Deutsche Bank
Markets Research

Rating
Hold

Asia
China

Property
Property

Company
Sunac

Reuters	Bloomberg	Exchange	Ticker
1918.HK	1918 HK	HSI	1918

Date
9 March 2015

Company Update

Price at 6 Mar 2015 (HKD)	7.09
Price target - 12mth (HKD)	7.35
52-week range (HKD)	8.15 - 3.52
HANG SENG INDEX	24,164

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Acquisition of Kaisa could turn out to be NAV-negative

Growing doubts on benefits of proposed acquisition of Kaisa

Recent announcements by Kaisa reveal that: 1) actual debts of Kaisa are significantly higher than previously reported or expected; 2) actual cash levels are meaningfully lower than expected; and 3) blockage of sales in its property projects are more serious than expected. In our view, all these highlight that: 1) Sunac might not have done adequate due diligence when it decided on the transaction, especially given that our est. NAV of Kasia turns out to be negative after factoring in the higher debts; and 2) the acquisition of Kaisa, even if completed, could be NAV-negative. Also, we continue to see higher operational, financial and political risks for Sunac following the purchase.

Latest statistics of Kaisa suggest that Sunac’s consideration is too high

According to Kaisa’s latest announcement, its total interest-bearing debt at end-2014 was RMB65bn, up significantly by RMB35.2bn from that reported at end-1H14, while its total cash balance has fallen significantly from RMB10.9bn at end-1H14 to only RMB1.9bn on 2 Mar 2015. Assuming that Kaisa’s total debt level did not increase from the level at end-2014, our latest estimated NAV for Kaisa would be at a negative value of RMB20.2bn (-HK$4.97/share) if its Shenzhen projects remain frozen by the government, and a negative value of RMB9.4bn (-HK$2.32/share) if its Shenzhen projects are unfrozen. In either scenario, Sunac’s consideration of HK$4.59bn looks very aggressive unless it can turn the negative NAV into a positive one within a short period of time.

A dilemma emerges on whether to proceed or not to proceed

In our view, given the lack of apparent NAV enhancement (and potential reduction), if the proposed acquisition of Kaisa is completed, the potential benefits to Sunac are not apparent, while the very different market positioning and geographical focuses between the two companies would result in an increase in operational, financial and political risks for Sunac. On the other hand, if the transaction is not completed, the time, efforts and resource of Sunac’s management will likely be wasted, not to mention the opportunity costs (potential growth from organic landbanking) involved.

We see fair valuations for Sunac, given aggressive acquisitions and higher risks

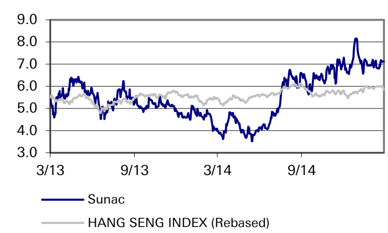
Our TP is based on a 45% discount to NAV (HK$13.32) while factoring the purchase of Kaisa (note the transaction has not been completed yet). We see risks to our est. NAV given high uncertainties with regard to the completion of the stake purchase in Kaisa. Key risks: unexpected economic & policy volatility.

Key changes

Price target	7.50 to 7.35	↓	-2.0%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	2.2	2.2	73.3
HANG SENG INDEX	-2.1	0.7	6.4

Source: Deutsche Bank

Forecasts And Ratios

Year End Dec 31	2012A	2013A	2014E	2015E	2016E
Sales (CNYm)	20,842.6	30,836.7	33,670.1	41,185.6	56,415.2
EBITDA(CNYm)	4,532.4	6,118.0	7,455.5	7,983.1	9,434.2
Reported NPAT(CNYm)	2,607.3	3,178.4	3,800.3	5,728.2	5,635.5
DB EPS FD (CNY)	0.80	0.95	1.13	1.70	1.68
PER (x)	3.3	4.6	5.1	3.4	3.4
Yield (net) (%)	3.0	4.4	3.5	3.8	4.0

Source: Deutsche Bank estimates, company data

Deutsche Bank AG/Hong Kong

Model updated:09 March 2015

Running the numbers

Asia

China

Property

Sunac

Reuters: 1918.HK | Bloomberg: 1918 HK

Hold

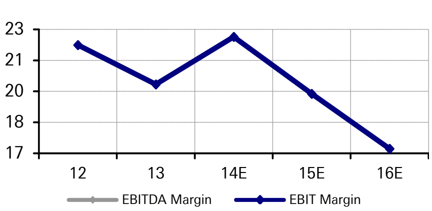
Price (6 Mar 15)	HKD 7.09
Target Price	HKD 7.35
52 Week range	HKD 3.52 - 8.15
Market Cap (m)	HKDm 21,270
	USDm 2,742

Company Profile

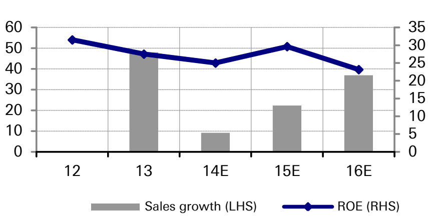
Sunac China Holdings Limited is an integrated residential and commercial property developer. To date, the Company has engaged in project developments in the Bohai-rim, South Jiangsu and Chengdu-Chongqing regions, which are currently in different phases and has covered a diverse range of property types, such as high-rise and mid-rise residences, detached villas, retail properties, offices and parking spaces.

