



Fundamental, Incisive,
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Industry
Hong Kong Property

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F.I.T.T. for investors

Demographically challenged

[A deep dive into demographics suggests a dire outlook for property prices](#)

Following an in-depth demographic study for Hong Kong, we have turned more negative on housing demand. Taking into account weaker demand and rising supply (we published a FITT report on supply in Sept-16) we have cut our medium-term (2018E-21E) residential price forecasts significantly. We now expect vacancy to surge to 9% (4% now) and ASP to slide 48% by 2026 from current levels. We reiterate our view that developers will be forced to change their business model from land-banking to asset turnover. Hence, we overhaul our valuation methodology from discount-to-NAV to SOTP, using P/E to value development businesses. We downgrade HLD, Kerry and NWD to Hold.



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A deep dive into demographics suggests a dire outlook for property prices

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Several negative demographic trends

In this report, we identify several notable demographic trends in Hong Kong, with the most significant being: 1) natural population growth has already peaked and is likely to turn negative by around 2027; 2) reduced immigration; 3) the quick shrinkage of the 25-44 years age group to 26% of the total population by 2025, from 38% in 1995 (vs. 29% now); 4) the rise in people aged over 60 years to 30% of the total population, from the current 22%. Hong Kong already has the second-highest over-60 population in Asia, as a percentage of total population, behind Japan.

Aging population constrains financing, translating into lower affordability

In our view, housing affordability will be severely affected by an aging population. We believe affordability (debt servicing) is a function of property prices, mortgage rates, loan tenures and income. As the population ages, fewer households will be able stretch their mortgages to the maximum tenure of 30 years. On our new estimates, we expect only 11.5% of total households will be able to afford an average private housing unit by 2019. Moreover, by factoring in upcoming rate hikes, we expect overall affordability to worsen and ASP to decline by 48% over 2017-26 to restore the supply/demand equilibrium.

A new valuation methodology for property development – P/E approach

With improving supply and a bleak outlook for the physical market, we expect land-banking to fade as a business strategy, and we anticipate a growing focus on asset turnover. As a result, we believe a discount-to-NAV valuation methodology will become less relevant in valuing the developers, and we advocate adopting a P/E approach for the development businesses. For the investment properties owned by the HK Property companies, we continue to estimate NAVs based on cap rates. We then apply a discount to the investment property NAV of 34% (the average discount over the past 25 years).

Structural contraction in P/Es; downgrading Henderson Land, Kerry and NWD

Between 1995 and 2010, we estimate the market was implying an average sector P/E on the property development business of 29x. Post 2010, this contracted to 10x, as growth slowed, and we expect P/Es to contract further, to 5-7x (on 2019E earnings), given our market outlook. Taking into account our new residential price forecast and new valuation approach, we downgrade HLD, Kerry and NWD to Hold from Buy, while maintaining a Hold on SHKP and Sino-Land. Our new vs. old estimates and target prices are outlined in Figure 9.

Key Changes

Company	Target Price	Rating
0016.HK	117.00 to 118.50(HKD)	-
0017.HK	-	Buy to Hold
1113.HK	72.20 to 66.10(HKD)	-
0012.HK	56.20 to 49.80(HKD)	Buy to Hold
0683.HK	29.20 to 29.00(HKD)	Buy to Hold
0083.HK	14.10 to 14.30(HKD)	-

Source: Deutsche Bank

Top picks

CK Property (1113.HK),HKD61.30	Buy
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Source: Deutsche Bank

Companies Featured

SHK Properties Ltd (0016.HK),HKD124.10	Hold
CK Property (1113.HK),HKD61.30	Buy
Henderson Land Dev. Co. (0012.HK),HKD52.55	Hold
New World Dev (0017.HK),HKD10.78	Hold
Kerry Prop (0683.HK),HKD27.40	Hold
Sino Land Co (0083.HK),HKD14.02	Hold

Source: Deutsche Bank

Our target price is based on the sum-of-the-parts approach, which is our new valuation metric adopted for all HK developers under our coverage. Key risks to our view include policy change and unexpected fluctuations in the economy. We discuss valuation and risks in more detail in the Valuation and Risks section on p.36.



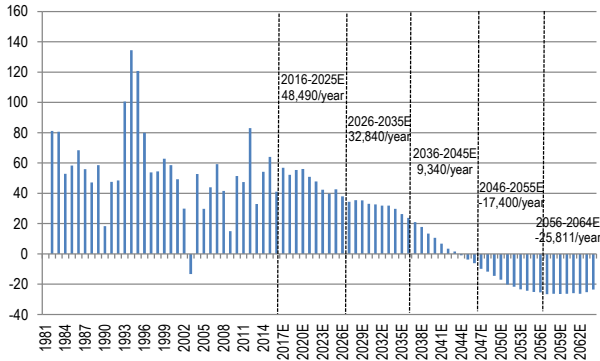
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Key charts

Figure 1: Government expects population growth to slow down materially and to peak in 2043 at 8.22m



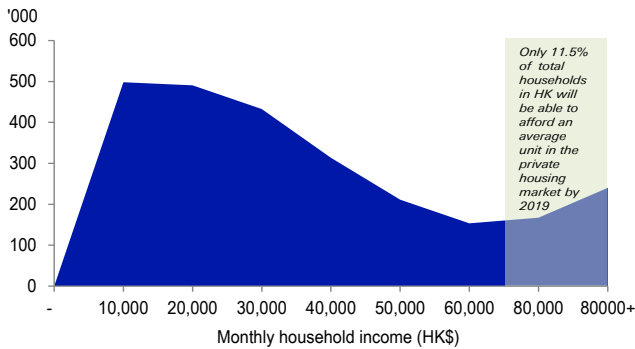
Source: Census & Statistics Department; Deutsche Bank estimates * Numbers represent net change in population in ('000)

Figure 2: Government versus Deutsche Bank's forecasts on new housing demand in 2017-2026

	2015/16-2024/25	2016/17-2025/26	2017/18-2026/27	DB's forecast in 2017-2026E
New households added	282,800	247,800	237,700	196,970
Redevelopment relocation inadequately households	39,100	45,400	62,900	37,344
Miscellaneous factors	105,600	106,600	105,500	94,000
Allowance for vacancy	18,500	18,500	17,500	-
Total (rounded up)	480,000	460,000	460,000	338,314

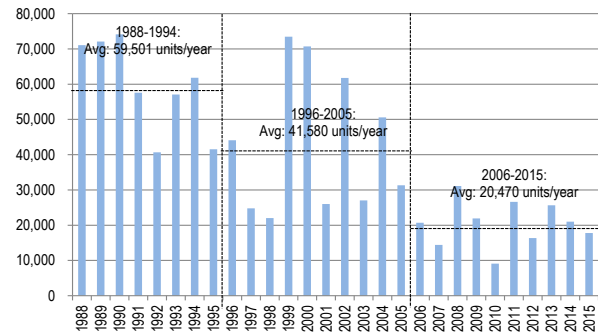
Source: Transport and Housing Bureau; Deutsche Bank estimates

Figure 3: Only 11.5% of total households in HK will be able to afford an average unit in the private housing market by 2019 (y-axis)



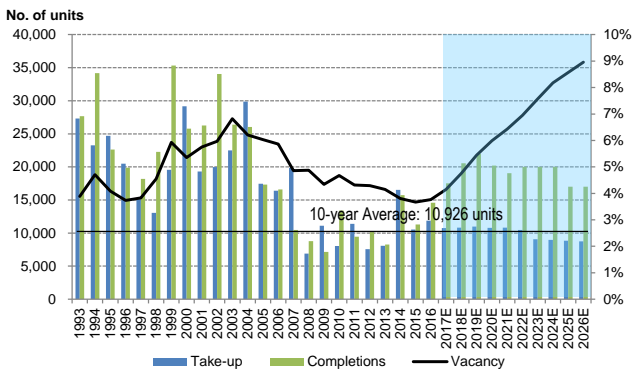
Source: Census & Statistics Department; Deutsche Bank

Figure 4: Housing take-up in HK slowed down markedly in the past decade, mirroring the worsening demographic trends



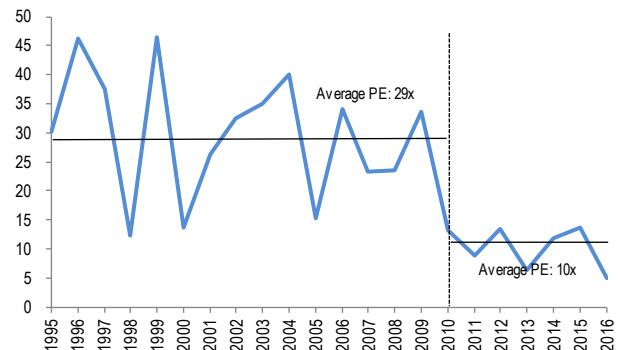
Source: Rating & Valuation Department; Deutsche Bank

Figure 5: Vacancy rate is expected to more than double to 9% by 2026 on stagnant demand/rising supply



Source: Rating & Valuation Department; Land Registry; Deutsche Bank estimates

Figure 6: Structural contraction in implied P/E multiples for property development in an ex-growth market



Source: Company data; Bloomberg Finance LP; Deutsche Bank



Key investment conclusions

Demand outlook

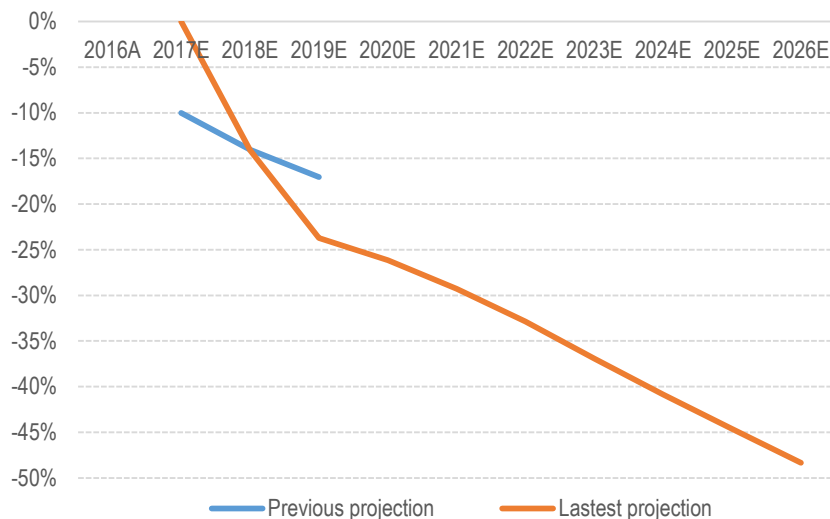
- Only 16.9% of total households in Hong Kong can afford an average unit in the private housing market at the current record low interest rate and the maximum mortgage tenure of 30 years. Total households that can afford such units will decline significantly, to just 11.5% by 2019, on our estimates, on shorter loan tenures (due to the aging population) and higher interest rates.
- Overall housing take-up has declined markedly in the past decade, mirroring the deceleration in population growth. We estimate total housing demand of 338,314 in 2017-26. This compares with new supply of 429,296 over the same period.

Please refer to the Appendix for the detailed findings of our proprietary demographic study

Supply outlook

- Supply will increase materially from now onwards, as land supply has normalized since 2011. Completion in the Hong Kong private housing market will average 19,330 units/year in 2017-26, markedly above the 10-year average of 10,926 units (see our report, "The Game has changed", published on 14 September 2016).
- We expect a private housing supply surplus of 93,781 in 2017-26 and residential prices to fall by 48%, to restore the supply/demand equilibrium.

Figure 7: Deutsche Bank's Hong Kong residential property price forecasts



Source: Deutsche Bank estimates

New earnings estimates

- Our new earnings estimates are higher for 2017 and 2018, reflecting the fact that residential prices YTD have been stronger than we had expected (which will affect 2018 earnings depending on when projects are booked). Our earnings estimates for 2019 (and beyond) are, however, significantly lower, reflecting our more bearish view on residential prices beyond this year.



New valuation approach

- We now regard a P/E approach as more appropriate to value the development businesses, because developers are expected to focus more on asset turnover (vs. land-banking), on the back of a normalization in land supply ahead and in the face of a bleak market outlook for physical prices, which will undermine the benefits of holding a landbank.
- Taking into account our negative view on demand and supply fundamentals, we believe applying a 5-7x P/E is fair (the point within this range is determined by a number of factors discussed on page 23). We show our target price (TP) changes below, which include material downward revisions for Henderson and Cheung Kong Property.
- We also show our NAV estimates below for reference. As already discussed, the overall company's NAV is no longer a driver of our target prices. We have raised our NAV estimates reflecting a much stronger-than-expected residential market YTD.

Figure 8: Summary of earnings revisions (HK\$m)

Developer	FY17E			FY18E			FY19E		
	New	Old	%	New	Old	%	New	Old	%
Cheung Kong Property	18,313	15,677	17%	15,885	15,311	4%	17,235	15,762	9%
Sun Hung Kai Properties	26,789	24,692	8%	25,137	24,858	1%	22,412	24,566	-9%
Sino Land	5,045	5,265	-4%	4,972	4,902	1%	4,504	4,720	-5%
Henderson Land	12,452	10,993	13%	12,195	10,976	11%	10,308	10,500	-2%
New World Development	7,106	6,525	9%	6,943	7,104	-2%	6,175	6,293	-2%
Kerry Properties	4,914	4,553	8%	3,635	3,295	10%	4,993	5,030	-1%

Source: Deutsche Bank estimates

Figure 9: Summary of NAV/TP revisions for HK developers (HK\$) – due to stronger-than expected property market YTD

Developer	Rating	Share price @ 6 June	Implied upside	DP (a)	IP (b)	Others (c)	New TP (a+b+c)	Old TP	%	New NAV	Old NAV	%
Cheung Kong Property	Buy	61.3	8%	25.80	41.26	-0.98	66.1	72.2	-8%	103.1	90.3	14.2%
Sun Hung Kai Properties	Hold	124.1	-5%	13.51	123.46	-18.43	118.5	117.0	1%	195.6	179.6	8.9%
Sino Land	Hold	14.02	2%	1.77	10.43	2.21	14.3	14.1	1%	22.1	20.2	9.2%
Henderson Land	Hold	52.55	-5%	3.60	30.50	15.70	49.8	56.2	-11%	80.1	74.9	6.9%
New World Development	Hold	10.78	3%	3.63	12.74	-5.33	11.1	11.1	-	20.0	18.4	8.7%
Kerry Properties	Hold	27.4	6%	12.70	32.30	-16.00	29.0	29.2	-1%	61.0	53.0	15.1%

Source: Deutsche Bank estimates

(a): Development properties; (b): Investment properties; (c) Includes other assets and net debt



Demand outlook

Aging population imposes financing constraints, translating into lower affordability of housing

- Only 16.9% of total households in Hong Kong can afford an average unit in the private housing market at the current record low interest rate and the maximum mortgage tenure of 30 years. Total households that can afford such units will decline sharply, to just 11.5% by 2019, on our estimates, due to shorter loan tenures, owing to the aging population and higher interest rates.
- Overall housing take-up has declined markedly in the past decade, mirroring the deceleration in population growth. We estimate aggregate housing demand of 338,314 in 2017-26.
- We expect a shortfall of 2,799 public units but a surplus of 93,781 private units in the next 10 years, based on our housing demand projection and the latest land supply situation revealed by the government.
- Please refer to our Appendix for more details on our demographic outlook. We outline key findings including a further slowing population growth and a rising proportion of the 60+ age group. In addition, the working population is likely to peak next year and decline thereafter.

Fewer households are entitled to maximum loan tenure as population ages

In our view, housing affordability will be severely affected by an aging population. Specifically, we see housing affordability (debt-servicing ratio, or DSR) as a function of property price, mortgage rate, loan tenure, and income. As the population ages, fewer households will be able to stretch their mortgages to the maximum tenure of 30 years.

The HKMA has imposed eight rounds of tightening on lending criteria since October 2009 (Figure 10 and Figure 11). According to the current measure, the maximum loan-to-value ratio (LTV) for properties with a lump-sum value below HK\$7m is capped at 60%, and for properties valued above HK\$10m, the LTV is capped at 50%. Moreover, all banks and their affiliates must stick to a 50% cap on DSR, i.e. mortgage applicants will not receive approval from banks and their affiliates if the monthly mortgage instalment exceeds 50% of household income. In addition, there is a stress test applicable to mortgage applicants that the DSR cannot exceed 60% by hypothetically assuming a 300bp interest rate hike.

Figure 10: Summary of maximum LTV imposed on residential mortgages

Date	Maximum loan-to-value (LTV)					
	<HK\$7m	HK\$7-8m	HK\$8-10m	HK\$10-12m	HK12-20m	>HK\$20m
Prior to Oct-09	70%	70%	70%	70%	70%	70%
Oct-09	70%	70%	70%	70%	70%	60%
Aug-10	70%	70%	70%	70%	60%	60%
Nov-10	70%	70%	60%	60%	50%	50%
Jun-11	70%	60%	60%	50%	50%	50%
Sep-12	70%	60%	60%	50%	50%	50%
Feb-13	70%	60%	60%	50%	50%	50%
Feb-15	60%	60%	60%	50%	50%	50%
May-17	60%	60%	60%	50%	50%	50%

Source: HKMA; Deutsche Bank



Figure 11: Summary of maximum LTV/loan cap under different criteria

	First property (no previous mortgage outstanding)		Subsequent properties (with previous mortgage outstanding)	
	With HK income	Without HK income	With HK income	Without HK income
Self-occupied units				
<HK\$7m	60%	50%	50%	40%
HK\$7-8m	60% (loan cap at HK\$5m)	50% (loan cap at HK\$4m)	50% (loan cap at HK\$4m)	40% (loan cap at HK\$3m)
HK\$8-10m	60% (loan cap at HK\$5m)	50% (loan cap at HK\$4m)	50% (loan cap at HK\$4m)	40% (loan cap at HK\$3m)
HK\$10-12m	50%	40%	40%	30%
HK\$12-20m	50%	40%	40%	30%
>HK\$20m	50%	40%	40%	30%
Non-self-occupied units	50%	40%	40%	30%
Net-worth-based mortgages	40%	40%	30%	30%

Source: HKMA; Deutsche Bank

Those who cannot meet the 40% minimum down payment requirement can obtain mortgage insurance from the Hong Kong Mortgage Corporation (HKMC), where the buyer can borrow a higher LTV by paying a mortgage insurance premium ranging from 2.6-4.35% of the original principal. Specifically, LTV is capped at 80% for properties valued up to HK\$6m, subject to a debt-to-income cap of 50% and a stress test debt-to-income cap of 60%. For first-time home buyers, the maximum LTV is capped at 90% for properties valued up to HK\$4m, but the maximum debt-servicing ratio (DSR) is capped at 45% (stress test debt-to-income cap at 55%).

16.9% of households can afford a home on 30-year tenure/current interest rate

The average unit in the private housing market in Hong Kong currently costs HK\$9.014m on our analysis. At the prevailing mortgage rate of 2%, the monthly mortgage instalment would range from HK\$19,991 to HK\$66,354, depending on the loan tenure and LTV ratio (Figure 12). Note that the sensitivity analysis for LTV of 70% and 80% is for illustrative purposes only, as the maximum LTV ratio is capped at 60% for properties over HK\$7m in value under the latest mortgage lending guidelines by the HKMA.

Figure 12: Sensitivity on mortgage instalment to loan tenure and LTV*

Mortgage Loan Tenure (years)	Loan-to-value ratio		
	80%	70%	60%
10	66,354	58,060	49,765
15	46,406	40,605	34,804
20	36,481	31,921	27,361
25	30,566	26,745	22,924
30	26,654	23,323	19,991

Source: Deutsche Bank estimates * Assuming prevailing mortgage rate of 2%

Taking into account our belief that most buyers will take out a second mortgage on the same property through various non-bank financial institutions, we assume an effective LTV of 70% in our analysis.



Figure 13: Mortgage instalment for an average private housing unit in HK

	First mortgage (a)	Second mortgage (b)	Total (a+b)
Property value (HK\$)	9,014,160	9,014,160	9,014,160
LTV (%)	55%	15%	70%
Mortgage principal (HK\$)	4,957,788	1,352,124	6,309,912
Mortgage rate p.a. (%)	2%	3%	NA
Loan tenure (years)	30	25	NA
Monthly repayment (HK\$)	18,325	6,412	24,737

Source: Deutsche Bank estimates

Figure 14: Minimum monthly household income required for the purchase of an average private housing unit in Hong Kong under stress test

	First mortgage (a)	Second mortgage (b)	Total (a+b)
Property value (HK\$)	9,014,160	9,014,160	9,014,160
LTV (%)	55%	15%	70%
Mortgage principal (HK\$)	4,957,788	1,352,124	6,309,912
Mortgage rate p.a. (%)*	5%	6%	NA
Loan tenure (years)	30	25	NA
Monthly repayment (HK\$)	26,614	8,712	35,326
Debt-servicing ratio on first mortgage under stress test			60%
Minimum household income/month (HK\$)			58,877

Source: Deutsche Bank estimates * Stress test assumes 300bps mortgage rate hike from current level

Based on the prevailing mortgage interest rate of 2% p.a., a maximum loan tenure of 30 years and an effective LTV of 70%, the monthly instalment would be HK\$24,737 for the average unit in the private housing market in Hong Kong (Figure 13). By taking into account the stress test imposed by the HKMA, the minimum monthly household income required to buy an average unit in the private housing market in Hong Kong is HK\$58,877 (Figure 14). As of end-2016, 425,000 (16.9%) out of a total of 2,507,000 households in HK earn such a monthly household income (Figure 17).

Figure 15: Sensitivity analysis of loan tenure and mortgage interest rates on monthly mortgage instalment (HK\$)

	Mortgage loan tenure (years)				
	10	15	20	25	30
2.00%	52,030	38,316	31,493	27,426	24,737
2.25%	52,587	38,890	32,084	28,034	25,363
2.50%	53,149	39,470	32,683	28,653	26,001
2.75%	53,715	40,057	33,291	29,283	26,652
3.00%	54,285	40,649	33,908	29,922	27,314
3.25%	54,859	41,249	34,532	30,572	27,989
3.50%	55,437	41,854	35,165	31,232	28,675
3.75%	56,020	42,466	35,806	31,901	29,372
4.00%	56,607	43,084	36,455	32,581	30,081
4.25%	57,198	43,708	37,112	33,270	30,801
4.50%	57,794	44,339	37,777	33,969	31,532
4.75%	58,393	44,975	38,450	34,677	32,274
5.00%	58,997	45,618	39,131	35,395	33,026
5.25%	59,605	46,266	39,820	36,121	33,789
5.50%	60,217	46,921	40,516	36,857	34,562

Source: Deutsche Bank estimates

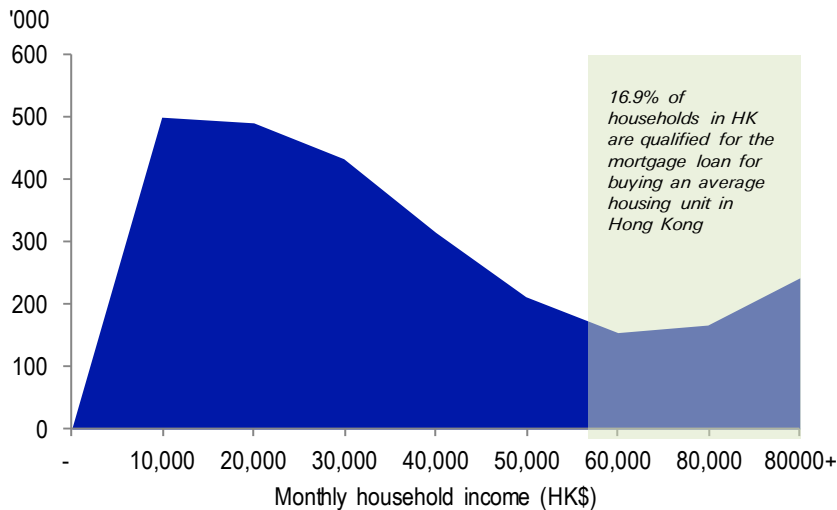


Figure 16: Sensitivity analysis of loan tenure and mortgage interest rates on minimum monthly household income required under stress test (HK\$)

Mortgage interest rate (%)	Mortgage loan tenure (years)				
	10	15	20	25	30
2.00%	104,060	79,863	69,052	62,824	58,877
2.25%	105,529	81,290	70,546	64,382	60,494
2.50%	107,012	82,732	72,056	65,958	62,132
2.75%	108,509	84,187	73,583	67,553	63,790
3.00%	110,020	85,655	75,126	69,166	65,468
3.25%	111,544	87,137	76,685	70,797	67,165
3.50%	113,082	88,633	78,260	72,446	68,881
3.75%	114,634	90,142	79,850	74,112	70,615
4.00%	116,199	91,663	81,456	75,794	72,367
4.25%	117,778	93,198	83,077	77,493	74,136
4.50%	119,370	94,745	84,712	79,209	75,922
4.75%	120,975	96,305	86,362	80,940	77,724
5.00%	122,594	97,877	88,027	82,687	79,542
5.25%	124,225	99,461	89,705	84,448	81,376
5.50%	125,869	101,058	91,397	86,225	83,224

Source: Deutsche Bank estimates

Figure 17: Number of households that can afford to buy an average private housing unit in Hong Kong at current mortgage rate/loan tenure



Source: Census and Statistics Department, Deutsche Bank

Number of households that qualify to buy will dramatically decline in future

As a result of an aging population along with an interest-rate hike, the number of households that qualify to buy a home will dramatically decline, in our view. In our analysis, assuming household income and the mortgage lending rate hold static, borrowing capacity will be reduced by 8.2%/18.7% for a five-year/10-year reduction in mortgage loan tenure (Figure 18). In addition, by factoring in the upcoming interest-rate hike, we expect overall affordability to further worsen. For instance, by assuming a 100bps hike in the mortgage interest rate alongside a reduction of loan tenure by 10 years (i.e., from 30 years to 20 years), buyers' borrowing capacity will be correspondingly reduced by 25.1%.



Figure 18: Sensitivity analysis of borrowing capacity on loan tenure and mortgage interest rates

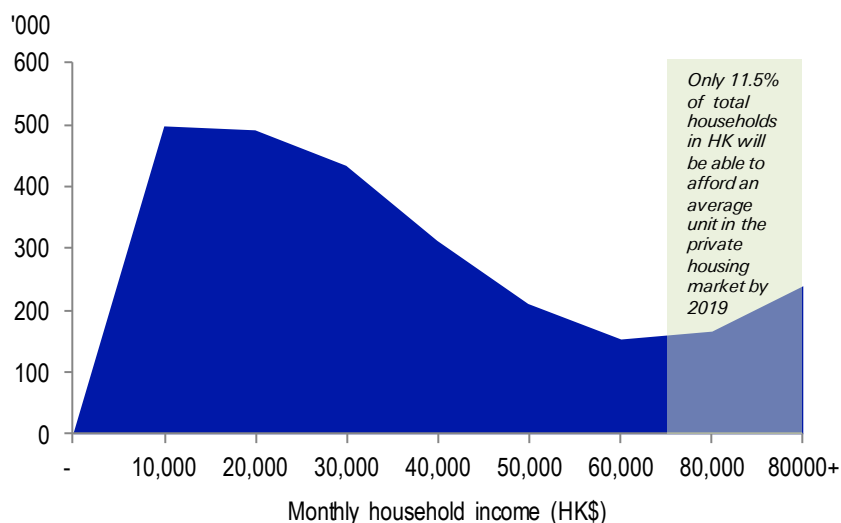
		Mortgage interest rate p.a. (%)			
		2.0%	2.5%	3.0%	3.5%
Loan tenure (years)	30	0.0%	-5.5%	-10.5%	-15.1%
	25	-8.2%	-12.6%	-16.7%	-20.5%
	20	-18.7%	-22.0%	-25.1%	-28.0%
	15	-32.1%	-34.3%	-36.4%	-38.4%

Source: Deutsche Bank estimates

Deutsche Bank expects seven US interest rate hikes in the next 24 months. If we incorporate our house view, the mortgage interest rate in Hong Kong is expected to rise to 3.75% by 2019 (from 2% currently). If the mortgage loan tenure remains unchanged, at 30 years, the monthly mortgage instalment will increase by 24%, to HK\$30,669 (from HK\$24,737 currently), and the minimum monthly household income required will correspondingly increase to HK\$70,615 (from HK\$58,877 currently). Assuming no change in earning power, this higher mortgage interest rate will reduce a household's borrowing capacity by 17.2%.

If we take into account an aging population (e.g. if loan tenure is reduced to 25 years), the monthly mortgage instalment will increase further, to HK\$33,198, and the minimum monthly household income required will increase to HK\$74,112. Under this scenario, the number of households that can afford to buy an average unit in the private housing market in Hong Kong will be reduced by 32%, to just 289,000, or 11.5% of total households (Figure 19).

Figure 19: Number of households that can afford to buy an average private housing unit in HK by 2019 due to aging population and higher interest rates



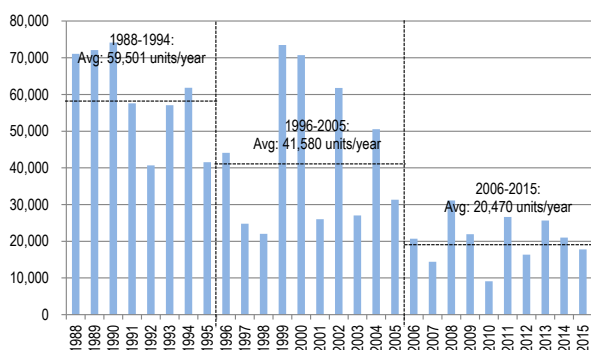
Source: Census and Statistics Department, Deutsche Bank



Overall housing take-up has slowed down markedly in the past decade

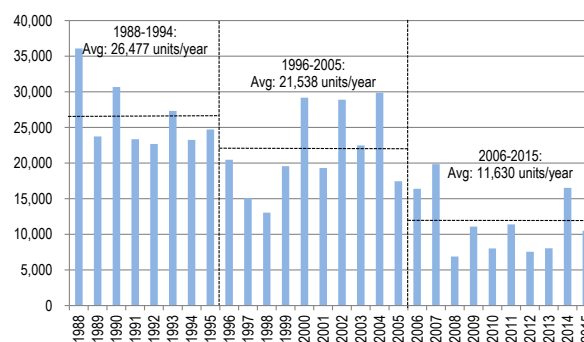
There has been a softening trend in total housing take-up in the past decade, which is in line with the worsening demographic trend over the same period. Specifically, overall housing take-up slowed to 20,470/year in 2006-15, from 41,580/year in the prior decade (Figure 20), while population growth correspondingly slowed to 17,830/year in 2006-15, from 33,520/year in the prior decade. Meanwhile, take-up in the private sector fell to 11,630/year in 2006-15 from 21,538/year in the prior decade and, in the public sector, it fell to 8,840/year from 21,645/year (Figure 21 and Figure 22). According to government statistics, the private sector has made up about 60% of total housing take-up in the past 20 years.

Figure 20: Overall housing take-up in Hong Kong



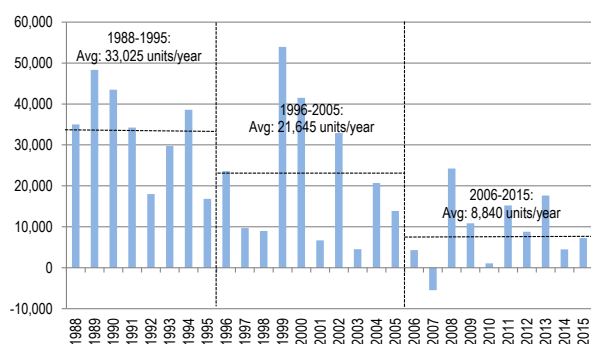
Source: Rating & Valuation Department; Deutsche Bank estimates

Figure 21: Take-up in the private housing segment



Source: Rating & Valuation Department; Deutsche Bank estimates

Figure 22: Take-up in the public housing segment



Source: Rating & Valuation Department; Deutsche Bank estimates

Housing take-up was understated by statistical treatment of sub-divided units

In our view, the increase in the number of households should bring a corresponding rise in housing take-up. However, housing take-up in the past decade has fallen short of the number of households added over the same period (Figure 24). The key reason for the short fall was the surge in sub-divided units, which the statistics captured as one unit being taken up, despite there being several households staying in the sub-divided unit (SDU).



The government published a report on sub-divided units in Mar-16 (Figure 22) and revealed that there were a total of 25,200 residential units that have been sub-divided into 88,800 units (i.e. average of 3.5 sub-divided units per residential unit). Meanwhile, there are 87,600 households with total population of close to 200,000 staying in the sub-divided flats. Among those who stay in sub-divided flats, median monthly household income stood at HK\$12,500 and median monthly rent (at HK\$4,200) accounted for 32% of income, on average (Figure 23).

