

Country Garden

Sales momentum in lower tier cities continues

Strong sales momentum remains in 1Q18,

Country Garden's sales momentum remains strong in 1Q18. The company has achieved RMB 188 bn of contracted sales in 1Q18, up 25% YoY. Country Garden is still ranking No.1 in terms of contracted sales and contracted GFA, according to CRIC. We expect Country Garden will maintain its strong sales momentum in 1H18, as sufficient saleable resource, mortgage quota and higher home price in lower tier cities comparing with that of last year. However, the company hasn't announced its sales target for 2018. 78% YoY growth of sales in 2017 should be hard to exceed in 2018.

Core net profit surged 123% in 2017; beat our estimates

Topline increased by 48.2% YoY, thanks to the adoption of HKFRS 15, contributing 15% of total revenues. GPM surged from 21.1% in 2016 to 25.9% in 2017. SG&A to contracted sales declined from 4% in 2016 to 3.3% in 2017. Attr. net profit margin surged from 5.8% in 2016 to 8.8% in 2017 while core net profit increased by 123.4% YoY, which beat our estimation by 21%.

Lower tier city strategy to benefit from continued urbanization

The company will keep focusing in lower tier cities with high turnover rate. Satellite cities of 1st tier cities and core locations of 3rd tier cities will be main targets. Besides, the company will accelerate its construction pace by standardize module building method and arranging all designation before land acquisition. In 2018, the company is targeting to complete construction in 12 months, which will accelerate its booking pace as well.

212 mn sq.m of land reserve for future development

Abundant land reserve of Country Garden supports sale growth in future. As of Dec 2017, the company has 212 mn sq.m of land reserve, 28% of which are in Guangdong, 13% in Jiangsu and 9 % in Anhui. In 2017, Country Garden had acquired 14.1 mn sq.m of land reverse in 2017. In terms of GFA, 69%/28% located in 3rd and 2nd tier cities. However, total attr. land consideration in 2017 amounts RMB 327.1 bn, which is about 60% of its 2017 contracted sales.

We expect GPM to be above 20% in next 3 years

We believe the company will deliver over 20% GPM in 2018, as home price surged in 2017 and reducing construction cost by module building method for standard high-rise products. We believe GPM will be 24.3%/24.1%/22.9% in 2018/2019/2020, respectively.

Revise up price target to HK\$17.20, 3% upside, 'HOLD'

We believe Country Garden's penetration in lower tier cities will keep contributing high turnover, while shanty housing redevelopment is still ongoing (5.8 mn units to redevelopment in 2018). And surged home price in lower tier cities also protect the company's margin. However, we believe the home prices in lower tier cities have limited upside potential in the coming two years and this will bring uncertainty to the company's margin from a longer-term perspective. In terms of valuation, we believe the company valuation is high, trading at 9.1x 18 core PE (vs. peers average of 7.4 x 18PE) and 2.2x 18 PB. Therefore, we maintain its rating 'HOLD' and revise up target price to HK\$17.20, due to new acquisitions are added to updated NAV. Our price target implies 50% discount to Dec-18 NAV, 9.4x 2018e core PE and 6.6x 2019e core PE. The stock is trading at 52% discount to Dec-18 NAV, 9.1x 2018e core PE and 2.2x 2018e PB.

Stock code: 2007.HK
Rating: HOLD
Price target (HK\$) 17.20

Previous target(HK\$): 11.20

Current price (HK\$, 12 Apr 2018) 16.70

Upside/downside % 3%

Market cap (HK\$ m) 363,056

Market cap (US\$ m) 46,250

Avg daily turnover (HK\$ m) 862.8

Source: Bloomberg, AMTD Equity Research

Key forecasts

| (RMB m) | 2017 | 2018e | 2019e | 2020e |
|--------------|---------|---------|---------|---------|
| Revenue | 226,900 | 355,376 | 464,967 | 587,772 |
| yoy % | 48% | 57% | 31% | 26% |
| Attr NP | 26,064 | 33,856 | 46,698 | 56,151 |
| yoy % | 126.3% | 29.9% | 37.9% | 20.2% |
| Core Attr NP | 19,929 | 31,167 | 44,010 | 53,462 |
| yoy % | 123% | 56% | 41% | 21% |
| Gross margin | 25.9% | 24.3% | 24.1% | 22.9% |
| Net gearing | 56.9% | 44.4% | 26.3% | 16.2% |
| EPS | 0.94 | 1.47 | 2.07 | 2.52 |
| DPS | 0.15 | 0.20 | 0.27 | 0.33 |
| BPS | 4.41 | 6.01 | 8.21 | 10.85 |

