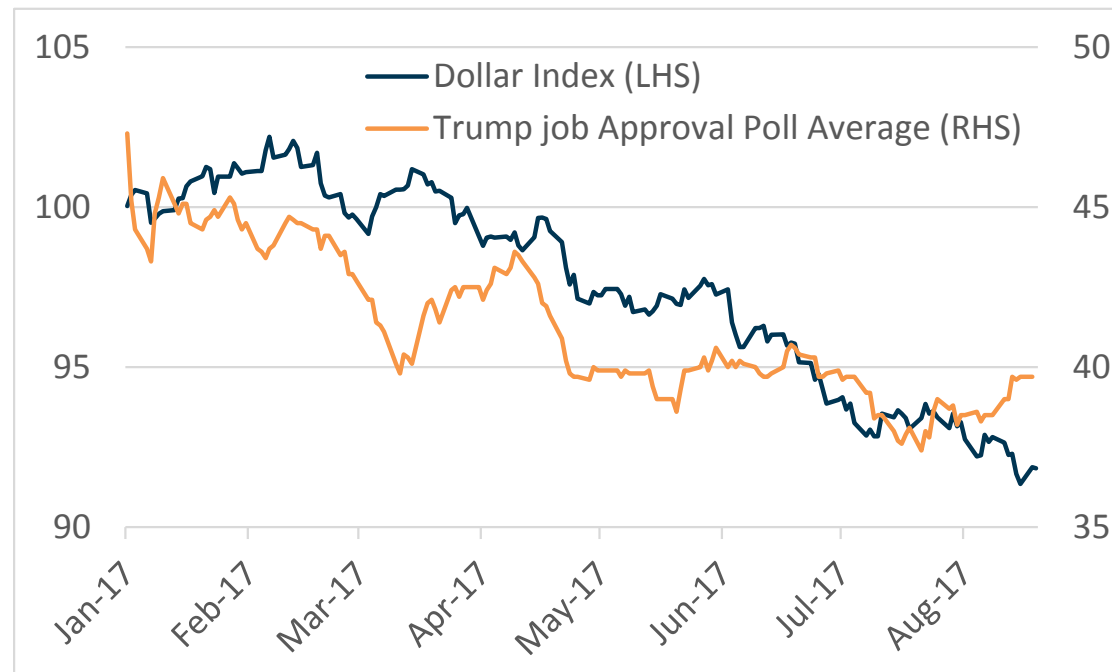
# No longer with Trump Administration



White House staff are sworn in on Jan. 22 in the East Room. Photo by Al Drago/The New York Times

# USD sink in line with Trump's approval rating

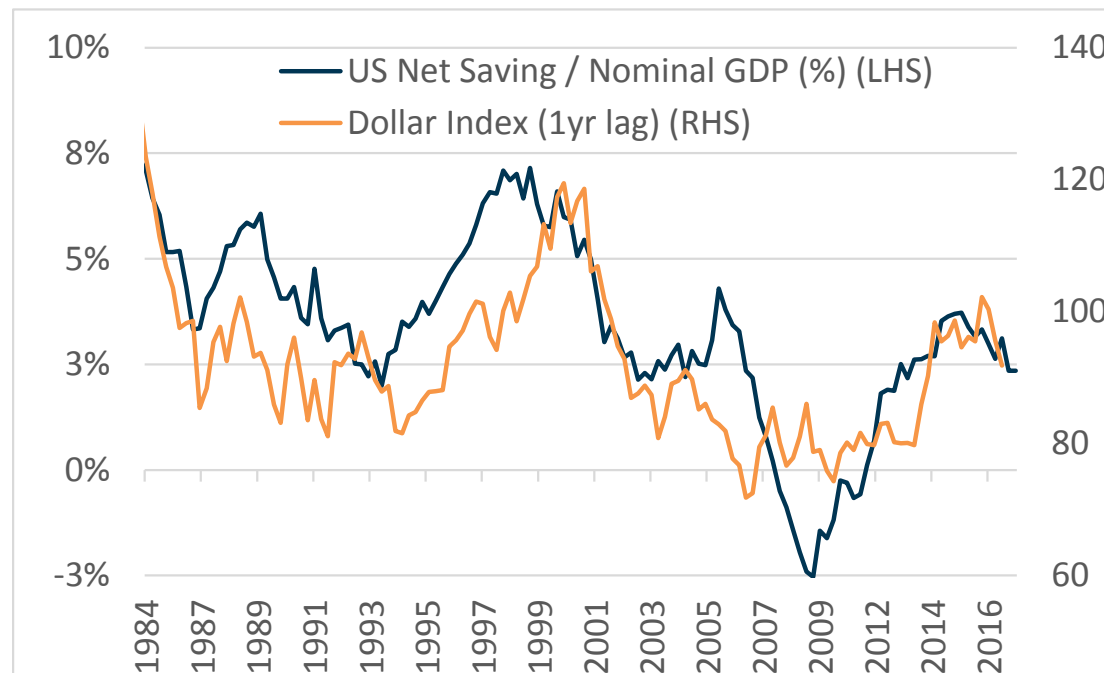
- Although it is just eight months into his Presidential term, it is safe to say that Trump has yet to meet the expectation of the public. This has anecdotally affected Trump's approval rating with a causation of a weaker U.S. dollar.



