Xinyi Glass

Lifting PT to HK$10.50 - Near-record margins all around

Overweight

0868.HK, 868 HK

Price: HK$7.04

▲ **Price Target: HK$10.50**
Previous: HK$10.00

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	YTD	1m	3m	12m
Abs	11.0%	0.4%	19.3%	71.3%
Rel	3.1%	-1.2%	15.3%	47.1%

Xinyi Glass (Reuters: 0868.HK, Bloomberg: 868 HK)Ṻ Ṕi A ƅ

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Revenue (HK$ mn)	10,861	11,460	12,848	16,750	19,357
Net Profit (HK$ mn)	1,365	2,113	3,216	4,374	5,099
EPS (HK$)	0.35	0.54	0.83	1.12	1.31
DPS (HK$)	0.15	0.27	0.40	0.56	0.65
Revenue growth (%)	9.3%	5.5%	12.1%	30.4%	15.6%
EPS growth (%)	(58.9%)	54.8%	53.1%	36.0%	16.6%
ROCE	6.1%	8.3%	13.5%	16.0%	16.8%
ROE	11.1%	16.9%	24.8%	29.1%	28.2%
P/E (x)	20.2	13.0	8.5	6.3	5.4
P/BV (x)	2.2	2.2	2.1	1.6	1.4
EV/EBITDA (x)	16.3	12.1	7.8	5.9	5.0
Dividend Yield	2.1%	3.8%	5.7%	8.T	

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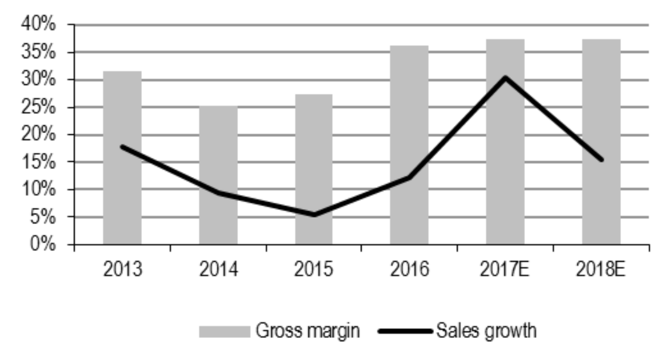
• Price of float glass improving after the slack 1Q season • More information on new electric (LCD) glass business to indicate sales and profit contribution • Finalization of new downstream solar projects	• A rise in float glass price higher than our expectations, driven by strong construction demand • New customers for the electric glass business of better quality than what we expect • Faster completion of new electric glass lines to boost sales	• Further weakness in PV glass demand from Europe • Falling demand for construction and float glass that may result from a cooling property market in China

Revenues (LC mn)	11,460	12,848	16,750	19,357
Revenue growth (%)	na	12.1%	30.4%	15.6%
EBITDA (LC mn)	2,528	3,991	5,202	6,031
EBITDA margin (%)	22.1%	31.1%	31.1%	31.2%
Tax rate (%)	11%	16%	16%	15%
Net profit (LC mn)	2,113	3,216	4,374	5,099
EPS (LC)	0.540	0.826	1.124	1.310
EPS growth (%)	na	53.1%	36.0%	16.6%
DPS (LC)	0.27	0.40	0.56	0.65
BVPS (LC)	3.25	3.39	4.32	4.98
Operating cash flow (LC mn)	2,838	3,717	4,026	4,900
Free cash flow (LC mn)	968	643	1,550	2,736
Interest cover (x)	50	52	368	457
Net margin (%)	18.4%	25.0%	26.1%	26.3%
Sales/assets (X)	0.54	0.57	0.63	0.64
Debt/equity (%)	47.4%	57.9%	45.4%	39.5%
Net debt/equity (%)	37.2%	37.1%	29.1%	21.8%
ROE (%)	17%	25%	29%	28%

Auto glass capacity (m)	16.6	17.4	18.3	19.2
Float glass capacity (mn tonnes)	5.1	5.9	6.6	7.0
Float glass price (HK$/ton)	1,379	1,573	1,840	1,932

Source: Company and J.P. Morgan estimates.

Our PT is derived from a DCF-based valuation with a WACC of 11.4% and a terminal growth rate of 3%.



Source: Bloomberg, Company and J.P. Morgan estimates.

Sensitivity to				
5% chg. in float glass price	9%	9%	7%	7%
5% chg. in fuel cost	-2%	-2%	-2%	-2%
5% chg. in wage	-3%	-3%	-2%	-2%
1% chg. in GM	4%	4%	3%	3%

Source: J.P. Morgan estimates.

