

China / Hong Kong Company Guide

Hongkong Land

Version 5 | Bloomberg: HKL SP EQUITY | Reuters: HKLD.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

11 Dec 2019

BUY

Last Traded Price (11 Dec 2019): US\$5.47 (STI : 3,173)
Price Target 12-mth: US\$6.64 (21.4% upside) (Prev US\$7.70)

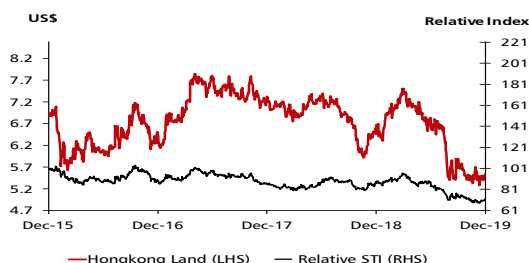
Analyst

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What's New

- **Reversionary growth for Central office portfolio to moderate as the market there has peaked out**
- **Despite challenges surrounding its Central portfolio, low valuation cushions downside risk**
- **Negatives largely discounted, maintain BUY with US\$6.64 TP**

Price Relative



Forecasts and Valuation

FY Dec (US\$ m)	2018A	2019F	2020F	2021F
Turnover	2,665	2,160	1,802	3,130
EBITDA	1,094	1,004	1,049	1,150
Pre-tax Profit	1,240	1,205	1,233	1,300
Underlying Profit	1,036	1,040	1,045	1,094
EPS (US\$)	0.44	0.45	0.45	0.47
EPS Gth (%)	9.1	0.7	0.5	4.7
PE (X)	12.4	12.3	12.2	11.7
P/Cash Flow (X)	16.5	10.7	17.1	6.3
EV/EBITDA (X)	15.3	16.7	16.0	14.6
DPS (US\$)	0.22	0.22	0.22	0.23
Div Yield (%)	4.0	4.0	4.0	4.2
Net Gearing (%)	9	11	13	11
ROE (%)	2.8	2.7	2.7	2.9
Est. NAV (US\$):			12.5	12.1
Disc. to NAV (%)			(56)	(55)
Earnings Rev (%):		(1)	(4)	New
Consensus EPS (US\$):		0.45	0.48	0.50
Other Broker Recs:		B:7	S:3	H:4

Source: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

Low valuation limits downside risk

Negatives largely discounted. HKL is trading at a 56% discount to our current appraised NAV, near the low end of its historical trading range. The challenging office and retail markets are expected cloud HKL's rental income growth outlook. However, the current low valuation, which has factored >30% fall in commercial prices in its Central portfolio, should provide a support to its share price. Hence we keep our BUY call with US\$6.64 TP.

Central portfolio facing challenges. According to JLL, the office vacancy in Central has increased to 3.3% in Oct-19 from Jun-19's 2.3%. This has resulted in office rentals falling 3.8% in 3Q19, and should weigh on HKL's future reversionary growth. HKL's Central retail portfolio is effectively fully occupied and base rental reversions had been positive reflecting the general increase in rents over the past few years. Nonetheless, the impact from the current social unrest in Hong Kong is yet to be reflected.

Improving sales from China. Attributable contracted sales in China more than tripled to US\$566m in 3Q19 as a result of more property launches and changes in product mix. Cumulative contracted sales for 3Q19 reached US\$1.2bn, up 50% y-o-y. As of Sep-19, sold but unrecognised sales reached US\$2bn, of which c.40% will be booked before end-20. While its China property business should add momentum to its earnings growth, this may not necessarily translate into higher valuation for the stock in the short-term given the risk inherently perceived by the market on the China property development sector.

Valuation:

Our TP of US\$6.64 is based on a target discount of 45% to our Dec-2020 NAV estimate.

Key Risks to Our View:

Any deterioration in leasing demand for office in Central and Singapore could drag HKL's earnings. Slow demand and property market cooling measures could adversely affect residential sales earnings from China. Cap rate expansion could lead to lower property valuations.

