

Malaysia Banks

Focus on the Wholesale-cum-Regional Banks

- **Focus stocks: Maybank, RHBC, CIMB** — In his report, “[Malaysia Long View: Growth Themes for the Long Term](#)”, our Asean economist Wei Zheng Kit critically assesses the sustainability of Malaysia’s growth model. This report reviews three key macro themes that could shape the banks’ business outlooks: [a] Sustainability of investment-led GDP growth; [b] Asean integration & regionalization; [c] Efforts to spread economic growth beyond the Klang Valley core. Malaysia’s three wholesale-IB/regional banks are the focus of the first 2 themes; but the third theme suggests that there still remains an investment case for pure domestic retail bank names. **Current stock preference ladder: Buy Maybank, RHBC; Sell CIMB. [Pg 3].**

- **Sustainability of investment-led GDP growth** — The ETP agenda from 2010 helped kick start a multi-year surge in investment spend. Now at close to 28% of GDP, sustainability may require prioritization toward higher-return projects, perhaps externally-oriented (incl. mfg.) segments. As these infra projects roll forward from planning to the execution stage, we have seen a bottoming (in mid-2013) and modest recovery of system business loan growth. Initially these are larger ticket corporate/commercial loans, to the benefit of the larger balance-sheet banks, but there should be a second-round impact down supply chains and SMEs. However, the impact on banks’ loan growth may end up being secondary to the funds raised in the capital markets, which has experienced a surge since 2009. **[Pg6].**

- **Asean integration/regionalization** — Prospects for Malaysia as an attractive FDI destination should improve on rising Asean integration, and equally greater regional integration may drive outward bound investment (ODI) into Asean. In part thanks to timely acquisitions enhancing wholesale/investment banking platforms, the larger banks’ IB capabilities have evolved beyond domestic Malaysia, enabling them to capture investment opportunities into the region. Equally, the larger banks, dominant in the domestic market, see the next level of growth as pursuing opportunities in Asean and beyond. This could be organic investment or selective M&A. **[Pg 12].**

- **Growth spread beyond the Klang Valley core?** — The Selangor-KL-Putrajaya corridor accounts for a quarter of Malaysia’s 29.6m population and 36% of GDP, and as importantly contributed more than half of economic growth during 2006-12. Spreading growth beyond the core has met with challenges, and near term we expect consumer loan growth to moderate. But fundamentally there remains clear support for consumer growth, especially mortgages, both cyclically (despite a likely property slowdown), and secularly driven by Malaysia’s favourable demographics and continued urbanization. This holds even if growth remains largely centered on the Klang Valley core, although NIM pressure eroding consumer banks’ top line loan growth remains a concern. **[Pg 22].**

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Investment Summary

Figure 1. Malaysia Banks Forecast Summary and Valuations

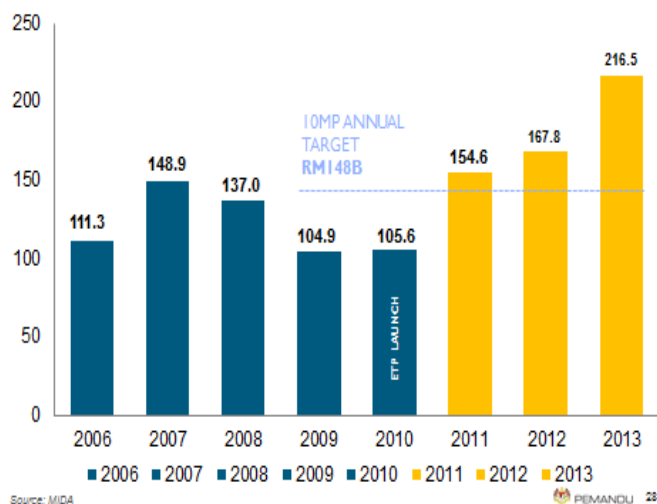
| Priced as of 29-Apr-14 | Price | Target Price | ETR | Mkt Cap | Net Profit* | | EPS | | EPS | | PER | | BPS | | PBV | | DPS | | Yield | | ROAE | |
|------------------------|-------|--------------|------|---------|-------------|-------|-------|------|----------|------|------|------|-------|-------|------|------|-------|------|-------|-----|------|------|
| Stock, Rating, BBG | LCY | LCY | (%) | US\$ b | (LCY m) | | (LCY) | | chg %YoY | | (x) | | (LCY) | | (x) | | (LCY) | | (%) | | (%) | |
| | | | | | 14E | 15E | 14E | 15E | 14E | 15E | 14E | 15E | 14E | 15E | 14E | 15E | 14E | 15E | 14E | 15E | 14E | 15E |
| MALAYSIA | | | | | | | | | | | | | | | | | | | | | | |
| Public, 1, PUBM.KL | 20.26 | 21.01 | 6.6 | 21.9 | 4,614 | 5,069 | 1.31 | 1.44 | 12.6 | 9.9 | 15.5 | 14.1 | 6.51 | 7.32 | 3.11 | 2.77 | 0.58 | 0.62 | 2.9 | 3.1 | 21.3 | 20.7 |
| Maybank, 1, MBBM.KL | 9.95 | 11.11 | 16.7 | 27.0 | 6,750 | 7,388 | 0.78 | 0.85 | 3.0 | 9.4 | 12.8 | 11.7 | 5.45 | 5.76 | 1.83 | 1.73 | 0.50 | 0.56 | 5.0 | 5.6 | 14.3 | 14.9 |
| CIMB Bank, 3, CIMB.KL | 7.51 | 6.75 | -6.5 | 19.2 | 4,871 | 5,413 | 0.59 | 0.66 | -1.3 | 11.1 | 12.7 | 11.4 | 4.61 | 4.95 | 1.63 | 1.52 | 0.27 | 0.29 | 3.6 | 3.9 | 14.3 | 13.8 |
| AMMB, 2, AMMB.KL | 7.18 | 7.58 | 9.3 | 6.6 | 2,004 | 2,219 | 0.67 | 0.74 | 9.9 | 10.7 | 10.8 | 9.8 | 4.72 | 5.16 | 1.52 | 1.39 | 0.27 | 0.30 | 3.8 | 4.2 | 14.7 | 14.9 |
| Hong Leong, 3, HLBB.KL | 13.98 | 13.76 | -1.9 | 8.0 | 2,127 | 2,282 | 1.21 | 1.30 | 6.7 | 7.2 | 11.5 | 10.8 | 9.10 | 10.05 | 1.54 | 1.39 | 0.49 | 0.50 | 3.5 | 3.6 | 14.0 | 13.6 |
| RHB Cap, 1, RHBC.KL | 8.43 | 8.87 | 8.3 | 6.6 | 2,023 | 2,240 | 0.79 | 0.88 | 8.9 | 10.7 | 10.6 | 9.6 | 7.19 | 7.80 | 1.17 | 1.08 | 0.26 | 0.28 | 3.1 | 3.3 | 11.5 | 11.7 |
| Alliance, 3, ALFG.KL | 4.50 | 4.78 | 10.7 | 2.1 | 614 | 685 | 0.40 | 0.45 | 9.2 | 11.5 | 11.2 | 10.0 | 3.01 | 3.25 | 1.50 | 1.39 | 0.20 | 0.22 | 4.5 | 5.0 | 13.7 | 14.1 |

Source: Citi Research estimates

Our Malaysia Long View report by Wei Zheng Kit and Brian Tan highlights three themes that could shape the banking sector outlook in the medium term, and puts in focus Malaysia's three wholesale-cum-investment banks, which also have regional growth aspirations. **We currently have Buy ratings on Maybank and RHB Capital, and a Sell rating on CIMB.**

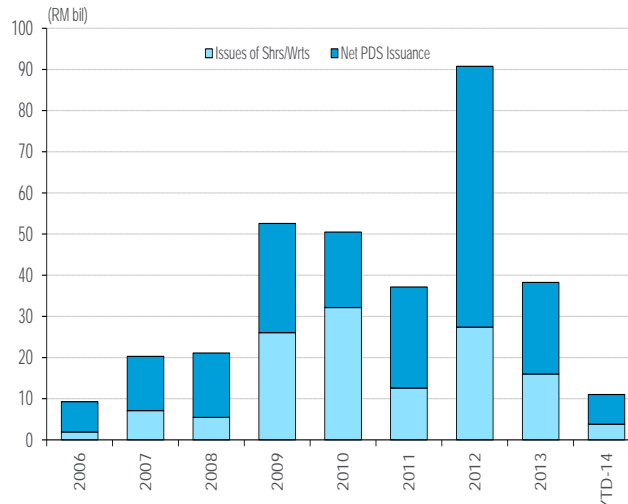
The first theme looks at how Malaysia's Economic Transformation Programme, or ETP, has since its launch in 2010 served as a catalyst for a surge in Malaysia's investment spending. This is timely for the bank sector as previously weak business loans seem to be recovering just as measures have been put in place to slow the rise in consumer debt. Even though large-ticket ETP announcements have slowed in the past year, banks' view that broader investment growth continues to maintain its momentum. The larger balance sheet wholesale banks will be the key beneficiaries, but importantly the growth in capital markets funding also highlights the need for a strong investment-banking capability.

Figure 2. Approved Investment Post-ETP — RM538.9bn



Source: MIDA, Pemandu and Citi Research

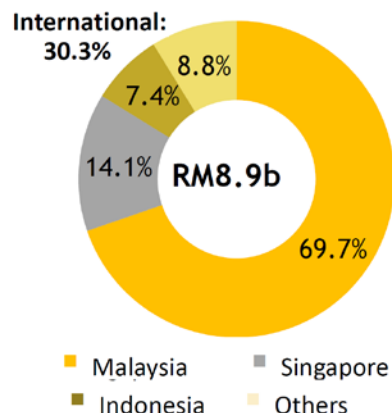
Figure 3. Funds Raised in Capital Market (Private Sector), Yearly Trend



Source: BNM and Citi Research

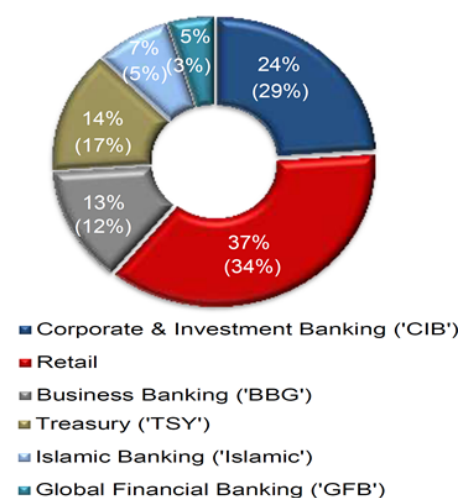
The second theme is the impact on Malaysia from tighter Asean integration. This gives two distinct opportunities for the regional wholesale banks, namely being able to capture the business/investment flows of Malaysian (and other Asean) companies going cross-border and, second, these bank themselves are broadening their geographic franchise via organic investment or M&A in regional markets.

Figure 4. Maybank PBT 30.3% International



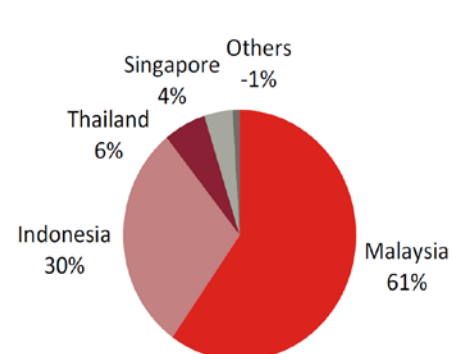
Source: Company

Figure 5. RHB Capital PBT 5% International



Source: Company

Figure 6. CIMB PBT 39% International



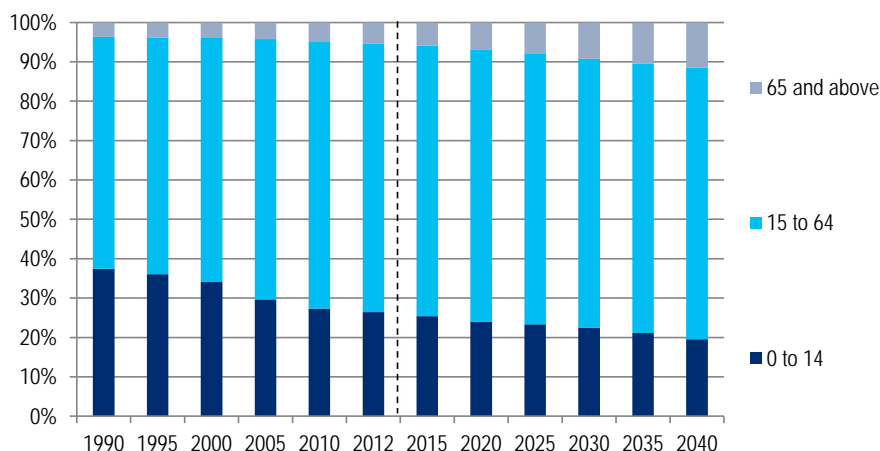
Source: Company

The final theme relates to efforts to spread growth geographically beyond the Klang Valley core, which is relevant to Malaysia's pure domestic retail-consumer banks. While we concede that consumer loan growth is set to moderate post central bank cooling measures, plus pressure from fiscal consolidation, it would be wrong to view the consumer story as "over".

