# Sunac Services (1516 HK)

## Set for a fast overtaking to Top 5; Initiate at Buy

Despite a relatively slower start, we expect Sunac Services to deliver one of the fastest growths in both GFA expansion and earnings growth. The key drivers would be 1) strong third-party bidding capability by leveraging its premium brand, strong city presence and leading incentive mechanism that may contribute 42-47% of newly added GFA under management; 2) community VAS that would accelerate from a low penetration rate and new initiatives. Together with strong support from parentco and margin trend, the net profits may grow 72% CAGR to RMB3bn in 2023E backed by the recent higher-than-expected 1H21 profits alert. Initiate with Buy and our risk-reward study indicates attractive.

- **Third-party bidding will become the key driver for GFA growth:** We are confident of its third-party expansion capability due to 1) its premium brand and high market share especially in Yangtze River Delta/Southwest which it could leverage. 2) Market-leading incentive mechanism: Not only it will offer reward 20% of first-year net profits in the newly acquired projects to the expansion team, but also it has set up a GFA-expansion KPI for the staff in Sunac Group to bring in synergy. With team size quickly rocketing to 210 in Apr 2021 from 100 in 2020, we think it would contribute 42-47% of new GFA under management and drive it to reach 478mn sq m by 2023E (52% CAGR).
- **Community VAS may see explosive growth to contribute 10% of total revenue by 2023E:** From a low base that it only contributed 4% of group revenue, we expect Company to make this business its second growth curve via increasing penetration rate in the traditional business (decoration and cleaning) and improving sentiment on property agent and advertisement business. Therefore, it is estimated to see a 2020-23E CAGR of 118% to reach RMB1.8bn or 10% of group revenue.
- **We also expect to see a margin uptrend:** Besides a fast growth of its top line, we expect gross margin and net margin to expand to 29% and 15% by 2023E. This is mainly driven by the basic PM business (GPM at 22% in 2020) that could improve from economies of scale, digitalization plan that may reduce 10% of staff costs in some projects as well as high-margin M&A projects (such as Zhangtai PM that has 40% GP margin).
- **Initiate at Buy with TP of HK$ 29.80.** With all above, we expect earnings to grow 72% CAGR in 2020-23E, reaching RMB3bn. Based on our scorecard, we assigned 30x 2022E PE to derive target price of HK$29.8/share. Currently it is trading at 19.5x 2022E PE vs. industry average of 20.5x PE. **Catalysts:** management raises full-year guidance; high-quality M&A; **Risks**: parentco's liquidity under distress; potential failure in M&A; IPO investors sell off.

**Earnings Summary**

| (YE 31 Dec) | FY19A | FY20A | FY21E | FY22E | FY23E |
|---|---|---|---|---|---|
| **Revenue (RMB mn)** | 2,827 | 4,623 | 8,873 | 14,188 | 21,021 |
| **YoY growth (%)** | 85.5 | 155.1 | 74.6 | 48.6 | 36.5 |
| **Net income (RMB mn)** | 270 | 601 | 1,233 | 1,981 | 3,072 |
| **EPS (RMB)** | 0.12 | 0.25 | 0.51 | 0.83 | 1.28 |
| **YoY growth (%)** | N.A. | N.A. | 114.7 | 105.3 | 60.6 |
| **Consensus EPS (RMB)** | N.A. | N.A. | 0.41 | 0.65 | 0.92 |
| **P/E (x)** | N.A. | 64.1 | 31.2 | 19.5 | 12.6 |
| **P/B (x)** | N.A. | N.A. | 5.4 | 4.8 | 4.0 |
| **ROE (%)** | 73.5 | 6.2 | 12.4 | 17.4 | 22.5 |
| **Net gearing (%)** | Net cash | Net cash | Net cash | Net cash | Net cash |

Source: Company data, Bloomberg, CMBIS estimates

**BUY (Initiation)**

| | |
|---|---|
| **Target Price** | **HK$29.80** |
| **Up/Downside** | **+53.8%** |
| **Current Price** | **HK$19.38** |

**China Property Service Sector**

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**Stock Data**

| | |
|---|---|
| Mkt Cap (HK$ mn) | 83,174 |
| Avg 3 mths t/o (HK$ mn) | 179.57 |
| 52w High/Low (HK$) | 29.4/11.43 |
| Total Issued Shares (mn) | 3,104 |

Source: Bloomberg

**Shareholding Structure**

| | |
|---|---|
| Sunac Holdings | 71.72% |
| Free float | 28.28% |

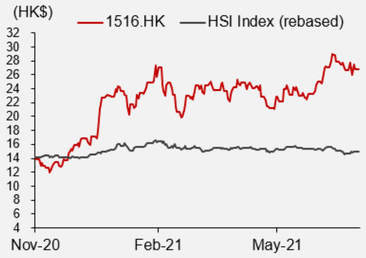
Source: HKEx

**Share Performance**

| | Absolute | Relative |
|---|---|---|
| 1-mth | 7.3% | 10.3% |
| 3-mth | 6.0% | 10.2% |
| 6-mth | 13.6% | 20.3% |
| 12-mth | N.A. | N.A. |

Source: Bloomberg

**12-mth Price Performance**




Source: Bloomberg

**Auditor: PwC**

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## Contents

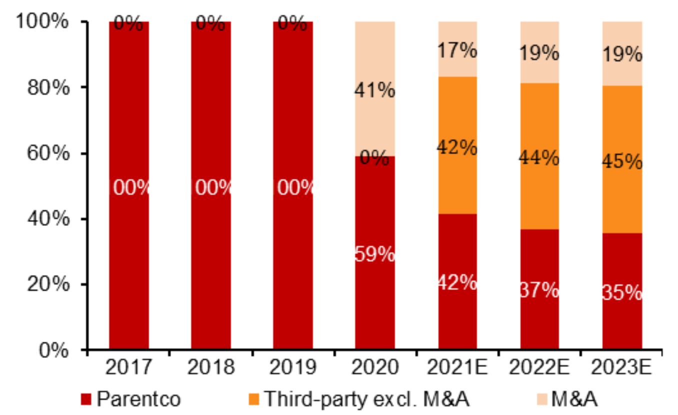
# Focus Charts

## Figure 1: key drivers

| Key drivers | 2017 | 2018 | 2019 | 2020 | 2021E | 2022E | 2023E |
|---|---|---|---|---|---|---|---|
| **Managed GFA (mn sqm)** | **20** | **29** | **53** | **135** | **236** | **350** | **478** |
| YoY growth | | 43% | 85% | 155% | 75% | 49% | 36% |
| Sunac Group affiliates | 20 | 28 | 53 | 92 | 137 | 184 | 231 |
| Third party | - | - | - | - | 36 | 79 | 129 |
| M&A | 0 | 0 | 0 | 43 | 63 | 88 | 118 |
| | | | | | | | |
| Contracted GFA (mn sqm) | 57 | 97 | 158 | 264 | 384 | 519 | 674 |
| YoY growth | | 69% | 63% | 67% | 45% | 35% | 30% |
| | | | | | | | |
| **Revenue (RMB mn)** | **1,112** | **1,842** | **2,827** | **4,623** | **8,873** | **14,188** | **21,021** |
| YoY growth | | 65.7% | 53.5% | 63.5% | 91.9% | 59.9% | 48.2% |
| Property management services | 575 | 760 | 1,148 | 2,774 | 5,904 | 9,536 | 13,778 |
| VAS to non-property owners | 524 | 1,029 | 1,572 | 1,673 | 2,569 | 3,797 | 5,419 |
| Community VAS | 13 | 53 | 107 | 176 | 399 | 855 | 1,824 |
| | | | | | | | |
| **Gross margin** | **21%** | **23%** | **25%** | **28%** | **28%** | **28%** | **29%** |
| Property management services | 2% | 6% | 12% | 22% | 23% | 23% | 23% |
| VAS to non-property owners | 42% | 35% | 35% | 36% | 36% | 36% | 36% |
| Community VAS | 20% | 23% | 35% | 46% | 48% | 50% | 50% |
| | | | | | | | |
| **Net profits (RMB mn)** | **43** | **98** | **270** | **601** | **1,233** | **1,981** | **3,072** |
| YoY growth | | 129% | 175% | 123% | 105% | 61% | 55% |
| Net margin | 4% | 5% | 10% | 13% | 14% | 14% | 15% |

