

China Merchants Bank (3968 HK / 600036 CH)

Outstanding profitability as main forte

- We are raising CMB's net fee income estimates in light of its strengthening momentum
- NIM pressure to persist in near term but easing can be expected in FY21E-23E
- Robust risk buffer continues to shield profitability through manageable provisions
- Excessive property loan exposure to be absorbed naturally, expect mild change in asset mix
- Maintain **BUY** with revised H/A shr TP at HK\$ 76.10/RMB 75.65, implying 2.27x/2.69x FY21E P/B

Strengthening net fee income. Factoring in CMB's 2020 results, we raise our FY21E/22E earnings forecasts by 3.95%/5.11% while extending our forecast to FY23E. Signs of recovery in net fee income was shown in FY20A by the 11.2% YoY increase driven by swift rebound in wealth management products (WMPs) related fees (agency services fees: +35.3% YoY). We raise our 21E/22E net fee income forecasts by 9.79%/14.97%, which reflects a net fee income CAGR of 11.3% in 20A-23E.

Mild NIM pressure to persist. Downside pressure in lending rates will persist in near term but some lessening can be expected in FY21E-23E; meanwhile, increased deposit competition would elevate deposit cost by 4bps-5bps each in FY21E-23E. As such, we forecast CMB's NIM to narrow by 5bps-9bps each in FY21E-23E, reaching 2.28% by FY23E, supporting a FY20A-23E NII CAGR of 10.0%. Our base case scenario assumes topline and net profit to grow at 9.9% and 13.1% CAGR over FY20A-23E; ROAE would be in the range of 15.13%-15.74% over FY21E-23E.

Leading profitability shielded by risk buffers. We believe CMB's solid risk buffer enabled its high ROAE at 15.73% in FY20A. CMB's NPL ratio was down 6bps QoQ at 1.07% in 4Q20; provisioning ratio and provision coverage ratio were 4.67% and 437.68% as of Dec 2020. We expect the improving macro environment and proactive NPL handling would contain NPL ratio at 0.99%-1.03% over FY21E-23E. The bank's provisioning ratio and provision coverage ratio would be in the range of 4.48%-4.6% and 446.6%-459.6% over FY21E-23E. With its robust risk buffer, we revise down our impairment loss estimates by 11.68%/11.14% for FY21E/22E. By sector, CMB's NPL handling effort has been targeting at the manufacturing and mining sectors as well as the micro finance loans. NPL ratios in the three areas dropped from 6.09%, 5.32%, and 0.81% in 2019 to 3.55%, 1.92%, and 0.64% in 2020.

(Continue next page)

Results and Valuation

FY ended Dec 31	2019A	2020A	2021E	2022E	2023E
Revenue (RMB mn)	268,065	287,398	319,015	349,516	381,104
Chg (% YoY)	8.5	7.2	11.0	9.6	9.0
Net profit* (RMB mn)	92,867	97,342	109,352	124,332	140,934
Chg (% YoY)	15.3	4.8	12.3	13.7	13.4
EPS (RMB)	3.62	3.79	4.26	4.84	5.49
Chg (% YoY)	15.7	4.7	12.3	13.7	13.4
BVPS (RMB)	22.89	25.36	28.11	31.26	34.84
Chg (% YoY)	14.1	10.8	10.9	11.2	11.4
P/E (x) – H-shr	14.64	13.98	12.45	10.95	9.66
P/B (x) – H-shr	2.31	2.09	1.88	1.69	1.52
P/E (x) – A-shr	14.86	14.19	12.63	11.11	9.80
P/B (x) – A-shr	2.35	2.12	1.91	1.72	1.54
ROAA (%)	1.31	1.23	1.23	1.25	1.26
ROAE (%)	16.84	15.73	15.13	15.47	15.74
DPS(RMB)	1.20	1.25	1.38	1.58	1.80
Yield (%) H-shr	2.26	2.36	2.61	2.98	3.39
Yield (%) A-shr	2.23	2.33	2.57	2.94	3.34

Note: HKD/CNY=1.1927

*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\$ 76.10

TP (A): RMB 75.65

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Price (H/A shr)	HK\$ 63.20/ RMB 53.78
Est. s price return (H/A shr)	20.41%/40.67%
Est. dividend yield (H/A shr)	2.61%/2.57%
Est. total return (H/A shr)	23.02%/43.24%
Last Rating & TP (H/A shr)	BUY, HK\$57.20/ BUY, RMB57.06
Previous Report Date	7 Jan, 2021

