

Company

16 August 2010 | 17 pages

Longfor Properties (0960.HK)

 Equity
 Target price change

Buy: 1H10 Results In Line, Strong Sales Pipeline

- Reiterate Buy/Low Risk (1L)** — TP of HKD9.81, based on 20% discount to 10E NAV of HKD12.26 (previously HKD12.22). Given the strong sales momentum and competitive products/brand name, we believe Longfor should act as one of the market consolidators in a market downturn.
- 1H10 results in line** — Longfor released 1H10 results with core net profit of RMB895mn, down 18% YoY, which is in line with our estimates. The skewed GFA completion split between the first and second half of the year resulted in recognized revenue of only RMB3.67bn in 1H, down 37.5% yoy. In 2010, 2.3mn sqm GFA is targeted to be completed, of which 673k sqm GFA is attained in 1H. Longfor has locked in around 94% of estimated recognized revenues in 2010.
- Better than expected financial position** — Thanks to good sales, Longfor has maintained a healthy financial position. Now, it has cash on hand of around RMB8.85bn and net gearing of only 52.6%, much better than expected. The strong financial position underpins its steady expansion pace in 2010 and 2011.
- Manageable 2010 sales target of RMB24.8bn** — In 1H, Longfor achieved RMB10.49bn sales already, 42.3% of the full-year target. In 2H, Longfor should have around RMB23.1bn properties available for sale; even assuming digestion ratio of 65%, it is expected to generate sales of RMB15bn in 2H. In 2010, there will be more than 60% of sales derived from Eastern China.
- Attributable landbank of 21.24m sqm GFA** — Now, Longfor's landbank has expanded into attributable of 21.24m sqm GFA, located in 11 key cities. Compared with most of its closest peers, Longfor's overall land cost appears to be quite reasonable with average land cost of around RMB2,215/sqm GFA. This is equivalent to 18.2% of its estimated RMB12,200/sqm ASP for its existing projects.

Buy/Low Risk	1L
Price (16 Aug 10)	HK\$7.95
Target price	HK\$9.81
	<i>from HK\$9.78</i>
Expected share price return	23.4%
Expected dividend yield	1.0%
Expected total return	24.4%
Market Cap	HK\$40,982M
	US\$5,273M

Price Performance (RIC: 0960.HK, BB: 960 HK)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Dec	(RmbM)	(Rmb)	(%)	(x)	(x)	(%)	(%)
2008A	332	0.080	-55.8	87.0	9.2	11.1	0.0
2009A	2,209	0.429	436.9	16.2	2.9	29.0	1.0
2010E	2,229	0.433	0.9	16.1	2.6	17.4	1.2
2011E	4,001	0.777	79.5	8.9	2.1	26.2	1.3
2012E	4,772	0.927	19.3	7.5	1.7	25.0	1.6

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Fiscal year end 31-Dec	2008	2009	2010E	2011E	2012E
Valuation Ratios					
P/E adjusted (x)	87.0	16.2	16.1	8.9	7.5
P/E reported (x)	87.0	16.2	16.1	8.9	7.5
P/BV (x)	9.2	2.9	2.6	2.1	1.7
Dividend yield (%)	0.0	1.0	1.2	1.3	1.6
Per Share Data (Rmb)					
EPS adjusted	0.080	0.429	0.433	0.777	0.927
EPS reported	0.080	0.429	0.433	0.777	0.927
BVPS	0.752	2.357	2.624	3.315	4.086
NAVps ordinary	na	na	na	na	na
DPS	0.000	0.070	0.080	0.090	0.110
Profit & Loss (RmbM)					
Net operating income (NOI)	1,165	3,332	4,668	7,444	8,872
G&A expenses	-634	-353	-675	-1,051	-1,401
Other Operating items	53	136	18	438	676
EBIT including associates	584	3,114	4,011	6,830	8,147
Non-oper./net int./except.	97	625	33	-5	-14
Pre-tax profit	681	3,739	4,044	6,826	8,132
Tax	-281	-1,247	-1,526	-2,202	-2,753
Extraord./Min. Int./Pref. Div.	-68	-283	-289	-623	-607
Reported net income	332	2,209	2,229	4,001	4,772
Adjusted earnings	332	2,209	2,229	4,001	4,772
Adjusted EBIT	520	2,978	3,993	6,392	7,470
Adjusted EBITDA	531	2,978	3,993	6,392	7,470
Growth Rates (%)					
NOI	-3.0	186.1	40.1	59.5	19.2
EBIT adjusted	-28.6	472.2	34.1	60.1	16.9
EPS adjusted	-55.8	436.9	0.9	79.5	19.3
Cash Flow (RmbM)					
Operating cash flow	-2,378	4,473	-4,291	-2,315	2,305
Depreciation/amortization	11	0	0	0	0
Net working capital	-1,795	1,382	-5,782	-6,628	-2,394
Investing cash flow	-1,554	-3,642	-1,297	-311	-799
Capital expenditure	0	0	0	0	0
Acquisitions/disposals	-269	-1,165	-1,297	-311	-799
Financing cash flow	4,819	2,742	3,826	1,556	-1,779
Borrowings	4,911	-3,074	4,449	2,500	-493
Dividends paid	-138	-227	-556	-944	-1,286
Change in cash	885	3,573	-1,762	-1,070	-273
Balance Sheet (RmbM)					
Total assets	32,396	42,445	51,977	60,309	71,236
Cash & cash equivalent	3,834	7,298	5,536	4,466	4,193
Net fixed assets	3,937	4,870	5,706	6,017	6,816
Total liabilities	28,452	29,207	37,304	41,956	48,790
Total Debt	12,840	9,766	14,215	16,715	16,222
Shareholders' funds	3,944	13,239	14,674	18,353	22,447
Profitability/Solvency Ratios					
EBIT margin adjusted (%)	11.6	26.2	27.9	30.0	28.7
ROE adjusted (%)	11.1	29.0	17.4	26.2	25.0
ROA adjusted (%)	1.2	5.9	4.7	7.1	7.3
Net debt to equity (%)	228.3	18.6	59.1	66.7	53.6
Interest coverage (x)	18.9	na	na	nm	488.5

