

HONG KONG | INVESTNOTES REPORTS REVIEW

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)

Software services stocks, led by market leaders, generally showed the overall decline in August.

Before the announcement, Tencent had reached historical high of \$ 134, but callback about 5.5% from its peak afterwards. Kingsoft's results were worse than expected. Despite a slight increase in revenue, the operating profit fell 22.3% yoy, and operating profit margin suffered further declining to a new low of 16.5% compared to the previous quarter. The share price fell nearly 10% after the earnings released.

Mobile gaming stocks moved in different directions based on performance. Boyaa's net profit increased 1.5 times yoy in the second quarter, while IGG's adjusted interim net profit rose 3.7 times yoy. The share prices had once risen about 16% and 30% after interim results released, but slowly dropped to the level as in mid-July.

Forgame, which issued a profit warning last month, on the 22nd of August, announced the decision to terminate the acquisition of Magic Feature's 21% stake. Instead, it planned to cooperate to jointly develop a global published mobile game. Net loss was RMB 21.77 million for the interim performance. Share price suffered from selling pressure since the mid July and JP Morgan, as the sponsor, cut its target price to \$ 15.

For the software sector, Sinosoft had published interim results with net profit increased 53% yoy. Kingdee's cost and expenses were significantly reduced, coupled with the low base in last year, net profit surged for 8.46 times. However, both of the stock prices did not follow the good performances and had been falling during the month.

Overall, besides the results speculation, investors had not put in too much attention to this sector in August; the fund appeared to shift to other industries. It is expected without particular good news, in the short run, the sector will maintain slightly downward movement. But we maintain optimistic view in the long run, the PRC government was still focused in developing the information industry, with sustainable good performances, traditional investors will gradually recognize its stable profitability.

Mainland Financial (Xingyu Chen)

The market recorded the stable performance in August, HSI increased maintained stable growth and reached to the new high after the financial crisis in 2008 this month stimulated by several good news such as the stock connect between Shanghai and Hong Kong. Due to the optimistic expectation of markets, the large amount of hot money flowed into Hong Kong in recent months, which caused the rich liquidity in the market. All Chinese banks' prices increased strongly this month due to the rich liquidity. However, almost all banks' share prices dropped this month after the large increase in July. This is mainly because investors hold the cautious view for the banks' performance after the announcement of interim results.

According to the banks' interim results, there are two key points: one is the slow-down of the profit growth. The profit growth of most banks declined compared with the same period of last year. For instance, ICBC's net profit increased by 7% approximately in 1H2014, compared with 12% in 1H2013. The other is the trend of the deterioration of the banks' asset quality. According to China Banking Regulatory Commission (CBRC), as at the end of June, the NPLs of China's banking financial institutions increased by RMB102.3 billion, already larger than that of the whole year of 2013. The quarterly NPLs increased by RMB48.3 billion in 2Q. Due to the large growth of NPLs, the NPL ratio also reached to 1.08%, up 0.08ppts compared with the end of 2013. Almost all banks' NPLs and NPL ratios increased to varying degrees. Take BoCom as an example, currently its profit growth is lower than other state-owned banks, in the analyst meeting, the management stated that BoCom's NPLs mainly focused on the industries with overcapacity, especially in steel trade industry in developed areas such as Jiangxi and Zhejiang. In 1H2014, 65% of BoCom's newly added NPLs came from steel trade industry and micro and small enterprises. Currently, the NPLs of steel trade loans amounted to RMB9.7 billion in the bank's total NPLs as RMB38.8 billion, with the proportion of 25% approximately.

We believe currently the listed banks' profit growth maintain stable, and the risks are still under control in the short term although the asset quality goes down. According to the share price, most banks' prices dropped to the varying degrees this month and we expect they are still facing the downward pressure in September, however, as the large-cap companies, the banks will become more attractive for investors when stock connect between Shanghai and Hong Kong is coming, and therefore the share price of banks would continue to go up slowly in future. Overall, we maintain the banking sector on Buy rating.

Mainland Telecom (Fan guohe)

The 4G business of China Mobile is on the trend of steady increasing, and the number of clients in the first half of year was only about 13.94 million, but the monthly growth of July increased by over 10% to 6.5 million. Looking into 2H14, China Telecom and China Unicom will accelerate the 4G construction and will provide pre-commercial service in 16 cities, more alternative terminals and the 4G tariff that is hopeful to decrease again may stimulate the shipment of 4G cellphones. Moreover, domestic cellphone vendors are expected to win bigger market share for their high cost performance.

