

January 27, 2015

**Sector Rating:  
Overweight**

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**Key Data**

Avg.15E P/E (x)	17.3
Avg.15E P/B (x)	2.0
Avg.15E Dividend Yield (%)	1.8

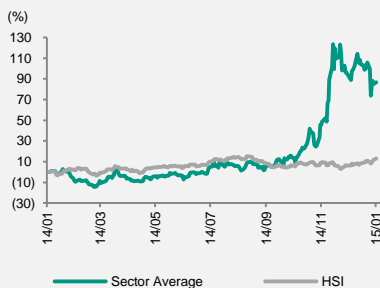
Source(s): Company, Bloomberg, ABCI Securities

**Sector performance (%)**

	Absolute	Relative*
1-mth	-6.48	-12.90
3-mth	58.65	52.22
6-mth	66.36	64.39

\*Relative to HSI

Source(s): Bloomberg, ABCI Securities

**1-Year sector performance**


Source(s): Bloomberg, ABCI Securities

## China Brokers

### Rising opportunities from capital market reform

- Improving liquidity and improved market sentiment spurred by monetary easing in China and the SH-HK stock connect are expected to enhance investors' confidence, driving up revenue in multiple business lines.
- Capital-based intermediary business would be one of the future earnings drivers. We expect its revenue contribution to increase to 20%-25% in 2015E from 18% in 1H14.
- Fee income from investment banking rebounded sharply in FY14 on IPO resumption in China; the momentum is expected to continue in 2015
- We are positive on the China brokerage sector on capital market reforms; our sector top pick is CGS (6881 HK)

**Strong trading volume in the A-share market.** SHCOMP index rose 59% in 2014 and exceeded the 3,200 level in Dec. We expect the index to edge up 10%-15% in 2015E amid improving liquidity and optimistic market sentiment spurred by the SH-HK stock connect and monetary easing in China. Upon announcement of the interest rate cut by PBOC on Nov 21, 2014, turnover in the A-share market continued to hit new highs; average daily turnover (ADT) surged from RMB 160bn in June to 783bn in Dec 2014 on strong velocity and increasing number of active trading accounts. 4Q14 ADT reached RMB 546bn, up 87.7% QoQ and 254.6% from 1H14 (vs. RMB 291bn in 3Q14 and RMB 181bn in 1H14). For 2015E, we expect ADT of the A-share market to reach RMB 386bn(+28% YoY); market cap of tradable A-shares would amount to ~RMB 35tr (as at end-Dec 2014: RMB 32tr), while annual turnover velocity of weighted average tradable A-shares would be at ~280%.

**Capital-based intermediary business is expected to be an earnings driver.** Increasing penalties established by CSRC indicate regulators' rising concerns over MFSL business. We believe risk profile for lending business is benign and controllable since the collateral ratio (total collateral/total lending balance) is above 240% at present. After surging 196% YoY in 2014, we expect growth in MFSL system balance would normalize to 46% YoY in 2015E. We expect its revenue share to increase to 20%-25% in 2015E from 18% in 1H14.

**Robust growth in investment banking business.** As China restarted its A-share IPO market in 1Q14, a total of 125 companies have executed their IPOs in 2014. We believe the introduction of the registration-based IPO system would be positive to the equity market. Total new equity funds raised in 2014 (including IPO, placement and rights issuance) was RMB 772bn, up 89.5% YoY. Fee income from investment banking also rebounded sharply in FY14 and we expect such momentum to continue in 2015.

**Positive on China's brokerage sector.** China's brokers, the key beneficiaries of the capital market reforms, have sound earnings growth prospects in our view. Our sector top pick is CGS (6881 HK), based on its solid capital position, conservative investment portfolio, highest market share in brokerage income and ROAE among peers.

**Risk factors:** 1) Further decline in brokerage commission rates; 2) Severe downturn in A-market turnover; 3) Slowdown in China's economic growth; 4) Higher-than-expected proprietary trading loss; 5) Lower-than-expected growth in flow-based businesses

**Sector Valuation Summary (Data as of Jan 26, 2015)**

Company	Ticker	Rating	Price (HK\$)	TP (HK\$)	FY14E P/E(x)	FY15E P/E (x)	FY14E P/B (x)	FY15E P/B (x)	FY14E Yield (%)	FY15E Yield (%)
CITICS-H	6030	BUY	25.15	32.40	24.33	19.38	2.39	2.14	1.33	1.68
HTS-H	6837	BUY	17.48	22.20	19.42	15.45	2.12	1.78	1.53	1.92
CGS	6881	BUY	8.74	12.00	15.85	12.33	2.09	1.68	1.79	2.16
CCS	1375	BUY	7.06	9.10	27.29	19.68	2.81	2.47	1.06	1.42

Source(s): Bloomberg, ABCI Securities



## Contents

<b>Industry overview</b> .....	<b>3</b>
<b>Positive on the brokerage sector</b>	
Strong trading volume in the A-share market.....	4
Capital-based intermediary business to be a future earnings driver .....	7
Robust growth in investment banking business.....	8
Potential relaxation of China's capital rules .....	11
Expansion of balance sheet leverage .....	12
Development trends of the PRC securities industry.....	13
<b>Investment Summary</b> .....	<b>15</b>
<b>Risk factors</b> .....	<b>16</b>
<b>China Galaxy Securities (6881 HK)</b> .....	<b>18</b>
<b>CITIC Securities (6030 HK)</b> .....	<b>22</b>
<b>Haitong Securities (6837 HK)</b> .....	<b>33</b>
<b>Central China Securities (1375 HK)</b> .....	<b>42</b>
<b>Disclosures</b> .....	<b>57</b>



### Industry overview

As at Dec 31, 2014, there were 120 securities companies in China, with total assets of RMB 4.1tn and net assets of RMB 920.5bn. Total revenue and net profit was RMB 260.3bn and RMB 96.6bn in 2014, up 63.7% YoY and 119.5% YoY.

Exhibit 1: 2014 industry data

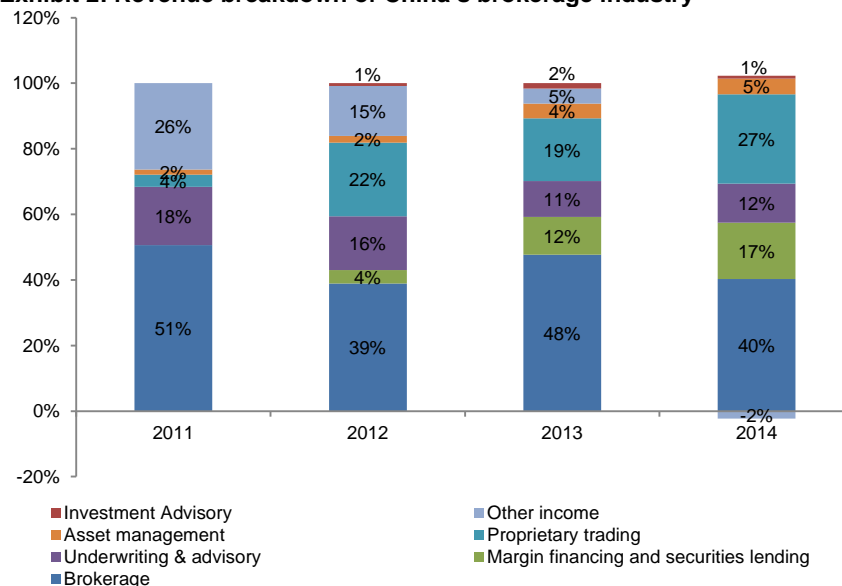
2014 industry data	
Revenue	RMB 260.3bn (+63.7% YoY)
Net profits	RMB 96.6bn (+119.5% YoY)
Annualized ROA	2.4% (2013: 2.6%)
Annualized ROE	10.5% (2013: 8.0%)
Net capital / net assets	73.8% (2013: 70.0%)

Source(s): China Securities Journal, CSRC, ABCI Securities

Brokerage business remained the industry's core contributor, accounting for ~40% of total revenue in 2014. Proprietary trading, margin financing and securities lending (MFSL), underwriting & advisory, asset management and investment advisory accounted for 27%, 17%, 12%, 5%, 1% of total revenue in 2014, respectively.

MFSL business grew rapidly since its launch in 2012; its contribution to the industry revenue surged from 4% in 2012 to 12% in 2013. With the ongoing deregulation in the financial industry, capital-based intermediary business is expected to become one of the future earnings drivers.

Exhibit 2: Revenue breakdown of China's brokerage industry



Source(s): China Securities Journal, CSRC, ABCI Securities

China brokerage industry is fragmented in terms of total assets, with the top 5 securities firms accounting for 40.4% of the industry total. Apart from national plays, there are numerous provincial brokers in China. The fragmented brokerage industry is currently undergoing a fresh wave of consolidation on the back of capital market reform, as exemplified by the slew of M&A activities including the merger of Shenyin Wanguo Securities and Hong Yuan Securities, Guotai Junan Securities's acquisition of Shanghai Securities, Founder Securities's acquisition of China Minzu Securities, merger of Sinotex Investment & Development and Essence Securities. We expect



further consolidation to take place given the intensifying competition, the relatively homogenous product variety among brokers, and the low industry concentration. Leading brokers with a strong capital position are more likely to acquire smaller ones to gain market share and expand geographical coverage and market presence.

### Strong trading volume in the A-share market

SHCOMP index rose 59% in 2014 and exceeded the 3,200 level in Dec 2014. We expect the index to rise 10%-15% in 2015 on improving liquidity and optimistic market sentiment spurred by both the SH-HK stock connect program and monetary easing in China. Since PBOC's rate cut on Nov 21, 2014, turnover in the A-share market continued to hit new record high, with average daily turnover (ADT) surging from RMB 160bn in June to RMB 783bn in Dec 2014, as supported by strong velocity and increasing number of active trading accounts. ADT in 4Q14 reached RMB 546bn, up 87.7% QoQ and 254.6% from 1H14 (vs. RMB 291bn I 3Q14 and RMB 181bn in 1H14). For 2015E, we expect ADT of the A-share market to reach RMB 386bn; market cap of tradable A-shares would rise to ~RMB 35tr (as at end-Dec 2014: RMB 32tr), while the annual turnover velocity of weighted average tradable A-shares would remain at ~270% -280%.

Market sentiment was overheating. The number of monthly new accounts in Dec 2014 reached almost 3mn, with 891,279 new accounts being created in the 2<sup>nd</sup> week of Dec. Total number of outstanding accounts was 181mn. The number of active trading accounts rebounded to an average of 23mn in Dec compared to 13mn in 2014, and represented 13% of total accounts at end-year.

SH-HK stock connect was officially launched on Nov 17, denoting a milestone toward greater liberalization in China's capital markets. Currently, the daily southbound and northbound quotas are RMB 10.5bn and RMB 13bn; the respective cumulative quotas are RMB 250bn and RMB 300bn. Transaction volume was disappointing at the initial weeks and we believe the low enthusiasm could be attributed to the differences in regulation, trading rule and investor mix. In our view, SH-HK stock connect is unlikely to drive up brokerage fee income substantially based on the limited quota; nonetheless, its launch would drum up market sentiment and enhance investors' confidence, benefiting multiple business lines such as investment banking and margin financing.

Exhibit 3: SHCOMP index rose 59% in 2014

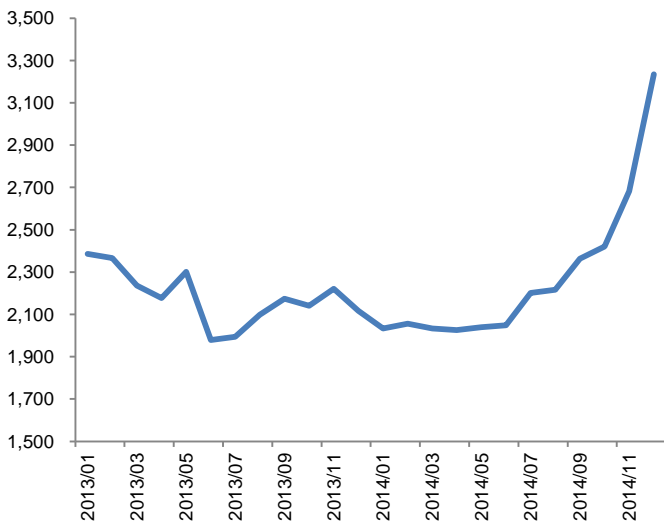
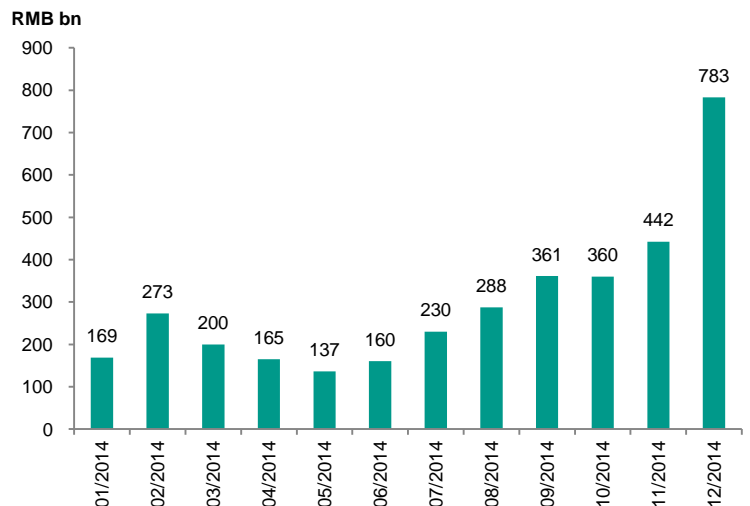
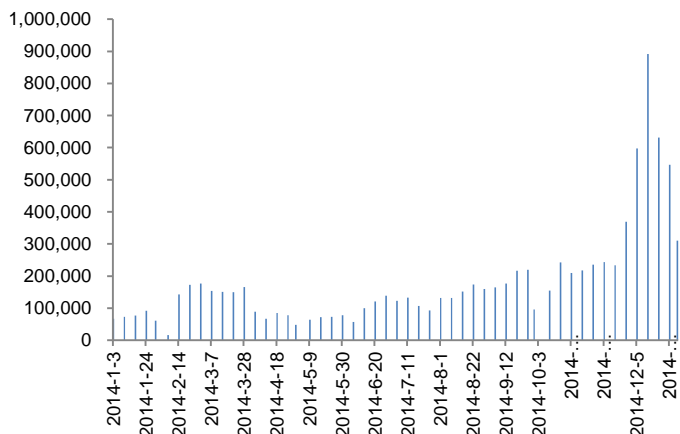


Exhibit 4: Monthly ADT has rebounded sharply since 3Q14

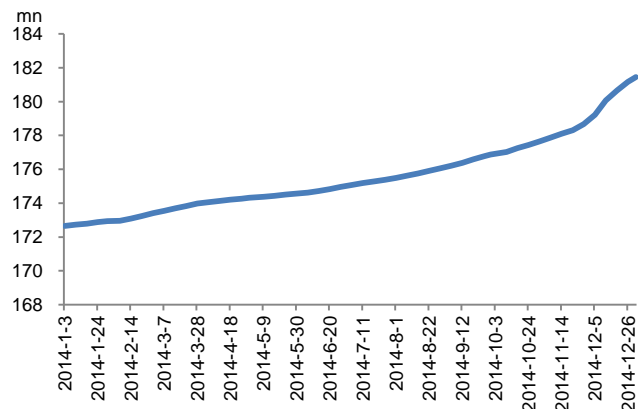


Source(s): Bloomberg, ABCI Securities

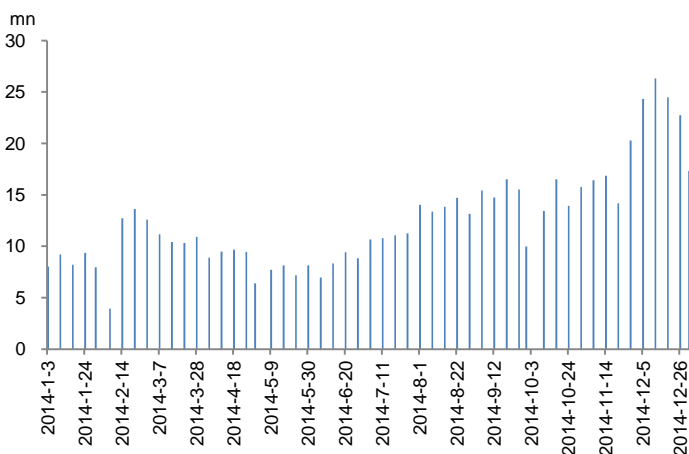
Source(s): Wind, ABCI Securities

**Exhibit 5: Number of newly created A-share accounts soared in Dec 2014**


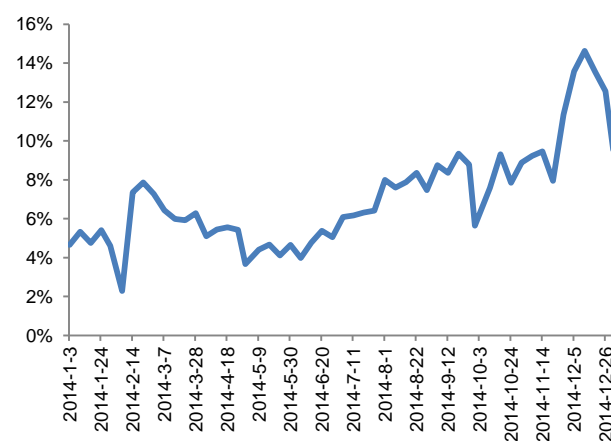
Source(s): Wind, ABCI Securities

**Exhibit 6: Total number of outstanding A-share accounts reached 181mn**


Source(s): Wind, ABCI Securities

**Exhibit 7: The number of active trading accounts have rebounded since Nov 2014**


Source(s): Wind, ABCI Securities

**Exhibit 8: Active trading accounts reached represents 14.6% of total accounts in mid-Dec 2014- a year-high level**


Source(s): Wind, ABCI Securities

**Exhibit 9: A-share market trading volume forecasts**

Stock turnover	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015E	2016E
<b>ADT (RMB bn)</b>	37	188	108	218	224	172	129	195	301	386	428
YoY Growth%		410%	-42%	102%	3%	-23%	-25%	52%	55%	28%	11%
Annual trading volume (RMB bn)	8,874	45,407	26,542	53,186	54,251	41,877	31,237	46,353	73,771	93,461	103,613
YoY Growth%		412%	-42%	100%	2%	-23%	-25%	48%	59%	27%	11%
No. of trading days	241	242	246	244	242	244	243	238	245	242	242
<b>Market Cap. - yr end (RMB bn) (A,B shares)</b>	8,940	32,714	12,137	24,394	26,542	21,476	23,036	23,908	37,693	41,462	45,608
YoY Growth%		266%	-63%	101%	9%	-19%	7%	4%	58%	10%	10%
Weighted average market cap. (RMB bn)	20,827	22,425	18,265	25,468	24,009	22,256	23,472	30,800	39,577	43,535	
<b>Tradable A-share market capitalization (RMB bn)</b>	2,370	9,073	4,455	14,962	19,104	16,360	18,014	19,803	31,515	35,243	38,767
% of tradable shares		28%	37%	61%	72%	76%	78%	83%	84%	85%	85%
Weighted average tradable A-share market cap. (RMB bn)	5,722	6,764	9,708	17,033	17,732	17,187	18,908	25,659	33,379	37,005	
<b>Turnover Velocity</b>											
Turnover velocity (with ref. to weighted average of total mkt. cap.)		218%	118%	291%	213%	174%	140%	197%	240%	236%	238%
Turnover velocity (with ref to weighted average of tradable A-share mkt cap)		500%	596%	355%	284%	256%	182%	245%	288%	280%	280%

Source(s): Wind, ABCI Securities estimates



### Brokerage commission rate under pressure

Since the introduction of Yong Jin Bao, an internet-based financial product that provides online brokerage by Sinolink Securities and Tencent in Feb 2014, commission rate have further declined. The average commission rate of the industry declined from ~7.9bps in 2013 to ~7.1bps in 1H14. Apart from the competition from online discount brokerage firms, the recent removal of the “one investor one account” policy is expected to fuel the competition and exert further pressure on the brokers’ commission rate.

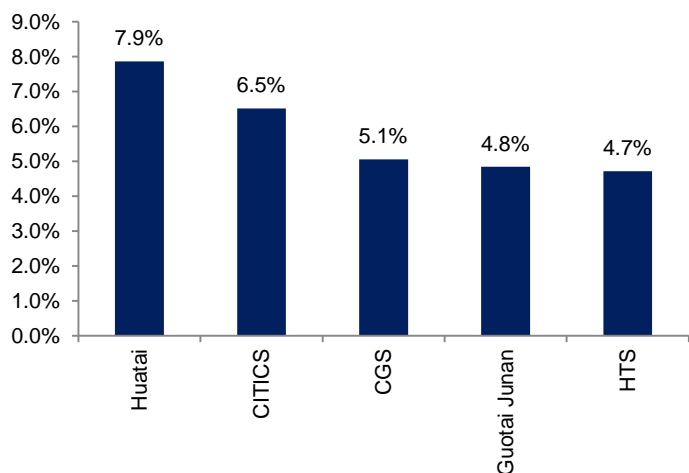
We expect the emergence of more online discount brokerage firms that offer lower commission rate than the conventional brokers to reduce commission rate further in the medium term. In our view, large players would focus on product/service differentiation to attract more high-end clients to mitigate the adverse impacts. Therefore, the decline in commission rate for large players should be slower than that of the smaller counterparts. Market shares of CITICS (6030 HK), HTS (6837 HK) and CGS (6881 HK) in brokerage business remained relatively stable in 2014.

