Transcript of DBS third-quarter 2016 results conference call for buy and sell sides, 31 October 2016

Michael Sia: Hello, everybody, and welcome to our third quarter conference call for the buy and sell side. With me are Piyush and Sok Hui and the rest of the management team here in Singapore and Hong Kong. We will just start off and take questions. We had two extensive briefings over the past two hours, so we can start off with questions immediately. Aaron, can you take questions now?

Operator: Thank you. We will now begin the question and answer session. Participants with questions to pose, please press zero one on your telephone keypad, and you'll be placed in the queue. To cancel the queue, please press zero two. Once again, zero one on your telephone keypad now. Our first question, Harsh Modi from JP Morgan. Please go ahead.

Harsh Modi: Hi, Piyush. A couple of questions. One is on this guidance on further weakness on margins. Is this coming just from SIBOR/SOR weakness, or there's something else, even credit spreads are going down? And second is just your view on this weaker transmission of LIBOR into Sing dollar rates, and how does that impact your view on margins next year?

And second is on asset quality. With this assessment that the long tail of O&G from one-third to half being at risk, how much of that devolves into NPLs in the next three to six months? Thanks.

Piyush Gupta: On the margin question, it's mostly to do with SIBOR/SOR. So, SIBOR/SOR anticipation is that the full impact of it will flow into the fourth quarter, and we'll give up a few basis points on the back of that. Credit spreads are actually holding up reasonably well. In the third quarter, in addition to the SIBOR/SOR, the other thing we did is we bulked up for liquidity, because of the change in the commercial paper situation in the US, and the uncertainty on the political side, we just chose to be more conservative and added up liquidity.

As that event is getting behind us, we can scale the liquidity down somewhat, so actually in some ways that might be beneficial, but SIBOR/SOR is the real issue, challenge on that front. I'm not sure what you meant when you said the transmission of weaker LIBOR to SIBOR.

Actually, as I said before, the SIBOR/SOR could have [come] down a lot more. If you ask me, the fact that LIBOR rates went up because of the same commercial paper challenge actually helped cushion some of the SIBOR/SOR situation. My own view is at the stage we reached any hikes – whether it's the December hike, we're positing a couple hikes next year – that you will start seeing [some] positive impact from those hikes on SIBOR/SOR, [but] whether all of it flows through to the Sing dollar [rates] is hard to say.

Traditionally, if you look at it historically, the Sing dollar [rates] pretty much starts reflecting it with a time lag, maybe two, three months after the US rates move. How tight the transmission mechanism is going forward is not entirely clear, but I do think that we will get some uplift from a tightening of the US policy late into next year.

The weak cases in that long tail have gone up, but it's quite granular, and as we look going forward, I think we might see a couple of them going non-performing in the fourth quarter, but as you look into next year, I don't expect it to be very large, and we'll probably be able to deal with it quite comfortably within our business-as-usual provisioning process. That's our current view.

Harsh Modi: Right, and sorry, just on the lengthening of duration of some of the loans where you said that the vessel life is long, and the loans are short, so you're lengthening the duration, does that get classified as restructured loans, or do they get classified as NPL as mentioned, or not really?

Piyush Gupta: No, they don't. So, I've been through this before. Our NPL policy is consistent with everybody else, not only in the market but around the world actually, that you make a distinction between [NPLs and] loans which are being refinanced, but refinanced around a commercially viable basis.

If a business is deemed to be commercially viable, but they have a liquidity situation, their assets are good, and so by refinancing the loans to be more in line with the cash flows, they should do okay. We don't classify those as either restructured or non-performing.

On the other hand, when you're in a situation where you don't assess the business to be viable, or you're forced to look at the [loan in] non-commercial terms, you have to drop pricing, then we keep those loans as restructured, even if they're not overdue. Then we'll treat them as non-performing. So they're two distinct categories.

Harsh Modi: Okay. Thank you.

Operator: Thank you. Our next question, Nick Lord from Morgan Stanley. Please go ahead.

Nick Lord: Okay, thank you very much for the call, Piyush. A couple of questions. First one is just on the write-offs in the third quarter. They were up at $491 [million]. Give us a little bit of clarity on what was being written off in the quarter. And then secondly, maybe just ask Sok Hui to clarify something she said in the presentation which I slightly missed.

In terms of Basel 3.5 impact, did you say that you now expect very little impact from the Fundamental Review of the Trading Book [FRTB], and if that is true, what's changed since the last couple of quarters that brings down that forecast impact?

Piyush Gupta: On the write-offs, the biggest chunk of what we wrote off was almost $200 million of Swiber. Of the total Swiber exposure, $190-something [million] is actually what we wrote off, because we figure that that's a component which is very unlikely for us to make any recoveries. Ex of that, the write-downs are fairly normal across the region. [For] some of our previous exposures, in a couple of cases we topped up and took 100% provision, and [then] we wrote it off. In some, we just wrote it off, but the bulk of that was the Swiber impact. Sok Hui, do you want to…?

Chng Sok Hui: On the Basel 3.5, the rules have been clarified around the Standardised Approach for Counterparty Credit Risk, as well as the FRTB rules. So, as we progress with updates to the MAS on each of the quantitative impact assessments, with each exercise that we conducted, we received more clarification from Basel on how the items are to be treated.

So, based on the latest quantitative impact study that we have submitted, actually the numbers look very manageable, so it's actually not going to be the impact we had originally anticipated, so the number is actually down to a very manageable number.

Nick Lord: So, when you say very manageable, are we talking about low single-digit percent impact on risk-weighted assets? Is that what you would define as manageable?

Chng Sok Hui: Risk-weighted assets will be around the $10 billion range.

Nick Lord: Okay, impact from both.

Chng Sok Hui: So, very small.

