Management Discussion and Analysis

Overview

	2018	2017	+/(–) %
Selected income statement items ($ million)			
Net interest income	6,220	5,528	13
Net fee and commission income	1,967	1,873	5
Other non-interest income	930	1,162	(20)
Total income	9,116	8,563	6
Less: Total expenses	4,003	3,739	7
Operating profit	5,113	4,824	6
Less: Allowances for credit and other losses	393	727	(46)
Add: Share of profit of associates and joint ventures	106	110	(4)
Net profit before tax	4,826	4,207	15
Less: Tax and non-controlling interests	818	816	0
Net profit after tax [1]	4,008	3,390	18
Selected balance sheet items ($ million)			
Net customer loans	258,627	232,212	11
Customer deposits	293,186	272,765	7
Total assets	388,099	358,592	8
Shareholders' equity [1]	37,628	36,850	2
Key financial ratios (%)			
Net interest margin	1.82	1.77	
Non-interest income/Total income	31.8	35.4	
Cost/Income ratio	43.9	43.7	
Overseas profit before tax contribution	39.6	40.8	
Credit costs on loans (bp)			
Non-impaired	1	(32)	
Impaired	15	61	
Total	16	28	
Non-performing loans ratio [2]	1.5	1.8	
Return on average ordinary shareholders' equity [3]	11.3	10.2	
Return on average total assets	1.07	0.98	
Return on average risk-weighted assets	1.93	1.63	
Loan/Deposit ratio [4]	88.2	85.1	
Liquidity coverage ratios (LCR) [5]			
All-currency	135	147	
Singapore Dollar	209	200	
Net stable funding ratio [6]	107	NA	
Capital adequacy ratios			
Common Equity Tier 1	13.9	15.1	
Tier 1	14.9	16.2	
Total	17.0	18.7	
Leverage ratio [7]	7.6	8.0	
Earnings per ordinary share ($) [3]			
Basic	2.34	1.99	
Diluted	2.33	1.98	
Net asset value (NAV) per ordinary share ($) [8]	21.31	20.37	
Revalued NAV per ordinary share ($) [8]	24.19	23.19	

1 Relates to amount attributable to equity holders of the Bank.
2 Refers to non-performing loans as a percentage of gross customer loans.
3 Calculated based on profit attributable to equity holders of the Bank net of perpetual capital securities distributions.
4 Refers to net customer loans and customer deposits.
5 Figures reported are based on average LCR for the respective year. A minimum requirement of Singapore Dollar LCR of 100% and all-currency LCR of 90% shall be maintained at all times with effect from 1 January 2018 (2017: 80%), with all-currency LCR increasing to 100% by 2019. Public disclosure required under MAS Notice 651 is available in the UOB website at www.UOBgroup.com/investor/financial/overview.html.
6 NSFR is calculated based on MAS Notice 652. A minimum requirement of 100% shall be maintained effective January 2018. Public disclosure required under MAS Notice 653 is available in the UOB website at www.UOBgroup.com/investor/financial/overview.html.
7 Leverage ratio is calculated based on the MAS Notice 637. A minimum ratio of 3% is required effective 1 January 2018.
8 Perpetual capital securities are excluded from the computation.

Performance Review

The Group achieved record net earnings of $4.01 billion for the full year of 2018, up 18% from a year ago.

Net interest income grew 13% to $6.22 billion, driven by broad-based loan growth and higher net interest margin. Net interest margin increased five basis points to 1.82%, in line with the rising interest rate environment.

Net fee and commission income increased 5% to $1.97 billion, driven by the strong performance in loan-related, credit card, trade-related and fund management fees. Other non-interest income declined 20% to $930 million mainly due to unrealised mark-to-market on investment securities and lower gains from sale of investment securities.

Business segments continued to deliver strong income growth. Total income for Group Retail rose 4% to $3.95 billion, supported by healthy volume growth and deposit margin improvement. Group Wholesale Banking reported an income growth of 11% to $3.94 billion, led by double-digit loan growth and broad-based increase in fee and customer treasury income. Total income for Global Markets grew 6% to $465 million, driven by favourable movements in foreign exchange and rates.

Total expenses increased 7% to $4.00 billion, largely driven by higher performance-related staff costs and IT-related expenses. This reflects the Group's continued commitment towards investing in talent and technology to improve product capabilities and customer experience and to reap benefits from digitalisation. The cost-to-income ratio for the year rose marginally to 43.9%.

Total allowances decreased 46% to $393 million with credit costs on impaired loans easing to 15 basis points. This reflected the fairly benign credit environment for most of 2018 as well as lower residual risks from the oil and gas and shipping sectors from the preceding years.

