

20 November 2024

Financial Services | Banks

United Overseas Bank (UOB SP)

Buy (from Neutral)

Time To Shine; Upgrade To BUY

- **Upgrade to BUY, new TP of SGD40.20 from SGD35.60, 10% upside with c.5% FY25F yield.** United Overseas Bank has lagged peers for a large part of the past 23 months, but we think this trend is set to reverse. We see four factors underpinning its outperformance and further valuation rerating ahead: i) A defensive, ASEAN-centric portfolio; ii) multi-year investments in platforms and synergies from the Citi acquisition are gaining traction and bearing fruit; iii) superior FY25 earnings growth prospects vs the sector; and iv) more aggressive capital returns, thanks to an improved capital position.
- **UOB offers investors a hideout from market volatility...** We think market volatility is likely to persist following the 2024 US presidential election outcome. With a largely ASEAN-centric portfolio (loan book: 49%/22% is domestic/ASEAN-4), UOB may offer investors a defensive shelter to ride through the volatility ahead. RHB Global Economics and Market Strategy (RHB GEMS) generally expects ASEAN economies under coverage to post stable-to-stronger economic growth in 2025 – on sustained strength in trade and manufacturing, tourism activities and policies to support consumption, among others. Trade exposure to the US is relatively low but RHB GEMS does have a caveat that the indirect impact via China could be substantial.
- **...while regional platforms and Citi acquisition bear fruit...** These benefits include positioning the wholesale banking business to better capture connectivity and FDI flows into the region, capturing the rise in retail wealth and further solidifying the group's funding franchise. We believe some of these benefits were evident in the recent 3Q24 results – its loan and CASA growth of +5% YoY and +17% YoY outpaced that of peers.
- **... leading to a positive 2025 outlook.** UOB had guided for higher total income on the back of high single-digit loan growth and double-digit fee growth, CIR at 41-42%, and stable credit cost of 25-30bps. On the back of this, coupled with a further step-down in the cost of the Citi integration, we expect its reported PATMI for FY25 to grow by 6% YoY, ie superior to the flat earnings for the sector. On a core basis, we still forecast FY25 PATMI to rise by 3%, thanks to non-Il prospects. The rise in PATMI and higher dividend payouts assumed supports our +9% DPS growth for FY25F.
- **Further upside potential for shareholder returns from capital management.** While we assume that its dividend payout ratio will rise to 52.5% in 2025 from 51% in 2024F, there could be further upside to capital returns in the form of higher dividends and/or share buybacks, now that UOB has a better line of sight on excess capital, with Basel III reforms having gone live. Also, its 14% mid-term ROE target excludes capital management activities.
- **Earnings forecasts unchanged but TP upped** as we cut our COE assumption by 100bps. This results in a revised GGM-derived P/BV of 1.31x (from 1.16x) – at the higher end of post-global financial crisis (GFC) levels but we think it is deserved, as confidence around UOB's 14% ROE target rises. Our TP includes a 2% ESG premium.

Forecasts and Valuation	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Reported net profit (SGDm)	4,573	5,711	5,855	6,218	6,467
Net profit growth (%)	12.2	24.9	2.5	6.2	4.0
Recurring net profit (SGDm)	4,819	6,061	6,024	6,218	6,467
Recurring EPS (SGD)	2.88	3.62	3.60	3.72	3.87
BVPS (SGD)	25.86	27.64	29.39	31.22	33.10
DPS (SGD)	1.35	1.70	1.79	1.96	2.03
Recurring P/E (x)	12.66	10.07	10.11	9.80	9.42
P/B (x)	1.41	1.32	1.24	1.17	1.10
Dividend Yield (%)	3.7	4.7	4.9	5.4	5.6
Return on average equity (%)	10.6	12.7	12.3	12.3	12.0

Source: Company data, RHB

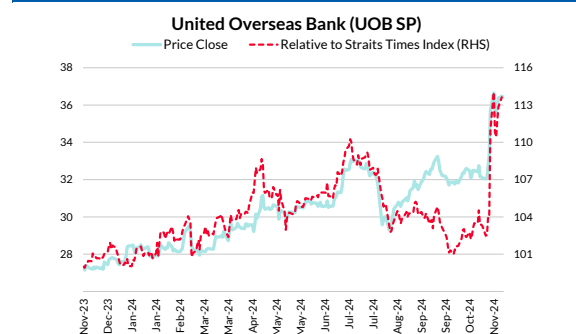
Target Price (Return):	SGD40.20 (+10%)
Price (Market Cap):	SGD36.4 (USD45,281m)
ESG score:	3.2 (out of 4)
Avg Daily Turnover (SGD/USD)	86.0m/65.6m

Analyst

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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	28.0	11.7	18.8	20.4	33.2
Relative	12.8	9.2	7.6	7.8	13.7
52-wk Price low/high (SGD)				27.2	–36.7



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 – with 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.

