

China Brokerage Sector

Resilient Mar set for better-than-expected 1Q20E results

China brokers released milder-than-expected net profit decline in Mar amid market turbulence, which could possibly support a better-than-expected growth of 1Q20E results on high base. As trading activity moderated since mid-Mar and IPO approval process resumed to normal, the growth driver may switch from brokerage/stock-driven prop-trading gains to investment banking. We add CSC to our top picks for its strong franchise in equity and corp. bond underwriting and higher sensitivity to IB volume changes. **Maintain OUTPERFORM on sector.**

■ **Leaders could see upbeat 1Q20E results despite high base.** Large listed brokers' revenue/net profit (parent company level) -12%/-7% MoM in Mar 2020, on coronavirus stock market slump (CSI 300 Index/ChiNext Index -6%/-10% MoM). With strong performance in 2M20 partly offsetting the weak Mar, most brokers still recorded positive YoY net profit growth in 3M20. We expect leaders less sensitive to stock market volatilities, with less burden from provision charges and strong franchise in investment banking to deliver upbeat 1Q20E results, e.g. CICC and CSC.

■ **Supportive policy stance reaffirmed; IB fees could drive divergence ahead.** On 9 Apr, the State Council issued a guidance on improving market-oriented allocation of production factors, calling for further liberalisation of capital market (incl. optimizing stock market mechanism, stepping up bond market reforms and advancing the industry opening-up), which reaffirmed favorable policy support for brokers, esp. at this hard time. Bond issuance already saw surging growth in 1Q20E, and we expect a normalized IPO approval pace in 2Q20E with reform measures (e.g. follow-on offering relaxation) gradually materialize. Prop-trading gains is likely to remain the key revenue contributor though, brokers with smaller directional exposure to stock market or higher exposure in bonds are better protected from heightened market uncertainty. (See more details in Fig. 9-28 for covered brokers' comparison charts by business lines).

■ **Maintain OUTPERFORM. Top picks: CITICS, CSC and CICC.** The sector trades at 0.64x 1-year forward P/B, close to historical trough (0.60x). We remain constructive on the sector due to 1) operations being not directly affected by the COVID-19 outbreak, 2) further capital market reforms unleashing direct financing demands, and 3) govt's supportive policies to shield economy growth and market liquidity. We continue to like leaders with strong franchise in investment banking as well as more stable prop-trading performance. **We add CSC to our top picks** as it would be a key beneficiary of equity and corp. bond underwriting vol. growth.

Valuation Table

Name	Ticker	Price (HK\$)	TP (HK\$)	Rating	P/B (x) FY20E	P/E (x) FY20E	Yield FY20E	ROE FY20E
CITICS	6030 HK	14.52	18.90	BUY	0.91	11.6	3.4%	8.2%
CSC	6066 HK	6.44	7.90	BUY	0.73	7.3	3.1%	10.3%
CICC	3908 HK	11.72	16.40	BUY	0.89	9.5	1.5%	9.7%
HTSC	6886 HK	12.44	14.60	BUY	0.79	10.8	3.7%	7.5%
HTS	6837 HK	7.16	9.40	BUY	0.55	7.4	4.1%	7.7%
GFS	1776 HK	8.65	8.90	HOLD	0.61	8.0	3.8%	7.9%
CGS	6881 HK	3.87	4.20	HOLD	0.47	6.3	4.7%	7.6%
Average					0.71	8.71	3.5%	8.4%

Source: Bloomberg, CMBIS estimates

OUTPERFORM
(Maintain)

China Brokerage Sector

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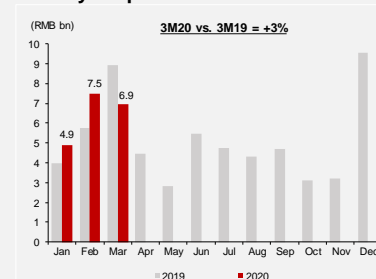
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1-yr forward P/B of China brokers - H



Source: Bloomberg, CMBIS estimates

Monthly net profit of tracked China brokers



Source: Company data, CMBIS

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Figure 1: Mar 2020 major H-share China brokers' financial data (parent company level)

Company	Ticker	Revenue (RMB mn)				Net profit (RMB mn)			
		Mar-20	MoM	3M20	YoY	Mar-20	MoM	3M20	YoY
CITICS	6030 HK	3,189	-3%	8,499	33%	1,356	8%	3,499	16%
GTJA	2611 HK	1,845	-7%	4,809	-18%	854	-11%	2,163	-29%
HTS	6837 HK	603	-69%	3,991	-12%	709	-19%	2,262	-11%
HTSC	6886 HK	1,907	-4%	5,024	18%	859	-11%	2,262	17%
GFS	1776 HK	1,104	-22%	3,846	-13%	471	-27%	1,730	-8%
CMS	6099 HK	1,562	0%	4,333	13%	708	-6%	2,035	18%
SWHY	6806 HK	1,866	54%	3,858	0%	970	77%	1,849	12%
CSC	6066 HK	1,160	-26%	4,049	40%	530	-31%	1,891	31%
CGS	6881 HK	1,254	-21%	3,854	16%	490	-30%	1,618	15%
Total		14,490	-12%	42,263	7%	6,947	-7%	19,310	3%

Source: Company data, CMBIS

Note: Revenue and net profit are the sum of parent company and reported subsidiaries, excluding dividends from subsidiaries.

