

China Brokerage Sector

Reform acceleration could drive further divergence

China brokers' Apr 2020 financial data showed meaningful MoM growth as market major indices rebounded, and we expect larger divergence among brokers driven by investment gains and investment banking fees ahead. Given sped-up capital market reforms and A-share market's relative resilience, as well as a low-base in 2Q19, the sector's near-trough valuation is attractive with visible earnings growth potential. All of our top picks (CITICS, CSC and CICC) are well positioned to capture policy-driven opportunities, while CICC may have better short-term performance. **Maintain OUTPERFORM on sector.**

■ **Major listed brokers posted 23%/17% MoM revenue/net profit growth in Apr 2020** (parent company level), largely on strong rebound of stock market after COVID-19's hit (CSI 300/ChiNext Index +6%/+11% MoM), more than offsetting a 31% MoM shrinkage of A-share total turnover. CSC/CITICS recorded highest YoY growth in 4M20 (63%/43% YoY), which was likely attributable to their relatively smaller exposure to stock market volatility in investments and robust investment banking fees. We believe these two factors will drive further divergence of brokers' top-line growth ahead, as 1) implementation of capital market reforms will boost investment banking demands, and 2) market volatility may sustain.

■ **Faster market reform still favors investment banking leaders.** Market reform measures have come beyond market expectations as regulators are seeking to support real economy recovery. On 27 Apr, the long-awaited ChiNext reform plan piloted registration-base IPO system was revealed; later on 30 Apr, CSRC eased domestic listing requirements for oversea-listed red chips, and rolled out a pilot program on public-funded REITS backed by infrastructure projects. We believe these new measures still skew favorably towards brokers' investment banking business through unleashing IPO and ABS issuance demands, and leaders are in better positions. Market is expecting listings under ChiNext new system to happen as early as in Aug; before that, we would expect STAR Market IPOs and relaxed follow-on offerings to continue to underpin a vigorous equity financing market in 2Q20E.

■ **Maintain OUTPERFORM. Top picks: CITICS, CSC and CICC.** The sector currently trades at 0.68x 1-year forward P/B, still close to historical trough (0.60x). We continue to like leaders in investment banking for policy-driven incremental businesses and those with stable invt. gains. Meanwhile, **we expect CICC to have higher short-term upside potential**, due to its current distressed valuation (vs. historical avg. of 1.17x), and a stronger 1Q20E results could spur a share price rebound.

Valuation Table

Name	Ticker	Price (HK\$)	TP (HK\$)	Rating	P/B (x) FY20E	P/E (x) FY20E	Yield FY20E	ROE FY20E
CITICS	6030 HK	14.56	18.90	BUY	0.91	11.7	3.4%	8.2%
CSC	6066 HK	7.25	7.90	BUY	0.82	8.3	2.8%	10.3%
CICC	3908 HK	12.28	16.40	BUY	0.93	10.0	1.4%	9.7%
HTSC	6886 HK	12.54	14.60	BUY	0.80	10.9	3.7%	7.5%
HTS	6837 HK	6.76	9.40	BUY	0.52	6.9	4.3%	7.7%
GFS	1776 HK	8.23	8.90	HOLD	0.58	7.6	4.0%	7.9%
CGS	6881 HK	3.87	4.20	HOLD	0.47	6.3	4.7%	7.6%
Average					0.72	8.8	3.5%	8.4%

Source: Bloomberg, CMBIS estimates

OUTPERFORM
(Maintain)

China Brokerage Sector

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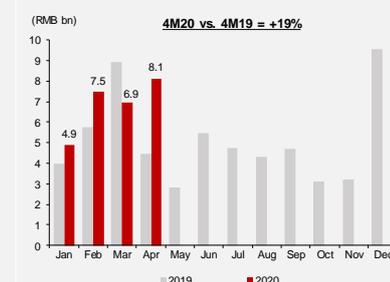
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1-yr forward P/B of China brokers - H



Source: Bloomberg, CMBIS estimates

Monthly net profit of tracked China brokers



Source: Company data, CMBIS

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

Company	Ticker	Revenue (RMB mn)				Net profit (RMB mn)			
		Apr-20	MoM	4M20	YoY	Apr-20	MoM	4M20	YoY
CITICS	6030 HK	3,506	10%	12,005	53%	1,624	20%	5,124	43%
GTJA	2611 HK	2,010	9%	6,818	-9%	797	-7%	2,961	-19%
HTS	6837 HK	2,065	242%	6,056	3%	968	36%	3,230	3%
HTSC	6886 HK	1,736	-9%	6,760	21%	780	-9%	3,042	23%
GFS	1776 HK	1,509	37%	5,355	-5%	681	44%	2,411	1%
CMS	6099 HK	1,858	19%	6,190	24%	820	16%	2,855	29%
SWHY	6806 HK	1,393	-25%	5,251	9%	567	-42%	2,416	14%
CSC	6066 HK	2,110	82%	6,159	61%	1,039	96%	2,930	63%
CGS	6881 HK	1,706	36%	5,560	30%	834	70%	2,452	39%
Total		17,891	23%	60,154	19%	8,110	17%	27,420	19%

