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CHINA BROKERS & ASSET MANAGERS

Assessing Renewed Regulatory Focus on TRS

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Media reports that the creation of new stock-related cross-border Total Return Swaps (TRS) has been suspended (with existing positions allowed to be closed out but not subject to forced liquidation) have intensified market concerns over disruptions to cross-border business.

We synthesize our recent discussions with companies (see GFS management meeting takeaways), the latest news and financial reporting data, to assess key points of interest:

1. **Cross-border TRS tightening - Not a new variable**. Since the beginning of 2024, cross-border TRS have already been subject to a "no net new additions" constraint, suggesting the current measure is a reinforcement of this rule, specifically for equities; TRS of other assets including FICC are not currently subject to a "no net new additions" restriction.
2. **A look at TRS revenue contribution suggests impact from "no net new additions" restriction is less than 4%**. Using two approaches (details below), we calculate the impact to broker revenue to be in the range of 1% to 4% (the variation is due to different calculation methodologies, as detailed in our estimates).
3. **The key differentiator for individual stocks lies in their Hong Kong business exposure**. **CICC** has a high proportion of its business in Hong Kong and can serve clients without relying on offshore TRS. We maintain that the key drivers for brokers' performance are not TRS or acquiring clients lost by online brokers, but rather the IPO pipeline and recovery of their Hong Kong business.
4. We will continue to monitor for further details around the regulation, such as the specific scope of execution and the range of constraints, and seek to understand the precise impact on individual broker. We maintain our Buy ratings on **CICC-H**, **GFS-A**, and **CITICS-A**.

1. Policy Review: Not a New Variable, but a Reinforcement of the 2024 Framework
A Total Return Swap (TRS) is an OTC derivative. In simple terms, a client (typically a domestic private fund or institution) can gain exposure to an overseas asset via a TRS without physically purchasing the asset or sending principal capital abroad. Instead, the client signs a contract with a broker (or its offshore subsidiary) with a 100% margin requirement. The broker then purchases the underlying asset overseas and, through the contract, transfers the total return (all income and capital gains) and total risk (all losses) of the asset (e.g. a stock) to the client. The client obtains the economic exposure, while the broker earns channel fees and transaction fees (typically at an annualized rate of approximately 1% to 2%, per past averages).

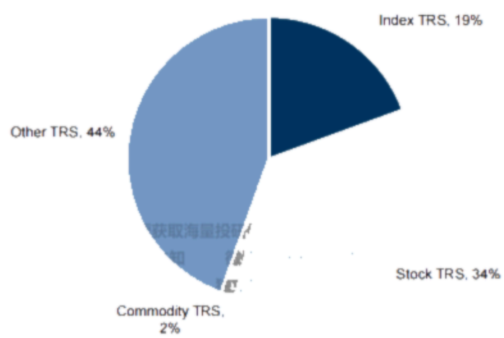
Core regulatory actions concerning cross-border TRS, as reported by media articles include:

- **Scope:** The suspension of new contracts applies only to stock-related cross-border TRS. TRS related to futures, urban investment bonds, as well as some FICC and Northbound trading activities, are not currently included.
- **Execution:** Existing positions can mature or be closed out of, as desired — i.e. there is no forced liquidation, indicating a clear soft landing approach, in our view.
- **Ambiguity:** The industry is still awaiting clarification on whether the final rule will entail prohibiting any net new quota while allowing for adjustments within the existing stock, or mandating the non-renewal of contracts upon their maturity.

While the recent media reports on TRS regulation have raised investor concerns, in reality, in as early as the beginning of 2024, regulators had already strengthened management on the scale of OTC derivatives (options + TRS) through window guidance, proposing a quota constraint of “no net new additions”. The latest move singles out the equities category for further reinforcement — which can be viewed as a continuation of the same policy lineage behind the recent reinforcement of rectification of illegal cross-border business activities at online brokers — with the core objective to block unlicensed offshore operations, curb unauthorized capital outflows and protect domestic investors.

