

16 December 2022

Financial Services | Banks

United Overseas Bank (UOB SP)

Buy (Maintained)

NIM Expansion And Citi Acquisition To Lift ROE; Keep BUY

Target Price (Return): SGD34.90 (13.1%)
 Price (Market Cap): SGD30.90 (USD38,154m)
 ESG score: 3.20 (out of 4)
 Avg Daily Turnover (SGD/USD) 88.3m/63.4m

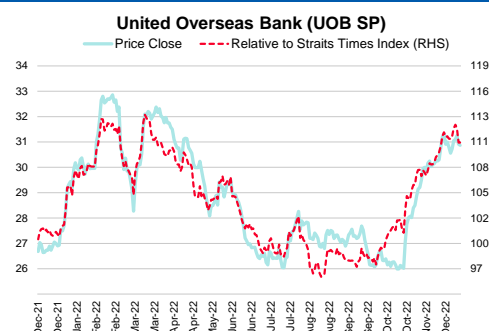
- **Keep BUY with a higher SGD34.90 TP from SGD31.40 and c.5% yield.** We expect United Overseas Bank to deliver strong earnings growth of c.18% in FY23 despite the expected softening in GDP growth. Tailwinds from further NIM expansion, coupled with contributions from Citi's consumer assets in Malaysia and Thailand would drive ROE improvements over the next two years. Our intrinsic value of SGD33.57 is based on a GGM-derived 1.26x FY23F P/BV.
- **NIM remains the bright spot.** The 3-month compounded Singapore Overnight Rate Average (SORA) rate crossed 3% for the first time on 5 Dec and looks set to trend higher. The 1-month SORA rate is at a higher 3.39% while the US federal funds rate (FFR) was raised another 50bps to 4.50% on 14 Dec. Recall that management guided for NIM to stay above 2.0% in 4Q22 and rise another 5-10bps should the FFR reach 4.0%. Along with the rise in lending rates, UOB similar to its peers, has also raised deposit rates since August. The rise in cost of funds would be mitigated by the very decent spread the bank makes from placing excess funds in the government treasury bills (T-bills).
- **Asset quality to hold up well.** Management expects the group's asset quality to remain resilient as rate hikes within the region have been orderly while businesses continue to have access to credit and employment markets are healthy. UOB's NPL ratio eased to 1.5% in 3Q22, from 1.7% in 2Q22, as NPLs fell 10% QoQ on lower NPL formation and higher recoveries. LLC was comfortable at 98%. Management guides for credit cost of 25bps in FY23, vs guidance of 20bps for FY22F (9M22: 18bps) with the 5bps coming from the consolidation of Citi's consumer business in Malaysia and Thailand.
- **Acquisition of Citi's consumer assets progressing well.** On 1 Nov 2022, UOB completed the acquisition of Citi's consumer assets in Malaysia and Thailand. The bank is working towards full system integration in 12-18 months. Consolidation of Citi's portfolio, which has a larger portion of unsecured loans, is expected to lift UOB's NIM by another 5-10bps while adding 5bps to credit cost. Management expects to incur MYR700-800m in a one-time cost that would keep FY23 CIR at c.44%. We gather that revenue numbers are tracking ahead of expectations, helped by the pick-up in economic and tourism activities in these two countries.
- **Earnings revisions and TP.** We nudged up our FY23F-24F net profit by 5% and 7% respectively, as we adjusted NIM assumptions up by 7-10bps for the two years. We now expect earnings to rise by a very healthy 18% in FY23F (FY22F: +16%), before moderating to a 12% growth in FY24F. Our TP rises to SGD34.90 (from SGD31.40) based on our updated GGM assumptions (Figure 2). The TP incorporates a 4% ESG premium, based on our in-house methodology.

Analyst

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Share Performance (%)

| | YTD | 1m | 3m | 6m | 12m |
|----------------------------|------|-----|------|------|------|
| Absolute | 14.8 | 2.9 | 13.1 | 14.5 | 15.7 |
| Relative | 10.0 | 3.0 | 12.9 | 9.1 | 10.6 |
| 52-wk Price low/high (SGD) | | | | 26.0 | 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 61.5% of permanent staff at end-2021 – 36.3 in senior management roles. 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 2021, 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 | 4,719 | 5,549 | 6,192 |
| Net profit growth (%) | (32.9) | 39.8 | 15.8 | 17.6 | 11.6 |
| Recurring net profit (SGDm) | 2,915 | 4,075 | 4,719 | 5,549 | 6,192 |
| Recurring EPS (SGD) | 1.74 | 2.44 | 2.82 | 3.32 | 3.70 |
| BVPS (SGD) | 24.45 | 25.50 | 26.30 | 27.78 | 29.92 |
| DPS (SGD) | 0.78 | 1.21 | 1.25 | 1.45 | 1.65 |
| Recurring P/E (x) | 17.69 | 12.67 | 10.94 | 9.30 | 8.34 |
| P/B (x) | 1.26 | 1.21 | 1.17 | 1.11 | 1.03 |
| Dividend Yield (%) | 2.5 | 3.9 | 4.0 | 4.7 | 5.3 |
| Return on average equity (%) | 7.2 | 9.8 | 10.9 | 12.3 | 12.8 |