Nick Lord: Okay, thank you.

Chng Sok Hui: In RWA terms.

Nick Lord: Yes.

Operator: Thank you. Our next question, Thomas from Macquarie. Please go ahead.

Thomas Stoegner: Thank you for the call. Can you just provide a bit more details on the credit cost guidance for 2017? I think you implied some 30 basis points in credit costs for next year, and I think you assumed that provisions relating to the oil and gas sector will start to taper off. Why do you assume this, and then what do you see for the non-oil sectors?

And then further I wanted to ask what level of new non-performing loans do you think is a normalised quarterly run rate, and then what industries or geographies may drive the new non-performing loans?

Piyush Gupta: We'll start with the last part of your question, where do we see the overall portfolio. Outside of the oil and gas, and what I've flagged earlier – steel and coal, we're actually not seeing a lot of stress in the portfolio overall. And then on a different part – SMEs, there's been some continued stress in SME that was originally in India, and then China and around the region. But we think [that of the] chunky non-performing items, actually the two big ones in oil and gas are done, so the rest of it is going to be quite granular. And my own sense is that even through next year, our NPL rate will probably stay south of 1.5%, maybe 1.5%, 1.3%, somewhere in that range. I don't see a lot more in the pipeline to warrant a much bigger uptick in non-performing loans.

If that is indeed the case, then the related impact on our provisioning will also be consistent with what we've seen in the last few quarters. This year, ex the Swiber impact I mentioned earlier, we targeted about $750 million in provisioning, [but] ex-Swiber we'll [actually] do $850 [million this year], so that's higher than what we anticipated.

Next year we're going with a view probably somewhere around that number again. Don't expect it to be much worse. Where is that likely to come from? I think we might see some continued residual impact from parts of our portfolio which are already non-performing. So, you [initially] make some assessment on how much provisions you need, but as you move on sometimes, you wind up having to take more provisions around that.

And I think we will continue with more provisions around the SME sector. I think the SME sector will take some time before you see some turnaround, so probably some more provisions there as well.

Thomas Stoegner: Thank you.

Operator: Hello, next question, Loo Kar Weng from HSBC. Please go ahead.

Loo Kar Weng: Hi. Thanks for the call. I've just got a few questions. Most of them are actually with regards to the ANZ transaction. So, I just wanted to get your sense of how you feel the competitive dynamics are changing in Singapore. So, I think back in 2012…

Piyush Gupta: Sorry, competitive dynamics is changing… I didn't hear the full sentence. Competitive dynamics is changing…

Michael Sia: Did you say Singapore?

Piyush Gupta: In Singapore, oh.

Loo Kar Weng: Yes, in Singapore. As you know, back in 2012, MAS basically said that the QFBs need to locally incorporate, and now basically ANZ is getting rid of their retail ops, I just wanted to get a sense of how you think things might actually develop. That's my first question. Maybe I'll ask the rest after that.

Piyush Gupta: I think it's hard to generalise. I think if you look at the last two, three years, many of the Western, the European names have been exiting the market. So, Barclays scaled down, as you know before RBS, they scaled down, and so on, now ANZ is exiting, so it's quite clear that people are rethinking their retail strategies. Even more established players, Citi, HSBC, have chosen to scale down in other parts of Asia. Not in Singapore though, they've continued to double down in Singapore.

On the other hand, I think over time you will see more presence of the Chinese banks in Asia. I know the Malaysians are still very keen on expanding their activities in Singapore. So, I think overall the competitive intensity in Singapore will continue to be roughly where it's been for the last few years. We don't see it substantially higher or significantly lower.

Within that, we've been fortunate that in the last couple of years we've been able to continue to increase market share. We're increasing market share across several asset classes, the mortgage business, the cards business, we're holding our savings account market share, we're increasing our bancassurance and wealth market share.

Some of that is to do not with competitive intensity, I believe, but just that we've been able to leverage the digital transformation and create a focus on some of our specific product lines in Singapore, and therefore both from a market share standpoint as well as actually from a profitability standpoint, our business is doing quite well. Our cost-income ratios for our consumer retail business in Singapore have been improving very significantly year after year. So, we feel very good about our relative position in the market overall.

Loo Kar Weng: I guess what I was alluding to is that despite the changing landscape in the market and the progress that you've made, we haven't really seen an improvement in pricing power at all, have we, within the various lending segments within Singapore?

Piyush Gupta: I don't think it's reasonable to expect improvement in pricing power. You get improved pricing power only if you've wound up with a monopoly or a tight duopoly. That's not the situation. There's just enough players in the market so you'll always have a competitive top line, in some business lines more, in some business lines less.

I think profitability in the market will come from things you can do on the cost line, not on the revenue line, and I think that's true for the retail business around the world in general, that as you see the impact of digitisation take place, you have to assume that you'll continue to find a top-line shrinkage in margins, but you have to make up for it in cost-income ratios, and that's what our focus is, and we've been able to do that quite successfully.

Loo Kar Weng: Got it. My other questions are much more granular in detail. I think that income disclosure with regards to the purchase consideration for ANZ, is it actually possible to break up how much was paid for the wealth management business and the retail business separately?

Piyush Gupta: No, we actually didn't approach it like that at all, so we did not unbundle what we're paying for wealth and what we're paying for retail. It's how we choose to look at the business. When we evaluated it, we said there is [both] a wealth business here and a retail business here, and chose to think of it in those terms.

When you look at the consideration you're paying, some of it relates to the trailer fees on the non-balance sheet AUMs over time. So, we've come to some agreement on which portion of those trailer fees we'll pass on to ANZ. That obviously you could attribute more to the wealth business than to the retail business. But the number is a composite number.

Loo Kar Weng: Okay. So, the $50 million profit number quoted by ANZ, that can't be broken up either?

