

ABC (1288 HK / 601288 CH)

Holding the key to sustainable earnings growth

- NIM pressure resulted in soft earnings growth in 2019; mild NIM pressure to persist in 2020
- ABC's robust risk buffers reduce provision pressure; such strength differentiates it favorably from peers amid an economic downturn
- Net fee income growth rebounded, thanks to strategic retail transformation and Fintech
- Maintain **BUY** on sustainable earnings growth. Our GGM-based H/A shr TPs imply target 20E P/B of 0.82x/0.93x

NIM squeezed by deposit cost marketization. ABC reported its 2019 net profit at RMB212,098mn, up 4.59% YoY. NIM was down by 16bps YoY to 2.17% in 2019, mainly driven by the 20bps YoY increase in deposit cost to 1.59% as a result of pricing marketization. NIM remained largely stable 2H19, inching up by 2bps HoH; meanwhile, the bank was able to maintain an average loan yield at 4.4% in 2019, same as 2018. However, increasing asset yield pressure can be expected starting from 4Q19 due to the global rate cut cycle. In 2019, loan-deposit spread and interbank asset-liability narrowed by 20bps and 40bps YoY; we forecast the ABC's interbank asset-liability spread to remain stable in 2020E-21E; loan-deposit spread would shrink by 14bps/15bps in 2020E/21E. NIM would contract by 16bps/10bps in 2020E/21E, in line with the industry trend.

Robust risk buffer defends earnings growth. ABC's risk buffer indicators are one of the highest in the sector, which exemption from large provision helped offset some of the negative impacts of narrowing NIM on earnings in 2019. The bank's provision expenses in 2019 grew only by 1.3% YoY - we believe this would help ABC outperform peers in a challenging economy. Provisioning ratio and provision coverage stayed high at 4.06% and 288.75% as of Dec 2019 while NPL ratio was marked at 1.4%. NPL ratio may see a temporary surge in mid-2020 due to the COVID-19 impact; while our base case scenario factor in a mild increase by 6bps YoY in 2020E and 5bps YoY in 2021E for the bank. With NPL ratio reaching 1.51% by end-21E, we estimate ABC's provision expenses to increase by 3.9%/2.1% YoY in 2020E/21E, sustaining a provisioning ratio and a provision coverage ratio at 4.14% and 274.17% by end-21E.

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Results and Valuation

FY ended Dec 31	2017A	2018A	2019A	2020E	2021E
Revenue (RMB mn)	542,898	602,557	629,350	666,797	705,481
Chg (% YoY)	6.4	11.0	4.4	6.0	5.8
Net profit* (RMB mn)	192,962	202,783	212,098	222,826	234,429
Chg (% YoY)	4.9	5.1	4.6	5.1	5.2
EPS (RMB)	0.58	0.59	0.59	0.61	0.64
Chg (% YoY)	5.0	1.3	0.9	2.7	5.4
BVPS (RMB)	4.15	4.54	5.00	5.44	5.90
Chg (% YoY)	8.7	9.6	9.9	8.8	8.5
P/E (x) - H-shr	4.92	4.86	4.81	4.69	4.45
P/B (x) - H-shr	0.69	0.63	0.57	0.52	0.48
P/E (x) - A-shr	5.81	5.74	5.68	5.54	5.25
P/B (x) - A-shr	0.81	0.74	0.67	0.62	0.57
ROAE (%)	14.57	13.66	12.43	11.70	11.44
ROAA (%)	0.95	0.93	0.90	0.86	0.83
DPS(RMB)	0.18	0.17	0.18	0.19	0.20
Yield (%) H-shr	6.25	6.09	6.37	6.69	7.04
Yield (%) A-shr	5.29	5.16	5.40	5.67	5.96

Note: Company; HKD/CNY=1.0898

*Net profit = Net profit attributable to shareholders of the Company

Source(s): Bloomberg, ABCI Securities estimates

Company Report

Rating (H): BUY
Rating (A): BUY
TP (H): HK\$ 4.88
TP (A): RMB 5.08

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Price (H/A shr) HK\$ 3.11/
RMB 3.37
Est. s price return (H/A shr) 56.9%/50.7%
Est. dividend yield (H/A shr) 6.69%/5.67%
Est. total return (H/A shr) 63.59%/
56.37%

