

Bank of Communications (3328 HK)

Muted earnings growth on COVID-19's shock

BoCom's 1Q20 net profit rose 1.8% YoY to RMB21.5bn, accounting for 26.5%/27.8% of CMBIS/consensus full-year estimates. The lackluster profit growth was mainly due to rising impairment charges (+11% YoY) and falling NIM, despite faster expansion in interest-earning assets. We expect asset quality pressure to persist in 2Q20, as COVID-19's impact further materializes. But NPL formation could start to ease in 3Q20, barring any worsening of the pandemic, as guided by management.

- **Results positives:** 1) **Asset growth was healthy at 5.5% QoQ**, on 5.0% QoQ loan extension and 7.4% QoQ boost in securities investments. As such, net interest income had a decent growth of 5.4% YoY. New loans were mainly towards corporate segment (+7.3% QoQ) on policy stimulus, while retail lending was subdued (0.2% QoQ) amid weak consumption activities in 1Q20. 2) **Deposit growth also picked up to 4.8% QoQ**, from 0.4% in 4Q19. LDR remained largely stable at 87.5%. 3) **Net fee income was up 5.4% YoY**, driven by agency and management service fees, especially from wealth management business. 4) **Tax expense declined 11.7% YoY**, likely due to rising investment to tax-free govt bonds.
- **Results negatives:** 1) **NIM narrowed 4bp YoY to 1.55**, as overall asset yield (-16bp) shrank faster than liability cost (-13bp). In particular, loan yield dropped 19bp YoY after series of LPR cut, while deposit cost stayed relatively rigid (-2bp). We expect further NIM downside, although liquidity loosening could help to ease interbank funding cost. 2) **Asset quality deteriorated**. NPL ratio climbed 12bp QoQ to 1.59%, and provision coverage pulled back 17.6ppt QoQ to 154.2%. BoCom saw more significant NPL pressure than SOE bank peers, partly due to higher exposure to credit card, of which NPL balance rose 10-20% in 1Q20. Meanwhile, one of the Bank's two loan collection centers was located in Wuhan, so it lost 45% of collection capacity during the city's lockdown. 3) **Capital ratio weakened**, as CET1 and total CAR declined 39bp QoQ and 67bp QoQ to 10.83% and 14.16%, respectively.
- **Maintain HOLD and lower TP to HK\$5.70**. We trim our FY20-22E earnings estimates by 2.8-4.2%, as we lower NIM forecast by 2-3bp and raise credit cost assumption by 4-5bp to factor in COVID-19's impact. Our new HK\$5.70 TP is derived from 0.51x target P/B and FY20E BPS of RMB10.0.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Operating income (RMB mn)	205,932	221,040	237,029	251,314	272,328
Net profit (RMB mn)	73,630	77,281	78,726	81,555	86,477
EPS (RMB)	0.96	1.00	1.02	1.06	1.13
EPS CHG (%)	5.2	5.1	1.9	3.7	6.2
Consensus EPS (RMB)	NA	NA	1.02	1.06	1.11
P/E (x)	4.7	4.4	4.4	4.2	4.0
P/B (x)	0.52	0.48	0.44	0.41	0.39
Dividend yield (%)	6.7	7.1	7.1	7.4	7.8
ROE (%)	11.4	11.2	10.6	10.2	10.1
NPL ratio (%)	1.49	1.47	1.54	1.49	1.45
Provision coverage (%)	173	172	166	176	187

Source: Company data, Bloomberg, CMBIS estimates

HOLD (Maintain)

Target Price **HK\$ 5.70**
 (Previous TP **HK\$ 6.20**)
 Up/Downside **+14.5%**
 Current Price **HK\$ 4.98**

China Banking Sector

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Stock Data

Mkt Cap (HK\$ mn)	395,509
Avg 3 mths t/o (HK\$ mn)	138
52w High/Low (HK\$)	6.73/4.2
Total Issued Shares (mn)	35,012 (H)
	39,251 (A)

Source: Bloomberg

Shareholding Structure

MoF	23.88%
HSBC	18.70%
NCSSF	6.07%

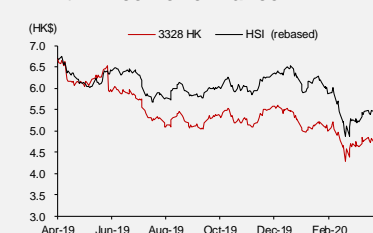
Source: Company data

Share Performance

	Absolute	Relative
1-mth	3.6%	0.2%
3-mth	-7.8%	6.2%
6-mth	-9.0%	0.0%
12-mth	-26.8%	-10.7%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: PwC

