



Trading Desk Note

Hong Kong Exchanges & Clearing (0388.HK)

- Risks for Chinese companies listed in the U.S. are mounting. This benefits non-U.S. exchanges.
- HKEX technically oversold: LSEG takeover bid & weak macro conditions. Ray of light on Hong Kong's civil unrest changes our call to bullish.
- BUY TP: HK\$266.60 31x FY20E P/E

Last Price:
HK\$237.20

Market Cap (HK\$):
\$299b

52w High/Low (HK\$):
195.60 – 286.20

T12M P/E (X):
31.3

T12M P/B (X):
6.8

Net Gearing:
Net Cash

The rumour mill has been circulating the idea of a Chinese listing ban, but recently hit headlines with a White House leak

1. Trump Administration Threatens Delisting Chinese Companies and Limiting Portfolio Flows to China

1.1. Bloomberg first reported the Trump administration is considering ways to limit portfolio flows to China. Internal deliberations said that they would do this by limiting American exposure through government pension funds and delisting Chinese companies from US stock exchanges.

1.2. UBS estimates, based on Federal Reserve sources, that this could be US\$60-100b of Chinese equities or about 3.5 – 6.0% of the MSCI China index. Not significant from the U.S. pension fund perspective.

1.3. But the long-term implication is that the U.S. exchanges will lose Chinese listings despite generally offering higher liquidity and valuations. In 2018, 31 Chinese companies raised US\$8.5b in NYSE/NASDAQ out of a total of 190 IPOs worth US\$47b. Alibaba raised US\$25b in 2014, iQiYi US\$2.4b, Tencent Music US\$1.1b and so on.

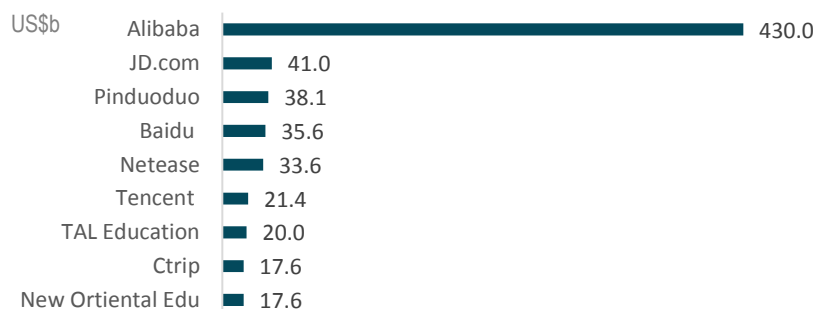
Exhibit 1: Portfolio Restriction News Flow Timeline

05/06/2019	Reuters: Bipartisan lawmakers introduce Equitable Act to block or face delisting, Chinese companies listed in the U.S. if they do not allow overseas companies to audit accounts or submit to regulatory oversight. "The Equitable Act."
26/08/2019	Bloomberg: "Trump Aides Say He Has Power to Force Companies from China" – Mnuchin referring to International Emergency Economic Powers Act (IEEPA).
27/09/2019	Bloomberg: "White House Weighs Limits on U.S. Portfolio Flows into China" according to people familiar with internal deliberations."
29/09/2019	Bloomberg: "U.S. Treasury Says No Plans to Block Chinese Listings 'at This Time.' – Stopped short of specific responses.
30/09/2019	CNBC: "Peter Navarro: Reports that US would restrict Chinese companies are 'fake news'"

Source: Bloomberg, Reuters, Platinum Research

The HKEX will be a primary beneficiary if a ban on Chinese listings or even delisting does occur.

Exhibit 2: Market Capitalization of Selected Chinese Companies on U.S. Exchanges (US\$b)



Source: Bloomberg, Platinum Research

Note: excludes SOE listings such as Petrochina & Sinopec

1.4. According to the U.S.-China Economic and Security Review Commission, there are 156 Chinese companies listed on U.S. exchanges with a total market cap of US\$1.2t. Many were highlighted to be non-compliant with Public Company Accounting Oversight Board's (PCAOB) and 11 were deemed state-owned (>30% State stake). These are the grounds U.S. lawmakers are pursuing to limit U.S. capital flowing to China.

2. How Would the U.S. Do It?

The U.S. Is Increasingly Seeing China as an Economic Competitor and Geopolitical Rival.

"[...] wonder if it is an inching towards bigger moves." - Dalio

2.1. Ray Dalio has discussed the situation and points to US history in the late 1930s and early 40s. The US froze Japanese assets and embargoed oil to Japan by utilising emergency powers. Today, US presidents have access to the International Emergency Economic Powers Act (IEEPA) of 1977. According to the US Treasury, **this would allow the President to unilaterally block any and all foreign exchange, capital flow and transactions towards a nation and even force divestitures** in order to deal with US national security threats.

