**Issuer Profile:**

Neutral (4)

Neutral (4)

**Ticker:**

STANLN

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# Standard Chartered PLC ("StanChart")

## Recommendation

- **FY2020 results highlight the impacts of COVID-19 with statutory profit before tax down 57% y/y to USD1.6bn. On an underlying basis, profit before taxation was down 40% y/y to USD2.5bn on weaker operating income and the substantial rise in credit impairments.**
- **That said, FY2021 has better prospects with the virus under some control in its main markets of China and Singapore. Its focus in 2021 will be on the consolidation of its Asian operations with its wholesale network, affluent clients, mass retail, and sustainability the top of its refreshed priorities. Its CET1 ratio of 14.4% improved 60bps y/y and is above the bank's target range. We will keep the Neutral (4) issuer profile.**
- **With StanChart having weathered the storm of FY2020 intact and positioned to improve in FY2021 together with expected improvements in operating conditions, we are overweight the STANLN 5.375% PERPc24s.**

**Relative Value:**

| Comparative Tier 2s/AT1s | Issuer Profile | Maturity / Call date | Reset Spread | Ask Price | Ask Yield | Spread | Recommen-dation |
|---|---|---|---|---|---|---|---|
| STANLN 5.375% 'PERPc24s | Neutral (4) | 03/10/2024 | 3.683% | 104.0 | 4.16% | 341bps | OW |
| BACR 3.75% '30c25s | Neutral (4) | 23/05/2025 | 1.589% | 105.4 | 2.41% | 152bps | N |
| CMZB 4.875% '27c22s | Neutral (4) | 01/03/2022 | 2.710% | 101.2 | 3.67% | 335bps | OW |
| CMZB 4.2% '28c23s | Neutral (4) | 18/09/2023 | 1.972% | 100.5 | 3.99% | 346bps | N |
| LBBW 3.75% '27c22s | Neutral (4) | 18/05/2022 | 1.780% | 100.5 | 3.31% | 296bps | OW |
| SOCGEN 6.125% 'PERPc24s | Neutral (4) | 16/04/2024 | 4.207% | 104.7 | 4.48% | 383bps | OW |

*Indicative prices as at 5 March 2021 Source: Bloomberg*

## Background

- Formed in 1969, Standard Chartered PLC ("StanChart") is a universal bank, offering broad services aligned both globally and regionally.
- Although headquartered in the UK, StanChart's footprint is skewed towards emerging markets, mostly in Greater China & North Asia (Hong Kong). As at 31 December 2020, it had total assets of USD789.1bn.
- Temasek Holdings Pte Ltd is StanChart's largest shareholder with ~16.2% as at 5 March 2021 followed by institutional investors including BlackRock Inc. and The Vanguard Group.

## Key Considerations

- **Pandemic left its mark on FY2020:** StanChart's FY2020 results highlight the impacts of COVID-19 on overall earnings with statutory profit before tax down 57% y/y to USD1.6bn. On an underlying basis (excluding infrequent or exceptional items), profit before taxation was down 40% y/y to USD2.5bn on weaker operating income and the substantial rise in credit impairments. Statutory results include restructuring charges of USD382mn for business restructuring as well as USD489mn in goodwill impairments for StanChart's businesses in India, UAE, Indonesia and Brunei to reflect weaker operating conditions going forward. Weaker underlying income (-3% y/y in FY2020) was driven by the fall in interest rates that impacted adjusted net interest margins that fell 31bps y/y to an average of 1.31% in FY2020. This was offset to an extent by a 3% y/y fall in operating expenses from lower bonus accruals and reduced discretionary spending with the underlying cost to income ratio rising marginally y/y to 66.4% in FY2020 (65.9% in FY2019). Expenditure increased on digital capabilities while in 4Q2020 there was a USD100mn increase in investment charges as StanChart prepares for an economic recovery in 2021. On a q/q basis, 4Q2020 represented a weaker performance compared to the FY2020 full year with underlying operating income down 9% q/q. This was due to lower Financial Markets performance following a solid 3Q2020 while net interest income rose 9% q/q on a 1bps improvement in net interest margins and growth in average interest earning assets.

