Singapore Industry Focus

Singapore Banks

Refer to important disclosures at the end of this report

DBS Group Research . Equity

4 Dec 2018

At the crossroads

- Three trends to watch in 2019: (1) NIM expansion as key earnings driver; (2) credit costs normalising; (3) loan growth moderating from high base
- Higher dividend payout ratio and dividend yield to support share prices
- Singapore banks trading near 1S.D. below 10-year average P/BV multiple
- BUY ratings for both UOB and OCBC; prefer UOB

Sustainability of net interest margin (NIM) expansion and asset quality hold the key to Singapore banks' valuations. We believe sustainability of (1) NIM expansion, and (2) asset quality will determine Singapore banks' valuations. We are projecting that NIM will be on an uptrend in 2019 and expect c.6-7bps improvement y-o-y in 2019 at the minimum (2018F: + c.8bps y-o-y). Our sensitivity analysis indicates that every 25-bp rise in interest rates that reprices the S$, HK$ and US$ books collectively would lift NIM by 3bps with a corresponding 2% increase in sector earnings. We expect credit costs to trend higher y-o-y, inching towards more normalised levels in the coming year due to the low base in 2018. We continue to keep watch on SME loans as an increase in non-performing loans (NPLs) may be reflective of a slowing economy. Asset quality stability and higher earnings growth (above historical average) in FY19-20F should drive Singapore banks' valuations towards 10-year average P/BV multiples.

Expect loan growth to moderate from high base. Both UOB and OCBC reported YTD loan growth of c.8% in 3Q18 (c.10% annualised). Loan growth should continue to be supported by drawdowns from property development projects and regional corporate loans, but is likely to moderate to c.6-7% in 2019 for the following reasons: (1) decline in new home sales post implementation of property cooling measures, and (2) weaker business sentiment arising from US-China trade war. In the longer term, we continue to see Singapore banks as potential beneficiaries from trade diversion into the Southeast Asian region.

Prefer UOB to OCBC. Dividend yields should support share prices, with UOB offering close to 5% yield and OCBC at c.4%. Although we have BUY ratings on both UOB and OCBC, we prefer UOB for the following reasons: (1) strong capital position and building up its liquidity buffers; (2) continuous growth in loan book and NIM expansion expected; (3) defensive pick as it has a smaller exposure to China among the local banks and more defensive wealth management franchise. Our BUY rating on OCBC is premised on (1) ongoing NIM expansion on full impact of loan repricing; (2) stronger capital position post scrip dividend issue (now in line with peers); (3) potentially higher dividends as a price catalyst.

Key risks: NIM fails to deliver as expected; worsening US-China trade relations and less firm macroeconomic outlook to pose downside risks to loan growth; deteriorating credit environment; sharp slowdown in the Singapore property market.

STI : 3,190.62

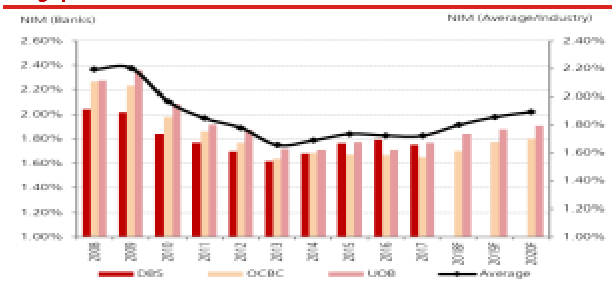
Analyst
Rui Wen LIM +65 66823720
ruiwenlim@dbs.com

STOCKS

	Price	Mkt Cap	12-mth Target Price	Performance (%)		Rating
	S$	US$m	S$	3 mth	12 mth	
DBS	25.11	46,873	NR	0.6	2.2	NR
OCBC Bank	11.60	36,082	13.20	3.1	(6.6)	BUY
UOB	25.98	31,688	29.50	(3.0)	(2.1)	BUY

Source: DBS Bank, Bloomberg Finance L.P. Closing price as of 3 Dec 2018

Singapore Banks: NIM trends

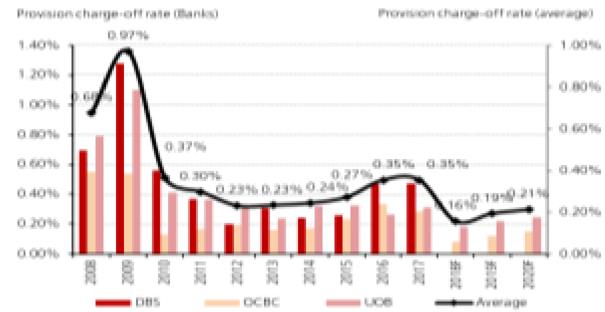


No forecasts for DBS *Source: Companies, DBS Bank*

Singapore Banks: Loan growth

Source: Companies, DBS Bank

Singapore Banks: Credit costs



Source: Companies, DBS Bank

Live more, Bank less

ed: JS/ sa: YM, CW, CS

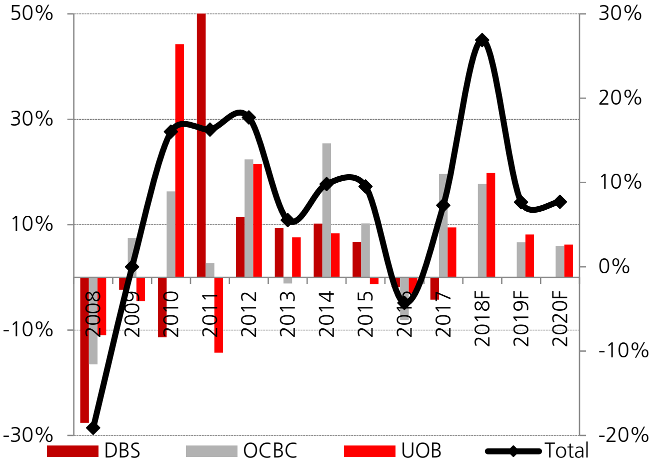
Trends to watch in 2019

Singapore banks' share prices have corrected >20% from the peak, now trading near 1S.D. below 10-year average P/BV multiple. Singapore banks' share prices rallied earlier in the year on the back of NIM expansion expectations, strong loan growth, and benign credit environment. Since then, share prices have corrected >20% from their peak in May 2018 on US-China trade war concerns, fears of China slowdown, and to a lesser extent, Singapore property cooling measures. Will 2019 be a better year? We believe the sustainability of (1) NIM expansion and (2) asset quality hold the key to Singapore banks' valuations. Singapore banks are now trading near 1S.D. below their 10-year average P/BV multiple. We believe sustained NIM expansion and continuing benign credit environment should drive Singapore banks' valuations towards 10-year average P/BV multiples, on the back of expectations of above historical average earnings growth in FY19-20F. Attractive dividend yields should also lend support to share prices, with UOB offering close to 5% and OCBC with c.4%.

Continues to deliver resilient earnings. We believe that Singapore banks will continue to deliver resilient earnings, having come from a high base as FY2018F is a record year with c.27% y-o-y earnings growth expected (excluding exceptional items in FY2017). We expect Singapore banks to deliver earnings growth of c. 8% in FY2019. While growth in non-interest income may moderate as a result of weaker market-related income, stronger net interest income and low credit costs should continue to support earnings.

Prefer UOB for its strong dividend yield. Although we have BUY ratings on both UOB and OCBC, we prefer UOB for the following reasons: (1) higher dividend yield versus OCBC, (2) strong capital position; building up its liquidity buffers as it continues to grow loan book and NIM, (3) defensive pick as it has a smaller exposure to China among the local banks and a more defensive wealth management franchise. Our BUY rating on OCBC is premised on (1) ongoing NIM expansion on full impact of loan repricing, (2) stronger capital position post scrip dividend issue (now in line with peers), (3) higher dividends could be a share price catalyst.

Singapore Banks: Earnings trend



Source: Companies, Bloomberg Finance L.P., DBS Bank

Key Risks

NIM fails to deliver. We have been positive on NIM uplift in a rising interest rates environment for some time. A slower-than-expected pass-through of Fed rate hikes to SIBOR/SOR could also derail the NIM uptrend, apart from slower-than-expected rate hikes. Competition in loan rates could be an added dent to NIM. Higher than expected pickup in cost of funds, especially in the SGD fixed deposits space, could also potentially slow down the NIM expansion trajectory.

Asset quality deterioration. While the current environment remains benign, any deterioration in asset quality could hurt banks' bottom lines. We continue to keep a lookout particularly the small medium enterprises' (SMEs) loan books as any increase in the level of delinquencies might be a leading indicator of a slowing economy. There might be concerns over the banks' Greater China exposure, which account for c.26% and c.15% of total loans at OCBC and UOB respectively (as of Sep 2018), should China's slowdown become more pronounced.

Slower-than-expected loan growth. Disappointment in macro indicators and a less firm macroeconomic outlook going forward could temper our current loan growth expectations. Although loan growth is less sensitive to earnings, any loan deceleration as a result of weaker sentiment would dent top-line prospects. A sharp slowdown in Singapore property market will also derail property-related loan growth.

Singapore Banks: 10-year valuation range (12-mth forward P/BV)

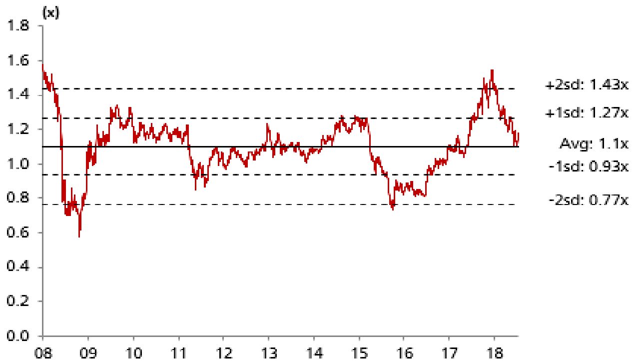
	Trough	-2 S.D.	-1 S.D.	Mean
DBS	0.58	0.77	0.93	1.10
OCBC	0.72	0.87	1.06	1.25
UOB	0.73	0.81	1.03	1.24

Source: Companies, Thomson Reuters Datastream, DBS Bank

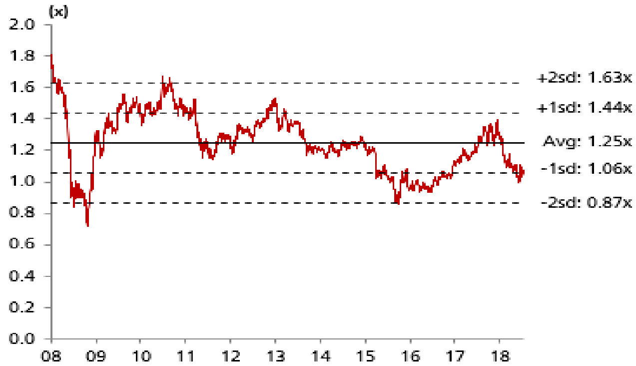
Singapore Banks: Rolling forward P/BV band (10-year)

Source: Bloomberg Finance L.P., DBS Bank (as of 28 Nov 2018)

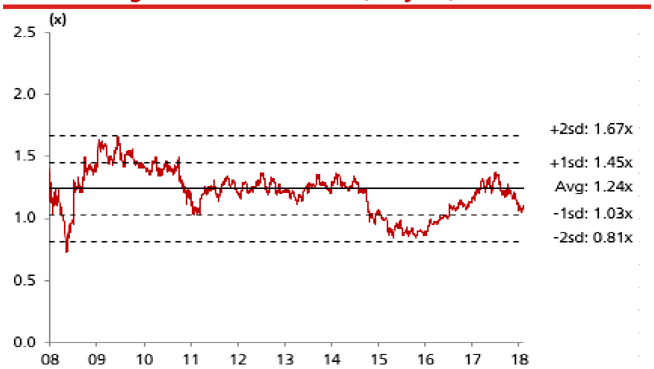
DBS: Rolling forward P/BV band (10-year)



OCBC: Rolling forward P/BV band (10-year)



UOB: Rolling forward P/BV band (10-year)



Source: Bloomberg Finance L.P., DBS Bank (as of 28 Nov 2018)

Singapore Banks: Peer Valuation

	Market cap	Price	12 mth Target Price	Rating	PE (x)			CAGR^ (%)	PBV (x)			ROE (%)	Net div (%)
	(US$m)	(S$/s)	(S$/s)		FY17A	FY18F	FY19F		FY17A	FY18F	FY19F	FY19F	FY19F
DBS*	45,627	24.38	NA	NR	13.0x	10.4x	9.3x	18%	1.3x	1.2x	1.2x	12.6%	4.9%
OCBC	34,938	11.26	12.40	BUY	11.1x	9.2x	8.7x	13%	1.2x	1.1x	1.1x	11.6%	3.6%
UOB	30,808	25.15	31.70	BUY	11.6x	9.4x	8.9x	14%	1.1x	1.1x	1.1x	11.5%	4.8%
Simple average					12.4x	10.1x	9.4x		1.2x	1.2x	1.1x	11.9%	4.6%
Weighted average					12.6x	10.2x	9.4x		1.3x	1.2x	1.1x	12.0%	4.7%

^ Refers to 2-year EPS CAGR for FY17-19F   ** Based on Bloomberg consensus*
Source: Companies, Bloomberg Finance L.P., DBS Bank (as of 28 Nov 2018)

(1) SIBOR rally continues, NIM expansion story should remain intact

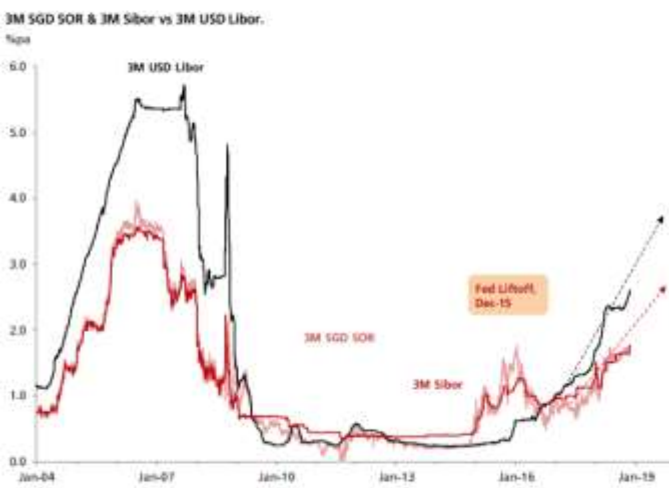
Higher pass-through seen in 2018; more room for SIBOR/SOR to head higher. We finally saw the impact of higher Fed Fund rates in 2018 translating to higher LIBOR and SIBOR/SOR with a stronger pass-through as USD continues to strengthen against SGD. As 3MLIBOR rises to factor in a December rate hike (and to a lesser extent, tighter funding conditions towards the end of the year), some pass-through can be seen in SGD rates. We continue to see 3MSIBOR/SOR having more room to head higher, with 3MSIBOR heading to 2.70% by end of 2019 according to DBS Group Research's forecast, after gaining c.26bps since the start of 2018. We still see strength in USD, and with more rate hikes in 2019 (consensus is currently expecting two rate hikes), this should bode well for sustained rise in SIBOR/SOR.

Effect of ongoing loans repricing to be seen in following quarters… Meanwhile, we believe that ongoing loans repricing should continue to support increases in loan yields as floating rate loans are repriced on a higher benchmark rate, while fixed rate loans that reach maturity are also repriced based on higher benchmark rates. Recall that it takes up to 90 days for a full re-pricing to take place, hence we expect the effect of ongoing repricing to be seen in the next few quarters as benchmark rates continue to tick up.

… and increase in loan yields should outpace the rise in cost of funds, translating to higher NIM. We believe that the NIM expansion story is still intact, even though in 2018, NIM quarterly trends across the banks have diverged from quarter to quarter (recall that OCBC's NIM was flat for three quarters since 4Q17 before spiking in 3Q18 as OCBC repriced its mortgage loans later than the other banks, also in part due to excess USD liquidity); UOB on the other hand saw steady NIM expansion through 2017 and 1Q18, and slight decline in NIM in the last two quarters as it built up liquidity buffers in anticipation of increased competition in the deposits space towards year-end, and loan pipeline.

