



Dec. 09, 2014
Company Report
Rating: SELL
TP: HK\$ 4.60

H-Share price (HK\$) 6.85
Est. share price return -32.85%
Est. dividend yield 1.36%
Est. total return -31.48%

Analyst: Mark Chen
Tel: (852) 2147 8819
Email: markychen@abci.com.hk

Key Data

52Wk H/L(HK\$)	8.34/4.91
Issued shares (mn)	4,918
H-Shares (mn)	1,958
A-Shares (mn)	2,960
Market cap	
H-shares (HK\$ mn)	13,337
A-Shares (HK\$ mn)	39,694
3-mth avg daily turnover (HK\$ mn)	140.7
Major shareholder(s) (%):	
Yankuang Group Company Limited	52.86

Source(s): Company, Bloomberg, ABCI Securities

FY13 Revenue breakdown (%)

Coal	96.22
Railway transportation service	1.11
Gross sales of electricity power	0.60
Gross sales of methanol	2.01
Gross sales of heat supply	0.06

Source(s): Company, ABCI Securities

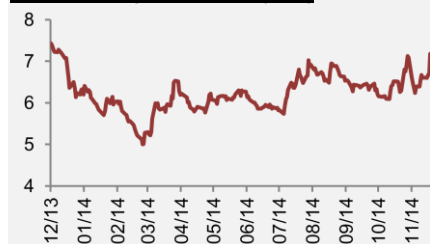
Share performance (%)

	Absolute	Relative*
1-mth	6.87	(2.62)
3-mth	(0.73)	(3.03)
6-mth	11.58	(0.63)

*Relative to HSCEI

Source(s): Bloomberg, ABCI Securities

1-Year stock performance (HK\$)



Source(s): Bloomberg, ABCI Securities

Yanzhou Coal (1171 HK)
Overvalued with unsustainable cost cut;
reiterate **SELL**

- The Group have recently raised prices of some of its high-quality thermal coal products by ~RMB 10/ton, which is much lower than the RMB 30/ton increase among the larger coal players. We believe this reflects the weak downstream demand as well as insufficient bargaining power of the Group
- The Group reported a significant cost cut for 9M14; however, much of the reduction was based on the drawing of provisions for production safety and maintenance expenses. We believe such cost cut measure is unsustainable
- The counter was removed from HSCEI on Dec. 8, 2014. This may negatively affect its share liquidity in the near future. We believe its current valuation at 22.78x FY15E P/E is demanding. Reiterate **SELL** with TP at HK\$4.6 (0.43x FY15E P/B)

A coal player with limited bargaining power. The Group have recently raised prices of some of its high-quality thermal coal products by ~RMB 10/ton during the peak season. Unlike Yanzhou Coal, China Shenhua (1088 HK), China Coal (1898 HK), and Yitai Coal(3948 HK) that increased their prices by RMB 30/ton in just 2 months, we believe the small increase reflects weak downstream demand and low bargaining power of the Group.

Coal spot prices to stabilize in FY15. We believe the fact that large players are raising prices implies the cessation of price war in the near future. We believe this will help stabilize the thermal coal prices in northern China. Bohai-Rim thermal coal prices index has regained support in recent weeks. Besides, China's move to reduce interest rate to lower financing costs for private firms will also support coal prices in the near future. The stabilization of China's coal price may in turn support international coal prices and this will benefit Yanzhou's overseas sales.

Recent cost control is unsustainable. The Group reported significant cost cut in 9M14, with unit cost in its headquarter being slashed by ~31%. However, we believe the cost cut is unsustainable. About 59% of the reduction in its headquarter was resulted from the drawing on provision for production safety expenses and production maintenance expenses. Excluding this factor, its cost cut was lowered by only 12.76%; meanwhile the headquarters' ASP dropped by 16%YoY (in 9M14).We believe the room for further cost cut is limited.

Highest unit cost among H-share peers. Its unit cost is RMB 265/ton (headquarter, under IFRS) in 1H14 , much higher than China Shenhua (RMB 127/ton), China Coal (RMB216/ton) and Yitai Coal (RMB 88/ton). Quality of the Group's coal mine reserves and its operation efficiency are lower compared to its H-share peers.