Source: Company data, CMBIS

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

Figure 2: Apr 2020 market data recap

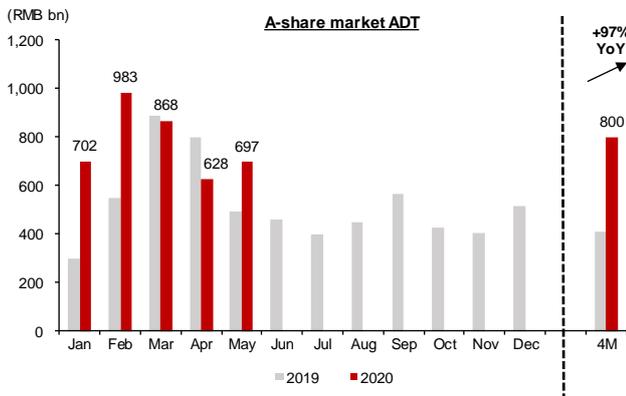
Item	Amount	MoM change	YoY change
Trading data (RMB bn, except for trading days)			
A-share ADT	628	-28%	-22%
A-share trading days	21	-5%	0%
Northbound net inflows	53	N/A*	N/A*
Margin financing & securities lending (daily avg. balance)	1,059	-4%	9%
Index performance (month-end)			
CSI 300 Index	3,913	6%	0%
ChiNext Index	2,069	11%	27%
ChinaBond Aggregate Return Index	132	1.1%	6.4%
Underwriting amount (RMB bn)			
Equity financing	128	11%	-24%
Incl. IPO	19	87%	112%
Incl. Placement & rights issue	80	-4%	117%
Debt financing	919	-14%	25%
Incl. Enterprise bonds	63	17%	62%
Incl. Corporate bonds	376	-18%	60%
Incl. ABS	131	5%	-4%

Source: Wind, CMBIS

*: Northbound recorded net outflow of RMB 68bn and RMB 18bn in Mar 2020 and Apr 2019, respectively.

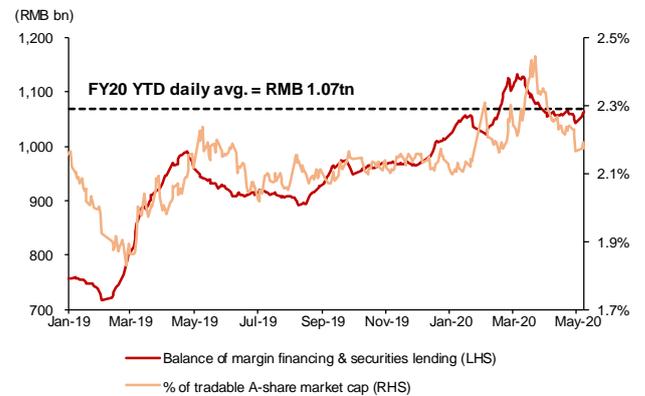
FY20 YTD market indicators in charts

Figure 3: A-share ADT shrank since late-Mar and was 22% lower YoY in Apr while bounced back in May



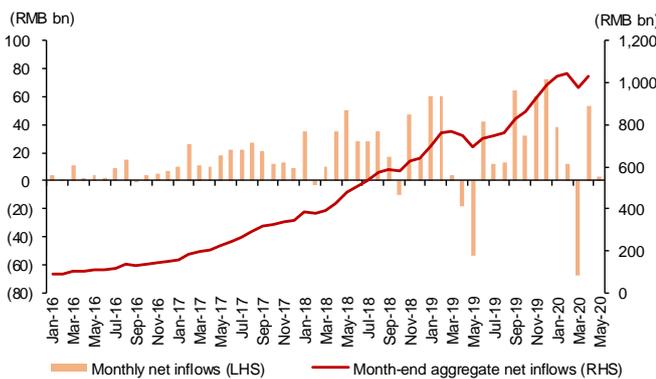
Source: Wind, CMBIS
Note: May 2020 data as of 11 May 2020.

Figure 4: Margin financing and securities lending balance slightly fell below FY20 YTD daily avg.



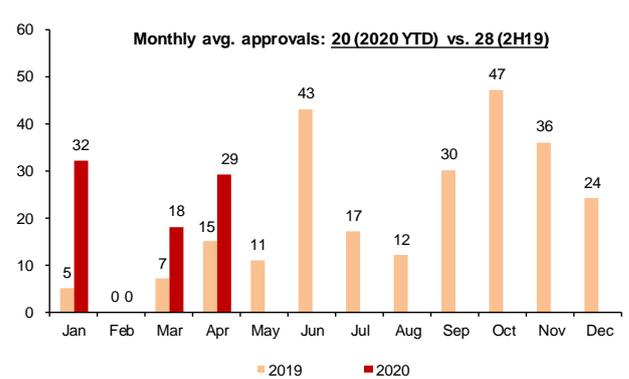
Source: Wind, CMBIS
Note: May 2020 data as of 8 May 2020.

