

BoCom (3328.HK)

Stable profit growth

CHINA | BANKING | COMPANY REPORT

27 February 2015

Summary

- According to BoCom's 2014Q3 Results, by the end of Sep 2014, the Group's net profits reached to RMB51.522 billion, up 5.8% y-y approximately, in line with our expectation, equivalent to the EPS of RMB0.69. The profit growth rate slowed down compared with 9.4% in 3Q2013. Net interest income growth rate reduced to 4.49% due to the large increase of interest expenses, but increased slightly q-q. Meanwhile, due to the obvious growth of the NPLs, the Group's impairment losses increased largely by 23.7% y-y to RMB16.5 billion. On the other hand, BoCom's intermediate business incomes increased stably, and net commission fees grew 17.9% y-y to RMB22.984 billion during the period;
- We pay close attention to the bank's asset quality. BoCom's asset quality went down obviously in 3Q2014. It reduced the expansion of loans to SMMEs, and the portion of the loans to total loans cut 2.48ppts to 40.37% in 3Q2014 from 42.85% in 2013, with the amount of RMB1.26 trillion, up 0.03% slightly. The management stated that bad debts in excess capacity industries such as steel trading industry and SMMEs increased consistently under the downturn of the macroeconomic environment, especially in Zhejiang and Jiangsu Provinces, which caused the Group's NPL ratio increased obviously from 1.05% in 2013 to 1.17% in 3Q2014, with the sharp growth of doubtful and loss loans. The coverage ratio dropped from 213.65% to 201.29%, down 12.36ppts. We believe BoCom will still face the risk of deterioration of asset quality in future, both the amount and ratio of NPLs will increase continually, and the NPL ratio would go up to 1.22% in 2014, the trend meets our expectation;
- Overall, BoCom's businesses recorded the stable growth, the profit growth continued to decrease, but will rebound in future. We expect its net profit growth would maintain around 7% in 2014, higher than that of 2013. In addition, BoCom's dividend payout ratio still stays at the high level as 30%, based on 3-stage DDM, we increase the Group's 12-m target price to HK\$8.20, around 22% higher than the current closing price, equivalent to 6.8xP/E and 0.9xP/B in 2015E respectively, the valuation is quite attractive, and maintains Buy rating.

Stable profit growth in 2014

By the end of Sep 2014, the Group's net profits reached to RMB51.522 billion, up 5.8% y-y approximately, in line with our expectation, equivalent to the EPS of RMB0.69. The profit growth rate slowed down compared with 9.4% in 3Q2013. Net interest income growth rate reduced to 4.49% due to the large increase of interest expenses, but increased slightly q-q. Meanwhile, the Group's impairment losses increased largely by 23.7% y-y to RMB16.5 billion due to the obvious growth of the NPLs.

However, due to the development of the market environment, BoCom's intermediate business incomes increased rapidly, and net commission fees grew 17.9% y-y to RMB22.984 billion. The fees of settlement and management increased by 38.98% and 43.58% y-y to RMB2.453 billion and 5.11 billion, and bank card fees also increased by 19.70% y-y to RMB7.916 billion. The fees of investment banking business dropped 22.71% y-y to RMB4.605 billion.

We expect BoCom's interest incomes and intermediate business incomes would maintain stable growth, but the operating expense will go up, especially for impairment losses, and the Group's net profit would increase by 7% approximately to RMB66.8 billion in 2014.

Buy (Maintain)

CMP HK6.71

TARGET HK\$8.20 (+22%)

