<u>Transcript of DBS second-quarter 2017 results media briefing, 4 August 2017</u>

Edna Koh This morning we announced record net profits of $2.35 billion of the first half, up 4% from a year ago, and total income was also at a new high. For the second quarter, net profit rose 8%. The board declared a higher dividend for the first half. And to tell us more, we have our CEO, Piyush Gupta, and our CFO, Chng Sok Hui. So without further ado, Sok Hui.

Chng Sok Hui Good morning, everyone, and thank you for joining us for our second-quarter results briefing.

<u>Highlights.</u> We achieved record earnings of $2.35 billion for the first half, up 4% from a year ago. Total income reached a half-year high of $5.81 billion, as broad-based loan growth and record fee income offset the impact of a lower net interest margin and weaker trading performance. Expenses were 1% lower at $2.52 billion as digitisation and productivity initiatives resulted in a one percentage point improvement in the cost-income ratio to 43%. Total allowances declined 6% to $504 million as NPA formation was lower.

For the second quarter, net profit rose 8% from a year ago to $1.14 billion. Total income of $2.92 billion was just shy of a quarterly high. Business momentum was heathy, as loans grew 2% over the quarter and the fee income trends were sustained. Total allowances fell 17% to $304 million from a high year-ago base.

The balance sheet continues to be sound. New NPA formation in the first and second quarters was lower than the levels in the preceding three quarters. The amount of non-performing assets was little changed from the previous quarter, as non-performing loan formation was offset by write-offs and recoveries. Allowance coverage was at 100% and at 234% when collateral was considered. Our capital and liquidity ratios remained well above regulatory requirements, with the final Common Equity Tier-1 ratio at 14.0% and the liquidity coverage ratio at 150%.

The board declared a 10% increase in dividends to 33 cents per share. The increase is consistent with our policy of paying progressive dividends in line with earnings while maintaining prudent capital levels to meet impending regulatory changes and long-term growth requirements.

<u>First half compared to a year ago.</u> For the first half, net profits of $2.35 billion rose 4% or $96 million from a year ago.

Net interest income rose 1% or $53 million to $3.72 billion. Loans increased 6% or $18 billion to $303 billion from broad-based growth in trade, corporate, consumer and Singapore housing loans. The increase in loan volumes was offset by a 12 basis point decline in net interest margin to 1.74% due to softer Singapore dollar interest rates.

Net fee income rose 8% or $99 million to $1.30 billion, with the increase coming almost entirely from wealth management fees. Fees from cards and transaction services were also higher. The increases were partially offset by lower investment fees as we had several large equity underwriting transactions in 2016. Other non-interest income fell 14% or $126 million to $790 million from lower trading gains and a non-recurring gain of $38 million a year ago.

Expenses declined 1% or $34 million to $2.52 billion from ongoing digitalisation and productivity initiatives. Profit before allowances increased 2% to $3.29 billion. Total allowances of $504 million were 6% lower than a year ago. Specific allowances declined $260 million in line with lower NPA formation, partially offset by the impact of a $228 million general allowance write-back in the second quarter last year.

<u>Second quarter compared to a year ago.</u> For the second quarter, net profit of $1.14 billion was 8% or $89 million higher than a year ago. Total income of $2.92 billion was a near quarterly high. There was little change year on year as higher net interest income offset the impact of lower trading, investment and fixed-asset gains.

Net interest income rose 3% or $55 million to $1.89 billion as the impact of a 6% loan growth was partially offset by a lower net interest margin, which declined 13 basis points to 1.74% due to softer Singapore dollar interest rates.

Net fee income increased 1% or $8 million to $636 million. A strong increase in annuity fee income streams, led by wealth management, was offset by a halving of investment banking fees from the second quarter of 2016, which had a bumper quarter of new equity listings. Other non-interest income fell 13% or $58 million to $400 million as trading income and gains from investment securities were lower. There had also been gains on fixed assets a year ago.

Expenses fell 1% or $17 million to $1.27 billion. The reduction in expenses contributed to a 1% increase in profit before allowances to $1.66 billion. Specific allowances of $304 million were almost half the amount a year ago. The reduction was partially offset by the impact of the general allowance write-back last year.

<u>Second quarter compared to previous quarter.</u> Compared to the previous quarter, net profit of $1.14 billion was 6% lower. Total income rose 1% or $38 million to $2.92 billion, which was a near quarterly high.

Net interest income of $1.89 billion was 3% or $57 million higher as loans grew 2% from higher corporate, trade and consumer loans. Net interest margin was unchanged at 1.74% as the benefit of higher Singapore dollar interest rates was offset by lower Hong Kong dollar rates.

Fee income of $636 million was 4% or $29 million below the record in the previous quarter. Loan-related and investment banking fees were lower. Other fee income streams, such as wealth management and transaction fees, were healthy and around recent quarterly highs. Other non-interest income of $400 million was 3% or $10 million higher. An improvement in trading income partially offset lower gains on investment securities.

