

China Galaxy Securities (6881 HK)

A brokerage-driven year; IB & AM weakness retained

CGS reported FY20 net profit of RMB 7.2bn, up 39% YoY, in-line with prelim results. Operating revenue increased 23% YoY to RMB 17.6bn, mainly boosted by brokerage, net interest income and investment banking, while prop-trading and asset management remained subdued. We think CGS's weak franchise in IB and AM makes it least favorable in enjoying capital market reforms among covered brokers and softening ADT could further pressure its top-line growth. We cut TP to HK\$ 5.50 and **maintain HOLD**, though its near-trough valuation (0.49x forward P/B) and >5% yield is attractive for short-term investment.

- **Results positives:** 1) **Investment banking fees** surged 98% YoY, thanks to >360% growth of equity underwriting amount (including 5 IPOs vs. 1 in 2019) and 68% growth of debt underwriting amount in domestic market. The strong growth was mainly on low base and IB still accounted for only 5% of CGS's FY20 operating income. 2) **Net interest income** +20% YoY, primarily boosted by 61% YoY growth of margin account (vs. 47% YoY of market margin financing balance) and higher interest income from bond investment, offsetting a 18% YoY decline in reverse repo balance. Meanwhile, CGS's financing costs greatly lowered due to easing monetary environment and more short-term funding (balance +85% YoY). 3) **Brokerage** +52% YoY on robust A-share stock market activity, of which we estimate domestic commission was up 42% YoY, slightly lower than industry income growth of +47%, suggesting possible market share loss; but this was offset by strong agency sales of financial products (+132% YoY) and future trading commissions (+45% YoY).
- **Results negatives:** 1) **Asset management fees** -7% YoY (vs. industry +9% YoY), as AUM continued to contract 28% YoY to reduce the scale of "channel business", though the Company's active management capability was gradually improved, as actively managed AUM accounted for 45% of its total AUM in 4Q20 vs. 35% in 4Q19, according to AMAC. 2) **Prop-trading gains** -1% YoY and cal. investment yield dropped 1.3ppt YoY despite the bullish A-share market. The Company explained that this was due to less recognition of "strategic investment gains" in FY20. 3) **Impairment losses** +21% YoY, mostly booked in 2H20 for SPLs and bond investment.
- **Cut TP to HK\$5.50; Maintain HOLD.** We maintain FY21E-22E earnings forecast for CGS largely unchanged but cut TP to HK\$ 5.50 on higher COE assumption (11.3% vs. prev. 10.1%). CGS now trades at 0.49x 1-year forward P/B or at its historical average -1SD. The near-trough valuation and >5% yield provide a reason for short-term investment, in our view, but we are cautious on its long-term growth prospectus.

Earnings Summary

(YE 31 Dec)	FY19A	FY20A	FY21E	FY22E	FY23E
Adj. op. revenue (RMB mn)	14,320	17,615	17,507	19,113	20,361
Net profit (RMB mn)	5,228	7,244	6,984	7,707	8,339
EPS (RMB)	0.52	0.71	0.69	0.76	0.82
EPS CHG (%)	81	39	(4)	10	8
Consensus EPS (RMB)	N/A	N/A	0.75	0.79	N/A
P/E (x)	7.9	5.7	5.9	5.3	4.9
P/B (x)	0.58	0.51	0.48	0.45	0.42
Yield (%)	3.9	5.4	5.1	5.6	6.1
ROE (%)	7.6	9.5	8.3	8.7	8.8
Adj. financial leverage (x)	3.3	4.3	4.3	4.3	4.2

Source: Company data, Bloomberg, CMBIS estimates

HOLD (Maintain)

Target Price **HK\$ 5.50**
 (Previous TP **HK\$ 6.30**)
 Up/Downside **+12.2%**
 Current Price **HK\$ 4.90**

China Brokerage Sector

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Stock Data

Mkt Cap (HK\$ mn)	98,214
Avg 3 mths t/o (HK\$ mn)	94.66
52w High/Low (HK\$)	6.34/3.57
Total Issued Shares (mn)	3,691 (H)
	6,446 (A)

