

14 September 2016

Industrial | Misc. Manufacturer

Xinyi Glass Holdings

Buy (Maintained)

Recovery To Continue

Target Price: HKD8.40
 Price: HKD7.21
 Market Cap: USD3,543m
 Bloomberg Ticker: 868 HK

We resume coverage on Xinyi with a BUY and higher TP of HKD8.40 (from HKD5.20, 17% upside). We remain bullish on the stock due to:

1. Strong recurring net profit CAGR of 28% in FY15-17F, primarily driven by continued float glass GPM expansion and low-teen topline growth;
2. Undemanding valuations – TP implies 10x FY17F P/E, close to 10-year mean (ex-Xinyi Solar implied P/E of 11x vs 10-year mean of 13x).

This report marks the transfer of coverage to Cyrus Chong.

Recovery at float glass segment to sustain, premised on:

- i. Volume growth, stable pricing, market share gains from weaker competitors, Government supply-side reforms and industry rationalisation;
- ii. Improved demand from the property construction sector, a key user of float glass in China;
- iii. Declining natural gas import prices and potentially further domestic price cuts by China's National Development and Reform Commission (NDRC).

Our price checks indicate that industry float glass prices are up 10% YoY in 9M16 (1H16: 5.9%) while imported natural gas cost fell by c.31% YoY in 8M16 (2015: -26%). We expect float glass sales to grow by 6%/6% and GPM to expand to 22.4%/24.4% in FY16/17F respectively (1H16 GPM: 22.3%).

Automobile and construction glass are stable growth drivers, given:

- i. Strategic focus on high value-added low-emission (low-e) glass (for construction) and stable after-sales market (for automobile);
- ii. High level of vertical integration and economies of scale;
- iii. Rising demand for low-e glass on supportive Government policies.

We expect the automobile/construction glass segments to deliver revenue CAGR of 6%/10% respectively in FY15-18F on resilient gross margins.

Solar exposure via top-of-class platform. Xinyi Glass Holdings (Xinyi) has valuable solar sector exposure via c.27%-associate, Xinyi Solar Holdings (Xinyi Solar) (968 HK, NR), a well-run solar business platform with a dominant market position and experiencing explosive growth in downstream solar farm operations. Profit contributions from Xinyi Solar are expected to rise by 77%/37%/27% in FY16-18F, and account for c.17-22% of Xinyi's pre-tax profit. The stake in Xinyi Solar is worth c.HK\$5.8bn (c.21% of Xinyi's market cap).

BUY with higher HKD8.40 TP, pegged at 10x FY17F P/E, close to 10-year mean. Our new TP also implies 2.1x FY17F P/BV (1SD> LT-average), which we believe is fair as the company is in an earnings upcycle. Excluding Xinyi Solar, our TP implies 11x FY17F P/E for its non-solar glass businesses, below the historic average of 13x. Key risks include a rebound in production capacity in the float glass industry and sharp recovery in natural gas prices.

Share Data

Avg Daily Turnover (HKD/USD) 77.0m/9.93m
 52-wk Price low/high (HKD) 3.23 - 7.08
 Free Float (%) 53
 Shares outstanding (m) 3,881
 Estimated Return 17%

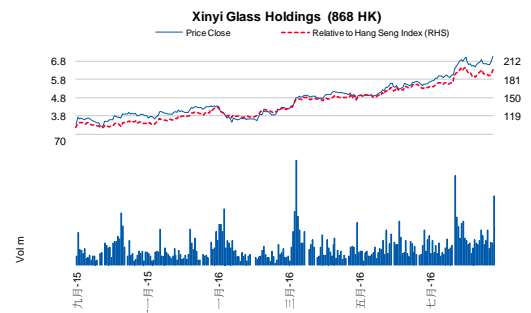
Shareholders (%)

Chairman Lee Yin Yee 21.3
 Other management staff 25.6

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	64.8	6.5	31.9	66.3	121.1
Relative	56.3	(0.9)	18.8	48.4	107.0

Source: Bloomberg



Source: Bloomberg

Forecasts and Valuations	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total turnover (HKDm)	10,861	11,460	12,926	14,283	15,725
Reported net profit (HKDm)	1,364	2,113	2,852	3,293	3,813
Recurring net profit (HKDm)	1,146	1,819	2,852	3,293	3,813
Recurring net profit growth (%)	(45.9)	58.7	56.8	15.5	15.8
Recurring EPS (HKD)	0.30	0.46	0.73	0.84	0.97
DPS (HKD)	0.15	0.26	0.35	0.41	0.47
Recurring P/E (x)	23.9	15.3	9.7	8.4	7.3
P/B (x)	2.25	2.18	1.93	1.76	1.60
P/CF (x)	14.1	9.9	7.8	6.8	6.0
Dividend Yield (%)	2.1	3.7	5.0	5.8	6.7
EV/EBITDA (x)	15.3	11.4	8.0	7.2	6.5
Return on average equity (%)	11.1	16.9	21.0	21.8	23.1
Net debt to equity (%)	42.0	37.2	33.1	26.7	20.1
Our vs consensus EPS (adjusted) (%)			5.4	3.7	5.7

Source: Company data, RHB

Analyst

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Financial Exhibits

Financial model updated on: 2016-09-07.

Asia
Hong Kong
Industrial
Xinyi Glass Holdings
Bloomberg 868 HK
Buy

Valuation basis

Long-term average P/E.

Key drivers

- Float glass price;
- Natural gas costs.

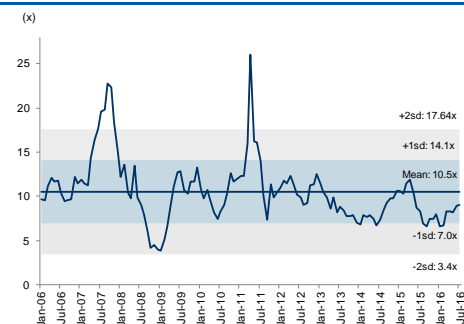
Key risks

- Weaker-than-expected glass demand and sharp rebound in raw material costs (in particular natural gas cost).

Company Profile

Founded in 1988 and listed in 2005, Xinyi Glass (Xinyi) is one of the largest glass producers in China. It has six major production bases – in Dongguan, Shenzhen, Jiangmen, Wuhu, Tianjin and Yingkou. It is also a one-stop maker of float glass, solar glass, auto glass and construction glass. The company's three major business segments – float glass, low-e construction glass and auto glass – accounted for 44%, 23% and 33% of total revenue in FY15. Xinyi spun off its solar business arm, Xinyi Solar (968 HK, NR), in late 2013, and now holds a 26.6% stake in the latter. The company also has an overseas production base in Malacca, Malaysia.

Xinyi's 1-year forward P/E



Source: Bloomberg

Financial summary	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Recurring EPS (HKD)	0.30	0.46	0.73	0.84	0.97
EPS (HKD)	0.35	0.54	0.73	0.84	0.97
DPS (HKD)	0.15	0.26	0.35	0.41	0.47
BVPS (HKD)	3.15	3.24	3.67	4.02	4.41
Weighted avg adjusted shares (m)	3,877	3,922	3,922	3,922	3,922

Valuation metrics	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Recurring P/E (x)	23.9	15.3	9.7	8.4	7.3
P/E (x)	20.1	13.1	9.7	8.4	7.3
P/B (x)	2.25	2.18	1.93	1.76	1.60
FCF Yield (%)	0.8	3.0	6.8	9.3	11.3
Dividend Yield (%)	2.1	3.7	5.0	5.8	6.7
EV/EBITDA (x)	15.3	11.4	8.0	7.2	6.5
EV/EBIT (x)	23.8	17.1	10.6	9.5	8.3

Income statement (HKDm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total turnover	10,861	11,460	12,926	14,283	15,725
Gross profit	2,733	3,133	4,451	4,943	5,473
EBITDA	1,707	2,282	3,344	3,709	4,100
Depreciation and amortisation	(612)	(763)	(820)	(880)	(922)
Operating profit	1,095	1,518	2,525	2,829	3,177
Net interest	(38)	(50)	(51)	(52)	(33)
Income from associates & JVs	138	317	560	767	975
Exceptional income - net	254	331	0	0	0
Pre-tax profit	1,593	2,380	3,279	3,830	4,434
Taxation	(228)	(266)	(426)	(536)	(621)
Minority interests	(1)	(0)	(0)	(0)	(0)
Recurring net profit	1,146	1,819	2,852	3,293	3,813

Cash flow (HKDm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Cash flow from operations	1,944	2,806	3,576	4,077	4,639
Capex	(1,729)	(1,967)	(1,700)	(1,500)	(1,500)
Cash flow from investing activities	(1,729)	(1,967)	(1,700)	(1,500)	(1,500)
Proceeds from issue of shares	(165)	0	0	0	0
Dividends paid	(902)	(608)	(1,284)	(1,482)	(1,716)
Cash flow from financing activities	(72)	(625)	(1,284)	(1,482)	(1,716)

Balance sheet (HKDm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total cash and equivalents	832	1,300	1,264	1,813	2,553
Tangible fixed assets	13,205	13,350	14,741	15,373	15,961
Intangible assets	79	75	75	75	75
Total investments	2,912	2,972	2,972	2,972	2,972
Total other assets	34	29	29	29	29
Total assets	21,034	21,422	22,837	24,408	26,149
Short-term debt	2,529	2,514	2,514	2,514	2,514
Other liabilities	255	63	63	63	63
Total liabilities	8,699	8,696	8,441	8,631	8,830
Shareholders' equity	12,333	12,718	14,388	15,770	17,311
Minority interests	2	7	7	7	7
Total equity	12,335	12,726	14,396	15,777	17,318
Net debt	5,181	4,729	4,764	4,215	3,475
Total liabilities & equity	21,034	21,422	22,837	24,408	26,149

