

## Mining sector

Share price	Target price
HK\$5.44	HK\$7.20

Reason for note	Initiate Coverage
Recommendation	OUTPERFORM

### Trading data

Beta	NA
% Upside to TP	32.4%
52-week range (HK\$)	3.25/5.70
Market cap. (HK\$m)	11,288
Market cap. (US\$m)	1,457
Shares outstanding (mn)	2,075
Avg. daily volume (mn)	6.8
Avg. daily value (HK\$m)	42.9
Major sh (%)	Trisonic Int'l - 57.51
Free float (%)	32.63

### Financial data

	2008A
Shareholder's Equity (RMBmn)	539
ROA (%)	32.2
ROE (%)	67.0
Net gearing (%)	Net cash

### Performance

	1-mth	3-mth	6-mth
Absolute	5.0	55.4	N/A
Rel to HSCEI	(0.3)	4.8	48.6

### Revenue Breakdown

	%
Iron concentrate	50
Iron pellet	49
Titanium concentrate	1

### Major Customers

	%
Direct customers	18.5
Distributors	81.5

### Major Competitors

Lomon Corp.  
Jingzhi Mine

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## China VTM (0893.HK)

## OUTPERFORM

### Profitable by nature

- A local miner with natural advantages.** China VTM is a leading iron ore mining company in Sichuan Province. During 2006-2009, it witnessed skyrocketing growth in both its top line (70% CAGR) and bottom line (132% CAGR), thanks to its capacity expansion and the iron ore price rally. We deem the company's natural advantages, outlined below, have been played out and should continue to play a vital role in its rapid development going forward. 1) Its iron ore contains vanadium and titanium, which are valuable by products. 2) Both of its major mines, namely Baicao Mine and Xiushuihe Mine, are open-pit iron ore mines, which need much lower mining costs compared to other mine types. 3) It sits in the Panxi Region, which is the largest vanadium-bearing titanomagnetite reserve region in China, and thus has a great potential for further expansion. 4) It is located close to the Chengkun Railway and its major customers, while the customers are far away from all the seaports and hence not easily accessible to the imported ores.
- Further leap in FY10F sales volume expected.** The company's IPO in September last year lent support to its expansion schedule regarding the new lines building and old lines upgrading projects. As such, we estimate China VTM's FY10 iron concentrate output will expand 32% y-o-y from 1.6mn tonnes to 2.1mn tonnes and its iron pellet output will increase by 28% y-o-y from 594,000 tonnes to 760,000 tonnes. Meanwhile, we also expect its high-grade titanium concentrate lines will commence operation shortly and produce 175,000 tonnes of products in FY10F. According to its previously signed sales contracts, the company will be able to sell all of its products in FY10.
- Buoyant ore price with a secured floor.** We believe China VTM's ore ASP will be solidly underpinned by the robust demand, given that 1) Local steel mills, including Pangang and Weiyuan Steel, are planning large-scale expansions, while an additional 11mn tpa of iron ore demand is expected to mainly come from the local miners. 2) The central government has advocated using vanadium-reinforced steel, hence, the demand for vanadium-bearing iron ores will likely rise as a result. Meanwhile, the company had signed floor-price contracts to eliminate any downside risks in FY10.
- Catalysts and risks.** The company is actively seeking acquisition opportunities in the Panxi Region and had penned a few candidates. The potential acquisitions would further enhance its enterprise value. Nonetheless, the uncertain value of any acquired mining asset is the other side of the coin.
- Valuation & recommendation.** We set our TP at HK\$7.20, implying 32% upside potential and representing 25x FY10F PER or 0.72x PEG over FY08-11F. The company will have a good chance of beating our earnings estimates if the iron ore spot price hovers at a high level during 2010. We initiate coverage of the counter with an Outperform rating.

