August 27, 2014
Company Report
Rating: BUY
TP: HK$ 8.54

H-Share price (HK$)	6.92
Est. share price return	23.41%
Est. dividend yield	1.45%
Est. total return	24.86%

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Key Data

52Wk H/L(HK$)	7.35 / 5.35
Issued shares (mn)	13,803
H-Shares (mn)	2,024
A-Shares (mn)	11,779
Market cap	
H-shares (HK$ mn)	14,006
A-Shares (mn) (RMB mn)	59,484
3-mth avg daily turnover (HK$ mn)	102.5
Major shareholder(s) (%):	
CSR Group (SOE)	56.48

Source(s): Company, Bloomberg, ABCI Securities

1H 14 Revenue breakdowns (%)

Locomotives	17.98
Passenger carriages	3.87
Freight wagons	5.99
MUs	28.22
Rapid transit vehicles	12.36
New Businesses	12.27
Others	19.31

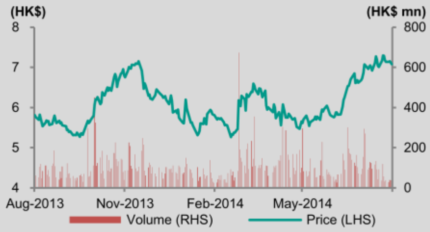
Source(s): Company, ABCI Securities

Share performance (%)

	Absolute	Relative*
1-mth	3.20	(1.48)
3-mth	24.32	13.69
6-mth	22.01	9.65

*Relative to HSI
Source(s): Bloomberg, ABCI Securities

Stock performance



Source(s): Bloomberg, ABCI Securities

CSR (1766 HK)
High earnings visibility in 2H14; reiterate BUY

- Revenue and net income were up 36.6% YoY and 41.1% YoY in 1H14 mainly on increased MU delivery.
- GPM soared to over 18% in 1H14 under changes in product mix with a larger share of MU
- Total backlog at end-1H14 was RMB 122,300mn. Together with CRC's MU procurement in Aug 2014, earnings visibility in 2H14 is clear
- We revise up our FY14E/15E earnings forecasts. Our new TP of HK$ 8.54 is based on 17x of FY14E EPS, equivalent to the upper quartile of its historical P/E since 2011. Reiterate **BUY**

Good 1H14 results. Thanks to resumption of procurement by China Railway Corporation (CRC), the Group's revenue increased by 36.6% YoY to RMB 49,771mn in 1H14. Increased delivery of multiple units (MUs) for high-speed railway (HSR) in 1H14 drovesegment revenue up by ~1.8 times YoY to RMB 14,045mn, contributing to ~28% of the total revenue during the period. Due to changes in product mix with more MUs delivered and reduced unit cost on revenue increment, GPM rose 1.92ppt YoY (or 1.19ppt HoH) to 18.7%; net income was up 41.1% YoY to RMB 2,062mn in 1H14.

Procurement by CRC in 2014. China Railway Corporation (CRC) announced the first MU procurement for 2014 on Aug 22. The tendering was separated into 2 parts: 57 units for 250 km/hr and 175 units for 350 km/hr. We estimate that the total value of this tender is ~RMB 38.5bn, of which CSR would possibly win ~50% of the tendering amount based on track record. The procured MUs are expected to be delivered in 4Q14-1H15, which would secure income growth of the Group in the near future and is beneficial to its supplier, such as ZCSR (3898 HK, BUY).

Abundant backlog enhances earnings visibility in 2H14. Total backlog of CSR at end-1H14 was RMB 122,300mn, up 112.7% YoY, mainly driven by the resumption of CRC's MU procurement and rapid expansion of urban railway transport that buoys demand for rolling stock. With CRC's procurement in Aug 2014 and the Group's huge backlog by end-1H14, we expect its 2H14 revenue to surge by ~60% HoH.

