

## KWG

### Shifting to fast track

**Upgrade PT to HK\$15.79; maintain Buy; Contract sales in Jan. surged 155% YoY to Rmb 5.56 bn. Rmb 100 bn of saleable resource support fast growth of contracted sales in 2018**

Under market consolidation, we see that KWG has accelerated land acquisition in 2017 at attractive costs. We believe the company has shifted its strategy to boost scale from a stable growth strategy with high margin in next few years. In 2017, the company achieved Rmb 38 bn of contracted sales, with 33% YoY growth (Rmb 28.7 bn of attributable contracted sales, up 29% YoY). The company will launch Rmb 100 bn of saleable resource in 2018 and target a 60% sell through rate, which implies over 50% of contracted sales growth. We upgrade our price target as we factor in new land acquisition and selling price into our NAV assumption.

#### Penetrate dual core areas of China: Yangtze River delta and Greater Bay area

The company has entered Shenzhen city by acquisition, a milestone for the company covering all 1<sup>st</sup> tier cities. Besides, the company has fully covered all core cities in Yangtze river delta and Greater Bay area. In Greater Bay area, the company has focused in Guangzhou & Foshan. We believe the company can manage policy risk in 2018, thanks to its balanced land reserve.

#### Look for safe margins in new cities

The company has acquired 5.97 mn sq.m of attributable GFA in 2017, up 150% YoY, for a total attributable consideration of Rmb 35.8 bn. Two newly acquired Hong Kong projects accounted for bulk of this, costing Rmb 12 bn. These Hong Kong projects will be launched in 2019 and 2020. Besides, the company has entered more cities: Shenzhen, Zhaoqing, Xi'an & Wuhan. Land cost of Shenzhen Bantian project is around Rmb 9,375 per sq.m, we estimate selling price at Rmb 45,000 per sq.m; land cost to price ratio at only 21%. Xi'an is another city guarantee a good margin: land cost to price ratio is only 20% as well. We believe the company's reasonable acquisition not only boost sales scale but could also enhance the company's profitability in next 3 years.

#### We expect GPM to be above 34% in 2017-2019

Reasonable land replenishment in 2017 will provide higher potential margin upgrade in next 3 years. Land cost to price ratio of 2017 replenishment is 32.5%, which enhance KWG profitability. We expect gross profit margin maintain over 34% in next 3 years, compared to 34.6% in 2016.

#### 50% sales growth ahead, maintain 'Buy'

The company has entered more cities for boosting scale. Besides, land cost of land replenishment is relatively low and provides better margin in next 3 years. We expect 1) 50% growth in contracted sales in 2018-2019; 2) over 30% growth in booking revenue in 2017-2019 and 3) its gross margin to be above 34% in 2017-2019. The company is trading at 7.1x 2018 PE, which is lower than 8.8x 18PE of sector average. We reiterate 'Buy' rating and lift target price to HK\$ 15.79, which implies 38% discount to Dec-18 NAV, 8.6x 2018 core PE and 1.2x 2018e PB. Risk factors: 1) sales price and sales volume miss expectation new entered cities, 2) home price cap further tightening in 1<sup>st</sup> and 2<sup>nd</sup> tier cities.

Stock code: 1813.HK

Rating: Buy

Price target (HK\$)	15.79
Previous price target (HK\$)	10.71
Current price (HK\$, 5 Feb 2017)	13.14
Upside/downside %	20%
Market cap (HK\$ m)	41,459
Market cap (US\$ m)	5,301
Avg daily turnover (HK\$ m)	120.0

Source: Bloomberg, AMTD Equity Research

#### Key forecasts

(RMB m)	2016	2017e	2018e	2019e
Revenue	8,865	12,115	16,334	22,245
yoy %	6%	37%	35%	36%
Net profit	3,465	3,474	4,565	6,231
yoy %	1%	0%	31%	36%
Adjusted NP	3,340	3,474	4,565	6,231
yoy %	16%	4%	31%	36%
Gross margin	34.6%	34.6%	34.7%	35.1%
Net gearing	66.8%	58.8%	73.1%	73.1%
EPS	1.15	1.15	1.51	2.06
DPS	0.40	0.40	0.53	0.72
BPS	7.93	9.08	10.59	12.65

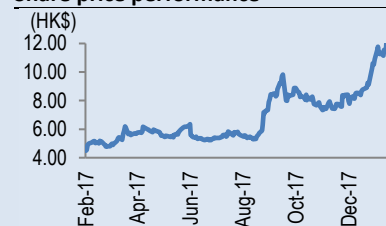
Source: Company data, AMTD Equity Research

#### Valuation

	2016	2017e	2018e	2019e
P/E	9.3	9.3	7.1	5.2
P/BV	1.3	1.2	1.0	0.8
Div. yield	3.8%	3.8%	4.9%	6.8%
ROE	14.4%	13.5%	15.4%	17.7%
ROA	3.1%	2.9%	3.1%	3.5%