COMPANY DATA

O/S SHARES (MN) :	35,012
MARKET CAP (HK\$ MN) :	223,879
52 - WK HI/LO (HK\$) :	7.36/ 4.53

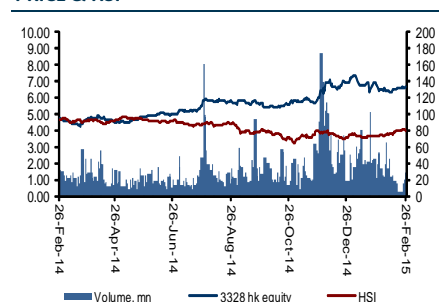
SHARE HOLDING PATTERN, %

MOF:	26.53
HKSCC Nominees	20.08
HSBC	18.70

PRICE PERFORMANCE, %

	1MTH	3MTH	1YR
BoCom	-4.08	9.11	39.62
HSI	-0.12	3.22	8.54

PRICE & HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

Key Financial Summary

FYE	12/13	12/14F	12/15F	12/16F
Operating Profit (RMB mn)	79,867	86,644	93,449	99,915
Net Profit, adj. (RMB mn)	62,295	66,784	71,922	77,061
EPS, adj. (RMB)	0.84	0.90	0.97	1.04
P/E (X)	6.5	6.0	5.6	5.2
BVPS (RMB)	5.65	6.36	7.10	7.89
P/B (X)	1.0	0.9	0.8	0.7
DPS (RMB)	0.26	0.27	0.29	0.31
Div. Yield	4.8%	5.0%	5.4%	5.7%

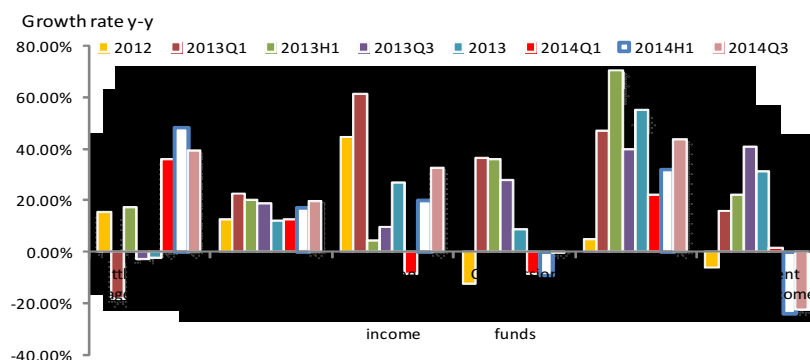
Source: Bloomberg, PSR est.

*All multiples & yields based on current market price

Source: Company reports, Phillip Securities Est.

Xingyu CHEN (+ 86 21 51699400-105)
chenxingyu@phillip.com.cn

The growth of BoCom's commission fees by the end of 3Q2014



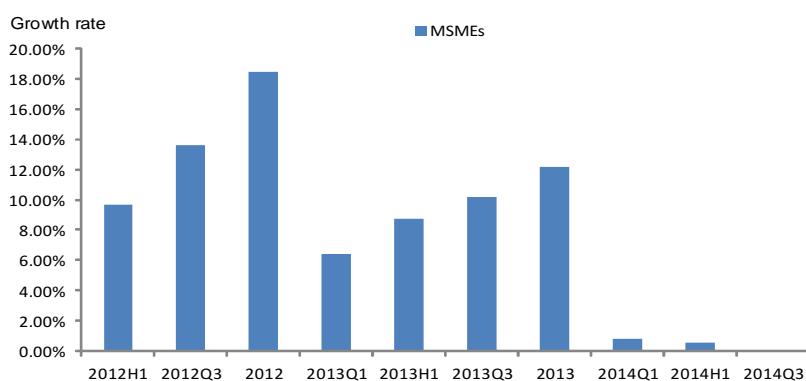
Source: Company, Phillip Securities (HK) Research

The asset quality went down continually

The assets of BoCom increased stably, and the Group's total assets raised around 4.22% to RMB6.21 trillion compared with the end of 2013, net asset increased by 8.6% to RMB455.80 billion, equivalent to the BVPS of RMB6.14.

