

Hongkong & Shanghai Hotels (45.HK)

New Hotels Consolidate the Leadership Position

Hong Kong | Property | Company report

10 May 2017

Investment Summary

- Possess a leading luxury hotel brand in the hospitality sector
- Future hotel in London and Istanbul will be located at prime tourist attractions

Business Overview

Recorded a drop in net profit in FY2016 result: Hongkong & Shanghai Hotels has a slight drop in revenue of 1.92% in FY2016, mainly contributed by the renovation of The Peninsula Beijing, which part of the hotel was in closure, causing a drop in the revenue. Net profit dropped 33.63% and the drop is contributed by the both the decrease in revenue and the decrease in the revaluation of investment properties owned by the group. Throughout FY2016, the group continued its renovation of The Peninsula Beijing and completed the renovation of The Peninsula Chicago, which allows the group to achieve highest revenue per available room in Chicago.

Long-standing leader in the sector: The group has been one of the leader of the hotel operation sector for a long period of time. The Peninsula Hotel has hotels established in almost every major global gateway cities in the world, such as Hong Kong, New York, Tokyo and Shanghai. Each hotel is regarded as the best hotel in the city in terms of locations, services and facilities, and the target customers are the high income individuals locating at the top end of the spectrum, allowing the company to have a large pricing power without being affected significantly by the price competition caused by the emergence of the large number of online travel agents providing price comparing services, such as Expedia and Trivago. These websites significantly affect the pricing power of hotels because these websites reduce the information asymmetry faced by the consumers. Moreover, the strategic positioning at the most luxurious segment of the hospitality industry allows the company to target at the high income individual, who is less concerned with prices and more concerned with services offered, thus allowing the company to continue its price setting position and high occupancy rate despite the increasingly competitive industry in terms of prices.

All hotels are located at excellent locations: The Peninsula Hotels are located in almost every wealthy countries in the world and the location of the hotels are all carefully chosen so that they can offer the most convenient and the best locations to their customers, further justifying the leading and price setting positions of the hotels. All of the hotels, especially the one in Tokyo, Chicago and Paris, are located next to the most popular tourist spots, and thus are more attractive to customer.

Hotels	No. of Rooms	Nearby Attractions
The Peninsula Hong Kong	300	Victoria Harbour, Harbour City
The Peninsula Shanghai	235	Lujiazui Pudong
The Peninsula Beijing	230	The Palace
The Peninsula New York	235	Empire State Building, Central Park
The Peninsula Chicago	339	Navy Pier, Michigan Avenue Bridge
The Peninsula Tokyo	314	Ginza, Imperial Palace
The Peninsula Bangkok	370	Assumption Cathedral, Chao Phraya River
The Peninsula Manila	469	Glorietta, Ayala Museum
The Peninsula Beverly Hills	105	Universal Studios Hollywood, The Grove
The Peninsula Paris	200	Arc de Triomphe

Source: Hongkong & Shanghai Hotels

Accumulate

CMP: HKD 9.14

(Closing price as at 8 May 2017)

TARGET: HKD 10.48 (+14.66%)

COMPANY DATA

O/S SHARES (MN) :	1,567
MARKET CAP (HKDMN) :	14,321
52 - WK HI/LO (HKD):	9.49 / 7.50

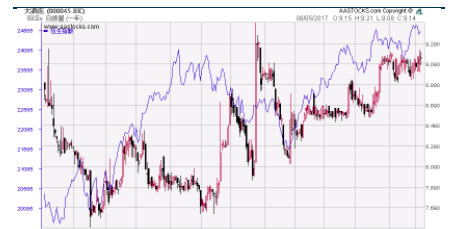
SHARE HOLDING PATTERN • %

Sir Michael David Kadoorie	53.43
----------------------------	-------

PRICE PERFORMANCE • %

	1M	3M	1Y
HK & SH Hotels	0.00	6.16	4.82
HSI	1.14	4.44	21.19

PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

HKD mn	FY15	FY16	FY17E	FY18E
Net Sales	5,741	5,631	5,768	5,849
Net Profit	1,005	667	710	744
EPS, HKD	0.6500	0.4300	0.4534	0.4748
PER, x	13.22	15.02	21.62	22.07
BVPS, HKD	23.6079	23.2029	23.4563	23.4777
P/BV, x	0.43	0.35	0.42	0.45
ROE, %	2.8	1.9	1.9	2.0

Source: Company reports, Phillip Securities Est.

