

R&F properties

High growth but higher gearing

Solid 2017 result, core net profit grew by 107% YoY

R&F achieved RMB 81.9 bn contracted sales in 2017, up by 35% YoY. The company set a 60% contracted sales growth target in 2018 and RMB 300 bn in 2020 which implies 54% CAGR in 2017-2020. Overall 2017 results are solid: revenue slightly improved by 10.3% YoY to RMB 59.3bn. Thanks to GPM growing by 7.1 pts to 35%, gross profit surged by 38% YoY. SG&A surged by 34%, which was close to 2017 sales growth of 35%. Profit for the year increased by 204% YoY, as one-off RMB 13.1 bn gain on bargaining purchase from acquisition of Wanda asset. Attr. core net profit surged by 100% to RMB 11 bn, representing core NPM of 18%. Booking ASP increased in 2017 pushed GPM improving and net profit enhancement. However, we have more concerns on R&F's balance sheet: 1) net gearing went even higher to 170% while contacted sales increased by 35%; cash and cash equivalent declined by 30% to only RMB 32 bn at YE17; 2) net debt surged by 47% to RMB 110 bn at YE17; 3) advanced proceeds received from customers amounted to only RMB 29 bn.

RMB 300 bn of sales target in 2020 implying 54% CAGR in 2017-2020

Following peers, R&F sets a 60% growth of contracted sales in 2018 and targets to RMB 130 bn/ 200 bn/ 300bn in 2018/2019/2020. The company will launch RMB 240 bn of saleable resource, 45%/55% in 1H/2H 2018, respectively. Among RMB 240 saleable resource, RMB 170 bn are new launches or new phases of existing projects. The company will launch 103 projects amounting within RMB 1 bn in terms of projects size to boost its sell-through rate. We noticed that the company would target to achieve RMB 3.5 bn/ 3.3 bn/ 3.1 bn in Jiangxi/Liaoning and Anhui, where only RMB 396 mn/ 772 mn & nil sales achieved in last year, respectively. We believe shanty housing redevelopment had helped destocking in these provinces in 2017. However, R&F's execution should be the key to achieve targets in these provinces.

Plan to reduce Capex for land acquisition in 2018

The company has sufficient saleable resource to support its sales target and will be cautious about the land market in 2018. We believe the company will reduce its Capex for land acquisitions in 2018, at least less than the RMB 584 bn in 2017. However, balance sheet expansion is unavoidable to achieve its aggressive 2020 target. In uptrend of funding costing and in a deleverage environment, it would be risky with abundant debts and high gearing.

We expect GPM to be above 30% in 2018

We believe the company will deliver over 30% GPM in next 3 years, as home price surged in last 2 years and relatively low cost of existing projects. The company plans to deliver 6.5 mn sq.m in 2018. We estimate booking ASP in 2018 will be around 12,500 per sq.m, which is close to 2016 contracted sales ASP. We expect GPM will be 34.5%/33.6%/33.1% in 2018/2019/2020, respectively.

Revise up price target to HK\$23.89, 14% upside, 'Hold'

We are cautious on property sector in this deaveraging environment. Rapid expansion strategy in the short term could be high uncertain. Moreover, high net gearing ratio is still a concern in the deleveraging environment. We maintain 'hold' rating and revise up target price to HK\$23.89 (due to inclusion of new projects in our NAV). Our price target implies 40% discount to Dec-18 NAV, 5.2x 2018e core PE and 4.1x 2019e core PE. The stock is trading at 47% discount to Dec-18 NAV, 4.6x 2018e core PE and 0.8x 2018e PB.

Stock code: 2777.HK
Rating: Hold

| Price target (HK\$) | 23.89 |
|-----------------------------------|--------|
| Previous target(HK\$): | 21.07 |
| Current price (HK\$, 20 Mar 2018) | 20.90 |
| Upside/downside % | 14% |
| Market cap (HK\$ m) | 67,347 |
| Market cap (US\$ m) | 8,586 |
| Avg daily turnover (HK\$ m) | 181.3 |

Source: Bloomberg, AMTD Equity Research

Key forecasts

| (RMB m) | 2017 | 2018e | 2019e | 2020e |
|--------------|--------|--------|--------|---------|
| Revenue | 59,278 | 80,829 | 97,409 | 118,174 |
| yoy % | 10% | 36% | 21% | 21% |
| Attr NP | 21,186 | 13,197 | 17,030 | 19,473 |
| yoy % | 214% | -38% | 29% | 14% |
| Core Attr NP | 10,770 | 13,197 | 17,030 | 19,473 |
| yoy % | 100% | 22% | 29% | 14% |
| Gross margin | 35.4% | 34.5% | 33.6% | 33.1% |
| Net gearing | 169.6% | 132.6% | 121.6% | 109.5% |
| EPS | 3.34 | 4.10 | 5.28 | 6.04 |
| DPS | 1.10 | 0.69 | 0.88 | 1.01 |
| BPS | 19.10 | 23.19 | 28.48 | 34.52 |

