

Bank of Communications (601328 CH)

Stable earnings growth setting pace for large banks

On 27 Aug, BoCom reported 1H19 net profit of RMB 42.7bn, up 4.9% YoY and accounting for 55.3%/57.3% of CMBIS/consensus full-year estimates. In 2Q19, PPOp rose moderately by 4.3% YoY (vs 15.7% YoY in 1Q19), as growth in both net interest income and net fee income softened. The high base effect also led to a YoY decline in trading gains. However, bottom-line earnings growth was largely stable at 4.8% YoY (vs 4.9% YoY in 1Q19), thanks to tax savings from rising investment in tax-free government bond. 1H19 annualized ROE slid 0.2ppt YoY to 12.8%.

■ **Results positives:** 1) **Healthy loan growth of 5.7% HoH** outpaced total asset growth of 3.7% HoH. 1H19 new loans was mainly from corporate segment (+8.0% HoH), as retail loans (+1.1% HoH) were held back by falling credit card overdrafts (-10.0% HoH). Outstanding discounted bills surged 41.7% HoH, suggesting the Bank's falling risk appetite. 2) **Deposit growth picked up to 5.9% in 1H19** (vs 4.7% in 1H18), sending LDR down slightly to 83.6%. That said, proportion of demand deposit declined 0.7ppt to 41.3%. 3) **Asset quality remained solid**, as NPL ratio was stable at 1.47%, and provision also held steady at 173.5%. NPL recognition was prudent, with >90-day overdue loan/NPL at 116%.

■ **Results negatives:** 1) **2Q19 NIM contracted 3bp QoQ** to 1.56%, by our estimate. Despite lower interbank funding cost (-15bps HoH), deposit cost climbed 10bp HoH due to heightened deposit competition. With relatively large proportion of interbank liability, BoCom would gain more from monetary easing, but marginal benefit should diminish going forward; 2) **Retail loan exposure declined 1.5ppt to 32.2%**. BoCom's below-peers retail loan proportion could make it more vulnerable to interest rate liberalization, although the Bank said during results briefing that the pricing of 70% new loans YTD was already based on LPR. 3) **1H19 CIR was 1.4ppt higher at 36.2%**, as opex rose 16.8% YoY. Management explained investment in technology development accounted for over 5% of total opex, and will increase to 10% in coming years.

■ **Initiate BoCom-A with HOLD rating and RMB 6.2 TP.** BoCom-A currently trades at 0.59x FY19E P/B, 12% below its past 5-year mean of 0.67x. Our TP of RMB 6.2 is based on GGM-derived target P/B of 0.67x and FY19E BPS of RMB 9.3.

Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Operating income (RMB mn)	183,800	205,932	214,763	229,469	245,157
Net profit (RMB mn)	70,223	73,630	77,360	81,389	86,146
EPS (RMB)	0.91	0.96	1.01	1.06	1.13
EPS CHG (%)	1.8	5.2	5.4	5.4	6.0
P/E (x)	6.0	5.7	5.4	5.1	4.8
P/B (x)	0.66	0.64	0.59	0.54	0.50
Dividend yield (%)	5.2	5.4	5.7	6.0	6.4
ROE (%)	11.4	11.4	11.3	11.0	10.8
NPL ratio (%)	1.50	1.49	1.52	1.55	1.58
Provision coverage (%)	155	173	178	181	183

Source: Company data, CMBIS estimates

HOLD (Initiation)

Target Price	RMB 6.20
Up/Downside	+13.6%
Current Price	RMB 5.46

China Banking Sector

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Stock Data

Mkt Cap (RMB mn)	380,011
Avg 3 mths t/o (RMB mn)	440.85
52w High/Low (RMB)	6.85/5.4
Total Issued Shares (mn)	39,251 (A)
	35,012 (H)

Source: Bloomberg

Shareholding Structure

Ministry of Finance	26.53%
HSBC	18.70%
NCSSF	3.42%

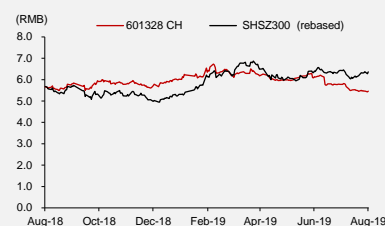
Source: Company data

Share Performance

	Absolute	Relative
1-mth	-6.1%	-3.7%
3-mth	-9.3%	-13.5%
6-mth	-14.5%	-16.3%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: PwC