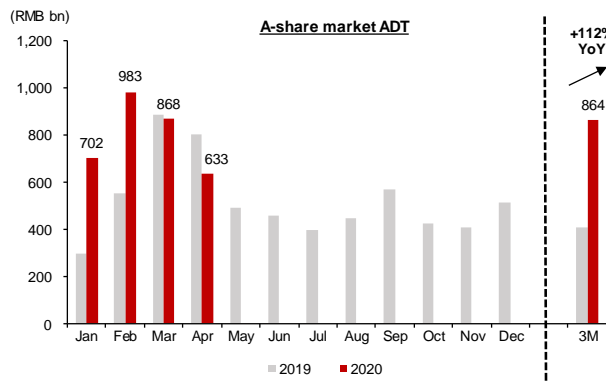
Figure 2: Mar 2020 market data recap

Item	Amount	MoM change	YoY change
Trading data (RMB bn, except for trading days)			
A-share ADT	868	-12%	-2%
A-share trading days	22	5%	5%
Northbound net inflows	(68)	-686%	-1658%
Margin financing & securities lending (daily avg. balance)	1,101	3%	25%
Index performance (month-end)			
CSI 300 Index	3,686	-6%	-5%
ChiNext Index	1,872	-10%	11%
ChinaBond Aggregate Return Index	130	1.0%	3.6%
Underwriting amount (RMB bn)			
Equity financing	116	15%	61%
Incl. IPO	10	-63%	5%
Incl. Placement & rights issue	84	97%	875%
Debt financing	1,069	290%	42%
Incl. Enterprise bonds	54	1429%	46%
Incl. Corporate bonds	459	261%	112%
Incl. ABS	125	205%	-19%

Source: Wind, CMBIS

FY20 YTD market indicators in charts

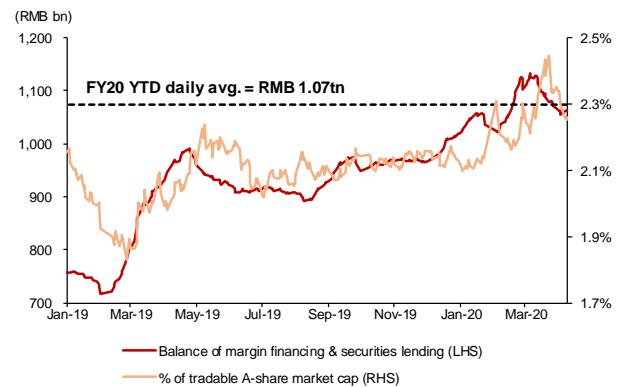
Figure 3: A-share ADT cooled down since mid-Mar but 1Q20 still recorded significant YoY growth



Source: Wind, CMBIS

Note: Apr 2020 data as of 10 Apr 2020.

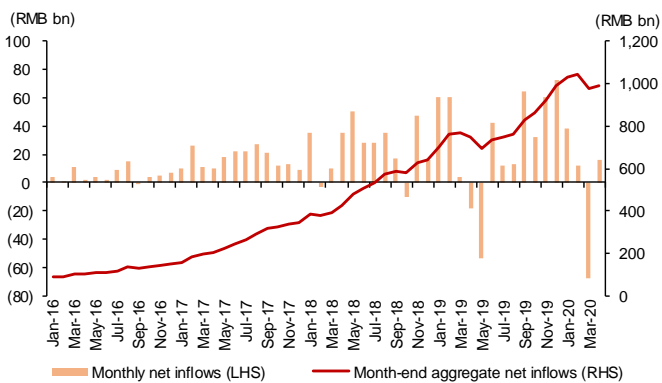
Figure 4: Margin financing and securities lending balance remained above RMB 1tn level



Source: Wind, CMBIS

Note: Apr 2020 data as of 9 Apr 2020.

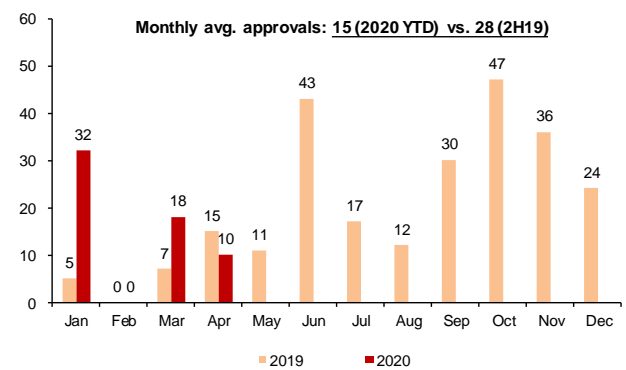
Figure 5: Northbound posted largest net outflow in Mar 2020 since launch of Stock Connect Scheme



Source: Wind, CMBIS

Note: Apr 2020 data as of 8 Apr 2020.

