

China Construction Bank (939 HK)

The issuance of preferred stock reduced the capital pressure

CHINA | BANKING | COMPANY NEWS

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Capital pressure declined

According to the latest announcement of China Construction Bank (CCB or the Group) last weekend, it will issue the preferred stock of 600 million shares privately, and the book value per share is RMB100, with the total amount of RMB60 billion, in order to increase its tier-1 capital.

The dividend of the preferred stock is paid annually, and according to the terms, if the core tier-1 CAR decreased to 5.125% (or below), CCB has the rights to convert the preferred stock into A Shares common stock without the agreement of the shareholders of the preferred stock.

In the previous report, we mentioned that the bank's capital pressure was smaller than other large-sized banks. By the end of this Sep, CCB's CAR and Core Tier-1 CAR recorded to 14.53% and 11.65% respectively, up 0.90ppts and 1.19ppts respectively compared with the end of 2013. After the issuance of the preferred stock, excluding the relative expenses, CCB's CAR and Core Tier-1 CAR would achieve to 15.12% and 11.65% respectively, representing the further decrease of the capital pressure.

Stable improvement of the performance

In all, the preferred stock will increase the bank's capital obviously, the performance met our expectation in the first three quarters, and the market environment will improve obviously in 4Q, and the investors hold more optimistic view on the expectation especially after the launch of the HK-SH Stock Connect, therefore we still hold cautiously optimistic view on the bank's future performance, but estimate the profit growth would go down continually and net profit should increase by 8% y-y in average in the next two years. We increase CCB's 12-month target price to HK\$6.90, 15% higher than the latest closing price, equivalent to P/E5.0x and P/B1.0x in 2015 respectively, and the valuation is quite attractive. Maintain Accumulate rating

Accumulate (Maintain)

CMP HK\$5.98

TARGET HK\$6.90 (+15%)

COMPANY DATA

O/S SHARES (MN) :	250,011
MARKET CAP (HK\$ MN) :	1,437,696
52 - WK HI/LO (RS) :	6.42/ 4.89

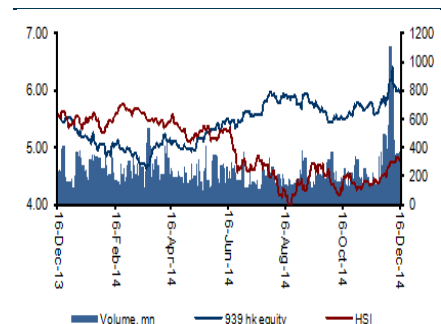
SHARE HOLDING PATTERN, %

Central Huijin Investment :	57.06
HKSCC Nominees :	29.86
Temasek Holdings :	6.39

PRICE PERFORMANCE, %

	1MTH	3MTH	1YR
CCB	5.28	2.93	7.85
HSI	-4.73	-3.62	-1.73

PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

Key Financial Summary

FYE	12/13	12/14F	12/15F	12/16F
Operating Profit (RMB mn)	279,746	317,490	353,786	375,060
Net Profit, adj. (RMB mn)	214,657	245,960	274,446	290,224
EPS, adj. (RMB)	0.86	0.98	1.10	1.16
P/E (X)	5.6	4.9	4.3	4.1
BVPS (RMB)	4.26	4.83	5.44	6.18
P/B (X)	1.1	1.0	0.9	0.8
DPS (RMB)	0.30	0.34	0.38	0.41
Div. Yield	6.3%	7.2%	8.0%	8.5%

Source: Bloomberg, PSR est.

*All multiples & yields based on current market price

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Investment Thesis

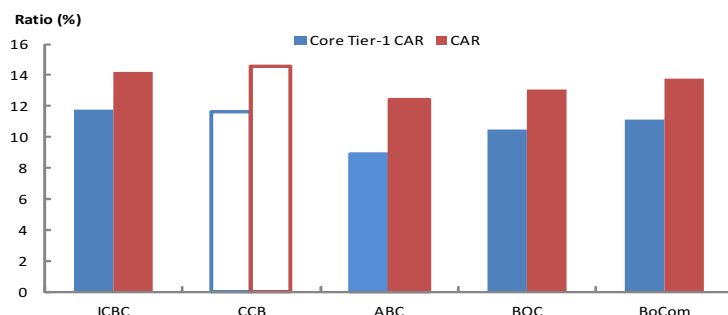
The issuance of the preferred stock will increase CCB's capital obviously this time, and based on the historical dividend payout record, the impact is quite small for the bank's common stockholders. Considering the Group's table performance, and the high CAR, we believe there is a further optimization of the bank's capital structure, and the profit growth will maintain at the stable level.

CAR will increase

The CAR of CCB increased obviously in 2014 due to the internal capital accumulation from profit outpacing that of risk-weighted assets and the issuance of qualifying capital instruments. By the end of Sep, CAR and Core Tier-1 CAR recorded to 14.53% and 11.65%, up 0.90ppts and 1.19ppts respectively compared with the end of 2013, and CCB's CAR was still on the top of the peers.