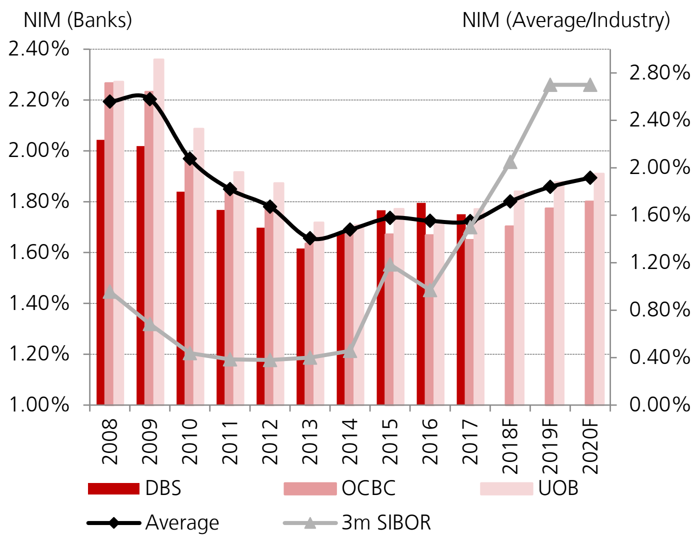
While SGD fixed deposit (which contributes meaningfully to OCBC and UOB's funding strategy) rates have also been on the rise since the start of the year, we believe that putting aside quarter-on-quarter movements, directionally, the increase in loan yields should outpace the rise in cost of funds. We believe that NIM is on an uptrend in 2019 and expect c.6-7bps improvement y-o-y in 2019 at the minimum (2018F: c.8bps improvement y-o-y). Our sensitivity analysis indicates that every 25-bp rise in interest rates that reprices the S$, HK$ and US$ books collectively would lift average NIM by 3bps with a corresponding 2% increase in sector earnings.

3-month SIBOR, SOR and LIBOR; correlation has strengthened



Source: Bloomberg L.P. Finance, DBS Bank

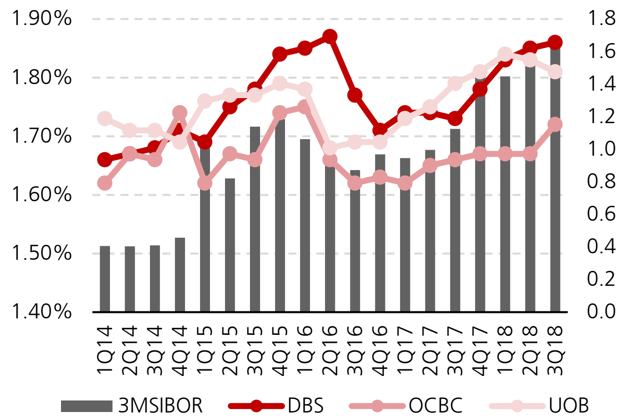
Singapore Banks: NIM on an uptrend



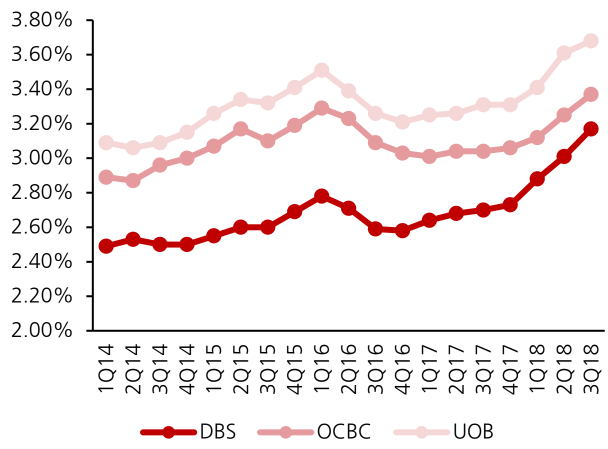
Source: Bloomberg L.P. Finance, DBS Bank

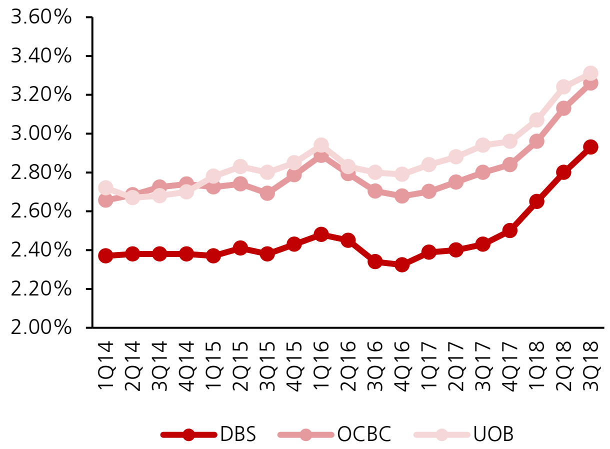
Singapore Banks: Margin trends (quarterly)

NIM (%) v 3MSIBOR

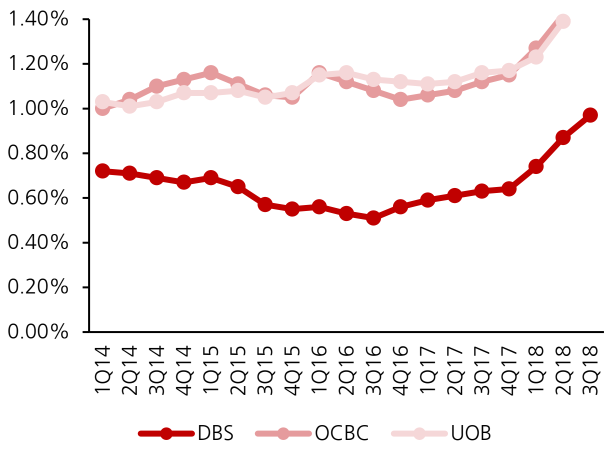


Loan yield (%)

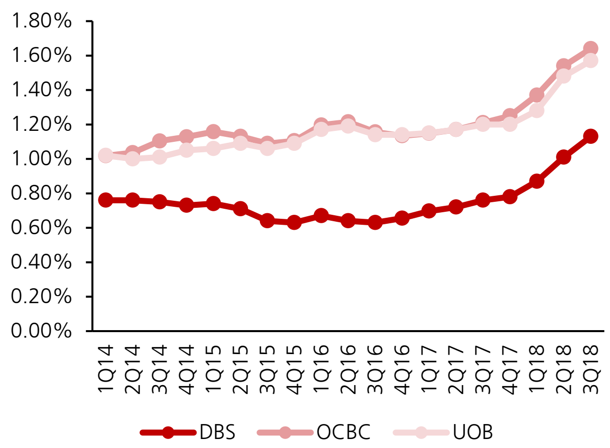




Deposit cost (%)



Cost of funds (%)



Source: Companies, DBS Bank

(2) Credit cost remains low amid benign credit environment

(2) Credit cost remains low amid benign credit environment
New NPL formation largely stable, credit environment remains benign. New NPL formation as well as NPL ratio among the banks were largely stable throughout 2018 as the credit environment remains benign. The banks have performed various stress tests using trade war scenarios, as well as their Greater China exposure and are keeping their eyes on the potentially vulnerable names.

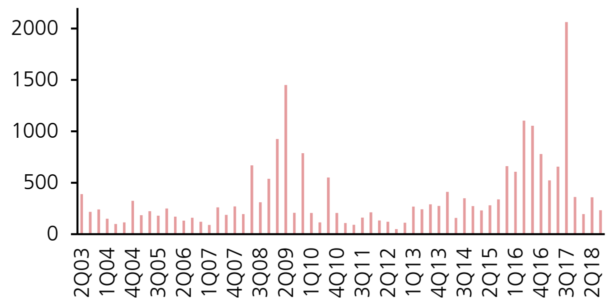
Keep watch on SME loan book. In 3Q18, OCBC highlighted that while NPLs on new non-mortgages are largely scattered and not concentrated in any particular industry, and attributable to a few small manufacturing companies and a palm oil-related company, going forward, there may be concerns of a general slowdown in the economy depending on developments in the US-China trade tensions. UOB is also closely monitoring accounts that show some vulnerability, and assessing the need to make provisions for some of these accounts. We continue to keep a watch on SME loan books. However, we note that SME loans are generally well secured and expect any NPLs to be contained.

Credit costs likely to trend towards more normalised levels. Credit costs were at a record low in 2018 with the implementation of IFRS9/SFRS109 alongside stable NPL formation. We continue to see a largely benign credit environment in 2019, though we believe that credit costs should still inch higher y-o-y towards more normalised levels in the coming year. UOB and OCBC are guiding for credit costs of 20-25bps and 12-15bps for FY2019F (3Q18 - UOB: 18bps; OCBC: 8bps) respectively, still below historical through-the-cycle levels of c.32bps and c.18bps. We forecast credit costs to come in at the lower end of the guidance range at 12bps and 20bps respectively for OCBC and UOB in FY2019F.

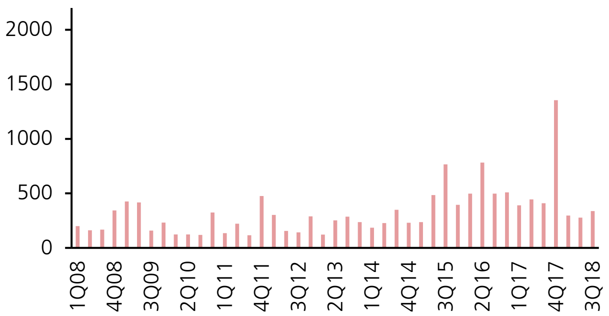
NPL coverage ratio remains healthy, though below historical levels. With the implementation of IFRS9/SFRS109, NPL coverage ratio of Singapore banks is now at c.80-90%. In our view, though the NPL coverage ratio is below historical levels of typically ≥100%, it remains healthy compared to regional peers.

Singapore Banks: New NPL formation

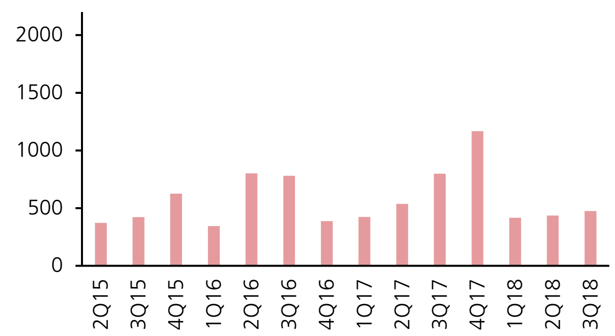
DBS



OCBC

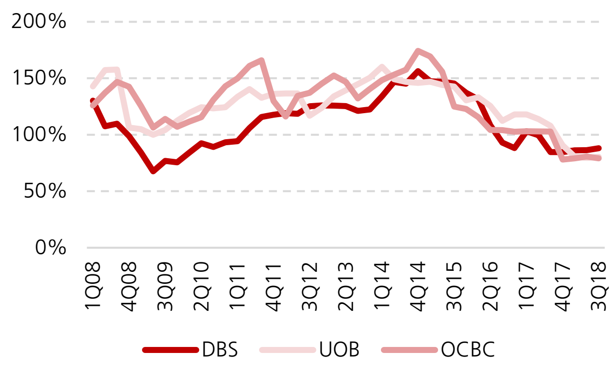


UOB



Source: Companies, DBS Bank

Singapore Banks: NPL coverage ratio



3) Loan growth to moderate from high base

Singapore banks benefitted from broad-based loan growth. Both UOB and OCBC saw YTD loan growth of c.8% in 3Q18 (c.10% annualised), supported by both domestic and ex-Singapore loans. Loan growth was broad-based, including building and construction loans, loans to financial institutions, investment and holding companies amongst others. UOB benefitted from strong growth in loans to manufacturing, while OCBC saw strong growth in general commerce, transportation, storage and communications loans.

Growth to moderate in 2019. We believe that loan growth will continue to be supported by drawdowns from property development projects and regional corporate loans, but moderating to c.6-7% for the Singapore banks in 2019 for the following reasons: (1) decline in new home sales post implementation of property cooling measures, and (2) potential impact on business sentiment arising from US-China trade war. In the longer term, we continue to see Singapore banks as potential beneficiaries from trade diversion into the Southeast Asian region. Sensitivity of loan growth to earnings is marginal (every 1-ppt increase in loan growth leads to only less than 1% impact on earnings).

Singapore Banks: Loan growth trend

Source: Companies, Bloomberg L.P. Finance, DBS Bank

Singapore Banks: Loan breakdown by industry (3Q18)

By sector (S$m)	DBS	%	y-o-y%	q-o-q%	UOB	%	y-o-y%	q-o-q%	OCBC*	%	y-o-y%	q-o-q%	Dom bks	%	y-o-y%	q-o-q%
Manufacturing	35,461	10%	5.7%	0.8%	21,507	8%	13.5%	-1.4%	16,399	6%	26.2%	8.1%	73,367	9%	16.3%	8.7%
Building & Construction	73,019	21%	16.8%	3.7%	60,174	24%	12.1%	4.0%	51,463	20%	46.0%	25.7%	184,656	22%	22.9%	15.6%
Housing loans	74,485	22%	6.5%	0.7%	67,631	27%	5.8%	1.0%	65,553	26%	5.7%	-0.5%	207,669	24%	10.0%	1.2%
General commerce	50,764	15%	-0.1%	-4.5%	32,365	13%	6.8%	2.8%	34,959	14%	26.5%	10.5%	118,088	14%	11.3%	4.1%
Transportation, storage & communications	30,474	9%	4.0%	-0.8%	9,996	4%	3.0%	4.4%	13,832	5%	13.4%	24.4%	54,302	6%	3.9%	10.5%
Financial institutions, investment & holdings companies	21,506	6%	37.8%	5.2%	22,698	9%	25.2%	5.3%	20,801	8%	-43.7%	-46.3%	65,005	8%	1.8%	-19.6%
Professionals & individuals	31,349	9%	11.8%	0.1%	28,934	11%	4.0%	0.3%	30,698	12%	9.9%	-0.7%	90,981	11%	13.4%	2.5%
Others	28,043	8%	-3.5%	2.1%	11,816	5%	1.9%	1.6%	22,871	9%	31.1%	27.3%	62,730	7%	5.6%	12.5%
Total	345,101	100%	8.2%	0.7%	255,122	100%	9.0%	2.2%	256,576	100%	10.4%	1.7%	856,799	100%	12.2%	4.4%

By currency	DBS	%	y-o-y%	q-o-q%	UOB	%	y-o-y%	q-o-q%	OCBC	%	y-o-y%	q-o-q%	Dom bks	%	y-o-y%	q-o-q%
Singapore dollar	139,526	40%	5.6%	1.4%	119,752	47%	4.3%	1.3%	90,067	35%	7.5%	1.3%	349,345	41%	8.0%	2.2%
US dollar	109,460	32%	8.7%	1.5%	50,377	20%	10.9%	2.0%	67,907	26%	11.7%	4.2%	227,744	27%	12.1%	7.5%
Malaysian ringgit	-	-	-	-	24,929	10%	7.0%	-0.7%	20,942	8%	4.2%	-0.6%	45,871	5%	5.8%	0.0%
Indonesia rupiah	-	-	-	-	5,014	2%	-2.9%	-0.6%	8,437	3%	10.4%	0.5%	13,451	2%	3.3%	6.7%
Hong Kong dollar	41,366	12%	12.0%	-0.7%	-	-	-	-	35,714	14%	12.6%	-0.8%	77,080	9%	17.9%	6.6%
Chinese Yuan	12,166	4%	17.7%	-5.9%	-	-	-	-	4,708	2%	-10.9%	-7.0%	16,874	2%	7.5%	-1.0%
Other	42,583	12%	9.9%	-0.1%	55,049	22%	21.2%	5.7%	28,801	11%	24.7%	3.9%	126,433	15%	26.5%	6.5%
Total	345,101	100%	8.2%	0.7%	255,122	100%	9.0%	2.2%	256,576	100%	10.4%	1.7%	856,799	100%	12.2%	4.4%

Source: Companies, DBS Bank
**OCBC saw reclassification in 3Q18 where exposure to investment and other holding companies were re-categorised to the underlying industries*

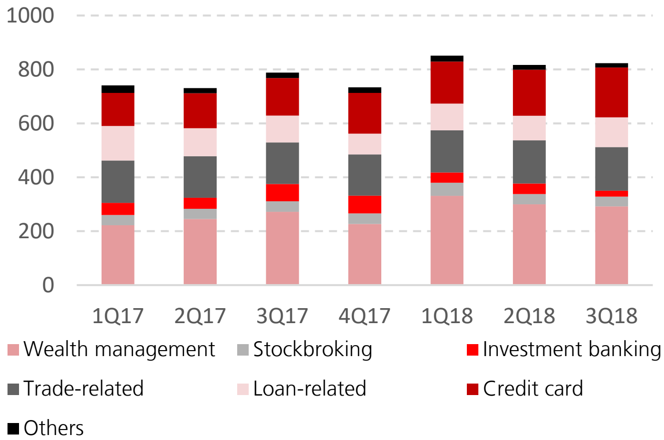
4) Market conditions may affect some portion of non-interest income; overall growth trend for non-interest income intact

Softer wealth management income, trading income. We are starting to see how market condition has affected parts of non-interest income across the banks, such as mark-to-market losses in UOB due to accounting asymmetry in its hedges.