Source(s): Bloomberg, ABCI Securities estimates

Key Data

52Wk H/L (HK\$) (H shr)	69.45/31.15
52Wk H/L (RMB) (A shr)	57.60/29.88
Total issued shares (mn)	25,219.8
Issued H shr (mn)	4,590.9
Issued A shr (mn)	20,628.9
Market cap (HK\$ mn)	1,613,652.1
H-shr market cap (HK\$ mn)	290,145.0
A-shr market cap (HK\$ mn)	1,323,507.1
3-mth avg daily turnover (HK\$ mn) (H shr)	1,108.06
3-mth avg daily turnover (RMB mn) (A shr)	4,350.83

Major shareholder(s) (%):

China Merchants Group	13.04
China Ocean Shipping	6.24

Source(s): Bloomberg, ABCI Securities

Reducing property related loan exposure. As required by PBOC and CBIRC, personal mortgage loans and property-related loans, as a proportion of the total gross loans, should not exceed 20% and 27.5% for medium-sized banks. CMB's related exposures lowered from 26.4% and 37.9% as of June 2020 to 25.3% and 35.2% as of Dec 2020. Given the sufficient grace period, CMB is likely to fulfill the requirements with ease. Assuming total assets would expand at 12.2% CAGR over FY21E-23E, we believe investment assets would grow faster at 17% CAGR. For the same period, we estimate net loans would increase at 11.3% CAGR, mainly attributable to inclusive finance and sectors with policy support.

Maintain BUY on outstanding profitability. We factor in the higher, sustainable ROAE and lower equity risk premium in our GGM model, and roll over our TP calculation to mid-FY22E BVPS. We raise CMB's H/A-share TP by 33.0%/32.6% to HK\$ 76.10/RMB 75.65, which imply 2.27x/2.69x FY21E P/B. CMB's H/A shares are currently trading at 1.88x/1.91x FY21E P/B. Reiterate **BUY** on CMB for its leading profitability- a strong appeal to investors.

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; 5) Policy risk in new and fast-growing businesses; 6) Resurgence of COVID-19.

Exhibit 1: CMB's 2020 actual results vs. ABCI estimates

(RMB mn)	2020E	2020A	AvE (%)
Net interest income	190,270	185,031	(2.75)
Net fee and commission	76,498	79,486	3.91
Operating income	293,067	287,398	(1.93)
Operating expenses	(102,326)	(102,814)	0.48
Impairment losses	(75,971)	(65,025)	(14.41)
Profit before tax	117,010	122,440	4.64
Income tax expenses	(23,402)	(24,481)	4.61
Net profit	92,941	97,342	4.74
Key indicators (%)			AvE (ppt)
Net interest margin	2.45	2.49	0.04
Net interest spread	2.35	2.40	0.05
Cost to income ratio	34.92	35.77	0.85
Return on average assets	1.16	1.23	0.07
Return on average equity	14.43	15.73	1.30
Dividend payout	33.00	33.02	0.02
CT1 CAR	10.87	12.29	1.42
Total CAR	13.48	16.54	3.06
NPL ratio	1.17	1.07	(0.10)
Provision to total loans	5.10	4.67	(0.43)
Provision coverage	435.90	437.68	1.78

Source(s): Company, ABCI Securities estimates

Exhibit 2: Changes in 2021E and 2022E forecasts

(RMB mn)	2021E (old)	2021E (new)	change (%)	(RMB mn)	2022E (old)	2022E (new)	change (%)
Net interest income	211,706	206,423	(2.50)	Net interest income	230,108	226,425	(1.60)
Net fee and commission	81,087	89,024	9.79	Net fee and commission	85,953	98,817	14.97
Operating income	321,986	319,015	(0.92)	Operating income	348,173	349,516	0.39
Operating expenses	(113,420)	(115,459)	1.80	Operating expenses	(125,561)	(129,206)	2.90
Impairment losses	(78,979)	(69,754)	(11.68)	Impairment losses	(77,311)	(68,701)	(11.14)
Profit before tax	132,476	137,547	3.83	Profit before tax	149,000	156,365	4.94
Income tax expenses	(26,495)	(27,509)	3.83	Income tax expenses	(29,800)	(31,273)	4.94
Net profit attributable to equity holders	105,194	109,352	3.95	Net profit attributable to equity holders	118,287	124,332	5.11
Key indicators (%)			change (ppt)	Key indicators (%)			change (ppt)
Net interest margin	2.35	2.40	0.05	Net interest margin	2.24	2.35	0.11
Net interest spread	2.24	2.28	0.04	Net interest spread	2.10	2.22	0.12
CIR	35.23	36.19	0.96	CIR	36.06	36.97	0.91
ROAA	1.14	1.23	0.09	ROAA	1.12	1.25	0.13
ROAE	14.69	15.13	0.44	ROAE	14.91	15.47	0.56
Dividend payout	33.00	33.00	-	Dividend payout	33.00	33.00	-
CT1 CAR	10.44	12.50	2.06	CT1 CAR	10.12	12.55	2.43
Total CAR	12.88	16.27	3.39	Total CAR	12.43	16.05	3.62
NPL ratio	1.22	1.03	(0.19)	NPL ratio	1.29	0.99	(0.30)
Provision to total loans	5.21	4.60	(0.61)	Provision to total loans	5.30	4.55	(0.75)
Provision coverage ratio	427.05	446.60	19.55	Provision coverage ratio	410.85	459.60	48.75

