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Auswide Bank (ABA)

Good progress in 2017

Recommendation
Buy (Hold)
Price
\$5.47
Target (12 months)
\$5.95 (previously \$5.85)

GICS Sector
Banks

Expected Return

Capital growth	8.8%
Dividend yield	6.0%
Total expected return	14.8%

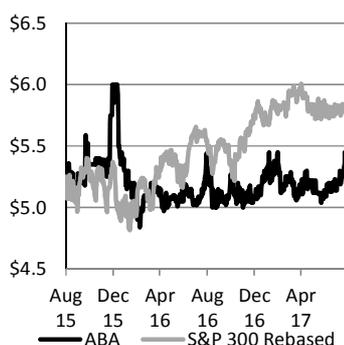
Company Data & Ratios

Enterprise value	n/m
Market cap	\$223m
Issued capital	41m
Free float	100%
Avg. daily val. (52wk)	\$120,764
12 month price range	\$4.99 - \$5.55

Price Performance

	(1m)	(3m)	(12m)
Price (A\$)	5.15	5.20	5.20
Absolute (%)	5.63	4.62	4.62
Rel market (%)	4.62	5.00	0.76

Absolute Price



SOURCE: IRESS

\$15.6m underlying NPAT, 17cps final dividend

Following a strong 1H17, underlying NPAT (excluding one-off acquisition-related professional fees and stamp duty) of \$15.6m (BP \$15.3m) was up 11% on a pcg basis. This was driven by volume growth (loan book +4% pcg to \$2.8bn), higher banking fees and commissions (volume-related) and ongoing cost discipline (costs down by 3% pcg to \$45.0m mainly in occupancy and general overheads) that more than offset 6bp lower NIM to 1.90% (BP 1.92%) largely due to competition on the asset side (average loan yield -35bp and average interest earning asset yield -37bp vs. average retail deposit cost -30bp and average interest bearing liability cost -31bp) and liquidity drag (including 1bp lower free fund effect), in addition to an immaterial uptick in the BDD charge (although arrears continue to be low with 90+ days loans at 39bp of GLA).

As a result, underlying ROE improved by 2bp to 7.2% and likewise the underlying cost-to-income ratio by ~4% to 66% (positive underlying "Jaws"), reported falling by ~7% to 67%. The final dividend was 17cps, fully franked (BP 16cps) resulting in an 80% payout ratio for the full year. A fully underwritten DRP has been reinstated for the final dividend at a 2.5% discount and is expected to raise at least \$6.9m in capital (that should increase Tier 1 capital to ~12.4% in 2018). 2017 Tier 1 capital ratio was 12.2% and total capital ratio was 14.6%.

The outlook is for: (1) slower home loan growth in 1H18 followed by a stronger 2H18 (2018 total loan growth forecast 4-5%); and (2) further reduction in the cost-to-income ratio (BP forecast -1% to 66%). We also expect NIM to increase by ~4bp to 1.94% in 2018 as the benefit of recent residential mortgage rate rises begins to kick in, although this will start to decrease as competition in the owner-occupied heats up again.

Price target increased to \$5.95, Buy rating reinstated

Solid progress has been made in strengthening revenues and managing costs, and we increase the price target by ~2% to \$5.95 that also reflects some DCF time creep and improving ROE. The Buy rating is reinstated based on an expected TSR of ~15%.

Earnings Forecast

Year end 30 June	2017	2018e	2019e	2020e
NPAT (reported) (A\$m)	15.1	16.9	18.2	19.5
NPAT underlying (A\$m)	15.6	16.9	18.2	19.5
EPS underlying (A¢)	39	41	43	46
EPS underlying growth (%)	3%	5%	7%	7%
PER (x)	14.2	13.5	12.6	11.8
P/Book (x)	1.0	0.9	0.9	0.9
P/NTA (x)	1.3	1.3	1.2	1.2
Dividend (A¢)	31	33	35	37
Yield (%)	5.6%	6.0%	6.4%	6.7%
ROE (%)	7.2%	7.4%	7.8%	8.2%
NIM (%)	1.90%	1.94%	1.93%	1.92%
Franking (%)	100.0%	100.0%	100.0%	100.0%

SOURCE: BELL POTTER SECURITIES ESTIMATES

Auswide Bank

Company description

ABA, formerly Wide Bay Australia Ltd, is Australia's 10th and QLD's 3rd listed bank. The QLD-based bank has a national omni-channel reach through its QLD branches, a national ATM and Bank@Post distribution network, and online and digital channels via strategic relationships such as mortgage brokers. The bank provides an extensive range of personal and business banking products and services issued directly or in partnership with leading national service providers.

