

# Country Garden Holdings Co Ltd 02007 ★★★ 10 Aug 2023 09:16, UTC

<b>Last Price</b> 1.04 HKD 10 Aug 2023	<b>Fair Value Estimate</b> 1.20 HKD 10 Aug 2023 09:11, UTC	<b>Price/FVE</b> 0.87	<b>Market Cap</b> 30.68 HKD Bil 9 Aug 2023	<b>Economic Moat™</b> None	<b>Equity Style Box</b> Large Value	<b>Uncertainty</b> Very High	<b>Capital Allocation</b> Standard	<b>ESG Risk Rating Assessment<sup>1</sup></b> 5 Jul 2023 05:00, UTC
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## Jeff Zhang, CFA

Equity Analyst  
Morningstar

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### Important Disclosure

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The primary analyst covering this company does not own its stock.

Reporting Currency: CNY | Trading Currency: HKD  
Currency amounts expressed with "\$" are in U.S. dollars (USD) unless otherwise denoted.

The ESG Risk Rating Assessment is a representation of Sustainalytics' ESG Risk Rating.

## Country Garden: Fair Value Trimmed on Increasing Likelihood of Default and Subdued Profitability

**Analyst Note** Jeff Zhang, CFA, Equity Analyst, 10 Aug 2023

We have cut our fair value estimate for Country Garden Holdings to HKD 1.20 from HKD 2.80 given the higher weighted average cost of capital on potential defaults and more compressed margins. CGH missed a USD 22.5 million interest payment on two offshore bonds on Aug. 7, fueling the market's concerns that it may eventually default after the 30-day grace period as evidenced by the plunge in its bond and share prices. While management cited liquidity pressure due to a deterioration in sales and the refinancing environment, they underscored an ongoing effort to arrange coupon payments. That said, we remain cautious about the likelihood of CGH's default, given its weak sales and elevated overseas funding costs. As such, we raised our assumptions for CGH's cost of debt and cost of equity by 550 basis points and 200 basis points, respectively, leading to WACC rising to 12.8% from 9.5%, according to our prior estimate. In addition, following CGH's profit warnings, we think pressured housing prices in lower-tier cities have further eaten into CGH's profitability and lowered our 2023 gross margin forecast to 6.1% from 9.9%.

We think CGH's missing offshore interest payment may not be an isolated event given its worsened liquidity status currently compared with the end of 2022. For the first half of 2023, the firm's attributable sales value has tumbled by over 30% year on year, adding to the pressure on operating cashflow. Also, CGH's overseas financing on the debt and equity front has been muted since 2023, implying that the firm has likely used its cash denominated in foreign currencies. Aside from coupon payments due in August, we estimate that CGH needs to fulfill at least USD 137 million of bond interest payments through the rest of 2023. Without additional credit support from Chinese regulators and sizable financial institutions, CGH should continue to see an elevated risk of


### Financial Summary and Key Statistics

	Actual		Forecast	
	2021	2022	2023	2024
Revenue (HKD Mil)	523,064	430,371	437,117	394,788
Revenue Growth %	13.0	-17.7	1.6	-9.7
Operating Income (Mil)	60,640	10,983	2,389	6,711
Operating Margin %	11.6	2.6	0.5	1.7
Adjusted EBITDA (Mil)	68,816	4,055	2,066	6,644
Adjusted EBITDA Margin %	13.2	0.9	0.5	1.7
Earnings Per Share (Diluted) (HKD)	1.18	-0.26	0.04	0.11
Adjusted Earnings Per Share (Diluted) (HKD)	1.18	-0.26	0.04	0.11
Adjusted EPS Growth %	-24.6	-121.7	-114.4	204.5
Price/Earnings	5.9	-10.3	27.8	10.1
Price/Book	0.8	0.3	0.1	0.1
EV/EBITDA	4.8	62.3	84.2	26.2
Free Cash Flow Yield %	—	—	—	—

Source: Morningstar Valuation Model. Data as of 10 Aug 2023.

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Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Equity Style Box	Uncertainty	Capital Allocation	ESG Risk Rating Assessment¹
1.04 HKD 10 Aug 2023	1.20 HKD 10 Aug 2023 09:11, UTC	0.87	30.68 HKD Bil 9 Aug 2023	None	Large Value	Very High	Standard	 5 Jul 2023 05:00, UTC