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1H10 Results In Line, Strong Sales Pipeline

FY10 Interim Result In Line

Core profit of RMB895mn, down 18%yoy

Longfor released the FY10 interim result with a headline profit of RMB2.2 bn, up 51.4% yoy. Stripping out the revaluation gain of the investment properties, the core attributable profit is around RMB895mn, down 18% YoY, which is in line with our estimates. EPS was RMB0.426 on a fully diluted basis and no interim dividend was declared.

The skewed GFA completion split between the first and second half of the year resulted in recognized revenue of only RMB3.67bn, down 37.5% yoy. This represented around 26.5% of our annual forecast of RMB13.9bn, but is well expected to boost up in the third and fourth quarters. Around 2.3mn sqm GFA is targeted to be completed in the current year and only 673k sqm GFA was attained in the first half.

Strong product sales with enlarged contribution from high-price cities (e.g., Beijing, Shanghai, etc.) have not been fully reflected in the profitability during the 1H period. Gross margin stayed flattish at around 31%, which is similar to the level in the corresponding period last year. Improvement was observed in the core net margin, which increased to 24.4% from 18.6% of 1H10, even if we exclude part of the increase resulting from the recognition of the reversal of income tax expenses.

Figure 1. Longfor – Condensed Income Statement (RMB '000)

6 months ended 30 Jun	1H2010	% of revenue	1H2009	% of revenue	YoY Chg
Revenue, net	3,672,389	100%	5,875,808	100.0%	-37%
Cost of sales	(2,537,228)	-69%	(4,035,743)	-68.7%	-37%
Gross profit	1,135,161	31%	1,840,065	31.3%	-38%
Other income	43,437	1%	344,159	5.9%	-87%
Change in Fair value of IP	2,130,612	58%	561,000	9.5%	280%
S,G&A	(201,557)	-5%	(190,797)	-3.2%	6%
Finance Costs	(1,333)	0%	(41,634)	-0.7%	-97%
Share of results of JCE	(7,655)	0%	32,570	0.6%	-124%
Taxation	(431,725)	-12%	(885,379)	-15.1%	-51%
PAT	2,666,940	73%	1,659,984	28.3%	61%
PAT excl impact of IP revaluation	1,068,981	29%	1,260,272	21.4%	-15%
Attributable profit	2,204,970	60%	1,456,061	24.8%	51%
Core attributable profit	895,093	24%	1,091,123	18.6%	-18%
EPS—basic	0.428		0.364		18%
EPS— diluted	0.426		N/A		
DPS	0		N/A		

Source: Company; Citi Investment Research and Analysis

Figure 2. Longfor – Segment Performance (RMB '000)

Revenue breakdown by segments	1H10	% of rev	1H09	% of rev	YoY Chg
Revenue breakdown by segment					
Property development *	3,467,181	94.4%	5,718,441	97%	-39%
Rental	114,443	3.1%	86,266	1%	33%
Property management	90,764	2.5%	71,101	1%	28%
Total	3,672,388	100%	5,875,808	100%	-37%
Gross margin by segment					
Property development	29.90%		30.60%		
Rental	80.80%		79.80%		
Property management	7.80%		27.70%		
Overall margin	30.90%		31.30%		

Source: Company; Citi Investment Research and Analysis

Financial position better than expected

It is foreseeable that Longfor's gearing should scale up during the reporting period after its proactive landbank expansions in FY09 and early FY10. The financial position turns out to be healthier than what we expected. Net gearing by end-June 2010 is approximately 52.6% with total cash on hand staying at RMB8.85bn. The company owns the unused credit facilities of RMB7.5bn, which implied a total of RMB16.35bn financial resources available for Longfor.

Though Longfor has acquired a lot of landbank reserves in the past several months, the company is still comfortable to maintain the financial position at a healthy level, expects to maintain the net gearing ratio of 50-60% by the end of 2010, and the key cash outflow for land premium payment and construction capex can be fully covered by the presale proceeds.

