

Agricultural Bank of China (601288 CH)

Solid asset quality overshadowed by NIM contraction

On 30 Aug, ABC reported 1H19 net profit of RMB 121.4bn, up 4.9% YoY and accounting for 56.3%/57.8% of CMBIS/consensus full-year estimates. 2Q19 PPOp was largely flat YoY, as net interest income growth was subdued (+1.9% YoY) on narrowing NIM. Thanks to lower opex (-10.2% YoY) and provision charges (-4.7% YoY), bottom-line earnings growth picked up to 5.5% YoY in 2Q19 (vs 4.3% YoY in 1Q19). **We initiate coverage on ABC A-share with BUY rating.**

- Results positives:** 1) 1H19 net fee income was up 16.6% YoY, mainly driven by strong fees from consultancy and advisory, bank card, and e-banking services. ABC's non-interest income as of total revenue increased to 22.4% from 18.3% in FY18; 2) 1H19 CIR declined 0.8ppt YoY to 28.4% on lower general operating and administrative expenses; 3) Loan growth topped Big-4 peers at 8.8% HoH, with balanced expansion in retail (+9.1% HoH) and corporate (+8.6% HoH) segments. Higher-yield credit card loan saw a rapid growth of 19.4% HoH, and default rate remained well controlled so far. 4) Asset quality continued to improve, as NPL ratio fell 9bp QoQ to 1.43%, and provision coverage climbed 14.4ppt to 278.4%. Overdue and special mention loans saw double-decline as well. Credit cost retreated 48bp QoQ to 0.90% and is likely to stay low in 2H19, so as to cushion weaker revenue momentum.
- Results negatives:** 1) 2Q19 NIM contracted 10bp QoQ to 2.11%, based on our estimate. Asset yield only rose 2bp HoH, yet deposit cost surged 17bp HoH. As an interbank net lender, ABC's NIM was also squeezed by falling market rates. 2) Deposits growth was muted in 2Q19 at 0.4% QoQ, while the proportion of demand deposit slid 0.6ppt to 57.0%. 3) 1H19 annualized ROE declined 1.3ppt to 14.7%, given the uninspiring earnings growth of 4.9% YoY.
- Initiate ABC-A with BUY rating and RMB 4.9 TP.** ABC-A currently trades at 0.68x FY19E P/B, 9% below its past 5-year mean of 0.75x. Our TP of RMB 4.9 is based on GGM-derived target P/B of 0.99x and FY19E BPS of RMB 4.97.

Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Operating income (RMB mn)	520,346	584,905	632,705	680,006	736,373
Net profit (RMB mn)	192,962	202,783	215,784	231,377	249,205
EPS (RMB)	0.58	0.59	0.60	0.65	0.70
EPS CHG (%)	5.0	1.3	2.7	7.4	7.9
P/E (x)	5.9	5.8	5.6	5.2	4.9
P/B (x)	0.82	0.75	0.68	0.63	0.57
Dividend yield (%)	5.2	5.1	5.4	5.8	6.3
ROE (%)	14.6	13.5	12.7	12.4	12.3
NPL ratio (%)	1.81	1.59	1.60	1.60	1.61
Provision coverage (%)	208	252	268	281	293

Source: Company data, CMBIS estimates

BUY (Initiation)

Target Price	RMB 4.90
Up/Downside	+44.1%
Current Price	RMB 3.40

China Banking Sector

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

Karen Sui
 (852) 3761 8775
 suixiaomeng@cmbi.com.hk

Stock Data

Mkt Cap (RMB mn)	1,170,068
Avg 3 mths t/o (RMB mn)	840.80
52w High/Low (RMB)	3.94/3.38
Total Issued Shares (mn)	319,244 (A)
	30,739 (H)