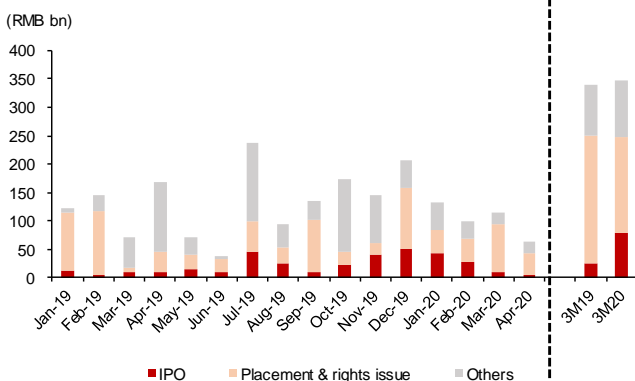
Figure 6: Monthly no. of IPO approvals started to rise as work resumption sped up



Source: Wind, CMBIS

Note: Apr 2020 data as of 10 Apr 2020.

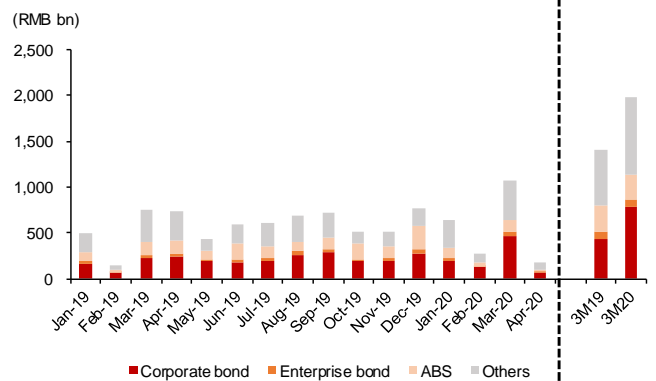
Figure 7: IPO underwriting amount remained strong despite coronavirus outbreak



Source: Wind, CMBIS

Note: Apr 2020 data as of 10 Apr 2020.

Figure 8: Debt underwriting amount surged 41% YoY in 1Q20 mainly boosted by corp. bond issuance



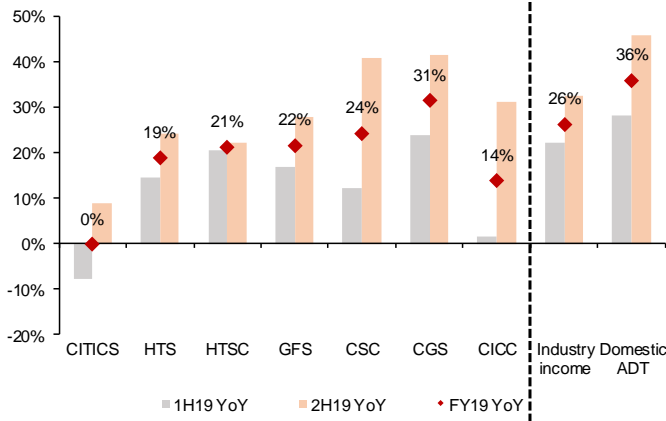
Source: Wind, CMBIS

Note: Apr 2020 data as of 10 Apr 2020.

Covered brokers' FY19 comparison by business lines

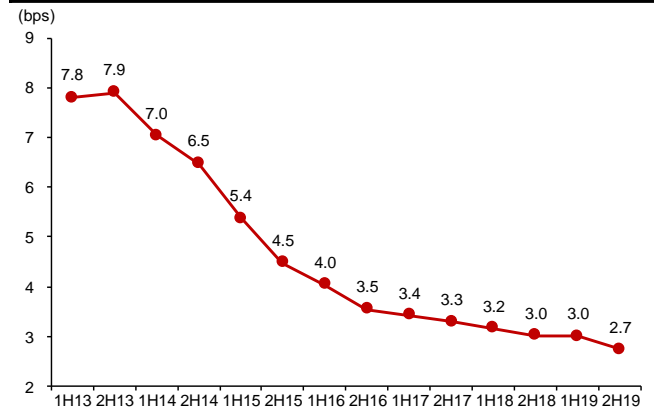
- Brokerage business: lower rates with market share losses; wealth management transformation yet to yield significant results

Figure 9: 2H19 brokerage commission posted higher YoY growth than 1H19 on low base...