Source: Company data, RHB

16 December 2022

Financial Services | Banks

Financial Exhibits

| | | | | | | |
|---|--|---------------|---------------|----------------|----------------|----------------|
| Asia Singapore Financial Services United Overseas Bank UOB SP Buy | Financial summary (SGD) | Dec-20 | Dec-21 | Dec-22F | Dec-23F | Dec-24F |
| | EPS | 1.74 | 2.44 | 2.82 | 3.32 | 3.70 |
| | Recurring EPS | 1.74 | 2.44 | 2.82 | 3.32 | 3.70 |
| | DPS | 0.78 | 1.21 | 1.25 | 1.45 | 1.65 |
| | BVPS | 24.45 | 25.50 | 26.30 | 27.78 | 29.92 |
| Valuation basis GGM-derived intrinsic value with an ESG overlay. Key GGM assumptions are: (i) COE of 10.6%; (ii) ROE of 12.5%; and (iii) 3.0% long-term growth | Valuation metrics | Dec-20 | Dec-21 | Dec-22F | Dec-23F | Dec-24F |
| | Recurring P/E (x) | 17.69 | 12.67 | 10.94 | 9.30 | 8.34 |
| | P/B (x) | 1.3 | 1.2 | 1.2 | 1.1 | 1.0 |
| | Dividend Yield (%) | 2.5 | 3.9 | 4.0 | 4.7 | 5.3 |
| | | | | | | |
| Key drivers Our net profit forecasts is most sensitive to changes in: (i) Impairment charges; (ii) NIM; and (iii) Non-IL growth. | Income statement (SGDm) | Dec-20 | Dec-21 | Dec-22F | Dec-23F | Dec-24F |
| | Interest income | 9,623 | 8,204 | 21,572 | 26,492 | 28,949 |
| | Interest expense | (3,588) | (1,816) | (13,375) | (16,937) | (18,628) |
| | Net interest income | 6,035 | 6,388 | 8,198 | 9,554 | 10,321 |
| | Non interest income | 3,141 | 3,401 | 3,245 | 3,463 | 3,734 |
| Key risks Key risks include: (i) Weaker-than-expected NIM; (ii) Sharper-than-expected deterioration in asset quality; and (iii) Softer-than-expected non-interest income growth. | Total operating income | 9,176 | 9,789 | 11,443 | 13,018 | 14,055 |
| | Overheads | (4,184) | (4,313) | (5,005) | (5,518) | (5,849) |
| | Pre-provision operating profit | 4,992 | 5,476 | 6,438 | 7,499 | 8,205 |
| | Loan impairment allowances | (1,596) | (629) | (625) | (800) | (740) |
| | Other impairment allowances | 42 | (28) | (15) | (26) | (20) |
| Company Profile UOB is the third largest Singapore bank by asset size. It also has significant operations in Malaysia, Thailand & Indonesia. | Income from associates | 98 | 118 | 90 | 102 | 118 |
| | Pre-tax profit | 3,536 | 4,937 | 5,888 | 6,775 | 7,563 |
| | Taxation | (606) | (850) | (1,164) | (1,220) | (1,361) |
| | Minority interests | (15) | (12) | (5) | (7) | (10) |
| | Reported net profit | 2,915 | 4,075 | 4,719 | 5,549 | 6,192 |
| | Recurring net profit | 2,915 | 4,075 | 4,719 | 5,549 | 6,192 |
| | | | | | | |
| | Profitability ratios | Dec-20 | Dec-21 | Dec-22F | Dec-23F | Dec-24F |
| | Return on average assets (%) | 0.7 | 0.9 | 1.0 | 1.0 | 1.1 |
| | Return on average equity (%) | 7.2 | 9.8 | 10.9 | 12.3 | 12.8 |
| | Return on IEAs (%) | 2.6 | 2.1 | 5.0 | 5.6 | 5.8 |
| | Cost of funds (%) | 1.0 | 0.5 | 3.1 | 3.5 | 3.7 |
| | Net interest spread (%) | 1.6 | 1.6 | 1.9 | 2.1 | 2.1 |
| | Net interest margin (%) | 1.6 | 1.6 | 1.9 | 2.0 | 2.1 |
| | Non-interest income / total income (%) | 34.2 | 34.7 | 28.4 | 26.6 | 26.6 |
| | Cost to income ratio (%) | 45.6 | 44.1 | 43.7 | 42.4 | 41.6 |
| | Credit cost (bps) | 58.0 | 21.2 | 19.6 | 23.8 | 20.9 |
| | | | | | | |
| | Balance sheet (SGDm) | Dec-20 | Dec-21 | Dec-22F | Dec-23F | Dec-24F |
| | Total gross loans | 281,387 | 310,800 | 327,900 | 344,295 | 363,231 |
| | Other interest earning assets | 99,454 | 98,208 | 127,000 | 141,005 | 152,167 |
| | Total gross IEAs | 380,841 | 409,008 | 454,900 | 485,300 | 515,398 |
| | Total provisions | (4,565) | (4,497) | (4,745) | (5,199) | (5,276) |
| | Net loans to customers | 277,201 | 306,713 | 323,155 | 339,096 | 357,955 |
| | Total net IEAs | 376,276 | 404,511 | 450,155 | 480,101 | 510,122 |
| | Total non-IEAs | 55,538 | 54,812 | 77,720 | 81,839 | 86,227 |
| | Total assets | 431,814 | 459,323 | 527,875 | 561,940 | 596,350 |
| | Customer deposits | 324,598 | 352,633 | 392,000 | 421,400 | 449,634 |
| | Other interest-bearing liabilities | 46,377 | 50,594 | 72,060 | 72,690 | 73,805 |
| | Total IBLs | 370,975 | 403,227 | 464,060 | 494,090 | 523,439 |
| | Total non-IBLs | 19,708 | 13,235 | 19,600 | 21,168 | 22,650 |
| | Total liabilities | 390,683 | 416,462 | 483,660 | 515,258 | 546,088 |
| | Share capital | 7,420 | 7,391 | 7,455 | 7,455 | 7,455 |
| | Shareholders' equity | 40,901 | 42,633 | 43,987 | 46,454 | 50,031 |
| | 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 | 1.7 | 1.8 | 1.7 |
| | Total provisions / reported NPLs (%) | 92.6 | 81.3 | 85.1 | 86.3 | 85.4 |
| | CET-1 ratio (%) | 15.8 | 14.4 | 13.6 | 13.6 | 13.3 |
| | Tier-1 ratio (%) | 15.8 | 14.4 | 13.6 | 13.6 | 13.3 |
| | Total capital ratio (%) | 18.4 | 16.6 | 15.8 | 15.7 | 15.2 |

