25 February 2011
Asia Pacific/Malaysia
Equity Research
Banks

RHB Capital

(RHBC.KL / RHBC MK)

Rating	**OUTPERFORM***
Price (23 Feb 11, RM)	8.10
Target price (RM)	11.80[1]
Chg to TP (%)	45.7
Market cap. (RM mn)	17,443 (US$ 5,725)
Enterprise value (RM mn)	17,443
Number of shares (mn)	2,153.48
Free float (%)	27.00
52-week price range	8.72 - 5.28

**Stock ratings are relative to the relevant country benchmark.*
[1]Target price is for 12 months.

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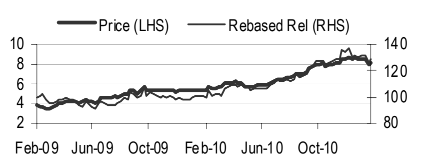
INITIATION

Transformers

- **Initiate with OUTPERFORM.** We initiate coverage on RHB Capital with an OUTPERFORM rating and a 12-month target price of RM11.80 (based on the Gordon Growth model), implying 46% potential upside. We are bullish on RHB for the following reasons: (1) the group's differentiated retail banking strategy which could lead to positive earnings surprises, (2) it is well positioned to be among the biggest beneficiaries of Malaysia's Economic Transformation Programme (ETP), (3) it is the cheapest large cap bank, (4) it is underowned by foreigners (12% foreign ownership versus the sector average of 23%).
- **Poised for huge market share gains.** We believe there is significant potential upside to its market share and profitability, which will be driven by: (1) a differentiated retail banking strategy that could significantly boost loan and deposit market shares and (2) aggressive efforts to grow non-interest income by capitalising on its relationship with EPF (National Pension Fund).
- **Best play on ETP.** RHB is arguably one of the best plays on ETP. Our house view is that the market has underestimated the economic impact of the ETP and we are beginning to witness early evidence of government execution. We believe RHB is well positioned to benefit from the following effects of the ETP: (1) increase in infrastructure and capital market activity, which will require active participation by EPF, (2) significant boost to loan growth should private investments pick up sharply, (3) creation of over two million new jobs in the mass market segment targeted by RHB.
- **Trades at 30% discount to local peers.** RHB trades at 2011E P/E of 10x (versus sector average of 14x, market P/E of 15x and regional peer average of 11x) and a P/B of 1.8x (with projected 2011 ROE of 16.4%). Key price catalysts are: (1) sell-down by EPF to enhance trading liquidity, (2) positive data points on market share gains and (3) completion of rights issue to fund its Indonesian acquisition that would remove overhang on the stock.

Share price performance



The price relative chart measures performance against the KUALA LUMPUR COMPOSITE index which closed at 1498.39 on 23/02/11
On 23/02/11 the spot exchange rate was RM3.05/US$1

Performance Over	1M	3M	12M
Absolute (%)	-4.7	1.6	52.0
Relative (%)	-2.4	0.0	27.4

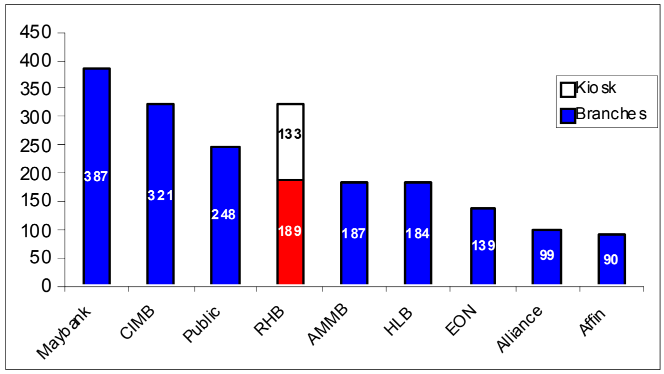
Financial and valuation metrics

Year	12/10A	12/11E	12/12E	12/13E
Pre-prov Op profit (RM mn)	2,410.6	2,867.3	3,428.4	4,029.9
Pre -tax profit (RM mn)	1,899.3	2,309.6	2,802.3	3,304.8
Net attributable profit (RM mn)	1,420.3	1,732.2	2,101.7	2,478.6
EPS (CS adj.) (RM)	0.66	0.80	0.98	1.15
Change from previous EPS (%)	n.a.			
Consensus EPS (RM)	n.a.	0.72	0.81	0.92
EPS growth (%)	18.2	22.0	21.3	17.9
P/E (x)	12.3	10.1	8.3	7.0
Dividend yield (%)	2.4	3.0	3.6	4.3
CS adj. BVPS (RM)	4.6	5.2	5.9	6.7
P/B (x)	1.8	1.6	1.4	1.2
ROE	15.2	16.4	17.6	18.3
ROA (%)	1.2	1.2	1.3	1.3
Tier 1 Ratio (%)	10.5	10.0	9.6	9.2

Source: Company data, Thomson Reuters, Credit Suisse estimates.

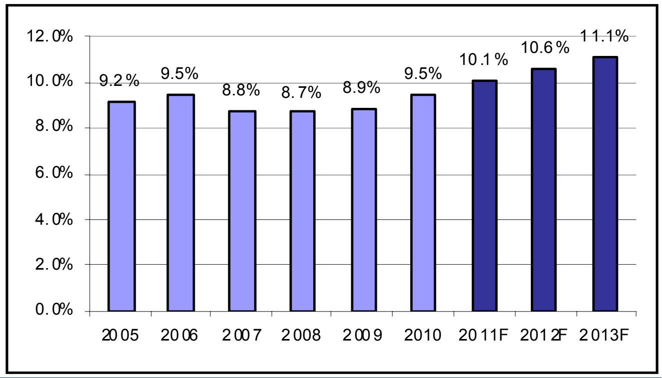
Focus charts

Figure 1: **Expanding footprint using "EASY" kiosks**



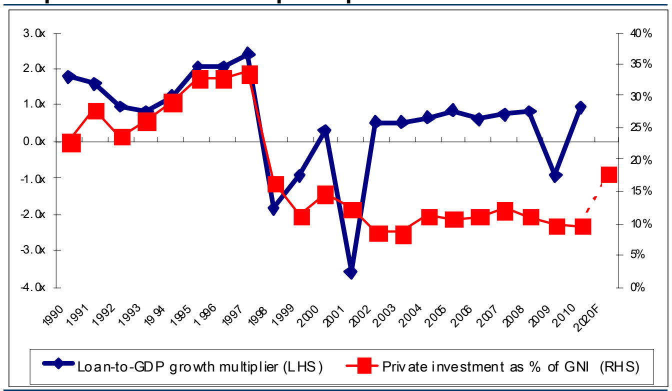
Source: Company data, Credit Suisse estimates

Figure 2: **RHB's loan market expected to rise further**



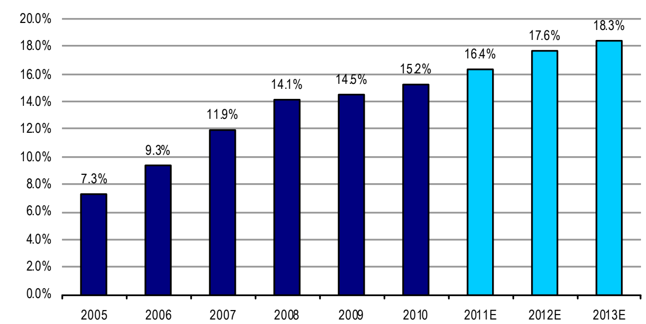
Source: Company data, Credit Suisse estimates

Figure 3: **System loan-to-GDP growth multiplier could rise as private investments pick up with ETP roll-out**



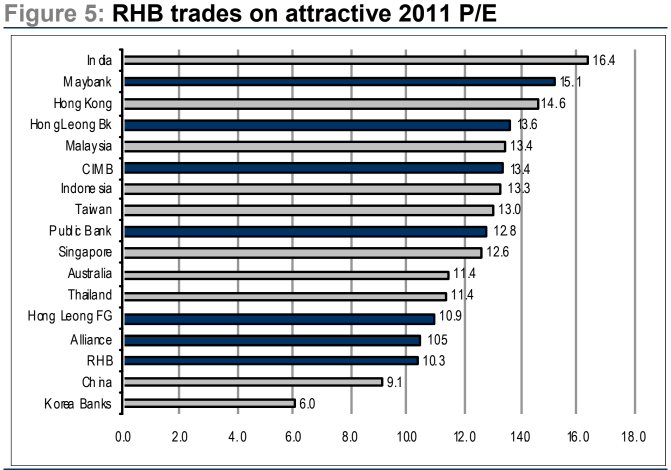
Source: Company data, Credit Suisse estimates

Figure 4: **ROE poised to expand further**



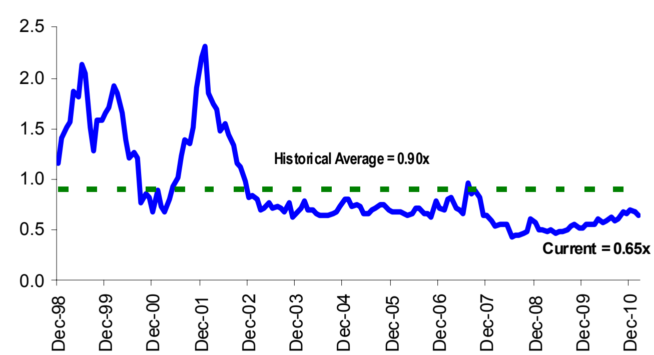
Source: Company data, Credit Suisse estimates

Figure 5: **RHB trades on attractive 2011 P/E**



Source: Company data, Credit Suisse estimates

Figure 6: **Trading at sizeable discount to market P/E**



Source: Company data, Credit Suisse estimates

Transformers

We are initiating coverage on RHB Capital with an OUTPERFORM rating and a 12-month target price of RM11.80 (based on Gordon Growth model) implying 46% potential upside. Our positive call on RHB is supported by the following:

Target price of RM11.80 implies 46% potential upside

Poised for huge market share gains

We believe there is significant potential upside to RHB's market share and profitability, which will be driven by: (1) its differentiated retail banking strategy (called "EASY") that could significantly boost loan and deposit market shares and (2) aggressive efforts to grow non-interest income by capitalising on its relationship with EPF (National Pension Fund). EASY allows RHB to expand its footprint rapidly at a significantly lower cost through setting up kiosks and is aimed at increasing penetration of the underserved mass market customer segment. Combining its branch network with EASY outlets, RHB has the second largest footprint in Malaysia (from the fourth largest branch network). Apart from its scalability, the key competitive advantage of EASY is that all transactions (including loan products) are processed in less than 10 minutes and are paperless. So far loan products sold (namely personal and unit trust loans) through EASY have seen a major jump in market share, and we believe that the expansion of its product range to target bigger-ticket loan segments could considerably increase RHB's market share.

Expanding product offering at EASY kiosks could be a massive boost to market share

Best play on Economic Transformation Programme

RHB is arguably one of the best plays on the ETP. Our house view is that the market has underestimated the economic impact of the ETP and we are beginning to witness early evidence of government execution. We believe RHB is well positioned to benefit from the following effects of the ETP:

ETP could result in upside to loan growth, capital market activity and increase in addressable market for RHB

- Increase in infrastructure and capital market activity, which will require active participation by EPF (who is likely to engage RHB for any mandate).
- Significant boost to loan growth should private investments pick up sharply (historically loan-to-GDP growth multiplier has been highly correlated with private investments).
- Creation of over 2 mn new jobs in the mass market segment which is targeted through RHB's EASY strategy

Earnings upside from fixing operational flaws

While management has substantially improved profitability of RHB over the past few years, we believe that there is further upside to ROE should the group address certain operational imperfections. From our analysis of RHB's ROE breakdown compared to its peers, we find that the key areas where the group is underperforming its peers are: (1) below average NIM, (2) non-interest income ratio of 26% is below industry average of 31% and (3) credit cost is comparatively higher. We believe that through EASY, good strategic partnerships and its relationship with EPF, the group can address these weaknesses.

Trades at 30% discount to local peers

RHB trades at 2011E P/E of 10x (versus sector average of 14x, market P/E of 15x and regional peer average of 11x) and a P/B of 1.8x (with projected 2011E ROE of 16.4%). Key price catalysts are: (1) sell-down by EPF to enhance trading liquidity, (2) positive data points on market share gains, (3) completion of rights issue to fund its Indonesian acquisition that would remove overhang on the stock. Our calculations suggest that RHB's current P/B valuation implies an ROE of 14% (compared to CS's estimate of 16.4% in 2011), which we believe grossly understates the earnings potential of the group.

