



ABC (1288 HK)

NIM trend to improve in 2014, reiterate BUY

March 26, 2014
Equity Focus
Rating: BUY
TP: HK\$ 4.74

H-Share price (HK\$) 3.20
Est. share price return 48.1%
Est. 2014 div. yield 7.7%
Est. total return 55.8%

Previous Rating & TP BUY; HK\$ 4.74
Previous Report Date Aug 2, 2013

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Key Data

52Wk H/L(HK\$)	4.09/2.94
Issued shares (mn)	324,794
H-Shares (mn)	30,739
A-Shares (mn)	294,055
Market cap	
H-shares (HK\$ mn)	98,364
A-Shares (HK\$ mn)	882,977
3-mth avg daily turnover (HK\$ mn)	488.39
Major shareholder(s) (%): Huijin	40.28

Source(s): Company, Bloomberg, ABCI Securities

2013 revenue breakdown (%)

Corporate banking	54.3
Retail banking	38.7
Treasury operations	6.0
Others	1.0

Source(s): Company, ABCI Securities

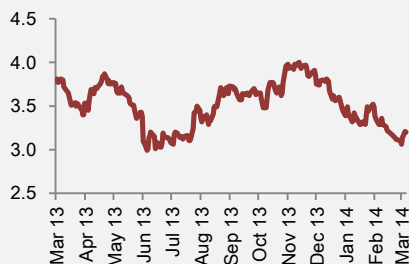
Share performance (%)

	Absolute	Relative*
1-mth	4.5	(0.8)
3-mth	(15.6)	(9.9)
6-mth	(13.3)	(7.5)

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

1-Year stock performance (HK\$)



Source(s): Bloomberg

- ABC's 2013 net profit grew 14.6% YoY; NIM improved in 4Q13 on better loan yield and reduction in deposit cost despite interest rate liberalization
- NPL ratio was down by 11bps to 1.22% by end-2013. Management expects a similar figure for 2014 despite expectation of a slight rebound in NPL balance
- The Group's CT1 and total CAR were able to fulfill the new capital requirement; issuance of preference share should lift investor's concern on Chinese banks' capital position by offering additional capital source
- Reiterate BUY on the counter based on its trough valuation at 0.85x FY14E P/B, fast growth and sound fundamentals. Our TP implies a 48.1% upside

2013 net profit in line with consensus. ABC reported its 2013 net profit at RMB 166,351mn, in line with consensus (RMB 165,864mn) and our forecast (RMB 168,651mn). NIM was reported at 2.79% (ABCI estimate: 2.8%). Based on the data released, we estimate NIM in 4Q13 to be 2.96%, driven by increased LDR, improved loan yield in 2H13, and reduced deposit cost (2013: -10bps yoy) despite interest rate liberalization. Management guided that NIM will follow a choppy uptrend after a decent start in 1Q14. As operating cost grew slower than topline revenue, CIR dropped by 46bps to 36.3%, while ROAE rose 15bps yoy to 20.89% in 2013.

Benign asset quality with strong provision as buffer. Taking into account of the six disposals amounting to RMB 4.1bn in 2013 (the lowest among the big four banks), ABC's NPL ratio was down by 11bps to 1.22%. New NPL were mainly from manufacturing and wholesale & retail sectors. Geographically, NPL ratio in Zhejiang and Wenzhou were 1.55% and 2.67% by end-2013. Although management expects a slight rebound in NPL balance for 2014, overall NPL ratio would remain stable at current level. We believe ABC's provisioning ratio of 4.46%, one of the highest among peers, and provision coverage ratio of 367.04% would provide strong buffer against any potential headwinds.

Preference share to provide new capital source. With CT1 and total CAR at 9.25% and 11.86%, ABC has been able to comply with the requirements under the new capital rule. Upcoming release of preference share issuance plan by CBRC should provide additional capital source to the Chinese banks. We believe this would alleviate the market's concern on CAR. We believe the big four banks, including ABC, would be among the first few to fortify its CAR position with this new channel.

Reiterate BUY at trough valuation. ABC is currently trading at the trough valuation of 0.85x FY14E P/B, which is almost 2s.d. below its historical P/B average. The Group remains our top pick for the sector based on its fastest growth among the big four banks, low LDR, and stable NIM amid interest rate liberalization. Our TP of HK\$ 4.74 implies a 48.1% upside. Reiterate **BUY**.

Risk factors: 1) Sharp deterioration in asset quality; 2) Deposit competition triggered by interest rate liberalization; 3) Increased competition from non-bank financial institutions.

