

# Franshion Properties (817 HK)

Share Price: HKD2.37

MCap (USD): 2.8B

China

Target Price: HKD3.32(+40%)

ADTV (USD): 2M

Real Estate

# BUY

(New)

## Buy one get one free; Initiate BUY

- Initiate at BUY with TP of HKD3.32. Key catalysts are our forecast of above-sector average sales growth and potential spin-off of the investment property (IP) portfolio.
- Strong sales growth from property development and maturing primary development projects in Changsha to boost revenue and core profit growth in 2013-15 by 30% and 27% CAGR.
- Market cap of the new entity of IP portfolio following spin-off could reach HKD19b, almost 90% of Franshion's market cap!

### What's New

We dubbed 2014 as the 'Year of Harvest' for Franshion's property development arm as it should surpass the CNY20b sales mark! We forecast Franshion's 2014 sales to increase by another 33% YoY, above the estimated sector average of 20-25%. This is following Franshion's 35% YoY sales growth for 2013.

Another major catalyst is the potential spin-off of the IP portfolio will unlock the intrinsic value. Assuming gross rental of HKD3.5b for the IP portfolio (which comprises only ~1/3 of Franshion's GAV), 35% net distributable income margin and 6.5% yield, the market cap of the new entity could reach ~HKD19b or close to 90% of its current market capitalisation!

### What's Our View

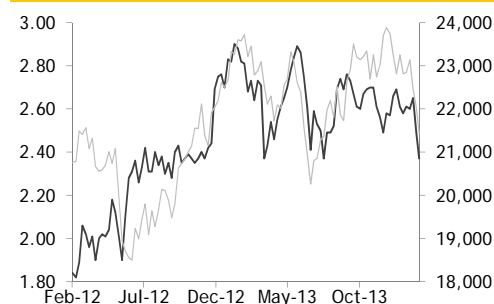
Franshion should trade at a premium to its peers given the two-fold re-rating story of: (i) high sale-through rate with high sales growth (narrows NAV discount to 45%); and (ii) asset-value realization from potential spin-off (further narrows NAV discount to 40%). We expect its strong earnings growth to continue in 2014-15F with GPM staying at ~40%. Initiate at BUY with TP of HKD3.32, representing 40% discount to NAV compared with peers' average at 54%. Our TP translates to 9.4x 2014 PER, 7.3x 2015 PER and 0.7x 2014 book value. Our 2013 and 2014 earnings forecasts are generally in line with consensus but we are more bullish on our 2015 earnings outlook (9% above on 2015 revenue and 7% above on underlying core profit).

FYE Dec (HKD m)	FY11A	FY12A	FY13E	FY14E	FY15E
Revenue	6,591.7	17,175.7	21,058.6	28,800.7	35,452.6
EBITDA	2,619.0	6,145.0	7,490.8	9,694.1	11,606.2
Core net profit	1,341.0	2,077.9	3,076.9	3,802.0	4,947.7
Core FDEPS (HKD)	0.12	0.19	0.28	0.35	0.46
Core FDEPS growth(%)	10.7	54.9	48.1	23.6	30.1
Net DPS (HKD)	0.04	0.07	0.09	0.11	0.14
Core FD P/E (x)	19.1	12.3	8.3	6.7	5.2
P/BV (x)	1.0	0.9	0.7	0.6	0.6
Net dividend yield (%)	1.7	2.9	3.6	4.5	5.8
ROAE (%)	5.1	6.4	8.5	9.4	10.9
ROAA (%)	2.2	2.7	3.6	4.1	5.0
EV/EBITDA (x)	11.7	7.5	6.3	5.2	4.4
Net debt/equity (%)	48.2	51.3	59.6	60.2	50.9

### Key Data

52w high/low (HKD)	2.91/2.22
Free float (%)	37.1
Issued shares (m)	9,161
Market capitalization	HKD21.7B
Major shareholders:	
-Sinochem Hong Kong (Group) Co. Ltd	63%
-GIC Pte Ltd.	5%
-Warburg Pincus LLC	2%

### Share Price Performance



— Franshion Properties (L) — Hang Seng Index (R)

	1 Mth	3 Mth	12 Mth
Absolute(%)	(3.7)	(11.2)	(12.2)
Relative to country (%)	2.0	(4.5)	(4.7)

### Maybank vs Market

	Positive	Neutral	Negative
Market Recs	9	3	0
Maybank Consensus			% +/-
Target Price (HKD)	3.32	3.62	(8.2)
2013 PATMI(HKDm)	3,077	3,193	(3.6)
2014 PATMI(HKDm)	3,802	3,808	(0.1)

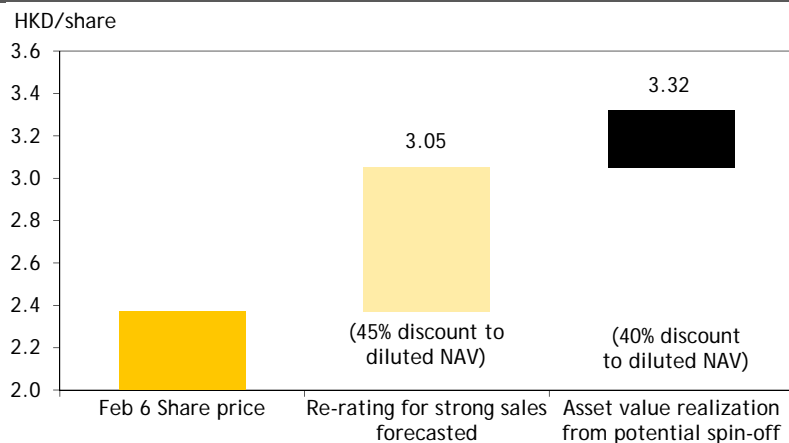
Source: FactSet, Maybank Kim Eng

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## Key things to know

Figure 1: Two-fold re-rating story for strong sales growth and potential asset value realization via spin-off



Source: Company data, Maybank Kim Eng

We believe Franshion should trade at a premium to the sector average given a two-fold re-rating story of strong sales growth and asset-value realization from the potential spin-off.

Figure 2: Another 33% YoY growth in sales in 2014F!

Year	Residential and commercial sales (CNY b)	Primary land sales (CNY b)	Total (CNY b)	YoY (%)
2010	~10	0.0	~10.0	NA
2011	~10	2.7	~12.7	27
2012	~10.5	5.0	~15.5	22
2013	14.6	6.4	21.0	35
2014F	~20.5	~7.5	~28	33

Source: Company data, Maybank Kim Eng

We expect 2014 will be a 'Year of Harvest' for Franshion's property development arm. We forecast its residential and commercial property sales to grow 40% YoY. Including primary land sales, we expect Franshion to achieve CNY28b in total sales, up 33% growth YoY, ahead of peers' average growth of 20 – 25%.

