

COMPANY NOTE

Estimate Change

China | Industrials | Basic Materials

1 March 2017

Jefferies

Xinyi Glass (868 HK) Solid FY16 Results and Stable Outlook

Key Takeaway

As preannounced in December 2016, Xinyi Glass' FY16 NPAT increased by 52%, driven by strong margin expansion. Under the current supply/demand dynamics, management is confident that it can pass through the rise in cost (energy + soda ash) and maintain a stable margin. Xinyi Glass is now trading at 8x 2017E P/E, with close to 6% dividend yield; reiterate Buy.

FY16 earnings review. As preannounced in December 2016, Xinyi Glass' FY16 NPAT grew by 52% YoY, driven by 1) reduction in natural gas price and other stringent cost control measure; 2) increase in sales volumes of float glass.

Maintain optimistic outlook. Management expects a healthy and stable supply/demand dynamics in 2017 with little new capacity coming into the market. As a result, we believe XYG can continue to pass through the higher energy/material cost to customer and maintain a stable margin.

Cost to decline. Natural gas price could be lower than the original level when the temporary price hike ends in mid-March, according to management. It also believes that soda ash prices have already peaked and should gradually decline; we expect soda ash cost in 1H17 to be 5-15% higher vs the same period last year.

Increase in volumes, driven by new capacity in Malaysia. The 1,200t/day capacity in Malaysia commenced operations in Jan; we expect the margin for the Malaysian facility to be higher than the domestic market due to higher ASP, lower transportation cost; this could avoid import tariff in the South East Asia market.

Stable dividend payout. FY dividend was HK\$0.4/share (vs HK\$0.27/share in 2015) with payout ratio maintained at around 48%. In addition, management is considering spinning off its solar farm business from Xinyi Solar (968 HK, HKD2.71, NC).

Changes in estimates. We revise down our FY16/17 earnings estimates by about 6%, as we cut our earnings assumption for Xinyi Solar by about 20%, reflecting its weaker-than-expected FY16 results.

Valuation/Risks

We maintain Buy with a PT of HK\$8.6 based on SOTP valuation methodology, valuing its glass business (float/auto/construction glass) at 11x 2017E earnings and Xinyi Solar at current market price. Our PT HK\$8.6 implies 10x 2017E P/E and 2.2x 2017E P/B, slightly above the historical average.

HKD	Prev.	2015A	Prev.	2016E	Prev.	2017E	Prev.	2018E
Rev. (MM)	--	11,460.0	12,896.0	12,848.0	13,936.0	14,194.0	14,380.0	14,711.0
Operating Profit (MM)	--	1,518.0	2,635.0	2,837.0	--	2,981.0	3,073.0	3,196.0
Net Profit	--	2,113.0	3,070.0	3,213.0	3,580.0	3,399.0	3,837.0	3,649.0
ROE	--	16.6%	20.8%	24.4%	21.3%	22.6%	20.3%	21.4%
DPS	--	0.27	0.39	0.40	0.45	0.42	0.49	0.45
Cons. EPS	--	--	--	--	0.84	0.92	0.93	0.99
EPS								
FY Dec	0.53	0.54	0.79	0.83	0.92	0.88	0.98	0.94
FY P/E		13.5x		8.8x		8.3x		7.7x

BUY

Price target HK\$8.60
Price HK\$7.28^

Bloomberg: 868 HK
Reuters: 868.HK

Financial Summary

Net Debt (MM): HK\$4,911.0

Market Data

52 Week Range: HK\$7.73 - HK\$3.65

Total Entprs. Value (MM): HK\$33,461.7

Market Cap. (MM): HK\$28,550.7

Shares Out. (MM): 3,921.8

Float (MM): 1,759.8

Avg. Daily Vol.: 11,124,660

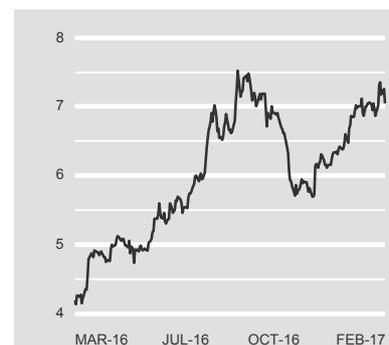
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Price Performance



^Prior trading day's closing price unless otherwise noted.

Changes in estimates

We revise our volume and gross margins slightly to incorporate FY16 results and lower our earnings assumption for its associate (Xinyi Solar) by about 20% to reflect the weaker-than-expected FY16 results. In summary, we revise down our FY16/17 earnings estimates by about 6%.