According to the plan of the preferred stock, excluding the relative expenses, and based on the 3Q results, CCB's CAR and Core Tier-1 CAR would achieve to 15.12% and 11.65% respectively, representing the further decrease of the capital pressure.

CAR of Big 5 state-owned banks in China in 3Q2014



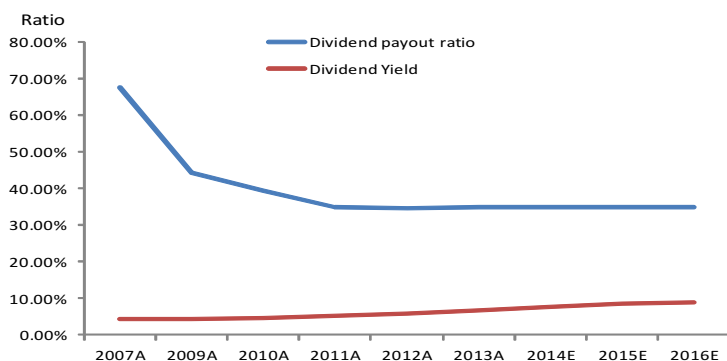
Source: Company, Phillip Securities (HK) Research

Small impact of profits

Common stockholders may have a loss of RMB3.6 billion based on the total amount of the preferred stock as RMB60 billion with the dividend yield of 6% because the preferred stockholders can gain the dividend primarily. However, considering CCB's stable historical dividend payout record, we believe the impact of the preferred stock is quite small.

Additionally, if all preferred stocks were converted into A Shares common stocks, based on the total amount of RMB60 billion and the convertible price of RMB5.20/share, the shares will be no more than 11.538 billion ($=600/5.2$), and as at the end of this Sep, CCB's total common stock was 250,011 million, therefore original shareholders' voting rights would be diluted no more than 4.41%.