The Group's funding position remained strong with a healthy loan-to-deposit ratio at 88.2%. Gross loans increased 11% to $262 billion, led by broad-based increase across all territories and industries. Customer deposits grew 7% year on year to $293 billion, in tandem with loan growth.

The full-year average Singapore Dollar and all-currency liquidity coverage ratios were 209% and 135% respectively, well above the corresponding regulatory requirements of 100% and 90%. The net stable funding ratio was 107% as at 31 December 2018.

The non-performing loan ratio improved to 1.5% from 1.8% a year ago. The coverage for non-performing assets remained stable at 87%, or 202% after taking collateral into account. Total allowances for non-impaired assets remained adequate at $1.98 billion as at 31 December 2018.

Compared with last year, shareholders' equity increased 2% to $37.6 billion mainly driven by higher retained earnings.

As at 31 December 2018, the Group's Common Equity Tier 1 CAR remained strong at 13.9%. The Group's leverage ratio of 7.6% was more than double the regulatory minimum requirement of 3%. The Group remains well capitalised to navigate the macro uncertainties ahead.

Management Discussion and Analysis

Net Interest Income

Net Interest Margin

	2018			2017		
	Average balance $ million	Interest $ million	Average rate %	Average balance $ million	Interest $ million	Average rate %
Interest Bearing Assets						
Customer loans	245,138	8,844	3.61	227,666	7,474	3.28
Interbank balances	68,730	1,532	2.23	58,869	997	1.69
Securities	28,095	765	2.72	25,650	605	2.36
Total	341,962	11,141	3.26	312,185	9,077	2.91
Interest Bearing Liabilities						
Customer deposits	286,820	4,083	1.42	264,516	3,018	1.14
Interbank balances/others	40,067	838	2.09	36,270	531	1.46
Total	326,887	4,921	1.51	300,786	3,548	1.18
Net Interest Margin [1]			1.82			1.77

1 Net interest margin represents net interest income as a percentage of total interest bearing assets.

Volume and Rate Analysis

	2018 vs 2017			2017 vs 2016		
	Volume change $ million	Rate change $ million	Net change $ million	Volume change $ million	Rate change $ million	Net change $ million
Interest Income						
Customer loans	574	796	1,369	490	(133)	356
Interbank balances	167	368	535	118	242	360
Securities	58	102	160	(64)	133	69
Total	798	1,266	2,064	544	242	786
Interest Expense						
Customer deposits	254	810	1,065	139	1	140
Interbank balances/others	56	252	308	56	53	108
Total	310	1,062	1,373	195	54	249
Net Interest Income	488	204	692	349	189	537

Net interest income grew 13% year on year to $6.22 billion, driven by broad-based loan growth and higher net interest margin. Net interest margin increased five basis points to 1.82%, in line with the rising interest rate environment.

Non-Interest Income

	2018 $ million	2017 $ million	+/(–) %
Net Fee and Commission Income			
Credit card [1]	**440**	404	9
Fund management	**261**	239	9
Wealth management	**543**	547	(1)
Loan-related [2]	**545**	471	16
Service charges	**154**	148	4
Trade-related [3]	**296**	272	9
Others	**63**	80	(21)
	2,303	2,161	7
Less: Fee and commission expenses [4]	**(336)**	(289)	(16)
	1,967	1,873	5
Other Non-Interest Income			
Net trading income	**683**	775	(12)
Net (loss)/gain from investment securities	**(35)**	127	(>100)
Dividend income	**27**	23	20
Rental income	**119**	119	(0)
Other income	**136**	117	16
	930	1,162	(20)
Total	**2,896**	3,035	(5)

1 Credit card fees are net of interchange fees paid.
2 Loan-related fees include fees earned from corporate finance activities.
3 Trade-related fees include trade, remittance and guarantees related fees.
4 Fee and commission expenses that are directly attributable to the fee and commission income. Certain comparative figures have been restated to conform with the current period's presentation.

Net fee and commission income for the year increased 5% to $1.97 billion, driven by the strong performance in loan-related, credit card, trade-related and fund management fees. Other non-interest income declined 20% to $930 million mainly due to unrealised mark-to-market on investment securities and lower gains from sale of investment securities.

