

**FIG**  
**Diversified Financial Services**  
 Equity – China

## Buy

Target price (HKD)	2.10		
Share price (HKD)	1.69		
Upside/Downside (%)	24		
Performance	1M	3M	12M
Absolute (%)	-3	1	-2
Relative <sup>A</sup> (%)	-3	-3	-21
Index <sup>A</sup>	HSCEI		
RIC	8207.HK		
Bloomberg	8207.HK		
Market cap (USDbn)	0.7		
Market cap (HKDbn)	5.4		
Free float (%)	39		

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# Credit China (8207 HK)

Buy: Internet finance contribution could rise to 40%

- **We expect internet finance revenue to double in 2015; contribution to group revenue likely to exceed 40% as traditional business fades out faster than expected**
- **Asset quality of peer-to-peer (P2P) loans is tracking well with collateral and guarantee, overdue ratio at 0.34% with zero loss ratio for investors**
- **We establish a Buy rating on Credit China, with a fair value TP of HKD2.10**

**Profit decline on revaluation and disposal:** Credit China FY14 profit was RMB58m, down 59% y-o-y, largely in line with pre-announced figures in Jan 2015. The reason for the decline was a lack of investment revaluation gain and some one-off adjustments from disposal of the Chongqing microfinance business, which should no longer be an issue for 2015.

**Internet finance tracking well, revenue to double:** Compared to the average monthly data in 4Q14, latest P2P volume rose 58% to RMB506m in January 2015. CEO Mr Phang indicated that such momentum has sustained into February. We expect revenue from internet finance to double in 2015e to RMB177m, and contribution to group revenue to exceed 40% as the traditional business fades out faster than our expectation. Credit China has managed to grow its third party payment system users from 540,000 by 2014 to nearly 800,000 currently. Mr Phang has mentioned growth targets of 3-4 times per year, which he believes to be achievable once the infrastructure is in place.

**Strong asset quality of P2P loans:** According to Mr Phang, the overdue ratio for P2P loans has remained low at 0.34%, thanks to the various collateral and guarantee protection. Loss rate for investors is zero. Note that the stress of collateral usage and guarantee from third party credit companies is why we think Credit China could stand out versus its peers. The company welcomes more stringent regulation on P2P as it would help reduce competition.

**Traditional business still challenging:** Overdue ratio for the traditional entrusted lending to property developers has remained high at 29% by 2014, marginally improving from the 35% in 1H14, yet still doubled the 14% in 2013.

**We set a fair value TP of HKD2.10 and establish a Buy rating on Credit China (vs OW(V) under our old rating system).** We have adjusted our estimates down by 4-6% to reflect the input from FY14 figures. We also introduce 2017 estimates. See page 2 for valuation and risks.

Credit China: Financial summary

<b>P&amp;L summary (RMBm)</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2014 y-o-y%</b>	<b>2014a vs our est</b>
Net Interest Income	254	283	232	150	-35	-31
Interest finance income			0	132	n.a.	91
Revenue	273	298	326	308	-5	4
Admin & other expense	-55	-69	-113	-200	77	26
Pre-provisional operating profit	199	223	207	101	-51	-22
Provisioning charge	0	0	0	0	n.a.	-100
Profit before tax	199	223	207	101	-51	-3
Income Tax	-53	-59	-52	-35	-32	34
Minority Interest	-2	-15	-14	-8	-40	-46
Att profit	143	150	141	58	-59	-9
<b>Balance sheet items (RMBm)</b>						
Total assets	1,025	1,321	2,312	2,672	16	1
Total loans	561	980	1,001	863	-14	-27
Debt and borrowings	277	317	690	492	-29	-37
Total equity	654	744	1,194	1,406	18	1
<b>Ratios (%)</b>						
Cost / income ratio	27.1	25.1	36.7	67.1	30.5	11.2
ROAE	27.3	21.4	14.6	4.5	-10.1	-0.5
Effective Tax	26.9	26.4	25.1	34.6	9.5	9.6