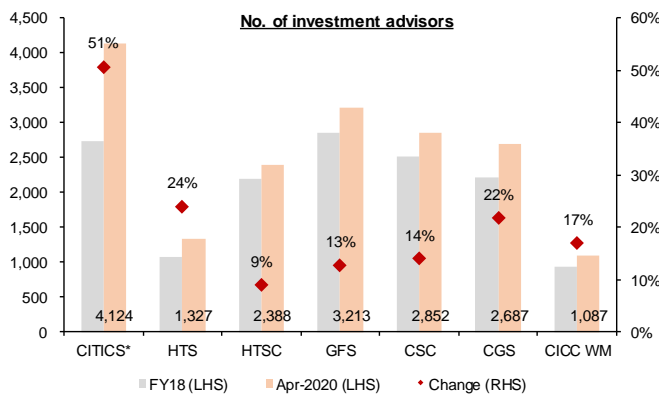
Source: Company data, Wind, CMBIS

Figure 10: ...while industry commission rate was still trending lower



Source: Wind, CMBIS

Figure 11: Brokers have been proactively growing their investment advisor teams

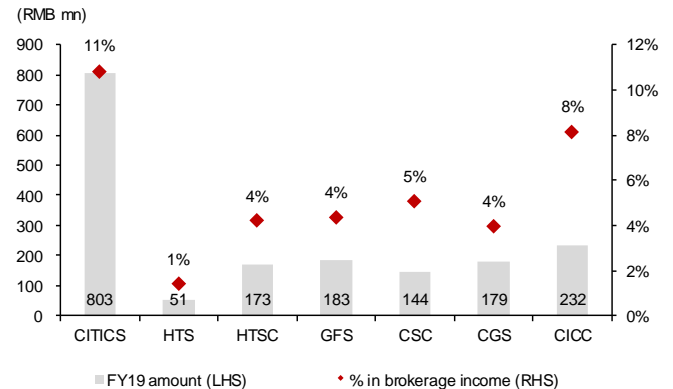


Source: SAC, CMBIS

*: including CITICS South China in latest data.

Note: Apr 2020 data as of 3 Apr 2020.

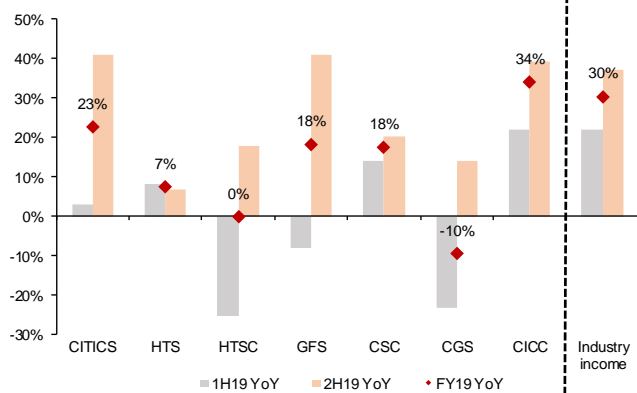
Figure 12: Revenue contribution from agency sales of financial products has great growth potential



Source: Company data, CMBIS

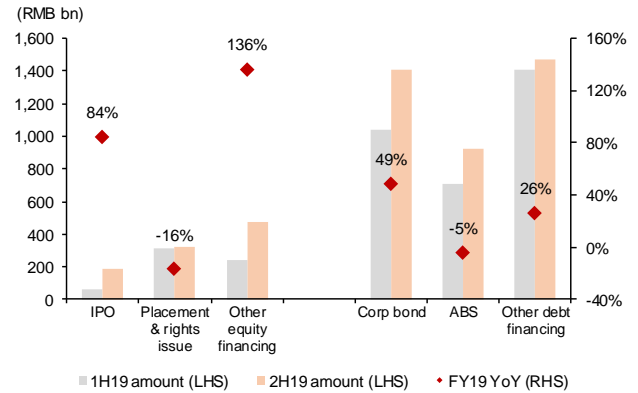
■ Investment banking business: STAR Market launch intensified industry consolidation, and so will the coming capital market reforms

Figure 13: 2H19 investment banking fees of covered brokers increased significantly YoY...



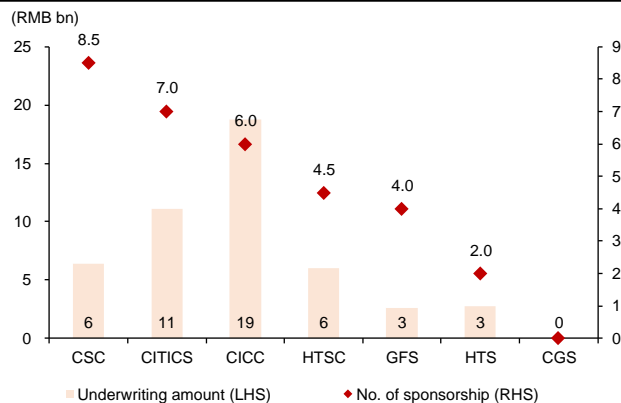
Source: Company data, CMBIS

Figure 14: ...as overall underwriting amount was higher in 2H19, marked by launch of STAR Market in 3Q19