Source: Company data, AMTD Equity Research

Valuation

| | 2017 | 2018e | 2019e | 2020e |
|------------|-------|-------|-------|-------|
| P/E | 5.6 | 4.6 | 3.6 | 3.1 |
| P/BV | 1.0 | 0.8 | 0.7 | 0.5 |
| Div. yield | 5.8% | 3.6% | 4.7% | 5.4% |
| ROE | 20.9% | 19.7% | 20.7% | 19.4% |
| ROA | 7.1% | 4.0% | 4.6% | 4.5% |

Source: Bloomberg, AMTD Equity Research

Share price performance



Source: Bloomberg

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Figure 1: Previous forecast vs actual result

| PnL, RMB '000 | 2016 | 2017 | AMTD 2017E | YoY | Actual vs Est |
|---|-------------|-------------|-------------|-----------|---------------|
| Revenue | 53,730,339 | 59,277,855 | 60,654,903 | 10.3% | -2.3% |
| Sales of properties | 49,489,281 | 53,709,393 | 55,770,786 | 8.5% | -3.7% |
| Cost of sales | -38,543,599 | -38,315,554 | -42,284,335 | -0.6% | -9.4% |
| GPM | 28% | 35% | 30% | 7.1 pts | 5.1 pts |
| Gross profit | 15,186,740 | 20,962,301 | 18,370,568 | 38.0% | 14.1% |
| Other income | 516,394 | 544,376 | 516,394 | 5.4% | 5.4% |
| Fair value gains on investment properties | 1,740,812 | 780,672 | 0 | -55.2% | n.a. |
| Selling expenses | -1,315,362 | -1,814,776 | -1,729,033 | 38.0% | 5.0% |
| Administrative expenses | -2,672,863 | -3,526,982 | -4,000,000 | 32.0% | -11.8% |
| Finance costs | -2,367,045 | -1,672,979 | -2,334,011 | -29.3% | -28.3% |
| Profit before tax | 11,868,840 | 28,475,020 | 11,688,532 | 139.9% | 143.6% |
| Income tax expense | -4,812,823 | -7,050,765 | -4,726,194 | 46.5% | 49.2% |
| Profit for the year | 7,056,017 | 21,424,255 | 6,962,338 | 203.6% | 207.7% |
| Adjusted profit for the year | 5,505,830 | 11,008,081 | 6,662,229 | 99.9% | 65.2% |
| Profit for the year attributable to: | | | | | |
| Owners of the Company | 6,755,908 | 21,186,451 | 6,662,229 | 213.6% | 218.0% |
| Non-controlling interests | 26,166 | 94,237 | 26,166 | 260.2% | 260.2% |
| Core net profit | 5,205,721 | 10,770,277 | 6,936,172 | 106.9% | 55.3% |
| Net Debt / Equity | 160% | 170% | 115% | 9.7 pts | 54.8 pts |
| Current Ratio | 204% | 190% | 239% | -14.3 pts | -49.4 pts |
| Interest Coverage | 6.2x | 11.0x | 6.2x | 4.7x | 4.8x |
| ROA | 2.98% | 7.11% | 2.84% | 4.1 pts | 4.3 pts |
| ROCE | 4.03% | 10.23% | 4.10% | 6.2 pts | 6.1 pts |
| ROE | 13.03% | 17.50% | 13.75% | 7.9 pts | 7.2 pts |
| GPM | 28.26% | 35.36% | 30.29% | 7.1 pts | 5.1 pts |
| NPM | 12.57% | 35.74% | 10.98% | 23.2 pts | 24.8 pts |
| Core NPM | 10.25% | 18.17% | 11.44% | 8.3 pts | 7.1 pts |
| Total Debt | 120,852,084 | 142,243,833 | 108,807,524 | 17.7% | 30.7% |
| Cash | 45,969,082 | 32,214,749 | 47,394,340 | -29.9% | -32.0% |
| Net Debt | 74,883,002 | 110,029,084 | 61,413,184 | 46.9% | 79.2% |
| ST Debt | 33,681,918 | 28,414,422 | 6,604,231 | -15.6% | 330.2% |
| Properties held under development | 81,134,542 | 110,865,723 | 88,342,278 | 36.6% | 25.5% |
| Advanced proceeds received from customers | 19,546,810 | 29,058,143 | 32,976,024 | 48.7% | -11.9% |

