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Equity Research

# Bubble Burst? Nope! Just Slow Down!

Home sales to slow down; sector valuation to de-rate

as the strictest tightening keeps going

2016 was a harvest year for real estate developers, Home-purchase-restriction (HPR) was loosened in 2nd and 3rd tier cities, mortgage rate was lowered, and developers recorded strong sales growth with rapid home price surge. However, as inventory dropped to a healthy level, tightening cycle ticked in again.

Sales performance in larger cities and that in lower tier cities diverged in 5M17: GFA sold in top 36 cities declined by 25% yoy vs. national GFA sold grew by 14% yoy. Giants are expanding their market shares, mid-sized developers' market share has been compressed further. The era of oligopoly has come.

Property sector share price on average has gained 50% YTD; sector average PE is approaching their highs in 2015 and 2012. We expect the property sector valuation to de-rate in 2H17. We selectively overweigh developers with achievable presales growth, less share price gain YTD, and relatively low valuation. We are cautious on developers with big share price gains.
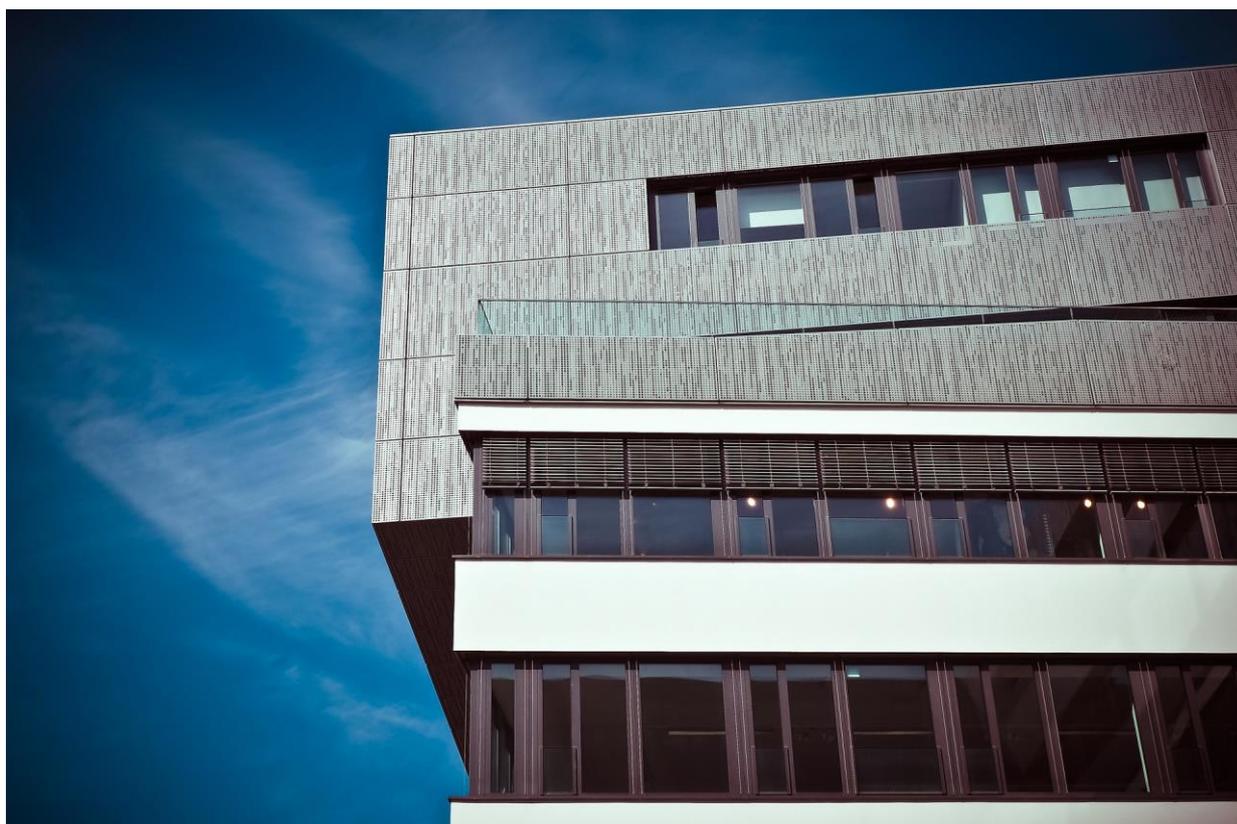
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Executive summary

Be cautious on giants, look for safety margin

We expect the property sector valuation to de-rate in 2H17. We selectively overweigh developers with achievable presales growth, less share price gain YTD, and relatively low valuation. We are cautious on developers with big share price gains YTD, as main consolidators such as Evergrande and Country Garden performed very well YTD, up by 187% and 106%. Thanks to the rapid growth of contracted sales in 3rd tier cities. Sunac also gained 137% YTD. We believe positive factors of 3rd tier cities have been priced in share price of Evergrande/ Country Garden/ COGO.

The 12mth forward P/E of property sector is about 8.3x, approaching their highs in 2015 and in 2012. We look back to 6 year ago, the hardest time in 2011, the market cap weighted P/E of property sector was only 4x. Giants and 3rd tier cities players with over 50% gain YTD should be avoided. On the other hand, names with low P/E & P/B, 15% ROE and high dividend yield should have higher safety margin and attractive.

Omni-directional tightening in 2017

New HPR introduced in 2017 reduced valid demand in 1st tier cities. A couple used to be allowed to own 4 units, but now is only allowed to own 2 units. The HPR requires 5 year social security record for home buying. Buyers with unpaid mortgages are required to put down 50%/70% down payment for their first home/second homes. 1st and 2nd tier cities introduced 2-3 year lockup period for home resold. Presale price cap is stricter than before, making developers to delay project launches. Land supply have been enlarged to stabilize land price in short term.

Sales growth momentum halted

As the HPR loosened in 2016, GFA sold grew strongly by 22.5% yoy in 2016. However, as HPR tightened again, the growth in GFA sold in 5M17 slowed down to 14.3% yoy, comparing to a 33.2% yoy growth for 5M16. Sales performance in larger cities and that in lower tier cities diverged in 5M17: GFA sold in top 36 cities declined by 25% yoy vs. national GFA sold grew by 14% yoy. Most developer are patient to wait till Golden Sept. & Silver Oct (金九银十) in order to launch projects at a desirable price. We believe the strict tightening intends to cool down the market and lower home price, not clamp down the market.

Inventory lowered and investment of real estate come to steady and healthy growth

Due to the strong sales in 2016/17, national inventory months have declined to a very healthy level of only 21.3 months in May 2017, the lowest level since 2011. This gives room and time for the tightening policies. Saleable GFA peaked in Feb. 2016. Then it declined steadily and recorded yoy declined in Nov. 2016. It is the first time recorded yoy decline of saleable GFA since 2004. In May 2017, saleable GFA declined by 8.5% yoy, while saleable residential GFA further declined by 17.8% yoy. Meanwhile, the growth of newly commence GFA are lower than that of GFA sold in 2015/2016/first 5 months of 2017. It indicates 1) developers are more cautious on commencement, in order to avoid liquidity crisis; and 2) uncertainty of policy trend in the near term.

Great improvement after a loosening year

18 of 29 developers have lowered their net gearing ratio in FY16. Booking GPM in FY16 have significantly improved as well. In FY15, only 4 of 29 companies recorded yoy increase of GPM. In FY16, only 7 of 29 companies recorded decline of GPM.

The era of oligopoly has come

Listed developers' performances are unexpectedly good. 5 companies have achieved over 50% of their target. Longfor even achieved 69% of its target. Developers mainly in 3rd tier cities, Evergrande, Country Garden and COGO, achieved 75.9%/ 30.9%/ 126.5% yoy growth. The era of oligopoly has come. Top 20 companies accounted for 25.2% of total home sales in China. Top 100 companies accounted for 44.8% of total sales. 21-100 ranking companies only accounted for 19.6% of total sales. In first 5 months of 2017, top 20 accounted for 59.6% of total sales, top 100 accounted for 37.1% of total sales, 21-100 ranking companies only accounted for 22.5%.

