Issuer Profile:
Neutral (3)

Ticker:
WHARF

Seow Zhi Qi
+65 6530 7348
zhiqiseow@ocbc.com

Wharf Holdings Ltd ("WHARF")

Recommendation

- **In 1H2019, revenue rose 3% y/y to HKD8.1bn from HKD7.8bn, on the back of stronger performance from IP though partially offset by the DP segment. Recurring income made up 29% of WHARF's revenue and 34% of the total operating profit in 1H2019.**
- **A drift towards IP was observed. For profit before tax which includes share of results of associates and joint ventures, DP/IP split was 30%/41% (2018: 69%/26%, 1H2018: 53%/37%). We think this trend is likely to persist and may skew further towards IP given that Tower 2 at Changsha IFS (under IP) will open and WHARF has not purchased any new land recently.**
- **Net gearing was 16.9%, though lower at 12.6% if we exclude debts that are non-resource to WHARF and its subsidiaries. EBITDA/Interest (including capitalised interest) was 6.3x, up from 4.7x a year ago. WHARF continues to have healthy liquidity with more than enough cash (HKD19.0bn) to pay off its short term debt (HKD9.5bn). We are maintaining WHARF's Neutral (3) Issuer Profile.**
- **We are neutral on WHARF 4.5% '21. We think the bond is trading largely fair relative to its peers. WHEELK 4.5% '21, which we have on an Issuer Profile of Positive (2), is offering a similar yield for an almost matching tenor.**

Relative Value

Bond	Maturity / Call date	Net gearing	Ask YTC / YTM	Spread
WHARF 4.5% '21	20/07/2021	17%	2.37%	77bps
WHEELK 4.5% '21	02/09/2021	25%	2.39%	79bps

Indicative prices as at 14 August 2019 Source: Bloomberg
Aggregate leverage based on latest available quarter

Background

- The Wharf (Holdings) Limited ("WHARF") was established and listed on the Hong Kong stock exchange in 1886. In November 2017, WHARF spun off its major portfolio of investment properties in Hong Kong which is currently listed as Wharf REIC.
- Today, WHARF principally engages in the following businesses
  - i) Investment Properties ("IP") – lease mainly retail and office properties in Mainland China
  - ii) Development Properties ("DP") – activities related to acquisition of land, construction and sales of properties in Hong Kong and Mainland China
  - iii) Hotels segment – operate 17 hotels in the Asia Pacific region, four of which owned by the Group
  - iv) Logistics segment – container terminal operations in Hong Kong and Mainland China
- WHARF is a subsidiary of Wheelock & Co. Ltd, which owns a 64.39% stake in the company.

Key Considerations

- **Contributions from DP in Mainland China slipped:** At present, WHARF is most exposed to Mainland China, which holds 68% of its total business assets (over RMB100bn). These assets generated 72% of the Group's revenue and 79% of total underlying net profit. DP in China recorded a 10% decline y/y in revenue to HKD5.2bn (including contributions from joint ventures and associates). Operating profit though fell by a mere 1% y/y to HKD1.8bn. Contracted sales also fell by 10% y/y to ~HKD7.2bn (i.e. RMB6.5bn). Net book order was ~HKD26.1bn (i.e. RMB23.5bn). We note that WHARF has land bank totalling 3.6mn sq m and has not made any new land purchase for nearly one year as the primary sales pricing is effectively controlled by government which seriously affects future project profitability. We think that government policy is likely to direct the performance of this business segment for WHARF going forward.

- **IP in Mainland China did well**: Revenue from this segment rose 22% y/y to HKD2.0bn, while operating profit was up by 30% y/y to HKD1.2bn. Both were due to the HKD0.4bn fresh revenue contribution from Changsha IFS (opened in late 2018) and a 14% y/y increase in revenue generated at Chengdu IFS to HKD0.9bn. Over 1H2019, Chengdu IFS saw tenant sales increase by 13% y/y and foot fall higher by 9% y/y. For Changsha IFS, Tower 2 (office property) is due to open in 2021. We note that management is expecting the oversupply in the office sector in most cities to increase in the coming years. The retail portion at Changsha IFS is 98% occupied. Overall DP and IP in Mainland China saw revenue down by 3% y/y to HKD7.2bn, while operating profit up by 11% y/y to HKD2.5bn. We note that RMB weakened by 4% against HKD in 1H2019, and this has continued into 2H2019 thus far. We think WHARF may potentially be negatively impacted.