Trades at 10x 2011E P/E vs local peer average of 14x

Financial summary

Figure 7: Profit and loss summary

Year-end Dec 31 (Rm mn)	2009A	2010A	2011F	2012F	2013F
Net interest income	2,739.4	3,007.0	3,478.9	4,061.3	4,687.8
Non-interest income	925.6	1,043.3	1,181.7	1,307.3	1,421.7
Net banking income	3,665.0	4,050.3	4,660.6	5,368.6	6,109.5
Total operating expenses	(1,565.8)	(1,639.6)	(1,793.3)	(1,940.2)	(2,079.7)
Operating profit	2,099.2	2,410.6	2,867.3	3,428.4	4,029.9
Loan-loss provisions	(561.3)	(512.2)	(557.7)	(626.1)	(725.1)
Income before tax	1,538.4	1,899.3	2,309.6	2,802.3	3,304.8
Tax	(329.8)	(470.7)	(577.4)	(700.6)	(826.2)
Reported net income	1,201.4	1,420.3	1,732.2	2,101.7	2,478.6

Source: Company data, Credit Suisse estimates

Figure 8: Balance sheet summary

Year-end Dec 31 (Rm mn)	2009A	2010A	2011F	2012F	2013F
Cash and cash equivalents	19,204.7	16,237.6	18,603.3	20,621.0	23,167.4
Net Loans	66,923.1	81,228.1	95,738.2	110,916.6	127,379.0
Investments	22,527.0	25,604.0	30,212.7	35,046.7	40,303.7
Fixed and other assets	6,296.6	6,255.8	6,463.2	6,688.7	6,933.9
Total assets	**114,951.4**	**129,325.5**	**151,017.5**	**173,273.1**	**197,784.0**
Interbank	7,416.0	10,066.2	11,072.8	12,014.0	12,975.1
Total customer deposits	84,841.1	94,433.8	113,320.6	132,585.1	153,798.7
Borrowings	7,238.5	8,147.1	8,294.4	8,449.0	8,617.0
Other liabilities	6,748.1	6,716.2	7,155.0	7,579.2	8,012.2
Total liabilities	**106,243.6**	**119,363.3**	**139,842.8**	**160,627.2**	**183,403.1**
Share capital	2,153.5	2,153.5	2,153.5	2,153.5	2,153.5
Shareholders' equity	**8,707.7**	**9,962.2**	**11,174.7**	**12,645.9**	**14,380.9**
Total liab. and shareholders' equity	**114,951.4**	**129,325.5**	**151,017.5**	**173,273.1**	**197,784.0**

Source: Company data, Credit Suisse estimates

Figure 9: Key ratios

Year-end Dec 31 (Rm mn)	2009A	2010A	2011F	2012F	2013F
Return and efficiency measures (%)					
ROAE	14.54	15.21	16.39	17.65	18.34
ROAA	1.09	1.16	1.24	1.30	1.34
Net interest margin	2.67	2.60	2.61	2.62	2.63
Non-interest income (% of revenue)	25.3	25.8	25.4	24.4	23.3
Cost/income	42.7	40.5	38.5	36.1	34.0
Cost/average assets	1.43	1.34	1.28	1.20	1.12
Balance sheet (%)					
Asset/equity (x)	13.2	13.0	13.5	13.7	13.8
RWCR (total)	13.8	13.8	14.6	13.8	13.2
Gross impaired loan ratio (%)	4.7	4.4	4.1	3.8	3.6
Impaired loan coverage (%)	83.4	67.6	75.9	84.0	92.3
Loans/deposits (%)	82.1	88.6	87.2	86.4	85.7
Key assumptions (%)					
Gross loan growth	10.3	20.2	18.0	16.0	15.0
Interest spread	2.07	1.98	1.91	1.97	2.01
Non-interest income growth	-2.3	12.7	13.3	10.6	8.7
Overhead expense growth	3.5	4.7	9.4	8.2	7.2

Source: Company data, Credit Suisse estimates

Poised for huge market share gains

RHB has recorded a quantum leap in ROA over the past five years (0.4% in 2005 to 1.2% in 2010) on the back of a pick up in loan growth, NIM expansion, improvements in cost-to-income ratio and credit cost reduction. Despite the sharp turnaround in RHB's ROA over the past five years, we believe there is further potential upside which will be driven by: (1) a differentiated retail banking strategy that should translate to substantial market share gains and (2) aggressive efforts to grow non-interest income.

ROA has more than doubled over the past five years

Differentiated retail banking strategy

"Easy by RHB"—a game changer

We believe that RHB has formulated an innovative kiosk-banking strategy known as "EASY by RHB" (launched in early 2010) to rebuild its retail banking footprint in Malaysia. EASY allows RHB to expand its footprint rapidly at significantly lower costs through setting up of kiosks (compared to branch expansion) and is aimed at increasing penetration of the underserved mass market customer segment.

EASY launched in early 2010

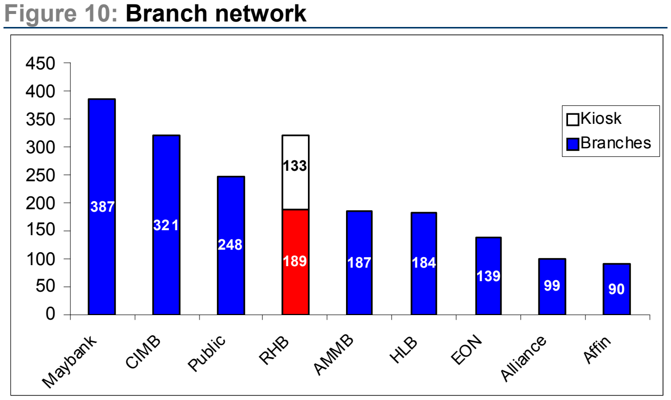
What is "Easy by RHB" ?

EASY was launched in early 2010; its key features are as follows :

- **Expansion of footprint through kiosks.** Since the start of 2010, RHB has set up 133 kiosks and management has set a target of expanding to 240 kiosks by end-2011 and 400 kiosks by end-2012. Each kiosk is a make-shift standalone outlet which is equipped with an ATM and cash deposit machine. By combining the kiosks with its 189 branches (fourth largest and just marginally ahead of the fifth and sixth largest players), RHB now has close to 322 outlets (only behind Maybank) and is on track to expand to 429 outlets by end-2011 (largest footprint in the country). To cater to rapid expansion in customers through EASY, RHB has also substantially beefed up its self-service terminal network to 1,656 terminals, the third largest in the country (from sixth prior to 2008).

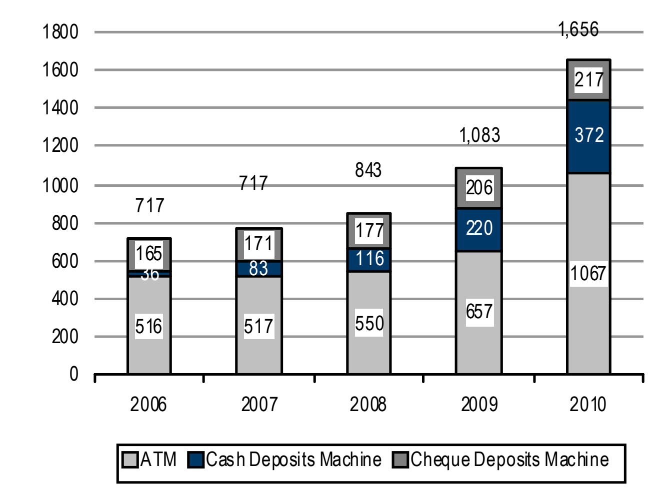
Combining kiosks and branches, RHB has 2nd largest footprint in Malaysia

Figure 10: **Branch network**



Source: Company data, Credit Suisse estimates

Figure 11: **RHB's self-service terminals**



Source: Company data

- **Strategic locations for the kiosks to target mass market.** EASY is aimed at increasing market share of customers in the mass market segment (household income of <RM5,000/month), which management believes accounts for 70% of the total consumer market and is currently underserved. To get kiosks to effectively penetrate the mass market segment, RHB's management selects locations that are frequented

by the middle income population group. RHB has also entered into arrangements with the following partners :

Tie-ups with Tesco, POS and RapidKL

(1) **Tesco** – RHB entered into an exclusive tie-up to set up kiosks in its stores. So far RHB has set up kiosks in 33 out of Tesco's 36 stores.

(2) **POS Malaysia** – RHB has an agreement with POS to set up kiosks at its post offices. POS has 550 post offices throughout the country. So far RHB has set up kiosks in 30 post offices and intends to eventually expand to 80 post offices. In addition, RHB has entered into a shared banking service agreement with POS that will involve 333 POS branches. At the moment, RHB has set up shared banking service arrangements at 21 branches.

(3) **RapidKL** (Light Rail Transit operator) – RHB has entered into partnership with RapidKL, which operates the Klang Valley light rail transit system, to set up EASY outlets at selected LRT stations. So far, RHB has set up EASY outlets at nine LRT stations.

EASY is scalable and costs less than branches

- **Lower cost, shorter breakeven period and faster roll-out.** A key advantage of EASY is that it is very scalable. The cost of setting up the kiosks is one-sixth of a branch and breakeven period is typically less than one-third of a branch. The kiosks can be set up quickly (unlike branches) and are easily movable. Each kiosk is manned by one to six staffers, mostly on temporary employment contracts.

- **Extended operating hours.** EASY kiosks are open everyday and operate on extended operating hours compared to normal bank branches.

Combines MyKAD technology with EPF and credit bureau database

- **Processing time below ten minutes and no forms to fill.** The main advantage of EASY is that it is extremely convenient and fast. All transactions are paperless and can be completed within ten minutes. The breakthrough application is the ability to approve loans and disburse cash within ten minutes without compromising credit quality. This is only possible in Malaysia with a combination of the following:

  (1) **Use of MyKAD** – Every Malaysian citizen carries an identity card (known as "MyKAD"), which has a microchip embedded that stores detailed personal information. Each loan applicant is required to scan his/her MyKAD together with a fingerprint biometric scan to verify the cardholder's identity.

  (2) **EPF's database** – Through its collaboration with EPF, RHB is able to link up with the EPF database to gain instant access to salary and savings records of loan applicants.

  (3) **Credit bureau** – Malaysia also has a well-established credit bureau that has been in operation since 1982 with comprehensive credit information on all borrowers in the banking system. With the MyKAD, RHB is able to tap the credit bureau database to check on the credit exposure and debt service record of loan applicants.

  While some of the above mentioned data are available in other countries, Malaysia is in a unique position to have a combination of all three to provide sufficient information for credit assessment.

Six products offered now

- **Limited product offering for now.** At the moment, RHB only offers six products at its EASY kiosks, comprising two loan products, two savings products and two insurance products. However, we understand that management intends to expand the product offering over time. We briefly describe below the salient features of the six products:

  (1) **Personal loans** – Through EASY, RHB offers flexible financing ranging from RM2,000 to 50,000 with repayment period of up to 60 months. Borrowers will be charged effective interest rates of 21-24% p.a. This typically takes more than a day at other banks.

Low-risk loans with zero default rate so far

(2) **Bumiputera unit trust (ASB) loans** – Borrowers can obtain a loan for 100% of the investment amount (ranging from RM10,000-200,000) with a tenure of 10-25 years to invest in Amanah Saham Bumiputera Unit trust (ASB, unit trust for Bumiputeras or Malays). RHB charges an interest rate of BLR less 1% (equivalent to 5.3% p.a.) and monthly repayments are low in the first five years of the loan (mainly interest service without principal repayment). Over 2007-2009, ASB achieved returns of 8-9% p.a. and has historically yielded returns in excess of 7% p.a. As such, we believe that the credit risk for these loans is negligible. Only two other local commercial banks, namely Maybank and CIMB, are authorised to grant ASB loans. Other banks take up to four days to process these loans compared to ten minutes at EASY kiosks.

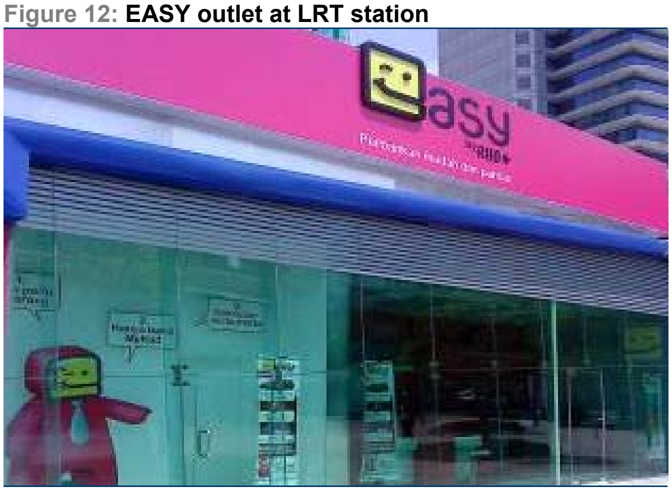
(3) **Debit card** – At the kiosks, customers can also apply for a visa debit card which can be activated instantly within ten minutes. To open an account, customers only need to deposit a minimum of RM20. The customer need not fill out any forms as the information required would be downloaded from their MyKAD. Debit card benefits include entitlement to VISA privileges through its merchant network worldwide, access to more than 1.2 mn ATMs worldwide and monthly SMS on account balance.

(4) **Savings deposit account opening** – At the kiosks, customers can also open savings deposit accounts on-the-spot in less than ten minutes without having to fill in any forms. Account openings take at least 30 minutes at other banks' branches.

(5) **Personal accident insurance coverage** – The kiosks also offer personal accident coverage, with monthly premiums starting from as low as RM15 (or an annual premium of RM3.60 per RM1,000 sum insured) for an insured sum of RM50,000. No documentation is required and coverage can commence in less than 10 minutes.

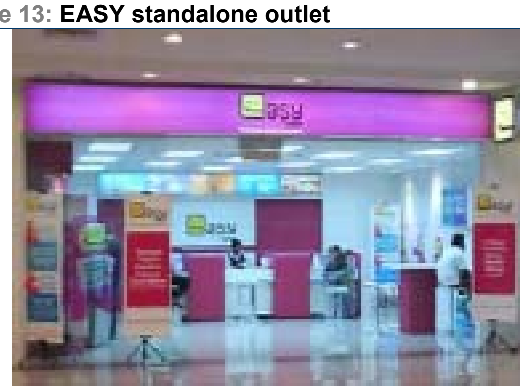
(6) **Life insurance coverage** – Customers can also purchase life insurance coverage that provides protection against death and total permanent disability at the kiosks. The comprehensive protection costs as low as RM1.80 per day for an insured sum of RM25,000. Approval can be obtained in 10 minutes, and buyers are not required to provide any documents or undergo a medical examination.

Figure 12: **EASY outlet at LRT station**



Source: Company

Figure 13: **EASY standalone outlet**



Source: Company

Figure 14: **EASY kiosk at POS Malaysia**

Source: Company

Figure 15: **EASY kiosk at TESCO**

Source: Company

EASY has been a success so far

EASY has so far been a huge success and among the positive results so far are :

- **RHB recorded highest loan growth among local banks in 2010** – Since its launch, RHB has generated RM1.2 bn (1.4% of RHB's loan base) of assets through EASY and is growing at a rate of RM100 mn per month. EASY has so far been most effective in growing ASB loans, which accounts for some 70% of EASY's asset growth. As a result, RHB's loans grew at an annualised 20% up to end-2010, which is the highest among local banks and well above system growth of 12.8%.

