Company report

FIG
Real Estate
Equity – China

HSBC
Global Research

Jinmao (China) Investment (6139 HK)

Buy: Sector leading yield supports near-term stability

- **Operating metrics disappointed although actual FY14 distribution income is guaranteed**
- **Annualized yield of 8.92% is the highest among H-REITs we cover; yield enhancement mechanism supports near-term stability**
- **We establish a Buy rating with a fair value TP of HKD6.20**

FY14 operating results disappointed although actual distribution is guaranteed. Jinmao reported FY14 distribution of HKD481m, or HK0.2405/unit which represents the guaranteed amount and hence no surprise. However, revenue actually came in 4% below our forecast, while cost of sales and SG&A expenses are 4% and 14% higher than our expectation, respectively. As a result, the distribution guarantee that kicked in amounts to HKD252m, which is above our HKD170m forecast. Note that Jinmao will be paying out dividend for the first time since listing on 2nd July 2014. Based on the current unit price of HKD5.39, the yield is 4.46%. In annualized terms, the yield would be 8.92%, the highest among the HK REITs we cover.

Hotel asset performance was steady. In 2014, revenue of the five mature hotels amounted to HKD1.27bn, largely flat y-o-y. Revpar growth in Grand Hyatt (Shanghai) and JW Marriott (Shenzhen) had effectively offset weakness at The Westin (Beijing), and Hilton and Ritz-Carlton in Sanya. While revenue was flat y-o-y, we would argue that this is still respectable results as Revpar of most mature hotels continue to outperform their respective competitive sets.

Management sees no threat from Shanghai Centre competition. While Shanghai Centre, a 220k sqm Grade A office building located adjacent to Jin Mao Tower, will be completed in June, the company has taken precautionary steps to minimize potential impact from new competition. Strategically, Jinamo has adopted a much more flexible arrangement for lease renewal and shorten lease negotiation time with existing tenants.

We establish a Buy rating on Jinmao (vs OW(V) under our previous rating system). We see fair value TP at HKD6.20 based on an unchanged 30% discount to our appraised value of HKD8.8 per unit, based on the equally weighted average of our DDM and NAV-based valuations. The FY15e DPU yield is 8.7% versus 5.8% average for the H-REITs we cover. Downside risks include: distribution volatility post expiry of yield stabilization mechanisms, slowdown in tourism, further curbs in corporate spending, and macro developments/interest rate hikes.

Index^	HSCEI
Index level	12,005
RIC	6139.HK
Bloomberg	6139 HK

Source: HSBC

Enterprise value (HKDm)	18,705
Free float (%)	100
Market cap (USDm)	1,387
Market cap (HKDm)	10,760

Source: HSBC

Buy

Target price (HKD)			6.20
Share price (HKD)			5.39
Upside/Downside (%)			15.0

Dec	2014 a	2015 e	2016 e
HSBC EPS	0.53	0.24	0.27
HSBC PE	10.2	22.5	20.0

Performance	1M	3M	12M
Absolute (%)	-2.5	-7.9	
Relative^ (%)	-2.2	-11.3	

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Issuer of report: The Hongkong and Shanghai Banking Corporation Limited

HSBC

Financials & valuation: Jinmao Investment

Buy

Financial statements

Year to	12/2014a	12/2015e	12/2016e	12/2017e
Profit & loss summary (HKDm)				
Hotel operating income	2,023	2,269	2,489	2,546
Property investment	568	608	639	671
Other business	169	174	180	185
Total Turnover	**2,761**	**3,051**	**3,307**	**3,402**
Total cost of sales	(1,208)	(1,244)	(1,361)	(1,395)
Gross profit	**1,553**	**1,807**	**1,946**	**2,007**
SG&A	(1,164)	(890)	(936)	(955)
Operating profit before non-operating expenses	**390**	**917**	**1,010**	**1,052**
Adjustment for Depreciation & Amortisation	307	316	322	325
Other gains/expenses included in EBITDA	18	11	12	12
EBITDA	**715**	**1,245**	**1,344**	**1,389**
Depreciation & Amortization	(307)	(316)	(322)	(325)
Other gains/expenses	27	14	16	16
Net interest expense	(374)	(341)	(345)	(351)
Revaluation Surplus	1,340	-	-	-
PBT	**1,401**	**602**	**692**	**730**
Taxation	(494)	(120)	(152)	(161)
Net profit	**907**	**481**	**540**	**569**
Adjustments				
Revaluation Surplus	(1,340)	-	-	-
Add: non cash portion of tax charge	383	-	-	-
Add: non cash portion of net finance costs	35	14	14	14
Depreciation & Amortization	307	316	322	325
FFE reserve capitalised	(23)	(24)	(24)	(25)
One-off gains / expenses	250	-	-	-
Full year income for distribution	**519**	**788**	**852**	**883**
Listing period Distribution Income	***229**	n.a.	n.a.	n.a.
Distribution guarantee/ shortfall payment	*252	151	101	49
Income to distribute	***481**	**939**	**952**	**932**