Figure 3: Market value of new entity of the potential spin-off ... almost ~88% of current Franshion's market cap (HK b)

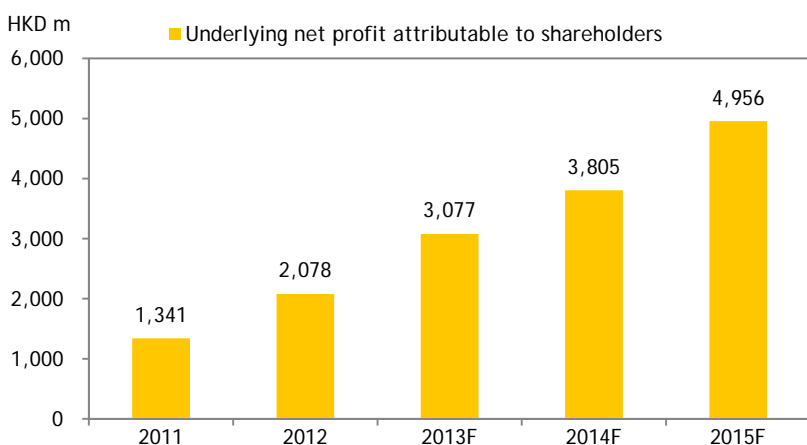
Required yield	Net distributable income margin				
	30.0%	32.5%	35.0%	37.5%	40.0%
6.00%	17.5	19.0	20.4	21.9	23.3
6.25%	16.8	18.2	19.6	21.0	22.4
6.50%	16.2	17.5	18.8	20.2	21.5
6.75%	15.6	16.9	18.1	19.4	20.7
7.00%	15.0	16.3	17.5	18.8	20.0

\* Based on gross rental income estimates of HKD3.5b

Source: Company data, Maybank Kim Eng estimates

Based on our assumption of HKD3.5b gross rental income for the IP portfolio that is likely to be spun off, 35% net distributable income margin and 6.5% required yield, the estimated market cap of the new entity could reach HKD18.8b, which is ~88% of Franshion's current market cap of ~HKD21.7b.

Figure 4: Strong core profit growth: 2011-2015 CAGR at 38.6%



Source: Company data, Maybank Kim Eng

Supported by robust growth in sales of both developments and primary land, we expect Franshion will enjoy strong growth in revenue and core profit for 2013 to 2015.

## Robust sales growth in FY14F

### Strong sales track record- but 2014 is the year for Franshion to break through the CNY20b property sales mark

Franshion started to expand its property development business in 2009 and it has reaped strong sales growth in sales since 2011. Contract sales (including land sales) achieved in 2010|2011|2012|2013 were about CNY10bn|12.7bn|15.5b|21b respectively, representing a 28% CAGR growth per annum. Drivers for the high growth include: (i) increased number of projects for sale (from only 2 projects in 2010 to ~10 major projects in 2013); (ii) sustaining high sale-through of ~85% along with the increase in saleable resources helped by good product layouts and “Jinmao” brand name; and (iii) additional contributions from Changsha land sales from the Meixi Lake primary development since 2011.

### Saleable resources in 2014 to rise 44% YoY

For residential and commercial developments, Franshion has acquired 13 new projects from 2012 to 2013 (seven in 2012 and six in 2013) with a total planned GFA of 3.6m sq m. Only two out of these new new projects were launched in 2013. We expect at least five new projects will be launched for pre-sales in 2014, which will bring total saleable resources (excluding primary land sales) for 2014 to ~CNY26b, implying an increase of ~44% YoY versus an estimated CNY18b of saleable resources in 2013.

Leveraging the reputable Jinmao brand from its initial office assets (Shanghai Jinmao Tower), we expect Franshion can continue to achieve a sale-through rate of ~80% which should translate to an estimated figure of ~CNY20.5b of property sales for 2014.

Figure 5: Breakdown of sales from 2010 to 2013 (CNY b)

Year	Residential and commercial sales	Primary land sales	Total	YoY (%)
2010	~10	0.0	~10.0	NA
2011	~10	2.7	~12.7	27
2012	~10.5	5.0	~15.5	22
2013	14.6	6.4	21.0	35
2014F	~20.5	~7.5	~28	33

Source: Company data, Maybank Kim Eng

Figure 6: Potential new project launches in 2014

Project	City	Total planned GFA (sq m)
Changsha Meixi Lake International Plaza	Changsha	370,000
Changsha Jinmao Residence	Changsha	382,190
Beijing Yizhuang Project	Beijing	298,783
Suzhou Jinmen Road Project	Suzhou	258,053
Lijiang Noble Manor	Lijiang	92,500

Source: Company data, Maybank Kim Eng

### **Primary development land sales enter new era**

**CNY13b Changsha project cost already recovered.** We believe Franshion can leverage its experience and success from the Changsha Meixi Lake primary development and extend into other primary development projects. Since the project was launched in 2011, the accumulated land sales up to 2013 reached ~CNY14.1b which more than covered the full CNY13b cost of the entire project.

**Jump in margins.** Franshion achieved land sales of CNY6.4b and GFA of 2.13m sq m in 2013, representing an AV of CNY3,012/sq m. Looking back to 2011 and 2012, the transacted prices were only ~CNY2,000/sq m. We believe the margin has been significantly improved comparing to the costs of only at CNY1,500/sq m.

We expect the existing Changsha Meixi Lake primary development projects will contribute land sales of ~CNY5b in 2014. Two new land development projects, a new phase of the Changsha Meixi primary land development and a project in Sanya Yazhou Bay (~1,500 mu land with cost at ~CNY1mn/mu and expected ASP at ~CNY3mn/mu), are also expected to be ready for land sales in 2014, which potentially could contribute an additional ~CNY2.5b in sales, bringing total land sales to around CNY7.5b. We estimate the GPM for the Sanya primary land development to be around 40%. Having said that, one of the risks of primary land development is potential uncertainty in the timing of the launch of land for sale - as it is partly driven by the local government.

### **33% sales growth expected in 2014 - putting it ahead of peers**

All in all, total 2014 sales including sales from property development and primary land development will total ~CNY28b, representing a 33.3% growth YoY. This would put Franshion's YoY contract sales growth for 2014 ahead of our China property coverage list's estimated 20-25% growth.

## Strong recurring income, one of the biggest China landlords

### Reputable Jinmao brand in Shanghai

Franshion currently owns 4 completed office/retail buildings with total leasing floor area of 350,000 sq m. Two are located in Beijing, one in Shanghai and one in Nanjing. The portfolio includes the landmark skyscraper Jinmao Tower in Shanghai, which was the tallest building in China from 1998 to 2007 until the completion of Shanghai WFC. Franshion also owns seven completed five-star hotels with 3,106 rooms located in Beijing, Shanghai, Shenzhen, Sanya and Nanjing. Looking solely at its investment properties (IPs), Franshion's total revenue from hotels and office/retail space reached HKD1.67b in 1H13. On an annualized basis, this should rank Franshion at no. 4 rank among HK-listed China developers, landlords and REITs (Figure 7).

