

Xinyi Glass [0868.HK]

2017 results beat expectations. Maintain BUY

Xinyi Glass (XYG) reported its 2017 results, which beat market expectations. The positives from float glass, other income and architectural glass were offset by the lower-than-expected performance of Xinyi Solar (XYS) and lower margin in the automobile glass segment. XYG's top-line growth in 2017 was driven mainly by a 23.2% YoY increase in sales of float glass products. Sales of auto glass products and architectural glass products reported YoY growth of 4.3% and 8.1%, respectively, in 2017. The negative impact on the automobile glass segment faded in 2H 2017. The blended gross margin was 37% in 2017, up from 36.3% in 2016. Management released positive guidance on the three segments of the Company. The float glass industry is expected to see a 2-5% YoY decline in production capacity in 2018, given capacity shutdown in late 2017 and increasing environmental protection controls, and glass prices are expected to remain resilient in 2018 and 2019. The automobile glass segment is also expected to resume faster growth in 2018 and 2019, given slower growth in 2017, as the Company expanded capacity. Property sector data also points to a positive outlook for XYG's architectural glass segment. Comparing XYG's three business segments, we got the impression that growth of XYS in 2018 may be slower, especially given the high base impact in 1H 2017. We maintain the view that XYG will be one of the major beneficiaries of supply-side reform in China. XYG's share price performance is expected to be supported by an earnings upgrade by the market and positive industry news flow about capacity shutdown and a better operating environment. Despite its share price outperformance, XYG is now trading at a 10.5x 2018 PER and an estimated dividend yield of 4.7%. With its undemanding valuation, we maintain our BUY call with a new target price of HK\$14.76 (based on a 13x 2018E PER, lower than its historical average and the average of its listed peers).

Investment Highlights

- 2017 results highlights.** XYG's net profit increased 24.9% YoY to HK\$4,013.8m in 2017, which beat market expectations. XYG's turnover was HK\$14,727.5m in 2017, up 14.6% YoY from HK\$12,848.4m in 2016. The top-line growth of Xinyi Glass was driven mainly by the float glass division, which reported turnover of HK\$8,016.9m in 2017, up 23.2% YoY from HK\$6,509.8m in 2016. Architectural glass and automobile glass reported respective YoY sales growth of 8.1% and 4.3% in 2017. XYG's automobile glass segment successfully resumed growth in 2H 2017, as the Company's automobile segment was affected by unfavourable currency movements, a drop in sales in some emerging markets, and the spin-off of Xinyi HK [8328.HK] in 1H 2017. The gross profit margins for float glass, architectural glass and automobile glass were 31.7%, 38.0% and 46.9%, respectively, in 2017 vs. 27.5%, 39.9% and 49.0% in 2016. The drop in the gross margins of automobile glass and construction glass was due mainly to higher input costs (higher float glass prices). The blended gross profit margin improved from 36.3% in 2016 to 37.0% in 2017, principally due to an increase in the average selling price of float glass, along with a wider variety in the product mix. Xinyi Glass declared a final dividend of HK\$0.28 per share for 2017.
- All divisions expected to report better growth.** XYG management remains positive on the outlook for all three business divisions. It expects demand for float glass in China to be resilient in 2018 and 2019, given strong property sales in 2017 and property under construction. Float glass capacity is expected to drop 2-5% in 2018, given capacity shutdown in late 2017 and increasing environmental protection controls. Float glass prices are expected to hold up well in 2018 and 2019, as there will be no major increase in production capacity in 2017 and 2018. Management mentioned that cost of production is expected to come down YoY in 2018, given a drop in soda ash prices, which dropped from RMB2,400/tonne in Nov/Dec 2017 to currently RMB1,600/tonne. The operating environment for the float glass industry is getting more favourable in 2018. Growth of XYG's automobile glass division picked up in 2H 2017 vs. negative growth in 1H 2017. XYG management guided that it expects growth of the automobile glass division to accelerate in 2018 and 2019, given capacity expansion. The architectural glass segment is expected to benefit from resilient demand in the property sector and the wider adoption of Low-E glass, and management mentioned that some areas in China are using triple Low-E glass products. The profitability of the automobile and architectural glass segments is expected to rebound, given higher sales growth.
- XYS management mentioned that the adoption of bifocal solar panels has created growth opportunities for XYS.** But we expect the growth of the Company's solar glass division to moderate in 2018, given stronger-than-expected sales growth in 2017. The spin-off of Xinyi Energy is expected to accelerate in 2018. The high base effect in 1H 2017 will make growth in 1H 2018 less exciting. We revised up our earnings forecasts for 2018 by 11.8%, as we factored in a faster growth rate and higher gross margin assumptions. We also introduce our 2019 forecasts.