Exhibit 10: Changes in brokerage market share

Ranking	Brokers	Market share (%)	Changes in market share compared with 2013
1	Huatai	7.86%	1.74%
2	<b>CITICS</b>	<b>6.51%</b>	<b>0.29%</b>
3	<b>CGS</b>	<b>5.05%</b>	<b>-0.11%</b>
4	Guotai Junan	4.84%	-0.22%
5	<b>HTS</b>	<b>4.72%</b>	<b>-0.08%</b>

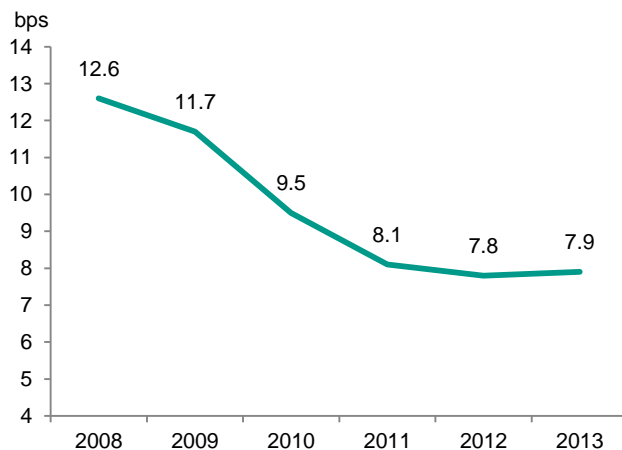
Source(s): Wind, ABCI Securities

Exhibit 11: Brokerage market share in terms of trading volume (stock + fund) in 2014



Source(s): Wind, ABCI Securities

Exhibit 12: Brokerage commission rate has been under pressure



Source(s): Company, ABCI Securities



### **Transforming from simple securities channel services to integrated financial services**

Due to similar business models and product /service offerings, competition among the Chinese securities firms has been stiff. However, prompted by the maturing industry development and CSRC's encouragement to expand the range of financial products to include market-making, individual stock option, and structured products, securities firms are enhancing their efforts to develop more differentiated and value-added services.

Leveraging on extensive client base and network, we believe leading brokers (e.g. CITICS and HTS) will take the lead in the development of innovative products and business.

In our view, small industry players in the market will slash price to gain market share, whereas large players would continue to diversify revenue sources, offering differentiated products/services and developing value-added wealth management business to attract more high-end clients and enhance customer stickiness.

### **Capital-based intermediary business to be a future earnings driver**

#### **Robust momentum in MFSL business is likely to persist**

The scale MFSL business has grown rapidly since its inception. Balance of MFSL in China surged from RMB 38bn in 2011 to RMB 1,026bn by end-Dec 2014, up 152% from end-June 2014 and 196% YoY, accounting for 4.0% of weighted average tradable A-share market cap. We estimate this ratio would reach 4.5%/ 5.0% in 2015E/ 2016E given the business is still in its early stage of development. Besides, penetration of margin financing is still low— only about 3% of A-share investors have opened a margin finance account. Assuming the tradable A-share market cap would reach RMB 35tr in 2015E and RMB 39tr in 2016E, we estimate the margin financing balance to increase by 46% YoY in 2015E and 23% in 2016E.

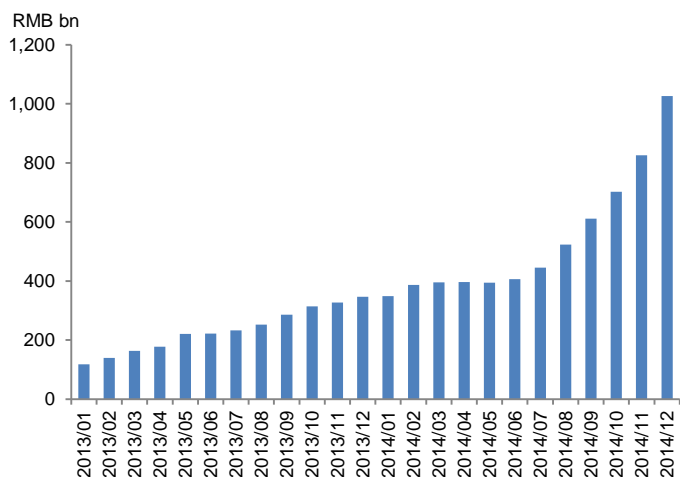
In Jan 2015, CSRC issued penalties for brokers who had violated regulations for margin financing business. Three securities firms, CITICS, HTS and Guotai Junan Securities were suspended from opening new MFSL client credit accounts for 3 months by reason of issues relating to extending the contractual term of MFSL contracts. In response to increasing surveillance by the regulators on the MFSL business, brokers are starting to adopt strict risk-control measures such as raising the minimum asset requirement for new credit accounts. We believe that risk profile for lending business is benign, since the collateral ratio (total collateral/total lending balance) is ~240% at present. Hence, the risk is controllable in our view. After surging by 196% YoY in 2014, we expect the growth of MFSL system balance would normalize to 46% YoY in 2015.

MFSL business contributed 4%, 12% and 17% to the industry's total revenue in 2012, 2013 and 2014 respectively. We expect its revenue share to increase to 20%-25% in 2015F. As at Dec 31 2014, market shares of the MFSL business in CITICS, CGS and HTS were 7.03%, 5.88%, and 5.57%, respectively; their respective ranking in the market was 1<sup>st</sup>, 5<sup>th</sup> and 7<sup>th</sup>. With the progressive deregulation of the financial industry, capital-based intermediary business is expected to become a future earnings driver for these companies.

### Capital raising in the sector

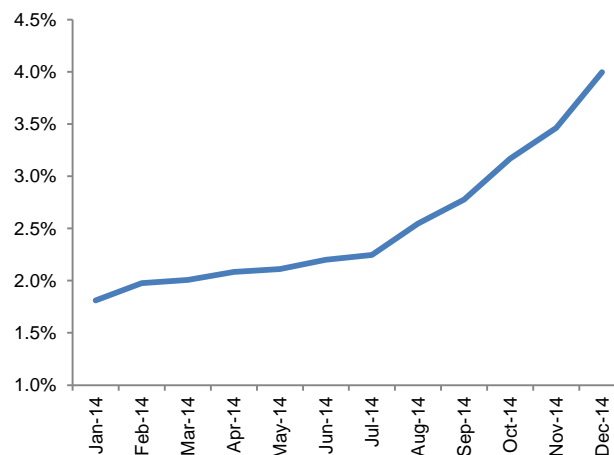
CITICS, HTS and CGS announced their placement plans in Dec 2014 and Jan 15 to raise around HK\$ 33bn, HK\$ 29bn and HK\$ 15bn, respectively, mainly for flow-based businesses such as margin financing, equity derivatives and FICC products (around 60-70% of the placement proceeds are allocated for the flow-based businesses). This reflects the shifting focus from fee-based business to flow-based one.

**Exhibit 13: Balance of MFSL in China soared 196% YoY in 2014**



Source(s): WIND, ABCI Securities

**Exhibit 14: MFSL balance represented 4.0% of weighted average tradable A-share market cap**



Source(s): WIND, ABCI Securities

### Quasi-lending business

In stock-pledged lending (SPL), brokers are allowed to provide financing against collateral pledged by the borrowers. The business has grown rapidly since its introduction in 2013. By end-2013, the value of the pledged stocks exceeded RMB 900bn, with brokers accounting for ~26% of the market share. By end-2014, RMB stocks totaling RMB 1,273bn were pledged for lending. SPL balance of brokers was RMB 698bn, and market share of brokers expanded significantly to ~55%. We expect SPL, in which share ownership transfer is not required, to gradually replace stock repo. We are positive on the demand for SPL business, given the widening funding channels, declining cost of capitals amid the interest rate cuts and rising leverage of brokers.

### Stellar growth in investment banking business

#### Equity financing

Since China restarted its A-share IPO market in 1Q14, a total of 125 companies have executed their IPOs in 2014. Until Jan 8, 2015, 88 IPO applications were under review by CSRC. The introduction of a registration-based IPO system, therefore, will be positive to development in the equity market by accelerating the approval process. Meanwhile, secondary offerings have remained strong. Total new equity funds raised in 2014 (including IPO, placement and rights issuance) was RMB 772bn, up 89.5% YoY. Fee income from investment banking rebounded sharply in 2014, and we expect such momentum to extend into 2015. Volume of IPO financing will largely depend on the pace of CSRC's approval. We expect total equity financing to expand by 46% YoY in 2015F.





Exhibit 15: Fund raised through IPO in the A-share market

	No. of company listed in 2014	Fund raised (RMB bn)	No. of company in the pipeline (as at Jan 8, 2015)
Main Board	43	31.18	37
SME Board	31	19.77	18
GEM Board	51	15.95	33
<b>Total</b>	<b>125</b>	<b>66.90</b>	<b>88</b>

Source(s): Wind, CSRC, ABCI Securities

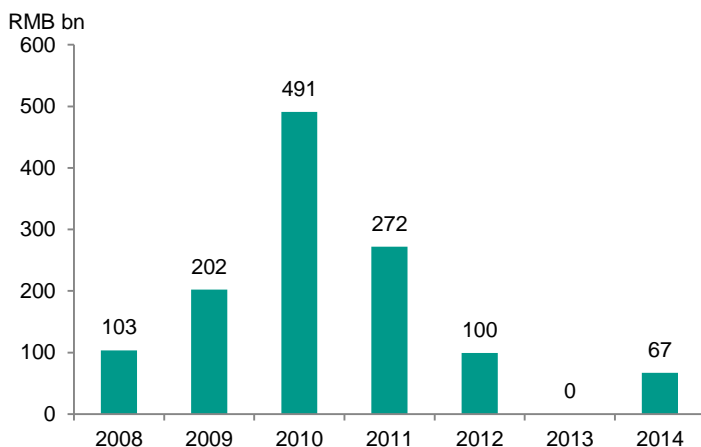
Debt financing

For debt financing, the amount of proceeds raised through bond issuance, including short-term financing bills and medium-term notes, corporate bonds, enterprise bonds, financial bonds, convertibles, government-backed institutional bonds, municipal bonds, asset-backed securities and private placement notes, increased from RMB 1,991bn in 2009 to RMB 6,317bn in 2014, representing a CAGR of 26.0%, according to the Wind data.

The share of corporate bonds in total social financing (TSF) increased from 2% in 2006 to 15% in 2014, whereas bank loans accounted for 61% of TSF in 2014. As financing from corporate bonds only constitutes a small proportion of TSF in China, we believe brokers' debt underwriting business still has much room for growth with the increasing financing opportunities given its huge growth potential.

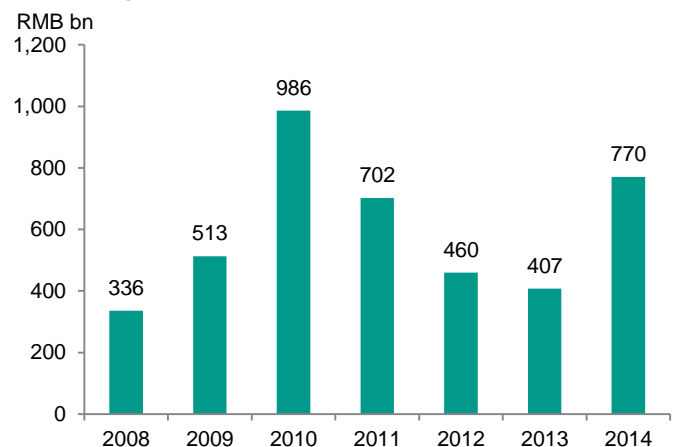
Debt underwriting volume was low in 2013 due to the rising bond yields as well as the deferral of bond issuance to 2014. Outstanding balance of bonds reached ~RMB 36tn as at end-2014, up 20% YoY. Total issuance of bonds reached RMB 12.1tr in 2014, up 34% YoY. The bond market was active in 2014, with bonds underwritten by brokers increasing by 73.1% YoY to RMB 1,998bn. We expect total debt financing volume to expand by 30% YoY in 2015E.

Exhibit 16: Gross proceeds raised through IPO in the A-share market

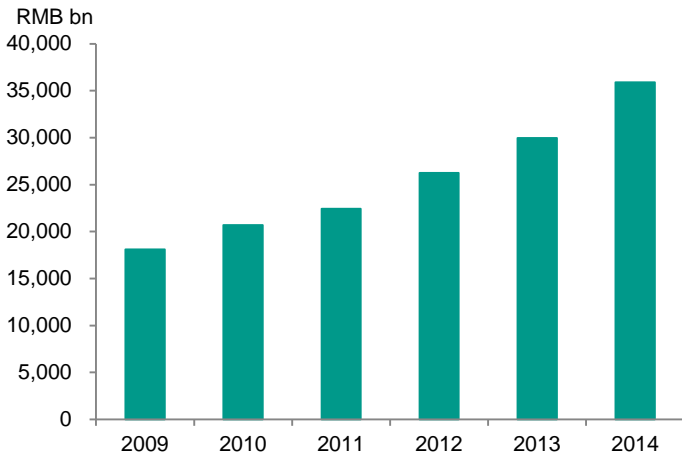


Source(s): WIND, ABCI Securities

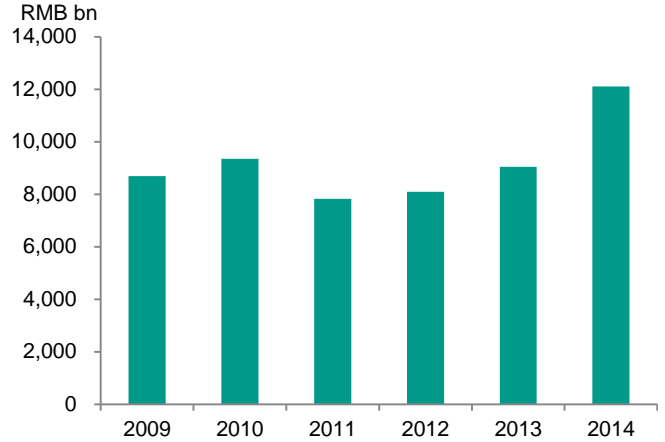
Exhibit 17: Gross proceeds raised through equity financing



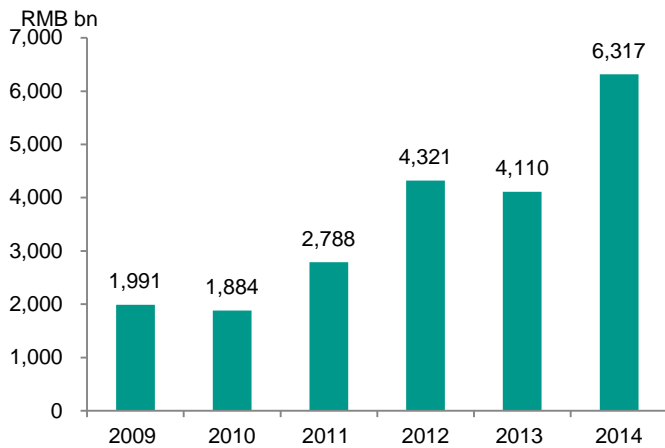
Source(s): WIND, ABCI Securities

**Exhibit 18: Outstanding balance of bonds in China**


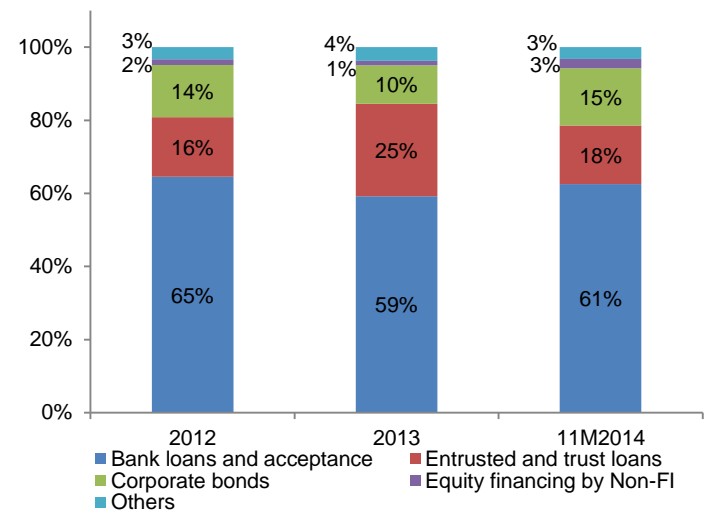
Source(s): WIND, ABCI Securities

**Exhibit 19: New bond issuance in China**


Source(s): WIND, ABCI Securities

**Exhibit 20: Total debt underwriting amount soared 54% YoY in 2014**


Source(s): WIND, ABCI Securities

**Exhibit 21: Composition for total social financing**


Source(s): PBOC, ABCI Securities

**Exhibit 22: Brokers' ranking by total equity underwriting amount 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 22: Brokers' ranking by total bond underwriting amount 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



## Potential relaxation of China's capital rules

According to the China Securities Journal, CSRC will be relaxing its risk management rules. The amendments under revision include: 1) lowering the regulatory requirement for net capital-to-net assets ratio, net capital-to-liabilities ratio, and net assets-to-liabilities ratio to 20%, 4% and 10% from the current 40%, 8%, and 20%, respectively; 2) introducing new measures, liquidity coverage ratio and net stable funding ratio; 3) lowering the capital deduction rate for long-term equity investment & fixed assets, and increasing the capital deduction rate for securities investments.

**Exhibit 24: Capital requirements for Chinese brokers**

	Old Warning level	New Warning level
Net capital/net assets (%)	>40%	>20%
Net capital/total liabilities (%)	>8.0%	>4.0%
Net assets/total liabilities (%)	>20.0%	>10.0%
Net capital/total capital reserves	>100%	>100%

Source(s): China Securities Journal, CSRC, ABCI Securities

**Exhibit 25: Capital and debt ratios for brokers**

	2012	2013	1H14	Warning level	Minimum/Maximum level
<b>Net capital/net assets</b>					
CITICS	56.0	48.5	57.1	>48%	>40%
HTS	67.0	65.0	61.0	>48%	>40%
CGS	78.0	82.0	n/a	>48%	>40%
CCS	74.8	71.2	n/a	>48%	>40%
<b>Net capital/total liabilities</b>					
CITICS	95.0	33.2	28.0	>9.6%	>8%
HTS	161.0	92.0	67.0	>9.6%	>8%
CGS	200.0	133.0	n/a	>9.6%	>8%
CCS	134.4	78.1	n/a	>9.6%	>8%
<b>Net assets/total liabilities</b>					
CITICS	170.0	68.3	48.9	>24%	>20%
HTS	239.0	142.0	110.0	>24%	>20%
CGS	256.0	163.0	n/a	>24%	>20%
CCS	179.7	109.6	n/a	>24%	>20%
<b>Net capital/total risk capital reserves</b>					
CITICS	1,333.0	849.7	750.1	>120%	>100%
HTS	1,429.0	1,281.0	1,145.0	>120%	>100%
CGS	663.0	909.0	n/a	>120%	>100%
CCS	543.0	478.0	n/a	>120%	>100%

Source(s): CSRC, ABCI Securities

Note 1: Warning level is set by the CSRC according to the Administrative Measures for the Risk Control Indicators of Securities firms in the PRC. If the risk control index is required to stay above a certain level, the warning level is 120.0% of the required minimum; and if the risk control index is required to stay below a certain level, the warning level is 80.0% of the required maximum.

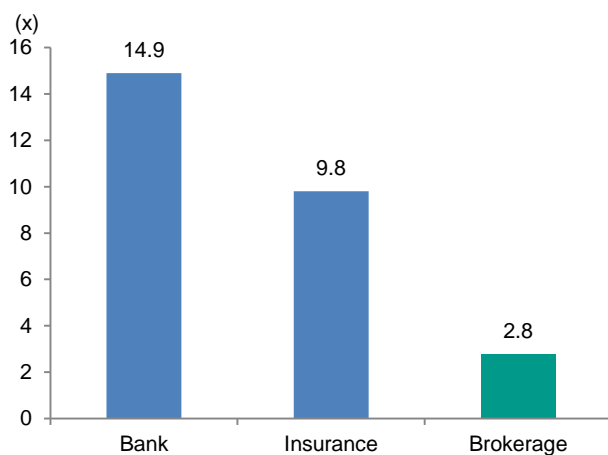
## Expansion of balance sheet leverage

China's securities industry is currently operating at a relatively low leverage (i.e. total asset/total equity). According to the Securities Association of China, the industry leverage in 2013 was 2.8x compared to 9.8x among China's insurers and 14.9x among China's banks. The low leverage was a result of the strict capital requirements and regulations in the industry that do not allow brokers to take aggressive position and leverage on its balance sheet for expansion.

Apart from regulatory factors, we believe another contributor to the low industry leverage is the lack of sustainable and profitable revenue channel and low-cost funding source to support a high-leverage business model, thus limiting the upside of the industry ROE. Under the new capital rules, if the net assets-to-liabilities ratio is lowered to 10%, the maximum leverage will be increased from 6x to 11x.

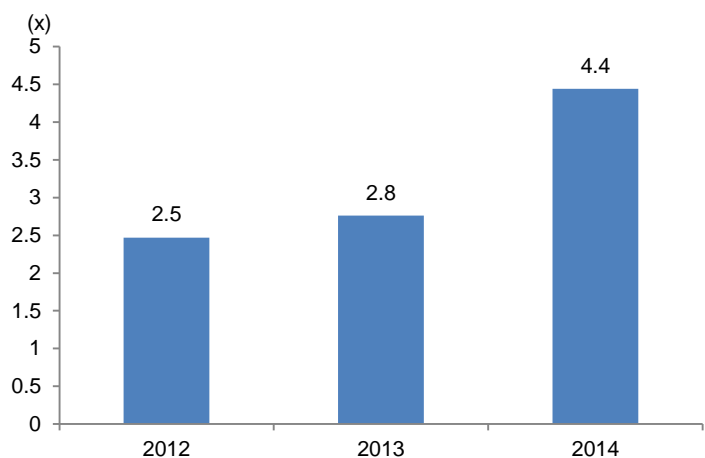
With the promotion of business innovation, CSRC has begun to adjust risk-control indicators and lower capital requirement. Moreover, financing channels and sources of fund have been diversifying with the issuance of corporate bonds, subordinated bonds, and short-term financing notes. Industry leverage increased from 2.8x in 2013 to 4.4x in 2014. Given the shift from a fee based to flow-based business, we expect the Chinese brokers will continue to leverage up by engaging in fundraising activities to support the rapid development of capital-intensive businesses. CITICS, HTS and CGS have announced their H-share placement plans in Dec 2014 and Jan 2015. CGS has also proposed A-share listing to support its flow-based businesses that demonstrated exponential growth. We expect the progressive regulatory relaxation would support the development of new, capital-intensive businesses among brokers, thus raising the industry's ROE in the long run.