JPMe old	1.09	1.26
JPMe new	1.124	1.310
Consensus	0.91	0.979

Source: Bloomberg, J.P. Morgan estimates.

CHINA STATE CONS	3311 HK	12.7	7,307.6	13.0	1.3	11.3	8.9	21.0	1.6	2.6
ND PAPER	2689 HK	9.9	5,928.6	21.8	45.3	17.1	10.7	13.4	1.3	0.9
LM PAPER	2314 HK	7.0	4,116.7	12.4	18.1	11.4	8.7	13.4	1.7	2.9
HAITIAN	1882 HK	16.3	3,339.3	2.1	5.3	16.1	13.3	17.0	1.9	2.1
KINGBOARD CHEM	148 HK	27.5	3,654.4	7.0	26.2	5.9	6.0	12.9	0.6	5.1
CHINA LESSO	2128 HK	5.8	2,318.9	1.8	3.9	8.1	7.4	18.3	1.1	3.1
KB LAM	1888 HK	8.7	3,413.1	5.7	26.6	6.7	10.6	29.0	1.5	12.7

Source: Company data, Bloomberg, J.P. Morgan estimates. Share prices are as of intraday price of 28 Feb 2017.

Highlights from the analyst briefing

FY16 results review

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Turnover	11,460	12,848	12.11%	13,451	-4%
Gross profit	3,132	4,659	48.75%	4,615	1%
GPM	27.3%	36.3%		34.3%	
EBIT	2,113	3,337	57.96%	2,925	14%
EBITM	18.4%	26.0%	478.5%	21.7%	
Net profit	2,113	3,213	52.08%	3,179	1%
NP margin	18.4%	25.0%		23.6%	
EPS (HK$)	0.53	0.82	54.40%	0.82	0%

Source: Company reports, J.P. Morgan estimates.

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Lifting earnings estimates to reflect a strong 2016 EBIT

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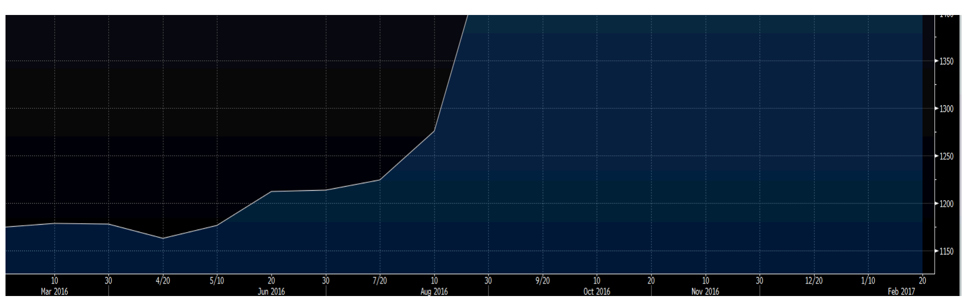

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Valuation and share price analysis

DCF valuation

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Sales	9,936	10,861	11,460	12,848	16,750	19,357	21,493	23,644
EBIT	2,212	1,274	1,733	3,178	4,310	5,062	5,714	6,371
NOPAT	2,229	1,092	1,540	2,924	3,861	4,550	5,144	5,781
Capex, net	(2,913)	(1,715)	(1,914)	(1,853)	(2,261)	(1,937)	(1,624)	(2,201)
Depreciation	639	644	795	812	892	969	1,021	1,051
Change in working capital	129	60	539	(8)	(569)	(324)	(223)	(299)
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Liabilities as a % of EV	10%	Terminal growth	3.0%
WACC	11.4%	Risk-free rate	4.2%
		Market risk	6.0%
1 1	**,1**	Beta	1.30
+ Net cash (debt), 14E	(4,913)	Cost of debt	6.2%
- Minorities (Market value)	(8)		
+/- Other items	0	Implied exit P/E multiple (x)	8x
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/ Number of shares	3,915		
e $ e HK	**1**		

Source: Company data, J.P. Morgan estimates.

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11	8.6	9		1	1	11.2	11.9
1	8.1	8.5	8.9	9.3	9.9	10.4	11.1
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Source: J.P. Morgan estimates.

