

Fortune REIT (778.HK)

Stable Growth in 2017 and Disposal of One Property

Hong Kong | Property | Company Report

7 March 2018

Investment Summary

- Stable growth in 2017 with effective cost controls;
- Improving occupancy of some assets and disposal of one property;
- AEs underpin future growth.

Business Overview

Stable growth in 2017. Fortune REIT reported revenue of HKD2030.3mn (+2.8% YoY) and net property income of HKD1456.7mn (+3.3% YoY). Higher net property income growth than revenue increase is mainly attributable to effective cost control measures, given continuously decreasing cost-to-revenue ratio from 26.4% in 2016 to 26% in 2017. Income available for distribution amounted to HKD 970.8mn representing YoY growth 3.8%, due to faster net income growth and declining financing cost. Finance costs over revenue ratio decreased to 13.21% compared 14.4% in 2016. We see that interest cost for 60% (2016: 67%) of outstanding debts was hedged through interest rate swaps and caps, which will cushion potential financial risks with expected US interest rate hike and tapering of Fed balance sheet. Meanwhile, Fortune REIT has kept steady dividend, given 2017 final dividend HKD0.2525 implying 3.27% YoY growth.

Effective cost controls. 2017 property operating expenses (excluding manager's performance fee) increased by 1.2% YoY to HKD528.3mn. Cost-to-revenue ratio continue to decline to 26% (2016: 26.4%), the lowest level since 2011. This is due to management's continued efforts in energy saving, given reduced electricity consumption and lower utility expenses in 2017.

Figure: Cost-to-revenue ratio

Year	2011	2012	2013	2014	2015	2016	2017
1H	26.3%	26.7%	26.0%	26.3%	26.9%	25.7%	25.3%
2H	27.2%	27.0%	27.4%	27.7%	27.5%	26.4%	26.7%
1Y	27.2%	27.0%	27.4%	27.7%	27.5%	26.4%	26.0%

Source: Company, Phillip Securities

Improving occupancy of some assets. Fortune REIT currently operates 17 property assets in HK, comprising approximately 3.18mn sq.ft. of retail space and 2713 car parking lots. The portfolio now has 1392 tenants, of which top 10 together contributed 27.8% to gross rental income and accounted for 22.4% of total GRA. Tenants in the non-discretionary trades made up around 70% of total GRA, including supermarkets, food and beverages as well as services and education. Occupancy continue to improve, given overall occupancy rate climbed by 1.4% to 98.1% in 2017 and majority property assets achieved better occupancy (i.e. Fortune Metropolis +2.9%, Caribbean Square +1.7%, and Hampton Loft +33.6%). We attribute this to effective measures involving optimizing tenant mix, retaining quality tenants, and achieving early commitment to renewal before leases expire.

No Rating

CMP HKD9.21

(Closing price at 5 Mar 2018)

COMPANY DATA

O/S SHARES (MN) :	1,914
MARKET CAP (HKDMN) :	17,726
52 - WK HI/LO (HKD):	9.87 / 8.52

SHARE HOLDING PATTERN , %

CK Asset	27.59
Schroder Inv Mgt	12.01

PRICE PERFORMANCE , %

	1M	3M	1Y
Fortune REIT	-0.86	-2.95	6.34
HSI	-6.36	4.68	28.19

RETURN VS. HSI



Source: Aastocks, Phillip Securities (HK) Research

KEY FINANCIALS

HKD mn	FY14	FY15	FY16	FY17
Revenue	1656	1882	1975	2030
Net Income	1161	1324	1410	1457
EPU, HKD	2.10	1.32	0.66	1.68
PER, x	4.39	6.98	13.95	5.49
BVPU, HKD	11.93	12.76	12.90	14.05
P/BV, x	0.77	0.72	0.71	0.66
ROE, %	17.61	10.35	5.11	11.94

Source: Company, Phillip Securities Est.