Figure 22: Sub-divided unit survey by the government

Year	No of residential units being sub-divided	Total no of SDUs	Average number of SDUs per residential unit	No of households living in SDUs	Population living in SDUs
2013	18,800	66,900	3.56	66,900	171,300
2014	24,600	86,400	3.51	85,500	195,500
2015	25,200	88,800	3.52	87,600	199,900

Source: Census & Statistics Department, Deutsche Bank

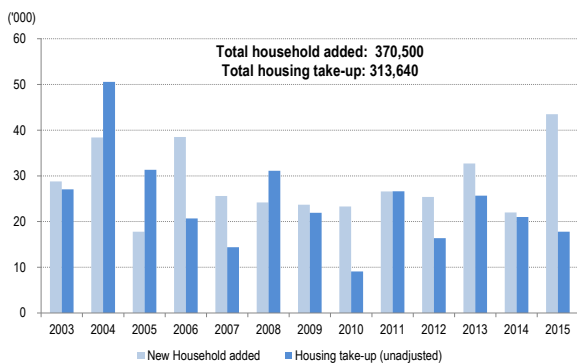
Figure 23: Sub-divided unit survey by the government

Year	No. of households living in SDUs	Population living in SDUs	Avg. household size	Avg. living space per capita (sf)	Median monthly rent (HK\$)	Median monthly household income (HK\$)	Median rent to income ratio (%)
2013	66,900	171,300	2.56	67.9			
2014	85,500	195,500	2.29	61.8	3,800	11,800	30.80%
2015	87,600	199,900	2.28	62.4	4,200	12,500	32.30%

Source: Census & Statistics Department, Deutsche Bank

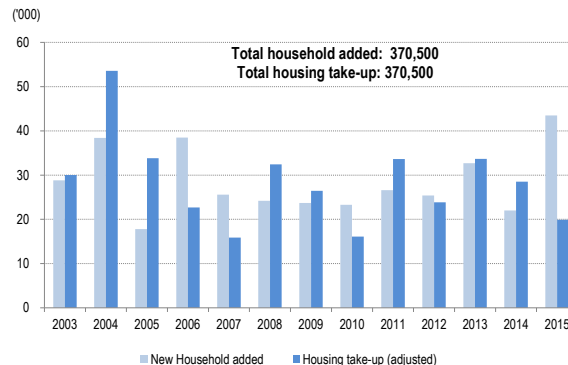
By adjusting for the statistic treatment (i.e., reclassifying the sub-divided units as separate take-up), aggregate housing take-up matched the corresponding new households added (the mismatch between household formation and housing take-up in a particular year is due to the timing difference in the statistics between new household formation and actual housing take-up) (Figure 25). Meanwhile, the split between private and public on the adjusted housing take-up is 39:61 (Figure 26 and Figure 27).

Figure 24: Unadjusted housing take-up versus new households added



Source: Rating & Valuation Department, Deutsche Bank estimates

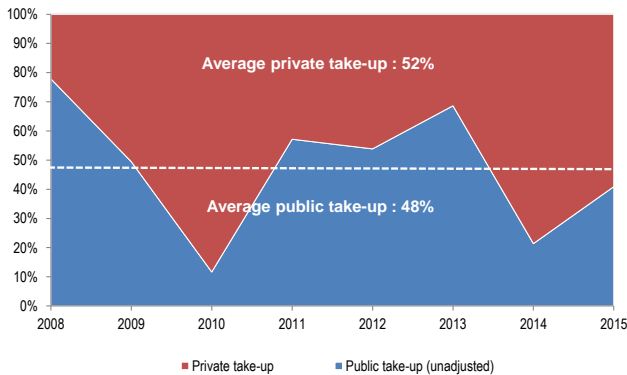
Figure 25: Adjusted housing take-up versus new households added



Source: Rating & Valuation Department, Deutsche Bank estimates

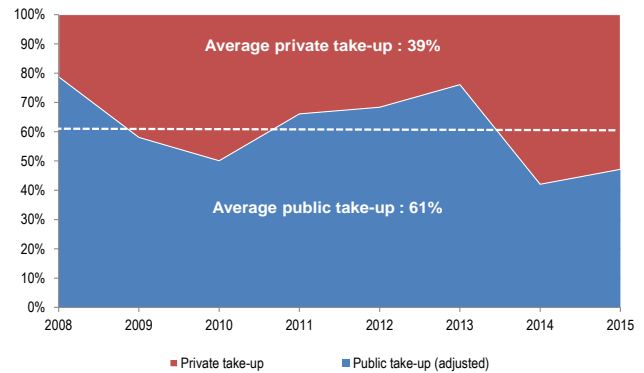


Figure 26: Housing demand split between private and public sector



Source: Rating & Valuation Department; Deutsche Bank estimates

Figure 27: Adjusted housing demand split between private and public sector



Source: Rating & Valuation Department; Deutsche Bank estimates

We estimate total housing demand of 338,314 units in the next 10 years

The HKSAR government first published the Long Term Housing Strategy Annual Report in 2014 and a progress report has been made available every year since (Figure 29). In the latest report, published in December 2016, the government projected that 460,000 residential units are needed as to satisfy the housing need for the 10-year period from 2017/18 to 2026/27.

Figure 29: Government versus Deutsche Bank's forecasts on new housing demand in 2017-2026

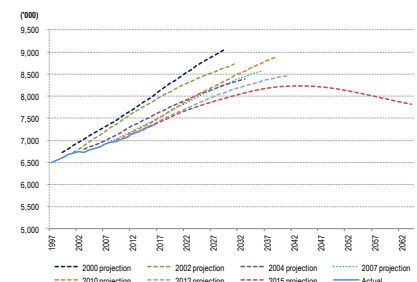
	2015/16-2024/25	2016/17-2025/26	2017/18 - 2026/27	DB's forecast in 2017-2026E
New households added	282,800	247,800	237,700	196,970
Redevelopment relocation	39,100	45,400	62,900	37,344
Inadequately households	105,600	106,600	105,500	94,000
Miscellaneous factors	36,000	36,700	33,400	10,000
Allowance for vacancy	18,500	18,500	17,500	-
Total (rounded up)	480,000	460,000	460,000	338,314

Source: Transport and Housing Bureau; Deutsche Bank

The government lowered its 10-year housing demand projection to 460,000 in December 2016 (from 480,000 in December 2014). Specifically, the housing demand projection from new household formation saw the largest decline, which is in line with the softening population growth. Indeed, projections from the government tend to overestimate actual demand (Figure 28 and Figure 30), which we believe is not unreasonable for resource planning purposes.

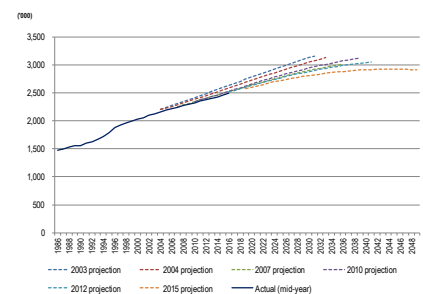
After analysing the prevailing demographic trend (please refer to the Appendix) and assuming that an increase in new households would bring a corresponding rise in housing take-up, we estimate that 196,970 residential units (Figure 31) will be needed in the next 10-year period (2017-26). After taking into account housing demand stemming from redevelopment relocation, inadequately housed households and other housing demands, we project total housing demand of 338,314, some 26% lower than the government's current projection (please refer to Figures 32 and 33 for detailed assumptions of our forecasts).

Figure 28: Government projections on Hong Kong population



Source: Census & Statistics Department; Deutsche Bank

Figure 30: Government projections on Hong Kong households



Source: Census & Statistics Department; Deutsche Bank



Figure 31: Deutsche Bank's forecasts for new household additions during 2017-26

	2017-26	Remarks
Household formation derived from new marriages	146,819	A shrinking number of people in the 25-34 age group should lead to a decline in the number of first-time marriages. Specifically, total population in this age group is expected to decline by 7% from 1.1m in 2016 to 1m in 2026, based on the government's latest population projection. Referencing the last period (1996-05) when we saw shrinkage in the 25-34 age group, first-time marriages saw a corresponding slowdown. Our projection assumes marriage rate at 2.9%, in line with historical average in 1996-16. Our projection is further adjusted for non-permanent resident marriages that we believe will not contribute to the increase in new households as they are likely to relocate outside HK. The adjustment rate we adopted is 49%-51% of total first time marriage, which is in line with the growing trend witnessed in the 10 years
Net increase in one-person households	67,391	Based on government projections for public housing units to be allocated to one-person households per annum (i.e. up to 2,200 public housing units to be allocated to non-elderly, one-person households, 2,400 public housing units to be allocated to elderly, one-person households, and about 1,910 subsidized housing units). We also assume a net addition of 925 one-person households in the private sector per year, slightly above the historical average of 899/year as a result of more small units (catered for one-person households) scheduled for completion
Immigration/expat movements	(17,366)	We generally expect the declining trend in expatriate population witnessed since 1996 to continue, but at a moderating pace from -5.3% in 2016 to -5% in 2017/18, further to -4.5% in 2019-21 and -3% in 2022-26
Departure of HK households	(27,480)	Based on the average number of departures of Hong Kong households in the past 10 years. The absolute number of departures has been quite consistent for the past eight years, ranging from 2,400 to 2,800 households per annum
Others	27,606	Based on the declining trend witnessed in the past few years, where there were only 4,060 households added per year in the past 5 years, markedly below 6,471 households per year in the prior 5 years. Others mostly refer to the relocation of departed Hong Kong households back to Hong Kong
Total	196,970	

Source: Deutsche Bank estimates

We further break down our housing demand projections by segment, where we project housing demand of 238,799 from the public sector and 99,515 from the private sector in the next 10 years, which implies a split between the public and private sectors of 69:31 (in line with the historical housing demand split between the private and public sector as shown in Figure 27).

Figure 32: Deutsche Bank's forecasts for Hong Kong housing demand by segment in 2017-26

	Total housing demand	Public sector	Private sector
New household added*	196,970	120,152	76,818
Redevelopment relocation**	37,344	24,647	12,697
Inadequately housed households^	94,000	94,000	-
Miscellaneous factors~	10,000	-	10,000
Total	338,314	238,799	99,515

Source: Deutsche Bank estimates

* Based on the historical adjusted housing take-up between the public and private sector at 61:39

** The split is based upon our assumed split for redevelopments between the public and private housing segments

^ Housing demand likely to skew towards the public sector by considering the median household income

~ Housing demand from mobile population/Non-local students more likely to go for private housing sector

Figure 33: Deutsche Bank projection for new households added in Hong Kong

	2010	2011	2012	2013	2014	2015	2016	2017F	2018F	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F
Number of first-time marriages	35,826	39,979	40,841	35,703	37,217	34,046	32,000	32,019	31,999	32,094	32,158	32,248	32,283	26,141	25,568	25,487	24,494
Adjustment for marriages to PRC	(16,041)	(18,159)	(18,474)	(16,309)	(17,645)	(16,378)	(15,680)	(15,817)	(15,807)	(15,983)	(16,015)	(16,188)	(16,206)	(13,227)	(12,937)	(12,998)	(12,492)
Net increase in one-person households	7,000	11,100	6,400	(300)	10,900	22,200	7,377	7,897	7,963	8,029	7,458	7,516	5,983	6,012	6,040	5,231	5,262
Movement of expatriate population	2,526	2,006	(3,797)	(1,867)	(4,312)	(3,576)	(2,986)	(2,672)	(2,538)	(2,170)	(2,073)	(1,979)	(1,260)	(1,222)	(1,186)	(1,150)	(1,116)
Departure of HK households	(2,441)	(2,823)	(2,594)	(2,603)	(2,371)	(2,414)	(2,500)	(2,748)	(2,748)	(2,748)	(2,748)	(2,748)	(2,748)	(2,748)	(2,748)	(2,748)	(2,748)
Others	1,330	(903)	3,324	10,276	2,811	922	3,000	3,045	3,075	3,133	3,061	3,072	2,942	2,438	2,402	2,253	2,184
TOTAL HOUSEHOLD ADDED	28,200	31,200	25,700	24,900	26,600	34,800	21,211	21,723	21,943	22,355	21,843	21,921	20,994	17,393	17,139	16,075	15,585

Source: Deutsche Bank estimates

Figure 34: Further details on our Hong Kong housing demand assumptions

	2017-26	Remarks
New household added	196,970	Based on DB's projection of 196,970 new households to be added in the next 10 years (2017-26) and by assuming the increase in new households would bring a corresponding rise in housing take-up
Redevelopment relocation	37,344	Based on the average number of units demolished for redevelopment in the past 10 years (public sector at 20,900 units and private sector at 16,444)
Inadequately housed households	94,000	Comprising 30,000 households living in temporary housing or non-residential buildings or sharing with other households (according to latest census). Moreover, of the 87,600 households currently staying in sub-divided units (SDUs), there are 64,000 households who expressed not satisfied with their living environment are captured in redevelopment relocation
Miscellaneous factors	10,000	Comprising increase of 7,000 households with mobile population based on past trends from census. Meanwhile, as the number of Mainland students studying in Hong Kong shows signs of peaking, we are expecting housing demand from non-local students/Mainland expatriates of merely 3,000 in the next 10 years (versus the government's projection of 6,900)
Allowance for vacancy	-	Given that the total number of private residential units has well exceeded the total number of private households and is well above natural vacancy allowance of 5%, the further allowance for vacancy is not needed, in our view
Total	338,314	

Source: Deutsche Bank estimates





Supply outlook

Supply to increase materially from now onwards

- Supply will likely increase materially from now onwards. Completion in the Hong Kong private housing market will average 19,330 units/year in 2017-26, 77% above the 10-year (2007-16) average of 10,926 units, on our estimates.
- We expect a private housing supply surplus of 93,781 in 2017-26, as residential prices fall by 48%, to restore the supply/demand equilibrium over this period. We had previously expected ASP to decline by 21% in 2017-19.
- We published a FITT report “The Game has changed” on 14 September 2016 where we pointed out that Hong Kong is not running out of land and land supply has normalized since 2011. In this report, we estimate the potential supply from the conversion of agricultural land held by four major developers can be as much as 1.05m private residential units, or 67% of the current stock.

Completion in private residential market to surge by 77% in 2017-26

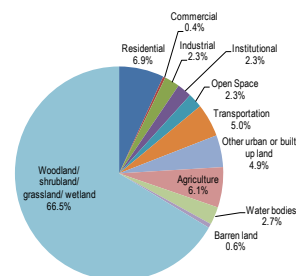
There is a widely held perception that Hong Kong has run out of land. When we look at the land utilization breakdown published by the Planning Department, we see that out of the total 1,110 sq km of land in Hong Kong, only about 30% of land has been utilized as of 2014, of which 6.1% is agricultural land that we believe will gradually be rezoned for other uses. Hence, effective land utilization is merely at 24% as of end-2014 (Figure 35).

While we agree that rezoning could be a lengthy process, in particular with the potential rezoning of woodland/shrubland/grassland/wetland (making up 66.5% of current land use) where there is more awareness regarding environmental protection, Hong Kong has not run out of land resources. Indeed, rezoning historically has been one of the most common ways to increase land supply, along with other alternative ways such as land reclamation, which has added some 60 sq km in land area, equivalent to over 5% of total land area.

Looking ahead, we see a normalization of land supply following an acceleration of the land development programme since 2013. On top of boosting short-to-medium-term land supply via rezoning, increasing development density, and conducting land use reviews on suitable sites, the government is proactively pushing for New Development Areas and new town extension, review of agricultural land and brownfield sites in the New Territories, planning for the long-term development in New Territories North and Lantau Island, and exploring land reclamation, rock cavern and underground space developments to ensure a sustainable medium-to-long-term land supply. Consequently, we anticipate the corresponding increase in completion in the Hong Kong private residential market from now onwards.

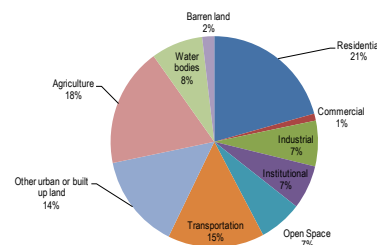
Specifically, we expect completion of 17,515 units in 2017, implying a 20% YoY increase, as well as the highest completion since 2005. Looking beyond, we anticipate that new completions in 2017-26 will average 19,330 units/year, markedly above the 10-year (2007-16) average of 10,926 units. In particular,

Figure 35: Land utilization in Hong Kong*



Source: Planning Department, Deutsche Bank * As of 2014

Figure 36: Land utilization in Hong Kong (excluding woodland/shrubland/grassland/wetland)*

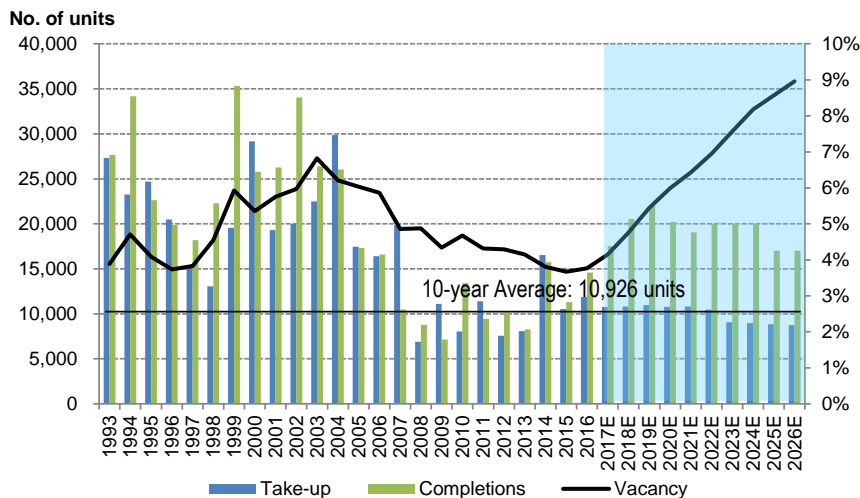


Source: Planning Department, Deutsche Bank * As of 2014



we expect a new completion peak of 21,984 units in 2019, the highest level of completion since 2004 (Figure 37).

Figure 37: Hong Kong private residential supply, take-up and vacancy rate



Source: CEIC, Deutsche Bank estimates

Conversion of agricultural land potentially adds 1.05m of private supply

Agricultural land is indeed the second largest category of land use in Hong Kong (by excluding unutilized land of woodland/shrubland/grassland/wetland) at 18% of total land area, just behind residential at 21%. Nevertheless, the pace of usage conversion for agricultural land has been rather slow in the past, with merely 200 hectares (21.5m sf) of agricultural land rezoned during 1994-2001, according to the Planning Department.

In light of the government's proactive push to boost residential supply, some developers have highlighted that the pace of land-use conversion has notably accelerated in recent months. In our analysis, the four major developers in Hong Kong collectively own 105m sf of agricultural land, which is adequate to add up to 1.05m units (or 67% of current stock) assuming all agricultural land plots can be rezoned for residential use at maximum plot ratio of 5x (Figure 38).

This potential source of supply is in addition of existing land bank owned by developers and the government's land reserve pipeline, highlighting that Hong Kong is not running out of land but supply has been artificially capped by policies in the past.

Figure 38: Summary of agricultural land reserve held by four major developers and potential supply based on different plot ratios

	Agricultural land reserve (sf)	Plot ratio		
		3.6x	4x	5x
CK Prop	13,000,000	93,600	104,000	130,000
SHKP	30,000,000	216,000	240,000	300,000
Henderson Land	44,800,000	322,560	358,400	448,000
New World	17,500,000	126,000	140,000	175,000
Potential number of residential units:		758,160	842,400	1,053,000

Source: Company, Deutsche Bank estimates



We expect the vacancy rate to surge to 9% by 2026, from 3.8% currently

Between 2017 and 2026, we expect total private residential supply of 193,296 units in Hong Kong, but we project corresponding housing demand (net take-up) of merely 99,515. Consequently, the marked supply surplus could lead to a surge in the vacancy rate to 9% by 2026 (from 3.8% now), on our estimates (Figure 39).

Figure 39: Summary of Deutsche Bank's projections on private housing take-up/supply in Hong Kong in 2017-26

Year	Demand projection*	Supply projection	Supply surplus
2017E	10,742	17,515	6,773
2018E	10,828	20,546	9,718
2019E	10,988	21,984	10,996
2020E	10,788	20,207	9,419
2021E	10,819	19,045	8,226
2022E	10,457	20,000	9,543
2023E	9,053	20,000	10,947
2024E	8,954	20,000	11,046
2025E	8,589	17,000	8,411
2026E	8,297	17,000	8,703
TOTAL	99,515	193,296	93,781

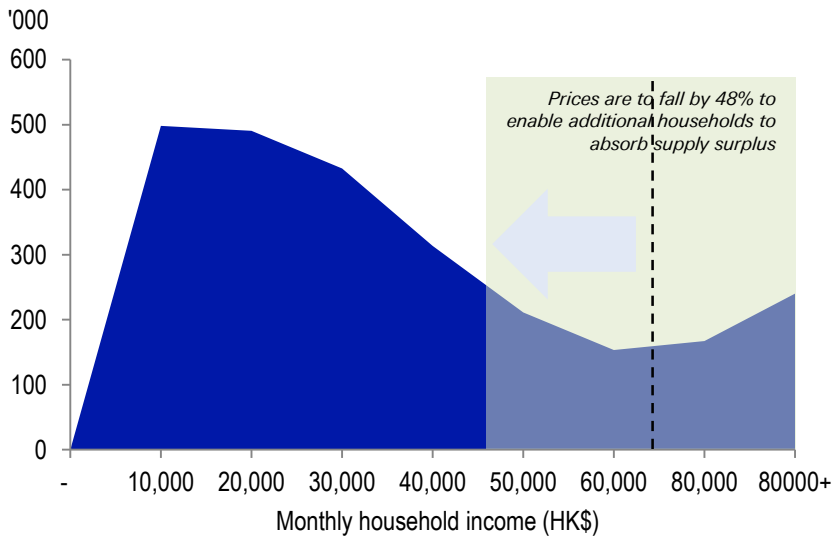
Source: Deutsche Bank estimates * In terms of net take-up

Residential prices to fall by 48% for supply/demand to reach equilibrium

To address the mismatch between supply and demand, we believe private residential prices in Hong Kong would need to decline by 48% in 2017-26 (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026). These price declines increase affordability to a level where surplus supply can be absorbed by the market, such that the overall residential inventory would remain at historical average level of about 8,000 units (Figure 40 and Figure 41). In particular, our approach is to assume that the effective home ownership rate remains unchanged at 71.3% (i.e. adjusted for the households in the public housing, which is non-saleable in nature). Hence, potential buying demand should come from the remaining 28.7% of these qualified households.

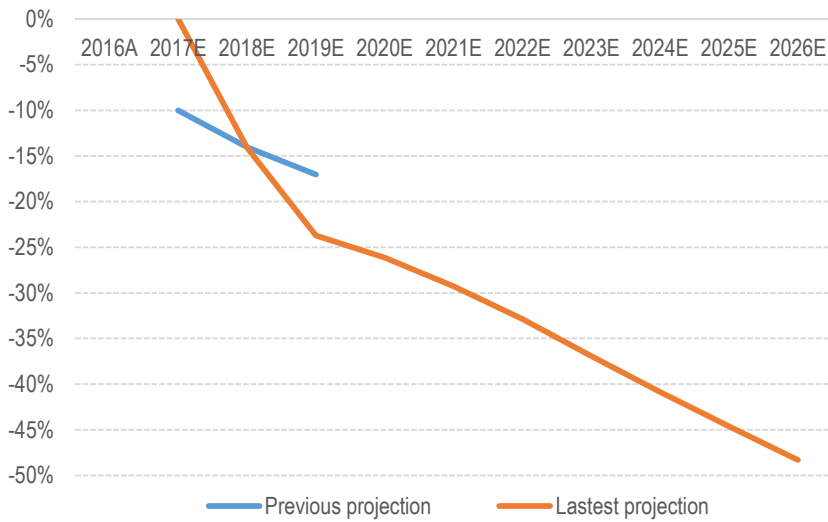


Figure 40: Number of households qualified for purchasing a property, should property prices decline by 48%



Source: Census and Statistics Department, Deutsche Bank

Figure 41: Deutsche Bank's Hong Kong residential property price forecasts



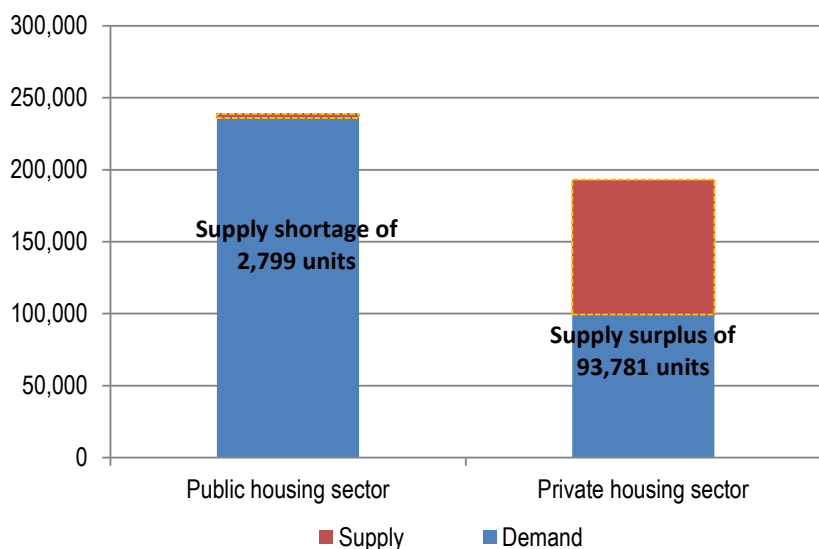
Source: Deutsche Bank estimates



Shortfall of 2,799 public units but surplus of 93,781 private units

In the Long Term Housing Strategy Annual Progress Report 2016, published in December 2016, the government reiterated the split between the public and private sectors at 60:40, or 280,000 units/180,000 units. The report revealed that while land supply for the private housing segment is on track, land plots identified for public housing developments are merely sufficient to provide 236,000 units (44,000 short of the government's long-term supply target). By mapping our housing demand projection with the latest land supply situation revealed by the government, we see that there is a potential shortfall of 2,799 public housing units, while there is a surplus of 93,781 units in the private housing sector (Figure 42).

Figure 42: Supply/demand dynamics for different housing sectors (2017-26)



Source: Deutsche Bank estimates



New valuation approach

We prefer P/E as primary valuation metric over NAV for property development in an ex-growth market

- We believe the conventional valuation methodology of applying an overall target discount on the estimated Net Asset Value (NAV) will become less relevant in valuing developers, as the business model evolves into one focused on asset turnover, rather than on landbank, due to a normalization in land supply ahead. Hence we move to a P/E-based approach for the development businesses.
- Taking into account our negative view on demand and supply fundamentals, we believe applying a 5-7x P/E on 2019E earnings for the development business is appropriate (we believe 2019 is a better reference year to reflect the change in business focus towards asset turnover).
- The average sector P/E implied for the property development business has seen a marked de-rating, from 29x between 1995 and 2010 to just 10x post 2010, as growth profiles have moderated over the period.
- We show new and old earnings estimates and target prices below in Figure 53 and 54. We note that YTD residential prices have been stronger than expected so near-term earnings estimates have been lifted. However, 2019E and beyond earnings have been cut reflecting our more negative outlook for ASPs. Target prices have also been cut in most cases and we downgrade Henderson Land, Kerry and NWD to Hold from Buy, while maintaining a Hold for SHKP and Sino Land.

A new valuation methodology for property development – P/E approach

A discount to Net Asset Value (NAV) based on a Discounted Cash Flow (DCF) has long been adopted as the primary valuation metric for property developers. However, the key drawbacks for this methodology are often the selection of underlying assumptions and target discounts.

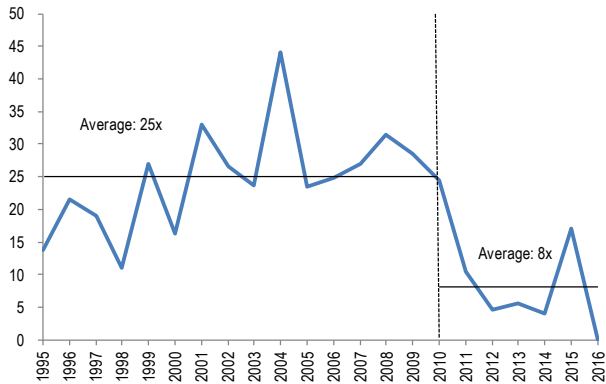
In our view, price-to-earnings multiples (P/Es) may well be a more appropriate primary valuation metric for property development businesses in Hong Kong. As residential land supply normalizes, and given our negative outlook for the physical market, the focus of the developers is likely to be increasingly on asset turnover, instead of landbank accumulation.

Implied P/E on property development trending lower, as growth diminishes

We have looked at the market-implied P/E multiple on property development among Hong Kong developers over the past 25 years, and conclude that this multiple has generally followed a downward trend (Figure 43 to Figure 46). Our approach is to strip out an estimated valuation for investment properties (i.e. assuming the historical average discount of 34% on Deutsche Bank valuations for investment properties), as well as DB valuations for other businesses from the respective group valuation, in order to derive the market-implied valuation for property development in P/Es.

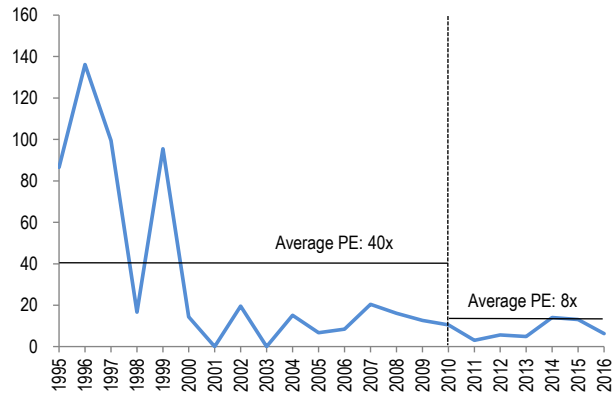


Figure 43: Implied P/E on property development for SHKP



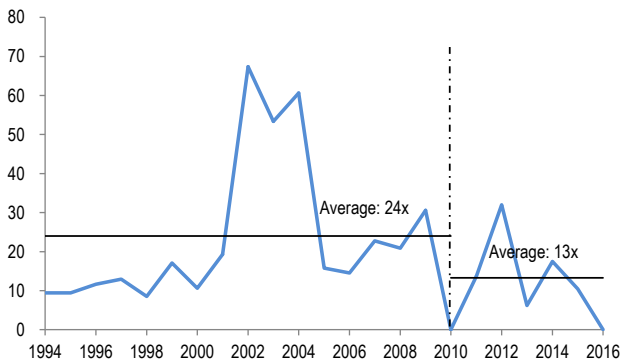
Source: Company; Bloomberg Finance LP; Deutsche Bank

Figure 44: Implied P/E on property development for Sino Land



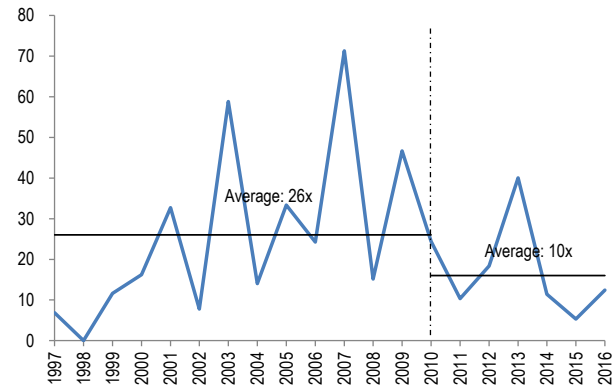
Source: Company; Bloomberg Finance LP; Deutsche Bank

Figure 45: Implied P/E on property development for HLD



Source: Company; Bloomberg Finance LP; Deutsche Bank

Figure 46: Implied P/E on property development for Kerry



Source: Company; Bloomberg Finance LP; Deutsche Bank

The sector market-implied P/E on property development contracted markedly, from an average of 29x prior to 2011 to just 10x since 2011, highlighting that investors have significantly changed their risk appetite towards property development, as growth profiles moderated following the introduction of the first government administrative tightening policy.



Target prices for HK developers to be based on SOTP valuations

Based on our analysis of the demographic trend in Hong Kong, we believe the Hong Kong housing market is heading towards ex-growth, where we will see lower transaction volumes going forward. Moreover, we expect development margins to be under pressure as a result of increasing competition from Mainland developers, who have significantly pushed up land prices in the recent years. We believe this operating environment should structurally lead to lower P/Es.

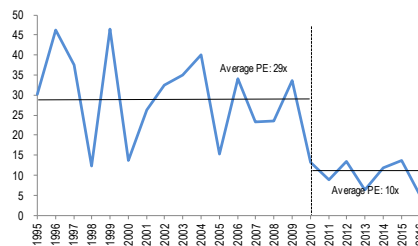
By taking into consideration the likelihood that Hong Kong developers will diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is sum-of-the-parts (SOTP) using target P/E for the property development business.

In selecting appropriate P/Es, we adopt a scorecard approach by considering four key factors – as shown in Figure 48. Specifically, we look at:

1. Development margin trends in the past three financial years and the respective absolute margins
2. Earnings growth in FY19E
3. Net gearing in the last financial year
4. Asset turnover in the past year

We note that we have not included land-bank size as a factor as we believe asset turnover is a better proxy than the absolute land-bank size. In our view, a developer can only realize any upside potential of its land-bank through development and hence this execution capability is better captured through asset turnover.

Figure 47: Implied P/E on property development for Hong Kong developers



Source: Company; Bloomberg Finance LP; Deutsche Bank

Figure 48: Scorecard for target P/E ratios of Hong Kong developers

Company	3-yr avg. development margin (a)	Earnings growth outlook (b)	Net gearing (c)	Asset turnover (d)	Total points	Target P/E for development business
CK Property	5	4	4	5	18	7
SHKP	2	5	3	0	10	6
Henderson	0	1	2	1	4	5
New World	1	3	0	2	6	5
Sino Land	3	0	5	4	12	6
Kerry Properties	4	2	1	3	10	6

Source: Deutsche Bank estimates

Note:
 (a) Development margin highest = 5 pt, lowest= 0 pt
 (b) EPS CAGR highest = 5 pt, lowest= 0 pt
 (c) FY16A net gearing highest = 5 pt, lowest= 0 pt
 (d) Highest asset turnover = 5 pt, lowest= 0 pt

By considering these factors, CK Property has the highest score in our scorecard analysis, followed by Sino Land, SHKP and Kerry.



We also make reference to other markets in exploring a target P/E range that is appropriate for Hong Kong developers. In China, by taking industry leaders such as COLI and CR Land as proxies, there has been a marked de-rating in the past eight years (P/E for COLI de-rated from average of 22x in 2007 to just 7x in 2016), despite the fact that China was in a fast-growing market, where overall primary sales volume registered a CAGR of 8% and companies were generating a much higher Return-on-Equity (ROE). We believe, however, that Hong Kong developers generally have much stronger balance sheets.

In Australia, a developed market, where growth for housing sales has been stagnant in the past 10 years, developers such as Peet, Sunland, CWP and Villa World are trading at about 8-9x forward P/E.