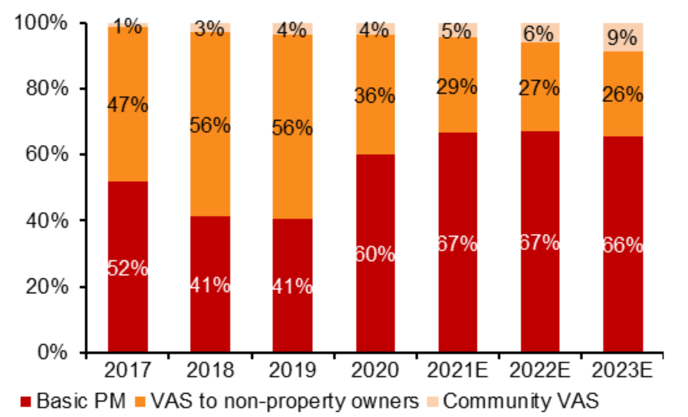
Source: CMBIS

## Figure 2: Newly-added Managed GFA by channels (third-party bidding will be the key driver)



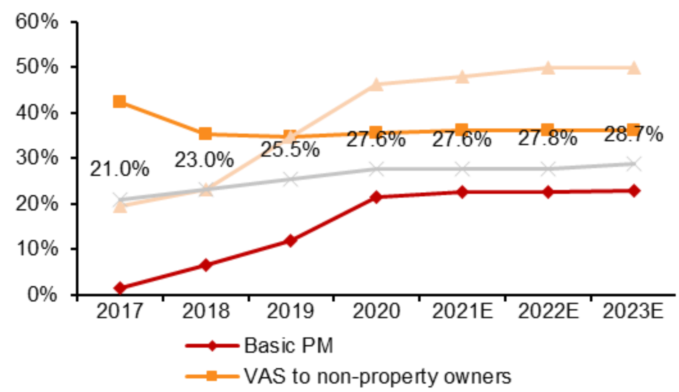

Source: Company data, CMBIS estimates

## Figure 3: Its contribution to group revenue will increase to 21%, catching up with the industry



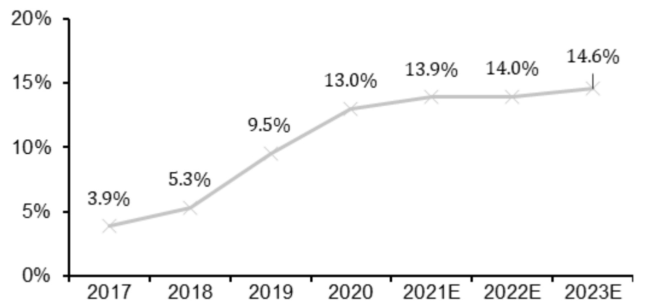

Source: Company data, CMBIS estimates

## Figure 4: Segment gross margin




Source: Company data, CMBIS estimates

## Figure 5: Net margin trend




Source: Company data, CMBIS estimates

## Scenarios study

As Sunac services have a close tie with its parentco on the business side (GFA expansion and VAS), the outlook of its parentco under the macro situation would also have some impacts and that is why we need to do the below scenario studies.

**Figure 6: Scenario study**

| Scenarios | Key assumptions | Target PE Multiple | PT (HKD/share) | Upside (downsdie) |
|---|---|---|---|---|
| Bear case | 1. Parentco slows down land acquisitions and its annual sales growth to 5% or below in order to deleverage earlier than expected.<br><br>2. Third-party bidding faces fierce competition in Yangtze River delta and may fall behind its target. Also M&A acquisitions are slower than expected. As a result GFA under management may only grow 44% 2020-23E CAGR<br><br>3. Community VAS find less smooth in penetrating new businesses and | 18x 2022E PE | 16.5 | -15% |
| Base case | 1. Parentco deleverages to meet all regulatory requirements by 2023 and continue to grow its annual sales at 5-10% YoY.<br><br>2. Third-party bidding goes as planned and will contribute 42-45% of newly-added GFA under management. Maintain one or two sizable and high-quality M&A deals per year so GFA under management can grow 52% 2020-23E CAGR<br><br>3. Community VAS grows explosively from a low base to achieve 118% 2020-23E CAGR | 30x 2022E PE | 29.8 | +54% |
| Bull case | 1. Parentco deleverages to meet all regulatory requirements by 2023 and continue to grow its annual sales at 5-10% YoY.<br><br>2. Third-party bidding expands faster-than-expected due to its strong team and branding. Also manage to secure some sizable and high-quality M&A deals per year like Zhangtai PM company.<br><br>3. Community VAS grows faster-than-expected on new initiatives. | 35x 2022E PE | 34.8 | +79% |

Source: CMBIS

## Company Overview

Sunac Services is one of the largest property management companies in China. Since its establishment, the Group has continued to create a better life by serving customers as its core. The Group has established a leading market position as one of the fastest growing large-scale comprehensive property management service providers in China focusing on mid-to-high-end properties in core cities. Also, the Group offers a full range of high-quality property services to its customers and is dedicated to becoming the “Leading Quality Service Provider in China. As at 31 Dec 2020, the total contracted area under management of the Group was approximately 264 million sq m, and the area under management was approximately 135 million sq m. On 19 Nov 2020, Sunac Services was successfully listed on the Main Board of The Stock Exchange of Hong Kong.

**Figure 7: Listed PMco Ranking by GFA under management**

| Company Name (mn sq m) | Ticker | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|
| Poly Services | 6049 HK | 106 | 191 | 287 | 380 |
| Country Garden Services | 6098 HK | 123 | 182 | 276 | 377 |
| A-Living | 3319 HK | 54 | 94 | 177 | 375 |
| Evergrande Services | 6666 HK | 138 | 185 | 238 | 300 |
| Greentown Service | 2869 HK | 138 | 170 | 212 | 248 |
| COPH | 2669 HK | 128 | 141 | 151 | 182 |
| Shimao Services | 873 HK | 43 | 45 | 68 | 146 |
| Sunac Services | 1516 HK | 20 | 29 | 53 | 135 |
| CR Mixc Lifestyle | 1209 HK | 61 | 85 | 101 | 119 |
| Languang Justbon | 2606 HK | 44 | 61 | 72 | 117 |
| Ever Sunshine | 1995 HK | 27 | 40 | 65 | 102 |
| Central China New Life | 9983 HK | 20 | 26 | 57 | 100 |
| S-Enjoy | 1755 HK | 36 | 43 | 60 | 100 |
| Kaisa Prosperity | 2168 HK | 24 | 27 | 46 | 57 |
| KWG Living | 3913 HK | 12 | 14 | 18 | 29 |
| Redsun Services | 1971 HK | 9 | 10 | 16 | 27 |
| Powerlong CM | 9909 HK | 15 | 16 | 18 | 21 |
| Excellence CM | 6989 HK | 7 | 9 | 10 | 12 |

Source: Company data

Its parentco Sunac Group (who owns 72% of the listco) was the 4th largest developer in China in terms of sales and it has recorded RMB575bn contracted sales in 2020. As of 2020, it has a land reserve of 258mn sq m with 78% of them located in Tier 1-2 cities.

# Investment thesis

## 52% GFA growth CAGR in 2020-23E driven by third-party bidding

We are confident that Sunac Service could deliver a very strong GFA expansion in 2020-23E to reach 412mn managed GFA. This is mainly because transiting from its heavy reliance on the projects delivered by parentco and its JV/associates, the future driver has become the third party bidding riding on its brand, network and incentive mechanism.

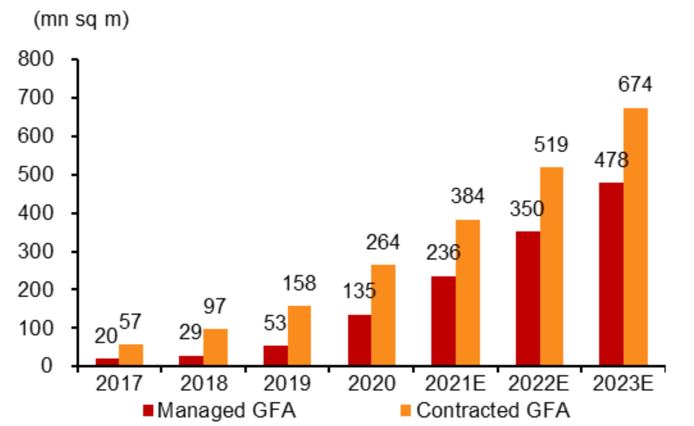
- **Brand:** Sunac is famous for its premium projects and service in Tier 1&2 cities. This can be seen from its higher-than-industry management fee at RMB3/sq m or above. We think this could help further gain market share especially in its dominate cities and regions such as (Yangtze River Delta, Chongqing, Tianjin and so on).

