

# China / Hong Kong Company Update

## HK Exchanges & Clearing

Bloomberg: 388 HK EQUITY | Reuters: 0388.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

28 Apr 2022

### HOLD

Last Traded Price (27 Apr 2022): HK\$321.40 (HSI : 19,946)

Price Target 12-mth: HK\$361 (12% upside) (Prev HK\$422)

#### Analyst

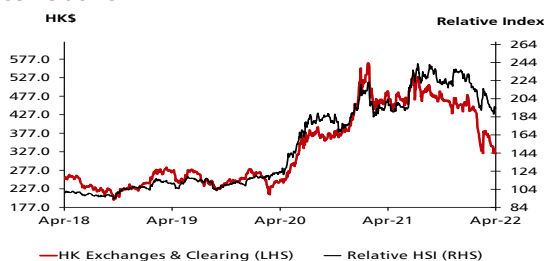
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#### What's New

- 1QFY22 earnings below market expectation, with 31% drop in net profit y-o-y
- Expect weak market sentiment to persist but a better 2H is anticipated where overhangs show easing sign
- Revised down FY22/23F earnings by 14/10% to reflect the lower ADT and net investment income expectation
- Maintain HOLD with a lower TP of HK\$361

#### Price Relative



#### Forecasts and Valuation

FY Dec (HK\$m)	2020A	2021A	2022F	2023F
Turnover	19,190	20,950	19,920	21,844
EBITDA	14,238	16,041	14,680	16,253
Pre-tax Profit	13,222	14,841	13,480	15,053
Net Profit	11,395	12,535	11,389	12,714
Net Pft (Pre Ex) (core profit)	11,395	12,535	11,389	12,714
Net Profit Gth (Pre-ex) (%)	21.3	10.0	(9.1)	11.6
EPS (HK\$)	9.04	9.94	9.03	10.08
EPS Gth (%)	21.3	10.0	(9.1)	11.6
Diluted EPS (HK\$)	9.04	9.94	9.03	10.08
DPS (HK\$)	6.63	6.63	6.02	6.72
BV Per Share (HK\$)	38.79	39.35	38.91	39.13
PE (X)	35.6	32.3	35.6	31.9
P/Cash Flow (X)	27.4	30.9	33.9	30.4
P/Free CF (X)	30.2	34.0	37.9	33.5
EV/EBITDA (X)	27.8	23.4	25.3	22.3
Net Div Yield (%)	2.1	2.1	1.9	2.1
P/Book Value (X)	8.3	8.2	8.3	8.2
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE (%)	24.5	25.4	23.1	25.8

Earnings Rev (%)			(14)	(10)
Consensus EPS (HK\$)			10.14	12.01
Other Broker Recs:		B:30	S:1	H:5

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

### Weak market sentiment to persist in near term

#### Investment Thesis

The weak market sentiment is likely to persist in the near term due to the Ukraine-Russia war, upcoming interest rate hikes, regulatory developments in the new economy sectors, and the COVID-19 pandemic and lockdowns in China. The year-to-date ADT stays at the HK\$140bn level, in contrast to HK\$204bn during the same period last year. We reckon the current risk appetite remains low in the HK equity market, given that there is no near-term catalyst.

A better 2H2022 ADT is anticipated and has been reflected in the current share price. We believe when the uncertainties show sign of clearing out, there is a likely return of southbound net buys for the companies offered in HK that are attractively valued and have unique secular growth; also, given the significant increase in southbound eligible mutual funds. We expect ADT for the rest of the year at HK\$165-175bn.

ADT structural changes to persist in FY22-23F. ADT structural changes such as secondary listings, MSCI derivatives, attractive valuation of the HK market vs. that of A-shares and the US, and higher southbound participation should support a further increase in trading activities when market uncertainties ease.

#### Valuation:

We maintain our HOLD recommendation with a lowered target price (TP), at HK\$361. The TP is based on an unchanged valuation benchmark to FY22F, with our TP premised on a 40x PE, pegged to a +1SD of its 10-year mean.

