

United Overseas Bank (UOB SP)

Onwards And Upwards

BUY

Share Price SGD 28.10
 12m Price Target SGD 31.08 (+11%)
 Previous Price Target SGD 29.33

ROE to recover; EPS and TP raised

We believe UOB can generate robust earnings in a cyclical upturn. We raised FY18-20E net profits by 2-5% mainly on higher loan growth and non-interest income assumptions. With the change in our EPS estimates, our assumed sustainable ROE is now 12.7% (12.1% previously), with COE of 10.1% and a growth rate of 3.5% (both unchanged). Accordingly, our TP is raised 6% to SGD31.08, pegged to ~1.4x FY18E P/BV (from 1.3x), 0.5SD above its historical mean of 1.3x to reflect higher forecast ROEs. Maintain BUY.

Healthy momentum

We raised FY18-20E loan growth slightly to ~9-10% from 9-9.5% based on an average multiplier between its loan growth and Singapore's GDP growth of 2.6x. A rebound in Singapore's property market can benefit UOB as 50% of its total loan book is related to housing and building and construction (B&C) loan vs 42% for peers. Also, we remain positive on UOB's capability for further WM fee growth. We think UOB's wealth franchise is underappreciated. Its organic AUM grew decently at a 7-year CAGR of 12% (vs peers' 15-22%). FY17 saw solid 12% YoY growth in AUM.

Scope for higher dividends

With earnings momentum likely to continue, strong fully-loaded CET1 capital at 14.7% and consistent improvement in return on risk-weighted assets in recent quarters, we think there is scope for capital management and higher dividends. We raised our FY18-20E DPS forecast to SGD1.20-1.40/sh (from SGD1/sh). This implies payout ratio of 42-46%.

Maintain BUY

We like UOB's disciplined pricing strategy and its sensitivity to re-pricing intervals. Risks to our BUY thesis are: 1) lower income; and 2) higher provisions.

FYE Dec (SGD m)	FY16A	FY17A	FY18E	FY19E	FY20E
Operating income	8,061	8,851	10,037	11,107	12,325
Pre-provision profit	4,365	4,824	5,734	6,532	7,458
Core net profit	3,004	3,299	4,259	4,821	5,482
Core EPS (SGD)	1.8	2.0	2.6	2.9	3.4
Core EPS growth (%)	(5.2)	9.8	29.1	13.2	13.7
Net DPS (SGD)	0.7	1.0	1.2	1.3	1.4
Core P/E (x)	15.3	13.9	10.8	9.5	8.4
P/BV (x)	1.5	1.3	1.2	1.2	1.1
Net dividend yield (%)	2.5	3.6	4.3	4.6	5.0
Book value (SGD)	18.77	21.20	22.49	24.08	25.97
ROAE (%)	10.1	10.1	11.9	12.7	13.4
ROAA (%)	0.9	0.9	1.1	1.2	1.3
Consensus net profit	-	-	3,856	4,300	4,623
MKE vs. Consensus (%)	-	-	12.9	14.3	20.6

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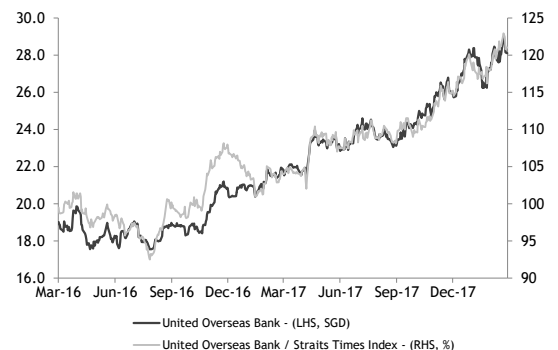
Statistics

52w high/low (SGD)	28.99/21.47
3m avg turnover (USDm)	54.1
Free float (%)	77.5
Issued shares (m)	1,615
Market capitalisation	SGD45.4B
	USD34.4B

Major shareholders:

WEE FAMILY	18.1%
LIEN FAMILY	5.2%

Price Performance



	-1M	-3M	-12M
Absolute (%)	3	8	28
Relative to index (%)	2	5	16

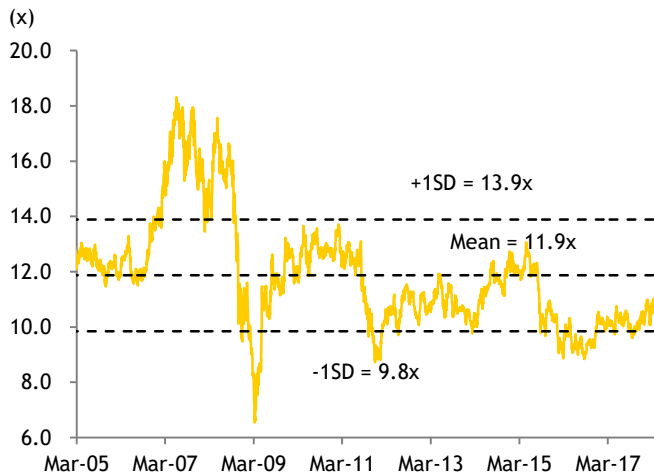
Source: FactSet

Fig 1: Revisions to estimates

UOB	Revised			Original		
	2018E	2019E	2020E	2018E	2019E	2020E
(SGD m)						
Net interest income	6,321.8	6,978.6	7,728.7	6,290.2	6,915.2	7,631.4
Non-interest income	3,715.6	4,128.0	4,596.5	3,644.0	3,979.6	4,340.4
Total income	10,037.4	11,106.6	12,325.2	9,934.2	10,894.9	11,971.8
Expenses	(4,303.1)	(4,574.5)	(4,867.5)	(4,303.1)	(4,574.5)	(4,867.5)
Provisions	(522.2)	(639.3)	(764.5)	(516.4)	(627.3)	(742.3)
Net profit [^]	4,259.4	4,821.4	5,481.9	4,179.5	4,657.6	5,210.3
Revisions (%)						
Net interest income	0.5	0.9	1.3			
Non-interest income	2.0	3.7	5.9			
Total income	1.0	1.9	3.0			
Expenses	-	-	-			
Provisions	1.1	1.9	3.0			
Net profit [^]	1.9	3.5	5.2			

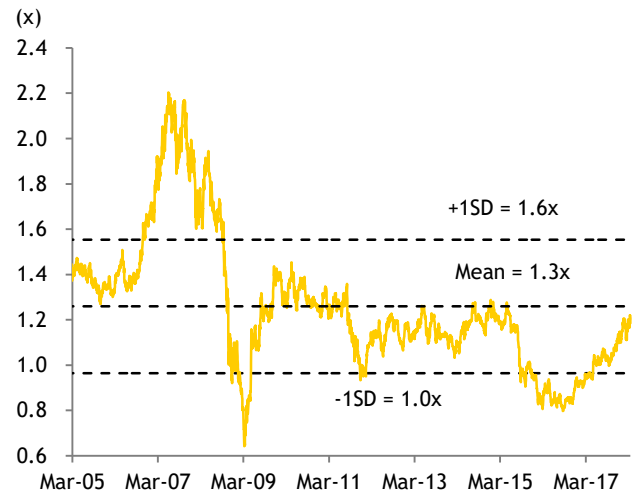
Source: Maybank Kim Eng. [^]Net profit excludes one-offs and preference share dividends

Fig 2: UOB's 12M forward rolling PER band



Source: Bloomberg, Maybank Kim Eng

Fig 3: UOB's 12M forward rolling P/BV band

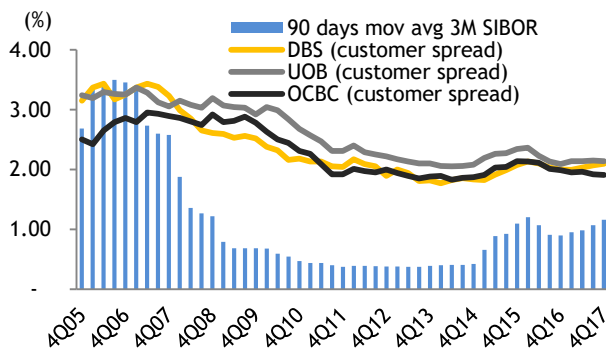


Source: Bloomberg, Maybank Kim Eng

Value Proposition

- Largest SME lender, reflecting its Chinese roots and legacy relationships, resulting in higher lending yields than peers.
- Corporate culture empowers branch managers to support SMEs in the heartlands, cultivating and fortifying relationships - a differentiating factor.
- Conservative, focused on traditional banking. Headed by founding family, which is not inclined to make aggressive overseas or treasury bets. Works well for harsh landscape.
- Strengthening regional footprint - Indonesia, Thailand, Malaysia and Hong Kong. Focus on Indonesia and consumer.
- But Goldilocks era (2010-2014) of low credit costs and asset expansion may be over.

