

Huishang Bank (3698 HK)

Sound balance sheet management; maintain BUY

- HB's 2016 earnings slightly exceeded consensus and were broadly in line with our forecasts. Robust growth was seen in both topline and balance sheet
- Increased allocation to high-yield asset class (such as investments) and reduction in high-cost interbank liabilities were results of proactive balance sheet management
- Sharp decline in payout ratio and uncertain dividend pattern cast uncertainties
- The counter is currently trading at 0.74x 17E P/B. Maintain **BUY** on solid fundamentals

Earnings slightly exceeded consensus. Huishang Bank (HB) reported its 2016 net profit at RMB 6,870mn, up 11.51% YoY, slightly higher than the Bloomberg consensus and our forecasts by 4.6% and 2.8%. NIM contracted by 12bps YoY to 2.59% while NII surged 23.6% YoY in 2016. Similar to other district banks, the squeeze was partially offset by robust growth in balance sheet. Given the Bank's high reliance on NII, net fee only accounted for 11.91% of topline revenue, up 1.48ppt YoY despite a 40.6% YoY growth in net fee income supported by growth in bank card fees and custodian service fees.

A more sensible balance sheet mix. HB managed its NIM through readjusting its balance sheet mix. On the asset side, the proportion of investments (high-yield asset class) increased significantly from 36.22% of total assets in 2015 to 44.79% in 2016 at the expense of loans and interbank assets. Average yield of investments was 5% (-36bps YoY) in 2016, versus 5.25% (-138bps YoY) for loans and 3.19% (-89bps YoY) for interbank assets. On the liability side, the proportion of customer deposits (low-cost funding source) surged from 60.5% of total liabilities to 65.85% as interbank liabilities fell. Average deposit cost was 1.59% (-45bps YoY), as compared to the cost of interbank liabilities at 3.15% (-63bps YoY).

Slashing payout ratio to sustain capital position. In order to strengthen its CAR position, HB reduced its dividend payout considerably from 28.5% in 2015 to 9.84% in 2016. With CT1 and total CAR reported at 8.79% and 12.99% in 2016, HB is in no immediate need of capital in our view. The shift in payout pattern will create uncertainty for investors.

Maintain BUY on solid fundamentals. The counter is trading at 0.74x 17E P/B. Maintain **BUY** on solid fundamentals. We will revise our forecasts considering the change in dividend policy.

Risk factors: 1) Sharp asset quality deterioration in the region; 2) Pricing competition from big banks in domestic area; 3) Failure to optimize business mix in retail banking; 4) Low average daily turnover of shares.

Results and Valuation

FY ended Dec 31	2014A	2015A	2016A	2017E	2018E
Revenue (RMB mn)	12,748	16,977	20,918	22,765	25,464
Chg (% YoY)	20.7	10.2	23.2	8.8	11.9
Net profit (RMB mn)	5,673	6,161	6,870	7,174	7,649
Chg (% YoY)	23.3	14.4	11.5	4.4	6.6
EPS (RMB)	0.51	0.56	0.62	0.65	0.69
Chg (% YoY)	(12.3)	8.6	11.2	4.7	6.6
BVPS (RMB)	3.29	3.72	4.15	4.67	5.36
Chg (% YoY)	14.8	13.1	11.6	12.5	14.8
P/E (x)	6.69	6.16	5.54	5.29	4.96
P/B (x)	1.04	0.92	0.83	0.74	0.64
ROAE (%)	16.68	15.89	15.63	13.23	12.21
ROAA (%)	1.31	1.10	1.01	0.90	0.83
DPS(RMB)	0.16	0.16	0.06	0.18	0.19
Yield (%)	4.54	4.63	1.78	5.20	5.44

Source(s): Bloomberg, ABCI Securities estimates

Company Report

Mar 27, 2017

Rating: BUY

TP:HK\$4.59

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Share price (HK\$)	3.88
Est. share price return	18.30%
Est. dividend yield	5.20%
Est. total return	23.50%
Previous Rating & TP	BUY;HK\$4.59
Previous Report Date	Oct 24,2016

