

United Overseas Bank Limited

Loans growth picked-up pace



13 September 2018

SINGAPORE | BANKING | 2Q18 RESULTS

- 2Q18 PATMI of S\$1,077mn is in line with our forecast of S\$1,067mn.
- NIM expansion, loans growth, and lower allowances were the key earnings drivers.
- NII grew 13.7% YoY on the back of strong loans growth of 9.7% YoY and expansion of NIM by 8bps to 1.83%.
- Upgrade to BUY (previously ACCUMULATE) with a higher target price of S\$34.50 (previous TP S\$31.70), as we raised our ROE and earnings estimates (+6%).**

BUY (Upgraded)

CLOSING PRICE	SGD 26.59
FORECAST DIV	SGD 1.05
TARGET PRICE	SGD 34.50
TOTAL RETURN	33.7%

COMPANY DATA

O/S SHARES (MN) :	1668
MARKET CAP (USD mn / SGD mn) :	33091/ 45216
52 - WK HI/LO (SGD) :	30.37 / 22.79
3M Average Daily T/O (mn) :	2.62

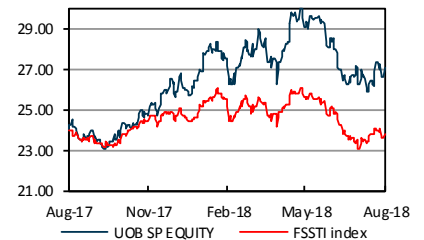
MAJOR SHAREHOLDERS (%)

Wee Investments	7.82%
Wah Hin & Co Pte Ltd	5.15%
Wee Chow Yaw	127%
Vanguard Group Inc/Wayne	104%

PRICE PERFORMANCE (%)

	1M TH	3M TH	1Y R
COMPANY	(0.5)	(10.1)	13.4
STI RETURN	138	(7.83)	0.79

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec	FY 16	FY 17	FY 18 e	FY 19 e
Total Inc (SGDmn)	8,060	8,783	9,669	10,470
Op Profit (SGDmn)	3,769	4,099	5,171	5,693
NPAT (SGDmn)	3,105	3,409	4,321	4,740
EPS (SGD)	183	196	244	264
PER, (X)	11.2	13.6	10.9	10.1
P/BV, (X)	1.1	1.3	1.2	1.2
DPS (SGD)	0.75	1.00	1.05	1.00
ROE, (%)	10.1%	10.2%	11.8%	12.1%

Source: Company Data, PSR est.

Valuation Method:

Gordon Growth Model (ERP: 5.5%; g: 3%)

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Results at a glance

(SGD mn)	2Q18	2Q17	YoY (%)	1Q18	QoQ (%)	Comments
NII	1,542	1,356	14%	1,470	5%	Loans grew 9.7% YoY and NIM rose 4.6% YoY to 1.83%.
Fees & Comm	498	517	-4%	517	-4%	Fund management grew 19.3% YoY and loan fees grew 45.1% YoY. Offset by decline in wealth management fees of 2.9% YoY.
Other Non Int Income	302	311	-3%	243	24%	Net gain from investment securities declined by 99% YoY due to gains on disposal of investment securities last year.
Total Revenue	2,342	2,184	7%	2,230	5%	
Expenses	1,022	995	3%	987	4%	Staff cost rose 13.2% YoY, offset by 10% YoY decline in other operating expense.
Allowances	90	180	-50%	80	13%	Credit cost at 13bps, a decline of 59% YoY from 32 bps. Guidance is at 20bps for the full year.
Net Profit	1,077	845	27%	978	10%	

Source: Company, PSR

The Positives

+ Net interest income enjoyed 13.7% YoY growth. NIM expanded 8bps YoY to 1.83% on a rising interest rate environment. NIM shrunk by 1 bps QoQ but excess funds are expected to be deployed effectively to raise NIM back up above 1.84%, supported by 2 more rate hikes. We have modelled in NIM of 1.86% for FY18e.

