

EARNINGS REVIEW

**Bank of Chongqing (1963.HK)**

Neutral

Equity Research

**In line with expectations; strong PPOP/NSCA offset higher NPLs**

**What surprised us**

BOCQ reported 2014 NPAT of Rmb2.8bn, up 25% yoy, in line with GHe and 4% higher than Bloomberg consensus. PPOP beat GHe by 6%, offsetting the 16% higher-than-expected provisions.

**Key positives:** 1) FY14 NII growth was a robust 20%, at 102% of GHe, on fast asset expansion. Loan yield edged up hoh despite policy rate cut, likely on good SME pricing; 2) 2H fees rose 64% on strong bankcard, wealth management and advisory businesses; 3) Cost-income ratio dropped 5pp yoy, mainly on good SG&A cost control.

**Key negatives:** 1) NIM shrank by 16bps hoh and FY14 NIM was 13bps lower than GHe largely on continued rise in deposit funding cost and fast asset expansion; 2) NSCA (Non-Standard Credit Assets) investments grew 34% hoh, pushing up adj. L/D to 94%; 3) 2H NPL formation rate rose to 85bps vs. 54bps in 1H, and SML ratio rose by 1pp, partly on corporate borrowers/guarantee companies in Sichuan, as well as coal projects in Guizhou. That said, asset quality of its SMEs/corporate borrowers in Chongqing remained relatively stable. 2H 1day+ overdues formation rate accelerated to 218bps but this partly reflected the adoption of a stricter definition (1-day interest or principal overdues vs. the prior 1-day principal overdues). Its 90+ overdues formation rate was much softer at 81bps.

**What to do with the stock**

We view BOCQ as a fast-growing bank, but with asset quality pressure outside Chongqing (c.20%+ of loans) and relatively high NSCA investments. We fine tune 2015E/16E NPAT by -1%/-2%, and retain our Neutral rating and 12-m RIM-based TP of HK\$7.20. We introduce 2017 estimates. Risks: NPL rise/decrease.

**BOCQ 2014 results snapshot**

|                          | 1H13  | 2H13  | 1H14  | 2H14  |
|--------------------------|-------|-------|-------|-------|
| <b>NIM</b>               | 2.90% | 2.76% | 2.78% | 2.62% |
| <b>Credit costs</b>      | 0.24% | 0.96% | 0.48% | 0.93% |
| <b>Loan/Deposit</b>      | 61%   | 61%   | 59%   | 63%   |
| <b>Cost income ratio</b> | 34%   | 46%   | 33%   | 42%   |

Source: Company data

**INVESTMENT LIST MEMBERSHIP**

Neutral

**Coverage View: Neutral**

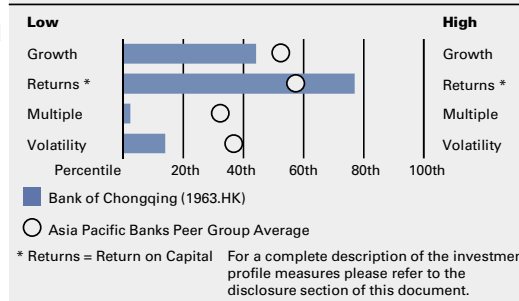
**Ning Ma**  
+86(10)6627-3063 ning.ma@ghsl.cn Beijing Gao Hua Securities Company Limited

**Jessica Wu**  
+86(10)6627-3487 jessica.wu@ghsl.cn Beijing Gao Hua Securities Company Limited

**Nan Li, CFA**  
+86(10)6627-3021 nan.li@ghsl.cn Beijing Gao Hua Securities Company Limited

**Yvonne Qian**  
+86(10)6627-3463 yvonne.qian@ghsl.cn Beijing Gao Hua Securities Company Limited

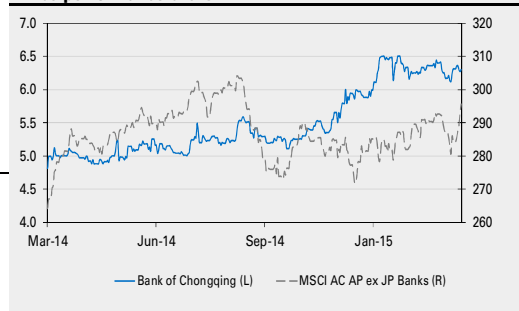
**Investment Profile**



| Key data                       | Current            |
|--------------------------------|--------------------|
| Price (HK\$)                   | 6.30               |
| 12 month price target (HK\$)   | 7.20               |
| Market cap (HK\$ mn / US\$ mn) | 17,042.9 / 2,196.5 |
| Foreign ownership (%)          | --                 |