Piyush Gupta: That can't be broken up either, no.

Loo Kar Weng: Okay, maybe just one other quick question. Can you remind me what your strategy in Indonesia was, because I was under the impression that you were basically riding mainly on the corporate business there. So, with this acquisition of ANZ's retail customer base in ANZ, does that represent a change in thinking?

Piyush Gupta: Actually not. In fact, if you go back to what we said when we launched the digital strategy – and we said we [would do] India first. We said that potentially this allows us the opportunity to expand our affluent business in these countries – to the emerging affluent and the upper middle class. But our whole agenda is that we want to try and do that principally digitally.

That's why the Digibank India launch is consistent with that. We now have actually [acquired] I want to say 300,000, last I saw it was probably closer to 350,000 new customers over the last four, five months. Those are all upper-income, but also mid-market customers who would not necessarily qualify as mass affluent, but we're doing it digitally. So, that is the agenda for other countries, both Indonesia, Taiwan, and China over time, that if we can do a digital penetration, then we will go a little bit deeper than mass affluent into what I call the emerging affluent base.

Loo Kar Weng: Got it. Okay, thank you.

Operator: Thank you. Our next question, Aakash from UBS. Please go ahead.

Aakash Rawat: Hi, thanks for the call. A few questions. Firstly, on the ANZ transaction, I'm not sure I understand how the 0.5% of AUM number comes up, because I'm under the impression that the book value is probably around $700 million or so, and if you're putting $110 million on top of that, obviously it will depend on when the transaction actually happens, but that's probably around $800 million or so, and $23 billion in assets. So, how do we get this 0.5% number which was in the presentation? That's the first question.

Second is on fixed costs. You said for this year you're expecting 43%, 44% [cost-income ratio]. Do you have a target for next year? And out of the cost efficiencies that you achieved this quarter, how much would you attribute to productivity gains versus how much of it is the strategic cost initiatives? And just some outlook on that for next year.

And thirdly on asset quality, a few questions there. How much of the provisions for this quarter were for the existing ones? If you were topping up your provisions there, how much of it was for the new NPLs, which was around $1 billion or so?

And one more question I have is, I don't know if you have the answer there, but OCBC didn't really see an increase in NPLs this quarter whereas I would think that there's not a huge difference between your oil and gas portfolio and theirs, so why this difference – why did we see a pickup in NPLs at DBS, but not at OCBC? Do you have any thoughts on that? That's all for me.

Michael Sia: Sorry, before we go, just on your question on SPs for new and existing NPLs – it is on page 27 of the CFO deck.

Aakash Rawat: Okay, cool, right.

Piyush Gupta: On your other question, so the percent of AUM is the standard for how percent of AUM is calculated, and in every other transaction around the region you transfer balance sheet assets at book, but when you talk about what you're paying for the total Wealth business, you treat it as a percentage of total assets under management independent of the book value. Sok Hui, you want to elaborate?

Chng Sok Hui: Yes. So, the way we look at it, a lot of the deposits as well as the investments under AUM, we look at it as basically the wealth AUM. So, if you take the $110 million divided by the $23 billion AUM that we have from the wealth segment, that is really the percentage that you're talking about.

Piyush Gupta: In other words, this measure is quite consistent. So, if you look at a SocGen transaction, or you look at a Barclays transaction, or any other transaction in Asia, that's always how it's calculated, it's the total goodwill or premium paid divided by the total AUMs. That's how we calculate it as well.

Aakash Rawat: Thank you. So, this 0.5% is very much comparable to the 1.8% number that you've seen in the past few transactions.

Piyush Gupta: That's correct. So, it's the same basis as 1.8%, with the caveat that if you look at the 1.8% in the market, by and large those tend to be private banking AUMs. In our case, two-thirds of the AUMs or more are mass affluent AUMs and not private bank AUMs. So, you could argue that you don't use the same prism. The reason that happens typically is that mass affluent AUMs tend to come with a higher cost base, because they tend to come with a branch footprint and a higher technology cost. So, cost-income ratio of mass affluent is typically higher than cost-income ratio of private bank.

In our case, actually it's fair to look at them with the same prism because we are not going to incur the higher cost-income from a mass affluent business because we're just going to take this whole thing and fold it into an existing infrastructure, but again that's just for additional colour, if you will. Your cost-income ratio, Sok Hui, do you want to take that as well, projections?

Chng Sok Hui: So, we gave guidance that for the year as a whole, we should be between 43% to 44%, which suggests that in fourth quarter I think the growth will be really moderate as well, and looking to next year, we've also guided there will be flat jaws, so to the extent that revenue [growth] will be single-digit, expenses will likewise be in that range.

We have been seeing really good productivity in our cost management, so if you look at the year-to-date headcount, we have got a reduction of headcount by about 116 just with a normal attrition process without having to add staff for the increased volume of business. We have rationalised some of our branches. You find that these productivity gains are real, and as we digitise further, we expect more and more to come out of these productivity saves.

Piyush Gupta: I pointed out somewhere, our call centre in Singapore, for example, our headcount peaked at 670. Today we're down to 450 on a larger book of business and larger volumes, and that's just because we've been able to digitise the end-to-end flow around several traditionally large-volume call [types]. And we've been able to do that in several other parts of our business, essentially taking out paper and taking out workload and volume, and so that's flowing through.

I also pointed out earlier that we've been doing all this now for a couple of years. That has given us some flexibility on the expense line. Oftentimes we've chosen to take some of these savings and then plough them back into business. So, if you look at the difference between second quarter and third quarter, second quarter we took some of these savings and put them back into our Digibank launch, into the marketing effort, into several other marketing initiatives. In the third quarter, we actually just let the savings flow through to the bottom line. So, we do have some ability do to that because of the strategic savings that we are generating.