#### Where we differ:

While some market participants focus on the long-term development for HKEx, we believe its share price will still be dominated in the performance of the ADT in the near term. As such, we continue to reference FY22F as a valuation basis rather than the more aggressive FY23F.

#### Key Risks to Our View:

Trading volume coming in higher than expected. Market overhangs clear out earlier than expected.

#### At A Glance

Issued Capital (m shrs)	1,268
Mkt Cap (HKm/US\$m)	407,535 / 51,939
Major Shareholders (%)	
The Hong Kong SAR Government	5.9
Free Float (%)	94.1
3m Avg. Daily Val. (US\$m)	292.43
GICS Industry: Financials / Diversified Financials	



Watchlist the stock on Insights Direct to receive prompt updates



## HK Exchanges & Clearing

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### WHAT'S NEW

#### HKEx 1QFY22 earnings below market expectation

**HKEx 1QFY22 earnings below market expectation.** HKEx's net profit dropped 31% y-o-y to HK\$2,668m, missing the market's expectation. Revenue dropped 16% y-o-y to HK\$4.8bn due to the lower trading and clearing fees driven by lower headline average daily turnover (ADT) and the decline in net investment income. The ADT was at HK\$146.5bn in 1QFY22, a 36% drop from 1QFY21, due to the weak market sentiment amid the Ukraine-Russia war and American depository receipt (ADR) financial conflicts between the US and China.

HKEx was not able to maintain its usual EBITDA margin of 77%-78% as it did in previous years and recorded a 75% EBITDA margin in 1QFY22. This is due to an increase in operating expenses because of higher allocated costs from the Listing Division and an increase in cash incentives relating to new products in the cash, equity, and financial derivatives segment and post trade segment.

**Weak market sentiment to persist in short term amid market uncertainties.** The Hang Seng Index has dropped 14% YTD. Persistent inflationary pressure, tightening of monetary policy, upcoming interest rate hikes, and geographical fragility could continue to impact investor willingness to invest in the equity market. Although the IPO pipeline remains strong, supported by Chinese companies seeking homecoming listings and a new listing regime for SPACs and overseas issuers, we think issuers are more likely to wait till the uncertainties to be clear. Moreover, the lockdowns in Shanghai also contributed to the low-risk appetite at the current stage.

Moving into 2H, these overhangs will likely persist, but tension should ease compared to 1Q2022. The market reaction to the existing overhangs is less. We are cautiously optimistic for 2H as compared to 1H this year.

**Revised down FY22/23F earnings estimate by 14/10% to reflect worse-than-expected 1Q.** Due to the weak market sentiment in 1QFY22, we have revised down our FY22/23F ADT estimates to HK\$157bn and HK\$176bn to reflect the lower-than-expected ADT. The new ADT estimate for FY22F is equivalent to HK\$165-175bn in the next seven months of the year. We are cautiously optimistic for 2H2022, and hopeful that the Ukraine-Russia war will end or ease moving toward to 2H. We revise down our earnings estimate by 14/10% to reflect the revision of the ADT estimate as well as the lower estimate for net investment income. We maintain HOLD with a lower TP of HK\$361. The TP is based on an unchanged valuation benchmark to FY22F, with our TP premised on a 40x PE, pegged to a +1SD of its 10-year mean.

#### Company Background

Hong Kong Exchanges & Clearing Limited (HKEx) owns and operates the stock exchange, futures exchange, and their related clearing houses in Hong Kong. The company provides trading platforms for a range of cash and derivatives products and the facilities for processing trades.

