

China Resources Land

Earnings and NAV upgrade

- China Resources Land (CRL) has so far launched three FY06 completions during the past four months as scheduled which progressed well. As for the upcoming two launches, which are mid-end housing projects in Wuhan and Hefei, we believe CRL is keen to go for volume instead of margin in such second-tier cities.
- Projects outside Beijing will be the bread-and-butter for CRL in the two years ahead due to the sizable production volume. Moreover, they are likely to have higher margins, thanks to the early entry to the cities, thus providing a strong base for a 65% CAGR in net profit between FY05 and FY07.
- On the Beijing front, mid-end housing demand is most resilient and favors mass residential project developers. CRL offers one of the highest exposures to Beijing among China property developers.
- On the back of the 96% share price growth in the past three months, the price performance of the stock may be capped in the short term. Nevertheless, we believe CRL's strong presence in Beijing, earnings quality, and multi-city exposure are solid earnings drivers. We maintain our Overweight rating, and raise our 12-month target price to HK\$2.70, based on 12x P/E and a 26% discount to our NAV estimate of HK\$3.66 per share.

Overweight

HK\$2.25

12 October 2005
Price Target: HK\$2.70

Hong Kong Property

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Figure 1: Historical share price



Source: Datastream

Table 1: Reuters: 1109.HK, Bloomberg: 1109 HK

HK\$ in millions, year-end Dec

	FY04	FY05E	FY06E	FY07E		
Sales	2,409	2,800	3,250	5,175	52-week range	HK\$1.12-\$2.375
Net profit	150	280	339	594	Market cap (HK\$MM)	3396.9
EPS (HK\$)	0.100	0.186	0.225	0.393	Market cap (US\$MM)	435.5
DPS (HK\$)	0.030	0.042	0.067	0.079	Shares outstanding (MM)	1,509.7
Sales growth (%)	10.8	16.3	16.0	59.3	Free float	44.40%
Net profit growth (%)	90.3	85.8	21.0	75.3	Avg daily value (HK\$MM)	13.2
EPS growth (%)	90.3	85.8	21.0	75.3	Avg daily value (US\$MM)	1.70
ROE (%)	3.7	6.8	7.6	11.7	Avg daily volume	MM shares
P/E (x)	22.5	12.1	10.0	5.7	Index	HSI 14898.77
EV/EBITDA (x)	20.4	10.5	7.7	4.5	Exchange rate	HK\$7.8/US\$1
Div yield (%)	1.3	1.9	3.0	3.5	Performance	1 mth 3 mths 12 mths
NAV per share (HK\$)	2.01	3.66			Absolute (%)	25.7 93.1 96.3
Book value/share (HK\$)	2.48	2.72	2.96	3.30	Relative (%)	27.4 87.9 84.3

Source: Datastream, Company, JPMorgan estimates

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Company Update

Three launches under good progress

China Resources Land (CRL) has so far launched three FY06 completions during the past four months as scheduled which progressed well. These include:

Fortune Island (110,475sq m in GFA, total 620 units, completion in 2H06):

According to the Beijing Real Estate Trading Center (BJFDC), CRL obtained presale approvals for two batches of Fortune Island units in May and September respectively, which involved 78,800 sqm of salable residential floor area. Since late May 48,050sq m, or 43% of the total floor area has been sold. The project is a low-rise development located within the South 4-5th Ring Road targeting the middle class households. The pricing of Rmb7,600 psm is affordable to the typical Beijing families. We therefore expect the project to be over 95% sold when the project is completed next year, and fetch a development profit of Rmb167million at a margin of 24%.

The Bund Side Ph1 (29,327sqm in GFA, total 220 units; completion in 2006): The Shanghai project was launched on 21 September on the back of the sluggish buying sentiment in Shanghai. Over 80 units have been sold within three weeks of launch. The average selling price of Rmb18,000psm was higher than management's initial target of Rmb17,000psm. We expect CRL to fetch Rmb150 million at a margin of 29% if all units are sold.

Chengdu Jade City Ph2 (55,948sqm in GFA, completion in 2006): The second phase of the project is half the size of Ph1 which were sold in 2003 at an average of Rmb3,300psm. The Ph2 was launched on 28 Aug with 220 units sold on the same day. Given the average commodity residential prices of Chengdu has reached Rmb3,680psm during 7M05 and that the project is better recognized due to location and branding, we have factored in an average selling price of Rmb4,100psm which is slightly lower than the average of the batch of units sold in August as the primary market in Chengdu showed some signs of slowdown around the National Holiday. Nevertheless, we estimate Ph2 could have a development margin of 31% as compared to 15% for Ph1.