Figure 3. Longfor – Financial Position (RMB mn)

	Jun-10	Dec-09
Cash on hand	8,847	7,298
Total debt	16,201	9,766
Net Debt	(7,354)	(2,468)
Equity (excluded MI)	13,994	12,139
Gearing	52.6%	20.3%

Source: Company; Citi Investment Research and Analysis

Comfortable to achieve RMB24.8bn 2010 Sales Target

1H sales of RMB10.49bn, 42.3% of full-year target

In 1H, Longfor achieved sales of RMB10.49bn, up by 30.7% yoy. Driven by sales of high ASP projects in Beijing, ASP increased by 81.7% to RMB14,234 psm when compared with 2009.

The sales from the cities in Eastern China accounted for around 60% of total sales while the cities in Western China accounted for the remaining 40%. In 1H, Beijing contributed RMB5.1bn sales, accounting for around 50% of total sales, within which Summer Palace Splendor, Blossom Chianti and Tangning One generated RMB1.55bn, RMB1.1bn and RMB1.02bn sales, respectively.

In 1H10, Longfor launched around 1.0m sqm GFA properties for sale and sold 0.75m sqm GFA, translating into a digestion ratio of around 75%.

Figure 4. Longfor- 1H10 Contracted Sales

Project	Location	Value (RMBmn)	GFA(sqm)	ASP (RMB)
Summer Palace Splendor	Beijing	1,547	23,754	65,126
Blossom Chianti	Beijing	1,096	49,694	22,055
Tangning One	Beijing	1,024	25,085	40,821
Chianti Riverside	Beijing	943	65,519	14,393
Toschna Villa	Chongqing	853	70,755	12,056
Three Thousand Castles	Chendu	732	63,256	11,572
Bamboo Groce	Chongqing	567	59,211	9,576
Sunshine City	Shanghai	465	19,307	24,085
Wuxi Taike Yuan I	Wuxi	446	35,942	12,409
Azure Chianti	Beijing	412	17,879	23,044
Sunshine Riverside	Chongqing	377	53,636	7,029
Chunsen Land	Chongqing	371	36,692	10,111
Shanghai Rose & Gingko Villa	Shanghai	294	10,145	28,980
Bridge County	Chendu	285	20,040	14,222
Wu Kuai Shi	Chendu	284	34,754	8,172
Peace Hill County	Chongqing	247	38,683	6,385
Chengdu Flamenco Spain	Chendu	203	33,334	6,090
Elegance Loft	Beijing	102	26,031	3,918
Xi'an Fairy Castle	Xi'an	73	9,763	7,477
Three Thousand Lane	Chendu	34	8,964	3,793
Wisdom Town	Chongqing	17	1,601	10,618
Others	N.A.	113	32,603	3,466
Total		10,485	736,648	14,234

Source: Company; Citi Investment Research and Analysis

Full-year target of RMB24.8bn is manageable; Beijing exposure risk is overstated

Given the good sales performance in 1H, the management is very confident of achieving its full-year target of RMB24.8bn. In 1H, Beijing and Chongqing acted as the key sales contributors with sales of RMB5.1bn and RMB2.3bn respectively while the projects in new cities should emerge as sales growth drivers in 2H. In August, Changzhou Qinglong and Shenyang Daoyi projects should be launched for sale. Hangzhou Xiasha and Beijing Changying projects should be launched for sale in 4Q.

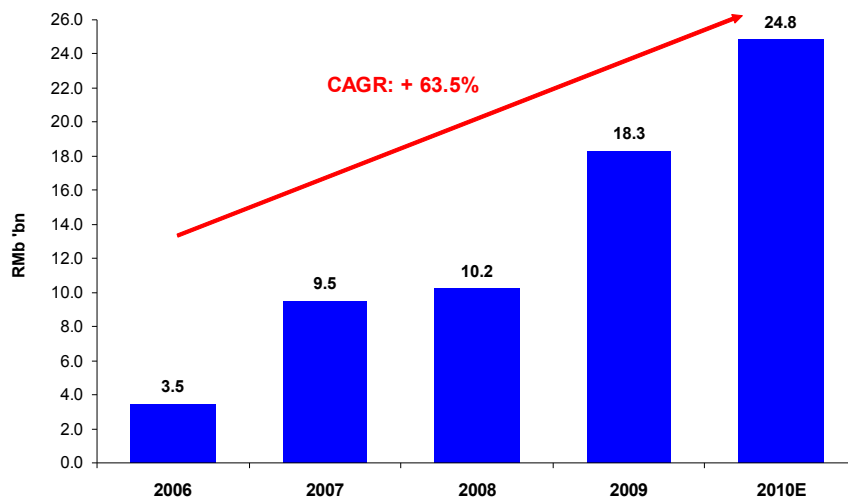
In July, Longfor recorded contract sales of RMB1.94 billion, representing 3.2% growth from last month. In the last seven months, the group's contract sales amounted to RMB12.43 billion, a 22.6% increase y-o-y. A breakdown of total contract sales according to regions: RMB5.04 billion was from the Western region, RMB5.87 billion from the Pan Bohai region and RMB1.52 billion from the Yangtze River Delta region.

