

4 May 2022

Financial Services | Banks

United Overseas Bank (UOB SP)

Neutral (from Buy)

Headwinds To Moderate FY22 Growth; D/G NEUTRAL

Target Price (Return): SGD32.70 (9.0%)
 Price (Market Cap): SGD30.00 (USD36,245m)
 ESG score: 3.20 (out of 4)
 Avg Daily Turnover (SGD/USD) 110m/81.1m

• **D/G to NEUTRAL from Buy, new SGD32.70 TP from SGD38.10, 9% upside, c.4% yield.** 1Q22 results missed expectations mainly on lower non-II. Although trading and investment (T&I) income is expected to rebound in 2Q22, we trimmed non-II due to the more challenging outlook. Our TP is lowered on account of higher risk premium and a tweak in the ESG score to 3.2 (from 3.3) as we recalibrate assessment of risks and regulatory requirements associated with data and cybersecurity. Share price should consolidate in the near term, given its YTD outperformance and more subdued FY22F earnings growth.

• **1Q22 results missed expectations.** Net profit of SGD906m (-11% QoQ, -10% YoY) was at 20% of our and consensus' FY22F earnings. Reported ROE was a lower 8.8% vs FY21's 10.2%, while CET-1 was relatively stable at 13.1%. PIOP fell 7% YoY as net fee income dropped 8% on lower wealth management and fund management, and T&I income plunged 83% (impacted by hedges and mark-to-market (MTM) losses on investments). The sharper bottomline decline was mainly due to higher tax provisions following Malaysia's imposition of prosperity tax for 2022. Provisions fell 11% on a SGD2m write-back of general allowance (GP) vs a SGD136m charge in 1Q21. Credit cost was 19bps vs 22bps in 4Q21 and 29bps in 1Q21.

• **FY22 guidance.** While domestic recovery in regional countries are still at a nascent stage, management is keeping a close watch on macroeconomic developments, given the geopolitical conflict and China's pandemic-related lockdown. Loan growth guidance of mid-to-high single digit growth in 2022 remains intact, and would likely be driven by lending to the wholesale segment. UOB now expects the US Federal Reserve to raise rates six times (from five times) in 2022, with every 25bps hike adding 4bps to NIM and SGD150m-200m in NII. NIM is expected to rise to 1.60-1.62% in 2Q22 and reach 1.70% in 4Q22. Non-II, which was earlier projected to grow by double digits, may be impacted by lower wealth management fees. Given that the MTM loss in 1Q22 is one-off, management guides for T&I income to recover to SGD200m per quarter from 2Q22. See Figure 2 for details.

• **Asset quality stable.** Management believes headwinds from current macro developments would likely have some impact from China. That said, the exposure should be manageable, and the bank's regular stress testing of portfolio has not revealed any significant weakness. UOB's NPL ratio was stable at 1.6% while NPA coverage is at a healthy 94%. Management is comfortable with its credit cost guidance of 20-25bps for FY22F. The bank is unlikely to write-back GP reserves in the near term.

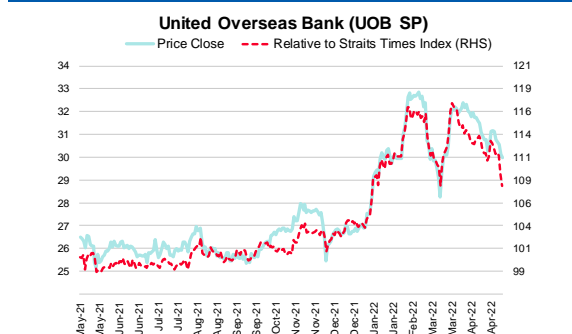
• **Earnings and TP lowered.** Our earnings forecasts are trimmed by 5-6% for FY22F-24F to take into account the 1Q22 MTM trading loss as well as more conservative assumptions on non-II, given the more challenging environment for wealth management and T&I. Our TP is revised to SGD32.70 as we refreshed GGM assumptions for higher equity risk premium and a lower 4% (from 6%) ESG premium, based on our in-house proprietary methodology.

Analyst

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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	11.5	(6.8)	0.1	12.1	12.8
Relative	4.0	(4.5)	(3.3)	7.1	8.6
52-wk Price low/high (SGD)	25.2 – 32.9				



Source: Bloomberg

Overall ESG Score: 3.20 (out of 4)

E: GOOD

UOB's sustainability strategy includes the integration of ESG considerations into the bank's credit evaluation and approval processes as well as its investment products. It is progressively adopting as well as promoting climate-resilient practices that will support clients' own transition to a lower-carbon economy. The bank conducts materiality assessments and stakeholder consultations on a continual basis. Aims to build a sustainable finance portfolio of SGD30bn by 2025 (2021: SGD17bn).