On the other hand, BoCom's asset quality went down obviously in 3Q2014. It reduced the expansion of loans to SMMEs, and the portion of the loans to total loans cut 2.48ppts to 40.37% in 3Q2014 from 42.85% in 2013, with the amount of RMB1.26 trillion, up 0.03% slightly. The management stated that bad debts in excess capacity industries such as steel trading industry and SMMEs increased consistently under the downturn of the macroeconomic environment, especially in Zhejiang and Jiangsu Provinces, which caused the Group's NPL ratio increased obviously from 1.05% in 2013 to 1.17% in 3Q2014, with the sharp growth of doubtful and loss loans, up 29.26% and 31.31% respectively compared with the end of 2013. The coverage ratio dropped from 213.65% to 201.29%, down 12.36ppts. We believe BoCom will still face the risk of deterioration of asset quality in future, both the amount and ratio of NPLs will increase continually, and the NPL ratio would go up to 1.22% in 2014, the trend meets our expectation

The Growth of BoCom's MSMEs by the end of 3Q2014



Source: Company, Phillip Securities (HK) Research

The breakdown of BoCom`s five loan categories (stipulated by the Chinese banking regulatory authorities) in 3Q2014

Loan quality analysis (RMB Million)	2013A	2014Q3	Growth rate	Portion (2013)	Portion (2014Q3)
Normal	3,173,011	3,356,160	5.77%	97.14%	96.46%
Special Mention	59,047	82,116	39.07%	1.81%	2.36%
Substandard	13,778	14,190	2.99%	0.42%	0.41%
Doubtful	13,586	17,561	29.26%	0.42%	0.50%
Loss	6,946	9,121	31.31%	0.21%	0.26%
Total non-performing loans	34,310	40,872	19.13%	1.05%	1.17%
Total loans and advances to customers	3,266,368	3,479,148	6.51%	100.00%	100.00%
Asset quality ratios			Changes (ppt)		
Non-performing loan ratio	1.05%	1.17%	0.12		
Allowances for impairment losses to non-performing loans	213.65%	201.29%	-12.36		

Source: Company, Phillip Securities (HK) Research

Risk

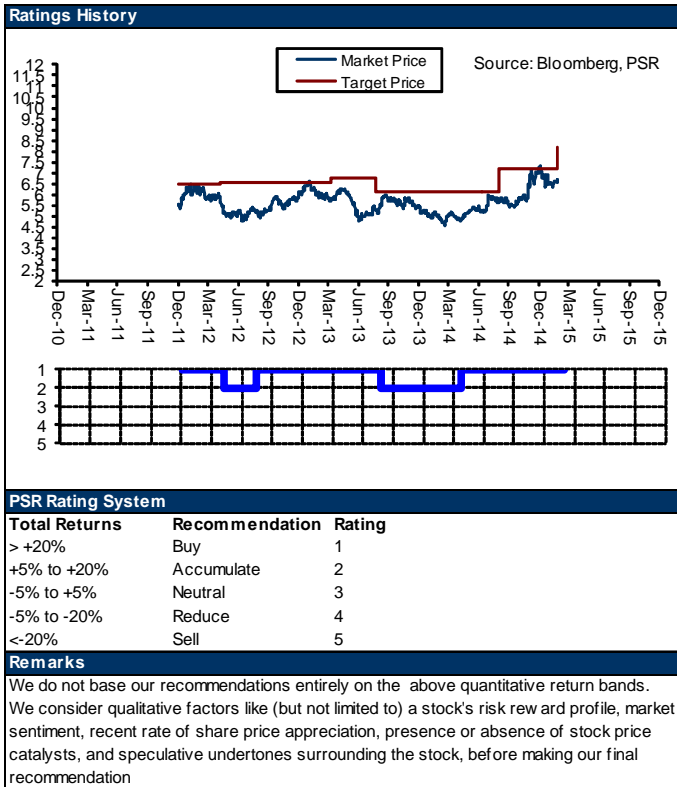
Lower-than-expected growth of incomes;
The deterioration of the asset quality due to the sharp growth of the NPLs;
Increase of the capital pressure;
Share price decreases largely affected by the market environment in the short run.

