Deutsche Bank
Markets Research

Rating
Sell

Asia
Hong Kong

Banking / Finance
Banks

Company
Standard Chartered

Reuters	Bloomberg	Exchange	Ticker
2888.HK	2888 HK	HKG	2888

Date
5 March 2015

Results

Price at 4 Mar 2015 (HKD)	116.40
Price target - 12mth (HKD)	101.00
52-week range (HKD)	174.90 - 103.10
HANG SENG INDEX	24,465

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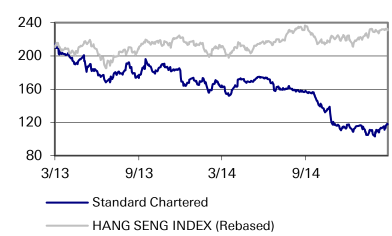
FY14 results: While we're waiting

Key changes

Price target	102.00 to 101.00	↓	-1.0%
Net profit (FYE)	2,936.1 to 2,734.1	↓	-6.9%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	7.5	-0.7	-28.4
HANG SENG INDEX	-0.9	2.7	8.0

Source: Deutsche Bank

Results 1% ahead, weak income outlook drives 6-7% downgrades

FY14 underlying PBT was 1% below DB and 6% below consensus driven by larger non-loan impairment charges. CRDIV CT1 at 10.7% was 20bps ahead of consensus driven by 4% lower RWAs: Deleveraging and de-risking is under way to pay the flat dividend and reposition the business. Near term though this drives a much weaker revenue outlook than we had allowed for, driving 6-7% EPS downgrades and reduction in our TP to HK$101. We retain our Sell on the substantial weakness we expect in forecast earnings as the business is repositioned post the arrival of new CEO Bill Winters.

More fundamental change required

Our February report – *Change doesn't come cheap* – analysed SC's product groups and key markets. We concluded that to restore the bank to the 15% ROE it needs for the model to work a substantial job of re-orienting balance sheet capital allocation was required. We advocated a capital increase, restructuring and loan loss charges, and narrowing of the footprint to reduce retail coverage in particular. Our work confirmed that SC's competitive advantage resides in Transaction Banking, Financial Markets and a small number of retail markets. Today's results do not dissuade us from these views.

Small steps in the right direction

In fact changes made by management in 2H14 in response to a weakening environment are in the direction we recommend but at a pace constrained by taught capital and succession issues. We think shareholder value is best rebuilt by grasping the nettle early and accelerating change under the new CEO. Meanwhile steps taken so far are sensible but not cheap – on actions taken already we've had to substantially cut our income estimates.

4-7% cuts to forecast EPS, TP to HK$101, Sell

The weaker outlook for revenues drives a 4-7% reduction in our adjusted EPS estimates. This leaves StanChart trading 12.2x 2016 EPS, 1.0x TNAV for an 7% ROTE. Though the dividend was held flat at FY14 we expect a rebasing this year to reduce the forward yield to around 2%. Lower earnings estimates contribute to a reduction in our SOTP-derived target price to HK$101 from HK$102. With substantial downside from current levels, retain Sell.

Key upside risks are much stronger-than-forecast capital formation, a bid for SC, or significant improvement in EM growth and commodity price prospects.

Forecasts And Ratios

Year End Dec 31	2013A	2014A	2015E	2016E
EPS (USD)	1.23	1.02	1.02	1.23
EPS growth (%)	-34.5	-17.1	-0.6	21.6
PER (x)	18.1	14.7	14.8	12.2
Yield (net) (%)	3.5	5.7	1.8	2.2
ROE (%)	6.7	5.5	5.5	6.7

Source: Deutsche Bank estimates, company data

Model updated:05 March 2015

Running the numbers

Asia

Hong Kong

Banks

Standard Chartered

Reuters: 2888.HK — Bloomberg: 2888 HK

Sell

Price (4 Mar 15)	HKD 116.40
Target Price	HKD 101.00
52 Week range	HKD 103.10 - 174.90
Market Cap (m)	HKDm 338,881
	USDm 43,698

Company Profile

Standard Chartered plc is an international banking group operating principally in Asia, Africa, Latin America and the Middle East. The Company offers its products and services in the personal, consumer, corporate, institutional and treasury areas, to customers in more than 50 countries. Standard Chartered is organised into three customer groups (Corporate & Institutional Clients, Commercial & Private Banking Clients and Retail Customers), supported by five product groups (Corporate Finance, Financial Markets, Transaction Banking, Wealth Management and Retail Products)

