

# Zhenro Properties | 6158 HK

## Financial upgrade completed, operational upgrade continues

### ► Earnings miss but financial position improves

### ► Steady improvement overall since listing

**Earnings miss but financial position improves.** Zhenro's FY19 results for dividend and core profit came in below our expectations. Dividend for the year declined 33% to HK\$0.1, with the payout ratio down 10ppt to 17%. Core profit grew 20% to RMB2.3b, 14% short of our estimate dragged by lower GPM. GPM declined 3ppt to 20% due to the recognition of inventory projects with low ASP. Profit from JVs & associates turned positive to contribute 23% of core profit, offset by higher profit shared with MI and perpetual shareholders. Zhenro has set a sales target of RMB140b, implying 7% YoY growth or 15% YoY on an attributable basis (55% attribution versus 51% in 2018). Saleable resources for 2020F amounted to RMB250b, implying sell-through of 64%. Zhenro replenished 5.6m sqm of landbank with a much higher attribution ratio of 73% compared with 33% in 2018.

**Notable financial improvement.** Since its listing in 2018, Zhenro's fundamentals have improved steadily to the point now where we believe the stock is due for an upgrade by the market. Net gearing, including perpetual securities and ABS, has shown notable 19ppt improvement to 95% in 2019. Short-term debt for FY19 was 1.8x covered by cash-on-hand, accounting for 34% of total debt at end-Dec 2019 compared with 51% at end-Dec 2018. Zhenro's financial structure has also improved, with trust loans accounting for 20% of total loans at end-Dec 2019 versus 36% at end-Dec 2018, mainly replaced by longer duration and lower cost bonds and syndicated loans, which saw average financing cost at Zhenro fall 3ppt to 7.5% in 2019.

**Steady improvement overall since listing.** We expect management to focus on upgrading the company's operations beginning in 2020F. This would entail raising the attribution ratio to 55% for 2020 contracted sales compared with 51% in 2019, and bringing GPM back up to 22%. We cut our 2020F/2021F core profit forecast by 25%/33% to reflect slower recognitions and lower GPM. Our target price of HK\$5.63 is based on a 55% discount to NAV as we expect margin for newly acquired landbank to offset lower-than-expected margin for existing landbank. Key risks to our Outperform rating include a further economic slowdown and overly aggressive land banking.

### Forecast and valuation

Year to 31 Dec	2018	2019	2020F	2021F	2022F
Revenue (RMB m)	26,453	32,558	37,008	43,545	50,172
YoY (%)	32.3	23.1	13.7	17.7	15.2
Net profit (RMB m)	1,921	2,312	2,857	3,494	4,124
YoY (%)	67.9	20.4	23.5	22.3	18.0
Fully diluted EPS (RMB)	0.5	0.5	0.7	0.8	0.9
YoY (%)	22.2	17.4	19.6	22.3	18.0
P/E (x)	8.3	7.4	6.7	5.5	4.6
DPS (RMB)	0.13	0.09	0.11	0.14	0.16
Dividend yield (%)	3.0	2.1	2.6	3.3	3.7
P/B (x)	1.2	1.2	1.0	0.9	0.8
ROAE (%)	10.5	8.3	8.8	9.7	10.3
Net debt/equity (%)	87.5	86.0	81.9	81.4	82.4

Source: Bloomberg, CCBIS estimates

## Outperform (maintained)

Current price:

**HK\$4.86**

(as at 30 Mar 2020)

Target:

**► HK\$5.63**

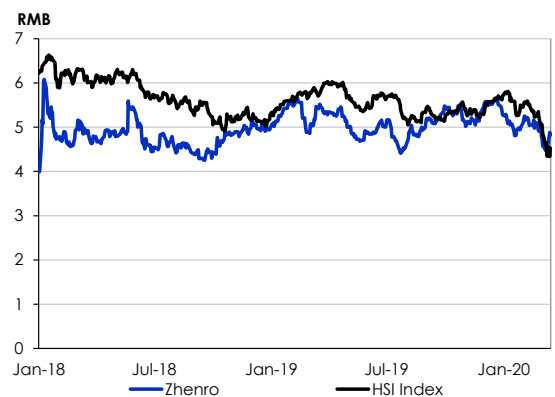
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### Trading data

52-week range	HK\$4.19-5.77
Market capital (ordinary)(m)	US\$2,744
Shares outstanding (m)	4,368
Free float (%)	29
3M average daily T/O (m share)	7
3M average daily T/O (US\$ m)	5
Expected 12-month return (%)	16