For mortgages in particular, we believe both cyclical factors (rising construction starts) plus secular drivers (young population, urbanization trends) should continue to drive owner occupier housing demand, underpinning mortgage demand. Our main near-term concern for the pure domestic consumer banks has been sustained net interest margin pressure from unhealthy price competition.

Figure 7. Secular Drivers for Housing Demand — Young Population and Urbanization

Population Profile (By Age Group) - 1990 to 2040



Source: Department of Statistics Malaysia

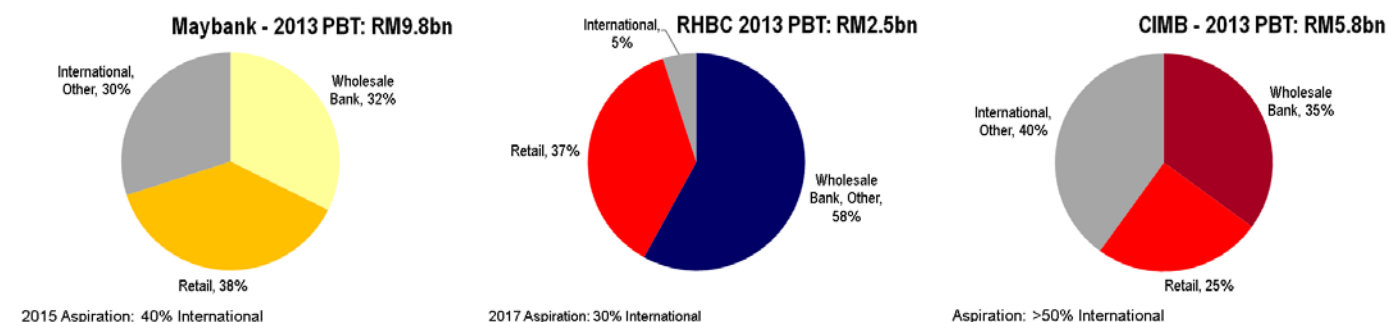
Focus stocks — Maybank, RHBC and CIMB

Maybank is our current preferred pick — It arguably has the most balanced business model of the three peers, being one of two dominant retail players in Malaysia, having a growing wholesale-IB platform under Kim Eng, and clear growth strategies for its key international units, currently dominated by Singapore and Indonesia.

RHBC Is perhaps the most leveraged domestic play on further growth in Malaysia's investment spend, but it is also putting in place clear goals for its retail business, while it has medium aspirations to grow its international contribution to 30%.

CIMB is already viewed as the most "Asean" of its peers with a 40% international contribution to its earnings, plus Malaysia's leading investment bank. But we view that its 30% Indonesia exposure will still undergo 1H14 earnings pressure, plus the RBS IB acquisition may still struggle to break even near term. Finally CIMB's January US\$1.1bn equity raising will be dilutive to ROE for 2014.

Figure 8. Estimated PBT Split Between Malaysia Retail, Malaysia Wholesale Bank*, and International Operations



Source: Citi Research Estimates * Note: Wholesale = Corporate, Business, Treasury and Investment Banks

Sustainability of Investment-led GDP Growth

Overview: After a virtual growth drought post the Asian Financial Crisis, from 2010 Malaysia's private investments have surged, with total (private + public) investment GDP comprising approximately 28% of GDP in 2013 (from just 22.5% in 2009). This surge likely coincided with the 2010 launch of the ambitious Economic Transformation Programme (ETP), which stated an aspirational target of a GNI per capita of US\$15,000 by 2020 (2013: US\$10,734) vs World Bank threshold of a high-income economy of approx. US\$12.5k. The ETP aims to attract US\$444bn in new investment by 2020 (cf. 2013 nominal GDP US\$312bn) to support the creation of 3.3m jobs (cf. labour force 2013: 13.2m) over that period. More fundamentally ETP aims to help Malaysia escape the so-called middle-income trap, by transitioning the economy towards a more productivity-driven (rather than factor accumulation) growth profile. The concerns resulting from such a surge in investment growth are:

[a] Whether the programme is simply too ambitious — cumulative end-2013 progress announced reached US\$69.3bn, 16% of the target, and during 2013 the size and frequency of new project announcements tailed off;

[b] Whether the investments are going into high-returns segments — Citi economist Wei Zheng Kit opines that the highest returns on capital productivity likely lie in manufacturing (especially electronics), while in contrast there are diminishing returns to the oil & gas sector. Clearly the returns debate arises when we consider the wide spectrum of projects such as MRT networks, high-speed rail links and KL commercial office properties;

[c] The impact on Malaysia's external balance — The preference for investment in areas such as manufacturing also lies in the impact it would have on net exports growth. Coincident with the surge in investment in the past few years has been a rapidly diminishing current-account balance, and a falling savings-investment gap.

Banks' perspective: Assuming that the investments trend continues, the key beneficiaries will be the larger balance sheet banks with a strong wholesale-cum-investment bank presence and the reach to go regional. Banks are indicating that many of the major ETP projects announced are rolling forward from the planning to the execution stage, and beyond these mega projects, private sector investment — both cross border and for domestic mid cap companies — is driving funding demand. And even though the pace of new ETP announcements may have tapered off in the past year, banks still see investment momentum continuing beneath these mega-ticket projects at the companies' level.

At the bank system level we note that the previously weak business loan cycle bottomed in mid-2013 and has started to stage a recovery (initially these are likely larger ticket loans but there should be a second-round impact down supply chains and to SMEs). But given overall ticket sizes involved the lift to banks' on-balance-sheet growth may end up being secondary to the size of funds raised in Malaysia capital markets, which experienced a surge since 2009.

Malaysia's ETP-boosted domestic investment revival now contributes 28% of GDP, with BNM viewing that this will support robust domestic demand well into 2015.

Even if investment growth is sustained, there is a near-term risk that it could place more pressure on the external account.

Malaysia's concern is about attracting the right type of FDI, and prioritizing projects in the higher returns segments.

Mfg FDIs are starting to flow into higher tech industries but perhaps not at the pace that will create the critical mass for a broader positive impact on the economy. Some successes include moving into downstream oil and gas, petrochemicals and also solar cells.

Domestic investments might be better used to force industries to upgrade from over-reliance on cheap labour.

Cross-border FDI is beginning to gather pace, such as from Singapore and China. Equally Malaysian corporates want to go overseas to expand within their industry core competencies.

Postponing of investment projects with high import content is a possible way to ease pressure on the external balance.

But aside from govt-backed projects such as the high-speed rail link and defense spending, a lot of projects are privately driven with their own timelines. Projects with long gestations such as office space (such as TRX) could also see phased development.

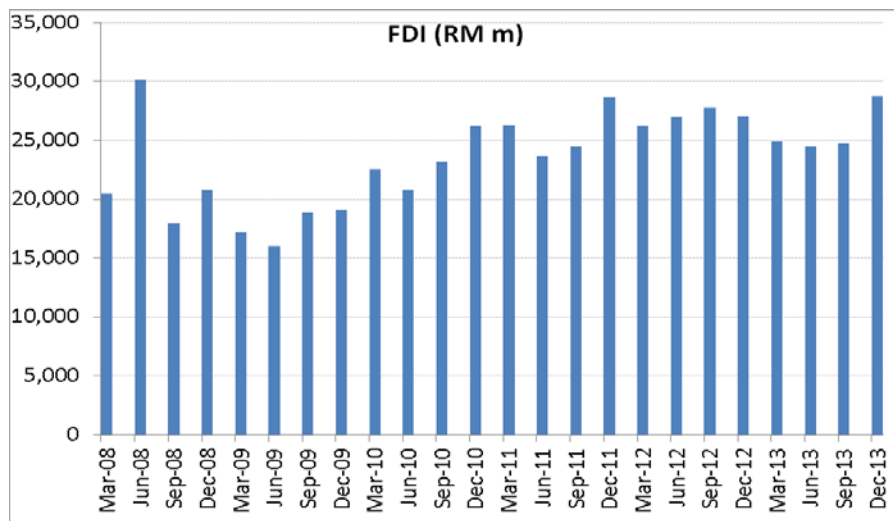
Prioritizing higher-return investment projects is key

Figure 9. Real Private Investment by Sector



Source: Department of Statistics, Malaysia and Bank Negara Malaysia Annual Report 2013

Figure 10. Malaysia FDI



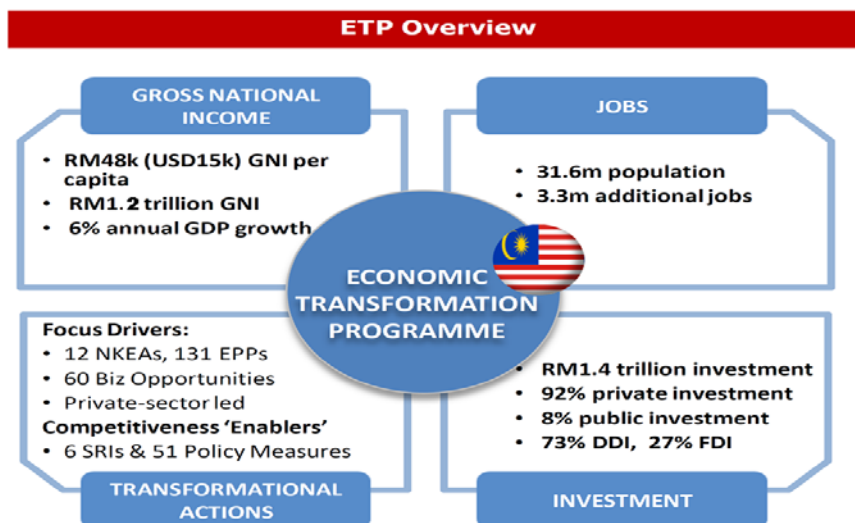
Source: CEIC, Citi Research

Figure 11. Selected Proposed Investment Projects (RM bn)

| Project | Type | Cost |
|------------------------------|---------------------|------|
| KL-Singapore High Speed Rail | Railway | 40.0 |
| Tun Razak Exchange | Commercial Property | 26.0 |
| Menara Warisan Merdeka | Commercial Property | 5.0 |
| Singapore-Johor Third Link | Bridge | - |

Source: The Edge, 1MDB, Budget 2011, Citi Research

Figure 12. Economic Transformation Program (ETP) Overview Diagram



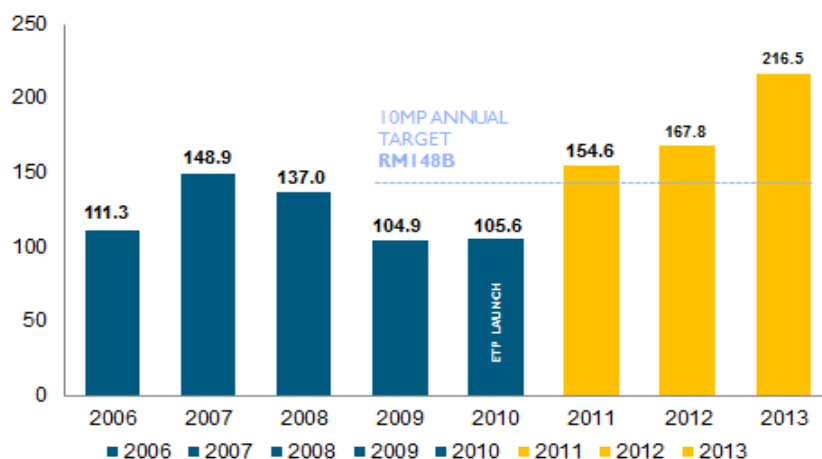
Source: AMMB, Citi Research

Figure 13. ETP Progress as of 2013

| 2011 110 Projects | 2012 39 Projects | 2013 47 Projects | 196 Projects | 2020 Target | % of Target Achieved |
|-----------------------------|---------------------------|---------------------------|-----------------------------|-----------------------------|------------------------|
| Investment: RM179.2 bil | Investment: RM32.1 bil | Investment: RM8.0 bil | Investment: RM219.3 bil | Investment: RM1,419 bil | Investment: 15.5% |
| GNI in 2020: RM129.5 bil | GNI in 2020: RM6.6 bil | GNI in 2020: RM7.4 bil | GNI in 2020: RM143.5 bil | GNI in 2020: RM1,190 bil | GNI in 2020: 12.1% |
| Jobs by 2020: 313,741 | Jobs by 2020: 94,702 | Jobs by 2020: 29,373 | Jobs by 2020: 437,816 | Jobs by 2020: 3.297 mil | Jobs by 2020: 13.3% |