Changes of CCB's dividend payment



Source: Company, Phillip Securities (HK) Research

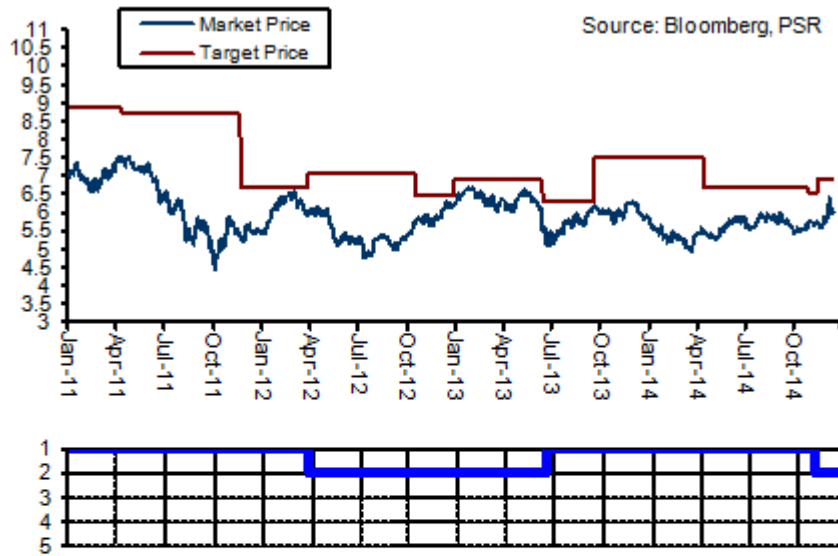
Financials

FYE	FY12	FY13	FY14F	FY15F	FY16F
Valuation Ratios					
P/E (X)	6.2	5.6	4.9	4.3	4.1
P/B (X)	1.3	1.1	1.0	0.9	0.8
Dividend Payout ratio	34.68%	34.95%	35.00%	35.00%	35.00%
Dividend Yield	5.6%	6.3%	7.2%	8.0%	8.5%
Per share data (RMB)					
EPS, reported	0.77	0.86	0.98	1.10	1.16
EPS, adj.	0.77	0.86	0.98	1.10	1.16
DPS	0.27	0.30	0.34	0.38	0.41
BVPS	3.77	4.26	4.83	5.44	6.18
Growth					
Net interest income	16.0%	10.3%	13.3%	10.4%	7.7%
Net fee and commission income(exp.)	7.5%	11.5%	5.8%	7.8%	9.8%
Operating income	15.8%	10.5%	10.4%	10.2%	8.5%
Net Income, adj.	14.1%	11.1%	14.6%	11.6%	5.7%
Key Ratios					
Net interest spread	2.58%	2.56%	2.59%	2.62%	2.65%
Net interest margin	2.75%	2.74%	2.80%	2.80%	2.81%
Loan to deposit	64.44%	70.28%	71.60%	73.46%	74.68%
Cost to income ratio	29.60%	29.65%	27.75%	26.69%	27.05%
ROAA	1.47%	1.47%	1.52%	1.52%	1.44%
ROAE	22.04%	21.23%	21.63%	21.36%	19.97%
NPL ratio	0.99%	0.99%	1.17%	1.24%	1.32%
Coverage ratio	271.29%	268.22%	231.18%	217.11%	204.55%
Core CAR	11.32%	10.75%	11.85%	12.05%	12.36%
CAR	14.32%	13.34%	14.74%	14.98%	15.12%
Income Statement (RMB mn)					
	FY12	FY13	FY14F	FY15F	FY16F
Interest income	603,241	646,253	723,803	803,422	875,730
Interest expense	(250,039)	(256,709)	(282,380)	(316,265)	(351,055)
Net interest income	353,202	389,544	441,423	487,156	524,675
Fee and commission income	96,218	107,432	113,878	122,988	135,287
Fee and commission expense	(2,711)	(3,149)	(3,495)	(3,950)	(4,542)
Net fee and commission income	93,507	104,283	110,383	119,038	130,745
Operating income	462,533	511,140	564,189	621,915	674,856
Operating expenses	(171,081)	(188,185)	(195,712)	(207,455)	(228,201)
Operating profit before impairment losses	291,452	322,955	368,476	414,460	446,655
Impairment losses	(40,041)	(43,209)	(50,987)	(60,674)	(71,595)
Operating profit	251,411	279,746	317,490	353,786	375,060
Profit before tax	251,439	279,806	317,592	353,928	375,260
Income tax	(57,837)	(64,684)	(71,152)	(78,979)	(84,508)
Effective income tax rate	23.00%	23.12%	22.40%	22.32%	22.52%
Profit for the year	193,602	215,122	246,439	274,949	290,752
Minority interests	423	465	479	503	528
Net profit attributable to equity holders o	193,179	214,657	245,960	274,446	290,224
Dividend	67,003	75,030	86,086	96,056	101,578
Balance Sheet (RMB mn)					
	FY12	FY13	FY14F	FY15F	FY16F
Cash and balances with banks and other finan	585,898	321,286	289,157	294,941	312,637
Balances with central bank	2,458,069	2,475,001	2,722,501	2,967,526	3,204,928
Trading financial assets	27,572	364,050	254,835	293,060	380,978
Net loans and advances to customers	7,309,879	8,361,361	9,364,724	10,394,844	11,434,328
Available-for-sale financial assets	701,041	760,292	897,145	1,067,602	1,270,446
Held-to-maturity investments	1,918,322	2,100,538	2,310,592	2,541,651	2,770,400
Debt securities classified as receivables	219,713	189,737	193,532	201,273	209,324
Interests in associates and jointly controlled en	2,366	2,624	3,044	3,500	3,990
Fixed assets	113,946	135,678	141,105	148,160	158,532
Deferred tax assets	27,051	38,448	39,217	41,178	44,060
Goodwill	1,651	1,610	3,542	3,577	3,649
Other assets	23,335	26,011	80,634	96,761	116,113
Total Assets	13,972,828	15,363,210	17,097,479	19,105,825	21,250,559
Deposits from banks and other financial institut	977,487	692,095	1,141,957	1,617,011	2,071,391
Borrowings from central banks	6,281	79,157	151,981	182,378	209,734
Placements from banks and non-bank financial	120,256	155,917	233,876	280,651	322,748
Deposits from customers	11,343,079	12,223,037	13,078,650	14,151,099	15,311,489
Financial liabilities at fair value through profit o	37,251	380,380	384,184	461,021	553,225
Accrued staff costs	32,772	34,080	35,102	38,613	42,474
Current taxation	53,271	60,209	62,617	68,879	75,767
Interest payable	123,215	153,627	199,715	229,672	264,123
Debt securities issued	262,991	357,540	464,802	557,762	669,315
Deffered tax liabilities	332	138	186	192	198
Other liabilities	47,389	65,942	95,616	114,739	137,687
Total Liabilities	13,023,283	14,288,881	15,877,308	17,732,324	19,690,826
Share capital	250,011	250,011	250,011	250,011	250,011
Reserves	691,657	815,940	958,499	1,110,928	1,296,221
Shareholder's equity	941,668	1,065,951	1,208,510	1,360,939	1,546,232
Minority interests	7,877	8,378	11,662	12,562	13,501
Total shareholders' equity	949,545	1,074,329	1,220,172	1,373,502	1,559,733
Total shareholders' equity and liabilities	13,972,828	15,363,210	17,097,479	19,105,825	21,250,559

Source: PSR

Source: Company, Phillip Securities (HK) Research Estimates

Ratings History



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
< -20%	Sell	5

Remarks

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PHILLIP RESEARCH STOCK SELECTION SYSTEMS

Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within \pm 5% from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

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