Price Performance

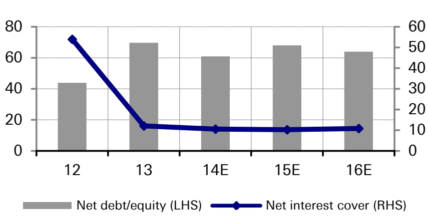
Margin Trends



Growth & Profitability



Solvency



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Fiscal year end 31-Dec	2012	2013	2014E	2015E	2016E
Financial Summary					
DB EPS (CNY)	0.80	0.95	1.13	1.70	1.68
Reported EPS (CNY)	0.87	0.95	1.13	1.70	1.68
DPS (CNY)	0.08	0.19	0.20	0.22	0.23
BVPS (CNY)	3.1	4.1	5.1	6.6	8.1
Weighted average shares (m)	3,005	3,302	3,315	3,315	3,315
Average market cap (CNYm)	7,926	14,450	17,176	17,176	17,176
Enterprise value (CNYm)	10,605	22,540	26,589	28,465	32,483
Valuation Metrics					
P/E (DB) (x)	3.3	4.6	5.1	3.4	3.4
P/E (Reported) (x)	3.0	4.6	5.1	3.4	3.4
P/BV (x)	1.55	0.90	1.13	0.87	0.71
FCF Yield (%)	96.7	40.1	nm	nm	nm
Dividend Yield (%)	3.0	4.4	3.5	3.8	4.0
EV/Sales (x)	0.5	0.7	0.8	0.7	0.6
EV/EBITDA (x)	2.3	3.7	3.6	3.6	3.4
EV/EBIT (x)	2.3	3.7	3.6	3.6	3.4
Income Statement (CNYm)					
Sales revenue	20,843	30,837	33,670	41,186	56,415
Gross profit	5,451	7,331	9,119	10,031	12,154
EBITDA	4,532	6,118	7,455	7,983	9,434
Depreciation	0	0	0	0	0
Amortisation	0	0	0	0	0
EBIT	4,532	6,118	7,455	7,983	9,434
Net interest income(expense)	-84	-506	-707	-778	-869
Associates/affiliates	-39	72	2,006	3,780	3,117
Exceptionals/extraordinaries	0	0	0	0	0
Other pre-tax income/(expense)	275	0	0	0	0
Profit before tax	4,685	5,684	8,755	10,985	11,683
Income tax expense	2,070	2,191	3,103	2,580	2,838
Minorities	7	315	1,852	2,677	3,209
Other post-tax income/(expense)	0	0	0	0	0
Net profit	2,607	3,178	3,800	5,728	5,635
DB adjustments (including dilution)	-206	0	0	0	0
DB Net profit	2,401	3,178	3,800	5,728	5,635
Cash Flow (CNYm)					
Cash flow from operations	7,692	5,824	-843	-1,297	-3,196
Net Capex	-25	-24	0	0	0
Free cash flow	7,667	5,800	-843	-1,297	-3,196
Equity raised/(bought back)	24	1,628	0	0	0
Dividends paid	-236	-261	-633	-663	-729
Net inc/(dec) in borrowings	1,297	4,851	6,293	-1,901	3,527
Other investing/financing cash flows	-1,420	-10,158	0	0	0
Net cash flow	7,332	1,861	4,817	-3,860	-399
Change in working capital	*6,610*	*4,813*	*-2,312*	*-3,020*	*-6,130*
Balance Sheet (CNYm)					
Cash and other liquid assets	12,263	16,009	20,825	12,006	11,608
Tangible fixed assets	928	552	564	579	595
Goodwill/intangible assets	0	0	0	0	0
Associates/investments	5,090	9,213	11,220	18,938	22,056
Other assets	52,654	71,581	94,278	107,008	103,725
Total assets	70,934	97,355	126,887	138,532	137,983
Interest bearing debt	17,526	28,706	34,999	33,098	36,625
Other liabilities	41,415	50,437	68,645	74,433	62,227
Total liabilities	58,940	79,144	103,644	107,531	98,852
Shareholders' equity	9,489	13,605	16,785	21,865	26,787
Minorities	2,505	4,606	6,458	9,135	12,344
Total shareholders' equity	11,994	18,211	23,243	31,001	39,132
Net debt	*5,263*	*12,698*	*14,174*	*21,092*	*25,017*
Key Company Metrics					
Sales growth (%)	nm	48.0	9.2	22.3	37.0
DB EPS growth (%)	na	18.3	19.1	50.7	-1.6
EBITDA Margin (%)	21.7	19.8	22.1	19.4	16.7
EBIT Margin (%)	21.7	19.8	22.1	19.4	16.7
Payout ratio (%)	9.1	19.8	17.4	12.7	13.5
ROE (%)	31.5	27.5	25.0	29.6	23.2
Capex/sales (%)	0.1	0.1	0.0	0.0	0.0
Capex/depreciation (x)	nm	nm	nm	nm	nm
Net debt/equity (%)	43.9	69.7	61.0	68.0	63.9
Net interest cover (x)	54.0	12.1	10.6	10.3	10.9

Source: Company data, Deutsche Bank estimates

Too anxious to pursue acquisition growth

Acquisition of Kaisa could turn out to be NAV-negative

In our view, the announced proposed acquisition of Kaisa within such a short period of time highlights that Sunac is relatively anxious to pursue third-party acquisition growth instead of organic growth, especially after the cancellation of the previously proposed purchase of a 24% stake in Greentown (cancelled in Dec 2014).

Recent announcements by Kaisa reveal that:

1) actual debts of Kaisa are significantly higher than previously reported or expected;

2) actual cash levels are meaningfully lower than expected; and

3) blockage of sales in its property projects are more serious than expected.

In our view, all these highlight that:

1) Sunac might not have done adequate due diligence when it decided on the transaction, especially given that our est. NAV of Kasia turns out to be negative after factoring in the higher debts; and

2) the acquisition of Kaisa, even if completed, could likely be NAV-negative.

Also, we continue to see higher operational, financial and political risks for Sunac following the purchase.

Latest Kaisa statistics suggest Sunac's consideration is too high

According to Kaisa's latest announcement, its total interest-bearing debt at end-2014 was RMB65bn, up significantly by RMB35.2bn from that reported at end-1H14, while its total cash balance has fallen significantly from RMB10.9bn at end-1H14 to only RMB1.9bn on 2 Mar 2015.

Assuming that the total debt level of Kaisa did not increase from the end-2014 level, our latest estimated NAV for Kaisa would be at a negative value of RMB20.2bn (-HK$4.97/share) if its Shenzhen projects remain frozen by the government, and a negative value of RMB9.4bn (-HK$2.32/share) if its Shenzhen projects are unfrozen.

In either scenario, Sunac's consideration of HK$4.59bn looks very aggressive unless it can turn the negative NAV into a positive one within a short period of time.

Figure 1: Kaisa – Estimated NAV after factoring latest announcements by Kaisa (on 8 Mar 2015)

RMBmn	Scenario A (if Shenzhen projects still frozen)	Scenario B (if Shenzhen projects unfrozen)
Est. Gross Asset Value	54,006	64,753
Outstanding Land Premium	(11,060)	(11,060)
Est. Gross Asset Value after O/S Land Premium	**42,946**	**53,693**
Gross Debts at end-2014	65,000	65,000
Cash at end-Mar 2015	1,897	1,897
Net Debt	**(63,103)**	**(63,103)**
Est. NAV	(20,157)	(9,410)
Est. NAV Per Share	(3.9)	(1.8)
Est. NAV (HK$mn)	(25,544)	(11,925)
Est. NAV Per Share	(4.97)	(2.32)
Sunac's Purchase Price (HK$)	1.80	1.80
Sunac's Stake	49.25%	49.25%
Sunac's Consideration for 49.25% (HK$mn)	**4,591**	**4,591**

Source: Kaisa, Company, Deutsche Bank

Figure 2: Kaisa – Updates on asset & liabilities (from announcement by Kaisa on 8 Mar 2015)

RMBbn	At end-2013	At end-1H14	At end-2014
Total Assets	87.8	105.6	110.4
Interest-Bearing Debt	22.2	29.8	64.0
Other Liabilities	43.8	50.1	36.2
Total Liabilities	66.1	79.9	100.2
Net Assets	**21.8**	**25.8**	**10.2**
Impact on Sunac			
Net Assets (HK$bn)	27.6	32.6	12.9
49.25% of Net Assets	13.6	16.1	6.3
Sunac's consideration			**4.6**
Est. Value-Added to Sunac			**1.8**

Source: Deutsche Bank, Company data

A dilemma emerges on whether to proceed or not to proceed

In our view, given the lack of apparent NAV-enhancement (and potential reduction), if the proposed acquisition of Kaisa is completed, the potential benefits to Sunac are not apparent, while the very different market positioning and geographical focuses between the two companies would result in an increase in operational, financial and political risks for Sunac.

