

# Sun Hung Kai Properties (0016.HK)

Earnings Review: FY18 results in line with expectations: 13% DPS hike plus ample capacity to sustain earnings delivery; CL-Buy

BUY CL

0016.HK 12m Price Target: **HK\$168.00** Price: **HK\$114.70** Upside: **46.5%**

## SHKP reported an in-line set of results for FY2018, with the following highlights:

- Underlying profit reached a record level of HK\$30.4bn, up 17% yoy, versus our forecast of HK\$30bn.
- Development profit at HK\$16.3bn, up 36% yoy.
- Attr. net rental profit at HK\$18.6bn, up 9% yoy.
- DPS at HK\$4.65/share, up 13% yoy (vs. 1H FY18's +9%), above our forecasts of HK\$4.40/share.
- BVPS at HK\$186.1, up 8.2% yoy, with IP book value at HK\$369bn, or HK\$127.5/share.

## Key takeaways from the analyst briefing

- HK residential sales:**
  - SHKP completed HK\$41bn contracted sales during the fiscal year, ahead of its target of HK\$36bn, and of which HK\$29bn has yet to be recognized. FY19-to-date (i.e. c.2.5 months), SHKP achieved another HK\$26bn of contracted sales (or c.2,000 units).
  - The company sees their development pipeline as sizable enough to sustain for 5-6 years and with a relatively low average land cost, reiterated their medium-term average HK\$40bn p.a. contracted sales target (first announced in early 2018).
- Farm land conversion:**
  - They are actively pursuing farm land conversion for land banking given keen competition in public tender market, and guided for two sites currently at advanced stage of the conversion progress.

**Justin Kwok, CFA**  
+852-2978-0481 | justin.kwok@gs.com  
Goldman Sachs (Asia) L.L.C.

**Colin Yao**  
+852-2978-1474 | colin.yao@gs.com  
Goldman Sachs (Asia) L.L.C.

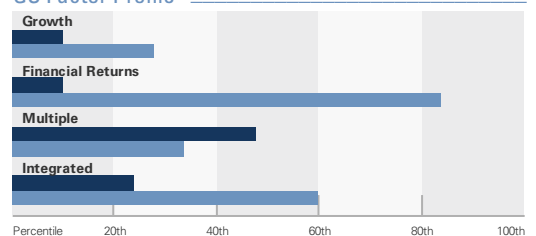
## Key Data

Market cap: HK\$308.9bn / \$39.4bn  
Enterprise value: HK\$404.7bn / \$51.6bn  
3m ADTV: HK\$349.8mn / \$44.6mn  
Hong Kong  
Hong Kong Property  
M&A Rank: 3  
Asia ex. Japan Conviction List

## GS Forecast

	6/18	6/19E	6/20E	6/21E
<b>Revenue (HK\$ mn) New</b>	<b>85,644.0</b>	<b>107,375.0</b>	<b>107,502.2</b>	<b>124,225.1</b>
Revenue (HK\$ mn) Old	79,463.3	105,599.6	105,670.8	-
EBITDA (HK\$ mn)	37,460.0	37,132.6	36,915.2	37,111.6
<b>EPS (HK\$) New</b>	<b>17.24</b>	<b>11.13</b>	<b>11.24</b>	<b>11.76</b>
EPS (HK\$) Old	10.37	10.97	11.22	-
P/E (X)	7.4	10.3	10.2	9.8
P/B (X)	0.7	0.6	0.6	0.6
Dividend yield (%)	3.7	4.3	4.6	4.8
FCF yield (%)	(7.8)	(4.2)	5.4	9.6
	<b>12/17</b>	<b>6/18</b>	--	--
EPS (HK\$)	11.40	5.84	-	-

## GS Factor Profile



■ 0016.HK relative to Asia ex. Japan Coverage  
■ 0016.HK relative to Hong Kong Property

Source: Company data, Goldman Sachs Research estimates. See disclosures for details.

