



September 8, 2016  
Company Report  
Rating: BUY  
TP: HK\$ 3.30

Share price (HK\$) 2.72  
Est. share price return 21.3%  
Est. dividend yield 7.7%  
Est. total return 29.0%

Previous Rating & TP NA  
Previous Report Date NA

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**Key Data**

52Wk H/L(HK\$)	2.79/1.59
Issued shares (mn)	3,816
Market cap (HK\$ mn)	10,380
3-mth avg daily turnover (HK\$ mn)	18.22
Major shareholder(s) (%):	
LAM Lung On & KWOK Ying Lan	68.0%

Source(s): Company, Bloomberg, ABCI Securities

**1H16 Revenue breakdown (%)**

Property development	97.0
Property management	1.5
Property investment	1.2
Hotels & others	0.3

Source(s): Company, ABCI Securities

**Share performance (%)**

	Absolute	Relative*
1-mth	8.8	3.1
3-mth	27.1	14.0
6-mth	64.4	38.4

\*Relative to HSI

Source(s): Bloomberg, ABCI Securities

**1-Year stock performance (HK\$)**



Source(s): Bloomberg, ABCI Securities

**Yuzhou (1628 HK)**

**Top developer in Xiamen and Hefei; initiate BUY**

- Yuzhou was among the top home sellers in Xiamen and Hefei in FY15. In 7M16, Yuzhou's presales surged 121%YoY to RMB 14.8bn, with Xiamen and Hefei accounting for 33% and 26% of total
- Despite margin erosion across the sector, Yuzhou's gross margin has never dropped below 30% in the past 6 years.
- Average cost of debt declined from 7.0% in FY15 to 6.3% in 1H16
- Initiate **BUY** with TP of HK\$3.30 based on a 60% discount to NAV

**A market leader in Xiamen and Hefei.** As at June 2016, Yuzhou has a total landbank of 9.04mn sqm, with Hefei and Xiamen accounting for 30% and 20% of total. In terms of GFA sold, Yuzhou was ranked first in Xiamen and second in Hefei in 2015. In 7M16, Xiamen and Hefei accounted for 33% and 26% of total presales, while Shanghai and Nanjing were the third and fourth largest contributors taking up 13% and 11%. Based on CRIC, 66% of homes sold in Xiamen were purchased by the non-locals in 2015, indicating huge external property demand. Xiamen's average property price (RMB 28k/sqm in Aug 2016) was ranked fourth in China, based on the statistics from fang.com. Population inflow to Hefei, the provincial capital of Anhui province, has been expanding. Property price in Xiamen and Hefei rallied 25% and 26% during 8M16. Driven by the two thriving cities, we expect Yuzhou's presales to jump 58%YoY to RMB 22.2bn in FY16, in line with its revised presales target of RMB 22bn.

**Impressive margins.** Yuzhou's gross margin has been consistently higher than most of its peers. In 2015, Yuzhou's gross margin was 35.8%, as compared to the sector average of 27.2%. Although land competition intensifies, we believe Yuzhou would maintain its gross margin at 30%+ given its ability to raise ASP. In 1H16, the Group's presales ASP was RMB 12.7k /sqm, 27% higher than the RMB 9,997/sqm in FY15.

**Decreasing cost of debt.** Yuzhou's finance cost has been falling from its peak of 9.7% since 2012 to 6.3% in 1H16. Increasing recognition in the bond market has contributed to the improvement. Coupon rate of Yuzhou's USD bonds dropped from 11.75% in 2012 to just 9% in 2014. In 2015, Yuzhou also raised RMB 2.0bn and RMB 3.0bn via the 3-year and 5-year corporate bonds in Oct 2015 and Dec 2015, with the respective coupon rates are 6.7% and 5.1%.

**Initiate BUY with TP of HK\$ 3.30 based on a 60% discount to NAV.** Based on the discount-to-NAV valuation, we apply a WACC of 10.5% for Yuzhou's property development projects (RMB 34.7bn) and a 6% cap rate for the investment properties (RMB 1.3bn). A 60% discount is applied to our 2016E NAV estimate of RMB 27.0bn (or HK\$ 8.35/ share); hence, our TP arrives at HK\$ 3.3/shr. Trading at 4.6x 2016PE with a 2016E yield of 7.7% yield, the counter is attractively valued with positive prospects in both Xiamen and Hefei. Initiate with **BUY**.

**Results and Valuation**

FY ended Dec 31	2014A	2015A	2016E	2017E	2018E
Revenue (RMB mn)	7,837	10,376	12,850	17,489	23,761
Chg (% YoY)	4.9	32.4	23.9	36.1	35.9
Core net profit (RMB mn) <sup>1</sup>	1,025	1,620	1,935	2,588	3,545
Chg (% YoY)	(6.0)	58.0	19.4	33.8	37.0
Underlying EPS (RMB)	0.30	0.44	0.51	0.68	0.93
Chg (% YoY)	(6.0)	48.5	15.1	33.8	37.0
BVPS (RMB)	2.36	2.62	2.82	3.22	3.76
Chg (% YoY)	11.0	10.6	7.8	14.1	17.0
Underlying PE (x)	7.8	5.3	4.6	3.4	2.5
P/B (x)	1.0	0.9	0.8	0.7	0.6
ROE (%)	12.5	16.8	18.0	21.1	24.7
ROA (%)	2.6	3.1	2.9	3.4	4.3
DPS(HK\$)	0.16	0.18	0.21	0.28	0.38
Yield (%)	5.9	6.6	7.7	10.3	14.1
Net gearing <sup>2</sup> (%)	59.8	79.4	79.5	Net Cash	Net Cash

<sup>1</sup>Core net profit = Net profit - revaluation gain of investment properties and one-off items

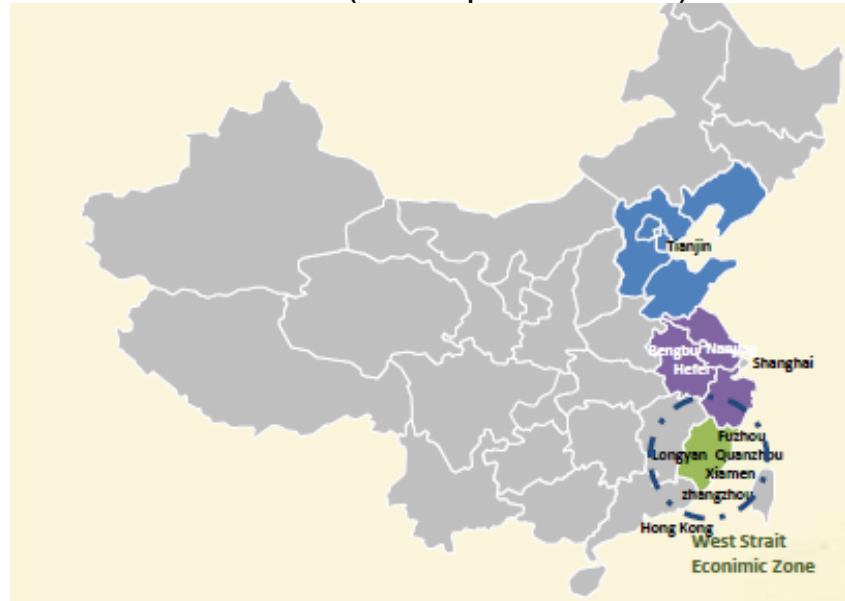
<sup>2</sup>Net gearing = Net debt / Shareholders' equity

Source(s): Bloomberg, ABCI Securities estimates

## A market leader in Xiamen and Hefei

Since its HK listing in 2009, Yuzhou has expanded its geographic presence from its headquarter Xiamen to three major economic regions, including the West Strait Economic Zone (Xiamen, Fuzhou, Quanzhou, Longyan), Yangtze River Delta (Shanghai, Nanjing, Hefei, Bengbu) and Bohai Rim (Tianjin). As at June 2016, Yuzhou has a total landbank of 9.04mn sqm, with Hefei and Xiamen accounting for 30% and 20% of total.