Source(s): Bloomberg, ABCI Securities

Key Data

52Wk H/L(HK\$)	4.20/3.43
Issued shares (mn)	11,050
H-share(mn)	3,163
Domestic shares (mn)	7,887
Market cap (HK\$ mn)	42,874
H-share(mn)	12,271
Domestic shares (mn)	30,603
3-mth avg daily turnover(HK\$ mn)	9.49
Major shareholder(s) (%):	
China Vanke	8.0

Source(s): Company, ABCI Securities

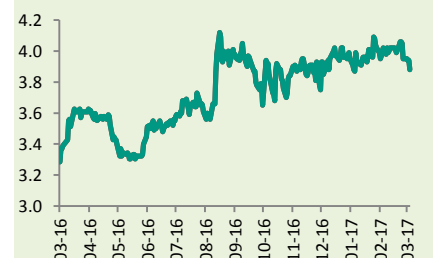
Share Performance (%)

	Absolute	Relative*
1-mth	(2.27)	(2.89)
3-mth	0.78	(10.74)
6-mth	(1.77)	(4.48)

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

1-Year share performance(HK\$)



Source(s): Bloomberg, ABCI Securities

Exhibit 1: HB's 2016 actual results versus ABCI estimates

(Rmb mn)	2016A	2016E	AvE (%)
Net interest income	18,340	17,482	4.90
Net fee and commission	2,491	2,161	15.28
Other operating income	88	381	(76.99)
Operating income	20,918	20,024	4.46
Operating expenses	(5,763)	(6,957)	(17.16)
Impairment losses	(6,487)	(4,601)	41.00
Share of associates	144	101	42.40
Profit before tax	8,813	8,568	2.85
Income tax expenses	(1,816)	(1,885)	(3.64)
Minority interest	(126)	(59)	112.77
Net profit	6,870	6,683	2.81
Key indicators (%)			AvE (ppt)
Net interest margin	2.59	2.63	(0.04)
Net interest spread	2.42	2.46	(0.04)
Net fee to total operating income	11.91	10.79	1.12
Cost to income ratio	27.55	34.74	(7.19)
Return on average assets	1.01	0.97	0.04
Return on average equity	15.63	14.46	1.17
CT1 CAR	8.79	10.23	(1.44)
Total CAR	12.99	13.54	(0.55)
NPL ratio	1.07	1.17	(0.10)
Provision to total loans	2.90	2.63	0.27
Provision coverage	270.77	224.79	45.98

Source(s): Company, ABCI Securities estimates



Consolidated income statement (2014A-2018E)

FY Ended Dec 31 (RMB mn)	2014A	2015A	2016A	2017E	2018E
Net interest income	11,423	14,843	18,340	19,772	21,932
Net fee and commission	856	1,771	2,491	2,593	3,112
Other operating income	469	363	88	400	420
Operating income	12,748	16,977	20,918	22,765	25,464
Operating expenses	(4,216)	(5,435)	(5,763)	(8,766)	(10,870)
Impairment losses	(1,197)	(3,657)	(6,487)	(4,918)	(4,921)
Share of associates	76	88	144	116	134
Profit before tax	7,411	7,973	8,813	9,198	9,807
Income tax expenses	(1,734)	(1,761)	(1,816)	(2,023)	(2,158)
Minority interest	(4)	(51)	(126)	(68)	(68)
Net profit	5,673	6,161	6,870	7,174	7,649
Growth (%)					
Net interest income	20.9	12.1	23.6	7.8	10.9
Net fee and commission	(4.1)	36.3	40.6	4.1	20.0
Other operating income	80.9	(88.6)	(75.8)	356.4	5.0
Operating income	20.7	10.2	23.2	8.8	11.9
Operating expenses	25.3	8.1	6.0	52.1	24.0
Impairment losses	(20.9)	(4.9)	77.4	(24.2)	0.1
Share of associates	10.4	37.0	63.8	(19.2)	15.0
Profit before tax	23.4	12.7	10.5	4.4	6.6
Income tax expenses	23.6	7.2	3.1	11.4	6.6
Net profit	23.3	14.4	11.5	4.4	6.6
Per share (RMB)					
EPS	0.51	0.56	0.62	0.65	0.69
BVPS	3.29	3.72	4.15	4.67	5.36
DPS	0.16	0.16	0.06	0.18	0.19
Key ratio (%)					
Net interest margin	2.74	2.71	2.59	2.59	2.55
Net interest spread	2.47	2.52	2.42	2.45	2.45
Net fee to total operating income	6.72	10.43	11.91	11.39	12.22
Cost to income ratio	33.08	32.02	27.55	38.51	42.69
Return on average assets	1.31	1.10	1.01	0.90	0.83
Return on average equity	16.68	15.89	15.63	13.23	12.21
Effective tax rate	23.40	22.09	20.61	22.00	22.00
Dividend payout	30.39	28.50	9.84	27.50	27.00

