

China Banking Sector

Corporate day takeaways – Retail banks in better position

Last week, we hosted investor conferences with four China banks, including CCB, BOC, PSBC, and CMB. Overall, management anticipated softening bottom-line growth in FY20 due to falling yields and profit-sacrifice guidance. On bright side, hard-hit areas amid COVID-19's outbreak, i.e. credit card and personal consumption loans, were recovering rapidly in 2Q20. We believe the worst period of retail asset quality deterioration is already behind us, and NPL pressure will mainly come from corporate side in 2H20. As such, we turned more positive on retail-focused banks. **Top picks are PAB, PSBC and CEB.**

- Steady recovery in retail credit.** All four banks indicated accelerated retail lending along with gradual work resumption in 2Q20, after a temporary slowdown in 1Q20. PSBC and CMB planned to allocate majority of the full-year loan quota to retail segment, meaning even faster catch-up for personal credit in 2H20. Banks saw stable mortgage growth, but were cautious towards financing to property developers given ongoing real estate tightening.
- Asset yield retreat to further squeeze margin.** All banks acknowledged still heavy NIM pressure, as asset yields are falling due to LPR reform and notably lower interest of MSE loans, while deposit cost stays relatively rigid. However, the pace of yield decline might become slower in 2H20. BOC saw relatively stable pricing for retail loans and expected this trend to persist in coming quarters.
- Benign asset quality in 2Q20 but uncertainties remain.** CMB expected the formation of retail NPLs to peak in 2Q20, but corporate asset quality might start to worsen in 3Q20 and could last until 2021. The spread of COVID-19 in overseas countries will disrupt global supply chain, and it takes time for export orders to recover to pre-pandemic status. Our observation on banks' NPL statistics during 2013-2016 credit cycle also suggests that corporate asset quality movement is hysteretic to retail by around 6 months.
- Expect subdued FY20E earnings growth.** A sector-wide moderation in net profit growth might be inevitable in FY20, although it has been largely priced in current valuation (0.61x/0.73x P/B for H/A-share China banks), in our view. That said, most banks are keeping at least 30% payout ratio, and they did not receive guidance to cut dividend. Potential acquisition of brokerage license would benefit banks' business prospects with stronger client-servicing capacity and improved customer stickiness.

Valuation Table

Name	Ticker	Price (Local ccy)	TP (Local ccy)	Rating	P/B (x) FY20E	P/E (x) FY20E	Yield FY20E	ROE FY20E
ICBC	1398 HK	4.86	7.50	BUY	0.58	4.8	6.3%	12.5%
CCB	939 HK	6.12	9.10	BUY	0.60	5.0	6.1%	12.6%
ABC	1288 HK	2.89	4.70	BUY	0.48	4.2	7.4%	11.9%
BOC	3988 HK	2.77	4.60	BUY	0.41	3.9	8.0%	11.0%
PSBC	1658 HK	4.53	6.70	BUY	0.65	5.3	5.8%	12.7%
CITICB	998 HK	3.56	5.60	BUY	0.33	3.1	8.3%	11.0%
CEB	6818 HK	3.08	4.90	BUY	0.42	3.7	8.4%	11.8%
BoCom	3328 HK	4.48	6.20	HOLD	0.40	3.8	8.1%	10.9%
MSB	1988 HK	4.98	6.30	HOLD	0.40	3.5	8.7%	11.9%
PAB	00001 CH	14.14	19.80	BUY	0.91	8.8	1.7%	10.8%

Source: Bloomberg, CMBIS estimates

OUTPERFORM
(Maintain)

