

China Banking Sector

High provision banks will outperform

25 bps cut on RRR is below the consensus of 50 bps. In addition, 1Q22 loan data indicates more headwind ahead. Regulators highlight that state-owned banks should lower provision coverage to maintain appropriate profit growth. High provision SOEs is expected to outperform in FY22. Maintain overweight on banking sector, top pick is PSBC (1658 HK), BUY PSBC with a target price of HK\$8.40.

- On 15 Apr 2022, PBOC announced a much-anticipated cut of its RRR to shore up its slowing economy amid growing headwinds. PBOC would cut the reserve requirement ratio (RRR) for all banks by 25bps, for small commercial banks and selected rural lenders will benefit from a further reduction of 25bps, releasing about RMB 530b in long-term liquidity, effective from 25 April 2022. The weighted average RRR for financial institutions will be lowered to 8.1% after the cut. The PBOC said the latest RRR cut would boost the long-term funds for banks, enabling them to step up support for industries and firms affected by COVID-19 outbreaks, and lower costs for financial institutions. The cut will help banks save RMB 6.5bn on the cost; the saved cost will translate to lower interest rate to help real economy. The PBOC will continue to keep liquidity broadly stable, while closely watching inflationary trends and policy changes made by developed countries.
- The RRR announced on Friday marks the third reserve cut in the current easing cycle, following 50 bps cuts in Jul 2021 and Dec 2021. It had been widely expected after China's cabinet said on Wednesday (13 Apr 22) that monetary policy tools should be used in a timely way to bolster growth. Although this will help nudge down bank lending rate, the reserve cut alone will have little impact to boost growth. In our view, we need more RRR and LPR cuts to stimulate the economy. As the headwind build, government's 5.5% GDP growth target in 2022 may now be hard to achieve without more aggressive stimulus measures. We continue to anticipate additional rate reduction in the near future, placing pressure on banks' net interest margins in 2022.
- Maintain OVERWEIGHT on banking sector and BUY on PSBC (1658 HK) as our top pick.** We roll over valuation basis to YE22 and lift target price to HK\$8.40 accordingly. Our TP implies 0.91x 2022E and 0.85x 2023E P/B. The stock is trading at 0.72x/0.66x FY22/23E P/B, almost equivalent to -1SD of 3-yr historical mean (0.82x P/B).

Valuation Table

| Name | Ticker | Mkt Cap | Rating | Closing price | TP (LC) | Upside | P/E | P/B | Yield |
|------|-----------|---------|--------|---------------|---------|--------|-----|-----|-------|
| PSBC | 1658 HK | 618 | BUY | 6.51 | 8.40 | 29% | 5.7 | 0.7 | 5.3% |
| CCB | 939 HK | 1,489 | BUY | 5.86 | 8.10 | 38% | 3.9 | 0.4 | 7.7% |
| SPDB | 600000 CH | 240 | HOLD | 8.15 | 9.34 | 14% | 4.2 | 0.4 | 6.5% |
| BOSH | 601229 CH | 97 | BUY | 6.75 | 9.04 | 34% | 3.9 | 0.5 | 7.3% |
| CQRC | 3618 HK | 34 | HOLD | 3.10 | 2.80 | -10% | 2.7 | 0.2 | 10.9% |
| BOCS | 601577 CH | 33 | HOLD | 7.93 | 8.32 | 5% | 4.0 | 0.6 | 6.3% |

Source: CMBIGM estimates based on 2022E earnings. Closing price @15 Apr, Mkt cap (LC bn)

OUTPERFORM
(Maintain)

China Banking Sector

Eric Wang

(852) 6367 0561
ericwang@cmbi.com.hk

Gigi Chen, CFA

(852) 3916 3739
gigichen@cmbi.com.hk

Stocks covered

| Ticker | Rating | TP (LC) | Upside |
|-----------|--------|---------|--------|
| 1658 HK | BUY | 8.40 | 29% |
| 939 HK | BUY | 8.10 | 38% |
| 600000 CH | HOLD | 9.34 | 14% |
| 601229 CH | BUY | 9.04 | 34% |
| 3618 HK | HOLD | 2.8 | -10% |
| 601577 CH | HOLD | 8.32 | 5% |
| 601658 SH | BUY | 7.07 | 24% |
| 601939 SH | BUY | 7.5 | 20% |
| 601077 SH | HOLD | 3.6 | -11% |

Source: CMBIGM estimates

Recent Reports:

- China Banking – Looking for the safe harbour ([link](#))
- China Banking – 4Q21 Quarterly Review ([link](#))
- China Financials Weekly – Manageable impacts from Russia-Ukraine Crisis ([link](#))

In terms of regulators' comments on provision strategy, because regulators highlighted that tolerating increasing NPL ratio and appropriate decline on provision coverage, we think allowance to total loan ratio and provision coverage ratio should not be less than 2.5% and 150% (regulator suggested level). We did sensitivity analyst on earnings change under the scenario of 50 bps and 100 bps cut on allowance on total loan ratio. Based on our analysis, PSBC and ABC are more sensitive to the ratio cut, meanwhile BOC and BoComm do not have too much capacity to release their "reserved profit" from provision.