- **Higher impairment charges are a cushion with heightened portfolio monitoring to continue:** Underlying credit impairment charges rose 153% or USD1.39bn y/y to USD2.29bn. 59% or USD823mn of the increase were due to impaired or Stage 3 exposures with around one third of total stage 3 impairments of USD1.47bn due to three unrelated Corporate & Institutional Banking exposures from 1Q2020 that were fraud related. The rest of the impairments relate to non-impaired exposures with the bulk of the increase in non-impaired impairments (~60% or USD337mn) due to a management overlay to cover forward looking risks not captured in internal models that were raised in 1H2020. Management indicated there were no new significant stage 3 exposures in 4Q2020 and asset quality is stabilizing with high risk assets continuing to reduce from the peak in August 2020 with 2H2020 credit impairments down USD840mn compared to 1H2020. That said, credit impairment charges rose 6% q/q in 4Q2020 on a 33% q/q rise in stage 3 impairments to USD324mn that was partially offset by a 54% fall in stage 1 and stage 2 impairments. As for loan quality, impaired or stage 3 loans rose 25% y/y to USD9.2bn with the impaired loan ratio at 3.2% as at 31 December 2020 (2.7% as at 31 December 2019). Despite the rise in credit impairments raised in FY2020m the stage 3 cover ratio fell to 58% as at 31 December 2020 against 68% as at 31 December 2019 due to write-offs and new downgrades with low coverage levels but are covered by credit insurance and guarantees from export credit agencies. Including collateral, the coverage ratio improves to 76% as at 31 December 2020 (85% as at 31 December 2019). Management also indicated that the amount of Early Alert Non-Purely Precautionary ("EANPP") accounts rose 50% in FY2020 due to pro-active monitoring of at-risk industries including aviation, hospitality and oil & gas.

- **Segment performance pointing the way forward:** On a segmental basis for FY2020 profit before tax, all segments reported weaker results y/y, particularly in Retail Banking ("RB": -46% y/y on low interest rates and higher impairments) and Commercial Banking ("CB": -57% y/y on higher impairments) while Corporate & Institutional Banking performed relatively better ("CIB": -18% y/y on strong Financial Markets performance and lower expenses). CIB continued to be the main contributor to total underlying profit before tax at 73.4% (68.1% before Central & Other Items, 54.1% in FY2019), followed by RB at 23.4% (21.7% before Central & Other Items, 26.2% in FY2019) and CB at 8.5% (7.9% before Central & Other Items, 12.0% in FY2019). By geography, the importance of Greater China & North Asia was elevated in FY2020 contributing 81.1% to total underlying profit before tax (63.3% before Central & Other Items, 58.3% in FY2019), followed by ASEAN & South Asia at 31.1% (24.2% before Central & Other Items, 24.6% in FY2019). While profit before tax for FY2020 was down 16% and 24% respectively y/y, profit before tax from Africa & Middle East was down materially by 98% (fall in operating income and higher impairments) while Europe & America's profit before tax rose 146% y/y from Financial Markets.

- **Giving back to shareholders within allowance:** StanChart's capital position remains decent in our view with its CET1 ratio stable q/q at 14.4% as at 31 December 2020 and up 60bps y/y from 13.8% as at 31 December 2019 as growth in capital from the sale of its 44.56% equity interest in PT Bank Permata Tbk, regulatory changes and earnings either offset or was higher than the growth in risk weighted assets from negative credit migration, asset growth and higher Financial Markets activity. StanChart's CET1 ratio includes an accrual for the proposed final FY2020 dividend of USD284mn. The CET1 ratio remains above the regulatory minimum requirement of 10.0% and above its 13-14% medium-term target range. Given its capital position, management announced their intention to complete the previously suspended share buy-back program targeting to purchase and cancel up to USD254mn in shares (10bps impact to the CET1 ratio). Both the FY2020 dividend and share buyback are within the limits imposed by the Prudential Regulation Authority.

- **Refining its strategic priorities:** Reported return on tangible equity in FY2020 of 3% was well below StanChart's longer term target of 10% due to the unexpected impacts from the pandemic. Given the altered operating environment, successful execution of its 2019 strategic priorities to date, and StanChart's desire to move from a transformation phase to global leadership phase, the bank has refreshed its overall strategy by focusing on four refined strategic priorities that are an extension of StanChart's 2019 objectives. These priorities include (1) combining its existing network in key emerging markets with delivery of digital capabilities to become a leading international wholesale bank; (2) focusing on wealth management for affluent clients within Retail Banking Priority and Premium, and Private Banking clients; (3) scaling up its mass market retail presence; and (4) providing a differentiated sustainability offering. To support these strategic priorities, StanChart have also identified three enablers – building a future-ready workforce, changing the way they work, and investing in innovation for client experience, operational efficiency and identifying new income opportunities. Management appears cautiously optimistic about the outlook - 2021 income is expected to be stable compared to 2020 on persisting low interest rates while credit impairment charges are expected to fall as the world enters into a recovery phase. This will be balanced however by higher operating expenses from investment in digital capabilities and likely further restructuring charges (USD500mn over the next few years with most in incurred in 2021). These actions however are expected to generate permanent productivity improvements to improve returns and allow the bank to maintain its capital position within its 13-14% target CET1 range.