Management Discussion and Analysis

Operating Expenses

	2018 $ million	2017 $ million	+/(–) %
Staff Costs	**2,447**	2,224	10
Other Operating Expenses			
Revenue-related [1]	**592**	600	(1)
Occupancy-related	**321**	332	(3)
IT-related	**414**	365	13
Others	**228**	217	5
	1,556	1,515	3
Total	**4,003**	3,739	7

1 Expenses directly attributable to fee and commission income are presented net of fee and commission income. Certain comparative figures have been restated to conform with current period's presentation.

Total expenses for the year increased 7% to $4.00 billion, largely driven by higher performance-related staff costs and IT-related expenses. This reflects the Group's continued commitment towards investing in talent and technology to improve product capabilities and customer experience and to reap benefits from digitalisation. The cost-to-income ratio for the year rose marginally to 43.9%.

Allowance for Credit and Other Losses

	2018 $ million	2017 $ million	+/(–) %
Allowance for non-impaired assets	**19**	(747)	>100
Allowance for impaired loans [1]			
Singapore	**201**	733	(73)
Malaysia	**(21)**	177	(>100)
Thailand	**111**	131	(16)
Indonesia	**123**	258	(52)
Greater China [2]	**16**	39	(59)
Others	**(54)**	68	(>100)
	376	1,407	(73)
Allowance for impaired securities and others	**(2)**	68	(>100)
Total	**393**	727	(46)

1 Allowance for impaired loans by geography is classified according to where credit risks reside, which is largely represented by the borrower's country of incorporation/operation for non-individuals and residence for individuals.
2 Comprise China, Hong Kong and Taiwan.

Total allowances for the year decreased 46% to $393 million with credit costs on impaired loans easing to 15 basis points. This reflected the fairly benign credit environment for most of 2018 as well as lower residual risks from the oil and gas and shipping sectors from the preceding years.

Customer Loans

	2018 $ million	2017 $ million
Gross customer loans	**261,707**	236,028
Less: Allowance for non-impaired loans	**1,571**	1,961
Allowance for impaired loans	**1,508**	1,855
Net customer loans	**258,627**	232,212
By Industry		
Transport, storage and communication	**10,185**	9,388
Building and construction	**63,139**	53,646
Manufacturing	**21,112**	18,615
Financial institutions, investment and holding companies	**23,199**	19,090
General commerce	**32,928**	30,664
Professionals and private individuals	**29,288**	28,182
Housing loans	**68,387**	65,569
Others	**13,469**	10,874
Total (gross)	**261,707**	236,028
By Currency		
Singapore Dollar	**123,347**	115,750
US Dollar	**50,674**	44,507
Malaysian Ringgit	**25,328**	24,000
Thai Baht	**15,600**	14,006
Indonesian Rupiah	**5,288**	4,853
Others	**41,471**	32,912
Total (gross)	**261,707**	236,028
By Maturity		
Within 1 year	**104,686**	92,969
Over 1 year but within 3 years	**48,826**	42,828
Over 3 years but within 5 years	**30,452**	24,851
Over 5 years	**77,744**	75,379
Total (gross)	**261,707**	236,028
By Geography [1]		
Singapore	**137,176**	127,602
Malaysia	**29,315**	26,948
Thailand	**16,813**	14,977
Indonesia	**11,289**	10,718
Greater China	**40,081**	32,301
Others	**27,033**	23,482
Total (gross)	**261,707**	236,028

1 Loans by geography are classified according to where credit risks reside, which is largely represented by the borrower's country of incorporation/operation for non-individuals and residence for individuals.

As at 31 December 2018, gross loans rose 11% year on year to $262 billion, led by broad-based increase across all territories and industries.

Singapore loans grew 8% from a year ago to $137 billion as at 31 December 2018, while regional countries registered a strong growth of 15% in the same period.

Management Discussion and Analysis

Non-Performing Assets

	2018 $ million	2017 $ million
Non-Performing Assets (NPA)		
Loans (NPL)	3,994	4,211
Debt securities and others	172	178
Total	4,166	4,389
By Grading		
Substandard	2,512	2,411
Doubtful	230	128
Loss	1,424	1,850
Total	4,166	4,389
By Security		
Secured by collateral type:		
Properties	1,897	1,771
Shares and debentures	6	8
Fixed deposits	13	12
Others [1]	453	467
	2,369	2,258
Unsecured	1,797	2,131
Total	4,166	4,389
By Ageing		
Current	885	936
Within 90 days	581	600
Over 90 to 180 days	379	735
Over 180 days	2,321	2,118
Total	4,166	4,389
Total Allowance		
Non-impaired	1,984	1,976
Impaired	1,651	2,014
Total	3,636	3,990

