China Aoyuan (3883 HK) : NOT RATED

Mkt. Cap: US$1,780m I **3m Avg. Daily Val:** US$8.4m

Last Traded Price (20 Aug 2018)**:** HK$5.21

Analyst

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Aiming to outperform peers

- **Strong presales along with revenue recognition in 1H18 to support share price**
- **Sufficient land bank to drive growth in 2018 and 2019**
- **Investors' focus mainly on short-term debt refinancing and land acquisition strategy**
- **Attractive valuation with decent dividend yield**

What's New

High earnings visibility for 2018 and 2019. Aoyuan achieved 57% y-o-y growth in core earnings and has locked in 48% of consensus estimates. The company has Rmb77.6bn worth of unbooked sales, of which Rmb14-16bn would be booked in 2H18, translating into Rmb35-36bn for FY18, with the remaining balance to be booked in the coming years. This means Aoyuan has locked in 100% and 90% of the consensus FY18 and FY19 revenue estimates respectively. It has also locked in Rmb26.6bn revenue for future booking. In terms of revenue recognition standard, although Aoyuan has adopted the IFRS15, limited revenue has been booked based on construction progress. The company believes it can benefit more from this new accounting method after presales contract term revisions were made in the future.

Gross margins expected to be flat. 1H18 gross profit margin came in at 28.6%, higher than the 26.9% registered in 1H17 and the 26.7% posted in FY17. Gross margin of unbooked presales is estimated at 26-27% depending on the actual cost incurred. Given the company's average land cost remains low at Rmb2,036/sm and contracted ASP of Rmb10,231/sm in 1H18, its current margin looks sustainable.

Confident in exceeding full-year presales target and to outperform peers in 2019. The company achieved Rmb40.3bn (84% attributable) contracted sales in 1H18 and locked in 55% of its full-year presales target. It has Rmb82bn saleable resources in 2H18 including Rmb28bn brought forward from 1H18. Given the company has Rmb327.5bn total saleable resources in its existing land bank and the pace of its construction new start is also fast in 1H18 (5.23m sm in 1H18 vs. 6.65m sm in FY17), we believe it can have sufficient saleable resources to drive 2019 presales. Aoyuan's 1H18 sell-through rate was 60%.

Short-term debt comprised mostly of bank loans. Over 55% of total debt or c. Rmb25bn will be due within one year. The ratio is slightly higher than the 51% as of end-2017. Management believes the bulk of the short-term debt comprises bank loans to support its development. As the company is speeding up its pace of development, the maturity periods of development loans are usually short. It has repaid Rmb3.6bn of onshore corporate bonds in July and issued a total of Rmb2.4bn at an average cost of 8.25% in August 2018. Management believes it can maintain its average funding cost within 7.5% for the full year, compared with 7.3% in 1H18 and 7.2% in 2017. Offshore debt accounts for 35% of its total debt. Onshore bank loans, corporate bonds, and trusts accounted for 46%, 13% and 6% of total debt as at mid-year. First-half cash collection rate stood at 80%. Outstanding land premium was Rmb5.3bn as at mid-year (See page 2 for cash flow in

1H18 and FY18E). Net debt ratio as at mid-2018 stood at 67.5% which is an acceptable level.

Land acquisition strategy remains consistent with further progress on redevelopment projects. The company is on track of spending 50% of its presales proceeds on land acquisitions. 1H18 land acquisition reached 7.3mn sm with total attributable land cost 12.9bn. Regional exposure will continue to be Greater Bay area with a long-term plan to have 35% exposure in South China, 20% in East China, 20% in core region of Central & Western China, 15% in Bohai Rim respectively. Redevelopment projects in Zhuhai and Guangzhou are making good progress. Aoyuan has 15 redevelopment projects with potential saleable resources of Rmb129bn, of which Zhuhai Cuiwei and Guangzhou Panyu Nitrogen Fertilizer Plan projects made good progress in 1H18. The construction works of these two projects are expected to start in 2H18 or 2019. Saleable resources of the projects are expected to be Rmb24bn and Rmb15bn respectively. Aoyuan planned c.9mn sqm GFA new commencement and c.4.5mn sqm GFA completion in 2018.

