

GUANGSHEN RAIL (525.HK)

Price Hike of Passenger Transportation and Land Development Are Catalysts of Stock Price

China | Railway Transportation | Company Initiation

• The main assets of Guangshen Railway include Guangshen Railway and Guangzhou-Pingshi section of Beijing-Guangzhou Railway. Its main businesses include passenger transportation, freight transportation, and railway network usage & railway operation services. Based on the FY2015 result, the proportion of these three parts to the total revenue was 45%, 11% and 37%, respectively. Additionally, the company also provides train repair, on-board catering services, leasing and other businesses related to railway transportation. Revenues from other businesses represent about 7% of the total revenues.

• To be specific, the passenger transportation encompasses transportation business of Guangzhou-Shenzhen inter-city express trains, long-distance trains and Through Trains in Hong Kong. The revenues from these three segments represent 32%, 55% and 7%, respectively. Affected by the diversion of Guangzhou-Shenzhen high-speed railway, the company's Guangzhou-Shenzhen inter-city express trains have showed a weak growth demand trend, and the revenues from passenger transportation in 2015 remained basically flat as compared with the same period last year.

• Freight businesses includes Guangzhou-Pingshi Railway, Guangzhou-Shenzhen Railway and other railway transportation services. Although the National Railway Administration raised the price of railway freight for a couple of times and hence fueled temporary increase in the company's freight income, the overall sluggish macro-economic environment makes the continued growth difficult to be maintained. Therefore, the revenues from freight transportation in 2015 declined by 0.2% year-on-year

• The revenues from railway network usage and other transportation services, which account for 37% of the total revenues, witnessed a rapid growth in recent years. Specifically, the growth of "railway network usage" was modest, while that of "other transportation services" was dramatic in the past five years with a compound annual growth rate of about 40%. This is mainly due to the constant increase in the commissioned operation (also known as "hosting") undertaken by the company. At present, the company is commissioned to host several railway arteries of China (including Wuhan-Guangzhou Passenger Railway (WGPR), Guangzhou-Shenzhen Railway (GSHR), Xiamen-Shenzhen Railway (XSR) and Ganzhou-Shaoguan Railway (GSR)). It mainly provides these railways with railway operation services, locomotive and passenger car leasing, passenger service and luggage transportation. In 2015, the company was also commissioned to host Guiyang-Guangzhou Railway and Nanning-Guangzhou Railway. Several of the commissioned railways are developing, and we are optimistic about its relatively high growth rate in the future.

• The company's largest shareholder is Guangzhou Railway Group, holding 37% equity, and its de facto controller is China Railway Corporation. The railways controlled by Guangzhou Railway Group include those railways in Guangdong, Hunan and Hainan provinces. The total operation mileage reached 6,519 kilometers and the mileage of high-speed railways + EMU trains amounted to 1,449 kilometers. However, the railway mileage managed by the company was only 481 kilometers, only 7.4% of the former, while its mileage of high-speed railways + EMU trains was only 152 kilometers, only 10% of the former. Presently, the profitability of other railways under Guangzhou Railway Group falls behind that of Guangzhou-Shenzhen Railway, but it is likely that their profitability soars after the price hike of passenger transportation in the future and that they gain asset injection.

29 September 2016

Accumulate (Initiation)

CMP: HKD 3.56

(Closing price as at 27 September 2016)

TARGET: HKD 4.10 (+15%)

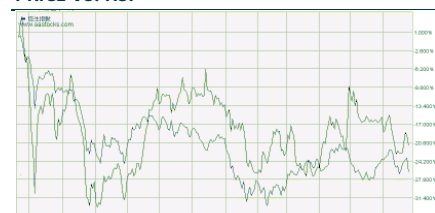
COMPANY DATA

O/S SHARES (MN) :	7084
MARKET CAP (CNY MN) :	5095
52 - WK HI/LO (CNY):	4.48/ 2.92

SHARE HOLDING PATTERN, %

Guangzhou Railway Group	37
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PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

CNY mn	FY14	FY15	FY16E	FY17E
Net Sales	14,801	15,725	16,404	17,478
Net Profit	662	1,071	1,171	1,287
EPS, CNY	0.09	0.15	0.17	0.18
P/E, x	30.1	19.7	18.1	16.6
BVPS, CNY	3.78	3.88	3.97	4.09
P/BV, x	0.7	0.8	0.8	0.7
DPS (CNY)	0.05	0.08	0.08	0.09
Div. Yield (%)	1.8%	2.7%	2.8%	3.1%

Source: Company reports, Phillip Securities Est.

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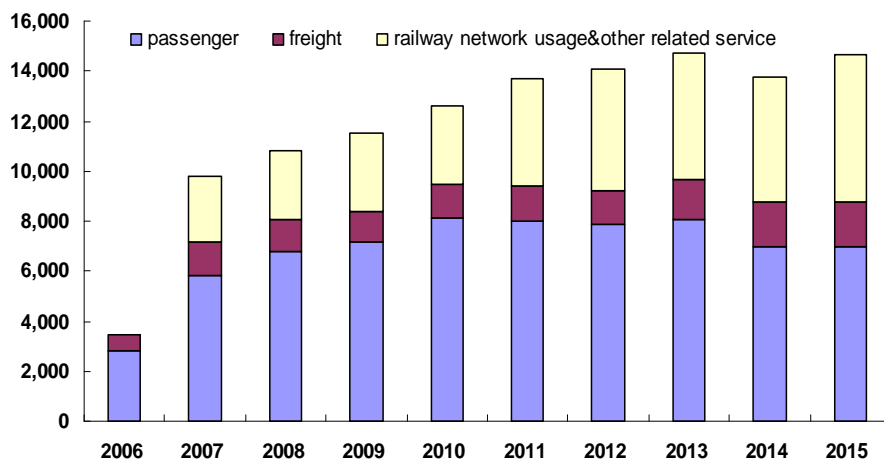
On the other hand, currently, the company's land that can be developed covers an area of approximately 2-4 million square meters. The assessed price in 1995 was only RMB65/square meter, but the present actual average comparable worth has exceeded RMB10000/square meter with an immense potential for land appreciation.