Source: Bloomberg

Shareholding Structure

Huijin	40.03%
MoF	39.21%
NCSSF	2.80%

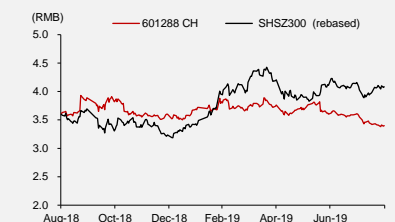
Source: Company data

Share Performance

	Absolute	Relative
1-mth	-5.8%	-4.2%
3-mth	-7.9%	-10.9%
6-mth	-10.8%	-13.6%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: PwC

Related Reports

- Moderate earnings pace with continued NIM pressure – 29 Apr 2019
- Funding Strength Is Playing Out – 29 Aug 2018

Figure 1: 1H19 results summary

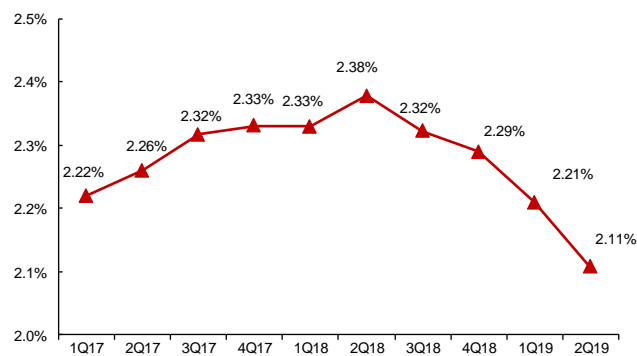
(RMB mn)						
P&L	1H18	1H19	YoY	2Q18	2Q19	YoY
Net interest income	233,833	237,632	1.6%	116,352	118,519	1.9%
Net fee and commission income	43,637	50,899	16.6%	20,251	21,681	7.1%
Operating income	294,006	306,408	4.2%	136,768	132,802	-2.9%
Operating expense	(86,017)	(87,094)	1.3%	(34,094)	(30,602)	-10.2%
PPoP	207,989	219,314	5.4%	102,674	102,200	-0.5%
Impairment losses	(66,443)	(73,427)	10.5%	(32,471)	(30,932)	-4.7%
Pre-tax profit	141,546	145,887	3.1%	70,203	71,268	1.5%
Income tax	(25,576)	(23,490)	-8.2%	(13,270)	(10,947)	-17.5%
Net profit	115,789	121,445	4.9%	57,053	60,194	5.5%

B/S	4Q18	2Q19	HoH	1Q19	2Q19	QoQ
Gross loans	11,913,625	12,962,302	8.8%	12,664,116	12,962,302	2.4%
Customers' deposits	17,346,290	18,529,174	6.8%	18,447,181	18,529,174	0.4%
Total assets	22,609,471	23,975,153	6.0%	23,657,926	23,975,153	1.3%
NPLs	190,002	185,312	-2.5%	192,705	185,312	-3.8%

Key ratios	1H18	1H19	YoY	1Q19	2Q19	QoQ
NIM	2.35%	2.16%	-19bp	2.21%	2.11%	-10bp
ROE	16.0%	14.7%	-1.3ppt	15.1%	14.6%	-0.5ppt
NPL ratio	1.62%	1.43%	-19bp	1.52%	1.43%	-9bp
Provision coverage	248.4%	278.4%	30.0ppt	263.9%	278.4%	14.4ppt
LDR	67.7%	70.0%	2.3ppt	68.7%	70.0%	1.3ppt
CET-1 CAR	11.2%	11.1%	-5bp	11.4%	11.1%	-26bp