Expenses of $1.27 billion were 2% or $20 million higher. Profit before allowances of $1.66 billion was 1% higher. Specific allowances of $304 million were $104 million higher, bringing first-half allowances to $504 million.

<u>Net interest income.</u> Second-quarter net interest income of $1.89 billion was 3% higher than both the previous quarter and a year ago. For the first half, net interest income was 1% higher at $3.72 billion.

Second-quarter net interest margin was unchanged from the previous quarter at 1.74%. The impact of higher Singapore dollar interest rates was offset by a decline in Hong Kong dollar interbank rates. We expect net interest margin to be slightly higher in the second half of the year as we are seeing more pass-through of higher US Libor rates to Sibor and Sor.

<u>Loans.</u> In constant-currency terms, overall gross loans rose $7 billion or 2% from the previous quarter, and $16 billion or 5% from a year ago to $307 billion. The growth was broad-based.

Consumer loans rose $2 billion or 2% during the quarter and $4 billion or 5% from a year ago. Wealth management loans and Singapore housing loans contributed to the increase in both periods.

Corporate loans grew $4 billion or 2% during the quarter and $7 billion or 4% from a year ago. The increase during the quarter was led by acquisition and real estate financing by Singapore and Hong Kong corporates.

Trade loans grew $3 billion or 7% during the quarter and $5 billion or 13% from a year ago to $43 billion. The increase during the quarter reflects stronger import and export data in recent months.

Our loan pipeline remains healthy and we expect second-half loan growth to be at similar levels to the first half. On top of that, the ANZ integration will add another $8 billion-$9 billion in the second half of 2017.

<u>Liquidity.</u> Deposits rose 1% from the previous quarter and 9% from a year ago in constant-currency terms to $343 billion. About 60% of the growth from a year ago was in current and savings accounts, reflecting the success of our cash management and consumer businesses in growing stable, lower-cost deposits. Other funding rose $2 billion during the quarter to $34 billion from issuances of commercial paper.

Our liquidity ratios remain well above regulatory requirements. The liquidity coverage ratio was at 150% while the net stable funding ratio exceeded the requirement of 100% due in 2018.

<u>Fee income.</u> Second-quarter gross fee income of $731 million was 4% higher than a year ago and 1% below the record in the previous quarter. Investment banking and loan-related fees were lower compared to both periods, muting the healthy performance in other fee income streams.

The $245 million in wealth management fees during the quarter included $23 million of service fees from in-house treasury products now sold on open architecture platforms. Compared to a year ago, the underlying increase was 24%, reflecting franchise growth and more buoyant market conditions.

Card fees of $130 million were higher than a year ago as Singapore and Hong Kong credit card transactions grew. Transaction service fees grew 4% from a year ago to $154 million from increased cash management fees.

Offsetting the growth of these fee activities was a halving of investment banking fees from a year ago, when we had a bumper quarter due to several large transactions. Loan-related fees fell 13% from a year ago and 19% from the previous quarter to $104 million as lower fees were recognised from loan syndication and other loan-related activities.

For the first half, gross fee income was 10% higher at $1.47 billion, as wealth management, card and transaction service fees grew.

<u>Institutional Banking.</u> First-half pre-tax profit for Institutional Banking rose 23% from a year ago to $1.28 billion as allowances declined.

Total income was 1% lower at $2.62 billion. Cash management income grew 28% to $506 million, reflecting steady growth in customers and mandates. The increase was offset by lower contributions from loans, treasury, customer as well as investment banking activities.

Expenses rose 1% to $860 million while profit before allowances declined 3% to $1.76 billion. Allowances fell by one-third to $480 million in line with lower NPL formation in the oil and gas support services sector.

Asset balances rose 7% or $15 billion to $236 billion as both trade and non-trade loans grew. Cash management deposits were 7% higher at $130 billion.

<u>Consumer Banking and Wealth Management.</u> First-half pre-tax profit for Consumer Banking and Wealth Management rose 12% to a new high of $1.00 billion.

Total income grew 10% or $207 million to a record $2.30 billion. Investment product income rose 21% to $684 million from broad-based growth across unit trusts and treasury products. Loan and deposit income grew 6% to $1.29 billion from higher housing loan and deposit volumes, partially offset by lower net interest margin. Card income grew 6% to $293 million in line with increased customer transactions.

Wealth management customer segment income rose 27% to $1.03 billion as assets under management grew 16% to $175 billion. The amount does not include ANZ, which will increase our AUM further when it is integrated from second-half 2017. Income from the retail customer segment declined 1% to $1.27 billion as volume growth was offset by lower net interest margin.

Our market share of Singapore housing loans increased from a year ago, while we continued to have more than 50% of Singapore-dollar savings deposit market share.

Expenses rose 8% to $1.23 billion from increased investments and marketing activities. The cost-income ratio declined one percentage point for Consumer Banking to 54%. Total allowances rose $11 million to $66 million with the increase due to general allowances taken in line with loan growth.

