

DBS (DBS SP)

Financial Services - Banks

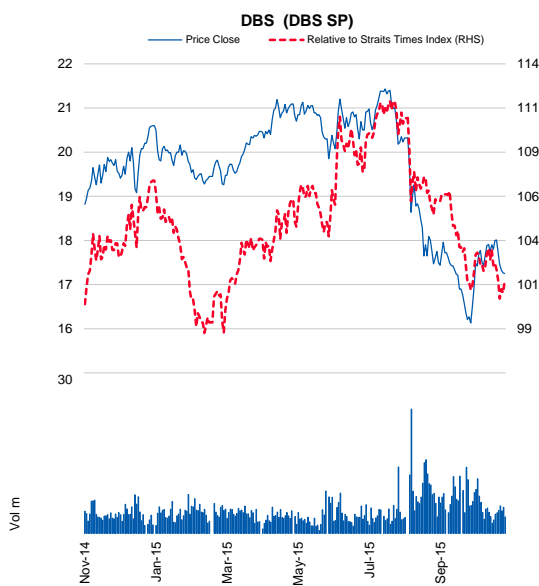
Market Cap: USD30,770m

Buy (Maintained)

 Target Price: **SGD21.10**

 Price: **SGD17.30**

Asset Quality Holding Up Well

 Macro
 Risks
 Growth
 Value


Source: Bloomberg

Avg Turnover (SGD/USD)	115m/81.5m
Cons. Upside (%)	22.5
Upside (%)	22.0
52-wk Price low/high (SGD)	16.1 - 21.4
Free float (%)	70
Share outstanding (m)	2,502
Shareholders (%)	
Temasek	30.0

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(16.3)	6.9	(14.5)	(18.2)	(6.7)
Relative	(4.7)	0.4	(7.4)	(3.5)	2.5

3Q15 earnings came in slightly ahead of expectations. Maintain BUY and SGD21.10 TP (22% upside), which implies 1.3x FY16F P/BV. Underlying operations were healthy while asset quality was stable. Management expects better earnings in 2016, underpinned by 7-8% topline growth and moderate rise in credit costs. Exposure to China and commodities are likely to remain resilient.

- ◆ **Slight beat.** DBS posted 3Q15 earnings of SGD1,066m (-5% QoQ, +6% YoY) while 9M15's SGD3,316m core net profit (+10% YoY) was 78%/77% of our/consensus' 2015F earnings of SGD4,266m/SGD4,311m respectively. The sequential decline in 3Q15 earnings was mainly on higher general provisions and a SGD50m charge from first-time adoption of a funding valuation adjustment for derivatives. Underlying operations were healthy while asset quality was stable.
- ◆ **Key positives for 3Q15 are a healthy net interest income growth of 4% with net interest margin (NIM) up 3bps QoQ and gross non-performing loan (NPL) down 1% QoQ to SGD2,471m.** Key negatives include: i) loans dipping 1% QoQ in constant currency terms mainly on the 10% decline in trade loans; ii) net fee income falling 11% QoQ as volatility in the financial markets led to lower income from wealth management, investment banking and stockbroking; and iii) fully-loaded Common Equity Tier 1 (CET1) ratio falling to 11.9% (June: 12.3%) on a currency translation effect on risk weighted assets and payment of interim dividends.
- ◆ **Comfortable with asset quality.** With no significant stress seen across its loans portfolio, management expects moderate non-performing loans (NPLs) and credit costs in 2016. Based on the internal stress tests of the bank's oil & gas exposure, management estimates that additional provisions would be <SGD100m. DBS is confident that its loan books would remain resilient given the good quality of its commodities exposure.
- ◆ **Maintain BUY.** Management is optimistic that DBS' topline can grow by 7-8% in 2016 on 5% loan growth, stable NIM and low-teens rise in non-interest income (non-II). With moderate increases in credit costs and operating expenses, this should filter down to bottomline growth. We make no change to our earnings forecasts and GGM-based SGD21.10 TP, which implies 1.3x FY16F P/BV. DBS remains our preferred pick among Singapore banks.

