

# China / Hong Kong Company Update

## Bank of China

Bloomberg: 3988 HK EQUITY | 601988 CH Equity | Reuters: 3988.HK | 601988.SS

Refer to important disclosures at the end of this report

DBS Group Research . Equity

8 Nov 2023

### H: BUY

Last Traded Price (H) (7 Nov 2023): HK\$2.79 (HSI : 17,670)  
Price Target 12-mth (H): HK\$3.70 (32.6% upside) (Prev HK\$4.00)

### A: HOLD

Last Traded Price (A) (7 Nov 2023): RMB3.89 (CSI300 Index : 3,620)  
Price Target 12-mth (A): RMB4.10 (5.4% upside) (Prev RMB4.80)

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#### What's New

- 9M23 net profit to shareholders increased by 1.6% y-o-y to Rmb175bn, in line with market expectations
- NIM dropped 13bps to 1.64%, supported by higher exposure to foreign currency assets; better than peers
- Asset quality on an improving trend, with NPL ratio dropping 5bps YTD to 1.27%
- Reiterate BUY with TP revised down to HK\$3.7 with negatives largely in price and attractive dividend yield of >10%

### Outperforms peers in terms of revenue growth

#### Investment Thesis

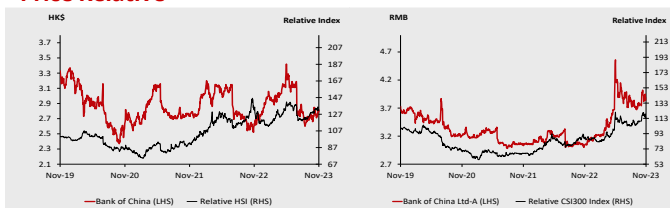
**Largest FX loan exposure to support NIM.** Benefitting from the rising US interest rate cycle, with c.17% of assets in USD/HKD, BOC's margin performance was much better than that of its peers, with 9M23 NIM dropping only 13bps to 1.64%. As such, BOC showed the highest revenue and NII growth among SOE banks in 9M23. However, with this round of US rate hikes coming to an end and the foreign currency deposit rate continuously increasing, we expect such a benefit to gradually come to an end and convert to an NIM downward trend in FY24F.

**2.7% earnings CAGR expected between FY22-25F.** This will be supported by 1) steady NII growth, mainly driven by double-digit y-o-y growth in its loan balance; 2) improving asset quality, as the stabilising property sector would benefit BOC – its NPL ratio for property sector loans was the highest among peers, at c.7.2% in FY22 and reduced to 5.1% in 1H23; and 3) recovering fee income growth in FY23/24F (from -c.11% in FY22), supported by a recovery in global trade and domestic consumption.

**China's economic recovery the key share price driver.** BOC's share price is positively correlated with China's economic performance, which impacts its loan growth, asset quality, and fee income. We expect steady GDP growth of 4.5% y-o-y in China in 2024 to support its share price performance. Any further signals of China's economy stabilising would be a catalyst for the stock.

**Reiterate BUY with TP revised down to HK\$3.7** (vs. HK\$4 previously), based on a DDM model and assuming a 17% cost of equity, 7% ROE, and 1% terminal growth. We have revised down our earnings expectation by 3%-8% for FY23-25F to factor in higher NIM downward pressure in FY24F from the existing mortgage repricing and potential LGFV restructure. Our TP implies a c.0.4x FY24F P/BV (vs. its five-year average of c.0.5x).

#### Price Relative



#### Forecasts and Valuation (H Shares)

| FY Dec (RMB m)            | 2022A   | 2023F   | 2024F   | 2025F   |
|---------------------------|---------|---------|---------|---------|
| Pre-prov. Profit          | 387,943 | 392,404 | 422,139 | 450,412 |
| Pre-prov. Profit Gth (%)  | 2       | 1       | 8       | 7       |
| Pretax Profit             | 284,595 | 284,601 | 295,299 | 308,625 |
| Net Profit                | 214,020 | 214,025 | 222,575 | 233,224 |
| EPS (RMB)                 | 0.73    | 0.73    | 0.76    | 0.79    |
| EPS (HK\$)                | 0.87    | 0.87    | 0.91    | 0.95    |
| EPS Gth (%)               | 4       | 0       | 4       | 5       |
| PE (X)                    | 3.2     | 3.2     | 3.1     | 2.9     |
| DPS (HK\$)                | 0.28    | 0.28    | 0.29    | 0.30    |
| Div Yield (%)             | 10.0    | 10.0    | 10.4    | 10.8    |
| BV Per Share (HK\$)       | 8.37    | 8.99    | 9.63    | 10.31   |
| P/Book Value (x)          | 0.3     | 0.3     | 0.3     | 0.3     |
| ROAE (%)                  | 10.8    | 10.0    | 9.7     | 9.5     |
| ROAE (ex-exceptional) (%) | 10.8    | 10.0    | 9.7     | 9.5     |
| ROA (%)                   | 0.77    | 0.70    | 0.65    | 0.62    |
| Earnings Rev (%)          |         | (3)     | (6)     | (8)     |
| Consensus EPS (RMB)       |         | 0.74    | 0.78    | 0.82    |
| Other Broker Recs:        |         | B:15    | S:0     | H:2     |

