



**Equity Research
Properties/ China**

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OP Express

Not Rated

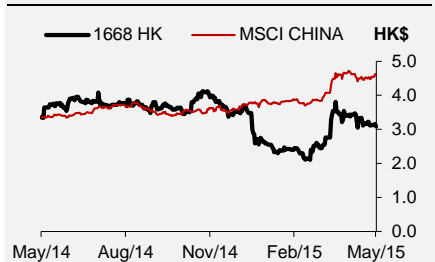
Close price: **HK\$3.09**

Key Data

HKEx code	1668
12 Months High (HK\$)	4.27
12 Month Low (HK\$)	2.07
3M Avg Dail Vol. (mn)	76.17
Issue Share (mn)	8,000.82
Market Cap (HK\$mn)	24,722.54
Fiscal Year	03/2014
Major shareholder (s)	DIRECTOR RICKY CHENG & ASSO. (30.5%)

Source: Company data, Bloomberg, OP Research
Closing price are as of 27/05/2015

Price Chart



	1mth	3mth	6mth
Absolute %	-9.6	28.8	-22.6
Rel. MSCI CHINA %	-7.7	9.9	-50.0

Company Profile

China South City Holdings Ltd. owns and operates an integrated logistics and trade center of industrial materials in China. The trade center primarily features textile and clothing materials; leather and accessories; electronics accessories and products; metals, chemicals and plastic materials and products; and printing and packaging materials.

China South City (1668 HK)

Taking Shenzhen success across China

China South City (1668 HK, "CSC") is a leading developer and operator of large-scale trade centres in China. Combining integrated logistics with trade services and facilities to produce a highly successful model in Shenzhen, CSC has replicated it in 8 other cities with acquired GFA of 26.6mn sqm and total planned GFA of 78.8mn sqm.

Partnership with Tencent for 4th generation wholesale center After fully exercising its options, Tencent made a strategic investment in CSC by buying 925.1mn shares or 11.55% stake for about HK\$2.32bn. This created opportunities for Tencent and CSC to jointly develop a leading integrated Online to Offline ("O2O") in 5 major areas. We believe CSC has an unique strategy to build 4th generation wholesale market integrating a modernized "physical + online + logistics" business eco-system to create synergy for their traditional business with e-commerce.

Recurring income hitting a critical mass Rental income of CSC has increased with the rapid growth of its operating area in CSC Shenzhen. With the development of rental areas in other CSC projects, such as Nanning, Nanchang, Xian and Zhengzhou, as well as logistics facilities and outlets, CSC is expected to make over HK\$1bn annual recurring income in near future, which would trigger a re-rating for less discount to NAV given stable and foreseeable nature of recurring income as it is making a material contribution to CSC core earnings.

China - Hong Kong Stock Links may change market valuation Since A-shares listed peers are trading at demanding valuation of over 50x average forward PE, CSC would offer a choice for mainland investors as being one of the eligible stocks in Shanghai-Hong Kong Stock Link. Given strong growth potential and high dividend yield, the stock may outperform in short run.

Exhibit 1: Historical financials

Year to Mar (HK\$ mn)	FY10A	FY11A	FY12A	FY13A	FY14A
Revenue	1,570.2	2,234.0	3,670.8	7,488.1	13,468.3
Growth (%)	n.a.	42.3	64.3	104.0	79.9
Net Profit	1,327.6	1,544.1	2,070.7	2,746.9	3,494.5
Growth (%)	n.a.	16.3	34.1	32.7	27.2
Diluted EPS (HK\$)	0.25	0.26	0.334	0.441	0.451
EPS growth (%)	n.a.	4.0	28.0	32.0	2.4
ROE (%)	18.69	19.88	16.0	19.1	19.5
P/E (x)	12.4	11.9	9.5	7.2	7.0
P/B (x)	2.1	1.8	1.5	1.2	1.1
Yield (%)	0.6	1.0	2.4	3.2	4.4
DPS (HK\$)	0.02	0.03	0.075	0.100	0.140

Source: Bloomberg, OP Research

Partnership with Tencent for 4th generation wholesale center

After fully exercised the options, Tencent made a strategic investment in CSC by purchasing 925.1mn shares or 11.55% stake at a consideration of some HK\$2.32bn. This creates opportunities for Tencent and CSC to jointly develop a leading integrated Online to Offline (“O2O”) in 5 major areas. We believe CSC has an unique strategy to build 4th generation wholesales market integrating a modernized “physical + online + logistics” business eco-system to create synergy for their traditional business with e-commerce.

Exhibit 2: Cooperation of Tencent and CSC

CSC 5 cooperation area with Tencent

1. Through the cooperation, an intelligent digital solution of wireless internet access service is developed to cover all China South City projects to actively disseminate promotional messages to Weixin users in China South City through real-time tracking and analysis of their shopping patterns.
2. Weixin public account platform will be used to promote B2C business collaboration with O2O.
3. Weixin platform of merchant alliance will be established to integrate with China South City’s B2B e-commerce platform, such as CSC86.com
4. China South City’s ERP and CRM system will be integrated with Weixin platform to build a China South City O2O business eco-system
5. Tencent will appoint a consultancy team to provide guidance to CSC on the e-commerce platforms and O2O mobile terminals establishment, membership system development and management, user experience enhancement, big data utilization and provision of value-added services

Source: Company, OP Research

Given a large base of tenants and SME clients in 8 CSC projects across China, the physical wholesale market offers a special strength and potential to CSC by integrating with online business platform. CSC has been rolling out their e-commerce tools and logistics system to utilize its hidden value.

CSC has a clear road map for e-commerce development. Initially, CSC will try to help their large base of traditional SMEs to go online by setting up CSC86.com. CSC will then build online sales and merchant database to improve the quality of tenants by sharing and analyzing merchant and customer data. In the future, by targeting high quality SMEs and online buyers, CSC can earn net interest margins and investment returns by offering micro-financing to build a cash pool. Besides, given co-operation of Tencent, CSC can utilize the online payment services to facilitate the transactions and to control credit risk.