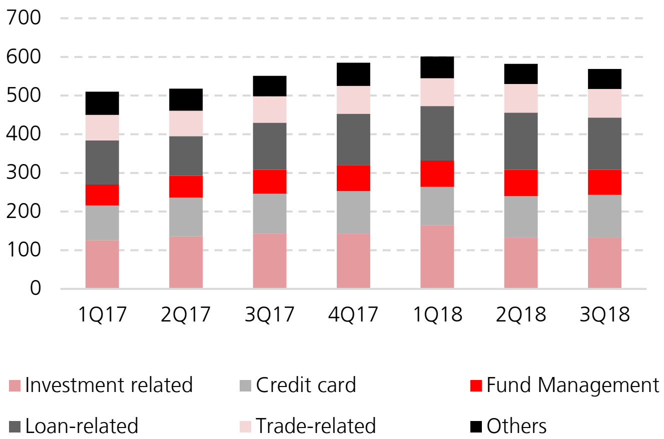
Generally, wealth-related income momentum was also softer. However, the overall growth trend is intact for non-interest income, especially for wealth management which remains a growth area for the Singapore banks. (See section on *Growing wealth management income*)

Singapore Banks: Quarterly fee income trend (S$m)

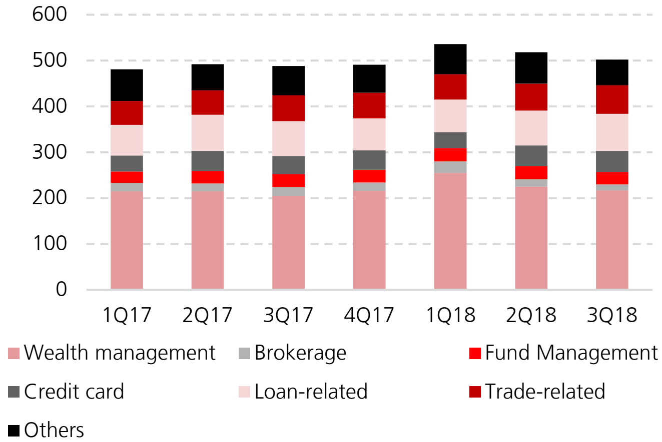
DBS



UOB



OCBC



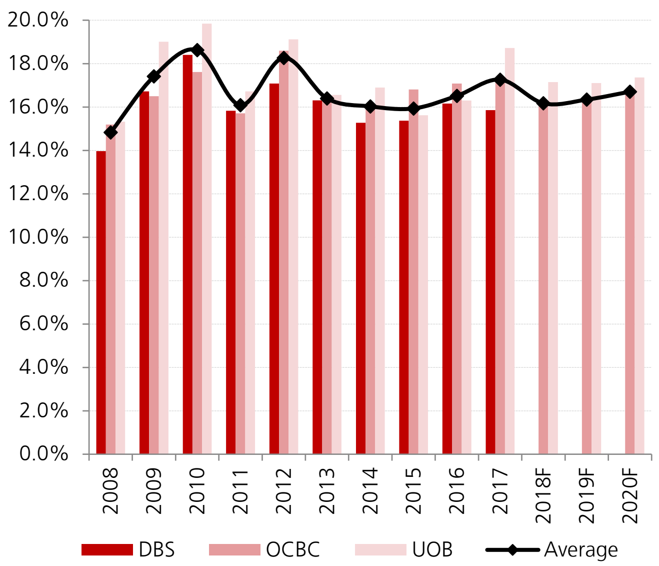
Source: Companies, Bloomberg L.P. Finance, DBS Bank

5) Capital and dividends

Strong capital position. In 3Q18, all Singapore banks recorded CET1 ratios of above 13.0%, with UOB having the highest ratio at 14.1%, which is above its comfortable range of 12.5% to 13.5%. While OCBC's CET1 ratio has been lower than its peers, since OCBC commenced scrip dividends in 2Q18, its CET1 ratio improved to 13.6% in 3Q18, above management's comfortable range, which is similar to UOB's.

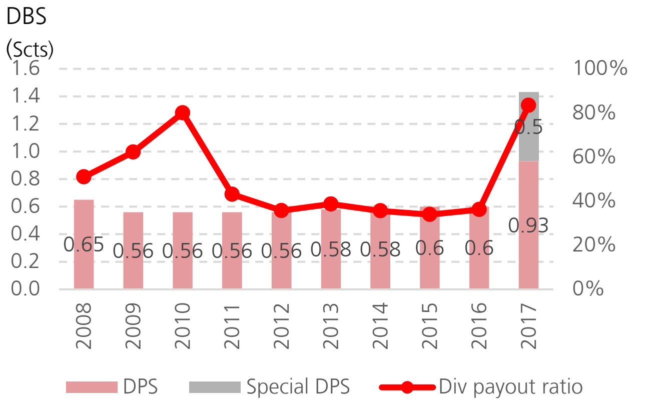
Upside to dividends. During FY2018, UOB committed to a new dividend payout ratio of c.50% (of net profit), subject to minimum CET1 ratio of 13.5% and sustainable business performance. UOB would be paying more dividends in 2H18 than 1H18 where it paid <50% of net profit. For OCBC, its dividend payout ratio has been c. 37% and with management reaffirming their commitment to a steady, predictable quantum of 40-50% dividend payout ratio, we believe that there may be potential for higher dividends now that OCBC has shored up its capital. At 40% dividend payout ratio, this translates to c.44 Scts (FY2017: 37 Scts). We believe Singapore banks' strong dividend yield of c.4-5% provides strong support to their share prices.

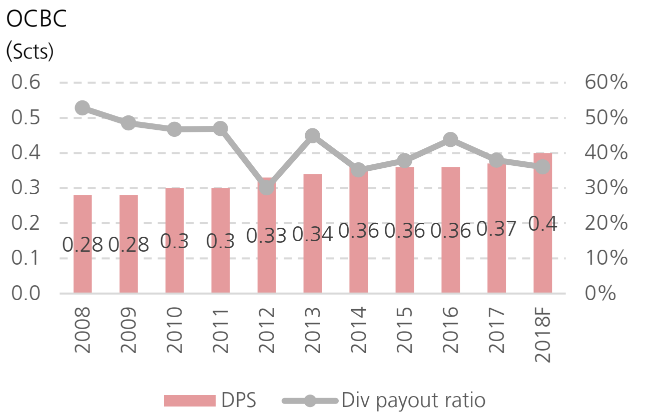
Singapore Banks: Total capital ratios

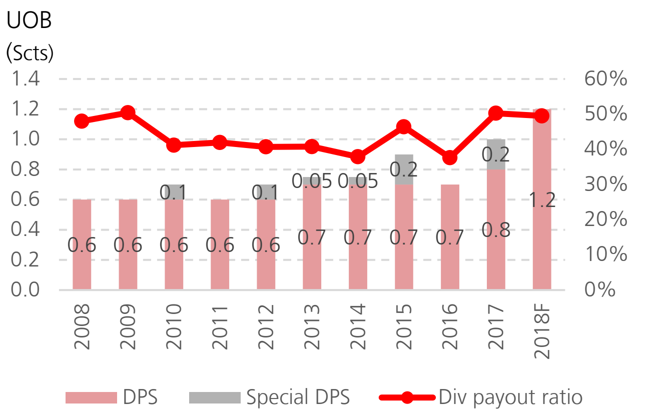


Source: Companies, DBS Bank

Singapore Banks: Dividends and payout ratio





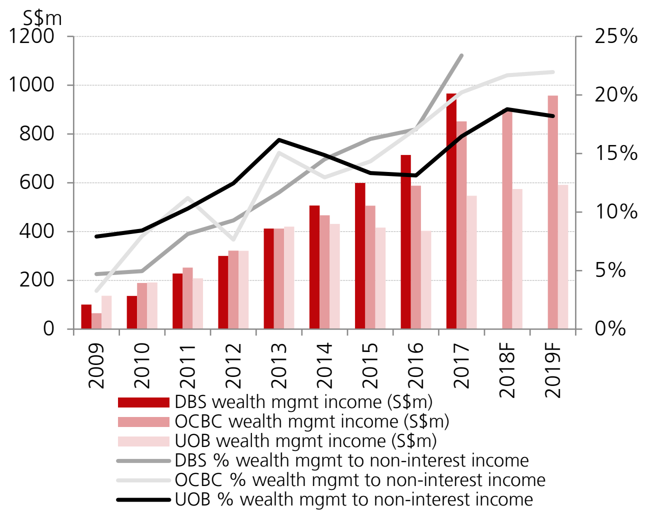


Source: Companies, Bloomberg L.P. Finance, DBS Bank

Growing wealth management income

Wealth management continues to be a growth driver. In the last eight years, wealth management has grown from a small fraction to nearly one-third of total fee and commission income for both DBS and OCBC. The banks' existing consumer customer franchise network, relationships with SME business owners, growth of wealth in the region continue to drive organic growth in wealth management income, post the wave of acquisitions by DBS and OCBC.

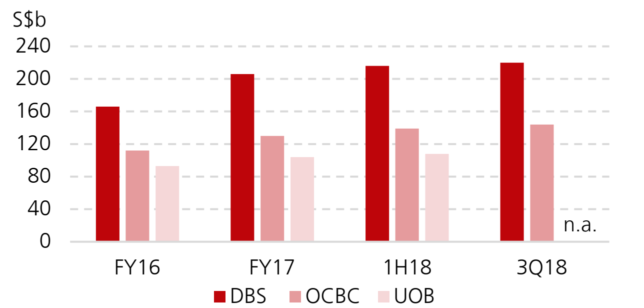
Singapore Banks: Wealth management income trends



Source: Companies, DBS Bank

Singapore Banks: Wealth Management AUM

S$bn	FY16	FY17	1H18	3Q18
DBS	166	206	216	220
OCBC	112 (US$79b)	130 (US$99b)	139 (US$102b)	144 (US$105b)
UOB	93	104	108	N/A

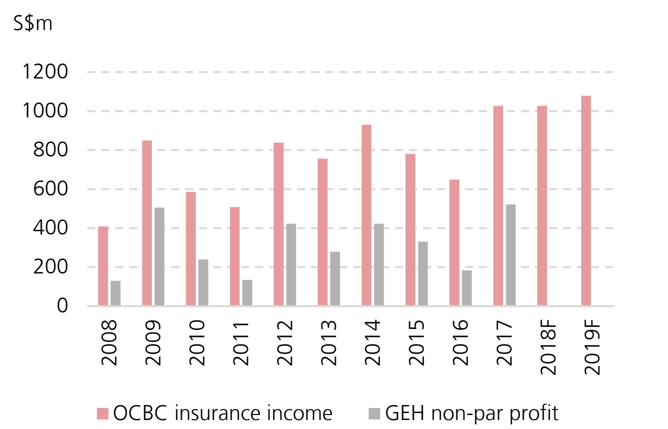


Note: OCBC's AUM is reported in US$
Source: Companies, DBS Bank

Wealth management remains a strong growth engine for OCBC in the long run. For OCBC, wealth management remains a strong growth engine in the long run, especially since its acquisition of Barclays' wealth and investment management arm in Asia. In 3Q18, OCBC's private banking AUM at US$105m represented an increase of 3% q-o-q and 11% y-o-y as mark-to-market valuations were lower. Bank of Singapore continued to see net new money inflows as it builds up its capabilities.

Great Eastern Holdings a key differentiator for OCBC. In particular, OCBC's subsidiary, Great Eastern Holdings (GEH), is a key differentiator for OCBC as it has a longstanding track record in offering a complete range of wealth-related and insurance products both in Singapore and Malaysia. OCBC's increasing stake in GEH over the years demonstrates the importance of an insurance subsidiary to the group's wealth business. Previously, GEH was exploring ways to divest a 30% stake in Great Eastern Malaysia (GELM) in reaction to Bank Negara Malaysia's (BNM) stricter enforcement of the 70% foreign ownership cap on insurers. With the change of government, we understand that OCBC is still in discussions with the Malaysian authorities that will enable GELM to satisfy foreign ownership requirements of insurance companies in Malaysia, including making a certain contribution to a special insurance development trust fund. In our view, other viable options for these companies to pare down their stakes are: 1) list (IPO) 30% of their shares to the public; 2) joint-venture with a local partner; or 3) divest to local institutional investors. We believe retaining 100% ownership of GELM is beneficial for OCBC in terms of earnings contribution.

OCBC: Insurance income trends



Source: Companies, DBS Bank

Regional agenda remains imperative

Diversifying geographically. Singapore banks have been pursuing their regional agenda in their own ways, especially in the last decade, and will continue to do so as they seek to diversify revenue streams geographically as Singapore's landscape remains competitive. Both UOB and OCBC's second largest source of profits are from Malaysia, where both banks have strong and longstanding track records, competing closely with the Malaysian banks. Both UOB and OCBC have also been building up their presence in Indonesia in the last few years. Although still a small contribution, we believe, over time, this will drive ROEs.

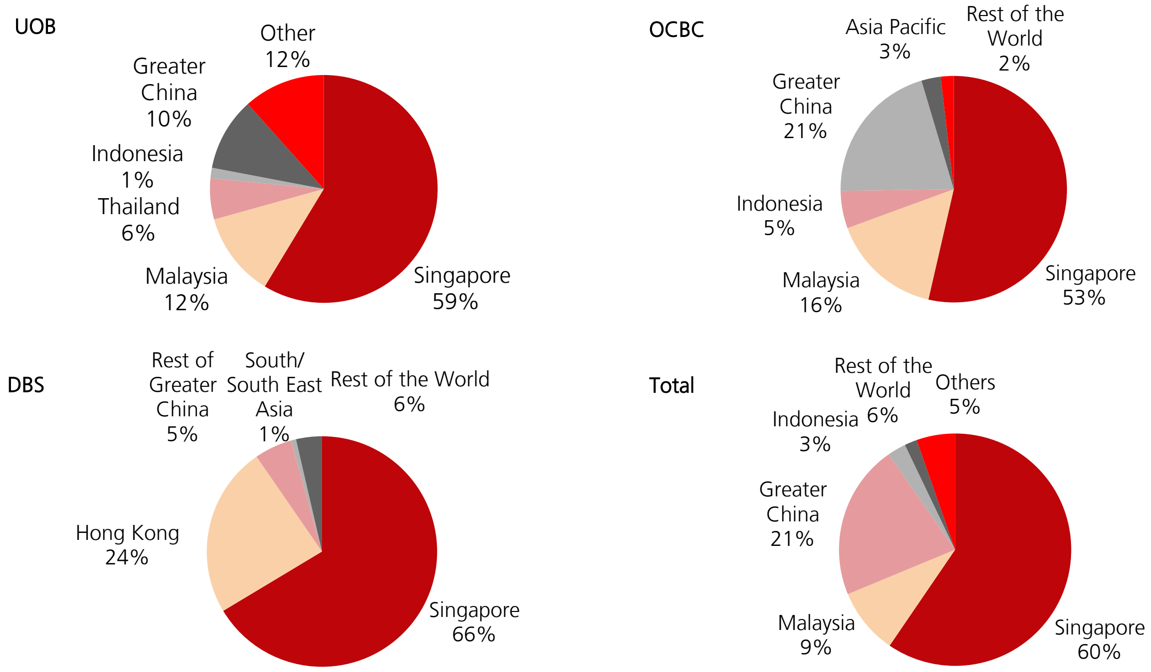
UOB continues to step up its ASEAN presence. UOB is the only Singapore bank with a substantial earnings contribution from Thailand, and continues to expand its ASEAN geographical footprint by incorporating a fully-owned subsidiary in Vietnam in Aug 2018. Collectively, Malaysia, Thailand and Indonesia make up c.19% of its profit before tax (in 9M18). In the longer term, we believe UOB is well-positioned to capture flows into Southeast Asia as the bank is able to offer ecosystem support for companies looking to invest in Southeast Asia. There may also be opportunities in North Thailand arising from China's Belt and Road Initiative.

OCBC targeting Greater Bay Area. OCBC has set its target to expand in the Greater Bay Area (GBA), which comprises Hong Kong, Macau and cities in the Guangdong province. OCBC is currently the fourth largest foreign bank by network size and continues to invest in the GBA franchise, with two-thirds of S$200m to be invested in technology expenditure. OCBC expects to obtain at least S$1bn in pre-tax profit from GBA, doubling the contribution in 2017.