**Exhibit 1: Yuzhou's landbank (9.04mn sqm as at June 2016)**



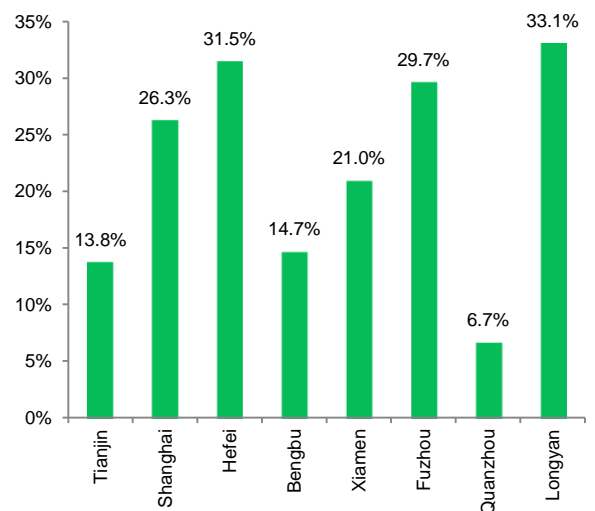
Source(s): Company, ABCI Securities

**Exhibit 2: Yuzhou's land cost by city (June 2016)**

City	Saleable GFA	No of project	Average land cost	% of saleable GFA
	('000 sqm)		RMB/sqm	%
Tianjin	326	2	1,061	4%
Shanghai	926	9	5,875	10%
Nanjing	517	6	9,286	6%
Hefei	2,735	11	2,562	30%
Bengbu	586	1	660	6%
Xiamen	1,769	24	4,076	20%
Fuzhou	644	4	3,192	7%
Quanzhou	1,073	1	374	12%
Longyan	207	1	1,921	2%
Zhangzhou	255	1	2,400	3%
Hong Kong	2	1	135,140	0%
	<b>9,040</b>	<b>61</b>	<b>4,035</b>	<b>100%</b>

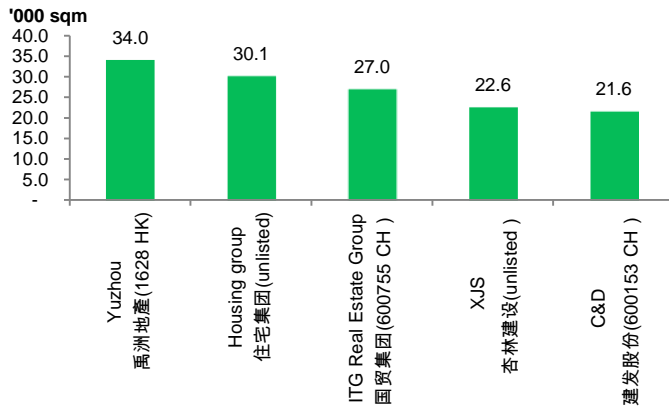
Source(s): Company, ABCI Securities

**Exhibit 3: Unit cost-to- presales ASP ratio in 1H16 for Yuzhou**

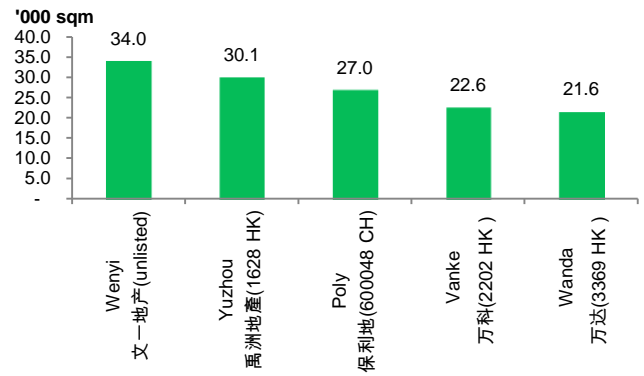


Source(s): Company, ABCI Securities

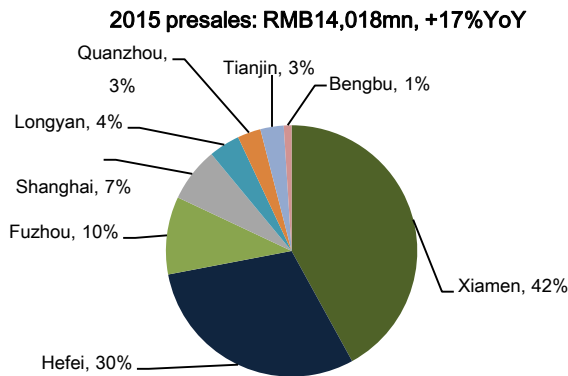
In 2015, Yuzhou was a leader in Xiamen and Hefei, ranking first and second in Xiamen and Hefei by GFA sold respectively. In 7M16, Xiamen and Hefei accounts for 33% and 26% of its total presales, while Shanghai and Nanjing were the 3<sup>rd</sup> and 4<sup>th</sup> cities with the highest presales, contributing to 13% of 11% of Yuzhou's total presales.

**Exhibit 4: Top 5 developers by GFA sold in Xiamen (2015)**


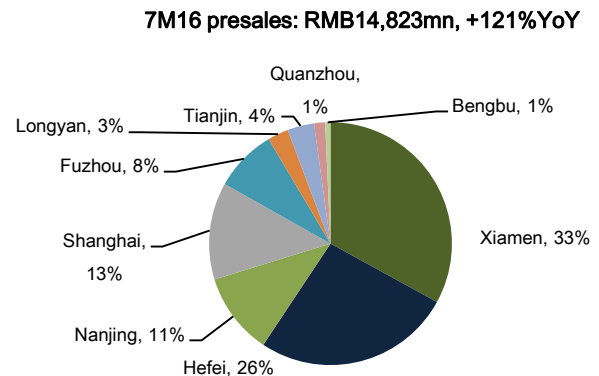
Source(s): Company, ABCI Securities

**Exhibit 5: Top 5 developers by GFA sold in Hefei (2015)**


Source(s): Company, ABCI Securities

**Exhibit 6: Presales breakdown (2015)**


Source(s): Company, ABCI Securities

**Exhibit 7: Presales breakdown (7M16)**


Source(s): Company, ABCI Securities

Yuzhou has various strategic investors from Xiamen and Taiwan. Xiamen ITG and Xiamen C&D, the two major SOEs in Xiamen, currently own 1.1% and 0.2% stakes in Yuzhou and were the cornerstone investors for the Group's IPO listing. Taiwan Life (with a 1.8% stake in Yuzhou) and Taiwan Transglobe Life (a 0.5% stake) were also introduced during the new share placement in 2015. Hengan's CEO (Xu Lianjia) also owned a 0.5% stake in the Group.

Mr Lam Lung On, Yuzhou's Chairman who owns a 68% stake in Yuzhou, has over 20 years of working experience in Xiamen's property market. In particular, he worked for the SOE Xiamen Land Development Company, before establishing the Group in 1994.

**Exhibit 8: Shareholding structure**

LAM Lung On & KWOK Ying Lan	68.00%
Xiamen ITG *	1.10%
Xiamen C&D *	0.20%
Norges Bank	0.10%
Taiwan Life	1.80%
Taiwan Transglobe Life	0.50%
Xu Lianjia, CEO of Hengan (1044 HK)	0.50%
Public	27.80%
<b>Total</b>	<b>100.00%</b>

\* Major SOEs in Xiamen  
 Source(s): Company, ABCI Securities

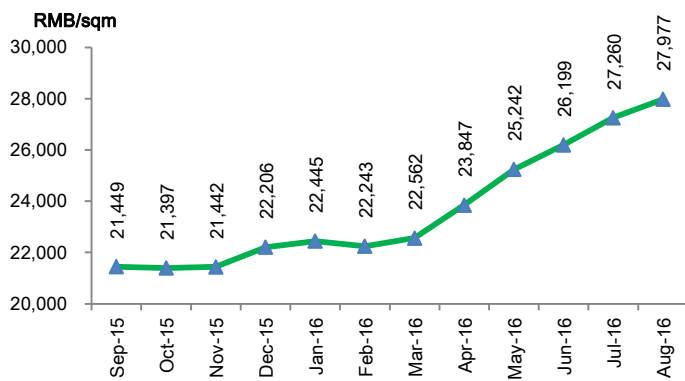
## Property boom in Xiamen and Hefei

Xiamen and Hefei accounted for 42% and 30% of FY15 presales. Driven by the thriving property market in the two cities, sales and ASP turn increasingly promising.