Key Financials (in HKDm)	2015	2016	2017	2018E	2019E
Revenue	11,460.3	12,848.4	14,727.5	16,544.3	19,219.9
Change (YoY %)	5.5	12.1	14.6	12.3	16.2
Gross Profit	3,132.7	4,659.3	5,444.1	6,235.3	7,191.2
Gross Margin %	27.3	36.3	37.0	37.7	37.4
Net Profit	2,113.1	3,213.4	4,013.8	4,505.4	5,153.5
Net Margin %	18.4	25.0	27.3	27.2	26.8
EPS (Basic)	0.54	0.83	1.01	1.14	1.30
Change (YoY %)	54.9	54.2	22.1	12.2	14.4
DPS	\$0.265	\$0.400	\$0.480	\$0.560	\$0.641
ROE (%)	16.9	24.8	25.6	23.3	23.9
Dividend Yield (%)	2.22	3.35	4.02	4.69	5.37
PER (x)	22.2	14.4	11.8	10.5	9.2
PBR (x)	3.7	3.5	2.6	2.3	2.1
FCF Yield (%)	2.24%	3.68%	1.99%	3.92%	5.02%
Capex (m)	(1,987.0)	(1,853.0)	(2,500.0)	(2,500.0)	(2,500.0)
Free cash flow per share	0.3	0.4	0.2	0.5	0.6
Net Gearing (%)	37.2	37.3	29.7	30.3	27.7

Source: Bloomberg, CGIS Research

China Construction Sector -

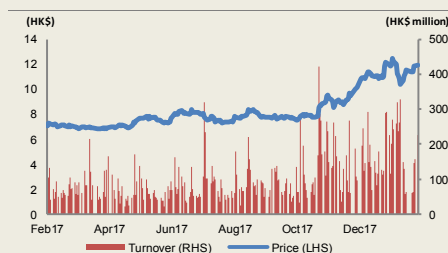
Building Materials

BUY

Close: HK\$11.94 (Feb 26, 2018)

Target Price: HK\$14.76 (+23.6%)

Share Price Performance



Sources: Bloomberg, CGIS Research

Market Cap	US\$6,132m
Shares Outstanding	3,999m
Auditor	Pricewaterhouse-
Free Float	46.3%
52W range	HK\$6.83-12.44
3M average daily T/O	US\$8.9m
Major Shareholder	Mr Lee Yin Yee (20.3%)

Mark Po, CFA — Senior Analyst

(852) 3698-6318

markpo@chinastock.com.hk

Wong Chi Man, CFA — Head of Research

(852) 3698-6317

cmwong@chinastock.com.hk

Figure 1: Results highlights

Results Highlights (HKD m)	1H 2014	2H 2014	1H 2015	2H 2015	1H 2016	2H 2016	1H 2017	2H 2017
Revenue	5,034	5,827	5,283	6,177	5,885	6,963	6,677	8,051
Cost of sales and services	-3,697	-4,430	-3,873	-4,455	-3,844	-4,346	-4,248	-5,036
Gross profit	1,337	1,397	1,410	1,723	2,041	2,618	2,429	3,015
Other income and other gains and losses	247	152	287	307	147	547	96	598
Distribution and selling expenses	-268	-340	-312	-367	-351	-269	-334	-341
Administrative expenses	-472	-558	-441	-494	-533	-669	-586	-784
Finance costs	-25	-14	-26	-24	-44	-52	-50	-47
JV & Associates	57	80	161	157	312	250	368	332
Profit before tax	876	716	1,079	1,301	1,572	2,425	1,923	2,773
Income tax expense	-114	-114	-138	-128	-202	-405	-285	-397
MI	-0	-0	-2	1	-0	-2	-2	2
Profit for the period	762	602	939	1,174	1,369	2,018	1,636	2,378
Gross margin (%)	26.6	24.0	26.7	27.9	34.7	37.6	36.4	37.4
Operating margin (%)	17.9	12.5	20.9	21.4	27.5	35.6	29.6	35.0
Net Margin (%)	15.1	10.3	17.8	19.0	23.3	29.0	24.5	29.5
Turnover by products (HKDm)								
Automobile glass	1,781	1,813	1,897	1,890	1,990	1,758	1,871	2,039
Construction glass	1,079	1,477	1,206	1,445	1,220	1,370	1,186	1,614
Float glass	2,175	2,538	2,180	2,843	2,675	3,835	3,619	4,398
Gross margin by products (%)								
Automobile glass	42.1	41.5	44.1	44.6	48.7	49.3	47.8	46.2
Construction glass	37.0	34.1	31.7	35.6	39.0	40.6	37.5	38.4
Float glass	8.6	5.6	8.7	12.9	22.3	31.2	30.1	33.0