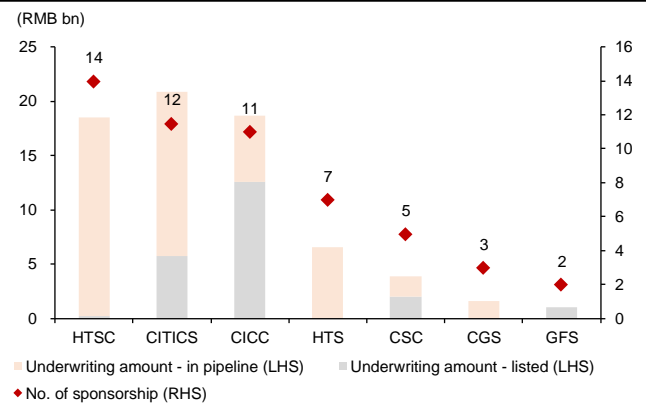
Source: Wind, CMBIS

Figure 15: STAR Market IPOs completed by covered brokers in FY19



Source: SSE, Wind, CMBIS
Note: 0.5 indicates joint sponsorship.

Figure 16: STAR Market IPOs completed and in pipelines of covered brokers YTD in FY20



Source: SSE, Wind, CMBIS
Note: data as of 31 Mar 2020.

Figure 17: Domestic equity underwriting league table

Rank(#)	FY19 Company	Total equity underwriting		IPO underwriting	
		market share	YoY amount change	market share	YoY amount change
1	CITICS	18.2%	54%	18.0%	255%
2	CICC	11.9%	56%	23.9%	63%
3	HTSC	8.8%	-1%	2.7%	-66%
4	CSC	7.8%	-20%	7.0%	33%
8	GFS	2.8%	101%	3.6%	136%
9	HTS	2.5%	-15%	1.4%	39%
27	CGS	0.6%	-7%	0.2%	-70%

Source: Wind, CMBIS

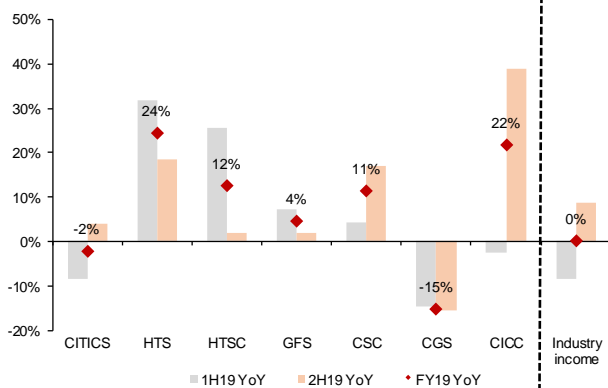
Figure 18: Domestic debt underwriting league table

Rank(#)	FY19 Company	Debt underwriting		Corp. bond underwriting	
		market share	YoY amount change	market share	YoY amount change
1	CITICS	12.3%	18%	7.9%	45%
2	CSC	11.4%	40%	13.2%	55%
3	CICC	7.2%	40%	4.2%	80%
5	HTS	5.3%	45%	4.2%	27%
8	HTSC	4.2%	59%	2.5%	56%
11	GFS	2.6%	18%	1.4%	-37%
21	CGS	0.9%	-24%	0.8%	-21%

Source: Wind, CMBIS

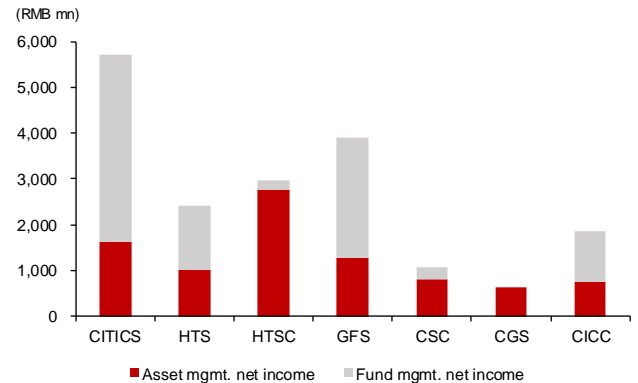
■ Asset management business: enhanced active management capabilities offset AUM shrinkage

Figure 19: Covered brokers AM fee generally increased



Source: Company data, CMBIS

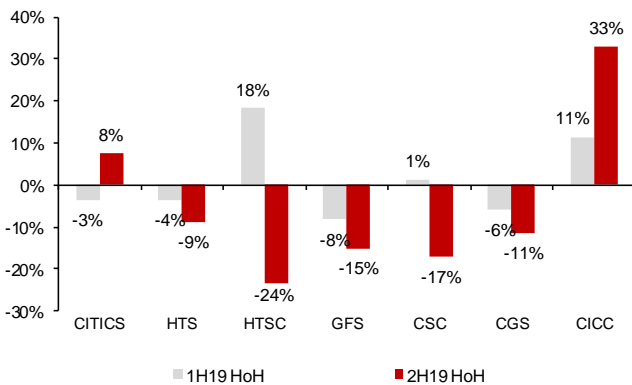
Figure 20: AM fee mix of covered brokers in FY19



