

8 December 2016

Industrial | Misc. Manufacturer

Xinyi Glass Holdings

Buy (Maintained)

Qianhai Land Acquisition a Long Term Strategic Move

We believe Xinyi Glass' (XYG) successful bid for a piece of land in Qianhai to build a new global headquarters has upside potential and is a long-term strategic move. In a conference call, XYG's management also reiterated its positive view on the company's float glass business despite property tightening measures. We find this reassuring. We maintain our **BUY** rating and TP of HKD8.40 (38% upside). XYG currently trades at an undemanding 7x FY17F P/E and also gives an attractive 6.5% FY16F yield.

A long-term strategic move supported by solid financials. Management stressed that the move is a strategic one with an aim to establish a global headquarters in the Qianhai zone, which should benefit from favourable government policies (eg competitive tax rate of 15% vs standard corporate tax rate of 25% in China, financial reform initiatives, trade-related support). Management expects the project could be comfortably financed by free cash capabilities and low-interest environment in HK, its interest cost is very competitive at only 2.2%. Management is confident of maintaining a decent dividend payout ratio.

Neighbourhood property transactions imply upside potential. According to management, office property price in regions adjacent to Qianhai zone is ~CNY80,000-90,000/sqm., which implies potential upside given the budgeted total development costs of just ~CNY40,000/sqm. (land cost:~CNY30,000/sqm; construction cost: <CNY10,000/sqm). The development period is expected to be ~three years. Although the office building would global headquarters, the company has the flexibility to rent out some of the floor area. The estimated annual market rent of ~CNY3,000/sqm implies a gross renta s view. Management re-iterated that XYG has no plans to diversify its business into property development.

Float glass recovery cycle to sustain into 2017. Management see stable and rational industry capacity supply and maintain the positive view on the float glass recovery cycle into 2017 on balanced supply/demand landscape. Float glass demand should remain strong despite recent property market tightening measures amid resilient end-user demand. Despite increased volatility in raw material price trends in 2H16, we view GPM expansion remained intact on diversified and cost-competitive raw material sourcing. Management indicated that the recent domestic natural gas price hike was seasonable and may return to the pre-hike level in mid-Jan 2017. Despite the recent surge in domestic soda ash price, management sees limited impact as XYG also increased the use of imported soda ash, for which pricing has been more stable.

Maintain BUY and HKD8.40 TP. Our TP is based on 10x FY17F recurring P/E, roughly on par with the long-term average. Our TP also implies 2.1x FY17F P/BV (~1SD > long term average), as we believe the earnings upcycle since early 2016 remains intact. We are keeping our earnings estimates unchanged.

Target Price: HKD8.40
Price: HKD6.09
Market Cap: USD3,055m
Bloomberg Ticker: 868 HK

Share Data

Avg Daily Turnover (HKD/USD) 82.0m/10.3m
52-wk Price low/high (HKD) 3.48 - 7.53
Free Float (%) 53
Shares outstanding (m) 3,922
Estimated Return 38%

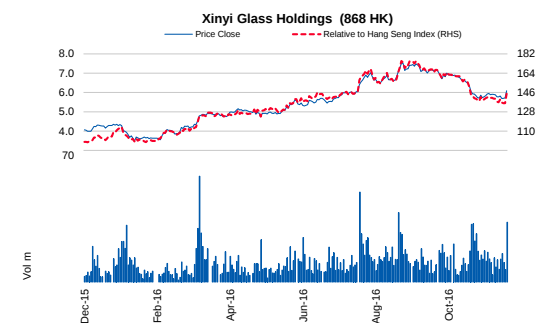
Shareholders (%)

Chairman LEE Yin Yee 21.3
Other management staff 25.6

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	41.8	0.7	(19.1)	8.9	50.4
Relative	37.5	0.9	(14.7)	1.6	46.0

Source: Bloomberg



Source: Bloomberg

Forecasts and Valuations	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total turnover (HKDm)	10,861	11,460	13,133	14,267	15,444
Reported net profit (HKDm)	1,364	2,113	3,017	3,285	3,776
Recurring net profit (HKDm)	1,146	1,819	3,017	3,285	3,776
Recurring net profit growth (%)	(45.9)	58.7	65.8	8.9	15.0
Recurring EPS (HKD)	0.30	0.46	0.77	0.84	0.96
DPS (HKD)	0.15	0.26	0.37	0.41	0.47
Recurring P/E (x)	20.6	13.1	7.9	7.3	6.3
P/B (x)	1.94	1.88	1.65	1.51	1.37
P/CF (x)	12.1	8.5	6.4	5.9	5.2
Dividend Yield (%)	2.5	4.3	6.2	6.7	7.7
EV/EBITDA (x)	13.7	10.2	6.8	6.4	5.7
Return on average equity (%)	11.1	16.9	22.2	21.7	22.7
Net debt to equity (%)	42.0	37.2	32.5	26.0	19.4
Our vs consensus EPS (adjusted) (%)			(1.5)	(6.8)	(0.2)