Source: Company, CGIS Research

Figure 2: Key assumptions for XYG

	2012	2013	2014	2015	2016	2017	2018F	2019F
Turnover (HKDm)								
Automobile glass	3,077.8	3,287.2	3,593.2	3,786.6	3,748.4	3,910.0	4,050.0	4,374.0
Construction glass	1,574.6	2,154.5	2,555.5	2,651.5	2,590.2	2,800.6	3,146.5	3,535.1
Float glass	3,780.6	4,494.3	4,712.4	5,022.2	6,509.8	8,016.9	9,347.7	11,310.7
Total	8,433.0	9,936.1	10,861.1	11,460.3	12,848.4	14,727.5	16,544.3	19,219.9
YoY Change (%)								
Automobile glass		6.8	9.3	5.4	(1.0)	4.3	3.6	8.0
Construction glass		36.8	18.6	3.8	(2.3)	8.1	12.4	12.4
Float glass		18.9	4.9	6.6	29.6	23.2	16.6	21.0
Total		17.8	9.3	5.5	12.1	14.6	12.3	16.2
Volume								
Automobile (piece)		12,110.0	12,889.0	13,582.8	13,582.8	13,786.6	14,475.9	15,634.0
Construction (sqm)		16,363.0	19,380.0	20,107.5	21,716.1	20,630.3	22,074.4	23,619.6
Float glass (tonne)		2,927.0	3,510.0	3,856.8	4,435.3	4,790.1	5,077.5	5,585.2
YoY Change (%)								
Automobile (piece)			6.4	5.4	0	1.5	5.0	8.0
Construction (sqm)			18.4	3.8	8.0	(5.0)	7.0	7.0
Float glass (tonne)			19.9	9.9	15.0	8.0	6.0	10.0
ASP								
Automobile (HKD/piece)		271.4	278.8	278.8	276.0	278.8	279.8	279.8
Construction (HKD per sqm)		131.7	131.9	131.9	119.3	135.8	142.5	149.7
Float glass (HKD per tone)		1,535.5	1,342.6	1,302.2	1,467.7	1,673.6	1,841.0	2,025.1
YoY Change (%)								
Automobile (HKD/piece)			2.7	0.0	(1.0)	1.0	0.4	0
Construction (HKD per sqm)			0.1	0	(9.5)	13.8	5.0	5.0
Float glass (HKD per tone)			(12.6)	(3.0)	12.7	14.0	10.0	10.0
Gross margin (%)								
Automobile glass	42.8	43.3	41.8	44.3	49.0	46.9	46.9	46.9
Construction glass	37.2	39.9	35.3	33.9	39.9	38.0	39.0	39.0
Float glass	8.6	19.0	7.0	11.1	27.5	31.7	33.2	33.2
Blended	26.4	31.6	25.2	27.3	36.3	37.0	37.7	37.4
Net margin (%)	14.1	35.4	12.6	18.4	25.0	27.3	27.2	26.8
Cost (HKDm)								
S,G&A	(1,056.7)	(1,250.9)	(1,638.0)	(1,614.5)	(1,822.4)	(2,045.1)	(2,297.4)	(2,668.9)
Financial Expenses	(57.3)	(59.7)	(38.1)	(50.2)	(76.8)	(96.6)	(96.6)	(110.3)
YoY Change (%)								
S,G&A		18.4	30.9	(1.4)	12.9	12.2	12.3	16.2
Financial Expenses		4.2	(36.2)	32.0	53.0	25.7	0	14.2
CAPEX (HKDm)	1,435.3	3,752.3	1,729.0	1,967.0	1,853.0	2,500.0	2,500.0	2,500.0
Net Gearing (%)	35.8	33.6	42.0	37.2	37.3	29.7	30.3	27.7