|                      | 12/14       | 12/15E      | 12/16E      | 12/17E      |
|----------------------|-------------|-------------|-------------|-------------|
| <b>EPS (Rmb) New</b> | <b>1.05</b> | <b>1.17</b> | <b>1.28</b> | <b>1.41</b> |
| EPS revision (%)     | 0.3         | (0.6)       | (2.2)       | --          |
| P/B (X)              | 0.7         | 0.7         | 0.6         | 0.6         |
| P/E (X)              | 3.9         | 4.3         | 3.9         | 3.6         |
| Dividend yield (%)   | 6.6         | 5.8         | 6.4         | 7.0         |
| P/PPOP (X)           | 2.9         | 2.6         | 2.4         | 2.2         |
| PPOP growth (%)      | 32.8        | 10.7        | 11.1        | 8.5         |
| Provision ROA (%)    | 1.9         | 1.7         | 1.7         | 1.6         |
| Credit cost (%)      | 0.8         | 0.9         | 0.9         | 0.9         |
| ROA (%)              | 1.17        | 1.07        | 1.03        | 1.01        |
| ROE (%)              | 19.2        | 18.5        | 17.7        | 17.0        |

**Price performance chart**



| Share price performance (%)    | 3 month | 6 month | 12 month |
|--------------------------------|---------|---------|----------|
| Absolute                       | 5.5     | 16.5    | 31.0     |
| Rel. to MSCI AC AP ex JP Banks | (0.7)   | 13.6    | 17.0     |

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 3/20/2015 close.

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# Bank of Chongqing: Summary Financials

