

Equity Research | China | Glass

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## A bargain with strong growth

- We have positive takeaways from our latest company meeting. We expect Xinyi Glass to benefit from the Malaysia's float glass project in terms of volume growth and margin expansion over the next two years.
- With China float glass prices holding up well YTD, we see a healthy demand-supply equilibrium in the domestic float glass market.
- We see the Malaysia project likely a re-rating catalyst for Xinyi Glass, which prompts us to raise our price target to HKD8.50 (from HKD8.0), based on 2.2x FY17E PBR (prev. 2.0x). Maintain Buy.

### Malaysia project to add to volume growth and drive margin expansion.

Given that the Malaysia project has commenced mass production earlier this month, we estimate the project will lead to a 5% YoY growth in float glass sales volume in FY17E. According to the company's development plan, it targets to add two float glass production lines, with a total designated capacity equivalent to 10% of the group's capacity, and scheduled to commence operation by mid-2018. Since float glass sales from Malaysia could yield higher margins due to lower cost of production as compared to the current market in China, we believe the Malaysia project would provide earnings growth prospects over the medium-term.

**China's domestic float glass market to remain balanced.** Although the market is concerned that glass demand may be adversely affected by the tightening policies in the property sector, but based on past experience, there is normally a time lag of a few quarters between policy introduction and actual implementation. Moreover, we think this round of tightening targets specific areas only and it is less scalable than 2011. Besides, we believe the supply discipline among existing producers has improved, as China's float glass daily melting capacity has been capped at 155k tons. Thus, we are confident that the market dynamics of China's domestic glass industry will continue to improve.

**Stable cost outlook.** The price of soda ash, which makes up approximately 20% of the company's float glass production cost, has retreated 25% from the year-high back in January. Meanwhile, we foresee the price of gas, which account for 30% of Xinyi's float glass production cost, to potentially edge down further in the near term amid a downtrend in global energy prices.

**Maintain Buy.** Trading at 8.0x FY17E PER and 6.1% dividend yield, we foresee further re-rating opportunities ahead on the back of its Malaysia project. Hence, we have raised our target multiple to 2.2x FY17E PBR, a 10% premium to our prior multiple of 2.0x, which we believe is justifiable in view of Xinyi Glass' stable margin performance and the growth prospects brought about by its Malaysia operation. Accordingly, we have raised our price target to HKD8.50 (from HKD8.0), and maintain Buy.

## Xinyi Glass (868 HK)

### Buy

(unchanged)

<b>Price Target</b>	<b>HK\$8.5</b>
(Revision)	(+6.2%)
(upside)	(15.8%)

EPS	2017E	2018E
revision	(-0.9%)	(+0.7%)

Close price	HKD7.34
Market cap.	HKD29,350 mn
Free float	46.3%
52-week range	HKD4.99 – 7.71
3-mth ave. T/O	HKD75.0 mn

Price as of 21 Jun 2017

Stock rel HSI performance (%)


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**Figure 1: Xinyi Glass' key assumptions**

Turnover	Unit	2014	2015	2016	2017E	2018E	2019E
Float glass	HKD mn	4,712	5,022	6,510	7,278	8,384	8,857
Automobile glass	HKD mn	3,593	3,787	3,748	3,786	3,842	3,842
Construction glass	HKD mn	2,556	2,651	2,590	3,297	3,297	3,297
<b>Total</b>	<b>HKD mn</b>	<b>10,861</b>	<b>11,460</b>	<b>12,848</b>	<b>14,361</b>	<b>15,522</b>	<b>15,995</b>
<b>% Split</b>							
Float glass	%	43.4	43.8	50.7	50.7	54.0	55.4
Automobile glass	%	33.1	33.0	29.2	26.4	24.8	24.0
Construction glass	%	23.5	23.1	20.2	23.0	21.2	20.6
<b>Total</b>	<b>%</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
<b>Sales volume</b>							
Float glass	tons	2,818	3,387	3,401	4,150	4,529	4,784
Automobile glass	piece	12,900	13,800	13,600	13,736	13,940	13,940
Construction glass	sqm	19,300	21,800	27,750	35,320	35,320	35,320
<b>Yo Y Change</b>							
Float glass	%	(16.2)	20.2	0.4	22.0	9.1	5.6
Automobile glass	%	14.1	7.0	(14)	10	15	-
Construction glass	%	30.4	13.0	27.3	27.3	-	-
<b>Unit price</b>							
Float glass	HKD/ton	1,672	1,483	1,914	1,754	1,851	1,851
Automobile glass	HKD/piece	279	274	276	276	276	276
Construction glass	HKD/sqm	132	122	93	93	93	93
<b>Yo Y Change</b>							
Float glass	%	25.1	(11.3)	29.1	(8.4)	5.6	-
Automobile glass	%	(4.2)	(15)	0.4	-	-	-
Construction glass	%	(9.0)	(8.1)	(23.3)	-	-	-
<b>Gross profit</b>							
Float glass	HKD mn	329	556	1,791	2,038	2,347	2,480
Automobile glass	HKD mn	1,502	1,679	1,836	1,855	1,883	1,883
Construction glass	HKD mn	902	898	1,032	1,319	1,319	1,319
<b>Total</b>	<b>HKD mn</b>	<b>2,733</b>	<b>3,133</b>	<b>4,659</b>	<b>5,212</b>	<b>5,549</b>	<b>5,681</b>
<b>Yo Y Change</b>							
Float glass	%	(61.4)	68.7	222.3	13.8	15.2	5.6
Automobile glass	%	5.5	11.8	9.3	10	15	-
Construction glass	%	5.0	(0.5)	15.0	27.7	-	-
<b>Total</b>	<b>%</b>	<b>(12.9)</b>	<b>14.6</b>	<b>48.7</b>	<b>11.9</b>	<b>6.5</b>	<b>2.4</b>
<b>GPM</b>							
Float glass	%	7.0	11.1	27.5	28.0	28.0	28.0
Automobile glass	%	41.8	44.3	49.0	49.0	49.0	49.0
Construction glass	%	35.3	33.9	39.9	40.0	40.0	40.0
<b>Blended</b>	<b>%</b>	<b>25.2</b>	<b>27.3</b>	<b>36.3</b>	<b>36.3</b>	<b>35.7</b>	<b>35.5</b>

