

1 November 2019

Financial Services | Banks

United Overseas Bank (UOB SP)

Buy (Maintained)

3Q19 YoY NIM Squeeze, But Good Non-II; BUY

Target Price (Return) SGD29.50 (+10%)
Price: SGD26.83
Market Cap: USD32,528m
Avg Daily Turnover (SGD/USD) 53m/39m

- **Maintain BUY with unchanged GGM-derived TP of SGD29.50, 10% upside plus c.5% yield, based on 1.26x 2020F P/BV.** Our long-term ROE assumption is 12.7% vs 9M19's 11.9%, which factors in growing non-interest income offset by narrowing NIM ahead. 9M19 net profit rose 8% YoY to SGD3,338m, representing 77% of our pre-results FY19 forecast. UOB remains our Top Pick among Singapore banks. This report is an update post analyst teleconference.

- **Strong YoY improvement for 3Q19 other non-interest income.** 3Q19 net profit rose 8% YoY but fell 4% QoQ. The YoY improvement was partly due to net gain from investment securities, and to wealth management fees (assets under management were up 10% YoY). We raised our 2019F overall net profit by 1%.

- **Management guided 2020 NIM to be 5-10 bps narrower YoY.** 3Q19 NIM of 1.77% was 4bps narrower both QoQ and YoY. The decrease was due to lower benchmark interest rates and short term placement in the securities market. Management is hopeful of maintaining current NIM in 4Q19. We forecast 2019 NIM of 1.79% vs 9M19's 1.79%. Management guided for 2020 NIM to be 5-10 bps narrower YoY, based on end-2020 3-month SIBOR of 1.4-1.5%, and UOB's intention to push hard to grow its CASA (to lower cost of funds). We forecast 2020 NIM of 1.73%.

- **Management guided 2020 loan growth of mid single-digits.** This is weaker than 3Q19's YoY loan expansion of 8%. We forecast 2020 loan expansion of 4.5%.

- **Management guided for 2019 CIR of 44%.** 3Q19 CIR was 44.2%, higher QoQ as UOB continued to invest in talent and technology. 3Q19 IT-related costs (11% share of total costs) were up 17% YoY.

- **TP based on GGM-derived 1.26x 2020F P/BV.** 3Q19's ROE of 11.8% was higher than 2018's 11.3%. Our valuation for UOB is based on a long-term ROE assumption of 12.7%. This yields a 2020F target P/BV of 1.26x, from which we derive our TP of SGD29.50. UOB is attractive as its current 2020F P/BV of 1.15x is also lower than the 6-year average of 1.22x.

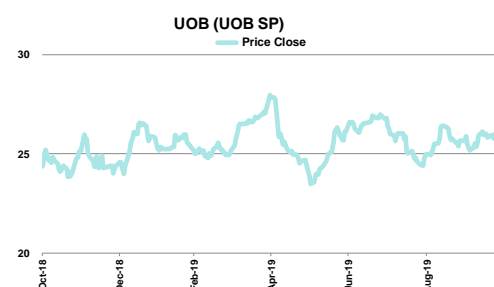
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	8.9	3.5	(0.9)	(3.9)	11.5
Relative	4.3	0.7	3.3	1.8	3.3
52-wk Price low/high (SGD)	23.39 – 27.76				



Source: Bloomberg

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Reported net profit (SGDm)	3,390	4,008	4,353	4,347	4,419
Recurring net profit (SGDm)	3,390	4,008	4,353	4,347	4,419
Recurring net profit growth (%)	9.5	18.2	8.6	(0.1)	1.7
Recurring EPS (SGD)	2.06	2.41	2.61	2.61	2.65
BVPS (SGD)	20.37	21.31	22.25	23.43	24.59
DPS (SGD)	1.00	1.20	1.30	1.40	1.45
Recurring P/E (x)	13.1	11.1	10.3	10.3	10.1
P/B (x)	1.32	1.26	1.21	1.15	1.09
Dividend Yield (%)	3.7	4.5	4.8	5.2	5.4
Return on average equity (%)	10.2	11.3	11.9	11.7	11.8
Return on average assets (%)	0.98	1.07	1.09	1.04	1.02

