

Kerry Properties

Every stock has a price

We believe Kerry's underperformance YTD is unjustified and with the implied discount on its China assets at 100%, we are reiterating our OW with some 32% upside potential to our price target of HK\$33. Fundamentally, nothing major has changed to drive its underperformance YTD. Value is the stock's main attraction.

- **Underperformance unjustified.** Kerry Properties has underperformed the market by about 13% YTD and the stock is trading at 65% discount to its NAV. Notwithstanding the reason of 'no catalyst', we believe Kerry Properties has reached a level that is too cheap to be ignored. *Kerry's share price is implying a 47% discount to its Hong Kong/others assets and its estimated HK\$32.3/shr. for its China assets is given to investors for free.*

- **What's been happening YTD?** Three key developments but none seem to be detrimental enough to drive the share's underperformance this year:

1) **Tianjin Kerry Centre opening** – Tianjin Kerry Centre is scheduled to open in 1H15 with >75% preleased already (vs. 20% at interim stage). The yield on cost of this project is expected to be low at 4-5%. However, the Hangzhou project has just started preleasing this year but we estimate the yield on cost of this to be at about 10-11%;

2) **Hong Kong residential sales** – so far Kerry has only launched 100 units at Dragon Range this year with only about 14-15 units sold. This was right after the further tightening of the LTV by the HKMA. Other than that, we believe another major launch of the Tuen Mun project will be in 4Q this year;

3) **Land purchases** – the company spent HK\$2.4bn and RMB3.9bn on land purchases in Hong Kong and China. In Hong Kong, we estimate the project will generate a margin of about 20% and we estimate the company's gearing will be contained at below 35% in 2015.

- **FY15 Results announcement on Wednesday.** We are expecting core earnings of HK\$4.29bn with HK\$695m one-off disposal gain. This represents a 2.8% YoY decline mainly driven by the full dilution of the Kerry Logistics spin-off. Contracted sales target in 2015 for China probably will remain modest but this should not be a major surprise to investors.

Kerry Properties Limited (Reuters: 0683.HK, Bloomberg: 683 HK)

HK\$ in mn, year-end Dec	FY12A	FY13A	FY14E	FY15E	FY16E
Revenue (HK\$ mn)	34,513	33,158	12,176	9,839	16,236
Net Profit (HK\$ mn)	4,696	4,413	4,291	3,647	3,806
Core Profit (HK\$ mn)	4,705	4,413	3,596	3,647	3,806
EPS (HK\$)	3.26	3.06	2.97	2.53	2.64
Core EPS (HK\$)	3.27	3.06	2.49	2.53	2.64
Core EPS growth (%)	29.7%	(6.4%)	(18.7%)	1.4%	4.4%
DPS (HK\$)	0.95	0.90	0.85	0.85	0.85
ROE	7.0%	6.0%	4.7%	4.6%	4.6%
P/E (Core)	7.6	8.1	9.9	9.8	9.4
P/BV (x)	0.5	0.5	0.5	0.4	0.4
BVPS (HK\$)	49.16	52.45	54.57	56.25	58.03
RNAV/Share	-	-	-	70.83	-
Dividend Yield	3.8%	3.6%	3.4%	3.4%	3.4%

Source: Company data, Bloomberg, J.P. Morgan estimates.

Overweight

0683.HK, 683 HK

Price: HK\$24.75

Price Target: HK\$33.00

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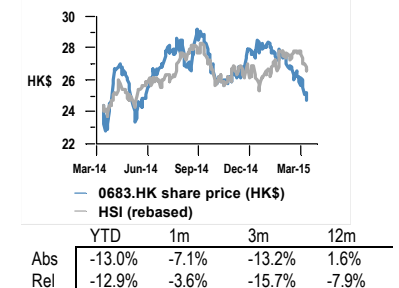
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Price Performance



Company Data	
Shares O/S (mn)	1,444
Market Cap (HK\$ mn)	35,749
Market Cap (\$ mn)	4,601
Price (HK\$)	24.75
Date Of Price	13 Mar 15
Free Float(%)	67.3%
3M - Avg daily vol (mn)	1.83
3M - Avg daily val (HK\$ mn)	49.93
3M - Avg daily val (\$ mn)	6.4
HSI	23,797.96
Exchange Rate	7.77
Price Target End Date	31-Dec-15

See page 8 for analyst certification and important disclosures, including non-US analyst disclosures.

