



## XYG (868.HK)

## FY10F Bottom-line Set To Surge, 'Buy'

Company Report

Rating: **Buy**→

Price : **HK\$6.08**

TP : **HK\$8.60**↑

Upside: **41%**

2 Feb 2010

### Event

Wuhu Plant Visit

EPS Change

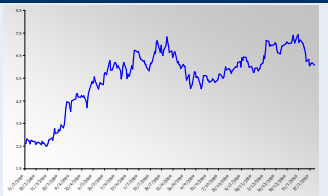
TP Change

### Stock Data (HK\$)

52 w Hi	7.61
52 w Lo	1.96
Mk Cap (HK\$ m)	10,780.2
Issued shares (m)	1,688.1
Daily Vol (m)	6.8
1M % chg	-13.5
Ytd % chg	-13.5
50 d MA	6.7
200 d MA	6.1
14 d RSI	36.1

Source: Bloomberg

### 1 yr price chart



Source: Bloomberg

### Event

- **Wuhu Plant Visit Notes.** Key take-aways from the trip are: natural gas replaced heavy oil as the energy supply; OEM now 1m cases per year, another 1m cases new capacity scheduled for commercial operation in 3Q 2010; 700t/d and 900t/d lines into operation in 2Q10.
- **Revising FY10F estimates:** We adjust: (1) FY10F's top-line figure upwards by 4.3% to HK\$6.54bn; (2) consolidated GM% estimates slightly lifted by 1ppt to 31.1% as we upgrade float glasses' GM% by 3ppt; (3) bottom line then was increased from previously HK\$1.23bn to HK\$1.36bn or EPS of HK\$0.710 to HK\$0.782.
- **Bull on PRC car sales growth.** We expect the passenger car sales in 2010 to experience growth between 15-20% YoY while we estimate the PRC's total auto sales to top 15m units.
- **Soda Ash recovering quickly but not greatly concerned.** We are less encouraged to raise our GM% further as input costs have been increasing. However, we are less concerned with XYG due to the use of gas which has more stable price movement and 10-15% cheaper than using fuels.
- **11x PE on FY10F EPS target.** We maintain 'Buy' on XYG with upgraded TP of HK\$8.60, representing 11x PE on FY10F's EPS of HK\$0.782, supported by our DCF model with modest growth assumptions. We like XYG's aggressive expansion into Auto Glass OEM market, pioneering the TCO glass lines in PRC and its expansion model focusing on Bohai Bay region, Yangtze River Delta and Pearl River Delta.

### Valuation Table

YE Dec (HK\$ m)	FY07	FY08	FY09F	FY10F	FY11F
Turnover	2,774.6	3,894.3	4,119.7	6,543.8	8,683.0
Net profit	670.9	709.2	612.6	1,360.3	1,689.3
Basic EPS (HK\$)	0.411	0.421	0.352	0.782	0.971
Growth %	67.1%	2.3%	-16.3%	122.1%	24.2%
PER (X)	14.8	14.5	17.3	7.8	6.3
PEG(X)	0.2	6.2	(1.1)	0.1	0.3
FD PER(X)	15.0	14.6	17.3	7.8	6.3
DPS (HK\$)	0.182	0.200	0.159	0.356	0.441
Yield (%)	3.0%	3.3%	2.6%	5.8%	7.3%
BVPS (HK\$)	2.347	2.601	2.754	3.281	3.947
P/B (X)	2.6	2.3	2.2	1.9	1.5

Source: Company, BOCOM Int'l

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## 1. Wuhu Plant Visit Notes

**Touring largest XYG plant.** We went to XYG's largest manufacturing base last Friday, which is 30% larger than the existing Dongguan plant. Key take-aways from the trip are:

Performance Improvement:

- Natural gas replaced heavy oil as the energy supply; Cost saving 10-15% compared to using heavy oil.
- We anticipate consolidated GM% improvement of c.2 ppts.

Wuhu Plant Products - Auto Glass:

- OEM now 1m cases per year, another 1m cases new capacity scheduled for commercial operation in 3Q 2010.
- Customers were mainly Chinese auto manufacturers: BYD, Dongfeng (东风), Chery (奇瑞) etc.

Wuhu Plant Products - Low-E Glass:

- German coating technology in use is more advanced compared to local competitors.
- One of the Guangzhou 16th Asian Game main stadiums is using XYG's Low-E Glass.
- Some provincial government (such as Fujian) has made it compulsory to use Low-E glass for public construction projects.