### Xiamen- property market driven by the non-locals

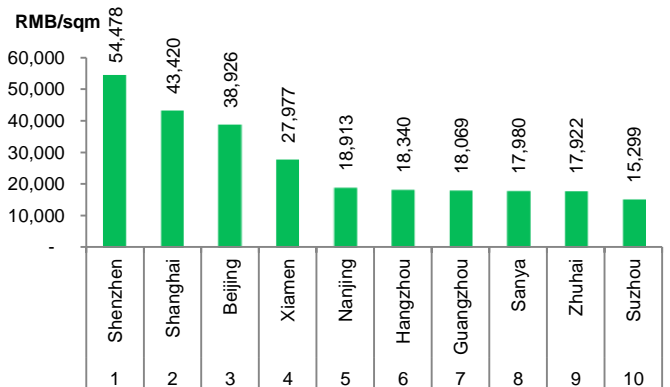
Xiamen, the only sub-provincial city in Fujian Province, is considered as a migrant city. Following Shenzhen and Dongguan, Xiamen has the 3<sup>rd</sup> highest non-local-to-local resident ratio of 2.05:1. Based on CRIC, out of the 3.52mn sqm of homes sold in Xiamen in 2015, 66% were taken up by the non-locals, indicating a huge external property demand. In fact, Xiamen's average property price was ranked 4<sup>th</sup> among the Chinese cities, rallying by 26% in the first 8 months of 2016 to RMB 28k/sqm according to fang.com.

Exhibit 9: Xiamen property price



Source(s): fang.com

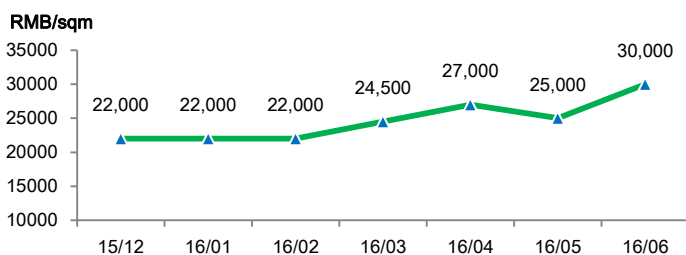
Exhibit 10: Top 10 cities by property price (Aug 16)



Source(s): fang.com

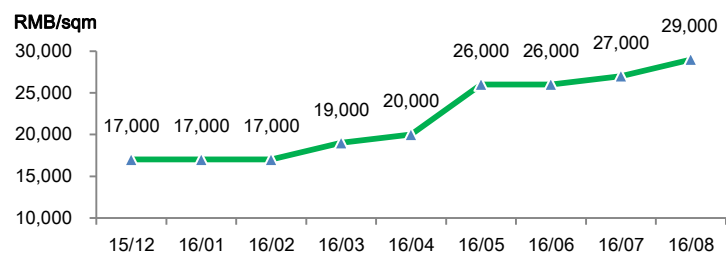
Yuzhou has a total landbank 1.8mn sqm in Xiamen with a low land cost of RMB 4,076/sqm. Key projects launched in 1H16 included Chunjiang Central, Haicang Dream Town, and Yuzhou Lucca Town. Based on Fang.com, the ASP range was RMB 29k–30k/sqm in Aug 2016, compared to RMB 17k–22k/sqm in Dec 2015.

Exhibit 11: Haicang Dream Town (海沧万科城)



Source(s): fang.com

Exhibit 12: Yuzhou Lucca Town (禹洲·盧卡小鎮)

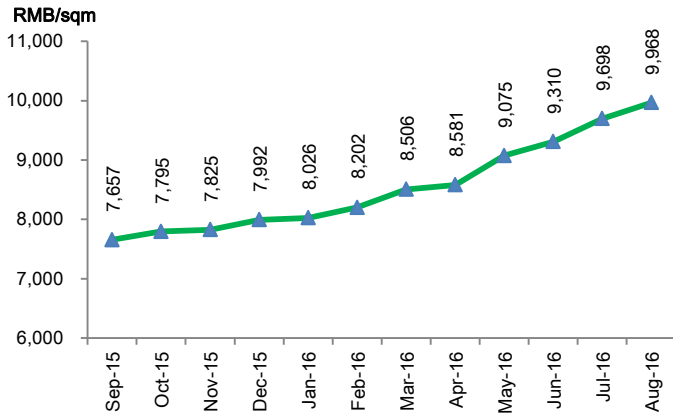


Source(s): fang.com



### Hefei: tight housing supply with only a 2-month inventory level

Hefei, being the provincial capital of Anhui province, attracts an ever-expanding inflow of population. As of end-2015, Hefei had a total population of 7.76mn, up 1.2% YoY. Nominal GDP also rose 10.5%, outperforming the national growth by 3.6ppt. According to CRIC, Hefei had one of the lowest housing inventory levels in China of 2.0 months as of June 2016. Given such a demand-supply imbalance, Hefei's property price rose 25% during the first 8 months of 2016, according to Fang.com

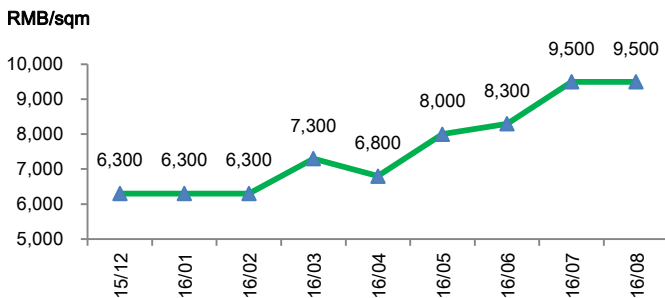
**Exhibit 13: Hefei property price**


Source(s): fang.com

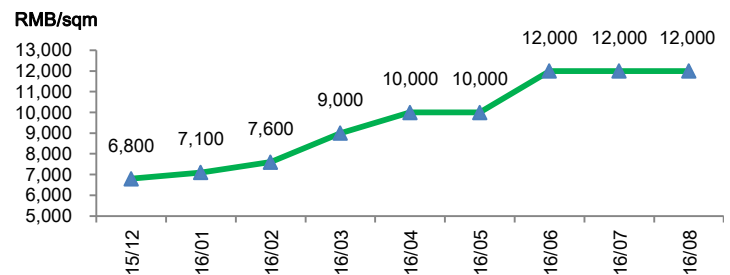
**Exhibit 14: Bottom 10 cities by inventory level (Jun 2016)**


Source(s): CRIC

In 2016, major Yuzhou projects available for sale include Yuzhou Skyline and Yuzhou Central Plaza. According to Fang.com, the two projects are selling at an ASP of RMB9,500-12,000/sqm in Aug 2016, compared to RMB 6,300-6,800/sqm in Dec 2015

**Exhibit 15: Yuzhou Skyline (禹洲·天境)**


Source(s): fang.com

**Exhibit 16: Yuzhou Central Plaza (禹洲·中央廣場)**


Source(s): fang.com



### New rounds of tightening have just begun

Following the policy tightening in Shenzhen and Shanghai since Mar 2016, various non-tier 1 cities, including Hefei, Suzhou, Nanjing, Xiamen and Wuhan, have also implemented restrictive measures (mortgage and home purchase restrictions) since June.

**Exhibit 17: Policy tightening for non-tier 1 cities in 2016**

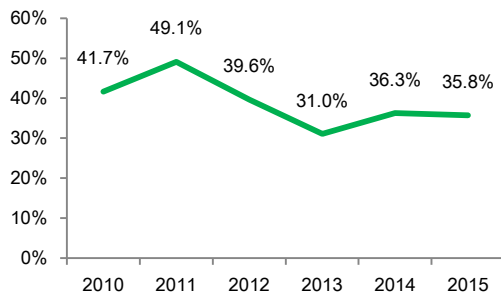
City	Month	Mortgage restriction	Home purchases restriction (HPR)
Hefei	24-Jun	- Down payment ratio was raised to 40% (from 25%) for homebuyers owning one property unit even if the respective mortgage loan has been fully repaid; - Down payment was raised to 50% (from 40%) for homebuyers owning two property units; no mortgage shall be granted for buyers with three or more property units.	None
Suzhou	11-Aug	- Down payment for homebuyers who has one outstanding mortgage loan was raised to 50% from 40%.	- Non-Suzhou residents were required to provide social security payment record of at least 1 year when they purchase the second home, while third-home purchases are prohibited.
Nanjing	11-Aug	- For homebuyers owning one property unit with the mortgage being fully repaid, down payment was raised to 35% from 30% - For homebuyers with one outstanding mortgage loan, down payment was raised to 50% from 40%.	None
Wuhan	31-Aug	- For 1) homebuyers owning one property unit; or 2) homebuyers owning two property units with a least one mortgage loan redeemed, down payment was raised to 40% from 30%; - Mortgage is suspended for homebuyers with two or more property units or two outstanding mortgage loans.	None
Xiamen	5-Sep	- Mortgage down payment was raised to 60% for homebuyers with one outstanding mortgage loan; homebuyers with two or more outstanding mortgage loans cannot apply for a third mortgage.	- New or second -handed property cannot be sold to 1) Xiamen residents with two or more property units; 2) Non-Xiamen residents with 1 or more property units.

