EQUITY RESEARCH

CSR (1766 HK)

Favorable factors has most reflected in the short term

Hong Kong | Industrial Goods | Update Report

22 January 2015

The Merger plan of CSR and CNR was officially launched

China CSR made an official announcement of the Merger at the end of December, 2014, which will be conducted in the way of China CNR being absorbed and incorporated into China CSR. According to the announcement, China CNR`s A/H shares will be canceled, and each China CNR share will be exchanged for 1.1 China CSR shares to be issued by CSR. Upon completion of the Merger, the Post-Merger New Company will be renamed CRRC Corporation Ltd or CRRC for short.

After the Merger, it is expected to avoid the price-cutting competition in overseas market

The previous split of CSR and CNR was an attempt of market reform of SOEs, with a purpose mainly to effectively prevent monopoly from impeding technical progress. Then in the following 14 years, the performance of both parties also proved the effect that mutual competition could promote development. But it also brought about the bad results of price battle and resource waste in the exploration of overseas market. The Merger of CSR and CNR is the outcome of the state will, which is expected to avoid the state`s interest being impaired by their internal rivalry in the expansion of overseas market, and will benefit the long-term development of Chinese high-end equipment manufacture enterprises in the global market.

The Synergy Effects are expected to bring about reduction in cost after the Merger

No matter the railway and urban metro market at home or abroad, the aggrandizement of the Post-Merger business scale will also enhance the Company`s negotiating ability, which will then bring about reduction in cost, and the Merger will be beneficial for the Synergy Effects to exert in staff allocation, material purchase, sales system and R&D area, so as to realize a more effective utilization of resources. In addition, the new company can share the research and development resources, make an overall planning on research and development system and product layout, to promote the company`s overall competitiveness.

The bellwether of "One Road One Belt" strategy

According to the International Union of Railways (UIC), the total length of the high-speed railway in service, under construction and in planning in the world is 54.6 thousand kilometers. And the construction cost of China`s high-speed railway is 1/3 to 1/2 of that of developed countries, and China can also provide package solutions of engineering design, construction, and equipment manufacturing and operation management. It can thus be seen that as the model of high-end equipment, China`s high-speed railway manufacturing industry has the reason and ability to share growth bonus of the global high-speed railway market, and CRRC Corporation Limited after mergence accords with the direction of China`s "Silk Road Economic Belt Region" strategy.

Investment Thesis

Nevertheless, this pre-arranged plan needs to be examined and approved by the A/H stockholders` meeting of CSR and CNR, the SASAC and the CSRC. There still exist some complicated procedures. After the consolidation by merger of any party, hundreds of billions of assets alteration and personnel disposition and arrangement can be finished after some very heavy and complicated procedures, which is just the reason for the subsequent stock price volatility.

CSR`s share price rose significantly early (rose by 40% in the past three months), we think the favorable factors in the short term has most reflected, the further rise in the share price may be restricted so far, thus we downgrade rating to "Cautious Accumulate".

Cautious Accumulate (Downgrade)

CMP	10.36	HKD	
TARGET	11.46	HKD	10.6%

COMPANY DATA

O/S SHARES (MN) :	13803
MARKET CAP (HKD MN) :	230,270
52 - WK HI/LO (HKD) :	5.35 - 12.68
Raw Beta (Past 2yrs weekly data)	0.95

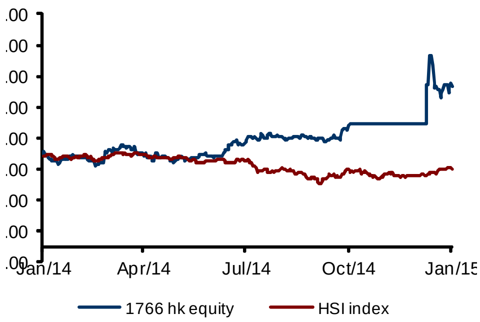
SHARE HOLDING PATTERN, %

South China car group company	56.48%
HKSCC Nominees Limited	14.62%

PRICE PERFORMANCE, %

	1MTH	3MTH	1YR
1766 hk	31.31	32.99	73.24
HSI index	4.76	4.78	6.24

PRICE VS. HSI



Source: Phillip Securities Hong Kong Research

KEY FINANCIALS

CNY mn	FY13	FY14E	FY15E	FY16E
Revenue	**89019**	**96525**	**116267**	**132465**
Net Profit	4009	4140	5582	6746
EPS, (yuan)	0.30	0.30	0.40	0.49
P/E (X),	27.9	27.1	20.2	16.7
BVPS (yuan)	2.37	2.65	2.80	3.45
P/B (X)	3.5	3.1	2.9	2.4
DPS (yuan)	0.09	0.09	0.12	0.15
Div. Yield (%	1.1%	1.1%	1.5%	1.8%

Source: Bloomberg, PSR est.

*All multiples & yields based on current market price

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As analyzed above, we revised EPS expectation of the Company to RMB 0.404, 0.489, 0.596 of 2014/2015/2016. And we accordingly revised the target price to 11.46, respectively 22.4/18.5/15.1x P/E and 3.2/2.6/2.4x P/B for 2014/2015/2016.