Forecasts and Valuations	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Reported net profit (SGDm)	3,672	4,046	4,419	4,638	5,089
Net profit growth (%)	(3.6)	10.2	9.2	5.0	9.7
Recurring net profit (SGDm)	3,501	3,848	4,280	4,638	5,089
Recurring EPS (SGD)	1.43	1.56	1.72	1.85	2.03
BVPS (SGD)	14.0	15.2	15.8	17.0	18.4
DPS (SGD)	0.58	0.58	0.62	0.62	0.64
Recurring P/E (x)	12.0	11.0	10.0	9.3	8.5
P/B (x)	1.23	1.13	1.09	1.01	0.94
Dividend Yield (%)	3.4	3.4	3.6	3.6	3.7
Return on average equity (%)	11.1	11.2	11.4	11.2	11.4
Return on average assets (%)	1.0	1.0	1.0	1.0	1.0
Our vs consensus EPS (adjusted) (%)			(1.2)	(0.8)	(2.9)

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Results At a Glance

Figure 1: DBS' 3Q15 and 9M15 results summary

FYE Dec (SGDm)	3Q14	2Q15	3Q15	QoQ (%)	YoY (%)	9M14	9M15	YoY (%)	Comments 9M15 vs 9M14
Net interest income	1,602	1,743	1,813	4	13	4,647	5,246	13	
Net interest margin	1.68%	1.75%	1.78%	3bps	10bps	1.67%	1.74%	7bps	Up 3bps QoQ on upward repricing of SGD loans and lower deposit costs in Singapore and Hong Kong.
Non-interest income (non-II)	912	947	899	(5)	(1)	2,829	3,028	7	Net fee income up 6% YoY to SGD1,659m led by wealth management (+21%), loan-related fees (+16%) and cards (+18%). Net trading and investment income rose 12% YoY to SGD1,100m.
Non-II/Total income	36.3%	35.2%	33.1%			37.8%	36.6%		
Operating income	2,514	2,690	2,712	1	8	7,476	8,274	11	
Overhead expenses	(1,109)	(1,218)	(1,259)	3	14	(3,204)	(3,658)	14	Up on to higher staff (+19% YoY) and revenue-related (+20% YoY) expenses.
Cost-Income Ratio	44.1%	45.3%	46.4%			42.9%	44.2%		
Pre-impairment profit	1,405	1,472	1,453	(1)	3	4,272	4,616	8	
Impairment charges	(177)	(137)	(178)	30	1	(456)	(496)	9	Specific allowances for loans rose 29% YoY to SGD425m, but cushioned by lower general allowances (-49%) due to slower loan growth.
Credit cost - annualised (bps)	27	19	25			24	23		
Operating profit	1,228	1,335	1,275	(4)	4	3,816	4,120	8	
Associates	6	10	(3)			70	11		
Pretax profit	1,234	1,345	1,272	(5)	3	3,886	4,131	6	
Tax	(193)	(197)	(179)			(572)	(591)		
Effective tax rate	15.6%	14.6%	14.1%			14.7%	14.3%		
Minority interest	(33)	(31)	(27)			(106)	(88)		
Net profit	1,008	1,117	1,066	(5)	6	3,208	3,452	8	
EI/Others	-	-	-			(198)	(136)		9M15: Relates to gain from disposal of property investment in Hong Kong. 9M14: Mainly gains from the sale of a stake in Bank of the Philippines Islands (BPI PM, NR).
Core profit	1,008	1,117	1,066	(5)	6	3,010	3,316	10	
Other key data and ratios									
Gross loans	265,204	283,723	288,749	2	9	265,204	288,749	9	Loans in constant-currency terms fell 1% QoQ as 1% rise in non-trade loans was offset by a 10% drop in trade loans.
Customer deposits	304,982	305,913	318,005	4	4	304,982	318,005	4	
Gross impaired loans	2,425	2,485	2,471	(1)	2	2,425	2,471	2	Higher NPLs in Hong Kong (+8% QoQ), and South and South-East Asia (+12%) offset by lower NPLs in Greater China (-10%) and rest of the world (-18%).
Total assets	424,383	440,257	456,361	4	8	424,383	456,361	8	
Shareholders' funds	36,750	39,168	39,404	1	7	36,750	39,404	7	
ROAA (%)	0.96	1.00	0.95			1.01	1.01		
ROAE (%)	11.1	11.4	10.9			11.8	11.8		
LDR (%)	85.8	91.6	89.7			85.8	89.7		
Gross impaired loans ratio (%)	0.91	0.88	0.86			0.91	0.86		
Loan loss reserves (%)	145.3	147.0	145.4			145.3	145.4		
CET-1 ratio (%)	13.4	13.4	12.9			13.4	12.9		
Total capital ratio (%)	15.6	15.3	14.8			15.6	14.8		