Omni-directional tightening in 2017

New round tightening has come for cooling down home price. Stricter HPR, pre-sales price restriction, high down payment rate and suspension of bond issuance are all applied.

Less quota for Singles, 2-3 year of lockup period for home resold

HPR policies become more specific in 1H2017. The singles and the families have different quota to buy house. In 1st tier cities, a family is allowed to buy two units of houses. The singles are allowed to buy only one house. New HPR reduces valid demand in 1st tier cities. A couple was allowed to buy 4 units, but now is only 2 units. Longer social insurance record is another barrier for non-local home buyers. The previous version of HPR require 2-3 year record of HPR policies. The updated version required 5 year record. After 1st tier cities introducing stricter version of HPR, 2nd tier cities follow suit.

Mortgage record is also a key factor under current HPR. Home buyers with unpaid mortgage record are required 50%/70% down payment for first home/second home. On the other hand, in order to reduce short term investment purchase, 1st and 2nd tier cities introduce 2-3 year lockup period for home resold in different cities.

Figure 1: New HPR introduced in 2016

| Cities	Local residents		Non-local residents		Down payment requirement			
	Family quota (units)	Single quota (units)	Quota (units)	Social Insurance Record (Years)	First Home (No mortgage record)	Second Home (No mortgage record)	First Home (With mortgage record)	Second Home (With mortgage record)
Beijing	2	1	1	5	35%	80%	80%	80%
Shanghai	2	1	1 (For family only)	5	35%	70%	70%	70%
Shenzhen	2	1	1	5	30%	50%	70%	70%
Guangzhou	2	1	1	5	30%	70%	70%	70%
Nanjing	2	1	1	2	30%	50%	50%	80%
Hangzhou	2	1 （included divorce）	1	2	30%	60%	30%	60%
Suzhou	2	1	1	5	30%	70%	70%	70%
Wuhan	3	3	1	3	30%	50%	50%	80%
Xiamen	2	1	1	3	30%	70%	30%	70%
Jinan	2	2	1	2	30%	60%	30%	60%
Zhengzhou	2	2	1	2	30%	60%	60%	60%
Hefei	2	2	1	1	30%	40%	40%	50%
Nanchang	1	1	1	2	30%	40%	40%	50%
Changsha	2	2	1	1	30%	35%	30%	45%
Tianjin	2	1	1	2	30%	70%	30%	70%
Shijiazhuan	No HPR	No HPR	1	1	30%	60%	30%	60%
Qindao	No HPR	No HPR	1	1	30%	50%	30%	50%
Fuzhou	2	2	1	1	30%	50%	30%	50%
Haikou	3	3	1	2	25%	40%	25%	50%
Ningbo	2	2	1	1	30%	40%	30%	40%

Source: CRIC; AMTD Equity Research

Government still executes the old ways to cool down the physical market: 1) control the pace of home demand releasing; 2) control pre-sales price of new residential projects.

However, **DOES IT WORK?** As Figure 2 shows, the efficiency of HPR lasted 6-9 months. After that, mom growth of home price rebounded again and turned to be positive growth in next 6-9 months. The last HPR tightening started at October 2016. Home price index fell from 1 in October 2016 to only 0.3 in January 2017, rebounded to 0.7 in April 2017. According to HPR history in last 6 years, if the home price rebounded in short term, more

HPR will be introduced in next 6-9 months. We estimate HPR will **not be the only** policy introduced this time.

Figure 2: Efficiency of Home Purchase Restriction
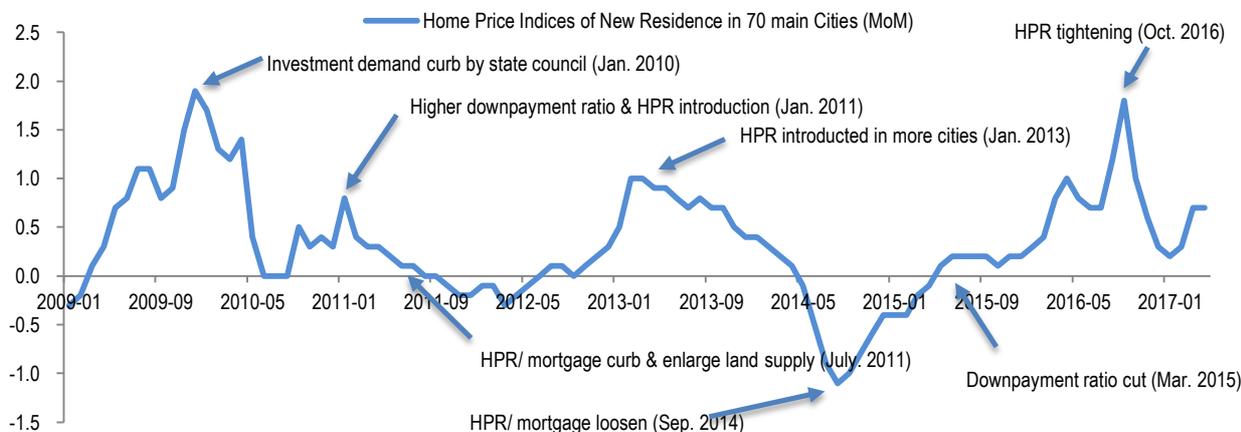
Source: NBS; AMTD Equity Research

More than HPR: strict approval of pre-sales price, bond issuance suspension and enlarge land supplies

In 1Q2017, 1st & 2nd tier cities have tightened the approval for pre-sales price, mainly the tightening measures are 1) pre-sales price of new phase must be lower than previous phase; or 2) pre-sales price of new residence must be lower than or same as home price of nearby residences (some cities restrict some price limit at certain district). Regarding the rule one, it is acceptable because land cost is almost the same in different phases of same project. It just limits the gross margin upside. However, the rule two may be nightmare for developers, as land price keep jumping in last few years, home price is capped as same price of old residences, which are built with much lower land cost years ago. Some land cost of new residence is almost as same as home price of nearby residence. Developers have to launch residences after home price of nearby project surges rapidly, otherwise profitability of new project will be very low.

Another tightening measure is suspension of onshore bond issuance. Most applications of bond issuance by developers are suspended from 4Q2017. There is no signal that the suspension will be removed in the short term. As of 19 June 2017, only RMB151.7 bn of bonds are issued by developers in onshore market, which was RMB621.2 bn in 2016. Feedback from HK listed developers is consistent: no signal for loosening. However, some developers have been required to submit supplementary documents, after that, no response again. On the other hand, permission of offshore issuance from NDRC is still needed. NDRC curbs approval of offshore bond issuance very strictly. This move also indicates government intends to cool down land market. High liquidity will boost land price rapidly, then home price surge simultaneously. The land price and home price form an infinitive loop of home price rocket until liquidity dries up.

Moreover, land supply have been enlarged by the end of 2016. According to CRIC data, in Jan. to May 2017, land supplies in 1st/2nd/3rd tier cities increased 31.2%/12.3%/21.8% yoy. However, as credit tightening from 4Q2016, land sold in GFA recorded -1.3% yoy decline in 1st tier cities, only 3.2%/13.7% yoy growth in 2nd/3rd tier cities. Land supply in GFA in Shanghai Beijing and Shenzhen recorded 52.9%/56.8%/65.7% yoy growth, but land sold in GFA in Shanghai and Beijing recorded only 1.9% and 8.4% yoy growth. Shenzhen recorded 97.4% yoy growth, but sold over supply ratio is only 55%, much lower than those of Beijing, Shanghai and Guangzhou, which are over 70%.