# Standard Chartered PLC

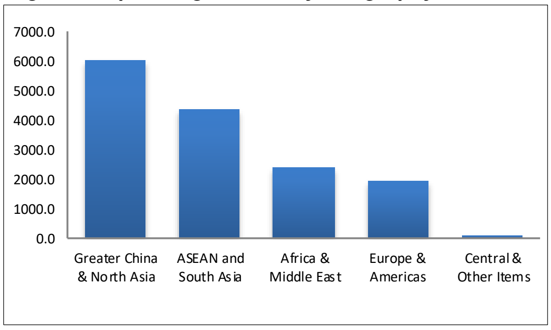
**Table 1: Summary Financials**

| Year Ended 31st Dec | FY2018 | FY2019 | FY2020 |
|---|---|---|---|
| **Income Statement (USD'mn)** | | | |
| Net Interest Income | 7,795 | 7,667 | 6,852 |
| Non Interest Income | 6,994 | 7,750 | 7,902 |
| Operating Expenses | 11,647 | 10,933 | 10,380 |
| Pre-Provision Operating Profit | 3,142 | 4,484 | 4,374 |
| Provisions | 835 | 908 | 2,325 |
| Other Income/(Expenses) | 241 | 137 | -436 |
| PBT | 2,548 | 3,713 | 1,613 |
| Income Taxes | 1,439 | 1,373 | 862 |
| Net Income to Common Shareholders | 1,054 | 2,303 | 724 |
| **Balance Sheet (USD'mn)** | | | |
| Total Assets | 688,762 | 720,398 | 789,050 |
| Total Loans (net) | 256,557 | 268,523 | 281,699 |
| Total Loans (gross) | 262,985 | 274,306 | 288,312 |
| Total Allowances | 6,428 | 5,783 | 6,613 |
| Total NPLs | 8,454 | 7,398 | 9,214 |
| Total Liabilities | 638,410 | 669,737 | 738,321 |
| Total Deposits | 391,013 | 405,357 | 439,339 |
| Total Equity | 50,352 | 50,661 | 50,729 |
| **Key Ratios** | | | |
| NIM | 1.69% | 1.62% | 1.31% |
| Cost-income Ratio | 78.8% | 70.9% | 70.4% |
| LDR | 65.6% | 66.2% | 64.1% |
| NPL Ratio | 3.21% | 2.70% | 3.20% |
| Allowance/NPLs | 76.0% | 78.2% | 71.8% |
| Credit Costs | 0.32% | 0.33% | 0.81% |
| Equity/Assets | 7.31% | 7.03% | 6.43% |
| CETier 1 Ratio | 14.2% | 13.8% | 14.4% |
| Tier 1 Ratio | 16.8% | 16.5% | 16.5% |
| Total CAR | 21.6% | 21.2% | 21.2% |
| ROE | 2.06% | 4.56% | 1.43% |
| ROA | 0.30% | 0.30% | 0.10% |