Financial:

- Management confident that 2H09 results to bounce back from 1H09 with improved margins and higher revenue.
- Current high quality float glass is selling RMB2,400/t plus, 2Q09 was only RMB1,400/t.

American Law Provision:

- We made full amount provision, c.HK\$85.3m in FY09F, i.e. HK\$0.05 per share EPS downward impact.
- Senior management confident about the case to be resolved fully.

FY10F outlook & Capacity Expansion:

- ASPs looking firm.
- TCO glass line will be putting into commercial operation in 2H09, which has a GM% over 50%.
- 700t/d and 900t/d melting capacity float glass lines will be put into operation in 2Q10 in Wuhu plant.

Overall key highlights of annual capacity expansion plans:

OEM Auto Glass: 2010 up 142% YoY

Low-E Glass: 2010 up 33% YoY

TCO: new in 2010 with 2m sqm

Float Glass: 2010 up 26% YoY

PV Glass: 2010 up 88% YoY

**Fig 1: Visit photos**

Wuhu plant's own 5,000t pier for raw material unload



700t/d and 900t/d plants, under construction



500t/d plant with downstream low-E glass and PV glass lines



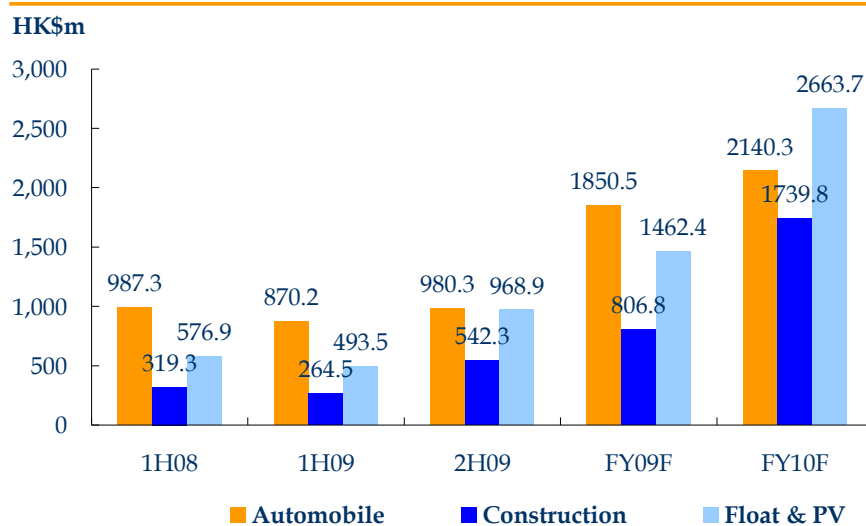
Source BOCOM Int'l

## 2. Revising FY10F estimates

**Upgrade FY10F's estimates.** We now upgrade our estimates for FY10F due to: (1) better than expected recovery of ASPs especially coming from float glass (currently up c.100% YoY compared to 1Q09); (2) better than expected GM% recovery; (3) expansion becoming faster than our previous anticipation especially on the new Jiangmen plant (600t/d line and 2x 900t/d lines operating in 4Q10).

Overall, we adjust: (1) FY10F's top-line figure upwards by 4.3% to HK\$6.54bn as ASPs are lifted; (2) consolidated GM% estimates slightly lifted by 1ppt to 31.1% as we upgrade float glasses' GM% by 3ppt; (3) bottom line then is increased from previously HK\$1.23bn to HK\$1.36bn or EPS of HK\$0.710 to HK\$0.782.

