Edited transcript of DBS third-quarter 2020 results conference call for buy and sell sides, 5 November 2020

Michael Sia Welcome to the briefing.

Jayden Vantarakis (Macquarie) You have given NIM guidance of 1.45-1.50% for the coming year. Could you let us know what the exit NIM in September was? You had said in the previous quarter that excess deposits placed in risk-free assets had a six-basis-point impact on NIM. What was the impact this quarter?

Piyush Gupta The exit NIM in September was 1.52%, not much difference from the 1.53% for the full quarter. The guidance for next year has a couple of moving parts. Nobody knows what will happen to market interest rates but we are assuming they stay roughly where they are now. This leaves the repricing of the FHR and fixed-rate loans, which we model will have an impact of a few basis points.

What we don't know is the second part of your question. Excess liquidity placed with the MAS is still impacting NIM by about five basis points. But how much of the liquidity stays is not entirely certain. Right now it looks sticky as we have continued to attract deposits. While these excess deposits impact NIM, they are accretive to earnings and ROE. On the other hand, you could make the case that by next year some of these deposits will flow out, in which case the reverse will happen.

Jayden Vantarakis During the media briefing you said you would lift dividends when possible. And risk-weighted assets are broadly flat for the quarter. Do you have any views what risk-weighted asset inflation may be in next year? What's the base case you're building in and what's the implication for dividends?

Chng Sok Hui There are a few factors. One will be loan growth, which we have guided to be in the mid-single digit. Another will be from model refinements that are undergoing approval at this time. The third is credit migration. Depending on the impact of moratoriums we might see some downward migrations, but our capital is comfortably cushioned at this stage.

Piyush Gupta I think there will be some migration but the size is uncertain. With CET-1 at 13.9%, which is above our operating range, we do have the capacity to step up our dividends.

Jayden Vantarakis Can you tell us how much was the net new money for AUM?

Piyush Gupta Our net new inflows have been SGD 2 billion-3 billion a quarter this year.

Robert Kong (Citigroup) On asset quality, I know you're sticking to the guidance on total allowances and I'm very glad that you're being conservative. But are there incremental developments to suggest you might come in towards the lower end of your guidance at SGD 3 billion. If you do, then you would have been fully provided by the end-2020, in which case you can normalise credit costs next year. That seems to be the guidance from the other banks that we've spoken to so far.

Piyush Gupta I like Jamie Dimon's response to this question a couple of weeks ago when he said JPM's allowances could be SGD 10 billion off on one side or SGD 20 billion on the other side. I feel much the same way. The reality is that anybody with a view of how much damage there is once the tide goes out is just guessing.

I'll take you through our businesses individually. In the consumer business, unsecured delinquencies are up from a year ago, although they have improved since the second quarter because economies have re-opened and our collections have stepped up. But I don't know how much of the improvement is also due to government support. And so when the support ends next year and the pain is felt, it is difficult to tell how much the deterioration will be.

For SMEs, the key to me are the moratoriums. While the SGD 13.5 billion we have is proportionately lower than other banks, how much of it eventually defaults is hard to say. What we're doing is not to rely on financials but cash flow forecasting. We're using data analytics to see much money is going into their operating accounts. While it's early days, there has been some cash flow improvement two months into the economic re-opening. But it will take more time to really understand which businesses are going to be able to withstand the challenges ahead, of how many would have only a liquidity issue and how many a solvency issue.

So you could make a case of defaults at 10%, 15%, 20% or 25%. I have no way of knowing what the right number is. A 10% default of corporate moratoriums would be SGD 1.3 billion; a 20% would be SGD 2.7 billion. And then you've got to assume how much can be recovered from collateral. The exposure is very much secured against shophouses, properties, plants and so on. What happens when we try to monetise them next year is anybody's guess. Would the recovery rate be the same as it has traditionally been? Nobody knows. So because you don't know either the proportion of defaults or the amount that can be recovered, the best thing to do is to take a conservative stance.

