

# Hong Kong Exchange & Clearing (388 HK)

## 1H19 results in-line; more challenges in 2H19E

**SUMMARY.** HKEx reported an in-line 1H19 results, with higher investment income and depository fees offsetting weaker trading activity-related incomes. Going forwards, the heightened macro uncertainty and absence of near-term catalyst will likely weigh on headline ADT and therefore its earnings in 2H19E.

- **2Q19 results in a nutshell.** 2Q19 revenue/ net profit was flat QoQ. Weaker trading, clearing and listing fees (-3%/-2%/-13% QoQ) were offset by stronger than seasonal growth of depository fees, and higher-than-expected net investment income despite a high base in 1Q19. Northbound trading was a major bright spot as ADT grew another 26% QoQ/ 129% YoY in 2Q19, and increased its contribution in trading and clearing fees to 8% (+1ppt QoQ/+4ppt YoY). Cost-to-income ratio was stable at 28.7%, up 0.3ppt QoQ.
- **Softening market condition likely weighs on earnings outlook.** Trading activity continued to moderate in 2HTD as headline ADT shrank to HK\$ 74bn, 24% lower than HK\$ 98bn in 1H19, which would drag trading and clearing fees. The strong performance from investment income is also not likely to sustain because the increase was largely from investment in equities, which should see QoQ declines. But two factors could partly help cushion the impact: 1) MSCI's further increasing weighting in A-shares that could support a strong YoY growth of Northbound trading, and 2) futures trading that delivers resilient performance esp. when market is volatile.
- **Near-term catalysts absent.** A major expectation to boost HKEx's revenue was the launch of MSCI A-share futures, in our view. This seems not possible to happen in this year, and it's still awaiting regulatory approval. Though the potential secondary listing of tech giant and inclusion of WVR companies into Southbound is encouraging, it is still wait-and-see whether this will have a meaningful earnings impact on HKEx. While the Company's long-term growth story of being a nexus between China's onshore market and the world remains intact, we think absence of near-term catalysts could cap its rebound potential in coming months.
- **Valuation.** After a 16% correction since Jul, HKEx now trades at 27x forward FY19E P/E, lower than its 5-year average of 30x. But the valuation would appear less attractive after the possible downward EPS revision on lower ADT assumption. We expect the stock to trade sideways due to persisting macro uncertainty and absence of near-term catalysts. **Upside risks:** a more accurate rollout schedule for MSCI A-share futures; better-than-expected ADT.

### Earnings Summary

(YE 31 Dec)	FY16A	FY17A	FY18A
Revenue (HK\$ mn)	11,116	13,180	15,867
Net income (HK\$ mn)	5,769	7,404	9,312
EPS (HK\$)	4.76	6.03	7.50
YoY growth (%)	(29)	27	24
P/E (x)	49.4	39.0	31.4
P/B (x)	8.9	7.8	7.2
Yield (%)	1.8	2.3	2.8
ROE (%)	18.6	21.3	23.9
EBITDA margin (%)	68.9	72.9	74.1

Source: Company data, Bloomberg, CMBIS

**NOT RATED**

Current Price

HK\$235.2

### Diversified Financials Sector

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### Stock Data

Mkt Cap (HK\$ mn)	295,907
Avg 3 mths t/o (HK\$ mn)	1,206.1
52w High/Low (HK\$)	286.2/195.6
Total Issued Shares (mn)	1,258.1

Source: Bloomberg

### Shareholding Structure

The Government of the Hong Kong Special Administrative Region	5.38%
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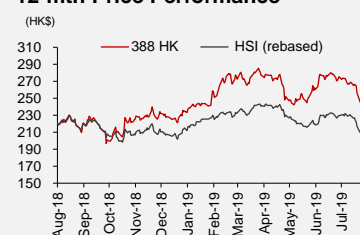
Source: HKEx

### Share Performance

	Absolute	Relative
1-mth	-14.6%	-3.9%
3-mth	-4.9%	5.7%
6-mth	-8.8%	2.5%

Source: Bloomberg

### 12-mth Price Performance



Source: Bloomberg

**Auditor: PwC**

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**Figure 1: Quarterly results summary of HKEx**