Source: Company data, CMBIS

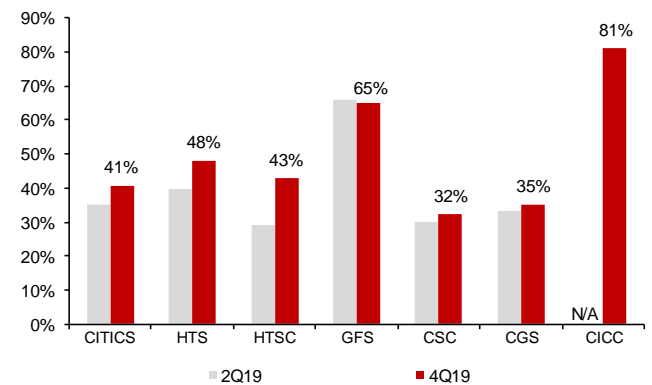
Note: CICC's fund mgmt. net income refers to PE mgmt. fees, while others are primarily mutual funds mgmt. fees.

Figure 21: Most covered brokers still saw HoH AUM contraction due to clean-up of "channel business"



Source: Company data, CMBIS

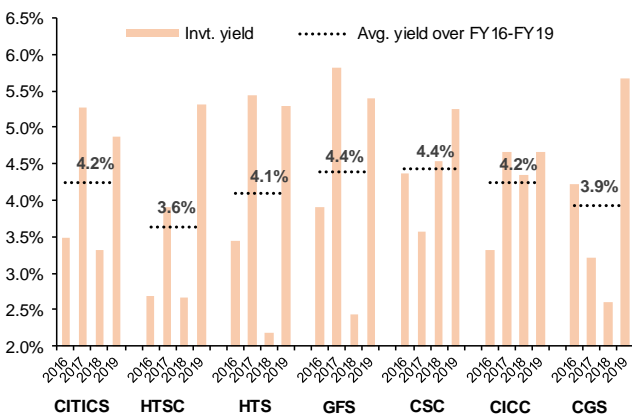
Figure 22: % of actively managed AUM further improved for covered brokers



Source: AMAC, CMBIS; Note: measured by monthly avg. balance.

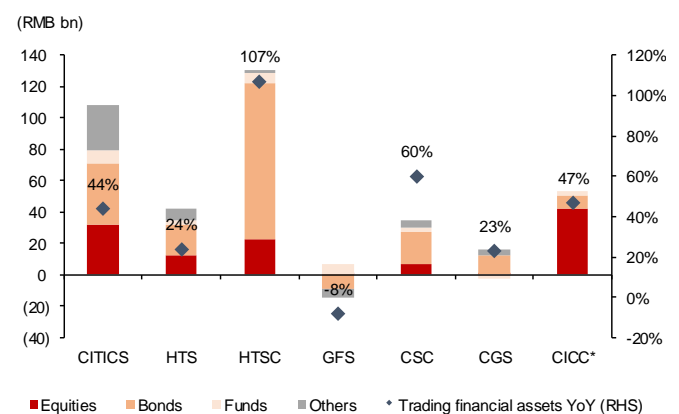
■ Prop-trading gains: notable improvement on better yield and enlarged investment assets

Figure 23: Inv't. yield greatly improved in FY19; CSC, CICC and CITICS saw more stable trend over years



Source: Company data, CMBIS Note: prop-trading gains include interest incomes from debt/other debt investments.

Figure 24: YoY net change of trading financial assets in FY19; brokers added most to fixed income inv't.

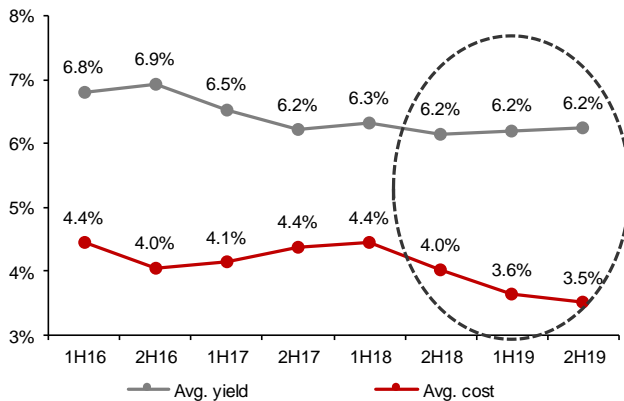


Source: Company data, CMBIS

*: fund investments include fund and other investments.