RHB's loan growth of 20% was highest among local banks and well above system's 12.8%

- **Deposits grew RM100 mn** – EASY also managed to collect some RM100 mn worth of deposits, somewhat unimpressive in comparison to the asset growth.

- **Successful in acquiring new customers** – So far, some 70% of EASY's customers are completely new customers to RHB. This demonstrates that EASY is a great tool for customer acquisition and is able to penetrate segments of the population that are beyond the reach of its traditional distribution channels.

EASY has also been attracting a lot of new customers

- **Huge gains in market share of ASB loans** – Despite charging higher interest rates (BLR less 1% vs competitors' BLR less 2.5%), the group's ASB loan growth of 80% in 2010 outpaced the industry average of 17%. As a result, RHB's market share of ASB loans surged to 15.6% (from 9.3% at end-2009), making it the second largest operator. RHB managed to grow at a faster rate primarily due to the convenience and speed of approval of its EASY outlets.

ASB market share jumped to 15.6% in 2010 (from 9.3% a year ago) despite charging higher interest rate

- **Personal loans' market share surged** – RHB's market share of personal loans also surged to 6.7% by end-2010 (from 5.6% a year ago) thanks to the rapid growth through EASY.

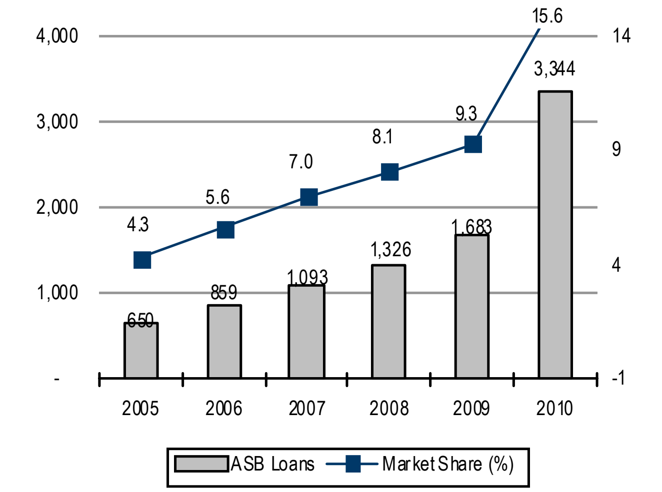
Also registered substantial gains in personal loan market share

- **Asset quality of loans intact** – Despite the rapid growth in loans, asset quality has been intact due to the quick albeit thorough credit evaluation process. The loan approval rates are not dissimilar to bank branches (30% approval for personal loans and 75% for ASB loans) and shows that the credit evaluation process at EASY outlets has been effective.

- **Much higher ROA versus group** – RHB has so far been able to realise an ROA of 3.5%, almost triple the group ROA of 1.2%, due to the lower operating cost, wider spreads and low credit cost of ASB loans.

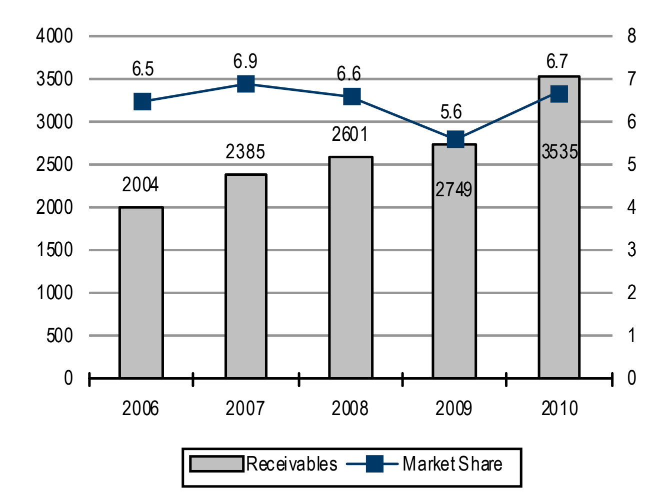
EASY generates ROA of 3.5% vs group ROA of 1.2%

Figure 16: ASB loan and market share trend



Source: Company data, Credit Suisse estimates

Figure 17: Personal loan trend



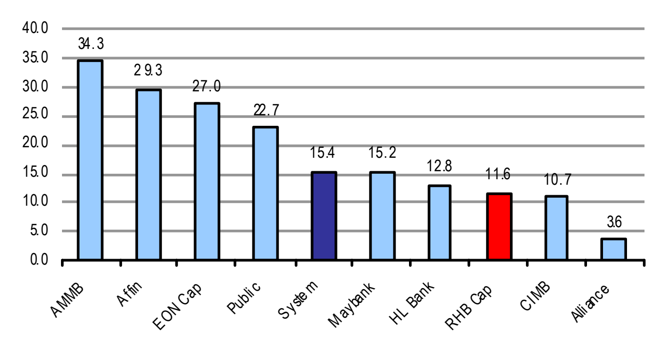
Source: Company data, Credit Suisse estimates

Expansion of product range could have a MASSIVE impact on RHB's market share

Plans to sell HP loans through EASY could have a huge impact on market share

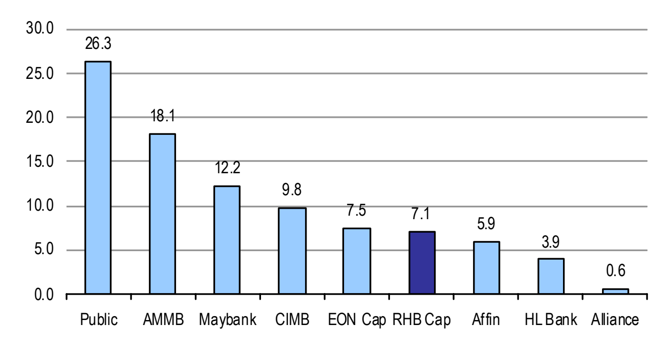
While the loan categories offered so far are small-ticket items that account for 7-8% of banking system loans, we believe that RHB management intends to launch other bigger-ticket loan products through its EASY kiosks, which could have a significant impact on its loan base. Among the loan products that will likely be introduced this year include hire purchase loans. Given that this is a much larger loan segment within the banking system (accounting for 15% of system loans), the launch of HP products could have a material impact on RHB's market share of the loan market. Compared to other local peers, RHB has a relatively small exposure to HP loans, which only accounts for 12% of its loans (please refer to chart below). RHB's market share of HP loans of 7% is below its overall loan share of 9.5%. Assuming EASY can enable RHB to raise its HP market share to 9.5%, the group's loan base would immediately expand by 4% or RM3 bn. Due to the convenience of using EASY, RHB might also be able to charge premium interest rates, similar to its ASB loans. We are forecasting loan growth of 15-18% over 2010-2013 and expect the group's loan market share to grow from 9.5% in 2010 to 11% by end-2013. Management also intends to introduce additional deposit-based products as the growth in liabilities has lagged asset growth.

Figure 18: HP as a % of total loans



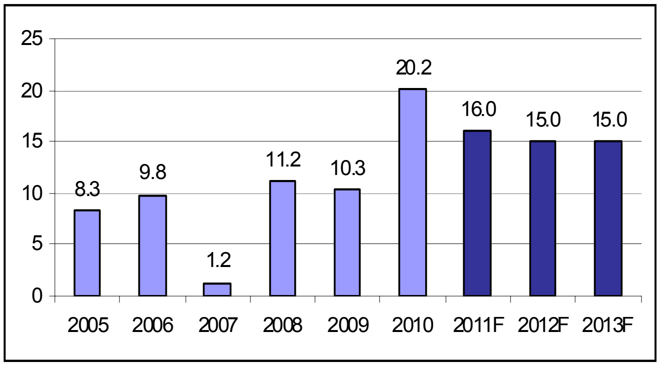
Source: Company data, Credit Suisse estimates

Figure 19: Market share of car loans



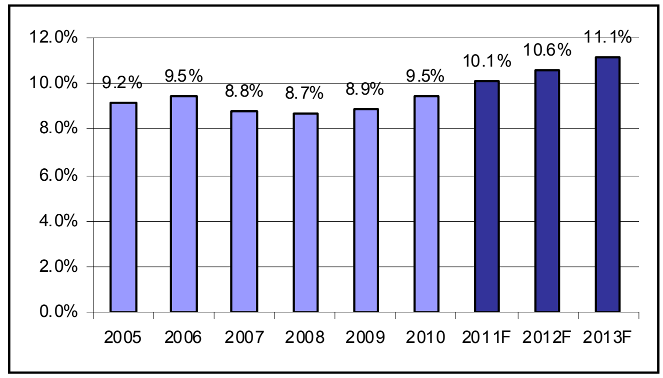
Source: Company data, Credit Suisse estimates

Figure 20: **RHB's loan growth**



Source: Company data, Credit Suisse estimates

Figure 21: **RHB's loan market share**



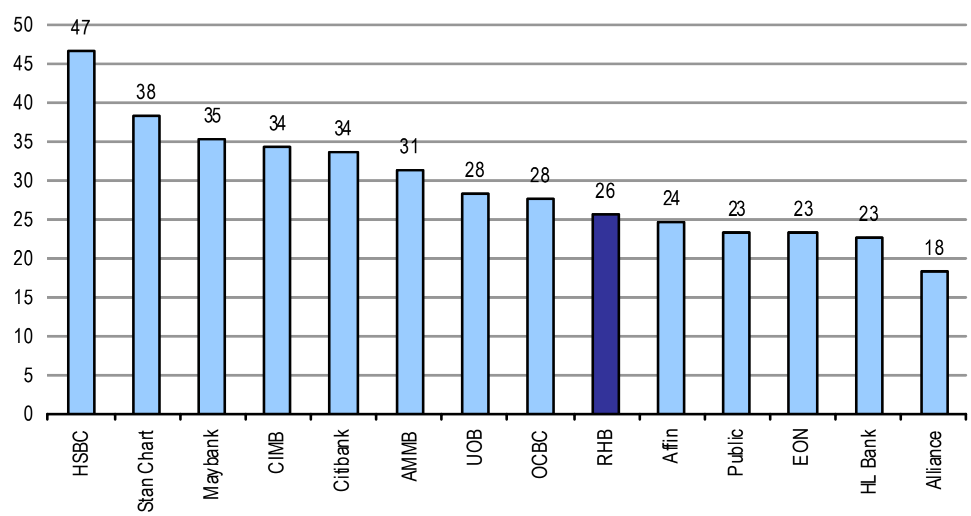
Source: Company data, Credit Suisse estimates

Initiatives to grow non-interest income

Management has also been focusing its efforts on boosting non-interest income. There is plenty of upside to non-interest income given that the group's non-interest income ratio of 26% (versus industry average of 31%) is among the lowest in the industry. We outline below some of management's key initiatives to enhance non-interest income.

RHB's non-interest income ratio below industry average

Figure 22: **Non-interest income ratio comparison**



Source: Company data, Credit Suisse estimates

Leveraging relationship with EPF to lift IB market share

RHB appears to be successfully leveraging its relationship with EPF to secure capital market mandates. This effort has resulted in a significant uplift in RHB's investment banking presence. Some of the notable achievements of RHB's investment banking unit in 2010 are :

Market share of M+A jumped to 59% in 2010 from 9% in 2009

- Most notable of all in 2010 was RHB's improvement in mergers and acquisitions (M+A) market share. In 2010, RHB emerged as the top adviser for mergers and acquisitions in South East Asia (ranked 21st in 2009) in terms of deal value, having worked on RM63.4 bn of deals.
- Domestically, RHB had 59% market share of M+A and ranked first.
- RHB's market share of equity capital market deals doubled YoY and the group ranked third among domestic banks on market share.

- RHB maintained its third position in market share of debt capital market deals but its market share slipped to 9.9% from 13.2% YoY.
- RHB improved its market share of the brokerage business to 6.6% in 2010 and ranking rose to fifth (from eighth).

We believe that EPF will play a major role in Malaysia's Economic Transformation Plans (ETP) and will likely be a key financier of a substantial portion of the entry point projects. As such, RHB is in an advantageous position to further enhance its investment banking revenue if the group continues to leverage its relationship with EPF.

Figure 23: RHB—investment banking market share and rankings

	2010		2009		2008	
	Mkt share (%)	Rank	Mkt share (%)	Rank	Mkt share (%)	Rank
M+A	58.8	1	9.0	3	9.6	4
Equities ^	7.7	3	8.9	3	16.6	3
Debt capital markets *	9.9	3	13.2	3	9.6	4
Brokerage	6.6	5	5.9	8	6.3	6

^ IPOs, rights and other issues, foreign brokers excluded

** Primary bond offerings*

Source: Company data, Bloomberg, Thomson Reuters

Bancassurance profits set to rise

RHB has also entered into a ten-year bancassurance partnership with Tokio Marine Life Insurance. RHB stands to earn a facilitation fee of RM140 mn over the life of the deal. Management expects commission earned over ten years to exceed RM1 bn. As such, management aims to increase bancassurance fee income from RM15-20 mn p.a. to RM100mn p.a. over the next three years.

Plans to raise bancassurance income to RM100 mn p.a. from RM15-20 mn p.a. now

Tie-up with Goldman Sachs to boost asset management fee income

RHB has also entered into an arrangement with Goldman Sachs Asset Management to jointly develop fund management products. RHB's fee income (annualised RM20 mn for 2010) derived from fund management is well behind domestic market leader, Public Bank (RM736 mn fee income in 2010 with RM41 bn of assets under management). RHB currently has over RM12 bn of assets under management comprising equity, fixed income, mixed assets, money market and structured capital guaranteed fund-of-funds.

RHB's fund management fee income is well below market leader

Best play on ETP

We believe that RHB is arguably one of the best plays on the Malaysian government's Economic Transformation Plan (ETP). Our house view is that the market has underestimated the economic impact of the ETP and we are beginning to witness early evidence of government execution. We believe that should the government continue in the same vein to roll out the ETP, there could be positive surprises to economic growth and could spell upside for banking sector earnings.