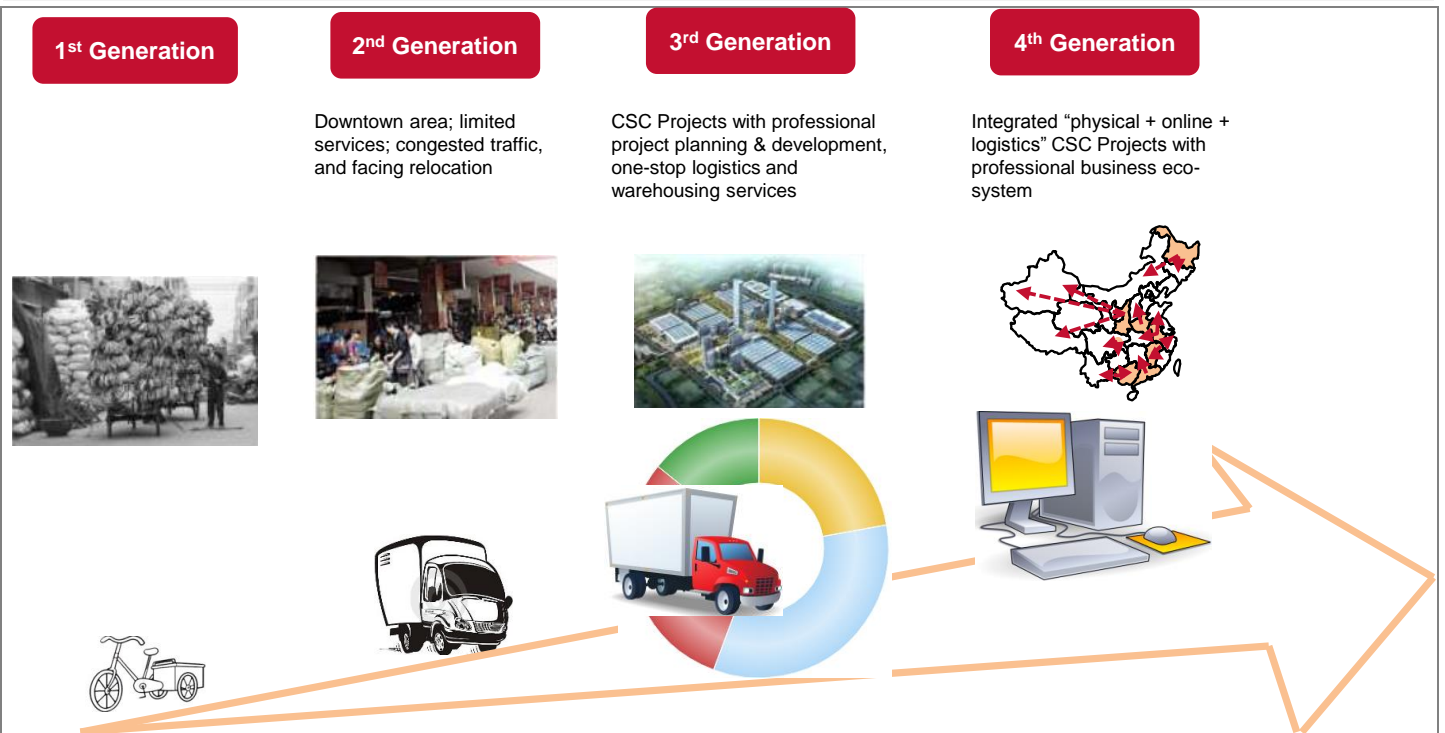
CSC86.com is one of the e-commerce services provided by CSC to existing CSC occupants. CSC86.com supply value-added services including technical support, website management, visual design and third party certificates. By introducing online membership program in FY14, over 7,000 SEMs joined in and generated a considerable income of near HK\$200mn in 2HFY14. With about 660,000 registered users and 2.3m products displayed online, CSC86.com may become one of the largest B2B websites, similar to Alibaba and HC360. In the long run,

given the strong offline presence, CSC86.com may expand their business quickly by exploring opportunities, such as one-stop sourcing and centralized procurements.

Apart from B2B, CSC also target B2C segment by developing online outlet store – Aolaigo.com. The online outlet store will connect with Weixin platform to create more internet traffic and sales. Given strong IT knowledge from Tencent, CSC has leverage on the partnership to build up a total operating model in O2O to run the outlets.

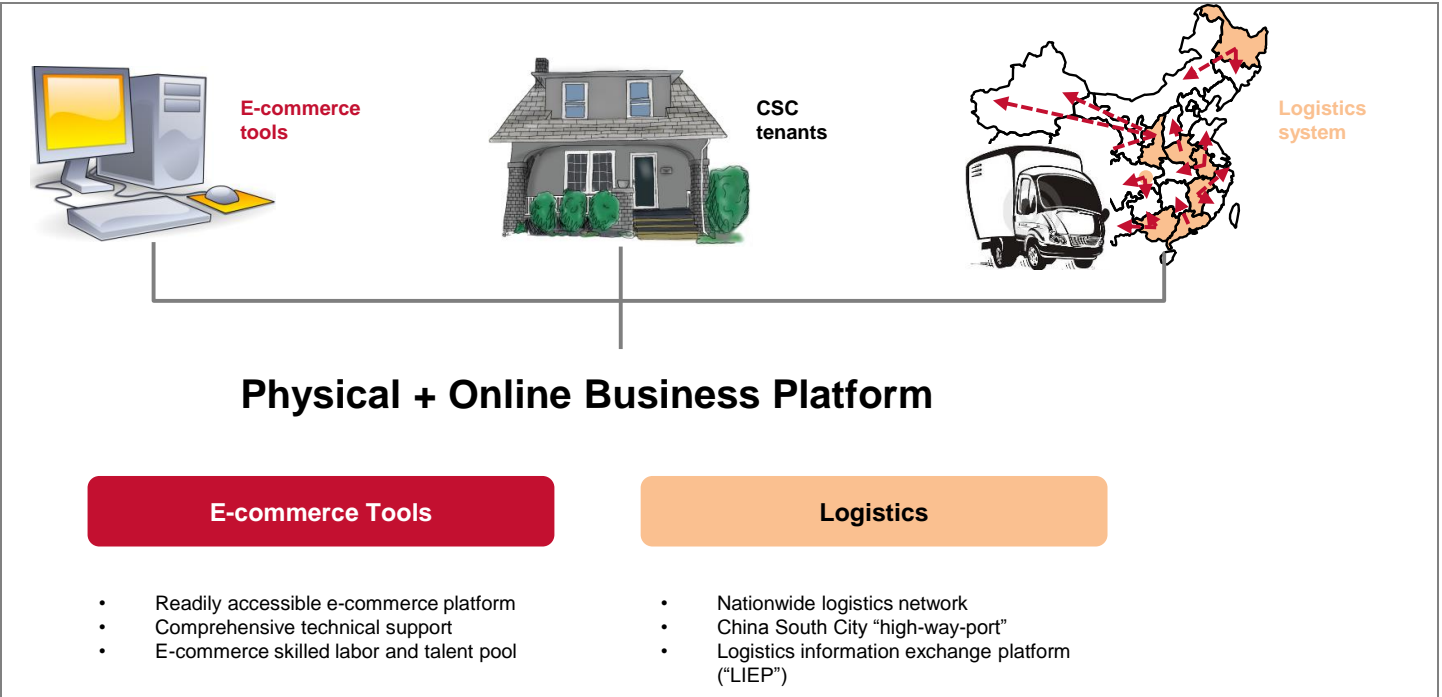
In conclusion, we believe CSC may unlock their true value by leveraging their strong physical presence for developing a 4th generation wholesale center concept as a B2B e-commerce and O2O arm for Tencent.