Source(s): Local governments, ABCI Securities

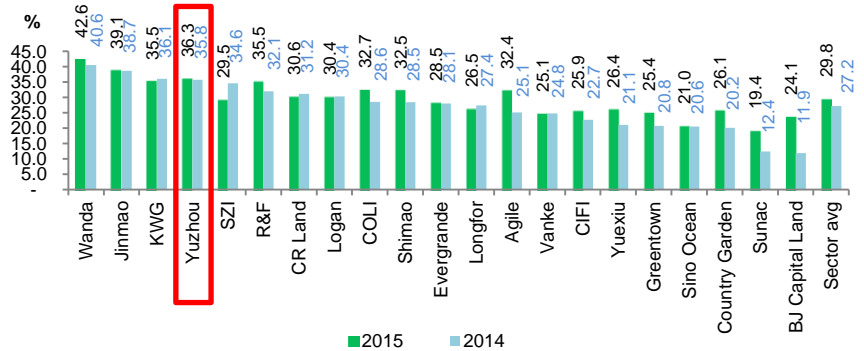
These measures, in our view, are relatively mild given most of them are targeting at the speculative buyers. Demand from the first-home buyers should be relatively unaffected. In Shenzhen and Shanghai, property price in Mar-Aug grew 11.3% and 11.2%, indicating buying sentiment has remained positive despite the additional restrictions applied.

## Impressive margins

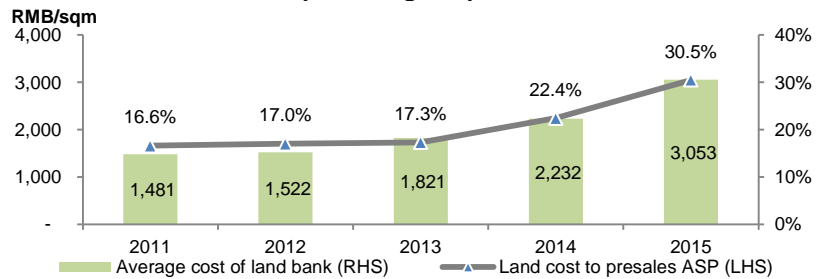
Yuzhou's gross margin is usually higher than that of its peers. The figure was 35.8% in FY15, higher than the sector average of 27.2%. Despite a sector-wide trend of declining profitability, Yuzhou's gross margin has never fallen below 30% in the past 6 years when market leaders, such as COLI, recorded a reduced gross margin of 28.6% in 2015. As land competition turns stiff, however, we expect margin pressure to increase. In 1H16, average land cost of Yuzhou's landbank rose 32% HoH to RMB 4,035/sqm, while land cost-to-ASP ratio increased from 30.5% in FY15, to 31.7% in 1H16. However, we project Yuzhou to maintain its gross margin at above 30% given its ability to raise ASP in Xiamen and Hefei. In 1H16, Yuzhou achieved a presales ASP of RMB 12.7k/sqm, 27% higher than its FY15 presales ASP of RMB 9,997/sqm.

**Exhibit 18: Yuzhou's gross margin**


Source(s): Company, ABCI Securities

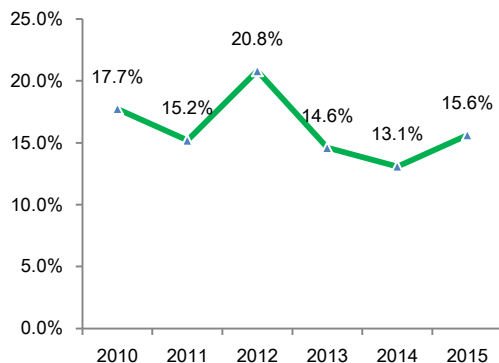
**Exhibit 19: Gross margin comparison of the HK-listed mainland developers**


Source(s): Company, ABCI Securities

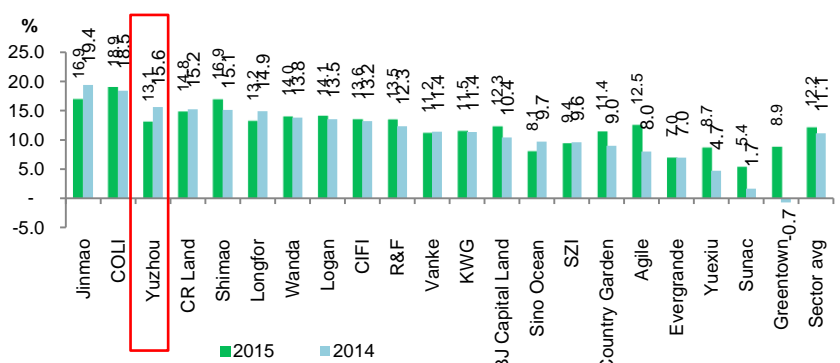
**Exhibit 20: Land cost as a percentage of presales ASP**


Source(s): Company, ABCI Securities

Thanks to Yuzhou's concentrated landbank portfolio and discipline in SG&A saving, its core profit margin at 15.6% was also much higher than the peer average of 11.1%.

**Exhibit 21: Core net margin**


Source(s): Company, ABCI Securities

**Exhibit 22: Core net margin vs. peers**


Source(s): Company, ABCI Securities



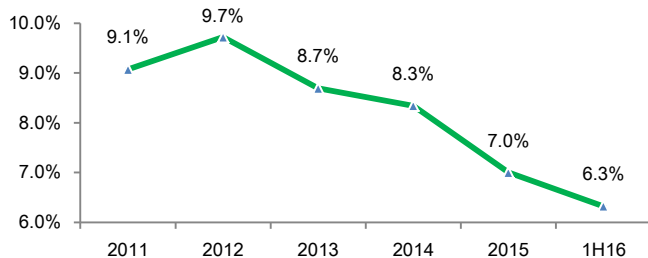
## Decreasing cost of debt

Yuzhou's financing cost has been falling from the peak at 9.7% since 2012 to 6.3% in 1H16. Apart from the effect of rate cuts in China over the past two years, the Group's increasing recognition in the bond market also help reduce its finance cost. Coupon rate of Yuzhou's USD bonds dropped from 11.75% in its first issuance in 2012 to just 9% in 2014. In 2015, Yuzhou also raised RMB 2.0bn and RMB 3.0bn through the 3- and 5-year corporate bonds issued in Oct and Dec 2015; the respective coupon rates were 6.7% and 5.1%.

Separately, Yuzhou successfully placed 360mn of new shares (10.42% dilution) at HK\$ 2.20/share (12.4% discount to closing price prior to issuance) to raise HK\$ 779mn in May 2015. This has helped strengthen Yuzhou's balance sheet and improve its credit profile.

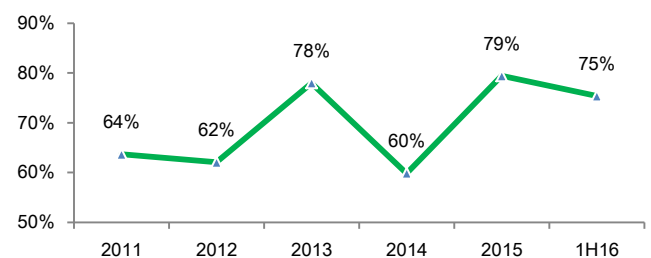
In 2016, we expect Yuzhou to redeem some of the high-cost offshore debts at an earlier date to lower finance cost. In particular, Yuzhou has redeemed HK\$1.5bn of guaranteed bonds with a 10% coupon (the China Life bonds) due 2019 in Feb 2016.