Fiscal year end 31-Dec	2011	2012	2013	2014	2015E	2016E
Data Per Share						
EPS (stated)(USD)	2.01	1.88	1.23	1.02	1.02	1.23
EPS (DB) (USD)	2.03	2.13	1.66	1.51	1.07	1.29
Growth Rate - EPS (DB) (%)	2.3	-6.3	-34.5	-17.1	-0.6	21.6
DPS (USD)	0.76	0.84	0.86	0.86	0.27	0.32
BVPS (stated) (USD)	16.45	17.36	18.40	19.52	na	na
Tang. NAV p. sh. (USD)	13.49	15.15	15.94	16.68	15.98	16.88
Market Capitalisation	52,032	60,970	54,258	37,121	43,698	43,698
Shares in issue	2,396	2,421	2,447	2,473	2,707	2,963
Valuation Ratios & Profitability Measures						
P/E (stated)	10.9	13.4	18.1	14.7	14.8	12.2
P/E (DB)	10.8	11.9	13.5	9.9	14.0	11.6
P/B (stated)	1.3	1.5	1.2	0.8	na	na
P/Tangible equity (DB)	1.6	1.7	1.4	0.9	0.9	0.9
ROE(stated)(%)	12.4	10.8	6.7	5.5	5.5	6.7
ROTE (tangible equity) (%)	15.5	15.0	10.8	9.3	6.6	7.9
ROIC (invested capital) (%)	12.5	12.2	9.0	8.1	5.8	7.0
Dividend yield(%)	3.1	3.6	3.5	5.7	1.8	2.2
Dividend cover(x)	2.6	2.2	1.4	1.2	3.8	3.8
Profit & Loss (USDm)						
Net interest revenue	10,153	10,781	11,156	11,003	10,668	11,065
Non interest income	7,484	7,788	7,621	7,331	6,866	7,300
Commissions	4,046	4,121	4,101	4,179	4,020	4,317
Trading Revenue	2,645	2,739	2,514	1,896	1,746	1,824
Other revenue	793	928	1,006	1,256	1,100	1,159
Total revenue	17,637	18,569	18,777	18,334	17,534	18,365
Total Operating Costs	9,590	10,286	10,815	11,753	10,191	10,398
Employee Costs	6,630	6,492	6,570	6,788	6,709	6,822
Other costs	2,960	3,794	4,245	4,965	3,482	3,576
Pre-Provision profit/(loss)	7,973	8,101	8,865	7,494	7,182	7,773
Bad debt expense	1,020	1,457	1,617	2,141	2,718	2,325
Operating Profit	7,027	6,826	6,345	4,440	4,625	5,642
Pre-tax associates	0	0	0	0	0	0
Pre-tax profit	7,027	6,826	6,345	4,440	4,625	5,642
Tax	1,842	1,866	1,864	1,530	1,125	1,318
Other post tax items	-438	-453	-1,492	-398	-766	-685
Stated net profit	4,747	4,507	2,989	2,512	2,734	3,639
Goodwill	253	254	281	205	213	222
Extraordinary & Other items	-146	397	783	1,018	-54	-35
Bad Debt Provisioning	0	0	0	0	0	0
Investment reval, cap gains / losses	0	0	0	0	0	0
DB adj. core earnings	4,854	5,158	4,053	3,735	2,893	3,825
Key Balance Sheet Items (USDm) & Capital Ratios						
Risk-weighted assets	270,510	301,861	322,251	341,648	362,147	383,876
Interest-earning assets	465,035	504,733	550,196	573,376	569,558	571,469
Customer Loans	272,538	289,607	296,711	288,599	285,068	292,395
Total Deposits	351,819	385,117	390,971	414,189	425,962	439,479
Stated Shareholder Equity	39,220	43,867	44,752	46,432	52,676	55,509
Equals: Tangible Equity	32,159	36,555	38,682	41,242	46,536	50,379
Tier 1 capital	37,012	40,600	42,335	38,799	45,929	48,611
Tier 1 ratio (%)	14	13	13	11	13	13
o/w core tier 1 capital ratio (%)	11.8	11.7	11.8	10.5	11.9	11.9
Credit Quality						
Gross NPLs/Total Loans(%)	1.53	1.91	2.18	2.60	4.00	3.00
Risk Provisions/NPLs(%)	64	56	54	52	46	54
Bad debt / Avg loans (%)	0.39	0.52	0.55	0.73	0.95	0.81
Bad debt/Pre-Provision Profit(%)	12.8	18.0	18.2	28.6	37.8	29.9
Growth Rates & Key Ratios						
Growth in revenues (%)	10	5	1	-2	-4	5
Growth in costs (%)	10	7	5	9	-13	2
Growth in bad debts (%)	6	43	11	32	27	-14
Growth in RWA (%)	10	12	7	6	6	6
Net int. margin (%)	2.30	2.21	2.14	1.90	1.88	1.94
Cap.-market rev. / Total revs (%)	0	0	3	3	3	4
Total loans / Total deposits (%)	77	75	76	70	67	67
ROTE Decomposition						
Revenue % ARWAs	6.84	6.49	6.02	5.52	4.98	4.92
Net interest revenue % ARWA	3.94	3.77	3.57	3.31	3.03	2.97
Non interest revenue % ARWA	2.90	2.72	2.44	2.21	1.95	1.96
Costs/income ratio (%)	54.8	56.4	52.8	59.1	59.0	57.7
Bad debts % ARWAs	0.40	0.51	0.52	0.64	0.77	0.62
Tax rate (%)	26.2	27.3	29.4	34.5	24.3	23.4
Adj. Attr. earnings % ARWA	1.88	1.80	1.30	1.13	0.82	1.03
Capital leverage (ARWA/Equity)	8.2	8.3	8.3	8.3	8.0	7.7
ROTE (Adj. earnings/Ave. equity)	15.5	15.0	10.8	9.3	6.6	7.9

Source: Company data, Deutsche Bank estimates

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More fundamental change required

FY14 results were 1% ahead of DBe, 6% below consensus

Profit before tax, restructuring charges, regulatory settlements and own credit value changes of $5,374m was 1% below DB and 6% below consensus. Relative to DBe, income was 1% better, costs in line and impairments 1% lower. RWAs were a full 4% lower than we forecast: deleveraging is under way, helping to fund the dividend and capital ratio build. We were surprised at the lack of negative credit migration in the RWA calculation in 2H14 despite higher loan losses which explains the lion's share of the RWA beat today.

Figure 1: FY results vs DB and consensus expectations

£m	3Q13	4Q13	3Q14	4Q14e	4Q14a	relDB %	QoQ%	YoY%	FY13	FY14e	cons	FY14a	relDB%	YoY%	relCons %
Operating income (ex FVOD)	4,471	4,449	4,514	4,350	4,451	2%	-1%	0%	18,671	18,133	18,200	18,234	1%	-2%	0%
Operating expenses	-2,424	-2,735	-2,523	-2,949	-2,958	0%	17%	8%	-10,193	-10,555	-10,500	-10,564	0%	4%	1%
PPP	**2,047**	**1,714**	**1,991**	**1,401**	**1,493**	**7%**	**-25%**	**-13%**	**8,478**	**7,578**	**7,700**	**7,670**	**1%**	**-10%**	**0%**
Loan impairments	-288	-599	-536	-773	-759	-2%	42%	27%	-1,617	-2,155	-2,200	-2,141	-1%	32%	-3%
Other impairments	-1	-117	-3	-57	-215	277%	nm	84%	-1,129	-245	n/a	-403	64%	-64%	n/a
Associates / JVs	72	42	78	34	57	66%	-27%	36%	226	225	200	248	10%	10%	24%
PBT	**1,830**	**1,040**	**1,530**	**606**	**576**	**-5%**	**-62%**	**-45%**	**5,958**	**5,404**	**5,716**	**5,374**	**-1%**	**-10%**	**-6%**

Source: Deutsche Bank estimates, company data

CRDIV capital ratio at 10.7% was 20bps ahead of our estimate and that of consensus at 10.5% driven by balance sheet deleveraging. Loans were down 2% YoY in 2014. SC are targeting an 11-12% core tier 1 ratio, arguing that profits generated and balance sheet restructuring put this target easily within reach. This is borne out by holding the dividend flat at last year's 86cps; in line with our forecast, this puts the stock on an historic dividend yield of 5.4%, in line with HSBC (Figure 2).

