

Banks

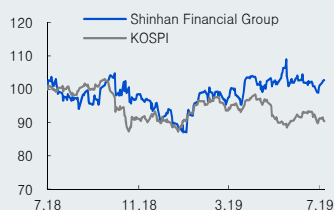
Company Report
July 19, 2019

(Maintain)	Buy
Target Price (12M, W)	60,000
Share Price (07/18/19, W)	45,250
Expected Return	33%

NP (19F, Wbn)	3,451
Consensus NP (19F, Wbn)	3,373
EPS Growth (19F, %)	9.3
Market EPS Growth (19F, %)	-24.5
P/E (19F, x)	6.2
Market P/E (19F, x)	12.4
KOSPI	2,066.55

Market Cap (Wbn)	21,458
Shares Outstanding (mn)	492
Free Float (%)	80.8
Foreign Ownership (%)	67.0
Beta (12M)	0.55
52-Week Low	38,350
52-Week High	48,000

(%)	1M	6M	12M
Absolute	-0.8	11.0	0.7
Relative	0.8	14.1	11.6



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[Banks/Credit Cards]

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Shinhan Financial Group

(055550 KS)

Key strengths are business portfolio and risk management

Steady profit growth over the past five years + inorganic growth momentum

Shinhan Financial Group (SFG) has recorded steady net profit growth since 2013, which we largely attribute to the earnings stability resulting from the group's diversified business portfolio and strong risk management capabilities.

For financial (bank) holding companies, business diversification across banks and non-banks can be a major advantage that provides earnings stability during times of interest rate changes. While a decline in interest rates is negative to the net interest margins (NIMs) of banks, and sentiment on the sector tends to be correlated to interest rate moves, lower interest rates can also drive non-interest income by increasing fixed income-related gains and boosting commission income, including trust fees from the sale of equity-linked securities (ELS) and equity-linked trusts (ELT), and wealth management fees. As lenders, credit card and finance companies raise funds by issuing corporate debt or ABS. Therefore, a fall in interest rates leads to a fall in their funding costs, providing a cushion for group net interest income. In the case of SFG, the relatively high earnings exposure to its credit card subsidiary had been a source of concern due to regulatory headwinds (i.e., merchant fee cuts). However, we believe the recent fall in interest rates and BOK rate cut are more positive than negative for credit card companies. From 2002 to 2007, SFG made a series of acquisitions, including Good Morning Securities, LG Card, and Chohung Bank. Following a 10-year break, the group purchased Orange Life Insurance and Asia Trust in 2018. As such, we expect the group to see inorganic profit growth momentum. We also project SFG's bank subsidiary to generate robust earnings, supported by solid loan growth and stable SG&A expenses.

W400bn share buyback underway

On May 10th, SFG signed a trust agreement for a W400bn share buyback lasting from May 13th to November 13th (six months). Of the W400bn, the group has so far bought back around W180bn worth of shares (as of July 17th). Further taking into account the previous W200bn share repurchase program announced on September 5, 2018 and completed on April 9, 2019, SFG will own a total of W600bn worth of treasury shares by November 13, 2019. We believe SFG will use its treasury shares to acquire the remaining shares in Orange Life Insurance that it does not already own. If so, we expect net profit (attributable to controlling interests) to gain additional growth momentum.

Earnings stability to stand out amid macro worries and falling interest rates

We are positive on SFG's strategy to: 1) secure profit growth drivers and diversify its income base via M&As; 2) expand its global business by advancing into Vietnam, which has higher growth/margin potential than the domestic market; and 3) strengthen its capital market competitiveness in Korea. Despite macro worries and falling interest rates, we believe SFG will display earnings stability on the back of its diversified business portfolio and strong risk management capabilities. We maintain our Buy rating and target price of W60,000 on SFG.

Fiscal year-end	12/16	12/17	12/18	12/19F	12/20F	12/21F
Net interest inc. (Wbn)	7,205	7,843	8,580	9,767	10,100	10,496
Net non-interest inc. (Wbn)	1,577	1,341	1,399	1,255	1,286	1,342
Operating profit (Wbn)	3,109	3,829	4,499	5,011	5,231	5,468
Net profit (Wbn)	2,775	2,918	3,157	3,451	3,569	3,713
EPS (W)	5,767	6,153	6,657	7,277	7,424	7,452
EPS growth (%)	18.2	6.7	8.2	9.3	2.0	0.4
P/E (x)	7.8	7.4	6.8	6.2	6.1	6.1
P/PPOP (x)	5.0	4.9	4.1	3.6	3.5	3.3
P/B (x)	0.69	0.65	0.60	0.56	0.54	0.51
ROE (%)	9.0	9.1	9.2	9.3	9.0	8.6
Dividend yield (%)	3.2	3.2	3.5	3.9	4.1	4.2

Note: All figures are based on consolidated K-IFRS; NP refers to net profit attributable to controlling interests
Source: Company data, Mirae Asset Daewoo Research estimates

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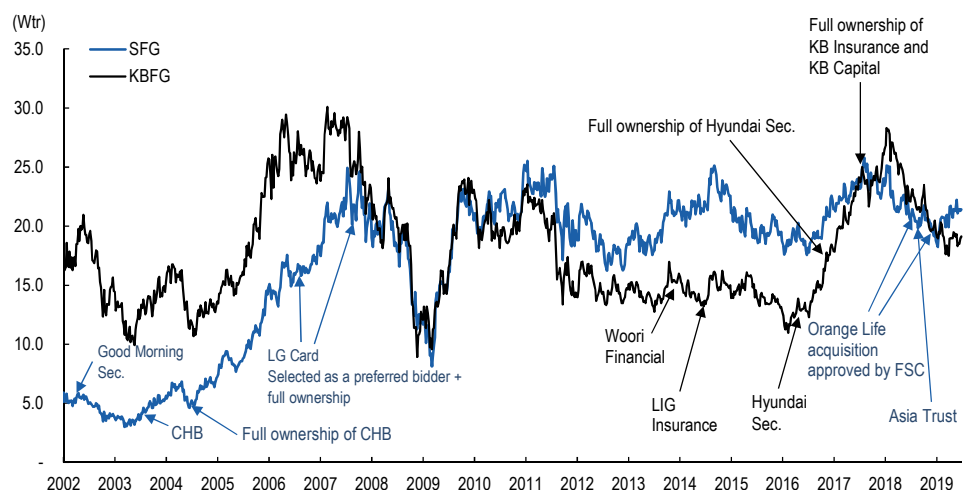
Business portfolio effects

As we mentioned above, for financial (bank) holding companies, business diversification across banks and non-banks can be a major advantage that provides earnings stability during times of interest rate changes. And with the high growth period of banks' domestic loan assets having come to an end, we believe efforts to strengthen non-bank operations through M&As make sense as a counter-strategy against the "low growth" trend.