Source: Company data, RHB

Analyst

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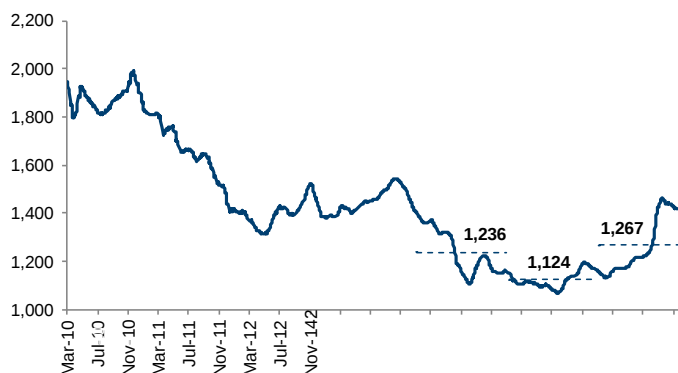


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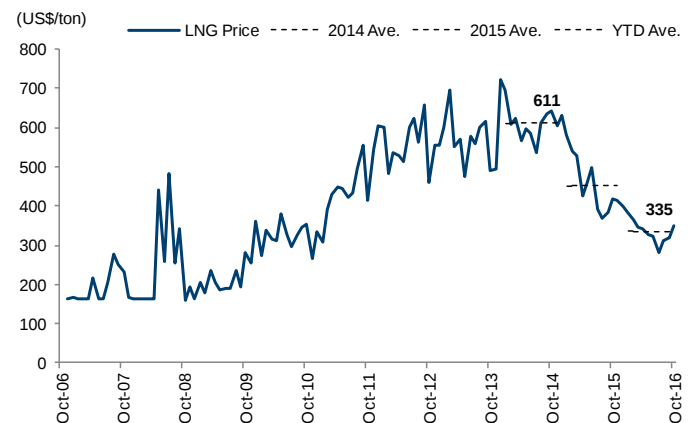
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Other key takeaways.

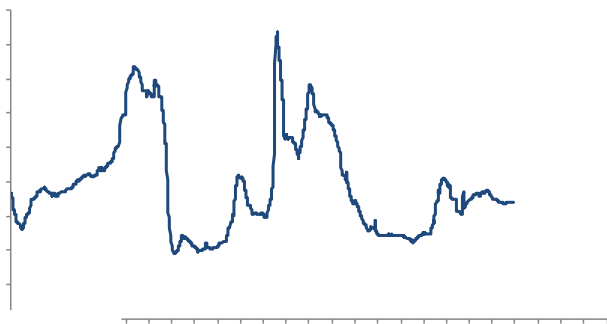
- i. Management see limited impact on XYG from the recent management shakeups at China Southern Glass (CSG) (000012 CH, NR). Although some former executives at CSG have joined competitor Zhuzhou Kibing (601636 CH, NR), integration would take time;
- ii. Ramp-up of the new Malaysia plant (1,200 tonnes per day) is on track with sales contribution starting to be reflected in 1H17. Industry glass ASP in Malaysia is ~15-20% higher than that in China while per-unit production cost is lower, which should translate into better GPM, according to management. The plant has an annual production capacity of ~350,000-360,000 tonnes (1,200 tonnes per day).

Figure 1: National average float glass price in major cities in China

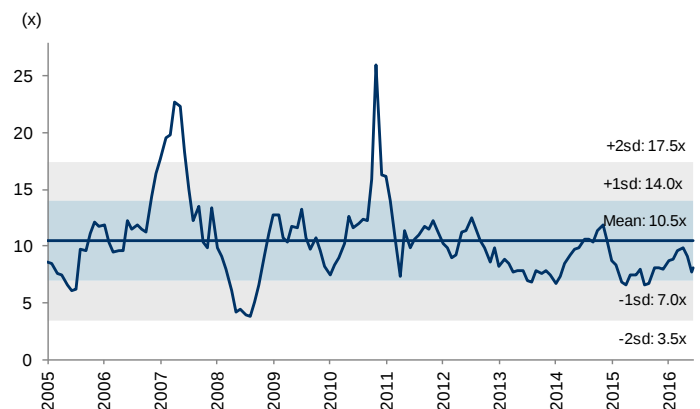
Source: Wind, RHB

Figure 2: Imported liquefied natural gas (LNG) price

Source: RHB

Figure 3: Domestic soda ash price in China

Source: Wind, RHB

Figure 4: Forward P/E band chart

Source: Company, RHB

About Qianhai Shenzhen-Hong Kong Modern Service Industry Corporation Zone. Qianhai is a modern demonstration of the innovative cooperation between Guangdong and Hong Kong to create a modern service industry zone. The State Council approved the overall development plan for the Shenzhen-Hong Kong modern service industry cooperation zone in Qianhai on 26 Aug 2010. The aim is to develop Qianhai into the

It was also determined that Qianhai should be built and developed at a high standard. The cooperation between Guangdong and Hong Kong puts into practice new approaches to Shenzhen-Hong Kong cooperation. A key comparative advantage of Qianhai is that corporations that have passed the evaluation can enjoy a corporate income tax rate of 15%. In addition, employee education and training expenses that do not exceed 8% of the -tax. Qianhai also enjoys close proximity to Hong Kong.

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Recommendation Chart



Date	Recommendation	Target Price	Price
2016-11-13	Buy	8.40	5.84
2016-09-14	Buy	8.40	7.23
2015-11-05	Buy	5.20	3.87
2015-07-29	Buy	5.50	3.62
2015-03-03	Buy	5.80	4.40
2015-02-25	Neutral	4.60	4.04
2014-07-24	Neutral	5.70	4.48
2014-02-27	Buy	8.95	6.44
2013-12-09	Buy	8.78	6.74
2013-10-16	Buy	9.33	6.47

Source: RHB, Bloomberg

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