Related Reports

1. Faster-than-peers NIM expansion – 29 Oct 2018
2. Key beneficiary on policy support for LG bond – 24 Aug 2018

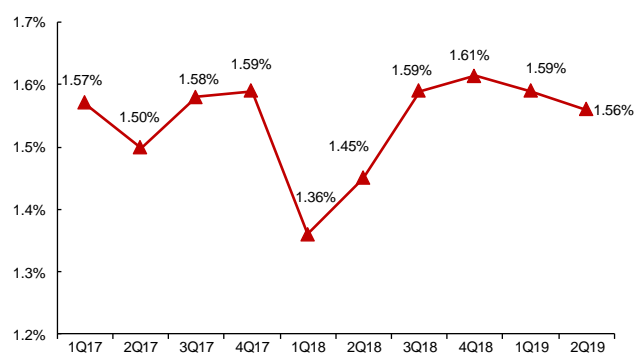
Figure 1: 1H19 results summary

(RMB mn)						
P&L	1H18	1H19	YoY	2Q18	2Q19	YoY
Net interest income	60,658	70,062	15.5%	31,446	35,205	12.0%
Net fee and commission income	21,182	23,122	9.2%	10,338	11,066	7.0%
Operating income	98,170	110,144	12.2%	51,802	54,651	5.5%
Operating expense	(34,174)	(39,927)	16.8%	(18,199)	(19,611)	7.8%
PPoP	63,996	70,217	9.7%	33,603	35,040	4.3%
Impairment losses	(16,666)	(21,550)	29.3%	(9,593)	(10,845)	13.1%
Pre-tax profit	47,330	48,667	2.8%	24,010	24,195	0.8%
Income tax	(6,476)	(5,811)	-10.3%	(3,323)	(2,636)	-20.7%
Net profit	40,771	42,749	4.9%	20,680	21,678	4.8%

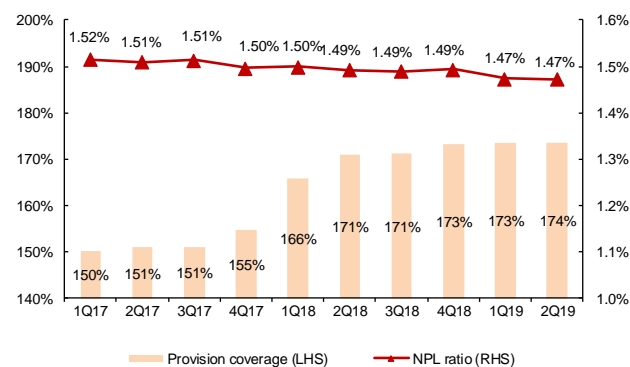
B/S	4Q18	2Q19	HoH	1Q19	2Q19	QoQ
Gross loans	4,854,228	5,130,612	5.7%	5,068,189	5,130,612	1.2%
Customers' deposits	5,793,324	6,135,448	5.9%	6,106,174	6,135,448	0.5%
Total assets	9,531,171	9,886,608	3.7%	9,785,747	9,886,608	1.0%
NPLs	72,512	75,508	4.1%	74,662	75,508	1.1%

Key ratios	1H18	1H19	YoY	1Q19	2Q19	QoQ
NIM	1.41%	1.58%	17bp	1.59%	1.56%	-3bp
ROE	13.4%	13.2%	-0.2ppt	13.0%	13.2%	0.2ppt
NPL ratio	1.49%	1.47%	-2bp	1.47%	1.47%	0bp
Provision coverage	171.0%	173.5%	2.6ppt	173.5%	173.5%	0.1ppt
LDR	83.6%	83.6%	0.0ppt	83.0%	83.6%	0.6ppt
CET-1 CAR	10.6%	10.9%	23bp	11.2%	10.9%	-34bp

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

Valuation

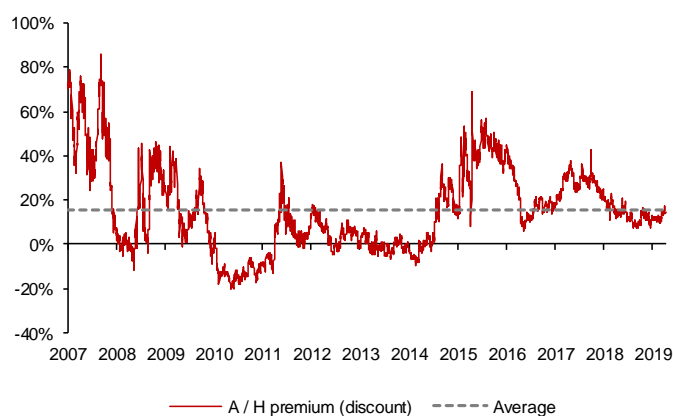
We use Gordon Growth Model to derive the TP for BoCom-A. Our key assumptions include: 1) Cost of equity of 13.8%, 2) Sustainable ROE of 10.2%; 3) Long-term growth rate of 3.0%. Our TP of RMB 6.2 is based on a target P/B of 0.67x and FY19E BVPS of RMB 9.3.