Exhibit 23: Yuzhou's weighted average cost of debt



Source(s): Company, ABCI Securities

Exhibit 24: Yuzhou's net gearing



Source(s): Company, ABCI Securities

Exhibit 25: Yuzhou's FY15 cash flow

	2015	FY16E	YoY	1H16
	RMBbn	RMBbn	chg	RMBbn
Presales	14	16	14%	12.9
Cash collection rate	93%	94%	+1ppt	98%
<b>Sales proceeds</b>	<b>13.1</b>	<b>15</b>	<b>15%</b>	<b>12.6</b>
<b>Other income</b>	<b>0.3</b>	<b>0.4</b>	<b>28%</b>	<b>0.3</b>
<b>Operating cash in flow</b>	<b>13.4</b>	<b>15.4</b>	<b>15%</b>	<b>12.9</b>
Land	6.4	5	-21%	6.5
Construction	4.5	4.7	4%	3.1
JV spending	1.2	-	na	-
Others expenses	4.4	5.3	19%	2.9
<b>Operating cash out flow</b>	<b>16.5</b>	<b>15</b>	<b>-10%</b>	<b>12.6</b>
<b>Net operating cash flow</b>	<b>-3.1</b>	<b>0.5</b>	<b>-115%</b>	<b>0.3</b>
Equity raising	0.6	-	na	-
Net change in debt	4.7	-1.2	-126%	3.4
<b>Change in cash</b>	<b>2.2</b>	<b>-0.8</b>	<b>-136%</b>	<b>3.7</b>

Source(s): Company, ABCI Securities estimates

Exhibit 26: Yuzhou's land acquisition in 1H16

Month	City	Stake %	Saleable GFA 000 sqm	Land cost RMB mn	Ava. land cost RMB/sqm
Jan-16	Shanghai	40%	91	2,630	28,972
Jan-16	Nanjing	100%	61	710	11,610
Feb-16	Fuzhou	67%	137	1,730	12,590
Apr-16	Hefei	100%	235	2,389	10,170
Apr-16	Hefei	100%	59	718	12,120
Apr-16	Hefei	100%	357	1,821	5,100
Jun-16	Hefei	100%	101	1,119	11,086
Jul-16	Hangzhou	100%	145	4,104	13,818
<b>Total</b>			<b>1,339</b>	<b>15,221</b>	<b>11,371</b>

Source(s): Company, ABCI Securities

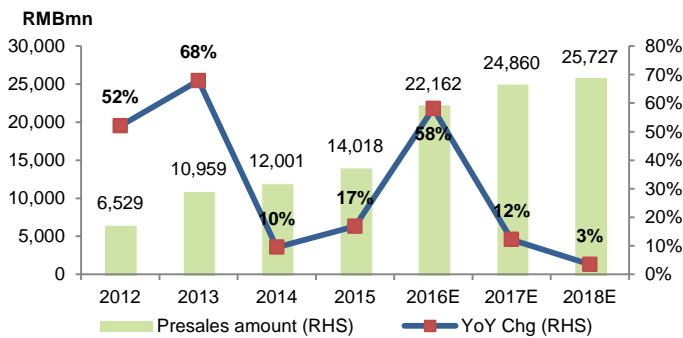


## Financial analysis

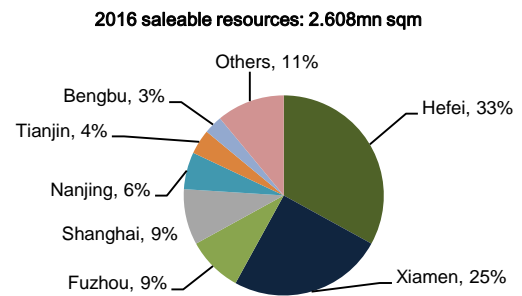
### Strong core profit growth at 22% CAGR in 2015-18E

We expect Yuzhou's presale to expand by 22% CAGR from RMB 14.0bn in 2015 to RMB 25.7bn in 2018E on the back of surging property markets in Xiamen and Hefei. For 2016, about 58% of the total saleable resources at 2.608mn sqm are from the two cities. We expect 2016 presale to jump 58% YoY to RMB 22.2bn, similar to its revised sales target of RMB 22bn for 2016 (RMB16bn previously).

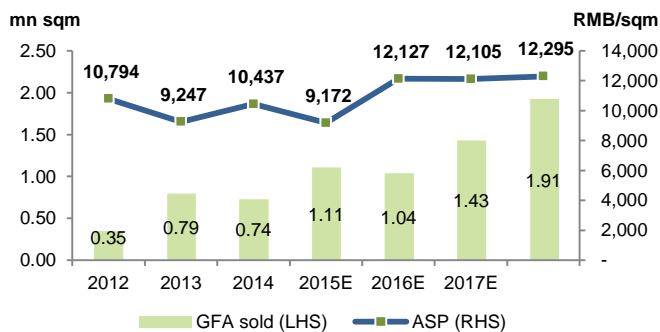
In line with the industry trend of declining margins, we expect the Group's gross margin to drop from 35.8% in FY15 to 32.4% in 2018E due to the rising land cost. Based on the price increase observed in 1H16, we expect 2016E gross margin to remain stable on higher ASP in Xiamen and Hefei. To be conservative, we assume a flat ASP growth for 2017E/18E, hence gross margin would decline. Driven mainly by volume growth, we expect core profit to surge from RMB 1.6bn in 2015 to RMB 3.5bn in 2018E, implying a 30% CAGR in 2015-18E.

**Exhibit 27: Yuzhou's presales**


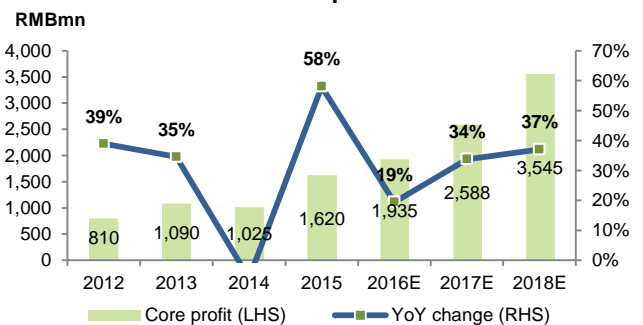
Source(s): Company, ABCI Securities estimates

**Exhibit 28 : Yuzhou's 2016E saleable resources by GFA**


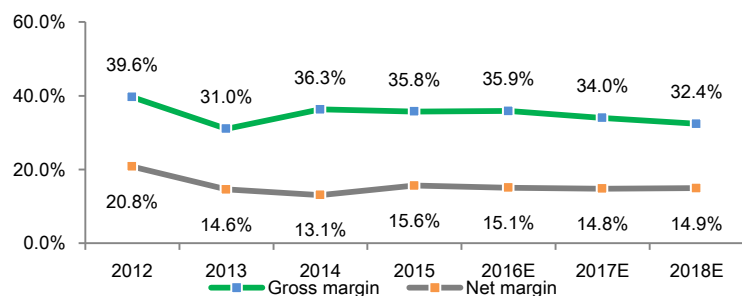
Source(s): Company, ABCI Securities estimates

**Exhibit 29: Yuzhou's booked sales**


Source(s): Company, ABCI Securities estimates

**Exhibit 30 : Yuzhou's core net profit**


Source(s): Company, ABCI Securities estimates

**Exhibit 31: Yuzhou's gross and net margins in 2010-16E**


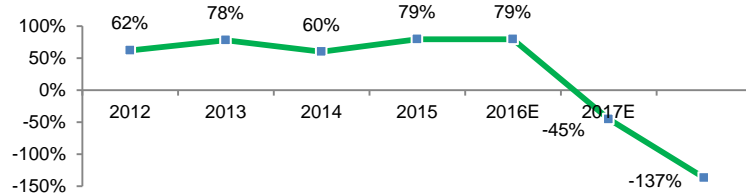
Source(s): Company, ABCI Securities estimates



### Gearing may rise in 2016E-17E

We expect Yuzhou's net gearing to maintain stable at 79% in 2016. Assuming no land acquisition in 2017E-18E given the high land cost in the heated market, we project net gearing to fall sharply for the period.

