

China Aoyuan Property

All eyes on scale - targeting RMB 73bn contracted sales in 2018

Solid 2017 result, robust growth in net profit, but GPM missed

Solid 2017 result: Revenue surged by 61.6% YoY to RMB 19.1bn. But GPM slightly missed our estimation of 27% and slipped by 1 ppt yoy to 26.7%. Financing cost has surged by 70.2% YoY. Attributable net profit surged by 86% and core attr. net profit increased by 151.0% YoY, in line with our estimation. The company has achieved RMB 45.6 bn contracted sales in 2017, targeting to achieve RMB 73 bn in 2018 and RMB 100 bn in 2019, with 2017-2019 CAGR of 368%. The company has accelerated its land acquisition strategy especially in 2H17 in 3rd tier cities and its balance sheet expands rapidly: total debt increased by 119.6% YoY to RMB 40.4 bn. The company has reduced its equity stake percentage in land acquisition in order to maintain a stable gearing ratio. Net gearing ratio stabilized at 51.0% (50.7% at YE16; 64.3% in 1H17).

Execution is the key to achieve RMB 73bn of 2018 sales target

The company also announced its 2018 contracted sales target of RMB 73bn, which implies a 60% YoY growth. Aoyuan has set its the priority on sales scale. In order to achieve this target, the company had acquired 58 projects (81% via M&A and 71% attributable interest), with 12.86 mn sq.m GFA. Out of these 38 projects were acquired in 3rd tier cities. Saleable resources will provide RMB 166.9bn worth of sales and increase its total saleable resources to approximately RMB 282.3bn (as of Dec-17). The company has significantly reduced its equity stake in new acquisitions in order to leverage up. Equity stake accounted for 71% of land cost in 2017 vs 88% in 1H2017 and 85% in 2016. However, execution will be the key for rapid expansion, especially the expansion with 58 new projects (vs 17 new projects in 2016) in deleverage environment would be challenging.

GPM is expected to be above 25% in next 3 years

We believe Aoyuan will gradually deliver its strong 2015-2017 contracted sales in next three years. We expect gross margin would slightly decline in next 3 years to 26.6%, 26.4% and 26.4% in 2018e-2020e, respectively, mainly due to the rise in land cost and construction cost. As a result, core net profit will grow with the increase of income steadily to be RMB 1.68 bn, 2.38 bn and 3.24 bn in 2018e-2020e, respectively.

Optimizing debt structure in rate-hike environment

In 14 March 2018, the company has announced the club loan of HKD 1.6 bn, including HKD and USD loan. The cost is Hibor+3.95% for HKD loan and Libor+3.95% for USD loan. We believe this should be a proper way to lower its funding cost in current rate-hike environment. As bond supply from Chinese property peers are abundant, funding cost of bond insurance would be costly. We also noticed that the debt due in one year surged from RMB 3.7 bn to RMB 18.2 bn. In addition, cash collection rate dropped to 80% in 2H17 from 86% in 1H17 (90% in YE16)

Revise up price target to HK\$8.10, 13% upside, 'Hold'

We are cautious on property sector in this deaverage environment. Expansion in 3rd tier cities in such a large scale could be challenging in the short term. Moreover, the company has priced in positive factors of Greater Bay and strong 2017 sales growth. We revise up target price to HK\$8.10 and change its rating to 'Hold' from "Buy". Our price target implies 55% discount to Dec-18 NAV, 10.3x 2018e core PE and 7.3x 2019e core PE. The stock is trading at 60% discount to Dec-18 NAV, 9.1x 2018e core PE and 1.3x 2018e PB.