UOB's customer spreads at 2.14% in 4Q17

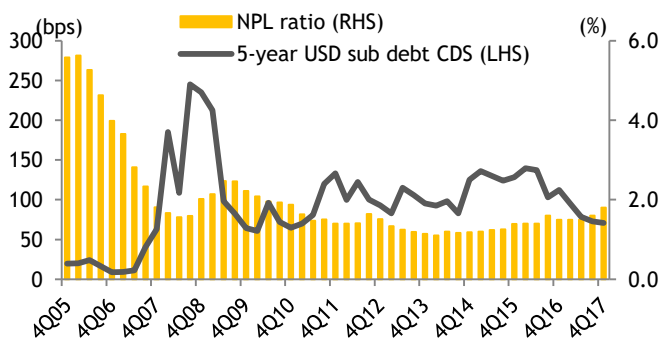


Source: Bloomberg, Companies.

Financial Metrics

- Asset quality: 1.8% NPL ratio in FY17. Higher NPL ratio seen in transport sector at 12.9% and Indonesia at 6.5%.
- Fully-loaded CET1 was 14.7% as at 4Q17, above management's comfort level of 12.5%. See scope for capital management and dividend upside.
- Expect -9-10% net loan growth in FY18-20E.
- Expect FY18/19/20E NIMs at 1.83%/1.87%/1.92%.
- Cost of capital will be a major consideration for the sector. Contagion risks, which may be reflected in its corporate papers or CDS, ought to be carefully watched.

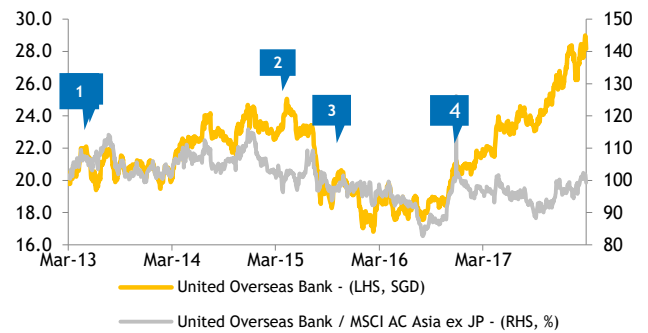
NPL ratio followed CDS spreads with a lag



Source: Bloomberg, Company

Price Drivers

Historical share price



Source: FactSet, Maybank Kim Eng

1. +20% broad-based rebound in 2012 core PATMI.
2. Record earnings with robust lending and asset resilience.
3. Weaker-than-expected 2H15, sharp CNY devaluation in August and O&G/commodity NPL worries.
4. Share price rallied on positive sentiment from interest rate hikes, USD strength and economic recovery. Risks from O&G abated.

Swing Factors

Upside

- Sharp and sustained rebound in commodity prices ease concerns about global risks.
- Ability to re-price assets at higher interest rates, widening credit spreads.
- Proactive restructuring of loans allows asset quality to hold up better than expected, with no major credit slippages.
- Higher demand for domestic mortgages from easing of property-cooling measures.

Downside

- Asset-quality deterioration becomes a systemic problem, especially if job losses in Singapore become pervasive and hurt the mortgage portfolio.
- Shocks in the fixed-income portfolio.
- Lack of liquidity of a funding currency.
- Succession issues.
- Major changes in the competitive banking landscape in Singapore that result in the emergence of a dominant financial institution.
- Translational losses from MYR/IDR depreciation.
- Capital raising by any institution in sector.