Exhibit 3: Generations of wholesale markets



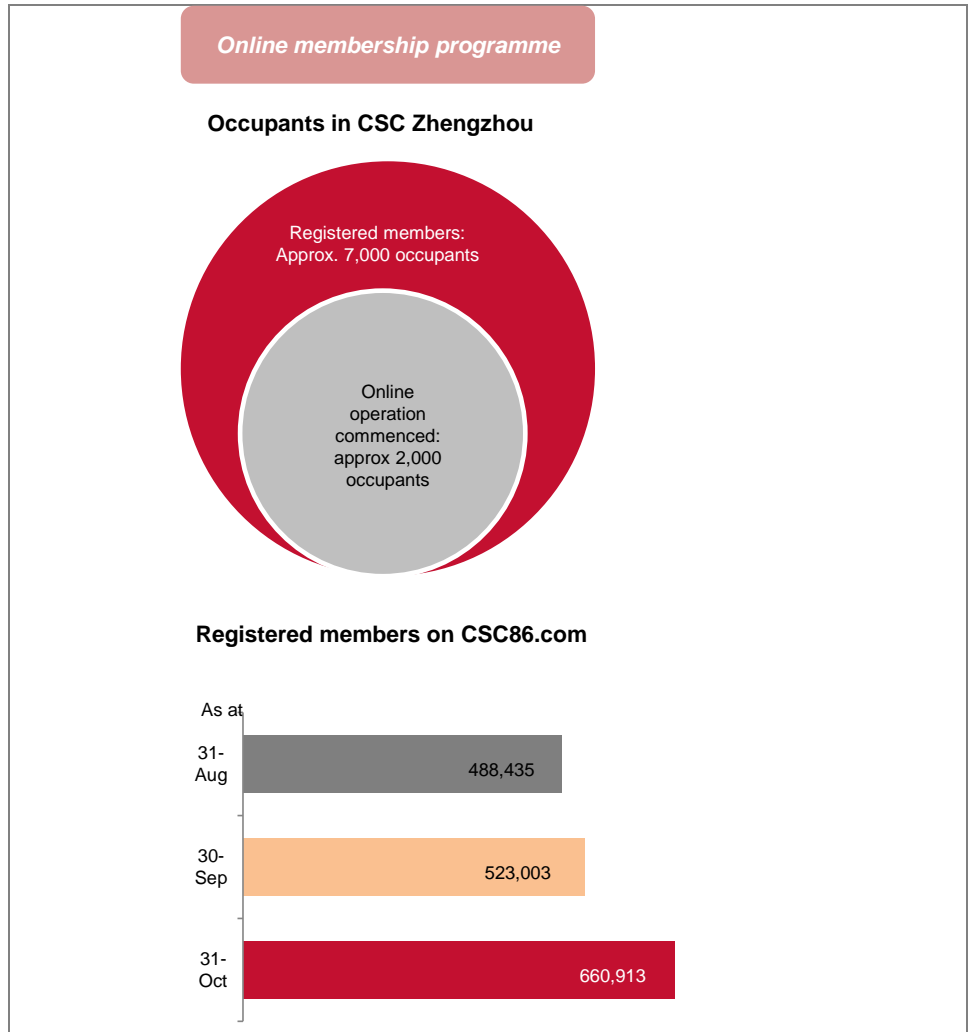
Source: Company, OP Research

Exhibit 4: 4th Generation wholesale center concept



Source: Company, OP Research

Exhibit 5: CSC B2B e-commerce detail in Zhengzhou project



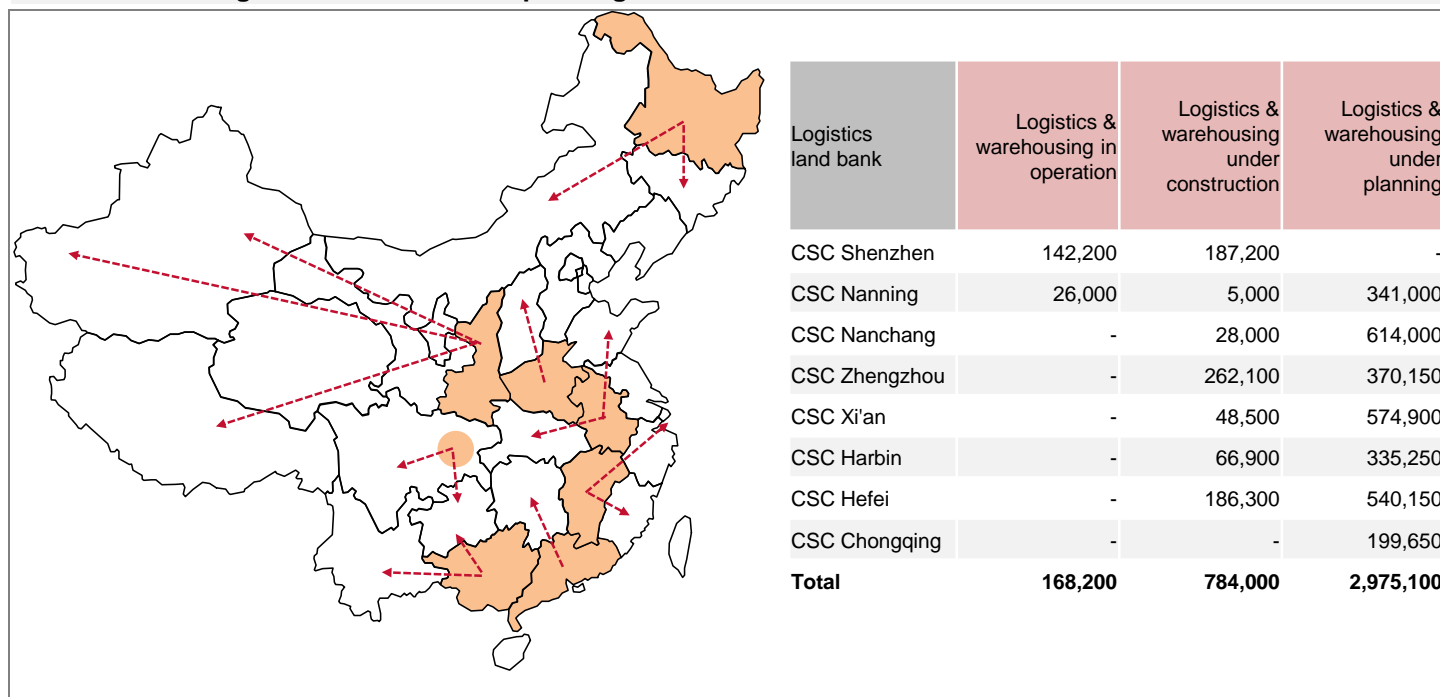
Source: Company, OP Research

Recurring income hitting a critical mass

CSC currently has about 170,000 sqm logistics and warehousing in operation in CSC Shenzhen and CSC Nanning. The revenue from logistics has more than doubled in 1HFY3/15 to HK\$25mn with the increase in operating area. CSC plans to increase the operating area by another 366% to 784,000 sqm within two years by constructing logistics facilities in current and new areas, such as Nanchang, Zhengzhou, Xian, Harbin and Hefei. Given low land costs and large SME client base, CSC plans to allocate 15% of their project pipeline into logistics, which makes a total of 2.98mn sqm in long run.

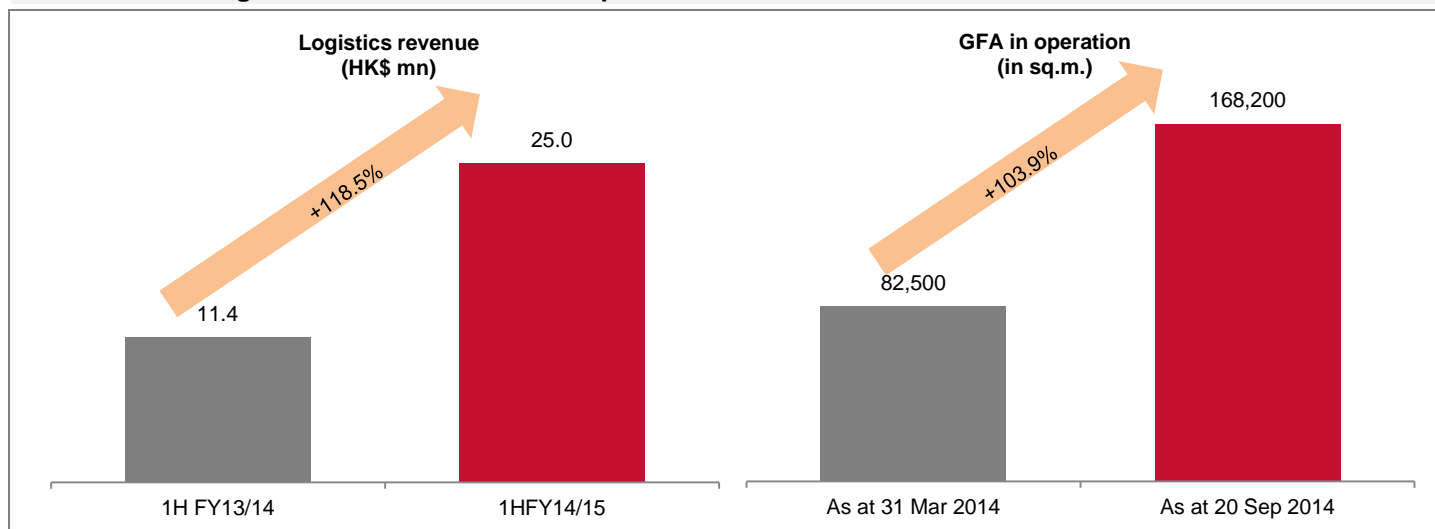
Besides, as CSC projects are located across China from South to North, CSC is building a nationwide logistics network with an online platform called Logistics Information Exchange Platform (“LIEP”) and CSC “highway-port”. Through LIEP, the logistics demand from SMEs can match with HGV drivers on a real-time basis. Currently, truck drivers normally need to pay the toll fee on return trips with empty loads. By using the logistics information uploaded in LIEP, the logistics costs will be saved as LIEP can facilitate the utilization of the returned transport capacity. On the other hand, CSC has built-in large scale highway-port in their projects, which are specially designed to serve long-haul LGVs, with warehouses at close distance. Given the scale of their plan, we believe CSC may become one of the largest logistics facilities providers in China, following Global Logistics Properties and Beijing Properties.

