

Company Update



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■ AT A GLANCE

SELL HOLD **BUY** ★★★

Target price	HK\$5 (+127%)
Current price	HK\$2.20
Bloomberg code	893 HK
Market cap	US\$551m
Shares out (float)	2.08bn (42%)
52-week high/low	HK\$4.33/2.06
ADT (3M)	US\$1.90m
One year performance	1M 6M 12M
China Vanadium	-26% -31% -23%
Hang Seng China Ent	-15% -16% -8%

■ KEY CHANGES

	New	Old	Chg%
Recommendation	Buy	Buy	
Target price (HK\$)	5	5.7	-12.3%
EPS 12-11E (Rmb)	0.31	0.31	-1%
EPS 12-12E (Rmb)	0.34	0.39	-13.1%
EPS 12-13E (Rmb)	0.40	0.45	-10.2%

■ SAMSUNG vs THE STREET

No. of I/B/E/S estimates	7
Target price vs I/B/E/S mean	+8%
Estimates up/down (4 weeks)	0/0
1yr fwd EPS vs I/B/E/S mean	NA
Estimates up/down (4 weeks)	0/0
I/B/E/S recommendation	Buy (1.50)

China Vanadium (893 HK)

Value to be uncovered

WHAT'S THE STORY?

Event: We attended China Vanadium's analyst meeting following the company's interim results announcement.

Impact: Iron pellet production and sales volumes were lower than expected as the company reduced outsourced pellet production. However, prices for iron and high-grade titanium concentrates were 7-8% higher than our forecasts. We reduce our earnings forecasts by 1% in 2011e and by 13% in 2012e as we factor in lower volumes, higher selling prices and higher costs.

Action: We maintain our BUY rating on the stock, but lower our DCF-based target price by 12% to HK\$5.00 from HK\$5.70 on our earnings revisions. The stock looks attractive, trading at only a 2011e P/E of 5.8x, with potential upside surprises from selling prices for iron ore and titanium products in 2H, strong growth prospects, including further acquisitions, and a positive management track record.

THE QUICK VIEW

Management estimates that Sichuan's iron ore market should be in a supply deficit by 2012 and expects iron concentrate prices to increase from 4Q11, when Pangang starts to prepare materials for its new plant. Management also expects titanium product prices to perform well over the next few months.

China Vanadium plans to increase its resources to ~600m tonnes from ~400m tonnes over the next 3 years. Our sense is that most of the resources growth should come through in 2H11-1H12e as management aims to acquire resources before an increase in competition drives up prices. Management's strong track record and abundant iron ore resources in Sichuan make us optimistic on the company's ability to deliver.

■ SUMMARY FINANCIAL DATA

	12-09	12-10	12-11E	12-12E	12-13E
Revenue (Rmb m)	1,084	1,554	1,998	2,452	2,794
EBITDA	480	798	991	1,191	1,377
Net Inc	328	533	648	707	830
EPS (Rmb)	0.20	0.26	0.31	0.34	0.40
P/E	19.8	12.8	5.8	5.3	4.5
EV/EBITDA	15.6	7.2	2.7	1.5	0.8
Div Yld (%)	0.3	1.6	3.5	3.8	4.4
P/B	3.7	2.3	1.1	1.0	0.8
ROE (%)	21	20	21	20	20

Source: Company data, Samsung Securities estimates

China Vanadium (893 HK)

Lower our earnings estimates

We lower our earnings estimates by 1% to Rmb648m in 2011e, by 13% to Rmb707m in 2012e and by 10% to Rmb830m in 2013e.

Production volume: We lower vanadium-bearing iron concentrates volume by 6% to 2.2m tonnes in 2011e, by 22% to 2.5m tonnes in 2012e and by 22% to 2.5m tonnes in 2013e. We now factor in more conservative volume growth as a production ramp-up seems to be taking longer than expected.

We lower our estimates of iron pellet volume by 6% to 850,000 tonnes in 2011e, but raise the volume by 2% to 1.3m tonnes and by 10% to 1.4m tonnes to factor in the new pellet plant which came on stream in 1H11.

