

# China Construction Bank (939 HK)

## Quality growth despite some margin pressure

On 28 Aug, CCB reported 1H19 net profit of RMB 154.2bn, up 4.9% YoY and accounting for 57.0%/58.4% of CMBIS/consensus full-year estimates. 1H19 PPOp had a decent growth of 6.7% YoY. Net interest income rose moderately by 4.6% YoY as margin narrowed, yet non-interest income (incl. fees, trading gains, and investment return) picked up 12.8% YoY. Thanks to slower expansion in opex and impairment charges, bottom-line earnings grew faster at 5.5% YoY in 2Q19 (vs 4.2% YoY in 1Q19). 1H19 annualized ROE declined 1ppt YoY to 15.9%, still the highest of the Big-4 banks.

- **Results positive:** 1) **1H19 net fee income was up 11.1% YoY**, driven by bank card, wealth management, and electronic banking services. As a result, CCB's non-interest income as of total revenue increased 1.5ppt YoY to 27.2%; 2) **Asset quality continued to improve**, as NPL ratio fell 3bp QoQ to 1.43% and provision coverage climbed 3.8ppt to 218%. However, we note that overdue loans rebounded 18.2% HoH, and we would seek for management's explanation during results briefing. 3) **Credit growth was prudent**. The Bank maintained a stable growth in mortgage (+5.3% HoH) while reduced personal consumption loan (-17.1% HoH). Lending to utility and construction segments, and discounted bills accounted for near 50% of new corporate loans. 4) **Capital position remained strongest in the sector**, as CET 1/total CAR only slid 13bp/8bp QoQ to 13.7%/17.1% due to appropriation of cash dividend in 2Q19.
- **Results negative:** 1) **2Q19 NIM contracted 4bp QoQ to 2.25%**, as liability cost went up faster than asset yield. Given higher proportion of deposit funding, CCB may not benefit as much as most joint-stock peers during monetary loosening, but we believe the weaker margin trend was within expectation. 2) **Proportion of demand deposit fell 0.5% HoH to 53.1%**, leading to rising deposit cost thereby smaller net interest spread. 3) **Asset growth slowed** to 0.8% in 2Q19 from 4.2% in 1Q19, as interbank assets pulled back 17% QoQ.
- **Maintain BUY and lower TP to HK\$8.5.** We expect a positive share price reaction to CCB's 1H19 results. The Bank currently trades at 0.62x FY19E P/B, 10% below its past 5-year mean of 0.69x. We trim our TP to HK\$8.5 from HK\$9.3, given a lower sustainable ROE forecast of 13.0%, higher COE assumption of 14.0%, and adjusted HK\$/RMB exchange rate of 0.897.

### Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Operating income (RMB mn)	594,031	633,772	680,537	724,856	771,203
Net profit (RMB mn)	242,264	254,655	270,345	289,440	311,389
EPS (RMB)	0.96	1.00	1.07	1.14	1.23
EPS CHG (%)	4.7	3.9	6.3	7.2	7.7
P/E (x)	5.4	5.2	4.9	4.6	4.2
P/B (x)	0.77	0.69	0.62	0.57	0.52
Dividend yield (%)	5.6	5.9	6.2	6.7	7.2
ROE (%)	14.8	13.9	13.4	13.1	12.8
NPL ratio (%)	1.49	1.46	1.49	1.53	1.51
Provision coverage (%)	171	208	232	251	275

Source: Company data, CMBIS estimates

## BUY (Maintain)

Target Price	HK\$ 8.50
(Previous TP	HK\$ 9.30)
Up/Downside	+46.6%
Current Price	HK\$ 5.80

### China Banking Sector

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### Stock Data

Mkt Cap (RMB mn)	1,467,442
Avg 3 mths t/o (RMB mn)	2,063.27
52w High/Low (RMB)	7.21/5.55
Total Issued Shares (mn)	240,417 (H)
	9,594 (A)

Source: Bloomberg

### Shareholding Structure

Central Huijin	57.31%
CSFC	0.88%

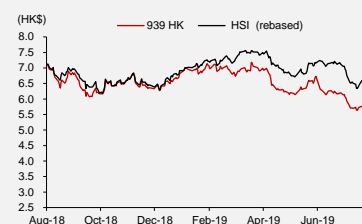
Source: Company data

### Share Performance

	Absolute	Relative
1-mth	-6.8%	3.2%
3-mth	-6.9%	-1.0%
6-mth	-18.2%	-8.4%

Source: Bloomberg

### 12-mth Price Performance



Source: Bloomberg

### Auditor: PwC

### Related Reports

1. Softer earnings but stronger risk resistance – 28 Mar 2019
2. Steady improvement in all aspects – 24 Oct 2018
3. Decent earnings growth with resilient asset quality – 29 Aug 2018