Figure 49: Summary of P/Es for COLI/CR Land

	Primary residential GFA sold YoY (%)	P/E range	
		COLI	CR Land
2007	27%	13 - 31x (22x)	17 - 44x (28x)
2008	-19%	15 - 33x (25x)	16 - 39x (27x)
2009	53%	11 - 23x (18x)	13 - 31x (23x)
2010	9%	11 - 15x (13x)	15 - 20x (17x)
2011	4%	7 - 11x (9x)	8 - 15x (12x)
2012	1%	7 - 12x (9x)	10 - 16x (12x)
2013	18%	7 - 10x (9x)	11 - 14x (13x)
2014	-9%	6 - 9x (8x)	7 - 10x (8x)
2015	7%	7 - 11x (9x)	8 - 13x (10x)
2016	22%	6 - 8x (7x)	7 - 10x (8x)

Source: Bloomberg Finance LP; Deutsche Bank Note: average in brackets

By considering that Hong Kong is approaching an ex-growth market, where overall housing demand is expected to decline (total residential sales volume has declined at a CAGR of 5% in the past 10 years) and profitability is expected to deteriorate ahead, on softening ASPs and higher land prices, we believe a P/E range of 5-7x is appropriate for property development, with the actual multiple depending on the results of our scorecard analysis.

For the China development businesses owned by the HK property companies, we believe applying a 7x P/E (at the upper range of the 2019E P/E for China developers and on a par with industry leaders with strong financial positions, such as COLI and CR Land) is appropriate, considering the financial strength and profitability profiles of Hong Kong developers.

On investment properties, we adopt an income capitalization approach. Our estimated rents and cap rates (4.5-8%) vary across the different types of properties and their locations. We believe applying a 34% target discount to our estimated value on the respective investment property portfolio is appropriate, as the average discount for landlords has been relatively stable, at 34%, in the past 25 years, during which time we have experienced different market cycles.

When arriving at the aggregate SOTP for a company, we take the aggregate estimated value for the above business segments and add the company's net debt positions. We value stakes of listed companies at the prevailing market price.



Figure 50: Summary of valuation metrics

	Past methodology	New methodology
Development properties	Discount Cash Flow	Earnings multiple
Investment properties	Income capitalization	Income capitalization with discount
Other businesses	Market value	Market value
	Gross Asset Value	Gross Asset Value
Plus:	Net debt	Net debt
	Net Asset Value	Aggregate Value
Target price	Apply target discount to NAV	Sum-of-the-parts (SOTP); no discount applied

Source: Deutsche Bank estimates

Figure 51: Valuation breakdown – SHKP, CK Property and New World

Category	SHKP		CK Property		New World	
	Old methodology	New methodology	Old methodology	New methodology	Old methodology	New methodology
	HK\$ per share	HK\$ per share	HK\$ per share	HK\$ per share	HK\$ per share	HK\$ per share
Development properties – Hong Kong	7.88	10.78	5.16	8.06	1.01	1.13
Development properties - China	3.1	2.73	23.85	17.74	3.36	2.5
Investment properties	187.06	123.46*	62.52	41.26*	19.3	12.74*
Other assets	8.68	8.68	5.2	5.43	4.39	4.39
Net cash / (debt)	-27.12	-27.12	-6.43	-6.43	-9.66	-9.66
NAV/aggregate value	179.6	118.5	90.3	66.1	18.4	11.1
Target price	117.0	118.5	72.2	66.1	11.1	11.1
	(35% disc to NAV)		(20% disc to NAV)		(40% disc to NAV)	

Source: Deutsche Bank estimates * After applying a 34% discount

Figure 52: Valuation breakdown – Henderson Land, Sino Land and Kerry Properties

Category	Henderson Land		Sino Land		Kerry Properties	
	Old methodology	New methodology	Old methodology	New methodology	Old methodology	New methodology
	HK\$ per share	HK\$ per share	HK\$ per share	HK\$ per share	HK\$ per share	HK\$ per share
Development properties – Hong Kong	10.5	3.5	1.16	1.64	7.2	6.3
Development properties - China	4.0	0.1	1.06	0.00	12.9	6.4
Investment properties	46.2	30.5*	15.77	10.41*	48.9	32.3*
Other assets	23.4	24.9	0.15	0.15	5.7	5.7
Net cash / (debt)	-9.2	-9.2	2.06	2.06	-21.7	-21.7
NAV/aggregate value	74.9	49.8	20.2	14.3	53.0	29.0
Target price	56.2	49.8	14.4	14.3	29.2	29.0
	(25% disc to NAV)		(30% disc to NAV)		(45% disc to NAV)	

Source: Deutsche Bank estimates * After applying a 34% discount



Figure 53: Summary of earnings revisions (HK\$m)

Developer	FY17E			FY18E			FY19E		
	New	Old	%	New	Old	%	New	Old	%
Cheung Kong Property	18,313	15,677	17%	15,885	15,311	4%	17,235	15,762	9%
Sun Hung Kai Properties	26,789	24,692	8%	25,137	24,858	1%	22,412	24,566	-9%
Sino Land	5,045	5,265	-4%	4,972	4,902	1%	4,504	4,720	-5%
Henderson Land	12,452	10,993	13%	12,195	10,976	11%	10,308	10,500	-2%
New World Development	7,106	6,525	9%	6,943	7,104	-2%	6,175	6,293	-2%
Kerry Properties	4,914	4,553	8%	3,635	3,295	10%	4,993	5,030	-1%

Source: Deutsche Bank estimates

Figure 54: Summary of NAV/TP revisions for HK developers (HK\$) – due to stronger-than expected property market YTD

Developer	Rating	Share price @ 6 June	Implied upside	DP (a)	IP (b)	Others (c)	New TP (a+b+c)	Old TP	%	New NAV	Old NAV	%
Sun Hung Kai Properties	Hold	124.1	-5%	13.51	123.46	-18.43	118.5	117.0	1%	195.6	179.6	8.9%
Sino Land	Hold	14.02	2%	1.77	10.43	2.21	14.3	14.1	1%	22.1	20.2	9.2%
Henderson Land	Hold	52.55	-5%	3.60	30.50	15.70	49.8	56.2	-11%	80.1	74.9	6.9%
New World Development	Hold	10.78	3%	3.63	12.74	-5.33	11.1	11.1	-	20.0	18.4	8.7%
Kerry Properties	Hold	27.4	6%	12.70	32.30	-16.00	29.0	29.2	-1%	61.0	53.0	15.1%

Source: Deutsche Bank estimates

(a): Development properties; (b): Investment properties; (c) Includes other assets and net debt

Figure 55: Hong Kong property – valuation table

Company	Ticker	DB Rating	Trade Ccy	Mkt Cap USDm	3M Daily T/O USDm	6 June 2017 Price	Target Price	Implied Upside	Est. NAV	NAV Disc	P/E (x)			PB(x) 16A	Dividend yield (%)			Net gearing (%)
											17E	18E	19E		16A	16A	17E	
Covered																		
SHKP	16 HK	Hold	HKD	46,107	59.7	124.10	118.50	-5%	195.6	-37%	14.8	14.6	14.5	0.8	3.1	3.1	10.7	
MTRC	66 HK	Hold	HKD	33,403	30.3	44.05	42.70	-3%	56.9	-23%	27.3	27.4	24.2	1.7	7.4	7.4	20.9	
CK Property	1113 HK	Buy	HKD	29,364	48.5	61.30	66.10	8%	103.1	-41%	13.0	15.0	15.3	0.9	2.5	2.6	3.8	
Wharf	4 HK	Hold	HKD	27,809	40.2	71.45	57.10	-20%	103.9	-31%	16.1	16.1	16.6	0.7	3.0	3.1	15.2	
Henderson Land	12 HK	Hold	HKD	24,523	18.4	52.55	49.80	-5%	80.1	-34%	13.5	17.4	17.4	0.7	2.9	3.0	14.3	
Hongkong Land	HKL SP	Sell	USD	18,281	15.9	7.77	6.10	-21%	10.2	-24%	21.6	21.1	21.2	0.6	2.4	2.4	10.6	
Link REIT	823 HK	Sell	HKD	17,504	33.0	61.65	48.60	-21%	58.2	6%	30.3	29.0	28.6	1.1	3.3	3.5	21.1	
New World Dev	17 HK	Hold	HKD	13,558	18.9	10.78	11.10	3%	20.0	-46%	14.3	15.0	13.8	0.6	4.1	4.1	39.7	
Hang Lung	101 HK	Hold	HKD	11,916	13.7	20.65	16.50	-20%	27.4	-25%	14.6	20.1	21.4	0.7	3.6	3.6	5.0	
Sino Land	83 HK	Hold	HKD	11,360	7.2	14.02	14.30	2%	21.7	-35%	16.2	16.4	17.6	0.7	3.6	3.6	Net cash	
Hysan Dev	14 HK	Sell	HKD	5,030	5.5	37.50	32.90	-12%	59.8	-37%	16.6	17.3	18.2	0.6	3.6	3.6	2.4	
Kerry Properties	683 HK	Hold	HKD	5,074	8.6	27.40	29.00	6%	61.0	-55%	10.8	8.7	12.1	0.5	4.0	4.2	30.3	
Average										-29%	17.4	18.2	18.4	0.8	3.6	3.7	14.5	

Source: Deutsche Bank estimates, Company data, Bloomberg Finance LP

The author of this report would like to acknowledge the contribution made by Will Chu.



Appendix: DB's Demographic Study

Notable demographic trends in Hong Kong

Our in-depth review of the demographic outlook for Hong Kong has identified several trends that overall should lead to weaker housing demand. We summarize these trends below.

Figure 56: Deutsche Bank's view on Hong Kong's demographic trends and the impact on housing demand

Trend	Impact on housing demand
Population growth slowing down	<ul style="list-style-type: none"> - HK's population growth is likely to continue to slow. The HK Government expects a mere 0.4% p.a. growth rate through to 2043 and for growth to turn negative from there - Generally, slowing population growth will lead to slowing demand for housing although when other factors (discussed below) are taken into account, the outlook deteriorates further
Aging population	<ul style="list-style-type: none"> - We expect a significant increase in the percentage of the population that is over 60 (to 30% by 2025 from 22% in '15) - As the population ages debt servicing will become more challenging as the average mortgage tenure will decline. This will clearly have a negative impact on housing affordability
Declining working population	<ul style="list-style-type: none"> - The working population in HK is expected to peak next year and to start declining slowly thereafter - A falling working population will clearly have a negative impact on housing affordability
Natural population growth slowing down	<ul style="list-style-type: none"> - Total population can be broken into "natural population" (births less deaths) and "net movements" population - While there was a mini recovery in the natural population in 2006-2012 this was attributable to a surge in births by non-HK residents. Subsequent changes in immigration policies have slowed this considerably and growth is likely to continue to slow to reach zero by 2027 - This trend will weaken housing demand
Net Movements in population	<ul style="list-style-type: none"> - Net population inflows have been a key driver of population growth in recent years and, while this is likely to remain the case, on balance we expect a slowdown in net movements. - This trend will weaken housing demand and in particular will affect demand for high end / large units
Composition of marriages	<ul style="list-style-type: none"> - While the total number of marriages showed significant positive trends from 2002-2012 a closer examination reveals that this was due largely to remarriages which typically do not drive housing demand. - We expect first time marriages (the more important driver of housing demand) to broadly track population growth

Source: Census and Statistics Department; Deutsche Bank



1) Slowing population growth

Population growth in Hong Kong has been slowing down since the mid-90s on the back of a sharp increase in immigration of Hong Kong households to countries such as US, UK, Canada, Australia and New Zealand. Between 1996 and 2015, population growth was 53,260/year (0.9% p.a.). According to the Hong Kong Government's projections, growth will slow down further to a mere 0.4% from 2017-2043. It is expected to peak in 2043 and decline thereafter.

While slowing population growth will generally weaken housing demand, in the following section, we provide more details regarding the expected change in the composition of Hong Kong's population which reinforces our negative view.

2) Aging population

The elderly population (aged above 60) has seen an accelerating trend since 2013. This group made up 21.7% of the total population in 2015 and according to World Bank estimates this proportion is expected to increase to over 26% by 2020 and over 30% by 2025 (Figure 57). Across Asia, Hong Kong now has the second-highest ageing population, as a percentage of total population, behind Japan.

As discussed in Figure 18 and 56 above, an ageing population will result in a lower average mortgage tenure and hence have a negative impact on affordability.

Figure 57: Percentage of population above the age of 60

Year	2005	2010	2015	2020	2025	2030
Japan	26.5%	30.7%	33.1%	34.3%	35.6%	37.3%
UK	21.2%	22.3%	23.0%	24.1%	26.1%	27.8%
Hong Kong	15.4%	18.2%	21.7%	26.1%	30.4%	33.6%
US	16.7%	18.4%	20.7%	23.1%	25.2%	26.1%
Australia	17.5%	19.0%	20.4%	21.9%	23.6%	24.6%
South Korea	13.4%	15.6%	18.5%	22.9%	27.4%	31.4%
Singapore	12.6%	14.1%	17.9%	22.3%	26.8%	30.7%
China	10.8%	12.4%	15.2%	17.5%	20.8%	25.3%

Source: World Bank estimates, Deutsche Bank

Population in age group 25-44 shrinking; pointing to softer housing demand

On the other hand, the population in the age group of 25-44 (the group we believe has the strongest housing demand) already peaked in 2000. Since then, the total population in this age group has continued to shrink and made up just below 30% of the total population in 2015 (Figure 58 and 59).

Figure 58: Percentage of population in age group 25-44

Year	2005	2010	2015	2020	2025	2030
China	34.2%	32.9%	32.2%	30.5%	28.9%	27.1%
South Korea	34.1%	32.6%	30.0%	28.1%	26.8%	24.4%
Hong Kong	33.9%	31.9%	29.7%	28.0%	25.7%	22.7%
Singapore	33.9%	31.8%	29.5%	27.6%	26.1%	24.7%
Australia	29.0%	28.3%	28.5%	27.7%	27.3%	26.0%
UK	28.7%	27.3%	26.4%	26.1%	25.7%	24.6%
US	28.3%	26.8%	26.3%	26.5%	26.4%	25.9%
Japan	27.5%	26.8%	25.5%	23.0%	21.6%	20.6%

Source: World Bank estimates, Deutsche Bank



We note that the median age in Hong Kong rose to 43.6 in 2016 (from 39.6 in 2006) and is much higher than Singapore (at 34.0), the UK (at 40.4) and the US (at 37.8) but still lower than Japan (46.5).

Figure 59: Total population in the age group 25-44 ('000)

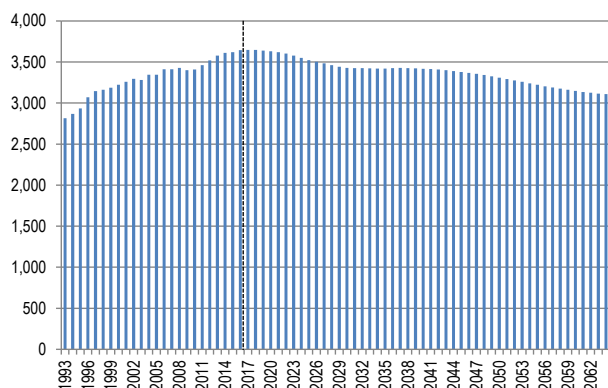
Year	2005	2010	2015	2020	2025	2030
China	445,224	439,704	441,217	425,546	407,161	381,529
South Korea	16,402	16,096	15,161	14,499	13,986	12,850
Hong Kong	2,310	2,244	2,170	2,115	2,002	1,803
Singapore	1,447	1,616	1,633	1,629	1,591	1,549
Japan	35,197	34,345	32,433	28,798	26,476	24,706

Source: World Bank estimates, Deutsche Bank

3) Working population expected to peak out next year

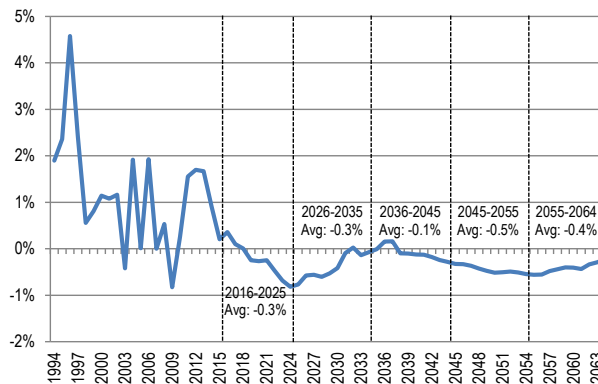
In tandem with the ageing population in Hong Kong, the working population grew at much slower pace in the past decade (0.8% p.a. vs 1.3% p.a. in the prior decade). The HKSAR government projects the working population to peak out in 2018 at 3,648,000 (implying that we are currently just about 4,000 away from the peak) and over the period 2016-25, the government expects 0.3% contraction p.a. (Figure 61).

Figure 60: Government projection on working population ('000)



Source: Census & Statistics Dept, Deutsche Bank

Figure 61: Government projection on working population growth



Source: Census & Statistics Dept, Deutsche Bank

4) Natural population growth

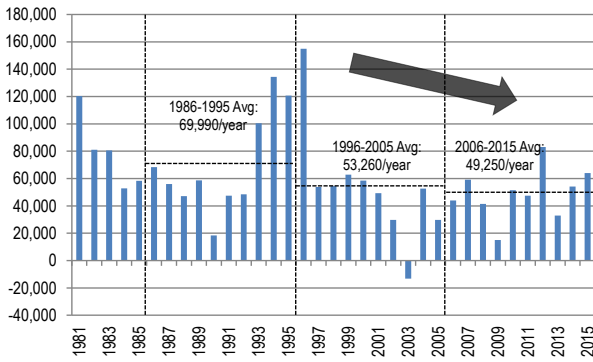
Total population growth can be broken down into the natural population growth and then net movements in population.

The natural increase in population (i.e. births minus deaths) has generally been on a declining trend in recent decades. True, we did see a slight recovery from 2006 to 2013, but this was merely driven by a surge in births among non-Hong Kong permanent residents, which made up 40% of new births in Hong Kong in the 2011 peak. Following the government's tightening up of relevant immigration policies in 2012, which effectively halted non-Hong Kong permanent residents giving birth in Hong Kong, the natural increase in population normalized.



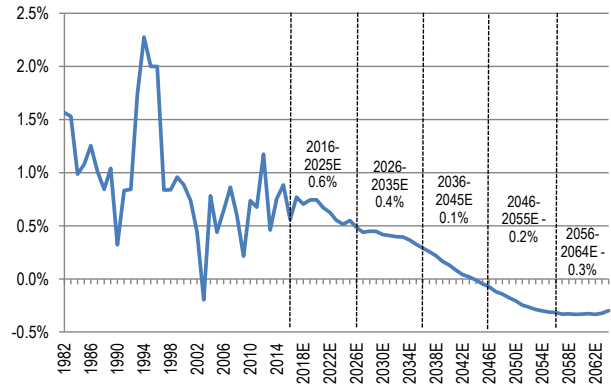
Hong Kong Government projections call for zero growth in the natural population by 2027, where deaths are expected to surpass new births for the first time.

Figure 62: Net increase in population in Hong Kong



Source: Census & Statistics Dept; Deutsche Bank

Figure 63: Population growth projection by government

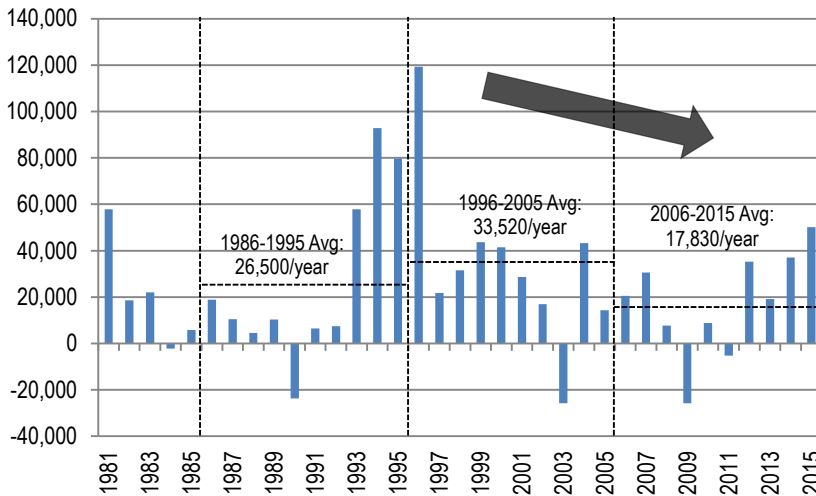


Source: Census & Statistics Dept; Deutsche Bank

5) Net movements in population

Population growth in Hong Kong has predominantly been driven by net movements in recent years although this too has been slowing down. The average net movement in the past 10 years (2006-15) at 17,830/year is significantly lower than the previous decade at 33,520/year.

Figure 64: Net movements in population



Source: Census & Statistics Dept; Deutsche Bank



Net movements in population can be broken into the following key components which we discuss in more detail below.

- i. One-way permit holders
- ii. Mainland students
- iii. Mainland expatriates
- iv. Other expatriates

i. One-way permit holders

One-way permit holders have been the main contributors to HK's population growth in recent years, making up more than 70% of the gross population inflow in 2015, according to Census & Statistics Department. However, the total number of approvals for One-way permits actually fell to the lowest in history at 37,785 in 2015 or just 104 per day, utilizing just 70% of the daily quota of 150. Indeed, the quota utilization has been on a downward trend since the 1997 handover (where numbers were strong for the first few years at about 55,000/year).

While we expect the number of One-way permit holders to pick up in coming years due to a slowing Chinese economy and continue to be the key population driver ahead, this is not likely to translate directly into new housing demand as the majority of these permit holders trend to come to Hong Kong to stay with their families. According to statistics conducted by the Home Affairs Department in 2016, 86% of One-way permit holders lived with family members. In addition, the median monthly income for these permit holders was relatively low at HK\$10,800.

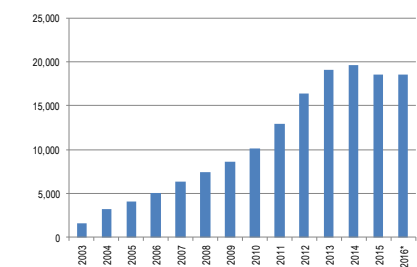
ii. Mainland students under the Entry for Study Scheme

Beginning in the 1999-2000 academic year, Mainland students have been allowed to pursue full-time undergraduate study programmes in Hong Kong under the Entry for Study Scheme. Since then, there has been an influx of students to Hong Kong (Figure 65) and the maximum aggregate quota for non-local students was already reached at 12% of total student population.

In our view, Hong Kong used to be an attractive destination for tertiary education for Mainland students as a result of the cheaper cost compared with other popular destinations for education. However, following a change in curriculum for the undergraduate programme since the academic year of 2012/13 (from a three-year programme to a four-year programme) and unfavourable currency movements in the past two years (i.e. currency in other popular destinations such as Australia and the UK fell significantly against the Rmb), we have seen a flattening out in the number of Mainland students studying in Hong Kong. We do not expect a pick up from current levels over the longer term.

In any case, we do not view Mainland students as a key driver of housing demand in Hong Kong as the majority of the Mainland students will stay in the student accommodation attached to the universities. There are a total of 33,386 student accommodation spaces provided by the eight tertiary education institutions in Hong Kong as of 2016, more than adequate to accommodate the 11,895 Mainland students in the respective period (Figure 66).

Figure 65: Mainland students studying in Hong Kong



Source: Immigration Dept, Deutsche Bank * As of Nov-16



Figure 66: Breakdown of student accommodation spaces by institution*

Institution	Number of spaces
Hong Kong University of Science and Technology	4,032
City University of Hong Kong	8,000
University of Hong Kong	6,500
City University of Hong Kong	3,700
Hong Kong Polytechnic University	4,654
Hong Kong Baptist University	1,700
Lingnan University	2,600
Education University of Hong Kong	2,200
Total	33,386

Source: University websites; Deutsche Bank *As of 2016

Figure 67: Breakdown of Mainland students by educational institution

Institution	2011/12	2012/13	2013/14	2014/15	2015/16
City University of Hong Kong	1,120	1,318	1,294	1,355	1,416
Hong Kong Baptist University	601	799	852	867	894
Lingnan University	195	187	180	173	189
Chinese University of Hong Kong	2,029	2,538	2,636	2,772	2,877
Education University of Hong Kong	239	246	259	274	312
Hong Kong Polytechnic University	1,191	1,466	1,552	1,597	1,647
Hong Kong University of Science and Technology	1,376	1,628	1,738	1,696	1,690
University of Hong Kong	2,185	2,781	2,863	2,876	2,870
Total	8,936	10,963	11,374	11,610	11,895
Total students	75,597	93,394	94,635	96,911	99,257
% of Mainland students	11.8%	11.7%	12.0%	12.0%	12.0%

Source: University Grants Committee; Deutsche Bank

* The statistics are for the academic years by University Grants Committee funded programmes only. Headcounts refer to simple count without specifying study mode (part-time/full-time)

Figure 68: Comparison of tuition fees/other costs among popular education destinations

Items	Hong Kong (HK\$)	Australia (AU\$)	USA (US\$)	UK (GBP)
Tuition fee (per annum)	120,000	24,500	33,480	12,000
Accommodation	13,500	18,610	11,890	12,000
Living expenses (meals, transportation and misc)	27,000		3,950	
Total cost per annum (local currency)	160,500	43,110	49,320	24,000
Total cost per annum (HK\$ equivalent)	160,500	245,727	384,696	240,000
Length of undergraduate programme	4	3	4	3
Total cost of an undergraduate programme (HK\$ equivalent) – before curriculum change	481,500	737,181	1,538,784	720,000
Total cost of an undergraduate programme (HK\$ equivalent) – after curriculum change	642,000	737,181	1,538,784	720,000

Source: Deutsche Bank estimates



iii. Mainland expatriates

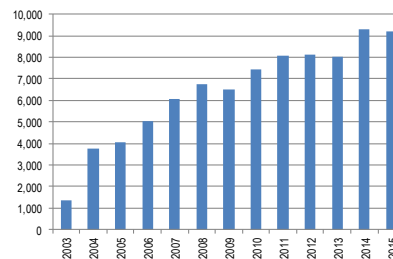
The flow of Mainland expatriates into Hong Kong started to pick up sharply in 2003 and this has been a significant driver of housing demand. In large part, this was supported by programs such the Admission Scheme for Mainland Talents and Professionals (ASMTF) which were designed to attract talent into Hong Kong.

However, we have seen recent slowdown in the numbers of Mainland Chinese entering Hong Kong through this program (Figure 69) and we expect further slowdown in light of increasing competition for talent from the Mainland from nearby areas such as Shenzhen Qianhai Financial District.

iv. Foreign expatriates

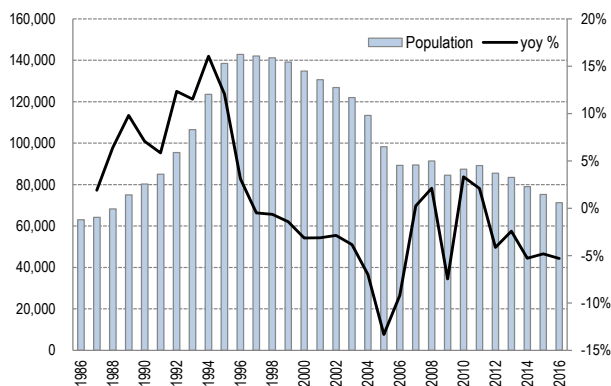
Foreign expatriates (i.e. expatriates from the US, the UK, Australia, Canada, Singapore and Japan) used to be a key population driver in Hong Kong till the mid-1990s. However, the foreign expatriate population peaked in 1996 at 142,800 and as of mid-2016, it was down to 71,251 (implying a 50% decline from the peak).

Figure 69: Total Mainland expatriates under Admission Scheme for Mainland Talents & Professionals



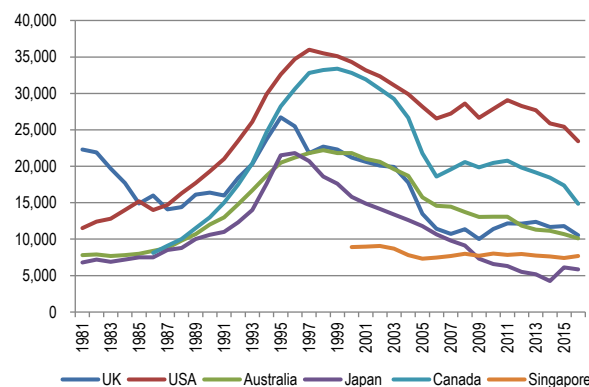
Source: Immigration Dept; Deutsche Bank

Figure 70: Foreign expatriate population in Hong Kong*



Source: Immigration Department; Deutsche Bank
 Note: foreign expatriates refer to persons of nationalities of the UK, the US, Australia, Japan, Canada and Singapore * Numbers exclude foreign domestic workers

Figure 71: Foreign expatriate population breakdown



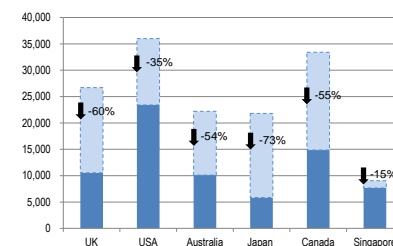
Source: Immigration Department; Deutsche Bank

We expect further declines in the expatriate population driven by concerns regarding the environment, access to international schools and a very high cost of living. For example, a recent Bloomberg report quotes Economist Intelligence Unit listing Hong Kong as one of the most expensive cities in Asia for expatriates.

The decline in housing prices we project in this report may ultimately be a positive factor and encourage some expatriates back to Hong Kong.

We note that a decline in the expatriate population will generally have a negative impact on demand for larger units (a significant portion of the current expatriate community are senior executives working for global organizations). Indeed, vacancy rates for large units have consistently being markedly higher than the overall vacancy rate at 8-11% in the past 5 years (versus overall vacancy rates of about 4%), according to statistics compiled by the Rating & Valuation Department, which is consistent with the decline in foreign expatriate population in Hong Kong.

Figure 72: Changes in foreign expatriate population (peak versus current)



Source: Immigration Department; Deutsche Bank

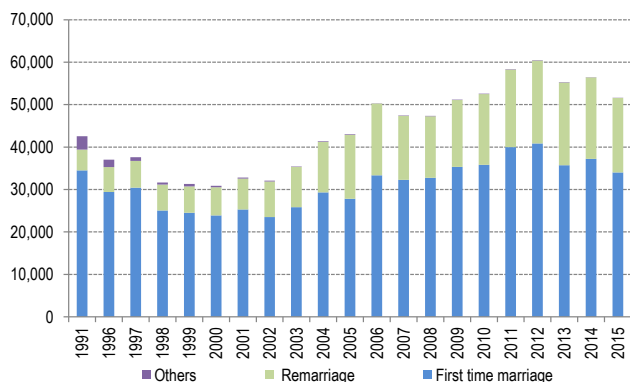


6) Recovery in number of marriages mostly driven by a surge in remarriages

The total number of marriages saw a recovery trend post 2000 and hit a 30-year high in 2012 before a pull-back in 2015.

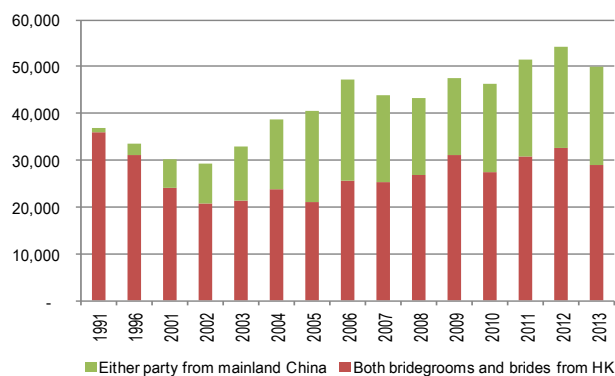
At first glance, the strong recovery in the total number of marriages would seem odd as it goes against the softening demographic trend in Hong Kong. However, on closer examination, the surge in total marriages was driven by remarriages. For example, remarriages made up more than one-third of all marriages in Hong Kong in 2015. By stripping out the remarriages, the number of first marriages indeed stayed at similar levels as the 1990s.

Figure 73: Total number of marriages in HK



Source: Census & Statistics Department; Deutsche Bank

Figure 74: Breakdown of bride/bridegrooms by origin



Source: Census & Statistics Department; Deutsche Bank

Another notable marriage trend in Hong Kong is the growing number of intermarriages between Hong Kong permanent residents and Mainlanders. In 2013, marriages with either the bride/bridegroom from the Mainland accounted for about 38% of the total number of marriages.

We believe remarriages and intermarriages between Hong Kong permanent residents and Mainlanders do not lead to the same housing demand as first marriages by Hong Kong permanent residents.

Based on the government's projection for a shrinking number of people in the 25-34 age group we believe there will be a corresponding decline in the number of first-time marriages by Hong Kong permanent residents which will affect household formation. Projections for new household formation in Hong Kong are shown in Figure 33 where the number of first-time marriages is down 18% by 2023.