How is ETP different and why it could work ?

Comprehensive plan with private sector inputs

Key differentiating features of the ETP compared to past government plans are:

ETP is driven by private sector

- **Private sector-led** - Unlike past government plans, the ETP has lots of private sector inputs. PEMANDU (Performance Management and Delivery unit), the government task force in charge of implementation of the ETP, is spearheaded by Idris Jala, who has plenty of private sector experience in turning around financially challenged companies (e.g., Malaysian Airlines). PEMANDU has identified 12 National Key Economic Areas (NKEA) that could be key drivers of the economy, comprising 11 key sectors of the economy and Greater KL region. The 11 sectors are: (1) financial services, (2) palm oil, (3) wholesale and retail, (4) tourism, (5) oil, gas and energy, (6) electricity and electronics, (7) healthcare, (8) education, (9) business services, (10) communications, content and infrastructure and (11) agriculture. Over an eight-week brainstorming session involving 12 private sector-led labs to focus on each of the NKEAs, the team identified a total of 191 projects (131 Entry Point Projects or EPP, 60 business opportunities) worth US$444 bn (RM1.3 tn) to spur private investments and drive the economy. The labs involved top management of 194 MNCs, government-linked corporations and SMEs, As the projects earmarked are identified by the private sector, we believe the projects should be technically and financially feasible; and hence would stand a better chance of being implemented.

- **Approval fast tracked for "ETP"-labeled projects** – PEMANDU has established an ETP unit that works closely with the Economic Planning Unit to expedite the approval process for key projects identified under the ETP. As a result, projects that have been held up for years (e.g., St Regis Hotel in KL Sentral) due to "red tape" within government agencies have been revived and approved for implementation under the ETP.

- **KPIs set for various ministries** – Ministerial KPIs have also been set to ensure that the respective ministers are under pressure to facilitate execution of the ETP.

Regular follow up to monitor progress

- **Regular follow-up to monitor progress** – Weekly Economic Council meetings are conducted to monitor progress of key projects. Weekly problem-solving committees have also been formed to identify bottlenecks in the implementation process.

- **Efforts to engage the public and the investment community** – PEMANDU has held an open day to brief the public on the ETP and also published a detailed handbook with details of its plan. An annual report will also be prepared for the public to track the progress of the ETP. PEMANDU has also conducted briefings for analysts and fund managers to run through the ETP and subsequently provide updates on progress of implementation periodically. PEMANDU officials are also easily accessible by investors to discuss details of the ETP and updates on its progress. By engaging the public as well as the investment community, there is mounting pressure on the government to ensure that the ETP is successfully implemented.

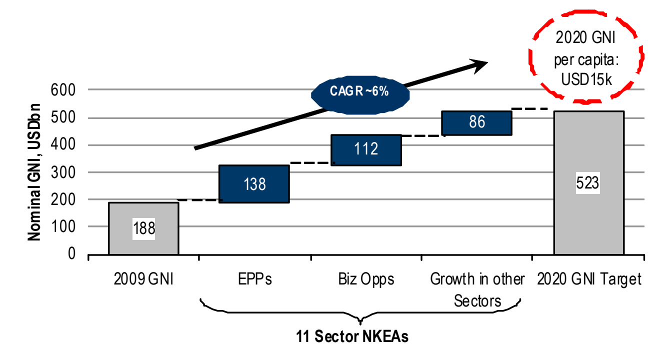
Key targets of the ETP

The key targets of the ETP are as follows :

- **More than double income per capita by 2020** to US$15,000 (from US$6,700 in 2009)
- **Generate RM1.3 tn of private sector investments over 2010-2020, raise private investment as % of GNI to 18% (from 10% now)** and grow private investments by 12.8% p.a. over 2011-2015 (versus 2% growth p.a. over 2006-2010)
- **Create 3.3 mn jobs over the next ten years,** with 64% in the medium to high income categories (>RM2,000 per month)

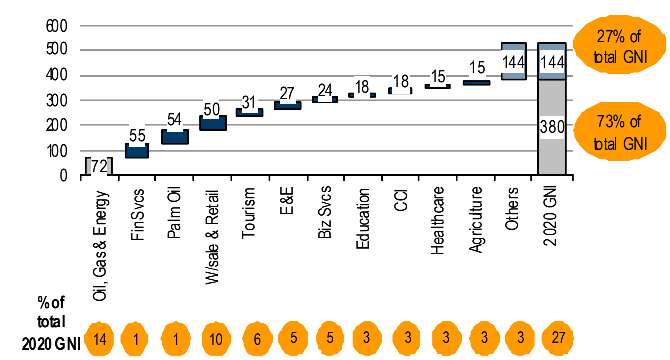
Double income per capita, raise private investments to 18% of GNI and create 3.3 mn new jobs

Figure 24: **Plan to double income per capita by 2020**



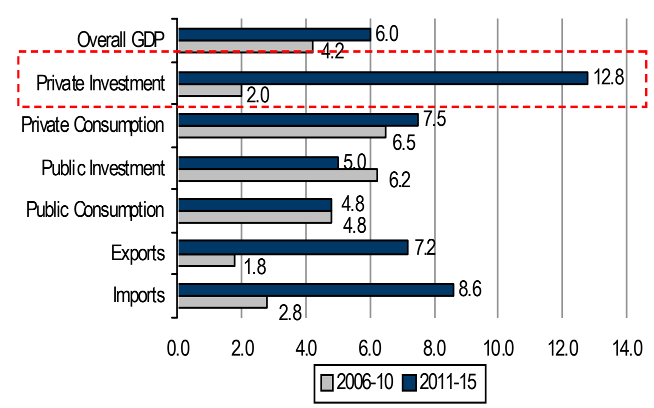
Source: Economic Transformation Programme

Figure 25: **Contribution to GNI increase from various NKEAs**



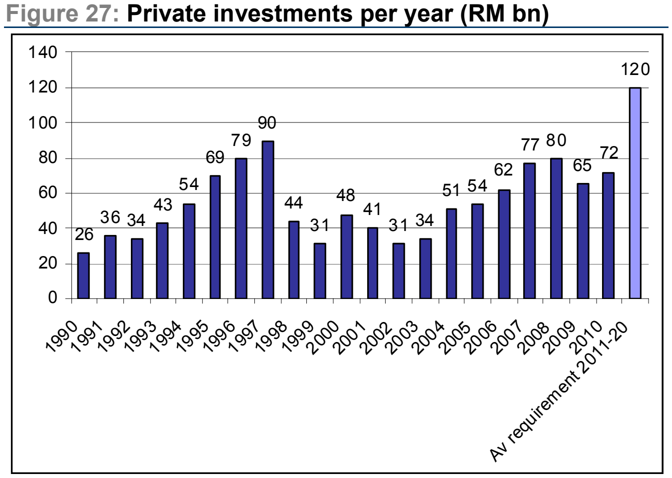
Source: Economic Transformation Programme

Figure 26: **Target higher private investment growth**



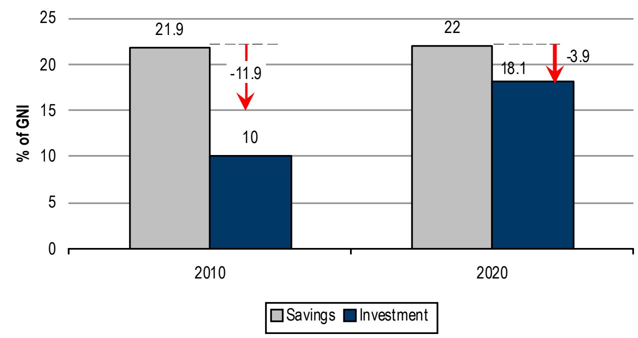
Source: Economic Transformation Programme

Figure 27: **Private investments per year (RM bn)**



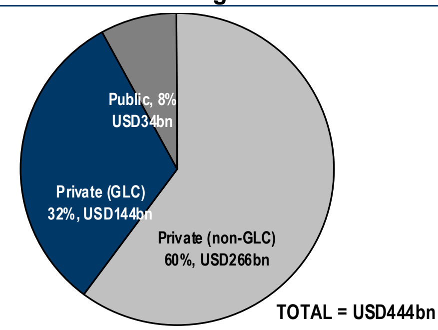
Source: Economic Transformation Programme

Figure 28: **Private investments as % of GNI**



Source: Economic Transformation Programme

Figure 29: **Breakdown of ETP target investments**



Source: Economic Transformation Programme

Politically crucial for government to deliver

We believe that PM Najib Razak is serious about transforming the economy and is supportive of the ETP initiatives. With a general election to contest and a credible opposition party, we believe Najib fully appreciates the importance of timely execution of the ETP such that the economic benefits are visible to the voting public.

Early signs of better execution

Major projects such as MRT progressing according to plan

So far we have been pleasantly surprised by the progress and pace of execution of the ETP. Since unveiling the ETP in September 2010, the list of EPP that have progressed to an advanced stage of implementation has been steadily rising. A series of oil and gas projects have been announced year-to-date, and the RM50 bn KL MRT project (arguably the most high profile ETP project with the greatest economic and political impact) is on track for the scheduled commencement of works by July 2011. We believe that the market remains skeptical that works on the KL MRT will kick off by July 2011, so any evidence to suggest that works could commence on schedule would provide a major boost to investors' confidence in the ETP.

How will RHB benefit ?

Loan growth could surprise on the upside if private investments pick up sharply

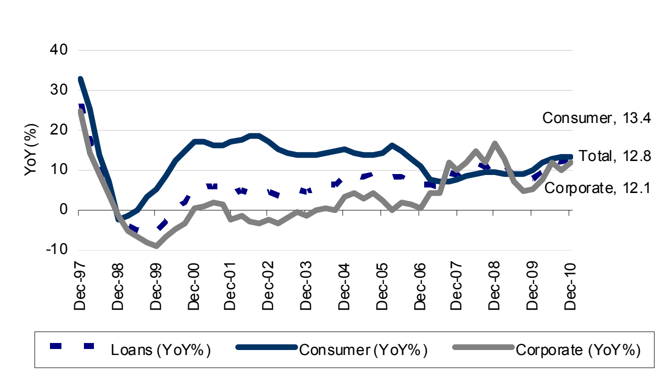
Loan growth has so far exceeded expectations

If successfully implemented, the ETP would be a massive boost to loan growth prospects. Already loan growth has surpassed consensus expectations, having remained above 10% thus far, while most analysts and corporates throughout most of last year were expecting system loan growth to hover around 7-8% by end-2010. Loan growth has been surprisingly firm at 12.8% as at Dec-2010, driven by a pick-up in corporate loan growth to above 10% since May 2010 (10-12.4% YoY growth during May-Dec 2010 period) and robust consumer loan growth (accelerated from 10% in early 2010 to 13-14% growth in 2H10).

Pick up in private investments could be a big boost to loan growth

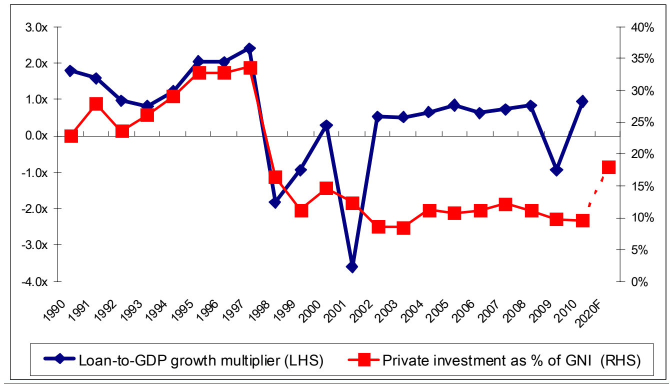
We believe the loan-to-GDP growth multiplier could likely return to >1x should the ETP successfully stimulate private investments. Since private investments as a percentage of GNI declined to 10% of GNI (gross national income) in the post Asian financial crisis period (i.e., 1998 onwards), we noticed that the loan-to-GDP growth multiplier has contracted to 0.3-0.8x. During the pre-Asian crisis period from 1990-1997 when private investments accounted for between 22-32% of GNI, the loan-to-GDP growth multiplier averaged 1.6x. Therefore, should the ETP achieve its target of lifting private investments to an average of RM120 bn p.a. (127% above the post-Asian crisis average and 67% above 2010 level) and to 18% of GNI, we believe the loan-to-GDP growth multiplier could expand to well above 1x. Combined with a target real GDP growth of 6-6.5% p.a. (i.e. nominal GDP of 9-10%), system loan growth could accelerate to 15-16% p.a. Should RHB succeed in gaining loan market share with its strong corporate relationships and EASY strategy, it is not inconceivable for the group's loan growth to well surpass 20% p.a. for an extended period of time.

Figure 30: System loan growth has surpassed expectations



Source: Bank Negara

Figure 31: Private investment (% GNI) versus loan-to-GDP growth multiplier



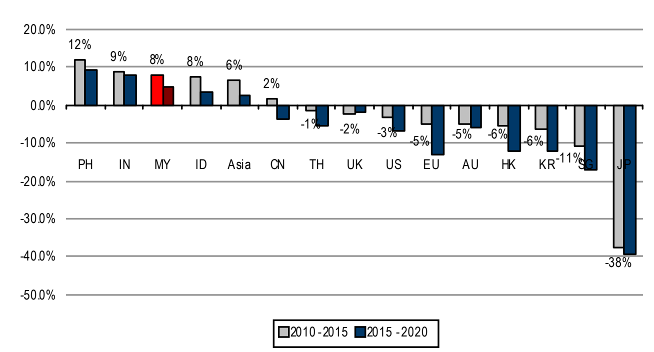
Source: Bank Negara , MOF, Credit Suisse estimates

EASY capitalises on Malaysia's favourable demographic structure

According to United Nation's projections, Malaysia's population in the working age group is projected to grow by 8% over the next five years, the third-highest growth in the world. The ETP's plans to create 3.3 mn new jobs over 2010-2020 could further accelerate the growth in working population. Out of the 3.3 mn new jobs to be created, 64% is expected to be in the mass market bracket, which RHB is targeting through its EASY strategy. Therefore, not only is EASY's target mass market customer segment underserved, it is also expected to grow rapidly with the ETP roll-out.