Indeed, the market views non-banking M&As positively, unless an excessive price is paid. Notably, non-banking M&As are seen as a good strategy to diversify revenue sources, particularly at a time when the medium/long-term growth of banks' domestic loan assets is in doubt due to the household debt issue and the economic slowdown. After a series of acquisitions from 2002 to 2007 (including Good Morning Securities, LG Card, and Chohung Bank), SFG took a long hiatus; however, it is now back on the M&A trail, taking over Orange Life Insurance and Asia Trust in Korea, giving rise to inorganic growth momentum.

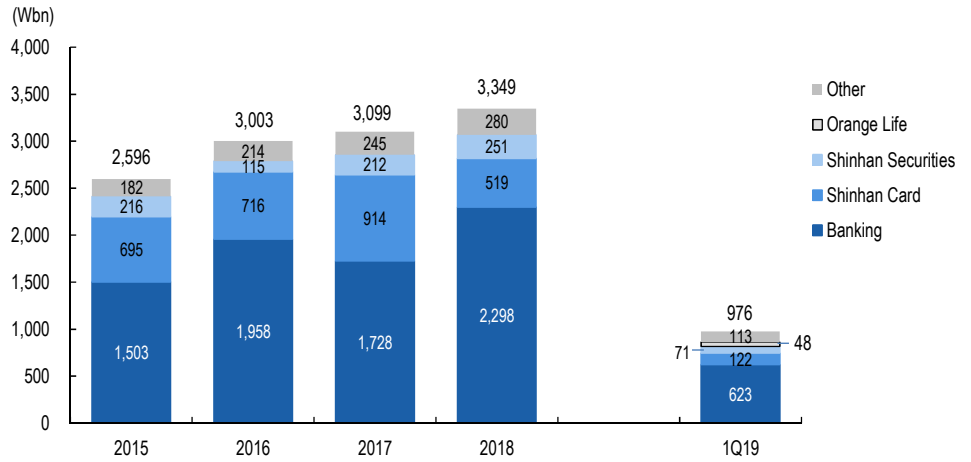
From the 2008 global financial crisis through 2017, SFG enjoyed the sector's largest market cap, but it was overtaken by KB Financial Group (KBFG) when the latter moved to make KB Insurance and KB Capital into wholly-owned subsidiaries—moves that were coupled with efforts to improve cost structure (aided by solid earnings and one-off gains). In early 2019, SFG's market cap once again overtook KBFG's, supported by earlier-than-expected approval of its move to acquire Orange Life Insurance from financial authorities and solid quarterly results.

Figure 1. Market caps of KBFG and SFG and major M&As



Source: Company data, Quantwise, Mirae Asset Daewoo Research

Figure 2. SFG: Profit contributions from banking/non-banking businesses (before consolidation adjustments/other adjustments)



Source: Company data, Mirae Asset Daewoo Research

Figure 3. SFG: Earnings contribution by subsidiary in 2018 (before reflecting consolidation adjustments and other factors)

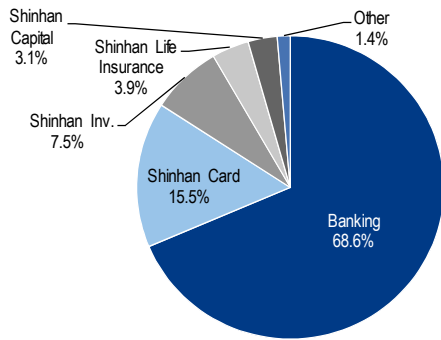
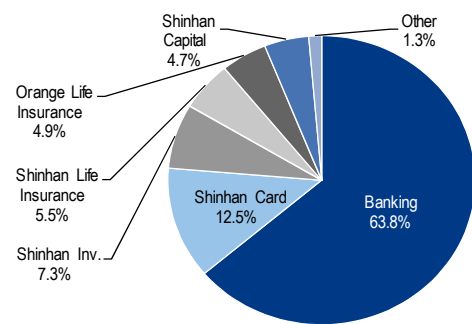


Figure 4. SFG: Earnings contribution by subsidiary in 1Q19 (before reflecting consolidation adjustments and other factors)



(Wbn)	Net profit (a)	Ownership (b)	Net profit (a) x (b)	(%)
Banking	2,306.4		2,298.7	68.6
Shinhan Bank	2,279.0	100.0	2,279.0	68.0
Jeju Bank	27.4	71.9	19.7	0.6
Non-banking	1,057.4		1,050.7	31.4
Shinhan Card	519.4	100.0	519.4	15.5
Shinhan Inv.	251.3	100.0	251.3	7.5
Shinhan Life Insurance	131.0	100.0	131.0	3.9
Shinhan BNP Paribas	18.9	65.0	12.3	0.4
Shinhan Capital	103.4	100.0	103.4	3.1
Shinhan Savings Bank	19.4	100.0	19.4	0.6
Shinhan Data System	1.3	100.0	1.3	0.0
Shinhan AITAS	8.5	99.8	8.4	0.3
Shinhan Credit Info.	1.4	100.0	1.4	0.0
Shinhan Alternative Inv.	-0.8	100.0	-0.8	0.0
Shinhan REIT's Mgmt	3.6	100.0	3.6	0.1
Total	3,363.8		3,349.4	100

Source: Company data, Mirae Asset Daewoo Research

(Wbn)	Net profit (a)	Ownership (b)	Net profit (a) x (b)	(%)
Banking	625.1		623.1	63.8
Shinhan Bank	618.1	100.0	618.1	63.3
Jeju Bank	7.0	75.3	5.0	0.5
Non-banking	387.9		353.1	36.2
Shinhan Card	122.2	100.0	122.2	12.5
Shinhan Inv.	70.8	100.0	70.8	7.3
Shinhan Life Insurance	53.9	100.0	53.9	5.5
Orange Life Insurance	80.4	59.2	47.6	4.9
Shinhan BNP Paribas	5.4	65.0	3.5	0.4
Shinhan Capital	45.6	100.0	45.6	4.7
Shinhan Savings Bank	5.5	100.0	5.5	0.6
Shinhan Data System	0.7	100.0	0.7	0.1
Shinhan AITAS	2.6	99.8	2.6	0.3
Shinhan Credit Info.	0.1	100.0	0.1	0.0
Shinhan Alternative Inv.	-0.6	100.0	-0.6	-0.1
Shinhan REIT's Mgmt	1.3	100.0	1.3	0.1
Total	1,013.0		976.2	100

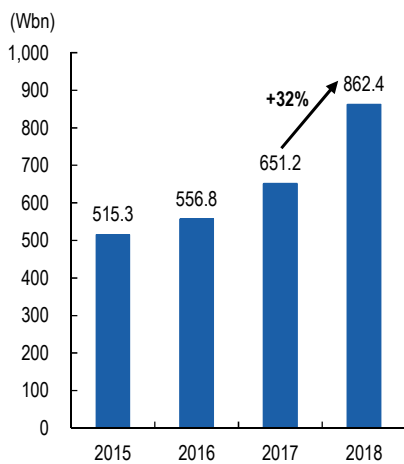
Source: Company data, Mirae Asset Daewoo Research

Global operations

Given the current domestic environment (low growth, low interest rates, and population aging), we believe it is essential for financial firms to advance into overseas markets with higher growth/margin potential (such as Southeast Asia) to find new growth drivers, raise profitability, and build more globally diversified asset portfolios over the medium and long term. While significant progress is unlikely in the near term, we expect a stark divergence to eventually emerge between those financial firms that expand overseas and develop a deep understanding of overseas markets and systems and those that do not.