**Exhibit 26: Gross leverage comparison**



Source(s): Company, ABCI Securities

**Exhibit 27: Sector gross leverage**



Source(s): Company, ABCI Securities



## Development trends of the PRC securities industry

### Emerging Internet-based securities services

PRC securities firms are actively developing various Internet-based securities services, such as online account opening, brokerage, sale of wealth management products and financing, to expand customer reach and lower operating costs. We believe this trend would help securities firms to enlarge customer base, increase their business efficiency, and facilitate product innovation.

### Open up of China's capital market

Shanghai-Hong Kong Stock Connect was officially launched on Nov 17, 2014. Through the program, investors in SEHK and SSE are allowed to trade eligible shares listed on the respective markets through local securities and brokerage firms. Initial aggregate quota for northbound trading is set at RMB 300.0bn, with a daily quota of RMB13.0bn; aggregate quota for southbound trading is RMB250.0bn, with a daily quota of RMB 10.5bn.

Although the mutual market connectivity would allow mainland and Hong Kong investors to trade stocks in each other's markets. The initial impact on revenue, however, would be limited in our view because only institutional investors and investors with a total balance over RMB 500,000 in their securities and cash accounts in China are qualified to trade in HKEx. Such investors account for less than 3% of the A-share investor base.

For the first 20 trading days, average usage of daily northbound quota was only 25.3%, which is far below expectation. Meanwhile, only 4.5% of daily southbound quota was utilized. The lukewarm success could be partially caused by the technical concerns of northbound investors. On Jan 2015, Chinese premier Li Keqiang hinted at a widely-anticipated cross-border trading program between Shenzhen and Hong Kong. We believe Shenzhen market is more appealing for foreign investors since the exchange focuses on small-cap firms within the technology and consumer sectors.

In our view, SH-HK stock connect is unlikely to generate substantial brokerage fee income with the limited quota; however, it would fuel market sentiment and enhance investors' confidence, benefiting multiple business lines such as investment banking and margin financing.

### Accelerated product innovation

China's capital markets provide limited financial products and services. CSRC seeks to encourage securities firms to develop and expand the financial product/service offering to include market-making, individual stock options, structured products, asset-backed securities, and interest swaps. We believe the increased product/service varieties will improve the business and profit of PRC securities firms.

Following the innovative development seminars in May 2012, China brokers carried out comprehensive program to redirect its effort to full-function development instead of sheer scale expansion, transforming to provide integrated financial. China's securities firms have been affected by intense competitions due to similar business models and product and service offerings. However, as the securities industry matures, business models of securities firms are evolving into ones with more differentiated and value-added services.



### Expanding financing channels

In Nov 2014, the CSRC published new regulations that allow securities firms to issue short-term financing bills. This new regulation is intended to diversify the financing sources for net capital replenishment and reduce the financing costs of securities firms.

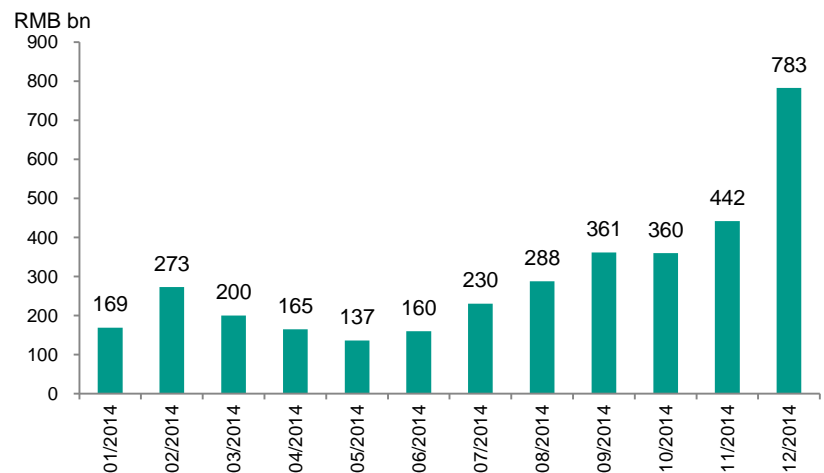
Besides regulatory factors, we believe the lack of low-cost funding source to support a high-leverage business model is one of the reasons behind the low industry leverage at present. The upside of the industry ROE has been limited for this reason. We believe near-term growth of the brokerage sector would be driven by the financing business and capital-intensive businesses. Relaxation of regulations and diversifying funding sources will facilitate the brokers' financing business.

### Investment summary

#### Strong performance in the A-share market

After the announcement of the interest rate cut by PBOC on Nov 21, 2014, A-share market turnover continued to hit new record high. ADT of the A-share market soared from RMB 160bn in June to RMB 783bn in Dec 2014. Moreover, MFSL balance exceeded 1,000bn by end-2014. Share price of brokers climbed on the A-share bull market. ABCI's macroeconomics team estimates that two more interest rate cuts would take place in 2015. We believe the ample liquidity supported by a moderately loose monetary policy would boost ADT and benefit the brokerage sector.

**Exhibit 28: ADT rocketed to 783bn in Dec 2014**



Source(s): Company, ABCI Securities

#### Bullish on China's brokerage sector

We are positive on the long-term prospects of China's brokerage sector due to the following reasons: 1) Strong trading volume in the A-share market; 2) New earnings driver from capital-based intermediary business; 3) Robust growth in investment banking business; 4) Potential relaxation of China's capital requirements; 5) Expansion of balance sheet leverage.



## Scenario analysis

Revenue growth of key business segment and earnings growth of the Chinese brokers have been highly correlated to performance of the A-share market and average daily turnover (ADT). Since A-share market turnover is highly cyclical and volatile, we have conducted a scenario analysis to investigate the impacts on earnings under different sets of assumption in the base, bull and bear cases.

**Exhibit 29: Scenario assumptions**

	2009	2010	2011	2012	2013	2014	2015E Base	2015E Bull	2015E Bear
Market Cap. (RMB bn)	24,394	26,542	21,476	23,036	23,908	37,693	41,462	45,231	38,446
% of GDP	72%	66%	45%	44%	41%	59%	60%	66%	56%
ADT	218	224	172	129	195	301	386	463	232
Turnover velocity (with ref. to weighted average tradable A-share market cap.)	355%	284%	256%	182%	245%	288%	280%	320%	180%
MFSL Balance (RMB mn)			38,207	89,516	346,527	1,025,656	1,502,050	2,098,849	1,089,766
% of MFSL balance to weighted average tradable A-share market cap.)			0.22%	0.52%	1.83%	4.00%	4.50%	6.00%	3.50%

Source(s): ABCI estimates

**Exhibit 30: Earning impact on brokers under different scenario**

	Base case	Bear case	vs base case	Bull case	vs base case
<b>2015E Net profit (RMB mn)</b>					
CITICS	11,264	8,448	-25%	15,544	38%
HTS	10,964	8,113	-26%	15,350	40%
CGS	4,754	3,233	-32%	7,369	55%
CCS	702	414	-41%	1,123	60%

Source(s): ABCI estimates

## CGS (6881 HK) remains our sector top pick

We expect China's brokers, the key beneficiaries of the capital market reforms, to demonstrate sound earnings growth. Our sector top pick is CGS (6881 HK). We believe its solid capital position, leading market share in brokerage income, conservative investment portfolio, and highest ROAE among peers would allow the Group to outperform. We reiterate our **BUY** rating on CGS with a TP of HK\$12.0.

We initiate coverage of CITICS, HTS and CCS with a **BUY** rating; our respective TPs for the companies are HK\$32.4, HK\$22.2 and HK\$ 9.1.

For 2015E, we expect ADT of the A-share market to reach RMB 386bn on monetary easing. CGS would be the key beneficiary of A-share market recovery given its strong brokerage business. Besides, the Group has a sound capital position – net capital/net assets ratio was 82% in 2013, higher than CSRC's required standard of 40%. A strong capital position would enable CGS to further develop its capital-based intermediary businesses, including MFSL, which in turn will reduce CGS's reliance on tradition brokerage business and enable a more balanced revenue mix. Moreover, CGS's FY13 ROAE at 10% was the highest among peers (CITICS: 6.0%, HTS: 6.7%, CCS: 6.3%), yet the counter is trading at a discount.



## Risk factors

- Decrease in market turnover and intensified competition in brokerage commission rate may have significant adverse impacts on brokerage revenue.
- Volatility in the A-share market may cause investment losses for the proprietary trading business.
- Lower-than-expected growth in flow-based businesses such as MFSL, stock-repo, and stock pledged lending upon downturn in A-share market.
- Regulatory issues that may hinder development and growth of innovative business.
- Slower-than-expected China economic growth may dampen market sentiment and A-share market turnover.
- Higher-than-expected costs of borrowing may squeeze the net interest margin of capital-intensive businesses.
- Brokers may raise capital to further expand capital-based intermediary businesses. Depending on the size of such fundraising activity, EPS and ROE of existing shareholders could be diluted.



**Exhibit 31: Peer comparison table**

		Market cap (USD mn)	Price Local ccy	P/B (x)			P/E (x)			ROE (%)			Div yield (%)			
				2014E	2015E	2016E	2014E	2015E	2016E	2013A	2014E	2015E	2016E	2014E	2015E	2016E
<b>H-share Securities</b>																
CITIC SECURITIES CO LTD-H	6030 HK	48,831	25.15	2.39	2.14	1.96	24.33	19.38	16.91	6.02	9.96	11.80	12.17	1.33	1.68	1.91
HAITONG SECURITIES CO LTD-H	6837 HK	31,033	17.48	2.12	1.78	1.64	19.42	15.45	13.89	6.71	10.45	11.95	11.97	1.53	1.92	2.19
CHINA GALAXY SECURITIES CO-H	6881 HK	8,498	8.74	2.09	1.68	1.49	15.85	12.33	11.79	10.02	12.50	14.30	13.81	1.79	2.16	2.36
CENTRAL CHINA SECURITIES C-H	1375 HK	2,397	7.06	2.81	2.47	2.14	27.29	19.68	17.65	6.39	9.27	11.07	13.14	1.06	1.42	1.59
Average				2.28	1.98	1.81	21.94	17.39	15.42	15.42	10.35	12.07	12.28	1.43	1.80	2.04
<b>A-share Securities</b>																
SHENWAN HONGYUAN GROUP CO-A	000166 CH	46,663	19.65	7.66	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
NORTHEAST SECURITIES CO LT-A	000686 CH	5,487	17.54	4.19	3.95	3.70	44.52	42.99	50.84	6.56	8.00	7.30	8.10	0.40	0.37	0.63
GUOYUAN SECURITIES CO LTD-A	000728 CH	10,831	34.50	4.07	3.89	3.71	57.21	46.88	41.77	4.36	7.24	8.42	10.02	0.91	1.06	1.01
SEALAND SECURITIES CO LTD -A	000750 CH	5,983	16.20	5.73	4.95	n/a	62.79	50.31	62.31	6.92	n/a	n/a	n/a	n/a	n/a	n/a
CHANGJIANG SECURITIES CO L-A	000783 CH	10,734	14.16	5.02	4.19	3.70	34.96	30.06	28.90	8.11	12.61	14.22	16.15	0.71	0.99	1.27
SHANXI SECURITIES CO LTD-A	002500 CH	5,737	14.25	n/a	4.55	4.33	78.30	57.46	46.72	4.00	7.40	5.50	5.60	0.42	0.35	0.35
WESTERN SECURITIES CO LTD-A	002673 CH	6,094	31.77	8.20	5.39	5.60	70.92	55.74	32.09	6.02	13.90	16.40	18.70	0.44	0.66	0.88
CITIC SECURITIES CO-A	600030 CH	48,831	28.62	3.40	3.07	2.80	35.46	30.38	26.48	6.02	9.79	10.79	11.24	0.89	1.02	1.22
SINOLINK SECURITIES CO LTD-A	600109 CH	7,813	17.23	5.81	5.44	4.71	49.51	36.20	29.40	4.85	9.36	12.32	12.23	0.61	0.87	1.03
SOUTHWEST SECURITIES CO LT-A	600369 CH	8,288	18.37	3.27	2.94	2.68	42.13	31.95	24.53	5.94	8.75	9.59	11.75	0.71	0.99	1.39
HAITONG SECURITIES CO LTD-A	600837 CH	31,033	21.39	3.12	2.74	2.58	31.78	26.05	23.64	6.71	10.43	12.08	12.02	0.91	1.20	1.41
CHINA MERCHANTS SECURITIES-A	600999 CH	22,838	24.60	3.54	3.15	2.89	37.85	27.06	24.28	8.43	9.68	11.34	13.95	0.91	1.10	1.02
PACIFIC SECURITIES CO/THE-A	601099 CH	6,862	12.16	6.92	4.64	4.44	121.60	83.86	64.00	3.46	8.90	10.23	11.07	0.40	0.53	0.33
INDUSTRIAL SECURITIES CO-A	601377 CH	11,138	13.40	5.18	4.39	4.21	48.38	35.45	34.36	6.20	10.07	13.01	16.57	0.56	0.92	0.95
SOOCHOW SECURITIES CO LTD-A	601555 CH	7,902	18.31	4.52	3.77	3.73	49.35	37.67	28.88	4.97	9.40	11.20	12.48	0.55	0.75	0.89
HUATAI SECURITIES CO LTD-A	601688 CH	20,086	22.44	3.29	2.97	2.83	36.49	27.27	24.23	6.33	8.70	10.82	12.89	0.95	1.18	1.28
EVERBRIGHT SECURITIES CO -A	601788 CH	13,205	24.17	3.38	3.13	3.05	55.06	36.73	31.80	0.91	5.42	7.90	10.42	0.56	0.97	1.11
FOUNDER SECURITIES CO LTD-A	601901 CH	12,266	12.58	4.96	3.20	3.12	48.95	35.64	37.22	7.40	9.10	10.37	12.40	0.64	0.95	0.40
Average				3.95	3.48	3.15	44.35	34.37	30.42	30.42	9.32	10.77	11.98	0.75	0.96	1.05
<b>Local Securities</b>																
GUOTAI JUNAN INTERNATIONAL	1788 HK	1,692	5.77	2.29	1.67	1.50	15.68	12.97	11.10	14.63	15.97	14.86	14.94	3.29	3.90	4.59
CHINA EVERBRIGHT LTD	165 HK	3,674	16.90	1.01	0.92	0.86	15.59	13.81	12.20	4.74	6.55	6.72	6.88	2.41	2.72	3.05
SHENYIN WANGUO HK LTD	218 HK	738	7.19	4.08	n/a	n/a	n/a	n/a	n/a	3.86	n/a	n/a	n/a	n/a	n/a	n/a
FIRST SHANGHAI INVESTMENTS	227 HK	296	1.64	0.87	n/a	n/a	n/a	n/a	n/a	1.64	n/a	n/a	n/a	n/a	n/a	n/a
HAITONG INTERNATIONAL SECURI	665 HK	1,395	4.95	1.34	1.20	1.11	11.51	10.27	8.62	12.95	13.18	12.80	13.77	4.10	4.91	6.26
CINDA INTERNATIONAL HOLDINGS	111 HK	122	1.47	1.47	1.36	1.30	34.19	29.40	26.73	11.49	4.30	4.70	5.00	n/a	n/a	n/a
Average				1.63	1.17	1.08	15.11	13.16	11.46	11.46	10.17	9.92	10.23	2.98	3.47	4.10

Note: Closing price as at Jan 26, 2015

Source(s): Bloomberg, ABCI Securities



January 27, 2015  
Company Report  
Rating: BUY  
TP: HK\$ 12.00

Share price (HK\$)	8.74
Est. share price return	37.3%
Est. dividend yield	2.1%
Est. total return	39.4%

Analyst : Pandora Leung  
Tel: (852) 2147 8809  
Email: pandoraleung@abci.com.hk

**Key Data**

52Wk H/L(HK\$)	11.5/4.22
Issued shares (mn)	7,537.3
Market cap (HK\$ mn)	65,876
3-mth avg daily turnover (HK\$ mn)	497
Major shareholder(s) (%):	
Huijin	68.2

Source(s): Company, Bloomberg, ABCI Securities

**1H14 Revenue breakdown (%)**

Brokerage	69
Trading	14
Investment Banking	10
Asset management	2
Others	5

Source(s): Company, ABCI Securities

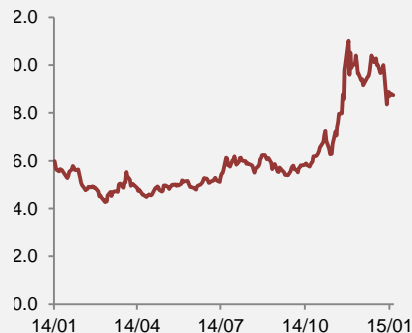
**Share performance (%)**

	Absolute	Relative*
1-mth	-4.48	-10.46
3-mth	49.91	41.55
6-mth	42.58	39.82

\*Relative to HSI

Source(s): Bloomberg, ABCI Securities

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



Source(s): Bloomberg, ABCI Securities

China Galaxy Securities (6881 HK)  
Key beneficiary of A-share market revival

- Trading volume and market sentiment have been strong in the A-share market. CGS, with its sound capital position, conservative investment portfolio and highest ROAE among peers, will benefit much from the A-share market revival and is our top pick for the sector.
- Maintain **BUY** with revised TP of HK\$ 12.00, which implies 2.0x 2015E P/B.

**Proxy for A-share market trading volume.** Trading volume was strong in the A-share market, with average daily turnover (ADT) in Dec 14 reaching RMB 784bn (vs. RMB 442bn in Nov 14). We expect ADT of the A-share market to reach ~RMB 386bn in 2015E due to recent monetary easing. Thus, CGS would be the key beneficiary of A-share market recovery since brokerage commission accounted for 53% of its total revenue in 2013 (CITICS: 34%, HTS: 37%).

**Sound capital position.** Net capital/net assets ratio was 82% in 2013 (CITICS: 49%, HTS: 65%), higher than CSRC's required standard of 40%. A strong capital position enables CGS to further develop its capital intensive businesses such as margin financing and securities lending (MFSL). The increasing contribution from flow-based business would reduce CGS's reliance on tradition brokerage business to develop a more well-balanced revenue mix.

**Conservative investment portfolio.** For 2013 and 1H14, CGS's investment portfolio accounted for 63% and 58% of total shareholders' equity, lower than that of CITICS (2013: 121%, 1H14: 168%) and HTS (2013: 100%, 1H14: 107%). For its portfolio mix in 1H14, equity investment accounted for only 7% of total investment (CITICS: 33%, HTS: 23%) while fixed income investment accounted for 85% of total investment (CITICS: 53%, HTS: 57%), rendering the Group less vulnerable to market volatility.

**A-share listing to strengthen position.** CSRC has already accepted the IPO application of CGS, successful listing in the A-share market could strengthen its capital position as well as its competitiveness in the market after the slew of M&A activities in the industry last year. Besides, CGS proposed to place no more than 2bn of H-shares in Jan 2015. Stronger capital position enables CGS to expand capital intensive businesses, such as margin financing and quasi-lending business, thus optimizing its revenue mix.

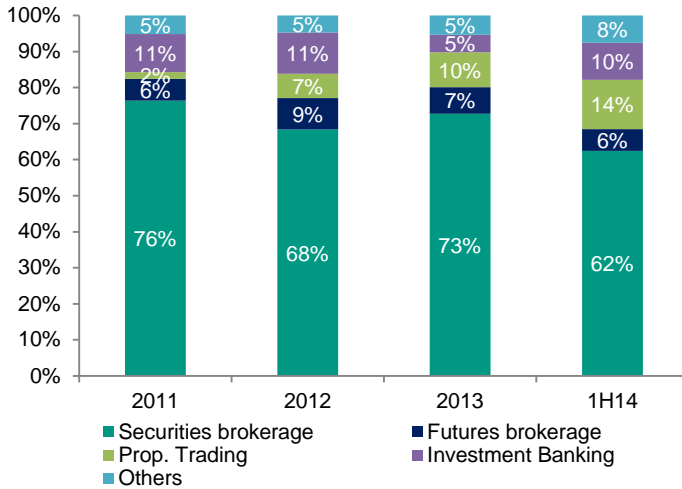
**Maintain BUY with revised TP of HK\$ 12.00.** CGS's annualized ROAE in 1H14 was 10.4%, the highest among peers (CITICS: 9.2%, HTS: 9.1%, CCS: 7.6%), yet the counter is trading at a discount to peers. CGS, a key beneficiary of A-share market revival, is our top pick for the sector. We maintain BUY with revised TP of HK\$12.00, which implies 2.0x 2015E P/B.