Exhibit 6: CSC logistics locations and operating area



Source: Company, OP Research

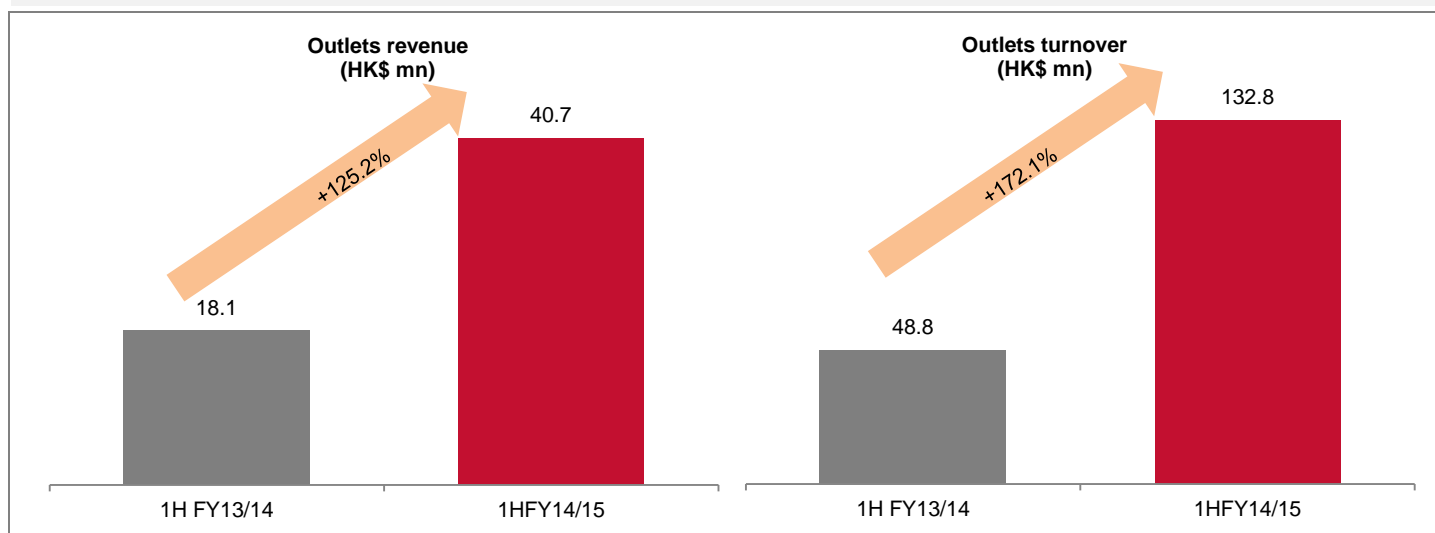
Exhibit 7: CSC logistics revenue and GFA in operation



Source: Company, OP Research

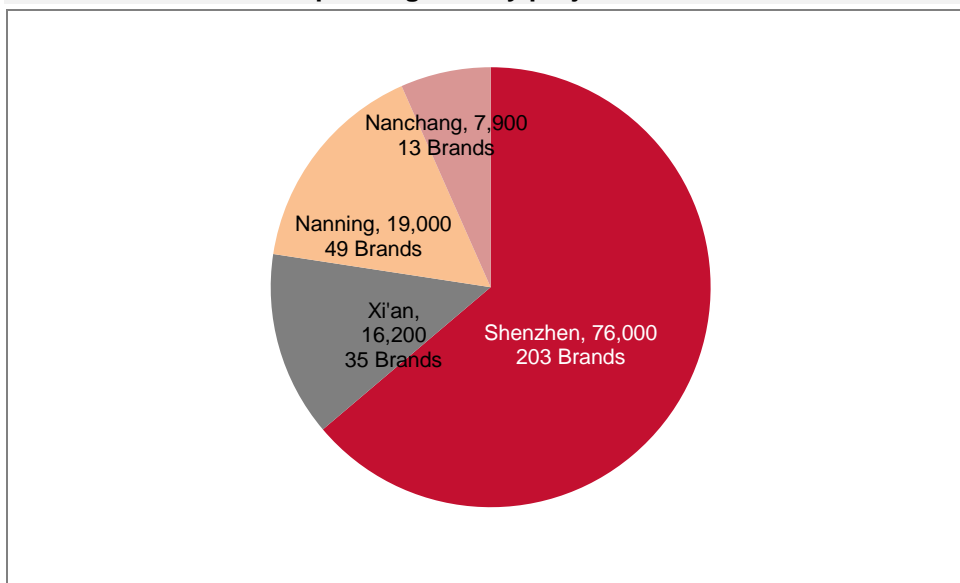
For another 15% of area to be developed in the projects, CSC will plan it as other commercial facilities, such as outlets. CSC currently has some 120,000 sqm operation area for outlets. Given relatively suitable distance from CBD areas to the cities and cooperation with Tencent to promote in Weixin, the revenue from outlets has increased by 125% to HK\$40mn in 1HFY3/15 based on the jump in outlet turnover. We believe this may generate recurring income to CSC in long run.

Exhibit 8: CSC outlets revenue and turnover



Source: Company, OP Research

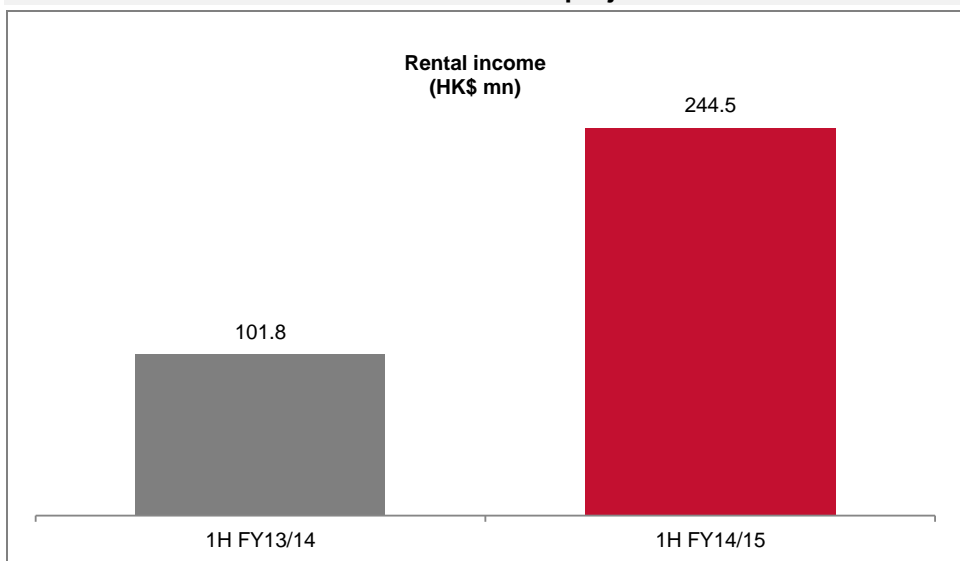
Exhibit 9: CSC outlets operating area by project



