

1 April 2019

Property | Real Estate

Sunac China Holdings (1918 HK)

Buy (Maintained)

Continuous Improvements; Keep BUY

Target Price (Return) HKD43.90 (+12%)
 Price: HKD39.10
 Market Cap: USD21,996m
 Avg Daily Turnover (HKD/USD) 679m/87m

- Keep BUY with new HKD43.90 TP from HKD32.10, 12% upside plus 4% yield.** We continue to observe Sunac's improving fundamentals, and its well-managed balance between sustaining contracted sales growth, revenue bookings pace and lowering leverage. Being one of the highest-leveraged developers, we believe Sunac will continue to benefit from the robust property market and loosening financing environment in China.
- Harvest period from scale expansion strategies.** Following the aggressive acquisitions at the expense of mounting leverage in the past few years, we see that Sunac has established the ideal landbank size to support its sustainable growth in the long term. While many developers are still catching up their revenue bookings and earnings growth with their contracted sales growth, we note Sunac's swift execution in achieving decent earnings growth (+43% in FY18, CAGR at 34.4% for FY18-21F). Moreover, Sunac is able to sustain its contracted sales growth momentum (+19% in FY19F), raise its dividend payout, but lower its gearing at the same time.
- Decent contracted sales momentum and normalising profit margins.** Investors' concerns about Sunac are usually on its leverage and weak profit margins. Given that Sunac's pain of low margin bookings from acquired assets is fading out, together with its heavy concentration in Tier-1 and -2 cities, we estimate a normalising GPM of 24-26% (consolidated) in the next three years. On the other hand, assuming no major acquisitions ahead, we expect Sunac to remain on the path of lowering its net gearing. Finally, we believe Sunac's 19% FY19F contracted sales growth target is the highest among the Top 4 developers.
- FY18 earnings beat, surprises on gearing and dividends.** FY18 core earnings (excluding FX loss, revaluation gains and exceptional items) rose 43% YoY, beating our and Street forecasts by 14% and 1%. Besides the strong earnings growth, its closely-watched net gearing (treating perpetual securities as debt) dropped further to 170%, compared with 232% and 257% as of end-1H18 and end-FY17. Riding on the improvement of financial positions, Sunac raised its dividend payout ratio (vs our core profit) to 23% (FY17: 20%).
- Maintain BUY with higher TP driven by ENAV.** We raise our FY19F-20F earnings by 5% and 1%, mainly factoring better GPM assumptions, and introduce FY21F earnings with 22% YoY growth. We raise our end-FY19F ENAV by a larger extent to HKD54.80 (from HKD42.90), reflecting Sunac's ability to enlarge its landbank and reduce its leverage at the same time. Narrowing our ENAV discount to 20% from 25% (maintaining at +2SD), we arrive at our new TP of HKD43.90.

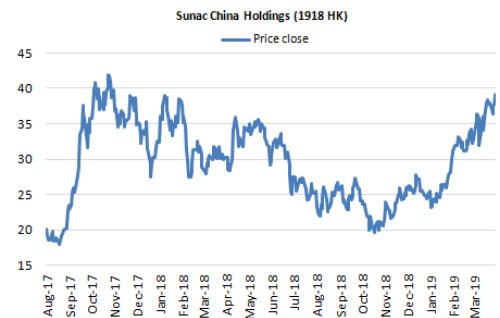
Analyst

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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	53.3	19.0	56.7	62.2	29.0
Relative	12.4	1.5	13.9	4.5	(3.5)
52-wk Price low/high (HKD)	19.1 – 39.9				



Source: Bloomberg

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover (CNYm)	65,874	124,746	180,222	243,341	290,509
Recurring net profit (CNYm)	11,120	15,919	23,073	31,595	38,682
Recurring net profit growth (%)	368.6	43.2	44.9	36.9	22.4
Recurring EPS (CNY)	2.79	3.62	5.19	7.04	8.53
Recurring P/E (x)	11.9	9.2	6.4	4.7	3.9
P/BV (x)	3.0	2.6	1.9	1.5	1.1
DPS (CNY)	0.50	0.83	1.30	1.76	2.13
Dividend Yield (%)	1.5	2.5	3.9	5.3	6.4
ROAE (%)	25.4	28.0	30.3	30.9	29.1
Net debt to equity (%)	256.7	169.8	152.4	139.5	132.3
Interest coverage (x)	2.0	1.6	2.2	2.4	2.5