Board/Management

(1) Professor John Humphrey (Chairman) – Former Senior Partner, Mallesons Stephen Jacques; (2) Martin Barrett (Managing Director); (3) Bill Schafer (Chief Financial Officer); (4) Craig Lonergan (Chief Risk Officer); (5) Steve Caville (Chief Information Officer).

Investment strategy

This is largely based on ABA as a challenger regional bank in Central QLD.

Valuation

The price target reflects a blended valuation comprising the company's DCF value (\$5.86 incorporating 10.0% cost of equity and 10.0% target Tier 1 requirement, 30% weighting), dividend yield valuation (\$5.95 based on 5.5% cap rate, 30% weighting), PB valuation (\$5.47 based on long term ROE of close to 9-10%, 20% weighting) and takeover valuation of \$6.56 (20% premium over last closing price, 20% weighting).

SWOT analysis

Strengths

Experienced management; strong service culture and brand; deep understanding of the customer base and the nuts and bolts of regional/community banking; irreplaceable branch network; IT capabilities; and presence in fast growing banking catchment areas.

Weaknesses

Sub-scale and heavily reliant on regional lending pickup; and lack of revenue and regional diversification.

Opportunities

SME/business banking initiatives; credit growth based on QLD rebuilding opportunities; efficiency gains through streamlining systems and processes; and M&A opportunities – e.g. tie up with other sub-scale building societies and credit unions.

Threats

Macroeconomic factors (such as slowing credit growth) and increased competition specifically from SUN, BEN, BOQ and any of the majors on the domestic front (e.g. in retail and wholesale banking and wealth management).