Source: Company, OP Research

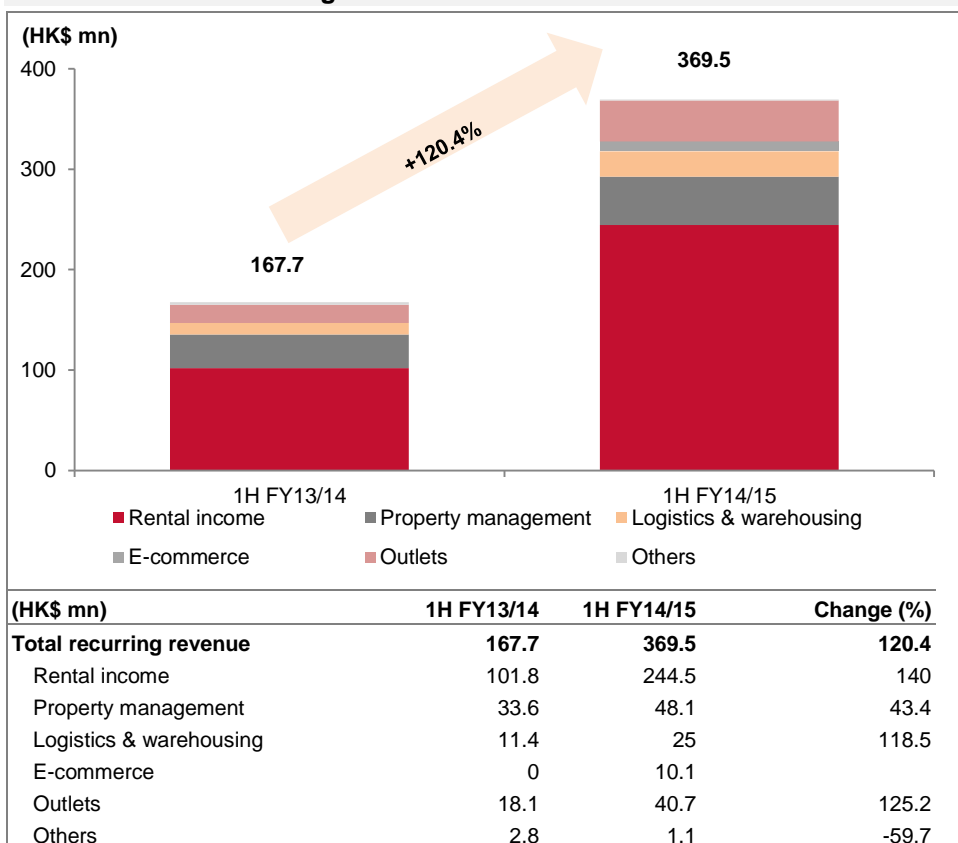
The total recurring revenue for CSC has increased by 120% to HK\$370mn in 1HFY3/15 with rental income contributing HK\$244mn, which mainly came from CSC Shenzhen. For every project, 50% of the area will be developed into trade centers, with half to be sold and half held for rental. Since CSC Shenzhen is the first project of CSC, it provided a majority of the rental income in 1HFY3/15. By replicating the same successful model and covering capex with more sales of the projects in initial phase, CSC plans to keep more operating areas for rental in Nanning, Nanchang, Xian and Zhengzhou at the later stage of development. It is expected the total annual recurring income may surpass HK\$1bn in near future to contribute a material portion of the earnings by forming a critical mass. Given fast growth in rental income and recurring income, we believe a re-rating in CSC for higher valuation will be triggered for less discount to NAV since CSC recurring income is stable and long-lasting to give stronger cashflow to improve credit rating.

