

TMB Bank (TMB.BK)

Alert: Sanguine Tone from Meeting with CEO

- Positive tone from management; yet, we think differently** – We met with TMB CEO and CFO for a half-year update. Management affirms its 14% ROE target in 2014 and 15% in 2015 (1H14 ROE 13.4%; core 11.2%), hinging on loan recovery in 2H, ability to tweak NIM, and fee-income recovery from down double digits to up double digits. Also, it sees scope to cut back credit cost if the economy improves. Mgmt also reiterates its core 'deposit-led' strategy and a new SME loan product building on the IFC guarantee structure as a tool. While we see room for 'core' operating improvement, we are not convinced of such a strong rebound barring a return to high-risk small SME lending, which TMB shrank in 1H14. Product coordination with IFC may change the risk-taking capacity if successful. Sell.
- Deposit-led strategy: will funding cost hitting low end?** – The CEO is upbeat on 34% QoQ for the SME operating account product (One Bank, One account) which waives transaction fees but pays a low interest rate (40bps). However, TMB did not disclose the contribution to total deposits. We note though that SME deposits have been between 15-16% of total deposits, and no uptrend. For disclosure by product, high yield CASA ('ME' and 'No Fixed' deposits) explained most of the deposit increase in 1H14 (34bn out of a 41bn increase). Without real improvement in low-cost CASA deposit balances (not the number of accounts), we view funding cost to have almost hit the low point at the current level of a 2.2% range.
- New IFC guarantee to support new products** – TMB has been actively using the government's Thai Credit Guarantee agency for SMEs (TCG) to structure high-leverage products for SME. For instance, TMB allows SMEs to borrow up to 3x of collateral. It then bought the guarantee from TCG up to 2x and took risk only up to collateral value. This allows 3x loan size vs collateral. TCG will charge a 175bps fee for the guarantee and take first loss **up to 20%** of total SME loans in the portfolio. **60% of small SME loans** made by TMB utilized the TCG structure. TMB is working with IFC (International Finance Corp) to take the **second tranche** of loss (i.e. from 20% to 50% loss on top of TCG initial loss absorption). TMB estimates that the 'net' fee charged to customers could be up c30bps but it allows TMB to extend longer-term loans to SMEs under a low collateral requirement, bundled with credit protection on top. TCG has balance sheet capacity to guarantee an additional Bt160bn SME loans for the industry.
- NIM: hitting limit around 3%** – Management expected room to tweak NIM in 2H14 (2Q14 2.8%) given strong deposit growth in 1H (+8% ytd); hence, it has the ability to cut costs and afford to lose some deposits. On lending, we see loan yields hovering around 6%, after adjusting for one-offs in the past few quarters. With small SME loan growth deceleration due to risk-off strategy, we expect NIM to be range-bound around 2.9-3% and no longer trend higher, unless TMB reverses the strategy and keeps growing small SME at 30-40% p.a., as it did in the past few years.

Sell	3
Price (16 Jul 14)	Bt2.62
Target price	Bt2.10
Expected share price return	-19.8%
Expected dividend yield	2.3%
Expected total return	-17.6%
Market Cap	Bt114,438M
	US\$3,560M

Price Performance (RIC: TMB.BK, BB: TMB TB)



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- **NPL sale and trend: More to come** – Management explained that NPL sales (Bt3.3bn) in 2Q14 was mostly legacy exposure (rice mill) at c60% loss rate. It appears that the current TMB book already provides ahead of actual loss, as witnessed in the writeback in 2Q14 credit cost. Management did not rule out further proactive NPL management (and possibly more writebacks when NPL sales take place).
- **Non-II and Cost Efficiency: Ambitious targets** – Management remained confident that Non-II should grow by double digits for 2014 and should post >20% growth in 2015 (vs -10% YoY in 1H14). Fee income recovered QoQ in 2Q14 driven by better fees from mutual funds and bancassurance, along with modest uptick in credit-related fees. Management viewed that bancassurance cross-sell rate on TMB clients remained low. As for cost to income (still >50% vs low 40% for top-end peers), TMB viewed that it required a ramp-up of revenue capacity rather than cost cutting. This will take time.
- **ROE strategy: May need some breakthrough** – Putting all together, we think that room to improve ROE from an 11% core level in 1H14 towards a 12% level could be achieved through economic recovery (Citi: 14E: 11.7%). However, to achieve a 14-15% level may require much stronger non-II strategy or renewed growth in small SMEs. This may prove to be tricky in execution.