+ Loans growth jumped 9.7% YoY, highest in almost 4 years. Loans growth was fairly broad-based and mainly driven by double-digit growth in loans from manufacturing and financial institutions. Greater China was a standout with a 36.9% YoY growth. Due to market headwinds, guidance is still maintained at high-single-digit loans growth for FY18 (PSR estimate +10% YoY).

+ Credit cost at 13bps, a decline of 19bps YoY. After an aggressive provisioning in 2Q17, ECL declined 50% due to a recovering O&G sector. Ongoing O&G recoveries will keep credit cost subdued. But offshore contractors still face the core issue of structural overcapacity. Hence, we forecast credit costs of 19bps for FY18, slightly lower than the guidance of 20bps.

The Negatives

- Non-interest income declined for the first time in 6 quarters. Non-interest income declined 3.4% YoY. Fees income was down 3.7% YoY as wealth management fees retracted 2.9% YoY as customers turned more risk averse due to uncertain market conditions. Net gain from investment securities declined almost 100% YoY due to a one-off gain on disposal of investment securities in 2Q17.

- Expectations of higher dividend payout may be let down. Despite industry high CET1 ratio of 14.5%, the 50 cents per share dividends declared is slightly lower than 50% pay-out guidance. With a new Digital Bank franchise being introduced, capital might be diverted to fund large initial IT expenses. Market uncertainties have made management more vigilant in deploying capital.

Outlook

UOB has introduced a new regional franchise called the Digital Bank. The existing digital banking is an omnichannel way to bank, that serves mainstream customers across all ages. While the new Digital Bank is a mono-channel, mobile-only way to bank that targets mainly the tech-savvy generation Z and Y, by providing an intuitive artificial intelligence interface that remembers and understands your needs. CIR of the new Digital Bank is expected to operate at 35%.

Due to property cooling measures, property transaction volume is expected to slow down in the near term but more noticeably next year. However, housing loans growth this year should still remain strong due to the drawdown of previously approved loans. The balance sheet of major developers remains strong and their credit risk is low. Mortgage loans and building and construction loans contributed to 50% of total loans.

The slowing Chinese economy may contribute to a slight slowdown in trade loans. However, the exposure to Greater China loans is small at 15% of total loans, with domestic loans accounting for 52% of total loans. This slight negative impact could be offset by higher NIM.

All in all, the rising interest rate environment together with higher loans growth and elevated NIM will drive earnings. UOB still maintains a high single-digit loans growth target. The bulk of the growth in FY18e will come from margin expansion and lower impairments.

List of Abbreviations

WM – Wealth Management
IBG – Institutional Banking Group
CBG – Consumer Banking Group
NII – Net Interest Income
Non-II – Non-Interest Income
NIM – Net Interest Margin
ECL – Expected credit loss
CIR – Cost-income ratio
LDR – Loan to Deposit Ratio
NPL – Non-performing Loans
CASA – Current Account, Savings Account
IB – Investment Banking
O&G – Oil and Gas
SP – specific provisions
GP – general provisions
AUM – Asset Under Management
Cost-to-income ratio – CIR

Figure 1: 2018e UOB guidance vs. PSR estimates

Assumptions	2Q18	UOB	PSR	Comment
NIM	1.83	≥1.84	1.86	UOB guides NIM of 1.84% or higher with expectations of 2 more fed rate hikes.
Loans growth	10%	HSD	10%	UOB guides high single digit full year loans growth.
Cost-income ratio	43.6%	42-43%	41.9%	UOB guides similar levels to 2Q18.
Credit Cost	13	20	19	UOB guides full year credit costs at 20 bps.
CET 1	14.90%	> 13.5%	15.0%	50% dividend payout policy guidance is subject to a min CET 1 ratio of 13.5%.
NPL ratio	1.7%	1.7%	1.3%	UOB guides similar levels to 2Q18.