Your last question on the NPL, it is hard for me to comment on OCBC other than reiterate the comment I made a couple of times before, that if you look at [NPLs] on a name-by-name basis, which we've done now for these two quarters, our policies for recognising non-performing [loans] are no different from any of our competitors in Singapore and around the region.

So, on a name-by-name basis, there's nothing that any competitor puts into non-performing before we put into non-performing. My speculation was and continues to be the case that some of the portfolio of some of our competitors is more Indonesia- and Malaysia-concentrated, and they started seeing stress in the Indonesia and Malaysia part of the portfolio before we started seeing the stress in the Singapore side of the portfolio.

Partly, that reflects the size of the companies, that the company is slightly bigger and therefore had some more resilience in the Singapore side of the book than the Malaysia-Indonesia side of the book. So, that might explain some of the difference in the shape of the curve for some of our competitors and us, but I have to admit that I'm speculating a bit here, because I frankly don't have that good an understanding of what exactly their situation is.

Aakash Rawat: Right, thanks for that. Just one last question quickly, if I may. What is the expectation for provision charges for next quarter? Is it going to be in the 50 basis point range overall, or would it normalise back to your 30 basis point range?

Piyush Gupta: I think it should normalise back, because I think it will be a lot more granular going forward from here.

Aakash Rawat: Okay, thank you very much.

Operator: Thank you. Our next question, Sukrit from Deutsche Bank. Please go ahead.

Sukrit Khatri: Thank you very much. I had a couple of questions. First was on China. I see that your loan book seems to have fluctuated. In December, it was about $40-something billion, and then it went down in June, now it's back up. Could you please explain where exactly is that coming from, what is driving it?

Piyush Gupta: Yes. Some of the big delta in China always tends to be around trade, because for us the opportunity to do trade finance vis-à-vis letters of credit from the Chinese banks at the margin is business we can choose or not choose to do. Underlying customer demand is actually quite robust.

Sometimes we choose to do it, and sometimes we don't, partly a function of the liquidity we have, and partly a function of the margins that we can get. That in turn depends on competitive intensity. That moves up and down a bit. In this last quarter, the trade from China actually popped up by $3 billion or $4 billion, but like I said, that moves up and down.

Sukrit Khatri: And how much visibility do you have for the next quarter or something? Is it sustainable or should we expect it to move up or down by $4 billion or $5 billion or something like that?

Piyush Gupta: No, I think at this point in time, I think it should be sustainable, flat.

Sukrit Khatri: Okay. Second is again on just especially your provision. I mean, what's your comfort level? The tone that I get from you seems to be slightly different from the other two banks, and you said that you believe that the worst could be over on the O&G book. So, I'm just trying to understand what's the comfort range around your provisions that we should be factoring in, if not for 2016, for 2017 onwards.

Piyush Gupta: Yes, so I think it does back to that, but I'm going to be careful, I think there's still stress in the sector. So, you know, please don't misunderstand what I'm saying. I think the sector is stressed, and if you break it down into two, I think the exploration part of the business will continue to be stressed through 2017.

Even at $50 oil prices, I don't see a lot of the majors wanting to do new exploration activity. So, what I said, a couple of projects have been announced. I saw something from Total or something from BP, but they're still few and far between, and my own sense is even if oil price starts trending up to $55, $60 that people are paying, you will not see a lot of significant upmarket investment start going in 2017. You might start seeing some of it in 2018 as opposed to 2017. What that means is that anybody who supports exploration activity, so people in the jack-up, the rig business, et cetera, I think they will still see a lot of headwinds over the next few quarters.

It is on the production support side of the business where my sense is we might have seen a trough. That doesn't necessarily mean you'll see a massive upswing anytime soon. I just think we might have seen a floor in terms of how bad that gets for people. Now, even if at this level it's a trough, there is still a lot of pain, because like I said, there is about 60% fleet utilisation in that segment, which means that cash flows are depressed.

First of all, people have ships which are not being put to work and, because of the excess capacity, margins are being shrunk, so cash flows are down. However, at $50 to $60 oil prices, I don't see more squeeze coming on the margin from the buyers, and I think the support sector has about reached the bottom of what they can afford to cut, and therefore I think the cash flows they're seeing now, you can use them fairly safely as a base case set of projections on what you might want to project out if you wanted to look at what the cash flows for some of the players in that part of the sector might be.

Our note on what the provisions are likely to be in the sector really comes from that, that if you think that you have a business which is a going concern, it's not going to fall apart, but that they will have challenges with P&I, principal and interest, but if you can then refinance the loan so you give them some headroom on principal and interest, they should be able to see through a large part of the pain in these coming quarters.

Based on that, we still see some provisions, but my point is only that the provisions that we expect to see are not likely to be very much different from the total provisions we talked about this year. Our total this year will be ex of Swiber about $850 [million], and plus minus that's about what we might expect to see next year.

Sukrit Khatri: Okay, and just for the provision that you expect, would it be more on the GP side, or would it be more on the SP? Do you have any…?

Piyush Gupta: Well, it goes back to what I was saying. If we can identify specific names, we take SPs. Our policy has been that if we can't identify specific names but we're still concerned, then we just try to load up on the GP. So, if we can't attribute it to a particular name, then we just put it into a general reserve so it can come handy at a bad time.

Chng Sok Hui: So, I think you should note that going into 2018, the new IFRS 9 rules will be implemented in 2018, the MAS has not finalised the rules, but based on the simulations that we have run, our general provisions today are in excess of what is needed under IFRS 9. So, we'll continue to be conservative, but that's to give you an idea of the level of conservatism, because we have actually built up more than enough general provisions [required] under the new IFRS 9, whereas a lot of global players are saying they can't afford to put aside [the] additional provisions [needed]. So, that's just to context it.