S: GOOD

UOB embraces gender diversity, with women accounting for 61% of permanent staff at end 2020 – 50% in senior and middle management roles – and targets to appoint at least one female director in 2021. Launched TMRW, ASEAN's first mobile-only digital bank, to improve financial inclusion in Thailand and Indonesia. In 2021, there were no legal proceedings against UOB in respect of any data privacy breach, nor any fine or sanction imposed on the bank.

G: EXCELLENT

UOB has a comprehensive framework of policies, processes, methodologies and tools for effective risk management. In 2020, no material fine, penalty or sanction was imposed on UOB for non-compliance in relation to any laws and regulations.

Forecasts and Valuation	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Reported net profit (SGDm)	2,915	4,075	4,212	5,092	5,718
Net profit growth (%)	(32.9)	39.8	3.4	20.9	12.3
Recurring net profit (SGDm)	2,915	4,075	4,212	5,092	5,718
Recurring EPS (SGD)	1.74	2.44	2.52	3.05	3.42
BVPS (SGD)	24.45	25.50	26.73	28.31	30.01
DPS (SGD)	0.78	1.21	1.32	1.60	1.80
Recurring P/E (x)	17.19	12.31	11.91	9.85	8.77
P/B (x)	1.23	1.18	1.12	1.06	1.00
Dividend Yield (%)	2.6	4.0	4.4	5.3	6.0
Return on average equity (%)	7.2	9.8	9.6	11.1	11.7

Source: Company data, RHB

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Financial Exhibits

Asia	Financial summary (SGD)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Singapore	EPS	1.74	2.44	2.52	3.05	3.42
Financial Services	Recurring EPS	1.74	2.44	2.52	3.05	3.42
United Overseas Bank	DPS	0.78	1.21	1.32	1.60	1.80
UOB SP	BVPS	24.45	25.50	26.73	28.31	30.01
Neutral						
	Valuation metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Valuation basis	Recurring P/E (x)	17.19	12.31	11.91	9.85	8.77
GGM-derived intrinsic value with an ESG overlay. Key GGM assumptions are:	P/B (x)	1.2	1.2	1.1	1.1	1.0
i. COE of 10.37%;	Dividend Yield (%)	2.6	4.0	4.4	5.3	6.0
ii. ROE of 11.5%; and						
iii. 4.0% long-term growth						
Key drivers	Income statement (SGDm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Our net profit forecast is most sensitive to changes in:	Interest income	9,623	8,204	10,533	13,647	14,649
i. Impairment charges;	Interest expense	(3,588)	(1,816)	(3,383)	(5,600)	(5,992)
ii. NIM;	Net interest income	6,035	6,388	7,150	8,047	8,658
iii. Non-II growth.	Non interest income	3,141	3,401	3,285	3,597	3,877
	Total operating income	9,176	9,789	10,435	11,644	12,535
	Overheads	(4,184)	(4,313)	(4,642)	(4,871)	(5,081)
	Pre-provision operating profit	4,992	5,476	5,793	6,773	7,454
	Loan impairment allowances	(1,596)	(629)	(680)	(650)	(580)
	Other impairment allowances	42	(28)	(30)	(26)	(20)
	Income from associates	98	118	128	138	150
	Pre-tax profit	3,536	4,937	5,211	6,235	7,004
	Taxation	(606)	(850)	(983)	(1,122)	(1,261)
	Minority interests	(15)	(12)	(16)	(20)	(25)
	Reported net profit	2,915	4,075	4,212	5,092	5,718
	Recurring net profit	2,915	4,075	4,212	5,092	5,718
Key risks						
Key risks include:	Profitability ratios	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
i. Weaker-than-expected NIM;	Return on average assets (%)	0.7	0.9	0.9	1.0	1.1
ii. Sharper-than-expected deterioration in asset quality; and	Return on average equity (%)	7.2	9.8	9.6	11.1	11.7
iii. Softer-than-expected non-interest income growth.	Return on IEAs (%)	2.6	2.1	2.5	3.0	3.1
	Cost of funds (%)	1.0	0.5	0.8	1.3	1.3
	Net interest spread (%)	1.6	1.6	1.7	1.8	1.8
	Net interest margin (%)	1.6	1.6	1.7	1.8	1.8
	Non-interest income / total income (%)	34.2	34.7	31.5	30.9	30.9
	Cost to income ratio (%)	45.6	44.1	44.5	41.8	40.5
	Credit cost (bps)	58.0	21.2	21.0	18.7	15.8
Company Profile	Balance sheet (SGDm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
UOB is the third largest Singapore bank by asset size. It also has significant operations in Malaysia, Thailand & Indonesia.	Total gross loans	281,387	310,800	337,300	357,538	377,203
	Other interest earning assets	99,454	98,208	99,870	104,493	108,849
	Total gross IEAs	380,841	409,008	437,170	462,031	486,052
	Total provisions	(4,565)	(4,497)	(5,136)	(5,287)	(5,419)
	Net loans to customers	277,201	306,713	332,574	352,661	372,193
	Total net IEAs	376,276	404,511	432,034	456,744	480,633
	Total non-IEAs	55,538	54,812	57,364	58,166	60,946
	Total assets	431,814	459,323	489,397	514,911	541,579
	Customer deposits	324,598	352,633	384,000	407,040	430,648
	Other interest-bearing liabilities	46,377	50,594	48,264	47,745	47,573
	Total IBLs	370,975	403,227	432,264	454,785	478,221
	Total non-IBLs	19,708	13,235	12,200	12,566	12,943
	Total liabilities	390,683	416,462	444,464	467,351	491,164
	Share capital	7,420	7,391	7,391	7,391	7,391
	Shareholders' equity	40,901	42,633	44,705	47,332	50,185
	Minority interests	230	228	228	228	230
	Asset quality and capital	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Reported NPLs / gross cust loans (%)	1.6	1.6	1.8	1.7	1.7
	Total provisions / reported NPLs (%)	92.6	81.3	80.1	80.2	80.5
	CET-1 ratio (%)	15.8	14.4	14.3	14.3	14.4
	Tier-1 ratio (%)	15.8	14.4	14.3	14.3	14.4
	Total capital ratio (%)	18.4	16.6	16.4	16.3	16.3

