

## **Hong Kong | INVESTNOTES REPORTS REVIEW**

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### Industry:

Software (Kay Ng), Mainland financial, Utilities (Xingyu Chen), Mainland Telecom (Fanguohe), Mainland property, Oil and gas service (Chengeng), Air, Automobiles, Infrastructure (ZhangJing), New energy & Environmental Goods (Zhang Kun)

### **Software (Kay Ng)**

Except some individual stocks surged due to news or expectations, software service sector is roughly range-bounded or slightly lower in July.

Mobile game stocks continued softening except Boyaa. Forgame issued a profit warning in mid-July expecting substantial decline in revenue due to the delay launching of the new web games. The estimated net loss will be between RMB 15 to 25 million. After the news, the stock prices tumbled and fell more than 30% throughout July.

According to market sources, SARFT will continue to simplify the administrative processes for mobile games, especially on the content review procedures for casual puzzle game and standardize mobile games publishing management. SARFT staff revealed that in the first half of this year, sales revenue of online games was RMB 49.62 billion (as below), an increase of 46.4% yoy, higher than the 38% growth yoy of last year. The growth on mobile games was nearly four times yoy.

According to the latest report from Enfodesk, the forecasted first half market revenue will increase by 10% qoq, while the annual income should be able to break through RMB 100 billion. Based on the report, the forecasted MMO still occupied the largest market share of over 55%, while the share of the rapid growing mobile games increased to 24%, exceeding 20% of web games.

Our view of the overall online gaming industry maintains as long-term optimism. However, the industry can easily be affected by the individual products or policies of one or several gaming companies. Therefore, the sustainability of high growth will depend on whether the introduction of new products is welcomed by the players. The strong past performance can easily turn weak, thus requires both companies and investors to have fast response capabilities.

For the software stocks, government continued to promote the domestic information products. When Premier Li Keqiang visited the Shandong Inspur, he promised to recommend the China-made "cloud computing" products to the global markets, that's why the stock price of Inspur surged in those two days, and softened now.

August is the month of interim result announcements, it is expected the stock performances will become extreme in the sector.

## **Mainland Financial (Xingyu Chen)**

The market recorded the strong performance in July, HSI increased strongly and reached to around 25,000 at the end of this month stimulated by several good news such as the cross-border trading between Shanghai and Hong Kong. Due to the optimistic expectation of markets, the large quantity of hot money flowed into Hong Kong, and forced Hong Kong Monetary Authority to inject the capital into the market in seventeen times continually in order to stabilize the market volatility. All Chinese banks' prices increased strongly this month due to the rich liquidity. This is because the operating performance of banks still maintains stable growth, and the valuation of banks is also low, therefore the market prospect is positive, additionally, the banks with large market value have the stronger ability to accept more capital from the market.

There are several large banks made the important announcement this month, for instance, ICBC announced the plan of the issuance of the preferred stock with the amount of RMB80 billion totally, in line with our expectation in the previous monthly report, and we believe CCB will make the plans as well in future. Additionally, the market paid close attention to BoCom's announcement for the bank's reform, which was the sign to show the further restructuring of domestic banks and improve the banks' competitiveness. One of key issues is to see if the incentive mechanism of the management and employees will be implemented in the reform, if so, this will have great impact for China's banking industry, but the details need to be confirmed after the bank's interim results.

According to the share price, most of banks recorded the better performance, among which BoCom achieved the best performance with the share price growth of 17.9% this month, and CMBC and ABC recorded the relative better performance among the peers, with the share price growth of 14.8% and 10.8% respectively compared with the end of last month. Overall, we upgrade the banking sector to Buy rating.

## **Mainland Telecom (Fanguohe)**

In July, China Communications Facilities Co. Ltd. (I.E. Tower Company) is established co-founded by China Mobile, China Unicom and China Telecom. The infrastructure of mobile communication has entered a new phase formally. The proportion of share of the three operators is nearly trisection. In the future private capital is expected to be introduced.

Besides, the development of 4G is promoted in good momentum. According to the operation data of June, 4G users have increased 5,834,000 in China Mobile, which surpassed China Unicom for the first time, the new users of which is 3,050,000. In general, in recent months new 4G users have outnumbered that of China Unicom during the following several months after releasing 3G license in 2009, which demonstrates the maturity of internet application, that 4G has been universally accepted and that it has become an irreversible trend for China Unicom and China Telecom to follow the trend of scale construction for 4G. In fact, China Telecom has launched 4G in 16 cities, the internet of which 80% of the network supports two LTE forms. In terms of termination, the shipment of 4G mobile phone is 40.39mn in the first half of the year domestically. Coolpad Group has outstripped Apple and Samsung, ranking first in mainland China.