Risk factors: 1) Further decline in brokerage commission rates; 2) Sharp decline in A-market turnover; 3) Slowdown in China's economic growth; 4) Sharp decline in MFSL growth; 5) EPS dilution risk on share placement

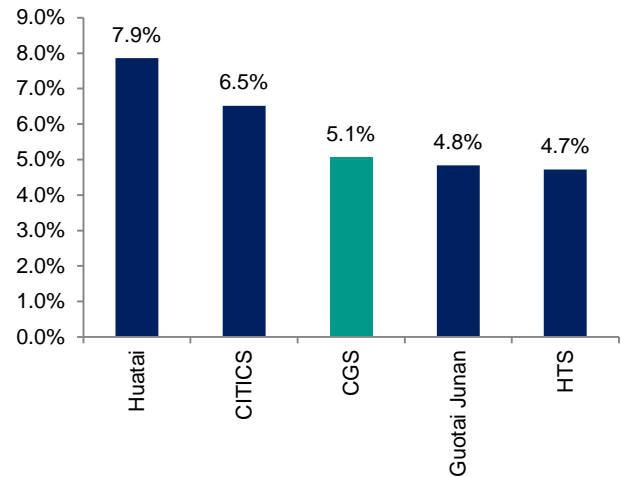
**Financial Summary**

FY ended Dec 31	2012A	2013A	2014E	2015E	2016E
Revenue (RMB mn)	5,962	8,426	12,201	15,053	17,775
Chg (% YoY)	(7.3)	41.3	44.8	23.4	18.1
Net profit (RMB mn)	1,420	2,135	3,785	4,754	5,661
Chg (% YoY)	(10.0)	50.4	77.3	25.6	19.1
EPS (RMB)	0.24	0.31	0.50	0.56	0.59
Chg (% YoY)	(10.0)	30.0	63.2	10.9	6.6
BVPS (RMB)	2.90	3.34	3.77	5.10	5.51
Chg (% YoY)	8.9	15.0	12.8	35.3	8.1
P/E (x)	29.2	22.5	13.8	12.4	11.6
P/B (x)	2.4	2.1	1.8	1.4	1.3
ROAE (%)	8.5	9.9	14.0	12.2	11.1
ROAA (%)	2.3	3.0	3.7	3.4	3.6
DPS(RMB)	-	0.06	0.15	0.15	0.18
Yield (%)	-	0.9	2.2	2.2	2.6

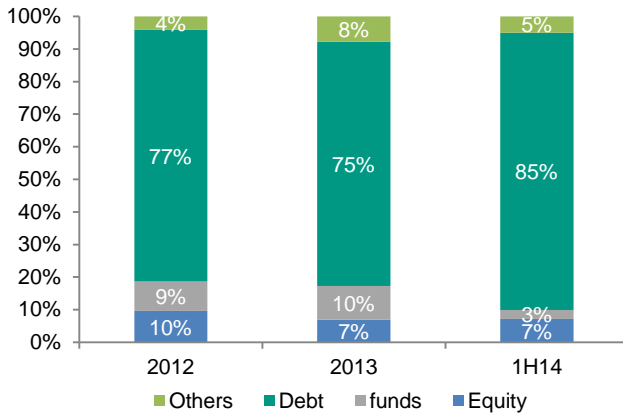
Source(s): Bloomberg, ABCI Securities estimates

**Exhibit 32: CGS's revenue mix**


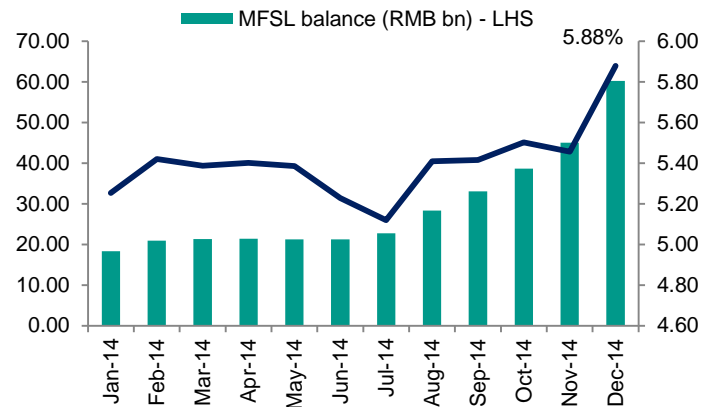
Note: Others include asset management, PE investment and overseas business  
 Source(s): WIND, ABCI Securities

**Exhibit 33: Market share by trading volume (stocks + funds) in 2014**


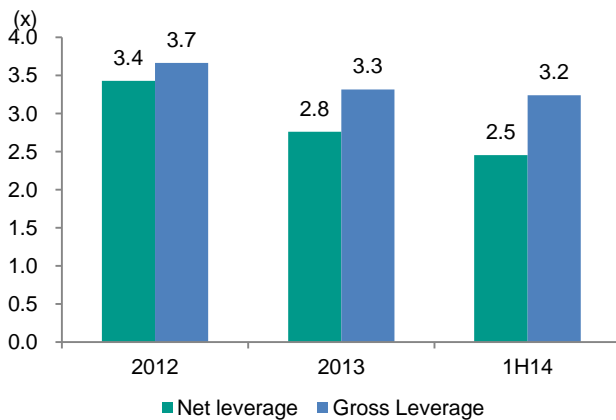
Source(s): Company, ABCI Securities

**Exhibit 34: CGS's investment assets mix by securities category**


Source(s): WIND, ABCI Securities

**Exhibit 35: CGS's MFSL balance**


Source(s): WIND, ABCI Securities

**Exhibit 36: CGS's gross and net leverage ratios**


Source(s): WIND, ABCI Securities

**Exhibit 37: 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



**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	3,831	5,039	5,896	6,317	6,504
Interest income	1,699	2,666	4,804	6,909	9,097
Investment income	395	697	1,475	1,801	2,147
Other income	38	23	25	26	28
<b>Revenue</b>	<b>5,962</b>	<b>8,426</b>	<b>12,201</b>	<b>15,053</b>	<b>17,775</b>
Operating costs	(4,075)	(5,533)	(7,093)	(8,645)	(10,149)
<b>Operating profits</b>	<b>1,886</b>	<b>2,893</b>	<b>5,108</b>	<b>6,409</b>	<b>7,626</b>
Associates & JCEs	0	0	0	(0)	(0)
<b>Profit before tax</b>	<b>1,886</b>	<b>2,893</b>	<b>5,108</b>	<b>6,408</b>	<b>7,626</b>
Tax	(454)	(738)	(1,302)	(1,634)	(1,945)
<b>Profit after tax</b>	<b>1,433</b>	<b>2,155</b>	<b>3,805</b>	<b>4,774</b>	<b>5,681</b>
Minority interests	(13)	(20)	(20)	(20)	(21)
<b>Net profits</b>	<b>1,420</b>	<b>2,136</b>	<b>3,785</b>	<b>4,754</b>	<b>5,661</b>
<b>Growth (%)</b>					
Fee and commission income (%)	(17.9)	31.6	17.0	7.1	2.9
Interest income (%)	4.3	57.0	80.2	43.8	31.7
Investment income (%)	278.1	76.6	111.6	22.1	19.2
Other income (%)	13.2	(39.1)	9.4	5.9	5.9
Total Revenue (%)	(7.3)	41.3	44.8	23.4	18.1
Total Operating costs (%)	(2.3)	35.8	28.2	21.9	17.4
Operating profit (%)	(16.6)	53.4	76.5	25.5	19.0
Net profit (%)	(10.0)	50.4	77.3	25.6	19.1
<b>Operating performance (%)</b>					
Operating margin (%)	31.6	34.3	41.9	42.6	42.9
Net margin (%)	23.8	25.3	31.0	31.6	31.8
Effective tax rate (%)	24.1	25.5	25.5	25.5	25.5
Dividend payout (%)	-	20.2	30.0	30.0	30.0
ROAE (%)	8.5	9.9	14.0	12.2	11.1
ROAA (%)	2.3	3.0	3.7	3.4	3.6
<b>Segmental revenue (RMB mn)</b>					
Securities brokerage	4,081	6,174	8,181	9,799	11,021
Futures brokerage	521	623	773	991	1,275
Proprietary trading	401	824	1,220	1,529	1,701
Investment bank	685	411	1,435	1,573	1,845
Asset management	45	137	171	245	336
Private equity investment	25	10	27	32	35
Overseas	33	203	248	638	1,106
Other income	169	46	146	245	520

Source(s): Company, ABCI Securities estimates



**Consolidated balance sheet (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>
Fixed assets	516	394	409	426	434
Goodwill	223	223	223	223	223
Other intangible assets	363	349	367	378	389
Investment securities	743	495	520	546	573
Other non-current assets	174	328	266	217	178
<b>Total non-current assets</b>	<b>2,019</b>	<b>1,789</b>	<b>1,786</b>	<b>1,790</b>	<b>1,797</b>
Cash & equivalents	36,607	33,084	40,362	45,206	48,822
Advances to customers	5,439	18,393	52,520	68,520	75,372
Trading securities	4,622	5,027	5,476	5,802	6,145
Investment securities	6,739	10,238	12,756	15,478	17,555
Other current assets	8,870	9,754	12,366	14,351	16,874
<b>Total current assets</b>	<b>62,277</b>	<b>76,495</b>	<b>123,480</b>	<b>149,357</b>	<b>164,769</b>
<b>Total assets</b>	<b>64,296</b>	<b>78,284</b>	<b>125,266</b>	<b>151,146</b>	<b>166,566</b>
Accounts payable	39,746	36,451	38,274	41,336	44,643
Other liabilities	6,991	16,411	58,307	60,695	68,806
<b>Current liabilities</b>	<b>46,737</b>	<b>52,863</b>	<b>96,581</b>	<b>102,031</b>	<b>113,448</b>
<b>Net current assets</b>	<b>15,540</b>	<b>23,632</b>	<b>26,899</b>	<b>47,326</b>	<b>51,320</b>
<b>Total assets less current liabilities</b>	<b>17,559</b>	<b>25,422</b>	<b>28,685</b>	<b>49,115</b>	<b>53,118</b>
Issued bonds	-	-	-	-	-
Other non-current liabilities	-	-	-	-	-
<b>Total non-current liabilities</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Net assets</b>	<b>17,559</b>	<b>25,422</b>	<b>28,685</b>	<b>49,115</b>	<b>53,118</b>
Equity attributable to owners of the parent	17,430	25,175	28,401	48,629	52,592
Minority interest	129	247	284	486	526
<b>Total equity</b>	<b>17,559</b>	<b>25,421</b>	<b>28,685</b>	<b>49,115</b>	<b>53,118</b>

Source(s): Company, ABCI Securities estimates



January 27, 2015  
Company Report  
Rating: BUY  
TP: HK\$ 32.40

Share price (HK\$)	25.15
Est. share price return	28.8%
Est. dividend yield	1.4%
Est. total return	30.2%

Analyst : Pandora Leung  
Tel: (852) 2147 8809  
Email: pandoraleung@abci.com.hk

**Key Data**

52Wk H/L(HK\$)	33.95/13.72
Issued shares (mn)	
H-share	1,178.3
A-share	9,838.6
Market cap	
H-share (HK\$m)	29,634
A-share (HK\$m)	348,972
3-mth avg daily turnover (HK\$ mn)	695
Major shareholder(s) (%):	
CITIC Group Corporation	20.3

Source(s): Company, Bloomberg, ABCI Securities

**1H14 Revenue breakdown (%)**

Brokerage	28
Trading	35
Investment Banking	6
Asset management	14
Others	17

Source(s): Company, ABCI Securities

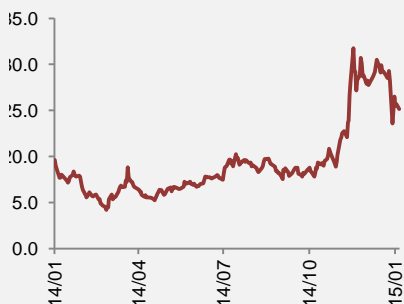
**Share performance (%)**

	Absolute	Relative*
1-mth	-9.37	-15.05
3-mth	38.04	30.34
6-mth	27.92	25.45

\*Relative to HSI

Source(s): Bloomberg, ABCI Securities

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



Source(s): Bloomberg, ABCI Securities

## CITIC Securities (6030 HK)

### Key beneficiary of capital market reform

- Net investment banking fee income surged 168% YoY for 9M14 after A-share IPO had resumed in 1Q14. Given CITICS's leading position in the underwriting business, we expect its investment banking fee income would continue to rebound in 2015.
- As at Dec 31, 2014, CITIC's MFSL balance reached RMB 72.1bn and was ranked 1<sup>st</sup> in China with a market share of 7.0%. We expect CITICS would continue to optimize revenue mix
- Initiate **BUY** with TP at HK\$ 32.40, equivalent to 2.4 x 2015E P/B.

**A leader in multiple business lines.** CITICS is the leading full-service investment bank in China and the largest securities firm in China. According to the SAC, CITICS was ranked 1<sup>st</sup> by total assets, net assets, and total revenue as of Dec 31, 2013. It also ranked 1<sup>st</sup> in terms of net income from investment banking business and net income from margin financing and securities lending (MFSL) business.

**Diversified revenue mix.** Trading, brokerage, asset management, and investment banking accounted for 35.0%, 27.5%, 14.0% and 5.6%, respectively, of the Group's total revenue in 1H14. Recognizing the challenges entailed in the traditional business model that relies heavily on retail brokerage, CITICS has been an early mover in diversifying its business into flow-based areas. As at Dec 31, 2014, CITIC's MFSL balance reached RMB 72.1bn and was ranked 1<sup>st</sup> in China with a market share of 7.0%. We also expect the Group would continue to optimize its revenue mix.

**Promising outlook for investment banking business.** According to Wind, CITICS was ranked 1st by debt underwriting amount and 2<sup>nd</sup> by equity underwriting amount among the Chinese brokers in 2014. Net investment banking fee income saw a robust growth of 168% YoY for 9M14. With its leading position in underwriting business, we expect its investment banking fee income would continue to rebound in 2015.

**Double-digit ROAE is expected in medium term.** The Group's gross leverage rose to 3.5x for 9M14 (vs. 2013: 2.5x) while core leverage (exclude client's deposits) reached 3.1x (vs 2013: 2.1x) for the same period. We expect the industry leverage would continue to climb on relaxation of capital rules, improving the industry ROAE over the long run. CITIC's ROAE in 9M14 increased by 2.81ppts to 7.05% on higher balance sheet leverage. Although its recent H-share placement may have diluted its ROAE, we expect the figure to reach double digits in the medium term.

**Initiate CITICS with BUY on its leading position.** CITICS would be the key beneficiary of the ongoing capital market reform and potential relaxation of capital rules. Its leading position in the industry and positive growth prospects have prompted us to initiate our coverage with a **BUY rating**. Our DDM-derived TP of HK\$ 32.40 implies 2.4x 2015E P/B.

**Risk factors:** 1) Weaker-than-expected A-share market; 2) Slowdown in MFSL business; 3) Slowdown in China's economic growth; 4) EPS dilution risk on share placement.

**Financial Summary**

FY ended Dec 31	2012A	2013A	2014E	2015E	2016E
Revenue (RMB mn)	13,071	20,279	32,829	43,504	53,818
Chg (% YoY)	(50.4)	55.1	61.9	32.5	23.7
Net profit (RMB mn)	4,237	5,244	9,054	11,264	13,322
Chg (% YoY)	(66.3)	23.8	72.7	24.4	18.3
EPS (RMB)	0.38	0.48	0.82	0.96	1.06
Chg (% YoY)	(68.8)	23.8	72.7	16.5	11.2
BVPS (RMB)	7.85	7.96	8.58	10.88	11.70
Chg (% YoY)	(0.1)	1.4	7.8	26.8	7.5
P/E (x)	51.9	41.9	24.3	20.9	18.8
P/B (x)	2.5	2.5	2.3	1.8	1.7
ROAE (%)	4.9	6.0	9.9	9.8	9.4
ROAA (%)	2.7	2.4	2.8	2.7	2.7
DPS(RMB)	0.30	0.15	0.25	0.29	0.32
Yield (%)	1.5	0.8	1.2	1.4	1.6

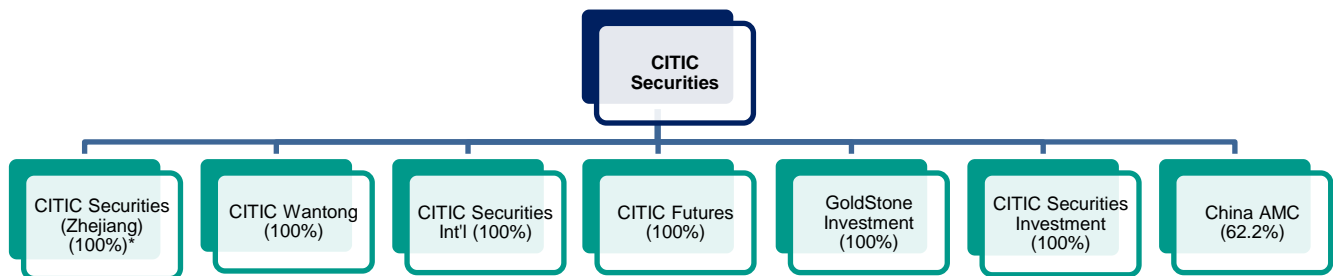
Source(s): Bloomberg, ABCI Securities estimates

## Company Profile

Established in 1995, CITICS is the leading full-service investment bank in China as well as the largest securities firm in China. According to the SAC, CITICS was ranked No.1 by total assets, net assets, and total revenue as of Dec 31, 2013. It also was ranked No.1 in terms of net incomes from investment banking business and margin financing and securities lending (MFSL) business.

The Company currently owns 6 wholly-owned principal subsidiaries, namely, the CITIC Securities (Zhejiang), CITIC Wantong Securities, CITIC Securities Int'l Co. Ltd. ("CSI"), CITIC Futures, GoldStone Investment and CITIC Securities Investment. It also has 1 principal controlling subsidiary, China Asset Management Co., Ltd. ("China AMC").

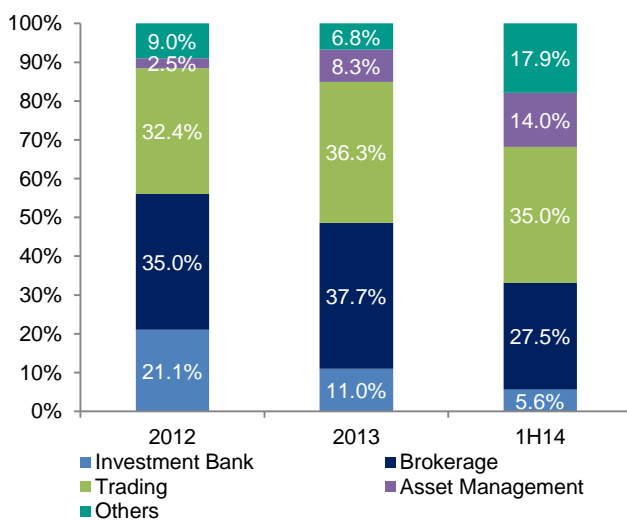
**Exhibit 38: CITICS' s 7 principal subsidiaries**



Note: CITICS proposed absorption and merger of CITIC Securities (Zhejiang) to further integrate internal resources; the proposal is subject to shareholders' approval  
 Source(s): Company, ABCI Securities

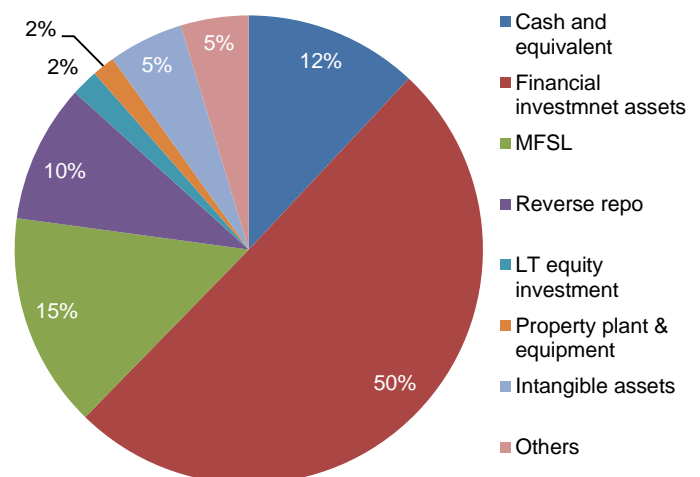
Principal lines of business include brokerage, investment banking, and asset management. Trading, brokerage, and asset management accounted for 35.0%, 27.5% and 14.0% of the Group's total revenue in 1H14.

**Exhibit 39: CITICS's revenue mix**



Source(s): Company, ABCI Securities

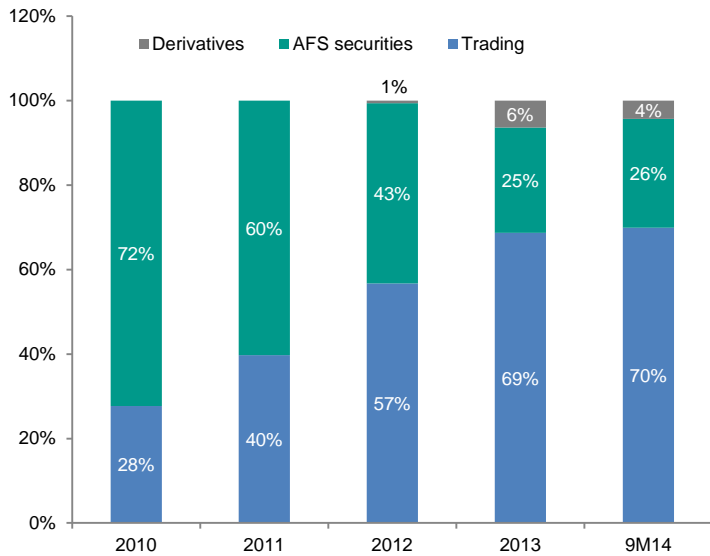
**Exhibit 40: CITICS's asset breakdown as at end-2013**



Source(s): Company, ABCI Securities

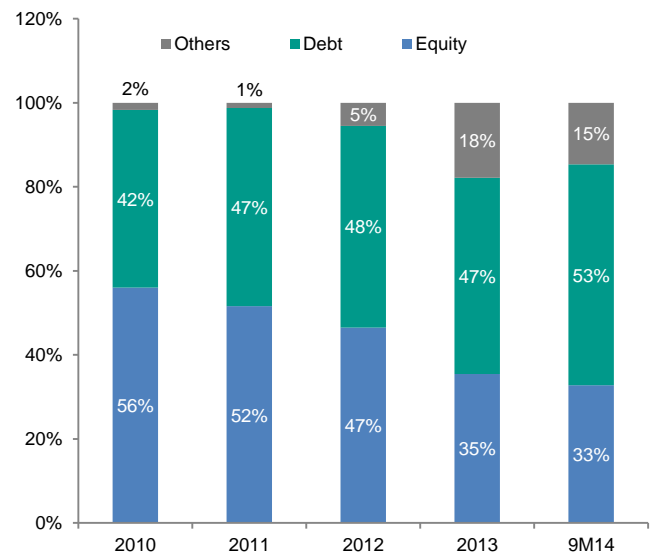


Exhibit 41: Investment asset mix by accounting category



Source(s): Company, ABCI Securities

Exhibit 42: Investment asset mix by securities category



Source(s): Company, ABCI Securities

## Leading position across different business lines

### Investment banking business

Investment banking services primarily include equity financing, debt financing, and financial advisory to institutional clients. The number of listed companies in China increased rapidly from 1,700 in 2009 to 2,613 in 2014, representing a CAGR of 9.0%.