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Automobile glass	3,287	3,593	3,786	3,748	4,323	4,540
YoY	6.8%	9.3%	5.4%	-1.0%	15.4%	5.0%
% of total	33.1%	33.1%	33.0%	29.2%	26.0%	23.8%
Construction glass	2,155	2,556	2,652	2,590	3,450	4,170
YoY	36.9%	18.6%	3.8%	-2.3%	33.2%	20.9%
% of total	21.7%	23.5%	23.1%	20.2%	20.8%	21.9%
Float glass	4,494	4,269	4,671	6,010	7,915	8,831
YoY i	18.9%	-5.0%	9.4%	28.7%	31.7%	11.6%
% of total	45.2%	39.3%	40.8%	46.9%	47.7%	46.3%
PV glass	0	0	0	0	0	0
YoY	45.2%	39.3%	40.8%	46.9%	47.7%	46.3%
% of total	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Electronic glass	0	443	351	475	919	1536
YoY	na	na	-20.8%	35.3%	93.4%	67.2%
% of total	0.0%	4.1%	3.1%	3.7%	5.5%	8.1%
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Source: Company data, J.P. Morgan estimates.

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YoY change (%)	1.5%	9.3%	5.5%	12.1%	30.4%	15.6%
Cost of goods sold	(6,799)	(8,127)	(8,328)	(8,189)	(10,485)	(12,108)
YoY change (%)	-7.0%	19.5%	2.5%	-1.7%	28.0%	15.5%
Gross profit	3,137	2,734	3,132	4,659	6,265	7,249
YoY change (%)	26.7%	-12.9%	14.6%	48.7%	34.5%	15.7%
Gross margin	31.6%	25.2%	27.3%	36.3%	37.4%	37.4%
SGA i	(1,251)	(1,638)	(1,615)	(1,822)	(2,295)	(2,568)
YoY change (%)	4.5%	30.9%	-1.4%	12.9%	25.9%	11.9%
Other income/(expenses)	326	178	215	342	340	381
Operating profit	2,212	1,274	1,733	3,178	4,310	5,062
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EBITDA margin	28.7%	17.4%	20.2%	31.1%	31.1%	31.2%
Depreciation & amortization	(639)	(612)	(580)	(812)	(892)	(969)
YoY change (%)	9.5%	-4.3%	-5.2%	40.0%	9.8%	8.6%
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EBIT margin	22.3%	11.7%	15.1%	24.7%	25.7%	26.2%
Net interest expense	(60)	(38)	(50)	(77)	(14)	(13)
Exceptional item	1,453	220	379	159	0	0
Associates	21	138	317	563	885	920
Gains/losses	0	0	0	0	0	0
Net income before taxes	3,627	1,594	2,379	3,823	5,180	5,969
YoY change (%)	159.5%	-56.1%	49.3%	60.7%	35.5%	15.2%
Tax	(381)	(228)	(266)	(607)	(807)	(870)
Effective tax rate	17.5%	16.6%	13.3%	16.6%	15.6%	14.6%
Minority interests	1	0	0	0	0	0
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YoY change (%)	172.9%	-36.1%	54.8%	52.2%	36.0%	16.6%
Net margin	32.7%	12.6%	18.4%	25.0%	26.1%	26.3%

Source: Company data, J.P. Morgan estimates.

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Total revenues	4,883	6,577	5,885	6,963	7,672	9,078
Gross profit	1,410	1,722	2,041	2,618	2,745	3,520
EBIT	944	789	1,304	1,875	1,767	2,542
Net income before taxes	1,085	1,294	1,572	2,251	2,125	3,056
Net income	946	1,167	1,369	1,846	1,794	2,580
Diluted EPS (HK$)	0.242	0.30	0.352	0.474	0.461	0.663
Revenue split	42.6%	57.4%	46%	54.2%	45.8%	54.2%
GPM	28.9%	26.2%	34.7%	37.6%	35.8%	38.8%
EBIT margin	19.3%	12.0%	22.2%	26.9%	23.0%	28.0%
NPM	19.4%	17.7%	23.3%	26.5%	23.4%	28.4%
Revenue	-3.0%	12.9%	20.5%	5.9%	30.4%	30.4%
GP	5.5%	23.3%	44.8%	52.0%	34.5%	34.5%
EBIT	11.9%	83.2%	38.1%	137.8%	35.6%	35.6%
NP	24.2%	93.4%	44.7%	58.3%	31.0%	39.7%

Source: Company data, J.P. Morgan estimates.