Listing period only
(2 July to 31 Dec 2014)

Cash flow summary (HKDm)				
Cash flow from operations	1,951	1,080	1,163	1,200
Capex	(1,545)	(365)	(139)	(138)
Other investing activities	369	247	(1)	(1)
Dividends paid	(6,321)	(710)	(946)	(942)
Net change in cash	(58)	10	179	242
Cash at the end	1,106	1,115	1,294	1,536

Balance sheet summary (HKDm)				
Shareholders' funds	9,107	9,154	8,773	8,401
Long-term liabilities	6,139	8,035	7,232	7,459
Deferred items	1,924	2,020	2,121	2,227
Total capital employed	17,170	19,208	18,126	18,087
Fixed assets	19,468	19,541	19,401	19,258
Other assets	1,810	1,852	1,879	1,905
Current assets	1,363	1,375	1,558	1,805
Total assets	22,640	22,768	22,838	22,968

Ratio, growth and per share analysis

Year to	12/2014a	12/2015e*	12/2016e	12/2017e
y-o-y % change				
Revenue	5%	11%	8%	3%
Operating profit	-50%	135%	10%	4%
PBT	2%	-57%	15%	5%
Ratios (%)				
ROIC ex-exceptional	5%	3%	3%	4%
ROAE ex-exceptional	8%	5%	6%	7%
ROAA ex-exceptionals	4%	2%	2%	2%
Operating margin	14%	30%	31%	31%
Interest cover ex-exceptional (x)	4.6	2.7	3.0	3.0
Gearing Ratio -Total Debt/Total Assets	37%	35%	36%	36%
Net debt/equity (incl. restricted cash)	66%	63%	63%	64%
Net debt/EBITDA (x)	10.1	5.6	5.1	4.8
Cash from operations/net debt	33%	21%	23%	24%
Per share data (HKD)				
Reported EPS (fully diluted)	0.53	0.24	0.27	0.28
HSBC EPS (fully diluted)	0.53	0.24	0.27	0.28
DPU (HKD)	*0.241	0.470	0.476	0.466

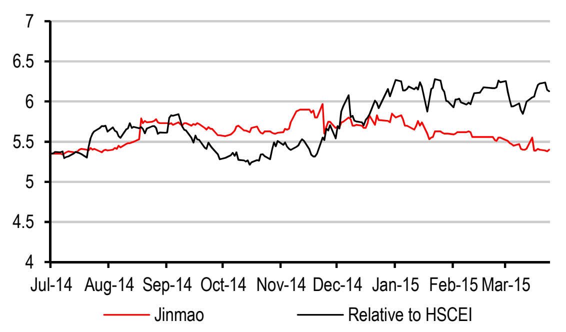
Listing period only (2 July to 31 Dec 2014)

Jinmao Investments: NAV breakdown

	(HKDm)	(HKD/sh)	% of GAV
Hotel properties			
Grand Hyatt Shanghai	3,663	1.83	14%
The Westin Beijing Chaoyang	3,030	1.52	11%
JW Marriott Hotel Shenzhen	1,917	0.96	7%
The Ritz-Carlton Sanya	3,436	1.72	13%
Hilton Sanya Resort and Spa	3,178	1.59	12%
Hyatt Regency Chonming	617	0.31	2%
Renaissance Beijing Wangfujing Hotel	566	0.28	2%
Grand Hyatt Lijiang	901	0.45	3%
Jinmao Tower (exlucding hotel)	**9,574**	**4.79**	**36%**
GAV	**26,883**	**13.44**	**100%**
Net debt (excluding restricted cash)	(6,922)	(3.46)	
Fair value NAV	**19,960**	**9.98**	

Source: HSBC estimates

Price relative



Source: HSBC

Note: price at close of 25 March 2015

Portfolio update – performance of key assets

Jinmao Tower. Total rental revenue grew 15% y-o-y to HKD524m. Jinmao Tower maintained a largely stable occupancy rate at 97.9% as of the end of 2014, just 0.6ppt lower than the 98.5% as of 1H14. Management noted a favourable market condition and they seized the opportunity to increase the average rental increased by a 10% y-o-y from RMB9.9/day/sqm in 2013 to RMB10.9/day/sqm in 2014.