After the stock market downturn in 2008, China's equity financing increased rapidly from 2009 to 2011. Due to the IPO suspension by CSRC in 2012, equity financing decreased sharply in 2012-13. Along with the reduced demand for bond issuance pressured by the rising bond yields in 2H13, CITICS' investment banking business declined by 19.3% YoY to RMB 2,224mn in 2013.

Since China resumed A-share IPO market in 1Q14, a total of 125 companies have executed their IPOs in 2014. Total new equity funds raised in 2014 (including IPO, placement and rights issuance) was RMB 772bn, up 89.5% YoY.

For debt financing, according to Wind, the amount of proceeds raised through bond issuance, including short-term financing bills and medium-term notes, corporate bonds, enterprise bonds, financial bonds, convertibles, government-backed institutional bonds, municipal bonds, asset-backed securities, and private placement notes increased from RMB 1,991bn in 2009 to RMB 6,317bn in 2014, representing a CAGR of 26.0%.

According to Wind, CITICS was ranked No.1 by debt underwriting amount and No.2 by equity underwriting amount among the Chinese brokers in 2014. Net investment banking fee income saw a robust growth of 168% YoY for 9M14. Given its leading position in underwriting business, we expect its investment banking fee income would continue to recover in 2015



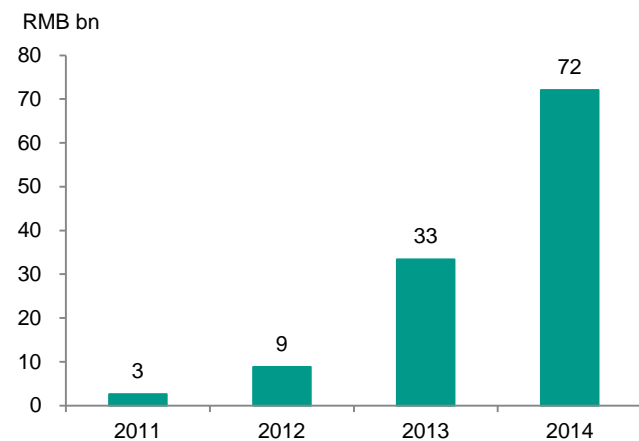


### Margin-financing and securities-lending business

According to SAC, CITICS was ranked the first in terms of the net income from margin financing and securities lending (MFSL) business in 2013.

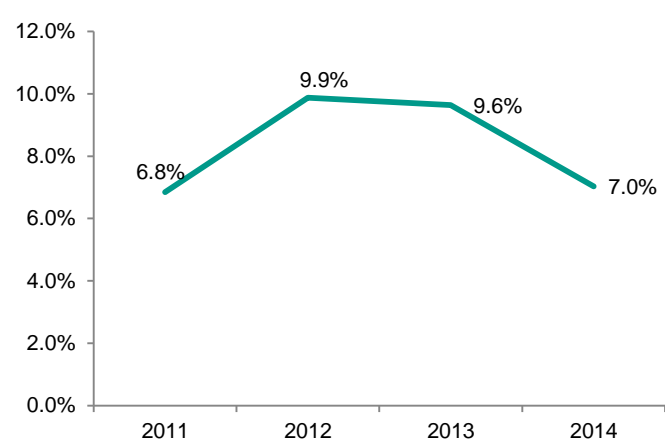
As at Dec 31 2014, the aggregate market share of the MFSL business of the Company, CITIC Securities (Zhejiang), and CITIC Securities (Shandong) was 7.0% and was ranked 1<sup>st</sup> in the market. Interest income on margin and other financing soared 180% YoY to RMB 2,219.5mn for 1H14. With the progressive deregulation of the financial industry, capital-based intermediary business is expected to be one of the Group's future earning drivers.

Exhibit 43: CITICS's MFSL balance



Source(s): WIND, ABCI Securities

Exhibit 44: Market share of CITICS's MFSL balance



Source(s): WIND, ABCI Securities

### Brokerage business

In 2014, CITICS recorded a total trading turnover of RMB 7.7tn of stocks and funds on the Shanghai Stock Exchange and Shenzhen Stock Exchange, representing a market share of 6.5% and was ranked No. 2 in the Chinese brokerage market.

Exhibit 45: Market share for brokerage trading in 2014

Ranking	Brokers	Stock and funds trading amount (RMB tr)	Market share (%)
1	Huatai	9.32	7.9%
2	<b>CITICS</b>	<b>7.72</b>	<b>6.5%</b>
3	CGS	5.99	5.1%
4	Guotai Junan	5.74	4.8%
5	Haitong	5.59	4.7%

Source(s): Wind, ABCI Securities

### Less vulnerable to commission rate pressure

The average commission rate of the industry stabilized in 2013 to reach ~ 7.9bps; however, it further declined to ~7.1bps in 1H14, down 0.1% as compared to end-2013. Apart from the competition from online discount brokerage firms, the recent removal of the 'one investor one account' policy is expected to intensify the competition and slash the brokerage commission rate further.

We believe CITICS is less vulnerable to the new accounting rules due to its



well-balanced revenue mix with less reliance on traditional brokerage business. Recognizing the inherent weakness of the traditional business model of the Chinese brokers that relies heavily on investment banking and retail brokerage, CITICS has been an early mover in diversifying its business into flow-based areas. In 1H14, the scale of flow-based businesses, such as margin financing, stock repo, stock-pledged repo, OTC derivatives, and ETF market-making, experienced rapid growth. We expect CITICS would continue to optimize revenue mix going forward.

### **Asset management business**

CITICS provides asset management services and products to domestic and overseas client. The Group provides collective-asset management (CAM) plans for retail customers, target-asset-management (TAM), and special-asset management (SAM) plans for high-net-worth individuals, institutional investors, annuity plans, and the National Social Security Fund (NSSF).

As at June 30, 2014, the Company's total AUM amounted to RMB 648,292mn, up 28.4% from end-2013, with CAM, TAM (including enterprise annuity and NSSF) and SAM contributing RMB 40,851mn, RMB 599,380mn and RMB 8,061mn, respectively.

### **China AMC**

CITICS conducted asset management business through its subsidiary, China AMC, which was acquired by the Group in Sep 2007. CITICS regained a controlling stake of 62.2% in China AMC as of 2013. The principal businesses of China AMC include fund raising, fund distribution, asset management, and other businesses permitted by CSRC. As at Dec 31, 2013, the staff size of China AMC was 710; its gross and net profits were RMB 1,285.37mn and RMB 970.79mn.

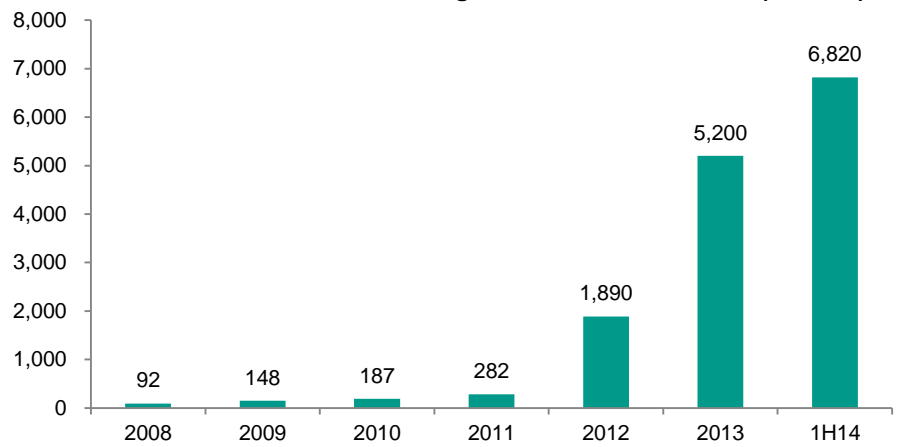
China AMC was the largest fund management company in China with a total AUM of RMB 432,374mn as at June 30, 2014, up 29.70% from end-2013; the AUM of its mutual funds was RMB 331,627mn, up 35.52% from end-2013. Its market share of 9.18% was the 2<sup>nd</sup> highest in China.

According to the SAC, the asset management business of PRC securities firms has grown substantially in 2008-13, with AUM increasing from RMB 92bn in 2008 to RMB 6.82tn in 1H14.

In 2013, asset management business accounted for 4% of the industry revenue, which is twice the percentage in 2012. The proportion further increased to 5% in 1H14. As social wealth and the number of high-net-worth individuals increase, we believe asset management business will continue to expand.



Exhibit 46: AUM of brokers' asset management business in China (RMB bn)



Source(s): SAC, WIND, ABCI Securities

### Synergies between CITICS and CLSA

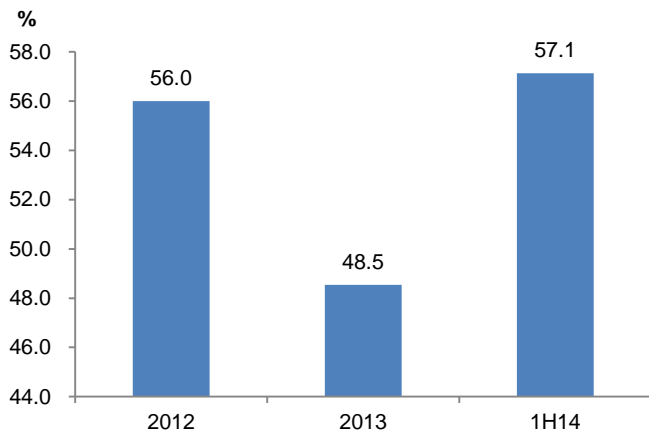
On July 31, 2013, the Group acquired a 100% interest in CLSA at a consideration of US\$ 1.09bn, or RMB 6.74bn, equivalent to 2.4x P/B based on the latter's net assets value by end-July 2013. CLSA contributed RMB 1,413mn in revenue and RMB 128mn in net profit in Aug-Dec 2013. Acquisition of CLSA provides the Group with a unique opportunity to develop its global equity business based on the former's strength in the Asia-Pacific region.

In our view, the synergies for CITICS and CLSA have yet to be realized as further business integration between two parties is necessary. Nonetheless, the acquisition marks an important step towards the Group's internationalization. CITICS would cooperate with CLSA to develop a global network to enhance cross-border business and expand market coverage in Europe, North America, Asia, Australia, and emerging markets such as Africa and South America. CLSA's overseas franchises in brokerage, research, and investment banking are expected to facilitate CITICS's overseas expansion plan.

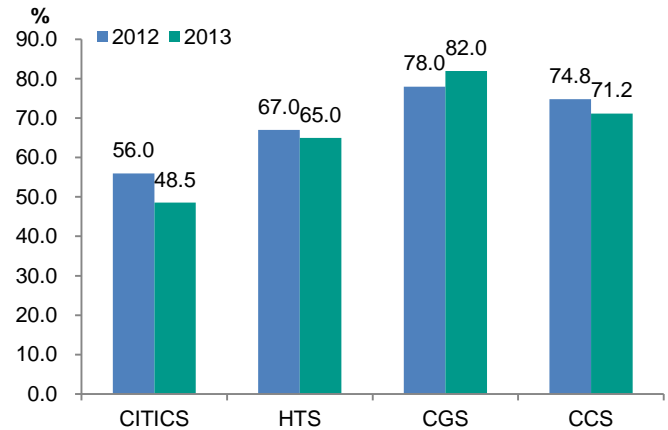
### Key beneficiary of potential capital rule relaxation

CITICS's capital has been stretched due to business expansion since long-term equity investment is currently 100% deductible in the net capital calculation. The Group's net capital-to-net asset ratio was 48.5% as at end-2013, close to the alert level of 48% primarily due to the consolidation of China AMC and CLSA.

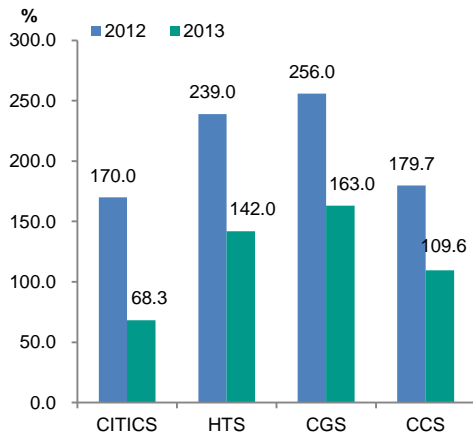
CITICS's net capital-to-net assets ratio increased to 57% as of June 30, 2014, rising by 8.6ppts HoH due to issuance of sub-debt and one-off disposal gain on asset sales. If the net capital-to-net assets ratio falls from 40% to 20%, we estimate that a 20ppt cut in net capital-to-net assets ratio requirement will free up ~RMB 14bn in capital for the Group. As CITIC's net capital-to-net assets ratio is the lowest among the HK-listed Chinese brokers, we believe it would benefit much from the potential relaxation of capital rules.

**Exhibit 47: CITIC's net capital/net assets ratio**


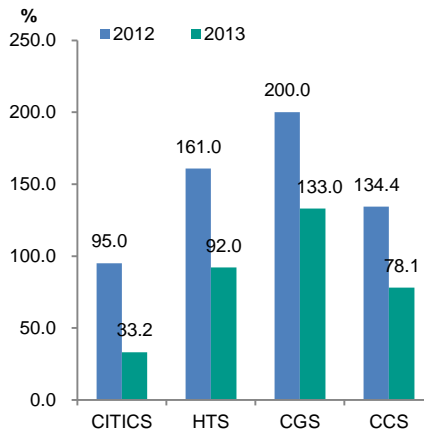
Source(s): Company, ABCI Securities

**Exhibit 48: Net capital/net assets ratio for HK-listed mainland brokers**


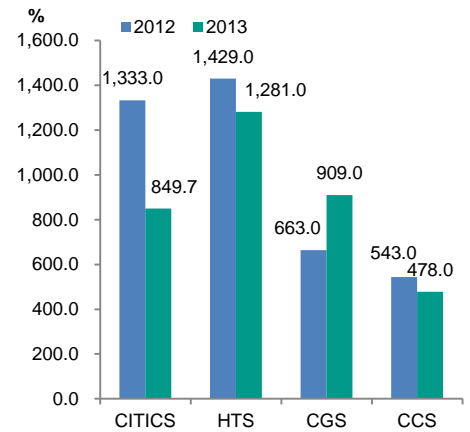
Source(s): Company, ABCI Securities

**Exhibit 49: Net assets/total liabilities ratio for HK-listed mainland brokers**


Source(s): Company, ABCI Securities

**Exhibit 50: Net capital/total liabilities ratio for HK-listed mainland brokers**


Source(s): Company, ABCI Securities

**Exhibit 51: Net capital/total risk capital reserves ratio for HK-listed mainland brokers**


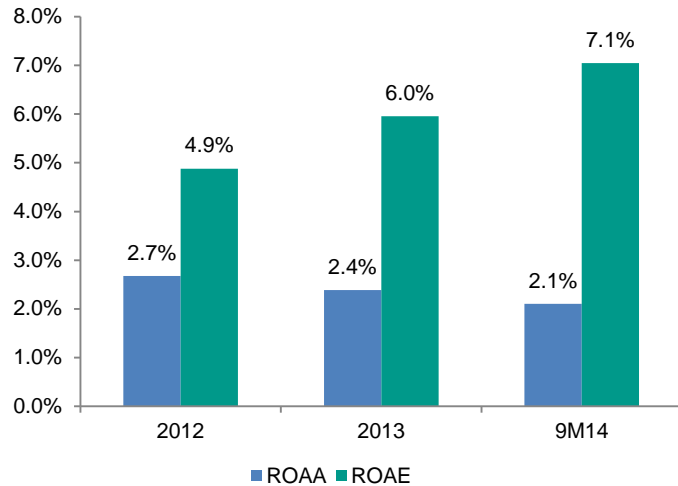
Source(s): Company, ABCI Securities

## Expansion of balance sheet

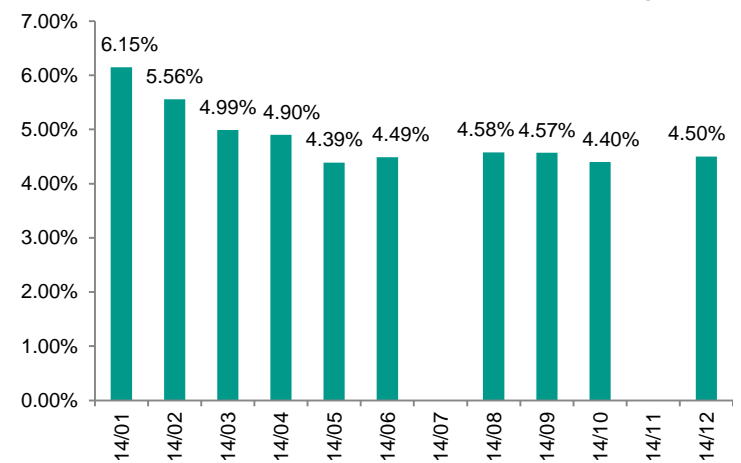
Under CSRC's support, financing channels and sources of fund are diversifying with the issuance of corporate bonds, subordinated bonds, and short-term financing bills. Coupon rate for CITIC's short-term financing bills have been falling gradually in 2014. With a stable lending rate in capital-based businesses, the Group's net interest margin could be enhanced.

Under the potential relaxation of capital rules, if the net assets-to-liabilities ratio is lowered to 10%, the maximum leverage will be increased from 6x to 11x. CITIC's ROAE in 9M14 increased by 2.81ppts to 7.05% on the higher balance sheet leverage. We expect the industry leverage to rise upon relaxation in regulatory requirements, thus improving the industry ROE in the long run.

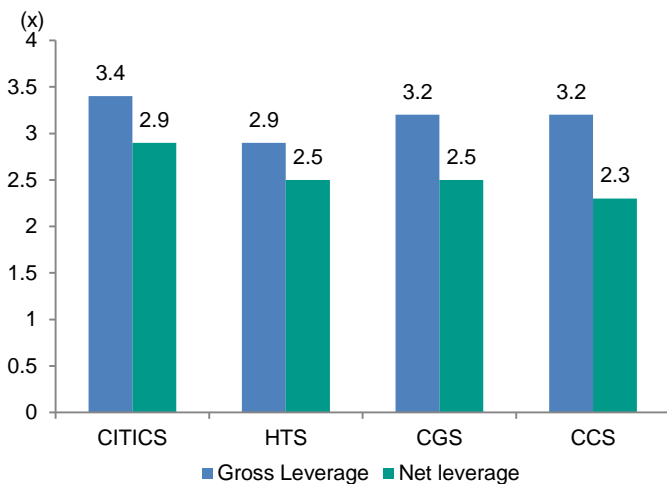
CITICS announced a placement plan on Dec 2014 to issue no more than 1.5bn shares for HK\$ 35-40bn. According to CITICS, 70% of the placement proceeds will be used for developing flow-based businesses, such as margin financing and equity derivatives products; 20% will be invested in its cross-border business platform; the remainder will be used to replenish working capital. ROE in 2015 would fall on the dilution impact from the share placement. Nonetheless, we expect CITIC's ROAE to reach double digits in medium term

**Exhibit 52: CITICS's ROAA and ROAE**


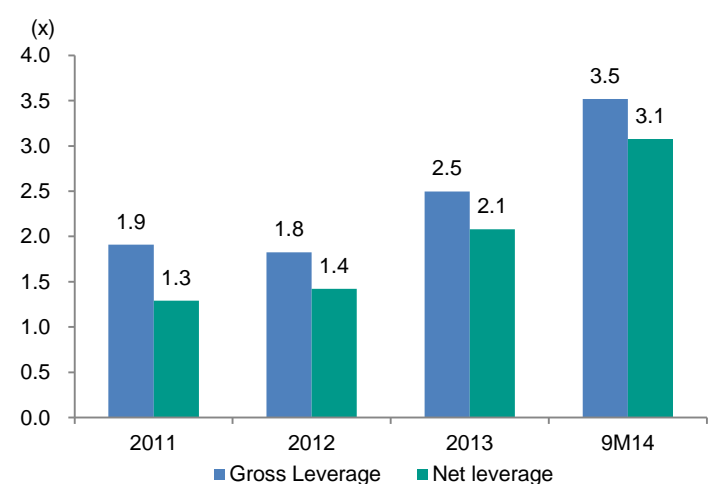
Source(s): Company, ABCI Securities

**Exhibit 53: Coupon rate of CITICS's short-term financing bills**


Source(s): Company, ABCI Securities

**Exhibit 54: Leverage ratios as at June 30, 2014**


Note: Net leverage = Average assets (excl. clients' deposits) / Average equity  
 Gross leverage = Average assets / Average equity  
 Source(s): Company, ABCI Securities

**Exhibit 55: CITICS's gross and net leverage ratios**


Note: Net leverage = Average assets (excl. clients' deposits) / Average equity  
 Gross leverage = Average assets / Average equity  
 Source(s): Company, ABCI Securities



### Valuation

As a leading full-service investment bank in China, CITICS is well-positioned to benefit from the accelerated internationalization and liberalization of China's capital markets. We expect growth in its brokerage, capital-based intermediary and investment banking businesses, and increased balance sheet leverage will be supportive to future earnings. Key concerns remain on the slower-than-expected growth in China's economy, intensifying commission price war, and failure to expand financing channels.

