

13 June 2018

Financial Services | Banks

Banks

Overweight (Maintained)

Slowing Credit Growth Implies Further Easing

Stocks Covered: 9
Ratings (Buy/Neutral/Sell): 6 / 3 / 0
Last 12m Earnings Revision Trend: Positive

We remain **OVERWEIGHT** on the sector, with **ABC** and **BOC** as our **Top Picks**. Despite stable new loans in May, **TSF** growth surprised on the downside, with a **51.2% MoM contraction**. This was led by continued unwinding in off-balance sheet financing and a notable decline in corporate bond issuance. The increasing loan allocation to mortgage points to falling risk appetite for banks, in our view. As such, we anticipate marginal policy easing from the **PBoC** going forward, to cushion the impact from shadow banking clean-up.

A miss in overall credit growth. On 12 Jun, the People's Bank of China (PBoC) released May's monetary statistics. Total social financing (TSF) fell sharply by 51.2% MoM to CNY761bn, or 41.5% below the consensus estimate. Meanwhile, monthly new loans remained largely stable, at CNY1.15trn (down 2.5% MoM) – although this was not able to offset the pullback in other financing channels. Both M2 and deposit growth were subdued, at 8.3% YoY and 8.9 YoY respectively.

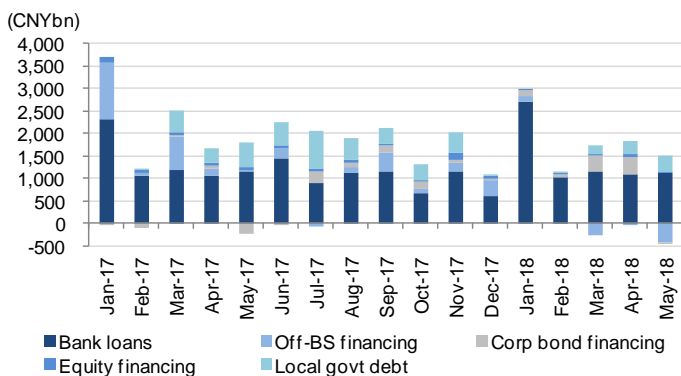
Rising risks from over-tightening. Off-balance sheet financing, including trust loans, entrusted loans, and acceptance bills, recorded the third consecutive monthly contraction, as the asset management rule came into force. Due to the recent surge in yields and credit spreads, net bond issuance declined by CNY43bn in May. As for loan breakdown, growth in mid- and long-term corporate loans was down 8% MoM, likely due to decelerating investments in the real estate and infrastructure sectors. On the flip side, the proportion of mortgages rebounded to 34% of total new loans in May (from 27% in Jan-Apr). The shift in loan mix suggests that banks' risk appetite is declining amid rising credit risks, in our view.

Relaxed deposit deviation to ease funding pressure. On 8 Jun, China Banking and Insurance Regulatory Commission (CBIRC) relaxed the deposit deviation standard (difference between month-end and average daily deposits) to 4% from 3%, and removed the ban on "high-interest deposit taking". These would allow smaller banks to compete for deposits with a certain pricing advantage, so as to ease their deposit growth pressure. It will be, however, achieved at the cost of rising funding expenses and squeezing NIM.

RRR cut only as a matter of time. The PBoC has recently rolled over the Medium-term Lending Facility (MLF) and extended its collateral range. This reflects the central bank's intention to maintain a smooth liquidity condition, and appears to reduce the urgency for a reserve requirement ratio (RRR) cut in the near term. However, we believe a cut is necessary to prepare banks for on-loading existing credits in off-balance sheet channels. Possible triggers include a further slowdown in total financing and deposit growth, and acceleration in bond defaults. We maintain our forecast for 50-100bps RRR cuts in the next six months (for impact to banks, please refer to our 5 Jun report: [RRR Cut Around The Corner?](#)).

Maintain OVERWEIGHT and reiterate our preference for large banks with a stronger deposit base and less off-balance sheet exposure. Top Picks are Agricultural Bank of China (ABC) and Bank of China (BOC).

Breakdown of TSF



Note: Local government debt was not included in official TSF data.
Source: Wind, RHB

YoY growth of TSF and bank loans



Source: Wind, RHB

Company Name	Rating	Price	Target	% Upside (Downside)	P/E (x) Dec-18F	P/B (x) Dec-18F	Yield (%) Dec-18F
Agricultural Bank of China	BUY	HKD4.13	HKD5.80	40.4	5.4	0.7	5.7
Bank of China	BUY	HKD4.19	HKD5.90	40.8	5.6	0.7	5.5
China CITIC Bank	BUY	HKD5.37	HKD6.50	21.0	4.9	0.5	6.3
China Construction Bank	BUY	HKD8.06	HKD10.30	27.8	6.5	0.9	4.7
China Merchants Bank	BUY	HKD32.55	HKD37.50	15.2	8.5	1.3	3.6
ICBC	BUY	HKD6.55	HKD8.50	29.8	6.4	0.8	4.8
Bank of Communications	NEUTRAL	HKD6.41	HKD6.30	(1.7)	5.5	0.6	5.7
China Everbright Bank	NEUTRAL	HKD3.9	HKD4.00	2.6	5.2	0.6	6.0
China Minsheng Banking Corp	NEUTRAL	HKD7.34	HKD7.90	7.6	4.7	0.6	3.1

Source: Company data, RHB

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