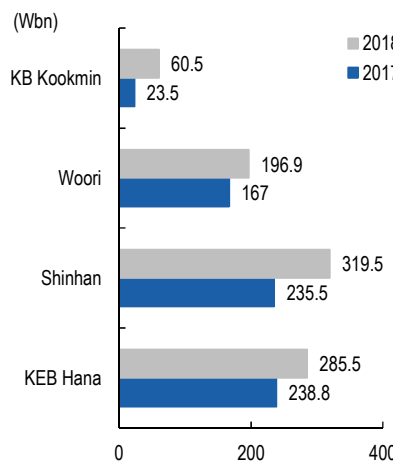
In 2018, the four major domestic commercial banks' combined won-denominated net profit from overseas operations climbed 32% YoY to W862.4bn, hitting a historic high. Shinhan Bank recorded the highest net profit, followed by KEB Hana Bank, Woori Bank, and KB Kookmin Bank. For SFG, overseas bank operations contributed won-denominated net profit of W320bn (14% of Shinhan Bank's overall result), with Vietnam and Japan making the largest contributions.

Figure 5. Four major commercial banks' combined net profit from overseas branches



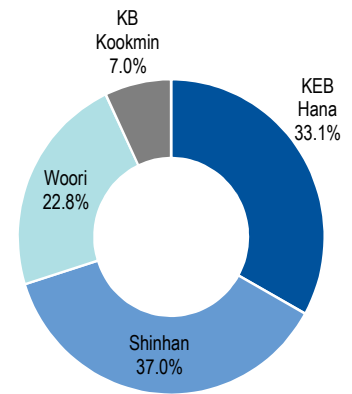
Source: KFB, press reports, company data, Mirae Asset Daewoo Research

Figure 6. Four major commercial banks' net profit from overseas branches (2017 vs. 2018)



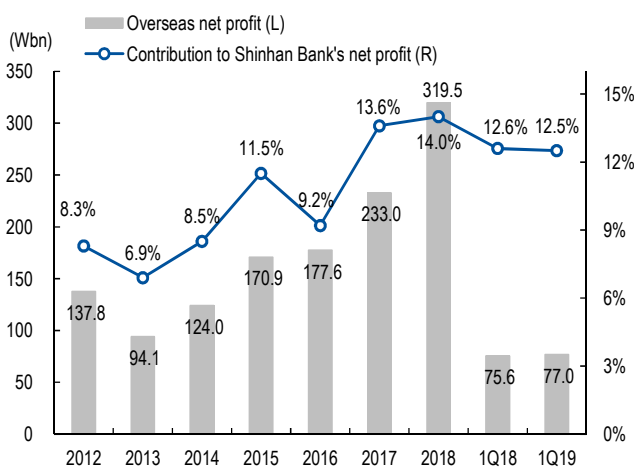
Source: KFB, press reports, company data, Mirae Asset Daewoo Research

Figure 7. Four major commercial banks' net profit contributions from overseas branches (2018)



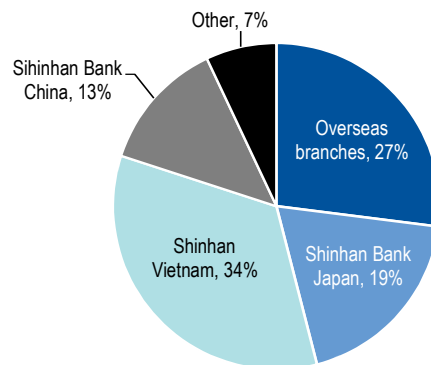
Source: KFB, press reports, company data, Mirae Asset Daewoo Research

Figure 8. SFG: Net profit from overseas banking operations



Source: Company data, Mirae Asset Daewoo Research

Figure 9. SFG: Net profit contribution from overseas banking operations (1Q19)



Source: Company data, Mirae Asset Daewoo Research

SFG is aiming to raise the group's net profit contribution from global operations to around 20% by 2020. The group has 213 overseas branches in 20 countries. In particular, Vietnam, Indonesia, Myanmar, India, Singapore, Cambodia, and the Philippines account for 76% of its total overseas operations and 81% of its global employees.

In 2017, SFG added eight overseas branches by acquiring ANZ Bank's (ANZ AU/CP: AU\$27.22) Vietnamese retail unit, making it no. 1 in terms of number of sales channels among foreign banks in Vietnam. In addition, early this year, SFG's card subsidiary obtained approval from the Vietnamese financial authorities to acquire Prudential Vietnam Finance Company (PVFC), and it acquired a 100% stake in PVFC in June. PVFC, which launched in early July under the new name Shinhan Vietnam Finance Company (SVFC), specializes in unsecured loans to premium customers in urban areas; it posted net profits of W10bn in 2016 and W13bn in 2017. Leveraging its non-bank financial license, SVFC plans to diversify into retail financial services, including auto financing, and seek new businesses in cooperation with Shinhan Bank.

2Q19 preview: Net profit of W929.3bn, above the consensus

For 2Q19, we forecast SFG to post net profit attributable to controlling interests of W929.3bn (-0.9% YoY, +1.2% QoQ), above the Bloomberg and FnGuide consensus (W910bn). One-off factors likely included a write-back of provisions (W15bn) related to Hanjin Heavy I&C (097230 KS/CP: W5,680).

Bank-level won-denominated loans likely grew 2.0% QoQ in 2Q19, up 4.6% since end-2018. For the full year, we forecast won-denominated loans to expand 5.2%, as the bank is likely to take a breather and focus more on asset quality and profitability in 2H19.

We estimate bank NIM declined 2bps QoQ to 1.59%. Market rates reflected the BOK's rate cut (July 18th) in advance, likely weighing on 2Q19 NIM. Based on our 2Q19 assumptions, we project bank NIM to decline a further 2bps in both 3Q19 (to 1.57%) and 4Q19 (to 1.55%).

Meanwhile, we estimate group-level net interest income at W2.44tr (+14.8% YoY, +2.3% QoQ) and net commission income at W488.9bn (-4.7% YoY, +0.9% QoQ). We estimate SG&A expenses modestly increased to W1.18tr (+4.8% YoY, +1.0% QoQ), with a cost-to-income ratio of 42.4% (-0.4%p YoY, -0.5%p QoQ). As the bank conservatively reflected non-financial items in credit evaluation and provisioning for corporate loans, we estimate credit costs increased to W260.4bn (+49.8% YoY, +3.8% QoQ), or 35bps (+9bps YoY, +1bp QoQ) of total credit.