Figure 5: Northbound saw strong net inflows in Apr after market shock in Mar



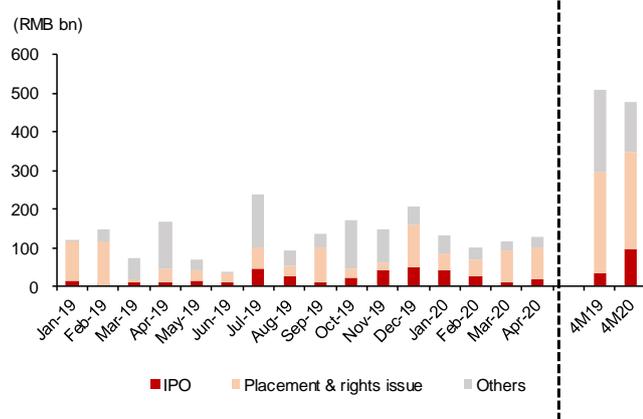
Source: Wind, CMBIS
Note: Apr 2020 data as of 8 Apr 2020.

Figure 6: Monthly no. of IPO approvals resumed to 2H19 level in Apr



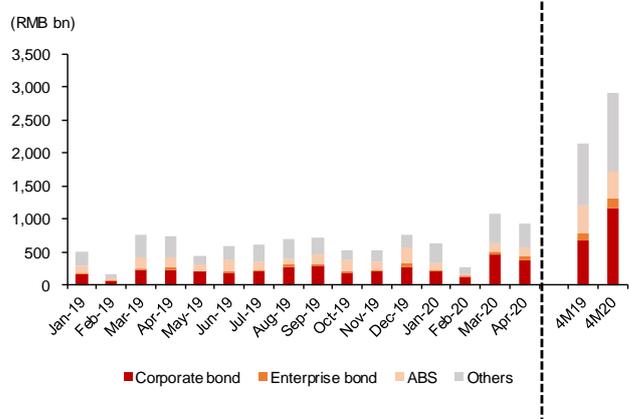
Source: Wind, CMBIS

Figure 7: IPO underwriting amount growth momentum remained strong (4M20 +183% YoY)



Source: Wind, CMBIS

Figure 8: Debt underwriting amount supported by robust corp. bond issuance (4M20 +74% YoY)



Source: Wind, CMBIS

Figure 9: 1Q20 results comp of covered China brokers

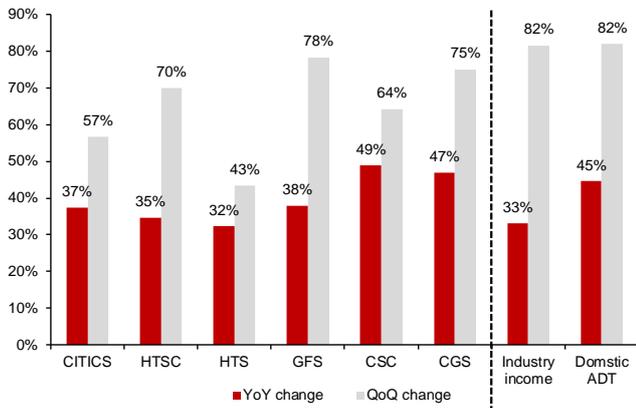
(RMB mn)	CITICS	HTSC	HTS	GFS	CSC	CGS
I/S						
Brokerage commissions	2,680	1,515	1,269	1,604	1,077	1,682
Investment banking fees	891	382	730	270	738	131
Asset mgmt. fees	1,617	847	661	1,243	156	154
Net interest income	313	446	1,160	890	333	963
Prop-trading gains	5,724	2,500	1,254	1,148	1,882	1,635
Other incomes	348	1,015	1,096	102	138	17
Adj. op. revenue	11,575	6,705	6,169	5,257	4,324	4,582
YoY growth	16%	11%	-26%	-22%	39%	27%
QoQ growth	20%	-2%	-20%	-1%	9%	20%
Adj. op. expenses	(4,444)	(2,915)	(2,284)	(2,421)	(1,722)	(2,153)
PPoP	7,130	3,790	3,885	2,837	2,602	2,428
Provision	(1,597)	(17)	(732)	(90)	(108)	(145)
YoY growth	-12792%	388%	176%	-31%	-125%	-370%
QoQ growth	0%	-86%	-33%	-56%	-307%	-59%
Pre-tax profit	5,533	3,773	3,153	2,747	2,494	2,284
Income tax expense	(1,310)	(863)	(870)	(580)	(536)	(503)
Net profit	4,076	2,888	2,283	2,071	1,951	1,754
YoY growth	-4%	4%	-39%	-29%	31%	14%
QoQ growth	139%	13%	7%	8%	16%	28%
B/S						
Margin accounts	77,241	70,658	55,044	57,930	29,297	58,260
Reverse repos	52,483	21,325	54,504	18,650	20,724	28,650
Financial investment	424,495	301,508	263,676	216,208	135,576	147,640
YoY growth	48%	69%	16%	14%	32%	36%
QoQ growth	7%	6%	6%	12%	6%	22%
Borrowings and bonds	195,050	105,993	297,957	131,745	92,405	108,010
YoY growth	33%	17%	15%	4%	39%	9%
QoQ growth	4%	18%	9%	25%	9%	13%
Key ratios						
ROE	9.6%	9.3%	7.2%	9.0%	13.5%	9.8%
YoY growth	-1.3ppt	-1.3ppt	2.5ppt	-4.5ppt	1.2ppt	0.6ppt
QoQ growth	5.4ppt	0.9ppt	0.4ppt	0.6ppt	1.5ppt	2.0ppt
ROA	1.9%	2.0%	1.4%	2.0%	2.7%	2.1%
YoY growth	-0.7ppt	-0.7ppt	0.4ppt	-0.9ppt	-0.1ppt	-0.2ppt
QoQ growth	1.0ppt	0.1ppt	0.0ppt	0.0ppt	0.2ppt	0.3ppt
Financial leverage	4.2x	3.9x	4.6x	3.7x	3.8x	3.8x
YoY growth	0.8x	0.6x	0.3x	0.0x	0.3x	0.5x
QoQ growth	0.0x	0.1x	0.2x	-0.2x	0.5x	0.5x
Investment yield	5.6%	3.4%	2.0%	2.2%	5.7%	4.9%
YoY growth	-1.1ppt	-2.0ppt	-0.8ppt	-5.2ppt	1.0ppt	-0.8ppt
QoQ growth	0.9ppt	-1.4ppt	-3.2ppt	-0.8ppt	1.0ppt	-0.5ppt
Cost-to-income ratio	38%	43%	36%	45%	39%	46%
YoY growth	-4ppt	4ppt	-21ppt	8ppt	-10ppt	1ppt
QoQ growth	-19ppt	-9ppt	-8ppt	-2ppt	-8ppt	1ppt