Figure 4: Peers valuation for A-share China banks

		Mkt. Cap	Avg 3M	Price	P/B (x)		P/E (x)		Dvd yield (%)		ROE (%)	
Company	Ticker	(US\$ mn)	(US\$ mn)	(RMB)	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Nationwide SOE & joint-stock banks												
ICBC	601398 CH	257.8	123.3	5.42	0.78	0.71	6.2	5.9	4.9	5.1	12.9	12.4
CCB	601939 CH	186.4	71.8	6.95	0.83	0.75	6.5	6.2	4.6	4.8	13.2	12.7
ABC	601288 CH	163.5	109.2	3.41	0.68	0.62	5.6	5.3	5.4	5.7	12.4	12.0
BOC	601988 CH	136.4	43.5	3.57	0.64	0.59	5.8	5.5	5.3	5.5	11.4	11.0
CMB	600036 CH	120.9	213.7	34.75	1.52	1.34	9.8	8.7	3.1	3.5	16.3	16.3
CITIC	601998 CH	33.9	15.3	5.55	0.62	0.57	5.9	5.6	4.4	4.7	10.6	10.4
MSB	600016 CH	34.2	50.1	5.82	0.57	0.52	4.9	4.6	5.2	5.6	12.0	11.6
CEB	601818 CH	25.5	37.5	3.67	0.61	0.56	5.5	5.1	4.9	5.3	11.3	11.3
PAB	000001 CH	34.3	171.5	14.31	0.99	0.89	9.0	7.9	1.1	1.3	11.6	11.8
SPDB	600000 CH	46.3	51.5	11.30	0.67	0.60	5.7	5.3	3.3	3.5	12.4	12.0
IND	601166 CH	53.0	172.8	18.27	0.77	0.69	5.8	5.4	4.1	4.6	13.6	13.4
HXB	600015 CH	15.6	14.1	7.25	0.51	0.46	5.2	4.9	3.1	3.4	10.0	9.3
Average					0.75	0.68	6.3	5.8	4.2	4.5	12.2	11.9
Regional city & rural commercial banks												
Bank of Beijing	601169 CH	15.4	30.6	5.22	0.58	0.53	5.3	4.8	5.2	5.9	11.2	11.2
Bank of Shanghai	601229 CH	17.7	32.6	8.95	0.80	0.72	6.4	5.2	4.6	5.3	12.4	12.8
Bank of Nanjing	601009 CH	9.2	46.9	7.77	0.85	0.74	5.3	4.6	5.1	5.9	16.3	16.4
Bank of Ningbo	002142 CH	18.0	56.3	23.11	1.57	1.34	9.2	7.8	2.0	2.4	17.1	17.6
Bank of Jiangsu	600919 CH	10.7	20.3	6.67	0.65	0.59	5.4	4.8	5.1	4.9	15.0	15.1
Bank of Guiyang	601997 CH	3.7	14.1	8.34	0.75	0.66	3.6	3.3	3.2	3.4	17.6	16.7
Bank of Hangzhou	600926 CH	5.8	16.0	8.05	0.79	0.71	7.0	5.9	3.6	4.2	10.9	11.4
Bank of Chengdu	601838 CH	4.1	15.1	8.18	0.83	0.73	5.3	4.5	5.0	5.8	16.5	17.1
JYRCB	002807 CH	1.3	3.9	4.42	0.83	0.78	10.0	9.2	2.1	2.3	7.9	8.0
WXRCB	600908 CH	1.4	4.2	5.28	0.85	0.78	8.1	7.2	2.5	2.7	11.2	11.4
CSRCB	601128 CH	3.0	18.4	7.88	1.29	1.14	10.7	9.1	2.9	3.5	13.2	13.6
WJRCB	603323 CH	1.3	9.0	5.15	0.77	0.72	9.0	8.2	2.9	3.3	8.9	8.9
ZJGRCB	002839 CH	1.4	8.6	5.46	0.96	0.89	10.7	9.4	-	-	9.3	-
Average					0.89	0.80	7.4	6.5	3.7	4.1	12.9	13.4

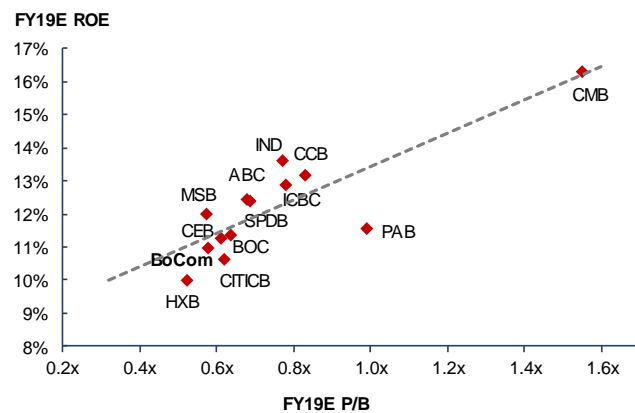
Source: Bloomberg, CMBIS estimates

Figure 5: BoCom's A/H valuation premium (discount)