Source: Pemandu and Citi Research

Figure 14. Approved Investment Post-ETP — RM538.9bn



Source: MIDA

Source: MIDA, Pemandu and Citi Research

Figure 15. ETP Targets 2020: Investment RM1.4 trillion, GNI Impact RM1.2 trillion and 3.3m Jobs

| | Investment RM Billion | Incremental GNI Impact RM Billion | Additional Jobs (‘000) |
|---|--------------------------|--------------------------------------|---------------------------|
| Agriculture | 21.8 | 29 | 75 |
| Business Services | 41.2 | 59 | 246 |
| Communications Content & Infrastructure | 51.5 | 36 | 43 |
| Education | 19.9 | 34 | 581 |
| Electronic and Electrical | 78.4 | 53 | 157 |
| Financial Services | 211.1 | 121 | 275 |
| Greater KL | 171.9 | 392 | 553 |
| Healthcare | 23.2 | 35 | 181 |
| Oil & Gas | 217.6 | 131 | 52 |
| Palm Oil | 124.2 | 125 | 42 |
| Tourism | 203.9 | 67 | 497 |
| Wholesale & Retail | 254.7 | 108 | 595 |
| Total Target by 2020 | 1,419.3 | 1,190 | 3,297 |

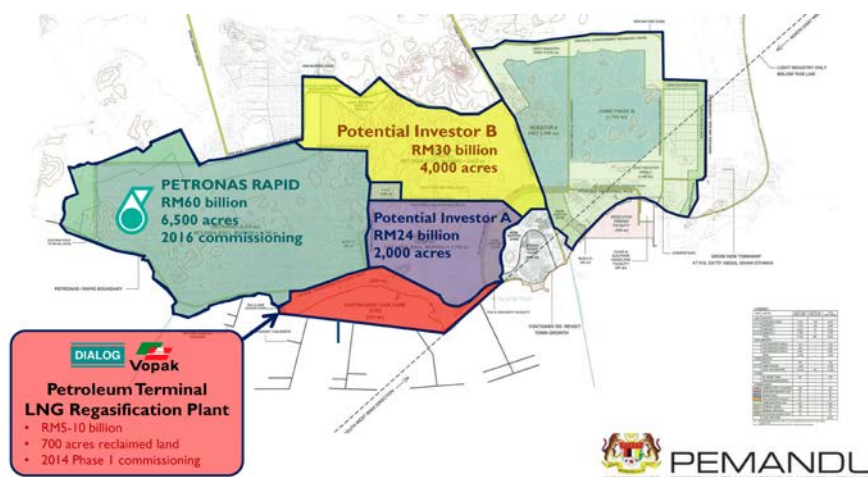
Source: Pemandu and Citi Research

Many of the ETP projects are privately funded and hence not under the govt purview of pacing.

Petronas' RM60bn, 2.43ha. Rapid Project has met with some delays — the project was originally slated to start operations in 2016 but it is likely to be pushed back to 2017.

Gives rise to overall question of performance monitoring and delivery. ETP's targets are somewhat more holistic (GNI growth, creating the right jobs and spurring investment in 12 key areas, as documented in ETP's annual report) rather than specific return on investment math.

Figure 16. Pengerang Integrated Petroleum Complex (PIPC) in Johor — RM170+ billion of investment and 21,000 acres of industrial area



Source: PEMANDU, Citi Research

Figure 17. High Impact Domestic Infrastructure Projects

| Project | Est value (RMbn) | Comments |
|--|------------------|---|
| Gemas-Johor Bahru Double Tracking | 8.0 | The last double tracking package, included in Budget 2012 and the ETP. A Chinese contractor is likely to play a major role. Malaysian contractors are vying for roles as JV partners or subcontractors. |
| West Coast Expressway | 5.6 | IJM is seen as the key beneficiary with a 38% effective stake in the concession. Concession agreement was signed in Jan 2013, followed by the financial close in December 2013. We expect the construction contract awards by year end. |
| Kuala Lumpur-Singapore High Speed Rail | 40.0 | Discussions are currently ongoing between the Malaysian and Singaporean governments with a target completion date of 2020 for the project. |
| IRWT: Langat 2 water treatment plant | 1.0 | The job was awarded to Salcon-MMC-AZRB in April 2014. However, it is uncertain if there is any impact from the current deadlock in the Selangor water assets consolidation. |
| Klang Valley MRT - SBK Line | 22.2 | Currently under construction at 24% completion. |
| Klang Valley MRT - SSP Line | 24.9 | The Malaysian Cabinet has approved the project and MMC-Gamuda as the PDP. Major contract awards are expected to begin in 2H2015. |
| Penang Traffic Alleviation Plan | 7.0 | Construction will only begin in 2015 as feasibility studies need to first be conducted. Tenders have been submitted. |
| Tun Razak Exchange (KLIFD) | 26.0 | Included in the ETP, formerly known as the KL International Financial District. A 28.3 ha development with an expected RM26bn GDV. The first earthworks package of RM169m was awarded to WCT. |

Source: The Star, NST, The Edge and Citi Research

Figure 18. Malaysia Five Economic Corridors Investment Target: Cumulative Investments in Five Economic Growth Corridors Jan-Sep 2013

| Corridor | Target Investment | Jan-Sep 2013 (RM billion) | | Major Projects in Progress |
|--|-----------------------------|---------------------------|----------|--|
| | | Committed | Realised | |
| East Coast Economic Region (ECER) Corridor | RM112 billion (2008-2020) | 22.8 | 3.7 | <ul style="list-style-type: none"> • Kuantan Port Expansion • Kuantan Port City Development • Malaysia-China Kuantan Industrial Park (MCKIP) • Kuala Terengganu City Centre (KTCC) • Kertih BioPolymer Park |
| Iskandar Malaysia | RM383 billion by 2035 | 12.6 | 10.0 | <ul style="list-style-type: none"> • Automotive Industrial Hub, Pekan • Pinewood Iskandar Malaysia Studios • Gleanegles Medini Hospital • Double Tree Hilton • Pegasus International School • Biotechnology Incubation Centre |
| Northern Corridor Economic Region (NCER) | RM177 billion (2007 - 2025) | 7.2 | 7.2 | <ul style="list-style-type: none"> • Aquaculture Development Complex, Selinsing • Expansion Programme Edu Citi Tel |
| Sabah Development Corridor (SDC) | RM77.5 billion by 2020 | 8.6 | 3.0 | <ul style="list-style-type: none"> • Sabah Oil and Gas Terminal (SOCGT) & Sabah Sarawak Gas Pipeline (SSGP) • Sipitang Oil and Gas Industrial Park (SOGIP - Phase 1 SAMUR) • Kimanis Power Plant • International Technology and Commercial Centre (ITCC) • Aeropod • Sabah International Conventional Centre (SICC) • Sabah Agro Industrial Precinct (SAIP) • Palm Oil Industrial Clusters (POIC) at Lahad Datu and Sandakan |
| Sarawak Corridor of Renewable Energy (SCORE) | RM334 billion (2008-2030) | 2.2 | 1.7 | <ul style="list-style-type: none"> • Ferro alloy manufacturing plant • Polycrystalline silicon manufacturing plant |
| Total | | 53.4 | 25.6 | |

Source: ECER, IRDA, NCER, SDC, SCORE, NST, Malaysia Economic Report 2013/2014 and Citi Research

Banks — rising business loans & capital markets activity

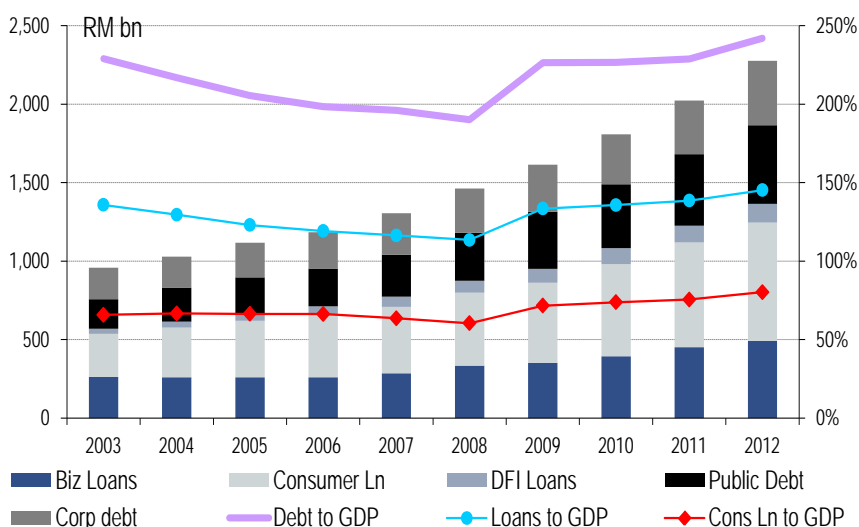
The expectation is that over 90% of the ETP investment (total estimated at RM1.4tr) will be private-sector funded.

While banks' business loan growth should benefit, there is a sense that the banking system is already looking overly expanded.

Hence further sources of private-sector funding (such as venture capital and private equity) may have to develop as deepening the corporate bond sector.

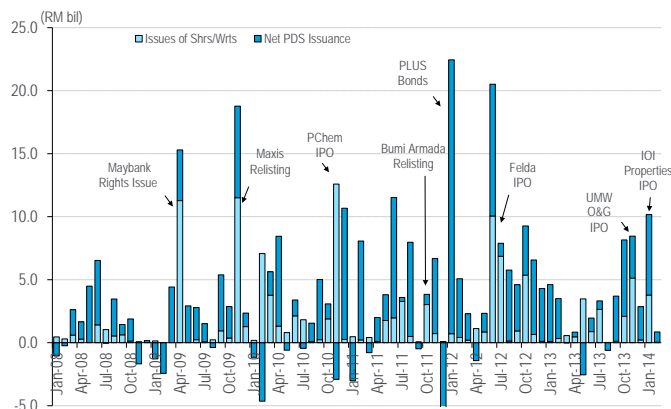
The rising importance of the capital markets as a primary source of investment funding has already been evident in the record amounts that have been raised in the past 3-4 years.

Figure 19. Malaysia Credit Penetration Analysis



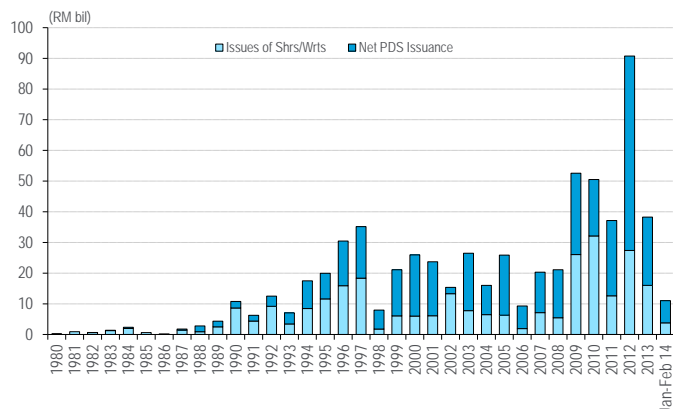
Source: Citi Research

Figure 20. Funds Raised in Capital Market (Private Sector), Mthly Trend



Source: BNM and Citi Research

Figure 21. Funds Raised in Capital Market (Private Sector), Yearly Trend

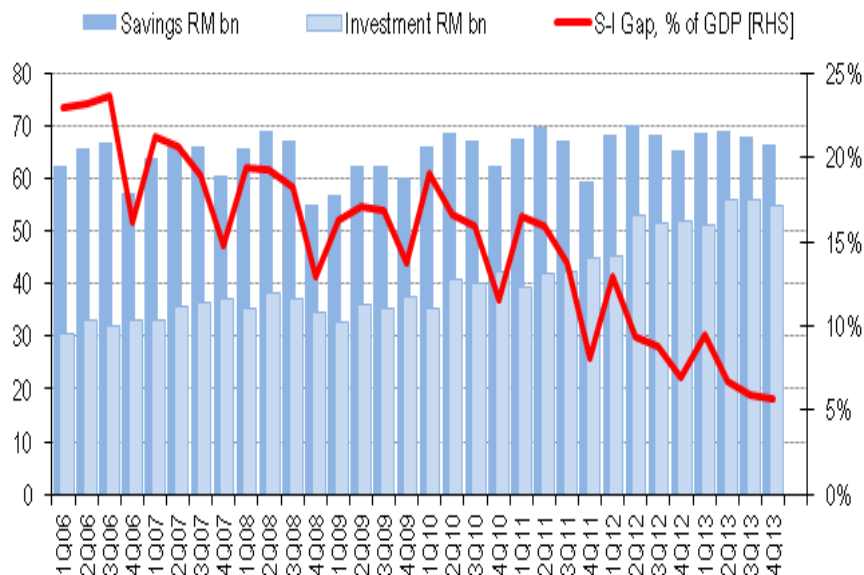


Source: BNM and Citi Research

Market participants view that there remains ample domestic savings for the domestic institutional funds to absorb new debt issues that would arise from ETP roll-out.

But the Savings-Investment gap has narrowed considerably in past 3-4 years.