At A Glance

Issued Capital (m shrs)	2,334
Mkt Cap (US\$m)	12,767
Major Shareholders (%)	
Jardine Strategic Holdings Ltd	50.4
Free Float (%)	49.6
3m Avg. Daily Val. (US\$m)	2.00
GICS Industry: Real Estate / Real Estate Management & Development	
Bloomberg ESG disclosure score (2018)^	28.9
- Environmental / Social / Governance	29.5 / 22.8 / 33.9

^ refer to back page for more information



Live more, Bank less

Hongkong Land

CRITICAL FACTORS TO WATCH

Critical Factors

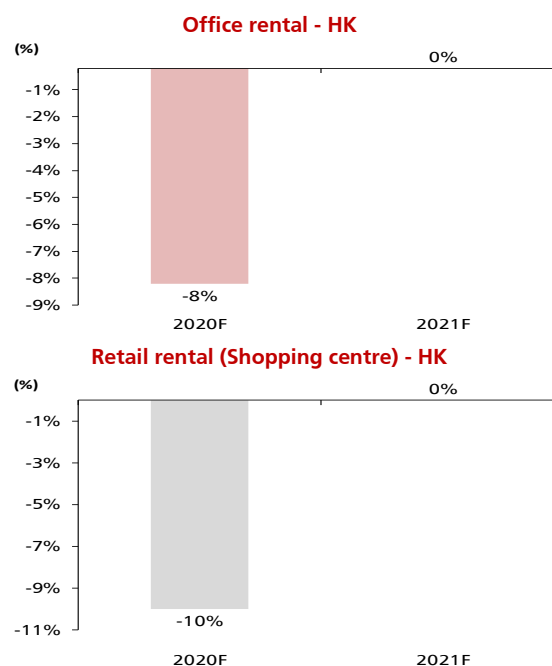
Hongkong Land's share price performance is primarily driven by NAV growth. We estimate that Central office represents 56% of Hongkong Land's (HKL) gross asset value (GAV). Hence HKL's NAV is sensitive to Central office property price. Our analysis suggests a 10% change in office prices would lead to 6.2% change in its NAV.

Reversionary growth for Central office portfolio to moderate as the market there has peaked out. Office vacancy in its Central portfolio improved slightly to 2.4% in Sep-19 from Jun-19's 2.8% as tenants took up the previously committed space. Rental reversions continued to stay positive in 3Q19, pushing average office net rents up further to HK\$117psf from 1H19's HK\$116psf. Having said that, the overall office vacancy in Central is rising and rents are starting to fall. The office vacancy in Central has increased to 3.3% in Oct-19 from Jun-19's 2.3% led by net withdrawal of office space, according to Jones Lang LaSalle. Selected landlords are finding it difficult to backfill the space led by the departure of tenants relocating out of Central. As a result, office rentals retreated 3.8% in 3Q19. This should weigh on HKL's future reversionary growth. HKL's Central retail portfolio was 99% occupied. Base rental reversions remained positive reflecting the general increase in rents over the past few years. Nonetheless, the impact from the current social unrest in Hong Kong has yet to be reflected. Reversionary growth of the company's Singapore office portfolio remains positive with vacancy improving remarkably to 1.3% in Sep-19 from Jun-19's 3.3%.

Improving contracted sales in China. The company's attributable contracted sales in China more than tripled to US\$566m in 3Q19 as a result of more launches and changes in product mix. This brought the cumulative contracted sales for 3Q19 to US\$1.2bn, up 50% y-o-y, thanks to stable market sentiment. As of Sep-19, sold but unrecognised sales reached US\$2bn, of which c.40% will be booked before end-20. In Singapore, contracted sales reached US\$403m in 9M19 with net order book of US\$540m in Sep-19. HKL is expected to commence sales of 638-unit Leedon Green (formerly Tulip Garden) in 1H20.

Growing contributions from China. In FY19, FY20, and FY21, Hongkong is scheduled to complete development properties of 0.66m sm, 0.67m sm and 0.8m sm respectively, up from FY18's 0.49m sm. While the bulk of projects scheduled for completion are from Chongqing, projects in new markets including Wuhan, Nanjing and Hangzhou should come onstream from FY20 onwards. With rising project completions in the years ahead, the China property business should add momentum to HKL's earnings growth. However, this does not necessarily translate into higher stock valuation in the short-to-medium term given the risk inherently perceived by the market on the China property development sector.