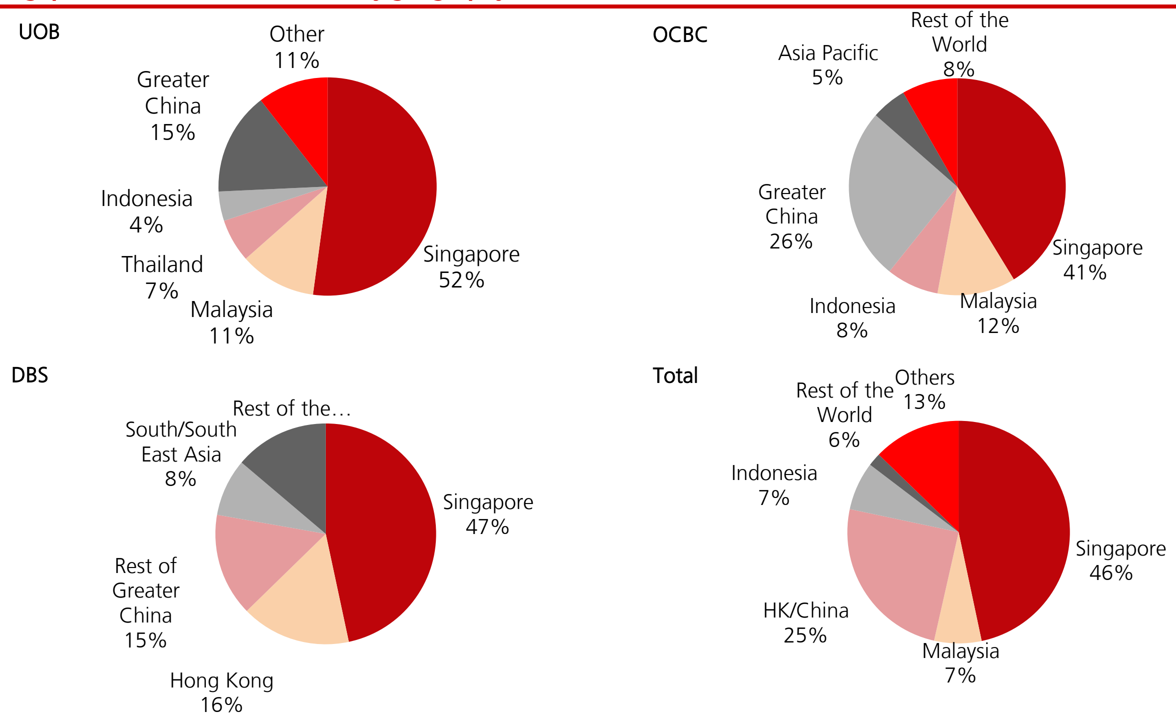
Building presence through digital initiatives. The Singapore banks have been building up their presence in Indonesia, which we believe could drive ROEs over time. OCBC NISP has started cross-referring SME owners to OCBC's private banking services, while continuing to embark on a mobile-first strategy and various partnerships to grow its market share in Indonesia (For more details, please refer to our previous report: OCBC: Digital quest to grow Indonesia market share). In the meantime, UOB also continues to add talent headcount into Indonesia. We are also expecting UOB to announce the launch of its Digital Bank, starting with one of the ASEAN countries, by early 2019 as it seeks to target potential underserved customers outside of Singapore. More recently, UOB has also entered into a strategic alliance with Grab regionally (For more details, please refer to our previous report: UOB: Grab-bing a regional alliance).

Updates on other overseas investments. OCBC's sale of its 33.33% stake in Hong Kong Life Insurance was aborted at end-Sep 2018. The original plan was for OCBC WHB to enter into a distribution agreement to distribute Hong Kong Life's insurance products in Hong Kong. OCBC has re-started discussions on potential options as it remains keen to divest this stake. On the other hand, UOB owns approx. 12% of Evergrowing Bank in China, which is still getting clearance for its financials, and has future IPO plans. UOB had previously mentioned in its 2Q18 results briefing that it does not expect this investment to have a significant impact on its books as it had already taken a significant discount to Evergrowing's net tangible assets when valuing the investment on its books.

Singapore Banks: Profit before tax by geography (9M2018)



Singapore Banks: Customer loans by geography (9M2018)



Source: Companies, DBS Bank

Impact of property cooling measures

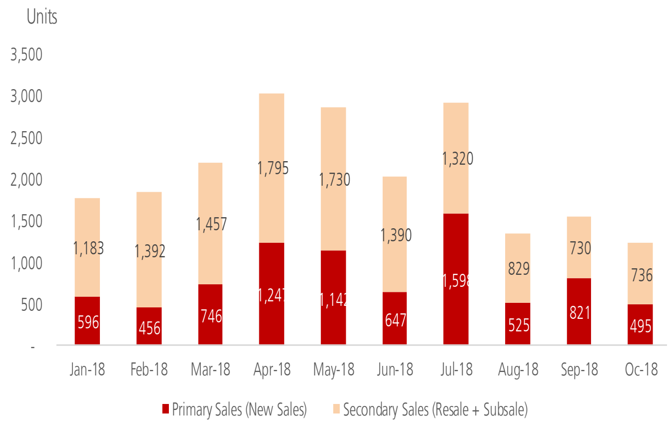
Sizeable exposure to property market. The Singapore banks have a sizeable exposure to the property market. We believe the bulk of the banks' mortgage loans, as well as building and construction loans, pertain to the domestic market. On top of that, lending to REITs or other private vehicles may be captured under "financial institutions, investment and holding companies". We estimate that approx. 49% to 60% of Singapore banks' loan books are Singapore property-related.

Singapore banks: Loan profile (3Q18)

	DBS	% total	OCBC	% total	UOB	% total
Manufacturing	35,461	10	16,399	6	21,507	9
Building & construction (1)	73,019	21	51,463	20	60,174	23
Housing loans (2)	74,485	22	65,553	26	67,631	27
General commerce	50,764	15	34,959	14	32,365	13
Transport, storage & comms	30,474	9	13,832	6	9,996	4
FIs, investment & holdcos	21,506	6	20,801	8	22,698	9
Professionals & private individuals	31,349	9	30,698	12	28,934	12
Others	28,043	8	22,871	9	11,816	5
Total Gross Loans	341,101	100	256,576	100	255,122	100
(1) + (2)		43		46		50

Source: Companies, DBS Bank

Singapore property: Transaction volumes tapered off post cooling measures



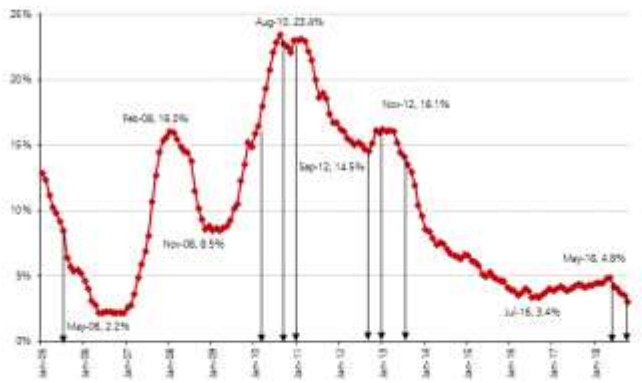
Source: URA, DBS Bank

Assuaging concerns on loan book. Singapore banks have indicated during their respective results briefings that mortgages are largely for owner-occupied homes, allaying concerns on a huge investment property portfolio, which is seen as more risky than owner-occupied homes. We understand that OCBC's and UOB's loan-to-valuation for the mortgage loans portfolio is at c.60%. We also understand that the Singapore banks typically lend to the larger developers, which have better credit quality, compared to other developer peers.

Transaction volumes have tapered off post measures. While we believe that enbloc buyers can still partially support demand in 1H19, DBS Group Research property analyst Derek Tan expects primary sales demand to drop back to 7,500-8,500 units in 2019, similar to the transaction volumes seen in 2014-2016 post the last round of cooling measures. In the longer term, we continue to see robust upgrader demand of c. 6,000 units per annum, which should support transaction volumes.

Mortgage loan growth took close to 4 years to find its bottom since the last major property cooling measures. Since the onslaught of property cooling measures from Oct 2012 when loan tenures and loan-to-valuation (LTVs) were targeted, Additional Buyer's Stamp Duty (ABSD) and Total Debt Servicing Ratio (TDSR) were introduced, mortgage loan growth in Singapore's system took 46 months to find its bottom at 3.4%, from highs of c. 16% in end-2012. This round, mortgage loan growth peaked at c.4.8% in May 2018 before the cooling measures were introduced. We believe that the slowdown in mortgages growth would be less pronounced this time.

Singapore: Mortgage loan growth (y-o-y) %



(1)	(2) (3) (4)	(5) (6) (7)	(8) (9)

Source: Companies, MAS, DBS Bank
Refer to the following table for details on measures imposed

DBS
Live more, Bank less

Singapore property cooling measures

	Measures	Details
(1)	Jul-05 Relaxation of LTV limits	LTV for housing loans raised from 80% to 90%
(2)	Feb-10 LTV limits targeted	- LTV reduced to 80% - Loans granted by HDB retained LTV cap at 90%
(3)	Aug-10 LTV limits targeted	- LTV reduced to 70% for borrowers with one or more outstanding loans - LTV at 80% for borrowers without outstanding loans - Loans granted by HDB retained LTV cap at 90%
(4)	Jan-11 LTV limits targeted	- LTV reduced to 60% for borrowers with one or more outstanding loans; - LTV at 80% for borrowers without outstanding loans - LTV for non-individual borrowers at 50% - Loans granted by HDB retained LTV cap at 90%
(5)	Oct-12 Loan tenure, LTV limits targeted	- Residential loan tenure capped at 35 years - For tenures exceeding 30 years or loan periods for borrowers beyond age 65: - LTV reduced to 40% for borrowers with one or more outstanding loans; - LTV at 60% for borrowers without outstanding loans - LTV for non-individual borrowers reduced to 40% from 50%
(6)	Jan-13 LTV limits targeted, ABSD introduced	- Additional Buyer's Stamp Duty (ABSD) rates - LTVs further tightened: 2nd house LTV at 50%, 3rd or subsequent house at 40%; non-individual borrowers at 20% - Min cash payment for 2nd or subsequent loans raised to 25%
(7)	Jun-13 TDSR introduced	- MAS expects any property loan extended by the FI to not exceed a TDSR threshold of 60%
(8)	Jul-18 LTV limits targeted, ABSD raised	- LTV reduced by 5%-point for all housing loans - Loans granted by HDB retained LTV cap at 90% - ABSD raised by 5%-point for all other individuals other than Singapore Citizens and PRs; raised by 10%-point for all entities - Introduction of new ABSD (5%), non-remittable for developers purchasing residential properties for housing development
(9)	Oct-18 Government imposes new restrictions on unit sizes	- Average development size to increase to 85 sqm for homes outside Central area (increase by +21% from current 70 sqm) - Reduction in bonus GFA cap for private outdoor spaces (balcony) - Introduce a new Bonus GFA scheme for provision of indoor recreation

Source: Companies, MAS, DBS Bank

Singapore banks' Greater China exposure

Varying exposure across Singapore banks. UOB has the smallest exposure to the Greater China region in terms of percentage of assets and loans relative to its peers who have sizeable Hong Kong franchises due to acquisitions in prior years. We believe a China slowdown will impact the Singapore banks' plans to grow various loan-related and fee-based income in Greater China, though, we might also see increased investments into Southeast Asia from China in the longer run.

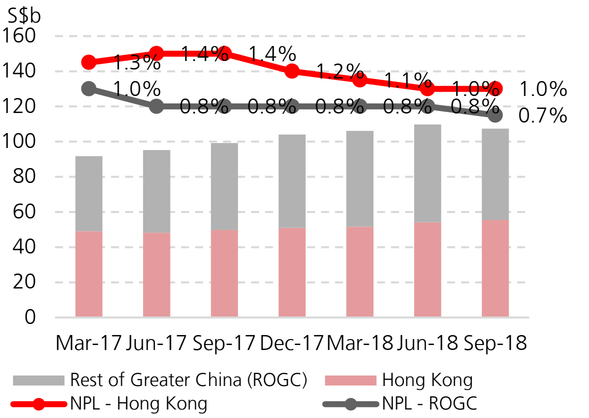
Managing Greater China exposure. Approximately 25% of OCBC's loan book relates to Greater China, where NPL ratio remains low at 0.3%. c.S$5bn out of S$66bn Greater China loan exposure are domestic loans, either to top-tier SOEs or are bank-backed. Notably, OCBC has stepped up on its credit procedures in China as a prudent measure. For UOB, 8.5% of total assets have China exposure, where c.80% have less than 1-year tenor. About 65% UOB's exposure to China pertains to bank exposure; 70% of this are to top 5 domestic banks and 3 policy banks, and half of the bank's exposure are trade exposures. Non-bank exposure is mainly to top-tier SOEs, large local corporates and foreign investment enterprises where NPL is 0.5%.

Singapore Banks: Exposure to Greater China

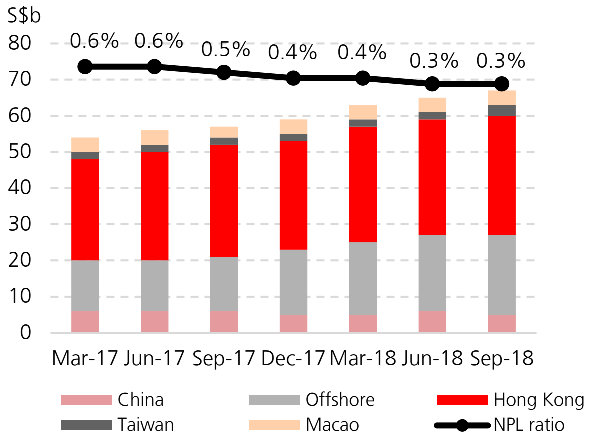
9M2018	DBS	OCBC	UOB
Loans			
Hong Kong	16%	-	-
Other Greater China	15%	26% incl HK	15%
NPL			
Hong Kong	1.0%	-	-
Other Greater China	0.7%	0.3% incl HK	0.4%
Assets			
Hong Kong	17%	-	-
Other Greater China	9%	18% incl HK	15%
Profit before tax			
Hong Kong	24%	-	-
Other Greater China	6%	20% incl HK	10%

Source: Companies, DBS Bank

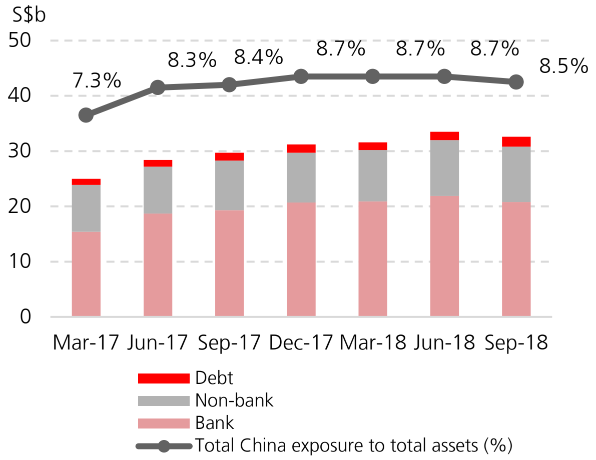
DBS: Greater China loan exposure



OCBC: Greater China loan exposure



UOB: Exposure to China



Source: Companies, DBS Bank

Singapore Company Guide

OCBC

Version 15 | Bloomberg: OCBC SP | Reuters: OCBC.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

2 Nov 2018

BUY (Upgrade from HOLD)

Last Traded Price (1 Nov 2018): S$11.15 **(STI :** 3,060.85)

Price Target 12-mth: S$13.20 (18% upside) (Prev S$12.40)

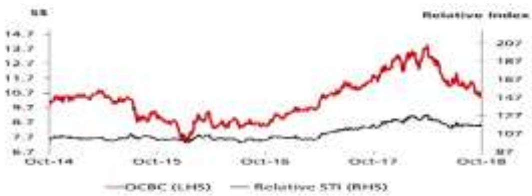
Analyst

Rui Wen LIM +65 66823720 ruiwenlim@dbs.com

What's New

- Long-awaited NIM expansion finally here with a 5-bp increase q-o-q largely on mortgage portfolio repricing
- Post scrip dividends in 2Q18, CET1 ratio of 13.6% now compares well to peers; ability to pay higher dividends removes overhang on stock price due to lower dividend yield
- Non-interest income supported by higher net trading gain against lower wealth management income
- Upgrade to BUY, TP of S$13.20 on higher ROE assumptions of c.12%

Price Relative



Forecasts and Valuation

FY Dec (S$m)	2017A	2018F	2019F	2020F
Pre-prov. Profit	5,498	5,945	6,447	6,936
Net Profit	4,084	4,808	5,127	5,434
Net Pft (Pre Ex.)	4,084	4,808	5,127	5,434
Net Pft Gth (Pre-ex) (%)	19.6	17.7	6.6	6.0
EPS (S cts)	97.7	113	118	125
EPS Pre Ex. (S cts)	97.7	113	118	125
EPS Gth Pre Ex (%)	17	15	5	6
Diluted EPS (S cts)	97.7	111	118	125
PE Pre Ex. (X)	11.4	9.9	9.5	8.9
Net DPS (S cts)	37.0	40.0	40.0	40.0
Div Yield (%)	3.3	3.6	3.6	3.6
ROAE Pre Ex. (%)	11.0	11.9	11.6	11.4
ROAE (%)	11.0	11.9	11.6	11.4
ROA (%)	1.0	1.1	1.1	1.1
BV Per Share (S cts)	909	976	1,054	1,139
P/Book Value (x)	1.2	1.1	1.1	1.0
Earnings Rev (%):		(4)	(3)	(4)
Consensus EPS (S cts):		111	120	129
Other Broker Recs:		B: 19	S: 0	H: 3

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P.