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## Sun Hung Kai Properties (0016.HK)

Rating since Jul 20, 2012

### Ratios & Valuation

	6/18	6/19E	6/20E	6/21E
P/E (X)	7.4	10.3	10.2	9.8
P/B (X)	0.7	0.6	0.6	0.6
FCF yield (%)	(7.8)	(4.2)	5.4	9.6
EV/EBITDA (X)	11.7	11.5	11.4	10.7
CROCI (%)	6.8	5.1	4.9	4.9
ROE (%)	9.7	5.9	5.8	5.8
Net debt/equity (%)	11.9	15.8	14.0	9.8
Interest cover (X)	17.9	11.8	10.7	10.5
Days inventory outst, sales	691.8	573.6	545.3	456.2
Receivable days	81.7	69.8	69.7	60.3
Days payable outstanding	307.5	207.7	185.8	145.2
DuPont ROE (%)	9.1	5.7	5.6	5.6
Turnover (X)	0.1	0.1	0.1	0.2
Leverage (X)	1.3	1.3	1.3	1.3

### Growth & Margins (%)

	6/18	6/19E	6/20E	6/21E
Total revenue growth	9.5	25.4	0.1	15.6
EBITDA growth	19.1	(0.9)	(0.6)	0.5
EPS growth	19.5	(35.5)	1.0	4.6
DPS growth	13.4	6.5	6.1	5.7
EBIT margin	41.4	32.7	32.4	28.2
EBITDA margin	43.7	34.6	34.3	29.9
Net income margin	58.5	30.0	30.3	27.4

### Price Performance



Source: FactSet. Price as of 13 Sep 2018 close.

### Income Statement (HK\$ mn)

	6/18	6/19E	6/20E	6/21E
Total revenue	85,644.0	107,375.0	107,502.2	124,225.1
Cost of goods sold	(47,834.0)	(69,882.0)	(70,215.6)	(86,731.0)
SG&A	(1,506.0)	(1,551.2)	(1,597.7)	(1,645.6)
R&D	-	-	-	-
Other operating inc./exp.)	1,156.0	1,190.7	1,226.4	1,263.2
ESO expense	-	-	-	-
<b>EBITDA</b>	<b>37,460.0</b>	<b>37,132.6</b>	<b>36,915.2</b>	<b>37,111.6</b>
Depreciation & amortization	(2,007.0)	(2,025.5)	(2,046.2)	(2,066.4)
<b>EBIT</b>	<b>35,453.0</b>	<b>35,107.1</b>	<b>34,869.0</b>	<b>35,045.3</b>
Net interest inc./exp.)	(1,617.0)	(2,648.2)	(2,944.8)	(2,942.1)
Income/(loss) from associates	9,748.0	3,531.5	4,153.8	5,663.2
<b>Pre-tax profit</b>	<b>59,356.0</b>	<b>38,999.1</b>	<b>39,394.2</b>	<b>41,091.0</b>
Provision for taxes	(8,402.0)	(6,186.4)	(6,152.3)	(6,186.5)
Minority interest	(829.0)	(577.9)	(683.7)	(846.4)
Preferred dividends	-	-	-	-
<b>Net inc. (pre-exceptionals)</b>	<b>50,125.0</b>	<b>32,234.8</b>	<b>32,558.2</b>	<b>34,058.0</b>
Post-tax exceptionals	(174.0)	-	-	-
<b>Net inc. (post-exceptionals)</b>	<b>49,951.0</b>	<b>32,234.8</b>	<b>32,558.2</b>	<b>34,058.0</b>
<b>EPS (basic, pre-exception) (HK\$)</b>	<b>17.30</b>	<b>11.13</b>	<b>11.24</b>	<b>11.76</b>
<b>EPS (diluted, pre-exception) (HK\$)</b>	<b>17.30</b>	<b>11.13</b>	<b>11.24</b>	<b>11.76</b>
<b>EPS (basic, post-exception) (HK\$)</b>	<b>17.24</b>	<b>11.13</b>	<b>11.24</b>	<b>11.76</b>
<b>EPS (diluted, post-exception) (HK\$)</b>	<b>17.24</b>	<b>11.13</b>	<b>11.24</b>	<b>11.76</b>
<b>EPS (diluted, excl. ESO) (HK\$)</b>	<b>--</b>	<b>--</b>	<b>--</b>	<b>--</b>
DPS (HK\$)	4.65	4.95	5.25	5.55