Figure 2: Key balances sheet items and operating metrics

	3Q13	4Q13	3Q14	4Q14e	4Q14a	relDB%	QoQ%	YoY%	FY13	FY14e	FY14a	Cons	Rel DB%	YoY%	relCons %
LLP %	n.a.	0.81%	0.71%	1.05%	1.04%	0%	0%	0%	0.54%	0.73%	0.73%	n/a	0.0%	0.2%	n/a
NPL %	n/a	2.18%	n/a	2.60%	2.59%	0%	nm	0%	2.18%	2.60%	2.59%	n/a	0.0%	0.2%	n/a
Loans and advances	**n.a.**	**296,711**	**296,412**	**293,671**	**289,295**	**-1%**	**-2%**	**-2%**	**296,711**	**293,671**	**289,295**	**302,000**	**-1%**	**-2%**	**-4%**
Deposits	**n.a.**	**390,971**	**395,492**	**396,763**	**414,000**	**4%**	**5%**	**6%**	**390,971**	**396,763**	**414,000**	**390,000**	**4%**	**6%**	**6%**
LDR	n/a	76%	75%	74%	70%	-4%	-5%	-6%	76%	74%	70%	77%	-4%	-8%	-68%
CRDIV Common equity	n.a.	36,508	n.a.	37,412	36,556	-2%	n/a	0%	36,508	37,412	36,556	37,948	-2%	0%	-4%
RWAs	n.a.	331,296	n.a.	357,722	341,648	-4%	n/a	3%	331,296	357,722	341,648	358,000	-4%	3%	-5%
CRDIV CET 1%	**n.a.**	**11.0%**	**n.a.**	**10.5%**	**10.7%**	**0%**	**n/a**	**0%**	**11.0%**	**10.5%**	**10.7%**	**10.6%**	**0.2%**	**0.0%**	
Tier 1 capital	n.a.	36,508	n.a.	37,412	36,494	-2%	n/a	0%	36,508	37,412	36,494	n/a	-2%	0%	n/a
Leverage Exposure	n.a.	776,766	n.a.	790,000	803,314	2%	n/a	3%	776,766	790,000	803,314	n/a	2%	3%	n/a
Tier 1 leverage ratio	n.a.	4.7%	n.a.	4.7%	4.5%	0%	n/a	0%	4.7%	4.7%	4.5%	n/a			
TNAV/share	**n.a.**	**1,594**	**n.a.**	**1,667**	**1,611**	**-3%**	**n/a**	**1%**	**1,594**	**1,667**	**1,611**	**n/a**	**-3%**	**1%**	**n/a**

Source: Deutsche Bank estimates, company data

By division, operating income was lower than we expected in commercial and private banking. Commercial banking in particular is showing the scars of the adjustment to the business model to reduce future conduct risks. The closure of the UAE SME business and client shedding through the client due diligence process (CDD) contributed to revenue down 22% YoY.

Figure 3: Operating income breakdown by division

Income breakdown by client	3Q13	4Q13	3Q14	4Q14e	4Q14a	Rel DB	QoQ%	YoY%	FY13	FY14e	FY14a	Rel DB	YoY	Cons	Rel Cons
Corporate and Institutional	2,521	2,558	2,562	2,415	2,535	5%	-1%	-1%	10,656	10,311	10,431	1%	-2%	10,408	0%
Commercial	370	329	294	279	272	-3%	-7%	-17%	1,511	1,189	1,182	-1%	-22%	1,205	-2%
Private Banking	142	143	155	158	143	-9%	-8%	0%	586	627	612	-2%	4%	624	-2%
Retail	1,438	1,419	1,503	1,499	1,501	0%	0%	6%	5,918	6,007	6,009	0%	2%	6,015	0%
Total income	**4,471**	**4,449**	**4,514**	**4,350**	**4,451**	**2%**	**-1%**	**0%**	**18,671**	**18,133**	**18,234**	**1%**	**-2%**	**18,252**	**0%**

Source: Deutsche Bank estimates, company data

By product, Trade income was 4% lower than we expected in 4Q14. The company says that margins were broadly stable, but average assets were down 4% in 2H14, partly driven by de-risking (shrinking) of the commodity book. Elsewhere, Financial markets was weaker than we expected, 12% down YoY for the full year, and 20% down YoY for 4Q. Corporate finance and ALM beat our estimates though implied guidance for 2015 ALM in line with 2H14 run-rates is a meaningful downgrade to our previous forecasts. As discussed below, exits and deleveraging already conducted lead to a much more subdued income outlook than we had previously included in our numbers even before we consider the more radical approach to reshaping the balance sheet which we think will be required under new CEO, Bill Winters, in order to get the bank's ROE to the 15% at which we think the business model works.