Figure 75: Population growth in Hong Kong breakdown by category

Mid-year	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
<i>In Thousands</i>																				
Population of previous year	6,435.5	6,489.3	6,543.7	6,606.5	6,665.0	6,714.3	6,744.1	6,730.8	6,783.5	6,813.2	6,857.1	6,916.3	6,957.8	6,972.8	7,024.2	7,071.6	7,154.6	7,187.5	7,241.7	7,305.7
NATURAL INCREASE																				
Births	63.5	55.2	52.1	51.1	53.1	47.1	48.6	46.1	54.1	60.3	67.4	75.0	81.3	84.7	95.5	91.6	57.1	62.3	59.9	59.8
Adjustment: live births born in HK by non-Hong Kong permanent residents					-7.1	-7.5	-8.7	-10.7	-14.6	-18.0	-18.2	-21.2	-22.8	-24.4	-26.1	-19.6	-4.8	-5.3	-4.9	-5.0
<i>Adjusted births</i>	<i>63.5</i>	<i>55.2</i>	<i>52.1</i>	<i>51.1</i>	<i>46.0</i>	<i>39.6</i>	<i>39.9</i>	<i>35.4</i>	<i>39.5</i>	<i>42.3</i>	<i>49.2</i>	<i>53.8</i>	<i>58.5</i>	<i>60.3</i>	<i>69.4</i>	<i>72.0</i>	<i>52.3</i>	<i>57.0</i>	<i>55.0</i>	<i>54.8</i>
Deaths	31.5	32.3	33.0	34.1	32.5	34.3	36.1	36.6	38.7	36.9	38.8	41.2	40.5	42.1	42.3	43.9	43.4	45.1	46.1	46.6
<i>Adjusted natural increase</i>	<i>32.0</i>	<i>22.9</i>	<i>19.1</i>	<i>17.0</i>	<i>13.5</i>	<i>5.3</i>	<i>3.8</i>	<i>-1.2</i>	<i>0.8</i>	<i>5.4</i>	<i>10.4</i>	<i>12.6</i>	<i>18.0</i>	<i>18.2</i>	<i>27.1</i>	<i>28.1</i>	<i>8.9</i>	<i>11.9</i>	<i>8.9</i>	<i>8.2</i>
INFLOW																				
Inflow of One-way Permit Holders	55.7	53.2	55.3	56.1	60.8	56.8	50.3	41.5	38.8	59.6	44.7	39.1	41.4	48.8	41.1	52.1	47.9	43.5	37.8	46.7
Mainland expatriates via ASMTP	-	-	-	-	-	-	1.4	2.4	0.3	1.0	1.0	0.7	-0.2	0.9	0.6	0.0	-0.1	1.3	-0.1	0.4
PRC dependants#	-	-	-	-	-	-	0.7	1.2	0.1	0.5	0.5	0.3	-0.1	0.5	0.3	0.0	0.0	0.6	0.0	0.2
Net movement of non-PRC expats and foreign domestic workers	22.3	25.3	9.4	18.0	13.3	3.4	-6.0	0.3	-6.6	-0.3	17.1	16.9	2.2	21.3	22.2	6.2	10.2	3.0	31.6	-0.6
Inflow of Mainland students via Entry for Study scheme	-	-	-	-	-	-	-	1.7	0.9	0.9	1.3	1.1	1.2	1.5	2.8	3.5	2.7	0.5	-1.1	0.0
<i>Sub-total</i>	<i>78.0</i>	<i>78.5</i>	<i>64.7</i>	<i>74.1</i>	<i>74.1</i>	<i>60.2</i>	<i>46.3</i>	<i>47.1</i>	<i>33.4</i>	<i>61.7</i>	<i>64.7</i>	<i>58.2</i>	<i>44.4</i>	<i>73.0</i>	<i>67.1</i>	<i>61.8</i>	<i>60.6</i>	<i>49.0</i>	<i>68.1</i>	<i>46.7</i>
OUTFLOW																				
HK emigrants	-30.9	-19.3	-12.9	-11.9	-10.6	-10.5	-9.6	-9.8	-9.8	-10.3	-9.9	-9.1	-7.2	-7.2	-8.3	-7.6	-7.6	-6.9	-7.0	-7.0
Other net movement*	-25.1	-27.6	-8.1	-20.6	-27.7	-25.1	-53.9	16.6	5.2	-12.9	-5.9	-20.2	-40.2	-32.6	-37.8	-1.7	-48.7	4.2	-6.0	-6.9
<i>Sub-total</i>	<i>-56.0</i>	<i>-46.9</i>	<i>-21.0</i>	<i>-32.5</i>	<i>-38.3</i>	<i>-35.6</i>	<i>-63.5</i>	<i>6.8</i>	<i>-4.6</i>	<i>-23.2</i>	<i>-15.8</i>	<i>-29.3</i>	<i>-47.4</i>	<i>-39.8</i>	<i>-46.1</i>	<i>-9.3</i>	<i>-56.3</i>	<i>-2.7</i>	<i>-13.0</i>	<i>-13.9</i>
Adjusted net movement	22.0	31.6	43.7	41.6	35.8	24.5	-17.1	53.9	28.9	38.5	48.8	28.9	-3.0	33.2	20.9	52.5	4.3	46.2	55.1	32.8
Net population change	53.8	54.4	62.8	58.5	49.3	29.8	-13.3	52.7	29.7	43.9	59.2	41.5	15.0	51.4	48.0	80.6	13.2	58.1	64.0	41.0
Ending population	6,489.3	6,543.7	6,606.5	6,665.0	6,714.3	6,744.1	6,730.8	6,783.5	6,813.2	6,857.1	6,916.3	6,957.8	6,972.8	7,024.2	7,071.6	7,154.6	7,187.5	7,241.7	7,305.7	7,346.7

Source: Census & Statistics Department; Immigration Department; Deutsche Bank

* Other net movement refers mostly to adjustment between mid-year/year-end statistics as provided by Immigration Department/Census & Statistics Department and departure of One-way Permit Holders





Risks

Key downside risks

- Government tightening measures might be stricter than we expect;
- Unexpected economic fluctuations in the Chinese economy;
- Weaker-than-expected volume recovery;
- Weaker-than-expected domestic consumption growth.

Key upside risks

- Policy loosening, leading to strong market recovery;
- Significant improvement in credit environment.

HLD (0012.HK)

Valuation

Our target price is based on the sum-of-the-parts approach (previously target discount on overall NAV), which implies a 2017 PE of 15x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio are appropriate in an ex-growth market. For China property development, we believe applying a 7x PE (at the upper range of 2018E PE for China developers and at par with industry leaders with strong financial positions such as COLI and CR Land) is appropriate considering the financial strength and profitability profile of Hong Kong developers. This is our new valuation metric adopted for all HK developers under our coverage.

Risks

Macro risks: 1) external shock and interest rate hike; 2) government tightening measures might be stricter than expected; 3) unexpected economic fluctuations in the Chinese economy.

Company-specific risks: 1) plan execution track record in China is not fully proven; 2) HLD could face stronger-than-expected competition for land bank.

Kerry Properties (0683.HK)

Valuation

Our target price is based on the sum-of-the-parts approach (previously target discount on overall NAV), which implies a 2017 PE of 9x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio are appropriate in an ex-growth market. For China property development, we believe applying a 7x PE (at the upper range of 2018E PE for China developers and at par with industry leaders with strong financial positions such as COLI and CR Land) is appropriate considering the financial strength and profitability profile of Hong Kong developers. This is our new valuation metric adopted for all HK developers under our coverage.



Risks

Key downside risks:

- Fluctuation in the Hong Kong/China economy could lead to lower/higher housing demand.
- An interest rate hike and continuous liquidity outflow could severely hurt sentiment and demand in the property market in Hong Kong.
- Unexpected fluctuations in the Chinese economy could affect our forecasts.
- If the actual rental/price declines are more severe than our current projection, there could be a downside to our current forecast and projected dividend payout and vice versa.

Key upside risk:

- Property market may further strengthen if the low interest rate environment persists.

New World Development (00017.HK)

Valuation

Our target price is based on the sum-of-the-part approach (previously target discount on overall NAV), which imply a 2017 PE of 14x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio is appropriate in an ex-growth market. For China property development, we believe applying 7x PE (at the upper range of 2019E PE for China developers and on par to industry leaders with strong financial positions such as COLI and CR Land) is appropriate by considering the financial strength and profitability profile of Hong Kong developers. Such methodology is now our new valuation metric adopted across HK developers under our coverage.

Risks

- 1) A softening/stronger outlook in the Hong Kong economy, which could lead to lower/stronger housing demand.
- 2) A low interest rate environment and ample liquidity flow could reverse, damaging sentiment and demand in the property market. However, if the low interest rate environment persists for longer, current high property prices may well be supported.
- 3) A further slowdown in the Chinese economy could result in a downside to our current forecasts. However, if we see stronger than expected economic growth, there could be upside to our current forecasts.
- 4) NWD could face severe competition for landbank, which would adversely affect the growth prospects of the company. However, if competition is less intensified, NWD could be able to acquire land at more reasonable costs, leading to stronger NAV growth.



Rating
Buy

Asia
Hong Kong

Property
Property

Company
CK Property

Reuters
1113.HK

Bloomberg
1113.HK

Price at 6 Jun 2017 (HKD)	61.30
Price target - 12mth (HKD)	66.10
52-week range (HKD)	61.30 - 46.00
HANG SENG INDEX	25,997

Jason Ching, CFA

Research Analyst
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Highest asset turnover should bring longer term outperformance

Highest asset turnover among peers should bring longer term outperformance

We reiterate our Buy rating on CK Property with a revised target price of HK\$66.1 (HK\$72.2) based on a new valuation methodology which we believe to be more appropriate in an ex-growth market on an aging population. In our view, the ramp up in the government's land development program that started in 2013 should lead to better equilibrium in the supply-demand dynamics going forward. In such an environment, we believe a high asset turnover is the best strategy in an inventory accumulation cycle. We therefore believe CKP could outperform its peers longer term, as it has the smallest landbank relative to operating scale and the highest asset turnover.

New valuation approach – we prefer PE to value property development

We believe the conventional valuation methodology of applying an overall target discount on the accessed NAV is becoming less relevant in valuing developers as market fundamentals have changed, and the historical average may not necessarily serve as a good reference. By taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is SOTP, where we adopt PE for the property development business and the income capitalization approach for investment properties.

FY17-19E earnings revised by 4-17% factoring in our latest ASP assumptions

Due to worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with rising supply, which would inevitably more than double the vacancy rate to 9% (from 3.8% now) and cause prices to slide 48% in 2017-26E (0% in 2017E, -14% in 2018E, -11% in 2019E, -3% in 2020E, -4% in 2021E, -5% in 2022E, -6% in 2023E, -6% in 2024/25E and -7% in 2026E). We therefore revise our earnings estimates by 4% to 17% in FY17-19 and increase the NAV by 14.2%.

Target price of HK\$66.1 is based on the sum-of-the parts approach

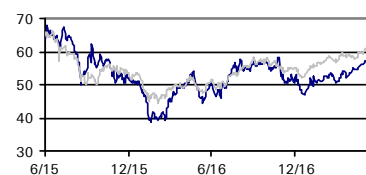
Our target price is based on the sum-of-the-parts approach (previously target discount on overall NAV), and implies a 2017E PE of 14x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolios is appropriate in an ex-growth market. This is the new valuation metric we adopt for all HK developers under our coverage. Risks: government policy, sales momentum and potential interest rate hikes.

Key changes

Price target	72.20 to 66.10	↓	-8.4%
Sales (FYE)	73,568 to 74,384	↑	1.1%
Op prof margin(FYE)	29.4 to 34.1	↑	16.0%
Net profit(FYE)	15,676.8 to 18,312.7	↑	16.8%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	9.1	20.1	22.0
HANG SENG INDEX	6.2	10.2	23.6

Source: Deutsche Bank

Forecasts And Ratios

Year End Dec 31	2015A	2016A	2017E	2018E	2019E
Sales (HKDm)	57,860.0	70,020.0	74,383.5	74,179.5	89,084.7
EBITDA(HKDm)	22,118.0	27,199.0	26,200.3	22,171.8	23,167.1
Reported NPAT(HKDm)	17,113.0	19,415.0	18,312.7	15,885.0	17,234.6
DB EPS FD (HKD)	4.03	4.72	4.85	4.21	4.56
PER (x)	14.4	10.6	12.6	14.6	13.4
DPS (net) (HKD)	1.40	1.53	1.57	1.60	1.65
Yield (net) (%)	2.4	3.0	2.6	2.6	2.7

Source: Deutsche Bank estimates, company data



Model updated: 23 May 2017

Running the numbers

Asia

Hong Kong

Property

CK Property

Reuters: 1113.HK

Bloomberg: 1113.HK

Buy

Price (6 Jun 17) HKD 61.30

Target Price HKD 66.10

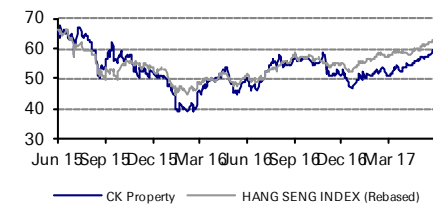
52 Week range HKD 46.00 - 61.30

Market Cap (m) HKDm 234,411
USDm 30,074

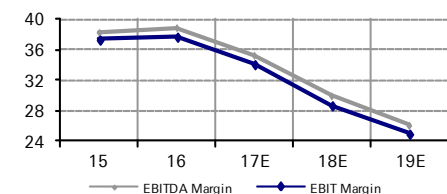
Company Profile

As a fully-integrated, multi-discipline property developer, the Group is one of the largest developers of residential, office, retail, industrial, and hotel property in Hong Kong. With its long history of property development expertise, the Group has built many of Hong Kong's most notable landmark buildings and complexes.

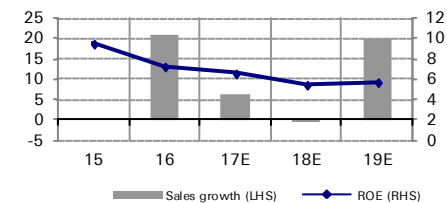
Price Performance



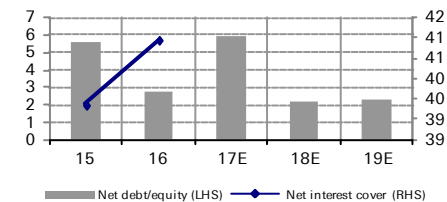
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 31-Dec

2015 2016 2017E 2018E 2019E

Financial Summary

DB EPS (HKD)	4.03	4.72	4.85	4.21	4.56
Reported EPS (HKD)	4.43	5.08	4.85	4.21	4.56
DPS (HKD)	1.40	1.53	1.57	1.60	1.65
BVPS (HKD)	68.2	70.7	75.3	77.9	80.8
Weighted average shares (m)	3,860	3,847	3,824	3,776	3,776
Average market cap (HKDm)	223,737	193,182	234,411	234,411	234,411
Enterprise value (HKDm)	233,320	191,592	244,619	234,630	236,329

Valuation Metrics

P/E (DB) (x)	14.4	10.6	12.6	14.6	13.4
P/E (Reported) (x)	13.1	9.9	12.6	14.6	13.4
P/BV (x)	0.74	0.67	0.81	0.79	0.76
FCF Yield (%)	7.8	3.0	3.7	6.8	6.6
Dividend Yield (%)	2.4	3.0	2.6	2.6	2.7
EV/Sales (x)	4.0	2.7	3.3	3.2	2.7
EV/EBITDA (x)	10.5	7.0	9.3	10.6	10.2
EV/EBIT (x)	10.8	7.3	9.6	11.0	10.6

Income Statement (HKDm)

Sales revenue	57,860	70,020	74,384	74,180	89,085
Gross profit	25,273	31,719	31,089	27,318	28,861
EBITDA	22,118	27,199	26,200	22,172	23,167
Depreciation	508	779	818	859	902
Amortisation	0	0	0	0	0
EBIT	21,610	26,420	25,382	21,313	22,265
Net interest income/(expense)	-549	-645	497	637	700
Associates/affiliates	378	137	887	887	887
Exceptionals/extraordinary	2,774	1,262	0	0	0
Other pre-tax income/(expense)	0	0	0	0	0
Profit before tax	24,213	27,174	26,767	22,837	23,852
Income tax expense	6,305	7,365	5,789	5,403	4,901
Minorities	795	394	2,666	1,549	1,716
Other post-tax income/(expense)	0	0	0	0	0
Net profit	17,113	19,415	18,313	15,885	17,235
DB adjustments (including dilution)	-1,545	-1,383	0	0	0
DB Net profit	15,568	18,032	18,313	15,885	17,235

Cash Flow (HKDm)

Cash flow from operations	17,918	5,881	8,577	15,777	15,325
Net Capex	-483	0	0	0	0
Free cash flow	17,435	5,881	8,577	15,777	15,325
Equity raised/(bought back)	0	0	0	0	0
Dividends paid	-33,266	0	0	0	0
Net inc/(dec) in borrowings	60,389	9,187	12,786	5,260	-7,152
Other investing/financing cash flows	-9,229	-291	-2,270	-6,496	-6,496
Net cash flow	35,329	14,777	19,093	14,541	1,676
Change in working capital	6,787	-11,525	-17,108	-200	-4,578

Balance Sheet (HKDm)

Cash and other liquid assets	45,861	62,601	65,546	81,633	73,789
Tangible fixed assets	0	0	0	0	0
Goodwill/intangible assets	0	0	0	0	0
Associates/investments	12,136	15,240	15,950	16,660	17,369
Other assets	313,808	318,995	337,376	342,861	352,680
Total assets	371,805	396,836	418,872	441,154	443,839
Interest bearing debt	60,989	70,176	82,962	88,222	81,070
Other liabilities	41,129	50,386	42,778	48,409	45,526
Total liabilities	102,118	120,562	125,741	136,631	126,596
Shareholders' equity	263,096	270,199	284,391	294,233	305,237
Minorities	6,591	6,075	8,741	10,290	12,006
Total shareholders' equity	269,687	276,274	293,131	304,523	317,243
Net debt	15,128	7,575	17,416	6,589	7,281

Key Company Metrics

Sales growth (%)	nm	21.0	6.2	-0.3	20.1
DB EPS growth (%)	na	16.9	2.8	-13.3	8.5
EBITDA Margin (%)	38.2	38.8	35.2	29.9	26.0
EBIT Margin (%)	37.3	37.7	34.1	28.7	25.0
Payout ratio (%)	31.6	30.3	32.8	38.0	36.2
ROE (%)	9.5	7.3	6.6	5.5	5.7
Capex/sales (%)	0.8	0.0	0.0	0.0	0.0
Capex/depreciation (x)	1.0	0.0	0.0	0.0	0.0
Net debt/equity (%)	5.6	2.7	5.9	2.2	2.3
Net interest cover (x)	39.4	41.0	nm	nm	nm

Source: Company data, Deutsche Bank estimates

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Investment Thesis

Outlook

The government's acceleration of the land development program that started in 2013 should in our view lead to better equilibrium in the supply/demand dynamics going forward. In such an environment, we believe high asset turnover is the best strategy in an inventory accumulation cycle. This should lead to CKP out performing longer term, as amongst peers it has the smallest land bank relative to operating scale, and consistently the highest asset turnover. We expect the company's higher recurring income base going forward (harvesting from aircraft leasing and acquisition of DUET) to give scope for a dividend hike. Moreover, with a strong cash position (HK\$62.6bn as of end-16), we see potential for share buyback. Indeed, CK Property is one of the most aggressive HK property companies buying back its shares in the past 12 months. Buy.

Valuation

Our target price is based on the sum-of-the-parts approach (previously target discount on overall NAV), and implies a 2017E PE of 14x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolios is appropriate in an ex-growth market. For China property development, we believe applying a 7x PE (at the upper range of 2019E PE for China developers and at par with industry leaders with strong financial positions such as COLI, HKD24.00 and CR Land, HKD23.20) is appropriate considering the financial strength and profitability profile of Hong Kong developers. This is the new valuation metric adopted for all HK developers under our coverage.

Risks

- 1) Government policies: Introduction of any additional policies by the Hong Kong/Chinese governments could have an adverse impact on CK Property's sales performance, earnings and profitability.
- 2) External shocks/interest rate hikes: In our view, potential external shocks/interest rate hikes would likely result in a turnaround in market sentiment and weaker housing demand which could trigger a significant correction in CK Property's key markets.



Financial Analysis

FY17-19E earnings revised by 4-17% factoring in our latest ASP assumptions

As a result of worsening demographic trends, we expect HK to see a slide in housing demand, coupled with rising supply, which would inevitably more than double the vacancy rate to to 9% (from 3.8% now) and cause prices to slide 48% in 2017-26E (0% in 2017E, -14% in 2018E, -11% in 2019E, -3% in 2020E, -4% in 2021E, -5% in 2022E, -6% in 2023E, -6% in 2024/25E and -7% in 2026E). Previously we had assumed a 21% dip in ASP in 2017-19 (-11% in 2017E, -7% in 2018E and -5% in 2019E). We therefore revise our earnings estimates by 4-17% in FY17-19. Specifically, we have revised our earnings estimates by 17% to HK\$18,313m for FY17E, 4% to HK\$15,885m for FY18E and 9% to HK\$17,235m for FY19E. We also now expect a higher absolute dividend per share of HK\$1.57 in FY17, HK\$1.6 in FY18 and HK\$1.65 in FY19, implying a gradual improvement in payout ratio.

Figure 76: Summary of earnings revisions

HK\$m	2017E			2018E			2019E		
	New	Old	%	New	Old	%	New	Old	%
Revenue	74,384	73,568	1%	74,180	76,236	-3%	89,085	78,102	14%
Gross Profit	31,089	26,886	16%	27,318	24,723	10%	28,861	24,997	15%
Profit before tax	26,767	23,114	16%	22,837	21,134	8%	23,852	21,179	13%
Core profit	18,313	15,677	17%	15,885	15,311	4%	17,235	15,762	9%
EPS (HK\$)	4.85	4.15	17%	4.21	4.05	4%	4.56	4.17	9%
DPS (HK\$)	1.57	1.57	0%	1.60	1.60	0%	1.65	1.65	0%

Source: Deutsche Bank estimates



Figure 77: Income Statement (HK\$m)

For year ended Dec 31	2014A	2015A	2016A	2017F	2018F	2019F
Property sales	19,389	48,141	56,475	56,995	56,696	71,516
Property rental	1,908	4,935	7,316	7,328	7,033	6,738
Hotel and serviced suite	2,213	3,767	4,823	4,379	4,388	4,388
Property/project management	528	437	500	575	661	727
Aircraft and leasing	-	-	186	4,315	4,531	4,758
Investment and others	784	580	720	792	871	958
Revenue	24,822	57,860	70,020	74,384	74,180	89,085
Cost of sales	(12,985)	(32,587)	(38,301)	(43,295)	(46,862)	(60,224)
Gross Profit	11,837	25,273	31,719	31,089	27,318	28,861
Gross interest expenses	815	1,387	1,326	2,074	2,206	2,027
Capitalized interest	-	(838)	(681)	(1,348)	(1,434)	(1,317)
Net interest expense/(income)	815	549	645	726	772	709
Net depreciation	286	508	779	818	859	902
Interest income	-	-	-	1,223	1,409	1,409
Administrative expenses	(525)	(2,475)	(3,990)	(4,247)	(4,377)	(5,078)
Others	(998)	(680)	(530)	(641)	(770)	(616)
SG&A	(1,523)	(3,155)	(4,520)	(3,665)	(3,737)	(4,285)
Profit from operations	9,213	21,061	25,775	25,880	21,950	22,965
Revaluation gains	4,542	1,408	1,262	-	-	-
Other adjustments	2,349	1,366	-	-	-	-
Associates	2,836	378	137	887	887	887
Pre-tax profit	18,940	24,213	27,174	26,767	22,837	23,852
Taxation	(1,624)	(6,305)	(7,365)	(5,789)	(5,403)	(4,901)
Post-tax profit before MI	17,316	17,908	19,809	20,979	17,434	18,951
Minority interests	(248)	(795)	(394)	(2,666)	(1,549)	(1,716)
Net attributable profit	17,068	17,113	19,415	18,313	15,885	17,235
Adjustment for non-recurring items	(5,017)	(1,545)	(1,383)	-	-	-
Core net profit	12,051	15,568	18,032	18,313	15,885	17,235
Fully diluted Core EPS (HK\$)	4.42	4.03	4.72	4.85	4.21	4.56
DPS (HK\$)	-	1.40	1.53	1.57	1.60	1.65

Source: Company data, Deutsche Bank estimates



Figure 78: Balance Sheet (HK\$m)

As of Dec 31	2014A	2015A	2016A	2017F	2018F	2019F
Non-current assets	43,514	142,721	162,559	148,726	148,726	150,098
Investment properties	33,285	119,959	125,306	125,306	125,306	125,306
Other assets	10,229	22,762	37,253	23,420	23,420	24,792
Associates	45,897	12,136	15,240	15,950	16,660	17,369
Other investments	7,172	5,451	6,233	6,233	6,233	6,233
Current assets	86,633	211,497	212,804	247,964	269,536	270,138
Properties for sale	73,259	153,301	137,548	165,889	171,744	175,610
Debtors & deposits/receivables/others	3,020	12,335	12,655	16,528	16,158	20,740
Bank balances & cash	10,354	45,861	62,601	65,546	81,633	73,789
Current liabilities	(82,796)	(36,627)	(43,757)	(41,038)	(57,675)	(58,730)
Bank loans and overdrafts	250	5,772	4,378	9,267	20,274	24,211
Forward sales deposits received	5,991	11,832	19,527	3,362	11,667	5,151
Creditors, deposits & accruals/others	75,209	14,785	17,396	17,852	17,432	20,935
Taxation	1,346	4,238	2,456	5,892	3,559	3,599
Proposed dividend	-	-	-	4,665	4,743	4,834
Total assets less current liabilities	100,420	335,178	353,079	377,834	383,479	385,109
Non-current liabilities	1,349	65,491	76,805	84,703	78,955	67,866
Long term bank loans	350	55,217	65,798	73,696	67,948	56,859
Deferred income tax	999	10,096	10,824	10,824	10,824	10,824
Others	-	178	183	183	183	183
Issued share capital	-	3,860	3,824	3,868	3,868	3,868
Share premium	-	250,951	249,179	250,943	250,943	250,943
Capital & other reserves	96,254	8,285	17,196	29,580	39,422	50,426
Shareholders' funds	96,254	263,096	270,199	284,391	294,233	305,237
Minority interests	2,817	6,591	6,075	8,741	10,290	12,006
Total capital employed	100,420	335,178	353,079	377,834	383,479	385,109

Source: Company data, Deutsche Bank estimates



Valuation and Risks

Our revised estimated NAV for CK Property is HK\$103.1/shr

Our estimated NAV is calculated via a sum-of-the-parts valuation. For development properties, we apply a DCF to estimate the value of its projects by taking the estimated cash inflow from property sales minus outstanding costs, including any outstanding land costs, construction costs, and related income taxes and LAT for China projects. For investment properties, we use the income capitalization approach, estimating the rental revenues of the investment properties and dividing this figure by the cap rates we expect. Our estimated rents and cap rates vary across the different types of properties and their locations. To arrive at the NAV for the company, we take the aggregate estimated value for the above business segments and add the company's net debt position. We value the stakes of listed companies at the prevailing market price. By factoring in our latest ASP assumption on Hong Kong residential prices (0% in 2017E, -14% in 2018E, -11% in 2019E, -3% in 2020E, -4% in 2021E, -5% in 2022E, -6% in 2023E, -6% in 2024/25E and -7% in 2026E), our revised estimated NAV is HK\$103.1/share.

Figure 79: NAV breakdown (end-FY17E)

	(HK\$ m)	(HK\$/share)	%
Development property			
Hong Kong	81,844	21.7	21.0%
Beijing	4,087	1.1	1.0%
Changchun	382	0.1	0.1%
Chengdu	2,987	0.8	0.8%
Chongqing	6,000	1.6	1.5%
Changsha	1,648	0.4	0.4%
Dongguan	2,892	0.8	0.7%
Guangzhou	3,895	1.0	1.0%
Qingdao	2,004	0.5	0.5%
Shanghai	6,021	1.6	1.5%
Changzhou	621	0.2	0.2%
Shenzhen	266	0.1	0.1%
Tianjin	899	0.2	0.2%
Wuhan	3,456	0.9	0.9%
Xi'an	660	0.2	0.2%
Zhuhai	1,781	0.5	0.5%
Dalian	3,299	0.9	0.8%
Foshan	369	0.1	0.1%
Nanjing	0	0.0	0.0%
Huizhou	356	0.1	0.1%
Jiangmen	490	0.1	0.1%
Zhongshan	153	0.0	0.0%
Singapore	828	0.2	0.2%
UK	27,635	7.3	7.1%
Bahamas	1,644	0.4	0.4%
	154,215	40.8	39.6%

Source: Deutsche Bank estimates



Figure 79: NAV breakdown (end-FY17E) (Cont'd)

	(HK\$ m)	(HK\$/share)	%
Investment property			
<u>Hong Kong</u>			
Residential	454	0.1	0.1%
Retail	51,625	13.7	13.3%
Office	102,776	27.2	26.4%
Carpark	238	0.1	0.1%
Hotel	49,095	13.0	12.6%
Others	18,641	4.9	4.8%
<u>China</u>			
Retail	8,962	2.4	2.3%
Office	103	0.0	0.0%
Hotel	2,027	0.5	0.5%
<u>Overseas</u>			
UK Office	311	0.1	0.1%
UK Industrial	1,940	0.5	0.5%
Bahamas Hotel	2,894	0.8	0.7%
	239,064	63.3	61.4%
Other assets			
Hui Xian REIT (870017.HK)	3,760	1.0	1.0%
Fortune REIT (778.HK)	4,450	1.2	1.1%
Prosperity REIT (808.HK)	956	0.3	0.2%
Farm land	3,900	1.0	1.0%
Aircraft leasing assets	7,690	2.0	2.0%
	20,756	5.5	5.3%
Gross asset value (GAV)	414,036	109.6	106.3%
Net cash / (debt)	(7,575)	(2.0)	-1.9%
Other adjustments	(16,927)	(4.5)	-4.3%
Net asset value (NAV) - fully diluted	389,534	103.1	100.0%

Source: Deutsche Bank estimates



Target price of HK\$66.1 is based on sum-of-the-parts

We believe the conventional valuation methodology of applying an overall target discount on the accessed NAV is becoming less relevant in valuing developers as market fundamentals have changed, and the historical average may not necessarily serve as a good reference. By taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is sum-of-the-parts (SOTP), where we adopt PE for the property development business and the income capitalization approach for investment properties.

In deriving our target price, we prefer a sum-of-the-parts approach to our previous methodology of applying a target discount to the overall net asset value estimate. Specifically, we believe applying a 7x PE (CKP has the highest profitability among peers) to Hong Kong property development is appropriate in an ex-growth market. For investment properties, we believe applying a 34% target discount to our estimated value on the respective investment property portfolios is appropriate as the average discount for landlords has been relatively stable at this level in the past 25 years. For China property development, we believe applying a 7x PE (at the upper range of 2019E PE for China developers and at par with industry leaders with strong financial positions, such as COLI and CR Land) is appropriate considering the financial strength and profitability profile of Hong Kong developers. Through this new valuation metric, we derive our target price for CKP at HK\$66.1.

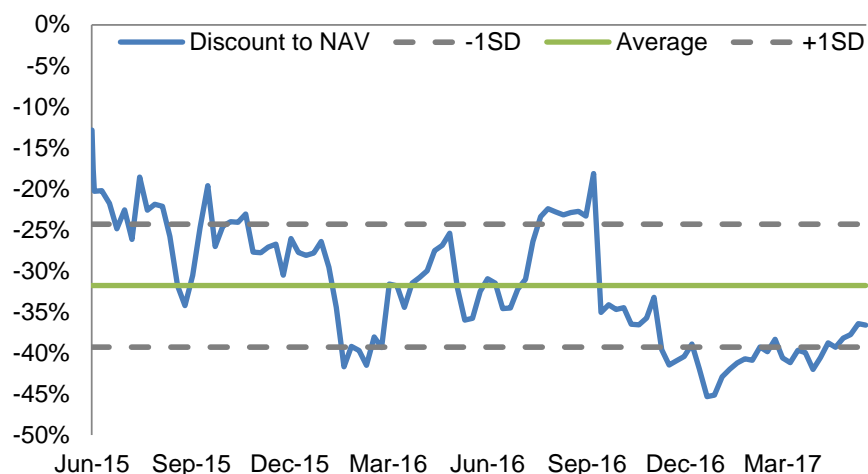
Figure 80: CKP target price breakdown

Category	HK\$ per share
Development properties – Hong Kong	8.06
Development properties – China	17.74
Investment properties	41.26
Other assets	5.43
Net cash / (debt)	(1.98)
Other adjustments	(4.45)
Target price	66.1

Source: Deutsche Bank estimates

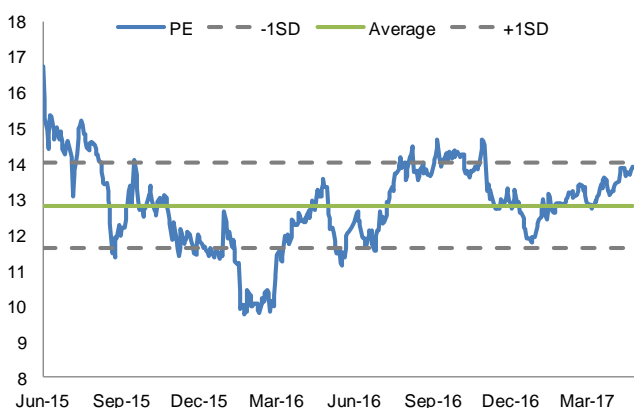


Figure 81: CKP – Discount to NAV



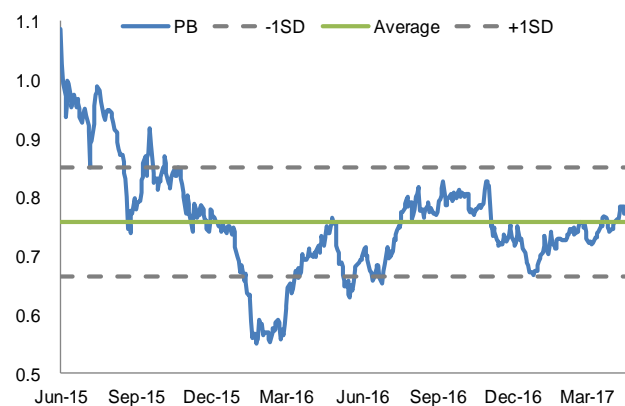
Source: Bloomberg Finance LP, Deutsche Bank estimates

Figure 82: CKP – PE chart



Source: Bloomberg Finance LP, Deutsche Bank estimates

Figure 83: CKP – PB chart



Source: Bloomberg Finance LP, Deutsche Bank estimates

Risks

- 1) Government policies: Introduction of additional policies by the Hong Kong/Chinese governments could have an adverse impact on CK Property's sales performance, earnings and profitability.
- 2) External shocks/interest rate hikes: In our view, potential external shocks/interest rate hikes would likely result in a turnaround in market sentiment and weaker housing demand which could trigger a significant correction in CK Property's key markets.