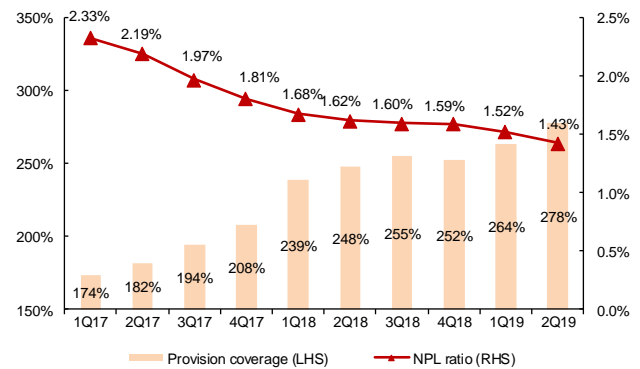
Source: Company data, CMBIS

Figure 2: Quarterly NIM of ABC



Source: Company data, CMBIS

Figure 3: NPL ratio and provision coverage of ABC



Source: Company data, CMBIS

Valuation

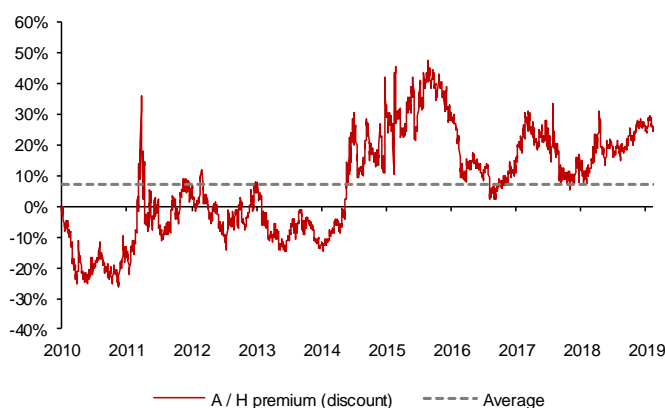
We use Gordon Growth Model to derive the TP for ABC-A. Our key assumptions include: 1) Cost of equity of 12.5%, 2) Sustainable ROE of 12.3%; 3) Long-term growth rate of 3.0%. Our TP of RMB 4.9 is based on a target P/B of 0.99x and FY19E BVPS of RMB 4.97.