Source(s): Company, ABCI Securities estimates

Exhibit 3: Changes in GGM assumptions

	H-shr		A-shr		Reason
	old	new	old	new	
TP (HKD/RMB)	57.20	76.10	57.06	75.65	Roll over to mid-2022 BVPS
Sustainable ROE (%)	14.79	15.36	14.79	15.36	Sustain on CMB's solid risk buffers
COE (%)	11.90	10.88	11.09	10.28	
Target 21E P/B (x)	1.59	2.27	1.91	2.69	
Rfr (%)	3.15	3.23	3.15	3.23	With reference to China 10Y government bond
Beta	1.08	1.02	0.98	0.94	With reference to Bloomberg
ERP (%)	8.10	7.50	8.10	7.50	Lower risk premium on improving macro outlook
LT gr (%)	7.00	7.00	7.00	7.00	

Source(s): Company, ABCI Securities estimates



Financial statements

CMB (3968HK/600036CH)

Consolidated income statement

FY Ended Dec 31 (RMB mn)	2019A	2020A	2021E	2022E	2023E
Net interest income	173,090	185,031	206,423	226,425	246,414
Non-interest income	94,975	102,367	112,592	123,091	134,690
Of which: Fees and commissions	71,493	79,486	89,024	98,817	109,687
Operating income	268,065	287,398	319,015	349,516	381,104
Operating expenses	(91,497)	(102,814)	(115,459)	(129,206)	(143,155)
Pre-provision operating profit	176,568	184,584	203,556	220,310	237,948
Impairment losses on loans	(61,159)	(65,025)	(69,754)	(68,701)	(66,634)
Operating profit	115,409	119,559	133,801	151,608	171,314
Non-operating income	1,723	2,881	3,745	4,757	5,898
Profit before tax	117,132	122,440	137,547	156,365	177,212
Tax	(23,709)	(24,481)	(27,509)	(31,273)	(35,442)
Minority interests	(556)	(617)	(685)	(760)	(836)
Net profit attributable to equity holders	92,867	97,342	109,352	124,332	140,934
Preference share dividend	1,670	1,641	3,616	3,616	3,616
Net profit attributable to ordinary shareholders	91,197	95,701	105,737	120,716	137,318
Growth (%)					
Net interest income	7.9	6.9	11.6	9.7	8.8
Of which: Fees and commissions	7.5	11.2	12.0	11.0	11.0
Operating income	8.5	7.2	11.0	9.6	9.0
Operating expenses	12.8	12.4	12.3	11.9	10.8
Pre-provision operating profit	6.4	4.5	10.3	8.2	8.0
Impairment losses on loans	0.5	6.3	7.3	(1.5)	(3.0)
Operating profit	9.7	3.6	11.9	13.3	13.0
Non-operating income	31.6	67.2	30.0	27.0	24.0
Profit before tax	10.0	4.5	12.3	13.7	13.3
Tax	(7.7)	3.3	12.4	13.7	13.3
Minority interests	114.7	11.0	11.0	11.0	10.0
Net profit attributable to equity holders	15.3	4.8	12.3	13.7	13.4
Preference share dividend	1.2	(1.8)	120.4	0.0	0.0
Net profit attributable to ordinary shareholders	15.6	4.9	10.5	14.2	13.8
Per share (RMB)					
EPS	3.62	3.79	4.26	4.84	5.49
BVPS	22.89	25.36	28.11	31.26	34.84
DPS	1.20	1.25	1.38	1.58	1.80
Key ratio (%)					
Net interest margin	2.59	2.49	2.40	2.35	2.28
Net interest spread	2.48	2.40	2.28	2.22	2.15
Cost to income ratio	34.13	35.77	36.19	36.97	37.56
Return on average assets	1.31	1.23	1.23	1.25	1.26
Return on average equity	16.84	15.73	15.13	15.47	15.74
Effective tax rate	20.24	19.99	20.00	20.00	20.00
Dividend payout	33.19	33.02	33.00	33.00	33.00