KEY ASSUMPTION

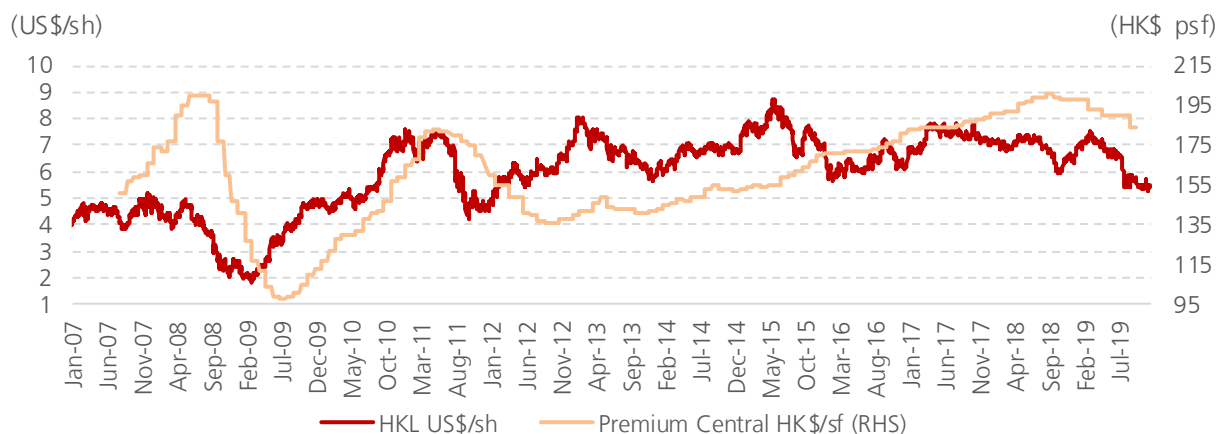


Source: Company, DBS HK

Hongkong Land

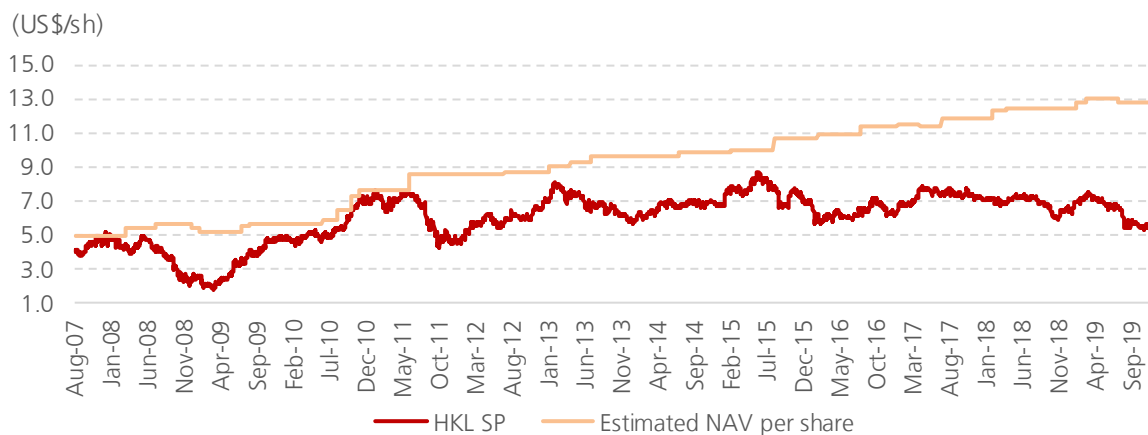
Appendix 1: A look at Company's listed history – what drives its share price?