Source: Bloomberg, AMTD Equity Research

#### Share price performance



Source: Bloomberg

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Figure 1:P&amp;L forecast and key ratios

PnL, RMB mn						YoY growth				
	2015	2016	2017e	2018e	2019e	2015	2016	2017e	2018e	2019e
<b>Revenue</b>	<b>8,340</b>	<b>8,865</b>	<b>12,115</b>	<b>16,334</b>	<b>22,245</b>	<b>-20.3%</b>	<b>6.3%</b>	<b>36.7%</b>	<b>34.8%</b>	<b>36.2%</b>
Sale of properties	7,563	7,923	11,079	15,297	21,209	-22.6%	4.8%	39.8%	38.1%	38.6%
Cost of sales	(5,330)	(5,795)	(7,922)	(10,670)	(14,443)					
<b>Gross profit</b>	<b>3,009</b>	<b>3,070</b>	<b>4,193</b>	<b>5,663</b>	<b>7,803</b>	<b>-19.0%</b>	<b>2.0%</b>	<b>36.6%</b>	<b>35.1%</b>	<b>37.8%</b>
Selling expenses	(277)	(323)	(469)	(868)	(1,303)	-7.3%	16.7%	45.3%	85.2%	50.0%
Administrative expenses	(775)	(969)	(1,085)	(1,410)	(1,800)	-2.5%	25.1%	12.0%	29.9%	27.7%
Share of post-tax loss of an associate	(3)	0	0	0	0					
Share of post-tax (losses)/profits of joint ventures	1,935	2,130	1,614	2,377	3,342					
<b>Finance costs</b>	<b>(10)</b>	<b>(160)</b>	<b>(177)</b>	<b>(212)</b>	<b>(240)</b>	<b>71.8%</b>	<b>1429.8%</b>	<b>10.4%</b>	<b>19.8%</b>	<b>13.3%</b>
<b>Profit before tax</b>	<b>4,662</b>	<b>4,527</b>	<b>4,690</b>	<b>6,164</b>	<b>8,416</b>	<b>0.4%</b>	<b>-2.9%</b>	<b>3.6%</b>	<b>31.4%</b>	<b>36.5%</b>
Income tax expense	(1,249)	(1,066)	(1,219)	(1,603)	(2,188)					
<b>Profit for the year</b>	<b>3,413</b>	<b>3,462</b>	<b>3,471</b>	<b>4,562</b>	<b>6,228</b>	<b>4.4%</b>	<b>1.4%</b>	<b>0.3%</b>	<b>31.4%</b>	<b>36.5%</b>
Profit for the year attributable to:										
<b>Net profit</b>	<b>3,416</b>	<b>3,465</b>	<b>3,474</b>	<b>4,565</b>	<b>6,231</b>	<b>4.4%</b>	<b>1.4%</b>	<b>0.3%</b>	<b>31.4%</b>	<b>36.5%</b>
<b>Core net profit</b>	<b>2,884</b>	<b>3,340</b>	<b>3,474</b>	<b>4,565</b>	<b>6,231</b>	<b>5.0%</b>	<b>15.8%</b>	<b>4.0%</b>	<b>31.4%</b>	<b>36.5%</b>
Non-controlling interests	(3)	(3)	(3)	(3)	(3)					
Dividends	869	1,557	1,216	1,598	2,181					
<b>EPS - basic</b>	<b>1.15</b>	<b>1.15</b>	<b>1.15</b>	<b>1.51</b>	<b>2.06</b>					
<b>EPS-underlying</b>	<b>0.97</b>	<b>1.11</b>	<b>1.15</b>	<b>1.51</b>	<b>2.06</b>					
<b>DPS - basic</b>	<b>0.29</b>	<b>0.40</b>	<b>0.40</b>	<b>0.53</b>	<b>0.72</b>					
<b>Key Ratios, RMB mn</b>	<b>2015</b>	<b>2016</b>	<b>2017e</b>	<b>2018e</b>	<b>2019e</b>					
GPM	36.1%	34.6%	34.6%	34.7%	35.1%					
NPM	41.0%	39.1%	28.7%	27.9%	28.0%					
Core NPM	34.6%	37.7%	28.7%	27.9%	28.0%					
ROA	4.3%	3.1%	2.9%	3.1%	3.5%					
ROCE	7.2%	5.9%	4.9%	5.6%	6.5%					
ROE	13.5%	14.4%	13.5%	15.4%	17.7%					
Total Debt / EBITDA	5.8x	8.9x	9.7x	8.9x	7.4x					
Total Debt / Equity	125.2%	178.9%	172.6%	177.4%	168.3%					
Total Debt / Capitalization	55.6%	64.1%	63.3%	63.9%	62.7%					
Net Debt / EBITDA	3.2x	3.3x	3.3x	3.7x	3.2x					
Net Debt / Equity	69.0%	66.8%	58.8%	73.1%	73.1%					
Net Debt / Capitalization	30.6%	24.0%	21.6%	26.4%	27.2%					
Current Ratio	132.0%	158.4%	184.0%	181.2%	157.3%					
Cash / Total Assets	15.8%	24.3%	25.9%	22.8%	20.3%					
Inventory / Total Assets	34.4%	41.0%	42.3%	51.0%	58.3%					
Net debt / Net Inventory	56.3%	35.4%	31.6%	31.4%	26.7%					
Quick Ratio	93.0%	101.6%	116.4%	126.6%	117.4%					
Cash Ratio	39.0%	56.9%	67.6%	54.7%	39.8%					
Interest Coverage	2.1x	1.7x	1.6x	1.8x	2.1x					