- **Incentive mechanism to boost third-party bidding team:** As the Company has put third-party bidding as the first priority, it has quickly expanded the team to a size of 210 staff in May 2021 from 100 in 2020. Besides the size, Sunac Services also reward 20% of first-year net profits in the newly-acquired projects to the team which is very competitive to the peers. Moreover, it has linked the bonus of parentco staff to how much they could help source third-party projects to the property management arm. Therefore, the incentive is designed in a way of team size, direct bonus and synergy with parentco which we think could help gain market share and quickly grow the area.

- **Network:** Benefiting from parentco's market leading position and M&A-friendly strategy, Sunac service could have a relatively easier access to a wide range of third party developers that may offer cooperation on the property management level.

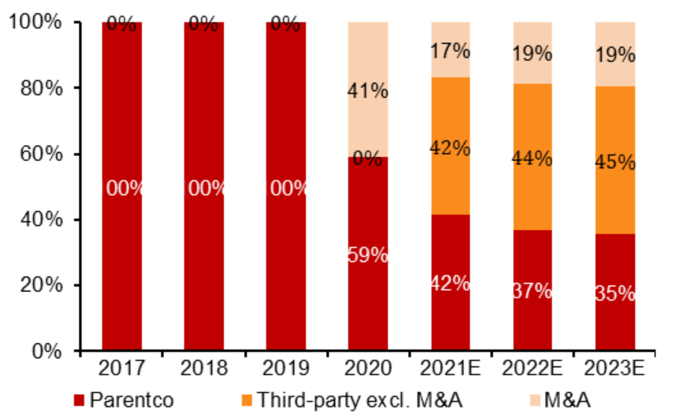
As a result, we expect 3rd-party bidding to contribute 42-45% of added GFA under management in 2020-23E at 36-50mn sq m. Together with a steady delivery of 45-48mn sq m per year from Sunac Group and 20-30mn sqm from M&A deals (such as Zhangtai deal in 2021), we estimate managed GFA to reach 478mn sq m by 2023E.

**Figure 8: Managed and contracted GFA (52% CAGR in 2020-23E)**




Source: Company data, CMBIS estimates

**Figure 9: newly-added Managed GFA by channels (3rd-party bidding will be the key driver)**




Source: Company data, CMBIS estimates

**Figure 10: We expect Sunac Services to further gain market share in its dominate regions given its premium service**

| City | Contracted GFA ('000 sq.m.) | Percentage | GFA under management ('000 sq.m.) | Percentage |
|---|---|---|---|---|
| Hangzhou | 23,517 | 8.9% | 17,198 | 12.7% |
| Chongqing | 20,879 | 7.9% | 15,381 | 11.4% |
| Tianjin | 11,000 | 4.2% | 9,054 | 6.7% |
| Qingdao | 10,017 | 3.8% | 2,887 | 2.1% |
| Taizhou | 8,201 | 3.1% | 6,356 | 4.7% |
| Jinan | 8,093 | 3.1% | 2,958 | 2.2% |
| Wuhan | 7,722 | 2.9% | 2,286 | 1.7% |
| Meishan | 7,327 | 2.8% | 2,960 | 2.2% |
| Chengdu | 6,932 | 2.6% | 4,061 | 3.0% |
| Wuxi | 6,690 | 2.5% | 5,176 | 3.8% |
| Kunming | 6,479 | 2.5% | 2,254 | 1.7% |
| Zhengzhou | 6,104 | 2.3% | 1,824 | 1.4% |
| Xuzhou | 6,024 | 2.3% | 4,024 | 3.0% |
| Harbin | 5,929 | 2.2% | 4,358 | 3.2% |
| Shaoxing | 4,865 | 1.8% | 3,265 | 2.4% |
| Ningbo | 4,643 | 1.8% | 1,814 | 1.3% |
| Xi'an | 4,003 | 1.5% | 2,730 | 2.0% |
| Nanchang | 3,972 | 1.5% | 1,834 | 1.4% |
| Hefei | 3,824 | 1.4% | 2,390 | 1.8% |
| Jiaxing | 3,664 | 1.4% | 2,526 | 1.9% |
| Shijiazhuang | 3,565 | 1.4% | 1,335 | 1.0% |
| Shanghai | 3,482 | 1.3% | 2,885 | 2.1% |
| Nanning | 3,341 | 1.3% | 1,617 | 1.2% |
| Yantai | 3,339 | 1.3% | 987 | 0.7% |
| Guiyang | 3,278 | 1.2% | 375 | 0.3% |
| Kaifeng | 3,198 | 1.2% | 2,275 | 1.7% |
| Beijing | 2,952 | 1.1% | 2,491 | 1.8% |
| Taiyuan | 2,942 | 1.1% | 1,091 | 0.8% |
| Shenyang | 2,724 | 1.0% | 1,898 | 1.4% |
| Wenzhou | 2,371 | 0.9% | 1,118 | 0.8% |
| Guangzhou | 2,304 | 0.9% | 1,388 | 1.0% |
| Jinhua | 2,105 | 0.8% | 492 | 0.4% |
| Yinchuan | 2,020 | 0.8% | 558 | 0.4% |
| Other cities | 66,254 | 25.2% | 21,255 | 15.8% |
| Total | 263,760 | 100.0% | 135,101 | 100.0% |

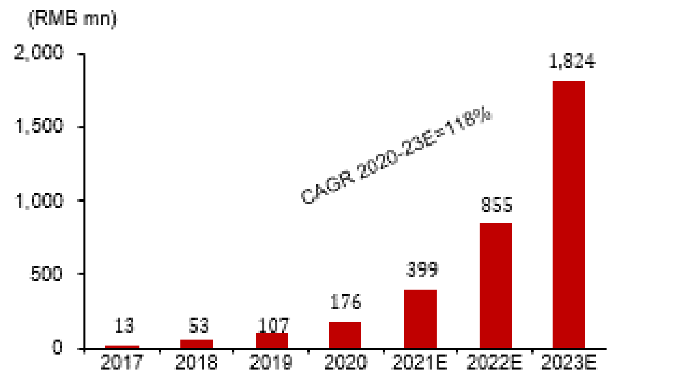
Source: CMBIS

## Huge room to improve for Community VAS at 118% 2020-23E CAGR

Sunac services have fallen behind the industry leaders on the Community VAS business which only contributed 4% of group revenue in 2020 results. The main reason behind is due to the low penetration rate and this will become the key focus looking forward.

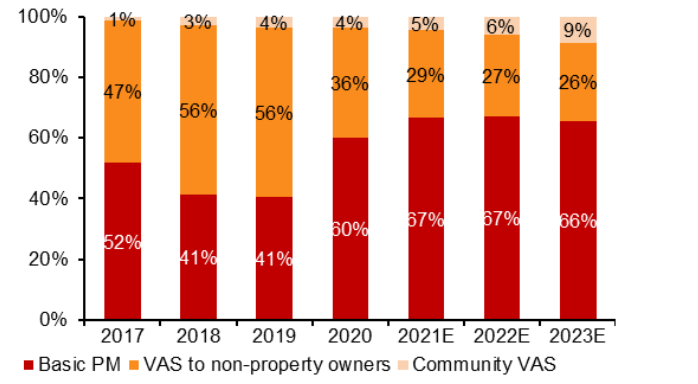
In terms of business segments, we think the traditional services such as property interior decoration and convenience services would continue to see explosive demand given its large GFA under management, hence may grow 125% CAGR in the next 3 years. Other high-margin businesses such as property brokerage services and space operation may see demand pick up from the COVID situation in 2020. All in all, we forecast Community VAS to grow 118% 2020-23E CAGR to RMB1.8bn and will contribute 9.5% of group revenue by 2023. Despite the narrowing gap with industry leaders, there is still huge room to improve further and we think Sunac Services will establish new initiatives to further monetize its large residence base.