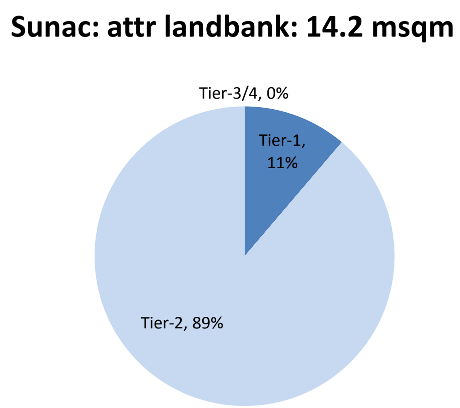
On the other hand, if the transaction is not completed, the time, efforts and resource of Sunac’s management will likely be wasted, not to mention the opportunity costs (potential growth from organic landbanking) involved.

We are concerned about strategic and geographical mismatches between Sunac and Kaisa

We used to like Sunac because of its strategic focus on prime-location, higher-end properties in Tier-1 and key Tier-2 cities. On our estimates, Tier-1 cities account for 11% of Sunac's landbank and 35% of GAV, while Tier-2 cities account for 89% of its landbank and 65% of GAV. Kaisa is very different from Sunac, as Kaisa focuses more on mid-end properties, and more in Tier-2-4 cities.

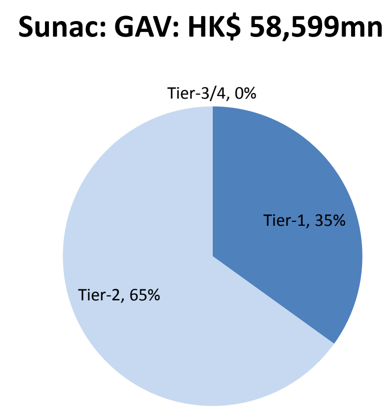
On our analysis, Tier-1 cities make up only 14% of Kaisa's landbank and 23% of GAV, while Tier-3/4 cities make up about 60% of its landbank and 43% of its GAV. Hence, we see very different market positioning and geographical focuses between Kaisa and Sunac. In our view, the acquisition of Kaisa would dilute Sunac's focus on core cities and stretch management resources. Also, with our expected relatively low margins for Kaisa's projects in Tier-2-4 cities, Sunac's margins would likely see more downward pressure. Lastly, as the Shenzhen projects of Kaisa are still frozen by the government, there are also risks of Sunac taking ownership and operating these projects.

Figure 3: Sunac – Landbank breakdown by city tier



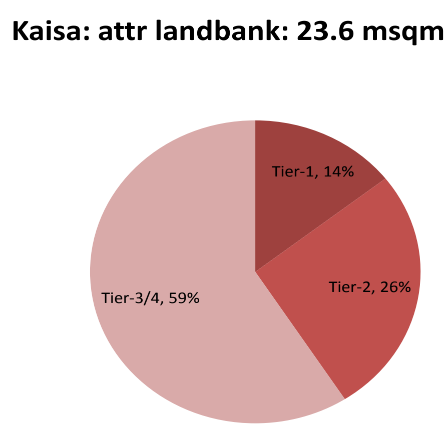
Source: Company, Deutsche Bank 1H14

Figure 4: Sunac – GAV breakdown by city tier



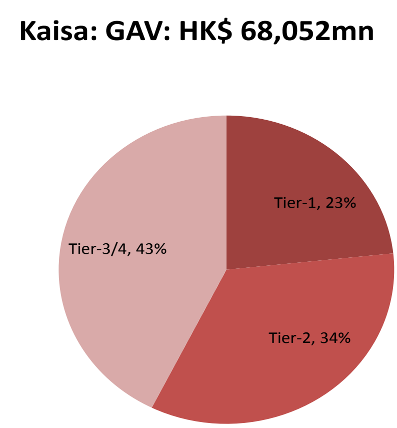
Source: Company, Deutsche Bank March 2015

Figure 5: Kaisa – Landbank breakdown by city tier



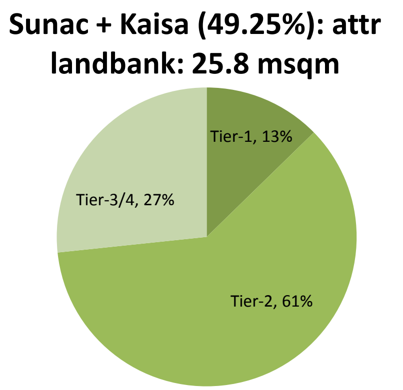
Source: Company, Deutsche Bank 1H14

Figure 6: Kaisa – GAV breakdown by city tier



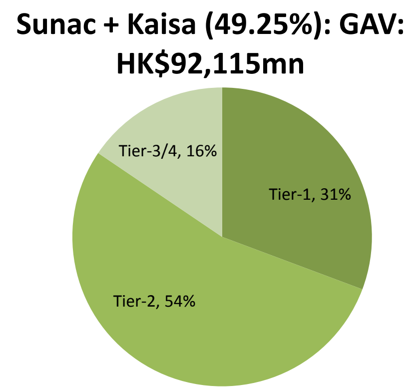
Source: Company, Deutsche Bank March 2015

Figure 7: Sunac + Kaisa (49.25%) – Landbank breakdown by city tiers



Source: Company, Deutsche Bank 1H14

Figure 8: Sunac+ Kaisa (49.25%) – GAV breakdown by city tiers



Source: Company, Deutsche Bank March 2015

Acquisition of Kaisa would increase Sunac's net gearing by 22-30%-pts

On our analysis, if Sunac just acquires the 49.25% equity stakes of Kaisa, share options and the 2015 CB, Sunac would need to pay about HK$5.78bn, and its end-2015E net gearing would rise by about 22%-pts to 96%.

Figure 9: Sunac's payment (if its does not need to make a general offer)

Items	Number	Unit Offer Price (HK$)	Total Consideration (HK$)
49.25% equity stakes	2,529,196,133	1.8	4,552,553,039
Share options with exercise price of HK$1.5	127,801,000	0.3	38,340,300
Share options with exercise price of HK$2.0	34,335,000	0.0001	3,434
Share options with exercise price of HK$2.61	11,000,000	0.0001	1,100
Share options with exercise price of HK$2.84	3,000,000	0.0001	300
Subtotal			**4,590,898,173**
2015 CB (RMB1.5bn USD settled 8% due 2015)	1,748,166,880	0.68	1,188,753,478
Total			**5,779,651,651**

Source: Company, Deutsche Bank

And if Sunac also needs to proceed with the possible mandatory general offer and purchase the 20.81% public float of Kaisa, Sunac's 2015E net gearing would go up by another 8%-ppts. Given weaker offshore bonds markets (with rising rates) for Chinese developers and expected RMB depreciation, we expect rising effective borrowing costs for Sunac. With higher net gearing after the transaction, we now also see higher financial risks.

Uncertainties regarding the completion of the transaction: proposed debt restructuring of Kasia involves maturity extension and lower coupon

Kaisa's debt restructuring plan for off-shore bond-holders is based upon 5 principles: 1) Equitable treatment of all creditors representing their inter-creditor priority; 2) No impairment of any creditor's principal debt claim and repayment of that principal in full over time; 3) Initial cash interest holiday; 4) timely support and high participation from all creditors; and 5) Short timetable. In particular, the plan generally involves an extension of the maturity date by 5 years, interest holiday in the first 2 years and substantially lower coupon by 2.9-7.7 percentage points. In our view, as creditors have already incurred a weighted average lost of 34%, the weighted average incremental benefit for accepting the plan is only 9%, we see a risk that creditors may vote against the proposal and hence, blocking Sunac's proposal to move forward.