Research Analyst
John Wong
+852 2277 6527
johnycwong@phillip.com.hk

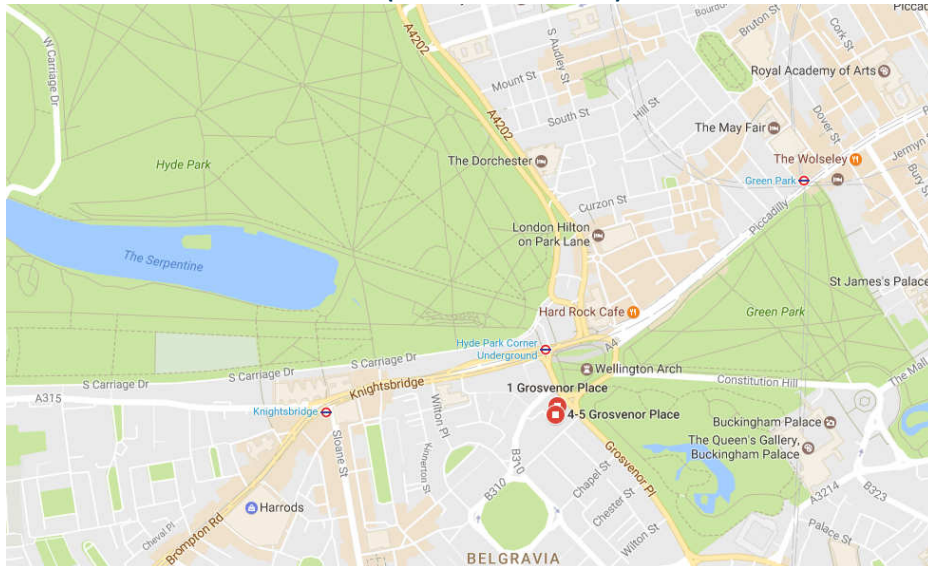
New hotel construction projects are on good track: The group currently has 3 hotel construction projects, namely The Peninsula London, The Peninsula Istanbul and The Peninsula Yangon. In particular, London and Istanbul are two of the most popular tourist attractions in the world especially London. Moreover, Istanbul is popular among the Middle East nations and the Istanbul hotel is expected to primarily attract tourists from those nations.

<i>Hotels</i>	<i>No. of Rooms</i>	<i>Nearby Attractions</i>	<i>Completion Date</i>
<i>The Peninsula London</i>	189	Hyde Park, Green Park	2021
<i>The Peninsula Istanbul</i>	180	Spice Bazaar	2019
<i>The Peninsula Yangon</i>	88	Kandawgyi Lake	2021

Source: Hongkong & Shanghai Hotels

The Peninsula London project's development cost is estimated to be GBP600Mn, which the cost has included the construction of the hotel and 24 to 28 luxury residential apartments, which will be for sales. Moreover, given that London is the central hub of business and tourism of the world, the residential apartment is expected to face strong demand especially it is located between Hyde Park and Green Park, which are the traditional high end residential district, and thus the apartments are expected to be sold at a high price. The hotel will also be in walkable distance to Harrods, Buckingham Palace and Victoria Station, which provides train service to the southern part of the Great Britain. The sales of the residential apartments is expected to cover a substantial proportion of the development cost and will significantly reduce the payback period.

Location of The Peninsula London (1-5 Grosvenor Place)



Source: Google Map

Moreover, the group has reached an agreement with Grosvenor to change their partnership agreement to a landlord-tenant agreement. The company will therefore be entitled to 100% of the proceeds of the future sales of the residential units as well as the profits from the hotel, benefiting the group in the sense that the group will be able to have full control over the operation and management of the hotel and fully utilize its pricing power in the hospitality industry.

Renovation project benefits by increasing room rates: The Peninsula Chicago renovation was completed in April 2016 and the newly refurbished hotel has the highest room rate in Chicago. The Peninsula Beijing has also started to undergo renovation and the renovation project is expected to be completed in mid-2017. The number of room will reduce from 525 rooms to 230 rooms. However, we expect the benefit from the room rate increase will cover the loss in revenue caused by the reduction in the number of rooms.