Figure 4: Operating income breakdown by product

Income breakdown by product	3Q13	4Q13	3Q14	4Q14e	4Q14a	Rel DB	QoQ%	YoY%	FY13	FY14e	FY14a	Rel DB	YoY%	Cons	Rel Cons
Transaction Banking	970	977	957	943	927	-2%	-3%	-5%	3,911	3,818	3,802	0%	-3%	n/a	n/a
Trade	517	510	490	486	467	-4%	-5%	-8%	2,069	1,975	1,956	-1%	-5%	n/a	n/a
Cash Management, Custody	453	467	467	456	460	1%	-1%	-1%	1,842	1,842	1,846	0%	0%	n/a	n/a
Financial Markets	902	742	899	827	721	-13%	-20%	-3%	3,856	3,506	3,400	-3%	-12%	n/a	n/a
Corporate Finance	606	675	614	588	632	7%	3%	-6%	2,519	2,443	2,487	2%	-1%	n/a	n/a
Wealth Management	339	355	441	447	443	-1%	0%	25%	1,449	1,705	1,701	0%	17%	n/a	n/a
Retail Products	1,250	1,208	1,211	1,162	1,194	3%	-1%	-1%	5,046	4,808	4,840	1%	-4%	n/a	n/a
Cards, Personal Loans, Unsecured	690	697	642	636	619	-3%	-4%	-11%	2,788	2,593	2,576	-1%	-8%	n/a	n/a
Deposits	290	298	311	309	313	1%	1%	5%	1,193	1,218	1,222	0%	2%	n/a	n/a
Mortgage and Auto	241	237	225	225	239	6%	6%	1%	997	924	938	1%	-6%	n/a	n/a
Other Retail Products	29	-24	33	-8	23	Nm	-30%	nm	68	73	104	42%	53%	n/a	n/a
Others	404	492	392	384	534	39%	36%	9%	1,890	1,854	2,004	8%	6%	n/a	n/a
Asset and Liability Management	101	142	119	90	114	27%	-4%	-20%	548	629	653	4%	19%	n/a	n/a
Lending and Portfolio Management	264	279	251	255	246	-4%	-2%	-12%	1,065	1,035	1,026	-1%	-4%	n/a	n/a
Principal Finance	39	71	22	39	174	352%	691%	145%	277	190	325	72%	17%	n/a	n/a
Total Operating Income	**4,471**	**4,449**	**4,514**	**4,350**	**4,451**	**2%**	**-1%**	**0%**	**18,671**	**18,133**	**18,234**	**1%**	**-2%**	**n/a**	**n/a**

Source: Deutsche Bank estimates, company data

Slightly enlarged targets for change; no game-changer

SC announced additional restructuring plans and targets with these results, which we repeat as the bank printed them below:

- CET1 target of 11-12% in 2015 and thereafter
- RoE target >10% in the medium term
- US$1.8bn of cumulative gross cost savings over the next 3 years
- US$25-30bn of RWA savings over the 2 years

Bottom line: right direction, too modest a destination

It is hard to say whether these plans will survive the arrival of Bill Winters as CEO - we don't think it likely that a new leader will accept entirely the strategy presented by the outgoing predecessor - but it is positive that StanChart isn't wasting the next six months waiting for new leadership.

The bottom line we think is that the 10% medium term ROE target isn't enough to get SC self-financing. The bank's balance sheet must grow much faster than the 5% a 10% ROE can finance to meet wage inflation (5% in the SC footprint, according to management), compliance (US$237m last year) and so on. This is especially the case given the flat dividend paid last year. Though a move we expected, this is incompatible with having the capital strength to restructure and grow the business.

Our forecasts assume a US$5.25bn primary capital raise and a substantial dividend reset to meet modest provisioning and business adjustment ambitions and even then we only get CT1 a little above 12% in 2015. As discussed in our detailed 8 Feb StanChart note we think the bank needs to:

- **Re-align capital** from large, low return corporate lending, corporate finance and own account activities. We recommend a non-core approach to shield market cap from the group EPS downgrades this would drive. We don't think it credible that SC's key margin problem is that the balance sheet has been shopped to cheaply and that the weaker elements of the return profile in Figure 5 will be solved by re-pricing.

Figure 5: Client segment income: too inefficient in Retail, too invested in Own Account?

	Corporate & Institutional	Commercial	Private Banking	Retail	Operating divisions	Own Account Income	Total
Income	4.6	0.6	0.3	2.8	**8.4**	0.9	9.3
Costs	-2.4	-0.3	-0.2	-1.9	**-4.9**	-0.2	-5.1
Pre-provision profit	**2.2**	**0.3**	**0.1**	**0.9**	**3.5**	**0.7**	**4.2**
Impairments (Actual)	-0.4	-0.1	0.0	-0.5	**-1.0**	0.0	-1.0
PBT	**1.8**	**0.2**	**0.1**	**0.4**	**2.5**	**0.7**	**3.2**
Associates & JVs	0.1	0.0	0.0	0.0	**0.1**	0.0	0.1
Operating profit	**1.9**	**0.2**	**0.1**	**0.5**	**2.6**	**0.7**	**3.3**
Tax & Minorities (26% tax, $220m minorities)	-0.5	-0.1	0.0	-0.1	**-0.8**	-0.2	-1.0
Bank levy (US$375m, alloc. By RWAs)	-0.1	0.0	0.0	0.0	**-0.2**	0.0	-0.2
Attributable profit	**1.2**	**0.1**	**0.0**	**0.3**	**1.7**	**0.5**	**2.1**
Capital at 12% assumed requirement	24.5	2.4	0.7	7.2	**34.9**	7.3	42.2
Loans	168.3	17.6	18.1	100.9	**305**	0.0	305.1
% loans	55%	6%	6%	33%	**100%**	n.a.	n.a.
RWAs	204	20	6	60	**291**	61	352
% of Group RWAs	**58%**	**6%**	**2%**	**17%**	**83%**	**17%**	**100%**
Income / RWAs	4.5%	6.1%	9.6%	9.5%	**5.8%**	3.0%	5.3%
Stated cost / income	48%	59%	72%	65%	**55%**	n.a.	n.a.
Cost / income ex Own Acc @ 20%	**52%**	**54%**	**77%**	**67%**	**58%**	**21%**	**55%**
Impairments / RWAs	0.4%	-1%	0%	-2%	**-1%**	0%	-1%
Impairments / Loans	**0.5%**	**1.1%**	**0.0%**	**1.0%**	**0.7%**	**0.0%**	**0.7%**
PBT / RWAs	1.7%	1.8%	2.2%	1.5%	**1.7%**	2.3%	1.8%
ROE (DB. Adj for Own Account)	**10%**	**10%**	**12%**	**8%**	**10%**	**13%**	**10%**

Source: Deutsche Bank estimates, Company data

- **Cut costs, especially in Retail:** We think StanChart should significantly narrow the retail footprint from 35 countries. Today StanChart said they had closed 40 branches this year past year. But retail cost/income ratio remains poor (66%) driven by cost underperformance, and leaves too little profit generation to fund future balance sheet growth.
- The plan to reduce the retail cost ratio to 55% at last year's income level – and as shown later income will likely fall from that level given deleveraging and de-risking – would require a 25% or $1bn cost reduction. Though management refused to give guidance on the restructuring costs to go with even this year's plans, last year's US$181m expense is small beer. Digitalisation and the like are important, but surely faster improvement could be delivered with a bigger budget for change?