Source: Company data, RHB

Figure 1: 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 | 8,127 | 9,217 | 9,813 | 8,198 | 9,554 | 10,321 | 1% | 4% | 5% |
| Non-interest income | 3,245 | 3,463 | 3,734 | 3,245 | 3,463 | 3,734 | 0% | 0% | 0% |
| Operating expenses | (5,005) | (5,518) | (5,849) | (5,005) | (5,518) | (5,849) | 0% | 0% | 0% |
| PIOP | 6,367 | 7,162 | 7,698 | 6,438 | 7,499 | 8,205 | 1% | 5% | 7% |
| Provision expenses | (640) | (826) | (760) | (640) | (826) | (760) | 0% | 0% | 0% |
| Pretax profit | 5,817 | 6,438 | 7,056 | 5,888 | 6,775 | 7,563 | 1% | 5% | 7% |
| Net profit | 4,662 | 5,272 | 5,776 | 4,719 | 5,549 | 6,192 | 1% | 5% | 7% |
| EPS (SGD) | 2.38 | 2.73 | 3.10 | 2.38 | 2.77 | 3.26 | 0% | 1% | 5% |
| DPS (SGD) | 1.20 | 1.25 | 1.40 | 1.20 | 1.25 | 1.45 | 0% | 0% | 4% |
| Loan growth (%) | 5.5 | 5.0 | 5.5 | 5.5 | 5.0 | 5.5 | | | |
| NIM (%) | 1.90 | 1.98 | 1.98 | 1.92 | 2.05 | 2.08 | | | |
| CIR (%) | 44.0 | 43.5 | 43.2 | 43.7 | 42.4 | 41.6 | | | |
| Credit cost (bps) | 20 | 25 | 21 | 20 | 25 | 21 | | | |

Source: Company data, RHB

Valuation and TP

Our TP is raised to SGD34.90 from of SGD31.40. This is based on a higher intrinsic value of SGD33.57 (from SGD30.18) and a 4% ESG premium based on RHB's in-house ESG methodology.