Source: Bloomberg, PSR

# Net saving rate, a leading indicator of U.S. dollar

- The combined saving of household, business and government is a reliable leading indicator in determining U.S. dollar.
- As the percentage of Net saving rate/Nominal GDP falls, so will the U.S. dollar with a 1 year lag.



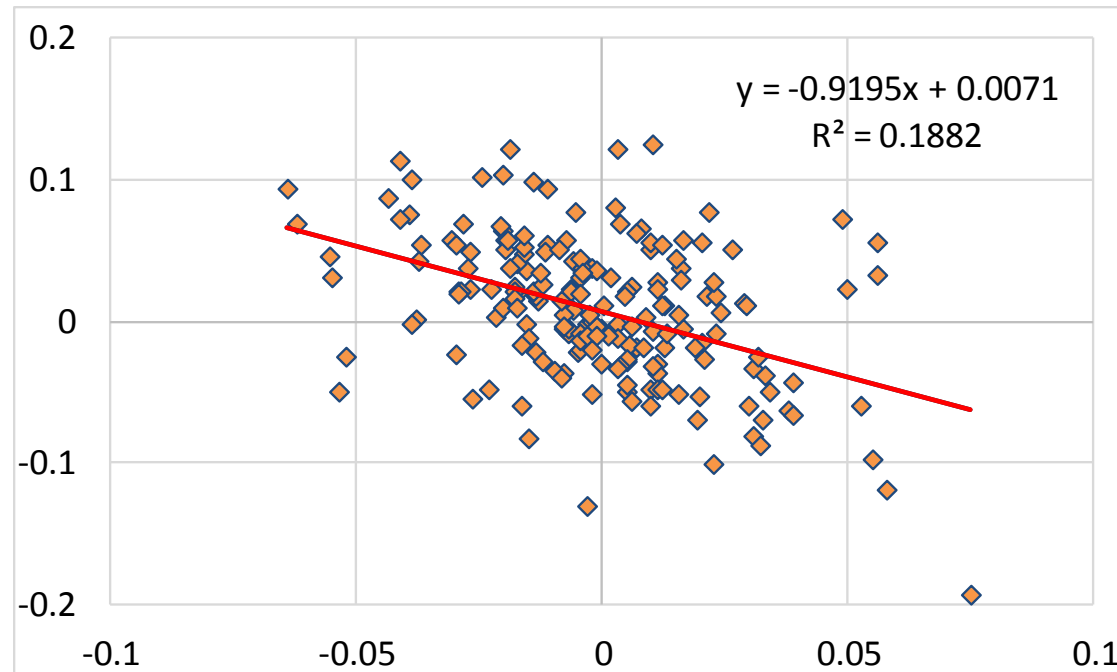
# Going for Gold again!