Source: Company data, CMBIS

Covered brokers' 1Q20 results comparison by business lines

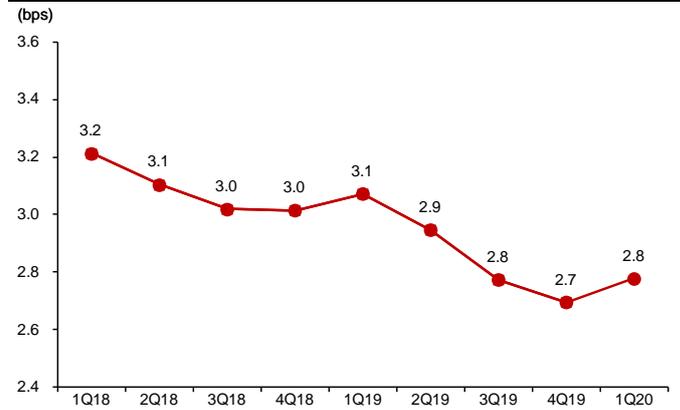
■ **Brokerage business: Overall improvement while retail-focused brokers winning bigger**

Figure 10: 1Q20 brokerage commission increased both YoY and QoQ for covered brokers



Source: Company data, Wind, CMBIS

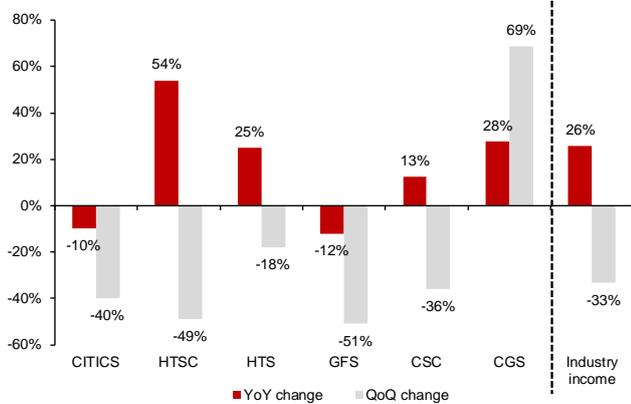
Figure 11: Industry commission rate stabilized as market ADT soared in 1Q20



Source: Wind, CMBIS

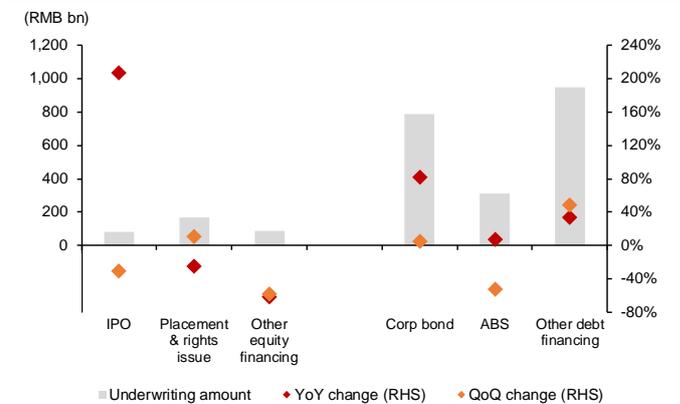
■ **Investment banking business: Mega IPO and corp. bond underpinned the growth; STAR Market and ChiNext the next boosters**

Figure 12: 1Q20 investment banking fee diverged mainly on different bases



Source: Company data, Wind, CMBIS

Figure 13: IPO amount was largely boosted by a mega deal and corp. bond issuance grew robustly in 1Q20



Source: Wind, CMBIS

Note: The IPO of Beijing-Shanghai High Speed Railway (raising RMB 30.7bn) accounted for 39% of total IPO amount in 1Q20.

