

China Hongqiao (1378 HK)

Expect higher ASP following China's stimulus

We believe aluminum (Al) is one of the sectors that is highly sensitive to the launch of the series of forceful pro-market policies in China. This, together with the weakness of dollar as a results of the start of rate-cut cycle in the US and a relatively limited new supply of Al, will likely boost the near-term Al price which will serve as key catalyst of Hongqiao. We revise up our 2024E-26E earnings forecast by 9-12%, largely due to higher price assumption of Al and alumina. We estimate every 1% increase in Al price will boost Hongqiao's earnings by 4%. Hongqiao is now trading at mid-cycle valuation (7x 2024E P/E) with an attractive yield of 7%. Our new TP of HK\$19.6 (previously HK\$17.9) is based on an unchanged 9.8x 2024E P/E. Maintain **BUY**.

- Limited new supply...** China's aluminum production growth in Aug slowed to 1.3% YoY (vs 5.3%/2.5% in Jun/Jul), with capacity utilisation rate reaching ~96.7%. Overseas, output increased 1% YoY in Aug (vs 1%/1.5% in Jun/Jul), according to IAI. We see limited room for meaningful supply additions given the maximum capacity of 45mt (~60% of global supply) set by the Chinese government. Meanwhile, capacity growth in oversea markets is limited as well.
- ...near-term demand to be supported by policies.** We estimate China construction (including property and infrastructure) and automobile account for 16% and 14%, respectively, of the global Al demand. We believe Chinese government's policies will help stabilise the expectation of the aforementioned demand. Longer-term, we continue to see light weighting trend of automobiles and fast-growing solar power installation as structural growth driver of Al.
- Favourable price trend.** The latest Shanghai Al price (VAT included) rebounded to RMB20,395/t (+3% since early Sep). In 3Q24, Shanghai Al price averaged at RMB19,600/t, up 4% YoY; for alumina, price momentum remained strong with a 35% YoY increase. We forecast Hongqiao's Al / alumina ASP to increase 5%/34% YoY in 2H24.
- Upcycle to drive valuation.** Over the past decade, Hongqiao traded at an average forward P/E of 6x. The stock normally peaked at 10x (except in 2017) and bottomed out at ~3x during the trough cycles (except 2020 due to the outbreak of COVID-19). Our new TP of HK\$19.6 is based on an unchanged 9.8x 2024E P/E, equivalent to 1.5SD above the historical average of 6x. Our above-average assumption is to reflect the potential industry upcycle.
- Key risks.** (1) A slowdown of global economy that affects the Al and alumina prices; (2) sharp increases in input costs such as bauxite, coal and power.

Earnings Summary

(YE 31 Dec)	FY22A	FY23A	FY24E	FY25E	FY26E
Revenue (RMB mn)	131,699	133,624	147,712	151,359	151,734
YoY growth (%)	15.0	1.5	10.5	2.5	0.2
Adjusted net profit (RMB mn)	8,702.0	11,460.7	17,612.8	19,007.3	19,160.2
EPS (Adjusted) (RMB)	0.94	1.21	1.86	2.01	2.02
Consensus EPS (RMB)	na	na	1.93	1.96	2.06
P/E (x)	12.4	9.6	6.9	5.8	5.7
P/B (x)	1.3	1.2	1.1	1.0	0.9
Yield (%)	4.0	5.0	6.9	8.1	8.2
Net gearing (%)	35.3	34.3	27.4	15.4	6.6

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	HK\$19.60
(Previous TP)	HK\$17.90
Up/Downside	52.9%
Current Price	HK\$12.82

China Materials

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Stock Data

Mkt Cap (HK\$ mn)	121,476.4
Avg 3 mths t/o (HK\$ mn)	347.9
52w High/Low (HK\$)	13.38/5.28
Total Issued Shares (mn)	9475.5

Source: FactSet

Shareholding Structure

Shipping Trust Company	64.2%
(Zhang's family)	
CITIC Group	9.0%

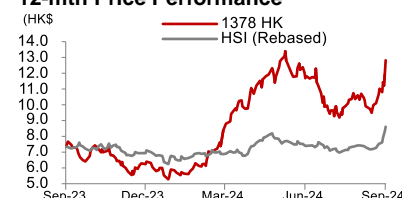
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	21.2%	5.0%
3-mth	9.8%	-5.8%
6-mth	51.4%	20.3%