Reiterate BUY. Looking forward, we expect demand for rolling stock to rise, driven by the completion of new railway lines, development of urban rails in the major cities, as well as growth in overseas railway procurement. We revise up our earnings projections for 2014E-15E by 15.7% and 16.5% on CRC's increased CAPEX budget. Our TP of HK$ 8.54 (previous TP: HK$ 7.10) is equivalent to 17x of FY14E EPS, representing the upper quartile of CSR's historical P/E since 2011. We expect CRC to announce more rolling stock procurement in the coming quarters. With this positive catalyst, we therefore reiterate BUY on CSR.

Risk factors: 1) CRC may delay MU procurement and CSR's earnings growth could be slowed as a result in the coming years; 2) Payout ratio may decrease in 2014-15 on higher working capital required for rolling stock delivery

Results and Valuation

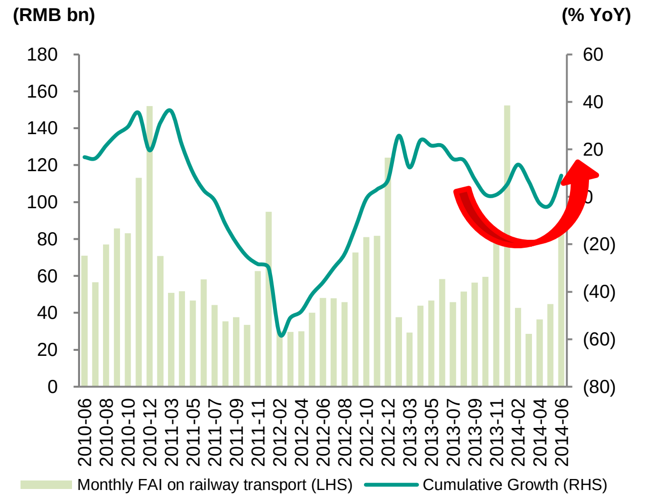
FY ended Dec 31	2012A	2013A	2014E	2015E	2016E
Revenue (RMB mn)	**89,019**	**96,525**	**129,940**	**150,951**	**164,202**
Chg (%,YoY)	11.95	8.43	34.62	16.17	8.78
Net Income (RMB mn)	**4,009**	**4,140**	**5,567**	**6,674**	**7,276**
Chg (%,YoY)	3.75	3.27	34.47	19.88	9.02
EPS (RMB)	**0.299**	**0.300**	**0.403**	**0.484**	**0.527**
P/E (x)	-	18.53	13.78	11.50	10.54
BVPS (RMB)	2.444	2.649	2.962	3.365	3.795
P/B (x)	-	2.10	1.88	1.65	1.46
DPS(RMB)	0.093	0.090	0.081	0.097	0.105
Yield (%)	-	1.62	1.45	1.74	1.90
ROAE (%)	14.49	11.95	14.38	15.28	14.72
Net gearing (%)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash

* Net gearing=Net debt/Total equity
Source(s): Bloomberg, ABCI Securities estimates

Railway transport investment to increase

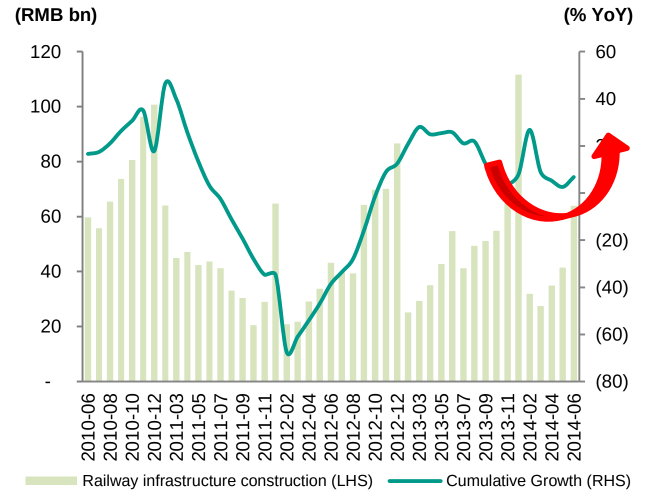
CRC's CAPEX is budgeted at RMB 800bn for 2014, upward revised from RMB 720bn. We believe railway investment would grow by 20.1% YoY for the full year. Since total railway infrastructure investment and CRC's CAPEX for 1H14 were up only by 6.77% YoY and 8.92% YoY, railway investment would escalate in 2H14. We believe CRC will likely procure MUs soon, supporting sales in CSR in 2H14/2015.