### 800k sq m of IPs and four hotels in the pipeline, rental to rise ~70% from here when fully ramped up by 2017/18

In addition to the current 350,000 sq m of IPs and seven hotels, Franshion has an additional 800k sq m of IPs and four hotels under construction, which it expects to be completed by end of 2016. With these IPs and hotels becoming more mature and revenue ramping up, we expect the total revenue from IPs and hotels will finally increase from ~HKD3.5b to ~6.0b per annum, or up ~70%.

Figure 7: Revenue from IPs and hotels HK-listed landlord, REITs and developers in China

	1H13 Revenue (***HKD b)	Full year reported or annualized figures (***HKD b)
Shangri-La Asia	2.97	5.94
CR Land **	2.52	5.35
Hang Lung Prop	3.53 (Full year 12/13)	3.53
<b>Franshion</b>	<b>1.67</b>	<b>3.34</b>
Hui Xian REIT	1.67	3.34
Wharf*	1.22	2.44
Sun Hung Kai Prop	2.35	2.35
GZ R&F**	0.95	2.15
Shui On Land	0.91	1.81
Swire Prop	0.85	1.70
Yuexiu REIT	0.81	1.62
Kerry Properties	0.66	1.33
SOHO China	0.11	0.22

\* Derived by revenue from China minus property sales in China

\*\* Forecasted by Maybank Kim Eng

\*\*\* Exchange rate adopted: HKD1 = CNY0.79, USD1 = HKD7.76

Source: Company data, Maybank Kim Eng

Figure 8: Franshion's completed investment properties

Building	Location	Leasable GFA (sq m)	1H13 Revenue (HKD m)	1H13 Occupancy rate (%)
Beijing Chemsunny World Trade Centre	Beijing	110,760	279.8	99
Sinochem Tower	Beijing	38,202	50.7	100
Jinmao Tower (office + retail)	Shanghai	145,117	268.8	97
Nanjing International Centre Phase 1 (office + retail)	Nanjing	56,662	29.2	95*
<b>TOTAL</b>		<b>350,741</b>	<b>628.5</b>	

\* Occupancy rate refers to office only for Nanjing International Centre Phase 1

Source: Company data, Maybank Kim Eng

Figure 9: Franshion's completed hotels

Hotel	Location	No of rooms	1H13 Revenue (HKD m)	Occupancy (%)	Average room rate (CNY)
Grand Hyatt	Shanghai	555	256.9	57	1,673
Hilton	Sanya	501	176.0	65	1,947
Ritz-Carlton	Sanya	450	273.8	68	3,126
Westin	Beijing	550	186.4	67	1,458
Wangfujing Grand Hotel*	Beijing	405	na	na	na
JW Marriott	Shenzhen	411	106.1	75	1,047
Nanjing Westin	Nanjing	234	42.8	64	848
<b>TOTAL</b>		<b>3,106</b>	<b>1,042.0</b>		

\* Beijing Wangfujing Grand Hotel has been closed for refurbishment since 2H2011.

Source: Company data, Maybank Kim Eng

Figure 10: Franshion's IPs and hotels under construction

Office / Retail	Location	Type	Total GFA (sq m)	Interest (%)	Planned completion
Shanghai International Shipping Service Center	Shanghai	Retail	17,927	50	2015
Shanghai International Shipping Service Center	Shanghai	Office	78,303	50	2015
Shanghai Haimen Road #55 Plot	Shanghai	Retail	109,964	50	2016
Shanghai Haimen Road #55 Plot	Shanghai	Office	193,500	50	2016
Nanjing International Centre Phase II	Nanjing	Retail	48,500	51	2016
Nanjing International Centre Phase II	Nanjing	Office	72,200	51	2016
Meixi Lake International Plaza	Changsha	Retail	99,000	100	2016
Meixi Lake International Plaza	Changsha	Office	55,000	100	2016
Changsha R&D Office Centre	Changsha	Office	14,996	80	2016
Qingdao Jinmao Harbour	Qingdao	Retail	97,268	100	2016
Lijiang Jinmao J-Life	Lijiang	Retail	12,990	100	2014
<b>TOTAL</b>			<b>799,648</b>		

Hotel	Location	No. of planned rooms	Total GFA (sq m)	Interest (%)	Planned completion
Grand Hyatt	Lijiang	381	82,700	100	2014
Hyatt	Shanghai	223	49,378	100	2014
St. Regis	Nanjing	200	23,500	51	2016
Meixi Lake International Plaza Hotel	Changsha	350	39,000	100	2016
<b>TOTAL</b>		<b>1,154</b>	<b>194,578</b>		

\* Beijing Wangfujing Grand Hotel has been closed for refurbishment since 2H2011.

Source: Company data, Maybank Kim Eng

## Potential spin-off of IP - Buy one get one free!

Many China property developers and landlords are trading at a significant discount to NAV (sector's average at ~54%). Many peers can only unlock the intrinsic value of their IPs by en-bloc disposal due to limitations of size of matured portfolio. Franshion is not under this limitation and it should be able to unlock value via spin-off.

In addition to only look at sales growth, some investors nowadays are interested in stocks with corporate restructuring stories that can help to unlock the intrinsic value of underlying assets, such as asset injections from parents of COLI and CR Land or Shui On Land's spin-off of its IPs.

We believe the potential spin-off of assets by Franshion will not only provide an opportunity to unlock the intrinsic value of its IPs but also provide an additional funding channel. Furthermore, with the proceeds from the spin-off, Franshion can speed up the pace of construction (more saleable resources), replenish more landbank and fund the capex for further primary development projects.

Disregarding any upcoming IP to be completed in the pipeline, the current completed IP portfolio (including offices, retail space and hotels in Figure 8 and 9) can generate gross annual rentals of about HKD3.5b. Assuming a net distributable income margin of 35 - 40% (HKD1.225b - 1.4b) and required distribution yield of 6-7%, the market value of the new entity would represent a market cap of HKD17.5n to 23.3b, which is almost 90% of Franshion's current market capitalization of HKD21.7b.

Assuming Franshion will hold 40% of the spun-off company, then the money raised in the capital markets, assuming an IPO (not a distribution by species), would be around HKD10.5-14b. There could also be a scenario where the actual spun off portfolio includes less than the entire completed IP portfolio or to it includes some upcoming IPs under construction. We estimate the timing of the spin-off to occur in 1H2015.