Source(s): Company, ABCI Securities estimates



Consolidated balance sheet (2014A-2018E)

As of Dec 31 (RMB mn)	2014A	2015A	2016A	2017E	2018E
Cash and bank	76,421	78,414	88,059	85,628	88,197
Due from bank and FIs	73,786	74,194	30,280	86,539	93,463
Net loans	214,734	237,428	269,336	286,221	311,577
Investment securities	112,358	230,397	338,149	374,501	461,653
Total IEA	477,299	620,433	725,825	832,889	954,890
Other assets	5,465	15,698	28,949	22,228	25,562
Total assets	482,764	636,131	754,774	855,117	980,452
Customer deposits	317,870	359,225	462,014	446,588	491,247
Due to bank and FIs	98,703	142,649	98,573	233,659	292,074
Subordinated debt	18,751	79,426	91,505	100,474	115,545
Total IBL	435,324	581,299	652,093	780,721	898,865
Other liabilities	10,887	12,486	49,498	16,039	14,608
Total liabilities	446,211	593,785	701,591	796,760	913,474
Share capital	11,050	11,050	11,050	11,050	11,050
Retained earnings	10,868	13,121	15,457	23,134	28,719
Reserves	14,456	16,988	24,053	22,465	25,161
MI	179	1,186	1,312	1,708	2,050
Total equity	36,553	42,345	51,871	58,357	66,979
Growth (%)					
Cash and bank	3.3	32.1	12.3	(2.8)	3.0
Due from bank and FIs	180.7	9.2	(59.2)	185.8	8.0
Net loans	19.4	19.6	13.4	6.3	8.9
Investment securities	19.3	5.6	46.8	10.8	23.3
Total IEA	26.0	17.9	17.0	14.8	14.6
Total assets	26.2	17.9	18.7	13.3	14.7
Customer deposits	17.7	13.9	28.6	(3.3)	10.0
Due to bank and FIs	88.5	12.7	(30.9)	137.0	25.0
Subordinated debt	0.0	125.1	15.2	9.8	15.0
Total IBL	26.1	15.2	12.2	19.7	15.1
Total liabilities	26.6	15.4	18.2	13.6	14.6
Total equity	19.9	54.6	22.5	12.5	14.8
Key ratio (%)					
CT1 CAR	11.50	9.80	8.79	10.26	10.25
Total CAR	13.41	13.24	12.99	13.51	13.49
NPL ratio	0.83	0.98	1.07	1.35	1.52
NPL growth	72.54	31.01	23.73	26.85	22.71
Net bad debt charge ratio	0.58	1.58	2.49	1.75	1.60
Provision to total loans	2.13	2.47	2.90	2.76	2.87
Provision coverage	255.27	250.49	270.77	204.44	188.82

Source(s): Company, ABCI Securities estimates



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Definition of equity rating

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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