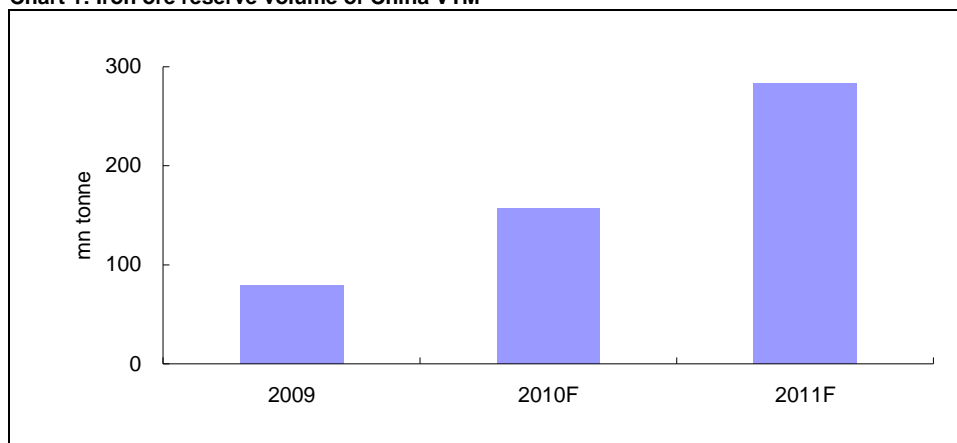
Financial summary					
FYE 31 Dec (RMBmn)	FY07	FY08	FY09F	FY10F	FY11F
Revenue	367	791	1,036	1,579	1,760
% chg	73.7	115.8	30.9	52.5	11.5
Gross Profit	179	427	597	968	1,097
Gross margin %	48.8	54.0	57.7	61.3	62.3
Op. profit	78	352	497	819	927
EBITDA	89	378	546	890	1,010
% chg	43.8	324.3	44.2	63.0	13.5
Net profit	54	249	327	538	606
% chg	31.4	363.2	31.4	64.6	12.6
EPS (RMB)	0.026	0.120	0.157	0.259	0.292
EPS Consensus (RMB)	-	-	0.180	0.263	0.333
PER (x)	201.8	39.9	31.1	18.9	16.8
PBR (x)	35.5	16.8	3.5	2.9	2.4
BVPS (RMB)	0.138	0.291	1.416	1.696	2.012
DPS (RMB)	0.000	0.000	0.000	0.052	0.058
Yield (%)	0.0	0.0	0.0	1.1	1.2

Source: Company data, SinoPac Securities estimates

## China VTM (0893.HK)

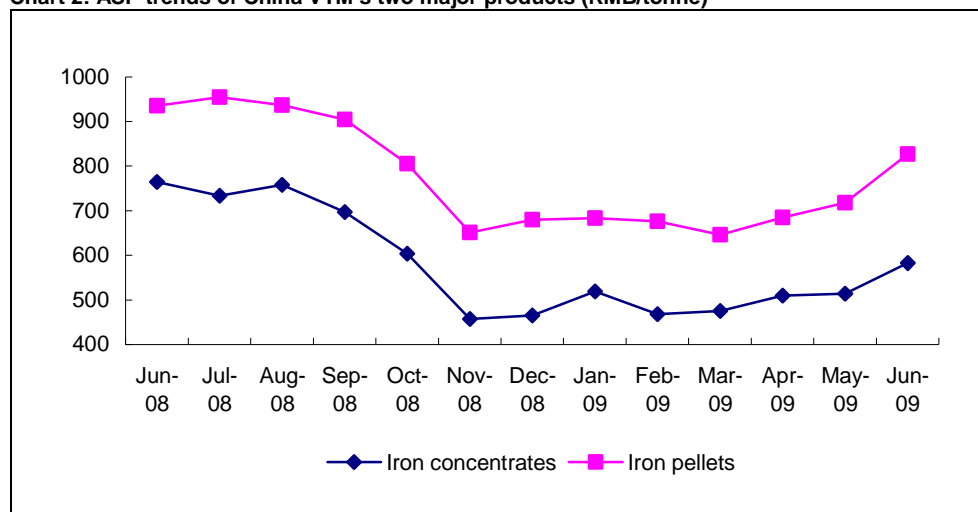
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Chart 1: Iron ore reserve volume of China VTM