**Figure 11: Revenue from Community VAS is expected to grow at 118% 2020-23E CAGR to RMB1.8bn**




Source: Company data, CMBIS estimates

**Figure 12: Its contribution to group revenue will increase to 21%, catching up with the industry**




Source: Company data, CMBIS estimates

## Margin uptrend to continue supporting bottom line further expansion

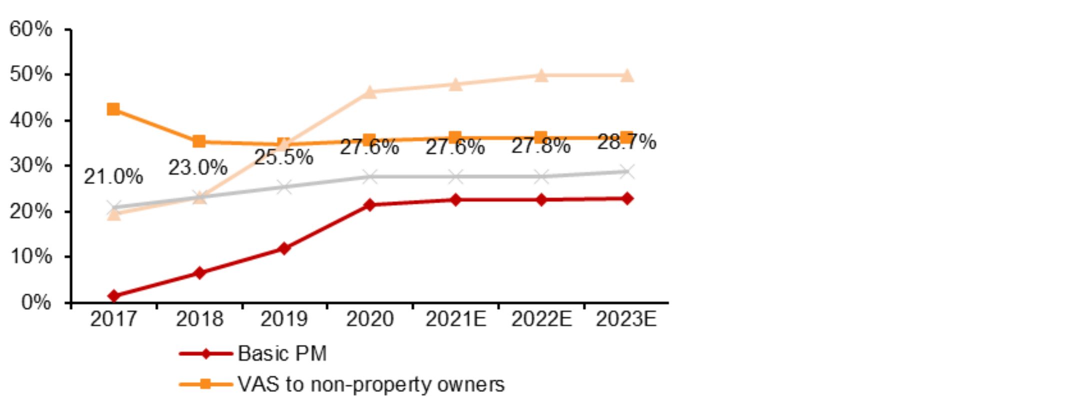
Besides a fast growth of its top line, we expect gross margin and net margin to expand to 29% and 15% by 2023E on economies of scale, cost saving, high-quality M&A, higher contribution from Community VAS.

For GP margin expansion, the reasons are 1) basic PM may gradually improve its GP margin at 21.6% in 2020 to 23% due to efficiency improvement, digitalization plan that may reduce 10% of staff costs in some projects and as well as high-margin M&A projects (such as Zhangtai PM that has 40% GP margin). 2) Higher contribution from Community VAS.

As for net margin, we think there is still some room for SG&A to go down from 11.3% in 2020 to 9.5% in 2023E.

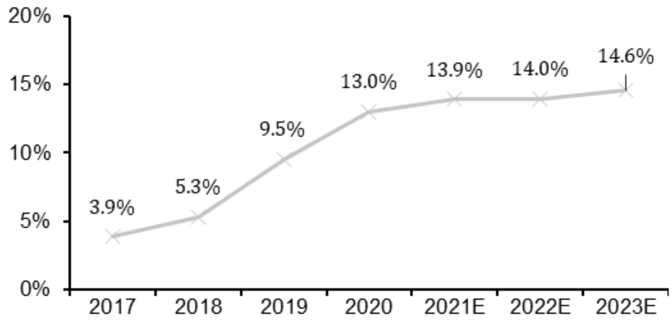
Therefore, together with both top line growth and margin expansion, we estimate net profits growth to increase 72% 2020-23E CAGR.

**Figure 13: We expect gross margin to improve to 29% in 2023E**




Source: Company data, CMBIS estimates

**Figure 14: We expect net margin to improve to 15% in 2023E**




Source: Company data, CMBIS estimates

# Key risks:

## Will its Parentco halt land acquisitions by regulators?

From the regulatory point of view, we think the chance of complete halting of land acquisitions is relatively small. This is mainly because:

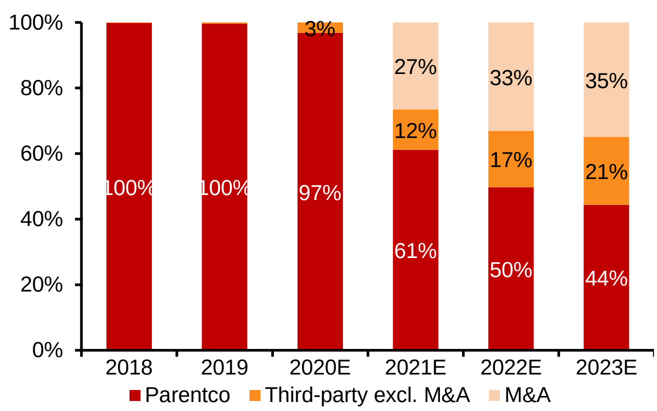
1) As of 2020, Sunac Group has met two of three red lines and has been put into yellow category. Despite some aggressive land acquisitions in 1H21, parentco still maintains the attributable land acquisitions/sales ratio below 40% in 5M21 which is still below PBOC's guidance.

2) We do see Sunac group continue to buy lands recently in Zhangjiakou.

However, there could be some slowdown in 2H21 given that Sunac Group already has a land reserve of 258mn sq m with 78% of them located in Tier 1-2 cities and sees no hurry in replenishment.

As for Sunac Services, we think the annual delivery from Sunac Group is still largely secured and the raise of RMB700bn sales target by its parentco also boosts the visibility in the near-to-mid term. Also, the key drivers of its GFA growth will shift to third-party bidding which could also diversify the risks.

**Figure 15: Newly added Managed GFA by channels (M&A will be the key driver)**




Source: Company data, CMBIS estimates

## Would third-party bidding face fierce competition especially in the Yangtze River Delta?

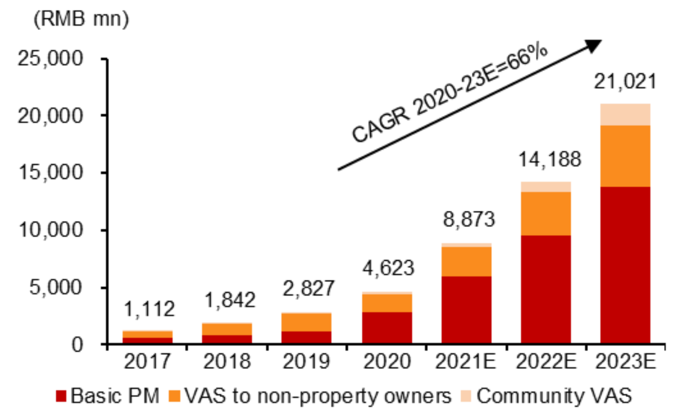
With more and more PM companies listed and trying to compete in the hot regions like Yangtze River Delta, we do see intensifying competitions among players. However, as we argue above, Sunac Services has the advantage of branding (especially its Yihaoyuan series), high market share especially in Hangzhou, Wuxi and the other key cities in the region and an integrated expansion team. With these right setting, the progress has been proven by the 4M21 data that shows 72% of newly-acquired GFA under management came from third-party bidding or 18mn sq m. This would help clear some doubts.

# Financial Analysis

## Revenue to grow at 61% CAGR in 2020-23E

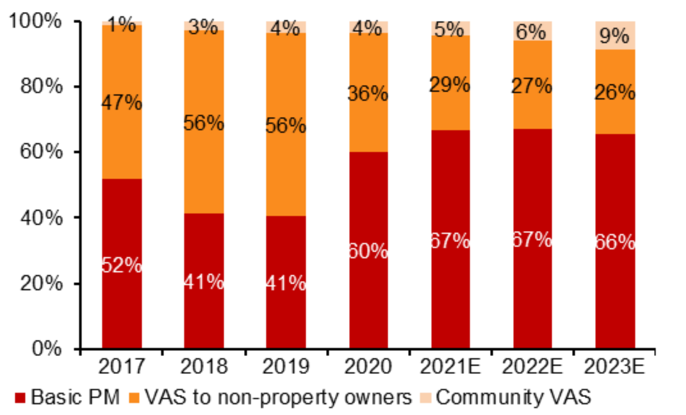
Thanks to robust GFA growth and booming VAS, revenue is set to grow at 38.7% CAGR from RMB4,623mn in 2020 to RMB21,021mn in 2023E. We expect basic PM services and community VAS (lifestyle services) to be major growth drivers, and expect segment revenue CAGR of 71% and 118%, respectively, in 2020-23E.

