

23 July 2024

Financial Services | Banks

United Overseas Bank (UOB SP)

Neutral (Maintained)

Valuations Should Provide Downside Support

Target Price (Return): SGD32.00 (-2%)
 Price (Market Cap): SGD32.66 (USD40,515m)
 ESG score: 3.2 (out of 4)
 Avg Daily Turnover (SGD/USD) 77.6m/57.4m

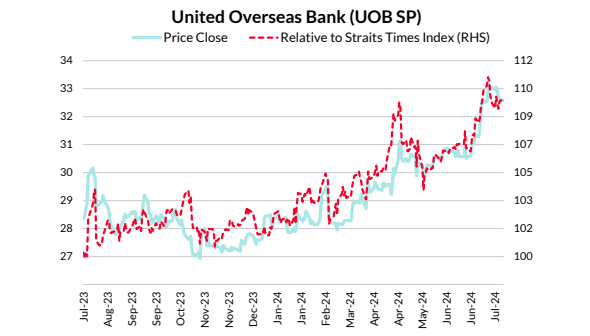
- **NEUTRAL, new SGD32 TP from SGD30.10, 2% downside with c.6% FY25F yield.** Post meeting with United Overseas Bank's management, we think 2Q24 PATMI could ease QoQ if trading & investment (T&I) income normalises from 1Q24's high level. The roll-off in Citi integration costs in 2H24 is positive for earnings, and efforts to build up the wholesale platform look to be bearing fruit. However, investors' focus will be on dividend yields and DPS growth in an interest rate downcycle, and UOB's preference to retain capital for growth means yields and DPS growth may lag peers.
- **2Q key trends likely mixed.** We gathered that loan growth momentum was surprisingly resilient in 2Q, thanks to broad-based growth. Coupled with NIM support from efforts to lower deposit cost (impact mainly felt in 2Q), 2Q NII should be decent QoQ while, YoY, NII could still be slightly lower on lower NIM. We understand that the reduction in deposit rates have not had a major impact on UOB's deposit market share so far and, for now, no decision has been made on whether to undertake another round of rate cuts. As for non-II, we expect fee income to remain healthy but believe the normalisation of T&I income will dampen overall operating income. 1Q24 T&I income was SGD522m and, based on the guided run rate of SGD350-400m/quarter, non-II and operating income growth may soften ahead. Lastly, asset quality continues to hold up and UOB has not noted any adverse developments.
- **Integration of Citi Thailand** had seen some teething issues, but management believes the issue can be resolved fairly quickly. Expect the Citi integration costs (c. SGD100m per quarter) that UOB has been incurring to largely run its course in 2Q, and drop off significantly in 2H24 now that Operating Day 1 for the major markets in Malaysia, Thailand and Indonesia is past. Management made no change to the core CIR guidance of 41-42%.
- **Wholesale platform starting to bear fruits.** UOB rolled out its digital platform for the wholesale business for the rest of the region two years ago, and this should have a positive impact on wholesale CASA momentum. Despite the elevated rates environment, its CASA deposits at end-1Q24 was up 12% (CASA ratio: 50.6%) vs 4Q22 (CASA ratio: 47.5%). The focus ahead is on revenue generation, eg growing trade loans, which should also bring in ancillary revenue streams such as FX and cash management.
- **Capital management unlikely at this juncture** as UOB prefers to continue building up its CET-1 ratio (1Q: 13.9%) to narrow the gap with peers (CET-1 ratios of 14.7-16.2%) and to retain capital for growth opportunities. It cited a CET-1 comfort level of 13.5-14%, which it thinks is sufficient to support risk-weighted assets growth of 7-8% and a 50% dividend payout ratio. If growth is weaker than expected, it will reconsider its capital management theme.
- **Forecasts unchanged but TP rises.** We raise our TP to SGD32 from SGD30.10 after rolling forward our valuation base year to FY25F. Our TP includes an unchanged 2% ESG premium.

Analyst

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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	14.5	6.5	7.0	16.6	13.8
Relative	8.4	2.5	0.4	7.5	9.0
52-wk Price low/high (SGD)				26.9	-33.1



Source: Bloomberg

Overall ESG Score: 3.2 (out of 4)

E: GOOD

In 2023, UOB purchased and retired 20.5k carbon offsets to address its Scope 1, residual Scope 2 and Scope 3 (business air travel) emissions. It has made a net zero commitment for six sectors by 2050 while aiming to build a sustainable finance portfolio of SGD30bn by 2025 (2023: SGD44.5bn). Meanwhile, about SGD10bn in total assets under management were in ESG-focused investments.

