

China / Hong Kong Company Update

China Evergrande Group

Bloomberg: 3333 HK Equity | Reuters: 3333.HK

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DBS Group Research . Equity

28 Sep 2020

BUY

Last Traded Price (25 Sep 2020): HK\$13.78 (HSI : 23,235)

Price Target 12-mth: HK\$18.96 (38% upside)

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What's New

- Expect renegotiations on investment terms to take place with strategic investors
- Equity fund raising from New Energy Vehicles and property management businesses to help deleverage
- Our cash flow analysis shows land acquisition slowdown is key to reduce total debt

Price Relative



Forecasts and Valuation

FY Dec (RMB m)	2019A	2020F	2021F	2022F
Turnover	477,561	560,889	649,605	680,047
EBITDA	98,071	96,067	105,796	100,546
Pre-tax Profit	74,172	79,474	92,658	88,559
Net Profit	17,280	23,457	29,278	29,954
Core Profit	24,558	23,457	29,278	29,954
Core Profit Gth (%)	(49.6)	(4.5)	24.8	2.3
Core EPS (RMB)	1.87	1.79	2.23	2.28
Core EPS (HK\$)	2.12	2.03	2.53	2.59
Core EPS Gth (%)	(49.6)	(4.5)	24.8	2.3
Core PE (X)	6.5	6.8	5.4	5.3
P/Cash Flow (X)	nm	2.0	1.3	10.4
EV/EBITDA (X)	9.6	9.1	7.3	7.7
DPS (HK\$)	1.62	1.01	1.27	1.29
Div Yield (%)	11.8	7.4	9.2	9.4
Net Gearing (%)	159.3	129.0	90.2	81.0
ROE (%)	12.4	15.5	17.8	16.7
Book Value (HK\$)	12.60	13.61	14.87	16.17
P/Book Value (X)	1.1	1.0	0.9	0.9

EPS Rev (%):	Nil	Nil	Nil
Consensus EPS (RMB)	2.09	2.43	2.69
Other Broker Recs:	B:7	S:1	H:6

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

Full effort to deleverage

Investment Thesis

Deleveraging is the top priority with an aim to reduce total debt by Rmb150bn in FY20-22 through presales, cash collection and slower land acquisitions.

Raising funds through its non-property development businesses.

Evergrande is raising funds for its new energy vehicle (NEV) and property management businesses via equity fund raising of up to HK\$45bn in 2H20 as per our estimates.

70%-owned NEV arm is trading at a similar market cap as the company, implying a distressed valuation for its property development business.

Valuation:

Our TP is based on an unchanged 6x FY21F PE on the company's development earnings, and potential market cap of its property management business with reference to the valuation of its recent round of pre-IPO share sale. Market value of NEV listco is not in price either.

Where we differ:

Our earnings estimates are lower than consensus as we have lower expectations on margins. Our valuation has factored in a potential property management arm spin-off at 36x FY21F PE, benchmarking the valuation to strategic investments.

Key Risks to Our View:

Lower-than-expected margins; insufficient land replenishment to drive growth.

At A Glance

Issued Capital (m shrs)	13,226
Mkt Cap (HK\$/US\$m)	182,254 / 23,517
Major Shareholders (%)	
Hui (Ka Yan)	71.7
Chinese Estates Holdings Ltd	6.6
Ding (Yu Mei)	6.1
Free Float (%)	15.6
3m Avg. Daily Val. (US\$m)	60.39
GIICS Industry: Real Estate / Real Estate Management & Development	



Live more, Bank less

WHAT'S NEW

Based on Evergrande's 1H20 financial reports and cash flow guidance, we believe Evergrande will need to fulfill the conditions below to sustain the business.

- To achieve Rmb700bn presales proceeds
- Cash collection rate of c. 90%
- All short-term debt can be refinanced
- Strategic investments can be extended
- No further land acquisitions if there is no loan expansion

Is it possible to fulfill the conditions? YES

- Evergrande should be able to achieve Rmb700bn presales proceeds in FY20F

Evergrande has achieved Rmb450bn presales in 8M20. Given the strong promotions, we believe Evergrande is likely to achieve Rmb62bn contracted sales/month for the rest of this year to achieve Rmb700bn in contracted sales.