Stock code: 3883.HK
Rating: Hold

| Price target (HK\$) | 8.10 |
|-----------------------------------|--------|
| Previous target(HK\$): | 6.94 |
| Current price (HK\$, 15 Mar 2018) | 7.15 |
| Upside/downside % | 13% |
| Market cap (HK\$ m) | 19,155 |
| Market cap (US\$ m) | 2,443 |
| Avg daily turnover (HK\$ m) | 89.16 |

Source: Bloomberg, AMTD Equity Research

Key forecasts

| (RMB m) | 2017 | 2018e | 2019e | 2020e |
|--------------|--------|--------|--------|--------|
| Revenue | 19,115 | 26,501 | 34,931 | 45,751 |
| yoy % | 61.6% | 38.6% | 31.8% | 31.0% |
| Attr NP | 1,638 | 2,001 | 2,694 | 3,552 |
| yoy % | 86.0% | 22.1% | 34.6% | 31.9% |
| Core Attr NP | 1,386 | 1,687 | 2,380 | 3,238 |
| yoy % | 150.8% | 17.7% | 34.6% | 31.9% |
| Gross margin | 26.7% | 26.6% | 26.4% | 26.4% |
| Net gearing | 51.0% | 50.9% | 40.7% | 34.3% |
| EPS | 0.52 | 0.63 | 0.89 | 1.21 |
| DPS | 0.15 | 0.12 | 0.16 | 0.21 |
| BPS | 3.80 | 4.43 | 5.28 | 6.40 |

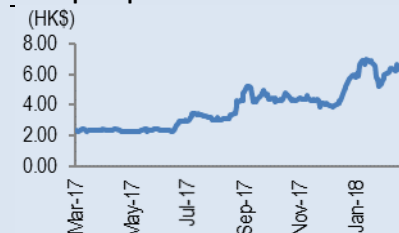
Source: Company data, AMTD Equity Research

Valuation

| | 2017 | 2018e | 2019e | 2020e |
|------------|-------|-------|-------|-------|
| P/E | 11.0 | 9.1 | 6.4 | 4.7 |
| P/BV | 1.5 | 1.3 | 1.1 | 0.9 |
| Div. yield | 2.6% | 2.1% | 2.8% | 3.7% |
| ROE | 17.8% | 18.2% | 20.8% | 22.8% |
| ROA | 1.7% | 1.3% | 1.3% | 1.3% |