Exhibit 1: Monthly fixed-asset investment by CRC and YTD growth in 1H10-1H14



Source(s): China Railway Corporation, ABCI Securities

Exhibit 2: Monthly infrastructure investment by CRC and YTD growth in 1H10-1H14



Source(s): China Railway Corporation, ABCI Securities

Exhibit 3: FY14E-15E financial projections for CSR

	FY14E			FY15E		
	Previous	**New**	***Chg (%)***	**Previous**	**New**	***Chg (%)***
Revenue (RMB mn)	**105,130**	**129,940**	***23.60***	**118,525**	**150,951**	***27.36***
Gross profit (RMB mn)	**18,482**	**23,383**	***26.52***	**21,014**	**27,229**	***29.57***
GPM (%)	*17.58*	*17.99*	*0.41ppt*	*17.73*	*18.04*	*0.31ppt*
Net income (RMB mn)	**4,811**	**5,567**	***15.71***	**5,731**	**6,674**	***16.45***
Net margin (%)	*4.58*	*4.28*	*(0.29ppt)*	*4.84*	*4.42*	*(0.41ppt)*
EPS (RMB)	0.349	0.403	*15.56*	0.415	0.484	*16.51*
BVPS (RMB)	2.875	2.962	*3.03*	3.220	3.365	*4.50*
DPS (RMB)	0.070	0.081	*15.23*	0.083	0.097	*16.51*

Source(s): ABCI Securities estimates

The huge backlog of CSR indicates that procurement of rolling stock components in 2H14 would stay high, benefiting CSR's supplier and 52%-owned subsidiary, ZCSR.

Exhibit 4: Financial summary of CSR in 1H12-1H14

(RMB mn)	1H12	2H12	1H13	2H13	1H14	(% YoY)
Revenue	**41,850**	**47,169**	**36,441**	**60,084**	**49,771**	***36.58***
Less: Operating cost	33,941	39,323	30,329	49,567	40,468	*33.43*
Gross Profit	**7,909**	**7,846**	**6,112**	**10,517**	**9,303**	***52.21***
GPM (%)	*18.90*	*16.63*	*16.77*	*17.50*	*18.69*	*1.92ppt*
Selling and distribution cost	1,354	1,799	1,044	2,042	1,670	*59.96*
Administrative cost	3,694	3,993	3,273	5,289	4,364	*33.33*
SG&A (RMB mn)	**5,048**	**5,792**	**4,317**	**7,331**	**6,034**	***39.77***
SG&A-to-revenue (%)	*12.06*	*12.28*	*11.85*	*12.20*	*12.12*	*0.28ppt*
Net profit (ex. MI)	**1,919**	**2,090**	**1,461**	**2,679**	**2,062**	***41.14***
Net profit margin (%)	*4.59*	*4.43*	*4.01*	*4.46*	*4.14*	*0.13ppt*
Total debt	14,938	9,323	11,841	11,175	21,671	*83.02*
Less: Total cash and equivalents	12,810	15,044	13,669	16,400	19,137	*40.00*
Net debt (cash)	**2,128**	**(5,721)**	**(1,828)**	**(5,225)**	**2,534**	***N/A***
Total equity	**36,725**	**39,510**	**40,689**	**46,155**	**47,257**	***16.14***
Net gearing (%)	***5.79***	***(14.48)***	***(4.49)***	***(11.32)***	***5.36***	***9.85ppt***