FYE 31 Dec	FY16A	FY17A	FY18E	FY19E	FY20E
Key Metrics					
Core P/E (x)	15.3	13.9	10.8	9.5	8.4
Core FD P/E (x)	15.3	13.9	10.8	9.5	8.4
P/BV (x)	1.5	1.3	1.2	1.2	1.1
P/NTA (x)	1.7	1.5	1.4	1.3	1.2
Net dividend yield (%)	2.5	3.6	4.3	4.6	5.0

INCOME STATEMENT (SGD m)

Interest income	8,290.5	9,077.0	10,367.6	11,569.1	12,967.2
Interest expense	(3,299.8)	(3,548.0)	(4,045.8)	(4,590.4)	(5,238.5)
Net interest income	4,990.8	5,529.0	6,321.8	6,978.6	7,728.7
Net insurance income	0.0	0.0	0.0	0.0	0.0
Net fees and commission	1,930.6	2,161.0	2,457.5	2,759.2	3,091.7
Other income	1,139.9	1,161.0	1,258.1	1,368.8	1,504.8
Total non-interest income	3,070.5	3,322.0	3,715.6	4,128.0	4,596.5
Operating income	8,061.3	8,851.0	10,037.4	11,106.6	12,325.2
Staff costs	(2,050.0)	(2,224.0)	(2,344.4)	(2,462.1)	(2,586.0)
Other operating expenses	(1,646.5)	(1,803.0)	(1,958.8)	(2,112.4)	(2,281.5)
Operating expenses	(3,696.5)	(4,027.0)	(4,303.1)	(4,574.5)	(4,867.5)
Pre-provision profit	4,364.8	4,824.0	5,734.3	6,532.1	7,457.7
Loan impairment allowances	(593.8)	(727.0)	(522.2)	(639.3)	(764.5)
Other allowances	0.0	0.0	0.0	0.0	0.0
Associates & JV income	5.9	110.0	115.5	121.3	127.3
Pretax profit	3,776.9	4,207.0	5,327.6	6,014.0	6,820.6
Income tax	(669.0)	(800.0)	(959.0)	(1,082.5)	(1,227.7)
Minorities	(11.7)	(16.0)	(16.8)	(17.6)	(18.5)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	3,096.3	3,391.0	4,351.8	4,913.9	5,574.3
Core net profit	3,003.9	3,298.6	4,259.4	4,821.4	5,481.9
Preferred Dividends	92.4	92.4	92.4	92.4	92.4

BALANCE SHEET (SGD m)

Cash & deposits with banks	40,032.9	52,181.0	53,746.4	55,358.8	57,019.6
Sec. under resale agreements	0.0	0.0	0.0	0.0	0.0
Derivatives financial assets	6,981.5	5,292.8	5,398.7	5,506.7	5,616.8
Dealing securities	5,489.8	4,276.6	4,866.7	5,048.6	5,237.8
Available-for-sale securities	8,462.6	9,314.2	9,314.2	9,314.2	9,314.2
Investment securities	18,330.0	15,424.2	15,970.0	16,536.3	17,123.9
Loans & advances	221,733.7	232,212.0	254,899.1	278,974.3	306,550.9
Central bank deposits	24,322.1	26,625.0	28,916.1	31,388.4	34,175.7
Investment in associates/JVs	1,108.9	1,194.0	1,205.9	1,218.0	1,230.2
Insurance assets	0.0	0.0	0.0	0.0	0.0
Fixed assets	2,989.8	3,059.0	3,104.9	3,151.5	3,198.7
Intangible assets	4,151.0	4,142.0	4,142.0	4,142.0	4,142.0
Other assets	6,425.3	4,871.2	4,631.5	4,554.6	4,458.5
Total assets	340,027.6	358,592.0	386,195.5	415,193.3	448,068.3
Deposits from customers	255,314.0	272,765.0	296,236.4	321,564.6	350,119.6
Deposits from banks & FIs	11,855.2	11,440.0	11,726.0	12,136.4	12,682.5
Derivatives financial instruments	6,837.1	5,962.2	6,051.6	6,142.4	6,234.5
Subordinated debt	5,926.0	4,827.0	4,827.0	4,827.0	4,827.0
Other securities in issue	16,541.0	16,674.9	17,109.9	17,557.8	18,019.2
Other borrowings	5,853.6	5,853.6	5,853.6	5,853.6	5,853.6
Insurance liabilities	0.0	0.0	0.0	0.0	0.0
Other liabilities	6,836.7	6,208.8	7,421.3	7,537.4	7,656.4
Total liabilities	309,163.5	323,731.5	349,225.8	375,619.2	405,392.9
Share capital	1,635.7	1,662.7	1,662.7	1,662.7	1,662.7
Reserves	29,060.0	33,009.8	35,118.4	37,721.0	40,820.5
Shareholders' funds	30,695.6	34,672.5	36,781.0	39,383.6	42,483.1
Preference shares	0.0	0.0	0.0	0.0	0.0
Minority interest	168.6	187.0	188.7	190.4	192.3
Total equity	30,864.2	34,859.5	36,969.7	39,574.1	42,675.4
Total liabilities & equity	340,027.6	358,592.0	386,195.5	415,193.3	448,068.3