Results and Valuation

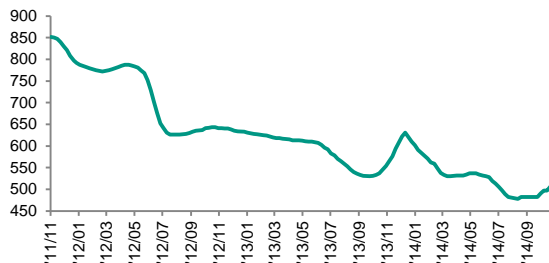
FY ended Dec 31	2012A	2013A	2014E	2015E	2016E
Turnover (RMB mn)	58,146	56,402	65,053	68,676	72,123
Chg (% YoY)	23.54	(3.00)	15.34	5.57	5.02
Net Income (RMB mn)	6,066	777	1,207	1,177	1,202
Chg (% YoY)	(30.64)	(87.18)	55.25	(2.45)	2.13
EPS (RMB)	1.23	0.16	0.25	0.24	0.24
Chg (% YoY)	(30.64)	(87.18)	55.25	(2.45)	2.13
BVPS (RMB)	9.26	8.21	8.38	8.55	8.72
Chg (% YoY)	7.25	(11.31)	2.09	1.97	1.97
P/E (x)	-	34.50	22.22	22.78	22.31
P/B (x)	-	0.66	0.65	0.64	0.63
DPS (HK\$)	0.36	0.02	0.07	0.07	0.08
Yield (%)	-	0.37	1.35	1.36	1.4
ROE (%)	13.79	1.81	2.96	2.83	2.83
ROA (%)	5.54	0.62	0.95	0.92	0.93

Source(s): Bloomberg, ABCI Securities estimates

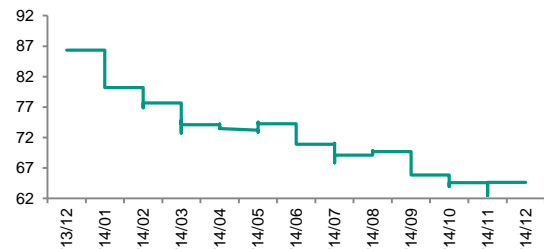
May benefit from SH-HK Stock Connect. The counter was removed from HSCEI on Dec. 8, 2014 and this may reduce its share liquidity in the near future. Its shares, however, are eligible for trading under the SH-HK stock connect launched on Nov. 17, 2014. Since its A-share is at premium to its H-share (A/H=146% assuming RMB/HKD=1.2606), the significant discrepancy provides potential arbitrage opportunities and reduces the impact of reduced liquidity caused by its removal from HSCEI.

Reiterate SELL with TP at HK\$ 4.6. We believe the A/H price premium will support the counter's H-share in the near future. However, we believe its shares are overvalued considering its weaker-than-peer fundamentals. We expect its FY15E EPS to drop slightly by 2.45%YoY to RMB 0.24, assuming that its cost control is insubstantial. Our TP reflected 0.43x FY15E P/B.

Risk factors: 1) Fluctuation in coal prices; 2) Imbalance in supply and demand; 3) Business cycles of downstream industries; 4) Cost rebound; 5) Foreign exchange risk entailed in overseas sales

Exhibit 1: Bohai-Rim thermal coal prices (RMB/ton)


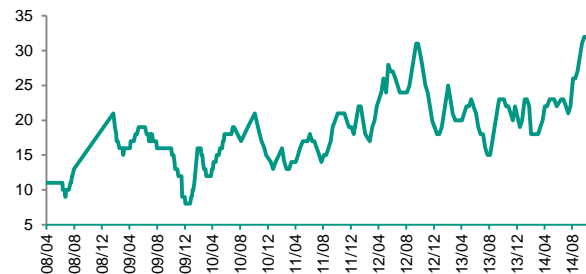
Source(s): Wind, ABCI Securities

Exhibit 2: Australia BJ thermal coal price index (US\$/ton)


Source(s): Wind, ABCI Securities

Exhibit 3: Mine-mouth price (RMB/ton) in Inner Mongolia


Source(s): Wind, ABCI Securities

Exhibit 4: Coal inventory days at major IPPs (day)


Source(s): Wind, ABCI Securities



Consolidated income statement (2012A-2016E)