Source: FactSet

12-mth Price Performance



Source: FactSet

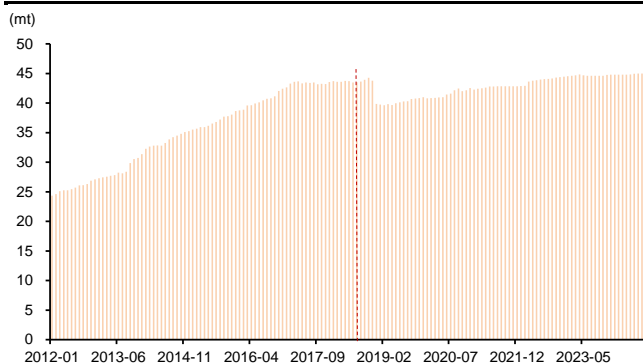
Related report:

China Hongqiao – Net profit in 1H24 +2.7x YoY beat expectations – 19 Aug 2024 ([link](#))

China Hongqiao – A key beneficiary of tight aluminum supply trading at attractive valuation; resume coverage with BUY – 17 Jun 2024 ([link](#))

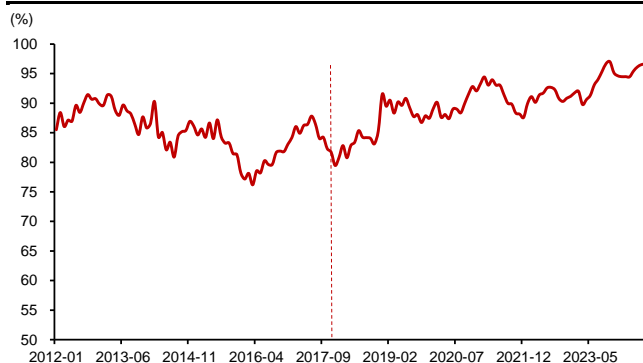
Industry trend

Figure 1: China aluminum annual capacity



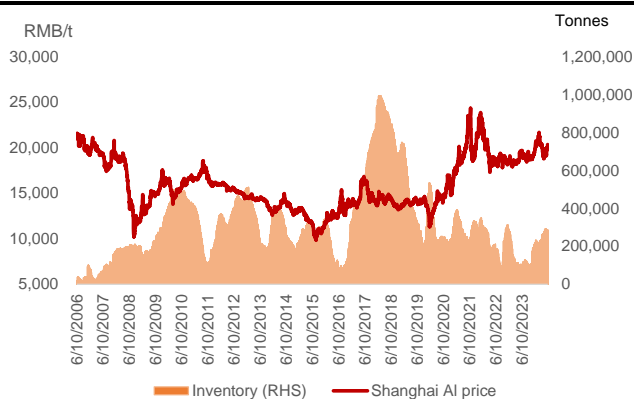
Source: Wind, CMBIGM

Figure 2: China aluminum capacity utilisation rate



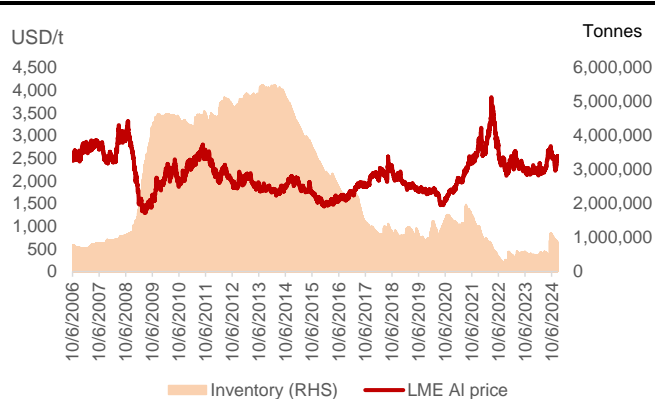
Source: Wind, CMBIGM

Figure 3: Shanghai aluminum price and inventory



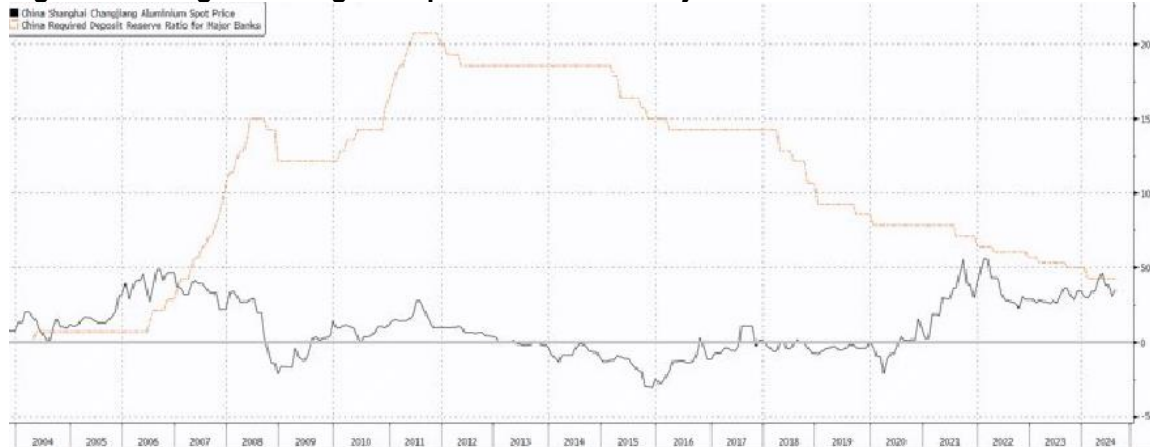
Source: Bloomberg, CMBIGM

Figure 4: LME aluminum price and inventory



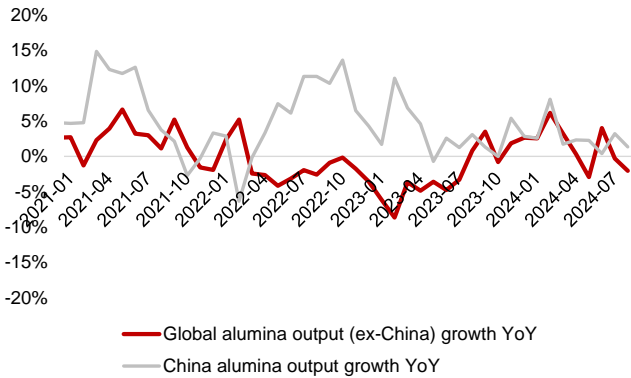
Source: Bloomberg, CMBIGM

Figure 5: Change in Shanghai AI price vs RRR for major banks in China