Sector	Industry
 Real Estate	Real Estate - Development

## Business Description

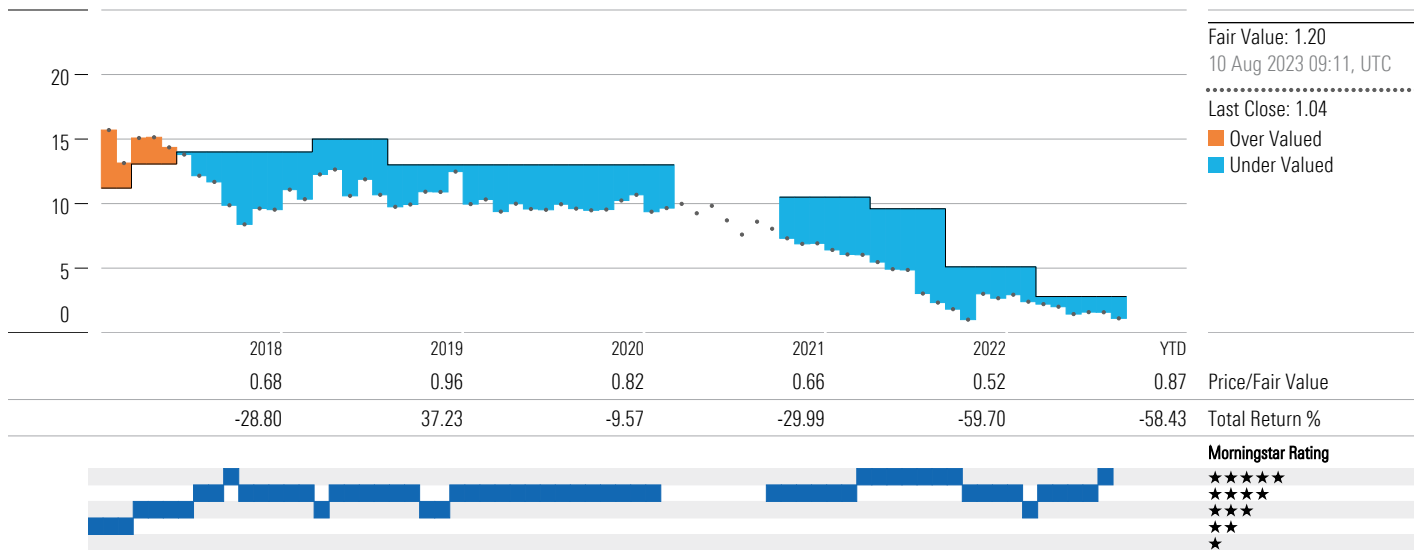
Listed in 2007, Country Garden Holdings has been one of the largest China real estate developers in contracted sales with a focus on Tier 3 and lower-tier cities. Property development has represented most of CGH's revenue and earnings, and the firm has tapped into new businesses such as robotics construction and venture capital investment. Following the retirement of founder Yang Guoqiang, Yang Huiyan (daughter of Yang Guoqiang) holds around a 61% stake of the company, while Ping An Life Insurance retains 7.7% equity ownership after the private placement in 2015.

defaulting on its overseas debt, in our view.

Another negative for CGH is that management expected net losses for the first half of 2023, mainly due to a gross margin decline, inventory impairment increase, and foreign-exchange losses. CGH remains heavily exposed to projects in lower-tier cities, which we do not believe will see a material sales improvement due to depressed homebuying sentiment. While the firm has not massively acquired land parcels in the first half, we forecast that most of its existing projects should post lower margins given faltering selling prices and the tempered pace of turnover. The recent credit event may further dent homebuyers' confidence in CGH's ability to promptly deliver presold projects, in our view. Hence, we revise our long-term margin assumptions and foresee CGH delivering an 8.0% gross margin in 2027 versus 15.0% previously. ■■■

# Country Garden Holdings Co Ltd 02007 ★★★ 10 Aug 2023 09:16, UTC

## Price vs. Fair Value



## Competitors

	Country Garden...oldings Co Ltd 02007	China Overseas...Investment Ltd 00688	China Resources Land Ltd 01109	China Jinmao H...ings Group Ltd 00817
	<p><b>Fair Value</b> 1.20 Uncertainty: Very High</p> <p><b>Last Close</b> 1.04</p>	<p><b>Fair Value</b> 31.00 Uncertainty: High</p> <p><b>Last Close</b> 17.62</p>	<p><b>Fair Value</b> 43.00 Uncertainty: High</p> <p><b>Last Close</b> 34.25</p>	<p><b>Fair Value</b> 1.90 Uncertainty: High</p> <p><b>Last Close</b> 1.18</p>
Economic Moat	None	None	None	None
Currency	HKD	HKD	HKD	HKD
Fair Value	1.20 10 Aug 2023 09:11, UTC	31.00 26 Apr 2023 14:09, UTC	43.00 6 Mar 2023 10:38, UTC	1.90 31 May 2023 03:21, UTC
1-Star Price	2.10	48.05	66.65	2.95
5-Star Price	0.60	18.60	25.80	1.14
Assessment	Significantly Undervalued 9 Aug 2023	Significantly Undervalued 9 Aug 2023	Under Valued 9 Aug 2023	Under Valued 9 Aug 2023
Moringstar Rating	★★★ 10 Aug 2023 09:16, UTC	★★★★★ 9 Aug 2023 16:33, UTC	★★★★★ 9 Aug 2023 16:33, UTC	★★★★★ 9 Aug 2023 16:33, UTC
Analyst	Jeff Zhang, Equity Analyst	Jeff Zhang, Equity Analyst	Jeff Zhang, Equity Analyst	Jeff Zhang, Equity Analyst
Capital Allocation	Standard	Standard	Standard	Standard
Price/Fair Value	0.87	0.57	0.80	0.62
Price/Sales	0.06	0.99	1.09	0.17
Price/Book	0.14	0.50	0.92	0.31
Price/Earnings	—	7.62	8.01	6.99
Dividend Yield	8.62%	4.54%	4.68%	9.32%
Market Cap	30.68 Bil	192.85 Bil	244.23 Bil	15.71 Bil
52-Week Range	1.00—3.48	14.40—23.75	23.95—40.50	1.01—2.07
Investment Style	Large Value	Large Value	Large Value	Mid Value

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## Morningstar Valuation Model Summary

### Financials as of 10 Aug 2023

Fiscal Year, ends 31 Dec	Actual			Forecast				
	2020	2021	2022	2023	2024	2025	2026	2027
Revenue (CNY Mil)	462,856	523,064	430,371	437,117	394,788	379,916	389,704	403,554
Operating Income (CNY Mil)	70,585	60,640	10,983	2,389	6,711	8,738	10,132	11,300
EBITDA (CNY Mil)	80,334	68,816	4,055	2,066	6,644	8,921	10,562	11,973
Adjusted EBITDA (CNY Mil)	80,334	68,816	4,055	2,066	6,644	8,921	10,562	11,973
Net Income (CNY Mil)	35,022	26,797	-6,052	911	2,890	4,010	4,572	4,843
Adjusted Net Income (CNY Mil)	35,022	26,797	-6,052	911	2,890	4,010	4,572	4,843
Free Cash Flow To The Firm (CNY Mil)	-94,964	-32,723	28,180	129,398	67,784	14,031	-12,377	-29,865
Weighted Average Diluted Shares Outstanding (Bil)	22	23	24	25	26	26	27	27
Earnings Per Share (Diluted) (CNY)	1.57	1.18	-0.26	0.04	0.11	0.15	0.17	0.18
Adjusted Earnings Per Share (Diluted) (CNY)	1.57	1.18	-0.26	0.04	0.11	0.15	0.17	0.18
Dividends Per Share (CNY)	0.45	0.31	0.00	0.01	0.03	0.04	0.04	0.04