Source: Company, PSR

Investment Actions

Upgrade to BUY (previously ACCUMULATE) with a higher target price of S\$34.50 (previous TP S\$31.70) based on Gordon Growth Model. The improvement in target price was due to our higher ROE assumption (previously 11.1%). Our FY18e earnings forecast is revised upwards by 6.1%.

Valuation: Gordon Growth Model

Item	Description	Value
R _f	Risk-free rate	2.6%
E	Equity-risk premium	5.5%
B	Beta	1.1
COE	Cost of Equity	8.5%
ROE	FY18e Return on Equity	11.8%
g	Terminal growth rate	2.8%
(ROE-g)	FY18e Target Price to Book	1.6
(COE-g)		
	FY18e BVPS, S\$	21.6
	FY18e Valuation, S\$	34.5

Figure 2: Growth in revenue

SGD mn	2Q18	2Q17	YoY (%)	1Q18	QoQ (%)
Net interest income	1,542	1,356	13.7%	1,470	4.9%
Net fee and comm inc	498	517	-3.7%	517	-3.7%
Other non-interest inc	302	311	-2.9%	243	24.3%
Total	2,342	2,184	7.2%	2,230	5.0%

Figure 3: Fee and commission income

SGD mn	2Q18	2Q17	YoY (%)	1Q18	QoQ (%)
Credit card	108	100	8.0%	99	9.1%
Fund management	68	57	19.3%	68	0.0%
Wealth management	132	136	-2.9%	165	-20.0%
Loan-related	148	102	45.1%	141	5.0%
Service charges	37	36	2.8%	36	2.8%
Trade-related	74	66	12.1%	72	2.8%
Other	15	20	-25.0%	20	-25.0%
Total	582	517	12.6%	601	-3.2%

Figure 4: Other non-interest income

SGD mn	2Q18	2Q17	YoY (%)	1Q18	QoQ (%)
Net trading income	215	164	31.1%	175	22.9%
Other income	36	23	56.5%	25	44.0%
Net gain/(loss) from inv. securities	1	76	-98.7%	12	-91.7%
Dividend income	20	18	11.1%	1	1900.0%
Rental income	30	30	0.0%	30	0.0%
Total other non int inc	302	311	-2.9%	243	24.3%

Figure 5: Loans by Industries

SGD mn	2Q18	2Q17	YoY (%)	1Q18	QoQ (%)
Tpt, storage & comms	9,575	9,487	0.9%	9,235	3.7%
Building and construction	57,861	53,063	9.0%	54,883	5.4%
Manufacturing	21,809	16,794	29.9%	19,993	9.1%
Financial institutions	21,558	16,328	32.0%	19,303	11.7%
General commerce	31,470	30,145	4.4%	31,307	0.5%
Professionals & Pri inv	28,851	27,314	5.6%	28,360	1.7%
Housing loans	66,983	62,922	6.5%	66,545	0.7%
Others	11,633	11,687	-0.5%	11,160	4.2%
Total loans	249,740	227,740	9.7%	240,786	3.7%

Figure 6: Loans by currencies

SGD mn	2Q18	2Q17	YoY (%)	1Q18	QoQ (%)
Singapore dollar	118,168	113,610	4.0%	115,514	2.3%
US dollar	49,367	42,330	16.6%	46,402	6.4%
Malaysian ringgit	25,100	23,270	7.9%	24,976	0.5%
Thai baht	14,487	12,946	11.9%	14,473	0.1%
Indonesian rupiah	5,044	5,363	-5.9%	4,769	5.8%
Others	37,572	30,220	24.3%	34,653	8.4%
Total loans	249,738	227,739	9.7%	240,787	3.7%

Figure 7: Profit before tax by Business segments

SGD mn	2Q18	2Q17	YoY (%)	1Q18	QoQ (%)
Group Retail	457	445	2.7%	466	-1.9%
Grp Wholesale	743	539	37.8%	710	4.6%
Global Mkts and IM	72	66	9.1%	60	-20.0%
Others	10	(18)	-155.6%	(49)	-120.4%
Total NPBT	1,282	1,032	24.2%	1,187	8.0%

