

Analyst: Anita Hwang

Main Board Listing – Research

KWG Property Holdings Limited [Stock Code: 1813] 合景泰富地產控股有限公司

Global coordinator, bookrunner, and underwriter : Morgan Stanley

Joint sponsors : Morgan Stanley Goldbond Securities ICEA Capital

Sector : Real Estate

Business : Real Estate development

Total share offer: <u>625,000,000</u> shares (25 % of the enlarged share capital) Public Offer: 62,500,000 shares (10%) Placing: 562,500,000 shares (90%) Greenshoe: 93,750,000 shares	<u>Business of KWG Property Holdings (KWG)</u> KWG is a property developer based in Guangzhou and it started its property development activities in 1995. It focuses on medium to high-end residential property developments mostly in prime areas in Guangzhou. Commercial properties, such as office buildings, serviced apartments and hotels were also added to the portfolio. KWG is currently developing 3 hotels in Guangzhou, including one of China's first W Hotels. KWG had 15 projects that were completed, under development or held for development. There are 10 projects under development or held for future development, including 4 projects in central business district (CBD) with a total GFA of 1.98 million sq.m as of 31 Mar 2007. The company provided a FY07E profit forecast with net profit attributable to shareholders after fair value gains on investment properties estimated to be no less than RMB2,516 million. Should the fair value gains be stripped out, the FY07E net profit attributable to shareholders would be some RMB961.1 million.
Price: HK\$5.90– HK\$7.28 per share Market Cap: HK\$14.75 – HK\$18.20 billion Pro-forma fully diluted FY07 PER: 15.1X – 18.7X (before fair value gains on investment properties) 5.7X – 7.1X (after fair value gains on investment properties) Adjusted NTA per share: HK\$1.82 – HK\$2.15 Staffing: 848	
HK Public Offer period: 18 th June 07 – 22 nd June 07 noon Receiving bank: ICBC (Asia) Bank of China (HK) The Bank of East Asia Share registrar: Computershare Hong Kong Investor Services Limited Listing date: 3 rd July 2007	

Major Shareholders after Listing (Assuming the over-allotment option is not exercised)

Mr. Kong Jian Min, the founder, executive director, and the Chairman	67.5%
SSF Swift, a company wholly-owned by property funds managed by affiliates of Morgan Stanley	7.5%
Public shareholders*	25.0%
	<u>100.0%</u>

Remarks: () KWG and the global coordinator have entered into corporate placing agreements with each of the following cornerstone investors:*

This report has been prepared solely for information purposes and we are not soliciting any action based upon it. Neither this document nor its contents shall be construed as an offer, invitation, advertisement, inducement or representation of any kind or form whatsoever. The information is based upon information, which we consider reliable, but accuracy or completeness is not guaranteed. Opinions expressed herein are subject to change without notice. At time of this report, East Asia Securities Company Limited has no position in securities of the company or companies mentioned herein, while its group companies may from time to time have interests in securities of the company or companies mentioned herein.



- **Dr. Lee Shau Kee**, through Junford Limited, will subscribe for HK\$333.3 million worth of shares (or some 2.02% of the enlarged share capital).
- **Li Sze Lim and Zhang Li**, chairman and vice-chairman respectively of Guangzhou R&F Properties, through Century Land Properties Limited, will subscribe for HK\$333.3 million worth of shares (or some 2.02% of the enlarged share capital).
- **CITIC Pacific Limited** (0267.HK), through Bloomway Enterprises Holdings Ltd., will subscribe for HK\$166.67 million worth of shares (or some 1.01% of the enlarged share capital).
- **Mr. Yung Chi Kin**, through Kason International Holdings Ltd., will subscribe for HK\$166.67 million worth of shares (or some 1.01% of the enlarged share capital).
- **Mr. Kwok Ping-Kwong Thomas**, will subscribe for HK\$150 million worth of shares (some 0.91% of the enlarged share capital).

Use of Proceeds

Net proceeds from the offer are estimated to be HK\$3,540 million – HK\$4,368 million. (Assuming the offer price range of HK\$5.90 – 7.28 per share and assuming the over-allotment option is not exercised)

	HK\$ million
To repay debt	600
To finance land costs for the Suzhou City and Conghua City projects	1,200
To finance construction costs for Guangzhou Science City, Suzhou City, Ling Feng, Sky Ville and Conghua City projects	1,780
For general working capital	Remaining

Financial Highlights

RMB million	Year ended 31 st December		
	2004	2005	2006
Revenue	545.0	437.7	654.6
Gross profit	144.2	168.9	202.2
Operating profit before changes in fair value of investment properties	117.0	120.2	143.1
Fair value gains on investment properties	74.8	112.1	151.6
Profit for the year	128.4	133.0	157.2
Gross Margin	26.5%	38.6%	30.9%
Operating Margin (before changes in fair value of investment properties)	21.5%	27.5%	21.9%
Net Margin	23.6%	30.4%	24.0%

Breakdown of turnover by activities

Year ended 31 st December	2004		2005		2006	
	RMB million	%	RMB million	%	RMB million	%
Property development	541.9	99.4%	431.7	98.6%	646.9	98.8%
Property investment	2.4	0.4%	2.9	0.7%	3.4	0.5%
Property management	0.7	0.1%	3.2	0.7%	4.4	0.7%
Total	545.0	100.0%	437.7	100.0%	654.6	100.0%

**Strengths/Opportunities**

- ✓ **Diverse property portfolio** In addition to the mid-end residential projects, KWG has also expanded into building residential communities with designed landscape, luxury residential projects, such as Cosmos, and investment properties.

