

# China Hongqiao (1378 HK)

## Expect a profit turnaround in 2023E

China Hongqiao announced its FY22 profit warning stating an approximately 40% YoY bottom-line decline, largely in line with market expectations. Two factors have contributed to such earnings drop including (i) rising raw materials and (ii) FX loss arising from the significant depreciation of RMB. However, we believe the profit of the aluminum industry is expected to rebound in 2023E given the marginal cost improvement. Moreover, we expect the valuation of the non-ferrous metal sector to recover as the Fed's interest rate hikes cycle will come to an end in mid-2023E. We maintain our BUY rating and adjust our target price slightly from HK\$13.8 to HK\$13.3.

- **Bottom-line drops by approximately 40% YoY, in line with market expectations.** Even though CHQ has posed excellent results in terms of sales volume, ASP, and sales revenue, raw materials such as coal, anode carbon, and crude oil experienced a significant increase amid global inflation in 2022, which eroded its bottom-line performance. Looking ahead, we believe that the darkest hour has passed. We observe that material costs have passed the peak since late 2022/early 2023E. As a result, we expect an industry-wide margin improvement in 2023E.
- **Production capacity switch was on track with a better electricity cost structure ahead.** CHQ's Wenshan production base phase 1 was fully ramped up in 2022 while phase 2 will be put into production in 2023E. Given such a production switch, CHQ has started to enjoy a better electricity cost structure. Meanwhile, the Company will get more attention from overseas investors as it poses a better ESG profile. In addition, the fully utilized Indonesia production facility of alumina will help CHQ seize the growth potential in Southeast Asia.
- **Maintain BUY rating given upcoming profit turnaround and the attractive valuation.** The global inventory of aluminum is still at a relatively low level for a few weeks, leaving room for replenishment in 2023E. We expect domestic demand for aluminum will be supported by the post-COVID recovery in 2023E. Specifically, we forecast that China's aluminum price will remain at RMB19,000 per ton. We believe that the material cost pressure will be significantly eased globally in 2023E given dim economic forecast overseas, contributing to a margin improvement. Moreover, we further expect that the sector sentiment will recover backed by the end of the Fed rate hike cycle in the mid-2023E. We trimmed FY23-24E EPS by 30-31% to reflect 2H22 results and higher raw material cost. We adjusted our TP to HK\$13.3 (based on rollover 7.5x 2023E P/E in-line with 5-year hist. avg. P/E given earnings recovery) from HK\$13.8. Reiterate BUY rating.

### Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (RMB mn)	86,145	114,491	120,111	124,031	122,603
YoY (%)	2.33	32.91	4.91	3.26	-1.15
Net Income (RMB mn)	10,496	16,073	9,746	13,768	14,298
EPS (RMB)	1.22	1.77	1.06	1.47	1.53
EPS CHG (%)	72.3	45.1	-40.4	39.7	3.8
Consensus EPS (RMB)	1.12	1.60	2.25	2.35	2.44
PE (x)	5.8	4.0	6.7	4.8	4.6
PB (x)	0.80	0.72	0.72	0.65	0.60
Yield (%)	7.58	12.3	7.5	10.5	10.9
ROE (%)	15.2	19.9	11.9	15.0	14.4
Net gearing (%)	39.7	7.7	11.5	0.4	NC

Source: Company data, Bloomberg, CMBIGM estimates

### BUY (Maintain)

Target Price	HK\$13.3
(Previous TP)	HK\$13.8
Up/Downside	+55.5%
Current Price	HK\$8.6

### China Aluminum Sector

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### Stock Data

Mkt Cap (HK\$ mn)	80,353
Avg 3 mths t/o (HK\$ mn)	137.22
52w High/Low (HK\$)	9.4/5.15
Equity share -1378.hk	9,476