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

#### Key Risks

Deteriorating asset quality as well as a substantial slowdown in China's foreign trade.

#### At A Glance

|   |                     |
|---|---------------------|
| Issued Capital - H shares (m shs)       | 83,622              |
| - Non H shrs (m shs)                    | 210,766             |
| H shs as a % of Total                   | 28                  |
| Total Mkt Cap (HK\$/US\$m)              | 1,113,970 / 142,459 |
| Major Shareholders (%)                  |                     |
| Central Huijin Investment Ltd.          | 89.4                |
| Major H Shareholders (As % of H shares) |                     |
| H Shares-Free Float (%)                 | 100.0               |
| 3m Avg. Daily Val. (US\$m)              | 78.86               |
| GICS Industry: Financials / Banks       |                     |

## Bank of China

### WHAT'S NEW

#### 9M23 results in line with expectation

##### 9M23 results in line with market expectations

BOC reported 9M23 net profit to shareholders of c.Rmb175bn, or 1.6% y-o-y growth, in line with market expectations. Revenue increased by 7.1% y-o-y to Rmb471bn, with NII increasing by 3.2% y-o-y to Rmb353bn and fee income up by 3.7% y-o-y to Rmb63bn. 9M23 NIM dropped by 13bps y-o-y to 1.64%. The drop is lower than the market trend, where the rest of the Big Four Banks saw a >30bps y-o-y drop, thanks to BOC's high exposure to high-interest rate, foreign currency assets. NPL ratio dropped by 1bp q-o-q or 5bp YTD to 1.27%, or the lowest among the Big Four Banks. 9M23 annualised ROE dropped by 0.77ppt vs. the same period last year, to 10.37%.

##### Outlook:

1) Optimise overseas asset and liability structure

In 9M23, BOC's RMB NIM dropped by 21bps y-o-y to 1.73% while FX assets' NIM improved by 14bps y-o-y or 4bps q-o-q to 1.11%. Its FX assets, which account for c.20% of its balance sheet, helped ease the overall NIM pressure when the RMB interest rate was low in 2022-23. Looking ahead, we expect the funding costs of FX liabilities to become much higher, and BOC may face some NIM challenges from the FX side as well as in FY24F.

BOC's strategy in FX asset and liability management include 1) making more investments into FX bonds with longer durations when overseas loan demand is subdued; 2) continuously focusing on the China corporation's need to expand their overseas markets and demand for overseas loans; and 3) on the liability side, expect the CASA ratio to be better than the average level of each market.

2) Expect asset quality to be largely stable

BOC keeps seeing improving asset quality YTD. The NPL balance increased by the end of Sep 2023 while the NPL ratio dropped. The increase in NPL was mainly from retail loans and overseas loans. As BOC has already reported an NPL ratio that is higher than that of its peers in the property sector, we don't expect a high risk or any further deterioration of its property exposure. Looking ahead, we expect its asset quality to be largely stable in FY24F, while its overseas exposure may face higher pressure when interest rates stay high.

We have revised down our NIM assumptions by 7/13/14bps respectively for FY23-25 to reflect the impact from existing mortgage repricing and potential LGFV debt restructuring. Our earnings and TP are revised down accordingly. We reiterate BUY for BOC's H-share, as we see the negative expectations are largely in the price now, when its H-share is trading at c.0.3x FY24F P/B with a >10% FY23/24F dividend yield.