As of end July, Longfor achieved around RMB6.0bn sales in Beijing already, around 80% of the full-year target of RMB7.7bn. In 2H, Summer Palace, Blossom, Tangning One should continue to sell while the Chaoyang Changying project should be launched for sale in 4Q10. In our view the solid management ability of Longfor has successfully removed the risk of so called "high exposure" in Beijing.

In 2H, Longfor should have 2.1m sqm GFA properties available for sale, equivalent to value of around RMB23.1bn, assuming a digestion ratio of 65%,

Longfor is expected to have sales of around RMB15bn in 2H (1H of RMB10.49bn).

Figure 5. Longfor – Contracted Sales 2006-10E



Source: Citi Investment Research and Analysis

* 2010E is from management guidance

Accelerating the Development of Investment Properties

Investment Properties, 2.0m sqm GFA in the Coming 5 Years

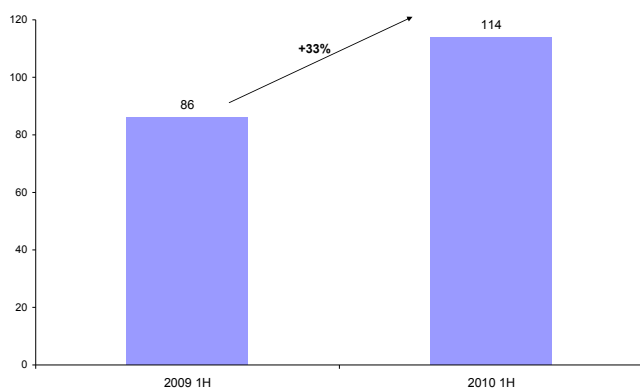
Now, Longfor has 4 investment properties in operation with total GFA of around 0.33m sqm GFA. The management plans to accelerate the development in investment properties portfolio, target to increase to 2.0m sqm GFA by the end of 2015 and the total number of investment projects increased to 18.

Figure 6. Development Schedule of Investment Properties

Project	Region	City	GFA(sqm'000)	Opening Year
Sunshine City	Y.R.D.	Shanghai	23	2012
Xia Sha	Y.R.D.	Hangzhou	150	2013
Dongjing 120 Project	Y.R.D.	Changzhou	100	2015
Taike Yuan II	Y.R.D.	Wuxi	82	2014
Xihu Road	Y.R.D.	Wuxi	100	2014
Baisha Project	P.B.R.	Qingdao	100	2012~2015
Changying	P.B.R.	Beijing	216	2013
Starry Street	P.B.R.	Beijing	7	2011
Wukuai Shi	Western	Chendu	230	2013
Three Thousand Mall	Western	Chendu	38	2010
Mopan Shan	Western	Chongqing	38	2015
University Town	Western	Chongqing	45	2012
Crystal Magic	Western	Chongqing	518	2012&2014
MOCO Center	Western	Chongqing	29	2010&2011
Crystal Constellation	Western	Chongqing	42	Before 2007
Fairy Castle	Western	Chongqing	29	Before 2008
West Paradise Walk	Western	Chongqing	112	Before 2009
North Paradise Walk	Western	Chongqing	146	Before 2010
Total			2,005	

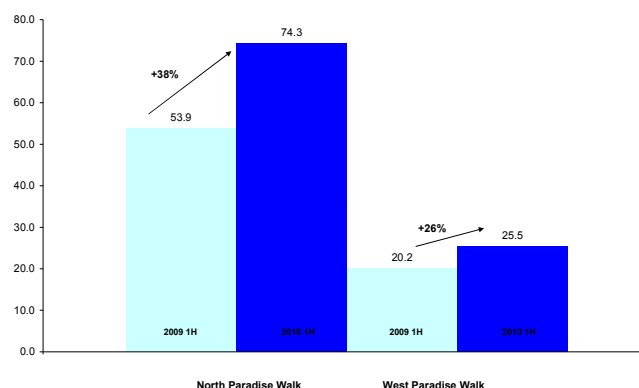
Source: Citi Investment Research and Analysis

Figure 7. Rental Income (RMB mn)



Source: Company; Citi Investment Research and Analysis

Figure 8. Rental Income from 2 Top IPs in Chongqing (RMB mn)



Source: Company; Citi Investment Research and Analysis

Great Improvements in Landbank

More than 13mn sqm GFA landbank acquired in 2009 and 1H10

Following the successful listing and capital raising in Nov 09, Longfor's financial position has been substantially improved. With the abundant financial resources, Longfor has speeded up its expansion pace and acquired several land plots in key cities like Hangzhou, Changzhou, Qingdao, Shenyang, Beijing, Shanghai, etc. In 2009 and 1H10, Longfor has splashed out around RMB29.99bn on the landbank replenishment with 13.36mn sqm Saleable/investment GFA added to the land reserve, translating into Av of

RMB2,224/sqm GFA, which averaged down the unit cost of Longfor's overall landbank reserves to RMB2,215/sqm GFA.

Within the 13.36m sqm GFA landbank, 6.12m sqm GFA were acquired after Longfor's IPO last November. Most of this newly acquired landbank is located in top tier/key second tier cities. The average AV of the newly acquired landbank in 2009 and 1H10 was RMB2,224psm, which is reasonably low in our view. This has reflected Longfor's capability to source different land reserves in the mean other than the competitive land auction market.

