

Company Report

China Coal (1898 HK) – Hold China Coal & Consumable Fuels Industry June 28, 2013

Rating: Hold
TP: HK\$4.48

Key Data

H-Share price (HK\$)	4.04
Upside potential (%)	10.89
52Wk H/L(HK\$)	9.04/4.01
Issued shares (mn)	13,259
H Shares (mn)	4,107
A Shares (mn)	9,152
Market cap	
- H Shares (HK\$m)	16,592
- A Shares (Rmb mn)	44,387
3-mth avg daily turnover (HK\$m)	213.06
Major shareholder (%):	
China Coal Group Corp Ltd	57.54%

Source: Company, Bloomberg, ABCI Securities

Revenue composition in FY12 (%)

Coal	82
Coke and coal-chemical product	5
Machinery	9
Others	4

Source: Company, ABCI Securities

Share performance (%)

	Absolute	Relative*
1-mth performance	(24.6)	(13.8)
3-mth performance	(41.6)	(33.3)
6-mth performance	(51.5)	(41.9)

*Relative to HSCFI Index

Source: Bloomberg, ABCI Securities

1 year price performance



Source: Bloomberg, ABCI Securities

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Kick-start price war in domestic market

We revise down China Coal's EPS as price war begins and is expected to intensify in 3Q. China Coal slashed ASP late this month and Shenhua (1088 HK) reacted with much lower ASP. The price war signals the sluggish demand in the downstream. The stock plunged to FY13 P/B of 0.46x but lacks upside catalyst. **HOLD.**

Price war begins. The *Economic Information*, an official financial newspaper reported on June 27th that China Coal lowered its 5,500kcal product to Rmb582/t on 24 June, five years' low and Rmb21/t lower than the Bohai-Rim Steam Coal Price Index, which was Rmb603/t on June 26. Our channel check indicates that the group has lowered spot prices of its coal products.

After China Coal slashed the coal price, its major competitor China Shenhua follows suit and lowers similar grade coal price to Rmb580/t. We believe price war has ignited, other small players will follow to slash coal price in July. Large players such as China Shenhua with high proportion of long-term contract sales will also suffer as the long-term contract price will be regularly reset and based on the monthly spot price.

Revise down EPS estimates. China Coal's spot sales accounted for 52.3% of the total domestic sales in FY12. Its price cut signals very weak domestic demand in summer season and over-supply situation is deteriorating in domestic market. Gross profit margins of coal producers will be squeezed in Q3 when price war is going to intensify. Accordingly, we revise down China Coal's FY13E EPS by 8.63% from Rmb0.556 to Rmb0.508, which is 4.2% below market consensus.

Slash target price. We lower our target FY13 PER of the stock to 7.0x in view of increasing downside risk of earnings. The latest TP is HK\$4.48 (vs previous HK\$6.0). Although the stock has underperformed, share price has yet to bottom as price war factor has not been discounted by the market.

Risk factors: 1) coal price risk; 2) downside earnings risk; 3) regulatory and policy risk; 4) change of tax regimes.

Performance and Valuation

FY ended Dec 31	2010A	2011A	2012A	2013E	2014E
Turnover (Rmb mn)	70,303	90,865	87,292	86,086	88,491
Chg (%.yoy)	32.2	29.2	(3.9)	(1.4)	2.8
Net Income (Rmb mn)	7,466	9,955	8,842	6,736	6,751
Chg (%.yoy)	0.8	33.3	(11.2)	(23.8)	0.2
EPS (Rmb)	0.56	0.75	0.667	0.508	0.509
Chg (%.yoy)	0.0	34.1	(11.2)	(23.8)	0.2
BVPS (Rmb)	5.6	6.2	6.5	6.9	7.3
Chg (%.yoy)	8.0	11.4	5.1	5.6	5.3
P/E (x)	-	-	4.8	6.3	6.3
P/B (x)	-	-	0.49	0.46	0.44
Dividend	0.16	0.22	0.21	0.14	0.14
Dividend yield (%)	-	-	6.6	4.5	4.5
ROAE (%)	10.5	12.7	10.4	7.6	7.2
ROAA (%)	6.4	7.0	5.1	3.5	3.3

Source: Company, Bloomberg, ABCI Securities estimates (assuming Rmb1.0=HK\$1.26)



Consolidated income statements forecast

As of Dec 31 (Rmb mn)	2010A	2011A	2012A	2013E	2014E
Revenue	70,303	90,865	87,292	86,086	88,491
Coal	55,839	74,038	71,783	70,267	71,882
Coke and coal-chemical product, Rmb mn	4,888	5,301	4,185	4,269	4,482
Machinery, Rmb mn	6,095	7,733	7,885	8,042	8,444
Others, Rmb mn	3,480	3,793	3,439	3,508	3,683
Cost of sales	(55,825)	(72,052)	(69,989)	(71,882)	(73,890)
Gross profit	14,478	18,813	17,303	14,204	14,601
Other income and gains	333	162	91	126	137
SG&A	(3,749)	(4,757)	(4,586)	(4,816)	(5,201)
Profit from operations	11,062	14,219	12,807	9,515	9,537
Other income/cost/and loss	(63)	97	(18)	39	40
Pre-tax profit	10,999	14,315	12,789	9,554	9,576
Profits tax	(2,848)	(3,462)	(3,214)	(2,389)	(2,394)
Net profit	8,151	10,854	9,575	7,166	7,182
Minority interests	685	898	733	430	431
Equity shareholders of the Company	7,466	9,955	8,842	6,736	6,751
EPS (Basic), Rmb	0.56	0.75	0.67	0.51	0.51
Dividend per share, Rmb	0.16	0.22	0.21	0.14	0.14

