Edited transcript for DBS first-quarter 2020 results conference call for buy and sell sides, 30 April 2020

Michael Sia Welcome to our first quarter briefing for the buy and sell sides.

Eugene Tarzimanov (Moody's) On asset quality, can you give us a sense of your Stage 2 loans? Many global banks have recorded quite significant increases. On liquidity, where did you deploy the big deposit inflows into because there has not been a huge change in high quality liquid assets.

Chng Sok Hui For Stage 2, we set aside a substantial amount of GP this quarter. Our methodology has not changed. We use a credit cycle index as a guide. Then we add any stress component that we think has not been well factored into the model. The third component, which accounted for the steep increase in GP, is the management overlay.

Piyush Gupta Loan stage classification starts with reported financials, which tends to be a lagging indicator. We therefore incorporate the macroeconomic outlook to determine which names should be downgraded. We also use judgment because the regulators are encouraging us to look past the short-term impact of the pandemic. Therefore, I think the better way to think about it is, are we providing enough? Our model came up with a smaller number than the $703 million of GP we took. We added a much bigger management overlay on top of what the model derived to make sure that we were providing enough for potential moves to Stage 2 over time.

Chng Sok Hui On liquidity, some of the deposits could be transient so we did not deploy all of them in high quality liquid assets as defined by the Basel rules, such as government securities. Some of the deposits found their way into short-term lending or were placed with MAS.

Robert Kong (Citigroup) Three questions if I could. First, for the credit cost guidance of $3 billion-5 billion, what is the corresponding projected NPL rate? Second, where do you think the steady-state NIM will be after the full repricing of loans and assuming that the Fed doesn't raise rates for some time. Third, how much unrealised mark-to-market gains do you have in your bond portfolio?

Piyush Gupta When the Fed went to zero the last time, our NIM bottomed out in the low-1.60% area. Our portfolio hasn't changed substantively since, so that's where it could bottom at. Over the past few years, we've been building duration and yield into our investment portfolio, which can cushion the impact of the current low rates. The portfolio is sitting on unrealised gains that are currently over $1 billion even after the amounts we realised in the first quarter. There is a trade-off: if the gains are harvested, it’s negative for NIM going forward; but if the investments are kept, they accrue interest income and benefit NIM in future periods.

I'm not sure we have an actual projection of the NPL rate for you.

Robert Kong Is there a rule of thumb between harvesting the investment gains now or holding out for better NIM?

Piyush Gupta First, we are guided by accounting rules. A large part of our book is classified as held-to-collect, and there are rules regarding how much can be sold. Second, we are guided by liquidity considerations about what assets to keep. Third, we consider market conditions. When rates fell so massively in the first quarter, it made sense to book the gains you could. When rates go back up after that, it provides an opportunity to rebuild a position.

Aakash Rawat (UBS) First, could you give some colour on what is the exposure to Reits and how you're thinking about commercial REITs? Second, how should we think about RWA inflation for rest of the year and next year?

Piyush Gupta I don't have the answer on Reits at hand, but we've used stress test scenarios to determine free cash flow and so on to see who might be weak. On RWA, we've factored in ratings migration as well as loan growth to calculate the impact on CET1, which we have said could get to the lower end of operating range of 12.5-13.5%.

Aakash Rawat So that includes credit migration and the dividends that you are potentially going to pay. That takes you to the lower end of your range.

Piyush Gupta Correct. So last year our profit before allowances was $8 billion. If you assume some stress in the coming two years, and add $5 billion in cumulative credit costs, then deduct the amount we pay as dividends, you arrive at the projected CET-1.

Aakash Rawat My third question is, if you assume that Fed rates remain at zero for a while, and NIM goes back down to where it was in 2012-14, your ROE was about 12% in those years. Is that a fair ROE to assume when your credit cost stabilises?

Piyush Gupta Our ROE was around 11% in 2012-14, I think that is what you should be looking for.

Aakash Rawat Finally, during Sars and the GFC, credit costs were elevated for three years during each period. Is that a risk as well for this period?

Piyush Gupta Yes, it could be. We have taken a cumulative two-year view because we have not been able to figure out how much allowances we'll see in the coming year as the moratoriums and government packages will provide some relief during the year.

David Wong (Aletheia Capital) Would you be able to offset NIM pressure on net interest income with volume growth through market share gains?

Piyush Gupta It will partly depend on what happens to the economy. Is it going to be like 2009, when it grew strongly? On market share gains, however, I'm confident we can continue to do so. If you look at the past decade, we have been growing share not only in Singapore but around the region in several product categories. In a crisis like the current one, there is an opportunity to build share as long as the franchise is resilient, is willing to support customers and has product capabilities. So I think there are opportunities. I would like to point out that banking is so fragmented that our regional market shares are miniscule. Even in transaction banking, where we've grown a lot, our market share is in the low single digits

Kevin Kwek (Bernstein) Three questions from me. First, on the aviation exposure, could you share your thinking around collateral value given that there wouldn't be a huge demand for aircraft? Second, how adequate is the GP of $703 million given the size of the SME and corporate segments you presented? Third, does the salary cost in the first quarter already include government subsidies and how would the number look into the next few quarters?

Piyush Gupta As I pointed out, one big assumption on aviation is that there will be government support for airlines, and so our assessment is not based entirely on aircraft collateral. But since we had collateral, we wanted to determine how different aircraft types affected collateral valuation: narrow-bodied aircraft values are more resilient than wide-bodied ones at this point in time. We used collateral valuations as a consideration, but also whether a borrower is a national carrier, which would likely be supported.

