农银国际
ABC INTERNATIONAL
ABCI SECURITIES COMPANY LIMITED

24 December 2012

Equity Focus

Lonking (3339 HK) – Sell

Construction & Farm Machinery Industry

Key Data

Share price (HK$)	2.14
Target price (HK$)	1.48
Upside potential (%)	-30.8
52Wk H/L(HK$)	3.50 / 1.01
Issued shares (mn)	4,280
Share market cap (HK$mn)	9,159
30-day avg vol (HK$mn)	96.9
Major shareholder (%):	
Li San Yim and spouse	55.69

Source: Company, Bloomberg, ABCI Securities

Sales breakdown in 1HFY12 (%)

Wheel loader	67.9
Excavator	11.2
Fork lift	8.9
Others	11.9

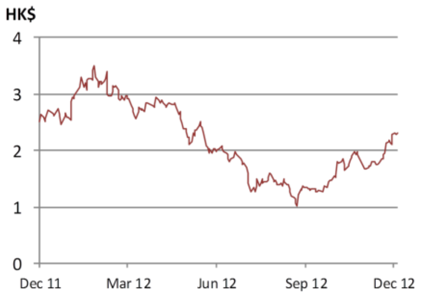
Source: Company

Share performance (%)

	Absolute	Relative*
1-mth	35.9	27.7
3-mth	79.1	63.0
6-mth	11.6	-3.7

**Relative to Hang Seng Index*
Source: Bloomberg

1 year price performance



Source: Bloomberg

Analyst

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Previous report
Date: 12 November 2012
Rating: Sell
Target price: HK$1.48

Keep falling sales and losing market share

The sales volume on wheel loader market was disappointed in Nov. The decline in sales volume deepened from -25.6% YoY in 1H12 to -29.4% YoY in 1-11M12. The market share of Lonking dropped from 18.1% in FY11 to 15.0% in 1-11MFY12. The sales volume of its wheel loader dropped by 39.0% YoY in 1-11MFY12, or 9.6ppt higher than market average. Although the counter has rebounded sharply last three months, the rebound was lack of fundamental support. We maintain "Sell" rating on Lonking with a TP of HK$1.48.

Sales decline yet to bottom. The counter has rebounded sharply last three months on the expectations of business recovery, but its sales performance kept deteriorating in November. Its sales volume of wheel loader, which is a key product and is expected to contribute 79.5% of its total gross profit in FY12, declined by 39.0% YoY in 1-11MFY12. The drop was deepened compared with -37.7% in 1-10MFY12.

Losing market share. With growing signs of the recovery on downstream construction industry, the full recovery of wheel loader industry is expected to be in in 2H13. However, its highly leveraged financial position (est. net debt/equity of 59.9% at end FY12) will constrain the Group to offer competitive credit terms to customers and it is losing market share to peers subsequently. Its market share was dropping since 2Q12. We believe that its pace of recovery is slow compared with its peers, such as SDLG, the largest wheel loader maker in China based on sales volume in 1-11M12.

Maintain "Sell" rating. We observe the demand for construction machinery is recovering in this quarter, but it is not a broad base recovery. The Group's business has yet to benefit from this recovery cycle, but its share price has gone up 35.9% in a month. Weak competitiveness of its wheel loader showed by falling market share is our major concern. We reiterate our "Sell" rating on Lonking with a TP of HK$1.48.

Risk factors: Prolong weakening construction industry; Losing market share to peers; Credit and liquidity risk.

Forecast and Valuation

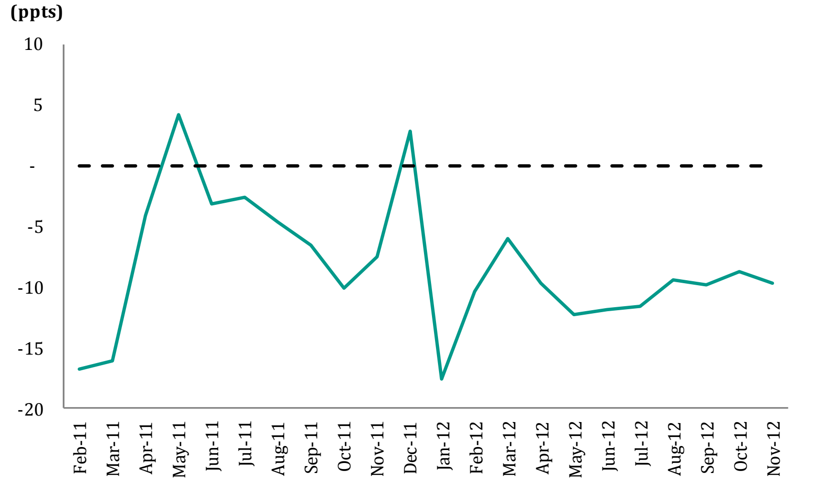
FY ended Dec 31	FY10A	FY11A	FY12E	FY13E	FY14E
Revenue (Rmb mn)	12,020	12,720	9,310	11,318	13,940
Chg (%YoY)	*74.2*	*5.8*	*(26.8)*	*21.6*	*23.2*
Net Income (Rmb mn)	1,766	1,730	496	832	953
Chg (%YoY)	*120.8*	*(2.1)*	*(71.3)*	*67.5*	*14.6*
EPS (Rmb)	0.413	0.404	0.116	0.194	0.223
Chg (%YoY)	*120.8*	*(2.1)*	*(71.3)*	*67.5*	*14.6*
PE (x)	-	4.3	15.0	9.0	7.8
PB (x)	-	1.16	1.10	1.02	0.93
Yield (%)	-	7.0	2.0	3.4	3.8
ROAA (%)	15.2	11.7	3.2	5.3	5.7
ROAE (%)	39.1	29.7	7.5	11.8	12.4
Net debt/total equity (%)	57.1	55.1	59.9	34.5	24.0

Source: Company, ABCI Securities estimates

The spread = (growth of total market sales volume of wheel loader in China) – (Growth of the sales volume of wheel loader of the Group). The spread fell below zero most of the time since 2011.

