



January 27, 2015  
 Company Report  
 Rating: BUY  
 TP: HK\$ 22.20

Share price (HK\$)	17.48
Est. share price return	27.0%
Est. dividend yield	2.0%
Est. total return	29.0%

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**Key Data**

52Wk H/L(HK\$)	23.2/9.5
Issued shares (mn)	
H-share	1,492.6
A-share	8,902.1
Market cap	
H-share (HK\$m)	26,091
A-share (HK\$m)	214,497
3-mth avg daily turnover (HK\$ mn)	777
Major shareholder(s) (%):	
Bright Food (Group) Co., Ltd.	4.40

Source(s): Company, Bloomberg, ABCI Securities

**1H14 Revenue breakdown (%)**

Brokerage	35
Headquarters and others	20
Proprietary Trading	15
Overseas	9
Investment Banking	7
Financial lease	7
Asset management	5
Direct investment	2

Source(s): Company, ABCI Securities

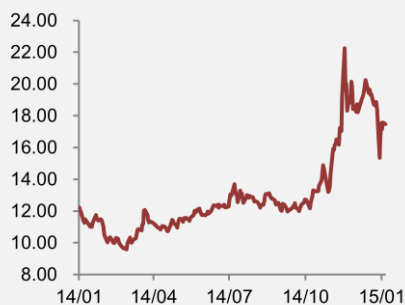
**Share performance (%)**

	Absolute	Relative*
1-mth	-4.06	-10.07
3-mth	40.06	32.25
6-mth	27.59	25.13

\*Relative to HSI

Source(s): Bloomberg, ABCI Securities

**1-Year stock performance (HK\$)**



Source(s): Bloomberg, ABCI Securities

# Haitong Securities (6837 HK)

## Strong growth momentum by multiple drivers

- According to Wind, HTS was ranked 5<sup>th</sup> by brokerage trading volume in 2014. MFSL balance grew 188% from end-Dec 2013 to RMB 57.2bn by end-Dec 2014, ranking 7<sup>th</sup> in the market.
- Commenced finance lease business in 2014 by acquiring UT Capital; the operation contributed to 6.23% of total profits in 1H14.
- Initiate coverage with **BUY**; our DDM-derived TP of HK\$ 22.20 implies 2.0x 2015E P/B

**Diversified revenue mix.** Principal lines of business include brokerage, asset management, proprietary trading, investment banking, direct investment, finance lease and overseas operations. HTS commenced the finance lease business in 2014, which further optimizes its revenue mix. According to Wind, HTS was ranked 5<sup>th</sup> by brokerage trading volume in 2014. Also, MFSL balance grew 188% from end-Dec 2013 to reach RMB 57.2bn as at end-Dec 2014, ranking 7<sup>th</sup> in the market.

**Solid investment banking growth.** Driven by A-share IPO resumption, robust growth in secondary offerings, and an active bond market, HTS was ranked 6<sup>th</sup> in terms of fundraising size and issuing scale through equity and bonds in 2014. Net investment banking fee income grew 44% QoQ and 137% YoY in 3Q14. We expect the growth momentum in investment banking business to continue in 2015.

**Finance lease business is ROE accretive.** HTS completed the acquisition of UT Capital, a financing leasing company, in early 2014. During 1H14, the financing lease business achieved a profit of RMB 241mn, accounting for 6.23% of total profits of HTS. We believe the acquisition is ROE accretive to HTS—ROE of UT Capital in 1H14 was ~15%, much higher than the ~9% in HTS. HTS is the only broker in China with a finance leasing platform. We believe the acquisition would continue to drive revenue and profit growth in the future.

**Improved contribution from innovative businesses.** HTS's innovative businesses accounted for 24.3% of revenue in 1H14—a share higher than most Chinese brokers.

**Effective cost control.** HTS has a higher operating efficiency than peers, with the lowest cost-to-income ratio of 58% in 2013, as opposed to 67%, 66% and 78% in CITICS, CGS and CCS, respectively.