Key metrics	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Revenue growth (%)	9.3	5.5	12.8	10.5	10.1
Recurrent EPS growth (%)	(47.1)	56.9	56.8	15.5	15.8
Gross margin (%)	25.2	27.3	34.4	34.6	34.8
Operating EBITDA margin (%)	15.7	19.9	25.9	26.0	26.1
Net profit margin (%)	12.6	18.4	22.1	23.1	24.2
Dividend payout ratio (%)	43.1	48.7	48.7	48.7	48.7
Capex/sales (%)	15.9	17.2	13.2	10.5	9.5
Interest cover (x)	12.1	16.8	26.2	29.3	32.9

Source: Company data, RHB

Head-To-Head Comparison Of Listed Peers

	Xinyi Glass Recovery Play	Flat Glass PV Glass Manufacturing Play	China Glass Victim of Industry Consolidation	Fuyao Glass Best-in-Class Auto Glass in OEM	Luoyang Glass A High-Cost Producer	CSG (南玻集团) Expensive Recovery Play	Kibing (株洲旗滨) Over-Diversification
Company Background							
Ticker	868 HK	6865 HK	3300 HK	3606 HK, 600660 CH	1108 HK	000012 CH	601636 CH
Rating	BUY	NR	NR	NR	NR	NR	NR
Year est.	1988	1998	2004	1987	1994	1984	2005
Major shareholder	Lee Yin Yee	Ruan Hongliang	Cao Zhijiang	Cho Tak Wong	State-owned	Qianhai Insurance	Kibing Group
Operation Background							
# of employees	12,746	~3,000	4,078	21,833	~4,000	~10,000	~6,000
# of production lines	n/a	~60	17	n/a	n/a	~15	23
o/w: float	n/a	2	14	n/a	n/a	10	n/a
Daily float glass melting capacity (tpd)	~13,800	~1,200	7,630	n/a	~2,000	~7,000-8,000	14,600
Export as % of sales	~30%	~40%	~29%	~50%	Limited	~10%	~3%
Foothold markets	Anhui, Tianjin, Guangdong		Jiangsu, Shandong	Fujian, Shanghai, Chongqing	Henan		Fujian, Guangdong, Hunan
Key products	Float, Low-E, Auto glass	PV, float, Low-E	Float, PV, Low-E	Auto glass, float	Ultra-thin float, silica sand	Flat, Low-E, PV, electronic glass	Float, Low-E, PV
Key COGS items (our estimates)	Natural gas (30%), Electricity (12), Soda ash (10), PVB (9)	Fuel (24%), Electricity (13), Soda ash (13), Packaging materials and coating liquid (12), Silica sand (11)	Energy (45), Soda ash (15)	Float glass (28%), Energy (16), PVB (11)	Energy (45%), Soda ash (10)	Natural gas (30%), Soda ash (10)	Natural gas (30%), Soda ash (10)
Float glass capacity growth (2015)	+9.6%	Flat	Flat	n/a	n/a	n/a	n/a
Float glass capacity growth (2016e)	+15.8%	Flatish	Flatish	n/a	n/a	n/a	n/a
Customer/Product Mix							
Automotive glass	33%	0%		~97%	0%	n/a	
Construction glass	23%	~12%		0%	0%	~36%	
Float glass	44%	~10%	Primarily construction glass	~100% for internal use	~100%	~44%	Primarily construction glass
PV glass	Thru' 26%-owned XYS	~75%					
Others	0%	~3%		~3%	0	~20%	
Financial data - 1H16							
Revenue (Rmb mn)	5,885	1,522	918	7,584	137	4,228	3,013
% y/y	11%	1.6%	-3%	15%	-63%	27%	30%
Net profit (Rmb mn)	1,369	331	-94	1,440	-26	467	125
% y/y	45%	71%	n/a	18%	n/a	127%	100%
GPM (%)	34.7%	36.8%	10.5%	42.2%	5.9%	n/a	20.5%
NPM (%)	23.3%	21.8%	-10.3%	19.0%	-18.8%	11.0%	4.1%
Financial data - FY15							
Revenue (Rmb mn)	11,460	2,914	1,969	13,573	662	7,430	5,169
% y/y	6%	3%	-21%	5%	0%	5%	4%
Net profit (Rmb mn)	2,113	434	-426	2,605	144	300	171
% y/y	55%	10%	n/a	17%	583%	-32%	-45%
GPM (%)	27.3%	29.3%	4.0%	41.5%	2.4%	21.6%	18.0%
NPM (%)	18.4%	14.9%	-21.7%	19.2%	Core NPM: -0.1%	8.4%	3.3%
Staff costs as % of sales	8.5%	6.9%	13.7%	15.0%	7.6%	3.7%	2.2%
R&D as % of sales	n/a	3.5%	0.1%	4.4%	2.1%	3.2%	n/a
Net debt to equity	38%	5%	47%	-7%	221%	65%	82%

Source: Company data, RHB

Float Glass Business Recovery Intact

Float glass business recovery momentum to sustain

We expect the float glass business of Xinyi (c.44%/18% of total revenue/GP respectively in FY15 and historically a key swing factor to Xinyi's overall profitability) to report decent profit growth and continued margin recovery in 2H16 and FY17.

In our view, the recovery is premised on:

- i. Mid-single digit to low-teen volume growth and stable pricing, as Xinyi gains market share from weaker competitors on Government's supply-side reform initiatives and rationalisation of industry supply;
- ii. Improved demand from the property construction sector, a key user of float glass in China;
- iii. Declining natural gas import prices into China and further potential domestic price cuts by China's National Development and Reform Commission in 2016/2017.

Accelerated float glass price rebound since May

Float glass market prices across major cities in China have rebounded since Jun-2015. Following a 5.9% YoY increase in 1H16, industry float glass prices continued to rise c.12% since end-1H16.

In our view, this recovery trend should continue into 2H16 and FY17F on the back of improved industry supply dynamics. We reckon that many high-cost regional producers with substandard production lines have exited the market following years of cost pressures as a result of high raw material costs (including heavy oil and natural gas). We estimate that every 1% change in float glass average selling prices (ASPs) will lead to a 1.5% change in Xinyi's net profit.

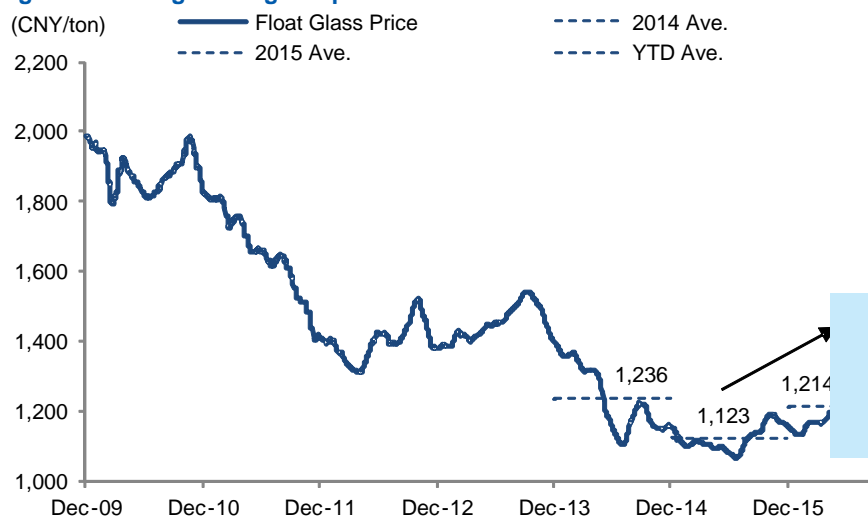
In fact, effective capacity (ie capacity operating on a regular basis) of the flat glass industry (of which float glass represented c.80% in 2015) declined by c.3% YoY in 2015, according to Xinyi.

As at August, there were 352 float glass production lines in China, of which 239 were effective. The number of suspended lines accounted for c.32% of total production lines in China. While we believe that some idle lines have been put back to operation on improved margin outlook – given that suspended lines fell from 38% in April – we believe the rebound in effective capacity will be manageable, as many remain unprofitable even at the current price/cost levels.

In addition, as private enterprises represent some 80% of the float glass market, chances of having poor performing state-owned players are lower. For instance, the collapse of the Jiangsu Farun (the largest glass manufacturer for over a decade until 2010) in 2015 due to over expansion and substandard pollution control, shows inefficient players will not be bailed out.

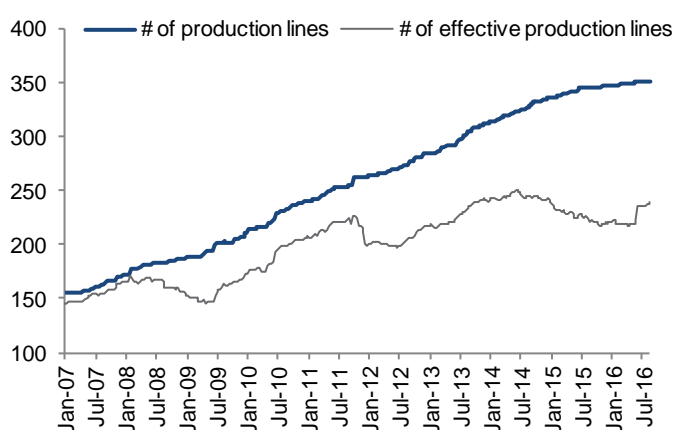
Overall, we are projecting flattish effective industry capacity growth in 2016/17, as smaller players exit the market on low efficiency, and the Government pushes supply-side reform initiatives.

