



September 1, 2016
Company Report
Rating: BUY
TP: HK\$ 7.30

Share price (HK\$) 5.36
Est. share price return 36.2%
Est. dividend yield 4.7%
Est. total return 40.9%

Previous Rating & TP BUY; HK\$ 7.30
Previous Report Date May 5, 2016

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Key Data

52Wk H/L(HK\$)	6.85/4.27
Issued shares (mn)	13,798
Market cap (HK\$ mn)	73,467
3-mth avg daily turnover (HK\$ mn)	123.9
Major shareholder(s) (%): HUI Ka Yan	70.10

Source(s): Company, Bloomberg, ABCI Securities

1H16 Revenue breakdown (%)

Property development	95.7
Property investment	0.3
Property management	0.8
Others	3.2

Source(s): Company, ABCI Securities

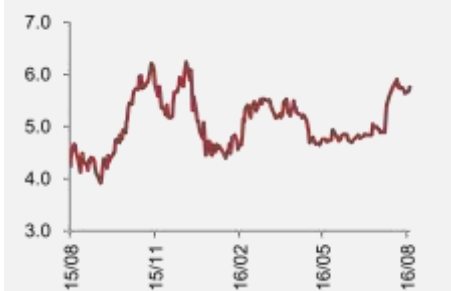
Share performance (%)

	Absolute	Relative*
1-mth	9.2	4.9
3-mth	13.5	2.8
6-mth	4.0	(9.6)

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

1-Year stock performance (HK\$)



Source(s): Bloomberg, ABCI Securities

Evergrande (3333 HK)

Presales should turn into profits soon

- 1H16 core profit (pre MI) dropped 23% YoY to RMB 7.8bn; if deducting the perpetual coupon payments and MI, core profit declined 57% YoY to RMB 2.7bn
- Net gearing dropped 0.5ppt HoH to 93.0% in June 2016; including PCI as debt, net gearing was up 170ppt to 432% in June 2016
- Rising PCI enabled Evergrande to expand its landbank at a faster pace, hence the Group's presales growth were higher than peers
- Evergrande acquired a 6.8% stake in Vanke's A shares at RMB 14.57bn, which produced a 28.8% return so far
- Maintain **BUY** with TP of HK\$7.30, still based on 40% discount to NAV

Earnings should rebound by 2017. Evergrande's 1H16 core profit (before MI and perpetual) declined 23% YoY to RMB 7.81bn. Gross margin stayed flat at 28.3% but fast SG&A growth (+50% YoY) eroded net profit. However, if we deduct the minority interest and perpetual payment, core profit attributable to ordinary shareholders declined 57% YoY to RMB2.7bn, mainly due to a 62% YoY increase in perpetual coupon payment (RMB 4.2bn). Management commented that there was a mismatch between the perpetual coupon payment and booking of earnings. In contrary to construction bank borrowing, interest payment for perpetual capital instrument (PCI) cannot be capitalized into asset and will be charged to P&L once the land is acquired. However, booking of earnings will only be made upon delivery, which usually occurs 2-3 years after land acquisition. In particular, Evergrande has started acquiring land in tier-1 cities through the use of perpetual securities since 2014, hence most of those projects would only start contributing to earnings in 2H16 or 2017.

PCI enabled fast growth. If PCI is considered as equity, Evergrande's net gearing would decline by 0.5ppt HoH to 93.0% in June 16. If the RMB 116bn of PCI (+53% HoH) on the balance sheet is considered as debt, however, net gearing would surge by 170ppt HoH to 432%. Key reasons justifying the increased use of PCI include: **1) Reduction of PCI coupon rate.** Average cost of PCI has come down from 11% since 2013 to just 9% currently. If the Group choose to set up JV with other equity funds, who will likely demand a return of 12-15% per annum, the resulting cost would be higher than that of PCI; **2) faster-than-peer growth.** As of June 2016, Evergrande has a total landbank of 186mn sqm, which is ranked no. 1 in China. In our view, the impressive presales growth (+63%YoY to RMB 142bn) relied heavily upon on owning a sizeable landbank. Thus, other than raising funds in the conventional channels such as bank borrowing and corporate bond issuance, it becomes necessary for the Group to diversify and utilize other funding channels, including the higher-cost PCI, to optimize its financial capability.

