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APAC banking outlook

30 June 2022

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Dividend forecasting | **Thematic Report**

APAC banking outlook[1]

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Key implications

- On an aggregate level, the growth rate of Asia Pacific (APAC) banking dividends is expected to moderate to 7% in fiscal year (FY) 2022 to US$209 billion, compared with FY 2021's 14.7%.
- Dividend growth of Chinese banks, the region's biggest dividends contributor, is expected to slow down owing to the stringent pandemic policy and its implication on the economy - the average dividend growth for the "big four" is expected to be 6.4% in FY22, as compared with 11.5% in FY21.
- While the majority of banks in APAC are set to embrace the tailwind from higher interest rate, the path of future growth might be dissimilar, even for banks in the same market.

A challenging and perplexing environment for APAC banks

APAC countries, akin to the rest of the world, are facing great economic challenges in 2022. Inflation pressure intensified during the first half of 2022, driven primarily by surging energy and food prices. This is particularly severe for importing countries such as India and Singapore. Both countries have seen a headline consumer price index (CPI) inflation rate of 7.8% and 5.4% in April, respectively, leading the rest of the key markets in APAC. To combat the inflation, an increasing number of APAC central banks have tightened monetary policy by increasing intertest rates, including central banks in India, Singapore, Malaysia, Australia, and South Korea. On the other side of the spectrum, China and Japan, two of APAC's largest economies, continue to keep their economic policy loose, as the central governments seek to stimulate the demand side of the equilibrium. Both countries reported a comparatively low CPI inflation rate of 2.1% and 2.5%, respectively, for April.

We expect APAC bank dividends to continue to grow in this perplexing and segmented macroeconomic environment, as the majority of banks are set for the tailwind from higher interest rates. At the same time, slowed economic growth, inflationary pressure, ongoing supply chain disruption, and the economic fallout of China's stringent covid policy are the major risks ahead to weigh on the growth potential. We expect the aggregate dividend to reach US$209 billion in FY 2022, representing a growth rate of 7%. This indicates our expectation that the growth rate will slow down from the 14.7% in FY 2021.

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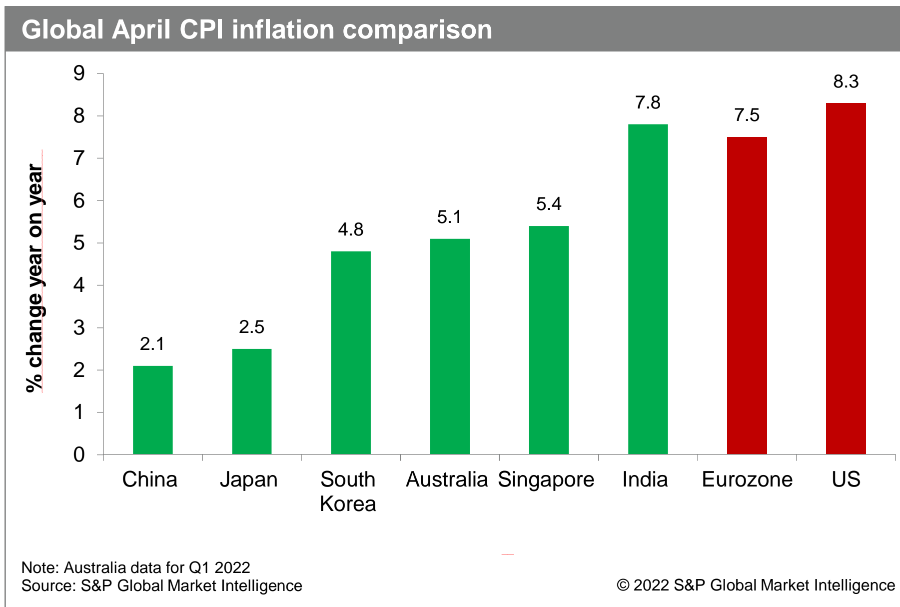

