



Feb 3, 2016  
Company Report  
Rating: BUY  
TP: HK\$ 2.90

Share price (HK\$) 2.01  
Est. share price return 44.3%  
Est. dividend yield 0.0%  
Est. total return 44.3%

Previous Rating & TP NA  
Previous Report Date NA

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**Key Data**

52Wk H/L(HK\$)	4.2/1.7
Issued shares (mn)	4,694
Market cap (HK\$ mn)	9,387
3-mth avg daily turnover (HK\$ mn)	2.62
Major shareholder(s) (%)	
Mr WONG Hong King	75.00

Source(s): Company, Bloomberg, ABCI Securities

**FY14 Revenue breakdown (%)**

Property development	88.7
Property investment	7.2
Comprehensive services	4.1

Source(s): Company, ABCI Securities

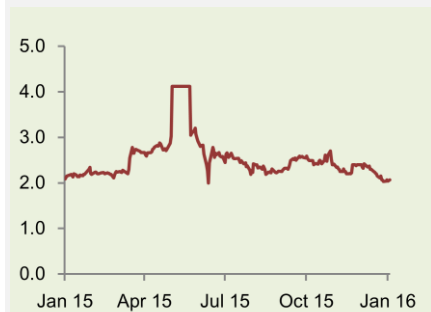
**Share performance (%)**

	Absolute	Relative*
1-mth	(15.7)	(5.7)
3-mth	(18.1)	(5.6)
6-mth	(23.0)	(4.1)

\*Relative to HSI

Source(s): Bloomberg, ABCI Securities

**1-Year stock performance (HK\$)**



Source(s): Bloomberg, ABCI Securities

LVGEM (95 HK)

A promising Shenzhen property play; initiate BUY

- LVGEM (China) has become a major developer in Shenzhen after asset injection
- Quality projects in Futian should ensure good presales and profitability in 2016E-17E
- Rental income rose 30% YoY in 2014 to RMB 352mn on the back of rising LFA
- Urban redevelopment provides LVGEM with cheap land sources
- Initiate **BUY** with TP of HK\$2.9 based on a 50% discount to NAV

**Becoming a major player in the Shenzhen property market.** Following the asset injection of HK\$13,785mn, LVGEM (China) will become a sizeable developer with over 3.6mn sqm of GFA in land reserves, of which 1.4mn sqm will be located in Shenzhen. LVGEM is set to benefit from the rising property market in the region.

**Quality projects located in Futian.** The injected properties include two major projects in Futian district of Shenzhen- Hongwan Garden (虹灣花園) and Mangrove Luxury Garden (紅樹華府). Presales of Hongwan Garden were a success with ASP increasing steadily from RMB 47,500/sqm in Jan 2015 to RMB 62,000/sqm in Dec 2015, according to Fang.com. For Mangrove Luxury Garden, we expect a better ASP given the better environment surrounding the project. We estimate presales would rise from RMB 5.7bn in 2015E to RMB 8.2bn in 2017E, implying a 20% CAGR over the period.

**Rising rental income.** A quality rental portfolio in Shenzhen with an LFA of 0.22mn sqm (as of Apr 2015) is now under LVGEM's ownership after the injection. Driven by Neo Urban commercials and Zoll Centers, rental income jumped 30% YoY in 2014 to RMB 352mn. Going forward, we expect rental income to grow at an 18% CAGR in 2015E-17E upon completion of the new Zoll Centers.

**Cheap land sources from urban redevelopment.** Ten out of 16 completed projects are obtained through urban redevelopment scheme that usually entails a low land cost, although the acquisition process could be lengthy. Hence, gross margin rose steadily from 25.1% in 2012 to 34.3% in 2013 and 46.4% in 2014.

**Initiate BUY with TP of HK\$ 2.90 based on a 50% discount to NAV.** We conduct our valuation for LVGEM based on the discount-to-NAV method. We apply the DCF with a WACC of 10.4% for the property development segment (RMB 20.0bn) and a 3% cap rate for the investment properties (RMB 17bn). A 50% discount is applied to our 2016E NAV estimate of RMB 23.0bn (or HK\$ 5.78/share) to derive our TP that arrives at HK\$ 2.90. Initiate **BUY**.

**Risk factors:** 1) Long relocation process; 2) Complicated regulations governing the redevelopment process; 3) Further tightening policies on the property market

**Results and Valuation**

FY ended Dec 31	2013A	2014A	2015E	2016E	2017E
Revenue (RMB mn)	1,971	4,851	2,350	8,696	10,190
Chg (% YoY)	306.3	146.2	(51.6)	270.1	17.2
Core net profit (RMB mn) <sup>1</sup>	273	1,200	287	1,807	2,390
Chg (% YoY)	(297.8)	339.6	(76.1)	529.2	32.3
Underlying EPS (RMB)	0.06	0.26	0.04	0.22	0.29
Chg (% YoY)	(297.8)	339.6	(86.1)	529.2	32.3
BVPS (RMB)	1.11	1.48	0.89	1.03	1.20
Chg (% YoY)	15.1	33.1	(39.7)	14.8	17.0
Underlying PE (x)	29.3	6.7	48.2	7.7	5.8
P/B (x)	1.5	1.2	1.9	1.7	1.4
ROE (%)	5.2	17.3	4.0	21.7	24.6
ROA (%)	1.5	5.9	1.1	6.4	7.8
DPS(HK\$)	-	-	-	0.09	0.12
Yield (%)	-	-	-	4.5	6.0
Net gearing <sup>2</sup> (%)	84.8	88.5	60.7	105.6	94.7

<sup>1</sup>Core net profit = Net profit - revaluation gain of investment properties and one-off items

