

September 6, 2013  
 Equity Focus  
 Rating: **HOLD**  
 TP: HK\$ 4.48

H-Share price (HK\$) 4.79  
 Est. share price return (6.47%)  
 Est. dividend yield 3.80%  
 Est. total return (2.67%)

Previous Rating & TP HOLD; HK\$ 4.48  
 Previous Report Date June 28, 2013

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#### Key Data

52Wk H/L(HK\$)	9.04/3.66
Issued shares (mn)	13,259
H-Shares (mn)	4,107
A-Shares (mn)	9,152
Market cap	
H-shares (HK\$ mn)	19,671
A-Shares (HK\$ mn)	48,689
3-mth avg daily turnover (HK\$ mn)	235.2
Major shareholder(s) (%):	
Shenhua Group Ltd.	57.54

Source(s): Company, Bloomberg, ABCI Securities

#### FY12 Revenue breakdown (%)

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

Source(s): Company, ABCI Securities

#### Share performance (%)

	Absolute	Relative*
1-mth	14.87	7.73
3-mth	(3.43)	(3.21)
6-mth	(34.20)	(25.22)

\*Relative to HSCEI

Source(s): Bloomberg, ABCI Securities

#### 1-Year stock performance (HK\$)



Source(s): Bloomberg

## China Coal (1898 HK)

### Wait for more signals; maintain HOLD

- Positive signals: 1) China's PMI rose for two consecutive months to 51.0; 2) inventory days of direct supply power plants declined to three-year low to 15 days; 3) China imposed a 3% import tariff on lignite
- Negative factors: 1) Bohai-Rim Thermal Coal Prices Index dropped to RMB540/ton on Sep.4; 2) Arrival of off-peak season in Sep/Oct; 3) Potential power tariff cuts might place additional pressure on coalminers
- China Coal slashed 5% of its unit cost in 1H13; more efforts are required in 2H13 to maintain a similar cost-cut level
- Present valuation at 7.47x FY14E P/E is generally in-line with our expectation. We maintain HOLD with TP at HK\$4.48, reflecting 7.0x FY14E P/E

**Positive economic signals indicate thermal coal prices may bottom out soon.** 1) China's Manufacturing PMI rose for two consecutive months to 51.0, hinting to an economic recovery; 2) inventory days of direct supply power plants declined to three-year low to 15 days. Spot prices will be supported by the upcoming restocking; 3) China announced a 3% import tariff on lignite, which will help narrow the price gap between domestic and import coal prices.

**Meaningful rebound in coal prices unlikely in the short term.** 1) As of Sep 4, Bohai-Rim spot prices was down 14% YoY and 15% YTM to RMB540/ton; 2) Anticipating the power demand will drop in off-peak season (Sep/Oct), IPPs have postponed restocking and spot coal prices may slide further temporarily; 3) A more than 5% annual decline in coal prices will trigger power tariff cuts, which in turn may affect coalminers because IPPs may pressure coal producers to offer discounts; 4) Provincial governments reduce surcharges for coalminers, but some of the measures could be temporary and provide only short-term financial relief.

**Stringent cost control required in 2H13.** China Coal's selling prices are highly correlated with the dwindling Bohai-Rim spot market price, creating additional pressure on the Group's revenue in an oversupplied and underdemanded market. The Group achieved a 5% cut in unit cost in 1H13. As most costs and expenses will only be recognized in 2H13, the firm would need to strengthen its effort to maintain a similar cost-cut level for the year.

**Maintain HOLD with TP at HK\$ 4.48.** The Group's 1H13 net profit attributable to shareholders was RMB 3,221mn, or 48% of our FY13E estimate at RMB 6,736mn. We maintain our FY13E EPS estimate of RMB 0.51. However, if coal prices slide further, we a downward adjustment in our estimates is likely. Currently the stock is trading at 7.47x FY14E P/E. We believe the counter is fairly valued. Maintain HOLD with TP at HK\$4.48, reflecting 7.0x FY14E P/E.

**Risk factors:** 1) Further declines in coal prices; 2) Imbalance in supply and demand; 3) Business cycles of downstream industries; 4) Surging costs.

#### Results and Valuation

FY ended Dec 31	2010A	2011A	2012A	2013E	2014E
Revenue (RMB mn)	70,303	90,865	87,292	86,086	88,491
Chg (% YoY)	32.18	29.25	(3.93)	(1.38)	2.79
Net Profit (RMB mn)	7,466	9,955	8,842	6,736	6,751
Chg (% YoY)	0.77	33.34	(11.18)	(23.82)	0.23
EPS (RMB)	0.56	0.75	0.67	0.51	0.51
Chg (% YoY)	0.00	34.08	(11.18)	(23.82)	0.23
BVPS (RMB)	5.17	5.58	6.22	6.54	6.90
Chg (% YoY)	7.95	11.45	5.09	5.56	5.28
P/E (x)			5.70	7.48	7.47
P/B (x)			0.58	0.55	0.52
DPS (RMB)	0.16	0.22	0.21	0.14	0.14
Yield (%)			5.53	3.80	3.81
ROE (%)	10.47	12.72	10.45	7.56	7.19
ROA (%)	6.38	6.98	5.08	3.52	3.29