Figure 11: New entity market cap sensitivity analysis (HK b) for the spin-off

Required yield	Net distributable income margin				
	30.0%	32.5%	35.0%	37.5%	40.0%
6.00%	17.5	19.0	20.4	21.9	23.3
6.25%	16.8	18.2	19.6	21.0	22.4
6.50%	16.2	17.5	18.8	20.2	21.5
6.75%	15.6	16.9	18.1	19.4	20.7
7.00%	15.0	16.3	17.5	18.8	20.0

\* Based on gross rental income estimates of HKD3.5b

Source: Company data, Maybank Kim Eng estimates



## Healthy financials, comfortable gearing

Leveraging on its SOE background, sizeable recurring cashflow generating from its IP portfolio and low gearing, Franshion is one of the very few China developers/landlords with an investment grade corporate credit rating. In October, 2013, Franshion issued 5-year USD300m senior notes with a coupon of 5.375%. In 2012, Franshion raised USD500m through senior notes with a coupon rate of only 4.7%, just slightly higher than the one by China State Construction (3.95%) and far lower than any other peers during 2012 (Figure 12).

Furthermore, it is also able to pledge its IP assets for commercial loans with lower costs comparing to traditional development loan. As a result, the blended financing cost is at ~6.2%, which is lower than ~7 - 9% for most other peers'.

Although Franshion had a net operating and investing cash outflow in 2013 mainly due to the high land premium paid (~CNY15b), we estimate it still had HKD11.5b (~CNY9b) cash on hand by end-2013 and net debt to attributable equity ratio of 59.6%, still slightly lower than our estimated sector's average of 67%. The company had an outstanding land premium of CNY10b as of end-2013, of which CNY8b will be paid in 2014 with the remaining CNY2b will be paid in 2015 and onwards.

For 2014, the company expects net operating cash inflow for including proceeds from sales of CNY26-27b, and rental and hotel income of around CNY3b. Aggregate cash outflow will be at around CNY26b, including expected construction capex (CNY10b), committed land premium (CNY8b), SG&A expenses (CNY2b), tax expenses (CNY4b) and interest expenses (CNY2b).

Figure 12: Summary of fixed income products issued by major listed developers in 2012 for comparison purposes

Company	Coupon (%)	Date of Maturity	Denominated currency	Fund raised (m)	Date of announcement
<b>2012 1H</b>					
China State Construction	4.875	15/2/2017	USD	750	9/2/2012
Agile Property	9.875	20/3/2017	USD	700	13/3/2012
KWG Property	13.250	22/3/2017	USD	400	15/3/2012
<b>2012 3Q</b>					
Kaisa Group	12.875	18/9/2017	USD	250	12/9/2012
Fantasia Holdings	13.750	27/9/2017	USD	250	19/9/2012
<b>2012 4Q</b>					
Sunac China	12.500	16/10/2017	USD	400	9/10/2012
China South City	13.500	17/10/2017	USD	125	10/10/2012
Longfor Properties	6.875	18/10/2019	USD	400	11/10/2012
Yuzhou Properties	11.750	25/10/2017	USD	250	17/10/2012
<b>Franshion Properties</b>	<b>4.700</b>	<b>26/10/2017</b>	<b>USD</b>	<b>500</b>	<b>19/10/2012</b>
SOHO China	5.750	7/11/2017	USD	600	31/10/2012
SOHO China	7.125	7/11/2022	USD	400	31/10/2012
China SCE Property	11.500	14/11/2017	USD	200	6/11/2012
China State Construction	3.950	15/11/2022	USD	700	7/11/2012
China State Construction	5.350	15/11/2042	USD	300	7/11/2012
Gemdale (Group)	7.125	16/11/2017	USD	350	12/11/2012
China Aoyuan Property	13.875	23/11/2017	USD	125	14/11/2012
Beijing Capital Land	7.600	29/11/2015	CNY	2,000	22/11/2012
Shui On Land	10.125	Perpetual	USD	500	3/12/2012

Note: Franshion issued a USD 300 m 5-year note with 5.375% coupon in October 2013.

The above 2012 issuance is for comparison purposes.

Source: Company data, Bloomberg and Maybank Kim Eng



## Earnings

### Estimated 2013 revenue growth at 22.6% YoY

We estimate 2013 revenue rose by 22.6% YoY to HKD21b, while core net profit grew 48.1% YoY to HKD3.1b. The total booked sales aggregated to an estimate of 0.35m sq m. We forecast FY14|15 will see a decent rate of growth with revenue increasing 36.8%|23.1% YoY to HKD28.8b|HKD35.5b, and core net profit rising by another 23.7%|30.2% YoY to HKD3.8bm|HKD5.0b.

### Expect gross margin to remain at close to 40% for 2015

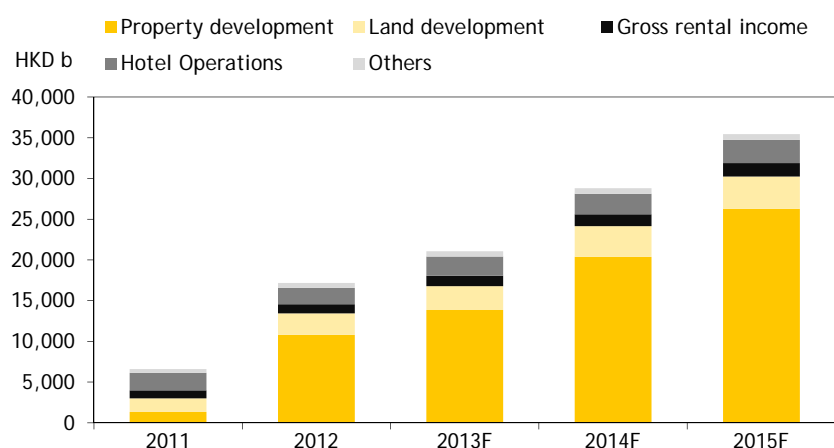
Franshion has the ability to price its projects at a premium over neighbouring projects due to the "Jinmao" brand and high construction quality. Furthermore, significant revenue contributions from the IPs also help to maintain its blended GPM at a higher level. Without considering any spin-off of IPs or disposals, we expect Franshion's GPM can remain at over 40% for 2013 and 2014, and still be close to 40% for 2015. The company targets to maintain GPM at 35 - 40% over the long term.

