

## COMPANY UPDATE

### Hong Kong Exchanges and Clearing (388 HK)

More Patience Needed For Recovery

**HKEX's sentiment appears weak, but we anticipate multiple positive signs in the near future, including: a) the potential expansion of Stock Connect, b) the launch of renminbi counters, c) the potential trading of treasury bond futures, and d) listing reform for hard tech companies. Maintain BUY with a reduced target price of HK\$405.30 as we made slight tweaks to EPS to incorporate full-year ADT adjustment.**

#### WHAT'S NEW

- **Recent market activities.** Hong Kong Exchanges and Clearing's (HKEX) share price has corrected by nearly 50% since 1Q21's peak mainly due to the Hong Kong stock market correction, which has reduced market capitalisation and consequently turnover volumes. Jan-Sep 22 ADT was HK\$124b (vs HK\$180b in Jan-Sep 21), representing a decrease of 31.3% yoy primarily due to: a) slowdown in monthly turnover (+1% mom), and b) a decline in average market capitalisation (-13.5% mom).
- **Multiple upsides ahead...** We anticipate multiple positive trends for HKEX as policies are being discussed to bolster HKEX's unique position in China, including:
  - Potential expansion of Stock Connect.** The China Securities Regulatory Commission (CSRC) plans to expand the Stock Connect programme to include more Hong Kong primary-listed foreign companies and listed companies on the Shanghai and Shenzhen exchanges.
  - Introduction of renminbi counters in Hong Kong in 1H23.** The authorities have been cooperating to achieve this target. To support this effort, the Hong Kong government has proposed waiving stamp duty on certain stock transactions for dual counter trading.
  - Possibility of Treasury bond futures trading in Hong Kong.** The CSRC will support Hong Kong's introduction of China Treasury bond futures, thereby accelerating China's Treasury bond futures market's opening to foreign investors.
  - Listing reform for hard-tech corporations.** HKEX is contemplating a rule change that would reduce the revenue requirement for hard tech companies seeking an IPO. According to reports, HKEX could begin public consultations as early as this month and finalise the rule change by the end of the year.
- **...but more time needed for recovery.** We view the aforementioned policies as catalysts for the medium-to-long term, as the timeline for implementing most of these policies has not been outlined. Hence, we believe more time is required for HKEX's share price to recover. However, we maintain our view on HKEX's near-term catalysts including the potential upticks in trading activities or IPOs which are contingent on the improvements in market conditions. In 3Q22, there were 27 IPOs that raised a total of US\$6.6b, more than twice the proceeds raised in 2Q22 including Tianqi Lithium and China Tourism Group Duty Free which had raised HK\$13.5b and HK\$16.2b respectively, in Jul 22 and Aug 22.

#### KEY FINANCIALS

Year to 31 Dec (HK\$m)	2020	2021	2022F	2023F	2024F
Net turnover	19,190	20,950	19,082	22,589	25,614
EBITDA	14,641	16,269	14,499	17,826	20,624
Operating profit	14,641	16,269	14,499	17,826	20,624
Net profit (rep./act.)	11,505	12,535	10,513	13,416	15,767
Net profit (adj.)	11,505	12,535	10,513	13,416	15,767
EPS (HK\$ cent)	915.3	989.0	829.4	1,058.5	1,244.0
PE (x)	29.8	27.6	32.9	25.8	21.9
P/B (x)	8.4	8.0	7.2	7.1	5.3
EV/EBITDA (x)	23.0	20.7	23.2	18.9	16.3
Dividend yield (%)	3.0	3.3	2.7	3.4	4.0
Net margin (%)	60.0	59.8	55.1	59.4	61.6
Net debt/(cash) to equity (%)	(24.8)	(17.5)	(18.3)	(21.0)	(16.1)
ROE (%)	29.5	29.5	22.6	27.2	27.2
Consensus net profit	-	-	10,401	12,849	14,733
UOBKH/Consensus (x)	-	-	1.01	1.04	1.07

Source: Hong Kong Exchanges and Clearing, Bloomberg, UOB Kay Hian

## BUY

(Maintained)

Share Price	HK\$272.60
Target Price	HK\$405.30
Upside	+48.7%
(Previous TP)	HK\$435.43

#### COMPANY DESCRIPTION

Hong Kong Exchanges and Clearing Limited (HKEx) owns and operates the stock exchange, futures exchange and their related clearing houses in Hong Kong.