Figure 14: 1Q20 domestic equity underwriting league table of covered brokers

Rank(#)	1Q20 Company	Total equity underwriting		IPO underwriting	
		market share	YoY amount change	market share	YoY amount change
1	CSC	23.6%	103%	7.0%	1511%
2	CITICS	19.9%	-6%	18.0%	47%
3	CICC	5.6%	-16%	23.9%	1563%
7	HTSC	4.1%	-50%	2.7%	-66%
14	HTS	1.3%	103%	1.4%	-100%
15	GFS	1.1%	-81%	3.6%	136%
29	CGS	0.6%	-53%	0.2%	-70%

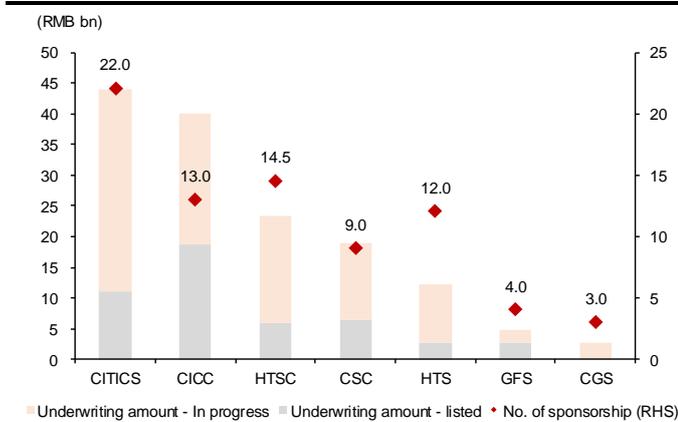
Source: Wind, CMBIS

Figure 15: 1Q20 domestic debt underwriting league table of covered brokers

Rank(#)	1Q20 Company	Total debt underwriting		Corp. bond underwriting	
		market share	YoY amount change	market share	YoY amount change
1	CSC	13.1%	56%	13.6%	52%
2	CITICS	12.6%	51%	8.3%	78%
4	HTS	5.4%	56%	5.2%	225%
5	CICC	4.7%	-5%	3.9%	117%
6	HTSC	4.7%	57%	3.1%	176%
11	GFS	2.0%	-23%	1.2%	10%
23	CGS	1.0%	49%	0.3%	-71%

Source: Wind, CMBIS

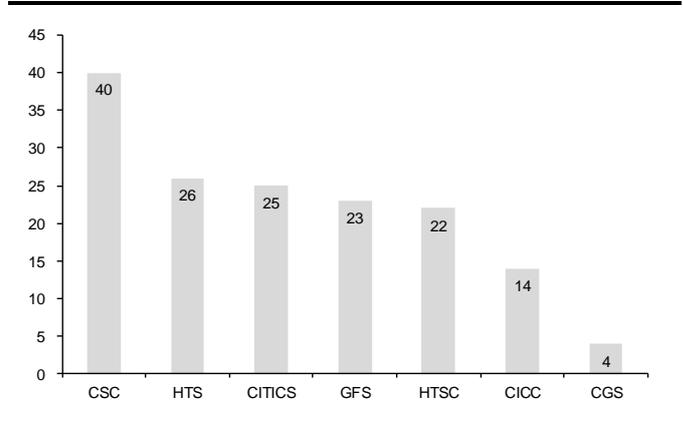
Figure 16: STAR Market IPOs completed and in pipelines of covered brokers YTD in FY20



Source: SSE, Wind, CMBIS

Note: 0.5 indicates joint sponsorship; data as of 11 May 2020.

Figure 17: ChiNext Board IPO pipeline of covered brokers

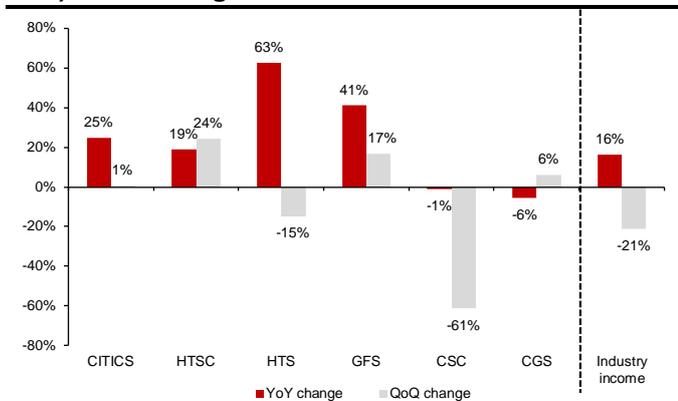


Source: SSE, Wind, CMBIS

Note: data as of 11 May 2020.

