



September 19, 2016
Company Report
Rating: HOLD
TP: HK\$ 8.70

Share price (HK\$)	8.10
Est. share price return	7.4%
Est. dividend yield	2.0%
Est. total return	9.4%

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Key Data

52Wk H/L(HK\$)	8.6/8.1
Issued shares (mn)	6,216
- H shares (mn)	1,028
- A shares (mn)	5,188
H-share market cap (HK\$ mn)	8,397
Avg daily turnover (HK\$ mn)*	32
Major shareholder(s) (%):	
Shenergy Group	24.74%
Shanghai Haiyan	4.61%
Wenhui Xinmin United Press	3.97%
Source(s): Company, Bloomberg, ABCI Securities	
*Since listing on Jul 8, 2016	

Share performance (%)

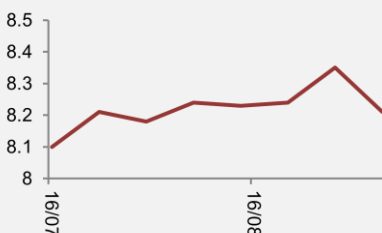
	Absolute	Relative*
1-mth	(1.0)	3.8
3-mth	NA	NA
6-mth	NA	NA

*Relative to HSI
Source(s): Bloomberg, ABCI Securities

1H16 Revenue breakdown (%)

Brokerage	50
Others	16
Investment banking	14
Investment management	12
Trading	8
Source(s): Company, ABCI Securities	

Stock performance (HK\$)



Source(s): Bloomberg, ABCI Securities

DFZQ (3958 HK)
A high-beta play

- 1H16 profit dropped by 78% YoY to RMB 1.3bn on steep decline in proprietary trading
- Heavy exposure to trading income makes it a high-beta play although asset allocation to high-grade bonds has helped mitigate overall risk
- May benefit from CSRC's downgrade of various H-listed brokers
- Limited re-rating potential in the near term due to high-beta nature. Recommend **HOLD**

1H16 highlights. Revenue and net profit dropped by 57% and 78% to RMB 5.8bn and RMB 1.3bn. Due to significant drop in revenue from proprietary trading, it suffered a steeper decline in earnings than peers. Operating margin dropped from 56.5% in 1H15 to 24.8% in 1H16 while net margin fell from 44.0% to 22.3% over the same period. ROE was 3.5% vs. 13.2% a year ago

High beta driven by proprietary trading. Proprietary trading revenue dropped 93% to RMB 484mn in 1H16 due to unfavorable investment environment. As a result, revenue from proprietary trading only accounted for 8% of total revenue, vs. 53% in 1H15. Overall, its high dependence on trading income has led to more volatile earnings than peers. To mitigate market risk, the Group has allocated ~76% of the trading assets to bonds, among which 98% achieved an external rating of "AA" or higher.

Expanding into gold trading. DFZQ is actively developing its gold trading business and has obtained the international membership to conduct gold proprietary trading business and agency business on the international board.

May benefit from rating downgrade of H-listed peers. Maintaining its "AA" rating, it may benefit from CSRC's recent rating downgrade of H-listed brokers including CITIC (6030 HK), Galaxy (6881 HK), GF (1776 HK), Haitong (6837 HK), Huatai (6886 HK), and CICC (3908 HK). We believe a lower regulatory rating could lead to higher headwinds in business development, funding channel and cost, as well as capital requirement.

Limited re-rating potential in the near term. The counter is currently trading at 1.1x forward P/B, in line with the sector average. We believe re-rating potential is limited in the near term due to its high exposure in proprietary trading. We set our TP to HK\$ 8.70, equivalent to 1.1x 2017E P/B. Recommend **HOLD**.

Risk factor: (1) Market risk of financial assets; (2) Credit risk to bond investments and lending business; (3) Volatility in market turnover.

Results and Valuation

FY ended Dec 31	2014A	2015A	2016E	2017E	2018E
Revenue (RMB mn)	7,888	20,459	11,794	13,367	15,068
Chg (% YoY)	72.0	159.4	(42.4)	13.3	12.7
Net profit (RMB mn)	2,342	7,325	2,822	3,249	3,863
Chg (% YoY)	132.5	212.7	(61.5)	15.2	18.9
Underlying EPS (RMB)	0.50	1.11	0.45	0.52	0.62
Chg (% YoY)	NA	122.0	(59.1)	15.2	18.9
BVPS (RMB)	4.3	6.6	6.4	6.8	7.2
Chg (% YoY)	NA	54.4	(3.4)	5.7	6.4
Underlying PE (x)	14.1	6.3	15.5	13.5	11.3
P/B (x)	1.6	1.1	1.1	1.0	1.0
ROE (%)	13.8	27.5	7.6	7.9	8.9
ROA (%)	2.8	4.6	1.4	1.6	1.8
DPS(HK\$)	0.22	0.53	0.16	0.18	0.22
Yield (%)	2.6	6.4	1.9	2.2	2.7

Source(s): Company, ABCI Securities estimates



1H16 performance by business segment

Proprietary trading. Segment revenue fell 93% to RMB 484mn in 1H16 on less favorable investment compared with 1H15. Proprietary trading asset balance remained largely stable at RMB 49.3bn in June 2016 vs. RMB 50.3bn at end-2015.

