

Golden Eagle (3308 HK)

Reduce

Target price (HKD)	8.20
Share price (HKD)	9.23
Upside/Downside (%)	-11.2

Dec	2014 a	2015 e	2016 e
HSBC EPS	0.53	0.51	0.51
HSBC PE	13.8	14.5	14.5
Performance	1M	3M	12M
Absolute (%)	-2.0	2.1	-9.7
Relative ^A (%)	-3.1	-2.1	-30.1

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Lina Yan*
Analyst
The Hongkong and Shanghai Banking Corporation Limited
+852 2822 4344
linayjyan@hsbc.com.hk

Erwan Rambourg*
Analyst
The Hongkong and Shanghai Banking Corporation Limited
+852 2996 6575
heraldvanderlinde@hsbc.com.hk

Vishal Goel*
Analyst

View HSBC Global Research at:
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Reduce: More pressure on profitability and liquidity

- ▶ **2H core profit fell 16.8% y-o-y, after a 12.5% drop in 1H, missing 2H guidance of flat core profit**
- ▶ **The benefit of XJK store improvement will be offset by losses on new stores; pressure on liquidity to remain**
- ▶ **Establish Reduce rating with a PE-based fair value target price of HKD8.2**

2014 core profit missed. Golden Eagle reported a 16.8% fall in operating profit in 2H, behind our estimate and management's guidance at the interim result of flat operating profit in 2H. But aided by RMB112m of non-operating gains relating to FX and investment disposals, full-year net profit came to RMB1,082m, in line with our and consensus forecasts. A final dividend of RMB0.151/sh was declared, bringing the full-year payout to 40%, up from 30% in 2013. It also spent RMB395m on buying back 2.7% of shares outstanding in 2014.

Improvement in XJK store will be offset by cost of expansion. On 26 April 2014, it opened Phase II of its XJK flagship store in Nanjing. Phase II has a GFA of 81,100sqm, enlarging the whole shopping complex by 3.4x. The XJK store's gross sales proceeds (GSP) fell 11.7% in 2014 and its profit dropped by RMB70.8m. However, we agree with management that the GSP of the XJK store is likely to achieve 30% growth in 2015. However, we think the improvement in profit from XJK will be fully offset by additional losses from 6 new stores opened in 2014 and 2015. We cut 2015/2016 operating profit forecasts by 15%/18% to reflect the miss in core earnings in 2014.

Medium-term outlook remains challenging and pressure on liquidity remains. The bigger picture is that competition among department stores and shopping malls continues to intensify and the traditional high ROIC concessionaire model needs to change. We have yet to see any catalysts, such as signs of consolidation, emerging. Medium-term earnings visibility is low, in our view, due to returns from new large shopping malls; it plans to add 1.45m sqm in 2015-2017 versus a total of 1.53m sqm in retail space as of 2014. In addition, there is execution risk in monetizing investments in lifestyle centres and various new initiatives. We also see pressure on liquidity. Its net cash position at end 2014 was down 40% from a year ago to RMB2,292m as a result of the 43% drop in operating cash flow, rise in capex and dividend payments and share backs. In 2015-16, the capex will be RMB1-1.5bn p.a. and it plans to maintain a dividend payout of 30-40%. Together with a decline in prepaid card sales, the pressure on liquidity is likely to remain.

Establishing a Reduce rating and setting our TP at HKD8.2 based on a target PE of 12.8x (applied to 2015) derived from the Gordon growth model. Our previous TP was HKD9.6; the change in TP comes from lower earnings and a lower PE from lowering ROE. Our target PE is about 20% below its average since 2012, which seems justified given the deteriorating ROE.