We derive CITICS's fair value with a P/B of 2.4x by applying the three-stage dividend discount model (DDM). Our derived TP of HK\$32.40 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

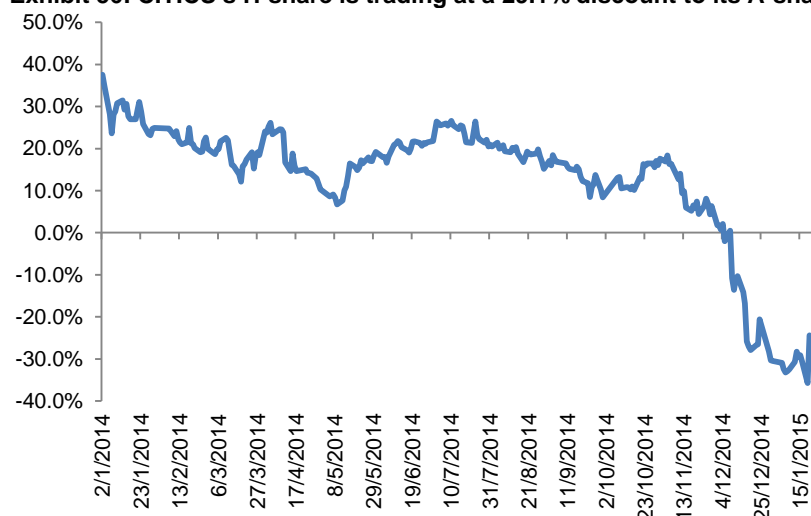
According to the Bloomberg consensus, A-share brokerage sector on average is trading at 3.5x 2015E P/B; the H-share brokers, including CITICS, HTS(6837 HK), CGS (6881 HK), and CCS (1375 HK), are trading at a weighted average of 2.0x 2015E P/B. The higher valuation in the A-share market may reflect different investor structure between A-share and H-share market. A-share market is retail investors oriented while H-share market is institutional investors oriented.

CITICS is currently trading at 2.1x 2015E P/B, while the ratios for HTS, CGS and CCS are at 1.8x, 1.7x and 2.5x, respectively. We believe the counter deserves a premium valuation as it is a full-service provider with a leading position in brokerage, underwriting business, and capital-based intermediary businesses. Its solid business model with a diversified revenue mix also reduces its reliance on traditional fee-based business.

### A/H valuation

CITICS's H-share is trading at a 29.1% 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 56: CITICS's H-share is trading at a 29.1% discount to its A-share



Source(s): Bloomberg, ABCI Securities estimates

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

FY Ended Dec 31 (RMB mn)	2012A	2013A	2014E	2015E	2016E
Fee and commission income	7,090	10,699	17,196	21,778	27,177
Interest income	2,172	4,090	7,273	11,510	15,079
Investment income	3,648	5,259	8,005	9,804	11,085
Other income	161	231	356	413	477
<b>Revenue</b>	<b>13,071</b>	<b>20,279</b>	<b>32,829</b>	<b>43,504</b>	<b>53,818</b>
Operating costs	(8,016)	(13,644)	(21,029)	(28,860)	(36,533)
<b>Operating Profits</b>	<b>5,055</b>	<b>6,635</b>	<b>11,801</b>	<b>14,644</b>	<b>17,285</b>
Associates & JCEs	432	211	249	294	347
<b>Profit before tax</b>	<b>5,487</b>	<b>6,846</b>	<b>12,049</b>	<b>14,937</b>	<b>17,632</b>
Tax	(1,180)	(1,538)	(2,707)	(3,356)	(3,961)
<b>Profit after tax</b>	<b>4,307</b>	<b>5,308</b>	<b>9,342</b>	<b>11,582</b>	<b>13,671</b>
Minority interests	(69)	(64)	(289)	(317)	(349)
<b>Net profits</b>	<b>4,237</b>	<b>5,244</b>	<b>9,054</b>	<b>11,264</b>	<b>13,322</b>

**Growth (%)**

Fee and commission income	(27.0)	50.9	60.7	26.6	24.8
Interest income	5.6	88.3	77.8	58.3	31.0
Investment income	(74.7)	44.2	52.2	22.5	13.1
Other income	(22.7)	43.0	54.2	16.1	15.6
Total Revenue	(50.4)	55.1	61.9	32.5	23.7
Total Operating costs	(31.8)	70.2	54.1	37.2	26.6
Operating profit	(65.4)	31.3	77.9	24.1	18.0
Net profit	(66.3)	23.8	72.7	24.4	18.3

**Operating performance (%)**

Operating margin (%)	38.7	32.7	35.9	33.7	32.1
Net margin (%)	32.4	25.9	27.6	25.9	24.8
Effective tax rate (%)	21.5	22.5	22.5	22.5	22.5
Dividend payout (%)	78.0	31.5	30.0	30.0	30.0
ROAE (%)	4.9	6.0	9.9	9.8	9.4
ROAA (%)	2.7	2.4	2.8	2.7	2.7

**Segmental revenue (RMB mn)**

Investment bank	2,755	2,224	3,672	4,223	4,890
Brokerage	4,574	7,642	10,819	12,976	14,387
Asset management	328	1,686	3,157	4,230	6,269
Trading	4,238	7,353	13,580	20,247	26,134
Other income	1,176	1,374	1,601	1,829	2,137

Source(s): Company, ABCI Securities estimates



**Consolidated balance sheet (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>
Fixed assets	3,712	4,070	4,051	4,417	4,815
Goodwill	501	10,047	10,550	11,394	12,305
Other intangible assets	161	1,916	2,012	2,112	2,218
Investment assets	12,258	13,009	13,570	14,328	15,283
Other non-current assets	11,706	6,841	7,551	8,259	9,009
<b>Total non-current assets</b>	<b>28,338</b>	<b>35,884</b>	<b>37,734</b>	<b>40,509</b>	<b>43,630</b>
Cash & equivalents	25,836	27,685	29,623	31,696	33,915
Cash held for clients	33,852	40,125	46,144	51,681	55,816
Investment assets	64,850	99,085	133,453	158,292	187,387
Loans to margin clients	9,423	34,302	99,476	124,345	142,996
Other current assets	6,209	34,274	46,065	57,806	68,590
<b>Total current assets</b>	<b>140,170</b>	<b>235,470</b>	<b>354,760</b>	<b>423,820</b>	<b>488,704</b>
<b>Total assets</b>	<b>168,508</b>	<b>271,354</b>	<b>392,494</b>	<b>464,329</b>	<b>532,335</b>
Accounts payable	34,807	45,196	51,976	56,134	59,502
Repo and other short-term borrowings	25,734	62,939	93,399	129,572	167,356
Other current liabilities	19,193	44,572	107,880	78,162	70,832
<b>Total current liabilities</b>	<b>79,735</b>	<b>152,708</b>	<b>253,255</b>	<b>263,867</b>	<b>297,690</b>
Bond payables	1,500	26,177	39,266	56,935	79,709
Other non-current liabilities	588	3,067	3,723	4,553	5,578
<b>Total non-current liabilities</b>	<b>2,088</b>	<b>29,245</b>	<b>42,989</b>	<b>61,489</b>	<b>85,287</b>
<b>Total liabilities</b>	<b>81,823</b>	<b>181,952</b>	<b>296,243</b>	<b>325,356</b>	<b>382,977</b>
Equity attributable to owners of the parent	86,465	87,688	94,363	136,248	146,429
Minority interest	219	1,714	1,887	2,725	2,929
<b>Total equity</b>	<b>86,684</b>	<b>89,402</b>	<b>96,251</b>	<b>138,973</b>	<b>149,358</b>
<b>Balance sheet structure</b>					
Investment assets	45.8%	41.3%	37.5%	37.2%	38.1%
Cash & equivalents	15.3%	10.2%	7.5%	6.8%	6.4%
Cash held for clients	20.1%	14.8%	11.8%	11.1%	10.5%
Loans to margin clients	5.6%	12.6%	25.3%	26.8%	26.9%
Other assets	13.2%	21.1%	17.9%	18.1%	18.2%
<b>Total assets</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>
Accounts payable	42.5%	24.8%	17.6%	17.3%	15.5%
Repo and other short-term borrowings	31.5%	34.6%	31.5%	39.8%	43.7%
Other liabilities	26.0%	40.6%	50.9%	42.9%	40.8%
<b>Total liabilities</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

Source(s): Company, ABCI Securities estimates





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%

Analyst : Pandora Leung  
Tel: (852) 2147 8809  
Email: pandoraleung@abci.com.hk

**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

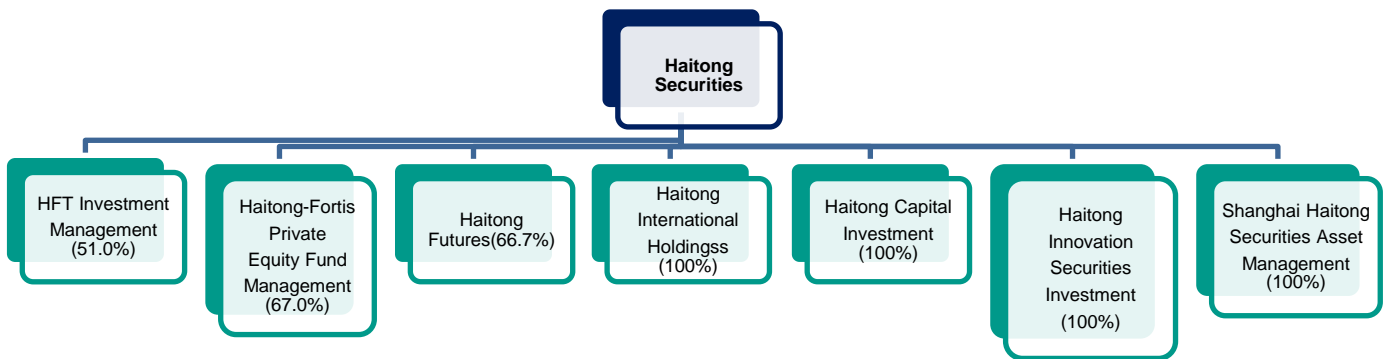


### Company Profile

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.

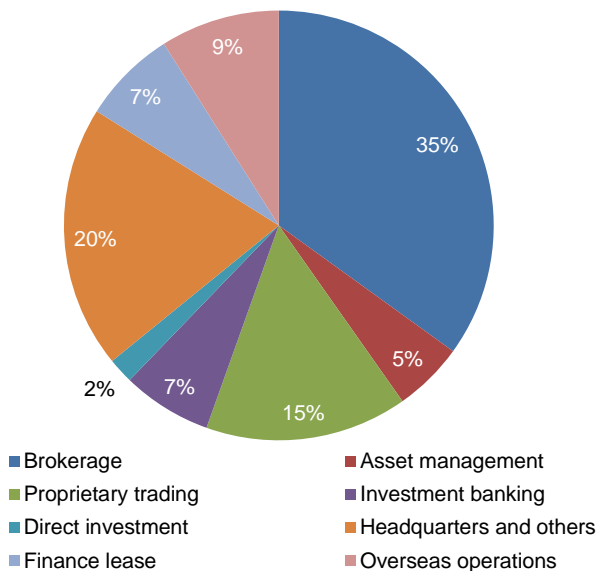
Principal subsidiaries of HTS included HFT Investment Management, Haitong-Fortis Private Equity Fund Management, Haitong Futures, Haitong Int'l Holdings, Haitong Capital Investment, Haitong Innovation Securities Investment, and Shanghai Haitong Securities Asset Management.

Exhibit 57: HTS's investment in subsidiaries



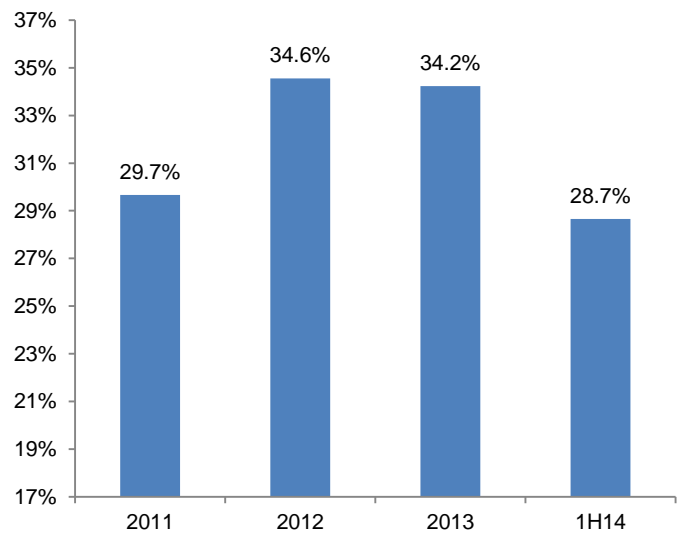
Source(s): Company, ABCI Securities

Exhibit 58: HTS's revenue mix for 1H14

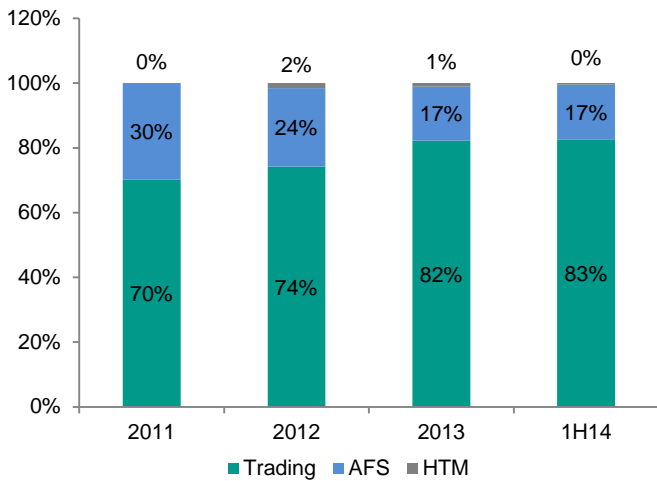


Source(s): Company, ABCI Securities

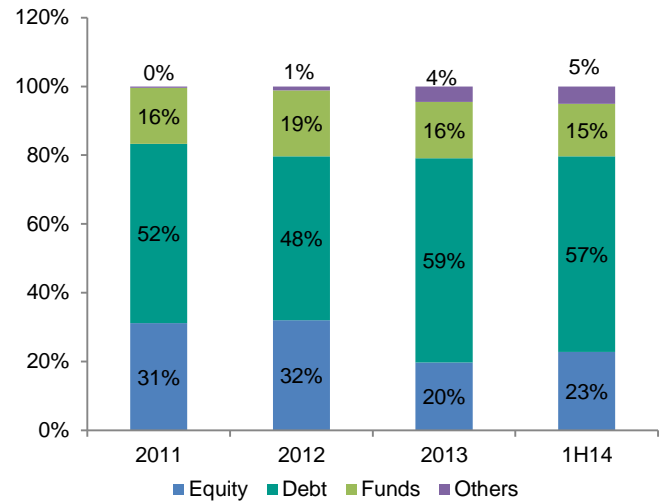
Exhibit 59: HTS's investment assets as a percentage of total assets



Source(s): Company, ABCI Securities

**Exhibit 60: Investment assets mix by accounting category**


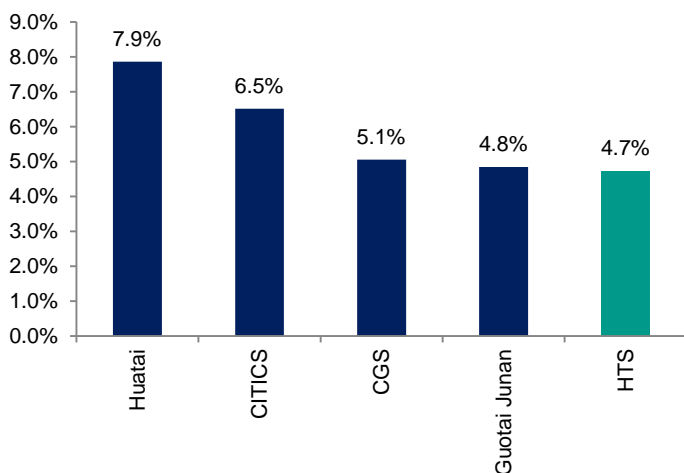
Source(s): Company, ABCI Securities

**Exhibit 61: Investment assets mix by securities category**


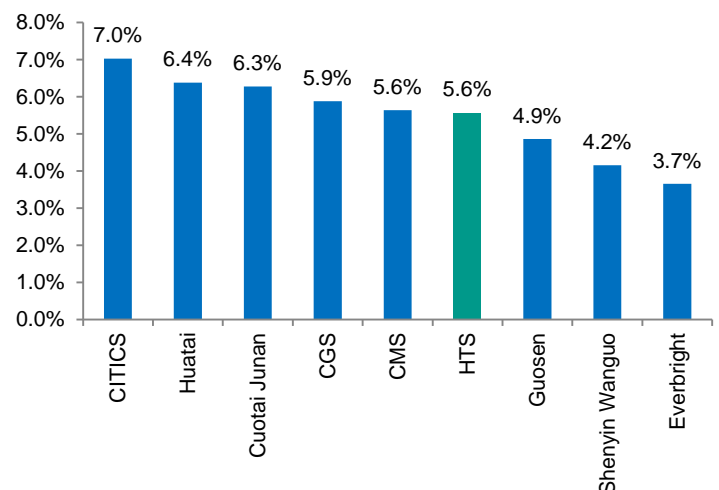
Source(s): Company, ABCI Securities

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


Source(s): Wind, ABCI Securities

**Exhibit 63: 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 64: 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 65: 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 66: 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

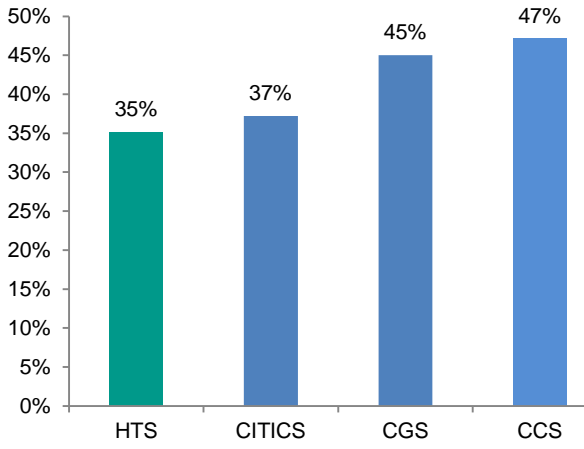
On Dec 4, 2014, HTS announced its wholly-owned subsidiary, Haitong Int'l Holdings, is under discussion with Novo Banco on an acquisition of a 100% stake in the latter's investment banking arm, BESI, at US\$ 467mn. HTS has not entered any formal agreement regarding the acquisition and the deal is currently 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.

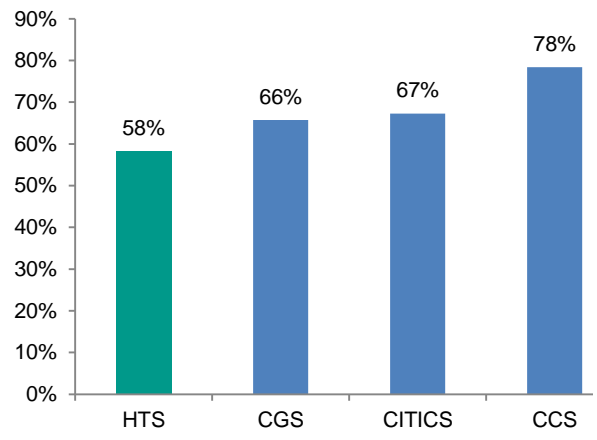


Exhibit 67: Staff cost-to-total expenses comparison (2013)



Sources: Company, ABCI Securities

Exhibit 68: 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%.

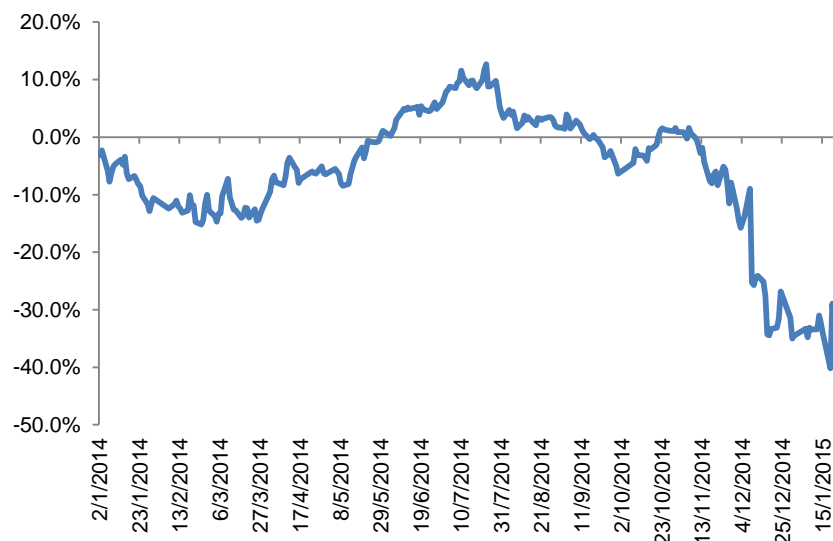
### Relative valuation

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 69: 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)**

<b>FY Ended Dec 31 (RMB mn)</b>	<b>2012A</b>	<b>2013A</b>	<b>2014E</b>	<b>2015E</b>	<b>2016E</b>
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 estimates



Jan 27, 2015  
Company Report  
Rating: BUY  
TP: HK\$ 9.10

Share price (HK\$) 7.06  
Est. share price return 28.9%  
Est. dividend yield 2.4%  
Est. total return 31.3%

Analyst : Pandora Leung  
Tel: (852) 2147 8809  
Email: pandoraleung@abci.com.hk

**Key Data**

52Wk H/L(HK\$)	9.33/2.13
Issued shares (mn)	2,631.6
Market cap	18,579
3-mth avg daily turnover (HK\$ mn)	91
Major shareholder(s) (%): Henan Investment Group	33.1
Source(s): Company, Bloomberg, ABCI Securities	

**1H14 Revenue breakdown (%)**

Brokerage	39
Trading	22
MFSL	18
Investment Banking	6
Others	15
Source(s): Company, ABCI Securities	

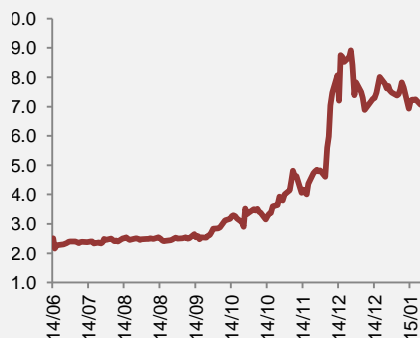
**Share performance (%)**

	Absolute	Relative*
1-mth	2.47	-3.95
3-mth	115.90	103.86
6-mth	182.40	176.94

\*Relative to HSI

Source(s): Bloomberg, ABCI Securities

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



Source(s): Bloomberg, ABCI Securities

## Central China Securities

### Regional leader in securities industry

- The only securities firm registered and headquartered in Henan province. Henan's 2013 GDP amounted to RMB 3.2tn and was ranked 5<sup>th</sup> nationally. The Group enjoys a strong local advantage and brand recognition in Henan
- It has the highest number of securities branches (26.1% of total securities branches in Henan) and was ranked 1<sup>st</sup> by trading volume of stocks and funds in the province
- Initiate coverage on CCS with **BUY**; our DDM-derived TP of HK\$ 9.1 implies 2.7x 2015E P/B

**Henan securities industry has a strong growth potential.** Located in central China, Henan has the highest GDP among 18 central and western provinces. It was ranked 5<sup>th</sup> nationally in terms of the provincial nominal GDP in 2013. As of Dec 31, 2013, the securitization ratio (total market capitalization of listed companies divided by nominal GDP) in Henan was 13.7%, far below the national average of 42.1%, revealing the province's strong potential in securities industry development.

