

19 March 2019

Property | Real Estate

Country Garden (2007 HK)

Buy (Maintained)

En Route To Being a Safety Play, Keep BUY

Target Price (Return)	HKD17.00 (+46%)
Price:	HKD11.68
Market Cap:	USD32,210m
Avg Daily Turnover (HKD/USD)	436m/56m

- Maintain BUY and HKD17.00 TP, 46% upside plus 6% yield.** We see Country Garden's improvement in profitability and financial position have moved it towards being a safety play among top-tier developers. Despite expecting normalised contracted sales growth ahead, earnings growth outlook remains intact, secured by considerable presales proceed. Overall, we maintain our positive view following its FY18 results. It is a candidate to benefit from supportive policies in low-tier cities, and the Greater Bay Area (GBA).

- On course to achieving desirable profitability and financial stability.** While FY18 earnings largely met, we see CG's GPM improvement and lower leverage as the major surprises – these mainly attributed to its cost control, low land cost, and slowdown of construction (especially in 2H18). Going forward, as there is still room for booked ASP increment, we believe it should keep GPM at 24-26% for FY19F-21F. However, we expect CG to restrain its gearing level, given its prudent land acquisition scale. The ramp up of construction pace is a swing factor, but it is unlikely to raise the company's leverage drastically. We estimate net gearing to stay at 40-60% in FY19F-21F, below the sector average of 70-80%.

- Prudent contracted sales growth ahead.** As mentioned in [our previous preview report](#), being one of the Top 3 developers in China in contracted sales value, we forecast CG to target a steady sales growth in FY19 by focusing more on the sustainability of ASP and profit margin. Given its saleable resources of CNY780bn, and our projected sell-through rate of 70-75%, we estimate FY19F attributable contracted sales revenue to reach CNY550-590bn, up 10-16% YoY. With more projects in Tier-1&2 cities to be launched, we believe CG's contracted ASP to turnaround from the YoY decline in 2M19.

- In line FY18 results.** FY18 results largely met, with core earnings up 38.2% YoY and 3% and 1% above our and Street forecasts. CG managed to improve GPM to 27% (from 25.9%), probably riding on the recovery in low-tier cities, as demonstrated by higher ASP and flat average cost. The positive impact was partially offset by higher minority interests distributions. We fine tune our FY19F-20F earnings by +2% each, and introduce FY21F earnings with 11% YoY growth, arriving at a CAGR of 16.3% for FY18-21F. Similarly, we tweak our end-FY19F ENAV to HKD26 (from HKD25.7). Staying at a 35% discount (+1SD from its sector average), we keep our TP at HKD17.

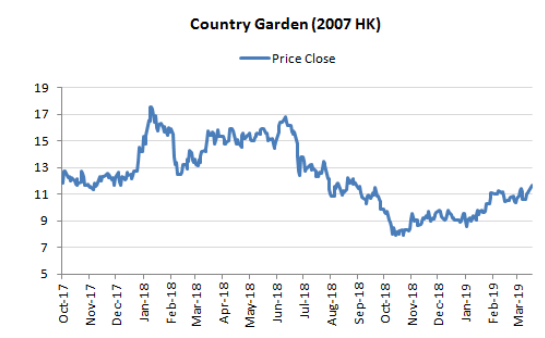
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	22.6	10.6	27.1	7.4	(25.9)
Relative	13.8	3.7	13.9	8.6	(6.6)
52-wk Price low/high (HKD)	16.9 – 7.7				



Source: Bloomberg

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover (CNYm)	226,900	379,079	493,171	527,275	580,881
Recurring net profit (CNYm)	24,686	34,120	42,732	48,124	53,604
Recurring net profit growth (%)	106.0	38.2	25.2	12.6	11.4
Recurring EPS (CNY)	1.16	1.59	1.90	2.14	2.38
Recurring P/E (x)	8.5	6.2	5.2	4.6	4.2
P/BV (x)	2.4	1.8	1.5	1.2	1.0
DPS (CNY)	0.40	0.49	0.58	0.66	0.73
Dividend Yield (%)	4.0	4.9	5.9	6.6	7.4
ROAE (%)	30.1	31.7	31.4	28.7	26.4
Net debt to equity (%)	56.9	49.6	55.7	49.6	49.3
Interest coverage (x)	3.7	4.1	3.6	3.5	3.7