**Figure 16: Revenue to grow at 61% CAGR in 20-23E**




Source: Company data, CMBIS estimates

**Figure 17: Revenue mix trend**

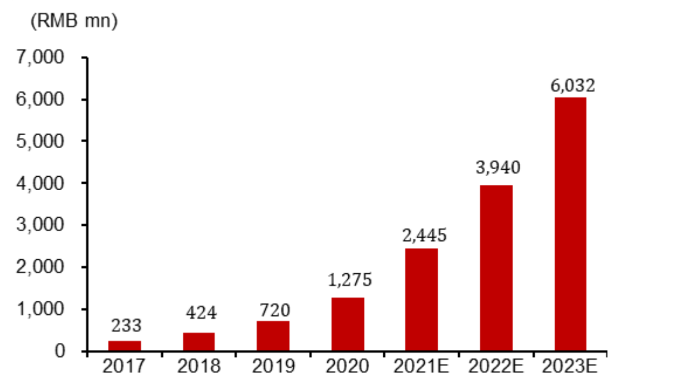



Source: Company data, CMBIS estimates

## Gross profit margin to increase steadily

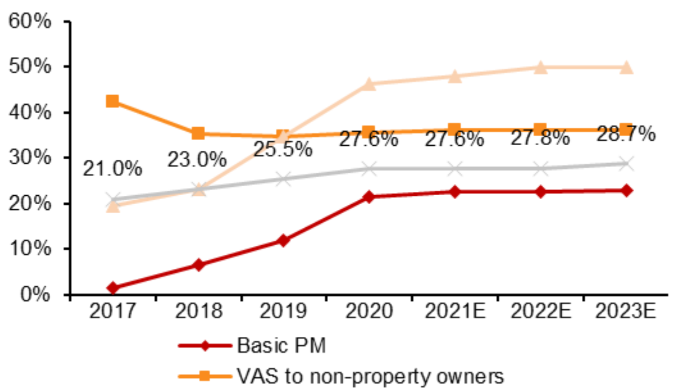
Gross profit was RMB720mn and RMB1,275mn in 2019 and 2020, while the corresponding gross margin was 25.5% and 27.6%, respectively. Going forward, we expect GPM to increase steadily to 27.6-28.7% in 2021E/22E/23E, respectively.

**Figure 18: Gross profit**




Source: Company data, CMBIS estimates

**Figure 19: Segment gross margin**




Source: Company data, CMBIS estimates

## SG&A expenses

Selling, General and Administrative (SG&A) expenses increased from RMB402mn in 2019 to RMB525mn in 2020. The rise in SG&A expenses was in line with the expansion of the Company's business scale. SG&A expenses to revenue ratio was at 11.4% at the end of 2020. We expect SG&A expenses/revenue to slightly decrease each year due to better economies of scale gained resulting from market and GFA expansion.

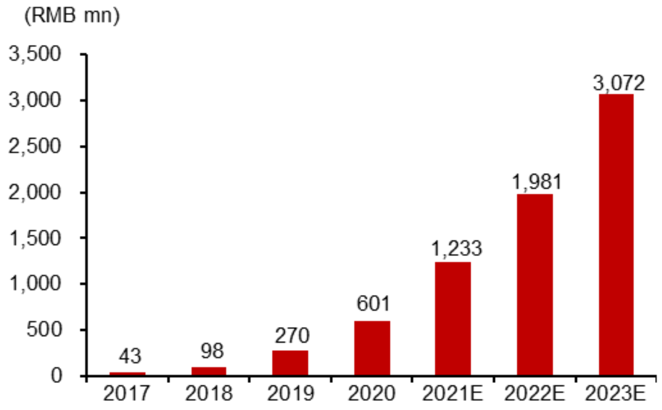
## Estimated net profit attributable to shareholders to grow at 72% CAGR in 2020-23E

Net attributable profit amounted to RMB270mn/601mn in 2019/2020, respectively. The corresponding net profit margin (attributed to shareholders) was 9.5%/13.0%, respectively. Going forward, we expect net profit to increase by 72% CAGR in 2020-23E, in line with revenue growth, to RMB3,072 mn in 2023E with net margin in an uptrend together with GP margin to 15% by 2023E.

## Strong operating cash flow to support potential M&As

Cash on hand was RMB9,368mn in 2020 and with annual operating cash flow to generate RMB2.9-5.9bn in 2021-2023E, we believe the Company's cash level is able to support potential M&A projects and further boost scale. We assume annual M&A spending at RMB1.0-2.0bn accordingly in 2021-2023E.

**Figure 20: Net profit attributable to shareholders**




Source: Company data, CMBIS estimates

# Price Target and Valuation

We value PM companies based on a scorecard system. There are six main categories as listed below:

1) **Parentco support (15% weights):** Companies with strong parentco support (on new GFA delivery) would have higher visibility on earnings.
2) **GFA growth (15%):** This is currently the key growth driver.
3) **VAS growth (20%):** It will be the future growth engine.
4) **Shopping mall contribution (20%):** High entrance barrier with high margin.
5) **Non-M&A expansion (10%):** Prefer companies with least expansion from M&A.
6) **Execution (20%):** It is based on the track record.

## Figure 21: Valuation scorecard

| Metrics | Overall score | Parentco support | GFA growth | VAS growth | Shopping mall contribution | Non-M&A expansion | Execution | Target 2022E P/E |
|---|---|---|---|---|---|---|---|---|
| Weights | | 15% | 15% | 20% | 20% | 10% | 20% | |
| CR MixC Lifestyle | 76 | 95 | 30 | 80 | 90 | 70 | 80 | 50x |
| Country Garden Services | 69 | 95 | 50 | 95 | 10 | 80 | 90 | 35x |
| Ever Sunshine | 66 | 80 | 80 | 80 | 20 | 60 | 80 | 35x |
| Powerlong Commercial | 60 | 70 | 40 | 30 | 90 | 70 | 60 | 30x |
| **Sunac Service** | **60** | **70** | **80** | **50** | **20** | **50** | **90** | **30x** |
| S-Enjoy | 58 | 70 | 70 | 70 | 20 | 70 | 60 | 25x |
| Greentown Services | 54 | 30 | 40 | 70 | 20 | 90 | 80 | 25x |
| Poly Services | 52 | 80 | 50 | 50 | 10 | 80 | 60 | 25x |
| Excellence CM | 51 | 50 | 50 | 60 | 30 | 80 | 50 | 20x |
| Central China New Life | 49 | 50 | 40 | 70 | 30 | 50 | 50 | 15x |
| Redsun Services | 42 | 40 | 60 | 30 | 30 | 50 | 50 | 15x |
| A-Living | 41 | 40 | 40 | 50 | 20 | 30 | 60 | 15x |
| Evergrande Services | 41 | 50 | 50 | 50 | 20 | 20 | 50 | 15x |
| Languang Justbon | 37 | 40 | 60 | 30 | 20 | 20 | 50 | 10x |

Source: CMBIS

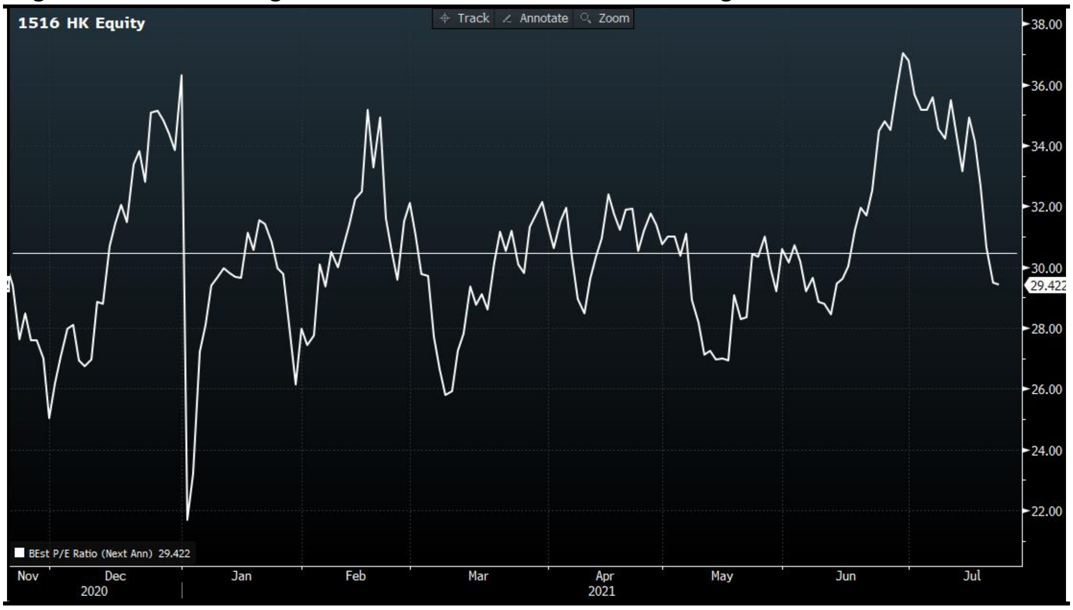
Based on the above scorecard, we target to assign 30x PE multiple on 2022E EPS to derive our target price of HK$29.80/share. Currently company is trading at 24x 2022E PE, in line with the industry average of 25x. However given its faster-than-industry GFA and earnings growth and market leading position, we expect Sunac Services to deserve a premium.