**Leveraging on the "Henan Advantage".** As of Dec 31, 2013, CCS had 49 securities branches in Henan, representing 26.1% of all securities branches in the province. Its brokerage trading volume of stocks and funds was ranked 1<sup>st</sup> in Henan, accounting for 24.1% of total in 2013. CCS was also ranked 1<sup>st</sup> in the province by the amount of equity financing underwritten in 2012 and 2013. Aggregate proceeds of secondary offerings underwritten by CCS in 2012 and 2013 were RMB 11.6bn, representing ~ 46.5% of Henan's total equity financing.

**Extensive branch network and customer base.** CCS has the largest number of branches in Henan. As of Dec 31, 2013, it had 62 securities branches and 5 futures branches; among which, a total of 49 securities branches and 3 futures branches were located in Henan with a total client base of 1.34mn. We expect the Group's extensive branch network in Henan to support the development of brokerage business .

**Margin financing & securities lending (MFSL) business grew rapidly.** In 2012, 2013 and 1H14, CCS's revenues from MFSL business were RMB 6.1m, RMB 155.8mn and RMB 145.4mn; contribution the Group's total revenue increased from 10.9% in 2013 to 18.2% in 1H14. Given the deregulation in the financial industry, capital-based intermediary business is expected to become one of the future earnings drivers.

**Initiate coverage on CCS with BUY rating.** CCS would benefit from Henan's accelerating economic transformation and growth in the region. Apart from its primary businesses in brokerage and investment banking, capital-based intermediary business is expected to become a key revenue driver in the future. We initiate our coverage with a **BUY** rating. Our DDM-derived TP is HK\$ 9.10, implying 2.7x 2015E P/B.

**Risk factors:** 1) Weaker-than-expected A-share market; 2) Slowdown in Henan's economic growth; 3) Intensifying competition in commission rate; 4) Slower growth on capital intensive businesses.

**Financial Summary**

FY ended Dec 31	2012A	2013A	2014E	2015E	2016E
Revenue (RMB mn)	1,218	1,435	2,231	3,184	4,007
Chg (% YoY)	26.1	17.7	55.5	42.7	25.8
Net profit (RMB mn)	183	223	488	702	838
Chg (% YoY)	97.1	22.3	118.4	43.8	19.4
EPS (RMB)	0.09	0.11	0.21	0.27	0.32
Chg (% YoY)	97.1	22.3	90.4	27.5	19.4
BVPS (RMB)	1.88	2.01	2.39	2.61	2.86
Chg (% YoY)	5.7	6.9	18.6	9.2	9.8
P/E (x)	62.9	51.4	27.0	21.2	17.7
P/B (x)	3.0	2.8	2.4	2.2	2.0
ROAE (%)	4.9	5.6	9.3	10.5	11.5
ROAA (%)	1.6	1.8	2.8	3.1	3.2
DPS(RMB)	-	-	0.09	0.13	0.16
Yield (%)	-	-	1.6	2.4	2.8

Source(s): Bloomberg, ABCI Securities estimates

## Company Profile

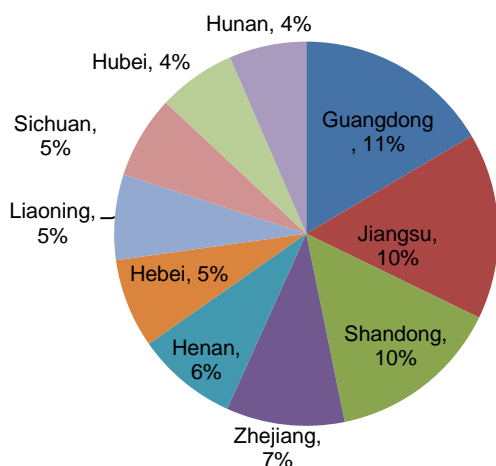
Central China Securities (CCS) is the leading securities firm in Henan with a full-service business platform and strategic presence in China. The Group's business lines include brokerage, investment banking, investment management, proprietary trading and other innovative businesses. CCS's key strength include its leading position in the securities, brokerage, and investment banking businesses in Henan; extensive branch network and customer base in the region, and its emerging innovative businesses.

### Leverage on the "Henan Advantage"

CCS is the only securities firm registered and headquartered in Henan. The Group enjoyed strong local advantages and brand recognition in the province.

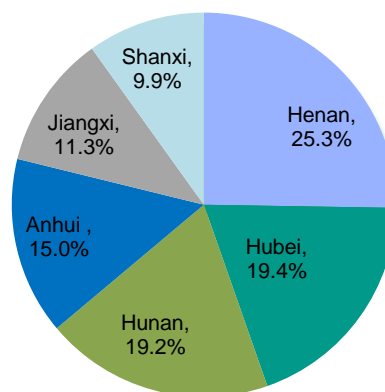
Henan, located in central China, has the highest GDP among the 18 central and western Chinese provinces, and was ranked 5<sup>th</sup> nationally in terms of provincial nominal GDP in 2013. Henan's 2013 nominal GDP amounted to RMB 3.2tn, accounting for 25.3% of the total among 6 provinces in central China.

**Exhibit 70: Nominal GDP contribution by top ten provinces in China for 2013**



Source(s): Company, NBS, ABCI Securities

**Exhibit 71: Nominal GDP contribution in Central China for 2013**



Source(s): Company, NBS, ABCI Securities

Henan is the central hub connecting eastern and western parts of China. At end-2013, Henan's population was ~106mn with an urbanization rate of 43.8%, 10ppt lower than the national average, indicating a robust potential for further urban development. The Henan government is accelerating its urbanization process and intends to increase the provincial urbanization rate to exceed 52.0% by 2017. In 2012, 6 high-growth industries in Henan, namely, electronics, equipment manufacturing, automobile, food processing, light industry and new materials, contributed to 57.9% of the total added-value from enterprises in the province.

Henan has experienced a rapid economic growth since the implementation of the "Rise of Central China Plan" in 2006. We expect Henan's economy would continue to benefit from the economic development policies, including the PRC national strategic plans and financial industry policies listed below (see Exhibit 72).



**Exhibit 72: PRC national strategies**

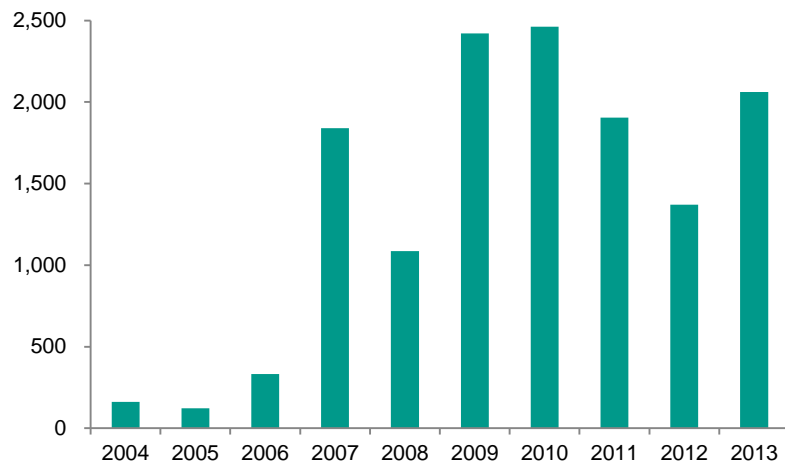
Strategic plan	Year
Zhengzhou Airport Economic Experimental Zone (鄭州航空港經濟綜合實驗區)	2013
Central Plains Economic Zone (中原經濟區)	2011
National Core Producing Area of Grains (國家糧食生產核心區)	2009

Source(s): Company, ABCI Securities

Apart from the National Strategic Plans, according to the “Opinions on further enhancing the financial work and accelerating the development of financial industry” issued by the Henan government ( “河南省人民政府關於進一步加強金融工作加快金融業發展的意見” ), the number of Henan-based publicly-listed companies would increase to over 150 by 2015. According to a government work report published by the 3<sup>rd</sup> session of the 12<sup>th</sup> Henan Provincial People’s Congress on Jan 16, 2014, Henan government plans to actively pursue (1) equity and debt financing in the private or public sector; (2) development of Regional OTC Board and local venture capital and private equity funds; (3) expansion of municipal bonds and SME private bonds; (4) trial development of perpetual debt; (5) accelerated reforms of local financial institutions.

Securities brokerage trading volume in Henan increased significantly in the past decade. According to Wind data, brokerage trading volume of stocks and funds increased from RMB 161.4bn in 2004 to RMB 2,060.8bn in 2013, representing a CAGR of 32.7%.

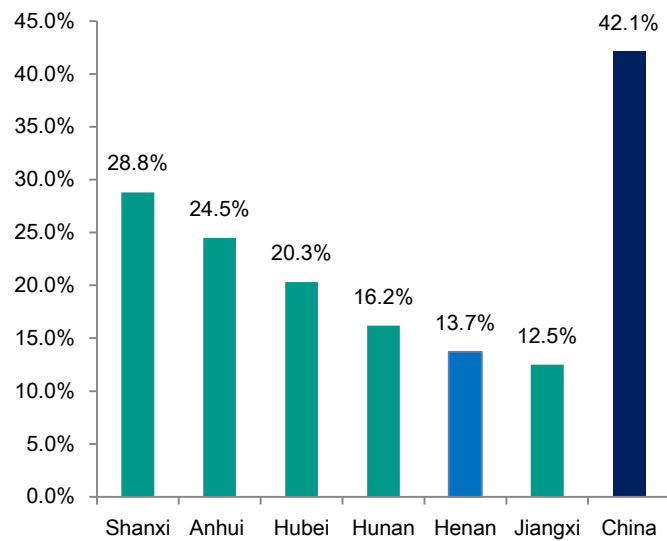
**Exhibit 73: Brokerage trading volume of stocks and funds in Henan (RMB bn)**



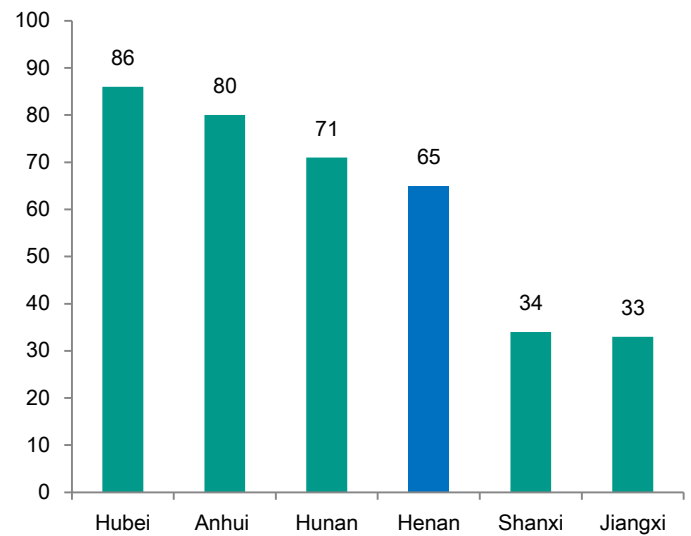
Source(s): Wind, ABCI Securities

The securities brokerage market in Henan has a relatively small scale. The brokerage trading volume of stocks and funds in Henan only accounted for 64.0% of Henan’s GDP in 2013, compared to the national average of 169.8% and was lower than the 5 remaining provinces in central China (ranging from 64.6% to 114.6%). In addition, the brokerage trading volume of stocks and funds per capita in Henan was RMB 21,894 in 2013, lower than the national average of RMB 70,970 and was the least among the 6 provinces in central China. Accelerating urbanization and increasing disposable income per capita are expected to drive up securities brokerage demand steadily, however.

As of Dec 31, 2013, Henan had 65 A-share listed companies, the 4<sup>th</sup> highest among the 6 provinces in central China and representing 2.6% of all listed companies in China. As of Dec 31, 2013, the securitization ratio (total market capitalization of listed companies divided by nominal GDP) in Henan was 13.7%, lower than the national average of 42.1%. Henan government authorities intend to facilitate corporate financing by qualified corporations through IPOs, secondary offerings and bond offerings. It also aims to establish a Regional OTC Board to promote a multi-tiered capital market system. With the support of favorable economic policies, we believe Henan's securitization ratio will further increase, providing new market opportunities for local securities firms.

**Exhibit 74: Securitization ratio among the six provinces in Central China as of Dec 31, 2013**


Source(s): Wind, ABCI Securities

**Exhibit 75: Number of domestically listed companies as of Dec 31, 2013**


Source(s): Wind, ABCI Securities

## Leading position in Henan's securities market

**Exhibit 76: Market ranking of CCS in Henan**

Criteria	Ranking or market share in Henan Province
Brokerage trading volume of stocks and funds	No.1 (2011-2013)
Revenue from securities branches	No.1 in 2013 with 28.9% market share
Balance of margin loans and securities lent	No.1 as at 31/12/2013 with 24.2% market share
Amount of equity financing underwritten	No.1 in 2012 and 2013
Amount of debt financing underwritten	No.2 in 2013; No.1 in 2012
No. of private companies recommended for share quotation and transfer on the NEEQ*	No.9 in 2013; No.1 in 2012

\*National Equities Exchange and Quotation, (also known as the "New Third Board")  
 Source(s): Company, ABCI Securities

CCS is a regional play in China's securities industry. Its strong business positioning in Henan differentiates itself from other large players in Henan.

According to SAC, in 2013, CCS was ranked 44<sup>th</sup> and 51<sup>st</sup> among all 115 PRC securities firms by total assets and net assets. In 2013, its revenue and net profit were ranked 40<sup>th</sup> and 43<sup>rd</sup> among PRC securities firms, representing 0.68% and 0.60% of the market share in China.

At end-2013, there were 52 securities firms with business presences in Henan. The top 10 securities firms commanded 83.1% of market share, as measured by revenue generated by securities branches in the province. In 2013, CCS had the highest local



market share of 28.9%. We believe the Group's relatively larger branch network in Henan differentiates itself from larger, national counterparts. CCS's provincial market share was higher than many reputable national players such as Guotai Junan, Galaxy, and Haitong in 2013.

**Exhibit 77: The top ten securities firms with business presences in Henan in 2013**

Ranking	Firm	Market share* (%)
1	Central China Securities	28.9
2	Minsheng Securities Co., Ltd.	15.3
3	Donghai Securities Co., Ltd.	8.9
4	Guotai Junan Securities Co., Ltd.	7.0
5	New Times Securities Co., Ltd.	5.4
	<b>Top 5</b>	<b>65.5</b>
6	China Investment Securities Co., Ltd.	5.0
7	China Galaxy Securities Co., Ltd.	4.9
8	Haitong Securities Co., Ltd.	3.6
9	Founder Securities Co., Ltd.	2.1
10	Zhong Cheng Securities Brokerage Co., Ltd.	2.0
	<b>Top 10</b>	<b>83.1</b>

\* Market share is calculated based revenue generated by securities branches in Henan  
Source(s): The Securities and Futures Association of Henan, ABCI Securities

**Extensive branch network and customer base in Henan**

The securities market in Henan is highly centralized and concentrated in Zhengzhou, the capital city of Henan. As of Dec 31, 2013, there were 77 securities branches in Zhengzhou, accounting for ~43.8% of total branches in Henan. The Group has the largest number of branches in Henan. As of Dec 31, 2013, CCS had 46 securities branches in Henan, representing 26.1% of total in the province.

About 92.0%, 91.3% and 89.3% of the Group's revenue and other income from securities brokerage business in 2011-13 were originated from Henan, respectively. The Group strategically located its branch network across major cities in China such as Beijing, Shanghai and Shenzhen. As of Dec 31, 2013, it had 62 securities branches and 5 futures branches. CCS had over 1.34mn securities brokerage clients and over 10,800 futures brokerage clients. In terms of customer loyalty, about 67.9% CCS's clients have retained a relationship with the Group for over 5 years. The Group's extensive branch networks in Henan will benefit from the development of regional brokerage business.

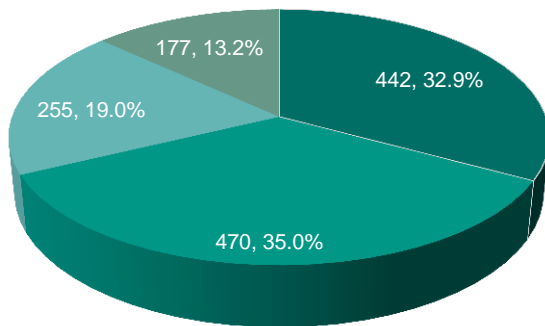


Exhibit 78: CCS's branch network in China as of Dec 31, 2013



Source(s): Company, ABCI Securities

Exhibit 79: Customers' account-holding period in 2013 (Thousand clients, %)



- ≥10 years
- <10 years and ≥ 5 years
- < 5 years and ≥ 3 years
- < 3 years

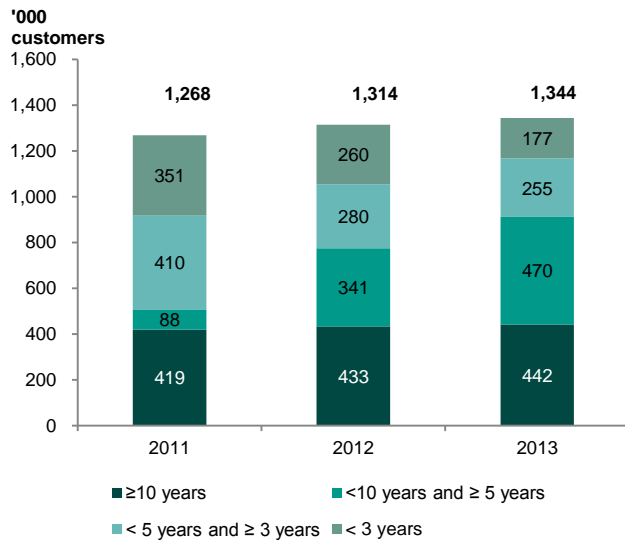
Source(s): Company, ABCI Securities

Exhibit 80: CCS's client mix

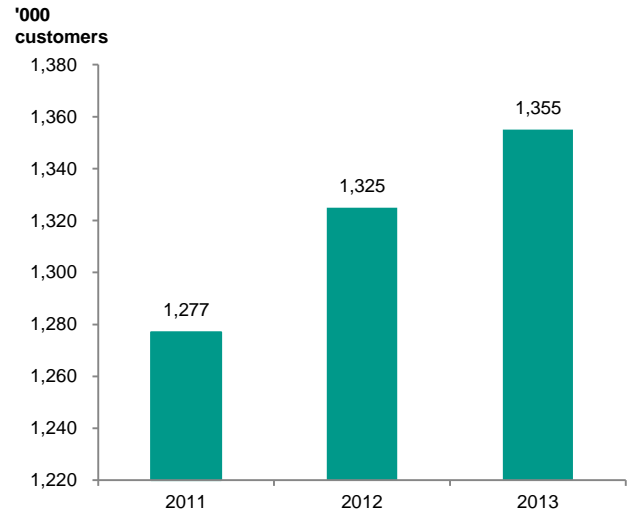
(As of Dec. 31)

(In thousand)	2013	2012	2011
<b>Securities brokerage clients</b>			
-Retail clients	1,343	1,314	1,268
-Institutional clients	1	1	1
<b>Total securities brokerage clients</b>	<b>1,344</b>	<b>1,315</b>	<b>1,269</b>
-Futures brokerage clients	11	10	8
<b>Total clients</b>	<b>1,355</b>	<b>1,325</b>	<b>1,277</b>
<b>Of which:</b>			
% Clients based in Henan	94.8%	95.2%	95.5%

Source(s): Company, ABCI Securities

**Exhibit 81: Customers' account-holding period**


Source(s): Company, ABCI Securities

**Exhibit 82: CCS's client base growth**


Source(s): Company, ABCI Securities

## Brokerage business continues to be a key driver

Contribution of CCS's segment revenue and other income from securities brokerage business to total revenue decreased from 73.1% in 2011 to 47.3% in 2013 and 36.1% in 1H14. Due to the intense competition, average securities brokerage commission rates have decreased in recent years though the decline has slowed since 2012. With the rise of online discount brokerage providers, however, the competition may rise again and drive down commission rate. In response, securities firms strive to provide more value-added services to mitigate the impacts of decreasing rate. The Group's MFSL business has grown rapidly since its inception, which helps stabilize brokerage commission rates and increase brokerage trading volume. We believe that the business would continue to be a key driver of revenue and profit growth for CCS.