China Banking Sector

Terry Sun, CFA
 (852) 3900 0836
 terrysun@cmbi.com.hk

Historical P/B of H-share China banks



Source: Bloomberg, CMBIS

Historical P/B of A-share China banks



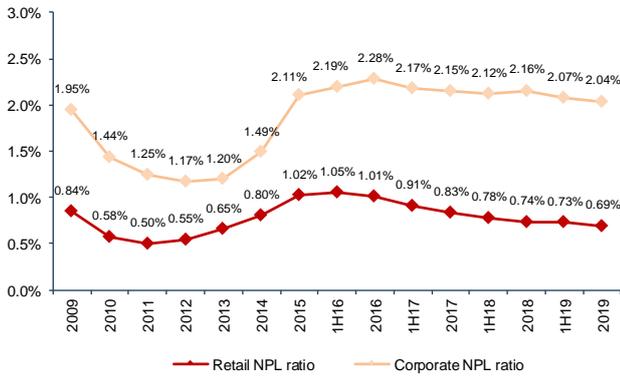
Source: Bloomberg, CMBIS

Related Reports

- Rising credit support from targeted RRR cut & ER rate cut – 6 Apr 2020
- 4Q19 results wrap – steady FY19 but challenging FY20 – 31 Mar 2020
- Assessing COVID-19's impact (III) – Is benchmark deposit rate cut a policy option? – 18 Feb 2020
- Assessing COVID-19's impact (II) – Delay in compliance of Asset Management Rule? – 11 Feb 2020
- Assessing COVID-19's impact (I) – 5 Feb 2020

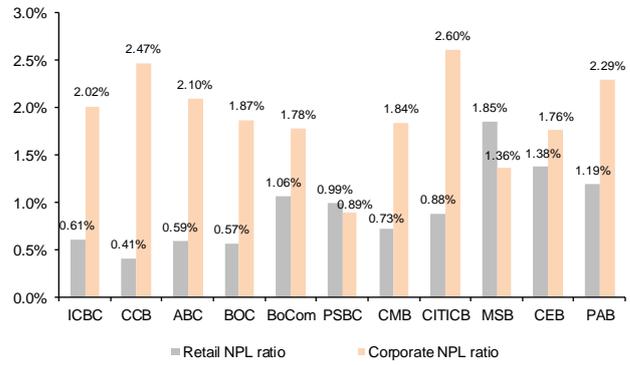
Please cast your valuable vote for CMBIS research team in the 2020 Asiamoney Brokers Poll:
<https://euromoney.com/brokers>

Figure 1: China banks' retail and corporate NPL ratio



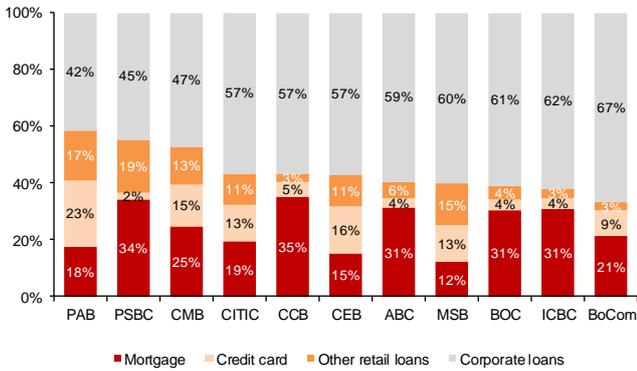
Source: Company data, CMBIS; Average data for 11 China banks, including ICBC, CCB, ABC, BOC, BoCom, PSBC, CMB, CITICB, MSB, CEB, PAB

Figure 2: Individual banks' retail and corporate NPL ratio (as of 2019)



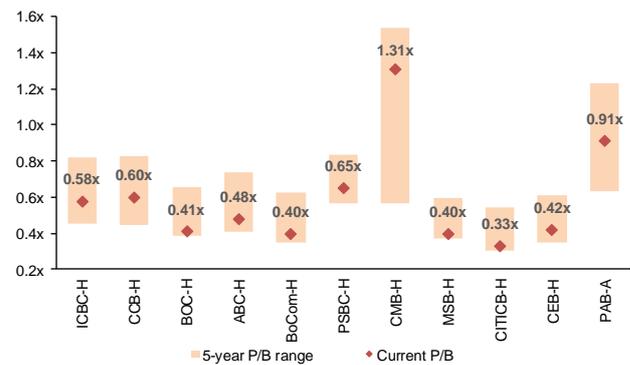
Source: Company data, CMBIS

Figure 3: Individual banks' loan mix (as of 2019)