- Cash collection rate of c. 90%

Reasonable assumption as this is similar 1H20's rate.

- All short-term debt can be refinanced

Short term debt can be refinanced in normal situation, but cost may vary.

- Strategic investment of Rmb 130bn stays

While we don't expect A-share listing to take place at this stage, we don't think strategic investors will pull their investments either. We believe the most likely outcome is a renegotiation of the terms, either to extend the due date or convert the investment to non-tradeable equity in Hengda Real Estate.

- No further land acquisitions if there is no loan expansion

We would need to monitor this aspect. But we believe the company realises it is time to suspend land acquisitions for now.

What else can help?

- Raising more cash from NEV. The company has raised HKD4bn through Evergrande New Energy Vehicle placement in Sep 2020.
- Further fund raising through spinning off its property management arm. Evergrande has sold over 20% to a group of investors and raised Rmb25bn in Sep. A further 20% reduction in interest may raise another c. Rmb20bn funding in our estimates

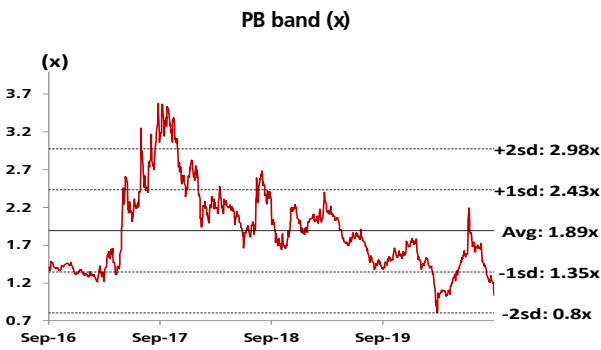
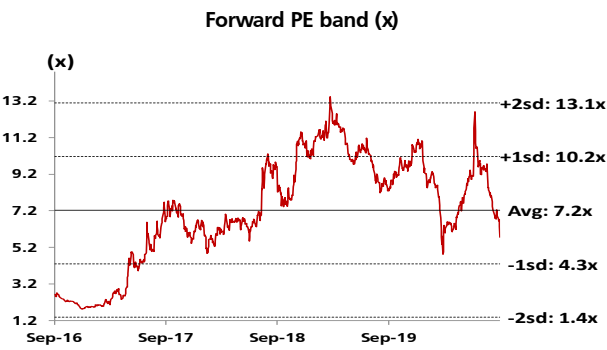
Expect short covering and sector rebound

Our discussions with investors in Aug pointed to low holdings in the China property sector. Evergrande's free float is even lower. Share price has corrected significantly, mainly from short selling in our view. Strong presales and potential information/announcement about Evergrande's renegotiation with strategic investors should potentially trigger short covering and share price recovery.

Company Background

Evergrande is among the top 3 developers in China in terms of property sales, with a large residential landbank of 240m sm as at Jun-20. It aims to be a conglomerate with exposure in the real estate, financial, cultural tourism, healthcare sectors, and high-tech industries.

Historical PE and PB band



Source: Thomson Reuters, DBS HK

Segmental Breakdown (RMB m)

FY Dec	2018A	2019A	2020F	2021F	2022F
Revenues (RMB m)					
Sales of properties	452,764	464,568	546,884	634,401	663,417
Rental income of investment	1,178	1,364	1,500	1,650	1,815
Property management services and Others	4,067	4,375	5,250	6,300	7,560
	8,187	7,254	7,254	7,254	7,254
Total	466,196	477,561	560,889	649,605	680,047

Source: Company, DBS HK

Income Statement (RMB m)