<sup>2</sup>Net gearing = Net debt / Shareholders' equity

Source(s): Bloomberg, ABCI Securities estimates

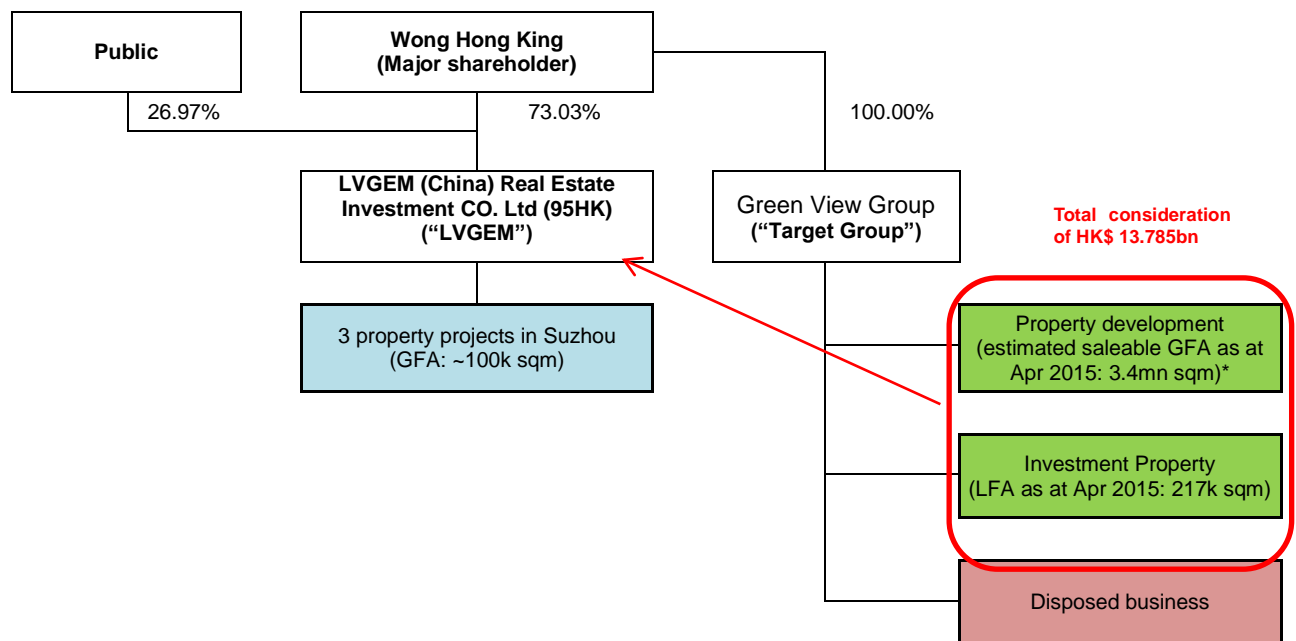


## Transforming into a Shenzhen play after asset injection

LVGEM (China) (95 HK) completed its asset injection in Nov 2015. LVGEM acquired the property segment of the Target Group (Green View Group) owned by the major shareholder of LVGEM, Mr. Wong Hong King. Total consideration for the injection was HK\$ 13,785mn. After the injection, LVGEM has transformed itself from a small Suzhou developer (with a 0.1mn sqm landbank as of Dec 2014) to a major Shenzhen player with an estimated land reserve of 3.4mn sqm GFA and 217k of leasable floor area (LFA) of completed investment property as of Apr 2015.

The whole transaction is financed by a share issuance at HK\$ 2.20 in the following structure: 1) 300mn shares were issued to Vanke, the largest developer in China; 2) 300mn shares were issued to Ping An, the leading insurance firm in China; 3) 200mn shares were issued to professional and institutional investors; 4) 2,509mn ordinary shares and 3,413mn convertible shares (at HK\$2.06) were issued to Mr. Wong

Exhibit 1: Asset injection in Nov 2015



Source(s): Company, ABCI Securities

Exhibit 2: Shareholding structure after injection (Nov 2015)

	Before injection		After injection			Assume all convertible shares are converted	
	No. of shares	% of total	No. of shares	Number of convertible shares	% of total	No. of shares	% of total
<b>Shareholders</b>	mn	%	mn	mn	%	mn	%
Mr Wong and his associates	1,011	73%	3,520	3,413	75%	6,934	86%
Vanke	-	0%	300	-	6%	300	4%
Ping An	-	0%	300	-	6%	300	4%
Placees	-	0%	200	-	4%	200	2%
Public shareholders	373	27%	373	-	8%	373	5%
<b>Total</b>	<b>1,384</b>	<b>100%</b>	<b>4,694</b>	<b>3,413</b>	<b>100%</b>	<b>8,107</b>	<b>100%</b>

Source(s): Company, ABCI Securities



Exhibit 3: Landbank of the Target Group (Apr 2015)

	City	Stake	Construction start	Completion	Saleable GFA-presold	Saleable GFA-unsold	Leasable GFA
					000sqm	000sqm	000sqm
<b>Completed</b>							
LVGEM Shan Zhuang (綠景山莊)	Shenzhen	100%	Apr-98	Apr-00	-	0	4
LVGEM Xin Yuan Phase I (綠景新苑一期)	Shenzhen	100%	Sep-00	Jan-02	-	-	-
LVGEM Xin Yuan Phase II (綠景新苑二期)	Shenzhen	100%	May-03	Feb-04	-	-	5
Lanwan Peninsula (藍灣半島社區)	Shenzhen	100%	May-02	Aug-04	-	0	5
Phase II of LVGEM Garden (綠景花園二期)	Shenzhen	100%	Nov-03	Jun-05	-	1	21
Zhongcheng Tianyoi Garden (中城天邑花園)	Shenzhen	100%	Mar-06	Dec-08	-	0	-
LVGEM Hotel (綠景錦江酒店)	Shenzhen	100%	Mar-06	Dec-08	-	-	4
Zhonghe Tixiang Famous Garden, Phase I 中核繞香名苑一期	Yiyang	100%	Aug-07	Apr-09	-	4	-
NEO Complex, Tower A, B and C (綠景紀元大廈 NEO A, B, C 座)	Shenzhen	100%	Jan-04	May-11	-	-	106
City Garden (城市立方花園)	Shenzhen	100%	Mar-08	Nov-10	-	2	5
LVGEM Chanson Garden (綠景香頌花園)	Shenzhen	100%	Feb-11	Dec-12	-	0	23
LVGEM Chanson Meilu Garden (綠景香頌美廬園)	Shenzhen	100%	May-11	May-13	-	-	0
LVGEM 1866 Garden (公館 1866 花園(南區、北區))	Shenzhen	100%	Jun-11	Aug-13	-	4	43
LVGEM International Garden 綠景國際花城( A1 區 )	Maoming	100%	Jul-13	Dec-14	-	38	-
<b>Subtotal</b>					-	<b>49</b>	<b>217</b>
<b>Under development</b>							
Hongwan Garden (虹灣花園)	Shenzhen	100%	Dec-12	Oct-15	23	114	34
LVGEM International Garden, Block A2 化州國際花城( A2 區 )	Maoming	100%	Mar-14	Nov-15	56	144	25
Mangrove Luxury Garden (紅樹華府)	Shenzhen	100%	Jul-14	Mar-17	-	123	21
<b>Subtotal</b>					<b>80</b>	<b>381</b>	<b>80</b>
					<b>Site Area</b>	<b>Estimated total GFA</b>	
<b>For future development</b>							
					<b>000sqm</b>	<b>000sqm</b>	
Land Lot of LVGEM International Garden, 綠景國際花城地段	Maoming	100%	2016		715	2,000	
Zhonghe Tixiang Famous Garden, Phase II 中核繞香名苑二期	Yiyang	100%	2016		27	95	
<b>Subtotal</b>					<b>742</b>	<b>2,095</b>	
<b>Projects planned to be redeveloped or contracted to be acquired</b>							
Mei Jing 美景	Shenzhen			TBD	14	90	
Liguang 黎光	Shenzhen			NA	271	726	
<b>Subtotal</b>					<b>285</b>	<b>816</b>	

Source(s): Company, ABCI Securities

Following the asset injection, LVGEM's revenue will enlarge by almost 10 times while its net income will swing into a profit of RMB1.2bn based on its FY14 figures. With a larger balance sheet and higher turnover, LVGEM could take up large or premium sites that were previously considered unaffordable.

Exhibit 4: Key financials of Target Group (FY14)

	LVGEM China (95 HK)	Target group (unlisted)
	HK\$mnn	RMBmnn
Revenue	524	4,851
YoY change	147%	146%
Gross profit	108	2,357
YoY change	342%	191%
Gross margin	21%	49%
Core profit (excl. one- off items)	(11)	1,200
YoY change	NA	340%
Core net margin	NA	24.7%

Source(s): Company, ABCI Securities

## Three core strengths arise in LVGEM after the injection

### 1. Quality projects located in Futian CBD

The two major projects in Shenzhen - Hongwan Garden (虹灣花園) and Mangrove Luxury Garden (紅樹華府), which were injected into the Group in 2015, will be the key presales and earnings driver for LVGEM in 2016-17.

