

## Aoyuan Healthy Life Group

### A Major Step in Building a Healthcare and Beauty Business Empire

Aoyuan acquired a land to develop a Healthcare and Beauty Complex in Shanghai, which we estimate will generate a ROIC of ~14% for the project itself. China Aoyuan Group (3883.HK) will bear the cost of the construction, so that Aoyuan Healthy life will remain asset-light. This marks a major step in Aoyuan Healthy Life in developing its Healthcare and Beauty Empire, in our view.

#### Development of Aoyuan's first Healthcare and Beauty Complex

On 12 Dec 2019, Aoyuan Healthy Life announced that they have successfully acquired a land in Shanghai Fengxian District to develop a Healthcare and Beauty Industrial Complex. We believe this is a key milestone in realizing the company's long term vision into the development of Healthcare and Beauty business line. Company also announced on 17 Dec 2019, that China Aoyuan Group will bear the cost of construction which should allay investors' concerns that Aoyuan Healthy Life is diverting away from their asset-light Prop Management + Healthcare business model. We believe that the development of the hardware (i.e. the complex) is only the first step. The more important assets are the Healthcare and Beauty business network that it will help Aoyuan build up and establish themselves in this new industry, in our view.

#### We estimate ~14% ROIC for the project, driving shareholders' returns

The land cost was only RMB82m for a Scientific Research and Design use land with GFA of 75,923sqm. This implies an AV of RMB1,080/sqm. If we add in a construction cost of ~RMB6,000/sqm the total cost of the complex will only be ~RMB7,000/sqm. To assess the value of this project, we can assume a rental value of ~RMB80/sqm/month, the unleveraged ROIC will be ~14%, plus the potential profits that will be generated from Aoyuan's Healthcare and Beauty businesses developed inside this complex. Just as a reference point, residential/commercial land sites in Shanghai Fengxian District has an AV of ~RMB15,000/sqm and residential properties are selling at an ASP of ~RMB30,000-35,000/sqm.

#### New Service Offering to Aoyuan Community

Customer acquisition cost is often a key obstacle when building any new business, but Aoyuan Healthcare can easily leverage on their community of potential customers living in their properties and cross-sell such Healthcare & Beauty services to this existing customer base, which we estimate at ~500,000 as of 2019. This will add to the earnings growth of the company in additional to the steady stream of property management fees.

#### Management expertise already in place to create value

Aoyuan Healthy Life has already added a strong management team of Healthcare specialists to help develop the Healthcare Business. Mr. Su Bo, Executive Vice President of Aoyuan Healthcare was previously President of Panyu Central Hospital and has extensive experience in Healthcare Industry. Meanwhile, Mr. Bai Chengmin, VP of Aoyuan Healthcare and GM of Aoyuan Medical Beauty, was previously CEO of Oracle Medical Group which had 70 beauty clinics across Asia.

This report marks the transfer of coverage to Jacky Chan.

Stock code: 3662.HK

Rating: Buy

<b>Price target (HK\$)</b>	<b>7.0</b>
Current price (HK\$, 16 Dec 2019)	5.64
Upside/downside %	24%
Market cap (HK\$ m)	22,832
Market cap (US\$ m)	2,946
Avg daily turnover (US\$ m)	3.6

Source: Bloomberg, AMTD Equity Research

#### Key forecasts

(RMB m)	2018	2019e	2020e	2021e
Revenue	619	893	1,275	1,771
yoy %	41.9%	44.4%	42.7%	38.9%
Net profit	78	123	208	293
yoy %	11.9%	57.5%	68.9%	40.7%
Adjusted NP	94	150	208	293
yoy %	11.9%	57.5%	68.9%	40.7%
Gross margin	33.7%	34.4%	34.4%	34.6%
Net gearing	Net Cash	Net Cash	Net Cash	Net Cash
EPS	0.13	0.21	0.29	0.40
DPS	0.00	0.05	0.08	0.11
BPS	0.16	0.17	1.14	1.42

Source: Company data, AMTD Equity Research

#### Valuation

	2018	2019e	2020e	2021e
P/E	38.0	24.6	17.7	12.6
P/BV	32.2	29.3	4.5	3.6
Div. yield	0.0%	1.6%	2.3%	3.2%
ROE	66.2%	28.9%	22.4%	24.8%
ROA	14.6%	10.5%	15.7%	18.0%

Source: Bloomberg, AMTD Equity Research

#### Share price performance



Source: Bloomberg

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Figure 1: Aoyuan Healthy Life Financial Forecasts and Key ratios

