

China Aoyuan Property

Progressing on track

Fixed Income

Asia

Outlook
Stable

Outperform on CAPGs

Offered at 107.5, 101.0 and 101.25, CAPG'17, '18 and '19 are trading at YTM of 10.1% (YTC 10.7%, callable at 106.94 starting Nov'15), 10.4% and 10.8% respectively. We maintain Outperform ratings on CAPG'17 and '19, and at the same time, we initiate an Outperform rating on CAPG'18. We like the decent carries of CAPGs and believe that recent capital market activities including onshore bond issuance will further improve its capital structure and lower the funding cost. We believe the impact of RMB depreciation on Aoyuan should be limited as the majority of its revenues and costs are RMB-denominated while offshore debts only account for 11% of its total borrowings.

Margin holding up well so far but downward pressure expected

On a yoy basis, Aoyuan's revenue, gross profit and operating profit increased 48%, 42% and 54% in 1H15 to RMB3.9bn, RMB1.2bn and RMB877mn respectively, thanks to the higher CFA delivered and ASP. Its profit margin held up well. In 1H15, its gross margin was 29.4%, lower than 30.5% in 1H14 but recovered modestly from 29.1% in 2H14. We believe that its more resilient profitability was attributable to the higher proportion of its sales from Guangzhou (GZ) and commercial properties. In 1H15, sales in GZ and sales of commercial properties accounted for 75% and 76% of its recognized sales, compared with 45% and 45% in 1H14 respectively. Taking cues from its contract sales in 1H15 (28% from GZ and 32% from commercial properties), we expect its margin to decline. The company guided for a gross margin of 26-28% in the coming 1-2 years. We take some comfort that the change of product mix with higher proportion of residential properties helps speed up asset turnover and improve cash flow. In 7M15, its contract sales grew c18% to RMB7.1bn, equivalent 53% of its full year sales target of RMB13.4bn. The run-rate is notably better compared with c40% in 7M14.

Funding exercises to lower funding cost

Aoyuan's net gearing ratio increased to 72.6% in Jun'15 from 61.8% in Dec'14. The company guided a higher budget for land purchase (to RMB5bn from RMB4bn during FY14 results) and slightly higher construction capex. These implied a small negative FCF in 2H15. It is maintaining the target of keeping the net gearing ratio below 80%. Subsequent to its funding exercises in 1H15, trust loan only accounted for 10% of its total borrowings in Jun'15 (15% in FYE14 and 28% in FYE13). In Jul'15, it issued 3-year onshore RMB bond of RMB2.4bn (c17% of its total debt as at Jun'15), mainly for refinancing. The coupon rate of the onshore bond was 5.8% vs its average funding cost of 9.9% in 1H15 (10.2% in 1H14). This should help further reduce its funding costs and lengthen its debt maturity. We expect the company to call CAPG'17 (coupon rate 13.875%) to lower funding cost but the recent market volatility, if it continues, could delay the redemption. It had cash on hand of RMB6.7bn and un-utilized bank facilities of RMB5.5bn as at Jun'15. These should adequately cover its short-term debts of RMB4.1bn and other short-term commitments.

Forex exposure manageable

The majority of the company's revenue and cost are RMB-denominated while offshore debts only accounted for 11% of its total borrowings. Its only overseas project is One30 Hyde Park in Sydney. The saleable resources of this project are cRMB2bn, compared with Aoyuan's total saleable resources of cRMB25bn in FY15 and its total assets of cRMB40bn as at Jun'15. On a pro-forma basis, its net gearing and EBITDA/int ratios are expected to only move to 75.3% and 1.4x from 72.6% and 1.5x in 1H15 assuming a 10% RMB depreciation.