Source: Company, CGIS Research

Figure 3: Earnings projection

Income Statement (HKDm)	FY2015	FY2016	FY2017	FY2018F	FY2019F
Revenue	11,460	12,848	14,728	16,544	19,220
Growth yoy%	5.5%	12.1%	14.6%	12.3%	16.2%
Gross Profit	3,133	4,659	5,444	6,235	7,191
Growth yoy%	14.6%	48.7%	16.8%	14.5%	15.3%
Selling General & Admin Exp.	(1,615)	(1,822)	(2,045)	(2,297)	(2,669)
Others Operating Expenses/Items	215	342	377	339	393
Operating Income	1,733	3,179	3,777	4,277	4,916
Growth yoy%	n.a.	83%	19%	13%	15%
Interest Expense	(50.2)	(76.8)	(96.6)	(96.6)	(110.3)
Interest and Invest. Income					
Income/(Loss) from Affiliates	317.3	562.6	699.7	849.6	944.0
Other Non-Operating Inc. (Exp.)	0	0	0	0	0
Impairment of Goodwill	0	0	0	0	0
Gain (Loss) On Sale Of Invest.	379	159	317	237	276
Gain (Loss) On Sale Of Assets					
Income Tax Expense	(266)	(607)	(682)	(765)	(875)
Minority Int. in Earnings	(0)	(3)	(0)	4	4
Net Income	2113	3213	4014	4505	5153
Growth yoy%	54.9%	52.1%	24.9%	12.2%	14.4%

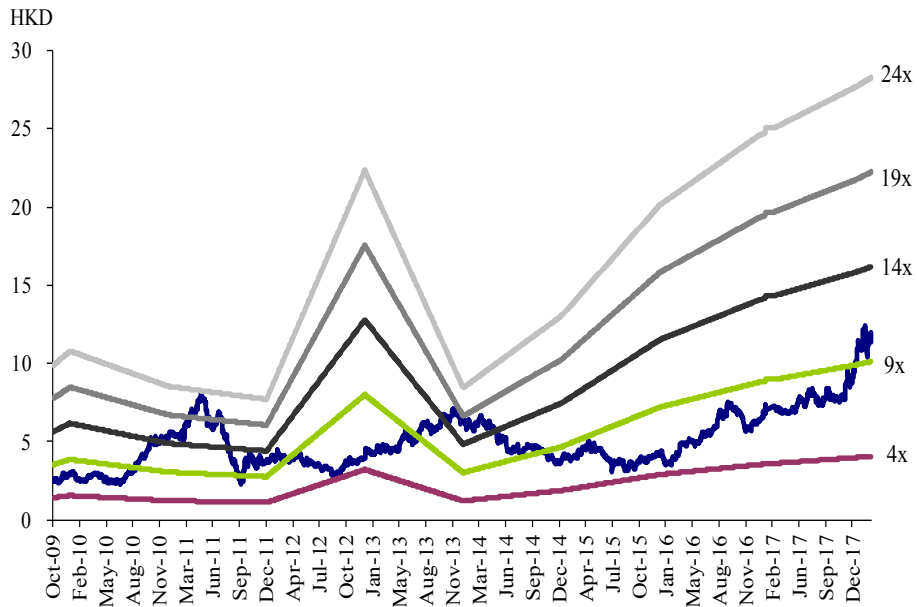
Cash Flow Statement (HKDm)	FY2015	FY2016	FY2017	FY2018F	FY2019F
Net Income	1,796	2,712	3,431	3,652	4,206
Depreciation & Amort.	766	808	883	1,003	1,123
Change in Working Capital	456	40	(869)	(299)	(451)
Cash from Ops.	3,018	3,560	3,445	4,356	4,877
Capital Expenditure	(1,967)	(1,853)	(2,500)	(2,500)	(2,500)
Sale of Property, Plant, and Equipment	-	-	-	-	-
Change in Investing Activities	40	51	55	55	41
Cash from Investing	(1,927)	(1,802)	(2,445)	(2,445)	(2,459)
Net increase in bank borrowings	16	1,646	792	0	0
Issuance of Common Stock	0	0	0	0	0
Common Dividends Paid	(1,043)	(1,552)	(1,905)	(2,224)	(2,544)
Special Dividend Paid	-	-	-	-	-
Other Financing Activities	0	(400)	0	0	0
Cash from Financing	(1,027)	(306)	(1,113)	(2,224)	(2,544)
Net Change in Cash	64	1,451	(113)	(313)	(125)