Source: Company data, RHB

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FY18 Results Review

Figure 1: CG's FY18 results vs RHB forecasts

FY end Dec 31 (CNY m)	Actual		2H18	RHB	2H18	Actual		FY18	RHB	FY18	BBG	FY18
	1H18	2H18	YoY	2H18	Variance	FY17	FY18	YoY	FY18	Variance	Consensus	Variance
Turnover	131,894	247,185	65.7%	217,478	13.7%	226,900	379,079	67.1%	349,372	8.5%	351,409	7.9%
Property sales	126,885	242,520	66.5%	212,374	14.2%	220,157	369,405	67.8%	339,259	8.9%		
Property mgmt and others	5,009	4,665	34.1%	5,105	-8.6%	6,742	9,674	43.5%	10,114	-4.3%		
Cost of sales	(96,921)	(179,682)	67.2%	(161,536)	11.2%	(168,114)	(276,603)	64.5%	(258,457)	7.0%		
Gross profit	34,973	67,503	61.9%	55,942	20.7%	58,785	102,476	74.3%	90,915	12.7%		
Other income	1,758	186	-72.5%	82	126.3%	920	1,944	111.3%	1,840	5.6%		
Selling and marketing exp	(4,502)	(8,031)	20.5%	(14,924)	-46.2%	(10,002)	(12,533)	25.3%	(19,426)	-35.5%		
Administrative expenses	26,347	48,939	55.7%	33,801	44.8%	41,402	75,286	81.8%	60,148	25.2%		
Operating profit	26,347	48,939	55.7%	33,801	44.8%	41,402	75,286	81.8%	60,148	25.2%		
Revaluation change	539	1,193	245.6%	0	N/A	505	1,732	243.2%	539	221.3%		
Other gains / (Losses) & exceptionals	0	0	-100.0%	0	N/A	1,691	0	N/A	0	N/A		
Finance costs	(596)	(501)	241.8%	(468)	7.1%	(147)	(1,097)	648.5%	(1,064)	3.1%		
Finance income	777	1,668	-35.7%	735	126.9%	3,423	2,445	-28.6%	1,512	61.7%		
Associates and JCEs	(210)	1,407	-492.5%	752	87.1%	(352)	1,197	N/A	542	120.8%		
Profit before taxation	26,857	52,706	54.5%	34,820	51.4%	46,522	79,563	71.0%	61,677	29.0%		
Taxation	(10,538)	(20,483)	49.1%	(12,899)	58.8%	(17,770)	(31,021)	74.6%	(23,437)	32.4%		
Profit after taxation	16,319	32,223	58.1%	21,921	47.0%	28,752	48,542	68.8%	38,240	26.9%		
Minority interests / PCS	(3,380)	(10,544)	480.5%	(1,209)	772.3%	(2,688)	(13,924)	418.0%	(4,589)	203.4%		
Reported net profit	12,939	21,679	16.8%	20,712	4.7%	26,064	34,618	32.8%	33,651	2.9%		
Recurring net profit	12,950	21,175	21.0%	20,297	4.3%	24,686	34,125	38.2%	33,247	2.6%	33,707	1.2%
Basic EPS (CNY)	0.600	1.012	15.2%	0.902	12.2%	1.228	1.612	31.3%	1.502	7.3%		
Core EPS (CNY)	0.601	0.988	19.4%	0.883	11.9%	1.163	1.589	36.6%	1.484	7.1%	1.564	1.6%
DPS (CNY)	0.185	0.303	21.5%	0.280	8.1%	0.400	0.488	22.2%	0.466	4.9%	0.528	-7.5%
BVPS (CNY)	4.869	5.651	28.0%	6.000	-5.8%	4.413	5.651	28.0%	6.000	-5.8%	5.946	-5.0%
Gross margin	26.5%	27.3%		25.7%		25.9%	27.0%		26.0%			
Operating margin	20.0%	19.8%		15.5%		18.2%	19.9%		17.2%			
Effective tax rate	-39.2%	-38.9%		-37.0%		-38.2%	-39.0%		-38.0%			
Net margin	9.8%	8.8%		9.5%		11.5%	9.1%		9.6%			
Core net margin	9.8%	8.6%		9.3%		10.9%	9.0%		9.5%			