**Initiate coverage on HTS with a BUY rating.** HTS is the 2<sup>nd</sup> largest brokers in China by total assets. Based on HTS's multiple business drivers, accelerated overseas expansion, unique finance lease platform, and stringent cost control, we initiate our coverage with a **BUY** rating. Our DDM-derived TP is HK\$ 22.20, implying 2.0x 2015E P/B.

**Risk factors:** 1) Weaker-than-expected A-share market; 2) Slowdown in China's economic growth; 3) Intensifying competition in commission rate; 4) Execution risk on overseas acquisition; 5) EPS dilution risk on share placement.

**Financial Summary**

FY ended Dec 31	2012A	2013A	2014E	2015E	2016E
Revenue (RMB mn)	10,743	12,803	22,441	31,300	41,520
Chg (% YoY)	(1.1)	19.2	75.3	39.5	32.7
Net profit (RMB mn)	3,038	4,035	7,817	10,964	14,845
Chg (% YoY)	(2.1)	32.8	93.7	40.3	35.4
EPS (RMB)	0.32	0.42	0.82	0.95	1.29
Chg (% YoY)	(15.0)	32.8	93.7	16.9	35.4
BVPS (RMB)	6.12	6.42	7.11	9.35	10.32
Chg (% YoY)	26.4	4.8	10.8	31.5	10.3
P/E (x)	44.1	33.2	17.1	14.7	10.8
P/B (x)	2.3	2.2	2.0	1.5	1.4
ROAE (%)	5.7	6.5	11.5	12.0	12.6
ROAA (%)	2.7	2.7	3.4	3.0	2.8
DPS(RMB)	0.12	0.12	0.24	0.29	0.39
Yield (%)	0.9	0.9	1.7	2.0	2.8

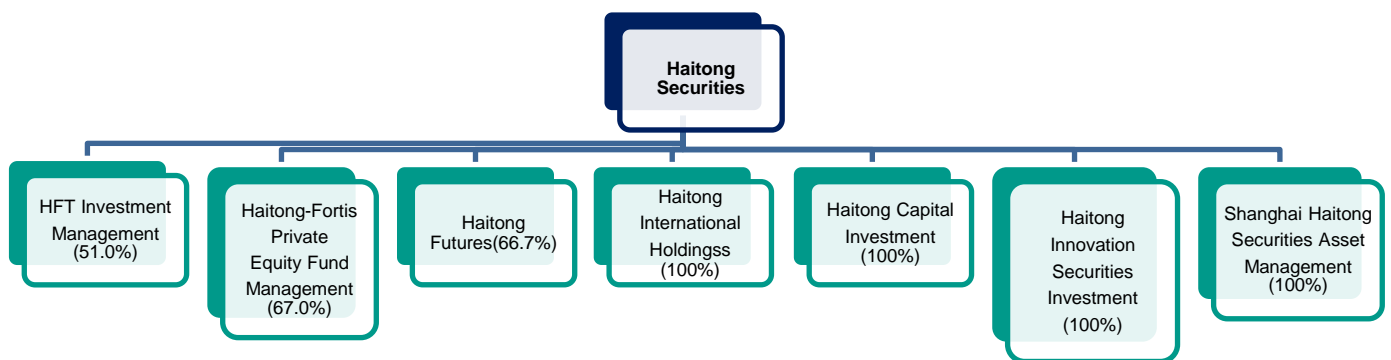
Source(s): Bloomberg, ABCI Securities estimates

## Company Profile

Established in 1988, Haitong Securities (HTS) is the leading full-service securities firm in China. According to the SAC, HTS was ranked 2<sup>nd</sup> by total assets, net assets and total revenue as of Dec 31, 2013. It was ranked No.6 in terms of net incomes from brokerage business and investment banking business. As of end-Sep 2014, HTS has 4.7 mn retail clients and over 20,000 institutional and high net worth clients.