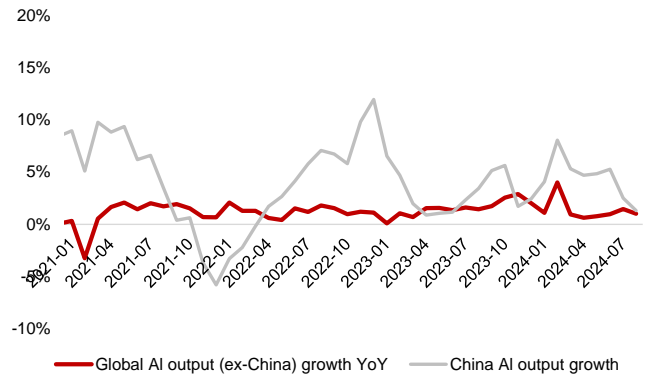
Source: Bloomberg, CMBIGM

Figure 6: Alumina production in China and the rest of the world



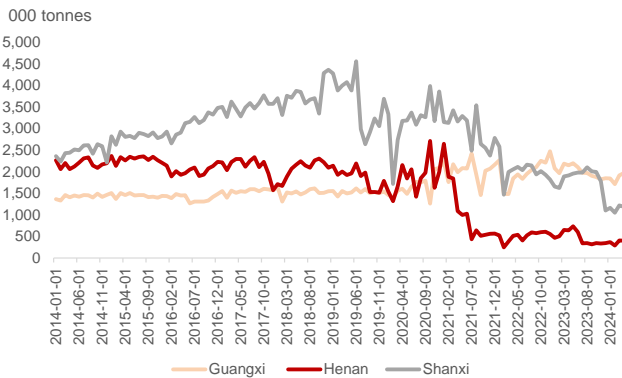
Source: Wind, CMBIGM

Figure 7: AI production in China and the rest of the world



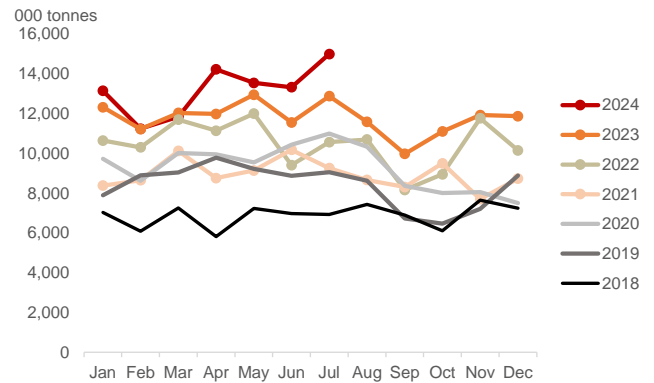
Source: Wind, CMBIGM

Figure 8: Bauxite output in China has been declining since 2019



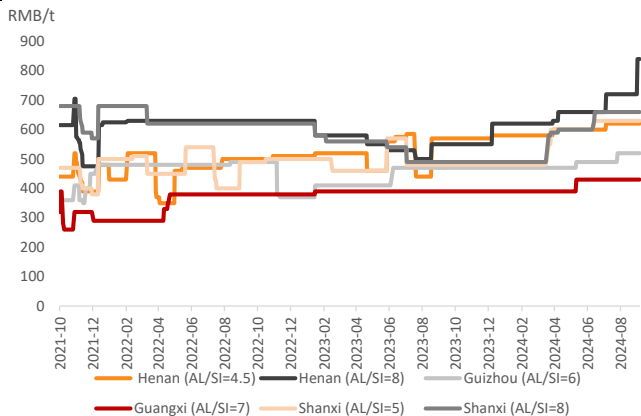
Source: Wind, CMBIGM

Figure 9: Monthly import volume of bauxite on the rise



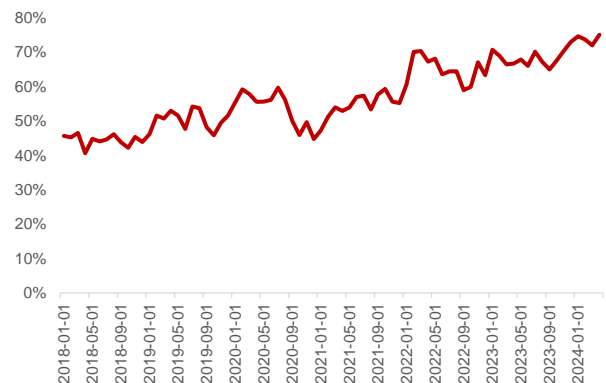
Source: Wind, CMBIGM

Figure 10: Bauxite price in China



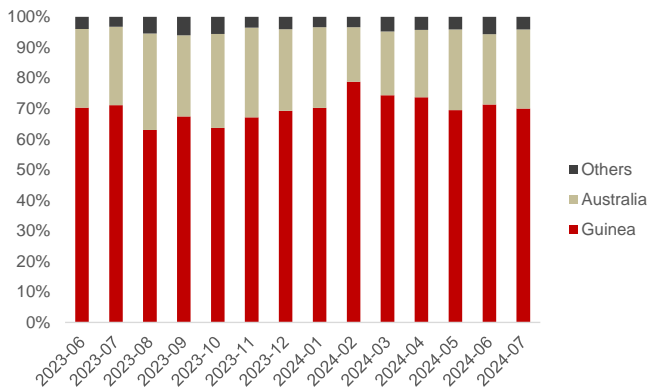
Source: Wind, CMBIGM

Figure 11: Bauxite import dependency marks a decade high



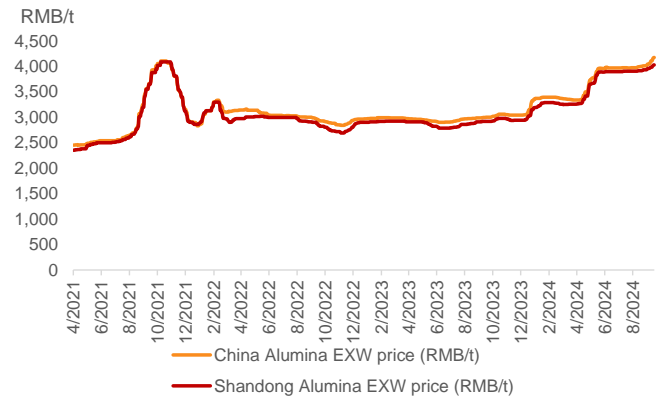
Source: Wind, CMBIGM

Figure 12: Bauxite import breakdown



Source: Wind, CMBIGM

Figure 13: Alumina EXW price in China has moved up since early this year



Source: Wind, CMBIGM

Operating assumptions