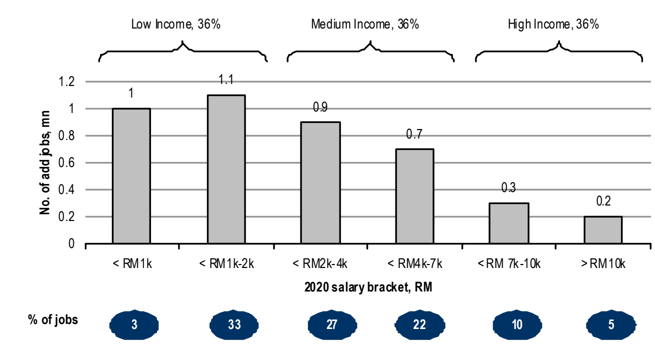
Malaysia has the 3rd highest growth in working population in the world

Figure 32: Growth in working population



Source: United Nations

Figure 33: ETP to create 3.3 mn jobs



Source: Economic Transformation Programme

Well positioned to tap upside to capital market given its EPF link

We believe that a substantial portion of the Entry Point Projects, particularly infrastructure projects, will be financed directly using debt capital market proceeds. As a start, the government has already identified public-private partnerships (PPP) infrastructure projects to be implemented in 2011 that would involve RM12.5 bn of private investments and has set aside RM1 bn of public sector funds to facilitate the execution of these projects. If we assume a typical debt-to-equity mix of 90:10 for PPP projects, the earmarked projects could generate debt capital market issuance of up to RM125 bn (well above gross issues of RM52 bn in 2010). We believe that EPF will likely be a key financier of a substantial portion of the ETP's entry point projects. With the benefit of a close working relationship with EPF, RHB is well positioned to clinch a sizeable share of the capital market mandates generated by the ETP. Given that public sector funding for ETP is expected to amount to US$34 bn (RM103 bn) over 2011-2020, we would also expect the government to tap the debt capital market for funding as well.

EPF expected to be an active participant in ETP and likely to engage RHB

Earnings upside from fixing operational flaws

Positive results so far but . . .

Management has successfully revived profitability, competitiveness and, more importantly, credibility with the investment community. We outline below some of the key achievements of RHB's management team so far, but we believe that there is still plenty of room for improvement and positive surprises to street's expectations.

Management has achieved profit targets and guidance to investors

Doubled profits since 2007

Over the past eight quarters (since early 2009), the group has consistently met or exceeded street's estimates. Having registered RM1.42 bn net profit, management has also achieved its target set in 2007 of doubling profitability (RM0.7 bn net profit in 2007).

In 2010, management has also achieved all its financial and operational targets with the exception of the percentage of international contribution (please refer to table below). The group achieved ROE of 15.2% (versus 14.5-15% target), ROA of 1.2% (versus 1.0-1.1% target), loan growth of 20% (versus 15% target) and cost-to-income ratio of 40% (better than 45% target).

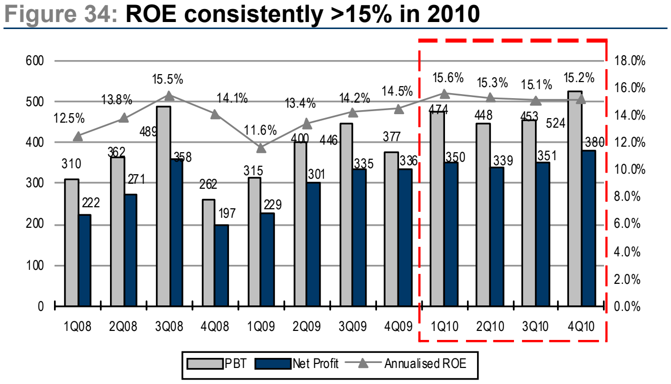
For 2011, management has set the following targets:

Set ROE target of >15.8% for 2011

- ROE target of 15.8%, which translates to 15.2% after the impending rights issue.
- ROA of >1.2%
- Loan growth of >15%
- Deposit growth of >15%
- Cost-to-income ratio of <43%
- Reduce gross impaired loan ratio to 4% (from 4.4% at end-2010)
- Raise international contribution to >10% of profitability (from 5% in 2010)

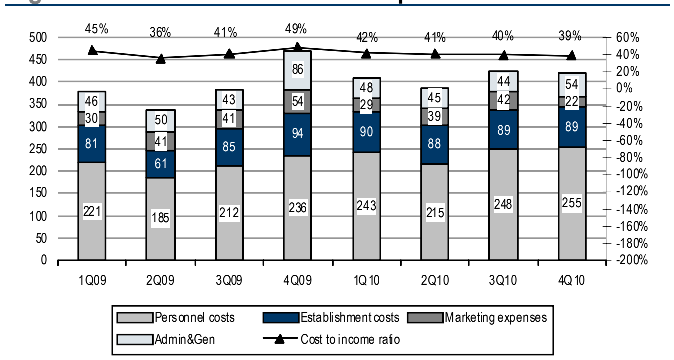
Given that management has so far delivered, we believe investors would be more optimistic that the group can achieve the targets set above.

Figure 34: ROE consistently >15% in 2010



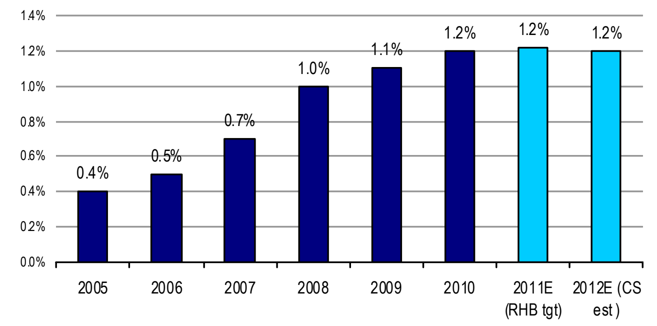
Source: Company data, Credit Suisse estimates

Figure 35: Cost-to-income ratio improved



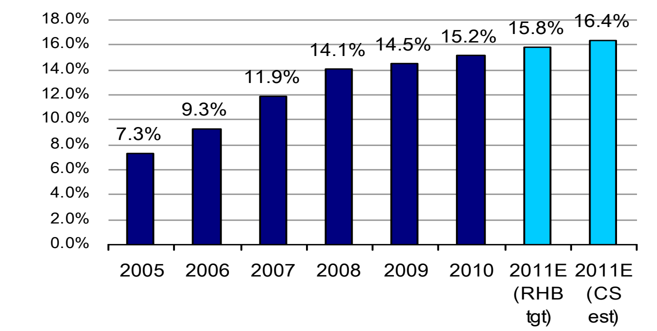
Source: Company data, Credit Suisse estimates

Figure 36: ROA long-term trend



Source: Company data, Credit Suisse estimates

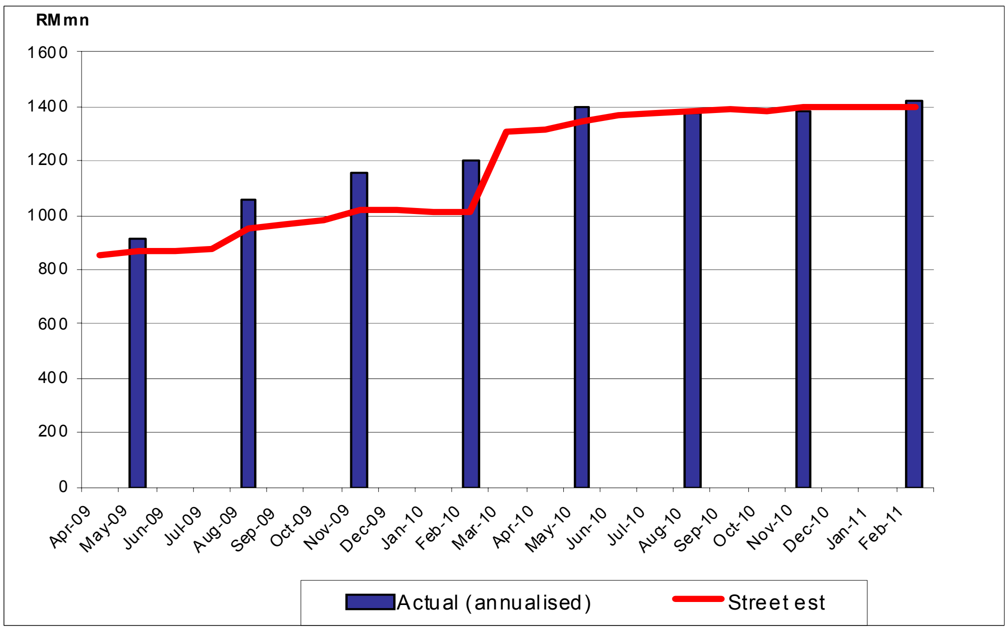
Figure 37: ROE long-term trend



Source: Company data, Credit Suisse estimates

Figure 38: Results versus street net profit estimates

Results consistently in line-to-above street's estimates



Source: Company data, Thomson Analytics

Figure 39: Key targets and scorecard

Top level indicators	FY07	FY08	FY09	FY10	Target 2010	2010 actual vs Target	2011 Target
Net profit (bn)	0.713	1.049	1.201	1.420	>1.4	+0.02	n.a.
ROE (%)	11.9	14.1	14.5	15.2	14.5 - 15.0	+0.2	>15.2 * (15.8 pre-rights issue)
ROA (%)	0.7	1.0	1.1	1.2	1.0-1.1	+0.1	1.2
Gross Impaired Loans Ratio (%)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	4.0
Loan Growth (%)	1.2	11.2	10.2	20.2	>15	5.2	>15
Deposit Growth (%)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	>15
Cost-to-income Ratio (%)	44	44	43	40	45	5	<43
International Contribution (%)	4	4	6	5	>10	5	5 - >10

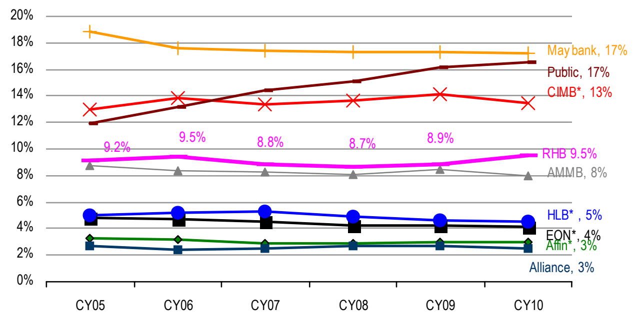
** post-rights issue target; Source: Company data*

Positive market share momentum

Market share of loans and deposit rose over past 2 years

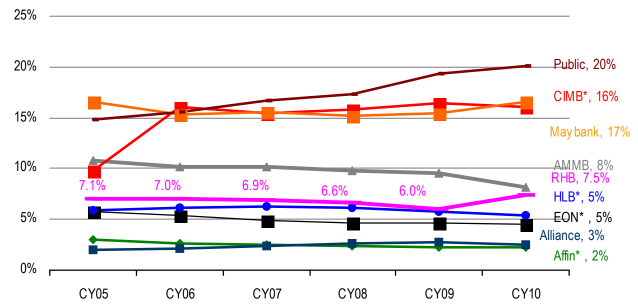
RHB has also been gaining market share of loans and deposits over the past two years. Overall market share of loans has grown to 9.5% from 8.7% two years ago, having grown at an average rate of 15% p.a. compared to system loan growth of 10% p.a. Deposit market share grew over the past two years to 8.8% from 7.6% two years ago, having grown at an average of 13% p.a. compared to system deposit growth of 8% p.a. CASA market share rebounded over the past year to 6.8% from 6.5% but is still lagging behind its total deposit share.

Figure 40: Loan market share trend



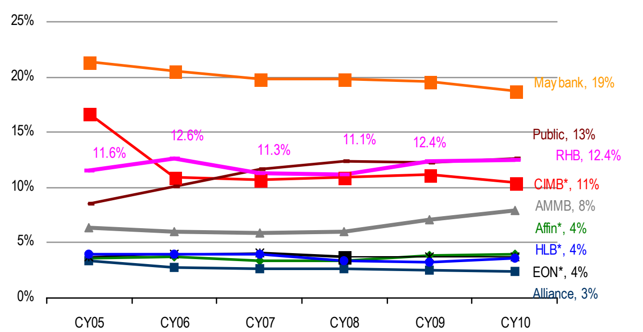
Source: Company data, Credit Suisse estimates

Figure 41: Consumer loan market share



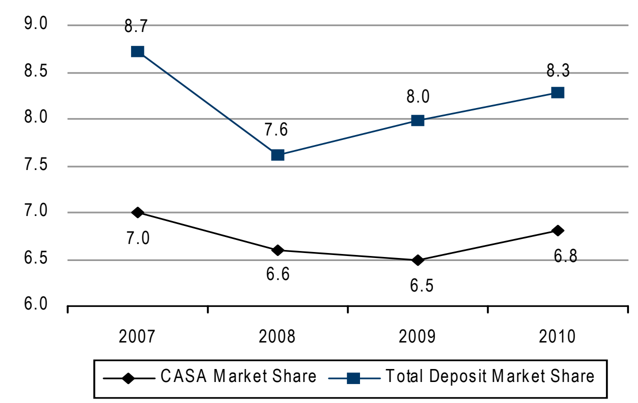
Source: Company data, Credit Suisse estimates

Figure 42: Corporate loan market share trend



Source: Company data, Credit Suisse estimates

Figure 43: Deposit market share trend



Source: Company data, Credit Suisse estimates

Still room for operational improvement

Despite RHB's sharp ROA improvement over the past five years, the group's ROA is still below other leading Malaysian banks such as CIMB, Maybank and Public. We compare below the ROA breakdown of RHB with Malaysia's leading local large cap banks.