| Profit model (Rmb mn)              | 12/14          | 12/15E         | 12/16E         | 12/17E         | Balance sheet (Rmb mn)               | 12/14            | 12/15E           | 12/16E           | 12/17E           |
|------------------------------------|----------------|----------------|----------------|----------------|--------------------------------------|------------------|------------------|------------------|------------------|
| Net interest income                | 6,231.7        | 7,010.2        | 7,653.9        | 8,256.0        | Gross loans                          | 106,448.9        | 122,097.8        | 137,281.1        | 153,708.3        |
| Non-interest income                | 1,251.3        | 1,254.2        | 1,482.5        | 1,669.3        | NPLs                                 | 732.0            | 1,030.0          | 1,371.9          | 1,756.3          |
| Operating revenue                  | 7,483.0        | 8,264.4        | 9,136.4        | 9,925.4        | Loan loss reserves                   | 2,334.1          | 2,944.1          | 3,661.0          | 4,349.4          |
| Non-interest expense               | (2,805.3)      | (3,088.2)      | (3,385.9)      | (3,688.3)      | <b>Total interest earning assets</b> | <b>270,001.2</b> | <b>309,005.0</b> | <b>348,528.1</b> | <b>391,745.7</b> |
| Provision operating profit         | 4,677.7        | 5,176.2        | 5,750.5        | 6,237.1        | Other non-interest earning assets    | 4,529.9          | 8,100.2          | 9,035.2          | 7,052.6          |
| Total provision charge             | (889.6)        | (1,095.1)      | (1,273.5)      | (1,329.6)      | <b>Total assets</b>                  | <b>274,531.1</b> | <b>317,105.2</b> | <b>357,563.4</b> | <b>398,798.2</b> |
| Associates                         | 2.0            | 2.0            | 2.0            | 2.0            | Customer deposits                    | 167,932.4        | 194,801.6        | 222,073.9        | 248,722.7        |
| Pretax profit                      | 3,790.2        | 4,083.1        | 4,479.0        | 4,909.5        | Total interest-bearing liabilities   | 253,353.3        | 292,467.8        | 329,128.1        | 366,103.9        |
| Tax                                | (963.2)        | (920.9)        | (1,006.8)      | (1,097.6)      | <b>Total equity</b>                  | <b>15,903.0</b>  | <b>18,329.4</b>  | <b>21,011.0</b>  | <b>23,954.9</b>  |
| Minorities                         | --             | --             | --             | --             | <b>CAMEL ratios (%)</b>              | <b>12/14</b>     | <b>12/15E</b>    | <b>12/16E</b>    | <b>12/17E</b>    |
| <b>Net profit</b>                  | <b>2,827.1</b> | <b>3,162.2</b> | <b>3,472.2</b> | <b>3,811.9</b> | C: Tier 1 capital ratio              | 9.6              | 9.4              | 9.3              | 9.2              |
| Dividends                          | 735.8          | 790.6          | 868.0          | 953.0          | C: Equity/loans                      | 15.3             | 15.4             | 15.7             | 16.0             |
| Dividends payout (%)               | 26.0           | 25.0           | 25.0           | 25.0           | C: Equity/assets                     | 5.8              | 5.8              | 5.9              | 6.0              |
| <b>Earnings growth drivers (%)</b> | <b>12/14</b>   | <b>12/15E</b>  | <b>12/16E</b>  | <b>12/17E</b>  | A: NPL ratio                         | 0.7              | 0.8              | 1.0              | 1.1              |
| Net interest margin                | 2.61           | 2.39           | 2.28           | 2.19           | A: Loan loss reserves/NPLs           | 318.9            | 285.8            | 266.9            | 247.6            |
| Provision charge/total loans       | 0.85           | 0.92           | 0.95           | 0.89           | E: Net interest margin               | 2.61             | 2.39             | 2.28             | 2.19             |
| <b>YoY Growth (%)</b>              |                |                |                |                | E: Non int inc/oper revenues         | 16.72            | 15.18            | 16.23            | 16.82            |
| Customer deposits                  | 10.2           | 15.2           | 13.3           | 11.3           | E: Cost-income ratio                 | 37.5             | 37.4             | 37.1             | 37.2             |
| Loans                              | 17.5           | 14.4           | 12.1           | 11.8           | E: ROAA                              | 1.17             | 1.07             | 1.03             | 1.01             |
| Net interest income                | 20.3           | 12.5           | 9.2            | 7.9            | L: Loan/deposit ratio                | 62.0             | 61.2             | 60.2             | 60.1             |
| Fee income                         | 41.0           | 29.8           | 19.4           | 13.3           | <b>Loan portfolio (%)</b>            | <b>12/14</b>     | <b>12/15E</b>    | <b>12/16E</b>    | <b>12/17E</b>    |
| Non-interest income                | 79.8           | 0.2            | 18.2           | 12.6           | Commercial & corporate               | 64.8             | 62.8             | 61.4             | 59.8             |
| Operating revenue                  | 27.4           | 10.4           | 10.6           | 8.6            | Mortgages/home loans                 | NM               | NM               | NM               | NM               |
| Operating expenses                 | (19.3)         | (10.1)         | (9.6)          | (8.9)          | Consumer                             | 30.6             | 33.1             | 34.7             | 36.6             |