Two more new launches to go before end this year

The upcoming two launches are mid-end housing projects at the second tier cities where unfurnished units would be delivered. CRL is applying for the presale permit of Hefei project and could be launched in November. Nevertheless, soft marketing has started since May and CRL is testing water on the sales price, tentatively within Rmb3,500-4,000psm. On the other hand, we expect the Wuhan project could be launched in late October when the Autumn housing fair in the city would be hosted. Development margin would be at mid-20% levels per our estimates and contribute only to 17% of the total development profits. However, we believe CRL is keen to go for volume in such second-tier cities instead of going for margin. Any margin expansion opportunities would rather lie in the cost savings through management control and economies of scale as their annual completions is growing from 0.3m sqm levels to 0.6m sq m in FY07.

Table 2: Sales launch in 2H05

	JPMorgan Est. price Rmb/sq m	Launch date and response
Fortune Island Ph1 - low rises (Beijing)	5,000-6,000	Sep-Oct 05
The Bund Side Ph1 (Shanghai)	18,000	Sep 05 (80 units sold)
Chengdu Jade City Ph2	4,100	28 Aug (sold 20%)
Hefei French Annecy Ph 1	3,900	4Q05 (to get presale permit)
Wuhan Phoenix City Ph1	4,900	Late Oct 05

Source: Company, JPMorgan estimates

Growth drivers

Capitalizing on the resilient Beijing property market

The Beijing commodity residential market remains on a steady uptrend this year due to: (1) lower supply of residential and commercial land sites, and the ban of land supply from those within the 2nd Ring Road; and (2) a drop in residential floor spaces approved for presale during 8M05. Despite the rollout of austerity measures, primary presale housing prices during April to August have stayed in the range of Rmb 6,800-7,140psm. Buying demand for flats at Rmb 5,000-7,000psm within the 4th-5th Ring Road are most resilient. This is particularly favorable to mass residential project developers that position their projects at such levels. And CRL offers one of the highest exposures to Beijing among China property developers.

Non-Beijing projects support 65% CAGR in net profit during FY05 to FY07

Although Beijing would remain as the major earnings contributor for CRL in the coming three years, contribution from projects in Chengdu and Shanghai is getting more significant. In particular, Chengdu Jade City has a salable residential floor area of 841,500 sq m and would provide sizable turnover up to 2009. The Shanghai and Chengdu projects would account for over 30% of the contracted sales during FY05-07 and 38% of the development profits. Moreover, they are likely to have higher margins than Beijing projects, thus providing a strong base for a 65% CAGR in net profit between FY05 and FY07.

Investor concerns

Land costs are getting higher

CRL's successful turnaround is partly attributable to the low-cost land bank acquired during 2002-03 outside Beijing. But land costs are surging recently especially those acquired through public auctions. The recent bid of CRL and its parent, China Resources Holdings, for the Qinghe site at Rmb2.66 billion (A.V Rmb3,523 psm) is much higher than land sites acquired earlier by other developers. Beijing Capital Land's average land costs nearby are below Rmb2,000psm, while Hopson's land costs in Beijing are Rmb1,000-1,500 psm. This favors CRL and other developers who already have a strong presence in the Capital but would have to face higher risk in replenishing their land banks.

Intensifying competition in Beijing

CRL's aggressive bidding (it outbid 50 developers to get the site) also illustrated the intensifying competition for land sites due to: (1) reduced supply of residential sites and (2) entry of non-Beijing based developers such as Guangzhou R&F and Hopson. Beijing-based developers would have to choose between maintaining their presence in Beijing by paying high land costs or foregoing the Beijing base and extending

their businesses to other second-tier cities where capital requirements are significantly lower.

Maintain Overweight; price target raised to HK\$2.70

Earnings and NAV upgrade

We raise our NAV and earnings forecasts because of (1) higher sales price of the launches achieved and (2) lower development costs than we earlier estimated. In particular, the construction costs in the second-tier cities could be much lowered and provide reasonable margins without asking for aggressive prices.