#### STOCK DATA

GICS sector	Financials
Bloomberg ticker:	388 HK
Shares issued (m):	1,267.8
Market cap (HK\$m):	345,612.3
Market cap (US\$m):	44,028.2
3-mth avg daily t'over (US\$m):	135.5

#### Price Performance (%)

52-week high/low		HK\$490.80/HK\$266.60		
1mth	3mth	6mth	1yr	YTD
(12.3)	(27.5)	(12.3)	(27.5)	(12.3)

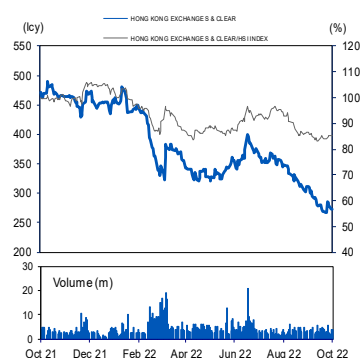
#### Major Shareholders

The Government of Hong Kong SAR	5.8
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FY22 NAV/Share (HK\$)	37.85
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FY22 Net Cash/Share (HK\$)	6.91
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#### PRICE CHART



Source: Bloomberg

#### ANALYST(S)

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### ESSENTIALS

- **Expansion of Stock Connect with dual-counter trading and the exemption of stamp duty.** Currently, HKEX has some international listings, but Mainland Chinese investors cannot trade or invest in such foreign firms listed in Hong Kong. Once Mainland Chinese investors are permitted to trade these stocks, we believe Hong Kong-listed foreign firms could see an increase in trading volume and would attract more foreign firms to list in Hong Kong. Note that southbound (SB) trade accounted for 12% of Hong Kong's total revenue but the six international listings only account for about HK\$240b market cap (around 0.78% of Sep 22's market cap). Thus, we see this as a long-term catalyst which will only be significant if more foreign companies choose to list in Hong Kong.

Under the dual counter-trading plan, Mainland Chinese can trade HK-listed/SB-eligible shares in HK dollar or renminbi. This increases the flexibility of trading currencies, giving Mainland investors more options and reducing forex risk. To facilitate this, the Hong Kong government has proposed waiving stamp duty for brokers who act as market makers to facilitate the trading of renminbi-denominated shares by the end of this year. 14 Hong Kong-listed companies have indicated they will consider issuing renminbi-denominated shares in support of a government plan to allow trading in such shares via the Stock Connect scheme beginning in 1H23. Note that the Hong Kong government raised the stamp duty on all share transactions by 30% to 0.13% of the trading value for both buyers and sellers in Aug 21.

- **Near-term catalysts remain unchanged, weak macro environment remains the key headwind.** We remain our view on the following catalysts which should take place in near term: a) expansion of Southbound Stock Connect by increasing the number of dual primary listings and/or the inclusion of secondary-listed names; b) China ADRs' accelerating pace of listing in Hong Kong and conversion of ADRs into H-shares (for those already listed in Hong Kong) – regardless of the outcome of negotiations between China and US authorities, accelerating the pace of listing and conversion should be a safe play for China ADRs; and c) IPO listings will increase in 2H22 following the conclusion of regulations and/or the relaxation of listing requirements. While multiple catalysts bode well for HKEX, we expect trading volume to still take some time to fully recover due to the weak macro environment. We view the 20th National Congress of the Chinese Communist Party to be key catalyst as policies should be finalised after the congress.

