

# China / Hong Kong Industry Focus

# China Brokerage Sector

Refer to important disclosures at the end of this report

DBS Group Research . Equity

8 Oct 2024

## Next level awaits

- **Revised up FY24F-26F earnings by 5%-104% on higher ADT assumptions; our blue sky scenario suggests further 30% earnings upside**
- **Attractive entry point after correction with valuation near historical mean, given how HK/CN market is under-owned**
- **Favoring brokers with strong IB/institutional franchise to benefit from structural reforms and the M&A wave driving consolidation**
- **Top picks: [CITICS](#) > [CICC](#) > [FUTU](#)**

**Strong retail investing momentum set to last.** Compared to Jul 23, we see (1) a more concerted effort in the form of supportive policies for the economy & capital market; (2) retail investing confidence restored; (3) foreign capital are coming back to HK/China especially valuations in the US and other key markets are relatively high; and (4) better market liquidity with the rate cuts. With social media magnifying the FOMO sentiment, we expect momentum rather than mean reversion. We estimate >Rmb4tn (5% of A-share free float) of potential new funds flowing into stock market via public funds, due to wealth re-allocation from cash and fixed income to equities.

**Earnings outlook substantially improved.** We forecast A-share ADT from now to FY25F of Rmb1.25tn, assuming a further 10% growth in the average market cap and turnover rate of 1.5%, slightly higher than the 10-year average (1.42%). Our blue sky scenario assumes a turnover rate of 2.0% (FY15: 2.5%), suggesting a further 30% earnings upside and showcasing brokers' high earnings elasticity. Online brokers like Futu and Up Fintech are key beneficiaries too, as c.80% of their client trading volume comes from HK/China clients, per our estimate.

**Buy on pullback to tap on market momentum.** History suggests China brokers typically are front-runners and outperformers during early stage of bull market. Attractive entry opportunity re-emerged as valuation returned to near mean level after 20-30% correction in China brokers' H-shares. **We like CITICS and CICC**, as both are (1) backed by central-SOEs, and (2) with strong investment banking/institutional franchises that are rare in markets, thereby set to be ultimate winners from the expected wave of M&A-driven consolidation. Among online brokers, **we like Futu** for its stronger market share position in HK.

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### Recommendation & valuation

Stock	Ticker	TP		Rating	Upside
		Old	New		
<a href="#">CITICS -H</a>	6030 HK	15.5	35.0	BUY	49%
<a href="#">CICC -H</a>	3908 HK	11.0	25.0	BUY	55%
<a href="#">GF -H</a>	1776 HK	10.0	18.0	BUY	45%
<a href="#">HTSC -H</a>	6886 HK	11.5	22.5	BUY	48%
<a href="#">FUTU</a>	FUTU US	90.0	170.0	BUY	32%
<a href="#">TIGR</a>	TIGR US	5.8	14.0	BUY	22%

Source: Thomson Reuters, DBS Bank (Hong Kong) Limited ("DBS HK")  
Note: As of 8 Oct closing for H-shares, or 7 Oct for FUTU and TIGR

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Earnings revision and investment thesis

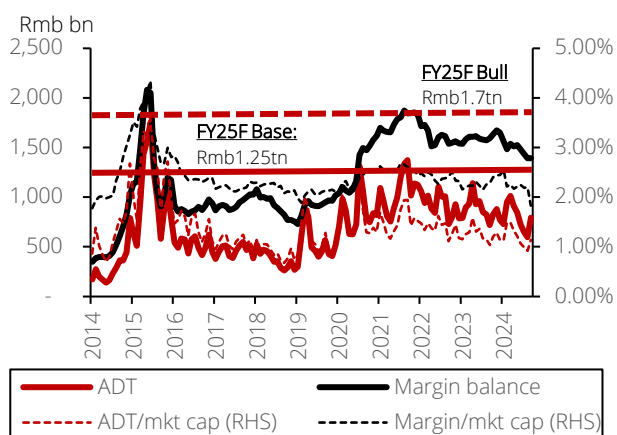
Due to record-high trading volume and likely a sustained run, we have substantially revised up China brokers' FY24F-26F earnings by 5%-104% to reflect our higher assumptions on A-share average daily trading (ADT), margin financing balance, public fund assets under management (AUM), and investment income. Our current projections, i.e. base case, assume FY25F A-share ADT to reach Rmb1.25tn (+40% y/y) – 10% increase in average market cap free-float from end-Sep to Rmb84tn, and turnover rate to reach 1.5% – is relatively conservative, which is just slightly higher than 10-year average of 1.4%.

