



## Bank of Qingdao (BQD, 3866 HK)

### A less-than-sanguine 2017

- BQD's net profit dropped 9.02% YoY in 2017 as a result of lower NIM on structural change in loan mix and issuance of debt securities
- NPL normalized to system average level; risk buffer remains healthy
- CAR position strengthened after preference share issuance; however, if balance sheet growth and high dividend payout persist, growing need to fuel up its CT1 in coming years
- The counter is currently trading at 1.26x 17 P/B

**Lower NIM on modified loan mix.** BQD's 2017 net profit was reported at RMB 1,900mn, down 9.02% YoY. NIM contracted 51bps YoY to 1.72% due to the combined effect of modified loan mix and the surge in interest expenses arising from debt securities issued. Loan mix in residential mortgage rose from 20.96% of total loans in 2016 to 24.61% in 2017; loan mix in corporate banking fell from 71.66% in 2016 to 68.65% in 2017. Consequently, average loan yield fell 46bps YoY to 4.75% in 2017. Moreover, the extra funding of ~RMB1.4tr from debt securities issued in 2017 was largely allocated to investments at a spread of 21bps, hence the lower overall NIM.

**NPL ratio on the rise.** Despite system NPL ratio remained stable at 1.74% in 2017, BQD's NPL ratio climbed 33bps YoY to 1.69%. Loan provision expenses surged 24.35% YoY to maintain a healthy provisioning ratio at 2.6% by Dec 2017. Provision coverage ratio decreased to the level of 153.52%. Manufacturing and wholesale & retail (W&R) sectors remained to be the core NPL components. The former's NPL ratio increased from 2.19% in 2016 to 4.43% in 2017 while W&R improved from 4.24% in 2016 to 3.04% in 2017.

**Strong CAR position; growing need to fuel up CT1.** After the issuance of preference shares in 2017, BQD strengthened its T1 CAR and total CAR to 12.57% and 16.6% as of Dec 2017. However the Group's CT1 was down 1.37ppt YoY to the marginal level of 8.71%. Taking into account of the Group's expanding total assets and total liabilities (up 10.18% and 13.05%) and its persistently high dividend payout ratio (2015-2017: 39.22%-44.23%), we believe there will be a growing need to fuel up its CT1.

**Valuation.** The counter is trading at 1.26x 17 P/B.

**Risk factors:** 1) Asset quality deterioration in Qingdao; 2) Pricing competition from big banks in local regions; 3) Low average daily turnover of shares; 4) Earning dilution in 2018E due to BQD's preference share issuance.

#### Results and Valuation

FY ended Dec 31	2013A	2014A	2015A	2016A	2017A
Revenue (RMB mn)	3,557	4,365	5,006	5,996	5,568
Chg (% YoY)	23.2	22.7	14.7	19.8	(7.1)
Net profit (RMB mn)	1,142	1,495	1,814	2,089	1,900
Chg (% YoY)	24.2	30.9	21.3	15.2	(9.0)
EPS (RMB)	0.45	0.59	0.58	0.51	0.47
Chg (% YoY)	25.0	31.1	(1.7)	(12.1)	(7.8)
BVPS (RMB)	3.21	3.83	4.14	4.35	4.38
Chg (% YoY)	10.3	19.2	8.2	5.0	0.7
P/E (x)	12.22	9.32	9.48	10.78	11.70
P/B (x)	1.71	1.44	1.33	1.26	1.26
ROAE (%)	14.60	16.62	13.74	12.20	10.73
ROAA (%)	0.96	1.02	1.06	0.90	0.65
DPS (RMB)	0.08	0.30	0.20	0.20	0.20
Yield (%)	1.45	5.53	3.64	3.64	3.64

Source(s): Bloomberg, ABCI Securities

## Company Report

Mar 27, 2018

Rating: NR

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Share price (HK\$)	6.81
Previous Rating & TP	NR
Previous Report Date	na

