



August 28, 2014
Company Report
Rating: BUY
TP: HK\$ 1.67

Share price (HK\$)	1.38
Est. share price return	21.01%
Est. dividend yield	2.75%
Est. total return	23.76%

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Key Data

52Wk H/L(HK\$)	1.91 / 1.26
Issued shares (mn)	4,280
Market cap (HK\$ mn)	5,906
3-mth avg daily turnover (HK\$ mn)	7.6
Major shareholder(s) (%):	
Li San Yim and spouse	55.68

Source(s): Company, Bloomberg, ABCI Securities

1H14 Revenue breakdowns (%)

Wheel loaders	63.10
Excavators	10.28
Fork lifts	13.98
Road rollers	1.11
Financial Leasing Income	0.27
Others	11.26

Source(s): Company, ABCI Securities

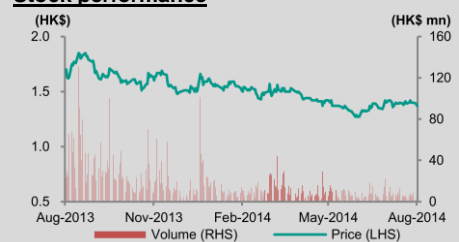
Share performance (%)

	Absolute	Relative*
1-mth	(2.14)	(5.49)
3-mth	(2.14)	(9.93)
6-mth	(9.27)	(19.25)

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

Stock performance



Source(s): Bloomberg, ABCI Securities

Lonking (3339 HK)
Resilient amid headwinds; maintain BUY

- Revenue and net income were up 0.3% YoY and 0.9% YoY in 1H14. With its stable earnings, Lonking outperforms its peers suffering from huge earnings decline in 1H14
- GPM increased 3.22ppt YoY under the new sales arrangement and deflating raw material prices. Cost of sales is expected to stay low in 2H14, thus high profitability is likely to sustain.
- Receivable turnover days reduced by 10 days YoY to 124 days in 1H14; operating cash flow remained positive.
- Considering the lukewarm machinery market and prudent credit control enforced by Lonking, we revise down both our FY14E/15E earnings forecasts and TP. The Group's improved asset quality and strong cash flow prompt us to maintain our BUY rating with a new TP of HK\$ 1.67.

Flat growth in lukewarm market outperforms peers. Revenue edged up by 0.3% YoY to RMB 4,485mn in 1H14, of which sales of wheel loader, the major business segment, contributed to 63.1% of total revenue, or RMB 2,830mn, in 1H14, representing a 2.9% decline YoY. According to CCMA, total sales volume of wheel loader in China declined by 7.5% YoY during the same period. Net income was flat at RMB 346mn in 1H14 (1H13: RMB 343mn), which is better than peers recording substantial declines for the same period. According Zoomlion (1157 HK, HOLD)'s announced profit warning, net income is expected to plunge 60% YoY in 1H14.

Profit margin recovery on track. GPM was up 3.22ppt YoY to 25.5% in 1H14 mainly on changes in sales arrangement. Lonking raised the selling price in 1H14 but bore the logistic cost of delivering from production base to distributors. Thus the selling and distribution cost, as a percentage to revenue, was up 2ppt YoY to 5.4% in 1H14. Nevertheless, if reallocating the increased logistic cost to costs of sales, GPM still improved by 1.2ppt YoY in 1H14, thanks to the deflated raw material costs. The average steel price dropped ~8% YoY in 1H14, and expected to stay low in 2H14.

Sustainable market share. Lonking's market share of wheel loader, based on the sales volume in China, was up from 14% in 2013 to 15% in 1H14, reflecting the competitiveness of Lonking's product. Lonking was ranked no. 30 among the Top 50 Global Construction Machinery Manufacturers which compares the sales of construction machinery business worldwide.

Maintain BUY. We believe more time will be needed for the construction industry to digest the overcapacity in construction machinery. Accordingly, we cut the FY14E/15E earnings forecasts by 3%/6% on weaker-than-expected recovery in the machinery sector. Nonetheless, we think Lonking distinguishes itself from the domestic peers by its solid market position and prudent sales strategy. The counter is currently trading at 9.1x FY14E P/E, at par with the lower quartile of its historical P/E since 2011, or 31.5% in discount to its book value at end-1H14, which is undemanding in our view. Our TP of HK\$ 1.67 (previous: HK\$ 1.73) represents 11x FY14E P/E, equivalent to the median of historical P/E since 2011. Maintain BUY.

