

Bank Mandiri (BMRI JJ)

27 July 2016

Results Note

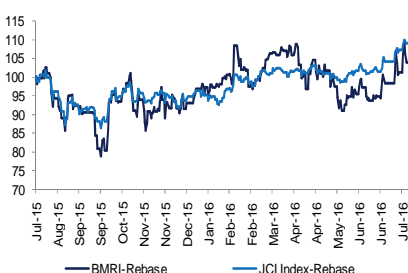
BUY (Unchanged)

Stock Data

Target price (Rp)	Rp12,000
Prior TP (Rp)	Rp10,850
Share price (Rp)	Rp9,850
Upside/downside (%)	+21.8
Shares outstanding (m)	23,333
Market cap. (US\$ m)	17,611
Free float (%)	40.0
Avg. 6m daily T/O (US\$ m)	18.4

Price Performance

	3M	6M	12M
Absolute (%)	2.8	3.4	2.3
Vs. JCI (%)	-5.0	-9.7	-6.4
52w high/low (Rp)	9,925 - 7,525		



Major Shareholders

Republic of Indonesia	60.0%
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Estimate Change; Vs. Consensus

	2016F	2017F
Latest EPS (Rp)	760	1,017
Vs. Prior EPS (%)	-6.6	0.0
Vs. Consensus (%)	-4.1	+6.4

Source: Bloomberg

Stephan Hasjim

PT Indo Premier Securities
stephan.hasjim@ipc.co.id
+62 21 5793 1168

Better visibility post loan review

- Net profit fell 29% to Rp7.1tn in 1H16 but weak 2Q was expected
- Ernst & Young loan review led to higher NPLs/credit cost guidance
- We expect this to improve visibility of earnings recovery next year
- Reiterate Buy; TP raised to Rp12,000 due to lower risk-free rate

Weak results. BMRI's profit of Rp7.1tn in 1H16 (-29% yoy) was expected as this was indicated by management post 1Q result. Core profit grew 14%, in line with our forecast, driven by 10% loan growth, better NIM of 5.96% (+45bps) and strong non-interest income. However, NPL ratio at 3.86% in 2Q (1Q: 3.21%) was higher than expected and led to higher credit cost guidance of 2.8-3.2% for FY16F (1H: 3.25%) while provisions/NPL coverage also declined to 113% (1Q: 132%). More importantly, we view management's more conservative NPL recognition policy as positive news as this should lead to better visibility of earnings recovery in the coming years on the back of the bank's normalising credit cost.

Comprehensive loan review. BMRI appointed Ernst & Young to conduct detailed review of the bank's entire commercial loans (29% of portfolio), which has seen worst asset quality deterioration in the past year. Based on this, management decided to be more conservative and front-load provisions to anticipate future problem loans. In turn, this led to downgrades of Rp7.8tn of loans into NPLs in 2Q (vs. Rp4.8tn in 1Q), of which 49.2%/15.7% of this amount came from commercial and corporate loans, respectively. Management is guiding for NPL ratio to remain elevated at 3.5-4.0% in 2H16 with a credit cost of 2.8-3.2% for FY16F.

Better earnings visibility. Although BMRI's NPL ratio and credit cost guidance for FY16F are higher than we expected, we view the bank's more conservative NPL recognition policy should lead to stronger visibility of earnings recovery in the coming years as its credit cost normalises. Although we lower our FY16F earnings by 6.6% due to our higher credit cost assumption of 300bps (previously 270bps), our FY17-18F forecasts are largely intact. We forecast strong earnings recovery in next two years, assuming its credit cost to fall to 216bps/179bps in FY17F/FY18F. We believe these assumptions are reasonable as they would still be well above BMRI's average credit cost of 106bps in 2009-2014.

Reiterate Buy. With our FY17-18F earnings intact, we raise our TP to Rp12,000 (from Rp10,850), largely due to lower cost of capital arising from a sharp fall in 10-yr yields to c.7.0% (from 8.8% at end 2015). Our GGM-derived target FY16F P/B of 1.77x assumes LT ROE of 15.2%, growth of 9% and cost of equity of 12.5%. Given our expectation for BMRI's NPLs peaking this year, its earnings to recover from next year and potential upside from ongoing tax amnesty program in Indonesia, we reiterate our Buy rating on the stock.