Source: Company, CSCI Research estimates

**Figure 2: Xinyi Glass**

Income statement (HKD mn)						Cash flow statement (HKD mn)					
Year end: Dec	2015	2016	2017E	2018E	2019E	Year end: Dec	2015	2016	2017E	2018E	2019E
Revenue	11,460	12,848	14,361	15,522	15,995	EBIT	2,430	3,900	4,360	4,685	4,801
COGS	(8,328)	(8,189)	(9,149)	(9,974)	(10,314)	Depreciation & amortisation	795	827	790	875	957
Gross profit	3,133	4,659	5,212	5,549	5,681	Net interest	50	77	86	97	83
Selling expenses	(680)	(620)	(693)	(749)	(772)	Taxes paid	(266)	(607)	(684)	(734)	(755)
General and administrative	(935)	(1,202)	(1,344)	(1,453)	(1,497)	Changes in working capital	375	(218)	(216)	(121)	(49)
Other opex	92	1,063	1,185	1,338	1,388	Others	(747)	(459)	(172)	(184)	(165)
<b>EBIT</b>	<b>2,430</b>	<b>3,900</b>	<b>4,360</b>	<b>4,685</b>	<b>4,801</b>	<b>Cash flow from operations</b>	<b>2,637</b>	<b>3,520</b>	<b>4,163</b>	<b>4,608</b>	<b>4,871</b>
Interest income	12	84	94	92	116	Capex	(1,834)	(1,322)	(3,966)	(2,500)	(2,500)
Interest expense	(163)	(161)	(180)	(189)	(199)	Acquisitions	(130)	(1,232)	-	-	-
JVs and associates	317	563	679	791	825	Disposals	292	18	-	-	-
<b>Pretax profit</b>	<b>2,380</b>	<b>3,823</b>	<b>4,274</b>	<b>4,588</b>	<b>4,718</b>	Others	152	256	-	-	-
Taxation	(266)	(607)	(684)	(734)	(755)	<b>Cash flow from investing</b>	<b>(1,520)</b>	<b>(2,280)</b>	<b>(3,966)</b>	<b>(2,500)</b>	<b>(2,500)</b>
Minority interests	(0)	(3)	(3)	(3)	(3)	Dividends	(608)	(1,321)	(1,747)	(1,875)	(1,929)
<b>Net profit</b>	<b>2,113</b>	<b>3,213</b>	<b>3,587</b>	<b>3,851</b>	<b>3,960</b>	Issue of shares	-	-	-	-	-
Net profit (adjusted)	2,113	3,213	3,587	3,851	3,960	Change in debt	(18)	1,611	500	500	500
Depreciation & Amortization	(795)	(827)	(790)	(875)	(957)	Others	1	(66)	-	-	-
<b>EBITDA</b>	<b>3,225</b>	<b>4,727</b>	<b>5,150</b>	<b>5,560</b>	<b>5,757</b>	<b>Cash flow from financing</b>	<b>(625)</b>	<b>225</b>	<b>(1,247)</b>	<b>(1,375)</b>	<b>(1,429)</b>
Basic EPS (HKD)	0.54	0.82	0.91	0.98	1.01	<b>Change in cash</b>	<b>492</b>	<b>1,465</b>	<b>(1,049)</b>	<b>733</b>	<b>942</b>
Diluted EPS (HKD)	0.54	0.82	0.91	0.98	1.01	Free cash flow	802	2,198	197	2,108	2,371
DPS (HKD)	0.26	0.40	0.45	0.48	0.49						

