

EARNINGS REVIEW

Kerry Properties (0683.HK)

Buy

Equity Research

Above expectations: Stable result despite smaller stake in logistics

What surprised us

Despite a decrease in its stake in Kerry Logistics Network (spun-off in Dec 2013), Kerry Properties managed to deliver a stable result in 2014, with underlying profit falling by a mere 0.7% yoy to HK\$4,384mn (HK\$3.04/share). The result is 5.6% above our estimate, with China rental income coming in better than our forecast. Gross rental profit was up 57% yoy to HK\$2,484bn, thanks to a 117% jump in China contribution on higher occupancy. Development income fell 18% yoy to HK\$3,659bn, dragged by a 54% drop in China sales while HK sales remained stable. Reversing a cut in 1H DPS, the board raised 2H DPS by HK\$0.05 to HK\$0.60, keeping the full year DPS unchanged at HK\$0.90. Following the results, we have raised our FY15-FY17 EPS estimates by 2.8%-3.3%.

What to do with the stock

Same as last year, Kerry's HK contracted sales (HK\$11.1bn) exceeded its target (HK\$6.5bn) but China sales (HK\$3.6bn) were behind plan (HK\$5.5bn). The shortfall in China sales was covered by a significant jump in China rental income, which helps build a solid earnings foundation for the group, in our view. With more projects in tier-2 cities (vs. a higher proportion of 3-tier city projects in 2014) ready for sale, management is confident of accelerating China sales in 2015. It is worth noting that, at the analyst briefing, the company CEO noted his awareness of investor demand for a higher dividend payout and stressed he will consider this in the future. Retain Buy rating and 12-month NAV-based TP of HK\$32.50 (set at 40% discount to NAV). **Key risk:** abrupt economic downturn.

Kerry Prop. FY14 Results Summary

(HK\$mn)	FY13 (restated)	FY14	YoY chg	1H FY14	2H FY14	HoH chg
Underlying profit	4,413	4,384	-0.7%	1,804	2,580	43.0%
Underlying EPS, basic (HK\$)	3.06	3.04	-0.9%	1.25	1.79	43.0%
DPS (HK\$)	0.90	0.90	0.0%	0.30	0.60	NM
Segment Results						
- Property sales	4,483	3,659	-18.4%	2,034	1,625	-20.1%
- Property rental	1,586	2,484	56.6%	1,152	1,332	15.7%
- Hotel	(12)	65	NM	49	16	-67.7%
Book value (HK\$/shr)	52.45	55.43	5.7%	52.63	55.43	5.3%

Source: Company data

INVESTMENT LIST MEMBERSHIP

Asia Pacific Buy List

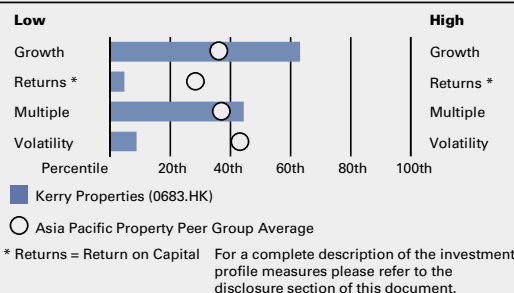
Coverage View: Attractive

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Investment Profile

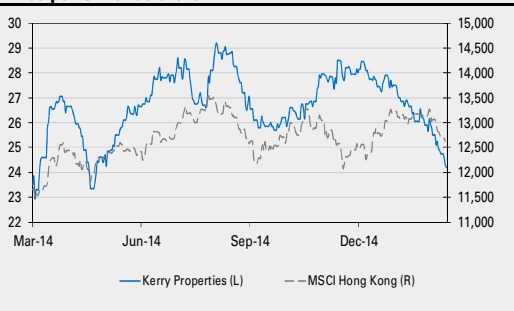


Key data

	Current
Price (HK\$)	24.20
12 month price target (HK\$)	32.50
Market cap (HK\$ mn / US\$ mn)	34,551.1 / 4,450.5
Foreign ownership (%)	--

	12/13	12/14E	12/15E	12/16E
EPS (HK\$) New	6.13	4.69	2.60	2.70
EPS revision (%)	(32.9)	63.2	2.8	3.3
EPS growth (%)	26.7	(23.5)	(44.5)	3.6
EPS (dil) (HK\$) New	6.12	4.68	2.60	2.69
P/E (X)	4.9	5.2	9.3	9.0
P/B (X)	0.6	0.4	0.4	0.4
EV/EBITDA (X)	31.7	12.9	19.1	15.4
Dividend yield (%)	3.0	3.7	3.7	3.7
ROE (%)	12.1	8.7	4.6	4.6

Price performance chart



Share price performance (%)	3 month	6 month	12 month
Absolute	(12.6)	(12.3)	3.0
Rel. to MSCI Hong Kong	(16.5)	(10.7)	(5.1)

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 3/18/2015 close.