Investment Thesis, Valuation and Risk

Our valuation model suggests a target price of HK\$10.48: Hongkong & Shanghai Hotels is a leading hotel operation company in the world and has hotels in almost every global gateway cities in the world. The group's expansion to London and Istanbul will produce significant revenue to the group since both cities are cities extremely attractive to tourists. Therefore, we have raised its target price to HK\$10.48, corresponding to a P/E and P/B of 21.62x and 0.42x, with an 'Accumulate' rating assigned. (Closing price as at 8 May 2017)

<i>Downside Risks</i>	<p>(1): Brexit may lead to inconvenience to enter UK by the Schengenian nation citizens</p> <p>(2): Unstable political and safety conditions in Middle East</p> <p>(3): Depreciation of GBP</p>
-----------------------	---

Financials

FYE	FY2014	FY2015	FY2016	FY2017F	FY2018F
Valuation Ratios					
Price Earnings (P/E)	11.36	13.22	15.02	21.62	22.07
Price to Book (P/B)	0.48	0.43	0.35	0.42	0.45
Per Share Data (HKD)					
EPS	0.7600	0.6500	0.4300	0.4534	0.4748
Book Value Per Share	23.6658	23.6079	23.2029	23.4563	23.4777
Dividend Per Share	0.2300	0.2000	0.1900	0.2000	0.2000
Growth & Margins (%)					
Growth					
Revenue	6.0	(1.7)	(1.9)	2.4	3.9
Operating Income	(29.9)	(17.1)	(33.4)	6.6	11.7
Net Profit	(33.9)	(11.1)	(33.6)	6.5	4.7
Margins					
Operating Profit Margin	18.9	17.7	14.6	14.5	14.0
Net Profit Margin	19.4	17.5	11.8	12.3	12.7
Key Ratios					
ROE (%)	3.2	2.8	1.9	1.9	2.0
ROA (%)	2.6	2.2	1.5	1.5	1.6
Income Statement (HKD Mn)					
Revenue	5,838	5,741	5,631	5,768	5,849
- Operating Expenses	(4,733)	(4,727)	(4,807)	(4,935)	(5,032)
Operating Income	1,105	1,014	824	833	817
- Net Non-Operating Gain	257	115	(72)	(32)	23
Pretax Income	1,362	1,129	752	801	840
- Income Tax Expenses	(231)	(124)	(85)	(91)	(96)
Net Profit	1,131	1,005	667	710	744

Source: Company, Phillip Securities (HK) Research Estimates
(Financial figures as at 8 May 2017)

PHILLIP RESEARCH STOCK SELECTION SYSTEMS

Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within $\pm 5\%$ from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

GENERAL DISCLAIMER

This publication is prepared by Phillip Securities (Hong Kong) Ltd ("Phillip Securities"). By receiving or reading this publication, you agree to be bound by the terms and limitations set out below.

This publication shall not be reproduced in whole or in part, distributed or published by you for any purpose. Phillip Securities shall not be liable for any direct or consequential loss arising from any use of material contained in this publication.

The information contained in this publication has been obtained from public sources which Phillip Securities has no reason to believe are unreliable and any analysis, forecasts, projections, expectations and opinions (collectively the "Research") contained in this publication are based on such information and are expressions of belief only. Phillip Securities has not verified this information and no representation or warranty, express or implied, is made that such information or Research is accurate, complete or verified or should be relied upon as such. Any such information or Research contained in this publication is subject to change, and Phillip Securities shall not have any responsibility to maintain the information or Research made available or to supply any corrections, updates or releases in connection therewith. In no event will Phillip Securities be liable for any special, indirect, incidental or consequential damages which may be incurred from the use of the information or Research made available, even if it has been advised of the possibility of such damages.

Any opinions, forecasts, assumptions, estimates, valuations and prices contained in this material are as of the date indicated and are subject to change at any time without prior notice.

This material is intended for general circulation only and does not take into account the specific investment objectives, financial situation or particular needs of any particular person. The products mentioned in this material may not be suitable for all investors and a person receiving or reading this material should seek advice from a financial adviser regarding the suitability of such products, taking into account the specific investment objectives, financial situation or particular needs of that person, before making a commitment to invest in any of such products.

This publication should not be relied upon as authoritative without further being subject to the recipient's own independent verification and exercise of judgment. The fact that this publication has been made available constitutes neither a recommendation to enter into a particular transaction nor a representation that any product described in this material is suitable or appropriate for the recipient. Recipients should be aware that many of the products which may be described in this publication involve significant risks and may not be suitable for all investors, and that any decision to enter into transactions involving such products should not be made unless all such risks are understood and an independent determination has been made that such transactions would be appropriate. Any discussion of the risks contained herein with respect to any product should not be considered to be a disclosure of all risks or a complete discussion of such risks.