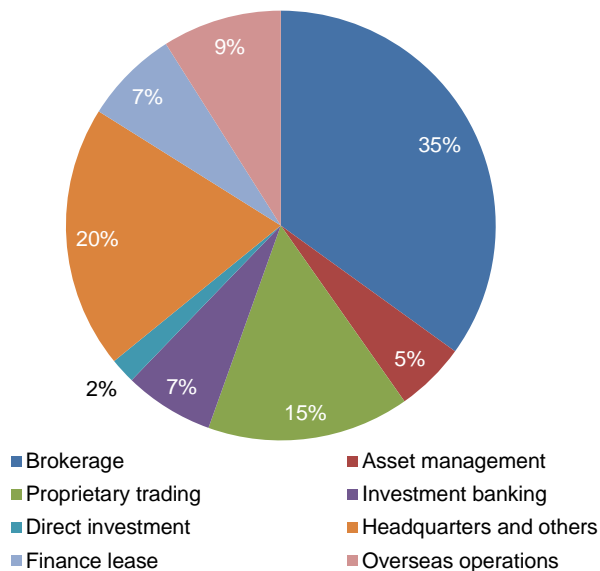
Principal subsidiaries of HTS included HFT Investment Management, Haitong-Fortis Private Equity Fund Management, Haitong Futures, Haitong Int'l Holdings, Haitong Capital Investment, Haitong Innovation Securities Investment, and Shanghai Haitong Securities Asset Management.