Figure 9. Longfor – Landbank Replenishment in 2009 and YTD 2010

Project name	Location	Attributable interest (%)	Site area (sqm)	Total GFA (sqm)	Total land cost (RMB mn)	Unit land cost (RMB/sqm)	Estimated completion date	Type
2009 (before IPO)								
Tai Ke Yuan	Wuxi	91.30%	188,496	270,657	644	2,379	Q2 2012	R
Tai Ke Yuan II	Wuxi	91.30%	125,400	279,547	546	1,953	Q1 2013	R/S
Qing Long	Changzhou	95.60%	164,855	418,000	509	1,218	Q2 2013	R
Qing Long II	Changzhou	85.10%	143,965	345,430	477	1,382	Q2 2012	R
Chianti Riverside	Beijing	91.30%	187,514	305,860	528	1,728	Q2 2012	R/S/CP
Hou Sha Yu	Beijing	91.30%	163,616	65,447	866	13,232	Q3 2013	R
Hui Shan	Shenyang	93.50%	84,086	85,137	82	962	Q4 2011	R/S
Dao Yi	Shenyang	91.30%	684,420	1,620,689	641	396	Q4 2015	R/S
Mo Pan Shan	Chongqing	93.50%	224,378	1,170,392	2,280	1,948	Q2 2015	R/S/CP
University Town 2	Chongqing	95.60%	588,220	1,774,955	1,060	597	Q2 2015	R/S/CP
Wu Kuai Shi	Chengdu	91.30%	184,487	901,813	2,173	2,410	Q3 2014	R/S/H/O/CP
2009 (After the IPO)								
Xi Hu Lu	Wuxi	91.30%	145,900	486,000	1,490	3,066	Q4 2014	R/S
Bai Sha	Qingdao	84.00%	509,300	622,240	506	814	Q4 2013	R/S/CP
Hong Zhuang	Changzhou	91.30%	294,440	809,700	1,588	1,961	Q3 2013	R
Xia Sha	Hangzhou	100.00%	177,478	591,214	3,570	6,038	Q4 2014	R/S/O/H
Bai Yin Lu	Shanghai	95.60%	62,819	146,080	1,729	11,835	Q3 2012	R/S
Mou Ma Heaven	Chengdu	95.60%	448,582	538,298	807	1,499	Q3 2014	R/S/H/CP
Total / Average			4,377,956	10,431,460	19,497	1,869		
2010 1H land bank replenishment review								
Dong Jing 120	Changzhou	91.30%	384,720	470,800	2,307	4,900	Q4 2012	R/S/CP
Hui Shan II	Shenyang	93.50%	371,311	610,462	362	593	–	–
Songjiang Long Xin Lu	Shanghai	95.60%	92,734	148,400	1,595	10,748	Q3 2012	R/S/CP
Chang Ying	Beijing	93.50%	131,897	462,929	4,540	9,807	–	R/S/CP
Dao Yi II	Shenyang	91.30%	204,787	409,574	184	449	–	–
Lvshun Long He	Dalian	48.40%	608,701	669,724	1,363	2,035	Q4 2015	R/S/CP
Da Xing Project	Xi'an	91.30%	24,503	159,270	138	866	Q3 2012	R/S/H/O/CP
Total / Average			1,818,653	2,931,159	10,489	3,578		

Source: Company; Citi Investment Research and Analysis

Attributable landbank of 21.24m sqm GFA (24.4m sqm GFA landbank)

Now, Longfor's landbank has expanded into around 24.4m sqm GFA (attributable of 21.24m sqm GFA). Looking forward in 2H2010, Longfor will continue its expansion pace and mainly focus on second tier/third tier cities in the Yangtze River Delta and the Bohai Rim.

All of the existing 24.4m sqm GFA landbank is located in 11 cities: Chongqing, Chengdu, Beijing, Xi'an, Shanghai, Wuxi, Shenyang, Hangzhou, Qingdao, Changzhou and Dalian. As its hometown, Chongqing has an important position in Longfor's project portfolio while the company has been steadily diversifying into other cities.

Figure 10. Longfor- Landbank by City (sqm)

	City	Total GFA	Attributable GFA
P.B.R.	Beijing	2,086,404	1,913,213
	Shenyang	2,725,862	2,503,872
	Qingdao	622,240	522,682
	Dalian	669,724	324,146
Y.R.D.	Shanghai	931,041	788,558
	Wuxi	1,036,204	946,054
	Changzhou	2,043,930	1,844,584
	Hangzhou	591,214	591,214
Western	Chongqing	8,240,311	6,994,881
	Chengdu	3,388,682	2,991,552
	Xian	2,030,595	1,823,318
Total		24,366,207	21,244,074

Source: Company; Citi Investment Research and Analysis

Average land cost of RMB2,215/sqm GFA low as relative to ASP of RMB12,200/sqm GFA

One of the key assessment criteria includes quality and average cost. Though the cheap land price era has nearly come to an end along with the government's strict controls on new land supply, the entry point of the existing landbank largely decides the profitability of a developer in the coming several years. Moreover, the average cost of developer's landbank is critical for a developer's defensiveness in a market downturn.