HK Land's share price vs. premium Central office rents



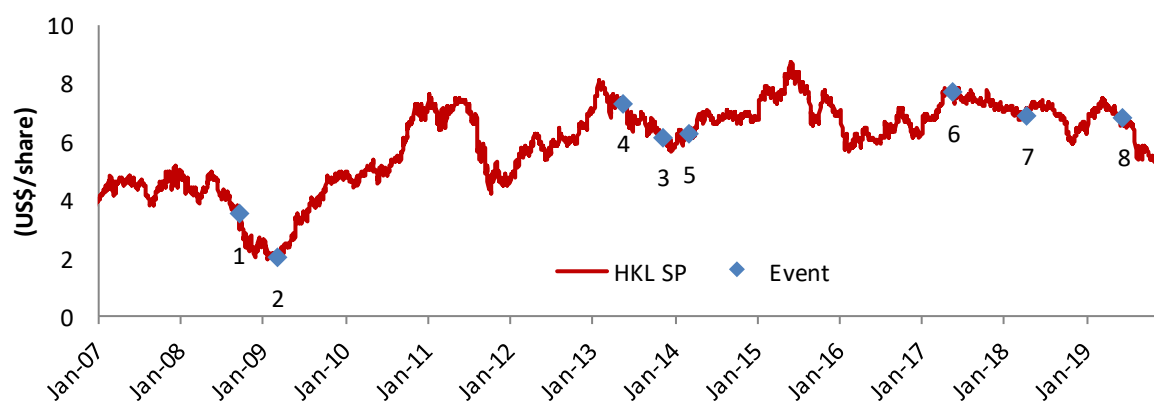
Source: Bloomberg Finance L.P., Knight Frank

HK Land share price vs. estimated NAV



Source: Bloomberg Finance L.P., DBS HK

HK Land's share price and key events



Event

- 1 Bankruptcy of Lehman Brothers during the global financial crisis, exerting downward pressure on Central office rents
- 2 Unexpected dividend cut during final results announcement. Rising office vacancy in Central portfolio
- 3 Acquired Central Avenue site in Chongqing in a 50:50 JV with a Chinese developer
- 4 Grand opening of Marina Bay Financial Center in Singapore
- 5 Completion of The Forum Redevelopment
- 6 Henderson Land pays record HK\$23.28bn for the Murray Road car park redevelopment site in Central
- 7 Repurchased shares at US\$7 a piece
- 8 First large scale anti extradition bill protest

Source: Bloomberg Finance L.P., various news reports, HK Land, DBS HK

Hongkong Land

Balance Sheet:

Net debt increased to US\$3.88bn in Jun-19 from Dec-18's US\$3.56bn due to acquisition of new sites in Wuhan and deposits paid for recent land auctions. This translated into gearing of 10%. (Dec-18: 9%) Despite slightly higher gearing, its financial risk remains well manageable.

Share Price Drivers:

Central office market, where Hongkong Land has heavy exposure, has peaked out. This should weigh on the company's future reversionary growth. However, its low valuation should lend support its share price performance.

Key Risks:

Market Risk Any deterioration in leasing demand for office in Central and Singapore could drag its rental earnings and share price performance. Any slower-than-expected take-up in Chongqing/Chengdu/Shanghai could adversely affect its residential sales earnings from China. Property market cooling measures is another risk.

Interest rate risk Any interest rate hike may lead to cap rate expansion and in turn adversely affect its valuation

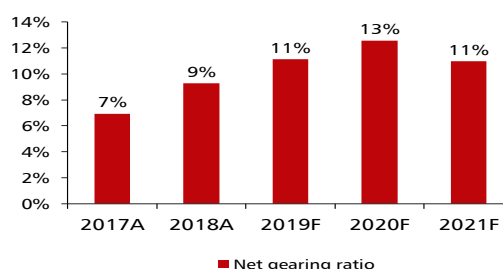
Environment, Social, Governance:

In HKL's investment properties portfolio, the company has upgraded its buildings to achieve high environmental standards. HKL has exceeded goals it set in 2008 for both energy consumption and greenhouse gas emissions. Jardine House, Chater House, and Alexandra House have been awarded Platinum rating for Hong Kong BEAM Plus. HKL also coordinates with commercial tenants and contractors to reduce solid waste and wastewater.