Nothing in this report shall be construed to be an offer or solicitation for the purchase or sale of a security. Any decision to purchase securities mentioned in this research should take into account existing public information, including any registered prospectus in respect of such security.

Disclosure of Interest

Analyst Disclosure: Neither the analyst(s) preparing this report nor his associate has any financial interest in or serves as an officer of the listed corporation covered in this report.

Firm's Disclosure: Phillip Securities does not have any investment banking relationship with the listed corporation covered in this report nor any financial interest of 1% or more of the market capitalization in the listed corporation. In addition, no executive staff of Phillip Securities serves as an officer of the listed corporation.

Availability

The information, tools and material presented herein are not directed, intended for distribution to or use by, any person or entity in any jurisdiction or country where such distribution, publication, availability or use would be contrary to the applicable law or regulation or which would subject Phillip Securities to any registration or licensing or other requirement, or penalty for contravention of such requirements within such jurisdiction.

Information contained herein is based on sources that Phillip Securities (Hong Kong) Limited ("PSHK") believed to be accurate. PSHK does not bear responsibility for any loss occasioned by reliance placed upon the contents hereof. PSHK (or its affiliates or employees) may have positions in relevant investment products. For details of different product's risks, please visit the Risk Disclosures Statement on <http://www.phillip.com.hk>.

© 2017 Phillip Securities (Hong Kong) Limited

Contact Information (Regional Member Companies)

SINGAPORE**Phillip Securities Pte Ltd**

Raffles City Tower
250, North Bridge Road #06-00
Singapore 179101
Tel : (65) 6533 6001
Fax : (65) 6535 6631
Website: www.poems.com.sg

HONG KONG**Phillip Securities (HK) Ltd**

Exchange Participant of the Stock Exchange of Hong Kong
11/F United Centre 95 Queensway
Hong Kong
Tel (852) 22776600
Fax (852) 28685307
Websites: www.phillip.com.hk

INDONESIA**PT Phillip Securities Indonesia**

ANZ Tower Level 23B,
Jl Jend Sudirman Kav 33A
Jakarta 10220 – Indonesia
Tel (62-21) 57900800
Fax (62-21) 57900809
Website: www.phillip.co.id

THAILAND**Phillip Securities (Thailand) Public Co. Ltd**

15th Floor, Vorawat Building,
849 Silom Road, Silom, Bangrak,
Bangkok 10500 Thailand
Tel (66-2) 6351700 / 22680999
Fax (66-2) 22680921
Website: www.phillip.co.th

UNITED KINGDOM**King & Shaxson Capital Limited**

6th Floor, Candlewick House,
120 Cannon Street,
London, EC4N 6AS
Tel (44-20) 7426 5950
Fax (44-20) 7626 1757
Website: www.kingandshaxson.com

AUSTRALIA**PhillipCapital Australia**

Level 12, 15 William Street,
Melbourne, Victoria 3000, Australia
Tel (613) 96188238
Fax (613) 92002272
Website: www.phillipcapital.com.au

MALAYSIA**Phillip Capital Management Sdn Bhd**

B-3-6 Block B Level 3 Megan Avenue II,
No. 12, Jalan Yap Kwan Seng, 50450
Kuala Lumpur
Tel (603) 21628841
Fax (603) 21665099
Website: www.poems.com.my

JAPAN**PhillipCapital Japan K.K.**

Nagata-cho Bldg.,
8F, 2-4-3 Nagata-cho,
Chiyoda-ku, Tokyo 100-0014
Tel (81-3) 35953631
Fax (81-3) 35953630
Website: www.phillip.co.jp

CHINA**Phillip Financial Advisory (Shanghai) Co. Ltd**

No 436 Hengfeng Road,
Greentech Unit 604,
Postal code 200070
Tel (86-21) 51699400
Fax (86-21) 63532643
Website: www.phillip.com.cn

FRANCE**King & Shaxson Capital Limited**

3rd Floor, 35 Rue de la Bienfaisance 75008
Paris France
Tel (33-1) 45633100
Fax (33-1) 45636017
Website: www.kingandshaxson.com

UNITED STATES**Phillip Futures Inc**

141 W Jackson Blvd Ste 3050
The Chicago Board of Trade Building
Chicago, IL 60604 USA
Tel +1.312.356.9000
Fax +1.312.356.9005