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Financial Exhibits

Asia	Financial summary (SGD)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Singapore	EPS	2.73	3.41	3.50	3.72	3.87
Financial Services	Recurring EPS	2.88	3.62	3.60	3.72	3.87
United Overseas Bank	DPS	1.35	1.70	1.79	1.96	2.03
UOB SP	BVPS	25.86	27.64	29.39	31.22	33.10
Buy						
Valuation basis	Valuation metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
GGM-derived intrinsic value with an ESG overlay. Key GGM assumptions are:	Recurring P/E (x)	12.66	10.07	10.11	9.80	9.42
i. COE of 10.6%;	P/B (x)	1.4	1.3	1.2	1.2	1.1
ii. ROE of 13%; and	Dividend Yield (%)	3.7	4.7	4.9	5.4	5.6
iii. 3.0% long-term growth						
Key drivers	Income statement (SGDm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Our net profit forecasts is most sensitive to changes in:	Interest income	12,862	22,242	22,393	22,010	21,771
i. Impairment charges	Interest expense	(4,519)	(12,563)	(12,719)	(12,298)	(11,967)
ii. NIM	Net interest income	8,343	9,679	9,674	9,712	9,803
iii. Non-II growth	Non interest income	3,232	4,253	4,549	4,893	5,329
	Total operating income	11,575	13,932	14,223	14,605	15,133
	Overheads	(4,971)	(5,797)	(6,069)	(6,242)	(6,429)
	Pre-provision operating profit	6,604	8,135	8,154	8,363	8,704
	Loan impairment allowances	(628)	(783)	(800)	(850)	(850)
	Other impairment allowances	22	(162)	(45)	(41)	(40)
	Income from associates	97	93	100	130	140
	Other exceptional items	(310)	(420)	(208)	-	-
	Pre-tax profit	5,785	6,863	7,201	7,602	7,954
	Taxation	(1,202)	(1,138)	(1,332)	(1,368)	(1,471)
	Minority interests	(10)	(14)	(14)	(16)	(15)
	Reported net profit	4,573	5,711	5,855	6,218	6,467
	Recurring net profit	4,819	6,061	6,024	6,218	6,467
Company Profile	Profitability ratios	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
United Overseas Bank is the third largest Singapore bank by asset size. It also has significant operations in Malaysia, Thailand and Indonesia.	Return on average assets (%)	0.9	1.1	1.1	1.1	1.1
	Return on average equity (%)	10.6	12.7	12.3	12.3	12.0
	Return on IEAs (%)	3.0	5.0	4.9	4.6	4.4
	Cost of funds (%)	1.1	2.8	2.8	2.6	2.4
	Net interest spread (%)	2.0	2.2	2.2	2.1	2.0
	Net interest margin (%)	2.0	2.2	2.1	2.1	2.0
	Non-interest income / total income (%)	27.9	30.5	32.0	33.5	35.2
	Cost to income ratio (%)	42.9	41.6	42.7	42.7	42.5
	Credit cost (bps)	19.9	24.4	24.5	24.9	23.5
	Balance sheet (SGDm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Total gross loans	319,663	321,150	330,785	350,632	371,669
	Other interest earning assets	116,707	125,723	130,670	135,313	139,868
	Total gross IEAs	436,370	446,873	461,455	485,945	511,537
	Total provisions	(4,308)	(4,145)	(4,317)	(4,512)	(4,677)
	Net loans to customers	315,355	317,005	326,468	346,120	366,992
	Total net IEAs	432,062	442,728	457,138	481,433	506,860
	Total non-IEAs	72,198	80,792	83,729	90,277	97,398
	Total assets	504,260	523,520	540,867	571,710	604,258
	Customer deposits	368,553	385,469	397,033	420,855	446,106
	Other interest-bearing liabilities	65,918	69,551	71,293	74,081	77,006
	Total IBLs	434,471	455,020	468,326	494,936	523,112
	Total non-IBLs	26,183	22,032	23,134	24,290	25,505
	Total liabilities	460,654	477,052	491,459	519,226	548,617
	Share capital	7,855	7,752	7,752	7,752	7,752
	Shareholders' equity	43,366	46,226	49,152	52,212	55,354
	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	15.9	15.9	15.9
	Tier-1 ratio (%)	14.4	14.4	15.9	15.9	15.9
	Total capital ratio (%)	16.7	16.6	18.0	18.0	17.9

Source: Company data, RHB

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Valuation and TP

We lower our COE assumption to 10.6% from 11.6%, leading to a revised GGM-derived P/BV of 1.31x (vs. 1.16x previously) and higher intrinsic value of SGD39.43 (from SGD34.91). UOB's defensive portfolio amid a volatile market, benefits from investments filtering through, and commitment to capital management are key rerating catalysts for the stock. Although our GGM-derived P/BV is at the higher end of its post-GFC valuation levels, we think this is well deserved, especially as confidence around management's 14% ROE target rises.