### Margins & Returns as of 10 Aug 2023

	Actual				Forecast					5 Year Avg
	3 Year Avg	2020	2021	2022	2023	2024	2025	2026	2027	
Operating Margin %	9.9	15.3	11.6	2.6	0.5	1.7	2.3	2.6	2.8	1.2
EBITDA Margin %	24.2	17.4	13.2	0.9	0.5	1.7	2.4	2.7	3.0	-65.6
Adjusted EBITDA Margin %	—	17.4	13.2	0.9	0.5	1.7	2.4	2.7	3.0	2.0
Net Margin %	3.8	7.6	5.1	-1.4	0.2	0.7	1.1	1.2	1.2	0.9
Adjusted Net Margin %	3.8	7.6	5.1	-1.4	0.2	0.7	1.1	1.2	1.2	0.9
Free Cash Flow To The Firm Margin %	-6.7	-20.5	-6.3	6.6	29.6	17.2	3.7	-3.2	-7.4	8.0

### Growth & Ratios as of 10 Aug 2023

	Actual				Forecast					2027 5 Year CAGR
	3 Year CAGR	2020	2021	2022	2023	2024	2025	2026	2027	
Revenue Growth %	-4.0	-4.7	13.0	-17.7	1.6	-9.7	-3.8	2.6	3.6	-1.3
Operating Income Growth %	—	-22.2	-14.1	-81.9	-78.2	180.9	30.2	16.0	11.5	0.6
EBITDA Growth %	-42.5	-19.1	-14.3	-94.1	-49.1	221.6	34.3	18.4	13.4	47.7
Adjusted EBITDA Growth %	-65.6	-19.1	-14.3	-94.1	-49.1	221.6	34.3	18.4	13.4	24.2
Earnings Per Share Growth %	—	-12.6	-24.6	-121.7	-114.4	204.5	36.2	12.0	4.2	—
Adjusted Earnings Per Share Growth %	—	-12.6	-24.6	-121.7	-114.4	204.5	36.2	12.0	4.2	—

### Valuation as of 10 Aug 2023

	Actual			Forecast				
	2020	2021	2022	2023	2024	2025	2026	2027
Price/Earnings	6.8	5.9	-10.3	27.8	10.1	7.4	6.5	6.2
Price/Sales	0.5	0.3	0.2	0.1	0.1	0.1	0.1	0.1
Price/Book	1.4	0.8	0.3	0.1	0.1	0.1	0.1	0.1
Price/Cash Flow	—	—	—	—	—	—	—	—
EV/EBITDA	5.0	4.8	62.3	84.2	26.2	19.5	16.5	14.5
EV/EBIT	5.7	5.5	23.0	72.8	25.9	19.9	17.2	15.4
Dividend Yield %	4.2	4.5	—	0.9	2.7	3.6	3.6	3.6
Dividend Payout %	29.0	26.4	0.0	25.0	25.0	25.0	25.0	25.0
Free Cash Flow Yield %	—	—	—	—	—	—	—	—

### Operating Performance / Profitability as of 10 Aug 2023

Fiscal Year, ends 31 Dec	Actual			Forecast				
	2020	2021	2022	2023	2024	2025	2026	2027
ROA %	1.7	1.4	-0.4	0.1	0.2	0.3	0.3	0.3
ROE %	13.6	8.9	-2.0	0.3	0.9	1.2	1.3	1.4
ROIC %	16.0	12.2	1.8	-2.4	-1.2	0.1	1.1	1.9

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## Financial Leverage (Reporting Currency)

Fiscal Year, ends 31 Dec	Actual			Forecast				
	2020	2021	2022	2023	2024	2025	2026	2027
Debt/Capital %	58.2	66.5	78.6	90.2	88.6	87.1	85.3	83.5
Assets/Equity	7.8	6.5	5.6	5.5	5.1	4.9	4.8	4.7
Net Debt/EBITDA	1.9	2.3	32.6	15.8	-0.7	0.0	3.2	7.5
Total Debt/EBITDA	4.1	4.6	67.0	128.3	39.3	28.8	23.9	20.8
EBITDA/ Net Interest Expense	-11.0	-19.7	-1.1	-0.7	-2.1	-2.3	-2.8	-3.8

## Forecast Revisions as of 10 Aug 2023

Prior data as of 25 May 2023	2023		2024		2025	
	Current	Prior	Current	Prior	Current	Prior
Fair Value Estimate Change (Trading Currency)	1.20	2.82	—	—	—	—
Revenue (HKD Mil)	437,117	438,395	394,788	387,346	379,916	372,514
Operating Income (HKD Mil)	2,389	19,449	6,711	21,691	8,738	27,194
EBITDA (HKD Mil)	2,066	28,923	6,644	32,051	8,921	38,500
Net Income (HKD Mil)	911	12,191	2,890	13,169	4,010	16,185
Earnings Per Share (Diluted) (HKD)	0.04	0.49	0.11	0.50	0.15	0.60
Adjusted Earnings Per Share (Diluted) (HKD)	0.04	0.49	0.11	0.50	0.15	0.60
Dividends Per Share (HKD)	0.01	0.12	0.03	0.13	0.04	0.15

## Key Valuation Drivers as of 10 Aug 2023

Cost of Equity %	13.5
Pre-Tax Cost of Debt %	14.5
Weighted Average Cost of Capital %	12.8
Long-Run Tax Rate %	25.0
Stage II EBI Growth Rate %	3.0
Stage II Investment Rate %	20.0
Perpetuity Year	10

Additional estimates and scenarios available for download at <https://pitchbook.com/>.