Compared with most of its closest peers, Longfor's overall land cost appears to be quite reasonable with average land cost of around RMB2,215/sqm GFA. This is equivalent to 18.2% of its estimated RMB12,200/sqm ASP for its existing projects. Its average land cost/estimated ASP ratio is lower than all of the four top-tier developers and most of the second-tier property market leaders such as R&F, Gemdale and Greentown. It means Longfor could be more comfortable maintaining a sustainable reasonable gross margin, though Within Longfor's 24.4m sqm GFA landbank portfolio, the average land cost in its projects in Chongqing, Xi'an, Wuxi, Qingdao and Shenyang appears to be relatively low, only accounting for around 5-18% of estimated ASPs. The average land cost is much higher in Beijing, Shanghai and Chengdu, where Longfor has entered these markets for only 3-4 years and most new land supplies have been strictly controlled by the local governments, which forces developers to participate in public auction to acquire land plots.

Earning Revisions

We have fine-tuned the ASP of Longfor after the release of the interim result. Accordingly, earnings for 2011 and 2012 have been adjusted upward by 0.4% and 1.0% respectively.

Figure 11. Longfor – Earnings Revisions

Year to	Net Income (RMB mn)			FD EPS (RMB)			DPS (RMB)		
	Old	New	% Chg.	Old	New	% Chg.	Old	New	% Chg.
2010E	2,229	2,229	0.0%	0.433	0.433	0.0%	0.080	0.080	0.0%
2011E	3,984	4,001	0.4%	0.774	0.777	0.4%	0.090	0.090	0.0%
2012E	4,723	4,772	1.0%	0.917	0.927	1.0%	0.090	0.090	0.0%

Source: Company; Citi Investment Research and Analysis estimates

Financial Statements

Figure 12. Longfor – Income Statement (RMB mn)

As at 31 Dec	2005	2006	2007	2008	2009	2010E	2011E	2012E
Property development	1,831	1,991	3,334	4,216	11,029	13,853	20,811	25,508
Property investment	58	67	102	159	198	286	291	261
Others	30	42	62	100	147	176	211	253
Total Turnover	1,919	2,101	3,498	4,475	11,374	14,316	21,313	26,023
Property development	533	721	1,191	1,154	3,148	4,426	7,186	8,638
Property investment	47	0	0	0	147	206	215	198
Others	0	0	0	0	36	35	42	35
Unallocated income and corporate expenses	(32)	(236)	(461)	(634)	(353)	(675)	(1,051)	(1,401)
EBIT	549	485	729	520	2,978	3,993	6,392	7,470
Net Interest Expenses	6	10	8	(28)	26	33	(5)	(15)
Net Operating Profit	555	494	738	492	3,004	4,026	6,387	7,455
Share of Associates & JV	(0)	1	(14)	63	136	18	438	676
Exceptionals	73	482	901	125	599	0	0	1
Pretax Profit	627	977	1,625	681	3,739	4,044	6,826	8,132
Taxation	(268)	(338)	(724)	(281)	(1,247)	(1,526)	(2,202)	(2,753)
Minority Interest	(177)	(268)	(151)	(68)	(283)	(289)	(623)	(607)
Net Profit	183	371	750	332	2,209	2,229	4,001	4,772

Source: Company; Citi Investment Research and Analysis estimates

Figure 13. Longfor – Statement of Cash Flow (RMB mn)

As at 31 Dec	2005	2006	2007	2008	2009	2010E	2011E	2012E
OP Cash Flow before WC Change	553	491	708	596	3,577	3,993	6,392	7,471
Change in Working Capital	-874	-804	2,027	-1,795	1,382	-5,782	-6,628	-2,394
Operating Cash Flow	-322	-314	2,735	-1,199	4,960	-1,789	-236	5,077
Returns on inv/service of finance	-44	-157	-448	-924	-784	-1,239	-1,874	-2,286
Tax paid	-59	-85	-151	-386	71	-1,818	-1,150	-1,772
NCF from Operating Activities	-425	-556	2,135	-2,509	4,246	-4,847	-3,260	1,019
NCF from Investing activities	-168	-902	-6,403	-1,554	-3,642	-1,297	-311	-799
NCF before Financing	-593	-1,457	-4,268	-4,063	604	-6,143	-3,571	220
NCF from Financing activities	636	1,831	5,877	4,956	2,968	4,382	2,500	-493
Increase in Cash/Bank	42	374	1,608	893	3,573	-1,762	-1,070	-273
Beginning Cash/Bank	314	356	729	2,338	3,229	6,802	5,040	3,970
FX and Other Adjustments	0	-1	0	-2	0	0	0	0
Ending Cash/Bank	356	729	2,338	3,229	6,802	5,040	3,970	3,697
Net Debt	-938	-2,370	-5,591	-9,611	-2,964	-9,175	-12,745	-12,525
Net Gearing	83%	159%	195%	308%	24%	68%	75%	60%
OCF/Share		(0.08)	0.66	(0.29)	1.20	(0.35)	(0.05)	0.99