A-share market assumptions, 2023-26F

Rmb tn	2023	2024F	2025F	2026F
Stock ADT, Rmb bn	877	895	1,253	1,339
yoy (%)	-3%	4%	40%	5%
Margin balance, Rmb bn	1,650	1,567	1,959	2,057
yoy (%)	7%	-5%	25%	5%
Public fund AUM, Rmb bn	27,599	33,119	38,418	43,028
yoy (%)	6%	20%	16%	12%

Source: Wind, DBS HK

A-share ADT / margin financing trend, 2014-now



Source: Wind, DBS HK

We have compiled a sensitivity analysis, on our top pick CITICS (6030 HK) for illustration, to showcase China brokers' high earnings elasticity amidst ADT expansion. Our blue sky scenario assumes that FY25F turnover rate to reach 2.0%, still lower than FY15's 2.5%, implying ADT to reach Rmb1.7tn (+90% y/y), lower than last five-day average of Rmb2.0tn. It also assumes margin financing balance and investment

income to grow at beta of 0.5. This will give 30% further upside in earnings for CITICS per our analysis, implying FY25F P/E of 9.8x, equivalent to -1SD over past 10-years. Thereby, we see meaningful upside from the sector despite the sharp rebound in share price over the past two weeks.

20%-30% pullback on sector share price offers another good entry point. The pull back on H-share after Golden-week holiday is largely within expectation. Brokers are typically front-runners during bull markets and heavily speculated by market participants, who might have taken profit after a well-expected catalyst was realised, i.e. ADT reached another record high of Rmb3.45tn on 8 Oct.

Yet, we think the strong retail momentum won't unwind easily once it's triggered in our view. With millions of new account opening pipelines and many investors have just re-activated their dormant brokerage accounts, and social media and online communication magnifying the FOMO sentiment, we expect retail investors to keep piling in new monies to the market, leading to a structural increase in market activities.

We estimate there could be >Rmb4tn of new monies flowing to A-shares via public funds, equivalent to 5% of A-share market free float, assuming (1) A-share as a % of total public fund asset (1H24: Rmb33tn) to rise from 17% (1H24 at 15%, assuming A-share AUM has gone up by 15% since then) to 25%, in line with end-2021, and (2) 3.7% of Rmb145tn household assets to flow back to public funds and 25% are allocated to equities, as public fund-to-deposit ratio to rebound from 23% in 1H24 to 26.7% in end-2021.

We think this round of retail-driven rally resembles the situation during 2014-15, as both saw (1) sudden dial-up of policy support, exceeding expectations; (2) huge injection of liquidity; and (3) a sharp market rally that reversed investor expectations. If history is any guide, the rally in 2014-15 lasted roughly more than half a year from Dec'14, when the turnover rate first surpassed 3%, similarly to 30 Sep (3.4%). While CITICS-H had deeper-than-market correction during Jan'15, it then outperformed the market again from then till Apr'15 with 44% return (vs SSE index: 26%). We think China brokers are still good beta play options for investors at this stage.

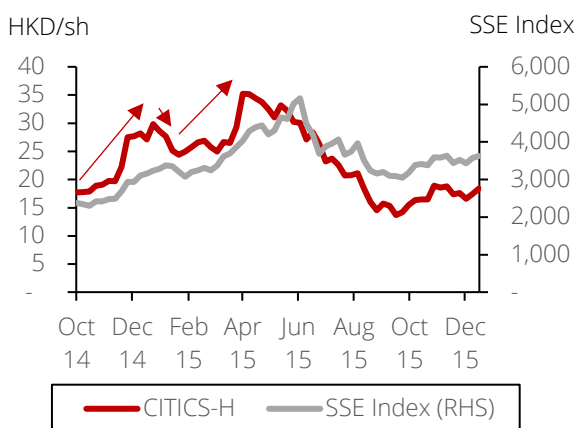
While this round of rally has been even sharper than in 2015, we still think it could be more sustainable vs. 2015, considering (1) more existing investors have experienced sharp pullbacks; (2) institutional – more rational – participation has significantly increased; (3) market is

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relatively mature with better investor protection mechanisms.