**Figure 1: 1H19 results summary**

(RMB mn)						
P&L	1H18	1H19	YoY	2Q18	2Q19	YoY
Net interest income	239,486	250,436	4.6%	119,746	125,361	4.7%
Net fee and commission income	69,004	76,695	11.1%	31,073	33,666	8.3%
Operating income	322,422	343,974	6.7%	157,504	165,149	4.9%
Operating expense	(74,060)	(78,284)	5.7%	(37,827)	(38,892)	2.8%
PPoP	248,362	265,690	7.0%	119,677	126,257	5.5%
Impairment losses	(67,029)	(74,638)	11.4%	(28,789)	(31,043)	7.8%
Pre-tax profit	181,333	191,052	5.4%	90,888	95,214	4.8%
Income tax	(33,955)	(35,472)	4.5%	(17,538)	(17,556)	0.1%
Net profit	147,027	154,190	4.9%	73,212	77,274	5.5%

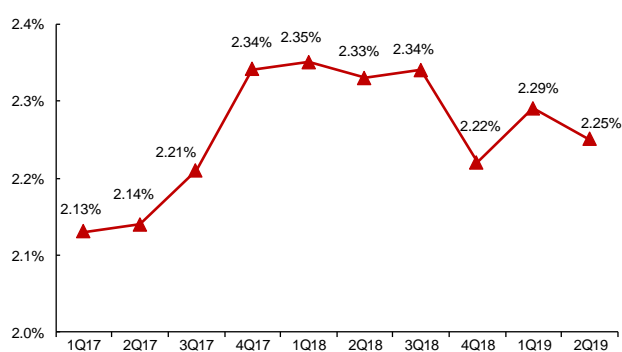
  

B/S	4Q18	2Q19	HoH	1Q19	2Q19	QoQ
Gross loans	13,783,053	14,539,839	5.5%	14,227,115	14,539,839	2.2%
Customers' deposits	17,108,678	18,214,072	6.5%	18,053,818	18,214,072	0.9%
Total assets	23,222,693	24,383,151	5.0%	24,190,914	24,383,151	0.8%
NPLs	200,881	208,069	3.6%	207,463	208,069	0.3%

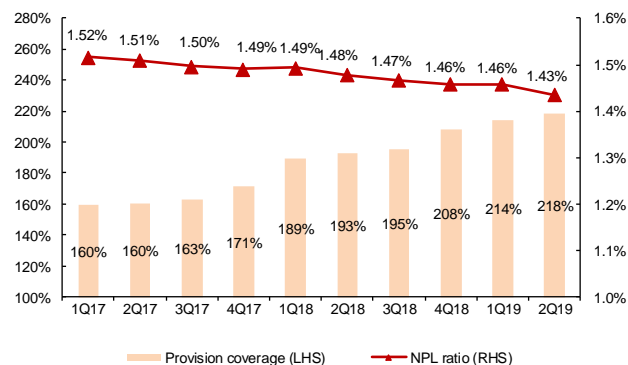
  

Key ratios	1H18	1H19	YoY	1Q19	2Q19	QoQ
NIM	2.34%	2.27%	-7bp	2.29%	2.25%	-4bp
ROE	17.0%	15.9%	-1.0ppt	15.9%	15.7%	-0.2ppt
NPL ratio	1.48%	1.43%	-4bp	1.46%	1.43%	-2bp
Provision coverage	193.2%	218.0%	24.9ppt	214.2%	218.0%	3.8ppt
LDR	79.3%	79.8%	0.5ppt	78.8%	79.8%	1.0ppt
CET-1 CAR	13.1%	13.7%	62bp	13.8%	13.7%	-13bp

Source: Company data, CMBIS

**Figure 2: Quarterly NIM of CCB**

Source: Company data, CMBIS

**Figure 3: NPL ratio and provision coverage of CCB**

Source: Company data, CMBIS

## Financial Summary

### Income Statement

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Interest income	750,154	811,026	878,878	944,691	1,015,181
Interest expenses	(297,698)	(324,748)	(349,390)	(377,862)	(409,331)
Net interest income	452,456	486,278	529,487	566,829	605,850
Net fee income	117,798	123,035	129,187	135,646	142,428
Others	23,777	24,459	21,862	22,381	22,925
<b>Operating income</b>	<b>594,031</b>	<b>633,772</b>	<b>680,537</b>	<b>724,856</b>	<b>771,203</b>
Operating expenses	(167,043)	(174,764)	(186,068)	(197,185)	(208,839)
<b>PPoP</b>	<b>426,988</b>	<b>459,008</b>	<b>494,468</b>	<b>527,671</b>	<b>562,363</b>
Provision	(127,362)	(150,988)	(167,534)	(177,717)	(185,949)
Operating profit	299,626	308,020	326,935	349,954	376,414
Non-operating income	161	140	140	140	140
Pre-tax profit	299,787	308,160	327,075	350,094	376,554
Income tax expenses	(56,172)	(52,534)	(55,759)	(59,683)	(64,194)
Minority interests	(1,351)	(971)	(971)	(971)	(971)
<b>Net profit</b>	<b>242,264</b>	<b>254,655</b>	<b>270,345</b>	<b>289,440</b>	<b>311,389</b>