FYE 31 Dec	FY16A	FY17A	FY18E	FY19E	FY20E
Key Ratios					
Growth (%)					
Net interest income	1.3	10.8	14.3	10.4	10.7
Non-interest income	(1.6)	8.2	11.8	11.1	11.3
Operating expenses	2.8	8.9	6.9	6.3	6.4
Pre-provision profit	(1.9)	10.5	18.9	13.9	14.2
Core net profit	(3.2)	9.8	29.1	13.2	13.7
Gross loans	8.8	4.7	9.7	9.4	9.9
Customer deposits	6.1	6.8	8.6	8.5	8.9
Total assets	7.6	5.5	7.7	7.5	7.9
Profitability (%)					
Non-int. income/Total income	38.1	37.5	37.0	37.2	37.3
Average lending yields	2.84	2.91	3.00	3.10	3.21
Average cost of funds	1.16	1.18	1.26	1.32	1.40
Net interest margin	1.71	1.77	1.83	1.87	1.92
Cost/income	45.9	45.5	42.9	41.2	39.5
Liquidity (%)					
Loans/customer deposits	86.8	85.1	86.0	86.8	87.6
Asset quality (%)					
Net NPL	1.5	1.8	1.4	1.5	1.6
Gross NPL	1.5	1.8	1.4	1.5	1.6
(SP+GP)/average gross loans	0.3	0.3	0.2	0.2	0.3
Loan loss coverage	116.3	90.9	112.4	104.2	98.4
Capital adequacy (%)					
CET1	13.1	16.2	16.2	16.5	16.6
Tier 1 capital	13.1	16.2	16.2	16.5	16.6
Risk-weighted capital	16.2	18.7	18.4	18.5	18.5
Returns (%)					
ROAE	10.1	10.1	11.9	12.7	13.4
ROAA	0.9	0.9	1.1	1.2	1.3
Shareholders equity/assets	9.0	9.7	9.5	9.5	9.5

Source: Company; Maybank

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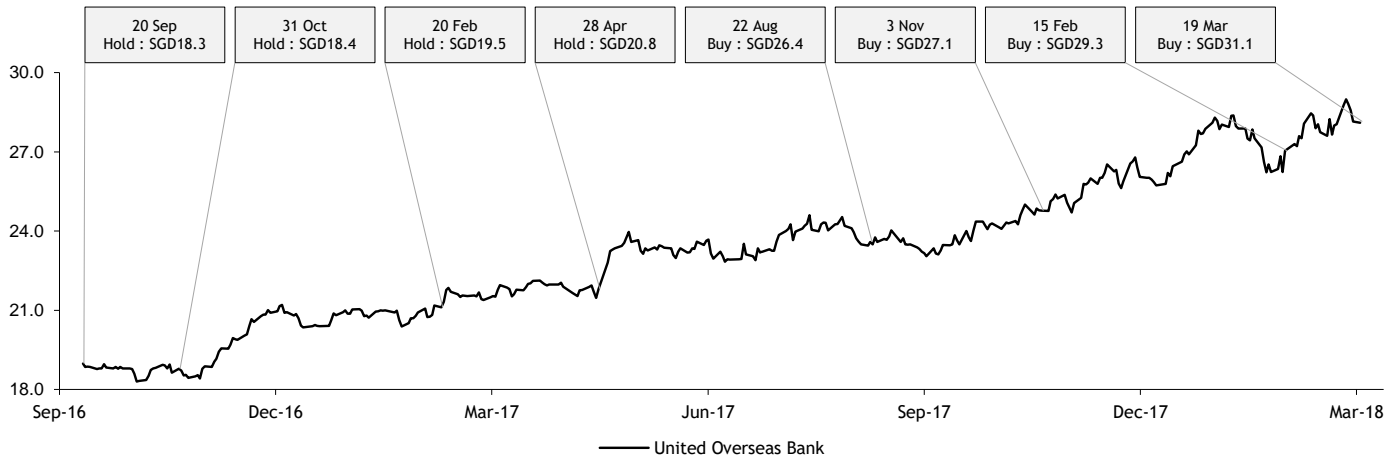
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