Last Rating & TP (H/A shr) BUY, HK\$5.41/
BUY, RMB5.52

Previous Report Date 12 Mar, 2020

Source(s): Bloomberg, ABCI Securities estimates

Key Data

52Wk H/L (HK\$) (H shr) 3.77/2.69
52Wk H/L (RMB) (A shr) 3.92/3.27
Total issued shares (mn) 349,983.0
Issued H shr (mn) 30,738.8
Issued A shr (mn) 319,244.2
Market cap (HK\$ mn) 1,271,501.9
H-shr market cap (HK\$ mn) 95,597.7
A-shr market cap (HK\$ mn) 1,175,904.2
3-mth avg daily turnover (HK\$ mn) (H shr) 537.67
3-mth avg daily turnover (RMB mn) (A shr) 673.98
Major shareholder(s) (%):
Central Huijin 40.03
MoF 35.29

Source(s): Bloomberg, ABCI Securities

Net fee income momentum resumed. Thanks to ABC's strategic retail transformation and investment in Fintech, net fee income rebounded by 11.2% YoY in 2019. This was mainly driven by 18.0% and 28.4% YoY growth in its bank card fees and e-banking fees in 2019. We believe these fees would continue be the core drivers, propelling a net fee income CAGR at 8.8% over 2019A-21E.

Prefer ABC for sustainable earnings growth. ABC's earnings growth would continue in 2020E-21E based on its high risk buffer and robust balance sheet growth. We adjust our model assuming lower NII and provision expenses in 2020E/21E; net profit growth would sustain at 5.1%/5.2% YoY in 2020E/21E. ABC's H/A shr are currently trading at 0.52x/0.62x 20E P/B. Our GGM-based H/A shr TPs imply target 20E P/B of 0.82x/0.93x. Maintain **BUY**.

Risk Factors: 1) Radical change in business environment induced by heavy-handed supervision and policies; 2) Increasing competition from non-bank financial institutions; 3) Sharp deterioration in asset quality in specific regions; 4) Sharp decline in loan demand; 5) Policy risk in new and fast-growing businesses; 6) Prolonged COVID-19 epidemic.

Exhibit 1: ABC's 2019 actual results vs. ABCI estimates

(RMB mn)	2019E	2019A	AvE (%)
Net interest income	531,616	486,871	(8.42)
Net fee and commission	83,311	86,926	4.34
Operating income	659,993	629,350	(4.64)
Operating expenses	(213,957)	(224,096)	4.74
Impairment losses	(153,988)	(138,605)	(9.99)
Profit before tax	274,486	266,576	(2.88)
Income tax expenses	(52,152)	(53,652)	2.88
Net profit	222,524	212,098	(4.69)
Key indicators (%)			AvE (ppt)
Net interest margin	2.34	2.17	(0.17)
Net interest spread	2.23	2.03	(0.20)
Cost to income ratio	32.42	30.49	(1.93)
Return on average assets	0.94	0.90	(0.04)
Return on average equity	12.74	12.43	(0.31)
Dividend payout	30.00	30.68	0.68
CT1 CAR	11.93	11.24	(0.69)
Total CAR	15.47	16.13	0.66
NPL ratio	1.50	1.40	(0.10)
Provision to total loans	4.10	4.06	(0.04)
Provision coverage	273.33	288.75	15.42

Source(s): Company, ABCI Securities estimates

Exhibit 2: Changes in 2020E and 2021E forecasts

(RMB mn)	2020E (old)	2020E (new)	change (%)	(RMB mn)	2021E (old)	2021E (new)	change (%)
Net interest income	583,994	508,183	(12.98)	Net interest income	640,513	530,912	(17.11)
Net fee and commission	89,390	95,123	6.41	Net fee and commission	94,541	102,945	8.89
Operating income	717,049	666,797	(7.01)	Operating income	777,493	705,481	(9.26)
Operating expenses	(229,642)	(221,767)	(3.43)	Operating expenses	(244,992)	(240,195)	(1.96)
Impairment losses	(171,288)	(144,167)	(15.83)	Impairment losses	(186,518)	(147,203)	(21.08)
Profit before tax	297,328	279,720	(5.92)	Profit before tax	326,064	294,402	(9.71)
Income tax expenses	(56,492)	(55,944)	(0.97)	Income tax expenses	(61,952)	(58,880)	(4.96)
Net profit attributable to equity holders	241,073	222,826	(7.57)	Net profit attributable to equity holders	264,409	234,429	(11.34)
Key indicators (%)			change (ppt)	Key indicators (%)			change (ppt)
Net interest margin	2.36	2.01	(0.35)	Net interest margin	2.39	1.91	(0.48)
Net interest spread	2.24	1.86	(0.38)	Net interest spread	2.25	1.74	(0.51)
CIR	32.03	33.26	1.23	CIR	31.51	34.05	2.54
ROAA	0.94	0.86	(0.08)	ROAA	0.95	0.83	(0.12)
ROAE	12.65	11.70	(0.95)	ROAE	12.72	11.44	(1.28)
Dividend payout	30.00	30.00	-	Dividend payout	30.00	30.00	-
CT1 CAR	11.96	11.25	(0.71)	CT1 CAR	12.08	11.16	(0.92)
Total CAR	15.49	16.09	0.60	Total CAR	15.63	15.94	0.31
NPL ratio	1.55	1.46	(0.09)	NPL ratio	1.61	1.51	(0.10)
Provision to total loans	4.17	4.10	(0.07)	Provision to total loans	4.25	4.14	(0.11)
Provision coverage ratio	269.03	280.82	11.79	Provision coverage ratio	263.98	274.17	10.19