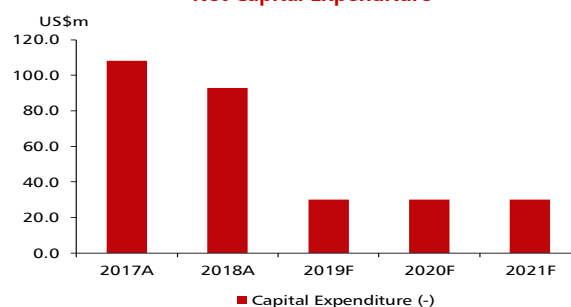
Company Background

Hongkong Land is one of Asia's leading property investment, management and development groups. The Group owns and manages c.800,000sm of prime office and luxury retail property in key Asian cities, principally in Hong Kong and Singapore.

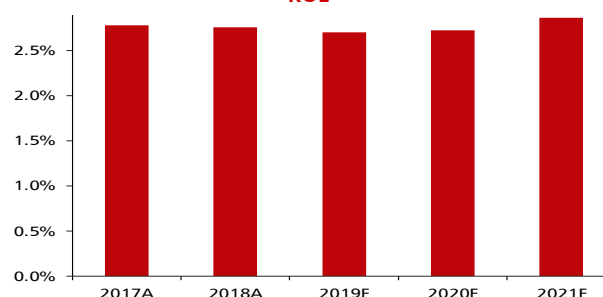
Gearing



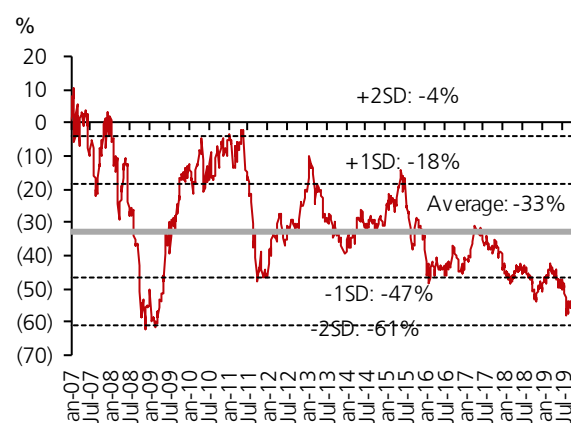
Net Capital Expenditure



ROE



Discount to NAV



Source: Company, DBS HK

Key Assumptions (%)

FY Dec	2020F	2021F
Office rental - HK	(8)	0
Retail rental (Shopping centre) - HK	(10)	0

Source: DBS HK

Segmental Breakdown (US\$ m)

FY Dec	2017A	2018A	2019F	2020F	2021F
Revenues (US\$ m)					
Rental income	912	983	1,026	1,032	1,030
Service and mgmt charges	140	150	145	148	152
Sale of trading properties	564	1,533	989	622	1,948
Total	1,616	2,665	2,160	1,802	3,130

Source: DBS HK

Income Statement (US\$ m)

FY Dec	2017A	2018A	2019F	2020F	2021F
Turnover	1,616	2,665	2,160	1,802	3,130
EBITDA	879	1,094	1,004	1,049	1,150
Depr / Amort	(3)	(4)	(4)	(4)	(4)
EBIT	876	1,089	1,000	1,045	1,146
Associates Inc	302	265	328	331	314
Interest (Exp)/Inc	(78)	(114)	(122)	(142)	(160)
Exceptionals	0	0	0	0	0
Pre-tax Profit	1,100	1,240	1,205	1,233	1,300
Tax	(151)	(206)	(167)	(190)	(207)
Minority Interest	(1)	2	1	1	1
Underlying Profit	947	1,036	1,040	1,045	1,094
Sales Gth (%)	(19)	65	(19)	(17)	74
Net Profit Gth (%)	12	9	0	0	5
EBITDA Margins (%)	54	41	46	58	37
EBIT Margin (%)	54	41	46	58	37
Tax Rate (%)	14	17	14	15	16

Source: DBS HK

Balance Sheet (US\$ m)