Source: Company data, RHB

Key Highlights From Management Briefing

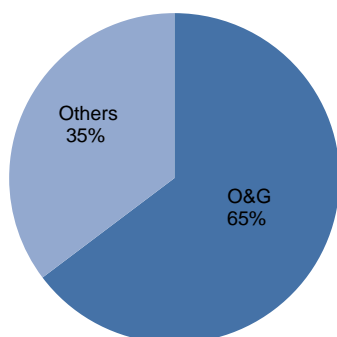
Asset quality solid

Exposure to broad commodity sector. DBS' loans and off balance sheet exposures to commodities-link companies stand at SGD34bn, of which oil & gas exposure amounted to SGD22m, or c.65% of the total. Other non-oil & gas commodities exposure include plantations and the coal industry.

Within the oil & gas segment, exposure to support services was SGD9bn, producers at SGD7bn, processors (smelters, refiners and storage/terminals) at SGD5bn and traders at SGD2bn.

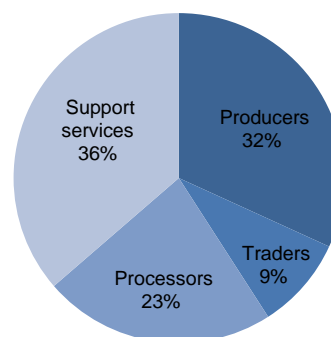
Comfortable with oil & gas exposure. From management's stress test of DBS' oil & gas exposure – assuming Brent crude oil is at USD40 per barrel (bbl) and West Texas Intermediate (WTI) crude oil at USD35 per bbl – only 5% of the portfolio would be at risk. Additional credit cost is estimated at no more than SGD100m, which would add c.3-4bps to our forecast loan credit cost of 26bps for 2016.

Figure 2: DBS' exposure to broad commodity sector (September)



Source: Company data, RHB

Figure 3: DBS' oil & gas exposure (September)



Source: Company data, RHB

Exposure to China. As at end-September, DBS' exposure to China was SGD43bn, comprising SGD26bn in trade loans (60.5% of total). Meanwhile, non-trade loans to entities with China parentage amounted to SGD10bn while those with foreign parentage stood at SGD7bn.

Its China exposure has declined by 14% when compared against the SGD50bn in Jun 2014, with the SGD10bn fall (-28%) in trade loans being the key factor that led to the lower exposure.

Management remains very comfortable with its exposure to China, given the low risk nature of trade loans. Meanwhile, the state-owned companies accounted for 50% of exposure to Chinese-owned entities.

Revenue outlook for 2016

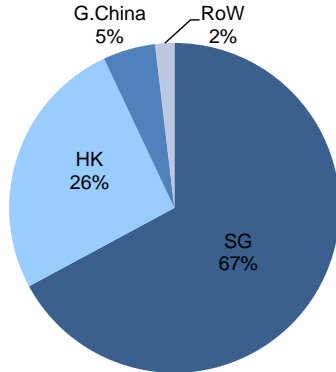
Expects topline growth of 7-8%. Management believes DBS can achieve revenue growth of 7-8% in 2016. This would come from: i) loan growth of 5% YoY (constant currency terms) underpinned by demand for mortgages and corporate loans, ii) relatively stable NIMs, and iii) low-teens non-Il growth led by the bank's wealth management and treasury businesses.

Loan demand. DBS is seeing good demand for mortgages in Singapore, with new bookings for 9M15 at 2x a year ago. Financing activities for corporates are healthy and the bank has seen a pick-up in demand from the building and construction sector. Management expects non-trade loans to grow by 6% YoY in 2016, with decline in trade loans moderating total loan growth to 5%.