Table 3: CRL-changes in earnings forecast and NAV estimates

	FY05E	FY06E	FY07E
Net profit (HK\$MM)			
Old	200.3	259.5	536.4
New	280.1	339.2	593.7
% change	40%	31%	11%
Core net profit (HK\$MM)			
Old	200.3	259.5	536.4
New	220.9	335.2	593.7
% change	10%	29%	11%
EPS (HK\$)			
Old	0.133	0.173	0.357
New	0.186	0.225	0.394
% change	40%	30%	10%
Core EPS (HK\$)			
Old	0.133	0.173	0.357
New	0.146	0.222	0.393
% change	10%	28%	10%
NAV (HK\$)			
Old	3.12		
New	3.66		
% change	17%		

Source: JPMorgan.

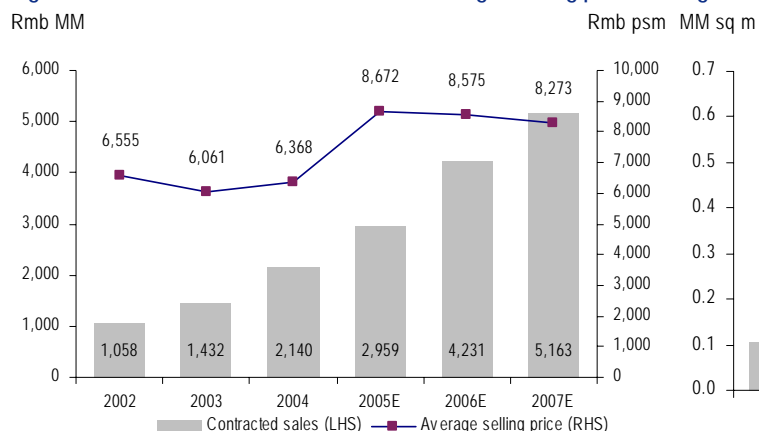
Valuation

China Resources Land is currently trading at 10.6x forward P/E compared with the long-term average of 12.5x and at a 35% discount to the NAV against the long-term average of 45%. The stock traded at an average of 16.5x and within the 20-30% NAV band during 2000-2002 when the Beijing property market trended up.

CRL's share price reached a year high of HK\$2.375 and was 96% above the trough in July 05. Price performance could be capped in the near term given the surge within the past three months. Nevertheless, we have a positive outlook on Beijing residential market. Half of CRL's land bank located in the city and is thus one of the major beneficiaries. Moreover, its regional exposure allows flexibility to go for-volume or for-margin. Added to this is their ability to lock-in profits for FY06 and even FY07, thus enhanced earnings visibility.

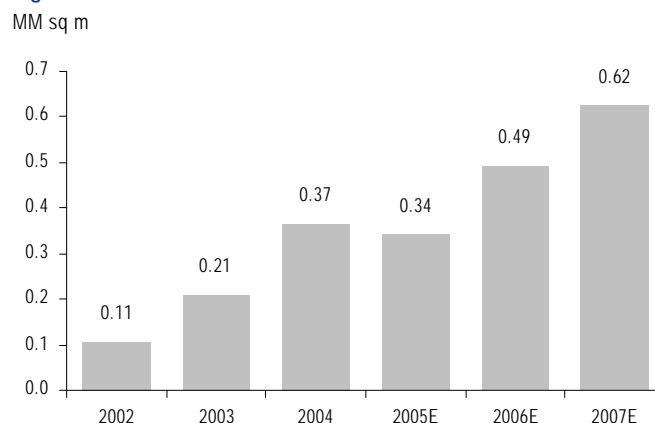
Considering the historical valuation trends and comparison against other China property peers, we have raised our target price to HK\$2.7, based on 12x FY06E P/E and represents a 26% discount to NAV, thus providing a 20% upside potential on a 12m horizon. We maintain our Overweight rating and suggest buying on weakness of the counter. Major risks to our price target include (1) macro risks of the China property market including policy measures implemented by the government and (2) the execution risks either if projects are wrongly positioned or the property prices consolidate.

Figure 2: CRL—Contracted sales forecast & averages selling price



Source: Company, JPMorgan estimates.

Figure 3: CRL—Contracted sales area



Source: Company, JPMorgan estimates.