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<p>Key catalysts for the stock price:</p> <ul style="list-style-type: none"> • Good sell-through rates for its development projects • Report of satisfactory performance from its Jing An Kerry Centre • Opening of Tianjin Kerry Centre and other investment properties in China 	<p>Upside risks to our view:</p> <ul style="list-style-type: none"> • Better-than-expected HK residential sales • Better-than-expected China projects delivery • Better-than-expected rental income from China investment properties 	<p>Downside risks to our view & PT:</p> <ul style="list-style-type: none"> • Slower-than-expected residential sales progress • Construction slippage of its mixed-use projects in China • Interest rate hike
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Key financial metrics	FY13A	FY14E	FY15E	FY16E
Revenues (HK\$)	33,158	12,176	9,839	16,236
Revenue growth (%)	-4%	-63%	-19%	65%
EBITDA (HK\$)	6,883	5,470	4,414	5,793
EBITDA margin (%)	21%	45%	45%	36%
Tax rate (%)	26%	18%	17%	20%
Net profit (HK\$)	4,413	4,291	3,647	3,806
EPS (HK\$)	3.06	2.97	2.53	2.64
EPS growth (%)	-6%	-3%	-15%	4%
DPS (HK\$)	0.90	0.85	0.85	0.85
BVPS (HK\$)	52.45	54.57	56.25	58.03
Operating cash flow (HK\$ mn)	(1,525)	1,094	3,858	5,314
Free cash flow (HK\$ mn)	(7,341)	(1,688)	1,112	2,587
Interest cover (X)	25.9	20.0	14.4	16.9
Net margin (%)	13%	35%	37%	23%
Sales/assets (X)	0.24	0.08	0.07	0.11
Debt/equity (%)	38.4%	37.1%	37.9%	39.6%
Net debt/equity (%)	25.8%	27.6%	28.0%	27.8%
ROE (%)	6.0%	4.7%	4.6%	4.6%

Key model assumptions	FY15E
HK residential price chg	0%
HK office rental chg	2-5%
HK retail rental chg	3%
HK office cap rate	5.25%
HK retail cap rate	5.75%
Shanghai office cap rate	7.25-8%
Shanghai retail cap rate	8-8.75%

Source: Company, J.P. Morgan estimates.

Sensitivity analysis	NAV	EPS
Sensitivity to	Dec-15	FY15E
5% chg in HK residential price	1.5%	2.9%
5% chg in China office rent	0.5%	0.2%
50 bps chg in HK cap rate	4.4%	n/a
50 bps chg in China cap rate	4.6%	n/a

Source: J.P. Morgan estimates.

Comparative metrics

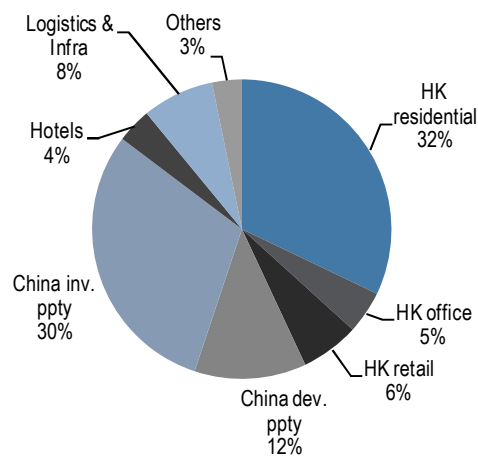
	CMP LC	Mkt Cap HK\$Bn	P/E		NAV discount	P/BV		YTD Stock perf.
			FY14E	FY15E	Dec-15	FY14E	FY15E	
Cheung Kong	150.08	347.62	13.4	11.2	-22%	0.90	0.87	15%
Henderson Land	51.40	154.22	15.7	15.8	-38%	0.68	0.65	-5%
SHKP	115.40	331.42	14.5	14.5	-37%	0.76	0.73	-2%
New World Development	8.85	78.71	9.7	11.7	-56%	0.48	0.48	-1%
Sino Land	11.62	70.46	19.1	12.3	-45%	0.62	0.61	-7%
Kerry Properties	24.75	35.76	8.9	9.5	-65%	0.45	0.44	-12%
Wheelock & Co	37.80	76.80	8.6	6.7	-34%	0.44	0.42	4%
Wharf Holdings	52.50	159.13	13.7	13.1	-44%	0.56	0.55	-6%
Hang Lung Prop	21.75	97.56	9.7	16.1	-38%	0.74	0.72	0%