For large corporates, we have better line of sight because we review them name by name. Our watchlist is relatively okay and we're not seeing a lot of deterioration. So this portfolio is probably at the better end of expectations so far.

Because there is so much uncertainty, I don't want to give a prediction which end of the guidance we will end up. But if we can cover SGD 3 billion this year, it means we can end up in the SGD 1 billion range next year.

Robert Kong You said in the previous quarter you were rethinking longer-term workforce and office plans. How are you thinking about your long-term costs?

Piyush Gupta We have task forces working on this. But we do expect that over the next two to three years, there will be a big pick-up in digital adoption from customers and hence our workforce and occupancy structure. In fact we took a small charge this quarter for the restructuring of our branch footprint. The potential for restructuring our expense base is real. We need some more time to get our hands around the specifics.

Robert Kong Could you give an update on digibank in India and Indonesia.

Piyush Gupta They haven't changed much since the previous quarter. In both countries, digibank is now working to what we most recently modelled. We continue to get better quality customers. With recent regulatory changes in India they've sort of liberalised again, giving us the opportunity to start acquiring customers more easily than two or three quarters ago. But we've slowed down on lending this year for obvious reasons to both consumers and SMEs. Deposits, wealth management and payments are doing well.

Aakash Rawat (UBS) On the asset quality outlook, it seems your peers have been guided by their experience on Malaysia, where there have been encouraging repayment trends since the expiry of moratoriums, which I guess is why they're feeling more comfortable overall. Is it fair to say you're missing that part?

Piyush Gupta As we don't have Malaysia exposures I am not in the best position to comment. But as the moratorium expired on 30 September, and we are now in the first week of November, I think it's still a bit early to figure out what the actual ability to repay is. But it could well be that a lot of customers are able to pay.

One of the requirements for the moratorium extension in Singapore is to require SMEs to make principal repayments of 20% from January. If customers are able to do so, it gives a lot of confidence that they are able to sustain their businesses.

The short answer is you could be right. It could be that peers are getting an early read from Malaysia which we don't have, but I also think that has only been four weeks and it is premature to know what's happening.

Aakash Rawat On structural cost changes, do you think that DBS can operate with significantly fewer branches in Singapore in a few years?

Piyush Gupta The right way is to think in terms of the nature of branches. We've been digitalising our branches and we're going to accelerate that. You will see branches with smaller footprint that are more digitalised and require less staffing even as we maintain our points of presence. I could even see a situation where there are more small kiosks in community centres and other locations that would be very low cost.

Aakash Rawat Based on your comments that discretionary portfolio management advisory as a percentage of total AUMs has not changed materially, is it fair to say that overall wealth management margins are probably not going to improve much in the next two three years?

Piyush Gupta I think that's a reasonable assumption. DPM advisory is growing, but the rest of the wealth management business is also growing, and so the relative percentage will stay in the same range.

Melissa Kuang (Goldman Sachs) Corporate loan moratoriums went up a bit. Can you let us know where that is coming from for that? In terms of your fee income guidance of double-digit growth, where do you see it coming from?

Piyush Gupta Corporate loan moratoriums went up from SGD 12.6 billion in the previous quarter to SGD 13.5 billion, of which SGD 500 million was in Hong Kong and most of the remainder in Singapore. On fee income growth, wealth management will continue to be a big driver while cards and payments will continue to recover. I expect brokerage to remain relatively strong. If Biden wins the US presidential elections, you might see momentum in emerging market equities. On investment banking, we have started seeing the deal flow pick up again; we have a robust pipeline for both ECM and DCM. So fee income growth is quite broad-based.

Melissa Kuang Can you remind us what percentage of your loan book is fixed and floating?

Piyush Gupta For housing loans, SGD 45 billion is on fixed rates or FHR, about half of which will be repriced this year and the remainder over the next two years. For corporate loans, only about SGD 20 billion is on fixed rates that reprice over four or five years. We also have a bond portfolio that reprices over the same period. Credit spreads are holding up, so the only impact on NIM from repricing is from interest rate changes.

