

Goldbond Group



Stellar FY03/08A results

STRONG BUY
(unchanged)

Better-than-expected results. Goldbond Group reported its net earnings for FY03/08A soared 270.0% YoY to HK\$180.2m or HK\$0.071/share, on an 811.0% surge in turnover to HK\$226.6m. The group's headline results were ahead of our previous projection for FY03/08A of HK\$140.1m.

China Banking/Finance

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Stunning growth in core earnings. Stripping off the earnings contribution from the discontinued property business of HK\$25.3m (including a gain of HK\$19.9m from the disposal of 25.0% interest in Nanjing City Plaza property development project and HK\$5.2m from the disposal of Golden Plaza in Hong Kong), the gain from the change in fair value of derivative component of convertible note of HK\$14.5m and gain from disposal of 20.0% interests in Goldbond Securities of HK\$25.4m, the group's core earnings for the period were HK\$114.6m. In FY03/07A, the group's core financial related business reported a loss of around HK\$38.0m.

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Stock data

Price	HK\$0.69
Target price	HK\$1.85 (+168.1%)
12 mth range	HK\$0.38-1.53
Market cap.	US\$231.6m
Daily t/o, 3 mth	US\$3.0m
Free float %	40.9%
Ticker	0172.HK/172 HK

Revenue breakdown. We estimate that Rongzhong's loan guarantee business and secured bridge financing business contributed about HK\$50.0m and HK\$166.3m to the group total turnover during the period under review. Meanwhile, the project financing loan provided to the property developers in Zhuhai generated an interest income of about HK\$10.3m to the group.

Financial summary

Year to Dec	06A	07A	08F	09F	10F
Turnover (HK\$m)	8.1	24.9	226.6	486.9	635.6
Net profit (HK\$m)	3.9	48.7	180.2	208.2	271.4
EPS (HK\$m)	0.002	0.029	0.071	0.079	0.100
EPS Δ %	(99.8)	1161.0	142.8	11.3	26.7
P/E (x)	297.1	23.6	9.7	8.7	6.9
P/B (x)	3.21	2.79	1.72	1.49	1.24
EV/EBITDA (x)	na	na	14.0	4.4	3.3
Yield (%)	-	-	-	-	-
ROE (%)	1.1	11.8	17.4	17.1	18.0
ROCE (%)	0.6	8.1	13.4	13.8	14.4
N. Gear. (%)	(66.2)	(20.6)	(21.5)	(12.7)	(13.6)

Higher-than-expected return on loan book. As at the end of March 2008, the value of Rongzhong's loan book surged more than eight-fold to HK\$582.7m. Since the group had gross cash of HK\$429.6m in hand, potentially, its loan book size can expand to about HK\$1.0b. We estimate that the group's loan portfolio yielded an average annual rate of return of 51.6% (or monthly return rate of 4.3%, calculated as the interest income generated from the loan book divided by the average loan book value as of the end of FY03/07A and FY03/08A), which was higher than our projected annual return rate of 48.0% (or monthly return rate of 4.0%).

Price Chart



Protection against default. The deteriorating macro environment in China may post negative impact on the quality of Rongzhong's loan book. Nevertheless, the loan-to-collateral value ratio of 50.0% and the high monthly interest rate of 4.0% it charged on each loan transaction should provide sufficient protection against defaults. For FY03/08A, the group provided HK\$12.1m as a allowance for debtors and loans, which was equivalent 2.1% of the group's loan book value.

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Loan guarantee business. The total guarantee amount granted by Rongzhong surged 138.4% YoY to RMB3.6b. We estimate Rongzhong generated a loan guarantee fee income of about HK\$50.0m. The return of the loan guarantee business seems low; However, the division serves as the cost center of Rongzhong as a whole, as the lucrative secured bridge financing division shares the same resources of the loan guarantee business. Further, the loan guarantee division helps Rongzhong to expand its network and strengthen its working relationship with banks in China.

Project financing. The three-year term project financing loans provided to the property development projects in Zhuhai of RMB115.0m were drawn down in January 2008. For the period of FY03/08A, the loans contributed about two and a half month interest income of HK\$10.3m to the group's top line. Interest income on the loans is expected to be recognized over three-year term. Total return of the loans is estimated at about HK\$150.0m, or 40.0% per annum, which is very lucrative.

Costs increase with revenue. The group's staff costs increased by 58.9% YoY to HK\$48.1m, accounting for 21.2% of the total turnover for FY03/08A. Its other operating expenses, including D&A, share options related expenses, allowance for debtors and loans, cost related to the employee scheme as well as other head office expenses, increased 141.7% YoY to HK\$56.9m for the period under review, on the expansion of its outlets networks. The other operating expenses for the period accounted for 25.1% of the group's total turnover.

Net cash position. As of the end of March 2008, the group had gross and net cash HK\$429.6m and HK\$194.3m in hand. Should we exclude the outstanding three-year term, zero-coupon convertible bond (face value of HK\$135.0m and exercise of HK\$1.08/share issued to Mr. Xie Xiao Qing, one of the directors of the group, as the consideration for the acquisition of the 20.0% interests in Rongzhong), the group was in the net cash position of HK\$319.7m as of the end of FY03/08A.

