



Guangzhou R&F (2777 HK)

Underperform (downgraded)

Target price: HK\$7.00



Dennis Yao

SFC CE No. ALK994

dennisyao@gfgroup.com.hk

+852 3719 1065

GF Securities (Hong Kong) Brokerage Limited
29-30/F, Li Po Chun Chambers
189 Des Voeux Road Central
Hong Kong

Lower-than-expected 2014 earnings; downgrade to Underperform

2014 results review 2014 revenue fell 4% YoY to Rmb34.7bn; gross margin decreased by 370bps YoY to 35.5%; other gains came in at Rmb1.9bn (mostly revaluation gains on investment properties). Excluding other gains, its core operating profit fell 22% YoY to Rmb9.3bn. Income tax for the year fell 30% YoY to Rmb3.65bn due to the decrease in land appreciation tax (LAT). Excluding profit to holders of perpetual capital instruments of Rmb1.3bn, 2014 net profit declined 32% YoY to Rmb5.2bn, worse than market consensus.

Contract sales review The company achieved contract sales of Rmb54bn, up 29% YoY; Guangzhou and Beijing accounted for 26% and 23% of total contract sales respectively. GFA sold rose 20% YoY to 4.05m sqm. Management is targeting contract sales growth of 10% YoY in 2015 to Rmb60bn, and has restated its focus on first and second-tier cities. It will also focus on first-tier cities for future land acquisitions.

66 projects under development As of end-2014, the company had saleable area of 10.4m sqm across 66 projects, with an available presales value of Rmb110bn.

2014 LAT provision below a normal level According to our calculations, LAT in 2014 was equal to just 4% of property development revenue, compared with 7% in 2013. Given the company had a gross margin of over 35% in 2014, we believe its LAT should represent 5-7% of property development revenue to bring it in line with the industry standard.

High gearing a long-term headwind; downgrade to Underperform We calculate the company had net gearing of 104% in 2014, and gross interest expenses of Rmb5.8bn. We believe its interest coverage ratio (operating profit/gross interest expense) is just 1.9x, with certain liquidity risks. Given its high gearing, declining gross margin and low earnings visibility, we downgrade our rating from Hold to Underperform, and cut our target price by 20% from HK\$8.70 to HK\$7.00, equal to 0.5x 2014 NBV.

Risks the company has sizable land bank in Tier 1 cities, rising ASP in those cities may lead to better-than-expected net earnings for the company in 2015.

Stock performance



Source: Bloomberg

Key data

Mar 17 close (HK\$)	8.05
Shares in issue (bn)	3,201.0
Major shareholder	Li Sze Lim (33.7%)
Market cap (HK\$ bn)	25,768.1
3M avg. vol. (m)	7.9
52w high/low (HK\$)	11.92/7.65

Source: Bloomberg

Valuation

	Turnover (Rmb m)	Net Profit (Rmb m)	EPS (Rmb)	EPS YoY (%)	P/E (x)	NBV (Rmb)	P/B (x)	ROE (%)
2012	30,365	5,502	1.722	14	3.7	8.3	0.8	20.8
2013	36,271	7,634	2.390	39	2.7	10.4	0.6	23.1
2014	34,705	5,221	1.632	(32)	3.9	12.0	0.5	13.6
2015E	48,181	5,907	1.853	14	3.5	13.8	0.5	13.4
2016E	55,708	6,455	2.017	9	3.2	15.9	0.4	12.7

Sources: Company data, Capital IQ

Rating definitions

Benchmark: Hong Kong Hang Seng Index
Time horizon: 12 months

Company ratings

Buy	Stock expected to outperform benchmark by more than 15%
Accumulate	Stock expected to outperform benchmark by more than 5% but not more than 15%
Hold	Expected stock relative performance ranges between -5% and 5%
Underperform	Stock expected to underperform benchmark by more than 5%

Sector ratings

Positive	Sector expected to outperform benchmark by more than 10%
Neutral	Expected sector relative performance ranges between -10% and 10%
Cautious	Sector expected to underperform benchmark by more than 10%

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29-30/F, Li Po Chun Chambers, 189 Des Voeux Road Central, Hong Kong
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