Risk factors: 1) Provisional loss on receivables; 2) China's prudent monetary policy may affect capital inflow and delay construction.

Results and Valuation

	FY ended Dec 31	2012A	2013A	2014E	2015E	2016E
Revenue (RMB mn)	7,896	8,158	7,798	8,324	9,113	
Chg (% YoY)	(37.93)	3.32	(4.42)	6.75	9.48	
Net Income (RMB mn)	151	480	523	609	760	
Chg (% YoY)	(91.27)	217.88	8.89	16.56	24.74	
EPS (RMB)	0.035	0.112	0.122	0.142	0.178	
P/E (x)	31.42	9.88	9.08	7.79	6.24	
BVPS (RMB)	1.459	1.599	1.715	1.877	2.075	
P/B (x)	0.76	0.69	0.65	0.59	0.53	
DPS (RMB)	-	0.051	0.031	0.036	0.044	
Yield (%)	-	4.64	2.75	3.21	4.00	
ROAE (%)	2.39	7.34	7.37	7.92	8.99	
Net gearing (%)	50.25	29.80	31.82	22.45	11.37	

* Net gearing=Net debt/Total equity

Source(s): Bloomberg, ABCI Securities estimates



Exhibit 1: Financial summary of Lonking in 1H12-1H14

(RMB mn)	1H12	2H12	1H13	2H13	1H14	(% YoY)
Revenue (RMB mn)	4,724	3,172	4,474	3,684	4,485	0.25
Wheel loaders	3,208	1,953	2,914	2,406	2,830	(2.88)
Excavators	530	350	566	215	461	(18.55)
Fork lifts	422	397	462	521	627	35.71
Road rollers	72	43	57	63	50	(12.28)
Financial Leasing Income	61	44	31	17	12	(61.29)
Others	431	385	444	462	505	13.74
Less: Operating cost (RMB mn)	3,746	2,621	3,476	2,758	3,340	(3.91)
Gross Profit (RMB mn)	978	551	998	926	1,145	14.73
<i>GPM (%)</i>	<i>20.70</i>	<i>17.37</i>	<i>22.31</i>	<i>25.14</i>	<i>25.53</i>	<i>3.22ppt</i>
SG&A (RMB mn)	489	418	417	498	532	27.58
Selling and distribution cost	211	172	148	184	240	62.16
Administrative cost	132	124	124	144	130	4.84
R&D expenses	146	122	145	170	162	11.72
<i>SG&A-to-revenue (%)</i>	<i>10.35</i>	<i>13.18</i>	<i>9.32</i>	<i>13.52</i>	<i>11.86</i>	<i>2.54ppt</i>
Net profit (RMB mn)	276	(125)	343	137	346	0.87
<i>Net profit margin (%)</i>	<i>5.84</i>	<i>(3.94)</i>	<i>7.67</i>	<i>3.72</i>	<i>7.71</i>	<i>0.05ppt</i>
Total receivables assets (RMB mn)	4,818	3,226	3,784	2,965	3,169	
Trade and bill receivables	4,240	2,944	3,646	2,939	3,156	
Financial leasing assets	578	282	138	26	13	
As percentage of revenue (%)	101.99	101.70	84.58	80.48	70.66	(13.92ppt)
Total debt (RMB mn)	4,842	5,105	4,427	4,238	4,441	
Total cash and equivalents (RMB mn)	1,474	967	966	1,195	1,037	
Net debt (Net cash) (RMB mn)	3,368	4,138	3,461	3,043	3,404	
Total equity (RMB mn)	6,369	6,245	6,631	6,845	6,933	
Net gearing (%)	52.88	66.26	52.19	44.46	49.10	(3.10ppt)

Source(s): Company, ABCI Securities

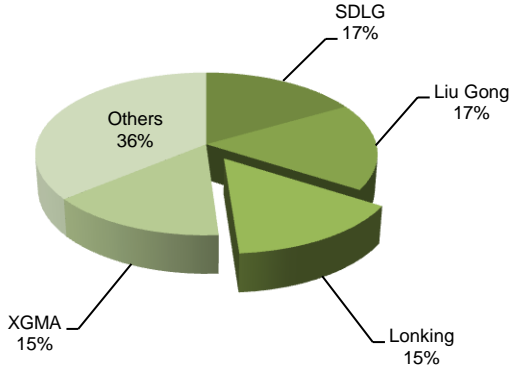
Exhibit 2: FY14E-15E financial projections for Lonking