### Balance Sheet (HK\$ mn)

	6/18	6/19E	6/20E	6/21E
Cash & cash equivalents	26,095.0	24,392.7	22,582.1	40,423.5
Accounts receivable	20,521.0	20,521.0	20,521.0	20,521.0
Inventory	177,807.0	159,673.5	161,546.4	148,969.7
Other current assets	859.0	859.0	859.0	859.0
<b>Total current assets</b>	<b>225,282.0</b>	<b>205,446.3</b>	<b>205,508.5</b>	<b>210,773.1</b>
Net PP&E	388,193.0	441,142.5	447,096.4	453,030.0
Net intangibles	4,976.0	4,976.0	4,976.0	4,976.0
Total investments	75,151.0	75,177.4	75,199.2	75,251.0
Other long-term assets	21,884.0	23,909.5	25,955.6	28,022.0
<b>Total assets</b>	<b>715,486.0</b>	<b>750,651.7</b>	<b>758,735.7</b>	<b>772,052.1</b>
Accounts payable	43,238.0	36,299.2	35,197.5	33,825.6
Short-term debt	12,646.0	9,716.0	20,027.0	20,027.0
Other current liabilities	10,551.0	11,420.1	12,289.2	13,158.3
<b>Total current liabilities</b>	<b>66,435.0</b>	<b>57,435.3</b>	<b>67,513.7</b>	<b>67,010.9</b>
Long-term debt	78,788.0	104,480.8	84,453.8	79,447.1
Other long-term liabilities	21,831.0	21,831.0	21,831.0	21,831.0
Total long-term liabilities	100,619.0	126,311.8	106,284.8	101,278.1
<b>Total liabilities</b>	<b>167,054.0</b>	<b>183,747.1</b>	<b>173,798.5</b>	<b>168,288.9</b>
<b>Preferred shares</b>	<b>3,887.0</b>	<b>3,887.0</b>	<b>3,887.0</b>	<b>3,887.0</b>
<b>Total common equity</b>	<b>539,098.0</b>	<b>556,992.7</b>	<b>574,341.6</b>	<b>592,321.2</b>
<b>Minority interest</b>	<b>5,447.0</b>	<b>6,024.9</b>	<b>6,708.6</b>	<b>7,555.0</b>
<b>Total liabilities &amp; equity</b>	<b>715,486.0</b>	<b>750,651.7</b>	<b>758,735.7</b>	<b>772,052.1</b>
<b>Net debt, adjusted</b>	<b>69,226.0</b>	<b>93,691.1</b>	<b>85,785.7</b>	<b>62,937.6</b>
Average capital employed	578,593.0	635,239.8	661,772.2	664,824.8
RNAV	641,031.6	647,011.2	-	-
BVPS (HK\$)	186.09	192.26	198.25	204.46

### Cash Flow (HK\$ mn)

	6/18	6/19E	6/20E	6/21E
Net income	49,951.0	32,234.8	32,558.2	34,058.0
D&A add-back	2,007.0	2,025.5	2,046.2	2,066.4
Minority interest add-back	829.0	577.9	683.7	846.4
Net (inc)/dec working capital	(27,790.0)	11,194.7	(2,974.5)	11,204.7
Other operating cash flow	(13,324.0)	(3,241.8)	(3,864.1)	(5,373.5)
<b>Cash flow from operations</b>	<b>11,673.0</b>	<b>42,791.1</b>	<b>28,449.4</b>	<b>42,802.0</b>
Capital expenditures	(40,570.0)	(57,000.5)	(10,046.2)	(10,066.4)
Acquisitions	-	-	-	-
Divestitures	-	-	-	-
Others	9,603.8	3,505.1	4,132.0	5,611.5
<b>Cash flow from investing</b>	<b>(30,966.2)</b>	<b>(53,495.4)</b>	<b>(5,914.1)</b>	<b>(4,454.9)</b>
Dividends paid (common & pref)	(12,162.6)	(13,760.8)	(14,629.9)	(15,499.0)
Inc/(dec) in debt	39,610.0	22,762.8	(9,716.0)	(5,006.8)
Other financing cash flows	(13,333.2)	0.0	0.0	0.0
<b>Cash flow from financing</b>	<b>14,114.2</b>	<b>9,002.0</b>	<b>(24,345.9)</b>	<b>(20,505.7)</b>
<b>Total cash flow</b>	<b>(5,179.0)</b>	<b>(1,702.3)</b>	<b>(1,810.6)</b>	<b>17,841.4</b>
Free cash flow	(28,897.0)	(14,209.4)	18,403.2	32,735.6

