

BOC (3988 HK / 601988 CH)

Offshore business poses uncertainty

- NIM pressure and a slow balance sheet growth dragged earnings recovery
- Expect better 1Q21 NPL ratio on NPL handling, while offshore asset quality poses higher uncertainties
- Internationalized profile dilutes benefits from macro recovery in China; expect lower earnings growth than other big banks
- Maintain **BUY** on trough valuation. Our GGM-based H/A shr TPs imply 21E P/B of 0.52x/0.64x

Earnings recovery dragged by mild balance sheet growth. Factoring in BOC's FY20 results, we lower our FY21E topline/net profit forecasts by 3.75%/3.95%. We extend our forecast to FY23E, with topline/net profit CAGRs estimated at 4.65%/3.65% in FY20-23E. Total asset and total liabilities grew relative slow at 7.17% and 6.71% YoY in FY20, compared to commercial banks' average of 11.5% and 11.7%, according to CBIRC data. BOC's NIM was at 1.85% in FY20, down 4bps YoY. Although NIM rebounded slightly in 4Q20, we project the bank's NIM to narrow by 4bps-7bps each in FY21E-23E to 1.69% in FY23E. Given the low interest rate environment and keen deposit competition, loan-deposit spread would narrow by 10bps-15bps each in FY21E-23E. This implies a 4.17% NII CAGR over FY21E-23E.

Expect volatility in NPL ratio. Thanks to increased NPL handling, BOC's NPL ratio was down 2bps QoQ to 1.46% in 4Q20. We believe the large-scale NPL handling to persist in 1Q21. BOC's offshore asset quality, however, would pose risk; to its NPL ratio; hence, we estimate the figure to be in the range of 1.48%-1.51% over FY21E-23E.

Increasing contribution from onshore business. BOC has the most internationalized profile among peers, though profit before tax and total asset contribution from offshore gradually reduced from 29% and 27.6% in FY19 to 23.4% and 26.2% in FY20. As we believe China's economy would rebound quicker than other major economies, BOC's significant overseas exposure would result in slower earnings growth than other big banks. Our base case scenario projects ROAE at 8.91%-9.49% in FY21E-23E, hence the sustainable ROAE assumption in our GGM calculation was revised down from 9.86% to 8.09%.

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Results and Valuation

FY ended Dec 31	2019A	2020A	2021E	2022E	2023E
Revenue (RMB mn)	550,010	567,647	607,659	623,502	650,662
Chg (% YoY)	9.2	3.2	7.0	2.6	4.4
Net profit* (RMB mn)	187,405	192,870	200,239	206,271	214,758
Chg (% YoY)	4.1	2.9	3.8	3.0	4.1
EPS (RMB)	0.61	0.61	0.64	0.66	0.69
Chg (% YoY)	4.2	0.1	4.1	3.2	4.4
BVPS (RMB)	5.61	5.98	6.47	6.98	7.50
Chg (% YoY)	9.2	6.6	8.2	7.8	7.5
P/E (x) – H-shr	4.09	4.08	3.92	3.80	3.64
P/B (x) – H-shr	0.45	0.42	0.39	0.36	0.33
P/E (x) – A-shr	5.38	5.37	5.16	5.00	4.79
P/B (x) – A-shr	0.59	0.55	0.51	0.47	0.44
ROAA (%)	0.92	0.87	0.79	0.77	0.75
ROAE (%)	11.45	10.61	9.49	9.14	8.91
DPS(RMB)	0.19	0.20	0.19	0.20	0.21
Yield (%) H-shr	7.62	7.86	7.65	7.90	8.24
Yield (%) A-shr	5.79	5.97	5.81	6.00	6.26

Note: Company; 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\$ 3.98
TP (A): RMB 4.12

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Price (H/A shr)	HK\$ 2.99/ RMB 3.30
Est. share price return (H/A shr)	33.11%/ 24.85%
Est. dividend yield (H/A shr)	7.65%/5.81%
Est. total return (H/A shr)	40.76%/ 30.66%
Last Rating & TP (H/A shr)	BUY, HK\$4.94/ BUY, RMB5.58
Previous Report Date	19 Feb, 2020