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- Gold went through a roller-coaster ride in 2016. Gaining ~30% in the first half of 2016, reaching US\$1375/oz before losing ~19% in the second half of 2016.
- After two failed attempt to break through the US\$1300/oz in 2017, gold price has once again broken out of the \$1300 psychological resistance level.
- This begged the question of whether it is, once again, time to take a look at the precious metal which many investors had a love/hate relationship.
- In retrospect, our technical analysis has always been bullish for gold,
- Our fundamental analysis of a higher gold price has not changed therefore we believe the primary factor that has affected gold price in recent price drop was by and large the change in sentiment.

# Gold is negatively correlated to USD

- The first and most observe reason for our belief in a stronger gold price relates back to our earlier argument on a weakening U.S. dollar.
- Recent history has shown that a weakening U.S. Dollar is favourable for the price of gold.

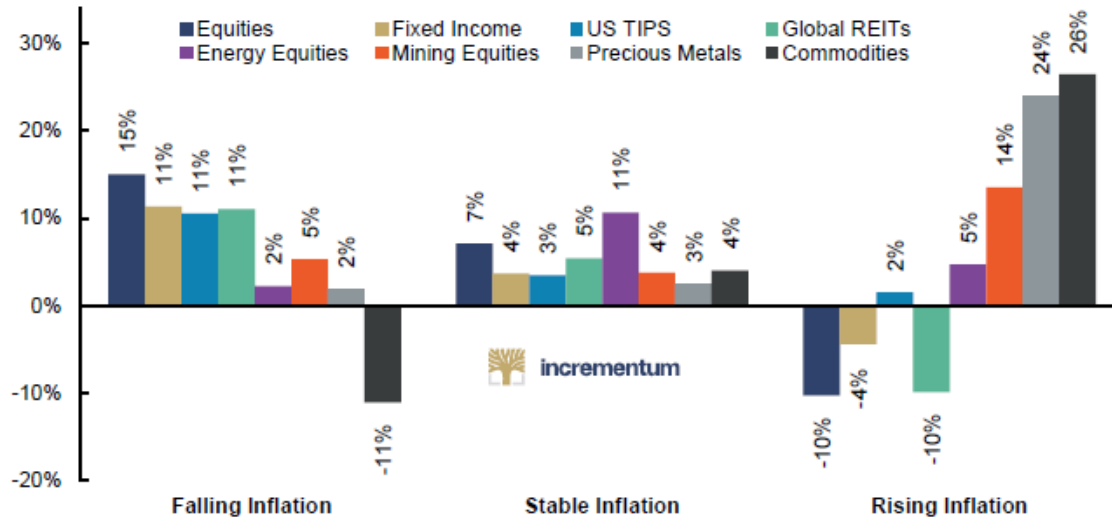


Monthly correlation since January 2002 till August 2017  
Source: Bloomberg, PSR

# Gold is a good inflationary hedged

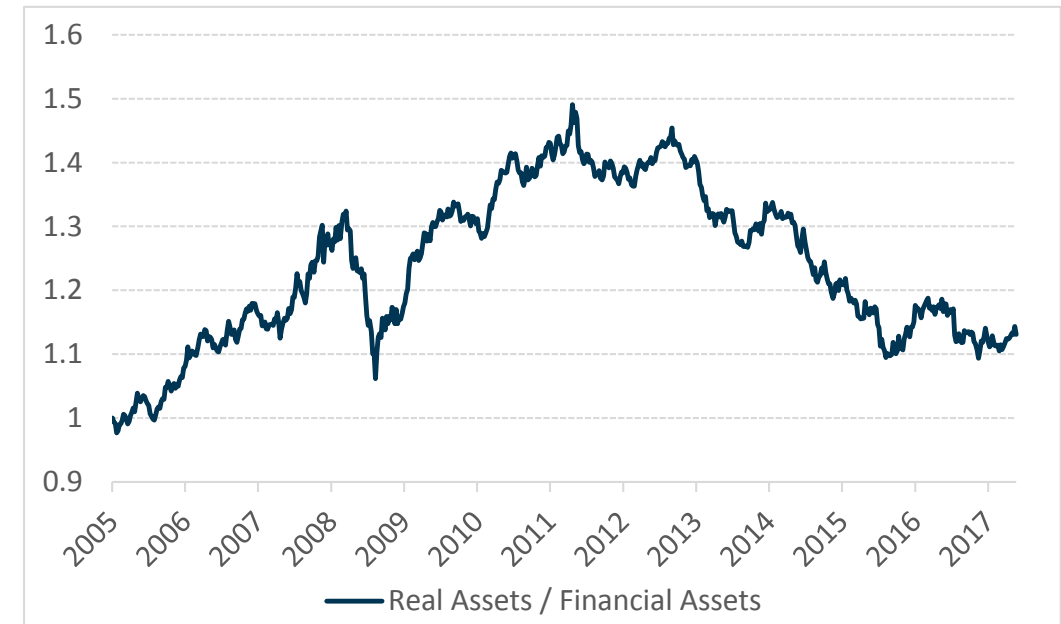
- As U.S. dollar is the reserve currency of the world, a weakening dollar will tend to have an inflationary effect on global trades
- During rising inflation periods, gold will be a good inflationary hedge
- In addition, real assets such as gold have never been this under-owned as compared to financial assets.