Figure 44: Comparison of ROA and ROE of RHB with other local peers

	RHB Capital			CIMB			Public			Maybank		
Year-end Dec 31 (RM mn)	**2008**	**2009**	**2010**	**2008**	**2009**	**9m2010**	**2008**	**2009**	**2010**	**2009**	**2010**	**1H2011**
As % of average assets												
Net interest income	2.38	2.50	2.46	2.62	3.07	3.06	2.31	2.29	2.43	2.46	2.53	2.49
Non-interest income	0.90	0.84	0.85	1.36	1.70	1.61	0.79	0.60	0.66	1.16	1.44	1.25
Net banking income	3.29	3.34	3.32	3.97	4.77	4.67	3.10	2.88	3.08	3.63	3.98	3.74
Total operating expenses	-1.44	-1.43	-1.34	-2.12	-2.56	-2.56	-0.97	-0.94	-0.95	-1.92	-1.98	-1.84
Operating profit	1.84	1.91	1.97	1.86	2.21	2.11	2.13	1.94	2.14	1.71	2.00	1.90
Loan-loss provisions	-0.49	-0.51	-0.42	-0.44	-0.52	-0.27	-0.31	-0.34	-0.30	-0.65	-0.37	-0.23
Income before tax	1.36	1.40	1.56	1.39	1.70	1.86	1.83	1.61	1.84	1.09	1.66	1.71
Net income (ROAA)	**1.00**	**1.09**	**1.16**	**1.00**	**1.25**	**1.41**	**1.39**	**1.22**	**1.37**	**0.75**	**1.18**	**1.24**
Leverage (x)	13.4	13.2	13.0	12.0	11.7	11.3	20.6	19.7	17.4	12.5	12.1	12.4
Net income (ROAE)	**14.1**	**16.2**	**15.2**	**11.8**	**14.8**	**16.1**	**27.3**	**24.5**	**25.3**	**9.9**	**14.5**	**15.1**

Source: Company data, Credit Suisse estimates

We outline some areas of operational deficiency and unproven areas which can present further upside to earnings/ROA as well as improve investability of the stock (offer comfort to investors).

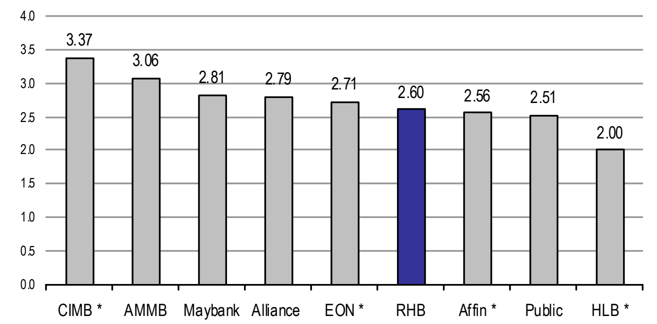
Key areas of weakness compared to its peers are :

NIM

Use EASY to boost deposits

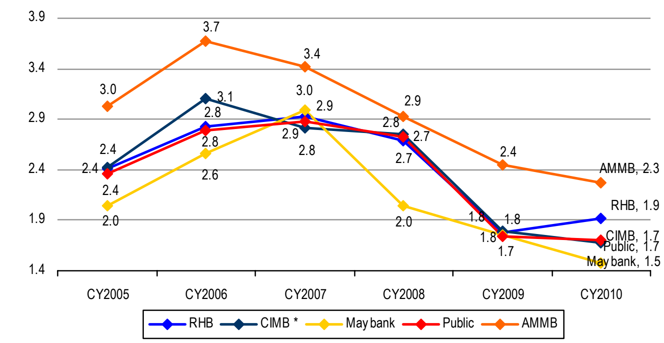
RHB's NIM is low in comparison to other GLC banks such as CIMB and Maybank. We would attribute this to the: (1) lack of exposure to foreign markets such as Indonesia, (2) comparatively higher funding cost given its lower CASA base, (3) aggressive expansion in public sector lending, which have low yields (but do not require capital charge), (4) management's efforts to lengthen tenure of deposit base resulting in higher cost of funds. We believe management's strategy to enhance its deposit franchise through improving convenience for customers (e.g., expand footprint with EASY, improved internet banking platform, etc) should help boost its low-cost deposit base and lower funding cost.

Figure 45: **NIM comparison**



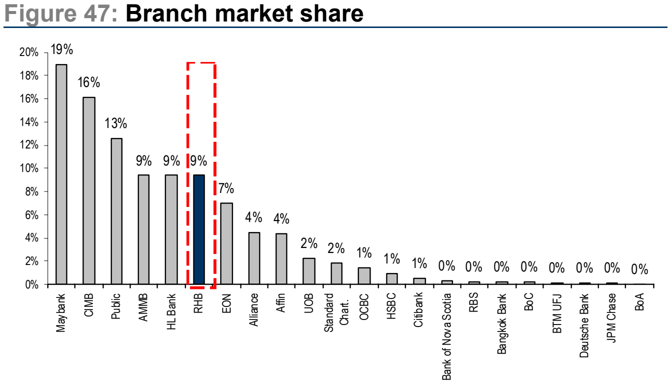
** only reported up to Sep 2010; source: Company data, Credit Suisse estimates*

Figure 46: **Funding cost trend**



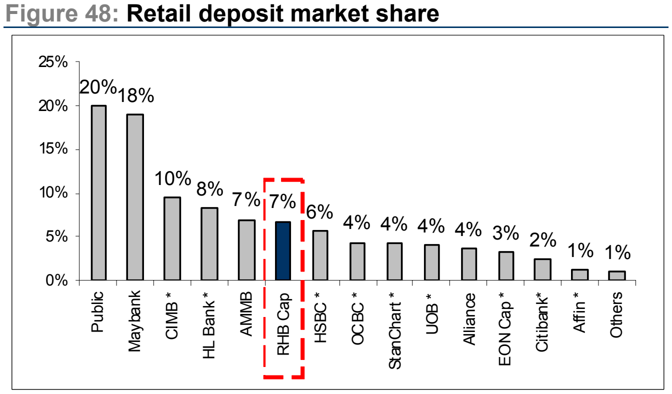
Source: Company data, Credit Suisse estimates

Figure 47: **Branch market share**



Source: Company data, Credit Suisse estimates

Figure 48: **Retail deposit market share**



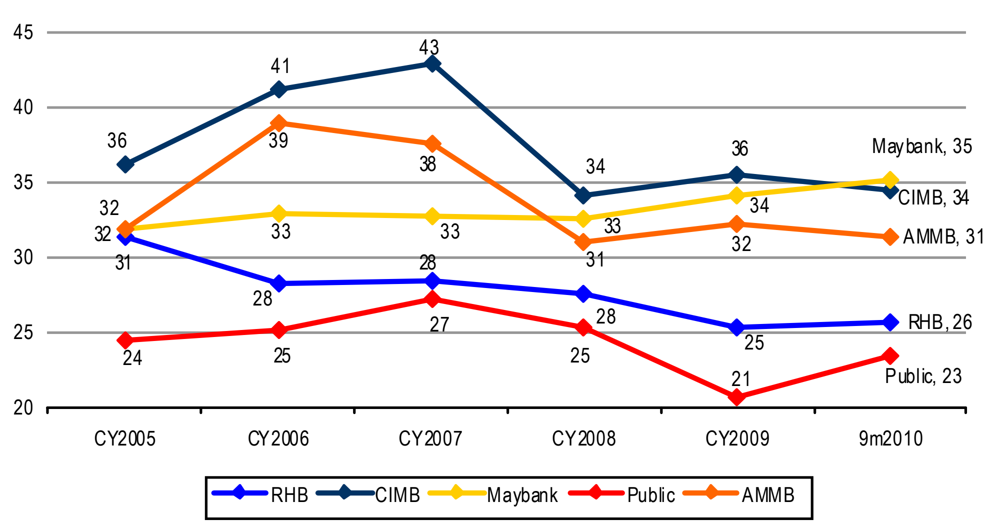
Source: Company data, Credit Suisse estimates

Non-interest income

Focus on IB and bancassurance to boost non-interest income

RHB's non-interest income is also relatively weak in comparison to other GLC banks such as CIMB and Maybank. RHB's non-interest income ratio of 26% is well below CIMB's 34% and Maybank's 35%. With efforts to boost its investment banking business through a closer working relationship with EPF and tie-ups with strategic partners in bancassurance as well as asset management, we believe there is upside potential to non-interest income. The potential uplift to the IB business could be accelerated if the ETP is successfully executed.

Figure 49: **Non-interest income ratio trend over past five years**



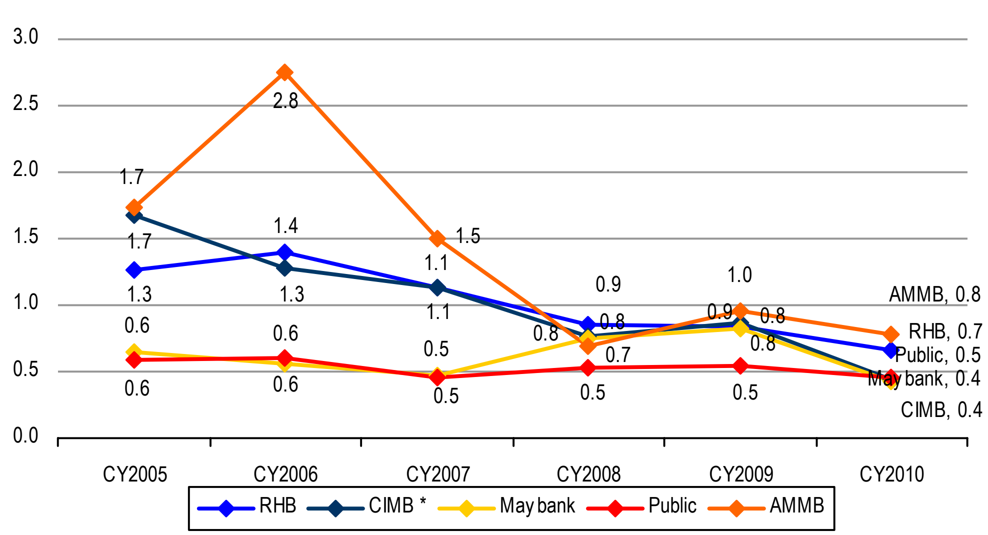
Source: Company data, Credit Suisse estimates

Asset quality

Another area of weakness compared to peers is the group's asset quality and credit cost. While RHB's credit costs has halved over the past five years to 0.7% in 2010, it is still higher than the likes of CIMB, Maybank and Public (0.4-0.5% range). RHB's gross impaired loan ratio of 4.4% is above industry average of 3% and provision coverage of 68% is also among the lowest in the industry (system average of 98%). However, it is worth noting that the group's gross impaired loan ratio is improving rapidly (dropped 2.3 p.p. over the past four quarters from 6.7% to 4.4%) and new impaired loan formation has improved to 1.3% from 2% a year ago. By tightening up on credit controls and increasing exposure to the consumer loan segment, we expect RHB's credit costs to improve in the future. However, we still expect its credit costs to hover around 59-61 bp in the coming years compared to our projections of <50 bp for Maybank, Public and CIMB.

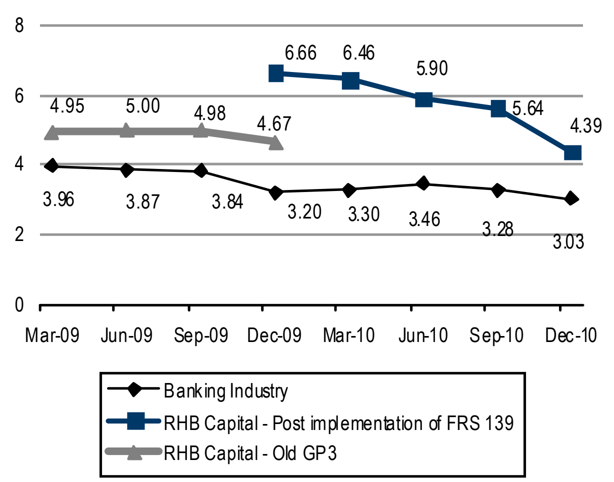
Credit cost has improved but still above other major local banks

Figure 50: **Credit cost trend over the past five years**



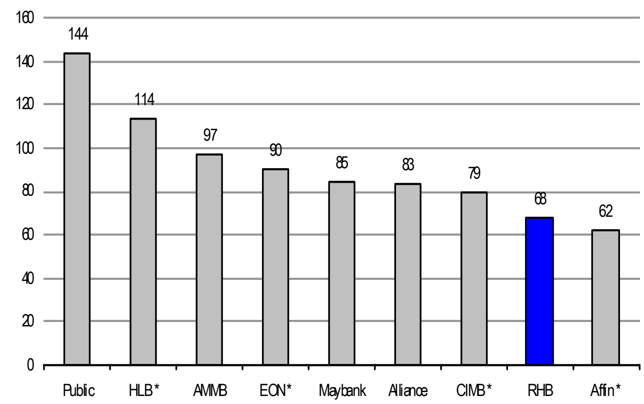
Source: Company data, Credit Suisse estimates

Figure 51: **RHB's gross impaired loan ratio versus industry**



Source: Company data, Credit Suisse estimates

Figure 52: **Provision coverage for impaired loans**



Source: Company data, Credit Suisse estimates

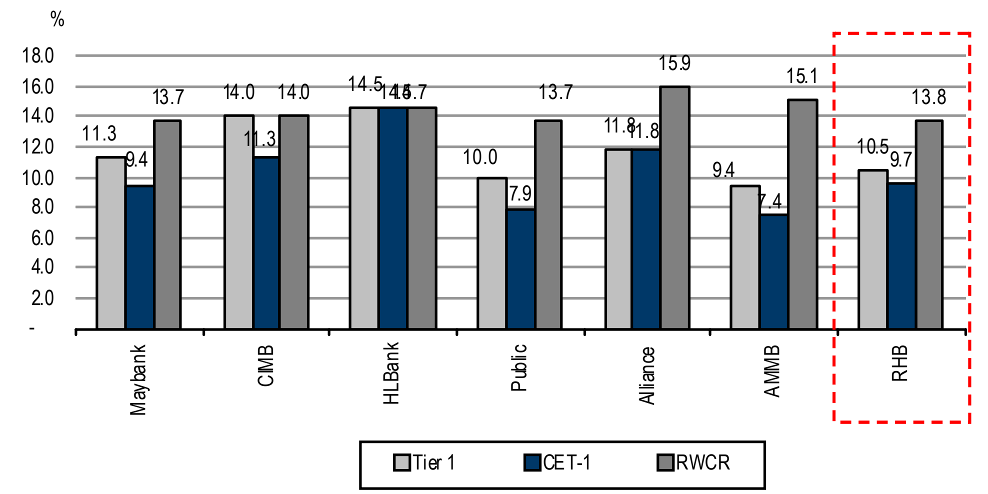
Key challenges ahead

Lean capital position

Capital healthy at bank level but gearing seems high at holding company

RHB's management has been conservative on dividend guidance. We believe RHB does not have a sufficiently strong capital position that can support a generous dividend policy at this point, particularly given that its loan base is expected to rapidly expand. At the bank level, the group has a core equity Tier 1 (CET 1) ratio of 9.7%. Following an impending rights issue to fund the group's proposed acquisition of PT Bank Mestika, we estimate that CET 1 could inch up to 10.1%. Management indicated that their internal computations suggest that BASEL 3 adjustments would not have a major dilutive impact on its CET 1, which will still remain above 9.5%. At the bank level, capital ratios appear healthy and sufficient to comply with any potential step-up in capital requirements arising from BASEL 3. However, gearing of the group at 0.56x and double leverage of 152% seems high. RHB only discloses the bank capital ratios and does not disclose the group ratios. While regulators only monitor the bank's capital ratios, investors are increasingly focusing on group capital adequacy. Our computations suggest that group CET 1 ratio could be closer to 7.5%, 2.2% below bank level due largely to the larger goodwill at the group level. However, one major caveat is that we do not have the full details required to accurately determine the group capital ratio. We believe that management is exploring options such as a dividend reinvestment plan to optimise yield to institutional shareholders and at the same time does not lead to much erosion of capital.

