

## Hong Kong Exchange & Clearing (388 HK)

### 1Q20 solid core revenue weighed by invt. losses

HKEx reported 1Q20 net profit of HK\$ 2.3bn (22% of consensus FY20E est.), down 13% YoY, as investment losses outweighed remarkable trading volume recovery (core revenue +19% YoY). HKEx's active de-risking action could alleviate impact from volatile investment gains in coming quarters, and potential secondary listing of tech giants in 2H20E may excite market, yet trading activity is moderating since Apr and catalysts to drive structural changes remain absent in near-term. In addition, we think Charles Li's stepping down could possibly adding uncertainty to the Company's future China-related strategy execution. **We fine-tune TP to HK\$ 254.0 post results and maintain HOLD.**

- 1Q20 results recap and implications:** While robust cash equity trading, record high Stock Connect ADT and resilient listing fees well drove core revenue growth despite COVID-19, net investment loss from external invt. portfolio (HK\$ 521mn) due to global sell-offs dragged HKEx' top-line growth. The Company has actively pared down this invt. portfolio size by ~40% to de-risk, and FV may reverse should market sentiment improved. On opex side, we still see HKEx enhancing investment into talents and IT.
- Market activity moderating since Apr; initiatives driving structural growth still not in sight.** Looking ahead, headline ADT is not likely to stay at similar high level in 1Q20, and we've already seen it down 29%/17% in Apr from Mar/1Q20. Initiatives that we expect to spur its structural growth and re-rating, e.g. the launch of MSCI A Index future, are still unlikely to be seen in near-term. Though potential secondary listing of tech giants in 2H20E may shore up market sentiment, we expect relatively limited revenue impact in FY20E. The inclusion of secondary listing WVR companies into Stock Connect would have more substantial positive impact, but this is also wait-and-see. Moreover, Charles Li's stepping down in 12-18mths could add uncertainties in the Bourse's future strategy, in our view. Regarding Charles Li's succession, mgmt. mentioned this would be a "global search" for someone who "dreams big, aims high" while at the same time protects what HKEx has achieved.
- Fine-tune TP to HK\$ 254; Maintain HOLD.** We trim FY20E/21E net profit by 3%/4%, mainly on lower ADT/ADV and invt. gains assumptions, while lift listing fees and maintain similar opex est. We also see potential downside revision of consensus EPS post results. We thus cut TP by 4% to HK\$ 254.0, implying 33x FY20E P/E (vs. 5-year avg. of 30x). **Maintain HOLD.**

#### Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (HK\$ mn)	15,867	16,311	16,995	19,014	21,126
Net profit (HK\$ mn)	9,312	9,391	9,776	10,896	12,114
EPS (HK\$)	7.50	7.49	7.72	8.52	9.39
EPS YoY growth (%)	24	(0)	3	10	10
Consensus EPS (HK\$)	N/A	N/A	8.24	9.10	9.86
P/E (x)	32.8	32.9	31.9	28.9	26.2
P/B (x)	7.5	7.0	6.5	6.1	5.8
Yield (%)	2.7	2.7	2.8	3.1	3.4
ROE (%)	23.9	22.1	21.3	22.1	22.8
EBITDA margin (%)	74.1	75.2	75.0	74.7	74.5

Source: Company data, Bloomberg, CMBIS estimates

#### HOLD (Maintain)

Target Price	HK\$ 254.0
(Previous TP)	HK\$ 265.0)
Up/Downside	+3.2%
Current Price	HK\$ 246.4

#### Diversified Financials Sector

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#### Stock Data

Mkt Cap (HK\$ mn)	312,395
Avg 3 mths t/o (HK\$ mn)	1,290.59
52w High/Low (HK\$)	283.6/206.0
Total Issued Shares (mn)	1,268

