

25 July 2018

Financial Services | Banks

## China Merchants Bank

**Buy** (Maintained)

Target Price: HKD37.50

Price: HKD30.60

Market Cap: USD101,808m

Bloomberg Ticker: 3968 HK

### Earnings Momentum Stays Intact

Maintain BUY and GGM-derived TP of HKD37.50, 23% upside. CMB's preliminary 1H18 results, once again, suggested an all-round improvement in its operations. Net profit growth is gradually recovering, likely driven by margin expansion and a notable pick-up in fee income. Loan growth also accelerated, thanks to the bank's strong deposit franchise. NPL ratio remained on the downward trajectory, reflecting decent risk control. We expect the big Chinese banks to report a similar trend in operating performance for 2Q18.

**Earnings growth picked up further.** CMB released preliminary 1H18 net profit of CNY44.8bn, up 14% YoY and accounting for 55% of our FY18 full-year estimates. On a quarterly basis, profit growth accelerated to 14.5% YoY in 2Q18 from 13.5% YoY in 1Q18, mainly driven by robust non-II (up 32% YoY). Fee income growth was likely strong due to its bank card and settlement businesses. 1H18's ROE rebounded by 0.5ppts YoY to 19.6%, in line with our forecast of a recovery in profitability.

**Balance sheet expansion with solid funding support.** On healthy deposit growth of 4.7% QoQ, total loans extended 4.4% QoQ, leading to a flattish LDR of 91% in 2Q18. We expect loan growth to remain strong in 2H18, as the bank taps further into the micro and smaller enterprises (MSE) and retail consumption market. Monetary easing by the People's Bank of China (PBoC) would also alleviate funding pressure of joint-stock banks.

**Asset quality keeps improving.** NPL ratio edged down 5bps QoQ to 1.43%, the sixth consecutive quarterly decline. We estimate a 5% YoY retreat in provision charge, while LLC ratio likely stayed the highest in the sector at around 300%. CMB's above-peer retail banking exposure and stringent NPL recognition should underpin a benign asset quality outlook.

**Maintain BUY.** We keep our earnings forecasts and valuation unchanged. Our TP of HKD37.50 is based on FY18F P/BV of 1.6x. The bank will tentatively report its full set of interim results on 24 Aug 2018.

Figure 1: CMB's preliminary 2Q18 results

FYE Dec (CNYm)	1H17	1H18	YoY (%)	2Q17	1Q18	2Q18	QoQ (%)	YoY (%)
<b>P&amp;L</b>								
NII	70,896	76,434	7.8	35,982	37,939	38,495	1.5	7.0
Non-II	41,988	49,397	17.6	19,938	23,047	26,350	14.3	32.2
Operating income	112,884	125,831	11.5	55,920	60,986	64,845	6.3	16.0
Profit before tax	49,942	58,631	17.4	24,814	29,286	29,345	0.2	18.3
Net Profit	39,259	44,756	14.0	19,282	22,674	22,082	(2.6)	14.5
<b>Balance sheet</b>								
Total loans	3,539,938	3,877,868	9.5	3,539,938	3,716,153	3,877,868	4.4	9.5
Total deposits	4,142,254	4,257,803	2.8	4,142,254	4,066,894	4,257,803	4.7	2.8
NPLs	60,459	55,454	(8.3)	60,459	54,958	55,454	0.9	(8.3)
Total assets	6,199,690	6,534,708	5.4	6,199,690	6,252,238	6,534,708	4.5	5.4
<b>Key ratios</b>								
ROE (%)	19.1	19.6	0.5	18.4	20.0	18.3	(1.7)	(0.0)
LDR (%)	85.5	91.1	5.6	85.5	91.4	91.1	(0.3)	5.6
NPL ratio (%)	1.71	1.43	(0.28)	1.71	1.48	1.43	(0.05)	(0.28)

Source: Company data, RHB

Forecasts and Valuations	Dec-16	Dec-17	Dec-18F	Dec-19F	Dec-20F
Reported net profit (CNYb)	62	70	79	92	109
Net profit growth (%)	7.6	13.0	13.0	16.3	17.9
Recurring net profit (CNYb)	62	70	79	92	109
Recurring EPS (CNY)	2.46	2.78	3.14	3.65	4.31
BVPS (CNY)	16.0	17.7	20.0	22.7	25.9
DPS (CNY)	0.74	0.84	0.96	1.11	1.31
Recurring P/E (x)	10.7	9.5	8.4	7.2	6.1
P/B (x)	1.66	1.49	1.32	1.16	1.02
Dividend Yield (%)	2.8	3.2	3.6	4.2	5.0
Return on average equity (%)	16.3	16.5	16.7	17.1	17.7
Return on average assets (%)	1.1	1.1	1.2	1.3	1.4
Our vs consensus EPS (adjusted) (%)			(0.4)	0.3	(12.1)

Source: Company data, RHB

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