	FY14E			FY15E		
	Previous	New	Chg (%)	Previous	New	Chg (%)
Revenue (RMB mn)	9,245	7,798	(15.65)	10,286	8,324	(19.08)
Gross profit (RMB mn)	2,069	1,895	(8.42)	2,302	2,010	(12.66)
<i>GPM (%)</i>	<i>22.38</i>	<i>24.30</i>	<i>1.92ppt</i>	<i>22.38</i>	<i>24.15</i>	<i>1.77ppt</i>
Net income (RMB mn)	538	523	(2.85)	650	609	(6.27)
<i>Net margin (%)</i>	<i>5.82</i>	<i>6.70</i>	<i>0.88ppt</i>	<i>6.32</i>	<i>7.32</i>	<i>1.00ppt</i>
EPS (RMB)	0.126	0.122	(3.08)	0.152	0.142	(6.36)
BVPS (RMB)	1.736	1.715	(1.20)	1.909	1.877	(1.66)
DPS (RMB)	0.031	0.031	(1.52)	0.038	0.036	(6.36)

Source(s): ABCI Securities estimates

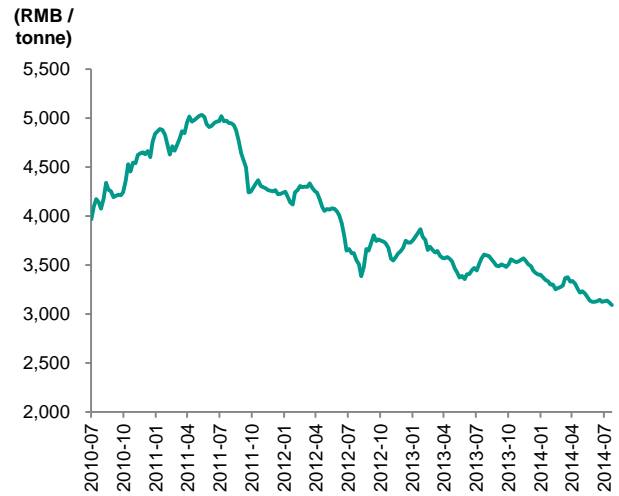


Exhibit 3: Market share of domestic wheel loader manufacturing industry based on sales volume, 1H14