NIM expected to be stable. Management does not expect a significant rise in US rates in 2016. To sustain NIM, management would continue to focus on managing the bank's funding cost. Margins pressure would come from China given expectations of further rate cuts in 2016.

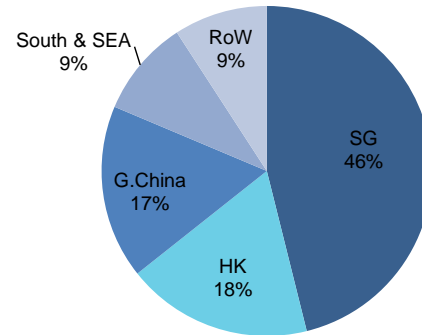
Future funding valuation adjustment (FVA) charges are not likely to be substantial. DBS is the first Asian bank to incorporate FVA to the fair value of over-the-counter derivatives. Management guides that there would not be substantial FVA charges in future quarters.

Figure 4: DBS' pre-tax profit by geography (9M15)



Source: Company data, RHB

Figure 5: DBS' loans by geography (September)



Source: Company data, RHB

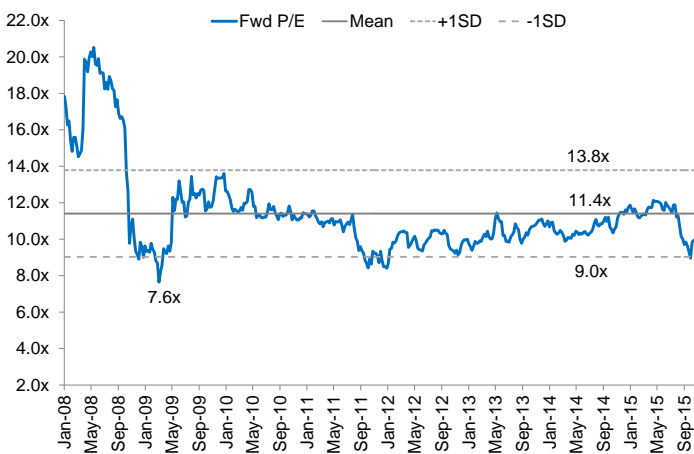
Valuation

Our GGM-derived SGD21.10 TP is based on 3-year forward ROE of 11.4%, cost of equity to 9.75% and long-term growth of 3.5%. Our revised TP implies FY16F P/BV of 1.26x (historical mean: 1.15x, -1SD: 0.97x) and P/E of 11.1x (historical mean: 11.4x).

Risks

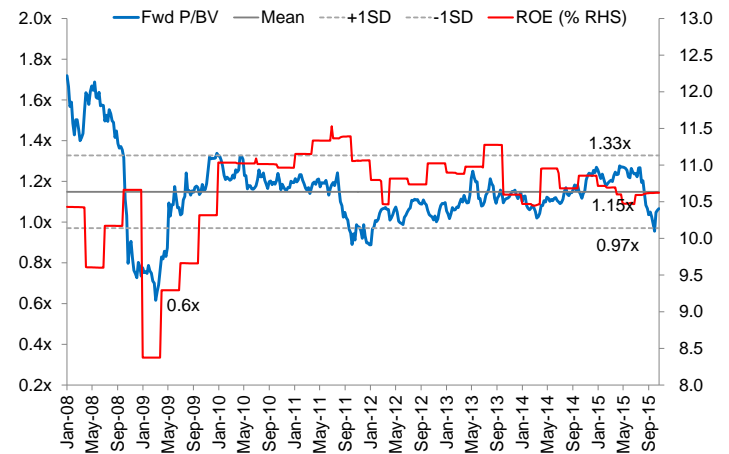
Key factors that would impede DBS' share price from reaching our target are: i) a sharper-than-expected slowdown in China and other major economies, ii) further delays in the US rate lift-off, and iii) a larger-than-expected increase in NPLs.

