

Renhe Commercial Holdings (1387 HK): Uncertain Earnings Outlook, Cash Collection a Tough Task; Maintain Underperform

Rating UNDERPERFORM

Price Target HK\$0.28

Price HK\$0.33

Key Takeaway

Renhe interim came in at a core net loss of RMB380mn, below our expectation due to no revenue contribution from transfer of operating rights in 1H12. No interim dividend was declared. Stretched cash flow and poor visibility remain our key concern. Debt servicing should be a top priority before searching for growth. Maintain Underperform.

Interim at a loss: Renhe reported a core net loss of RMB380mn, below expectation mainly because of no revenue contribution from the transfer of operation rights in 1H12. Leasing income grew 21% driven by an 18% increase in average rent. Due to the volatile recognition of transfer of operating rights, margins dropped significantly. Despite the net revaluation of RMB1.75bn, net gearing climbed 3ppts to 28% at interim from end-2011.

Cash collection a difficult task: Renhe's cash on hand declined to RMB1.4bn as at end-June from RMB2.2bn as at end-2011. Trade receivable amount was about RMB2.2bn with RMB150mn collected in 1H12. Together with the RMB1.6bn receivables from BVI disposal, Renhe still had RMB3.8bn uncollected cash as compared to approximately RMB2.2bn budgeted cash outflow in 2H12. Based on management guidance, about RMB1.3bn could be collected before end of the year, which is not significant to improve the financial position, in our view.

Low visibility in challenging market: There would be RMB1bn from Hunan Yueyang to be recognised in 2H12 according to the management. While the macro outlook stays challenging, revenue upside from the transfer of operating rights is increasingly unpredictable. Growth in leasing income may only come slowly in view of 5-10% rental reversion.

Debt servicing a top priority, Maintain Underperform: Renhe recurring income is still a low base of RMB201mn at interim. We see refinancing a risk on US\$300mn senior notes (11.75% p.a.) due in 2015. We believe its rental property businesses will take time to materialize while no timetable for asset disposal can be expected. At 54% NAV disc, similar to the sector average, Renhe would be under pressure as it is still in the mode of collecting cash. Maintain Underperform.

Valuation/Risks. Our 12-month target price of HK\$0.28 is based on a 60% discount to 2012E NAV (WACC: 15%). Upside risks: stronger-than-expected transfer of operating rights; significant improvement in cash collection; and sharp rental growth.