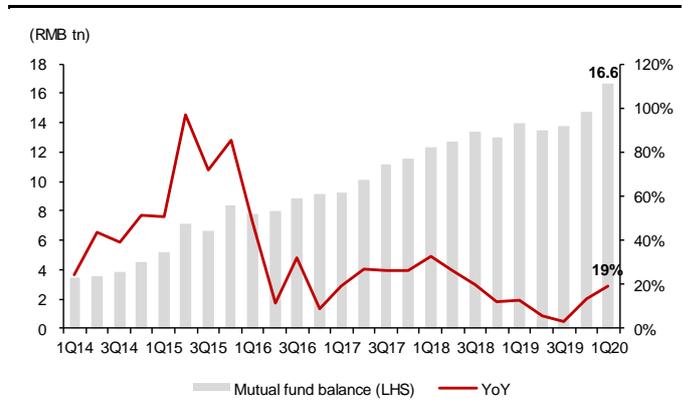
Asset management business: mutual fund subsidiaries and active mgmt. capabilities made the difference

Figure 18: Brokers with fund mgmt. subsidiaries (e.g. CITICS & GFS) and with higher active AUM (e.g. HTSC, HTS) saw better growth in 1Q20



Source: Company data, Wind, CMBIS

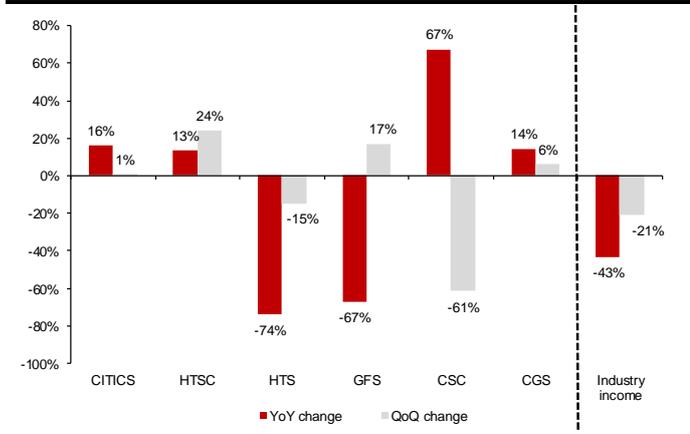
Figure 19: Mutual fund balance reached historical high at RMB 16.6tn by 1Q20, +19% YoY



Source: Wind, CMBIS

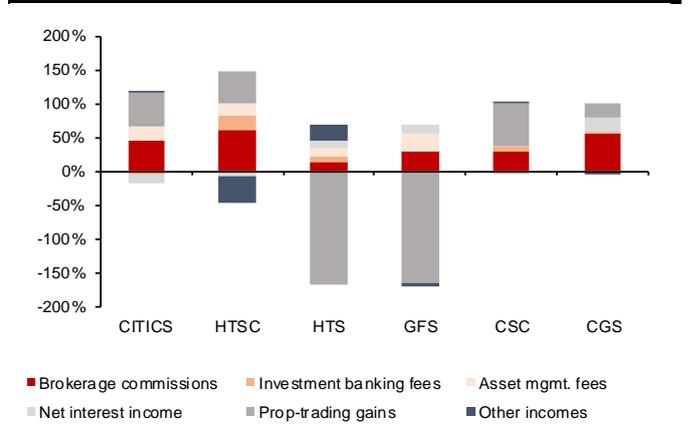
■ Prop-trading gains: diverged performance amid market volatility

Figure 20: 1Q20 prop-trading gains diverged among covered brokers; YoY decrease largely on FV losses



Source: Company data, CMBIS

Figure 21: Prop-trading gains continued to be the key factor affecting brokers' top line growth in 1Q20

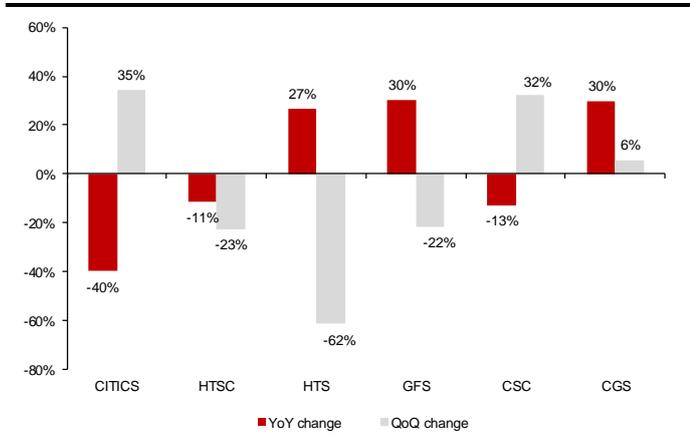


Source: Company data, CMBIS

Note: measured by net YoY changes in amount of each business lines/net change in total op. revenue

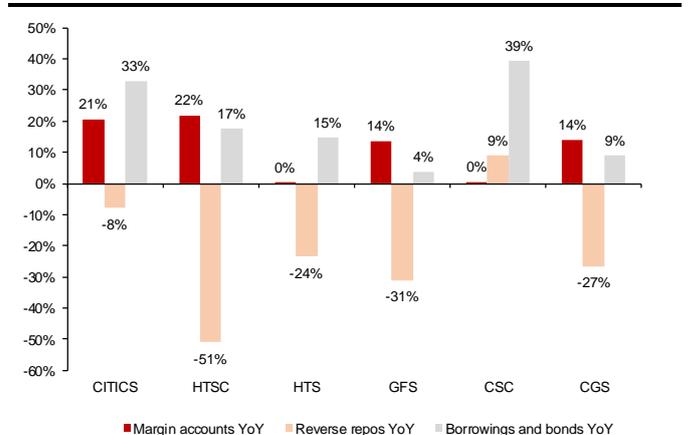
■ Credit business: Increased leverage outpacing credit asset growth amid monetary easing; impairment losses impact limited