Source: Bloomberg, CCBIS estimates

### Share price vs HSI



Source: Bloomberg

### Stock performance

Performance over	1M	3M	12M
Absolute	1	9	-17
Relative (%) to HSI	-5	4	-22

Source: Bloomberg

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## Zhenro Properties – results analysis

RMB m	2018	2019	YoY (%)	2019F	Variance (%)
Property sales	26,179	32,185	22.9	32,440	-0.8
Rental income	105	134	28.1	136	-1.4
Property management	57	85	51.0	74	16.2
Other	112	153	36.5	146	5.0
<b>Revenue</b>	<b>26,453</b>	<b>32,558</b>	<b>23.1</b>	<b>32,796</b>	<b>-0.7</b>
Cost of sales	(20,432)	(26,060)	27.5	(25,215)	3.3
<b>Gross profit</b>	<b>6,021</b>	<b>6,498</b>	<b>7.9</b>	<b>7,581</b>	<b>-14.3</b>
Selling expenses	(877)	(972)	10.9	(1,148)	-15.3
Administrative expenses	(985)	(1,214)	23.3	(1,312)	-7.4
Other	282	372	31.7	(54)	-789.6
<b>Operating profit</b>	<b>4,442</b>	<b>4,683</b>	<b>5.4</b>	<b>5,067</b>	<b>-7.6</b>
Finance cost	(381)	(484)	26.9	(332)	46.0
JVs and associates	(158)	521	N/A	365	42.7
<b>Profit before tax</b>	<b>3,902</b>	<b>4,720</b>	<b>20.9</b>	<b>5,101</b>	<b>-7.5</b>
Tax	(1,870)	(1,820)	-2.7	(1,832)	-0.7
<b>Core profit – consolidated</b>	<b>2,032</b>	<b>2,900</b>	<b>42.7</b>	<b>3,269</b>	<b>-11.3</b>
Minority interest and perpetuals	(112)	(588)	425.5	(573)	2.5
<b>Core profit</b>	<b>1,921</b>	<b>2,312</b>	<b>20.4</b>	<b>2,696</b>	<b>-14.2</b>
One-off items	200	194	-3.1		
<b>Reported earnings</b>	<b>2,121</b>	<b>2,506</b>	<b>18.2</b>		
<b>Dividend per share (HK\$)</b>	<b>0.150</b>	<b>0.100</b>	<b>-33.3</b>	<b>0.183</b>	<b>-45.5</b>
<b>Ratios</b>	<b>2018</b>	<b>2019</b>	<b>YoY (%)</b>	<b>2019F</b>	<b>ppt cig</b>
Gross margin (%)	22.8	20.0	-2.8	23.1	-3.2
SG&A/revenue (%)	7.0	6.7	-0.3	7.5	-0.8
LAT/revenue (%)	4.0	2.7	-1.3	2.7	0.0
Effective tax rate (%)	27.3	28.5	1.2	25.0	3.5
JV/core profit (%)	-8.2	22.5	30.8	13.5	9.0
MI/Perps/core profit (%)	5.7	24.7	19.0	21.9	2.8
Core margin - consolidated (%)	8.3	7.3	-1.0	8.9	-1.5
Core margin (%)	7.3	7.1	-0.2	8.2	-1.1
NOS – year-end (m shares)	4,123	4,368	5.9	4,368	0.0
Net gearing (%)	74.0	75.2	1.2	72.5	2.7
Net gearing - perps/ABS as debt (%)	113.7	95.0	-18.7	127.9	-32.9
Dividend payout (%)	27.5	17.2	-10.3	27.0	-9.9

Source: Company, CCBIS estimate

## Zhenro Properties – earnings changes

	2020F	2021F
Revenue – old (RMB m)	42,464	55,386
Revenue – new (RMB m)	37,008	43,545
Change (%)	-12.8	-21.4
GPM – old (%)	23.1	23.1
GPM – new (%)	22.0	22.8
Change (ppt)	-1.1	-0.3
Core profit – old (RMB m)	3,950	5,318
Core profit – new (RMB m)	2,959	3,541
Change (%)	-25.1	-33.4