Taking a look at past M&A activities in China property

Most M&A activities in the past have not been that successful

Industry consolidations normally take two forms:

1) organic market share gains via good operations (i.e. buying land, doing development, and selling properties); and

2) M&A activities (like one developer acquiring another developer).

Looking at the major M&A activities in the China property market in the past, we found that most M&A activities have not shown good outcomes. In particular, past M&A activities that involved active management and operations of the buyers have not turned out positive results, for the most part.

Conversely, past M&A activities that involved only passive investment have tended to show stronger operational/financial results. Interestingly, this is consistent with the fact that most leading developers have been growing mainly via organic means (e.g. land purchases from government).

Not that many M&A activities have taken place in the past

In the past 9 years, the China property market has already gone through 3 up-and-down cycles already, but despite this, the number of major M&A activities was not high, and we identified only 8, including:

1) Road King's acquisition of Sunco in 2006;

2) COLI's purchase of Shell Electric in 2009;

3) Shanghai Industrial's purchase of Neo China in 2010;

4) Wharf's purchase of Greentown in 2012;

5) Sunac's purchase of Greentown in 2014;

6) CCCG's purchase of Greentown in 2014;

7) China Life and Nan Fung's purchase of Sino Ocean in 2009-13; and

8) Sunac's proposed conditional acquisition of Kaisa in 2015.

Figure 10: China Property – Major M&A activities in the past

No	Target Company	Buyer	Date	Share and %	Consideration	Takeover / management by Buyer	Performances after the event	Success? (DB's view)
1	Sunco Property (Not Listed)	Road King (1098.HK)	Dec-06	55% of enlarged cap	RMB 1.28bn	Yes	After the deal completed, Road King cannot get the controlling power until Oct 2007. Road King then sued Mr. Sun for not disclosing potential debts.	No
	Sunco Property (Not Listed)	Road King (1098.HK)	Jul-07	39.74% of enlarged cap	RMB 0.445 bn	Yes	In Nov 2007, Road King announced that it has submitted application on spinning off Sunco for listing, but Mr. Sun sued Road King in Jan 2008, pledging Road King violated the M&A contract.	No
2	Neo-China Land (0563.HK) Name changed to Shanghai Industrial Urban Development	Shanghai Industrial Holdings (0363.HK)	Jun-10	45.02% of enlarged cap	HK$2.32/shr; Total: HK$2.75bn	Yes	No significant turnaround yet.	Not yet
3	Shell Electric Manufacturing (0081.HK)	COLI (0688.HK)	Sep-09	23.08% of enlarged cap	HK$2.90/shr; Total: HK$0.46bn	Yes	COGO recorded solid growths in sales and earnings in 2011-2013, financial positions improved and borrowing costs fell.	Not yet
	Name changed to COGO		Feb-10	31.36% of enlarged cap	HK$5.0/shr; Total HK$2.62bn	Yes	However, previous owners of Shell Electric retained ownership, resulting in complicated shareholding structure. Also profit warnings have been announced for 2014.	Not yet
4	Greentown (3900.HK)	Wharf (0004.HK)	Jun-12	24.3% of enlarged cap	HK$5.2/shr Total for shr: HK$2.548bn; CB: HK$3.393bn	No	Company became more prudent on new land acquisitions and gained better access to financing. Net gearing fell, borrowing costs also fell.	Yes
5	Greentown (3900.HK)	Sunac (1918.HK)	May-14	24.30%	HK$12.0/shr; Total: HK$6.298 bn	Yes (before the deal closed and cancelled)	The deal was cancelled on 24 Dec 2014. Sunac proposed to buy the Sunac-Greentown JV platform on 31 Dec, but Greentown disagreed.	No
6	Greentown (3900.HK)	China Communications Construction Group	Dec-14	24.29%	HK$11.4/shr; Total: HK$6.015bn	No	Borrowing cost is expected to fall further.	Yes
7	Sino-Ocean (3377.HK)	China Life (2628.HK)	Dec-09	16.57% of enlarged cap	HK$6.23 / shr; Total HK$0.75bn	No	Sino Ocean has since been going through a turnaround.	Yes
		China Life (2628.HK)	Jan-10	7.51%	approx. HK$7.08 / shr; Total: HK$3.08bn	No	The turnaround is successfully taking place:	Yes
		China Life (2628.HK)	Oct-13	8.74% of enlarged cap	HK$4.74 / shr; Total HK$3.01bn	No	1) Margins of Sino Ocean has stabilized.	Yes
		Nan Fung Group	Dec-10	11.70%	HK$5.60 / shr; Total HK$3.69bn	No	2) Sales growth of Sino Ocean has resumed.	Yes
		Nan Fung Group	Jul-11	PCS, approx. 5.69% of enlarged cap	HK$6.85 / shr; Total approx. HK$2.59bn (through PCS)	No	3) Borrowing costs of Sino Ocean have been falling	Yes
		Nan Fung Group	Oct-13	9.43% of enlarged cap	HK$4.74 / shr; Total HK$3.25bn	No		Yes
8	Kaisa (1638.HK)	Sunac (1918.HK)	Feb-15	49.25%	HK$1.80 / shr; Total HK$4.55bn	Yes (Proposed)	Pending completion	TBC

Source: Company, HKEX, Soufun, house.china.com.cn, Ming Pao; Deutsche Bank

Have past M&A activities returned positive outcomes?

M&As with active management by buyers have not shown good results, in our opinion

Looking at these past major activities, we found out that past M&A activities that involved a management takeover or active management of the acquirers in the acquired companies and/or acquired assets have, in general, not returned positive outcomes (like sales and earnings growth).

On our analysis, the likely reasons behind this relative lack of success include:

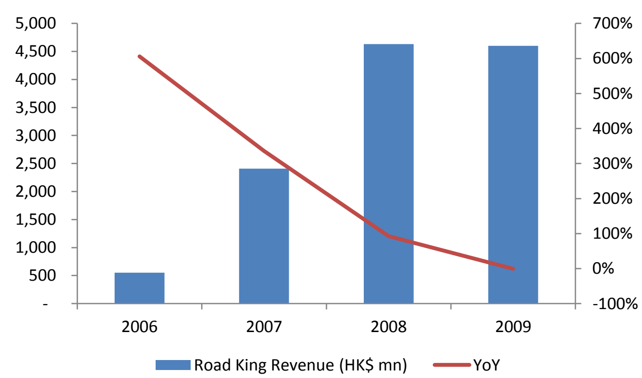
1) Actual debt levels of the acquired companies turned out to be much higher than expected or reported;

2) Differences in operational strategies and product positioning between the buyers and the acquired companies;

3) Previous owners of the acquired companies retained their shareholdings, leading to complicated shareholding structure that affected capital expansion and growth; and

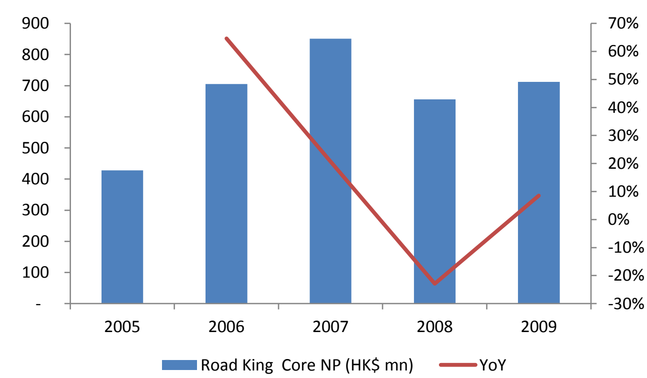
4) Previous management members of the acquired companies retained their influence, resulting in cultural conflicts or operational challenges.