For online brokers, we peg their FY25F P/E multiples to slightly above their five-year average, as client acquisition efficiency, client asset inflows and trading velocity have substantially improved, and are comparable to the window of 2020-21 bull market centred on Chinese tech stocks.

**CITICS-H vs SSE index during 2014-15 rally**



(See peer comparison table for more valuation details)

Source: Bloomberg, DBS HK

Our top picks are CITICS and CICC, as both are (1) backed by central enterprises – who hold controlling / major stakes in a few China brokers and are more likely to facilitate M&As for the companies, and (2) with strong investment banking, institutional franchises, and international franchises, setting them apart from peers and likely be the ultimate winners from the expected wave of M&A-driven consolidation. Also, we expect improvement in trading income from cross-border investing and equity underwriting especially in HK market, benefitting CITICS/CICC.

We think online brokers will also benefit from the improved equity investing sentiment in HK/China, as **we estimate c.80% of Futu/Up Fintech’s client assets/trading volume is from HK/China**, (roughly 60%/50% of their clients are from HK/China, with higher average assets and they trade more frequently than clients from other countries such as Singapore). **We prefer Futu** for its stronger market share position in HK, thereby benefitting from a stronger structural boost.

For China traditional brokers, we peg their FY25F P/B multiple to 0.5-1SD above 10-year average, as the current vibrant market sentiment is clearly better than anytime over past five years, and the latest comparable window is 2014-15 rally when last record high in ADT was reached.

## Earnings revisions for China brokers

	RMB bn				YoY				Revisions			ROE			
	FY23	FY24F	FY25F	FY26F	FY23	FY24F	FY25F	FY26F	FY24F	FY25F	FY26F	FY23	FY24F	FY25F	FY26F
CITICS	19.2	22.8	27.1	31.0	-8%	19%	19%	14%	29%	47%	51%	7.8%	8.8%	9.8%	10.3%
CICC	5.5	6.6	9.5	11.1	-22%	20%	44%	17%	58%	97%	104%	6.4%	7.2%	9.6%	10.3%
GF	6.3	7.0	10.2	11.7	-33%	11%	46%	15%	15%	52%	New	5.7%	6.0%	8.4%	9.1%
HTSC	12.2	13.1	15.6	17.8	15%	8%	19%	14%	30%	53%	57%	8.1%	8.3%	9.2%	9.8%
<b>Average</b>	<b>10.8</b>	<b>12.4</b>	<b>15.6</b>	<b>17.9</b>	<b>-10%</b>	<b>15%</b>	<b>26%</b>	<b>15%</b>	<b>33%</b>	<b>62%</b>	<b>71%</b>	<b>7.0%</b>	<b>7.6%</b>	<b>9.3%</b>	<b>9.9%</b>

## Online brokers

	HKD/USD mn				YoY				Revisions			ROE			
	FY23	FY24F	FY25F	FY26F	FY23	FY24F	FY25F	FY26F	FY24F	FY25F	FY26F	FY23	FY24F	FY25F	FY26F
FUTU (HKD mn)	4,281	5,184	8,081	9,338	46%	21%	56%	16%	5%	38%	40%	18.8%	19.3%	24.4%	22.5%
TIGR (USD mn)	33	44	88	108	n.m.	36%	98%	23%	15%	50%	67%	7.0%	8.7%	15.2%	16.0%
<b>Average</b>	<b>n.m.</b>	<b>n.m.</b>	<b>n.m.</b>	<b>n.m.</b>	<b>n.m.</b>	<b>n.m.</b>	<b>n.m.</b>	<b>n.m.</b>	<b>10%</b>	<b>44%</b>	<b>53%</b>	<b>12.9%</b>	<b>14.0%</b>	<b>19.8%</b>	<b>19.2%</b>

Source: Company, DBS HK

## Key assumptions for our earnings adjustments:

- **A-share ADT** – we assume another 10% increase in the average market cap free-float to Rmb84tn, and **turnover rate of 1.5%** (10Y avg: 1.4%) from now till end-2025
- **A-share margin financing balance** – assume the beta to ADT growth is roughly 0.5, mirroring the pace of change during 2021
- **Public fund AUM** – expect retail investors continue shifting part of the household deposits (>Rmb140tn) to public funds
- **Investment income** – lifted investment yield to reflect higher return from proprietary equity investments and stronger equity trading income
- **For online brokers** – we forecast 44%-49% growth in trading volume in FY25F, slightly higher than market, thanks to client growth, asset inflows and revived interest towards Chinese internet stocks