#### Company Background

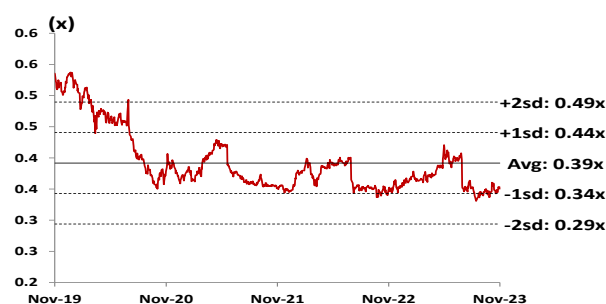
Established in 1912, BOC served as the country's central bank, international exchange bank, and specialised international trade bank from inception to 1949. Due to its positioning as a specialised foreign exchange and trade bank, BOC became responsible for managing China's foreign exchange operations and provided vital support to China's foreign trade development and economic infrastructure. In 1994, BOC was transformed into a wholly state-owned commercial bank. It was dual listed on the HKEX and SSE in 2006. As at end-2022, BOC operated 11,439 outlets, of which 10,908 were in Mainland China.

### Historical PE and PB band

Forward PE band (x)



PB band (x)



Source: Thomson Reuters, DBS HK

## Bank of China

### Key Assumptions

| FY Dec                       | 2021A | 2022A | 2023F | 2024F | 2025F |
|------------------------------|-------|-------|-------|-------|-------|
| NIM (%)                      | 1.75  | 1.76  | 1.62  | 1.56  | 1.55  |
| Loan growth (%)              | 11    | 12    | 14    | 10    | 10    |
| Fee growth (%)               | 8     | (11)  | 4     | 5     | 4     |
| Cost-to-income (%)           | 37.4  | 37.3  | 37.8  | 36.8  | 36.8  |
| Credit cost (%)              | 0.70  | 0.63  | 0.58  | 0.61  | 0.62  |
| Customer Deposits Growth (%) | 8     | 11    | 15    | 12    | 10    |
| Yld. On Earnings Assets (%)  | 3.25  | 3.33  | 3.26  | 3.18  | 3.16  |
| Avg Cost Of Funds (%)        | 1.63  | 1.75  | 1.89  | 1.83  | 1.79  |

Source: Company, DBS HK

### Income Statement (RMB m)

| FY Dec                      | 2021A          | 2022A          | 2023F          | 2024F          | 2025F          |
|-----------------------------|----------------|----------------|----------------|----------------|----------------|
| Net Interest Income         | 425,142        | 460,678        | 468,929        | 500,229        | 542,149        |
| Non-Interest Income         | 180,575        | 158,461        | 161,607        | 167,187        | 170,565        |
| <b>Operating Income</b>     | <b>605,717</b> | <b>619,139</b> | <b>630,536</b> | <b>667,415</b> | <b>712,715</b> |
| Operating Expenses          | (226,355)      | (231,196)      | (238,132)      | (245,276)      | (262,303)      |
| <b>Pre-provision Profit</b> | <b>379,362</b> | <b>387,943</b> | <b>392,404</b> | <b>422,139</b> | <b>450,412</b> |
| Provisions                  | (104,220)      | (103,993)      | (108,448)      | (127,509)      | (142,486)      |
| Associates                  | 1,478          | 645            | 645            | 669            | 699            |
| Exceptionals                | 0              | 0              | 0              | 0              | 0              |
| <b>Pre-tax Profit</b>       | <b>276,620</b> | <b>284,595</b> | <b>284,601</b> | <b>295,299</b> | <b>308,625</b> |
| Taxation                    | (49,281)       | (47,091)       | (47,092)       | (48,862)       | (51,067)       |
| Minority Interests          | (10,780)       | (10,065)       | (10,065)       | (10,444)       | (10,915)       |
| Preference Dividend         | (10,651)       | (13,419)       | (13,419)       | (13,419)       | (13,419)       |
| <b>Net Profit</b>           | <b>205,908</b> | <b>214,020</b> | <b>214,025</b> | <b>222,575</b> | <b>233,224</b> |
| Net Profit bef Except       | 205,908        | 214,020        | 214,025        | 222,575        | 233,224        |

### Growth (%)

|                         |       |      |      |      |      |
|-------------------------|-------|------|------|------|------|
| Net Interest Income Gth | 2.22  | 8.36 | 1.79 | 6.67 | 8.38 |
| Net Profit Gth          | 13.86 | 3.94 | 0.00 | 3.99 | 4.78 |