Rating Hold

Asia
Hong Kong

Property

Company SHK Properties Ltd

Reuters Bloomberg
0016.HK 16 HK

Price at 6 Jun 2017 (HKD)	124.10
Price target - 12mth (HKD)	118.50
52-week range (HKD)	124.10 - 87.35
HANG SENG INDEX	25,997

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Stronger-than-expected property market in 4M17 priced in; Hold

Maintaining Hold as stronger-than-expected property market already priced in

As the largest developer in terms of number of units for sale in Hong Kong in 2017, SHKP is a key beneficiary of the recent warm-up in the primary residential sales market, where achieved ASPs are higher than our previous expectation. However, we believe the stronger-than-expected property market in 4M17 has already been priced in, following a 20% share price rally YTD. We maintain our Hold rating but lift our target price slightly to HK\$118.5 (from HK\$117), based on a new valuation methodology, which we believe is more appropriate in an ex-growth market with an aging population.

New valuation approach – PE preferred to value property development

We believe the conventional valuation methodology, of applying an overall target discount on the assessed NAV, becomes less relevant in valuing developers, as market fundamentals have changed, so that the historical average may not necessarily serve as a good reference. By taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is SOTP, where we adopt PE for the property development business and the income capitalization approach for investment properties.

Earnings revised by -9-8% in FY17-19E; factoring in our latest ASP assumptions

As a result of worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with rising supply, which should lead the vacancy rate to more than double to 9% (from 3.8% now) and prices to slide 48% in 2017-2026 (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026). Consequently, we revise our earnings estimates by 8% to -9% in FY17-19E, and NAV upwards by 8.9%.

Target price of HK\$118.5 is based on the sum-of-the parts approach

Our target price is based on the sum-of-the-parts approach (previously target discount on overall NAV), which implies a 2017 PE of 13x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio is appropriate in an ex-growth market. Such a methodology is now our new valuation metric adopted across HK developers under our coverage. Risks: government policy, sales momentum and interest rate trend (Details on page 54).

Key changes

Price target	117.00 to 118.50	↑	1.3%
Sales (FYE)	83,925 to 88,131	↑	5.0%
Op prof margin (FYE)	32.0 to 33.3	↑	4.1%
Net profit (FYE)	24,692.2 to 26,789.1	↑	8.5%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	6.4	10.8	33.5
HANG SENG INDEX	6.2	10.2	23.6

Source: Deutsche Bank

Forecasts And Ratios

Year End Jun 30	2015A	2016A	2017E	2018E	2019E
Sales (HKDm)	66,783.0	91,184.0	88,131.0	101,842.4	107,353.7
EBITDA (HKDm)	24,750.0	30,806.0	29,387.7	28,239.6	25,201.5
Reported NPAT (HKDm)	31,082.0	32,666.0	26,789.1	25,137.3	22,412.1
DB EPS FD (HKD)	7.07	8.37	9.24	8.67	7.73
PER (x)	16.9	11.7	13.4	14.3	16.0
DPS (net) (HKD)	3.35	3.85	3.90	3.90	3.90
Yield (net) (%)	2.8	3.9	3.1	3.1	3.1

Source: Deutsche Bank estimates, company data



Model updated: 23 May 2017

Running the numbers

Asia

Hong Kong

Property

SHK Properties Ltd

Reuters: 0016.HK

Bloomberg: 16 HK

Hold

Price (6 Jun 17) HKD 124.10

Target Price HKD 118.50

52 Week range HKD 87.35 - 124.10

Market Cap (m) HKDm 359,275
USDm 46,094

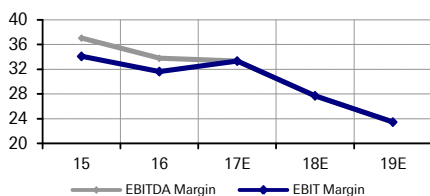
Company Profile

Sun Hung Kai Properties Limited, through its subsidiaries, develops and invests in properties. The Company also operates hotels, manages properties, car parking and transportation infrastructure. In addition, Sun Hung Kai operates logistics business, construction, financial services, internet infrastructure and enabling services.

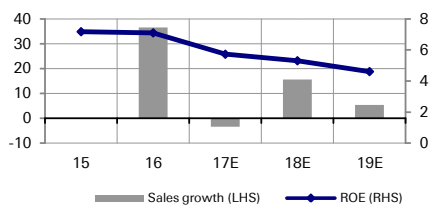
Price Performance



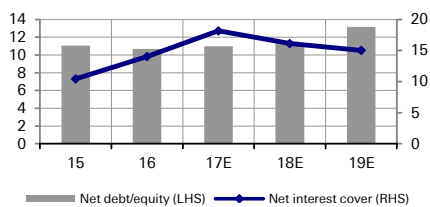
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 30-Jun

2015 2016 2017E 2018E 2019E

Financial Summary

DB EPS (HKD)	7.07	8.37	9.24	8.67	7.73
Reported EPS (HKD)	11.09	11.31	9.24	8.67	7.73
DPS (HKD)	3.35	3.85	3.90	3.90	3.90
BVPS (HKD)	156.8	161.9	161.1	165.9	169.8
Weighted average shares (m)	2,804	2,887	2,895	2,895	2,895
Average market cap (HKDm)	334,416	282,158	359,275	359,275	359,275
Enterprise value (HKDm)	333,804	277,865	352,197	352,455	359,891

Valuation Metrics

P/E (DB) (x)	16.9	11.7	13.4	14.3	16.0
P/E (Reported) (x)	10.8	8.6	13.4	14.3	16.0
P/BV (x)	0.80	0.57	0.77	0.75	0.73
FCF Yield (%)	2.2	1.7	2.7	1.6	nm
Dividend Yield (%)	2.8	3.9	3.1	3.1	3.1
EV/Sales (x)	5.0	3.0	4.0	3.5	3.4
EV/EBITDA (x)	13.5	9.0	12.0	12.5	14.3
EV/EBIT (x)	14.7	9.6	12.0	12.5	14.3

Income Statement (HKDm)

Sales revenue	66,783	91,184	88,131	101,842	107,354
Gross profit	29,766	36,689	34,794	34,606	31,953
EBITDA	24,750	30,806	29,388	28,240	25,202
Depreciation	1,972	1,950	0	0	0
Amortisation	0	0	0	0	0
EBIT	22,778	28,856	29,388	28,240	25,202
Net interest income/(expense)	-2,180	-2,055	-1,617	-1,750	-1,676
Associates/affiliates	5,550	4,216	4,943	4,103	3,956
Exceptionals/extraordinary	10,987	8,769	0	0	0
Other pre-tax income/(expense)	0	0	0	0	0
Profit before tax	37,135	39,786	32,714	30,593	27,482
Income tax expense	4,771	6,390	4,999	4,481	4,167
Minorities	1,282	730	925	974	903
Other post-tax income/(expense)	0	0	0	0	0
Net profit	31,082	32,666	26,789	25,137	22,412
DB adjustments (including dilution)	-11,257	-8,496	0	0	0
DB Net profit	19,825	24,170	26,789	25,137	22,412

Cash Flow (HKDm)

Cash flow from operations	10,555	11,336	14,526	10,346	6,854
Net Capex	-3,308	-6,624	-4,663	-4,761	-7,957
Free cash flow	7,247	4,712	9,862	5,585	-1,103
Equity raised/(bought back)	15,003	2,046	0	0	0
Dividends paid	-9,938	-10,517	0	0	0
Net inc/(dec) in borrowings	-741	-2,539	-5,347	5,175	-3,146
Other investing/financing cash flows	2,207	1,566	2,527	-5,573	-7,522
Net cash flow	13,778	-4,742	7,043	5,187	-11,771
Change in working capital	-8,204	-9,803	-2,844	-9,460	-10,479

Balance Sheet (HKDm)

Cash and other liquid assets	32,561	30,048	25,831	28,038	14,403
Tangible fixed assets	25,621	25,446	30,109	34,871	42,828
Goodwill/intangible assets	0	0	0	0	0
Associates/investments	56,975	60,807	65,750	69,854	73,810
Other assets	488,953	498,214	508,827	517,552	525,537
Total assets	604,110	614,515	630,518	650,314	656,577
Interest bearing debt	83,132	80,761	77,785	83,379	80,233
Other liabilities	64,160	59,246	79,490	78,872	76,257
Total liabilities	147,292	140,007	157,276	162,251	156,490
Shareholders' equity	451,026	468,707	466,524	480,371	491,492
Minorities	5,792	5,801	6,717	7,692	8,595
Total shareholders' equity	456,818	474,508	473,242	488,063	500,087
Net debt	50,571	50,713	51,954	55,341	65,830

Key Company Metrics

Sales growth (%)	nm	36.5	-3.3	15.6	5.4
DB EPS growth (%)	na	18.4	10.4	-6.2	-10.8
EBITDA Margin (%)	37.1	33.8	33.3	27.7	23.5
EBIT Margin (%)	34.1	31.6	33.3	27.7	23.5
Payout ratio (%)	30.2	34.0	42.1	44.9	50.4
ROE (%)	7.2	7.1	5.7	5.3	4.6
Capex/sales (%)	6.7	7.3	5.3	4.7	7.4
Capex/depreciation (x)	2.3	3.4	nm	nm	nm
Net debt/equity (%)	11.1	10.7	11.0	11.3	13.2
Net interest cover (x)	10.4	14.0	18.2	16.1	15.0

Source: Company data, Deutsche Bank estimates

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Investment Thesis

Outlook

We maintain our Hold rating on SHKP. As the largest developer in terms of number of units for sale in Hong Kong in 2017, SHKP is a key beneficiary of the recent warm-up in the primary residential sales market, where achieved ASPs are higher than our previous expectation. However, we believe the stronger-than-expected property market YTD has already been priced in, following a strong share price rally YTD.

Valuation

Our target price is based on the sum-of-the-part approach (previously target discount on overall NAV), which implies a 2017 PE of 13x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio is appropriate in an ex-growth market. For China property development, we believe applying 7x PE (at the upper range of 2019E PE for China developers and on a par to industry leaders with strong financial positions, such as COLI and CR Land) is appropriate, on consideration of the financial strength and profitability profile of Hong Kong developers. Such a methodology is now our new valuation metric adopted across HK developers under our coverage. Risks: government policy, sales momentum and interest rate trend.

Risks

The key risks to our call on SHKP include: 1) fluctuations in the Hong Kong economy may lead to higher/lower housing demand; 2) an interest rate hike and continuous liquidity outflow may severely hurt sentiment and demand in the property market; however, the property market may further strengthen if the low interest rate environment persists; 3) unexpected fluctuations in the Chinese economy could affect our forecasts; and 4) the Chinese government's measures may be stricter/looser than expected.



Financial Analysis

Earnings revised by -9-8% in FY17-19 by factoring in our latest ASP assumptions

As a result of worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with rising supply, which should lead the vacancy rate to more than double to 9% (from 3.8% now) and prices to slide 41% in 2017-2024 (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026). Our previous ASP assumption was 21% decline in 2017-2019 (-11% in 2017, -7% in 2018 and -5% in 2019). We have revised our earnings estimates by 8% to HK\$26,789mn for FY17E, 1% to HK\$25,137mn for FY18E and -9% to HK\$22,412mn for FY19E.

Figure 84: Summary of earnings revisions

	2017E			2018E			2019E		
	New	Old	%	New	Old	%	New	Old	%
Revenue	88,131	83,925	5%	101,842	106,983	-5%	107,354	105,067	2%
Gross Profit	34,794	32,006	9%	34,606	34,685	0%	31,953	34,421	-7%
Profit before tax	32,714	30,200	8%	30,593	30,280	1%	27,482	30,073	-9%
Core profit	26,789	24,692	8%	25,137	24,858	1%	22,412	24,566	-9%
EPS	9.24	8.52	8%	8.67	8.58	1%	7.73	8.48	-9%
DPS	3.90	3.90	0%	3.90	3.90	0%	3.90	3.90	0%

Source: Deutsche Bank estimates



Figure 85: Income Statement (HK\$m)

For year ended Jun 30	2014A	2015A	2016A	2017E	2018E	2019E
Property sales	33,607	17,676	40,790	36,494	48,874	52,799
... Hong Kong	26,463	11,067	36,432	30,950	46,346	49,346
... China	7,144	6,609	4,358	5,544	2,528	3,453
Property rental	14,977	16,053	17,240	16,776	16,504	16,255
... Hong Kong	12,015	12,910	13,954	13,530	13,028	12,215
... China	2,962	3,143	3,286	3,246	3,475	4,040
Hotel operation	3,930	4,136	4,031	4,084	3,917	3,856
Telecommunications	13,244	18,659	18,356	19,274	20,237	21,249
Transport infrastructure and logistics	3,507	3,549	3,781	3,819	3,857	3,896
Other businesses	5,835	6,710	6,986	7,685	8,453	9,298
Revenue	75,100	66,783	91,184	88,131	101,842	107,354
Cost of sales	(44,989)	(38,989)	(56,445)	(53,337)	(67,237)	(75,400)
Gross Profit	30,111	27,794	34,739	34,794	34,606	31,953
Gross interest expenses	2,598	2,784	2,595	2,178	2,335	2,247
Capitalized interest	(290)	(339)	(306)	(327)	(350)	(337)
Net interest expense/(income)	2,308	2,445	2,289	1,851	1,984	1,910
Interest income	258	265	234	234	234	234
Selling/marketing/Administrative expenses	(6,138)	(5,610)	(6,646)	(6,169)	(7,129)	(7,515)
Others	1,009	594	763	763	763	763
SG&A	(4,871)	(4,751)	(5,649)	(5,172)	(6,132)	(6,518)
Revaluation gains	12,131	10,987	8,769	-	-	-
Profit from operations	35,063	31,585	35,570	27,770	26,489	23,526
Associates	5,467	5,550	4,216	4,943	4,103	3,956
Pre-tax profit	40,530	37,135	39,786	32,714	30,593	27,482
Taxation	(6,195)	(4,771)	(6,390)	(4,999)	(4,481)	(4,167)
Post-tax profit before MI	34,335	32,364	33,396	27,714	26,112	23,315
Minority interests	(815)	(1,282)	(730)	(925)	(974)	(903)
Net attributable profit	33,520	31,082	32,666	26,789	25,137	22,412
Adjustment for non-recurring items	(12,105)	(11,257)	(8,496)	-	-	-
Core net profit	21,415	19,825	24,170	26,789	25,137	22,412
Fully diluted Core EPS (HK\$)	7.94	7.01	8.37	9.24	8.67	7.73
DPS (HK\$)	3.35	3.35	3.85	3.90	3.90	3.90

Source: Deutsche Bank estimates



Figure 86: Balance Sheet (HK\$m)

For year ended Jun 30	2014A	2015A	2016A	2017E	2018E	2019E
Non-current assets	308,183	339,736	348,752	353,563	358,295	366,075
Investment properties	277,640	309,205	318,517	318,517	318,517	318,517
Property and equipment	25,376	25,621	25,446	30,109	34,871	42,828
Other assets	5,167	4,910	4,789	4,937	4,907	4,730
Associates	53,589	56,975	60,807	65,750	69,854	73,810
Other investments	2,899	3,210	3,326	3,326	3,326	3,326
Current assets	192,377	204,189	201,630	207,878	218,840	213,366
Properties for sale	149,409	149,750	144,844	155,808	163,577	169,567
Inventories	299	294	596	328	344	357
Debtors & deposits/receivables/others	24,141	21,584	26,142	25,911	26,881	29,040
Bank balances & cash	18,528	32,561	30,048	25,831	28,038	14,403
Current liabilities	(46,555)	(57,733)	(59,071)	(76,249)	(89,290)	(88,129)
Bank loans and overdrafts	9,241	10,816	17,486	8,653	6,922	5,538
Other loans due within one year	-	-	-	5,349	20,739	23,577
Forward sales deposits received	5,538	13,904	6,976	22,410	23,536	20,737
Creditors, deposits & accruals/others	25,283	25,690	27,493	27,321	25,461	25,765
Taxation	6,493	7,323	7,116	3,600	3,600	3,479
Proposed dividend	-	-	-	8,917	9,033	9,033
Total assets less current liabilities	510,493	546,377	555,444	554,269	561,024	568,448
Non-current liabilities	75,051	72,735	63,526	64,203	56,137	51,537
Long term bank loans	74,490	72,316	63,275	63,784	55,718	51,118
Others	561	419	251	419	419	419
Deferred income tax	15,753	16,824	17,410	16,824	16,824	16,824
Issued share capital	53,464	68,451	70,384	68,451	68,451	68,451
Retained profits	351,820	373,382	398,323	388,880	402,727	413,848
Revaluation surplus	1,134	1,249	1,249	1,249	1,249	1,249
Capital & other reserves	8,365	7,944	7,944	7,944	7,944	7,944
Shareholders' funds	414,783	451,026	468,707	466,524	480,371	491,492
Minority interests	4,906	5,792	5,801	6,717	7,692	8,595
Total capital employed	510,493	546,377	555,444	554,269	561,024	568,448

Source: Deutsche Bank estimates



Valuation

Our revised estimated NAV for SHKP is HK\$195.6/shr

Our estimated NAV is calculated via a sum-of-the-parts valuation. For development properties, we apply a DCF to estimate the value of its projects by taking the estimated cash inflows from property sales minus outstanding costs, including any outstanding land costs, construction costs, and related income taxes and LAT for China projects. For investment properties, we use the income capitalization approach, taking the estimated rental revenues of the investment properties and dividing this figure by the estimated cap rates. Our estimated rents and cap rates vary across the different types of property and their locations. When arriving at the NAV for the company, we take the aggregate estimated value for the above business segments and add the company's net debt position. We value the stakes of listed companies at the prevailing market price. By factoring in our latest ASP assumption on Hong Kong residential prices (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026), our revised estimated NAV is HK\$195.6/share.

Figure 87: NAV breakdown (end-FY17)

	(HK\$ mn)	(HK\$/share)	%
Development property			
Hong Kong	68,878	23.8	12.2%
Guangzhou	1,028	0.4	0.2%
Zhongshan	209	0.1	0.0%
Chengdu	788	0.3	0.1%
Shanghai	5,235	1.8	0.9%
Suzhou	444	0.2	0.1%
Foshan	1,244	0.4	0.2%
Dongguan	844	0.3	0.1%
	78,669	27.2	13.9%
Investment property			
<u>Hong Kong</u>			
Residential	9,219	3.2	1.6%
Retail	157,333	54.3	27.8%
Office	146,864	50.7	25.9%
Hotel	55,603	19.2	9.8%
Other	10,964	3.8	1.9%
<u>China</u>			
Residential	2,910	1.0	0.5%
Retail	77,427	26.7	13.7%
Office	51,248	17.7	9.1%
Hotel	8,707	3.0	1.5%
<u>Singapore</u>			
Retail	21,264	7.3	3.8%
	541,539	187.1	95.6%

Source: Deutsche Bank estimates



Figure 87: NAV breakdown (end-FY17) (Cont'd)

	(HK\$ mn)	(HK\$/share)	%
Other assets			
SmarTone (0315.HK)	7,174	2.5	1.3%
Sunevision (8008.HK)	5,502	1.9	1.0%
Transport International Holdings (0062.HK)	2,907	1.0	0.5%
RoadShow Holdings (0888.HK)	556	0.2	0.1%
Agricultural land (30mn sf site area)	9,000	3.1	1.6%
	25,139	8.7	4.4%
Gross asset value (GAV)			
	645,347	222.9	114.0%
Net cash / (debt)	(50,713)	(17.5)	-9.0%
Other adjustments	(27,791)	(9.6)	-4.9%
Net asset value (NAV) - fully diluted	566,843	195.6	100.0%

Source: Deutsche Bank estimates

Target price of HK\$118.5 is based upon sum-of-the-parts

We believe the conventional valuation methodology of applying an overall target discount on the assessed NAV becomes less relevant in valuing developers as market fundamentals have changed, so that the historical average may not necessarily serve as a good reference. By taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is SOTP, where we adopt PE for the property development business and the income capitalization approach for investment properties.

In deriving the target price, we prefer the sum-of-the-parts approach to the previous methodology of applying a target discount to the overall Net Asset Value estimate. Specifically, we believe applying 6x PE to Hong Kong property development is appropriate in an ex-growth market. Meanwhile, for investment properties, we believe applying a 34% target discount to our estimated value on the respective investment property portfolio is appropriate as the average discount for landlords has been relatively stable at 34% in the past 25 years. For China property development, we believe applying 7x PE (at the upper range of 2019E PE for China developers and on par to industry leaders with strong financial positions such as COLI and CR Land) is appropriate in consideration of the financial strength and profitability profile of Hong Kong developers. On adopting the new valuation metric, we derive our target price for SHKP at HK\$118.5.

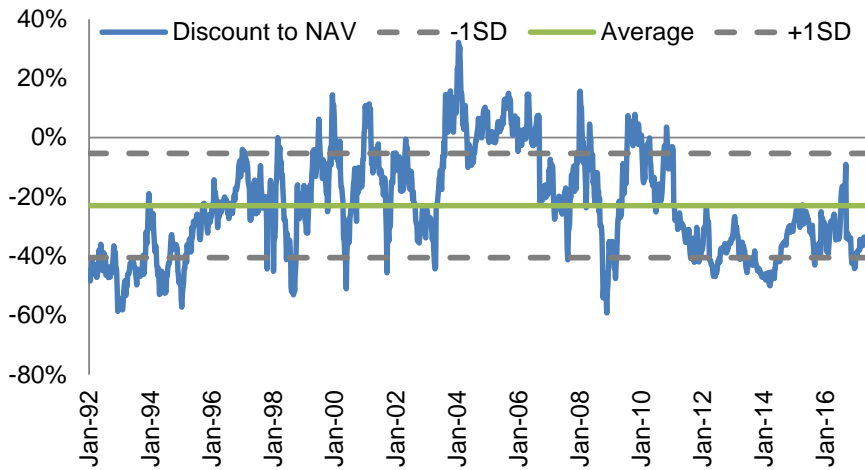
Figure 88: SHKP target price breakdown

Category	HK\$ per share
Development properties – Hong Kong	10.78
Development properties - China	2.73
Investment properties	123.46
Other assets	8.68
Net cash / (debt)	(17.52)
Other adjustments	(9.60)
Target price	118.5

Source: Deutsche Bank estimates

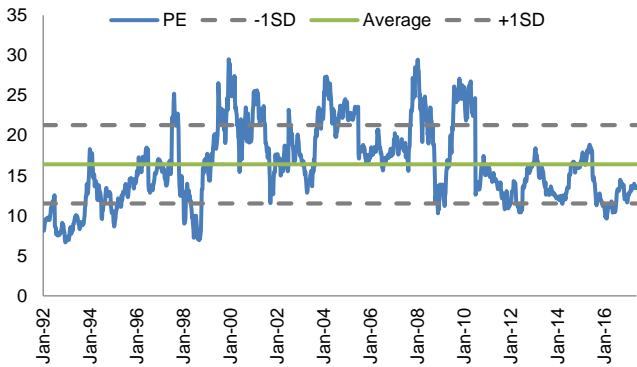


Figure 89: SHKP – Discount to NAV



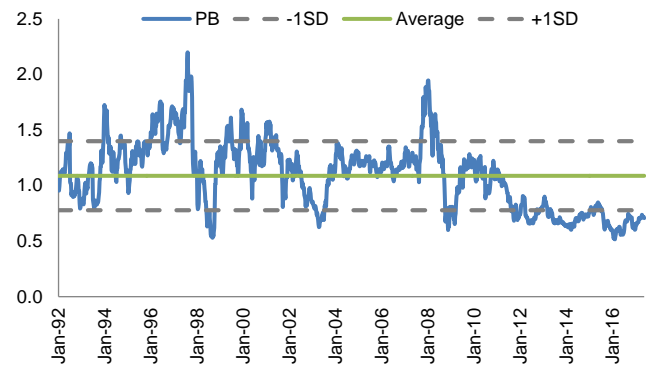
Source: Bloomberg Finance LP, Deutsche Bank estimates

Figure 90: SHKP – PE chart



Source: Bloomberg Finance LP, Deutsche Bank estimates

Figure 91: SHKP – PB chart



Source: Bloomberg Finance LP, Deutsche Bank estimates



Risks

Macro and company-specific risks

1. Fluctuations in the Hong Kong economy may lead to higher/lower housing demand;
2. An interest rate hike and continuous liquidity outflow may severely harm sentiment and demand in the property market. On the other hand, the property market may further strengthen if the low interest rate environment persists;
3. Unexpected fluctuations in the Chinese economy could affect our forecasts;

The Chinese government's measures may be stricter/looser than expected.



Rating
Hold

Asia
Hong Kong

Property

Company
**Henderson Land
Dev. Co.**

Reuters: 0012.HK
Bloomberg: 12 HK

Price at 6 Jun 2017 (HKD)	52.55
Price target - 12mth (HKD)	49.80
52-week range (HKD)	52.55 - 40.35
HANG SENG INDEX	25,997

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Near-term catalysts already priced in post YTD rally; downgrading to Hold

Downgrading to Hold as near-term catalysts already priced in; TP HK\$49.8

We downgrade Henderson Land, from Buy to Hold, with a revised target price of HK\$49.8 (HK\$56.2), based upon a new valuation methodology, which we believe is more appropriate in an ex-growth market with an aging population. We like Henderson's large agricultural land reserve/good progress in acquiring projects via urban redevelopment, which we believe is a competitive edge in alternative sourcing of landbank so as to ensure better profitability (which is increasingly important with intensifying competition from Mainland developers in government tenders). However, we believe the near-term catalyst has already been priced in at the current price, post a 23% share price rally YTD.

New valuation approach – PE preferred to value property development

We believe the conventional valuation methodology, of applying an overall target discount on the assessed NAV, becomes less relevant in valuing developers, as market fundamentals have changed, so that the historical average may not necessarily serve as a good reference. Taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is SOTP, where we adopt PE for the property development business and the income capitalization approach for investment properties.

Earnings revised by -2-13% in FY17-19E; factoring in our latest ASP assumptions

As a result of worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with rising supply, which will inevitably lead to the vacancy rate more than doubling to 9% (from 3.8% now) and prices sliding 48% in 2017-2026 (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026). Consequently, we revise our earnings estimates by -2% to 13% in FY17-19E, and NAV upwards by 6.9%.

Target price of HK\$49.8 is based on the sum-of-the parts approach

Our target price is based on the sum-of-the-parts approach (previously it was on target discount on overall NAV), which implies a 2017 PE of 15x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio is appropriate in an ex-growth market. Such a methodology is now our new valuation metric adopted across HK developers under our coverage. Risks: government policy, sales momentum and interest rate trend.

Forecasts And Ratios

Year End Dec 31	2015A	2016A	2017E	2018E	2019E
Sales (HKDm)	23,641.0	25,568.0	23,126.3	21,061.7	21,790.5
EBITDA (HKDm)	8,516.0	8,276.0	9,807.4	9,080.3	6,879.5
Reported NPAT (HKDm)	21,326.0	21,916.0	12,451.9	12,194.6	10,307.6
DB EPS FD (HKD)	3.03	3.90	3.42	3.35	2.83
PER (x)	17.3	11.5	15.4	15.7	18.5
DPS (net) (HKD)	1.45	1.55	1.60	1.65	1.70
Yield (net) (%)	2.8	3.5	3.0	3.1	3.2

Source: Deutsche Bank estimates, company data

Key changes

Rating	Buy to Hold	↓	
Price target	56.20 to 49.80	↓	-11.4%
Sales (FYE)	21,181 to 23,126	↑	9.2%
Op prof margin (FYE)	37.1 to 42.4	↑	14.2%
Net profit (FYE)	10,993.4 to 12,451.9	↑	13.3%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	8.6	16.8	21.9
HANG SENG INDEX	6.2	10.2	23.6

Source: Deutsche Bank



Model updated: 23 May 2017

Running the numbers

Asia

Hong Kong

Property

Henderson Land Dev. Co.

Reuters: 0012.HK

Bloomberg: 12 HK

Hold

Price (6 Jun 17) HKD 52.55

Target Price HKD 49.80

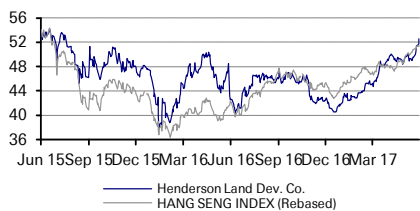
52 Week range HKD 40.35 - 52.55

Market Cap (m) HKDm 191,146
USDm 24,524

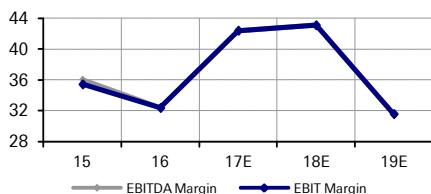
Company Profile

Henderson Land Development Company Limited, through its subsidiaries, develops, invests in, and manages properties. The Company also provides project management, construction, and finance services. In addition, Henderson Land Development operates department stores, hotels and infrastructure business.

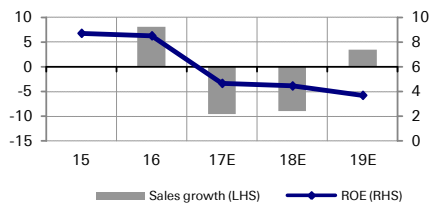
Price Performance



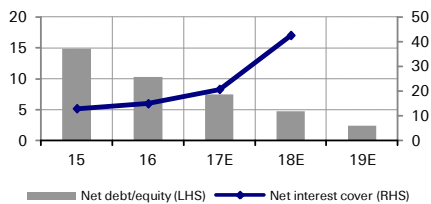
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 31-Dec

Financial Summary

	2015	2016	2017E	2018E	2019E
DB EPS (HKD)	3.03	3.90	3.42	3.35	2.83
Reported EPS (HKD)	5.87	6.03	3.42	3.35	2.83
DPS (HKD)	1.45	1.55	1.60	1.65	1.70
BVPS (HKD)	76.0	72.5	74.4	76.1	84.9
Weighted average shares (m)	3,633	3,637	3,637	3,637	3,637
Average market cap (HKDm)	190,695	162,248	191,146	191,146	191,146
Enterprise value (HKDm)	146,262	99,805	121,070	112,629	106,682

Valuation Metrics

	2015	2016	2017E	2018E	2019E
P/E (DB) (x)	17.3	11.5	15.4	15.7	18.5
P/E (Reported) (x)	8.9	7.4	15.4	15.7	18.5
P/BV (x)	0.63	0.57	0.71	0.69	0.62
FCF Yield (%)	2.7	6.9	9.4	11.3	8.8
Dividend Yield (%)	2.8	3.5	3.0	3.1	3.2
EV/Sales (x)	6.2	3.9	5.2	5.3	4.9
EV/EBITDA (x)	17.2	12.1	12.3	12.4	15.5
EV/EBIT (x)	17.5	12.1	12.3	12.4	15.5

Income Statement (HKDm)

	2015	2016	2017E	2018E	2019E
Sales revenue	23,641	25,568	23,126	21,062	21,791
Gross profit	9,675	9,064	10,286	9,583	7,407
EBITDA	8,516	8,276	9,807	9,080	6,880
Depreciation	139	0	0	0	0
Amortisation	0	0	0	0	0
EBIT	8,377	8,276	9,807	9,080	6,880
Net interest income/(expense)	-649	-555	-474	-213	47
Associates/affiliates	8,300	7,780	6,668	6,872	5,533
Exceptionals/extraordinary	7,310	8,940	0	0	0
Other pre-tax income/(expense)	0	0	0	0	0
Profit before tax	23,338	24,441	16,001	15,739	12,459
Income tax expense	1,464	2,255	2,640	2,597	2,056
Minorities	548	270	909	947	96
Other post-tax income/(expense)	0	0	0	0	0
Net profit	21,326	21,916	12,452	12,195	10,308
DB adjustments (including dilution)	-10,317	-7,747	0	0	0
DB Net profit	11,009	14,169	12,452	12,195	10,308

Cash Flow (HKDm)

	2015	2016	2017E	2018E	2019E
Cash flow from operations	5,600	14,123	19,081	21,732	17,032
Net Capex	-408	-2,980	-1,198	-117	-123
Free cash flow	5,192	11,143	17,883	21,615	16,909
Equity raised/(bought back)	0	0	331	0	0
Dividends paid	-3,391	-5,773	-6,274	-6,475	-6,231
Net inc/(dec) in borrowings	4,774	4,312	1,992	-1,808	1,513
Other investing/financing cash flows	-5,145	607	-3,888	-5,392	-3,654
Net cash flow	1,430	10,289	10,043	7,940	8,537
Change in working capital	0	0	0	0	0

Balance Sheet (HKDm)

	2015	2016	2017E	2018E	2019E
Cash and other liquid assets	11,779	22,966	32,532	40,472	49,264
Tangible fixed assets	130,289	133,269	134,467	134,584	134,707
Goodwill/intangible assets	527	377	807	762	696
Associates/investments	87,572	95,884	97,006	98,700	98,207
Other assets	106,102	103,002	103,875	106,744	104,528
Total assets	336,269	355,498	368,687	381,262	387,402
Interest bearing debt	49,896	50,640	53,240	53,960	56,264
Other liabilities	30,104	35,557	38,729	43,917	43,581
Total liabilities	80,000	86,197	91,969	97,877	99,845
Shareholders' equity	251,247	263,534	270,497	276,690	280,814
Minorities	5,022	5,767	6,222	6,695	6,743
Total shareholders' equity	256,269	269,301	276,718	283,385	287,557
Net debt	38,117	27,674	20,708	13,488	7,000

Key Company Metrics

	2015	2016	2017E	2018E	2019E
Sales growth (%)	nm	8.2	-9.5	-8.9	3.5
DB EPS growth (%)	na	28.6	-12.1	-2.1	-15.5
EBITDA Margin (%)	36.0	32.4	42.4	43.1	31.6
EBIT Margin (%)	35.4	32.4	42.4	43.1	31.6
Payout ratio (%)	24.7	25.7	46.7	49.2	60.0
ROE (%)	8.7	8.5	4.7	4.5	3.7
Capex/sales (%)	3.1	11.7	5.2	0.6	0.6
Capex/depreciation (x)	5.2	nm	nm	nm	nm
Net debt/equity (%)	14.9	10.3	7.5	4.8	2.4
Net interest cover (x)	12.9	14.9	20.7	42.5	nm

Source: Company data, Deutsche Bank estimates

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Investment Thesis

Outlook

We have a Hold rating on Henderson Land. We like Henderson's large agricultural land reserve/good progress in acquiring projects via urban redevelopment – which we believe is a competitive edge in alternative sourcing of landbank so as to ensure better profitability, something that is increasingly important with intensifying competition from Mainland developers in government tenders. However, we believe the near-term catalyst has already been priced in at the current price, following a 23% share price rally YTD.