Sukrit Khatri: Okay, understood, and one last question. This refers to slide 26 on the CFO deck. I see that there's a huge spike on the less than 90 days overdue. So, does this usually correspond with the retail side, or is this something else?

Piyush Gupta: No, I think the 13% to 25%, this is likely to do with that NPL we moved…

Chng Sok Hui: Yes, Swiber has moved into NPL.

Piyush Gupta: No, it's not Swiber. The weak name we moved into NPL this quarter.

Chng Sok Hui: It's the 25%, so it's the 90 days overdue.

Piyush Gupta: Less than 90 days overdue.

Chng Sok Hui: Yes, less than 90 days overdue.

Michael Sia: Sorry, were you referring to the 90 days overdue, or less than 90 days overdue?

Sukrit Khatri: Yes, less than 90 days overdue, actually.

Chng Sok Hui: Yes, so remember Swiber had no overdues as of second quarter, so Swiber has moved into overdue. So, basically that is the movement in the less than 90 days overdue category.

Sukrit Khatri: Understood. Thank you very much. No more from me.

Operator: Thank you. Our next question, Robert Kong from Citigroup. Please go ahead.

Robert Kong: Hi. Actually, several of my questions have been answered already, but I have just a couple of small ones left. The first one is on the cost side. I understand the full idea about the productivity and the benefits that are coming through digitisation, but a 5% q-on-q for 7% year-on-year [decline], it does look a little bit sudden. I just wanted to see if there's a bit more colour on such a sharp drop quarter-on-quarter.

And the second question is, apologies, I missed the first part of the call, so this question may have been asked already, but did you actually give a NIM guidance for 2017, and if there are further rate hikes, at what level do rising rates start to impact on asset quality in the broader market, particularly SMEs? Thank you.

Piyush Gupta: So, on the cost, the quarter-on-quarter is [lower] because the second quarter had some one-timers. We took a chunk of expenses for marketing, particularly for Digibank launch in India and some other marketing activities in the second quarter, and we didn't have to incur those [in the third quarter].

But on the whole, the cost reduction for the year has really been driven, one, by headcount. So, we've been able to shrink [underlying] headcount this year in our business by about a hundred people down. The actual [headcount] shows up as increased, but that's because we insourced some business, specifically we insourced some technology businesses because we found that we can do them much cheaper ourselves than the outsourcing rates we were paying, so that's also resulted in much improved cost dynamics, the insourcing of the tech businesses. All of that is flowing through our numbers.

Finally, on a quarter-on-quarter basis, as Sok Hui said, we had much lower bonus for this quarter, reflecting of course the overall performance of the business. That's why the delta between one quarter to the other, but I think the real story is not the quarter-on-quarter, the big shift is really that the underlying nature of our business is showing efficiency gains from all of the measures we've been undertaking.

I'd mentioned before that we thought the cost-income ratio would peak at the 45%, 46% range. It indeed did, and my own target was that we should be able to start driving cost-income ratio down by about a percentage point a year. Actually, we've been able to see some gains quicker than that, than we anticipated, and that's what's flowing through in our numbers. The second question you had was…

Unidentified Male Speaker 1: NIM versus asset quality.

Piyush Gupta: You know, it's kind of hard to give a projection for NIM, so we did say that we expected fourth-quarter NIM to be a few basis points below the third quarter. I think my own opinion is it could be four or five basis points lower than third quarter. If you look into next year, I think the NIM projection is really a function of principally the Fed call.

My sense if you see a Fed hike in December, and if you see what we think today is about a couple of rate hikes next year, then [at this stage] we see a reasonable proportion of that flowing into the Singapore rates. How much uplift we [eventually] get on NIM though for the full year is hard to call, so we'll get a better sense of it after December with a rate hike or not. Our base case is that we should be able to hold fourth-quarter NIM levels through next year, and then we see what happens with the Fed rate hikes.

Now, what happens if you end up with a 25 basis point lift in pricing on NIM in the Singapore market? I don't think it's that material in terms of credit quality. I think for the increase in rates to start materially impacting credit quality, you've got to start seeing rates at 1% or 2% higher, and I don't see that happening honestly.

Robert Kong: Okay, thank you very much.

Operator: Thank you. Our next question, Harsh Modi from JP Morgan. Please go ahead.

Harsh Modi: Hi, sorry. A couple of follow-ups, quick ones. First one, what is the capital consumption on the ANZ deal? Is it between five to ten basis points, at least based on my calculations? Second, are you seeing any further weakness in the collateral values of some of the offshore marine assets? And third, for refinanced loans which are done on commercial terms, could you give the quantum of those loans in the offshore and marine sector done in the last 12 and 18 months? Thanks.

Piyush Gupta: Capital.

Chng Sok Hui: Okay. So, on the capital for the ANZ transaction, we expect it to have an initial impact of about 30 basis points. It is a very small impact, but because the transaction will be completed over a one-year period, and the ROE of this business is high – basically the payback is within one to two years – so there should be no capital impact other than the very initial one-time when we take it into our books.

Piyush Gupta: So, capital was question one. Question two was collateral values. So, it is hard to say because we do collateral updates in a formal way for the whole portfolio periodically. We did the last one in June, as we told you. We haven't done a formal one [since], but the fact is that even the valuers, and I've talked to them, find it hard to put a value on the collateral at this point in time. I think it's safe to say if you wanted to make a sale in today's market, collateral value will have [to] come off very sharply.

In the few [weak] cases which I've gone and specifically looked at, collateral values have come off, but depending on the ship, in most of those cases we think we'll be able to recover a loan if we really had to sell the collateral. But you'd have to actually put it on the market to see how deep it is, what will people pay.

