

# GF Securities (1776 HK)

## 4Q19 slight beat on stronger investment banking

GFS reported FY19 net profit of RMB 7.5bn, up 75% YoY, 4%/5% above CMBIS/consensus estimates. FY19 operating revenue grew 46% YoY to RMB 20.5bn, mainly fueled by a 10.7x rebound of prop-trading gains from low base in FY18, while impairment losses surged 125% YoY largely from debt investments. 4Q19 results surprised us on higher investment banking fees. We maintain HOLD on GFS as it is not a principal beneficiary of policy tailwinds, in our view.

■ **Results positives: 1) Investment banking fees +49% QoQ in 4Q19**, primarily on 153% QoQ increase in equity financing underwriting amount, with four STAR Market IPOs listed in 4Q19. GFS has completed another two sponsored IPOs on the new board in 1Q20E, and now has no active sponsorship in its STAR Market pipeline. The Company may need to catch up as we still see STAR Market as major IPO supply in FY20E. **2) Prop-trading gains +23% QoQ** on better A-share stock market performance towards year-end. **3) Asset mgmt. fees +25% QoQ**, likely partly due to higher performance fees. AM business's total AUM was still contracting under tighter regulations (-22% YoY/-15% HoH at YE FY19), while higher proportion of actively managed AUM improved fee rates. GFS obtained approvals for two CAM products to transform into mutual funds in Nov 2019, which may help stabilize its AUM trend. **4) Net interest income +14% QoQ**, vs. most peers seeing a sequential decline. We believe this was resulted from higher interest income as margin financing balance expanded 8% QoQ, and lower interest expenses as total debts decreased 6% QoQ. GFS was one of few brokers under our coverage lowering its leverage, of which the YE adj. financial leverage decreased 0.4x from 3.9x in FY18 to 3.5x in FY19.

■ **Results negatives: 1) Brokerage commission -9% QoQ**, vs. -8% domestic stock market turnover trend. We estimated both market share loss (-0.3ppt) and slightly lower commission rate in 2H19. **2) Impairment losses surged 18x QoQ in 4Q19 and 125% YoY in FY19**. 2H19 impairment losses halved HoH though, those from GFS's leasing subsidiary were likely the main components.

■ **Maintain HOLD**. GFS currently trades at 0.58x 1-year forward P/B, close to its historical trough (0.52x). Though the valuation is very low, we see limited catalysts ahead for an upward re-rating. We made no changes to our earnings forecast, and maintain HOLD rating on GFS with TP at HK\$ 8.90.

### Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. op. revenue (RMB mn)	14,035	20,486	20,457	22,379	24,398
Net profit (RMB mn)	4,300	7,539	7,431	8,238	9,148
EPS (RMB)	0.56	0.99	0.98	1.08	1.20
EPS CHG (%)	(50)	75	(1)	11	11
Consensus EPS (RMB)	N/A	N/A	1.02	1.14	N/A
P/E (x)	13.2	7.5	7.6	6.9	6.2
P/B (x)	0.67	0.62	0.58	0.55	0.51
Yield (%)	0.0	6.9	3.9	4.4	4.8
ROE (%)	5.1	8.6	7.9	8.2	8.6
Financial leverage (x)	3.9	3.5	3.4	3.4	3.5

Source: Company data, Bloomberg, CMBIS estimates

### HOLD (Maintain)

Target Price	HK\$ 8.90
(Previous TP	HK\$ 8.90)
Up/Downside	+7.2%
Current Price	HK\$ 8.30

### China Brokerage Sector

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#### Stock Data

Mkt Cap (HK\$ mn)	104,114
Avg 3 mths t/o (HK\$ mn)	70.90
52w High/Low (HK\$)	11.74/7.24
Total Issued Shares (mn)	1,702 (H)
	5,919 (A)

Source: Wind

#### Shareholding Structure

Jilin Aodong	16.43%
Liaoning Cheng Da	16.40%
Zhongshan Public Utilities	9.01%

Source: Company data

#### Share Performance

	Absolute	Relative
1-mth	-10.9%	-0.9%
3-mth	-9.5%	8.8%
6-mth	5.4%	16.5%

Source: Wind

#### 12-mth Price Performance



Source: Wind

#### Auditor: Ernst & Young

#### Related Reports

1. "On an upward policy trajectory" – 19 Mar 2020
2. "COVID-19 unlikely to derail industry upswing" – 12 Feb 2020
3. "Policy implementation to light up the road ahead" – 18 Dec 2019
4. "Prop trading gains offset by weakness across other businesses" – 30 Oct 2019
5. "Higher earnings visibility given favorable policy environment" – 6 Sep 2019