Source: Bloomberg, Company and J.P. Morgan estimates. Prices are as of 13 March 2015

Valuation and price target basis

Our price target of HK\$33 is based on 52% discount to our Dec-15 NAV, 1 standard deviation below long-term average discount.

NAV breakdown (Dec-15E)



Source: Bloomberg, Company and J.P. Morgan estimates.

JPM vs. consensus, change in estimates

EPS	FY14E	FY15E
JPM old	3.27	2.61
JPM new	2.97	2.53
% chg	-9%	-3%
Consensus	2.72	2.56

Source: Bloomberg, Company and J.P. Morgan estimates.

Table 1: FY14 earnings forecasts

Year ended 31 December	2013A	2014E	YoY%
Net rental income - HK	745	712	-4.4%
Net rental income - China	841	1,667	98.2%
Profit from sales of HK properties	2,836	2,807	-1.0%
Profit from sales of PRC properties	1,647	668	-59.4%
Logistics	2,897	-	NM
Hotel	(12)	133	NM
Gross profit	8,955	5,987	-33.1%
Dividend income	88	90	2.0%
Administrative costs	(2,882)	(1,400)	-51.4%
Others	140	151	8.0%
Operating profits	6,300	4,828	-23.4%
Net interest	(266)	(274)	3.2%
Exceptional item	0	695	NM
Profit before associates	6,035	5,249	-13.0%
Associated profits	571	1,169	104.8%
Profit before taxation	6,605	6,418	-2.8%
Taxation	(1,689)	(1,184)	-29.9%
Profit after taxation	4,917	5,234	6.4%
Minority interests	(504)	(942)	87.2%
Net profit	4,413	4,291	-2.8%

Source: Company data, JPM estimates

Earnings changes

We have revised earnings for Kerry Properties by -9% and 3% for FY14 and FY15-16 respectively as we revised down the delivery of its China property developments. This also caused a moderate decline in estimated NAV of the company to HK\$70.8 from HK\$71.1 previously.

Table 2: Earnings and NAV changes

	FY14E	FY15E	FY16E
Old Earnings (HK\$mn)	4,724	3,765	3,914
New Earnings (HK\$mn)	4,291	3,647	3,806
% change	-9%	-3%	-3%
Old EPS (HK\$)	3.27	2.61	2.71
New EPS (HK\$)	2.97	2.53	2.64
% change	-9%	-3%	-3%
Old DPS (HK\$)	0.85	0.85	0.85
New DPS (HK\$)	0.85	0.85	0.85
% change	0%	0%	0%
Old NAV (HK\$)	71.1		
New NAV (HK\$)	70.8		
% change	0%		

Source: JPM estimates

Table 3: Estimate breakdown of China and Hong Kong/others NAV

HK\$/shr	GAV	Est. net debts	NAV
China property	40.6	-8.3	32.3
Hong Kong and others property	46.9	-8.3	38.6
Group	87.5	-16.7	70.8
Share price	24.75		
Discount to HK/others	-47%		
Implied discount to China	-100%		

Source: JPM estimates

Kerry Properties *(Overweight; Price Target: HK\$33.00)*

Investment Thesis

While China contracted sales remain relatively slow, Kerry has already exceeded its sales target in Hong Kong for FY14. The company has also managed to attain decent yield on cost for its investment property portfolio in China, and we believe the market has not been paying much attention to this. Even though the China property development business remains challenging, as the market has not ascribed any value to this business, we believe this will not derail the re-rating story of Kerry Properties.