Investment in Vanke (000002 CH) produced a mark-to-market gain of RMB4.19bn in a month. On Aug 15, 2016, Evergrande announced that it had acquired 6.8% stake or 752.7mn shares in Vanke's A shares at RMB 14,570mn (RMB 19.36/share). As at Aug 31, Vanke's A-share price was RMB 24.93, implying an unrealized return of 28.8% or RMB 4.19bn in a month.(Continue next page)

Results and Valuation

FY ended Dec 31	2014A	2015A	2016E	2017E	2018E
Revenue (RMB mn)	111,398	133,130	196,559	236,057	228,178
Chg (% YoY)	18.9	19.5	47.6	20.1	(3.3)
Underlying Net Income (RMB mn) ¹	3,470	1,992	6,137	14,399	19,559
Chg (% YoY)	(54.9)	(42.6)	208.1	134.6	35.8
Underlying EPS (RMB)	0.24	0.14	0.43	1.00	1.36
Chg (% YoY)	(51.0)	(41.3)	208.1	134.6	35.8
BVPS (RMB)	7.1	8.8	8.3	8.1	8.1
Chg (% YoY)	53.7	24.7	(5.5)	(2.3)	(0.2)
Underlying PE (x)	19.1	32.5	10.6	4.5	3.3
P/B (x)	0.6	0.5	0.5	0.6	0.6
ROE (%)	3.3	1.6	5.1	12.3	16.7
ROA (%)	0.7	0.3	0.8	1.7	2.4
DPS(HK\$)	0.43	0.38	0.21	0.50	0.68
Yield (%)	9.6	8.5	4.7	11.1	15.1
Net gearing ² (%)	85.9	93.5	72.1	15.2	Net cash

¹ Underlying net income = Net profit - revaluation gain of investment properties and one-off items

² Net gearing = Net debt/Total equity

Source(s): Bloomberg, ABCI Securities estimates



Evergrande commented it will remain as a passive financial investor. We believe this lucrative transaction may provide a short-term boost to Evergrande's share price.

Maintain BUY with TP of HK\$ 7.30. Overall, the higher-than-expected PCI balance is a negative shock to the market. We keep our NAV estimate (HK\$ 12.08) and TP of HK\$ 7.30 unchanged, which is still based on discount of 40% to NAV. While the market perceives Evergrande's high debt level to be largely negative, we believe the Group's consistency in delivering higher-than-peer presales growth with a stable margin despite a high base is sufficient to justify the associated risk. Maintain **BUY**.

Risks factors: 1) Gearing can be understated with the use of perpetual securities; 2) Loss in non-property business may increase on the weakening economy; 3) Increase in SG&A expenses and PCI coupon payment