Table 1. SFG: 2Q19 preview

(Wbn)	4Q17	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19F	YoY chg. (%, %p)	QoQ chg. (%, %p)
Net interest income	2,072.2	2,058.8	2,121.4	2,171.8	2,228.1	2,381.5	2,435.6	14.8	2.3
Net fee & commission income	431.7	482.6	513.3	479.4	463.7	479.9	488.9	-4.7	1.9
Net other income	-195.6	-98.1	-1.6	-214.6	-225.2	-131.8	-138.3	RR	RR
Total net operating income	2,308.3	2,443.3	2,633.1	2,436.6	2,466.5	2,729.5	2,786.2	5.8	2.1
SG&A expenses	1,587.5	1,087.0	1,126.4	1,089.2	1,439.0	1,168.4	1,180.0	4.8	1.0
PPOP	720.8	1,356.3	1,506.7	1,347.4	1,027.5	1,561.2	1,606.2	6.6	2.9
Provisions	385.4	179.4	173.8	214.8	170.6	250.8	260.4	49.8	3.8
Operating profit	335.4	1,176.9	1,332.9	1,132.6	856.9	1,310.3	1,345.8	1.0	2.7
Non-operating income	-115.0	17.1	-24.1	33.7	-59.4	12.2	3.4	TTB	-72.0
Pretax profit	220.5	1,194.0	1,308.8	1,166.3	797.5	1,322.5	1,349.2	3.1	2.0
Net profit	211.5	857.5	938.1	847.8	513.3	918.4	929.3	-0.9	1.2
Total assets	426,306	433,397	453,268	457,709	459,608	513,865	525,713	16.0	2.3
Total loans & receivables	275,566	277,838	287,921	292,360	299,609	307,960	313,490	8.9	1.8
Won-denominated loans (bank)	195,497	197,409	201,294	205,188	209,568	215,007	219,307	8.9	2.0
Total credit	263,976	266,659	276,024	281,369	287,918	295,961	301,143	9.1	1.8
Total deposits	249,419	250,965	259,911	260,651	265,000	273,848	279,313	7.5	2.0
Total shareholders' equity	33,703	33,148	34,299	36,017	36,659	38,594	39,600	15.5	2.6
(%)									
NIM (bank)	1.58	1.61	1.63	1.62	1.61	1.61	1.59	-0.04	-0.02
Cost-to-income ratio	68.8	44.5	42.8	44.7	58.3	42.8	42.4	-0.4	-0.5
NPL (sub-standard & below) ratio	0.62	0.64	0.59	0.55	0.53	0.54	0.51	-0.08	-0.03
NPL coverage ratio	259.6	262.3	276.4	290.7	301.8	297.2	335.5	59.1	38.3
RoAE	0.05	0.20	0.21	0.19	0.11	0.19	0.18	-0.03	-0.01
RoAA	0.64	2.63	2.84	2.46	1.45	2.55	2.54	-0.31	-0.02
Credit costs (to total credit)	0.15	0.07	0.06	0.08	0.06	0.08	0.09	0.02	0.00
BIS ratio	14.78	14.86	14.87	15.25	14.87	14.02	14.20	-0.67	0.17
Tier 1 ratio	13.32	13.43	13.45	13.79	13.42	12.66	12.94	-0.51	0.28

Note: ROA, ROE, and credit cost data are non-annualized.

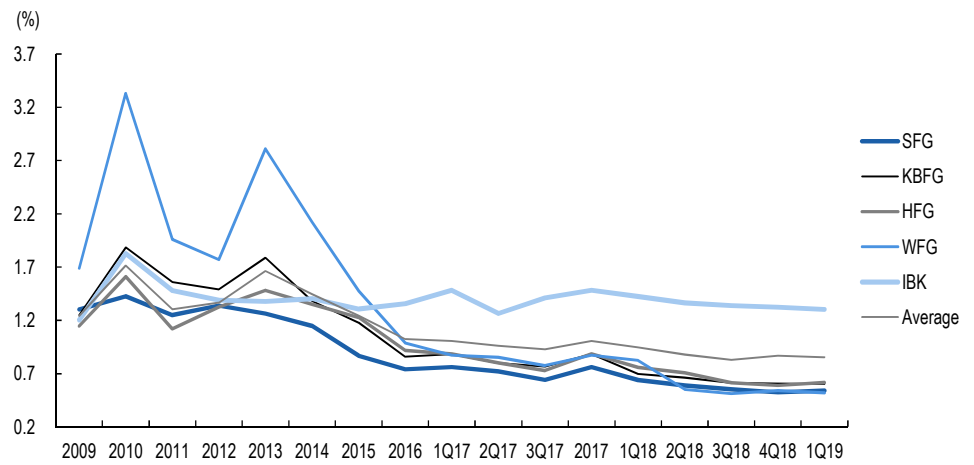
Source: Company data, Mirae Asset Daewoo Research

Table 2. SFG: Earnings forecast revisions

(Wbn)	Revised			Previous			% chg.		
	2019F	2020F	2021F	2019F	2020F	2021F	2019F	2020F	2021F
Net interest income	9,767	10,100	10,496	9,891	10,290	10,674	-1.3	-1.8	-1.7
Net non-interest income	1,255	1,286	1,342	1,208	1,160	1,236	3.9	10.8	8.6
Total net operating income	11,021	11,386	11,838	11,099	11,450	11,910	-0.7	-0.6	-0.6
SG&A expenses	5,068	5,201	5,319	5,131	5,266	5,386	-1.2	-1.2	-1.2
PPOP	5,953	6,185	6,519	5,967	6,184	6,524	-0.2	0.0	-0.1
Provisions	943	954	1,051	905	963	1,066	4.2	-0.9	-1.4
Operating profit	5,011	5,231	5,468	5,063	5,221	5,458	-1.0	0.2	0.2
Non-operating income	13	0	0	13	0	0	0.0	0.0	0.0
Pretax profit	5,024	5,231	5,468	5,076	5,222	5,458	-1.0	0.2	0.2
Net profit	3,451	3,569	3,713	3,488	3,562	3,705	-1.1	0.2	0.2