As of Dec 31 (RMB mn)	2012A	2013A	2014E	2015E	2016E
Revenue	58,146	56,402	65,053	68,676	72,123
Coal	56,201	54,445	63,100	66,358	69,682
Railway transportation service income	464	458	453	596	642
Gross sales of electricity power	324	332	146	316	309
Gross sales of methanol	1,118	1,156	1,327	1,367	1,452
Gross sales of heat supply , RMB mn	40	11	26	39	38
Transportation costs of coal	(2,104)	(2,024)	(2,463)	(2,603)	(2,734)
Cost of sales and service provided	(42,149)	(42,512)	(51,724)	(54,669)	(57,413)
Cost of electricity power	(331)	(321)	(390)	(412)	(433)
Cost of methanol	(911)	(851)	(1,035)	(1,094)	(1,149)
Cost of heat supply	(25)	(7)	(8)	(9)	(9)
COGS	(45,520)	(45,714)	(55,620)	(58,787)	(61,737)
Gross profit	12,626	10,688	9,433	9,889	10,386
SG&A	(7,988)	(10,381)	(7,173)	(7,573)	(7,953)
Other income and gains	1,432	(887)	(861)	(874)	(868)
Pre-tax profit	6,070	(580)	1,398	1,442	1,565
Income tax	(36)	395	(154)	(216)	(313)
Net profit	6,034	(185)	1,244	1,226	1,252
Profit attributable to:					
Minority interests	(31)	(963)	37	49	50
Equity shareholders of the Company	6,066	777	1,207	1,177	1,202
EPS (Basic), RMB	1.23	0.16	0.25	0.24	0.24
DPS, RMB	0.36	0.02	0.07	0.07	0.08

Source(s): Company, ABCI Securities estimates

Consolidated balance sheet (2012A-2016E)

As of Dec 31 (RMB mn)	2012A	2013A	2014E	2015E	2016E
Property, plant and equipment	39,503	41,897	38,839	35,973	33,333
Prepaid lease payments	696	676	686	686	683
Intangible assets	33,634	38,256	35,945	35,945	36,716
Other non-current assets	18,499	15,105	16,202	15,872	16,200
Total non-current assets	92,332	95,934	91,672	88,477	86,932
Bank balances and cash	12,717	10,923	13,121	18,633	18,335
Bills and accounts receivable	7,460	9,020	9,414	10,447	10,683
Inventories	1,566	1,589	1,842	1,937	2,034
Prepayments and other receivables	4,197	5,260	5,404	6,047	6,159
Other current assets	3,894	4,733	4,248	4,255	4,467
Current assets	29,833	31,524	34,029	41,318	41,678
Total assets	122,165	127,458	125,700	129,795	128,610
Bills and accounts payable	(6,812)	(2,717)	(7,610)	(7,983)	(8,393)
Other payables and accrued expenses	(9,014)	(8,385)	(10,096)	(10,666)	(11,175)
Borrowings-due within one year	(7,713)	(11,275)	(9,494)	(9,494)	(10,088)
Other short-term liabilities	(5,085)	(6,439)	(5,762)	(6,095)	(5,932)
Total current liabilities	(28,623)	(28,816)	(32,962)	(34,238)	(35,588)
Borrowings-due after one year	(33,284)	(44,100)	(38,692)	(40,703)	(38,413)
Deferred tax liability	(7,564)	(8,468)	(8,016)	(8,242)	(8,129)
Other Non-current liabilities	(3,975)	(2,088)	(1,124)	(821)	214
Total non-current liabilities	(44,822)	(54,656)	(47,832)	(49,766)	(46,327)
Total liabilities	(73,445)	(83,472)	(80,794)	(84,004)	(81,915)
Total equity	48,720	43,986	44,906	45,791	46,695
Non-controlling interests	3,190	3,607	3,683	3,755	3,830
Equity of the firm	45,530	40,379	41,223	42,036	42,865
BVPS, RMB	9.26	8.21	8.38	8.55	8.72

Source(s): Company, ABCI Securities estimates



Consolidated cash flow statement (2012A-2016E)

As of Dec 31 (RMB mn)	2012A	2013A	2014E	2015E	2016E
Profit before income tax	6,070	(580)	1,398	1,442	1,565
Depreciation of property, plant and equipment	2,819	3,125	2,834	2,654	2,446
Interest expenses	1,449	1,766	2,241	2,003	2,122
Interest income	(722)	(489)	(489)	(489)	(489)
Decrease (increase) in inventories	(59)	(265)	(253)	(95)	(97)
Decrease (increase) in bills and accounts receivable	(93)	(1,722)	(395)	(1,032)	(236)
Other adj. items	(2,960)	(4,035)	(262)	(5,719)	(5,317)
CF Operating	6,504	(2,201)	5,075	(1,236)	(7)
Purchases of property, plant and equipment	(6,230)	(10,221)	(2,471)	(6,308)	(6,333)
Others	3,043	(3,283)	(1,292)	1,234	(475)
CF Investing	(3,187)	(13,504)	(3,763)	(5,074)	(6,808)
Proceeds from bank borrowings	12,282	21,103	2,003	20,665	11,874
Dividend paid	(2,803)	(1,771)	(98)	(362)	(365)
Cash flows from other financing	(8,333)	(6,046)	(1,119)	(8,760)	(5,326)
CF from/(used) in Financing activities	1,145	13,287	786	11,544	6,183
Net change in cash	4,461	(2,419)	2,098	5,234	(632)
Cash at the beginning	8,145	12,717	10,923	13,121	18,633
Exchange difference	111	624	100	278	334
Cash at the end	12,717	10,923	13,121	18,633	18,335