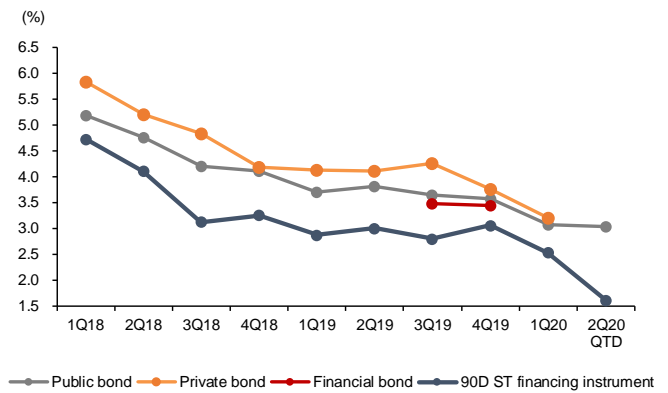
■ Credit business: risks manageable with better profitability ahead on lower financing cost

Figure 25: Yield from margin financing/SPL remained resilient amid monetary easing...



Source: Company data, CMBIS

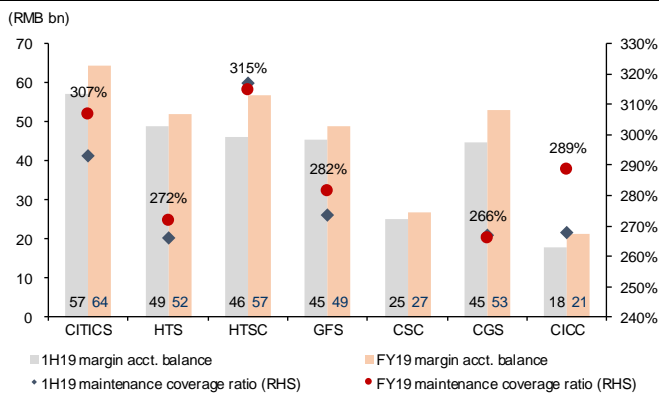
Figure 26: ... and we see faster decline of brokers' financing cost since FY20



Source: Company data, CMBIS

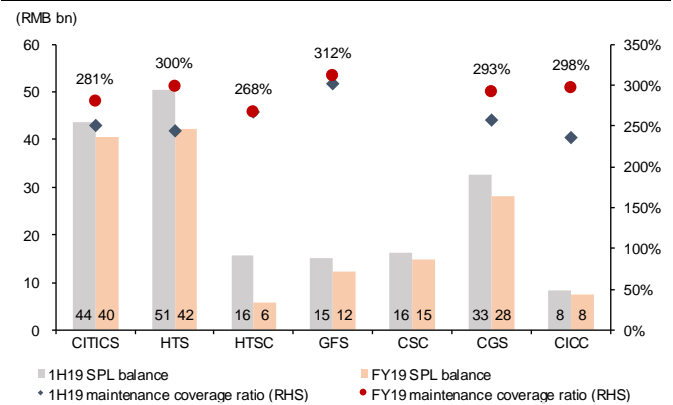
Note: all public/private/financial bonds with AAA issuer rating and 3-year maturity

Figure 27: Margin financing & securities lending – increased balance and maintenance coverage ratio



Source: Company data, CMBIS; Note: CSC's data is not available.

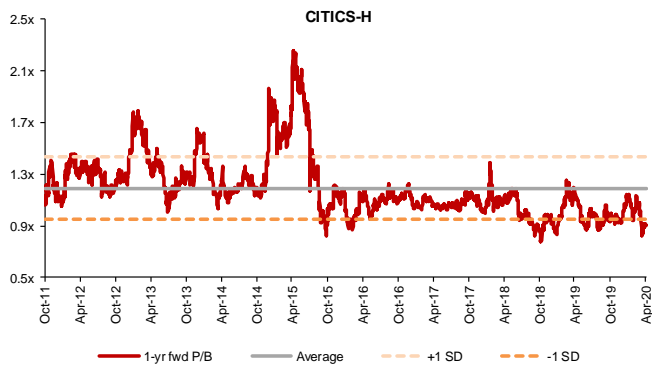
Figure 28: SPL business – slashed balance with increased maintenance coverage ratio



Source: Company data, CMBIS; Note: CSC's data is not available.