Figure 14: Change in earnings forecast

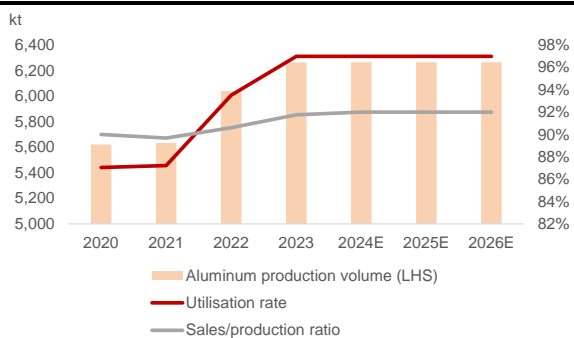
	2024E	Old 2025E	2026E	2024E	New 2025E	2026E	2024E	Change 2025E	2026E
(RMB mn)									
Revenue									
Aluminum alloy products	99,175	101,159	101,159	100,599	102,611	102,611	1%	1%	1%
Alumina	29,575	30,221	30,221	33,608	34,343	34,343	14%	14%	14%
Aluminum fabrication products	12,516	13,317	13,584	12,516	13,317	13,584	0%	0%	0%
Steam	1,064	1,170	1,287	990	1,089	1,197	-7%	-7%	-7%
Total	142,329	145,867	146,251	147,712	151,359	151,734	4%	4%	4%
Revenue growth									
Aluminum alloy products	4.8%	2.0%	0.0%	6.3%	2.0%	0.0%	1.5	(0.0)	0.0
Alumina	11.4%	2.2%	0.0%	26.5%	2.2%	0.0%	15.2	0.0	0.0
Aluminum fabrication products	8.8%	6.4%	2.0%	8.8%	6.4%	2.0%	0.0	0.0	0.0
Steam	15.0%	10.0%	10.0%	7.0%	10.0%	10.0%	(8.0)	0.0	0.0
Average	6.5%	2.5%	0.3%	10.5%	2.5%	0.2%	4.0	(0.0)	(0.0)
Gross profit									
Aluminum alloy products	18,090	18,775	18,692	17,868	18,006	17,923	-1%	-4%	-4%