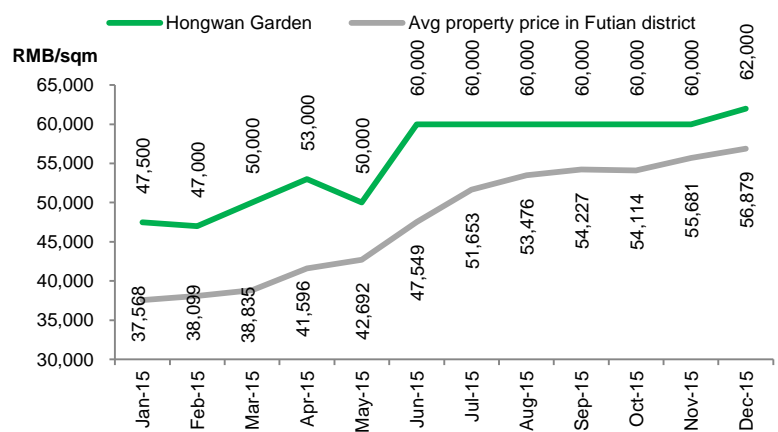
- Hongwan Garden (虹灣花園):** Hongwan Garden is a residential and commercial project conveniently located in the CBD of Futian district, Shenzhen, and is adjacent to the Mei Lin metro station. It consists of five high-rise residential buildings, two apartment buildings and a retail shopping mall. Along with the rising property price in Shenzhen, Hongwan Garden's ASP increased by 31% from RMB 47,500/sqm in Jan 2015 to RMB 62,000/sqm in Dec 2015, according to Fang.com. We forecast this project would generate RMB 3.6bn/ RMB 1.7bn in presales for 2015E/16E, and RMB 5.3bn in booked revenue for 2016E upon completion.

Exhibit 5: Hongwan Garden (虹灣花園)



Source(s): fang.com

Exhibit 6: ASP of Hongwan Garden (虹灣花園) vs. average property price in Futian



Source(s): Fang.com, ABCI Securities

Exhibit 7: Location of Hongwan Garden (虹灣花園)



Source(s): fang.com

Exhibit 8: Details of Hongwan Garden (虹灣花園)

Total GFA	367.4k sqm
LFA of commercial area <A>	34k sqm
GFA presold <B>	23k sqm
Unsold saleable residential GFA <C>	113k sqm
Total development cost <D>	RMB2.7bn
land and construction cost per sqm <D/(A+B+C)>	RMB19,728/sqm
Construction start	Dec 2012
Launch of presales	Oct 2014
Expected completion	Oct 2015

Source(s): Company, ABCI Securities

- Mangrove Luxury Garden (紅樹華府):** Mangrove Luxury Garden is a residential and commercial project conveniently located in southeast corner of the intersection of Shazui Road and Jindyi Road in the CBD of Futian district. In addition to the shopping center, the project will have three residential towers and an integrated building with offices, a hotel, and apartments. Presales should commence in 2016, and we expect its ASP to be higher than that of Hongwan Garden given the former's spectacular sea view.

**Exhibit 9: Mangrove Luxury Garden (紅樹華府)**


Source(s): fang.com

**Exhibit 10: Mangrove Luxury Garden (紅樹華府)**


Source(s): Company, ABCI Securities

**Exhibit 11: Location of Mangrove Luxury Garden (紅樹華府)**


Source(s): fang.com, ABCI Securities

**Exhibit 12: Details of Mangrove Luxury Garden (紅樹華府)**

Total GFA	305k sqm
LFA of commercial area <A>	20.5k sqm
Unsold saleable residential GFA <B>	123k sqm
Estimated total development cost <C>	RMB2.0bn
land and construction cost per sqm <C/(A+B)>	RMB13,938/sqm
Construction start	Jul 2014
Launch of presales	4Q2015
Expected completion	Mar 2017

Source(s): Company, ABCI Securities

- Projects to be redeveloped or acquired in Shenzhen:** Apart from the above two projects under development, the asset injection also contains two projects (Meijing and Liguang) with the land redevelopment/ land acquisition proceedings in process.

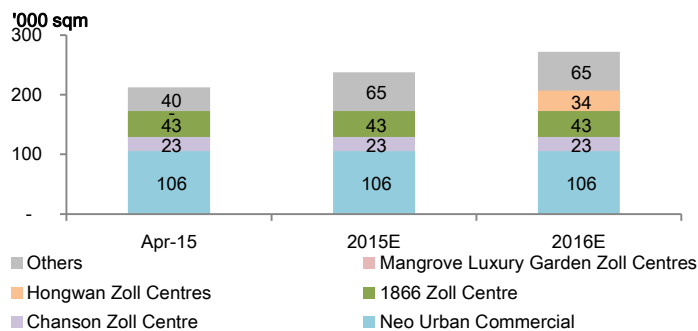
**1) Meijing project (美景):** The Meijing project is located on No. 4088 Qiaoxing Road in Nanshan district. It is situated in a well-developed area complemented with public transport facilities and is within walking distance to the Railway Line 1 and 2. Currently, the project has a site area of 13,865sqm with six industrial buildings with a total GFA of 30,569 sqm. It is 40% owned by the Target group and 60% owned by Shenzhen Shawei Industrial Co. Ltd, a villager-representative company. The project is scheduled to be redeveloped into an industrial complex and existing buildings should be demolished in 1-2 years. The project has been submitted to relevant authorities for approval. Upon successful application, a total GFA of 89,848 sqm will be granted.

**2) Liguang project (黎光)** : The project is in Liguang Village, Guanlan Town, Bo'an District, Shenzhen. Liguang project is situated in a mature residential area near Guanlanhu Liguang Golf Club. A total site area of 271k sqm will be developed into a residential, commercial and industrial complex. The Target Group has entered into agreements with relevant parties to acquire the development right of the project. The name of the project has yet to be determined.

## 2. The Zoll Centers: LVGEM's flagship commercial property to drive rental income

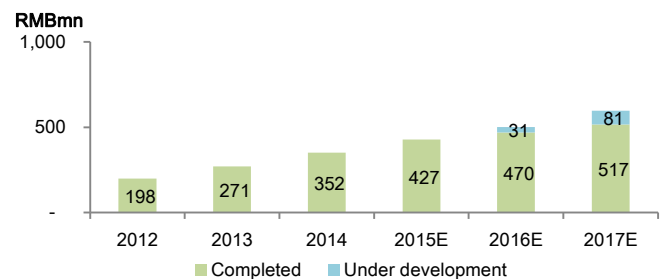
A quality rental portfolio in Shenzhen with an LFA of 0.22mn sqm (as of Apr 2015) is now under LVGEM's ownership after the injection. The portfolio registered impressive rental income growth of 30%YoY in 2014. The two core properties, Neo Urban commercials and Zoll centers, contributed to 86% of total rental income (RMB 352mn) in 2014. Upon completion of new Zoll centers, we expect rental income to rise further.

**Exhibit 13: LFA of LVGEM's investment properties**



Source(s): Company, ABCI Securities estimates

**Exhibit 14: Breakdown of rental revenue**



Source(s): Company, ABCI Securities estimates

**Exhibit 15: Rental income breakdown**

(RMBmn)	2012	2013	2014	CAGR	4M14	4M15	YoY
<b>Zoll Centers</b>							
- Chanson Zoll Centers	-	14	37	NA	11	12	10%
- 1866 Zoll Centers	-	-	14	NA	0	12	6428%
<b>Neo Urban Commercial Complex</b>	152	207	249	28%	86	95	11%
<b>Others</b>	46	50	51	5%	10	12	21%
<b>Total</b>	<b>198</b>	<b>271</b>	<b>352</b>	<b>33%</b>	<b>108</b>	<b>132</b>	<b>23%</b>

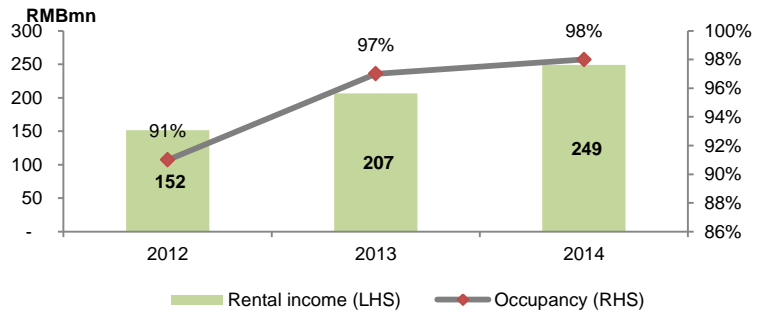
Source(s): Company, ABCI Securities

- Neo Urban Commercials:** The Neo Urban Commercial Complex, which commenced operations in May 2011, is a large urban complex located at the junction of Shennan Boulevard and Tairan Boulevard at the CBD of Futian District, Shenzhen. The complex comprises of three main buildings- Tower A is a skyscraper that offers Grade A offices, while Tower B and C offer office, retail and residential spaces. As at Apr 2015, the Target Group owns a substantial portion of Tower A and all retail spaces in Tower B and C; the aggregate LFA owned by the Group in this project is 106k sqm.

