

China Aoyuan (CAPG)

Strong FY2015 results

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CHINA PROPERTY

- ▶ Revenue up 37% y-o-y, driven by an 11% increase in gross floor area delivered and a 23% y-o-y increase in selling price
- ▶ Material improvement in liquidity; unrestricted cash on hand of RMB7.8bn comfortably covers short-term debt of RMB2.6bn and RMB310m unpaid land premium as of 2015
- ▶ Upgrade fundamental recommendation to Overweight from Neutral; buy CAPG'18 (106/107, 7.9%/7.4%) and '19-17c (107.5/108.5, 8.3%/7.3% to Jan-17 call)

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Tick-boxes checked for FY2015

On 7 March 2016, China Aoyuan (CAPG; rated B2/B, bond rated B3/B-) announced a strong set of FY2015 results. Recognised revenue was up by 37% y-o-y to RMB9.6bn, driven by an 11% y-o-y increase in gross floor area delivered to 1 million sq m, as well as a 23% y-o-y increase in the recognised average selling price on the shift in delivery mix towards Guangzhou. Within our expectation and in line with peers, profitability as reflected by gross margin declined to 28% in 2015 from 30% in 2014. The group managed to exceed its RMB13.5bn contracted sales target by 12%, finishing 2015 with contracted sales of RMB15.2bn. It has dynamically adjusted the sales mix towards residential away from commercial property to capture increased demand for the former upon the loosening of purchase restriction and mortgage availability.

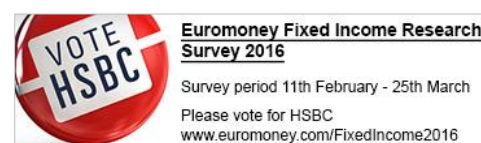
Strong balance sheet liquidity; debt leverage contained

China Aoyuan's balance sheet liquidity improved notably during the year, driven by stronger-than-expected cash inflow from pre-sales and release of restricted cash. Its unrestricted cash on hand totalled RMB7.8bn as of end-2015, more than covering short-term debt of RMB2.6bn and outstanding land premium of RMB310m. The group's blended average debt financing cost dropped to 9.5% in 2015 and will be down further to 9%, pro-forma for the call of USD112.5m CAPG'17 (13.875% coupon). Its debt maturity profile is lengthened, with RMB2.4bn raised from onshore corporate bond at 5.8% coupon in July 2015 and RMB2bn raised from onshore private placement notes at 7.8-7.9% coupon. Reported net gearing of 63% as of 2015 stayed largely flat versus 2014 and was comfortably below the 80% cap set.

2016: Reported net gearing could increase to 70%, liquidity to stay adequate

China Aoyuan sets its 2016 contracted sales growth target at 10-15%, versus RMB15.2bn contracted sales achieved in 2015 (i.e. target of RMB16.7-17.4bn), based on sales through-rate assumptions of 55-60%. The group also sets aside RMB5.7bn for land.

This note replaces the one of the same title and date to correct the EBITDA data in table 2 and its related ratios in table 3.



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1. China Aoyuan: Stronger-than-expected cash flow from pre-sales in 2015

Year ended Dec (RMBbn)	1H15	2H15	2015 actual	HSBC 2015 forecast	Variance	HSBC 2016 forecast	Y-o-Y
Cash sales proceeds	5.3	7.2	12.5	11.7	7%	14.5	16%
Construction costs	-3.6	-2.3	-5.8	-6.8	-15%	-6.3	9%
Interest expense	-0.5	-0.8	-1.3	-1.2	8%	-1.5	15%
SG&A, tax	-0.9	-1.2	-2.1	-2.0	5%	-2.4	14%
Recurrent income	0.0	0.0	0.0	0.0	0%	0.0	0%
Operating cash flow (OCF)	0.4	2.9	3.3	1.7	94%	4.3	30%
Land premium payment	-2.4	-3.0	-5.4	-5.0	8%	-6.0*	11%
Project/ project stake disposal	0.0	0.0	0.0	0.0	0%	0.0	0%
Others	1.2	2.2	3.4	0.0	NA	0.0	0%
Free cash flow (FCF)	-0.9	2.1	1.3	-3.3	NA	-1.7	NA
Cash dividend	0.0	-0.3	-0.3	-0.2	25%	-0.3	0%
Share repurchases	0.0	0.0	0.0	0.0	0%	0.0	0%
Retained cash flow (RCF)	-0.9	1.8	1.0	-3.5	NA	-2.0	NA
Additional onshore borrowings	0.6	3.1	3.7	4.5	-18%	0.5	NA
Additional offshore borrowings	2.4	-1.3	1.1	2.4	-55%	-0.2	NA
Perpetual issuance/ share placement	0.0	0.0	0.0	0.0	0%	0.0	0%
Change in cash	2.2	3.6	5.8	3.4	70%	-1.7	NA
Unrestricted cash balance at beginning of year	2.0	4.2	2.0	2.0	NA	7.8	NA
Unrestricted cash balance at end of year	4.2	7.8	7.8	5.4	44%	6.0	-22%

* Outstanding land premium carried forward from 2015: RMB310m

Source: China Aoyuan, HSBC estimates

banking, with targeted entry into Shenzhen and Zhuhai. Under our base case forecast, we expect its reported net gearing to increase to low-70% by end-2016e. We expect the group to pursue international expansion in a prudent manner, as demonstrated by its acquisition of One30 Hyde Park project in Sydney, Australia.

