

21 March 2019

Property | Real Estate

China Overseas Land (688 HK)

Buy (Maintained)

Safe Ship With Ongoing Recovery, Still a BUY

Target Price (Return)	HKD36.10 (+21%)
Price:	HKD29.95
Market Cap:	USD41,801m
Avg Daily Turnover (HKD/USD)	427m/55m

- Maintain BUY with a new HKD36.10 TP** (from HKD32.40), 21% upside plus 4.5% FY19F yield. We expect China Overseas Land to resume solid earnings growth from FY19 onwards, following its ongoing contracted sales recovery. Its investment property (IP) business is near a harvest period, too, in our view. We expect its leading position in GPM and financial strengths to continue in FY19-21F. Overall, we recommend COLI to investors seeking a steady large-cap play with low-beta nature and solid fundamentals.
- Contracted sales recovery, followed by earnings growth.** Since the current chairman and CEO Mr Yan Jianguo took over the role in late 2016, COLI has delivered its promise of resuming contracted sales growth (+29.2% YoY) in FY18. We expect contracted sales to easily reach the benchmark levels of CNY350bn/CNY400bn in FY19F/FY20F, translating into 16%/14% YoY growth. It is solely based on the sell-through rate of 50% and excludes most of the newly-acquired projects during the period. As such, we believe these are conservative targets and COLI is likely to exceed them eventually. On the other hand, we regard the gap in FY18 core earnings growth as an expected story. It was largely a lag impact from the sluggish contracted sales booked in FY16-17. As its contracted sales recovery is evident, we maintain that COLI is set to resume solid earnings growth from FY19F onwards (at a CAGR of 25.2% for FY18-21F).
- Accelerating IP business a hidden gem.** Being the largest office landlord in China, COLI achieved 38% YoY income growth from investment properties (which include hotels). We believe it is just the beginning and not the end of the growth story. With 5.5m sqm under development – equivalent to 1.3x of current operations – we expect IP income to grow continuously in the next 5 years, at a CAGR of 20%. IP represents 22% of our gross asset value (GAV) by now, and there is room for further increment, in our view.
- In-line FY18 results.** FY18 core earnings rose 8.3% YoY and largely met our forecasts (1.5% above), despite missing the Street estimate by 7%. We see COLI has kept its edge of having a strong GPM (37.8%) and sector-leading financial strength (net gearing of 33.7%, weighted average financing cost of 4.3%). We fine-tune FY19F-20F earnings by +1%/-2%, and introduce FY21F earnings with 21% YoY growth. Our end-FY19F ENAV also increases to HKD48.10 from HKD43.20, mainly due to higher IP values and higher NPM assumptions. At an unchanged 25% discount to ENAV (+1SD from historical mean), we raise our TP to HKD36.10.

Analyst

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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	11.3	4.0	11.5	17.9	7.7
Relative	13.4	2.8	14.4	6.7	(7.1)
52-wk Price low/high (HKD)	30.8 – 22.4				



Source: Bloomberg

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover (HKDm)	166,045	171,461	245,608	303,180	365,203
Recurring net profit (HKDm)	34,257	37,091	48,735	60,312	72,795
Recurring net profit growth (%)	9.2	8.3	31.4	23.8	20.7
Recurring EPS (HKD)	3.13	3.39	4.45	5.50	6.64
Recurring P/E (x)	9.6	8.8	6.7	5.4	4.5
P/BV (x)	1.2	1.2	1.0	0.9	0.8
DPS (HKD)	0.80	0.90	1.33	1.65	1.99
Dividend Yield (%)	2.7	3.0	4.5	5.5	6.7
ROAE (%)	14.0	13.5	16.3	18.1	19.4
Net debt to equity (%)	27.9	33.7	28.5	23.8	17.1
Interest coverage (x)	7.3	6.4	7.9	8.8	9.9