Source: Wind

Shareholding Structure

China Galaxy Financial Holdings Limited	51.17%
Wenze Int'l Investment Ltd.	2.17%

Source: Company data

Share Performance

	Absolute	Relative
1-mth	-4.2%	-2.0%
3-mth	2.0%	-5.3%
6-mth	5.8%	-12.4%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Ernst & Young

Related Reports

1. "Optimism & reform suggest more earnings upsides" – 9 Jul 2020
2. "Reform acceleration could drive further divergence" – 12 May 2020
3. "Another brokerage-driven quarter" 28 Apr 2020
4. "Resilient Mar set for better-than-expected 1Q20E results" – 14 Apr 2020
5. "Fee incomes weaker than expected in 4Q19" – 30 Mar 2020

Figure 1: CGS's quarterly results summary

(RMB mn)										
I/S	4Q19	1Q20	2Q20	3Q20	4Q20	QoQ	YoY	FY19	FY20	YoY
Net fees and commissions	1,242	1,988	1,692	2,837	2,004	-29%	61%	5,773	8,521	48%
Brokerage	960	1,682	1,372	2,561	1,305	-49%	36%	4,551	6,921	52%
Investment banking	78	131	141	373	305	-18%	292%	480	950	98%
Asset Management	145	154	156	133	149	12%	3%	634	592	-7%
Net interest income	950	963	981	1,206	1,028	-15%	8%	3,492	4,178	20%
Prop trading gains	1,545	1,635	1,293	964	936	-3%	-39%	4,897	4,828	-1%
Adj. op. revenue	3,823	4,582	3,918	5,039	4,076	-19%	7%	14,320	17,615	23%
Adj. op. expenses	(1,756)	(2,153)	(1,706)	(2,338)	(1,765)	-25%	1%	(7,079)	(7,962)	12%
PPoP	2,067	2,428	2,212	2,701	2,311	-14%	12%	7,241	9,652	33%
Provision	(356)	(145)	85	(73)	(364)	400%	2%	(410)	(496)	21%
Pre-tax profit	1,711	2,284	2,298	2,629	1,947	-26%	14%	6,830	9,157	34%
Income tax expense	(340)	(503)	(482)	(516)	(343)	-34%	1%	(1,580)	(1,845)	17%
Net profit	1,368	1,754	1,799	2,098	1,593	-24%	16%	5,228	7,244	39%
B/S	4Q19	1Q20	2Q20	3Q20	4Q20	QoQ	YoY	FY19	FY20	YoY
Margin accounts	58,721	58,260	62,043	86,423	82,018	-5%	40%	51,060	82,018	61%
Reverse repos	30,438	28,650	28,281	26,567	31,863	20%	5%	38,982	31,863	-18%
Financial investment	121,437	147,640	154,499	172,204	184,435	7%	52%	108,275	184,435	70%
Borrowings and bonds	150,491	181,113	180,445	224,119	225,680	1%	50%	99,039	225,680	128%
Total shareholders' equity	70,896	72,772	72,820	74,400	81,255	9%	15%	67,966	81,255	20%
Ratios	4Q19	1Q20	2Q20	3Q20	4Q20	QoQ	YoY	FY19	FY20	YoY
ROE	7.8%	9.8%	9.9%	11.4%	8.2%	-3.2ppt	0.4ppt	7.6%	9.5%	1.9ppt
ROA	1.8%	2.1%	1.9%	2.1%	1.5%	-0.6ppt	-0.3ppt	1.8%	1.9%	0.1ppt
Leverage	3.3x	3.8x	3.9x	4.4x	4.3x	-0.1x	1.0x	3.3x	4.3x	1.0x
Investment yield*	5.4%	4.9%	3.4%	2.4%	2.1%	-0.3ppt	-3.3ppt	5.7%	4.4%	-1.3ppt
Cost-to-income ratio	45%	46%	43%	46%	42%	-4ppt	-3ppt	49%	44%	-5ppt

Source: Company data, CMBIS

*: including interest income from debt/other debt investments when calculating annual investment yield.