Selling prices: We raise vanadium-bearing iron concentrates prices by 11% to Rmb690/t in 2011e to factor in 1) stronger-than-expected prices in 1H11 and 2) the potential to benefit from higher selling prices in 2H as the company switches from contract pricing to spot pricing. We also raise selling prices by 15% in 2012-13e, accordingly.

We also raise high-grade titanium selling prices by 8% in 2011e to Rmb1,132/t to factor in higher-than-expected prices so far this year and positive outlook on downstream demand, based on our conversations with management. We also raise selling prices by 11% in 2012-13e, accordingly.

Costs: We raise iron pellet unit costs by 14% in 2011-13e to factor in the cost increase driven by the pelletizing contracting fee increase. We now forecast the unit cost to be Rmb544/t in 2011e.

We also raise the high-grade titanium concentrates unit cost by 14% in 2011-13e. We now forecast the unit cost to be Rmb535/t for 2011e, in line with 1H11. Our sense is that the cost increase is probably driven by general inflation and higher depreciation expenses after facility upgrades.

Figure 1: EPS changes

(Rmb m)	Old			New			Change		
	2011e	2012e	2013e	2011e	2012e	2013e	2011e	2012e	2013e
Revenues	1,935	2,735	3,041	1,998	2,452	2,794	3%	-10%	-8%
Net income	654	813	925	648	707	830	-1%	-13%	-10%
EPS, Rmb	0.31	0.39	0.45	0.31	0.34	0.40	-1%	-13%	-10%

Source: Samsung Securities

Maintain BUY

We maintain our BUY rating, but lower our DCF-based target price by 12% to HK\$5.00. We like the company, based on our view of potential selling prices surprises, strong growth prospects and strong management track record. The stock looks cheap, trading at 5.8x P/E, 1.1x

P/B and 2.8x EV/EBITDA in 2011e. We think the catalysts are 1) stronger-than-expected iron and titanium product selling prices in 2H and 2) further acquisitions.

Management estimates that steel-making capacity in the Sichuan region will increase by 10.7m tonnes by 2012. This should result in a supply deficit in Sichuan's iron ore market and further push up prices. Management expects to see the price increase from 4Q11, when Pangang starts to prepare materials for its new plant.

For titanium products, selling prices have more than doubled YoY, driven by titanium import disruptions and strong downstream demand. Management expects these factors to persist over the next few months.

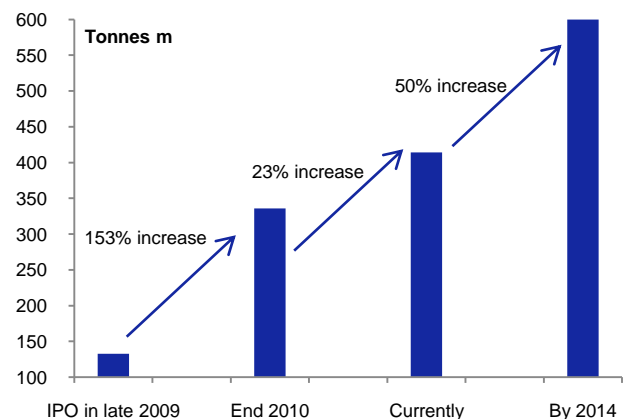
Figure 2: Selling prices for major products

Selling prices (Rmb/t)	1H10	2H10	1H11	YoY	HoH
Vanadium iron concs	665	665	664	0%	0%
Iron pellets	877	873	901	3%	3%
Medium-grade titanium	86	109	177	106%	63%
High-grade titanium	512	556	1,132	121%	104%

Source: Company data, Samsung Securities

The company plans to increase resources to ~600m tonnes from ~400m tonnes over the next 3 years. Our sense is that most of the resources growth should come through in 2H11-1H12e as management aims to acquire resources before an increase in competition drives up prices. Management's good track record and abundant iron ore resources in Sichuan make us confident about their ability to deliver.

Figure 3: Iron ore resources



Source: Company data

1H11 results broadly in line

China Vanadium reported on Aug 29 that net income in 1H11 was Rmb301m, up 29% YoY, but flat HoH. The results are broadly in line, representing 46% of our and consensus forecasts for full-year 2011.