The Grand Hyatt Shanghai. 2014 RevPAR was up 4% to RMB1,001, driven by a 5.1ppt increase in occupancy from 58.6% in 2013 to 63.7% in 2014, partially offset by a 4% decline in average room rate from RMB1,640 in 2013 to RMB1,572 in 20 14.

The Ritz-Carlton Sanya. RevPAR was down 2.7% y-o-y in 2014, hurt by a 4% decline in average room rate while occupancy rate was largely unchanged at 70.0% in 2014 versus 69.1% in 2013. Performance of this hotel (together with Hilton Sanya Resort and Spa) was impacted by increasing market supply in Haitang Bay in Hainan which is seeing a cluster of new luxury hotels.

The Westin Beijing. RevPAR declined slightly by 3.4% y-o-y. Due to more intense market competition from new supply in the vicinity such as the Four Seasons hotel, the company had lowered the room rate by 11% y-o-y in order to win more market share. However, the resultant 6.2 ppt increase in occupancy level from 71.7% in 2013 to 77.9% in 2014 was insufficient to offset impact from the room rate decline.

Hotel operational metrics

	Actual 2014	Actual 2013	y-o-y
Grand Hyatt Shanghai (1999)			
Occupancy	63.7%	58.6%	5.1ppt
Implied room rate	1,572	1,642	-4.3%
RevPAR	1,001	962	4.0%
The Westin Beijing Chaoyang (2008)			
Occupancy	77.9%	71.7%	6.2ppt
Implied room rate	1,215	1,367	-11.1%
RevPAR	946	979	-3.4%
JW Marriott Hotel Shenzhen (2009)			
Occupancy	77.0%	75.0%	2ppt
Implied room rate	1,060	1,039	2.0%
RevPAR	817	779	4.9%
The Ritz-Carlton Sanya (2008)			
Occupancy	70.0%	69.1%	0.9ppt
Implied room rate	2,661	2,773	-4.0%
RevPAR	1,864	1,916	-2.7%
Hilton Sanya Resort and Spa (2006)			
Occupancy	70.7%	65.8%	4.9ppt
Implied room rate	1,529	1,666	-8.2%
RevPAR	1,081	1,098	-1.5%
Hyatt Regency Chonming			
Occupancy	42.4%	N/A	N/A
Implied room rate	892	N/A	N/A
RevPAR	378	N/A	N/A
Renaissance Beijing Wangfujing Hotel (2014)			
Occupancy	34.7%	N/A	N/A
Implied room rate	668	N/A	N/A
RevPAR	232	N/A	N/A
Grand Hyatt Lijiang			
Occupancy	15.8%	N/A	N/A
Implied room rate	875	N/A	N/A
RevPAR	139	N/A	N/A

Source: Company data

Highlights from the analyst briefing

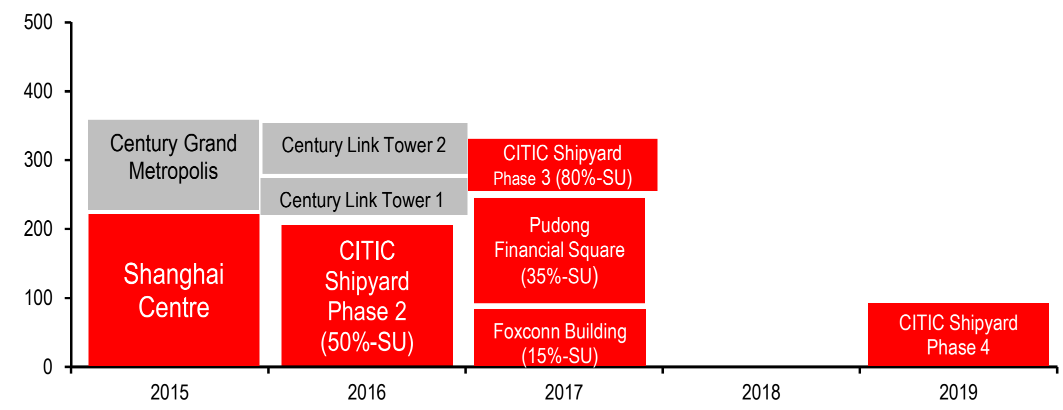
FY14 results – performance of mature assets lower than expectation. Management highlighted operating performance of the hotel assets were below expectation as it was previously expecting moderate growth from 2013. As a result, distribution income (pre-guarantee) was around HKD160m below their expectation.