Source(s): Bloomberg, ABCI Securities

#### Key Data

52Wk H/L(HK\$)	7.71/5.40
Issued shares (mn)	4,059
H share	1,763
Domestic share	2,296
Market cap (HK\$ mn)	27,681
H share	12,024
Domestic share	15,657
3-mth avg daily turnover(HK\$ mn)	
Major shareholder(s)	0.27
(%):	
Qingdao Conson	12.64
Haier	10.21

Source(s): Company, ABCI Securities

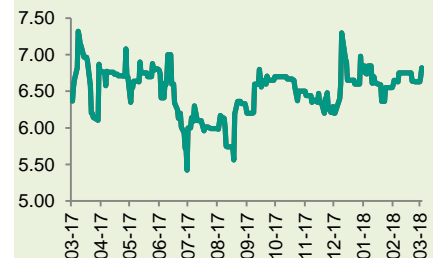
#### Share Performance

	Absolute	Relative*
1-mth	2.71	5.96
3-mth	10.00	7.35
6-mth	10.00	(0.19)

\*Relative to HSI

Source(s): Bloomberg, ABCI Securities

#### 1-Year share performance(HK\$)



Source(s): Bloomberg, ABCI Securities



**Consolidated income statement (2013A-2017A)**

<b>FY Ended Dec 31 (RMB mn)</b>	<b>2013A</b>	<b>2014A</b>	<b>2015A</b>	<b>2016A</b>	<b>2017A</b>
Net interest income	3,088	3,596	4,114	5,008	4,802
Net fee and commission	425	689	750	888	829
Other operating income	43	80	142	100	(64)
<b>Operating income</b>	<b>3,557</b>	<b>4,365</b>	<b>5,006</b>	<b>5,996</b>	<b>5,568</b>
Operating expenses	(1,689)	(1,995)	(2,077)	(2,214)	(1,819)
Impairment losses	(349)	(411)	(580)	(1,109)	(1,379)
<b>Profit before tax</b>	<b>1,519</b>	<b>1,958</b>	<b>2,349</b>	<b>2,674</b>	<b>2,370</b>
Income tax expenses	(377)	(463)	(535)	(585)	(466)
<b>Net profit</b>	<b>1,142</b>	<b>1,495</b>	<b>1,814</b>	<b>2,089</b>	<b>1,900</b>
<b>Growth (%)</b>					
Net interest income	18.5	16.5	14.4	21.7	(4.1)
Net fee and commission	80.6	61.9	8.8	18.5	(6.7)
Other operating income	(2.1)	85.2	77.4	(29.5)	(163.7)
<b>Operating income</b>	<b>23.2</b>	<b>22.7</b>	<b>14.7</b>	<b>19.8</b>	<b>(7.1)</b>
Operating expenses	22.4	18.1	4.1	6.6	(17.8)
Impairment losses	23.0	17.9	41.0	91.2	24.4
<b>Profit before tax</b>	<b>24.2</b>	<b>28.9</b>	<b>20.0</b>	<b>13.8</b>	<b>(11.4)</b>
Income tax expenses	24.3	22.9	15.6	9.3	(20.3)
<b>Net profit</b>	<b>24.2</b>	<b>30.9</b>	<b>21.3</b>	<b>15.2</b>	<b>(9.0)</b>
<b>Per share (Rmb)</b>					
EPS	0.45	0.59	0.58	0.51	0.47
BVPS	3.21	3.83	4.14	4.35	4.38
DPS	0.08	0.30	0.20	0.20	0.20
<b>Key ratio (%)</b>					
Net interest margin	2.54	2.43	2.36	2.23	1.72
Net interest spread	2.38	2.26	2.23	2.05	1.57
Cost to income ratio	41.06	39.61	35.80	34.71	31.68
Return on average assets	0.96	1.02	1.06	0.90	0.65
Return on average equity	14.60	16.62	13.74	12.20	10.73
Effective tax rate	24.80	23.65	22.79	21.88	19.67
Dividend payout	17.86	52.04	44.23	39.22	42.55

Source(s): Company, ABCI Securities



Consolidated balance sheet (2013A-2017A)