Source(s): Bloomberg, ABCI estimates



2013 Interim Results Highlights

For 6 months ended June 30 (RMB mn)	1H12	1H13	Chg,%
Revenue	45,720	40,398	(11.64)
<b>Cost of sales</b>			
Materials	(19,851)	(16,361)	(17.58)
Staff costs	(2,278)	(2,284)	0.30
Depreciation and amortization	(2,110)	(2,525)	19.63
Repair and maintenance	(549)	(560)	2.08
Transportation costs	(5,459)	(5,910)	8.26
Sales taxes and surcharges	(722)	(654)	(9.48)
Others	(5,124)	(4,867)	(5.01)
Total cost of sales	(36,093)	(33,161)	(8.12)
<b>Gross profit</b>	<b>9,627</b>	<b>7,238</b>	<b>(24.82)</b>
GPM	21.06%	17.92%	
Selling, general and administrative expenses	(2,352)	(2,035)	(13.49)
Other income	4	2	(43.81)
Other gains, net	47	16	(66.60)
<b>Profit from operations</b>	<b>7,327</b>	<b>5,221</b>	<b>(28.74)</b>
Finance income	421	299	(29.01)
Finance costs	(594)	(455)	(23.35)
Share of profits of associates and jointly controlled entities	208	141	(32.16)
<b>Profit before income tax</b>	<b>7,362</b>	<b>5,206</b>	<b>(29.29)</b>
Income tax expense	(1,837)	(1,307)	(28.84)
Profit for the period	5,525	3,899	(29.43)
<b>Profit attributable to:</b>			
<b>Equity holders of the Company</b>	<b>5,182</b>	<b>3,221</b>	<b>(37.84)</b>
Non-controlling interests	343	677	97.58
<b>EPS, RMB</b>	<b>0.39</b>	<b>0.24</b>	<b>(38.46)</b>

Source(s): Company, ABCI Securities

Consolidated income statement (2010A-2014E)

FY Ended Dec 31 (RMB mn)	2010A	2011A	2012A	2013E	2014E
<b>Revenue</b>	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)
<b>Gross profit</b>	<b>14,478</b>	<b>18,813</b>	<b>17,303</b>	<b>14,204</b>	<b>14,601</b>
Other income and gains	333	162	91	126	137
SG&A	(3,749)	(4,757)	(4,586)	(4,816)	(5,201)
<b>Profit from operations</b>	<b>11,062</b>	<b>14,219</b>	<b>12,807</b>	<b>9,515</b>	<b>9,537</b>
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)
<b>Net profit</b>	<b>8,151</b>	<b>10,854</b>	<b>9,575</b>	<b>7,166</b>	<b>7,182</b>
<b>Profit attributable to:</b>					
Minority interests	685	898	733	430	431
<b>Equity shareholders of the Company</b>	<b>7,466</b>	<b>9,955</b>	<b>8,842</b>	<b>6,736</b>	<b>6,751</b>
<b>EPS (Basic), RMB</b>	<b>0.56</b>	<b>0.75</b>	<b>0.67</b>	<b>0.51</b>	<b>0.51</b>
<b>Dividend per share, RMB</b>	<b>0.16</b>	<b>0.22</b>	<b>0.21</b>	<b>0.14</b>	<b>0.14</b>

Source(s): Company, ABCI Securities estimates

**Consolidated balance sheet (2010A-2014E)**

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
<b>Total non-current assets</b>	<b>74,236</b>	<b>104,979</b>	<b>136,306</b>	<b>151,804</b>	<b>169,102</b>
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
<b>Current assets</b>	<b>48,700</b>	<b>57,173</b>	<b>49,381</b>	<b>45,045</b>	<b>45,074</b>
<b>Total assets</b>	<b>122,936</b>	<b>162,152</b>	<b>185,688</b>	<b>196,849</b>	<b>214,177</b>
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)
<b>Total current liabilities</b>	<b>(19,391)</b>	<b>(29,824)</b>	<b>(34,126)</b>	<b>(33,219)</b>	<b>(33,895)</b>
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)
<b>Total non-current liabilities</b>	<b>(17,207)</b>	<b>(35,454)</b>	<b>(50,141)</b>	<b>(56,574)</b>	<b>(67,577)</b>
<b>Total liabilities</b>	<b>(36,598)</b>	<b>(65,278)</b>	<b>(84,267)</b>	<b>(89,793)</b>	<b>(101,472)</b>
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
<b>Equity of the firm</b>	<b>74,049</b>	<b>82,525</b>	<b>86,726</b>	<b>91,545</b>	<b>96,376</b>
<b>Book value/share, RMB</b>	<b>5.58</b>	<b>6.22</b>	<b>6.54</b>	<b>6.90</b>	<b>7.27</b>

Source(s): Company, ABCI Securities estimates

**Consolidated cash flow statement (2010A-2014E)**

FY ended 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)
<b>CF Operating</b>	<b>10,683</b>	<b>14,547</b>	<b>10,887</b>	<b>10,819</b>	<b>11,278</b>
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)
<b>CF Investing</b>	<b>1,466</b>	<b>(35,283)</b>	<b>(31,889)</b>	<b>(32,217)</b>	<b>(27,329)</b>
Cash flows from short-term borrowing activities	9	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
<b>CF from/(used) in Financing activities</b>	<b>(1,853)</b>	<b>18,593</b>	<b>13,311</b>	<b>16,201</b>	<b>16,229</b>
<b>Net change in cash</b>	<b>10,296</b>	<b>(2,142)</b>	<b>(7,691)</b>	<b>(5,197)</b>	<b>178</b>
Cash at the beginning	12,628	23,057	20,907	13,223	8,019
Exchange difference	(2)	(7)	(7)	(7)	(7)
<b>Cash at the end</b>	<b>22,922</b>	<b>20,908</b>	<b>13,210</b>	<b>8,019</b>	<b>8,190</b>

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 2008-2012

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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