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8 November 2016

China Materials

Reuters 0868.HK
Bloomberg 868 HK

Priced on 8 November 2016
HS CEI @ 9,659.9

12M hi/lo HK\$7.53/3.48

12M price target HK\$8.30
± % potential +37%

Shares in issue 3,891.4m
Free float (est.) 43.9%

Market cap US\$3,171m

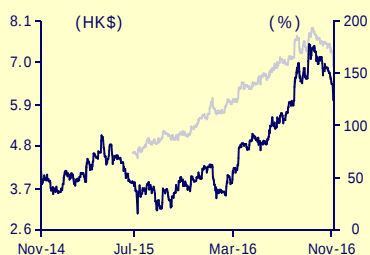
3M average daily volume
HK\$91.3m (US\$11.8m)

Foreign s'hlding 52.7%

Major shareholders
Lee Yin Yee 21.7%
Tung Ching Sai 9.7%

Stock performance (%)

	1M	3M	12M
Absolute	(15.7)	(10.8)	59.0
Relative	(13.4)	(14.3)	73.8
Abs (US\$)	(15.7)	(10.8)	58.9



Source: Bloomberg

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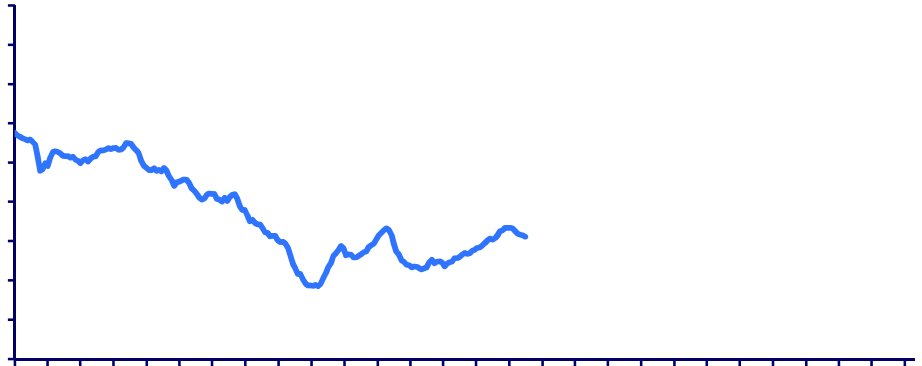
Financials

Year to 31 December	14A	15A	16CL	17CL	18CL
Revenue (HK\$m)	10,861	11,460	13,112	13,719	14,217
Adjusted net profit (HK\$m)	1,144	1,734	2,992	3,583	3,969
Adjusted EPS (HK¢)	28.4	43.0	74.5	89.6	99.2
CL/consensus (8) (EPS%)	-	-	96	98	101
Adj EPS growth (% YoY)	(45.3)	51.7	73.2	20.2	10.8
Adjusted PE (x)	21.3	14.1	8.1	6.8	6.1
Dividend yield (%)	2.5	4.4	6.2	7.5	8.3
ROE (%)	11.1	16.9	22.4	24.1	23.6
Net debt/equity (%)	42.0	37.2	36.9	24.9	12.6

Source: CLSA

Figure 1

Float glass prices in various regional markets across China



Source: WIND, CLSA

Figure 2

XYG's float glass product price quotes (5mm clear glass)

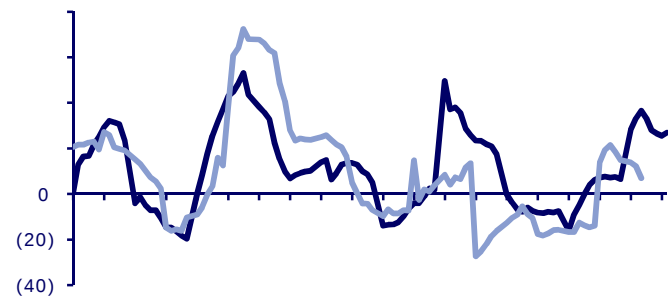
Source: SCI99.com, CLSA

Figure 3

Float glass demand/supply dynamics

Source: CLSA

Figure 4
YTD Property sales/new starts started to slow but not yet massively



Source: NBS, CLSA

Figure 5
Glass demand lags behind property sales



Source: NBS, CLSA

Figure 6
Float glass capacity under operation in China (including lines just ignited and ultra-clear lines)