Index ^A	HSCEI	Enterprise value (CNYm)	11223
Index level	12,178	Free float (%)	25
RIC	3308.HK	Market cap (USDm)	2,125
Bloomberg	3308 HK	Market cap (HKDm)	16,485

Source: HSBC

Source: HSBC

Financials & valuation

Financial statements

Year to	12/2014a	12/2015e	12/2016e	12/2017e
Profit & loss summary (CNYm)				
Revenue	3,910	4,391	4,863	5,550
EBITDA	1,577	1,678	1,754	1,950
Depreciation & amortisation	-255	-355	-408	-461
Operating profit/EBIT	1,323	1,323	1,346	1,489
Net interest	100	-14	-35	-50
PBT	1,538	1,312	1,314	1,443
HSBC PBT	1,425	1,312	1,314	1,443
Taxation	-458	-390	-391	-429
Net profit	1,082	922	923	1,014
HSBC net profit	970	922	923	1,014

Cash flow summary (CNYm)

Cash flow from operations	722	920	1,076	1,148
Capex	-808	-1,240	-1,334	-1,367
Cash flow from investment	454	-180	-834	-867
Dividends	-429	-365	-366	-402
Change in net debt	1,551	959	825	804
FCF equity	368	-349	-297	-274

Balance sheet summary (CNYm)

Intangible fixed assets	2,466	2,425	2,385	2,346
Tangible fixed assets	6,020	7,206	8,338	9,416
Current assets	6,385	4,641	4,318	4,675
Cash & others	5,409	3,389	2,656	2,280
Total assets	16,497	15,899	16,668	18,064
Operating liabilities	5,409	5,299	5,419	5,774
Gross debt	3,116	2,056	2,148	2,576
Net debt	-2,292	-1,333	-508	296
Shareholders funds	5,411	5,967	6,525	7,136
Invested capital	5,029	6,560	7,943	9,358

Ratio, growth and per share analysis

Year to	12/2014a	12/2015e	12/2016e	12/2017e
Y-o-y % change				
Revenue	0.4	12.3	10.8	14.1
EBITDA	-8.8	6.4	4.6	11.2
Operating profit	-12.7	0.0	1.8	10.6
PBT	-10.0	-14.7	0.2	9.8
HSBC EPS	-10.8	-4.7	0.2	9.8

Ratios (%)

Revenue/IC (x)	0.9	0.8	0.7	0.6
ROIC	22.4	16.0	13.0	12.1
ROE	18.2	16.2	14.8	14.8
ROA	7.6	6.9	6.5	6.6
EBITDA margin	40.3	38.2	36.1	35.1
Operating profit margin	33.8	30.1	27.7	26.8
EBITDA/net interest (x)		121.6	49.7	39.1
Net debt/equity	-42.3	-22.3	-7.8	4.1
Net debt/EBITDA (x)	-1.5	-0.8	-0.3	0.2
CF from operations/net debt				388.2

Per share data (CNY)

EPS reported (fully diluted)	0.60	0.51	0.51	0.56
HSBC EPS (fully diluted)	0.53	0.51	0.51	0.56
DPS	0.24	0.20	0.20	0.22
Book value	3.00	3.31	3.62	3.96

Key forecast drivers

Year to	12/2014a	12/2015e	12/2016e	12/2017e
Effective OFA growth %	6	24	22	26
SSS %	-5.5	3.0	2.2	3.1
Direct sales margin %	18	18	18	18
Commission rate %	18.2	18.0	17.8	17.7
Effective tax rate %	29.8	29.8	29.8	29.8
Dividend payout ratio %	39.6	39.6	39.6	39.6

Valuation data

Year to	12/2014a	12/2015e	12/2016e	12/2017e
EV/sales	2.6	2.6	2.5	2.3
EV/EBITDA	6.5	6.7	6.9	6.6
EV/IC	2.0	1.7	1.5	1.4
PE*	13.8	14.5	14.5	13.2
P/Book value	2.5	2.2	2.0	1.9
FCF yield (%)	2.9	-2.8	-2.4	-2.2
Dividend yield (%)	3.2	2.7	2.7	3.0

Note: * = Based on HSBC EPS (fully diluted)



Note: price at close of 23 Mar 2015

More pressure on profitability and liquidity

- ▶ Core profit fell 16.8% y-o-y in 2H, after a 12.5% drop in 1H, missing 2H guidance of flat core profit
- ▶ The benefit of XJK store improvement will be offset by losses on new stores; pressure on liquidity to remain
- ▶ We establish a Reduce rating with a revised PE-based target price of HKD8.2