**Fig 2: Product sales expected to be recovered in 2H09, leading to great advancement in FY10F**



Source: CEIC BOCOM Int'l

### 3. Key Assumptions

Revenue Assumption BreakDown					
	FY07	FY08	FY09F	FY10F	FY11F
<b>Float &amp; PV Glass</b>					
Y/E Output (m t)	0.51	0.97	1.00	1.56	2.38
Sales Volume (m t)	0.46	0.82	0.85	1.19	1.82
ASP (HK\$/t)	1,078.7	1,557.6	1,713.4	1,970.4	1,970.4
<u>Total Turnover (HK\$m)</u>	491.9	1,279.2	1,462.4	2,351.3	3,590.0
<b>Automobile</b>					
Y/E Output (m pcs)	9.20	10.70	11.20	12.70	13.70
Sales Volume (m pcs)	5.15	6.42	6.72	7.62	8.22
ASP (HK\$/pcs)	333.2	306.0	275.4	280.9	286.5
<u>Total Turnover (HK\$m)</u>	1,716.8	1,964.3	1,850.5	2,140.3	2,355.0
<b>Construction</b>					
Y/E Output (m sq.m)	2.00	3.00	4.38	9.25	11.50
Sales Volume (m sq.m)	1.12	1.68	2.45	5.18	6.44
ASP (HK\$/sq.m)	505.3	387.4	329.3	335.9	342.6
<u>Total Turnover (HK\$m)</u>	565.9	650.8	806.8	1,739.8	2,206.3
<b>TCO</b>					
Y/E Output (m sq.m)	0.00	0.00	0.00	2.06	3.43
Sales Volume (m sq.m)	0.00	0.00	0.00	1.56	2.61
ASP (HK\$/sq.m)	0.0	0.0	0.0	200.0	204.0
<u>Total Turnover</u>	0.0	0.0	0.0	312.4	531.8
<u>Consolidated Total</u>	2,774.6	3,894.3	4,119.7	6,543.8	8,683.0

Gross Margin Assumption BreakDown					
	FY07	FY08	FY09F	FY10F	FY11F
<b>Float &amp; PV Glass GM</b>					
Float & PV Glass GM	33.7%	20.5%	22.6%	31.6%	34.7%
Float Glass GP (HK\$ m)	165.8	262.4	330.0	742.8	1247.5
<b>Automobile Glass GM</b>					
Automobile Glass GM	41.4%	38.2%	36.3%	36.3%	36.3%
Automobile GP (HK\$ m)	710.8	749.9	671.1	776.2	854.1
<b>Construction Glass GM</b>					
Construction Glass GM	34.7%	30.5%	33.6%	33.6%	33.6%
Construction Glass GP (HK\$ m)	196.4	198.6	270.8	584.0	740.6