Source: Company data, RHB

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FY18 Results Review

Figure 1: Sunac's FY18 results vs RHB forecasts

FY end Dec 31 (CNY m)	Actual	Actual	2H18	RHB		Actual	Actual	FY18	RHB		BBG	
	1H18	2H18	YoY	2H18	Diff	FY17	FY18	YoY	FY18	Diff	Consensus	Diff
Turnover	46,583	78,163	53.0%	79,445	-1.6%	65,874	124,746	89.4%	126,027	-1.0%	143,683	-13.2%
Property sales	44,343	73,372	51.9%	76,728	-4.4%	62,569	117,714	88.1%	121,071	-2.8%		
Property rental and mgmt	2,240	4,791	70.4%	2,716	76.4%	3,304	7,031	112.8%	4,956	41.9%		
Cost of sales	(35,055)	(58,555)	43.7%	(60,555)	-3.3%	(52,246)	(93,610)	79.2%	(95,610)	-2.1%		
Gross profit	11,528	19,608	89.6%	18,889	3.8%	13,628	31,136	128.5%	30,417	2.4%		
Selling and distribution exp	(1,919)	(2,441)	-7.5%	(2,863)	-14.7%	(3,419)	(4,361)	27.5%	(4,782)	-8.8%		
Administrative expenses	(2,962)	(4,394)	-8.1%	(4,812)	-8.7%	(5,559)	(7,357)	32.3%	(7,774)	-5.4%		
Other income and gains	5,346	946	-96.0%	3,476	-72.8%	27,916	6,292	-77.5%	8,822	-28.7%		
Other expenses and losses	(247)	(1,739)	-81.4%	(318)	447.2%	(10,689)	(1,986)	-81.4%	(565)	251.4%		
Operating profit	11,745	11,980	-30.4%	14,373	-16.6%	21,876	23,725	8.5%	26,118	-9.2%		
Revaluation change	0	209	N/A	0	N/A	0	209	N/A	0	N/A		
Exceptionals	(430)	1,085	N/A	430	N/A	0	655	N/A	0	N/A		
Finance cost - net	(2,193)	1,312	-148.5%	(3,733)	-135.1%	(4,523)	(881)	-80.5%	(5,926)	-85.1%		
Associates and JCEs	1,112	3,844	-311.6%	2,823	36.2%	(1,994)	4,956	-348.6%	3,935	26.0%		
Profit before taxation	10,234	18,430	45.4%	13,892	32.7%	15,359	28,664	86.6%	24,126	18.8%		
Taxation	(3,456)	(7,763)	159.9%	(5,003)	55.2%	(3,695)	(11,219)	203.7%	(8,460)	32.6%		
Profit after taxation	6,778	10,667	10.1%	8,889	20.0%	11,664	17,445	49.6%	15,667	11.4%		
MI/PCS	(417)	(462)	41.0%	(1,257)	-63.2%	(661)	(878)	33.0%	(1,673)	-47.5%		
Reported net profit	6,361	10,205	9.0%	7,632	33.7%	11,004	16,567	50.6%	13,994	18.4%		
Recurring net profit	6,609	9,310	-1.3%	7,385	26.1%	11,120	15,919	43.2%	13,994	13.8%	15,695	1.4%
Basic EPS (CNY)	1.446	2.317	-4.3%	2.060	12.5%	2.757	3.763	36.5%	3.506	7.3%		
Core EPS (CNY)	1.502	2.114	-13.4%	2.004	5.5%	2.786	3.616	29.8%	3.506	3.1%	3.475	4.1%
DPS (CNY)	0.000	0.827	65.1%	0.701	17.9%	0.501	0.827	65.1%	0.701	17.9%	0.750	10.3%
BVPS (CNY)	10.828	12.910	17.6%	13.928	-7.3%	10.974	12.910	17.6%	13.928	-7.3%	12.651	2.0%
Gross margin	24.7%	25.1%		23.8%		20.7%	25.0%		24.1%			
Operating margin	25.2%	15.3%		18.1%		33.2%	19.0%		20.7%			
Effective tax rate	-33.8%	-42.1%		-36.0%		-24.1%	-39.1%		-35.1%			
Net margin	13.7%	13.1%		9.6%		16.7%	13.3%		11.1%			
Core net margin	14.2%	11.9%		9.3%		16.9%	12.8%		11.1%			