FY Dec	2018A	2019A	2020F	2021F	2022F
Turnover	466,196	477,561	560,889	649,605	680,047
Cost of Goods Sold	(297,249)	(344,624)	(417,721)	(489,729)	(522,834)
Gross Profit	168,947	132,937	143,167	159,876	157,213
Other Opg (Exp)/Inc	4,160	3,689	0	0	0
Operating Profit	140,071	93,334	94,931	104,660	99,409
Associates Inc	(874)	2,967	0	0	0
Net Interest (Exp)/Inc	(14,623)	(22,763)	(15,457)	(12,002)	(10,850)
Exceptional Gain/(Loss)	2,191	634	0	0	0
Pre-tax Profit	126,765	74,172	79,474	92,658	88,559
Tax	(60,218)	(40,630)	(44,523)	(49,033)	(43,928)
Minority Interest	(29,157)	(16,262)	(11,494)	(14,346)	(14,677)
Net Profit	37,390	17,280	23,457	29,278	29,954
Core Profit	48,680	24,558	23,457	29,278	29,954
Sales Gth (%)	49.9	2.4	17.4	15.8	4.7
Net Profit Gth (%)	53.4	(53.8)	35.7	24.8	2.3
Core Profit Gth (%)	57.0	(49.6)	(4.5)	24.8	2.3
Gross Mgn (%)	36.2	27.8	25.5	24.6	23.1
Core Profit Margin (%)	10.4	5.1	4.2	4.5	4.4
Tax Rate	47.5	54.8	56.0	52.9	49.6

Source: Company, DBS HK

Balance Sheet (RMB m)

FY Dec	2018A	2019A	2020F	2021F	2022F
Fixed Assets	212,582	231,907	231,907	231,907	231,907
Invt in Assocs & JVs	0	0	0	0	0
Other LT Assets	91,695	127,856	127,856	127,856	127,856
Cash & ST Invt	204,209	228,767	178,505	150,588	114,309
Other Current Assets	1,371,542	1,618,047	1,718,846	1,795,012	1,904,086
Total Assets	1,880,028	2,206,577	2,257,114	2,305,364	2,378,158
ST Debt	318,285	372,169	322,169	272,169	222,169
Creditors	554,313	717,618	717,618	717,618	717,618
Other Current Liab	286,858	260,248	416,412	585,676	678,816
LT Debt	354,857	427,726	348,876	248,876	248,876
Other LT Liabilities	57,089	70,279	70,279	70,279	70,279
Minority Interests	175,631	212,837	224,331	238,678	253,355
Shareholder's Equity	132,995	145,700	157,429	172,068	187,045
Total Capital	1,880,028	2,206,577	2,257,114	2,305,364	2,378,158
Share Capital (m)	13,125	13,138	13,138	13,138	13,138
Net Cash/(Debt)	(468,933)	(571,128)	(492,540)	(370,457)	(356,736)
Working Capital	530,371	640,181	584,816	491,718	507,651
Net Gearing (%)	151.9	159.3	129.0	90.2	81.0

Source: Company, DBS HK

Cash Flow Statement (RMB m)

FY Dec	2018A	2019A	2020F	2021F	2022F
Profit Before Tax	126,765	74,172	79,474	92,658	88,559
Assoc. & JV Inc/(loss)	0	0	0	0	0
Tax Paid	(25,510)	(19,059)	(44,523)	(49,033)	(43,928)
Depr/Amort	1,136	1,136	1,136	1,136	1,136
Chg in Wkg.Cap.	(16,907)	(75,359)	44,640	80,121	(29,241)
Other Non-Cash	(28,569)	(47,063)	(1,136)	(1,136)	(1,136)
Operating CF	54,749	(67,357)	79,592	123,746	15,390
Net chg in inv.	(895)	(7,743)	0	0	0
Assoc, MI, Invsmt	(59,468)	(47,565)	0	0	0
Investing CF	(60,363)	(55,308)	0	0	0
Net Chg in Debt	(60,710)	108,895	(128,850)	(150,000)	(50,000)
New Capital	(2,625)	295	0	0	0
Dividend	(27,684)	(2,748)	(11,729)	(14,639)	(14,977)
Other Financing CF	73,368	36,721	10,725	12,977	13,307
Financing CF	(17,651)	143,163	(129,854)	(151,663)	(51,669)
Chg in Cash	(22,644)	20,692	(50,263)	(27,916)	(36,279)
Chg in Net Cash	(24,030)	(102,195)	78,588	122,084	13,721

Source: Company, DBS HK

Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	1-Apr-20	HK\$12.86	HK\$14.30	Buy
2:	17-Sep-20	HK\$16.72	HK\$18.96	Buy

Source: DBS HK

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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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