Figure 8: Profit before tax by Geographical segments

SGD mn	2Q18	2Q17	YoY (%)	1Q18	QoQ (%)
Singapore	770	597	29.0%	679	13.4%
Malaysia	145	154	-5.8%	159	-8.8%
Thailand	60	57	5.3%	77	-22.1%
Indonesia	11	21	-47.6%	40	-72.5%
Greater China	124	98	26.5%	118	5.1%
Others	172	107	60.7%	120	43.3%
Total NPBT	1,282	1,034	24.0%	1,193	7.5%

Source (Figure 2-8): Company, PSR

NIM improvement supported NII growth.

Fund management and loan-related fees maintained double-digit growth but wealth management fees declined for the first time in 7 quarters due to risk aversion.

Net gain from investment securities fell due to a one-off gain on disposal of investment securities a year ago.

Loans growth was fairly broad-based with manufacturing and financial institution loans sustaining double-digit loans growth.

SGD loans growth accelerated mildly while USD loans and trade loans via Hong Kong (under others) grew the fastest.

The wholesale business performed the best.

Singapore contributed 60% of earnings and Greater China 10%.

Financials

Income Statement

Y/E Dec, SGD mn	FY15	FY16	FY17	FY18e	FY19e
Net Int Income	4,925	4,991	5,528	6,323	6,831
Fees and Commission	1,884	1,931	2,092	2,209	2,401
Other Non-int income	1,239	1,138	1,163	1,138	1,238
Total operating income	8,048	8,060	8,783	9,669	10,470
Operating expenses	3,596	3,697	3,957	4,047	4,132
Provisions	671	594	727	451	645
Operating profit	3,781	3,769	4,099	5,171	5,693
Associates & JVs	90	5	110	90	90
Profit Before Tax	3,871	3,774	4,209	5,261	5,783
Taxation	649	669	800	939	1,044
Profit After Tax	3,222	3,105	3,409	4,321	4,740
Non-controlling Interest	12	12	16	20	18
Net Income, reported	3,210	3,093	3,393	4,301	4,721
Net Income, adj.	3,210	3,093	3,393	4,301	4,721

Per share data

Y/E Dec, SGD mn	FY15	FY16	FY17	FY18e	FY19e
EPS, reported	1.94	1.83	1.96	2.48	2.74
EPS, adj.	1.94	1.83	1.96	2.48	2.74
DPS	0.90	0.75	1.00	1.05	1.00
BVPS (less pref shares)	17.84	18.82	20.37	21.63	23.54

Supplementary items

Y/E Dec, SGD mn	FY15	FY16	FY17	FY18e	FY19e
CET1 CAR (%)	13.0%	13.0%	14.7%	15.0%	15.5%
Tier 1 CAR (%)	13.0%	13.1%	16.2%	15.0%	15.5%
Total CAR (%)	15.6%	16.2%	18.7%	17.7%	18.8%

Source: Company, PSR

*Forward multiples & yields based on current market price; historical multiples & yields based on historical market price.

Balance Sheet

Y/E Dec, SGD mn	FY15	FY16	FY17	FY18e	FY19e
Cash bal w central banks	32,306	24,322	26,625	23,183	25,757
Due from banks	28,646	40,033	52,181	47,133	49,667
Investment securities	10,562	11,640	11,273	10,727	10,754
Loans to non-bank cust	203,611	221,734	232,212	255,385	270,319
Others	40,886	42,123	36,027	45,503	45,357
Total Assets	316,011	339,852	358,318	381,932	401,854
Due to banks	11,986	11,855	11,440	12,184	12,306
Due to non-bank cust	240,524	255,314	272,765	290,969	306,938
Debts issued	20,288	26,143	25,178	27,095	27,365
Others	12,289	13,674	12,171	12,536	12,912
Total liabilities	285,087	306,986	321,554	342,784	359,521
Shareholder's equity	30,771	32,876	36,852	38,941	42,108
Non-controlling interest	156	169	187	207	226
Total Equity	30,927	33,045	37,039	39,149	42,333

