

**First Read**

# China Aoyuan Property

## Solid operating results but higher leverage

**Fixed Income**

Asia Pacific Ex. Japan

**Prefer CAPG'19**

We initiate buy on CAPG'19 and maintain buy recommendations on CAPG'17. Despite higher gearing in the course of expansion, we view positively Aoyuan's growing operating scale, stronger access to capital markets and gradually improving profit margin. The short-term market volatility and negative market sentiment may provide better entry opportunities. Offered at 109.75 and 100, CAPG'17 and '19 are trading at YTM of 10.59% and 11.24%, respectively. The bonds offer good carry. Between '17 and '19, we prefer '19 given the yield pick-up of c70bps, c10 pts lower in cash price and better trading liquidity for about 14 months in maturity.

**Solid results and pre-sales performance in FY13**

In FY13, Aoyuan's revenue, gross profit and recurring operating profit grew 45%, 48% and 88% to RMB5.7bn, RMB1.8bn and RMB1.1bn, respectively, driven by higher GFA delivered. Its gross margin in FY13 was 30.7%, slightly higher than the 30.1% in FY12. Aoyuan's contract sales increased 91% to RMB10bn in FY13, driven by 28% and 49% respective increases in GFA pre-sold and contracted ASP. The higher ASP, attributable to price recovery and higher proportion of commercial property sales, should support further margin improvement. Aoyuan sets contract sales target at RMB15bn in FY14, implying a sell-through rate of c50% of its saleable resources of RMB30bn. As per the company, its sell-through rate was c70% in FY13.

**Net gearing not exceeding 80%**

Its net debt increased cRMB3bn given its significant capex. Its land premium payment in FY13 was equivalent to 52% of cash collection from pre-sales, a high level within our universe. Its net gearing ratio therefore weakened considerably to 64% in FY13 from 25% in FY12. The company guided a negative FCF of cRMB2bn including new land acquisitions. The company expects to draw on new loans to plug the gap in FCF; as such, its net gearing ratio should continue to increase. As per the company, it will maintain net gearing ratio not exceeding 80%. It appears that the company has relaxed its previous financial policy of maintaining net gearing not exceeding 60%. It has c28% of its total borrowings in the form of trust financing. Going forward, it will manage the level at c20% of its total borrowing.

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	Time Horizon	UBS Terminology	Expectation	Definition
Sector recommendations	3 months	OVERWEIGHT	outperform	Sector is anticipated to <expectation> other sectors in the local currency investment universe* over a three-month horizon
		MARKET WEIGHT	perform in line	
		UNDERWEIGHT	underperform	
Company credit fundamentals	6 months	IMPROVING	improve	Credit fundamentals of the company are anticipated to <expectation> over the next six months
		STABLE	remain stable	
		DETERIORATING	deteriorate	
Company / bond	3 months	BUY	outperform	Company/Bond is anticipated to <expectation> other companies/bonds within a given peer group in the local currency investment universe* over a three-month horizon
		HOLD	perform in line	
		SELL	underperform	
Credit Default Swaps	3 months	BUY protection	widen by 5 bps or more	CDS level anticipated to <expectation>
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		SELL protection	tighten by 5 bps or more	
All recommendation types	N/A	Under Review	N/A	The recommendation is under review and a new recommendation may be published within the next 18 days

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\* Europe - iBoxx NonSovereign € and NonGilt £ universe measured on a curve-adjusted, excess return basis

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### Company Disclosures

#### Issuer Name

**China Aoyuan Property Group<sup>2, 4, 5</sup>**

Source: UBS; as of 18 Mar 2014.

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