(HK\$ mn)	2Q18	3Q18	4Q18	1Q19	2Q19	QoQ	YoY	1H18	1H19	YoY
<b>I/S</b>										
Trading fees and tariffs	1,540	1,515	1,490	1,491	1,449	-3%	-6%	3,334	2,940	-12%
Listing fees	395	456	410	453	394	-13%	0%	855	847	-1%
Clearing and settlement fees	830	784	750	834	821	-2%	-1%	1,747	1,655	-5%
Depository, custody and nominee services fees	368	295	166	140	435	211%	18%	518	575	11%
Market data fees	224	232	224	229	232	1%	4%	443	461	4%
Net investment income	416	539	250	882	637	-28%	53%	795	1,519	91%
Other revenue and incomes	271	281	281	259	322	24%	19%	502	581	16%
<b>Total revenue</b>	<b>4,044</b>	<b>4,102</b>	<b>3,571</b>	<b>4,288</b>	<b>4,290</b>	<b>0%</b>	<b>6%</b>	<b>8,194</b>	<b>8,578</b>	<b>5%</b>
Opex	(983)	(1,025)	(1,167)	(970)	(983)	1%	0%	(1,918)	(1,953)	2%
<b>EBITDA</b>	<b>3,061</b>	<b>3,077</b>	<b>2,404</b>	<b>3,318</b>	<b>3,307</b>	<b>0%</b>	<b>8%</b>	<b>6,276</b>	<b>6,625</b>	<b>6%</b>
D&A	(198)	(198)	(186)	(248)	(247)	0%	25%	(378)	(495)	31%
<b>Operating profit</b>	<b>2,863</b>	<b>2,879</b>	<b>2,218</b>	<b>3,070</b>	<b>3,060</b>	<b>0%</b>	<b>7%</b>	<b>5,898</b>	<b>6,130</b>	<b>4%</b>
Finance costs	(28)	(31)	(28)	(44)	(42)	-5%	50%	(55)	(86)	56%
Shares in associate/JVs	2	(1)	(1)	3	3	0%	50%	4	6	50%
<b>Pre-tax profit</b>	<b>2,837</b>	<b>2,847</b>	<b>2,189</b>	<b>3,029</b>	<b>3,021</b>	<b>0%</b>	<b>6%</b>	<b>5,847</b>	<b>6,050</b>	<b>3%</b>
Taxation	(366)	(409)	(361)	(422)	(425)	1%	16%	(822)	(847)	3%
<b>Profit for the period</b>	<b>2,471</b>	<b>2,438</b>	<b>1,828</b>	<b>2,607</b>	<b>2,596</b>	<b>0%</b>	<b>5%</b>	<b>5,025</b>	<b>5,203</b>	<b>4%</b>
Non-controlling interests	8	5	0	1	1	0%	-88%	16	2	-88%
<b>Net profit</b>	<b>2,479</b>	<b>2,443</b>	<b>1,828</b>	<b>2,608</b>	<b>2,597</b>	<b>0%</b>	<b>5%</b>	<b>5,041</b>	<b>5,205</b>	<b>3%</b>
<b>Key ratios</b>										
Cost-to-income ratio	29.2%	29.8%	37.9%	28.4%	<b>28.7%</b>	0.3ppt	-0.5ppt	28.0%	28.5%	0.5ppt
EBITDA margin	75.7%	75.0%	67.3%	77.4%	<b>77.1%</b>	-0.3ppt	1.4ppt	76.6%	77.2%	0.6ppt
ROAE	24.6%	24.4%	18.2%	26.0%	<b>24.8%</b>	-1.2ppt	0.2ppt	25.9%	24.5%	-1.3ppt
ROAA	3.2%	3.5%	2.9%	4.0%	<b>4.1%</b>	0.1ppt	0.8ppt	3.2%	4.2%	0.9ppt
<b>Key drivers</b>										
Cash equity ADT (HK\$ bn)	107	92	86	101	<b>95</b>	-6%	-11%	127	98	-23%
Southbound ADT (HK\$ bn)	13	10	8	12	<b>10</b>	-12%	-19%	16	11	-32%
Northbound ADT (HK\$ bn)	25	22	26	45	<b>57</b>	26%	129%	24	51	110%
HKEx derivatives ADV ('000 contracts)	1,123	1,129	1,223	1,187	<b>1,173</b>	-1%	4%	1,233	1,180	-4%
LME commodities ADV ('000 contracts)	689	621	581	611	<b>628</b>	3%	-9%	659	620	-6%

Source: Company data, CMBIS

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