Source: Bloomberg

#### Shareholding Structure

JPMorgan Chase & Co	8.02%
The Government of HKSAR	5.93%

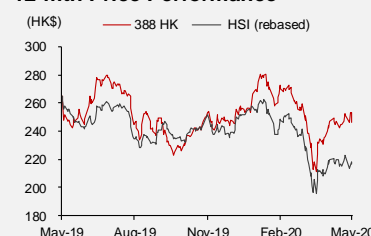
Source: Bloomberg

#### Share Performance

	Absolute	Relative
1-mth	5.4%	3.7%
3-mth	-7.2%	5.7%
6-mth	0.9%	15.7%

Source: Bloomberg

#### 12-mth Price Performance



Source: Bloomberg

Auditor: PwC

#### Related Reports

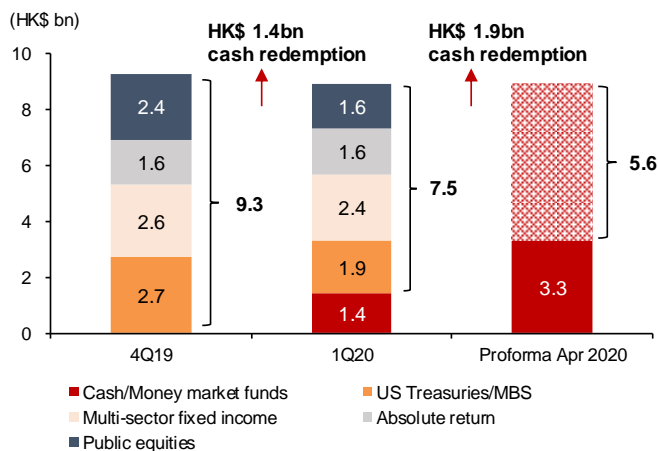
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- "Near-term catalysts take time to materialize" (Initiation) – 30 Dec 2019
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Figure 1: HKEx's quarterly results summary

(HK\$ mn)	1Q19	2Q19	3Q19	4Q19	1Q20	QoQ	YoY
<b>I/S</b>							
Trading fees and tariffs	1,491	1,449	1,369	1,283	1,794	40%	20%
Listing fees	453	394	394	392	492	26%	9%
Clearing and settlement fees	834	821	777	728	1,052	45%	26%
Depository, custody & nominee services fees	140	435	276	201	160	-20%	14%
Market data fees	229	232	231	227	237	4%	3%
Net investment income	882	637	637	573	(47)	-108%	-105%
Other revenue and incomes	259	322	303	342	321	-6%	24%
<b>Total revenue</b>	<b>4,288</b>	<b>4,290</b>	<b>3,987</b>	<b>3,746</b>	<b>4,009</b>	<b>7%</b>	<b>-7%</b>
Opex	(970)	(983)	(949)	(1,146)	(1,025)	-11%	6%
<b>EBITDA</b>	<b>3,318</b>	<b>3,307</b>	<b>3,038</b>	<b>2,600</b>	<b>2,984</b>	<b>15%</b>	<b>-10%</b>
D&A	(248)	(247)	(271)	(278)	(274)	-1%	10%
<b>Pre-tax profit</b>	<b>3,029</b>	<b>3,021</b>	<b>2,605</b>	<b>2,296</b>	<b>2,680</b>	<b>17%</b>	<b>-12%</b>
Taxation	(422)	(425)	(400)	(314)	(422)	34%	0%
<b>Net profit</b>	<b>2,608</b>	<b>2,597</b>	<b>2,207</b>	<b>1,979</b>	<b>2,262</b>	<b>14%</b>	<b>-13%</b>
<b>Key ratios</b>							
Cost-to-income ratio	28.4%	28.7%	30.6%	38.0%	32.4%	-5.6ppt	4.0ppt
EBITDA margin	77.4%	77.1%	76.2%	69.4%	74.4%	5.0ppt	-2.9ppt
ROE	26.0%	24.8%	20.4%	18.3%	20.8%	2.6ppt	-5.1ppt
ROA	4.0%	4.1%	3.5%	2.9%	2.9%	0.0ppt	-1.1ppt
<b>Key drivers</b>							
Headline cash equity ADT (HK\$ bn)	101	95	77	77	121	57%	20%
Equity ADT excl. Southbound (HK\$ bn)	63	64	53	54	85	57%	34%
DWs, CBBCs and IWs ADT (HK\$ bn)	27	19	14	13	18	39%	-34%
Southbound ADT (HK\$ bn)	11.9	10.5	9.7	11.2	21.6	93%	82%
Northbound ADT (RMB bn)	38.5	49.7	38.5	40.9	78.0	91%	103%
HKEx F&Os ADV ('000 contracts)	1,187	1,173	990	937	1,298	39%	9%
LME commodities ADV ('000 contracts)	611	628	617	614	683	11%	12%