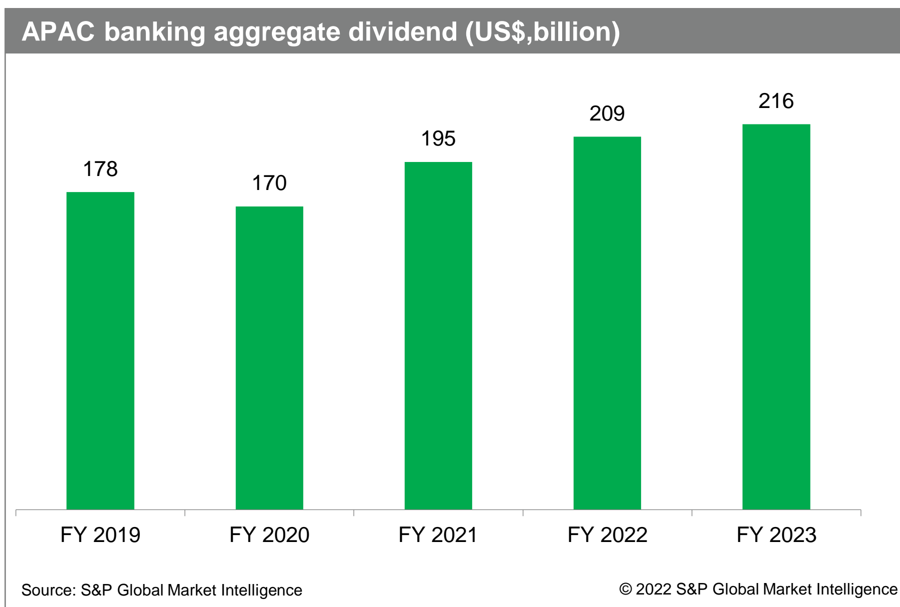

Mainland China and Japan buck the trend—pandemic policy, economic policy, and banking dividend

While rest of the world is relaxing pandemic-related restrictions and embracing the reopening of borders, mainland China continues to insist on a zero-covid policy. The sweeping lockdown in Shanghai, the commerce and finance powerhouse, caused severe disruptions of business and investment activities not just in China but also the global business and trade network. Factoring the impacts, our economist team is projecting the GDP growth to be 4.3% for 2022, well below the official target of 5.5%. The subdued environment has too obviously and negatively impacted the banking sector, the most critical pillar of China's economy and capital distribution. As per the data from the People's Bank of China, loan growth tapered to 8.4% in April this year, as compared with 11.3% one year ago, creating pressure on banks' top line growth, as China banks primarily rely on interest income generated from loans. Prompt regulatory actions were rolled out by the government to reinvigorate loan

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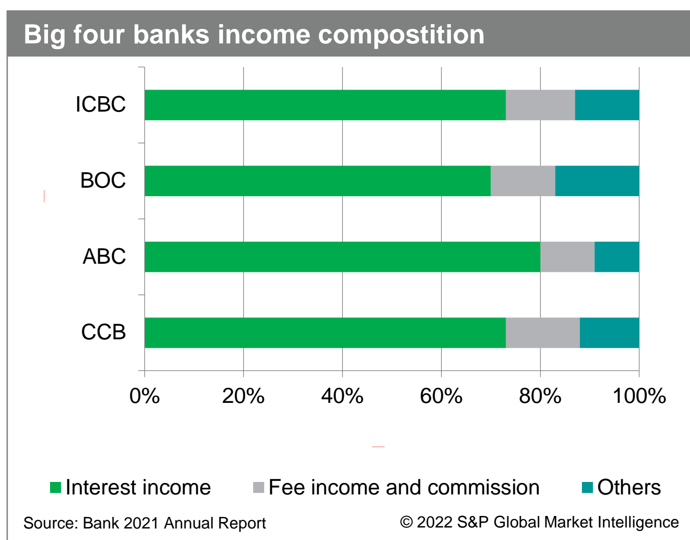
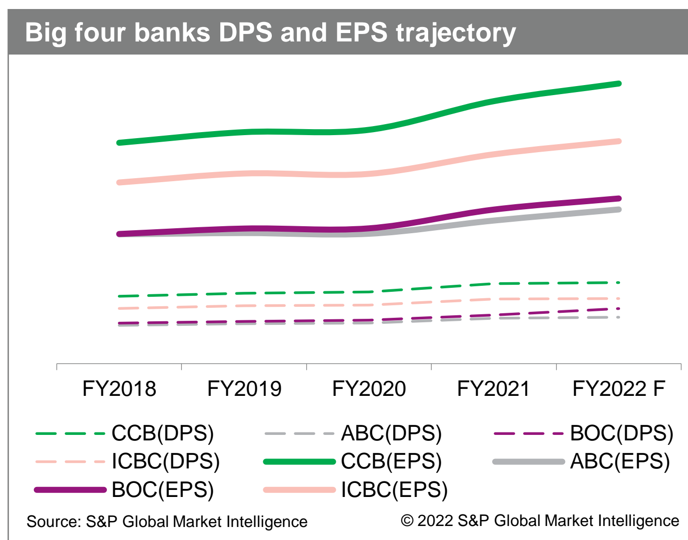
demand—a further cut in key interest rate, the five-year loan prime rate (LPR). The cut is the second one this year and the largest on record. We notice that banks in China have not been spared from the margin compression over the past two years. The further loosening of policy is expected to create more pressure to the margin of the banks, as regulatory bodies, including The China Banking and Insurance Regulatory Commission (CBIRC), have recently sent strong message to the financial institutions to call for stimulus measures to support the grappling corporates. This means a sacrifice in profitability for the banks.

