

Appalling interim results expected

Hong Kong Properties

Midland (1200 HK, HK\$3.38)

SELL (unchanged)

Target price: HK\$1.83 (-46%)

Midland is due to announce its FY12/06 interim results on Fri, Sep 15.

Only a handful of brokers follow this stock closely. We are one of the very few.

Downward trend for the first 8 months of 2006. While we forecast a net loss of HK\$105m for 2006, we reckon the loss at interim will exceed HK\$60m as 2H06 property transaction value would be somewhat boosted by new primary flat launches. Total HK property transaction by value in 1H06 were down by 42.3% YoY by value. The trend remained pretty much the same for July (down 40.6%). Only starting from Aug 06, we saw some revival in primary flat unit sales as developers need to speed up sales to book profit for the year (up 155% YoY for Aug but still down 52.6% YoY for year to Aug compared with a decline of 61.8% YoY for year to July). Despite this, secondary property flat unit sales remained weak with a YoY decline of 13.6% for Aug 06 and 29.5% for year to Aug.

Bad debt provisions will provide a nasty surprise. We expect bad debt provisions would be a swing factor in 2006 again (HK\$75m in 1H06 and HK\$43m in 2H06) as many primary flat speculators forfeit their flats amid a slow market in 1H06.

Long-term investors continue to trim holdings. OppenheimerFunds reduced another 4.45m shares at HK\$3.477 or 0.6% to only 4.84% on Sep 8, the third time it trimmed its holding in the past three weeks. Third Avenue, Legg Mason, AIG and Fidelity, all lowered stakes in the past two to three months.

Shock wave to the market. We expect the interim results will shock the market and the stock will finally start to tumble.

Maintain target price and SELL. We maintain our SELL call and target price of HK\$1.83, based on 1.5x P/B.

Midland is only a bull market play. Many investors buy Midland for its operating leverage and proxy to the Hong Kong property market. But this will only work during a bull market. The flip side of the coin is that the negative operating leverage effect will also be much more powerful than the market anticipates during a weak and slow market. In addition, the time Midland takes to recover will also be longer than the market expects due to its fixed overhead cost structure (at least a two-year rental lease for all new shops).

Table 1: Financial summary

Year to Dec	Net profit HK\$m	EPS HK\$	EPS Δ %	P/E x	P/B x	EV/EBITDA x	Yield %	ROE %	ROCE %	N. Gearing %
04A	330.7	0.470	164.5	7.2	2.93	4.5	2.1	48.1	52.1	Cash
05A	213.6	0.292	(37.8)	11.6	2.48	7.4	3.0	23.6	21.8	Cash
06A	(105.0)	(0.143)	-	-	2.77	(69.6)	-	(11.1)	(10.5)	Cash
07F	83.0	0.113	-	29.9	2.62	12.9	0.5	9.0	8.1	Cash
08F	171.8	0.234	107.1	14.5	2.37	7.7	1.0	17.2	16.3	Cash

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