Exhibit 10: CSC rental income in Shenzhen project



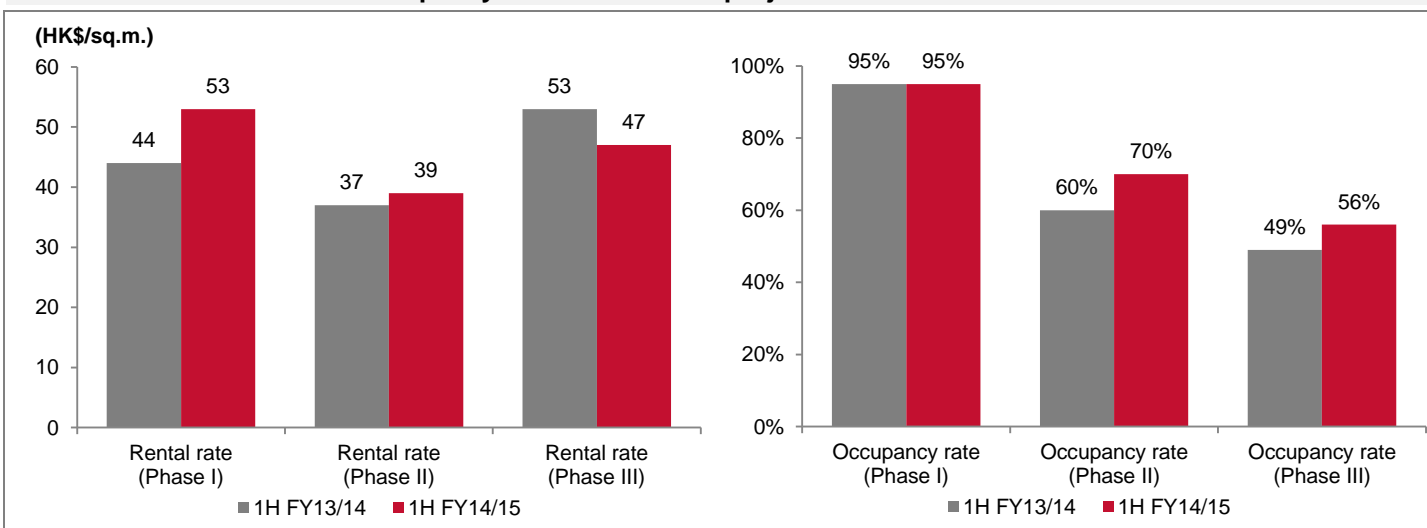
Source: Company, OP Research

Exhibit 11: CSC recurring income in 1HFY3/15



Source: Company, OP Research

Exhibit 12: CSC rental and occupancy rate in Shenzhen project



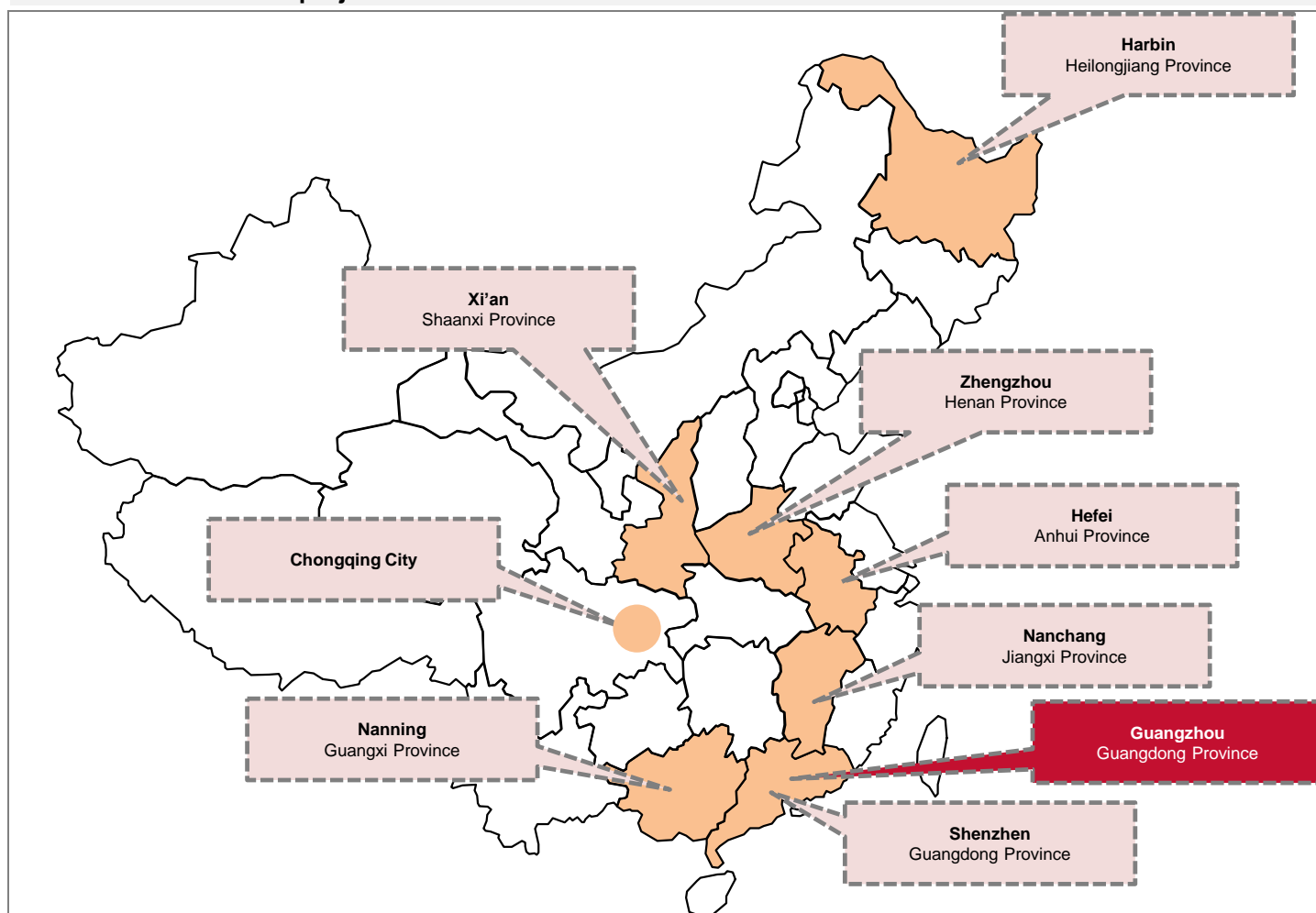
Source: Company, OP Research

China - Hong Kong Stock Links may change market valuation

The company currently has 8 mega projects in 8 provincial capitals with total acquired GFA of over 23mn mn sqm for development. The company has received strong support from government since relocating traditional wholesales markets into CSC would drive industry upgrade and accelerate urbanization to optimize urban space. Thus, local government would build expressways and railways to connect to the CSC projects. With special requirements in the land plot auction, CSC is always the “only bidder” in the auction to secure a very low land cost (average less than Rmb300 per sqm), which gives CSC over 50% gross margin and near 20% net margin. It is expected CSC may keep on buying the planned GFA of 78.8mn sqm at low land cost in the future.

CSC is one of the eligible stocks in Shanghai-Hong Kong Stock Link available for mainland investors to trade. Although the A-shares peers normally have smaller scale with less growth potential, the valuation is usually demanding with an average of 50x forward PE. Since CSC has a special concept of growth with large scale project pipeline, sizable recurring income and stable dividend policy, we believe the participation of mainland investors would give CSC a higher valuation in near future.