During the past two years, Chinese banks have maintained a steady growth of dividend, defying the worldwide trend of suspending or cutting dividends to preserve capital and to extend the support to the economy during the pandemic. This is attributable to the early control of virus, strong capital buffer and high state-ownership of major banks, as banks provide an important source of income. However, with the challenging environment this year, banks are facing the trade-off between profitability and the support for the economy. The pressure on the topline growth, coupled by the further margin squeeze, are expected to contribute to a lower growth in dividends in 2022. For example, we expect **China Construction Bank (CNE1000002H1)** will pay 0.39 Chinese yuan per share for FY 2022 dividend, representing a year-on-year increase of around 7%, compared with around 12% in FY 2021. The bank has consistently been adopting a 30% payout ratio in the past. However, the payout ratio is expected to be applied to a lower earning for FY 2022. A similar trend is observed for rest of the "big four."





Net interest margin of China banks (%)

Name	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022 F
CCB	2.29	2.32	2.19	2.13	2.09
ABC	2.33	2.23	2.20	2.12	2.07
BOC	1.90	1.85	1.85	1.75	1.70
ICBC	2.39	2.15	2.15	2.11	2.09

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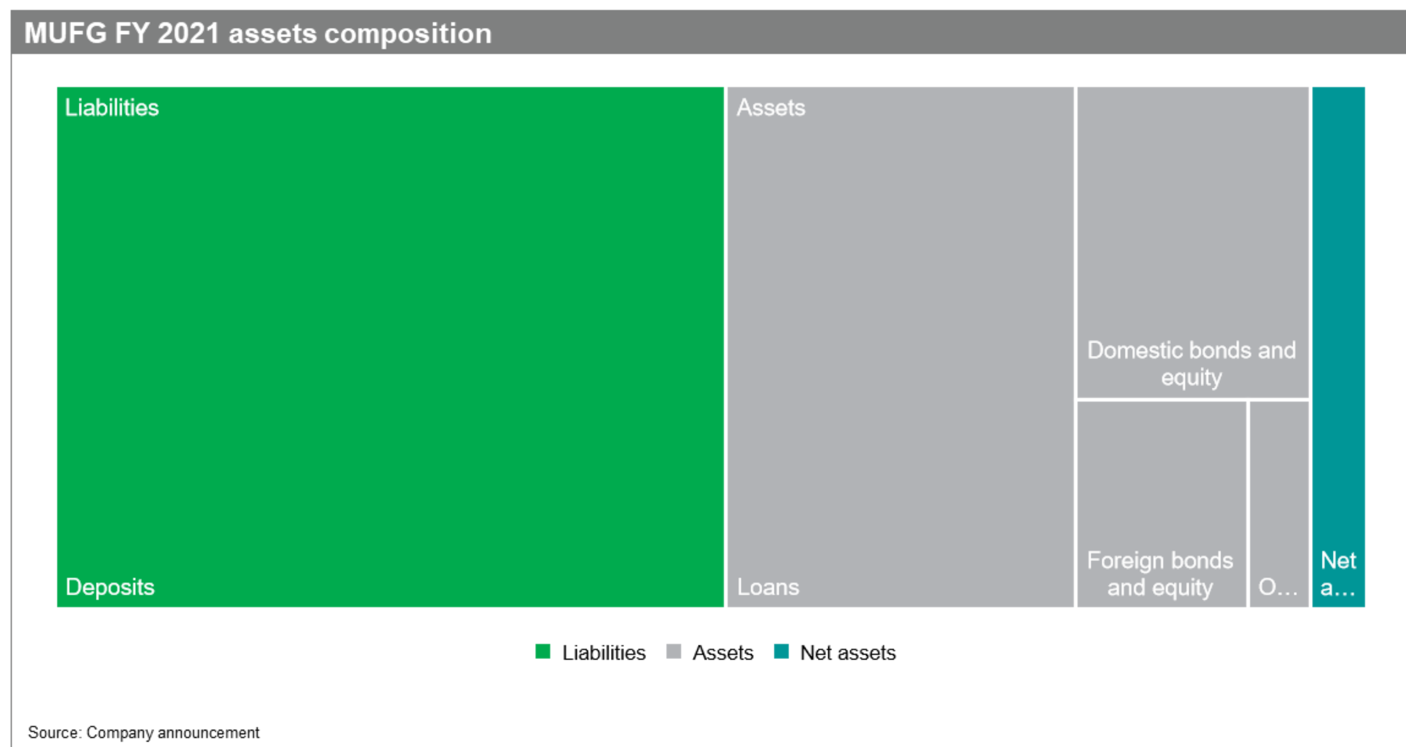
Loan demand might pick up with the continuous loosening of policy, such as cutting the LPR rate. However, this is not expected to come without introducing additional risks, particularly to the banks with large exposure to the already-fragile real estate sector and engineering and construction sector that faced delay in delivering projects owing to lockdowns. However, we notice that big state-owned banks including the big four have very limited exposure to the real estate sectors, with an average of less than 10% of total corporate loan. On the contrary, smaller regional players in commercial banking such as **Bank of Shanghai (CNE100002FM5)** and **China**

