Transcript of DBS first-quarter 2018 results conference call for buy and sell sides, 30 April 2018

Michael Sia Everybody welcome to our first-quarter call for the buy and sell sides. We've gone through the briefing at the media session just now, so we'll go straight to Q&A.

Anand Swaminathan (BAML) I just have a question on the wealth management top line contribution which has been growing at very rapid pace for the last few years. How do we think about it in the context of very conducive market conditions? Do you break it down into a kind of fee income stream-driven and then there is a market beta element? What could happen to this top line item if the market is down 10% for a couple of quarters or very weak risk sentiment?

Piyush Gupta There's an element of that wealth business which is positively correlated to markets. We've seen in the past that if the markets really suffer, that income stream slows, and that's because a lot of our clients' trading activity does come down.

But the underlying, both in terms of our customer base and the extent of activity we're doing with them, is fairly broad-based and robust. And the number of products we sell to them is also quite diversified.

The wealth business includes the bancassurance business, unit trusts and treasury products – the whole range of underlying activities. And we do therefore have some in-built shock absorbers; there're some pluses and minuses if something goes slow or something picks up.

The other positive we have in the business is that we continue to get improved productivity at an RM level and from the ANZ acquisition. When we acquired the business, its average RM productivity was about half the DBS RM productivity. And, with the new client base and the better DBS platform, we are able to raise productivity. So, that's another consistent driver of growth.

Anand Swaminathan Are there any other assets you are still interested in or the big assets have already been bought and you want to just focus on organic [growth] going forward?

Piyush Gupta We've always said that we're quite happy to look at bolt-on acquisitions in the wealth management and private banking space, but I don't think that there're many of those [big asset acquisitions] available anymore.

Aakash Rawat (UBS) Congratulations on a great result. My question is that while investors and all of us are starting to see the benefits of the structural ROE improvement, there're increasingly more worries on the impact of rising rates on your exposures in Hong Kong in particular, not so much in Singapore I would say at the moment. Do you think this is a fair concern and is there any colour that you could share on how to think about this?

Piyush Gupta Our large corporate client base is robust. Our client selection is good at the top end of the market. The rates are coming off historical lows. The cash flows of these client businesses are good. So, I don't expect any material impact on the top end of the market.

The second in the corporate space is the SME sector, which generally tends to be more vulnerable to rising interest rates. In our case, a large part of our SME business does tend to be secured and security values are good. Now, rates are coming off historic lows and so even if they go up a percentage point, relative to historic levels, they're not very high. And there is a degree of resiliency in that SME sector. So, I expect [delinquencies] to go up [when rates go up], but I don't think it will fall off a cliff.

In the consumer space, the largest part of its portfolio [of around two-thirds] is the mortgage book. For the mortgage book, we have traditionally worked with a 3.5% interest rate assumption when we calculate the debt-burden ratio. Rates are far from the 3.5% level and as with the corporate [clients], I do expect some delinquencies but it will not be material. If you look at our mortgage performance, the bulk of the business is from Singapore. If you look at the performance through the ups and downs historically, [there hasn't been] materially huge credit costs in rising interest rate environments, so there's no reason to expect [it] now.

The fourth piece is the unsecured consumer book. It used to be smaller for us but with the acquisition of ANZ, it's become a little bit bigger. We will see increased delinquencies and cost of credit in that book as rates go up [although] that's built into the long-term average cost of doing business in that sector.

Now, when we put all of that together, I don't think we'll get out of kilter with the [guidance of through-the-cycle] provisions of roughly 25 to 27 basis points.

At the same, the flip to that is that we make out extremely well on the top line when rates go up. We've already indicated that every basis point increase in rates in SGD, HKD and dollar book [combined] gives us about eight million dollars of income. So, if you assume a 100 basis point increase in rates, full year on average, that's $800 million of income. I think that impact will be much, much more material than any impact on the cost of credit line.

Aakash Rawat A couple more questions from me. Firstly, on the customer deposit cost which rose by roughly ten basis points, quarter-on-quarter. Is this kind of pick-up to be expected in future or was there something specifically going on in this quarter, because of this you saw this jump?