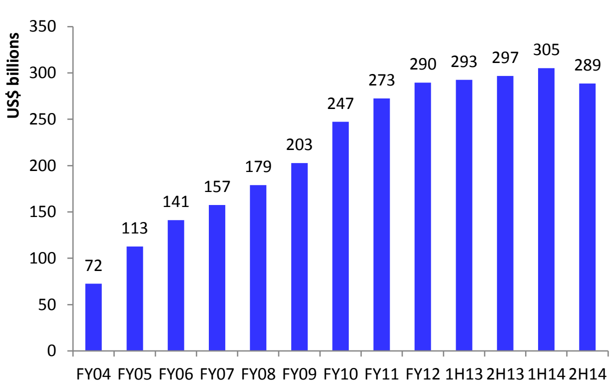
Figure 6: Product returns: Dreadful in Retail, Lending and perhaps also Corporate and Principle Finance relative to inherent risk

1H14	Transaction Banking	Financial Markets	Corp. Fin., Prin. Fin.	Wealth Man.t	Retail Products	ALM, Lending, Port. Man.	Group
Income	1.9	1.8	1.4	0.8	2.4	0.9	9.3
Costs	-1.0	-1.0	-0.6	-0.6	-1.7	-0.2	-5.1
Pre-provision profit	**0.9**	**0.8**	**0.8**	**0.2**	**0.7**	**0.7**	**4.1**
Impairments on EL basis	-0.3	-0.1	-0.4	0.0	-0.5	-0.4	-1.6
PBT	**0.7**	**0.7**	**0.4**	**0.2**	**0.3**	**0.3**	**2.5**
Associates & JVs	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	0.1
Operating profit	**0.7**	**0.7**	**0.4**	**0.2**	**0.3**	**0.3**	**2.6**
Tax & Minorities (26% tax, $220m minorities)	-0.2	-0.2	-0.1	0.0	-0.1	-0.1	-0.8
Bank levy (US$375m, alloc. By RWAs)	0.0	0.0	0.0	0.0	0.0	-0.1	-0.2
Attributable profit	**0.4**	**0.5**	**0.2**	**0.1**	**0.1**	**0.2**	**1.7**
Capital at 12%	7.0	8.1	7.4	0.8	6.9	11.9	42.2
Credit risk RWAs	49	53	50	4	48	92	296
Op risk RWAs	7	7	5	3	9	3	35
Market risk RWAs	2	8	6	0	0	4	20
Total est. RWAs	58	68	62	7	57	99	351
% of Credit risk RWAs	17%	18%	17%	1%	16%	31%	100%
% of est. Group RWAs	**17%**	**19%**	**18%**	**2%**	**16%**	**28%**	**100%**
Income / Credit risk RWAs	7.8%	6.8%	5.6%	40.0%	10.0%	2.0%	6.3%
Cost / income	51%	57%	44%	77%	70%	21%	55%
Impairments / CR RWAs	1.1%	0.3%	1.5%	0.7%	1.9%	0.8%	1.1%
Impairments / Loans	0.6%	n.a.	n.a.	n.a.	n.a.	n.a.	1.0%
Co. Basis RoRWA	**2.7%**	**2.6%**	**1.6%**	**8.5%**	**1.1%**	**0.7%**	**1.7%**
ROE (DB. Adj.)	**13%**	**11%**	**7%**	**28%**	**4%**	**3%**	**8%**

Source: Deutsche Bank estimates

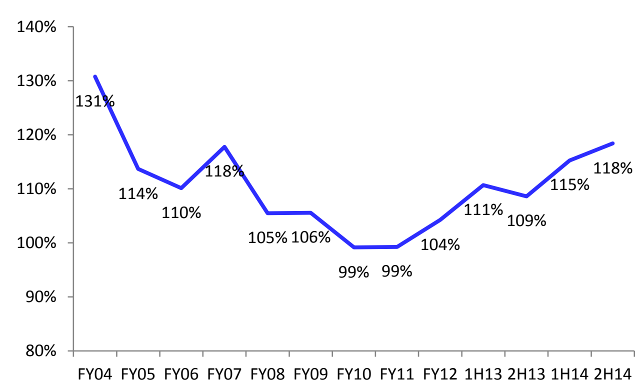
- **Large capital increase:** The bigger budget for change has to come from a raise rather than deleveraging. Funds are needed for restructuring, write-offs and growth. Barring large accretive disposals we think US$5bn is needed. Loan balances fell at StanChart (Figure 7) for the first time in over a decade. The business is acting capital constrained, and we would expect this to continue as it works towards its 11-12% target.

Figure 7: Loan balances over time



Source: Company data

Figure 8: Risk weights / advances



Source: Deutsche Bank estimates, company data

The most prominent loan reductions were in ASEAN (down 9% HoH), but risk weights rose 2% (Figure 9).

Figure 9: Risk weighted asset and loan progression

RWA progression	1H13	2H13	1H14	2H14	HoH%	YoY%
Greater China	62,487	63,284	65,299	66,585	2%	5%
North East Asia	26,286	26,701	25,453	23,990	-6%	-10%
South Asia	26,668	26,721	28,678	26,522	-8%	-1%
ASEAN	86,463	80,377	81,173	82,603	2%	3%
MENAP	30,644	29,402	31,022	29,775	-4%	1%
Africa	21,493	19,729	19,866	20,289	2%	3%
Americas	10,982	12,454	12,572	13,692	9%	10%
Europe	67,920	74,389	98,505	89,592	-9%	20%
Netting balances	-9,167	-10,806	-10,983	-11,400	4%	5%
Total risk-weighted assets	**323,776**	**322,251**	**351,585**	**341,648**	**-3%**	**6%**

Loan progression	1H13	2H13	1H14	2H14	HoH%	YoY%
Greater China	86,411	89,846	95,848	89,646	-6%	0%
North East Asia	32,587	30,618	29,626	29,582	0%	-3%
South Asia	26,109	25,608	24,324	22,859	-6%	-11%
ASEAN	82,259	82,852	86,561	78,541	-9%	-5%
MENAP	23,322	23,535	23,941	22,775	-5%	-3%
Africa	12,600	13,122	13,766	13,103	-5%	0%
Americas	9,286	10,429	11,277	10,952	-3%	5%
Europe	19,219	20,005	19,718	21,141	7%	6%
Total	**291,793**	**296,015**	**305,061**	**288,599**	**-5%**	**-3%**

Source: Deutsche Bank estimates, company data

Our early read on announced targets was too optimistic

The analyst meeting confirmed a much less bullish read for income, costs and RWAs inherent in the objectives shared today. We expect this will drive meaningful consensus downgrades in the coming days.