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Kerry Properties: Summary Financials

Profit model (HK\$ mn)	12/13	12/14E	12/15E	12/16E	Balance sheet (HK\$ mn)	12/13	12/14E	12/15E	12/16E
Total revenue	33,158.0	14,663.7	11,654.5	14,659.4	Cash & equivalents	11,480.1	11,322.4	12,058.0	8,570.8
Cost of goods sold	(6,781.4)	(6,614.9)	(5,818.2)	(7,766.4)	Accounts receivable	2,669.5	3,680.7	0.0	0.0
SG&A	(21,746.7)	(1,840.9)	(1,791.2)	(1,841.3)	Inventory	10,538.9	11,613.0	14,490.1	13,172.1
R&D	--	--	--	--	Other current assets	630.7	563.7	563.7	563.7
Other operating profit/(expense)	(2,096.4)	(709.1)	106.8	106.3	Total current assets	25,319.2	27,179.7	27,111.8	22,306.5
EBITDA	2,533.5	5,498.9	4,151.8	5,158.1	Net PP&E	96,143.4	96,428.4	103,215.7	105,844.2
Depreciation & amortization	(583.1)	(364.3)	(367.9)	(371.6)	Net intangibles	122.5	122.5	122.5	122.5
EBIT	1,950.4	5,134.6	3,783.9	4,786.5	Total investments	20,437.7	21,354.7	21,683.4	21,862.2
Interest income	326.3	323.2	331.4	292.4	Other long-term assets	366.5	347.0	347.0	347.0
Interest expense	(591.8)	(626.9)	(608.3)	(689.4)	Total assets	142,389.4	145,432.3	152,480.4	150,482.3
Income/(loss) from uncons. subs.	791.7	1,302.9	1,862.1	1,012.4	Accounts payable	7,764.6	7,527.3	3,272.2	1,846.3
Others	11,978.0	3,400.2	0.0	0.0	Short-term loans	3,965.1	3,091.6	11,283.3	855.6
Pretax profits	14,454.6	9,534.1	5,369.2	5,401.9	Other current liabilities	2,871.1	1,844.3	1,844.3	1,844.3
Income tax	(3,250.9)	(1,698.3)	(957.3)	(963.2)	Total current liabilities	14,600.7	12,463.1	16,399.7	4,546.2
Minorities	(2,374.0)	(1,062.1)	(651.8)	(544.7)	Long-term debt	31,010.6	31,147.0	31,147.0	37,863.8
Net income pre-preferred dividends	8,829.7	6,773.6	3,760.0	3,894.0	Other long-term liabilities	7,902.6	8,407.8	8,407.8	8,407.8
Preferred dividends	0.0	0.0	0.0	0.0	Total long-term liabilities	38,913.2	39,554.8	39,554.8	46,271.6
Net income (pre-exceptionals)	8,829.7	6,773.6	3,760.0	3,894.0	Total liabilities	53,513.9	52,018.0	55,954.5	50,817.8
Post-tax exceptionals	0.0	0.0	0.0	0.0	Preferred shares	0.0	0.0	0.0	0.0
Net income	8,829.7	6,773.6	3,760.0	3,894.0	Total common equity	75,755.2	80,078.5	82,538.3	85,132.1
EPS (basic, pre-except) (HK\$)	6.13	4.69	2.60	2.70	Minority interest	13,120.2	13,335.8	13,987.6	14,532.4
EPS (basic, post-except) (HK\$)	6.13	4.69	2.60	2.70	Total liabilities & equity	142,389.4	145,432.3	152,480.4	150,482.3
EPS (diluted, post-except) (HK\$)	6.12	4.68	2.60	2.69	BVPS (HK\$)	52.45	55.43	57.13	58.93