Exhibit 1: Evergrande's 1H16 results

P&L	1H16	1H15	YoY Chg	Operating statistics	1H16	1H15	YoY Chg
	RMB mn	RMB mn	(%)				(%)
Turnover	87,498	77,743	13	Presales GFA (mn sqm)	16.6	11.4	46
Cost of Sales & direct operating costs	(62,728)	(55,673)	13	Presales ASP (RMB/sqm)	8,538	7,656	12
Gross Profit	24,770	22,070	12	Presale (RMBmn)	141,780	87,110	63
Gross Margin (%)	28.3	28.4	(0.1ppt)	GFA Delivered (mn sqm)	10.8	10.8	0
Selling and distribution costs	(8,029)	(5,300)	51	Booked ASP (RMB/sqm)	7,754	7,004	11
Administrative expense	(5,284)	(3,516)	50	Property sales booked (RMBmn)	83,740	75,370	11
EBIT	11,457	13,254	(14)	Segment EBIT			
EBIT Margin (%)	13.1	17.0	(4.0ppt)	Property development	13,977	15,829	(12)
Other income, gains and losses	1,875	1,217	54	Property investment	212	69	206
Fair value gain of investment properties	3,283	5,534	(41)	Property management	99	(132)	(175)
Gain on financial assets at fair value	(425)	2,481	na	Others business	(1,027)	(1,488)	(31)
Exchange gain/(losses)	(1,572)	27	na	Total	13,261	14,278	(7)
Share of profit from JCE/ Associates	(71)	39	0	Balance sheet	Jun 16	Dec 15	HoH
Finance cost	(210)	(634)	(67)		RMBmn	RMBmn	(%)
Profit before tax	14,337	21,918	(35)	Gross debt	381,261	296,906	28
Tax	(7,210)	(8,632)	(16)	Cash	212,003	132,884	60
- LAT	(3,159)	(3,002)	5	Net debt	169,258	164,022	3
- Enterprise tax	(4,157)	(3,898)	24	Perpetual capital instruments	116,002	75,737	53
- Deferred tax	106	(1,732)	(106)	Total Equity	182,048	142,142	28
Profit after tax	7,127	13,286	(46)	Net gearing- PCI as equity (%)	93.0	93.5	(0.5)
MI and perpetual capital instrument	(5,110)	(3,860)	32	Net gearing- PCI as debt (%)	431.9	261.8	170.1
Net profit	2,017	9,426	(79)	Major P&L items	1H16	1H15	YoY Chg
Core net profit	7,810	10,160	(23)	Perpetual coupon payment	4,220	2,611	62
Core net profit- after MI and perpetual	2,700	6,300	(57)	Gross finance cost	13,549	7,879	72
				Donation	1,124	123	814

Source(s): Company, ABCI Securities

Exhibit 2: Evergrande's FY16E NAV

	Attr. GFA (mn sqm)	Net assets value (RMB mn)	% of total	Valuation Method	Implied value per sqm (RMB)
Property development					
Guangdong	14.8	14,108	5%		950
Liaoning	13.2	11,200	4%		847
Jiangsu	12.9	11,088	4%		858
Hebei	11.7	10,884	4%	DCF at	927
Shangdong	10.8	10,071	3%	WACC of	934
Anhui	10.0	8,152	3%	10.3%	818
Henan	7.7	6,839	2%		889
Hunan	5.4	4,713	2%		880
Others	64.2	118,548	38%		1,846
Subtotal	150.8	195,604	63%		1,298
Investment Properties		97,216	31%	1x P/B	
Football business		1,200	0%	50% stake sold to Jack Ma at RMB1.2bn	
Financial investment		14,736	5%	Market value of Shengjing Bank	
Consumer and O2O business		-	0%		
Total 2016E GAV		308,756	100%		
2016E Net debt		(97,886)	-32%		
Perpetual capital instrument		(65,737)	-21%		
Total 2016E NAV		145,134	47%		
No. of share outstanding (diluted)		14,411			
NAV per share (RMB)		10.07			
Exchange rate		1.20			
NAV per share (HKD)		12.08			
Target discount (%)		40%			
Target Price (HKD)		7.30			
WACC	10.3%				
Cost of Debt	8.2%				
Cost of Equity	20.0%				
Debt/ (Debt + Equity)	70%				

Source(s): Company, ABCI Securities estimates



Consolidated income statement (2013A-2018E)