Results and Valuation

FY ended Dec 31	2011A	2012A	2013A	2014E	2015E
Revenue (RMB mn)	379,756	424,964	465,771	540,339	612,551
Chg (% YoY)	29.9	11.9	9.6	16.0	13.4
Net profit (RMB mn)	121,927	145,094	166,315	181,677	199,133
Chg (% YoY)	28.5	19.0	14.6	9.2	9.6
EPS (RMB)	0.38	0.45	0.51	0.56	0.61
Chg (% YoY)	5.0	19.0	14.6	9.2	9.6
BVPS (RMB)	2.00	2.31	2.60	3.01	3.35
Chg (% YoY)	19.8	15.4	12.6	15.9	11.3
P/E (x)	-	5.73	5.00	4.58	4.18
P/B (x)	-	1.11	0.98	0.85	0.76
ROE (%)	20.5	20.7	20.9	19.9	19.3
ROA (%)	1.11	1.16	1.22	1.17	1.14
DPS(RMB)	0.13	0.16	0.18	0.20	0.21
Yield (%)	-	6.11	6.91	7.65	8.38

Source(s): Bloomberg, ABCI Securities estimates



Exhibit 1: ABC's quarterly P&L trend

(RMB mn)	1Q13	2Q13	3Q13	4Q13	4Q13E	QoQ (%)	A vs E	2012	2013	2013E	YoY (%)	A vs E
Net interest margin	2.78	2.70	2.77	2.96	2.91	0.19	(0.05)	2.81	2.79	2.80	(0.02)	(0.01)
Net interest income	89,288	90,714	95,622	100,578	115,451	5.18	14.8	341,879	376,202	391,075	10	(3.8)
Non-interest income	30,553	25,489	21,226	12,301	18,450	(42.05)	50.0	83,085	89,569	95,718	8	(6.4)
Topline	119,841	116,203	116,848	112,879	133,902	(3.40)	18.6	424,964	465,771	486,794	10	(4.3)
Operating expenses	(46,675)	(47,396)	(48,845)	(55,691)	(73,709)	14.02	32.4	(182,802)	(198,607)	(216,625)	9	(8.3)
POPP	73,166	68,807	68,003	57,188	60,192	(15.90)	5.3	242,162	267,164	270,168	10	(1.1)
Loan loss provision	(12,442)	(10,029)	(9,012)	(21,507)	(19,605)	138.65	(8.8)	(54,235)	(52,990)	(51,088)	(2)	3.7
Profit before tax	60,724	58,778	58,991	35,681	40,588	(39.51)	13.8	187,927	214,174	219,081	14	(2.2)
Tax expenses	(13,673)	(13,445)	(13,338)	(7,507)	(9,933)	(43.72)	32.3	(42,796)	(47,963)	(50,389)	12	(4.8)
Minority interest	(40)	8	(17)	153	8	(1,000)	(94.6)	(37)	104	(41)	(381)	(355.5)
Net profit	47,011	45,341	45,636	28,327	30,663	(37.93)	8.2	145,094	166,315	168,651	15	(1.4)

Source(s): Company, ABCI Securities estimates

Exhibit 2: ABC P/B(x) band chart (Dec 2010- Mar 2014)



Source(s): Company, Bloomberg, ABCI Securities estimates



Consolidated income statement (2011A-2015E)

FY Ended Dec 31 (RMB mn)	2011A	2012A	2013A	2014E	2015E
Net interest income	307,199	341,879	376,202	431,105	489,928
Non-interest income	72,557	83,085	89,569	109,234	122,623
Of which: fees and commissions	68,750	74,844	83,171	99,074	111,458
Operating income	379,756	424,964	465,771	540,339	612,551
Operating expenses	(144,200)	(167,306)	(181,146)	(235,951)	(280,083)
Amortization	(13,130)	(15,496)	(17,461)	(19,959)	(22,354)
Pre-prov. operating profits	222,426	242,162	267,164	284,429	310,114
Impairment loans losses	(64,225)	(54,235)	(52,990)	(48,427)	(51,437)
Operating profit	158,201	187,927	214,174	236,003	258,678
Profit before tax	158,201	187,927	214,174	236,003	258,678
Tax	(36,245)	(42,796)	(47,963)	(54,281)	(59,496)
Minority interests	(29)	(37)	104	(45)	(49)
Net profit	121,927	145,094	166,315	181,677	199,133
Growth (%)					
Net interest income	26.9	11.3	10.0	14.6	13.6
Non-interest income	44.8	14.5	7.8	22.0	12.3
Of which: fees and commissions	49.0	8.9	11.1	19.1	12.5
Operating income	29.9	11.9	9.6	16.0	13.4
Operating expenses	23.4	16.0	8.3	30.3	18.7
Amortization	16.2	18.0	15.0	12.0	12.0
Pre-prov. operating profits	35.5	8.9	10.3	6.5	9.0
Impairment loans losses	47.9	(15.6)	(2.3)	(8.6)	6.2
Operating profit	31.0	18.8	14.0	10.2	9.6
Profit before tax	31.0	18.8	14.0	10.2	9.6
Tax	40.3	18.1	12.1	13.2	9.6
Minority interests	(14.7)	27.6	10.0	10.0	10.0
Net profit	28.5	19.0	14.6	9.2	9.6
Per share data (RMB)					
EPS	0.38	0.45	0.51	0.56	0.61
BVPS	2.00	2.31	2.60	3.01	3.35
DPS	0.13	0.16	0.18	0.20	0.21
Key ratio (%)					
Net interest margin	2.85	2.81	2.79	2.82	2.87
Net interest spread	2.73	2.67	2.65	2.58	2.61
Cost to income ratio	38.0	39.4	36.3	43.7	45.7
Return on average assets	1.11	1.16	1.22	1.17	1.14
Return on average equity	20.5	20.7	20.9	19.9	19.3
Effective tax rate	22.9	23.0	23.0	23.0	23.0
Dividend payout	35.0	35.0	35.0	35.0	35.0