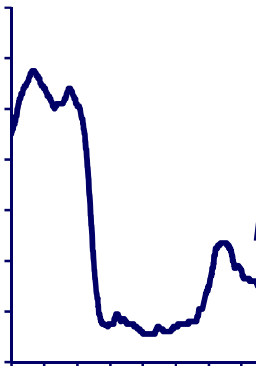
Source: CLSA

Figure 7
Float glass inventory (at producers) in China

Source: CLSA

Concerns priced in

Figure 8
Domestic soda ash prices



Source: CLSA

Figure 9
List of products enjoying high tax rebates

Source: MoF, CLSA

Figure 10

Earnings revisions

	16CL			17CL		
	New	Old	Change	New	Old	Change
Revenue (HK\$ m)	13,112	13,112	0.0 %	13,719	13,282	3.3 %
- Automobile glass products	3,978	3,978	0.0 %	4,102	4,052	1.2 %
- Construction glass	2,635	2,635	0.0 %	2,529	2,424	4.3 %
- Float glass (inc. electronic glass)	6,463	6,463	0.0 %	6,883	6,602	4.3 %
- Wind farm	37	37	0.0 %	204	204	0.0 %
Gross profit margin	35.1 %	35.1 %	0.0 ppt	37.2 %	37.5 %	-0.3 ppt
- Automobile glass products	49.2 %	48.7 %	0.4 ppt	52.5 %	51.2 %	1.3 ppt
- Construction glass	39.0 %	39.1 %	-0.1 ppt	38.7 %	39.1 %	-0.5 ppt
- Float glass (inc. electronic glass)	24.7 %	24.9 %	-0.3 ppt	26.7 %	27.5 %	-0.8 ppt
- Wind farm	70.3 %	70.3 %	0.0 ppt	70.3 %	70.3 %	0.0 ppt
Core profit (HK\$ m)	2,992	3,030	-1.3 %	3,583	3,622	-1.1 %

Source: CLSA

Figure 11

Valuation of Xinyi Glass

PE basis

Average 17-18CL EPS (HK\$)	0.95
Target multiple (x)	10.0
Fair value (HK\$)	9.50

PB basis

Average 16-17CL BVPS (HK\$)	3.71
Target multiple (x)	1.9
Fair value (HK\$)	7.10

Average (HK\$)

8.30

Implied 16/17CL PE

11.0x / 9.2x

Source: CLSA

Figure 12

Valuation of Xinyi Glass's non-solar business

HK\$m		FY16CL	FY17CL
Net profit of Xinyi Glass		2,992	3,583
Less: after-tax share of profits of Xinyi Solar		(498)	(556)
Non-solar profit	(a)	2,494	3,027
Current market cap of Xinyi Glass	(b)	23,543	23,543
Current market cap of Xinyi Solar	(c)	18,897	18,897
M'cap of Xinyi Glass's non-solar business	(d) = (b) - 29.5% * (c)	18,082	18,082
PE of Xinyi Glass's non-solar business	(e) = (d) / (a)	7.3	6.0

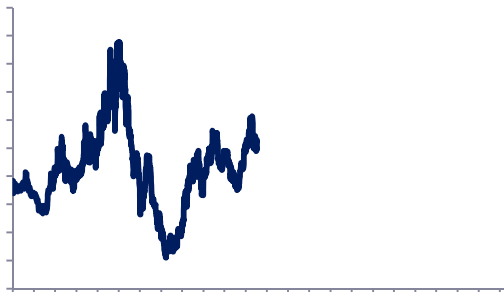
Source: CLSA

Our TP is based on a blended PE and PB approach

Current market-cap implies 7.3x/6.0x its non-solar businesses earnings in 16/17CL

Figure 13

Xinyi Glass 12m fwd PE chart



Source: CLSA, Datastream

Figure 14

Xinyi Glass 12m fwd PB chart



Figure 15

12m fwd PE chart – Xinyi Glass after stripping out Xinyi Solar at market price (since Dec-13)