Alumina	5,839	5,984	5,984	8,770	9,436	9,436	50%	58%	58%
Aluminum fabrication products	2,128	2,397	2,445	2,315	2,397	2,445	9%	0%	0%
Steam	11	12	13	-79	-54	-60	n/a	n/a	n/a
Total	26,067	27,168	27,134	28,874	29,785	29,744	11%	10%	10%
Gross margin								Change in ppt	
Aluminum alloy products	18.2%	18.6%	18.5%	17.8%	17.5%	17.5%	-0.48	-1.01	-1.01
Alumina	19.7%	19.8%	19.8%	26.1%	27.5%	27.5%	6.35	7.67	7.67
Aluminum fabrication products	17.0%	18.0%	18.0%	18.5%	18.0%	18.0%	1.50	0.00	0.00
Steam	1.0%	1.0%	1.0%	-8.0%	-5.0%	-5.0%	-9.00	-6.00	-6.00
Blended gross margin	18.3%	18.6%	18.6%	19.5%	19.7%	19.6%	1.23	1.05	1.05
Net finance expense	-2,788	-2,730	-2,659	-2,792	-2,729	-2,641	0%	0%	-1%
S&D expense ratio	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.0	0.0	0.0
Administrative expense ratio	3.5%	3.5%	3.5%	3.3%	3.3%	3.3%	(0.2)	(0.2)	(0.2)
Other expense ratio	0.5%	0.5%	0.5%	0.6%	0.5%	0.5%	0.1	0.0	0.0
Recurring net profit	16,110	16,944	17,090	17,613	19,007	19,160	9%	12%	12%