Valuation

Our target price is based on a sum-of-the-parts approach (previously it was on target discount on overall NAV), which implies a 2017 PE of 15x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio is appropriate in an ex-growth market. For China property development, we believe applying 7x PE (at the upper range of 2019E PE for China developers and on a par to industry leaders with strong financial positions, such as COLI and CR Land) is appropriate, in consideration of the financial strength and profitability profile of Hong Kong developers. Such a methodology is now our new valuation metric, adopted across HK developers under our coverage.

Risks

Macro risks: 1) external shocks and interest rate hikes; if the low interest rate environment persists for longer, the current high property prices could be well supported for longer, and vice versa; 2) government tightening measures might be stricter than expected and adversely impacting the property market; on the other hand, the property market could be boosted if the government decided to loosen the current administrative tightening measures; and 3) unexpected economic fluctuations in the HK/Chinese economy may have a positive/negative impact on housing demand.

Company-specific risks: 1) its track record on execution in China is not fully proven; however, if execution improves, we may see a re-rating; 2) HLD could face stronger-than-expected competition for land bank; however, if competition is less intensified, as expected, it may be able to acquire land at more reasonable prices, leading to higher NAV growth.



Financial Analysis

Earnings revised by -2-13% in FY17-19 by factoring in our latest ASP assumptions

As a result of worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with rising supply, which will inevitably lead to the vacancy rate more than doubling to 9% (from 3.8% now) and prices sliding 48% in 2017-2026 (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026). Our previous ASP assumption was a 21% decline in 2017-2019 (-11% in 2017, -7% in 2018 and -5% in 2019). We have revised our earnings estimates by 13% to HK\$12,452mn for FY17E, 11% to HK\$12,195mn for FY18E, and -2% to HK\$10,308mn for FY19E.

Figure 92: Summary of earnings revisions

	2017E			2018E			2019E		
	New	Old	%	New	Old	%	New	Old	%
Revenue	23,126	21,181	9%	21,062	19,970	5%	21,791	22,135	-2%
Operating profit	10,177	8,231	24%	9,458	8,364	13%	7,254	7,595	-4%
Pre-tax profit	16,001	14,055	14%	15,739	14,028	12%	12,459	12,690	-2%
Core profit	12,452	10,993	13%	12,195	10,976	11%	10,308	10,500	-2%
EPS	3.42	3.02	13%	3.35	3.02	11%	2.83	2.89	-2%
DPS	1.60	1.60	0%	1.65	1.65	0%	1.70	1.70	0%

Source: Deutsche Bank estimates



Figure 93: Income Statement (HK\$m)

Year ended Dec 31	2014	2015	2016	2017E	2018E	2019E
Sale of properties	15,466	15,690	17,679	15,054	12,972	13,709
Property investment	5,445	5,589	5,559	5,628	5,526	5,391
Building construction	888	-	-	-	-	-
Hotel operation	188	99	78	80	81	83
Department Stores	431	879	871	915	960	1,008
Others	953	1,384	1,381	1,450	1,523	1,599
Revenue	23,371	23,641	25,568	23,126	21,062	21,791
Total operating profit	6,956	8,570	10,530	10,177	9,458	7,254
Gross interest expenses	(2,021)	(1,795)	(1,740)	(1,405)	(985)	(546)
Capitalized interest	1,162	953	858	562	394	218
Net interest (expense)\income	(859)	(842)	(882)	(843)	(591)	(328)
Profit from operations	6,097	7,728	9,648	9,334	8,867	6,926
Associates & Jointly Controlled Entities	6,838	8,300	7,780	6,668	6,872	5,533
Revaluation of investment properties	5,538	7,310	7,013	-	-	-
Exceptional items	5,538	7,310	7,013	-	-	-
Pre-tax profit	18,473	23,338	24,441	16,001	15,739	12,459
Total taxation	(1,533)	(1,464)	(2,255)	(2,640)	(2,597)	(2,056)
Profit after-tax before minority interests	16,940	21,874	22,186	13,361	13,142	10,403
Minority interests	(188)	(548)	(270)	(909)	(947)	(96)
Net profit	16,752	21,326	21,916	12,452	12,195	10,308
Core EPS (HK\$) - Fully diluted	5.44	5.72	5.87	3.42	3.35	2.83
DPS (HK\$)	1.10	1.45	1.55	1.60	1.65	1.70

Source: Deutsche Bank estimates



Figure 94: Balance Sheet (HK\$m)

As at 31 Dec	2014	2015	2016	2017E	2018E	2019E
Fixed assets	119,705	130,289	133,269	134,467	134,584	134,707
Investment properties	119,705	130,289	133,269	134,356	134,356	134,356
Other fixed assets	-	-	-	111	228	351
Associates & Jointly controlled entities	82,511	87,572	92,664	93,786	95,480	94,987
Investment in securities	7,741	8,622	11,212	11,212	11,212	11,212
Intangibles and deferred tax assets	917	527	377	807	762	710
Current assets	106,106	109,259	117,976	128,415	139,224	145,800
Leasehold land	9,888	10,130	10,334	10,334	10,334	10,334
Property under development	60,615	61,884	54,440	56,252	59,310	57,467
Completed properties for sale	9,518	9,460	10,388	8,469	8,930	8,653
Inventories & amts due from customers	80	82	80	212	223	216
Deposits for acquisition of property	5,463	4,820	4,608	5,646	5,953	5,768
Debtors & deposits	7,018	6,017	8,979	7,929	7,096	7,391
Installments receivable	1,281	2,146	1,561	2,421	2,285	2,087
Amt due from associates & JC entities	221	208	111	111	111	111
Assets classified as held for sale	-	-	3,220	3,220	3,220	3,220
Cash held by stakeholders	1,719	2,733	1,289	1,289	1,289	1,289
Bank balances & cash	10,303	11,779	22,966	32,532	40,472	49,264
Current liabilities	(32,240)	(32,304)	(42,461)	(46,233)	(52,741)	(53,329)
Bank loans and overdrafts	13,590	10,216	14,392	14,992	16,312	17,236
Other loans due within one year	-	2,192	5,760	5,152	2,624	1,833
Forward sales deposits received	6,404	8,235	8,353	12,174	20,733	21,058
Rental & other deposits	1,374	1,428	1,750	1,407	1,381	1,348
Creditors, deposits & accruals	8,505	8,484	7,748	8,094	7,372	7,627
Derivative financial instruments	-	3	318	318	318	318
Amount due to associates & JC entities	1,021	948	3,054	3,054	3,054	3,054
Amount due to a fellow subsidiary	409	8	-	-	-	-
Taxation	937	790	1,054	1,010	915	824
Liabilities classified as held for sale	-	-	32	32	32	32
Total assets less current liabilities	284,740	303,965	313,037	322,454	328,521	334,073
Long term liabilities	41,523	47,696	43,736	45,736	45,136	46,516
Long term bank loans	12,968	24,798	28,086	30,086	29,486	30,866
Other long term loans	16,144	13,705	7,846	7,846	7,846	7,846
Derivatives financial instruments	1,473	1,773	906	906	906	906
Amounts due to fellow subsidiaries	4,612	1,177	316	316	316	316
Deferred Tax Liabilities	6,326	6,243	6,582	6,582	6,582	6,582
Minority interests	5,067	5,022	5,767	6,222	6,695	6,743
Share Capital	5,699	52,345	52,345	52,676	52,676	52,676
Share Premium	46,311	-	-	-	-	-
Retained Profits	177,482	195,592	211,189	217,821	224,014	228,138
Shareholders' funds	238,150	251,247	263,534	270,497	276,690	280,814
Total capital employed	284,740	303,965	313,037	322,454	328,521	334,073

Source: Deutsche Bank estimates



Valuation

Our revised estimated NAV for HLD is HK\$80.1/shr

Our estimated NAV is calculated via a sum-of-the parts valuation. For development properties, we apply a DCF to estimate the value of its projects by taking the estimated cash inflows from property sales minus outstanding costs, including any outstanding land costs, construction costs, and related income taxes and LAT for China projects. For investment properties, we use the income capitalization approach, taking the estimated rental revenues of the investment properties and dividing this figure by the estimated cap rates. Our estimated rents and cap rates vary across the different types of property and their locations. When arriving at the NAV for the company, we take the aggregate estimated value for the above business segments and add the company's net debt position. We value the stakes of listed companies at the prevailing market price. By factoring in our latest ASP assumption on Hong Kong residential prices (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026), our revised estimated NAV is HK\$80.1/share.

Figure 95: NAV breakdown (end-FY17)

	NAV (HK\$m)	NAV/share (HK\$)	% of NAV
Development Properties			
Hong Kong Residential	34,839	10.5	13.2%
Hong Kong Farmland	3,854	1.2	1.5%
China Residential	657	0.2	0.2%
	39,350	11.9	14.9%
Investment Properties			
Hong Kong Residential	1,873	0.6	0.6%
Hong Kong Car parks	5,513	1.7	1.8%
Hong Kong Office	38,922	11.8	13.1%
Hong Kong Retail	77,245	23.4	25.9%
Hong Kong Industrial	3,463	1.0	1.2%
Hong Kong Hotel	8,304	2.5	2.8%
China Office	32,365	9.8	10.9%
China Retail	519	0.2	0.2%
	168,204	50.9	56.4%
Other Assets			
Miramar Hotels	4,215	1.3	1.6%
Hongkong and China Gas	65,874	19.9	24.9%
HK Ferries	1,076	0.3	0.4%
Agricultural land	13,440	4.1	5.1%
Other financial assets	6,023	1.8	2.3%
	90,628	27.4	34.2%
Gross asset value	298,182	90.2	112.6%
Net debt	(33,434)	(10.1)	-12.0%
Fully-diluted net asset value	264,748	80.1	100.0%

Source: Deutsche Bank estimates



Target price of HK\$49.8 is based upon sum-of-the-parts

We believe the conventional valuation methodology of applying an overall target discount on the assessed NAV becomes less relevant in valuing developers, as market fundamentals have changed, so that the historical average may not necessarily serve as a good reference. By taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is SOTP, where we adopt PE for the property development business and the income capitalization approach for investment properties.

In deriving the target price, we prefer the sum-of-the-parts approach to the previous methodology of applying a target discount to the overall Net Asset Value estimate. Specifically, we believe applying 5x PE to Hong Kong property development is appropriate in an ex-growth market. Meanwhile, for investment properties, we believe applying a 34% target discount to our estimated value on the respective investment property portfolio is appropriate as the average discount for landlords has been relatively stable at 34% in the past 25 years. For China property development, we believe applying 7x PE (at the upper range of 2019E PE for China developers and on a par with industry leaders with strong financial positions such as COLI and CR Land) is appropriate by considering the financial strength and profitability profile of Hong Kong developers. On adopting the new valuation metric, we derive our target price for HLD at HK\$49.8.

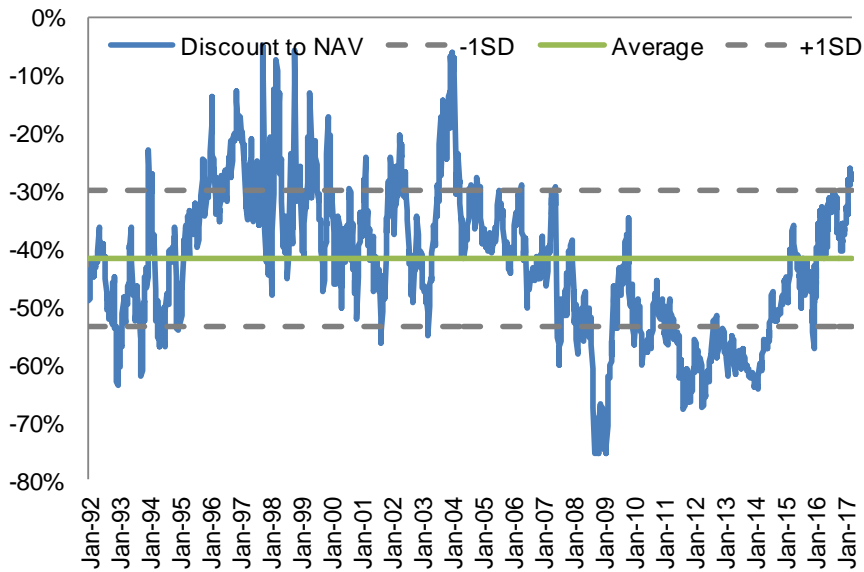
Figure 96: HLD target price breakdown

Category	HK\$ per share
Development properties – Hong Kong	3.5
Development properties - China	0.1
Investment properties	30.5
Other assets	24.9
Net cash / (debt)	(9.2)
Target price	49.8

Source: Deutsche Bank estimates

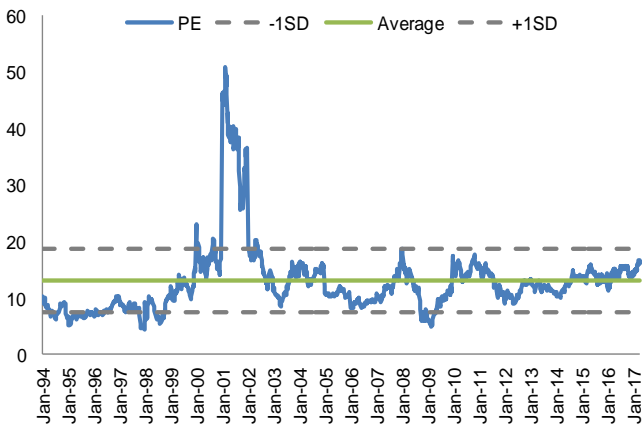


Figure 97: HLD – Discount to NAV



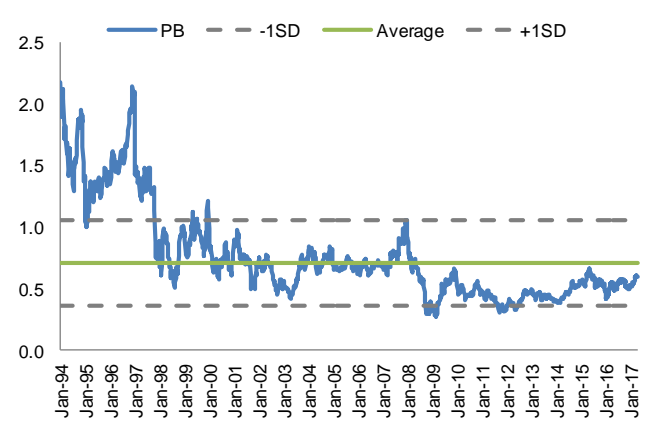
Source: Bloomberg Finance LP, Deutsche Bank estimates

Figure 98: HLD – PE chart



Source: Bloomberg Finance LP, Deutsche Bank estimates

Figure 99: HLD – PB chart



Source: Bloomberg Finance LP, Deutsche Bank estimates



Risks

Macro risks

- 1) External shocks and interest rate hikes; if the low interest rate environment persists for longer, current high property prices could be well supported for longer and vice versa;
- 2) Government tightening measures might be stricter than expected and adversely impact the property market; on the other hand, the property market could be boosted if the government decided to loosen the current administrative tightening measures;
- 3) Unexpected economic fluctuations in the HK/Chinese economy may have a positive/negative impact on housing demand.

Company-specific risks

- 1) Its track record in execution in China is not fully proven; however, if execution improves, we may see a re-rating;
- 2) HLD could face stronger-than-expected competition for land bank; however, if competition is less intensified, as expected, it may be able to acquire land at more reasonable prices, leading to higher NAV growth.



Rating
Hold

Asia
Hong Kong

Property

Company
Sino Land Co

Reuters: 0083.HK
Bloomberg: 83 HK

Price at 6 Jun 2017 (HKD)	14.02
Price target - 12mth (HKD)	14.30
52-week range (HKD)	14.34 - 11.16
HANG SENG INDEX	25,997

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Research Analyst
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Stronger-than-expected property market in 4M17 priced in; Hold

Maintaining Hold as stronger-than-expected property market already priced in
Sino-Land stands out among its peers with net cash since 2013; its net cash position stood at HK\$23bn as of 1HFY17, or about 16% of our estimated NAV. It has also benefited from the recent heating up of the primary residential sales market, where achieved ASPs are higher than our former expectations. However, we believe these positive catalysts are already reflected in the share price, following a 20% share price rally YTD (vs the sector +22%, Hang Seng Index +18%). We maintain Hold with a revised target price of HK\$14.3 (from HK\$14.1), based on a new valuation methodology, which we believe is more appropriate in an ex-growth market for an aging population.

New valuation approach – PE preferred to value property development

We believe the conventional valuation methodology of applying an overall target discount on the accessed NAV becomes less relevant in valuing developers as market fundamentals have changed, and the historical average may not necessarily serve as a good reference. By taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is SOTP, where we adopt PE for the property development business and the income capitalization approach for investment properties.

Revising earnings by -5%–1% for FY17-19E; factoring latest ASP assumptions

As a result of worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with rising supply, which should lead the vacancy rate to more than double to 9% (from 3.8% now) and prices to slide 48% in 2017E-2026E (0% in 2017E, -14% in 2018E, -11% in 2019E, -3% in 2020E, -4% in 2021E, -5% in 2022E, -6% in 2023E, -6% in 2024/25E and -7% in 2026E). Consequently, we revise our earnings estimates by -5% to 1% for FY17-19, and NAV upwards by 9.2%.

Target price of HK\$14.3 is based on sum-of-the parts approach

Our target price is based on the sum-of-the-part approach (previously target discount on overall NAV), implying a 2017 PE of 17x. We believe that applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio is appropriate in an ex-growth market (see page 75). This methodology is our new valuation metric adopted across HK developers under our coverage. Upside/downside risks are related to government policy, sales momentum and the interest rate trend (see page 77).

Forecasts And Ratios

Year End Jun 30	2015A	2016A	2017E	2018E	2019E
Sales (HKDm)	21,838.5	10,803.7	14,620.4	13,090.7	11,151.6
EBITDA (HKDm)	5,018.1	3,709.1	4,724.1	4,382.8	3,997.6
Reported NPAT (HKDm)	9,370.0	7,090.4	5,045.4	4,972.2	4,503.6
DB EPS FD (HKD)	0.88	0.87	0.82	0.81	0.73
PER (x)	14.7	13.4	17.1	17.4	19.2
DPS (net) (HKD)	0.50	0.51	0.51	0.51	0.51
Yield (net) (%)	3.9	4.4	3.6	3.6	3.6

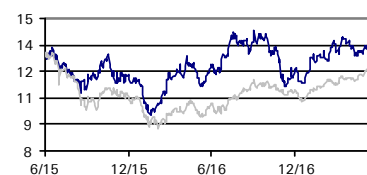
Source: Deutsche Bank estimates, company data

Key changes

Price target	14.10 to 14.30	↑	1.4%
Sales (FYE)	12,175 to 14,620	↑	20.1%
Op prof margin (FYE)	36.5 to 32.3	↓	-11.5%
Net profit (FYE)	5,267.6 to 5,045.4	↓	-4.2%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	7.8	3.1	14.9
HANG SENG INDEX	6.2	10.2	23.6

Source: Deutsche Bank



Model updated: 31 May 2017

Running the numbers

Asia

Hong Kong

Property

Sino Land Co

Reuters: 0083.HK

Bloomberg: 83 HK

Hold

Price (6 Jun 17) HKD 14.02

Target Price HKD 14.30

52 Week range HKD 11.16 - 14.34

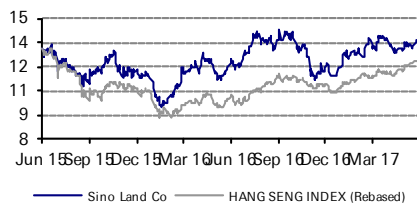
Market Cap (m) HKDm 86,432

USDm 11,089

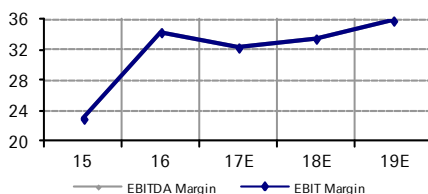
Company Profile

Sino Land Company Limited, through its subsidiaries, develops and invests in real estate, trades and invests in securities, and provides financing and management services. The Company also operates hotels.

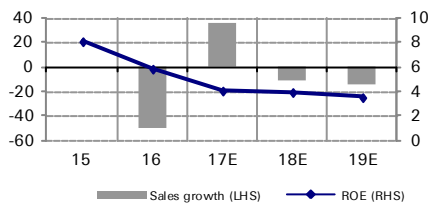
Price Performance



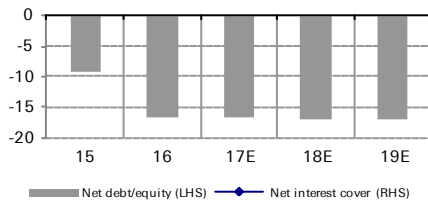
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 30-Jun

Financial Summary

	2015	2016	2017E	2018E	2019E
DB EPS (HKD)	0.88	0.87	0.82	0.81	0.73
Reported EPS (HKD)	1.54	1.15	0.82	0.81	0.73
DPS (HKD)	0.50	0.51	0.51	0.51	0.51
BVPS (HKD)	19.5	19.8	20.1	20.4	20.6
Weighted average shares (m)	6,049	6,114	6,165	6,165	6,165
Average market cap (HKDm)	77,923	71,060	86,432	86,432	86,432
Enterprise value (HKDm)	37,044	21,597	36,972	36,178	36,827

Valuation Metrics

	2015	2016	2017E	2018E	2019E
P/E (DB) (x)	14.7	13.4	17.1	17.4	19.2
P/E (Reported) (x)	8.4	10.1	17.1	17.4	19.2
P/BV (x)	0.67	0.64	0.70	0.69	0.68
FCF Yield (%)	9.6	12.0	3.1	2.1	1.6
Dividend Yield (%)	3.9	4.4	3.6	3.6	3.6
EV/Sales (x)	1.7	2.0	2.5	2.8	3.3
EV/EBITDA (x)	7.4	5.8	7.8	8.3	9.2
EV/EBIT (x)	7.4	5.8	7.8	8.3	9.2

Income Statement (HKDm)

Sales revenue	21,839	10,804	14,620	13,091	11,152
Gross profit	7,122	4,698	6,095	5,601	5,022
EBITDA	5,018	3,709	4,724	4,383	3,998
Depreciation	0	1	0	0	0
Amortisation	0	0	0	0	0
EBIT	5,018	3,708	4,724	4,383	3,998
Net interest income/(expense)	298	295	294	237	286
Associates/affiliates	2,030	1,981	1,490	2,240	1,409
Exceptionals/extraordinary	0	0	0	0	0
Other pre-tax income/(expense)	3,274	1,769	0	0	0
Profit before tax	10,619	7,753	6,508	6,859	5,692
Income tax expense	1,146	594	1,341	1,794	911
Minorities	103	69	122	94	278
Other post-tax income/(expense)	0	0	0	0	0
Net profit	9,370	7,090	5,045	4,972	4,504
DB adjustments (including dilution)	-4,070	-1,739	0	0	0
DB Net profit	5,299	5,351	5,045	4,972	4,504

Cash Flow (HKDm)

Cash flow from operations	7,818	8,743	2,792	1,853	1,421
Net Capex	-343	-222	-75	-61	-58
Free cash flow	7,475	8,521	2,717	1,792	1,364
Equity raised/(bought back)	-31	-47	0	0	0
Dividends paid	-2,121	-2,123	-3,205	-3,191	-3,283
Net inc/(dec) in borrowings	-2,073	-2,531	1,396	-1,571	-1,100
Other investing/financing cash flows	1,896	2,463	-99	2,050	2,049
Net cash flow	5,146	6,283	809	-920	-970
Change in working capital	3,402	5,534	-1,227	-1,178	-1,493

Balance Sheet (HKDm)

Cash and other liquid assets	19,698	27,442	28,251	27,331	26,361
Tangible fixed assets	60,244	61,398	61,494	61,577	61,651
Goodwill/intangible assets	0	0	0	0	0
Associates/investments	30,355	29,373	29,131	29,455	28,783
Other assets	31,506	30,846	31,929	31,658	31,193
Total assets	141,803	149,058	150,806	150,021	147,988
Interest bearing debt	8,706	6,809	7,319	5,882	4,750
Other liabilities	14,071	19,576	18,851	17,628	15,228
Total liabilities	22,777	26,384	26,169	23,510	19,978
Shareholders' equity	118,558	122,131	124,032	125,861	127,220
Minorities	468	543	604	651	790
Total shareholders' equity	119,026	122,674	124,636	126,511	128,010
Net debt	-10,992	-20,633	-20,932	-21,449	-21,611

Key Company Metrics

Sales growth (%)	nm	-50.5	35.3	-10.5	-14.8
DB EPS growth (%)	na	-0.9	-5.7	-1.5	-9.4
EBITDA Margin (%)	23.0	34.3	32.3	33.5	35.8
EBIT Margin (%)	23.0	34.3	32.3	33.5	35.8
Payout ratio (%)	32.3	44.0	62.3	63.2	69.8
ROE (%)	8.1	5.9	4.1	4.0	3.6
Capex/sales (%)	1.6	2.1	0.5	0.5	0.5
Capex/depreciation (x)	904.7	276.9	nm	nm	nm
Net debt/equity (%)	-9.2	-16.8	-16.8	-17.0	-16.9
Net interest cover (x)	nm	nm	nm	nm	nm

Source: Company data, Deutsche Bank estimates

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Investment thesis

Outlook

Sino-Land stands out among its peers with net cash since 2013; its net cash position stood at HK\$23bn as of 1HFY17, or about 16% of our estimated NAV. It has also benefited from the recent heating up of the primary residential sales market, where achieved ASPs are higher than our former expectations. However, we believe these positive catalysts are already reflected in the share price, following strong share price rally YTD. Maintain Hold.

Valuation

Our target price is based on the sum-of-the-part approach (previously target discount on overall NAV), implying a 2017 PE of 17x. We believe that applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio is appropriate in an ex-growth market. For China property development, we believe that applying 7x PE (at the upper range of 2019E PE for China developers and at par with industry leaders with strong financial position, such as COLI and CR Land) is appropriate by considering the financial strength and profitability profile of Hong Kong developers. This methodology is our new valuation metric adopted across HK developers under our coverage.

Risks

Macro risks: 1) External shock and interest rate hike: if the low interest rate environment persists for longer, current high property prices could be well supported for longer and vice versa; 2) Government tightening measures might be stricter than expected and adversely impact the property market; on the other hand, the property market could be boosted if the government decides to loosen on the current administrative tightening measures; 3) Unexpected economic fluctuations in the HK/Chinese economy may have positive/negative impact on housing demand.

Company-specific risks: 1) Track record in execution in China is not fully proven; however, if execution improves, we may see a re-rating; 2) HLD could face stronger-than-expected competition for land bank; however, if competition is less intensified as expected, it may be able to acquire land at more reasonable prices, leading to higher NAV growth.



Financial analysis

Revising earnings by -5% to 1% for FY17-19 by factoring in our latest ASP assumptions

As a result of worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with rising supply, which should lead the vacancy rate to more than double to 9% (from 3.8% now) and prices to slide 48% in 2017E-2026E (0% in 2017, -14% in 2018, -11% in 2019E, -3% in 2020E, -4% in 2021E, -5% in 2022E, -6% in 2023E, -6% in 2024E/25E and -7% in 2026E). Our previous ASP assumption was a 21% decline in 2017E-2019E (-11% in 2017E, -7% in 2018E and -5% in 2019E). We revise our earnings estimates by -4% to HK\$5,045mn for FY17, by 1% to HK\$4,972mn for FY18, and by -5% to HK\$4,504mn for FY19.

Figure 100: Summary of earnings revisions

	2017E			2018E			2019E		
	New	Old	%	New	Old	%	New	Old	%
Revenue	14,620	12,175	20%	13,091	10,892	20%	11,152	15,234	-27%
Operating profit	4,724	4,444	6%	4,383	3,605	22%	3,998	3,921	2%
Pre-tax profit	6,508	6,535	0%	6,859	5,960	15%	5,692	5,923	-4%
Core Profit	5,045	5,265	-4%	4,972	4,902	1%	4,504	4,720	-5%
EPS	0.82	0.85	-4%	0.81	0.80	1%	0.73	0.77	-5%
DPS	0.51	0.51	0%	0.51	0.51	0%	0.51	0.51	0%

Source: Deutsche Bank estimates



Figure 101: Income statement (HK\$ mn)

For Year Ended Jun 30	2014	2015	2016	2017E	2018E	2019E
Property Sales	2,741	16,957	5,760	9,396	7,888	6,025
Property Rentals	2,757	2,863	2,963	3,036	2,933	2,791
Investment in securities	106	60	64	64	64	64
Financing	2	1	3	3	3	3
Hotel	863	885	859	851	868	868
Building management and services	982	1,073	1,156	1,271	1,335	1,401
Total Revenue	7,451	21,839	10,804	14,620	13,091	11,152
Total Operating Profit	3,865	5,019	3,708	4,724	4,383	3,998
Finance Income	368	504	489	484	433	436
Finance Costs	(233)	(206)	(194)	(190)	(196)	(151)
Gross Interest Expenses	(253)	(239)	(217)	(211)	(217)	(167)
Interest Capitalized	20	33	22	21	22	17
Net Finance Income/(Costs)	135	298	295	294	237	286
Fair Value Gains	3,290	3,225	1,302	-	-	-
Others One-off items	1,396	50	467	-	-	-
Total Others	4,686	3,275	1,769	-	-	-
Associated Entities	1,638	2,030	1,981	1,490	2,240	1,409
Profit before Tax	10,324	10,621	7,753	6,508	6,859	5,692
Income Tax	(1,281)	(1,146)	(594)	(1,341)	(1,794)	(911)
Profit after Tax	9,043	9,475	7,159	5,167	5,066	4,781
Minorities	(122)	(103)	(69)	(12)	(94)	(278)
Net Profit	8,921	9,372	7,090	5,045	4,972	4,504
Core Net Profit	5,022	5,301	5,351	5,045	4,972	4,504
Core EPS (HK\$)	0.84	0.88	0.88	0.83	0.82	0.74
DPS	0.50	0.50	0.51	0.51	0.51	0.51

Source: Deutsche Bank estimates, company data



Figure 102: Balance sheet (HK\$ mn)

For Year Ended Jun 30	2014	2015	2016	2017E	2018E	2019E
Investment properties	56,281	58,409	59,256	59,507	59,589	59,663
Hotel property	1,891	1,696	1,987	1,987	1,987	1,987
Property plant and equipment	129	139	155	-	-	-
Long term loans receivable	50	228	718	718	718	718
Prepaid lease payments - non current	1,303	1,178	1,165	1,165	1,165	1,165
Interests in associates	17,476	15,598	16,200	13,393	12,373	12,021
Jointly controlled entity	2,242	3,101	3,200	3,200	3,200	3,200
Available for sale investments	1,009	906	734	734	734	734
Advances to associates	9,686	9,329	7,339	9,904	11,248	10,928
Advances to non-controlling interests	96	-	-	-	-	-
Advances to investee companies	18	16	16	16	16	16
Total Non-current assets	90,181	90,599	90,771	90,625	91,032	90,434
Properties under development	27,884	20,454	22,687	24,365	24,365	24,365
Stocks of unsold properties	1,618	7,166	4,386	2,707	2,707	2,707
Hotel inventories	19	17	19	19	19	19
Prepaid lease payments- current	20	21	20	20	20	20
Amounts due from associates	971	500	189	594	675	656
Amounts due from a JV	-	20	545	545	545	545
Accounts and other receivables	1,117	2,895	2,685	3,363	3,011	2,565
Trading securities	555	11	8	8	8	8
Restricted bank deposits	413	195	546	546	546	546
Cash and cash equivalents	13,999	19,503	26,896	27,705	26,785	25,815
Current portion of long term receivable	4	5	16	16	16	16
Taxation recoverable/ others	148	99	209	209	209	209
Assets classified as held for sale	-	317	-	-	-	-
Amount due from a minority interest	-	-	81	81	81	81
Total Current assets	46,747	51,204	58,287	60,181	58,989	57,554
Accounts and other payables	6,098	9,408	15,169	14,620	13,091	11,152
Amounts due to associates	3,836	1,177	1,133	594	675	656
Amounts due to minority interest	-	368	148	148	148	148
Taxation payable	1,044	1,089	1,199	1,562	1,789	1,347
Current portion of long term bank loans	29	-	-	-	-	-
Secured	92	801	-	1,571	1,100	950
Total current liabilities	11,098	12,843	17,650	18,496	16,802	14,252
Net current assets	35,649	38,361	40,638	41,864	42,187	43,303
Total assets less current liabilities	125,830	128,960	131,409	132,310	133,219	133,736
Long term bank borrowings	7,920	5,238	4,442	4,267	3,167	2,217
Deferred taxation	1,714	2,030	1,926	1,926	1,926	1,926
Advances from associates	1,652	1,686	1,876	990	1,125	1,093
Advances from minority shareholders	1,595	981	490	490	490	490
Total non-current liabilities	12,881	9,934	8,735	7,673	6,708	5,726
Net assets	112,949	119,026	122,674	124,636	126,511	128,010
Share capital	6,017	6,084	6,165	6,165	6,165	6,165
Share premiums	30,751	31,584	32,492	32,492	32,492	32,492
Retained earnings	72,197	80,890	83,474	85,375	87,204	88,563
Shareholders' equity	111,665	118,558	122,131	124,032	125,861	127,220
Minority interests	1,284	468	543	604	651	790
Total equity	112,949	119,026	122,674	124,636	126,511	128,010

Source: Deutsche Bank estimates, company data



Valuation

Our revised estimated NAV for Sino Land is HK\$22.1/share

Our estimated NAV is calculated via a sum-of-the parts valuation. For development properties, we apply a DCF to estimate the value of its projects by taking the estimated cash inflows from property sales minus outstanding costs, including any outstanding land costs, construction costs, and related income taxes and LAT for China projects. For investment properties, we use the income capitalization approach, taking the estimated rental revenues of the investment properties and dividing this figure by the estimated cap rates. Our estimated rents and cap rates vary across the different types of properties and their locations. When arriving at the NAV for the company, we take the aggregate estimated value for the above business segments and add the company's net debt position. We value the stakes of listed companies at the prevailing market price. By factoring in our latest ASP assumptions for Hong Kong residential prices (0% in 2017E, -14% in 2018E, -11% in 2019E, -3% in 2020E, -4% in 2021E, -5% in 2022E, -6% in 2023E, -6% in 2024E/25E, and -7% in 2026E), our revised estimated NAV is HK\$22.1/share.