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**Earnings sensitivity: Blue sky scenario suggests another 30% earnings upside from our current projections**

(using our top pick CITICS (6030 HK) for illustration)

CITICS (6030 HK)			FY25F ADT (Rmb tn)										
FY25F earnings (Rmb mn)			0.90	0.98	1.07	1.16	1.25	1.34	1.43	1.52	1.61	1.70	1.79
			0%	10%	20%	30%	40%	50%	60%	70%	80%	90%	100%
FY25F Margin Financing Balance (Rmb tn)	1.57	0%	20.6	22.0	23.4	24.9	26.3	27.8	29.2	30.7	32.1	33.5	35.0
	1.72	10%	20.9	22.3	23.8	25.2	26.7	28.1	29.5	31.0	32.4	33.9	35.3
	1.88	20%	21.2	22.6	24.1	25.5	27.0	28.4	29.9	31.3	32.7	34.2	35.6
	2.04	30%	21.5	23.0	24.4	25.9	27.3	28.7	30.2	31.6	33.1	34.5	36.0
	2.19	40%	21.8	23.3	24.7	26.2	27.6	29.1	30.5	31.9	33.4	34.8	36.3
	2.35	50%	22.2	23.6	25.1	26.5	27.9	29.4	30.8	32.3	33.7	35.2	36.6
	2.51	60%	22.5	23.9	25.4	26.8	28.3	29.7	31.1	32.6	34.0	35.5	36.9
	2.66	70%	22.8	24.3	25.7	27.1	28.6	30.0	31.5	32.9	34.4	35.8	37.2
	2.82	80%	23.1	24.6	26.0	27.5	28.9	30.4	31.8	33.2	34.7	36.1	37.6
	2.98	90%	23.5	24.9	26.3	27.8	29.2	30.7	32.1	33.6	35.0	36.4	37.9
3.13	100%	23.8	25.2	26.7	28.1	29.6	31.0	32.4	33.9	35.3	36.8	38.2	

Base

Blue Sky

CITICS (6030 HK)			FY25F ADT (Rmb tn)										
Implied PE (x)			0.90	0.98	1.07	1.16	1.25	1.34	1.43	1.52	1.61	1.70	1.79
			0%	10%	20%	30%	40%	50%	60%	70%	80%	90%	100%
FY25F Margin Financing Balance (Rmb tn)	1.57	0%	16.7	15.6	14.6	13.8	13.0	12.3	11.7	11.2	10.7	10.2	9.8
	1.72	10%	16.4	15.4	14.4	13.6	12.9	12.2	11.6	11.1	10.6	10.1	9.7
	1.88	20%	16.2	15.1	14.2	13.4	12.7	12.1	11.5	11.0	10.5	10.0	9.6
	2.04	30%	15.9	14.9	14.1	13.3	12.6	11.9	11.4	10.8	10.4	9.9	9.5
	2.19	40%	15.7	14.7	13.9	13.1	12.4	11.8	11.2	10.7	10.3	9.8	9.5
	2.35	50%	15.5	14.5	13.7	12.9	12.3	11.7	11.1	10.6	10.2	9.8	9.4
	2.51	60%	15.2	14.3	13.5	12.8	12.1	11.5	11.0	10.5	10.1	9.7	9.3
	2.66	70%	15.0	14.1	13.3	12.6	12.0	11.4	10.9	10.4	10.0	9.6	9.2
	2.82	80%	14.8	14.0	13.2	12.5	11.9	11.3	10.8	10.3	9.9	9.5	9.1
	2.98	90%	14.6	13.8	13.0	12.3	11.7	11.2	10.7	10.2	9.8	9.4	9.1
3.13	100%	14.4	13.6	12.9	12.2	11.6	11.1	10.6	10.1	9.7	9.3	9.0	

Source: Company, DBS HK

Note: For the sensitivity analysis, assuming investment income will grow along with increase in ADT with beta of 0.5