Figure 22. Malaysia GDP Savings-Investment Gap



Savings defined as total GDP less consumption led govt spend

Source: CEIC, Citi Research

Asean Integration & Regionalization

Overview: Prospects for Malaysia as an attractive FDI destination should improve on rising Asean integration, with manufacturing FDI likely focused on intermediate goods (primarily for G3 final demand), and services FDI likely on Asia/Asean final demand. But equally, greater regional integration may drive more outward bound investment (ODI) into Asean by large Malaysian corporates, and for Iskandar, eventual economic integration with Singapore should be a long-term boon for growth. Further rounds of FTAs and other integration initiatives (including AEC in 2015) to reduce tariff/non-tariff barriers arguably should also spur complementary FDI and GDP gains through Asean. For Malaysia Inc. there are several industries maturing domestically, and each industry's dominant players are increasingly looking to capture incremental growth upside in the Asean region (and beyond), and/or looking at overseas investment as a way to counter rising costs domestically.

Banks' perspective: [1] Thanks to timely acquisitions in recent years to expand wholesale and investment-banking platforms, the larger banks' IB capabilities have evolved beyond domestic Malaysia, enabling them to capture increasing investment flows and growth opportunities that are extending into the region. This could be both through financing Malaysian principals expanding organically into the region, and also through growth into other Asean markets through M&A. [2] Equally for the larger Malaysian banks themselves, with dominant shares in segments of the domestic banking industry, and with likely limited rationale to pursue further domestic consolidation, these banks' mgmt. view the next level of growth as pursuing direct opportunities in Asean. Typically this is further (organic) investment in building out existing geographic platforms or operating subsidiaries, but it has also driven a wave of regional bank M&A in recent years, and selectively (where there is a strong business case and a deal makes sense financially) we could see this M&A trend continue.

Maybank — regionalization key to earnings alpha

Maybank seeks to be the undisputed #1 retail financial services provider by 2015.

Figure 23. Maybank's Domestic Retail financial Services Market Share

| | Dec-11 | Dec-12 | Mar-13 | Jun-13 | Sep-13 | Dec-13 | Dec-13 vs. Dec-12 | MBB Rank ^ |
|--|--------|--------|--------|--------|--------|--------|-------------------------|------------|
| Deposits | | | | | | | | |
| Total Deposits | 17.4% | 17.1% | 16.8% | 17.7% | 17.7% | 18.2% | ▲ | 1 |
| Total Core Retail Deposits | 18.1% | 18.3% | 18.3% | 18.3% | 18.7% | 19.0% | ▲ | 2 |
| Retail CASA | 23.3% | 23.6% | 23.3% | 23.1% | 23.9% | 24.8% | ▲ | 1 |
| Retail Savings | 28.1% | 28.2% | 28.19% | 28.0% | 27.5% | 29.8% | ▲ | 1 |
| Retail Fixed Deposits (FD) | 15.1% | 15.2% | 15.3% | 15.4% | 15.6% | 15.7% | ▲ | 2 |
| Loans | | | | | | | | |
| Total Consumer/Household | 16.4% | 17.0% | 17.1% | 17.1% | 17.1% | 17.2% | ▲ | 2 |
| Auto (Purchase of transport vehicles) | 19.2% | 20.2% | 20.3% | 20.5% | 21.0% | 21.5% | ▲ | 2 |
| Total Mortgage* | 13.2% | 13.4% | 13.3% | 13.3% | 13.2% | 13.1% | ▼ | 2 |
| Credit Cards # | 15.3% | 15.2% | 15.3% | 15.4% | 15.3% | 15.1% | ▼ | 2 |
| Unit Trust | 63.9% | 60.2% | 58.5% | 57.6% | 56.8% | 55.8% | ▼ | 1 |
| | Dec-11 | Dec-12 | Mar-13 | Jun-13 | Sep-13 | Dec-13 | Dec-13 Vs Dec-12 | MBB Rank^ |
| Internet Banking - 3 months Active Users | 35.68% | 34.1% | 34.1% | 34.0% | 34.31% | N/A | N/A | 1 |
| Mobile Banking - 1 month Active Users | 87.0% | 80.5% | 75.7% | 76.7% | 75.43 | N/A | N/A | 1 |
| Branch Network | 19.0% | 19.0% | N/A | 20.0% | 23.0% | 20.0% | | 1 |

* Refers to Housing & Shophouse Loans

The above market share for Cards refers to Receivables. In terms of Cardbase, Billings and Merchant Sales, Maybank is ranked No. 1.

^ MBB ranking as at Sep'13

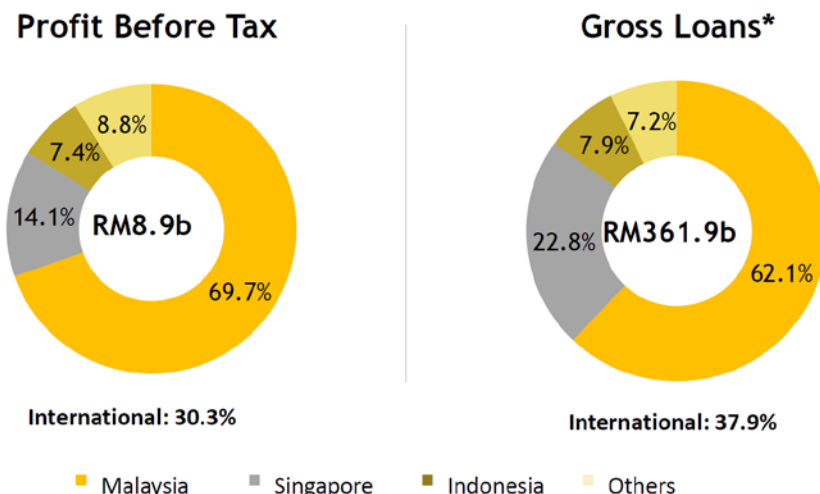
The above industry figure includes commercial banks and Non-Financial Institutions

Source: Company

Domestic dominance curbs above-market growth rates: Maybank's desire to go regional for future growth is due in part to the extent of its existing market share dominance in Malaysia. Maybank is already the #1 or #2 player in most aspects of domestic retail financial services (typically vying with Public Bank) and arguably has an unrivaled distribution both in the physical and digital banking space. Given this dominance, there appears to be little logic to Maybank seeking a material domestic in-market acquisition unless it was to capture a very specific product space.

Maybank's stated strategic goal is to derive 40% of PBT from international operations by 2015, versus 2013 30.3%, although we suspect this is more aspirational than a firm target.

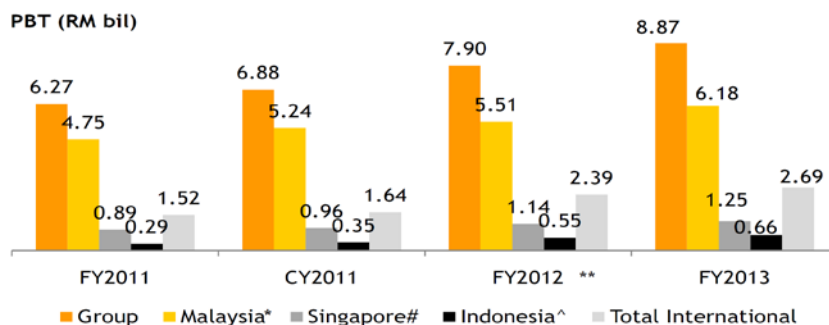
Figure 24. International Contributes 30% of Group PBT



Source: Company

Seeking regional growth for alpha: As recently as 2007, Maybank was still primarily a domestic bank with >85% of PBT from Malaysia. More than half of the c.15% international contribution came from its long standing Singapore business, other contributions coming from smaller markets such as the Philippines. But by mid-2008 the bank was in the midst of completing 3 acquisitions in South/Southeast Asia, notably a controlling stake in Indonesia Bank BII (current legal stake 80%/economic stake 97%), plus a 20% stake in Pakistan's MCB Bank and 15% (current stake 20%) in Vietnam's AnBinh Bank.

Figure 25. PBT Growth by Geography



* Malaysia = Domestic Banking Ops, Investment Banking, Insurance & Asset Management, Group Elim, Group Adjustment, Other Subsidiaries

Singapore = Singapore Branch and Kim Eng Group

^ Indonesia = BII and Maybank Syariah Indonesia.

**PBT for CY2011 includes six months PBT in second half FY2011

Source: Company

As of 2013, just over 30% of PBT was derived from international. Singapore has grown in prominence to 14% of PBT, Indonesia under BII contributes over 7%, while the remainder comes from other geographies including the Philippines, and the Pakistan (and to a lesser extent Vietnam) associates. With Maybank's dominance in Malaysia likely restricting domestic growth to being largely in line with the industry, the additional "alpha" will need to come from the regional businesses. We see this broadly being executed in three ways.

[a] Further investment in and organic growth of existing overseas entities:

The key drivers of Maybank's overseas growth have remained Singapore, and re-energizing BII in Indonesia from the lows of the 2009 GFC.

Singapore continues to be an important growth driver, but the loans business has felt the pain of thin net interest margins, and 2014 growth is likely increasingly driven by corporate & business loans rather than consumer. We suspect that earnings will also migrate towards fee-based sources to reflect Singapore's position as a regional hub for trade, cash mgmt. and wealth mgmt. flows. Trade and cash mgmt. have helped Maybank drive sticky deposit growth outside of Malaysia. Wealth mgmt. at present is small for the Singapore operation but should become an important business longer term.

Indonesia had a strong 2013 (profits rose 29%yoy) as strategies put in place to re-energize the franchise came to fruition. The business model is currently more retail and SME/business banking centric; historic dependence on 2W finance has been de-emphasized. Heavy investment in distribution (2013 branches 422, ATMs c.1,500) was a key factor in driving strong CASA growth (2013: +26%yoy), and BII is likely to further raise this to about 450 branches. Key areas of improvement (and hence earnings alpha) include capturing opportunities on the corporate bank side, by replicating a more client-focused model that has worked well in Malaysia as well as leveraging Kim Eng's capabilities. Near term BII (like other small banks) is facing a tough 2014 given the current liquidity crunch and high rates environment. Maybank recently reduced its legal ownership in BII to 80% to meet local market requirements.

Philippines has become a new focus area for investment in the past 2 years. Although Maybank has had a long standing presence in the Philippines it was very small (near or just outside the top 20 banks), but in the past few years the branch network has been expanded from 55 to 77. Mgmt. plan to further increase this to 100, as well as improve Maybank's presence in Metro Manila as a consumer bank. 2014 is likely to be another "buildout" year for the franchise, with cost-income ratio still high (2013: 74%) and taking care of legacy asset quality issues. It could be another 2 years away before the Philippines can become a more material growth driver for the group (2013 profit: P678m or RM49m).

Overseas associates: Maybank reported RM139m in associate income in 2013, the bulk of which was driven by its 20% stake in MCB and to a lesser extent the 20% of AnBinh Bank. How Maybank can develop these businesses is less clear to us given that it cannot exert much mgmt. influence nor can Maybank increase its stake given the foreign ownership caps.

[b] Regionalization of key business lines such as the wholesale bank:

Maybank's global banking (=corporate + markets + investment bank) operation was transformed by the Aug-2011 acquisition of Singapore-based brokerage Kim Eng, although much of the early profit synergies generated in the first year came mainly in Malaysia as the new entity captured quick wins. Maybank-Kim Eng is structured as a regional business model, but currently still over 60% of the business growth is

Malaysia-dependent. Thus the earnings alpha of the enlarged wholesale-investment bank will come from more fully exploiting its Asean regional platform in terms of completed capital markets deal, M&A advisory and bond offerings. While within a Malaysia context Maybank-Kim Eng is a top 3 player, on a regional basis the goal would be able to break into the top 10.