- Business exits flagged will cause the loss of US$450m of 2014's income will not recur in 2015;
- Though last year's income was already US$300m lower than otherwise would have been the case given de-risking (UAE SME exit, CDD, retail unsecured retrenchment), the fact that much of this was second half weighted means that income will face up to US$300m in additional drag from last year's de-risking.
- It is realistic to expect some revenue drag from the US$25-30bn in RWA "savings" planned. We understand these savings to entail release from current lower return portfolios for deployment. Our work suggests the opoortunity here is even bigger, but this is a one-step-backwards-two-steps-forwards business in our view.
- The near term income outlook is therefore pretty tough, we think. Figure 10 shows how much work is required. Just taking de-risking and exits into account we have revenue down 4% relative to what was reported in FY14.:

Figure 10: Adjusting for de-risking and exit business changes

	Company view			DB view				
	2013	2014	YoY	2013	2014	2014 incl actions	Delta	Comments
Income	18,671	18,234	-2%	18,671	18,234	17,484	-4%	FY14 would have been $300m higher ex de-risking (e.g. UAE SME Aug 2014, smaller retail unsecured book, smaller commodities book), but phasing means will drag again in 2015. We assume the de-risking happened in 2H14, so another $300m to go. Majority of $450m to be lost from 2015.
Expenses	-9,946	-10,198	3%	-9,946	-10,198	-9,995	-2%	> $200m (say $250m) saved from past exits gets to 2014 underlying $10bn,, plus 5% inflation less $450m tgt cost save.
Restructuring costs	-12	-181	1408%	0	0	0	0%	$181m last year to save $200m, plan to save $600m gross in 2015
Levy	-235	-366	56%	-235	-366	-366	0%	
Pre Prov Op Profit	**8,478**	**7,489**	**-12%**	**8,490**	**7,670**	**7,123**	**-7%**	
Loan impairments	-1,617	-2,141	32%	-1,617	-2,141	-2,041	0%	$100m relating to exits reported in FY14
Other impairments	-129	-403	212%	0	0	0	0%	
Associates	226	248	10%	226	248	248	0%	
Profit before tax (Adjusted)	**6,958**	**5,193**	**-25%**	**7,099**	**5,777**	**5,330**	**-8%**	
Own credit adjustment	106	100	-6%	n.a.	n.a.	n.a.	n.a.	
Civil monetary penalty	0	-300	100%	n.a.	n.a.	n.a.	n.a.	
Goodwill impairment	-1,000	-758	-24%	n.a.	n.a.	n.a.	n.a.	
Profit before tax (Stated)	**6,064**	**4,235**	**-30%**	**7,099**	**5,777**	**5,330**	**n.a.**	
PBT ex restructuring	**7,099**	**5,777**		**7,099**	**5,777**	**5,230**	**-8%**	

Source: Deutsche Bank estimates, company data

- **Expenses for 2014** would have been c.US$200m lower, we think, including ~US$250m of cost saves from exit businesses + US$450m of gross cost saves less 5% underlying inflation (cost saves are gross, not net).
- **Loan losses of US$100m** relating to exits were reported last year.
- **PBT looks challenging: Ex restructuring but including the intended gross cost savings for the year we have PBT down 8% pro-forma before the income costs of further planned actions.** In other words, cost plans are smaller than revenues forgone to date.

The picture is a little worse if 4Q14 run rate revenue is used.

4Q14 revenue on an annualized basis was 4% lower than the reported full year number (Figure 11). Unsurprising given deleveraging and expected seasonality in markets but nonetheless important given cost pressures elsewhere. Applying using the 4Q14 run rate figures for costs and income in Figure 10 would get an implied delta of closer to -18%.

Figure 11: Run rate implies 4% lower income, before actions

	FY13	FY14	4Q14 run rate	% ch.
Transaction Banking	**3,911**	**3,802**	**3,708**	**-2%**
o/w Trade	2,069	1,956	1,868	-4%
o/w Cash	1,842	1,846	1,840	0%
Financial Markets	**3,856**	**3,400**	**2,884**	**-15%**
Corporate Finance	**2,519**	**2,487**	**2,528**	**2%**
Wealth Management	**1,449**	**1,701**	**1,772**	**4%**
Retail Products	**5,046**	**4,840**	**4,776**	**-1%**
o/w Unsecured	2,788	2,576	2,476	-4%
o/w Deposits	1,193	1,222	1,252	2%
o/w Mortgage and Auto	997	938	956	2%
o/w Other	68	104	92	-12%
Others	**1,890**	**2,004**	**1,900**	**-5%**
o/w ALM	548	653	416	-36%
o/w Lending, Portfolio Management	1,065	1,026	984	-4%
o/w Principal Finance	277	325	500	54%
Total operating income ex FVOD	**18,671**	**18,234**	**17,568**	**-4%**

Source: Deutsche Bank estimates, company data

Credit quality stance will make kitchen sinking tougher

Loan losses and NPLs reported in line with DBe and CFO Andy Halford endorsed the adequacy of loan provisions citing work done with external auditors on higher risk positions. This will make it harder to put through a clean-up provision under the new CEO at mid year, raising market hopes of avoiding a capital increase. We genuinely think that shareholder value creation is best served by getting a raise, restructuring and provision cycle over and done with so that the balance sheet can return to growth to support a better operational gearing picture than current plans suggest we should expect.

Other noteworthy elements of the credit risk picture shared today included:

- **Commodities / Oil & Gas:** Fuller disclosures of commodity and oil exposures were given in the release, and FD Andrew Halford spent time on the call describing the changes. Overall commodity net exposure was down 11%; oil & gas exposures are down 14% YoY. 98% of the producers exposure is apparently to clients with a break even price below where current levels or to state owned enterprises. The company says it has conducted a “thorough review” of their commodity exposure. FD: “I've also gone through these extensively with the new head of our Group special asset management team, as well as our external auditors, KPMG. The majority of the issues relate to advances made several years ago, and very few relate to recent credit decisions.”
- **NPL formation** during 2H14 was 16% up on FY13, but lower than we had expected and only 4% higher than 1H14. Past due but not impaired loans were lower (US$5.2bn vs US$7bn at 2013 and 1H14). Grade 12 loans (the lowest quality performing loans) were lower at US$5.6bn, down from US$6.5bn at 1H14. But coverage was lower at 52% (Figure 12).