Table 1: Changes in estimates

		Old		New		Changes	
		2017E	2018E	2017E	2018E	2017E	2018E
Revenue	HK\$ m	13,936	14,380	14,194	14,711	1.9%	2.3%
Gross profit	HK\$ m	5,071	5,230	4,994	5,283	-1.5%	1.0%
Operating profit	HK\$ m	2,981	3,073	2,981	3,196	0.0%	4.0%
NPAT	HK\$ m	3,580	3,837	3,399	3,649	-5.1%	-4.9%
Diluted EPS	HK\$	0.92	0.98	0.86	0.92	-6.5%	-6.4%

Source: Company data, Jefferies estimate

FY2016 Earnings Review

- Sales was up by 12% yoy to Rmb13bn as float glass increased by 30% yoy to Rmb6.5bn.
- Gross margin expanded to 36.3% vs just 27.3% last year on higher ASP. Gross margin for float glass expanded by more than 16ppts to 27.5%. Reported net profit is up 52% YoY to Rmb3.2bn.
- Net gearing remains healthy at about 37% and payout ratio was stable at about 48%, with FY DPS of HK\$0.4/share vs HK\$0.27/share in 2015.
- The company's operating cash flow increased from Rmb2.6bn to Rmb3.6bn, while capital expenditure was around Rmb1.8bn.
- Capex commitment for the company in 2017 amounted to Rmb2.5bn and should be well covered by the strong operating cash flow.
- Management expects annualised float glass capacity to increase by 7.1% YoY in 2017, mainly driven by the new capacity built in Malacca, Malaysia. The second phase of the Malaysia project will be built in 2017.
- The single-digit percentage growth in auto glass capacity was purely driven by increase in efficiency.
- Management is considering spinning off its solar farm business from Xinyi Solar (968 HK, NC).

PT of HK\$8.6

We value Xinyi Glass based on SOTP valuation methodology, valuing its glass business (float/auto/construction glass) at 11x 2017E earnings and Xinyi Solar at the current market price. Our PT of HK\$8.6 implies 10x 2017E P/E and 2.2x 2017E P/B, slightly above the historical average.

Chart 62: Xinyi Glass Valuation

Xinyi Glass	
Float/Auto/Construction Glass Business	
NPAT (2017E)	2,768
x Target multiple	11
Market Value (HK\$ m)	30,452
÷ Shares outstanding (m)	3,882
Share price (HK\$/share)	7.84
Xinyi Solar (968 HK)	
Current Share Price (HK\$)	2.70
XYG's shareholdings	30%
Market value of Xinyi Solar's holdings	0.80
Target Price	8.64
Rounded to HK\$0.10/share	8.60
Latest price	7.28
Upside	18%

Source: Jefferies estimates

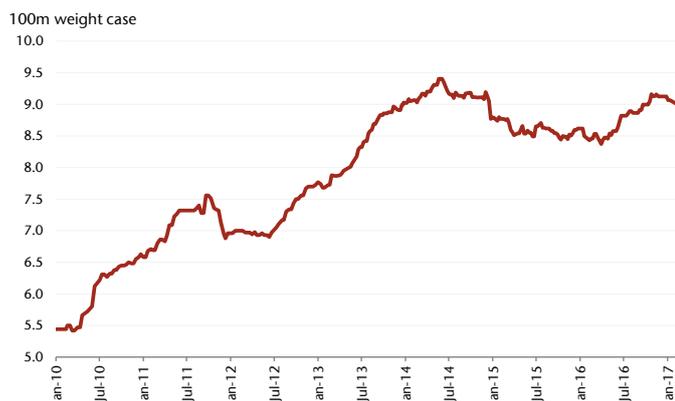
Risks

Key risks to our estimates and PT: liquidity tightening policy, which could negatively impact new floor spaces started and construction demand; collapse in float glass prices due to more than expected new capacity in operation and slowdown in demand growth; intensifying competition of high quality float glass product; additional expenses due to overseas capacity expansion; trade disputes and currency fluctuations.