Source: Wind

### Shareholding Structure

Hongqiao Holdings	66.62%
CITIC Group	12.71%

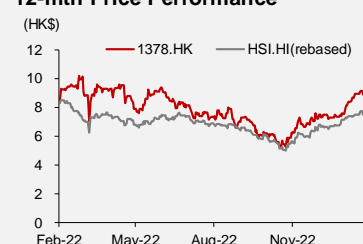
Source: HKEx, Bloomberg

### Share Performance

	Absolute	Relative
1-mth	12.5%	11.2%
3-mth	36.0%	6.4%
6-mth	15.2%	9.7%

Source: Wind

### 12-mth Price Performance



Source: Wind

**Auditor: Shinewing (HK)**

## Financial Summary

### Income statement

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Revenue</b>	<b>86,145</b>	<b>114,491</b>	<b>120,111</b>	<b>124,031</b>	<b>122,603</b>
Aluminum products	63,257	84,313	84,917	88,858	88,113
Aluminum fabrication	8,781	12,524	14,937	15,523	15,789
Alumina	13,487	16,967	19,597	18,989	18,040
Steam	619	687	661	661	661
<b>COGS</b>	<b>(66,789)</b>	<b>(84,038)</b>	<b>(99,344)</b>	<b>(100,02)</b>	<b>(98,659)</b>
Gross profit	19,355	30,453	20,767	24,010	23,944
Other income and gains	2,701	3,707	1,956	3,634	3,735
S&D expenses	(400)	(526)	(577)	(595)	(588)
Admin expenses	(4,052)	(5,708)	(6,006)	(5,705)	(5,272)
Other expenses	(617)	(1,691)	(418)	(425)	(422)
Financial costs	(4,506)	(3,626)	(2,814)	(2,391)	(2,143)
Change in fair value	(291)	(117)	130	130	130
Share profits	515	62	639	666	684
Subsidy disposal loss	-	-	-	-	-
<b>Profit Before Tax</b>	<b>12,704</b>	<b>22,554</b>	<b>13,678</b>	<b>19,323</b>	<b>20,067</b>
Income tax	(2,260)	(5,705)	(3,420)	(4,831)	(5,017)
Less: Minority Interest	(51)	775	513	725	753
<b>Net profit</b>	<b>10,496</b>	<b>16,073</b>	<b>9,746</b>	<b>13,768</b>	<b>14,298</b>

### Cash flow Summary

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Profit before tax</b>	<b>12,704</b>	<b>22,554</b>	<b>13,678</b>	<b>19,323</b>	<b>20,067</b>
Interest payment	4,506	3,626	2,814	2,391	2,143
DD&A	6,904	6,717	7,573	7,833	8,074
Change in WC	(5,372)	(176)	(5,012)	974	(1,976)
Tax adjustments	(2,882)	(5,522)	(3,190)	(5,383)	(5,048)
Others	1,919	2,457	(2,107)	(3,026)	48
<b>Net cash from operation</b>	<b>17,779</b>	<b>28,650</b>	<b>13,756</b>	<b>22,112</b>	<b>23,308</b>
Capex & investments	(5,260)	(4,869)	(6,289)	(6,377)	(6,011)
Others	(1,714)	(425)	-	-	-
<b>Net cash from investment</b>	<b>(6,974)</b>	<b>(5,102)</b>	<b>(6,289)</b>	<b>(6,377)</b>	<b>(6,011)</b>
Equity raised	1,007	1,183	(35)	-	-
Change of Debts	(3,831)	(18,195)	(8,000)	(5,000)	(2,000)
Dividend paid	(3,833)	(7,145)	(7,889)	(4,878)	(6,812)
Interest payment	(4,506)	(3,626)	(2,814)	(2,391)	(2,143)
Others	4,014	5,526	513	725	753
<b>Net cash from financing</b>	<b>(7,150)</b>	<b>(19,758)</b>	<b>(18,225)</b>	<b>(11,544)</b>	<b>(10,203)</b>
Net change in cash	3,655	3,790	(10,758)	4,191	7,094
Cash at beginning	41,857	44,887	48,677	37,919	42,109
FX change	(625)	-	-	-	-
<b>Cash at the end</b>	<b>45,465</b>	<b>49,227</b>	<b>37,919</b>	<b>42,109</b>	<b>49,203</b>
Less: pledged cash	-	-	-	-	-
<b>Cash at balance sheet</b>	<b>45,465</b>	<b>49,227</b>	<b>37,919</b>	<b>42,109</b>	<b>49,203</b>