S: EXCELLENT

UOB embraces gender diversity, with women accounting for 62% of permanent staff at end-2023 - 38% in senior management roles. It launched TMRW, ASEAN's first mobile-only digital bank, to improve financial inclusion in Thailand and Indonesia.

G: EXCELLENT

UOB has a comprehensive framework of policies, processes, methodologies and tools for effective risk management. There is a much publicised ongoing money laundering case in Singapore, where UOB is one of several banks mentioned in relation to the case.

Forecasts and Valuation	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Reported net profit (SGDm)	4,573	5,711	5,876	6,089	6,266
Net profit growth (%)	12.2	24.9	2.9	3.6	2.9
Recurring net profit (SGDm)	4,819	6,061	6,045	6,089	6,266
Recurring EPS (SGD)	2.88	3.62	3.61	3.64	3.75
BVPS (SGD)	25.86	27.64	29.43	31.24	33.16
DPS (SGD)	1.35	1.71	1.76	1.81	1.86
Recurring P/E (x)	11.32	9.00	9.01	8.95	8.69
P/B (x)	1.26	1.18	1.11	1.04	0.98
Dividend Yield (%)	4.1	5.2	5.4	5.6	5.7
Return on average equity (%)	10.6	12.7	12.3	12.0	11.6

Source: Company data, RHB

Financial Exhibits

Asia	Financial summary (SGD)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Singapore	EPS	2.73	3.41	3.51	3.64	3.75
Financial Services	Recurring EPS	2.88	3.62	3.61	3.64	3.75
United Overseas Bank	DPS	1.35	1.71	1.76	1.81	1.86
UOB SP	BVPS	25.86	27.64	29.43	31.24	33.16
Neutral						
	Valuation metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Valuation basis	Recurring P/E (x)	11.32	9.00	9.01	8.95	8.69
GGM-derived intrinsic value with an ESG overlay. Key GGM assumptions are:	P/B (x)	1.3	1.2	1.1	1.0	1.0
i. COE of 12.5%;	Dividend Yield (%)	4.1	5.2	5.4	5.6	5.7
ii. ROE of 12.5%; and						
iii. 3.0% long-term growth.						
	Income statement (SGDm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Key drivers	Interest income	12,862	22,242	22,457	22,324	22,211
Our net profit forecasts is most sensitive to changes in:	Interest expense	(4,519)	(12,563)	(12,719)	(12,389)	(12,110)
i. Impairment charges	Net interest income	8,343	9,679	9,738	9,936	10,100
ii. NIM	Non interest income	3,232	4,253	4,428	4,722	5,054
iii. Non-II growth.	Total operating income	11,575	13,932	14,166	14,658	15,155
	Overheads	(4,971)	(5,797)	(5,987)	(6,431)	(6,678)
	Pre-provision operating profit	6,604	8,135	8,179	8,226	8,477
Key risks	Loan impairment allowances	(628)	(783)	(800)	(850)	(850)
Key risks include:	Other impairment allowances	22	(162)	(45)	(41)	(40)
i. Weaker-than-expected NIM	Income from associates	97	93	100	110	120
ii. Sharper-than-expected deterioration in asset quality	Other exceptional items	(310)	(420)	(208)	-	-
iii. Challenges related to integration of Citi's consumer assets.	Pre-tax profit	5,785	6,863	7,226	7,445	7,707
	Taxation	(1,202)	(1,138)	(1,337)	(1,340)	(1,426)
	Minority interests	(10)	(14)	(14)	(16)	(15)
	Reported net profit	4,573	5,711	5,876	6,089	6,266
	Recurring net profit	4,819	6,061	6,045	6,089	6,266
Company Profile						
United Overseas Bank is the third largest Singapore bank by asset size. It also has significant operations in Malaysia, Thailand & Indonesia.	Profitability ratios	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Return on average assets (%)	0.9	1.1	1.1	1.1	1.1
	Return on average equity (%)	10.6	12.7	12.3	12.0	11.6
	Return on IEAs (%)	3.0	5.0	4.9	4.7	4.5
	Cost of funds (%)	1.1	2.8	2.8	2.6	2.4
	Net interest spread (%)	2.0	2.2	2.2	2.1	2.1
	Net interest margin (%)	2.0	2.2	2.1	2.1	2.1
	Non-interest income / total income (%)	27.9	30.5	31.3	32.2	33.4
	Cost to income ratio (%)	42.9	41.6	42.3	43.9	44.1
	Credit cost (bps)	19.9	24.4	24.5	25.1	24.0
	Balance sheet (SGDm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Total gross loans	319,663	321,150	330,785	347,324	361,217
	Other interest earning assets	116,707	125,723	130,670	135,313	139,868
	Total gross IEAs	436,370	446,873	461,455	482,637	501,084
	Total provisions	(4,308)	(4,145)	(4,317)	(4,469)	(4,546)
	Net loans to customers	315,355	317,005	326,468	342,855	356,671
	Total net IEAs	432,062	442,728	457,138	478,168	496,538
	Total non-IEAs	72,198	80,792	83,790	89,271	98,390
	Total assets	504,260	523,520	540,928	567,439	594,928
	Customer deposits	368,553	385,469	397,033	416,885	437,729
	Other interest-bearing liabilities	65,918	69,551	71,293	73,747	75,952
	Total IBLs	434,471	455,020	468,326	490,632	513,681
	Total non-IBLs	26,183	22,032	23,134	24,290	25,505
	Total liabilities	460,654	477,052	491,459	514,922	539,186
	Share capital	7,855	7,752	7,752	7,752	7,752
	Shareholders' equity	43,366	46,226	49,212	52,245	55,456
	Minority interests	240	242	256	272	287
	Asset quality and capital	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Reported NPLs / gross cust loans (%)	1.6	1.5	1.5	1.5	1.5
	Total provisions / reported NPLs (%)	85.1	85.1	87.0	87.2	86.8
	CET-1 ratio (%)	14.4	14.4	15.0	15.1	15.3
	Tier-1 ratio (%)	14.4	14.4	15.0	15.1	15.3
	Total capital ratio (%)	16.7	16.6	17.0	17.1	17.2