Source(s): CCMA, ABCI Securities

Exhibit 4: China's domestic steel rebar 25 mm spot average price, 1H10-1H14



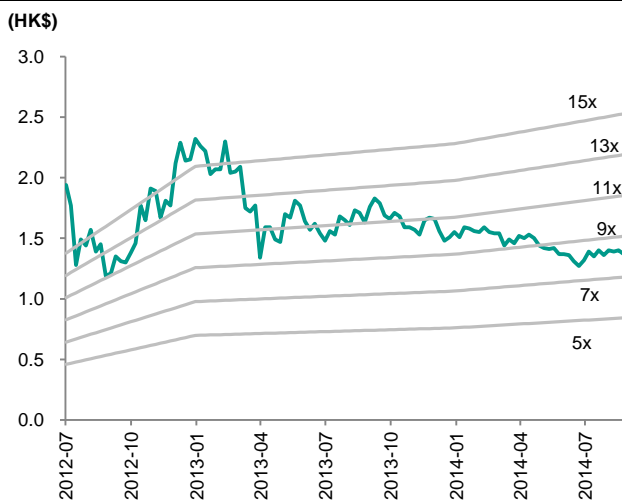
Source(s): Bloomberg, ABCI Securities

Exhibit 5: Valuation of domestic and international construction machinery makers

Company	Ticker	Mkt cap (HK\$ mn)	CRY	As of 27/8/2014 Share Price	P/E (x)		EPS (%YoY)		P/B (x)		ROAE (%)	
					FY14E	FY15E	FY14E	FY15E	FY14E	FY15E	FY14E	FY15E
CATERPILLAR INC	CAT US	528,191	USD	108.55	17.35	15.05	6.59	15.26	3.52	3.22	19.91	22.70
KOMATSU LTD	6301 JP	173,391	JPY	2,361	14.12	13.18	(0.11)	7.14	1.54	1.43	11.75	11.41
SANY HEAVY INDUS	600031 CH	51,791	CNY	5.40	11.21	10.19	26.58	9.98	1.56	1.41	12.80	13.30
ZOOMLION HEAVY-H	1157 HK	7,021	HKD	4.91	8.81	8.66	(9.40)	1.77	0.69	0.66	8.09	7.96
ZOOMLION HEAVY-A	000157 CH	36,506	CNY	4.60	9.79	8.78	(6.00)	11.49	0.81	0.76	7.41	8.13
XCMG CONSTRUCT-A	000425 CH	20,064	CNY	7.70	9.72	9.02	8.63	7.82	0.76	0.70	8.05	8.23
GUANGXI LIUGONG	000528 CH	8,816	CNY	6.23	16.34	14.11	26.67	15.79	0.73	0.69	3.50	4.52
TEREX CORP	TEX US	31,882	USD	37.33	14.50	10.78	26.80	34.50	1.68	1.44	12.79	14.60
TADANO	6395 JP	18,051	JPY	1,866	14.59	12.90	12.50	13.07	2.04	1.80	14.54	14.82
SHANTUI CONST-A	000680 CH	5,040	CNY	3.22	N/A	N/A	(62.50)	9.52	0.96	1.00	(8.41)	(3.50)
XIAMEN XGMA-A	600815 CH	5,735	CNY	4.73	N/A	N/A	(17.74)	15.69	1.26	1.50	(12.06)	(17.07)
LONKING HOLDINGS	3339 HK	5,906	HKD	1.38	9.08	7.79	8.89	16.56	0.65	0.59	7.37	7.92
Sector Weighted Average					15.15	13.32	6.36	13.58	2.65	2.43	16.07	17.80

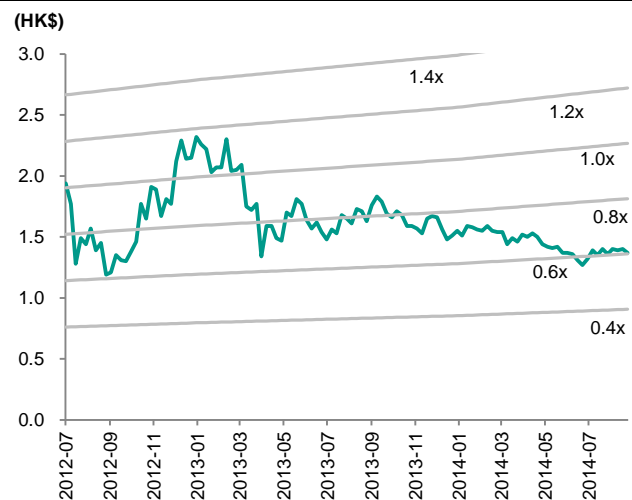
Source(s): Bloomberg, ABCI Securities estimates

Exhibit 6: P/E band of Lonking in 7M12-8M14



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

Exhibit 7: P/B band of Lonking in 7M12-8M14



Source(s): Company, 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	7,896	8,158	7,798	8,324	9,113
Wheel loaders	5,161	5,320	4,722	4,817	5,058
Excavators	880	781	707	707	728
Fork lifts	819	983	1,254	1,580	1,991
Road rollers	115	120	114	120	126
Financial Leasing Income	105	48	4	4	4
Others	816	906	997	1,096	1,206
COGS	(6,367)	(6,234)	(5,903)	(6,313)	(6,863)
Gross profit	1,529	1,924	1,895	2,010	2,250
SG&A	(907)	(915)	(958)	(1,037)	(1,147)
Other income and gains	(346)	(438)	(307)	(239)	(186)
Pre-tax profit	276	571	630	734	916
Income tax	(124)	(90)	(107)	(125)	(156)
Net profit	152	480	523	609	760
Profit attributable to:					
Minority interests	0.09	0.29	0.19	0.23	0.29
Equity shareholders of the Company	152	480	523	609	760
EPS (RMB)	0.035	0.112	0.122	0.142	0.178
DPS (RMB)	-	0.051	0.031	0.036	0.044
EBIT	653	809	783	877	1,051
EBITDA	989	1,175	1,033	1,130	1,308

Source(s): Company, ABCI Securities estimates

Consolidated balance sheet (2012A-2016E)