**Exhibit 1: HTS's investment in subsidiaries**



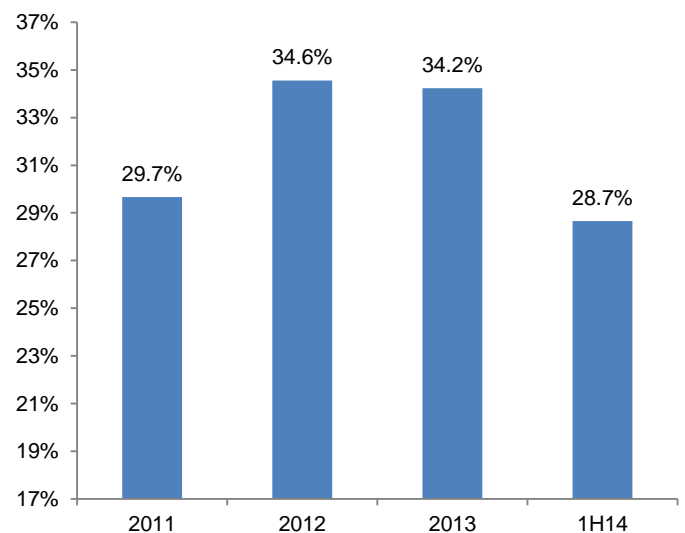
Source(s): Company, ABCI Securities

**Exhibit 2: HTS's revenue mix for 1H14**

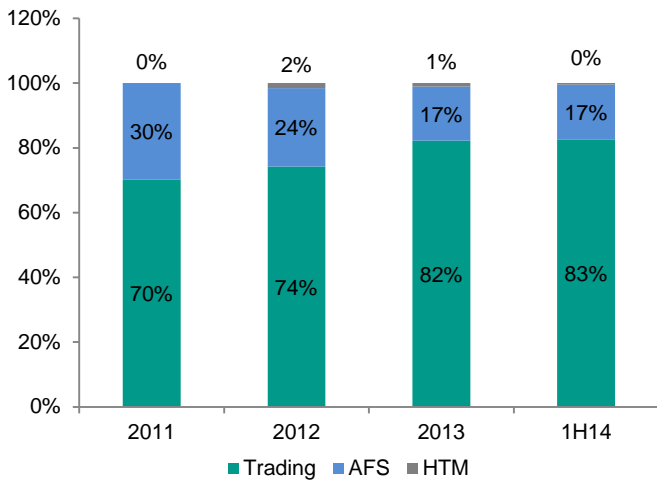


Source(s): Company, ABCI Securities

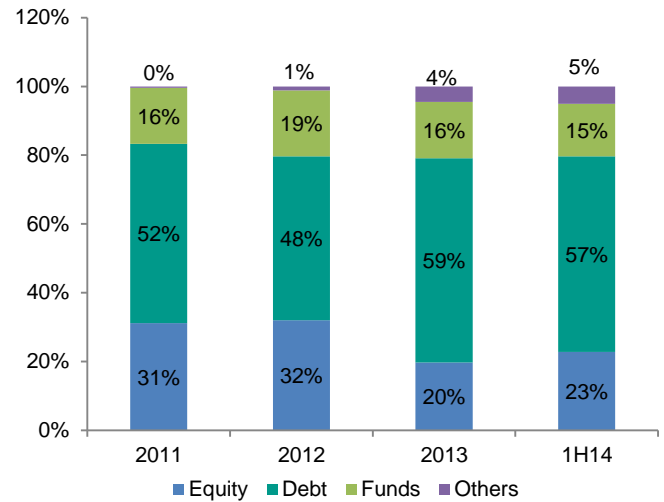
**Exhibit 3: HTS's investment assets as a percentage of total assets**



Source(s): Company, ABCI Securities

**Exhibit 4: Investment assets mix by accounting category**


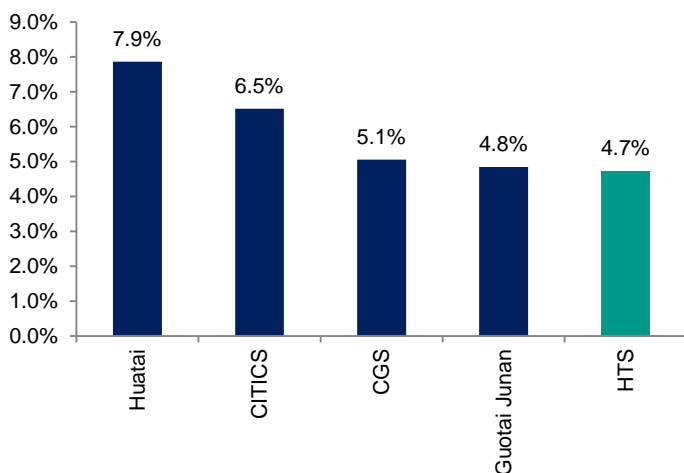
Source(s): Company, ABCI Securities

**Exhibit 5: Investment assets mix by securities category**


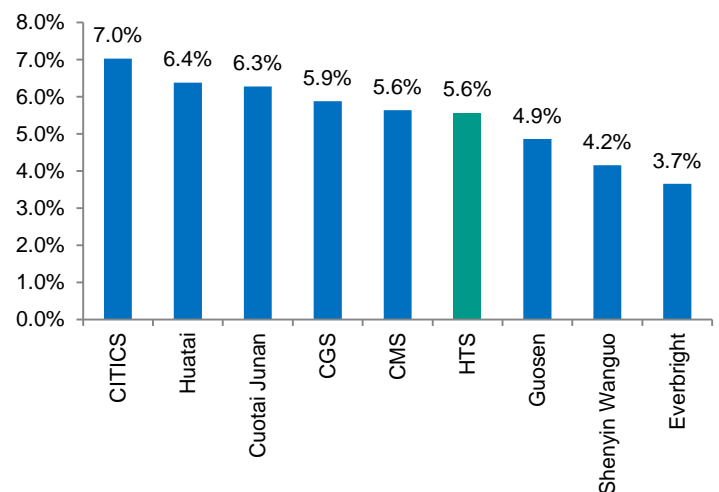
Source(s): Company, ABCI Securities

### Diversified revenue mix

HTS's principal lines of business include brokerage, asset management, proprietary trading, investment banking, direct investment, finance lease and overseas operations. Brokerage (including margin financing and securities lending, or MFSL), the headquarters and others (mainly represents head office operations, investment holding, along with interest income and interest expense incurred for general working capital purpose), proprietary trading, and overseas operations accounted for 35%, 20%, 15% and 9% of total revenue in 1H14. HTS started its finance lease business in 2014, which further optimizes its revenue mix. According to Wind, HTS was ranked 5<sup>th</sup> by brokerage trading volume in 2014. MFSL balance grew 188% from end-Dec 2013 to reach RMB 57.2bn by end-Dec 2014 and was ranked 7<sup>th</sup> in the market.