*Source: Company*

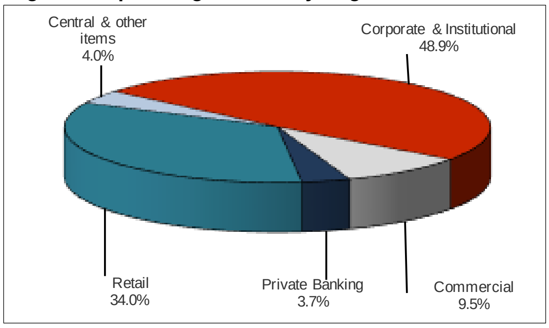
Source: Company

**Figure 1: Operating Income by Geography - FY2020**



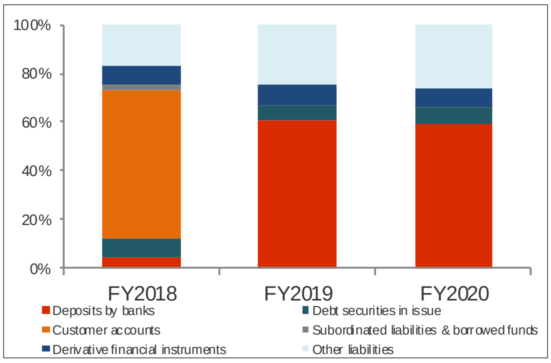

*Source: Company*

**Figure 2: Operating Income by Segment - FY2020**




*Source: Company*

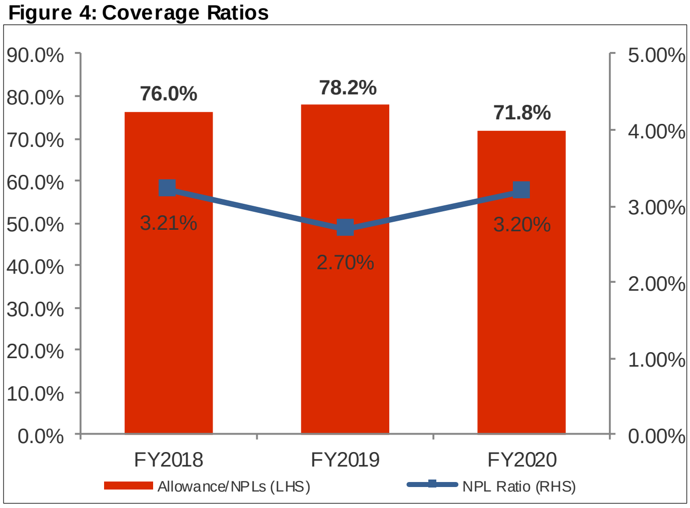
**Figure 3: Liabilities Composition**




*Source: Company*

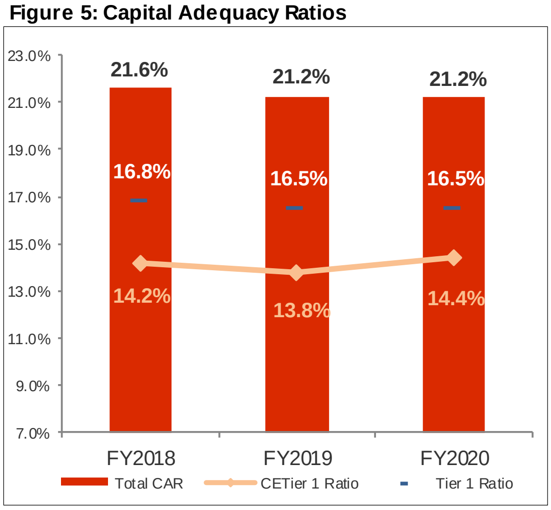
Source: Company

**Figure 4: Coverage Ratios**




*Source: Company, OCBC estimates*

**Figure 5: Capital Adequacy Ratios**




*Source: Company*

**Explanation of Issuer Profile Rating / Issuer Profile Score**

**Positive ("Pos") –** The issuer's credit profile is either strong on an absolute basis or expected to improve to a strong position over the next six months.

**Neutral ("N") –** The issuer's credit profile is fair on an absolute basis or expected to improve / deteriorate to a fair level over the next six months.

**Negative ("Neg") –** The issuer's credit profile is either weaker or highly geared on an absolute basis or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7-point Issuer Profile Score scale.

| IPR | Positive | | Neutral | | | Negative | |
|---|---|---|---|---|---|---|---|
| IPS | 1 | 2 | 3 | 4 | 5 | 6 | 7 |

**Please note that Bond Recommendations are dependent on a bond's price, underlying risk-free rates and an implied credit spread that reflects the strength of the issuer's credit profile. Bond Recommendations may not be relied upon if one or more of these factors change.**

**Explanation of Bond Recommendation**

**Overweight ("OW")** – The bond represents **better relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

**Neutral ("N")** – The represents **fair relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

**Underweight ("UW")** – The represents **weaker relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

**Other**

**Suspension –** We may suspend our issuer rating and bond level recommendation on specific issuers from time to time when OCBC is engaged in other business activities with the issuer. Examples of such activities include acting as a joint lead manager or book runner in a new issue or as an agent in a consent solicitation exercise. We will resume our coverage once these activities are completed.

**Withdrawal ("WD") –** We may withdraw our issuer rating and bond level recommendation on specific issuers from time to time when corporate actions are announced but the outcome of these actions are highly uncertain. We will resume our coverage once there is sufficient clarity in our view on the impact of the proposed action.

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