On GP, I don't believe $703 million will be sufficient, which is why we've given guidance for what we think the cumulative cost of credit could be over the next two years. We have the capacity to keep building GP over the next few quarters before the need for SP manifests itself. You should not assume that we have built all the GP we need in just this quarter.

On the third question, we did not take in any of the government subsidies yet in the first quarter. But let me say that for 2020 we can hold total expenses flat to 2019.

Harsh Modi (JP Morgan) First, what are the unemployment rate assumptions you have used in your stress tests? Second, why did you not put the scrip dividend option in place as it would have allowed you more leeway over time? Third, over the next 12-18 months, there will likely be some interesting deals. If they were available, would you be keen?

Piyush Gupta The unemployment rate assumption is close to 4% for Singapore and about 5% for Hong Kong.

Chng Sok Hui On the scrip dividend, certainly we will evaluate it and decide as we go into the next quarter.

Piyush Gupta Nobody can tell the extent of the ravages of the pandemic and it would be a little foolhardy and certainly premature to think about a deal right now. But fundamentally, we haven't changed our approach to acquisitions. Any deal will have to be strategically relevant, financially attractive and which we can manage and absorb – all the criteria we spoke about before.

Nicholas Teh (Credit Suisse) First, I know the guidance is to try maintaining the dividend but is there a pay-out ratio level that can act as a limitation? Second, what is the LTV on the commercial property loans you have?

Piyush Gupta We do not think of dividends in terms of the pay-out ratio. But if you wanted an indicator, I would say we could live with the 70-80% range. The principal guidance is the stability of the dividend rather than the pay-out ratio. The commercial property LTV is, from memory, around 60% on average.

Jayden Vantarakis (Macquarie) I have three questions. First, on risk weighted asset density, we're still well below GFC or previous crises. Do you have any thoughts on how much it could go up and in what sort of timeframe? Second, how much pricing power do you think the bank has in terms of credit spread? If there is a pick-up in credit risk, how much additional margin will be possible to pick up? Third, what is the Casa ratio after the strong deposit inflows during the quarter?

Piyush Gupta One of the differences in RWA compared to previous crises is the model improvements we have made over the past decade. Our risk density has improved significantly and we still have further opportunities. The private bank assets are on the verge of being approved for upgrade, which will provide RWA relief to mitigate the expected RWA migration for the overall portfolio.

Chng Sok Hui In addition, during the GFC, bilateral netting arrangements had not been put in place. Since then, they have helped in RWA as well.

Piyush Gupta On pricing power, we've been able to price up credit even for the best names at this time. How long it stays obviously depends on competitive intensity as you go forward. If you look at history, I would say that we will continue to have pricing power for the rest of this year if some banks withdraw or become more conservative, but whether it stays into the medium term is anybody's guess.

On Casa, the deposits we got during the quarter were a mix of consumer, which was primarily Casa, and corporate, which was primarily fixed deposits, some of which were short-term.

Michael Sia The deposit inflow was $18 billion for fixed deposits and $21 billion for Casa in nominal terms (and $13 billion and $17 billion respectively in constant-currency terms).

Nick Lord (Morgan Stanley) First, how much RWA movement do you expect to take place over the next nine months. I'm trying to work out how much of that is credit migration.

Piyush Gupta Our projections assume some growth in RWAs but at the same time there are potential savings from portfolio upgrades as well as market risk. There are a lot of moving parts.

Nick Lord On GP, is there a geographic split to the $703 million?

Chng Sok Hui The management overlay, which was the largest part of this quarter's GP, is held at the centre. We don't parcel it out to the various countries.

Krishna Guha (Jefferies) First, which sectors are driving the $10 billion growth in non-trade corporate loans? Second, for the month of April, what kind of payments are you seeing across the network? Some real estate companies are saying they have been able to collect 90% of their usual rent. Have you noticed any month-on-month or year-on-year differences?

Piyush Gupta Out of the $10 billion, $3 billion was from drawdowns of committed lines. The residual $7 billion was diversified: there was real estate and properties; telecoms, media and technology; and acquisitions and privatisations. In the second quarter, we're seeing some financing deals, such as Singapore Airlines. On the second question, we don't have the data you referred to.

Robert Kong Just a couple of follow-ups. First, on the oil trader exposure that became non-performing, could you give a sense of how much you are able to recover? If the dollar exposure was a hundred dollars, how much were you able to offset in terms of recoverable value? Second, you clearly have other exposures in the oil trader segment. I'm wondering if you can comment on how your exposures look there and what might be on your watch list. Third, as the loan moratoriums progress, where do you think the low point for your LCR and NSFR are as you absorb more of that liquidity?

Piyush Gupta On the first question, it's tough to call. As you know, the banks are right now trying to investigate what is salvageable. The oil trader has trading positions, oil inventories and receivables, but it will take time to ascertain how much are recoverable. We have taken a proportion of our exposure as allowances without being able to get any real insight into how much collateral can be set off. Therefore it's possible we have to top up allowances in the second quarter. It's also possible we've taken enough allowances already. We don't know just yet. To your second question, we don't have any other oil trader exposure that is under suspicion of fraud.

On your third question, the amount of payments affected by loan moratoriums – about $0.5 billion this year – will eventually come to us, so it doesn't move the needle too much in terms of cash flow, so it's not that material.

Michael Sia Thank you for joining us. We'll see you next quarter.