Zheshang Bank (CNE100003PS9) have higher exposures to the real estate sector, with over 20% of corporate loans in the sector. As the "zero-COVID" policy continues and a higher tolerance for risks to gain growth becomes commonplace, we expect the asset quality of these banks to come under more pressure in the short term.

As China's neighbor, Japan is another country that maintains a loose economic policy, even though the inflation rate is creeping up to 2.1%, slightly higher than its target rate of 2.0%. Japan is seeing huge economic impacts from the Fed's increase in interest rate, with Japanese yen depreciating to a 20-year low recently owing to the increasing divergence of Japan's rock-bottom interest rate and that of its US counterpart. Instability of prices and costs triggered by the currency depreciation is expected to take a toll on local businesses that have heavy reliance on imports of raw materials. Japan's banking sector is widely impacted by the changing interest rate environment as well. Unlike the majority of their peers in APAC, Japanese banks are more diversified in term of income generation and geographical exposure of assets. Apart from the loans sitting on the balance sheet, they hold a substantial amount of investment in securities too, which consists of both domestic securities and a high portion of foreign equities and bonds, as the banks seek to shift away from the multi-decades low interest rate environment and pursue higher return overseas. As reported in the latest earning season in May, banks such as **Mitsubishi UFJ Financial Group (JP3902900004)** and **Sumitomo Mitsui Financial Group (JP3890350006)** have reported a surge in unrealized loss from foreign bonds. This is a short-term pinch from the rising interest rate environment worldwide, owing to the inverse relationship between bond prices and interest rates. However, this is beneficial to the income of banks in the medium term, as the interest earnings on roll-overs are expected to improve with the higher interest rate.



Japanese banks have a relatively larger exposure to Russia than their peers in APAC. However, the portion of outstanding loans to Russian companies against the total loans book is still immaterial. For instance, **Mizuho Financial Group (JP3885780001)** has an exposure to Russia of US$2.87 billion, representing a mere 0.2% of consolidated exposure. We therefore do not expect the ongoing war to have a profound impact on Japanese banks and their earnings.

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Although the macroeconomic environment remains uncertain, the performance of Japanese banks is expected to be largely stable as the current global interest rate environment is favorable to them. The outlook is expected to improve further with the rising upward pressure domestically on rate increases for the rest of the year. We notice that among the 10 banks within Nikkei 225, 7 continue to guide a higher total dividend for the upcoming financial year. Top payers such as **Sumitomo Mitsui Trust Holdings** and **Mitsubishi UFJ Financial Group** are expected to lead the dividend growth with a rate of 17.6% and 14.3%, respectively.

Japan top banks total dividend for FY 2023

Name	FY 2022 (H)	FY 2023	FY 2023 amount status	Year-on-year growth rate
Sumitomo Mitsui Trust Holdings	170	200	C	17.6%
Mitsubishi UFJ Financial Group	28	32	C	14.3%
Fukuoka Financial Group	95	105	C	10.5%
Chiba Bank Ltd.	24	26	C	8.3%
Concordia Financial Group	18	19	C	5.6%
Sumitomo Mitsui Financial Group	210	220	C	4.8%
Shizuoka Bank Ltd.	26	27	C	3.8%
Mizuho Financial Group	80	80	C	0.0%
Resona Holdings	21	21	C	0.0%
Aozora Bank Limited	149	136	E	-8.7%

Note: Data sorted by growth rate; JPY/share. C refers to company guidance, E refers to forecast as no guidance provided

