

Key Data

Average PER (x)	5.2
Average PBV (x)	0.9
Average Dividend Yield (%)	5.7
Sector 3 months avg vol (HK\$m)	4,907

Source: Company, Bloomberg, ABCI Securities

Operating income composition in 1H12 (%)

Net interest income	79.5
Non-interest income	20.5

Source: CBRC

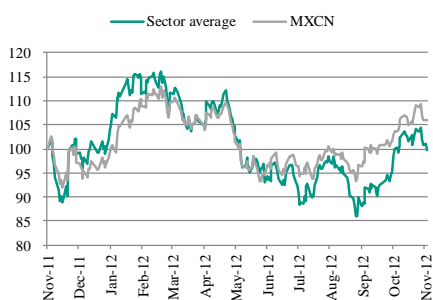
Share performance (%)

	Absolute	Relative*
1-mth	(0.1)	(2.3)
3-mth	2.5	(3.2)
6-mth	(2.9)	(6.9)

Source: Bloomberg

*Relative to MSCI China

1 year price performance



Source: Bloomberg

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China Bank Sector – Neutral Diversified Banks Industry

Loan rate competition kicked off

The PBOC data showed a reduction of average loan rate in 3Q12, with increased use of direct funding through corporate bonds. This is in line with our expectation that the financial reform aims at reducing loan reliance in the economy and previous channel check that banks are turning more aggressive in their loan pricing so far in 4Q12. We think this is a kickoff of loan rate competition. Prefer big banks for better loan growth capacity and pricing power.

Average loan rate is declining. By looking into recent the PBOC loan rate data, we notice a downward trend of loan rate in 3Q12 which combined the impact of expanded rate range and previous rate cuts. Proportion of loan rate below benchmark rate had increased from 7.9% in June to 11.3% in September, at the expense of loan mainly ranged at 1x-1.3x of benchmark rate. In September average total loan rate was 6.97%, down 9bps from June, while discounted bills rate surged 116bps to 6.23% over the same period.

Direct funding is on the rise. Although October new loans came below both market and our expectation at Rmb505bn, the use of direct funding sources became more active. Bank loans to total financing of the economy remained stable at 49.2%, while corporate bonds has been on a substantial rise from 4.5% in January to 23.2% in October. In addition, the use of entrusted loans and trust loans had reduced from 21% in September to 18.5% in October. The diversification of financing channels is in line with the PBOC's policy to diversify risks from banking system and deepen the development of capital markets.

Facts well matched with our view. On the back of a declining loan rate trend, big banks show NIM expansion in 3Q. Given the slower than expected new loan growth in October, big four banks' market share had returned to 40% level, due to lower LDR and stable deposit base. Looking forward into 4Q, we expect NIM to slightly go down for re-pricing and the kickoff of loan rate competition, while loan growth to remain stable to achieve the full year target. We continue to favor big banks.

Risk factors. Prolonged slowdown of China economy, acceleration of interest rate liberalization, sharp deterioration of asset quality and increasing competition from non-bank financial institutions.

Sector Valuation Summary

Companies	Ticker	Rating	Price (HK\$)	Target (HK\$)	Upside (%)	13E PER	13E PBV	13E Yield
CCB	939 HK	Buy	5.66	6.30	11.3	5.8	1.1	5.9
ABC	1288 HK	Buy	3.27	3.45	5.5	5.5	1.0	5.5
MSB	1988 HK	Buy	7.16	7.66	7.0	4.2	0.9	5.9
ICBC	1398 HK	Hold	4.96	4.44	(10.5)	6.1	1.1	4.8
BOC	3988 HK	Hold	3.09	2.94	(4.9)	5.2	0.8	6.2
BoCom	3328 HK	Hold	5.35	5.13	(4.1)	4.8	0.8	6.7
CMB	3968 HK	Hold	13.82	13.47	(2.5)	5.5	1.0	4.5
CNCB	998 HK	Hold	3.85	3.61	(6.2)	4.3	0.6	5.9

Source: Company, Bloomberg, ABCI Securities estimates

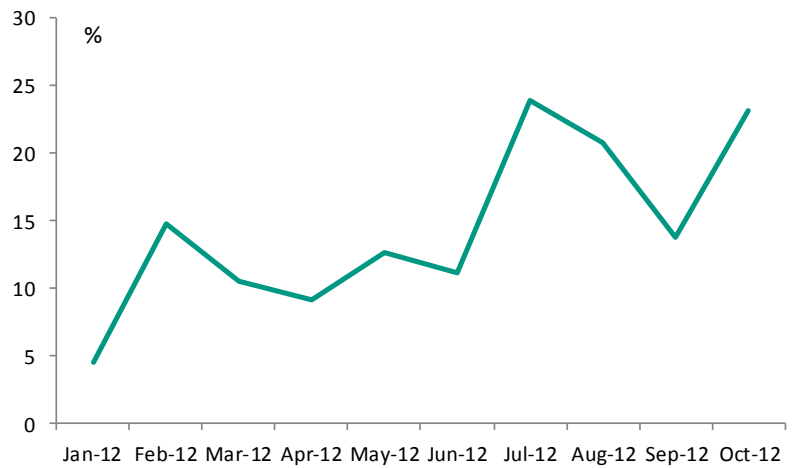


Exhibit 1: Rmb loan rate to benchmark rate

	0.9-1x	1x	1-1.1x	1.1-1.3x	1.3-1.5x	1.5-2x	>2x
Jan-12	4.8	26.2	22.3	25.5	8.8	9.2	3.2
Feb-12	5.5	27.6	23.1	23.8	8.0	8.6	3.4
Mar-12	4.6	25.0	21.1	27.0	9.5	9.4	3.4
Apr-12	5.0	23.1	20.8	28.9	10.1	9.0	3.2
May-12	5.4	24.1	20.5	28.9	9.7	8.3	3.1
Jun-12	7.9	25.1	19.9	27.9	8.9	7.7	2.6
Jul-12	9.5	24.4	19.7	26.8	9.1	7.6	2.9
Aug-12	11.6	22.7	19.6	26.5	8.3	8.3	3.0
Sep-12	11.3	24.6	20.2	25.2	8.1	7.7	3.0

Source: PBOC, ABCI Securities estimates

Exhibit 2: Use of corporate bonds to total financing of the economy



Source: PBOC, 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 from 2007-2011

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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