DPS (HK\$)	0.90	0.90	0.90	0.90	RNAV (HK\$ mn)	87,431.7	79,086.9	80,745.9	--
Dividend payout ratio (%)	14.7	19.2	34.6	33.4	RNAVPS (HK\$)	58.82	53.03	54.18	--
Free cash flow yield (%)	(14.7)	4.9	(1.1)	7.5					
Growth & margins (%)	12/13	12/14E	12/15E	12/16E	Ratios	12/13	12/14E	12/15E	12/16E
Sales growth	(3.9)	(55.8)	(20.5)	25.8	ROE (%)	12.1	8.7	4.6	4.6
EBITDA growth	(64.0)	117.0	(24.5)	24.2	ROA (%)	6.3	4.7	2.5	2.6
EBIT growth	(70.5)	163.3	(26.3)	26.5	ROACE (%)	10.6	7.1	3.8	3.7
Net income growth	26.9	(23.3)	(44.5)	3.6	Inventory days	567.2	611.2	818.8	650.0
EPS growth	26.7	(23.5)	(44.5)	3.6	Receivables days	59.1	79.0	57.6	--
Gross margin	79.5	54.9	50.1	47.0	Payable days	514.4	421.9	338.7	120.3
EBITDA margin	7.6	37.5	35.6	35.2	Net debt/equity (%)	26.4	24.5	31.5	30.3
EBIT margin	5.9	35.0	32.5	32.7	Interest cover - EBIT (X)	7.3	16.9	13.7	12.1
Cash flow statement (HK\$ mn)	12/13	12/14E	12/15E	12/16E	Valuation	12/13	12/14E	12/15E	12/16E
Net income pre-preferred dividends	8,829.7	6,773.6	3,760.0	3,894.0	P/E basic (X)	4.9	5.2	9.3	9.0
D&A add-back	583.1	364.3	367.9	371.6	P/B (X)	0.6	0.4	0.4	0.4
Minorities interests add-back	2,374.0	1,062.1	651.8	544.7	EV/EBITDA (X)	31.7	12.9	19.1	15.4
Net (inc)/dec working capital	(6,505.6)	(2,322.5)	(3,451.6)	(107.7)	Dividend yield (%)	3.0	3.7	3.7	3.7
Other operating cash flow	(3,041.5)	(1,142.9)	(1,862.1)	(1,012.4)					
Cash flow from operations	(2,177.0)	2,344.9	(534.0)	3,690.2	Underlying valuation	12/13	12/14E	12/15E	12/16E
Capital expenditures	(6,177.6)	0.0	0.0	0.0	Underlying profit (HK\$ mn)	4,413.0	4,384.0	3,760.0	3,894.0
Acquisitions	(3,840.4)	(649.3)	(7,155.2)	(3,000.0)	Underlying EPS (HK\$)	3.06	3.04	2.60	2.70
Divestitures	0.0	0.0	0.0	0.0	Underlying ROE (%)	6.0	5.6	4.6	4.6
Others	4,727.5	1,072.9	1,533.4	833.7	Underlying ROA (%)	3.2	3.0	2.5	2.6
Cash flow from investments	(5,290.5)	423.6	(5,621.9)	(2,166.3)	Underlying ROACE (%)	6.5	5.0	3.8	3.7
Dividends paid (common & pref)	(1,296.3)	(1,227.7)	(1,300.2)	(1,300.2)	Underlying P/E (X)	9.9	8.0	9.3	9.0
Inc/(dec) in debt	6,320.4	(1,810.7)	8,191.7	(3,710.9)	Underlying dividend payout (%)	29.4	29.7	34.6	33.4
Common stock issuance (repurchase)	102.2	0.0	0.0	0.0	Underlying EPS growth (%)	(6.2)	(0.9)	(14.2)	3.6
Other financing cash flows	(886.7)	(10,802.5)	0.0	0.0					
Cash flow from financing	4,239.5	(13,840.9)	6,891.5	(5,011.1)					
Total cash flow	(3,228.0)	(11,072.5)	735.6	(3,487.2)					

Note: Last actual year may include reported and estimated data.
Source: Company data, Goldman Sachs Research estimates.