Figure 103: NAV breakdown (end-FY17)

	HK\$m	HK\$/Share	% of NAV
Property Development			
Hong Kong Residential	19,700	3.20	14%
Hong Kong Office	1,468	0.24	1%
China Residential	3,996	0.65	3%
	25,164	4.08	19%
Property Investment			
Hong Kong Residential	4,375	0.71	3%
Hong Kong Retail	41,642	6.75	34%
Hong Kong Office	21,192	3.44	16%
Hong Kong Car Parks	2,612	0.42	2%
Hong Kong Industrial	6,939	1.13	5%
Hong Kong Hotel	2,067	0.34	2%
China Retail	3,652	0.59	3%
China Car Parks	4	0.00	0%
China Office	1,197	0.19	1%
China Hotel	637	0.10	0%
Singapore Retail	1,898	0.31	1%
Singapore Hotel	10,013	1.62	7%
Australia Hotel	976	0.16	1%
	97,204	15.77	71%
Other Assets			
Total Other Assets	917	0.15	1%
Gross Asset Value	123,285	20.00	91%
Net Cash/(Debt)	21,378	3.47	16%
Other adjustment	(8,688)	(1.41)	(6%)
Fully Diluted NAV	135,975	22.1	100%

Source: Deutsche Bank estimates



Target price of HK\$14.3 is based upon sum-of-the-parts

We believe the conventional valuation methodology of applying an overall target discount on the accessed NAV becomes less relevant in valuing developers as market fundamentals have changed, and the historical average may not necessarily serve as a good reference. By taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is SOTP, where we adopt PE for the property development business and the income capitalization approach for investment properties.

In deriving the target price, we prefer the sum-of-the-part approach to the previous methodology of applying a target discount to the overall Net Asset Value estimate. Specifically, we believe that applying 6x PE to Hong Kong property development is appropriate in an ex-growth market. Meanwhile, for investment properties, we believe that applying a 34% target discount to our estimated value on the respective investment property portfolio is appropriate, as the average discount for landlords has been relatively stable at 34% in the past 25 years. For China property development, we believe that applying 7x PE (at the upper range of 2019E PE for China developers and at par with industry leaders with strong financial position, such as COLI and CR Land) is appropriate by considering the financial strength and profitability profile of Hong Kong developers. On adopting the new valuation metric, we derive our target price for Sino Land at HK\$14.3.

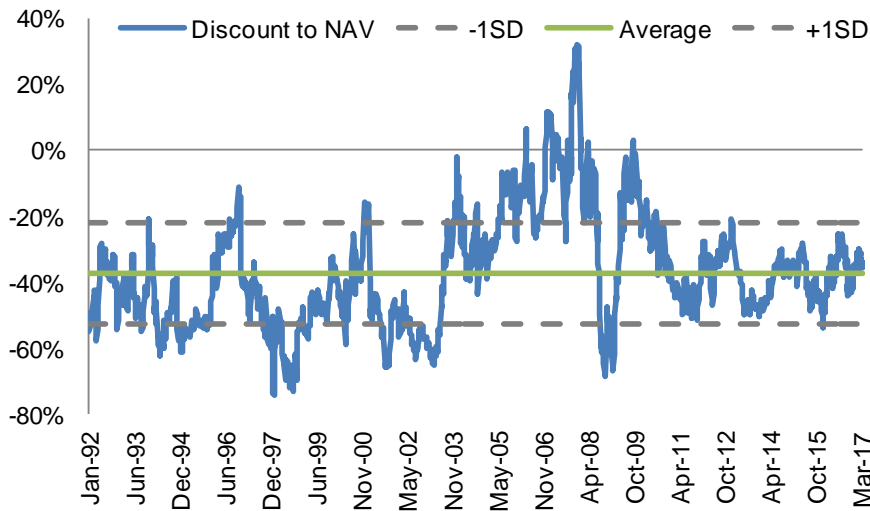
Figure 104: Sino Land target price breakdown

Category	HK\$ per share
Development properties – Hong Kong	1.64
Development properties – China	0
Investment properties	10.41
Other assets	0.15
Net cash / (debt) & other adjustments	2.06
Target price	14.3

Source: Deutsche Bank estimates

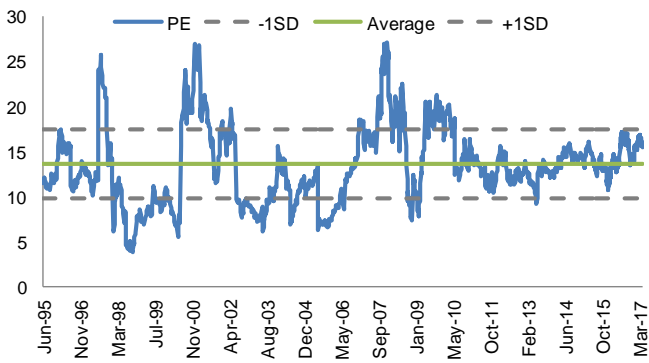


Figure 105: Sino Land – Discount to NAV



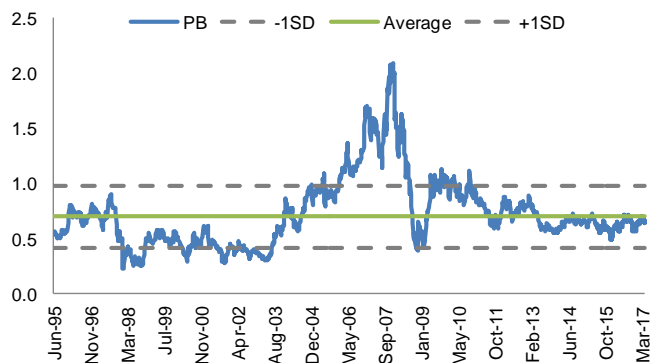
Source: Deutsche Bank estimates; Bloomberg Finance LP

Figure 106: Sino Land – PE



Source: Deutsche Bank estimates; Bloomberg Finance LP

Figure 107: Sino Land – PB



Source: Deutsche Bank estimates; Bloomberg Finance LP



Risks

Macro risks

- 1) External shock and interest rate hike: if the low interest rate environment persists for longer, current high property prices could be well supported for longer and vice versa;
- 2) Government tightening measures might be stricter than expected and adversely impact the property market; on the other hand, the property market could be boosted if the government decides to loosen on the current administrative tightening measures;
- 3) Unexpected economic fluctuations in the HK/Chinese economy may have positive/negative impact on housing demand.

Company-specific risks

- 1) Track record in execution in China is not fully proven; however, if execution improves, we may see a re-rating;
- 2) HLD could face stronger-than-expected competition for land bank; however, if competition is less intensified than expected, it may be able to acquire land at more reasonable prices, leading to higher NAV growth.



Rating
Hold

Asia
Hong Kong

Property

Company
New World Dev

Reuters
0017.HK

Bloomberg
17 HK

Price at 6 Jun 2017 (HKD)	10.78
Price target - 12mth (HKD)	11.10
52-week range (HKD)	10.78 - 7.19
HANG SENG INDEX	25,997

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Near-term catalysts priced-in following recent rally; D/G to Hold

Downgrading to Hold on valuation following strong rally in the past two weeks

While we view the upcoming completion of Victoria Dockside (formerly known as New World Centre redevelopment) a key near-term catalyst for NWD, where rental revenue is expected to mostly double from the current level, and its ability to raise dividend payout will improve correspondingly, we believe such catalyst has already priced-in following the strong 12% rally in the past two weeks (Vs. Hang Seng up 2%). Consequently, we downgrade NWD to Hold (from Buy) with a TP of HK\$11.1 based upon a new valuation methodology, which we believe is more appropriate in an ex-growth market on an aging population in Hong Kong.

New valuation approach – PE preferred to value property development

We believe the conventional valuation methodology of applying an overall target discount on the accessed NAV becomes less relevant in valuing developers as market fundamentals have changed and that historical average may not necessarily serve as a good reference. By taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is SOTP, where we adopt PE for the property development business and the income capitalization approach for investment properties.

FY17-19E earnings revised by -2-9% factoring in our latest ASP assumptions

As a result of worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with rising supply, which should push the vacancy rate to more than double to 9% (from 3.8% now) and prices to slide 48% in 2017-26 (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026). Consequently, we revise our earnings estimates by -2% to 9% in FY17-19E, and NAV upwards by 8.7%.

Target price of HK\$11.1 is based on the sum-of-the-parts approach

Our target price is based on the sum-of-the-parts approach (previously target discount on overall NAV), which implies a 2017 PE of 14x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio are appropriate in an ex-growth market. This is the new valuation metric adopted for all HK developers under our coverage. Risks: government policy, sales momentum and interest rate trend (Details on page 87).

Key changes

Rating	Buy to Hold	↓	
Sales (FYE)	61,263 to 60,863	↓	-0.7%
Op prof margin (FYE)	12.6 to 16.0	↑	27.4%
Net profit (FYE)	7,283.8 to 7,864.6	↑	8.0%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	14.1	7.9	43.9
HANG SENG INDEX	6.2	10.2	23.6

Source: Deutsche Bank

Forecasts And Ratios

Year End Jun 30	2015A	2016A	2017E	2018E	2019E
Sales (HKDm)	55,245.0	59,570.0	60,863.4	60,981.1	61,812.7
EBITDA (HKDm)	10,801.5	8,898.4	9,732.6	9,534.2	8,741.8
Reported NPAT (HKDm)	19,112.0	8,666.3	7,864.6	6,943.4	6,174.5
DB EPS FD (HKD)	0.77	0.75	0.78	0.76	0.68
PER (x)	12.4	10.2	13.8	14.2	15.9
EV/EBITDA (x)	10.8	11.4	11.6	10.8	11.8
DPS (net) (HKD)	0.42	0.44	0.44	0.44	0.44
Yield (net) (%)	4.4	5.7	4.1	4.1	4.1

Source: Deutsche Bank estimates, company data



Model updated:06 June 2017

Running the numbers

Asia

Hong Kong

Property

New World Dev

Reuters: 0017.HK

Bloomberg: 17 HK

Hold

Price (6 Jun 17) HKD 10.78

Target Price HKD 11.10

52 Week range HKD 7.19 - 10.78

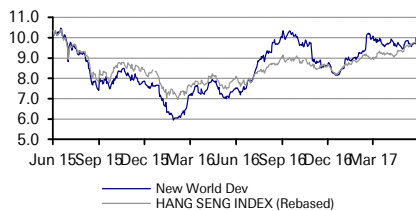
Market Cap (m) HKDm 96,987

USDm 12,443

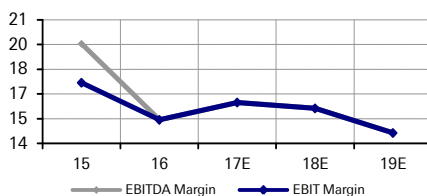
Company Profile

New World Development Company Limited, through its subsidiaries, develops and invests in property, operates hotels and restaurants, and provides construction and engineering services. The company also operates infrastructure businesses and provides telecommunications services.

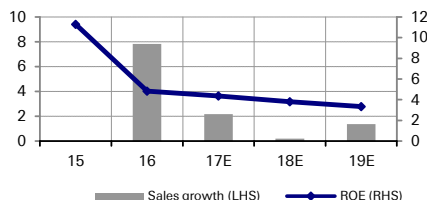
Price Performance



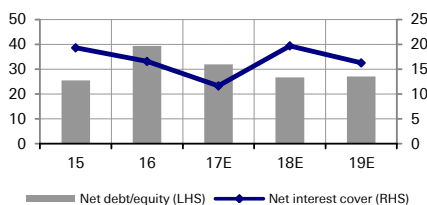
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 30-Jun

Financial Summary

	2015	2016	2017E	2018E	2019E
DB EPS (HKD)	0.77	0.75	0.78	0.76	0.68
Reported EPS (HKD)	2.17	0.95	0.86	0.76	0.68
DPS (HKD)	0.42	0.44	0.44	0.44	0.44
BVPS (HKD)	19.9	19.1	20.1	20.4	20.7
Weighted average shares (m)	8,790	9,146	8,997	8,997	8,997
Average market cap (HKDm)	83,748	70,611	96,987	96,987	96,987
Enterprise value (HKDm)	116,640	101,521	112,910	102,663	103,397

Valuation Metrics

	2015	2016	2017E	2018E	2019E
P/E (DB) (x)	12.4	10.2	13.8	14.2	15.9
P/E (Reported) (x)	4.4	8.1	12.5	14.2	15.9
P/BV (x)	0.51	0.41	0.54	0.53	0.52
FCF Yield (%)	nm	31.4	28.1	18.3	6.8
Dividend Yield (%)	4.4	5.7	4.1	4.1	4.1
EV/Sales (x)	2.1	1.7	1.9	1.7	1.7
EV/EBITDA (x)	10.8	11.4	11.6	10.8	11.8
EV/EBIT (x)	12.3	11.4	11.6	10.8	11.8

Income Statement (HKDm)

	2015	2016	2017E	2018E	2019E
Sales revenue	55,245	59,570	60,863	60,981	61,813
Gross profit	20,610	18,522	19,166	18,864	18,385
EBITDA	10,802	8,898	9,733	9,534	8,742
Depreciation	1,304	0	0	0	0
Amortisation	0	0	0	0	0
EBIT	9,497	8,898	9,733	9,534	8,742
Net interest income/(expense)	-492	-537	-836	-484	-537
Associates/affiliates	3,657	2,661	4,319	3,689	3,473
Exceptionals/extraordinaries	18,474	7,685	893	0	0
Other pre-tax income/(expense)	0	0	0	0	0
Profit before tax	31,137	18,707	14,109	12,739	11,678
Income tax expense	4,264	6,424	4,067	3,688	3,831
Minorities	7,760	3,617	2,177	2,108	1,673
Other post-tax income/(expense)	0	0	0	0	0
Net profit	19,112	8,666	7,865	6,943	6,175
DB adjustments (including dilution)	-12,342	-1,774	-759	0	0
DB Net profit	6,770	6,893	7,106	6,943	6,175

Cash Flow (HKDm)

	2015	2016	2017E	2018E	2019E
Cash flow from operations	4,977	22,163	32,410	18,371	7,217
Net Capex	-8,190	0	-5,196	-651	-666
Free cash flow	-3,212	22,163	27,214	17,720	6,550
Equity raised/(bought back)	148	0	0	0	0
Dividends paid	-5,427	-4,117	0	0	0
Net inc/(dec) in borrowings	-3,418	17,528	18,510	-1,195	-411
Other investing/financing cash flows	9,535	-39,961	-35,420	-7,566	-7,919
Net cash flow	-2,374	-4,387	10,304	8,959	-1,779
Change in working capital	1,849	0	29,507	10,699	959

Balance Sheet (HKDm)

	2015	2016	2017E	2018E	2019E
Cash and other liquid assets	59,352	54,965	69,655	80,229	77,979
Tangible fixed assets	20,484	23,873	23,873	23,873	23,873
Goodwill/intangible assets	0	0	0	0	0
Associates/investments	67,184	69,410	72,865	75,817	78,595
Other assets	250,912	242,061	229,190	230,254	238,069
Total assets	397,931	390,309	395,584	410,172	418,515
Interest bearing debt	115,988	133,963	134,945	136,114	135,703
Other liabilities	59,585	57,250	58,348	66,674	71,539
Total liabilities	175,573	191,213	193,293	202,788	207,243
Shareholders' equity	178,919	179,573	180,591	183,576	185,792
Minorities	43,439	21,322	23,499	25,608	27,280
Total shareholders' equity	222,358	200,895	204,090	209,183	213,072
Net debt	56,636	78,998	65,290	55,885	57,725

Key Company Metrics

	2015	2016	2017E	2018E	2019E
Sales growth (%)	nm	7.8	2.2	0.2	1.4
DB EPS growth (%)	na	-2.2	3.6	-2.4	-11.2
EBITDA Margin (%)	19.6	14.9	16.0	15.6	14.1
EBIT Margin (%)	17.2	14.9	16.0	15.6	14.1
Payout ratio (%)	19.3	46.4	50.3	57.0	64.1
ROE (%)	11.3	4.8	4.4	3.8	3.3
Capex/sales (%)	16.6	0.0	8.5	1.1	1.1
Capex/depreciation (x)	7.0	nm	nm	nm	nm
Net debt/equity (%)	25.5	39.3	32.0	26.7	27.1
Net interest cover (x)	19.3	16.6	11.6	19.7	16.3

Source: Company data, Deutsche Bank estimates

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Investment Thesis

Outlook

We have a Hold rating on New World Development. While we view the upcoming completion of Victoria Dockside (formerly known as New World Centre redevelopment) a key near-term catalyst for NWD, where rental revenue is expected to mostly double from the current level, and its ability to raise dividend payout will improve correspondingly, we believe such catalyst has already priced-in following the strong rally recently.

Valuation

Our target price is based on the sum-of-the-parts approach (previously target discount on overall NAV), which imply a 2017 PE of 14x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio are appropriate in an ex-growth market. For China property development, we believe applying 7x PE (at the upper range of 2019E PE for China developers and at par with industry leaders with strong financial positions such as COLI and CR Land) is appropriate considering the financial strength and profitability profile of Hong Kong developers. This is the new valuation metric adopted for all HK developers under our coverage.

Risks

- 1) A softening/stronger outlook in the Hong Kong economy, which could lead to lower/stronger housing demand.
- 2) A low interest rate environment and ample liquidity flow could reverse, damaging sentiment and demand in the property market. However, if the low interest rate environment persists for longer, current high property prices may well be supported.
- 3) A further slowdown in the Chinese economy could result in a downside to our current forecasts. However, if we see stronger than expected economic growth, there could be upside to our current forecasts.
- 4) NWD could face severe competition for landbank, which would adversely affect the growth prospects of the company. However, if competition is less intensified, NWD could be able to acquire land at more reasonable costs, leading to stronger NAV growth.



Financial Analysis

FY17-19E earnings revised by -2-9% factoring in our latest ASP assumptions

As a result of worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with rising supply, which should push the vacancy rate to more than double to 9% (from 3.8% now) and prices to slide 48% in 2017-2026 (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026). Earlier, we had assumed a 21% dip in ASP in 2017-19 (-11% in 2017, -7% in 2018 and -5% in 2019). Consequently, we revise our earnings estimates by -2-9% in FY17-19. Specifically, we have revised our earnings estimates by 9% to HK\$7,106m for FY17E, -2% to HK\$6,943m for FY18E and -2% to HK\$6,175m for FY19E.

Figure 108: Summary of earnings revisions

	2017E			2018E			2019E		
	New	Old	%	New	Old	%	New	Old	%
Revenue	60,863	61,263	-1%	60,981	61,757	-1%	61,813	48,817	27%
Gross profit	19,166	17,185	12%	18,864	19,946	-5%	18,385	15,440	19%
Profit before tax	14,109	12,496	13%	12,739	13,408	-5%	11,678	10,454	12%
Core profit	7,106	6,525	9%	6,943	7,104	-2%	6,175	6,293	-2%
EPS	0.78	0.72	9%	0.76	0.78	-2%	0.68	0.69	-2%
DPS	0.44	0.44	0%	0.44	0.44	0%	0.44	0.44	0%

Source: Deutsche Bank estimates



Figure 109: Income Statement (HK\$m)

For year ended Dec 31	2014A	2015A	2016A	2017F	2018F	2019F
Property sales	29,329	25,682	28,528	26,760	23,351	20,252
Property rental	2,348	2,402	2,492	2,794	4,872	5,572
Hotel operation	3,751	4,061	1,762	2,096	2,298	2,537
Service	13,787	15,844	19,904	21,894	24,083	26,010
Infrastructure operations	2,346	2,471	2,444	2,724	2,860	3,003
Department store operations	3,975	3,913	3,550	3,758	3,720	3,683
Other businesses	964	873	890	838	796	756
Revenue	56,501	55,245.0	59,570.0	60,863	61,981	61,813
Cost of sales	(34,948)	(35,939)	(41,048)	(41,697)	(42,117)	(43,428)
Gross Profit	21,554	19,306	18,522	19,166	18,864	18,385
Gross interest expenses	5,029	5,236	5,745	6,073	6,125	6,107
Capitalized interest	(3,102)	(3,614)	(3,810)	(3,947)	(3,981)	(3,664)
Net interest expense/(income)	1,927	1,622	1,936	2,125	2,144	2,443
Interest income	1,084	1,130	1,399	1,290	1,660	1,906
Selling and marketing costs	(1,675)	(1,958)	(1,769)	(1,522)	(1,525)	(1,699)
Administrative expenses	(7,041)	(7,851)	(7,855)	(7,912)	(7,806)	(7,974)
SG&A	(7,633)	(8,679)	(8,225)	(8,144)	(7,670)	(7,737)
Revaluation gains	1,426	3,166	307	-	-	-
Other adjustments	2,560	15,308	7,378	893	-	-
Profit from operations	15,980	27,479	16,047	9,789	9,051	8,205
Associates	3,097	3,657	2,661	4,319	3,689	3,473
Pre-tax profit	19,076	31,137	18,707	14,109	12,739	11,678
Taxation	(5,738)	(4,264)	(6,424)	(4,067)	(3,688)	(3,831)
Post-tax profit before MI	13,338	26,872	12,283	10,042	9,052	7,847
Minority interests	(3,612)	(7,760)	(3,617)	(2,177)	(2,108)	(1,673)
Net attributable profit	9,725	19,112	8,666	7,865	6,943	6,175
Adjustment for non-recurring items	(3,219)	(12,342)	(1,774)	893	-	-
Core net profit	6,507	6,770	6,893	7,106	6,943	6,175
Fully diluted Core EPS (HK\$)	0.92	0.77	0.75	0.78	0.76	0.68
DPS (HK\$)	0.42	0.42	0.44	0.44	0.44	0.44

Source: Deutsche Bank estimates



Figure 110: Balance Sheet (HK\$m)

As of Dec 31	2014A	2015A	2016A	2017F	2018F	2019F
Non-current assets	146,524	162,049	153,639	154,537	154,926	156,433
Investment properties	77,385	91,625	86,597	91,793	92,444	93,110
Land use rights	27,617	28,948	20,489	20,489	20,489	20,489
Property and equipment	18,291	20,484	23,873	23,873	23,873	23,873
Other assets	23,231	20,992	22,680	18,383	18,121	18,961
Associates	62,742	67,184	69,410	72,865	75,817	78,595
Other investments	4,770	6,951	10,122	10,122	10,122	10,122
Current assets	155,191	161,748	158,938	159,859	171,107	175,165
Properties for sale	48,713	51,578	50,755	49,021	49,032	49,076
Inventories	20,267	26,376	21,163	17,361	17,055	17,288
Other inventories	561	708	666	613	640	669
Debtors & deposits/receivables/others	23,924	23,735	29,589	21,408	23,321	29,899
Available for sale financial assets	-	-	1,800	1,800	1,800	1,800
Bank balances & cash	61,726	59,352	54,965	69,655	80,229	77,979
Current liabilities	(70,071)	(81,003)	(66,523)	(63,602)	(72,640)	(75,997)
Bank loans and overdrafts	6,970	2,396	1,513	1,211	968	775
Other loans due within one year	25,380	31,122	18,577	14,861	15,815	14,500
Forward sales deposits received	6,128	12,604	12,604	15,843	22,523	26,166
Creditors, deposits & accruals/others	25,172	28,930	25,671	29,214	27,878	28,313
Taxation	6,422	5,952	7,973	1,261	1,753	1,652
Derivative financial instruments	-	-	186	-	-	-
Proposed dividend	-	-	-	1,211	3,167	3,167
Total assets less current liabilities	299,157	316,928	325,586	333,781	339,332	344,318
Non-current liabilities	89,869	85,282	116,238	121,238	121,695	122,793
Long term bank loans	54,028	48,095	-	5,000	5,457	6,555
Other long term loans	32,074	34,374	114,842	114,842	114,842	114,842
Amounts due to/(from) group companies	2,128	1,169	-	-	-	-
Others	1,639	1,643	1,395	1,395	1,395	1,395
Deferred income tax	9,012	9,288	8,453	8,453	8,453	8,453
Issued share capital	63,761	66,712	69,600	66,712	66,712	66,712
Retained profits	80,147	98,428	96,194	100,100	103,085	105,301
Revaluation surplus	3,436	3,726	3,726	3,726	3,726	3,726
Capital & other reserves	12,464	10,054	10,054	10,054	10,054	10,054
Shareholders' funds	159,808	178,919	179,573	180,591	183,576	185,792
Minority interests	40,468	43,439	21,322	23,499	25,608	27,280
Total capital employed	299,157	316,928	325,586	333,781	339,332	344,318

Source: Deutsche Bank estimates



Valuation

Our revised estimated NAV is HK\$20 per share

Our estimated NAV is calculated via a sum-of-the-parts valuation. For development properties, we apply a DCF to estimate the value of its projects by taking the estimated cash inflow from property sales minus outstanding costs, including any outstanding land costs, construction costs, and related income taxes and LAT for China projects. For investment properties, we use the income capitalization approach, taking the estimated rental revenues of the investment properties and dividing this figure by the estimated cap rates. Our estimated rents and cap rates vary across the different types of properties and their locations. When arriving at the NAV for the company, we take the aggregate estimated value for the above business segments and add the company's net debt position. We value the stakes of listed companies at the prevailing market price. By factoring in our latest ASP assumption on Hong Kong residential prices (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026), our revised estimated NAV is HK\$20/share.

Figure 111: NAV breakdown (end-FY17)

	(HK\$ m)	(HK\$/share)	%
Development properties			
Hong Kong	14,313	1.6	8.0%
Beijing	12,131	1.3	6.7%
Langfang	232	0.0	0.1%
Shenyang	5,493	0.6	3.1%
Anshan	675	0.1	0.4%
Wuhan	4,182	0.5	2.3%
Changsha	344	0.0	0.2%
Yiyang	207	0.0	0.1%
Guangzhou	15,021	1.7	8.4%
Huiyang	739	0.1	0.4%
Ningbo	1,450	0.2	0.8%
	54,788	6.1	30.5%
Investment properties			
<u>Hong Kong</u>			
Residential	2,007	0.2	1.1%
Retail	58,207	6.5	32.4%
Office	20,222	2.2	11.2%
Serviced Apartment	33,384	3.7	18.6%
Carpark	3,362	0.4	1.9%
Hotel	9,167	1.0	5.1%
Others	12,992	1.4	7.2%
<u>China</u>			
Residential	796	0.1	0.4%
Retail	10,967	1.2	6.1%
Office	2,307	0.3	1.3%
Serviced Apartment	821	0.1	0.5%

Source: Deutsche Bank estimates



Figure 111: NAV breakdown (end-FY17) (Cont'd)

	(HK\$ m)	(HK\$/share)	%
Carpark	1,573	0.2	0.9%
Hotels	14,691	1.6	8.2%
Overseas Hotels	5,507.2	0.6	3.1%
	176,002	19.6	97.9%
Other assets			
NWS (659.HK)	33,367	3.7	18.6%
NWDS (825.HK)	1,481	0.2	0.8%
Farm land	5,130	0.6	2.9%
	39,978	4.4	22.2%
Gross asset value (GAV)	270,768	30.1	150.6%
Net cash / (debt)	(72,030)	(8.0)	-40.1%
Other adjustments	(16,502)	(1.8)	-9.2%
Net asset value (NAV) - fully diluted	182,237	20.0	100.0%

Source: Deutsche Bank estimates

Target price of HK\$11.1 is based on sum-of-the-parts valuation

We believe the conventional valuation methodology of applying an overall target discount on the accessed NAV becomes less relevant in valuing developers as market fundamentals have changed and that historical average may not necessarily serve as a good reference. By taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is sum-of-the-parts (SOTP), where we adopt PE for the property development business and the income capitalization approach for investment properties.

In deriving the target price, we prefer the sum-of-the-parts approach to the previous methodology of applying a target discount to the overall net asset value estimate. Specifically, we believe applying a 5x PE to Hong Kong property development is appropriate in an ex-growth market. Meanwhile, for investment properties, we believe applying a 34% target discount to our estimated value on the respective investment property portfolio is appropriate as the average discount for landlords has been relatively stable at 34% in the past 25 years. For China property development, we believe applying a 7x PE (at the upper range of 2019E PE for China developers and at par with industry leaders with strong financial positions such as COLI and CR Land) is appropriate by considering the financial strength and profitability profile of Hong Kong developers. On adopting the new valuation metric, we derive our target price for NWD at HK\$11.1.

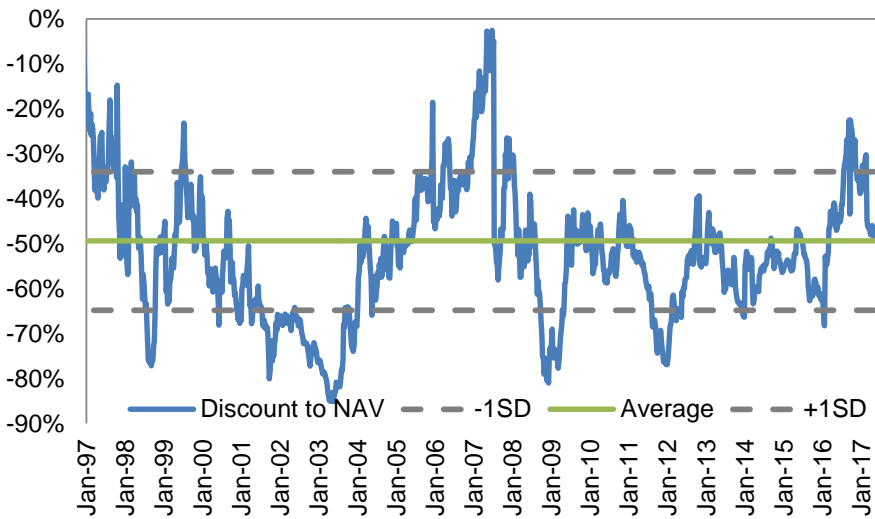
Figure 112: NWD target price breakdown

Category	HK\$ per share
Development properties – Hong Kong	1.13
Development properties – China	2.50
Investment properties	12.74
Other assets	4.39
Net cash / (debt)	(7.90)
Other adjustments	(1.76)
Target price	11.1

Source: Deutsche Bank estimates

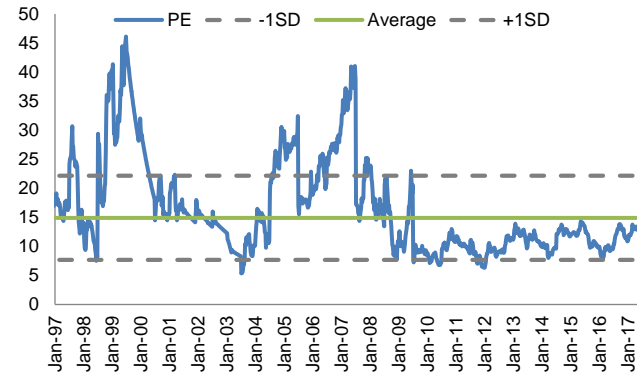


Figure 113: NWD – Discount to NAV



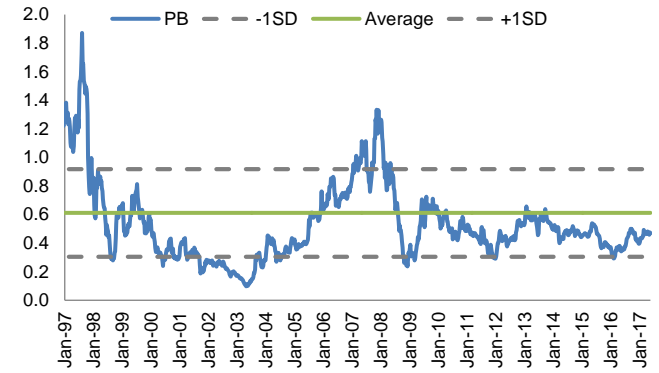
Source: Bloomberg Finance LP, Deutsche Bank estimates

Figure 114: NWD – PE chart



Source: Bloomberg Finance LP, Deutsche Bank estimates

Figure 115: NWD – PB chart



Source: Bloomberg Finance LP, Deutsche Bank estimates



Risks

Macro risks

- A softening/stronger outlook in the Hong Kong economy, which could lead to lower/stronger housing demand.
- A low interest rate environment and ample liquidity flow could reverse, damaging sentiment and demand in the property market. However, if the low interest rate environment persists for longer, current high property prices may well be supported.
- Further slowdown in the Chinese economy could result in a downside to our current forecasts. However, if we see stronger than expected economic growth, there could be upside to our current forecasts.

