

Xinyi Glass (868.HK)

Short-term highlights: lower cost and increasing efficiency

Hong Kong | Industry Goods | Update Report

19 March 2015

- **FY2014 earnings declined by almost 60%.** Xinyi Glass recorded a turnover of 10.86 billion HK dollars for 2014, with an increase of 9.3% yoy. But the net profit attributable to shareholders was only 1.364 billion, with a great decline of 58% yoy, and the earnings per share (EPS) of 34.78 HK cents. If the one-time gains of 1.315 billion yuan from the spin-off of the listed Xinyi Solar (968.HK) in 2013 were not considered, the net profit attributable to shareholders would decline by 38% yoy.

- **Price weakness of float glass is the main factor.** The major business depts. of the company, i.e. float glass, automotive glass and low-emission engineering glass, had different performances. Float glass was impacted by the slow-down of real estate industry, energy cost increase and excess industry production capacity, and the gross margin of float glass declined by 12 ppts to 7% yoy. Thus the overall gross margin of the company decreased by 6.4 ppts from 31.6% in 2013 to 25.2%.

- **Automotive glass and low-emission glass kept a steady growth.** The company's automotive glass business benefited from the upturn of the global automotive market demand and recorded a steady growth. During that period, the subdivision's revenue and gross profit respectively increased by 9.3% and 5.5% yoy. Meanwhile, thanks to the constant growth of the demand of domestic construction industry for energy-saving and low-emission coated glass, there was a strong demand for the company's low-emission glass products, and the company's revenue and gross profit respectively recorded a growth of 18.6% and 5% yoy in that period. The subdivision of automotive glass and low-emission glass had a gross margin basically kept at 40%.

- **Float glass business sees the initial improvement.** The management expresses that, the worst moment of float glass business has gone, and the supply and demand situation of glass in South China Region market has improved since the beginning of this year. We think if the country's measures to eliminate the outdated capacity in glass industry can be effectively implemented, it will be helpful. Besides, the company plans to build new production lines in Malaysia so as to utilize the lower energy and labor cost in the local area, and the production lines are expected to be put into operation in 2017.

- **The diversification strategy seems to be continued.** Meanwhile, the company's diversification strategy will continue. Apart from the second electronic glass production line that will be put into operation this year, the company intends to enter wind power business, and is expected to do small-scale tests within this year. And the company plans to launch the first wind power plant program in Anhui Province so as to seize the growth opportunity from China's policy of encouraging clean and renewable energy.

- **Valuation and investment thesis.** The Chinese government announces that it will reduce the natural gas price from April, which will be helpful for reducing the company's production cost. So we attribute reducing cost and increasing efficiency are the short-term highlights of the company. We adjust the EPS in 2015/2016 to the expected 0.49/0.65 HKD, and correct the target price to 5.29 HKD, corresponding to respectively 10.8/8.1 x P/E ratio in 2015/2016, and give an Accumulate rating.

Accumulate (Upgrade)

CMP HKD 4.71

TARGET HKD 5.29 (+12%)

COMPANY DATA

O/S SHARES (MN) :	3921
MARKET CAP (HKD MN) :	18471
52 - WK HI/LO (HKD):	6.8 / 3.77

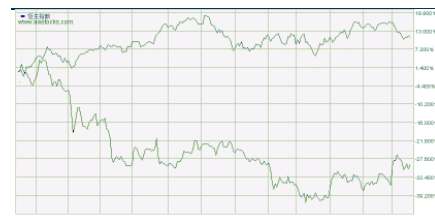
SHARE HOLDING PATTERN, %

Realbest Investment Limited	18.49
High Park Technology Limited	6.8

PRICE PERFORMANCE, %

	1M	3M	1Y
Xinyi G	4.57	16.84	-29.54
HIS index	8.31	12.15	-40.28

PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

CNY mn	FY13	FY14E	FY15E	FY16E
Net Sales	9936	10861	12287	14207
Net Profit	3522	1366	1964	2607
EPS, CNY	0.92	0.35	0.49	0.65
P/E, x				
BVPS, CNY	3.11	3.15	3.47	3.86
P/BV, x				
DPS (CNY)	0.27	0.15	0.22	0.30
Div. Yield (%)				

Source: Company reports, Phillip Securities Est.