Exhibit 32: Yuzhou's net gearing in 2012-17E



Source(s): Company, ABCI Securities estimates

### Key highlights of 1H16 results

- Margin to remain stable in the next few years:** Revenue grew 18.3% YoY to RMB 4.1bn as GFA delivered rose 68.3% YoY to 0.53mn sqm. Core profit increased 19% YoY to RMB 657mn despite gross margin fell by 1.5ppt YoY to 32.5% in 1H16, mainly due to higher contribution from Hefei with lower ASP. However, Yuzhou expects gross margin to be ~32% in the next few years, given the robust property market in Xiamen and Hefei. Net gearing also dropped to 75% in Jun 16 from 19% in Dec 15.
- Sell-through rate increased to 78% in 1H16 from 65% in FY15:** With an improved sell through rate, Yuzhou's presales soared 124%YoY to RMB 12.9bn in 1H16. Net gearing dropped 4ppt HoH as a result.
- Increase exposure to YRD region:** The Group's headquarter has been relocated to Shanghai from Xiamen. Going forward, YRD, which includes the four key cities- Shanghai, Nanjing, Hefei, and Hangzhou, will contribute more to Yuzhou's presale. Sales contribution from YRD is expected to increase from 50% to 70%.

Exhibit 33: Yuzhou's 1H16 results

P&L	1H16	1H15	YoY Chg	Operating statistics	1H16	1H15	YoY Chg
	RMBmn	RMBmn	(%)				%
<b>Turnover</b>	<b>4,143</b>	<b>3,502</b>	<b>18.3</b>	Contracted GFA (mn sqm)	1.01	0.64	58.6
Cost of Sales & direct operating costs	(2,798)	(2,314)	20.9	Contracted ASP (RMB/sqm)	12,738	9,004	41.5
<b>Gross Profit</b>	<b>1,345</b>	<b>1,188</b>	<b>13.2</b>	<b>Contracted Sales (RMB mn)</b>	<b>12,872</b>	<b>5,736</b>	<b>124.4</b>
<b>Gross Margin (%)</b>	<b>32.5</b>	<b>33.9</b>	<b>(1.5ppt)</b>	GFA Delivered (mn sqm)	0.53	0.31	68.3
Selling and distribution costs	(107)	(86)	24.0	Booked ASP (RMB/sqm)	7,592	10,865	(30.1)
Administrative expense	(155)	(104)	49.0	<b>Property sales booked (RMB mn)</b>	<b>4,019</b>	<b>3,418</b>	<b>17.6</b>
<b>EBIT</b>	<b>1,084</b>	<b>998</b>	<b>8.6</b>	<b>Balance sheet</b>	<b>Jun-16</b>	<b>Dec-15</b>	<b>HoH chg</b>
<b>EBIT Margin (%)</b>	<b>26.2</b>	<b>28.5</b>	<b>(2.4ppt)</b>		<b>RMB mn</b>	<b>RMB mn</b>	<b>ppt</b>
Other income	116	177	(34.5)	Gross debt	23,507	20,083	17.0
Fair Value gains on IP and other exceptional items	223	23	886.0	Cash	15,670	11,949	31.1
Share of profit from JCE/ Associates	(5)	(50)	(90.7)	<b>Net debt</b>	<b>7,837</b>	<b>8,134</b>	<b>(3.7)</b>
Finance cost	(156)	(66)	135.1	<b>Net gearing (%)</b>	<b>75%</b>	<b>79%</b>	<b>(4ppt)</b>
<b>Profit before tax</b>	<b>1,262</b>	<b>1,081</b>	<b>16.7</b>				
<b>Tax</b>	<b>(579)</b>	<b>(417)</b>	<b>39.0</b>				
- LAT	(196)	(238)	(17.8)				
- Enterprise tax	(383)	(206)	86.2				
<b>Profit after tax</b>	<b>683</b>	<b>665</b>	<b>2.7</b>				
Minority Interest	10	(22)	(146.5)				
<b>Net profit</b>	<b>693</b>	<b>642</b>	<b>7.9</b>				
<b>Core net profit</b>	<b>657</b>	<b>552</b>	<b>19.0</b>				
<b>Core net margin</b>	<b>15.9</b>	<b>15.8</b>	<b>(0.1ppt)</b>				

Source(s): Company, ABCI Securities



## Initiate BUY with TP of HK\$3.30 based on a 60% discount to NAV

Exhibit 34: Yuzhou's end- FY16E NAV estimates

	Attr. GFA (M sqm)	Net assets value (RMB m)	% of total	Valuation Method	Implied value per sqm (RMB)
<b>Property development</b>					
Xiamen	1.9	7,627	21%	DCF at WACC of 10.5%	4,103
Hefei	2.9	7,531	21%		2,565
Shanghai	0.9	5,403	15%		6,021
Nanjing	0.5	5,334	15%		10,314
Fuzhou	0.6	1,978	5%		3,243
Others	3.4	6,840	19%		2,028
<b>Subtotal</b>	<b>10.2</b>	<b>34,714</b>	<b>96%</b>		
<b>Property investment &amp; management</b>		1,328	4%	6.0% cap rate on 2016E rental income	
<b>Total 2016E GAV</b>		<b>36,042</b>	<b>100%</b>		
2016E Net debt		(9,029)	-25%		
<b>Total 2016E NAV</b>		<b>27,012</b>	<b>75%</b>		
No. of share outstanding (diluted)		3,816			
<b>NAV per share (RMB)</b>		<b>7.08</b>			
Ex rate		1.18			
<b>NAV per share (HKD)</b>		<b>8.35</b>			
Target discount (%)		60%			
<b>Target Price (HKD)</b>		<b>3.30</b>			

<b>WACC</b>	<b>10.5%</b>
Cost of debt	7.3%
Cost of equity	20.0%
<b>Debt/ (Debt + Equity)</b>	<b>65%</b>

Source(s): Company, ABCI Securities estimates

Our valuation of Yuzhou is based on the discount-to-NAV method, one of the most common valuation metrics used for developers in China:

- **Property development:** We conduct a DCF analysis and apply a WACC of 10.5% to gauge the value of individual projects; total value of property development projects arrives at RMB 34.7bn.
- **Investment properties:** We apply a cap rate of 6% on 2016E rental income to arrive at our estimate of RMB 1.3bn.

Overall, Xiamen and Hefei jointly account for 42% of our GAV estimates, while Nanjing and Shanghai, where significant increase in property price have also been observed, jointly account for 30%. We subtract our 2016E net debt estimate (RMB 9.0bn) from the end-2016E GAV of RMB 36.0bn to derive our end-2016E NAV of RMB 27,012mn, or HK\$ 8.35/share.

We apply a 60% discount (toward the low-end of sector's discount range) to our NAV estimates and derive our TP of HK\$3.30, implying 5.5x 2016E P/E and 1.0X 2016E P/B.

Compared to the small cap peers' average at 6.3x P/E with a 4.6% yield, Yuzhou's current valuation at 4.6x 2016E P/E with a 2016E dividend yield of 7.7% is appealing. Given the upbeat outlook for Xiamen's and Hefei's property market, we initiate **BUY** for the counter with a TP of HK\$ 3.30.