Source: Company data

Chart 2: ASP trends of China VTM's two major products (RMB/tonne)



Source: Company data

Table 1: Peers comparison

Company	Code	Ccy	Close pr	Shares out	Mkt cap	PER (x)			PBR	Yield(%)	ROE(%)
						FY08	FY09F	FY10F	FY09F	FY09F	FY09F
Zijin Mining	2899.HK	HK\$	8.10	14,541	117,785	31.0	28.1	23.2	5.8	1.7	21.2
China Moly	3993.HK	HK\$	6.71	4,876	32,719	17.4	33.9	18.0	2.6	1.1	6.4
Xinjiang Xinxin	3833.HK	HK\$	4.58	2,210	10,122	28.8	42.5	21.7	1.7	0.6	4.4
<b>Average of domestic mining companies</b>						<b>25.7</b>	<b>34.9</b>	<b>21.0</b>	<b>3.4</b>	<b>1.1</b>	<b>10.6</b>
BHP Billiton	BHP.AU	AU\$	43.77	3,358	227,120	38.0	22.5	21.4	5.5	2.1	21.5
Rio Tinto	RIO.AU	AU\$	79.00	607	144,246	176.3	22.9	18.6	3.5	0.6	8.4
CVRD	VALE.N	US\$	30.78	3,257	155,529	NA	30.4	17.8	2.9	1.5	11.2
Fortescue	FMG.AU	AU\$	5.17	3,103	16,041	25.9	36.5	48.9	43.5	0.0	19.0
<b>Average of overseas mining companies</b>						<b>80.1</b>	<b>28.1</b>	<b>26.7</b>	<b>13.9</b>	<b>1.1</b>	<b>15.0</b>
China VTM	0893.HK	HK\$	5.44	2,075	11,288	39.9	31.1	18.9	3.5	0.0	19.7

Source: Bloomberg, company data, SinoPac Securities

**China VTM (0893.HK)**

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Profit & loss forecasts					Balance sheet forecasts				
FYE 31 Dec (RMBmn)	FY08	FY09F	FY10F	FY11F	FYE 31 Dec (RMBmn)	FY08	FY09F	FY10F	FY11F
Net sales	791	1,036	1,579	1,760	<b>Total Assets</b>	<b>951</b>	<b>3,336</b>	<b>4,035</b>	<b>4,726</b>
Cost of goods sold	(364)	(438)	(611)	(663)	Current Assets	406	2,421	2,894	3,495
<b>Gross Profits</b>	<b>427</b>	<b>597</b>	<b>968</b>	<b>1,097</b>	Cash & cash equivalent	133	2,081	2,402	2,952
Total operating exp	(75)	(100)	(149)	(169)	Inventories	66	79	110	119
Operating exp. SD&A	(55)	(73)	(111)	(123)	Accounts Receivable	88	115	175	195
Operating expense (gains)	20	28	38	46	Others	119	147	208	228
<b>EBIT</b>	<b>352</b>	<b>497</b>	<b>819</b>	<b>927</b>	Non-current Assets	546	914	1,141	1,231
Depreciation	(19)	(41)	(63)	(76)	LT Investments	38	65	70	75
Amortization	(8)	(8)	(8)	(7)	Net fixed Assets	357	702	926	1,014
<b>EBITDA</b>	<b>378</b>	<b>546</b>	<b>890</b>	<b>1,010</b>	Others	150	147	145	143
Share of profits of associates	0	0	0	0	<b>Total Liabilities</b>	<b>347</b>	<b>398</b>	<b>515</b>	<b>551</b>
Net other non-operating income	0	0	0	0	Current Liabilities	290	341	458	494
<b>Total Non-Oper. Expenses</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	Accounts Payable	260	311	428	464
Interest expense	(3)	0	0	0	ST Borrowings	0	0	0	0
<b>Total Non-Oper. Expenses</b>	<b>(3)</b>	<b>0</b>	<b>0</b>	<b>0</b>	Others	30	30	30	30
<b>Pretax Income</b>	<b>349</b>	<b>497</b>	<b>819</b>	<b>927</b>	Long-term Liabilities	57	57	57	57
Income taxes exp.	(30)	(78)	(129)	(151)	Long-term Debts	0	0	0	0
<b>Net Income before Extr.</b>	<b>319</b>	<b>419</b>	<b>690</b>	<b>776</b>	Others	57	57	57	57
Extraordinaries	0	0	0	0	<b>Total Equity</b>	<b>604</b>	<b>2,938</b>	<b>3,520</b>	<b>4,175</b>
<b>Net Income after Extraordinaries</b>	<b>319</b>	<b>419</b>	<b>690</b>	<b>776</b>	Shareholders' equity	539	2,781	3,212	3,696
Minority interest	70	92	152	171	Common Stock	0	200	200	200
<b>Net Income for shareholders of the company</b>	<b>249</b>	<b>327</b>	<b>538</b>	<b>606</b>	Capital Surplus	539	2,581	3,012	3,496
Dividend to common share holders	0	0	108	121	Minority interest	65	157	308	479
<b>Retained Earnings</b>	<b>249</b>	<b>327</b>	<b>430</b>	<b>484</b>	<b>Net Assets</b>	<b>604</b>	<b>2,938</b>	<b>3,520</b>	<b>4,175</b>
					Net Current Assets	116	2,081	2,436	3,001