Source: Company data, ABCI Securities estimates

Balance sheet forecast

As of Dec 31 (Rmb mn)	2010A	2011A	2012A	2013E	2014E
Property, plant and equipment	46,418	60,823	85,510	104,314	119,951
Mining and exploration rights	18,611	28,973	32,479	30,726	31,602
Land use rights	2,564	2,819	3,529	3,174	3,351
Other non-current assets	6,643	12,364	14,789	13,591	14,198
Total non-current assets	74,236	104,979	136,306	151,804	169,102
Inventories	6,215	7,315	6,697	6,556	6,706
Accounts and bills receivable	7,006	8,014	11,394	11,153	11,409
Prepaid expenses and other current assets	5,439	6,468	6,367	6,233	6,376
Cash and cash equivalents	22,922	20,907	13,223	8,019	8,190
Other current assets	7,118	14,468	11,701	13,085	12,393
Current assets	48,700	57,173	49,381	45,045	45,074
Total assets	122,936	162,152	185,688	196,849	214,177
Trade and notes payables	(9,254)	(11,003)	(16,102)	(15,761)	(16,124)
Accruals, advance and other payables	(6,997)	(12,053)	(9,262)	(9,066)	(9,274)
Short-term borrowings	(396)	(2,255)	(5,130)	(5,130)	(5,130)
Other short-term liabilities	(2,743)	(4,514)	(3,633)	(3,261)	(3,367)
Total current liabilities	(19,391)	(29,824)	(34,126)	(33,219)	(33,895)
Long-term borrowings	(10,716)	(11,456)	(20,171)	(20,867)	(25,519)
Long-term bonds	-	(14,955)	(19,906)	(25,823)	(32,071)
Other Non-current liabilities	(6,491)	(9,043)	(10,064)	(9,884)	(9,987)
Total non-current liabilities	(17,207)	(35,454)	(50,141)	(56,574)	(67,577)
Total liabilities	(36,598)	(65,278)	(84,267)	(89,793)	(101,472)
Total equity	86,339	96,874	101,420	107,056	112,705
Non-controlling interests	12,290	14,349	14,694	15,511	16,329
Equity of the firm	74,049	82,525	86,726	91,545	96,376
Book value/share, Rmb	5.58	6.22	6.54	6.90	7.27

Source: Company data, ABCI Securities estimates



Consolidated cash flow statements forecast

As of Dec 31 (Rmb mn)	2010A	2011A	2012A	2013E	2014E
Profit before income tax	10,999	14,315	12,789	9,554	9,576
DD&A	3,752	4,854	4,944	4,897	4,875
Financial cost	(656)	(715)	(2,201)	(1,458)	(1,829)
Financial income	781	353	903	628	765
(Increase) decrease in inventories	(1,254)	(1,174)	519	141	(151)
Decrease in trade and bills receivables	(2,123)	(1,851)	(3,383)	241	(256)
Other adj. items	(816)	(1,235)	(2,683)	(3,184)	(1,702)
CF Operating	10,683	14,547	10,887	10,819	11,278
Purchases of property, plant and equipment	(12,060)	(19,156)	(24,934)	(22,045)	(19,840)
Others	13,525	(16,127)	(6,955)	(10,172)	(7,489)
CF Investing	1,466	(35,283)	(31,889)	(32,217)	(27,329)
Cash flows from short-term borrowing activities	9,215	1,779	2,876	2,327	2,601
Cash flows from long-term borrowing activities	(276)	3,693	9,396	6,545	7,970
Cash flows from other financing	(1,586)	13,122	1,039	7,329	5,657
CF from/(used) in Financing activities	(1,853)	18,593	13,311	16,201	16,229
Net change in cash	10,296	(2,142)	(7,691)	(5,197)	178
Cash at the beginning	12,628	23,057	20,907	13,223	8,019
Exchange difference	(2)	(7)	(7)	(7)	(7)
Cash at the end	22,922	20,908	13,210	8,019	8,190

Source: Company data, ABCI Securities estimates



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Definition of equity rating

Rating	Definition
Buy	Stock return \geq Market return rate
Hold	Market return - 6% \leq 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	$2.6 \leq 180$ day volatility/180 day benchmark index volatility
High	$1.5 \leq 180$ day volatility/180 day benchmark index volatility < 2.6
Medium	$1.0 \leq 180$ 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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