Live more, Bank less

Edited transcript for DBS third-quarter 2018 results conference call for buy and sell sides, 5 November 2018

Michael Sia Welcome to our third-quarter results session for the buy and sell sides.

Robert Kong (Citi) First, could you elaborate on the non-loan specific allowance charge. Second, what was the amount of the one-off expenses during the quarter. Third, could you hazard a guess about fee income growth next year.

Piyush Gupta The non-loan specific allowance charge is due to a contingent performance guarantee for the same Singapore name we spoke about in the previous quarter. I don't expect the guarantee to be called but we've taken the charge to be conservative, just in case it is called. But it's a one-off case.

On expenses, we had three different non-recurring items. There was the fiftieth-anniversary staff bonus we paid out. We also spent money on the 'Live More Bank Less' advertising campaign – it's the first rebranding in a decade. And we had a litigation case from ten years ago in Hong Kong that we recognised expenses for as well. The amounts were roughly $15 million for each item.

On fee income growth, we expect it to be in the high-single digits.

Robert Kong Hong Kong NIM didn't go up as much as I thought it would. Hibor rose about 44 basis points during the quarter, so it was probably one of the best movements for some time. Prime rates also rose.

Sebastian Paredes The prime rate increased only 12.5 basis points at end-September, so the full impact was not felt during the quarter on housing loans, which is small in our case, and part of the SME portfolio. So we did have some margin compression on part of our loan book, so that probably explains your point.

Nick Lord (Morgan Stanley) On wealth management revenue, in the absence of market activity picking up, can you still grow wealth management next year? And what are your thoughts on market activity?

Piyush Gupta Wealth management is one of the areas we continue to invest in, by adding relationship managers. Our headcount increased by 600 during the quarter, which is high, but 250 of them were RMs. In their first year, productivity is marginal – they bring in $200,000 in the first year but the amount jumps to $1.5 million in the second and $3 million in the third. So even if there is no increase in market activity, the new hires will drive a substantial growth in the top line from increased productivity.

Tan Su Shan First, markets go up and down. And when markets are volatile, there are opportunities for DBS from customers' flight to safety. When everyone gets scared, our AUMs and net new money outperform peers as customers look for safety.

Live more, Bank less

Second, Asian wealth is still being created. We recently expanded our Treasures Private Client business to Taiwan and Indonesia, which have shown some early success. There is also a need for estate planning that, if done well, will provide a bank with sticky long-term assets and recurring income. We're seeing quite a lot of fee growth from estate planning, which brings long-term recurring income. We're also pivoting from a reliance on commissions from trades to an advisory fee model. We've seen gradual growth in our discretionary assets, including digital portfolios.

Third, the digitisation of the whole wealth business – not just from the viewpoint of customers but also internal staff – has reduced the costs and turnaround time of serving customers, whether for requests on pricing or trading.

Nick Lord On capital, your CET-1 is fluctuating in the 13% range depending on whether you paid a dividend in the prior quarter. I assume you're going to continue bouncing around this range for the short- to medium-term.

Piyush Gupta The guidance we gave was 12.5% to 13.5%. At this quarter's 13.3%, we're at the higher end of guidance. We might drift to 13.0% on greater capital efficiency, but it will be within the range.

Loo Kar Weng (HSBC) Earnings from South and Southeast Asia were zero during the quarter. Can you give some colour.

Piyush Gupta Some of the increase in allowances this quarter was in South and Southeast Asia, where we had specific cases in Indonesia that are not part of any trend. The overall trends in India and Indonesia remain positive although they are still under-performing. In India, where approval for subsidiarisation has come through, we will begin expanding next year, including opening up new kiosks and branches. We expect India to continue being a drag on group earnings till 2020 because of the investment costs needed. In Indonesia, the trend is positive. Digibank is doing well and we are seeing an improvement in the consumer business with ANZ. The corporate business is also doing well.

Akash Rawat (UBS) On the NPL slide, can I better understand what the line item 'translation' means. There was also a pick-up of $700 million in restructured NPAs during the quarter. What was that? Finally, card fee income of $185 million this quarter is roughly $35 million higher than a year ago. Is this a new level of card fee income?

Chng Sok Hui The line item shows the translation effects of NPAs that are in foreign currencies into Singapore dollars.

Akash Rawat If it falls under IBG will it be classified separately?

Michael Sia The translation number is for IBG and CBG combined.

Piyush Gupta On restructured NPAs, they are NPAs that have gone through a restructuring exercise, which means we have taken some haircuts, extended the term of the loan or some such thing. The loan is moved into the restructured category but it's still an NPA. The bulk of the restructuring that is still happening is in oil and gas support services, which is where the bulk of NPAs are.