Figure 26. Maybank Kim Eng Gaining Improved Recognition in its Regional Franchise

Strategic Objective 2: Leading ASEAN wholesale bank eventually expanding to Middle East, China & India

| NOTABLE DEALS COMPLETED FROM JAN - DEC 2013 | | | | |
|--|---|--|--|--|
| Malaysia  Malakoff Power Bhd RM 5.8 billion Sukuk Sole Principal Adviser, Lead Manager, Facility Agent, Shariah Adviser, Trustee & Security Agent January 2013 | Malaysia  Sime Darby Global Berhad USD 1.5 billion Multi-Currency Sukuk Issuance Programme Joint Principal Adviser, Joint Lead Arranger, Joint Lead Manager, Dealer, Bursa Listing Agent & Joint Shariah Adviser January 2013 | Malaysia  AirAsia X Berhad RM 1.14 billion IPO Joint: Global Coordinator, Joint: Bookrunner, Joint: Managing Underwriter and Joint Underwriter July 2013 | Malaysia  Battersea Project Holding Co Ltd & Battersea Project Phase 1 Holding Co Ltd GBP790.2 million Syndicated TI/RC/BG Facilities Joint Mandated Lead Arranger & Lender October 2013 | Singapore  Swiber Holdings Ltd USD 500 million Multicurrency Islamic Trust Certificate Issuance Programme Programme Sole Lead Arranger, Bookrunner, Global Coordinator August 2013 |
| Philippines  Travellers International Hotel Group Inc. PHP 18 billion IPO Joint: Global Coordinator, Joint: Bookrunner & Joint Lead Manager November 2013 | Vietnam  Vingroup USD250 million Syndicated Loan Mandated Lead Arranger & Bookrunner October 2013 | Indonesia  PT Matahari Departmental Store Tbk IDR 14.6 trillion Share Placement Co-Lead Manager March 2013 | Philippines  San Miguel Corporation USD 1.5 billion Syndicated Revolving Credit Loan Mandated Lead Arranger and Bookrunner April 2013 | Hong Kong  Huawei Tech Investment Co Ltd USD 1.5 billion Syndicated Term Loan and Revolving Credit Facility Mandated Lead Arranger September 2013 |

Source: Company, Citi Research

Regional League Table - Mergers & Acquisitions

| 2013 | | 2012 | | 2011 | |
|---------|----------------|---------|----------------|---------|---------------|
| Ranking | Advisor | Ranking | Advisor | Ranking | Advisor |
| 1 | Morgan Stanley | 1 | Goldman Sachs | 1 | UBS |
| 2 | JP Morgan | 2 | Morgan Stanley | 2 | Deutsche Bank |
| 3 | HSBC Bank | 3 | Credit Suisse | 3 | Goldman Sachs |
| 4 | Credit Suisse | 4 | JP Morgan | 4 | CIMB |
| 7 | Maybank | 8 | Maybank | 10 | Maybank |

Regional League Table - Regional Bonds

| 2013 | | 2012 | | 2011 | |
|---------|-----------|---------|-----------|---------|--------------------------|
| Ranking | Advisor | Ranking | Advisor | Ranking | Advisor |
| 1 | HSBC Bank | 1 | HSBC Bank | 1 | HSBC |
| 2 | SCB | 2 | SCB | 2 | UBS |
| 3 | CIMB | 3 | CIMB | 3 | Citi |
| 4 | DBS Group | 4 | DBS Group | 4 | Ind & Comm Bank of China |
| 11 | Maybank | 5 | Maybank | 14 | Maybank |

Source: Bloomberg, Dec 2013

Countries : Malaysia, Indonesia, Singapore, HK, Philippines, Thailand & Vietnam

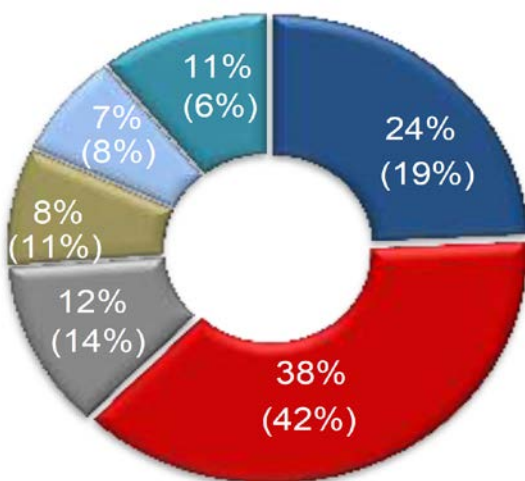
In the long term, we view that this regionalization goal potentially could be followed by other Maybank business units such as insurance and possibly its Islamic businesses. Part of Maybank's decision to reorganize it country vs business mgmt. reporting matrix to ensure that full synergies are reaped out of all business units in each of its key geographies.

[c] Further M&A? Notwithstanding aggressive growth objectives by both geography and business units, to achieve 40% international PBT by 2015 we view as an unrealistic goal, with even 33%-35% being a stretch target. However, arguably a material overseas M&A could provide the required boost. Views in 2013 that Maybank was considering a material acquisition in Thailand (BAY was eventually sold to a Japanese bank) petered out when it became clear that Maybank was not willing to overpay and that the existing operating terms were not compelling. While we view that further M&A cannot be ruled out, our sense is that mgmt. will remain extremely disciplined in the ensuring an appropriate operational fit as well as valuation before heading down the M&A route. In the near term Maybank appears to have much to do by simply expanding organically.

RHBC — a “regional Asean powerhouse” by 2017

Currently the most domestic of the 3 Malaysia peers: As of 2013 RHBC was still arguably largely a Malaysia domestic banking play. In terms of loan book, Malaysia still dominates at 92.5% of group loans, the main international contributors to the 7.5% being Singapore (6.2%), Thailand (0.6%), and Cambodia (0.4%).

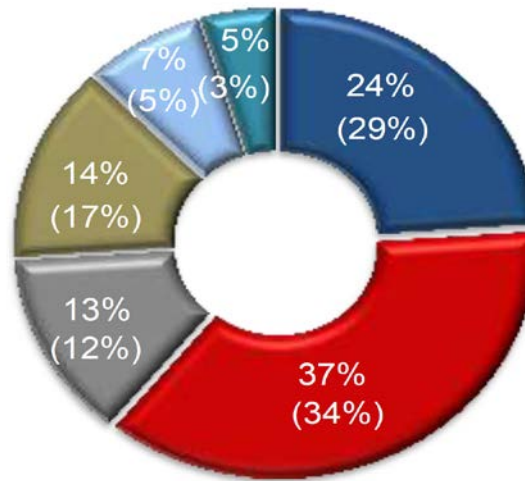
Figure 27. 2013 Group Income by Division 2013 (2012 in Brackets)



- Corporate & Investment Banking ('CIB')
- Retail
- Business Banking ('BBG')
- Treasury ('TSY')
- Islamic Banking ('Islamic')
- Global Financial Banking ('GFB')

Source: Company

Figure 28. Group PBT by Division 2013 (2012 in Brackets)



Source: Company

In terms of revenues and earnings, RHBC discloses a segment called “Global Financial Banking” (which captures commercial banking businesses in Singapore, Thailand, Cambodia and Brunei, as well as the international component of investment banking). As of 2013 revenues from this segment came to 11% of group, while PBT contributed just 5% of group. Per mgmt. guidance about 5%pts of overseas revenue comes from RHBC’s Singapore operation.

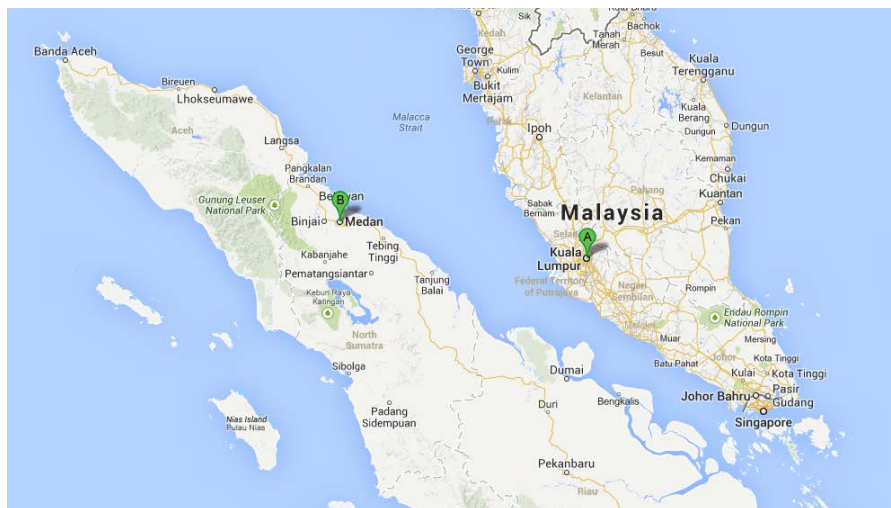
Targeting 30% of revenues outside Malaysia by 2017: RHBC recently laid out their “IGNITE 2017” strategy blueprint where among other goals it targeted a tripling of the international component of group revenues from 11% to 30%. This appears to be based on 4 main drivers:

[1] Planned acquisition of Bank Mestika Indonesia: Successful execution of an Indonesia commercial bank expansion through M&A could contribute around 5%pt to 10%pts of RHBC’s international revenue contribution by 2017.

In this long-delayed Indonesia M&A deal (initially proposed back in 2009, with the present revised terms set in Jan 2013), RHBC agreed to purchase a 40% stake in Bank Mestika Dharma for Rp2.07tr (or an estimated RM581m at current exchange rates), which equates to a P/B multiple of 2.66x equity based on the latest 2013 financial data. RHBC has issued a number of extensions to the offer period (the current offer extension expiring 30 June 2014), awaiting regulatory approval from the Indonesia regulator OJK. It seems likely that the current offer period will again lapse, but we understand that RHBC is likely to make a further extension to the

deal, knowing that current political elections in Indonesia may be the main reason for the OJK approval delay. Bank Mestika is a small-mid sized bank based in the predominantly Chinese business area of Medan in North Sumatera, Indonesia.

Figure 29. Medan, Indonesia is 340km (<1 hour flight) away from Kuala Lumpur, Malaysia



Source: Citi Research

RHBC continue to view Bank Mestika as an important acquisition for the group's medium-term strategy as it will provide a Rupiah commercial bank balance sheet to compliment RHBC's investment banking business in Indonesia, which today is effectively run offshore out of Singapore. The bank itself is primarily a family run SME bank serving the local Chinese business community, which also enjoys a strong deposit base (2013: CASA ratio 64%, LDR 102%), and with the vendor likely retaining a greater than 40% stake in the bank post sale, RHBC should have a supportive partner to ensure the ongoing health of the bank.

For now RHBC is capped at 40% by BI regulations introduced in early 2013, and while there are provisions which allow an eventual increase in stake up to 80% in practice at this point it is not entirely clear if and when BI would approve that. So while RHBC would prefer a larger stake, for now mgmt. view that 40% stake gives them sufficient control over the bank to implement its growth strategy. The aspects of control set out in the terms of the agreement should also ensure that RHBC can consolidate Bank Mestika into its group earnings and also avoid punitive capital treatment under Basel 3. Should the transaction go ahead, we expect RHBC to proceed with a rights issue (RM581m is less than 2.7% of RHBC market cap).

Based on 2013 data, Bank Mestika reported total revenues of Rp706bn (c.RM202m, or 3.4% of RHBC group revenues) and a net profit of Rp613bn (c.RM175m), which assuming a 40% stake would equal about 4% of RHBC group profit. Thus assuming the deal goes through and RHBC eventually assumes an 80% stake in Mestika, the target of contributing 5%-10% of RHBC's target overseas revenue contribution by 2017 seems quite feasible if we include the expected lift to the investment banking business in Indonesia.

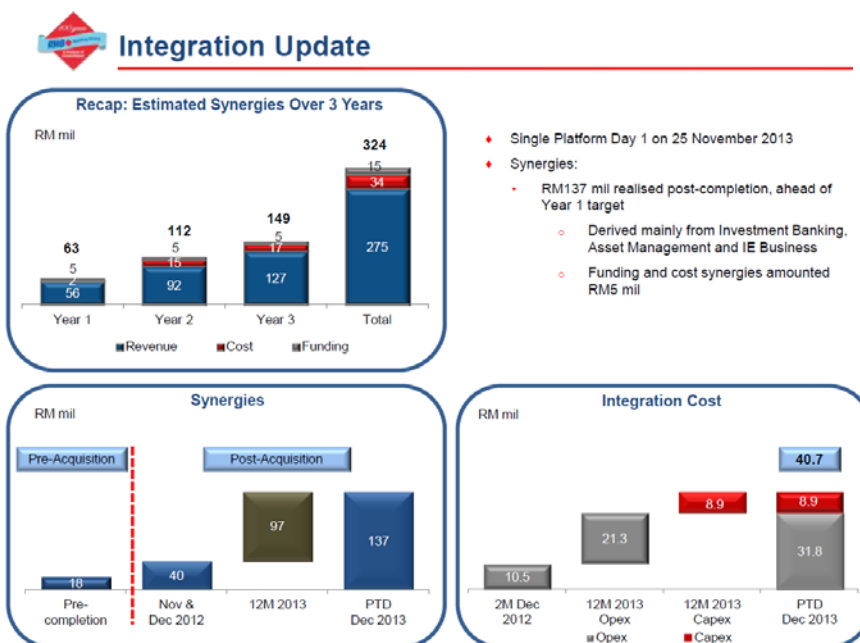
[2] Singapore — repositioning to be a regional hub for flow businesses: RHB's Singapore unit ("RHB SG") presently contributes 5% of RHBC group revenues, with mgmt. targeting to double this contribution to about 10% by 2017. RHB SG was established more than 50 years ago, and right up to today the bank has continued to run a relatively simple retail-SME loan based business model out of its 7 branches. In 2013 RHB SG posted a profit of close to S\$35m (RM91m, or 5% of group profit).

Mgmt. view there is considerable upside to the earnings capability of RHB SG. On the basic loans front mgmt. still see good potential in the middle market business space, where customer may view RHB SG as a second banking relationship after one of the large local banks. But the most material upside lies in a re-positioning of the Singapore franchise to be a regional hub for RHBC in major flows and fees businesses, including treasury, global corporate account mgmt. (IB advisory, trade finance), and asset mgmt. (AUM is small at c.RM45bn but growing quickly). RHB SG will also set up a wealth mgmt. unit targeting the S\$1m-S\$5m investible assets segment, and in a later phase could set up a cash mgmt. offering.