More catalysts ahead

NIM expansion a positive catalyst, higher dividends to come? OCBC's NIM has been largely flattish in the last four quarters on slower loan repricing amid higher cost of funds. In 3Q18, OCBC started to reprice its mortgage portfolio and we expect to see the full impact in 4Q18. OCBC has also released some of the excess USD liquidity built up in 2H17 after its internal assessment. Post turning on of scrip dividends in 2Q18, CET1 ratio of 13.6% now compares well to peers and we believe that OCBC has the ability to pay higher dividends. This may remove the overhang on the stock price due to its lower dividend yield compared to peers and should be viewed as a positive catalyst. OCBC currently has a dividend yield of c. 3.6% compared to its peers' dividend yield of c. 5%. As such, we upgrade our call to BUY with a TP of S$13.20.

Where we differ: Our earnings forecasts remain higher than consensus as we believe that OCBC will benefit from lower credit costs compared to historical levels (post the implementation of IFRS9) in the current benign environment.

Potential catalysts: Sustained NIM deliveries and higher dividends. Further NIM expansion could further boost earnings in a rising interest rate environment. A higher dividend yield for OCBC, closer to its peers', could be a re-rating catalyst. However, in the event that trade war escalates, it might trigger further risks to loan growth.

Valuation:

Upgrade to BUY, TP of S$13.20. We arrive at our revised TP S$13.20 (12% ROE, 3% growth, 10% cost of equity) on higher ROE assumptions (previous: c. 11%), equivalent to c.1.3x FY19F P/BV, at its average 10-year forward P/BV multiple. We believe that OCBC will continue to benefit from the rising rate cycle. We revised our earnings marginally by -3% to -4% largely on lower non-interest income expectations going forward. Despite this, our earnings is above consensus.

Key Risks to Our View:

Asset quality trends. Further escalation of trade war may subject some companies to vulnerability. Should asset quality turn malign, more specific provisions might be required. In the event that trade war escalates, it might trigger further risks to loan and fee growth, especially for OCBC's Greater China exposures.

At A Glance

Issued Capital (m shrs)	4,252
Mkt. Cap (Sm/USm)	47,412 / 34,446
Major Shareholders (%)	
Selat Pte Ltd	11.1
Free Float (%)	88.9
3m Avg. Daily Val (US$m)	47.3
ICB Industry : Financials / Banks	

DBS

Live more, Bank less

ed: TH/ sa: WMT, CW, CS

WHAT'S NEW

Yet another record quarter

Another record quarter for OCBC. OCBC's 3Q18 earnings of S$1,245m was higher by 9% q-o-q and 16% y-o-y, ahead of consensus expectations by c.8% and in-line with ours. Net interest income grew 4% q-o-q and 9% y-o-y due to increasing NIM and strong loan growth. Non-interest income was relatively flat q-o-q and y-o-y, led by strong net trading income (mainly treasury-related income from customer flows) against weaker wealth management and insurance income.

Wealth management income declined 6% q-o-q and 2% y-o-y largely led by declines in insurance income. In the meantime, private banking AUM at US$105m increased 3% q-o-q and 11% y-o-y as Bank of Singapore continued to see net new money inflows.

NIM uptick finally came through. After four consecutive quarters of flattish NIM, OCBC delivered a strong 5-bp improvement q-o-q and 6-bp improvement y-o-y to 1.72%. This was largely attributed to repricing of mortgage loans in Singapore, as well as release of excess USD amassed in 2H17 in anticipation of stronger loan demand that did not materialise. OCBC saw improved margins in Singapore, Malaysia and Greater China against a higher loan-to-deposit ratio (LDR). Increases in loan yields outpaced the increase in cost of deposits.

Asset quality continues to be benign. Provisions were higher (lowest among peers since 1Q18) at S$49m (3Q17: S$156m; 2Q18: S$21m). Credit cost was only at 8bps (3Q17: 24bps; 2Q18: 3bps). Absolute NPLs were flattish while new NPL formation continues to normalise at c.S$300m levels. NPL ratio remained stable at 1.4%, similar to a quarter ago. According to management, while the NPLs are scattered with no industry concentration, going forward, there may be concerns of general slowdown in the economy depending on developments of US-China trade tensions. While the credit environment remains benign, OCBC has stepped up on its credit procedures in Indonesia and China as a prudent measure.

Broad-based loan growth. Loan growth was largely broad-based at 2% q-o-q and 10% y-o-y, mainly driven by USD loans. Deposits declined marginally q-o-q but increased 7% y-o-y with CASA proportion moving to 47.5% (3Q17: 50.5%; 2Q18: 47.7%). As such, LDR continued to rise to 88.5% (2Q18: 85.9%) as loans grew faster than deposits.

Capital levels improved. Post turning on of scrip dividends, CET1 was higher at 13.6% (2Q18: 13.2%), while Tier-1 CAR and Total CAR were higher at 14.4% and 16.1% respectively.

Key takeaways from analyst briefing

Scrip dividend may be turned off; potential for higher dividends. Post scrip dividend being turned on in 2Q18, CET1 ratio is now at 13.6% which is above the management's comfortable range of 12.5-13.5%. Management has also reaffirmed their commitment to a steady, predictable quantum of 40-50% dividend payout ratio. We believe that there may be potential for higher dividends now that OCBC has shored up some capital. At 40% dividend payout ratio, it translates to c.44 Scts.

Full impact of repricing to be seen in 4Q18's NIM. According to management, of the 5-bp improvement in NIM, 1-1.5bps can be attributed to the release of excess USD amassed, while the remaining is largely due to repricing of loans. As repricing had started in 3Q18, the full impact will be seen in 4Q18 and we expect a slight uptick in NIM going forward.

Guidance into 2019. OCBC continues to see loan growth at a mid-to-high single digit into FY2019 and for credit costs to normalise over time to 12-15bps. OCBC expects NIM to remain steady with a slight bias on the positive side.

Hong Kong Life Insurance updates. OCBC has started rediscussing potential options as the disposal deal had lapsed and is keen to divest it. The buyer, First Origin International Limited, has forfeited the deposit of c. S$124m to the seller, OCBC Wing Hang (WHB) which we expect to be recognised in 4Q18.

Pending outcome on Great Eastern Malaysia. GEH is still in discussions with authorities on the alternatives should it divest 30% of its stake in Great Eastern Malaysia. Should the divestment occur, there may be potential for a one-off dividend payment from the sale proceeds.

Valuation and recommendation

Upgrade to BUY, TP of S$13.20. We arrive at our TP of S$13.20 (12% ROE, 3% growth, 10% cost of equity) on higher ROE assumptions (previous: c. 11%), equivalent to c.1.3x FY19F P/BV, at its average 10-year forward P/BV multiple. We revised our earnings marginally by -3% to -4% largely on lower non-interest income expectations going forward and our earnings still remain higher than consensus. We believe that OCBC will continue to benefit from the rising rate cycle. With NIM expansion now visible and CET1 ratio at 13.6% above OCBC's comfortable range, this may remove overhang on the stock price due to its lower dividend yield compared to peers should OCBC decide to pay higher dividends.

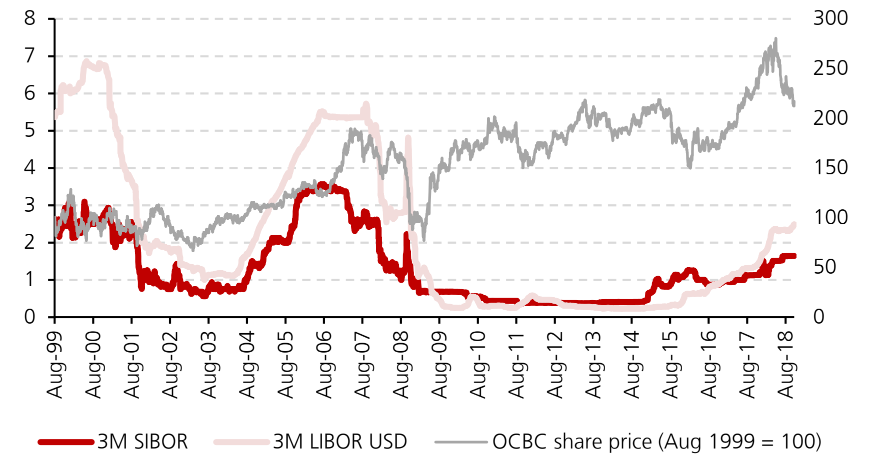
Quarterly / Interim Income Statement (S$m)

FY Dec	3Q2017	2Q2018	3Q2018	% chg yoy	% chg qoq
Net Interest Income	1,382	1,450	1,505	8.9	3.8
Non-Interest Income	978	1,024	1,039	6.2	1.5
Operating Income	**2,360**	**2,474**	**2,544**	**7.8**	**2.8**
Operating Expenses	(1,027)	(1,061)	(1,095)	6.6	3.2
Pre-Provision Profit	**1,333**	**1,413**	**1,449**	**8.7**	**2.5**
Provisions	(156)	(21.0)	(49.0)	(68.6)	133.3
Associates	127	112	134	5.5	19.6
Exceptionals	0.0	0.0	0.0	-	-
Pretax Profit	**1,304**	**1,504**	**1,534**	**17.6**	**2.0**
Taxation	(192)	(246)	(233)	21.4	(5.3)
Minority Interests	(55.0)	(49.0)	(56.0)	(1.8)	14.3
Net Profit	**1,057**	**1,209**	**1,245**	**17.8**	**3.0**
Growth (%)					
Net Interest Income Gth	2.8	2.5	3.8		
Net Profit Gth	(2.4)	8.7	3.0		
Key ratio (%)					
NIM	1.7	1.7	1.7		
NPL ratio	1.3	1.4	1.4		
Loan-to deposit	85.3	85.9	88.5		
Cost-to-income	43.5	42.9	43.0		
Total CAR	16.1	15.9	16.1		

Source of all data: Company, DBS Bank

Appendix 1: A look at Company's listed history – what drives its share price?

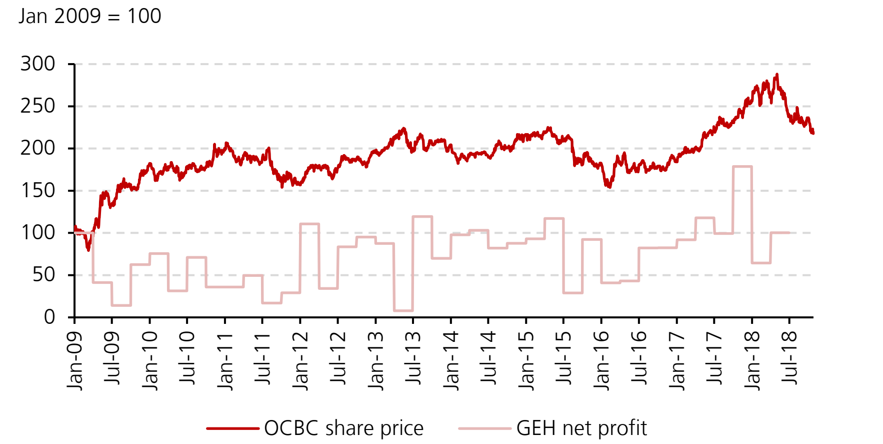
Interest rates as critical factor



Remarks

Interest rates, particularly SIBOR, is linked to loan pricing and hence NIM, which in turn drives earnings and share price performance. The Fed rate hikes which should lead to SIBOR uplift was historically 60% correlated. The relationship has somewhat broken down since late 2016 due to the relative strength of the SGD. Nevertheless, expectations of Fed rate hikes, which are expected to pass through to SIBOR, does have a positive correlation to banks' share prices.

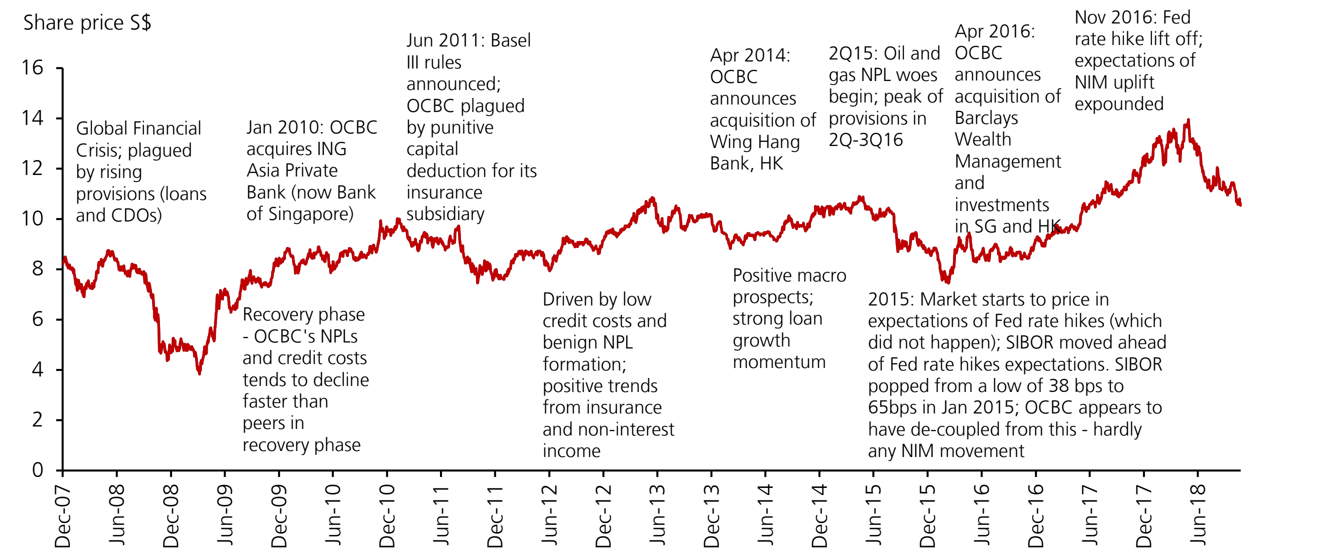
Interest rates as critical factor



Remarks

GEH contributes approximately c.20% of non-interest income, translating into c.13-23% of OCBC's net profit through FY16-17. While not being directly correlated, GEH's profits do indicate OCBC's overall non-interest income trends. GEH also forms part of OCBC's wealth management offerings.

Share price movement (10-year historical trends)



Source: Bloomberg Finance L.P, DBS Bank

CRITICAL DATA POINTS TO WATCH

Critical Factors

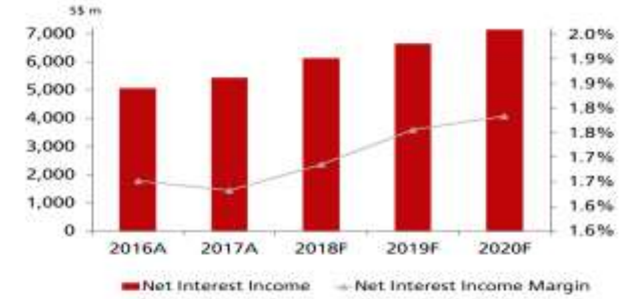
NIM uplift happens finally. OCBC managed to reprice its mortgage loans and with NIM uplift across Singapore, Malaysia and Indonesia, OCBC showed its first significant NIM uptick in four quarters. OCBC's loan profile is largely variable rate based at 90%, with one-third prime-rate based, one-third SIBOR based and 25% SOR based. Our sensitivity analysis implies that for every 25-bp increase in SIBOR/SOR and HKD and USD loan rates (collectively), OCBC's NIM could rise by 2bps with an accompanying 1.4% impact on net profit, holding everything else constant. The bonus to its NIM uplift could lie in its treasury operations, where in a rising rate environment, there would be more opportunities to rebalance its securities portfolio given the steepened yield curve.

Loan growth at a high single digit in FY18F. Management is still maintaining guidance for a high single-digit loan growth in FY18F. Loan demand appears apparent for Singapore companies investing abroad. Every 1-ppt rise in loan growth leads to a 0.9% increase in net profit. We are forecasting loan growth at c. 6-7% p.a. across FY18-20F.