Figure 13: Franshion's income statement and earning forecast (HKD m)

HKD m	2011A	2012A	2013F	2014F	2015F
Property development revenue	1,322	10,796	13,857	20,364	26,263
Land development	1,673	2,649	2,914	3,788	3,977
Gross Rental Income	989	1,106	1,280	1,437	1,650
Hotel Operations	2,134	2,010	2,363	2,534	2,852
Others	474	614	644	677	710
<b>Turnover</b>	<b>6,592</b>	<b>17,176</b>	<b>21,059</b>	<b>28,801</b>	<b>35,453</b>
<b>Gross Profit</b>	<b>3,575</b>	<b>7,199</b>	<b>8,942</b>	<b>11,688</b>	<b>13,987</b>
SG&A	(1,158)	(1,407)	(1,685)	(2,246)	(2,659)
Other income (net)	(134)	13	0	0	0
<b>EBIT</b>	<b>2,283</b>	<b>5,804</b>	<b>7,257</b>	<b>9,441</b>	<b>11,328</b>
Net interest income	(664)	(817)	(868)	(955)	(959)
Interest income	195	170	180	154	193
Interest expenses after capitalization	(859)	(986)	(1,049)	(1,109)	(1,152)
Gross interest expense	(1,372)	(1,721)	(1,907)	(2,133)	(2,304)
Capitalised interest	513	735	858	1,024	1,152
Share of P&L of Associates and JCEs	4	2	0	0	0
Exceptional item	2,475	1,733	0	0	0
<b>Pretax income</b>	<b>4,097</b>	<b>6,723</b>	<b>6,389</b>	<b>8,486</b>	<b>10,369</b>
Income taxes	(216)	(1,145)	(1,597)	(2,122)	(2,592)
LAT	(970)	(1,638)	(920)	(1,171)	(1,286)
<b>Net income</b>	<b>2,911</b>	<b>3,940</b>	<b>3,872</b>	<b>5,194</b>	<b>6,491</b>
Minority interests	(566)	(563)	(795)	(1,392)	(1,544)
<b>Net income attributable to shareholders</b>	<b>2,344</b>	<b>3,378</b>	<b>3,077</b>	<b>3,802</b>	<b>4,948</b>
<b>Underlying net profit attributable to shareholders</b>	<b>1,341</b>	<b>2,078</b>	<b>3,077</b>	<b>3,802</b>	<b>4,948</b>

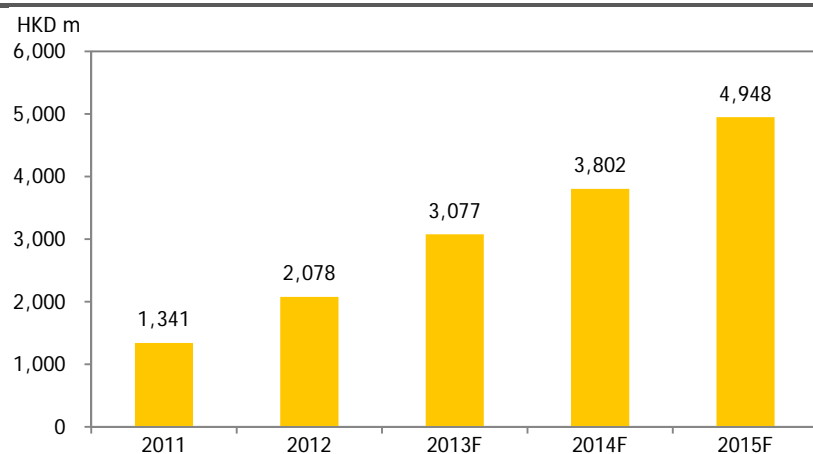
Source: Company data, Maybank Kim Eng estimates

Figure 14: Franshion's revenue breakdown (HKD b)



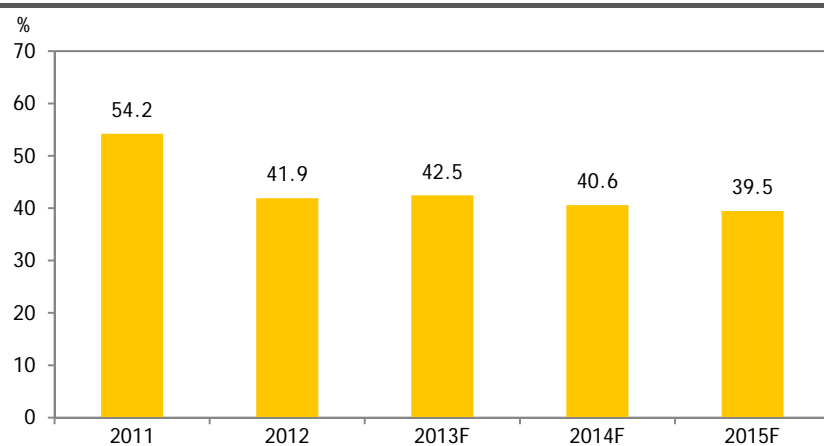
Source: Company data, Maybank Kim Eng

Figure 15: Franshion's underlying net profit attributable to shareholders (HKD m)



Source: Company data, Maybank Kim Eng

Figure 16: Franshion's gross profit margin (%)



Source: Company data, Maybank Kim Eng

Figure 17: Franshion's key projects planned completion schedule in 2013 - 2015F

Projects		Total saleable area (sq m)	2013F	To let (GFA, sq m)	2014F	To let (GFA, sq m)	2015F	To let (GFA, sq m)
			For sale (saleable area, sq m)		For sale (saleable area, sq m)		For sale (saleable area, sq m)	
Beijing Jinmao Palace Guangqu	Residential	199,858	99,131		15,256			
	Apartment	62,001	24,818		37,183			
	Retail	8,424					8,424	
Beijing JM Palace Wangjing	Residential	86,817			40,514		46,303	
	Retail	10,438			638		9,800	
Beijing JM Residence	Residential	137,615			137,615			
Beijing Yizhuang	Residential - X85R1 plot	107,445					107,445	
	Residential - X88R1 plot	102,338					102,338	
Shanghai International Shipping Service Centre	Office	341,802	43,342		70,312		51,194	96,230
Shanghai Haimen Road #55 Plot	Office (for sale)	194,838						
	Office (for let)	121,258						
	Retail	109,964						
Shanghai Jinmao Noble Manor	Villa	38,360	7,145		9,632		8,090	
	Apartment	24,357	6,929		972			
	Club House	1,882					1,882	
	Hotel	49,378		49,378				
Suzhou Jinmen Road	Residential	249,305					82,290	
Nanjing International Centre Phase 2	Residential	51,800						
	Office	72,200						
	Retail	48,500						
	Hotel	23,500						
Lijiang Whisper of Jade Dragon	Villa & Apartment	159,416			96,803		45,062	
	Retail	12,990				12,990		
	Hotel	45,031				57,351		
Lijiang Jinmao Noble Manor	Villa	6,000			1,333		3,333	
	Hotel	16,900				25,349		
Qingdao Jinmao Harbour	Apartment	275,215	91,387		57,861		65,337	
	Serviced Apartment	17,414						
	Retail	120,774	1,210		5,861		12,000	
Chongqing Jinmao Delicate Residence	Apartment	313,293			170,045		124,988	
	Serviced Apartment	35,332			26,514		7,694	
	Retail	43,958			686		20,060	
Changsha Jinmao Meixi Lake	Apartment	347,003	65,985		150,190		130,828	
	Villa	12,268	9,814		2,454			
	Serviced Apartment	18,000					18,000	
	Retail	10,600			3,180		7,420	
Changsha R&D Office Centre	Office	78,141	8,093	14,996	5,575		5,575	
Changsha International Plaza	Apartment	387,100			80,000		120,000	
	Serviced Apartment	86,300						
	Office	90,000						
	Retail	78,000			8,000			
	Hotel	45,000						
<b>TOTAL</b>		<b>4,240,815</b>	<b>357,854</b>	<b>64,374</b>	<b>920,624</b>	<b>95,690</b>	<b>978,063</b>	<b>96,230</b>

Source: Company data, Maybank Kim Eng

## Valuation

### Target price at 40% discount to NAV

On a sum-of-the-parts valuation, we estimate the company's NAV at HKD59.8b or HKD5.54 per share.