Figure 4: Peers valuation for A-share China banks

Company	Ticker	Mkt. Cap (US\$ mn)	Avg 3M (US\$ mn)	Price (RMB)	P/B (x)		P/E (x)		Dvd yield (%)		ROE (%)		
					FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	
Nationwide SOE & joint-stock banks													
ICBC	601398 CH	258.0	122.2	5.39	0.77	0.71	6.2	5.9	4.9	5.2	12.9	12.4	
CCB	601939 CH	187.7	71.6	6.90	0.82	0.75	6.5	6.2	4.7	4.9	13.2	12.7	
BOC	601988 CH	135.9	42.3	3.53	0.63	0.59	5.7	5.4	5.4	5.6	11.4	11.0	
BoCom	601328 CH	52.6	55.2	5.41	0.57	0.53	5.3	5.1	5.7	6.0	11.0	10.6	
CMB	600036 CH	119.8	216.5	34.28	1.49	1.32	9.6	8.6	3.1	3.5	16.3	16.3	
CITIC	601998 CH	34.4	15.0	5.59	0.62	0.57	5.9	5.7	4.3	4.6	10.7	10.4	
MSB	600016 CH	34.3	48.9	5.81	0.57	0.52	4.9	4.6	5.4	5.6	12.0	11.6	
CEB	601818 CH	26.2	37.7	3.76	0.62	0.58	5.6	5.2	4.8	5.2	11.3	11.2	
PAB	000001 CH	34.0	172.1	14.16	0.98	0.88	8.9	7.8	1.1	1.3	11.6	11.8	
SPDB	600000 CH	46.3	51.0	11.28	0.67	0.60	5.6	5.2	3.3	3.5	12.4	12.0	
IND	601166 CH	49.9	178.6	17.17	0.72	0.65	5.5	5.1	4.3	4.8	13.6	13.3	
HXB	600015 CH	15.6	13.6	7.24	0.51	0.45	5.2	4.9	3.1	3.4	10.0	9.3	
Average					0.74	0.67	6.2	5.8	4.3	4.5	12.2	11.9	
Regional city & rural commercial banks													
Bank of Beijing	601169 CH	15.5	30.5	5.25	0.58	0.54	5.3	4.8	5.2	5.9	11.0	10.9	
Bank of Shanghai	601229 CH	17.9	32.2	9.02	0.76	0.67	6.2	5.2	4.8	5.5	12.8	13.3	
Bank of Nanjing	601009 CH	9.3	45.1	7.80	0.84	0.74	5.3	4.6	5.1	5.9	16.0	16.1	
Bank of Ningbo	002142 CH	17.8	56.0	22.84	1.55	1.33	9.1	7.7	2.1	2.4	17.1	17.5	
Bank of Jiangsu	600919 CH	10.8	19.5	6.68	0.65	0.59	5.4	4.8	5.1	4.9	15.0	15.1	
Bank of Guiyang	601997 CH	3.7	13.9	8.20	0.75	0.64	3.9	3.5	3.7	4.2	16.3	15.6	
Bank of Hangzhou	600926 CH	5.7	15.7	7.98	0.78	0.71	6.9	5.8	3.6	4.2	10.8	11.3	
Bank of Chengdu	601838 CH	4.1	14.9	8.19	0.84	0.73	5.3	4.5	5.0	5.8	16.5	17.1	
JYRCB	002807 CH	1.3	3.9	4.30	0.81	0.76	9.8	9.0	2.2	2.3	7.9	8.0	
WXRCB	600908 CH	1.3	4.1	5.21	0.84	0.77	8.0	7.1	2.5	2.7	11.2	11.4	
CSRCB	601128 CH	2.8	18.8	7.37	1.20	1.07	10.3	8.7	2.8	3.3	12.8	13.1	
WJRCB	603323 CH	1.3	8.8	5.10	0.82	0.77	9.4	8.3	2.9	3.3	8.9	8.9	
ZJGRCB	002839 CH	1.3	8.4	5.32	0.94	0.87	10.4	9.2	-	-	9.3	-	
Average					0.87	0.78	7.3	6.4	3.8	4.2	12.7	13.2	

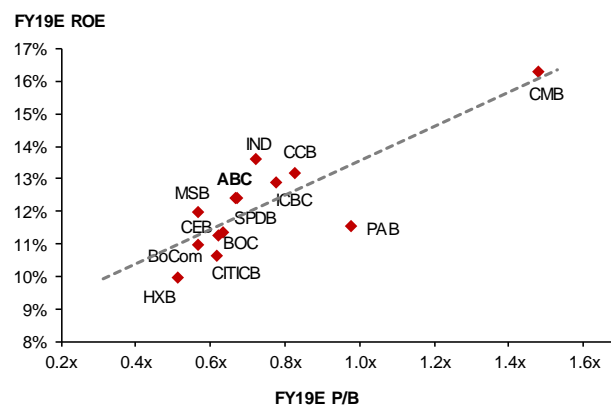
Source: Bloomberg, CMBIS

Figure 5: ABC'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	713,699	784,724	875,612	943,304	1,022,169
Interest expenses	(271,769)	(306,964)	(337,672)	(363,116)	(390,950)
Net interest income	441,930	477,760	537,940	580,188	631,220
Net fee income	72,903	78,141	82,048	86,150	90,458
Others	5,513	29,004	12,717	13,667	14,695
Operating income	520,346	584,905	632,705	680,006	736,373
Operating expenses	(182,716)	(196,311)	(214,144)	(232,043)	(252,709)
PPoP	337,630	388,594	418,561	447,963	483,664
Provision	(98,166)	(136,898)	(150,718)	(160,752)	(174,310)
Operating profit	239,464	251,696	267,843	287,211	309,354
Non-operating income	14	(22)	(22)	(22)	(22)
Pre-tax profit	239,478	251,674	267,821	287,189	309,332
Income tax expenses	(46,345)	(49,043)	(52,190)	(55,964)	(60,279)
Minority interests	(171)	152	152	152	152
Net profit	192,962	202,783	215,784	231,377	249,205