Source: Company data, Goldman Sachs Research estimates.

- In addition, they see “up-zoning” being potentially a key way the government could increase flat supply and better utilize limited land resources, and they have applied to the government for a higher plot ratio at their Shap Sze Heung site (current GFA: 4.8mn sq. ft., converted back in 2Q17) for another c.20% more GFA.
- **HK retail rentals:**
  - Their retail rental portfolio saw double-digit-growth in tenant sales 2018YTD and into 2H2018E they have not noticed a slowdown in the momentum.
  - While SHKP acknowledges that macro uncertainties and FX volatility could weigh on consumption sentiment, the company sees a potential offset through better regional connectivity (high-speed rail and HK-Macau-Zhuhai bridge).
- **China and overseas investments:**
  - China: With still keen competition and increasing policies related to the residential segment, the company reiterated its focus on mixed-use development, citing a 435k sq ft GFA commercial site in Nansha Free Trade Zone which they acquired in May 2018 as an example.
  - Overseas: SHKP is open to experimental overseas projects through JVs with reputable local partners, and sees London and Singapore as likely cities they could explore. Aside from their existing ION Orchard complex in Singapore (JV with Capitaland), the company disclosed that it invested in a JV residential project in Canary Wharf in London with Ballymore.

### What to do with the stock

- Based on the latest dividend, the stock stands at a 4.1% yield on its last close. We estimate roughly HK\$5.5 per share post-tax rental cash flow p.a., which is more than sufficient cover for the aforesaid DPS of HK\$4.65 per share, and rentals at an estimated 5% CAGR between FY18 to FY21E amid positive rental reversions and new openings.
- Trading at a deep 50% discount to its FY19E NAV, our analysis indicates current valuations are ascribing zero value to its development property landbank or pipeline — where we believe the company stands to command sustainable margins from prudent landbank accumulation over recent years, especially as it unlocks farm land that it owns.
- We reiterate our Buy (on CL) on SHKP for its steadily growing recurring income and sizable existing development land bank with large margin buffers to support its earnings in years to come. We fine-tune our FY19E/20E EPS by up to 1.4%, and introduce FY21E EPS, and raise our FY19E NAV-based 12m TP by 1.2% to HK\$168 (still based on 25% discount to NAV).
- **Risks**
  - **Real estate policies:** Potential changes to the real estate policies by the current administration, including but not limited to pace of land formation and supply, public housing policies, and demand side measures.

- **Interest rates:** We see rate hikes remaining a structural negative to the residential price outlook. We estimate the average private residential unit has a 75% debt-service ratio (DSR) and 18X price-to-income. The 20-year history for the two metrics shows averages of 46% and 9.5X respectively.