We believe the company should deserve a premium over its peers with the two-pronged re-rating story of strong sales growth and asset value realization. We expect Franshion's strong sales pipeline will allow it to deliver sales growth above the average of that of its peers in 2014. Although the large commercial property portfolio has lowered its ROE given the huge asset base, we believe Franshion has sufficient initiatives to monetize the portfolio via a spin-off. The mature and relatively profitable primary development project experience also allows the company to expand its footprint to other cities. We expect the huge capital recycling from the Changsha primary project will be able to support capex of other primary development projects under comfortable and controllable gearing levels.

Initiate at BUY with a target price of HKD3.32, representing 40% discount to NAV compared with peers' current average discount of 54%. Our target price translates to 9.4x 2014 PER, 7.3x 2015 PER and 0.7x 2014 book value. Our 2013 and 2014 earnings forecasts are generally in line with consensus but we are more bullish on its 2015 earnings outlook (9% above consensus on 2015 revenue and 7% above on core profit).

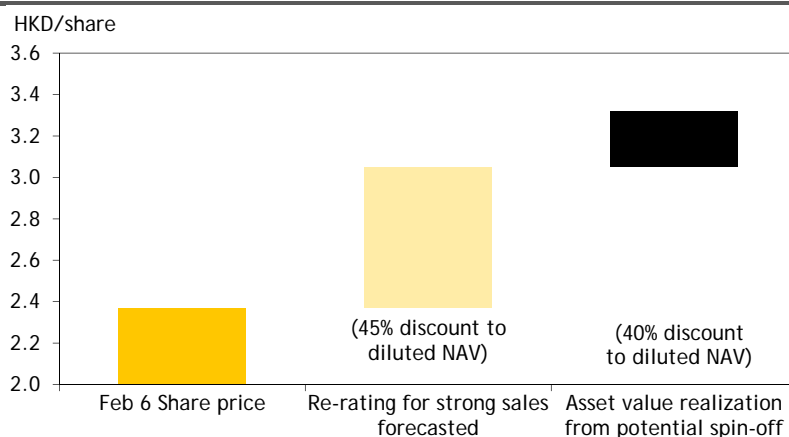
Figure 18: Franshion's GAV and NAV breakdown (HKD b)

	(HKD b)	per share (HKD)	% of GAV (%)	% of NAV (%)
Development Properties	48,735	4.51	51	81
Completed investment Properties	32,337	2.99	34	54
Primary land development	14,545	1.35	15	24
<b>GAV</b>	<b>95,617</b>	<b>8.85</b>	<b>100</b>	<b>160</b>
Outstanding land premium	(3,442)	(0.32)		(6)
Net cash / (Net debt)	(23,828)	(2.21)		(40)
LAT liabilities	(8,513)	(0.79)		(14)
<b>NAV</b>	<b>59,834</b>	<b>5.54</b>		<b>100</b>

Note: Based on fully-diluted number of shares

Source: Company data, Maybank Kim Eng estimates

Figure 19: Two-fold re-rating story for strong sales growth and asset value realization



Source: Company data, Maybank Kim Eng

Figure 20: Peers valuations comparison table

2/6/2014	Share Rating	Share Price	Mkt Cap (USD\$b)	3M ATV (USD\$m)	2013	2014	1-	Est	Dis to	PER			P/B			Div Yield		
					Perf*	Ytd Perf*	Month Perf.*	NAV/share	NAV Est	2013F	2014F	2015F	2013F	2014F	2015F	2013F	2014F	2015F
HK-listed																		
Simple avg					-14%	-10%	-9%		-54%	6.2	5.6	4.9	0.84	0.74	0.65	4.4%	5.1%	5.9%
Agile	HOLD	6.95	3.1	6.5	-24%	-16%	-16%	19.8	-65%	4.1	3.8	3.4	0.55	0.50	0.44	5.9%	6.3%	7.1%
COLI	BUY	20.30	21.5	57.3	-6%	-7%	-2%	27.9	-27%	8.6	7.0	5.8	1.59	1.34	1.13	2.3%	2.6%	3.2%
COUNTRY	BUY																	
Garden		4.15	9.8	13.7	15%	-11%	-11%	6.5	-36%	7.5	6.1	4.9	1.38	1.21	1.02	4.9%	5.6%	7.0%
CRL	BUY	17.96	13.5	19.0	-9%	-7%	-5%	26.0	-31%	12.0	9.8	7.0	1.39	1.26	1.12	2.7%	3.4%	4.0%
Evergrande	NR	3.04	6.3	15.6	-30%	3%	7%	8.5	-64%	4.3	3.8	3.2	0.74	0.64	0.55	3.6%	5.1%	5.8%
Franshion	BUY	2.37	2.8	2.3	-3%	-12%	-4%	5.5	-57%	8.3	6.7	5.2	0.69	0.63	0.56	3.6%	4.5%	5.8%
Greentown	NR	10.58	2.9	4.6	-17%	-11%	-5%	28.7	-63%	3.3	2.8	2.5	0.71	0.58	0.49	6.0%	6.8%	7.6%
GZ R&F	HOLD	10.14	4.2	7.7	-12%	-11%	-7%	24.2	-58%	4.9	4.2	3.4	0.86	0.76	0.66	8.2%	8.5%	9.3%
Hopson	NR	7.09	2.1	1.1	-25%	-24%	-21%	30.1	-76%	5.9	4.6	3.3	0.27	0.26	0.24	0.5%	1.1%	1.7%
KWG	BUY	3.95	1.5	2.6	-26%	-8%	-4%	10.3	-62%	4.0	3.3	2.6	0.53	0.47	0.40	5.0%	6.1%	7.1%
Longfor	HOLD	10.28	7.2	5.9	-29%	-5%	1%	17.7	-42%	7.2	6.0	5.0	1.26	1.07	0.92	2.8%	3.3%	4.1%
Poly Property	BUY	3.65	1.7	4.9	-32%	-12%	-8%	10.6	-66%	5.1	4.0	3.4	0.46	0.42	0.39	5.9%	7.4%	8.9%
Shenzhen Inv	NR	2.71	1.9	2.7	-7%	-7%	-3%	8.0	-66%	5.7	5.2	4.5	0.50	0.49	0.45	5.5%	6.3%	7.2%
Shimao	BUY	16.32	7.2	13.8	22%	-8%	-6%	27.6	-41%	7.0	5.5	4.5	1.12	0.97	0.83	4.4%	5.5%	5.9%
Sino-Ocean	HOLD	4.19	3.9	3.5	-12%	-18%	-14%	8.4	-50%	8.6	6.6	5.9	0.59	0.55	0.52	5.0%	5.7%	6.3%
SOHO China	SELL	6.12	4.1	5.4	-2%	-8%	-6%	10.2	-40%	5.6	12.9	17.1	0.73	0.72	0.71	5.4%	5.2%	5.2%
Sunac	BUY	4.59	2.0	6.6	-23%	-1%	2%	10.9	-58%	3.7	3.0	2.2	0.86	0.68	0.53	2.8%	3.3%	4.4%
Yuexiu Prop	BUY	1.57	1.9	5.3	-22%	-18%	-14%	5.3	-70%	7.9	6.3	4.4	0.40	0.38	0.35	6.4%	7.5%	9.1%