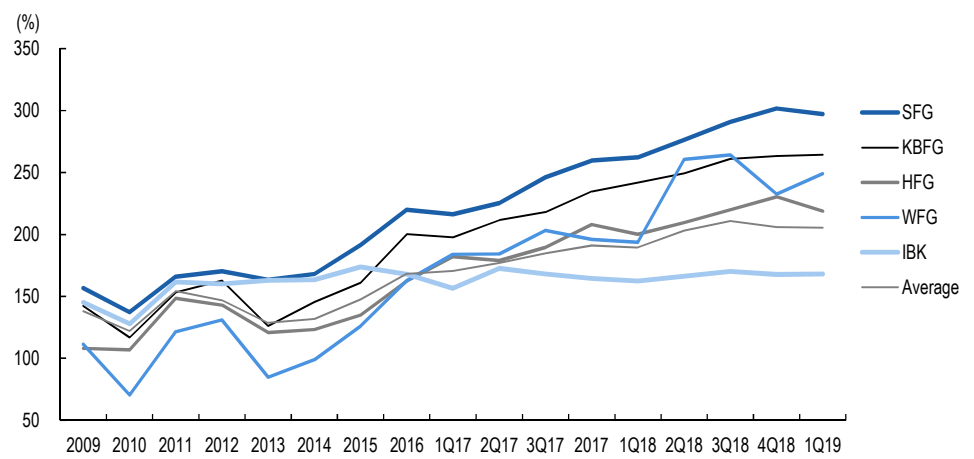
Source: Mirae Asset Daewoo Research estimates

Figure 10. Group-level NPL ratio trends



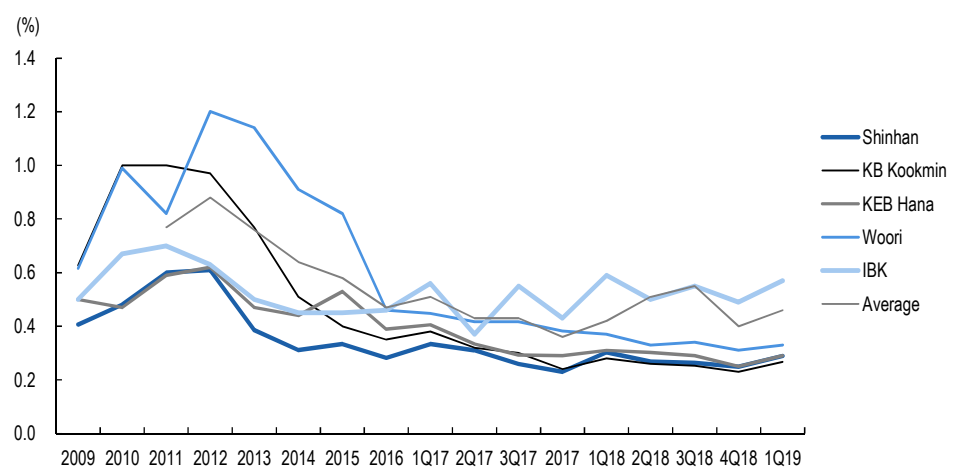
Source: Company data, Mirae Asset Daewoo Research

Figure 11. Group-level NPL coverage ratio trends



Source: Company data, Mirae Asset Daewoo Research

Figure 12. Bank-level delinquency rate trends



Source: Company data, Mirae Asset Daewoo Research

Table 3. SFG: TP calculation

Sustainable ROE	8.50%
Growth	2.00%
Cost of equity	10.78%
Cost of equity	10.78%
Rf	2.5%
Beta	1.38
Market premium	6.0%
Fair P/B (x)	0.74
2019F BPS (W)	80,981
TP (W)	60,000

Source: Mirae Asset Daewoo Research

Table 4. SFG: Valuation metrics at TP of W60,000

	2016	2017	2018	2019F	2020F	2021F
P/B (x)	0.91	0.87	0.80	0.74	0.71	0.68
P/E (x)	10.4	9.8	9.0	8.2	8.1	8.1
ROE (%)	9.0	9.1	9.2	9.3	9.0	8.6
EPS growth (%)	18.2	6.7	8.2	9.3	2.0	0.4
Dividend yield (%)	2.4	2.4	2.7	2.9	3.1	3.2

Source: Company data, Mirae Asset Daewoo Research

Table 5. Bank (financial) holding company and credit card stocks: Valuation table

		SFG	KBFG	HFG	IBK	BNKFG	DGBFG	JBFG	Samsung Card
Ticker		055550 KS	105560 KS	086790 KS	024110 KS	138930 KS	139130 KS	175330 KS	029780 KS
Rating		Buy	Buy	Buy	Buy	Buy	Buy	Buy	Trading Buy
TP (W)		60,000	65,000	58,500	19,500	8,900	12,000	8,300	40,500
CP (W)		45,250	45,000	35,450	13,700	7,210	7,730	5,730	36,650
Upside (%)		32.6	44.4	65.0	42.3	23.4	55.2	44.9	10.5
Market cap (Wbn)		21,458	18,815	10,644	7,877	2,350	1,307	1,129	4,246
Foreign ownership (%)		67.0	67.5	69.3	23.5	52.8	59.0	42.2	11.6
P/B (x)	2017	0.65	0.55	0.44	0.46	0.33	0.33	0.36	0.61
	2018	0.60	0.53	0.40	0.43	0.31	0.31	0.36	0.63
	2019F	0.56	0.49	0.38	0.41	0.30	0.29	0.32	0.61
	2020F	0.54	0.45	0.35	0.38	0.28	0.27	0.29	0.58
	2021F	0.51	0.41	0.32	0.35	0.26	0.25	0.27	0.56
P/E (x)	2017	7.4	5.6	5.2	6.0	5.8	4.3	4.8	11.0
	2018	6.8	6.1	4.7	5.1	4.7	3.4	3.7	12.3
	2019F	6.2	5.5	4.3	4.9	4.5	3.8	3.3	12.0
	2020F	6.1	5.3	4.0	4.7	4.2	3.6	3.3	11.5
	2021F	6.1	5.0	3.7	4.5	4.0	3.5	3.2	10.9
P/PPOP (x)	2017	4.9	4.1	2.9	2.6	2.1	2.2	1.7	5.4
	2018	4.1	3.8	2.9	2.3	1.9	2.5	1.5	4.9
	2019F	3.6	3.5	2.5	2.3	1.9	1.8	1.7	5.0
	2020F	3.5	3.2	2.3	2.2	1.8	1.7	1.7	4.6
	2021F	3.5	3.0	2.2	2.0	1.7	1.6	1.6	4.4
Dividend yield (%)	2017	3.2	4.3	4.4	4.5	3.2	4.4	1.7	4.1
	2018	3.5	4.3	5.4	5.0	4.2	4.7	3.1	4.4
	2019F	3.9	5.0	6.1	5.3	4.4	5.2	4.4	4.6
	2020F	4.1	5.4	6.6	5.5	4.9	5.8	5.2	4.9
	2021F	4.2	5.8	7.2	5.8	5.3	6.3	6.1	5.2
ROE (%)	2017	9.1	10.2	8.8	8.0	5.8	8.0	7.8	5.7
	2018	9.2	8.8	8.9	8.6	6.8	9.4	8.7	5.0
	2019F	9.3	9.3	9.0	8.6	6.8	7.8	9.9	5.2
	2020F	9.0	8.9	9.1	8.4	6.9	7.7	9.4	5.2
	2021F	8.6	8.6	8.8	8.2	6.8	7.3	8.7	5.2
ROA (%)	2017	0.7	0.8	0.6	0.6	0.4	0.5	0.4	1.7
	2018	0.7	0.7	0.6	0.6	0.5	0.6	0.5	1.5
	2019F	0.7	0.7	0.6	0.6	0.5	0.5	0.7	1.5
	2020F	0.7	0.7	0.6	0.6	0.5	0.5	0.7	1.5
	2021F	0.7	0.7	0.7	0.6	0.5	0.5	0.7	1.5
EPS growth (%)	2017	6.7	45.6	53.1	29.4	-19.6	5.0	25.2	10.7
	2018	8.2	-8.9	9.0	16.8	24.6	26.9	29.2	-10.7
	2019F	9.3	12.6	9.5	5.4	4.1	-11.3	12.4	2.8
	2020F	2.0	3.2	8.2	3.6	6.7	5.7	1.5	4.1
	2021F	2.0	5.5	6.8	4.9	4.6	2.8	2.5	5.6
PPOP margin (%)	2017	1.1	1.1	1.0	1.3	1.2	1.1	1.1	3.5
	2018	1.2	1.1	1.0	1.4	1.3	0.9	1.3	3.8
	2019F	1.2	1.1	1.0	1.3	1.2	1.0	1.3	3.6
	2020F	1.1	1.2	1.1	1.3	1.2	1.1	1.4	3.7
	2021F	1.2	1.2	1.1	1.3	1.3	1.1	1.5	3.8