Valuation

Our Dec-15 PT of HK\$33 is based on a 53% target discount to NAV, which is 1SD below the long-term average discount to NAV of 36%.

	Dec-15 HK\$MM	HK\$/sh	% of GAV
Hong Kong & Macau properties			
Property under development			
Lux Residential	23,461	16.2	18.6%
Mass Residential	5,802	4.0	4.6%
	29,262	20.3	23.2%
Property investment			
Lux Residential	12,128	8.4	9.6%
Office	6,024	4.2	4.8%
Retail	6,783	4.7	5.4%
Car Park	488	0.3	0.4%
	25,423	17.6	20.1%
Hotel	328	0.2	0.3%
HK Properties total	55,013	38.1	43.5%
China properties			
Property under development			
Residential	15,084	10.4	11.9%
Commercial	470	0.3	0.4%
	15,554	10.8	12.3%
Property investment			
Existing	31,953	22.1	25.3%
Under development	6,534	4.5	5.2%
	38,487	26.6	30.5%
Existing hotel	4,613	3.2	3.7%
China properties total	58,654	40.6	46.4%
Overseas properties total	1,816	1.3	1.4%
Total properties	115,483	80.0	91.4%
Logistics network			
Logistics and distribution	8,520	5.9	6.7%
Total logistics network	8,520	5.9	6.7%
Infrastructure			
Western Harbour Crossing (15%)	511	0.4	0.4%
Total infrastructure	511	0.4	0.4%
Available for sale investments	1,863	1.3	1.4%
Gross Asset Value	126,377	87.5	94.3%
Net Debt	(21,235)	-14.7	
Associated debt	(2,844)	-2.0	
NAV	102,298	70.8	

Source: J.P. Morgan estimates

Risks to Rating and Price Target

Downside risks to our OW rating and price target include worse-than-expected Hong Kong and China residential sales, worse-than-expected China project delivery, lower-than-expected yield from new investment properties in China and interest rate hikes.