Receivable increase alongside with loan book. As of the end of FY03/08A, the group had long-term loan receivables of about HK\$125.0m outstanding. Such loans were drawn down by the property developer in Zhuhai in January 2008. Further, the group's debtors, advances provided to customers, prepayments and deposits surged 554.6% YoY to HK\$722.8m, due to the 704.4% YoY surge in Rongzhong's loan book to HK\$582.7m. The group's debtors and advances provided to customers also increased 328.8% YoY to HK\$84.3m. Those debtors and advances provided by the group to its customers included the working capital requirement of about HK\$40.0m for Rongzhong's loan guarantee business, interest income receivables of HK\$30.0m for Rongzhong's secured bridge financing division, interest income receivables of HK\$10.3m for the group's project financing division

Increase its interests in Rongzhong. In May and August 2007, the group entered into two loan agreements with Rongzhong, pursuant to which the Group conditionally agreed to advance a HK\$60 million and a HK\$500 million revolving loans facility respectively to Rongzhong as general working capital at interest rate of 16% per annum. The two loan agreements were approved by shareholders in June and September 2007 respectively. At the end of March 2008, the total outstanding loan advanced to Rongzhong amount to HK\$379.7m. Further, the group acquired an additional 20.0% interest in Rongzhong at the consideration of HK\$135.0m satisfied by the issuance of a three-year term zero-coupon CBs with conversion price of HK\$1.08/share to Mr. Xie in October 2007. Upon the completion of the transaction, the group's interests in Rongzhong increased to 71.0% from 51.0% previously.

Foray into private equity sector in China. Wuhan Rongzhong Growth Fund, a private equity fund with China focus was launched in May 2008. The committed capital of the fund was RMB130.0m, in which, Rongzhong had contributed RMB50.0m while other independent private enterprise investors contributed RMB80.0m. Rongzhong is appointed as a manager of the fund. The fund will leverage on Rongzhong's network and expertise to source investment opportunities in China. The fund is looking to raise another RMB50.0m from an anchor state-owned enterprise investor in August 2008. It also plans to launch a roadshow in 4Q of this year to meet other potential investors. The source of incomes from the fund to Rongzhong are: 1) management and consultancy fee income and 2) carried interests. At this stage, the group would book Rongzhong's investment into the fund as interests in associate. Should Rongzhong's interests diluted to below 20.0%, the group will treat the interests as other long term investment in the balance sheet.

Leasing business. In April 2008, Rongzhong group was granted a wholly-foreign owned leasing license by the Ministry of Commerce of PRC, and Rongzhong International Finance Lease Limited was established with

an initial registered capital of US\$10.0m. Since the leasing business is at a initial stage, we do not expect it to provide significant contribution to the group in the near future. However, the leasing business would create another source of income for Rongzhong in the long term. Further, synergy is expected to arise between Rongzhong's existing business and the leasing division, as the leasing division can share resources with Rongzhong's loan guarantee division and bridge financing division, in our view. Cross-selling opportunities are expected to emerge among Rongzhong's business lines. The leasing division will also broaden Rongzhong's network in China further.

Remain a STRONG BUY. The non-bank financial institutions are trading at an average one-year forward P/E of 12.8x and two-year forward P/E of 11.4x. Trading at FY03/09F P/E of 8.7x and FY03/10F P/E of 6.9x, the group's valuation is attractive, in our view. At this juncture, we maintain our earnings projections and key assumptions on the group's earnings for FY03/09F and FY03/10F. STRONG BUY recommendation with target price of HK\$1.85 reiterated.

Table 1: Peer group comparison

Company name	Ticker	Year End	Currency	Price	Market cap (US\$m)	P/E (x)	
						1-yr forward	2-yr forward
Aeon Credit Service Asia Co Ltd	900 HK	Feb	HKD	7.8	416.1	11.2	10.3
Credit Saison Co Ltd	8253 JP	Mar	JPY	2,130.0	3,626.9	13.9	11.8
OMC Card Inc	8258 JP	Feb	JPY	314.0	628.8	10.7	9.7
Aiful Corp	8515 JP	Mar	JPY	1,160.0	1,820.5	6.8	8.2
Takefuji Corp	8564 JP	Mar	JPY	1,373.0	1,856.6	17.5	13.5
Aeon Credit Service Co Ltd	8570 JP	Feb	JPY	1,294.0	1,903.4	13.3	11.4
Acom Co Ltd	8572 JP	Feb	JPY	2,840.0	4,248.3	10.3	13.1
Promise Co Ltd	8574 JP	Mar	JPY	2,445.0	3,090.1	17.2	10.9
Cattles PLC	CTT LN	Dec	GBp	21.8	1,103.1	10.8	11.2
CIT Group Inc	CIT US	Dec	USD	10.2	503.0	11.2	7.1
Dollar Financial Corp	DLLR US	Jun	USD	7.3	283.8	7.3	6.5
<i>Average</i>						<i>12.8</i>	<i>11.4</i>

Source: Bloomberg

Disclosure of interests: SBI E2-Capital Securities Ltd. acted as the Placing Agent for Goldbond Group (350.5m vendor shares at HK\$1.26) on August 6, 2007.