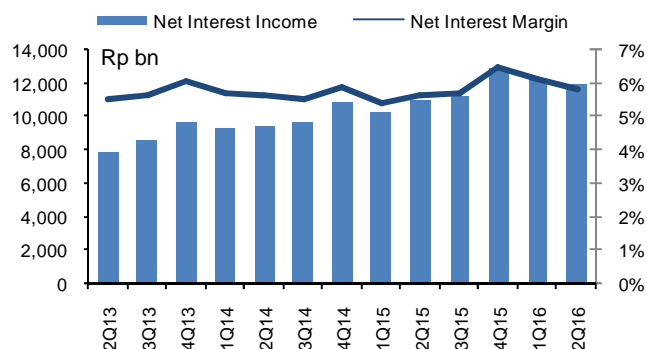
Year To 31 Dec	2014A	2015A	2016F	2017F	2018F
Operating income (RpBn)	54,275	63,706	70,012	76,838	85,927
PPOP (RpBn)	28,900	34,951	38,141	41,652	47,027
Net profit (RpBn)	19,872	20,335	17,725	23,721	28,513
Net profit growth (%)	9.2	2.3	(12.8)	33.8	20.2
FD EPS (Rp)	852	871	760	1,017	1,222
P/E (x)	11.6	11.3	13.0	9.7	8.1
P/B (x)	2.2	1.9	1.4	1.3	1.1
Dividend yield (%)	2.1	2.2	1.9	2.6	3.1
ROAA (%)	2.6	2.3	1.9	2.3	2.4
ROAE (%)	21.4	19.0	12.9	14.1	14.9

Source: BMRI, IndoPremier

Share Price Closing as of : 26-July-2016

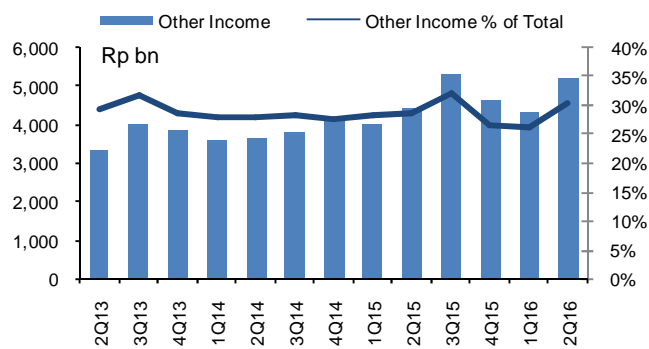
BMRI Results Note

Fig. 1: Net Interest Income (Rp bn) and NIMs (%)



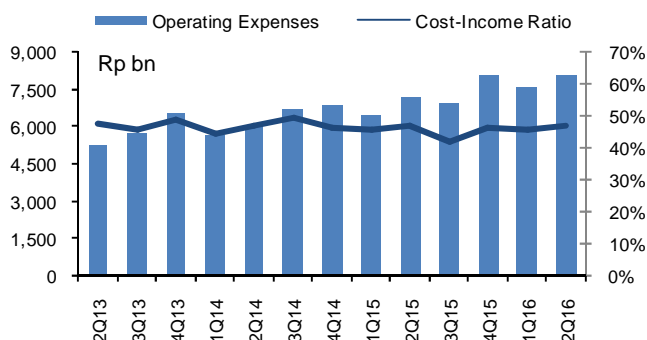
Source: Company, IndoPremier

Fig. 2: Non-Interest Income (Rp bn; % of Gross Income)



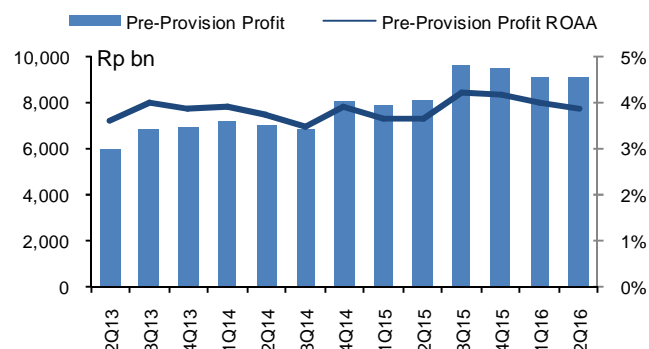
Source: Company, IndoPremier

Fig. 3: Operating Expense (Rp bn) and Cost/Income Ratio (%)



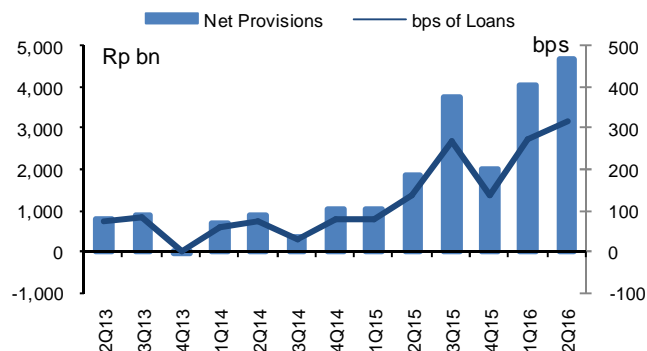
Source: Company, IndoPremier

Fig. 4: Pre-Provision Profit (Rp bn; % of Average Assets)