Source: CCBIS estimate

## Zhenro Properties | 6158 HK – financial summary

### Profit and loss

FYE 31 Dec (RMB m)	2018	2019	2020F	2021F	2022F
Property development	26,179	32,185	36,523	42,915	49,352
Rental income	105	134	175	227	295
Property agency/mgmt	57	85	111	144	188
Other	112	153	199	259	337
<b>Revenue</b>	<b>26,453</b>	<b>32,558</b>	<b>37,008</b>	<b>43,545</b>	<b>50,172</b>
COGS	(20,432)	(26,060)	(29,531)	(34,555)	(39,636)
<b>Gross profit</b>	<b>6,021</b>	<b>6,498</b>	<b>7,478</b>	<b>8,990</b>	<b>10,536</b>
Other income	327	471	–	–	–
Operating expenses	(1,907)	(2,286)	(2,605)	(3,068)	(3,542)
<b>EBIT</b>	<b>4,442</b>	<b>4,683</b>	<b>4,873</b>	<b>5,922</b>	<b>6,994</b>
Net financial income (exp.)	(381)	(484)	(494)	(541)	(585)
JVs and associates	(158)	521	900	1,080	1,296
Other	200	194	–	–	–
<b>Profit before tax</b>	<b>4,103</b>	<b>4,914</b>	<b>5,278</b>	<b>6,462</b>	<b>7,705</b>
Tax	(1,870)	(1,820)	(1,770)	(1,991)	(2,713)
<b>Total profit</b>	<b>2,233</b>	<b>3,094</b>	<b>3,508</b>	<b>4,471</b>	<b>4,992</b>
Minority interest	(112)	(588)	(651)	(977)	(869)
<b>Net profit attributable to shareholders</b>	<b>2,121</b>	<b>2,506</b>	<b>2,857</b>	<b>3,494</b>	<b>4,124</b>
Extraordinary items	200	194	–	–	–
<b>Core profit</b>	<b>1,921</b>	<b>2,312</b>	<b>2,857</b>	<b>3,494</b>	<b>4,124</b>
Reported EPS (RMB)	0.00	0.00	0.00	0.00	0.00
Diluted EPS (RMB)	0.51	0.59	0.65	0.80	0.94
Core EPS (RMB)	0.47	0.55	0.65	0.80	0.94
Dividend (RMB m)	528	397	490	625	698
Dividend per share (RMB)	0.13	0.09	0.11	0.14	0.16

### Cash flow

FYE 31 Dec (RMB m)	2018	2019	2020F	2021F	2022F
<b>Profit before tax</b>	<b>4,103</b>	<b>4,914</b>	<b>5,278</b>	<b>6,462</b>	<b>7,705</b>
Amortization & depreciation	34	35	37	39	41
Net financial charge adj.	381	484	494	541	585
Change in working capital	(2,187)	(5,781)	1,246	(426)	(589)
Tax paid	(1,539)	(1,820)	(1,770)	(1,991)	(2,713)
Other	(3,455)	(1,199)	(1,394)	(1,621)	(1,881)
<b>Operating cash flow</b>	<b>(2,664)</b>	<b>(3,366)</b>	<b>3,891</b>	<b>3,004</b>	<b>3,148</b>
Disposal of fixed assets	1	3,368	–	–	–
Capex	(420)	(600)	(600)	(600)	(600)
Investment	(2,742)	(3,291)	(3,949)	(4,739)	(5,687)
Other	(359)	–	–	–	–
<b>Investment cash flow</b>	<b>(3,521)</b>	<b>(523)</b>	<b>(4,549)</b>	<b>(5,339)</b>	<b>(6,287)</b>
Change in borrowings	(2,100)	5,000	5,000	8,000	5,000
Equity issues	3,588	1,055	–	–	–
Dividend paid	(330)	(528)	(397)	(490)	(625)
Other	12,943	4,192	(129)	(129)	(129)
<b>Financing cash flow</b>	<b>14,102</b>	<b>9,719</b>	<b>4,474</b>	<b>7,380</b>	<b>4,246</b>
<b>Change in cash flow</b>	<b>7,917</b>	<b>5,830</b>	<b>3,816</b>	<b>5,046</b>	<b>1,107</b>
Cash & equivalents, begin	14,539	22,539	28,369	32,185	37,231
Forex	82	–	–	–	–
<b>Cash &amp; equivalents, end</b>	<b>22,539</b>	<b>28,369</b>	<b>32,185</b>	<b>37,231</b>	<b>38,338</b>
<b>Free cash flow</b>	<b>4,218</b>	<b>8,165</b>	<b>1,429</b>	<b>3,963</b>	<b>4,562</b>