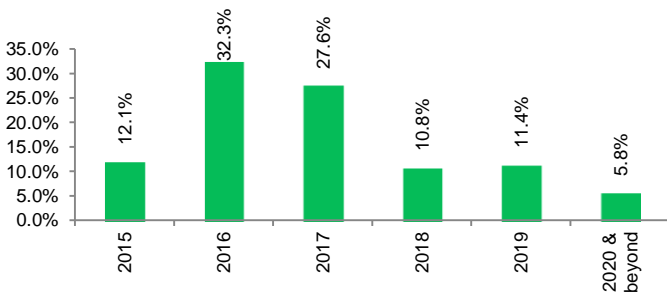
According to Jones Lang LaSalle (JLL), rental rate of Grade A office in Shenzhen grew 9.0%YoY in 2013 and 17.9% in 2014, higher than other tier-one cities. With an occupancy rate close to 98%, we believe the rental rate of Neo Urban Commercials is likely to rise, especially since 32.3%/27.6% of the tenancy will expire in 2016/2017.

**Exhibit 16: Neo Urban commercials**

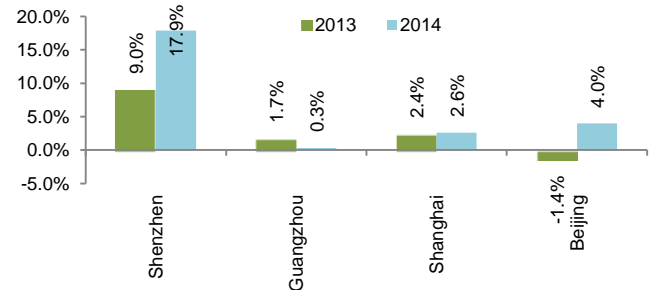

Source(s): Company, ABCI Securities

**Exhibit 17: Key metrics of Neo Urban Commercials**


Source(s): Company, ABCI Securities

**Exhibit 18: Tenancy expiry profile**


Source(s): Company, ABCI Securities estimates

**Exhibit 19: Grade A Office rental rate in tier-one cities (YoY change)**


Source(s): JLL, ABCI Securities

- Zoll Centers:** The Zoll Centers are a series of community-based lifestyle shopping centers. As of Dec 2014, LVGEM owned and operated two Zoll Centers, namely the Chanson Zoll Center and the 1866 Zoll Center, which commenced operation in May 2013 and May 2014. Two more Zoll Centers are currently under construction and scheduled for completion in 2016 and 2017.

According to JLL, rental rates of shopping centers in Shenzhen have been increasing steadily at 0.5-1.2% QoQ for the past five quarters. We believe the upcoming new Zoll Centers could attain a high rental rate. For the existing Zoll Centers in operation, tenancy for 75% of the GFA will expire 5 years later, thus upward rent adjustments are highly unlikely in the near term. Nonetheless, 22% of rental income is calculated based on turnover or the combined method in 4M15, meaning that LVGEM should be able to obtain a higher rent when retail sales are strong.

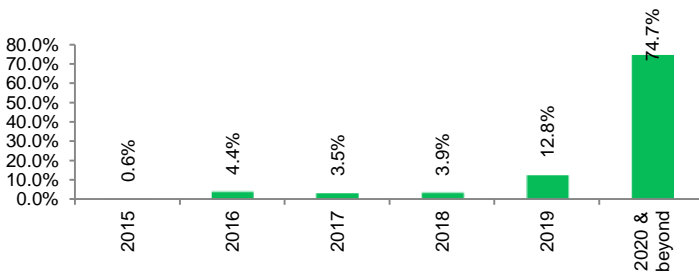
**Exhibit 20: Chanson Zoll Center**


Source(s): Company, ABCI Securities

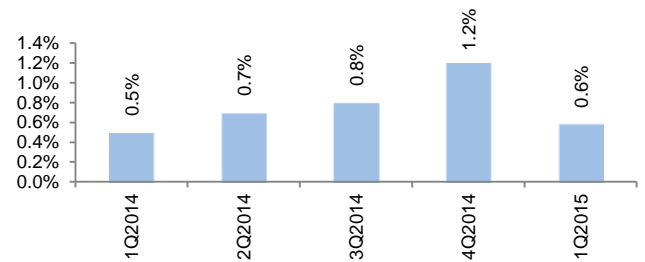
**Exhibit 21: Zoll Centers' LFA by sector (Apr 2015)**

(Usage by GFA in %)	Chanson Zoll Centers	1866Zoll Centers
Retail	25.4%	11.4%
Supermarket	24.6%	35.2%
F&B	23.9%	10.6%
Living ancillary services	11.1%	12.0%
Children services	8.8%	21.4%
Leisure and entertainment	5.5%	7.4%
Others	0.7%	2.0%
	<b>100.0%</b>	<b>100.0%</b>

Source(s): Company, ABCI Securities

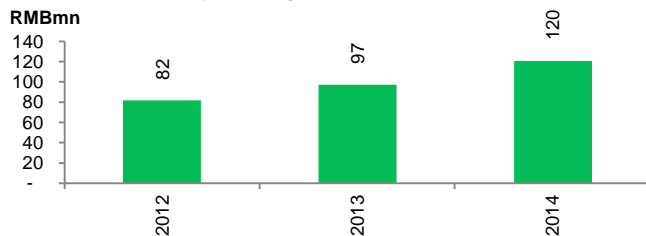
**Exhibit 22: Tenancy expiry profile**


Source(s): Company, ABCI Securities estimates

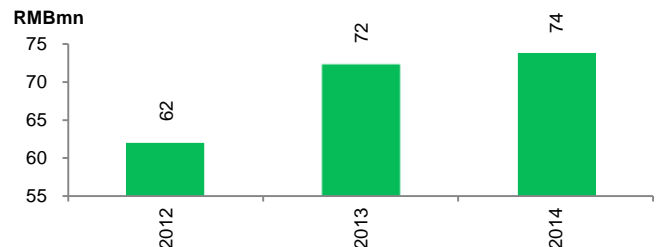
**Exhibit 23: Shenzhen shopping mall rent (QoQ %)**


Source(s): JLL, ABCI Securities

**Comprehensive services:** This segment mainly consists of property management services and hotel operations. As of Apr 2015, 19 properties with an aggregated GFA of 1.99mn sqm are managed by LVGEM. Sixteen of the 19 properties under management are also developed by the Group. Revenue from property management increased steadily from RMB 81.7mn in 2012 to RMB120.4mn in 2014 upon completion of new projects. In 2011, the LVGEM hotel, which has 330 rooms and is located in the CBD of the Futian District, commenced operation. The hotel generated a steady revenue stream of RMB 62mn-74mn annually in the last three years.

