



Key Data

Average PER (x)	5.2
Average PBV (x)	0.9
Average Dividend Yield (%)	5.7
Sector 3 months avg vol (HK\$m)	4,948

Source: Company, Bloomberg, ABCI Securities

Operating income composition in 3Q12 (%)

Net interest income	80.5
Non-interest income	19.5

Source: CBRC

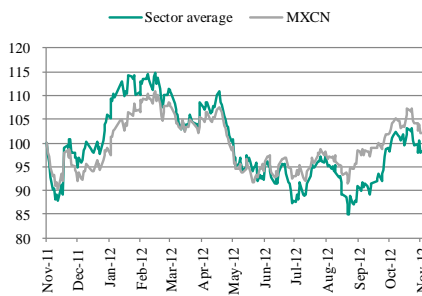
Share performance (%)

	Absolute	Relative*
1-mth	(0.8)	(1.0)
3-mth	2.2	(2.8)
6-mth	(2.4)	(5.1)

Source: Bloomberg

*Relative to MSCI China

1 year price performance



Source: Bloomberg

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China Bank Sector – Neutral
Diversified Banks Industry

Three takeaways from 3Q CBRC statistics

We noticed three key points from the CBRC 3Q banking indicators. First, high 2.77% NIM was offset by weak fee income, as a result to lower ROE. Second, big banks' assets quality are the strongest given their consistent prudence operation. Last but not the least, higher LDR hinted banks started to transmit their deposit base into wealth management products for higher fees, thus placing risks on small banks' future loan growth capacity and deposit competitions.

Record NIM, lower ROE. Despite the CBRC released 3Q12 system NIM at 2.77%, the highest level since 2011, system ROE reduced by 75bps to 21.5%. We believe this was mainly due to weaker-than-expected non-interest income in 3Q12, which has reduced by 116bps to 19.5%. Weak export momentum and bearish capital market atmosphere resulted in declining fees generated from trade financing and wealth management products. We expect situation to gradually improve in 4Q12 amid mild recovery of economic indicators in October and November.

Asset quality divergence. Although 3Q12 system NPL ratio increased only by 1bp to 0.95%, NPL balance has increased by 5% Q-Q. Amongst, all categories of banks saw increased NPL% except large commercial banks, i.e. big five banks. Joint stock commercial banks and rural commercial banks saw largest NPL balance increment by 13% and 14% respectively. Interestingly large banks had a higher NPL% of 1% than 0.7% for joint stock banks; this was mainly due to a more prudent risk management rather than a relatively poor asset quality.

Inched up LDR. System LDR rose by 95bps to 65.3%. Besides stable loan growth, we believe the inch up was also due to the slowdown of deposits growth. The latest October data saw a slight deposits outflow and we believe some banks started to boost their wealth management products which were partly funded by original deposits customers, given wealth management products allowed them to record a front-end fees. However, especially to small banks, this would place additional risks on future loan growth capacity and deposit competition.

Risk factors. Acceleration of interest rate liberalization, sharp deterioration of asset quality and increasing competition from non-bank FIs.

Sector Valuation Summary

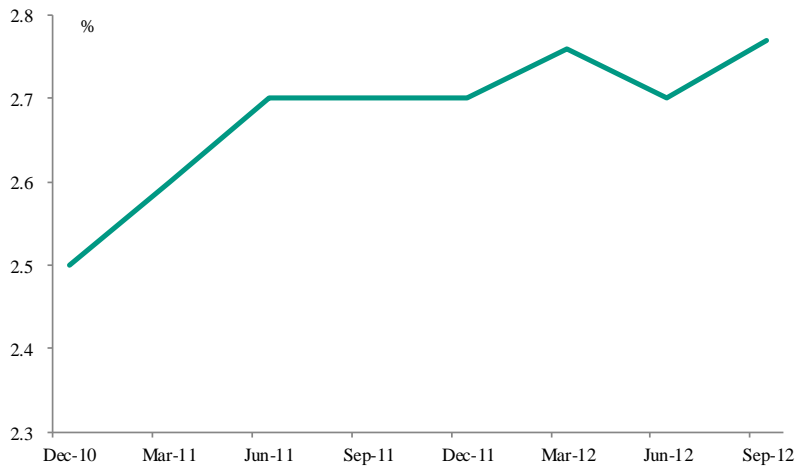
Companies	Ticker	Rating	Price (HK\$)	Target (HK\$)	Upside (%)	13E PER	13E PBV	13E Yield
CCB	939 HK	Buy	5.69	6.30	10.7	5.9	1.1	5.9
ABC	1288 HK	Buy	3.30	3.45	4.5	5.5	1.0	5.5
MSB	1988 HK	Buy	7.11	7.66	7.7	4.2	0.9	5.9
ICBC	1398 HK	Hold	5.02	4.44	(11.6)	6.2	1.1	4.8
BOC	3988 HK	Hold	3.14	2.94	(6.4)	5.2	0.8	6.1
BoCom	3328 HK	Hold	5.34	5.13	(3.9)	4.8	0.8	6.7
CMB	3968 HK	Hold	13.84	13.47	(2.7)	5.5	1.0	4.5
CNCB	998 HK	Hold	3.86	3.61	(6.5)	4.3	0.6	5.9

Source: Company, Bloomberg, ABCI Securities estimates



System NIM slightly rose by 4bps in 3Q12 to 2.77%, this was combined effect of better big banks NIM, which accounted for 40% market share, and higher LDR.