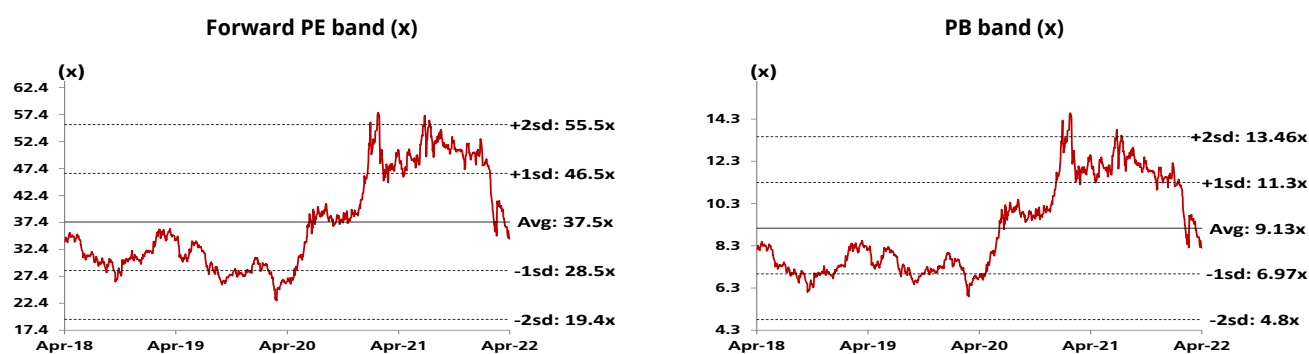
## HK Exchanges & Clearing

### Quarterly / Interim Income Statement (HK\$m)

FY Dec	1Q2021	4Q2021	1Q2022	% chg y-o-y	% chg q-o-q
Revenue	5,956	4,813	4,690	(21.3)	(2.6)
Cost of Goods Sold	0.0	0.0	0.0	N/A	N/A
<b>Gross Profit</b>	<b>5,956</b>	<b>4,813</b>	<b>4,690</b>	<b>(21.3)</b>	<b>(2.6)</b>
Other Oper. (Exp)/Inc	(1,474)	(1,663)	(1,571)	6.6	(5.5)
<b>Operating Profit</b>	<b>4,482</b>	<b>3,150</b>	<b>3,119</b>	<b>(30.4)</b>	<b>(1.0)</b>
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	nm	nm
Associates & JV Inc	16.0	22.0	25.0	56.3	13.6
Net Interest (Exp)/Inc	(39.0)	(38.0)	(36.0)	7.7	5.3
Exceptional Gain/(Loss)	0.0	0.0	0.0	nm	nm
<b>Pre-tax Profit</b>	<b>4,459</b>	<b>3,134</b>	<b>3,108</b>	<b>(30.3)</b>	<b>(0.8)</b>
Tax	(632)	(463)	(445)	(29.6)	(3.9)
Minority Interest	13.0	3.00	5.00	(61.5)	66.7
<b>Net Profit</b>	<b>3,827</b>	<b>2,674</b>	<b>2,663</b>	<b>(30.4)</b>	<b>(0.4)</b>
Net profit bef Except.	3,827	2,674	2,663	(30.4)	(0.4)
EBITDA	4,747	3,444	3,426	(27.8)	(0.5)
<b>Margins (%)</b>					
Opg Profit Margins	75.3	65.4	66.5		
Net Profit Margins	64.3	55.6	56.8		

Source: Company, DBS HK

### Historical PE and PB band



Source: Thomson Reuters, DBS HK

## HK Exchanges & Clearing

### Key Assumptions

FY Dec	2019A	2020A	2021A	2022F	2023F
ADT on the Stock Exchange (\$bn)	87.2	129.5	166.0	156.8	176.4
ADT of DWs, CBBCs and warrants traded on the Stock Exchange (\$bn)	18.0	18.6	20.1	23.5	26.5
ADT of Northbound Trading	41.7	91.3	120.1	116.9	135.4
ADT of Southbound Trading (HK\$bn)	10.8	24.4	24.4	36.9	44.1
Number of newly listed companies on Main Board	168.0	146.0	97.0	97.0	97.0