Source: Company data, RHB

Changes In Earnings Forecasts

Figure 2: Changes to our forecasts

(CNY m)	FY19F			FY20F		
	Original	New	chg (%)	Original	New	chg (%)
Revenue	180,960	180,222	0%	240,020	243,341	1%
Cost of goods sold	(138,288)	(134,050)	-3%	(184,353)	(183,822)	0%
Gross Profit	42,672	46,173	8%	55,667	59,519	7%
Selling expenses	(5,802)	(5,609)	-3%	(5,880)	(6,049)	3%
General and administrative expenses	(9,862)	(9,678)	-2%	(10,462)	(10,913)	4%
Interest Expense	(8,910)	(4,976)	-44%	(10,204)	(5,784)	-43%
Interest Income	2,716	1,259	-54%	3,564	1,319	-63%
JCE & Associate items	6,828	6,351	-7%	9,844	8,864	-10%
Others	8,370	4,826	-42%	5,187	4,440	-14%
Pre-tax profit	36,012	38,345	6%	47,716	51,396	8%
Income tax & LAT	(12,236)	(13,483)	10%	(14,605)	(18,052)	24%
Minority Interests	(1,097)	(1,372)	25%	(1,238)	(1,331)	7%
Distribution to PCS	(701)	(417)	-40%	(701)	(417)	-40%
Reported net profit	21,978	23,073	5%	31,172	31,595	1%
Recurring net profit	21,978	23,073	5%	31,172	31,595	1%
Gross profit margin (%)	23.6%	25.6%	2.0ppts	23.2%	24.5%	1.3ppts
Reported net margin (%)	12.1%	12.8%	0.7ppts	13.0%	13.0%	0.0ppts
Recurring net margin (%)	12.1%	12.8%	0.7ppts	13.0%	13.0%	0.0ppts
Recurring net margin, ex. JCE/Asso. (%)	9.0%	10.0%	1.1ppts	9.4%	9.9%	0.5ppts

Source: RHB

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

FY end Dec 31 (CNY m)	FY17	FY18	FY19F	FY20F	FY21F
Property sales	62,569	117,714	169,324	226,448	264,325
Property rental and mgmt	3,304	7,031	10,899	16,893	26,184
Total revenue	65,874	124,746	180,222	243,341	290,509
Cost of sales	(52,246)	(93,610)	(134,050)	(183,822)	(223,078)
Gross profit	13,628	31,136	46,173	59,519	67,430
Other income and expenses	17,227	5,170	4,826	4,440	5,283
Selling and marketing exp	(3,419)	(4,361)	(5,609)	(6,049)	(6,388)
Administrative expenses	(5,559)	(7,357)	(9,678)	(10,913)	(11,525)
Finance cost - net	(4,523)	(881)	(3,717)	(4,465)	(5,319)
Associates and JCEs	(1,994)	4,956	6,351	8,864	11,850
Profit before taxation	15,359	28,664	38,345	51,396	61,332
Taxation	(3,695)	(11,219)	(13,483)	(18,052)	(21,306)
Profit after taxation	11,664	17,445	24,862	33,344	40,026
Distribution to PCS	(679)	(591)	(417)	(417)	(417)
MI	19	(287)	(1,372)	(1,331)	(927)
Reported net profit	11,004	16,567	23,073	31,595	38,682
Recurring net profit	11,120	15,919	23,073	31,595	38,682
Reported EPS (CNY)	2.757	3.763	5.189	7.035	8.528
Recurring EPS (CNY)	2.786	3.616	5.189	7.035	8.528
DPS (CNY)	0.501	0.827	1.297	1.759	2.132
Profit margin:					
Gross margin	20.7%	25.0%	25.6%	24.5%	23.2%
Reported net margin	16.7%	13.3%	12.8%	13.0%	13.3%
Recurring net margin	16.9%	12.8%	12.8%	13.0%	13.3%
YoY growth:					
Turnover	86.4%	89.4%	44.5%	35.0%	19.4%
Booked property sales revenue	80.8%	88.1%	43.8%	33.7%	16.7%
Reported net profit	344.0%	50.6%	39.3%	36.9%	22.4%
Recurring net profit	368.6%	43.2%	44.9%	36.9%	22.4%
Reported EPS	285.7%	36.5%	37.9%	35.6%	21.2%
Recurring EPS	307.1%	29.8%	43.5%	35.6%	21.2%