## Figure 22: Price target

| Price Target | |
|---|---|
| 2022E EPS | 0.83 |
| HKDRMB rate | 0.83 |
| Target PE multiple | 30 x |
| Price Target (HKD/share) | 29.80 |

Source: CMBIS

## Figure 23: 2YR-rolling forward PE below historical average




Source: CMBIS

**Figure 24: Comps table**

| Company | Ticker | CMBI rating | TP | Last price | Mkt Cap | P/E | | | Net profit growth (%) | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | (HK$) | (HK$) | (HK$ mn) | 20A | 21E | 22E | 21E | 22E |
| Country Garden Services | 6098 HK | BUY | 91.2 | 59.6 | 192,166 | 59.0 | 36.8 | 24.8 | 60.2 | 48.3 |
| CR MixC Lifestyle | 1209 HK | BUY | 56.0 | 40.0 | 91,300 | 75.5 | 52.6 | 37.8 | 43.4 | 39.3 |
| Evergrande Services | 6666 HK | BUY | 10.4 | 5.8 | 62,486 | 18.2 | 12.7 | 8.3 | 54.0 | 52.5 |
| Sunac Services | 1516 HK | BUY | 29.8 | 19.4 | 60,146 | 64.1 | 31.2 | 19.5 | 105.3 | 60.6 |
| A-Living | 3319 HK | HOLD | 34.2 | 33.0 | 46,789 | 20.9 | 15.3 | 11.7 | 36.2 | 31.1 |
| Greentown Services | 2869 HK | HOLD | 9.5 | 8.3 | 26,962 | 36.4 | 23.1 | 17.3 | 57.1 | 33.7 |
| Ever Sunshine | 1995 HK | BUY | 22.2 | 15.0 | 25,089 | 59.3 | 33.2 | 21.9 | 78.4 | 51.5 |
| Poly Services | 6049 HK | HOLD | 53.4 | 46.8 | 25,868 | 34.1 | 24.5 | 18.9 | 39.0 | 29.6 |
| S-Enjoy | 1755 HK | BUY | 34.6 | 17.6 | 15,383 | 28.5 | 18.3 | 12.7 | 55.9 | 43.6 |
| Powerlong Commercial | 9909 HK | BUY | 33.2 | 22.3 | 14,329 | 40.5 | 26.5 | 19.1 | 52.6 | 38.9 |
| Excellence CM | 6989 HK | BUY | 14.9 | 6.7 | 8,191 | 19.3 | 12.7 | 9.2 | 51.9 | 38.7 |
| Central China New Life | 9983 HK | BUY | 12.9 | 6.1 | 7,734 | 14.2 | 10.1 | 7.3 | 40.2 | 38.4 |
| Sino-Ocean Services | 6677 HK | BUY | 7.1 | 5.0 | 5,920 | 13.2 | 11.6 | 8.1 | 13.7 | 43.8 |
| New Hope Services | 3658 HK | BUY | 4.4 | 2.2 | 1,791 | 13.0 | 6.9 | 4.8 | 88.5 | 43.7 |
| Redsun Services | 1971 HK | BUY | 9.4 | 4.1 | 1,693 | 18.1 | 8.9 | 6.0 | 103.0 | 48.3 |
| COPH | 2669 HK | NR | NA | 6.9 | 22,778 | 31.9 | 24.8 | 19.3 | 28.3 | 29.0 |
| Times Neighborhood | 9928 HK | NR | NA | 5.2 | 5,125 | 19.1 | 10.5 | 7.1 | 80.8 | 48.5 |
| Aoyuan Healthy Life | 3662 HK | NR | NA | 4.9 | 3,522 | 12.6 | 8.1 | 5.9 | 57.0 | 35.9 |
| Shimao Services | 873 HK | NR | NA | 17.8 | 42,126 | 43.0 | 27.4 | 16.7 | 56.9 | 64.1 |
| KWG Living | 3913 HK | NR | NA | 7.0 | 14,024 | 32.5 | 17.0 | 10.6 | 91.8 | 60.5 |
| Jinke Smart Services | 9666 HK | NR | NA | 46.0 | 30,031 | 32.5 | 22.9 | 15.2 | 41.7 | 50.7 |
| | | | | | Average | 47.0 | 29.9 | 20.5 | 57.4 | 43.5 |

Source: CMBIS

## Risk factors

In our view, the key risk factors are:

1) Reliance on property delivery from Sunac Group, joint ventures or associates of Sunac Group or associates of the ultimate controlling shareholders of Sunac;
2) Potential failure to secure new or renew existing PM contracts on favourable terms;
3) Potential failure in future M&A;
4) Potential adverse impact arising from business concentration in Southwestern China and Eastern China due to any adverse development in governmental policies or macro business environment;
5) Potential difficulty in fee collection;
6) Potential fluctuations on labour and subcontracting costs; and
7) The COVID-19 pandemic.

# Financial Summary

**Income statement**

| YE 31 Dec (RMB mn) | FY19A | FY20A | FY21E | FY22E | FY23E |
|---|---|---|---|---|---|
| **Revenue** | **2,827** | **4,623** | **8,873** | **14,188** | **21,021** |
| Property management | 1,148 | 2,774 | 5,904 | 9,536 | 13,778 |
| VAS to non-property | 1,572 | 1,673 | 2,569 | 3,797 | 5,419 |
| Community VAS | 107 | 176 | 399 | 855 | 1,824 |
| **Gross Profit** | **720** | **1,275** | **2,445** | **3,940** | **6,032** |
| Other income | 37 | 57 | 26 | 26 | 26 |
| Selling expenses | (19) | (29) | (44) | (71) | (105) |
| Administrative expenses | (383) | (496) | (799) | (1,277) | (1,892) |
| Other gains/(losses) | | | - | - | - |
| Impairment | (3) | (15) | (18) | (28) | (42) |
| **Operating profit** | **357** | **803** | **1,611** | **2,590** | **4,019** |
| **Pre-tax Profit** | **346** | **822** | (2) | (2) | (2) |
| | | | **1,618** | **2,599** | **4,030** |
| Income tax | (76) | (197) | (372) | (598) | (927) |
| **PROFIT FOR THE YEAR** | **270** | **601** | **1,246** | **2,001** | **3,103** |

**Balance sheet**

| YE 31 Dec (RMB mn) | FY19A | FY20A | FY21E | FY22E | FY23E |
|---|---|---|---|---|---|
| **Non-current assets** | **153** | **1,949** | **2,497** | **3,964** | **5,926** |
| Property, plant and equipment | 29 | 59 | 69 | 79 | 89 |
| Others | 124 | 1,890 | 2,428 | 3,885 | 5,837 |
| **Current assets** | **2,118** | **11,008** | **13,250** | **16,646** | **21,365** |
| Inventories | 82 | 41 | 129 | 205 | 300 |
| Trade and other receivables | 946 | 1,388 | 2,268 | 3,597 | 5,305 |
| Cash and cash equivalents | 1,090 | 9,368 | 10,843 | 12,834 | 15,750 |
| Others | - | 211 | 10 | 10 | 10 |
| **Total assets** | **2,271** | **12,957** | **15,747** | **20,611** | **27,291** |
| **Current liabilities** | **1,751** | **2,950** | **5,506** | **8,968** | **13,460** |
| Trade and other payables | 1,087 | 1,773 | 3,405 | 5,534 | 8,244 |
| Others | 664 | 1,177 | 2,101 | 3,434 | 5,216 |
| **Non-current liabilities** | **22** | **272** | **217** | **218** | **219** |
| Deferred income tax | 7 | 81 | 30 | 30 | 30 |
| Others | 16 | 191 | 188 | 189 | 190 |
| **Total liabilities** | **1,773** | **3,222** | **5,723** | **9,187** | **13,679** |
| **Equity to shareholders** | **367** | **9,684** | **9,985** | **11,405** | **13,624** |
| Non-controlling interests | 131 | 51 | 39 | 19 | (12) |
| **Total Equity** | **498** | **9,735** | **10,024** | **11,424** | **13,612** |