Attractive valuation with decent dividend yield.
Management is likely to maintain consistent full-year dividend payout of c. 40%. The company is currently traded at 5.2x FY18/3.8x FY19 PE and offers a 6.3%/8.7% FY18/FY19 dividend yield. We believe the valuation is attractive compared with sector average of 5.9x/4.5x FY18/FY19 PE.

Cash flow

Cash Flow (RMB Bn)	1H18	FY18E
Cash proceeds	31.2	58.4
Land premium	-12.6	-28.0
Construction expenses	-13.5	-23.0
SG&A	-1.2	-2.7
Tax paid	-2.8	-6.0
Interest paid	-1.5	-3.3
Dividend paid	-	-0.7
Others	-5.0	-3.0
OCF	**-5.4**	-8.3
New debt	12.4	27.4
Debt repayment	-7.8	-17.2
FCF	**4.7**	**10.2**

Source: DBS HK

Result

FY Dec (RMB mn)	1H18	1H17	y-o-y %	1H18
Revenue	**13,667**	**8,154**	***68%***	
- Property development	12,950	7,675	*69%*	1H18: primarily led by a 48% increase in GFA delivery and 14% rise in recognised ASP
- Property investment	53	51	*5%*	
- Others	663	429	*55%*	
Cost of goods sold	(9,764)	(5,963)	*64%*	
Gross profit	**3,902**	**2,191**	***78%***	1H18: overall GPM grew by 2ppts to 28.6%, driven primarily by the recognition of higher margin development projects
Selling and marketing expenses	(600)	(346)	*74%*	
Administrative expenses	(651)	(332)	*96%*	FY18: SG&A to presales ratio improved 1ppt to 3.1%
Other income, gains and losses	153	(147)	*-204%*	
Gain on disposal of subsidiaries	18	-	*n.a*	
Fair value G/(L) on investment properties	407	142	*186%*	
FX gain/(loss)	(168)	143	*n.a*	
Fair value G/(L) on completed properties for sale upon transfer to IP	8	-	*n.a*	
Operating profit	**3,069**	**1,652**	***86%***	
Finance income	89	34	*164%*	
Finance costs	(173)	(118)	*46%*	1H18: effective interest rate on borrowings arrived at 7.3% (1H17: 7.6%, FY17: 7.2%)
Share of results of a JCE	89	(39)	*-326%*	
Pretax profit	**3,074**	**1,528**	***101%***	
- Income tax	(974)	(431)	*126%*	
- LAT	(625)	(238)	*162%*	1H18: led by an increase in the recognition of development projects with higher profit margins
Taxation	**(1,599)**	**(669)**	***139%***	
Minority interests	(259)	(108)	*139%*	
Reported profit	**1,216**	**750**	***62%***	
Reported core earning	**1,160**	**741**	***57%***	
Gross profit margin (%)	28.6%	26.9%	↑ *2 ppts*	
Core net profit margin (%)	8.5%	9.1%	↓ *1 ppts*	
Reported profit margin (%)	8.9%	9.2%	↓ *0 ppts*	
SG&A as % of top line (%)	9.2%	8.3%	↑ *1 ppts*	
SG&A as % of presales (%)	3.1%	4.1%	↓ *1 ppts*	
Effective tax rate (%)	52%	44%	↑ *8 ppts*	
EPS (RMB)	0.45	0.28	*62%*	
Core EPS (RMB)	0.43	0.28	*56%*	
Contracted sales (Rmb m)	40,291	16,520	*144%*	
Contracted GFA ('000 sm)	3,938	1,563	*152%*	
Contracted sales ASP (Rmb/sm)	10,231	10,569	*-3%*	
GFA delivery ('000 sm)	1,646	1,114	*48%*	
ASP of sales recognized (Rmb/sm)	7,868	6,893	*14%*	
	Jun-18	Dec-17		
Net debt ratio	68%	51%	↑ *17 ppts*	1H18: partly led by an increase in land bank replenishment activities (acquired 31 parcels of land or c.7.27m sm)
ST debt as % of total debt	55%	51%	↑ *5 ppts*	
Cash level (Rmb m)	**25,823**	**26,540**	*-3%*	

Source: Company, DBS HK

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Share price appreciation + dividends

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