Figure 3: Land supply in 1ˢᵗ / 2ⁿᵈ / 3ʳᵈ tier cities

| Cities	Cities in Chinese	GFA Sold in Jan. to May. 2016 (sq.m)	GFA Sold in Jan. to May. 2017 (sq.m)	yoy Growth
1st tier cities				
Shanghai	上海	3,498,081	5,347,308	52.9%
Beijing	北京	1,654,813	2,594,801	56.8%
Guangzhou	广州	3,967,448	3,320,736	-16.3%
Shenzhen	深圳	2,024,966	3,356,256	65.7%
Sub-total		11,145,308	14,619,101	31.2%
2nd tier cities				
Wuhan	武汉	11,389,221	16,586,325	45.6%
Chengdu	成都	9,091,105	9,902,280	8.9%
Tianjin	天津	15,280,436	17,248,491	12.9%
Qingdao	青岛	11,855,321	12,711,903	7.2%
Changsha	长沙	4,385,823	4,681,406	6.7%
Nanjing	南京	5,367,529	5,986,089	11.5%
Kunming	昆明	6,222,336	6,428,290	3.3%
Suzhou	苏州	5,662,251	4,717,869	-16.7%
Hangzhou	杭州	7,074,045	8,264,946	16.8%
Nanning	南宁	4,157,098	6,058,990	45.8%
Nanchang	南昌	4,108,088	4,044,492	-1.5%
Ningbo	宁波	8,077,626	8,303,321	2.8%
Dalian	大连	4,930,953	4,601,525	-6.7%
Fuzhou	福州	690,093	814,866	18.1%
Sub-total		98,291,925	110,350,793	12.3%
3rd tier cities				
Zhongshan	中山	1,869,553	1,901,280	1.7%
Dongguan	东莞	3,832,863	3,584,926	-6.5%
Changzhou	常州	8,117,410	9,216,692	13.5%
Wuxi	无锡	3,375,159	2,982,048	-11.6%
Weifang	潍坊	24,212,572	31,820,039	31.4%
Zhenjiang	镇江	5,867,589	7,726,158	31.7%
Baotou	包头	2,130,686	2,956,351	38.8%
Huizhou	惠州	3,382,537	2,603,375	-23.0%
Haikou	海口	1,055,870	1,113,864	5.5%
Wenzhou	温州	3,775,275	7,128,350	88.8%
Beihai	北海	260,745	273,544	4.9%
Langfang	廊坊	892,401	1,195,246	33.9%
Dongying	东营	4,656,462	6,531,048	40.3%
Lianyungang	连云港	2,435,865	3,257,711	33.7%
Changde	常德	4,946,472	4,874,530	-1.5%
Jiangmen	江门	2,632,319	3,175,286	20.6%
Jinhua	金华	4,844,136	6,154,222	27.0%
Zhaoqing	肇庆	5,718,467	5,400,560	-5.6%
Taizhou	泰州	1,184,226	1,918,438	62.0%
Taian	泰安	3,331,442	4,426,820	32.9%
Mudanjiang	牡丹江	1,307,975	1,745,785	33.5%
Anqing	安庆	2,937,307	3,466,687	18.0%
Shantou	汕头	2,423,536	2,246,422	-7.3%
Yueyang	岳阳	952,157	1,442,879	51.5%
Sub-total		96,143,024	117,142,261	21.8%
Total		205,580,257	242,112,155	17.8%

Source: CRIC; AMTD Equity Research

Sales growth momentum halted

Tightening policies show their efficiency.

In Jan. 2013, more cities introduced HPR, GFA sold growth declined from 17.3% yoy in 2013 to -7.6% yoy in 2014. In 2015, the GFA sold growth rebounded to 6.5% yoy, but much lower than that of 2013. As the HPR loosening in 2016, GFA sold growth rebounded 22.5% yoy in 2016. However, HPR tightening comes again, the growth in Jan. to May 2017 fell to 14.3% yoy, which was up 33.2% in Jan. to May 2016.

**Figure 4: Cumulative GFA sold in China**
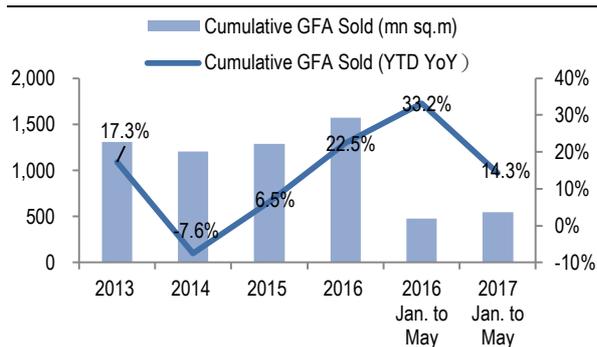
Source: NBS

The 15.7% growth seems to be good in tightening situation. However, GFA sold breakdown by cities will show you different views:

In 1st tier cities, GFA sold in Shanghai/Beijing/Shenzhen fell 41.4%/35.6%/53.1% yoy. Overall, GFA sold in 1st tier cities declined by 31.4%

In 2nd tier cities, Only 2 of 13 cities recorded positive yoy growth. GFA sold in 2nd tier cities declined by 28.2%

In 3rd tier cities, sales growth becomes polarization. Sales growth in Langfang/Beihai/Yueyang jumped to 322.1%/314.2%/161.6% yoy. Sales growth in Shantou/Haikou/Wuxi fell to -85.5%/-70.4%/-69.1%. GFA sold in 3rd tier cities was down by 25.8%. **Our guess is the growth of home sales may be in lower tier cities not tracked.**

Figure 5: GFA sold and yoy growth in 1st tier cities in Jan. to May 2017
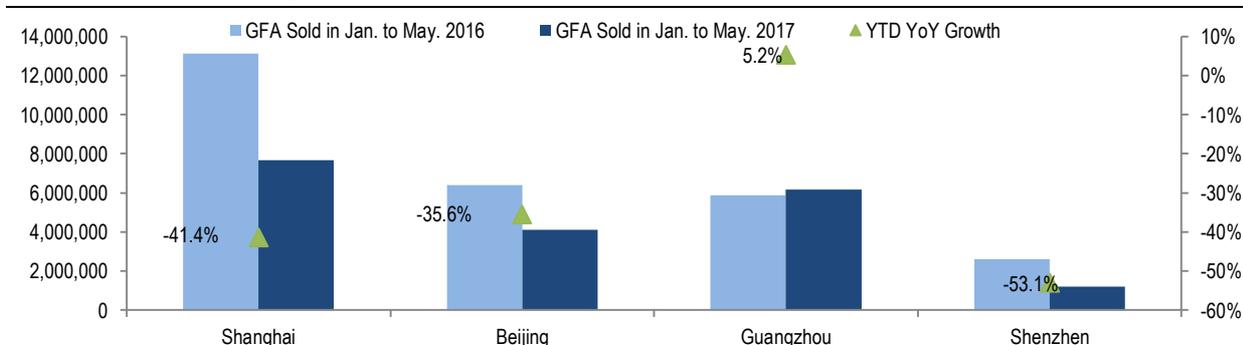
Source: CRIC; AMTD Equity Research

Figure 6: GFA sold and yoy growth in 2ⁿᵈ tier cities in Jan. to May 2017

Source: CRIC; AMTD Equity Research

Figure 7: GFA sold and yoy growth in 3ʳᵈ tier cities in Jan. to May 2017

Source: CRIC; AMTD Equity Research

Pre-sales price approval is the key in 2H2017

Moreover, pre-sales price approval is the key factor that developers have to worry. If the pre-sales price is approved at a low price, profitability will be much lower than expectation. However, if the developers hold on launching, interest burden will lower profit. It becomes a dilemma for developers. **Most developers are patient to wait till Golden Sept. & Silver Oct (金九银十) in order to launch new supplies at desirable price. The strict tightening intends to cool down the market and lower home price, not clamp down the market.**

Inventories & Investment

It is unavoidable to discuss these topics in property sector report. We all know property play crucial role in GDP growth. However, how crucial is the property market?