Source(s): Company, ABCI Securities estimates

Financial ratios (2012A-2016E)

As of Dec 31 (RMB mn)	2012A	2013A	2014E	2015E	2016E
Profitability ratio (%)					
Gross profit margin	21.71	18.95	14.50	14.40	14.40
EBT margin	10.44	(1.03)	2.15	2.10	2.17
Net profit margin	10.43	1.38	1.86	1.71	1.67
ROA	5.54	0.62	0.95	0.92	0.93
ROE	13.79	1.81	2.96	2.83	2.83
Cost ratio (%)					
Admin/Sales	13.74	18.40	11.03	11.03	11.03
Effective tax rate	0.60	68.04	11.00	15.00	20.00
Leverage (x)					
Current ratio	1.04	1.09	1.03	1.21	1.17
Quick ratio	0.99	1.04	0.98	1.15	1.11
Cash ratio	0.44	0.38	0.40	0.54	0.52
Total debt/total equity (%)	150.75	189.77	179.92	183.45	175.43
Total debt/total asset (%)	23.43	22.61	26.22	26.38	27.67
Working capital data and Ratios					
Inventory turnover	30.79	28.98	32.42	31.11	31.09
Receivables turnover	7.87	6.85	7.06	6.92	6.83
Payables turnover	10.10	9.60	10.82	7.55	7.55
Days' inventory on hand	11.85	12.59	11.26	11.73	11.74
Days' of sales outstanding	46.36	53.32	51.71	52.78	53.47
Days' payables	36.16	38.02	33.73	48.33	48.33
Cash conversion cycle	22.06	27.90	29.24	16.18	16.87

Source(s): Company, ABCI Securities estimates

Disclosures

Analyst Certification

I, Chen Yibiao, Mark, 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.

Disclosures of Interests

ABCI Securities Company Limited and/or its affiliates may pursue financial interests to the companies mentioned in the report.

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 2009-2013

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.

Disclaimers

This report is for our clients only and is for distribution only under such circumstances as may be permitted by applicable law. It has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient. It is published solely for informational purposes and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments. No representation or warranty, either expresses or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein. This report should not be regarded by recipients as a substitute for the exercise of their own judgment. Any opinions expressed in this report are subject to change without notice and may differ or be contrary to opinions expressed by other business areas as a result of using different assumptions and criteria. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. The analyst(s) responsible for the preparation of this report may interact with trading desk personnel, sales personnel and other constituencies for the purpose of gathering, synthesizing and interpreting market information. ABCI Securities Company Limited is under no obligation to update or keep current the information contained herein. ABCI Securities Company Limited relies on information barriers to control the flow of information contained in one or more areas within ABCI Securities Company Limited, into other areas, units, groups or affiliates of ABCI Securities Company Limited. The compensation of the analyst who prepared this report is



determined exclusively by research management and senior management (not including investment banking). Analyst compensation is not based on investment banking revenues, however, compensation may relate to the revenues of ABCI Securities Company Limited as a whole, of which investment banking, sales and trading are a part. The securities described herein may not be eligible for sale in all jurisdictions or to certain categories of investors. The price and value of the investments referred to in this research and the income from them may fluctuate. Past performance is not necessarily indicative of future results. Foreign currency rates of exchange may adversely affect the value, price or income of any security or related instrument mentioned in this report. For investment advice, trade execution or other enquiries, clients should contact their local sales representative. Neither ABCI Securities Company Limited nor any of its affiliates, directors, employees or agents accepts any liability for any loss or damage arising out of the use of all or any part of this report. Additional information will be made available upon request.

Copyright 2014 ABCI Securities Company Limited

No part of this material may be (i) copied, photocopied or duplicated in any form by any means or (ii) redistributed without the prior written consent of ABCI Securities Company Limited.

**Office address: ABCI Securities Company Limited, 13/F Fairmont House,
8 Cotton Tree Drive, Central, Hong Kong.**

Tel: (852) 2868 2183