The next question is credit costs are up 20 basis points for this quarter. You're still guiding for 25 to 27, I think, for the whole year, I guess. Was this quarter particularly flattered by some recoveries for the Hong Kong/China? Specific provisions are very low. Were there any specific recoveries and, if so, then which sectors was that?

And then, again, on wealth management. So, wealth management you had something like $331 million for this quarter, which is roughly 37% higher compared to your quarterly average of last year. Is it possible for you to break down this 37% into how much is structural and how much is the market environment cyclical, so we have a better way to forecast this for the rest of the year depending on market conditions?

And, just one more question. Is your loan growth guidance still 8% for the rest of the year or do you think that's a bit too light and it might be higher than that?

Piyush Gupta The first question, if you look at our [US and Hong Kong] dollar book, while we do have a fair amount of CASA, certainly outside in Hong Kong for example, we still have a fair amount of fixed deposits. So when LIBOR or HIBOR goes up, our funding costs in deposits go up as well. But it's counterbalanced because at the same time we charge higher on the loan side.

So, the important thing is does your loan yield go up higher than your cost of FDs – and that is actually the case. Loan yields in the dollar book were up by about 20 to 30 basis points, which are much higher than the [increase in] cost of fixed deposits.

We did have some recoveries in Hong Kong/China. They were not material and were broad-based. There were some unsecured loans, there were some SME sector recoveries. I do think we might see more recoveries in the course of the year, including from some of the offshore marine cases.

The reason we're still leaving the [credit cost] guidance of 25 to 27 basis points unchanged is because of the potential impact of higher interest rates on the unsecured consumer book and SME book. However, from an industry standpoint, we are not seeing any material downside impact as we speak.

At the [media briefing conference earlier] I said where ROE winds up at the end of the year is a function of where the cost of credit number winds up at. My line of sight is I'm not seeing too much damage, but I'm also not sure what the overall impact of the rising interest rates might be in a couple of the sectors. So, we'll watch and see.

On wealth management, some of the growth is the ANZ. We added ANZ in Singapore and Hong Kong in the middle of last year, and so some of the pick-up you see reflects the addition of the ANZ business, as well as the improved productivity [from it].

Our structural growth, which is based on AUM growth, is in the mid-teens. Now, how much more money you make also depends on the markets. I pointed out [earlier that when] the markets are good and positive, customers trade a lot more, so you actually can make a lot more money. This quarter, everything worked. Relative to a year ago, our AUMs are up, we have more productivity and customers' activity was [higher], so it was fairly broad-based.

Finally, on loan growth, we grew 2% in the quarter on loan growth and we'll probably do roughly the same rate every quarter for the rest of the year which would give you 8% loan growth. I think, also, in a rising interest rate environment it's not clear to me whether loan demand slows down in the later part of the year or not. So, I think 8% guidance is probably fairly accurate at this point.

Melissa Kuang (Goldman Sachs) Just two questions. Firstly, on the margins. Looking at your Hong Kong margins, it went up quite strongly quarter-on-quarter. I just wanted to get a sense of the Singapore side, if you can give a guidance, whether it was fairly similar to Hong Kong or much, much lower.

Also, in terms of just following up on the question before about deposit cost. Yes, the FD rates have gone up, but we have seen SIBOR move quite a lot since, but we haven't seen saving rates actually go up. Do you think at some point you might see some pressure of raising the saving rates, as well?

Lastly, in terms of AUM, really strong growth. I just wanted to understand, in terms of regions, where you're seeing the growth coming in and do you think you can sustain such high AUM growth going forward. Thank you.

Piyush Gupta Actually, our margin increase was quite broad-based.

If you look at our five basis points we reported, about 2.2 to 2.3 basis points of that came from the Singapore book. Just a tad below 2.0 basis points – 1.6-1.7 – came from the US dollar and the Hong Kong book. And we got some lift in Indonesia as well because we added on a higher margin portfolio from ANZ. So, we got a tad [above] 1.0 from there.

If you look at the last couple of weeks, the flow-through from USD LIBOR into SOR and SIBOR has really picked up a lot. Assuming that the flow-through stays, you should expect to see improved margin impact in Singapore. In Hong Kong, the HIBOR flow-through has been somewhat low. It is improving but not as much as Singapore.