Source: Company data, RHB

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FY18 Results Review

Figure 1: COLI's FY18 results vs RHB forecasts

FY end Dec 31 (HKD m)	Actual		2H18	RHB	2H18	Actual		YoY	RHB	Diff (%)	BBG	
	1H18	2H18	YoY	2H18	Diff (%)	FY17	FY18		FY18		Consensus	Diff (%)
Turnover	88,601	82,860	5.1%	94,168	-12.0%	166,045	171,461	3.3%	182,769	-6.2%	198,811	-13.8%
Property sales	86,301	80,736	5.1%	91,855	-12.1%	162,140	167,037	3.0%	178,156	-6.2%		
Property rental and mgmt	1,762	1,772	37.2%	1,704	4.0%	2,450	3,534	44.2%	3,466	2.0%		
Other operations	538	353	-52.4%	610	-42.1%	1,455	891	-38.8%	1,148	-22.4%		
Cost of sales	(56,900)	(49,757)	-1.9%	(63,598)	-21.8%	(111,345)	(106,658)	-4.2%	(120,498)	-11.5%		
Gross profit	31,701	33,103	17.8%	30,570	8.3%	54,700	64,803	18.5%	62,271	4.1%		
Other income and expenses	1,423	(318)	-107.4%	813	-139.2%	5,886	1,104	-81.2%	2,236	-50.6%		
Selling and distribution exp	(1,100)	(1,521)	-19.5%	(1,901)	-19.9%	(2,950)	(2,622)	-11.1%	(3,001)	-12.6%		
Administrative expenses	(1,685)	(1,281)	-20.6%	(2,224)	-42.4%	(2,849)	(2,967)	4.1%	(3,910)	-24.1%		
Operating profit	30,338	29,982	3.6%	27,258	10.0%	54,788	60,319	10.1%	57,596	4.7%		
Revaluation change	5,408	5,004	130.2%	0	N/A	5,946	10,413	75.1%	5,408	92.5%		
Exceptionals	0	0	-100.0%	0	N/A	2,140	0	N/A	0	N/A		
Finance cost	(690)	(895)	20.6%	(862)	3.9%	(1,394)	(1,586)	13.8%	(1,552)	2.1%		
Associates and JCEs	2,088	1,334	143.1%	2,285	-41.6%	1,938	3,422	76.5%	4,373	-21.7%		
Profit before taxation	37,144	35,424	16.0%	28,681	23.5%	63,419	72,568	14.4%	65,825	10.2%		
Taxation	(12,889)	(12,978)	19.1%	(10,702)	21.3%	(21,277)	(25,866)	21.6%	(23,590)	9.6%		
Profit after taxation	24,255	22,447	14.2%	17,979	24.8%	42,142	46,702	10.8%	42,234	10.6%		
Minority interests	(1,037)	(765)	40.9%	(599)	27.7%	(1,375)	(1,802)	31.0%	(1,636)	10.1%		
Reported net profit	23,219	21,682	13.4%	17,380	24.8%	40,767	44,900	10.1%	40,599	10.6%		
Recurring net profit	19,170	17,920	2.5%	17,372	3.2%	34,257	37,090	8.3%	36,542	1.5%	39,818	-6.9%
Basic EPS (HKD)	2.119	1.979	13.4%	1.586	24.8%	3.721	4.098	10.1%	3.706	10.6%		
Core EPS (HKD)	1.750	1.636	2.5%	1.586	3.2%	3.127	3.385	8.3%	3.335	1.5%	3.562	-5.0%
DPS (HKD)	0.400	0.500	11.1%	0.434	15.3%	0.800	0.900	12.5%	0.834	7.9%	0.969	-7.1%
BVPS (HKD)	25.180	25.874	6.7%	26.682	-3.0%	24.251	25.874	6.7%	26.682	-3.0%	27.056	-4.4%
Gross margin	35.8%	40.0%		32.5%		32.9%	37.8%		34.1%			
Operating margin	34.2%	36.2%		28.9%		33.0%	35.2%		31.5%			
Effective tax rate	-34.7%	-36.6%		-37.3%		-33.6%	-35.6%		-35.8%			
Net margin	26.2%	26.2%		18.5%		24.6%	26.2%		22.2%			
Core net margin	21.6%	21.6%		18.4%		20.6%	21.6%		20.0%			