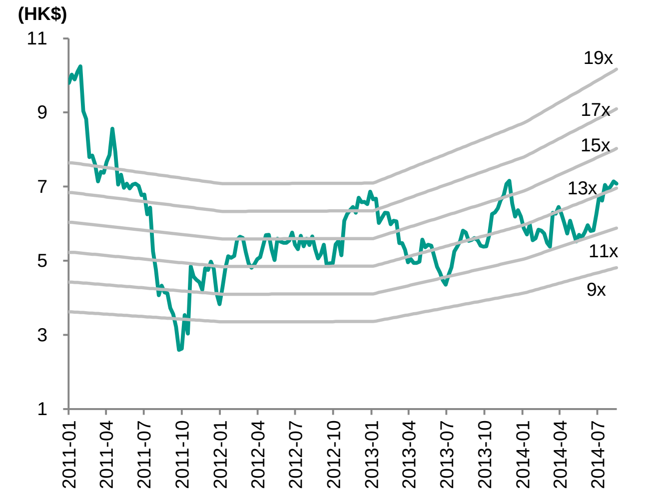
Source(s): Company, ABCI Securities

Exhibit 5: Financial summary of ZCSR in 1H12-1H14

(RMB mn)	1H12	2H12	1H13	2H13	1H14	(% YoY)
Revenue	**3,174**	**4,012**	**2,603**	**6,178**	**5,150**	***97.85***
Less: Operating cost	2,070	2,733	1,628	4,067	3,324	*104.18*
Gross Profit	**1,104**	**1,279**	**975**	**2,111**	**1,826**	***87.28***
GPM (%)	*34.78*	*31.88*	*37.46*	*34.17*	*35.46*	*(2.00ppt)*
Selling and distribution cost	143	191	131	367	275	*109.92*
Administrative cost	434	429	366	639	494	*34.97*
SG&A (RMB mn)	**577**	**620**	**497**	**1,006**	**769**	***54.73***
SG&A-to-revenue (%)	*18.18*	*15.45*	*19.09*	*16.28*	*14.93*	*(4.16ppt)*
Net profit (ex. MI)	**546**	**678**	**400**	**1,067**	**857**	***114.25***
Net profit margin (%)	*17.20*	*16.90*	*15.37*	*17.27*	*16.64*	*1.27ppt*
Total debt	28	69	66	83	60	*(9.09)*
Less: Total cash and equivalents	1,341	2,319	1,583	3,136	2,729	*72.39*
Net debt (cash)	**(1,313)**	**(2,250)**	**(1,517)**	**(3,053)**	**(2,669)**	***N/A***
Total equity	**5,618**	**6,319**	**6,307**	**9,150**	**9,656**	***53.10***
Net gearing (%)	***(23.37)***	***(35.61)***	***(24.05)***	***(33.37)***	***(27.64)***	***(3.59ppt)***