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Figure 1: Financial summary

FYE Dec 31 (RMB 'mn)	2012	2013	2014	1H14	1H15
Income Statement					
Revenue	3,943	5,729	6,976	2,658	3,935
Cost of sales	(2,757)	(3,971)	(4,909)	(1,846)	(2,779)
Gross profit	1,187	1,759	2,067	812	1,156
Selling and distribution expenses	(237)	(319)	(379)	(100)	(101)
Administrative expenses	(370)	(351)	(391)	(143)	(178)
Opertaina profit	580	1,088	1,297	569	877
Fair value gain on investments properties	183	85	98	18	125
Gain on disposal of a JV/subsidiary	858	21	0	0	0
Finance costs	(66)	(44)	(65)	(35)	(59)
Other income	(23)	115	110	15	80
Share of result of a jointly controlled entity	(7)	(0)	9	1	(2)
Income tax expenses	(593)	(513)	(666)	(249)	(465)
Non-controlling interests	(2)	(16)	26	(10)	(17)
Net Profit	930	736	809	309	538
Balance sheet					
Properties for sale	11,548	19,437	24,947	21,036	26,205
Trade and other receivables	735	1,064	1,849	2,114	2,384
Restricted bank deposits	762	1,899	3,928	2,541	2,577
Bank balances and cash	2,381	2,812	1,989	3,744	4,154
Propertv. plant and equipment	376	415	501	419	493
Prepaid lease payments	3	168	16	15	16
Investment properties	1,949	2,419	2,728	2,450	3,356
Others assets	3,058	1,717	827	774	1,130
Total Assets	20,813	29,932	36,786	33,092	40,315
Trade and other payables	2,299	2,953	3,501	2,320	4,542
Sales deposits	4,244	6,463	8,772	7,892	7,497
Other liabilities	2,244	3,468	3,981	3,677	4,738
Borrowings-current	1,675	2,411	4,464	2,994	4,091
Borrowings-term	3,248	7,113	7,033	8,628	9,707
Total equity	7,104	7,524	9,034	7,580	9,740
Cash flow Statement					
Funds from operations (FFO)	(104)	49	(215)	(156)	NA
Net changes in working capital	(2,917)	(1,822)	(1,430)	(942)	NA
Cash flow from operations (CFFO)	(3,021)	(1,773)	(1,645)	(1,099)	NA
Gross capex	(25)	(37)	(113)	(15)	NA
Disposals	1,422	(26)	974	0	NA
Investments	903	(1,854)	(2,491)	(173)	NA
Free operating cash flow (FOCF)	(721)	(3,690)	(3,275)	(1,286)	NA
Dividends	(135)	(470)	(221)	0	NA
Free cash flow (FCF)	(856)	(4,160)	(3,496)	(1,286)	NA
Debt financing	151	4,740	2,793	2,945	NA
Equity financing	0	4	1	1	NA
Others	2,230	(153)	(122)	(728)	NA
Change in cash	1,524	431	(823)	932	NA
Credit Metrics					
Cash	3,143	4,712	5,917	6,285	6,731
Gross Debt	4,923	9,524	11,497	11,623	13,798
Net Debt	1,779	4,812	5,580	5,338	7,067
EBITDA	613	1,122	1,323	580	877
Gross margin (%)	30%	31%	30%	31%	29%
Operating margin (%)	15%	19%	19%	21%	22%
EBITDA margin (%)	16%	20%	19%	22%	22%
EBITDA/gross interest expense (x)	1.3	1.3	1.0	1.0	1.5
Gross debt/EBITDA (x)	8.0	8.5	8.7	10.0	7.9
Net debt/EBITDA (x)	2.9	4.3	4.2	4.6	4.0
Debt/Equity (%)	69%	127%	127%	153%	142%
Net Debt/Equity (%)	25%	64%	62%	70%	73%
Debt/total capitalisation (%)	41%	56%	56%	61%	59%
Net debt/net total capitalisation (%)	20%	39%	38%	41%	42%

Source: Company, UBS

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Source: UBS

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Issuer Name	Credit Rating	Outlook
China Aoyuan Property ^{2, 4, 5}	-	Stable

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