Treasury. First-half treasury customer income fell 5% to $594 million as an increase in income from wealth management customers was more than offset by a decline from corporate customers, mainly due to lower RMB hedging activities. Income from the Treasury Markets business segment, which reflects structuring, market-making and trading activities, fell 23% to $445 million. The weaker results were due to less favourable performance in interest rate activities. Total treasury income amounted to $1.04 billion, 14% below a year ago.

Expenses. First-half expenses fell 1% to $2.52 billion. For the second quarter, expenses were also 1% lower than a year ago at $1.27 billion. The decline marked the fourth consecutive quarter of year-on-year declines, reflecting sustained improvement in operating efficiency from digitalisation and productivity initiatives. Similarly, underlying headcount has been falling gradually over the past few quarters and is more than 2% lower than the start of 2016.

The cost-income ratio improved from 44% a year ago to 43%. We expect the ratio to be around 43% for full-year 2017.

Hong Kong. Hong Kong's first-half net profit rose 24% from a year ago to $457 million. Total income grew 4% to $1.06 billion.

Net interest income was 7% or $44 million higher at $694 million. The impact of higher asset volumes and an improved deposit mix was partially offset by a six basis point decline in net interest margin to 1.74% due to lower Hibor rates.

Fee income rose 29% or $64 million to $283 million from broad-based growth led by wealth management, cash management and investment banking. Other non-interest income declined 46% or $72 million from lower trading gains and treasury customer flows. There was also an absence of gains on fixed assets from a year ago.

Expenses were stable at $465 million. The positive jaw resulted in a 5% increase in profit before allowances to $595 million. Total allowances declined $79 million to $46 million from lower specific allowances. General allowances rose $27 million in line with loan growth.

Non-performance loans. Non-performing assets of $4.85 billion were little changed from the previous quarter as non-performing loan formation was offset by write-offs and recoveries. The non-performing loan ratio rose slightly to 1.5%.

NPA formation during the quarter continued to include several oil and gas support services exposures. There were also two secured exposures to India, including one that was still current. The write-offs included partial write-downs of two oil and gas support service exposures provided for previously. Specific allowance charges for the quarter amounted to $304 million.

Allowance coverage. Allowance coverage of non-performing assets was at 100%. Taking into account collateral, which was valued at $2.79 billion, coverage of unsecured non-performing assets was at 234%.

Capital. Our capital ratios remained strong. The fully phased-in Common Equity Tier-1 ratio was 14.0%. It was slightly lower than [the 14.2% in] the previous quarter as an increase in retained earnings was offset by dividends paid and an increase in risk-weighted assets. Our leverage ratio was stable at 7.9%, more than twice the minimum of 3% envisaged by the Basel Committee.

Dividends. The interim dividend of 33 cents per share represents a three-cent or 10% increase from recent payouts. Based on yesterday’s closing price, the annualised dividend yield is 3.0%. The payout, which amounts to 36% of our first-half earnings, is consistent with our policy of paying sustainable dividends over time, consistent with our capital management objective, long-term growth prospects and the need to maintain prudent capital levels in view of the uncertain impact of regulatory changes.

The scrip dividend scheme will apply to this dividend. Shareholders electing to receive their dividend in scrip will be issued new shares at the average of the closing share prices on 11, 14 and 15 August.

In summary. We delivered a strong operating performance in the first half. Loan growth was broad-based and fee income rose to a record. The results were muted by lower Singapore dollar interest rates and a weaker trading performance.

Our business pipeline is healthy. The business momentum in the second quarter has continued into July. We expect the broad-based loan growth across trade, corporate and Singapore housing loans to continue.

Net interest margin is likely to improve slightly in the second half. The extent of the increase will depend on the flow-through of US dollar Libor and Singapore dollar Sor and Sibor rates. Fee income growth will continue to be supported by multiple activities, including wealth management and cash management.

Asset quality will remain under pressure and we expect heightened credit costs in the oil and gas support services sector to persist with the low oil prices.

The 10% dividend increase reflects the Board’s confidence in the quality of our earnings and balance sheet, especially the strong capital buffers we have built.

Thank you, and I'll now hand you over to Piyush.

Piyush Gupta Thanks, Sok Hui.

<u>Key highlights.</u> The second quarter was a noisy quarter from an income standpoint, and there are four things I would draw your attention to.

First, loan growth was about $6 billion but it was substantially back-ended. Most of the loan growth came in June, which means our average asset growth for the quarter was only up by about $1 billion, even though the quarter-on-quarter growth was about $6 billion. The good news is, as Sok Hui said, the momentum's continued, and so we continue to see very strong loan growth [going into July and] the third quarter.

The second noise was in NIM. In the second quarter, the impact of Libor increases on Sibor and Sor was somewhat muted. The amount of pass-through that we saw in the quarter was [subdued] – in the region of around 35% of Libor, when, as we pointed out earlier, that historically this should be 60-70%. [Nevertheless,] it was a positive.