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## Peer comparison

Company Name	Ticker	price (LC)	Stock rating	Target		PB		PE		Div Yield		ROE		EPS CAGR
				Price (HK\$)	Mkt Cap (US\$ m)	FY24F (X)	FY25F (X)	FY24F (X)	FY25F (X)	FY24F (%)	FY25F (%)	FY24F (%)	FY25F (%)	23-26F (%)
<b>H-share brokers</b>														
China International Capital Corp L	3908 HK	16.14	BUY	25.00	21,557	0.77	0.70	11.0	7.6	1.7%	2.4%	7.2%	9.6%	26.4%
CITIC Securities Co Ltd	6030 HK	23.55	BUY	35.00	59,696	1.21	1.13	14.2	12.0	3.0%	3.2%	8.8%	9.8%	17.3%
GF Securities Co Ltd	1776 HK	12.38	BUY	18.00	18,128	0.74	0.70	12.6	8.6	3.0%	4.0%	6.0%	8.4%	23.1%
Huatai Securities Co Ltd	6886 HK	15.20	BUY	22.50	23,423	0.79	0.73	9.8	8.2	3.8%	4.5%	8.3%	9.2%	13.4%
<b>Mean</b>						0.88	0.82	11.9	9.1	2.9%	3.5%	7.6%	9.3%	20%
<b>Median</b>						0.78	0.72	11.8	8.4	3.0%	3.6%	7.7%	9.4%	20%
<b>Online brokers</b>														
Futu Holdings Ltd	FUTU US	128.93	BUY	170.00	18,169	5.30	4.17	26.7	16.9	0.0%	0.0%	19.3%	24.4%	30.7%
Up Fintech Holding Ltd	TIGR US	11.46	BUY	14.00	1,630	3.35	2.88	40.2	20.3	0.0%	0.0%	8.7%	15.2%	49.0%
<b>Mean</b>						4.32	3.52	33.4	18.6	0.0%	0.0%	14.0%	19.8%	40%

Source: Bloomberg, DBS HK

Note: As of 8 Oct closing for H-shares, or 7 Oct for FUTU and TIGR

#### Why we think this time is different

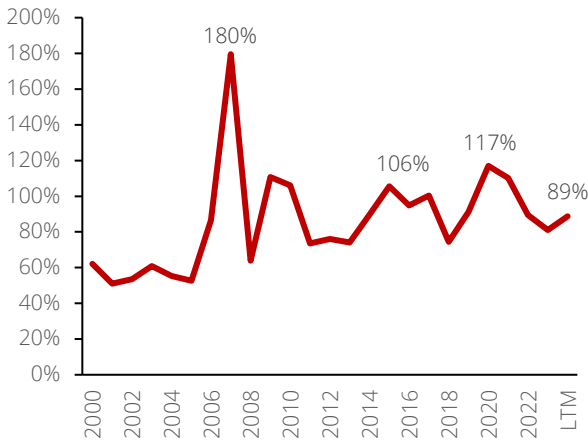
The Politburo first talked about the “revitalising the capital market” theme in its Jul 23 meeting. The CSRC launched numerous supportive initiatives shortly after that, including halving stamp duty, yet the market rally was short-lived. Below are reasons why we think this current rally could be different, and thereby more sustainable and possibly bring structural growth to China brokers.

#### What's different now

1. **Record-high volume reached**, which reflects the much broader participation by different market players, i.e. more investors have a stake now
2. **More monies coming in amidst FOMO** – retail customers are queuing to open brokerage accounts, reflecting their eagerness to participate in the rally, i.e., incremental funds
3. **Selling forces restricted, plus better investor protection** compared to a year ago, as the CSRC has tightened securities lending, discouraged derivatives, placed restrictions on share reduction by management, and concentrated selling orders by quant funds
4. **More concerted effort for supportive policies with better timing** – capital market measures alone weren't enough to reverse the lack of confidence; this time, the government launched measures for real estate, consumption, and the capital market on consecutive days, shortly after the US rate cut was announced
5. **Foreign capital still underweight** – per EPFR, we note sharp inflows from foreign capital during 26 Sep-3 Oct, reversing 24% of cumulative YTD outflows, as they might have switched out from relatively expensive markets. Yet, it takes time to reach equal weight again, and substantially more inflows should be expected
6. **Wealth effect for self-reinforcing cycle** – starting to see stronger consumption data during Golden Week upon a stronger capital market, which would possibly give the government confidence to continue with related policies, to drive consumption and thereby lift the economy
7. **National team is more ready** – the Rmb800bn in swap facilities/loans for buyback, potential set-up of a stabilisation fund, the potential new monies from Central Huijin, pension funds, and insurance funds are at the ready to stabilise the market to avoid big crashes that would erase investor confidence once again