Source(s): Company, ABCI Securities estimates



Exhibit 3: Changes of GGM assumptions

	H-shr		A-shr		Reason
	old	new	old	new	
TP (HKD/RMB)	5.41	4.88	5.52	5.08	Roll over to mid-2021 BVPS
Sustainable ROE (%)	12.56	11.20	12.56	11.20	Revise down earnings on NIM pressure
COE (%)	13.30	12.94	12.50	11.96	
Target 20E P/B (x)	0.87	0.82	1.01	0.93	
Rfr (%)	3.30	2.65	3.30	2.65	Referencing China 10Y government bond
Beta	1.25	1.05	1.15	0.95	Referencing Bloomberg data
ERP (%)	8.00	9.80	8.00	9.80	Factor in higher risk as a result of COVID-19 and decelerating economic growth in China
LT gr (%)	7.70	4.70	7.70	4.70	Normalizing growth rate with other big banks

Source(s): Company, ABCI Securities estimates

Financial statements

ABC (1288HK/601288CH) Consolidated income statement (2017A-2021E)

FY Ended Dec 31 (RMB mn)	2017A	2018A	2019A	2020E	2021E
Net interest income	441,930	477,760	486,871	508,183	530,912
Non-interest income	100,968	124,797	142,479	158,615	174,568
Of which: Fees and commissions	72,903	78,141	86,926	95,123	102,945
Operating income	542,898	602,557	629,350	666,797	705,481
Operating expenses	(186,975)	(197,572)	(205,340)	(221,767)	(240,195)
Amortization	(18,279)	(16,413)	(18,711)	(21,143)	(23,681)
Pre-provision operating profit	337,644	388,572	405,299	423,887	441,605
Impairment loans losses	(98,166)	(136,898)	(138,723)	(144,167)	(147,203)
Profit before tax	239,478	251,674	266,576	279,720	294,402
Tax	(46,345)	(49,043)	(53,652)	(55,944)	(58,880)
Minority interests	(171)	152	(826)	(950)	(1,092)
Net profit attributable to equity holders	192,962	202,783	212,098	222,826	234,429
Preference share dividend	4,600	4,600	4,600	9,753	9,753
Net profit attributable to ordinary shareholders	188,362	198,183	207,498	213,073	224,676
Growth (%)					
Net interest income	11.0	8.1	1.9	4.4	4.5
Non-interest income	(9.9)	23.6	14.2	11.3	10.1
Of which: Fees and commissions	(19.8)	7.2	11.2	9.4	8.2
Operating income	6.4	11.0	4.4	6.0	5.8
Operating expenses	5.0	5.7	3.9	8.0	8.3
Amortization	(4.0)	(10.2)	14.0	13.0	12.0
Pre-provision operating profit	7.8	15.1	4.3	4.6	4.2
Impairment loans losses	13.6	39.5	1.3	3.9	2.1
Profit before tax	5.7	5.1	5.9	4.9	5.2
Tax	8.9	5.8	9.4	4.3	5.2
Minority interests	43.7	(188.9)	(643.4)	15.0	15.0
Net profit attributable to equity holders	4.9	5.1	4.6	5.1	5.2
Preference share dividend	0.0	0.0	0.0	112.0	0.0
Net profit attributable to ordinary shareholders	5.0	5.2	4.7	2.7	5.4
Per share (RMB)					
EPS	0.58	0.59	0.59	0.61	0.64
BVPS	4.15	4.54	5.00	5.44	5.90
DPS	0.18	0.17	0.18	0.19	0.20
Key ratio (%)					
Net interest margin	2.28	2.33	2.17	2.01	1.91
Net interest spread	2.15	2.20	2.03	1.86	1.74
Cost to income ratio	32.96	32.79	32.63	33.26	34.05
Return on average assets	0.95	0.93	0.90	0.86	0.83
Return on average equity	14.57	13.66	12.43	11.70	11.44
Effective tax rate	19.35	19.49	20.13	20.00	20.00
Dividend payout	30.74	30.71	30.68	30.00	30.00

