

JPM-pp1

Asia Pacific Equity Research

24 March 2015

China Overseas Land & Investment (688 HK)

Neutral

Price: HK\$22.90

23 Mar 2015

Price Target: HK\$24.50

PT End Date: 31 Dec 2015

Injection looks positive initially; c.HK\$1 accretion

COLI announced that it will buy a property portfolio from CSCEC, which was first mentioned back in August 2013, at Rmb33.8 bn. This will be settled with equity in full, to be issued at HK\$25.38 per share. This represents a 21% dilution from the existing share base, or 17% dilution from enlarged share base. The portfolio is similar to market expectation, with a mix of wanted and unwanted assets. Based on a rough calculation, the consideration should be slightly NAV accretive, and as COLI's share trades at a narrower discount to its peers, we think the deal should be overall NAV accretive, and could be positive to the share price in the near-term.

JPM View

- The portfolio included investment properties in Shanghai and Beijing, and mostly residential developments in nine other cities plus some landbank in London. A rough calculation suggests that the portfolio may be worth about Rmb41 bn, generating at least Rmb7 bn NAV accretion (~HK\$1 per share).
- After the injection and share placement, the pro-forma net gearing will go down from current 32% to 23%, on total equity basis. This is to prepare COLI for the bigger upcoming land premium payment post aggressive landbanking in 2H2014, in our view.
- As mentioned in our earlier notes, we think COLI's share price has become more attractive after recent underperformance. With the injection overhang removed, we expect to see slight near-term strength in the share price.

More details post analyst briefing at 4:00 pm today, 5/F Island Shangri-La.

COLI's balance sheet proforma analysis

Assets to be acquired	HK\$ mn
Total assets	42,806
Shareholders' loan	40,497
Total equity	2,309
Total liabilities and equity	42,806

COLI (Dec-2014)	HK\$ mn
Cash	51,215
Other assets	299,722
Total assets	350,937

Debt	94,532
Other liabilities	119,597

Total equity	136,808
Total liabilities and equity	350,937

Net gearing	32%
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COLI (proforma after asset injection)	HK\$ mn
Cash	51,215
Other assets	342,528
Total assets	393,743

Debt	94,532
Shareholders' loan	40,497
Other liabilities	119,597
Total equity	139,116
Total liabilities and equity	393,743

Net gearing	60%
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COLI (proforma after asset injection and share placement)	HK\$ mn
Cash	94,021
Other assets	342,528
Total assets	436,549

Debt	94,532
Shareholders' loan	40,497
Other liabilities	119,597
Total equity	181,922

Total liabilities and equity**436,549**

Net gearing	23%
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Sources: Company data, J.P. Morgan estimates

Landbank to be injected

		GFA (sqm)	% total
Beijing	Tier 1	1,025	9%
Shanghai	Tier 1	555	5%
Tianjin	Top tier 2	280	3%
Chongqing	Low tier 2	2,316	21%
Suzhou	Top tier 2	30	0%
Chengdu	Top tier 2	386	4%
Xi'an	Low tier 2	750	7%
Urumqi	Tier 3	1,620	15%
Changsha	Low tier 2	573	5%
Weifang	Tier 3	2,325	21%
Zibo	Tier 3	1,009	9%
London	London	48	0%
	Tier 1	1,580	14%
	Top tier 2	696	6%
	Low tier 2	3,639	33%
	Tier 3	4,954	45%
	London	48	0%

Sources: Company data, J.P. Morgan estimates

Investment Thesis

COLI's sales have slowed down year to date and have not seen a big improvement so far. This should result in less delivery and hence lower earnings in 2015-16E. We expect the earnings CAGR to slow to single digits for the coming 2.5 years. COLI has finished 80% of its land acquisition target in 2014, but a big portion of this landbank is expensive with slow asset turnover.

Valuation

Our Dec-2015 price target of HK\$24.5 is based on 8.0x 2015E P/E. The P/E we use is the highest among pure developers given COLI's high ROE, lower gearing and SOE background. Such a multiple is the same as China Vanke, as COLI has a higher ROA, offset by slower growth. The P/E we use is slightly lower than the average P/E since 2011, which is the time when growth started to slow down for the industry. We argue COLI should trade below this due to the slowdown in growth rate for COLI specifically.

Risks to Rating and Price Target

Key upside risks to our PT are subsequent acquisition of cheap landbank, broad based policy easing, and substantial NAV accretion from injection by CSCEC. Key downside risks to our PT are a demand shock caused by substantial deterioration in the macro economy, substantial NAV dilutive injection, and further Rmb depreciation against the USD.

China / Hong Kong Property

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Date	Rating	Share Price (HK\$)	Price Target (HK\$)
18-Mar-07	OW	8.70	9.60
18-Apr-07	OW	10.66	10.50
01-Jun-07	OW	10.96	13.00
19-Jul-07	OW	14.38	17.50
26-Nov-07	OW	15.74	20.00
01-Feb-08	OW	14.63	19.00
24-Mar-08	OW	11.43	15.00
20-Jan-09	N	11.10	9.00
24-Mar-09	N	12.82	10.00
08-Jun-09	OW	16.42	18.50
18-Aug-09	OW	17.30	19.50
07-Jun-10	OW	14.74	17.00
12-Aug-10	OW	16.30	18.00
11-Nov-10	OW	16.38	19.50
18-Mar-11	OW	13.14	18.00
10-Aug-11	OW	16.42	21.30
19-Oct-11	OW	12.36	16.50
23-Feb-12	OW	15.96	18.30
16-Mar-12	OW	15.78	18.50
12-Aug-12	OW	18.08	21.00
30-Nov-12	OW	22.50	23.50
17-Jan-13	N	24.80	26.00
19-Mar-13	N	21.10	23.00
22-Jul-13	N	20.65	21.50
24-Oct-13	OW	23.65	27.00
14-Mar-14	OW	18.80	26.00
22-Jun-14	OW	19.46	24.50
31-Jul-14	OW	22.75	29.00
30-Oct-14	N	21.85	24.50

<http://gfd-app.emea.jpmchase.net:6080/server/console/chart/?shareClassId=503252&shareClassServerId=4&chartDesignation=1&actionType=C>

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