Balance Sheet (HKDm)	FY2015	FY2016	FY2017	FY2018F	FY2019F
ASSETS					
Cash And Equivalents	1,298	2,763	3,049	2,283	2,157
Receivables	2,381	2,377	3,072	3,411	3,980
Inventory	1,223	1,321	1,698	1,885	2,200
Other Current Assets	93	76	107	107	107
Total Current Assets	4,995	6,537	7,926	7,687	8,445
Net Property, Plant & Equipment	13,177	12,952	16,356	18,377	19,757
Long-term Investments	-	-	-	-	-
Other Intangibles	-	-	-	-	-
Deferred Tax Assets, LT	-	-	-	-	-
Other Long-Term Assets	3,249	4,534	6,017	6,663	7,390
Goodwill	-	-	-	-	-
Accounts Receivable Long-Term	-	-	-	-	-
Total Long Term Assets	16,426	17,486	22,373	25,040	27,147
Total Assets	21,422	24,022	30,299	32,726	35,592
LIABILITIES & EQUITY					
Accounts Payable	2,112	2,297	2,554	2,836	3,309
Accrued Exp.	-	-	-	-	-
Short-term Borrowings	2,514	3,165	2,068	2,068	2,068
Curr. Port. of LT Debt	-	-	-	-	-
Curr. Income Taxes Payable	-	-	-	-	-
Unearned Revenue, Current	-	-	-	-	-
Other Current Liabilities	333	538	535	535	535
Total Current Liabilities	4,959	6,000	5,157	5,439	5,912
Long-Term Debt	3,514	4,509	6,399	6,399	6,399
Def. Tax Liability, Non-Curr.	159	218	335	335	335
Other Non-Current Liabilities	63	48	108	108	108
Total Liabilities	8,696	10,775	11,999	12,281	12,754
Common Stock	4,277	1,719	2,557	4,839	7,449
Additional Paid In Capital	-	-	-	-	-
Retained Earnings	8,442	11,462	15,680	15,542	15,328
Treasury Stock	-	-	-	-	-
Comprehensive Inc. and Other	-	-	-	-	-
Minority Interest	7.2	66.0	69.0	65.2	61.4
Total Equity	12,726	13,247	18,306	20,446	22,838
Total Liabilities And Equity	21,422	24,022	30,305	32,727	35,592

Ratios	FY2015	FY2016	FY2017	FY2018F	FY2019F
Profitability					
Return on Assets %	10.0%	14.1%	14.8%	14.3%	15.1%
Return on Capital %	7.9%	13.0%	13.0%	12.7%	13.5%
Return on Equity %	16.9%	24.8%	25.6%	23.3%	23.9%
Margin Analysis					
Gross Margin %	27.3%	36.3%	37.0%	37.7%	37.4%
SG&A Margin %	14.1%	14.2%	13.9%	13.9%	13.9%
EBIT Margin %	15.1%	24.7%	25.6%	25.8%	25.6%
EBITDA Margin %	21.8%	31.0%	31.6%	31.9%	31.4%
Net Income Margin %	18.4%	25.0%	27.3%	27.2%	26.8%
Asset Turnover					
Total Asset Turnover	0.5x	0.5x	0.5x	0.5x	0.5x
Fixed Asset Turnover	0.7x	0.7x	0.7x	0.7x	0.7x
Accounts Receivable Turnover	4.7x	5.4x	5.4x	5.1x	5.2x
Inventory Turnover	9.4x	9.7x	8.7x	8.8x	8.7x
Liquidity					
Current Ratio	1.0x	1.1x	1.5x	1.4x	1.4x
Quick Ratio	0.7x	0.9x	1.2x	1.0x	1.0x
Avg. Days Sales Out.	75.8	67.5	76.1	75.3	75.6
Avg. Days Inventory Out.	38.9	37.5	42.1	41.6	41.8
Avg. Days Payable Out.	89.6	98.3	95.4	95.4	93.2
Avg. Cash Conversion Cycle	62.2	61.1	79.6	79.4	79.5
Net Debt to Equity	37%	37%	30%	30%	28%
Growth Over Prior Year					
Total Revenue	5.5%	12.1%	14.6%	12.3%	16.2%
Net Income	54.9%	52.1%	24.9%	12.2%	14.4%
Payout Ratio %	49.4%	48.3%	47.5%	49.4%	49.4%

Sources: Company, CGIS Research

Figure 4: XYG's PER trend



Sources: Bloomberg, CGIS Research estimates

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- SELL : share price will decrease by >20% within 12 months in absolute terms
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