## Discounted Cash Flow Valuation as of 10 Aug 2023

	HKD Mil
Present Value Stage I	153,796
Present Value Stage II	5,685
Present Value Stage III	9,481
<b>Total Firm Value</b>	<b>168,961</b>
Cash and Equivalents	128,281
Debt	271,718
Other Adjustments	0
<b>Equity Value</b>	<b>25,524</b>
Projected Diluted Shares	25
<b>Fair Value per Share (HKD)</b>	<b>1.20</b>

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## Income Statement (HKD)

Fiscal Year, ends 31 Dec	Actual			Forecast				
	2020	2021	2022	2023	2024	2025	2026	2027
<b>Revenue (Mil)</b>	<b>462,856</b>	<b>523,064</b>	<b>430,371</b>	<b>437,117</b>	<b>394,788</b>	<b>379,916</b>	<b>389,704</b>	<b>403,554</b>
Cost of Goods Sold (Mil)	361,951	430,282	397,488	410,356	367,153	351,422	359,307	371,269
<b>Gross Profit (Mil)</b>	<b>100,905</b>	<b>92,782</b>	<b>32,883</b>	<b>26,761</b>	<b>27,635</b>	<b>28,494</b>	<b>30,397</b>	<b>32,284</b>
Selling, General, Administrative & Other Expenses (Mil)	13,752	15,316	11,298	11,802	10,264	9,498	9,743	10,089
Advertising & Marketing Expenses (Mil)	13,919	13,518	8,438	9,073	7,896	7,598	7,794	8,071
Research & Development (Mil)	2,649	3,308	2,164	3,497	2,764	2,659	2,728	2,825
Depreciation & Amortization (if reported separately) (Mil)	0	0	0	0	0	0	0	0
<b>Adjusted Operating Income (Mil)</b>	<b>70,585</b>	<b>60,640</b>	<b>10,983</b>	<b>2,389</b>	<b>6,711</b>	<b>8,738</b>	<b>10,132</b>	<b>11,300</b>
Financial Non-Cash (Gains)/Losses (Mil)	-4,822	-3,175	7,829	3,117	3,067	3,016	2,964	2,911
Irregular Cash (Gains)/Losses (Mil)	-2,816	-1,637	1,365	0	0	0	0	0
<b>Operating Income (Mil)</b>	<b>78,223</b>	<b>65,452</b>	<b>1,789</b>	<b>-728</b>	<b>3,644</b>	<b>5,722</b>	<b>7,168</b>	<b>8,389</b>
Net Interest Expense (Mil)	-7,306	-3,497	-3,572	-2,898	-3,236	-3,825	-3,718	-3,142
Income Tax Expense (Mil)	31,411	27,967	8,323	868	2,752	3,819	4,355	4,612
After-Tax Items (Mil)	0	0	0	0	0	0	0	0
(Minority Interest) (Mil)	-19,096	-14,185	-3,090	-391	-1,238	-1,718	-1,960	-2,075
<b>Net Income (Mil)</b>	<b>35,022</b>	<b>26,797</b>	<b>-6,052</b>	<b>911</b>	<b>2,890</b>	<b>4,010</b>	<b>4,572</b>	<b>4,843</b>
<b>Adjusted Net Income (Mil)</b>	<b>35,022</b>	<b>26,797</b>	<b>-6,052</b>	<b>911</b>	<b>2,890</b>	<b>4,010</b>	<b>4,572</b>	<b>4,843</b>
Weighted Average Diluted Shares Outstanding (Bil)	22	23	24	25	26	26	27	27
<b>Diluted Earnings Per Share</b>	<b>1.57</b>	<b>1.18</b>	<b>-0.26</b>	<b>0.04</b>	<b>0.11</b>	<b>0.15</b>	<b>0.17</b>	<b>0.18</b>
<b>Diluted Adjusted Earnings Per Share</b>	<b>1.57</b>	<b>1.18</b>	<b>-0.26</b>	<b>0.04</b>	<b>0.11</b>	<b>0.15</b>	<b>0.17</b>	<b>0.18</b>
Dividends Per Common Share (HKD)	0.45	0.31	0.00	0.01	0.03	0.04	0.04	0.04
<b>EBITDA (Mil)</b>	<b>80,334</b>	<b>68,816</b>	<b>4,055</b>	<b>2,066</b>	<b>6,644</b>	<b>8,921</b>	<b>10,562</b>	<b>11,973</b>
<b>Adjusted EBITDA (Mil)</b>	<b>80,334</b>	<b>68,816</b>	<b>4,055</b>	<b>2,066</b>	<b>6,644</b>	<b>8,921</b>	<b>10,562</b>	<b>11,973</b>

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## Key Cash Flow Items (HKD)