Source: CLSA, Datastream

Figure 16

Valuation comp – Xinyi Glass

Stock	Ticker	Price (local)	Mkt Cap (USD,m)	ADTV (USD,m)	CLSA			12m forward valuations					EPS Cagr FY1-FY3	PEG	Gearing (%)	Performance (%)			
					Rec	Target	Upside	PE	PB	Yield	EV/Ebitda	ROE				1m	3m	6m	12m
Xinyi Glass	868 HK	6.05	3,036	11.8	BUY	8.30	37%	7.0	1.5	7.3	5.9	23.8	15.4	0.5	37	(16)	(9)	29	68
Fuyao Glass - H	3606 HK	22.90	6,728	7.0				14.9	2.6	4.4	8.3	18.3	11.2	1.3	(7)	(1)	8	31	32
China Glass	3300 HK	0.89	208	0.2											47	(14)	(20)	(11)	(21)
Luoyang Glass	1108 HK	5.27	358	2.2											221	(17)	16	13	(6)
Fuyao Glass - A	600660 CH	17.72	6,728	26.2				13.5	2.3	4.9	8.3	18.2	11.8	1.1	(7)	5	7	25	26
Yaohua Pilkington	600819 CH	7.97	1,011	8.1											46	8	7	21	4
Shandong Jinjing	600586 CH	4.69	1,009	17.4				20.1	1.5		9.2	7.3	24.5	0.8	57	2	8	5	(19)
AVIC Sanxin	002163 CH	8.47	1,004	24.4					9.7			2.6			265	6	20	20	(16)
Xiuqiang Glasswork	300160 CH	12.05	1,062	15.4				51.7	4.8	0.6	30.8	10.9	27.3	1.9	1	1	5	(17)	57
Changzhou Almaden	002623 CH	55.35	1,306	30.6											(7)	46	69	76	57
Zhuzhou Kibing	601636 CH	3.92	1,508	37.2				14.3	1.6		6.8	11.3	9.7	1.5	82	6	19	16	(19)
Taiwan Glass	1802 TT	13.90	1,285	1.5											67	(6)	5	1	(1)
Asahi Glass	5201 JP	711.00	8,072	27.5	O-PF	780.00	10%	17.1	0.8	2.5	3.5	4.7	11.5	1.5	31	7	13	16	(1)
Nippon Sheet Glass	5202 JP	786.00	679	6.7				11.9	0.9	0.2	6.4	7.7	33.1	0.4	333	(5)	(3)	(4)	(27)
Central Glass	4044 JP	405.00	833	2.7				8.9	0.5	2.7	4.9	5.7	(0.0)		23	0	(3)	(31)	(32)
Hankuk Glass Industries	002000 KS	27,000.00	240	0.0											(16)	(1)	(4)	(1)	6
Cie de St-Gobain	SGO FP	39.60	24,298	58.3				14.5	1.1	3.2	6.9	7.8	14.3	1.0	25	4	3	3	(2)
PPG Industries Inc	PPG US	94.35	24,908	167.3	O-PF	115.00	22%	14.1	4.9	1.7	9.6	34.5	12.2	1.2	59	1	(10)	(13)	(8)
Turkiye Sise	SISE TI	3.18	2,051	5.4				8.7	0.8	4.0	5.9	8.5	14.8	0.6	15	(3)	(8)	(3)	3
Trakya Cam Sanayii	TRKCM TI	2.49	729	2.9				8.4	0.7	6.4	6.4	7.4	(20.0)		14	(2)	(3)	29	27
Corning	GLW US	22.98	21,859	215.0	SELL	20.00	(13%)	14.6	1.7	2.7	8.3	10.7	(1.3)		(0)	(3)	1	25	21
Average								15.7	2.4	3.4	8.6	12.0	11.8	1.1	61.2				

Source: Bloomberg, CLSA

Valuation details

We value XYG using a blended PE and PB approach. We apply a target multiple of 10x to average 17-18CL EPS and a target multiple of 1.9x to average 16-17CL BVPS, in line with the historical averages.

Investment risks

Key risks include: 1) Weakening of the property market or even the auto market. Demand for float glass and construction glass is highly dependent on the property market. Besides, despite being a stable business, the auto glass segment is correlated to the global number of vehicles in use, and any significant slowdown in the global auto industry may also affect the segment's performance. 2) Further tightening of credit. Tightening of credit also affects developers' cash flows and progress in construction of property projects. 3) Incremental production costs. A significant surge in natural gas, international crude oil prices and other raw material costs may affect XYG's gross margin if it cannot pass on incremental costs by raising ASP. 4) More capacity additions in the market.

Valuation details - Asahi Glass Co Ltd 5201 JP

We value the stock using a PB valuation derived from a PB - ROE correlation. We use quarterly PB and ROE since 2010 for our linear regression. While we forecast Asahi Glass to see revenue and operating profit growth in the medium term as the US and Eurozone economies improve and chemicals experience success with new products along with growth in Southeast Asia, nonoperating costs are a slight drag on net profits and ROE. Our target price of ¥780 is based on a PB of 0.81x FY12/17CL estimates.

Investment risks - Asahi Glass Co Ltd 5201 JP

Fluctuating fuel costs are a risk because almost all of its businesses consume large amounts of fuel and materials. A US\$1 fall in oil prices adds ¥400mn to OP. An increase in oil prices would cause a decline in profits. We expect the LCD substrate market to continue to see price cuts, but if weakness in downstream markets put more pressure on prices they may decline more than our expectations. The company is expecting ¥30bn in non-operating costs, but we are assuming ¥20bn. If non-operating costs reach ¥30bn, net profits would drop which would affect our PB-ROE correlation derived PB multiple.