Figure 11: Road King – Revenue



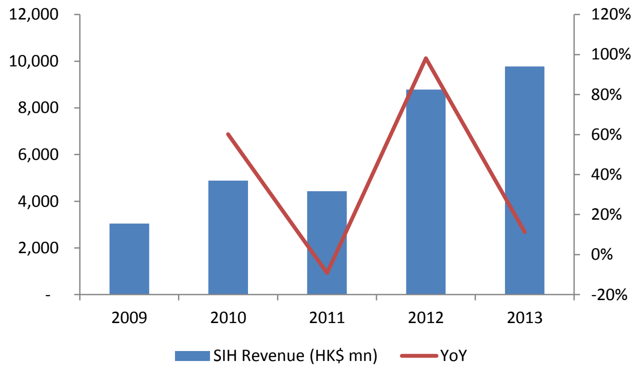
Source: Company, Deutsche Bank

Figure 12: Road King – Core net profit



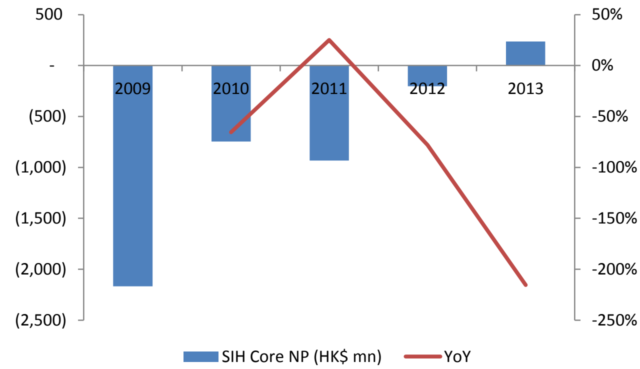
Source: Company, Deutsche Bank

Figure 13: Shanghai Industrial Urban Development – Revenue



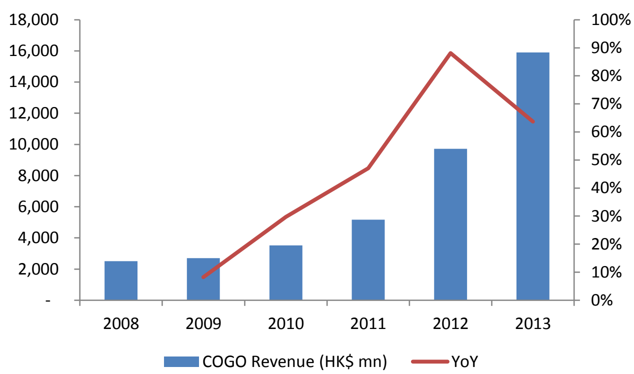
Source: Company, Deutsche Bank

Figure 14: Shanghai Industrial Urban Development – Core net profit



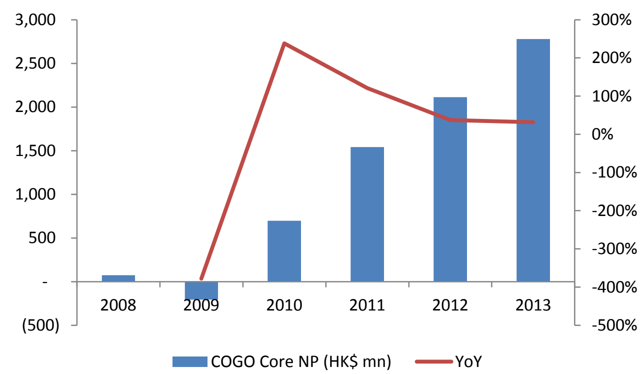
Source: Company, Deutsche Bank

Figure 15: COGO – Revenue



Source: Company, Deutsche Bank

Figure 16: COGO – Core net profit



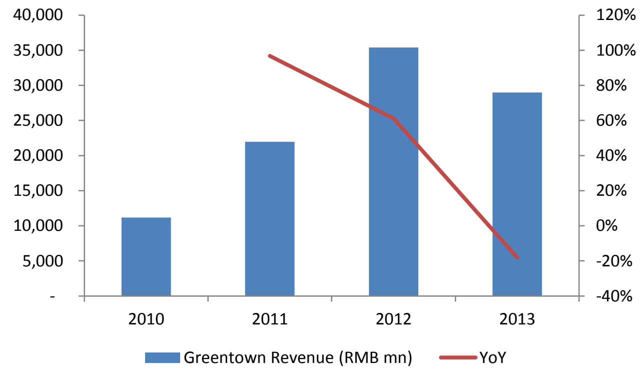
Source: Company, Deutsche Bank

M&As that involved only passive investment but buyers have done better

Conversely, M&A activities that represented more just a pass investment by the buyers in the acquired companies have tended to return better outcomes, like operational and/or financial turnaround, in the form of stronger financial positions, lower borrowing costs, more disciplined land purchases, recovering margins.

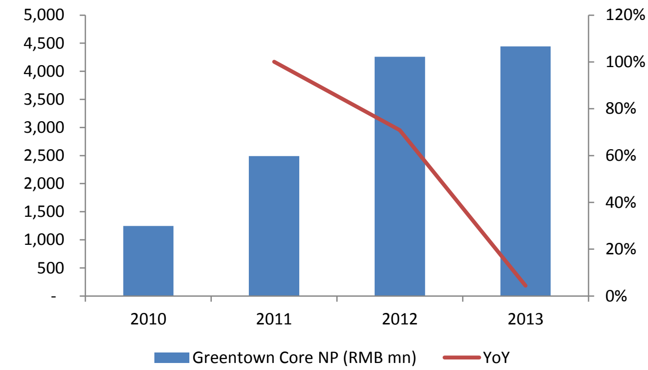
Examples are China Life and Nan Fung's purchases at Sino Ocean. For Greentown China, the stake purchase by Wharf in 2012 has led to a more prudent approach on new land acquisitions, and Greentown's net gearing has started to show meaningful improvement. At the same time, after Wharf's investment, Greentown has been able to gain better access to financing and borrowing costs have also fallen meaningfully.