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 | 53,730 | 59,278 | 80,829 | 97,409 | 118,174 | 21.3% | 10.3% | 36.4% | 20.5% | 21.3% |
| Sales of properties | 49,489 | 53,709 | 70,123 | 86,456 | 112,080 | 21.5% | 8.5% | 30.6% | 23.3% | 29.6% |
| Cost of sales | (38,544) | (38,316) | (52,977) | (64,642) | (79,087) | | | | | |
| Gross profit | 15,187 | 20,962 | 27,853 | 32,767 | 39,087 | 6.9% | 38.0% | 32.9% | 17.6% | 19.3% |
| Selling expenses | (1,315) | (1,815) | (2,659) | (2,400) | (3,300) | 46.7% | 38.0% | 46.5% | -9.7% | 37.5% |
| Administrative expenses | (2,673) | (3,527) | (5,168) | (5,600) | (7,700) | 10.9% | 32.0% | 46.5% | 8.4% | 37.5% |
| Share of post-tax loss of an associate | 844 | (33) | (37) | (40) | (44) | | | | | |
| Share of post-tax (losses)/profits of joint ventures | (64) | 128 | 128 | 128 | 128 | | | | | |
| Finance costs | (2,367) | (1,673) | (2,819) | (2,466) | (2,537) | 9.9% | -29.3% | 68.5% | -12.5% | 2.9% |
| Profit before tax | 11,869 | 28,475 | 17,843 | 22,933 | 26,178 | 2.4% | 139.9% | -37.3% | 28.5% | 14.1% |
| Income tax expense | (4,813) | (7,051) | (4,408) | (5,666) | (6,467) | | | | | |
| Profit for the year | 7,056 | 21,424 | 13,435 | 17,268 | 19,710 | 5.1% | 203.6% | -37.3% | 28.5% | 14.1% |
| Profit for the year attributable to: | | | | | | | | | | |
| Net profit | 6,756 | 21,186 | 13,197 | 17,030 | 19,473 | 20.3% | 213.6% | -37.7% | 29.0% | 14.3% |
| Core net profit | 5,206 | 10,770 | 13,197 | 17,030 | 19,473 | 36.1% | 106.9% | 22.5% | 29.0% | 14.3% |
| Non-controlling interests | 274 | 144 | 144 | 144 | 144 | | | | | |
| Dividends | 26 | 94 | 94 | 94 | 94 | | | | | |
| Special Dividends | 2,083 | 3,545 | 2,208 | 2,849 | 3,258 | | | | | |
| EPS - basic | 2.10 | 6.57 | 4.10 | 5.28 | 6.04 | | | | | |
| EPS-underlying | 1.62 | 3.34 | 4.10 | 5.28 | 6.04 | | | | | |
| DPS - basic | 0.65 | 1.10 | 0.69 | 0.88 | 1.01 | | | | | |
| BVPS | 13.61 | 19.10 | 23.19 | 28.48 | 34.52 | | | | | |
| Key Ratios, RMB mn | 2016 | 2017 | 2018e | 2019e | 2020e | | | | | |
| GPM | 28.3% | 35.4% | 34.5% | 33.6% | 33.1% | | | | | |
| NPM | 12.6% | 35.7% | 16.3% | 17.5% | 16.5% | | | | | |
| Core NPM | 10.2% | 18.6% | 16.6% | 17.7% | 16.7% | | | | | |
| ROA | 3.0% | 7.1% | 4.0% | 4.6% | 4.4% | | | | | |
| ROCE | 4.0% | 10.2% | 6.2% | 7.6% | 8.5% | | | | | |
| ROE | 13.0% | 20.9% | 19.7% | 20.7% | 19.4% | | | | | |
| Total Debt / EBITDA | 8.2x | 4.7x | 6.5x | 5.1x | 4.0x | | | | | |
| Total Debt / Equity | 258.0% | 219.2% | 171.7% | 134.7% | 100.2% | | | | | |
| Total Debt / Capitalization | 72.1% | 68.7% | 63.2% | 57.4% | 50.1% | | | | | |
| Net Debt / EBITDA | 5.1x | 3.6x | 5.0x | 3.7x | 3.1x | | | | | |
| Net Debt / Equity | 159.9% | 169.6% | 132.6% | 99.5% | 76.5% | | | | | |
| Net Debt / Capitalization | 44.7% | 53.1% | 48.8% | 42.4% | 38.2% | | | | | |
| Current Ratio | 203.9% | 189.7% | 184.3% | 165.5% | 160.8% | | | | | |
| Cash / Total Assets | 20.3% | 10.8% | 9.4% | 9.0% | 6.2% | | | | | |
| Inventory / Total Assets | 47.8% | 48.6% | 53.4% | 58.7% | 66.1% | | | | | |
| Net debt / Net Inventory | 69.2% | 76.0% | 59.5% | 43.2% | 30.3% | | | | | |
| Quick Ratio | 151.4% | 161.1% | 161.0% | 146.3% | 148.4% | | | | | |
| Cash Ratio | 52.6% | 28.6% | 23.4% | 19.2% | 12.4% | | | | | |
| Interest Coverage | 6.2x | 11.0x | 7.5x | 9.3x | 8.1x | | | | | |