Source: Bloomberg, AMTD Equity Research

Share price performance



Source: Bloomberg

Donald Yu
Analyst

+852 3163 3384

Donald.Yu@amtd.com.hk
Michelle Li
Analyst

+852 3163 3383

Michelle.Li@amtd.com.hk

Figure 1: Previous forecast vs actual result

| PnL, RMB '000 | 2016 | 2017 | AMTD 2017E | YoY | Actual vs Est |
|---|----------------|------------------|--------------|--------|---------------|
| Revenue | 11,827,268 | 19,115,255 | 18,127,333 | 61.6% | 5.4% |
| Sales of properties | 11,239,878 | 17,960,391 | 17,481,204 | 59.8% | 2.7% |
| Cost of sales | (8,550,184) | (14,003,778) | (12,998,980) | 63.8% | 7.7% |
| GPM | 28% | 27% | 28% | -3.5% | -5.5% |
| Gross profit | 3,277,084 | 5,111,477 | 5,128,354 | 56.0% | -0.3% |
| Other income | (230,432) | 287,622 | (230,432) | | |
| Fair value gains on investment properties | 309,527 | 336,543 | - | | |
| Selling expenses | (592,275) | (926,166) | (566,422) | 56.4% | 63.5% |
| Administrative expenses | (489,359) | (799,638) | (721,833) | 63.4% | 10.8% |
| Finance costs | (157,419) | (267,859) | (157,419) | 70.2% | 70.2% |
| Profit before tax | 2,084,989 | 3,625,592 | 3,420,110 | 73.9% | 6.0% |
| Income tax expense | (1,078,381) | (1,673,434) | (1,738,106) | 55.2% | -3.7% |
| Profit for the year | 1,006,608 | 1,952,158 | 1,682,005 | 93.9% | 16.1% |
| Adjusted profit for the year | 677,793 | 1,699,751 | 1,556,359 | 150.8% | 9.2% |
| | 18% | | | | |
| <i>Profit for the year attributable to:</i> | | | | | |
| Owners of the Company | 880,962 | 1,638,362 | 1,556,359 | 86.0% | 5.3% |
| Non-controlling interests | 125,646 | 313,796 | 125,646 | 149.7% | 149.7% |
| Core net profit | 552,147 | 1,385,955 | 1,299,366 | 151.0% | 6.7% |
| Net Debt / Equity | 50.7% | 51.0% | 59.7% | 0.2% | -8.7% |
| Current Ratio | 166% | 154% | 141% | -11.9% | 12.3% |
| Interest Coverage | 1.3x | 1.8x | 2.0x | 55.8% | -19.6% |
| ROA | 1.5% | 1.3% | 2.1% | -0.2% | -0.8% |
| ROCE | 2.9% | 3.3% | 4.5% | 0.4% | -1.3% |
| ROE | 7.9% | 17.8% | 16.1% | 9.9% | 1.8% |
| GPM | 27.7% | 26.7% | 28.3% | -1.0% | -1.6% |
| NPM | 7.4% | 8.6% | 8.6% | 1.1% | 0.0% |
| Core NPM | 4.7% | 7.3% | 7.2% | 2.6% | 0.1% |
| Total Debt | 18,380,451 | 40,369,761 | 19,570,876 | 119.6% | 106.3% |
| Cash | 10,956,456 | 26,540,063 | 9,826,517 | 142.2% | 170.1% |
| Net Debt | 7,423,995 | 13,829,698 | 9,744,359 | 86.3% | 41.9% |
| ST Debt | 4,505,888 | 20,489,599 | 8,321,648 | 354.7% | 146.2% |
| Properties held under development | 43,486,574 | 77,069,025 | 62,482,621 | 77.2% | 23.3% |
| Advanced proceeds received from customers | 20,523,884 | 34,760,145 | 35,517,562 | 69.4% | -2.1% |