TMB Bank

Valuation

Our Bt2.1 target price for TMB equates to a P/E of 10.9x 2015E (EPS of Bt0.193). Our TP is equiv to 1.26x 2015E BV (Bt1.66/share). Our target price is derived from: 1) DDM assuming 33% payout and 2015E sustainable ROAE after transition period of 13.6%, gives a fair-value of Bt2.1, or P/E of 10.9x 15E.

2) Our P/E cycle analysis tracks how the market values the banks in terms of P/E ascribed to 1-yr fwd consensus earnings. This suggests an average trough-peak P/E range of 5x-11.8x, with a mean of 8.4x. We use these two methodologies because we believe the market tends to price bank stocks based on an estimate of sustainable dividend cash flows and also near-term expected earnings outlook, which the DDM and our trough-peak P/E cycle analysis seek to measure.

Risks

Upside risks to our target price include: 1) M&A potential: With the MoF and ING holding a sizable stake in the company and seemingly willing to sell, TMB shares could react positively to a change in the ownership situation. 2) Successful balance sheet deployment in small SMEs, coupled with strong fee income cross selling, could boost earnings capacity above our estimates

Downside risks to our target price include: 1) TMB begin to grow in small SME and high yield retail, which is relatively higher risk 2) Revenue model on non-II which seems to depend on loan origination 3) Lackluster growth after political struggle could cause asset quality to deteriorate esp small SMEs and unsecure retail loans.

Appendix A-1

Analyst Certification

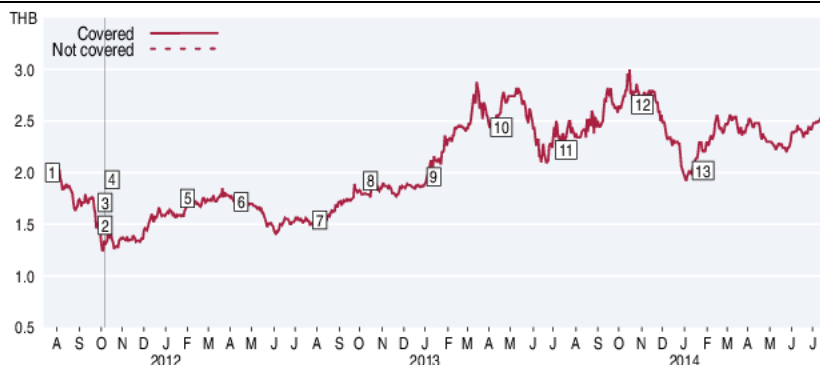
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TMB Bank (TMB.BK)

Ratings and Target Price History Fundamental Research

Analyst: Kritapas Siripassorn, CFA



	Date	Rating	Target Price	Closing Price
1	26-Jul-11	3L	*1.55	2.04
2	7-Oct-11	Stock rating system changed		
3	7-Oct-11	*1	1.55	1.30
4	18-Oct-11	*3	*1.20	1.35
5	1-Feb-12	3	*1.35	1.75

* Indicates change

	Date	Rating	Target Price	Closing Price
6	17-Apr-12	3	*1.40	1.66
7	6-Aug-12	3	*1.45	1.53
8	16-Oct-12	3	*1.50	1.76
9	13-Jan-13	3	*1.70	2.06
10	18-Apr-13	3	*2.00	2.68

	Date	Rating	Target Price	Closing Price
11	18-Jul-13	3	*2.10	2.34
12	4-Nov-13	3	*2.30	2.66
13	28-Jan-14	3	*2.10	2.20

Rating/target price changes above reflect Eastern Standard Time

TMB Bank (TMB.BK)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Kritapas Siripassorn, CFA



	Date	Rating	Target Price	Closing Price
1	11-Apr-14	*REM LP	-	2.48

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Data current as of 30 Jun 2014

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12 Month Rating			Relative Rating		
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49%	40%	12%	0%	100%	0%
55%	53%	46%	0%	54%	0%

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