Table 4: CRL—Profit and loss summary

HK\$ in millions, year-end December

	FY02	FY03	FY04	FY05E	FY06E	FY07E
Turnover						
Total property sales	1,057.6	1,184.0	2,313.2	2,658.9	3,104.8	5,025.8
Total rental income	13.3	8.0	21.9	66.3	68.3	70.3
Others	59.3	60.3	73.7	75.2	76.7	79.2
Total Turnover	1,130.2	1,252.3	2,408.8	2,800.3	3,249.7	5,175.3
Total property sales	42.0	62.1	271.4	546.4	706.1	1,108.1
Total rental income	5.9	-10.7	3.6	1.1	14.5	14.9
Others	-6.9	-2.7	-21.7	-36.0	-36.0	-41.0
EBIT	40.9	48.8	253.3	511.5	684.6	1,082.0
Net interest income	-1.4	-32.0	-27.7	-109.3	-111.4	-105.8
Operating Profit	39.5	16.8	225.7	402.3	573.2	976.2
Associate income	20.9	7.4	20.0	4.8	5.1	5.3
Exceptional items						
One off gains (asset disposal, etc.)	63	0	0	0	0	0
Provisions / Write-back (non cash items)	-64.6	12.2	-57.8	59.1	4.0	0.0
Profit before Tax	58.7	36.4	187.8	466.2	582.3	982.5
Taxation	74.1	-17.3	-81.0	-139.9	-163.0	-274.8
Minority interests	35.9	59.8	43.3	-46.3	-80.0	-113.0
Net Profit	168.6	78.9	150.1	280.1	339.2	594.7
Core profit	170.3	66.7	146.4	220.9	335.2	593.7
EPS (\$/share)	0.112	0.053	0.100	0.186	0.225	0.394
Core EPS (\$/ share)	0.113	0.044	0.097	0.147	0.223	0.395
DPS (\$/share)	0.027	0.027	0.030	0.042	0.067	0.079

Source: Company reports, JPMorgan estimates.

Table 5: CRL-development projects in pipeline

	Est. Total cost		Est. Sales Prices Rmb /sq m	EBIT Margin %	Est. profit recognized (Rmb MM)			
	Total GFA	Rmb /sq m			FY05E	FY06E	FY07E	FY08E
Unsold stocks								
Jing Tong Sunny Up Town	4,998	4,659	5,000	7%	1.7	0.0	0.0	0.0
Top Box Majestic Garden Ph2	3,934	10,339	11,000	6%	6.4	0.0	0.0	0.0
U-Space Ph1 (Youth Court)	16,319	8,065	9,000	10%	5.2	0.0	0.0	0.0
La Firenze Ph1a (former: Jade City)	11,150	5,408	6,800	20%	16.2	0.0	0.0	0.0
FY05								
Phoenix City Ph2	129,616	9,840	11,600	15%	192.3	36.5	0.0	0.0
Grand Constellation (former: Resources Center)	40,589	14,572	17,000	14%	54.5	24.6	19.7	0.0
La Firenze Ph1b (former: Jade City)	8,750	5,367	6,850	22%	8.3	4.7	0.0	0.0
La Firenze Ph2b (former: Jade City)	83,132	4,792	5,500	13%	58.8	0.0	0.0	0.0
Cheungdu Jade City Ph1	125,659	2,806	3,300	15%	62.3	0.0	0.0	0.0
FY06								
U-Space Ph2 (Youth Court)	33,755	8,573	11,000	22%	0.0	65.5	16.4	0.0
Fortune Island (La Firenze Ph5)	110,475	4,804	6,300	24%	0.0	166.6	0.0	0.0
Phoenix City Ph3	54,139	9,821	13,000	24%	0.0	138.0	34.4	0.0
Cheungdu Jade City Ph2	55,948	2,743	4,000	31%	0.0	67.0	3.5	0.0
Wuhan Phoenix City Ph1	69,450	3,699	4,900	25%	0.0	83.4	0.0	0.0
Hefei French Annecy Ph 1	40,000	2,976	3,900	24%	0.0	37.0	0.0	0.0
The BundSide Ph1 (Part 1)	29,327	12,743	18,000	29%	0.0	154.2	0.0	0.0
FY07								
Phoenix City Ph3a	75,972	10,193	13,000	22%	0.0	0.0	127.9	85.3
Phoenix City Ph3-commercial	62,600	10,865	16,000	32%	0.0	0.0	321.2	0.0
Fortune Island (Shopping)	5,469	4,804	8,000	40%	0.0	0.0	8.7	8.7
Qing He project Ph1	180,000	6,675	7,800	14%	0.0	0.0	87.7	118.7
Hefei French Annecy Ph 2	70,000	2,976	3,900	24%	0.0	0.0	45.3	19.4
Wuhan Phoenix City Ph2	69,450	3,872	5,200	26%	0.0	0.0	55.3	27.7
The BundSide Ph1 (Part 2)	56,671	13,033	18,000	28%	0.0	0.0	225.2	56.3
Cheungdu Jade City Ph2	102,637	2,806	4,000	30%	0.0	0.0	98.0	24.5
FY08								
Majestic Garden Ph3	66,009	10,646	12,000	11%	0.0	0.0	0.0	76.0
Phoenix City Ph3-commercial	106,400	10,967	15,000	27%	0.0	0.0	0.0	429.1
Cheungdu Jade City Ph4	210,769	2,806	4,000	30%	0.0	0.0	0.0	188.7
Cheungdu Jade City (Shopping)	75,324	2,806	4,000	30%	0.0	0.0	0.0	89.9
Qing He project Ph2	280,000	6,675	8,200	19%	0.0	0.0	0.0	320.1
The BundSide Ph2a	102,364	13,570	18,000	25%	0.0	0.0	0.0	453.4
Hefei Project Ph3	87,213	2,976	4,000	26%	0.0	0.0	0.0	53.6