The problem was in Hong Kong, where particularly one-month Hibor, which is what we price our loans off, took a massive dip [because of a tremendous amount of Hong Kong dollar liquidity in the system]. As we pointed out last time, our deposit franchise in Hong Kong has now become heavily geared to rates because of our deposit mix – Casa is about 60% and therefore when Hibor comes off, that puts a squeeze on our net interest margin. So we picked up about two basis points in Singapore and we gave up two basis points in Hong Kong, which is why we wound up with a flat NIM for the quarter. July saw [rates in general picking up,] including Sibor and Hibor. Based on our assessment of currency movements, I think there's upside in the rates in the second half. I'll talk about that in a bit.

[Third,] as Sok Hui pointed out again, our income from annuity fee businesses – wealth, cards, transaction banking – was very solid. But year on year, we suffered from a high base in investment banking, [specifically with] equity capital markets. In last year's second quarter, we did a couple of big trades, such as the Manulife REIT [transaction], and as a consequence, while we had a good investment banking [performance this] quarter, it fades in comparison to the quarter we had last year. We're off by $40 million-$50 million on fee income, just because of a comparison effect. [Debt capital markets were up year on year.]

[Fourth,] markets. The good news is the second quarter was much better than the first quarter. In the first quarter, trading was really challenged; the second quarter was much stronger. But again, year on year, the second quarter is still poorer than the second quarter last year and the overall challenge in FICC continues to be there – [particularly on] rates, comparing last year to this year.

<u>Underlying business momentum.</u> While it's been a noisy quarter for a lot of reasons, the underlying business momentum of our key businesses has been very strong.

We pointed out before that we have continued to grow mortgage market share in Singapore. Between last year and this year, our market share is up by almost another percentage point – 80 basis points. The better news is that our new bookings for the second quarter were the highest in five years. [This shows that] there has been a very clear pick-up in housing activity in Singapore in the second quarter of this year, and that's coming not just from new launches but also resale and refinancing. Because the booking was so high, we expect the flow-through of that to show up in the third and fourth quarters of this year. It's looking quite healthy and promising.

Similarly, on cards, our market shares on both billings and receivables have continued to increase. In both categories, we are up by almost one percentage point of market share [compared to last year]. These market shares are a record for us – we've previously never had such high market shares on the card business, so again, momentum is very good.

On wealth management, we had 16% growth on AUM over the year, $175 billion for all wealth AUM. When we add on ANZ, which will happen now and over the next three quarters, that should give us [about] another $20 billion on top of the $175 billion. So again, momentum continues to be very good with solid business growth.

Finally, on transaction banking, cash management and security services, [our income is] up 28% year on year. We're getting all the usual growth, we're winning regional deals, we're winning multinational deals, our balances are going up, so this continues to be very solid. [Also, we] have been consistently rebuilding [our trade book since it came off between 2014-2015]. At the end of June, our total trade book – both customer loans as well as interbank – was up to $47 billion again.

You can see all the key underlying parts of our business – on the consumer side as well as on the corporate side – are exhibiting very strong momentum.

<u>ANZ integration.</u> A quick word [on ANZ] – we are making good progress. We completed the China integration and it went smoothly. It's a small business so it doesn't move the needle very much and it was relatively uncomplicated. We are scheduled to do Singapore tomorrow and the day after, over this weekend. It's a fairly large business with 300,000 customers and I'm hoping it will be smooth. There will be some hours of inconvenience for some of our existing customers; people can't use their debit cards for two or three hours tomorrow, they can use the Nets card but they can't use the debit card. We've made adequate arrangement to advise customers in advance so hopefully it will not be too much of a challenge.

We should be able to get Hong Kong done in the third quarter, Taiwan in the fourth quarter, and then Indonesia in the first quarter next year. We project that once we get this done, we should get about a $600 million lift in the top line next year, and [the integration is] on track. So far, we've made offers and about 85% percent of all the employees we are targeting to join us have accepted. Also, as best I can tell, [we should be able to move] about 85-90% of the original AUMs that [came with the transaction, which is] the basis of that $600 million [total income] number for next year.

Expenses. Sok Hui pointed out for expenses, not only has the cost-income ratio been improving, our absolute expenses have been coming off. In the first-half of this year, our absolute expenses are down 1%, and that reflects the effort we're making in multiple ways.

First, we're seeing real improvement in our channels and our distribution costs. The ATM network, cash deposit machines, branch footprint, contact centre – we've been able to rationalise and take costs out of every one of these. In the contact centres – we're using data analytics to reduce the [length of] calls as well as call volumes. In the branches – we're putting virtual teller machines, we're putting video teller machines, we're putting in cash recyclers so we get reduced numbers of cash trips we make because [customers] can recycle cash back into the same machine. So we're getting substantial cost reductions in the distribution.

[Second,] we're seeing cost reduction by digitising the end-to-end process. Our digital acquisitions continue to improve. In the past, I've talked about digital acquisition for SME accounts, for cards and for unsecured [loans]. Last quarter, for the first time, more than half of our mortgages came through direct sourcing, without going through brokers, without going through developers, principally on account of our online activities in the mortgage space. Similarly, our straight-through-processing rates are improving across every category, not just through payments where we are up in the 90% range, but all of the other products that we do as well. So we've seen cost improvement there.