### EARNINGS REVISION/RISK

- **Modest revision to EPS as we incorporate full-year ADT adjustment.** We revise our 2022 and 2023 EPS to incorporate our full-year ADT adjustment due to slowdown in Jan-Sep 22 ADT.

### VALUATION/RECOMMENDATION

- **Maintain BUY with a lower target price of HK\$405.30 (previous: HK\$435.43),** as we trim our 2022 and 2023 EPS and ADT by 2% and 3% respectively because the lower trading volume is expected to persist, given the weak macro environment. Despite the temporary setback in sentiment, we believe that the market will look ahead towards steep earnings recovery in 2023 and partially price in the potential ADT uplift due to Chinese ADRs delisting.
- **Our target price is derived based on the three-stage DDM,** assuming payout ratio: 85%; growth rate: Y1: -17.47%, Y2: 27.61%, Y3: 17.52%; and terminal: 4%; EPS: Y1: HK\$8.29, Y2: HK\$10.58, Y3: HK\$12.44, Y4: HK\$12.69. Our target price also implies 33x 2023F PE (+0.5SD below five-year mean) and trades at about 30x PE premium compared with Hang Seng Index (HSI). We deem that such valuation is reasonable as historically HKEX trades at a 22-37x PE premium to HSI (2018-21).

### SIX FOREIGN LISTINGS IN HONG KONG

Name	Stock Code	Market Cap (HK\$B)	Daily Average Turnover (HK\$M)
Prada SpA	1913 HK	102.61	35.46
United Co Rusal International PJSC	0486 HK	50.90	28.71
L'Occitane International SA	0973 HK	34.93	12.21
Samsonite International SA	1910 HK	28.62	95.07
NagaCorp Ltd	3918 HK	23.84	8.80
Vesync Cp. Ltd	2148 HK	3.70	4.38

Source: Bloomberg, UOB Kay Hian

### 14 COMPANIES CONSIDERING ISSUING RENMINBI-DENOMINATED SHARES

Name	Stock Code	Daily Average Turnover (HK\$M)
Tencent	0700 HK	8,791.52
New World Development	0017 HK	104.97
Ping An Insurance	2318 HK	1,475.54
Hong Kong Exchanges and Clearing (HKEX)	0388 HK	1,687.51
AIA	1299 HK	1,914.73
Bank of China (HK)	3988 HK	741.04
JD.com	9618 HK	2,524.87
Lenovo	0992 HK	330.31
CNOOC	0883 HK	1,300.03
Sun Hung Kai Properties	0016 HK	367.40
China Resources Beer	0291 HK	509.26
Xiaomi	1810 HK	1,215.54
NetEase	9999 HK	986.53
Meituan	3690 HK	5,319.43

Source: Bloomberg, UOB Kay Hian

### PROFIT & LOSS

Year to 31 Dec (HK\$m)	2021	2022F	2023F	2024F
Net turnover	20,950.0	19,082.4	22,588.7	25,614.5
EBITDA	16,269.0	14,499.3	17,825.5	20,623.5
Deprec. & amort.	0.0	0.0	0.0	0.0
EBIT	16,269.0	14,499.3	17,825.5	20,623.5
Total other non-operating income	(1,354.0)	(1,489.4)	(1,683.0)	(1,901.8)
Associate contributions	(74.0)	(100.0)	(112.0)	(112.0)
<b>Pre-tax profit</b>	<b>14,841.0</b>	<b>12,909.9</b>	<b>16,030.5</b>	<b>18,609.7</b>
Tax	(2,343.0)	(2,452.9)	(2,698.2)	(2,968.0)
Minorities	37.0	55.5	83.3	124.9
<b>Net profit</b>	<b>12,535.0</b>	<b>10,512.6</b>	<b>13,415.6</b>	<b>15,766.6</b>
Net profit (adj.)	12,535.0	10,512.6	13,415.6	15,766.6