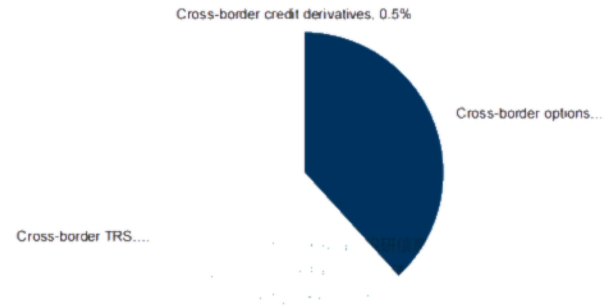
We see two likely reasons for the regulator’s focus on this area: 1) Preventing Circumvention: Following the sharpening of regulatory focus on online brokers, some capital began to flow through private funds, which then used TRS to invest overseas — essentially a loophole for personal fund outflow. 2) Proactive Risk Control: Although TRS require normally 100% margin, they can still have a leverage effect (especially in some structured products), creating scope for a market pullback to set off a sequence effect. As such, regulators appear to be acting preemptively to manage this risk.

Exhibit 1: Broker sector TRS category mix, as of 2023



Source: SAC

Exhibit 2: Broker sector cross-border derivatives mix, as of 2023



Source: SAC

2. What's the Potential Impact on Brokers' Performance?

According to industry estimates from the media, the current outstanding notional principal of cross-border stock TRS is between Rmb 200bn and Rmb 300bn, which is roughly in line with our channel cross-checks. It is important to note that there are two different calculation methodologies in the market, with discrepancies arising mainly from different statistical approaches. We present both in this report (Exhibit 3). This illustrative analysis suggests the revenue contribution from TRS is, at most, in the single digits (1%-4%), implying a relatively limited impact on brokers' operations.

1) Approach 1 (stock basis): This method directly calculates based on the outstanding notional principal. Assuming a midpoint of Rmb 250bn for the outstanding stock and an annualized channel fee rate of 1.5% (within the industry standard range of 1% to 2%), this corresponds to an annual industry revenue of approximately Rmb 3.75bn. When allocated across the nine brokers authorized to conduct cross-border TRS business (with an aggregate group-level revenue of approximately Rmb 338.6bn in 2025), the implied revenue contribution is about 1%.

2) Approach 2 (flow basis): Considering that the average tenor of a TRS is about three months, this implies an annual turnover of 4x. Therefore, an outstanding stock of Rmb 250bn in offshore TRS corresponds to an annual trading flow (or GMV) of Rmb 1tn. If we estimate using a 1.5% fee rate, the annual revenue contribution to the industry would be approximately Rmb 15bn. When allocated across the nine eligible brokers for cross boarder TRS business (with an aggregate 2025 group-level revenue of approximately Rmb 338.6bn), the implied revenue contribution is about 4%.

Exhibit 3: Illustrative review suggests revenue contribution from TRS is, at most, in the single digits (1%-4%), implying that the marginal impact on brokers operations is relatively limited.
Rmb bn (2025)

Rmb bn	
Approach 1: Stock Basis	
Outstanding notional principal of cross-border equity TRS	250
Fee rate	1.5%
Revenue generated	3.75
as % of total revenue of 9 eligible brokers	1%
Approach 2: Flow Basis	
Outstanding notional principal of cross-border equity TRS	250
Average duration of cross-border equity TRS (months)	3
Turnover	4x
Trading flow of cross-border equity TRS	1000
Fee rate	1.5%
Revenue generated	15
as % of total revenue of 9 eligible brokers	4%

Source: SAC, Company data, Goldman Sachs Global Investment Research

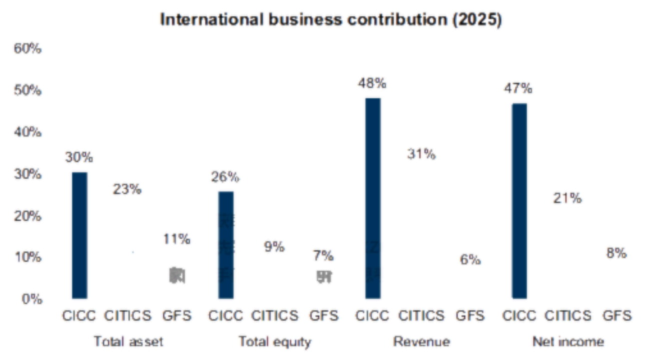
Furthermore, stock-related TRS require a 100% margin, meaning the broker does not bear directional risk in the structure (all floating profits and losses belong to the client) and only collects a channel fee. Therefore implying that even a reduction in this business would not lead to significant impairment losses. Moreover, the ROE for this type of flow-based business has been relatively low. Brokers can achieve higher returns by reallocating these resources to other business, such as their Hong Kong operations.