[Third,] we have been able to simplify our business model and our organisation structure in some businesses, principally SME, where we've rethought our strategy in several markets and tightened them a bit, as well as commodity derivatives, where we scaled down the business. Also in the brokerage business where, as I alluded to before, we unbundled the business activity and have [merged] the retail part of it into wealth, and [more tightly coupled] the institutional part of it with capital markets. So in all of these cases, we've been able to see efficiencies flow through.

And finally, in terms of our technology, as we insource more and more of our applications technology into Hyderabad and as we leverage cloud architecture – moving away from the large data centres, large mainframe constructs to more micro-services and commoditised hardware constructs – we're seeing the benefits come through quite nicely as well. We're quite confident that we should continue to see efficiencies on the expense side, because all of the programmes that we've launched are already delivering us value, and we see that continuing to happen as we go forward.

Portfolio update on support services. In terms of portfolio, I've said we've about $7 billion of exposure in the support services, ex-Swiber. Of that, $1.6 billion is to government-linked shipyards, mostly in Singapore, which we don't consider at risk. The residual portfolio is $5.4 billion, of which there are two categories. [The first is to] five large names, [which make up] $2.4 billion. That used to be $2.6 billion. It's come down because we wrote off some [NPLs] in this category. [In the second category,] we have about 100-odd names where we have $3 billion in exposure overall.

Now, the sector continues to stay challenged, and as oil struggles to get over $50, and as long as oil is staying in the $45-$50 range, two things are happening. One, there is very little new development activity happening [for those in the industry] supporting drilling and exploration. That has been challenged for two years and that is already factored in.

But the other thing that is happening is even in producing wells and servicing, while the contracts are picking up somewhat, the oil and gas service players don't have any pricing power. While they've been able to get short-term contracts and roll-over contracts, they're not able to price up. At the prices they're getting for the contracts right now, they're barely able to cover opex, so it's really hard for them on a sustained basis to cover [payments on] interest and principal.

This continues to be the case, and as long as oil prices stay in this range, I'm seeing it to be very hard for the sector to regain any degree of pricing power. If you look at the announcements [of the oil majors], they're all factoring in a long-term view that oil will stay at $50 and, therefore, they're recalibrating their costs to a $50 oil price. As a consequence, they refuse to pay the suppliers any more than they paid in the last year or two, and therefore pricing is really being challenged for most contractors.

On the $3 billion portfolio [of about 100-odd names], I'd earlier said that about 60% of that is weak, and of that, about $800 million has already moved to non-performing – of which $600 million moved in the first six months of this year, [resulting in first-half] provisions in the $300 million range.

[This leaves a] residual portfolio of about $1 billion that is still weak, and I think a large part of that will move to non-performing during the rest of this year and next year. I expect to see NPA formation of roughly the same level as the first half in the second half [of 2017], and therefore the SP for the second half will be about the same as the first half. We took $300 million in the first half and we're likely to take about $300 million in the second half [for this $1 billion portfolio]. This is consistent with what we've said. Our previous assessment is intact from that standpoint – no new cases are getting into the watchlist, we're not seeing new weak names. It's just that the names that were previously identified as weak are moving into NPA, as we projected they would, and are likely to continue to do so for the rest of this year and into next year.

The risk [to our assumptions] in this [$1 billion portfolio] comes not from [an acceleration in] incremental NPAs but from collateral values. Our latest set of collateral values are almost 40-50% lower than this time last year. Collateral values are reflecting the fact that there is no pricing power in the sector. If collateral values continue to creep lower – and I've said before, we have one or two ships which are bespoke, so we've got to figure what price we can get for them – it is possible that we might have to take more provisions against that lot of existing NPAs. In the normal course, I'd expect [any additional provisions due to lower collateral] to be no more than another $300 million. A lot of that could happen next year [rather than] this year, but it depends on how our negotiations go and when we actually sell the ships. Some of that could spill over into this year if that were to happen.

Finally, [on the five large] names, two of those names are [already] non-performing. After write-offs, the NPA related to that is about $600 million. The other three names have in the past been relatively robust in terms of the contracts [and work] they have on hand, but [one or two] of those names have some liquidity events coming due in the next 12-18 months – large bond maturities. Over the next 6-12 months, we have to work with these names to re-profile and restructure [their debt] so that they can handle the liquidity events. There's always a degree of risk you might have an event-driven shock as you go through the re-profiling or restructuring process.