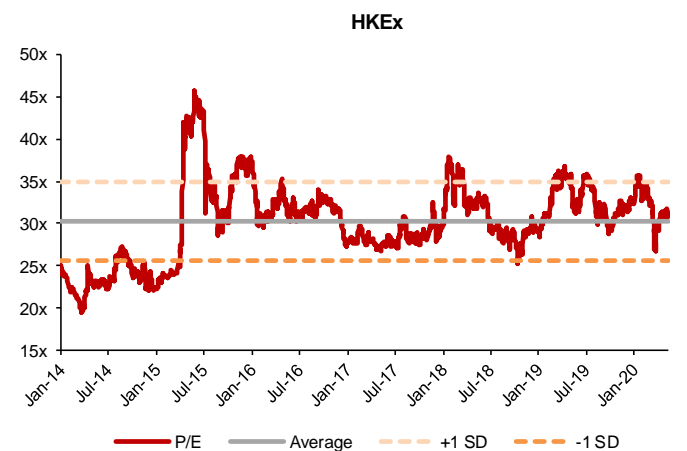
Source: Company data, CMBIS

Figure 2: HKEx redeemed a total of HK\$ 3.3bn cash from its external invt. portfolio since FY20 for de-risking



Source: Company data, CMBIS

Figure 3: HKEx's historical 1-year forward P/E



Source: Bloomberg, CMBIS estimates

**Figure 4: Earnings revision**

(HK\$ mn) I/S	New			Change vs. Old		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Trading fees and tariffs	6,151	6,956	7,923	-1%	-6%	-6%
Listing fees	1,910	2,161	2,421	7%	9%	13%
Clearing and settlement fees	3,611	4,292	4,934	-6%	-7%	-7%
Depository, custody & nominee services fees	1,126	1,204	1,289	0%	0%	0%
Market data fees	984	1,042	1,103	3%	3%	3%
Net investment income	1,877	2,042	2,063	-13%	-8%	-11%
Other revenue and incomes	1,349	1,483	1,632	0%	0%	0%
<b>Total revenue</b>	<b>17,007</b>	<b>19,182</b>	<b>21,365</b>	<b>-2%</b>	<b>-4%</b>	<b>-4%</b>
Opex	(4,252)	(4,853)	(5,448)	-2%	-4%	-4%
<b>EBITDA</b>	<b>12,755</b>	<b>14,329</b>	<b>15,917</b>	<b>-2%</b>	<b>-4%</b>	<b>-4%</b>
D&A	(1,169)	(1,310)	(1,414)	0%	0%	0%
<b>Operating profit</b>	<b>11,586</b>	<b>13,019</b>	<b>14,503</b>	<b>-3%</b>	<b>-4%</b>	<b>-4%</b>
<b>Pre-tax profit</b>	<b>11,433</b>	<b>12,860</b>	<b>14,335</b>	<b>-3%</b>	<b>-4%</b>	<b>-4%</b>
Taxation	(1,651)	(1,857)	(2,070)	-3%	-4%	-4%
<b>Net profit</b>	<b>9,783</b>	<b>11,004</b>	<b>12,266</b>	<b>-3%</b>	<b>-4%</b>	<b>-4%</b>
<b>Key drivers</b>	<b>FY20E</b>	<b>FY21E</b>	<b>FY22E</b>	<b>FY20E</b>	<b>FY21E</b>	<b>FY22E</b>
Cash equity ADT (HK\$ bn)	105	122	139	-1%	-5%	-5%
Southbound ADT (HK\$ bn)	18.2	21.7	23.1	13%	15%	9%
Northbound ADT (HK\$ bn)	62.8	71.8	82.8	-2%	-2%	-1%
HKEx F&Os ADV ('000 contracts)	1,080	1,267	1,479	-5%	-8%	-7%
LME commodities ADV ('000 contracts)	632	672	720	-3%	-4%	-5%