Figure 12: NPL growth and cover by region

NPL growth	Greater China	North East Asia	South Asia	ASEAN	MENAP	Africa	Americas	Europe	Total
2H13 (HoH)	2%	-4%	9%	18%	-12%	104%	-69%	175%	**13%**
1H14 (HoH)	12%	12%	9%	11%	-10%	59%	-80%	30%	**11%**
1H14 (YoY) * Different basis	14%	8%	19%	31%	-21%	223%	-94%	257%	**25%**
2H14 (YoY)	**45%**	**-22%**	**11%**	**31%**	**-17%**	**-22%**	**640%**	**125%**	**16%**
NPL cover by region	Greater China	North East Asia	South Asia	ASEAN	MENAP	Africa	Americas	Europe	Total
1H13	70%	64%	42%	55%	57%	54%	31%	64%	**56%**
2H13	64%	75%	43%	52%	62%	56%	180%	23%	**54%**
1H14 * Different basis	75%	71%	41%	52%	69%	44%	700%	21%	**53%**
2H14	**63%**	**81%**	**44%**	**52%**	**62%**	**34%**	**24%**	**43%**	**52%**
NPL ratio by region	Greater China	North East Asia	South Asia	ASEAN	MENAP	Africa	Americas	Europe	Total
1H13	0.5%	1.8%	6.7%	1.1%	12.6%	3.7%	0.2%	0.6%	**2.0%**
2H13	0.5%	1.9%	7.4%	1.3%	10.8%	7.5%	0.0%	1.7%	**2.2%**
1H14 * Different basis	0.6%	2.2%	7.8%	1.4%	9.3%	11.4%	0.0%	2.2%	**2.4%**
2H14	**0.7%**	**1.5%**	**5.2%**	**1.8%**	**7.6%**	**3.7%**	**0.3%**	**8.1%**	**2.6%**

Source: Deutsche Bank estimates, company data

Forecast changes, valuation and risks

The weaker outlook for revenues drives a 4-7% reduction in our adjusted EPS estimates. This leaves the share trading 12.2x 2016 EPS, 1.0x TNAV for an 7% ROTE. Though the dividend was held flat at FY14 we expect a rebasing this year to reduce the forward yield to around 2%.

Figure 13: StanChart forecast changes and key valuation metrics

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015e	2016e	2017e
EPS (Adj.) (Old) (US$ c)	160	197	230	175	195	203	213	166	155	113	138	167
EPS (Adj.) (New) (US$ c)	**160**	**197**	**230**	**175**	**195**	**203**	**213**	**166**	**151**	**107**	**129**	**161**
% change	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**-6%**	**-7%**	**-4%**
DPS (US$ c)	71.0	79.4	61.6	63.6	69.2	76.0	84.0	86.0	86.0	26.7	32.3	40.2
TNAV (US$ c)	811	931	753	955	1,274	1,349	1,515	1,594	1,668	1,598	1,688	1,773
Market Cap (US$'m)	21,810	22,220	29,874	31,912	37,002	37,569	38,026	38,247	38,972	45,880	47,027	48,203
P/E (Adj.)	**9.9**	**8.0**	**6.9**	**9.0**	**8.1**	**7.8**	**7.4**	**9.5**	**10.4**	**14.7**	**12.2**	**9.8**
Div yield (%)	**4.5%**	**5.0%**	**3.9%**	**4.0%**	**4.4%**	**4.8%**	**5.3%**	**5.5%**	**5.5%**	**1.7%**	**2.0%**	**2.5%**
Adj. EPS payout ratio	**45%**	**40%**	**27%**	**36%**	**36%**	**38%**	**39%**	**52%**	**57%**	**25%**	**25%**	**25%**
P/TBVPS	**1.9**	**1.7**	**2.1**	**1.7**	**1.2**	**1.2**	**1.0**	**1.0**	**0.9**	**1.0**	**0.9**	**0.9**
P/BVPS	**1.3**	**1.1**	**1.4**	**1.2**	**1.0**	**1.0**	**0.9**	**0.9**	**0.8**	**0.9**	**0.8**	**0.8**
ROTE (%)	**20%**	**21%**	**23%**	**17%**	**14%**	**15%**	**12%**	**8%**	**6%**	**6%**	**7%**	**9%**
Basel 3 Core tier 1	**n/a**	**n/a**	**n/a**	**n/a**	**10.8%**	**10.8%**	**10.7%**	**11.0%**	**10.7%**	**12.1%**	**12.1%**	**12.3%**
BCBS tier 1 lev ratio	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**4.7%**	**4.6%**	**5.5%**	**5.7%**	**5.9%**

Source: Deutsche Bank estimates, Company data; Note: Our valuations include an assumed $5.25bn capital increase in 2015

Our StanChart target price is derived using a sum-of-the-parts calculation which values the operating divisions by applying fair P/E multiples to our 2016 earnings forecasts. Multiples applied are calibrated against peers, making allowances for our assessment of differences in growth and risk. Our terminal valuation is further adjusted for our assessment of SC's capital need and our expectations for excess loan write-offs and restructuring charges. Lower earnings estimates contribute to a reduction in TP to HK$101 from HK$102. With substantial downside from current levels, retain Sell.

Figure 14: StanChart SOTP valuation

	PBT (US$'m, 16e)	PAT (US$'m, 16e)	TNAV (US$'m, 15e)	ROTE	P/TNAV	P/E	Value (US$'m)	% value	Value per share (HKD)
Corporate & Institutional Clients	4,112	2,637	36,015	7%	1.0	13.7	36,015	76%	112
Commercial Clients	264	178	1,679	10%	1.1	10.0	1,777	4%	6
Private Banking Clients	177	116	1,400	8%	0.8	10.0	1,158	2%	4
Retail Clients	1,255	850	7,442	11%	1.1	9.6	8,186	17%	26
Operating divisions	**5,808**	**3,780**	**46,536**	**8%**	**1.0**	**12.5**	**47,136**	**100%**	**147**
Bank levy	-365	-365	0	n.a.	n.m.	12.5	-4,551	n.a.	n.a.
Total business value	**5,443**	**3,415**	**46,536**	**8%**	**0.9**	**12.5**	**42,585**	**100%**	**133**
Discounted to 12 months fwd									**123**
% rel. to spot									**5%**
Strategic change									
Capital increase							-5,250	n.a.	-16
Provisions & Restructuring							-2,220	n.a.	-7
Adjusted valuation							**35,115**	**n.a.**	**109**
Discounted target price									**101**
Relative to current price									**-13%**

Source: Deutsche Bank estimates, Company data

Key upside risks are much stronger-than-forecast capital formation, a bid for SC, or significant improvement in EM growth and commodity price prospects.