Expects decent office rent growth in Jinmao Tower. While the average rental in 2014 was RMB10.9/sqm/day, management indicated that spot rent has reached RMB13/sqm/day for the recent renewals. With the exception of Shanghai Centre, supply in 2014-2016 is mainly for self-use and hence should continue to underpin favourably supply/demand dynamics.

Management sees no threat from Shanghai Centre competition. Management expects minimal impact to be seen in Jinmao Tower upon completion of Shanghai Centre, a Grade A office building located adjacent to Jinmao it scheduled for completion in June-15. In order to cope with more intense competition, Jinmao has adopted a much more flexible arrangement for lease renewal and shorten lease negotiation time with existing tenants.

China hotel market continues to recover. Management believes the hotel industry will continue to recover, citing strong statistics from domestic tourist growth and the fact that hotel demand in key cities has outpaced hotel supply in 2014, according got STR Global. Generally speaking, the decline in average room rate was offset by higher occupancy level. For the four key cities that it tracks, 2014 Revpar was flat in Beijing and Sanya, while Shenzhen and Shanghai recorded decent growth of 7% and 10.8% y-o-y, respectively.

Shanghai Pudong future supply (lettable GFA '000)



Source: JLL
Note: SU refers to the percentage of self-use space

What's changed? DPU, valuation and TP

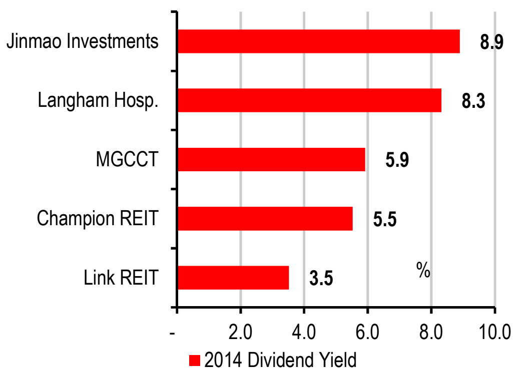
We tweak our FY15e and FY16e DPU by -4% and -4%, respectively, mainly to reflect slightly lower hotel occupancy rate and room rate for the mature hotel portfolio, particularly for Hilton Sanya Resort and Spa and Ritz-Carlton Sanya where new supply in the region continues to paint a challenging physical market backdrop. We have also factored in lower room rates for two new hotels - Renaissance Beijing Wangfujing Hotel and Grand Hyatt Lijiang, based the latest achieved figure in 2014. We introduce 2017 DPU of HKD0.466, which represents a decline of -2% y-o-y. Note that we have fully utilized the distribution shortfall quota of HKD300m (aggregate) in 2017. The outstanding shortfall quota which we could utilize by end-16 is HKD49m, which is insufficient to cover our expected shortfall of HKD95m.

Based on our DPU estimate changes, our DDM valuation is revised down 6% to HKD7.6 per stapled unit. Likewise, our NAV estimate has been lowered by 5% to HKD10.0 per stapled unit amid the changes to key income drivers. The average of these two valuation methods is HKD8.8 per stapled unit which represents our appraised value. For DDM, our assumptions of 8% cost of equity and a terminal growth of 1.5% remain unchanged.

We establish a Buy rating on Jinmao (vs OW(V) under our previous rating system). We see fair value at HKD6.20 based on an unchanged 30% discount to our appraised valuation. Jinmao continues to offer one of the highest yields in the sector. It currently trades at a 2015e distribution yield of 8.7% and 7.3% if we exclude the yield enhancement mechanisms, versus an average yield of 5.8% for the HK REITs we cover.

Our key downside risks include: distribution volatility post expiry of yield stabilization mechanisms, slowdown in tourism, further curbs in corporate spending, and macro developments/interest rate hikes.