Source: Company data, RHB

Changes In Earnings Forecasts

Figure 2: Changes to our forecasts

(HKD m)	FY19F			FY20F		
	Original	New	chg (%)	Original	New	chg (%)
Revenue	250,265	245,608	-2%	312,056	303,180	-3%
Cost of goods sold	(167,439)	(164,319)	-2%	(210,536)	(204,494)	-3%
Gross Profit	82,826	81,290	-2%	101,520	98,686	-3%
Selling and distribution exp	(4,098)	(3,168)	-23%	(4,958)	(3,870)	-22%
Administrative expenses	(4,711)	(3,281)	-30%	(4,939)	(3,639)	-26%
Other income, expenses and gains	3,233	1,786	-45%	4,648	2,607	-44%
Exceptional	0	0	N/A	0	0	N/A
Revaluation gain	0	0	N/A	0	0	N/A
Interest expense	(1,596)	(1,933)	21%	(1,612)	(2,134)	32%
JCE & Associate items	6,258	4,399	-30%	8,096	5,553	-31%
Profit before tax	81,911	79,093	-3%	102,754	97,204	-5%
Taxation	(31,462)	(28,349)	-10%	(38,790)	(34,342)	-11%
Minority Interests	(2,004)	(2,008)	0%	(2,605)	(2,551)	-2%
Reported net profit	48,445	48,735	1%	61,360	60,312	-2%
Recurring net profit	48,445	48,735	1%	61,360	60,312	-2%
Gross profit margin (%)	33.1%	33.1%	0.0ppts	32.5%	32.6%	0.0ppts
Reported net profit margin (%)	19.4%	19.8%	0.5ppts	19.7%	19.9%	0.2ppts
Recurring net profit margin (%)	19.4%	19.8%	0.5ppts	19.7%	19.9%	0.2ppts

Source: RHB

Figure 3: COLI's annual P&L (FY17-21F)

FY end Dec 31 (HKD m)	FY17	FY18	FY19F	FY20F	FY21F
Property sales	162,140	167,037	240,221	296,722	357,436
Property investment	2,450	3,534	4,452	5,476	6,736
Property mgmt and others	1,455	891	936	982	1,031
Total revenue	166,045	171,461	245,608	303,180	365,203
Cost of sales	(111,345)	(106,658)	(164,319)	(204,494)	(247,014)
Gross profit	54,700	64,803	81,290	98,686	118,189
Other income	5,886	1,104	1,786	2,607	3,449
Selling and marketing exp	(2,950)	(2,622)	(3,168)	(3,870)	(4,633)
Administrative expenses	(2,849)	(2,967)	(3,281)	(3,639)	(4,356)
Revaluation change & Exceptionals	8,086	10,413	0	0	0
Finance cost	(1,394)	(1,586)	(1,933)	(2,134)	(2,284)
Associates and JCEs	1,938	3,422	4,399	5,553	6,943
Profit before taxation	63,419	72,568	79,093	97,204	117,308
Taxation	(21,277)	(25,866)	(28,349)	(34,342)	(41,354)
Profit after taxation	42,142	46,702	50,743	62,863	75,953
Minority interests	(1,375)	(1,802)	(2,008)	(2,551)	(3,158)
Reported net profit	40,767	44,900	48,735	60,312	72,795
Recurring net profit	34,257	37,091	48,735	60,312	72,795
Reported EPS (HKD)	3.721	4.098	4.448	5.505	6.644
Recurring EPS (HKD)	3.127	3.385	4.448	5.505	6.644
DPS (HKD)	0.800	0.900	1.334	1.651	1.993
Profit margin:					
Gross margin	32.9%	37.8%	33.1%	32.6%	32.4%
Reported net margin	24.6%	26.2%	19.8%	19.9%	19.9%
Recurring net margin	20.6%	21.6%	19.8%	19.9%	19.9%
YoY growth:					
Turnover	1.2%	3.3%	43.2%	23.4%	20.5%
Booked property sales revenue	1.4%	3.0%	43.8%	23.5%	20.5%
Reported net profit	10.1%	10.1%	8.5%	23.8%	20.7%
Recurring net profit	9.2%	8.3%	31.4%	23.8%	20.7%
Reported EPS	2.4%	10.1%	8.5%	23.8%	20.7%
Recurring EPS	1.5%	8.3%	31.4%	23.8%	20.7%