**Exhibit 6: HTS was ranked 5<sup>th</sup> in brokerage trading volume in 2014**


Source(s): Wind, ABCI Securities

**Exhibit 7: MFSL market share among brokers in 2014**


Source(s): Wind, ABCI Securities



## Solid investment banking growth

Driven by the A-share IPO resumption, robust growth in secondary offerings and an active bond market, Haitong was ranked 6<sup>th</sup> by fundraising size and issuing scale through equity and bonds in 2014. Net investment banking fee income grew 44% QoQ and 137% YoY in 3Q14. 9M14 net investment banking fee income grew 37% YoY. We expect the growth momentum in investment banking business to continue in 2015.

**Exhibit 8: Total equity underwriting amount among brokers in 2014**

Ranking	Brokers	Total underwriting amount (RMB bn)	Market share (%)
2	CITICS	39	7.5%
3	HTS	35	6.7%
9	CGS	17	3.4%

Source(s): Wind, ABCI Securities

**Exhibit 9: Total debt underwriting amount among brokers in 2014**

Ranking	Brokers	Total underwriting amount (RMB bn)	Market share (%)
1	CITICS	272	15.1%
8	HTS	59	3.3%
11	CGS	50	2.8%

Source(s): Wind, ABCI Securities

**Exhibit 10: Summary of leading brokers by underwriting size in 2014**

	Funding raising size/Issuing scale (RMB mn)						No. of underwriting					
	IPO	Secondary offering	Rights issue	CB	Debt	Total	IPO	Secondary offering	Rights issue	CB	Debt	Total
CITICS	6,252	31,817	590	7,206	264,392	310,256	4	20	1	5	194	224
CDB Securities	0	3,117	0	0	182,541	185,658	0	3	0	0	128	131
China Securities	4,232	38,316	0	2,000	105,877	150,425	7	24	0	2	104	137
Guotai Junan	3,529	18,472	3,552	0	90,531	116,084	4	15	2	0	97	118
CICC	2,433	11,691	0	3,333	82,498	99,955	3	11	0	2	51	67
<b>HTS</b>	<b>1,866</b>	<b>31,471</b>	<b>1,398</b>	<b>760</b>	<b>58,465</b>	<b>93,960</b>	<b>4</b>	<b>23</b>	<b>1</b>	<b>1</b>	<b>53</b>	<b>82</b>

Source(s): Company, ABCI Securities



## Finance lease business is ROE accretive

HTS completed the acquisition on UT Capital in early 2014. UT Capital is a financial leasing companies focusing on transportation, medical care, education, printing, and packaging industries. In 1H14, total assets of UT Capital reached RMB 16.8bn, up 26% compared to the start of the year. In 1H14, profit of the financing lease business was RMB 241mn, accounting for 6.23% of total profits of HTS. We believe the acquisition is ROE accretive to HTS, since the ROE of UT Capital in 1H14 was ~15%, compared with ~9% in HTS. So far, HTS is the only broker in China with a finance leasing platform. We believe the acquisition would continue to drive revenue and profit in the future.

## Rising contribution from innovative business

Compared to peers, HTS's innovative businesses account for a much higher proportion of its total revenue. Focusing on businesses in MFSL, stock repo securities, stock collateralized repo and fund custody; the Group is a leader in terms of the number and scale of products offered in the over-the-counter market. Revenue generated from the innovative businesses continued to increase and reached 24.3% in 1H14. HTS had a MFSL balance of ~RMB 57.2bn as of Dec 31, 2014, representing a 5.57% market share in China.