Source: Company, BOCOM Int'l

## 4. Financials

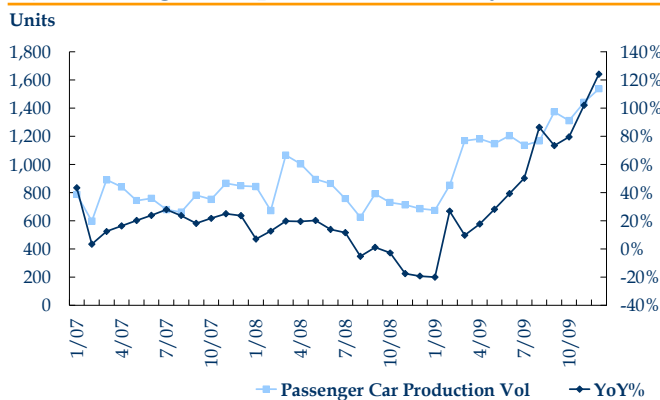
YE Dec (HK\$ m)	FY08	FY09F	FY10F	FY11F	YE Dec (HK\$ m)	FY08	FY09F	FY10F	FY11F
<b>Profit &amp; Loss</b>					<b>Cash Flow Statement</b>				
<b>Turnover</b>	<b>3,894.3</b>	<b>4,119.7</b>	<b>6,543.8</b>	<b>8,683.0</b>	Profit before tax	753.1	667.4	1,482.0	2,149.3
COGS	(2,683.4)	(2,847.7)	(4,440.7)	(5,840.8)	Interest income	(9.1)	(9.0)	(13.2)	0.0
Gross Profit	1,210.9	1,271.9	2,103.0	2,842.2	Finance Costs	24.0	25.0	25.3	22.3
Other Revenue	93.4	(42.1)	55.7	56.9	Depreciation	224.6	300.6	331.8	360.8
Distribution Expenses	(318.2)	(324.9)	(394.1)	(440.8)	Other changes in P&L	22.8	18.5	17.2	21.0
General & Admin expenses	(209.2)	(213.5)	(257.8)	(287.6)	change in working capital	242.6	(209.3)	(299.1)	(356.0)
Operating Profit	776.8	691.4	1,506.8	2,170.8	Tax paid	(34.2)	(29.1)	(56.7)	(181.2)
Associate and Others	0.3	0.9	0.6	0.8	<b>Operating cash flow</b>	<b>1,223.7</b>	<b>764.0</b>	<b>1,487.4</b>	<b>2,016.1</b>
Finance cost	(24.0)	(25.0)	(25.3)	(22.3)	Capex	(856.7)	(784.0)	(784.0)	(627.2)
Profit before taxation	753.1	667.4	1,482.0	2,149.3	Other investing CF	(95.0)	(63.9)	(83.6)	(83.5)
Taxation	(42.3)	(54.7)	(121.5)	(459.9)	<b>Investing cash flow</b>	<b>(951.7)</b>	<b>(847.9)</b>	<b>(867.6)</b>	<b>(710.7)</b>
MI	(1.6)	(0.1)	(0.1)	0.0	Net Borrowings Rasied (Paid)	508.2	46.7	17.5	(153.4)
<b>Net Profit</b>	<b>709.2</b>	<b>612.6</b>	<b>1,360.3</b>	<b>1,689.3</b>	Interest Paid	(56.1)	(25.0)	(25.3)	(22.3)
<b>Consolidated Balance Sheet</b>					<b>Financing cash flow</b>				
<b>Fixed Assets</b>					Other financing CF	(581.2)	203.8	(457.1)	(706.6)
PPE	4,334.8	4,450.9	4,839.1	5,054.3	<b>Financing cash flow</b>	<b>(129.1)</b>	<b>225.6</b>	<b>(464.9)</b>	<b>(882.3)</b>
Land use rights	280.9	300.5	321.6	344.1	<b>Net Cash Flow</b>	<b>143.0</b>	<b>141.6</b>	<b>154.9</b>	<b>423.1</b>
Other fixed assets	117.4	101.5	101.5	101.5	Cash balance at year begin	309.5	435.7	658.3	935.6
<b>Current Asset</b>					Exchange Effect	(16.8)	81.0	122.4	174.0
Cash balance	435.7	658.3	935.6	1,532.7	Cash balance at year end	435.7	658.3	935.6	1,532.7
Inventories	612.1	625.6	975.5	1,283.1	<b>Key Ratios</b>				
A/C receivables	710.1	801.1	1,272.4	1,688.4	Gross margin (%)	31.1	30.9	32.1	32.7
Other current assets	6.9	12.3	12.5	11.0	Operating margin (%)	19.9	16.8	23.0	25.0
<b>Current Liabilities</b>					Net margin (%)	18.2	14.9	20.8	19.5
ST borrowings	722.4	750.4	760.9	669.0	ROE (%)	16.8	13.2	25.4	26.3
A/C payables	879.3	773.5	1,295.0	1,662.1	ROCE (%)	13.7	10.4	20.5	22.1
Other current liabilities	21.6	26.7	58.7	218.2	ROA (%)	12.0	9.1	17.7	18.3
<b>Long-term Liabilities</b>					Gearing	27.6%	25.7%	21.9%	16.0%
LT Loans	484.1	502.8	509.9	448.3	Net debt / equity	17.6%	12.2%	5.8%	Net Cash
Other LT liabilities	1.0	1.1	1.2	1.3	Interest cover (X)	32.3	27.7	59.5	97.5
<b>Net Asset</b>	<b>4,389.5</b>	<b>4,895.7</b>	<b>5,832.6</b>	<b>7,016.2</b>	Altman-Z-Score	4.9	5.0	4.9	5.0
Represented by:					Asset turnover	0.6	0.6	0.8	0.9
Share capital	1,998.0	1,998.0	1,998.0	1,998.0	Current ratio	1.1	1.4	1.5	1.8
Reserves	2,371.4	2,877.5	3,814.2	4,997.8	A/C rec turnover (days)	67	66	57	61
MI	20.2	20.3	20.4	20.4	A/C payable turnover (days)	97	104	78	87
	<b>4,389.5</b>	<b>4,895.7</b>	<b>5,832.6</b>	<b>7,016.2</b>	Inventory turnover days	75	78	65	70

Source: Company, BOCOM Int'l

## 5. Domestic Car Sales Upbeat

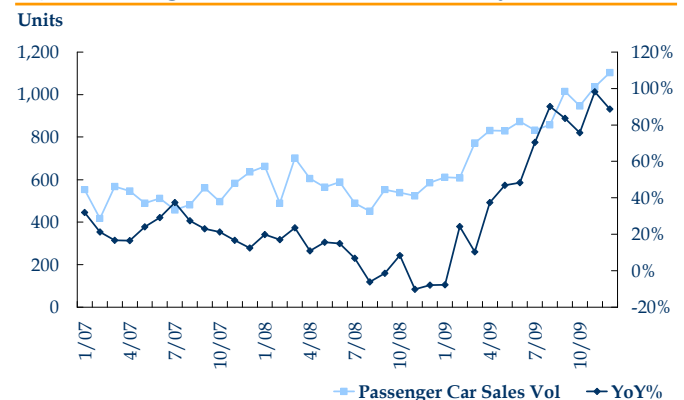
PRC passenger car market 15-20% growth expected. We expect the passenger car sales in 2010 to experience growth between 15-20% YoY while we estimate the PRC's total auto sales to top 15m units, i.e. 15% YoY growth on 2009. As the auto market retains its rapid double digit growth, and XYG aggressively enters the PRC Auto Glass OEM market, we remain optimistic on XYG's auto sector performance with stable ASP forecasts and GM% estimate although the overseas market lacks upward momentum.