Figure 1: Average float glass prices in China



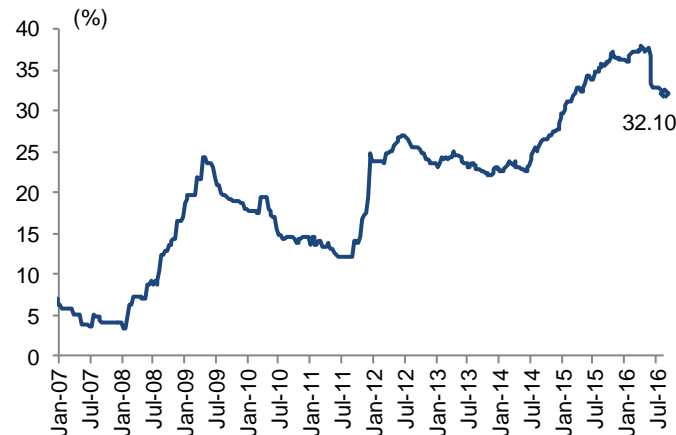
Source: Wind, RHB

Figure 2: Number of float glass production lines in China



Source: Wind, RHB

Figure 3: Percentage of production lines in suspension

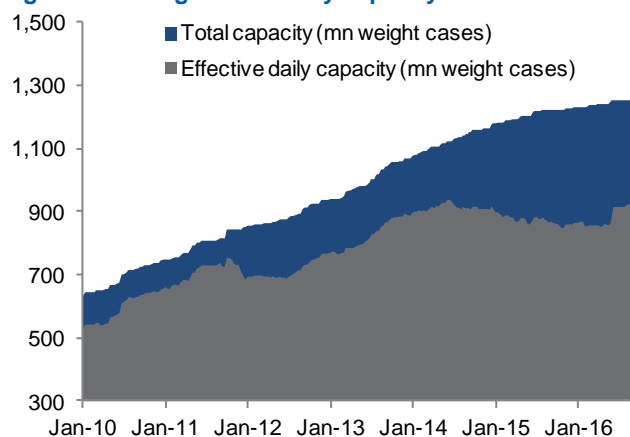


Source: Wind, RHB

Although we saw a modest rebound in effective daily capacity in recent months as some idle production lines have been put back to operation, we are of the view that the modest supply increase has been largely absorbed by the market given stable industry inventory levels.

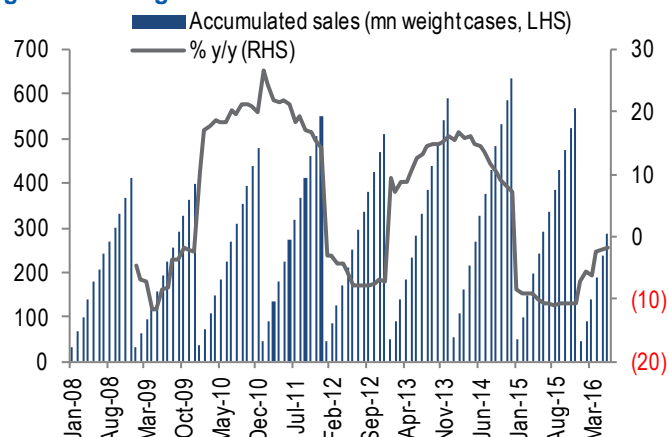
Inventory levels have actually declined from c.35m weight cases to c.32m weight cases since March. Inventory levels as a percentage of effective capacity has been stable at c.3-4% for the past one year, implying healthy supply/demand dynamics.

Figure 4: Float glass industry capacity in China



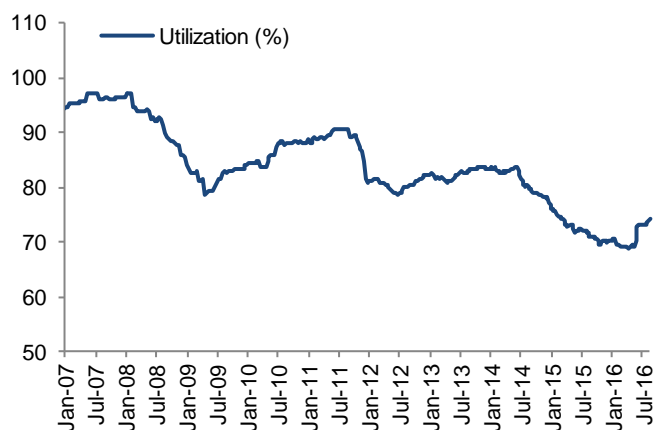
Source: Wind, RHB

Figure 5: Float glass sales in China



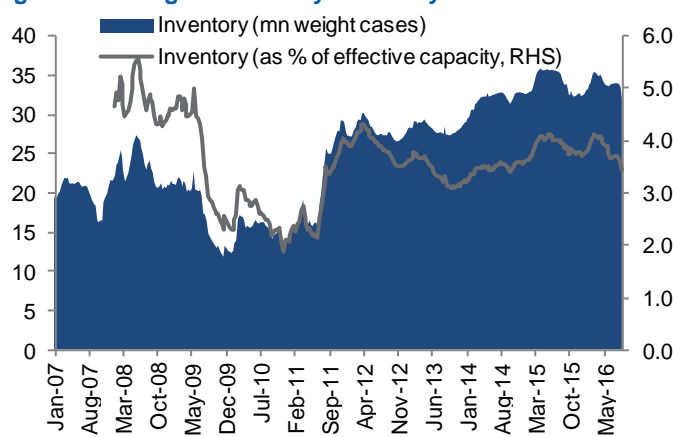
Source: Wind, RHB

Figure 6: Float glass industry utilisation rates in China



Source: Wind, RHB

Figure 7: Float glass industry inventory levels in China



Source: Wind, RHB

End-market demand stabilises

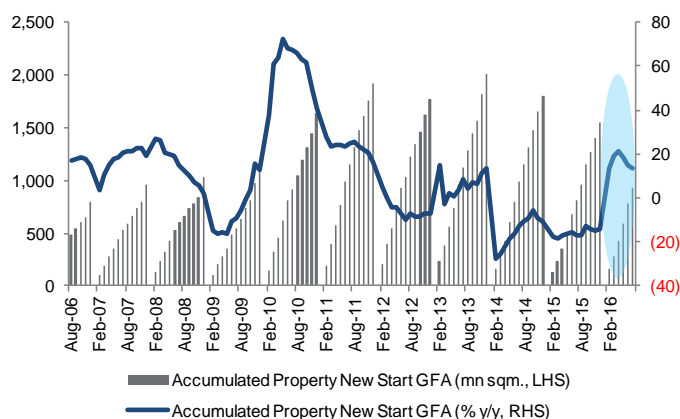
According to the China Architectural and Industrial Glass Industry Association, around 60% of float glass produced in China is used in construction and related industries (eg windows and walls), while automobile-related demand accounts for c.20% (a typical passenger vehicle uses 5-6 pieces of glass as wind shield, windows and display boards).

The turnaround in accumulated property new starts since February (c.13.7% YoY growth during 7M16) shows that demand from the property sector is picking up following two years of sluggishness.

The automobile market data also paints an encouraging picture. According to China Association of Automobile Manufacturers (CAAM), accumulated auto sales during 7M16 were up 9.8% YoY. The robust growth in new-energy vehicles (+98.1% YoY to 207,000 units during 7M16) and rising middle class in China should continue to drive auto-glass demand for both the new car and replacement markets.

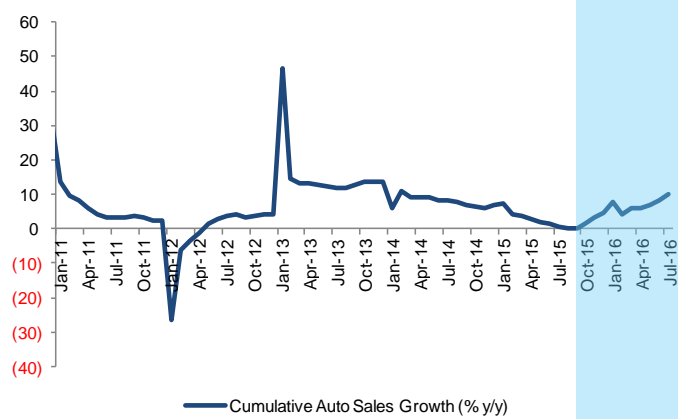
According to CAAM, auto sales in China are expected to rise 6.1% YoY in 2016, which implies a healthy growth pace for the rest of 2016. CAAM also forecasts new-energy car sales to reach 700,000 in 2016.