Meanwhile, the performance of relevant companies is optimistic. MOBI Development · Coolpad Group and ZTE have released positive profit alert. We believe that with the cut in fees, more available smartphones and low smartphone ASP, inland 4G market developments will accelerate and the shipment of smartphone is expected to increase at faster growth.

We grant the sector “accumulate” rating and recommend MOBI Development , Coolpad Group, and ZTE.

### **Mainland Property & Oil/Gas service (Chengeng)**

In July, 2014 I wrote four research reports on ACS, Tencent, GEG and Antonoil, which got success by unique operation model. We recommend “Tencent”. Tencent Holdings is one of the best Internet companies in China. The game business of mobile terminals will continue to drive the rapid growth of its performance in 2014, besides, with the gradual improvement of WeChat ecosphere, O2O business will become another pillar for commercialized mobile terminals from 2015. Better business models and more diversified WeChat services will support the monetization of its mobile terminals, which will become the main driving force of the share price in the future. To sum up, we maintain the rating of "Accumulate" for Tencent Holdings, with 12m TP at HKD136, corresponding to 43x and 32x of expected P/E ratio in 2014 and 2015 respectively.

### **Automobile & Air (ZhangJing)**

This month we released 3 updated equity reports: GAC (2238.HK), Dongfeng (489.HK), and Brilliance (1114.HK). As far as the potential room is concerned, we prefer Brilliance with the more attractive expected growth ratio.

BMW Group has issued the guidance on the future planning of Chinese market, and is going to announce recently that joint venture contract would be extended to 2028. This move is expected to eliminate the uncertainty of the source for future profitability, and is conducive to the introduction of new BMW models and their technologies, which is beneficial to the company's stock performance and the level of valuation. We believe that, after experiencing the explosive growth in past few years, the increase rate of China's luxury car market begins to slow down, with structure-based and pluralism market development trend becoming apparent, so BMW's accelerated introduction of segmentation products is conducive to continuous development of new segment markets. We revised our target price to HK\$16.45, based on 15/11/8.5xP/E in 2014/2015/2016, which we believe is rational considering its high ROE and fast growth ahead among peers, and the suggestions of “accumulate” rating be given.

### **New energy & Environmental Goods (Zhang Kun)**

National Energy Administration has released the data of wind power operation in the first half. The utilization hour is 986 hours, which is 114 hours lower yoy. The three provinces which have largest decrease are Sichuan, Shanxi and Xinjiang. These provinces have sharp increase in wind power installation, which reflect too fast installation speed will cause the power generation efficiency decrease.

On 25th this month, Ministry of Environmental Protection release the ‘Air pollution government plan for key industry around Beijing’, the plan require 296 power plants to transform. Part of the power plants will use nature gas as new power generation resource. This plan will promote the new energy projects in this area, we recommend ‘Jingneng Clean Energy (579.HK)’ and ‘Suntein Green Energy (956.HK)’. The power plants transforming will increase the wind power generation efficiency and the nature gas demand will increase.