Source: Company data, RHB

Results At a Glance

Figure 1: UOB – summary of 1Q22 results

FYE 31 Dec (SGDm)	1Q21	4Q21	1Q22	QoQ (%)	YoY (%)	Comments: 1Q22 vs 4Q21
NII	1,529	1,677	1,686	1	10	Up QoQ mainly on loan growth. As rate hike started in late March, impact will only be felt in quarters ahead.
<i>NIM (%) – reported</i>	1.57%	1.56%	1.58%			
Non-II	957	757	673	-11	-30	
Net fee & commission income	619	580	572	-1	-8	Slipped QoQ as higher loan/trade-related fees were offset by lower fees from wealth management and credit cards.
Other non-II	338	177	101	-43	-70	Fell QoQ on impact from hedges as interest rates rose, and unrealised MTM on investments. Customer-related trading income rose 18% QoQ as market volatility led to higher hedging needs.
<i>Non-II/total income (%)</i>	38.5%	0.0%	0.0%			
Operating income	2,486	2,434	2,359	-3	-5	
Overhead expenses	(1,089)	(1,095)	(1,058)	-3	-3	
<i>CIR (%)</i>	43.8%	45.0%	44.8%			
PIOP	1,397	1,339	1,301	-3	-7	
Impairments charges	(201)	(112)	(178)	59	-11	Specific provisions fell 13% QoQ to SGD148m, but general provision write-backs declined 97% QoQ to SGD2m.
<i>Annualised credit cost (bps)</i>	28	15	23			SP credit cost was 19bps vs 22bps in 4Q21.
Operating profit	1,196	1,227	1,123	-8	-6	
Associates	32	19	29			
Pre-tax profit	1,228	1,246	1,152	-8	-6	
Tax	(216)	(226)	(243)			
<i>Effective tax rate (%)</i>	17.6%	18.1%	21.1%			
Minorities	(3)	(3)	(3)			
Net profit	1,009	1,017	906	-11	-10	
Other key data and ratios						
Gross loans	293,267	310,800	319,999	3	9	Up 3% YTD on trade and term loans in Singapore.
Customer deposits	331,979	352,633	361,747	3	9	CASA ratio was stable at 55.9% vs 56.2% in Dec 2021.
Gross impaired loans	4,399	5,030	5,120	2	16	
Total assets	440,749	459,323	475,847	4	8	
Shareholders' funds	41,700	42,633	42,892	1	3	
ROAA (%)	0.92	0.89	0.78			
ROAE (%)	10.2	10.0	8.8			
LDR (%)	86.7	86.7	87.0			
NPL ratio	1.50	1.62	1.60			
NPA coverage	112.0	96.0	94.0			
CET-1 ratio (%)	14.3	13.5	13.1			
Total capital ratio (%)	17.9	16.6	15.8			