Harsh Modi (JP Morgan) Were the new NPAs this quarter on moratorium or not?

Piyush Gupta They were not on moratorium. Moratorium loans are mainly to SMEs.

Harsh Modi You already have SGD 4 billion of GP reserves. Let’s say the moratorium loans have a default rate of 30% and a loss given default of 40%, your GP reserves would be more than sufficient to cover them. So are you more concerned about non-moratorium credits defaulting?

Piyush Gupta That’s the right way to look at it. The issue is uncertainty. In a normal year, our credit costs would be SGD 700 million-800 million, or SGD 1.5 billion over two years. Then the question is what the additional amount is for 2020-21. It is hard to call, but if one estimates additional allowances for the consumer and SME portfolios at SGD 1.5 billion, the result would be SGD 3 billion. Then one estimate additional allowances for the large corporate book to derive total allowances for 2020-21.

Now one could also easily paint a scenario where total allowances might not even reach SGD 3 billion. So while one could paint a scenario of SGD 4 billion or SGD 5 billion, one could paint a more optimistic scenario as well. So the sensible thing for us has been to fortify the balance sheet upfront.

Harsh Modi Since loan growth is a function of nominal GDP, is there upside risk to your loan growth guidance of mid-single digit for a region that is broadly growing at a nominal 8%?

Piyush Gupta The upside risk is possible, but if you look at what's happened in the past three to four months, corporates have been issuing bonds in Asia and elsewhere because there is so much liquidity and yield curve has been flat. That means they don’t need as much bank loans. That’s one uncertainty. Another is how fast and sustainable the re-opening of regional economies is. We are still not that clear when we would accelerate growth in SME loans. We have let some of them run down because we have been cautious. But in the large corporate space, I think there might be opportunities.

Harsh Modi How have digital capabilities helped in underwriting? Over the recent stressful nine-month period, have you seen any differences from using AI to figure out cash flows?

Piyush Gupta For SME and consumer business, we are using more data and algorithms for onboarding. We’ve also got algorithmic-based lending. And I believe that is doing two things. First, it allows us to improve the quality of our underwriting although we certainly still rely on credit bureaus. Second, data have allowed us to go into parts of the market that are potentially unbanked. We wouldn’t have been able to bank customers with no credit bureau history or scores in the past, but because we’ve been able to build proxies for credit bureau scores, we are able to add portfolios we weren’t able to. We started doing so late last year but have slowed down because of the pandemic.

In addition, digitalisation has been helpful in early monitoring and managing the portfolio. The impact is very significant. We can not only track cash flows but also put models to predict what future cash flows might be. We have something called networking analysis to see everyone else in the system that would be impacted by a particular customer's weakness. This helps in our monitoring and watch list process, which allows us to engage customers early and improve credit risk management.

Harsh Modi One last question. On the digital exchange, is it anything meaningful?

Piyush Gupta We don't have regulatory approval, so I'd rather not talk about it at this point in time.

Krishna Guha (Jefferies) You seem quite optimistic about growth. Are there any regions you would like to highlight?

Piyush Gupta The strong growth next year is due to the low base this year. So we are saying that you will see a V-shape recovery in Asia. And we're seeing that. Our pipelines in China are robust, stronger than I've seen in the past few years. And in India as well to some extent. This is going to the best year we've had in India in a long time, partly because the rest of the banking system is on the backfoot somewhat. We cleaned up our book some time ago and because we have both capital and liquidity, we're able to do have a strong year in India. My general take is that across the region, you will see a lot of activity. I think M&A will continue to be strong. Some of that will be in new capital investments.

And we're well positioned. There have been incremental supply-chain shifts involving Korean and Taiwanese companies. Money is beginning to go to India and Vietnam. We are in a position to intermediate these moves. Very few banks who have that footprint that we can cover, so it's quite positive for us.

Michael Sia Thank you for joining us. See you next quarter.