Valuation Ratios

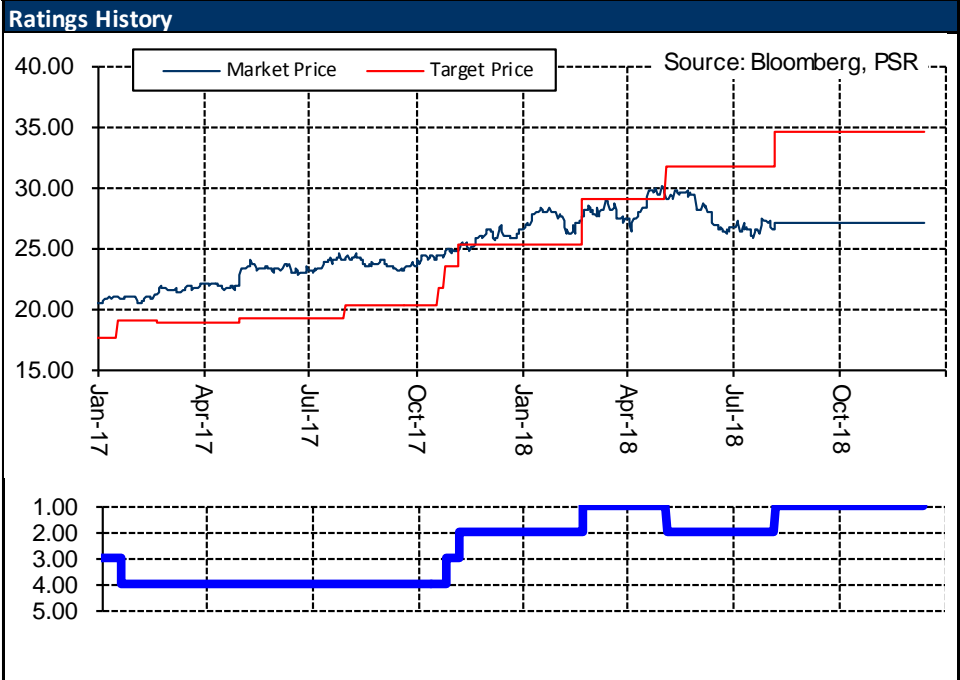
Y/E Dec, SGD mn	FY15	FY16	FY17	FY18e	FY19e
P/E (X), adj.	10.1	11.2	13.6	10.7	9.7
P/B (X)	1.1	1.1	1.3	1.2	1.1
Dividend Yield (%)	4.6%	3.7%	3.8%	3.9%	3.8%

Growth & Margins (%)

Growth					
Net interest income	8.1%	1.3%	10.8%	14.4%	8.0%
Non interest income	7.7%	-1.7%	6.1%	2.8%	8.7%
Pre provision op profit	7.9%	0.1%	9.0%	10.1%	8.3%
Operating income	2.9%	-0.3%	8.8%	26.1%	10.1%
Net income, reported	-1.2%	-3.6%	9.7%	26.8%	9.8%
Margins					
Net interest margin	1.77%	1.71%	1.77%	1.86%	1.90%

Key Ratios (%)

ROE	11.9%	10.1%	10.2%	11.8%	12.1%
ROA	1.0%	0.9%	1.0%	1.1%	1.2%
RORWA	1.6%	1.4%	1.7%	1.9%	2.0%
Non-int/total income ratio	38.8%	38.1%	37.1%	34.6%	34.8%
Cost/income ratio	44.7%	45.9%	45.1%	41.9%	39.5%
Loan/deposit ratio	84.7%	86.8%	85.1%	87.8%	88.1%
NPL ratio	1.39	1.47	1.78	1.29	1.19



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
<-20%	Sell	5

Remarks

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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