## Precious Metals such as gold is always a good hedge against inflation



Source: Wellington Asset Management, Incrementum AG

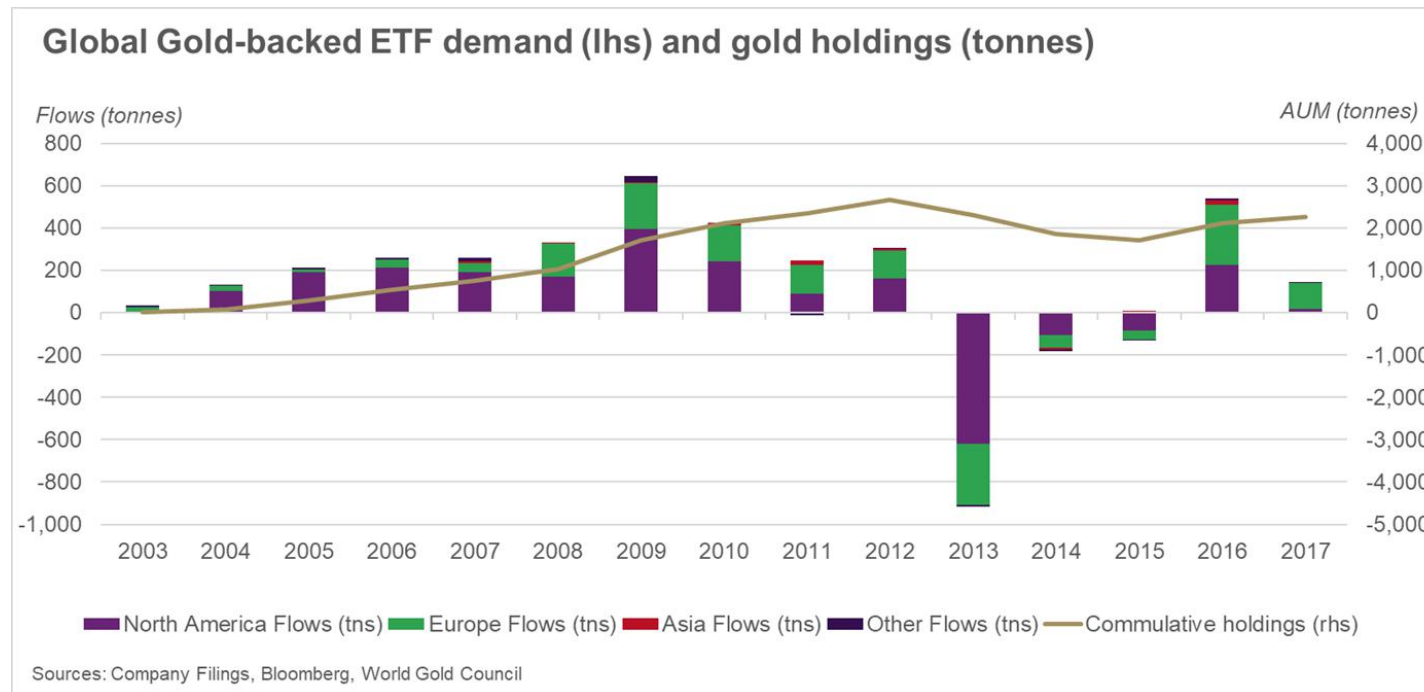
## Real Assets vs Financial Assets





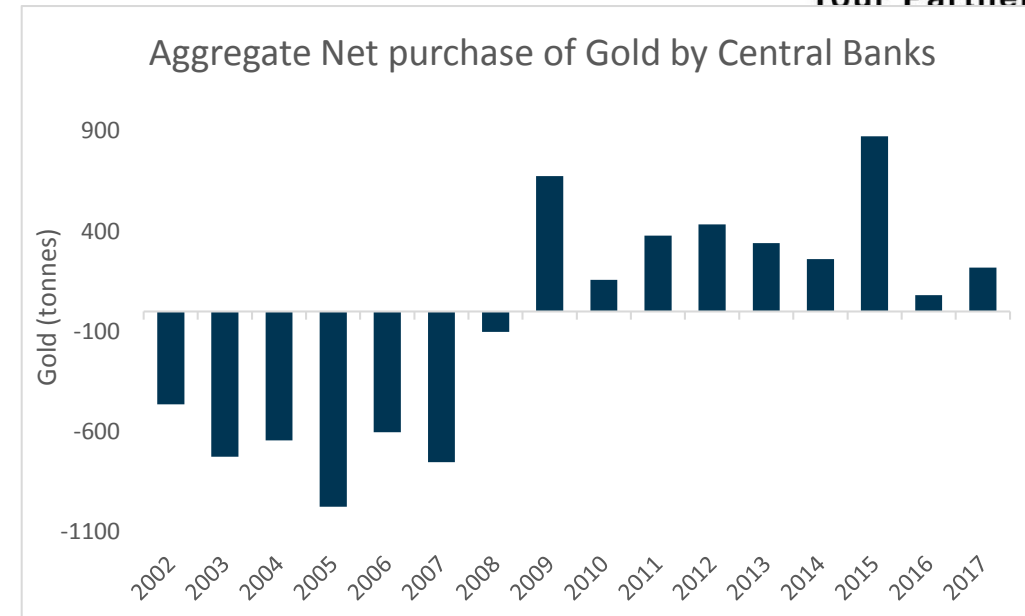
# Positive net inflow for Gold-backed ETFs

- Gold resonates much emotion amongst many investors. The changes sentiment influence the price of gold in the short run.
- We note the change in sentiment by observing the changes in funds flowing into Gold-Backed ETFs
- 2016 recorded the first positive net inflow after 3 consecutive years of outflow.
- 2017 is on track to be another positive net inflow for Gold-backed ETFs



# Central Banks are Buying

- Another group of buyers of gold are the Central Bank
- Central bank are accumulating Gold amid questions over stability of current monetary systems. Especially after GFC.
- The accumulation of gold is even more evident in the emerging economies.



## Annual net purchase of gold by emerging economies (rank by largest buyer in recent years)

Country	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