Source: Company, DBS HK

### Segmental Breakdown (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
<b>Revenues (HK\$ m)</b>					
Cash instruments	3,646	4,991	6,131	5,245	5,767
Equity and Financial Derivatives	2,988	3,241	3,436	3,694	4,098
Commodities	1,399	1,454	1,478	1,426	1,494
Clearing	6,226	7,637	7,995	7,810	8,539
Platform and Infrastructure	796	910	1,050	1,208	1,389
Corporate Items	1,256	957	860	538	558
<b>Total</b>	<b>16,311</b>	<b>19,190</b>	<b>20,950</b>	<b>19,920</b>	<b>21,844</b>
<b>EBITDA (HK\$ m)</b>					
Cash instruments	3,043	4,396	5,517	4,375	4,816
Equity and Financial Derivatives	2,437	2,549	2,645	3,011	3,344
Commodities	731	762	783	744	781
Clearing	5,402	6,752	7,125	6,772	7,414
Platform and Infrastructure	551	606	731	835	962
Corporate Items	99	(424)	(546)	(830)	(837)
<b>Total</b>	<b>12,263</b>	<b>14,641</b>	<b>16,269</b>	<b>14,908</b>	<b>16,481</b>
<b>EBITDA Margins (%)</b>					
Cash instruments	83.5	88.1	90.0	83.4	83.5
Equity and Financial Derivatives	81.6	78.6	77.0	81.5	81.6
Commodities	52.3	52.4	53.0	52.2	52.3
Clearing	86.8	88.4	89.1	86.7	86.8
Platform and Infrastructure	69.2	66.6	69.6	69.2	69.3
Corporate Items	N/A	N/A	N/A	N/A	N/A
<b>Total</b>	<b>75.2</b>	<b>76.3</b>	<b>77.7</b>	<b>74.8</b>	<b>75.4</b>

Source: Company, DBS HK

## HK Exchanges & Clearing

### Income Statement (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenue	16,311	19,190	20,950	19,920	21,844
Cost of Goods Sold	0	0	0	0	0
<b>Gross Profit</b>	<b>16,311</b>	<b>19,190</b>	<b>20,950</b>	<b>19,920</b>	<b>21,844</b>
Other Opg (Exp)/Inc	(5,092)	(5,746)	(6,035)	(6,366)	(6,717)
<b>Operating Profit</b>	<b>11,219</b>	<b>13,444</b>	<b>14,915</b>	<b>13,554</b>	<b>15,127</b>
Other Non Opg (Exp)/Inc	0	(110)	0	0	0
Associates & JV Inc	32	69	80	80	80
Net Interest (Exp)/Inc	(300)	(181)	(154)	(154)	(154)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>10,951</b>	<b>13,222</b>	<b>14,841</b>	<b>13,480</b>	<b>15,053</b>
Tax	(1,561)	(1,845)	(2,343)	(2,128)	(2,376)
Minority Interest	1	18	37	37	37
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>9,391</b>	<b>11,395</b>	<b>12,535</b>	<b>11,389</b>	<b>12,714</b>
Net Profit before Except.	9,391	11,395	12,535	11,389	12,714
EBITDA	11,695	14,238	16,041	14,680	16,253
<b>Growth</b>					
Revenue Gth (%)	2.8	17.7	9.2	(4.9)	9.7
EBITDA Gth (%)	1.4	21.7	12.7	(8.5)	10.7
Opg Profit Gth (%)	2.0	19.8	10.9	(9.1)	11.6
Net Profit Gth (%)	0.8	21.3	10.0	(9.1)	11.6
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	100.0	100.0	100.0	100.0	100.0
Opg Profit Margin (%)	68.8	70.1	71.2	68.0	69.3
Net Profit Margin (%)	57.6	59.4	59.8	57.2	58.2
ROAE (%)	22.1	24.5	25.4	23.1	25.8
ROA (%)	3.5	3.4	3.1	2.9	3.2
ROCE (%)	21.0	22.8	23.5	21.4	23.9
Div Payout Ratio (%)	89.0	73.3	66.7	66.7	66.7
Net Interest Cover (x)	37.4	74.3	96.9	88.0	98.2