Source: Company data, CMBIGM

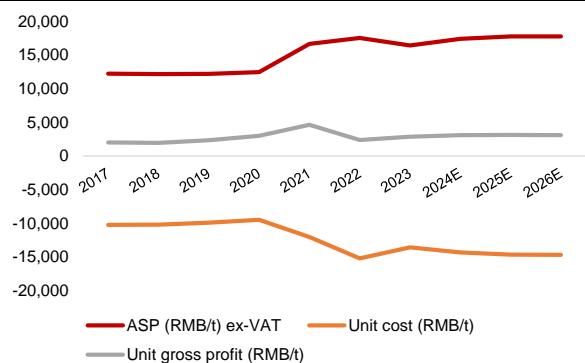
Figure 15: Key operating assumptions

	2021	2022	2023	2024E	2025E	2026E
Sales volume (000 tonnes)						
Aluminum alloy products	5,052	5,473	5,748	5,764	5,764	5,764
Alumina	7,163	8,298	10,374	10,502	10,626	10,626
Aluminum fabrication products	657	609	580	610	636	649
Change YoY						
Aluminum alloy products	-0.2%	8.3%	5.0%	0.3%	0.0%	0.0%
Alumina	6.4%	15.8%	25.0%	1.2%	1.2%	0.0%
Aluminum fabrication products	9.3%	-7.3%	-4.8%	5.1%	4.3%	2.0%
ASP (RMB/t) ex-VAT						
Aluminum alloy products	16,689	17,582	16,465	17,453	17,802	17,802
Alumina	2,369	2,580	2,560	3,200	3,232	3,232
Aluminum fabrication products	19,062	21,843	19,835	20,529	20,940	20,940
Change YoY						
Aluminum alloy products	33.5%	5.4%	-6.4%	6.0%	2.0%	0.0%
Alumina	18.3%	8.9%	-0.8%	25.0%	1.0%	0.0%
Aluminum fabrication products	30.5%	14.6%	-9.2%	3.5%	2.0%	0.0%
Unit cost (RMB/t)						
Aluminum alloy products	-12,035	-15,212	-13,602	-14,353	-14,678	-14,692
Alumina	-1,812	-2,186	-2,275	-2,365	-2,344	-2,344
Aluminum fabrication products	-14,160	-17,930	-17,016	-16,731	-17,171	-17,171
Change YoY						
Aluminum alloy products	26.7%	26.4%	-10.6%	5.5%	2.3%	0.1%
Alumina	8.2%	20.6%	4.1%	4.0%	-0.9%	0.0%
Aluminum fabrication products	24.3%	26.6%	-5.1%	-1.7%	2.6%	0.0%
Unit gross profit (RMB/t)						
Aluminum alloy products	4,654	2,370	2,863	3,100	3,124	3,109
Alumina	556	394	285	835	888	888
Aluminum fabrication products	4,902	3,913	2,819	3,798	3,769	3,769
Change YoY						
Aluminum alloy products	55.1%	-49.1%	20.8%	8.3%	0.8%	-0.5%
Alumina	69.6%	-29.2%	-27.6%	192.7%	6.3%	0.0%
Aluminum fabrication products	52.3%	-20.2%	-28.0%	34.7%	-0.8%	0.0%

Source: Company data, CMBIGM estimates

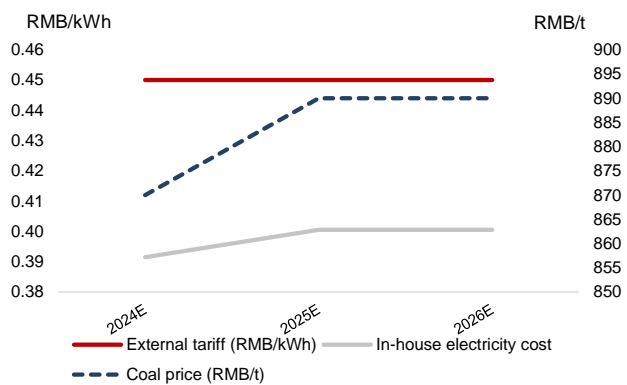
Figure 16: Aluminum production volume, utilisation rates & sales/production ratios

Source: Company data, CMBIGM estimates

Figure 17: Aluminum ASP, unit cost & margin

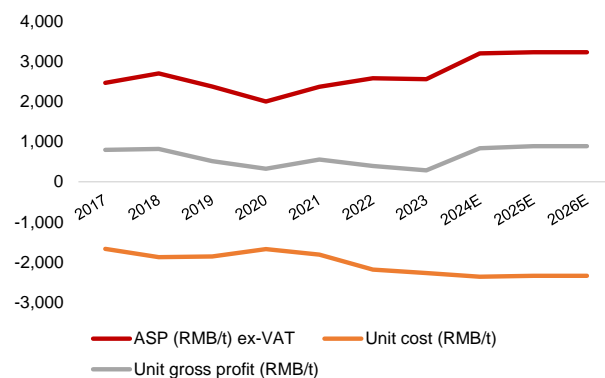
Source: Company data, Wind, CMBIGM

Figure 18: Electricity and coal cost



Source: Company data, CMBIGM estimates

Figure 19: Alumina ASP, unit cost & margin



Source: Company data, Wind, CMBIGM

Earnings sensitivity

Figure 20: Earnings sensitivity (annualized) to 5% change in AI ASP & coal cost

2024E net profit (RMB mn)		AI ASP (RMB/t)					
		15,708	16,580	17,453	18,326	19,198	
Coal cost	783	12,105	15,561	19,017	22,473	25,929	
	826.5	11,403	14,859	18,315	21,771	25,227	
	870	10,701	14,157	17,613	21,069	24,525	
	RMB/t	913.5	9,999	13,455	16,911	20,367	23,823
		957	9,297	12,753	16,209	19,665	23,121