Source: Company data, AMTD Equity Research

Valuation

| | 2017 | 2018e | 2019e | 2020e |
|------------|-------|-------|-------|-------|
| P/E | 14.2 | 9.1 | 6.4 | 5.3 |
| P/BV | 3.0 | 2.2 | 1.6 | 1.2 |
| Div. yield | 1.1% | 1.5% | 2.0% | 2.4% |
| ROE | 22.4% | 22.1% | 23.1% | 21.5% |
| ROA | 2.5% | 3.1% | 4.0% | 4.9% |

Source: Bloomberg, AMTD Equity Research

Share price performance


Source: Bloomberg

Donald Yu, Analyst

+852 3163 3385

Donald.Yu@amtdgroup.com
Max Liang, Analyst

+852 3163 3384

Max.Liang@amtdgroup.com
Michelle Li, Analyst

+852 3163 3383

Michelle.Li@amtdgroup.com

Figure 1: Previous forecast vs actual result

| PnL, RMB '000 | 2016 | 2017 | AMTD 2017E | YoY | Actual vs Est |
|---|---------------|---------------|---------------|----------|---------------|
| Revenue | 153,086,977 | 226,899,786 | 193,557,711 | 48.2% | 17.2% |
| Sales of properties | 148,180,135 | 220,157,369 | 192,193,548 | 48.6% | 14.5% |
| Cost of sales | (120,850,891) | (168,114,404) | (151,068,778) | 39.1% | 11.3% |
| GPM | 21.1% | 25.9% | 22.0% | 4.9 pts | 4.0 pts |
| Gross profit | 32,236,086 | 58,785,382 | 42,488,933 | 82.4% | 38.4% |
| Other income | 1,530,465 | 2,611,495 | 1,530,465 | 70.6% | 70.6% |
| Fair value gains on investment properties | 711,604 | 504,718 | - | -29.1% | n.a. |
| Selling expenses | (7,383,618) | (10,002,400) | (11,220,000) | 35.5% | -10.9% |
| Administrative expenses | (4,970,364) | (8,301,008) | (6,120,000) | 67.0% | 35.6% |
| Finance costs | (1,095,305) | 3,276,086 | (1,085,872) | -399.1% | -401.7% |
| Profit before tax | 21,390,572 | 46,521,969 | 25,955,230 | 117.5% | 79.2% |
| Income tax expense | (7,727,349) | (17,770,164) | (8,014,976) | 130.0% | 121.7% |
| Profit for the year | 13,663,223 | 28,751,805 | 17,940,254 | 110.4% | 60.3% |
| Adjusted profit for the year | 11,066,953 | 22,617,738 | 17,203,380 | 104.4% | 31.5% |
| Profit for the year attributable to: | | | | | |
| Owners of the Company | 11,516,815 | 26,063,518 | 17,203,380 | 126.3% | 51.5% |
| Non-controlling interests | 736,874 | 2,688,287 | 736,874 | 264.8% | 264.8% |
| Core net profit | 8,920,545 | 19,929,451 | 16,466,506 | 123.4% | 21.0% |
| Net Debt / Equity | 49% | 57% | 39% | 8.3 pts | 18.0 pts |
| Current Ratio | 120% | 113% | 119% | -6.8 pts | -6.7 pts |
| Interest Coverage | 6.0x | 6.6x | 7.3x | 0.6x | nm |
| ROA | 1.95% | 2.48% | 2.38% | 0.5 pts | 0.1 pts |
| ROCE | 5.80% | 9.21% | 7.34% | 3.4 pts | 1.9 pts |
| ROE | 14.11% | 22.35% | 17.28% | 8.2 pts | 5.1 pts |
| GPM | 21.06% | 25.91% | 21.95% | 4.9 pts | 4.0 pts |
| NPM | 7.52% | 11.49% | 8.89% | 4.0 pts | 2.6 pts |
| Core NPM | 5.83% | 8.78% | 8.51% | 3.0 pts | 0.3 pts |
| Total Debt | 136,196,876 | 214,765,027 | 134,911,679 | 57.7% | 59.2% |
| Cash | 96,490,887 | 148,402,122 | 96,165,500 | 53.8% | 54.3% |
| Net Debt | 39,705,989 | 66,362,905 | 38,746,179 | 67.1% | 71.3% |
| ST Debt | 30,512,725 | 47,671,787 | 34,506,334 | 56.2% | 38.2% |
| Properties held under development | 216,383,252 | 360,921,992 | 347,170,148 | 66.8% | 4.0% |
| Advanced proceeds received from customers | 192,408,932 | 346,747,257 | 306,215,384 | 80.2% | 13.2% |