Figure 53: **Comparison of capital ratios**



Source: Company data, Credit Suisse estimates

Indonesian acquisition still unproven

RHB is finalising its acquisition of an 80% stake in PT Bank Mestika for RM1.16 bn. The transaction price translates to a P/B of 3x and 21x annualised 2010 net profit. Key facts about Mestika as follows:

- Mestika has 56 branches in Northern Sumatra and 4% share of loans in Sumatra. However, its loan size is only <0.3% of the banking system.
- Loan book only comprises four segments, i.e., trade finance (30% of loans), SME (58%), vehicle financing (5%) and mortgage (7%). Almost all its loans are secured.
- Mestika's loan-to-deposit ratio is currently 95%, while CASA ratio is 73%
- Historical NIM at 7.8% in 1H10
- Mestika generated an ROE of 14% in 1H10 and net profit equivalent to RM35 mn.
- Capital adequacy ratio of 29%, which is all equity funded.

Aim to complete acquisition of Mestika and rights issue by April 2011

RHB's management plans to raise RM1.3 bn from a rights issue to fund the acquisition and aims to complete the entire exercise by April 2011. Management is also planning a listing exercise for Mestika, which could take place by mid-2011. While we have no doubt that RHB's vast experience should enable it to add significant value to the operations of Mestika, we are still cautious on our assumptions for the Indonesian operations. While management has set an aggressive target of raising Indonesian contributions to 20% of RHB's net profit by 2013, we have been more conservative on our forecasts given the challenging operating environment in Indonesia and management's unproven track record on acquisitions.

Figure 54: Impact of rights issue and acquisition of PT Bank Mestika

	2011E	2012E	2013E
Current net profit	1,732.2	2,101.7	2,478.6
Add : Mestika	81.4	122.5	187.3
Add : net interest on excess cash	2.9	2.9	2.9
Post-acquisition net profit	1,816.4	2,227.1	2,668.7
Indonesia as % of total	4%	6%	7%
EPS			
- Current	0.80	0.98	1.15
- Post-rights	0.78	0.96	1.14
Dilution	-3%	-2%	-1%
ROE (%)			
- Current	16.4%	17.6%	18.3%
- Post-rights	16.1%	16.7%	17.8%
Dilution	-0.2%	-0.9%	-0.6%
BV/sh			
- Current	5.19	5.87	6.68
- Post-rights	5.38	6.04	6.84
Core equity tier 1 ratio (%)	9.7%		
Post-acquisition core equity tier 1 ratio (%)	10.1%		

Source: Company data, Credit Suisse estimates

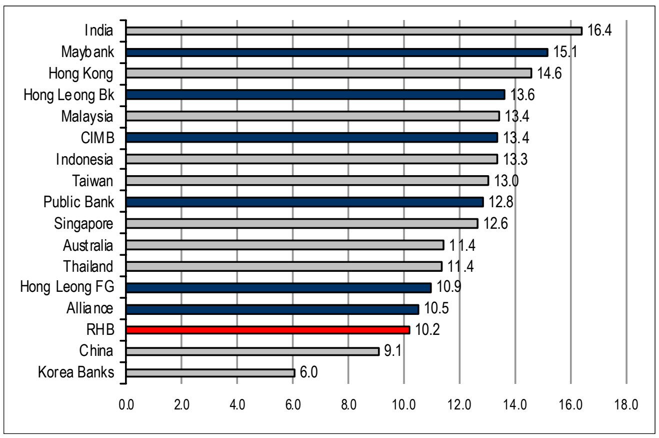
Trades at 30% discount to local peers

P/E comparison

RHB trades at 10x 2011E P/E versus Malaysian banking peer average of 14x and regional peer average of 11x. Comparing the 2011E P/E of banks across the region, RHB is cheaper than banks in most countries, with the exception of China and Korea. Relative to the market P/E of 15x for 2011, RHB trades at a discount of 35%. We are projecting a two-year net profit growth over 2010-2012 of 22% p.a. for RHB versus market's projected growth of 16% p.a. RHB also currently trades well below its historical P/E average of 14x.

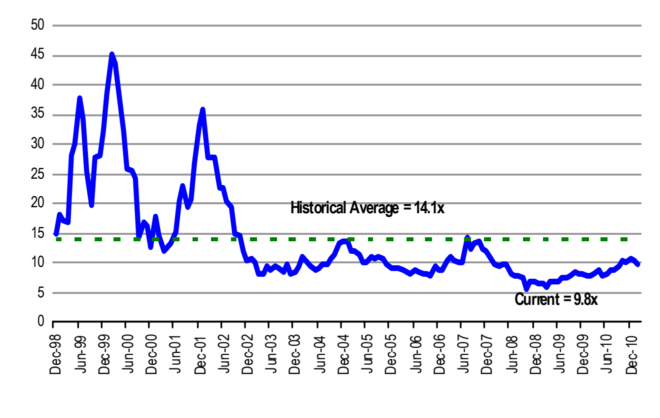
Trades at 10x P/E vs local peer average of 14x

Figure 55: Regional P/E comparison



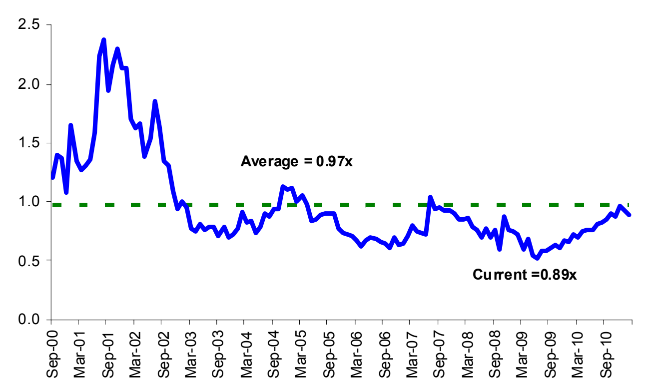
Source: Company data, Credit Suisse estimates

Figure 56: P/E trend



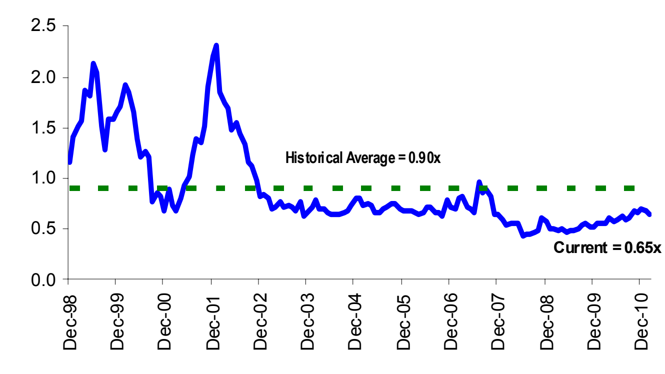
Source: Company data, Credit Suisse estimates

Figure 57: P/E relative to regional peers



Source: Company data, Credit Suisse estimates

Figure 58: P/E relative to market



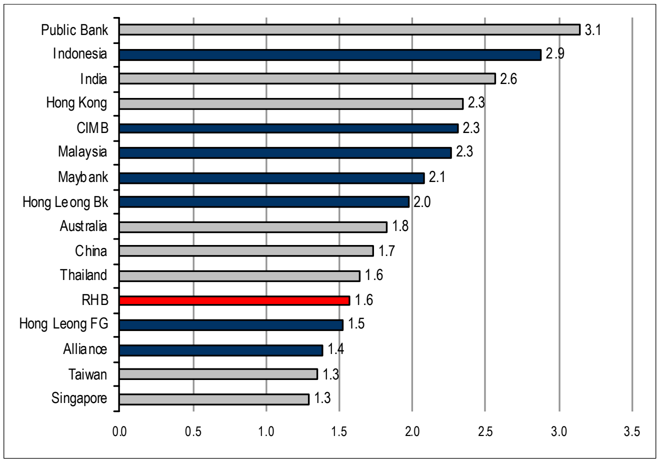
Source: Company data, Credit Suisse estimates

P/B comparison

RHB trades at a P/B of 1.8x with projected 2011E ROE of 16.4%. This compares with the Malaysian peer average of 2.5x with projected 2011E ROE of 17.8%. Regional peers trade at an average of 1.9x with projected 2011E ROE of 15.7%. Our calculations suggest that the current P/B valuation of RHB implies an ROE of 14% (compared to CS's estimate of 16.4% in 2011), which we believe understates the earnings potential of the group.

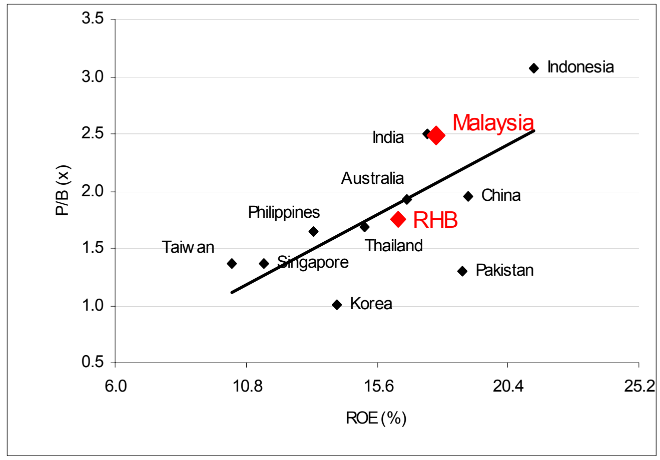
Trades at market implied ROE of 14%, which grossly understates its earnings potential

Figure 59: Regional P/B comparison



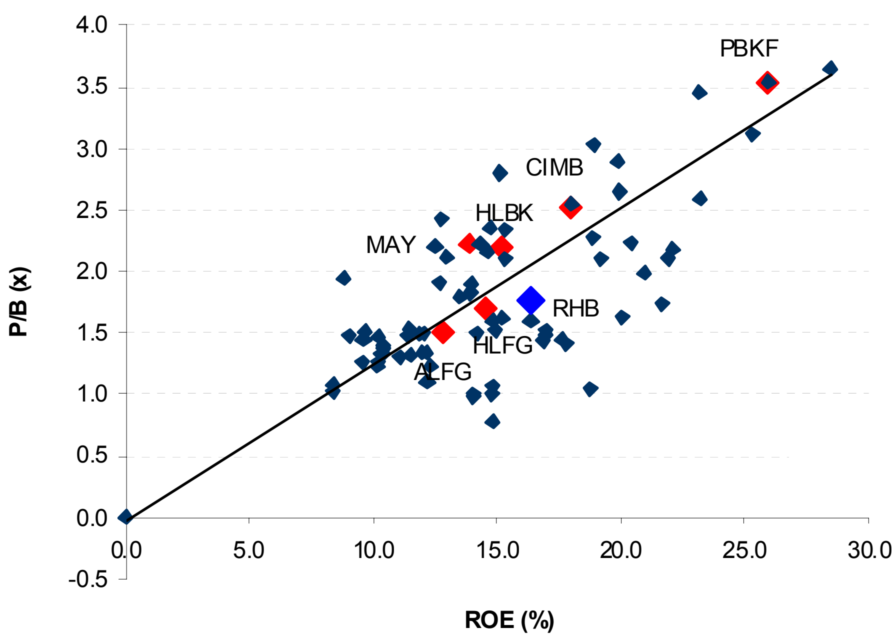
Source: Company data, Credit Suisse estimates

Figure 60: P/B vs ROE (country)