3. Stock Differentiation: CICC stands out vs. CITIC and GFS; Hong Kong Business Exposure is the Differentiator

CICC's Hong Kong business is a leader in the industry by scale, allowing it to conduct overseas investments directly in Hong Kong. Consequently, its reliance on stock-related cross-border TRS is minimal. Given this, the regulatory tightening has very limited on **CICC**; on the contrary, its Hong Kong business offers the greatest elasticity vs. peers. During a recent CEO meeting, **CICC** mentioned that its offshore subsidiaries are well-resourced and have strong compliance capabilities; and that in the future, a greater share of the cross-border business will likely concentrate among such well-positioned brokers.

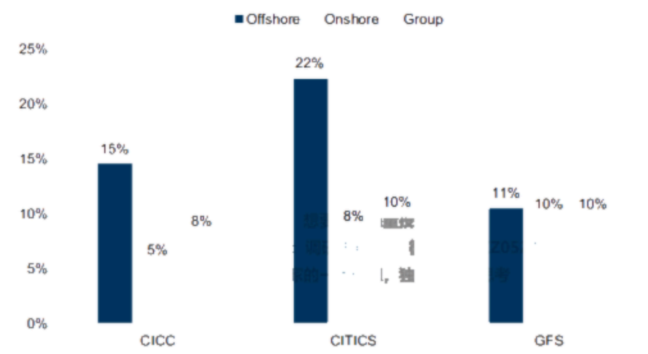
Separately, although CITICS and GFS have completed their capital replenishment and fundamentals behind the logic for their ROE recovery remains intact, the scale of their Hong Kong exposure is smaller than **CICC**'s. As a result, they are relatively more impacted by the reduction in TRS business — i.e. their elasticity as a sector allocation choice is weaker than **CICC**'s.

Exhibit 4: CICC's offshore business contributes the most to both revenue and profit, at over 40%, the highest among covered Chinese brokers, as of 2025



Source: Company data

Exhibit 5: The average ROE for the offshore subsidiaries of the three brokers in our coverage is 16%, compared to the group average level of 9%, as of 2025



Source: Company data, Goldman Sachs Global Investment Research

Some investors have asked whether the regulation of online brokers benefits traditional brokers: We think this is not the case. The retail client base of traditional brokers' Hong Kong brokerage businesses is limited. The client profiles of online brokers do not significantly overlap with those of traditional brokers' Hong Kong clients, and they do not have the infrastructure and operational capability to absorb these clients. The market performance of China broker stocks since May also corroborates this view: they fell for two days after the clampdown on online brokers and only began to reverse course in late June on expectations related to IPOs and the recovery of Hong Kong business exposure.

As we have previously mentioned, we believe the key, sustainable drivers for the outperformance of broker stocks in the next two quarters are two main themes, and not TRS: 1) IPO Pipeline: The anticipated wave of large-scale company listings in the second half of the year would bring substantial contributions from cornerstone investment and co-investment returns. 2) Hong Kong Business Exposure: This includes businesses Hong Kong stock brokerage, and cross-border asset management, which offer higher leverage and ROE compared to domestic business.

Based on this comprehensive analysis, our stock recommendations remain Buy rated **CICC-H**, **GFS-A**, and **CITICS-A**.