High chance of CAPG'19 being called in January 2017; upgrade fundamental recommendation to Overweight from Neutral; buy CAPG'18 and '19-17c

As we expect China Aoyuan to maintain its strong balance sheet liquidity in 2016e, we see high chance of USD300m CAPG'19 being called at 105.625 in January 2017, with its high coupon of 11.25%. We also see CAPG'18 as offering a decent carry, with yield of 7.4% (ask) and double-digit coupon of 10.875%. We change our trading call on CAPG'18 (106/107, 7.9%/7.4%) and '19 (107.5/108.5, 8.3%/7.3%-to-Jan-17 call) to buy from hold and upgrade our fundamental recommendation on China Aoyuan to Overweight from Neutral. The key downside risk is aggressive debt-funded expansion.

2. China Aoyuan: Consolidated income statements

Year ended Dec (RMBm)	2013	2014	2015	Y-o-Y
Revenue	5,729	6,976	9,572	37.2%
Cost of sales	(3,971)	(4,909)	(6,926)	41.1%
Gross Profit	1,759	2,067	2,646	28.0%
Selling, admin & operating expenses	(670)	(770)	(890)	15.6%
Operating profit	1,088	1,297	1,756	35.3%
Finance costs	(44)	(65)	(91)	40.4%
Other revenue and gains	221	207	192	-7.4%
Share of profit in associated & JCEs	(0)	9	28	203.5%
Tax	(513)	(666)	(977)	46.7%
Minority interest	(16)	26	(95)	-460.3%
Net profit	736	809	812	0.3%
Memo item:				
Depreciation and amortization	34	25	34	35.4%
EBITDA	1,122	1,323	1,790	35.3%
Total interests	(848)	(1,276)	(1,393)	9.2%

Source: China Aoyuan, HSBC

3. China Aoyuan: Consolidated balance sheets and financial metrics

Year ended Dec (RMBm)	2013	2014	2015
Cash and cash equivalents	2,812	1,989	7,769
Restricted bank deposits	1,899	3,928	1,267
Properties for sale	19,437	24,947	31,792
Other short-term assets	2,632	2,286	2,370
Investment properties	2,419	2,728	4,505
Other long-term assets	731	908	1,124
Bank loans and borrowings	2,411	4,464	2,570
Trade and other payables	2,953	3,501	5,348
Sales deposits	6,463	8,772	9,823
Other short-term liabilities	3,136	3,641	5,028
LT borrowings	7,113	7,033	13,727
Others	332	341	754
Minority interest	305	1,315	3,333
Shareholders' equity	7,219	7,719	8,243
Memo items:			
Cash	2,812	1,989	7,769
Debt	9,524	11,497	16,298
Net debt	6,712	9,508	8,529
Total equity	7,524	9,034	11,576
Total capitalisation	17,048	20,531	27,874
Total assets	29,932	36,786	48,827
Financial metrics			
Gross margin (%)	30.7%	29.6%	27.6%
Operating margin (%)	19.0%	18.6%	18.3%
EBITDA margin (%)	19.6%	19.0%	18.7%
EBITDA/total interest (x)	1.32	1.04	1.29
Return on equity (%)	10.1%	9.8%	7.9%
Return on total assets (%)	2.9%	2.4%	1.9%
Debt/EBITDA (x)	8.49	8.69	9.10
Net debt/EBITDA (x)	5.98	7.19	4.76
Debt/equity (x)	1.27	1.27	1.41
Net debt/equity (x)	0.89	1.05	0.74
Debt/total capitalisation (%)	55.9%	56.0%	58.5%
Net debt/net total capitalisation (%)	47.1%	51.3%	42.4%
Cash/total assets (%)	9.4%	5.4%	15.9%

Source: China Aoyuan, HSBC

Disclosure appendix

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Rating changes for long-term investment opportunities**Recommendation History of CHINA AOYUAN**

From	To	Date
Not Rated	Neutral	2013-12-11

Source: HSBC

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Neutral	164	57	52	32
Underweight	53	19	9	17

Source: HSBC

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Company	Ticker	Recent price	Price date	Disclosure
CHINA AOYUAN	3883.HK	1.33	07-Mar-2016	6

Source: HSBC

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