Source: Company; Citi Investment Research and Analysis estimates

Figure 14. Longfor – Financial Ratios

As at 31 Dec	2005	2006	2007	2008	2009	2010E	2011E	2012E
ROE	16.3%	28.3%	34.4%	11.1%	29.0%	17.4%	26.2%	25.0%
ROA	6.1%	9.0%	10.2%	3.2%	14.1%	9.9%	14.5%	14.6%
Net Gearing	83.4%	158.7%	194.9%	307.8%	24.4%	67.9%	74.7%	59.5%
Interest Cover	12.9	3.9	2.4	0.7	5.3	5.8	6.9	7.5
Property Sales Margin	29%	36%	36%	27%	29%	32%	35%	34%

Source: Company; Citi Investment Research and Analysis estimates

Figure 15. Longfor – Balance Sheet (RMB mn)

As at 31 Dec	2005	2006	2007	2008	2009	2010E	2011E	2012E
Investment properties	1,728	2,337	3,634	3,759	4,698	5,534	5,846	6,645
Properties under development	108	130	0	11	0	0	0	0
Properties and equipment	50	55	133	167	172	172	172	172
Other non-current assets	84	797	5,688	3,893	6,501	6,501	6,501	6,501
Fixed assets	1,969	3,319	9,455	7,830	11,372	12,208	12,519	13,318
Associates & JC entities	49	49	506	932	2,374	2,392	2,830	3,506
Deferred tax assets	16	45	72	348	228	228	228	228
Development Props	2,502	5,189	9,114	17,601	19,622	30,442	39,031	48,521
Bank balances & cash	356	729	2,338	3,229	6,802	5,040	3,970	3,697
Other current assets	718	758	1,155	2,456	2,049	1,668	1,731	1,967
Current Assets	3,576	6,676	12,607	23,286	28,472	37,150	44,732	54,185
Loans & overdrafts	387	649	3,176	6,480	3,710	5,439	5,625	4,818
Deposits and payables	2,019	3,778	9,096	13,844	16,362	20,303	21,403	27,749
Tax payables	176	381	688	936	1,616	1,324	2,375	3,356
Other current liabilities	12	37	154	102	364	364	364	364
Current liabilities	2,593	4,845	13,114	21,361	22,052	27,429	29,767	36,287
Total Net assets	3,017	5,244	9,526	11,035	20,393	24,548	30,542	34,949
Long term bank loans	907	2,450	4,772	6,360	6,055	8,776	11,090	11,404
Other long-term liabilities	227	304	625	731	1,099	1,099	1,099	1,099
Long term liabilities	1,133	2,754	5,397	7,091	7,154	9,874	12,189	12,503
Minority interests	760	997	1,259	822	1,100	1,158	1,282	1,404
Shareholders' funds	1,124	1,494	2,869	3,123	12,139	13,516	17,071	21,043
Total capital employed	3,017	5,244	9,526	11,035	20,393	24,548	30,542	34,949
Book Value Per Share		0.36	0.69	0.75	2.36	2.62	3.31	4.09
Target P/B		23.29	12.12	11.14	3.56	3.19	2.53	2.05
P/B					2.61	2.34	1.86	1.51

Source: Company; Citi Investment Research and Analysis estimates

Longfor Properties

Company description

Founded in 1994, Longfor started its property development business in Chongqing, which is the hometown of the founder and Chairwoman Madam Wu. In 1997, Longfor commenced development of its first property project in Chongqing - Longhu Garden Nanyuan. Later, Longfor developed Longfor Garden Xiyuan, Fragrant Forest (one of the most reputable high-end villa projects in Chongqing), Crystal Town, Blue Lake County (the biggest pure villa/townhouse project in Chongqing), Chongqing Fairy Castle, Hill of Good Hope, Bamboo Grove (one of the most successful high-rise/townhouse complex projects in Chongqing) and many other projects. Besides these well-known residential projects in Chongqing, Longfor also developed many commercial property projects in Chongqing, including a popular shopping mall - North Paradise Walk and West Paradise Walk. In the past 13 years, Longfor has developed 15 projects with approximately 4.55m sqm GFA of properties sold in Chongqing. Longfor has successfully developed the ability to offer a wide spectrum of high-quality property products in Chongqing, including villa, townhouse, high-rise apartment, shopping mall, office etc, which gives it a broad customer base and diversifies risks.

Investment strategy

We rate Longfor Properties shares as Buy/Low Risk. Longfor is now trading at a significant discount to NAV, which is attractive in our view, given strong contracted sales, quality products and valuable 24.4mn sqm GFA landbank. We consider Longfor Properties one of the best candidates among the 2nd-tier developers to advance into the top-tier developer group, thereby triggering a further stock re-rating. After the completion of product differentiation and diversification during its earlier expansion, Longfor is now looking at a new round of aggressive geographical expansion. We view Longfor as a candidate to jump from second-tier to first-tier status given this growth in the context of: 1) competitive products and proprietary bank of products; 2) prestigious brand name; 3) attractive geographical exposure with reasonable land cost (RMB2,215/sqm GFA); 4) scalable organization structure, and 5) proven expansion capability and differentiating development strategy.