**Exhibit 24: Property management revenue**


Source(s): Company, ABCI Securities

**Exhibit 25: Hotels revenue**


Source(s): Company, ABCI Securities

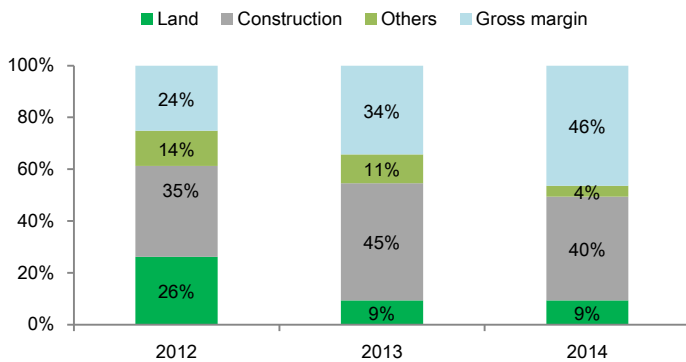
### 3. Cheap source of land from urban redevelopment

Ten out of the LVGEM's 16 completed projects, including Hongwan Garden and Mangrove Luxury, are acquired through urban redevelopment scheme. As new land supply of Shenzhen continues to shrink, the LVGEM's ability to secure new land from urban redevelopment becomes increasingly important.

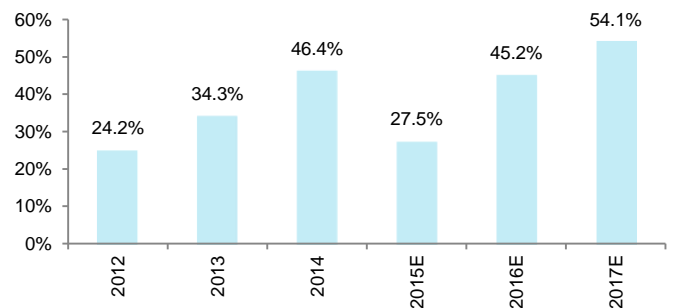


The land costs of urban redevelopment projects tend to be low although the acquisition/development process could be lengthy. According to urban redevelopment policy in Shenzhen, for a GFA at below 2.5x plot ratio, no land premium is applied; for a GFA at 2.5x-4.5x plot ratio, 20% of benchmark land premium will be paid; for a GFA with a plot ratio exceeding 4.5x, a 100% land premium will be paid. For a usual project with a 10x plot ratio, a land premium at only 65% of market rate is applied. In 2013 and 2014, land cost represents 9% of Target group's ASP only, much lower than the 15%-25% for the sector.

As a result of the low land cost, we estimate LVGEM's gross margins for Hongwan Garden and Mangrove Luxury would be high at 48.7% and 65.3%, which should elevate its overall gross margin from 27.5% in 2015E (due to the booking of non-Shenzhen projects) to 54.1% in 2017E.

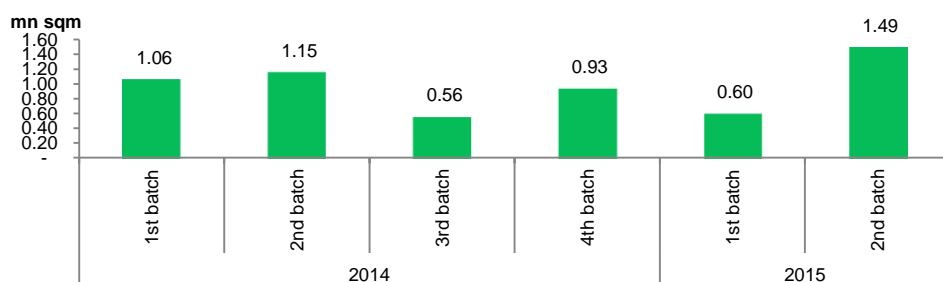
**Exhibit 26: Cost of sales breakdown**


Source(s): Company, ABCI Securities

**Exhibit 27: Gross margin for property development**


Source(s): Company, ABCI Securities estimates

With a solid track record in Shenzhen's urban redevelopment, we believe LVGEM could secure more new redevelopment projects in the future. Shenzhen approved a total of 3.7mn sqm of site area in 2014 and 2.09mn sqm in 1H2015 for urban redevelopment under the city's renewal plan. We expect LVGEM will secure additional redevelopment projects in the next 12 months.

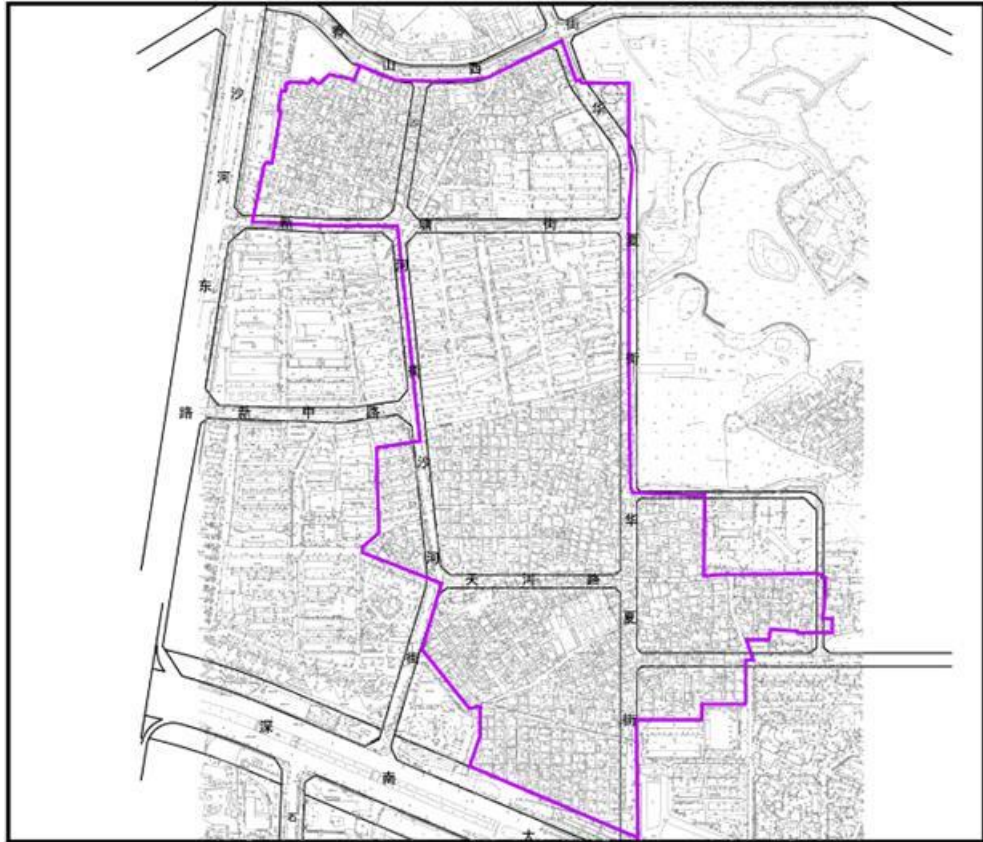
**Exhibit 28: Total area approved by the Shenzhen City Renewal Plan (深圳市城市更新单元计划)**


Source(s): Urban Planning, Land and Resources Commission of Shenzhen, ABCI Securities



Exhibit 29: Shenzhen's largest urban redevelopment site approved in 2014

南山区沙河街道沙河五村城市更新单元调整后拟拆除重建范围示意图



拟拆除重建范围面积：459542m<sup>2</sup>

Source(s): Urban Planning, Land and Resources Commission of Shenzhen.