China Vanadium (893 HK)

Figure 4: Financial summary

(Rmb m)	1H10	2H10	1H11	YoY	HoH
Revenue	686	868	845	23%	-3%
Cost of sales	326	397	414	27%	4%
Gross profit	360	471	431	20%	-8%
<i>Gross margin</i>	<i>52%</i>	<i>54%</i>	<i>51%</i>		
Selling & distribution expenses	17	27	23	33%	-15%
Admin expenses	31	49	50	65%	3%
Operating profit	312	395	358	15%	-9%
<i>Operating margin</i>	<i>45%</i>	<i>46%</i>	<i>42%</i>		
Interest expenses	(11)	(3)	(10)	-14%	179%
Interest income	1	2	2	137%	-20%
Others	6	0	16	162%	58941%
Profit before tax	307	394	366	19%	-7%
Tax expenses	(52)	(66)	(62)	21%	-5%
<i>Tax rate</i>	<i>17%</i>	<i>17%</i>	<i>17%</i>		
Minority interest	(22)	(29)	(3)	-86%	-89%
Net income	234	300	301	29%	0%
<i>Net margin</i>	<i>34%</i>	<i>35%</i>	<i>36%</i>		

Source: Company data, Samsung Securities

Revenues reached Rmb845m in 1H11, up 23% YoY, but representing only 44% of our full-year forecast. Production volume for iron concentrates was only 1.0m tonnes, up 20% YoY, representing 43% of our full-year forecast. Production volume for iron pellets was only ~300,000 tonnes, down 17% YoY, representing 33% of our full-year forecast. China Vanadium reduced pellet production from a third-party plant to only 90,000 tonnes (down 58% YoY) as a result of the significant increase in pelletizing contracting fees.

Figure 5: Operations summary

	1H10	2H10	1H11	YoY	HoH
Production (tonnes 000s)					
Vanadium-bearing iron concentrates	866	1,142	1,039	20%	-9%
Ordinary iron concentrates	24	n.a.	3	-89%	n.a.
Iron pellets	362	352	300	-17%	-15%
Medium-grade titanium	40	61	72	79%	18%
High-grade titanium	34	33	58	69%	77%
Sales volume (tonnes 000s)					
Vanadium-bearing iron concentrates	507	810	703	39%	-13%
Ordinary iron concentrates	21	n.a.	3	-88%	n.a.
Iron pellets	376	352	335	-11%	-5%
Medium-grade titanium	37	47	54	47%	17%
High-grade titanium	31	31	57	85%	86%

Source: Company data, Samsung Securities

Despite the low volume, revenue was boosted by higher-than-expected selling prices. Selling prices for iron concentrates was Rmb664/t in 1H11 (7% higher than our forecast) and selling prices for high-grade titanium reached Rmb1,132/t (8% higher than our forecast).

Cost increases seem to be increasing faster than we expected, as the gross margin in 1H11 (51%) was flat compared to our forecast, despite the higher-than-expected selling prices. Management mentioned that the unit cost increase was mainly driven by increases in unit stripping costs and unit mining costs.

China Vanadium (893 HK)