Note: BOC was on ABCI research restricted list during Mar-20 to Jan-21

Source(s): Bloomberg, ABCI Securities estimates

Key Data

52Wk H/L (HK\$) (H shr)	3.19/2.33
52Wk H/L (RMB) (A shr)	3.96/3.15
Total issued shares (mn)	294,387.8
Issued H shr (mn)	83,622.3
Issued A shr (mn)	210,765.5
Market cap (HK\$ mn)	1,076,293.8
H-shr market cap (HK\$ mn)	250,030.6
A-shr market cap (HK\$ mn)	826,263.2
3-mth avg daily turnover (HK\$ mn) (H shr)	977.20
3-mth avg daily turnover (RMB mn) (A shr)	507.79

Major shareholder(s) (%):

Central Huijin	64.02
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Source(s): Bloomberg, ABCI Securities

Maintain BUY on low valuation. We roll over our TP calculation to mid-22E BVPS. Lower sustainable ROAE and higher EPR assumption resulted in a 19.4% and 26.2% drop in our GGM-based H/A shr TPs to HK\$ 3.98 and RMB 4.12, implying 0.52x/0.64x FY21E P/B. BOC's H/A shr are trading at 0.39x/0.51x 21E P/B; maintain **BUY** on low valuation.

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 pandemic.

Exhibit 1: 2020 actual results vs. ABCI estimates

(RMB mn)	2020E	2020A	AvE (%)
Net interest income	436,275	415,918	(4.67)
Net fee and commission	91,621	75,522	(17.57)
Operating income	587,949	567,647	(3.45)
Operating expenses	(197,819)	(202,411)	2.32
Impairment losses	(135,296)	(119,016)	(12.03)
Profit before tax	258,130	246,378	(4.55)
Income tax expenses	(43,882)	(41,282)	(5.92)
Net profit	199,306	192,870	(3.23)
Key indicators (%)			AvE (ppt)
Net interest margin	1.93	1.85	(0.08)
Net interest spread	1.76	1.72	(0.04)
Cost to income ratio	33.65	26.73	(6.92)
Return on average assets	0.83	0.87	0.04
Return on average equity	11.07	10.61	(0.46)
Dividend payout	34.00	30.07	(3.93)
CT1 CAR	11.44	11.28	(0.16)
Total CAR	15.66	16.22	0.56
NPL ratio	1.52	1.46	(0.06)
Provision to total loans	3.06	2.96	(0.10)
Provision coverage	201.32	177.84	(23.48)

Source(s): Company, ABCI Securities estimates

Exhibit 2: Changes in 2021E forecasts

(RMB mn)	2021E (old)	2021E (new)	change (%)
Net interest income	476,555	448,219	(5.95)
Net fee and commission	93,453	78,543	(15.95)
Operating income	631,364	607,659	(3.75)
Operating expenses	(209,596)	(218,049)	4.03
Impairment losses	(154,901)	(131,617)	(15.03)
Profit before tax	270,989	258,191	(4.72)
Income tax expenses	(46,068)	(43,893)	(4.72)
Net profit attributable to equity holders	208,484	200,239	(3.95)
Key indicators (%)			change (ppt)
Net interest margin	1.95	1.80	(0.15)
Net interest spread	1.76	1.61	(0.15)
CIR	33.20	35.88	2.68
ROAA	0.80	0.79	(0.01)
ROAE	10.77	9.49	(1.28)
Dividend payout	34.00	30.00	(4.00)
CT1 CAR	11.44	11.47	0.03
Total CAR	15.95	16.21	0.26
NPL ratio	1.58	1.48	(0.10)
Provision to total loans	3.18	3.05	(0.13)
Provision coverage ratio	201.27	172.30	(28.97)