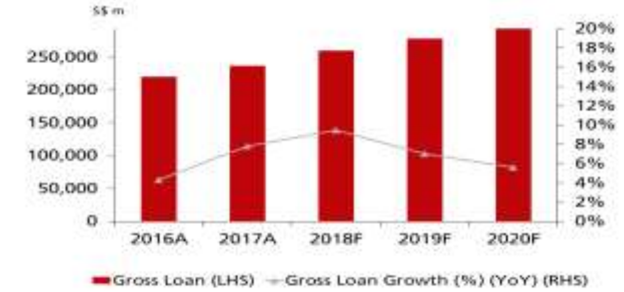
Non-interest income drivers remain its key differentiator, especially wealth management and insurance. OCBC differentiates itself from peers in terms of its non-interest income composition. Its focus is on growing its non-interest income franchise, especially its wealth management business. Its insurance business via 87.75%-owned subsidiary, Great Eastern Holdings (GEH), remains a dominant contributor to its non-interest income. OCBC has no plans to sell its stake in GEH as it remains complementary to its non-interest income franchise. Management believes it is still logical and beneficial to keep the insurance product manufacturing in-house. However, in view of the need to meet regulatory requirements in Malaysia, GEH may look to divest part of its operations in Malaysia. It is currently exploring options to meet this requirement. GEH tends to exhibit earnings volatility due to fluctuations of interest rates. It is best to track GEH's underlying business trends i.e. total weighted new sales and new business embedded values. These metrics have been growing robustly for GEH. Since the acquisition of Bank of Singapore in 2010, its wealth management income has been growing steadily; and this trend is expected to be sustainable. The acquisition of the wealth and investment business of Barclays Bank in Singapore and Hong Kong, completed in December 2016, added US$13bn to OCBC's AUM. In May 2017, OCBC further acquired National Bank of Australia's wealth business in Singapore and Hong Kong.

Regionalisation is a key item on its agenda. Malaysia remains OCBC's second largest contributor. Its business proposition in Malaysia has a track record of over 80 years and its added advantage lies in its Islamic banking franchise. Management feels bullish about its operations in Indonesia. While still a small contributor, opportunities are aplenty for further growth. We see the wealth management income line as the key indicator to watch for sustained synergies in OCBC-Wing Hang.

Margin Trends

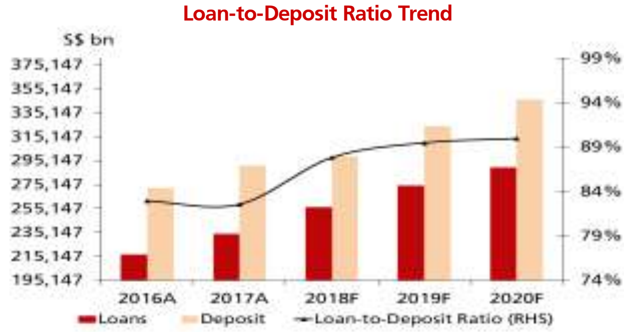


Gross Loan & Growth

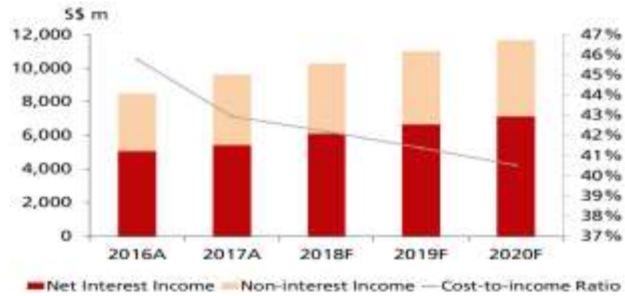


Customer Deposit & Growth

Loan-to-Deposit Ratio Trend



Cost & Income Structure



Source: Company, DBS Bank

Balance Sheet:

Asset quality concerns a thing of the past. OCBC's NPL ratio stood at 1.4% as at end-June 2017 largely from the oil & gas segment. We understand collaterals have been written down to 30% of market value. Its credit cost has stayed lower compared to peers. Despite concerns of an unsustainably low credit cost level, OCBC has successfully weathered through the storm as seen during several crises over the past ten years.

Capital ratios remain strong. OCBC reintroduced its scrip dividend scheme after halting it in 2Q16, to help shore up capital. Separately, while there are still some non-core assets the bank can divest, these are not large and not an immediate priority. There has been a continuous debate on whether OCBC should divest its insurance business, GEH, as it is perceived to be capital punitive once Basel III is fully enforced. But we believe that without majority control of the business, integrating it as part and parcel of its wealth management offerings would be challenging.

Share Price Drivers:

Rising interest rates lift NIM and possibly better insurance business revenues. Rising NIM and hence earnings will be key drivers to share price. Barring volatility in its insurance contribution due to accounting reasons, higher interest rates bode well for its life insurance business to build longer-term revenues. Successful credit costs and NPL containment could provide an added catalyst. Ability to demonstrate these should see the stock re-rate above its 5-year mean P/BV multiple.

Key Risks:

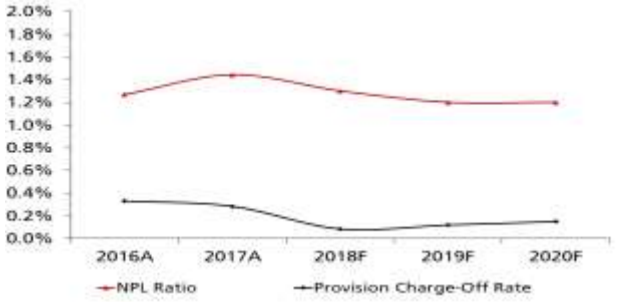
Inability to deliver NIM uplift. Expectations are rife that the Singapore banks will deliver strong NIM trends following sequential Fed rate hikes. Slower-than-expected SIBOR/SOR pass-through or faster increase in cost of funds over loan yields could upset NIM uplift trends.

Asset quality trend reversal. Banks are already on a recovery trend for their NPLs. A larger-than-expected NPL occurrence could unwind expectations of credit cost and NPL declines, posing risks to earnings.

Company Background

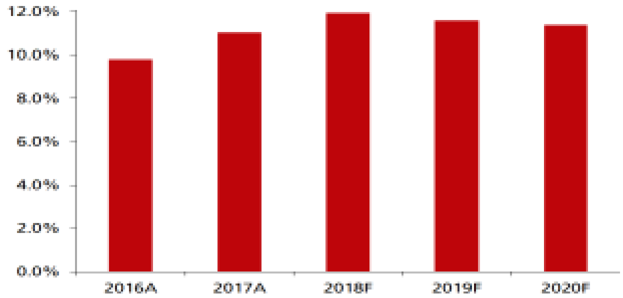
The OCBC Bank group of businesses comprises a family of companies owned by Singapore's longest-established local bank. Its banking business franchise includes OCBC Bank, Bank OCBC NISP and Bank of Singapore, with branches in over 15 countries. OCBC has strategic stakes in other financial service businesses operating under independent brands such as Great Eastern, Bank of Singapore and Lion Global Investors.

Asset Quality

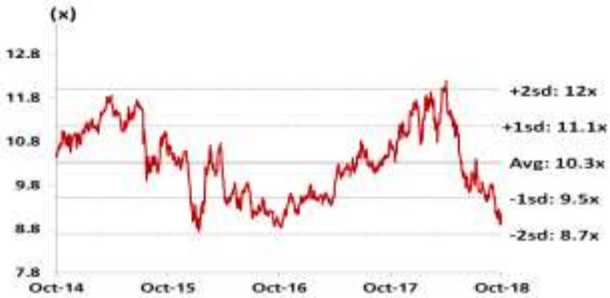


Capitalisation (%)

ROE (%)



Forward PE Band (x)



PB Band (x)

Source: Company, DBS Bank

Key Assumptions

FY Dec	2016A	2017A	2018F	2019F	2020F
Gross Loans Growth	4.3	7.8	9.5	7.0	5.6
Customer Deposits Growth	6.2	8.5	3.0	5.0	5.0
Yld. On Earnings Assets	2.8	2.8	3.1	3.2	3.3
Avg Cost Of Funds	1.2	1.2	1.5	1.6	1.6

Income Statement (S$m)

FY Dec	2016A	2017A	2018F	2019F	2020F
Net Interest Income	5,052	5,423	6,120	6,639	7,129
Non-Interest Income	3,437	4,213	4,165	4,360	4,536
Operating Income	**8,489**	**9,636**	**10,284**	**10,999**	**11,665**
Operating Expenses	(3,884)	(4,138)	(4,340)	(4,551)	(4,729)
Pre-provision Profit	**4,605**	**5,498**	**5,945**	**6,447**	**6,936**
Provisions	(726)	(671)	(217)	(328)	(436)
Associates	396	389	397	405	413
Exceptionals	0.0	0.0	0.0	0.0	0.0
Pre-tax Profit	**4,275**	**5,216**	**6,125**	**6,524**	**6,912**
Taxation	(629)	(803)	(980)	(1,044)	(1,106)
Minority Interests	(173)	(267)	(314)	(334)	(354)
Preference Dividend	(59.2)	(62.1)	(22.7)	(19.0)	(19.0)
Net Profit	**3,414**	**4,084**	**4,808**	**5,127**	**5,434**
Net Profit bef Except	3,414	4,084	4,808	5,127	5,434
Growth (%)					
Net Interest Income Gth	(2.6)	7.3	12.8	8.5	7.4
Net Profit Gth	(10.7)	19.6	17.7	6.6	6.0
Margins, Costs & Efficiency (%)					
Spread	1.6	1.6	1.6	1.6	1.7
Net Interest Margin	1.7	1.6	1.7	1.8	1.8
Cost-to-Income Ratio	45.8	42.9	42.2	41.4	40.5
Business Mix (%)					
Net Int. Inc / Opg Inc.	59.5	56.3	59.5	60.4	61.1
Non-Int. Inc / Opg inc.	40.5	43.7	40.5	39.6	38.9
Fee Inc / Opg Income	19.3	20.3	19.9	19.5	19.2
Oth Non-Int Inc/Opg Inc	21.2	23.5	20.6	20.1	19.7
Profitability (%)					
ROAE Pre Ex.	9.8	11.0	11.9	11.6	11.4
ROAE	9.8	11.0	11.9	11.6	11.4
ROA Pre Ex.	0.9	1.0	1.1	1.1	1.1
ROA	0.9	1.0	1.1	1.1	1.1

Lower provisions from FY18F in absence of general provision buffers

Gradual NIM uptrend should follow, in line with CEO's expectations

Source: Company, DBS Bank

Quarterly / Interim Income Statement (S$m)

FY Dec	3Q2017	4Q2017	1Q2018	2Q2018	3Q2018
Net Interest Income	1,382	1,424	1,415	1,450	1,505
Non-Interest Income	978	1,205	918	1,024	1,039
Operating Income	**2,360**	**2,629**	**2,333**	**2,474**	**2,544**
Operating Expenses	(1,027)	(1,093)	(1,057)	(1,061)	(1,095)
Pre-Provision Profit	**1,333**	**1,536**	**1,276**	**1,413**	**1,449**
Provisions	(156)	(178)	(12.0)	(21.0)	(49.0)
Associates	127	28.0	125	112	134
Exceptionals	0.0	0.0	0.0	0.0	0.0
Pretax Profit	**1,304**	**1,386**	**1,389**	**1,504**	**1,534**
Taxation	(192)	(257)	(228)	(246)	(233)
Minority Interests	(55.0)	(96.0)	(49.0)	(49.0)	(56.0)
Net Profit	**1,057**	**1,033**	**1,112**	**1,209**	**1,245**
Growth (%)					
Net Interest Income Gth	2.8	3.0	(0.6)	2.5	3.8
Net Profit Gth	(2.4)	(2.3)	7.6	8.7	3.0

Balance Sheet (S$m)

FY Dec	2016A	2017A	2018F	2019F	2020F
Cash/Bank Balance	16,559	19,594	20,451	21,473	22,547
Government Securities	24,364	27,471	26,922	26,922	26,922
Inter Bank Assets	39,801	49,377	33,346	35,676	37,661
Total Net Loans & Advs.	216,830	234,141	256,505	274,432	289,699
Investment	23,157	25,329	25,651	27,443	28,970
Associates	2,415	2,352	3,067	3,472	3,885
Fixed Assets	4,572	4,281	4,217	4,428	4,649
Goodwill	5,473	5,160	5,160	5,160	5,160
Other Assets	452,353	497,854	508,836	541,780	571,383
Total Assets	**409,884**	**454,938**	**466,143**	**496,188**	**523,279**
Customer Deposits	261,486	283,642	292,151	306,759	322,097
Inter Bank Deposits	10,740	7,485	6,660	17,346	24,168
Debts/Borrowings	19,947	32,235	32,235	32,235	32,235
Others	406,296	461,442	466,619	493,971	517,898
Minorities	2,635	2,768	3,082	3,415	3,769
Shareholders' Funds	37,007	39,008	43,469	46,856	50,551
Total Liab& S/H's Funds	**409,884**	**454,938**	**466,143**	**496,188**	**523,279**

Source: Company, DBS Bank

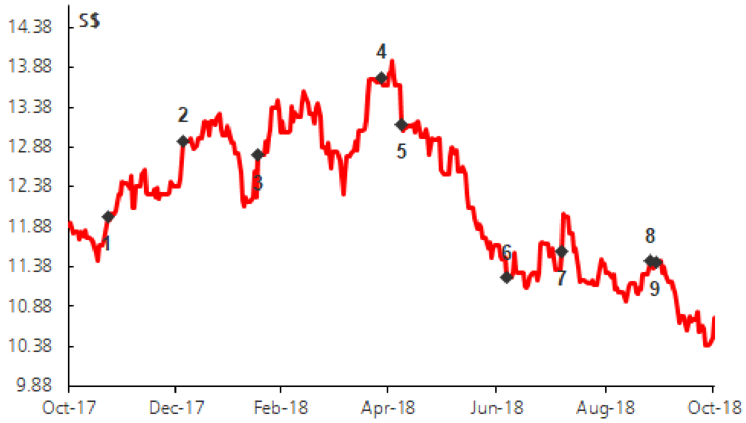
Financial Stability Measures (%)

FY Dec	2016A	2017A	2018F	2019F	2020F
Balance Sheet Structure					
Loan-to-Deposit Ratio	82.9	82.5	87.8	89.5	89.9
Net Loans / Total Assets	52.9	51.5	55.0	55.3	55.4
Investment / Total Assets	5.6	5.6	5.5	5.5	5.5
Cust . Dep./Int. Bear. Liab.	89.5	87.7	88.3	86.1	85.1
Interbank Dep / Int. Bear.	3.7	2.3	2.0	4.9	6.4
Asset Quality					
NPL / Total Gross Loans	1.3	1.4	1.3	1.2	1.2
NPL / Total Assets	0.7	0.8	0.7	0.7	0.7
Loan Loss Reserve Coverage	102.7	77.7	80.7	87.1	90.6
Provision Charge-Off Rate	0.3	0.3	0.1	0.1	0.1
Capital Strength					
Total CAR	17.1	17.2	16.1	16.2	16.6
Tier-1 CAR	14.7	13.9	13.9	14.2	14.7

Capital levels remain strong, albeit lowest among peers

Source: Company, DBS Bank

Target Price & Ratings History



***Note**: Share price and Target price are adjusted for corporate actions.*

S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	22 Nov 17	12.01	13.50	BUY
2:	04 Jan 18	12.95	14.00	BUY
3:	15 Feb 18	12.78	14.00	BUY
4:	26 Apr 18	13.76	15.30	BUY
5:	07 May 18	13.17	15.30	BUY
6:	06 Jul 18	11.24	12.20	HOLD
7:	06 Aug 18	11.58	12.40	HOLD
8:	25 Sep 18	11.45	12.40	HOLD
9:	28 Sep 18	11.44	12.40	HOLD

Source: DBS Bank
Analyst: Rui Wen LIM

DBS Bank recommendations are based an Absolute Total Return* Rating system, defined as follows:
STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)
BUY (>15% total return over the next 12 months for small caps, >10% for large caps)
HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)
FULLY VALUED (negative total return i.e. > -10% over the next 12 months)
SELL (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

Share price appreciation + dividends

Completed Date: 2 Nov 2018 08:59:06 (SGT)

Dissemination Date: 2 Nov 2018 09:14:35 (SGT)

Sources for all charts and tables are DBS Bank unless otherwise specified.