Company-specific risk

- NWD could face severe competition for landbank, which would adversely affect the growth prospects of the company. However, if competition is less intensified, NWD could be able to acquire land at more reasonable costs, leading to stronger NAV growth.

We expect the upcoming completion of the Victoria Dockside project will significantly boost rental income and hence the ability to raise dividend. Unexpected delays in completion/leasing may affect our current earnings projection. However, if rental performance comes in stronger-than-expected, there could be further upside on our current estimates.



Rating
Hold

Asia
Hong Kong

Property

Company
Kerry Prop

Reuters: 0683.HK
Bloomberg: 683 HK

Price at 6 Jun 2017 (HKD)	27.40
Price target - 12mth (HKD)	29.00
52-week range (HKD)	30.00 - 18.46
HANG SENG INDEX	25,997

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Scope for further dividend hike priced-in after YTD rally; downgrade to Hold

Downgrading to Hold as scope for further dividend hike priced-in; TP HK\$29

We downgrade Kerry Properties to Hold with a revised target price of HK\$29 (HK\$29.2) using a new valuation methodology, which we believe is more appropriate in an ex-growth market on an aging population in Hong Kong. While we prefer defensive names with secure dividend/scope for further dividend hikes where Kerry has the highest dividend coverage ratios by recurring income among peers at 179% (net profit from investment property portfolio covers its dividend), we believe this is already well reflected in the current share price, after a 29% share price rally YTD (vs the sector was up by 22% and Hang Seng Index up by 18% over the period).

New valuation approach – PE preferred to value property development

We believe the conventional valuation methodology of applying an overall target discount on the accessed NAV is less relevant in valuing developers as market fundamentals have changed and that historical average may not necessarily be a good reference. By taking into account that HK developers are likely to diversify their business away from property sales in an ex-growth market, we believe the most appropriate valuation metric is SOTP, where we adopt PE for the property development business and the income capitalization approach for investment properties.

FY17-19E earnings revised -1-10% considering our latest ASP assumptions

Due to worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with a rising supply, which will inevitably push the vacancy rate by more than double to 9% (from 3.8% now) and prices to slide 48% in 2017-26 (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25, and -7% in 2026). Consequently, we revise our earnings estimates by -1% to 10% in FY17-19E, and increase the NAV by 15.1%.

Target price of HK\$29 is based on the sum-of-the parts approach

Our target price is based on the sum-of-the-parts approach (previously target discount on overall NAV), which implies a 2017 PE of 9x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio are appropriate in an ex-growth market (see page 95). This is the new valuation metric adopted for all HK developers under our coverage. Risks: government policy, sales momentum and interest rate trend (see page 97).

Forecasts And Ratios

Year End Dec 31	2015A	2016A	2017E	2018E	2019E
Sales (HKDm)	10,392.9	12,990.5	27,083.0	25,770.0	28,016.8
EBITDA (HKDm)	2,942.6	4,688.3	5,721.6	4,154.3	5,703.6
Reported NPAT (HKDm)	5,530.0	6,537.3	4,914.0	3,634.6	4,993.5
DB EPS FD (HKD)	2.41	2.54	3.41	2.52	3.46
PER (x)	10.9	8.3	8.0	10.9	7.9
DPS (net) (HKD)	0.90	1.10	1.15	1.17	1.20
Yield (net) (%)	3.4	5.2	4.2	4.3	4.4

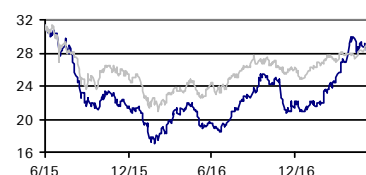
Source: Deutsche Bank estimates, company data

Key changes

Rating	Buy to Hold	↓	
Price target	29.20 to 29.00	↓	-0.7%
Sales (FYE)	26,599 to 27,083	↑	1.8%
Op prof margin (FYE)	19.8 to 21.1	↑	6.7%
Net profit (FYE)	4,533.3 to 4,914.0	↑	8.4%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	-4.5	11.8	40.7
HANG SENG INDEX	6.2	10.2	23.6

Source: Deutsche Bank



Model updated: 23 May 2017

Running the numbers

Asia

Hong Kong

Property

Kerry Prop

Reuters: 0683.HK

Bloomberg: 683 HK

Hold

Price (6 Jun 17) HKD 27.40

Target Price HKD 29.00

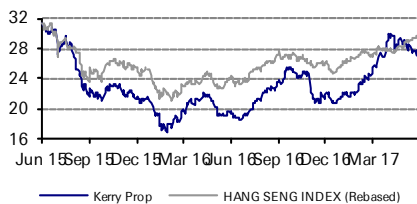
52 Week range HKD 18.46 - 30.00

Market Cap (m) HKDm 39,542
USDm 5,073

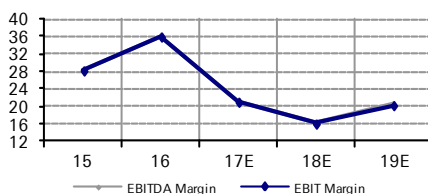
Company Profile

Kerry Properties Limited, through its subsidiaries, invests in and develops real estate. The company also owns and operates logistics, freight and warehouses businesses. In addition, Kerry Properties invests in infrastructure-related projects, and operates hotels.

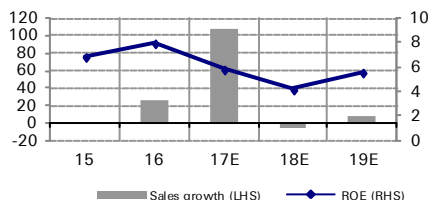
Price Performance



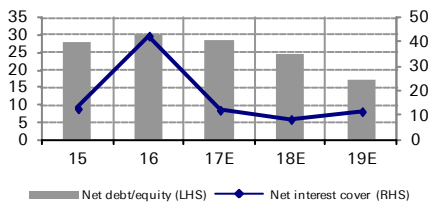
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 31-Dec

2015 2016 2017E 2018E 2019E

Financial Summary

DB EPS (HKD)	2.41	2.54	3.41	2.52	3.46
Reported EPS (HKD)	3.83	4.53	3.41	2.52	3.46
DPS (HKD)	0.90	1.10	1.15	1.17	1.20
BVPS (HKD)	56.3	57.3	59.6	61.0	63.2
Weighted average shares (m)	1,446	1,443	1,443	1,443	1,443
Average market cap (HKDm)	37,936	30,389	39,542	39,542	39,542
Enterprise value (HKDm)	56,918	53,064	61,020	56,810	49,217

Valuation Metrics

P/E (DB) (x)	10.9	8.3	8.0	10.9	7.9
P/E (Reported) (x)	6.9	4.6	8.0	10.9	7.9
P/BV (x)	0.38	0.37	0.46	0.45	0.43
FCF Yield (%)	nm	nm	4.0	11.5	16.2
Dividend Yield (%)	3.4	5.2	4.2	4.3	4.4
EV/Sales (x)	5.5	4.1	2.3	2.2	1.8
EV/EBITDA (x)	19.3	11.3	10.7	13.7	8.6
EV/EBIT (x)	19.4	11.3	10.7	13.7	8.6

Income Statement (HKDm)

Sales revenue	10,393	12,991	27,083	25,770	28,017
Gross profit	3,915	5,859	8,443	6,758	8,539
EBITDA	2,943	4,688	5,722	4,154	5,704
Depreciation	4	3	12	12	13
Amortisation	0	0	0	0	0
EBIT	2,939	4,686	5,710	4,142	5,691
Net interest income/(expense)	-227	-110	-462	-483	-483
Associates/affiliates	2,018	1,801	1,958	2,101	2,153
Exceptionals/extraordinary	2,531	3,953	0	0	0
Other pre-tax income/(expense)	0	0	0	0	0
Profit before tax	7,260	10,330	7,206	5,760	7,361
Income tax expense	1,190	2,595	1,189	950	1,215
Minorities	541	1,198	1,103	1,175	1,153
Other post-tax income/(expense)	0	0	0	0	0
Net profit	5,530	6,537	4,914	3,635	4,993
DB adjustments (including dilution)	-2,049	-2,866	0	0	0
DB Net profit	3,481	3,671	4,914	3,635	4,993

Cash Flow (HKDm)

Cash flow from operations	1,212	-875	3,552	4,857	6,815
Net Capex	-2,000	-1,844	-1,982	-303	-404
Free cash flow	-788	-2,719	1,569	4,554	6,410
Equity raised/(bought back)	0	0	0	0	0
Dividends paid	-1,301	-1,587	-1,660	-1,688	-1,732
Net inc/(dec) in borrowings	-12,642	-9,699	4,151	1,209	0
Other investing/financing cash flows	14,647	-12,069	-5,759	4,558	4,567
Net cash flow	-83	-26,075	-1,698	8,632	9,245
Change in working capital	2,632	-1,901	680	3,363	5,533

Balance Sheet (HKDm)

Cash and other liquid assets	10,865	16,481	15,228	19,844	26,563
Tangible fixed assets	5,405	5,758	5,758	5,758	5,758
Goodwill/intangible assets	0	0	0	0	0
Associates/investments	20,008	18,651	20,494	22,473	24,500
Other assets	114,940	131,755	134,347	128,434	122,865
Total assets	151,217	172,646	175,828	176,508	179,686
Interest bearing debt	37,046	45,333	43,623	44,832	44,832
Other liabilities	20,009	32,094	32,609	28,958	27,722
Total liabilities	57,055	77,427	76,232	73,791	72,554
Shareholders' equity	81,353	82,744	86,019	87,965	91,227
Minorities	12,809	12,474	13,577	14,752	15,905
Total shareholders' equity	94,162	95,218	99,596	102,718	107,132
Net debt	26,181	28,852	28,395	24,989	18,270

Key Company Metrics

Sales growth (%)	nm	25.0	108.5	-4.8	8.7
DB EPS growth (%)	na	5.6	33.9	-26.0	37.4
EBITDA Margin (%)	28.3	36.1	21.1	16.1	20.4
EBIT Margin (%)	28.3	36.1	21.1	16.1	20.3
Payout ratio (%)	23.5	24.3	33.8	46.5	34.7
ROE (%)	6.9	8.0	5.8	4.2	5.6
Capex/sales (%)	19.2	14.2	7.3	1.2	1.4
Capex/depreciation (x)	494.2	702.8	170.1	24.8	31.4
Net debt/equity (%)	27.8	30.3	28.5	24.3	17.1
Net interest cover (x)	12.9	42.7	12.4	8.6	11.8

Source: Company data, Deutsche Bank estimates

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Investment Thesis

Outlook

We downgrade Kerry Properties to Hold with a revised target price of HK\$29 (HK\$29.2) based on a new valuation methodology, which we believe is more appropriate in an ex-growth market on an aging population in Hong Kong. While we prefer defensive names with secure dividend/scope for further dividend hikes where Kerry has the highest dividend coverage ratios by recurring income among peers at 179% (net profit from IP fully covers its dividend), we believe this is already well reflected in the current share price, after a strong share price rally YTD.

Valuation

Our target price is based on the sum-of-the-parts approach (previously target discount on overall NAV), which implies a 2017 PE of 9x. We believe applying a 5-7x PE to HK property development and a 34% target discount to our estimated value on the respective investment property portfolio are appropriate in an ex-growth market. For China property development, we believe applying a 7x PE (at the upper range of 2019E PE for China developers and at par with industry leaders with strong financial positions such as COLI and CR Land) is appropriate considering the financial strength and profitability profile of Hong Kong developers. This is the new valuation metric adopted for all HK developers under our coverage.

Risks

- Key downside risks:
 - Fluctuation in the Hong Kong/China economy could lead to lower/higher housing demand.
 - An interest rate hike and continuous liquidity outflow could severely hurt sentiment and demand in the property market in Hong Kong.
 - Unexpected fluctuations in the Chinese economy could affect our forecasts.
 - If the actual rental/price declines are more severe than our current projection, there could be downside to our current forecast and projected dividend payout and vice versa.
- Key upside risk:
 - The property market may further strengthen if the low interest rate environment persists.
 - The Hong Kong government may loosen on the existing administrative measures on the property sector should there be more signs pointing to a downward trend in the property market.
 - If competition for land is not as intensified as expected, Kerry may be able to acquire land at more reasonable prices and NAV growth will be faster than our current expectation.



Financial Analysis

FY17-19E earnings revised by -1-10% considering our latest ASP assumptions

Due to worsening demographic trends, we expect HK to see a precipitous slide in housing demand, coupled with rising supply, which will inevitably push the vacancy rate to more than double to 9% (from 3.8% now) and prices to slide 48% in 2017-24 (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026). In our previous ASP assumption, we assumed a 21% decline in 2017-19 (-11% in 2017, -7% in 2018 and -5% in 2019). Consequently, we revise our earnings estimates by 8-11% in FY17-19. We have revised our earnings estimates by 8% to HK\$4,914m for FY17E, 11% to HK\$3,635m for FY18E and -0.3% to HK\$4,993m for FY19E.

Figure 116: Summary of earnings revisions

	2017E			2018E			2019E		
	New	Old	%	New	Old	%	New	Old	%
Revenue	27,083	26,599	2%	25,770	25,307	2%	28,017	28,064	0%
Gross profit	8,431	7,948	6%	6,745	6,282	7%	8,526	8,573	-1%
Profit before tax	7,206	6,750	7%	5,760	5,322	8%	7,361	7,377	0%
Core profit	4,914	4,553	8%	3,635	3,274	11%	4,993	5,009	0%
EPS	3.41	3.14	8%	2.52	2.27	11%	3.46	3.47	0%
DPS	1.15	1.15	0%	1.17	1.17	0%	1.20	1.20	0%

Source: Deutsche Bank estimates



Figure 117: Income Statement (HK\$m)

For year ended Dec 31	2014A	2015A	2016A	2017F	2018F	2019F
Sale of properties	10,274	5,084	7,204	21,525	19,984	22,152
Rental and others	3,169	3,801	4,053	3,735	3,832	3,776
Hotel revenue	1,221	1,507	1,734	1,822	1,955	2,089
Revenue	14,664	10,393	12,991	27,083	25,770	28,017
Cost of sales	(8,456)	(6,482)	(7,135)	(18,652)	(19,025)	(19,491)
Gross Profit	6,208	3,911	5,856	8,431	6,745	8,526
Gross interest expenses	1,253	1,301	1,169	1,527	1,569	1,569
Capitalized interest	(670)	(877)	(901)	(763)	(785)	(785)
Net interest expense/(income)	583	424	268	763	785	785
Fair value loss on derivatives	44	127	143	-	-	-
Total finance costs	627	551	411	763	785	785
Depreciation expense	(4)	(4)	(3)	(12)	(12)	(13)
Interest income	323	324	301	301	301	301
Dividend income	91	98	105	111	116	122
Administrative/other operating expenses	(1,240)	(1,075)	(1,278)	(2,844)	(2,732)	(2,970)
SG&A	(826)	(653)	(871)	(2,432)	(2,314)	(2,546)
Revaluation gains	2,511	2,466	3,244	-	-	-
Other adjustments	961	65	709	-	-	-
Profit from operations	8,231	5,243	8,529	5,248	3,659	5,208
Associates	1,303	2,018	1,801	1,958	2,101	2,153
Pre-tax profit	9,534	7,260	10,330	7,206	5,760	7,361
Taxation	(1,698)	(1,190)	(2,595)	(1,189)	(950)	(1,215)
Post-tax profit before MI	7,835	6,070	7,735	6,017	4,810	6,146
Minority interests	(1,062)	(541)	(1,198)	(1,103)	(1,175)	(1,153)
Net attributable profit	6,773	5,530	6,537	4,914	3,635	4,993
Adjustment for non-recurring items	(3,045)	(2,049)	(2,866)	-	-	-
Core net profit	3,728	3,481	3,671	4,914	3,635	4,993
Fully diluted Core EPS (HK\$)	2.58	2.41	2.54	3.41	2.52	3.46
DPS (HK\$)	0.90	0.90	1.10	1.15	1.17	1.20

Source: Deutsche Bank estimates, company data



Figure 118: Balance Sheet (HK\$m)

As of Dec 31	2014A	2015A	2016A	2017F	2018F	2019F
Non-current assets	99,040	83,512	94,074	97,181	95,121	92,944
Investment properties	55,519	57,065	56,950	58,944	59,259	59,676
Leasehold land and land use rights	1,198	1,270	1,893	1,893	1,893	1,893
Property, plant and equipment	5,039	5,405	5,758	5,758	5,758	5,758
Properties under development	33,409	13,749	22,307	23,419	21,044	18,451
Land deposits	1,262	3,468	1,086	1,086	1,086	1,086
Intangible assets	123	123	123	123	123	123
Other Assets	2,489	2,434	5,958	5,958	5,958	5,958
Associates	19,212	20,008	18,651	20,494	22,473	24,500
Current assets	27,180	47,697	58,137	56,370	57,131	60,459
Completed properties held for sale	3,589	4,698	3,787	4,684	4,209	3,690
Properties under development	8,024	30,496	34,985	30,445	27,358	23,986
Debtors & deposits/receivables/others	4,175	1,638	2,884	6,013	5,721	6,220
Bank balances & cash	11,391	10,865	16,481	15,228	19,844	26,563
Non-current assets as held for sale	-	-	386	386	386	386
Assets of disposal groups held for sale	-	-	1,398	1,398	1,398	1,398
Current liabilities	(12,463)	(24,080)	(30,595)	(32,270)	(26,277)	(26,268)
Bank loans and overdrafts	3,092	9,642	3,856	8,889	7,326	8,554
Other short term loans/ bonds	-	3,254	4,652	780	-	-
Forward sales/ rental deposits received	3,299	-	-	2,153	1,998	2,215
Creditors, deposits & accruals/others	4,228	10,017	20,596	18,958	15,462	14,008
Taxation	1,844	1,168	1,491	1,491	1,491	1,491
Liabilities of disposal groups held for sale	-	-	(339)	(339)	(339)	(339)
Total assets less current liabilities	132,969	127,137	141,711	143,219	149,892	153,079
Non-current liabilities	33,493	26,671	39,566	36,695	40,248	39,020
Long term bank loans	20,954	17,199	34,507	32,417	35,969	34,741
Other long term loans/ bonds	10,193	6,951	2,318	1,538	1,538	1,538
Amounts due to / (from) group companies	2,346	2,430	2,591	2,591	2,591	2,591
Others	-	90	150	150	150	150
Deferred income tax	6,062	6,304	6,927	6,927	6,927	6,927
Issued share capital	1,445	1,446	1,443	1,446	1,446	1,446
Share premium	12,384	12,427	12,409	12,427	12,427	12,427
Retained profits	50,659	55,533	60,713	63,968	65,914	69,176
Capital & other reserves	14,221	11,948	8,179	8,179	8,179	8,179
Shareholders' funds	80,079	81,353	82,744	86,019	87,965	91,227
Minority interests	13,336	12,809	12,474	13,577	14,752	15,905
Total capital employed	132,969	127,137	141,711	143,219	149,892	153,079

Source: Deutsche Bank estimates, company data



Valuation

Our revised estimated NAV is HK\$61 per share

Our estimated NAV is calculated via a sum-of-the parts valuation. For development properties, we apply a DCF to estimate the value of its projects by taking the estimated cash inflow from property sales minus the outstanding costs, including any outstanding land costs, construction costs, and related income taxes and LAT for China projects. For investment properties, we use the income capitalization approach, taking the estimated rental revenues of the investment properties and dividing this figure by the estimated cap rates. Our estimated rents and cap rates vary across the different types of properties and their locations. When arriving at the NAV for the company, we take the aggregate estimated value for the above business segments and add the company's net debt position. We value the stakes of listed companies at the prevailing market price. By factoring in our latest ASP assumption on Hong Kong residential prices (0% in 2017, -14% in 2018, -11% in 2019, -3% in 2020, -4% in 2021, -5% in 2022, -6% in 2023, -6% in 2024/25 and -7% in 2026), our revised estimated NAV is HK\$61 per share.

Figure 119: Kerry NAV breakdown (end-FY17)

	NAV (HK\$m)	NAV/share (HK\$)	% of NAV
Development property			
China	18,345	12.7	20.8%
Hong Kong	19,351	13.4	21.9%
Philippines	3,031	2.1	3.4%
	40,727	28.2	46.2%
Investment property			
China Office	17,852	12.3	14.9%
China Retail	14,941	10.3	12.5%
China SA	8,335	5.8	7.0%
China Hotel	3,742	2.6	3.1%
Hong Kong SA	10,875	7.5	9.1%
Hong Kong Retail	6,991	4.8	5.8%
Hong Kong Office	5,415	3.7	4.5%
Hong Kong Carpark	241	0.2	0.2%
Hong Kong Hotel	219	0.2	0.2%
Philippines Retail	1,636	1.1	1.4%
Philippines Office	271	0.2	0.2%
Philippines Carpark	71	0.0	0.1%
Philippines Hotel lease	17	0.0	0.0%
	70,605	48.8	59.1%
Others			
Champion REIT (2778.HK)	754	0.5	0.9%
Kerry Logistics (636.HK)	7,471	5.2	8.5%
	8,225	5.7	9.3%
Gross asset value (GAV)	119,557	82.7	135.5%
Net cash / (debt)	(28,852)	(20.0)	-32.7%
Outstanding land premium	(2,466)	(1.8)	-2.8%
Net asset value (NAV) - fully diluted	88,239	61.0	100.0%

Source: Deutsche Bank estimates



Target price of HK\$29 is based on sum-of-the-parts

We believe the conventional valuation methodology of applying an overall target discount on the accessed NAV is less relevant in valuing developers as market fundamentals have changed and that historical average may not necessarily serve as a good reference. By taking into account that HK developers are likely to diversify their business focus further away from property sales in an ex-growth market, we believe the most appropriate valuation metric is sum-of-the-parts (SOTP), where we adopt PE for the property development business and the income capitalization approach for investment properties.

In deriving the target price, we prefer the sum-of-the-parts approach to the previous methodology of applying a target discount to the overall net asset value estimate. Specifically, we believe applying a 6x PE to Hong Kong property development is appropriate in an ex-growth market. Meanwhile, for investment properties, we believe applying a 34% target discount to our estimated value on the respective investment property portfolio is appropriate as the average discount for landlords has been relatively stable at 34% in the past 25 years. For China property development, we believe applying a 7x PE (at the upper range of 2019E PE for China developers and at par with industry leaders with strong financial positions such as COLI and CR Land) is appropriate by considering the financial strength and profitability profile of Hong Kong developers. By adopting the new valuation metric, we derive our target price for Kerry at HK\$29.

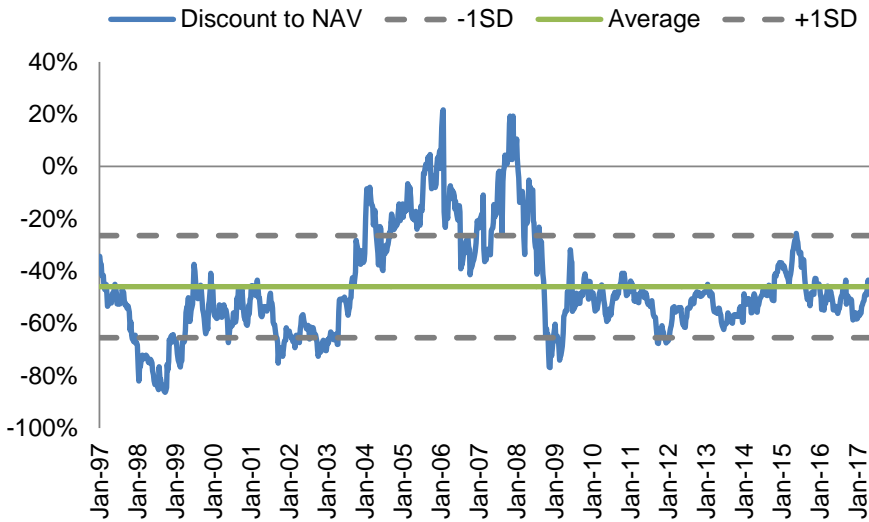
Figure 120: Kerry target price breakdown

Category	HK\$ per share
Development properties – Hong Kong	6.3
Development properties – China	6.4
Investment properties	32.3
Other assets	5.7
Net cash / (debt) & other adjustments	(21.7)
Target price	29.0

Source: Deutsche Bank estimates

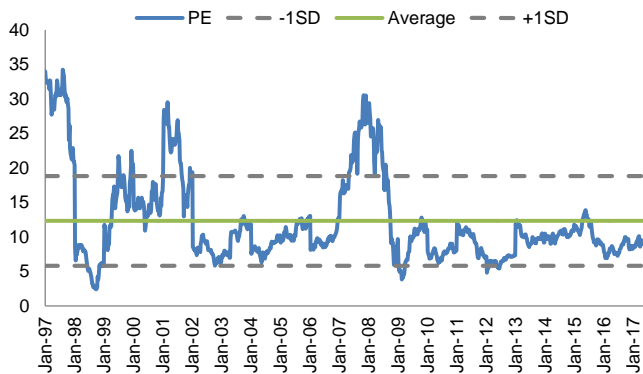


Figure 121: Kerry – Discount to NAV



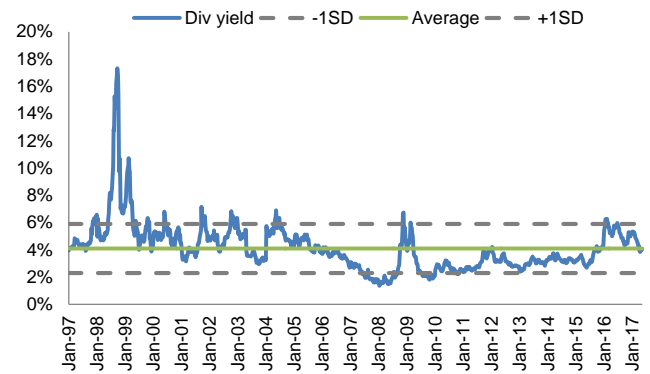
Source: Deutsche Bank estimates; Bloomberg Finance LP

Figure 122: Kerry - PE



Source: Deutsche Bank estimates; Bloomberg Finance LP

Figure 123: Kerry - PB



Source: Deutsche Bank estimates; Bloomberg Finance LP



Risks

Macro risks

- Further slowdown in the Hong Kong/China economy could lead to lower housing demand and vice versa.
- An interest rate hike and continuous liquidity outflow could severely hurt sentiment and demand in the property market in Hong Kong. On the other hand, if the low interest rate environment persists, current high property prices could be well supported.
- Unexpected fluctuations in the Chinese economy could affect our forecasts.

Company-specific risk

- If the actual rental/price declines are more severe than our current projection, there could be downside to our current forecast and projected dividend payout and vice versa.
- If competition in the land market is not as intensified as expected, Kerry may be able to acquire projects at more reasonable costs and NAV growth will be faster than our current expectation.
- Kerry has long been penalized by its relatively slow execution. If execution capability improves, we may see a re-rating in the stock.



Appendix 1

Important Disclosures

*Other information available upon request

Disclosure checklist

Company	Ticker	Recent price*	Disclosure
New World Dev	0017.HK	10.78 (HKD) 6 Jun 17	14,15
CK Property	1113.HK	61.30 (HKD) 6 Jun 17	1,7

Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg and other vendors. Other information is sourced from Deutsche Bank, subject companies, and other sources. For disclosures pertaining to recommendations or estimates made on securities other than the primary subject of this research, please see the most recently published company report or visit our global disclosure look-up page on our website at <http://gm.db.com/ger/disclosure/DisclosureDirectory.eqsr>. Aside from within this report, important conflict disclosures can also be found at <https://gm.db.com/equities> under the "Disclosures Lookup" and "Legal" tabs. Investors are strongly encouraged to review this information before investing.

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Disclosures marked with an asterisk may also be required by at least one jurisdiction in addition to the United States. See Important Disclosures Required by Non-US Regulators and Explanatory Notes.

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1. Within the past year, Deutsche Bank and/or its affiliate(s) has managed or co-managed a public or private offering for this company, for which it received fees.
7. Deutsche Bank and/or its affiliate(s) has received compensation from this company for the provision of investment banking or financial advisory services within the past year.

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The views expressed in this report accurately reflect the personal views of the undersigned lead analyst about the subject issuers and the securities of those issuers. In addition, the undersigned lead analyst has not and will not receive any compensation for providing a specific recommendation or view in this report. Jason Ching



Historical recommendations and target price: New World Dev (0017.HK)

(as of 6/6/2017)



Previous Recommendations

- Strong Buy
- Buy
- Market Perform
- Underperform
- Not Rated
- Suspended Rating

Current Recommendations

- Buy
- Hold
- Sell
- Not Rated
- Suspended Rating

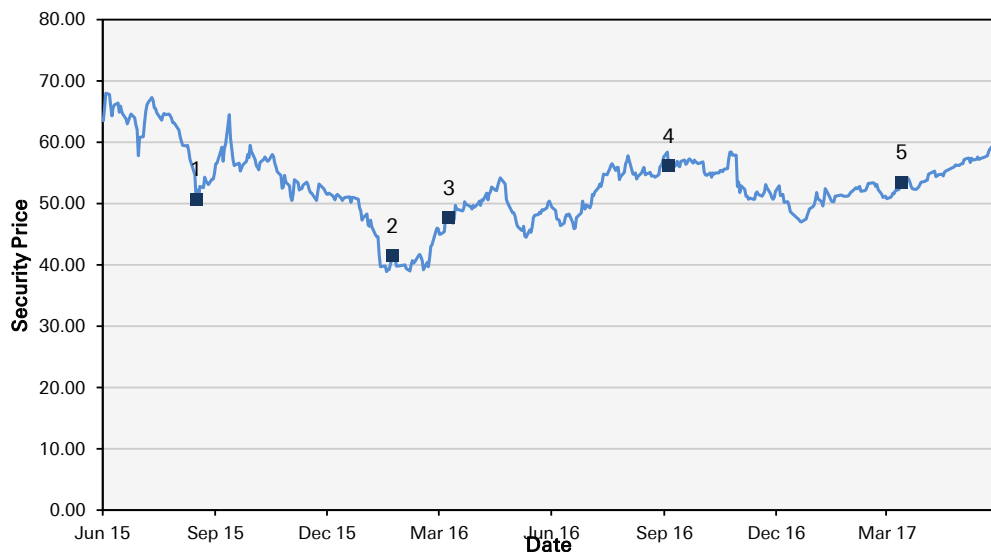
*New Recommendation Structure as of September 9,2002

**Analyst is no longer at Deutsche Bank

1.	28/09/2015:	Buy, Target Price Change HKD13.00	Jason Ching	3.	13/09/2016:	Buy, Target Price Change HKD10.90	Jason Ching
2.	28/01/2016:	Buy, Target Price Change HKD8.67	Jason Ching	4.	22/02/2017:	Buy, Target Price Change HKD11.10	Jason Ching

Historical recommendations and target price: CK Property (1113.HK)

(as of 6/6/2017)



Previous Recommendations

- Strong Buy
- Buy
- Market Perform
- Underperform
- Not Rated
- Suspended Rating

Current Recommendations

- Buy
- Hold
- Sell
- Not Rated
- Suspended Rating

*New Recommendation Structure as of September 9,2002

**Analyst is no longer at Deutsche Bank

1.	25/08/2015:	Buy, Target Price Change HKD75.00	Jason Ching	4.	13/09/2016:	Buy, Target Price Change HKD69.30	Jason Ching
2.	01/02/2016:	Buy, Target Price Change HKD50.00	Jason Ching	5.	22/03/2017:	Buy, Target Price Change HKD72.20	Jason Ching
3.	18/03/2016:	Buy, Target Price Change HKD53.50	Jason Ching				



Equity rating key

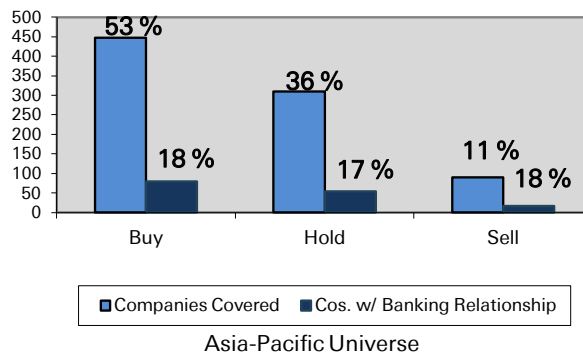
Buy: Based on a current 12-month view of total share-holder return (TSR = percentage change in share price from current price to projected target price plus projected dividend yield), we recommend that investors buy the stock.

Sell: Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock

Hold: We take a neutral view on the stock 12-months out and, based on this time horizon, do not recommend either a Buy or Sell.

Newly issued research recommendations and target prices supersede previously published research.

Equity rating dispersion and banking relationships





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Macroeconomic fluctuations often account for most of the risks associated with exposures to instruments that promise to pay fixed or variable interest rates. For an investor who is long fixed rate instruments (thus receiving these cash flows), increases in interest rates naturally lift the discount factors applied to the expected cash flows and thus cause a loss. The longer the maturity of a certain cash flow and the higher the move in the discount factor, the higher will be the loss. Upside surprises in inflation, fiscal funding needs, and FX depreciation rates are among the most common adverse macroeconomic shocks to receivers. But counterparty exposure, issuer creditworthiness, client segmentation, regulation (including changes in assets holding limits for different types of investors), changes in tax policies, currency convertibility (which may constrain currency conversion, repatriation of profits and/or the liquidation of positions), and settlement issues related to local clearing houses are also important risk factors to be considered. The sensitivity of fixed income instruments to macroeconomic shocks may be mitigated by indexing the contracted cash flows to inflation, to FX depreciation, or to specified interest rates – these are common in emerging markets. It is important to note that the index fixings may – by construction – lag or mis-measure the actual move in the underlying variables they are intended to track. The choice of the proper fixing (or metric) is particularly important in swaps markets, where floating coupon rates (i.e., coupons indexed to a typically short-dated interest rate reference index) are exchanged for fixed coupons. It is also important to acknowledge that funding in a currency that differs from the currency in which coupons are denominated carries FX risk. Naturally, options on swaps (swaptions) also bear the risks typical to options in addition to the risks related to rates movements.

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