CHINA CONNECT

Lifting PT to HK$9.3 - Float glass recovery stronger than expected

Price: HK$7.08

Previous: HK$8.20

AC

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YTD	1m	3m	12m
Abs	55.3%	6.5%	24.2%	106.4%
Rel	46.8%	-0.9%	11.1%	90.8%

m D	Y	Y	Y	Y	Y
Revenue (HK$ mn)	10,861	11,460	13,059	15,603	17,453
Net Profit (HK$ mn)	1,365	2,113	3,119	3,806	4,419
EPS (HK$)	0.35	0.54	0.80	0.98	1.14
DPS (HK$)	0.15	0.27	0.40	0.49	0.57
Revenue growth (%)	9.3%	5.5%	14.0%	19.5%	11.9%
EPS growth (%)	(58.9%)	54.8%	48.9%	22.0%	16.1%
ROCE	6.1%	8.3%	12.6%	14.0%	15.2%
ROE	11.1%	16.9%	23.1%	25.0%	25.6%
P/E (x)	20.3	13.1	8.8	7.2	6.2
P/BV (x)	2.2	2.2	1.9	1.7	1.5
EV/EBITDA (x)	14.4	10.7	7.2	5.9	4.9
Dividend Yield	2.1%	3.7%	5.7%	6.9%	8.0%

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

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Shares O/S (mn)	3,687
Market Cap (HK$ mn)	26,103
Market Cap ($ mn)	3,366
Price (HK$)	7.08
Date Of Price	06 Sep 16
Free Float(%)	45.4%
3M - Avg daily vol (mn)	12.63
3M - Avg daily val (HK$ mn)	78.41
3M - Avg daily val ($ mn)	10.1
HSI	2,3649.55
Exchange Rate	7.76
Price Target End Date	31-Dec-17
Price Target (HK$)	9.30

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	Upside risks	Downside risks
• 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 is of a 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

	FY15	FY16E	FY17E	FY18E
Revenues (LC)	11,460	13,059	15,603	17,453
Revenue growth (%)	na	14.0%	19.5%	11.9%
EBITDA (LC)	2,528	3,661	4,390	5,101
EBITDA margin (%)	22.1%	28.0%	28.1%	29.2%
Tax rate (%)	11%	14%	14%	14%
Net profit (LC)	2,113	3,119	3,806	4,419
EPS (LC)	0.540	0.804	0.981	1.139
EPS growth (%)	na	48.9%	22.0%	16.1%
DPS (LC)	0.27	0.40	0.49	0.57
BVPS (LC)	3.25	3.68	4.17	4.74
Operating cash flow (LC mn)	2,838	3,061	3,482	4,237
Free cash flow (LC mn)	968	1,390	1,904	2,559
Interest cover (x)	50	54	104	228
Net margin (%)	18.4%	23.9%	24.4%	25.3%
Sales/assets (X)	0.54	0.58	0.63	0.63
Debt/equity (%)	47.4%	42.9%	37.8%	33.3%
Net debt/equity (%)	37.2%	28.6%	22.5%	15.4%
ROE (%)	17%	23%	25%	26%

	FY15	FY16E	FY17E	FY18E
Auto glass capacity (m)	16.6	17.4	18.3	19.2
Float glass capacity (mn tonnes)	5.1	5.8	5.8	6.1
Float glass price (HK$/ton)	1,379	1,517	1,669	1,753

Source: Company and J.P. Morgan estimates.

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

Source: Company and J.P. Morgan estimates.