Source: CMBIGM estimates

Figure 21: Earnings sensitivity (annualized) to 5% change in AI ASP & external tariff

2024E net profit (RMB mn)		AI ASP (RMB/t)					
		15,708	16,580	17,453	18,326	19,198	
External tariff	0.41	11,967	15,423	18,879	22,335	25,791	
	0.43	11,334	14,790	18,246	21,702	25,158	
	0.45	10,701	14,157	17,613	21,069	24,525	
	RMB/kWh	0.47	10,068	13,524	16,980	20,436	23,892
		0.50	9,435	12,891	16,347	19,803	23,259

Source: CMBIGM estimates

Figure 22: Earnings sensitivity (annualized) to 5% change in alumina ASP & bauxite cost

2024E net profit (RMB mn)		Alumina ASP (RMB/t)					
		2,880	3,040	3,200	3,360	3,520	
Bauxite	585	18,050	18,719	19,388	20,058	20,727	
	617.5	17,162	17,831	18,501	19,170	19,839	
	650	16,274	16,944	17,613	18,282	18,951	
	RMB/t	682.5	15,387	16,056	16,725	17,394	18,063
		715	14,499	15,168	15,837	16,506	17,176

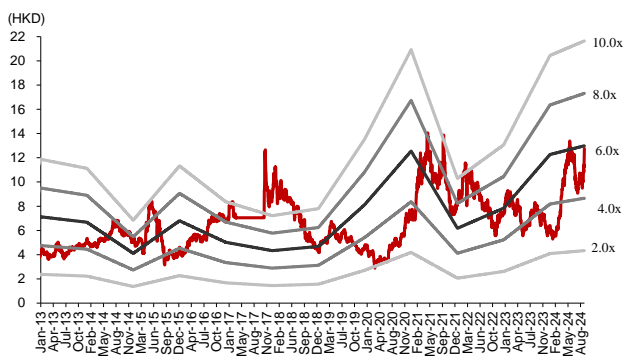
Source: CMBIGM estimates

Valuation

Over the past decade, Hongqiao traded at an average forward P/E of 6x. The stock normally peaked at 10x (except in 2017) and bottomed out at ~3x during the trough cycles (except 2020 due to the outbreak of COVID-19).

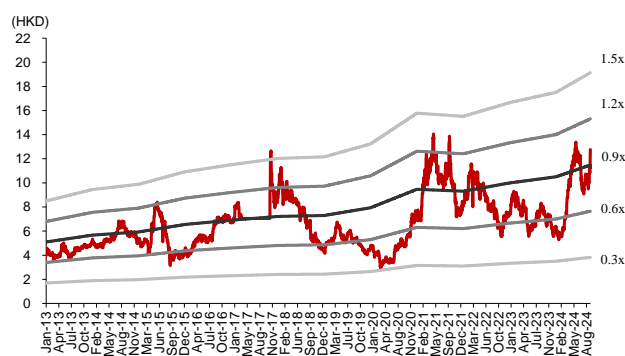
Our new TP of HK\$19.6 is based on an unchanged 9.8x 2024E P/E, equivalent to 1.5SD above the historical average of 6x. Our above-average assumption is to reflect the potential industry upcycle.