Source: Company data, RHB

Changes In Earnings Forecasts

Figure 2: Changes to our forecasts

FY end Dec 31 (CNY m)	FY19F			FY20F		
	Original	New	chg (%)	Original	New	chg (%)
Revenue	439,065	493,171	12%	499,888	527,275	5%
Cost of goods sold	(329,366)	(369,837)	12%	(376,940)	(397,535)	5%
Gross Profit	109,699	123,334	12%	122,948	129,740	6%
Administrative expenses	(14,908)	(14,928)	0%	(16,935)	(17,495)	3%
Selling and marketing exp	(21,581)	(19,725)	-9%	(24,118)	(21,906)	-9%
Other incomes/expenses, inc. exceptionals	1,472	1,555	6%	1,178	1,477	25%
Revaluation gains	0	0	N/A	0	0	N/A
Interest Expense	(1,243)	(1,220)	-2%	(1,320)	(1,295)	-2%
Interest Income	1,588	2,425	53%	1,588	2,275	43%
JCE & Associate items	579	1,205	108%	623	1,287	106%
Profit before tax	75,606	92,645	23%	83,963	94,083	12%
Taxation	(28,352)	(35,668)	26%	(31,066)	(35,752)	15%
Minority Interests	(5,434)	(14,244)	162%	(5,554)	(10,208)	84%
Reported net profit	41,820	42,732	2%	47,342	48,124	2%
Recurring net profit	41,820	42,732	2%	47,342	48,124	2%
Gross profit margin (%)	25.0%	25.0%	0.0ppts	24.6%	24.6%	0.0ppts
Reported net profit margin (%)	9.5%	8.7%	-0.9ppts	9.5%	9.1%	-0.3ppts
Recurring net profit margin (%)	9.5%	8.7%	-0.9ppts	9.5%	9.1%	-0.3ppts

Source: RHB

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

FY end Dec 31 (CNY m)	FY17	FY18	FY19F	FY20F	FY21F
Property sales	220,157	369,405	486,951	520,353	573,178
Property mgmt and others	6,742	9,674	6,220	6,922	7,704
Total revenue	226,900	379,079	493,171	527,275	580,881
Cost of sales	(168,114)	(276,603)	(369,837)	(397,535)	(437,963)
Gross profit	58,785	102,476	123,334	129,740	142,918
Other income/expenses	(530)	1,944	1,555	1,477	1,404
Selling and marketing exp	(10,002)	(12,533)	(19,725)	(21,906)	(22,350)
Administrative expenses	(8,301)	(16,601)	(14,928)	(17,495)	(18,784)
Revaluation change	505	1,732	0	0	0
Exceptionals	1,450	0	0	0	0
Finance cost - net	3,276	1,348	1,205	980	1,031
Associates and JCEs	(352)	1,197	1,205	1,287	1,429
Profit before taxation	44,831	79,563	92,645	94,083	105,649
Taxation	(17,770)	(31,021)	(35,668)	(35,752)	(40,675)
Profit after taxation	27,060	48,542	56,977	58,332	64,974
Minority interests	(2,688)	(13,924)	(14,244)	(10,208)	(11,371)
Reported net profit	24,372	34,618	42,732	48,124	53,604
Recurring net profit	24,686	34,120	42,732	48,124	53,604
Reported EPS (CNY)	1.228	1.612	1.899	2.139	2.383
Recurring EPS (CNY)	1.163	1.589	1.899	2.139	2.383
DPS (CNY)	0.400	0.488	0.584	0.657	0.732
Profit margin:					
Gross margin	25.9%	27.0%	25.0%	24.6%	24.6%
Reported net margin	10.7%	9.1%	8.7%	9.1%	9.2%
Recurring net margin	10.9%	9.0%	8.7%	9.1%	9.2%
YoY growth:					
Turnover	48.2%	67.1%	30.1%	6.9%	10.2%
Booked property sales revenue	48.6%	67.8%	31.8%	6.9%	10.2%
Reported net profit	111.6%	42.0%	23.4%	12.6%	11.4%
Recurring net profit	106.0%	38.2%	25.2%	12.6%	11.4%
Reported EPS	135.4%	31.3%	17.8%	12.6%	11.4%
Recurring EPS	114.2%	36.6%	19.5%	12.6%	11.4%