Figure 8: Property new start gross floor area (GFA) in China



Source: Wind, RHB

Figure 9: Auto sales growth in China

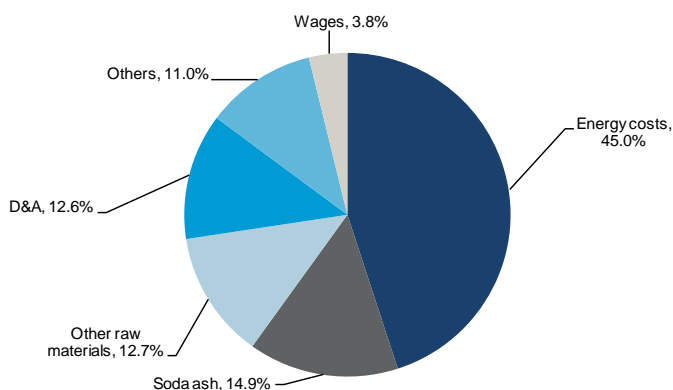


Source: Wind, RHB

Natural gas price decline, stable soda ash price – additional margin drivers

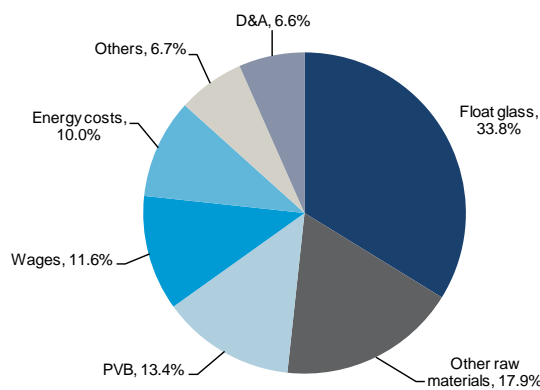
Based on information disclosed by peer companies – including Flat Glass Group (FGG) (6865 HK, NR) and Fuyao Glass Industry Group (Fuyao) (3606 HK, NR) – we estimate that natural gas cost accounts for c.30% of Xinyi’s total cost of goods sold (COGS), followed by electricity (c.12%), soda ash (c.10%) and polyvinyl butyral (PVB) (c.9%). According to Xinyi’s management, imported natural gas accounts for c.40% of total gas usage (mainly for its production plants in Guangdong) while domestic gas sources account for the remaining c.60%.

Figure 10: Estimated float glass COGS breakdown



Source: Company data, RHB

Figure 11: Estimated automobile glass COGS breakdown



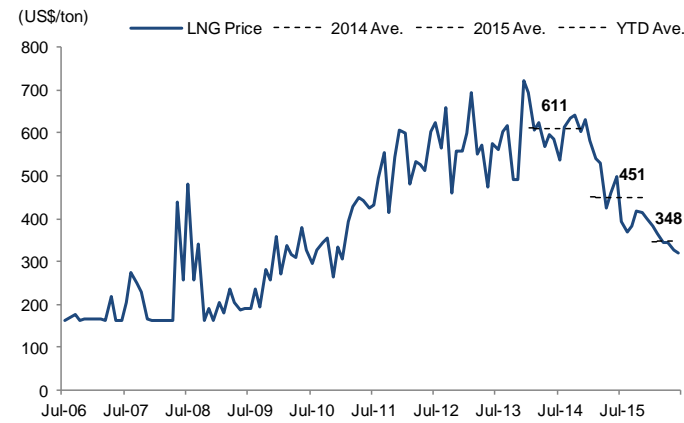
Source: Company data, RHB

The imported natural gas price is closely tied to international gas prices, which have plummeted c.50% since 2014 as the shale gas boom in US ignited an oversupply situation. For instance, imported gas price (in USD terms) has declined by c.31% YoY during 8M16, after falling c.26% YoY in 2015.

Domestic gas prices are regulated by the NDRC with price adjustments on an irregular basis. In Nov 2017, NDRC initiated a price cut of CNY0.7/cubic meter (c.28% cut on average) for non-residential city-gate gas. The market is generally expecting another price cut in late-2016 or 2017, given weak downstream industrial demand on elevated domestic prices.

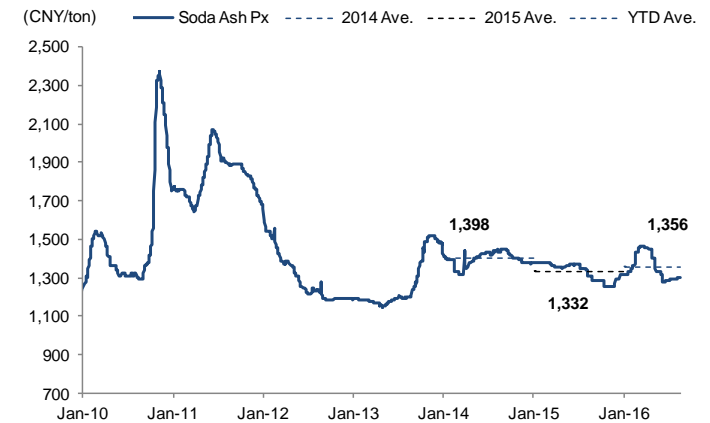
Soda ash, another key cost component, has seen stable price movements in the range of c.CNY1,200-1,500/tonne in the past few years. Given the balanced supply and demand situation in China and globally, we expect the stable price trend for soda ash to continue into 2H16F and FY17F.

Figure 12: Liquefied natural gas import price in China



Source: Wind, RHB

Figure 13: Soda ash price in China



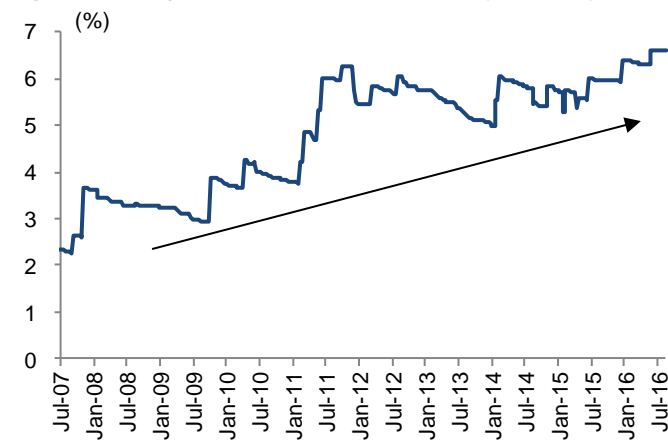
Source: Wind, RHB

Respectable market share gains over the past decade

The float glass industry in China is highly fragmented with the top 10 players accounting for c.34% of total capacity. According to our estimates, Xinyi is the largest player with c.6.6% market share by capacity as at August.

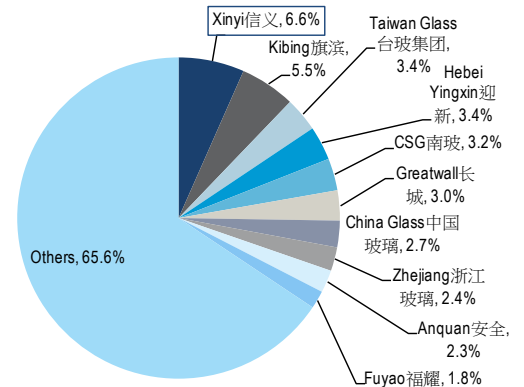
Our calculations show that Xinyi has gained market share from competitors since the financial crisis in 2008, by leveraging on its solid balance sheet and ready access to international funding sources supported by its HK listing status. We highlight that Xinyi's float glass capacity has jumped from c.2,600 tonnes/day at end-2006 to c.13,800 tonnes/day at the end of August, whilst its market share has increased from an estimated 2% to 6.6% over the same period.

Figure 14: Xinyi's market share in China by capacity



Source: Wind, RHB

Figure 15: Float glass market share by capacity (August)



Source: Wind, RHB

Stable Auto Glass Business

Xinyi focuses on after-sales replacement market

The automotive glass market is typically divided into two segments:

- i. Original equipment manufacturers (OEM) market for glass products that are sold to automobile manufacturers for installation on new vehicles;
- ii. After sales replacement glass (ARG) market for products sold to aftermarket suppliers for replacement purposes.

While the overall automotive glass market is dominated by Fuyao given its strong foothold in the OEM market segment (c.90% of industry volume), we believe Xinyi has carved a niche for itself by focusing on the ARG market (c.10% of total automotive glass market volume). Auto glass sales accounted for c.33%/54% of Xinyi's sales/GP in FY15.

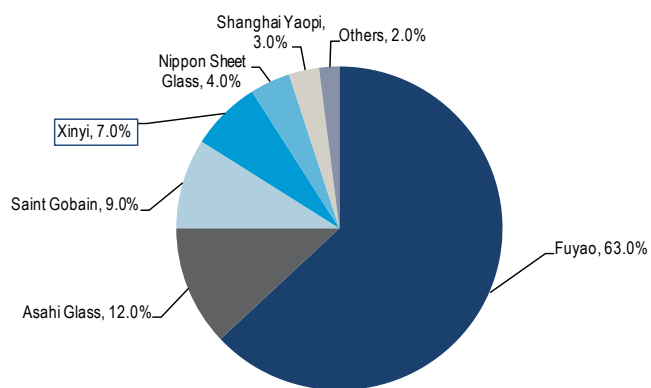
Xinyi has a long history of supplying laminated windshields to overseas customers. According to Xinyi, its automobile glass accounts for over 20% of the world's aftermarket automobile glass production and is exported to over 130 countries.

By export volume, Xinyi is the largest exporter in the automobile aftermarket sector. North America (primarily US and Canada) and Europe are key export markets for Xinyi's automobile business.

According to the International Organisation of Motor Vehicle Manufacturers (OICA), the number of vehicles in use globally has been growing steadily at low-to-mid single digit per year since 2005-2014. Despite the global financial crisis in 2009, the total number of vehicles in use still managed to grow by 2.8% YoY.