Kerry Properties: Summary of Financials

Income Statement					Cash flow statement				
HK\$ in millions, year end Dec	FY13	FY14E	FY15E	FY16E	HK\$ in millions, year end Dec	FY13	FY14E	FY15E	FY16E
Revenues	33,158	12,176	9,839	16,236	EBIT	6,300	4,828	3,709	5,017
% change Y/Y	(3.9%)	(63.3%)	(19.2%)	65.0%	Depr. & amortization	583	641	706	776
EBIT	6,300	4,828	3,709	5,017	Change in working capital	(7,552)	(3,191)	325	847
% change Y/Y	(5.3%)	(23.4%)	(23.2%)	35.3%	Others	(1,125)	(2,182)	(1,896)	(1,669)
EBIT Margin	19.0%	39.7%	37.7%	30.9%	Cash flow from operations	(1,525)	1,094	3,858	5,314
Net Interest	(266)	(274)	(308)	(343)	Capex	(6,178)	(3,000)	(3,000)	(3,000)
Earnings before tax	6,605	6,418	5,165	5,968	Disposal/(purchase)	-	-	-	-
% change Y/Y	(2.5%)	(2.8%)	(19.5%)	15.6%	Net Interest	(1,001)	(1,060)	(1,145)	(1,236)
Tax	(1,689)	(1,184)	(884)	(1,215)	Free cash flow	(7,341)	(1,688)	1,112	2,587
as % of EBT	25.6%	18.5%	17.1%	20.4%	Equity raised/(repaid)	102	0	0	0
Net income (reported)	4,413	4,291	3,647	3,806	Debt raised/(repaid)	1,000	1,000	1,000	0
% change Y/Y	(6.0%)	(2.8%)	(15.0%)	4.4%	Other	5,363	0	0	1,000
Core net profit	4,413	3,596	3,647	3,806	Dividends paid	(1,832)	(1,228)	(1,228)	(1,228)
% change Y/Y	(6.2%)	(18.5%)	1.4%	4.4%	Beginning cash	14,155	11,072	8,939	9,569
Shares outstanding	1,444	1,444	1,444	1,444	Ending cash	11,072	8,939	9,569	11,655
EPS (reported) (HK\$)	3.06	2.97	2.53	2.64	DPS (HK\$)	0.90	0.85	0.85	0.85
% change Y/Y	(6.2%)	(3.0%)	(15.0%)	4.4%					
Core EPS (HK\$)	3.06	2.49	2.53	2.64					
% change Y/Y	(6.4%)	(18.7%)	1.4%	4.4%					
Balance sheet					Ratio Analysis				
HK\$ in millions, year end Dec	FY13	FY14E	FY15E	FY16E	%, year end Dec	FY13	FY14E	FY15E	FY16E
Cash and cash equivalents	11,494	8,939	9,569	11,655	EBIT margin	19.0%	39.7%	37.7%	30.9%
Accounts receivable	2,669	5,860	5,535	4,688	Net margin	13.3%	29.5%	37.1%	23.4%
Inventories	4,000	4,000	4,000	4,000	SG&A/Sales	-	-	-	-
Others	6,973	5,665	5,665	5,665	Sales per share growth	(4.1%)	(63.4%)	(19.2%)	65.0%
Current assets	25,319	24,647	24,952	26,192	Sales growth	(3.9%)	(63.3%)	(19.2%)	65.0%
LT investments	20,438	20,438	20,438	20,438	Net profit growth	(6.2%)	(18.5%)	1.4%	4.4%
Net fixed assets	96,632	100,316	104,134	108,092	EPS growth	(6.4%)	(18.7%)	1.4%	4.4%
Total Assets	142,389	145,401	149,523	154,722	Interest coverage (x)	25.9	20.0	14.4	16.9
Liabilities					Net debt to total capital	20.5%	21.6%	21.9%	21.8%
ST loans	3,965	3,965	3,965	3,965	Net debt to equity	25.8%	27.6%	28.0%	27.8%
Payables	7,765	7,765	7,765	7,765	Sales/assets	0.2	0.1	0.1	0.1
Others	2,871	2,871	2,871	2,871	Assets/equity	1.9	1.9	1.8	1.8
Total current liabilities	14,601	14,601	14,601	14,601	ROE	6.0%	4.7%	4.6%	4.6%
Long-term debt	31,011	30,957	32,659	35,279	ROCE	4.4%	3.4%	2.7%	3.3%
Other liabilities	5,630	5,630	5,630	5,630					
Total Liabilities	51,242	51,188	52,890	55,510					
Shareholder's equity	75,755	78,821	81,241	83,819					
BVPS	52.45	54.57	56.25	58.03					

Source: Company reports and J.P. Morgan estimates.

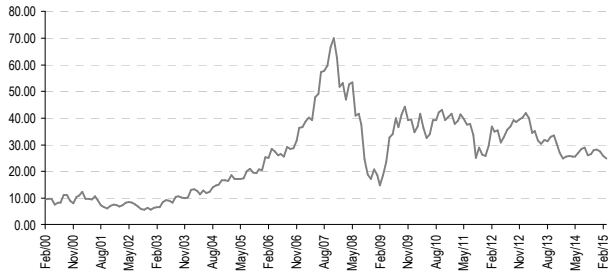
JPM Q-Profile

Kerry Properties Limited (HONG KONG / Financials)