| <b>Provision operating profit</b>  | <b>32.8</b>    | <b>10.7</b>    | <b>11.1</b>    | <b>8.5</b>     | <b>Valuation (current price)</b>     | <b>12/14</b>     | <b>12/15E</b>    | <b>12/16E</b>    | <b>12/17E</b>    |
| Provision charges                  | 36.7           | 25.9           | 16.5           | 1.5            | P/E basic (X)                        | 3.9              | 4.3              | 3.9              | 3.6              |
| Pretax profit                      | 26.8           | 7.7            | 9.7            | 9.6            | P/B (X)                              | 0.70             | 0.74             | 0.65             | 0.57             |
| Net profit                         | 25.0           | 11.9           | 9.8            | 9.8            | P/PPOP (X)                           | 2.9              | 2.6              | 2.4              | 2.2              |
| EPS                                | 25.0           | 11.9           | 9.8            | 9.8            | Dividend yield (%)                   | 6.6              | 5.8              | 6.4              | 7.0              |
| DPS                                | 21.4           | 7.4            | 9.8            | 9.8            | EPS, basic (Rmb)                     | 1.05             | 1.17             | 1.28             | 1.41             |
| <b>Market dimensions</b>           | <b>12/14</b>   | <b>12/15E</b>  | <b>12/16E</b>  | <b>12/17E</b>  | EPS, fully-diluted (Rmb)             | 1.05             | 1.17             | 1.28             | 1.41             |
| No of branches                     | --             | --             | --             | --             | EPS, basic growth (%)                | 25.0             | 11.9             | 9.8              | 9.8              |
| No of staff (000)                  | --             | --             | --             | --             | EPS, fully diluted growth (%)        | 25.0             | 11.9             | 9.8              | 9.8              |
| Revenues/staff (US\$)              | NM             | NM             | NM             | NM             | BVPS (Rmb)                           | 5.88             | 6.78             | 7.77             | 8.86             |
| Net profit/staff (US\$)            | NM             | NM             | NM             | NM             | DPS (Rmb)                            | 0.27             | 0.29             | 0.32             | 0.35             |
| <b>DuPont analysis (%)</b>         | <b>12/14</b>   | <b>12/15E</b>  | <b>12/16E</b>  | <b>12/17E</b>  |                                      |                  |                  |                  |                  |
| ROE                                | 19.2           | 18.5           | 17.7           | 17.0           |                                      |                  |                  |                  |                  |
| x leverage                         | 6.1            | 5.8            | 5.8            | 5.9            |                                      |                  |                  |                  |                  |
| =ROA                               | 1.17           | 1.07           | 1.03           | 1.01           |                                      |                  |                  |                  |                  |
| <b>% of assets</b>                 | <b>12/14</b>   | <b>12/15E</b>  | <b>12/16E</b>  | <b>12/17E</b>  |                                      |                  |                  |                  |                  |
| Net interest income                | 2.59           | 2.37           | 2.27           | 2.18           |                                      |                  |                  |                  |                  |
| Fee income                         | 0.38           | 0.40           | 0.42           | 0.42           |                                      |                  |                  |                  |                  |
| Non-interest income                | 0.52           | 0.42           | 0.44           | 0.44           |                                      |                  |                  |                  |                  |
| Operating revenue                  | 3.11           | 2.79           | 2.71           | 2.62           |                                      |                  |                  |                  |                  |
| Operating expenses                 | 1.17           | 1.04           | 1.00           | 0.98           |                                      |                  |                  |                  |                  |
| Provision operating profit         | 1.94           | 1.75           | 1.70           | 1.65           |                                      |                  |                  |                  |                  |
| Loan loss provisions               | 0.30           | 0.31           | 0.32           | 0.29           |                                      |                  |                  |                  |                  |
| Pretax profits                     | 1.57           | 1.38           | 1.33           | 1.30           |                                      |                  |                  |                  |                  |
| Taxes                              | 0.40           | 0.31           | 0.30           | 0.29           |                                      |                  |                  |                  |                  |