Golden Eagle – Revisions to HSBC earnings estimates

Year-end Dec (RMBm)	2H14e	2H14a	Diff	2014e	2014a	Diff	2015e - old	2015e - new	Diff	2016e - old	2016e - new	Diff	2017e
Gross sales proceeds (GSP)	8,582	7,903	-8%	16,520	15,841	-4%	17,913	17,558	-2%	19,711	19,194	-3%	21,738
Yoy %	5%	-4%		-2%	-6%		8%	11%		10%	9%		13%
Concessionaire	7,776	7,055	-9%	14,926	14,205	-5%	16,079	15,615	-3%	17,563	16,944	-4%	19,089
Direct sales	735	762	4%	1,458	1,486	2%	1,590	1,729	9%	1,758	1,981	13%	2,352
Operating Revenue	2,052	2,009	-2%	3,953	3,910	-1%	4,352	4,391	1%	4,862	4,863	0%	5,550
Yoy %	5%	3%		2%	0%		10%	12%		12%	11%		14%
Operating profit	749	626	-16%	1,446	1,323	-8%	1,559	1,323	-15%	1,642	1,346	-18%	1,489
Yoy %	0%	-17%		-5%	-13%		8%	0%		5%	2%		11%
Net finance income (cost)	34	57	68%	77	100	30%	60	-14	-123%	52	-35	-168%	-50
Non-operating gain (loss)	0	150		-38	112		0	0		0	0		0
Profit before tax	778	840	8%	1,476	1,538	4%	1,609	1,312	-18%	1,683	1,314	-22%	1,443
Tax	(214)	(243)		(428)	(458)		(434)	(390)		(437)	(391)		(429)
Net profit	564	599	6%	1,048	1,082	3%	1,174	922	-22%	1,245	923	-26%	1,014
Yoy %	-7%	-1%		-15%	-12%		12%	-15%		6%	0%		10%
Adjusted Net Profit	564	449	-20%	1,085	970	-11%	1,174	922	-22%	1,245	923	-26%	1,014
Yoy %	5%	-17%		-4%	-15%		8%	-5%		6%	0%		10%
Key drivers			Ppt Diff			Ppt Diff			Ppt Diff			Ppt Diff	
Effective OFA growth Yoy %	15%	10%	-5%	10%	6%	-4%	27%	24%	-3%	20%	22%	2%	26%
SSSG %	-2.2%	-4.3%	-2%	-4.5%	-5.5%	-1%	1.0%	3.0%	2%	2.9%	2.2%	-1%	3.1%
Commission rate	18.4%	18.5%	0.1%	18.2%	18.2%	0.0%	18.1%	18.0%	-0.1%	17.9%	17.8%	-0.1%	17.7%
Consolidated gross margin	18.3%	18.4%	0.1%	18.1%	18.2%	0.0%	18.1%	18.0%	-0.1%	17.9%	17.8%	-0.1%	17.7%
Staff costs / GSP	2.6%	3.1%	0.5%	2.5%	2.7%	0.2%	2.4%	2.9%	0.5%	2.8%	3.1%	0.3%	3.2%
DA+Lease / GSP	2.4%	3.0%	0.6%	2.5%	2.8%	0.3%	2.7%	3.2%	0.6%	3.0%	3.4%	0.4%	3.4%
Operating margin (/ Rev)	36.5%	31.2%	-5.3%	36.6%	33.8%	-2.7%	35.8%	30.1%	-5.7%	33.8%	27.7%	-6.1%	26.8%
Net finance income (cost) / Rev	1.7%	2.9%	1.2%	1.9%	2.6%	0.6%	1.4%	-0.3%	-1.7%	1.1%	-0.7%	-1.8%	-0.9%
Effective tax rate	27.4%	28.9%	1.5%	29.0%	29.8%	0.8%	27.0%	29.8%	2.8%	26.0%	29.8%	3.8%	29.8%
Dividend payout	0.0%	0.0%	0.0%	33.2%	39.6%	6.5%	33.2%	39.6%	6.5%	33.2%	39.6%	6.5%	39.6%
Reported net profit margin (/ Rev)	27.5%	29.8%	2.3%	26.5%	27.7%	1.2%	27.0%	21.0%	-6.0%	25.6%	19.0%	-6.6%	18.3%