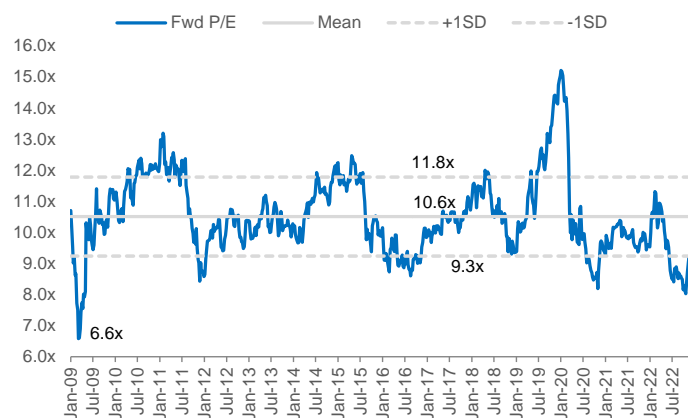
The higher intrinsic value is mainly due to assumptions of a higher ROE of 12.5% (from 11%) following the earnings upgrade, which more than offsets the higher cost of equity of 10.56% (from 10.16%). The GGM-derived P/BV of 1.26x (from 1.12x) is at +1SD from the historical mean.

Figure 2: UOB – GGM valuation with ESG overlay

| | | | |
|--|-------|---------------------------------|-----------------|
| Cost of equity (COE) computation: | | Sustainable ROE (%) | 12.50 |
| Risk free rate (%) | 3.00 | COE (%) | 10.56 |
| Equity premium (%) | 7.20 | Long-term growth (g) | 3.00 |
| Beta (x) | 1.05 | Implied P/BV (x) | 1.26 |
| Cost of equity - CAPM (%) | 10.56 | BVPS – 12-month rolling forward | SGD26.70 |
| | | Intrinsic value | SGD33.57 |
| ESG premium/(discount) (%) | 4.0 | ESG premium/(discount) | SGD1.34 |
| | | TP (rounded) | SGD34.90 |

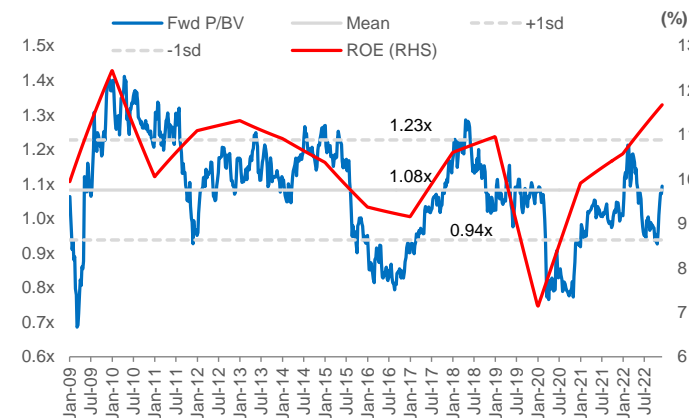
Source: Company data, RHB

Figure 3: UOB's 12-month forward consensus P/E



Source: Bloomberg, RHB

Figure 4: UOB's 12-month forward consensus P/BV



Source: Bloomberg, RHB

16 December 2022

Financial Services | Banks

Recommendation Chart

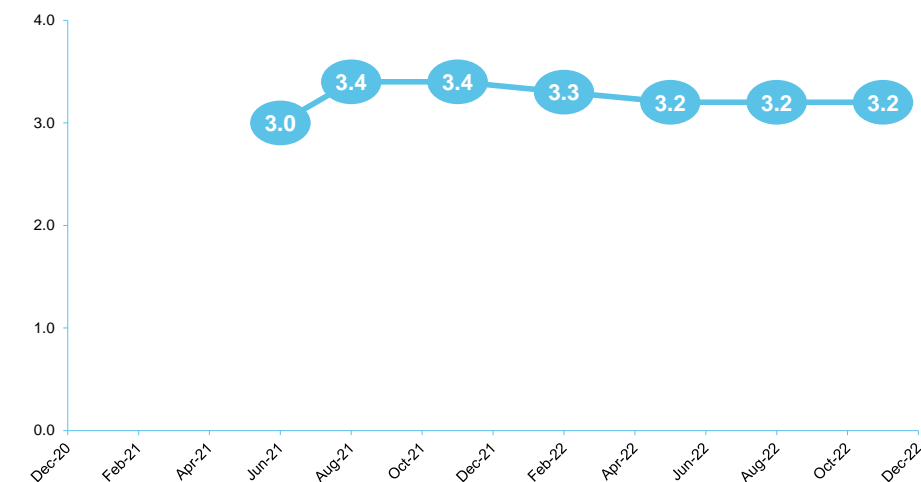


Source: RHB, Bloomberg

| Date | Recommendation | Target Price | Price |
|------------|----------------|--------------|-------|
| 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 |
| 2021-08-05 | Buy | 30.2 | 26.5 |
| 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 |
| 2020-02-04 | Neutral | 25.8 | 25.8 |

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

RHB Guide to Investment Ratings

| | |
|---------------------|--|
| Buy: | Share price may exceed 10% over the next 12 months |
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| 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 |
| Sell: | Share price may fall by more than 10% over the next 12 months |
| Not Rated: | Stock is not within regular research coverage |

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