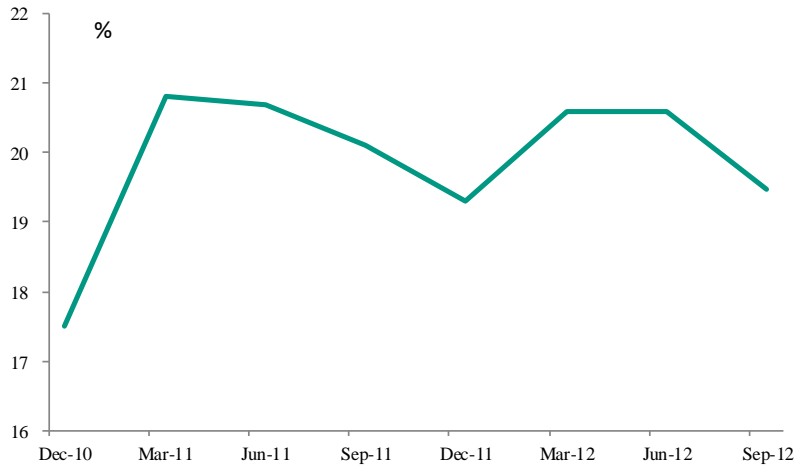
Exhibit 1: System NIM trend



Source: CBRC, ABCI Securities estimates

Non-interest income to operating income reduced in 3Q12 due to weaker trade related fee and fee from wealth management products on the back on slowed trade data and weak capital market momentum.

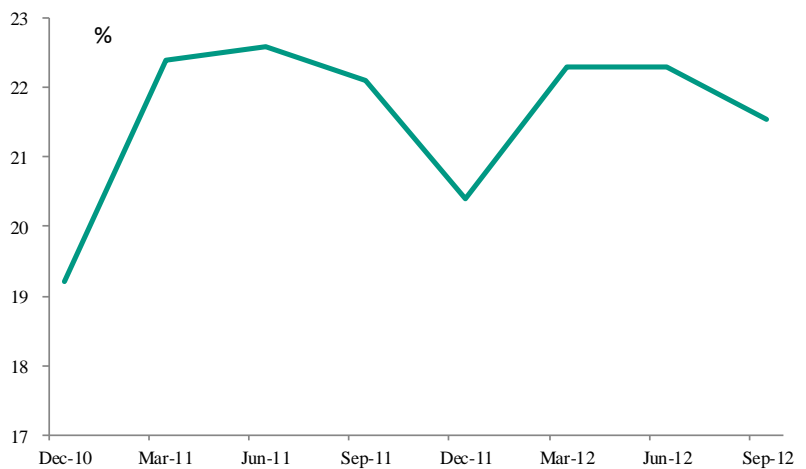
Exhibit 2: System non-interest income to operating income trend



Source: CBRC, ABCI Securities estimates

Net net, we saw a mild reduction of ROE, however we expect fee momentum to pick up from 4Q for better macro data and banks to dedicate more in fee income growth to offset weakening NIM outlook.

Exhibit 3: System ROE trend



Source: CBRC, ABCI Securities estimates



Exhibit4: System NPL trend

(Rmb bn)	1Q12		2Q12		Q-Q	3Q12		Q-Q
	NPL	NPL%	NPL	NPL%		NPL	NPL%	
System	4,382	0.94	4,564	0.94	4.2	4,788	0.95	4.9
Large commercial banks*	2,994	1.04	3,020	1.01	0.9	3,070	1.00	1.7
Joint stock commercial bank**	608	0.63	657	0.65	8.1	743	0.70	13.1
City commercial banks	359	0.78	403	0.82	12.3	424	0.85	5.2
Rural commercial banks	374	1.52	426	1.57	13.9	487	1.65	14.3
Foreign banks	48	0.49	58	0.58	20.8	63	0.62	8.6

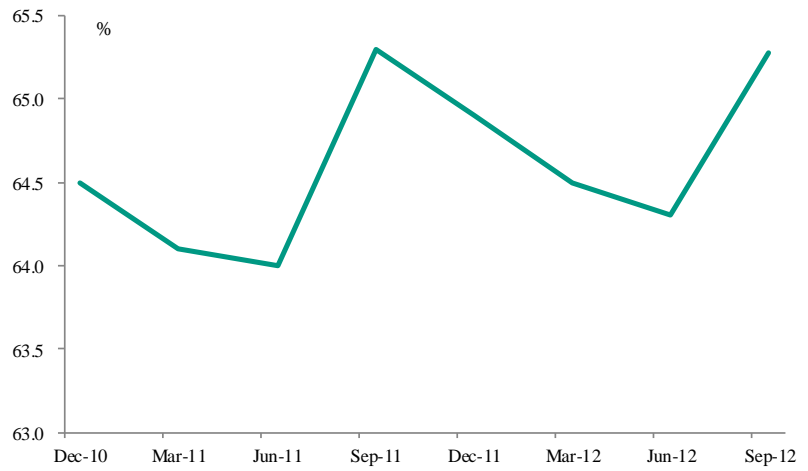
Source: CBRC, ABCI Securities estimates

*Large commercial banks included ABC, ICBC, CCB, BOC and BoCom

** Joint stock commercial banks mainly included MSB, SMB, CNCB, Huaxia, GF, PingAn Bank, SHPD, Industrial Bank, and Everbright Bank

Exhibit5: System LDR trend

We believe the increase in LDR reflected the fact that banks started to focus on wealth management product for front end fee income, with funds from deposits base.



Source: CBRC, 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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