Last round of loosening succeed in destocking

Due to the strong sales in 2016/17, national inventory months have declined to a very healthy level of only 21.3 months in May 2017, the lowest level since 2011. This gives room and time for the tightening policies.

Saleable GFA peaked in Feb. 2016. Then it declined steadily and recorded yoy declined in Nov. 2016. It is the first time recorded yoy decline of saleable GFA since 2004. In 2015, government loosened HPR and lowered down payment ratio, which released demand that have been curbed for 2-3 years. Sales boomed and inventory keep declining. In May 2017, saleable GFA declined by 8.5% yoy, while saleable residential GFA further declined by 17.8% yoy.

Figure 8: Healthy inventory months give room and time window for tightening policies to play out
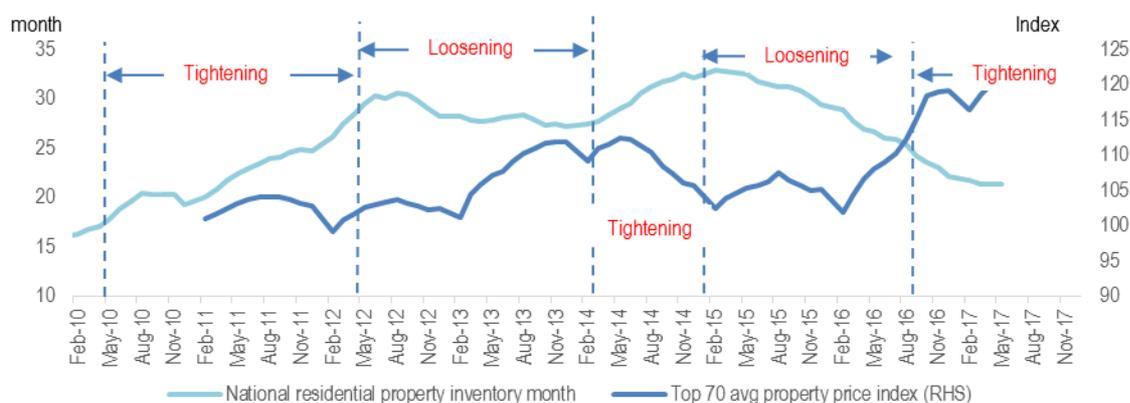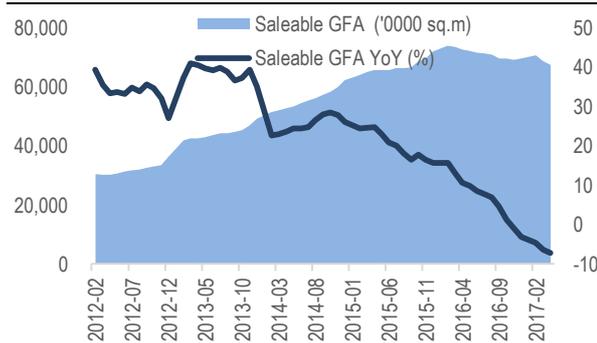

Source: NBS; AMTD Equity Research

Figure 9: saleable residential GFA
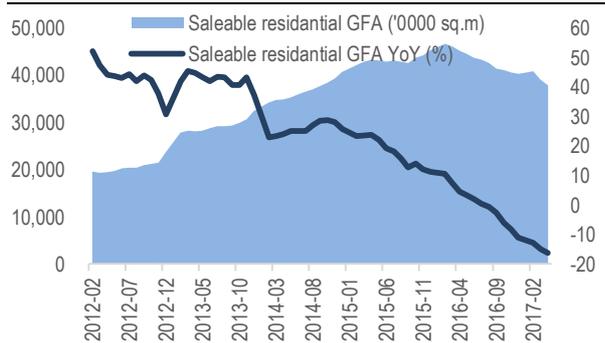
Source: NBS

Figure 10: saleable GFA

Source: NBS

Fierce competition of land auction in 2nd tier cities, more capital flows into 3rd tier cities recently.

According to Wind, the land sold in top 100 cities declined in last four years. Over 50%/40% of GFA sold are contribution from 3rd/2nd tier cities. In terms of value of land sold, 3rd tier cities only contributed 23.2% of total value. 61.9% of total value are contributed by 2nd tier cities.

Before 2015, most of developers were chasing land bank in 1st tier cities. Land auctions became fiercer. Average premium rate of land sold in 1st tier cities is 25.3%. Some developers shifted to 2nd tier cities for better margin. The success of these developers attracted more developers entered 2nd tier and 3rd tier cities, especially satellite cities of 1st tier cities, e.g: Huizhou, Dongguan, Suzhou, Jiaxin and Langfang. Premium rate of land sold in 2nd tier and 3rd tier cities jumped from single digit to over 60%, even over 90%.
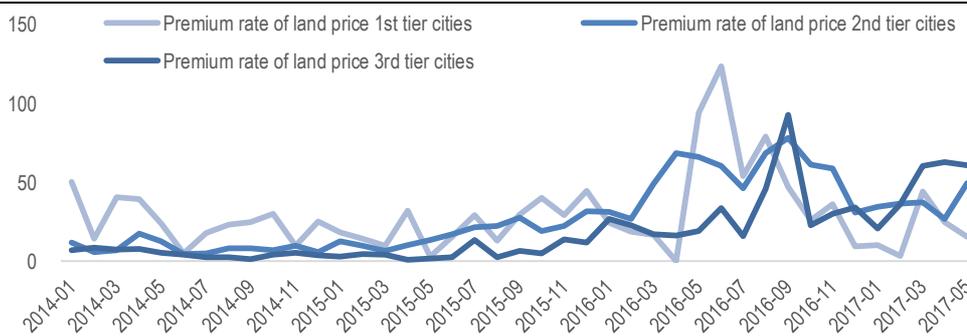
Figure 11: Land sold in 100 cities
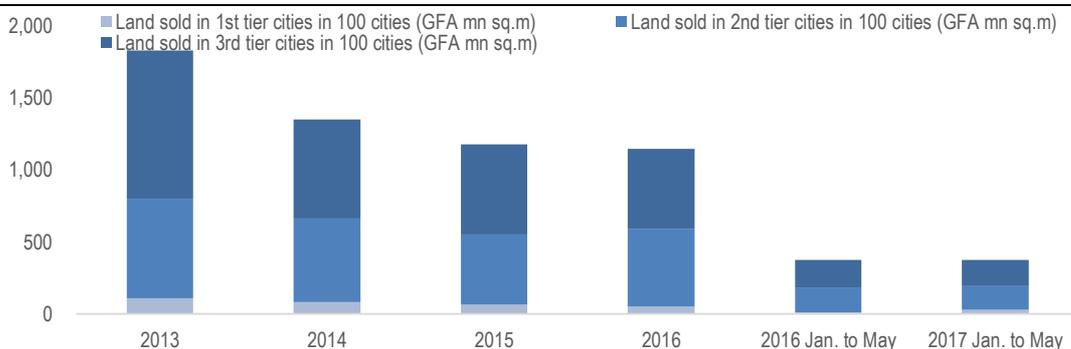
Source: Wind

Figure 12: Value of land sold in 100 cities
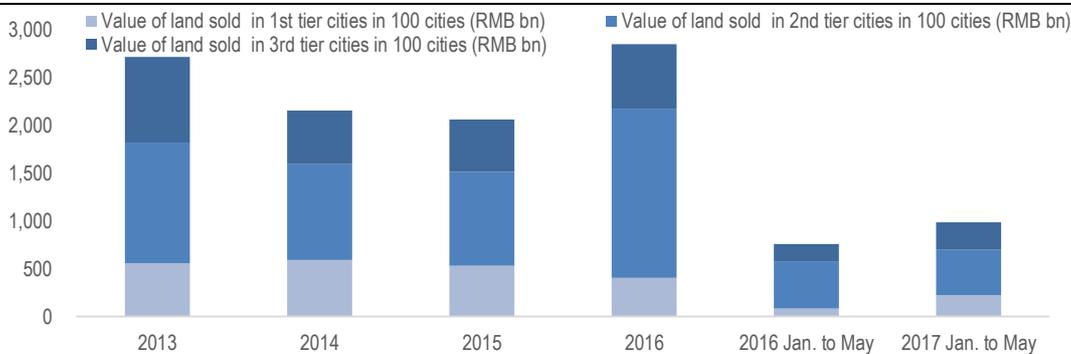
Source: Wind

**Figure 13: Premium rate of land sold in 100 cities**

Source: Wind

Real estate investment come to steady and healthy growth after unreasonable growth in 2011-2013.