### Balance sheet

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Non-current Assets</b>	<b>84,097</b>	<b>84,892</b>	<b>82,698</b>	<b>82,032</b>	<b>80,014</b>
Fixed Assets	64,750	63,442	61,364	58,843	55,798
Right-of-use assets	5,647	5,718	6,333	6,733	7,033
Interests in associates	6,681	6,065	6,245	6,911	7,595
Others	7,019	9,667	8,757	9,545	9,588
<b>Current Assets</b>	<b>97,434</b>	<b>103,528</b>	<b>103,547</b>	<b>111,127</b>	<b>118,968</b>
Cash and cash	45,465	49,227	37,919	42,109	49,203
Trade and bills	19,493	19,203	23,422	24,186	23,908
Prepayments	9,126	10,768	13,212	12,403	11,647
Inventories	19,718	22,705	26,823	30,006	32,558
Others	3,631	1,624	2,171	2,423	1,652
<b>Current Liabilities</b>	<b>73,351</b>	<b>61,158</b>	<b>61,309</b>	<b>46,850</b>	<b>45,461</b>
Account Payables	13,377	18,735	19,869	20,004	19,732
Other payables	12,106	11,480	14,902	18,004	17,759
ST borrowings	45,577	26,120	21,686	3,961	3,059
Others	2,291	4,823	4,852	4,881	4,911
<b>Non-Current Liabilities</b>	<b>30,163</b>	<b>31,284</b>	<b>30,151</b>	<b>41,910</b>	<b>40,885</b>
LT borrowings	28,131	29,393	28,346	39,812	38,714
Derivative component of CB	550	241	253	266	279
Deferred income	582	835	877	921	967
Others	900	814	674	911	925
<b>Total net assets</b>	<b>76,802</b>	<b>92,439</b>	<b>94,785</b>	<b>104,399</b>	<b>112,637</b>
<b>Minority Interests</b>	<b>5,606</b>	<b>11,131</b>	<b>11,644</b>	<b>12,369</b>	<b>13,121</b>
<b>Shareholder's equity</b>	<b>71,196</b>	<b>81,308</b>	<b>83,141</b>	<b>92,030</b>	<b>99,516</b>

### Key ratios

YE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Sales mix (%)</b>					
Aluminum products	73.4%	73.6%	70.7%	71.6%	71.9%
Aluminum fabrication	10.2%	10.9%	12.4%	12.5%	12.9%
Alumina	15.7%	14.8%	16.3%	15.3%	14.7%
Steam	0.7%	0.6%	0.5%	0.5%	0.5%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>
<b>P&amp;L ratios (%)</b>					
Gross profit margin	22.5	26.6	17.3	19.4	19.5
Operating margin	20.0	22.9	13.7	17.5	18.1
Net margin	12.2	14.0	8.1	11.1	11.7
Effective tax rate	17.8	25.3	25.0	25.0	25.0
<b>Balance sheet ratios</b>					
Current ratio (x)	1.33	1.64	1.67	2.32	2.58
Inventory turnover days	114.5	100.7	91.0	103.7	115.7
Creditor's turnover	86.7	61.7	64.8	70.1	71.6
Debtors turnover days	87.0	76.2	70.9	72.8	73.5
Liabilities/Assets (%)	57.7	50.9	49.4	46.5	43.8
Net gearing ratio (%)	39.7	7.7	11.5	0.44	NC
<b>Returns (%)</b>					
ROE	14.7	19.8	11.7	15.0	14.4
ROA	5.8	8.5	5.3	7.2	7.2
<b>Per share</b>					
EPS (RMB)	1.22	1.77	1.06	1.47	1.53
DPS (HK\$)	0.65	1.05	0.64	0.90	0.93
BVPS (RMB)	8.02	8.91	8.91	9.86	10.66

Source: Company data, CMBIGM estimates

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