Source: Company data, CMBIS

Figure 4: Individual banks' P/B and 5-year range



Source: Bloomberg, CMBIS

Figure 5: Valuation summary

Company	Ticker	Mkt cap (bn)	Last Price	TP	Rating	P/B (x)		P/E (x)		Yield		ROE	
		(Local ccy)	(Local ccy)	(Local ccy)		2020E	2021E	2020E	2021E	2020E	2021E	2020E	2021E
H-share													
ICBC	1398 HK	1,935	4.86	7.50	BUY	0.58	0.53	4.8	4.5	6.3%	6.7%	12.5%	12.1%
CCB	939 HK	1,538	6.12	9.10	BUY	0.60	0.55	5.0	4.7	6.1%	6.5%	12.6%	12.3%
ABC	1288 HK	1,250	2.89	4.70	BUY	0.48	0.44	4.2	4.0	7.4%	7.7%	11.9%	11.6%
BOC	3988 HK	1,029	2.77	4.60	BUY	0.41	0.38	3.9	3.7	8.0%	8.4%	11.0%	10.7%
PSBC	1658 HK	441	4.53	6.70	BUY	0.65	0.59	5.3	4.7	5.8%	6.6%	12.7%	13.2%
CITICB	998 HK	250	3.56	5.60	BUY	0.33	0.30	3.1	2.8	8.3%	9.2%	11.0%	11.2%
CEB	6818 HK	210	3.08	4.90	BUY	0.42	0.39	3.7	3.4	8.4%	9.2%	11.8%	11.9%
BoCom	3328 HK	370	4.48	6.20	HOLD	0.40	0.37	3.8	3.6	8.1%	8.6%	10.9%	10.6%
MSB	1988 HK	262	4.98	6.30	HOLD	0.40	0.37	3.5	3.3	8.7%	9.2%	11.9%	11.7%
CMB	3968 HK	999	37.75	-	NR	1.31	1.17	8.6	7.7	3.8%	4.3%	16.0%	16.3%
Average						0.61	0.56	4.9	4.6	6.6%	7.0%	12.5%	12.3%
A-share													
ICBC	601398 CH	1,745	5.06	7.80	BUY	0.67	0.61	5.6	5.3	5.5%	5.8%	12.5%	12.1%
CCB	601939 CH	1,387	6.29	9.50	BUY	0.69	0.63	5.7	5.3	5.4%	5.7%	12.6%	12.3%
ABC	601288 CH	1,127	3.28	5.20	BUY	0.60	0.56	5.3	5.0	5.8%	6.1%	11.9%	11.6%
BOC	601988 CH	928	3.41	5.00	BUY	0.56	0.52	5.3	5.1	5.8%	6.1%	11.0%	10.7%
PSBC	601658 CH	398	4.72	7.20	BUY	0.75	0.69	6.2	5.4	5.0%	5.7%	12.7%	13.2%
CITICB	601998 CH	226	5.22	7.30	BUY	0.53	0.49	5.0	4.6	5.1%	5.6%	11.0%	11.2%
CEB	601818 CH	189	3.87	5.50	BUY	0.59	0.54	5.2	4.7	6.0%	6.6%	11.8%	11.9%
PAB	000001 CH	274	14.14	19.80	BUY	0.91	0.83	8.8	7.7	1.7%	2.0%	10.8%	11.2%
BoCom	601328 CH	333	4.89	6.50	HOLD	0.49	0.45	4.6	4.4	6.7%	7.0%	10.9%	10.6%
MSB	600016 CH	236	5.60	7.00	HOLD	0.50	0.46	4.4	4.1	6.9%	7.4%	11.9%	11.7%
CMB	600036 CH	901	36.08	-	NR	1.40	1.23	9.0	7.9	3.6%	4.1%	16.1%	16.5%
Average						0.73	0.66	6.0	5.5	5.3%	5.6%	12.5%	12.3%

Source: Bloomberg, CMBIS estimates; CMB's valuation is based on Bloomberg consensus.

Disclosures & Disclaimers

Analyst Certification

The research analyst who is primary responsible for the content of this research report, in whole or in part, certifies that with respect to the securities or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by that analyst in this report.

Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the stock(s) covered in this research report 3 business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong listed companies covered in this report; and (4) have any financial interests in the Hong Kong listed companies covered in this report.

Disclosure

CMBIS or its affiliate(s) have investment banking relationship with the issuers covered in this report in preceding 12 months.