Source: Company data, RHB

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Figure 2: UOB – management guidance and financial targets

	2021 targets	1Q22 achieved	2022 targets	Comments – FY22 targets
Loan growth	+10% YoY	+9% YoY	Mid-to-high single digit	Management remains fairly positive on its outlook, with the impact of an imminent interest rate upcycle expected to be manageable. Growth is expected to be led by working capital loans and mortgages for its retail banking operations. Loan growth in ASEAN is expected to gain momentum, helped by recoveries in these countries.
NIM	1.56%	1.58%	1.6% in 2Q22, 1.7% by 4Q22	NIM expected to rise to 1.60-1.62% in 2Q22, and reach 1.70% in 4Q22. UOB expects six rate hikes (revised from five) in US rates in 2022. A 25bps rise in US rates would add 4bps to NIM and SGD150-200m to NII over a 12-month period.
Non-II growth	+8% YoY	-30% YoY	Double-digit growth	Management guides that the large unrealised MTM loss on investments in 1Q22 will not be repeated. Income from T&I is expected to revert to c.SGD200m a quarter for the remaining quarters.
CIR (%)	+44.1%	+44.8%	Stable YoY	Opex will rise in FY22 on higher staff costs (at least 10% increase) and digital investments. Management aims to keep CIR stable, with revenue expected to grow in tandem. A stronger-than-expected rise in US rates would have a positive impact on CIR.
Credit cost	20bps	23bps	20-25bps	Remains comfortable with guidance. SP is expected to be lower in quarters ahead while GPs will be raised on expected loan growth. Management estimated additional GP of SGD10-15m per quarter for new loans.

Source: Company data, RHB

Revisions to estimates

We lowered net profit forecasts by 5-6% for FY22F-24F after taking into account the 1Q22 MTM trading loss, as well as on downward revisions in non-II for FY23F-24F.

Figure 3: UOB – revisions to forecasts

	Previous FY22F	Previous FY23F	Previous FY24F	Revised FY22F	Revised FY23F	New FY24F	% Change FY22F	% Change FY23F	% Change FY24F
FYE Dec (SGDm)									
Net interest income	7,150	8,047	8,658	7,150	8,047	8,658	0%	0%	0%
Non-interest income	3,565	3,943	4,294	3,285	3,597	3,877	-8%	-9%	-10%
Operating expenses	(4,642)	(4,871)	(5,081)	(4,642)	(4,871)	(5,081)	0%	0%	0%
PIOP	6,073	7,119	7,871	5,793	6,773	7,454	-5%	-5%	-5%
Provision expenses	(710)	(676)	(600)	(710)	(676)	(600)	0%	0%	0%
Pretax profit	5,491	6,581	7,421	5,211	6,235	7,004	-5%	-5%	-6%
Net profit	4,441	5,377	6,060	4,212	5,092	5,718	-5%	-5%	-6%
EPS (SGD)	2.38	2.60	3.16	2.38	2.46	2.99	0%	-5%	-5%
DPS (SGD)	1.20	1.32	1.60	1.20	1.32	1.60	0%	0%	0%
Loan growth (%)	8.5	6.0	5.5	8.5	6.0	5.5			
NIM (%)	1.71	1.81	1.85	1.71	1.81	1.85			
CIR (%)	43.3	40.6	39.2	44.5	41.8	40.5			
Credit cost (bps)	22	19	16	22	19	16			

Source: Company data, RHB

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Valuation and TP

Our TP is revised to SGD32.70 (from SGD38.10), based on an intrinsic value of SGD31.43 (from SGD35.95) and a 4% (from 6%) ESG premium – the latter is based on RHB's proprietary ESG methodology.

The lower intrinsic value is mainly due to a higher cost of equity on account of geopolitical conflict, uncertainties arising from China's pandemic-related lockdowns, and risk of recession from spiralling inflation. We tweaked the ESG score to 3.2 from 3.3 as we recalibrate assessment of risks and regulatory requirements associated with data and cybersecurity.