Table 1 – Financial summary

Auswide Bank						Share Price (A\$)					5.47
As at	28-Aug-17					Market Cap (A\$M)					223
	46.4	45.0									
PROFIT AND LOSS						VALUATION DATA					
Y/e June 30 (\$m)	2016	2017	2018e	2019e	2020e	Y/e June 30	2016	2017	2018e	2019e	2020e
Net interest income	53.9	57.5	61.6	64.4	67.4	NPAT (normalised) (\$m)	14.0	15.6	16.9	18.2	19.5
Fees and commissions	9.1	10.2	11.1	11.7	12.3	EPS (statutory basis) (cps)	31	37	41	43	46
Total banking income	63.0	67.7	72.7	76.2	79.7	- Growth	-14%	20%	9%	7%	7%
Premium revenue (MRM)	0.0	0.0	0.0	0.0	0.0	EPS (underlying basis) (cps)	37	39	41	43	46
Share of profit of FTSP	0.0	0.0	0.0	0.0	0.0	- Growth	1%	3%	5%	7%	7%
Other revenue	0.0	0.0	0.0	0.0	0.0	P / E ratio (times)	14.6	14.2	13.5	12.6	11.8
Sign up payment	0.0	0.0	0.0	0.0	0.0	P / Book ratio (times)	1.0	1.0	0.9	0.9	0.9
Total operating income	63.0	67.7	72.7	76.2	79.7	P / NTA ratio (times)	1.3	1.3	1.3	1.2	1.2
Fees and commissions	-9.0	-9.7	-11.1	-11.7	-12.3	Net DPS (cps)	30	31	33	35	37
SAW	-19.0	-19.2	-19.6	-20.2	-20.8	Yield	5.4%	5.6%	6.0%	6.4%	6.7%
Depreciation expense	-1.7	-1.9	-2.0	-2.1	-2.1	Franking	100%	100%	100%	100%	100%
Amortisation expense (assume acquisition costs of \$2,038,922)	-0.4	-0.8	-1.7	-1.7	-1.7	Payout (cash basis)	79%	80%	81%	80%	79%
G&A expenses	-16.3	-13.3	-13.2	-13.5	-13.7	CAPITAL ADEQUACY					
Underwriting expenses	0.0	0.0	0.0	0.0	0.0	Y/e June 30	2016	2017	2018e	2019e	2020e
Impairment expenses	0.0	0.0	0.0	0.0	0.0	Risk weighted assets (\$m)	1,262.9	1,276.1	1,340.1	1,407.5	1,478.4
Bad and doubtful debts expense	0.6	-1.0	-1.3	-1.4	-1.5	Average risk weight	43%	41%	41%	41%	41%
Net profit before income tax	17.1	21.7	23.8	25.6	27.4	Tier 1 ratio	12.1%	12.2%	12.4%	12.0%	11.7%
Corporate tax expense	-5.8	-6.7	-7.1	-7.7	-8.2	CET1 capital ratio	12.1%	12.2%	12.4%	12.0%	11.7%
Minority interests & other	0.3	0.1	0.3	0.3	0.3	Total capital ratio	14.3%	14.6%	14.6%	14.2%	13.8%
NPAT (statutory basis)	11.7	15.1	16.9	18.2	19.5	Equity ratio	7.1%	6.8%	6.8%	6.6%	6.4%
Adjustments						PROFITABILITY RATIOS					
- Sign up payment	0.0	0.0	0.0	0.0	0.0	Y/e June 30	2016	2017	2018e	2019e	2020e
- Impairment expenses/one-offs	2.3	0.5	0.0	0.0	0.0	Return on assets (underlying)	0.5%	0.5%	0.5%	0.5%	0.5%
- Amortisation expense	0.0	0.0	0.0	0.0	0.0	Return on equity (underlying)	6.9%	7.2%	7.4%	7.8%	8.2%
NPAT (underlying basis)	14.0	15.6	16.9	18.2	19.5	Leverage ratio	5.1%	4.8%	4.9%	4.8%	4.6%
CASHFLOW						Net interest margin	1.96%	1.90%	1.94%	1.93%	1.92%
Y/e June 30 (\$m)	2016	2017	2018e	2019e	2020e	Cost / income ratio	74%	67%	66%	65%	64%
NPAT (statutory basis)	11.7	15.1	16.9	18.2	19.5	Cost / average assets	1.57%	1.41%	1.39%	1.37%	1.35%
Increase in loans	-336.3	-106.8	-130.2	-136.3	-142.7	Growth in operating income	3%	8%	7%	5%	5%
Increase in other assets	1.4	-51.2	-25.3	-27.4	-29.6	Growth in operating expenses	12%	-3%	6%	3%	3%
Capital expenditure	2.4	0.9	-0.4	-0.5	-0.5	Jaws	-9%	11%	2%	2%	1%
Investing cashflow	-332.5	-157.1	-156.0	-164.2	-172.8	Effective tax rate	34%	31%	30%	30%	30%
Increase in deposits & borrowings	331.8	120.7	138.3	146.6	155.4	ASSET QUALITY					
Increase in other liabilities	7.3	89.4	7.0	13.6	13.0	Y/e June 30	2016	2017	2018e	2019e	2020e
Equity raised	16.0	2.1	6.9	0.0	0.0	Impairment expense / GLA	-0.02%	0.04%	0.04%	0.05%	0.05%
Other	-18.1	-18.0	-13.1	-14.2	-15.0	Impairment expense / RWA	-0.04%	0.08%	0.10%	0.10%	0.10%
Financing cashflow	337.1	194.2	139.1	146.0	153.4	Total provisions + GRCL (\$m)	5.0	6.7	7.2	7.7	8.2