Valuation

Our target price for Longfor of HK\$9.81 (Prev. HK\$9.78/sh) is based on 20% discount to our 2010E NAV, with our discount rate factoring in heightened policy risk in China's property sector. We estimate Longfor's 2010E NAV to be HK\$12.26/sh (prev. HK\$12.22/sh), based on our estimated property values, excluding net debt. We adjusted the NAV slightly after fine-tuning the ASP. The appropriate valuation methodology that should be applied to a property company is the subject of diverse views. Clearly, being an asset-based business, an NAV-based methodology has its appeal. However, when the companies are growing their revenue and profits very rapidly, as was the case in the past 2-3 years, given the high asset turnover inherent in the property development versus the property investment business, many would argue that the NAV approach is too conservative. In fact, some analysts have suggested that property companies be valued on a strict P/E basis and treated like consumer stocks due to the expected rapid growth ahead. We believe no single methodology that can provide a conclusive or authoritative valuation benchmark. The NAV methodology seems to break down because analysts

cannot revise NAV estimates quickly enough to match the new land acquired or the changes in property prices. Moreover, in a rising market, investors are imputing a forward-looking element into what they perceive to be the fair value of the property company.

Figure 16. Longfor – Breakdown of NAV

	NAV (HK\$m)	NAV (HK\$/Share)	% of NAV	% of GAV
Development Properties				
Residential	53,514	10.39	84.8%	68.6%
Retail	4,741	0.92	7.5%	6.1%
Office	1,477	0.29	2.3%	1.9%
Carparks	763	0.15	1.2%	1.0%
Subtotal Development Properties	60,495	11.75	95.8%	77.5%
Investment Properties				
Office	0	-	0.0%	0.0%
Retail	17,525	3.40	27.8%	22.5%
Serviced Apartments	0	-	0.0%	0.0%
Subtotal Investment Properties	17,525	3.40	27.8%	22.5%
Others	0	-	0.0%	0.0%
Gross Asset Value (GAV)	78,020	15.15	123.6%	100.0%
Net Cash/(Debt)	(10,734)	(2.08)	-17.0%	
Potential LAT Liabilities	(4,162)	(0.81)	-6.6%	
NAV	63,124	12.26	100.0%	

Source: Company; Citi Investment Research and Analysis

Risks

Our quantitative risk-rating system suggests a Medium Risk rating for the stock given its short listing history (Longfor was listed in the Stock Exchange of Hong Kong in November 2009). Given that Longfor has a relatively strong balance sheet and operational position after its IPO, we believe a Low Risk rating is more appropriate. Longfor is exposed to property markets and the primary land market in mainland China. The most notable downside risks to Longfor are economic and policy-related. With regard to economic risks, we think that any weaker-than-expected GDP growth for the Chinese and/or global economies, and the risk of a hard landing in the domestic economy could negatively affect buyers' sentiment toward China's property markets, which could render our revenue and earnings estimates for Longfor optimistic. In addition, we think that any stronger-than-expected pickup in inflation could result in a sharp rise in interest rates, which would affect housing affordability of homebuyers. This could also attract new austerity measures, which could further dampen sentiment in the housing market and so land values. In addition, the income generated by its investment properties will also be affected. On the policy front, any tightening measures and policy changes by the central government with regard to mortgage applications and approvals, project financing, and property pre-sales to curb speculation and overinvestment could adversely affect the bottom lines and cash flows of property developers, and homebuyer sentiment.

Appendix A-1

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Longfor Properties (0960.HK)

Ratings and Target Price History

Fundamental Research

Analyst: Oscar Choi

Covered since December 23 2009

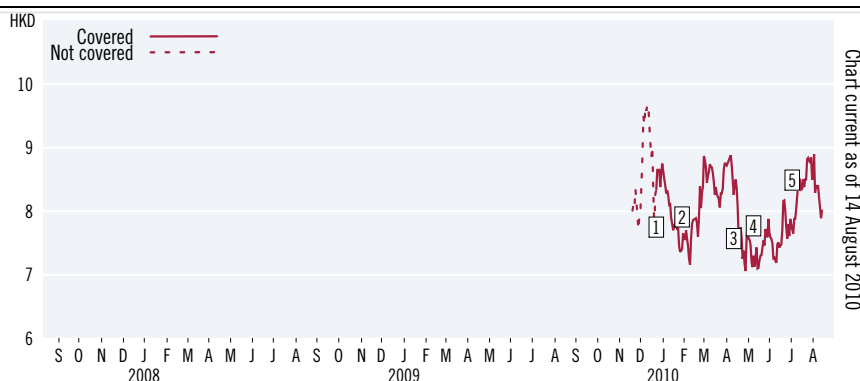


Chart current as of 14 August 2010

	Date	Rating	Target Price	Closing Price
1	23-Dec-09	*1L	*11.09	8.34
2	28-Jan-10	1L	*11.32	7.41

	Date	Rating	Target Price	Closing Price
3	12-Apr-10	1L	*12.12	8.26
4	10-May-10	1L	*9.74	7.30

	Date	Rating	Target Price	Closing Price
5	2-Jul-10	1L	*9.78	7.71

* Indicates change

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