Source: Company, DBS HK

## HK Exchanges & Clearing

### Quarterly Income Statement (HK\$ m)

FY Dec	1Q2021	2Q2021	3Q2021	4Q2021	1Q2022
Revenue	5,956	4,872	5,309	4,813	4,690
Cost of Goods Sold	0	0	0	0	0
<b>Gross Profit</b>	<b>5,956</b>	<b>4,872</b>	<b>5,309</b>	<b>4,813</b>	<b>4,690</b>
Other Oper. (Exp)/Inc	(1,474)	(1,409)	(1,489)	(1,663)	(1,571)
<b>Operating Profit</b>	<b>4,482</b>	<b>3,463</b>	<b>3,820</b>	<b>3,150</b>	<b>3,119</b>
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	16	22	20	22	25
Net Interest (Exp)/Inc	(39)	(38)	(39)	(38)	(36)
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>4,459</b>	<b>3,447</b>	<b>3,801</b>	<b>3,134</b>	<b>3,108</b>
Tax	(632)	(685)	(563)	(463)	(445)
Minority Interest	13	8	13	3	5
<b>Net Profit</b>	<b>3,827</b>	<b>2,783</b>	<b>3,238</b>	<b>2,674</b>	<b>2,663</b>
Net profit bef Except.	<b>3,827</b>	<b>2,783</b>	<b>3,238</b>	<b>2,674</b>	<b>2,663</b>
EBITDA	3,744	3,744	4,106	3,444	3,426

### Growth (QoQ)

Revenue Gth (%)	16.8	(18.2)	9.0	(9.3)	(2.6)
EBITDA Gth (%)	28.7	(21.1)	9.7	(16.1)	(0.5)
Opg Profit Gth (%)	32.3	(22.7)	10.3	(17.5)	(1.0)
Net Profit Gth (%)	30.8	(27.3)	16.3	(17.4)	(0.4)

### Growth (YoY)

Revenue Gth (%)	48.6	2.1	0.0	(5.6)	(21.3)
EBITDA Gth (%)	63.6	2.5	0.0	(6.6)	(27.8)
Opg Profit Gth (%)	65.6	0.2	(1.9)	(7.0)	(30.4)
Net Profit Gth (%)	69.2	(6.3)	(3.0)	(8.6)	(30.4)

### Margins

Gross Margins (%)	100.0	100.0	100.0	100.0	100.0
Opg Profit Margins (%)	75.3	71.1	72.0	65.4	66.5
Net Profit Margins (%)	64.3	57.1	61.0	55.6	56.8

Source: Company, DBS HK

## HK Exchanges & Clearing

### Balance Sheet (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Net Fixed Assets	1,589	1,657	1,605	1,537	183
Invt in Associates & JVs	95	164	244	142	161
Other LT Assets	22,172	21,592	22,386	22,386	22,386
Cash & ST Invt	10,603	10,417	30,242	35,253	42,875
Inventory	0	0	0	0	0
Debtors	25,791	47,059	32,717	18,341	18,341
Other Current Assets	218,801	318,218	312,112	316,226	314,880
<b>Total Assets</b>	<b>279,051</b>	<b>399,106</b>	<b>399,304</b>	<b>393,882</b>	<b>398,822</b>
ST Debt	338	340	340	340	340
Creditors	22,447	42,974	28,335	23,511	25,831
Other Current Liab	208,152	303,020	317,289	317,289	319,665
LT Debt	80	83	86	85	85
Other LT Liabilities	3,533	3,453	3,344	3,344	3,344
Shareholder's Equity	44,173	48,918	49,626	49,067	49,346
Minority Interests	328	318	284	247	210
<b>Total Cap. &amp; Liab.</b>	<b>279,051</b>	<b>399,106</b>	<b>399,304</b>	<b>393,882</b>	<b>398,822</b>
Non-Cash Wkg. Capital	13,993	19,283	(795)	(6,233)	(12,276)
Net Cash/(Debt)	10,185	9,994	29,816	34,829	42,450
Debtors Turn (avg days)	493.8	692.8	694.9	467.8	306.5
Creditors Turn (avg days)	(7,135.0)	(9,974.4)	(9,611.4)	(6,988.1)	(6,650.6)
Asset Turnover (x)	0.1	0.1	0.1	0.1	0.1
Current Ratio (x)	1.1	1.1	1.1	1.1	1.1
Quick Ratio (x)	0.2	0.2	0.2	0.2	0.2
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	261.0	319.4	286.6	302.9	294.8
Z-Score (X)	1.6	1.6	1.7	1.7	1.7