Source: Company Data, HSBC estimates

Earnings revisions

We now expect OP to be flat in 2015 vs our earlier estimate of 8% growth. Along with the disappointing core profit in 2014, we cut our 2015 OP estimate by 15%. We also lower our net interest income forecast and raise our effective tax rate assumption in 2015, leading to a 22% cut in our net profit estimate.

Golden Eagle – Valuation summary

	New	Old	% diff
12 month fwd ROE	16.2%	19.4%	
- Period	FY2015e	FY2014e	
- ROE	16.2%	19.4%	
Cost of equity (COE)	9.4%	9.4%	
Risk-free rate	3.5%	3.5%	
Equity risk premium	6.5%	6.5%	
Equity beta			
- sector beta	0.95	0.95	
- company specific beta	0.95	0.95	
Long-term growth rate (g)	3.0%	3.0%	
Target PE = (ROE - g) / (ROE x [COE - g])	12.8	13.3	-4%
12 month EPS (RMB)	0.51	0.58	
- Period	FY2015e	FY2014e	
- EPS	0.51	0.58	
HKD : RMB	1.25	1.25	
Target price (HKD)	8.2	9.6	-15%

Source: Company Data, HSBC estimates

Valuation and risks

We establish a Reduce rating with TP of HKD8.20 (previously HKD9.6). The target price is based on a 12.8x PE derived from the Gordon Growth Model with a one-year forward ROE of 16.2%. Under our old rating system, the stock was rated Underweight with a target price of HKD9.6 based on a 13.3x PE derived from the Gordon Growth Model with a one-year forward ROE of 19.4%. Our target PE is about 20% below its average since 2012, which seems justified given the deteriorating ROE.

Upside risks to our view: Better-than-expected SSSG; stronger than expected profit recovery in XJK store.



Disclosure appendix

Analyst Certification

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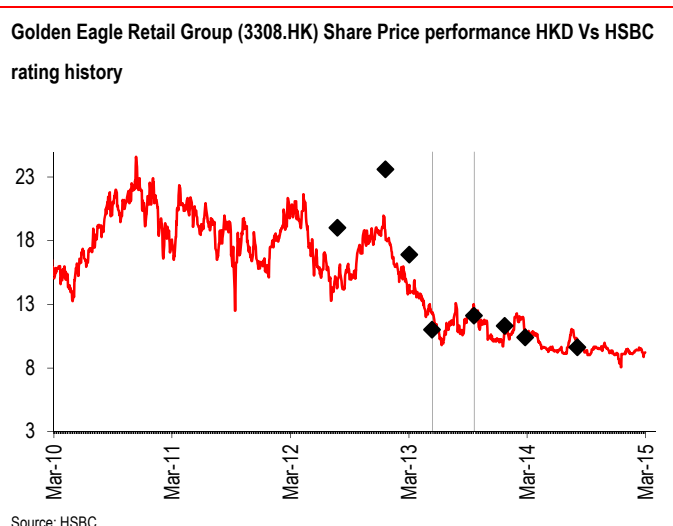
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Share price and rating changes for long-term investment opportunities



Recommendation & price target history

From	To	Date
Overweight (V)	Underweight (V)	03 June 2013
Underweight (V)	Underweight	11 October 2013
Target Price	Value	Date
Price 1	19.00	15 August 2012
Price 2	23.60	10 January 2013
Price 3	16.90	25 March 2013
Price 4	11.00	03 June 2013
Price 5	12.10	11 October 2013
Price 6	11.30	14 January 2014
Price 7	10.40	18 March 2014
Price 8	9.60	26 August 2014

Source: HSBC

HSBC & Analyst disclosures

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Company	Ticker	Recent price	Price Date	Disclosure
GOLDEN EAGLE RETAIL GROUP	3308.HK	9.23	23-Mar-2015	5, 6, 7