**Exhibit 1: SHKP FY18 results review**

( HK\$m)	FY2017	FY2018	YoY Chg	2HFY17	2HFY18	YoY Chg
<b>Turnover</b>	<b>78,207</b>	<b>85,644</b>	<b>9.5%</b>	<b>31,864</b>	<b>30,478</b>	<b>-4.3%</b>
<b>Property sales</b>	<b>35,962</b>	<b>39,795</b>	<b>10.7%</b>	<b>11,830</b>	<b>6,363</b>	<b>-46.2%</b>
- Hong Kong	30,224	35,699	18.1%	11,018	3,964	-64.0%
- China	5,738	4,096	-28.6%	812	2,399	195.4%
<b>Property rental</b>	<b>17,970</b>	<b>19,411</b>	<b>8.0%</b>	<b>9,105</b>	<b>9,995</b>	<b>9.8%</b>
- Hong Kong	14,555	15,494	6.5%	7,354	7,967	8.3%
- China	3,415	3,917	14.7%	1,751	2,028	15.8%
<b>Hotel</b>	<b>4,166</b>	<b>4,438</b>	<b>6.5%</b>	<b>1,995</b>	<b>2,145</b>	<b>7.5%</b>
<b>Telecommunications</b>	<b>8,715</b>	<b>9,988</b>	<b>14.6%</b>	<b>3,343</b>	<b>5,880</b>	<b>75.9%</b>
<b>Others</b>	<b>11,394</b>	<b>12,012</b>	<b>5.4%</b>	<b>5,591</b>	<b>6,095</b>	<b>9.0%</b>
<b>Operating profit after change in fair value of investment properties</b>	<b>43,336</b>	<b>51,225</b>	<b>18.2%</b>	<b>21,048</b>	<b>18,397</b>	<b>-12.6%</b>
<b>Property sales</b>	<b>11,086</b>	<b>15,342</b>	<b>38.4%</b>	<b>3,320</b>	<b>1,988</b>	<b>-40.1%</b>
- Hong Kong	9,909	13,914	40.4%	3,246	1,269	-60.9%
- China	1,177	1,428	21.3%	74	719	871.6%
<b>Property rental</b>	<b>14,020</b>	<b>15,222</b>	<b>8.6%</b>	<b>7,234</b>	<b>7,984</b>	<b>10.4%</b>
- Hong Kong	11,264	12,026	6.8%	5,787	6,293	8.7%
- China	2,756	3,196	16.0%	1,447	1,691	16.9%
<b>Hotel</b>	<b>1,108</b>	<b>1,227</b>	<b>10.7%</b>	<b>491</b>	<b>567</b>	<b>15.5%</b>
<b>Telecommunications &amp; others</b>	<b>3,312</b>	<b>3,662</b>	<b>10.6%</b>	<b>1,272</b>	<b>1,802</b>	<b>41.7%</b>
<b>Surplus arising from inv prop reval</b>	<b>13,810</b>	<b>15,772</b>	<b>14.2%</b>	<b>8,731</b>	<b>6,056</b>	<b>n.a.</b>
<b>Net interest income/(expense)</b>	<b>(1,709)</b>	<b>(1,617)</b>	<b>-5.4%</b>	<b>(785)</b>	<b>(895)</b>	<b>14.0%</b>
<b>Associates &amp; JVs</b>	<b>7,598</b>	<b>9,748</b>	<b>28.3%</b>	<b>3,850</b>	<b>3,281</b>	<b>-14.8%</b>
<b>Property sales</b>	<b>831</b>	<b>919</b>	<b>10.6%</b>	<b>252</b>	<b>378</b>	<b>50.0%</b>
- Hong Kong	27	22	-18.5%	(1)	(4)	300.0%
- China	773	886	14.6%	232	371	59.9%
- Singapore	31	11	-64.5%	21	11	-47.6%
<b>Property rental</b>	<b>3,122</b>	<b>3,425</b>	<b>9.7%</b>	<b>1,635</b>	<b>1,772</b>	<b>8.4%</b>
- Hong Kong	2,413	2,523	4.6%	1,221	1,283	5.1%
- China	196	338	72.4%	136	192	41.2%
- Singapore	513	564	9.9%	278	297	6.8%
<b>Hotel</b>	<b>217</b>	<b>243</b>	<b>12.0%</b>	<b>99</b>	<b>127</b>	<b>28.3%</b>
<b>Other businesses</b>	<b>519</b>	<b>633</b>	<b>22.0%</b>	<b>254</b>	<b>182</b>	<b>-28.3%</b>
<b>Finance costs</b>	<b>(387)</b>	<b>(475)</b>	<b>22.7%</b>	<b>(200)</b>	<b>(227)</b>	<b>13.5%</b>
<b>Taxation</b>	<b>(1,099)</b>	<b>(1,249)</b>	<b>13.6%</b>	<b>(527)</b>	<b>(660)</b>	<b>25.2%</b>
<b>Reval. gains at assoc and JV</b>	<b>4,395</b>	<b>6,252</b>	<b>42.3%</b>	<b>2,337</b>	<b>1,709</b>	<b>n.a.</b>
<b>PBT</b>	<b>49,225</b>	<b>59,356</b>	<b>20.6%</b>	<b>24,113</b>	<b>20,783</b>	<b>-13.8%</b>
Taxation	(6,750)	(8,402)	24.5%	(2,712)	(3,308)	22.0%
Perpetual securities	(18)	(174)	n.a.	(18)	(87)	
Minorities	(675)	(829)	22.8%	(260)	(468)	80.0%
<b>Net profit</b>	<b>41,782</b>	<b>49,951</b>	<b>19.6%</b>	<b>21,123</b>	<b>16,920</b>	<b>-19.9%</b>
<b>Underlying profit</b>	<b>25,965</b>	<b>30,398</b>	<b>17.1%</b>	<b>11,357</b>	<b>10,425</b>	<b>-8.2%</b>
<b>EPS (HK\$)</b>	<b>14.43</b>	<b>17.24</b>	<b>19.5%</b>	<b>7.29</b>	<b>5.84</b>	<b>-20.0%</b>
<b>Underlying EPS (HK\$)</b>	<b>8.97</b>	<b>10.49</b>	<b>16.9%</b>	<b>3.92</b>	<b>3.59</b>	<b>-8.4%</b>
<b>DPS (HK\$)</b>	<b>4.10</b>	<b>4.65</b>	<b>13.4%</b>	<b>3.55</b>	<b>3.45</b>	<b>-2.8%</b>
<b>Investment property valuation</b>	<b>337,980</b>	<b>369,477</b>	<b>9.3%</b>	<b>337,980</b>	<b>369,477</b>	<b>9.3%</b>
<b>Shareholders' funds (HK\$ mn)</b>	<b>498,215</b>	<b>539,098</b>	<b>8.2%</b>	<b>498,215</b>	<b>539,098</b>	<b>8.2%</b>
<b>Book value per share (HK\$)</b>	<b>172.0</b>	<b>186.1</b>	<b>8.2%</b>	<b>172.0</b>	<b>186.1</b>	<b>8.2%</b>