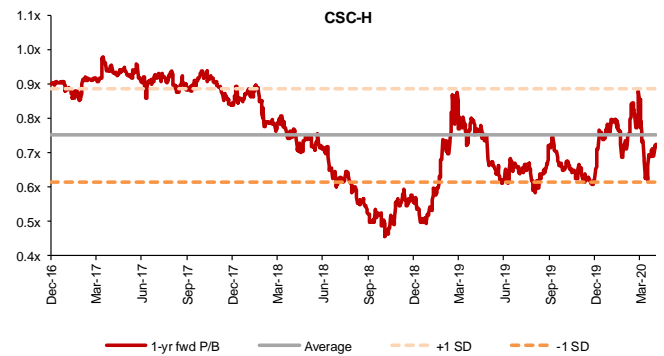
Valuation of H-share China brokers

Figure 29: CITICS's 1-yr forward P/B



Source: Bloomberg, CMBIS estimates

Figure 30: CSC's 1-yr forward P/B



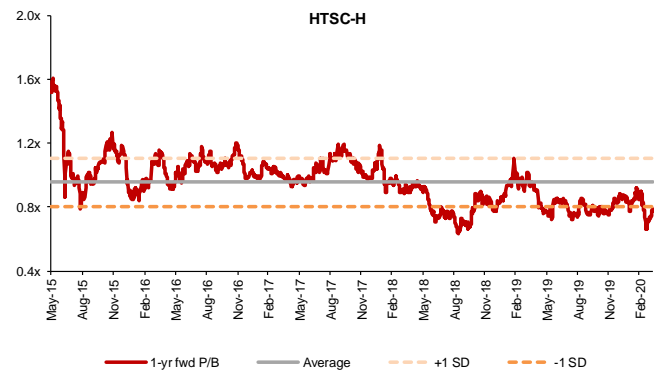
Source: Bloomberg, CMBIS estimates

Figure 31: CICC's 1-yr forward P/B



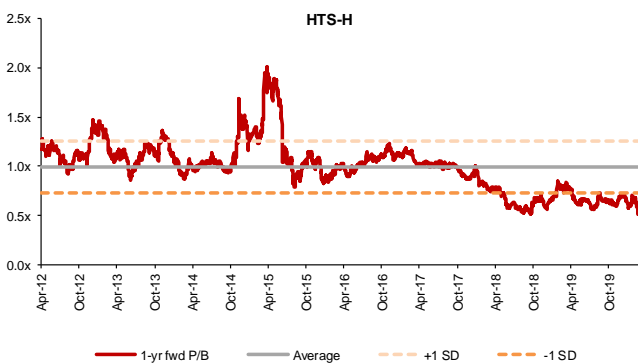
Source: Bloomberg, CMBIS estimates

Figure 32: HTSC's 1-yr forward P/B



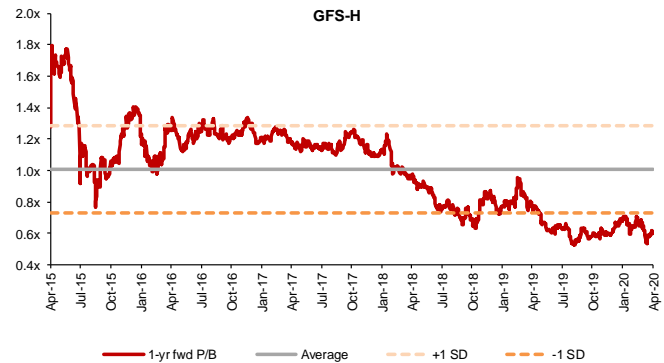
Source: Bloomberg, CMBIS estimates

Figure 33: HTS's 1-yr forward P/B

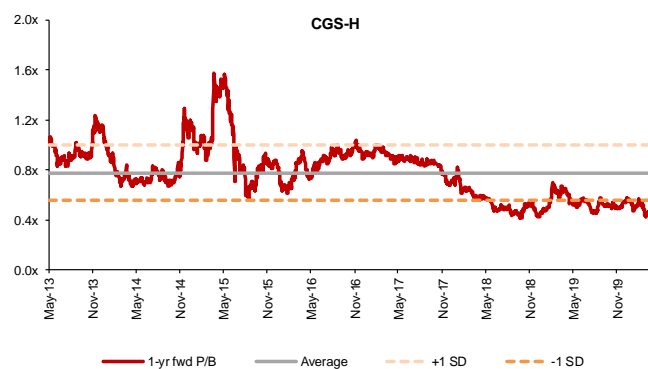


Source: Bloomberg, CMBIS estimates

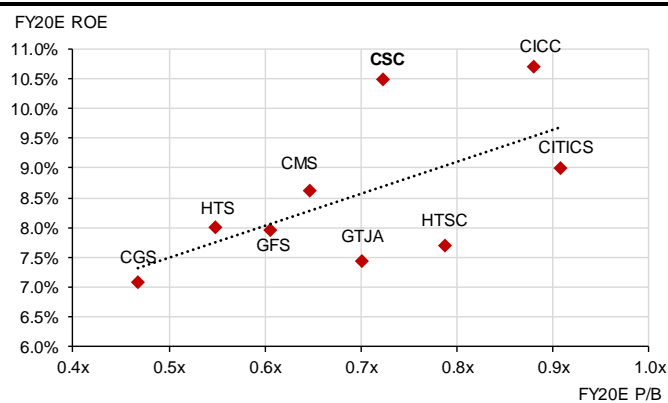
Figure 34: GFS's 1-yr forward P/B



Source: Bloomberg, CMBIS estimates

Figure 35: CGS's 1-yr forward P/B

Source: Bloomberg, CMBIS estimates

Figure 36: China brokers' P/B vs. ROE

Source: Bloomberg

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