Net change in cash	16.3	52.3	0.0	0.0	0.0	Total provisions + GRCL / RWA	0.40%	0.53%	0.53%	0.55%	0.56%
Cash at end of period	67.8	120.1	120.1	120.1	120.1	Total provisions + GRCL / loans	0.19%	0.24%	0.25%	0.25%	0.26%
BALANCE SHEET						Indiv ass prov / gross imp assets	125%	134%	134%	134%	134%
Y/e June 30 (\$m)	2016	2017	2018e	2019e	2020e	IBL / IEA	97%	99%	98%	98%	98%
Cash and liquid assets	67.8	120.1	120.1	120.1	120.1	INTERIMS					
Divisional gross loans	2,671.5	2,777.5	2,908.1	3,044.9	3,188.0	2H15	1H16	2H16	1H17	2H17	
Provisions	-5.0	-4.3	-4.7	-5.0	-5.5	Net interest income	25.3	26.5	27.4	28.3	29.2
Other gross loans / inter div.	0.0	0.0	0.0	0.0	0.0	Fees and commissions	4.2	4.9	4.2	4.6	5.6
Other IEA	247.1	310.4	335.8	363.2	392.8	Total banking income	29.6	31.5	31.5	32.9	34.8
Intangibles	49.1	56.9	56.9	56.9	56.9	Premium revenue (MRM)	0.0	0.0	0.0	0.0	0.0
PP&E	15.5	14.6	15.0	15.5	16.0	Share of profit of FTSP	0.0	0.0	0.0	0.0	0.0
Insurance assets	0.0	0.0	0.0	0.0	0.0	Other revenue	1.0	0.0	0.0	0.0	0.0
Other assets	26.9	14.7	14.7	14.7	14.7	Sign up payment	0.0	0.0	0.0	0.0	0.0
Total assets	3,072.8	3,290.0	3,446.0	3,610.2	3,783.0	Total operating income	30.6	31.5	31.5	32.9	34.8
Divisional deposits	2,183.9	2,304.6	2,442.9	2,589.5	2,744.8	Fees and commissions	-6.0	-2.8	-6.2	-3.1	-6.6
Other borrowings	641.8	736.0	743.0	756.6	769.6	SAW	-7.4	-8.5	-10.5	-8.5	-10.7
Other liabilities	30.4	25.6	25.6	25.6	25.6	Depreciation expense	-0.9	-0.9	-0.8	-0.9	-1.0
Total liabilities	2,856.2	3,066.3	3,211.5	3,371.7	3,540.1	Amortisation expense (assume acquisition costs of \$2,038,922)	0.0	0.0	-0.4	0.0	-0.8
Ordinary share capital	182.6	184.8	191.7	191.7	191.7	G&A expenses	-6.5	-11.5	-4.8	-9.4	-3.9
Other equity instruments	0.0	0.0	0.0	0.0	0.0	Underwriting expenses	-0.1	0.0	0.0	0.0	0.0
Reserves	13.4	11.6	11.6	11.6	11.6	Impairment expenses	0.0	0.0	0.0	0.0	0.0
GRCL	0.0	2.4	2.5	2.6	2.8	Bad and doubtful debts expense	0.0	0.8	-0.3	-0.4	-0.6
Retained profits	20.7	23.7	27.4	31.3	35.6	Net profit before income tax	9.7	8.7	8.5	10.6	11.1
Minority interests	0.0	1.3	1.3	1.3	1.3	Corporate tax expense	-2.8	-2.6	-3.2	-3.3	-3.4
Total shareholders' equity	216.7	223.7	234.5	238.5	242.9	Minority interests & other	0.0	0.0	0.3	0.0	0.1
Total sh. equity & liabs.	3,072.8	3,290.0	3,446.0	3,610.2	3,783.0	NPAT (statutory basis)	6.9	6.1	5.6	7.3	7.8
WANOS - statutory (m)	37.5	40.6	41.7	42.0	42.0	Adjustments	0.0	0.0	0.0	0.0	0.0
WANOS - normalised (m)	37.5	40.6	41.7	42.0	42.0	- Sign up payment	0.0	0.0	0.0	0.0	0.0
						- Impairment expenses/one-offs	0.2	0.7	1.6	0.0	0.5
						- Amortisation expense	0.0	0.0	0.0	0.0	0.0
						NPAT (underlying basis)	7.2	6.8	7.3	7.3	8.3

SOURCE: BELL POTTER SECURITIES ESTIMATES

Recommendation structure

Buy: Expect >15% total return on a 12 month view. For stocks regarded as 'Speculative' a return of >30% is expected.

Hold: Expect total return between -5% and 15% on a 12 month view

Sell: Expect <-5% total return on a 12 month view

Speculative Investments are either start-up enterprises with nil or only prospective operations or recently commenced operations with only forecast cash flows, or companies that have commenced operations or have been in operation for some time but have only forecast cash flows and/or a stressed balance sheet.

Such investments may carry an exceptionally high level of capital risk and volatility of returns.

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TS Lim owns 2,431 shares in ABA.

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