### Margins, Costs & Efficiency (%)

|                      |      |      |      |      |      |
|----------------------|------|------|------|------|------|
| Spread               | 1.63 | 1.58 | 1.37 | 1.35 | 1.37 |
| Net Interest Margin  | 1.75 | 1.74 | 1.60 | 1.55 | 1.55 |
| Cost-to-Income Ratio | 37.4 | 37.3 | 37.8 | 36.8 | 36.8 |

### Business Mix (%)

|                         |      |      |      |      |      |
|-------------------------|------|------|------|------|------|
| Net Int. Inc / Opg Inc. | 70.2 | 74.4 | 74.4 | 75.0 | 76.1 |
| Non-Int. Inc / Opg inc. | 29.8 | 25.6 | 25.6 | 25.0 | 23.9 |
| Fee Inc / Opg Income    | 13.4 | 11.7 | 12.0 | 11.9 | 11.6 |
| Oth Non-Int Inc/Opg Inc | 16.4 | 13.9 | 13.7 | 13.2 | 12.3 |

### Profitability (%)

|              |      |      |      |     |     |
|--------------|------|------|------|-----|-----|
| ROAE Pre Ex. | 11.2 | 10.8 | 10.0 | 9.7 | 9.5 |
| ROAE         | 11.2 | 10.8 | 10.0 | 9.7 | 9.5 |
| ROA Pre Ex.  | 0.9  | 0.9  | 0.8  | 0.7 | 0.7 |
| ROA          | 0.8  | 0.8  | 0.7  | 0.7 | 0.6 |

Source: Company, DBS HK

## Bank of China

### Quarterly Income Statement (RMB m)

| FY Dec                      | 3Q2022         | 4Q2022         | 1Q2023         | 2Q2023         | 3Q2023         |
|-----------------------------|----------------|----------------|----------------|----------------|----------------|
| Net Interest Income         | 118,601        | 118,697        | 117,334        | 116,658        | 118,980        |
| Non-Interest Income         | 27,595         | 60,724         | 48,883         | 36,832         | 32,245         |
| <b>Operating Income</b>     | <b>146,196</b> | <b>179,421</b> | <b>166,217</b> | <b>153,490</b> | <b>151,225</b> |
| Operating Expenses          | (48,140)       | (93,279)       | (53,647)       | (50,653)       | (52,523)       |
| <b>Pre-Provision Profit</b> | <b>98,056</b>  | <b>86,142</b>  | <b>112,570</b> | <b>102,837</b> | <b>98,702</b>  |
| Provisions                  | (29,999)       | (21,269)       | (33,060)       | (27,521)       | (30,522)       |
| Associates                  | 488            | (23)           | (229)          | 322            | 515            |
| Exceptionals                | 0              | 0              | 0              | 0              | 0              |
| <b>Pretax Profit</b>        | <b>68,545</b>  | <b>64,850</b>  | <b>79,281</b>  | <b>75,638</b>  | <b>68,695</b>  |
| Taxation                    | (11,998)       | (7,448)        | (17,556)       | (9,675)        | (9,880)        |
| Minority Interests          | (3,532)        | (2,143)        | (4,062)        | (3,531)        | (4,052)        |
| <b>Net Profit</b>           | <b>53,015</b>  | <b>51,499</b>  | <b>57,663</b>  | <b>50,169</b>  | <b>54,763</b>  |

### Growth (%)

|                         |      |     |     |       |     |
|-------------------------|------|-----|-----|-------|-----|
| Net Interest Income Gth | 10.6 | 8.8 | 7.0 | 2.6   | 0.3 |
| Net Profit Gth          | 4.5  | 3.0 | 0.5 | (3.8) | 3.3 |