Including the likely growing contribution from leveraging the investment banking advisory platform under OSKIB and the 51% JV brokerage OSK-DMG, mgmt. envision that Singapore could become a S\$100m business within the next few years.

[3] Leveraging the OSKIB platform: RHBC's late-2012 OSKIB acquisition has already surprised on the upside, delivering strong revenue synergies ahead of schedule in its first year of operation.

Figure 30. OSKIB Integration Update — RM137m Realised Synergies vs RM63m Projection



Source: Citi Research

Much of those early wins have still been Malaysia-centric, with international still at present only 20% of the IB business. Thus leveraging the corporate investment bank platform into the region (with Singapore being the base for global corporate account mgmt.) should provide further growth upside including in Indonesia and the nascent Hong Kong business. The growing international IB franchise should be a key driver of the final 10%pt contribution that makes up the 30% 2017 intl. target.

However, domestic Malaysia will still be a strong business driver for the enlarged IB platform. The old RHB IB side historically depended on large corporate relationships (assisted in part by its major shareholder) as the main deal flow, vying for business as part of the big 3 local banks. But OSKIB has brought to the table a lot more mid-cap corporate deals, which although smaller in ticket size, are generally more profitable. This gives the enlarged franchise a strong pipeline of "business as usual"

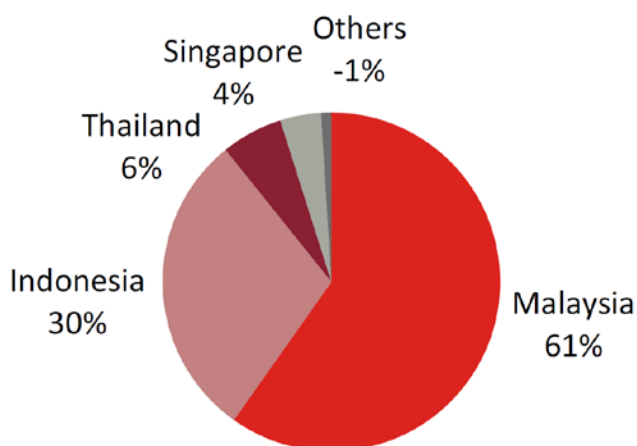
banking deals, whether mid-cap companies or larger private sector corporates. While RHBC will gain its share of the headline ETP mega-ticket deals (some of which arguably will have a long gestation period to deliver returns), the BAU pipeline will continue to drive business revenue. The OSKIB Year 2 integration synergies were projected to be RM112m; mgmt. guide that in 1Q2014 alone, the business appears to be on track for almost 40% of that target already.

[4] Other international plans: Although there will likely be a much longer gestation period for returns, RHBC mgmt. are looking at several other international opportunities: **[a] Hong Kong-China:** OSKIB HK already turned a small profit in 2013 of RM2m (historically loss making) as it leveraged on the RHB name and balance sheet to secure deals. Hong Kong is likely to also be the basis for China growth unless there is a really compelling case to acquire a direct presence in China. **[b] Philippines** is one of the few Asean markets where RHBC has no presence; mgmt. are studying opportunities there but the likely entry vehicle will also be IB so that mgmt. can better understand the market before committing more capital and resource needed for a commercial banking operation.

CIMB — goal of >50% of PBT outside Malaysia

Currently the broadest regional footprint of its Malaysia peers: CIMB already leads its Malaysian peers in having the largest international contribution to group earnings. As of 2013 close to 40% of group PBT was derived from outside Malaysia. Despite a relatively challenging year for CIMB Niaga, Indonesia remained by far the biggest regional driver at 30% of profits. The other main international drivers of Singapore and Thailand saw 2013 strong growth, albeit from a small base.

Figure 31. 2013 Group PBT by Country



Notes on PBT growth figures (RHS):

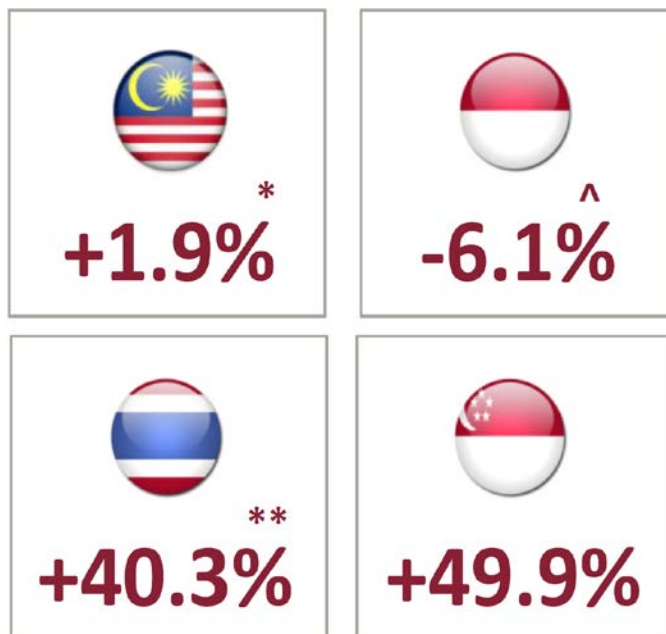
* Excluding HQ costs, gains from sale of CIMB Aviva and MSS charges

^ IDR depreciated 8.1% Y-o-Y (daily average rate). In local currency, Indonesia recorded a growth of 2.1% Y-o-Y

** Excluding gain from TAMC and other one-off items, Thailand's PBT grew 54.7% Y-o-Y

Source: Company

Figure 32. 2013 PBT Growth by Key Countries



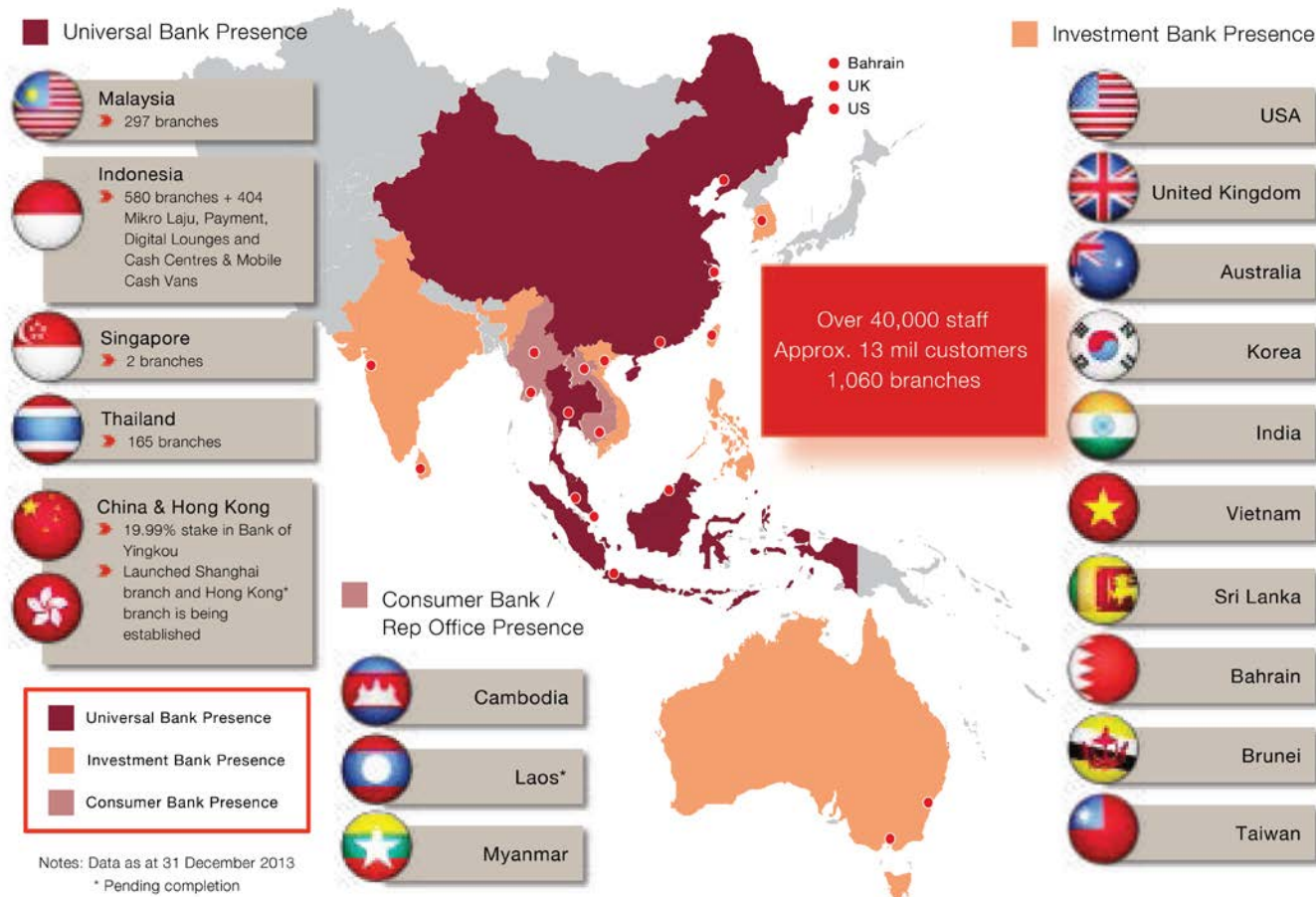
Source: Company

Management expects the regional contribution to PBT to continue to grow:

CIMB has held a long-standing goal to raise the international contribution of group PBT to above 50% in the medium term. **Indonesia** — Notwithstanding a tough 2013, Indonesia under CIMB Niaga remains on a high longer-term growth trajectory. Mgmt. acknowledge that the 1H14 will continue to be challenging; NIMs are expected to see some further pressure of c.20-30bps in 2014, which is far less than

the 53bps of 2013. CIMB Niaga still expects to grow loans in the mid-teens range, with more emphasis to the corporate side on the expectation of a better second half for the economy post elections, while continuing to work on CASA growth from transactional balances. **Singapore** — After exceptional growth of >60% in 2013, mgmt. expect Singapore should still post around 20% asset growth in 2014, although the rapid trade finance growth will ease off. **Thailand** — Despite the present macro and political backdrop, mgmt. feel that more can be done to develop the consumer banking side of the franchise which up to now has been more wholesale driven.

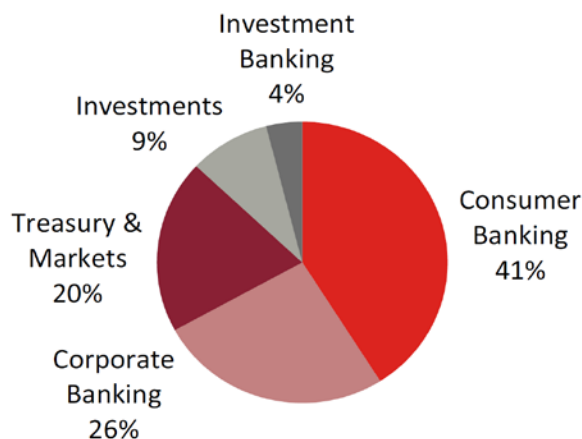
Figure 33. CIMB's Group Platform — Philippines is the Missing Piece in Asean



Source: Company

M&A — Philippines still on the table: To boost a 40% international PBT contribution to over 50% still suggests M&A, and mgmt. has indicated that CIMB is still actively looking for opportunities to enter the Philippines market, which remains one of the major Asean markets where the group is yet to have a presence. Mgmt. aborted a mid-2012 plan to buy the mid-sized Bank of Commerce in the Philippines, partly due to valuation and part on terms relating to the operating and collaboration terms with the vendor. But CIMB is still keen to establish a universal banking presence in the Philippines to complete the Asean presence. Elsewhere in Asean CIMB is still waiting to receive a Vietnam banking licence (an investment banking presence already exists) and to complete the 10 country Asean presence. CIMB Thai is expected to open a branch in Laos in 2Q2014.

Figure 34. 2013 Group PBT by Division

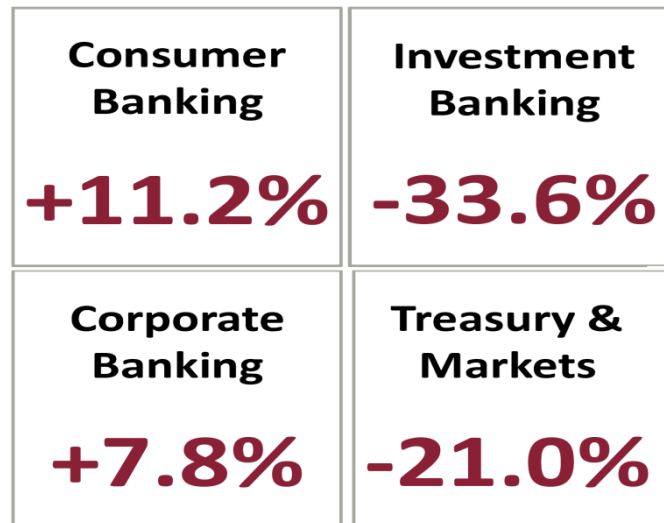


Notes on PBT growth figures:

* "Investments" PBT (9% of Group PBT) fell 9.6%yoy, excluding gains from sale of CIMB Aviva and MSS charges.