**Figure 1: GFS's 4Q19 results summary**

(RMB mn)											vs. CMBIS est.
I/S	1Q19	2Q19	3Q19	4Q19	QoQ	4Q18	YoY	FY18	FY19	YoY	
Net fee and commissions	2,420	2,524	2,251	2,566	14%	2,186	17%	8,619	9,761	13%	4%
Brokerage	1,163	1,152	984	900	-9%	922	-2%	3,453	4,198	22%	0%
Investment banking	307	214	369	548	49%	211	159%	1,216	1,438	18%	26%
Asset Management	880	1,113	854	1,063	25%	1,025	4%	3,743	3,911	4%	0%
Net interest income	683	855	761	869	14%	988	-12%	3,689	3,168	-14%	1%
Prop trading gains	3,495	537	1,190	1,465	23%	(15)	N/A	571	6,687	1071%	2%
<b>Adj. op. revenue</b>	<b>6,704</b>	<b>4,099</b>	<b>4,390</b>	<b>5,294</b>	<b>21%</b>	<b>3,745</b>	<b>41%</b>	<b>14,035</b>	<b>20,486</b>	<b>46%</b>	<b>4%</b>
Adj. op. expenses	(2,554)	(2,136)	(2,270)	(2,568)	13%	(1,885)	36%	(7,727)	(9,528)	23%	7%
<b>PPoP</b>	<b>4,150</b>	<b>1,963</b>	<b>2,119</b>	<b>2,725</b>	<b>29%</b>	<b>1,860</b>	<b>47%</b>	<b>6,308</b>	<b>10,957</b>	<b>74%</b>	<b>2%</b>
Provision	(130)	(334)	(11)	(206)	1821%	(69)	196%	(303)	(681)	125%	12%
<b>Pre-tax profit</b>	<b>4,019</b>	<b>1,629</b>	<b>2,109</b>	<b>2,520</b>	<b>19%</b>	<b>1,790</b>	<b>41%</b>	<b>6,004</b>	<b>10,276</b>	<b>71%</b>	<b>2%</b>
Income tax expense	(845)	(363)	(485)	(473)	-2%	(329)	44%	(1,372)	(2,166)	58%	-3%
<b>Net profit</b>	<b>2,919</b>	<b>1,221</b>	<b>1,476</b>	<b>1,923</b>	<b>30%</b>	<b>1,332</b>	<b>44%</b>	<b>4,300</b>	<b>7,539</b>	<b>75%</b>	<b>4%</b>
<b>B/S</b>	<b>1Q19</b>	<b>2Q19</b>	<b>3Q19</b>	<b>4Q19</b>	<b>QoQ</b>	<b>4Q18</b>	<b>YoY</b>	<b>FY18</b>	<b>FY19</b>	<b>YoY</b>	
Margin accounts	50,959	48,757	50,767	54,787	8%	45,355	21%	45,355	54,787	21%	
Financial investment	189,400	191,517	190,893	193,368	1%	185,492	4%	185,492	193,368	4%	
Reverse repos	27,043	28,859	18,585	20,689	11%	36,813	-44%	36,813	20,689	-44%	
Customer deposits	88,770	82,062	77,744	79,681	2%	58,445	36%	58,445	79,681	36%	
Total shareholder's equity	88,784	89,912	91,422	91,234	0%	85,018	7%	85,018	91,234	7%	
<b>Ratios</b>	<b>1Q19</b>	<b>2Q19</b>	<b>3Q19</b>	<b>4Q19</b>	<b>QoQ</b>	<b>4Q18</b>	<b>YoY</b>	<b>FY18</b>	<b>FY19</b>	<b>YoY</b>	
ROE	13.4%	5.5%	6.5%	8.4%	1.9ppt	6.3%	2.2ppt	5.1%	8.6%	3.5ppt	
ROA	2.9%	1.2%	1.5%	2.0%	0.5ppt	1.4%	0.6ppt	1.2%	1.9%	0.8ppt	
Leverage	3.7x	3.6x	3.4x	3.5x	0.1x	3.9x	-0.4x	3.9x	3.5x	-0.4x	
Investment yield*	7.5%	1.1%	2.5%	3.0%	0.6ppt	0.7%	2.4ppt	2.4%	5.4%	3.0ppt	
Cost-to-income ratio	38%	51%	51%	48%	-3ppt	50%	-2ppt	54%	46%	-8ppt	

Source: Company data, CMBIS

\*: include interest income from debt/other debt investments when calculating full-year yield.

