

Quarterly Financial Review of the Securities Industry

Intermediaries Supervision Department¹

November 2006

Summary

Overall profitability of the securities industry reduced in the third quarter of 2006 as compared to the preceding quarter primarily due to shrinkage in market turnover.

Overview of the Securities Industry in the Third Quarter of 2006

1. Market turnover slowed down in the third quarter of 2006 as compared to the preceding 3 months. The average SEHK daily turnover shrank by 23% to \$26.3 billion in the third quarter of 2006 from \$34.1 billion in the second quarter of 2006.
2. Table 1 summarizes the securities industry's statistical information and financial highlights for the third quarter of 2006.

As at	30/09/2006	30/06/2006
Total number of securities dealers & securities margin financiers	641	640
Total number of active cash clients ²	685,539	688,256
Total number of active margin clients ²	83,480	77,819
Balance Sheet (HK\$ mn)		
Cash in hand and at bank ³	125,192	120,483
Amounts receivable from margin clients	17,087	17,637
Amounts receivable from clients and other dealers arising from dealing in securities (+27%)	210,958	165,822
Proprietary positions	90,067	94,807
Other assets	147,695	142,675
Total assets (+9%)	590,999	541,424
Amounts payable to clients and other dealers arising from dealing in securities	232,217	228,901
Total borrowings from financial institutions (+53%)	146,488	95,965
Short positions held for own account	41,325	46,737
Other liabilities	75,527	77,051
Total shareholders' fund ⁴ (+3%)	95,442	92,770
Total liabilities and shareholders' fund	590,999	541,424
	3 months to	3 months to
	30/09/2006	30/06/2006
Profit and loss (HK\$ mn)		
Total value of transactions ⁵ (-15%)	6,545,020	7,678,756
Net securities commission income (-25%)	5,650	7,505
Gross interest income	2,597	2,588
Other income ⁶ (-10%)	10,823	12,034
Net profit/ (loss) on proprietary trading	205	(217)
Total overheads and interest expense (+3%)	(15,692)	(15,300)
Net profit for the period (-46%)	3,583	6,610
Remarks:		
¹ The above data were extracted from the monthly Financial Returns submitted in accordance with the Securities and Futures (Financial Resources) Rules by licensed corporations licensed for dealing in securities or securities margin financing. Figures reported by an overseas-incorporated licensed corporation which carries out its principal business activities outside Hong Kong and operates in Hong Kong as a branch office were excluded from the above figures.		
² Active clients are clients for whom the licensed corporation is required to prepare and deliver monthly statement of accounts in respect of the relevant reporting month in accordance with the Securities and Futures (Contract Notes, Statements of Account and Receipts) Rules.		
³ Cash in hand and at bank includes trust monies held on behalf of clients amounting to \$53,048 mn (30/06/2006: \$49,283 mn).		
⁴ The value of shareholders' fund includes value of redeemable shares.		
⁵ Total value of transactions includes trading in equities and bonds both in Hong Kong and overseas.		
⁶ Other income mainly comprises corporate finance income, fund management income, intercompany charges and others.		

¹ The objective of this paper is to provide summary financial data so that those who are interested can use these data for benchmarking, research analysis or other purposes. Observations made in this review should not be taken as definitive market commentaries.

3. Comparing the third quarter end of 2006 with the second quarter end of 2006, balance sheet figures remained relatively stable except for the amounts receivable from clients and other dealers arising from dealing in securities, and the total borrowings from financial institutions. The upsurge in these two items was mainly due to the IPO financing activities during the end of September 2006.
4. As illustrated in Table 1, the net profit of the securities industry almost dropped by half in

the third quarter of 2006 as compared to the preceding quarter. This substantial drop was mainly caused by the contraction in trading activities and the reduction in service fee income from group companies.

Business Performance of SEHK Participants

5. Table 2 summarizes the financial performance of each category of SEHK participants for the third quarter of 2006.

Table 2 – Financial Performance of SEHK Participants for the Third Quarter of 2006 – Breakdown by Different Categories (HK\$ mn)

	Category A*		Category B*		Category C*		All SEHK Participants	
	3 months ended 30/9/2006	3 months ended 30/6/2006	3 months ended 30/9/2006	3 months ended 30/6/2006	3 months ended 30/9/2006	3 months ended 30/6/2006	3 months ended 30/9/2006	3 months ended 30/6/2006
Total value of transactions	2,131,729	2,557,513	1,748,819	2,109,977	641,519	684,075	4,522,067	5,351,565
Total income	3,567	4,775	3,105	3,393	1,405	1,675	8,077	9,843
Salary and staff benefits	(859)	(1,232)	(896)	(791)	(379)	(345)	(2,134)	(2,368)
Other overheads and interest expense	(1,879)	(1,790)	(1,242)	(1,500)	(549)	(587)	(3,670)	(3,877)
Net profit for the period	829	1,753	967	1,102	477	743	2,273	3,598

* Categories A, B and C SEHK participants are identified on a monthly basis, based on their turnover on the SEHK. Category A SEHK participants refer to the top 14 brokers by market turnover, whilst Category B SEHK participants refer to those ranked 15 - 65 and the remainders are grouped under Category C SEHK participants.
Sources: Monthly Financial Returns submitted in accordance with the Securities and Futures (Financial Resources) Rules by securities dealers

6. As shown in Table 2, total value of transactions reported in the third quarter of 2006 decreased by 16% which led to a respective adjustment in the aggregate income of SEHK participants by 18%, as compared to the second quarter of 2006. All categories of SEHK participants experienced a drop in total income, ranging from 8% to 25%, in the third quarter of 2006.
7. Shrinkage in turnover also gave rise to the significant decrease in the profitability of all SEHK participants by 37% in the third quarter of 2006 as compared to preceding quarter. Profitability of Category A brokers was further impacted by the increase in total overheads and interest expense, which resulted in a drop of net profit by more than half in the third quarter of 2006. ■