  

Balance sheet (HKD mn)						Key ratios					
Year end: Dec	2015	2016	2017E	2018E	2019E	Year end: Dec	2015	2016	2017E	2018E	2019E
Cash	1,298	2,763	1,714	2,446	3,389	<b>Operating ratios</b>					
Short term investments	-	-	-	-	-	Gross margin	27.3	36.3	36.3	35.7	35.5
Accounts receivables	2,381	2,377	2,659	2,874	2,962	EBITDA margin (%)	28.1	36.8	35.9	35.8	36.0
Inventory	1,223	1,321	1,421	1,549	1,602	Effective tax rate (%)	112	15.9	16.0	16.0	16.0
Other current assets	93	76	76	76	76	Revenue growth (%)	-	12.1	118	8.1	3.0
<b>Total current assets</b>	<b>4,995</b>	<b>6,537</b>	<b>5,870</b>	<b>6,945</b>	<b>8,028</b>	Net income growth (%)	-	52.1	116	7.4	2.8
PP&E	11,971	11,831	15,007	16,631	18,175	EPS growth adj (%)	-	52.1	116	7.4	2.8
Intangible Assets	1,453	1,801	1,801	1,801	1,801	DPS growth (%)	-	52.1	116	7.4	2.8
Total investments	2,972	3,804	3,804	3,804	3,804						
Other long term assets	30	50	50	50	50	<b>Efficiency ratios</b>					
<b>Total long term assets</b>	<b>16,426</b>	<b>17,486</b>	<b>20,662</b>	<b>22,287</b>	<b>23,830</b>	ROE (%)	16.6	24.4	23.9	22.7	20.8
<b>TOTAL ASSETS</b>	<b>21,422</b>	<b>24,022</b>	<b>26,532</b>	<b>29,232</b>	<b>31,858</b>	ROCE (%)	14.8	21.6	21.6	20.9	19.4
Short term debt	2,514	3,165	3,372	3,578	3,784	Asset turnover (x)	0.5	0.5	0.5	0.5	0.5
Accounts payables	2,112	2,297	2,463	2,685	2,777	Op cash / EBIT (x)	1.1	0.9	1.0	1.0	1.0
Other current liabilities	333	538	538	538	538	Depreciation / CAPEX (x)	0.4	0.6	0.2	0.4	0.4
<b>Total current liabilities</b>	<b>4,959</b>	<b>6,000</b>	<b>6,373</b>	<b>6,801</b>	<b>7,099</b>	Accounts receivable days	77.5	67.6	64.0	65.1	66.6
Long term debt	3,514	4,509	4,803	5,097	5,390	Accounts payable days	89.6	98.3	94.9	94.2	96.6
Deferred tax	169	218	218	218	218						
Bonds payable	-	-	-	-	-	<b>Leverage ratios</b>					
Other long term liabilities	63	48	48	48	48	Net gearing (%)	37.2	37.3	43.0	36.6	30.4
<b>Total long term liabilities</b>	<b>3,737</b>	<b>4,775</b>	<b>5,069</b>	<b>5,363</b>	<b>5,657</b>	Net debt / EBITDA (x)	15	10	13	11	10
<b>TOTAL LIABILITIES</b>	<b>8,696</b>	<b>10,775</b>	<b>11,442</b>	<b>12,164</b>	<b>12,755</b>	Interest cover (x)	48.4	50.8	50.6	48.3	58.0
Shareholders' funds	12,718	13,181	15,021	16,997	19,028	Current ratio (x)	10	1.1	0.9	1.0	1.1
Minority interests	7	66	69	71	74	<b>Valuation</b>					
<b>TOTAL LIAB AND EQUITY</b>	<b>21,422</b>	<b>24,022</b>	<b>26,532</b>	<b>29,232</b>	<b>31,858</b>	PER (x)	13.6	9.0	8.0	7.5	7.3
Net cash / (debt)	(4,730)	(4,911)	(6,461)	(6,228)	(5,786)	EV/EBITDA (x)	10.5	7.2	6.8	6.3	6.0
						PBR (x)	2.3	2.2	1.9	1.7	1.5
						Dividend yield (x)	3.6	5.4	6.1	6.5	6.7

Source: Company, Bloomberg, CSCI Research estimates



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## Company Rating Definition

The Benchmark: Hong Kong Hang Seng Index; Time Horizon: 12 months

<b>Buy</b>	12-month absolute total return: $\geq 10\%$
<b>Hold</b>	12-month absolute total return: $> -10\%$ but $< 10\%$
<b>Sell</b>	12-month absolute total return: $\leq -10\%$

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