Exhibit 35: Valuation of the HK-listed Chinese developers

China Property	Ticker	Rating	TP	Mkt cap	Share Price	Performance			Discount to NAV (%)	Valuation									
						3M	YTD	2015		P/E			Yield (%)			P/B			
				(HKD bn)	(local ccy)	% Chg	% Chg	% Chg		2015A	2016E	2017E	2015A	2016E	2017E	2015A	2016E	2017E	
<b>Residential:</b>																			
1	COLI	688 HK	BUY	31.70	267.7	27.15	12	2	22	(14.25)	9.0	7.8	5.8	3.4	3.9	5.2	1.3	1.3	1.2
2	Vanke-H	2202 HK	NR		289.4	19.82	5	(9)	30	(13.64)	16.0	9.2	7.7	4.2	4.8	5.7	2.0	1.7	1.5
3	CR Land	1109 HK	NR		161.1	23.25	20	6	13	(33.78)	11.3	9.5	8.1	2.5	2.8	3.3	1.4	1.2	1.1
4	Country Garden	2007 HK	NR		91.7	4.13	33	33	11	(29.96)	8.1	8.0	6.4	3.6	3.9	4.7	1.2	1.1	1.0
5	Longfor	960 HK	NR		75.3	12.90	29	16	19	(27.35)	9.3	8.1	7.1	3.2	3.6	4.1	1.1	1.0	0.9
6	Evergrande	3333 HK	BUY	7.30	75.0	5.48	2	(12)	143	(54.65)	34.1	11.1	4.7	8.1	4.5	10.6	0.5	0.6	0.6
7	Guangzhou R&F	2777 HK	NR		44.2	13.72	29	59	6	(22.32)	6.7	6.0	5.2	10.2	6.5	7.0	0.9	0.8	0.8
8	Shimao	813 HK	NR		39.2	11.42	12	(14)	(15)	(58.66)	5.4	5.2	4.7	5.8	6.1	6.7	0.7	0.6	0.6
9	SZI	604 HK	BUY	4.60	29.4	3.85	23	11	70	(57.80)	13.2	9.7	7.8	4.2	5.1	6.4	0.8	0.8	0.8
10	Sino Ocean	3377 HK	NR		27.6	3.67	9	(23)	18	(62.16)	9.9	7.3	6.0	3.3	4.7	5.5	0.6	0.5	0.5
11	Sunac	1918 HK	HOLD	5.40	19.4	5.71	13	0	(22)	(63.29)	4.8	5.4	4.8	4.0	3.4	3.8	0.9	0.8	0.7
12	Logan	3380 HK	BUY	4.70	19.2	3.46	28	39	13	(63.40)	7.6	6.4	5.4	4.0	4.3	5.8	1.2	1.1	1.0
13	Agile	3383 HK	NR		17.8	4.55	15	16	2	(59.17)	6.3	5.8	4.8	3.1	5.4	6.5	0.5	0.4	0.4
14	CIFI	884 HK	BUY	3.20	17.4	2.59	34	59	21	(55.96)	6.4	4.9	4.2	5.4	5.8	6.2	1.1	1.0	0.9
15	KWG	1813 HK	NR		16.1	5.27	6	(2)	14	(69.37)	4.8	4.4	3.9	6.4	7.1	7.9	0.6	0.5	0.5
16	Yuexiu Properties	123 HK	NR		15.0	1.21	16	(8)	(7)	(60.33)	10.4	9.9	8.4	3.8	3.8	4.5	0.4	0.4	0.4
17	Greentown	3900 HK	HOLD	6.10	14.9	6.88	23	(11)	0	(43.74)	16.9	10.5	7.1	0.0	1.9	2.8	0.5	0.5	0.5
18	Yuzhou	1628 HK	BUY	3.30	10.4	2.72	14	40	17	(67.44)	5.3	4.6	3.4	6.6	7.7	10.3	1.0	0.9	0.8
19	BJ Capital Land	2868 HK	NR		9.8	3.25	18	(1)	29	(40.91)	9.1	5.7	4.4	7.2	6.1	7.5	0.6	na	na
20	LVGEM	95 HK	BUY	2.70	9.7	2.07	9	(14)	9	(62.07)	229.1	12.8	5.7	0.5	2.7	6.2	1.8	1.7	1.4
21	Times Property	1233 HK	NR		6.2	3.59	11	41	(14)	NA	3.6	2.7	2.3	5.1	7.3	8.8	0.7	0.6	0.5
22	COGO	81 HK	NR		5.8	2.53	3	(23)	(17)	(72.62)	6.8	4.9	3.7	0.0	1.3	1.7	0.5	0.5	0.4
<b>HK Listed Avg</b>							<b>16</b>	<b>10</b>	<b>15</b>	<b>(49.33)</b>	<b>19.4</b>	<b>7.4</b>	<b>5.7</b>	<b>4.2</b>	<b>4.6</b>	<b>5.8</b>	<b>0.9</b>	<b>0.9</b>	<b>0.8</b>
<b>- Large cap (&gt;HKD30b), ex Evergrande</b>							<b>20</b>	<b>13</b>	<b>12</b>	<b>(28.57)</b>	<b>9.4</b>	<b>7.7</b>	<b>6.4</b>	<b>4.7</b>	<b>4.5</b>	<b>5.2</b>	<b>1.2</b>	<b>1.1</b>	<b>1.0</b>
<b>- Small-mid cap (&lt;HKD30b), ex LVGEM</b>							<b>16</b>	<b>11</b>	<b>10</b>	<b>(59.68)</b>	<b>8.1</b>	<b>6.3</b>	<b>5.1</b>	<b>4.1</b>	<b>4.9</b>	<b>6.0</b>	<b>0.7</b>	<b>0.7</b>	<b>0.6</b>
<b>Commercial:</b>																			
1	SOHO China	410 HK	NR		24	4.69	28	40	(21)	(41.38)	49.6	46.3	41.6	0.0	5.4	3.6	0.6	0.6	0.6
2	HLP	101 HK	NR		83	18.44	19	9	(16)	(46.89)	18.9	16.1	16.5	4.1	4.1	4.1	0.6	0.6	0.6
3	China South City	1668 HK	HOLD	1.60	15	1.87	22	10	(47)	(41.72)	12.4	14.4	9.7	2.7	2.3	3.4	0.6	0.6	0.5
4	Hui Xian REIT	87001 HK	NR		21	3.31	3	8	3	(24.34)	23.4	13.0	12.6	7.6	8.7	9.0	0.6	0.6	0.6
5	Jinmao	817 HK	BUY	3.60	28	2.58	18	1	25	(71.22)	9.5	7.9	6.2	3.1	4.1	5.2	0.7	0.7	0.7
6	Shui On Land	272 HK	NR		18	2.27	14	8	20	(36.50)	na	9.5	8.7	2.1	2.4	2.3	0.4	0.4	0.4
7	Yuexiu REIT	405 HK	NR		14	5.04	16	26	15	na	57.3	27.6	25.9	5.7	6.1	5.9	0.9	1.0	1.0
<b>Commercial Avg</b>							<b>17</b>	<b>14</b>	<b>(3)</b>	<b>(43.67)</b>	<b>28.5</b>	<b>19.3</b>	<b>17.3</b>	<b>3.6</b>	<b>4.7</b>	<b>4.8</b>	<b>0.6</b>	<b>0.6</b>	<b>0.6</b>

\*closing as at 7 Sep 2016

Source(s): Company, ABCI Securities estimates



## Risk factors

- **Margin contraction on expensive land acquisition.** To sustain Yuzhou's fast presales growth, the Group purchased expensive new sites whose prices may have been inflated by fierce land competition. In 1H16, the Group's average landbank cost rose 32% HoH to RMB 4,035/sqm, while land cost-to-ASP ratio increased from 30.5% in FY15 to 31.7% in 1H16. Although Yuzhou managed to lift its overall ASP by 27% YoY in 1H16, land cost has been rising at a much faster pace and this will pose pressure on Yuzhou's margin.
- **Placement risk.** Yuzhou placed 360mn of new shares (10.42% dilution) at HK\$ 2.20/share (12.4% discount to closing price prior to placement) to raise net proceeds of HK\$779mn in May 2015. As Yuzhou's shares are now trading at HK\$2.70-2.80, which is much higher than previous placement price, Yuzhou may issue new share at this level to reduce its gearing or to replenish its land bank.
- **Further policy tightening.** In Mar 2016, major tightening policies were launched in Shenzhen and Shanghai where property price surged 18% and 28% YTD. As property price in Hefei and Xiamen rallied 26% and 25% in 8M16, property tightening measures such as HPR and higher down payment for second-home loans, have been implemented since June and Aug. Should property prices show no signs of moderation, local governments may implement more stringent measures. Besides, the existing austerity measures on housing market may have time lag effect. The adverse impacts may emerge late this year or early next year.
- **High dividend payout policy in the future may change** if the group intends to retain more financial resources for internal use or business expansion.