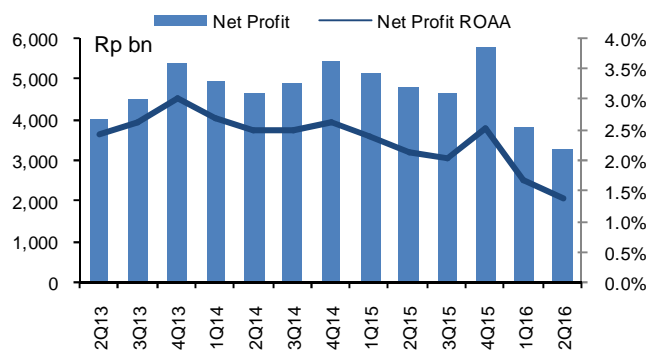
Source: Company, IndoPremier

Fig. 5: Net Loan Provisioning (Rp bn; bps of Average Loans)



Source: Company, IndoPremier

Fig. 6: Net Profit (Rp bn) and ROAA (%)



Source: Company, IndoPremier

1H16 results and earnings review

We lower our FY16F earnings forecast by 6.6% but keep our FY17F-18F forecasts unchanged on the back of our revised assumptions as follows: 1) we raise our NPL ratio forecast to 3.9% for FY16F (previously 3.5%) on the back of management revised guidance of 3.5-4.0%; 2) we raise our gross credit cost assumption to 300bps for FY16F (previously 270bps) to be more in line with revised guidance of 2.8-3.2% - on net credit cost basis (including recoveries), this translate to net credit cost assumption of 238bps for FY16F (previously 206bps); and 3) we lower our NIM forecast slightly to 5.90% (from 6.02%) in line with lower NIM of 5.79% in 2Q (1Q: 6.13%). Our forecast assumptions for FY17F-18F are largely unchanged.

Fig. 7: Results (Rp Bn)	1H16	1H15	% Y-Y	2Q16	1Q16	% Q-Q
Net Interest Income	24,244	21,200	14.4	11,912	12,331	-3.4
Fees & Commissions	5,482	5,026	9.1	2,951	2,531	16.6
Insurance & Other Incomes	2,636	2,336	12.9	1,449	1,187	22.0
Trading Income	1,426	1,074	32.7	806	620	30.1
Operating Income	33,788	29,636	14.0	17,119	16,669	2.7
Operating Expenses	-15,630	-13,705	14.0	-8,058	-7,572	6.4
Pre-Provision Profit	18,158	15,931	14.0	9,061	9,097	-0.4
Loan Provisions	-9,888	-3,996	147.5	-5,292	-4,596	15.1
Loan Recoveries	1,191	1,149	3.6	620	571	8.7
Operating Profit	9,461	13,084	-27.7	4,390	5,071	-13.4
Other Non Operating Items	-8	2	n.m	-3	-5	-34.7
Pre-Tax Profit	9,453	13,087	-27.8	4,386	5,066	-13.4
Tax	-1,951	-2,750	-29.1	-912	-1,039	-12.2
Minorities	-422	-412	2.4	-212	-210	0.6
Net Profit	7,080	9,924	-28.7	3,263	3,817	-14.5
Gross Loans	610,887	552,778	10.5	610,887	574,704	6.3
Customer Deposits	691,359	654,858	5.6	691,359	655,063	5.5
Non-Performing Loans (NPL)	23,580	13,433	75.5	23,580	18,140	30.0
Special Mention Loans	30,255	23,935	26.4	30,255	31,458	-3.8
Loan Loss Reserves (LLR)	26,576	18,497	43.7	26,576	23,927	11.1
Total Assets	971,444	914,075	6.3	971,444	906,739	7.1
Risk-Weighted Assets	691,101	631,796	9.4	691,101	643,643	7.4
Shareholders' Funds	144,809	107,237	35.0	144,809	116,014	24.8
BV Per Share	6,206	4,596	35.0	6,206	4,972	24.8