Figure 6: DBS' 12-month forward consensus P/E/s



Source: Bloomberg, RHB

Figure 7: DBS' 12-month forward consensus P/BVs



Source: Bloomberg, RHB

Financial Exhibits

Profit & Loss (SGDm)	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Interest income	7,986	8,948	9,611	10,152	10,640
Interest expense	(2,417)	(2,627)	(2,663)	(2,760)	(2,850)
Net interest income	5,569	6,321	6,948	7,392	7,790
Non interest income	3,358	3,297	3,688	4,032	4,388
- Fee income	1,885	2,027	2,350	2,580	2,780
Total operating income	8,927	9,618	10,636	11,424	12,178
Overheads	(3,918)	(4,330)	(4,810)	(5,100)	(5,360)
- Staff costs	(2,065)	(2,294)	(2,680)	(2,820)	(2,960)
Pre-provision operating profit	5,009	5,288	5,826	6,324	6,818
Loan impairment allowances	(756)	(638)	(660)	(760)	(720)
Other impairment allowances	(14)	(29)	(25)	(30)	(27)
Income from associates	79	79	35	40	44
Other exceptional items	171	198	139	-	-
Pre-tax profit	4,489	4,898	5,315	5,574	6,115
Taxation	(615)	(713)	(771)	(803)	(881)
Minority interests	(202)	(139)	(125)	(133)	(145)
Reported net profit	3,672	4,046	4,419	4,638	5,089
Recurring net profit	3,501	3,848	4,280	4,638	5,089

Source: Company data, RHB

	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Per Share Data					
EPS (SGD)	1.50	1.65	1.77	1.85	2.03
Recurring EPS (SGD)	1.43	1.56	1.72	1.85	2.03
DPS (SGD)	0.58	0.58	0.62	0.62	0.64
BVPS (SGD)	14.00	15.24	15.82	17.05	18.44
Growth Rates					
EPS growth (%)	(5.6)	9.3	7.8	4.2	9.7
Recurrent EPS growth (%)	2	9	10	8	10
DPS growth (%)	4	0	7	-	3
BVPS growth (%)	7.5	8.9	3.8	7.8	8.1
Gross cust loan growth (%)	17.9	10.7	3.8	5.0	5.5
Total asset growth (%)	13.9	9.6	3.5	3.9	5.1
Cust deposit growth (%)	15.3	8.5	0.9	5.5	6.0
Net interest income growth (%)	5.4	13.5	9.9	6.4	5.4
Non interest income growth (%)	20.8	(1.8)	11.9	9.3	8.8
Overhead growth (%)	8.4	10.5	11.1	6.0	5.1
Operating profit growth (%)	12.6	5.6	10.2	8.5	7.8
Loan impairment allowance growth (%)	84.8	(15.6)	3.4	15.2	(5.3)
Net profit growth (%)	(3.6)	10.2	9.2	5.0	9.7
Profitability					
Return on IEAs (%)	2.5	2.5	2.6	2.6	2.6
Cost of funds (%)	0.8	0.7	0.7	0.7	0.7
Net interest spread (%)	1.7	1.8	1.8	1.9	1.9
Net interest margin (%)	1.8	1.8	1.8	1.9	1.9
Non-interest income / total income (%)	37.6	34.3	34.7	35.3	36.0
Cost to income ratio (%)	43.9	45.0	45.2	44.6	44.0
Credit cost (bps)	32	24	23	26	23
Return on average assets (%)	1.0	1.0	1.0	1.0	1.0
Return on average equity (%)	11.1	11.2	11.4	11.2	11.4