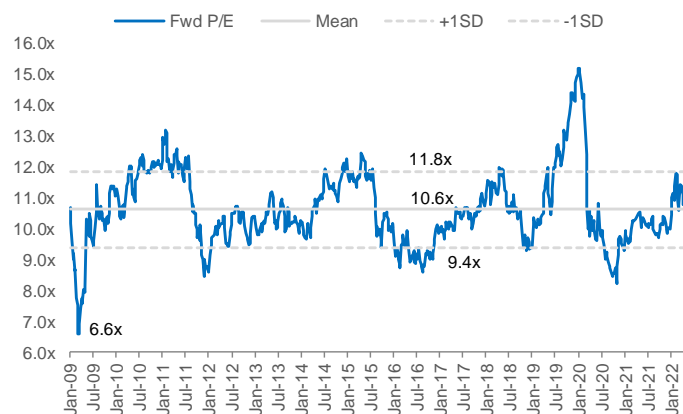
The GGM-derived P/BV of 1.18x (from 1.37x) is at +0.5SD from the historical mean, against an ROE of 11.5%.

Figure 4: UOB – GGM valuation with ESG overlay

Cost of equity (COE) computation:		Sustainable ROE (%)	11.50
Risk free rate (%)	2.50	COE (%)	10.37
Equity premium (%)	7.5	Long-term growth (g)	4.00
Beta (x)	1.05	Implied P/BV (x)	1.18
Cost of equity - CAPM (%)	10.37	BVPS – 12-month rolling forward	SGD26.70
		Intrinsic value	SGD31.43
ESG premium/(discount) (%)	4.0	ESG premium/(discount)	SGD1.26
		TP (rounded)	SGD32.70

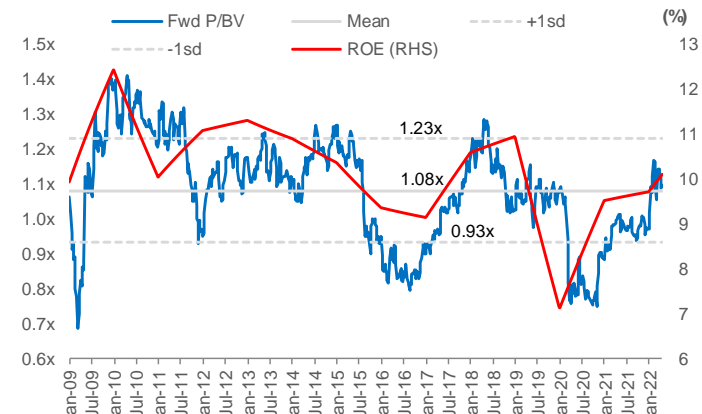
Source: Company data, RHB

Figure 5: UOB's 12-month forward consensus P/E



Source: Bloomberg, RHB

Figure 6: UOB's 12-month forward consensus P/BV



Source: Bloomberg, RHB

Recommendation Chart

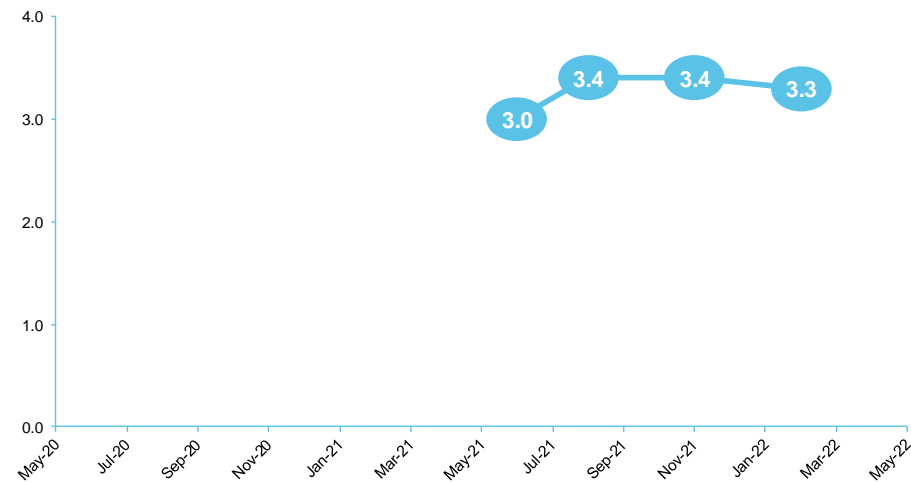


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-02-16	Buy	38.1	32.8
2021-11-04	Buy	33.5	27.2
2021-05-06	Buy	30.2	26.0
2021-02-25	Neutral	26.4	24.7
2020-11-04	Neutral	21.0	19.8
2020-08-06	Neutral	18.8	19.8
2020-05-06	Neutral	19.4	19.9
2020-03-20	Neutral	20.0	19.0
2020-02-21	Neutral	25.2	25.7
2020-02-04	Neutral	25.8	25.8
2019-11-01	Buy	29.5	26.6
2019-05-03	Buy	30.8	27.8

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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