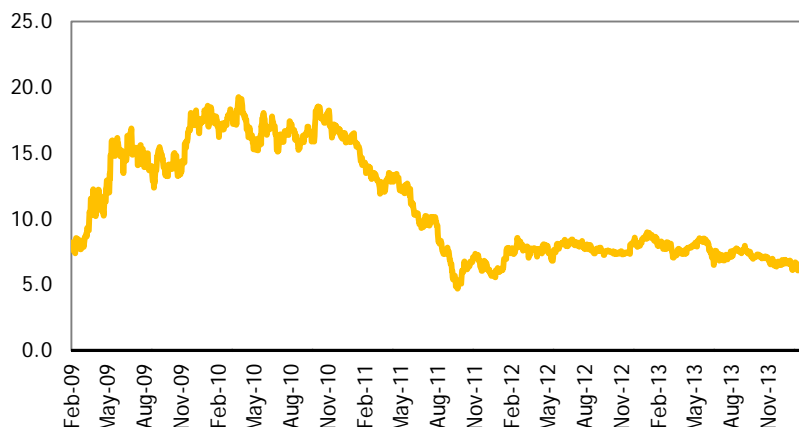
\*Not adjusting for dividends

Note: Orange highlighted cells indicate close to 2008 GFC trough valuations

Consensus numbers are used for non-covered companies

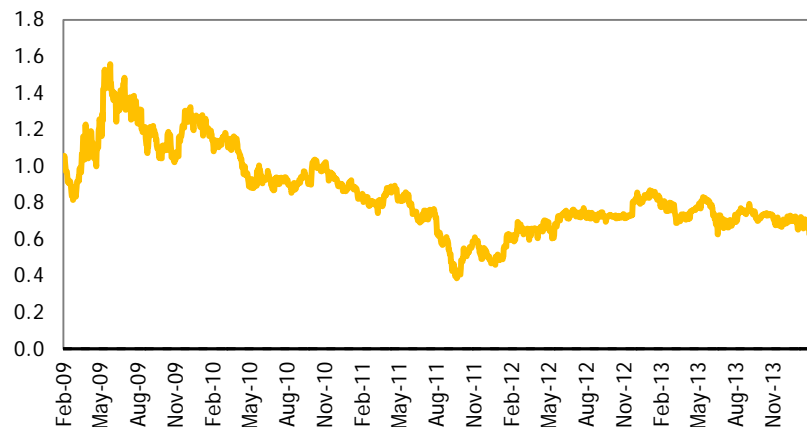
Source: Company data, Bloomberg, Maybank Kim Eng

Figure 21: Franshion's historical forward PE



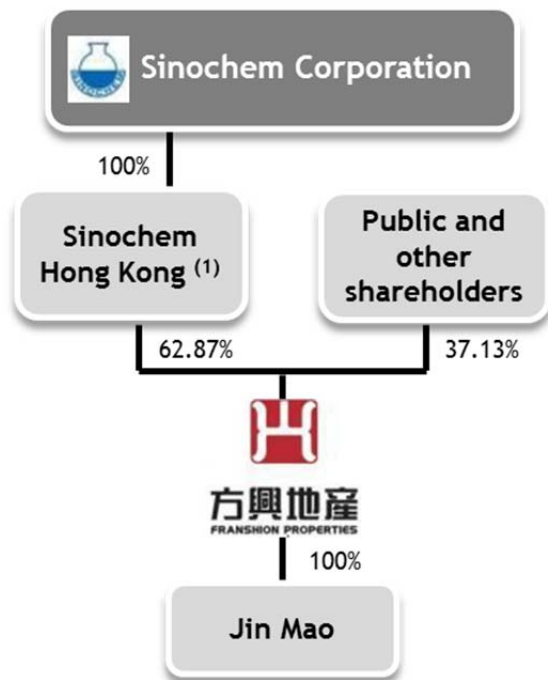
Source: Bloomberg, Maybank Kim Eng

Figure 22: Franshion's historical forward P/B



Source: Bloomberg, Maybank Kim Eng

Figure 23: Shareholding structure (as at 31 Dec 2013)



Note: 1) Sinochem Hong Kong (Group) Co., Ltd, a wholly owned subsidiary of Sinochem Corporation.

Source: Company data, Maybank Kim Eng

## Investment risks

### **Might be difficult to replenish landbank at low cost**

With the rising land costs and its focus on Tier-1 and 2 cities, it might be difficult for Franshion to replenish a sizeable landbank at a low cost. Its recent acquisition of a project in the northern Zhabei District in Shanghai with a project partner was expensive. That said, we estimate Franshion's landbank is sufficient for ~4-5 years' developments. Its total current landbank is ~7m sq m, and 5.7m sq m on an attributable basis.

### **Primary development project sales schedule not completely controlled by Franshion**

The Changsha primary development project was successfully launched for sale with a good track record since 2011. Although Franshion controls whether the land plots are ready for sale or not, the actual sales pipeline timing is under the government's control. Moreover, this kind of primary development project is not easy to replicate in other cities as it requires close relations with different city governments.

### **Potential dilution from CB conversion**

In 2010, Franshion issued a batch of convertible securities with a principal amount of USD600m with a conversion price of HKD2.83 at a distribution rate of 6.8%. We believe the relatively high distribution rate will lower some conversion intention. However, if we assume the share price performs well and triggers a full conversion, the convertible securities could be convertible into 1.645b shares in total, which represents about 17.95% of the current issued share capital.