Source: Company data, AMTD Equity Research

**Figure 2: Balance sheet forecast & Cash flow forecast**

<b>Balance Sheet, RMB mn</b>	<b>2015</b>	<b>2016</b>	<b>2017e</b>	<b>2018e</b>	<b>2019e</b>
Non-current assets	37,190	35,795	35,795	35,795	35,795
Current assets	42,492	74,947	85,099	110,763	143,844
Properties under development	20,895	38,503	44,299	67,816	97,874
Completed properties held for sale	6,534	6,866	6,866	6,866	6,866
Restricted bank deposits	1,620	1,131	1,131	1,131	1,131
Bank balances and cash	10,946	25,771	30,128	32,275	35,298
Others	2,497	2,676	2,676	2,676	2,676
Current liabilities	32,190	47,309	46,241	61,125	91,468
Advanced proceeds received from customers	3,036	4,186	6,391	18,094	37,385
Borrowings	3,983	4,754	1,481	4,662	15,714
Others	25,171	38,369	38,369	38,369	38,369
Non-current liabilities	25,133	39,424	47,173	53,392	49,903
Borrowings	24,015	38,196	45,945	52,164	48,675
Others	1,118	1,228	1,228	1,228	1,228
Capital and reserves	22,359	24,009	27,479	32,041	38,269
Equity attributable to owners of the Company	22,341	23,950	27,424	31,989	38,219
Non-controlling interests	18	58	55	52	49
<b>Cash Flow Statement, RMB mn</b>	<b>2015</b>	<b>2016</b>	<b>2017e</b>	<b>2018e</b>	<b>2019e</b>
<b>Profit before income tax</b>	<b>4,662</b>	<b>4,527</b>	<b>4,690</b>	<b>6,164</b>	<b>8,416</b>
Operating cash flows before movements in working capital	2,149	2,270	2,899	3,575	4,834
Cash (used in) from operations	3,114	524	(691)	(8,239)	(5,932)
Interest received	41	170	177	212	240
Interest paid	(2,337)	(2,231)	(2,997)	(3,591)	(4,069)
PRC Income tax paid	(232)	(324)	(657)	(863)	(1,178)
Land appreciation tax paid	(285)	(229)	(563)	(740)	(1,010)
<b>Net cash (used in) from operating activities</b>	<b>301</b>	<b>(2,091)</b>	<b>(4,731)</b>	<b>(13,222)</b>	<b>(11,949)</b>
<b>Net cash used in investing activities</b>	<b>(1,370)</b>	<b>3,318</b>	<b>4,611</b>	<b>5,969</b>	<b>7,411</b>
Financing activities					
<b>Proceeds from borrowings</b>	<b>4,699</b>	<b>9,068</b>	<b>9,230</b>	<b>10,881</b>	<b>12,224</b>
<b>Repayments of borrowings</b>	<b>(5,155)</b>	<b>(11,148)</b>	<b>(4,754)</b>	<b>(1,481)</b>	<b>(4,662)</b>
<b>Net cash from (used in) financing activities</b>	<b>1,890</b>	<b>13,580</b>	<b>4,476</b>	<b>9,400</b>	<b>7,562</b>
<b>Net increase in cash and cash equivalents</b>	<b>820</b>	<b>14,807</b>	<b>4,357</b>	<b>2,147</b>	<b>3,024</b>
Effect of foreign exchange rate changes	32	17	0	0	0
Cash and cash equivalents at beginning of the year	10,094	10,946	25,771	30,128	32,275

Source: Company data, AMTD Equity Research

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#### Stock Rating

<b>Buy</b>	Stock with potential return of over 20% over the next 12 months
<b>Hold</b>	Stock with potential return of -20% to +20% over the next 12 months
<b>Sell</b>	Stock with potential loss of over 20% over the next 12 months

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