Source: Company data, AMTD Equity Research

Figure 2: P&L forecast and key ratios

| PnL, RMB mn | 2016 | 2017 | 2018e | 2019e | 2020e | 2017 | 2018e | 2019e | 2020e |
|--|---------------|---------------|---------------|----------------|----------------|--------------|---------------|--------------|--------------|
| Revenue | 153,087 | 226,900 | 355,376 | 464,967 | 587,772 | 35.2% | 48.2% | 56.6% | 30.8% |
| Sales of properties | 148,180 | 220,157 | 348,392 | 457,718 | 580,231 | | | | |
| Cost of sales | (120,851) | (168,114) | (268,952) | (352,692) | (453,004) | | | | |
| Gross profit | 32,236 | 58,785 | 86,424 | 112,276 | 134,767 | 41.0% | 82.4% | 47.0% | 29.9% |
| Selling expenses | (7,384) | (10,002) | (13,219) | (15,202) | (18,395) | 57.5% | 35.5% | 32.2% | 15.0% |
| Administrative expenses | (4,970) | (8,301) | (11,897) | (13,682) | (16,722) | 53.9% | 67.0% | 43.3% | 15.0% |
| Share of post-tax loss of an associate | 362 | (352) | (352) | (352) | (352) | | | | |
| Share of post-tax (losses)/profits of joint ventures | - | - | - | - | - | | | | |
| Finance costs | (1,095) | 3,276 | (640) | (610) | (593) | -15.1% | -399.1% | -119.5% | -4.7% |
| Profit before tax | 21,391 | 46,522 | 62,926 | 85,041 | 101,317 | | | | |
| Income tax expense | (7,727) | (17,770) | (26,382) | (35,654) | (42,478) | 50.9% | 130.0% | 48.5% | 35.1% |
| Profit for the year | 13,663 | 28,752 | 36,544 | 49,387 | 58,839 | 40.7% | 110.4% | 27.1% | 35.1% |
| Profit for the year attributable to: | | | | | | | | | |
| Net profit | 11,517 | 26,064 | 33,856 | 46,698 | 56,151 | 24.2% | 126.3% | 29.9% | 37.9% |
| Core net profit | 11,067 | 22,618 | 33,856 | 46,698 | 56,151 | 27.3% | 104.4% | 49.7% | 37.9% |
| Non-controlling interests | 737 | 2,688 | 2,688 | 2,688 | 2,688 | | | | |
| Perpetual capital securities | 1,410 | - | - | - | - | | | | |
| Dividends | 3,734 | 3,205 | 4,164 | 5,743 | 6,906 | | | | |
| EPS - basic | 0.52 | 1.23 | 1.60 | 2.20 | 2.65 | | | | |
| EPS-underlying | 0.40 | 0.94 | 1.47 | 2.07 | 2.52 | | | | |
| DPS - basic | 0.17 | 0.15 | 0.20 | 0.27 | 0.33 | | | | |
| NAV per share | 3.18 | 4.41 | 6.01 | 8.21 | 10.85 | | | | |
| Key Ratios, RMB mn | 2016 | 2017 | 2018e | 2019e | 2020e | | | | |
| GPM | 21.1% | 25.9% | 24.3% | 24.1% | 22.9% | | | | |
| NPM | 7.5% | 11.5% | 9.5% | 10.0% | 9.6% | | | | |
| Core NPM | 5.8% | 8.8% | 8.8% | 9.5% | 9.1% | | | | |
| ROA | 1.9% | 2.5% | 3.1% | 4.0% | 4.9% | | | | |
| ROCE | 5.8% | 9.5% | 9.6% | 11.5% | 11.9% | | | | |
| ROE | 14.1% | 22.4% | 22.1% | 23.1% | 21.5% | | | | |
| Total Debt / EBITDA | 5.9x | 5.0x | 3.5x | 2.7x | 2.4x | | | | |
| Total Debt / Equity | 166.9% | 184.2% | 145.2% | 113.9% | 95.3% | | | | |
| Total Debt / Capitalization | 62.5% | 64.8% | 59.2% | 53.3% | 48.8% | | | | |
| Net Debt / EBITDA | 1.7x | 1.5x | 1.1x | 0.6x | 0.4x | | | | |
| Net Debt / Equity | 48.7% | 56.9% | 44.4% | 26.3% | 16.2% | | | | |
| Net Debt / Capitalization | 18.2% | 20.0% | 18.1% | 12.3% | 8.3% | | | | |
| Current Ratio | 119.6% | 112.8% | 126.1% | 134.0% | 153.4% | | | | |
| Cash / Total Assets | 16.3% | 14.1% | 14.1% | 15.4% | 17.9% | | | | |
| Inventory / Total Assets | 51.0% | 46.9% | 48.7% | 49.2% | 46.6% | | | | |
| Net debt / Net Inventory | 13.2% | 13.5% | 12.7% | 9.4% | 7.9% | | | | |
| Quick Ratio | 95.8% | 93.5% | 104.9% | 109.6% | 120.8% | | | | |
| Cash Ratio | 23.8% | 19.3% | 21.3% | 24.4% | 32.7% | | | | |
| Interest Coverage | 6.0x | 6.6x | 9.4x | 12.2x | 13.4x | | | | |