Fiscal Year, ends 31 Dec	Actual			Forecast as of 10 Aug				
	2020	2021	2022	2023	2024	2025	2026	2027
Cash from Working Capital (Mil)	-126,110	-72,574	37,114	129,023	65,613	11,089	-15,938	-34,021
(Capital Expenditures) (Mil)	-4,013	-3,908	-4,104	-4,186	-4,270	-4,355	-4,442	-4,531
Depreciation (Mil)	1,908	3,154	2,125	2,560	2,723	2,877	3,025	3,167
Amortization (Mil)	203	210	141	234	277	322	368	417
<b>Net New (Investment), Organic (Mil)</b>	<b>-128,012</b>	<b>-73,118</b>	<b>35,276</b>	<b>127,631</b>	<b>64,343</b>	<b>9,933</b>	<b>-16,987</b>	<b>-34,968</b>
(Purchases)/Sales of Companies & Assets (Mil)	-1,904	-14,134	-475	-523	-575	-632	-696	-765
<b>Net New (Investment), Total (Mil)</b>	<b>-129,916</b>	<b>-87,252</b>	<b>34,801</b>	<b>127,108</b>	<b>63,768</b>	<b>9,300</b>	<b>-17,682</b>	<b>-35,733</b>
Other Non-Cash Items, From Cash Flows (Mil)	4,553	29,811	-2,543	0	0	0	0	0
<b>Free Cash Flow to the Firm (Mil)</b>	<b>-94,964</b>	<b>-32,723</b>	<b>28,180</b>	<b>129,398</b>	<b>67,784</b>	<b>14,031</b>	<b>-12,377</b>	<b>-29,865</b>

## Balance Sheet (HKD)

Fiscal Year, ends 31 Dec	Actual			Forecast				
	2020	2021	2022	2023	2024	2025	2026	2027
<b>Assets</b>								
Cash and Equivalents (Bil)	167	147	128	232	266	257	219	160
Inventory (Bil)	1,095	1,064	942	805	727	713	732	773
Accounts Receivable (Bil)	411	407	380	407	362	349	358	370
Net Property, Plant and Equipment (Bil)	26	27	26	27	29	30	32	33
Goodwill (Bil)	0	0	0	0	0	0	0	0
Other Intangibles (Bil)	1	1	2	2	2	2	3	3
Other Operating Assets (Bil)	236	190	171	179	188	198	209	221
Non-Operating Assets (Bil)	78	112	96	76	76	76	76	76
<b>Total Assets (Bil)</b>	<b>2,016</b>	<b>1,948</b>	<b>1,744</b>	<b>1,729</b>	<b>1,650</b>	<b>1,626</b>	<b>1,629</b>	<b>1,636</b>
<b>Liabilities</b>								
Accounts Payable (Bil)	660	551	437	467	412	395	404	417
Debt (Bil)	327	319	272	265	261	257	253	250
Other Operating Liabilities (Bil)	771	779	726	682	654	642	631	618
Non-Operating Liabilities (Bil)	0	0	0	0	0	0	0	0
<b>Total Liabilities (Bil)</b>	<b>1,759</b>	<b>1,648</b>	<b>1,435</b>	<b>1,414</b>	<b>1,327</b>	<b>1,294</b>	<b>1,287</b>	<b>1,285</b>
<b>Equity</b>								
Shareholders' Equity (Bil)	175	199	204	204	206	209	213	217
Minority Interest (Bil)	82	102	106	111	117	123	129	135
<b>Total Equity (Bil)</b>	<b>257</b>	<b>301</b>	<b>310</b>	<b>316</b>	<b>323</b>	<b>332</b>	<b>342</b>	<b>352</b>

# Country Garden Holdings Co Ltd 02007 ★★★ 10 Aug 2023 09:16, UTC

<b>Last Price</b> 1.04 HKD 10 Aug 2023	<b>Fair Value Estimate</b> 1.20 HKD 10 Aug 2023 09:11, UTC	<b>Price/FVE</b> 0.87	<b>Market Cap</b> 30.68 HKD Bil 9 Aug 2023	<b>Economic Moat™</b> None	<b>Equity Style Box</b> Large Value	<b>Uncertainty</b> Very High	<b>Capital Allocation</b> Standard	<b>ESG Risk Rating Assessment<sup>1</sup></b> 5 Jul 2023 05:00, UTC
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## ESG Risk Rating Breakdown

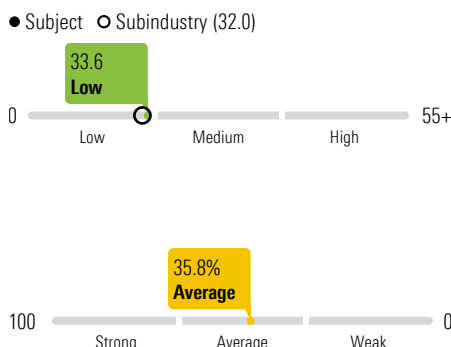
### Exposure

Company Exposure <sup>1</sup>	33.6	
- Manageable Risk	32.6	
<b>Unmanageable Risk<sup>2</sup></b>	<b>1.0</b>	

### Management

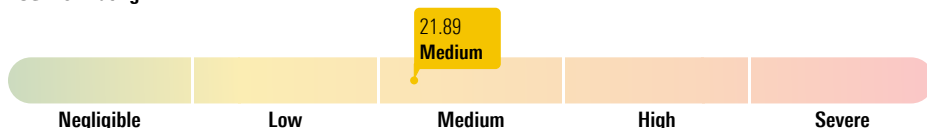
Manageable Risk	32.6	
- Managed Risk <sup>3</sup>	11.7	
<b>Management Gap<sup>4</sup></b>	<b>20.9</b>	

**Overall Unmanaged Risk 21.9**



- ▶ Exposure represents a company's vulnerability to ESG risks driven by their business model
- ▶ Exposure is assessed at the Subindustry level and then specified at the company level
- ▶ Scoring ranges from 0-55+ with categories of low, medium, and high-risk exposure
- ▶ Management measures a company's ability to manage ESG risks through its commitments and actions
- ▶ Management assesses a company's efficiency on ESG programs, practices, and policies
- ▶ Management score ranges from 0-100% showing how much manageable risk a company is managing

## ESG Risk Rating



ESG Risk Ratings measure the degree to which a company's value is impacted by environmental, social, and governance risks, by evaluating the company's ability to manage the ESG risks it faces.