## Before the injection

In Jan 2014, New Heritage (former name of LVGEM China) announced the sale of 858.8mn shares (64.83% stake) at HK\$ 944.7mn or HK\$1.1/share by controlling shareholders to China LVGEM (wholly-owned by Mr. Wong). A cash offer was also announced to comply with the listing rules. In June 2014, Mr. Wong became a controlling shareholder of New Heritage. with a 70.03% stake. After the share acquisition, New Heritage changed its name to LVGEM China.

The development of LVGEM has not slowed after the change in major shareholder. With solid experience in Shenzhen's property market, LVGEM conducted two major acquisitions to strengthen its position in Shenzhen before the asset injection had completed. According to the announcements filed by LVGEM on HKEX, the following acquisitions were made:

- **Acquisition of a project in Shenzhen:** In Apr 2015, LVGEM acquired a 75% stake in a project in Baoan district, Shenzhen. The acquisition amount was RMB 145mn, or RMB 3,779/sqm based on a GFA of 38,365sqm. The project contributed to RMB 2.6mn in rental revenue in 1H15.
- **Expansion to Hong Kong:** On July 30, 2015, LVGEM announced to acquire an agricultural site in Lau Fau Shan for HK\$ 710mn. Only 10% of the consideration is paid as deposit. The transaction will be completed when: 1) the farm land is approved for residential use; 2) the project has no less than 23,880sqm in GFA, which translates to HK\$ 29,731/sqm or HK\$ 2,763/sqft; 3). The minimum building height should be no less than 3 stories and 12.5 meters above the mean formation level. Upon successful change of land use, we believe this project could attract significant buyers' demand from Shenzhen due to its proximity to Futian CBD area and its view of Hong Kong's Wetland Park. In fact, land price of the nearby area Tuen Mun has been rising over the last 3 months as land transaction price surged from HK\$ 3,720/sqft (mass residential sites) in June 2015 to HK\$ 15,095/sqft (luxury low-rise projects) in Sep 2015.

**Exhibit 30: Land transaction in northwest New Territories**

Date	Site	Buyer	GFA	Consideration	AV
			000 sqft	HK\$mn	HK\$/sqft
Sep-15	Tuen Mun- Castle Peak Road	Poly	115	1,730	15,095
Aug-15	Yuen Long- Ngau Tam Mei	L'Avenue	45	548	12,119
Jul-15	Tuen Mun- So Kwun Wat	Vanke	842	3,822	4,541
Jun-15	Tuen Mun- Kwun Chui Road	Henderson	785	3,629	4,621
Jun-15	Tuen Mun- Hoi Wing Road	SHKP	355	1,319	3,720

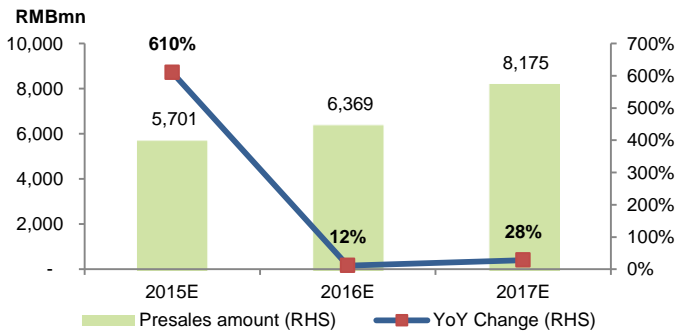
Source(s): Land Department, ABCI Securities

## Financial analysis

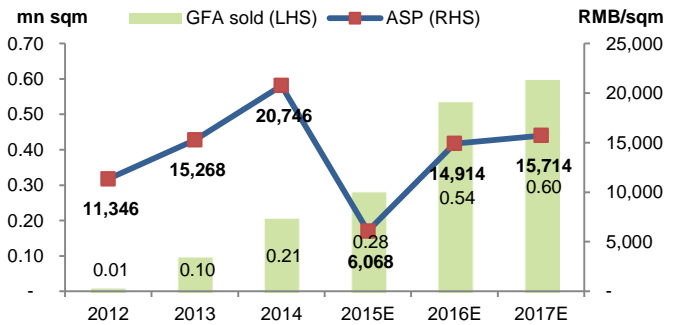
### Strong core profit growth at 26% CAGR in 2014-17E

We expect the LVGEM's presales to expand by 20% CAGR from RMB 5.7bn in 2015E to RMB 8.2bn in 2017E on the back of an active property market in Shenzhen. The two key projects, Hongwan Garden and Mangrove Luxury Garden, will be the key earnings contributors over the next few years. However, as Hongwan Garden and Mangrove Luxury Garden would be completed in 2016 and 2017, we estimate core profit would slow in 2015E to RMB 287mn, down 76% YoY. However, earnings growth will resurge to RMB2.4bn in 2017E, implying a 26% CAGR in 2014-17E

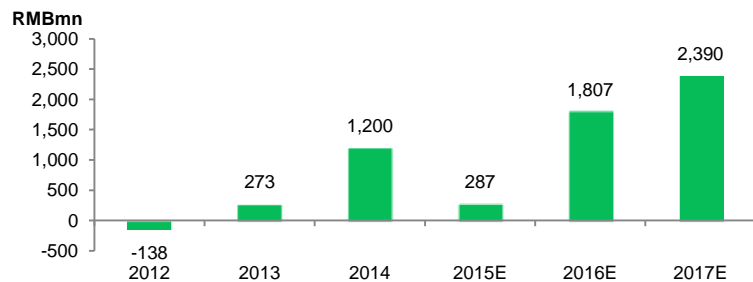
Margin-wise, gross margin will stay higher than 40% in 2016E-17E due to the low land cost of urban redevelopment projects. For 2015E, however, margins will be lower as we expect non- Shenzhen projects will account for a larger part in profit booking. We expect margins to improve steadily in 2016E-17E (2015E: 36.4%; 2016E: 43.2%; 2017E: 51.7%) as the LVGEM Group should attain a higher pricing power on the supply shortage in Shenzhen.

**Exhibit 31: LVGEM's presales**


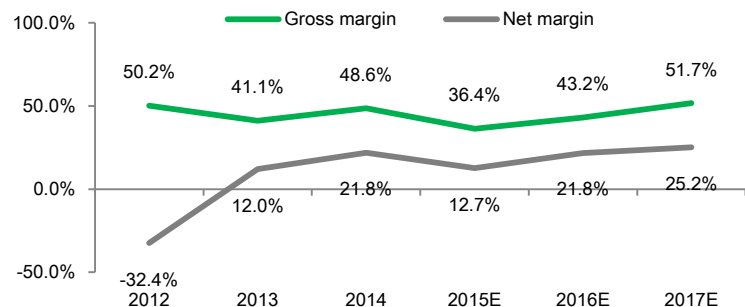
Source(s): Company, ABCI Securities estimates

**Exhibit 32 : LVGEM's booked sales**


Source(s): Company, ABCI Securities estimates

**Exhibit 33: LVGEM's core net profit in 2012-17E (RMB mn)**


Source(s): Company, ABCI Securities estimates

**Exhibit 34: LVGEM's gross and net margins in 2010-16E**


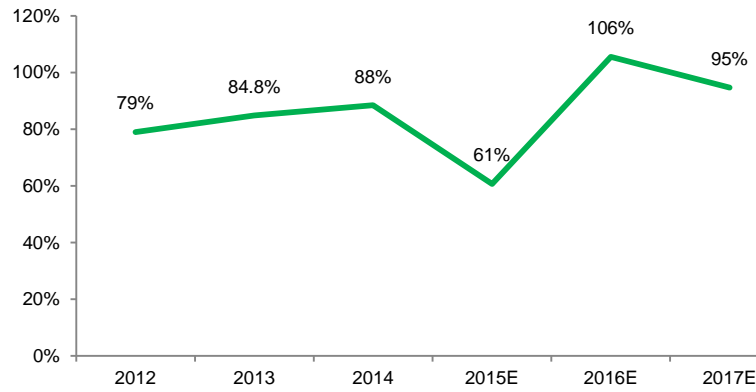
Source(s): Company, ABCI Securities estimates



### Gearing may rise in 2016E-17E

We expect LVGEM's net gearing to fall from 88% in 2014 to 61% in 2015E due to strong cash inflow from presales of Hongwan Garden and Magrove Luxury Garden. However, we expect gearing to rise as on increasing investment in redevelopment projects.