	2018		2017	
	NPL $ million	NPL ratio %	NPL $ million	NPL ratio %
NPL by Industry				
Transport, storage and communication	813	8.0	1,209	12.9
Building and construction	497	0.8	428	0.8
Manufacturing	709	3.4	638	3.4
Financial institutions, investment and holding companies	41	0.2	92	0.5
General commerce	511	1.6	485	1.6
Professionals and private individuals	320	1.1	295	1.0
Housing loans	739	1.1	677	1.0
Others	364	2.7	387	3.6
Total	3,994	1.5	4,211	1.8

1 Comprise mainly of marine vessels.

Non-Performing Assets (continued)

	NPL/NPA $ million	NPL ratio %	Allowances for impaired assets $ million	Allowances for impaired assets as a % of NPL/NPA %
NPL by Geography [1]				
Singapore				
2018	**2,085**	**1.5**	**818**	**39**
2017	2,058	1.6	934	45
Malaysia				
2018	**558**	**1.9**	**161**	**29**
2017	585	2.2	220	38
Thailand				
2018	**456**	**2.7**	**153**	**34**
2017	439	2.9	157	36
Indonesia				
2018	**545**	**4.8**	**221**	**41**
2017	694	6.5	312	45
Greater China				
2018	**120**	**0.3**	**53**	**44**
2017	132	0.4	76	58
Others				
2018	**230**	**0.9**	**102**	**44**
2017	303	1.3	156	52
Group NPL				
2018	**3,994**	**1.5**	**1,508**	**38**
2017	4,211	1.8	1,855	44
Group NPA				
2018	**4,166**		**1,651**	**40**
2017	4,389		2,014	46

	Total allowances	
	as a % of NPA %	as a % of unsecured NPA %
Group		
2018	**87**	**202**
2017	91	187

1 Non-performing loans by geography are classified according to where credit risks reside, which is largely represented by the borrower's country of incorporation/operation for non-individuals and residence for individuals.

The Group's overall loan portfolio remained sound. Total NPA decreased 5% year on year to $4.17 billion.

NPL ratio improved to 1.5% as at 31 December 2018, 0.3% point lower than last year. The coverage for non-performing assets remained adequate at 87%, or 202% after taking collateral into account.

Management Discussion and Analysis

Customer Deposits

	2018 $ million	2017 $ million
By Product		
Fixed deposits	150,071	139,257
Savings deposits	71,601	66,404
Current accounts	58,858	57,570
Others	12,656	9,534
Total	293,186	272,765
By Maturity		
Within 1 year	289,448	268,233
Over 1 year but within 3 years	2,085	2,545
Over 3 years but within 5 years	833	1,174
Over 5 years	819	813
Total	293,186	272,765
By Currency		
Singapore Dollar	130,981	123,806
US Dollar	71,704	67,739
Malaysian Ringgit	28,312	26,475
Thai Baht	17,148	15,317
Indonesian Rupiah	5,148	5,119
Others	39,894	34,308
Total	293,186	272,765
Group Loan/Deposit ratio (%)	88.2	85.1
Singapore Dollar Loan/Deposit ratio (%)	93.5	92.3
US Dollar Loan/Deposit ratio (%)	69.5	63.9

Customer deposits as at 31 December 2018 increased 7% year on year to $293 billion, in tandem with loan growth.

As at 31 December 2018, the Group's loan-to-deposit ratio and Singapore Dollar loan-to-deposit ratio remained healthy at 88.2% and 93.5% respectively.

Debts Issued

	2018 $ million	2017 $ million
Unsecured		
Subordinated debts	5,062	4,827
Commercial papers	13,974	13,674
Fixed and floating rate notes	5,586	2,630
Others	1,583	1,801
Secured		
Covered bonds	4,401	2,247
Total	30,606	25,178
Due within 1 year	15,680	14,807
Due after 1 year	14,926	10,371
Total	30,606	25,178

Shareholders' Equity

	2018 $ million	2017 $ million
Shareholders' equity	**37,623**	36,850
Add: Revaluation surplus	**4,802**	4,679
Shareholders' equity including revaluation surplus	**42,425**	41,529

Compared with last year, shareholders' equity increased 2% to $37.6 billion mainly driven by higher retained earnings.

As at 31 December 2018, the revaluation surplus of $4.80 billion relating to the Group's properties, was not recognised in the financial statements.