Note: Based on July 18th closing prices.

Source: Company data, Quantwise, Mirae Asset Daewoo Research estimates

Figure 13. P/B-ROE comparison vs. global peers (FY1)

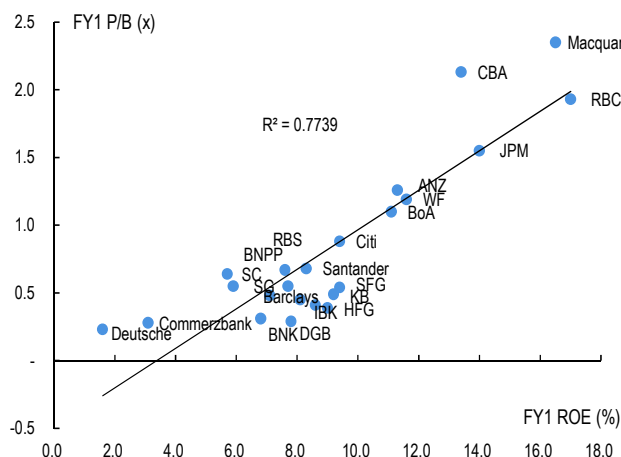
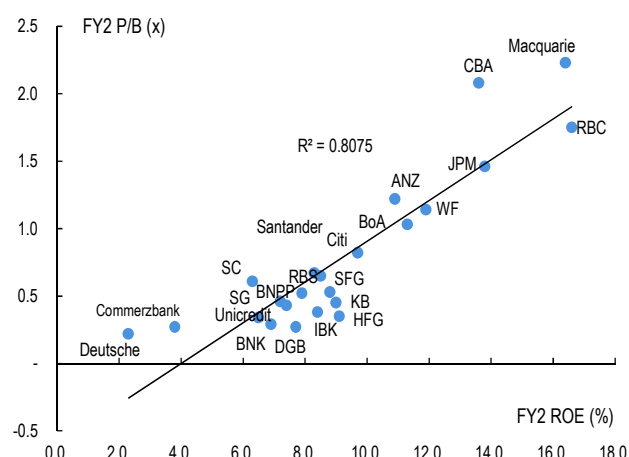


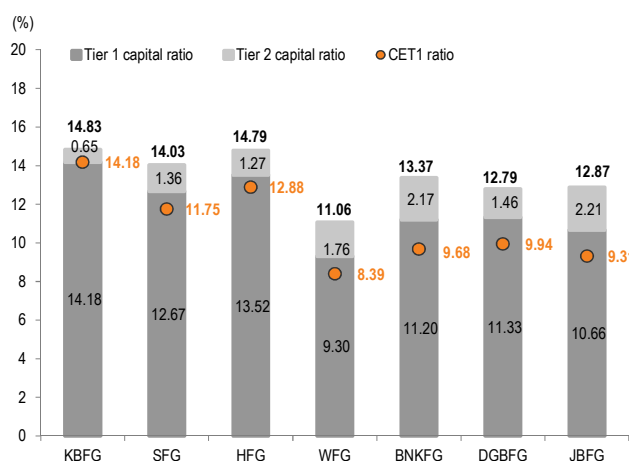
Figure 14. P/B-ROE comparison vs. global peers (FY2)



Notes: FY1 refers to the year ending Dec. 31, 2019 (Sept. 30, 2019 for ANZ; Mar. 31, 2020 for Macquarie; June 30, 2019 for CBA); share prices as of July 12th.
Source: Bloomberg, Mirae Asset Daewoo Research

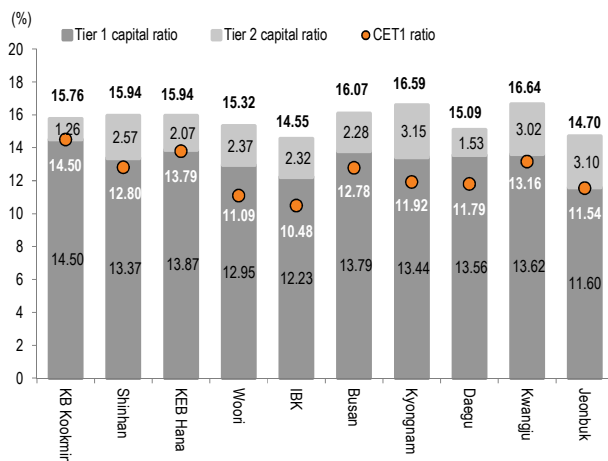
Notes: FY2 refers to the year ending December 31, 2020 (Sept. 31, 2020 for ANZ; Mar. 31, 2021 for Macquarie; June 30, 2020 for CBA); share prices as of July 12th.
Source: Bloomberg, Mirae Asset Daewoo Research

Figure 15. BIS capital ratio by financial group (1Q19)



Source: Company data, FSS, Mirae Asset Daewoo Research

Figure 16. BIS capital ratio by bank (1Q19)



Source: Company data, FSS, Mirae Asset Daewoo Research

SFG to focus on acquiring full ownership of Orange Life Insurance and managing CET1 ratio

Group CET1 ratio fell to 11.75% (-1.33%p YoY, -0.8%p QoQ) at end-1Q19 due to the Orange Life Insurance acquisition (59.15%). In 2Q19, CET1 ratio was likely further weighed down by the inclusion of Asia Trust and SVFC (former PVFC) in consolidated financials and share buybacks. However, we view the decline in CET1 ratio as temporary, given the group's robust earnings-generating power and the mandatory conversion of convertible preferred shares worth W750bn. SFG's strategic investor (IMM Private Equity) will have the option to convert shares one year from the date of issuance through the following four years (May 1, 2020 through April 30, 2023). Any shares that are not converted during that period will automatically be converted to common shares on the first day the period expires. Furthermore, we think SFG can use treasury shares to acquire of the remaining shares of Orange Life Insurance it does not already own. Once full ownership is achieved, we expect CET1 ratio to increase at an accelerating rate, driven by earnings growth. That said, we think SFG is unlikely to meaningfully raise its dividend payout ratio until it acquires the remaining Orange Life Insurance shares.