Figure 2: Earnings revision

(HK\$)	New		Old		New vs. Old	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Adj. operating income (mn)	17,507	19,113	19,108	20,744	-8%	-8%
Net profit (mn)	6,984	7,707	7,072	7,718	-1%	0%
EPS	0.69	0.76	0.69	0.76	0%	0%
BVPS	8.49	9.05	7.97	8.53	6%	6%
ROE	8.3%	8.7%	9.0%	9.2%	-0.7ppt	-0.5ppt

Source: CMBIS estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Brokerage commission	4,551	6,921	6,739	7,376	7,710
Investment banking fee	480	950	898	937	1,019
Asset management fee	634	592	530	546	596
Net interest income	3,492	4,178	3,835	3,947	4,178
Prop-trading gains	4,897	4,828	5,390	6,030	6,581
Others	266	146	115	277	277
Adj. op. revenue	14,320	17,615	17,507	19,113	20,361
Adj. op. expenses	(7,079)	(7,962)	(8,266)	(8,851)	(9,330)
PPoP	7,241	9,652	9,241	10,262	11,031
Provision	(410)	(496)	(365)	(304)	(255)
Pre-tax profit	6,830	9,157	8,876	9,958	10,776
Income tax expense	(1,580)	(1,845)	(1,985)	(2,191)	(2,371)
Minority interests	(22)	(68)	(55)	(60)	(66)
Net profit	5,228	7,244	6,984	7,707	8,339

Balance sheet

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Deposit held on behalf of clients	60,282	76,852	84,433	93,585	98,025
Clearing reserves	11,276	17,584	19,636	21,764	22,797
Margin accounts	58,721	82,018	91,040	98,324	104,223
Reverse repos	30,438	31,863	33,456	35,129	36,534
Financial investments	121,437	184,435	201,034	215,106	225,861
Other assets	33,511	52,978	50,457	54,865	56,257
Total assets	315,666	445,730	480,056	518,773	543,698
Customer brokerage deposits	80,509	97,671	106,385	127,275	133,314
Short-term debts	86,468	160,011	174,743	182,018	190,289
Long-term debts	64,023	65,669	70,266	73,780	76,731
Other liabilities	12,744	40,371	41,825	43,186	44,754
Total liabilities	243,744	363,722	393,220	426,259	445,088
Total shareholders' equity	70,896	81,255	86,045	91,698	97,770
Incl. Perpetual bonds	0	4,962	4,962	4,962	4,962
Minority interest	1,026	754	791	815	839

Key Ratios

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Operating revenue mix					
Brokerage commission	32%	39%	38%	39%	38%
Investment banking fee	3%	5%	5%	5%	5%
Asset management fee	4%	3%	3%	3%	3%
Net interest income	24%	24%	22%	21%	21%
Prop-trading gains	34%	27%	31%	32%	32%
Others	2%	1%	1%	1%	1%
Total	100%	100%	100%	100%	100%
Growth, YoY					
Brokerage commission	31%	52%	-3%	9%	5%
Investment banking fee	-10%	98%	-5%	4%	9%
Asset management fee	-15%	-7%	-10%	3%	9%
Net interest income	1%	20%	-8%	3%	6%
Prop-trading gains	418%	-1%	12%	12%	9%
Adj. op. revenue	55%	23%	-1%	9%	7%
PPoP	77%	33%	-4%	11%	7%
Net profit	81%	39%	-4%	10%	8%
Total assets	26%	41%	8%	8%	5%
Efficiency					
Cost-to-income ratio	49%	44%	46%	45%	45%
Leverage					
Adj. financial leverage (x)	3.3	4.3	4.3	4.3	4.2
Investment/ equity	171%	227%	234%	235%	231%
Profitability					
ROE	7.6%	9.5%	8.3%	8.7%	8.8%
ROA	1.8%	1.9%	1.5%	1.5%	1.6%
Per share					
EPS (RMB)	0.52	0.71	0.69	0.76	0.82
DPS (RMB)	0.16	0.22	0.21	0.23	0.25
BVPS (RMB)	6.99	8.02	8.49	9.05	9.64

Source: Company data, CMBIS estimates

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