And at some stage, savings rates will have to be guided up. But when you go back the last ten years and [look at] when rates were much higher, [savings rates in Singapore] go up, [but] they're relatively inelastic. And, so, a large part of the increase [in interest rates] does flow-through to the bottom line. When we estimate the roughly eight million dollars [growth in income per one basis point increase in rates], we already [built in] some lift in the savings account rates over time.

AUM is actually very broad-based. We continue to raise money from North Asia, the region, and internationally. Our international operations cover the Middle East and Europe. Those have been kicking in quite nicely as well.

Yeo Zhi Bin (CIMB) Just wondering whether you could identify the Hong Kong property which was disposed and maybe some colour behind it.

Piyush Gupta We sold one floor of the building which we occupy. As you know, there was a general bid for the building. Our philosophy is, particularly in Singapore and Hong Kong which are our big centres, we like to own our [premises] because it allows us to manage cost in the long term.

The property is held at book value, original equity cost. It's not a drag on equity. Now, what happens is that if we can create efficiency in our operations, which is what we were able to do in Hong Kong, partly through digitising a large part of our paper and our operations, then we can reduce our footprint. So, we were able to save one floor in Hong Kong and restack all our people in one floor fewer.

Krishna Guha (Jefferies) Congratulations on a good set of numbers. A few questions from my side. First is on your liquidity coverage ratio trend. If you can give some colour of what is the cause behind the gradual reduction in that LCR ratio despite pretty strong growth in deposits, as well as your LDR kind of staying stable. Second question is on your duration of your investment portfolio. If you can share some colour as to what your broad thinking is. The third question is related to the prior question, that given you are digitising the whole organisation, will your footprint also be reduced in Singapore. I believe, now, you do not own that building, but what are your thoughts on that. And, finally, a request on your additional Tier 1 dividends that you give. Can you put them upfront in your long form as to how much is the AT1 dividend for the quarter?

Chng Sok Hui On the LCR coverage, this quarter the average is 125%. This is really a ratio of high quality liquid assets divided by the projected outflow under a stress scenario. The number does fluctuate from time to time.

Krishna Guha Because it has come down from 150%, probably, four or five quarters ago, which was the peak, and the trend has been just in one direction, so that's the broader question.

Chng Sok Hui The question is what level should it be at. Typically, the target level would be around 110%. That would be the optimal coverage ratio that you should expect. Something like 150% is probably excessive. But from time to time, you may see higher numbers.

Piyush Gupta [On] your second question on the duration of the book, some time ago we basically figured that there's value in the belly of the curve, so we actually kept duration in the three to five-year bucket, that's where the bulk of our durations were. Because of the expectation and rising interest rates, we've not been very long, but we have been in that part of the curve. I think that's where the bulk of duration is.

Chng Sok Hui You can look at the disclosure we put out this morning on slide 26. You find the bulk of [duration] is really less than three years. So, out of the total portfolio, of the $20 billion [in government securities], $14 billion are in the less-than-three-years portfolio, so we stay on the shorter duration of the curve.

Piyush Gupta On footprint in Singapore, we're actually rationalising it, but it's mostly to do with the branch distribution. We're changing the format of the branches. We have smaller branches in many locations and so on. On the headquarters building itself, we do own one-third of this building and we have no plans to divest this. As I said, our general philosophy is that, in the long term, owning your premises insulates you from higher rental costs, so we're going to hold on to that.

Krishna Guha On the [dividends paid for] additional Tier 1 securities, I think you do disclose it in the annual report. If you can also disclose it in the quarterly performance summary statement as well?

Chng Sok Hui It's in the Pillar 3 disclosure. With every quarter there is a Pillar 3 disclosure that's posted on the website. If you look at page A-3 [of the disclosure], additional Tier 1 capital instruments as at 31st March is about $3 billion. You can also see on page 26 of the Performance Summary the dividends paid to shareholders in the number under the revenue reserve of $18 million.