In terms of asset allocation, bonds accounted for 76% of total trading assets, followed by stocks and funds (18%) and others (6%). In addition, about 98% of bonds have a crediting rating of “AA” or higher. It remained to be the top five market makers among all securities companies in the interbank bond market. Overall, trading assets accounted for 26% of total assets and 150% of total equity in June 2016.

It is also expanding into gold trading after getting an international membership to trade on the international board.

Investment banking. Investment banking revenue increased by 35% to RMB 801mn in 1H16, largely in line with the increase in fundraising activities during the period. Overall, investment banking accounted for 14% of total revenue in 1H16.

In 1H16, it completed 10 equity deals, including four IPOs, two private placements, and two financial advisory projects. Its equity lead underwriting amount increased from RMB 4.7bn in 1H15 to RMB 6.0bn in 1H16. Its bond lead underwriting amount increased from RMB 18bn in 1H15 to RMB 40bn in 1H16.

Brokerage. Brokerage revenue dropped 29% RMB 2.9bn amid lower turnover and weak market sentiment compared with last year. Overall, brokerage remained the largest contributor, accounting for 50% of total revenue in 1H16.

Its stock and fund turnover was RMB1.7trn in 1H16 with a 1.28% market share.

Securities financing balance was RMB38.8bn in June 2016, 2.3% higher than that in end-2015. Margin finance and securities lending balance dropped from RMB 13.6bn at end-2015 to RMB 9.3bn in June 2016. Collateralized stock repurchase and repurchase agreement balance increased from RMB 24.1bn at end-2015 to RMB 28.9bn in June 2016.

Investment management. Segment revenue fell 38% to RMB 677mn in 1H16 and accounted for 12% of total revenue. Overall, total AUM of Orient Securities Asset Management was RMB 124bn in June 2016, up 14.1% compared with end-2015. In terms of product mix, targeted asset management schemes (TAM) accounted for 53.1% of total AUM, followed by mutual funds (20.1%), collective asset management schemes (CAM) (17.5%), and specialized asset management schemes (SAM) (9.3%).

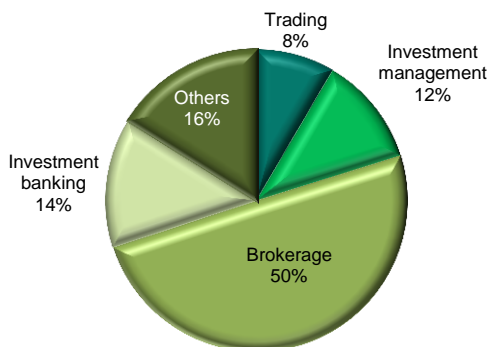


Exhibit 1: 1H16 results highlight

	1H15	1H16	YoY	Comment
Fee and commission income	3,692	2,270	(39%)	
Interest income	1,986	2,203	11%	
Investment income	7,557	1,002	(87%)	Less favorable market environment
Other income	114	275	142%	
Total revenue and other income	13,349	5,749	(57%)	
Total expenses	5,810	4,322	(26%)	Cost control
Operating Profits	7,539	1,428	(81%)	
Share of profit of associates	161	133	(18%)	
Profit before tax	7,700	1,560	(80%)	
Tax	1,768	204	(88%)	
Profit after tax	5,932	1,356	(77%)	
Minority interests	55	73	33%	
Net Profits	5,878	1,283	(78%)	
Revenue by segment				
Trading	7,084	484	(93%)	Unfavorable investment return
Investment management	1,090	677	(38%)	
Brokerage	4,055	2,863	(29%)	Falling market turnover
Investment banking	593	801	35%	
Others	527	925	76%	
Total revenue and other income	13,349	5,749	(57%)	
Ratios				
Operating margin	56.5%	24.8%		
Net margin	44.0%	22.3%		
ROAE	22.3%	3.7%		