Source(s): Company, ABCI Securities estimates



Consolidated balance sheet (2011A-2015E)

As of Dec 31 (RMB mn)	2011A	2012A	2013A	2014E	2015E
Cash & cash equivalent	2,487,082	2,613,111	2,603,802	2,922,227	3,110,672
Dues from banks	873,997	1,300,233	975,351	1,970,087	2,352,118
Investment securities	2,628,052	2,851,448	3,228,284	3,365,717	3,647,778
Net loans and advances	5,410,086	6,153,411	6,902,522	7,873,099	8,806,640
Total interest earning assets	11,399,217	12,918,203	13,709,959	16,131,129	17,917,209
Property and equipment	131,815	141,490	150,859	163,506	174,951
Other non-interest earning assets	146,545	184,649	701,284	264,197	313,419
Total assets	11,677,577	13,244,342	14,562,102	16,558,832	18,405,579
Customer deposits	9,622,026	10,862,935	11,811,411	13,365,321	14,781,619
Due to banks	724,286	934,139	903,717	1,424,562	1,709,474
Subordinated debt	119,390	192,639	266,261	265,842	305,718
Total interest bearing liabilities.	10,465,702	11,989,713	12,981,389	15,055,725	16,796,811
Current taxes	37,868	40,419	44,263	48,907	53,798
Deferred tax liabilities	27	15	8	22	26
Other liabilities	524,192	462,841	691,905	473,246	463,561
Total liabilities	11,027,789	12,492,988	13,717,565	15,577,900	17,314,196
Share capital	324,794	324,794	324,794	324,794	324,794
Reserves	324,807	425,021	518,314	654,326	764,633
Minorities	187	1,539	1,429	1,812	1,957
Shareholder's equity	649,788	751,354	844,537	980,932	1,091,384
Growth (%)					
Cash & cash equivalent	19.4	5.1	(0.4)	12.2	6.4
Dues from banks	25.1	48.8	(25.0)	102.0	19.4
Investment securities	4.0	8.5	13.2	4.3	8.4
Net loans and advances	13.0	13.7	12.2	14.1	11.9
Total interest earning assets	12.9	13.3	6.1	17.7	11.1
Total assets	13.0	13.4	9.9	13.7	11.2
Customer deposits	8.3	12.9	8.7	13.2	10.6
Due to banks	24.2	29.0	(3.3)	57.6	20.0
Subordinated debt	91.5	61.4	38.2	(0.2)	15.0
Total interest bearing liabilities.	9.8	14.6	8.3	16.0	11.6
Total liabilities	12.6	13.3	9.8	13.6	11.1
Shareholder's equity	19.8	15.4	12.4	16.1	11.3
Key ratio (%)					
Loan to deposits	58.6	59.2	61.2	61.7	62.5
Core CAR	9.5	9.7	9.3	9.8	9.8
Total CAR	11.9	12.6	11.9	12.8	12.9
NPL ratio	1.55	1.33	1.22	1.60	1.66
NPL growth	(13.0)	(1.7)	2.3	19.0	15.7
Net bad debt charge ratio	1.2	0.9	0.7	0.7	0.6
Provision to total loans	4.1	4.4	4.5	4.6	4.6
Provision coverage	263.1	326.1	367.0	283.5	277.4

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 from 2009-2013

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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