Performance by Business Segment [1,2]

	GR $ million	GWB $ million	GM $ million	Others $ million	Total $ million
2018					
Net interest income	**2,721**	**2,829**	**125**	**545**	**6,220**
Non-interest income	**1,230**	**1,108**	**340**	**218**	**2,896**
Operating income	**3,951**	**3,937**	**465**	**763**	**9,116**
Operating expenses	**(1,928)**	**(954)**	**(245)**	**(876)**	**(4,003)**
Allowance for credit and other losses	**(192)**	**(178)**	**(2)**	**(21)**	**(393)**
Share of profit of associates and joint ventures	**–**	**14**	**–**	**92**	**106**
Profit before tax	**1,831**	**2,819**	**218**	**(42)**	**4,826**
Tax					**(805)**
Profit for the financial year					**4,021**
2017					
Net interest income	2,550	2,472	237	269	5,528
Non-interest income	1,231	1,060	203	541	3,035
Operating income	3,781	3,532	440	810	8,563
Operating expenses	(1,800)	(819)	(253)	(867)	(3,739)
Allowance for credit and other losses	(218)	(1,280)	1	770	(727)
Share of profit of associates and joint ventures	–	4	–	106	110
Profit before tax	1,763	1,437	188	819	4,207
Tax					(800)
Profit for the financial year					3,407

1 Operating income is presented net of fee and commission expense.
2 Comparative segment information for the prior year has been adjusted for changes in organisational structure and management reporting methodology.

Performance by Business Segment (continued)

The Banking Group is organised into three major business segments – Group Retail, Group Wholesale Banking and Global Markets. Others includes non-banking activities and corporate functions.

Group Retail (GR)

Compared to a year ago, profit before tax grew 4% to $1.83 billion. Total income increased 4% to $3.95 billion largely supported by net interest income which rose 7% from healthy volume growth and deposit margin improvement. Non-interest income was broadly unchanged while expenses were higher by 7% from ongoing investments in staff and digital capabilities to drive retail franchise growth.

Group Wholesale Banking (GWB)

Operating profit grew 10% to $2.98 billion from a year ago. Total income rose 11% to $3.94 billion, driven by stronger net interest income from double-digit growth in volume and margin improvement on the back of rising interest rates. Non-interest income increased 5% to $1.11 billion from loan-related fees, trade and investment banking. Expenses were 16% higher primarily from continued investments in technology and headcount to support customer franchise and regional expansion. Profit before tax surged 96% to $2.82 billion as credit costs eased in a benign credit environment.

Global Markets (GM)

Compared to a year ago, profit before tax rose 16% to $218 million. Total income grew 6% to $465 million from favourable movements in foreign exchange and rates. Expenses declined 3% to $245 million.

Others

Others registered a loss of $42 million for the year as compared to a net profit of $819 million a year ago mainly due to gain from sale of equity investments and reversal of allowances for non-impaired assets last year.

Performance by Geographical Segment [1]

	Total operating income		Profit before tax	
	2018	2017	**2018**	2017
	$ million	$ million	**$ million**	$ million
Singapore	**5,123**	4,913	**2,917**	2,491
Malaysia	**1,068**	985	**600**	581
Thailand	**964**	871	**282**	218
Indonesia	**444**	461	**77**	29
Greater China	**864**	751	**443**	419
Others	**653**	582	**507**	469
Total	**9,116**	8,563	**4,826**	4,207

1 Based on the location where the transactions and assets are booked. Information is stated after elimination of inter-segment transactions.

Total operating income for 2018 rose 6% year on year to $9.12 billion, led by broad-based growth across most of the geographical segments.

Profit before tax also registered a strong growth of 15% to $4.83 billion from a year ago, on the back of strong performance and lower allowances in a fairly benign credit environment.

Capital Adequacy and Leverage Ratios

	2018 $ million	2017 $ million
Common Equity Tier 1 capital (CET1)	**30,750**	30,134
Additional Tier 1 capital	**2,129**	2,086
Tier 1 capital	**32,879**	32,220
Tier 2 capital	**4,663**	5,128
Eligible total capital	**37,542**	37,348
Risk-weighted assets (RWA)	**220,568**	199,481
Capital adequacy ratios (CAR)		
CET1	**13.9%**	15.1%
Tier 1	**14.9%**	16.2%
Total	**17.0%**	18.7%
Leverage ratio	**7.6%**	8.0%

The Group's CET1, Tier 1 and Total CAR as at 31 December 2018 were well above the regulatory minimum requirements.

Year on year, total capital was higher mainly from retained earnings, partly offset by redemption of the S$850 million perpetual capital securities and lower eligible provisions. RWA was higher largely due to asset growth.

As at 31 December 2018, the Group's leverage ratio was 7.6%, comfortably above the regulatory minimum requirement of 3%.