Source: S&P Global Market Intelligence

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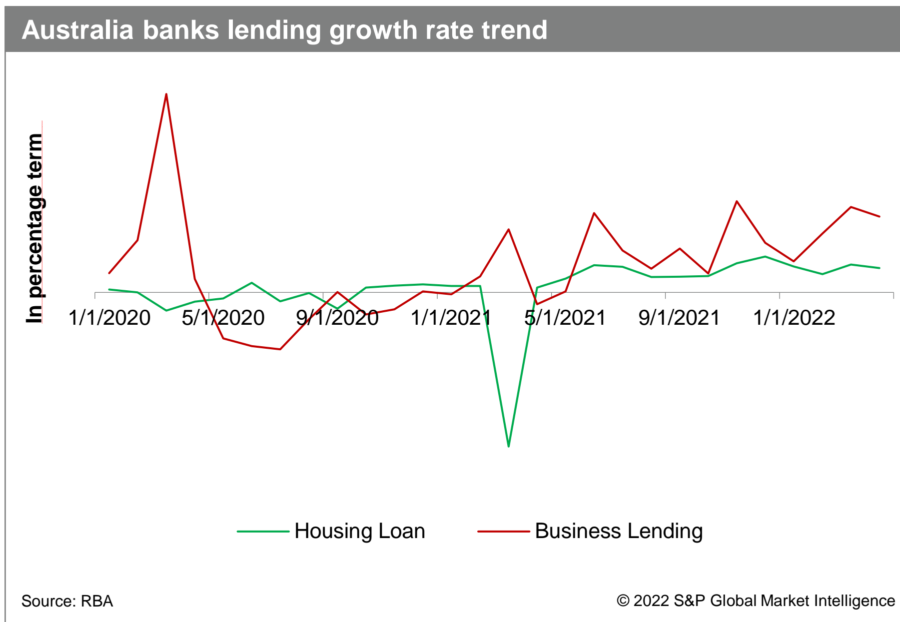
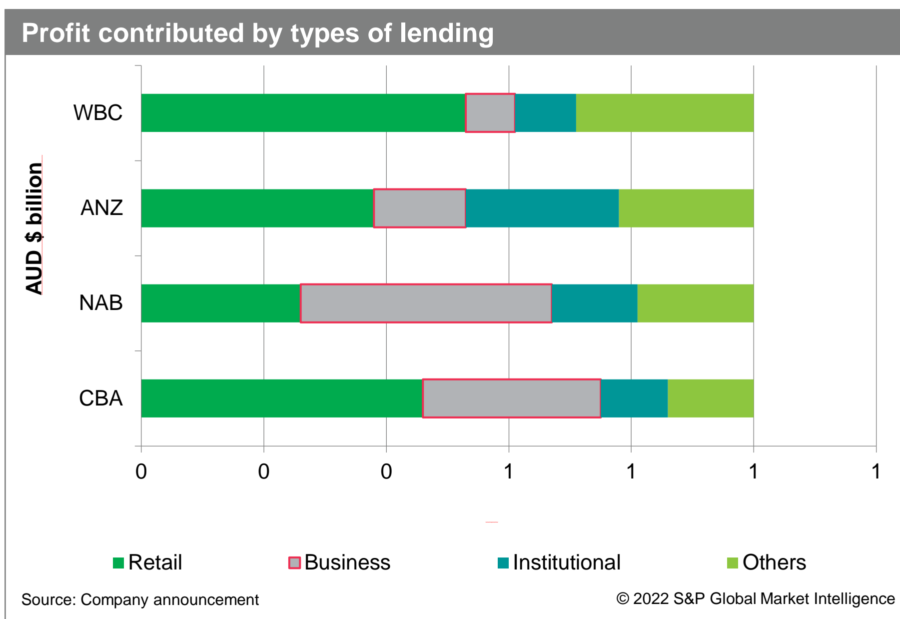
The battle against inflation—Australia, Singapore, South Korea, Malaysia, and India's dissimilar growth potential

Australia and Singapore are two APAC developed markets that are affected by high inflation. Both countries have tightened the monetary in their own way. For Australia, Reserve Bank of Australia followed the steps of most of the developed economies and raised the official interest rate twice within a span of a few weeks, bringing the previous historical-low interest rate of 0.1% to 0.85%. However, Singapore, the city-state that heavily relies on imports, adjusted the slope of the Singapore dollar nominal effective exchange rate (S$NEER) policy band—the band that Singapore dollars are allowed to fluctuate against a basket of major trading currencies. The larger room for the Singapore dollar to appreciate makes imports less expensive.

The higher interest rate will undoubtedly give Australian banks a breather to their net interest margin (NIM), as the banks have been experiencing margin compression over the past two years in the low interest rate environment. We notice that the NIM has already stabilized for the banks in the latest financial results ending March 2022, with more growth potential to kick in from the second half of this year onward. However, the tailwind from the higher interest rate is not expected to benefit the banks the same way, owing to the different level of competitiveness in the loan market, cost control capability, and assets mix. As per the data released by the Reserve Bank of Australia (RBA), banks' loan books continued to grow at the fastest pace since 2008. This is mainly attributable to the acceleration of business lending, as companies reemerge from lockdowns and increase in spending. On the other hand, mortgage lending growth appears to have stabilized. We expected the banks with more entrenched positions in the business loan segment to be in a better position to capitalize on the favorable trend. The business lending segment, which primarily serves small and medium enterprises, is also more lucrative compared with mortgages or institutional lending. **Commonwealth Bank of Australia (CBA:AU000000CBA7)** and **National Australia Bank (NAB:AU000000NAB4)** are expected to be the winners on this front, widening the gap between them and **Australia & New Zealand Banking Group (ANZ:AU000000ANZ3)** and **Westpac Banking Corp (WBC:AU000000WBC1)**. The following figures provide some indication of this trend.