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Figure 1: 1Q20 results summary

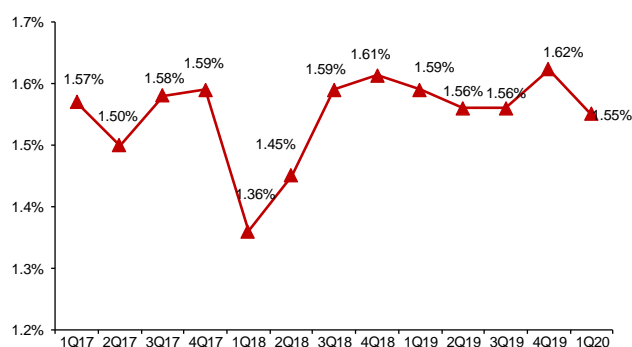
(RMB mn)						
P&L	4Q19	1Q20	QoQ	1Q19	1Q20	YoY
Net interest income	37,756	36,736	-2.7%	34,857	36,736	5.4%
Net fee and commission income	9,167	12,596	37.4%	12,056	12,596	4.5%
Operating income	54,245	57,586	6.2%	55,493	57,586	3.8%
Operating expense	(19,459)	(21,371)	9.8%	(20,316)	(21,371)	5.2%
PPoP	34,786	36,215	4.1%	35,177	36,215	3.0%
Impairment losses	(15,273)	(11,892)	-22.1%	(10,705)	(11,892)	11.1%
Pre-tax profit	19,513	24,323	24.7%	24,472	24,323	-0.6%
Income tax	(1,878)	(2,804)	49.3%	(3,175)	(2,804)	-11.7%
Net profit	17,134	21,451	25.2%	21,071	21,451	1.8%

B/S	4Q19	1Q20	QoQ	1Q19	1Q20	YoY
Gross loans	5,304,275	5,568,059	5.0%	5,068,189	5,568,059	9.9%
Customers' deposits	6,072,908	6,366,064	4.8%	6,106,174	6,366,064	4.3%
Total assets	9,905,600	10,454,383	5.5%	9,785,747	10,454,383	6.8%
NPLs	78,043	88,455	13.3%	74,662	88,455	18.5%

Key ratios	4Q19	1Q20	QoQ	1Q19	1Q20	YoY
NIM	1.62%	1.55%	-7bp	1.59%	1.55%	-4bp
ROE	10.0%	12.2%	2.2ppt	13.0%	12.2%	-0.8ppt
NPL ratio	1.47%	1.59%	12bp	1.47%	1.59%	12bp
Provision coverage	171.8%	154.2%	-17.6ppt	173.5%	154.2%	-19.3ppt
LDR	87.3%	87.5%	0.1ppt	83.0%	87.5%	4.5ppt
CET-1 CAR	11.2%	10.8%	-39bp	11.2%	10.8%	-37bp

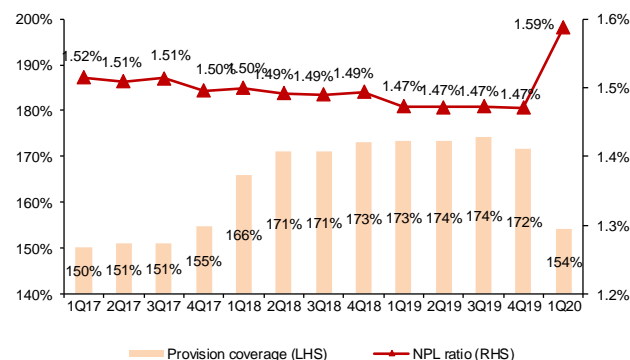
Source: Company data, CMBIS

Figure 2: Quarterly NIM of BoCom



Source: Company data, CMBIS

Figure 3: NPL ratio and provision coverage of BoCom



Source: Company data, CMBIS

Figure 4: Adjustments of earnings forecasts

	Net profit (RMB mn)			EPS (RMB)			NIM			Credit cost		
	Old	New	Change	Old	New	Change	Old	New	Change	Old	New	Change
FY20E	80,988	78,726	-2.8%	1.05	1.02	-2.5%	1.55%	1.53%	-2bp	0.98%	1.02%	+4bp
FY21E	85,060	81,555	-4.1%	1.11	1.06	-4.3%	1.53%	1.50%	-3bp	0.95%	1.00%	+5bp