Fig 1. Performance of Recommended Stocks

| Time      | Ticker | Company                       | Analyst | Rating     | Price on |        |         | Last     | Last    | Closing | 1M     |         |
|-----------|--------|-------------------------------|---------|------------|----------|--------|---------|----------|---------|---------|--------|---------|
|           |        |                               |         |            | Recommen | Target | Expecte | Month    | Month   | Price   | Price  |         |
|           |        |                               |         |            | ation    | Date   | Price   | d Return | Closing | Return  | 2M ago | Chg     |
| 2014-7-3  | 596    | HK Equity INSPUR INTL         | KN      | Neutral    |          | 1.65   | 1.56    | -5.45%   | 1.64    | -0.61%  | 1.65   | -0.61%  |
| 2014-7-4  | 2382   | HK Equity Sunny Optical       | GH      | Accumulate |          | 11.04  | 11.8    | 6.88%    | 10.26   | -7.07%  | 10.96  | -6.39%  |
| 2014-7-7  | 6818   | HK Equity CEB                 | XY      | Buy        |          | 3.64   | 5.27    | 44.78%   | 3.6     | -1.10%  | 3.36   | 7.14%   |
| 2014-7-8  | 579    | HK Equity JNCEC               | ZK      | Buy        |          | 3.74   | 5.1     | 36.36%   | 3.31    | -11.50% | 3.46   | -4.34%  |
| 2014-7-9  | 8210   | HK Equity ADVANCED CARD       | CG      | Buy        |          | 1.26   | 3       | 138.10%  | 1.37    | 8.73%   | 1.2    | 14.17%  |
| 2014-7-10 | 2238   | HK Equity GAC GROUP           | ZJ      | Accumulate |          | 9.42   | 10      | 6.16%    | 8.75    | -7.11%  | 8.86   | -1.24%  |
| 2014-7-11 | 6899   | HK Equity Ourgame             | KN      | Accumulate |          | 3.75   | 4.1     | 9.33%    | 3.65    | -2.67%  | 3.75   | -2.67%  |
| 2014-7-14 | 763    | HK Equity ZTE                 | GH      | Buy        |          | 14.78  | 21      | 42.08%   | 16.3    | 10.28%  | 15.28  | 6.68%   |
| 2014-7-15 | 3903   | HK Equity HANHUA FIN          | XY      | Buy        |          | 1.52   | 2.5     | 64.47%   | 1.57    | 3.29%   | 1.63   | -3.68%  |
| 2014-7-16 | 27     | HK Equity GALAXY ENT          | CG      | Accumulate |          | 62.95  | 72      | 14.38%   | 65.95   | 4.77%   | 62     | 6.37%   |
| 2014-7-17 | 489    | HK Equity Dongfeng GROUP      | ZJ      | Accumulate |          | 14.6   | 16.5    | 13.01%   | 13.88   | -4.93%  | 13.88  | 0.00%   |
| 2014-7-18 | 2020   | HK Equity ANTA                | AL      | Accumulate |          | 12.46  | 13.3    | 6.74%    | 12.8    | 2.73%   | 12.32  | 3.90%   |
| 2014-7-21 | 552    | HK Equity Chinacomservice     | GH      | Buy        |          | 3.87   | 4.7     | 21.45%   | 3.8     | -1.81%  | 3.61   | 5.26%   |
| 2014-7-22 | 750    | HK Equity Singyes Solar       | ZK      | Buy        |          | 11.34  | 15      | 32.28%   | 11.4    | 0.53%   | 13.06  | -12.71% |
| 2014-7-23 | 6030   | HK Equity Citic SEC           | XY      | Buy        |          | 18.18  | 22.3    | 22.66%   | 19.5    | 7.26%   | 17.1   | 14.04%  |
| 2014-7-24 | 700    | HK Equity TENCENT             | CG      | Accumulate |          | 124.3  | 136     | 9.41%    | 128.4   | 3.30%   | 118.2  | 8.63%   |
| 2014-7-25 | 1114   | HK Equity Brilliance          | ZJ      | Accumulate |          | 14.32  | 16.45   | 14.87%   | 14.54   | 1.54%   | 14.54  | 0.00%   |
| 2014-7-28 | 484    | HK Equity FORGAME             | KN      | Neutral    |          | 19.78  | 19      | -3.94%   | 18.38   | -7.08%  | 26.65  | -31.03% |
| 2014-7-29 | 2618   | HK Equity TCL Comm            | GH      | Accumulate |          | 10.34  | 11.76   | 13.73%   | 9.75    | -5.71%  | 9.38   | 3.94%   |
| 2014-7-30 | 6138   | HK Equity Harbin Bank         | XY      | Buy        |          | 2.99   | 3.85    | 28.76%   | 2.95    | -1.34%  | 3.1    | -4.84%  |
| 2014-7-31 | 3337   | HK Equity Anton Oilfield Serv | CG      | Accumulate |          | 4.51   | 5.2     | 15.30%   | 4.39    | -2.66%  | 5.28   | -16.86% |

Source: Company, Phillip Securities Research

**PHILLIP RESEARCH STOCK SELECTION SYSTEMS**

| Total Return | Recommendation | Rating | Remarks                                      |
|--------------|----------------|--------|--|
| >+20%        | Buy            | 1      | >20% upside from the current price           |
| +5% to +20%  | Accumulate     | 2      | +5% to +20% upside from the current price    |
| -5% to +5%   | Neutral        | 3      | Trade within $\pm$ 5% from the current price |
| -5% to -20%  | Reduce         | 4      | -5% to -20% downside from the current price  |
| <-20%        | Sell           | 5      | >20% downside from the current price         |

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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