We anticipate the trend to translate into better growth potential for outperformers' dividends. We expect CBA to increase total dividend to A$3.85 per share for FY 2022, representing an increase of 10%. For NAB, we project the bank to increase total dividend by 12.5% to A$1.43 per share for FY 2022. Whereas for ANZ and WBC, we see the dividend growth rate to be merely around 1% and 3%, respectively. However, the increase in interest is not all positive for banks; there are downside risks too. This is reflected in the market sentiment on the day when RBA announced a 0.5% increase in rate—ASX200 fell into red as the market was concerned about the risk of rising defaults on borrowings. This is something worth looking out for in the banks' financial disclosures going forward.

The rise in interest rate is expected to be the differentiator for the banking trio in Singapore too, namely **DBS Group Holding (DBS: SG1L01001701)**, **Oversea-Chinese Banking Corp (OCBC:SG1S04926220)**, and **United Overseas Bank Limited (UOB: SG1S04926220)**. DBS is expected to be best positioned for the rising

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rates because of the high portion (close to 94%) of its deposit in current account and savings account (CASA), which is a low-cost way for banks to fund liabilities. The high sensitivity to the rate, coupled with strong digital capability is expected to give the bank the edge for a wider NIM expansion. We expect the bank to increase its FY 2022 dividend to S$1.44 per share, with S$0.36 per share to be paid each quarter. The amount represents a strong annual growth rate of 20%, as compared with OCBC's 9% and UOB's 11.6%.

The Bank of Korea is the earliest and most proactive central bank in APAC to deliver a back-to-back interest rate hike to combat inflation. To ensure the banking system remains solid while tightening the monetary policy amid the slowed economic growth, government announced on 7 June 2022 that financial support programs for small and medium-sized enterprises (SMEs) will be extended by another six months to the end of this year to avoid a hard-landing for the backbone of the economy. This includes extension of loan maturity, interest rate cuts, and new financing to operating SMEs facing liquidity issues. Currently, there are 226 SMEs under the scheme, and the number is expected to increase. Despite the tightened monetary actions, Korean banks' financial position remains sound. As per the recent data released by Financial Supervisory Service, although household loans softened owing to weak demand, corporate loans continue to grow, owing to the reduced government COVID-19 subsidies and increased production volume in hope of economy recovery. The market consensus for large, medium, and small office loans growth is expected to remain solid.

Korean banks' earnings and dividends for the current financial year are expected to be pushed up by a few factors apart from the NIM expansion from higher interest rate. As reflected by **KB Financial Group (KR7105560007)**'s Q1 FY 2022 results, net profits increased by 14% on a year-on-year basis, primarily owing to the 82 Korean won billion provisions released in light of the improving situation. This came much later than its global peers in the banking sector owing to prudent steps taken by the bank in risk management. As per the official data, the eight major banks in Korea have accumulated around 3.4 trillion won in pandemic-related provision over the past two years, representing around 13% of combined pre-tax income of banks. Korean banks' dividends are expected to be pushed not only by increase in earnings but also the banks' initiatives to enhance shareholder returns. To increase shareholder confidence and rejuvenate the subdued share prices performances, drastic changes have been implemented by the banks over the past two year. This includes increasing the frequency of payment and payout ratio.

South Korea top banks shareholder return summary

	KB	Shinhan	Hana	Woori
Previous payout frequency	Annually	Annually	Semi-annually	Annually
Payout frequency	Quarterly since FY 2022	Quarterly since FY 2021	Semi-annual since FY 2005	Semi-annual since FY 2021
Mid/long-term target payout ratio	30%	30%	30%	30%
FY 2022 payout ratio*	28%	18%	28%	29%
FY 2022 DPS(E), KRW	3,400	1,600	3,500	1,100
Amount confidence rank	Medium	Low	Medium	Low
FY 2022 DPS growth (E)	55%	-18%	13%	22%
FY 2022 treasury share cancellation confirmed, KRW	150 bln	150 bln	150 bln	-
Previous payout frequency	Annually	Annually	Semi-annually	Annually

Note: *Our payout ratio assumption is relevant for cash dividend only. This does not include treasury share repurchase/cancellation.