International Financial Place (IFP), a Grade-A office building offering a GFA of 61,363 sq. m. in Tianhe district of Guangzhou, is scheduled for completion in June 2007. According to the management, the average rent would be around RMB200 /sq m. in those secured rental contracts (remarks: according to Knight Frank, the average rent for prime office in Guangzhou in 1Q07 was around USD16.7 / sq m.

KWG is developing 3 hotels in Guangzhou City: a W-Hotel in CBD, a Sheraton Resort Hotel and a Four Points by Sheraton Hotel. These hotels will be operated by the Starwood Group, which is the operator of several well-known hotel brands, including Sheraton, Westin, W Hotels, Le Meridien and St. Regis Hotels.

- ✓ **Ample land bank at low cost** A large portion of land bank was acquired at very low cost, with the development margin before LAT in the range of 50% for some of the high-end projects.
- ✓ **Good growth prospect** For the year ended 31 Dec 2004, 2005 and 2006, KWG delivered an aggregate GFA of 140,516 sq. m., 100,176 sq. m. and 121,692 sq. m., respectively, representing an average realized selling price of RMB3,856.5, RMB4,309.4 and RMB5,315.9 respectively. Based on the profit forecasts given by KWG, the net profit for FY07E (net of fair value gains) is estimated to be no less than RMB 961.1 million, which is about 5 times higher than that in FY06. The forecast is well-supported as over 320,000 sq. m. are expected to be booked in FY07E and another 600,000 sq. m. in FY08E as various projects complete. These projects will likely be sold at significantly higher average selling price because of larger contribution from higher-end products, The Cosmos, which is expected to sell at RMB20,000 / sq m.
- ✓ **Reasonable valuation** The IPO price range of KWG at a FY07E pro-forma fully diluted PER range of 15.1X – 18.7X should be reasonable when compared with its peers. HK-listed peers with strong operations in Guangdong include Guangzhou R&F Properties (2777), Agile Property (3383), Hopsun Development (0754) and Country Garden (2007). The peers' FY07E PER range is 12.4X to 25.9X with an average of 19.4X. From a discount/premium to NAV perspective, the comparable peers trade at a discount of 10% to a premium of about 20%. KWG is priced at about 5% to 19% discount to its NAV.

Weaknesses/Threats

- × **High concentration in Guangzhou** Before securing the land use rights for the land in Suzhou City and Conghua City, all of KWG's projects are in the Guangzhou area. This single city exposure can put KWG at a very disadvantaged position in the event of any regulatory changes targeting Guangzhou or the Guangdong province. In terms of gross asset value, property projects in Guangzhou accounted for 71%, while the Group's pending projects in Suzhou made up 24% and the planned Conghua project accounted for the remaining 5%.
- × **Abundant supply of office space in Guangzhou** According to Jones Lang LaSalle's research, there will be 722,000 sq. m of new supply of office space in Guangzhou in 2007. While the demand for premium office space in Guangzhou is strong, supply is likely to remain abundant.

Recommendation: Buy



Important Disclosure / Analyst Certification / Disclaimer

This document is published by East Asia Securities Company Limited, a wholly-owned subsidiary of The Bank of East Asia, Limited (BEA).

The research analyst primarily responsible for the content of this report, in part or in whole certifies that the views on the companies and their securities mentioned in this report accurately reflect his/her personal views. The analyst also certifies that no part of his/her compensation was, is, or will be, directly, or indirectly, related to specific recommendations or views expressed in this report.

This report has been prepared solely for information purposes and has no intention whatsoever to solicit any action based upon it. Neither this report nor its contents shall be construed as an offer, invitation, advertisement, inducement or representation of any kind or form whatsoever. The information is based upon information, which East Asia Securities Company Limited considers reliable, but accuracy or completeness is not guaranteed. Information and opinions expressed herein reflect a judgment as of the date of this document and are subject to change without notice. Any recommendation contained in this report does not have regard to the specific investment objectives, financial situation and the particular needs of any specific addressee. This report is not to be taken in substitution for the exercise of judgment by respective readers of this report, who should obtain separate legal or financial advice. East Asia Securities Company Limited and / or The BEA Group accepts no liability whatsoever for any direct or consequential loss arising from any use of this report or further communication given in relation to this report.

At time of this report, East Asia Securities Company Limited has no position in securities of the company or companies mentioned herein the report, while BEA along with its affiliates and/or persons associated with any of them may from time to time have interests in the securities mentioned in this report. BEA and its associates, its directors, and/or employees may have positions in, and may effect transactions in securities mentioned herein and may also perform or seek to perform broking, investment banking and other banking services for these companies.

BEA and/or any of its affiliates may beneficially own a total of 1% or more of any class of common equity securities of the subject company or companies mentioned in this report and may, within the past 12 months, have received compensation and/or within the next 3 months seek to obtain compensation for investment banking services from the subject company or companies mentioned in the report.

This document is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of, or located in, any locality, state, country or other jurisdiction, publication, availability or use would be contrary to law and regulation.