Figure 22: Some brokers saw negative NII growth largely due to interest expenses outpacing incomes in 1Q20



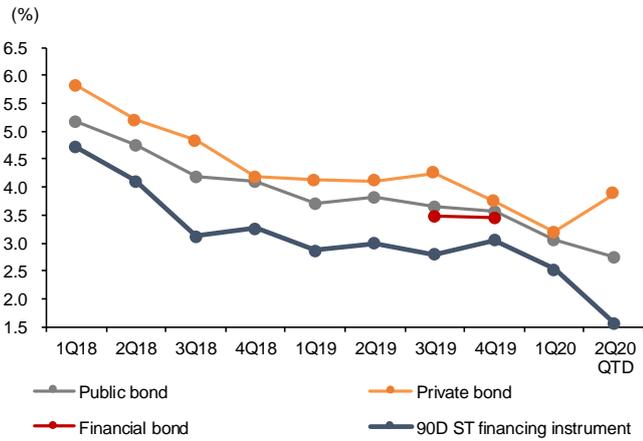
Source: Company data, CMBIS

Figure 23: Brokers increased margin balance and active financing while cutting down on SPL YoY in 1Q20



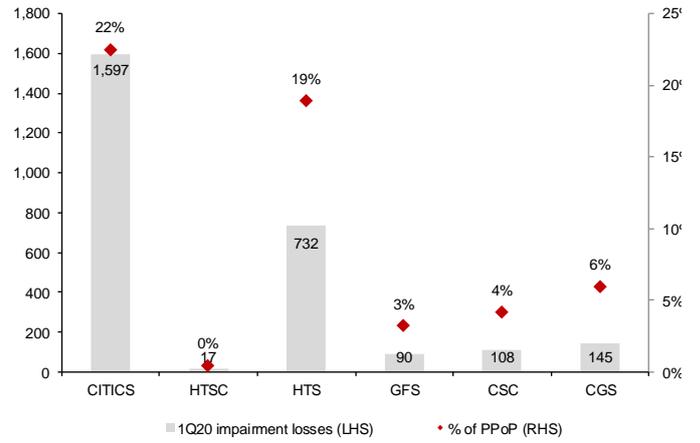
Source: Company data, CMBIS

Figure 24: Brokers funding costs kept decreasing amid monetary easing



Source: Wind, CMBIS
 Note: all public/private/financial bonds with AAA issuer rating and 3-year maturity; data as of 11 May 2020.

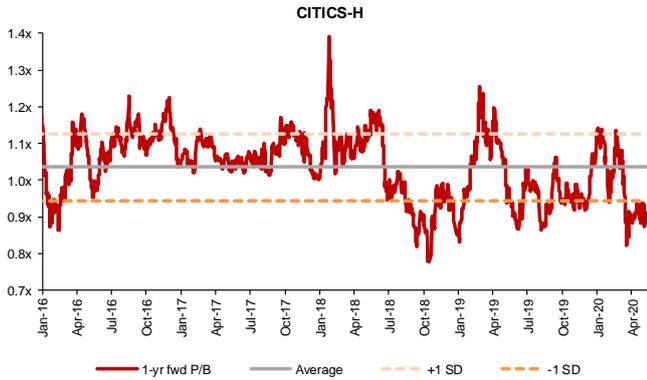
Figure 25: Most brokers experienced limited provision impact in 1Q20 except CITICS and HTS



Source: Company data, CMBIS

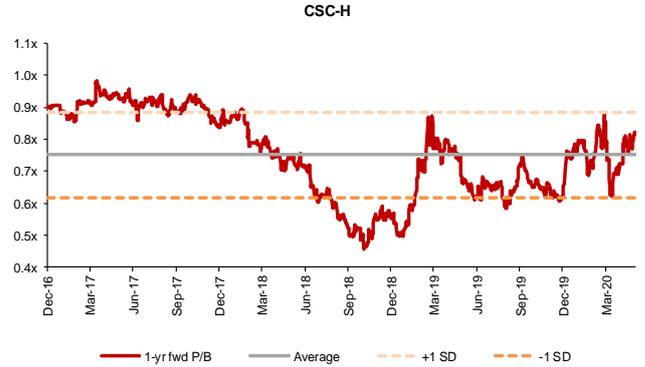
Valuation of H-share China brokers (since 2016)