Source: Company data, RHB

Financial Exhibits

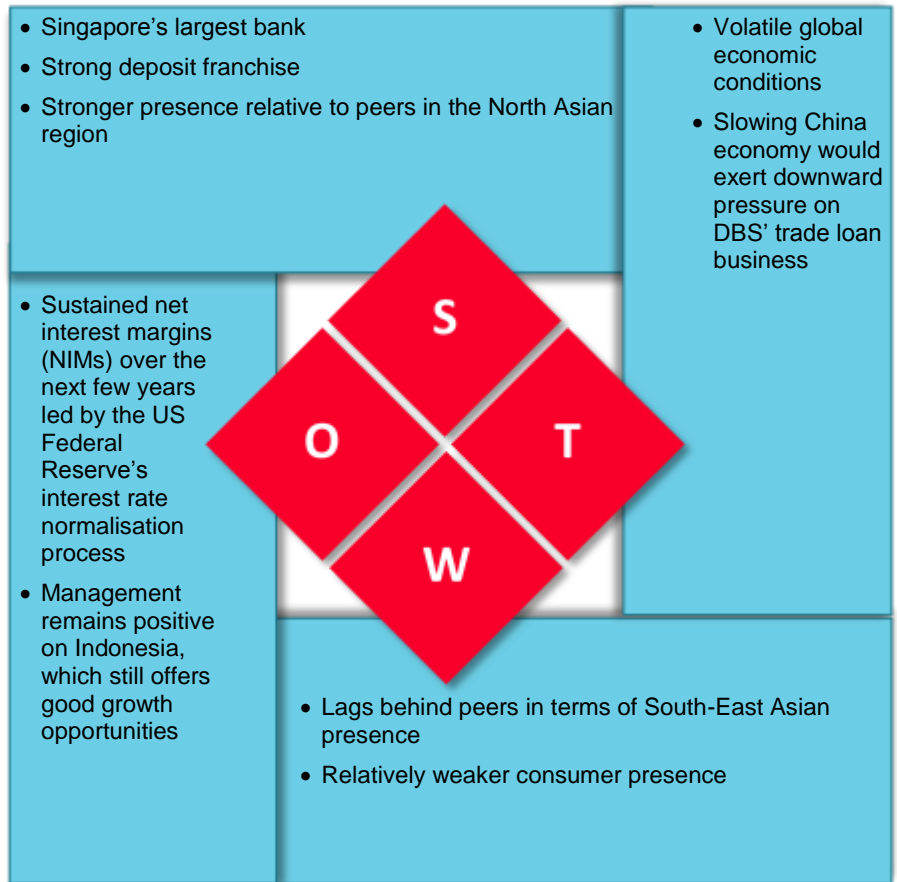
Balance Sheet (SGDm)	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Total gross loans	252,181	279,154	289,800	304,300	321,100
Other interest earning assets	86,040	91,474	92,900	93,300	97,100
Total gross IEAs	338,221	370,628	382,700	397,600	418,200
Total provisions	(3,527)	(3,566)	(3,910)	(4,220)	(4,470)
Net loans to customers	248,654	275,588	285,890	300,080	316,630
Total net IEAs	334,694	367,062	378,790	393,380	413,730
Tangible fixed assets	1,449	1,485	1,510	1,560	1,640
Intangible assets	4,802	5,117	5,117	5,117	5,117
Total non-IEAs	67,314	73,604	77,417	80,567	84,152
Total assets	402,008	440,666	456,207	473,947	497,882
Customer deposits	292,365	317,173	320,000	337,700	358,100
Other interest-bearing liabilities	42,231	52,804	58,900	60,500	61,800
Total IBLs	334,596	369,977	378,900	398,200	419,900
Total non-IBLs	29,726	30,483	35,105	30,445	29,180
Total liabilities	364,322	400,460	414,005	428,645	449,080
Share capital	2,441	2,441	2,441	2,441	2,441
Other reserves	31,792	35,267	37,264	40,363	43,863
Shareholders' equity	34,233	37,708	39,704	42,804	46,304
Minority interests	3,453	2,498	2,498	2,498	2,498