Newly commencement always lag behind by GFA sold. Gap between newly commence GFA and GFA sold is narrowing in the last four years. Growth of newly commence GFA are lower than that of GFA sold in 2015/2016/first 5 months of 2017. It indicates 1) Developers are more cautious on commencement, in order to avoid liquidity crisis; and 2) policy uncertainty in the near term.

Figure 14: Newly commence GFA and GFA sold
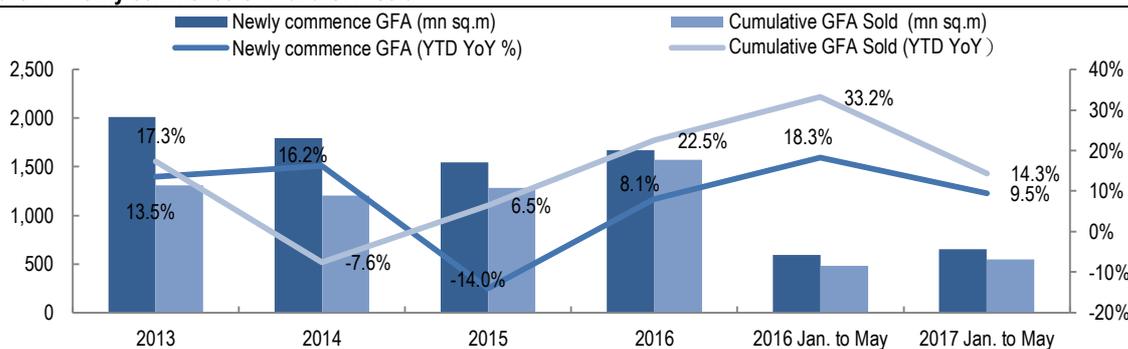
Source: NBS

As more cities introduced HPR in early 2013, growth of GFA sold and completed investment of real estate came to a turning point in 2013. Growth of completed investment declined from 2013 to 2015, bottomed out in 2015, due to loosening of HPR. Although saleable GFA is declining, developers are still cautious on newly commencement. HPR loosening released demands in 2015, meanwhile, home price surged again. Growth of home price is higher than government's expectation in 2016, new round of HPR tightening has come 4Q2016. Policy uncertainty and credit tightening affect developers' confidence.

Figure 15: Completed investment of real estate
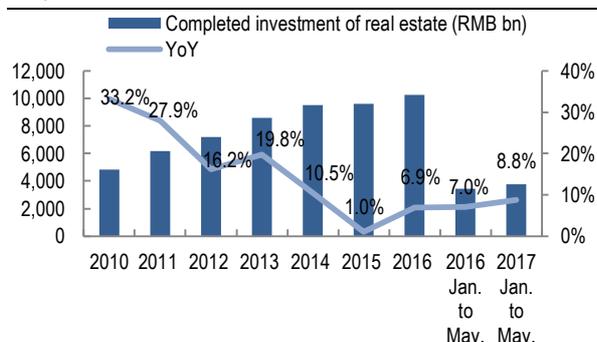
Source: NBS

Figure 16: Completed investment of residence
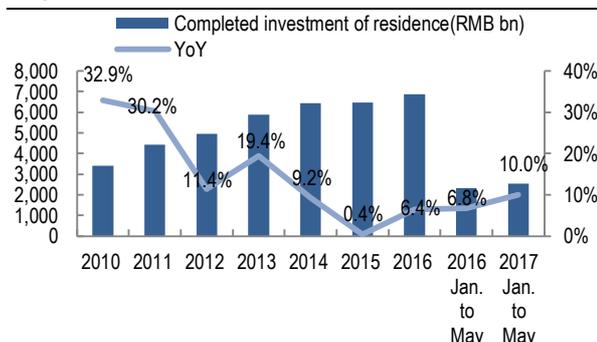
Source: NBS

Consolidators are growing fast

Giants are gaining more market share, which have been priced in share price. However, will share price keep gaining in 2H2017?

Great financial improvement after a loosening year.

Loosening in 2015 and 2016 further released home demand in 2016. Home sales rebounded and home price surged in 2016. All developers have grasped the window period to improve sales performance. Besides, 18 of 29 developers have reduced their net gearing ratio in FY16. The highest reduction is Jingrui, which declined 107 pts of net gearing ratio. In the giants group, COLI and Country Garden reduced their net gearing ratio by 29.4 pts and 34.6 pts. In mid-size group, Times ppty./Sino-ocean/Future Land/ reduced their net gearing ratio by 46.8/20.5/20.4 pts. There are some exceptions, e.g.: Evergrande up 206 pts with very aggressive land acquisitions; Sunac China up 157.7 pts with land acquisitions; R&F up 48.1 pts; Modern Land up 38.8 pts with land replenishment.

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Figure 17: Net gearing ratio comparison				
	Net gearing Ratio			
%	FY2014	FY2015	FY2016	FY14/FY15 Change (pts)	FY15/FY16 Change (pts)
Country Garden	50.6	82.0	47.4	31.4	-34.6
Vanke	6.3	14.5	30.5	8.2	16.1
Evergrande	226.6	260.5	466.7	33.9	206.1
COLI	29.1	38.1	8.6	9.0	-29.4
Sunac	22.1	37.9	195.5	15.7	157.7
Longfor	57.6	55.0	54.1	-2.6	-0.9
CR Land	41.9	33.6	33.3	-8.3	-0.3
CIFI	48.1	54.8	50.7	6.7	-4.2
Shimao	66.9	59.4	52.4	-7.4	-7.0
Greentown	97.7	98.5	91.2	0.8	-7.3
Future Land	64.1	66.9	46.5	2.8	-20.4
R & F Properties	171.2	119.7	167.8	-51.5	48.1
Agile	76.6	62.5	66.4	-14.1	3.9
BJ Capital Land	87.2	112.5	132.4	25.3	19.9
Sino-ocean	58.9	59.0	38.5	0.1	-20.5
Poly Property	113.5	130.4	112.1	16.9	-18.3
Logan	80.3	63.7	76.2	-16.6	12.6
Yuexiu	65.3	75.8	65.8	10.5	-10.0
Jinmao	72.0	64.8	61.4	-7.2	-3.5
Kaisa	431.9	528.7	332.6	96.8	-196.0
COGO	90.4	76.1	71.2	-14.3	-4.9
Times property	146.6	120.2	73.4	-26.5	-46.8
SCE	94.3	89.1	109.1	-5.2	20.0
Aoyuan	105.2	73.7	62.2	-31.6	-11.5
Central China	64.2	43.3	65.5	-20.9	22.1
Powerlong	71.4	67.2	75.4	-4.2	8.2
Modern Land	52.9	76.1	114.9	23.2	38.8
Jingrui	193.7	214.3	107.3	20.5	-107.0
Fantasia	107.6	98.1	96.1	-9.5	-1.9
Source: Bloomberg, companies, AMTD Equity Research					