Fig 3 Passenger Car prod volume mthly & YoY%



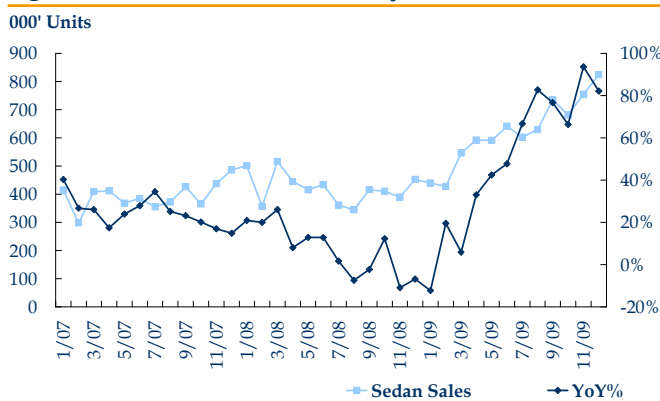
Source: CEIC, BOCOM Int'l

Fig 4 Passenger Car sales volume mthly & YoY%



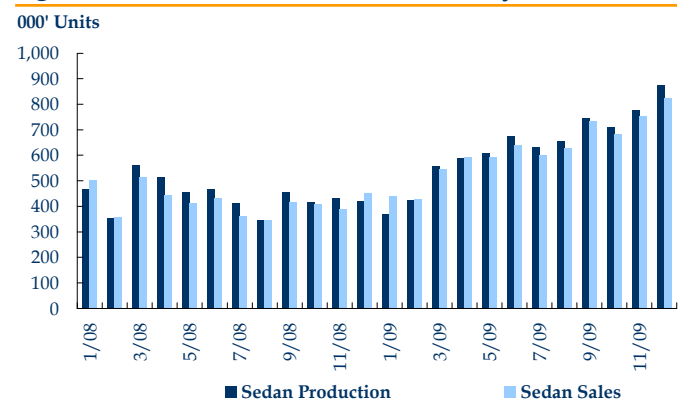
Source: CEIC, BOCOM Int'l

Fig 5 Sedan sales volume mthly & YoY%



Source: CEIC, BOCOM Int'l

Fig 6 Sedan Prod vs. Sedan Sales, mthly



Source: CEIC, BOCOM Int'l

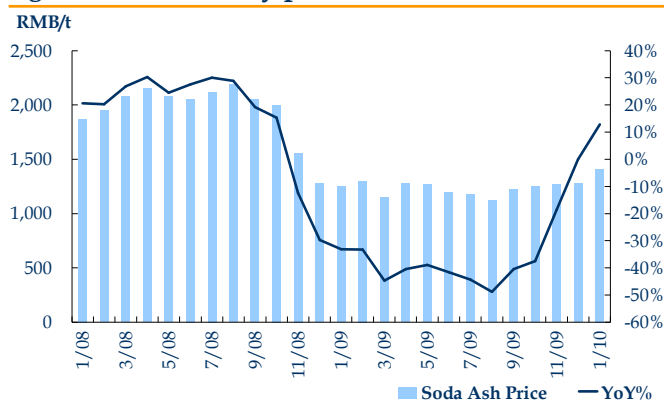


## 6. Input costs recovering

**Soda Ash recovering most quickly.** We are less encouraged to raise our GM% further as soda ash and heavy oil's prices have been increasing. We have also seen certain smaller manufactures reopening their closed lines as the demand for glasses recovered following the government RMB4tn stimulus package. As more players are coming back to the market, demand for raw material and energy will surge, and we expect those related prices to continue their advancement in 2010, biting into manufacture's GM%. **However, we are less concerned with XYG due to the use of gas which has more stable price movement and 10-15% cheaper than using fuels. 45% or more energy usage (35%+ of COGS) is expected to come from gas while the remaining stays with fuel.**