Source: Company data, RHB

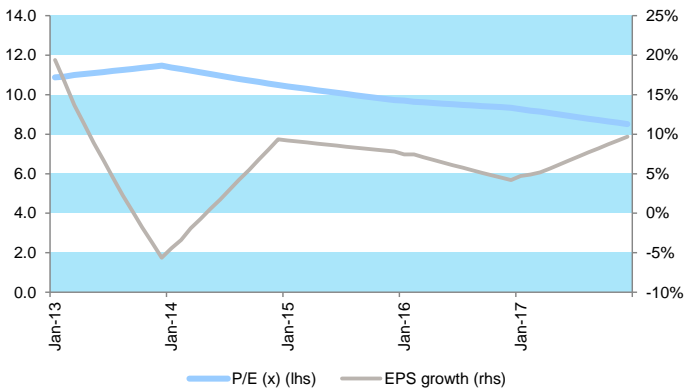
	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Balance Sheet Structure					
Net cust loans/cust deposits (%)	85.0	86.9	89.3	88.9	88.4
CASA deposits / customer deposits (%)	55.1	56.9	60.0	59.0	58.0
Total assets / shareholders' funds (x)	11.7	11.7	11.5	11.1	10.8
Asset Quality and Capital					
Reported NPLs / gross cust loans (%)	1.1	0.9	0.9	0.9	0.9
Net impaired loans / loans (%)	(0.3)	(0.4)	(0.4)	(0.5)	(0.5)
Collective allowance / net loans (%)	1.0	0.9	1.0	1.0	1.0
Total provisions / reported NPLs (%)	122.4	147.4	147.5	148.1	148.0
CET-1 ratio (%)	13.7	13.1	13.9	14.2	14.8
Tier-1 ratio (%)	13.7	13.1	13.9	14.2	14.8
Total capital ratio (%)	16.3	15.3	14.8	15.7	16.9
Du-Pont (as % of avg assets)					
Net interest income (%)	1.5	1.5	1.5	1.6	1.6
Non-interest income (%)	0.9	0.8	0.8	0.9	0.9
Operating expenses (%)	1.0	1.0	1.1	1.1	1.1
Pre-provision ROAA (%)	1.3	1.3	1.3	1.4	1.4
Loan & other impairment allowance (%)	0.2	0.2	0.2	0.2	0.2
Associates (%)	0.0	0.0	0.0	0.0	0.0
Exceptionals (%)	0.0	0.0	0.0	0.0	0.0
Pre tax ROAA (%)	1.2	1.2	1.2	1.2	1.3
Return on average assets (%)	1.0	1.0	1.0	1.0	1.0
Leverage (x)	11.4	11.7	11.6	11.3	10.9
Return on average equity (%)	11.1	11.2	11.4	11.2	11.4

Source: Company data, RHB

SWOT Analysis

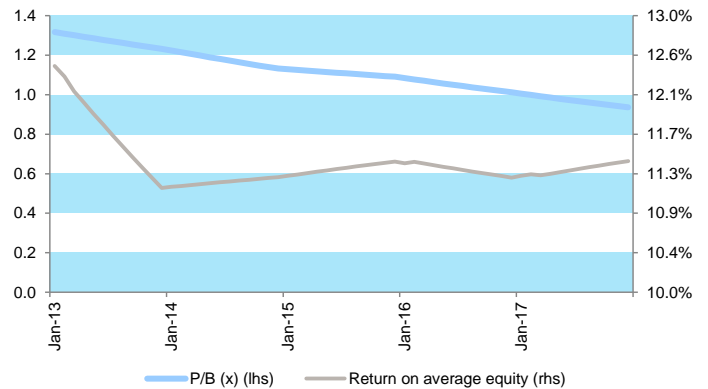


P/E (x) vs EPS growth



Source: Company data, RHB

P/BV (x) vs ROAE



Source: Company data, RHB

Company Profile

DBS is the largest Singapore bank by assets. It also has significant operations in Hong Kong and China.

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2015-10-15	Buy	21.1	17.7
2015-07-28	Buy	23.3	21.0
2015-04-28	Buy	23.3	21.0
2015-02-10	Buy	22.3	19.5
2014-12-30	Buy	22.6	20.6
2014-11-03	Buy	21.0	18.8
2014-08-03	Buy	21.0	18.3
2014-05-02	Buy	19.2	17.2
2014-02-17	Buy	19.2	16.6
2013-11-04	Buy	19.4	16.8

Source: RHB, Bloomberg

RHB Guide to Investment Ratings

Buy: Share price may exceed 10% over the next 12 months

Trading Buy: Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

Neutral: Share price may fall within the range of +/- 10% over the next 12 months

Take Profit: Target price has been attained. Look to accumulate at lower levels

Sell: Share price may fall by more than 10% over the next 12 months

Not Rated: Stock is not within regular research coverage

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