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Source: Bloomberg data

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Y t D (Dn	Y	Y	Y	Y	Y	Y
Turnover	13,059	15,603	12,980	15,050	0.6%	3.7%
Gross profit	4,493	5,354	4,356	5,048	3.2%	6.1%
EBIT	2,857	3,461	2,730	3,226	4.6%	7.3%
Net profit	3,119	3,806	3,011	3,603	3.7%	9.0%
EPS (HKD)	0.80	0.98	0.78	0.93	3.7%	9.0%
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Gross margin	34.4%	34.3%	33.6%	33.5%	0.9%	0.8%

Source: J.P. Morgan estimates

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Automobile glass	3,287	3,593	3,786	3,932	4,323	4,540
YoY	6.8%	9.3%	5.4%	3.9%	10.0%	5.0%
% of total	33.1%	33.1%	33.0%	30.2%	28.0%	26.4%
Construction glass	2,155	2,556	2,652	2,895	3,912	4,074
YoY	36.9%	18.6%	3.8%	9.2%	35.1%	4.1%
% of total	21.7%	23.5%	23.1%	22.2%	25.3%	23.7%
Float glass	4,494	4,269	4,671	5,733	6,306	7,022
YoY	18.9%	-5.0%	9.4%	22.7%	10.0%	11.4%
% of total	45.2%	39.3%	40.8%	44.0%	40.8%	40.9%
PV glass	0	0	0	0	0	0
YoY	45.2%	39.3%	40.8%	44.0%	40.8%	40.9%
% 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%	3.6%	5.9%	8.9%
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Source: Company data, J.P. Morgan estimates

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YoY change (%)	1.5%	9.3%	5.5%	14.0%	19.5%	11.9%
Cost of Goods Sold	(6,799)	(8,127)	(8,328)	(8,565)	(10,249)	(11,257)
YoY change (%)	-7.0%	19.5%	2.5%	2.9%	19.7%	9.8%
Gross Profit	3,137	2,734	3,132	4,493	5,354	6,196
YoY change (%)	26.7%	-12.9%	14.6%	43.5%	19.2%	15.7%
Gross Margin	31.6%	25.2%	27.3%	34.4%	34.3%	35.5%
SGA	(1,251)	(1,638)	(1,615)	(1,878)	(2,159)	(2,323)
YoY change (%)	4.5%	30.9%	-1.4%	16.3%	15.0%	7.6%
Other Income/(Expenses)	326	178	215	241	265	264
Operating profit	2,212	1,274	1,733	2,857	3,461	4,136
D						0
EBITDA margin	28.7%	17.4%	20.2%	28.0%	28.1%	29.2%
Depreciation & Amortization	(639)	(612)	(580)	(804)	(929)	(964)
YoY change (%)	9.5%	-4.3%	-5.2%	38.6%	15.6%	3.8%
EBIT margin	22.3%	11.7%	15.1%	21.9%	22.2%	23.7%
Net Interest Expense	(60)	(38)	(50)	(68)	(42)	(22)
Exceptional item	1,453	220	379	0	0	0
Associates	21	138	317	830	997	1,013
Gains/losses	0	0	0	0	0	0
Net Income Before Taxes	3,627	1,594	2,379	3,619	4,416	5,127
YoY change (%)	159.5%	-56.1%	49.3%	52.1%	22.0%	16.1%
Tax	(381)	(228)	(266)	(499)	(610)	(708)
Effective Tax rate	17.5%	16.6%	13.3%	13.8%	13.8%	13.8%
Minority Interests	1	0	0	0	0	0
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YoY change (%)	172.9%	-36.1%	54.8%	47.6%	22.0%	16.1%
Net margin	32.7%	12.6%	18.4%	23.9%	24.4%	25.3%

Source: Company data, J.P. Morgan estimates

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Y D (d	0	0	0	0	0	0
EBIT	2,212	1,274	1,733	2,857	3,461	4,136
Depreciation and Amortization	639	644	795	804	929	964
Working Capital Changes	129	60	539	(334)	(408)	(254)
Tax Paid	(209)	(381)	(228)	(266)	(499)	(610)
Cash Flow From Operations	2,772	1,598	2,838	3,061	3,482	4,237
Capital expenditures	(2,913)	(1,715)	(1,914)	(1,568)	(1,444)	(1,518)
Investments and others	(208)	32	243	87	129	125
Net interest	(60)	(38)	(50)	(68)	(42)	(22)
Cash Flow from Investing	(3,181)	(1,720)	(1,721)	(1,549)	(1,358)	(1,416)
	(0	(				
Dividends	(834)	(902)	(608)	(1,299)	(1,731)	(2,056)
Common issue	916	(3)	1	0	0	0
Other Financing	688	833	(18)	531	49	36
Contribution from owner	0	(17)	(25)	0	0	0
Cash Flow from financing	770	(89)	(650)	(767)	(1,682)	(2,020)
Change in cash	338	(195)	467	744	442	800
Cash beginning	703	1,042	831	1,298	2,042	2,484
Foreign exchange changes	1	(17)	0	0	0	0
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Source: Company data, J.P. Morgan estimates