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Cash and cash equivalents	1,042	831	1,298	2,763	2,762	3,435
Inventories	1,232	1,478	1,223	1,321	1,722	1,990
Accounts receivable	2,255	2,487	2,381	2,377	3,099	3,581
Other current assets	7	8	93	76	2,103	2,852
Total current assets	4,537	4,805	4,995	6,537	9,685	11,859
Intangible assets	0	0	0	0	0	0
Property and equipment, net	9,983	11,293	13,177	12,952	14,320	15,288
Other assets	5,131	4,936	3,249	4,534	4,761	4,999

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EBIT	2,212	1,274	1,733	3,178	4,310	5,062
Depreciation and amortization	639	644	795	812	892	969
Working capital changes	129	60	539	(8)	(569)	(324)
Tax paid	(209)	(381)	(228)	(266)	(607)	(807)
Cash flow from operations	2,772	1,598	2,838	3,717	4,026	4,900
Capital expenditures	(2,913)	(1,715)	(1,914)	(1,853)	(2,261)	(1,937)
Investments and others	(208)	32	243	(1,116)	39	38
Net interest	(60)	(38)	(50)	(77)	(14)	(13)
Cash flow from investing	(3,181)	(1,720)	(1,721)	(3,046)	(2,236)	(1,912)
c		**1**	**1,11**	**1**	**1,**	**,**
Dividends	(834)	(902)	(608)	(1,297)	(1,872)	(2,368)
Common issue	916	(3)	1	0	0	0
Other financing	688	833	(18)	2,092	81	54
Contribution from owner	0	(17)	(25)	0	0	0
Cash flow from financing	770	(89)	(650)	794	(1,791)	(2,314)
Change in cash	338	(195)	467	1,465	(1)	674
Cash beginning	703	1,042	831	1,298	2,763	2,762
Foreign exchange changes	1	(17)	0	0	0	0
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Source: Company data, J.P. Morgan estimates.

Investment Thesis, Valuation and Risks

Xinyi Glass *(Overweight; Price Target: HK$10.50)*

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D&A	(644)	(795)	(812)	(892)	(969)
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Net Interest	(38)	(50)	(77)	(14)	(13)
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Tax	(228)	(266)	(607)	(807)	(870)
Minority Interest	0	0	0	0	0
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Reported EPS	0.35	0.54	0.83	1.12	1.31
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Payout ratio	43.0%	49.1%	48.4%	50.0%	50.0%
Shares outstanding	3,915	3,915	3,893	3,893	3,893

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Cash and cash equivalents	831	1,298	2,763	2,762	3,435
Accounts receivable	2,487	2,381	2,377	3,099	3,581
Inventories	1,478	1,223	1,321	1,722	1,990
Other current assets	8	93	76	2,103	2,852
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PP&E	11,293	13,177	12,952	14,320	15,288
LT investments	4,936	3,249	4,534	4,761	4,999
Other non current assets	4,936	3,249	4,534	4,761	4,999
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Short term borrowings	2,609	2,514	3,165	2,780	2,780
Payables	724	740	789	1,029	1,189
Other short term liabilities	1,468	1,705	2,046	2,815	3,431
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Long-term debt	3,483	3,514	4,509	4,895	4,895
Other long term liabilities	3,898	3,737	4,775	5,242	5,296
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Shareholders' equity	12,333	12,718	13,181	16,835	19,385
Minority interests	2	8	66	66	66
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Net debt/(cash)	5,261	4,730	4,911	4,913	4,239

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o/w Depreciation & amortization	644	795	812	892	969
o/w Changes in working capital	60	539	(8)	(569)	(324)
i e i i i e c	1,	1, 1	,	,	1,
o/w Capital expenditure	(1,723)	(1,914)	(3,138)	(2,487)	(2,175)
%					
i i i i e c c				1, 1	, 1
o/w Dividends paid	(902)	(608)	(1,297)	(1,872)	(2,368)
o/w Net debt issued/(repaid)	833	(18)	2,092	81	54
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EBITDA margin	17.7%	22.1%	31.1%	31.1%	31.2%
EBIT margin	11.7%	15.1%	24.7%	25.7%	26.2%
Net profit margin	12.6%	18.4%	25.0%	26.1%	26.3%
ROE	11.1%	16.9%	24.8%	29.1%	28.2%
ROA	6.7%	10.0%	14.2%	16.6%	16.7%
ROCE	6.1%	8.3%	13.5%	16.0%	16.8%
Net debt/equity	42.7%	37.2%	37.1%	29.1%	21.8%
Sales/Assets (x)	0.5	0.5	0.6	0.6	0.6
Interest cover (x)	50.4	50.3	51.9	368.0	457.2

	1	1	1	1	1
P/E (x)	20.2	13.0	8.5	6.3	5.4
P/BV (x)	2.2	2.2	2.1	1.6	1.4
EV/EBITDA (x)	16.3	12.1	7.8	5.9	5.0
Dividend Yield	2.1%	3.8%	5.7%	8.0%	9.3%

Source: Company reports and J.P. Morgan estimates.
Note: HK$ in millions (except per-share data).Fiscal year ends Dec. o/w - out of which

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