Source: Company data, AMTD Equity Research

Figure 2: P&L forecast and key ratios

| PnL, RMB mn | | | | | | YoY growth | | | | |
|--|-------------|-------------|--------------|--------------|--------------|------------|--------|-------|-------|-------|
| | 2016 | 2017 | 2018e | 2019e | 2020e | 2016 | 2017 | 2018e | 2019e | 2020e |
| Revenue | 11,827 | 19,115 | 26,501 | 34,931 | 45,751 | 23.6% | 61.6% | 38.6% | 31.8% | 31.0% |
| Sales of properties | 11,240 | 17,960 | 25,231 | 33,533 | 44,214 | | | | | |
| Cost of sales | (8,550) | (14,004) | (19,453) | (25,722) | (33,672) | | | | | |
| Gross profit | 3,277 | 5,111 | 7,048 | 9,209 | 12,078 | 23.8% | 56.0% | 37.9% | 30.6% | 31.2% |
| Selling expenses | (592) | (926) | (1,219) | (1,625) | (2,133) | 21.2% | 56.4% | 31.6% | 33.3% | 31.3% |
| Administrative expenses | (489) | (800) | (1,147) | (1,529) | (2,007) | 21.8% | 63.4% | 43.4% | 33.3% | 31.3% |
| Share of post-tax loss of an associate | - | 0 | 0 | 0 | 0 | | | | | |
| Share of post-tax (losses)/profits of joint ventures | (32) | (116) | (116) | (116) | (116) | | | | | |
| Finance costs | (157) | (268) | (268) | (353) | (644) | 72.1% | 70.2% | 0.0% | 31.9% | 82.1% |
| Profit before tax | 2,085 | 3,626 | 4,298 | 5,585 | 7,178 | 10.6% | 73.9% | 18.6% | 29.9% | 28.5% |
| Income tax expense | (1,078) | (1,673) | (1,983) | (2,577) | (3,312) | | | | | |
| Profit for the year | 1,007 | 1,952 | 2,315 | 3,008 | 3,866 | 10.9% | 93.9% | 18.6% | 29.9% | 28.5% |
| Profit for the year attributable to: | | | | | | | | | | |
| Net profit | 881 | 1,638 | 2,001 | 2,694 | 3,552 | 8.5% | 86.0% | 22.1% | 34.6% | 31.9% |
| Core net profit | 678 | 1,700 | 2,001 | 2,694 | 3,552 | 18.3% | 150.8% | 17.7% | 34.6% | 31.9% |
| Non-controlling interests | 126 | 314 | 314 | 314 | 314 | | | | | |
| Dividends | 245 | 259 | 317 | 426 | 562 | | | | | |
| Special Dividends | - | 142 | - | - | - | | | | | |
| EPS - basic | 0.32 | 0.61 | 0.75 | 1.01 | 1.33 | | | | | |
| EPS-underlying | 0.20 | 0.52 | 0.63 | 0.89 | 1.21 | | | | | |
| DPS - basic | 0.09 | 0.15 | 0.12 | 0.16 | 0.21 | | | | | |
| BVPS | 3.27 | 3.80 | 4.43 | 5.28 | 6.40 | | | | | |
| Key Ratios, RMB mn | 2016 | 2017 | 2018e | 2019e | 2020e | | | | | |
| GPM | 27.7% | 26.7% | 26.6% | 26.4% | 26.4% | | | | | |
| NPM | 7.4% | 8.6% | 7.6% | 7.7% | 7.8% | | | | | |
| Core NPM | 5.7% | 8.9% | 7.6% | 7.7% | 7.8% | | | | | |
| ROA | 1.5% | 1.7% | 1.3% | 1.3% | 1.3% | | | | | |
| ROCE | 2.9% | 3.3% | 2.5% | 2.6% | 2.6% | | | | | |
| ROE | 7.9% | 17.8% | 18.2% | 20.8% | 22.8% | | | | | |
| Total Debt / EBITDA | 8.2x | 10.4x | 13.7x | 13.7x | 16.1x | | | | | |
| Total Debt / Equity | 125.6% | 148.8% | 215.2% | 257.3% | 359.7% | | | | | |
| Total Debt / Capitalization | 55.7% | 59.8% | 68.3% | 72.0% | 78.2% | | | | | |
| Net Debt / EBITDA | 3.3x | 3.6x | 3.2x | 2.2x | 1.5x | | | | | |
| Net Debt / Equity | 50.7% | 51.0% | 50.9% | 40.7% | 34.3% | | | | | |
| Net Debt / Capitalization | 22.5% | 20.5% | 16.1% | 11.4% | 7.5% | | | | | |
| Current Ratio | 165.5% | 153.6% | 180.9% | 177.6% | 187.8% | | | | | |
| Cash / Total Assets | 16.5% | 21.1% | 27.1% | 29.4% | 34.8% | | | | | |
| Inventory / Total Assets | 66.1% | 61.4% | 60.4% | 61.1% | 58.4% | | | | | |
| Net debt / Net Inventory | 16.9% | 17.9% | 13.9% | 9.1% | 6.3% | | | | | |
| Quick Ratio | 135.2% | 118.5% | 129.0% | 123.0% | 120.4% | | | | | |
| Cash Ratio | 30.3% | 35.1% | 51.9% | 54.6% | 67.4% | | | | | |
| Interest Coverage | 1.3x | 1.8x | 2.1x | 2.1x | 1.5x | | | | | |