On card income, the increase is mostly from ANZ, including Taiwan and Indonesia. When Indonesia was first integrated, there was some attrition and delinquencies went up. Over the past few months, we've managed the business more tightly and started seeing a return of receivables to where they had been before the integration. That accounts for the bulk of the increase in card fees.

Harsh Modi (JPM) A few questions on NIM. First, assuming no change in Sibor, how much more can asset yields increase from lagged repricing. Second, what is your current assumption for the pass-through from Libor to Sibor?

Piyush Gupta In our Singapore dollar loan book, 45% prices off Sibor – and even so it takes several weeks for the impact to flow through. Another 45% – including about $30 billion of fixed-deposit-rate-based (FHR) housing loans – reprices with a considerable lag and so will continue to flow through to next year. At an average yield of 1.80%, the NIM on FHR loans is 12-15 basis points lower than before. With fixed-deposit rates about 2%, there are opportunities to reprice further in the next few quarters. There is an even bigger drag from fixed-rate loans, which account for $14 billion in housing loans and some more in corporate loans. Most fixed-rate loans reprice over two years, so the impact will flow into next year and the year after.

On the pass-through, the long-term average is roughly two-thirds. But it can go as low as 30% and as high as 100%. For the nine months this year, it has been 65%, with an even higher level in the past quarter. The size depends on the strength of the US dollar relative to the Singapore dollar. Despite the MAS policy stance, we expect the Singapore dollar to continue to weaken. If that happens, we'll see a lot more pass-through. If we're wrong and the Singapore dollar goes the other way, we'll see less pass-through. Our assumption is based on the through-cycle average of 60-65%.

Harsh Modi Does the recent increase in Libor worry you in terms of sequencing to Sibor and US dollar deposit costs?

Piyush Gupta I think there are a lot of moving parts, a lot of noise. It isn't useful to worry about how each component moves in short-term periods. I just tend to look at broad aggregates. We're maintaining both our US dollar deposits and wholesale funding. Our view is that rates are going up and we're better off locking in funding at current rates.

Harsh Modi Why did your treasury asset yield not pick up as much? Did you reduce the duration of treasury during this quarter?

Piyush Gupta The weak treasury asset yield pick-up was the result of three different things. First, there was an accounting tear: if you swap from a high-interest-rate currency to a low-interest-rate currency, you'll give up on NIM and make up on the swap points, which is recorded as non-interest income. That caused two-thirds of the treasury NIM drag. The remaining one-third comes from two things. One, the yield curve has been relatively flat and since we're in the two- to five-year bucket, we've had fewer chances to opportunities to gap. Two, because we're in this bucket, the securities reprice with a lag of up to five years.

Harsh Modi Finally, on the NPL pick-up in Indonesia, was it due to ANZ or something else? And more importantly, is there any read-through?

Piyush Gupta There is no read-through. The increase was partly due to a borrower that was caught up in the global restructuring of an affiliate. Our customer actually has fairly robust cashflow.

Marcus Chua (Nomura) First, Singapore dollar fixed deposits have increased. Is this related to the NSFR? And non-SGD deposits are flat to down. Is management thinking that next year's growth will likely come from the SGD book? Second, what is the NIM assumption for next year?

Piyush Gupta Our NSFR is quite comfortable at 109%, so that was not a principal factor. The increase in Singapore dollar fixed deposits reflects market trends of a shift from Casa to fixed deposits. There has also been a shift to Temasek and Singapore government bonds. The slowdown in Hong Kong and China currency deposits is due to the run-off in our trade assets. We've said that if we can't put on trade loans at a positive margin, we will let them run off and hence the deposits as well.

We haven't provided a NIM projection because using an assumption of two US rate increases reaches a very different conclusion on NIM from four rate increases.

Melissa Kuang (Goldman Sachs) First, is the decrease in China loans during the quarter due to trade? Have you done any bottom-up or top-down risk analysis on the China book and is there anything we should be worried about? Second, investment banking fees have been a bit weak. What is the pipeline for the rest of the year and next year?

Piyush Gupta Yes, the run-down in China loans was due to trade loans, which include loans backed by letters of credit from China banks. We are in the middle of our third review using a bottom-up approach on China to evaluate the impact of deleveraging, liquidity and so on. We are by and large quite comfortable. For the whole portfolio, we have identified fewer than 20 names that might have some degree of risk and we are getting our hands quite nicely around them. In the 60-plus bond defaults that have occurred in China this year, we had a couple of customers who themselves had not defaulted but had group affiliates that did. So they did not impact us materially.