Source(s): Company, ABCI Securities estimates

Exhibit 3: Changes of GGM assumptions

	H-shr		A-shr		Reason
	old	new	old	new	
TP (HKD/RMB)	4.94	3.98	5.58	4.12	Roll over to mid-2022E BVPS
Sustainable ROE (%)	9.86	8.09	9.86	8.09	To reflect pressure on NIM and provision expenses
COE (%)	11.55	11.11	10.20	10.06	
Target 21E P/B (x)	0.57	0.52	0.60	0.64	
Rfr (%)	3.30	3.23	3.30	3.23	With reference to China 10Y government bond
Beta	1.10	0.90	0.92	0.78	With reference to Bloomberg data
ERP (%)	7.50	8.75	7.50	8.75	Adjust according to current macro outlook
LT gr (%)	5.50	5.50	5.50	5.50	

Source(s): Company, ABCI Securities estimates

Financial statements

Consolidated income statement

FY Ended Dec 31 (RMB mn)	2019A	2020A	2021E	2022E	2023E
Net interest income	390,050	415,918	448,219	454,441	470,104
Non-interest income	159,960	151,729	159,440	169,061	180,558
Of which: Fees and commissions	73,812	75,522	78,543	83,255	89,083
Operating income	550,010	567,647	607,659	623,502	650,662
Operating expenses	(198,269)	(202,411)	(218,049)	(233,254)	(248,884)
Pre-provision operating profit	351,741	365,236	389,610	390,248	401,778
Impairment losses on loans	(102,153)	(119,016)	(131,617)	(122,494)	(120,939)
Operating profit	249,588	246,220	257,994	267,753	280,839
Non-operating income	1,057	158	198	247	309
Profit before tax	250,645	246,378	258,191	268,000	281,147
Tax	(48,754)	(41,282)	(43,893)	(45,560)	(47,795)
Minority interests	(14,486)	(12,226)	(14,060)	(16,169)	(18,594)
Net profit attributable to equity holders	187,405	192,870	200,239	206,271	214,758
Preference share dividend	6,826	12,029	12,029	12,029	12,029
Net profit attributable to ordinary shareholders	180,579	180,841	188,210	194,242	202,729
Growth (%)					
Net interest income	8.4	6.6	7.8	1.4	3.4
Non-interest income	11.0	(5.1)	5.1	6.0	6.8
Of which: Fees and commissions	(15.4)	2.3	4.0	6.0	7.0
Operating income	9.2	3.2	7.0	2.6	4.4
Operating expenses	12.0	2.1	7.7	7.0	6.7
Pre-provision operating profit	7.6	3.8	6.7	0.2	3.0
Impairment losses on loans	2.9	16.5	10.6	(6.9)	(1.3)
Operating profit	9.7	(1.3)	4.8	3.8	4.9
Non-operating income	(49.9)	(85.1)	25.0	25.0	25.0
Profit before tax	9.1	(1.7)	4.8	3.8	4.9
Tax	31.0	(15.3)	6.3	3.8	4.9
Minority interests	17.3	(15.6)	15.0	15.0	15.0
Net profit attributable to equity holders	4.1	2.9	3.8	3.0	4.1
Preference share dividend	0.8	76.2	0.0	0.0	0.0
Net profit attributable to ordinary shareholders	4.2	0.1	4.1	3.2	4.4
Per share (RMB)					
EPS	0.61	0.61	0.64	0.66	0.69
BVPS	5.61	5.98	6.47	6.98	7.50
DPS	0.19	0.20	0.19	0.20	0.21
Key ratio (%)					
Net interest margin	1.89	1.85	1.80	1.73	1.69
Net interest spread	1.74	1.72	1.61	1.55	1.50
Cost to income ratio	28.00	26.73	35.88	37.41	38.25
Return on average assets	0.92	0.87	0.79	0.77	0.75
Return on average equity	11.45	10.61	9.49	9.14	8.91
Effective tax rate	19.45	16.76	17.00	17.00	17.00
Dividend payout	30.00	30.07	30.00	30.00	30.00