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

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

Source(s): Company, ABCI Securities estimates

CMB (3968HK/600036CH)
Consolidated balance sheet

As of Dec 31 (RMB mn)	2019A	2020A	2021E	2022E	2023E
Cash & equivalent	641,803	602,123	574,432	553,434	548,203
Interbank assets	408,136	499,565	559,231	646,807	752,462
Investment securities	1,828,656	2,115,967	2,496,841	2,921,304	3,388,713
Net loans and advances	4,267,751	4,794,606	5,371,981	5,988,760	6,606,702
Total interest earning assets	7,146,346	8,012,261	9,002,484	10,110,305	11,296,080
Property and equipment	68,333	71,093	74,648	77,634	80,739
Other non-interest earning assets	202,561	278,094	327,152	377,914	430,110
Total assets	7,417,240	8,361,448	9,404,284	10,565,852	11,806,929
Customer deposits	4,858,801	5,642,578	6,419,760	7,280,013	8,159,743
Interbank liabilities	1,138,714	1,335,373	1,535,679	1,750,674	1,960,755
Subordinated debt	578,191	346,141	259,606	220,665	198,598
Total interest bearing liabilities	6,642,340	7,434,504	8,365,205	9,451,065	10,578,723
Current taxes	19,069	18,648	17,716	16,830	15,988
Deferred tax liabilities	956	1,073	1,191	1,322	1,454
Other liabilities	137,168	176,869	211,013	197,237	209,032
Total liabilities	6,799,533	7,631,094	8,595,125	9,666,454	10,805,197
Share capital	25,220	25,220	25,220	25,220	25,220
Other equity instruments	34,065	84,054	84,054	84,054	84,054
Reserves	552,016	614,476	693,017	782,981	884,958
Minorities	6,406	6,604	6,868	7,143	7,500
Shareholder's equity	617,707	730,354	809,159	899,398	1,001,732
Growth (%)					
Cash & equivalent	6.9	(6.2)	(4.6)	(3.7)	(0.9)
Interbank assets	(19.0)	22.4	11.9	15.7	16.3
Investment securities	7.2	15.7	18.0	17.0	16.0
Net loans and advances	14.1	12.3	12.0	11.5	10.3
Total interest earning assets	9.1	12.1	12.4	12.3	11.7
Property and equipment	17.3	4.0	5.0	4.0	4.0
Other non-interest earning assets	48.1	37.3	17.6	15.5	13.8
Total assets	10.0	12.7	12.5	12.4	11.7
Customer deposits	5.8	29.5	21.5	19.5	16.9
Due to other banks & FIs	36.1	(40.1)	(25.0)	(15.0)	(10.0)
Subordinated debt	9.7	11.9	12.5	13.0	11.9
Total interest bearing liabilities	9.7	11.9	12.5	13.0	11.9
Current taxes	(6.6)	(2.2)	(5.0)	(5.0)	(5.0)
Deferred tax liabilities	(21.1)	12.2	11.0	11.0	10.0
Other liabilities	10.6	28.9	19.3	(6.5)	6.0
Total liabilities	9.6	12.2	12.6	12.5	11.8
Share capital	0.0	0.0	0.0	0.0	0.0
Other equity instruments	0.0	146.7	0.0	0.0	0.0
Reserves	14.8	11.3	12.8	13.0	13.0
Minorities	83.7	3.1	4.0	4.0	5.0
Shareholder's equity	13.6	18.2	10.8	11.2	11.4
Key ratio (%)					
CT1 CAR	11.95	12.29	12.50	12.55	12.89
Total CAR	15.54	16.54	16.27	16.05	16.21
NPL ratio	1.16	1.07	1.03	0.99	1.00
Provision to total loans	4.97	4.67	4.60	4.55	4.48
Provision coverage ratio	426.78	437.68	446.60	459.60	448.00

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

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

Source(s): Company, ABCI Securities estimates

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Definition of equity rating

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

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 (For reference: HSI total return index 2008-20 CAGR at 9.2%)

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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