Booking margins also have improved in FY16

Booking GPM in FY16 have significantly improved. In FY15, only 4 of 29 companies recorded yoy increase of GPM. In FY16, only 7 of 29 companies recorded decline of GPM. Regarding ROE, Country Garden/Vanke/COLI's ROE are over 15%; some mid-size companies have very high ROE: Logan 27.2%, SCE 27.0%, Times ppty. 24.1%, Shimao 20.2%

Figure 18: Profitability comparison

	Gross Margin					Net Income Margin					ROE		
	FY2014	FY2015	FY2016	FY14/FY15 Change	FY15/FY16 Change	FY2014	FY2015	FY2016	FY14/FY15 Change	FY15/FY16 Change	FY2014	FY2015	FY2016
Country Garden	26.1	20.2	21.1	-5.9	0.9	12.1	8.2	7.5	-3.9	-0.7	20.3	15.2	17.0
Vanke	25.1	22.2	25.5	-2.9	3.3	11.4	10.2	9.2	-1.2	-1.0	19.1	19.2	19.7
Evergrande	28.5	28.1	28.1	-0.4	0.0	15.2	11.7	7.4	-3.5	-4.2	25.3	20.5	10.7
COLI	30.0	28.8	28.8	-1.3	0.0	20.8	21.6	23.3	0.8	1.7	22.3	20.2	17.1
Sunac	17.3	12.4	13.7	-4.9	1.3	12.9	14.3	7.9	1.5	-6.5	21.5	18.7	11.7
Longfor	26.5	27.4	29.1	0.9	1.6	16.4	19.0	16.7	2.6	-2.3	19.7	17.5	15.7
CR Land	30.5	31.1	33.7	0.6	2.6	16.9	17.0	17.8	0.2	0.8	15.9	16.0	16.8
CIFI	32.5	28.5	27.6	-4.0	-0.9	14.5	10.6	8.7	-3.9	-1.9	18.3	12.6	10.1
Shimao	25.9	22.7	25.4	-3.1	2.7	11.5	11.7	12.6	0.2	0.9	19.8	18.2	20.2
Greentown	25.4	20.8	20.8	-4.6	0.0	6.5	3.1	6.6	-3.3	3.5	7.1	2.2	7.9
Future Land	18.7	20.4	23.4	1.7	3.0	5.0	4.3	4.9	-0.6	0.6	14.3	13.0	15.9
R & F Properties	35.4	32.1	28.3	-3.3	-3.8	20.9	15.2	13.1	-5.7	-2.1	15.5	12.2	16.0
Agile	32.4	25.1	26.5	-7.3	1.3	12.1	4.1	5.8	-8.0	1.7	13.6	4.1	6.6
BJ Capital Land	25.0	12.1	10.8	-13.0	-1.2	18.0	14.0	10.7	-4.0	-3.2	19.0	17.0	12.7
Sino-ocean	21.0	20.6	22.1	-0.4	1.5	11.8	7.7	11.0	-4.1	3.3	11.1	5.2	8.7
Poly Property	19.8	11.5	16.3	-8.3	4.8	3.3	-10.8	0.5	-14.0	11.3	3.1	-10.2	0.3
Logan	30.4	30.4	31.9	0.0	1.5	18.8	18.2	21.9	-0.6	3.7	25.3	21.4	27.2
Yuexiu	26.4	21.1	20.8	-5.3	-0.3	15.7	4.6	7.4	-11.2	2.8	9.3	3.4	5.1
Jinmao	39.1	38.7	37.4	-0.5	-1.3	17.9	17.1	9.3	-0.8	-7.9	17.1	12.2	7.9
Kaisa	14.6	3.1	13.0	-11.5	9.9	-6.6	-10.3	-3.4	-3.7	6.8	-8.3	-8.0	-4.6
COGO	24.1	15.6	17.2	-8.4	1.5	9.1	5.1	5.3	-3.9	0.1	10.7	7.3	8.3
Times property	30.6	26.0	26.2	-4.6	0.2	12.3	10.4	12.1	-1.9	1.6	27.1	22.7	24.1
SCE	34.9	28.2	25.0	-6.7	-3.1	13.1	10.9	17.0	-2.2	6.1	14.7	13.6	27.0
Aoyuan	29.6	27.6	27.7	-2.0	0.1	11.6	8.5	7.4	-3.1	-1.0	10.8	10.2	10.3
Central China	33.6	22.2	24.1	-11.4	2.0	9.6	6.4	4.2	-3.2	-2.1	14.2	12.1	6.1
Powerlong	28.8	32.9	33.4	4.1	0.5	14.6	18.7	18.3	4.1	-0.4	7.7	10.6	11.4
Modern Land	40.6	30.9	19.5	-9.6	-11.5	12.8	9.1	7.9	-3.7	-1.2	19.5	17.4	15.8
Jingrui	18.3	3.0	4.1	-15.3	1.0	5.2	-5.3	1.2	-10.5	6.4	8.1	-10.0	3.2
Fantasia	38.4	30.9	32.3	-7.6	1.5	17.8	15.6	7.7	-2.2	-7.9	14.9	12.2	7.5

Source: Bloomberg, companies, AMTD Equity Research

Sales performances of listed developers are unexpectedly good.

Although sales data breakdown by cities shows that the property sales growth slowed down, it is surprising that listed developers' performances are unexpectedly good. 5 companies have achieved over 50% of their target. Longfor even achieved 69% of its target. **Developers mainly in 3rd tier cities, Evergrande, Country Garden and COGO, achieved RMB183 bn, RMB224 bn and HKD13 bn in first 5 months of 2017, representing 75.9% yoy, 30.9% yoy and 126.5% yoy. We believe there are some positive factors in 3rd cities: 1) less tightening on pre-sales price approval, 2) lower home price with lower risk control for commercial banks, 3) destocking in 3rd tier cities and no HPR in most of 3rd tier cites.**

Figure 19: Sales target achievement in Jan. to May 2017

Source: Company data; AMTD Equity Research

Giants, Vanke & COLI, whose core assets locate in 1st and 2nd tier cities, achieved RMB228 bn and HKD83 bn, down by 1.3% and 0.6% yoy. Sunac/Longfor/CR Land are catching up with COLI, which achieved RMB80 bn /76 bn/53 bn, representing 91%/54%/49% yoy growth.

Figure 20: Sales comparison of over RMB20 bn sales in Jan. to May 2017
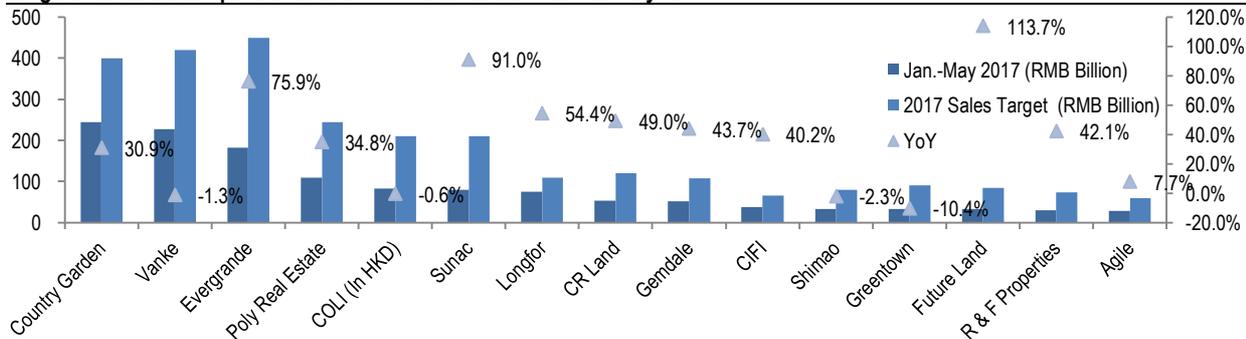
Source: Company data; AMTD Equity Research

In the group of below RMB20 bn sales, all of listed developers recorded moderate yoy growth, from 8% to 35%.