Exhibit 35: LVGEM's net gearing in 2012-17E



Source(s): Company, ABCI Securities estimates



Initiate BUY with TP of HK\$2.90 based on a 50% discount to NAV

Exhibit 36: LVGEM's end- FY16E NAV estimates

	Attr. GFA	Net assets value		Valuation	Implied value per
	(M sqm)	(RMB m)	% of total	Method	sqm (RMB)
Shenzhen	1.5	17,419	46%		11,570
Maoming	2.5	2,040	5%	DCF at WACC of 10.4%	821
Others	0.2	121	0%		598
HK	0.0	436	1%	Book value	24,370
Property development	4.2	20,017	53%	DCF at WACC of 10.4%	4,774
Property investment & management	0.25	16,684	44%	3% cap rate of 2016E rental income	67,617
Comprehensive services		1,042	3%		10x 2016E PE
<b>Total 2016E GAV</b>		<b>37,744</b>	<b>100%</b>		
Convertible preference share		(5,860)	-16%		
2016E Net cash/ (debt)		(8,906)	-24%		
<b>Total 2016E NAV</b>		<b>22,978</b>	<b>61%</b>		
No. of share outstanding (diluted)		4,694			
<b>NAV per share (RMB)</b>		<b>4.90</b>			
Ex rate		1.18			
<b>NAV per share (HKD)</b>		<b>5.78</b>			
Target discount (%)		50%			
<b>Target Price (HKD)</b>		<b>2.90</b>			

<b>WACC</b>	<b>10.4%</b>
Cost of debt	8.5%
Cost of equity	15.0%
<b>Debt/ (Debt + Equity)</b>	<b>54%</b>

Source(s): Company, ABCI Securities estimates

We assess the valuation of LVGEM based on the discount-to-NAV method, one of the most common valuation metrics used by developers in China:

- **Property development:** We conduct a DCF analysis and apply a WACC of 10.4% to gauge the value of individual projects; total value of property development projects arrives at RMB 20bn. We assume LVGEM to successfully acquire 0.5mn sqm of new landbank in Shenzhen via redevelopment in 2016E. For the 75% stake in the Lau Fou Shan site in Hong Kong, we only include its acquisition cost (or book value) at HK\$710mn (RMB582mn) in our valuation as the approval process of usage conversion (from agriculture to residential) could be lengthy.
- **Investment properties:** We apply a cap rate of 3% on 2016E rental income to arrive at our valuation estimate of RMB 17.0bn. This translates into RMB 67,617/sqm based on the total leasable floor area of 0.25mn sqm by end- 2016E.
- **Comprehensive services:** We apply 10x 2016E P/E on LVGEM's property management and hotel business.

Overall, Shenzhen property assets (property development and investment properties) represent 90% of our gross asset value forecast. We subtract the GAV of RMB 37.7bn by our 2016E net debt estimate (RMB 8.9bn) and convertible preference share amount (RMB 5.9bn) to derive our end-FY16E NAV of RMB 22,978mn, or HK\$5.78/share.

We apply a 50% discount (towards low end of sector range) to our NAV estimates and derive our TP of HK\$2.90. We believe LVGEM deserves to be traded at premium given its high Shenzhen exposure. Initiate **BUY**.



## Risk factors

- **Relocation process could be lengthy.** The long process of urban redevelopment can be attributed to the negotiations with residents on the resettlement compensations in the form of cash, replacement properties, or both. The whole process could take 3-5 years for an individual site. Hence, timing for land acquisition is usually uncertain and the Group could be short on saleable resources if the process takes longer than expected.
- **Complicated regulations governing the redevelopment process.** Presales of Kaisa's urban redevelopment projects have been halted by relevant authorities due to possible breach of rules and regulations. So far, the LVGEM has not been involved in any legal cases regarding to similar violations. In our view, the LVGEM's has positioned itself to be a niche developer instead of one prioritizing a fast asset turnover. Thus, it is less likely to breach relevant regulations to speed up the relocation process.
- **Correlation to A-share market.** There are concerns that recent correction in A-share market may impair sentiment in property market, especially in Shenzhen where penetration of stock brokerages is high. However, property price in Shenzhen has showed no signs of abating. In fact, capital may have been diverted from stock market to physical properties as many Chinese citizens consider real estate to be a more defensive investment.
- **Policy tightening if property market is overheated.** High-tier cities have always been more tightly regulated as compared to other cities in China. E.g., the home purchase restriction in tier-1 cities has not been officially removed. If Shenzhen's property price surge excessively to an unaffordable level, the government may intervene with more tightening measures.



**Consolidated income statement (2012A-2017E)**

<b>FY Ended Dec 31 (RMB mn)</b>	<b>2012A</b>	<b>2013A</b>	<b>2014A</b>	<b>2015E</b>	<b>2016E</b>	<b>2017E</b>
<b>Revenue</b>	<b>485</b>	<b>1,971</b>	<b>4,851</b>	<b>2,350</b>	<b>8,696</b>	<b>10,190</b>
Cost of sales	(242)	(1,161)	(2,493)	(1,494)	(4,944)	(4,921)
<b>Gross Profit</b>	<b>243</b>	<b>810</b>	<b>2,357</b>	<b>855</b>	<b>3,753</b>	<b>5,269</b>
SG&A expenses	(204)	(197)	(193)	(141)	(308)	(359)
<b>EBIT</b>	<b>39</b>	<b>613</b>	<b>2,165</b>	<b>714</b>	<b>3,445</b>	<b>4,910</b>
Finance cost	(231)	(206)	(217)	(307)	(375)	(443)
Share of profit of associates	(0)	0	(0)	-	-	-
Other income/ (expenses)	2	8	19	37	44	38
Fair value gain of investment properties	-	591	895	-	-	-
Disposal/one-off items	652	0	-	-	-	-
<b>Profit before tax</b>	<b>461</b>	<b>1,006</b>	<b>2,861</b>	<b>445</b>	<b>3,114</b>	<b>4,505</b>
Tax	(130)	(326)	(1,132)	(146)	(1,220)	(1,942)
<b>Profit after tax</b>	<b>331</b>	<b>680</b>	<b>1,729</b>	<b>299</b>	<b>1,894</b>	<b>2,563</b>
Minority interest	(1)	0	(0)	(12)	(87)	(173)
<b>Reported net profit</b>	<b>330</b>	<b>680</b>	<b>1,728</b>	<b>287</b>	<b>1,807</b>	<b>2,390</b>
<i>Less: exceptional items</i>	<i>(468)</i>	<i>(407)</i>	<i>(528)</i>	-	-	-
<b>Core net profit</b>	<b>(138)</b>	<b>273</b>	<b>1,200</b>	<b>287</b>	<b>1,807</b>	<b>2,390</b>
<b>Per share</b>						
Underlying EPS (RMB)	(0.03)	0.06	0.26	0.04	0.22	0.29
DPS (HK\$)	0.00	-	-	-	0.09	0.12
Payout ratio (%)	-7%	0%	0%	0%	41%	41%
BVPS (RMB)	0.97	1.11	1.48	0.89	1.03	1.20
<b>Growth %</b>						
Revenue		306.3%	146.2%	-51.6%	270.1%	17.2%
Gross Profit		232.9%	191.1%	-63.7%	338.8%	40.4%
EBIT		1475.1%	253.3%	-67.0%	382.4%	42.5%
Core net profit		-297.8%	339.6%	-76.1%	529.2%	32.3%
<b>Margin %</b>						
Gross margin	50.2%	41.1%	48.6%	36.4%	43.2%	51.7%
Gross margin (post-LAT)	172.3%	47.2%	43.9%	46.9%	39.2%	44.1%
EBIT margin	8.0%	31.1%	44.6%	30.4%	39.6%	48.2%
Core net margin	-32.4%	12.0%	21.8%	12.7%	21.8%	25.2%
<b>Key assumptions</b>						
Contracted Sales (RMB mn)				5,701	6,369	8,175
GFA sold (mn sqm)				0.42	0.52	0.60
ASP (RMB/sqm)				13,523	12,290	13,691
Booked Sales (RMB mn)				1,714	7,981	9,376
GFA delivered (mn sqm)				0.28	0.54	0.60
Booked ASP (RMB/sqm)				6,068	14,914	15,714