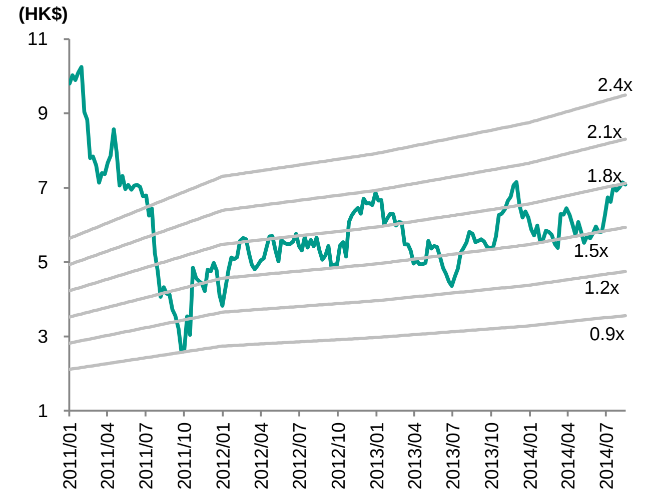
Source(s): Company, ABCI Securities

Exhibit 6: P/E band of CSR in 1M11-8M14



Source(s): Company, Bloomberg, ABCI Securities estimates

Exhibit 7: P/B band of CSR in 1M11-8M14



Source(s): Company, Bloomberg, ABCI Securities estimates

Exhibit 8: Valuation of domestic and international rolling-stock manufacturers

		Mkt cap	As of 26/8/2014		P/E (x)		EPS (%YoY)		P/B (x)		ROAE (%)	
Company	**Ticker**	**(HK$ mn)**	**CRY**	**Share Price**	**FY14E**	**FY15E**	**FY14E**	**FY15E**	**FY14E**	**FY15E**	**FY14E**	**FY15E**
Domestic Rolling Stock Makers												
CSR-H	1766 HK	14,006	HKD	6.92	13.78	11.50	34.47	19.88	1.88	1.65	14.38	15.28
CSR-A	601766 CH	74,925	RMB	5.05	12.52	10.44	34.47	19.88	1.70	1.50	14.38	15.28
CNR-H	6199 CH	13,636	HKD	6.39	13.98	12.36	14.25	13.13	1.55	1.41	12.30	11.88
CNR-A	601299 CH	63,227	RMB	4.90	10.52	8.99	16.50	16.95	1.16	1.04	10.83	9.70
ZCSR	3898 HK	31,268	HKD	26.60	13.91	12.46	23.11	11.58	2.41	2.11	18.57	18.04
Zhuzhou Times	600458 CH	8,373	RMB	10.05	25.13	18.96	90.48	32.50	2.17	2.06	8.70	11.01
Changchun Eurasia Group	600697 CH	3,817	RMB	19.05	10.07	8.24	22.79	22.32	1.90	1.59	22.41	21.00
Jinxi Axle	600495 CH	9,418	RMB	11.14	30.69	29.32	70.82	4.68	2.86	2.58	6.37	9.27
Sector 's Weighted Average					**13.53**	**11.60**	**29.89**	**17.30**	**1.72**	**1.53**	**13.40**	**13.53**
International Rolling Stock Makers												
Alstom	ALO FP	85,037	EUR	26.89	11.41	10.52	30.94	8.40	1.39	1.27	13.76	11.47
Bombardier Inc	BBD/A CN	47,558	CAD	3.88	9.30	8.36	22.90	11.29	2.36	1.98	27.51	25.38
CAF	CAF SM	10,554	EUR	301.00	10.55	9.62	8.44	9.68	1.37	1.26	13.62	13.62
Vossloh A.G.	VOS GR	6,996	EUR	51.33	(34.75)	15.40	(218.16)	(325.66)	1.64	1.50	(17.09)	9.58
Faiveley Transport	LEY FP	7,854	EUR	52.54	12.98	12.02	15.63	7.98	1.23	1.14	9.94	9.85
Nippon Sharyo	7102 JP	4,045	JPY	370.00	17.79	14.86	(56.67)	19.71	0.81	0.78	11.86	5.37
Kinki Sharyo	7122 JP	1,662	JPY	323.00	(12.38)	22.28	(69.62)	(155.56)	0.79	0.76	(6.17)	3.48
Sector 's Weighted Average					**8.76**	**10.34**	**12.59**	**(6.36)**	**1.65**	**1.47**	**15.99**	**15.26**
Overall Weighted Average					**11.49**	**11.06**	**22.49**	**7.17**	**1.69**	**1.50**	**14.51**	**14.27**

Source(s): Bloomberg, ABCI Securities estimates

Financial statements of the Group

Consolidated income statement (2012A-2016E)