Figure 17: Greentown – Revenue



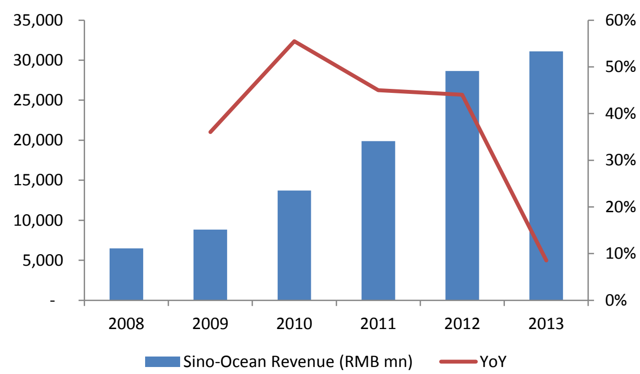
Source: Company, Deutsche Bank

Figure 18: Greentown – Core net profit



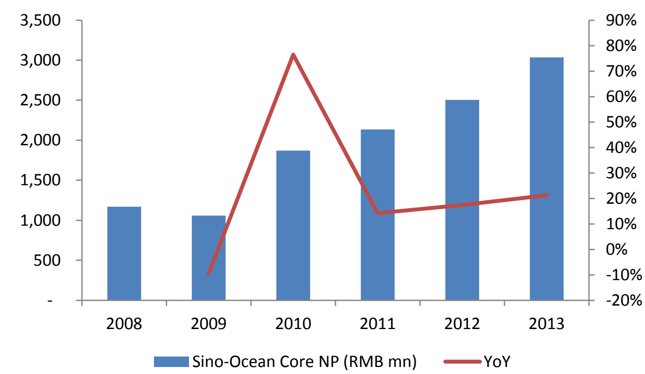
Source: Company, Deutsche Bank

Figure 19: Sino-Ocean – Revenue



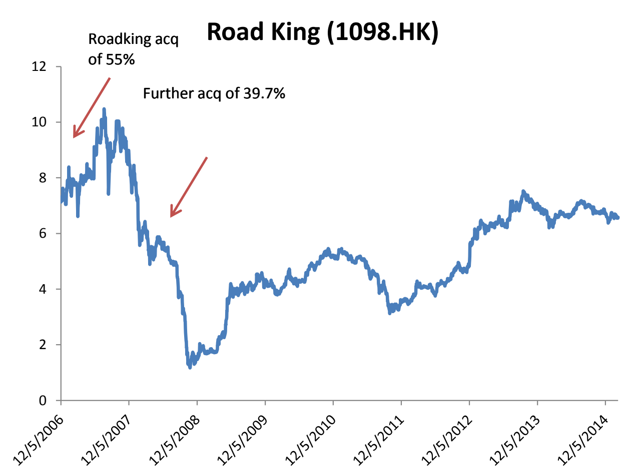
Source: Company, Deutsche Bank

Figure 20: Sino-Ocean – Core net profit



Source: Company, Deutsche Bank

Figure 21: Road King: share price performance after proposed acquisition of Sunco

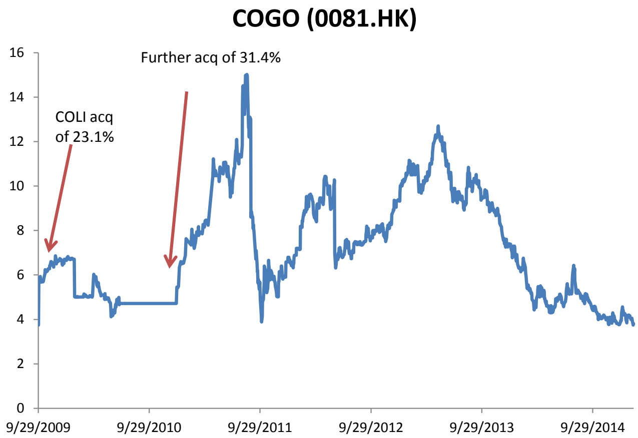


Source: Company, Deutsche Bank

Figure 22: Shanghai Industrial Urban Development: share price performance after purchase by Shanghai Industrial

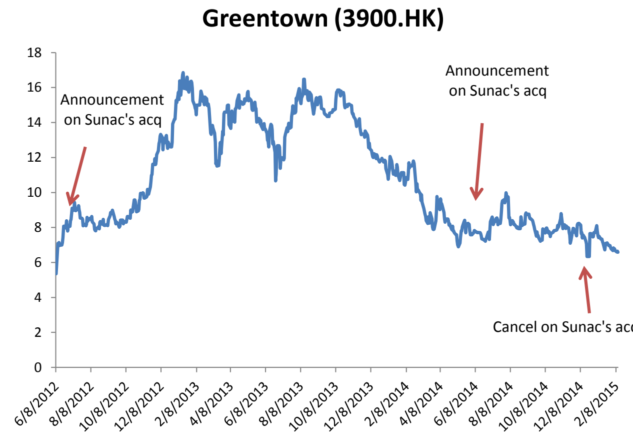
Source: Company, Deutsche Bank

Figure 23: COGO: share price after purchase by COLI



Source: Company, Deutsche Bank

Figure 24: Greentown: share price after stake purchase by Wharf and later by Sunac



Source: Company, Deutsche Bank

Financial analysis

NAV and earnings revisions

We have revised down our estimated NAV for Sunac from HK$13.47/share to HK$13.32/share as we adjusted down our estimated value for Kaisa (49.25% equity stake and the CB) in our model. With this, we have also lowered our target price for Sunac from HK$7.50 to HK$7.35. When determining our TP, we are now applying a 45% NAV discount (wider than the big-cap leaders) on Sunac's ex-Kaisa assets given Sunac's consistent aggressive stance on new acquisitions, the mismatch between Sunac's own landbank and the landbank of Kaisa that may lead to managerial and operational problems for the management of Sunac, the continued uncertainties with regard to the status of Kaisa's projects, and the resulting sharp increases in our estimated end-2015 net gearing of Sunac following the acquisitions.

Figure 25: Sunac – Income Statement (HK$ mn)

Year Ended Dec 31	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E
Property Development	3,433	4,777	6,594	10,433	20,654	30,565	33,361	40,850	56,051
Property Management	-	-	41	153	171	240	264	291	320
Property Investment	16	18	19	18	17	32	45	45	45
Total Revenue	**3,449**	**4,795**	**6,654**	**10,604**	**20,843**	**30,837**	**33,670**	**41,186**	**56,415**
Property Development	1,078	1,359	2,877	3,554	5,422	7,221	9,026	9,975	12,137
Property Management	-	-	1.29	12.97	(39.34)	(44.76)	(49.23)	(54.16)	(59.57)
Property Investment	-	-	-	-	-	-	18	18	18
Other expenses	(175)	(154)	(242)	(604)	(850)	(1,059)	(1,539)	(1,955)	(2,662)
EBIT	**902**	**1,206**	**2,636**	**2,962**	**4,532**	**6,118**	**7,455**	**7,983**	**9,434**
Net financing cost	(106)	(108)	(168)	(183)	(84)	(506)	(707)	(778)	(869)
Share results of associates	(10)	188	129	(10)	(39)	72	2,006	3,780	3,117
Exceptional item	(26)	57	-	760	275	-	-	-	-
Pre-tax profit	**761**	**1,342**	**2,597**	**3,528**	**4,685**	**5,684**	**8,755**	**10,985**	**11,683**
Income tax	(170)	(307)	(550)	(710)	(938)	(1,290)	(2,189)	(2,400)	(2,473)
LAT	(114)	(164)	(507)	(435)	(1,132)	(901)	(914)	(180)	(365)
Minority interests	(19)	46	16	27	7	315	1,852	2,677	3,209
Net profit	**496**	**825**	**1,525**	**2,356**	**2,607**	**3,178**	**3,800**	**5,728**	**5,635**
EPS	0.17	0.28	0.64	0.79	0.87	0.96	1.15	1.73	1.70