## Financial Summary

### Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Brokerage commission	3,453	4,198	5,208	5,704	6,237
Investment banking fee	1,216	1,438	1,201	1,280	1,339
Asset management fee	3,743	3,911	4,059	4,363	4,821
Net interest income	3,689	3,168	3,498	3,745	4,126
Prop-trading gains	571	6,687	5,693	6,413	7,001
Others	1,363	1,084	799	874	874
<b>Adj. op. revenue</b>	<b>14,035</b>	<b>20,486</b>	<b>20,457</b>	<b>22,379</b>	<b>24,398</b>
Adj. op. expenses	(7,727)	(9,528)	(9,465)	(10,246)	(11,108)
PPoP	6,308	10,957	10,992	12,133	13,290
Provision	(303)	(681)	(427)	(342)	(205)
Pre-tax profit	6,004	10,276	10,565	11,791	13,085
Income tax expense	(1,372)	(2,166)	(2,372)	(2,695)	(2,991)
Minority interests	(332)	(571)	(762)	(859)	(947)
<b>Net profit</b>	<b>4,300</b>	<b>7,539</b>	<b>7,431</b>	<b>8,238</b>	<b>9,148</b>

### Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Deposit held on behalf of clients	39,515	58,366	66,646	73,021	80,323
Clearing reserves	17,900	19,548	24,630	27,586	30,344
Margin accounts	45,355	54,787	57,896	61,949	65,666
Reverse repos	36,813	20,689	18,377	19,296	20,261
Financial investments	185,492	193,368	216,358	229,340	238,513
Other assets	64,030	47,632	37,764	40,881	46,429
<b>Total assets</b>	<b>389,106</b>	<b>394,391</b>	<b>421,671</b>	<b>452,072</b>	<b>481,536</b>
Customer brokerage deposits	58,445	79,681	87,306	95,657	105,223
Short-term debts	127,216	114,299	103,859	109,949	115,298
Long-term debts	74,170	86,213	105,631	113,998	120,569
Other liabilities	40,646	20,062	23,701	24,923	25,833
<b>Total liabilities</b>	<b>300,477</b>	<b>300,254</b>	<b>320,498</b>	<b>344,527</b>	<b>366,924</b>
<b>Shareholders' fund</b>	<b>85,018</b>	<b>91,234</b>	<b>97,191</b>	<b>103,365</b>	<b>110,223</b>
Incl. Perpetual bonds	0	0	0	0	0
Minority interest	3,611	2,903	3,981	4,180	4,389

### Key Ratios

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Operating revenue mix</b>					
Brokerage commission	25%	20%	25%	25%	26%
Investment banking fee	9%	7%	6%	6%	5%
Asset management fee	27%	19%	20%	19%	20%
Net interest income	26%	15%	17%	17%	17%
Prop-trading gains	4%	33%	28%	29%	29%
Others	10%	5%	4%	4%	4%
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>
<b>Growth, YoY</b>					
Brokerage commission	-20%	22%	24%	10%	9%
Investment banking fee	-56%	18%	-16%	7%	5%
Asset management fee	-6%	4%	4%	7%	11%
Net interest income	685%	-14%	10%	7%	10%
Prop-trading gains	-94%	1071%	-15%	13%	9%
<b>Adj. op. revenue</b>	<b>-35%</b>	<b>46%</b>	<b>0%</b>	<b>9%</b>	<b>9%</b>
PPoP	-48%	74%	0%	10%	10%
<b>Net profit</b>	<b>-50%</b>	<b>75%</b>	<b>-1%</b>	<b>11%</b>	<b>11%</b>
Total assets	9%	1%	7%	7%	7%
<b>Efficiency</b>					
Cost-to-income ratio	54%	46%	45%	45%	45%
<b>Leverage</b>					
Adj. financial leverage (x)	3.7	3.5	3.4	3.4	3.5
Investment/ equity	218%	212%	223%	222%	216%
<b>Profitability</b>					
ROE	5.1%	8.6%	7.9%	8.2%	8.6%
ROA	1.2%	1.9%	1.8%	1.9%	2.0%
<b>Per share</b>					
EPS (RMB)	0.56	0.99	0.98	1.08	1.20
DPS (RMB)	0.00	0.30	0.29	0.32	0.36
BVPS (RMB)	11.16	11.97	12.75	13.56	14.46

Source: Company data, CMBIS estimates

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