Source: RHB

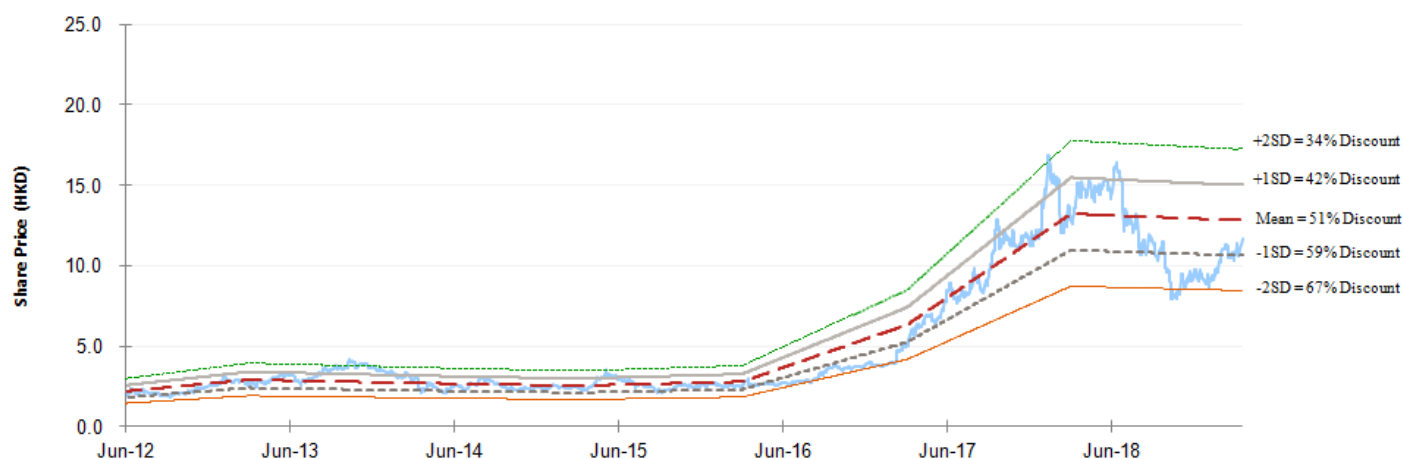
Valuations

Figure 4: CG's end-FY19F ENAV

Details	Total HKD m	HKD/share	% of total
Landbank - development properties	684,200	31.61	122%
Landbank - investment properties & hotels	21,100	0.97	4%
Net debt as at end-FY19F	(142,466)	(6.58)	-25%
Total	562,835	26.00	100%

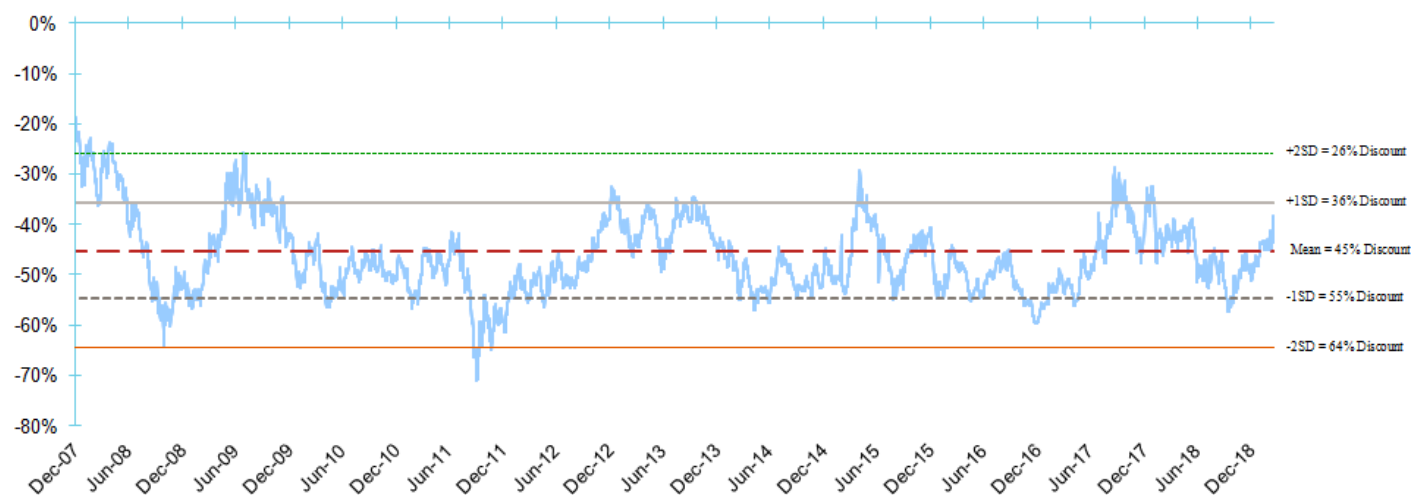
Source: RHB

Figure 5: CG'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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