As Of: 13-Mar-2015

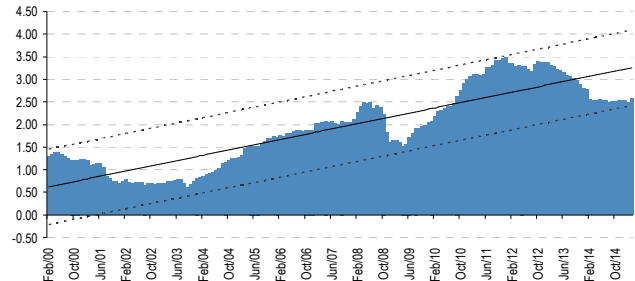
Local Share Price

Current: **24.95**



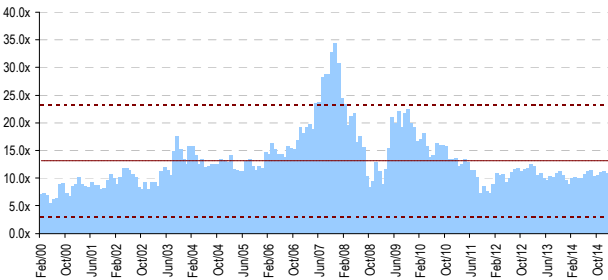
12 Mth Forward EPS

Current: **2.58**



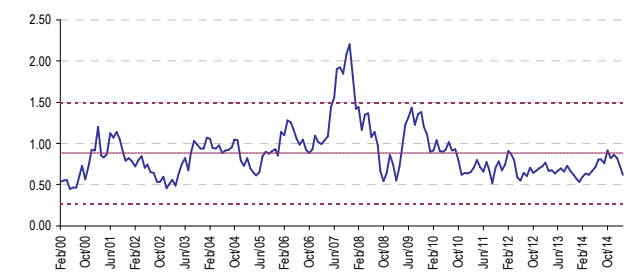
PE (1Yr Forward)

Current: **9.7x**



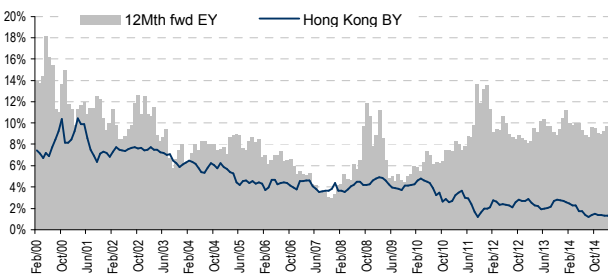
P/E Relative to Hong Kong Index

Current: **0.62**



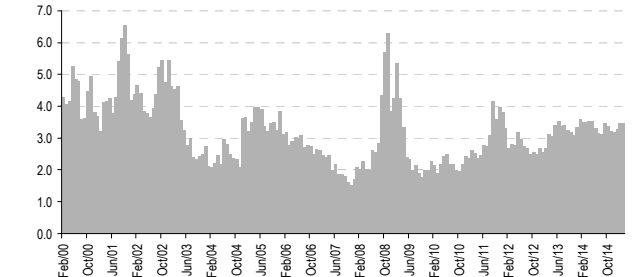
Earnings Yield (& Local Bond Yield)

Current: **10%**



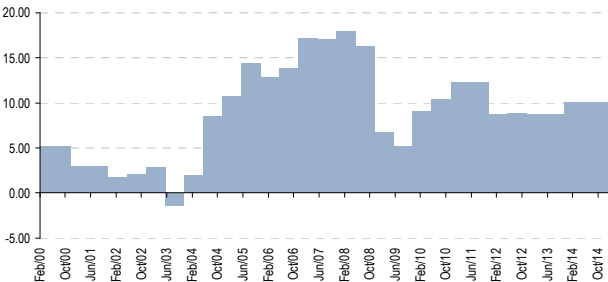
Dividend Yield (Trailing)

Current: **3.47**



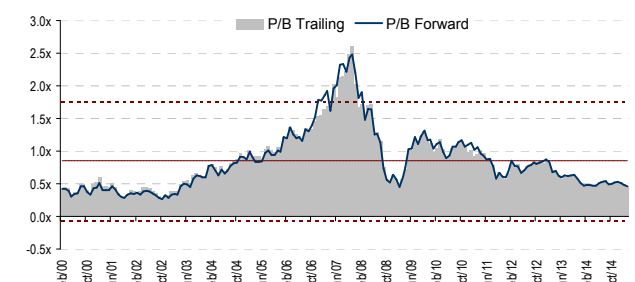
ROE (Trailing)

Current: **10.07**



Price/Book (Value)