FYE 31 Dec (HKD m)	FY11A	FY12A	FY13E	FY14E	FY15E
<b>Key Metrics</b>					
P/E (reported) (x)	9.3	6.4	7.1	5.7	4.4
Core P/E (x)	9.3	10.4	7.1	5.7	4.4
Core FD P/E (x)	19.1	12.3	8.3	6.7	5.2
P/BV (x)	1.0	0.9	0.7	0.6	0.6
P/NTA (x)	1.0	0.9	0.7	0.6	0.6
Net dividend yield (%)	1.7	2.9	3.6	4.5	5.8
FCF yield (%)	nm	nm	nm	1.0	16.8
EV/EBITDA (x)	11.7	7.5	6.3	5.2	4.4
EV/EBIT (x)	13.5	7.9	6.5	5.3	4.5
<b>Income Statement</b>					
Revenue	6,591.7	17,175.7	21,058.6	28,800.7	35,452.6
Gross profit	3,575.0	7,198.7	8,941.6	11,687.9	13,987.2
EBITDA	2,619.0	6,145.0	7,490.8	9,694.1	11,606.2
Depreciation	(276.8)	(281.8)	(233.9)	(252.7)	(277.9)
Amortisation	(59.3)	(59.0)	0.0	0.0	0.0
EBIT	2,282.9	5,804.3	7,256.9	9,441.5	11,328.3
Net interest income /(exp)	(664.4)	(816.5)	(868.4)	(955.2)	(959.2)
Associates & JV	3.6	2.5	0.0	0.0	0.0
Exceptionals	2,475.3	1,733.1	0.0	0.0	0.0
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	4,097.3	6,723.3	6,388.5	8,486.2	10,369.1
Income tax	(1,186.6)	(2,783.0)	(2,516.8)	(3,292.7)	(3,877.8)
Minorities	(566.4)	(562.6)	(794.8)	(1,391.5)	(1,543.5)
Reported net profit	2,344.4	3,377.7	3,076.9	3,802.0	4,947.7
Core net profit	1,341.0	2,077.9	3,076.9	3,802.0	4,947.7
<b>Balance Sheet</b>					
Cash & Short Term Investments	12,592.1	13,464.4	11,575.0	14,347.6	15,899.9
Property, Plant & Equip (net)	27,958.3	25,410.6	25,501.9	25,590.7	25,671.3
Intangible assets	26.8	22.4	22.4	22.4	22.4
Investment in Associates & JVs	36.1	38.5	38.5	38.5	38.5
Other assets	29,157.8	43,566.2	51,381.9	56,794.4	60,341.8
Total assets	69,771.0	82,502.2	88,519.7	96,793.6	101,973.9
ST interest bearing debt	6,028.0	8,952.2	4,329.9	7,147.9	9,131.5
LT interest bearing debt	19,171.8	19,323.2	26,069.4	28,086.5	26,528.9
Other liabilities	14,024.4	19,724.0	20,105.4	19,056.2	18,116.1
Total Liabilities	39,224.2	47,999.4	50,504.7	54,290.6	53,776.5
Shareholders Equity	26,170.7	28,877.8	31,595.2	34,691.7	38,842.5
Minority Interest	4,376.5	5,625.0	6,419.8	7,811.3	9,354.8
Total shareholders equity	30,547.3	34,502.8	38,015.0	42,503.0	48,197.4
<b>Cash Flow</b>					
Pretax profit	4,097.3	6,723.3	6,388.5	8,486.2	10,369.1
Depreciation & amortisation	336.2	340.7	233.9	252.7	277.9
Adj net interest (income)/exp	(787.3)	(949.4)	180.4	154.0	192.8
Change in working capital	(8,835.9)	(4,336.7)	(6,667.3)	(5,732.8)	(3,721.3)
Cash taxes paid	1,109.8	1,136.9	(1,989.2)	(2,612.1)	(3,104.4)
Other operating cash flow	(3,249.5)	(2,719.3)	0.0	0.0	0.0
Cash flow from operations	(7,711.2)	(50.9)	(1,853.7)	548.0	4,014.1
Capex	(217.8)	(314.6)	(325.2)	(341.5)	(358.5)
Free cash flow	(8,147.5)	(727.1)	(2,178.9)	206.5	3,655.6
Dividends paid	(229.0)	(366.5)	(641.3)	(923.1)	(1,140.6)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Change in Debt	6,131.2	3,118.9	2,123.9	4,835.0	426.0
OTH investing/financing cash flow	3,495.2	(948.0)	(1,193.2)	(1,345.9)	(1,388.7)
Effect of exch rate changes	248.1	(10.1)	0.0	0.0	0.0
Net cash flow	939.7	484.3	(1,889.4)	2,772.6	1,552.3

FYE 31 Dec (HKD m)	FY11A	FY12A	FY13E	FY14E	FY15E
<b>Key Ratios</b>					
<b>Growth ratios (%)</b>					
Revenue growth	3.8	160.6	22.6	36.8	23.1
EBITDA growth	7.8	134.6	21.9	29.4	19.7
EBIT growth	(4.6)	154.3	25.0	30.1	20.0
Pretax growth	33.9	64.1	(5.0)	32.8	22.2
Reported net profit growth	36.8	44.1	(8.9)	23.6	30.1
Core net profit growth	25.6	54.9	48.1	23.6	30.1
<b>Profitability ratios (%)</b>					
EBITDA margin	39.7	35.8	35.6	33.7	32.7
EBIT margin	34.6	33.8	34.5	32.8	32.0
Pretax profit margin	nm	39.1	30.3	29.5	29.2
Payout ratio	15.4	18.5	25.4	25.4	25.4
<b>DuPont analysis</b>					
Net profit margin (%)	nm	19.7	14.6	13.2	14.0
Revenue/Assets (x)	0.1	0.2	0.2	0.3	0.3
Assets/Equity (x)	2.7	2.9	2.8	2.8	2.6
ROAE (%)	5.1	6.4	8.5	9.4	10.9
ROAA (%)	2.2	2.7	3.6	4.1	5.0
<b>Liquidity &amp; Efficiency</b>					
Cash conversion cycle	nm	nm	nm	nm	nm
Days receivable outstanding	8.0	22.1	34.2	25.0	20.3
Days inventory outstanding	nm	nm	nm	nm	nm
Days payables outstanding	183.5	87.9	75.0	53.1	42.4
Dividend cover (x)	6.5	5.4	3.9	3.9	3.9
Current ratio (x)	1.4	1.5	2.0	2.2	2.3
<b>Leverage &amp; Expense Analysis</b>					
Asset/Liability (x)	1.8	1.7	1.8	1.8	1.9
Net debt/equity (%)	48.2	51.3	59.6	60.2	50.9
Net interest cover (x)	3.4	7.1	8.4	9.9	11.8
Debt/EBITDA (x)	9.6	4.6	4.1	3.6	3.1
Capex/revenue (%)	3.3	1.8	1.5	1.2	1.0
Net debt/ (net cash)	12,607.7	14,811.0	18,824.3	20,886.8	19,760.5

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