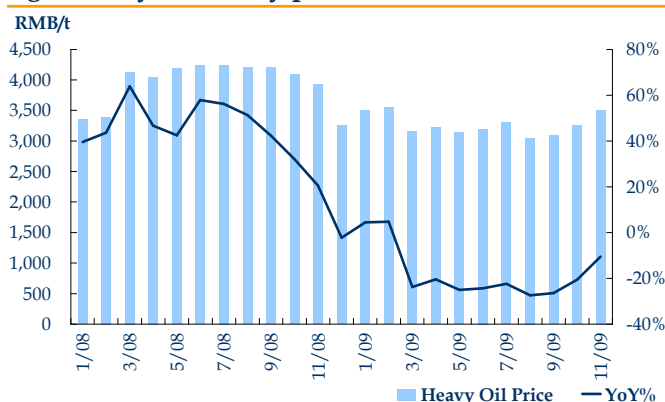
Due to heavy oil and soda ash's prices being low in the 2H09, we anticipate the 2H09's results will be improved greatly from the 1H09 results. Float glass's GM% could be improved as much as 15ppt caused by combined effects of lowered costs and recovered ASP (4Q09's prices doubling the 1Q09).

Fig 7 Soda Ash mthly prices



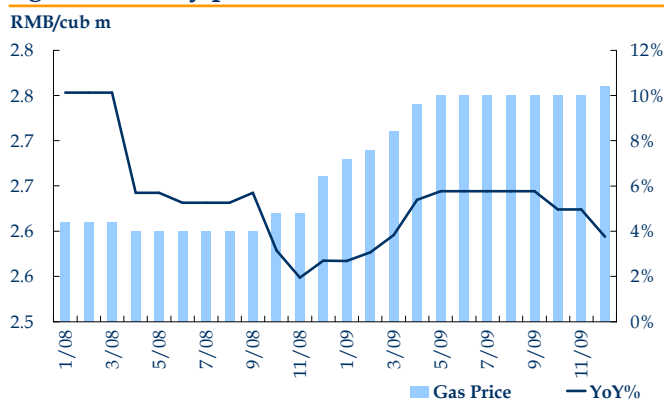
Source: CEIC, BOCOM Int'l

Fig 8 Heavy Oil mthly prices



Source: CEIC, BOCOM Int'l

Fig 9 Gas mthly prices



Source: CEIC, BOCOM Int'l

## 7. Investment Thesis & Valuation

We maintain 'Buy' on XYG with upgraded TP of HK\$8.60 from HK\$6.40. Buying points are: (1) leveraging to the future of TCO which XYG is the pioneer in the domestic glass industry, and the production line is expected to be running from 2H10; (2) XYG's huge after-market auto glass market shares in the overseas and its potentials in PRC as well as its future PRC OEM Auto Glass market growth; (3) FY10F's bottom-line likely to double from FY09 whose results will be released in Mar.

Our DCF model suggests a similar target of HK\$8.73 per share, representing P/E of 11X FY10F's EPS.

### Risk

Valuation upside risks mainly are: (1) GM% expanded larger than expected due to higher actual ASPs than expected if the government's crack down on obsolete capacity came out to be more aggressive than expected; (2) better than expected auto glass sales due to western country economy recovering better than expected.

Downside risks: (1) soda ash costs hiking more severe than expected; (2) expanded capacity further distorts the float glass supply demand picture causing more severe over-supply; (3) law suit in the US to have beyond expected damaging impacts such as more penalty or limiting XYG's exporting capability to the US.

### Company Description

Established in 1988, currently Xinyi Glass Holdings Ltd takes 20% of global automobile replacement glass market, and related exports have been ranked No.1 in China while possessing the leading coating technology from Germany for Low-E glass products. Its aftermarket automobile glass production capacity in FY07 reached 8.5m pieces. Xinyi Glass's business includes production and sale of automobile (50% of FY08 total turnover), construction (17% of FY08 total turnover), and float and PV glass products (33% of FY08 total turnover). The company has 4 manufacturing bases namely Shenzhen, Dongguan in Guangdong province, Wuhu in Anhui province and Tianjin. Shares have been listed on HKEX since Feb 2005.



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**Rating System**

**Company Rating**

Buy: Expect more than 20% upside in 12 months

LT Buy: Expect more than 20% upside but longer than 12 months

Neutral: Expect low volatility

Sell: Expect more than 20% downside in 12 months

**Sector Rating**

Outperform: Expect more than 10% upside in 12 months

Market perform: Expect low volatility

Underperform: Expect more than 10% downside in 12 months

**Analyst Certification**

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