Marcus Chua (Nomura) Just two quick questions. The first one is, just now, Piyush mentioned that there might be a writeback or recoveries from offshore marine. In what conditions will DBS start to write back or feel confident in that sector? And, the second is, did DBS disclose the stage one and stage two loans.

Piyush Gupta We write back in two circumstances. One is if we've written off the loan and if we have collateral, we sell the collateral at better values than we've marked it down to. That's a straightforward writeback because we recovered more for the loan.

The other is if, if after restructuring, the company goes back into performing status. Now, when that happens, we don't write back immediately. We wait for a period of time to make sure the company is indeed able to perform as we expect. In those cases, it's unlikely that we'll record a write back any time soon. But those are the conditions under which you might see writebacks and recoveries.

Chng Sok Hui On stage one and stage two [loans], when we issued the Performance Summary this quarter, we also appended an appendix that relates to the transition to the new accounting standard. [In] the appendix page seven, you can see the provisions on stage one and stage two [loans].

So, if you look at the appendix, page seven, you'll find that of the $2.5 billion that we said is the expected credit loss as the beginning of the year, stage one has got $887 million and stage two has $1.6 billion. So, in other words, we have about two-thirds of the total expected credit loss under stage two.

Marcus Chua Thank you. On the overall stage two loans, is there a categorisation for that?

Chng Sok Hui Stage two loans are about 6% of the overall base but it carries about two-thirds of the total ECL. In other words, what you should take away is that we are very conservative in our estimate of stage two expected credit losses, so that when you eventually do move into stage three, you will not see such a big impact on specific provision charge.

Harsh Modi (JP Morgan) Piyush, just on the provisions, your guidance, do you see downside risk this year or think the writebacks get pushed to next year? And, in downside, does that mean that specific provisions can come to the higher mid-teens kind of number this year [instead of 20 basis points]?

Piyush Gupta It's hard to say because I'm still not entirely sure what the interest rate impact might be on some of the portfolios and that's why we are holding the guidance. If the interest rate impact on the unsecured consumer and SME is really benign, then we could do much better than the 20 basis points. But we are holding the guidance with the expectation that there will be a pick-up in cost of credit on account of the interest rate increases, it's just very hard to fathom how much that might be.

Harsh Modi Right. In that, are you seeing any early warning system, anything which is giving you any indication that there is stress building up in some parts of the book, either if I look at a geography sector split, anything which is starting to flash amber, I guess?

Piyush Gupta Not yet. But, also, as part of the book, what we acquired from ANZ, in Indonesia, we just had on our books since mid-Feb, so it's very early to form a view on that. ANZ Taiwan was also only for the last four of five months. So, both acquired books we've got to watch and make sure that they behave okay. The rest of our own business is actually not showing any amber signals yet, but I cannot believe that if rates goes up you won't see it; you will see some impact of that, it's just hard to determine when that comes through and what that impact is.

Harsh Modi Okay, that's fair. And, the second one on the cost-income ratio. Are we still holding the line on 43% or do you think 42% is something you are comfortable guiding and what are the risks around that number coming lower in the course of the year?

Piyush Gupta Unlikely. Remember, this first quarter is flattered because of that property disposal in Hong Kong. So, if you exclude the property, then the number is closer to 42.6%.

Also, we are seeing two things; one, there is an opportunity to continue to invest, and we are doing that. So, we are adding to our wealth management RMs, insurance RMs. As you know, these RMs pay back very quickly, but you have to continue to invest in some of the businesses. The expectation is that we will continue to do that through the course of this year. So, no, we're not looking at changing our guidance for now.

Harsh Modi And, if I could just gauge your confidence on the revenue with the cost line. Are you a bit worried about the pass-through of NIMs and fee? Is that a high risk? What do you say that if you do get that top line you would use the opportunity of that leeway to just ramp up [investments] as you were talking about last quarter, or in other parts of the business.

Piyush Gupta The reason I am managing the cost-income ratio is because I think it does give us the opportunity to make smart investments at a time when we have momentum in the top line. And, those investments are not just in headcount but also in continued transformation activities. And if we do [make additional investments] we will be obviously judicious.

Nick Lord (Morgan Stanley) Quick question, just on payments. I notice that your card income held up very well this quarter, and I guess some of that has to do with acquisitions, and you obviously made comments at the media briefing about PayLah!