Source: HSBC

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Issuer of report

The Hongkong and Shanghai Banking Corporation Limited

Level 19, 1 Queen's Road Central

Hong Kong SAR

Telephone: +852 2843 9111

Fax: +852 2596 0200

Website: www.research.hsbc.com

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Global Consumer Brands & Retail Research Team

Europe

Consumer Brands & Retail

Antoine Belge
Head of Consumer Brands and Retail Equity Research
+33 1 56 52 43 47 antoine.belge@hsbc.com

Anne-Laure Jamain
Analyst
+44 207 991 6587 annelaure.jamain@hsbcib.com

David McCarthy
Head of Consumer Retail, Europe
+44 207 992 1326 david1.mccarthy@hsbcib.com

Andrew Porteous
Analyst
+44 20 7992 4647 andrew.porteous@hsbc.com

Jérôme Samuel
Analyst
+33 1 56 52 44 23 jerome.samuel@hsbc.com

Emmanuelle Vigneron
Analyst
+33 1 56 52 43 19 emmanuelle.vigneron@hsbc.com

Paul Rossington
Analyst
+44 20 7991 6734 paul.rossington@hsbcib.com

Graham Jones
Analyst
+44 20 7992 5347 graham.jones@hsbc.com

Damian McNeela
Analyst
+44 20 7992 4223 damian.mcneela@hsbc.com

CEEMEA

Consumer Brands & Retail

Bulent Yurdagul
Analyst
+90 212 3764612 bulentyurdagul@hsbc.com.tr

Jeanine Womersley
Analyst
+27 21 6741082 jeanine.womersley@za.hsbc.com

Specialist Sales

David Harrington
+44 20 7991 5389 david.harrington@hsbcib.com

Asia

Consumer Brands & Retail

Erwan Rambourg
Head of Consumer Brands and Retail Equity Research
+852 2996 6572 erwanrambourg@hsbc.com.hk

Christopher Leung
Analyst
+852 2996 6531 christopher.k.leung@hsbc.com.hk

Lina Yan
Analyst
+852 2822 4344 linayjyan@hsbc.com.hk

Catherine Chao
Analyst
+852 2996 6570 catherinefchao@hsbc.com.hk

Charlene Liu
+852 2822 4398 charlenerliu@hsbc.com.hk

Alice Chan
+852 2996 6535 aliceptchan@hsbc.com.hk

Karen Choi
Analyst
+822 3706 8781 karen.choi@kr.hsbc.com

Jena Han
Analyst
+822 3706 8772 jenahan@kr.hsbc.com

Permada (Mada) Darmono
Analyst
+65 6658 0613 permada.w.darmono@hsbc.com.sg

Ananita M Kusumaningsih
Analyst
+65 6658 0610 ananita.m.kusumaningsih@hsbc.com.sg

Thilan Wickramasinghe
Analyst
+65 6658 0609 thilanw@hsbc.com.sg

Amit Sachdeva
Analyst
+91 22 2268 1240 amit1sachdeva@hsbc.co.in

Chloe Wu
Analyst
+ 8862 6631 2866 chloe.c.wu@hsbc.com.tw

North & Latin America

Consumer & Retail

Richard Cathcart
Analyst
+55 11 2169 4429 richard.cathcart@hsbc.com

Stewart Ragar
Analyst
+55 11 3847 9342 stewart.h.ragar@us.hsbc.com

Ruben Couto
Associate
+ 55 11 2169 4615 ruben.c.couto@hsbc.com.br

Food & Beverage

James Watson
Analyst
+1 212 525 4905 james.c.watson@us.hsbc.com

Agricultural Products

Alexandre Falcao
Analyst
+55 11 3371 8203 alexander.p.falcao@hsbc.com.br

Ravi Jain
Analyst
+1 212 525 3442 ravijain@us.hsbc.com

Gustavo Gregori
Analyst
+55 11 3847 9881 gustavo.h.gregori@hsbc.com.br