Figure 1: Impacts from changes on provision strategy

| | Allowance to total loan | | Earnings released (RMB m) | | As % of FY21 net profit | | Provision coverage | |
|---------------|-------------------------|-------------|---------------------------|-------------|-------------------------|-------------|--------------------|-------------|
| | cut 50 bps | cut 100 bps | cut 50 bps | cut 100 bps | cut 50 bps | cut 100 bps | cut 50 bps | cut 100 bps |
| ICBC | 2.50% | 2.50% | 65,102 | 65,102 | 18.7% | 18.7% | 184% | 184% |
| CCB | 2.90% | 2.50% | 70,529 | 126,953 | 23.3% | 42.0% | 213% | 192% |
| ABC | 3.80% | 3.30% | 64,407 | 128,813 | 26.7% | 53.4% | 274% | 247% |
| BOC | 2.50% | 2.50% | - | - | - | - | - | - |
| BoComm | 2.50% | 2.50% | - | - | - | - | - | - |
| PSBC | 2.93% | 2.50% | 24,203 | 45,017 | 31.8% | 59.1% | 373% | 333% |

Source: Company data, CMBIGM estimates

Disclosures & Disclaimers

Analyst Certification

The research analyst who is primary responsible for the content of this research report, in whole or in part, certifies that with respect to the securities or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by that analyst in this report.

Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the stock(s) covered in this research report 3 business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong listed companies covered in this report; and (4) have any financial interests in the Hong Kong listed companies covered in this report.

CMBIGM Ratings

BUY : Stock with potential return of over 15% over next 12 months
HOLD : Stock with potential return of +15% to -10% over next 12 months
SELL : Stock with potential loss of over 10% over next 12 months
NOT RATED : Stock is not rated by CMBIGM

OUTPERFORM : Industry expected to outperform the relevant broad market benchmark over next 12 months
MARKET-PERFORM : Industry expected to perform in-line with the relevant broad market benchmark over next 12 months
UNDERPERFORM : Industry expected to underperform the relevant broad market benchmark over next 12 months

CMB International Global Markets Limited

Address: 45/F, Champion Tower, 3 Garden Road, Hong Kong, Tel: (852) 3900 0888 Fax: (852) 3900 0800

CMB International Global Markets Limited ("CMBIGM") is a wholly owned subsidiary of CMB International Capital Corporation Limited (a wholly owned subsidiary of China Merchants Bank)

Important Disclosures

There are risks involved in transacting in any securities. The information contained in this report may not be suitable for the purposes of all investors. CMBIGM does not provide individually tailored investment advice. This report has been prepared without regard to the individual investment objectives, financial position or special requirements. Past performance has no indication of future performance, and actual events may differ materially from that which is contained in the report. The value of, and returns from, any investments are uncertain and are not guaranteed and may fluctuate as a result of their dependence on the performance of underlying assets or other variable market factors. CMBIGM recommends that investors should independently evaluate particular investments and strategies, and encourages investors to consult with a professional financial advisor in order to make their own investment decisions.

This report or any information contained herein, have been prepared by the CMBIGM, solely for the purpose of supplying information to the clients of CMBIGM or its affiliate(s) to whom it is distributed. This report is not and should not be construed as an offer or solicitation to buy or sell any security or any interest in securities or enter into any transaction. Neither CMBIGM nor any of its affiliates, shareholders, agents, consultants, directors, officers or employees shall be liable for any loss, damage or expense whatsoever, whether direct or consequential, incurred in relying on the information contained in this report. Anyone making use of the information contained in this report does so entirely at their own risk.

The information and contents contained in this report are based on the analyses and interpretations of information believed to be publicly available and reliable. CMBIGM has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIGM provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIGM may issue other publications having information and/or conclusions different from this report. These publications reflect different assumption, point-of-view and analytical methods when compiling. CMBIGM may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIGM may have a position, make markets or act as principal or engage in transactions in securities of companies referred to in this report for itself and/or on behalf of its clients from time to time. Investors should assume that CMBIGM does or seeks to have investment banking or other business relationships with the companies in this report. As a result, recipients should be aware that CMBIGM may have a conflict of interest that could affect the objectivity of this report and CMBIGM will not assume any responsibility in respect thereof. This report is for the use of intended recipients only and this publication, may not be reproduced, reprinted, sold, redistributed or published in whole or in part for any purpose without prior written consent of CMBIGM.

Additional information on recommended securities is available upon request.

For recipients of this document in the United Kingdom

This report has been provided only to persons (I) falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended from time to time) ("The Order") or (II) are persons falling within Article 49(2) (a) to (d) ("High Net Worth Companies, Unincorporated Associations, etc.") of the Order, and may not be provided to any other person without the prior written consent of CMBIGM.

For recipients of this document in the United States

CMBIGM is not a registered broker-dealer in the United States. As a result, CMBIGM is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. The research analyst who is primary responsible for the content of this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA"). The analyst is not subject to applicable restrictions under FINRA Rules intended to ensure that the analyst is not affected by potential conflicts of interest that could bear upon the reliability of the research report. This report is intended for distribution in the United States solely to "major US institutional investors", as defined in Rule 15a-6 under the US, Securities Exchange Act of 1934, as amended, and may not be furnished to any other person in the United States. Each major US institutional investor that receives a copy of this report by its acceptance hereof represents and agrees that it shall not distribute or provide this report to any other person. Any U.S. recipient of this report wishing to effect any transaction to buy or sell securities based on the information provided in this report should do so only through a U.S.-registered broker-dealer.

For recipients of this document in Singapore

This report is distributed in Singapore by CMBI (Singapore) Pte. Limited (CMBISG) (Company Regn. No. 201731928D), an Exempt Financial Adviser as defined in the Financial Advisers Act (Cap. 110) of Singapore and regulated by the Monetary Authority of Singapore. CMBISG may distribute reports produced by its respective foreign entities, affiliates or other foreign research houses pursuant to an arrangement under Regulation 32C of the Financial Advisers Regulations. Where the report is distributed in Singapore to a person who is not an Accredited Investor, Expert Investor or an Institutional Investor, as defined in the Securities and Futures Act (Cap. 289) of Singapore, CMBISG accepts legal responsibility for the contents of the report to such persons only to the extent required by law. Singapore recipients should contact CMBISG at +65 6350 4400 for matters arising from, or in connection with the report.