Source: RHB

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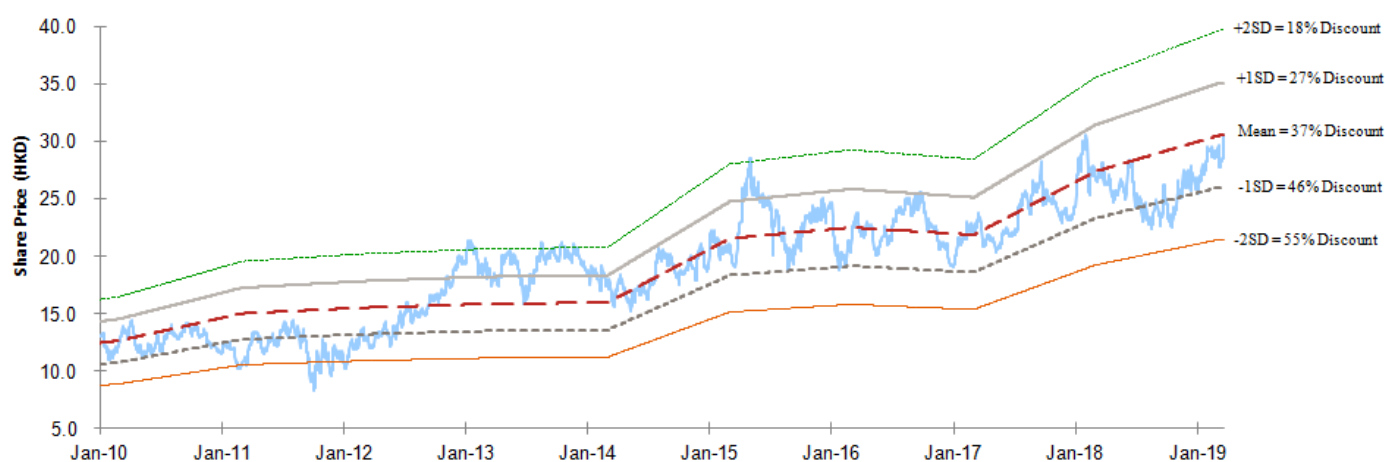
Valuations

Figure 4: COLI's end-FY19F ENAV

Details	Total HKD m	HKD/share	% of Total
Landbank and properties under development	496,749	45.3	94%
Investment properties completed and under development	115,286	10.5	22%
38% stake in COGO	4,321	0.4	1%
Net debts as of end-FY19F	(89,876)	(8.2)	-17%
Total	526,480	48.1	100%

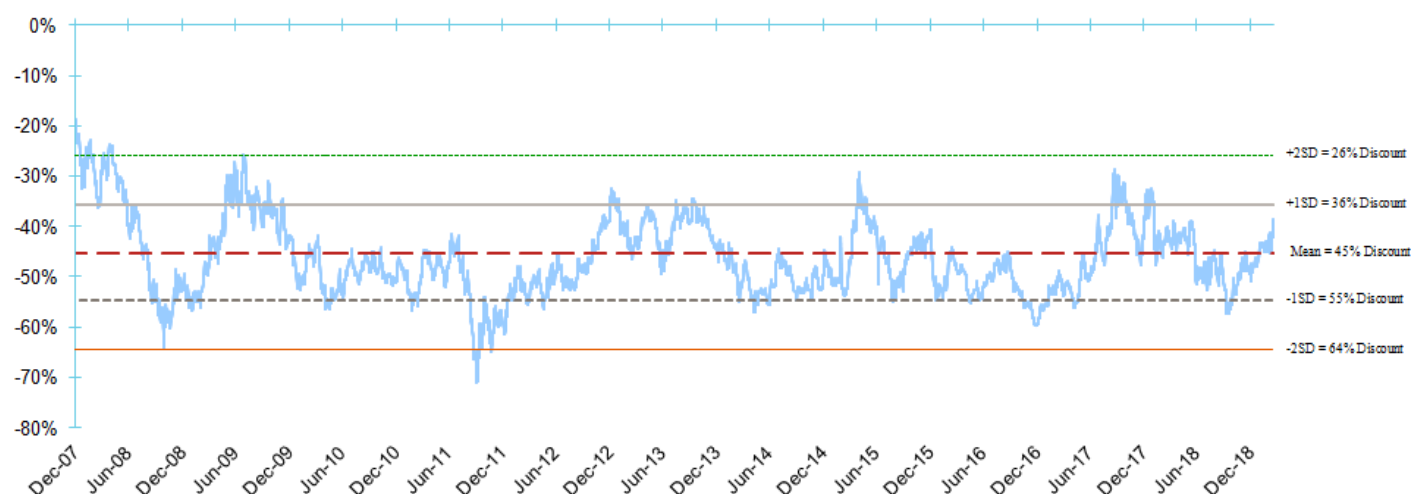
Source: RHB

Figure 5: COLI's 5-year rolling forward ENAV band



Source: Bloomberg, RHB

Figure 6: China property sector – 10-year ENAV discount band



Source: Bloomberg, RHB

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