Source: Company, DBS HK

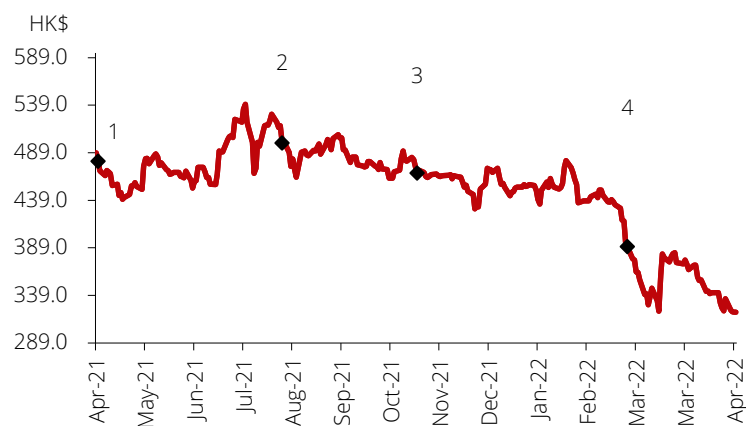
### Cash Flow Statement (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Pre-Tax Profit	10,951	13,222	14,841	13,480	15,053
Dep. & Amort.	1,044	1,198	1,356	1,357	1,358
Tax Paid	(431)	(1,845)	(2,343)	(2,128)	(2,376)
Assoc. & JV Inc/(loss)	(32)	(69)	(80)	(80)	(80)
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg. Cap.	65	(127)	(101)	(113)	(69)
Other Operating CF	(1,535)	2,391	(546)	(546)	(546)
<b>Net Operating CF</b>	<b>10,062</b>	<b>14,770</b>	<b>13,127</b>	<b>11,970</b>	<b>13,340</b>
Capital Exp. (net)	(1,091)	(1,351)	(1,221)	(1,286)	(1,254)
Other Invt. (net)	(2,435)	(6,131)	0	0	0
Invt in Assoc. & JV	0	0	(80)	103	(20)
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	41	0	0	0	0
<b>Net Investing CF</b>	<b>(3,485)</b>	<b>(7,482)</b>	<b>(1,301)</b>	<b>(1,184)</b>	<b>(1,273)</b>
Div Paid	(5,785)	(6,983)	(5,908)	(5,501)	(4,169)
Chg in Gross Debt	(1,121)	(118)	(119)	(118)	(119)
Capital Issues	0	0	0	0	0
Other Financing CF	(248)	(373)	14,027	(154)	(154)
<b>Net Financing CF</b>	<b>(7,154)</b>	<b>(7,474)</b>	<b>8,000</b>	<b>(5,774)</b>	<b>(4,442)</b>
Currency Adjustments	0	0	0	0	0
Chg in Cash	(577)	(186)	19,826	5,013	7,625
Opg CFPS (HK\$)	7.93	11.81	10.49	9.58	10.63
Free CFPS (HK\$)	7.11	10.64	9.44	8.47	9.58

Source: Company, DBS HK

## HK Exchanges & Clearing

### Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	29-Apr-21	HK\$488.80	HK\$563.00	Buy
2:	12-Aug-21	HK\$517.50	HK\$501.00	Hold
3:	28-Oct-21	HK\$474.80	HK\$501.00	Hold
4:	25-Feb-22	HK\$394.60	HK\$422.00	Hold

Source: DBS HK

Analyst: Dennis Lam  
Byron Lam



## HK Exchanges & Clearing

DBS HK 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: 28 Apr 2022 13:29:38 (HKT)

Dissemination Date: 28 Apr 2022 14:12:48 (HKT)

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

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