Source: Company, JPMorgan estimates

Table 6: CRL-NAV breakdown

	Basis	Current NAV (HK\$ MM)	(HK\$/share)	% of GAV
Development Properties				
	DCF			
Residential		4,871	3.23	63.6%
Office		1,401	0.93	
Total development properties		6,272	4.15	81.9%
Rental Properties				
	Cap rate			
Residential		206	0.14	2.7%
Office		166	0.11	2.2%
Retail		680	0.45	8.9%
Total rental properties		1,053	0.70	13.7%
Listed Subsidiaries	Market value	331	0.22	4.3%
Gross Asset Value		7,656	5.07	100.0%
Attributable net debt		(2,131)	(1.41)	
Net Asset Value		5,524	3.66	

Source: Company, JPMorgan estimates

Companies Recommended in This Report (as of COB 12 October 2005)

China Resources Land (1109.HK/HK\$2.25/Overweight)

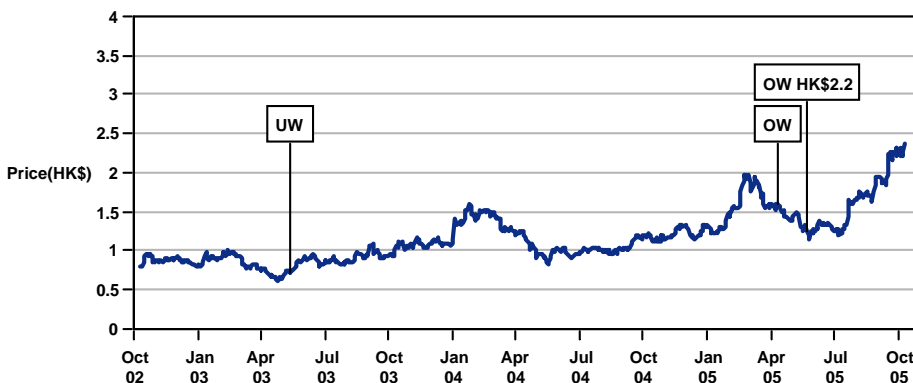
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China Resources Land (1109.HK) Price Chart



Date	Rating	Share Price (HK\$)	Price Target (HK\$)
13-May-03	UW	0.73	-
10-Apr-05	OW	1.59	-

Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends. Initiated coverage May 13, 2003. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts' discretion. JPMorgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

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IB clients*	46%	45%	39%
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IB clients*	65%	55%	45%

*Percentage of investment banking clients in each rating category.