Regarding the performance in 1H14, the operators are better than expectation, and China Mobile shows the improvement of competitive position. In the meantime, the upstream companies such as ZTE and MOBI Development, etc. all have realized explosive growth. Although the terminal manufacturers such as Coolpad Group have realized substantial growth as well, the industrial competition

becomes fiercer, plus with the subsidy cut, their profitability is faced with challenges. We expect that 4G support will still build a beneficial environment for the telecom industry, and suggest to continue to pay close attention to ZTE, MOBI Development and Tongda Group.

Mainland Property & Oil/Gas service (Chen geng)

In August 2014 I wrote three research reports on Yestar, Tencent and Greentown, 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 give the rating of "Neutral" 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's car stocks differed, Dongfeng Group, BYD, Qingling Motors in better performance under the good expected results, and Guangzhou Automobile Group, Geely, Weichai and other stocks have declined due to difficulties encountered prospects. While Brilliance, GWM is basically flat.

This month we released 4 updated equity reports: Weichai (2338.HK), GWM (2333.HK), Geely (175.HK) and Cathay (293.HK). As far as the potential room is concerned, we prefer GWM with the more attractive expected growth room.

Though GWM have recorded a minor decrease of 3.1% yoy in 2014H result, according to the Company's plan, new SUV H2 (already launched in July), H1, H9, the updated M4, automatic H6 Sport will be launched successively in 2H, and the upgraded C50, the updated C30 in sedan vehicles will also be put into market, the attracting high-end SUV H8 may be put into market again by the end of this year, the intensive introduction of new models will not only make up the lack of new vehicles due to the delay of H8 in the 1H but also help the Company for improving the product series. We revised our target price to HK\$37, based on 9.6/7.3xP/E in 2014/2015, 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 Price	
					Recommen	Target	Expecte	Month	Month	Price	Chg	
					ation Date	Price	d Return	Closing	Return	2M ago		
2014-8-1	2338	HK Equity Weichai	ZJ	Neutral		34	34	0.00%	31.4	-7.65%	34	-7.65%
2014-8-5	777	HK Equity NETDRAGON	KN	Accumulate	14.46	17.34	19.92%	14.98	3.60%	14.64	2.32%	
2014-8-6	1330	HK Equity DYNAGREEN	ZK	Buy	3.8	5	31.58%	4.1	7.89%	3.73	9.92%	
2014-8-7	728	HK Equity China Telecom	GH	Neutral	4.14	4.25	2.66%	4.79	15.70%	4.39	9.11%	
2014-8-8	165	HK Equity China EB	XY	Buy	14.42	17.5	21.36%	14.7	1.94%	12.08	21.69%	
2014-8-11	3900	HK Equity GREENTOWN CHII	CG	Accumulate	8.16	8.69	6.50%	8.16	0.00%	9.99	-18.32%	
2014-8-12	2333	HK Equity GWM	ZJ	Accumulate	31.9	37	15.99%	32.9	3.13%	32.1	2.49%	
2014-8-13	434	HK Equity Boyaa	KN	Accumulate	9.22	10.44	13.23%	8.6	-6.72%	9.001	-4.46%	
2014-8-14	762	HK Equity China Unicom	GH	Accumulate	13.02	14.2	9.06%	13.82	6.14%	13.6	1.62%	
2014-8-15	1336	HK Equity NCI	XY	Buy	28	36.6	30.71%	27.65	-1.25%	28.2	-1.95%	
2014-8-18	700	HK Equity TENCENT	CG	Neutral	130.3	136	4.37%	126.5	-2.92%	128.4	-1.48%	
2014-8-19	293	HK Equity Cathay	ZJ	Accumulate	14.86	16.84	13.32%	14.4	-3.10%	14.72	-2.17%	
2014-8-20	3888	HK Equity Kingsoft	KN	Neutral	24.2	23.17	-4.26%	22.2	-8.26%	23.25	-4.52%	
2014-8-21	257	HK Equity EB INTL	ZK	Accumulate	10.92	11.94	9.34%	10.62	-2.75%	10.44	1.72%	
2014-8-22	941	HK Equity China Mobile	GH	Accumulate	94.4	103.75	9.90%	96.4	2.12%	85.9	12.22%	
2014-8-25	1375	HK Equity CC SECURITIES	XY	Buy	2.49	3.5	40.56%	2.42	-2.81%	2.43	-0.41%	
2014-8-26	2393	HK Equity Yestar	CG	Neutral	7.49	7.2	-3.87%	7.5	0.13%	6.03	24.38%	
2014-8-27	175	HK Equity Geely	ZJ	Neutral	3.02	3.07	1.66%	2.97	-1.66%	3.14	-5.41%	
2014-8-28	1432	HK Equity CHINA SHENGMU	KN	Accumulate	2.5	2.79	11.60%	2.47	-1.20%	2.09	18.18%	
2014-8-29	698	HK Equity Tongda	GH	Buy	1.07	1.37	28.04%	1.06	-0.93%	1.11	-4.50%	

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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