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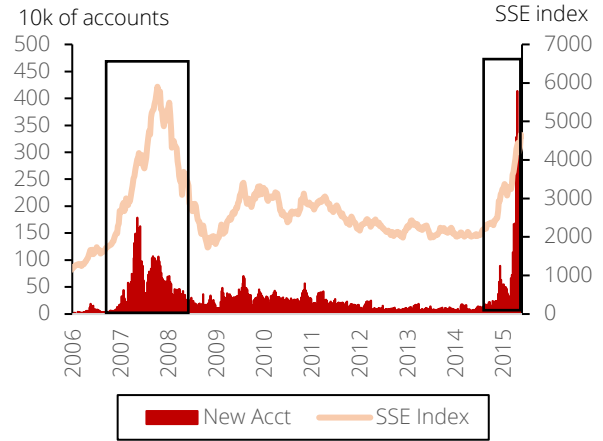
Market cap-to-GDP - more room to go



Source: CEIC, Wind, DBS HK

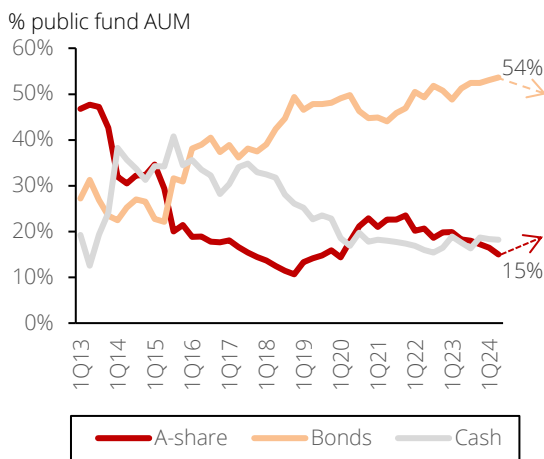
Note: Aggregate both HK & Mainland China figures for both Market Cap and GDP; GDP figures as of last four quarters, market cap as of 7 Oct

New brokerage account vs market indices



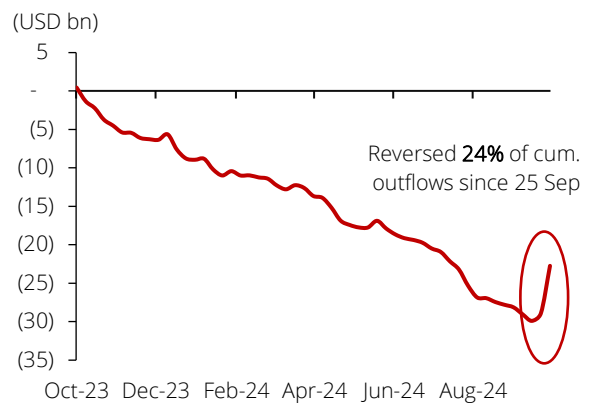
Source: Wind, DBS HK

Potential re-allocation from fixed income to equities



Source: Wind, DBS HK

Foreign capital flowing back to China



Source: EPFR, DBS HK



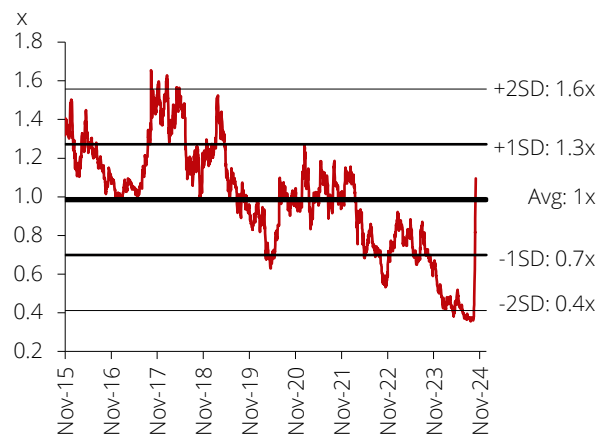
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China International Capital Corp - PE chart



