

28 May 2018

Financial Services | Banks

Banks

Overweight (Maintained)

Limited Impact From Liquidity Risk Measures

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. CBIRC issued the finalised measures for commercial banks' liquidity risk management, targeting to improve China banks' funding stability and contain risks of maturity mismatch. We expect limited impact to the sector, as the regulator has set out reasonable transition periods while most banks would be able to fulfil the newly introduced requirements. That said, smaller banks will likely see slower balance sheet expansion given their unfavourable liability structure.

Finalised liquidity rule is within expectation. On 25 May, China Banking and Insurance Regulatory Commission (CBIRC) issued the final version of "[Measure for Commercial Banks' Liquidly Risk Management](#)". It was broadly in line with the draft version released on 6 Dec 2017, but set out a longer transition period for certain requirements. The new rule will take effect on 1 July 2018.

Three new quantitative indicators are introduced in the measure: 1) Net stable funding ratio (NSFR), 2) High-quality liquidity asset adequacy ratio (HQLAAR), and 3) Liquidity match ratio (LMR). These, along with the existing two requirements - liquidity ratio and liquidity coverage ratio - make up a comprehensive regulatory framework. In particular, HQLAAR is applicable to banks with assets less than CNY200bn, which are mainly rural commercial banks. Therefore, the measure could minimise the contagion risk from liquidity squeeze in the banking system.

More deposits competition and slower assets growth. The calculation of liquidity requirements favours deposits over short-term interbank funding, and it favours loans and bonds over non-standard credit assets. Therefore, the new rule will further restrict interbank and off-balance sheet businesses. It could also intensify the competition for deposit funding and lead to more rational asset growth of those smaller banks with less solid deposit base.

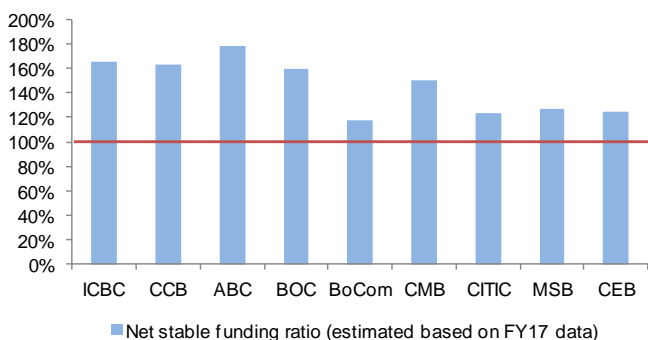
Still prefer large banks. According to our estimates, all nine banks under our coverage are in compliance with the NSFR requirement, but three joint-stock banks might fail to meet the LMR requirement.

Figure 1: Summary of liquidity measures for China banks

| Measures | Requirement | Calculation | Regulatory scope |
|--|-------------------------------|--|------------------------------|
| Net stable funding ratio* | 100% | Available stable fund / required stable fund | Banks with assets > CNY200bn |
| High-quality liquidity asset adequacy ratio* | 80% by 2018, 100% by Jun 2019 | High-quality liquid assets / short term net cash outflow | Banks with assets < CNY200bn |
| Liquidity match ratio* | 100% by 1 Jan 2020 | Weighted funding source / weighted funding usage | All banks |
| Liquidity coverage ratio | 100% by 2018 | High-quality liquid assets / 30-days net cash outflow | Banks with assets > CNY200bn |
| Liquidity ratio | 25% | Current assets / current liabilities | All banks |

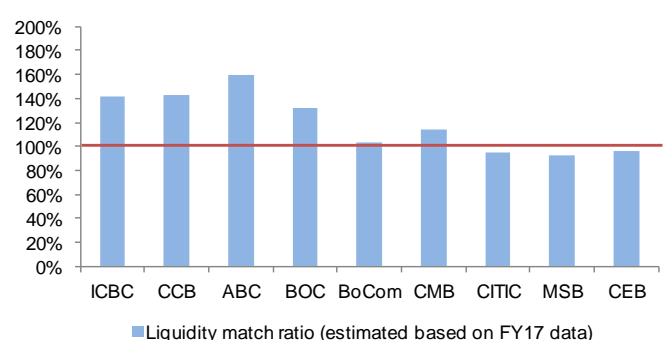
* Measures newly introduced
 Source: CBIRC, RHB

Figure 2: Net stable funding ratio



Source: Company data, RHB

Figure 3: Liquidity match ratio



Source: Company data, 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 | HKD4.14 | HKD5.80 | 40.1 | 5.4 | 0.7 | 5.7 |
| Bank of China | BUY | HKD4.14 | HKD5.90 | 42.5 | 5.5 | 0.6 | 5.6 |
| China CITIC Bank | BUY | HKD5.79 | HKD6.50 | 12.3 | 5.3 | 0.6 | 5.9 |
| China Construction Bank | BUY | HKD8.08 | HKD10.30 | 27.5 | 6.5 | 0.9 | 4.7 |
| China Merchants Bank | BUY | HKD33.00 | HKD37.50 | 13.6 | 8.5 | 1.3 | 3.6 |
| ICBC | BUY | HKD6.62 | HKD8.50 | 28.4 | 6.4 | 0.9 | 4.8 |
| Bank of Communications | NEUTRAL | HKD6.30 | HKD6.30 | - | 5.4 | 0.6 | 5.8 |
| China Everbright Bank | NEUTRAL | HKD3.98 | HKD4.00 | 0.5 | 5.4 | 0.6 | 2.9 |
| China Minsheng Banking Corp | NEUTRAL | HKD7.46 | HKD7.90 | 5.9 | 4.4 | 0.5 | 4.7 |

Source: Company data, RHB

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