Source: Bloomberg, CMBIS

Figure 6: P/B vs ROE for A-share China banks



Source: Bloomberg, CMBIS

Financial Summary

Income Statement

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Interest income	314,200	348,864	387,088	416,656	448,555
Interest expenses	(189,327)	(217,956)	(237,790)	(255,887)	(275,494)
Net interest income	124,873	130,908	149,299	160,769	173,060
Net fee income	40,551	41,237	42,976	45,124	47,381
Others	18,376	33,787	22,489	23,576	24,716
Operating income	183,800	205,932	214,763	229,469	245,157
Operating expenses	(69,258)	(75,898)	(83,366)	(90,623)	(98,523)
PPoP	114,542	130,034	131,397	138,846	146,635
Provision	(31,469)	(43,514)	(40,549)	(43,321)	(45,590)
Operating profit	83,073	86,520	90,849	95,525	101,044
Non-operating income	192	(453)	(453)	(453)	(453)
Pre-tax profit	83,265	86,067	90,396	95,072	100,591
Income tax expenses	(12,574)	(11,902)	(12,501)	(13,147)	(13,911)
Minority interests	(468)	(535)	(535)	(535)	(535)
Net profit	70,223	73,630	77,360	81,389	86,146

Key Ratio

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Op. income mix					
Net interest income	68%	64%	70%	70%	71%
Net fee income	22%	20%	20%	20%	19%
Others	10%	16%	10%	10%	10%
Total	100%	100%	100%	100%	100%
Growth, YoY					
Net interest income	-7.4%	4.8%	14.0%	7.7%	7.6%
Net fee income	10.2%	1.7%	4.2%	5.0%	5.0%
Operating income	-0.6%	12.0%	4.3%	6.8%	6.8%
PPoP	-1.4%	13.5%	1.0%	5.7%	5.6%
Net profit	4.5%	4.9%	5.1%	5.2%	5.8%
Gross loans	11.6%	6.0%	8.5%	8.0%	8.0%
Customer deposits	17.3%	4.5%	7.0%	7.0%	7.0%
Efficiency					
Cost-to-income ratio	36.3%	35.6%	37.5%	38.1%	38.8%

Balance Sheet

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Due from central banks	921,948	825,506	872,487	933,561	998,910
Interbank assets	782,468	848,067	775,225	808,004	842,422
Investments	2,528,276	2,821,909	3,104,100	3,337,742	3,589,342
Gross loans	4,579,256	4,854,228	5,266,837	5,688,184	6,143,239
Less: provision	106,001	125,540	142,240	159,768	177,515
Other assets	332,307	307,001	394,003	408,179	428,193
Total assets	9,038,254	9,531,171	10,270,412	11,015,902	11,824,591
Due to central banks	532,867	520,138	572,152	629,367	692,304
Interbank liabilities	1,723,807	2,008,908	2,154,199	2,297,210	2,453,698
Customer deposits	5,545,366	5,793,324	6,198,857	6,632,777	7,097,071
Debt securities issued	287,662	317,688	354,625	403,258	461,618
Other liabilities	272,281	185,805	192,505	199,539	206,926
Total liabilities	8,361,983	8,825,863	9,472,338	10,162,152	10,911,616
Shareholders' equity	671,143	698,405	791,171	846,847	906,071
Incl. Perpetual bonds	-	-	40,000	40,000	40,000
Incl. Preferred stocks	59,876	59,876	59,876	59,876	59,876
Minority interest	5,128	6,903	6,903	6,903	6,903
Total equity	676,271	705,308	798,074	853,750	912,974

Asset quality					
NPL ratio	1.50%	1.49%	1.52%	1.55%	1.58%
Provision coverage	155%	173%	178%	181%	183%
Provision/ total loans	2.31%	2.59%	2.70%	2.81%	2.89%
Credit costs	0.69%	0.90%	0.78%	0.77%	0.75%
Capital adequacy					
CET-1 CAR	10.8%	11.2%	11.3%	11.4%	11.5%
Tier-1 CAR	11.9%	12.2%	13.0%	12.9%	12.9%
Total CAR	14.0%	14.4%	15.0%	14.8%	14.7%
Profitability					
NIM	1.51%	1.51%	1.54%	1.54%	1.54%
ROE	11.4%	11.4%	11.3%	11.0%	10.8%
ROA	0.77%	0.76%	0.76%	0.74%	0.73%
RoRWA	1.25%	0.00%	0.00%	0.00%	0.00%
Per share					
EPS (RMB)	0.91	0.96	1.01	1.06	1.13
DPS (RMB)	0.29	0.30	0.31	0.33	0.35
BVPS (RMB)	8.23	8.60	9.31	10.06	10.86

Source: Company data, CMBIS estimates

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