FY Ended Dec 31 (RMB mn)	2013A	2014A	2015A	2016E	2017E	2018E
Revenue	93,672	111,398	133,130	196,559	236,057	228,178
Cost of sales	(66,023)	(79,615)	(95,717)	(138,872)	(166,144)	(158,464)
Gross Profit	27,649	31,784	37,413	57,687	69,913	69,714
SG&A expenses	(9,462)	(14,588)	(20,541)	(30,207)	(29,522)	(22,952)
EBIT	18,187	17,195	16,872	27,480	40,391	46,761
Finance cost	(34)	(1,015)	(807)	(1,687)	(1,482)	(1,276)
Share of profit of associates	0	(104)	(392)	1,285	2,150	2,388
Other income/ (expenses)	699	1,431	2,262	918	1,090	1,297
Fair value gain of investment properties	0	0	0	0	0	0
Disposal/one-off items	6,545	13,685	13,510	0	0	0
Profit before tax	25,396	31,191	31,445	27,996	42,150	49,170
Tax	(11,687)	(13,175)	(14,105)	(15,900)	(22,285)	(24,838)
Profit after tax	13,709	18,016	17,340	12,096	19,865	24,332
Minority interest	(1,097)	(5,412)	(6,880)	(5,959)	(5,466)	(4,773)
Reported net profit	12,612	12,604	10,460	6,137	14,399	19,559
<i>Less: exceptional items</i>	<i>(4,908)</i>	<i>(9,134)</i>	<i>(8,469)</i>	<i>(0)</i>	<i>(0)</i>	<i>0</i>
Underlying net profit	7,703	3,470	1,992	6,137	14,399	19,559
Per share						
Underlying EPS (RMB)	0.48	0.24	0.14	0.43	1.00	1.36
DPS (RMB)	0.43	0.43	0.38	0.21	0.50	0.68
Payout ratio (%)	90%	183%	275%	50%	50%	50%
BVPS (RMB)	4.59	7.05	8.79	8.31	8.12	8.10
Growth %						
Revenue	43.5%	18.9%	19.5%	47.6%	20.1%	-3.3%
Gross Profit	51.8%	15.0%	17.7%	54.2%	21.2%	-0.3%
EBIT	59.1%	-5.5%	-1.9%	62.9%	47.0%	15.8%
Underlying net profit	24.2%	-54.9%	-42.6%	208.1%	134.6%	35.8%
Margin %						
Gross margin	29.5%	28.5%	28.1%	29.3%	29.6%	30.6%
Gross margin (post-LAT)	24.7%	25.6%	26.1%	25.8%	26.0%	27.1%
EBIT margin	19.4%	15.4%	12.7%	14.0%	17.1%	20.5%
Core net margin	9.4%	7.1%	5.7%	5.5%	7.5%	9.6%
Key assumptions						
Contracted Sales (RMB mn)	100,400	131,510	201,340	270,284	260,464	182,024
GFA sold (mn sqm)	14.89	18.20	25.51	32.60	31.21	22.53
ASP (RMB/sqm)	6,741	7,228	7,892	8,292	8,346	8,079
Booked Sales (RMB mn)	92,235	107,450	126,449	187,936	225,673	215,614
GFA delivered (mn sqm)	14.96	16.84	17.24	23.62	27.62	26.38
Booked ASP (RMB/sqm)	6,166	6,382	7,334	7,958	8,170	8,174

Source: Company, ABCI Securities estimates



Consolidated balance sheet (2013A-2018E)

