

Last Closing: HK\$ 129.8

Upside: +11.7%

Target Price: HK\$ 145.00 ↑

HK Property Sector

SHKP (16 HK)

1HFY18 review; a promise worth a thousand gold

UP MP OP

Financial Highlights

Y/E 30 Jun	FY16	FY17	FY18E	FY19E	FY20E
Revenue (HK\$ m)	101,746	89,140	94,351	98,355	103,009
YoY growth (%)	29.6	(12.4)	5.8	4.2	4.7
Core profit (HK\$ m)	24,170	25,965	30,139	28,110	30,064
Core EPS (HK\$)	8.37	8.97	10.41	9.70	10.38
EPS growth (%)	18.4	7.2	16.0	(6.8)	6.9
Vs. Consensus (+/- %)			0.9	(13.6)	(15.2)
P/E (x)	15.5	14.5	12.5	13.4	12.5
DPS (HK\$)	3.850	4.100	4.300	4.500	4.700
Dividend yield (%)	2.97	3.16	3.31	3.47	3.62

Source: Company data, BOCOM Int'l estimates

- Strong headline growth led by Cullinan West.** 1HFY18 core profit rose 37% YoY to HK\$20.0bn, 19% ahead of consensus. The positive surprise came from the early booking of Cullinan West. Mainland net rental income also rose 21% YoY, helped by contribution from new malls and RMB appreciation. On the other hand, HK net rental income only posted a mild ~3% YoY organic growth, with rental reversion staying at low teens. Book value increased to HK\$181.8/share as of December 2017 (June 2017: HK\$172.0). Net gearing slightly improved to 8.5% (June 2017: 8.8%). 1HFY18 DPS rose 9% YoY to HK\$1.2. Above all, we are upbeat on the company's medium-term (MT) target of HK\$40bn annual HK property sales.
- Early recognition of HK property profit.** Cullinan West and Victoria Harbour are two high-margin projects in SHKP's landbank. Therefore, the early booking of Cullinan West helped to boost property profit by 89% YoY, with EBIT margin expanded to 40%. However, other projects' margins are still capped at ~30%, dragged by higher land costs and selling expenses, in our estimate. In addition, 1HFY18 has already accounted for 92% of FY18E completion in residential GFA, and the company might restate the FY18E booking after adopting HKFRS15. Therefore, we see the heavily front-loaded earnings as only an accounting entry.
- Good track record to override market uncertainty.** Nevertheless, we believe the MT sales target would help mitigate the uncertainty in property profit outlook, especially when SHKP has a good track record in delivering promise regardless of market condition. Its current HK residential landbank of 18m sq ft GFA could support such target, at least for the next six years, in our view. We believe this can safeguard SHKP against potential property market weakness from US rate hike, as we expect it to speed up asset turnover to deliver the sales target, even in a property market slowdown. This will also help maintain ROE in the event of margin compression, in our view. Therefore, we lift our MT forecast of HK property profit to HK\$10bn (in case of property price correction), which could rise to HK\$12bn-14bn (if market stays buoyant). We revise up our FY18-20E core profit forecasts by 8-27% accordingly.
- Continuous rental income growth despite high base.** Rental income outlook remains positive, as management guided to a steady 3-5% organic rental growth in both HK and mainland. In addition, the company still has 1.3m sq ft GFA and 4.0m sq ft GFA completing in the next three years in HK and mainland, representing 6% and 33% of existing portfolio, respectively. Major upcoming openings include Two Harbour Square in Hong Kong and ITC (Xujiahui project) in Shanghai. Together with contribution from new malls, we maintain our forecast of 5% 18-20E CAGR in net rental income.
- Upgrade to Buy.** Management intends to maintain a progressive DPS in absolute terms, supported by continuous rental income growth. Moreover, we believe the MT sales target should help to mitigate market concern about HK property market and restore investor confidence on the sustainability of SHKP's property profit, hence narrowing the NAV discount. We revise up our NAV estimate to HK\$180.7 (from HK\$171.0), to reflect the higher rents in HK CBD offices and prime shopping malls, as well as higher ASP at recent new launches. We lift our target price from HK\$120.00 to HK\$145.00, based on a 20% target NAV discount (from 30%), to reflect the faster asset turnover. We upgrade the counter from Neutral to **Buy**.