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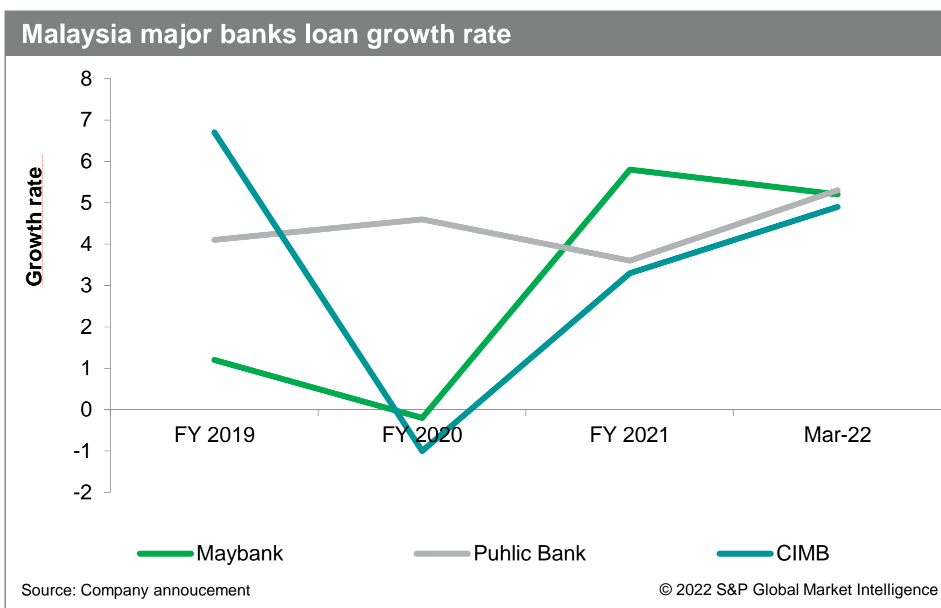
As one of the key APAC trading nations deeply plugged in the global supply chain, Malaysia's economy is facing challenges too. The latest figures show that CPI rose year on year by 2.3% in April for Malaysia. Despite the modest increase, the central bank of Malaysia joined its peers in APAC to hike the overnight interest policy rate in May. Food inflation in April was higher than the rest of the goods and reached 4.1%, as Malaysia is a net

importer. The rate hike is to lessen the further depreciation pressure of its currency, ringgit, against US dollar, which might exacerbate the inflationary pressure. In such an environment, we expect the dividends from Malaysian banks to continue to grow. We expect top players such as **Malayan Banking Bhd (MYL1155OO000)** and **Public Bank Bhd (MYL1295OO004)** to increase dividend by around 7% and 2.6%, respectively. Before the pandemic, banks in Malaysia have been committed to pay progressive dividends. When the pandemic hit in 2020, although the major banks suspended dividends as a conservative play, they soon compensated the shareholders with increment in dividends. Going forward, we expect the banks' dividends to resume their progressive trajectory. Malaysian banks have been maintaining good liquidity and assets quality ratio as compared with regional peers, allowing them to continue their commitment to shareholder returns. We also notice in the banks' Q1 FY 2022 results that NIMs have stabilized, with solid loan growth brought about by the recovery of the economy. We expect all those factors to cushion the downside risks on dividend for the current financial year, despite the one-off prosperity tax imposed on banks in the first quarter this year.



India's central bank raised its benchmark repo rate by 40 basis points to 4.4% at an unscheduled review of its monetary settings on 4 May, marking the first hike in nearly four years. Dividends from Indian banks including **HDFC Banking (INE040A01034)**, **State Bank of India (SBI: INE062A01020),** and **ICICI Bank (INE090A01021)** are expected to grow strongly owing to solid credit growth and improving assets quality and widening of NIM. As per the data released by the Reserve Bank of India, bank credit growth reached its highest level in three years at 13.1%. Multiple factors contributed to the growth, including the normalization of companies' working capital requirement, which had fallen during the pandemic. From the FY 2022 financial results, HDFC reported a 21% increase in loans; SBI's gross advances increase by 11%; ICICI bank reported a 17.1% year on year growth. The growth on toplines is accompanied by the decline in provision owing to the improvement in asset quality, boosting the growth in net profit. We expect aggregate dividends denominated in US dollar to increase by around 18.3% in FY 2023 (most of the bank already concluded FY 2022 and released results in April). **HDFC** is expected to be the outperformer as the largest private bank in India. The bank's assets more than doubled from the period of FY 2017 to FY 2022 from 5,586 billion rupees to 13,805 billion rupees. Its earning performance has demonstrated resilience across cycles. The bank's announcement to acquire the mortgage lending behemoth Housing Development Finance Corp (HDFC) is expected to provide further competitive edge to expand customer base and explore new revenue channel.

