

Key Data

| | |
|---|-------------|
| Share price (HK\$) | 1.43 |
| Target price (HK\$) | 1.55 |
| Upside potential (%) | 8.4 |
| 52Wk H/L(HK\$) | 4.01 / 1.27 |
| Issued shares (mn) | 4,280 |
| Market cap (HK\$mn) | 6,120 |
| 30-day avg vol (HK\$mn) | 30 |
| Major shareholder (%): Li San Yim and spouse | 55.69 |

Source: Company, Bloomberg, ABCI Securities

Revenue breakdown by product in FY11 (%)

| | |
|--------------|------|
| Wheel loader | 69.7 |
| Excavator | 13.5 |
| Fork lift | 7.3 |
| Others | 9.5 |

Source: Company

Share performance (%)

| | Absolute | Relative* |
|-------|----------|-----------|
| 1-mth | -25.5% | -26.1% |
| 3-mth | -51.4% | -47.7% |
| 6-mth | -55.9% | -54.7% |

Source: Bloomberg

*Relative to Hang Seng Index

1 year price performance



Source: Bloomberg

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Lonking (3339 HK) – HOLD Construction & Farm Machinery Industry

Conservative wheel loader maker in tough environment

Lonking, a market leader in wheel loader segment, suffered from the slowdown of construction activities in infrastructure industry in 1H12. Although we observe the recovery signals of the industry, our analysis indicates the Group's sales take longer time to regain growth momentum. Its high gearing ratio implies higher chance to look for equity finance and to have earnings dilution risk in 2H12. Its valuation is bargain but the counter lacks upside catalyst in the short-term.

Sales dropped on product demand tumble. The total market sales of wheel loaders and excavators plunged in China by 25.6% YoY and 36.9% YoY in the 1H12 respectively. Even worse, industry statistics showed the Group is losing its market share in wheel loader segment. We predict its sales to decline by 40% YoY for 1HFY12.

Financial position worsens. Its net gearing ratio was 55.1% high at end of FY11. Although the PBOC has cut the lending interest rates twice this year, we anticipate its interest coverage ratio to drop from 6.2x at end of FY11 to 4.2x at end of FY12. To maintain solvency of the business operation, the group deliberately constrains its sales growth or seeks equity finance.

Recovery is hindered. The high gearing hinders the Group to fully capture the market recovery expected to start in 2H12. We estimate revenue and net income will tumble by 25.3% and 44.2% YoY in FY12, respectively. We expect the Group to take a longer period to recover the sales decline compared with the large player, such as Zoomlion (1157 HK, BUY).

Our 12-month target price of HK\$1.55 is based on 5.6x of our FY12E EPS, 40% discount to the mean of peers². We believe this valuation is justified as its EPS will plunge 44.2% YoY to Rmb0.225 in FY12 and it takes a longer time to recover. **We initiate Lonking with a "HOLD" rating.**

Risk factors: Financial and liquidity risk; Loss of market share

Forecast and Valuation

| FY ended Dec 31 | FY10A | FY11A | FY12E | FY13E | FY14E |
|----------------------------------|--------|--------|--------|--------|--------|
| Revenue (Rmb mn) | 12,020 | 12,720 | 9,502 | 11,552 | 14,202 |
| <i>Chg (% YoY)</i> | 74.2 | 5.8 | (25.3) | 21.6 | 22.9 |
| Gross Profit (Rmb mn) | 3,427 | 3,213 | 2,326 | 2,874 | 3,600 |
| <i>Chg (% YoY)</i> | 111.8 | (6.2) | (27.6) | 23.6 | 25.3 |
| Net Income (Rmb mn) | 1,766 | 1,730 | 965 | 1,264 | 1,651 |
| <i>Chg (% YoY)</i> | 120.8 | (2.1) | (44.2) | 31.0 | 30.6 |
| EPS (Rmb) | 0.413 | 0.404 | 0.225 | 0.295 | 0.386 |
| <i>Chg (% YoY)</i> | 120.8 | (2.1) | (44.2) | 31.0 | 30.6 |
| PE (x) | - | 2.9 | 5.2 | 3.9 | 3.0 |
| PB (x) | - | 0.78 | 0.70 | 0.62 | 0.55 |
| Yield (%) | - | 10.5 | 5.8 | 7.6 | 10.0 |
| ROAA (%) | 15.2 | 11.7 | 6.1 | 7.8 | 9.3 |
| ROAE (%) | 39.1 | 29.7 | 14.3 | 16.8 | 19.3 |
| Net debt/total equity (%) | 57.1 | 55.1 | 58.4 | 55.9 | 49.3 |

Source: Company, Bloomberg, ABCI Securities estimates



Disclosures

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