Note: Last actual year may include reported and estimated data.

Source: Company data, Goldman Sachs Research estimates.

## Analyst Contributors

### Ning Ma

ning.ma@ghsl.cn

### Jessica Wu

jessica.wu@ghsl.cn

### Nan Li, CFA

nan.li@ghsl.cn

### Yvonne Qian

yvonne.qian@ghsl.cn

**Exhibit 1: BOCQ's FY14 NPAT rose 25% yoy. NII/fee/CIR were strong, offsetting higher-than-expected provisions; Provision/loan ratio and Adj. L/D rose**

| RMB mn                               | Annual results |                |                 |                       | Half year results |                |                 |                 |
|--------------------------------------|----------------|----------------|-----------------|-----------------------|-------------------|----------------|-----------------|-----------------|
|                                      | 2013           | 2014           | YoY (%)<br>2014 | FY14A<br>vs.<br>FY14E | 1H14              | 2H14           | HoH (%)<br>2H14 | YoY (%)<br>2H14 |
| <b>Income statement</b>              |                |                |                 |                       |                   |                |                 |                 |
| Net interest income                  | 5,179          | 6,232          | 20              | 102                   | 2,983             | 3,248          | 9               | 20              |
| Non-interest income                  | 696            | 1,251          | 80              | 125                   | 624               | 627            | 0               | 186             |
| Net fee income                       | 645            | 909            | 41              | 109                   | 455               | 454            | (0)             | 64              |
| Gross fee income                     | 703            | 975            | 39              | 109                   | 482               | 493            | 2               | 57              |
| Fee expense                          | (50)           | (66)           | 33              | 111                   | (27)              | (39)           | 41              | 44              |
| Other non-interest income            | 51             | 343            | 568             | 198                   | 169               | 173            | 2               | (397)           |
| <b>Total operating revenue</b>       | <b>5,874</b>   | <b>7,483</b>   | <b>27</b>       | <b>105</b>            | <b>3,608</b>      | <b>3,875</b>   | <b>7</b>        | <b>33</b>       |
| <b>Operating expense</b>             | <b>(2,351)</b> | <b>(2,805)</b> | <b>19</b>       | <b>105</b>            | <b>(1,175)</b>    | <b>(1,611)</b> | <b>37</b>       | <b>19</b>       |
| <b>Preprovision operating profit</b> | <b>3,523</b>   | <b>4,678</b>   | <b>33</b>       | <b>106</b>            | <b>2,433</b>      | <b>2,245</b>   | <b>(8)</b>      | <b>43</b>       |
| <b>Total provisions</b>              | <b>(536)</b>   | <b>(890)</b>   | <b>66</b>       | <b>116</b>            | <b>(238)</b>      | <b>(651)</b>   | <b>174</b>      | <b>50</b>       |
| <b>Loan Loss Provisions</b>          | <b>(536)</b>   | <b>(732)</b>   | <b>37</b>       | <b>96</b>             | <b>(238)</b>      | <b>(494)</b>   | <b>107</b>      | <b>14</b>       |
| <b>Provision for other assets</b>    | <b>0</b>       | <b>(158)</b>   | <b>NM</b>       | <b>NM</b>             | <b></b>           | <b>(158)</b>   | <b>NM</b>       | <b>NM</b>       |
| Pretax profits                       | 2,989          | 3,790          | 27              | 103                   | 2,196             | 1,595          | (27)            | 41              |
| Tax                                  | (728)          | (963)          | 32              | 114                   | (530)             | (433)          | (18)            | 53              |
| <b>Net profits</b>                   | <b>2,261</b>   | <b>2,827</b>   | <b>25</b>       | <b>100</b>            | <b>1,666</b>      | <b>1,161</b>   | <b>(30)</b>     | <b>37</b>       |
| <b>Balance sheet</b>                 |                |                |                 |                       |                   |                |                 |                 |
| Total assets                         | 206,787        | 274,531        | 33              | 113                   | 226,176           | 274,531        | 21              | 33              |
| Gross loans                          | 90,504         | 106,449        | 18              | 99                    | 99,524            | 106,449        | 7               | 18              |
| Impaired loans                       | 355            | 732            | 106             | 134                   | 535               | 732            | 37              | 106             |
| Loan loss reserves                   | (1,866)        | (2,334)        | 25              | 99                    | (2,089)           | (2,334)        | 12              | 25              |
| Customer deposits                    | 148,801        | 167,932        | 13              | 94                    | 168,002           | 167,932        | (0)             | 13              |
| Total Equity                         | 13,479         | 15,903         | 18              | 101                   | 14,618            | 15,903         | 9               | 18              |
| NSCA investments                     | 33,317         | 50,824         | 53              | NM                    | 37,840            | 50,824         | 34              | 53              |
| Total earning assets                 | 204,911        | 272,335        | 33              | 113                   | 224,306           | 272,335        | 21              | 33              |
| <b>Camel ratios %</b>                |                |                |                 |                       |                   |                |                 |                 |
| <b>Capital adequacy</b>              |                |                |                 |                       |                   |                |                 |                 |
| Equity/assets                        | 6.52           | 5.79           | -0.7            | (0.66)                | 6.46              | 5.79           | (0.7)           | (0.7)           |
| Equity/loans                         | 14.89          | 14.94          | 0.0             | 0.38                  | 14.69             | 14.94          | 0.3             | 0.0             |
| <b>Asset quality</b>                 |                |                |                 |                       |                   |                |                 |                 |
| NPL ratio                            | 0.39           | 0.69           | 0.30            | 0.18                  | 0.54              | 0.69           | 0.15            | 0.30            |
| LLR/NPLs                             | 526.4          | 318.9          | (207.5)         | (112.9)               | 390.4             | 318.9          | (71.5)          | (207.5)         |
| Credit costs                         | 0.59           | 0.69           | 0.10            | (0.02)                | 0.48              | 0.93           | 0.45            | (0.03)          |
| LLR/loans                            | 2.06           | 2.19           | 0.13            | 0.01                  | 2.10              | 2.19           | 0.09            | 0.13            |
| <b>Earnings</b>                      |                |                |                 |                       |                   |                |                 |                 |
| Net interest margin                  | 2.88           | 2.61           | -0.27           | (0.13)                | 2.78              | 2.62           | (0.16)          | (0.15)          |
| Non-int income/oper revenue          | 11.85          | 16.72          | 4.88            | 2.59                  | 17.30             | 16.18          | (1.12)          | 8.68            |
| Cost-income ratio                    | 40.03          | 37.49          | -2.54           | (0.26)                | 32.56             | 41.56          | 9.00            | (4.87)          |
| <b>Preprov operating ROAA</b>        | <b>1.94</b>    | <b>1.94</b>    | <b>0.00</b>     | <b>(0.02)</b>         | <b>2.25</b>       | <b>1.79</b>    | <b>(0.45)</b>   | <b>0.21</b>     |
| <b>ROA</b>                           | <b>1.25</b>    | <b>1.17</b>    | <b>-0.07</b>    | <b>(0.08)</b>         | <b>1.54</b>       | <b>0.93</b>    | <b>(0.61)</b>   | <b>0.07</b>     |
| <b>ROE</b>                           | <b>20.80</b>   | <b>19.24</b>   | <b>-1.56</b>    | <b>(0.08)</b>         | <b>23.72</b>      | <b>15.22</b>   | <b>(8.50)</b>   | <b>0.44</b>     |
| <b>Liquidity</b>                     |                |                |                 |                       |                   |                |                 |                 |
| Loan/deposits                        | 60.8           | 63.4           | 2.6             | 2.8                   | 59.2              | 63.4           | 4.1             | 2.6             |
| Adjusted loan/deposits               | 83.2           | 93.7           | 10.4            | NM                    | 81.8              | 93.7           | 11.9            | 10.4            |
| Effective tax rates (%)              | 24.4           | 25.4           | 1.1             | 1.81                  | 24.13             | 27.18          | 3.1             | 2.2             |
| <b>Averages</b>                      |                |                |                 |                       |                   |                |                 |                 |
| Average assets                       | 181,475        | 240,659        | 33              | 107                   | 216,481           | 250,354        | 16              | 27              |
| Average equity                       | 10,869         | 14,691         | 35              | 101                   | 14,049            | 15,261         | 9               | 33              |