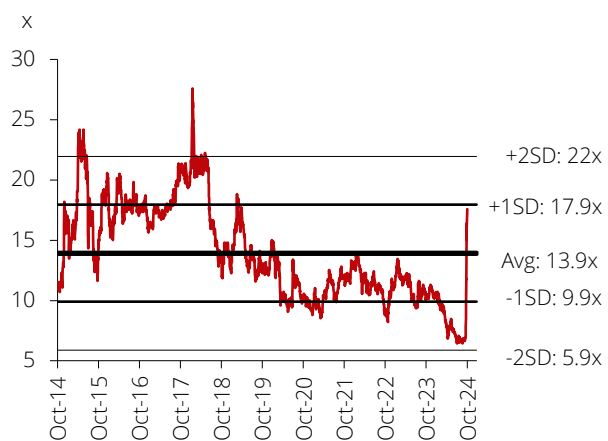
Source: Thomson Reuters, DBS Vickers

China International Capital Corp - PB chart



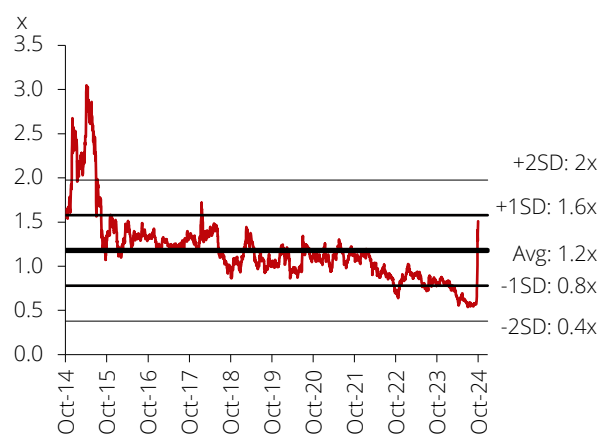
Source: Thomson Reuters, DBS Vickers

CITIC Securities - PE chart



Source: Thomson Reuters, DBS Vickers

CITIC Securities - PB chart



Source: Thomson Reuters, DBS Vickers

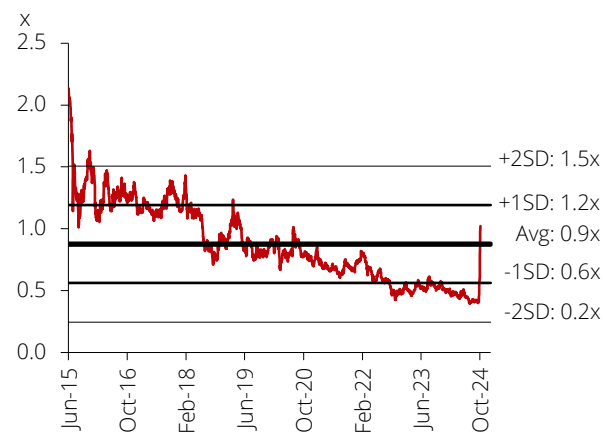
China Brokerage Sector

Huatai Securities - PE chart



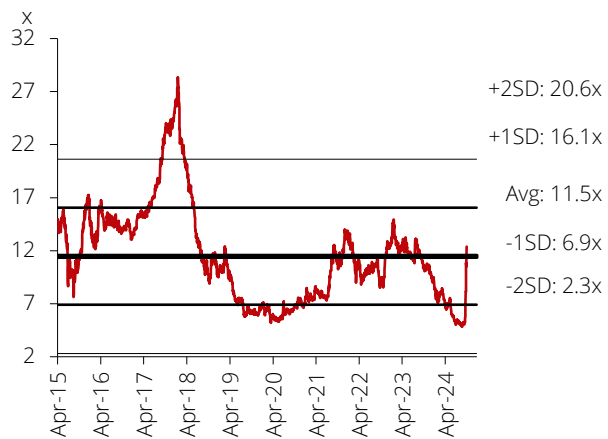
Source: Thomson Reuters, DBS HK

Huatai Securities - PB chart



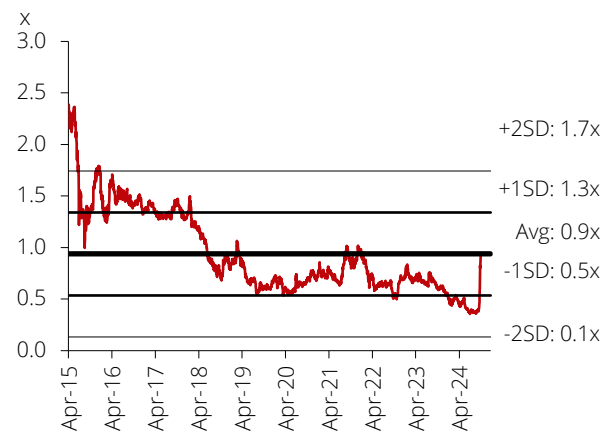
Source: Thomson Reuters, DBS HK

GF Securities - PE chart



Source: Thomson Reuters, DBS HK

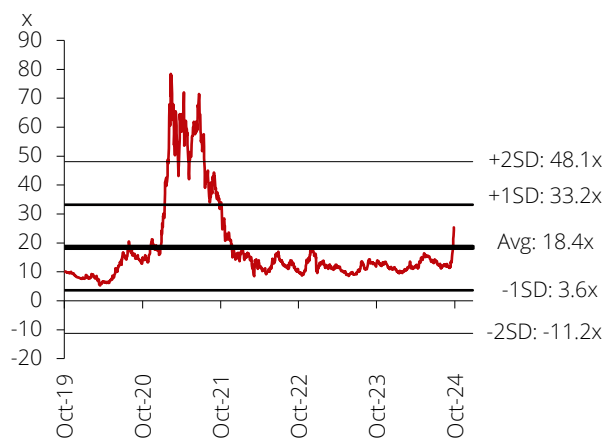
GF Securities - PB chart



Source: Thomson Reuters, DBS HK

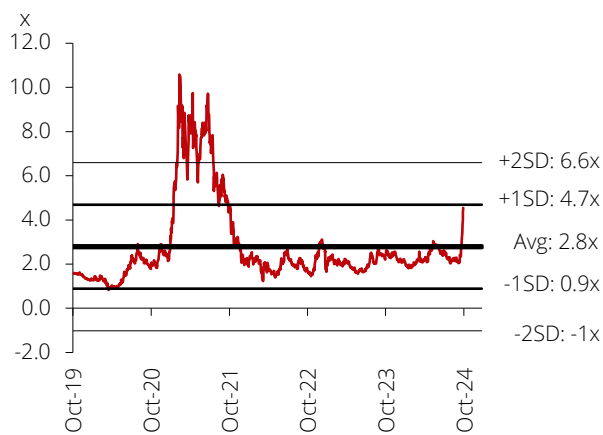