Eurus Zhou (2277 6515)
euruszhou@phillip.com.hk

Figure: Property Assets

Property	GRA (Sq.Ft.)	Valuation HK\$ million	Number of Carpark Lots	Occupancy	Change
Fortune City One	414,469	7,939	653	98.40%	0.00%
Fortune Kingswood	665,244	7,462	622	95.80%	-2.60%
Ma On Shan Plaza	310,084	5,489	290	99.00%	-0.20%
Metro Town	180,822	3,590	74	100.00%	0.00%
Fortune Metropolis	332,168	2,557	179	98.40%	+2.90%
Laguna Plaza	163,203	2,450	150	96.40%	-0.60%
Belvedere Square	276,862	2,370	329	99.60%	-0.40%
Waldorf Avenue	80,842	1,651	73	100.00%	0.00%
Caribbean Square	63,018	1,080	117	100.00%	+1.70%
Provident Square	180,238	1,061	N/A	98.10%	+13.50%
Jubilee Square	170,616	892	97	97.80%	+0.90%
Smartland	123,544	723	67	97.50%	+1.40%
Tsing Yi Square	78,836	656	27	100.00%	+1.00%
Centre de Laguna	43,000	299	N/A	98.90%	-1.10%
Hampton Loft	74,734	283	35	100.00%	+33.60%
Lido Avenue	9,836	190	N/A	100.00%	0.00%
Rhine Avenue	14,604	120	N/A	100.00%	0.00%
Total / Overall average	3,182,120	38,812	2,713	98.10%	+1.4%

Source: Company, Phillip Securities

Proposed sale of Provident Square in 2018. In Dec 2017, Fortune REIT disclosed disposal of Provident Square for HKD2bn at 1.8% yield. The disposed value is 3.1 times its purchase price and 88.5% over its appraised value as at 30 Nov 2017 after 5-year holding period. The deal results in a gain of HKD921mn after completion on 28 Feb 2018. The proceeds will be used in asset enhancement initiatives (AEIs), debt repayment, etc. We expect debt over asset ratio to drop after the transaction.

AEIs underpin future growth. AEIs of Fortune Kingswood will commence in 18Q2. Fortune Kingswood is now the largest asset of Fortune REIT, contributing 18.5% of portfolio revenue and 19.2% of portfolio value (HKD7426mn). It was set up in 1996 without any renovation since. It is believed that Fortune Kingswood has great potential to be unlocked for being the largest shopping mall in Tin Shui Wai. Proposed AEIs will build Fortune Kingswood a regional shopping and entertainment hub absorbing more customers from Yuen Long area. The first-phase project will be launched in 18Q2 focusing on West Block renovation with an expected capex of HKD150mn. We are positive on Fortune Kingswood's potential to expand catchment and boost future income.

Financials

FYE	2013	2014	2015	2016	2017
Valuation Ratios					
Price to Earnings (P/E)	4.46	4.39	6.98	13.95	5.49
Price to Book (P/B)	0.90	0.77	0.72	0.71	0.66
Per Share Data (HKD)					
EPU	2.07	2.10	1.32	0.66	1.68
Book Value Per Unit	10.26	11.93	12.76	12.90	14.05
Dividend Per Unit	0.36	0.42	0.47	0.49	0.51
Growth (%)					
Revenue	18.30	25.68	13.67	4.95	2.77
Pretax Income	60.90	8.46	-34.60	-45.22	132.75
Income Available for Distribution	16.91	21.54	13.29	5.72	3.80
Margins (%)					
Net Property Income Margin	70.46	72.31	72.53	73.58	73.98
Pretax Income Margin	287.06	247.73	142.53	74.39	168.48
Income Available for Distribution Margin	48.76	47.15	47.00	47.34	47.82
Key Ratios					
ROE (%)	20.15	17.61	10.35	5.11	11.94
ROA (%)	12.03	11.70	6.77	3.39	8.08
FYE					
2013					
2014					
2015					
2016					
2017					
Income Statement (HKD Mn)					
Revenue	1,317.5	1,655.8	1,882.1	1,975.4	2,030.2
-Operating expenses	-389.1	-494.6	-558.1	-565.6	-573.4
Net property income	928.3	1,161.2	1,324.0	1,409.8	1,456.7
- Other G/L	2,853.6	2,940.6	1,358.6	59.8	1,963.6
Pretax Income	3,781.9	4,101.8	2,682.6	1,469.6	3,420.3
Tax Expenses	-132.5	-170.9	-196.5	-211.7	-219.3
Distribution to unitholder	-642.4	-780.8	-884.6	-935.2	-970.8
Profit after Distribution	3,007.0	3,150.1	1,601.6	322.7	2,230.2

Source: Company, Aastocks, Phillip Securities (HK) Research
(Financial figures as at 5 Mar 2018)

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>.

© 2018 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