Exhibit 13: CSC current projects



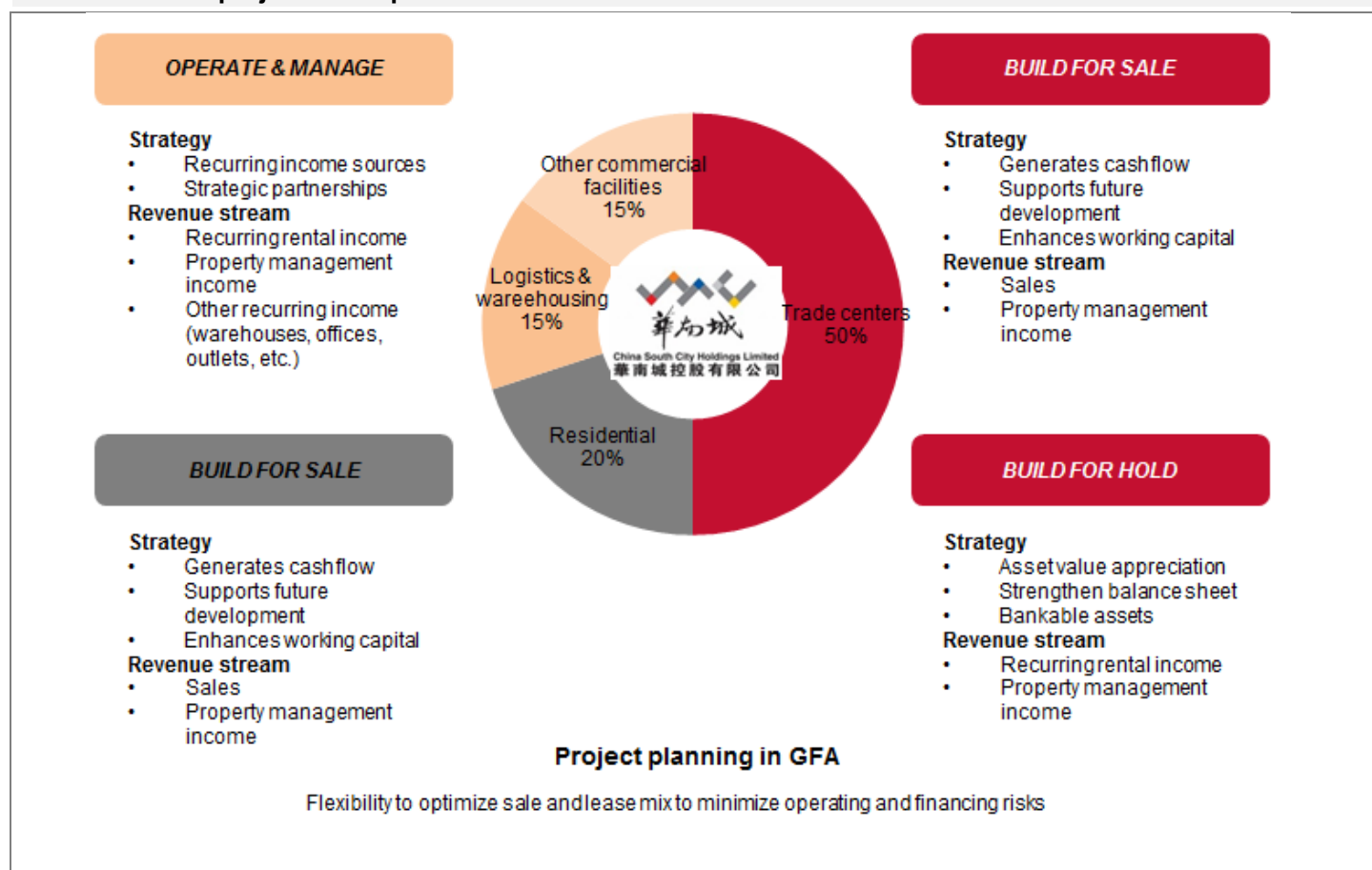
Source: Company, OP Research

Exhibit 14: CSC landbank in 1HFY3/15

(in dq.m.)	Completed properties		Properties under development	Properties to be completed by FY14/15 Estimated	Properties under planning on GFA acquired Estimated	Total planned GFA Estimated	GFA acquired (% to total planned GFA)	
	Sold	Unsold						%
CSC Shenzhen	690,500	1,209,800	497,200	110,500	246,500	2,644,000	2,644,000	100
CSC Nanchang	638,500	456,000	747,200	403,000	2,438,300	4,280,000	4,280,000	100
CSC Nanning	226,600	589,400	762,000	558,500	902,000	4,880,000	2,480,000	51
CSC Xi'an	468,000	428,500	731,400	168,500	2,528,100	17,500,000	4,156,000	24
CSC Harbin	148,600	87,000	1,167,000	130,800	1,278,400	12,000,000	2,681,000	22
CSC Zhengzhou	819,500	1,025,300	1,313,600	65,500	1,056,600	12,000,000	4,215,000	35
CSC Hefei	652,500	155,900	1,355,600	563,600	2,679,000	12,000,000	4,843,000	40
CSC Chongqing	-	-	877,700	680,000	453,300	13,500,000	1,331,000	10
Total	3,644,200	3,951,900	7,451,700	2,680,400	11,582,200	78,804,000	26,630,000	34

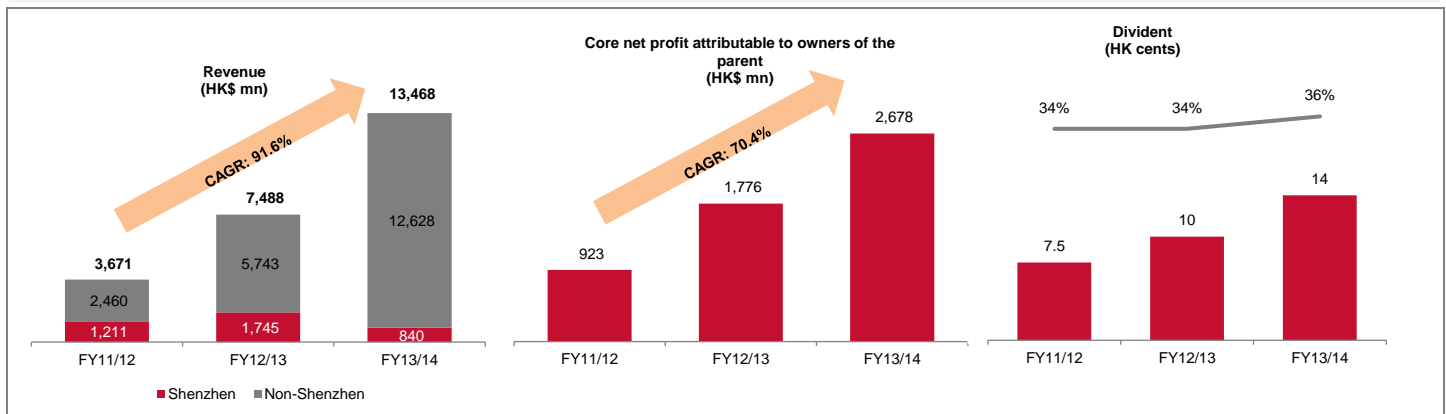
Source: Company, OP Research

Exhibit 15: CSC project development allocation



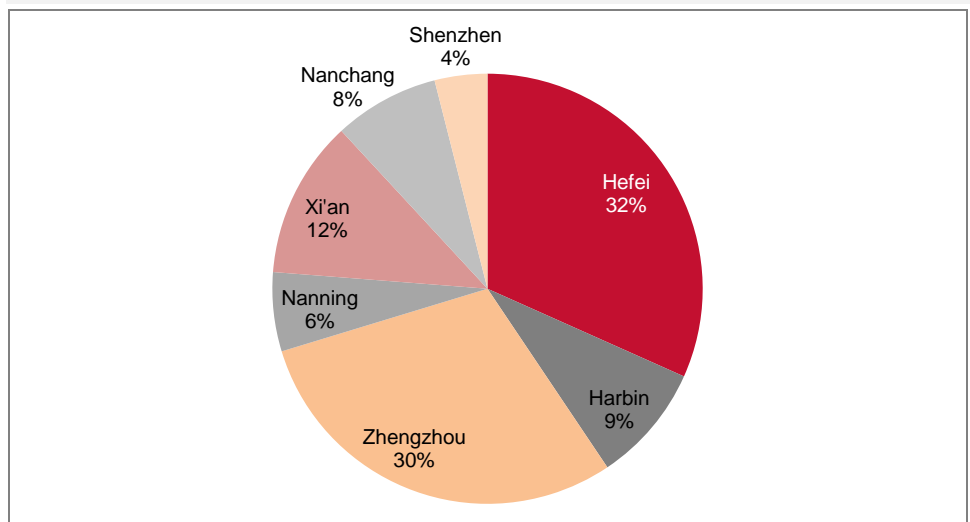
Source: Company, OP Research

Exhibit 16: CSC financial figures



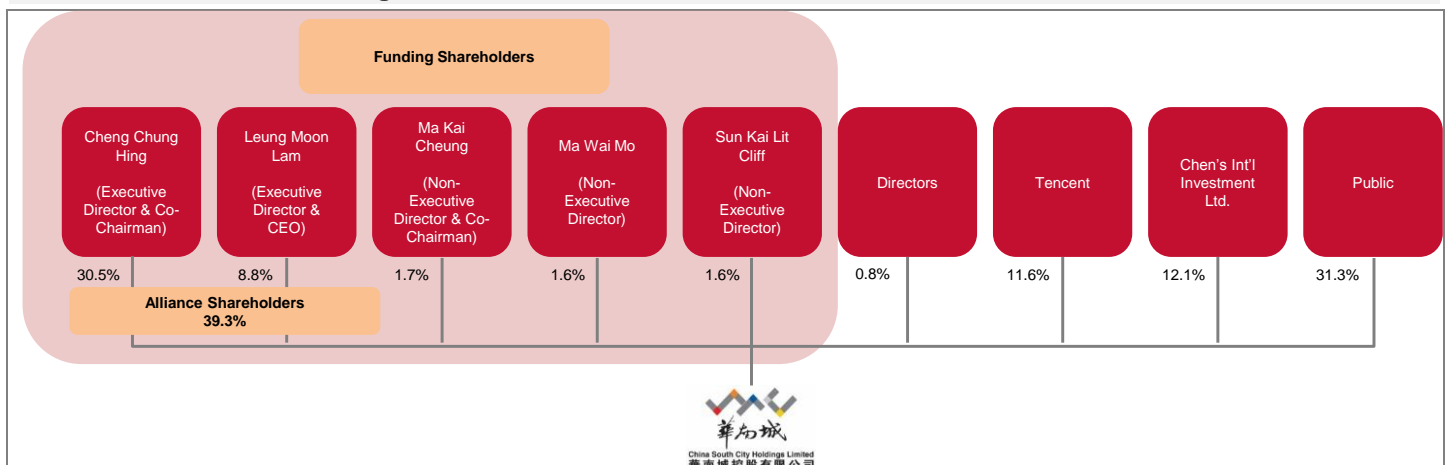
Source: Company, OP Research

Exhibit 17: CSC contracted sales in FY3/14



Source: Company, OP Research

Exhibit 18: CSC shareholding structure



Source: Company, OP Research

Note: On 15 September 2013, Mr. Cheng Chung Hing, Mr. Cheng Tai Po and Mr. Leung Moon Lam, together with their respective associates, approximately 39.37% in aggregate (or assuming all the Share Options held by Mr. Leung Moon Lam are fully exercised, approximately 40.23% in aggregate) of the total issued share capital of the Company as at 30 September 2014, have entered into an alliance agreement that a written approval from the other two alliance parties for any transfer of CSC shares. Certain first right of refusal and tag-along right are also granted to the alliance parties in respect of such transfer