Source: Company, CMBIS estimates

Financial Summary

Income Statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Interest income	348,864	367,453	397,406	423,863	457,196
Interest expenses	(217,956)	(223,370)	(242,621)	(260,884)	(279,750)
Net interest income	130,908	144,083	154,786	162,979	177,446
Net fee income	41,237	43,625	46,731	50,002	53,503
Others	33,787	33,332	35,512	38,333	41,379
Operating income	205,932	221,040	237,029	251,314	272,328
Operating expenses	(75,898)	(80,668)	(87,991)	(95,307)	(104,177)
PPoP	130,034	140,372	149,038	156,007	168,152
Provision	(43,514)	(52,224)	(59,258)	(63,031)	(69,614)
Operating profit	86,520	88,148	89,780	92,977	98,538
Non-operating income	(453)	52	52	52	52
Pre-tax profit	86,067	88,200	89,832	93,029	98,590
Income tax expenses	(11,902)	(10,138)	(10,326)	(10,693)	(11,332)
Minority interests	(535)	(781)	(781)	(781)	(781)
Net profit	73,630	77,281	78,726	81,555	86,477

Key Ratio

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Op. income mix					
Net interest income	64%	65%	65%	65%	65%
Net fee income	20%	20%	20%	20%	20%
Others	16%	15%	15%	15%	15%
Total	100%	100%	100%	100%	100%
Growth, YoY					
Net interest income	4.8%	10.1%	7.4%	5.3%	8.9%
Net fee income	1.7%	5.8%	7.1%	7.0%	7.0%
Operating income	12.0%	7.3%	7.2%	6.0%	8.4%
PPoP	13.5%	8.0%	6.2%	4.7%	7.8%
Net profit	4.9%	5.0%	1.9%	3.6%	6.0%
Gross loans	6.0%	9.3%	8.5%	8.5%	8.5%
Customer deposits	4.5%	4.8%	8.0%	7.5%	7.5%
Efficiency					
Cost-to-income ratio	35.6%	35.3%	35.8%	36.6%	36.9%

Balance Sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Due from central banks	825,506	745,704	787,682	846,758	910,265
Interbank assets	848,067	648,488	687,397	728,641	772,360
Investments	2,821,909	3,005,843	3,214,819	3,396,207	3,587,904
Gross loans	4,854,228	5,304,275	5,755,138	6,244,325	6,775,093
Less: provision	125,540	134,052	147,675	164,081	183,183
Other assets	307,001	335,342	360,358	358,159	356,174
Total assets	9,531,171	9,905,600	10,657,719	11,410,009	12,218,612
Due to central banks	520,138	462,933	486,080	510,384	535,903
Interbank liabilities	2,008,908	1,940,140	2,081,703	2,209,137	2,345,813
Customer deposits	5,793,324	6,072,908	6,558,741	7,050,646	7,579,445
Debt securities issued	317,688	403,918	444,310	488,741	537,615
Other liabilities	185,805	224,789	233,312	242,262	251,659
Total liabilities	8,825,863	9,104,688	9,804,146	10,501,170	11,250,434
Shareholders' equity	698,405	793,247	845,909	901,174	960,514
Incl. Perpetual bonds	-	39,994	39,994	39,994	39,994
Incl. Preferred stocks	59,876	59,876	59,876	59,876	59,876
Minority interest	6,903	7,665	7,665	7,665	7,665
Total equity	705,308	800,912	853,574	908,839	968,179

Asset quality					
NPL ratio	1.49%	1.47%	1.54%	1.49%	1.45%
Provision coverage	173%	172%	166%	176%	187%
Provision/ total loans	2.59%	2.53%	2.57%	2.63%	2.70%
Credit costs	0.90%	0.97%	1.02%	1.00%	1.02%
Capital adequacy					
CET-1 CAR	11.2%	11.2%	11.8%	11.8%	11.9%
Tier-1 CAR	12.2%	12.8%	13.4%	13.3%	13.2%
Total CAR	14.4%	14.8%	13.6%	13.5%	13.4%
Profitability					
NIM	1.51%	1.58%	1.53%	1.50%	1.52%
ROE	11.4%	11.2%	10.6%	10.2%	10.1%
ROA	0.76%	0.77%	0.74%	0.71%	0.71%
RoRWA	0.00%	0.00%	0.00%	0.00%	0.00%
Per share					
EPS (RMB)	0.96	1.00	1.02	1.06	1.13
DPS (RMB)	0.30	0.32	0.32	0.33	0.35
BVPS (RMB)	8.60	9.34	10.05	10.79	11.59

Source: Company data, CMBIS estimates

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