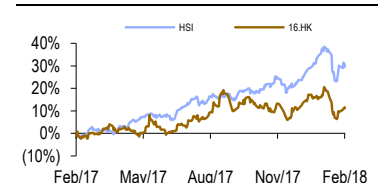
- 1H18 core profit beat consensus by 19%
- We believe the medium-term annual sales target of HK\$40bn should help mitigate market concern about overall HK property market and restore investor confidence on the earnings sustainability.
- Raise TP to HK\$145.00; upgrade to **Buy**.

Stock data

52w High (HK\$)	139.60
52w Low (HK\$)	110.8
Market cap (HK\$m)	376,019
Issued shares (m)	2,897
Avg daily vol (m)	3.94
1-mth change (%)	(6.15)
YTD change (%)	(0.46)
50d MA (HK\$)	130.10
200d MA (HK\$)	125.32
14-day RSI	55.19

Source: Company data, Bloomberg

1 Year Performance chart



Source: Company data, Bloomberg

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Figure 1: 1HFY18 results summary

HK\$ m	1HFY17	1HFY18	% YoY	Remarks
Total revenue	52,482	60,762	+15.8	
EBIT				
- HK	6,691	12,671	+89.4	1HFY18 accounted for 92% of FY18 residential GFA completion
- China	1,644	1,224	-25.5	Expect mainland property profit to stay low, with 1 HFY18 contracted sales at only RMB2bn
- Singapore	10	-	NM	
Property sales	8,345	13,895	+66.5	
- HK	6,669	6,973	+4.6	Organic rental growth ~3% YoY
- China	1,369	1,651	+20.6	
- Singapore	235	267	+13.6	
Rental income	8,273	8,891	+7.5	
Hotel operation	735	776	+5.6	
Telecommunications	527	453	-14.0	
Transportation, infrastructure and logistics	823	952	+15.7	
Other businesses	894	910	+1.8	
Other income	679	677	-0.3	
Overhead	(618)	(681)	+10.2	
EBIT total	19,658	25,873	+31.6	
IP reval gain	7,137	14,259	+99.8	
Finance cost	(1,111)	(970)	-12.7	
Tax	(4,610)	(5,683)	+23.3	
MI & PCS	(415)	(448)	+8.0	
Net profit	20,659	33,479	+62.1	
Core profit	14,608	19,973	+36.7	
Core EPS (HK\$)	5.05	6.90	+36.6	
DPS (HK\$)	1.10	1.20	+9.1	
- payout (%)	21.8	17.4	-4.4ppt	
BVPS (HK\$)	164.7	181.8	+10.4	
Net gearing (%)	8.8	8.5	-0.3ppt	
HK Prop sales margin (%)	34.8	39.9	+5.1ppt	Est. >45% margin at Cullinan West, versus ~30% at other projects
Mainland Prop sales margin (%)	23.9	43.4	+19.5ppt	
HK net rental margin (%)	77.2	77.4	+0.2ppt	
Mainland net rental margin (%)	74.5	77.1	+2.6ppt	

Source: Company data, BOCOM Int'l

Figure 2: SHKP: Earnings revision

	Old	New	% change
Core profit - FY18E (HK\$ m)	23,753	30,139	26.9
Core profit - FY19E (HK\$ m)	25,960	28,110	8.3
Core profit - FY20E (HK\$ m)	27,539	30,064	9.2
Core EPS - FY18E (HK\$)	8.202	10.409	26.9
Core EPS - FY19E (HK\$)	8.964	9.704	8.3
Core EPS - FY20E (HK\$)	9.509	10.378	9.1
DPS - FY18E (HK\$)	4.3	4.3	-
DPS - FY19E (HK\$)	4.5	4.5	-
DPS - FY20E (HK\$)	4.7	4.7	-

Source: BOCOM Int'l estimates

Figure 3: SHKP: NAV summary

	NAV (HK\$ m)	% of GAV (%)	NAV/ share (HK\$)
HK residential	126,577	20.6	43.7
HK office / retail	321,479	52.3	111.0
HK hotels	35,910	5.8	12.4
China residential	15,456	2.5	5.3
China office / retail	43,229	7.0	14.9
China hotels	2,581	0.4	0.9
HK farmland	8,400	1.4	2.9
Overseas properties	3,838	0.6	1.3
Smartone (62 HK, 65.2%)	6,207	1.0	2.1
Other investment	20,232	3.3	7.0
Cash	31,274	5.1	10.8
GAV	615,183	100.0	212.4
Total borrowings	(67,326)		(23.2)
Other borrowings	(24,514)		(8.5)
NAV	523,343		180.7
NAV (HK\$)	180.7		
Target price (HK\$)	145.0		
- Target discount (%)	20.0		