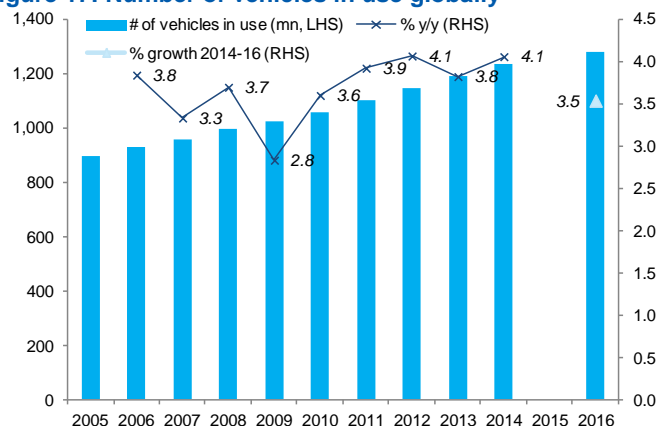
The North American and European markets also showed resilient growth. Based on the estimates done by the Automotive Aftermarket Industry Association (AAIA), vehicles on average have a windshield replacement rate of 3.39% every year. Driven by steady replacement demand, we believe that the after-sales market is a smaller but more stable market compared to the OEM market.

Figure 16: Automobile glass market in China (2013)



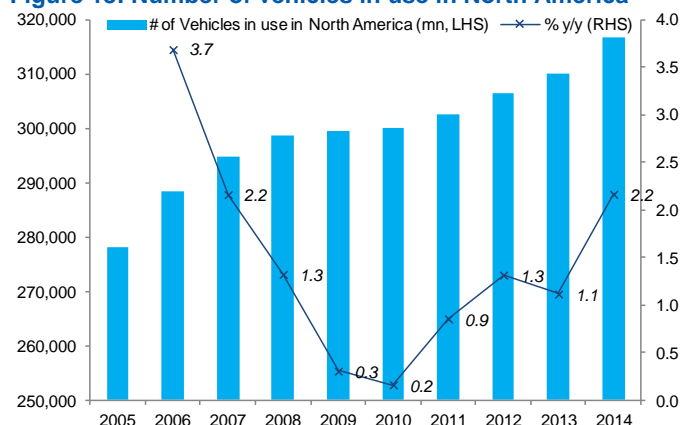
Source: Fuyao Glass prospectus, RHB

Figure 17: Number of vehicles in use globally



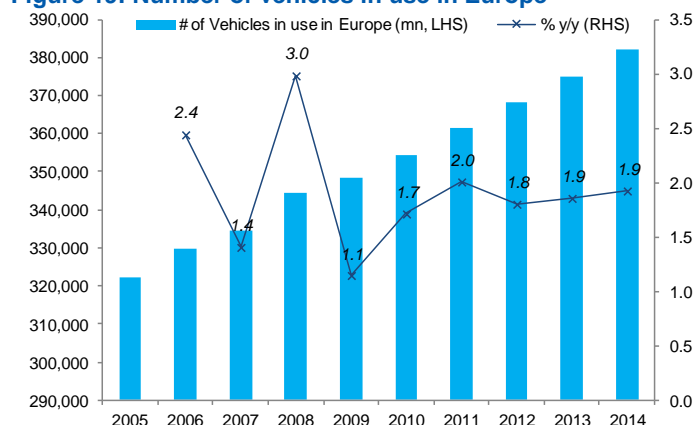
Source: OICA, RHB

Figure 18: Number of vehicles in use in North America



Source: OICA, RHB

Figure 19: Number of vehicles in use in Europe



Source: OICA, RHB

Industry supply-demand dynamics

Float glass is a major type of raw flat glass, generally used for further processing into other glass products (eg curtain walls, household glass, automobile glass) and accounted for over 90% of all flat glass production in China. Therefore, flat glass industry data is highly representative of the float glass industry.

The flat glass industry has long been a target for the NDRC to impose out-dated capacity elimination and tighter environmental controls on new capacity. According to the Ministry of Industry and Information Technology (MIIT) in China, flat glass capacity of c.173m weight cases per year has been eliminated by the Chinese Government since 2010-2014.

We estimate a further c.51.8m/53.8m of capacity to be eliminated by the Government in 2015/2016. Together with some out-dated capacity eliminated (to be eliminated) by market forces, we estimate that effective capacity has declined by c.11% in 2015, and will only grow by a modest 4%/3% in 2016/2017.

Figure 20: Flat glass industry supply and demand

(m weight case/year)	2008	2009	2010	2011	2012	2013	2014	2015	2016F	2017F
New addition		88.0	106.0	117.0	84.0	82.0	87.0	-46.0	46.0	40.0
Total capacity	603.0	691.0	797.0	914.0	998.0	1080.0	1167.0	1121.0	1167.0	1207.0
Capacity phased out by Gov't			18.4	30.4	58.6	28.0	37.6	51.8^	53.8	55.8
Idle/Phased-out capacity	104.0	107.0	90.0	174.0	169.0	190.0	196.0	259.0	269.0	279.0
Effective capacity	499.0	584.0	707.0	740.0	829.0	890.0	971.0	862.0	898.0	928.0
% YoY		17%	21%	5%	12%	7%	9%	-11%	4%	3%
Production	598.9	585.7	663.3	791.1	750.5	792.9	831.3	738.6	769.5	795.2

Source: Wind, MIIT, RHB. ^Our estimates

Leader In Energy-Saving Construction Glass

Largest low-e glass manufacturer in China

Xinyi is the largest manufacturer of energy-saving low-e construction glass in China, with a market share of c.18% in terms of sales volume (2014).

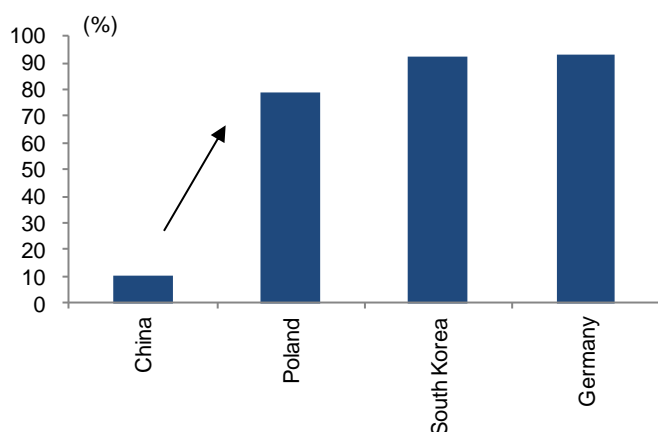
Low-e glass is a type of glass that is coated with a thin film to reduce the emission of radiant infrared energy. Low-e glass is generally used in the real estate industry to improve the energy efficiency of buildings via reducing thermal exchange between the building and the outside environment.

Low-e glass is a major product within the architectural glass product type. The low-e glass segment is rather consolidated with the top four players accounting for c.57% of the total market.

According to Frost & Sullivan, the sales volume for low-e glass in China is expected to reach 280.9m square meter in 2020 from 158.2m sqm in 2014, translating to c.10% CAGR over the same period. We believe the strong growth is primarily driven by rising standards on the energy efficiency of buildings in China.

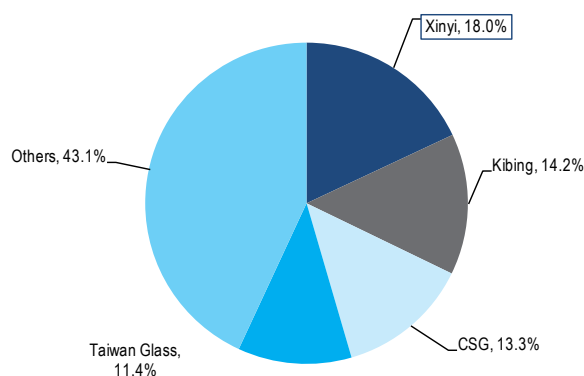
The penetration rate of low-e glass in China is still very low at c.11%, compared to >80% in developed countries such as Germany and the US. Construction glass (primarily low-e glass) accounted for c.23%/29% of Xinyi's sales/GP in FY15.

Figure 21: Low-e glass penetration rates



Source: ASKCI, RHB

Figure 22: China's low-e glass industry market share by volume (2014)



Source: Flat Glass, RHB

Xinyi Solar: China's Largest Solar Glass Maker

Solar glass exposure via c.27%-owned Xinyi Solar

Xinyi Solar used to be a fully-owned subsidiary of Xinyi before the former's spin-off in Dec 2013 on the main board. Xinyi held a 31.2% stake in Xinyi Solar immediately after the spin-off.

After three rounds of placements in Aug 2014, Mar 2015 and Oct 2015, Xinyi's shareholding in Xinyi Solar was reduced to 26.54%. The contribution from Xinyi Solar is reflected under "share in profit/loss of associates" at Xinyi.

There is very strong market demand for solar glass currently as the Chinese Government pushes forward its aggressive photovoltaic (PV) installation target for 2020. Xinyi Solar is the largest solar glass manufacturer in China with a dominant market share of c.30-35%.

Leveraging on its solar glass manufacturing capabilities and EPC experience, Xinyi Solar is rapidly expanding into the downstream solar farming business, which should display explosive growth over the next two years, in our view.

At end-1H16, Xinyi Solar had around 1,074MW grid-connected solar farm projects, which included 20MW wholly-owned projects, 954MW projects held by 75%-owned subsidiaries (Xinyi Energy), and a 100MW project held by a joint-venture (JV). Xinyi Solar has set an installation target of 1.7GW cumulative installed capacity by end-2016.

Based on an installation scale of c.1,000MW per year during FY16-18F, we estimate solar farms' contribution to Xinyi Solar's GP to rise to 23%, 34% and 40% for the three-year period, from 13% in FY15.