Peer Comparison

Ticker	Name	Mkt Cap (HKD mil)	BEst P/B	BEst P/B:2 FY	BEst P/E:1 FY	BEst P/E:2FY	BEst Curr EV/BEst EBITDA	P/B	ROA LF	ROE
CNY (1 security)										
601299 CH Equity	CHINA CNR CORP LTD-A	189936	2.9	3.0	27.3	23.2	16.4	3.4	3.6	13.6
EDM (1 security)										
SIE GR Equity	SIEMENS AG-REG	750796	2.4	2.2	13.3	12.5	9.2	2.6	5.2	18.2
EFR (1 security)										
ALO FP Equity	ALSTOM	74760	1.6	1.3	18.5	15.0	14.0	1.5	1.4	8.4
HKD (2 securities)										
1766 HK Equity	CSR CORP LTD - H	202859	2.8	2.5	20.7	17.6	18.0	3.1	3.8	13.5
3898 HK Equity	ZHUZHOU CSR TIMES ELECTRIC	56011	4.1	3.6	22.0	19.6	17.8	4.7	15.1	24.6
JPY (1 security)										
7012 JP Equity	KAWASAKI HEAVY INDUSTRIES	59366	2.2	2.0	17.6	14.1	10.3	2.4	2.7	12.6
USD (1 security)										
BDRBF US Equity	BOMBARDIER INC-B	35208	1.9	1.6	6.3	6.1	7.4	#N/A F	1.5	24.8

Source: Company, Phillip Securities Hong Kong Research

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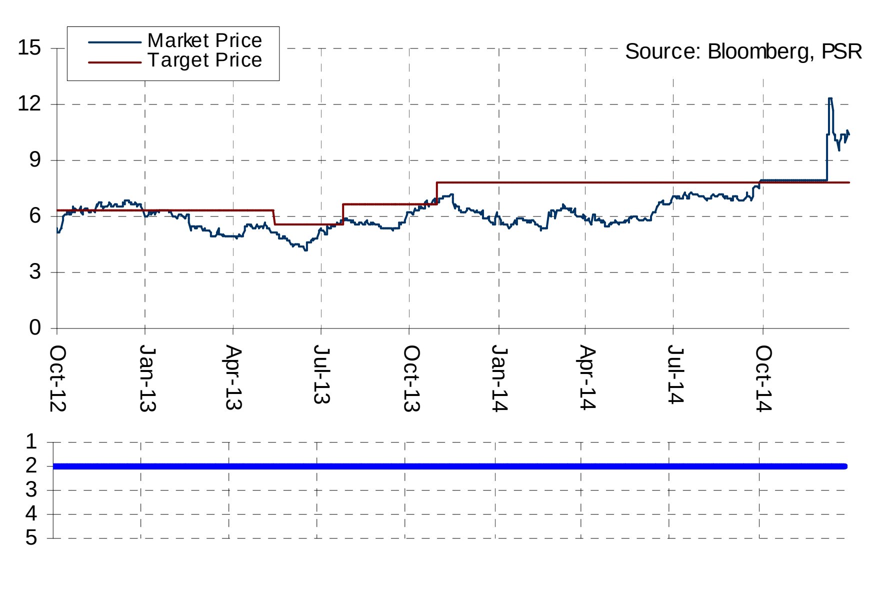
Financials

FYE DEC	FY11	FY12	FY13	FY14F	FY15F	FY16F
Valuation Ratios						
P/E (X), adj.	25.8	27.9	27.1	20.2	16.7	13.7
P/B (X)	4.4	3.5	3.1	2.9	2.4	2.2
Dividend Yield (%)	2.1%	1.1%	1.1%	1.5%	1.8%	2.1%
Dividend Payout Yield (%)	55.2%	30.1%	30.0%	29.7%	30.7%	28.5%
Per share data (RMB)						
EPS, (Basic)	0.33	0.30	0.30	0.40	0.49	0.60
EPS, (Diluted)	0.33	0.30	0.30	0.40	0.49	0.60
DPS	0.18	0.09	0.09	0.12	0.15	0.17
BVPS	1.91	2.37	2.65	2.80	3.45	3.75
Growth & Margins (%)						
Growth						
Revenue	24.0%	12.0%	8.4%	20.5%	13.9%	20.9%
EBIT	61.8%	-1.2%	1.9%	31.8%	20.1%	21.3%
Net Income, adj.	53.0%	3.8%	3.3%	34.8%	20.9%	21.9%
Margins						
Gross margin	18.7%	17.7%	17.2%	18.0%	18.5%	18.7%
EBIT margin	8.1%	7.1%	6.7%	7.3%	7.7%	7.8%
Net Profit Margin	4.9%	4.5%	4.3%	4.8%	5.1%	5.1%
Key Ratios						
ROE	21.3%	18.4%	19.1%	19.2%	19.4%	119.4%
Income Statement (RMB mn)						
Revenue	**79517**	**89019**	**96525**	**116267**	**132465**	**160113**
Gross profit	14870	15755	16629	20951	24453	29941
EBIT	6436	6357	6479	8538	10255	12438
Profit before tax	5442	5593	5933	7759	9262	11366
Tax	-699	-740	-859	-1117	-1338	-1767
Profit for the period	4743	4852	5074	6642	7923	9598
Minority interests	879	843	934	1060	1177	1378
Total capital share	11840	13400	13803	13803	13803	13803
Net profit	**3864**	**4009**	**4140**	**5582**	**6746**	**8220**

Source: PSR

Ratings History



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
<-20%	Sell	5

Remarks

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

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 ± 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

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