- **Substantial recurring income:** The IP and Hotel business segments make up WHARF's recurring income. These accounted for 29% of WHARF's revenue (1H2018: 24%) and 34% of total operating profit (1H2018:36%) in 1H2019. Revenue from IP and Hotel was HKD2.3bn (+21% y/y) while operating profit generated was HKD1.3bn (+25% y/y) which alone is more than sufficient to cover for its interest expenses of HKD0.6bn (including capitalised interest). Profit before tax of both segments though was largely stable at HKD1.6bn (-0.5% y/y). We continue to see the DP and IP split at WHARF drift towards IP. For profit before tax which includes share of results of associates and joint ventures, DP/IP split was 30%/41% (2018: 69%/26%, 1H2018: 53%/37%). We think this trend is likely to persist and may skew further towards IP given that Tower 2 at Changsha IFS will open and WHARF has not purchased any new land.

- **Pipeline of DP in Hong Kong:** Over 1H2019, Mount Nicholson saw total contracted sales of HKD3.6bn as demand for luxury homes remain steady. While contributions from DP in Hong Kong have been somewhat low, WHARF has a handful of projects underway. They are
  i) 11 Plantation Road which will provide 7 houses (GFA 46,000 sq ft)
  ii) 77 Peak Road which will provide 8 houses (GFA 42,000 sq ft)
  iii) 1 Plantation Work which will provide 20 houses (GFA 91,000 sq ft)
  iv) Kowloon Tong Residential Project (foundation work is in progress for 4 blocks of 13 storey residential buildings, GFA 436,000 sq ft)
  v) Kowloon East Waterfront Portfolio which comprises Kowloon Godown (considering redevelopment options) and 15%-owned Yau Tong Bay (provide 6,300 residential units, GFA 4mn sq ft).

- **Manageable credit metrics:** Net debt was reduced by 4% y/y to HKD24.6bn from HKD25.6bn leading to net gearing ratio of 16.9%. Excluding debts that are non-resource to WHARF and its subsidiaries, net debt was HKD18.4bn and adjusted net gearing was 12.6%. EBITDA/Interest (including capitalised interest) was 6.3x, up from 4.7x a year ago. WHARF continues to have healthy liquidity with more than enough cash (HKD19.0bn) to pay off its short term debt (HKD9.5bn).

Explanation of Issuer Profile Rating / Issuer Profile Score

Positive ("Pos") – The issuer's credit profile is either strong on an absolute basis, or expected to improve to a strong position over the next six months.

Neutral ("N") – The issuer's credit profile is fair on an absolute basis, or expected to improve / deteriorate to a fair level over the next six months.

Negative ("Neg") – The issuer's credit profile is either weaker or highly geared on an absolute basis, or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7 point Issuer Profile Score scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

Please note that Bond Recommendations are dependent on a bond's price, underlying risk free rates and an implied credit spread that reflects the strength of the issuer's credit profile. Bond Recommendations may not be relied upon if one or more of these factors change.

Explanation of Bond Recommendation

Overweight ("OW") – The performance of the issuer's specific bond is expected to outperform the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Neutral ("N") – The performance of the issuer's specific bond is expected to perform in line with the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Underweight ("UW") – The performance of the issuer's specific bond is expected to underperform the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Other

Suspension – We may suspend our issuer rating and bond level recommendation on specific issuers from time to time when OCBC is engaged in other business activities with the issuer. Examples of such activities include acting as a joint lead manager or book runner in a new issue or as an agent in a consent solicitation exercise. We will resume our coverage once these activities are completed.

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Treasury Research & Strategy

Macro Research

Selena Ling
Head of Strategy & Research
LingSSSelena@ocbc.com

Emmanuel Ng
Senior FX Strategist
NgCYEmmanuel@ocbc.com

Tommy Xie Dongming
Head of Greater China Research
XieD@ocbc.com

Terence Wu
FX Strategist
TerenceWu@ocbc.com

Howie Lee
Thailand, Korea & Commodities
HowieLee@ocbc.com

Alan Lau
Malaysia & Indonesia
AlanLau@ocbc.com

Carie Li
Hong Kong & Macau
carierli@ocbcwh.com

Dick Yu
Hong Kong & Macau
dicksnyu@ocbcwh.com

Credit Research

Andrew Wong
Credit Research Analyst
WongVKAM@ocbc.com

Ezien Hoo
Credit Research Analyst
EzienHoo@ocbc.com

Wong Hong Wei
Credit Research Analyst
WongHongWei@ocbc.com

Seow Zhi Qi
Credit Research Analyst
ZhiQiSeow@ocbc.com

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