PnL, RMB mn	2017	2018	2019e	2020e	2021e	Balance Sheet, RMB mn	2017	2018	2019e	2020e	2021e
Revenue	436.0	618.8	893.4	1,274.6	1,770.6	Property, plant and equipment	5.6	12.7	12.7	12.7	12.7
COGS	(287.5)	(410.1)	(586.2)	(836.1)	(1,158.2)	Intangible assets	3.9	3.0	2.4	1.9	1.6
<b>Gross Profit</b>	<b>148.5</b>	<b>208.8</b>	<b>307.2</b>	<b>438.5</b>	<b>612.3</b>	Goodwill	3.5	3.5	3.5	3.5	3.5
Selling and marketing expenses	(0.3)	(1.3)	(1.4)	(1.9)	(2.7)	Deferred tax assets	1.5	7.4	7.4	7.4	7.4
General and administrative expenses	(41.9)	(89.0)	(115.3)	(161.9)	(221.3)	Deposits paid for acquisition of PPE	-	1.1	-	-	-
Impairment losses on trade receivables	(2.0)	(1.0)	(0.5)	(0.5)	(0.7)	Deferred contract costs	3.4	2.3	2.3	2.3	2.3
IPO expenses	(4.6)	(15.5)	(27.0)	-	-	Amount due from a fellow subsidiary	-	-	-	-	-
Other income and other gains and losses	0.8	6.6	8.2	15.1	19.3	<b>Non-current assets</b>	<b>17.9</b>	<b>30.0</b>	<b>28.3</b>	<b>27.8</b>	<b>27.4</b>
Interests on bank borrowing	-	(0.0)	-	-	-	Inventories and other contract costs	0.1	0.1	0.2	0.2	0.2
<b>Profit before tax</b>	<b>100.4</b>	<b>108.5</b>	<b>171.2</b>	<b>289.2</b>	<b>406.9</b>	Trade and other receivables	87.3	87.0	82.4	114.4	106.1
Income tax expense	(30.5)	(30.2)	(47.9)	(81.0)	(113.9)	Deferred contract costs	11.2	9.5	8.4	12.0	(8.5)
<b>Net profit</b>	<b>69.9</b>	<b>78.3</b>	<b>123.3</b>	<b>208.2</b>	<b>293.0</b>	Amounts due from fellow subsidiaries	283.4	175.9	163.6	193.3	196.2
Shareholders' Profit	69.8	78.1	123.1	208.0	292.7	Amounts due from related parties	6.7	0.2	0.7	0.8	0.9
Minority Interest	0.2	0.1	0.1	0.2	0.3	Bank balances and cash	164.4	200.3	891.4	1,123.2	1,459.0
<b>Shareholders' Core Net Profit</b>	<b>74.4</b>	<b>93.7</b>	<b>150.1</b>	<b>208.0</b>	<b>292.7</b>	<b>Current assets</b>	<b>553.0</b>	<b>473.1</b>	<b>1,146.6</b>	<b>1,444.0</b>	<b>1,754.0</b>
Dividends	-	170	39	60	83	Contract Liabilities	45.1	120.8	93.6	135.8	147.5
Special Dividends	-	-	-	-	-	Bank and Other Borrowings	-	1.8	1.8	1.8	1.8
EPS - basic	-	0.11	0.17	0.29	0.40	Trade and Other Payables	196.5	226.2	220.5	263.9	267.3
EPS-underlying	-	0.13	0.21	0.29	0.40	Others	217.3	27.2	31.7	34.8	36.4
DPS - basic	-	-	0.05	0.08	0.11	<b>Current liabilities</b>	<b>458.9</b>	<b>376.0</b>	<b>347.6</b>	<b>436.3</b>	<b>452.9</b>
BPS	-	0.16	0.17	1.14	1.42	Deferred tax liability	1.0	0.8	0.8	0.8	0.8
						Others	-	-	-	-	-
						<b>Non-current liabilities</b>	<b>1.0</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>
						Capital and reserves	110.5	125.7	825.9	1,034.2	1,327.1
						<b>Shareholders' equity</b>	<b>110.5</b>	<b>125.7</b>	<b>825.9</b>	<b>1,034.2</b>	<b>1,327.1</b>
						Non-controlling interests	0.5	0.6	0.6	0.6	0.6
						<b>Total equity</b>	<b>111.0</b>	<b>126.3</b>	<b>826.6</b>	<b>1,034.8</b>	<b>1,327.8</b>
<b>Cash Flow Statement, RMB mn</b>	<b>2017</b>	<b>2018</b>	<b>2019e</b>	<b>2020e</b>	<b>2021e</b>	<b>Key Ratios, RMB mn</b>	<b>2017</b>	<b>2018</b>	<b>2019e</b>	<b>2020e</b>	<b>2021e</b>
Profit Before Tax	100.4	108.5	171.2	289.2	406.9	GP Margins	34%	34%	34%	34%	35%
<b>Operating CF before Working Cap</b>	<b>104.3</b>	<b>107.5</b>	<b>174.4</b>	<b>292.3</b>	<b>410.1</b>	Net Margins	16%	13%	14%	16%	17%
PUD	0.0	0.0	(0.1)	-	(0.0)	Core Attri Net Margins	17%	15%	17%	16%	17%
Trade & Other Receivables	(53.8)	2.9	4.2	(32.5)	7.5	ROE	73%	66%	29%	22%	25%
Trade & Other Payables	90.3	29.2	(5.8)	43.4	3.4	ROA	15%	15%	10%	16%	18%
Increase in contract liabilities	9.6	75.7	(27.2)	42.2	11.7	Net Debt / Total Equity	Net cash	Net cash	Net cash	Net cash	Net cash
Deferred Contract Costs	(5.8)	2.7	1.1	(3.6)	20.5	Net Debt / Shareholders' Equity	Net cash	Net cash	Net cash	Net cash	Net cash
Others	(106.9)	5.5	(31.5)	(107.8)	(115.4)	Total Assets / Total Equity	514%	398%	142%	142%	134%
<b>Net Operating Cashflows</b>	<b>37.7</b>	<b>223.6</b>	<b>115.2</b>	<b>233.9</b>	<b>337.9</b>	Total Assets / Shareholders' Equity	517%	400%	142%	142%	134%
<b>Net Investing Cashflows</b>	<b>5.6</b>	<b>(249.2)</b>	<b>(1.1)</b>	<b>(2.1)</b>	<b>(2.1)</b>	Asset Turnover	97%	115%	106%	96%	109%
Bank & Other Borrowings	-	1.8	-	-	-						
Others	51.4	40.5	577.0	-	-						
<b>Net Financing Cashflows</b>	<b>51.4</b>	<b>42.2</b>	<b>577.0</b>	<b>-</b>	<b>-</b>						
<b>Net Cash Flows</b>	<b>94.7</b>	<b>16.6</b>	<b>691.1</b>	<b>231.8</b>	<b>335.8</b>						