FINANCIALS

FYE	FY12	FY13	FY14F	FY15F	FY16F
Valuation Ratios					
P/E (X)	6.1	6.5	6.0	5.6	5.2
P/B (X)	1.1	1.0	0.9	0.8	0.7
Dividend Payout ratio	30.53%	30.99%	30.00%	30.00%	30.00%
Dividend Yield	4.43%	4.80%	4.98%	5.36%	5.75%
Per share data (RMB)					
EPS, reported	0.88	0.84	0.90	0.97	1.04
EPS, adj.	0.88	0.84	0.90	0.97	1.04
DPS	0.24	0.26	0.27	0.29	0.31
BVPS	5.12	5.65	6.36	7.10	7.89
Growth					
Net interest income	17.1%	8.8%	6.1%	6.7%	6.8%
Net fee and commission income(exp.)	6.8%	24.4%	17.5%	21.2%	23.1%
Operating income	16.0%	11.4%	9.4%	10.1%	11.2%
Net Income, adj.	15.1%	6.7%	7.2%	7.7%	7.1%
Key Ratios					
Net interest spread	2.43%	2.33%	2.22%	2.29%	2.35%
Net interest margin	2.59%	2.52%	2.44%	2.48%	2.54%
Loan to deposit ratio	73.23%	79.17%	76.25%	77.61%	77.16%
Cost-to-income ratio	29.85%	29.68%	29.14%	28.06%	27.00%
Return on average assets	1.18%	1.11%	1.08%	1.08%	1.05%
Return on average equity	17.91%	15.58%	14.98%	14.39%	13.85%
Non-performing loan ratio	0.92%	1.05%	1.16%	1.28%	1.28%
Provision coverage of impaired loans	250.68%	213.65%	207.11%	186.86%	186.86%
Allowances for impairment losses to total loans	2.30%	2.24%	2.34%	2.40%	2.40%
Core capital adequacy ratio	11.24%	9.76%	11.15%	11.56%	11.32%
Capital adequacy ratio	14.07%	12.08%	13.45%	13.92%	13.60%
Income Statement (RMB mn)					
	FY12	FY13	FY14F	FY15F	FY16F
Net interest income	120,126	130,658	138,659	148,000	158,098
Net fee and commission income	20,882	25,968	30,501	36,962	45,491
Other incomes	7,176	8,402	11,381	13,852	17,453
Operating income	148,184	165,028	180,542	198,814	221,042
Operating expenses	(57,805)	(65,578)	(68,857)	(73,677)	(79,571)
Insurance business expense	(630)	(1,173)	(2,581)	(3,613)	(5,058)
Operating profit before impairment losses	89,749	98,277	109,104	121,524	136,413
Impairment losses	(14,537)	(18,410)	(22,460)	(28,075)	(36,498)
Operating profit	75,212	79,867	86,644	93,449	99,915
Shares of P/L of Jonit controlled Entities	4	42	105	115	135
Profit before tax	75,216	79,909	86,749	93,564	100,050
Income tax	(16,740)	(17,448)	(19,716)	(21,294)	(22,571)
Effective income tax rate	22.26%	21.83%	22.73%	22.76%	22.56%
Net profit for the period	58,476	62,461	67,033	72,270	77,479
Minority interest	103	166	249	349	418
Net profit attributable to equity holders of the	58,373	62,295	66,784	71,922	77,061
Dividend	17,823	19,308	20,035	21,577	23,118
Balance Sheet (RMB mn)					
	FY12	FY13	FY14F	FY15F	FY16F
Cash and balances with banks and other financial institutions	520,963	566,429	577,758	600,868	672,972
Balances with central bank	816,846	896,556	932,418	997,688	1,097,456
Financial assets held for trading	52,161	73,310	87,972	114,364	142,955
Loans and advances to customers	2,879,628	3,193,063	3,416,577	3,689,904	4,021,995
Investments	833,618	1,011,594	1,041,942	1,190,940	1,369,580
Fixed assets	45,536	57,179	77,192	88,770	100,311
Deferred tax assets	12,501	17,224	16,363	20,454	24,544
Other assets	112,126	145,582	203,815	244,578	293,493
Total Assets	5,273,379	5,960,937	6,354,036	6,947,564	7,723,306
Deposits and placements from banks and other financial institutions	942,989	1,126,563	1,276,396	1,429,563	1,572,520
Deposits from customers	3,728,412	4,157,833	4,257,621	4,521,593	4,955,666
Financial liabilities at fair value through profit or loss	23,060	28,640	24,344	26,048	28,653
Other liabilities	110,769	113,435	147,466	213,825	288,664
Current taxes	7,125	6,107	8,244	9,481	11,377
Deferred tax liabilities	5	18	10	14	25
Subordinated notes issued	79,572	106,857	165,628	216,973	277,726
Total Liabilities	4,891,932	5,539,453	5,879,709	6,417,498	7,134,631
Share capital	74,263	74,263	74,263	74,263	74,263
Reserves	305,655	345,298	397,890	452,910	511,307
Shareholders' equity	379,918	419,561	472,153	527,173	585,570
Minority interest	1,529	1,923	2,174	2,892	3,105
Total shareholders' equity	381,447	421,484	474,327	530,066	588,675
Total shareholders' equity and liabilities	5,273,379	5,960,937	6,354,036	6,947,564	7,723,306