Valuation details - Corning Inc GLW US

Our price target of \$20 equates to a PE multiple of 12.6x applied to our 2017 EPS estimate of \$1.59. This reflects a 25% discount overall to the market multiple (in line with last few years) due to the low quality of its earnings, weak TV, partially offset by near term better panel demand trends, and includes part of its net cash and dividend and relatively stable pricing environment. Corning has a strong net cash position, pays dividends (about 3% yield), and we expect it to generate healthy free cashflow in 2016 that should limit further downside risk. At our price target, the stock would be discounting a 6% FCF yield on 17CL estimates.

Investment risks - Corning Inc GLW US

Risks to our rating and price target include stabilizing weeks of inventory in the supply chain, a more favorable pricing environment, and improving profitability for Samsung Corning Precision and Dow Corning. Downside risks include an inability to diversify the business in the coming years, an extended inventory correction in LCD panels and Gorilla Glass in the coming quarters, and continued LCD glass price pressures not factored into our model.

Valuation details - PPG Industries Inc PPG US

Our target price is based on a three-stage DCF model with explicit, mid-cycle and long-term phases. Each phase assumes asset growth, return on capital, capital structure and cost of debt representative of economic cycle and probable funding costs. In general, we assume return and asset growth fade to long-term trends, with return on invested capital generally approximating the firm's weighted average cost of capital over the long term. For cost of equity, we use a beta of one which approximates the firm's historical average, and a market risk premium of 6%.

Investment risks - PPG Industries Inc PPG US

PPG's broad economic exposure suggests that in a weakening environment, the company's results are likely to suffer. The inability to effect meaningful M&A could harm PPG's long-term growth potential. Conversely, a large acquisition could harm the company's balance sheet by increasing debt levels to risky levels and substantially expanding interest costs and leverage. A downturn in global auto production would harm PPG's profitability given the end market represents close to 25% of the company's revenue in terms of OEM and refinish.



Summary financials

Year to 31 December	2014A	2015A	2016CL	2017CL	2018CL
Summary P&L forecast (HK\$m)					
Revenue	10,861	11,460	13,112	13,719	14,217
Op Ebitda	1,740	2,313	3,638	4,238	4,578
Op Ebit	1,095	1,518	2,761	3,279	3,546
Interest income	53	40	52	48	42
Interest expense	(91)	(90)	(122)	(93)	(61)
Other items	536	912	798	906	1,046
Profit before tax	1,593	2,380	3,490	4,140	4,573
Taxation	(228)	(266)	(498)	(556)	(604)
Minorities/Pref divs	(1)	0	0	0	0
Net profit	1,364	2,113	2,992	3,583	3,969
Summary cashflow forecast (HK\$m)					
Operating profit	1,095	1,518	2,761	3,279	3,546
Operating adjustments	-	-	-	-	-
Depreciation/amortisation	644	795	876	959	1,032
Working capital changes	(559)	(207)	(246)	(59)	(62)
Net interest/taxes/other	(314)	(421)	(620)	(649)	(665)
Net operating cashflow	867	1,685	2,772	3,531	3,851
Capital expenditure	(1,729)	(1,967)	(1,700)	(1,500)	(1,300)
Free cashflow	(862)	(282)	1,072	2,031	2,551
Acq/inv/disposals	93	-	(618)	-	-
Int, invt & associate div	588	951	850	954	1,088
Net investing cashflow	(1,049)	(1,016)	(1,468)	(546)	(212)
Increase in loans	873	16	619	(1,611)	(1,647)
Dividends	(902)	(1,029)	(1,471)	(1,762)	(1,952)
Net equity raised/other	0	812	(265)	0	0
Net financing cashflow	(30)	(202)	(1,117)	(3,374)	(3,599)
Incr/(decr) in net cash	(211)	468	187	(390)	40
Exch rate movements	-	-	-	-	-
Opening cash	1,043	832	1,300	1,487	1,098
Closing cash	832	1,300	1,487	1,098	1,137
Summary balance sheet forecast (HK\$m)					
Cash & equivalents	832	1,300	1,487	1,098	1,137
Debtors	1,028	1,136	1,238	1,295	1,342
Inventories	1,478	1,223	1,368	1,371	1,404
Other current assets	1,467	1,337	1,337	1,337	1,337
Fixed assets	11,293	11,971	12,825	13,396	13,694
Intangible assets	1,366	1,281	1,250	1,220	1,191
Other term assets	3,570	3,174	3,792	3,792	3,792
Total assets	21,034	21,422	23,298	23,509	23,898
Short-term debt	2,529	2,514	2,772	2,100	1,414
Creditors	724	740	741	743	761
Other current liabs	1,548	1,705	1,705	1,705	1,705
Long-term debt/CBs	3,483	3,514	3,875	2,936	1,976
Provisions/other LT liabs	414	223	223	223	223
Minorities/other equity	2	7	7	7	7
Shareholder funds	12,333	12,718	13,974	15,795	17,812
Total liabs & equity	21,034	21,422	23,298	23,509	23,898
Ratio analysis					
Revenue growth (% YoY)	9.3	5.5	14.4	4.6	3.6
Ebitda growth (% YoY)	(37.7)	33.0	57.3	16.5	8.0
Ebitda margin (%)	16.0	20.2	27.7	30.9	32.2
Net profit margin (%)	12.6	18.4	22.8	26.1	27.9
Dividend payout (%)	44.4	50.5	50.7	50.6	50.6
Effective tax rate (%)	14.3	11.2	14.3	13.4	13.2
Ebitda/net int exp (x)	45.7	46.1	52.2	95.2	236.9
Net debt/equity (%)	42.0	37.2	36.9	24.9	12.6
ROE (%)	11.1	16.9	22.4	24.1	23.6
ROIC (%)	6.2	8.7	15.1	17.2	18.1
EVA@/IC (%)	(5.4)	(2.9)	3.5	5.6	6.5