Net profits at Xinyi Solar are projected to reach c.HKD2.1bn, 2.9bn and 3.7bn in FY1-18, translating to associate profit contributions of c.HKD560m, HKD767m HKD975m respectively for Xinyi (or c.17-23% of Xinyi's pre-tax profit).

Our net profit estimates for Xinyi Solar is c.4%/10%/20% higher than consensus estimates mainly due to higher margin assumptions. Our assumptions for solar farm projects include:

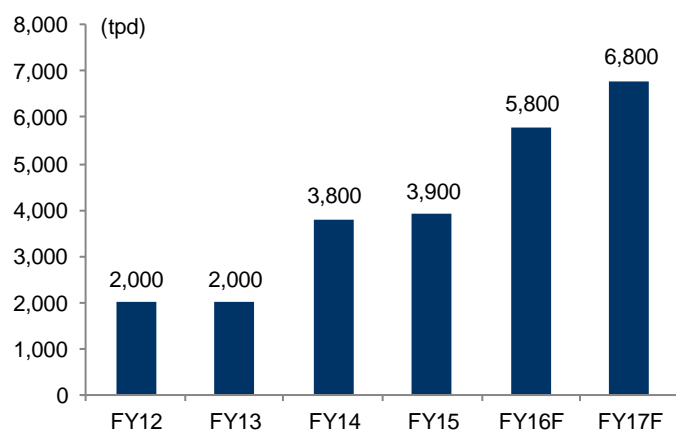
- i. Utilisation hours of c.1,100 per year;
- ii. Tariff of c.CNY0.86-0.9 per kWh;
- iii. GPM of 71%, 68% and 68% for FY16F-18F.

Figure 23: Xinyi Solar's solar farm projects

Project Location	Capacity (MW)	Grid-Connection Start
Jinzhai, Lu'an, Anhui	150	4Q14
Sanshan, Wuhu, Anhui	100	1Q15
Nanping, Fujian	30	1Q15
Lixin, Bozhou, Anhui - Phase 1	40	3Q15
Lixin, Bozhou, Anhui - Phase 2	100	1Q16
Wuwei, Wuhu, Anhui	100	4Q15
Hongan, Hubei - Phase 1	50	4Q15
Hongan, Hubei - Phase 2	50	1Q16
Fanchang, Anhui - Phase 1	40	4Q15
Fanchang, Anhui - Phase 2	20	2Q16
Shou, Lu'an, Anhui	100	4Q15
Tianjin Binhai	174	1Q16
Huainan, Anhui	20	1Q16
Total (end-1H16):	974	
2H16 Addition	380	
FY17 Addition	1,000	
FY18 Addition	1,000	

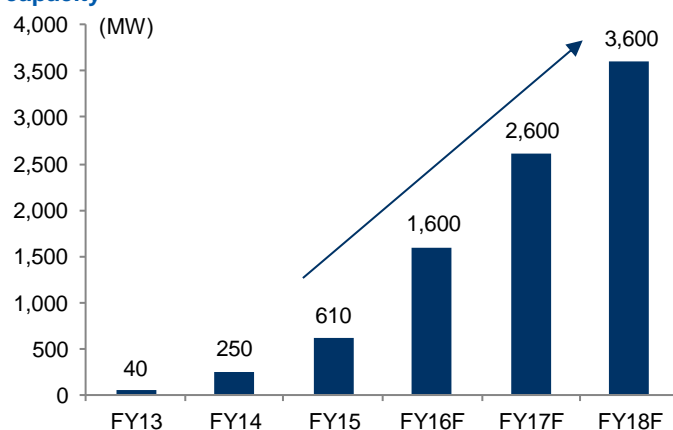
Source: Company data, RHB

Figure 24: Xinyi Solar's raw PV glass capacity



Source: Company data, RHB

Figure 25: Xinyi Solar's solar farm cumulative installed capacity



Source: Company data, RHB

Earnings Forecasts And Financials

Changes to our estimates

We have raised our earnings estimates for Xinyi after factoring in:

- i. Higher ASP and margin estimates for the float glass segment following the strong 1H16 results, and sustained ASP and cost trends into 2H16F. We expect continued gross margin recovery for the float glass segment to 22.4%/24.2% in FY17F/FY18F due to the pick-up in property new start activities and more controlled industry capacity expansion;
- ii. Stronger earnings contributions from Xinyi Solar, as we believe the solar farm expansion will accelerate into FY16F/FY17F. We have also introduced estimates for FY18 post the release of 1H16 results.

Overall, we have revised up our recurring net profit estimates by 38%/34% in FY16F/17F and are projecting growth of 57%/16%/16% in FY16-18F. The growth is primarily driven by:

- i. Steady auto glass and construction glass businesses;
- ii. Continued margin recovery at the float glass business;
- iii. Rising contributions from solar power associate, Xinyi Solar.

Our net profit estimates for Xinyi are 4.3%/3.0%/4.2% higher than consensus estimates in FY16-18F.

Figure 26: Changes to our Xinyi earnings estimates and turnover mix

(HKDm)	FY16F			FY17F			FY18F
	New	Old	Chg	New	Old	Chg	New
Turnover							
Auto glass	4,014	4,211	-4.7%	4,255	4,378	-2.8%	4,510
Construction glass	2,946	3,412	-13.7%	3,213	3,829	-16.1%	3,505
Float glass	5,936	5,930	0.1%	6,714	6,554	2.4%	7,595
Total	12,895	13,553	-4.9%	14,182	14,761	-3.9%	15,610
GPM							
Auto glass	49.0%	43.7%	5.3 ppt	48.0%	43.7%	4.3 ppt	48.0%
Construction glass	39.0%	31.0%	8.0 ppt	39.0%	31.0%	8.0 ppt	39.0%
Float glass	22.4%	11.9%	10.5 ppt	24.2%	13.8%	10.4 ppt	25.2%
Blended	34.4%	26.6%	7.8 ppt	34.6%	27.1%	7.5 ppt	34.8%
Revenue	12,926	13,553	-4.6%	14,283	14,761	-3.2%	15,725
Gross profit	4,451	3,605	23.5%	4,943	4,005	23.4%	5,473
Operating profit	2,770	2,005	38.2%	3,115	2,307	35.0%	3,492
Share of profit of an associate	560	439	27.6%	767	607	26.4%	975
Profit before tax	3,279	2,407	36.2%	3,830	2,876	33.2%	4,434
Reported net profit	2,852	2,061	38.4%	3,293	2,463	33.7%	3,813
Recurring net profit	2,852	2,061	38.4%	3,293	2,463	33.7%	3,813
Gross margin	34.4%	26.6%	7.8 ppt	34.6%	27.1%	7.5 ppt	34.8%
Operating margin	21.4%	14.8%	6.6 ppt	21.8%	15.6%	6.2 ppt	22.2%
Net margin	22.1%	15.2%	6.9 ppt	23.1%	16.7%	6.4 ppt	24.2%
Recurring profit margin	22.1%	15.2%	6.9 ppt	23.1%	16.7%	6.4 ppt	24.2%

Source: Company data, RHB

Figure 27: Xinyi's net profit estimates vs consensus

(HKD m)	2016F	2017F	2018F
RHB	2,852	3,293	3,813
Consensus	2,734	3,198	3,658
% Difference	4.3%	3.0%	4.2%