Figure 23: Hongqiao's 12M forward P/E band



Source: Bloomberg, company data, CMBIGM estimates

Figure 24: Hongqiao's 12M forward P/B band



Source: Bloomberg, company data, CMBIGM estimates

Financial Summary

INCOME STATEMENT	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Dec (RMB mn)						
Revenue	114,491	131,699	133,624	147,712	151,359	151,734
Cost of goods sold	(84,038)	(113,460)	(112,669)	(118,838)	(121,574)	(121,990)
Gross profit	30,453	18,239	20,955	28,874	29,785	29,744
Selling expense	(526)	(598)	(755)	(739)	(757)	(759)
Admin expense	(5,708)	(5,934)	(4,953)	(4,874)	(4,995)	(5,007)
R&D expense	(1,691)	(329)	(945)	(886)	(757)	(759)
Other income	3,473	3,736	3,405	3,693	3,784	3,793
Other gains/(losses)	(117)	(185)	(49)	(1,615)	(76)	(76)
Share of (losses)/profits of associates/JV	62	503	1,193	1,247	1,430	1,596
EBITDA	32,483	21,836	24,619	33,263	34,483	34,636
Depreciation	6,482	6,721	6,912	7,196	7,422	7,624
EBIT	26,001	15,115	17,707	26,067	27,060	27,013
Interest income	234	193	308	493	562	655
Interest expense	(3,626)	(3,020)	(3,268)	(3,286)	(3,291)	(3,296)
Net Interest income/(expense)	(3,392)	(2,826)	(2,960)	(2,792)	(2,729)	(2,641)
Pre-tax profit	22,554	12,607	15,890	22,908	25,685	25,892
Income tax	(5,705)	(2,798)	(3,393)	(5,612)	(5,137)	(5,178)
Minority interest	(775)	(1,107)	(1,037)	(1,297)	(1,541)	(1,554)
Adjusted net profit	16,073	8,702	11,461	17,613	19,007	19,160
Gross dividends	8,449	4,386	5,465	7,519	8,933	9,005
BALANCE SHEET						
YE 31 Dec (RMB mn)						
Current assets	103,528	87,568	87,395	98,185	105,404	119,421
Cash & equivalents	49,227	27,385	31,721	35,926	46,163	55,507
Account receivables	7,285	4,611	5,489	5,033	5,749	5,060
Inventories	22,705	37,268	33,958	39,623	36,985	41,222
ST bank deposits	1,624	1,720	1,827	1,827	1,827	1,827
Other current assets	22,687	16,585	14,400	15,776	14,680	15,805
Non-current assets	84,892	98,174	112,925	116,492	119,514	121,502
PP&E	63,442	68,061	70,200	72,513	74,100	74,488
Deferred income tax	2,617	2,605	2,990	2,990	2,990	2,990
Investment in JVs & assos	6,065	10,297	11,034	12,282	13,711	15,308
Intangibles	33	34	43	50	55	59
Goodwill	278	278	278	278	278	278
Financial assets at FVTPL	1,059	1,543	13,127	13,127	13,127	13,127
Other non-current assets	11,399	15,356	15,253	15,253	15,253	15,253
Total assets	188,421	185,742	200,320	214,677	224,918	240,923
Current liabilities	63,067	71,373	74,029	78,833	74,874	79,131
Short-term borrowings	29,377	43,434	49,118	49,218	49,318	49,418
Account payables	18,735	14,911	11,648	16,352	12,293	16,450
Tax payable	2,720	618	2,586	2,586	2,586	2,586
Other current liabilities	12,234	12,410	10,677	10,677	10,677	10,677
Non-current liabilities	32,915	18,063	20,035	20,035	20,035	20,035
Long-term borrowings	30,973	16,236	13,792	13,792	13,792	13,792
Other non-current liabilities	1,942	1,827	6,243	6,243	6,243	6,243
Total liabilities	95,982	89,436	94,064	98,867	94,908	99,165
Total shareholders equity	81,308	84,499	92,245	100,500	113,159	123,354
Minority interest	11,131	11,807	14,012	15,309	16,850	18,404
Total equity and liabilities	188,421	185,742	200,320	214,677	224,918	240,923

CASH FLOW	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	22,554	12,607	15,890	22,908	25,685	25,892
Depreciation & amortization	6,482	6,721	6,912	7,196	7,422	7,624
Tax paid	(5,001)	(6,148)	(1,686)	(5,612)	(5,137)	(5,178)
Change in working capital	376	(8,660)	(983)	(1,882)	(1,040)	(517)
Others	20,697	20,693	11,647	23,206	24,440	23,963
Net cash from operations	28,650	7,622	22,402	24,154	28,230	28,866
Investing						
Capital expenditure	(4,178)	(8,798)	(5,662)	(9,500)	(9,000)	(8,000)
Acquisition of subsidiaries/ investments	(2,207)	(3,550)	(3,700)	0	0	0
Others	921	(4,425)	(8,526)	478	547	640
Net cash from investing	(5,463)	(16,773)	(17,889)	(9,022)	(8,453)	(7,360)
Financing						
Dividend paid	(7,184)	(8,226)	(3,786)	(7,742)	(6,348)	(8,966)
Net borrowings	(14,488)	(681)	3,240	100	100	100
Proceeds from share issues	1,972	0	0	0	0	0
Others	305	(3,884)	347	(3,286)	(3,291)	(3,296)
Net cash from financing	(19,396)	(12,790)	(200)	(10,928)	(9,539)	(12,162)
Net change in cash						
Cash at the beginning of the year	45,465	49,227	27,385	31,721	35,926	46,163
Exchange difference	(28)	98	22	0	0	0
Cash at the end of the year	49,227	27,385	31,721	35,926	46,163	55,507

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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