FY Ended Dec 31 (RMB mn)	FY12A	FY13A	FY14E	FY15E	FY16E
Revenue	**89,019**	**96,525**	**129,940**	**150,951**	**164,202**
Locomotives	14,396	19,846	21,490	24,714	27,882
Passenger carriages	7,753	6,590	7,044	7,886	8,832
Freight wagons	10,419	9,932	10,645	12,488	14,203
MUs	21,524	19,189	40,750	49,514	49,096
Rapid transit vehicles	7,947	8,251	15,561	19,999	25,745
New Businesses	10,902	13,053	13,803	14,672	15,681
Others	16,078	19,664	20,647	21,680	22,764
COGS	**(73,264)**	**(79,896)**	**(106,558)**	**(123,722)**	**(134,749)**
Gross profit	**15,755**	**16,629**	**23,383**	**27,229**	**29,453**
SG&A	(10,840)	(11,647)	(15,897)	(18,297)	(19,765)
Other income and gains	**678**	**951**	**783**	**987**	**1,115**
Pre-tax profit	**5,593**	**5,933**	**8,268**	**9,919**	**10,803**
Income tax	(741)	(859)	(1,240)	(1,488)	(1,620)
Net profit	**4,852**	**5,074**	**7,028**	**8,431**	**9,183**
Profit attributable to:					
Minority interests	843	934	1,461	1,757	1,906
Equity shareholders of the Company	**4,009**	**4,140**	**5,567**	**6,674**	**7,276**
EPS (RMB)	**0.299**	**0.300**	**0.403**	**0.484**	**0.527**
DPS (RMB)	**0.093**	**0.090**	**0.081**	**0.097**	**0.105**
EBIT	**6,422**	**6,530**	**9,012**	**10,683**	**11,569**
EBITDA	**8,205**	**8,470**	**11,096**	**12,860**	**13,832**

*: Revenue excludes business tax and surcharges
Source(s): Company, ABCI Securities estimates

Consolidated balance sheet (2012A-2016E)

As of Dec 31 (RMB mn)	FY12A	FY13A	FY14E	FY15E	FY16E
Current assets	**72,261**	**82,953**	**101,841**	**105,207**	**116,699**
Cash and equivalent	15,044	16,400	21,705	19,010	21,100
Trade and bill receivables	30,355	40,317	45,123	49,996	53,474
Inventories	18,770	17,721	26,070	26,809	32,260
Other current assets	8,092	8,515	8,943	9,393	9,865
Non-current assets	**32,956**	**38,177**	**42,832**	**47,657**	**48,098**
Property, plant and equipment	22,996	25,231	26,396	27,485	28,504
Intangible assets	5,367	5,818	6,252	6,669	7,071
Long-term investments	3,099	3,662	4,028	4,431	4,874
Other non-current assets	1,494	3,466	6,155	9,072	7,650
Total assets	**105,217**	**121,130**	**144,672**	**152,865**	**164,797**
Current liabilities	**61,538**	**67,000**	**84,611**	**85,334**	**89,247**
Trade and bill payables	39,663	45,373	56,806	57,086	57,358
Receipts in advance	7,272	7,142	10,658	10,020	12,473
Short term borrowings	8,596	7,606	9,580	9,904	10,259
Other current liabilities	6,007	6,879	7,567	8,324	9,156
Non-current liabilities	**4,169**	**7,975**	**8,413**	**8,916**	**9,469**
Long-term borrowings	727	3,569	3,566	3,585	3,605
Other non-current liabilities	3,442	4,406	4,847	5,331	5,864
Total liabilities	**65,707**	**74,975**	**93,023**	**94,250**	**98,716**
Minority interests	**6,754**	**9,595**	**10,764**	**12,169**	**13,695**
Shareholders' equities	**32,755**	**36,560**	**40,885**	**46,445**	**52,387**
BVPS (RMB)	**2.444**	**2.649**	**2.962**	**3.365**	**3.795**

Source(s): Company, ABCI Securities estimates

Consolidated cash flow statement (2012A-2016E)