Source: Company data, AMTD Equity Research

Figure 3: Balance sheet forecast & Cash flow forecast

| Balance Sheet, RMB mn | 2016 | 2017 | 2018e | 2019e | 2020e |
|--|---------|----------|----------|----------|----------|
| Non-current assets | 6,589 | 9,696 | 9,696 | 9,696 | 9,696 |
| Current assets | 59,830 | 116,110 | 166,778 | 223,535 | 317,263 |
| Properties held under development | 43,487 | 77,069 | 106,419 | 142,363 | 190,843 |
| Pledged bank deposits | 486 | 1,771 | 1,771 | 1,771 | 1,771 |
| Bank balances and cash | 10,471 | 24,769 | 46,087 | 66,900 | 112,148 |
| Others | 5,387 | 12,501 | 12,501 | 12,501 | 12,501 |
| Current liabilities | 36,143 | 75,573 | 92,193 | 125,858 | 168,898 |
| Advanced proceeds received from customers | 20,524 | 34,760 | 61,129 | 96,396 | 142,482 |
| Senior note and bond | 1,508 | - | - | - | - |
| Borrowings | 2,997 | 20,490 | 10,741 | 9,139 | 6,093 |
| Others | 11,113 | 20,323 | 20,323 | 20,323 | 20,323 |
| Non-current liabilities | 15,645 | 23,106 | 55,156 | 75,666 | 123,050 |
| Borrowings | 3,795 | 19,880 | 51,929 | 72,440 | 119,823 |
| Senior notes | 10,079 | - | - | - | - |
| Others | 1,770 | 3,226 | 3,226 | 3,226 | 3,226 |
| Capital and reserves | 14,631 | 27,126 | 29,125 | 31,706 | 35,010 |
| Equity attributable to owners of the Company | 8,918 | 10,155 | 11,840 | 14,107 | 17,097 |
| Non-controlling interests | 5,713 | 16,971 | 17,285 | 17,599 | 17,913 |
| Total equity | 14,631 | 27,126 | 29,125 | 31,706 | 35,010 |
| Cash Flow Statement, RMB mn | 2016 | 2017 | 2018e | 2019e | 2019e |
| Operating activities | | | | | |
| Profit before income tax | 2,085 | 3,626 | 4,298 | 5,585 | 7,178 |
| Operating cash flows before movements in working capital | 2,268 | 3,557 | 4,566 | 5,938 | 7,822 |
| Increase in inventories | (26) | 248 | - | - | - |
| Increase in properties for sale | (1,676) | (33,582) | (29,350) | (35,944) | (48,480) |
| Increase in deposits received for sale of properties | 10,012 | 14,236 | 26,369 | 21,261 | 46,086 |
| Cash (used in) from operations | 8,360 | (11,559) | 1,585 | (8,746) | 5,429 |
| PRC Income tax paid | (880) | (1,673) | (1,983) | (2,577) | (3,312) |
| Interest paid | (1,535) | (1,867) | (1,867) | (2,464) | (4,487) |
| Net cash (used in) from operating activities | 5,945 | (15,100) | (2,266) | (13,786) | (2,370) |
| Net cash used in investing activities | (4,069) | (4,179) | - | - | - |
| Financing activities | | | | | |
| New bank and other borrowings raised | 5,245 | 33,577 | 40,465 | 43,656 | 53,476 |
| Repayment of bank and other borrowings | (5,916) | - | (18,165) | (10,741) | (9,139) |
| Net cash from (used in) financing activities | 808 | 33,577 | 23,583 | 34,599 | 47,618 |
| Net increase in cash and cash equivalents | 2,683 | 14,298 | 21,318 | 20,813 | 45,248 |
| Effect of foreign exchange rate changes | 18 | - | - | - | - |
| Cash and cash equivalents at beginning of the year | 7,769 | 10,471 | 24,769 | 46,087 | 66,900 |
| Cash and cash equivalents at end of the year | 10,471 | 24,769 | 46,087 | 66,900 | 112,148 |

Source: Company data, AMTD Equity Research

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| | |
|-------------|---|
| Buy | Stock with potential return of over 20% over the next 12 months |
| Hold | Stock with potential return of -20% to +20% over the next 12 months |
| Sell | Stock with potential loss of over 20% over the next 12 months |

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AMTD Global Markets Limited

Address: 23/F & 25/F, Nexus Building, No. 41 Connaught Road Central, Central, Hong Kong

Tel: (852) 3163-3288 **Fax:** (852) 3163-3289

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