Source: Company data, Goldman Sachs Global Investment Research

# Disclosure Appendix

## Reg AC

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Financial Returns and Multiple use the Goldman Sachs analyst forecasts at the fiscal year-end at least three quarters in the future. Growth uses inputs for the fiscal year at least seven quarters in the future compared with the year at least three quarters in the future (on a per-share basis for all metrics).

For a more detailed description of how we calculate the GS Factor Profile, please contact your GS representative.

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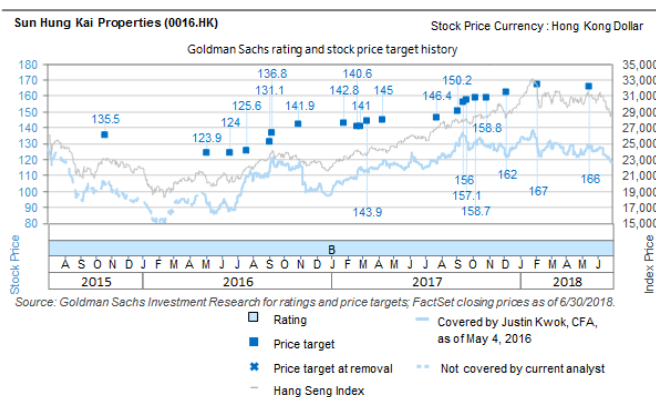
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