Source: Company data, HSBC estimates

**Valuation and risks:** Our valuation methodology, based on the Gordon Growth model, is unchanged. We arrive at a PB multiple of 3.6x (unchanged) applied to end-2015e (previously 1H15e) BVPS of RMB0.46 (previously RMB0.45), assuming a medium-term ROE of 28% (unchanged), a growth rate of 5% and a cost of equity (COE) of 11.3% (unchanged), with RMB/HKD of 1.23 (unchanged). COE was based on a risk-free rate of 3.5%, equity risk premium of 6% and beta of 1.30. The gives us a rounded fair value target price of HKD2.10.

Under our new ratings system, we establish a Buy rating on Credit China.

Key downside risks include more volatile asset quality in entrusted loan book, lower loan pricing power, and potential unfavourable regulation on P2P platforms.

## Financials & forecasts Credit China (8207 HK)

Year	2014	2015e	2016e	2017e
<b>P&amp;L summary (RMBm)</b>				
Interest & fee income	242	199	170	147
Interest Expense	-92	-51	-51	-51
Net Interest Income	150	148	119	96
Internet housing loan fees	25	51	85	122
Third party payment fees	61	126	207	290
Gain on transfer of loan rights	46	42	38	34
<b>Operating Income</b>	<b>282</b>	<b>367</b>	<b>449</b>	<b>543</b>
Other Income	19	19	19	19
Gain on disposal / fair value	8	0	0	0
<b>Total income</b>	<b>308</b>	<b>386</b>	<b>468</b>	<b>561</b>
Admin & other expense	-203	-240	-288	-345
FV change in CB deriv	0	0	0	0
Share-based payment	-5	-6	-7	-8
Provisioning charge	0	0	0	0
<b>Profit before tax</b>	<b>101</b>	<b>140</b>	<b>173</b>	<b>208</b>
Income Tax	-35	-35	-43	-52
Net profit	66	105	130	156
Minority Interest	-8	-8	-7	-7
<b>Att profit</b>	<b>58</b>	<b>98</b>	<b>123</b>	<b>149</b>
<b>ROAA Deconstruction</b>				
Net interest income	6.0	5.4	4.1	3.1
Internet housing loans	1.0	1.9	3.0	4.0
Third party payment fees	2.4	4.6	7.2	9.5
<b>Operating income</b>	<b>10.5</b>	<b>12.6</b>	<b>14.9</b>	<b>17.2</b>
Operating expenses	-8.2	-9.0	-10.2	-11.5
PPOP	2.3	3.6	4.7	5.7
Impairment loss on L&A	0.0	0.0	0.0	0.0
<b>Profit before tax</b>	<b>2.3</b>	<b>3.6</b>	<b>4.7</b>	<b>5.7</b>
Taxation	-1.4	-1.3	-1.5	-1.7
Minorities	-0.3	-0.3	-0.3	-0.2
<b>ROAA</b>	<b>2.3</b>	<b>3.6</b>	<b>4.3</b>	<b>4.9</b>
Leverage (x)	1.9	1.9	1.9	1.9
<b>ROAE</b>	<b>4.5</b>	<b>6.7</b>	<b>8.0</b>	<b>9.0</b>
<b>Per share data (RMB)</b>				
EPS (diluted)	0.02	0.03	0.04	0.05
EPS (basic)	0.02	0.03	0.04	0.05
DPS	0.00	0.01	0.01	0.01
BVPS	0.44	0.46	0.49	0.53
<b>Valuation multiple</b>				
P/E (diluted)	74.7	45.7	36.3	29.9
P/E (basic)	74.1	45.4	36.1	29.7
P/B	3.1	3.0	2.8	2.6
Dividend yield%	0.3	0.4	0.6	0.7
Source: HSBC estimates; Note: Price at close 24 March 2015				
Year	2014	2015e	2016e	2017e
<b>BS summary (RMBm)</b>				
Loan receivables	867	795	756	718
Cash	601	781	959	1,160
Investment properties	575	575	575	575
Intangible / goodwill	180	180	180	180
Others	453	477	502	530
<b>Total assets</b>	<b>2,672</b>	<b>2,804</b>	<b>2,968</b>	<b>3,159</b>
Corporate bonds	204	210	210	210
Borrowings	288	288	288	288
<b>Total liabilities</b>	<b>1,252</b>	<b>1,314</b>	<b>1,374</b>	<b>1,441</b>
Share capital	268	268	268	268
Reserves	1,138	1,221	1,324	1,449
<b>Att equity</b>	<b>1,406</b>	<b>1,489</b>	<b>1,592</b>	<b>1,717</b>
Minority Interest	14	1	1	1
<b>Growth rate (YoY %)</b>				
Net Interest Income	-35	-1	-20	-19
Internet housing loan fees	NA	105	68	43
Third party payment fees	NA	108	64	40
Operating Income	21	30	22	21
Total income	-5	25	21	20
Admin & other expense	78	18	20	20
<b>Att profit</b>	<b>-59</b>	<b>68</b>	<b>26</b>	<b>21</b>
Loan receivables	-13	-8	-5	-5
<b>Total assets</b>	<b>16</b>	<b>5</b>	<b>6</b>	<b>6</b>
Debt and borrowings	-20	3	0	0
<b>Total liabilities</b>	<b>23</b>	<b>5</b>	<b>5</b>	<b>5</b>
<b>Key ratios (%)</b>				
Cost-to-income	67.1	63.6	62.9	62.9
Cost/avg assets	8.2	9.0	10.2	11.5
Op income per staff (RMBm)	1.0	0.7	0.5	0.4
Profit per staff (RMBm)	0.2	0.3	0.3	0.4
ROAA	2.3	3.6	4.3	4.9
Asset to equity leverage	1.9	1.9	1.9	1.9
ROAE	4.5	6.7	8.0	9.0
<b>Issuer information</b>				
Share price (HKD)				1.69
Target price (HKD)				2.10
Upside				24%
Number of shares (bn)				3.2
Market cap (USDbn)				0.7
Market cap (HKDbn)				5.4
Free float				39%
Exchange rate assumed				1.23
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# Disclosure appendix