2.2. But most likely, Chinese companies will face U.S. auditing standards if they want to remain listed in the U.S, but ultimately Beijing will have a final say. **Alternatively, Chinese companies could relist on another market such as London, Hong Kong or China.**

2.3. Delisting happens all the time, but the lines are blurring. Semiconductor Manufacturing International Corp. voluntarily delisted on the NYSE, citing low trading liquidity. SMIC was blacklisted by Washington on national security concerns as a key Huawei Technology client.

2.4. The impact is already being felt by Chinese companies. In 2018, ZTE was brought to its knees with an export ban and a fine of US\$1.2b by the U.S. Department of Commerce. **Chinese companies now need to seriously consider any political risk by going to U.S. markets.**

3. The HKEX – Next Best Out of the West?

3.1. Even if the above is difficult to execute, this gives non-U.S. bourses an excellent opportunity to woo Chinese companies seeking capital raising. We see measures such as dual-class shares (WVR), biotech listings and secondary exchange rules for Chinese or international companies seeking a listing in Hong Kong.

Exhibit 3: HKEX / CSRC Deregulation

Hong Kong		
Apr-2018	Amendments to Main Board Listing Rules	Permits biotech companies, weighted voting right structures (WVR) and concessionary secondary listing route into Hong Kong
China		
May-2018	CDR Issuing and Trading Administration Rule	Listing requirements and trading rules for CDRs was published.

Source: HKEX, China Securities Regulatory Commission (CSRC)

Exhibit 4: Global Exchange New Capital Raised IPO (US\$m)

US\$m	2014	2015	2016	2017	2018
SSE	5,052	17,366	15,313	20,574	13,042
HKEX	29,980	33,940	25,164	16,495	36,745
SZSE	5,745	7,821	7,208	13,818	7,738
NYSE	63,155	18,047	28,244	11,404	26,253
NASDAQ	22,809	13,033	8,335	7,472	22,300
KRX	4,430	3,903	5,415	7,058	2,510
ASX	11,834	8,150	6,343	5,204	6,329
JPX	8,351	14,451	7,512	5,136	28,379
SGX	2,753	414	1,722	3,400	554
TWSE	718	569	388	280	553

Source: World Federation of Exchanges, Platinum Calculations

Exhibit 5: China Has the 2nd Highest Total Valuation of Unicorns

Country	Total Valuation (US\$b)	Global total of 403 unicorns
1 United States	606.6	China has 23% of them totalling a valuation of US\$331b.
2 China	330.8	
3 India	47.2	
4 Others	46.8	
5 United Kingdom	38.4	Four decacorns (US\$10b+) are based in China.
6 South Korea	25.9	
7 Indonesia	20.0	Bytedance, Didi Chuxing, Bitmain, DJI
8 Germany	18.9	
9 Singapore	14.0	

Source: CB Insights, Platinum Calculations (as of May 2019)

Note: Unicorn = unlisted company with valuation over US\$1b

HKEX and China Deregulation Indicates the Exchanges are Gearing Up to Attract New Listings Away from the U.S.

HKEX is Consistently a Top 2 IPO Exchange Globally

Plenty of Fish in the Sea: HKEX Eyes China for IPOs

PRC Ministry of Science suggests a total valuation of US\$600b...



PLATINUM
Broking

Recommendation:
BUY

TP: HK\$266.60 (+12.4%)

Hong Kong Exchange & Clearing (388.HK)

11 October 2019

SECTOR: Exchange & Clearing

HSI: 26,308

PRICE: HK\$237.20

EARNINGS (reported in HK\$m)						KEY DATA	
For the fiscal year ended	2016	2017	2018	2019E	2020E	Issued Capital (m Shrs)	1,261.2
Turnover	10,398	11,574	14,252	16,193	17,919	Market Cap (HK\$m)	299,157
Operating Profit	6,897	8,744	10,978	11,596	13,031	Avg. 6M Turnover (HK\$m)	1,296.1
Net Profit	5,769	7,404	9,312	9,548	10,599	52 Week High/Low (HK\$)	286.2 / 195.6
EPS (HK\$)	4.76	6.03	7.50	7.63	8.48	Net Gearing (%)	(252.38)
% Change	(29.0%)	26.7%	24.4%	1.7%	11.1%	Book Value per Share (HK\$)	35.07
DPS (HK\$)	4.25	5.40	6.68	6.95	7.80	Free Float (%)	94.02%
Dividend yield (%)	1.8%	2.3%	2.8%	2.9%	3.3%	Major Shareholder(s)	Hong Kong S.A.R. (5.98%)
PE Ratio (x)	38.49	39.77	30.21	31.08	27.99		

INTERIM RESULTS (reported in HK\$m)				
Period	1H18	1H19	% change	
Turnover	8,194	8,578	4.7%	
Operating Profit	5,847	6,130	4.8%	
Net Profit	5,025	5,203	3.5%	
EPS (HK\$)	4.07	4.16	2.2%	

Note: Differences may arise due to rounding errors

Time-sensitive data and value were retrieved as at 29 August 2016.