Source: RHB

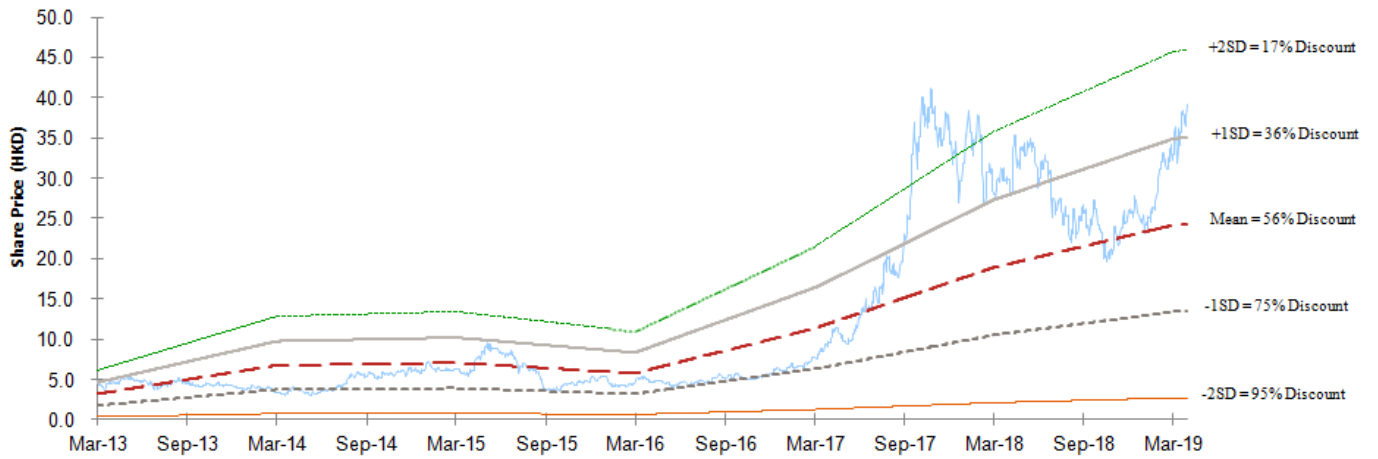
Valuation

Figure 4: Sunac's end-FY19F ENAV

Details	Total HKD m	HKD/share	% of Total
Landbank and properties under development	380,480	86.2	157%
Investment properties	20,007	4.5	8%
Net debts as of end-FY19F	(158,429)	(35.9)	-65%
Total	242,057	54.8	100%

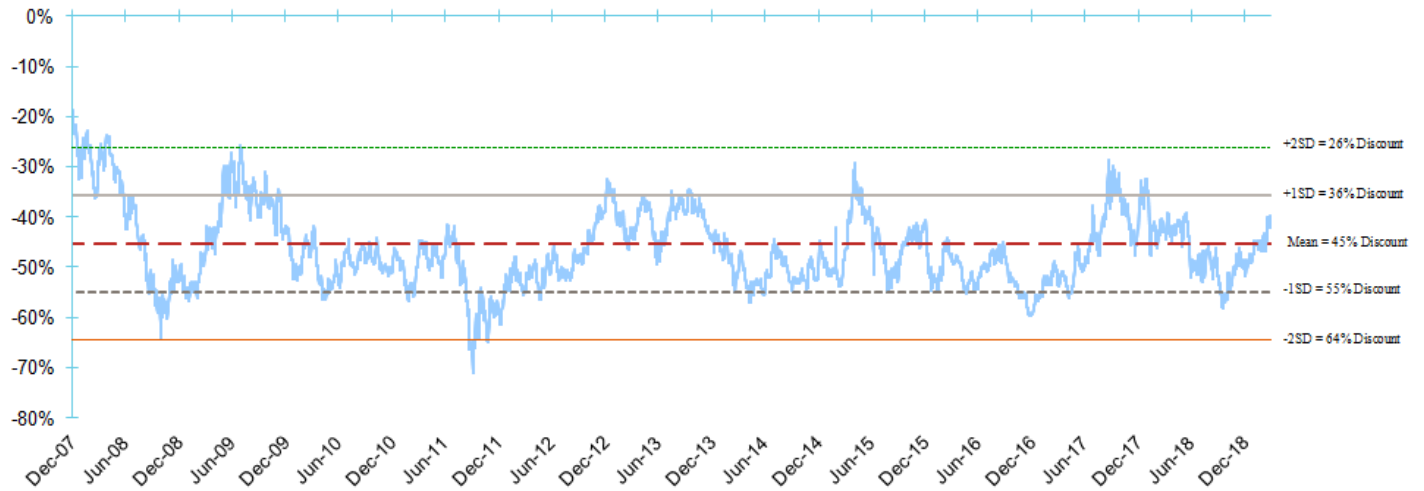
Source: RHB

Figure 5: Sunac'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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