OCBC Bank

Asia Credit Research

Earnings Review: Standard Chartered PLC ("StanChart")

Issuer Profile: Neutral (4)

Ticker: **STANLN**

Background

Formed almost 50 years ago, Standard Chartered PLC ('StanChart') is a universal bank, offering broad services aligned both globally and regionally. Although headquartered in the UK, StanChart's footprint is skewed towards emerging markets, mostly in Greater China & North Asia (Hong Kong), followed by ASEAN & South Asia. As at 31 December 2017, it had total assets of USD663.5bn.

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Recommendation

- Trends in StanChart's 1Q2018 results were positive in our view considering both (1) income and underlying profit growth on a q/q and y/y basis; and (2) successful execution of its 2015 strategic plan.
- Its capital position has benefited as a result and remains above both the bank's target range and our estimate of its 2019 minimum Supervisory Review and Evaluation Process CET1 requirement. As such, we retain StanChart's Neutral (4) Issuer Profile.
- We see better value in the CMZB Tier 2 4.875% '27c22s as we think the pick up more than compensates for the extension in duration. We hold all four issuers below at Neutral (4) Issuer Profile.

Relative Value:

Bond	Maturity / Call date	CET1 Ratio	Ask Yield	Spread
STANLN 4.4 '26c21 (T2)	23/01/2021	13.9%	3.05%	83
CMZB 4.875 '27c22 (T2)	01/03/2022	14.1%	4.41%	207
BACR 3.75 '30c25 (T2)	23/05/2025	12.7%	4.45%	187
BPCEGP 4.45 '25c20 (T2)	17/12/2020	15.4%	3.44%	124

Indicative prices as at 9 May 2018 Source: Bloomberg
Common Equity Tier 1 (CET1) Ratio based on latest available quarter

Key Considerations

- **Decent trends in results:** StanChart's 1Q2018 interim management results appear constructive. Operating income of USD3.9bn was up 7% y/y (+5% y/y on a constant currency basis) driven by performance in transaction banking, mortgages, wealth management and deposits. Other segments including credit cards, personal loans and corporate finance performance were also positive although treasury income was lower y/y due to absence of one-off gains from 1Q2017. What is positive in segment performance from management's view is that the solid y/y growth trends are in line with StanChart's strategic plan implemented in late 2015 to reduce its risk appetite and loan book and invest in Private Banking and Retail Banking to expand opportunities.

- **Lower cost growth helped bottom line:** Operating expenses of USD2.2bn increased 5% y/y or 1% on a constant currency basis as prior year cost efficiency programs appear to be paying off as per management's statements. Regulatory costs were also lower y/y due to the implementation of several regulatory programs at the end of 2017. Supporting overall cost trends, impairment expenses were lower (-4% y/y and -29% q/q) with management indicating that this is the result of portfolio rebalancing and improved macro conditions in StanChart's main markets including Hong Kong, China and Singapore. The 29% q/q fall in impairment losses was larger due to the inclusion of a one-off provision in the prior quarter in Korean retail banking following a change in regulation.

- **Macro environment and strategy shows in segment performance:** Segment wise, operating income performance was supportive across all segments with Corporate & Institutional Banking ('CIB') and Commercial Banking up 7% y/y with CIB benefitting from a 20% increase in client operating account average balances. As mentioned above, revenues connected with Private Banking ('PB') and Retail Banking ('RB') grew the most with these segments improving 23% y/y and 14% y/y respectively with PB growth due to capacity expansion from senior relationship manager hiring and over USD700mn in net new money in 1Q2018. CIB continues to generate the bulk of segment income at 45% (same as 1Q2017) of total income for 1Q2018. This is followed by RB at 35% (up from 32% in 1Q2017). Geographic wise, income performance grew the most in Greater China & North Asia (+13% y/y) followed by ASEAN & South Asia (+7% y/y) while performance in Europe & Americas and Africa and Middle East were flat.

- **Capital Ratios benefitting from loan portfolio improvements**: StanChart's balance sheet continues to grow with net loans and advances up 3% q/q and 9% y/y. As growth was marginally ahead of customer account growth, the advance to deposit ratio rose y/y and q/q. At the same time, asset quality was slightly weaker q/q but improved y/y. Trends in loan quality will continue to be a focus in our view, particularly given the declining trend in credit impairment provisions with coverage ratios before and after collateral falling q/q. Management also continues to wind down its liquidation portfolio. As a result, risk weighted assets were stable q/q despite loan growth and combined with earnings for the quarter, StanChart's CET1 ratio improved 26bps q/q to 13.9%. This remains above the bank's target range of 12-13% and our estimate of its 2019 minimum Supervisory Review and Evaluation Process CET1 requirement of 10.0%. StanChart also disclosed in the release of its FY2017 results that it estimates its minimum requirement for own funds and eligible liabilities (MREL) position as at 31 December 2017 was ~25.5%, above the Bank of England's estimated MREL requirement of 16.0 per cent in 2019. As such, StanChart's capital position remains sound in our view.

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Explanation of Issuer Profile Rating / Issuer Profile Score

Positive ("Pos") – The issuer's credit profile is either strong on an absolute basis, or expected to improve to a strong position over the next six months.

Neutral ("N") – The issuer's credit profile is fair on an absolute basis, or expected to improve / deteriorate to a fair level over the next six months.

Negative ("Neg") – The issuer's credit profile is either weaker or highly geared on an absolute basis, or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7 point Issuer Profile Score scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

Explanation of Bond Recommendation

Overweight ("OW") – The performance of the issuer's specific bond is expected to outperform the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Neutral ("N") – The performance of the issuer's specific bond is expected to perform in line with the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Underweight ("UW") – The performance of the issuer's specific bond is expected to underperform the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Other

Suspension – We may suspend our issuer rating and bond level recommendation on specific issuers from time to time when OCBC is engaged in other business activities with the issuer. Examples of such activities include acting as a joint lead manager or book runner in a new issue or as an agent in a consent solicitation exercise. We will resume our coverage once these activities are completed.

Withdrawal ("WD") – We may withdraw our issuer rating and bond level recommendation on specific issuers from time to time when corporate actions are announced but the outcome of these actions are highly uncertain. We will resume our coverage once there is sufficient clarity in our view on the impact of the proposed action.

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