Figure 21: Sales comparison of below RMB20 bn sales in Jan. to May 2017
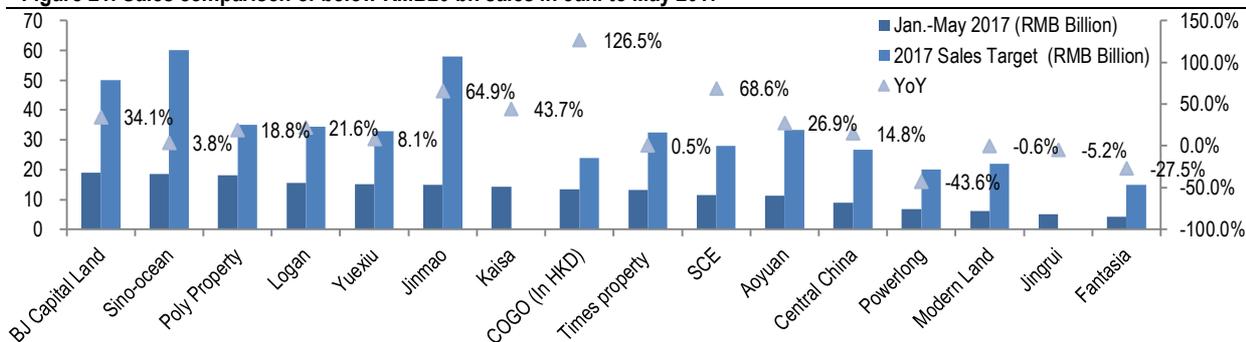
Source: Company data; AMTD Equity Research

Sector leaders preformed much better than smaller developers. Market concentration accelerates and sales scale become the key of developers. **The era of oligopoly has come. Top 20 companies accounted for 25.2% of total sales of commercial house in China. Top 100 companies accounted for 44.8% of total sales in China. 21-100 ranking companies only accounted for 19.6% of total sales.** In first 5 months of 2017, top 20 accounted for 59.6% of total sales, top 100 accounted for 37.1% of total sales, 21-100 ranking companies only accounted for 22.5%. Leaders will enjoy lower interest cost, higher pricing power with strong brand premium and more co-operating opportunities. **In current market environment. We believe in currently situation, more saleable resource in 3rd tier cities and satellite cities of 1st tier cities should have better sales performance.**

Figure 22: % of Top 20 &100 sales of total home sales in China
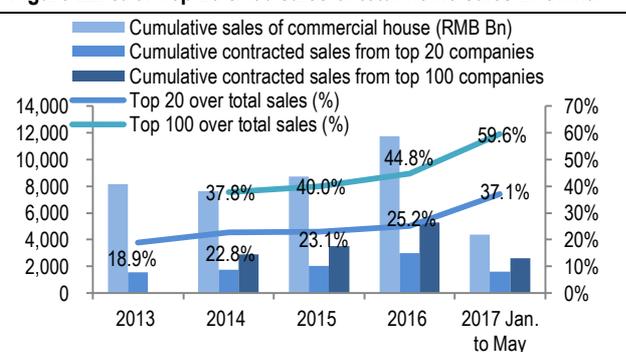
Source: Company data; CRIC, NBS

Who have got too much land bank?

Low land bank year doesn't mean low growth potential; oppositely, it means health turnover rate and better sales performance. However, if land bank year is longer than 5 years that would be a signal that the companies have acquired too many land plot without development abilities. Giants usually have 4.1-5.1 of land bank year, as high turnover. Holding too many land bank will have more interest cost (most companies acquired land by leverage). However, if the land bank year is lower than 2.5 years that would be a hint that the companies face sustainable development issue.

Companies with high land bank year always go with high net gearing ratio, because **inventories have not been converted to profit effectively**. If we assume home price unchanged but growth maintains, more GFA will be sold, how will the land bank year be? Giants will have 3.4-4.3 years. Sunac still has 7.3 years. Expected land bank year of Greentown/R&F/Jinmao/Powerlong/Fantasia are higher than 7 years. We still believe 3-5 year should be comfort room for developers, good for balance sheet and lower interest cost in tightening policy and credit environment.

Figure 23: Land bank comparison

| ('000 sq.m.)	Land bank as of Dec 2016	Land acquired in 2016	GFA Sold	Land bank year	Expected growth of sales	Expected GFA sold in 2017	Land bank year (under expected sales)
Country Garden	166,040	87,520	37,827	4.4	29.5%	48,989	3.4
Vanke	112,840	31,570	27,654	4.1	15.3%	31,877	3.5
Evergrande	229,000	102,380	44,690	5.1	20.5%	53,864	4.3
COLI	56,770	9,716	13,358	4.2	8.1%	14,441	3.9
Sunac	72,913	47,730	7,267	10.0	37.0%	9,956	7.3
Longfor	41,475	12,549	5,947	7.0	24.8%	7,422	5.6
CR Land	44,845	10,520	7,806	5.7	20.7%	9,420	4.8
Shimao	30,790	3,965	4,916	6.3	22.6%	6,028	5.1
CIFI	17,500	6,500	3,691	4.7	17.4%	4,335	4.0
Greentown	45,570	2,282	6,245	7.3	-6.1%	5,867	7.8
Future Land	35,320	14,242	5,949	5.9	36.2%	8,102	4.4
R & F Properties	42,965	5,041	4,917	8.7	20.0%	5,900	7.3
Agile	32,600	2,320	5,407	6.0	13.6%	6,143	5.3
BJ Capital Land	11,120	1,660	2,205	5.0	9.8%	2,422	4.6
Sino-ocean	21,699	4,765	2,702	8.0	19.1%	3,218	6.7
Poly Property	19,000	1,230	2,788	6.8	0.3%	2,796	6.8
Logan	14,090	1,966	3,201	4.4	20.2%	3,847	3.7
Yuexiu	9,660	4,210	2,560	3.8	9.1%	2,793	3.5
Jinmao	35,825	6,211	2,388	15.0	54.8%	3,697	9.7
Kaisa	21,300	1,622	2,269	9.4	n.a.	n.a.	n.a.
COGO	17,741	1,353	2,674	6.6	-0.1%	2,672	6.6
Times property	13,064	3,438	2,714	4.8	10.8%	3,008	4.3
SCE	9,100	1,680	1,797	5.1	19.0%	2,139	4.3
Aoyuan	14,650	3,140	2,966	4.9	30.1%	3,858	3.8
Central China	20,920	1,510	3,017	6.9	33.0%	4,013	5.2
Powerlong	13,200	3,823	1,508	8.8	13.4%	1,710	7.7
Modern Land	5,403	2,080	1,436	3.8	32.9%	1,908	2.8
Jingrui	3,023	986	1,353	2.2	n.a.	n.a.	n.a.
Fantasia	14,976	n.a.	1,325	11.3	22.9%	1,629	9.2

Source: Bloomberg, Company data

Be cautious on giants, look for safe margin after consolidators gained more YTD

We expect the property sector valuation to de-rate in 2H17. We selectively overweigh developers with achievable presales growth, less share price gain YTD, and relatively low valuation. We are cautious on developers with big share price gains YTD, as main consolidators, Evergrande and Country Garden performed very well YTD, up 187% and 106%. Thanks to the rapid growth of contracted sales in 3rd tier cities. Sunac also gained 137% YTD. Future Land and COGO have rapid growth of contracted sales in Jan. to May 2017, which have priced in the share price as well. As HPR continues, sales performance is expected to be affected, high yoy growth in first 5 months in 2017 might not happen again in 2H2017. Sales in 1st /2nd cities are expected to slow down, sales in 3rd tier cities and satellite cities of 1st tier cities expected to keep robust in 2H2017. **However, positive factors of 3rd tier cities have been priced in share price of Evergrande/ Country Garden/ COGO.**