### Key Ratio

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
<b>Op. income mix</b>					
Net interest income	76%	77%	78%	78%	79%
Net fee income	20%	19%	19%	19%	18%
Others	4%	4%	3%	3%	3%
Total	100%	100%	100%	100%	100%
<b>Growth, YoY</b>					
Net interest income	8.3%	7.5%	8.9%	7.1%	6.9%
Net fee income	-0.6%	4.4%	5.0%	5.0%	5.0%
Operating income	6.1%	6.7%	7.4%	6.5%	6.4%
PPoP	10.0%	7.5%	7.7%	6.7%	6.6%
Net profit	4.7%	5.1%	6.2%	7.1%	7.6%
Gross loans	9.8%	6.8%	8.0%	8.0%	8.0%
Customer deposits	6.2%	4.6%	7.0%	7.0%	7.0%
<b>Efficiency</b>					
Cost-to-income ratio	27.1%	26.6%	26.4%	26.2%	26.1%

### Balance Sheet

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Due from central banks	2,914,380	2,567,648	2,742,905	2,931,681	3,133,673
Interbank assets	708,598	1,038,521	1,080,355	1,124,280	1,170,402
Investments	5,181,648	5,714,909	6,114,953	6,532,514	6,978,831
<b>Gross loans</b>	<b>12,903,441</b>	<b>13,783,053</b>	<b>14,885,697</b>	<b>16,076,553</b>	<b>17,362,677</b>
Less: provision	328,968	417,623	515,097	617,272	721,770
Other assets	745,284	536,185	696,413	849,932	1,027,150
<b>Total assets</b>	<b>22,124,383</b>	<b>23,222,693</b>	<b>25,005,225</b>	<b>26,897,688</b>	<b>28,950,964</b>
Due to central banks	547,287	554,392	609,831	670,814	737,896
Interbank liabilities	2,116,279	2,250,045	2,435,326	2,648,449	2,895,453
<b>Customer deposits</b>	<b>16,363,754</b>	<b>17,108,678</b>	<b>18,306,285</b>	<b>19,587,725</b>	<b>20,958,866</b>
Debt securities issued	275,160	404,202	442,475	492,129	549,231
Other liabilities	1,026,076	913,782	989,593	1,072,237	1,162,348
<b>Total liabilities</b>	<b>20,328,556</b>	<b>21,231,099</b>	<b>22,783,509</b>	<b>24,471,355</b>	<b>26,303,794</b>
<b>Shareholders' equity</b>	<b>1,779,760</b>	<b>1,976,463</b>	<b>2,206,585</b>	<b>2,411,202</b>	<b>2,632,039</b>
Incl. Perpetual bonds	-	-	40,000	40,000	40,000
Incl. Preferred stocks	79,636	79,636	79,636	79,636	79,636
Minority interest	16,067	15,131	15,131	15,131	15,131
<b>Total equity</b>	<b>1,795,827</b>	<b>1,991,594</b>	<b>2,221,716</b>	<b>2,426,333</b>	<b>2,647,170</b>

<b>Asset quality</b>					
NPL ratio	1.49%	1.46%	1.49%	1.53%	1.51%
Provision coverage	171%	208%	232%	251%	275%
Provision/ total loans	2.55%	3.03%	3.46%	3.84%	4.16%
Credit costs	1.00%	1.07%	1.11%	1.09%	1.06%
<b>Capital adequacy</b>					
CET-1 CAR	13.1%	13.8%	14.3%	14.6%	14.9%
Tier-1 CAR	13.7%	14.4%	14.9%	15.1%	15.3%
Total CAR	15.5%	17.2%	16.6%	16.7%	16.9%
<b>Profitability</b>					
NIM	2.21%	2.31%	2.28%	2.27%	2.26%
ROE	14.8%	13.9%	13.4%	13.1%	12.8%
ROA	1.12%	1.11%	1.11%	1.10%	1.10%
RoRWA	1.94%	1.89%	1.89%	1.89%	1.89%
<b>Per share</b>					
EPS (RMB)	0.96	1.00	1.07	1.14	1.23
DPS (RMB)	0.29	0.31	0.32	0.35	0.37
BVPS (RMB)	6.80	7.59	8.35	9.17	10.05

Source: Company data, CMBIS estimates

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