Source: Company data, CCBIS estimates

### Balance sheet

FYE 31 Dec (RMB m)	2018	2019	2020F	2021F	2022F
Cash and equivalents	28,369	35,307	39,123	44,169	45,276
Receivables	12,790	13,600	19,600	25,600	31,600
Property under dev'ment	75,776	94,006	107,834	125,283	142,852
Other current assets	9,710	8,605	8,605	8,605	8,605
<b>Total current assets</b>	<b>126,644</b>	<b>151,518</b>	<b>175,163</b>	<b>203,658</b>	<b>228,334</b>
PPE/investment property	1,091	970	1,533	2,094	2,653
Intangible assets	10	7	7	7	7
JVs and associates	3,729	5,542	10,391	16,210	23,192
Other non-current assets	9,926	11,183	11,183	11,183	11,183
<b>Total non-current assets</b>	<b>14,755</b>	<b>17,701</b>	<b>23,113</b>	<b>29,493</b>	<b>37,035</b>
<b>Total assets</b>	<b>141,399</b>	<b>169,219</b>	<b>198,276</b>	<b>233,151</b>	<b>265,369</b>
Short-term borrowings	23,839	21,065	23,565	27,565	30,065
Presale deposit	60,812	65,098	86,173	109,196	132,176
Other current liabilities	5,631	10,283	10,283	10,283	10,283
<b>Total current liabilities</b>	<b>90,282</b>	<b>96,446</b>	<b>120,021</b>	<b>147,044</b>	<b>172,524</b>
Long-term borrowings	25,938	40,947	43,447	47,447	49,947
Other non-current liabilities	700	766	766	766	766
<b>Total non-current liabilities</b>	<b>26,638</b>	<b>41,713</b>	<b>44,213</b>	<b>48,213</b>	<b>50,713</b>
<b>Total liabilities</b>	<b>116,920</b>	<b>138,159</b>	<b>164,234</b>	<b>195,258</b>	<b>223,238</b>
Reserves & retained profits	13,529	16,396	18,856	21,860	25,359
<b>Shareholders' equity</b>	<b>16,537</b>	<b>17,836</b>	<b>20,296</b>	<b>23,300</b>	<b>26,799</b>
Minority interest	7,942	13,224	13,746	14,593	15,333
<b>Total equity</b>	<b>24,479</b>	<b>31,060</b>	<b>34,042</b>	<b>37,893</b>	<b>42,131</b>
<b>Total equity and liabilities</b>	<b>141,399</b>	<b>169,219</b>	<b>198,276</b>	<b>233,151</b>	<b>265,369</b>

### Ratios

FYE 31 Dec	2018	2019	2020F	2021F	2022F
<b>Growth (%)</b>					
Revenue	32.3	23.1	13.7	17.7	15.2
EBITDA	46.8	5.4	4.1	21.4	18.0
EBIT	46.8	5.4	4.1	21.5	18.1
Net profit	50.5	18.2	14.0	22.3	18.0
Core net profit	67.9	20.4	23.5	22.3	18.0
<b>Profitability (%)</b>					
Gross margin	22.8	20.0	20.2	20.6	21.0
EBITDA margin	16.9	14.5	13.3	13.7	14.0
EBIT margin	16.8	14.4	13.2	13.6	13.9
Net margin	8.0	7.7	7.7	8.0	8.2
Core net margin	7.3	7.1	7.7	8.0	8.2
Tax rate	45.6	37.0	33.5	30.8	35.2
<b>Interest coverage (x)</b>					
EBIT coverage	1.0	0.9	0.9	1.0	1.1
Cash coverage	6.1	7.0	7.6	7.8	7.4
Cash to short-term debt	1.2	1.7	1.7	1.6	1.5
<b>Returns &amp; leverage (%)</b>					
ROAA	1.5	1.5	1.6	1.6	1.7
ROAE	10.5	8.3	8.8	9.7	10.3
ST debt to total debt	0.5	0.3	0.4	0.4	0.4
Payout ratio	24.9	15.3	17.2	17.9	16.9
<b>Liquidity (x)</b>					
Current ratio	1.4	1.6	1.5	1.4	1.3
Quick ratio	0.6	0.6	0.6	0.5	0.5

**Rating definitions:****Outperform (O) – expected return > 10% over the next twelve months****Neutral (N) – expected return between -10% and 10% over the next twelve months****Underperform (U) – expected return < -10% over the next twelve months****Analyst certification:**

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