Source: Company data, Gao Hua Securities Research

# Disclosure Appendix

## Reg AC

We, Ning Ma, Jessica Wu, Nan Li, CFA and Yvonne Qian, hereby certify that all of the views expressed in this report accurately reflect our personal views about the subject company or companies and its or their securities. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

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The Goldman Sachs Investment Profile provides investment context for a security by comparing key attributes of that security to its peer group and market. The four key attributes depicted are: growth, returns, multiple and volatility. Growth, returns and multiple are indexed based on composites of several methodologies to determine the stocks percentile ranking within the region's coverage universe.

The precise calculation of each metric may vary depending on the fiscal year, industry and region but the standard approach is as follows:

**Growth** is a composite of next year's estimate over current year's estimate, e.g. EPS, EBITDA, Revenue. **Return** is a year one prospective aggregate of various return on capital measures, e.g. CROCI, ROACE, and ROE. **Multiple** is a composite of one-year forward valuation ratios, e.g. P/E, dividend yield, EV/FCF, EV/EBITDA, EV/DACF, Price/Book. **Volatility** is measured as trailing twelve-month volatility adjusted for dividends.

## Quantum

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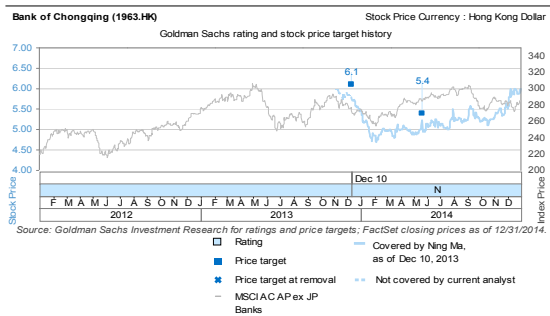
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