Source: Company data, RHB

Valuation and TP

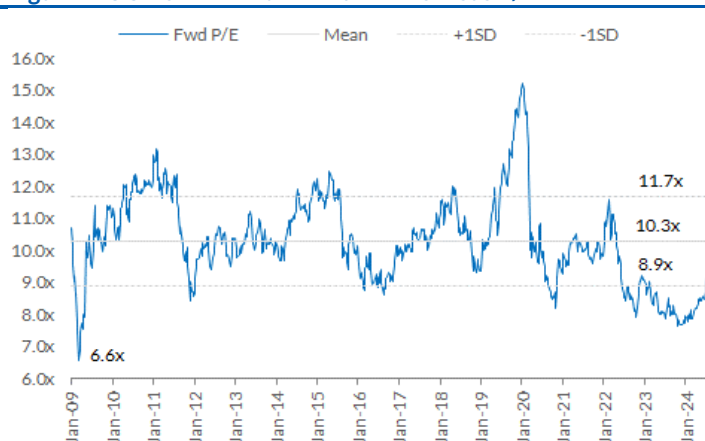
We raise our TP to SGD32.00 from SGD30.10 after rolling forward our BVPS assumption (base case) to FY25F from FY24F. This led to a revised intrinsic value of SGD31.38, vs SGD29.55 previously. There is no change to our GGM-derived P/BV of 1.04x, which is slightly below the mean P/BV of 1.08x. Our TP includes an unchanged ESG premium of 2% applied – given UOB’s ESG core of 3.2 out of 4.0, using our proprietary in-house methodology.

Figure 1: UOB – GGM valuation with ESG overlay

Cost of equity (COE) computation:		Sustainable ROE (%)	12.5
Risk free rate (%)	3.0	COE (%)	12.1
Equity premium (%)	8.3	Long-term growth (g)	3.0
Beta (x)	1.1	Implied P/BV (x)	1.04
Cost of equity - CAPM (%)	12.1	BVPS - FY24F	SGD30.16
		Intrinsic value	SGD31.38
ESG premium/(discount) (%)	2.0	ESG premium/(discount)	SGD0.63
		TP (rounded)	SGD32.00

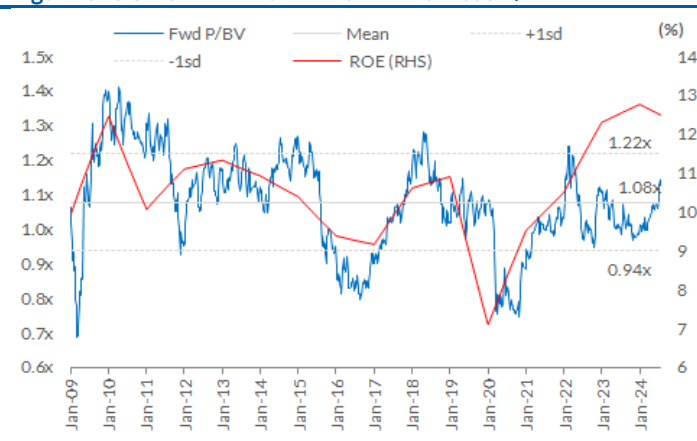
Source: Company data, RHB

Figure 2: UOB’s 12-month forward consensus P/E



Source: Bloomberg, RHB

Figure 3: UOB’s 12-month forward consensus P/BV



Source: Bloomberg, RHB

Emissions And ESG

Trend analysis

In 2023, UOB purchased and redeemed a total of 135k GWh in Renewable Energy Certificates (RECs) to address its electricity consumption in all key markets. UOB also purchased and retired 20.5k carbon offsets to address its Scope 1, residual Scope 2 and Scope 3 (business air travel) emissions.