FY Dec	2017A	2018A	2019F	2020F	2021F
Fixed Assets	32,588	33,846	33,534	32,558	32,260
Other LT Assets	5,698	6,855	7,171	7,489	7,788
Cash & ST Invt	1,622	1,375	1,150	958	1,840
Other Current Assets	3,044	2,887	3,813	4,490	4,160
Total Assets	42,952	44,963	45,669	45,495	46,048
ST Debt	191	794	300	450	500
Creditors	1,695	1,337	1,362	1,366	1,370
Other Current Liab	114	119	119	119	119
LT Debt	3,980	4,145	5,139	5,289	5,539
Other LT Liabilities	164	198	198	198	198
Minority Interests	35	28	21	14	7
Shareholder's Equity	36,774	38,342	38,529	38,059	38,315
Total Cap. & Liab.	42,952	44,963	45,669	45,495	46,048
Share Capital (m)	2,353	2,334	2,334	2,334	2,334
Net Cash/(Debt)	(2,549)	(3,564)	(4,289)	(4,781)	(4,199)
Working Capital	2,667	2,011	3,181	3,512	4,010
Net Gearing (%)	7	9	11	13	11

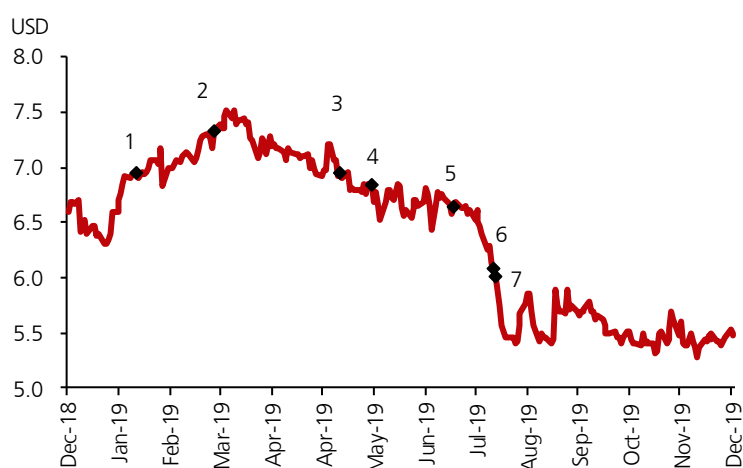
Source: DBS HK

Cash Flow Statement (US\$ m)

FY Dec	2017A	2018A	2019F	2020F	2021F
EBIT	876	1,089	1,000	1,045	1,146
Tax Paid	(137)	(172)	(167)	(190)	(207)
Depr/Amort	3	4	4	4	4
Chg in Wkg.Cap	40	(329)	316	(150)	1,060
Other Non-Cash	18	12	(128)	(152)	(171)
Operating CF	800	604	1,025	558	1,832
Net Capex	(108)	(93)	(30)	(30)	(30)
Assoc, MI, Invsmt	(839)	(963)	(1,200)	(500)	(700)
Investing CF	(947)	(1,056)	(1,230)	(530)	(730)
Net Chg in Debt	239	838	500	300	300
New Capital	0	(132)	0	0	0
Dividend	(447)	(469)	(521)	(519)	(519)
Other Financing CF	15	0	0	0	0
Financing CF	(193)	237	(21)	(219)	(219)
Chg in Cash	(340)	(215)	(225)	(192)	882

Source: DBS HK

Target Price & Ratings History



Source: DBS HK

Analyst: Jeff YAU CFA,
Ian CHUI CFA,

[^] Bloomberg ESG Disclosure Scores rate companies annually based on their disclosure of quantitative and policy-related ESG data. It is based on a scoring scale of 0-100, and calculated using a subset of more than 100 raw data points it collects on ESG. It is designed to measure the robustness of companies' disclosure of ESG information in their reporting/the public domain. Based on Bloomberg disclosures, as of 25 Jan 2019, the global ESG disclosure average score is 24.92 and 22.14, 28.26, 49.97 for Environmental, Social and Governance, respectively.

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STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

**Share price appreciation + dividends*

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Sources for all charts and tables are DBS HK unless otherwise specified.

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