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### **From 23rd March 2015 HSBC has assigned ratings on the following basis:**

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

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For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile\*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile\*). Stocks between these bands were classified as Neutral.

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## Rating distribution for long-term investment opportunities

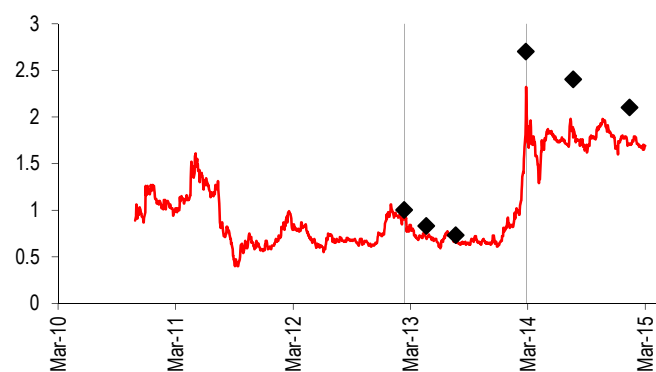
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For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see “Stock ratings and basis for financial analysis” above.

## Share price and rating changes for long-term investment opportunities

Credit China Holdings Lim (8207.HK) Share Price performance HKD Vs HSBC rating history



Source: HSBC

Recommendation & price target history

From	To	Date
N/A	Neutral (V)	05 March 2013
Neutral (V)	Overweight (V)	19 March 2014
Target Price	Value	Date
Price 1	1.00	05 March 2013
Price 2	0.83	13 May 2013
Price 3	0.73	13 August 2013
Price 4	2.70	19 March 2014
Price 5	2.40	13 August 2014
Price 6	2.10	04 February 2015

Source: HSBC

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