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FUTU Holdings - PE chart



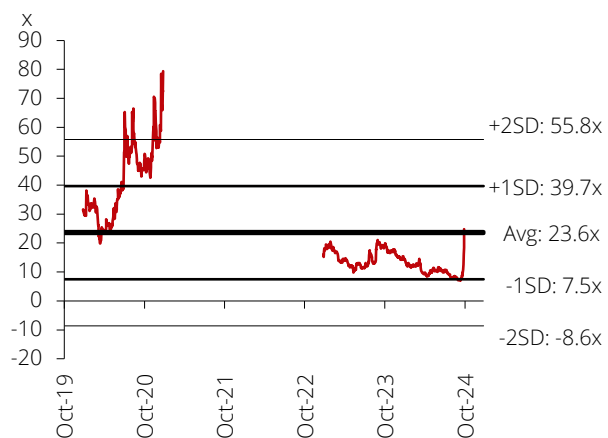
Source: Thomson Reuters, DBS HK

FUTU Holdings - PB chart



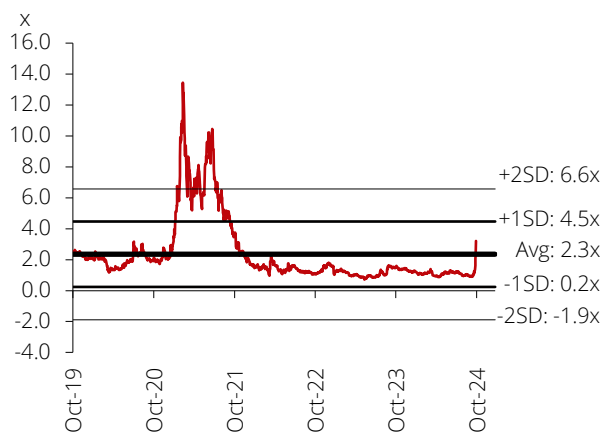
Source: Thomson Reuters, DBS HK

Up Fintech - PE chart



Source: Thomson Reuters, DBS HK

Up Fintech - PB chart



Source: Thomson Reuters, DBS HK

DBS Group Research recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

**HOLD** (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

**FULLY VALUED** (negative total return, i.e., > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

\*Share price appreciation + dividends

Completed Date: 8 Oct 2024 20:29:38 (HKT)

Dissemination Date: 8 Oct 2024 21:09:10 (HKT)

Sources for all charts and tables are DBS HK unless otherwise specified.

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