**Consolidated income statement (2013A-2018E)**

<b>FY Ended Dec 31 (RMB mn)</b>	<b>2013A</b>	<b>2014A</b>	<b>2015A</b>	<b>2016E</b>	<b>2017E</b>	<b>2018E</b>
<b>Revenue</b>	<b>7,471</b>	<b>7,837</b>	<b>10,376</b>	<b>12,850</b>	<b>17,489</b>	<b>23,761</b>
Cost of sales	(5,152)	(4,992)	(6,666)	(8,241)	(11,547)	(16,066)
<b>Gross Profit</b>	<b>2,319</b>	<b>2,845</b>	<b>3,709</b>	<b>4,609</b>	<b>5,943</b>	<b>7,695</b>
SG&A expenses	(400)	(547)	(658)	(891)	(1,040)	(1,163)
<b>EBIT</b>	<b>1,919</b>	<b>2,298</b>	<b>3,052</b>	<b>3,718</b>	<b>4,903</b>	<b>6,532</b>
Finance cost	(170)	(175)	(152)	(221)	(300)	(376)
Share of profit of associates	(3)	0	(42)	-	5	11
Other income/ (expenses)	78	75	107	120	129	137
Fair value gain of investment properties	617	493	-	-	-	-
Disposal/one-off items	19	-	179	-	-	-
<b>Profit before tax</b>	<b>2,461</b>	<b>2,692</b>	<b>3,143</b>	<b>3,616</b>	<b>4,737</b>	<b>6,303</b>
Tax	(971)	(1,329)	(1,475)	(1,650)	(2,118)	(2,748)
<b>Profit after tax</b>	<b>1,490</b>	<b>1,363</b>	<b>1,668</b>	<b>1,966</b>	<b>2,618</b>	<b>3,555</b>
Minority interest	(20)	(109)	(11)	(31)	(30)	(10)
<b>Reported net profit</b>	<b>1,470</b>	<b>1,254</b>	<b>1,657</b>	<b>1,935</b>	<b>2,588</b>	<b>3,545</b>
<i>Less: exceptional items</i>	(380)	(229)	(37)	0	0	(0)
<b>Underlying net profit</b>	<b>1,090</b>	<b>1,025</b>	<b>1,620</b>	<b>1,935</b>	<b>2,588</b>	<b>3,545</b>
<b>Per share</b>						
Underlying EPS (RMB)	0.32	0.30	0.44	0.51	0.68	0.93
DPS (RMB)	0.15	0.16	0.18	0.21	0.28	0.38
Payout ratio (%)	48%	54%	41%	41%	41%	41%
BVPS (RMB)	2.13	2.36	2.62	2.82	3.22	3.76
<b>Growth %</b>						
Revenue	91.9%	4.9%	32.4%	23.9%	36.1%	35.9%
Gross Profit	50.3%	22.7%	30.4%	24.3%	28.9%	29.5%
EBIT	53.0%	19.7%	32.8%	21.8%	31.9%	33.2%
Underlying net profit	34.6%	-6.0%	58.0%	19.4%	33.8%	37.0%
<b>Margin %</b>						
Gross margin	31.0%	36.3%	35.8%	35.9%	34.0%	32.4%
Gross margin (post-LAT)	24.8%	28.9%	30.7%	28.3%	26.9%	25.8%
EBIT margin	25.7%	29.3%	29.4%	28.9%	28.0%	27.5%
Core net margin	13.6%	12.7%	15.2%	15.3%	14.9%	14.9%
<b>Key assumptions</b>						
Contracted Sales (RMB mn)	10,959	12,001	14,018	22,162	24,860	25,727
GFA sold (mn sqm)	1.04	1.20	1.40	1.83	2.02	2.02
ASP (RMB/sqm)	10,499	9,972	9,997	12,127	12,298	12,753
Booked Sales (RMB mn)	7,349	7,681	10,158	12,632	17,271	23,543
GFA delivered (mn sqm)	0.79	0.74	1.11	1.04	1.43	1.91
Booked ASP (RMB/sqm)	9,247	10,437	9,172	12,127	12,105	12,295

Source: Company, ABCI Securities estimates



Consolidated balance sheet (2013A-2018E)

As of Dec 31 (RMB mn)	2013A	2014A	2015A	2016E	2017E	2018E
<b>Current assets</b>	<b>21,847</b>	<b>29,560</b>	<b>44,739</b>	<b>56,510</b>	<b>67,520</b>	<b>73,772</b>
Cash	3,508	9,296	10,973	12,078	28,931	45,541
Restricted cash	376	489	976	976	976	976
Trade & other receivables	1,630	1,679	2,163	2,163	2,163	2,163
Property under development	13,985	16,979	28,913	39,580	33,737	23,379
Other current assets	2,349	1,118	1,714	1,714	1,714	1,714
<b>Non-current assets</b>	<b>5,515</b>	<b>9,515</b>	<b>8,107</b>	<b>9,120</b>	<b>9,063</b>	<b>8,992</b>
Property, plant & equipment	454	795	871	831	773	700
Investment properties	4,851	5,960	6,471	6,471	6,471	6,471
Investment in Associate and JCE	-	2,508	89	1,141	1,142	1,144
Other non-current assets	209	252	677	677	677	677
<b>Total Assets</b>	<b>27,362</b>	<b>39,075</b>	<b>52,846</b>	<b>65,630</b>	<b>76,583</b>	<b>82,764</b>
<b>Current Liabilities</b>	<b>11,483</b>	<b>17,279</b>	<b>25,626</b>	<b>37,293</b>	<b>46,747</b>	<b>50,887</b>
Short term borrowings	1,984	3,805	3,987	5,987	7,987	9,987
Trade & other payables	2,504	3,690	6,297	6,297	6,297	6,297
Pre-sales deposits	4,003	3,893	7,221	16,888	24,342	26,482
Other current assets	2,992	5,890	8,120	8,120	8,120	8,120
<b>Non-current liabilities</b>	<b>8,407</b>	<b>12,407</b>	<b>16,979</b>	<b>16,979</b>	<b>16,979</b>	<b>16,979</b>
Long term borrowings	7,726	11,599	16,096	16,096	16,096	16,096
Other payables	-	-	-	-	-	-
Other non-current assets	681	808	883	883	883	883
<b>Total Liabilities</b>	<b>19,890</b>	<b>29,685</b>	<b>42,605</b>	<b>54,271</b>	<b>63,725</b>	<b>67,865</b>
<b>Net Assets</b>	<b>7,472</b>	<b>9,390</b>	<b>10,241</b>	<b>11,359</b>	<b>12,858</b>	<b>14,899</b>
<b>Shareholders' Equity</b>	<b>7,362</b>	<b>8,173</b>	<b>9,622</b>	<b>10,757</b>	<b>12,277</b>	<b>14,358</b>
Perpetual capital instrument	-	-	-	-	-	-
Minority Interest	110	1,216	620	601	581	541
<b>Total Equity</b>	<b>7,472</b>	<b>9,390</b>	<b>10,241</b>	<b>11,359</b>	<b>12,858</b>	<b>14,899</b>
<b>Key ratio</b>						
Gross debt (RMB mn)	9,710	15,404	20,083	22,083	24,083	26,083
Net debt (RMB mn)	5,827	5,620	8,134	9,029	(5,824)	(20,434)
Net gearing (%)	78%	60%	79%	79%	-45%	-137%
Contracted sales/ Total assets (x)	40%	31%	27%	34%	32%	31%

Source(s): Company, ABCI Securities estimates



Consolidated cash flow statement (2013A-2018E)

As of Dec 31 (RMB mn)	2013A	2014A	2015A	2016E	2017E	2018E
EBITDA	1,947	2,322	3,094	3,777	4,980	6,625
Change in Working Capital	1,887	(82)	(997)	255	14,497	13,627
Tax payment	(876)	(817)	(1,355)	(1,650)	(2,118)	(2,748)
<b>Operating Cash flow</b>	<b>2,958</b>	<b>1,424</b>	<b>742</b>	<b>2,382</b>	<b>17,359</b>	<b>17,503</b>
Purchase of PP&E	(123)	(55)	(112)	(20)	(20)	(20)
Addition of Investment Properties	-	(331)	(881)	-	-	-
Others	(3,771)	(333)	(324)	(932)	133	146
<b>Investing Cash flow</b>	<b>(3,894)</b>	<b>(718)</b>	<b>(1,316)</b>	<b>(952)</b>	<b>113</b>	<b>126</b>
Debt raised	5,721	7,945	8,144	10,000	10,000	10,000
Debt repaid	(3,544)	(2,462)	(4,088)	(8,000)	(8,000)	(8,000)
Interest expenses	(868)	(1,130)	(1,295)	(1,476)	(1,500)	(1,505)
Equity raised	-	-	623	-	-	-
Dividend to shareholders	(231)	(405)	(443)	(799)	(1,069)	(1,464)
Others	35	1,134	(691)	(50)	(50)	(50)
<b>Financing Cash flow</b>	<b>1,113</b>	<b>5,082</b>	<b>2,251</b>	<b>(325)</b>	<b>(619)</b>	<b>(1,019)</b>
<b>Net cash inflow/ (outflow)</b>	<b>178</b>	<b>5,788</b>	<b>1,677</b>	<b>1,105</b>	<b>16,853</b>	<b>16,610</b>
Cash- beginning	3,330	3,508	9,296	10,973	12,078	28,931
<b>Cash- year-end</b>	<b>3,508</b>	<b>9,296</b>	<b>10,973</b>	<b>12,078</b>	<b>28,931</b>	<b>45,541</b>

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 from 2009-2013

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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