Source: Bloomberg, HKEx, Company data, Platinum estimates

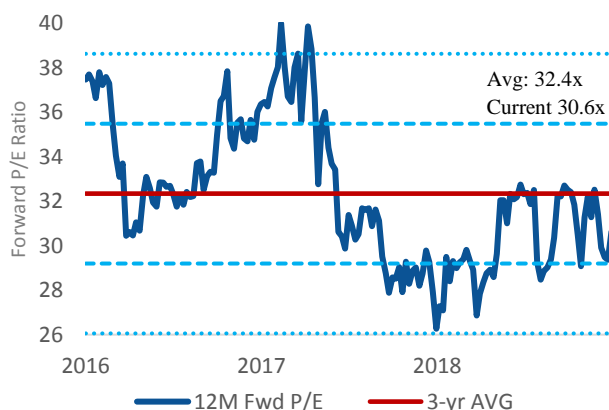
SECTION 4 Valuation

2.1. BUY TP: HK\$266.60 31x FY20E EPS:\$7.70

2.2. Consensus estimates have been revised downwards due to weak macro conditions, Hong Kong political unrest and a decline in investment flows through IPOs (-32.7% YoY). Revenue is forecasted to only grow modestly at 2.4% YoY and EPS at 2.6% YoY implying a FY19E P/E of 29.4x. Currently 1 S.D. below 3-yr average.

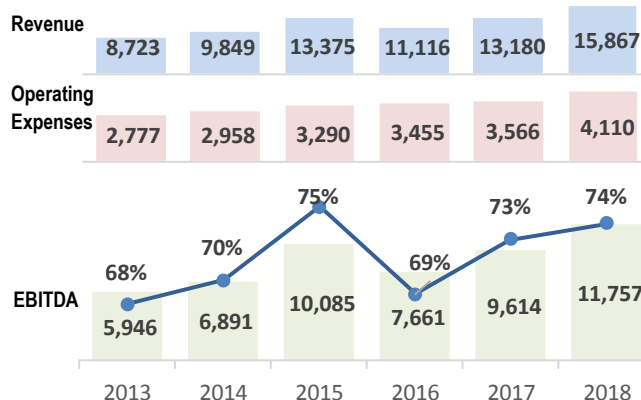
2.3. We think these estimates look conservative in 2019 considering market conditions and look towards improving conditions in FY20E with EPS growth of 11.8% YoY.