Source: BOCOM Int'l estimates

Company background

Sun Hung Kai Properties (SHKP) is now one of the largest property companies in Hong Kong. It earns its brand name by its premium quality, and offers a wide range of product from mass-market to luxury-end. SHKP is also the biggest landlord in town with over 29.8m sqft GFA of completed investment properties in Hong Kong, as of December 2017. Landmark buildings, e.g. IFC and ICC, mark the most prestige commercial properties in Hong Kong. The company also invests in Telecommunications, Information technology and Infrastructure, which accounts for less than 5% of its asset value in our estimates, but provide a recurrent income over the long term.

SHKP (16 HK): Financial Statements

Profit & loss (HK\$ m)

Year ended 30 Jun	2016	2017	2018E	2019E	2020E
Total revenue	101,746	89,140	94,351	98,355	103,009
Property sales	11,701	11,917	15,498	11,476	11,901
Rental income	16,481	17,142	18,185	19,794	21,387
Hotel operation	1,259	1,325	1,462	1,503	1,583
Other businesses	4,299	4,306	4,667	4,819	4,975
Other income	763	927	1,143	908	936
Unallocated expenses	(1,320)	(1,402)	(1,376)	(1,431)	(1,489)
EBIT	33,183	34,215	39,579	37,069	39,293
IP revaluation gain	9,998	18,205	16,773	5,067	5,118
Finance cost	(2,418)	(2,096)	(1,973)	(1,706)	(1,493)
Taxation	(7,367)	(7,849)	(8,472)	(7,331)	(7,798)
PCS	(18)	(18)	(174)	(174)	(174)
Minority interests	(730)	(675)	(499)	(709)	(735)
Net profit	32,666	41,782	45,234	32,215	34,210
Core profit	24,170	25,965	30,139	28,110	30,064
Dividend	11,144	11,292	12,456	13,035	13,615

Balance sheet (HK\$ m)

As of 30 Jun	2016	2017	2018E	2019E	2020E
Cash and equivalent	30,048	31,274	33,342	36,128	41,091
Properties for sale	144,844	146,409	146,838	147,173	147,445
Debtors, prepayments and others	25,024	17,813	25,921	26,442	26,973
Others	1,714	1,242	888	888	888
Current asset	201,630	196,738	206,989	210,631	216,397
Investment properties	318,517	337,980	344,383	347,836	351,323
Fixed assets	25,446	26,977	33,617	34,975	36,388
Asso&Jces	60,807	63,841	69,790	72,739	75,729
Loan receivables	1,035	4,981	4,986	4,986	4,986
Others	7,080	8,899	8,456	8,456	8,456
Non-current assets	412,885	442,678	461,232	468,992	476,882
Total asset	614,515	639,416	668,221	679,622	693,279
Trade and other payables	27,493	26,908	31,236	32,498	33,811
Presale deposits	6,976	10,458	6,809	6,995	7,181
Bank and other borrowings	17,486	5,390	9,666	8,600	7,271
Taxation	7,116	8,216	8,027	7,699	8,145
Current liabilities	59,071	50,972	55,738	55,793	56,408
LT borrowings	63,275	61,936	46,670	37,736	29,065
Deferred tax liabilities	17,410	18,930	21,028	21,597	22,173
Others	251	215	188	188	188
Non-current liabilities	80,936	81,081	67,886	59,521	51,426
Issued capital	70,384	70,516	70,582	70,582	70,582
Retained earnings and reserve	390,217	419,592	455,712	474,892	495,487
Proposed dividend	8,106	8,107	8,980	9,270	9,559
Shareholders fund	468,707	498,215	535,274	554,744	575,629
PCS	-	3,910	3,910	3,910	3,910
Minority interest	5,801	5,238	5,413	5,655	5,907
Total Equity	474,508	507,363	544,597	564,308	585,446

Source: Company data, BOCOM Int'l estimates

Cash flow (HK\$ m)