Source: BMRI, IndoPremier

Fig. 8: Key Ratios (%)	1H16	1H15	% Y-Y	2Q16	1Q16	% Q-Q
ROAA (annualized)	1.54	2.27	-32.3	1.39	1.68	-17.3
ROAE (annualized)	11.5	19.1	-39.6	10.0	13.1	-23.9
Net Interest Margin (bps)	596	551	8.2	579	613	-5.5
Net Credit Cost (bps)	326	139	134.0	355	297	19.4
Fee Inc/Operating Income	16.2	17.0	-4.3	17.2	15.2	13.6
Non Int Inc/Operating Income	28.2	28.5	-0.8	30.4	26.0	16.9
Op. Cost/ Operating Income	46.3	46.2	0.0	47.1	45.4	3.6
Loan-to-Deposit Ratio (LDR)	88.4	84.4	4.7	88.4	87.7	0.7
NPL/Loan Ratio	3.9	2.4	58.8	3.9	3.2	22.3
LLR/NPL Ratio	112.7	137.7	-18.2	112.7	131.9	-14.6
Tier-1 Capital Ratio	18.5	14.8	24.4	18.5	15.3	20.4
Total Capital Ratio	20.9	17.2	21.6	20.9	17.9	16.8

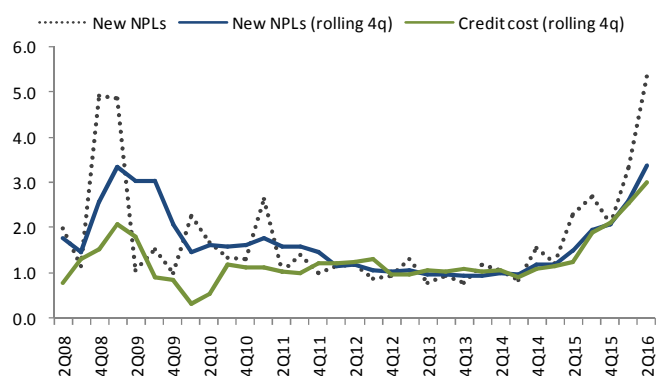
Source: BMRI, IndoPremier

New NPLs vs. Credit Cost forecasts

Fig. 9 shows the trend of BMRI's gross credit cost vs. new NPL formation on a rolling 4 quarter basis since 2008. The bank's new NPLs jumped to 5.35% of loans in 2Q16, which was above its previous peak new NPLs of 4.9% post the global financial crisis in 4Q08 and 1Q09 – this led to an annualised new NPL formation of 3.39% based on 4 quarter rolling basis. In comparison, the bank's new NPL formation was stable at around 1.0-1.2% p.a. during 2013-2014. The bank's asset quality worsening also led to a sharp rise in its gross credit cost (excluding loan recoveries) to 326bps of loans in 1H16 or an annualised rate of 300bps (on a 4 quarter rolling basis), from 110bps during 2013-2014 period.

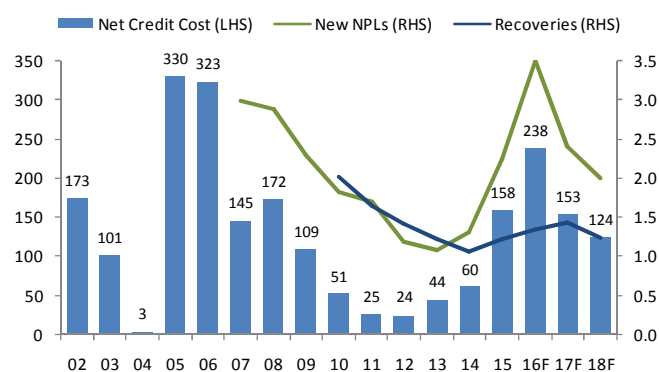
Meanwhile, we show in Fig. 10 our net credit cost assumption for BMRI (which is credit cost net of loan recoveries), which we expect to rise to 238bps in FY16F (from 158bps in FY15) before improving to 153bps in FY17F and 124bps in FY18F. Our assumption of declining net credit cost in the next two years underpins our forecast for BMRI's earnings growth recovery in the coming years.