Source: Company, Deutsche Bank

Figure 26: Sunac – Cashflow Statement (HK$ mn)

For Year Ended Dec 31	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E
Profit before tax	902	1,206	2,636	3,528	4,685	5,684	7,455	7,983	9,434
Non cash adjustments	15	14	-	(496)	(97)	616	-	-	-
Working capital changes	(541)	631	(4,287)	(4,462)	6,610	4,813	(2,312)	(3,020)	(6,130)
Income tax paid	(138)	(210)	(1,327)	(1,246)	(1,688)	(2,790)	(2,647)	(2,841)	(2,709)
Interests paid	-	-	-	(202)	(1,817)	(2,500)	(3,340)	(3,419)	(3,792)
Net cash from operation	**239**	**1,640**	**(2,978)**	**(2,877)**	**7,692**	**5,824**	**(843)**	**(1,297)**	**(3,196)**
Disposal / purchase	(179)	(289)	-	(1,466)	(5,238)	(15,040)	-	-	-
Others	(45)	(60)	-	(13)	(22)	(27)	-	(4,959)	-

Net cash from investing activities	**(223)**	**(349)**	**-**	**(1,479)**	**(5,260)**	**(15,067)**	**-**	**(4,959)**	**-**
Net change in borrowings	(114)	(308)	3,471	2,961	2,071	8,674	6,293	(1,901)	3,527
Equity raised	19	-	2,041	200	1,365	3,481	-	-	-
Dividends paid	-	(198)	-	-	(236)	2,196	(633)	(663)	(729)
Net cash from financing activities	**(95)**	**(506)**	**5,513**	**3,161**	**3,199**	**14,351**	**5,659**	**(2,564)**	**2,797**
Net change in cash and cash equivalents	**(79)**	**785**	**2,534**	**(1,195)**	**5,632**	**5,107**	**4,817**	**(8,819)**	**(399)**
Beginning cash	**718**	**639**	**1,424**	**3,958**	**2,763**	**8,394**	**13,414**	**18,231**	**9,412**
Ending cash	**639**	**1,424**	**3,958**	**2,763**	**8,394**	**13,414**	**18,231**	**9,412**	**9,013**

Source: Company, Deutsche Bank

Figure 27: Sunac – Statement of Financial Position (HK$ mn)

As at Dec 31	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E
Cash and equivalents	639	1,424	3,958	2,763	8,394	13,414	18,231	9,412	9,013
Charged bank deposits	231	512	291	1,104	3,869	2,595	2,595	2,595	2,595
Receivables	593	404	682	1,345	416	1,214	1,168	1,634	2,242
Inventories and PUD	7,104	5,808	9,042	25,651	46,401	58,106	80,849	93,113	89,222
Other current asset	1	-	-	-	5,752	12,261	12,261	12,261	12,261
Total Current assets	**8,568**	**8,148**	**13,973**	**30,863**	**64,832**	**87,590**	**115,103**	**119,014**	**115,333**
Investment properties	433	584	584	552	571	252	304	318	332
Fixed assets and land use rights	13	9	18	28	49	65	26	28	29
Goodwill	258	258	258	-	-	-	-	-	-
Intangible asset	30	24	51	314	309	234	234	234	234
Interests in subsidiaries and associate	100	640	638	1,421	4,205	7,909	9,915	12,310	13,638
Other non-current assets	54	55	228	435	970	1,305	1,305	6,628	8,418
Total non-current assets	**888**	**1,569**	**1,776**	**2,749**	**6,103**	**9,765**	**11,784**	**19,518**	**22,651**
Total assets	**9,457**	**9,717**	**15,750**	**33,613**	**70,934**	**97,355**	**126,887**	**138,532**	**137,983**
Payables	2,141	2,188	2,447	5,213	7,116	12,402	16,681	9,396	11,771
Advance from customers	3,277	2,456	1,422	5,840	15,146	13,647	27,120	40,455	25,744
Short term debt	1,154	677	1,518	2,320	11,783	7,835	13,440	10,631	8,892
Other current liabilities	101	207	731	1,255	5,096	6,512	6,968	6,707	6,836
Total current liabilities	**6,672**	**5,528**	**6,118**	**14,628**	**39,141**	**40,396**	**64,209**	**67,188**	**53,243**
Long term borrowings	1,519	2,102	4,757	9,321	9,942	20,872	21,559	22,467	27,733
Other non-current liabilities	190	216	211	2,258	4,704	6,483	6,483	6,483	6,483
Total non-current liabilities	**1,709**	**2,318**	**4,968**	**11,579**	**14,646**	**27,355**	**28,042**	**28,950**	**34,216**
Total liabilities	**8,380**	**7,846**	**11,086**	**26,207**	**53,787**	**67,751**	**92,251**	**96,138**	**87,459**
Minority Interests	539	500	-	355	2,505	4,606	6,458	9,135	12,344
Total net Asset	**538**	**1,371**	**4,664**	**7,051**	**14,642**	**24,998**	**28,178**	**33,258**	**38,180**
Capital and retained earnings	423	1,250	4,499	6,709	9,006	13,561	16,729	21,794	26,700
Other reserves	115	121	165	342	483	44	56	72	88
Shareholders' funds	**538**	**1,371**	**4,664**	**7,051**	**9,489**	**13,605**	**16,785**	**21,865**	**26,787**
BVPS	0.18	0.46	1.55	2.35	3.15	4.10	5.06	6.60	8.08

Source: Company, Deutsche Bank

Valuation

Our estimated NAV for Sunac is HK$13.32/share

Our target price of HK$7.35 for Sunac is based on a 45% discount to our estimated NAV for Sunac assets excluding Kaisa and our TP of HK$1.8 per share for Sunac's stakes in Kaisa. When determining our target price, we are now applying a 45% NAV discount (wider than the big-cap leaders) on Sunac's ex-Kaisa assets given Sunac's aggressive stance on new acquisitions, the mismatch between Sunac's own landbank and the landbank of Kaisa that may lead to managerial and operational problems for the management of Sunac, the continued uncertainties with regard to the status of Kaisa's projects, and the resulting sharp increases in our estimated end-2015 net gearing of Sunac following the acquisitions.

We calculate our estimated NAV for Sunac by using sum-of-the-parts methodology. We apply DCF to estimate the value of the company's development projects by taking the estimated cash inflows from property sales minus the outstanding costs, including any outstanding land costs, construction costs, related income taxes and the LAT for each of the development projects. With respect to the investment properties' valuation, we use the income capitalization approach, taking the estimated rental revenues of the investment properties divided by the estimated capitalization (cap) rates. For different types of properties in different locations, our estimated rents and cap rates differ. In arriving at the NAV for the company, we take the aggregate estimated value for the previously mentioned business segments and then add the company's net cash position or subtract its net debt position. Specifically, our estimated NAV of HK$13.47/share incorporates the following assumptions:

1) ASP increases of 3-5% for Tier-1 cities in 2015;

2) Full payment of the LAT (estimated according to the LAT formula);