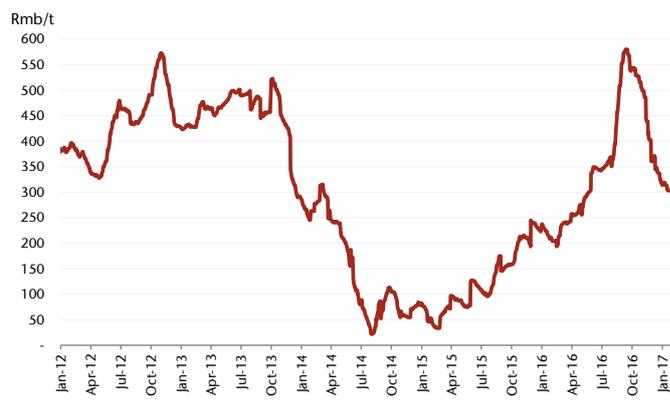
Table 6: Valuation comparison

Company	Ticker	Mkt cap (US\$ bn)	Price (local)	Target (local)	Upside to Rec. target	P/E (x)		P/B (x)		EV*/EBITDA (x)		ROE (%)		Div Yield (%)		
						2016E	2017E	2016E	2017E	2016E	2017E	2016E	2017E	2016E	2017E	
Glass - H																
Fuyao Glass	3606 HK	7.2	24.20	24.00	Buy	-1%	18.1	17.2	2.9	2.7	8.4	7.5	17.0	16.8	4.1	4.5
Xinyi Glass	868 HK	3.7	7.28	8.60	Buy	18%	9.0	8.5	2.1	1.9	9.1	8.8	24.4	22.6	5.5	5.8
Flat Glass	6865 HK	0.4	1.69		NC		4.6	4.5	0.7	0.7	2.2	1.9	18.7	20.2	5.4	5.8
Average							10.6	10.1	1.9	1.8	6.6	6.1	20.0	19.9	5.0	5.4
Glass - A																
Fuyao Glass - A	600660 CH	7.2	19.39		NC		14.3	13.1	2.5	2.3	9.0	8.1	18.0	18.2	4.3	4.5
CSG Holdings	000012 CH	2.8	11.65		NC		25.9	23.3	nmf	nmf	nmf	nmf	nmf	nmf	nmf	nmf
Zhuzhou Kibing Group	601636 CH	1.7	4.45		NC		16.9	14.8	1.9	1.7	7.7	7.0	12.0	11.8	nmf	nmf
Jinjing Group	600586 CH	1.0	4.88		NC		16.8	10.0	1.6	1.5	10.0	9.3	6.7	7.4	nmf	nmf
Average							18.5	15.3	2.0	1.8	8.9	8.2	10.3	10.9	4.3	4.5

Source: Company data, Jefferies estimates, NC data from Bloomberg

Chart 1: Capacity in operation has gone up with ASP increase

Source: Wind, Jefferies

Chart 2: Margin spread (ASP minus soda ash and natural gas cost)

Source: Wind, Bloomberg, Jefferies Estimate

Table 8: Xinyi Glass Financials Summary

Income statement					Cash flow				
HK\$ m	2015	2016	2017E	2018E	HK\$ m	2015	2016	2017E	2018E
Revenue	11,460	12,848	14,194	14,711	Profit before tax	2,380	3,823	4,037	4,341
COGS	-8,328	-8,189	-9,200	-9,428	D&A	776	824	816	932
Gross profit	3,133	4,659	4,994	5,283	Change in working cap.	500	46	-128	-68
Operating expenses	-1,615	-1,822	-2,013	-2,087	Other	-1,019	-1,542	-641	-690
Operating profit	1,518	2,837	2,981	3,196	CF from operations	2,637	3,151	4,083	4,516
Other gains - net	634	552	565	602	Capex	-2,105	-1,853	-2,500	-1,500
Share of results of assoc. & JCE's	317	563	630	693	Acquisitions and others	584	0	0	0
Finance costs	-90	-128	-139	-150	CF from investing	-1,520	-1,853	-2,500	-1,500
Pre-tax profit	2,380	3,823	4,037	4,341	Equity raised/ (repaid)	-607	-1,467	0	0
Tax	-266	-607	-641	-690	Debt raised/ (repaid)	16	1,646	681	681
Profit	2,114	3,216	3,396	3,652	Dividends, interest and others	-33	-981	-1,553	-1,642
Minority interest	0	-3	3	-3	CF from financing	-625	-802	-871	-961
Net profit	2,113	3,213	3,399	3,649	Net cash flow	492	496	712	2,055
Basic EPS (Rmb)	0.54	0.83	0.88	0.94	Exchange gain	-25	0	0	0
Diluted EPS (Rmb)	0.53	0.81	0.86	0.92	Cash at end of year	1,298	2,763	3,475	5,530
Balance sheet					Ratio & financial metrics analysis				
HK\$ m	2015	2016	2017E	2018E		2015	2016	2017E	2018E
Cash	1,298	2,763	3,475	5,530	Revenue Growth	5.5%	12.1%	10.5%	3.6%
Inventories	1,223	1,321	1,484	1,520	EBIT Growth	38.6%	86.9%	5.1%	7.2%
Receivables	2,381	2,377	2,626	2,722	EPS Growth	54.9%	53.6%	5.8%	7.4%
Other current assets	93	76	76	76	EBIT Margin	13.2%	22.1%	21.0%	21.7%
Fix assets	11,971	11,831	13,514	14,082	Net Profit Margin	18.4%	25.0%	23.9%	24.8%
Others assets	4,455	5,655	5,655	5,655	Payout Ratio	49.2%	48.3%	48.3%	48.3%
Total assets	21,422	24,022	26,830	29,585	Valuation metrics				
ST debt	2,514	3,165	3,817	4,468	PER (x)	13.5	8.8	8.3	7.7
Other current liabilities	2,445	2,835	3,118	3,182	EV/EBITDA (x)	14.5	9.2	8.8	7.8
LT debt	3,514	4,509	4,539	4,569	Price to Book (x)	2.2	2.1	1.9	1.7
Other LT liabilities	223	266	266	266	Balance Sheet Ratios				
Total liabilities	8,696	10,775	11,740	12,486	ROE	16.6%	24.4%	22.6%	21.4%
Shareholder's equity	12,718	13,181	15,027	17,033	ROCE	7.7%	13.2%	12.6%	13.1%
Minority interests	7	66	63	66	Net debt to Equity	37.2%	37.1%	32.3%	20.5%
Total liability & equity	21,422	24,022	26,830	29,585	Interest coverage (x)	25.4	28.7	27.3	27.5
					Book value per share	3.2	3.4	3.9	4.4