Source: PSR

Source: Company, Phillip Securities (HK) Research Estimates



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

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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Contact Information (Regional Member Companies)

SINGAPORE

Phillip Securities Pte Ltd
Raffles City Tower
250, North Bridge Road #06-00
Singapore 179101
Tel : (65) 6533 6001
Fax : (65) 6535 6631
Website: www.poems.com.sg

HONG KONG

Phillip Securities (HK) Ltd
Exchange Participant of the Stock Exchange of Hong Kong
11/F United Centre 95 Queensway
Hong Kong
Tel (852) 22776600
Fax (852) 28685307
Websites: www.phillip.com.hk

INDONESIA

PT Phillip Securities Indonesia
ANZ Tower Level 23B,
Jl Jend Sudirman Kav 33A
Jakarta 10220 – Indonesia
Tel (62-21) 57900800
Fax (62-21) 57900809
Website: www.phillip.co.id

THAILAND

Phillip Securities (Thailand) Public Co. Ltd
15th Floor, Vorawat Building,
849 Silom Road, Silom, Bangrak,
Bangkok 10500 Thailand
Tel (66-2) 6351700 / 22680999
Fax (66-2) 22680921
Website: www.phillip.co.th

UNITED KINGDOM

King & Shaxson Capital Limited
6th Floor, Candlewick House,
120 Cannon Street,
London, EC4N 6AS
Tel (44-20) 7426 5950
Fax (44-20) 7626 1757
Website: www.kingandshaxson.com

AUSTRALIA

PhillipCapital Australia
Level 12, 15 William Street,
Melbourne, Victoria 3000, Australia
Tel (613) 96188238
Fax (613) 92002272
Website: www.phillipcapital.com.au

MALAYSIA

Phillip Capital Management Sdn Bhd
B-3-6 Block B Level 3 Megan Avenue II,
No. 12, Jalan Yap Kwan Seng, 50450
Kuala Lumpur
Tel (603) 21628841
Fax (603) 21665099
Website: www.poems.com.my

JAPAN

PhillipCapital Japan K.K.
Nagata-cho Bldg.,
8F, 2-4-3 Nagata-cho,
Chiyoda-ku, Tokyo 100-0014
Tel (81-3) 35953631
Fax (81-3) 35953630
Website: www.phillip.co.jp

CHINA

Phillip Financial Advisory (Shanghai) Co. Ltd
No 436 Hengfeng Road,
Greentech Unit 604,
Postal code 200070
Tel (86-21) 51699400
Fax (86-21) 63532643
Website: www.phillip.com.cn

FRANCE

King & Shaxson Capital Limited
3rd Floor, 35 Rue de la Bienfaisance 75008
Paris France
Tel (33-1) 45633100
Fax (33-1) 45636017
Website: www.kingandshaxson.com

UNITED STATES

Phillip Futures Inc
141 W Jackson Blvd Ste 3050
The Chicago Board of Trade Building
Chicago, IL 60604 USA
Tel +1.312.356.9000
Fax +1.312.356.9005