

9 May 2019

Financial Services | Exchanges

## HK Exchanges (388 HK)

**Buy** (Maintained)

### Sequential SADV Strength; Keep BUY

Target Price (Return) HKD313.00 (+18%)  
 Price: HKD265.20  
 Market Cap: USD42,510m  
 Avg Daily Turnover (HKD/USD) 1387m/177m

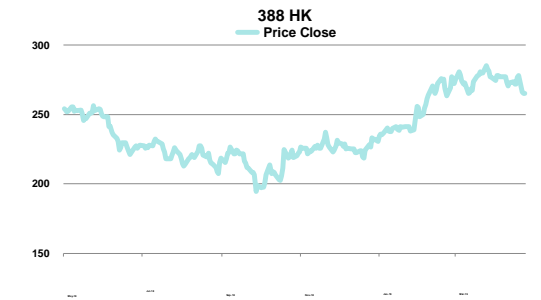
- **Keep BUY, HKD313.00 TP is based on 38x 2019F EPS** (+1SD from 31.3x historical mean), 18% upside plus 3% FY19F yield. 1Q19 results are in line, at 26% of our FY19 estimate. 1Q19 securities market SADV plunged sharply by 31% YoY, but grew 18% QoQ to HKD101bn. We assume 2019 SADV of HKD115bn, up from 2018's HKD107.4bn, as the recent uncertainties on US-China trade could generate more equities trading. Our 2020 SADV assumption is HKD130bn.
- **Within expectations.** Hong Kong Exchanges' 1Q19 net profit of HKD2.61bn was up 2% YoY, and a much stronger 43% QoQ – representing 26% of our FY19 projection. We maintain our earnings forecasts.
- **Revenue rose 3% YoY**, mainly driven by investment income and sundry income more than doubling YoY, a consequence of fair value gains on collective investment schemes, and higher interest income from margin funds and corporate funds. However, this gain was offset by the 17% drop in trading fees and trading tariffs from a 31% YoY SADV decline.
- **Stock Connect generated record quarterly high 1Q19 revenue and other income of HKD232m** (vs 1Q18's HKD172m). In particular, Northbound Trading turnover hit a record quarterly high, with a new record turnover of CNY75bn on 4 Mar.
- **Net profit margin of 61% was marginally lower YoY** but marked a sharp improvement over 4Q18's 51%.
- **Limited downside** even if 2019F SADV were to be lower than our base HKD115bn case. Our TP of HKD313.00 is pegged to 38x 2019F EPS. Hypothetically, if 2019F SADV were to be 20% lower at HKD92bn, HKEx's fair value would be HKD280, which is close to the current traded price.
- **Downside risks to our forecasts** include global geopolitical developments that could dampen economic growth and affect equities market investment sentiment.

#### Analyst

Hong Kong Research  
 +852 2525 1118  
[research.hk.equity@rhbgroup.com](mailto:research.hk.equity@rhbgroup.com)

#### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	17.0	(7.1)	10.1	16.8	3.5
Relative	3.4	(4.7)	5.1	4.9	6.9
52-wk Price low/high (SGD)	195.60 – 286.20				



Source: Bloomberg

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover (HKDm)	13,180	15,867	17,123	18,267	19,595
Recurring net profit (HKDm)	7,404	9,312	10,186	10,990	11,862
Recurring net profit gr (%)	28.3	25.8	9.4	7.9	7.9
Recurring P/E (x)	44.8	35.6	32.6	30.2	28.0
P/B (x)	8.9	8.1	7.9	7.7	7.5
P/CF (x)	44.7	35.0	41.9	36.5	33.8
Dividend Yield (%)	2.0	2.5	2.8	3.0	3.2
EV/EBITDA (x)	18.4	17.9	17.3	16.2	15.0
Return on average equity (%)	21.3	23.9	24.7	26.0	27.3
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash
Interest coverage (x)	65.3	96.4	96.5	93.6	99.5

Source: Company data, RHB

**Figure 1: HKEx's 1Q19 results summary**

FYE Dec (HKDm)	1Q18	4Q18	1Q19	YoY%	Comments
Revenue	4,150	3,571	4,288	3.3	Mild 1Q19 revenue YoY growth was mainly due to investment & sundry income growth, but partly offset by the decline in trading fees and trading tariffs.
EBIT	3,035	2,218	3,070	1.2	
Net Profit	2,562	1,828	2,608	1.8	1Q19 net profit of HKD2.61bn represents 26% of our FY19F.
Net profit margin (%)	61.5%	51.2%	60.8%		
Securities ADV (HKD bn)	146.1	85.7	101.1	(30.8)	1Q19 cash market SADV rose 18% QoQ, although it declined a sharp 31% YoY.
Derivatives ADC on Futures Exch	676,821	755,389	659,000	(2.6)	1Q19 derivatives ADC contracted by a marginal 3% YoY.