Note1: Individual items may not sum to total due to rounding difference

Note2: Key ratios may not match with financial reports due to adjustment for comparison consistency among individual equities

Source(s): Company, ABCI Securities estimates



ABC (1288HK/601288CH)

Consolidated balance sheet (2017A-2021E)

As of Dec 31 (RMB mn)	2017A	2018A	2019A	2020E	2021E
Cash & equivalent	2,896,619	2,805,107	2,699,895	2,655,515	2,674,075
Interbank assets	1,175,900	1,032,742	1,467,476	1,720,568	1,984,890
Investment securities	6,152,743	6,885,075	7,422,930	7,956,845	8,467,904
Net loans and advances	10,316,311	11,461,542	12,819,610	14,278,456	15,774,006
Total interest earning assets	20,541,573	22,184,466	24,409,911	26,611,384	28,900,875
Property and equipment	155,258	152,452	152,484	154,009	155,549
Other non-interest earning assets	356,551	272,553	315,893	363,348	413,220
Total assets	21,053,382	22,609,471	24,878,288	27,128,741	29,469,645
Customer deposits	16,194,279	17,346,290	18,542,861	19,750,539	20,903,860
Interbank liabilities	1,720,738	2,011,058	2,437,808	2,949,748	3,510,200
Subordinated debt	475,017	780,673	1,108,212	1,440,676	1,815,251
Total interest bearing liabilities	18,390,034	20,138,021	22,088,881	24,140,963	26,229,311
Current taxes	32,842	49,248	59,286	69,957	81,850
Deferred tax liabilities	87	139	520	650	813
Other liabilities	1,201,022	747,276	769,839	801,564	877,760
Total liabilities	19,623,985	20,934,684	22,918,526	25,013,134	27,189,733
Share capital	404,693	429,882	549,869	549,869	549,869
Reserves	1,021,722	1,240,412	1,398,486	1,552,620	1,714,957
Minorities	2,982	4,493	11,407	13,118	15,086
Shareholder's equity	1,429,397	1,674,787	1,959,762	2,115,607	2,279,911
Growth (%)					
Cash & equivalent	3.0	(3.2)	(3.8)	(1.6)	0.7
Interbank assets	(23.0)	(12.2)	42.1	17.2	15.4
Investment securities	15.4	11.9	7.8	7.2	6.4
Net loans and advances	10.7	11.1	11.8	11.4	10.5
Total interest earning assets	8.2	8.0	10.0	9.0	8.6
Property and equipment	(2.1)	(1.8)	0.0	1.0	1.0
Other non-interest earning assets	(15.1)	(23.6)	15.9	15.0	13.7
Total assets	7.6	7.4	10.0	9.0	8.6
Customer deposits	7.7	7.1	6.9	6.5	5.8
Interbank liabilities	(1.6)	16.9	21.2	21.0	19.0
Subordinated debt	22.4	64.3	42.0	30.0	26.0
Total interest bearing liabilities	7.1	9.5	9.7	9.3	8.7
Current taxes	100.8	50.0	20.4	18.0	17.0
Deferred tax liabilities	50.0	59.8	274.1	25.0	25.0
Other liabilities	13.7	(37.8)	3.0	4.1	9.5
Total liabilities	7.5	6.7	9.5	9.1	8.7
Share capital	0.0	6.2	27.9	0.0	0.0
Reserves	11.8	21.4	12.7	11.0	10.5
Minorities	(12.2)	50.7	153.9	15.0	15.0
Shareholder's equity	8.2	17.2	17.0	8.0	7.8
Key ratio (%)					
CT1 CAR	10.63	11.55	11.24	11.25	11.16
Total CAR	13.74	15.12	16.13	16.09	15.94
NPL ratio	1.81	1.59	1.40	1.46	1.51
Provision to total loans	3.77	4.02	4.06	4.10	4.14
Provision coverage ratio	208.37	252.18	288.75	280.82	274.17

Note1: Individual items may not sum to total due to rounding difference

Note2: Key ratios may not match with financial reports due to adjustment for comparison consistency among individual equities

Source(s): Company, ABCI Securities estimates

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Rating	Definition
Buy	Stock return \geq Market return rate (10%)
Hold	- Market return (-10%) \leq Stock return < Market return rate (10%)
Sell	Stock return < - Market return (-10%)

Notes: Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months

Market return rate: average market return rate since 2008 (HSI total return index 2008-19 CAGR at 10%)

Time horizon of share price target: 12-month

Stock rating, however, may vary from the stated framework due to factors including but not limited to: corporate governance, market capitalization, historical price volatility relative to corresponding benchmark index, average daily turnover of the stock relative to market capitalization of the stock, competitive advantages in corresponding industry, etc.

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