Investment Thesis a lua tion and isks

(Overweight; Price Target: HK$9.30)

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s,y c rm ll D	Y	Y	Y	Y	Y
Revenues	10,861	11,460	13,059	15,603	17,453
% change Y/Y	9.3%	5.5%	14.0%	19.5%	11.9%
Gross Profit	2,734	3,132	4,493	5,354	6,196
% change Y/Y	(12.9%)	14.6%	43.5%	19.2%	15.7%
EBITDA	1,918	2,528	3,661	4,390	5,101
% change Y/Y	(32.7%)	31.8%	44.8%	19.9%	16.2%
EBIT	1,274	1,733	2,857	3,461	4,136
% change Y/Y	(42.4%)	36.0%	64.9%	21.1%	19.5%
EBIT Margin	11.7%	15.1%	21.9%	22.2%	23.7%
Net Interest	(38)	(50)	(68)	(42)	(22)
Earnings before tax	1,594	2,379	3,619	4,416	5,127
% change Y/Y	(56.1%)	49.3%	52.1%	22.0%	16.1%
Tax	(228)	(266)	(499)	(610)	(708)
as % of EBT	14.3%	11.2%	13.8%	13.8%	13.8%
Net income (reported)	1,365	2,113	3,119	3,806	4,419
% change Y/Y	(57.9%)	54.8%	47.6%	22.0%	16.1%
Shares outstanding	3,915	3,915	3,881	3,881	3,881
EPS (reported)	0.35	0.54	0.80	0.98	1.14
% change Y/Y	(58.9%)	54.8%	48.9%	22.0%	16.1%

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s,y c rm ll D	Y	Y	Y	Y	Y
EBIT	1,274	1,733	2,857	3,461	4,136
Depr. & amortization	644	795	804	929	964
Change in working capital	60	539	(334)	(408)	(254)
Taxes	(381)	(228)	(266)	(499)	(610)
Cash flow from operations	1,598	2,838	3,061	3,482	4,237
Capex	(1,723)	(1,914)	(1,730)	(1,615)	(1,698)
Net Interest	(38)	(50)	(68)	(42)	(22)
Other	41	95	249	299	304
Free cash flow	(93)	968	1,390	1,904	2,559
Equity raised/(repaid)	(3)	1	0	0	0
Debt raised/(repaid)	833	(18)	531	49	36
Other	(17)	(25)	0	0	0
Dividends paid	(902)	(608)	(1,299)	(1,731)	(2,056)
Beginning cash	1,042	831	1,298	2,042	2,484
Ending cash	831	1,298	2,042	2,484	3,285
DPS	0.15	0.27	0.40	0.49	0.57

s,y c rm ll D	Y	Y	Y	Y	Y
Cash and cash equivalents	831	1,298	2,042	2,484	3,285
Accounts receivable	2,487	2,381	2,714	3,242	3,627
Inventories	1,478	1,223	1,393	1,665	1,862
Others	8	93	63	790	1,508
Current assets	4,805	4,995	6,211	8,181	10,281
LT investments	4,936	3,249	3,412	3,582	3,761
Net fixed assets	11,293	13,177	13,941	14,456	15,010
Total Assets	21,034	21,422	23,564	26,219	29,053
Liabilities					
Short-term loans	2,609	2,514	2,219	2,219	2,219
Payables	724	740	843	1,007	1,127
Others	1,468	1,705	2,054	2,593	3,062
Total current liabilities	4,801	4,959	5,116	5,820	6,408
Long-term debt	3,483	3,514	3,908	3,908	3,908
Other liabilities	414	223	254	303	339
Total Liabilities	8,698	8,696	9,278	10,030	10,654
Shareholders' equity	12,333	12,718	14,278	16,181	18,391
BVPS	3.15	3.25	3.68	4.17	4.74