Source: Company, ABCI Securities estimates





Consolidated balance sheet (2012A-2017E)

As of Dec 31 (RMB mn)	2012A	2013A	2014A	2015E	2016E	2017E
<b>Current assets</b>	<b>6,392</b>	<b>7,438</b>	<b>7,879</b>	<b>14,118</b>	<b>15,593</b>	<b>17,909</b>
Cash	513	653	1,099	4,855	2,368	3,782
Restricted cash	43	388	742	742	742	742
Trade & other receivables	447	772	825	825	825	825
Property under development	5,267	5,310	4,932	7,416	11,377	12,279
Other current assets	122	315	280	280	280	280
<b>Non-current assets</b>	<b>9,684</b>	<b>11,133</b>	<b>12,630</b>	<b>12,701</b>	<b>12,773</b>	<b>12,844</b>
Property, plant & equipment	428	419	392	363	335	307
Investment properties	8,588	9,771	11,143	11,143	11,143	11,143
Investment in Associate and JCE	465	505	522	622	722	822
Other non-current assets	203	438	573	573	573	573
<b>Total Assets</b>	<b>16,076</b>	<b>18,571</b>	<b>20,509</b>	<b>26,819</b>	<b>28,365</b>	<b>30,753</b>
<b>Current Liabilities</b>	<b>7,530</b>	<b>6,975</b>	<b>5,065</b>	<b>11,077</b>	<b>11,465</b>	<b>12,264</b>
Short term borrowings	1,875	1,029	1,762	3,762	5,762	7,762
Trade & other payables	1,867	1,545	1,861	1,861	1,861	1,861
Pre-sales deposits	3,531	4,177	679	4,691	3,079	1,878
Other current assets	257	225	762	762	762	762
<b>Non-current liabilities</b>	<b>3,989</b>	<b>6,345</b>	<b>8,464</b>	<b>8,464</b>	<b>8,464</b>	<b>8,464</b>
Long term borrowings	2,282	4,464	6,254	6,254	6,254	6,254
Other payables	-	-	-	-	-	-
Other non-current assets	1,707	1,881	2,210	2,210	2,210	2,210
<b>Total Liabilities</b>	<b>11,519</b>	<b>13,320</b>	<b>13,529</b>	<b>19,540</b>	<b>19,929</b>	<b>20,728</b>
<b>Net Assets</b>	<b>4,558</b>	<b>5,251</b>	<b>6,980</b>	<b>7,279</b>	<b>8,437</b>	<b>10,026</b>
<b>Shareholders Equity</b>	<b>4,542</b>	<b>5,226</b>	<b>6,954</b>	<b>1,381</b>	<b>2,452</b>	<b>3,868</b>
Convertible preference share	-	-	-	5,860	5,860	5,860
Minority Interest	16	26	26	38	125	298
<b>Total Equity</b>	<b>4,558</b>	<b>5,251</b>	<b>6,980</b>	<b>7,279</b>	<b>8,437</b>	<b>10,026</b>
<b>Key ratio</b>						
Gross debt (RMB mn)	4,157	5,493	8,016	10,016	12,016	14,016
Net debt (RMB mn)	3,601	4,452	6,175	4,419	8,906	9,492
Net gearing (%)	79%	85%	88%	61%	106%	95%
Contracted sales/ Total assets (x)	0%	0%	0%	21%	22%	27%

Source(s): Company, ABCI Securities estimates



Consolidated cash flow statement (2013A-2017E)

FY ended Dec 31 (RMB mn)	2012A	2013A	2014A	2015E	2016E	2017E
EBITDA	69	661	2,213	763	3,493	4,958
Change in Working Capital	890	(53)	(2,774)	1,988	(5,011)	(1,440)
Tax payment	(168)	(176)	(219)	(146)	(1,220)	(1,942)
<b>Operating Cashflow</b>	<b>792</b>	<b>432</b>	<b>(780)</b>	<b>2,605</b>	<b>(2,738)</b>	<b>1,577</b>
Purchase of PP&E	(137)	(40)	(20)	(20)	(20)	(20)
Addition of Investment Properties	(489)	(767)	(510)	-	-	-
Others	(40)	(456)	(161)	(63)	(56)	(62)
<b>Investing Cashflow</b>	<b>(666)</b>	<b>(1,263)</b>	<b>(691)</b>	<b>(83)</b>	<b>(76)</b>	<b>(82)</b>
Debt raised	1,571	3,251	4,390	10,000	10,000	10,000
Debt repaid	(1,004)	(1,915)	(1,867)	(8,000)	(8,000)	(8,000)
Interest expenses	(388)	(375)	(606)	(766)	(936)	(1,106)
Equity raised	-	-	-	-	-	-
Dividend to shareholders	-	-	-	-	(737)	(974)
Others	-	10	0	-	-	-
<b>Financing Cashflow</b>	<b>178</b>	<b>971</b>	<b>1,917</b>	<b>1,234</b>	<b>327</b>	<b>(81)</b>
<b>Net cash inflow/ (outflow)</b>	<b>305</b>	<b>140</b>	<b>447</b>	<b>3,756</b>	<b>(2,487)</b>	<b>1,414</b>
Cash- beginning	208	513	653	1,099	4,855	2,368
<b>Cash- year-end</b>	<b>513</b>	<b>653</b>	<b>1,099</b>	<b>4,855</b>	<b>2,368</b>	<b>3,782</b>

Source(s): Company, ABCI Securities estimates



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### Definition of equity rating

Rating	Definition
Buy	Stock return $\geq$ Market return rate
Hold	Market return – 6% $\leq$ Stock return < Market return rate
Sell	Stock return < Market return – 6%

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate from 2009-2013

Time horizon of share price target: 12-month

### Definition of share price risk

Rating	Definition
Very high	$2.6 \leq 180$ day volatility/180 day benchmark index volatility
High	$1.5 \leq 180$ day volatility/180 day benchmark index volatility < 2.6
Medium	$1.0 \leq 180$ day volatility/180 day benchmark index volatility < 1.5
Low	180 day volatility/180 day benchmark index volatility < 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index.

Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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