## Overseas business expansion is accelerating

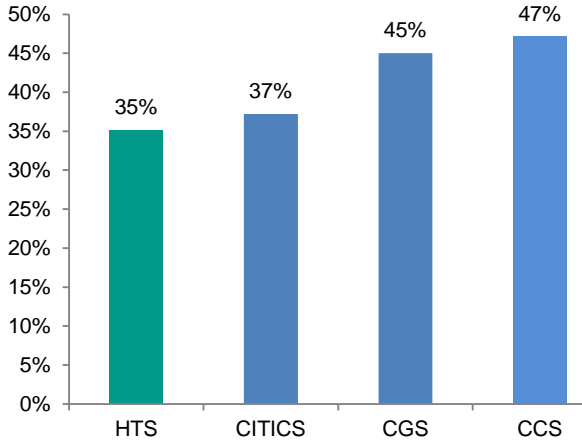
On Dec 4, 2014, HTS announced its wholly-owned subsidiary, Haitong Int'l Holdings, is under discussion with Novo Banco on an acquisition of a 100% stake in the latter's investment banking arm, BESI, at US\$ 467mn. HTS has not entered any formal agreement regarding the acquisition and the deal is currently subject to regulatory approval. BESI employs around 1,000 staff with offices in Lisbon, Sao Paulo, and London, and provides corporate finance, capital markets, project finance, acquisition finance, private equity, asset management in the markets it operates. As of end-June, 2014, BESI had EUR 5.8bn in assets. Due to rising bad debt costs, BESI's ROE in 2013 and 1H14 was low at 1.15% and 0.8%. Its net profit was EUR 2.5mn in 1H14, equivalent to ~0.7% of HTS's 1H14 net profits. HTS is accelerating its overseas expansion to gain global presence and create business synergies. In our view, although the full synergy may not be realized in the short term, the acquisition can broaden HTS's global presence, enhancing its brand while expanding customer base.

## Effective cost control

Comparing the staff cost-to-total expenses ratio among HK-listed brokers, HTS has the lowest ratio of 35.1% in 2013, as opposed to CITICS's 37.2%, CGS's 45.0%, and CCS's 47.1%. In addition, HTS has a higher operating efficiency than peers with the lowest cost-to-income ratio of 58% in 2013, as opposed to 67%, 66% and 78% in CITICS, CGS, and CCS, respectively.

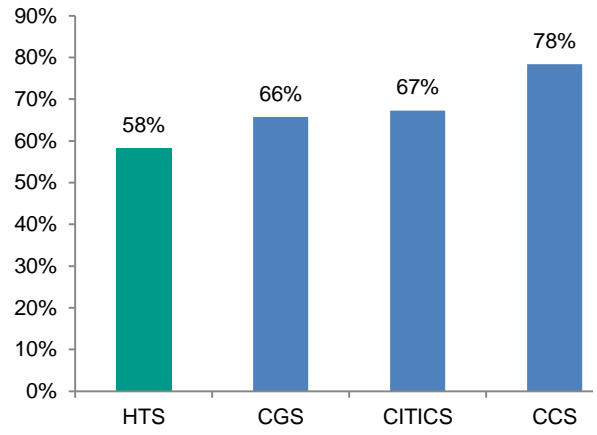


Exhibit 11: Staff cost-to-total expenses comparison (2013)



Sources: Company, ABCI Securities

Exhibit 12: Cost-to-income comparison (2013)



Sources: Company, ABCI Securities



### Valuation

HTS is the 2<sup>nd</sup> largest broker in China by asset size at end-2013, its diversified revenue mix and robust growth in innovative business, which reduce its reliance on traditional fee-based business.

We derive the fair value for HTS by applying the 3-stage dividend discount model (DDM). Our derived TP of HK\$ 22.20 is based on the 2015E BVPS. We assume a cost of equity at 14.0%, a long-term growth rate of 7.6%, and a sustainable ROAE of 19.0%.