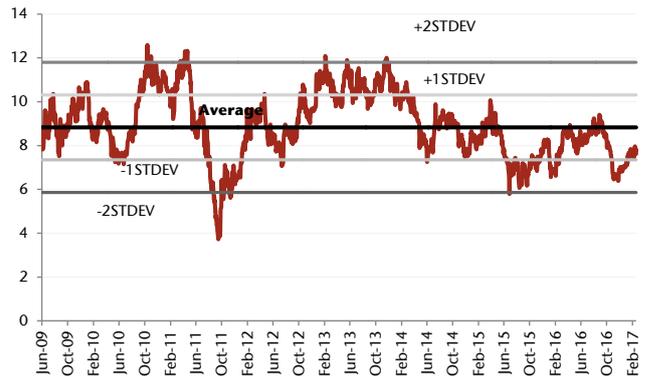
Source: Company data, Jefferies estimates

Chart 63: Xinyi Glass Historical PE Chart



Source: Bloomberg, Jefferies

Chart 7: Xinyi Glass Historical PE Chart



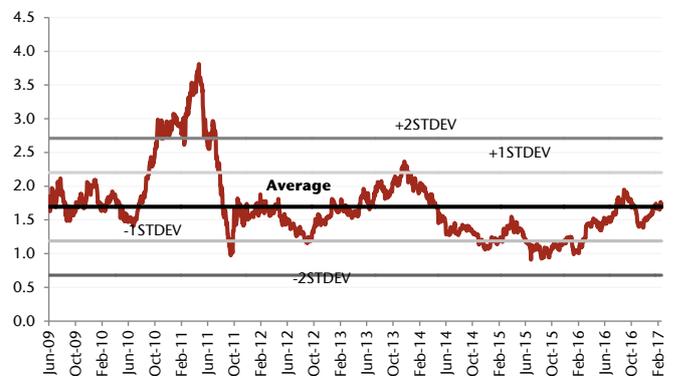
Source: Bloomberg, Jefferies

Chart 8: Xinyi Glass Historical PB Chart



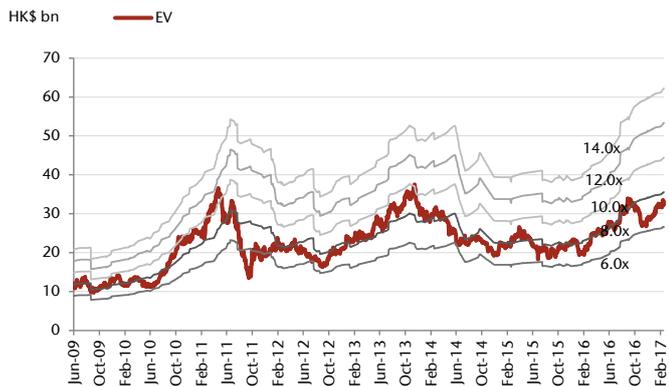
Source: Bloomberg, Jefferies

Chart 9: Xinyi Glass Historical PB Chart



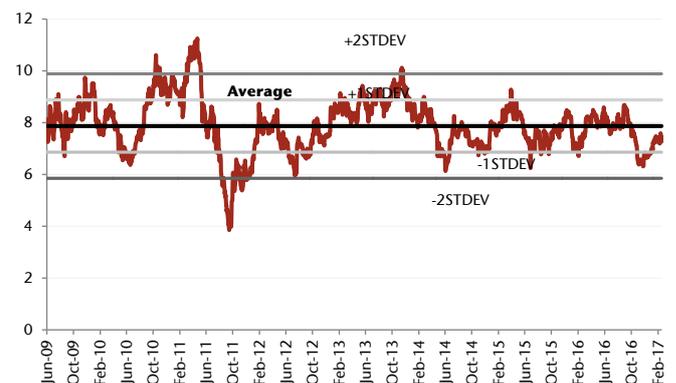
Source: Bloomberg, Jefferies

Chart 10: Xinyi Glass Historical EV/EBITDA Chart



Source: Bloomberg, Jefferies

Chart 64: Xinyi Glass Historical EV/EBITDA Chart



Source: Bloomberg, Jefferies

Company Description

Xinyi Glass is engaged in the production and sales of a wide range of glass products, including automobile glass, energy saving construction glass, high quality float glass and other glass products. Its customers include companies in the business of automobile glass manufacturing, wholesale