Do you have a sense of what you market share of payments is in Singapore and whether that's moving up because of the things you're doing on PayLah!? And, do you have a sense of what's happening to your credit card market share?

Piyush Gupta We have a sense. PayNow, for example, we know, because that's easily tracked, and we have 54% share of the PayNow volumes in Singapore; that's a hard number because it comes from the central data.

On credit cards, both receivables and billings market share is continuing to inch up. We're close to about a 25% on share on cards, but that's credit cards. We also have a massive debit card base. We have the biggest debit card portfolio.

And, then the other types of payments, there is no market data. What I do know is that our own volumes are picking up very, very strongly. Our month-on-month growth is very strong and, more than that, anecdotally the use cases are beginning to diversify.

So today, we are seeing about 15,000 transactions a week in the Comfort taxis using PayLah! We're seeing 150,000 transactions a week in all the campuses and universities around Singapore using PayLah! We're seeing about 30,000 transactions on hawker stalls. So, it's actually beginning to be very diversified and growing very nicely.

Diksha Gera (Bloomberg) A couple of questions from me. One, I wanted to get your thoughts around oil, $75, and, then, where are you thinking? Could it result in more stress or do you think the shale gas is a kind of common place, so you're not too worried about that? And, the second one is on the Hong Kong CASA ratio. The ratio went up five percentage points. What is driving that? Third, China opening up news flow; what does it mean for you and how much would you read into it? And, the last one is on the data privacy issue with Facebook. Do you anticipate some spillover for the banking sector, particularly in Singapore?

Piyush Gupta On oil your guess is as good as mine, frankly. I think there are two things. I read somewhere recently that the shale guys are now profitable at as low as $20 to $25. So the shale is in constant production and that will have a bearing.

I think the bigger impact, right now, is geopolitics, so what happens with Iran and what Trump does on May 12, if the sanctions go up. If Iran's production gets impacted, then that obviously will have an impact on overall prices.

As a general rule, higher oil prices are not good for emerging markets and, therefore, I think, at this level, $75 is already very toppish for countries like India; it's going to start impacting their trade balance. If it gets much higher than that, you start seeing some negative impact.

Obviously, more parochially for us, higher oil prices mean that many of the oil and gas support sector might start benefiting. They're beginning to see some improvement in the margins, but it's very, very small, but if oil prices stay up or go up then, hopefully, their margins will start improving and that might actually have some impact on the previous question on what kind of recovery you might expect from the sector.

On the Hong Kong CASA, the increase has been secular. So, in the past few years, we've been able to [double] our CASA mix in Hong Kong to 63%. And, we showcased that a few quarters ago, pointing out that the real growth is coming from our cash management business. The GTS cash management business is picking up really well and we are getting a whole range of operating account balances, both from Hong Kong and multinational Chinese companies in Hong Kong. So, that's actually been robust and that continues to help us. Partly, the growth has been from improved CASA in the SME space. So, we've been able to use the digital banking capabilities and the instant account opening to improve our CASA positions in the SME segment, so that's been quite helpful.

Your question on China, if I understood rightly, this is with China opening up, what is the impact of that on DBS. You saw the soundbites in the last two or three days that people want to wait and see what that opening up really means before reacting to it. But, yes, as they continue to open up the market, it has actually two impacts.

One, it might allow us to do certain activities that we can't do today. As you know, China requires licensing for almost everything. It's not like other places where you have a banking licence means you can automatically do 100 things. Here, within that licence, you still have go and re-apply for licence for everything you want to do. And, as they open that up, that might simplify our ability to [carry out activities]; bond markets, in particular, is a good case in point.

The second thing, however, is the hope that if they open up and they really follow through on liberalising interest rates, the window guidance on deposit interest rates, that might allow us to improve our local currency funding. If we can do that, then that obviously gives us the capacity to grow our book a bit better and stronger.

The last thing was on data privacy and Facebook. I think this should be a big issue. I think it will be a big issue and not just on the back of Facebook, everything over the next three-five years. But, I think the net outcomes of this are relatively unclear.