China	99.2	0.0	0.0	0.0	0.0	0.0	0.0	454.1	0.0	0.0	0.0	0.0	0.0	708.2	80.2	0.0
Russia	-35.3	2.5	-3.2	-0.1	14.6	48.9	69.2	129.5	139.6	94.3	74.8	77.4	173.0	206.4	200.7	114.2
Turkey	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	79.2	164.3	160.1	9.4	-13.6	-138.5	105.9
Kazakhstan	-4.1	1.0	3.0	2.7	7.6	2.2	2.4	-1.5	-3.1	14.7	33.3	28.4	48.1	30.0	36.2	22.9
India	0.0	0.0	0.0	0.0	0.0	0.0	0.0	200.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Mexico	-0.2	-1.7	-1.0	-1.0	-0.5	0.8	2.5	2.4	-1.5	98.9	18.5	-1.4	-0.4	-1.3	-1.0	-0.3
Korea	0.1	0.1	0.2	0.1	-1.2	1.3	0.0	0.1	0.0	40.0	30.0	20.0	0.0	0.0	0.0	0.0
Iraq	0.0	0.0	-123.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	23.9	12.4	47.6	0.0	0.0	0.0
Thailand	0.6	3.1	3.1	0.0	0.0	0.0	0.0	0.0	15.6	52.9	0.0	0.0	0.0	0.0	0.0	0.0
Philippines	23.3	-15.9	-34.2	-66.9	-10.8	-12.1	22.3	1.2	-1.0	5.0	33.6	0.8	1.8	0.6	0.4	0.0
Brazil	-0.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	33.6	0.0	0.0	0.0	0.1	0.0