Investment Thesis

Overall, according to our expectation, the company's EPS in 2016/2017 is RMB0.165/RMB0.182 and, its BVPS is RMB3.97/RMB4.09 and the current stock price is equivalent to around PE 18 x / 17 x and PB 0.7 x / 0.8 x.

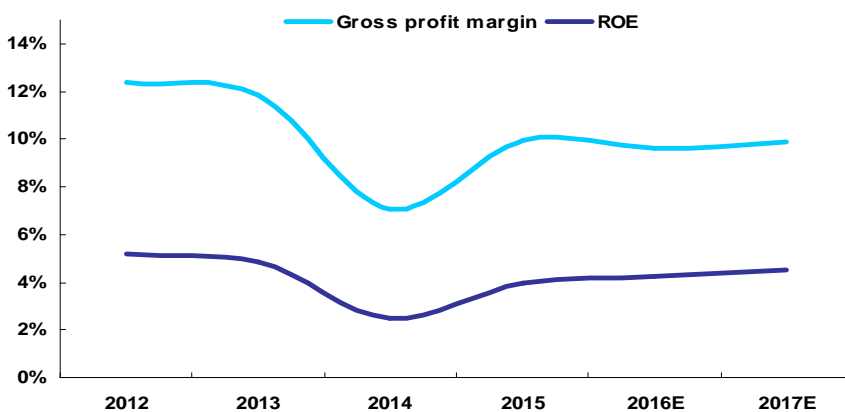
The approaching expectation for price hike of railways and passenger transportation renders the company's result relatively flexible, since the revenues from ordinary passenger trains account for more than half of the company's revenues from passenger transportation, significantly promoting the result growth. Taking into account the favorable expectation for the price hike of railways and passenger transportation and the potential land value, we believe that it is reasonable to give the company a valuation of 0.9x/0.8x BPS in 2016/2017, equivalent to target price of HK\$ 4.1 and Accumulate rating. (Closing price as at 27 September 2016)

Main product breakdown



Source: Company, Phillip Securities Hong Kong Research

Key margin trend



Source: Company, Phillip Securities Hong Kong Research

Financials

FYE DEC	FY11	FY12	FY13	FY14	FY15	FY16F	FY17F
Valuation Ratios							
P/E (X), adj.	11.5	15.3	15.6	30.1	19.7	18.1	16.6
P/B (X)	0.8	0.8	0.7	0.7	0.8	0.8	0.7
Dividend Yield (%)	3.1%	3.5%	2.9%	1.8%	2.7%	2.8%	3.1%
Dividend payout ratio (%)	35.3%	53.7%	44.5%	53.5%	52.9%	50.2%	50.6%
Per share data (RMB)							
EPS, reported	0.25	0.19	0.18	0.09	0.15	0.17	0.18
EPS, adj.	0.25	0.19	0.18	0.09	0.15	0.17	0.18
DPS(HKD)	0.09	0.10	0.08	0.05	0.08	0.08	0.09
BVPS	3.58	3.66	3.76	3.78	3.88	3.97	4.09
Growth & Margins (%)							
Growth							
Revenue	31.5%	2.7%	4.7%	-6.3%	6.2%	4.3%	6.5%
EBIT	16.9%	-24.3%	-2.7%	-44.0%	37.2%	8.8%	9.9%
Net Income, adj.	11.4%	-26.8%	-3.5%	-48.0%	61.7%	9.4%	9.9%
Margins							
Gross margin	17.6%	12.3%	11.9%	7.1%	10.0%	9.6%	9.9%
EBIT margin	17.5%	12.9%	12.0%	7.2%	9.3%	9.7%	10.0%
Net Profit Margin	12.3%	8.7%	8.1%	4.5%	6.8%	7.1%	7.4%
Key Ratios							
ROE (%)	7.3%	5.1%	4.84%	2.48%	3.95%	4.21%	4.51%
Income Statement (RMB mn)							
Revenue	14,691	15,092	15,801	14,801	15,725	16,404	17,478
Gross profit	2,590	1,863	1,874	1,049	1,568	1,575	1,730
Operating profit	2,564	1,935	1,889	1,056	1,454	1,580	1,736
EBIT	2,569	1,946	1,894	1,061	1,456	1,584	1,741
Profit before tax	2,378	1,759	1,702	881	1,452	1,578	1,732
Tax	(576)	(441)	(431)	(220)	(389)	(415)	(454)
Profit for the period	1,802	1,318	1,271	661	1,063	1,163	1,278
Minority interests	(2)	(2)	(3)	(1)	(8)	(8)	(9)
Total capital share	7,084	7,084	7,084	7,084	7,084	7,084	7,084
Net profit	1,804	1,320	1,274	662	1,071	1,171	1,287

Source: PSR

(Financial figures as at 27 September 2016)

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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