To put [everything] together, we guided that our total SP for this year should be roughly the same as last year, ex-Swiber, and in the normal course that's what we'd expect. However, depending on collateral values and our ability to dispose of some assets in the back-end of the year, [SP] might creep up. If we unfortunately [wind up] with some event over the next 1-1.5 years, our SP might be [even higher, but] we'd have to look at that separately. [Excluding that event scenario and assuming that we are able to sell our collateral at imputed valuations next year], my own assessment is that [there would be] about $300 million of SP next year from new NPA formation. [In the worst case, there might be] another $300 million from [reduced] collateral [valuations], which would mean that next year SP [for the sector] will be pretty similar to this year's [base-case SP of $600 million].

<u>Outlook.</u> Our loan pipeline, like we said, is healthy. [The] third quarter has continued to be very robust. We saw 3% loan growth in the first-half of the year [and] we think we should be able to get 3% in the second-half of the year; it'd be at the high-end of the mid-single-digit guidance we gave earlier.

[We should see at least mid-single-digit growth in] income for the second half, partly because the base-year comparisons on margins will be better, and partly because we have a more positive outlook on the flow-through for both Sor and Hibor in the second-half of the year; this is fundamentally driven by our view on currencies. If the Singapore dollar, which hit 1.36 and turned back, starts weakening again, you'll see a stronger US dollar over the next few months. That should allow a better pass-through of rates into Sor over the next several months. In July, Sor and Sibor are already up almost 10 to 20 basis points compared to the second quarter, so we should see some impact of that flow-through into our NIM.

[We would see a similar effect] on the Hong Kong dollar, which is weak ironically. As it starts weakening – it's already hit 7.82 – and as it starts heading to the top of the band at 7.85, you should start seeing some reversal in the rates in Hibor. We've begun to see that, and in the past few weeks, Hibor has also moved up by seven to eight basis points. Our projection is that you start seeing that pick back up again and, based on that, we think our NIM should be up by a couple of basis points as we go forward from here.

On top of that, if you get another hike – even if the hike is postponed to December – we might see a couple of weeks' impact from the hike as well. So [on a net basis], we should [hopefully] be able to see a two to three basis points lift in margins in the second-half of the year, which should give us a full-year NIM of 1.75-1.76%.

We've guided before [on our cost-income ratio] and I think we should be able to retain our cost efficiencies and keep it in the 43% range. SP, as I just talked to you about, could be higher than what we previously guided, depending on what comes in with the collateral values as we go forward.

I'll stop and I'm happy to take questions.

Chanyapond Chanjaroen (Bloomberg) Could you talk a bit about NIM in the second quarter? I just want to understand a bit better about [the impact of] Hibor on NIM.

Piyush Gupta We pointed out last year that our liability profile in Hong Kong has moved. [Current and savings accounts, Casa] used to be about 40% [of deposits]; today it's about 60%. Since our liabilities are in Casa, it means [that deposit costs] are fairly steady and low. [At the same time,] 75% of our loan book is priced off Hibor, of which the vast majority is priced off one-month Hibor. So if one-month Hibor goes up and the cost of funding based on Casa doesn't move, then our margin goes up; if one-month Hibor comes down, then our margin comes down.

One-month Hibor came down very sharply in the last quarter because of the huge increase in Hong Kong dollar liquidity. Why there is an increase in Hong Kong dollar liquidity is a little uncertain. My own speculation is part of that reflects conversions from CNH [deposits] back to Hong Kong dollars. CNH [deposits] in Hong Kong peaked at 1 trillion yuan and they've now come down to about 400 billion yuan. Over the past several [quarters], there's been a conversion of almost 0.5 trillion yuan to Hong Kong dollars, and I think that's propelling a lot of Hong Kong dollar liquidity. There's just a lot of Hong Kong dollar liquidity which HKMA has not been mopping up and, as a consequence, Hibor has been edging lower.

But the way the central bank [manages] its monetary policy and currency band is that as the Hong Kong dollar depreciates and gets closer to 7.85, then HKMA will come in and intervene. The Hong Kong dollar is now at 7.82 and already you're beginning to see some people reversing their positions. I'm not sure if there's a central bank intervention or just the market reversing its position, [which has led to] Hibor beginning to creep up again.

Chanyapond Chanjaroen And also on the new NPA formation, what's your guidance for the rest of the year? Do you expect lumpy [formation]?

Piyush Gupta No. We said that of our $3 billion portfolio of granular names, 60% or $1.8 billion, is weak. Out of that, $800 million is already in NPA, so there is another $1 billion of weak names [that are not NPA]. Of that, I expect about half of that to move to NPA this year, another $500 million. [If so,] our SPs for that will be [about] $300 million to cover the NPAs that get formed. That's consistent with what we've told you before – our total provisions for the sector were [expected to be] about $600 million for the year. [We've taken] $300 million in the first half and we're [expecting to take] roughly that much in the second half [as well].

Brandon Tanoto (Channel NewsAsia) We're seeing pressure on asset quality, so how is DBS addressing this, and do you reckon we'll see any signs of improvement going forward?