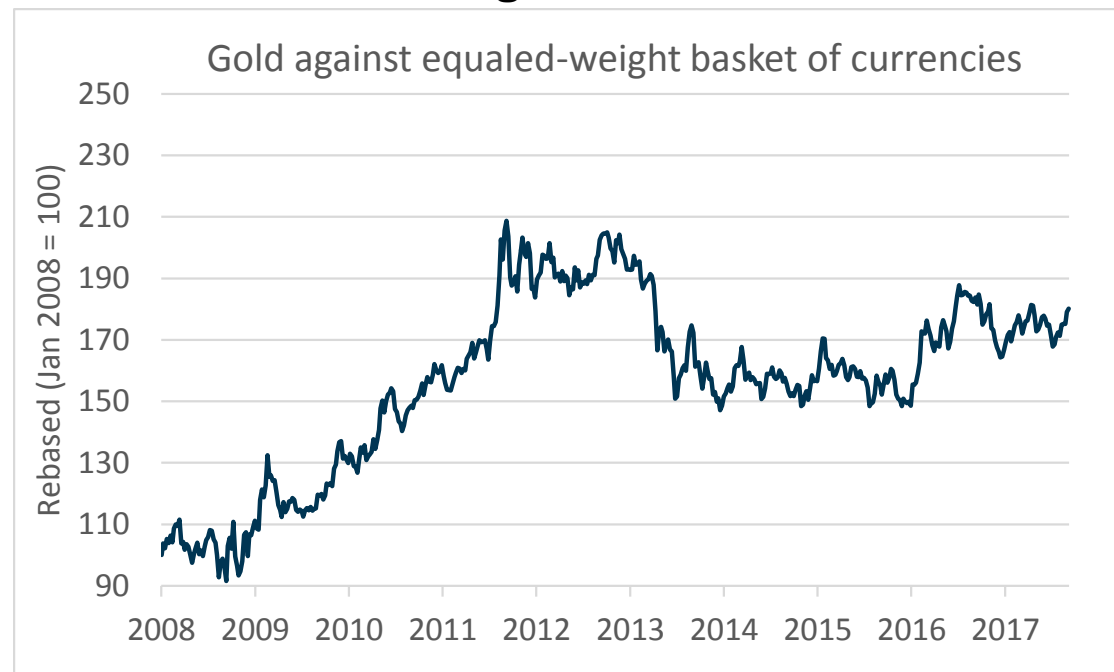
Source: World Gold Council, PSR



# Gold is up against most currencies

- Gold is not just performing well against the U.S. dollar; it has also appreciated against a basket of global currencies.
- This highlight that the strength of gold is not just reflecting the weakness of U.S. dollar.

## Gold near all-time high



Source: Bloomberg. PSR

- basket includes Euro, Sterling, Yen, Swiss Franc, Aussie Dollar, Canadian Dollar, Chinese Yuan, Russia Ruble and India Rupee.

# Conclusion

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- **U.S. dollar will continue its structural downtrend**
  - High level of public & private debt coupled with low saving rates and rising interest rates will keep downward pressure on the U.S. dollar.
  - The confidence in the dollar has also been greatly shaken by the erratic behaviour of President Trump and his inability in pushing through campaign promises.
- **Gold will reach its 2011 high of US\$1920/oz**
  - Negatively correlated to USD makes it a good Inflation hedge
  - Positive sentiment suggested by the net inflow into gold-backed ETFs
  - Central Bank buying
  - Gold is up against major traded currencies

<b>Recommended ETFs:</b>	PowerShares DB US Dollar Index Bear – (AMEX:UDN) SPDR GLD US\$ – (SGX:O87) SPDR Gold Trust – (AMEX:GLD)
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