Source: Company data

**Figure 2: HKEx's earnings sensitivity to changes in stock market turnover**

	FY19F			
	Base case	20%	40%	-20%
Stockmarket turnover % rise		20%	40%	-20%
SADV (HKD bn)	115	138	161	92
Revenue (HKDm)	17,123	18,466	19,808	15,781
Net profit (HKDm)	10,186	11,282	12,379	9,089
Diluted EPS (HKD)	8.1	9.0	9.9	7.3
Target P/E rating	38	38	38	38
TP (HKD)	313	347	381	280

Source: RHB

Figure 3: HKEx's financial data

FYE 31Dec (in HKDm)	2017	2018	2019F	2020F	2021F
Income affected by market turnover:	8,439	10,599	11,609	12,568	13,774
- Trading fees and trading tariff	4,856	6,339	7,237	7,671	8,491
- Clearing & settlement fees	2,691	3,281	3,275	3,677	3,769
- Depository, custody and nominee services fees	892	979	1,097	1,221	1,514
Stock exchange listing fees	1,333	1,721	1,625	1,503	1,531
Market data fees	857	899	1,028	1,310	1,353
Other revenue	945	1,033	1,020	983	986
<b>Revenue</b>	<b>11,574</b>	<b>14,252</b>	<b>15,282</b>	<b>16,365</b>	<b>17,645</b>
Net investment income	1,599	1,584	1,841	1,902	1,950
<b>Total revenue</b>	<b>13,180</b>	<b>15,867</b>	<b>17,123</b>	<b>18,267</b>	<b>19,595</b>
Operating expenses	(4,424)	(4,872)	(5,058)	(5,255)	(5,563)
<b>EBIT</b>	<b>8,756</b>	<b>10,995</b>	<b>12,065</b>	<b>13,012</b>	<b>14,032</b>
Finance costs					
<b>PBT</b>	<b>8,610</b>	<b>10,883</b>	<b>11,943</b>	<b>12,877</b>	<b>13,898</b>
Tax	(1,255)	(1,592)	(1,791)	(1,932)	(2,085)
<b>PAT</b>	<b>7,355</b>	<b>9,291</b>	<b>10,152</b>	<b>10,945</b>	<b>11,813</b>
<b>PATMI</b>	<b>7,404</b>	<b>9,312</b>	<b>10,186</b>	<b>10,990</b>	<b>11,862</b>
<b>Growth (YoY %)</b>					
Total revenue	19%	20%	8%	7%	7%
EBIT	27%	26%	10%	8%	8%
PAT	28%	26%	9%	8%	8%
<b>Margins (%)</b>					
EBIT	66%	69%	70%	71%	72%
PAT	56%	59%	59%	60%	60%
<b>Key assumptions</b>					
<b>SADV - HKD bn</b>					<b>131.0</b>
	<b>88.2</b>	<b>107.4</b>	<b>115.0</b>	<b>130.0</b>	
<b>Growth %</b>	<b>32%</b>	<b>22%</b>	<b>7%</b>	<b>13%</b>	<b>1%</b>
<b>Equities market velocity (%)</b>	<b>64%</b>	<b>89%</b>	<b>90%</b>	<b>96%</b>	<b>90%</b>
<b>Futures Exch derivatives avg daily contracts</b>	<b>441,320</b>	<b>686,602</b>	<b>650,000</b>	<b>670,000</b>	<b>670,000</b>
<b>Growth %</b>	<b>-5%</b>	<b>56%</b>	<b>-5%</b>	<b>3%</b>	<b>0%</b>

Source: Company data, RHB

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## KUALA LUMPUR

### RHB Investment Bank Bhd

Level 3A, Tower One, RHB Centre  
Jalan Tun Razak  
Kuala Lumpur 50400  
Malaysia  
Tel : +603 9280 8888  
Fax : +603 9200 2216

## JAKARTA

### PT RHB Sekuritas Indonesia

Wisma Mulia, 20th Floor  
Jl. Jenderal Gatot Subroto No. 42  
Jakarta 12710  
Indonesia  
Tel : +6221 2783 0888  
Fax :+6221 2783 0777

## HONG KONG

### RHB Securities Hong Kong Ltd.

12<sup>th</sup> Floor, World-Wide House  
19 Des Voeux Road  
Central  
Hong Kong  
Tel : +852 2525 1118  
Fax : +852 2810 0908

## BANGKOK

### RHB Securities (Thailand) PCL

10th Floor, Sathorn Square Office Tower  
98, North Sathorn Road, Silom  
Bangrak, Bangkok 10500  
Thailand  
Tel: +66 2088 9999  
Fax :+66 2088 9799

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### RHB Securities Singapore Pte Ltd.

10 Collyer Quay  
#09-08 Ocean Financial Centre  
Singapore 049315  
Tel : +65 6533 1818  
Fax : +65 6532 6211