Source: Company, DBS HK

### Balance Sheet (RMB m)

| FY Dec                             | 2021A             | 2022A             | 2023F             | 2024F             | 2025F             |
|------------------------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| Cash/Bank Balance                  | 2,228,726         | 2,313,859         | 2,747,821         | 3,077,559         | 3,385,315         |
| Government Securities              | 0                 | 0                 | 0                 | 0                 | 0                 |
| Inter Bank Assets                  | 1,902,229         | 1,989,160         | 2,088,618         | 2,193,049         | 2,302,701         |
| Total Net Loans & Adv.             | 15,322,484        | 17,116,005        | 19,406,235        | 21,361,832        | 23,409,053        |
| Investment                         | 5,603,029         | 5,822,139         | 6,113,246         | 6,418,908         | 6,739,854         |
| Associates                         | 35,769            | 38,304            | 38,304            | 38,304            | 38,304            |
| Fixed Assets                       | 265,645           | 269,700           | 273,817           | 277,997           | 282,240           |
| Goodwill                           | 39,732            | 41,396            | 41,396            | 41,396            | 41,396            |
| Other Assets                       | 1,324,794         | 1,302,985         | 1,536,597         | 2,450,936         | 3,177,631         |
| <b>Total Assets</b>                | <b>26,722,408</b> | <b>28,893,548</b> | <b>32,246,034</b> | <b>35,859,981</b> | <b>39,376,494</b> |
| Customer Deposits                  | 17,982,468        | 19,911,743        | 22,898,504        | 25,646,325        | 28,210,957        |
| Inter Bank Deposits                | 4,046,063         | 3,622,516         | 3,984,768         | 4,383,244         | 4,821,569         |
| Debts/Borrowings                   | 1,388,678         | 1,540,935         | 1,240,927         | 1,365,019         | 1,501,521         |
| Others                             | 954,646           | 1,255,053         | 1,401,404         | 1,581,769         | 1,787,264         |
| Minorities                         | 125,400           | 139,328           | 145,083           | 150,563           | 156,327           |
| Shareholders' Funds                | 2,225,153         | 2,423,973         | 2,575,348         | 2,733,061         | 2,898,856         |
| <b>Total Liab&amp; S/H's Funds</b> | <b>26,722,408</b> | <b>28,893,548</b> | <b>32,246,034</b> | <b>35,859,981</b> | <b>39,376,494</b> |

Source: Company, DBS HK

## Bank of China

### Financial Stability Measures (%)

| FY Dec                         | 2021A | 2022A | 2023F | 2024F | 2025F |
|--------------------------------|-------|-------|-------|-------|-------|
| <b>Balance Sheet Structure</b> |       |       |       |       |       |
| Loan-to-Deposit Ratio          | 87.2  | 87.9  | 86.9  | 85.5  | 85.2  |
| Net Loans / Total Assets       | 57.3  | 59.2  | 60.2  | 59.6  | 59.4  |
| Investment / Total Assets      | 21.0  | 20.2  | 19.0  | 17.9  | 17.1  |
| Cust. Dep./Int. Bear. Liab.    | 77.5  | 78.1  | 80.0  | 80.8  | 80.8  |
| Interbank Dep / Int. Bear.     | 16.7  | 15.9  | 14.8  | 14.7  | 14.8  |
| <b>Asset Quality</b>           |       |       |       |       |       |
| NPL / Total Gross Loans        | 1.3   | 1.3   | 1.3   | 1.3   | 1.3   |
| NPL / Total Assets             | 0.8   | 0.8   | 0.8   | 0.8   | 0.8   |
| Loan Loss Reserve Coverage     | 168.8 | 168.9 | 190.8 | 198.4 | 207.5 |
| Provision Charge-Off Rate      | 0.7   | 0.6   | 0.5   | 0.6   | 0.6   |
| <b>Capital Strength</b>        |       |       |       |       |       |
| Total CAR                      | 16.5  | 17.5  | 17.2  | 16.4  | 15.8  |
| Tier-1 CAR                     | 11.3  | 11.8  | 11.8  | 11.4  | 11.1  |

Source: Company, DBS HK

**Bank of China**

**H Share - Target Price & Ratings 12-mth History**



| S.No. | Date      | Closing Price | Target Price | Rating |
|-------|-----------|---------------|--------------|--------|
| 1     | 12-Dec-22 | HK\$2.75      | HK\$3.30     | BUY    |
| 2     | 9-May-23  | HK\$3.42      | HK\$4.00     | BUY    |

Source: DBS HK

Analyst: Manyi Lu

Ken Shih

Iris GAO

**A Share - Target Price & Ratings 12-mth History**



| S.No. | Date      | Closing Price | 12-mth Target Price | Rating |
|-------|-----------|---------------|---------------------|--------|
| 1:    | 12-Dec-22 | RMB3.16       | RMB3.60             | Buy    |
| 2:    | 9-May-23  | RMB4.49       | RMB4.80             | Hold   |

Source: DBS HK

Analyst: Manyi Lu

Ken Shih

Iris GAO

DBS HK recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

**HOLD** (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

**FULLY VALUED** (negative total return, i.e., > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

\*Share price appreciation + dividends

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Sources for all charts and tables are DBS HK unless otherwise specified.

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## Bank of China

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