## Brokerage commission rate under pressure

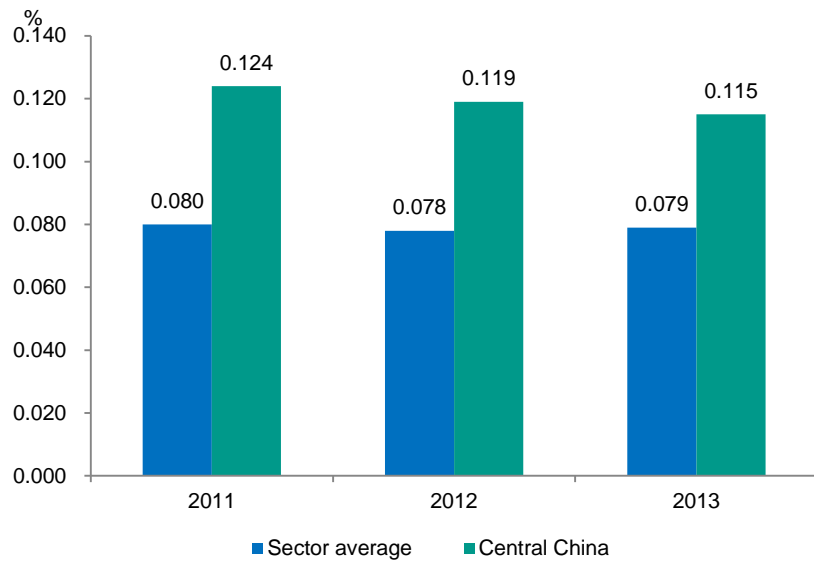
Henan's brokerage sector is relatively fragmented. There are a total of 52 securities brokerage firms with business presences in the province as of 2013. Intense price competition in recent years has led to lower commission rates in CCS's securities brokerage business. Overall, the sector's average commission rate declined from 0.095% in 2010 to 0.079% in 2013.

Sinolink Securities and Tencent jointly introduced Yong Jin Bao, an internet-based financial product that provides online brokerage, brokerage fund management, and investment advisory services, in Feb 2014. The product offers a flat commission rate of 2bps (vs. current sector average of 7.9bps); hence, the sector's commission rate will be pressured in the medium term. CCS's average securities brokerage commission rates were 0.124%, 0.119% and 0.115% in 2011-13, respectively, higher than the sector average during the period.





Exhibit 83: Brokerage commission rate (%)



Source(s): Wind, ABCI Securities

We expect the emergence of online discount brokerage firms, which offer lower commission rates than the conventional brokers, would drive down commission rate in the medium term. In our view, securities firms would continue to accelerate development in innovative business and seek for more product differentiation. To mitigate the adverse impacts, CCS also plans to implement several strategies as follows:

1. Diversify revenue sources and improve average securities brokerage commission rates by developing value-added wealth management business;
2. Provide comprehensive investment and financing services by transiting traditional brokerage branches to comprehensive securities and financial services platforms;
3. Increase cross-selling among different business lines and attract more high-end individual customers

**Accelerating the transition of brokerage business**

As of Mar 31, 2014, CCS has completed the transition of 36 key securities branches to comprehensive securities and financial services platforms that provide integrated brokerage, investment banking and investment management services.

CCS also seeks to enhance operational efficiency and cost reduction opportunities. The Group started to establish "light branches", which are small-sized branches of less than 200sq.m with fewer on-site staff, in. These light branches enable CCS to expand network coverage and capture local markets in locations outside Henan more swiftly at lower costs.

In addition, CCS encourages the use of alternative trading platform that integrates middle and back office functions. In 2013, 83% of CCS's securities brokerages were completed through their online platform. In early 2014, CCS launched the electronic securities platform, which enables the Group to expand customer reach and reduce operating costs. Going forward, we expect CCS to improve this online platform by enhancing customer experience and offering more diverse wealth management products.

CCS's also plans to develop more high-net-worth clients. According to the 2013 Hurun Wealth Report, there were 18,700 high-net-worth individuals in Henan as of Dec 31, 2012. CCS's also plans to develop more high-net-worth clients.by enhancing the



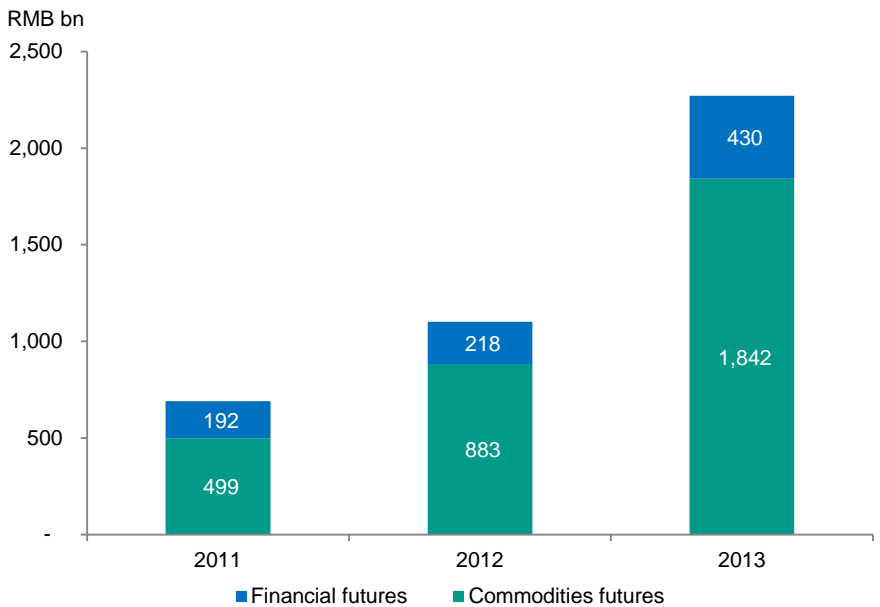
company's wealth management functions in branches, as well as utilizing the cross-selling synergy from its investment bank division and asset management division.

### Futures brokerage

CCS provides futures brokerage services through its subsidiary, Central China Futures, which is a member of the Shanghai Futures Exchange, the Zhengzhou Commodity Exchange, the Dalian Commodity Exchange and the China Financial Futures Exchange. As of Dec 31, 2013, CCS offers all of the futures products available in China, including 38 commodity futures (such as agricultural products, bullion, chemical products and metals etc.) and 2 financial futures, namely (i.e. stock index futures and treasury-bond futures).

As of Dec 31, 2013, CCS had 10,800 futures customers, representing a 17.3% CAGR over 2011-13. Futures brokerage revenue grew 31.8% CAGR over the same period. As we expect regulators to include more futures types in the future, we expect increasing contribution from this segment to contribute to 5-6% of total revenue in 2015E-16E.

Exhibit 84: CCS's futures mix



Source(s): Company, ABCI Securities

According to CCS, the Group's total brokerage trading volume of stocks and funds was ranked 1<sup>st</sup> in Henan from 2011-2013, accounting for ~ 24.6%, 24.3% and 24.1% of total in Henan in 2011-13, respectively.

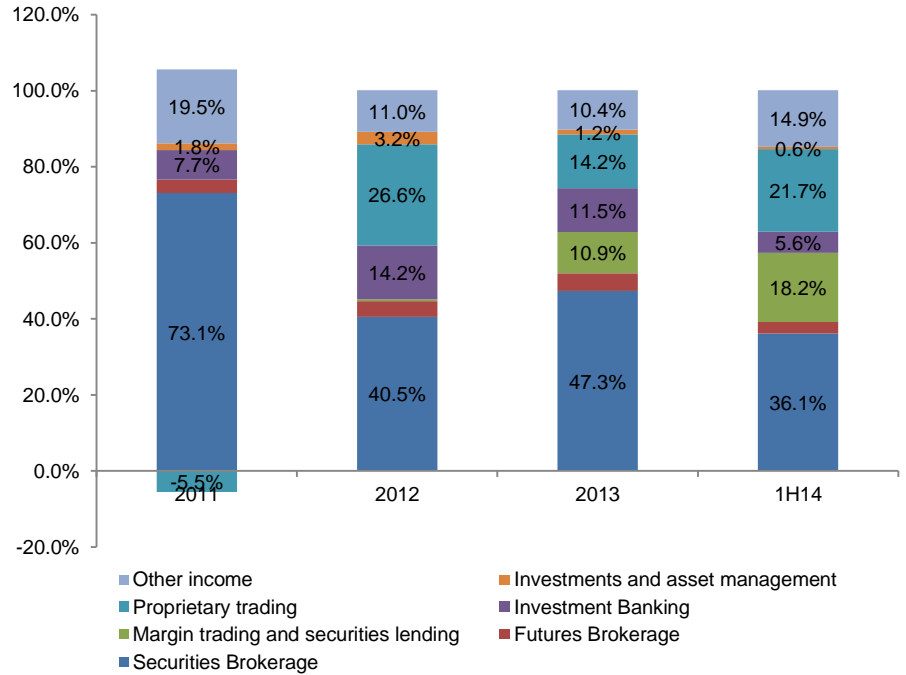
### New earnings driver from innovative businesses

The Group is actively developing various types of capital-based intermediary businesses, including MFSL, securities-backed lending, and securities repurchase. Balance of MFSL in China surged from RMB 38.2bn in 2011 to RMB 1,502.1bn in 2013, representing a CAGR growth of 199.4%. The Group obtained the qualification for the MFSL business from CSRC in June 2012 and launched the business subsequently in July 2012.



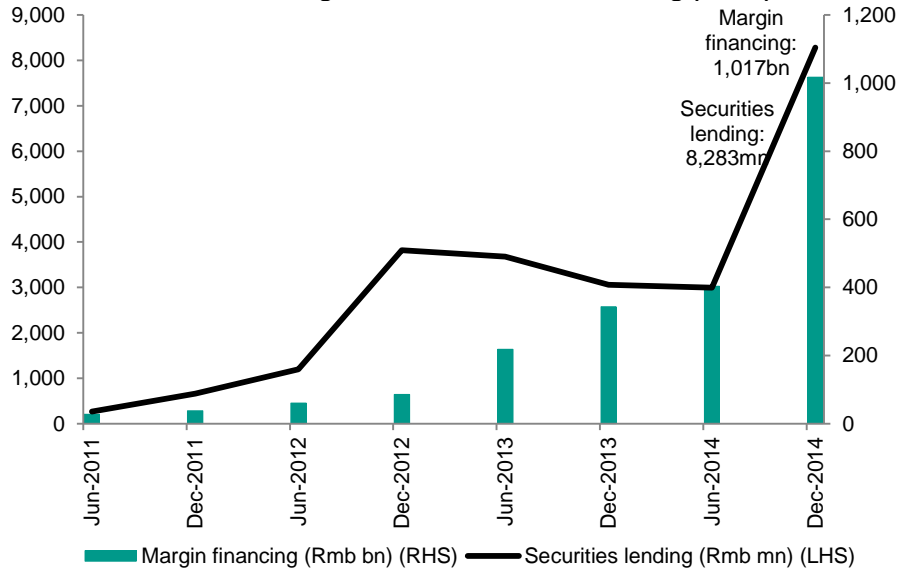
MFSL business has grown rapidly since its launch in July 2012, and the balance of the Group's margin loans and securities lending increased from RMB 2,267mn as of Dec 31, 2013 to RMB 7,407mn as of Dec 31, 2014, up 227% YoY. Separately, securities repurchase business and securities-backed lending business were launched in Oct 2012 and Aug 2013.

Exhibit 85: CCS's revenue mix



Source(s): Company, ABCI Securities

Exhibit 86: Balance of margin loans and securities lending (MFSL) in China

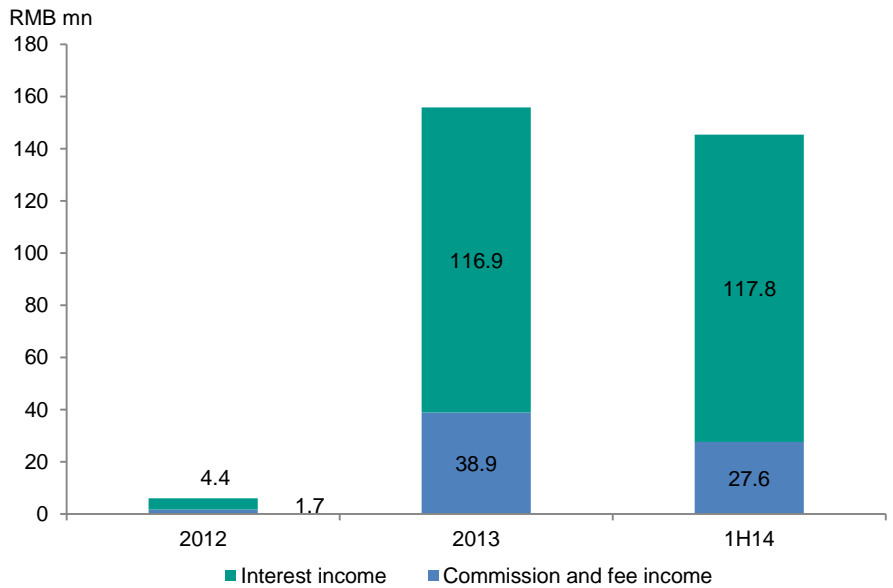


Source(s): Wind, ABCI Securities

Currently, the interest rates for CCS's margin financing and securities lending are 3.0% and 5.0% above the PBOC benchmark interest rate for 6-month loans. MFSL clients are allowed to provide securities quoted on the Shenzhen Stock Exchange (SZSE) and the Shanghai Stock Exchange (SSE) as collaterals.

MFSL business generates both interest income and brokerage commission income from customers' margin trade. In 2012, 2013 and 1H14, CCS's segment revenues from MFSL business were RMB 6.1mn, RMB 155.8mn and RMB 145.4mn, respectively.

**Exhibit 87: Income from CCS's margin financing and securities lending business (RMB mn)**



Source(s): Company, ABCI Securities

CCS was ranked 1<sup>st</sup> in Henan in MFSL balance as of Dec 31, 2013, representing ~24.2% of the local market share. Nationally, the Group's market share increased from 0.24% in 2012 to 0.65% and 0.72% in Dec 31, 2013 and 2014. Despite its strong growth, MFSL balance only accounted for 4.0% of tradable A-share market cap. Nonetheless, we believe strong growth in the brokerage business and extensive customer base will help CCS's to capture new business opportunities going forward.



Considering CCS's core strength in client base, we expect its market share in MFSL to increase to 0.75%-0.8% in 2015E. As of Dec 31, 2013, a total of 88,874 of CCS's customers were eligible for a margin account; only 12,607 customers, representing 0.93% of total customers or 14.18% of eligible individuals had a margin account with CCS. Thus, we believe the room for growth is ample in coming years. In 1H14, segment revenue and other income MFSL business was RMB 145.4mn, representing 18.2% of total revenue (2013: 10.9%). With the deregulation in the financial industry, we expect capital-based intermediary business to become one of the Group's earning drivers.

### **Innovative business**

**Securities-backed lending and stock repurchase:** In a stock repurchase transaction, investors obtain financing from brokers by transferring ownership of stock and agreeing to buy the shares back in the future (in no more than 1 year). Securities-backed lending was introduced in May 2013. For such lending, investors obtain funds from brokers by offering shares as collaterals to the stock exchange and agreeing to repay the amount in no more than 3 years. Compared with stock repurchase, securities-backed lending has longer tenors and allows the controlling shareholders to receive financing via their untradeable shares.

CCS launched its securities repurchase business in Oct 2012 and securities-backed lending business in Aug 2013. As of Dec 31, 2013, the balances of securities-backed lending and securities repurchase amounted to RMB 254.6mn and RMB 72.1mn. The interest rate charged for these services is generally comparable to that of the Group's margin financing service.

**Individual stock option:** An individual stock option refers to a standardized contract designed by the stock exchange in which a counterparty has the right to purchase, or sell, the underlying securities at a pre-determined price on a specified date. CCS is among the first batch of PRC securities firms involved in the pilot testing of individual stock options.

**NEEQ market-making:** NEEQ market-making refers to a service offered by a securities firm such that it continuously releases two-way quotations and transacts with investors in the NEEQ system. CCS can earn the bid-ask spread and commission fee rebates from such service to expand enhance its income source as well as investment banking capability.

**Interest-rate swap:** 2 counter-parties, usually based on a specified nominal amount, agree to exchange interest cash flows from a fixed rate to a floating rate (or vice versa) during a period to manage their interest risk exposure. The introduction of interest-rate swaps will diversify the Group's proprietary trading business and manage finance cost. Revenue will be mainly generated from interest-rate spreads and services fees.

CCS was qualified in May 2010 to provide recommendation services to help private companies enter into the NEEQ for share quotation and transfer. In 2012, CCS recommended 9 private companies for share quotation and transfer on the NEEQ, ranking first among all PRC securities firms. In 2011, financial advisory business ranked 1<sup>st</sup> among all PRC securities firms in terms of revenue growth.

Led by the Henan government, CCS also intends to assist in the establishment of the "Regional OTC Board" in the province that will enable local SMEs to obtain financing and transfer shares with greater flexibility.



## Valuation

In view of the improved market efficiency and accelerated internationalization of China's capital market, we expect the Group's future earnings will be supported by an increased balance sheet leverage as well as its businesses in brokerage, capital-based intermediary, and investment banking. Potential risks to the counter include downturn in A-share market, slowdown in China's economy, intensifying commission price war, and the group's failure to expand financing channels.

We value CCS with the three-stage dividend discount model (DDM), which we believe to be an appropriate and commonly used valuation method for brokerage firms. Besides, DDM can also reflect the high growth in near term driven by China's economic growth, further monetary easing, and CCS's leading position in Henan's securities industry supportive to future dividend payments. Our derived TP of HK\$ 9.10 is based on the 2015E BVPS. We assume a cost of equity at 14.0%, a long-term growth rate of 7.9% and a sustainable ROAE of 17.5%.

## 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 CCS, CITICS(6030 HK), CGS (6881 HK) and HTS (6837 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/H share markets. A-share market is retail investors-oriented, whereas H-share market is institutional investors-oriented.

CCS is currently trading at 2.5x 2015E P/B, higher than the 2.1x, 1.8x and 1.7x for CITICS, HTS and CGS, respectively. We believe the Group deserves a premium valuation based on its leading position in brokerage, margin financing, and investment banking businesses in Henan province. Transforming into a full-service provider, the Group will continue to strengthen its regional advantage in brokerage and investment banking business while expanding its capital-based intermediary businesses. Positive on its business prospects, we initiate our coverage with a **BUY** rating.



**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	737	953	1,461	2,119	2,653
Interest income	143	287	440	642	847
Investment income	321	159	280	367	438
Other income	17	36	50	57	69
<b>Total Revenue</b>	<b>1,218</b>	<b>1,435</b>	<b>2,231</b>	<b>3,184</b>	<b>4,007</b>
Operating costs	(961)	(1,096)	(1,513)	(2,161)	(2,788)
<b>Operating Profits</b>	<b>257</b>	<b>338</b>	<b>718</b>	<b>1,024</b>	<b>1,218</b>
Associates & JCEs	0	0	0	0	0
<b>Profit before tax</b>	<b>257</b>	<b>338</b>	<b>718</b>	<b>1,024</b>	<b>1,218</b>
Tax	(74)	(100)	(216)	(307)	(365)
<b>Profit after tax</b>	<b>183</b>	<b>238</b>	<b>503</b>	<b>717</b>	<b>853</b>
Minority interests	(0)	(15)	(15)	(15)	(15)
<b>Net Profits</b>	<b>183</b>	<b>223</b>	<b>488</b>	<b>702</b>	<b>838</b>
<b>Growth (%)</b>					
Revenue	26.1	17.7	55.5	42.7	25.8
Operating EBITDA	15.9	14.0	38.0	42.8	29.0
Operating EBIT	87.6	31.6	112.4	42.5	19.0
Net profit	97.1	22.3	118.4	43.8	19.4
<b>Operating performance (%)</b>					
Operating margin (%)	21.1	23.6	32.2	32.1	30.4
Net margin (%)	15.0	15.6	21.9	22.0	20.9
Effective tax rate	28.7	29.5	30.0	30.0	30.0
Dividend payout (%)	0.0	0.0	50.0	50.0	50.0
ROAE (%)	4.9	5.6	9.3	10.5	11.5
ROAA (%)	1.6	1.8	2.8	3.1	3.2
<b>Segmental revenue (RMB mn)</b>					
Securities Brokerage	494	679	762	886	901
Futures Brokerage	50	67	107	132	160
Margin trading and securities lending	6	156	536	1,031	1,434
Investment Banking	173	165	291	425	617
Proprietary trading	324	204	321	393	470
Investments and asset management	39	17	43	80	94
Other income	132	147	171	238	331

Source(s): Company, ABCI Securities estimates



Consolidated balance sheet (2012A-2016E)

FY Ended Dec 31 (RMB mn)	2012A	2013A	2014E	2015E	2016E
Fixed assets	272	257	276	296	315
Goodwill	7	7	7	7	7
Other intangible assets	32	47	61	79	103
Investment securities	89	40	32	26	26
Other non-current assets	382	522	546	572	598
<b>Total non-current assets</b>	<b>783</b>	<b>873</b>	<b>922</b>	<b>979</b>	<b>1,049</b>
Cash & equivalents	998	570	1,281	704	402
Cash held for clients	4,370	3,963	4,280	4,708	5,179
Trading securities	3,400	3,439	4,196	4,830	5,371
Investment securities	83	391	450	472	496
Other current assets	1,570	4,312	9,547	12,627	15,720
<b>Total current assets</b>	<b>10,420</b>	<b>12,675</b>	<b>19,753</b>	<b>23,341</b>	<b>27,168</b>
<b>Total assets</b>	<b>11,203</b>	<b>13,548</b>	<b>20,675</b>	<b>24,320</b>	<b>28,217</b>
Accounts payable	5,209	4,994	5,219	4,958	4,710
Other current liabilities	2,154	4,480	9,092	12,420	15,894
<b>Total current liabilities</b>	<b>7,362</b>	<b>9,474</b>	<b>14,311</b>	<b>17,378</b>	<b>20,604</b>
Issued bonds	-	-	-	-	-
Other non-current liabilities	3	0	0	0	0
<b>Total non-current liabilities</b>	<b>3</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Total liabilities</b>	<b>7,365</b>	<b>9,474</b>	<b>14,311</b>	<b>17,378</b>	<b>20,604</b>
Net current assets	3,058	3,201	5,442	5,964	6,564
Equity attributable to owners of the parent	3,826	4,091	6,280	6,859	7,529
Minority interest	13	84	84	84	84
<b>Total equity</b>	<b>3,839</b>	<b>4,175</b>	<b>6,364</b>	<b>6,943</b>	<b>7,613</b>

Source(s): Company, ABCI Securities estimates





## Disclosures

### Analyst Certification

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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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