Or we should look at some names with low valuation, lower gain YTD, high growth potential, high ROE and moderate dividend yield. Currently, new round of HPR has started, we haven't seen HPR influence on valuation. Moreover, if home sales slows down, we should choose some defensive names in foreseeable downtrend of valuation. **The current P/E of property sector is about 8.3x, approaching their highs in 2015 and in 2012. We look back to 6 year ago, the hardest time in 2011, the market cap weighted P/E of property sector was only 3.9x. Giants and 3rd tier cities players with 8x P/E and over 50% gain YTD should be avoided. On the other hand, names with low P/E & P/B, 15% ROE and high dividend yield should be have higher safety margin and attractive for long-only funds.**

Figure 24: Market cap weighted PE vs. Home price indices mom
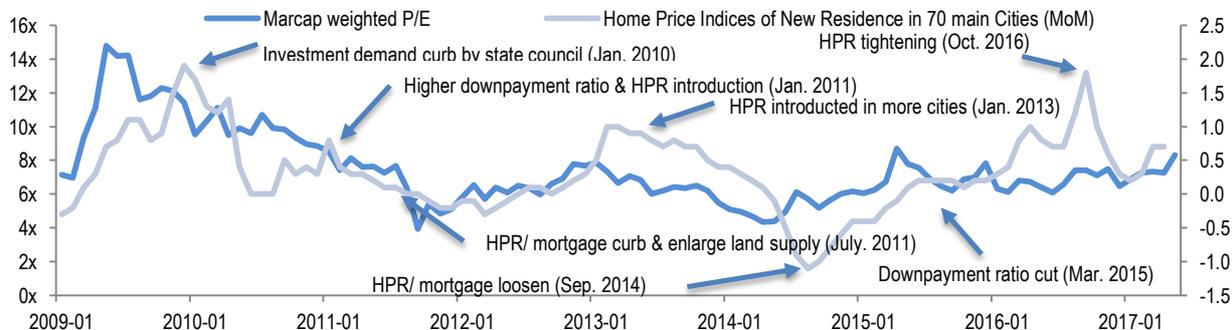
Source: Bloomberg; NBS; AMTD Equity Research

Figure 25: Share price gain comparison
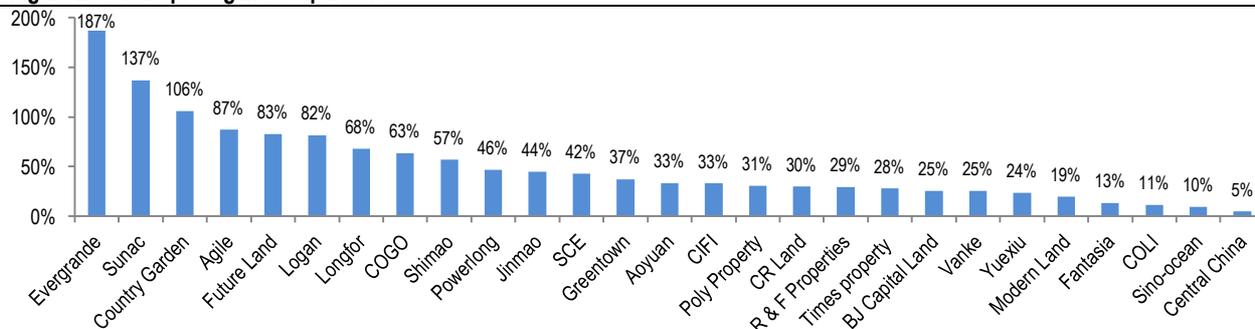
Source: Bloomberg; NBS; AMTD Equity Research

Figure 26: Peers comparison

Company	Currency	Mkt Cap (million)	Last price (HKD)	PER			PB			D/Y%	ROE (%)
				17F	18F	19F	17F	18F	19F	17F	17F
Country Garden	HKD	190,785	8.94	11.6	9.1	7.0	2.0	1.7	1.3	2.7	19.2
Vanke	HKD	312,305	22.20	8.4	7.2	6.5	1.6	1.4	1.3	4.9	20.8
Evergrande	HKD	182,450	13.94	13.0	8.6	6.6	2.7	2.1	1.6	4.3	21.6
COLI	HKD	249,801	22.80	7.2	6.4	5.8	1.0	0.9	0.8	3.6	14.6
Sunac	HKD	60,067	15.40	18.7	10.4	7.2	2.0	1.8	1.5	1.8	9.4
Longfor	HKD	97,245	16.56	8.9	7.7	6.5	1.2	1.1	1.0	3.7	14.9
Cr Land	HKD	156,986	22.65	8.2	7.1	6.3	1.2	1.0	0.9	3.5	15.6
CIFI	HKD	45,589	13.46	5.9	5.1	4.5	0.7	0.6	0.6	6.1	12.1
Shimao	HKD	22,421	3.29	5.4	4.4	3.7	1.1	0.9	0.8	6.7	21.8
Greentown	HKD	18,583	8.59	8.7	7.9	7.6	0.6	0.6	0.5	2.0	6.6
Future Land	HKD	16,408	2.90	8.1	5.6	4.8	1.3	1.1	0.9	3.3	21.4
R & F	HKD	38,991	12.10	4.6	4.2	3.8	0.7	0.6	0.6	9.1	15.7
Agile	HKD	27,811	7.10	6.6	5.8	5.2	0.6	0.6	0.5	6.2	9.2
BJ Capital Land	HKD	11,052	3.65	5.7	4.1	n.a.	0.6	0.6	n.a.	6.6	19.3
Sino-Ocean	HKD	28,333	3.77	6.7	5.8	5.1	0.5	0.5	0.5	5.9	8.4
Poly Property	HKD	12,303	3.36	33.3	19.3	15.6	0.5	0.5	0.5	0.4	1.4
Logan	HKD	29,350	5.34	6.2	4.7	4.0	1.2	1.0	0.9	5.7	18.8
Yuexiu	HKD	16,246	1.31	8.7	7.4	6.9	0.4	0.4	0.4	4.9	5.2
Jinmao	HKD	32,337	3.03	8.9	7.4	6.5	0.8	0.8	0.7	4.4	10.3
COGO	HKD	9,448	4.14	6.2	5.3	4.5	0.7	0.7	0.6	1.0	13.4
Times Property	HKD	8,412	4.83	3.4	2.5	2.5	0.7	0.6	0.5	9.3	21.9
SCE	HKD	11,436	3.34	6.2	4.7	3.6	1.0	0.9	0.7	5.0	17.8
Aoyuan	HKD	6,171	2.31	4.2	3.3	2.7	0.5	0.5	0.4	9.1	14.5
Central China	HKD	4,298	1.76	3.6	2.7	3.3	0.5	0.4	0.4	8.0	15.0
Powerlong	HKD	13,391	3.35	4.8	4.1	3.8	0.5	0.4	0.4	5.7	10.8
Modern Land	HKD	3,079	1.23	3.1	2.8	2.5	0.4	0.5	0.4	8.5	18.6
Fantasia	HKD	6,396	1.11	6.9	5.1	4.2	0.5	0.5	0.4	5.2	6.9
Median				6.7	5.6	5.0	0.7	0.6	0.6	5.0	14.9
Simple Average				8.3	6.3	5.4	0.9	0.8	0.7	5.1	14.3
Weighted Average				9.2	7.3	6.1	1.4	1.2	1.0	4.2	16.7

Source: Bloomberg; AMTD Equity Research
Note: As of 29 June 2017

IMPORTANT DISCLOSURES

Analyst Certification

We, Donald Yu 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 Asset Management Limited.

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GENERAL DISCLOSURES