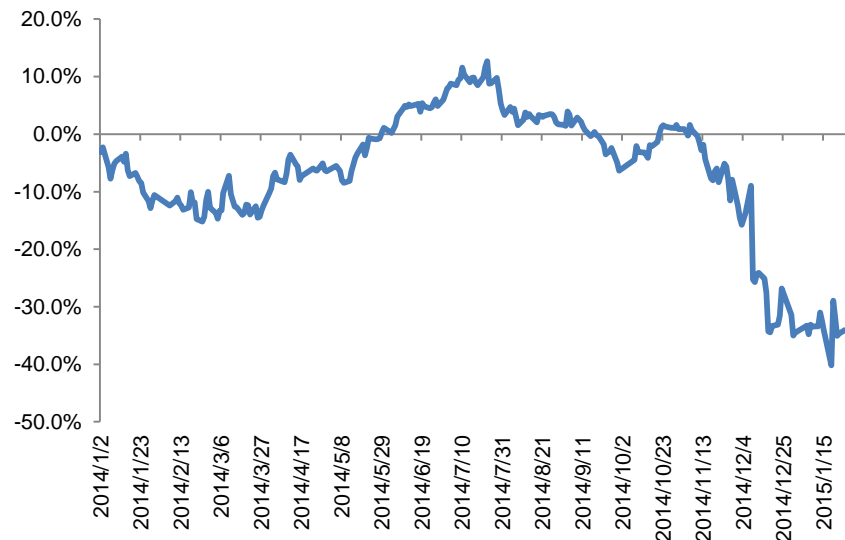
### Relative valuation

According to the Bloomberg consensus, A-share brokerage sector on average is trading at 3.5x 2015E P/B; the H-share brokers, including HTS, CITICS (6030 HK), CGS (6881 HK), and CCS (1375 HK), are trading at a weighted average of 2.0x 2015E P/B. The higher valuation in the A-share market may reflect different investor structure between A-share and H-share market. A-share market is retail investors oriented while H-share market is institutional investors oriented. HTS is currently trading at 1.8x 2015E P/B, while the ratios for CITICS, CGS and CCS are at 2.1x, 1.7x and 2.5x, respectively.

### A/H valuation

HTS's H-share is trading at a 34.1% discount to its A-share as at Jan 26, 2015. Its A-H valuation discrepancy has been fluctuating in the past year. With the commencement of the SH-HK stock connect, we expect the valuation discrepancy will be narrowed on increased arbitrage trading.

**Exhibit 13: HTS's H-share is trading at a 34.1% discount to its A-share**



Source(s): Bloomberg, ABCI Securities estimates



**Consolidated income statement (2012A-2016E)**

<b>FY Ended Dec 31 (RMB mn)</b>	<b>2012A</b>	<b>2013A</b>	<b>2014E</b>	<b>2015E</b>	<b>2016E</b>
Fee and commission income	5,210	6,751	9,723	12,384	15,316
Interest income	2,879	3,671	6,689	11,039	16,965
Investment income	2,404	2,150	5,764	7,580	8,919
Other income	251	231	265	297	321
<b>Total Revenue</b>	<b>10,743</b>	<b>12,803</b>	<b>22,441</b>	<b>31,300</b>	<b>41,520</b>
Operating costs	(6,682)	(7,465)	(12,170)	(16,941)	(22,122)
<b>Operating Profits</b>	<b>4,061</b>	<b>5,338</b>	<b>10,270</b>	<b>14,359</b>	<b>19,398</b>
Associates & JCEs	66	117	197	245	305
<b>Profit before tax</b>	<b>4,127</b>	<b>5,455</b>	<b>10,468</b>	<b>14,604</b>	<b>19,703</b>
Tax	(875)	(1,174)	(2,355)	(3,286)	(4,433)
<b>Profit after tax</b>	<b>3,252</b>	<b>4,281</b>	<b>8,112</b>	<b>11,318</b>	<b>15,270</b>
Minority interests	(214)	(246)	(295)	(354)	(425)
<b>Net Profits</b>	<b>3,038</b>	<b>4,035</b>	<b>7,817</b>	<b>10,964</b>	<b>14,845</b>
<b>Growth (%)</b>					
Fee and commission income (%)	(20.7)	29.6	44.0	27.4	23.7
Interest income (%)	12.8	27.5	82.2	65.0	53.7
Investment income (%)	59.6	(10.6)	168.1	31.5	17.7
Other income (%)	7.3	(8.0)	14.8	12.3	8.1
Total Revenue (%)	(1.1)	19.2	75.3	39.5	32.7
Total Operating costs (%)	0.7	11.7	63.0	39.2	30.6
Operating profit (%)	(3.9)	31.4	92.4	39.8	35.1
Net profit (%)	(2.1)	32.8	93.7	40.3	35.4
<b>Operating performance (%)</b>					
Operating margin (%)	37.8	41.7	45.8	45.9	46.7
Net margin (%)	28.3	31.5	34.8	35.0	35.8
Effective tax rate	21.2	21.5	22.5	22.5	22.5
Dividend payout (%)	37.9	28.5	30.0	30.0	30.0
ROAE (%)	5.7	6.5	11.5	12.0	12.6
ROAA (%)	2.7	2.7	3.4	3.0	2.8
<b>Segmental revenue (RMB mn)</b>					
Investment banking	746	716	1,669	3,616	4,724
Brokerage	4,312	6,460	11,694	15,335	18,521
Asset management	962	611	729	821	923
Proprietary trading	1,738	2,404	4,714	6,264	7,742
Overseas	1,007	1,407	1,479	1,627	1,952
Finance lease	-	-	726	799	898
Other income	1,979	1,206	1,430	2,838	6,761