Based on common shares, SFG's DPS was W1,450 in 2016, W1,450 in 2017, and W1,600 in 2018, which translate to dividend payout ratios of 24.8%, 23.6%, and 23.9%, respectively. Our 2019, 2020, and 2021 DPS forecasts are W1,750, W1,850, and W1,900, respectively, based on common shares. Factoring in preferred shares, we estimate total dividend payout ratio at 24.2% for 2019, 25.0% for 2020, and 25.6% for 2021. Based on the current share price, these figures imply dividend yield of 3.9% for 2019, 4.1% for 2020, and 4.2% for 2021.

Table 6. SFG: Quarterly earnings

(Wbn)	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19F	3Q19F	4Q19F
Net interest income	1,869.2	1,914.7	1,986.8	2,072.2	2,058.8	2,121.4	2,171.8	2,228.1	2,381.5	2,435.6	2,473.4	2,476.1
Net non-interest income	387.6	437.1	454.6	431.7	482.6	513.3	479.4	463.7	479.9	488.9	478.6	479.0
Net other income	-90.2	29.4	-113.4	-195.6	-98.1	-1.6	-214.6	-225.2	-131.8	-138.3	-185.9	-215.6
Total net operating income	2,166.6	2,381.2	2,328.1	2,308.3	2,443.3	2,633.1	2,436.6	2,466.5	2,729.5	2,786.2	2,766.1	2,739.5
SG&A expenses	1,064.8	1,078.4	1,080.6	1,587.5	1,087.0	1,126.4	1,089.2	1,439.0	1,168.4	1,180.0	1,197.9	1,521.9
PPOP	1,101.8	1,302.8	1,247.5	720.8	1,356.3	1,506.7	1,347.4	1,027.5	1,561.2	1,606.2	1,568.2	1,217.7
Provisions	-196.5	147.3	208.1	385.4	179.4	173.8	214.8	170.6	250.8	260.4	219.0	212.4
Operating profit	1,298.3	1,155.5	1,039.4	335.4	1,176.9	1,332.9	1,132.6	856.9	1,310.3	1,345.8	1,349.2	1,005.2
Non-operating income	7.5	34.0	41.1	-115.0	17.1	-24.1	33.7	-59.4	12.2	3.4	19.0	-21.3
Pretax profit	1,305.7	1,189.5	1,080.5	220.5	1,194.0	1,308.8	1,166.3	797.5	1,322.5	1,349.2	1,368.1	983.9
Net profit	997.1	892.0	817.3	211.5	857.5	938.1	847.8	513.3	918.4	929.3	941.5	661.5

Note: Net interest income and net other income differ from the data in SFG's IR materials, as interest expenses in liabilities under insurance contracts, which are booked as non-interest expenses in financial statements, were classified as interest expenses in IR materials.

Source: Company data, Mirae Asset Daewoo Research

Table 7. SFG: Annual earnings

(Wbn)	2012	2013	2014	2015	2016	2017	2018	2019F	2020F	2021F
Net interest income	6,979.7	6,602.9	6,789.8	6,692.9	7,205.4	7,843.0	8,580.1	9,766.6	10,100.4	10,495.6
Net non-interest income	1,543.1	1,386.4	1,469.2	1,621.0	1,565.5	1,711.0	1,939.0	1,926.5	1,949.6	1,992.4
Net other income	39.1	35.1	-191.3	165.3	11.4	-369.7	-539.5	-671.7	-663.6	-650.1
Total net operating income	8,561.9	8,024.3	8,067.6	8,479.2	8,782.3	9,184.2	9,979.5	11,021.3	11,386.4	11,837.9
SG&A expenses	4,061.6	4,202.5	4,462.9	4,475.1	4,508.6	4,811.2	4,741.6	5,068.1	5,201.2	5,318.6
PPOP	4,500.3	3,821.7	3,604.8	4,004.2	4,273.8	4,373.0	5,238.0	5,953.2	6,185.2	6,519.3
Provisions	1,322.4	1,184.2	949.9	1,031.0	1,165.1	544.4	738.6	942.7	954.3	1,051.3
Operating profit	3,178.0	2,637.6	2,654.8	2,973.1	3,108.6	3,828.6	4,499.4	5,010.6	5,231.0	5,468.0
Non-operating income	52.7	44.6	212.8	167.4	61.8	-32.4	-32.8	13.3	0.5	-0.2
Pretax profit	3,230.6	2,682.1	2,867.6	3,140.6	3,170.5	3,796.2	4,466.6	5,023.8	5,231.4	5,467.8
Net profit	2,321.9	1,902.8	2,081.1	2,367.2	2,774.8	2,917.9	3,156.7	3,450.7	3,569.3	3,712.7

Note: Net interest income and net other income differ from the data in SFG's IR materials, as interest expenses in liabilities under insurance contracts, which are booked as non-interest expenses in financial statements, were classified as interest expenses in IR materials.

Source: Company data, Mirae Asset Daewoo Research

Shinhan Financial Group (055550 KS/Buy/TP: W60,000)

Comprehensive Income Statement (Summarized)

Year-end 12 (Wbn)	12/18	12/19F	12/20F	12/21F
Interest income	13,572	15,647	16,065	16,669
Interest expense	4,992	5,881	5,965	6,173
Net interest income	8,580	9,767	10,100	10,496
Net fees and commissions	1,939	1,926	1,950	1,992
Net other non-interest income	-540	-672	-664	-650
Total net operating income	9,980	11,021	11,386	11,838
G&A expenses	4,742	5,068	5,201	5,319
PPOP	5,238	5,953	6,185	6,519
Total provision expenses	739	943	954	1,051
Operating profit	4,499	5,011	5,231	5,468
Net non-operating income	-33	13	0	0
Income before income taxes	4,467	5,024	5,231	5,468
Income tax expense	1,268	1,375	1,439	1,504
Net profit	3,198	3,649	3,793	3,964
Net profit (ex. minority interest)	3,157	3,451	3,569	3,713
Normalized net profit	3,157	3,451	3,569	3,713
Core income	10,519	11,693	12,050	12,488
Core PPOP	5,778	6,625	6,849	7,169

DuPont analysis (%)