CMBIS Ratings

BUY	: Stock with potential return of over 15% over next 12 months
HOLD	: Stock with potential return of +15% to -10% over next 12 months
SELL	: Stock with potential loss of over 10% over next 12 months
NOT RATED	: Stock is not rated by CMBIS
OUTPERFORM	: Industry expected to outperform the relevant broad market benchmark over next 12 months
MARKET-PERFORM	: Industry expected to perform in-line with the relevant broad market benchmark over next 12 months
UNDERPERFORM	: Industry expected to underperform the relevant broad market benchmark over next 12 months

CMB International Securities Limited

Address: 45/F, Champion Tower, 3 Garden Road, Hong Kong, Tel: (852) 3900 0888 Fax: (852) 3900 0800

CMB International Securities Limited ("CMBIS") is a wholly owned subsidiary of CMB International Capital Corporation Limited (a wholly owned subsidiary of China Merchants Bank)

Important Disclosures

There are risks involved in transacting in any securities. The information contained in this report may not be suitable for the purposes of all investors. CMBIS does not provide individually tailored investment advice. This report has been prepared without regard to the individual investment objectives, financial position or special requirements. Past performance has no indication of future performance, and actual events may differ materially from that which is contained in the report. The value of, and returns from, any investments are uncertain and are not guaranteed and may fluctuate as a result of their dependence on the performance of underlying assets or other variable market factors. CMBIS recommends that investors should independently evaluate particular investments and strategies, and encourages investors to consult with a professional financial advisor in order to make their own investment decisions.

This report or any information contained herein, have been prepared by the CMBIS, solely for the purpose of supplying information to the clients of CMBIS or its affiliate(s) to whom it is distributed. This report is not and should not be construed as an offer or solicitation to buy or sell any security or any interest in securities or enter into any transaction. Neither CMBIS nor any of its affiliates, shareholders, agents, consultants, directors, officers or employees shall be liable for any loss, damage or expense whatsoever, whether direct or consequential, incurred in relying on the information contained in this report. Anyone making use of the information contained in this report does so entirely at their own risk.

The information and contents contained in this report are based on the analyses and interpretations of information believed to be publicly available and reliable. CMBIS has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIS provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIS may issue other publications having information and/ or conclusions different from this report. These publications reflect different assumption, point-of-view and analytical methods when compiling. CMBIS may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIS may have a position, make markets or act as principal or engage in transactions in securities of companies referred to in this report for itself and/or on behalf of its clients from time to time. Investors should assume that CMBIS does or seeks to have investment banking or other business relationships with the companies in this report. As a result, recipients should be aware that CMBIS may have a conflict of interest that could affect the objectivity of this report and CMBIS will not assume any responsibility in respect thereof. This report is for the use of intended recipients only and this publication, may not be reproduced, reprinted, sold, redistributed or published in whole or in part for any purpose without prior written consent of CMBIS.

Additional information on recommended securities is available upon request.

For recipients of this document in the United Kingdom

This report has been provided only to persons (I) falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended from time to time) ("The Order") or (II) are persons falling within Article 49(2) (a) to (d) ("High Net Worth Companies, Unincorporated Associations, etc.") of the Order, and may not be provided to any other person without the prior written consent of CMBIS.

For recipients of this document in the United States

This report is intended for distribution in the United States to "major US institutional investors", as defined in Rule 15a-6 under the US, Securities Exchange Act of 1934, and may not be furnished to any other person in the United States. Each major US, institutional investor that receives a copy of this research report by its acceptance hereof represents and agrees that it shall not distribute or provide this research report to any other person.

For recipients of this document in Singapore

This report is distributed in Singapore by CMBI (Singapore) Pte. Limited (CMBISG) (Company Regn. No. 201731928D), an Exempt Financial Adviser as defined in the Financial Advisers Act (Cap. 110) of Singapore and regulated by the Monetary Authority of Singapore. CMBISG may distribute reports produced by its respective foreign entities, affiliates or other foreign research houses pursuant to an arrangement under Regulation 32C of the Financial Advisers Regulations. Where the report is distributed in Singapore to a person who is not an Accredited Investor, Expert Investor or an Institutional Investor, as defined in the Securities and Futures Act (Cap. 289) of Singapore, CMBISG accepts legal responsibility for the contents of the report to such persons only to the extent required by law. Singapore recipients should contact CMBISG at +65 6350 4400 for matters arising from, or in connection with the report.