Source: Company data, Credit Suisse estimates

Figure 61: P/B vs ROE—Malaysian banks



Source: Company data, Credit Suisse estimates

Figure 62: **Valuation summary**

Bank	AMMBH*	HL Bank	HLFG	Maybank	CIMB	PBKF	Alliance	RHB Cap	EON Cap*	Affin*
Year ending	31-Mar	30-Jun	30-Jun	30-Jun	31-Dec	31-Dec	31-Mar	31-Dec	31-Dec	31-Dec
Bloomberg	AMM MK	HLBK MK	HLFG MK	MAY MK	CIMB MK	PBKF MK	AFG MK	RHBC MK	EON MK	AHB MK
Mkt cap (US$ mn)	18,989	14,679	9,264	63,850	60,874	46,198	4,660	17,443	4,866	5,037
Out. shares (mn)	3,014	1,580	1,053	7,322	7,433	3,532	1,548	2,153	693	1,495
Rating	NR	N	O	U	O	O	O	O	NR	NR
Price (RM)	6.30	9.29	8.80	8.72	8.19	13.08	3.01	8.10	7.02	3.37
Target (RM)	NA	9.30	10.00	7.60	10.80	17.30	3.70	11.80	NA	NA
Upside (%)	NA	0.1	13.6	-12.8	31.9	32.3	22.9	45.7	NA	NA
ROE (%)										
2012E	13.8	15.3	14.8	14.6	18.7	27.3	14.2	17.6	11.6	10.2
2011E	13.0	15.2	14.5	13.9	18.0	25.9	12.8	16.4	11.9	9.8
2010E	11.4	16.4	17.5	14.5	16.9	25.3	10.6	15.2	11.7	9.5
2009A	11.4	16.8	14.7	3.1	14.8	24.5	8.6	14.5	10.1	8.1
ROAA (%)										
2012E	1.4	1.2	0.9	1.2	1.6	1.5	1.2	1.3	0.9	1.1
2011E	1.3	1.2	0.8	1.1	1.6	1.5	1.2	1.2	0.9	1.1
2010E	1.1	1.2	0.9	1.2	1.5	1.4	0.5	1.2	0.9	1.1
2009A	2.7	1.2	0.7	0.8	1.3	1.2	0.5	1.1	0.8	1.0
Calendar P/E (x)										
2011E	12.8	13.5	11.0	15.1	13.4	12.9	10.3	10.1	9.9	9.6
2010E	15.2	14.5	11.3	16.4	16.2	15.2	12.7	12.3	11.1	10.9
2009A	18.4	15.5	12.8	23.0	20.6	18.4	16.7	14.5	14.3	13.5
2008A	20.0	18.0	15.8	25.5	30.0	17.9	17.7	16.6	36.9	16.9
Calendar P/B (x)										
2011E	1.7	1.9	1.5	2.1	2.3	3.2	1.4	1.6	1.2	0.9
2010E	1.8	2.2	1.7	2.2	2.5	3.5	1.5	1.8	1.3	1.0
2009A	2.0	2.4	1.9	2.4	2.8	4.2	1.6	2.0	1.4	1.1

Source: Company data, Credit Suisse estimates

Reasons for the valuation discount to local peers

We attribute the valuation discount to the following factors and believe that RHB could rerate upwards to narrow the valuation gap if these were addressed:

- **Free float and liquidity** – As EPF (48%) and Abu Dhabi Commercial Bank (25%) control a combined 73% of RHB, its free float remains very tight. This has contributed to the lower liquidity of the stock compared to its other banking peers. EPF has announced intentions to trim its stake to 40% (from 48% now) as part of the government's initiatives to enhance capital market activity and broaden list of investable listed companies. In our view, the impending sell-down by EPF would boost the stock's trading liquidity and could be a rerating catalyst.

Free float of 27% now could expand when EPF completes its divestment

- **Coverage by brokers** – Currently RHB is covered by 19 brokers compared to 23-25 for other well-followed local peers such as CIMB, Maybank and AMMB. We expect broker coverage on RHB to increase should management maintain its investor relations initiatives, continue to deliver strong consensus-beating earnings performances and improve trading liquidity.

Under-researched stock, with 19 brokers covering it compared to 23-25 for other local peers

- **Underowned by foreigners** – The stock is under-owned by foreign investors, largely due to the poor liquidity (linked to tight free float), lack of broker coverage and legacy problems. Currently, foreign institutional investors own 12% of RHB, well below the average foreign ownership of 22% in the Malaysian market and 23% in the banking sector. With plans to increase free float to stimulate trading liquidity, expanding broker coverage and expectations of positive street earnings momentum, we expect foreign investor interest to pick up.

Foreign ownership of 12% is low compared to industry average of 23%

- **Dividend yield** – Management of RHB does not offer much promise of generous dividend yield in the near-to-medium term unlike the likes of Maybank, CIMB and Public Bank. This is largely because management envisages an aggressive asset expansion path for the group and capital position remains lean. As such, we expect RHB's net dividend yield to hover at around 3% (based on 30% payout ratio, consistent with historical payout) over the next two years, in line with market average but below the banking peer average of 4%. However, we believe that RHB might potentially explore other options such as dividend reinvestment plan to optimise yield to institutional shareholders.

Management does not promise much yield but possible implementation of dividend reinvestment plan could spell upside for dividend yields

- **Impending rights issue** – Another reason for the valuation discount could be the impending rights issue to fund RHB's acquisition of Mestika. The group expects to complete a RM1.3 bn rights issue and acquisition of Mestika by April 2011. We estimate that the rights issue and acquisition could dilute RHB's EPS by 3% in 2011, but would be EPS neutral by 2013. Even after factoring in effects of the dilution, RHB still trades on an attractive 2011E P/E of 10.6x, a huge discount to the local peer average of 13x.

Complete rights issue by April 2011

RM11.80 target price, implies 46% potential upside

Using the Gordon Growth model, we have set out 12-month price target at RM11.80. Key drivers of our price target are :

Price target based on 17.6% ROE

- Sustainable ROE of 17.6%, which is based on an explicit forecast for 2012
- Cost of equity of 11.4%, a premium to rates used for other large cap peers (i.e., Maybank, CIMB, Public) of 10.7-10.9% due to lower trading liquidity
- Terminal growth of 6.5% p.a. (in line with expected long-term GDP growth rate)

After factoring in the effects of the rights issue and acquisition of Mestika, we arrive at a proforma target price of RM11.20.

Figure 63: **Target price summary**

Banks	Current	Post-rights issue
Risk free rate	4.1%	4.1%
Market risk premium	7.3%	7.3%
Cost of equity	11.4%	11.4%
Growth (terminal)	6.5%	6.5%
Sustainable ROE assumed (%)	17.6%	16.7%
Theoretical P/BV	2.3	2.1
BV/share (end of current FY)	5.19	5.35
Price target (RM) -- Based on Gordon	**11.80**	**11.17**
Implied 2012 P/E	12.6	12.1

Source: Company data, Credit Suisse estimates

Key risks

In our view, the key risks for RHB that could derail our investment case are as follows:

- **Management changes** - One of the main risks for RHB is potential changes in management team. Given that the top management is responsible for the successful turnaround of RHB's operations and profitability, any loss of key personnel could be a setback for the group. We would like to see the group put in place a share option scheme aimed at retaining its key personnel.
- **Shareholding changes** - Another major risk is potential changes in shareholding . Given that the working relationship between RHB and EPF has yielded positive results so far, any risk to this partnership could adversely affect the earnings outlook for RHB. However, we believe there is little risk of EPF selling out of RHB.

Companies Mentioned *(Price as of 23 Feb 11)*
Affin Holdings Bhd (AFIN.KL, RM3.37)
Alliance Financial Group BHD (ALFG.KL, RM3.01, OUTPERFORM, TP RM3.70)
AMMB Holdings (AMMB.KL, RM6.30)
CIMB Group Holdings Bhd (CIMB.KL, RM8.19, OUTPERFORM, TP RM10.80)
EON Capital (EONP.KL)
Hong Leong Bank (HLBB.KL, RM9.29, NEUTRAL, TP RM9.30)
Hong Leong Financial Group Berhad (HLCB.KL, RM8.80, OUTPERFORM, TP RM10.00)
Malayan Banking (MBBM.KL, RM8.72, UNDERPERFORM, TP RM7.60)
Public Bank (PUBMe.KL, RM13.08, OUTPERFORM, TP RM17.30)
RHB Capital Berhad (RHBC.KL, RM8.10, OUTPERFORM, TP RM11.80)
United Overseas Bank (UOBH.SI, S$18.32, NEUTRAL, TP S$22.50)
Standard Chartered (STAN.L, 1606.00p, OUTPERFORM, TP 1870.00p, OVERWEIGHT)
Oversea-Chinese Banking Corporation (OCBC.SI, S$9.25, OUTPERFORM, TP S$11.60)
HSBC Holdings (0005.HK, HK$89.05, OUTPERFORM, TP HK$97.00)
Bank of Nova Scotia (BNS.TO, C$58.50, OUTPERFORM, TP C$66.00)
Royal Bank of Scotland (RBS.L, 47.32p, NEUTRAL [V], TP 46.00p, OVERWEIGHT)
Bangkok Bank (BBL.BK, TBH155.5)
Bank of China Ltd (3988.HK, HK$4.00, OUTPERFORM, TP HK$5.22)
Mitsubishi UFJ (8306.T, JPY448)
Deutche Bank (DBKGn.DE, EUR45.845)
JPMorgan Chase (JPM.N, USD45.96)
Bank of America (BAC.N, USD14.17)
Citigroup Inc (C.N, USD4.70)

Disclosure Appendix

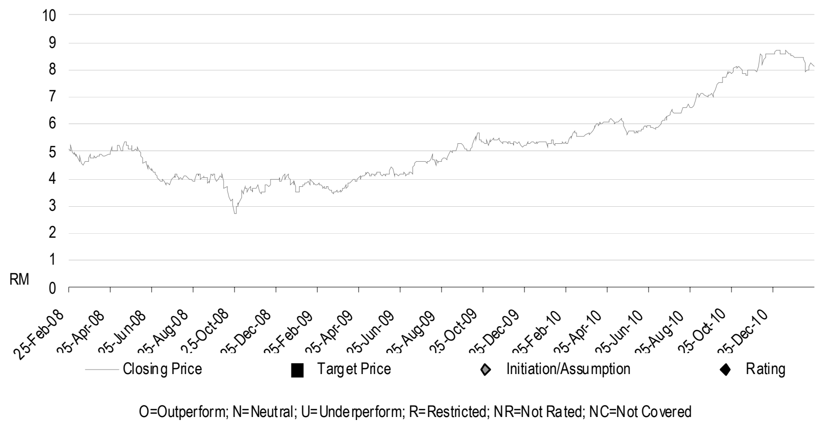
Important Global Disclosures

I, Danny Goh, certify that (1) the views expressed in this report accurately reflect my personal views about all of the subject companies and securities and (2) no part of my compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this report.

See the Companies Mentioned section for full company names.

3-Year Price, Target Price and Rating Change History Chart for RHBC.KL

RHBC.KL Date	Closing Price (RM)	Target Price (RM)	Rating	Initiation/ Assumption



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Outperform (O): The stock's total return is expected to outperform the relevant benchmark* by at least 10-15% (or more, depending on perceived risk) over the next 12 months.

Neutral (N): The stock's total return is expected to be in line with the relevant benchmark* (range of ±10-15%) over the next 12 months.

Underperform (U): The stock's total return is expected to underperform the relevant benchmark* by 10-15% or more over the next 12 months.

Relevant benchmark by region: As of 29th May 2009, Australia, New Zealand, U.S. and Canadian ratings are based on (1) a stock's absolute total return potential to its current share price and (2) the relative attractiveness of a stock's total return potential within an analyst's coverage universe, with Outperforms representing the most attractive, Neutrals the less attractive, and Underperforms the least attractive investment opportunities. Some U.S. and Canadian ratings may fall outside the absolute total return ranges defined above, depending on market conditions and industry factors. For Latin American, Japanese, and non-Japan Asia stocks, ratings are based on a stock's total return relative to the average total return of the relevant country or regional benchmark; for European stocks, ratings are based on a stock's total return relative to the analyst's coverage universe**. For Australian and New Zealand stocks a 22% and a 12% threshold replace the 10-15% level in the Outperform and Underperform stock rating definitions, respectively, subject to analysts' perceived risk. The 22% and 12% thresholds replace the +10-15% and -10-15% levels in the Neutral stock rating definition, respectively, subject to analysts' perceived risk.*

***An analyst's coverage universe consists of all companies covered by the analyst within the relevant sector.*

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Volatility Indicator [V]: A stock is defined as volatile if the stock price has moved up or down by 20% or more in a month in at least 8 of the past 24 months or the analyst expects significant volatility going forward.

Analysts' coverage universe weightings are distinct from analysts' stock ratings and are based on the expected performance of an analyst's coverage universe* versus the relevant broad market benchmark**:

Overweight: Industry expected to outperform the relevant broad market benchmark over the next 12 months.

Market Weight: Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.

Underweight: Industry expected to underperform the relevant broad market benchmark over the next 12 months.

**An analyst's coverage universe consists of all companies covered by the analyst within the relevant sector.*

***The broad market benchmark is based on the expected return of the local market index (e.g., the S&P 500 in the U.S.) over the next 12 months.*

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	Global Ratings Distribution	
Outperform/Buy*	46%	(62% banking clients)
Neutral/Hold*	41%	(60% banking clients)
Underperform/Sell*	11%	(52% banking clients)
Restricted	2%	

**For purposes of the NYSE and NASD ratings distribution disclosure requirements, our stock ratings of Outperform, Neutral, and Underperform most closely correspond to Buy, Hold, and Sell, respectively; however, the meanings are not the same, as our stock ratings are determined on a relative basis. (Please refer to definitions above.) An investor's decision to buy or sell a security should be based on investment objectives, current holdings, and other individual factors.*

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Price Target: (12 months) for (RHBC.KL)
Method: Our target price of RM11.80 for RHB Capital is based on the Gordon growth model, assuming a sustainable return-on-equity (ROE) of 17.6%. We have applied a cost of equity of 11.4% p.a. (using a beta of 1.0) and terminal growth of 6.5% p.a. Our ROE forecast is predicated on the assumption that management will pay out 30% of net earnings in dividends.
Risks: The following risks could impede achievement of our RM11.80 target price for RHB Capital: 1) potential acquisitions could alter its earnings growth trajectory, 2) change in regulatory environment, 3) drastic change in economic outlook, 4) management change and 5) ownership changes

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