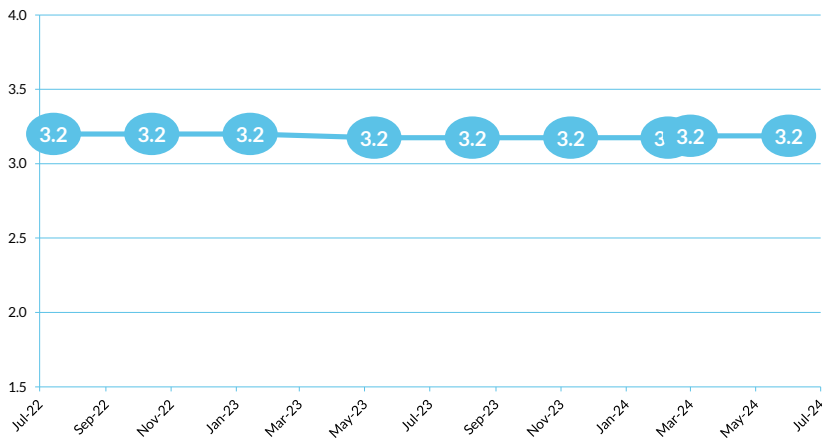
Emissions (tCO2e)	Dec-21	Dec-22	Dec-23
Scope 1	4,300	5,800	4,800
Scope 2	1,000	1,100	1,600
Scope 3	600	4,000	14,100
Total emissions	5,900	10,900	20,500

Source: Company data, RHB

Latest ESG-Related Developments

- **UOB Transition Finance Framework:** This was launched in 2022 to help companies in carbon-intensive sectors with their net-zero transition plans.
- **Sustainable targets:** Sustainable finance portfolio of SGD30bn by 2025 and net zero for six sectors (currently 60% of corporate lending portfolio) by 2050.
- **Signatory to the Equator Principles (EP):** EP requirements are integrated into UOB Group's Responsible Financing Policy.
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ESG Rating History

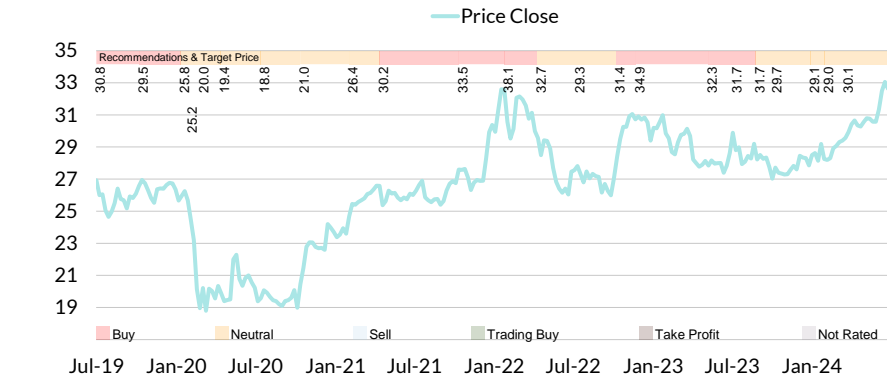


Source: RHB

Recommendation Chart

23 July 2024

Financial Services | Banks



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2024-05-09	Neutral	30.1	30.4
2024-03-21	Neutral	29.0	29.2
2024-02-22	Neutral	29.0	28.5
2024-01-21	Neutral	29.1	27.9
2023-10-26	Neutral	29.7	27.3
2023-09-17	Neutral	31.7	29.2
2023-07-27	Buy	31.7	28.9
2023-05-30	Buy	32.3	28.1
2023-02-23	Buy	34.9	29.6
2022-12-16	Buy	34.9	30.7
2022-10-30	Buy	31.4	27.1
2022-07-31	Neutral	29.3	27.6
2022-05-03	Neutral	32.7	30.0
2022-02-16	Buy	38.1	32.8
2021-11-04	Buy	33.5	27.2

Source: RHB, Bloomberg

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