Year ended 30 Jun	2016	2017	2018E	2019E	2020E
EBITDA	24,728	25,463	36,679	34,763	36,868
Change in working capital	(9,803)	7,876	2,217	727	767
Interest paid	(2,574)	(2,366)	(2,146)	(1,673)	(1,362)
TAX	(5,038)	(3,817)	(6,004)	(6,027)	(5,699)
Others	5,409	5,440	-	-	-
CFO	12,722	32,596	30,745	27,790	30,574
Interest & dividend received	2,862	3,261	2,814	1,520	1,563
Capex	(6,954)	(11,699)	(8,594)	(3,312)	(3,367)
Proceeds from disposal	450	3,187	-	-	-
Acquisitions / investments	(1,350)	(348)	-	-	-
Other Items (+/-)	(578)	(3,813)	-	-	-
CFI	(5,570)	(9,412)	(5,780)	(1,792)	(1,804)
Issue of new shares	1,910	112	-	-	-
Net new borrowings	(1,147)	(13,249)	(10,990)	(10,000)	(10,000)
Dividend paid	(9,982)	(11,292)	(11,583)	(12,746)	(13,325)
Others	(48)	2,552	(325)	(467)	(483)
CFF	(9,267)	(21,877)	(22,898)	(23,212)	(23,808)
Change in net cash	(2,115)	1,307	2,068	2,786	4,962
FX	(398)	(81)	-	-	-
Total cash	30,048	31,274	33,342	36,128	41,091
(Increase)/decrease in net debt	142	(14,661)	(13,058)	(12,786)	(14,962)
Net (debt)/cash	50,713	36,052	22,994	10,208	(4,755)

Key ratio

Year ended 30 Jun	2016	2017	2018E	2019E	2020E
Revenue growth (% YoY)	29.6	(12.4)	5.8	4.2	4.7
EBIT growth (% YoY)	20.2	3.1	15.7	(6.3)	6.0
Core profit growth (% YoY)	21.9	7.4	16.1	(6.7)	6.9
EBIT margin (%)	32.6	38.4	41.9	37.7	38.1
Core net margin (%)	23.8	29.1	31.9	28.6	29.2
ROE (%)	5.3	5.4	5.8	5.2	5.3
ROA (%)	4.4	4.5	4.9	4.4	4.6
Core EPS (HK\$)	8.370	8.970	10.409	9.704	10.378
BVPS (HK\$)	161.90	172.02	184.78	191.51	198.72
DPS (HK\$)	3.850	4.100	4.300	4.500	4.700
Payout ratio (%)	46.1	43.5	41.3	46.4	45.3
Core P/E (x)	15.5	14.5	12.5	13.4	12.5
P/B (x)	0.8	0.8	0.7	0.7	0.7
Yield (%)	3.0	3.2	3.3	3.5	3.6
Net gearing/(cash) (%)	10.8	7.2	4.3	1.8	(0.8)
NOSH (million)	2,895	2,896	2,897	2,897	2,897

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Rating System

Analyst Stock Ratings:

Buy: The stock's total return is expected to **exceed** that of the corresponding industry over the next 12 months.

Neutral: The stock's total return is expected to be **in line with** that of the corresponding industry over the next 12 months.

Sell: The stock's total return is expected to be **below** that of the corresponding industry over the next 12 months.

Not-Rated: The analyst **does not have conviction** regarding the outlook of the stock's total return relative to that of the corresponding industry over the next 12 months.

Trading Buy: The stock's **absolute** return is expected to be **very attractive** in the near term. This rating can be different from the rating with a view over the next 12 months.

Trading Sell: The stock's **absolute** return is expected to be **very unattractive** in the near term. This rating can be different from the rating with a view over the next 12 months.

Analyst Industry Views:

Outperform: The analyst expects the industry coverage universe to be **attractive** relative to the relevant broad market benchmark over the next 12 months.

Market perform: The analyst expects the industry coverage universe to be **in line with** the relevant broad market benchmark over the next 12 months.

Underperform: The analyst expects the industry coverage universe to be **unattractive** relative to the relevant broad market benchmark over the next 12 months.

Broad market benchmark for Hong Kong is **the Hang Seng Composite Index**, for China A-shares is the **MSCI China A Index**, for US-listed Chinese companies is **S&P US Listed China 50 (USD) Index**.

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