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 | 106,736 | 181,754 | 181,754 | 181,754 | 181,754 |
| Current assets | 484,836 | 867,915 | 916,242 | 972,349 | 971,053 |
| Properties under development | 216,383 | 360,922 | 400,253 | 433,363 | 402,712 |
| Completed properties held for sale | 30,885 | 27,886 | 30,885 | 30,885 | 30,885 |
| Restricted cash | 11,844 | 11,318 | 11,318 | 11,318 | 11,318 |
| Cash and cash equivalents | 84,647 | 137,084 | 143,080 | 166,078 | 195,432 |
| Others | 141,076 | 330,705 | 330,705 | 330,705 | 330,705 |
| Current liabilities | 405,314 | 769,537 | 726,558 | 725,595 | 632,913 |
| Advanced proceeds received from customers | 192,409 | 346,747 | 350,915 | 349,259 | 270,697 |
| Corporate bonds | 8,207 | 16,814 | - | - | - |
| Bank and other borrowings | 30,513 | 47,672 | 21,135 | 21,827 | 7,708 |
| Others | 174,185 | 358,303 | 354,508 | 354,508 | 354,508 |
| Non-current liabilities | 104,642 | 163,521 | 218,282 | 225,965 | 258,512 |
| Bank and other borrowings | 97,477 | 146,484 | 201,245 | 208,928 | 241,475 |
| Others | 7,166 | 17,037 | 17,037 | 17,037 | 17,037 |
| Capital and reserves | 81,615 | 116,612 | 153,156 | 202,543 | 261,382 |
| Equity attributable to owners of the Company | 70,128 | 93,671 | 127,526 | 174,225 | 230,375 |
| Perpetual capital instruments | - | - | - | - | - |
| Non-controlling interests | 11,487 | 22,941 | 25,630 | 28,318 | 31,006 |
| Cash Flow Statement, RMB mn | 2016 | 2017e | 2018e | 2019e | 2020e |
| Profit for the year | 13,663 | 28,752 | 36,544 | 49,387 | 58,839 |
| Operating cash flows before movements in working capital | 20,898 | 46,522 | 62,926 | 85,041 | 101,317 |
| Property under development and completed properties held for sale | (43,516) | (188,038) | (42,330) | (33,109) | 30,650 |
| Advanced proceeds received from customers | 88,294 | 154,338 | 4,168 | (1,656) | (78,562) |
| Cash (used in) from operations | 57,303 | 183,824 | 24,764 | 50,275 | 53,405 |
| PRC Income tax paid | (9,919) | (17,770) | (26,382) | (35,654) | (42,478) |
| Interest paid | (6,121) | (10,736) | (9,877) | (9,277) | (8,931) |
| Net cash (used in) from operating activities | 41,263 | 155,317 | (11,495) | 5,344 | 1,996 |
| Net cash used in investing activities | (20,457) | (56,166) | - | - | - |
| Financing activities | | | | | |
| New bank and other borrowings raised | 36,536 | 37,435 | 42,121 | 29,511 | 40,255 |
| Repayment of bank and other borrowings | (20,507) | (38,720) | (34,506) | (21,135) | (21,827) |
| Net cash from (used in) financing activities | 27,454 | (46,715) | 17,491 | 17,653 | 27,358 |
| Net increase in cash and cash equivalents | 48,260 | 52,437 | 5,996 | 22,997 | 29,354 |
| Effect of foreign exchange rate changes | 147 | - | - | - | - |
| Cash and cash equivalents at beginning of the year | 36,241 | 84,647 | 137,084 | 143,080 | 166,078 |
| Cash and cash equivalents at end of the year | 84,647 | 137,084 | 143,080 | 166,078 | 195,432 |