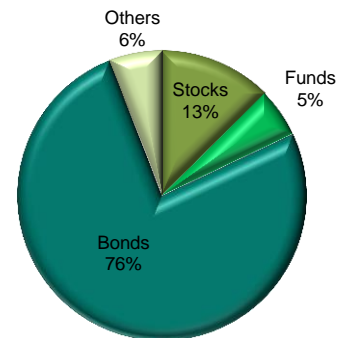
Source(s): Company, ABCI Securities

Exhibit 1: 1H16 sales breakdown



Source(s): Company, ABCI Securities

Exhibit 2: Asset allocation of trading assets (June 2016)



Source(s): Company, ABCI Securities



Financial Summary

Consolidated income statement (2014A-2018E)

FY Ended Dec 31 (RMB mn)	2014A	2015A	2016E	2017E	2018E
Fee and commission income	2,460	6,621	5,187	5,660	6,461
Interest income	1,446	4,290	4,400	5,000	5,600
Investment income	3,906	9,342	2,000	2,500	2,800
Total revenue	7,812	20,253	11,587	13,160	14,861
Other income	76	207	207	207	207
Total revenue and other income	7,888	20,459	11,794	13,367	15,068
Total expenses	5,090	11,397	8,722	9,855	10,900
Operating Profits	2,798	9,062	3,072	3,512	4,168
Share of profit of investments in associates	136	436	524	628	754
Profit before tax	2,934	9,499	3,595	4,140	4,922
Tax	575	2,125	755	869	1,034
Profit after tax	2,137	7,374	2,840	3,271	3,888
Minority interests	17	49	19	21	25
Profits attributable to shareholders	2,120	7,325	2,822	3,249	3,863
Growth					
Total revenue and other income (%)	72.0	159.4	(42.4)	13.3	12.7
Total expenses	42.3	123.9	(23.5)	13.0	10.6
Operating Profits (%)	176.9	223.9	(66.1)	14.3	18.7
Net profit (%)	132.5	212.7	(61.5)	15.2	18.9
Operating performance					
Operating margin (%)	35.5	44.3	26.0	26.3	27.7
Net margin (%)	27.1	36.2	24.4	24.7	26.0
ROAE (%)	13.8	27.5	7.6	7.9	8.9
ROAA (%)	2.8	4.6	1.4	1.6	1.8

Source(s): Company, ABCI Securities estimates



Consolidated balance sheet (2014A-2018E)

As of Dec 31 (RMB mn)	2014A	2015A	2016E	2017E	2018E
Property and equipment	1,537	1,719	1,804	1,895	1,989
Goodwill	32	32	32	32	32
Other intangible assets	86	97	101	106	112
Investment in associates and JV	1,004	1,909	2,004	2,104	2,209
AFS	2,893	11,369	11,938	12,535	13,161
Financial assets held under resale agreements	5,482	10,210	10,720	11,256	11,819
Deposits with exchanges and a non-bank financial institution	-	-	-	-	-
Other non-current assets	1,321	612	642	674	708
Total non-current assets	12,354	25,946	27,242	28,602	30,031
Cash & equivalents	23,803	55,344	54,836	57,010	59,612
Clearing settlement funds	5,649	8,825	7,060	7,413	7,784
AFS	37,540	48,507	53,358	56,026	58,827
Financial assets at FVTPL	7,274	31,871	22,310	23,425	24,596
Financial assets held for trading	0	0	0	0	0
Derivatives	57	77	81	85	89
Other current assets	757	1,060	848	890	935
Other receivables and prepayments	2,113	5,737	4,338	4,555	4,783
Advances to customers	9,946	14,241	11,393	11,962	12,561
Financial assets held under resale agreements	8,037	16,289	19,546	20,524	21,550
Total current assets	95,175	181,951	173,770	181,891	190,737
Total assets	107,529	207,897	201,012	210,493	220,768
Accounts payable	21,783	43,193	34,554	36,282	38,096
Loans and debt	6,985	15,365	22,217	22,472	22,740
Financial liabilities at FV through P/L	878	3,147	3,305	3,470	3,643
Financing instrument payables	6,780	8,396	8,816	9,257	9,719
Other current liabilities	38,840	42,662	44,795	47,035	49,386
Total current liabilities	75,266	112,763	113,687	118,515	123,585
Financial assets sold under repurchase agreements	94	11,215	5,608	5,888	6,182
Loans and bonds payables	363	385	405	425	446
Financing instrument payables	501	977	1,025	1,077	1,131
Other non-current liabilities	12,680	47,181	40,104	42,109	44,215
Total non-current liabilities	13,637	59,758	47,142	49,499	51,974
Total liabilities	88,904	172,521	160,828	168,014	175,559
Net current assets	19,908	69,188	60,083	63,376	67,152
Equity attributable to owners of the parent	18,353	34,958	39,747	42,022	44,726
Minority interest	272	418	436	458	483
Total equity	18,625	35,376	40,183	42,479	45,209

Source(s): Company, ABCI Securities estimates

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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

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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