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s,y c rm ll D	Y	Y	Y	Y	Y
Gross margin	25.2%	27.3%	34.4%	34.3%	35.5%
EBITDA margin	17.7%	22.1%	28.0%	28.1%	29.2%
Operating margin	11.7%	15.1%	21.9%	22.2%	23.7%
Net margin	12.6%	18.4%	23.9%	24.4%	25.3%
Sales per share growth	6.8%	5.5%	14.9%	19.5%	11.9%
Sales growth	9.3%	5.5%	14.0%	19.5%	11.9%
Net profit growth	(57.9%)	54.8%	47.6%	22.0%	16.1%
EPS growth	(58.9%)	54.8%	48.9%	22.0%	16.1%
Interest coverage (x)	50.4	50.3	53.6	103.9	227.9
Net debt to equity	42.7%	37.2%	28.6%	22.5%	15.4%
Working Capital to Sales	0.0	0.0	0.1	0.2	0.2
Sales/assets	0.5	0.5	0.6	0.6	0.6
Assets/equity	1.7	1.7	1.7	1.6	1.6
ROE	11.1%	16.9%	23.1%	25.0%	25.6%
ROCE	6.1%	8.3%	12.6%	14.0%	15.2%

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

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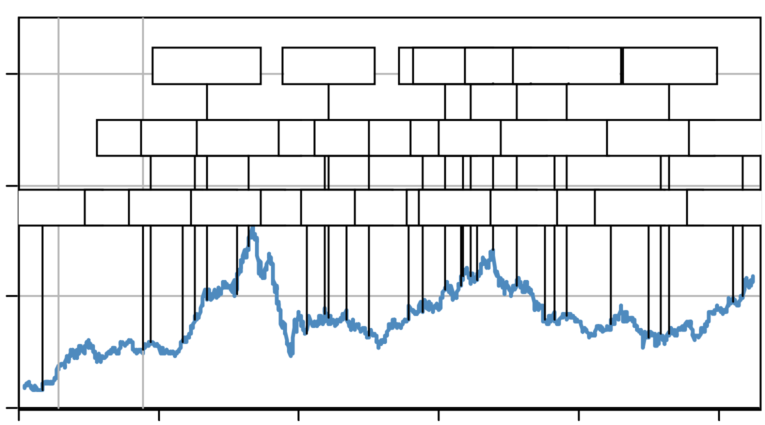

03-Feb-09	1.00	2.25
0 -Mar-10	3.16	.12
31-Mar-10	3.59	5.50
02-Aug-10	3.51	5.70
20-Sep-10	.76	6.80
09- ov-10	5.80	8.80
01-Mar-11	6.13	9.00
20-Apr-11	8.77	11.00
28- ov-11	.03	6.00
09-Feb-12	5.01	5.10
27-Feb-12	.80	.60
07-May-12	.78	5.50
01-Aug-12	3.92	5.10
31- ec-12	.78	5.90
28-Feb-13	5.16	6.90
22-May-13	6.30	8.00
23-Jul-13	6.58	8.70
31-Jul-13	7.13	10.00
0 -Sep-13	7.07	10.50
26-Sep-13	6.92	10.90
25- ov-13	8.53	9.80
26-Feb-1	6.56	10.00

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20 Jun-1	.76	650
2 Jul-1	.76	5.70
15-Sep-1	.92	6.70
02-Mar-15	.55	6.10
28 Jul-15	3.80	5.50
10-Sep-15	3.95	5.20
15- ct-15	3.97	6.00
17 Jun-16	5.67	7.00
02-Aug-16	6.0	8.20

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