It reflected that the Group declined at a faster way compared with the average of peers'. The market share of the Group is reducing toward its competitors.

Growth spread of sales volume growth of wheel loader of Lonking and the industry



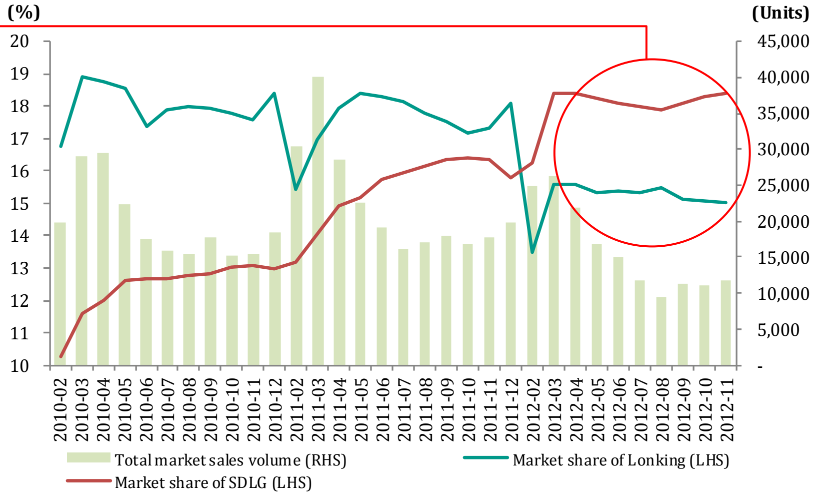
Source: CCMA, ABCI Securities

The market share of Lonking is dropping against its peers. The Group's market share drops from 18.1% in FY11 to 15.0% in 1-11MFY12.

In the meanwhile, the market share of SDLG, its largest competitor, increased from 15.8% in FY11 to 18.4% in 1-11MFY12.

Profile of SDLG**: SDLG is a leading Brand in the Chinese construction machinery industry, especially for wheel loaders. SDLG is a brand of Shandong Lingong Construction Machinery Co. Ltd, one of the five largest manufacturers of loaders in the world. Founded in 1972, In 2006, Lingong sold 70% of their shares to **Volvo CE (VOLVB SS) and now their share is 82%.

Market share of Lonking and SDLG based on YTD sales volume of wheel loaders



Source: CCMA, ABCI Securities

Peer group valuation and earnings forecasts summary of construction machinery sector

Company	Ticker	MKT CAP* (HKD mn)		Share Price	PE (x) Current Year	PE (x) Next Year	EPS Change (%) Current Year	EPS Change (%) Next Year	ROE (%) Current Year	ROE (%) Next Year
Construction Machinery Maker										
CATERPILLAR INC	CAT US	445,479	USD	87.90	9.65	10.13	19.19	(4.69)	37.22	28.95
KOMATSU LTD	6301 JP	188,441	JPY	2,076.00	11.12	10.89	7.64	2.08	18.53	14.16
SANY HEAVY INDUS	600031 CH	93,247	CNY	9.87	10.02	8.61	(13.52)	16.45	32.92	26.14
ZOOMLION HEAVY-H	1157 HK#	85,439	HKD	11.24	7.52	6.06	14.91	23.95	24.00	24.40
ZOOMLION HEAVY-A	000157 CH#	87,518	CNY	9.10	7.57	6.11	14.91	23.95	24.00	24.40
XCMG CONSTRUCT-A	000425 CH	29,205	CNY	11.38	7.28	6.40	(4.70)	13.76	26.18	23.65
GUANGXI LIUGONG	000528 CH	13,579	CNY	9.70	18.87	13.84	(56.07)	36.38	4.01	5.86
TEREX CORP	TEX US	22,789	USD	26.78	13.29	10.42	391.46	27.59	10.37	13.00
TADANO	6395 JP	8,119	JPY	679.00	49.69	17.28	(44.83)	187.62	2.30	6.70
SHANTUI CONST-A	000680 CH	6,815	CNY	4.81	(22.17)	13.29	(151.67)	(266.82)	1.25	5.15
XIAMEN XGMA-A	600815 CH	6,700	CNY	6.74	11.42	12.77	(20.27)	(10.51)	10.83	8.99
LONKING HOLDINGS	3339 HK#	9,159	HKD	2.14	14.83	8.85	(71.30)	67.53	7.50	11.80
Sector Weighted Average					**9.91**	**9.46**	**17.20**	**5.78**	**28.62**	**23.63**

** The market capital value of the companies are translated into HKD*
 # ABCI Securities estimates
Source: Bloomberg, (The data in the table is as at December 21, 2012)

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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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