**Cash flow summary**

| YE 31 Dec (RMB mn) | FY19A | FY20A | FY21E | FY22E | FY23E |
|---|---|---|---|---|---|
| **Profit before tax** | **346** | **822** | **1,618** | **2,599** | **4,030** |
| D&A | 35 | 82 | 65 | 72 | 79 |
| Change in working capital | 353 | 270 | 1,588 | 2,057 | 2,689 |
| Others | (27) | (151) | (390) | (606) | (924) |
| **Net cash from operating** | **707** | **1,024** | **2,881** | **4,122** | **5,873** |
| Capex | (8) | (13) | (16) | (40) | (40) |
| Capital Injection | - | - | (1) | - | - |
| Others | 611 | (1,358) | (999) | (1,476) | (1,976) |
| **Net cash from investing** | **603** | **(1,371)** | **(1,016)** | **(1,516)** | **(2,016)** |
| Equity raised | - | 7,592 | - | - | - |
| Change of debts | 304 | (713) | (615) | - | - |
| Others | (896) | 1,750 | 225 | (614) | (942) |
| **Net cash from financing** | **(592)** | **8,629** | **(390)** | **(614)** | **(942)** |
| Net change in cash | 718 | 8,282 | 1,475 | 1,991 | 2,915 |
| **Cash at the beginning of the year** | **372** | **1,090** | **9,368** | **10,843** | **12,834** |
| Exchange difference | (0) | (4) | - | - | - |
| **Cash at the end of the year** | **1,090** | **9,368** | **10,843** | **12,834** | **15,750** |

**Key ratios**

| YE 31 Dec | FY19A | FY20A | FY21E | FY22E | FY23E |
|---|---|---|---|---|---|
| **Sales mix (%)** | | | | | |
| Property management | 40.6 | 60.0 | 66.5 | 67.2 | 65.5 |
| VAS to non-property owners | 55.6 | 36.2 | 29.0 | 26.8 | 25.8 |
| Community VAS | 3.8 | 3.8 | 4.5 | 6.0 | 8.7 |
| **Total** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |
| **Profit & loss ratios (%)** | | | | | |
| Gross margin | 25.5 | 27.6 | 27.6 | 27.8 | 28.7 |
| Net margin | 9.5 | 13.0 | 13.9 | 14.0 | 14.6 |
| Effective tax rate | 22.0 | 23.9 | 23.0 | 23.0 | 23.0 |
| **Growth (%)** | | | | | |
| Revenue | 53.5 | 63.5 | 91.9 | 59.9 | 48.2 |
| Gross profit | 69.9 | 77.0 | 91.8 | 61.1 | 53.1 |
| Operating profit | 106.4 | 125.3 | 100.5 | 60.8 | 55.2 |
| Net profit | 174.5 | 122.6 | 105.3 | 60.6 | 55.1 |
| **Balance sheet ratios** | | | | | |
| Current ratio (x) | 1.2 | 3.7 | 2.4 | 1.9 | 1.6 |
| Receivable turnover days | 76 | 107 | 91 | 91 | 91 |
| **Returns (%)** | | | | | |
| ROE | 73.5 | 6.2 | 12.4 | 17.4 | 22.5 |
| ROA | 11.9 | 4.6 | 7.8 | 9.6 | 11.3 |
| **Per share** | | | | | |
| EPS (RMB) | 0.12 | 0.25 | 0.51 | 0.83 | 1.28 |
| DPS (RMB) | 0.00 | 0.00 | 0.15 | 0.25 | 0.38 |

Source: Company data, CMBIS estimates

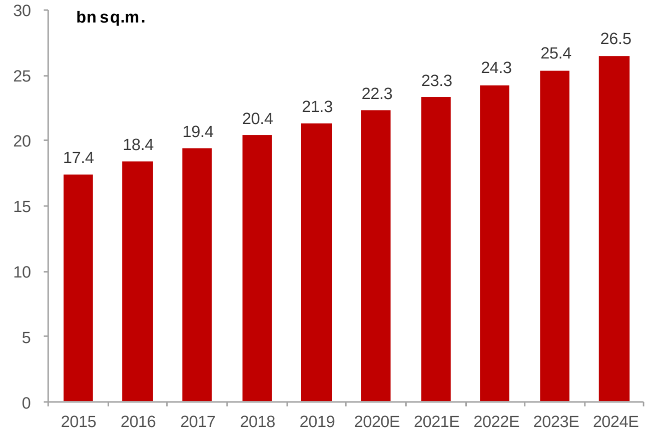
# Industry Overview

## Property management industry in China

The property management industry in China has been developing for nearly 40 years. As of the end of 2019, there were approximately 137,000 property management companies in China. The overall market size of the property management industry in China increased from 17.4bn sq m in 2015 to 21.3bn sq m in 2019, representing a CAGR of 5.2%. According to Savills and EH Consulting, the CAGR for the management area of the Chinese property industry from 2020 to 2024 will be 4.5%.

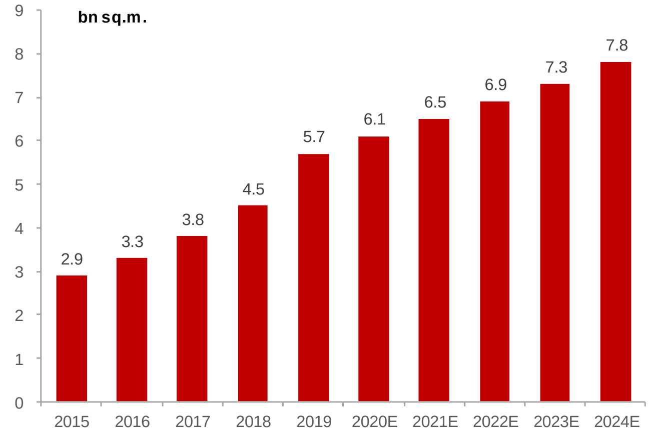
The Top 100 PM Companies in China have accelerated their growth in terms of managed GFA. According to Savills and EH Consulting, the GFA under management of the Top 100 grew steadily to 5.7bn sq m. in 2019, with a CAGR of 19.1% from 2015 to 2019. According to Savills and EH Consulting, the GFA under management of the Top 100 will increase at a CAGR of 6.2%.

**Figure 25: The overall market size of the property management industry in China, 2015-2024E**




Source: Savills and EH Consulting, CMBIS

**Figure 26: The GFA under management of the top 100 property management companies in China**



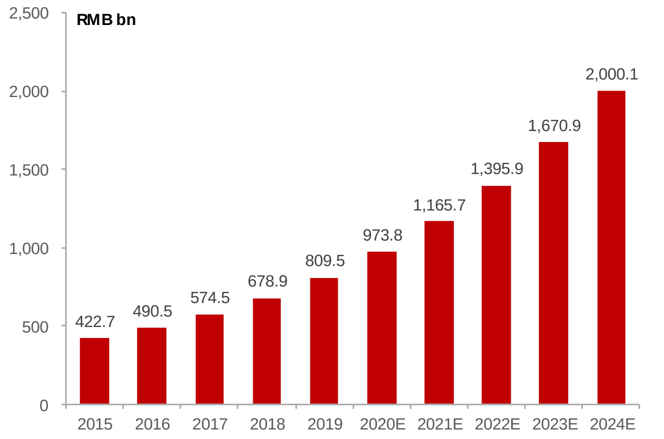

Source: Savills and EH Consulting, CMBIS

The continuous increase in the GFA, growing customer needs of diversified services and the expansion of diversified revenue channels have promoted greater growth in the operating revenue. In 2019, the total operating revenue of the PM industry of China increased 19.2% YoY to approximately RMB809.5bn, whereas the CAGR for the total operating income of the PM industry reached 17.6% between 2015 and 2019. According to Savills and EH Consulting, the CAGR for the total operating revenue of the PM industry will reach 19.7% from 2020 to 2024.

The operating revenue of the Top 100 Property Management Companies reached a record high of RMB 149.4bn in 2019, accounting for 18.5% of the entire industry, representing a YoY increase of 38.8% as compared to RMB 107.6bn in 2018. The CAGR for the operating revenue of the Top 100 Property Management Companies was 22.2% from 2015 to 2019, which was 4.6% higher than the CAGR for the overall operating revenue of the industry.

