# China Inc.'s Investment Bank Dives Into Troubled Retail Market

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China International Capital Corp., the investment bank ex-Premier Zhu Rongji set up two decades ago to help restructure the Chinese economy, is again taking on a role that fits with the government's agenda.

CICC's $2.5 billion acquisition of China Investment Securities Corp. will plunge the firm into the retail investor market, a segment it had long shunned because of thin margins and a traditional focus on institutional clients. The deal is part of Chief Executive Officer Bi Mingjian's push to lessen dependence on volatile investment banking fees.

Yet the transaction also ties in with a key objective of the government, which will become CICC's largest shareholder as a result of the purchase. Having used CICC to take some of the largest state companies public since the late 1990s, China is now looking for assistance in its quest to reform a retail-driven equities market that's prone to speculative booms and busts.

In the wake of the latest such episode, a stock market meltdown last year, the government launched an unprecedented crackdown on the securities industry and arrested several high-ranking executives.

"CICC will once again play this civilizing and globalizing role, only with the more far-reaching aim of helping to professionalize the often-shambolic Chinese stock market," said Peter Fuhrman, chairman of China First Capital, a Shenzhen-based advisory firm. “Its reputation is still unsullied in China, unlike other banks whose leaders have been marched out in handcuffs and whose market practices are widely blamed for the rampant speculative fever that often afflicts China’s domestic capital markets.”

## Reforming Role

In announcing the takeover on Friday, CICC hinted at a reforming role by saying the two firms will “work together to improve the quality and efficiency of mass market services” through training and by upgrading technology systems at China Investment Securities’ 192 branches across the country that serve retail clients.

CICC is buying China Investment Securities from state-owned Central Huijin Investment Ltd. It will issue shares to Central Huijin, more than doubling the entity’s stake in CICC to 58.7 percent. CICC had to get a waiver from the Hong Kong Stock Exchange for the transaction, so that Central Huijin’s controlling stake wouldn’t be classified as a reverse takeover.

An additional rationale for the deal is Huijin’s push to consolidate the securities industry by combining institutional and retail brokerage businesses, said Zhang Chunxin, an analyst at CMB International Capital Holdings Corp. She cautioned that “the reform process will be long and gradual.”

China Investment Securities ranked 17th among Chinese securities firms by revenue last year, while CICC was 23rd, according to official data. Bi’s overhaul has the support of the firm’s foreign shareholders, who had already been pushing CICC to diversify into areas such as asset and wealth management, a person with knowledge of the matter said.

Sherry Tan, spokeswoman at CICC, declined to comment.

## Shareholder Backing

The combined stakes of CICC’s main foreign backers -- private equity firms TPG Capital and KKR & Co., and Singapore sovereign wealth fund GIC Pte -- will drop to 15.3 percent as a result of the takeover. However, the foreign firms may buy additional stakes from Central Huijin in future, people familiar with the matter said.

When former premier Zhu Rongji created CICC in 1995, China was launching a shakeup of its state-run industrial sector, leading to the closure of some 60,000 firms and loss of 40 million jobs. Since then, CICC has worked on some of the biggest listings of state enterprises, such as China Construction Bank Corp. and China Mobile Ltd. It was the top adviser on mergers involving Chinese companies in 2014, 2015 and so far this year.

Buying China Investment Securities is a departure from former CEO Levin Zhu’s strategy. The son of the former premier, who ran the firm until two years ago, had long resisted expanding into retail broking, fearing it would erode margins and its differentiation from other Chinese securities firms, according to people familiar with the matter.

Last year's leverage-fueled equities rally and the subsequent implosion brought worldwide attention to the shortcomings of China's markets. The government responded with an effort that included enlisting securities firms in supporting the stock market as well as jailing senior brokerage executives for alleged wrongdoing. CICC wasn't among the firms that took part in the stock-market rescue, but China Investment Securities was.

## Market Manias

China's 114 million individual investors account for the bulk of equities trading. That makes them a hard-to-ignore segment, but also one that tends to be susceptible to market manias. Critics contend that the government's efforts to restore market calm last year only served to hurt investor confidence further.

The Shanghai Composite Index remains 39 percent below its June 2015 peak. Xiao Gang, who was removed from his post as chairman of China's securities regulator this year, in January acknowledged loopholes and ineptitude within the regulatory system.

Some analysts aren't convinced the deal is in CICC's best interest. The stock fell 2.1 percent on Monday after a trading halt was lifted.

The transaction makes the firm "more like a state-owned company, which could compromise CICC's corporate governance, operational autonomy" and its ability to retain top talent, said Fred Hu, Goldman Sachs Group Inc.'s former Greater China chairman.

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