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Singapore Company Guide

UOB

Version 17 | Bloomberg: UOB SP | Reuters: UOBH.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

29 Oct 2018

BUY

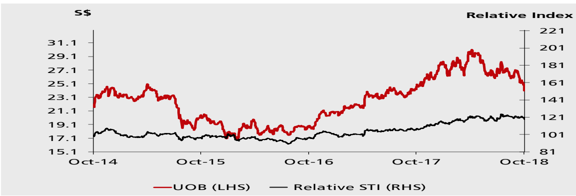
Last Traded Price (26 Oct 2018): S$24.07 (**STI :** 2,972.02)
Price Target 12-mth: S$29.50 (23% upside) (Prev S$31.70)

Analyst
Rui Wen LIM +65 66823720 ruiwenlim@dbs.com

What's New

- Respectable quarter amidst market volatility as strong loan growth continues to drive interest income
- NIMs declined as UOB deliberately built deposits; remains hopeful of future NIM expansion
- Continues to benefit from rising rate cycle
- Maintain BUY, revised TP of S$29.50; at current prices, the stock provides 4.8% yield

Price Relative



Forecasts and Valuation

FY Dec (S$m)	2017A	2018F	2019F	2020F
Pre-prov. Profit	4,824	5,225	5,726	6,126
Net Profit	3,288	3,939	4,259	4,524
Net Pft (Pre Ex.)	3,288	3,939	4,259	4,524
Net Pft Gth (Pre-ex) (%)	9.5	19.8	8.1	6.2
EPS (S cts)	209	236	255	271
EPS Pre Ex. (S cts)	209	236	255	271
EPS Gth Pre Ex (%)	9	13	8	6
Diluted EPS (S cts)	198	234	253	269
PE Pre Ex. (X)	11.5	10.2	9.4	8.9
Net DPS (S cts)	100	120	120	120
Div Yield (%)	4.2	5.0	5.0	5.0
ROAE Pre Ex. (%)	10.2	11.3	11.5	11.5
ROAE (%)	10.2	11.3	11.5	11.5
ROA (%)	1.0	1.1	1.1	1.1
BV Per Share (S cts)	2,151	2,145	2,280	2,430
P/Book Value (x)	1.1	1.1	1.1	1.0
Earnings Rev (%):		(5)	(4)	(3)
Consensus EPS (S cts):		241	261	282
Other Broker Recs:		B: 19	S: 0	H: 3

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P.

Respectable quarter amidst volatility

Poised to benefit from strong capital position and rising rate cycle. We believe UOB will continue to be a beneficiary of the rising rate cycle even as it currently sees pressures from higher deposit costs. UOB's strong capital position continues to provide opportunities to tap quality loan growth as broad-based loan growth outlook for the year continues to stand tall, with mid-to-high single-digit growth expected next year. UOB is also less exposed to volatility in wealth management fees as its customers invest mostly in non-leveraged products. Capital levels remain strong with fully loaded CET1 ratio at 14.1% as at September 2018. Higher dividends are possible on its higher capital levels with UOB's new dividend policy as the bank continues to deliver sustained growth.

Where we differ. We continue to like UOB for its strong capital position in current volatile market conditions. UOB has deliberately built up SGD deposits ahead of the curve as it anticipates further increases in cost of deposits. We view this as an appropriate and conservative move.

Potential catalyst: Sustained positive deliveries. Further improvement in NIM should support earnings. Lower credit cost is a new trend for UOB and should be viewed positively.

Valuation:

Maintain BUY, revised TP of S$29.50. We arrive at our revised TP of S$29.50 (previously S$31.70) based on the Gordon Growth Model (12% ROE, 3% growth, 10% cost of equity), equivalent to c.1.3x FY19F P/BV, at its average 10-year forward P/BV multiple. We believe UOB will continue to benefit from the rising rate cycle as it continues to leverage on its strong funding position to deliver loan growth. We revised our earnings marginally by -3 to -5% through FY20F mainly on lower non interest-income expectations.

Key Risks to Our View:

Asset quality trends. Further escalation of trade war may subject some companies to vulnerability. Should asset quality turn malign, more specific provisions might be required. In the event that trade war escalates, it might trigger further risks to loan and fee growth.

At A Glance

Issued Capital (m shrs)	1,667
Mkt. Cap (Sm/USm)	40,136 / 29,082
Major Shareholders (%)	
Wee Investment Pte Ltd	7.8
Wah Hin & Co Pte Ltd	5.2
Free Float (%)	87.0
3m Avg. Daily Val (US$m)	44.3
ICB Industry : Financials / Banks	

DBS
Live more, Bank less

ed: TH/ sa: WMT, CW, CS

WHAT'S NEW

Respectable quarter amidst market volatility

3Q18 earnings driven by higher loan growth and lower credit costs. 3Q18 earnings of S$1.04bn (-4% q-o-q, +17% y-o-y) were in line with expectations as quarterly earnings cross the S$1bn mark for the second time this year. Earnings were driven by higher net interest income on higher loan growth and lower credit costs. Fee income improved y-o-y on higher loan-related, credit card and trade-related fees but declined 3% q-o-q due to lower loan-related and fund management fees, as well as structural foreign exchange positions in relation to its accounting asymmetry from its hedges.

Credit costs remain low. Credit costs were lower as expected at 18bps vs historical 32bps (2Q18: 13bps) while absolute non-performing loans (NPLs) declined slightly against a larger loan book, NPL ratio improved to 1.6% (2Q18: 1.7%). New NPL formation stayed at normalised levels of S$475m compared to S$436m in 2Q18.

Strong loan growth supports net interest income. Loan growth continued to be strong at 2% q-o-q, 10% y-o-y and was broad based with increases largely across sectors. However, net interest margin (NIM) dipped during the quarter from 1.83% in 2Q18 to 1.81% this quarter even as loan yields rise (3Q17: 1.79%), as UOB continued to build up deposits during the quarter. Group loan-to-deposit ratio (LDR) at 85.7% remained stable y-o-y.

Expenses grew ahead of revenue. Expenses were down 1% q-o-q, 12% y-o-y largely due to staff variable costs and IT investments. On higher revenues, cost-to-income ratio improved q-o-q to 43.4% (3Q17: 41.6 %; 2Q18: 43.6%).

Mixed regional performance. UOB saw broad-based y-o-y growth across most countries. In particular, Thailand saw strong q-o-q performance on higher incomes against lower provisions while Malaysia started to see cost of funds going up. China's liquidity conditions have also driven up short-term funding significantly. As UOB continues to restructure its Indonesia operations, provisions increased q-o-q in a lower NIM environment.

Capital ratios remain strong, dividend policy reiterated. Capital ratios stood strong with CET1, Tier-1 and Total CAR at 14.1%, 15.1% and 17.4% respectively. UOB reaffirmed its commitment to the new dividend payout ratio of c.50% (of net profit), subject to minimum CET1 ratio of 13.5% and sustainable business performance. No dividends were declared for the quarter.

Key takeaways from analyst briefing

NIM declines as UOB builds deposits in anticipation of higher interest rates and pipeline. UOB had deliberately built up SGD deposits, particularly fixed deposits, and lowered the SGD LDR to 91.5% (2Q18: 94.8%) against the current macroeconomic backdrop, in anticipation that deposit costs is likely to trend up further as there is increasing competition for SGD deposits. UOB expects some drawdowns that did not happen in the quarter to occur next quarter, as it continues to deploy loans. While UOB expects some uptick in cost of funds next quarter, the bank remains hopeful that there will be NIM recovery in the rising rate environment due to better loan pricing.

Current credit environment still benign, stress tests performed across portfolio. Credit costs for the year might come in lower than UOB's original guidance of 20bps in the current benign environment. While UOB does not see any major deterioration in its loan portfolio and weakness coming up from trade war currently, UOB has proactively conducted stress tests based on trade war scenarios and is closely monitoring accounts that show some vulnerability and assessing the need to make provisions for some of these accounts.

UOB to capture opportunities from shift of manufacturing base to Southeast Asia. According to UOB, firms in the region are planning to shift their manufacturing base to SEA even as trade activities slow down for the time being. UOB believes that it is able to capture loan opportunities in this space by helping companies in their move.

Launch of Digital Bank by early 2019. UOB is planning to launch its Digital Bank, starting with one of the regional countries, by early 2019 as it seeks to target potential underserved customers outside of Singapore.

Updates on Evergrowing bank. Evergrowing bank is still getting clearance for its financials and has future IPO plans. UOB had previously mentioned in its 2Q18 results briefing that it does not expect significant impact on UOB's books as UOB took a significant discount to Evergrowing's net tangible assets when valuing the investment on its books.

FY19 guidance. UOB sees loan growth at mid-to-high single digit next year, following a higher base this year as it continues to drive cost-to-income ratio lower, on digitalisation and cost efficiencies.

Valuation and recommendation

Maintain BUY, revised TP of S$29.50. We arrive at our revised TP of S$29.50 (previous: S$31.70) based on the Gordon Growth Model (12% ROE, 3% growth, 10% cost of equity), equivalent to c.1.3x FY19F P/BV, at its average 10-year forward P/BV multiple. We believe UOB will continue to benefit from the rising rate cycle as it continues to leverage on its strong funding position to deliver loan growth. We revised our earnings marginally by -3 to -5% through FY20F mainly on lower non interest-income expectations.

Quarterly / Interim Income Statement (S$m)

FY Dec	3Q2017	2Q2018	3Q2018	% chg yoy	% chg qoq
Net Interest Income	1,408	1,542	1,599	13.6	3.7
Non-Interest Income	829	800	728	(12.2)	(9.0)
Operating Income	**2,238**	**2,342**	**2,327**	**4.0**	**(0.6)**
Operating Expenses	(973)	(1,022)	(1,010)	3.8	(1.2)
Pre-Provision Profit	**1,265**	**1,320**	**1,317**	**4.1**	**(0.2)**
Provisions	(221)	(90.0)	(95.0)	(57.0)	5.6
Associates	29.0	52.0	25.0	(13.8)	(51.9)
Exceptionals	0.0	0.0	0.0	-	-
Pretax Profit	**1,073**	**1,282**	**1,247**	**16.2**	**(2.7)**
Taxation	(187)	(202)	(206)	10.2	2.0
Minority Interests	(3.0)	(4.0)	(3.0)	nm	(25.0)
Net Profit	**883**	**1,077**	**1,037**	**17.4**	**(3.7)**
Growth (%)					
Net Interest Income Gth	3.9	4.9	3.7		
Net Profit Gth	4.4	10.1	(3.7)		
Key ratio (%)					
NIM	1.8	1.8	1.8		
NPL ratio	1.6	1.7	1.6		
Loan-to deposit	-	-	-		
Cost-to-income	43.5	43.6	43.4		
Total CAR	17.8	18.4	17.4		

Source of all data: Company, DBS Bank

CRITICAL DATA POINTS TO WATCH

Critical Factors

Lowering loan growth against rising NIM. UOB's loan growth momentum continues to be strong as it leverages on its excess capital for higher loan growth. Meanwhile, we expect UOB's NIM to rise by 7bps (previous forecast: 9bps) in FY18F and another 4bps (previous forecast: 5bps) in FY19F, taking into account some element of competition. Our sensitivity analysis indicates that for every additional 25-bp increase in SIBOR, UOB's NIM will rise by 1bp, holding other variables constant, and this would lead to a further c.1% uplift to earnings. We note that UOB's SGD loan-to-deposit ratio remains the highest among peers and that itself could pressure SGD funding cost; SGD deposits form close to half of UOB's total deposit base.

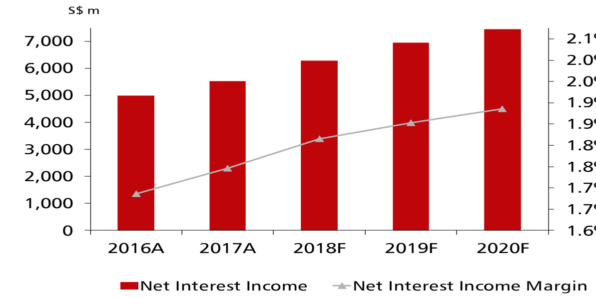
Non-interest income driven more by loan activities. Contrary to peers, UOB's non-interest income focuses more on loan activities, which is its core business. While there is increasing traction from wealth management income, it remains small vs peers. Fee income should be consumer-business driven from credit cards and private banking rather than from capital markets. UOB's wealth management business continues to pick up albeit making up only a smaller proportion of non-interest income vs its peers.

Costs skewed to business growth. We expect operating expenses to stay high with costs skewed towards business expansion and technology which is required particularly for digital banking and cyber security. Other investments to further enhance regional operations are still ongoing but the increase should not be high. Cost-to-income ratio may ease with stronger revenue growth amid its tight cost-control strategies despite having to invest to grow its business but the target is 40% over the longer term. We forecast a 44% cost-to-income ratio for FY18F.

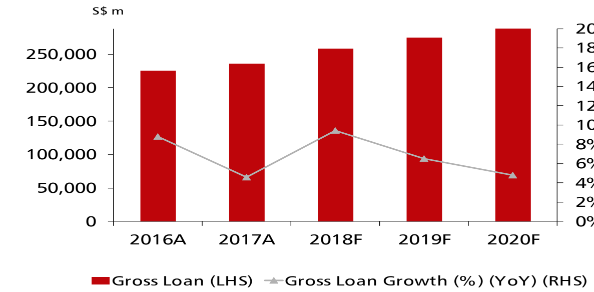
Expect lower credit costs; reversal in trends with IFRS9. Compared to peers, UOB's credit costs tend to hover at higher levels largely due to its conservative stance towards setting aside higher general provisions (1.2% of total loans). With IFRS9 implemented, banks will no longer be allowed to build general provision buffers. This is a new positive for UOB. Management is guiding for 20-25bps credit cost at the moment. We are assuming 16-22bps credit cost over FY18-20F, as credit costs continue to remain low in 9M18.

Regionalisation remains core to UOB's strategy. UOB's regionalisation agenda remains intact. The bank is relooking at its operations in Indonesia, given the current challenging operating environment. In Malaysia, growth remains cautious but asset quality is at a comfortable position. Its Thai operations remain small, while its Greater China operations are still smaller than peers. UOB has not been aggressively acquiring to add new revenue streams but has chosen to grow organically. UOB has announced a Digital Bank for ASEAN's "mobile first" and "mobile only" customers, in Singapore, Malaysia, Indonesia, Thailand and Vietnam as part of its efforts to scale up its regional franchise over the next few years.

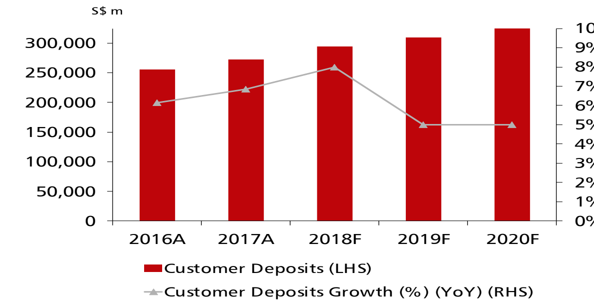
Margin Trends



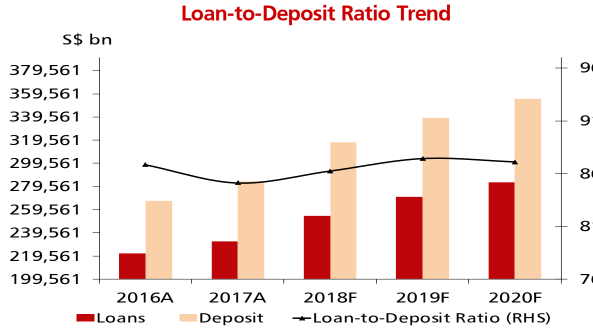
Gross Loan& Growth



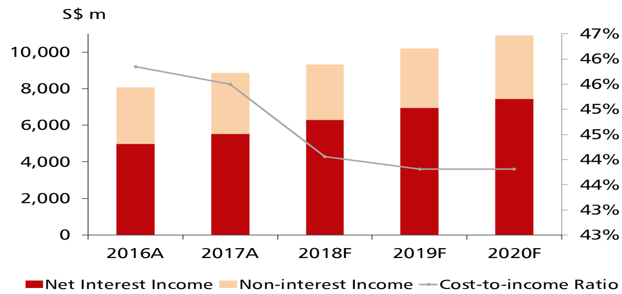
Customer Deposit & Growth



Loan-to-Deposit Ratio Trend



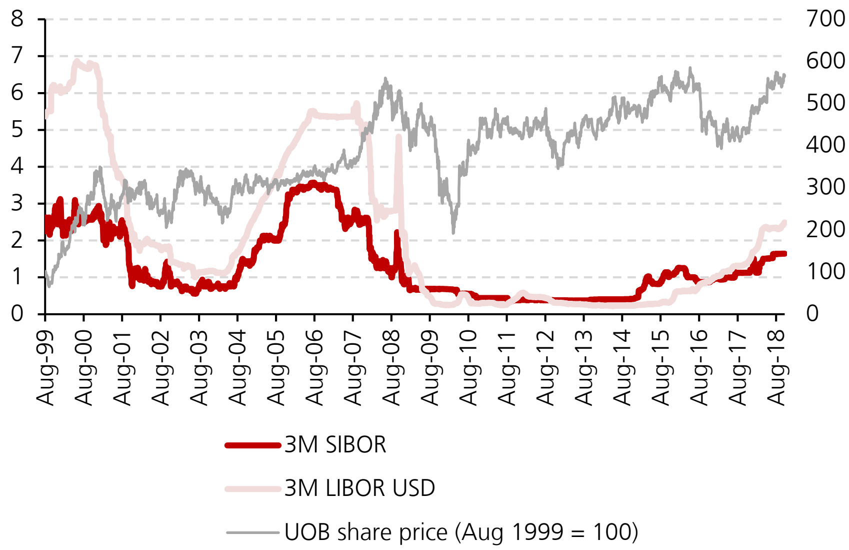
Cost & Income Structure



Source: Company, DBS Bank

Appendix 1: A look at Company's listed history – what drives its share price?