Source: Company data, RHB

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Financial Exhibits

Financial model updated on: 2019-11-01

Asia	Financial summary	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Singapore	EPS (SGD)	1.99	2.34	2.58	2.58	2.62
Financials	Core EPS (SGD)	2.06	2.41	2.61	2.61	2.65
UOB	DPS (SGD)	1.00	1.20	1.30	1.40	1.45
UOB SP	BVPS (SGD)	20.37	21.31	22.25	23.43	24.59
BUY						
Valuation basis	Valuation metrics	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Gordon Growth Methodology (GGM)	Recurring P/E (x)	13.1	11.1	10.3	10.3	10.1
	P/B (x)	1.32	1.26	1.21	1.15	1.09
	Dividend yield (%)	3.7	4.5	4.8	5.2	5.4
Key drivers	Balance sheet (SGDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Our net profit forecast is most sensitive to	Gross loans & advances	236,028	261,707	276,001	288,547	301,675
i. Changes in NIM;	Loan impairment allowances	3,816	3,080	3,667	3,958	4,279
ii. Non-interest income growth;	Net loans & advances	232,212	258,627	272,334	284,589	297,396
iii. Credit costs.	Total assets	358,592	388,092	408,153	424,142	442,564
	Deposits from customers	272,765	293,186	305,207	319,551	334,570
	Total liabilities	321,555	350,281	368,688	382,683	399,046
	Shareholders' funds	36,850	37,623	39,258	41,222	43,241
	Total equity	37,037	37,811	39,465	41,460	43,517
Key risks	Income statement (SGDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
i. Higher impairment charges;	Net interest income	5,528	6,220	6,598	6,675	6,864
ii. Weaker NIMs;	Non-interest income	3,034	2,897	3,567	3,787	4,104
iii. Softer non-IL.	Operating income	8,563	9,116	10,165	10,462	10,968
	Overhead expenses	3,739	4,003	4,529	4,745	5,124
	Pre-provision operating profit	4,824	5,113	5,636	5,717	5,844
	Loan impairment allowances	727	393	439	550	580
	Other impairment allowances	0	0	0	0	0
	Pretax profit	4,207	4,826	5,244	5,239	5,345
	Reported net profit	3,390	4,008	4,353	4,347	4,419
	Recurring net profit	3,390	4,008	4,353	4,347	4,419
Company Profile	Profitability	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
UOB is the third largest Singapore bank by global assets. Its overseas operations are focused in ASEAN.	ROA (%)	0.98	1.07	1.09	1.04	1.02
	ROE (%)	10.2	11.3	11.9	11.7	11.8
	Yield on IEAs (%)	2.91	3.26	3.52	3.43	3.38
	Cost of funds (%)	1.18	1.51	1.78	1.76	1.73
	Net interest margin (%)	1.77	1.82	1.79	1.73	1.72
	Non-IL / Total income (%)	35.4	31.8	35.1	36.2	37.4
	CIR (%)	43.7	43.9	44.6	45.4	46.7
	Credit cost (bps)	28	16	17	20	20
	PIOP growth (%)	10.5	6.0	10.2	1.4	2.2
	Net profit growth (%)	9.7	18.4	8.6	-0.1	1.7
	Asset quality	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	Gross impaired loans/Gross loans (%)	1.8	1.5	1.5	1.5	1.6
	Loan loss coverage ratio (%)	90.9	87.3	84.7	84.6	86.3
	NPL formation (bps)	124.0	74.0	70.5	71.0	72.6
	Liquidity	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	Loan growth (%)	4.7	11.4	5.3	4.5	4.5
	Customer deposits growth (%)	6.8	7.5	4.1	4.7	4.7
	LDR (%)	85.1	88.2	89.2	89.1	88.9
	Capital	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	CET1 ratio (%)	15.1	13.9	14.1	14.9	15.4
	Tier-1 ratio (%)	16.2	14.9	15.1	15.4	16.0
	Total capital ratio (%)	18.7	17.0	17.1	17.4	17.9