Fig. 9: Quarterly Gross Credit Cost vs. New NPLs (% loans)



Source: Company data, IndoPremier

Fig. 10: Yearly Net Credit Cost vs. New NPLs (bps of loans)



Source: Company data, IndoPremier forecasts

BMRI Results Note

Year To 31 Dec (RpBn)	2014A	2015A	2016F	2017F	2018F
Income Statement					
Interest income	62,638	71,570	72,422	78,287	86,904
Interest expense	(23,506)	(26,207)	(22,712)	(23,332)	(25,806)
Net interest income	39,132	45,363	49,710	54,954	61,098
Fees and commissions	9,132	10,015	11,251	12,938	14,879
Trading income	1,969	2,495	3,100	2,400	2,750
Other operating income	4,042	5,833	5,951	6,546	7,200
Total operating income	54,275	63,706	70,012	76,838	85,927
Personnel expenses	(10,848)	(12,377)	(14,109)	(15,803)	(17,699)
G&A expenses	(11,448)	(12,800)	(14,080)	(15,488)	(17,037)
Other operating expenses	(3,078)	(3,578)	(3,681)	(3,896)	(4,165)
Pre-provision operating profit	28,900	34,951	38,141	41,652	47,027
Provisions	(5,529)	(12,043)	(19,361)	(15,776)	(15,010)
Loan recovery income	2,607	3,430	4,500	5,000	5,000
Operating profit	25,978	26,339	23,280	30,876	37,017
Non-operating profit	30	30	0	0	0
Exceptional items	0	0	0	0	0
Pre-tax profit	26,008	26,369	23,280	30,876	37,017
Income tax	(5,353)	(5,217)	(4,656)	(6,175)	(7,403)
Minority interests	(783)	(817)	(899)	(980)	(1,100)
Reported net profit	19,872	20,335	17,725	23,721	28,513
Balance Sheet					
Cash	20,705	25,109	24,204	26,682	29,243
Current account with BI	50,599	56,314	49,011	53,948	59,120
Placements at BI & other banks	70,101	47,473	59,063	62,016	65,116
Short-term investments	60,210	44,318	57,000	52,200	47,880
Government bonds	86,154	103,869	98,607	98,607	98,607
Gross loans	529,974	595,458	655,003	753,254	866,242
Loan provisions	(17,919)	(22,558)	(33,543)	(38,719)	(43,229)
Other assets	55,217	60,080	89,596	97,752	106,867
Total Assets	855,040	910,063	998,940	1,105,739	1,229,845
Customer deposits	636,382	676,388	703,244	775,904	851,811
Deposits from other banks	17,774	12,954	15,145	17,196	19,533
Securities and borrowings	36,096	44,764	46,383	51,021	56,123
Other liabilities	59,943	56,466	73,229	81,122	93,075
Total Liabilities	750,195	790,572	838,000	925,243	1,020,543
Share capital	28,983	28,983	28,983	28,983	28,983
Reserves and others	(368)	(1,137)	27,428	27,428	27,428
Retained earnings	74,043	89,225	101,866	121,156	149,669
Shareholders' equity	102,658	117,070	158,277	177,566	206,079
Minority interest	2,187	2,422	2,664	2,930	3,223
Total Liabilities & Equity	855,040	910,064	998,940	1,105,739	1,229,845

Source: BMRI, IndoPremier

BMRI Results Note

Year To 31 Dec	2014A	2015A	2016F	2017F	2018F
Growth Ratios (% yoy)					
Gross loans	12.3	12.4	10.0	15.0	15.0
Total assets	16.6	6.4	9.8	10.7	11.2
Customer deposits	14.4	6.3	4.0	10.3	9.8
Net interest income	15.7	15.9	9.6	10.5	11.2
Non-interest income	7.2	21.1	10.7	7.8	13.5
Total operating income	10.3	1.4	(11.6)	32.6	19.9
Operating expense	12.6	13.3	10.8	10.4	10.6
PPOP	13.8	20.9	9.1	9.2	12.9
Net profit	9.2	2.3	(12.8)	33.8	20.2
Profitability Ratios					
ROAA (%)	2.58	2.28	1.86	2.25	2.44
ROAE (%)	21.4	19.0	12.9	14.1	14.9
NIM (%)	5.68	5.80	5.90	5.93	5.92
Credit cost (bps)	59.9	157.8	237.7	153.0	123.6
Cost/income (%)	46.8	45.1	45.5	45.8	45.3
LDR (%)	83.3	88.0	93.1	97.1	101.7
CAR (%)	16.1	18.0	21.7	21.0	20.7
NPL ratio (%)	2.2	2.6	3.9	3.7	3.3
Provisions/NPL (%)	156.7	143.9	131.3	140.6	149.6

Source: BMRI, IndoPremier

Head Office**PT INDO PREMIER SECURITIES**

Wisma GKBI 7/F Suite 718

Jl. Jend. Sudirman No.28

Jakarta 10210 - Indonesia

p +62.21.5793.1168

f +62.21.5793.1167

INVESTMENT RATINGS

BUY : Expected total return of 10% or more within a 12-month period
HOLD : Expected total return between -10% and 10% within a 12-month period
SELL : Expected total return of -10% or worse within a 12-month period

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