Piyush Gupta I thought I just spent a long time explaining that. The point [is that] we're not seeing asset quality pressures of significance outside the [oil and gas support services] sector, [whether in] Singapore or [elsewhere]. There are some episodic cases, [some] in the news as well, but they don't move the needle that much. [While] you're not seeing too much pressure anywhere else, the [oil and gas support services] sector continues to be challenged. [But] because we've already identified the sources of weakness, we know where they are [and] it's just a question of how much [of the sector] continues to move to non-performing and at what stage. That's what I gave some details on earlier.

Richard Hartung (The Asian Banker) You mentioned digitisation and productivity had a one percentage point impact [on the cost-income ratio], and that there's been a lot done. Do you see further [significant] reductions in expenses due to digitisation? If so, where is it going to come from?

Piyush Gupta I pointed out four areas on my [expenses] slide and I said that over the next few years, we hope to be able to bring our cost-income ratio down to 40% from 43% [currently]. We peaked at 45%, we're down to 43% – we're headed in the right direction. If you build out the trajectory, we think we can get to 40% over the next two years.

It comes from all of these [four categories] I laid out. In terms of the distribution costs, so far we haven't had to reduce branches, but over the next three to five years, we should be able to rationalise the branch footprint. If you look at the Netherlands, branches are down to 25% of what they were five years ago. If you look at Scandinavia, branches are down to 30-40% of what they used to be. Our own footfall in our branches is coming down because we continue to move people onto digital channels. As more and more people are using our iBanking, PayLah, and PayNow, they come to the branch [less]. We're seeing a reduction of almost 3-4% in footfall in the branches.

Equally, we're able to rationalise our ATMs partly because we've been able to [bring in] a new generation of ATMs. Earlier, we had [separate] machines to put in cash and take out cash. Today, you can put in cash and take out cash from the same machine. Now that is quite a dramatic impact because not only can we reduce the number of machines, but it also saves the number of cash trips we need to make. [Previously], we had staff going to withdraw cash from one set of machines, bring it back and count it, and then another bunch of staff going to load cash into the other set of machines. Now, because the cash goes into the machine, it cuts down the number of trips. Our total cost of cash handling in Singapore is $80 million-$100 million, so as we rationalise both the machines and the cash recycling process, you see visible saves in that.

The second is our end-to-end process digitisation. We're moving a lot more of our business to online [customer] acquisition. That's true in credit cards and unsecured loans, which are [more straightforward], but now we're doing that in bancassurance, mortgages, SME origination and loans. When you acquire [customers] online, your cost of acquisition goes down. So that will continue to be the case, and there is a lot of opportunity to continue the shift to online acquisition.

We're also moving a lot of our business to straight-through [processing and] we're killing paper. The minute you kill paper, you don't need to do the manual entries and the paper handling. The transaction goes straight through from the customer all the way to our back-end systems, eliminating work.

Then, the fourth category, which is the technology infrastructure. Moving from legacy technology architecture to cloud-native architecture has massive impact on expenses, both on hardware, data centre infrastructure, software. On top of that, because we're insourcing, we're also reducing sourcing costs from vendors and providers as well. All of these are very positive.

Ishika Mookerjee (Citywire) How has digitalisation affected costs in private banking in particular, and what impact has it had on the cost-income ratio? Second, what were some of the challenges during the ANZ integration for high-net-worth clients and what kind of AUM is coming over?

Piyush Gupta Our total cost-income ratio on the high net worth, Su Shan – do you remember the number?

Tan Su Shan We don't normally share it but it's actually now down to a record low.

Piyush Gupta All right, so it's been coming down regularly. I once said it was 58-59% which is a record, because the industry average is in the 70% range. So we are very efficient in our wealth management business at the top end.

As we've been very successful with iWealth, we continue to get better costs. iWealth has been fantastic for us – it's extremely well regarded and more and more of our customers are happy to deal online. You can deal 24/7, you can do equity, you can manage your portfolio. The feedback is very [positive]. As more and more of our wealthy customers begin self-servicing on the back of iWealth, that drives [further] improvement in our cost-income ratio at the top-end of wealth.

In terms of [ANZ], we have only integrated China so far, and that's not a consequential business, so the big pieces are going to be Singapore tomorrow and Hong Kong in a couple of months. But the big challenge with the wealth integration is always during post-integration, which is around know-your-customer and customer due diligence. Because of privacy laws, you really don't know what customers you're going to inherit until you actually get them on your book.

In your due diligence, you take look at the policies [of the bank you bought the portfolio from], so that you can have a high degree of confidence that its customer policies are good. But once the customers come on board, you have got to go through them customer by customer to make sure you're comfortable with a customer or not. That is typically the biggest challenge with wealth integration, and that is still ahead of us.

Jamie Lee (Business Times) On the restructuring of the oil and gas sector, in terms of the vessels, is there a way to repurpose these vessels. There's been a lot of talk about how can that be done. How optimistic are you about that? Second, do you see costs going up for wealth management? People have talked about how wealth management is inherently a very expensive business, especially for the high end, you still need expensive relationship managers. I assume that you're still building out the business, so how much more investments do you see in this space?