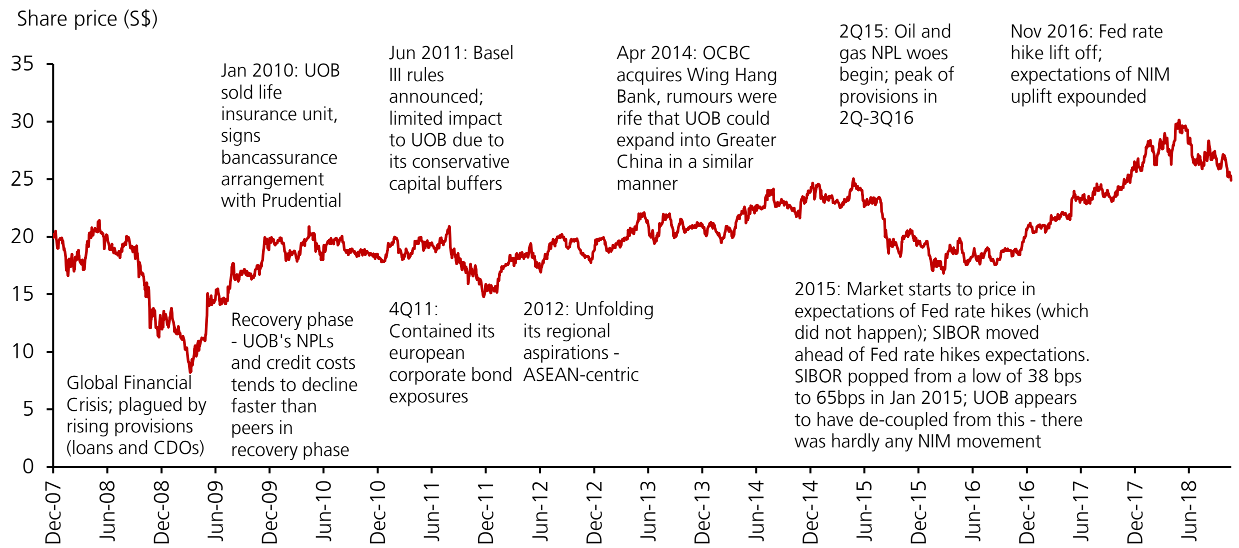
Interest rates as critical factor



Remarks

Interest rates, particularly SIBOR, is linked to loan pricing and hence NIM, which in turn drives earnings and share price performance. The Fed rate hikes which should lead to SIBOR uplift was historically 60% correlated. The relationship has somewhat broken down since late 2016 due to the relative strength of the SGD. Nevertheless, expectations of Fed rate hikes, which are expected to pass through to SIBOR, do have a positive correlation to banks' share prices.

Share price movement (10-year historical trends)



Source: Bloomberg Finance L.P, DBS Bank

Balance Sheet:

Asset quality concerns are a thing of the past. UOB's NPL ratio is higher vs peers, sitting at 1.6% as at end-September 2018. Issues pertaining to the oil & gas exposure have largely been taken care of. As these related accounts are mostly secured; hence the impact on P/L should be limited. UOB is the only bank that has disclosed that it has taken a 70-80% haircut to the value of its oil & gas collateral. There is little concern on the other commodity segments including metal, mining and agriculture.

Strong capital position. Its CET1 ratio's comfort zone is 13.5%. We expect absolute DPS to be sustainable at S$1.00. UOB announced the suspension of its scrip dividend programme in its 2Q18 results. With its strong capital position (fully loaded CET1 ratio at 14.1% as at end-September 2017), we believe there is possibility of higher dividends with its new dividend policy (dividend payout ratio of c.50%, subjected to minimum CET1 ratio of 13.5%).

Share Price Drivers:

Strong property market recovery met with cooling measures. The strong property market recovery from 2017-2018 has met with cooling measures. UOB's share price may be affected as it is seen as the proxy to the property market, having the largest proportion of property-related loans vs peers.

Sustained NIM. With asset quality issues largely to be dealt with by end-FY17, all eyes are on top-line growth. With a sustained SOR/SIBOR uptrend, NIM uplift is here to stay. Sustained strong loan growth also adds to a boost in net interest income, though we believe it might be dampened should the cooling measures successfully arrest the strong property market recovery.

Key Risks:

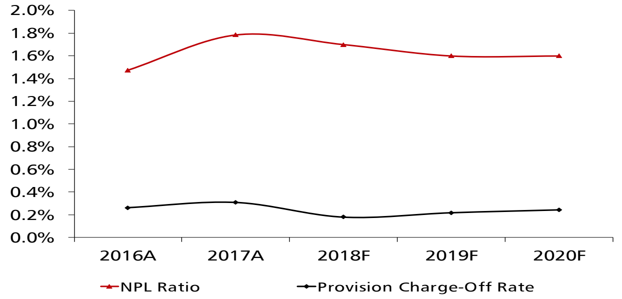
NIM trend reversal. Hopes on NIM improvement could dissipate if SIBOR/SOR movements turn south from here. NIM movements are more sensitive to earnings compared to loan growth. If NIM trends stop improving, earnings growth would be at risk.

Asset quality upsets. While unlikely at this juncture, any NPL formation above the normal levels of S$300-400m could upset trends and raise provisions, which could lead to earnings disappointment.

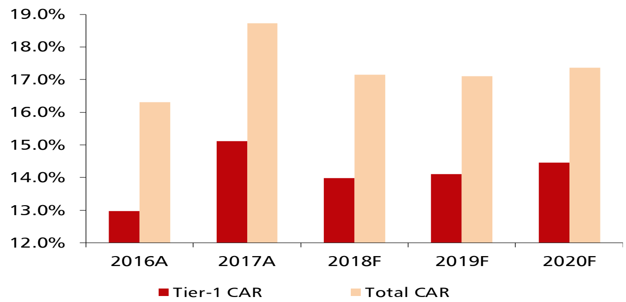
Company Background

UOB provides a wide range of financial services through its global network of branches, offices, subsidiaries and associates: personal financial services, private banking, commercial and corporate banking, investment banking, corporate finance, capital market activities, treasury services, futures broking, asset management, venture capital management, insurance and stockbroking services.

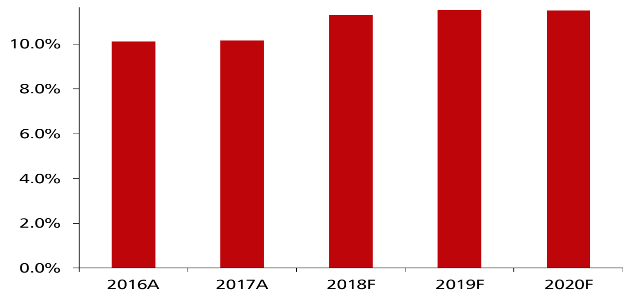
Asset Quality



Capitalisation (%)

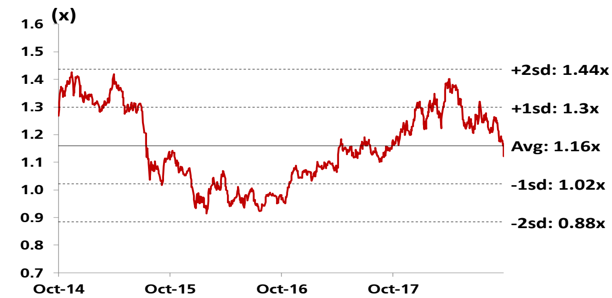


ROE (%)



Forward PE Band (x)

PB Band (x)



Source: Company, DBS Bank

Live more, Bank less

Key Assumptions

FY Dec	2016A	2017A	2018F	2019F	2020F
Gross Loans Growth	8.8	4.6	9.4	6.5	4.8
Customer Deposits Growth	6.1	6.8	8.0	5.0	5.0
Yld. On Earnings Assets	2.8	2.9	3.3	3.4	3.5
Avg Cost Of Funds	1.2	1.2	1.5	1.6	1.7

Income Statement (S$m)

FY Dec	2016A	2017A	2018F	2019F	2020F
Net Interest Income	4,991	5,528	6,282	6,940	7,444
Non-Interest Income	3,071	3,323	3,058	3,251	3,459
Operating Income	**8,061**	**8,851**	**9,340**	**10,191**	**10,903**
Operating Expenses	(3,696)	(4,027)	(4,115)	(4,465)	(4,777)
Pre-provision Profit	**4,365**	**4,824**	**5,225**	**5,726**	**6,126**
Provisions	(593)	(727)	(466)	(601)	(702)
Associates	6.00	110	137	158	179
Exceptionals	0.0	0.0	0.0	0.0	0.0
Pre-tax Profit	**3,778**	**4,207**	**4,896**	**5,283**	**5,603**
Taxation	(669)	(800)	(832)	(898)	(953)
Minority Interests	(12.0)	(16.0)	(14.7)	(15.9)	(16.8)
Preference Dividend	(92.5)	(102)	(110)	(110)	(110)
Net Profit	**3,003**	**3,288**	**3,939**	**4,259**	**4,524**
Net Profit bef Except	3,004	3,289	3,939	4,259	4,524
Growth (%)					
Net Interest Income Gth	1.3	10.8	13.6	10.5	7.3
Net Profit Gth	(3.1)	9.5	19.8	8.1	6.2
Margins, Costs & Efficiency (%)					
Spread	1.7	1.7	1.8	1.8	1.8
Net Interest Margin	1.7	1.8	1.8	1.9	1.9
Cost-to-Income Ratio	45.9	45.5	44.1	43.8	43.8
Business Mix (%)					
Net Int. Inc / Opg Inc.	61.9	62.5	67.3	68.1	68.3
Non-Int. Inc / Opg inc.	38.1	37.5	32.7	31.9	31.7
Fee Inc / Opg Income	24.0	24.4	21.5	21.1	21.2
Oth Non-Int Inc/Opg Inc	14.1	13.1	11.2	10.8	10.5
Profitability (%)					
ROAE Pre Ex.	10.1	10.2	11.3	11.5	11.5
ROAE	10.1	10.2	11.3	11.5	11.5
ROA Pre Ex.	0.9	1.0	1.1	1.1	1.1
ROA	0.9	1.0	1.1	1.1	1.1

Source: Company, DBS Bank

Lower provisions from FY18F in the absence of general provision buffers

NIM uptrend intact with rate hike expectations

Quarterly / Interim Income Statement (S$m)

FY Dec	3Q2017	4Q2017	1Q2018	2Q2018	3Q2018
Net Interest Income	1,408	1,460	1,470	1,542	1,599
Non-Interest Income	829	846	760	800	728
Operating Income	**2,238**	**2,307**	**2,231**	**2,342**	**2,327**
Operating Expenses	(973)	(1,102)	(987)	(1,022)	(1,010)
Pre-Provision Profit	**1,265**	**1,205**	**1,244**	**1,320**	**1,317**
Provisions	(221)	(140)	(80.0)	(90.0)	(95.0)
Associates	29.0	22.0	29.0	52.0	25.0
Exceptionals	0.0	0.0	0.0	0.0	0.0
Pretax Profit	**1,073**	**1,087**	**1,193**	**1,282**	**1,247**
Taxation	(187)	(226)	(212)	(202)	(206)
Minority Interests	(3.0)	(6.0)	(3.0)	(4.0)	(3.0)
Net Profit	**883**	**855**	**978**	**1,077**	**1,037**
Growth (%)					
Net Interest Income Gth	3.9	3.7	0.7	4.9	3.7
Net Profit Gth	4.4	(3.2)	14.4	10.1	(3.7)

Balance Sheet (S$m)

FY Dec	2016A	2017A	2018F	2019F	2020F
Cash/Bank Balance	24,322	26,625	35,350	37,118	38,974
Government Securities	17,515	15,976	16,775	17,614	18,494
Inter Bank Assets	40,033	52,181	55,903	59,496	62,250
Total Net Loans & Advs.	221,734	232,212	254,104	270,439	282,956
Investment	14,767	13,039	14,560	15,469	16,192
Associates	1,109	1,194	1,331	1,489	1,669
Fixed Assets	2,990	1,971	1,823	1,667	1,667
Goodwill	4,151	4,142	4,142	4,142	4,142
Other Assets	13,407	11,252	20,328	21,635	22,636
Total Assets	**340,028**	**358,592**	**404,316**	**429,069**	**448,981**
Customer Deposits	255,314	272,765	294,586	309,316	324,781
Inter Bank Deposits	11,855	11,440	23,309	29,660	30,502
Debts/Borrowings	26,143	25,178	25,178	25,178	25,178
Others	13,674	12,172	22,257	23,654	24,730
Minorities	169	187	202	218	234
Shareholders' Funds	32,873	36,850	38,785	41,043	43,556
Total Liab& S/H's Funds	**340,028**	**358,592**	**404,316**	**429,069**	**448,981**

Source: Company, DBS Bank

Financial Stability Measures (%)

FY Dec	2016A	2017A	2018F	2019F	2020F
Balance Sheet Structure					
Loan-to-Deposit Ratio	86.8	85.1	86.3	87.4	87.1
Net Loans / Total Assets	65.2	64.8	62.8	63.0	63.0
Investment / Total Assets	4.3	3.6	3.6	3.6	3.6
Cust . Dep./Int. Bear. Liab.	87.0	88.2	85.9	84.9	85.4
Interbank Dep / Int. Bear.	4.0	3.7	6.8	8.1	8.0
Asset Quality					
NPL / Total Gross Loans	1.5	1.8	1.7	1.6	1.6
NPL / Total Assets	1.0	1.2	1.1	1.0	1.0
Loan Loss Reserve Coverage	118.0	90.6	96.0	107.9	116.7
Provision Charge-Off Rate	0.3	0.3	0.2	0.2	0.2
Capital Strength					
Total CAR	16.3	18.7	17.1	17.1	17.4
Tier-1 CAR	13.0	15.1	14.0	14.1	14.5

Source: Company, DBS Bank

Strong capital levels; possibility of higher dividends

Target Price & Ratings History

S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	03 Nov 17	24.77	27.50	BUY
2:	22 Nov 17	25.77	27.50	BUY
3:	04 Jan 18	27.02	29.50	BUY
4:	15 Feb 18	27.04	29.50	BUY
5:	26 Apr 18	29.39	33.20	BUY
6:	03 May 18	29.58	33.20	BUY
7:	06 Jul 18	26.26	28.30	HOLD
8:	06 Aug 18	27.13	31.70	BUY

Note : Share price and Target price are adjusted for corporate actions.

Source: DBS Bank
Analyst: Rui Wen LIM

DBS Bank recommendations are based an Absolute Total Return* Rating system, defined as follows:
STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)
BUY (>15% total return over the next 12 months for small caps, >10% for large caps)
HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)
FULLY VALUED (negative total return i.e. > -10% over the next 12 months)
SELL (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

Share price appreciation + dividends

Completed Date: 29 Oct 2018 08:50:11 (SGT)

Dissemination Date: 29 Oct 2018 09:00:54 (SGT)

Sources for all charts and tables are DBS Bank unless otherwise specified.

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DBS Regional Research Offices

HONG KONG
DBS (Hong Kong) Ltd
Contact: Carol Wu
11th Floor The Center
99 Queen's Road Central
Central, Hong Kong
Tel: 852 3668 4181
Fax: 852 2521 1812
e-mail: dbsvhk@dbs.com

MALAYSIA
AllianceDBS Research Sdn Bhd
Contact: Wong Ming Tek (128540 U)
19th Floor, Menara Multi-Purpose,
Capital Square,
8 Jalan Munshi Abdullah 50100
Kuala Lumpur, Malaysia.
Tel.: 603 2604 3333
Fax: 603 2604 3921
e-mail: general@alliancedbs.com

SINGAPORE
DBS Bank Ltd
Contact: Janice Chua
12 Marina Boulevard,
Marina Bay Financial Centre Tower 3
Singapore 018982
Tel: 65 6878 8888
Fax: 65 65353 418
e-mail: equityresearch@dbs.com
Company Regn. No. 196800306E

THAILAND
DBS Vickers Securities (Thailand) Co Ltd
Contact: Chanpen Sirithanarattanakul
989 Siam Piwat Tower Building,
9th, 14th-15th Floor
Rama 1 Road, Pathumwan,
Bangkok Thailand 10330
Tel. 66 2 857 7831
Fax: 66 2 658 1269
e-mail: research@th.dbs.com
Company Regn. No 0105539127012
Securities and Exchange Commission, Thailand

INDONESIA
PT DBS Vickers Sekuritas (Indonesia)
Contact: Maynard Priajaya Arif
DBS Bank Tower
Ciputra World 1, 32/F
Jl. Prof. Dr. Satrio Kav. 3-5
Jakarta 12940, Indonesia
Tel: 62 21 3003 4900
Fax: 6221 3003 4943
e-mail: research@id.dbsvickers.com