Source: Company data, RHB

Figure 1: UOB's financial data

FYE Dec (SGDm)	FY17	FY18	FY19F	FY20F	FY21F
Net Interest Income	5,528	6,220	6,598	6,675	6,864
Non-interest Income	3,034	2,897	3,567	3,787	4,104
- Dividends	23	27	49	35	37
- Fee & Commission Income	1,873	1,967	2,103	2,255	2,501
- Rental Income	119	119	113	119	121
- Other Operating Income	1,019	784	1,302	1,378	1,445
Total operating income	8,563	9,116	10,165	10,462	10,968
Operating Expenses	(3,739)	(4,003)	(4,529)	(4,745)	(5,124)
Operating Profit	4,824	5,113	5,636	5,717	5,844
Provisions	(727)	(393)	(439)	(550)	(580)
Associates	110	106	47	72	81
Pre-tax profit	4,207	4,826	5,244	5,239	5,345
Taxation	(800)	(805)	(876)	(876)	(909)
Profit after tax	3,407	4,021	4,368	4,363	4,436
Minorities	(16)	(13)	(15)	(16)	(17)
Net Profit	3,390	4,008	4,353	4,347	4,419
EPS (SGD¢)	199.0	234.0	258.2	257.7	261.7
Book value (SGD)	20.37	21.31	22.25	23.43	24.59
Revalued book (SGD)	23.18	24.19	25.13	26.31	27.46
P&L ratios (%)					
ROE (Avg)	10.2	11.3	11.9	11.7	11.8
Net Interest Margin	1.77	1.82	1.79	1.73	1.72
Net interest income / income	64.6	68.2	64.9	63.8	62.6
Operating Expenses / income	43.7	43.9	44.6	45.4	46.7
P&L YoY change (%)					
Net Interest Income	10.8	12.5	6.1	1.2	2.8
Non-interest income	(1.2)	(4.5)	23.1	6.2	8.4
Fee & commission income	(3.0)	5.0	6.9	7.2	10.9
Total income	6.2	6.5	11.5	2.9	4.8
Operating expenses	1.2	7.1	13.1	4.8	8.0
Operating profit	10.5	6.0	10.2	1.4	2.2
Provisions	22.4	(45.9)	11.7	25.3	5.5
Pre-tax Profit	11.4	14.7	8.7	(0.1)	2.0
Net Profit	9.7	18.4	8.6	(0.1)	1.7
BS data (SGDm)					
Assets	358,592	388,092	408,153	424,142	442,564
Non-bank loans	232,212	258,627	272,334	284,589	297,396
Customer deposit	272,765	293,186	305,207	319,551	334,570
Non-performing assets	4,389	4,166	4,330	4,676	4,961
Cumulative loan loss provisions	3,990	3,636	3,667	3,958	4,279
Balance sheet ratios (%)					
Loans deposit ratio	85.1	88.2	89.2	89.1	88.9
Non-bank loans growth (YoY%)	4.7	11.4	5.3	4.5	4.5
Customer deposit growth (YoY%)	6.8	7.5	4.1	4.7	4.7
NPL / Non-bank loans	1.8	1.5	1.5	1.5	1.6
Loan loss coverage	90.9	87.3	84.7	84.6	86.3
Total CAR	18.7	17.0	17.1	17.4	17.9
Tier 1 CAR	16.2	14.9	15.1	15.4	16.0

Source: Bloomberg, RHB

Figure 2: 3Q19 results summary

FYE Dec (SGDm)	3Q18	2Q19	3Q19	QoQ%	YoY%	Comments
Net Interest Income	1,599	1,653	1,687	2.1	5.5	QoQ, net loans rose 1%. However, NIM narrowed by 4bps QoQ to 1.77%. The NII QoQ rise came from additional day count and asset growth.
Non-interest Income	727	931	922	(1.0)	26.8	
Total operating income	2,327	2,584	2,609	1.0	12.1	
Operating Expenses	(1,010)	(1,130)	(1,154)	2.1	14.3	3Q19 CIR of 44.2% was above 2Q19's 43.7%.
Operating Profit	1,317	1,454	1,455	0.1	10.5	
Provisions	(95)	(51)	(145)	184.3	52.6	3Q19 total credit costs were up 15bps QoQ to 23bps.
	0					
Associates	25	0	14	#DIV/0!	(44.0)	
Pre-tax profit	1,246	1,403	1,324	(5.6)	6.3	
Taxation	(206)	(231)	(202)	(12.6)	(1.9)	
Profit after tax	1,040	1,172	1,122	(4.3)	7.9	
Minorities	(3)	(4)	(3)	(25.0)	0.0	
Net Profit	1,037	1,168	1,118	(4.3)	7.8	9M19 net profit of SGD3.34bn represents 77% of our pre-results 2019 forecast.
Other Key Data & Ratios						
ROE (Avg)	11.7	12.5	11.8			3Q19 ROE of 11.8% was marginally better than 3Q18's 11.7%.
Net Interest Margin	1.81	1.81	1.77			We expected 3Q19 NIM to be narrower - 3Q19 NIM was 4bps narrower YoY.
Net interest income / income	68.7	64.0	64.7			
Ops exp / income (excl one-time items)	43.4	43.7	44.2			
Assets	382,638	406,382	408,383	0.5	6.7	
Non-bank loans	251,755	269,820	271,886	0.8	8.0	Sequential growth led by the 5% QoQ expansion in loans to general commerce (13% loan share).
Customer deposit	293,634	304,792	304,423	(0.1)	3.7	
Non-performing assets	4,374	4,185	4,350	3.9	(0.5)	NPL ratio of 1.5% was flat sequentially.
Cumulative loan loss provisions	3,935	3,474	3,582	3.1	(9.0)	
Loans deposit ratio	85.7	88.5	89.3			
NPL / Non-bank loans	1.6	1.5	1.5			
Loan loss coverage	90.0	83.0	82.3			
Total CAR	17.4	17.2	16.9			
Tier 1 CAR	15.1	14.9	15.0			

Source: Company data

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Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
Neutral:	Share price may fall within the range of +/- 10% over the next 12 months
Take Profit:	Target price has been attained. Look to accumulate at lower levels
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Not Rated:	Stock is not within regular research coverage

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