1. A company's Exposure to material ESG issues 2. Unmanageable Risk refers to risks that are inherent to a particular business model that cannot be managed by programs or initiatives 3. Managed Risk = Manageable Risk multiplied by a Management score of 35.8% 4. Management Gap assesses risks that are not managed, but are considered manageable 5. ESG Risk Rating Assessment = Overall Unmanaged Risk = Management Gap plus Unmanageable Risk

## ESG Risk Rating Assessment<sup>5</sup>



ESG Risk Rating is of Jul 05, 2023. Highest Controversy Level is as of Aug 08, 2023. Sustainalytics Subindustry: Real Estate Development. Sustainalytics provides Morningstar with company ESG ratings and metrics on a monthly basis and as such, the ratings in Morningstar may not necessarily reflect current Sustainalytics' scores for the company. For the most up to date rating and more information, please visit: [sustainalytics.com/esg-ratings/](https://sustainalytics.com/esg-ratings/).

## Peer Analysis 05 Jul 2023

Peers are selected from the company's Sustainalytics-defined Subindustry and are displayed based on the closest market cap values

Company Name	Exposure		Management		ESG Risk Rating	
<b>Country Garden Holdings Co Ltd</b>	33.6   Low	0 —●— 55+	35.8   Average	100 —●— 0	21.9   Medium	0 —●— 40+
China Resources Land Ltd	32.8   Low	0 —●— 55+	34.7   Average	100 —●— 0	21.8   Medium	0 —●— 40+
China Jinmao Holdings Group Ltd	33.2   Low	0 —●— 55+	33.1   Average	100 —●— 0	22.5   Medium	0 —●— 40+
Shimao Group Holdings Ltd	32.4   Low	0 —●— 55+	30.7   Average	100 —●— 0	22.7   Medium	0 —●— 40+
China Overseas Land & Investment Ltd	30.0   Low	0 —●— 55+	47.5   Average	100 —●— 0	16.1   Low	0 —●— 40+



# Research Methodology for Valuing Companies

## Overview

At the heart of our valuation system is a detailed projection of a company's future cash flows, resulting from our analysts' research. Analysts create custom industry and company assumptions to feed income statement, balance sheet, and capital investment assumptions into our globally standardized, proprietary discounted cash flow, or DCF, modeling templates. We use scenario analysis, in-depth competitive advantage analysis, and a variety of other analytical tools to augment this process. Moreover, we think analyzing valuation through discounted cash flows presents a better lens for viewing cyclical companies, high-growth firms, businesses with finite lives (e.g., mines), or companies expected to generate negative earnings over the next few years. That said, we don't dismiss multiples altogether but rather use them as supporting cross-checks for our DCF-based fair value estimates. We also acknowledge that DCF models offer their own challenges (including a potential proliferation of estimated inputs and the possibility that the method may miss short-term market-price movements), but we believe these negatives are mitigated by deep analysis and our long-term approach.

Morningstar's equity research group ("we," "our") believes that a company's intrinsic worth results from the future cash flows it can generate. The Morningstar Rating for stocks identifies stocks trading at a discount or premium to their intrinsic worth—or fair value estimate, in Morningstar terminology. Five-star stocks sell for the biggest risk adjusted discount to their fair values, whereas 1-star stocks trade at premiums to their intrinsic worth.

Four key components drive the Morningstar rating: (1) our assessment of the firm's economic moat, (2) our estimate of the stock's fair value, (3) our uncertainty around that fair value estimate and (4) the current market price. This process ultimately culminates in our single-point star rating.

## 1. Economic Moat

The concept of an economic moat plays a vital role not only in our qualitative assessment of a firm's long-term investment potential, but also in the actual calculation of our fair value estimates. An economic moat is a structural feature that allows a firm to sustain excess profits over a long period of time. We define economic profits as re-

turns on invested capital (or ROIC) over and above our estimate of a firm's cost of capital, or weighted average cost of capital (or WACC). Without a moat, profits are more susceptible to competition. We have identified five sources of economic moats: intangible assets, switching costs, network effect, cost advantage, and efficient scale.

Companies with a narrow moat are those we believe are more likely than not to achieve normalized excess returns for at least the next 10 years. Wide-moat companies are those in which we have very high confidence that excess returns will remain for 10 years, with excess returns more likely than not to remain for at least 20 years. The longer a firm generates economic profits, the higher its intrinsic value. We believe low-quality, no-moat companies will see their normalized returns gravitate toward the firm's cost of capital more quickly than companies with moats.

When considering a company's moat, we also assess whether there is a substantial threat of value destruction, stemming from risks related to ESG, industry disruption, financial health, or other idiosyncratic issues. In this context, a risk is considered potentially value destructive if its occurrence would eliminate a firm's economic profit on a cumulative or mid-cycle basis. If we deem the probability of occurrence sufficiently high, we would not characterize the company as possessing an economic moat.

## 2. Estimated Fair Value

Combining our analysts' financial forecasts with the firm's economic moat helps us assess how long returns on invested capital are likely to exceed the firm's cost of capital. Returns of firms with a wide economic moat rating are assumed to fade to the perpetuity period over a longer period of time than the returns of narrow-moat firms, and both will fade slower than no-moat firms, increasing our estimate of their intrinsic value.

Our model is divided into three distinct stages:

### Stage I: Explicit Forecast

In this stage, which can last five to 10 years, analysts make full financial statement forecasts, including items such as revenue, profit margins, tax rates, changes in working capital accounts, and capital spending. Based on these projections, we calculate earnings before interest, after taxes (EBI) and the net new investment (NNI) to de-

rive our annual free cash flow forecast.