Current: **0.5x**



Summary

Kerry Properties Limited		TICKER		683 HK		As Of:		13-Mar-15			
HONG KONG						Local Price:		24.95			
Financials						EPS:		2.58			
	Latest	Min	Max	Median	Average	2 S.D.+	2 S.D. -	% to Min	% to Max	% to Med	% to Avg
12mth Forward PE	9.68x	5.51	34.37	11.68	13.17	23.33	3.00	-43%	255%	21%	36%
P/BV (Trailing)	0.47	0.29	2.61	0.76	0.85	1.76	-0.05	-39%	451%	61%	80%
Dividend Yield (Trailing)	3.47x	1.54	6.56	3.12	3.22	5.22	1.21	-56%	89%	-10%	-7%
ROE (Trailing)	10.07	-1.36	17.90	8.84	8.86	18.99	-1.27	-114%	78%	-12%	-12%

Source: Bloomberg, Reuters Global Fundamentals, IBES CONSENSUS, JPMorgan Quantitative & Derivative Strategy

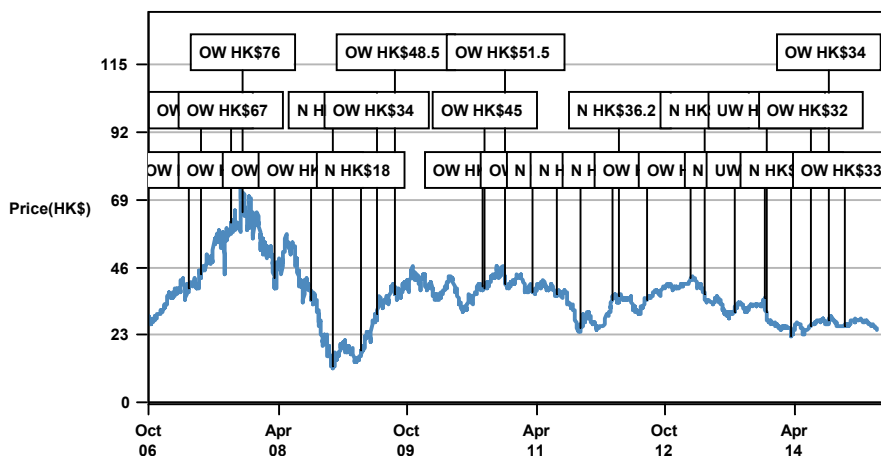
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- **Client:** J.P. Morgan currently has, or had within the past 12 months, the following company(ies) as clients: Kerry Properties.

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Kerry Properties (0683.HK, 683 HK) Price Chart



Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.
Initiated coverage Mar 23, 2007.

Date	Rating	Share Price (HK\$)	Price Target (HK\$)
23-Mar-07	OW	39.20	45.00
09-May-07	OW	43.50	50.00
16-Sep-07	OW	61.25	65.00
17-Sep-07	OW	61.25	67.00
07-Nov-07	OW	64.65	76.00
20-Mar-08	OW	41.95	50.00
20-Aug-08	OW	35.05	40.00
17-Nov-08	N	12.30	15.00
19-Mar-09	N	17.60	18.00
26-May-09	OW	30.10	34.00
12-Aug-09	OW	37.00	48.50
16-Aug-10	OW	39.30	43.50
27-Aug-10	OW	38.85	45.00
21-Nov-10	OW	40.50	51.50
18-Mar-11	OW	37.55	51.00
26-Jun-11	N	36.65	35.60
07-Oct-11	N	25.10	25.30
16-Feb-12	N	34.90	37.30
15-Mar-12	N	36.10	36.20
09-Jul-12	OW	34.60	41.00
17-Jan-13	OW	42.50	42.00
15-Mar-13	N	36.70	35.00
22-Jul-13	N	30.95	34.50
26-Nov-13	UW	35.50	31.50
02-Dec-13	UW	30.70	29.80
17-Mar-14	N	22.75	26.40
04-Jun-14	OW	25.80	32.00
21-Aug-14	OW	27.85	34.00
30-Oct-14	OW	25.85	33.00

The chart(s) show J.P. Morgan's continuing coverage of the stocks; the current analysts may or may not have covered it over the entire period.

J.P. Morgan ratings or designations: OW = Overweight, N= Neutral, UW = Underweight, NR = Not Rated

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	Overweight (buy)	Neutral (hold)	Underweight (sell)
J.P. Morgan Global Equity Research Coverage	45%	43%	12%
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*Percentage of investment banking clients in each rating category.

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