Source(s): Company, ABCI Securities estimates





Consolidated balance sheet (2012A-2016E)

FY Ended Dec 31 (RMB mn)	2012A	2013A	2014E	2015E	2016E
Fixed assets	1,225	1,258	1,314	1,372	1,433
Goodwill	642	623	604	586	569
Other intangible assets	289	256	231	207	187
Investment securities	6,860	9,135	13,079	18,862	27,362
Other non-current assets	784	1,805	2,016	2,253	2,519
<b>Total non-current assets</b>	<b>9,800</b>	<b>13,077</b>	<b>17,243</b>	<b>23,280</b>	<b>32,070</b>
Cash & equivalents	52,000	52,587	63,104	94,657	104,122
Investment securities	39,850	52,824	75,840	95,506	112,443
Other current assets	24,831	50,636	132,405	230,291	369,695
<b>Total current assets</b>	<b>116,682</b>	<b>156,046</b>	<b>271,349</b>	<b>420,453</b>	<b>586,260</b>
<b>Total assets</b>	<b>126,482</b>	<b>169,124</b>	<b>288,592</b>	<b>443,733</b>	<b>618,330</b>
Borrowings	10,776	9,916	21,723	32,092	47,595
Other current liabilities	55,125	76,742	168,261	270,410	414,761
<b>Total current liabilities</b>	<b>65,901</b>	<b>86,658</b>	<b>189,984</b>	<b>302,502</b>	<b>462,357</b>
Net current assets	50,780	69,388	81,365	117,952	123,903
<b>Total assets less current liabilities</b>	<b>60,581</b>	<b>82,466</b>	<b>98,608</b>	<b>141,232</b>	<b>155,973</b>
Bonds payables	-	17,940	19,734	21,707	23,878
Other non-current liabilities	150	421	7,321	7,903	8,563
<b>Total non-current liabilities</b>	<b>150</b>	<b>18,361</b>	<b>27,054</b>	<b>29,610</b>	<b>32,440</b>
<b>Net assets</b>	<b>60,431</b>	<b>64,105</b>	<b>71,554</b>	<b>111,622</b>	<b>123,533</b>
Equity attributable to owners of the parent	58,680	61,507	68,176	107,568	118,669
Minority interest	1,751	2,598	3,378	4,053	4,864
<b>Total equity</b>	<b>60,431</b>	<b>64,105</b>	<b>71,554</b>	<b>111,622</b>	<b>123,533</b>

Source(s): Company, ABCI Securities estima



## Disclosures

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### Definition of equity rating

Rating	Definition
Buy	Stock return $\geq$ Market return rate
Hold	Market return - 6% $\leq$ Stock return < Market return rate
Sell	Stock return < Market return - 6%

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate from 2010-2014

Time horizon of share price target: 12-month

### Definition of share price risk

Rating	Definition
Very high	$2.6 \leq$ 180 day volatility/180 day benchmark index volatility
High	$1.5 \leq$ 180 day volatility/180 day benchmark index volatility < 2.6
Medium	$1.0 \leq$ 180 day volatility/180 day benchmark index volatility < 1.5
Low	180 day volatility/180 day benchmark index volatility < 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index.

Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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