Source: Company data, AMTD Equity Research

## Valuation and Risks

### DCF valuation – HK\$7.0 per share

Our price target of HK\$7.0 is based on the three-stage discounted cash flow model. This implies 2020e P/E (recurring) of 21.5x (in-line with industry average). We use a three-stage DCF model to derive our valuation. In the first stage (the fast growth stage), we forecast explicitly five year of free cash flows to the enterprise. In the second stage (medium term), the growth rates are gradually phased down towards the perpetual growth rate. We derive the terminal multiple using the standard  $(1+g)/(wacc-g)$ . This cash flow stream is discounted using 11.7% weighted average cost of capital (“WACC”) assumption.

Figure 2: Derivation of DCF valuation

Stage 1	518
Stage 2	1,214
Stage 3	1,854
Net cash	890
Total equity value (Rmb mn)	4,475
Total equity value (HK \$mn)	5,085
Shares outstanding (mn)	726
<b>Dec-20 Price target (HK\$)</b>	<b>7.0</b>
Implied 2019e PE	29.8x
Implied 2020e PE	21.5x

Source: AMTD Research

Figure 3: Peers Valuation comparison

Date	12/16/2019	Share Price (HK\$)	ADTV (USD mn)	Mkt cap (USD mn)	FY18 P/E	FY19E P/E	FY20E P/E	FY18 P/B	FY19E P/B	FY20E P/B	Div. yield
<b>Equity</b>											
<b>China Property Management</b>											
3662 HK	Aoyuan Healthy Life	5.64	3.57	526	37.9x	24.6x	17.7x	32.2x	29.3x	4.5x	NA
2168 HK	Kaisa Prosperity	18.80	1.07	338	37.6x	17.8x	13.4x	5.2x	4.6x	3.6x	NA
6098 HK	Country Garden Services	26.30	17.33	9,152	71.2x	46.9x	35.3x	29.1x	14.4x	11.1x	0.5%
3319 HK	A-Living Services	26.85	19.68	4,595	43.3x	31.4x	22.4x	2.1x	6.0x	5.1x	0.0%
1778 HK	Colour Life	4.20	1.85	767	11.1x	10.3x	8.9x	1.8x	1.5x	1.4x	3.7%
2869 HK	Greentown Service	8.04	6.76	2,878	47.3x	39.2x	29.9x	9.6x	8.3x	6.9x	0.9%
<b>Total</b>					<b>41.4x</b>	<b>28.4x</b>	<b>21.2x</b>	<b>13.3x</b>	<b>10.7x</b>	<b>5.4x</b>	

Source: Bloomberg Estimates, \*AMTD Equity Research Estimates

Note: As of 16<sup>th</sup> Dec, 2019; \*Div Yield is Trailing Dividend Yield

### Key Risks

Key risks for the stock includes (1) the capital deployed into Healthcare and Beauty sector will create uncertainty and business risks; (2) Slower than expected project completion and delivery of property projects affecting the growth in Properties Under Management.

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#### Stock Rating

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

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We, Jacky Chan and Michelle Li, hereby certify that (i) all of the views expressed in this research report reflect accurately our personal views about the subject company or companies and its or their securities; and (ii) no part of our compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed by us in this research report, nor is it tied to any specific investment banking transactions performed by AMTD Global Markets Limited.

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