As of Dec 31 (RMB mn)	2013A	2014A	2015A	2016A	2017A
Cash and bank	20,871	23,610	19,920	22,698	27,098
Due from bank and FIs	3,181	3,175	4,693	7,041	3,991
Repo	8,208	2,698	2,517	3,957	3,584
Net loans	54,106	61,248	70,655	84,865	95,515
Investment securities	45,637	61,243	84,780	152,928	164,589
<b>Total IEA</b>	<b>132,002</b>	<b>151,974</b>	<b>182,566</b>	<b>271,489</b>	<b>294,777</b>
Other assets	3,687	4,192	4,669	6,499	11,499
<b>Total assets</b>	<b>135,689</b>	<b>156,166</b>	<b>187,235</b>	<b>277,988</b>	<b>306,276</b>
Customer deposits	96,284	101,734	115,322	141,605	160,084
Due to bank and FIs	12,814	21,742	30,388	51,944	30,676
Repo	10,130	10,069	2,000	17,043	11,900
Borrowing from central bank	1,024	1,004	529	3,432	584
Subordinated debt	4,987	8,335	16,314	41,786	68,633
<b>Total IBL</b>	<b>125,239</b>	<b>142,884</b>	<b>164,553</b>	<b>255,810</b>	<b>271,877</b>
Other liabilities	2,246	3,497	6,069	4,542	8,276
<b>Total liabilities</b>	<b>127,484</b>	<b>146,381</b>	<b>170,622</b>	<b>260,352</b>	<b>280,153</b>
<b>Total equity</b>	<b>8,205</b>	<b>9,784</b>	<b>16,614</b>	<b>17,636</b>	<b>26,123</b>
<b>Growth (%)</b>					
Cash and bank	4.0	13.1	(15.6)	13.9	19.4
Due from bank and FIs	(31.6)	(0.2)	47.8	50.0	(43.3)
Repo	40.1	(67.1)	(6.7)	57.2	(9.4)
Net loans	21.6	13.2	15.4	20.1	12.5
Investment securities	92.6	34.2	38.4	80.4	7.6
<b>Total IEA</b>	<b>33.6</b>	<b>15.1</b>	<b>20.1</b>	<b>48.7</b>	<b>8.6</b>
<b>Total assets</b>	<b>33.5</b>	<b>15.1</b>	<b>19.9</b>	<b>48.5</b>	<b>10.2</b>
Customer deposits	27.3	5.7	13.4	22.8	13.0
Due to bank and FIs	81.0	69.7	39.8	70.9	(40.9)
Repo	(1.2)	(0.6)	(80.1)	752.2	(30.2)
Borrowing from central bank	na	(2.0)	(47.3)	549.0	(83.0)
Subordinated debt	na	67.1	95.7	156.1	64.2
<b>Total IBL</b>	<b>34.7</b>	<b>14.1</b>	<b>15.2</b>	<b>55.5</b>	<b>6.3</b>
<b>Total liabilities</b>	<b>35.3</b>	<b>14.8</b>	<b>16.6</b>	<b>52.6</b>	<b>7.6</b>
<b>Total equity</b>	<b>10.3</b>	<b>19.2</b>	<b>69.8</b>	<b>6.2</b>	<b>48.1</b>
<b>Key ratio (%)</b>					
Loan to deposits	56.79	55.54	59.99	58.24	56.42
CT1 CAR	9.75	9.72	12.48	10.08	8.71
Total CAR	10.88	10.75	15.04	12.00	16.60
NPL ratio	0.75	1.14	1.19	1.36	1.69
Provision to total loans	2.74	2.76	2.81	2.64	2.60
Provision coverage	365.47	242.34	236.13	194.01	153.52

Source(s): Company, ABCI Securities

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Rating	Definition
Buy	Stock return $\geq$ Market return rate
Hold	Market return $- 6\% \leq$ Stock return $<$ Market return rate
Sell	Stock return $<$ Market return $- 6\%$

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate

Time horizon of share price target: 12-month

### Definition of share price risk

Rating	Definition
Very high	$2.6 \leq$ 180 day volatility/180 day benchmark index volatility
High	$1.5 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 2.6
Medium	$1.0 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 1.5
Low	180 day volatility/180 day benchmark index volatility $<$ 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index. Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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