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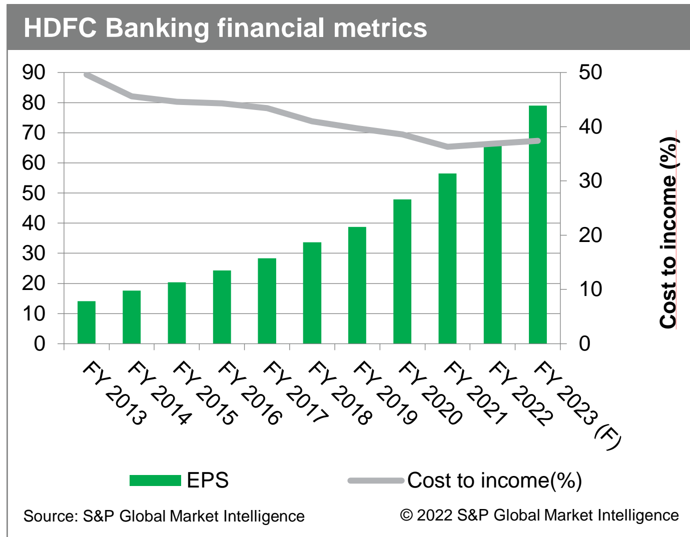

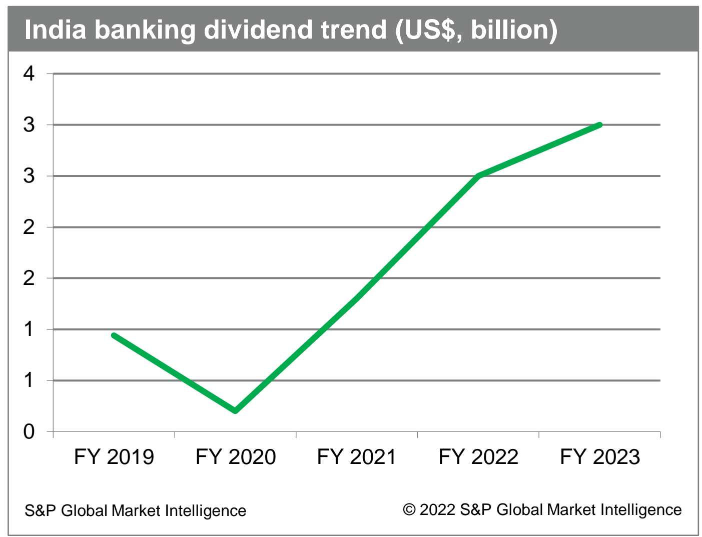

Top APAC banks' upcoming payments

Name	ISIN	Amount forecast	Amount confidence	XD forecast	XD forecast confidence
China Construction Bank Corp	CNE1000002H1	CNY0.39	Medium	28-Jun-23	Medium
Industrial and Commercial Bank of China	CNE000001P37	CNY0.2955	Medium	12-Jul-23	Low
Agricultural Bank of China	CNE100000RJ0	CNY0.2107	Medium	17-Jul-23	Low
Bank of China Ltd.	CNE000001N05	CNY0.25	Medium	17-Jul-23	Low
China Merchants Bank Co Ltd	CNE000001B33	CNY1.522	High	15-Jul-22	Medium
Commonwealth Bank of Australia	AU000000CBA7	AUD2.1	Medium	17-Aug-22	High
Industrial and Commercial Bank of China	CNE1000003G1	CNY0.303	Medium	04-Jul-23	Medium
Industrial Bank Co	CNE000001QZ7	CNY1.07	Low	16-Jun-23	Low
Westpac Banking	AU000000WBC1	AUD0.61	Medium	17-Nov-22	High
National Australia Bank Ltd	AU000000NAB4	AUD0.7	Medium	15-Nov-22	High
Postal Savings Bank of China	CNE100003PZ4	CNY0.2688	Medium	12-Jul-23	Low
Mitsubishi UFJ Financial Group	JP3902900004	JPY16	High	29-Sep-22	High
Australia & New Zealand Banking Group	AU000000ANZ3	AUD0.72	Medium	07-Nov-22	High
DBS Group Holdings Ltd ORD	SG1L01001701	SGD0.36	Medium	15-Aug-22	Medium
Shanghai Pudong Development Bank	CNE0000011B7	CNY0.41	Medium	22-Jul-22	Low
Bank of Communications	CNE1000000S2	CNY0.349	Medium	12-Jul-23	Medium
Sumitomo Mitsui Financial Group	JP3890350006	JPY110	High	29-Sep-22	High
Oversea-Chinese Banking Corp	SG1S04926220	SGD0.27	Medium	11-Aug-22	Medium
BOC Hong Kong (Holdings) Limited	HK2388011192	HKD0.469	Medium	14-Sep-22	Medium
China Construction Bank Corp	CNE1000002H1	CNY0.39	Medium	28-Jun-23	Medium

Note: Data sorted by aggregate dividend in FY 2023

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