### Stage II: Fade

The second stage of our model is the period it will take the company's return on new invested capital—the return on capital of the next dollar invested ("RONIC")—to decline (or rise) to its cost of capital. During the Stage II period, we use a formula to approximate cash flows in lieu of explicitly modeling the income statement, balance sheet, and cash flow statement as we do in Stage I. The length of the second stage depends on the strength of the company's economic moat. We forecast this period to last anywhere from one year (for companies with no economic moat) to 10–15 years or more (for wide-moat companies). During this period, cash flows are forecast using four assumptions: an average growth rate for EBI over the period, a normalized investment rate, average return on new invested capital (RONIC), and the number of years until perpetuity, when excess returns cease. The investment rate and return on new invested capital decline until a perpetuity value is calculated. In the case of firms that do not earn their cost of capital, we assume marginal ROICs rise to the firm's cost of capital (usually attributable to less reinvestment), and we may truncate the second stage.

### Stage III: Perpetuity

Once a company's marginal ROIC hits its cost of capital, we calculate a continuing value, using a standard perpetuity formula. At perpetuity, we assume that any growth or decline or investment in the business neither creates nor destroys value and that any new investment provides a return in line with estimated WACC.

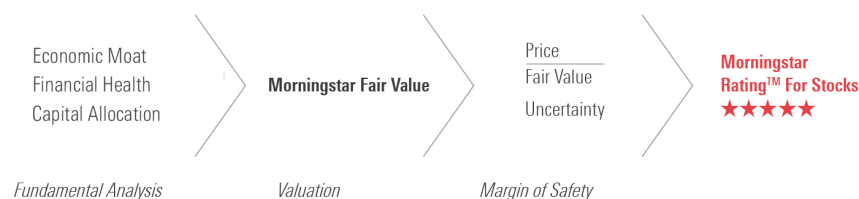
Because a dollar earned today is worth more than a dollar earned tomorrow, we discount our projections of cash flows in stages I, II, and III to arrive at a total present value of expected future cash flows. Because we are modeling free cash flow to the firm—representing cash available to provide a return to all capital providers—we discount future cash flows using the WACC, which is a weighted average of the costs of equity, debt, and preferred stock (and any other funding sources), using expected future proportionate long-term, market-value weights.

## 3. Uncertainty Around That Fair Value Estimate

Morningstar's Uncertainty Rating is designed to capture the range of potential outcomes for a company's intrinsic value. This rating is used to assign the margin of safety required before investing, which in turn explicitly drives our stock star rating system. The Uncertainty Rating is aimed at identifying the confidence we should have in assigning a fair value estimate for a given stock.

Our Uncertainty Rating is meant to take into account anything that can increase the potential dispersion of future outcomes for the intrinsic value of a company, and any-

## Morningstar Equity Research Star Rating Methodology



# Research Methodology for Valuing Companies

thing that can affect our ability to accurately predict these outcomes. The rating begins with a suggested rating produced by a quantitative process based on the trailing 12-month standard deviation of daily stock returns. An analyst overlay is then applied, with analysts using the suggested rating, historical rating data, and their own knowledge of the company to inform them as they make the final Uncertainty Rating decision. Ultimately, the rating decision rests with the analyst. Analysts take into account many characteristics when making their final decision, including cyclical factors, operational and financial factors such as leverage, company-specific events, ESG risks, and anything else that might increase the potential dispersion of future outcomes and our ability to estimate those outcomes.

Our recommended margin of safety—the discount to fair value demanded before we’d recommend buying or selling the stock—widens as our uncertainty of the estimated value of the equity increases. The more uncertain we are about the potential dispersion of outcomes, the greater the discount we require relative to our estimate of the value of the firm before we would recommend the purchase of the shares. In addition, the Uncertainty Rating provides guidance in portfolio construction based on risk tolerance.

Our Uncertainty Ratings are: Low, Medium, High, Very High, and Extreme.

Margin of Safety		
Qualitative Analysis	★★★★★ Rating	★ Rating
Uncertainty Ratings	★★★★★ Rating	★ Rating
Low	20% Discount	25% Premium
Medium	30% Discount	35% Premium
High	40% Discount	55% Premium
Very High	50% Discount	75% Premium
Extreme	75% Discount	300% Premium

Our uncertainty rating is based on the interquartile range, or the middle 50% of potential outcomes, covering the 25th percentile–75th percentile. This means that when a stock hits 5 stars, we expect there is a 75% chance that the intrinsic value of that stock lies above the current market price. Similarly, when a stock hits 1 star, we expect there is a 75% chance that the intrinsic value of that stock lies below the current market price.