Source: Company data, SinoPac Securities estimates

Source: Company data, SinoPac Securities estimates

Cash flow forecasts					Key assumptions				
FYE 31 Dec (RMBmn)	FY08	FY09F	FY10F	FY11F	FYE 31 Dec	FY08	FY09F	FY10F	FY11F
<b>Operating Cash Flow</b>	<b>423</b>	<b>450</b>	<b>726</b>	<b>845</b>	<b>ASP (RMB/tonne)</b>				
Pre-tax Profit	249	327	538	606	Iron concentrate	622	540	590	620
Depreciation & Amortization	27	49	71	83	Pellet	826	775	868	911
Change in Working Capital	72	(17)	(35)	(14)	Medium-grade titanium concentrate	200	200	200	200
Others	76	92	152	171	High-grade titanium concentrate	-	600	600	600
<b>Investment Cash Flow</b>	<b>(267)</b>	<b>(418)</b>	<b>(298)</b>	<b>(174)</b>	<b>Sales volume (thousand tonne)</b>				
Net CAPEX	(173)	(386)	(288)	(164)	Iron concentrate	797	993	1,340	1,490
Change in LT Investment	0	0	0	0	Pellet	305	594	760	760
Change in Other Assets	(94)	(32)	(10)	(10)	Medium-grade titanium concentrate	217	125	118	28
<b>Free Cash Flow</b>	<b>222</b>	<b>61</b>	<b>445</b>	<b>694</b>	High-grade titanium concentrate	0	25	175	231
<b>Financing Cash Flow</b>	<b>(30)</b>	<b>1,915</b>	<b>(107)</b>	<b>(121)</b>	<b>Average cash costs (RMB/tonne)</b>				
Change in Share Capital	0	200	0	0	Iron concentrate	175	177	183	191
Net Change in Debt	(30)	0	0	0	Pellet	337	347	344	353
Change in Other LT Liab.	(0)	1,715	(108)	(121)	Medium-grade titanium concentrate	186	219	179	179
<b>Net Cash Flow</b>	<b>126</b>	<b>1,948</b>	<b>321</b>	<b>551</b>	High-grade titanium concentrate	-	363	363	371
Exch rate movements	0	0	0	0					
Cash at the beginning of yr	8	133	2,081	2,402					
Cash at the end of yr	133	2,081	2,402	2,952					

Source: Company data, SinoPac Securities estimates

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Recommendation definitions:

Outperform	: return > 10% in excess of benchmark return in a year
In-line	: return within 10% of benchmark return in a year
Underperform	: return > 10% below benchmark return in a year

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