Source: CMBIS estimates

## Financial summary

### Income statement

YE 31 Dec (HK\$ mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Trading fees and tariff	6,339	5,592	6,151	6,956	7,923
Listing fees	1,721	1,633	1,910	2,161	2,421
Clearing & settlement fees	3,281	3,160	3,611	4,292	4,934
Depository & custody fees	979	1,052	1,126	1,204	1,289
Market data fees	899	919	984	1,042	1,103
Net investment income	1,584	2,729	1,877	2,042	2,063
Others	1,064	1,226	1,349	1,483	1,632
<b>Total revenue</b>	<b>15,867</b>	<b>16,311</b>	<b>17,007</b>	<b>19,182</b>	<b>21,365</b>
Staff costs	(2,540)	(2,703)	(2,852)	(3,256)	(3,647)
IT costs	(508)	(580)	(656)	(797)	(952)
Other opex	(1,062)	(765)	(744)	(800)	(849)
<b>Total opex</b>	<b>(4,110)</b>	<b>(4,048)</b>	<b>(4,252)</b>	<b>(4,853)</b>	<b>(5,448)</b>
<b>EBITDA</b>	<b>11,757</b>	<b>12,263</b>	<b>12,755</b>	<b>14,329</b>	<b>15,917</b>
D&A	(762)	(1,044)	(1,169)	(1,310)	(1,414)
Pre-tax profit	10,995	11,219	11,586	13,019	14,503
Taxation	(1,592)	(1,561)	(1,651)	(1,857)	(2,070)
Minority interests					
<b>Net profit</b>	<b>9,312</b>	<b>9,391</b>	<b>9,783</b>	<b>11,004</b>	<b>12,266</b>

### Balance sheet

YE 31 Dec (HK\$ mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Cash & Financial assets	217,840	230,794	279,565	266,218	277,313
Fixed assets	1,625	3,955	4,074	4,196	4,322
Goodwill & intangible assets	18,019	18,378	18,562	18,747	18,935
Interest in JV/ assoc.	63	95	105	115	126
Other assets	18,401	25,829	26,605	27,670	29,330
<b>Total assets</b>	<b>255,948</b>	<b>279,051</b>	<b>328,909</b>	<b>316,946</b>	<b>330,027</b>
Margin deposits	123,728	142,536	186,109	162,371	165,697
CP's Clearing Funds	14,787	14,394	15,689	16,631	17,462
Borrowings	1,166	418	418	418	418
Other liabilities	75,364	77,202	78,714	85,935	90,982
<b>Total liabilities</b>	<b>215,045</b>	<b>234,550</b>	<b>280,930</b>	<b>265,355</b>	<b>274,560</b>
<b>Shareholders' fund</b>	<b>40,729</b>	<b>44,173</b>	<b>47,635</b>	<b>51,230</b>	<b>55,087</b>
Minority interest	174	328	344	362	380

### Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Key market indicators</b>					
Cash equity ADT (HK\$ bn)	107	87	105	122	139
Southbound ADT (HK\$ bn)	12.7	10.8	18.2	21.7	23.1
Northbound ADT (RMB bn)	24.1	47.3	69.8	80.0	92.3
HKEx F&Os ADV ('000)	1,204	1,070	1,080	1,267	1,479
LME commodities ADV ('000)	630	618	632	672	720
<b>Biz segment revenue mix</b>					
Cash	24%	22%	25%	25%	25%
Equity & financial derivatives	22%	18%	19%	19%	20%
Commodities	9%	9%	9%	8%	8%
Post-trade	39%	38%	39%	39%	39%
Others	6%	13%	8%	9%	8%
Total	100%	100%	100%	100%	100%
<b>% of total revenue</b>					
Trading fees and tariff	40%	34%	36%	36%	37%
Listing fees	11%	10%	11%	11%	11%
Clearing and settlement fees	21%	19%	21%	22%	23%
Staff costs	16%	17%	17%	17%	17%
IT costs	3%	4%	4%	4%	4%
<b>Growth, YoY</b>					
Total revenue	20.4%	2.8%	4.3%	12.8%	11.4%
EBITDA	22.3%	4.3%	4.0%	12.3%	11.1%
Net profit	25.8%	0.8%	4.2%	12.5%	11.5%
<b>Efficiency</b>					
Cost-to-income ratio	31%	31%	32%	32%	32%
EBITDA margin	74%	75%	75%	75%	75%
<b>Profitability</b>					
ROE	23.9%	22.1%	21.3%	22.3%	23.1%
ROA	3.2%	3.5%	3.2%	3.4%	3.8%
<b>Per share</b>					
EPS (HK\$)	7.50	7.49	7.72	8.61	9.51
DPS (HK\$)	6.68	6.68	6.92	7.71	8.52
BVPS (HK\$)	32.71	35.28	37.70	40.18	42.81

Source: Company data, CMBIS estimates

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