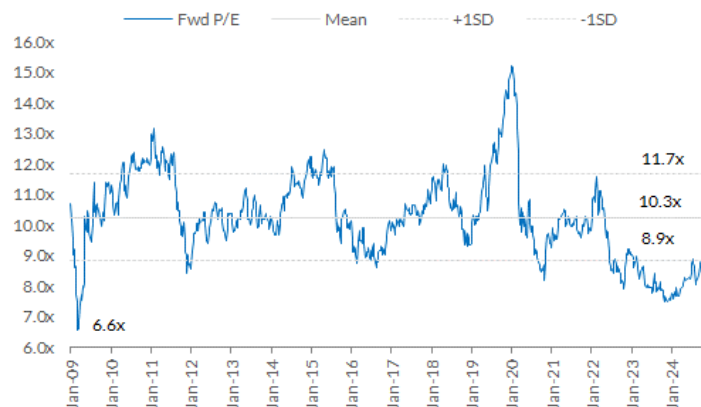
Imputing an unchanged 2% ESG premium to the stock's intrinsic value results in a new TP of SGD40.20 (previously SGD35.60). The premium ascribed reflects UOB's ESG score of 3.2 out of 4.0, in accordance with our proprietary in-house methodology.

Figure 1: UOB – GGM valuation with ESG overlay

Cost of equity (COE) computation:		Sustainable ROE (%)	13.0
Risk free rate (%)	3.0	COE (%)	10.6
Equity premium (%)	8.3	Long-term growth (g)	3.0
Beta (x)	1.04	Implied P/BV (x)	1.31
Cost of equity - CAPM (%)	10.6	BVPS – FY25F	SGD30.14
		Intrinsic value	SGD39.43
ESG premium/(discount) (%)	2.0	ESG premium/(discount)	SGD0.79
		TP (rounded)	SGD40.20

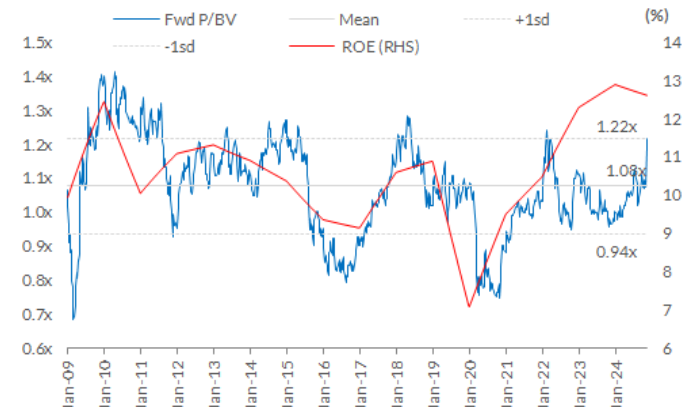
Source: Company data, RHB

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.

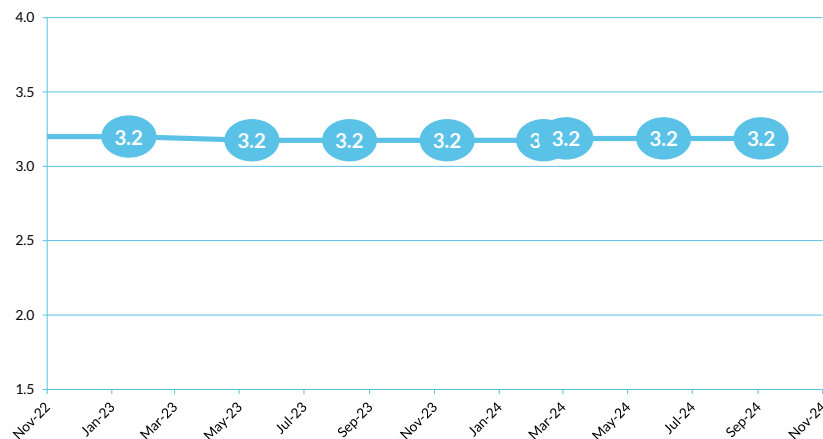
Emissions (tCO ₂ e)	Dec-21	Dec-22	Dec-23
Scope 1	4,300	5,800	4,800
Scope 2	1,000	1,100	1,600
Scope 3	600	4,000	14,100
Total emissions	5,900	10,900	20,500

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

ESG Rating History



Source: RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2024-11-10	Neutral	35.6	35.7
2024-07-22	Neutral	32.0	32.6
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

Source: RHB, Bloomberg

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