Source: Company data, AMTD Equity Research

IMPORTANT DISCLOSURES

AMTD Investment Ratings

Stock Rating

| | |
|-------------|---|
| 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 |

Analyst Certification

We, Donald Yu, Max Liang and Michelle Li, hereby certify that (i) all of the views expressed in this research report reflect accurately our personal views about the subject company or companies and its or their securities; and (ii) no part of our compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed by us in this research report, nor is it tied to any specific investment banking transactions performed by AMTD Global Markets Limited.

AMTD Global Markets Limited

Address: 23/F & 25/F, Nexxus Building, No. 41 Connaught Road Central, Central, Hong Kong
Tel: (852) 3163-3288 **Fax:** (852) 3163-3289

GENERAL DISCLOSURES

The research report is prepared by AMTD Global Markets Limited ("AMTD") and is distributed to its selected clients.

This research report provides general information only and is not to be construed as an offer to sell or a solicitation of an offer to buy any security in any jurisdiction where such offer or solicitation would be illegal. It does not (i) constitute a personal advice or recommendation, including but not limited to accounting, legal or tax advice, or investment recommendations; or (ii) take into account any specific clients' particular needs, investment objectives and financial situation. AMTD does not act as an adviser and it accepts no fiduciary responsibility or liability for any financial or other consequences. This research report should not be taken in substitution for judgment to be exercised by clients. Clients should consider if any information, advice or recommendation in this research report is suitable for their particular circumstances and seek legal or professional advice, if appropriate.

This research report is based on information from sources that we considered reliable. We do not warrant its completeness or accuracy except with respect to any disclosures relative to AMTD and/or its affiliates. The value or price of investments referred to in this research report and the return from them may fluctuate. Past performance is not reliable indicator to future performance. Future returns are not guaranteed and a loss of original capital may occur.

The facts, estimates, opinions, forecasts and any other information contained in the research report are as of the date hereof and are subject to change without prior notification. AMTD, its group companies, or any of its or their directors or employees ("AMTD Group") do not represent or warrant, expressly or impliedly, that the information contained in the research report is correct, accurate or complete and it should not be relied upon. AMTD Group will accept no responsibilities or liabilities whatsoever for any use of or reliance upon the research report and its contents.

This research report may contain information from third parties, such as credit ratings from credit ratings agencies. The reproduction and redistribution of the third party content in any form by any means is forbidden except with prior written consent from the relevant third party. Third party content providers do not guarantee the timeliness, completeness, accuracy or availability of any information. They are not responsible for any errors or omissions, regardless of the cause, or for the results obtained from the use of such content. Third party content providers give no express or implied warranties, including, but not limited to, any warranties of merchantability of fitness for a particular purpose or use. Third party content providers shall not be liable for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including lost income or profits and opportunity costs) in connection with any use of their content. Credit ratings are statements of opinions and are not statements of fact or recommendations to purchase, hold or sell securities. They do not address the suitability of securities for investment purposes, and should not be relied on as investment advice.

To the extent allowed by relevant and applicable law and/or regulation: (i) AMTD, and/or its directors and employees may deal as principal or agent, or buy or sell, or have long or short positions in, the securities or other instruments based thereon, of issuers or securities mentioned herein; (ii) AMTD may take part or make investment in financing transactions with, or provide other services to or solicit business from issuer(s) of the securities mentioned in the research report; (iii) AMTD may make a market in the securities in respect of the issuer mentioned in the research report; (iv) AMTD may have served as manager or co-manager of a public offering of securities for, or currently may make a primary market in issues of, any or all of the entities mentioned in this research report or may be providing, or have provided within the previous 12 months, other investment banking services, or investment services in relation to the investment concerned or a related investment.

AMTD controls information flow and manages conflicts of interest through its compliance policies and procedures (such as, Chinese Wall maintenance and staff dealing monitoring).

The research report is strictly confidential to the recipient. No part of this research report may be reproduced or redistributed in any form by any means to any other person without the prior written consent of AMTD Global Markets Limited.