Figure 6: Summary Financials

	12-09	12-10	12-11E	12-12E	12-13E
Profit & Loss (Rmb m)					
Revenue	1,084	1,554	1,998	2,452	2,794
COGS	-582	-724	-996	-1,245	-1,391
Gross profit	502	830	1,002	1,207	1,403
Gross profit margin (%)	46	53	50	49	50
Selling, general & admin	-64	-124	-134	-164	-187
Operating profit	438	707	868	1,043	1,216
Operating margin (%)	40	45	43	43	44
Interest expense	-4	-15	-8	-4	-4
Interest income	0	3	11	24	36
Others	3	6	-5	-5	-5
Profit before tax	437	701	867	1,058	1,244
Taxation	-70	-117	-139	-265	-311
Minorities	-39	-51	-80	-87	-103
Net income	328	533	648	707	830
Net income margin	30	34	32	29	30
Adjusted net income	328	533	648	707	830
Adjusted EPS, Rmb	0.20	0.26	0.31	0.34	0.40
DPS, Rmb	0.01	0.05	0.06	0.07	0.08
Dividend payout ratio (%)	6	20	20	20	20
EBITDA	480	798	991	1,191	1,377
EBITDA margin (%)	44	51	50	49	49
Balance Sheet (Rmb m)					
Current assets	2,304	1,542	1,885	2,908	3,760
Cash and cash equivalents	1,884	1,096	1,164	2,019	2,764
Trade receivables	137	208	219	269	306
Inventory	71	70	136	170	191
Other current assets	212	170	366	449	499
Fixed assets	496	1,476	2,004	2,105	2,195
Other non-current assets	344	784	521	513	505
Total assets	3,144	3,803	4,410	5,526	6,460
Current liabilities	-461	-813	-962	-1,261	-1,407
Borrowings due in <1 year	-100	-175	-50	-50	-50
Trade payables	-86	-255	-246	-307	-324
Other current liabilities	-275	-383	-667	-904	-1,033
Long-term liabilities	-6	-131	-55	-55	-55
Borrowings due >1 year	-6	-131	-55	-55	-55
Other long-term liabilities	0	0	0	0	0
Total liabilities	-467	-944	-1,017	-1,316	-1,462
Shareholders' equity	2,514	2,775	3,293	3,858	4,522
Total debt and sh. equity	3,144	3,803	4,410	5,526	6,460
Cash Flow (Rmb m)					
Pre-tax profit	437	701	867	1,058	1,244
Depreciation & amortisation	43	91	123	148	161
Increase in working capital	-106	485	67	165	60
Others	-31	-83	-413	-564	-662
Net cash from operating activities	342	1,194	643	807	801
Capex	-239	-975	-642	-242	-242
Associates & investments	0	0	0	0	0
Others	-89	-776	124	132	0
Net cash in investing	-328	-1,750	-518	-110	-242
Dividends paid	-24	0	-108	-130	-141
New debts / debts (repaid)	100	200	-250	0	0
Issue of shares	1,662	0	0	0	0
Others	0	-430	302	288	327
Net cash in financing	1,737	-230	-56	158	186
Net increase in cash	1,751	-788	69	855	745

	12-09	12-10	12-11E	12-12E	12-13E
Ratio Analysis					
PER (x)	19.8	12.8	5.8	5.3	4.5
Price to book (x)	3.7	2.3	1.1	1.0	0.8
Price to sales (x)	6.0	4.4	1.9	1.5	1.3
EV/EBITDA (x)	15.6	7.2	2.7	1.5	0.8
EV/Sales (x)	6.9	3.7	1.3	0.7	0.4
Dividend yield (%)	0.3	1.6	3.5	3.8	4.4
Revenues growth (%)	37	43	29	23	14
EBITDA growth (%)	21	66	24	20	16
EPS growth (%)	18	28	21	9	17
ROE (%)	21.5	20.2	21.4	19.8	19.8
ROA (%)	15.8	15.4	15.8	14.2	13.9
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash
Net debt to total capital (%)	net cash	net cash	net cash	net cash	net cash
Total debt to equity (%)	4.1	11.0	3.1	2.6	2.2
Interest cover (x)	110.9	61.5	nm	nm	nm
Interest and current liabs cover (x)	0.9	0.9	0.9	0.8	0.9
Current assets/current liabilities	5.0	1.9	2.0	2.3	2.7
Curr asset less cash/curr liab	0.9	0.5	0.7	0.7	0.7

	12-09	12-10	12-11E	12-12E	12-13E
Sales volume, tonnes 000s					
Iron concentrates	950	1,317	1,337	1,188	1,087
Iron pellets	693	728	850	1,250	1,350
Titanium concs - medium grade	167	83	151	52	2
Titanium concs - high grade	0	62	130	200	250
Selling prices, Rmb/t					
Iron concentrates	558	665	690	711	732
Iron pellets	775	875	919	947	975
Titanium concs - medium grade	102	99	180	100	100
Titanium concs - high grade	0	534	1,132	1,166	1,201
Cost of sales, Rmb000/t					
Iron concentrates	258	267	280	289	295
Iron pellets	429	453	544	560	571
Titanium concs - medium	239	250	263	270	276
Titanium concs - high	440	453	535	551	567

Shareholding Structure				
Shareholders	Code	No. of shares	%	
Trisonic Int'l Ltd	893 HK	1,198	58%	
Other public shares	893 HK	877	42%	
Total shares in issue		2,075	100%	

Source: Company data, Samsung Securities estimates

China Vanadium (893 HK)

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