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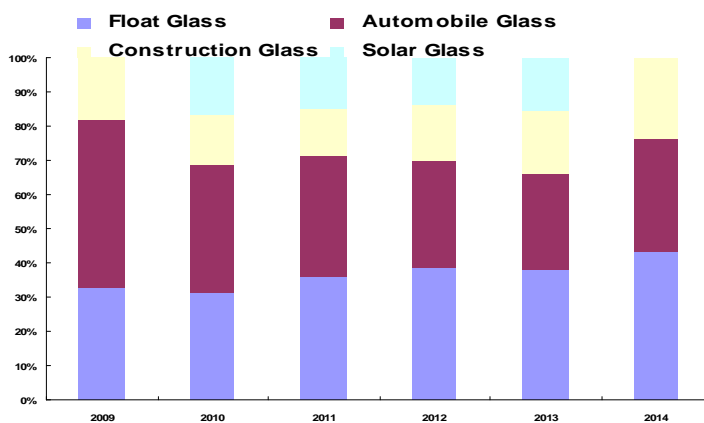
In 2014, the earnings declined by almost 60%

According to the whole year results in 2014 published by Xinyi Glass, it recorded a turnover of 10.86 billion HK dollars, with an increase of 9.3% yoy. But the net profit attributable to shareholders was only 1.364 billion, with a great decline of 58%, and the EPS of 0.3478 HK dollars. The results were lower than our expectation. Final dividend was 6 cents while the dividend for the same period last year was 14 cents. If the one-time gains of 1.315 billion yuan from the spin-off of the listed Xinyi Solar (968.HK) in 2013 were not considered, the net profit attributable to shareholders would decline by 38% yoy.

The price weakness of float glass is the main factor

The major businesses of the company, i.e. float glass, automotive glass and low-emission engineering glass, had different performances. For the business unit of float glass, due to the slow-down of the real estate industry and the impact from the excess production capacity of float glass industry, the market price started to drop sharply since last May, which impacted the profitability of this business unit. Therefore, the gross margin of the company's float glass business declined by 12ppts to 7% in 2014. Though the revenue of this business had increased by about 5% yoy, the gross profit contributed had a great decline of 61% yoy.

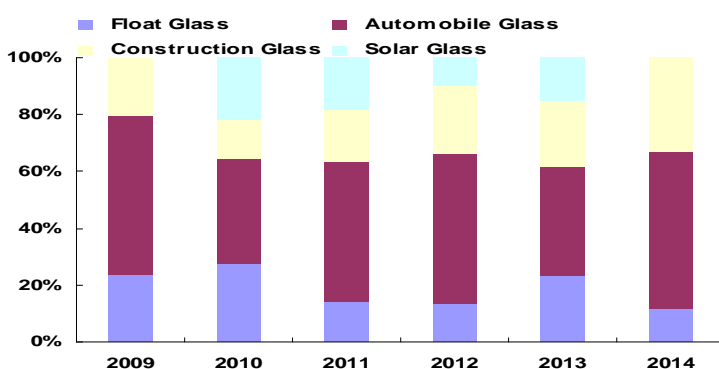
Revenue Breakdown



Source: Company reports, Phillip Securities Hong Kong Research

The overall gross margin declined by 6.4ppts from 31.6% in 2013 to 25.2% in 2014. Apart from the reasons mentioned above, this was also attributed to rise of the company's overall cost due to the increase of the natural gas price by the government in August 2014 which increased the company's energy cost.

Gross profit Breakdown



Source: Company reports, Phillip Securities Hong Kong Research

Automotive glass and low-emission glass keep a steady growth

For the automotive glass business, thanks to the upturn of the global automotive market demand, especially the demand for automotive glass in North America Region turning high, the company's automotive glass business recorded a steady growth. In that period, this subdivision's revenue and gross profit increased respectively by 9.3% and 5.5% yoy. Meanwhile, thanks to the constant growth of the demand of domestic construction industry for energy-saving and low-emission coated glass, there was a strong demand for the company's low-emission glass products, and the company's revenue and gross profit respectively recorded a growth of 18.6% and 5% yoy in that period. The subdivision of automotive glass and low-emission glass had a gross margin basically kept at a relatively high level of 40%.

The float glass business sees the initial improvement and the diversification strategy will continue

The management expresses that, the worst moment of float glass business has gone, and the supply and demand situation of glass in South China Region market has improved since the beginning of this year. We have noticed that the average price index of domestic glass had the sign of hitting the bottom. If the country's measures to eliminate the outdated capacity in glass industry can be effectively implemented, it will be helpful for the improvement of the supply and demand structure of the industry and the price recovery of the company.