As of Dec 31 (RMB mn)	FY12A	FY13A	FY14E	FY15E	FY16E
Current assets	7,960	8,061	7,502	7,926	8,279
Cash and equivalent	967	1,195	1,255	1,317	1,822
Trade and bill receivables	2,944	2,939	2,616	2,402	2,092
Financial leasing receivables	216	23	51	29	61
Inventories	2,731	2,342	1,863	2,288	2,224
Other current assets	1,102	1,562	1,718	1,890	2,079
Non-current assets	5,714	5,482	5,656	5,832	5,999
Property, plant and equipment	3,822	3,720	3,779	3,834	3,886
Intangible assets	321	316	318	320	321
Long-term investments	66	6	7	7	8
Long-term receivables	66	3	9	3	7
Other non-current assets	1,439	1,437	1,544	1,667	1,777
Total assets	13,674	13,543	13,158	13,757	14,278
Current liabilities	3,257	3,052	2,674	2,964	2,865
Trade and bill payables	1,048	1,101	840	1,063	1,005
Receipts in advance	33	85	32	93	44
Short term borrowings	1,184	813	697	647	597
Other current liabilities	992	1,053	1,106	1,161	1,219
Non-current liabilities	4,172	3,646	3,139	2,755	2,529
Long-term borrowings	3,921	3,425	2,907	2,511	2,274
Other non-current liabilities	251	221	232	244	256
Total liabilities	7,429	6,698	5,814	5,719	5,394
Minority interests	2	3	3	3	3
Shareholders' equities	6,243	6,843	7,341	8,035	8,880
BVPS (RMB)	1.459	1.599	1.715	1.877	2.075

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	276	571	630	734	916
Changes in depreciation and amortization	336	366	249	253	256
Changes in working capital	195	291	455	100	230
Income tax paid	37	19	31	32	39
Financial cost	341	238	153	143	135
Others	(106)	91	(164)	(187)	(228)
CF Operating	1,079	1,576	1,354	1,076	1,350
Increase in PP&E	(559)	(242)	(300)	(300)	(300)
Increase in intangible assets	(122)	(4)	(10)	(10)	(10)
Others	(448)	(73)	-	-	-
CF Investing	(1,129)	(319)	(310)	(310)	(310)
Capital injection	-	-	-	-	-
Net debt financing	(523)	(738)	(634)	(446)	(288)
Dividend payout	(314)	-	(220)	(131)	(152)
Interest paid	(279)	(231)	(153)	(143)	(135)
Others	365	(178)	23	16	41
CF Financing	(751)	(1,147)	(984)	(704)	(535)
Net change in cash	(801)	110	60	62	505
Cash at the beginning	2,155	967	1,195	1,255	1,317
Adjustment (Time deposit & FX effect)	(387)	118	-	-	-
Cash at the end	967	1,195	1,255	1,317	1,822

Source(s): Company, ABCI Securities estimates

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

FY ended Dec 31	FY12A	FY13A	FY14E	FY15E	FY16E
Sales mixed (%)					
Wheel loaders	65.36	65.21	60.56	57.87	55.50
Excavators	11.14	9.57	9.07	8.49	7.99
Fork lifts	10.37	12.05	16.08	18.98	21.85
Road rollers	1.46	1.47	1.46	1.44	1.38
Financial Leasing Income	1.33	0.59	0.05	0.05	0.05
Others	10.33	11.11	12.78	13.17	13.23
Profit & loss ratios (%)					
Gross margin	19.36	23.58	24.30	24.15	24.69
Net profit margin	1.91	5.88	6.70	7.32	8.34
Effective tax rate	44.93	15.76	17.00	17.00	17.00
Growth (%)					
Revenue	(37.93)	3.32	(4.42)	6.75	9.48
Gross profit	(52.43)	25.83	(1.52)	6.11	11.91
EBIT	(73.49)	23.89	(3.16)	11.92	19.91
EBITDA	(64.11)	18.81	(12.10)	9.39	15.75
Net profit	(91.27)	217.88	8.89	16.56	24.74
Balance sheet ratios					
Current ratio (x)	2.44	2.64	2.81	2.67	2.89
Quick ratio (x)	1.61	1.87	2.11	1.90	2.11
Cash ratio (x)	0.30	0.39	0.47	0.44	0.64
Trade and bill receivables days	140	132	130	110	90
Trade and bill payables turnover days	108	63	60	55	55
Inventory turnover days	204	149	130	120	120
Total debt / equity ratio (%)	81.75	61.91	49.08	39.29	32.31
Net debt / equity ratio (%)	50.25	29.80	31.82	22.45	11.37
Returns (%)					
ROAE	2.39	7.34	7.37	7.92	8.99
ROAA	1.02	3.53	3.92	4.53	5.42
Payout ratio	-	45.83	25.00	25.00	25.00

Source(s): Company, 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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