Jinmao has the highest 2014 yield among REITs/trusts we cover



Source: HSBC estimates

HSBC

FY2014 comparison table

(HKDm)	2013	2014	y-o-y%
Turnover			
Property leasing	519	568	9%
Hotel operations	1,962	2,023	3%
Other operations	153	169	10%
Total Turnover	**2,634**	**2,761**	**5%**
Cost of sales	(1,107)	(1,208)	9%
Gross Profit	**1,527**	**1,553**	**2%**
Selling and distribution costs	(159)	(267)	68%
Administrative expenses	(591)	(897)	52%
Government Grant	10	11	5%
Adjustment: Depreciation	216	251	16%
Adjustment: Recognition of prepaid land lease payments	50	52	3%
Adjustment: Amortisation of intangible assets	5	4	-23%
"Others" within "Other Gain"	6	5	-26%
Share of profits of JV	2	3	39%
EBITDA	**1,068**	**715**	**-33%**
Other income and gains	62	27	-56%
Fair value gains on investment properties	843	1,340	59%
Finance costs	(334)	(374)	12%
Minus: Depreciation & Amortisation	(272)	(307)	13%
Profit before taxation	**1,368**	**1,401**	**2%**
Income tax	(116)	(116)	0%
Deferred tax	(238)	(377)	58%
Profit for the year	**1,013**	**907**	**-10%**
Net Profit	**1,013**	**907**	**-10%**
Reported EPS (HKD)	**0.72**	**0.53**	**-27%**
EBITDA	**1,068**	**715**	**-33%**
Net Finance Costs	N/A.	(339)	
Taxes Paid	N/A.	(111)	
FFE Reserve capitalised	N/A.	(23)	
one-off listing expenses	N/A.	73	
Share of profits of losses of JV	N/A.	(3)	
Pre-opening expenses	N/A.	207	
Distributable income (for full period)	N/A.	**519**	
Distributable income (actual, for listing period)	N/A.	***229**	
Distribution guarantee/ shortfall payment	N/A.	252	
Total distribution (for listing period)	N/A.	***481**	
DPS (HKD)	N/A.	***0.24**	
**For listing period (2 July to 31 Dec 2014) only*			
Margins			**ppt change**
SG&A ratio	28.5%	42.1%	13.7
Gross margin	58.0%	56.2%	(1.7)
Reported NP margin	38.5%	32.9%	(5.6)
Liquidity	**YE2013**	**YE2014**	**% change / ppt change**
Long-term borrowings	2,099	6,139	193%
Short-term borrowings	3,470	2,183	-37%
Cash (incl. restricted cash)	1,183	1,129	-5%
Net Debt	4,385	7,193	64%
Total equity + amount due to related parties	12,121	10,891	-10%
Net debt-to-adjusted capital ratio	36%	66%	29.9

Source: Company data, HSBC estimates

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.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

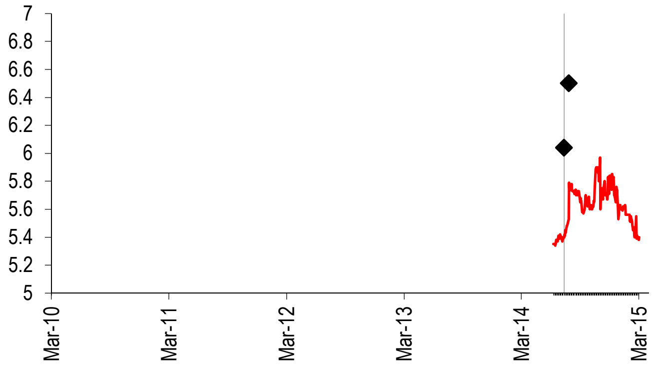
As of 25 March 2015, the distribution of all ratings published is as follows:

Buy	41%	(30% of these provided with Investment Banking Services)
Hold	39%	(28% of these provided with Investment Banking Services)
Sell	20%	(20% of these provided with Investment Banking Services)

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

Jinmao (China) Investment (6139.HK) Share Price performance HKD Vs HSBC rating history



Source: HSBC

Recommendation & price target history

From	To	Date
N/A	Overweight (V)	04 August 2014
Target Price	**Value**	**Date**
Price 1	6.04	04 August 2014
Price 2	6.50	19 August 2014

Source: HSBC

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
JINMAO (CHINA) INVESTMENTS HOL	6139.HK	5.40	25-Mar-2015	1, 5

Source: HSBC

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