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Exhibit 1: Kerry Properties FY14 Results Review

(HK\$ mn)	FY13 (restated)	FY14	YoY chg	1H FY14	2H FY14	HoH chg	Remarks (FY14)
Property sale	11,265	10,274	-8.8%	4,140	6,134	48.2%	
Hong Kong	7,194	7,132	-0.9%	3,437	3,695	7.5%	Contributed by sales of The Summa, 3 Ede Rd., 8 LaSalle, The Altitude and Lions Rise
China	4,071	3,142	-22.8%	703	2,439	246.8%	Contributed by Arcadia Court and Enterprise Square, Parkview Residence Ph.2, the Metropolis-Arcadia Court Ph.1, and Changsha Xiangjiang Arcadia Court
Property rental	2,147	3,169	47.6%	1,474	1,695	15.0%	
Hong Kong	936	875	-6.5%	437	438	0.2%	
China	1,211	2,293	89.3%	1,037	1,257	21.2%	
Hotel	558	1,221	119.0%	560	662	18.2%	Mainly driven by Shanghai Jing An Shangri-La Hotel and Shenyang Shangri-La Hotel
Total revenue	13,970	14,664	5.0%	6,174	8,490	37.5%	
Property sale	4,483	3,659	-18.4%	2,034	1,625	-20.1%	
Hong Kong	2,836	2,900	2.2%	1,782	1,118	-37.2%	
China	1,647	759	-53.9%	252	507	101.1%	
Property rental	1,586	2,484	56.6%	1,152	1,332	15.7%	
Hong Kong	745	663	-11.0%	337	326	-3.2%	Margin at 76% (vs. 80% in 2013); Occupancy at 95%-97%.
China	841	1,821	116.6%	815	1,006	23.5%	Margin at 79% (vs. 69% in 2013); Occupancy at 79%-98%.
Hotel	(12)	65	NM	49	16	-67.7%	
Segmental gross profit	6,057	6,208	2.5%	3,234	2,974	-8.1%	
Other income and net gains	496	1,375	177.0%	171	1,204	604.7%	
Admin and other operating expense	(1,334)	(1,236)	-7.3%	(601)	(635)	5.7%	
Change in fair value of inv. prop.	7,028	2,511	-64.3%	826	1,685	104.1%	
Finance costs	(503)	(627)	24.7%	(310)	(316)	1.9%	Net gearing was 28.5% at end-14 (vs. 31.9% at Jun-14).
Operating profit	11,745	8,231	-29.9%	3,320	4,911	47.9%	
Associates	665	1,303	95.9%	566	737	30.1%	
Profit before tax	12,409	9,534	-23.2%	3,886	5,648	45.3%	
Taxation	(2,957)	(1,698)	-42.6%	(885)	(813)	-8.1%	
Minorities	(2,075)	(1,062)	-48.8%	(611)	(451)	-26.2%	
Net profit attrib to shareholders from cont'd operations	7,377	6,774	-8.2%	2,390	4,384	83.4%	
Profit from discontinued operations (net of MI)	5,778	-	n.a.	-	-	n.a.	Kerry Logistics spun off in Dec 2013, it then became an associate of Kerry Prop.
Net profit attrib to shareholders	13,154	6,774	-48.5%	2,390	4,384	83.4%	Decrease due to a smaller increase in fair value of investment properties and a higher base in 2013 with Kerry Logistics spin-off gain of HK\$4,325m
Adj. for gain from Kerry Logistics Spin-off	(4,325)	-	n.a.	-	-	n.a.	
Net effects of HKAS 40 & HK(SIC) Int 21	(4,416)	(2,390)	n.a.	(586)	(1,804)	n.a.	
Underlying profit	4,413	4,384	-0.7%	1,804	2,580	43.0%	
EPS (HK\$)	9.13	4.69	-48.6%	1.65	3.04	84.2%	
EPS - fd (HK\$)	9.12	4.69	-48.6%	1.65	3.04	84.1%	
Underlying EPS (HK\$)	3.06	3.04	-0.9%	1.25	1.79	43.0%	
DPS (HK\$)	0.90	0.90	0.0%	0.30	0.60	NM	Implied payout ratio of 30% (vs. 29% in FY13)
Investment Property Valuation	53,671	55,519	3.4%	53,839	55,519	3.1%	
Reported book per share (HK\$/shr)	52.45	55.43	5.7%	52.63	55.43	5.3%	