FY ended Dec 31 (RMB mn)	FY12A	FY13A	FY14E	FY15E	FY16E
Profit before tax	**5,593**	**5,933**	**8,268**	**9,919**	**10,803**
Changes in depreciation and amortization	1,783	1,940	2,084	2,176	2,263
Changes in working capital	(4,764)	(2,034)	(5,537)	(6,276)	(8,496)
Financial cost	764	546	707	726	728
Income tax paid	(855)	(968)	(1,247)	(1,495)	(1,629)
Others	(126)	(5)	-	-	-
CF Operating	**2,395**	**5,412**	**4,275**	**5,049**	**3,669**
Increase in PP&E	(3,104)	(4,123)	(3,000)	(3,000)	(3,000)
Increase in intangible assets	(768)	(458)	(683)	(683)	(683)
Others	(373)	(2,664)	-	-	-
CF Investing	**(4,245)**	**(7,245)**	**(3,683)**	**(3,683)**	**(3,683)**
Capital injection	9,310	2,697	-	-	-
Net debt financing	(11,166)	1,847	1,971	342	375
Dividend payout	(2,782)	(1,507)	(1,242)	(1,113)	(1,335)
Interest paid	(970)	(545)	(707)	(726)	(728)
Others	(64)	(1,019)	4,691	(2,564)	3,792
CF Financing	**(5,672)**	**1,473**	**4,713**	**(4,061)**	**2,105**
Net change in cash	**(7,522)**	**(360)**	**5,305**	**(2,695)**	**2,091**
Cash at the beginning	23,730	15,044	16,400	21,705	19,010
Adjustment (Time deposit & FX effect)	(1,164)	1,716	-	-	-
Cash at the end	**15,044**	**16,400**	**21,705**	**19,010**	**21,100**

Source(s): Company, ABCI Securities estimates

Key operating and financial ratios (2012A-2016E)

FY ended Dec 31	FY12A	FY13A	FY14E	FY15E	FY16E
Sales mixed (%)					
Locomotives	16.17	20.56	16.54	16.37	16.98
Passenger carriages	8.71	6.83	5.42	5.22	5.38
Freight wagons	11.70	10.29	8.19	8.27	8.65
MUs	24.18	19.88	31.36	32.80	29.90
Rapid transit vehicles	8.93	8.55	11.98	13.25	15.68
New Businesses	12.25	13.52	10.62	9.72	9.55
Others	18.06	20.37	15.89	14.36	13.86
Profit & loss ratios (%)					
Gross margin	17.70	17.23	17.99	18.04	17.94
Net profit margin	4.50	4.29	4.28	4.42	4.43
Effective tax rate	13.25	14.48	15.00	15.00	15.00
Growth (%)					
Revenue	11.95	8.43	34.62	16.17	8.78
Gross profit	5.95	5.55	40.61	16.45	8.17
EBIT	(1.25)	1.68	38.02	18.54	8.29
EBITDA	1.77	3.23	31.01	15.89	7.56
Net profit	3.75	3.27	34.47	19.88	9.02
Balance sheet ratios					
Current ratio (x)	1.17	1.24	1.20	1.23	1.31
Quick ratio (x)	0.68	0.64	0.67	0.65	0.71
Cash ratio (x)	0.24	0.24	0.26	0.22	0.24
Trade and bill receivables days	99	134	120	115	115
Trade and bill payables turnover days	168	194	175	168	155
Inventory turnover days	91	83	75	78	80
Total debt / equity ratio (%)	23.60	24.21	25.45	23.01	20.98
Net debt / equity ratio (%)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash
Returns (%)					
ROAE	14.49	11.95	14.38	15.28	14.72
ROAA	4.05	3.66	4.19	4.49	4.58
Payout ratio	30.98	30.00	20.00	20.00	20.00

Source(s): Company, ABCI Securities estimates

Disclosures

Analyst Certification

I, Steve Wong, being the person primarily responsible for the content of this research report, in whole or in part, hereby certify that all of the views expressed in this report accurately reflect my personal view about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report. I and/or my associates have no financial interests in relation to the listed company (ies) covered in this report, and I and/or my associates do not serve as officer(s) of the listed company (ies) covered in this report.

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Definition of equity rating

Rating	Definition
Buy	Stock return ≥ Market return rate
Hold	Market return – 6% ≤ Stock return < Market return rate
Sell	Stock return < Market return – 6%

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate from 2007-2011

Time horizon of share price target: 12-month

Definition of share price risk

Rating	Definition
Very high	2.6 ≤180 day volatility/180 day benchmark index volatility
High	1.5 ≤ 180 day volatility/180 day benchmark index volatility < 2.6
Medium	1.0 ≤180 day volatility/180 day benchmark index volatility < 1.5
Low	180 day volatility/180 day benchmark index volatility < 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index.

Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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