What I have been tracking is the secondary market transactions in the AHTS and production support PSV market. There have been some transactions – up until August [this year], for example, there were 47 vessels which got sold in AHTS and PSV. Last year full year, there were 62 vessels that happened in all of 2015, so on a run-date basis this year, the number of sales is about the number of sales last year.

If you look at the prices at which those vessels have been trading, they're not unreasonable. They've come off a bit, but they're not unreasonable. So then it goes back to, is there somebody who has a contract and they don't have a ship, then they're willing [to pay] the price to get a ship. And so it's certainly a case-by-case basis you've got to look at and see what you will get for the sale. On a [business-as-usual] basis, like I said, there is [a] market there [for] getting value, but we haven't done a stress test valuation any time more recently.

Your third question was what is the number of weak cases in that long tail. Like I said, we refinanced about 40% of that long tail in the last 12 months. So, if you take that long tail of about $1.3 billion, about $500 million of that is what we have refinanced over the last year or so. The rest of it we're still in discussions, so we might still refinance the additional amount of that, depending on how we feel about the viability of the business and the nature of the borrower and so on.

Harsh Modi: Got it. Thanks, Piyush.

Chng Sok Hui: Harsh, if your question is around whether there's a possibility that we treat as refinancing and don't classify as NPL, whereas other banks might do so, the answer is no, because we do actually check and compare notes with the other banks, so the terminology in terms of refinancing and restructuring is consistent.

Harsh Modi: Yes, okay. Thank you.

Operator: Thank you. Our next follow-up question, Kar Weng from HSBC. Please go ahead.

Loo Kar Weng: Hello? Hi. Sorry. I just wanted to ask a very quick question, a follow-up to Robert's question on margins. Your 2017 guidance, if I heard correctly, you were saying that you're expecting single-digit revenue growth and stable jaws, right? What's the underlying NIM assumption behind that? Is that based on higher margin assumptions or not?

Piyush Gupta: So, it depends. If we get flat margins to this year, then we'll probably get 4%-odd top line growth. If we get a margin lift of 25 to 50 basis points through these two hikes, then that revenue growth would be closer to 6%, 7%.

Loo Kar Weng: Okay, got it. Thank you.

Operator: Thank you. Our next question, Marcus Chua from Nomura. Please go ahead.

Marcus Chua: Good afternoon. Thank you for the call. I have two main questions, one on asset quality and another on DBS's growth expectations. On asset quality, specifically on the non-mortgage consumer book, there are multiple quarters of deterioration in the NPL ratio. With increasing unemployment and slower growth, what is your thought on the direction of this book, and can we expect a more significant deterioration as we enter 2017? The second question is on growth.

Piyush Gupta: I didn't follow the question.

Marcus Chua: Okay. I'll ask it again. With increasing unemployment and slower growth, what is your thought on the direction of this book, and can we expect a more significant deterioration in this book entering 2017? So, that's the first part. Second is on growth. In the media briefing, you mentioned that the bank is looking at mid- to single-digit growth. Can we have some colour on which industries and geographies are this growth intended for?

Piyush Gupta: So, on the mortgage, we currently see almost zero pressure on the portfolio, and our delinquencies are currently at historical lows. We're not seeing [any change in] 30-day, 90-day [past due loans, which are] very low. We've often pointed out that our own portfolio is actually performing even better than the market average. Based on credit bureau data, we are about 30, 40 basis points lower than the market average for 30 and 90 [days past due], and I think that in part also reflects the nature of our focus on owner-occupied and HDB properties.

Again, just to remind you, part of this is really because of the Singapore CPF situation. A large part of mortgage servicing happens from their [CPF] account, and since everybody has a CPF balance built in there, that creates a lot more resiliency in the mortgage market in Singapore than in many other countries.

Michael's just showing to me, if you look at [our] total 30 [days past due loans], it was 0.3% in the third quarter 2015, and it's actually fallen to 0.28% in the third quarter 2016. That has improved in the last year, not deteriorated, and so I just want to say…

Marcus Chua: I meant the non-mortgage, sorry, the non-mortgage consumer book.

Piyush Gupta: Oh, the non-mortgage consumer book. Okay, sorry, so I misunderstood you. So, on the non-mortgage consumer book, there is some increase in delinquencies, and a lot of it is driven by the government's effort to do the debt consolidation, [to reduce a borrower's overall unsecured credit limit across banks to] 24 times, 18 times [monthly income]. But honestly, I think it has been ahead of the curve by driving first of all the four-times [monthly income limit per bank] for the past several years, and then driving this 24 and now 18 times [overall] debt consolidation quite quickly.

They've been able to have the industry keep the total delinquencies and NPLs in the non-consumer loans quite tight. So, again, we've seen some pick-up, but it's not alarming, and we don't expect it to get to an alarming state by any means. What was the other question?

Marcus Chua: Oh, the second question is on the banks looking at…

Piyush Gupta: Oh, yes, where is the growth coming from. Actually, as I keep saying, if you think about it, you can see we're getting growth across multiple industries and multiple geographies. India and Indonesia are still growing. India is now growing 7.5%, Indonesia is growing 5%, so there's some demand from there. There is some demand from our clients in the region who are expanding outside the region, so some of our growth has been in Australia. Ever since we've opened a branch there, that has been good for us. Some of our growth is in the UK market. Now, these are Singapore and Hong Kong clients who are willing to do more business in those regions that we can intermediate, so we've done that.

Some of the growth has come from deals. There is more consolidation and refinancing, so we've been able to get some growth from there, and some of the growth has come from China's offshoring strategy, the One Belt, One Road. Some of the Chinese clients are going internationally. We can participate selectively in some of that business. So, it's quite diversified and broad-based.

Marcus Chua: Thank you. Thank you very much.