Exhibit 6: HKEX rolling 3-year forward P/E ratio



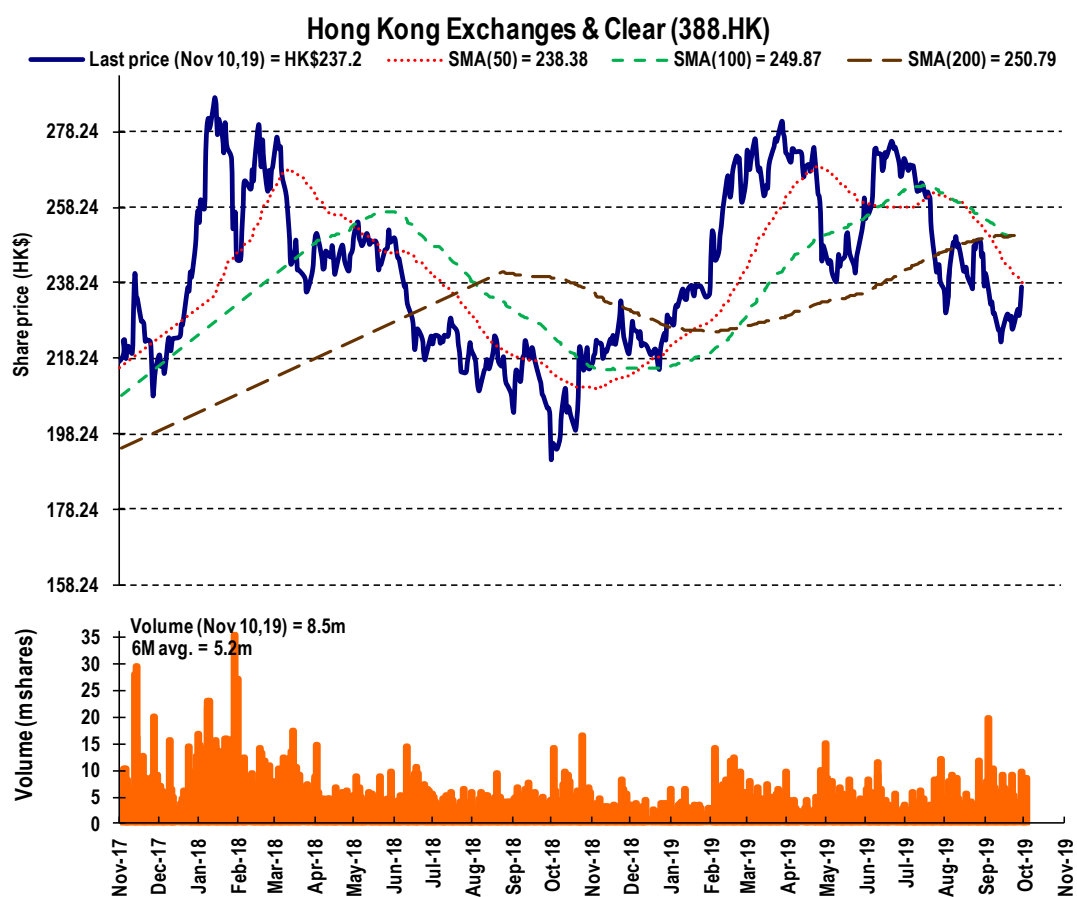
Source: Bloomberg, Platinum Research

Exhibit 7: EBITDA% Follows Revenue - 1H19 EBITDA 77%



Source: Company data, Platinum Research

Exhibit 8: HKEX 2-year Share Price Performance



Source: Bloomberg, Platinum

Exhibit 8: HKEX Market Peer Comparisons

Name	Ticker	FY18 Total Assets (HK\$m)	Mkt cap (HK\$m)	Closing price (HK\$)	52-week High/Low (HK\$)	6M Volume (m shrs)	6M Turnover (HK\$m)	Cur. P/E (x)	FY19E P/E (x)	FY20E P/E (x)	Cur. P/B (x)	FY19E P/B (x)	FY20E P/B (x)	FY18 ROE (%)	FY19E ROE (%)	FY20E ROE (%)
APAC																
1	HKEX	255,948	299,157	237.20	286.2 / 195.6	5.11	1,287.7	31.26	31.08	27.99	6.76	6.89	6.61	23.88	22.77	24.65
2	Singapore Exchange	12,172	51,353	47.95	49.15 / 38.36	2.84	127.4	23.01	23.53	21.82	8.24	8.34	7.72	34.12	35.30	36.35
3	ASX	81,750	83,942	433.59	470.86 / 301.25	0.46	203.7	31.99	31.75	31.17	4.02	3.96	4.09	11.33	12.39	13.01
Simple avg								28.75	28.79	26.99	6.34	6.40	6.14	23.11	23.49	24.67
Mkt cap wtd avg								30.42	30.32	27.87	6.41	6.49	6.25	22.66	22.24	23.78
US																
1	Intercontinental Exchange	727,741	416,403	743.03	749.38 / 546.56	2.16	1,467.2	28.06	24.87	22.55	3.11	3.08	2.98	11.64	11.87	12.45
2	NASDAQ	123,132	127,301	772.99	825.53 / 592.04	0.66	501.1	20.69	19.96	18.34	2.94	2.82	2.67	8.09	14.54	15.56
3	CME Group	607,626	606,321	1693.18	1763.92 / 1263.08	1.37	2,123.3	35.83	31.95	29.51	2.91	2.87	2.83	8.12	8.67	9.38
Simple avg								28.19	25.59	23.47	2.98	2.92	2.83	9.28	11.69	12.46
Mkt cap wtd avg								31.34	28.06	25.75	2.98	2.94	2.87	9.39	10.48	11.18
Europe																
1	London Stock Exchange Group	8,289,138	249,395	712.43	779.1 / 377.85	0.63	382.3	52.53	36.73	32.54	7.32	7.83	5.44	14.61	17.00	16.65
2	Euronext	13,820	41,879	598.28	656.63 / 401.16	0.12	68.9	22.82	18.31	16.32	5.97	5.17	4.39	28.67	29.15	29.04
Simple avg								37.67	27.52	24.43	6.64	6.50	4.92	21.64	23.08	22.85
Mkt cap wtd avg								24.49	19.34	17.24	6.04	5.32	4.45	27.88	28.47	28.35
Overall avg								31.54	27.30	24.96	5.32	5.27	4.63	18.01	19.42	19.99
Overall mkt wtd avg								30.91	28.42	26.09	3.98	3.95	3.81	13.43	14.11	15.01

Source: Bloomberg, Platinum

Key Risks

1. HKEX income and profitability largely depends on the performance and liquidity of stocks listed on the exchange. Profitability will be negatively impacted if market capitalisation of the listed stocks drops and other variables such as derivatives, commodities and fees. These factors typically depend on prevailing market and macro sentiment.

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