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

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



Consolidated balance sheet

As of Dec 31 (RMB mn)	2019A	2020A	2021E	2022E	2023E
Cash & equivalent	565,467	803,145	963,774	1,137,253	1,319,214
Interbank assets	2,078,809	2,076,840	2,118,377	2,160,744	2,203,959
Investment securities	5,514,062	5,591,117	5,702,939	5,816,998	5,933,338
Net loans and advances	12,743,425	13,848,304	15,029,833	16,194,018	17,384,260
Total interest earning assets	20,901,763	22,319,406	23,814,923	25,309,013	26,840,771
Property and equipment	244,540	248,589	253,561	258,632	261,218
Derivative assets	93,335	171,738	206,086	241,120	274,877
Other non-interest earning assets	1,530,106	1,662,926	1,786,990	1,910,568	2,032,646
Total assets	22,769,744	24,402,659	26,061,559	27,719,333	29,409,513
Customer deposits	15,817,548	16,879,171	18,103,577	19,346,851	20,587,946
Interbank liabilities	3,153,998	3,216,763	3,281,098	3,346,720	3,413,655
Subordinated debt	1,124,098	1,270,437	1,397,481	1,537,229	1,690,952
Total interest bearing liabilities	20,095,644	21,366,371	22,782,156	24,230,800	25,692,552
Trading liabilities	90,060	212,052	275,668	350,098	437,622
Current taxes	59,102	55,665	54,552	53,461	52,391
Deferred tax liabilities	5,452	6,499	7,669	8,973	10,408
Other liabilities	542,790	599,235	624,304	599,300	573,434
Total liabilities	20,793,048	22,239,822	23,744,348	25,242,631	26,766,407
Share capital	494,281	571,878	571,878	571,878	571,878
Reserves	1,357,420	1,466,541	1,610,962	1,759,703	1,914,496
Minority interest	124,995	124,418	134,371	145,121	156,731
Total shareholders' equity	1,976,696	2,162,837	2,317,212	2,476,702	2,643,105
Growth (%)					
Cash & equivalent	28.5	42.0	20.0	18.0	16.0
Interbank assets	(10.8)	(0.1)	2.0	2.0	2.0
Investment securities	9.1	1.4	2.0	2.0	2.0
Net loans and advances	10.7	8.7	8.5	7.7	7.3
Total interest earning assets	8.1	6.8	6.7	6.3	6.1
Property and equipment	7.5	1.7	2.0	2.0	1.0
Derivative assets	(24.8)	84.0	20.0	17.0	14.0
Other non-interest earning assets	(2.8)	8.7	7.5	6.9	6.4
Total assets	7.1	7.2	6.8	6.4	6.1
Customer deposits	6.3	6.7	7.3	6.9	6.4
Interbank liabilities	(3.0)	2.0	2.0	2.0	2.0
Subordinated debt	37.9	13.0	10.0	10.0	10.0
Total interest bearing liabilities	6.0	6.3	6.6	6.4	6.0
Trading liabilities	(9.3)	135.5	30.0	27.0	25.0
Current taxes	111.9	(5.8)	(2.0)	(2.0)	(2.0)
Deferred tax liabilities	19.9	19.2	18.0	17.0	16.0
Other liabilities	17.8	10.4	4.2	(4.0)	(4.3)
Total liabilities	6.4	7.0	6.8	6.3	6.0
Share capital	25.4	15.7	0.0	0.0	0.0
Reserves	11.4	8.0	9.8	9.2	8.8
Minority interest	11.2	(0.5)	8.0	8.0	8.0
Shareholders' equity	14.6	9.4	7.1	6.9	6.7
Key ratio (%)					
CT1 CAR	11.30	11.28	11.47	11.61	11.75
Total CAR	15.59	16.22	16.21	16.34	16.49
NPL ratio	1.37	1.46	1.48	1.51	1.50
Provision to total loans	2.97	2.96	3.05	3.10	3.15
Provision coverage ratio	182.86	177.84	172.30	172.19	176.67

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

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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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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