### CASH FLOW

Year to 31 Dec (HK\$m)	2021	2022F	2023F	2024F
<b>Operating</b>	<b>14,769.0</b>	<b>15,887.2</b>	<b>17,092.2</b>	<b>18,390.7</b>
Pre-tax profit	11,956.0	12,792.9	13,688.4	14,646.6
Other operating cashflows	2,813.0	3,094.3	3,403.7	3,744.1
<b>Investing</b>	<b>(7,482.0)</b>	<b>(6,542.1)</b>	<b>(5,950.1)</b>	<b>(5,611.8)</b>
Proceeds from sale of assets	56.0	61.6	67.8	74.5
Others	(7,538.0)	(6,603.7)	(6,017.9)	(5,686.3)
<b>Financing</b>	<b>(7,474.0)</b>	<b>(9,004.0)</b>	<b>(9,022.6)</b>	<b>(10,748.0)</b>
Dividend payments	(6,983.0)	(7,681.3)	(8,449.4)	(9,294.4)
Proceeds from borrowings	(31.0)	(37.2)	(44.6)	(53.6)
Others/interest paid	(460.0)	(1,285.5)	(528.6)	(1,400.1)
<b>Net cash inflow (outflow)</b>	<b>(187.0)</b>	<b>341.1</b>	<b>2,119.4</b>	<b>2,030.9</b>
<b>Beginning cash &amp; cash equivalent</b>	<b>10,603.0</b>	<b>11,133.2</b>	<b>11,689.8</b>	<b>12,274.3</b>
Changes due to forex impact	26.0	26.0	26.0	26.0
<b>Ending cash &amp; cash equivalent</b>	<b>10,753.0</b>	<b>11,828.3</b>	<b>13,011.1</b>	<b>14,312.2</b>

### BALANCE SHEET

Year to 31 Dec (HK\$m)	2021	2022F	2023F	2024F
Fixed assets	3,955.0	3,850.0	3,501.0	4,778.3
Other LT assets	19,901.0	19,563.0	20,734.0	27,145.7
Cash/ST investment	10,753.0	11,828.3	13,011.1	14,312.2
Other current assets	244,442.0	363,864.7	362,057.9	497,107.2
<b>Total assets</b>	<b>279,051.0</b>	<b>399,106.0</b>	<b>399,304.0</b>	<b>543,343.5</b>
ST debt	700.0	758.0	721.0	1,018.2
Other current liabilities	230,237.0	345,576.0	345,243.0	471,046.2
LT debt	2,314.0	2,137.0	1,846.0	2,644.7
Other LT liabilities	1,299.0	1,399.0	1,584.0	2,032.4
Shareholders' equity	44,173.0	48,918.0	49,626.0	66,205.3
Minority interest	328.0	318.0	284.0	396.6
<b>Total liabilities &amp; equity</b>	<b>279,051.0</b>	<b>399,106.0</b>	<b>399,304.0</b>	<b>543,343.5</b>

### KEY METRICS

Year to 31 Dec (%)	2021	2022F	2023F	2024F
<b>Profitability</b>				
EBITDA margin	77.7	76.0	78.9	80.5
Pre-tax margin	70.8	67.7	71.0	72.7
Net margin	59.8	55.1	59.4	61.6
ROA	4.7	3.1	3.4	3.3
ROE	29.5	22.6	27.2	27.2
<b>Growth</b>				
Turnover	9.2	(8.9)	18.4	13.4
EBITDA	11.1	(10.9)	22.9	15.7
Pre-tax profit	11.3	(13.0)	24.2	16.1
Net profit	9.0	(16.1)	27.6	17.5
Net profit (adj.)	9.0	(16.1)	27.6	17.5
EPS	8.1	(16.1)	27.6	17.5
<b>Leverage</b>				
Debt to total capital	6.3	5.6	4.9	5.2
Debt to equity	6.8	5.9	5.2	5.5
Net debt/(cash) to equity	(17.5)	(18.3)	(21.0)	(16.1)
EBITDA margin	77.7	76.0	78.9	80.5

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