Meanwhile, the company's diversification strategy will continue. Apart from the second electronic glass production line that will be put into operation this year, the company intends to develop wind power business, and is expected to do small-scale tests within this year. And the company plans to launch the first wind power plant program in Anhui Province so as to seize the growth opportunity from China's policy of encouraging clean and renewable energy.

The company's capacity targets this year are respectively 16.56 million pieces for automotive glass, 38 million m² for low-emission glass, and 4.842 million tons for float glass. The capital expenditure this year is expected to be 1.5 billion HKD.

Valuation

Considering the reduced fuel cost, we adjust the EPS in 2015/2016 to the expected 0.49/0.65 HKD, and correct the target price to 5.29 HKD, corresponding to respectively 10.8/8.1 x P/E ratio in 2015/2016, and give an Accumulate rating.

Peer Comparison

Ticker	Name	Mkt Cap (HKD)	BEst P/B	BEst P/B:2FY	BEst P/E:1FY	BEst P/E:2FY
CNY						
600660 CH Equity	FUYAO GROUP GLASS IND	36792	2.53	2.21	12.59	10.80
600819 CH Equity	SHANGHAI YAOHUA PILKII	9548	N/A	N/A	N/A	N/A
HKD						
868 HK Equity	XINYI GLASS HOLDINGS LT	17726	1.33	1.18	8.73	7.15
200012 CH Equity	CSG HOLDING CO LTD - B	21352	1.18	1.08	9.20	8.03
425 HK Equity	MINTH GROUP LTD	16449	1.62	1.45	11.52	9.84
1108 HK Equity	LUOYANG GLASS COMPAN	3969	N/A	N/A	N/A	N/A
3300 HK Equity	CHINA GLASS HOLDINGS L	1611	N/A	N/A	N/A	N/A
JPY						
5201 JP Equity	ASAHI GLASS CO LTD	56674	0.78	0.77	23.47	23.00
USD						
GLW US Equity	CORNING INC	227443	1.44	1.35	14.63	13.46

Source: Bloomberg, Phillip Securities Hong Kong Research

Financials

FYE DEC	FY11	FY12	FY13	FY14	FY15F	FY16F
Valuation Ratios						
P/E (X), adj.	13.4	14.8	5.1	13.5	9.7	7.3
P/B (X)	2.0	1.8	1.5	1.5	1.4	1.2
Dividend Yield (%)	3.4%	3.2%	5.7%	3.2%	4.7%	6.4%
Per share data (HK\$)						
EPS, reported	0.35	0.32	0.92	0.35	0.49	0.65
EPS, adj.	0.35	0.31	0.89	0.34	0.49	0.65
DPS	0.16	0.15	0.27	0.15	0.22	0.30
BV/PS	2.31	2.63	3.11	3.15	3.47	3.86
Growth & Margins (%)						
Growth						
Revenue	29.3%	18.9%	1.5%	9.3%	13.1%	15.6%
EBIT	-17.9%	-5.8%	152.5%	-54.6%	41.9%	33.0%
Net Income, adj.	-19.5%	-6.1%	196.4%	-61.2%	43.8%	32.7%
Margins						
EBIT margin	19.0%	15.0%	37.3%	15.5%	19.4%	22.4%
Net Profit Margin	15.4%	12.1%	35.4%	12.6%	16.0%	18.3%
Key ratios						
ROE	17.0%	13.1%	32.3%	11.3%	14.9%	17.6%
Dividend payout ratio	45.5%	47.3%	29.4%	43.1%	45.2%	46.4%
Income Statement (HK\$ mn)						
Revenue	8227	9785	9936	10861	12287	14207
Cost of sales	5,873	7,310	6,799	8,128	8,822	10,002
Gross profit	2,354	2,475	3,137	2,733	3,465	4,205
Operating expenses	5,500	1,788	1,251	1,638	1,728	1,980
Profit from operations	965	1,197	2,207	1,266	1,863	2,362
Financial cost	32	71	83	91	103	112
Net non oper loss	-13	-68	-1,471	-452	-539	-805
Profit before tax	1,526	1,398	3,627	1,593	2,286	3,065
Tax	262	209	381	228	311	417
Profit for the period	1,264	1,189	3,522	1,365	1,975	2,648
Minority interests	(1)	1	0	(1)	11	41
Net profit	1,265	1,188	3,522	1,366	1,964	2,607

Source: PSR

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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