Key Ratio

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Op. income mix					
Net interest income	85%	82%	85%	85%	86%
Net fee income	14%	13%	13%	13%	12%
Others	1%	5%	2%	2%	2%
Total	100%	100%	100%	100%	100%
Growth, YoY					
Net interest income	11.0%	8.1%	12.6%	7.9%	8.8%
Net fee income	-19.8%	7.2%	5.0%	5.0%	5.0%
Operating income	4.3%	12.4%	8.2%	7.5%	8.3%
PPoP	7.8%	15.1%	7.7%	7.0%	8.0%
Net profit	4.9%	5.1%	6.4%	7.2%	7.7%
Gross loans	10.3%	11.1%	9.5%	9.5%	9.5%
Customer deposits	7.7%	7.1%	8.0%	8.0%	8.0%
Efficiency					
Cost-to-income ratio	34.2%	32.7%	32.8%	33.1%	33.3%

Balance Sheet

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Due from central banks	2,788,122	2,705,858	2,908,712	3,127,794	3,364,402
Interbank assets	1,175,900	1,032,742	1,084,379	1,138,598	1,195,528
Investments	6,152,743	6,885,075	7,390,844	7,889,431	8,401,895
Gross loans	10,720,611	11,913,625	13,045,419	14,284,734	15,641,784
Less: provision	404,300	479,143	560,260	644,983	736,259
Other assets	620,306	551,314	546,663	628,681	640,793
Total assets	21,053,382	22,609,471	24,415,757	26,424,254	28,508,143
Due to central banks	465,947	561,195	589,255	618,717	649,653
Interbank liabilities	1,779,849	2,085,831	2,249,707	2,427,650	2,620,883
Customer deposits	16,194,279	17,346,290	18,733,993	20,232,713	21,851,330
Debt securities issued	269,748	301,806	282,880	282,880	282,880
Other liabilities	914,162	639,562	694,814	755,172	821,114
Total liabilities	19,623,985	20,934,684	22,550,649	24,317,133	26,225,860
Shareholders' equity	1,426,415	1,670,294	1,860,616	2,102,629	2,277,790
Incl. Perpetual bonds	-	-	40,000	120,000	120,000
Incl. Preferred stocks	79,899	79,899	79,899	79,899	79,899
Minority interest	2,982	4,493	4,493	4,493	4,493
Total equity	1,429,397	1,674,787	1,865,109	2,107,122	2,282,283

Asset quality					
NPL ratio	1.81%	1.59%	1.60%	1.60%	1.61%
Provision coverage	208%	252%	268%	281%	293%
Provision/ total loans	3.77%	4.02%	4.29%	4.52%	4.71%
Credit costs	0.91%	1.15%	1.15%	1.12%	1.11%
Capital adequacy					
CET-1 CAR	10.6%	11.6%	11.9%	12.0%	12.1%
Tier-1 CAR	11.3%	12.1%	12.4%	12.5%	12.6%
Total CAR	13.7%	15.1%	14.9%	15.1%	15.3%
Profitability					
NIM	2.28%	2.33%	2.29%	2.28%	2.29%
ROE	14.6%	13.5%	12.7%	12.4%	12.3%
ROA	0.93%	0.91%	0.90%	0.89%	0.89%
RoRWA	1.54%	1.51%	1.48%	1.47%	1.47%
Per share					
EPS (RMB)	0.58	0.59	0.60	0.65	0.70
DPS (RMB)	0.18	0.17	0.19	0.20	0.21
BVPS (RMB)	4.15	4.54	4.97	5.44	5.94

Source: Company data, CMBIS estimates

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CMB International Securities Limited

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

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