Operator: Thank you. Our next question, Danny Goh from Credit Suisse. Please go ahead.

Danny Goh: Hi, thanks for the call. A couple of questions from me. Firstly, I'd just like to clarify on the income that's coming from the ANZ acquisition. The $200 million that you referred to, is that a top-line or is that a bottom-line number, and if it's a bottom-line number, is that largely driven by cost synergies?

Piyush Gupta: No, that's a top-line number. Well, actually we reported two $200 millions. So, in the first instance, we should see a top-line impact of $200 million next year. So, in fact when the previous questioner asked about growth next year, all of the numbers we told you are ex the ANZ impact. If you add another $200 million-odd to the top line, that's between 1.5% to 2.5% of [additional] revenue pick-up from the ANZ transaction.

That number by 2018 should be in the $600 million range, $600 million because we're expecting some attrition, we lose some customers, lose some revenue. But we should be able to have about $600 million pick-up in the revenue line. We also referred to our $200 million bottom-line pick-up, but that is three years out.

Once we can bring over all the businesses by end of next year or early 2018, through 2018 we think we can start driving much of the cost synergy. For example, in the first instance, we think we are going to bring across about 30 branches. We're not bringing all the branches, but where we think the branches have good locations, better than ours, we're bringing them across, but in the course of 2018 then we're shutting down our branches of the same number, so we then are able to get some efficiency from that.

We're getting some efficiency from technology, a significant impact. All of that will flow through 2018, and so by the third year out, we think the bottom line impact of this transaction should be at least $200 million.

Danny Goh: Okay, got it. Another question related to asset quality. You mentioned in the slides that half of the smaller accounts [in oil and gas support services] are now showing signs of stress compared to one-third in the last quarter. How much of that has already been classified as NPLs? And also I was just wondering whether in terms of your watchlist, some of your competitors have said that basically they haven't seen a broadening of the number of names in their watchlist. Are you seeing a similar trend as well?

Piyush Gupta: No. In fact, the ones which I'm categorising as showing weakness are not in NPL, and we are not seeing a similar trend [as competitors] because we saw an increase in accounts showing weakness in this quarter, which came from two areas. One, there are some accounts which are very directly Swiber-linked. Those accounts were doing all right, but now because of the Swiber supply chain impact they are showing signs of stress.

The second is a couple of accounts who we think will have more difficult capital market access. They were well set to be able to get some either equity or capital market funding, but the markets are pretty much shut down post-Swiber, and as a consequence they are beginning to show some more signs of stress than they were showing in the second quarter.

Danny Goh: Right, and just two more very quick questions. One is just looking at the size of the oil and gas exposure, and you've reduced it by $3 billion, is that due to a repayment that is scheduled?

Piyush Gupta: No, that goes back to what I said, the trade business we do with the large oil-producing names and the large traders can go up and down. It's partly driven by our liquidity, partly driven by what's happening to the market. So, yes, technically they are repayments because the trade matures and we don't replace it.

Danny Goh: I see, and lastly on the $2.3 billion [in oil and gas support services] that's spread across the five accounts, is that an exposure which is evenly distributed among the five names?

Piyush Gupta: Yes, pretty evenly, plus minus $50 million-odd here or there.

Danny Goh: Okay, got it. Thank you very much.

Operator: Thank you. Our next question, Krishna from Jefferies. Please go ahead.

Krishna Guha: Yes, hi. Thank you, Piyush, for hosting this call. Most of it was answered, but just a couple of quick clarifications. On your specific provisions you gave a guidance of $850 million for next year, and what kind of assumption are you making on your coverage ratios for next year? That's the first question.

Second is on your employees, I think for the first time you are giving this insourcing number, about 700 employees from insourcing. I mean, is it they're on the same terms as your normal staff, and how should we think about this particular thing going forward?

And just one observation, if I look at the collateral number over the unsecured NPAs, that ratio is about 200% for DBS. If I remember, for your peers it is about 250% and 300%, so I was just wondering, if you can comment on that as to how should we think about collateralisation of your loan book, and also the valuation of your collaterals.

Piyush Gupta: Okay. On the first question with coverage ratio, our coverage ratio target is to try and be at 100% coverage against our total NPLs. That's why we bumped up our GPs. We could afford to bump that up to make sure we stayed at 100%. Depending on how operating performance is, if we can bump it up further along the way, we will do that, but the target is to try and stay at 100% and north.

The second question was insourcing. Actually, I'm not sure where you got the 700 number. We've insourced 300-odd people, but we will be insourcing a lot more. We've actually given an indication we're setting up or we have set up this large tech facility in Hyderabad. What we're doing is, a large part of the work that we have traditionally outsourced to external providers, people like IBM and Infosys and so on, we're now bringing into this facility.

It's a facility we've set up to do technology business. We think that as we go forward, one, the intellectual property around some of the stuff we're doing is quite useful to keep in-house, and second, we're finding that now that we've got our hands around how to run Agile and so on, doing this through an insourced basis is actually a lot more cost-efficient than the outsourcing arrangements that we had.

Some of that you can see in our cost-income ratios. Part of the big improvement that we get is also this, that we don't have to pay the overhead and the margins of the outsource providers, and we're bringing it and doing it in-house in our own facility. Actually, the agenda is to grow Hyderabad. It's at about 300, 400 people now. The intent is to grow that to 1,500 people by the end of next year. So, we'll see that the insourcing headcount will continue to increase, but costs will continue to reduce because this is just cheaper than doing it externally.

Chng Sok Hui: So, you should see the reduction in cost over time in the computerisation line. That's why we disclosed the staff numbers separately, because as these programs get developed, these are basically IT applications. They will be consistently treated per the current methodology for outsource providers. They will be capitalised and then amortised over time, because it's basically a software cost.

Piyush Gupta: And then the second, third… 200%.