Source: Company data, Goldman Sachs Global Investment Research

Exhibit 2: Kerry Properties FY14 Results Highlights

- FY14 underlying profit fell 0.7% yoy to HK\$4,384 mn (HK\$3.04/share), mainly due to less contribution from Kerry Logistics after its spin-off in Dec-13
- Gross profit from HK property sales was up 2.2% yoy to HK\$2,900mn, largely derived from sales of The Summa, 3 Ede Rd., 8 LaSalle, The Altitude and Lions Rise
- Gross profit from China property sales fell 53.9% yoy to HK\$759mn; main contributors include Arcadia Court and Enterprise Square in Shenyang, Parkview Residence Ph.2 in Hangzhou, the Metropolis-Arcadia Court Ph.1 in Chengdu, and Changsha Xiangjiang Arcadia Court.
- Rental revenue from China up 89.3% yoy to HK\$2,293mn. Major contributors include Shanghai Jing An Kerry Center Ph.1 (HK\$200mn) and Ph.2 (HK\$830mn), Shenzhen Kerry Plaza I & II (HK\$500mn), and Beijing Kerry Center (HK\$450mn).
- Profit from rental was up 56.6% yoy or 15.7% hoh to HK\$2,484mn with China up 116.6% yoy or 23.5% hoh to HK\$1,821mn.
- Hotel profit rose to HK\$65mn from a HK\$12mn loss in 2013, mainly driven by Shanghai Jing An Shangri-La Hotel and Shenyang Shangri-La Hotel
- Set 2015 contracted sales target at HK\$12bn, with HK and China accounting for HK\$6bn each
- Up to mid-March, the company has achieved contracted sales of HK\$2bn, HK\$1bn from HK and HK\$1bn from China
- On HK property sales, management plans to launch So Kwun Wat project in Tuen Mun and continue to sell the remaining units at 3 Ede road, 8 LaSalle and Dragons Range in 2015
- On China property sales, management plans to launch residential developments in Zhijiang, Hangzhou and Bai Xia District of Nanjing, as well as the office units of Shanghai Kerry Everbright City Ph.3 in 2015
- Net gearing ratio fell to 28.5% as at Dec-14 from 31.9% as at Jun-14
- Investment property portfolio valuation was up 3.4% yoy or 3.1% hoh to HK\$55,519mn. The increase was mainly attributable to Jing An Kerry Center Ph. II
- BVPS at HK\$55.43, up 5.7% yoy or up 5.3% hoh.

Source: Company data, Goldman Sachs Global Investment Research

Disclosure Appendix

Reg AC

We, Anthony Wu, Justin Kwok, CFA and Claire Cheng, hereby certify that all of the views expressed in this report accurately reflect our personal views about the subject company or companies and its or their securities. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

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Disclosures

Coverage group(s) of stocks by primary analyst(s)

Anthony Wu: Hong Kong Property. Justin Kwok, CFA: Asia Pacific Conglomerates, Hong Kong Property.

Asia Pacific Conglomerates: Beijing Enterprises Holdings, Cheung Kong Holdings, Cheung Kong Infrastructure, China Gas Holdings, China Merchants Holdings, China Resources Gas Group, China Suntien Green Energy, CITIC Ltd., COSCO Pacific, Dalian Port Co., ENN Energy Holdings, Fosun International, Galaxy Entertainment Group, Hopewell Holdings, Hutchison Port Holdings Trust, Hutchison Whampoa, Jardine Matheson, Kunlun Energy Co., Melco Crown Entertainment, Melco Crown Entertainment Ltd., Melco International Development, MGM China, MTR Corp., NWS Holdings, Sands China, Shanghai Industrial, Shanghai International Port, Shun Tak Holdings, Sinopec Kantons, SJM Holdings, Summit Ascent Holdings Ltd., Swire Pacific (A), Tianhe Chemicals Group Limited, Tianjin Development Holdings, Tianjin Port Development Holdings, Towngas China, Wharf Holdings, Wheelock and Co., Wynn Macau, Yingde Gases Group.

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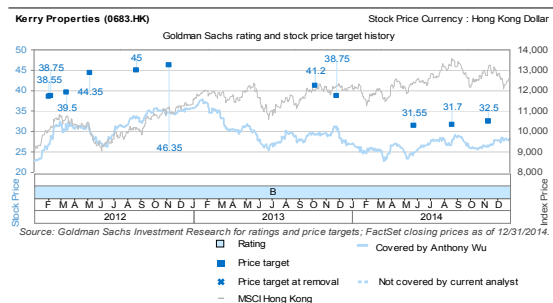
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