Our ECM and DCM pipeline is huge, with a long list of clients ready to take to the market as soon as conditions allow.

Danny Goh (Credit Suisse) First, what was the exit NIM at the end of the quarter? Second, what is the longer-term outlook on costs and will you continue to bring the cost-income ratio down by about half to about one percentage point per year. Is there an update on the migration of customers to the digital platform?

Piyush Gupta The exit NIM was 1.86%. On costs, the process of driving strategic cost management continues apace. By the way, we are targeting half a percentage point a year. But we have also indicated there will be a slowdown in the reduction this year and next because of ANZ – where the increase in costs was more income – and investments for subsidiarising our India operations. We expect to hold our cost-income ratio for the time being before resuming the downward trajectory.

On customer conversion to digital, we track it every six months and there hasn't been any update for the past quarter. The previous update didn't have anything to suggest the conversion is slowing down.

Danny Goh Is IT spend still averaging about $1 billion per annum?

Piyush Gupta It's about that amount. We are investing more money on data, but we've been able to get savings in other parts of technology.

Kevin Kwek (Bernstein) First, are the ANZ costs due to one-time integration expenses and not running costs, and therefore we can expect them to fall off at some point, and when is that? Second, could you give some guidance on wealth management AUM and fee growth. Third, could you give some commentary on what's driving the strength in Hong Kong? Fourth, will the strong growth in cash management continue?

Piyush Gupta The ANZ expenses are not due to integration. They are the ongoing running costs of the business. This accounted for six percentage points of the group's expense growth.

Tan Su Shan This year we grew AUM slightly above the market, but excluding ANZ we're probably in line with the two big Swiss banks. I think the difference from them is that we don't do a lot of chunky, North Asia single-promoter shares. We don't get those big IPO counts when they come. Our customer base is more diverse and less concentrated. We are focusing on sustainable long-term assets such as family assets linked to their companies.

On fees, insurance and wealth estate planning will continue to grow. Recurrent income from discretionary portfolios will also continue to grow. The value from digitalisation will continue – RMs using digital tools and more data analytics to predict client needs will help with productivity. All these translate into higher ROA than peers. And without those chunky concentrations, our business will be more stable.

Sebastian Paredes Hong Kong growth has been broad based. Loan growth has been robust at 16%, deposits at 13%, with Casa at 11%, which contributed to the NIM increase from 1.69% a year ago to 2.06% as Hibor rose. Because of new SME and China customers, fee income from cash management is up 64% from a year ago. You can say our growth is broad based, it's customer derived, it's driven by acquisition of China customers, and importantly, we've got a strong income lift from cash management as interest rates increase.

Piyush Gupta Our cash management business is growing across the region. And it's not just higher NIM – our activity volumes are very robust. I'm not very sure how they do it, but Euromoney rated us number three in the world for cash management market share through a survey of 25,000 non-bank institutions around the world. We can see that in our business. Our API protocols have given us the ability to integrate with customers and get into many supply chains, including the insurance and auto component sectors. We've been able to drive a lot of receivable and payable activities though our API integration.

Kevin Kwek How much of the growth in SMEs is from Singapore?

Piyush Gupta It's broad based. We're seeing SME growth across the region.

Harsh Modi How does local incorporation change your strategy in India? What can you do now better over next 12-18 months with local incorporation in place?

Piyush Gupta I'm finding that a 'phygital' strategy is better than a 100% digital strategy, based on our experience in Indonesia compared to India. And so we are going to expand into three or four more cities but also deepen our presence in Delhi, Mumbai and elsewhere where we've had only one branch so far. In addition, we are going to open 70-80 kiosks to increase our points of presence in industrial estates where SMEs are located.

Harsh Modi With liquidity becoming tight in India, coupled with priority sector lending obligations that come with local incorporation, are you rethinking your India strategy, especially as a relatively smaller bank with a limited deposit franchise.

Piyush Gupta If you start rethinking strategy with every quarterly shift in the cycle, you'll never have a strategy. You need a longer-term view. The reason we want to build a SME and consumer franchise is to build a deposit base and in a sensible way for the long term. We're seeing some success so far in raising deposits through Tally and in the consumer space. The key is to do it in a measured way.

Harsh Modi Is the focus for both consumer and SME on liabilities or assets?

Piyush Gupta It's led by liabilities followed by assets.

Michael Sia Thank you everybody for dialling in. We will see you next quarter.