Figure 26: CITICS's 1-yr forward P/B



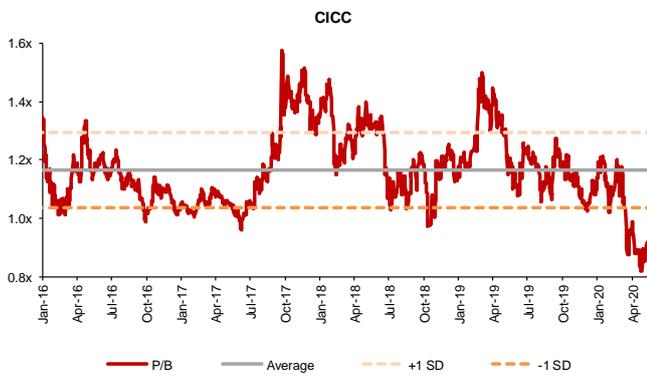
Source: Bloomberg, CMBIS estimates

Figure 27: CSC's 1-yr forward P/B



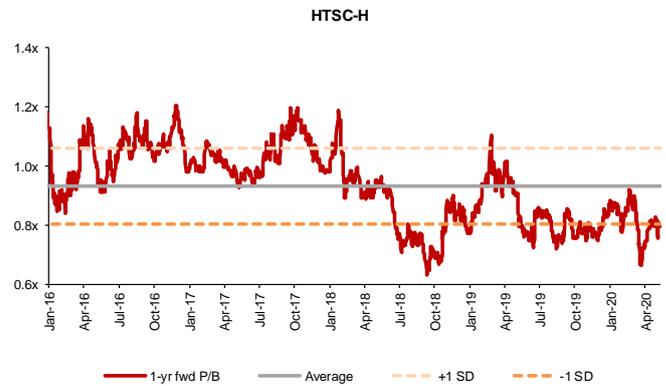
Source: Bloomberg, CMBIS estimates

Figure 28: CICC's 1-yr forward P/B



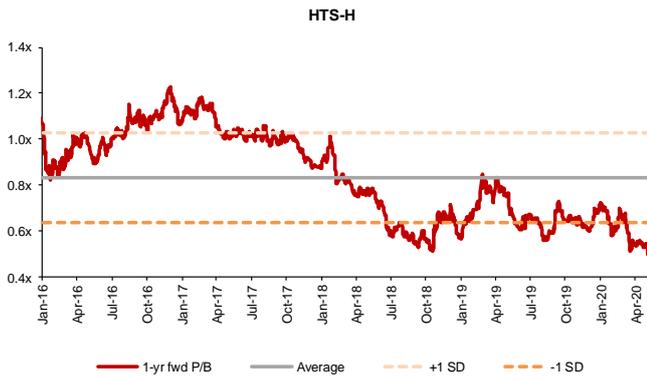
Source: Bloomberg, CMBIS estimates

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



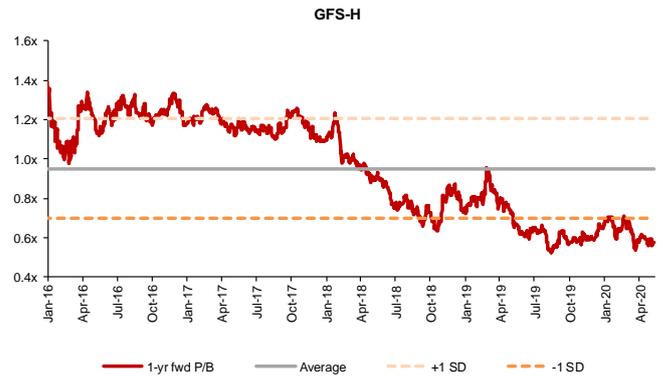
Source: Bloomberg, CMBIS estimates

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



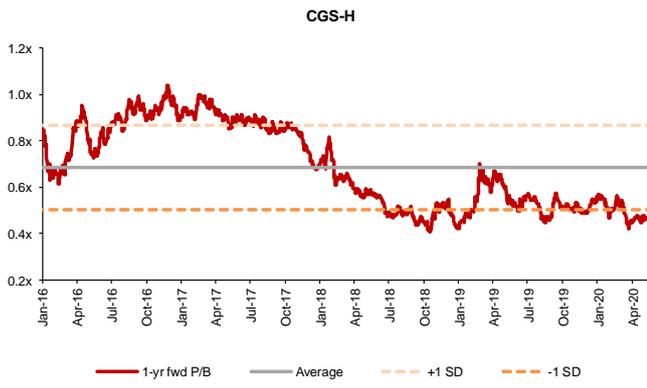
Source: Bloomberg, CMBIS estimates

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



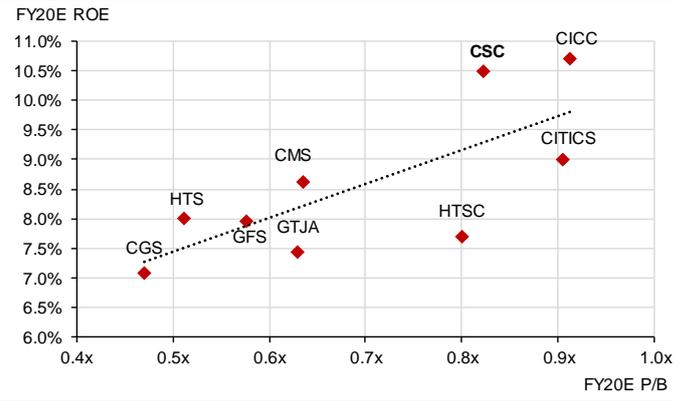
Source: Bloomberg, CMBIS estimates

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



Source: Bloomberg, CMBIS estimates

Figure 33: China brokers' P/B vs. ROE



Source: Bloomberg

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