How much does it result in regulations saying you cannot use or share data versus how much it results in regulation saying that you've got to open up and let everybody use data? So, frankly, it can go either way.

In Singapore, there is a big effort to look at both sides of the equation. At the government level, people are focused on how we can actually use data for national productivity and national use. At the same time, we are also looking, at the government level, at how you can create the right rules around what are appropriate and suitable uses of data and how do control that. So, I think there will be a lot of work in this area in the next three or four years, but the net outcomes of that are not entirely clear yet.

Diksha Gera In China are there any businesses that intrigue you, given that the process could speed up? And, second, on the Hong Kong cash management and digital banking side, how do you stack up again HSBC and the local banks? What are your strengths versus how they're doing?

Piyush Gupta I think the big story in China is going to be the continued opening up on the capital account and, therefore, a range of business in that space, whether it's to do with custody business, which is a support activity, or to do a bond market business, which is international flows going into Hong Kong, or it is to do with Chinese money leaving China for international investments. I think each of these business opportunities is quite interesting.

And, in some cases, you can't do that today because you need to go and get a specific licence to do something or the other. If they liberalise and make that easier, that will certainly be beneficial.

In terms of our own capabilities, our cash management capabilities in China now are on par with any of the other boys. Again, we use national clearing systems and domestic arrangements to do that. However, the large part of our opportunity is outside China. The bulk of the opportunity we see is the Chinese companies with the international cash management needs. And, obviously, in the international space, our capabilities are not only on par, in some cases we think we are best in class, particularly where we've been able to use digital and API connectivity to offer solutions to large companies which many of our competitors don't.

Paul Chew (Phillip Securities) Just three questions. I notice your loans growth in SGD in the first quarter was around 10%, but looking at the industry data to February, it was about 5%. I was just wondering, was there some surge in March or was it just market share?

My second question would be just on the status of the oil and gas vessels for the borrowers that defaulted. I was just wondering who takes ownership of these vessels and are these still operating or are they stacked?

And, my last question, in wealth management, what parts of the business can pick up when you see market volatility rise?

Chng Sok Hui I don't readily have the data on March versus February but when we look at the results this morning published by the MAS, we saw an uptick in the market share of both on consumer as well as on the business loans.

Piyush Gupta On the vessels, in some cases, we have taken charge of the vessels and we are driving the process of what to do with them. When they are cold stacked, in most cases we put working capital in to make sure they are running so it doesn't deplete value. But that's a handful.

In other cases, the appointed judicial magistrate takes charge of the vessels and then they use the same thing on how much does it cost to keep the vessel cold stacked. And, in some cases, the original promoter/owner is still running the vessels, but at the same time trying to put them to market and trying to find a market for them. So, all of the three things are happening.

In a couple of the negotiations and discussions we are in, we are getting fairly interesting bids, so I'm somewhat optimistic that the higher oil price might result in some improvement in the collateral values in the course of the year.

And, finally, your wealth management question. Actually, it's across the board. It depends on which part of the market is hardest. If equities are doing well, then clients tend to do a lot more equity-related trades. If the Treasury market, FX markets, if people have view on the currency, then they wind up doing a lot more dual-currency-linked trades.

So, some percentage of the portfolio for most Asian wealth clients tends to be portfolios that they bring to go in the market and trade with, and that's quite broad-based. It depends on the market situation.

Tan Su Shan When volatility goes up, obviously, the risk premium goes up, and so customers don't want to be long-only. So, in very high volatile times there will be a move towards structured products with lower strikes, and these could be equity-linked or interest rate-linked or CMS structures or FX-linked.

What we are seeing is customers are looking at yield and premium, looking to sell volatility in these high-volatility environments. But they're also cautious and they're also diversifying. So you do see customers who want to take some profits in the equity market and stay in cash, others who want to invest in more high-yielding like REITs or high-yielding bond funds, a diversified bond fund.

We are seeing customers take a more disciplined asset allocation approach, which is not a bad thing. In the past, when the markets were good, there were a lot of a la carte trades. Now, it's a lot more disciplined, it's a lot more diversified, and it's a lot more risk-adjusted.

Michael Sia Okay. Thank you all. We will see you next quarter.