Appendix 1

Important Disclosures

Additional information available upon request

Disclosure checklist

Company	Ticker	Recent price*	Disclosure
Standard Chartered	2888.HK	116.70 (HKD) 4 Mar 15	1,6,7,14

*Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg and other vendors . Data is sourced from Deutsche Bank and subject companies.

Important Disclosures Required by U.S. Regulators

Disclosures marked with an asterisk may also be required by at least one jurisdiction in addition to the United States. See Important Disclosures Required by Non-US Regulators and Explanatory Notes.

1. Within the past year, Deutsche Bank and/or its affiliate(s) has managed or co-managed a public or private offering for this company, for which it received fees.

6. Deutsche Bank and/or its affiliate(s) owns one percent or more of any class of common equity securities of this company calculated under computational methods required by US law.

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1. Within the past year, Deutsche Bank and/or its affiliate(s) has managed or co-managed a public or private offering for this company, for which it received fees.

6. Deutsche Bank and/or its affiliate(s) owns one percent or more of any class of common equity securities of this company calculated under computational methods required by US law.

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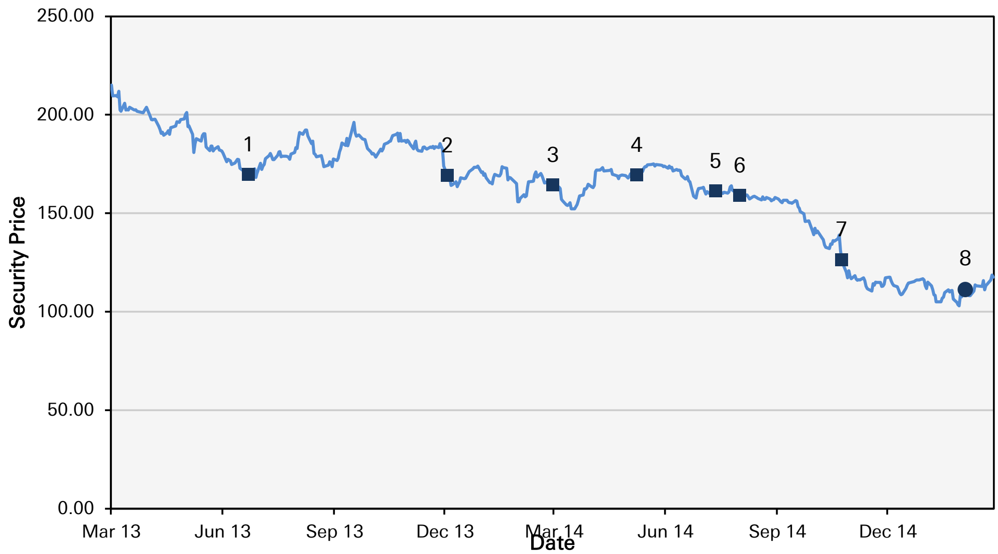
Analyst Certification

The views expressed in this report accurately reflect the personal views of the undersigned lead analyst(s) about the subject issuer and the securities of the issuer. In addition, the undersigned lead analyst(s) has not and will not receive any compensation for providing a specific recommendation or view in this report. Jason Napier

Historical recommendations and target price: Standard Chartered (2888.HK)

(as of 3/4/2015)



Previous Recommendations

Strong Buy
Buy
Market Perform
Underperform
Not Rated
Suspended Rating

Current Recommendations

Buy
Hold
Sell
Not Rated
Suspended Rating

*New Recommendation Structure as of September 9,2002

1.	28/06/2013:	Hold, Target Price Change HKD195.00	5.	18/07/2014:	Hold, Target Price Change HKD153.00
2.	09/12/2013:	Hold, Target Price Change HKD178.00	6.	07/08/2014:	Hold, Target Price Change HKD155.00
3.	06/03/2014:	Hold, Target Price Change HKD176.00	7.	30/10/2014:	Hold, Target Price Change HKD135.00
4.	14/05/2014:	Hold, Target Price Change HKD166.00	8.	09/02/2015:	Downgrade to Sell, Target Price Change HKD102.00

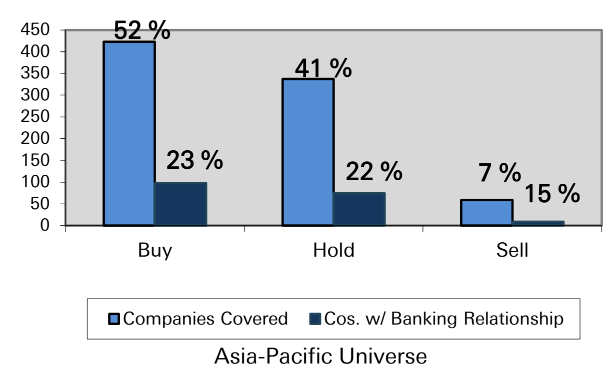
Equity rating key

Buy: Based on a current 12- month view of total share-holder return (TSR = percentage change in share price from current price to projected target price plus pro-jected dividend yield) , we recommend that investors buy the stock.
Sell: Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock
Hold: We take a neutral view on the stock 12-months out and, based on this time horizon, do not recommend either a Buy or Sell.
Notes:

1. Newly issued research recommendations and target prices always supersede previously published research.
2. Ratings definitions prior to 27 January, 2007 were:

    Buy: Expected total return (including dividends) of 10% or more over a 12-month period
    Hold: Expected total return (including dividends) between -10% and 10% over a 12-month period
    Sell: Expected total return (including dividends) of -10% or worse over a 12-month period

Equity rating dispersion and banking relationships



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