Piyush Gupta On the first, it is possible to repurpose, but one of my realisations over the past 12-18 months is that it's not that easy. Where people have been able to repurpose their ships, it takes some capex. So you've got to first put some money into the ship to repurpose it and then you've got to look at what rates you are able to get for the repurpose. It turns out that because of the overall climate, even repurposed ships don't get very high rates; so there remain challenges after repurposing. [Even] if you put some money in, repurpose the ship, can put it to work [and] get cash flows, you don't get the same kinds of rates that you used to three years ago.

On the wealth management business, of course we continue to invest. The question is: do we make more money than we spend? And we have made a lot more money than we spent, which is why our cost-income ratio keeps improving. If you go back to the whole notion of why are we more cost-efficient in wealth than anybody else – and we've said that before – [it is because of] our wealth continuum. We uniquely run private bank, private client and mass affluent segments off a common platform. Because of that, we get tremendous synergies and economies of scale which none of our competitors do. We run a common backbone [inclusive of] technology, compliance, legal and product selection, and just have differences at the front-end of the model.

Second, our digitisation of wealth has proven to be very beneficial, so it allows us to do a lot more with the digital channel.

Finally, one of the positive outcomes of the wealth continuum is that in addition to getting customer mobility, we also get staff mobility. Many of our private bankers are promoted from the private client [segment], and many of the private client bankers are promoted from the mass affluent [segment], and all the way down to our branches. I was just shown the case of somebody who started as a POSB teller and has worked all the way up into being a private banker. When you promote and move your people internally, you don't pay the very high costs of hiring from the market. So overall, we continue to invest but our efficiency ratios continue to improve.

Goola Warden (The Edge) My question is on the risk-weighted assets, your CAR, and your fully loaded Tier-1. [Your CAR ratio is] higher than the other two banks.

Chng Sok Hui The CAR ratio moved from 14.2% last quarter to 14.0% largely due to the payout of the dividend during the quarter. [The ratio is higher than the other two banks] because we have been conservative in accretion of capital. Earnings growth has been good and we have also had a consistent scrip dividend policy.

Goola Warden What's the likely impact of IFRS 9 on your financials, on your P&L, balance sheet [and] capital?

Chng Sok Hui We're still working through the numbers and we should be able to have a [more complete] assessment in the next quarter when MAS [provides definitive] guidance; they have done a consultation paper but they have not finalised the approach. The final numbers will depend on whether MAS goes for approach one or approach two in their consultation paper.

Approach one is aligned to IFRS 9 that is published globally, with the minimum 1% general provision that's required as a movement through reserves. Approach two is more similar to what we have today – you need to meet the 1% minimum requirement passed through the P&L, but you have [to make] the full IFRS 9 disclosure. As far as we understand, the banks have a preference to continue with the current approach, which is more conservative, to actually take the 1% general provision requirement through the P&L, with full disclosure of the IFRS 9 numbers as a disclosure note.

Mayuko Tani (Nikkei) I have two questions. One is about cost. [Expenses fell by 1% from a year ago] and I believe the technology has played a role, but what is the outlook for savings due to digitisation? Is it going to continue and is it going to be bigger from now or is it done? Another is about digibank. You had India and then you were planning to have Indonesia. Can you give us an update, please?

Piyush Gupta I just indicated that this is a continuous journey. I think there's still significant opportunities to take cost out of the system through all of the measures we just identified. The fact that I think we can bring our cost-income ratio down to 40% over the next three or four years means that we should be able to continue to get cost efficiency over the next few years. So I think it's an ongoing journey.

My own view is that if you were to do a complete digital bank, you can run a cost-income ratio in the low 30% range. I think that's possible to do based on, essentially, no branch infrastructure at the front end, a straight-through-processing regime and using AI and chatbots at the back end. So even if you end up with customer acquisition costs, your actual processing and servicing cost is very low.

That's what we're being able to see with digibank in India. We're now at about 1.4 million customers in July. Of that, about 300,000 are full savings account customers. We are processing that with about 60 people. In the normal course, we would need 400-500 people to do that scale. By year end, we think we'll be down to half – to 30 people.

This tells you that if you can design for something like that, the cost can be very low. Now, the reality is you can't get to that level when you have a legacy base. So it'll be very hard to get to a low-30%-range cost-income ratio for us in Singapore for example, because you've got branches [and ATMs to cater to customers in the heartlands]. But [at the same time] that [can be] a goal: if you have to think over ten years what could banks get to, I think that's possible.

In digibank in India, we are very encouraged. Our customer acquisition is continuing at over 100,000 customers every month. We get them both directly as well as through channel partners; the account balance build-up is very consistent and good. Like every good fintech we're losing money! We expect to continue to invest and lose money for three or four years. But if we [compare and] try to do the same build-up with an old-fashioned branch model, you will need 15-20 years to pay back. In the digital model, you can get that scale and presence and still look to break-even in three to four years.

Edna Koh I'm afraid that's really all the time we have today. Thank you all for coming. See you next quarter.

Piyush Gupta Thanks, everybody.