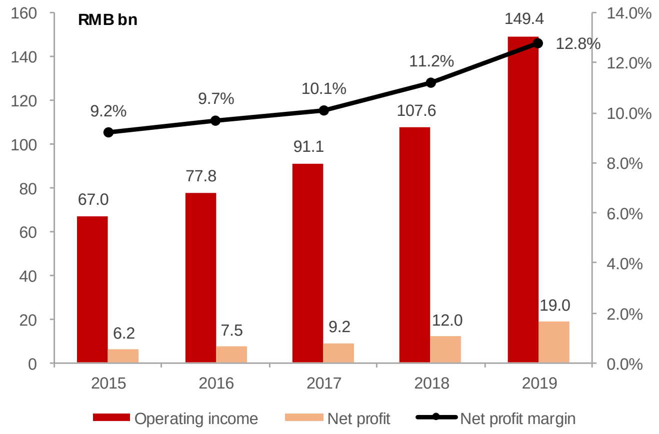
The Top 100 Property Management Companies have achieved steady growth in net profits while maintaining stable charging levels. According to Savills and EH Consulting Report, net profit of the Top 100 Property Management Companies amounted to RMB 19.0bn in 2019, representing a YoY increase of 58.2% from 2018. The CAGR for net profits of the Top 100 Property Management Companies was 32.6% from 2015 to 2019.

**Figure 27: The operating revenue of property management service market in China**




Source: Savills and EH Consulting, CMBIS

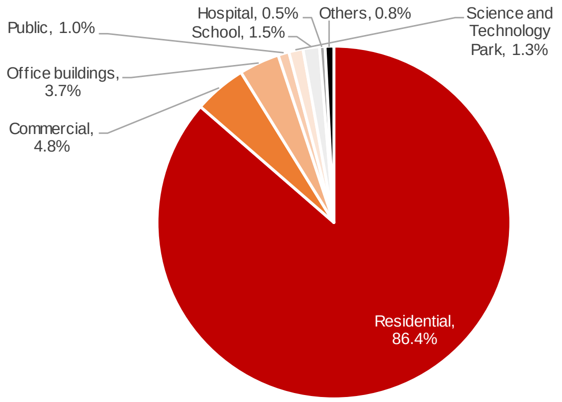
**Figure 28: Operating revenue, net profit and net profit margin of the top 100 property management companies from 2015 to 2019**




Source: Savills and EH Consulting, CMBIS

At present, the principal property management services in China are provided to residential and non-residential properties, of which the residential properties remain the main focus. In 2019, the area of residential properties under management of the Top 100 Property Management Companies amounted to 5.0bn sq m, accounting for 86.4% of the total area under management of the Top 100 Property Management Companies.

**Figure 29: The proportion of property types under management of the top 100 property management companies in 2019**

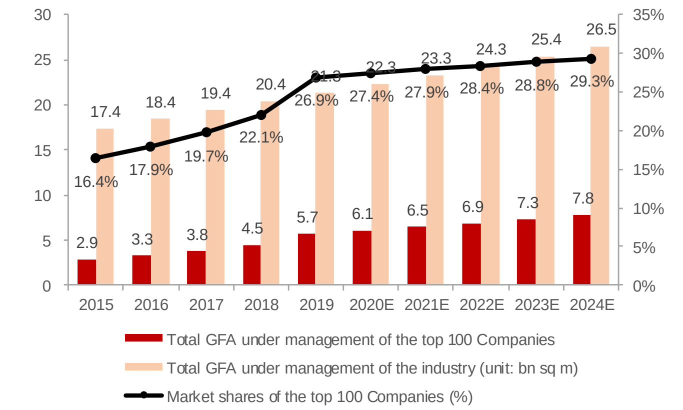



Source: Savills and EH Consulting, CMBIS

## Competitive landscape

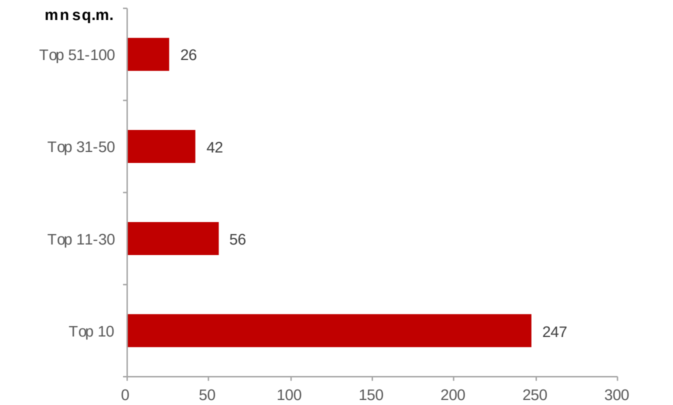
The PM industry in China is highly competitive. The Top 100 companies rely on strong capital and resource advantages to capture a market share of near 26.9% in terms of GFA under management. Growing property companies make use of competitive advantages to differentiate themselves from large players, developing diversified VAS while improving basic PM services, in order to gain market share among intense competition.

**Figure 30: Increasing market concentration**




Source: Savills and EH Consulting, CMBIS

**Figure 31: Competitive landscape of property management industry in China**




Source: Savills and EH Consulting, CMBIS

## Key industry drivers

**Introduction of the Relevant Supporting Policies**

Laws and regulations are the fundamental supporting pillar of the industry, and a good policy environment creates an important foundation for the industry's healthy development.

On 29 Oct 2020, the NDRC and 14 other ministries jointly issued the Work Programme on The Promotional Fees for The Recent Expansion of Domestic Demand, which provides external protection for the diversification of the property industry and is conducive to promoting the construction of intelligent communities and community life services for property management companies.

On 5 Jan 2021, the MOHURD issued Notice on Strengthening and Improving the Management of Residential Property, which clearly improves the pricing mechanism of property services, emphasizes the market-oriented pricing tone of residential property management, and establishes a dynamic adjustment mechanism based on the implementation of government-directed prices.

**The Significant growth in population, urbanization rate and per capita disposable income**

According to the NBS, the total population of China was 1.4bn at the end of 2019, representing a net increase of 4.7 million as compared to 2018. At the end of 2019, the urbanization rate of China has reached 60.6%, representing a CAGR of 2.4% from 2015 to 2019. The per capita disposable income of urban residents of China increased from RMB31,195 in 2015 to RMB42,359 in 2019, representing a CAGR of 7.9% from 2015 to 2019. The significant growth in the urbanization rate and per capita disposable income have become the major driving factors of the development of the PM industry.

**New Opportunities under the Epidemic**

During the COVID-19 epidemic, PM companies improved customer satisfaction by providing quality services and meeting customer needs. PM companies have received government financial support for the development of mobile applications, internet platforms and smart communities. In addition, driven by the demand for epidemic prevention, old residential communities will seek and entrust PM companies to provide necessary services.

## Entry barriers

According to Savills and EH Consulting, entry barriers of the PM industry are as follows:

**Figure 32: Operating revenue of PM service market in China**

| Entry barriers | Reason |
|---|---|
| **Market demand for professional services** | The demand for PM services varies by client and property type. New players may be at disadvantage as they typically lack understanding and experience in providing PM services to different clients. |
| **Demand for professional talents** | The development of new technologies have led to a substantial increase in the demand for professional talents. |
| **Standardization of operations and management** | PM companies need to standardize service and operations to better control costs and ensure service quality, which could present a challenge to new players. |
| **Specialized brands** | It is challenging for new players without established brands to gain market share in the PM industry. |
| **Capital requirement** | Capital is required to improve management and operations efficiency, which can be an obstacle for new players. |

Source: Savills and EH Consulting, CMBIS

## Financial Formula

Operating profit=Gross profit + Other income – Other net losses - Selling and distribution expenses – Admin expenses

Operating margin = Operating profit/Revenue

Pre-tax margin = Pre-tax profit/Revenue

Effective tax rate = Profit tax/Pre-tax profit

Net debt/total equity ratio = Total borrowings including loans from related parties, interest bearing bank and other borrowings and lease liabilities less cash and cash equivalents and restricted cash divided by total equity

ROA = Profit for the period divided by the average balance of total assets as of the beginning and end of the period and multiplied by 100%

ROE = Profit for the period divided by the average balance of total equity as of the beginning and end of the period and multiplied by 100%

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| | |
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