Interest income	3.06	3.15	2.96	2.96
Interest expense	1.13	1.18	1.10	1.10
Net interest income	1.94	1.97	1.86	1.86
Net commissions income	0.44	0.39	0.36	0.35
Net other non-interest income	-0.12	-0.14	-0.12	-0.12
Total net operating profit	2.25	2.22	2.10	2.10
G&A expenses	1.07	1.02	0.96	0.94
PPOP	1.18	1.20	1.14	1.16
Total provision expenses	0.17	0.19	0.18	0.19
Net non-operating income	-0.01	0.00	0.00	0.00
Income before income taxes	1.01	1.01	0.96	0.97
Income tax expense	0.29	0.28	0.27	0.27
Net profit (non-controlling)	0.01	0.04	0.04	0.05
ROA	0.71	0.70	0.66	0.66
Leverage (x)	12.9	13.4	13.6	13.0
ROE	9.21	9.31	8.96	8.59

Asset quality (%)

NPL ratio	0.53	0.49	0.45	0.42
Broad NPL ratio	1.30	1.27	1.23	1.19
NPL coverage ratio	301.8	322.0	331.2	337.1
Reserves to total credits	1.6	1.6	1.5	1.4
Credit cost (% of total loans)	0.25	0.30	0.29	0.31
Credit cost (% of total credit)	0.26	0.31	0.30	0.32

Per share items (W)

EPS (reported)	6,657	7,277	7,424	7,452
EPS (normalized)	6,657	7,277	7,424	7,452
BVPS	75,354	80,981	83,967	88,725
DPS (common share)	1,600	1,750	1,850	1,900
PPOP/ share	11,046	12,554	12,866	13,085

Source: Company data, Mirae Asset Daewoo Research estimates

Statement of Financial Condition (Summarized)

Year-end 12 (Wbn)	12/18	12/19F	12/20F	12/21F
Cash & dues	17,416	23,867	24,548	25,251
Securities	84,257	98,255	101,166	104,167
Net loans and receivables	299,609	316,054	329,618	343,231
Tangible assets	3,479	9,436	9,691	9,954
Other assets	54,847	86,242	88,323	90,461
Total assets	459,608	533,855	553,346	573,064
Deposits	265,000	281,779	292,114	302,571
Borrowings	29,819	30,735	30,824	30,951
Debentures	63,228	71,156	72,384	73,652
Other liabilities	64,903	109,214	113,947	117,671
Total liabilities	422,949	492,884	509,269	524,844
Capital stock	2,645	2,732	2,732	2,732
Hybrid securities	1,532	1,532	1,532	1,532
Capital surplus	9,895	10,581	10,581	10,581
Retained earnings	22,959	24,975	27,859	31,749
Capital adjustments	-553	-964	-964	-964
Other comprehensive income	-746	-454	-454	-454
Non-controlling interests	926	2,569	2,793	3,044
Total shareholders' equity	36,659	40,971	44,078	48,220

Key ratios (%)

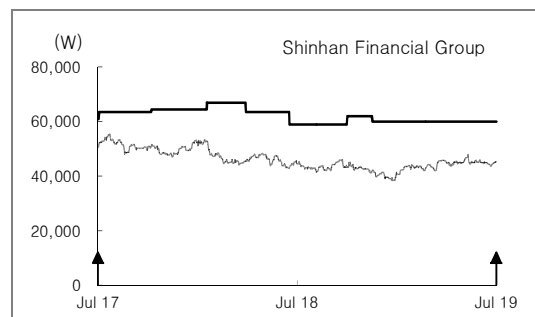
Growth (YoY)				
W loan growth (Bank)	7.2	5.2	4.3	4.2
Net loans & receivables growth	8.7	5.5	4.3	4.1
Deposit growth	6.2	6.3	3.7	3.6
Shareholders' equity growth	8.8	11.8	7.6	9.4
Total assets growth	7.8	16.2	3.7	3.6
Net interest income growth	9.4	13.8	3.4	3.9
Net fee income growth	13.3	-0.6	1.2	2.2
PPOP growth	19.8	13.7	3.9	5.4
Operating profit growth	17.5	11.4	4.4	4.5
Net profit growth	8.2	9.3	3.4	4.0
Profitability				
Net interest spread (Bank)	1.87	1.83	1.80	1.80
Net interest margin (Bank)	1.62	1.58	1.55	1.55
PPOP margin	1.2	1.2	1.1	1.2
ROA	0.7	0.7	0.7	0.7
ROE	9.2	9.3	9.0	8.6
Liquidity				
W LDR (excl. CDs) (Bank)	99.2	97.3	97.3	97.3
Loans to assets	65.2	59.2	59.6	59.9
Capital adequacy				
Total CAR	14.9	14.4	14.7	15.3
Tier 1 CAR	13.4	13.3	13.8	14.6
Tier 2 CAR	1.5	1.1	0.9	0.7
Operating efficiency				
Cost to income	47.5	46.0	45.7	44.9
Cost to assets	1.0	0.9	0.9	0.9
Dividend				
Payout ratio	23.9	24.2	25.0	25.6

APPENDIX 1

Important Disclosures & Disclaimers

2-Year Rating and Target Price History

Company (Code)	Date	Rating	Target Price
Shinhan Financial Group (055550)	12/04/2018	Buy	60,000
	10/19/2018	Buy	62,000
	07/05/2018	Buy	59,000
	04/16/2018	Buy	63,500
	02/08/2018	Buy	67,000
	02/08/2018	Buy	63,500
	02/04/2018	Buy	67,000
	10/25/2017	Buy	64,500
	07/21/2017	Buy	63,500
	04/21/2017	Buy	61,000



Stock Ratings

Buy	: Relative performance of 20% or greater
Trading Buy	: Relative performance of 10% or greater, but with volatility
Hold	: Relative performance of -10% and 10%
Sell	: Relative performance of -10%

Industry Ratings

Overweight	: Fundamentals are favorable or improving
Neutral	: Fundamentals are steady without any material changes
Underweight	: Fundamentals are unfavorable or worsening

Ratings and Target Price History (Share price (—), Target price (—), Not covered (≡), Buy (▲), Trading Buy (■), Hold (●), Sell (◆))

* Our investment rating is a guide to the relative return of the stock versus the market over the next 12 months.

* Although it is not part of the official ratings at Mirae Asset Daewoo Co., Ltd., we may call a trading opportunity in case there is a technical or short-term material development.

* The target price was determined by the research analyst through valuation methods discussed in this report, in part based on the analyst's estimate of future earnings.

* The achievement of the target price may be impeded by risks related to the subject securities and companies, as well as general market and economic conditions.

Equity Ratings Distribution & Investment Banking Services

	Buy	Trading Buy	Hold	Sell
Equity Ratings Distribution	83.14%	8.72%	8.14%	0.00%
Investment Banking Services	77.78%	11.11%	11.11%	0.00%

* Based on recommendations in the last 12-months (as of June 30, 2019)

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