and distribution, curtain wall engineering and installing, construction and furniture glass manufacturing, and float glass wholesale and distribution. As of YE15, the company has ~5mt of float glass capacity.

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(Article 3(1)e and Article 7 of MAR)

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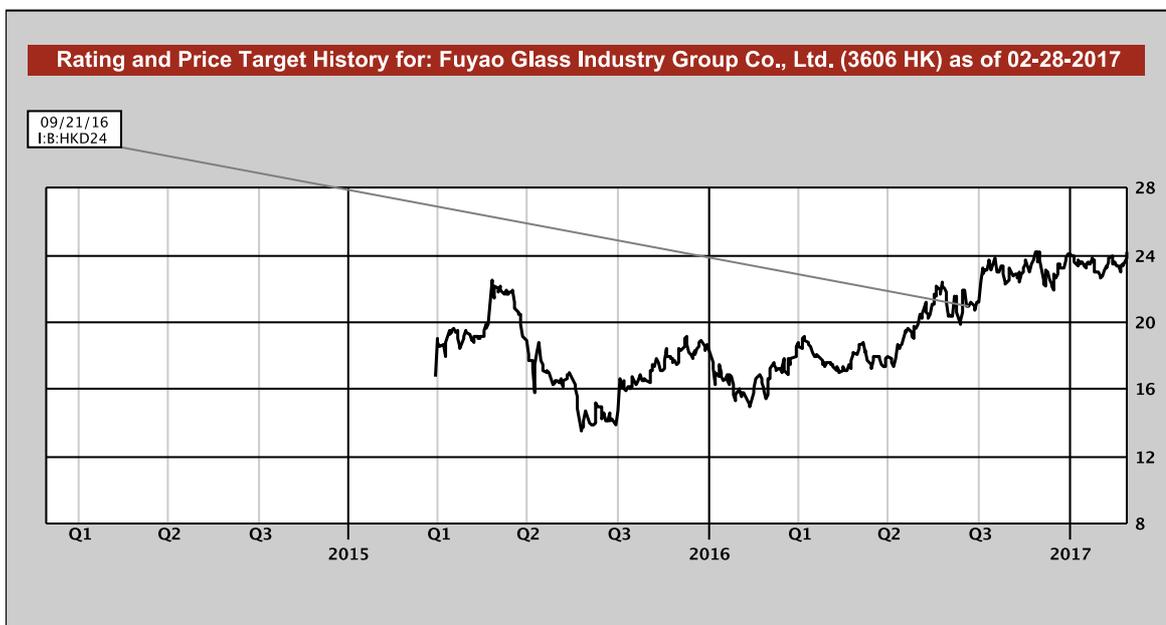
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Other Companies Mentioned in This Report

- Fuyao Glass Industry Group Co., Ltd. (3606 HK: HK\$24.20, BUY)
- Xinyi Glass Holdings Limited (868 HK: HK\$7.28, BUY)



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Legend:

I: Initiating Coverage

D: Dropped Coverage

B: Buy

H: Hold

UP: Underperform

868 HK

Estimate Change

1 March 2017

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Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
BUY	1101	50.37%	338	30.70%
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