Source: Bloomberg, Company data, RHB

Figure 28: Xinyi's detailed P&L

(HKDm)	1H15	2H15	1H16	2H16F	FY14	FY15	FY16F	FY17F	FY18F
Revenue									
Auto glass	1,897	1,890	1,990	2,024	3,593	3,787	4,014	4,255	4,510
Construction glass	1,206	1,445	1,220	1,711	2,556	2,651	2,931	3,197	3,488
Float glass	2,180	2,843	2,675	3,306	4,712	5,022	5,981	6,831	7,728
Total	5,283	6,177	5,885	7,040	10,861	11,460	12,926	14,283	15,725
% YoY									
Auto glass	6.5%	4.2%	4.9%	7.1%	9.3%	5.4%	6.0%	6.0%	6.0%
Construction glass	11.8%	-2.1%	1.1%	18.4%	18.6%	3.8%	10.6%	9.1%	9.1%
Float glass	0.2%	12.0%	22.7%	16.3%	4.9%	6.6%	19.1%	14.2%	13.1%
Total	4.9%	6.0%	11.4%	14.0%	9.3%	5.5%	12.8%	10.5%	10.1%
% Mix									
Auto glass	35.9%	30.6%	33.8%	28.7%	33.1%	33.0%	31.1%	29.8%	28.7%
Construction glass	22.8%	23.4%	20.7%	24.3%	23.5%	23.1%	22.7%	22.4%	22.2%
Float glass	41.3%	46.0%	45.5%	47.0%	43.4%	43.8%	46.3%	47.8%	49.1%
GPM									
Auto glass	44.1%	44.6%	48.7%	49.3%	41.8%	44.3%	49.0%	48.0%	48.0%
Construction glass	31.7%	35.6%	39.0%	39.0%	35.3%	33.9%	39.0%	39.0%	39.0%
Float glass	8.7%	12.9%	22.3%	22.5%	7.0%	11.1%	22.4%	24.2%	25.2%
Blended	26.7%	27.9%	34.7%	34.2%	25.2%	27.3%	34.4%	34.6%	34.8%
Revenue	5,283	6,177	5,885	7,040	10,861	11,460	12,926	14,283	15,725
% YoY	4.9%	6.0%	11.4%	14.0%	9.3%	5.5%	12.8%	10.5%	10.1%
COGS	(3,873)	(4,455)	(3,844)	(4,631)	(8,128)	(8,328)	(8,475)	(9,340)	(10,252)
Gross profit	1,410	1,723	2,041	2,409	2,733	3,133	4,451	4,943	5,473
<i>GPM</i>	26.7%	27.9%	34.7%	34.2%	25.2%	27.3%	34.4%	34.6%	34.8%
Other income	112	103	104	51	178	215	155	186	204
Selling and marketing costs	(312)	(367)	(351)	(411)	(608)	(680)	(763)	(843)	(912)
Administrative expenses	(441)	(494)	(533)	(630)	(1,030)	(935)	(1,163)	(1,271)	(1,384)
<i>Opex% sales</i>	(14.2%)	(14.0%)	(15.0%)	(14.8%)	(15.1%)	(14.1%)	(14.9%)	(14.8%)	(14.6%)
Gain on spin off	--	--	--	--	--	--	--	--	--
Operating profit	944	1,168	1,304	1,467	1,494	2,113	2,770	3,115	3,492
<i>OPM</i>	17.9%	18.9%	22.2%	20.8%	13.8%	18.4%	21.4%	21.8%	22.2%
% YoY	11.9%	79.7%	38.1%	25.5%	(59.2%)	41.4%	31.1%	12.4%	12.1%
Non-recurring items	156	--	--	--	254	331	--	--	--
Finance costs	(46)	(44)	(60)	(36)	(91)	(90)	(96)	(96)	(96)
Share of profit of an associate	161	157	312	248	138	317	560	767	975
PBT	1,085	1,295	1,572	1,707	1,593	2,380	3,279	3,830	4,434
Tax	(138)	(128)	(202)	(224)	(228)	(266)	(426)	(536)	(621)
<i>Tax rate</i>	(12.7%)	(9.9%)	(12.9%)	(13.1%)	14.3%	11.2%	13.0%	14.0%	14.0%
Minority interests	(2)	1	0	(0)	(1)	(0)	(0)	(0)	(0)
Reported NP	945	1,168	1,370	1,483	1,364	2,113	2,852	3,293	3,813
<i>NPM</i>	17.9%	18.9%	23.3%	21.1%	12.6%	18.4%	22.1%	23.1%	24.2%
% YoY	24.0%	94.1%	45.0%	26.9%	(61.3%)	55.0%	35.0%	15.5%	15.8%
Recurring NP	789	1,168	1,370	1,483	1,146	1,819	2,852	3,293	3,813
<i>NPM</i>	14.9%	18.9%	23.3%	21.1%	10.6%	15.9%	22.1%	23.1%	24.2%
% YoY	39.1%	130.1%	73.7%	26.9%	(45.9%)	58.7%	56.8%	15.5%	15.8%

Source: Company data, RHB

Figure 29: Xinyi's key assumptions

	2013	2014	2015	2016F	2017F	2018F
Sales (HK\$ m)						
Auto glass	3,287	3,593	3,787	4,014	4,255	4,510
Construction glass	2,155	2,556	2,651	2,931	3,197	3,488
Float glass	4,494	4,712	5,022	5,981	6,831	7,728
Total	9,936	10,861	11,460	12,926	14,283	15,725
Sales Mix (%)						
Auto glass	33.1%	33.1%	33.0%	31.1%	29.8%	28.7%
Construction glass	21.7%	23.5%	23.1%	22.7%	22.4%	22.2%
Float glass	45.2%	43.4%	43.8%	46.3%	47.8%	49.1%
Revenue growth (%)						
Auto glass	6.8%	9.3%	5.4%	6.0%	6.0%	6.0%
Construction glass	36.8%	18.6%	3.8%	10.6%	9.1%	9.1%
Float glass	18.9%	4.9%	6.6%	19.1%	14.2%	13.1%
Total	17.8%	9.3%	5.5%	12.8%	10.5%	10.1%
Capacity growth (%)						
Auto glass	14%	10%	1%	5%	3%	2%
Construction glass	8%	40%	32%	19%	5%	4%
Float glass	5%	8%	10%	16%	7%	5%
Volume growth (%)						
Auto glass	3%	6%	5%	6%	6%	6%
Construction glass	10%	18%	4%	10%	8%	8%
Float glass	n/a	20%	10%	12%	11%	11%
ASP growth (%)						
Auto glass	3%	3%	0%	0%	0%	0%
Construction glass	24%	0%	0%	1%	1%	1%
Float glass	n/a	-13%	-3%	7%	3%	2%
Cost growth (%)						
Per-unit natural gas cost	n/a	4%	-25%	-25%	4%	4%
Gross margin (%)						
Auto glass	43.3%	41.8%	44.3%	49.0%	48.0%	48.0%
Construction glass	39.9%	35.3%	33.9%	39.0%	39.0%	39.0%
Float glass	19.0%	7.0%	11.1%	22.4%	24.2%	25.2%
Total	31.6%	25.2%	27.3%	34.4%	34.6%	34.8%

Source: Company data, RHB

Figure 30: Xinyi's sensitivity analysis summary

	% Impact on 2017F net profit
Float glass price: 1% increase	1.5%
Natural gas cost: 5% increase	(1.3%)
Float glass segment GPM: 1ppt increase	1.8%

Source: Company data, RHB

Valuations

We have lifted our TP to HKD8.40 on our refreshed earnings forecasts. Our new TP offers a 17% upside from the current price level, and is pegged at 10x FY17F P/E (previously 10x FY16F P/E), which is in line with the stock's 10-year average forward P/E multiple.

By comparison, HK-listed peers are trading at FY17F P/E of 8.8x, whilst China A-shares peers are trading at a substantially higher FY17F P/E of 25.9x.

We have also cross-checked against the stock's implied forward P/BV multiple, which stands at 2.1x or 2.1SD above the 10-year average. We believe the P/BV premium above its long-term average is fair, given that Xinyi is experiencing an earnings up-cycle.

As Xinyi Solar was spun off from Xinyi in Dec 2013, we also highlight the valuations by stripping out Xinyi Solar. Based on the current market capitalisation and valuations of Xinyi and Xinyi Solar, the market is currently implying a FY17F P/E of 8.7x for Xinyi's non-solar business, which is well-below the 10-year average 1-year forward P/E of 13.1x, or 1.1SD below the mean.

Key risks to our call include an abrupt rebound in production capacity in the float glass industry, and a sharp rebound in imported natural gas costs. Key catalysts are a faster-than-expected float glass price rebound and further decline in natural gas costs.

Figure 31: Xinyi's valuations excluding Xinyi Solar

(HKDm)	FY17F	Notes
Recurring net profit	3,293	
Target multiple (x)	10x	
Target price (HKD)	8.40	
Recurring net profit	3,293	
(-) share of interests from Xinyi Solar	(767)	
Core glass profit	2,526	
Current mkt cap of Xinyi Glass	27,757	(a)
Current mkt cap of Xinyi Solar	21,934	(b)
Implied core glass mkt cap	21,923	(c)=(a)-(b)*26.6%
Implied P/E for core glass business	8.7x	

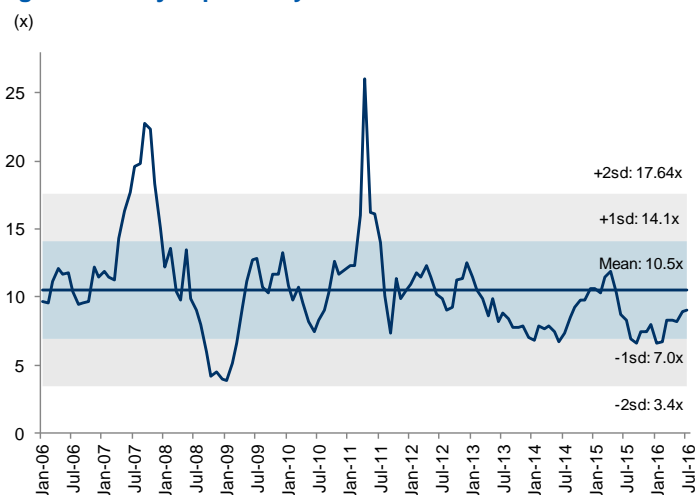
Source: Company data, RHB

Figure 32: Xinyi's TP sensitivity to target P/E and recurring EPS

		Target P/E				
		8x	9x	10x	11x	12x
FY17F Recurring EPS	+25%	8.4	9.4	10.5	11.5	12.6
	+20%	8.1	9.1	10.1	11.1	12.1
	+15%	7.7	8.7	9.7	10.6	11.6
	+10%	7.4	8.3	9.2	10.2	11.1
	+5%	7.1	7.9	8.8	9.7	10.6
	Base case	6.7	7.6	8.4	9.2	10.1
	-5%	6.4	7.2	8	8.8	9.6
	-10%	6	6.8	7.6	8.3	9.1
	-15%	5.7	6.4	7.1	7.9	8.6
	-20%	5.4	6	6.7	7.4	8.1
	-25%	5	5.7	6.3	6.9	7.6