Exhibit 19: Peer Group Comparison

Company	Ticker	Price	Mkt cap (US\$m)	3-mth		PER FY1	PER FY2	EPS FY1	EPS FY2	3-Yr EPS Cagr (%)	PEG (x)	Div	Div	P/B	P/B	EV/ Hist	EV/ Cur Yr	Net	Gross	Net	ROE Hist	ROE FY1 (%)	Sh px	
				avg t/o	PER Hist							Hist	gearing					margin	margin	ROE			1-mth	3-mth
China South	1668 HK	3.09	3,189	30.2	5.5	8.5	7.1	(34.7)	19.8	(4.2)	N/A	4.5	3.5	1.09	1.05	7.4	7.3	31.0	48.6	25.9	19.6	12.4	(9.6)	26.1
HSI		28,081.21			11.9	13.5	12.2	(11.8)	10.8	2.1	6.30	3.0	2.9	1.53	1.45						12.9	10.8	(1.2)	13.1
HSCEI		14,701.88			10.6	10.3	9.3	3.0	11.0	7.4	1.40	2.9	2.9	1.46	1.36						13.8	13.2	(0.3)	20.6
CSI300		5,181.43			21.9	19.1	16.7	15.0	14.3	15.4	1.24	1.2	1.5	3.04	2.72						13.9	14.3	7.8	45.0
Adjusted sector avg*					24.8	33.7	24.3	35.5	18.2	15.0	1.33	1.1	1.0	2.46	2.62	26.9	24.0	24.5	48.6	44.2	8.8	9.5	14.3	37.8
Zall Development	2098 HK	2.92	1,318	1.0	5.2	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	1.03	N/A	20.0	N/A	56.6	49.1	79.2	22.1	N/A	1.7	19.7
Wuzhou Internati	1369 HK	1.78	1,070	2.8	26.2	11.9	17.8	121.0	(33.3)	30.3	0.39	2.0	N/A	1.81	1.72	17.4	13.4	101.0	34.8	5.9	7.1	11.9	33.8	34.8
Hydoo Internatio	1396 HK	1.53	792	0.9	9.6	6.8	5.6	41.7	22.2	34.6	0.20	3.9	5.7	1.15	N/A	5.9	N/A	0.0	41.6	15.2	11.8	16.0	0.0	5.5
Beijing Properti	925 HK	0.88	767	1.7	34.9	146.7	88.0	(76.2)	66.7	(3.0)	N/A	N/A	N/A	1.43	1.28	(1,268.1)	75.0	55.2	82.1	82.2	4.4	(2.0)	15.8	41.9
Global Logistic	GLP SP	2.77	9,949	34.2	21.8	32.1	27.4	(32.0)	17.2	0.3	101.05	1.6	2.0	1.13	1.09	36.8	26.1	11.0	N/A	68.7	5.5	4.4	1.1	6.9
Zhejiang China-A	600790 CH	13.38	2,258	78.9	42.4	35.9	29.4	18.3	22.0	12.0	2.99	1.3	1.1	4.02	3.76	27.8	37.9	0.0	55.1	48.0	9.3	9.9	18.5	92.2
Haining China-A	002344 CH	28.31	5,110	77.9	33.7	26.7	23.3	26.4	14.3	16.0	1.66	0.5	0.7	6.68	5.26	23.7	18.8	0.0	65.3	43.3	18.8	19.0	16.6	63.6
Commodities Ci-A	600415 CH	16.59	14,554	238.6	221.2	88.7	42.0	149.3	111.2	62.2	1.43	0.4	0.2	10.10	10.30	56.9	N/A	48.4	45.4	11.2	4.7	7.5	26.9	124.0

* Outliners and "N/A" entries are in red and excl. from the calculation of averages

Source: Bloomberg, OP Research

Our recent reports

Date	Company / Sector	Stock Code	Title	Rating	Analyst
22/05/2015	EGL	6882	Fly me to the moon	BUY	Bruce Yeung
21/05/2015	On Time Logistics	6123	At the right time to make a move	BUY	Bruce Yeung
20/05/2015	HC International	2280	1Q15 results miss	SELL	Lindsay Hu/Yuji Fung
20/04/2015	Sinotrans	598	A mixed bag of 1Q15 results	BUY	Bruce Yeung
02/04/2015	Beijing Properties	925	Robust rental income growth in FY14	BUY	Bruce Yeung
31/03/2015	Far East Global	830	Coming out of the tunnel	NR	Bruce Yeung
30/03/2015	Shenzhen International	152	FY14 results beat with surprise in CBEC	BUY	Bruce Yeung
30/03/2015	Sinotrans	598	Buy on unjustified concerns	BUY	Bruce Yeung
27/03/2015	BWI Intl	2339	FY14 earnings record huge gain of HK\$183 mn	NR	Kelvin Ng
25/03/2015	Sinotrans	598	FY14 result first take	HOLD	Bruce Yeung
25/03/2015	COOLPAD	2369	Question marks over Dazen JV bring some cool	HOLD	Yuji Fung
24/03/2015	Technovator	1206	NDR Takeaway	BUY	Yuji Fung
23/03/2015	Shenzhen International	152	Decent dividend from toll road subsidiary	BUY	Bruce Yeung
19/03/2015	Technovator	1206	FY14 results First Take	BUY	Yuji Fung
18/03/2015	Ju Teng Intl	3336	In-line FY14 result; Margin expansion resumed	BUY	Yuji Fung
17/03/2015	Kwoon Chung Bus	306	Value unlocked	NR	Bruce Yeung
12/03/2015	BWI Intl	2339	FY14 earnings hit huge gain of HK\$169 mn	NR	Kelvin Ng
10/03/2015	Technovator	1206	Spin-off and poised to swamp China	BUY	Yuji Fung
03/03/2015	TCL COMM	2618	Strong guidance ahead	BUY	Yuji Fung
06/02/2015	Technovator	1206	Positive signaling from stake increase by ParentCo	BUY	Yuji Fung
04/02/2015	Beijing Properties	925	Divest for reinvesting logistics properties	BUY	Bruce Yeung
03/02/2015	TK Group	2283	When the best is served by the best of best	NR	Lindsay Hu/ Yuji Fung
15/01/2015	Ju Teng Intl	3336	Correction overdone	BUY	Yuji Fung
12/01/2015	TCL COMM	2618	Profits soar with Iron Man, X-men and OneTouch	BUY	Yuji Fung
09/01/2015	Technovator	1206	Past year promising, New Year winning	BUY	Yuji Fung
06/01/2015	Sinomedia	623	Downgrade on economic slowdown	HOLD	Yuji Fung
05/01/2015	SCUD Group	1399	Beneficiary of Xiaomi Success	BUY	Yuji Fung

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