Source: Company

Figure 35. 2013 PBT Growth by Key Division



Source: Company

Figure 36. IB Market Shares Malaysia

| | FY13 | | FY12 | |
|--|--------------|------|--------------|------|
| | Market Share | Rank | Market Share | Rank |
|  Cash Equities | 17.3% | 1 | 11.7% | 1 |
| IPO | 19.6% | 1 | 21.8% | 1 |
| ECM | 24.8% | 1 | 25.2% | 1 |
| M&A | 23.0% | 1 | 24.0% | 3 |
| Syndication ^ | 7.6% | 5 | 11.6% | 3 |
| DCM | 26.2% | 1 | 26.8% | 1 |
| Sukuk | 26.2% | 1 | 28.1% | 1 |

Source: Company

RBS acquisition — creating an Asia-wide investment banking platform:

Another channel by which CIMB is expected to capture the longer term flows of cross-border investment and regional integration is through its enhanced regional investment banking platform (which is part of the wholesale bank).

2013 was a mixed year for CIMB's overall wholesale banking operation, which contributed about half of the group PBT. Corporate banking (26% of PBT) recorded +10% loan growth and +7.8% PBT growth, loan volumes primarily driven out of Malaysia and Singapore. Treasury & Markets (20% of PBT) had a soft 2013, PBT down 21%yoy. But the Investment Bank (9% of PBT) had the sharpest drop (close to -34%yoy) coming off the back of a strong 2012 laden with "jumbo" deals.

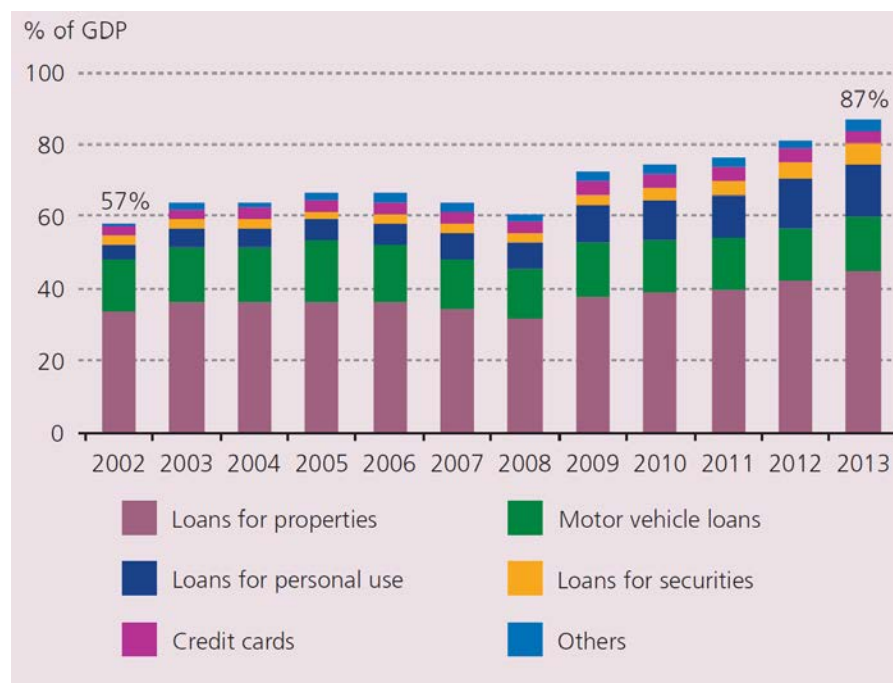
The 2013 IB result excluded the acquisition of RBS Asia Investment Bank (it will be included from 1Q14 onwards). Having faced some delays in integration, by July 2013 CIMB-cum-RBS had a full Asia Pacific ex-Japan equities footprint covering 12 markets (including 3 JVs). Early ECM successes of the enlarged platform were already evident in 4Q13, with deals in Hong Kong, Taiwan and Australia. Getting RBS and the investment bank "right" could be an important driver for 2014 and beyond. For 2013 the ex-RBS platform made a loss of just over RM300m (core loss closer to RM200m excluding one-time start-up costs). Mgmt. remains hopeful that the ex-RBS business should break even in 2014; deal pipeline indications are strong, but execution as always are markets dependent.

Growth Spread Beyond Klang Valley Core?

Overview: As a country spanning 330,000 sq km divided into 13 states and 3 Federal territories, the geographic distribution of Malaysia's growth is rather uneven, with economic activity still heavily concentrated in the Selangor-Kuala Lumpur-Putrajaya corridor in the Klang Valley. This core region accounts for a quarter of the country's 29.6m population and 36% of national GDP, and as importantly contributed more than half of economic growth during the period 2006-2012. Outside of this central growth core, it appears that Johor (integration with Singapore) and Penang (focus on export led growth) have the clearest growth stories. Regional development beyond these more obvious areas could receive greater political urgency, including the North, East Coast economic corridors as well as development in both Sarawak (renewal energy) and Sabah. But the laggard states suffer from underperformance partly due to their relative isolation from major shipping routes, which arguably more than offsets the benefit of lower labour costs in attracting more investment.

Banks impact: National data citing high household debt levels, and as importantly the sharp rise in household debt over the past 5 years, may suggest that without a wider dispersion of Malaysia's economic growth to new/laggard regions beyond the traditional central core, the ability for domestic retail/consumer banking to continue even modest levels of growth could be compromised. We expect consumer loan growth to moderate in 2014, given recent BNM cooling measures, plus likely rising consumer debt service burden as a consequence of further fiscal rationalization (fuel hikes, electricity tariff rebalancing, and by 2015 GST).

Figure 37. Malaysia — Composition of Household Debt

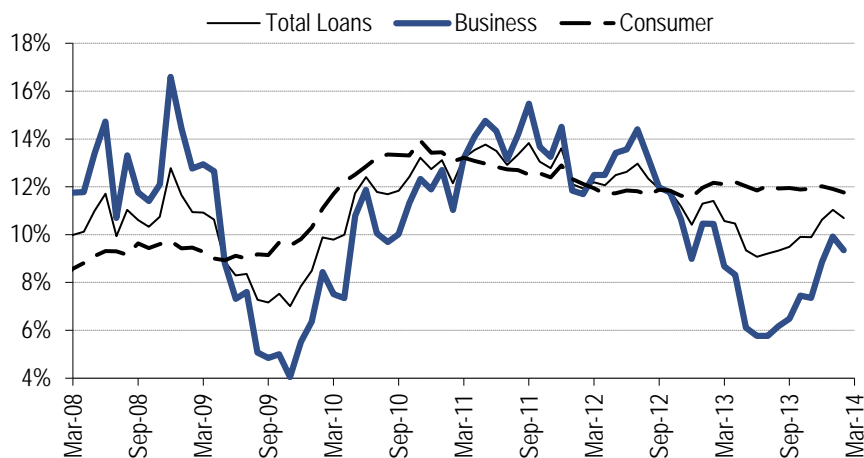


Source: Bank Negara Malaysia Annual Report 2013

But fundamentally we view that there remains clear support for continued consumer loan growth, especially in mortgages (and to a lesser extent auto loans), driven by Malaysia's relatively favourable demographics and continued urbanization. We view this as valid even if Malaysia's economic growth (as in past years) remains largely centered on the Klang Valley core. However, banks will need to be more selective in an expected rising rate environment to reduce asset quality concerns.

Although they are our less preferred segment of the banking space, there remain sustainable top line growth drivers for Malaysia's pure domestic retail banks (Public, Hong Leong Bank, AMMB, AFG). We however temper this by flagging that ongoing NIM pressure is a key biggest concern as it erodes NII growth.

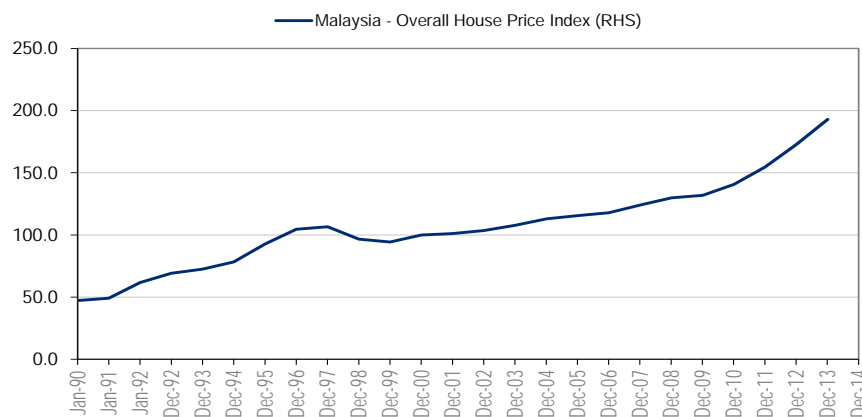
Figure 38. Malaysia System Loan Growth — Consumer vs Business (Non-Consumer)



Source: Citi Research

Mortgage outlook — why fundamentals remain supportive

Figure 39. Malaysia Housing Price Index (1990 to 2013)



Source: NAPIC, Citi Research

Construction starts should support cyclical mortgage trends even if property prices soften

While there is growing evidence that Malaysia property prices are likely peaking and potentially softening going forward, aside perhaps for more speculative segments it does not necessarily suggest a rapid slowdown in mortgage growth will follow.

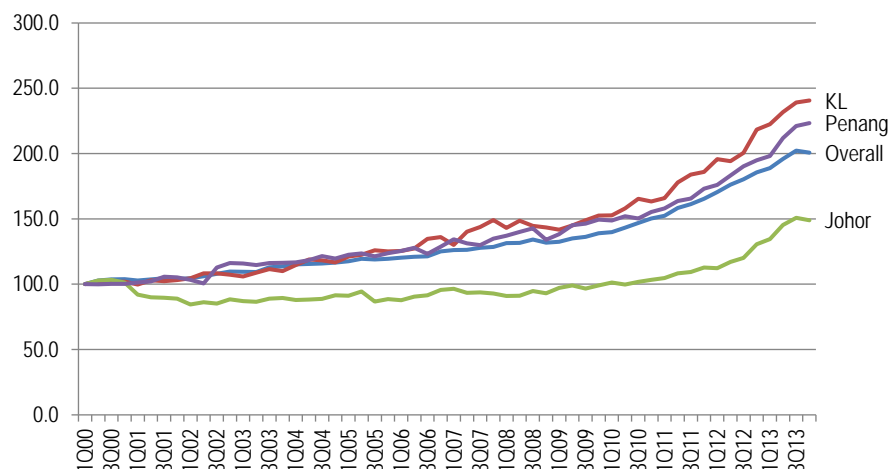
In the physical market, BNM's property measures are arguably already starting to have some impact, with the number of housing transactions falling (especially in the secondary market). The implementation of higher RPGT from Jan 2014 also has had at least a temporary impact on new mortgage applications (arguably in part because there was a jump in 4Q13 applications ahead of the RPGT change).

At the national Malaysia level, property prices have risen over +40% from 1Q 2009 or 9% CAGR.

Over the same period the regional indices have risen for KL >60%, Selangor (proxy for Klang Valley ex-central KL) >50%, Johor (proxy for Iskandar) >35% and Penang close to +50%.

But prices are already starting to stabilize.

Figure 40. Malaysia Property Price Indices by Key Region



Source: NAPIC, Citi Research

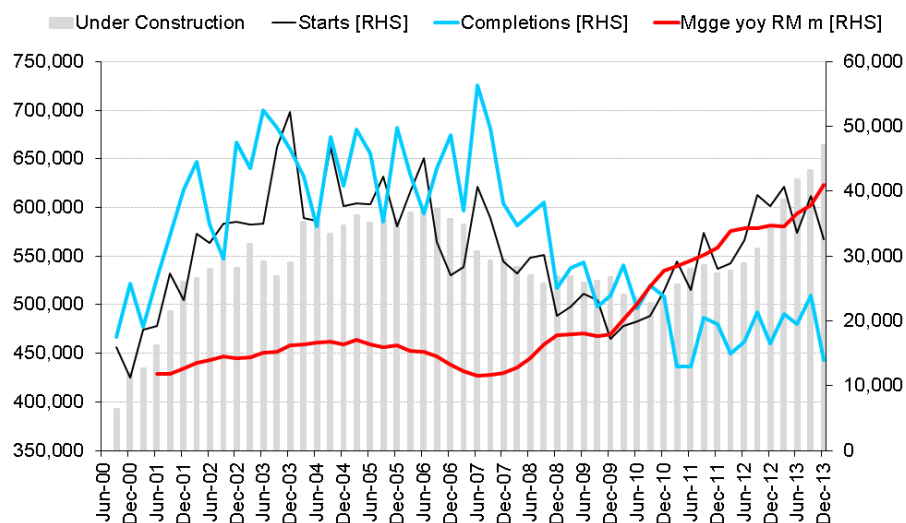
From a trends perspective, mortgage growth in the past 2 years has been largely supported by the sharp rise in **value per housing unit**. National property price indices suggest that average house prices have enjoyed strong double-digit growth in the past 2 years, with KL, Johor and Selangor even peaking in the +15-20% price increase range. But even as value per housing unit peaks or even softens, the volume effect should kick in to continue to drive mortgage volumes.