3) WACC of 12.2%,

4) Our TP of HK$1.8 for Sunac's stake in Kaisa, and

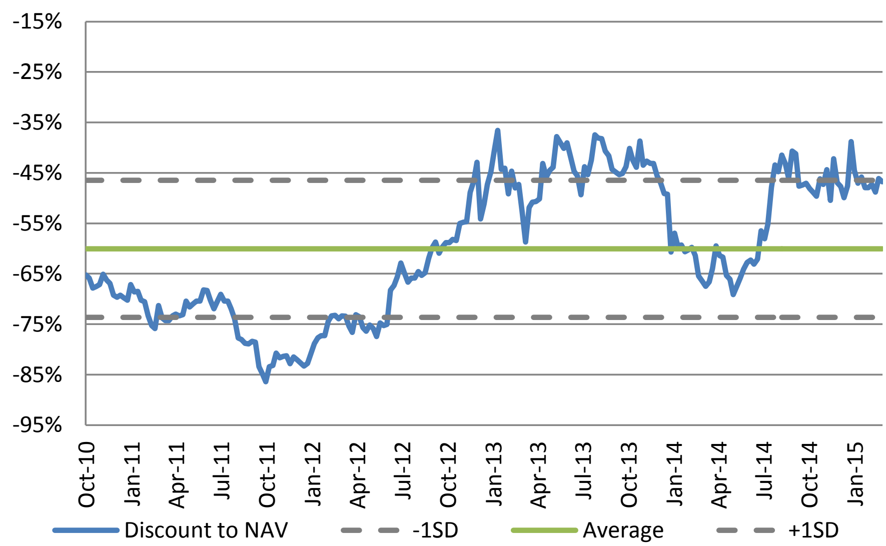
5) Cap rates of 8-10% for the investment properties of Sunac.

Figure 28: Sunac – Estimated NAV

	HK$mn	HK$/Share	% of NAV	% of GAV
Property Development				
Residential	57,820	17.44	131%	89%
Office	3,749	1.13	8%	6%
Retail	418	0.13	1%	1%
Others	2,376	0.72	5%	4%
Total Property Development	**64,362**	**19.41**	**146%**	**99%**
Property Investment				
Retail	816	0.25	2%	1%
Others	20	0.01	0%	0%
Total Property Investment	**837**	**0.25**	**2%**	**1%**
Stake in Kaisa	4,553	1.37	10%	7%
Kaisa CB	1,188.8	0.36	3%	2%
Outstanding LAT Payables	(5,760)	(1.74)	-13%	-9%
Total Other Assets	(19)	(0.01)	0%	0%
Gross Asset Value	**65,180**	**19.66**	**148%**	**100%**
Net Cash/(Debt)	(21,017)	(6.34)	-48%	
NAV	**44,163**	**13.32**	**100%**	

Source: Deutsche Bank

Figure 29: Sunac - Historical discount to NAV



Source: Bloomberg Finance LP; Deutsche Bank

Investment risks

Macro risks

Downside:

Government property tightening measures might be stricter than expected

The China property market is not only dependent on economic conditions and the demand-and-supply balance, but also on government policies. At times when the government is tightening its fiscal and monetary policies, especially via administrative measures, there could be volatile moves in housing transaction volumes, housing prices, land prices, and financing available to developers and homebuyers. With this in mind, if the government property market tightening measures are stricter than expected or if the impact of the measures already introduced is stronger than expected, we could see weaker-than-expected sales and price performance for the property businesses of Chinese property companies, including Sunac.

Unexpected economic fluctuations in the Chinese economy

In our view, any weaker-than-expected performance in the Chinese economy would likely result in weaker housing demand, hence affecting Chinese developers' property sales. On the other hand, any overly strong growth in the Chinese economy could raise concerns about overheating and attract tightening measures from the government. Therefore, any unexpected fluctuations in the Chinese economy would likely affect demand and supply in the China property market and the business of China property companies such as Sunac.

Upside:

Stronger-than-expected Chinese economy

Currently, the slowdown in the economic growth in China is affecting housing demand, especially after the sharp increases in property prices in 2013. In our view, any stronger-than-expected performance in the Chinese economy would likely result in stronger housing demand, hence positively affecting Chinese developers' property sales and the business of China property companies such as Sunac.

Company specific risks

Downside:

Rapid expansion could bring execution risks

Sunac has embarked on a rapid expansion of landbank since its IPO in 2010. While Sunac has an experienced management that have operated in the China property market for over 15 years, differences in policy, operating, and financial environments could lead to unforeseeable operational, financial and logistical challenges for Sunac.

Record of aggressive new land acquisitions

To pursue its longer term growth and market share target, the management of Sunac has also been using a higher leverage for the company, leading to rising net gearing for Sunac. At the same time, to generate faster asset turnover to plow back its cashflow for new landbank acquisitions, the project pricing of Sunac has also been pretty competitive, leading to some sacrifices on margins.

Hence we see risks of higher-than-expected leverage and lower-than-expected margins.

Upside:

Potential share buybacks and other related activities

Any potential share buybacks by Sunac or stake increase by the controlling shareholder of Sunac could lead to positive share price momentum on the stock.

Appendix 1

Important Disclosures

Additional information available upon request

Disclosure checklist

Company	Ticker	Recent price*	Disclosure
Sunac	1918.HK	7.09 (HKD) 6 Mar 15	14

*Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg and other vendors . Data is sourced from Deutsche Bank and subject companies.

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Historical recommendations and target price: Sunac (1918.HK)

(as of 3/6/2015)

Previous Recommendations

Strong Buy
Buy
Market Perform
Underperform
Not Rated
Suspended Rating

Current Recommendations

Buy
Hold
Sell
Not Rated
Suspended Rating

*New Recommendation Structure as of September 9,2002

1.	20/05/2013:	Downgrade to Sell, Target Price Change HKD5.25
2.	27/09/2013:	Sell, Target Price Change HKD4.24
3.	27/02/2014:	Upgrade to Buy, Target Price Change HKD5.01
4.	02/04/2014:	Buy, Target Price Change HKD5.57
5.	25/05/2014:	Buy, Target Price Change HKD5.27
6.	26/08/2014:	Downgrade to Hold, Target Price Change HKD6.39
7.	07/11/2014:	Upgrade to Buy, Target Price Change HKD7.48
8.	30/12/2014:	Buy, Target Price Change HKD8.50
9.	08/02/2015:	Downgrade to Hold, Target Price Change HKD7.50

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Buy: Based on a current 12- month view of total share-holder return (TSR = percentage change in share price from current price to projected target price plus pro-jected dividend yield) , we recommend that investors buy the stock.
Sell: Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock
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Notes:

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2. Ratings definitions prior to 27 January, 2007 were:

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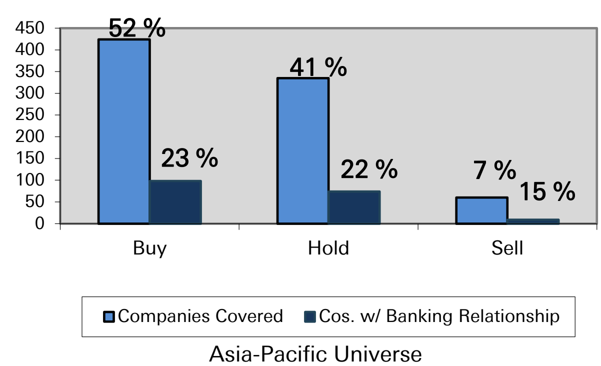
Equity rating dispersion and banking relationships



Regulatory Disclosures

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