Unidentified Male Speaker 1: Will the Hyderabad be on the same incomes as the bank employees?

Piyush Gupta: No. So, because like everybody else, when we set up the whole subsidiary arrangement, we benchmarked it to market, and so the overall cost of the technology thing is benchmarked to the market for technology, which obviously is different from the cost structure of the banking entity.

Krishna Guha: So, basically you are saving on the margins of, say, IBM or Infosys.

Chng Sok Hui: That's correct.

Piyush Gupta: Correct.

Krishna Guha: Okay, and if I'm just on that point, if I can ask to focus your gaze on your cost-to-income ratio for, say, 2018 or 2019, would you peg it at 40%, 41%? I mean, the cost-to-income ratio, say, three, four years down the line.

Piyush Gupta: So, our agenda, as we said from the beginning of this year, is that [with the cost-income ratio] having peaked at 45%, 46%, with efficiency and digitisation we should be able to drive [it] down by a percentage point every year. So, if we look out five years, our target is to get to 40% cost-income ratio. Like I said, we're getting closer to 43% now than 45%, and I think as we continue building forward from here, you will continue to see improvements in what we are doing.

Just as an aside, my view is if you have a completely digital bank, and we're seeing that in Digibank in India, you can actually run a cost-income ratio of much lower than that. So, my target, if we can digitise properly for a digital offering, is a cost-income ratio in the low 30s, not even in the 40s.

Anecdotally, we think that for the Digibank in India, our blueprint suggests that we can run with about 20 people what would normally take 350 people to run. Today, we're running it with about 75 people, so we're already running it with one-fourth the headcount of a normal bank, but over the next year or so we should be able to get it down to one-fourth of what we have today, and the reason for that is we have no branches, we have no call centre.

We're addressing 350,000 people's calls, 96% of that has been handled through artificial intelligence and a chat bot, and we have no branches. So, it's just a very different cost structure. When we drive the cost structure down, we can partly use it to compensate the customer, so we improve our offering to the customer in higher interest rate, but we can also use it to compensate our shareholder by just letting [the cost savings] drop to the bottom line.

Krishna Guha: Thank you very much, and on the final question now on the collateral to unsecured NPA, which is over 200% for you, and I remember UOB and OCBC is about, I think, 250% and 300% respectively, so again, not comparing with peers, but if you can give some colour on that, and what are your thoughts.

Chng Sok Hui: When you look at what is the meaning of this ratio, this is just saying specific provisions plus general provisions divided by NPLs less collateral. The portion that is already covered by collaterals, you remove it, and you have two times over, so actually it is a very conservative number. So, it is a function of the collateral that you have associated with these NPLs in the first place. A coverage ratio of 200% is actually very conservative.

Krishna Guha: Okay. Thank you very much.

Operator: Thank you. Our next question, Asheefa from CLSA. Please go ahead.

Asheefa Sarangi: Good afternoon. Just three quick ones from me, please. Firstly, what drove down the market risk weights in the third quarter? The second thing is, on the acquisitions, the 30 basis point negative impact to your CET1, does that assume some attrition on the $7 billion of risk weights that you're taking over? And the third question is on the PRC exposure, which was $28 billion last quarter, could you just give us an update, because I know obviously the trade loans have gone up by about $1 billion to $13 billion, but just wondering what the total PRC exposure is now. Thank you.

Piyush Gupta: PRC exposure. I think you have the data on it. So, the first question was on market risk weights. Is that the question?

Chng Sok Hui: So, we didn't really get your questions, so could you repeat your first question?

Asheefa Sarangi: Yes. What drove down the market risk weights in the quarter Is my first question.

Chng Sok Hui: Market risk weights. For market risk, we actually use a standardised approach, so we don't have something called a market risk weight. The market risk capital charge is computed based on the standardised approach. As you know, Singapore banks are not allowed to go on internal models for market risk. So, against the methodology that's specified under the standardised approach, which is more punitive, we would pick our market risk RWA charge. So, could you be more specific about your question, because it is not a risk weight question?

Asheefa Sarangi: Yes. So, the market risk assets have come down from $45 billion as of September of last year to $36 billion as of September of this year, and you've dropped another $2 billion in the quarter, and I'm just wondering if that's volatility.

Chng Sok Hui: So, that's just reduced exposure. So, it's just a function of the position sizes being reduced.

Asheefa Sarangi: Okay, thank you. That's very clear. The second question relates to the acquisition. So, on my back-of-the-envelope numbers, if I take the goodwill and I take the $7 billion of credit risk weights, I get an impact of 38 basis points from the transaction. You're guiding for roughly 30. I'm just wondering if the attrition number that you've given for revenue, if that's also partially built into the credit risk weights as well.

Chng Sok Hui: So, the portfolio has got mortgages. We have assumed basically a standardised approach, although we may actually get the benefit of using our own internal models approach for the mortgage portfolio in Singapore. So, all-in-all, we expect the overall capital charge to be $700 million to $800 million, which gives you an impact of 30 to 35 basis points impact on the CAR ratio, but as I mentioned earlier, because the transaction will be accretive very quickly, the impact disappears after a one- to two-year period.

Asheefa Sarangi: Okay. Thank you for that additional detail, and then lastly, on the China portfolio, last quarter it was $28 billion, split $12 billion trade, $16 billion nontrade. This quarter it's $13 billion for trade. Just wondering what the nontrade number is, the total portfolio.

Piyush Gupta: The non-trade number is flat.

Asheefa Sarangi: Flat. Thank you.

Michael Sia: Okay. So, thank you for joining us, and we'll call it a day here. Okay, thanks everybody.

Operator: Thank you. Ladies and gentlemen, this concludes today's conference call. Thank you for your participation. You may now disconnect.