4. What Requires Ongoing Monitoring Going Forward?

Finally, given the limited information disclosed in the news, many details will require further observation and confirmation including:

- Execution Specifics: How will the final rules be implemented? Will it be: 1) No net new additions, with adjustments allowed within the existing stock?" or 2) No renewal of contracts upon maturity? The former implies a slower reduction in TRS, while the latter would accelerate the contraction in TRS.
- Scope Expansion to FICC: Currently, only equities are in scope. Howe demand for TRS to invest in offshore bonds (especially in a low-inte environment). It remains to be confirmed whether TRS for futures a investment bonds will be brought under quota management in the f

- Undisclosed Exposure of Individual Brokers: The specific exposures of each broker are not publicly disclosed. We can only make estimates based on industry totals and use the scale of Hong Kong business as an indirect proxy to judge individual differences. **CICC**'s low reliance is relatively certain, but the impact on other brokers cannot be precisely quantified.

Exhibit 6: Broker valuation summary

Price as of Jun 24

Name	Ticker	Price (Local currency)	Rating	Valuation method	Target multiple	Target price (Local currency)	Upside (%)	Net profit growth		Trading PE		Trading PB		Implied PE		Implied PB	
								2026E	2027E	2026E	2027E	2026E	2027E	2026E	2027E	2026E	2027E
Covered companies																	
Brokers (A)																	
CICC-A	601995.SS	34.99	Neutral	12m PE	18.0x	45.72	↑ 31%	24%	1%	14.0x	13.8x	1.2x	1.1x	18.2x	18.0x	1.6x	1.4x
CITICS-A	600030.SS	27.89	Buy	12m PE	16.0x	39.96	↑ 43%	23%	0%	11.2x	11.2x	1.2x	1.1x	16.0x	16.0x	1.7x	1.5x
GFS-A	000776.SZ	22.66	Buy	12m PE	14.0x	32.09	↑ 42%	37%	-5%	9.4x	9.9x	0.9x	0.9x	13.4x	14.0x	1.3x	1.2x
Brokers (H)																	
CICC-H	3908.HK	20.52	Buy	12m PE	11.0x	30.45	↑ 48%	24%	1%	7.5x	7.4x	0.6x	0.6x	11.1x	11.0x	0.9x	0.9x
CITICS-H	6030.HK	27.44	Neutral	12m PE	11.0x	29.95	↑ 9%	23%	0%	10.1x	10.1x	1.0x	1.0x	11.0x	11.0x	1.1x	1.1x
GFS-H	1776.HK	17.07	Neutral	12m PE	8.0x	19.99	↑ 17%	37%	-5%	6.5x	6.8x	0.6x	0.6x	7.6x	8.0x	0.8x	0.7x

Target Price is based on a 12-month basis.

Source: FactSet, Goldman Sachs Global Investment Research

The authors would like to thank Zihan Wang for her contribution to this report.

Price Target Risks and Methodology - CITIC Securities Co.
We are Buy/Neutral on CITICS A/H. Our 12-month target prices of Rmb 39.96/HK$ 29.95 are based on 16x/11x 2027E P/Es.

Downside Risks: 1) further slower revenue growth on weaker capital market, 2) decreasing AUM and take rate of asset management business, 3) slower growth of investment income, 4) more operating expense to keep cost income ratio high.

Upside risks for H share: 1) improving capital market and higher ADTV to drive core business growth, 2) further greater than expected cost savings.

Price Target Risks and Methodology - GFS Co.
We are Buy/Neutral on GFS-A/H. Our 12-month target prices of Rmb 32.09/HK$ 19.99 are based on 14x/8x 2027E P/Es.

Upside risks: 1) improving brokerage fees and IBD income, 2) increasing asset management AUM, 3) more cost savings to support ROE.

Downside risks: 1) weaker-than-expected China capital market, 2) a decrease in AUM and fee rate, 3) higher cost-to-income ratio.

Price Target Risks and Methodology - China International Capital Corp.
We are Buy/Neutral on **CICC-H/CICC-A**. Our 12-month target prices of HK$ 30.45/Rmb 45.72 are based on 11x/18x 2027E P/Es.

Downside risks: 1) weaker-than-expected China capital market, 2) OTC derivative losses, 3) decreased AUM and fee rate, 4) higher cost income ratio.

Upside risks for A shares: 1) improving brokerage fee and IBD income, 2) increasing OTC derivative business and income growth, 3) more cost savings to support ROE.