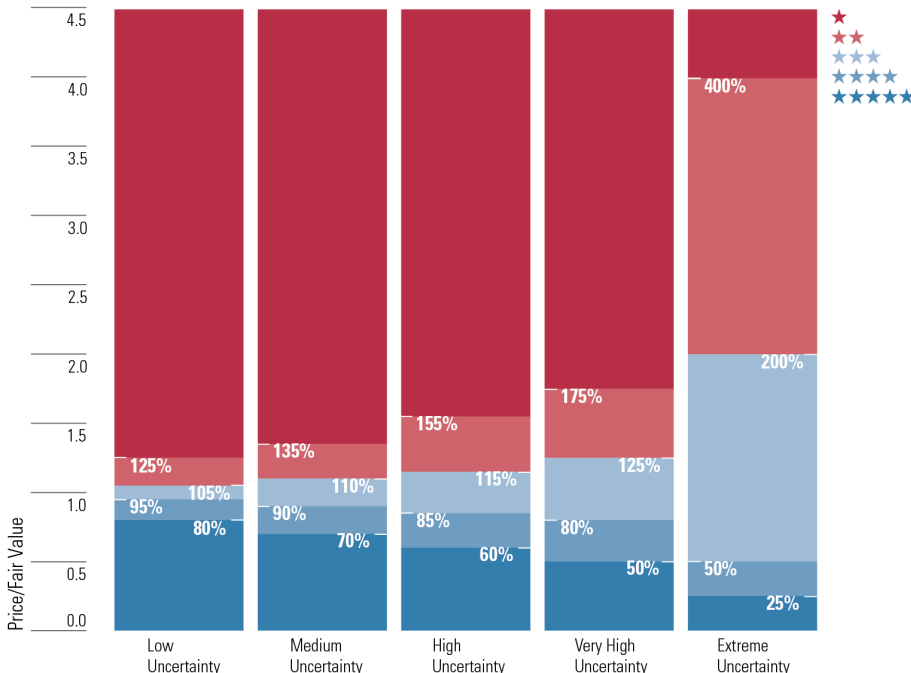
## 4. Market Price

The market prices used in this analysis and noted in the report come from exchange on which the stock is listed which we believe is a reliable source.

For more details about our methodology, please go to <https://shareholders.morningstar.com>

## Morningstar Star Rating for Stocks

Morningstar Equity Research Star Rating Methodology



Once we determine the fair value estimate of a stock, we compare it with the stock’s current market price on a daily basis, and the star rating is automatically re-calculated at the market close on every day the market on which the stock is listed is open. Our analysts keep close tabs on the companies they follow, and, based on thorough and ongoing analysis, raise or lower their fair value estimates as warranted.

Please note, there is no predefined distribution of stars. That is, the percentage of stocks that earn 5 stars can fluctuate daily, so the star ratings, in the aggregate, can serve as a gauge of the broader market’s valuation. When there are many 5-star stocks, the stock market as a whole is more undervalued, in our opinion, than when very few companies garner our highest rating.

We expect that if our base-case assumptions are true the market price will converge on our fair value estimate over time generally within three years (although it is impossible to predict the exact time frame in which market prices may adjust).

Our star ratings are guideposts to a broad audience and individuals must consider their own specific investment goals, risk tolerance, tax situation, time horizon, income needs, and complete investment portfolio, among other factors.

The Morningstar Star Ratings for stocks are defined below:

★★★★★ We believe appreciation beyond a fair risk ad-

justed return is highly likely over a multiyear time frame. Scenario analysis developed by our analysts indicates that the current market price represents an excessively pessimistic outlook, limiting downside risk and maximizing upside potential.

★★★★ We believe appreciation beyond a fair risk-adjusted return is likely.

★★★ Indicates our belief that investors are likely to receive a fair risk-adjusted return (approximately cost of equity).

★★ We believe investors are likely to receive a less than fair risk-adjusted return.

★ Indicates a high probability of undesirable risk-adjusted returns from the current market price over a multiyear time frame, based on our analysis. Scenario analysis by our analysts indicates that the market is pricing in an excessively optimistic outlook, limiting upside potential and leaving the investor exposed to Capital loss.

## Other Definitions

**Last Price:** Price of the stock as of the close of the market of the last trading day before date of the report.

**Capital Allocation Rating:** Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management’s capital allocation, with particular emphasis on the firm’s balance sheet, investments, and shareholder distributions. Analysts consider compan-

# Research Methodology for Valuing Companies

ies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exemplary", "Standard", or "Poor". Analysts judge Capital Allocation from an equity holder's perspective. Ratings are determined on a forward looking and absolute basis. The Standard rating is most common as most managers will exhibit neither exceptionally strong nor poor capital allocation.

Capital Allocation (or Stewardship) analysis published prior to Dec. 9, 2020, was determined using a different process. Beyond investment strategy, financial leverage, and dividend and share buyback policies, analysts also considered execution, compensation, related party transactions, and accounting practices in the rating.

**Capital Allocation Rating:** Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management's capital allocation, with particular emphasis on the firm's balance sheet, investments, and shareholder distributions. Analysts consider companies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exemplary", "Standard", or "Poor". Analysts judge Capital Allocation from an equity holder's perspective. Ratings are determined on a forward looking and absolute basis. The Standard rating is most common as most managers will exhibit neither exceptionally strong nor poor capital allocation.

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**Sustainalytics ESG Risk Rating Assessment:** The ESG Risk Rating Assessment is provided by Sustainalytics; a Morningstar company.

Sustainalytics' ESG Risk Ratings measure the degree to which company's economic value at risk is driven by environment, social and governance (ESG) factors.

Sustainalytics analyzes over 1,300 data points to assess a company's exposure to and management of ESG risks. In other words, ESG Risk Ratings measures a company's unmanaged ESG Risks represented as a quantitative score. Unmanaged Risk is measured on an open-ended scale

starting at zero (no risk) with lower scores representing less unmanaged risk and, for 95% of cases, the unmanaged ESG Risk score is below 50.

Based on their quantitative scores, companies are grouped into one of five Risk Categories (negligible, low, medium, high, severe). These risk categories are absolute, meaning that a 'high risk' assessment reflects a comparable degree of unmanaged ESG risk across all subindustries covered.

The ESG Risk Rating Assessment is a visual representation of Sustainalytics ESG Risk Categories on a 1 to 5 scale. Companies with Negligible Risk = 5 Globes, Low Risk = 4, Medium Risk = 3 Globes, High Risk = 2 Globes, Severe Risk = 1 Globe. For more information, please visit [sustainalytics.com/esg-ratings/](https://sustainalytics.com/esg-ratings/)

Ratings should not be used as the sole basis in evaluating a company or security. Ratings involve unknown risks and uncertainties which may cause our expectations not to occur or to differ significantly from what was expected and should not be considered an offer or solicitation to buy or sell a security.

## Risk Warning

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