Source: CLSA

Improving margins and higher associates profit to drive earnings growth

Capex mainly on wind farm and Malaysia investments

Balance sheet still healthy

Improving ROE

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Companies mentioned

Xinyi Glass (868 HK - HK\$6.05 - BUY)¹
Asahi Glass (5201 JP - ¥711 - OUTPERFORM)¹
AVIC Sanxin (N-R)
Central Glass (N-R)
Changzhou Almaden (N-R)
China Glass (N-R)
Corning (GLW US - US\$22.98 - SELL)²
Fuyao Glass - H (N-R)
Fuyao Glass (N-R)
Hankuk Glass Ind (N-R)
Jinjing (N-R)
Kibing (N-R)
Luoyang Glass (N-R)
NSG (N-R)
PetroChina (857 HK - HK\$5.40 - BUY)¹
PPG (PPG US - US\$94.35 - OUTPERFORM)²
Saint-Gobain (N-R)
Sise Cam (N-R)
SYP Glass (N-R)
Taiwan Glass (N-R)
Trakya Cam Sanayii (N-R)
Xinyi Solar (968 HK - HK\$2.80 - BUY)¹
Xiuqiang Glasswork (N-R)

¹ Covered by CLSA; ² Covered by CLSA Americas

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Important disclosures

Recommendation history of Xinyi Glass Holdings Ltd 868 HK

Date	Rec	Target	Date	Rec	Target
LATEST	BUY	8.30	24 Apr 2015	O-PF	4.90
08 Sep 2016	BUY	8.35	03 Mar 2015	O-PF	4.81
03 Aug 2016	BUY	7.25	10 Dec 2014	O-PF	4.23
15 Jun 2016	O-PF	6.12	25 Sep 2014	O-PF	5.28
04 May 2016	O-PF	5.56	24 Jul 2014	O-PF	4.85
16 Mar 2016	O-PF	4.80	25 Jun 2014	O-PF	4.95
05 Feb 2016	O-PF	4.24	23 May 2014	BUY	6.31
19 Nov 2015	O-PF	4.33	27 Feb 2014	BUY	8.48
29 Jul 2015	O-PF	4.24	02 Dec 2013	BUY	8.95

Source: CLSA

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to our "Double Bagger" list. "High Conviction" Ideas are not necessarily stocks with the most upside/downside, but those where the Research Head/Strategist believes there is the highest likelihood of positive/negative returns. The list for each market is monitored weekly.

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Investment banking clients as a % of rating category: Buy / Outperform - CLSA: 2.78%; CLSA Americas only: 0.00%; CLST only: 0.00%, Underperform / Sell - CLSA: 2.79%; CLSA Americas only: 0.00%; CLST only: 0.00%, Restricted - CLSA: 0.00%; CLSA Americas only: 0.00%; CLST only: 0.00% . Data for 12-month period ending 30 September 2016.

There are no numbers for Hold/Neutral as CLSA/CLSA Americas/CLST do not have such investment rankings.

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