As of Dec 31 (RMB mn)	2013A	2014A	2015A	2016E	2017E	2018E
Current assets	289,378	383,650	612,344	652,243	685,277	662,799
Cash	40,118	29,847	103,090	138,088	215,697	273,221
Restricted cash	13,535	29,651	60,932	60,932	60,932	60,932
Trade & other receivables	9,512	16,027	21,708	21,708	21,708	21,708
Property under development	184,833	246,476	383,728	388,628	344,054	264,052
Other current assets	41,381	61,649	42,886	42,886	42,886	42,886
Non-current assets	58,770	90,812	144,691	159,837	159,794	159,753
Property, plant & equipment	11,378	15,504	16,720	15,121	13,361	11,426
Investment properties	36,039	61,857	97,146	97,216	97,286	97,356
Investment in Associate and JCE	0	1,062	8,580	25,256	26,902	28,726
Other non-current assets	11,353	12,389	22,245	22,245	22,245	22,245
Total Assets	348,148	474,462	757,035	812,080	845,070	822,553
Current Liabilities	188,198	268,237	456,681	518,106	553,345	530,496
Short term borrowings	35,796	79,663	158,744	158,744	158,744	158,744
Trade & other payables	99,895	123,673	191,309	190,284	189,260	188,235
Pre-sales deposits	39,000	47,348	83,061	145,510	181,774	159,950
Other current assets	13,506	17,553	23,567	23,567	23,567	23,567
Non-current liabilities	80,608	93,847	158,212	158,212	158,212	158,212
Long term borrowings	73,021	76,401	138,162	138,162	138,162	138,162
Other payables	0	0	0	0	0	0
Other non-current assets	7,587	17,446	20,050	20,050	20,050	20,050
Total Liabilities	268,806	362,084	614,893	676,318	711,557	688,708
Net Assets	79,343	112,378	142,142	135,762	133,513	133,845
Shareholders' Equity	48,590	51,120	60,613	63,682	70,881	80,661
Perpetual capital instrument	25,024	52,852	66,130	56,130	46,130	36,130
Minority Interest	5,729	8,406	15,399	15,951	16,503	17,054
Total Equity	79,343	112,378	142,142	135,762	133,513	133,845
Key ratio						
Gross debt (RMBm)	108,817	156,065	296,906	296,906	296,906	296,906
Net debt (RMBm)	55,164	96,566	132,884	97,886	20,277	(37,247)
Net gearing (%)	70%	86%	93%	72%	15%	-28%
Contracted sales/ Total assets (x)	0.29	0.28	0.27	0.33	0.31	0.22

Source(s): Company, ABCI Securities estimates



Consolidated cash flow statement (2013A-2018E)

FY ended Dec 31 (RMB mn)	2013A	2014A	2015A	2016E	2017E	2018E
EBITDA	19,214	18,332	18,326	29,080	42,151	48,697
Change in Working Capital	(44,409)	(52,024)	(25,704)	79,183	99,710	74,285
Tax payment	(5,850)	(13,175)	(14,105)	(15,900)	(22,285)	(24,838)
Operating cash flow	(31,045)	(46,868)	(21,483)	92,363	119,575	98,143
Addition of PP&E and IP	(11,782)	(1,532)	(10,246)	(70)	(70)	(70)
Others	(1,353)	(1,869)	12,905	(14,472)	1,595	1,859
Investing cash flow	(13,134)	(3,402)	2,659	(14,542)	1,525	1,789
Debt raised	74,368	52,794	115,470	5,000	5,000	5,000
Debt repaid	(25,463)	(5,000)	(641)	(5,000)	(5,000)	(5,000)
Interest expenses	(7,827)	(14,649)	(21,102)	(24,346)	(21,377)	(18,408)
Equity raised	3,526	0	(658)	0	0	0
Dividend to shareholders	(2,292)	(6,339)	(5,476)	(3,068)	(7,199)	(9,779)
Perpetual securities raised	24,367	13,241	(5,083)	(15,357)	(14,864)	(14,171)
Others	(174)	(50)	9,557	(50)	(50)	(50)
Financing cash flow	66,506	39,997	92,067	(42,822)	(43,491)	(42,409)
Net cash inflow/ (outflow)	22,327	(10,272)	73,243	34,998	77,609	57,524
Cash- beginning	17,789	40,118	29,847	103,090	138,088	215,697
Cash- Year end	40,116	29,847	103,090	138,088	215,697	273,221

Source(s): Company, ABCI Securities estimates

Disclosures

Analyst Certification

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Definition of equity rating

Rating	Definition
Buy	Stock return \geq Market return rate
Hold	Market return – 6% \leq Stock return < Market return rate
Sell	Stock return < Market return – 6%

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate

Time horizon of share price target: 12-month

Definition of share price risk

Rating	Definition
Very high	$2.6 \leq$ 180 day volatility/180 day benchmark index volatility
High	$1.5 \leq$ 180 day volatility/180 day benchmark index volatility < 2.6
Medium	$1.0 \leq$ 180 day volatility/180 day benchmark index volatility < 1.5
Low	180 day volatility/180 day benchmark index volatility < 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index.

Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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