Source: Company data, AMTD Equity Research

Figure 3: Balance sheet forecast & Cash flow forecast

| Balance Sheet, RMB mn | 2016 | 2,017 | 2018e | 2019e | 2020e |
|---|----------------|----------------|----------------|----------------|----------------|
| Non-current assets | 48,034 | 84,429 | 84,429 | 84,429 | 84,429 |
| Current assets | 178,378 | 213,680 | 241,485 | 289,830 | 353,840 |
| Properties held under development | 81,135 | 110,866 | 140,295 | 185,674 | 255,988 |
| Properties held for sale | 26,783 | 33,449 | 33,449 | 33,449 | 33,449 |
| Bank balances and cash | 25,306 | 19,697 | 18,073 | 21,039 | 14,735 |
| Others | 45,154 | 49,668 | 49,668 | 49,668 | 49,668 |
| Current liabilities | 87,474 | 112,666 | 131,000 | 175,111 | 220,068 |
| Short-term borrowings | 33,682 | 28,414 | 24,241 | 31,300 | 18,514 |
| Deposits received on sale of properties | 19,547 | 29,058 | 51,566 | 88,618 | 146,362 |
| Others | 34,245 | 55,193 | 55,193 | 55,193 | 55,193 |
| Non-current liabilities | 92,101 | 120,550 | 116,729 | 103,838 | 103,325 |
| Borrowings | 87,170 | 113,829 | 110,009 | 97,118 | 96,604 |
| Others | 4,931 | 6,720 | 6,720 | 6,720 | 6,720 |
| Equity attributable to owners of the Company | 43,778 | 61,532 | 74,730 | 91,759 | 111,232 |
| Perpetual capital instruments | 2,404 | 2,404 | 2,404 | 2,404 | 2,404 |
| Non-controlling interests | 654 | 957 | 1,051 | 1,145 | 1,240 |
| Cash Flow Statement, RMB mn | 2016 | 2017e | 2018e | 2019e | 2020e |
| Profit for the year | 7,056 | 21,424 | 13,435 | 17,268 | 19,710 |
| Operating cash flows before movements in working capital | 15,129 | 35,374 | 24,678 | 28,914 | 32,330 |
| — Properties under development and completed properties held for sale | (1,165) | (36,397) | (29,429) | (45,379) | (70,314) |
| — Deposits received on sale of properties | 1,139 | 9,511 | 22,508 | 37,052 | 57,743 |
| Cash (used in) from operations | 5,705 | 9,815 | 17,757 | 20,587 | 19,759 |
| Interest paid | (5,217) | (6,899) | (6,835) | (5,981) | (6,153) |
| Enterprise income tax and land appreciation tax paid | (3,826) | (7,051) | (4,408) | (5,666) | (6,467) |
| Net cash (used in) from operating activities | (3,338) | (4,135) | 6,514 | 8,941 | 7,139 |
| Net cash used in investing activities | 2,526 | (18,976) | 0 | 0 | 0 |
| Financing activities | | | | | |
| Net Proceeds from borrowings, net of transaction costs | 33,847 | 21,392 | (7,994) | (5,832) | (13,300) |
| Net cash from (used in) financing activities | 12,080 | 17,573 | (8,138) | (5,975) | (13,444) |
| Net increase in cash and cash equivalents | 11,268 | (5,538) | (1,624) | 2,966 | (6,304) |
| Effect of foreign exchange rate changes | 29 | 0 | 0 | 0 | 0 |
| Cash and cash equivalents at beginning of the year | 13,938 | 25,235 | 19,697 | 18,073 | 21,039 |
| Cash and cash equivalents at end of the year | 25,235 | 19,697 | 18,073 | 21,039 | 14,735 |

Source: Company data, AMTD Equity Research

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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 |

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