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China Resources Land: Summary of financials

Profit and Loss statement						Cash flow statement					
HKD in millions, year-end Dec	FY03A	FY04A	FY05E	FY06E	FY07E	HKD in millions, year-end Dec	FY03A	FY04A	FY05E	FY06E	FY07E
Revenues	1,252	2,409	2,800	3,250	5,175	EBIT	49	253	512	685	1,082
% change Y/Y	10.8	92.4	16.3	16.0	59.3	Depreciation & amortisation	20	22	20	21	22
EBIT	49	253	512	685	1,082	Change in working capital	-630	-273	-370	-453	-415
% change Y/Y	19.2	419.6	101.9	33.8	58.0	Other items	-35	55	98	163	159
EBIT Margin (%)	3.9	10.5	18.3	21.1	20.9	Taxes	27	-36	-81	-112	-130
Net Interest	-32	-28	-109	-111	-106	Cash flow from operations	-632	-123	-18	48	471
Earnings before tax	36	188	466	582	983	Capex	-3	-2	-2	-2	-2
% change Y/Y	-38.0	416.2	148.2	24.9	68.7	Disposal/ (purchase)	3	0	-35	0	0
Tax	17	81	140	163	275	Net Interest	-98	-89	-153	-155	-147
as % of EBT	-35.6	-32.0	-27.3	-23.8	-25.4	Free cash flow	-648	-151	-77	24	448
Net Income (Reported)	79	150	280	339	595	Equity raised/ (repaid)	0	0	0	0	0
% change Y/Y	-53.2	90.3	86.6	21.1	75.3	Debt raised/ (repaid)	1,306	338	-50	0	-500
Core Net Profit	67	146	221	335	594	Other	0	0	0	0	0
% change Y/Y	-60.8	119.6	50.9	51.7	77.1	Dividends paid	-41	-41	-45	-64	-101
Shares Outstanding	1503	1503	1510	1510	1510	Beginning cash	772	1,389	1,536	1,527	1,653
EPS (reported)	0.053	0.100	0.186	0.225	0.394	Ending cash	1,389	1,536	1,527	1,653	1,658
% change Y/Y	-53.2	90.3	85.8	21.0	75.3	DPS	0.027	0.030	0.042	0.067	0.079
Core EPS	0.044	0.097	0.146	0.222	0.393						
% change Y/Y	-60.8	119.6	50.2	51.7	77.1						
Balance sheet						Ratio Analysis					
HKD in millions, year-end Dec	FY03A	FY04A	FY05E	FY06E	FY07E	% , year-end Dec	FY03A	FY04A	FY05E	FY06E	FY07E
Cash and cash equivalents	1,389	1,536	1,527	1,653	1,658	EBIT margin	3.9	10.5	18.3	21.1	20.9
Accounts receivable	959	906	876	826	776	Operating margin	1.3	9.4	14.4	17.6	18.9
Inventories	4,900	5,523	5,857	6,219	6,386	Net profit margin	6.3	6.2	10.0	10.4	11.5
Others	315	286	334	336	317	SG&A/sales					
Current assets	7,564	8,251	8,594	9,034	9,138	Sales per share growth	10.806	92.352	16.254	16.047	59.254
LT investments	1,271	1,257	1,268	1,189	1,171	Sales growth	10.806	92.352	16.254	16.047	59.254
Net fixed assets	451	440	401	404	406	Net profit growth	-53.2	90.3	86.6	21.1	75.3
Total assets	9,286	9,948	10,263	10,627	10,714	EPS growth	-53.2	90.3	85.8	21.0	75.3
Liabilities						Interest coverage (x)	1.3	2.8	3.7	6.1	10.0
ST loans	1,231	1,937	1,637	1,657	1,657	Net debt to total capital	27.4	29.6	27.9	25.0	18.8
Payables	800	2,115	2,090	2,069	2,051	Net debt to equity	50.8	59.4	53.0	45.7	30.9
Others	0	23	0	0	0	Sales/assets	14.4	25.0	27.7	31.1	48.5
Total current liabilities	2031	4075	3727	3726	3708	Assets/equity	233.4	266.9	250.5	237.5	214.9
Long term debt	2181	1813	2063	2043	1543	ROE	2.0	4.0	6.8	7.6	11.9
Other liabilities	152	4	5	0	0	ROCE	0.8	3.7	6.6	8.4	13.3
Total liabilities	4364	5892	5795	5769	5251						
Shareholders' equity	3979	3728	4098	4475	4986						
BVPS	2.649	2.482	2.717	2.964	3.303						

Source: Company reports and JPMorgan estimates.