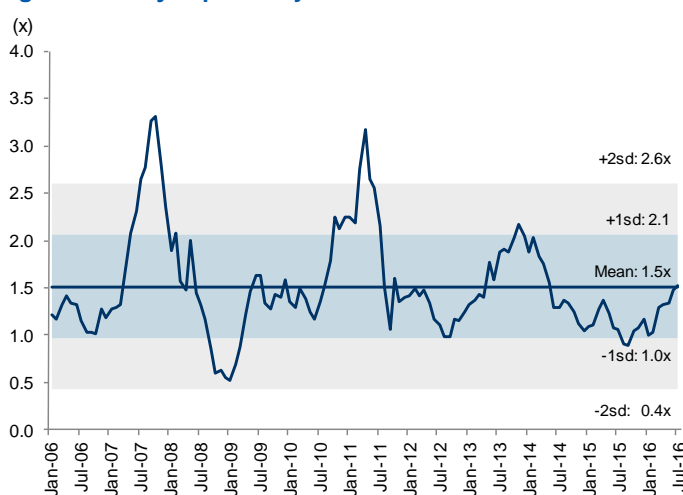
Source: Company data, RHB

Figure 33: Xinyi's past 10-year forward P/E



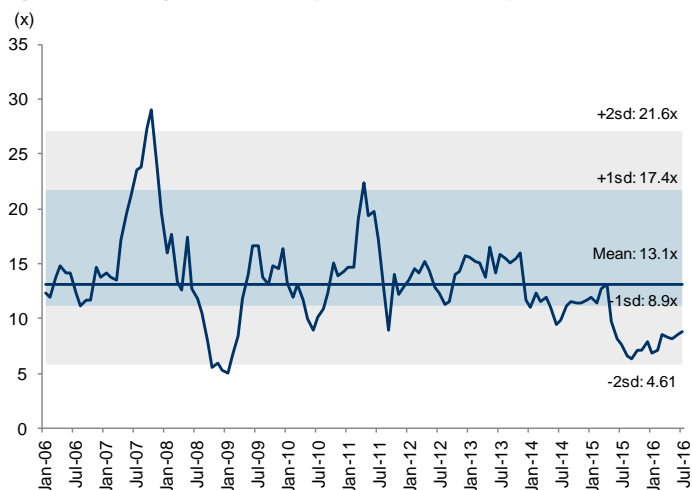
Source: Bloomberg, Company data, RHB

Figure 34: Xinyi's past 10-year forward P/BV



Source: Bloomberg, Company data, RHB

Figure 35: Xinyi's (excl. Xinyi Solar) past 10-year forward P/E



Source: Bloomberg, Company data, RHB

Figure 36: Peer comparison I

Company	Ticker	Price	Mkt cap (USDm)	3-mth avg t/o (USDm)	P/E Hist (x)	P/E FY1 (x)	P/E FY2 (x)	EPS FY1 YoY%	EPS FY2 YoY%	3-Yr EPS Cagr (%)	PEG (x)	Div yld Hist (%)	Div yld FY1 (%)	P/B Hist (x)	P/B FY1 (x)
Xinyi Glass	868 HK	7.21	3,613	11.2	13.4	9.9	8.6	35.0	15.5	28.0	0.5	4.7	4.5	2.1	1.8
HK-listed peers															
Fuyao Glass In-H	3606 HK	20.10	6,165	4.8	15.7	14.5	12.7	8.6	13.9	11.0	1.3	4.4	4.5	2.6	2.4
Xinyi Solar Hlds	968 HK	3.28	2,853	9.2	17.7	11.1	8.6	59.7	28.7	33.5	0.3	5.1	3.8	3.4	2.9
Flat Glass Group	6865 HK	1.79	415	0.4	5.0	5.3	5.0	(6.8)	6.9	7.8	0.7	4.7	N/A	1.1	0.8
Average					12.8	10.3	8.8	20.5	16.5	17.5	0.8	4.7	4.1	2.4	2.0
China A-shares peers															
Fuyao Glass-A	600660 CH	16.19	6,165	25.8	14.7	13.8	12.1	6.5	14.5	10.2	1.4	4.6	4.7	2.5	2.2
Csg Holding Co-A	000012 CH	11.40	2,896	44.8	38.0	28.3	22.5	34.3	25.8	27.2	1.0	2.6	2.6	N/A	2.7
Changzhou Alma-A	002623 CH	34.00	814	15.1	100.0	91.9	54.0	8.8	70.3	42.3	2.2	0.1	N/A	2.5	2.5
Zhuzhou Kibing-A	601636 CH	3.69	1,383	35.9	53.1	14.6	15.2	264.0	(4.0)	60.4	0.2	1.1	N/A	1.7	1.6
Average					51.5	37.1	25.9	78.4	26.7	35.0	1.2	2.1	3.7	2.3	2.3

Note: Share price related data as at 13 Sep 2016.

Source: RHB, Bloomberg

14 September 2016

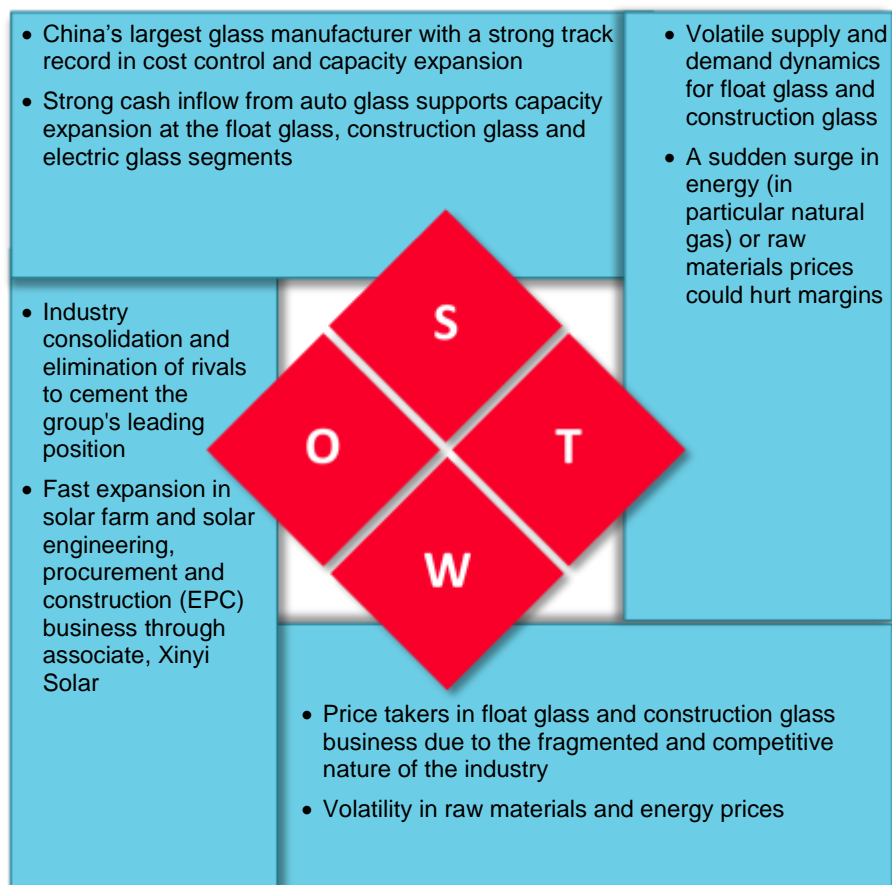
Industrial | Misc. Manufacturer

Figure 37: Peer comparison II

Company	Rev Hist (USDm)	Rev FY1 (USDm)	NP Hist (USDm)	NP FY1 (USDm)	Net gearing Hist (%)	Net gearing FY1 (%)	Unlev beta	Gross margin Hist (%)	Net margin Hist (%)	Net margin FY1 (%)	Net ROE Hist (%)	ROE FY1 (%)	Sh px 1-mth %	Sh px 3-mth %
Xinyi Glass	1,477	1,657	272	366	38.3	33.1	0.7	27.3	18.4	22.1	19.5	21.0	5.3	41.9
HK-listed peers														
Fuyao Glass In-H	2,032	2,375	390	450	0.0	1.8	N.A	41.5	19.2	19.0	20.6	17.4	(2.0)	14.9
Xinyi Solar Hlds	612	846	155	260	10.5	45.6	0.8	36.0	25.4	30.8	30.4	29.9	1.5	13.0
Flat Glass Group	436	455	65	78	5.4	N/A	N.A	29.3	14.9	17.1	20.5	19.1	10.5	19.3
Average					5.3	23.7	0.8	35.6	19.8	22.3	23.9	22.1	3.4	15.7
China A-shares peers														
Fuyao Glass-A	2,032	2,349	390	440	0.0	2.4	0.6	41.5	19.2	18.7	18.3	16.7	(1.1)	18.7
Csg Holding Co-A	1,107	1,364	94	125	64.5	N/A	0.6	21.2	8.5	9.2	N/A	9.8	(4.8)	4.4
Changzhou Alma-A	163	234	8	9	0.0	N/A	1.3	15.7	5.0	3.7	1.7	2.7	2.8	11.5
Zhuzhou Kibing-A	770	1,051	26	95	81.6	N/A	0.6	17.6	3.3	9.1	4.4	11.1	(1.1)	18.6
Average					36.5	2.4	0.7	24.0	9.0	10.2	8.1	10.1	(1.0)	13.3

Source: RHB

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2015-11-05	Buy	5.20	3.87
2015-07-29	Buy	5.50	3.62
2015-03-03	Buy	5.80	4.40
2015-02-25	Neutral	4.60	4.04
2014-07-24	Neutral	5.70	4.48
2014-02-27	Buy	8.95	6.44
2013-12-09	Buy	8.78	6.74
2013-10-16	Buy	9.33	6.47
2013-07-24	Buy	8.19	5.91
2013-03-21	Buy	7.13	4.75

Source: RHB, Bloomberg

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