By regulation developer must complete a landed development within 2 years of launch (non-landed 3 years), thus incoming supply gives some forward guidance to property completions, which in turn lifts mortgage drawdowns.

For the last 2 years quarterly property completions have been at low levels of 15-20k, compared to a peak of 45-50k quarterly during the mid-2000s.

Given the natural lag of 2+ years between housing starts and completions we expect annual completions to rise sharply from the current low levels of about 15-20k, perhaps progressing back to historic levels of over 40k, which in turn will drive the draw-down in mortgage facilities.

Figure 41. Rising Construction Starts Bodes Well for Mortgage Growth

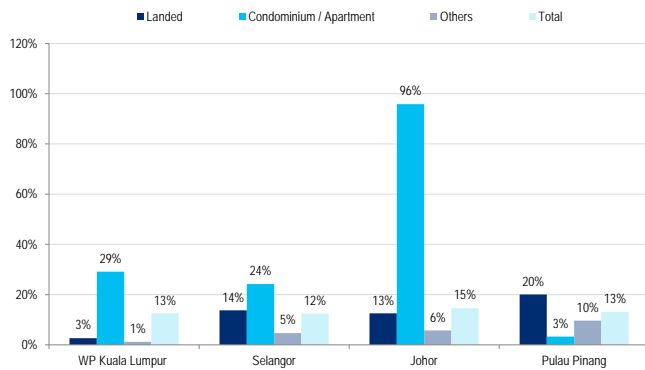


Source: NAPIC, Citi Research

A physical property demand-supply analysis suggests that property prices should flatten out over the next 2 years, due to the rapid increase of units under construction, which according to official govt. data is in excess of 650,000 units as of Dec 2013, or about 14% of the existing stock (4.7m units). Compare this to total population growth of about 2.6m in the past 6 years to 29.7m by 2013, or approximately 430k annually, which in turn implies c.70-80k units of annual demand based on natural population growth.

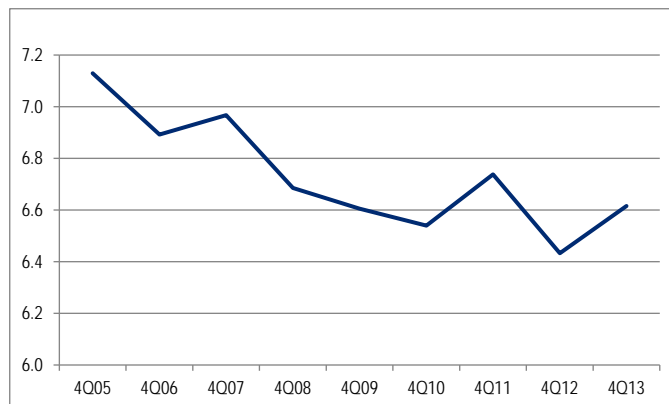
However, taking this analysis one level down, it would appear that much of the excess supply is skewed to the condominium segment (notably Johor and also Kuala Lumpur), while landed seems relatively in balance.

Figure 42. Incoming Supply as % of Existing Stock



Source: NAPIC, Citi Research

Figure 43. Ratio of Population to Housing Supply

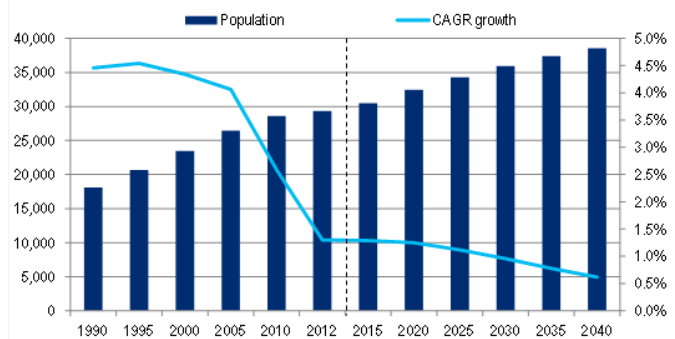


Source: Dept of Statistics, NAPIC, Citi Research

Secular mortgage demand supported by demographics/urbanization

Figure 44. Projected Population Growth to 2040

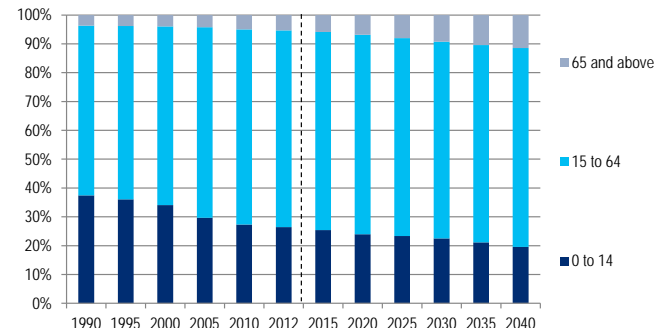
Malaysia - Population and CAGR Growth (1990 to 2040)



Source: Department of Statistics Malaysia

Figure 45. Population Profile by Age Group to 2040

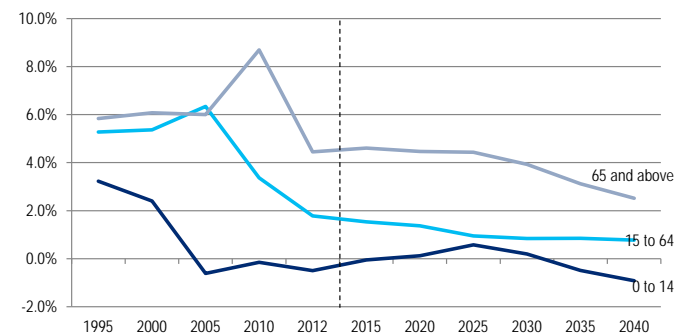
Population Profile (By Age Group) - 1990 to 2040



Source: Department of Statistics Malaysia

Figure 46. Population Growth Profile by Age Group to 2040

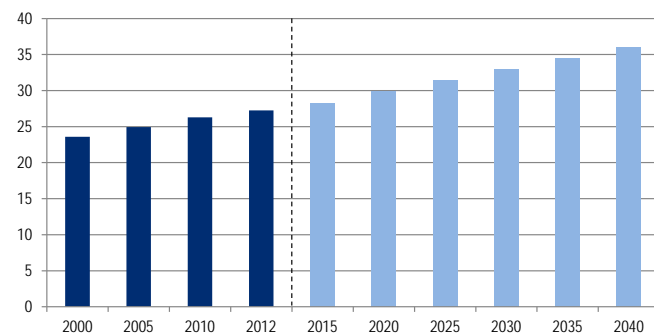
Population Profile (By Age Group) - CAGR Growth



mSource: Department of Statistics Malaysia

Figure 47. Population Median Age to 2040

Median Age - 2000 to 2040

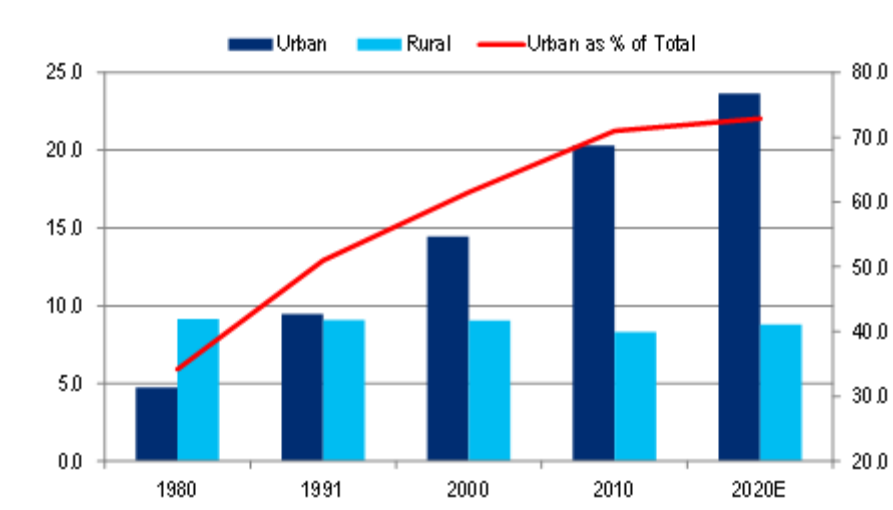


Source: Department of Statistics Malaysia

Beyond the current property cycle, long range population studies carried out by Malaysia's Department of Statistics suggest still-favourable demographics for longer term housing demand and hence mortgage growth. While overall population growth is expected to slow, the expected growth of the 15-64 years age group bodes well for housing demand.

And even if Malaysia's economic growth remains concentrated into the traditional Selangor-KL-Putrajaya core (plus Penang and Johor), housing demand will benefit from the ongoing trend of urbanization.

Figure 48. Urban Population (as % of Total)



Source: Department of Statistic, Ministry of Urban Development and Scared Area Development, Citi Research

Figure 49. Population to Households Ratio — Malaysia

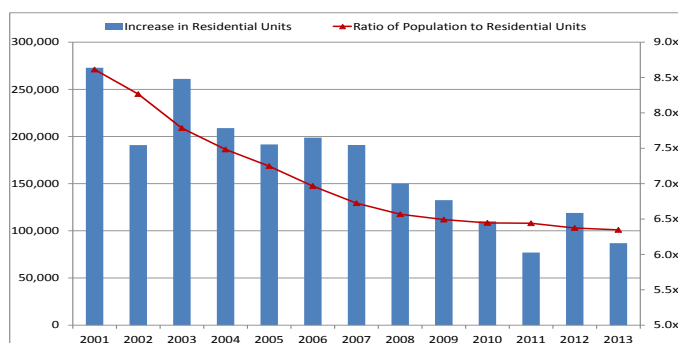


Figure 50. Population to Households Ratio — Kuala Lumpur

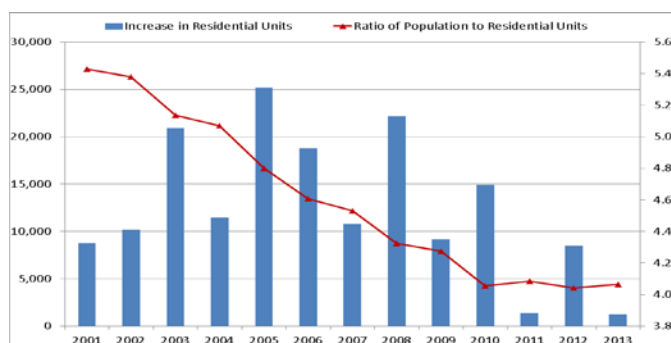


Figure 51. Population to Households Ratio — Selangor (Klang Valley proxy)

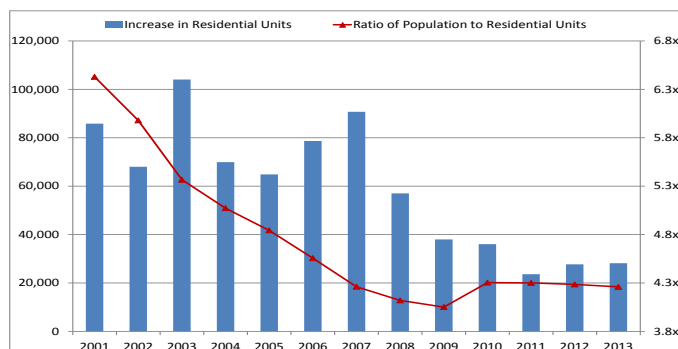
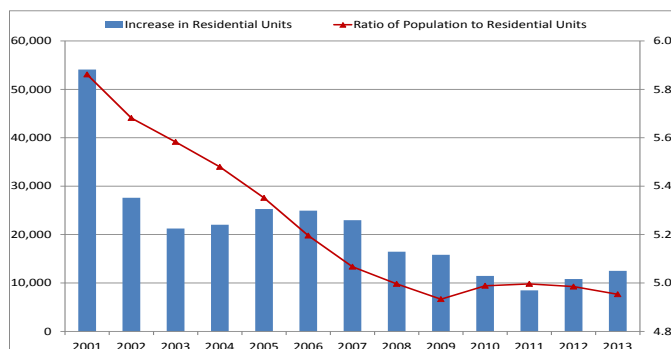


Figure 52. Population to Households Ratio Trend — Johor (Iskandar proxy)



Source: National property information centre, Citi Research

Appendix A-1

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