

May 27, 2015

Aluminum Corp. of China Ltd.

Takeaways from China Summit

Industry View

Cautious

Stock Rating

Overweight

Quick Comment: During our China Summit meetings, Chalco management shed light on its cost-cutting efforts through increase efficiency, reduce power cost and increase bauxite sufficiency.

Cost cut: Management reiterated its target to reduce alumina and aluminum production costs by 5% and 3% respectively in 2015. The cost reduction will be achieved through: 1) increase in bauxite sufficiency ratio to 70% by end of 2015 and further to 80% by end of 2016; and 2) reduction in power cost by increasing direct power purchase percentage to 68% from the current 50-51%.

Industry demand: Management is confident in aluminum demand, expecting 9-10%YoY growth in 2015-2016. Positives include: 1) property support policies from government; 2) lightweight trend in automobiles and transportation sectors; 3) construction of ultra-high-voltage power networks and upgrade of rural grid; and 4) substitution demand to replace copper and steel.

Industry supply: Management estimates total capacity at 35mnt at the end of 2014, vs. 28mnt demand. It sees 3mnt capacity being added in 2015 (2014: 3mnt), but future additions will be limited, as government no longer approves new projects. Management expects a 200-300kt/year reduction in capacity in the next few years.

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Aluminum Corp. of China Ltd. (2600.HK, 2600 HK)

China Materials / China

Stock Rating**Overweight****Industry View****Cautious**

Shr price, close (May 27, 2015)

HK\$4.97

52-Week Range

HK\$5.62-2.74

Sh out, dil, curr (mn)

3,944

Mkt cap, curr (mn)

Rmb112,834

EV, curr (mn)

Rmb190,011

Avg daily trading value (mn)

HK\$85

Fiscal Year Ending	12/14	12/15e	12/16e	12/17e
ModelWare EPS (Rmb)	(1.20)	0.01	0.20	0.22
Consensus EPS (Rmb)\$	(0.49)	(0.21)	0.05	0.19
Revenue, net (Rmb mn)	141,772	153,887	159,478	161,648
EBITDA (Rmb mn)	3,487	12,384	17,555	18,001
ModelWare net inc (Rmb mn)	(16,217)	142	2,897	3,149
P/E	NM	391.8	19.7	18.1
P/BV	1.4	1.7	1.6	1.5
ROE (%)	(36.6)	0.5	8.7	8.7
EV/EBITDA	42.6	15.5	10.9	10.3
Leverage (EOP) (%)	275.5	225.9	204.0	176.4

Unless otherwise noted, all metrics are based on Morgan Stanley ModelWare framework
 \$ = Consensus data is provided by Thomson Reuters Estimates
 e = Morgan Stanley Research estimates

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Detailed takeaways

Industry

Industry capacity

- Aluminum capacity at 35mnt at the end of 2014, demand at 28mnt.
- 2015 will see addition of 3mnt in capacity.
- Government has already started to curb over-capacity; there will be no approval of new projects going forward.
- Capacity will be reduced by 200-300kt/year.
- The market-driven capacity closures are temporary. In 2014, there were 2.4-2.5mnt shutdowns and 3mnt additions.

Demand

- Demand for aluminum is not a concern; management expects it to grow at 9-10%YoY in 2015-16.
- Expects property demand to recover, due to government support. Even during property- controlling periods, aluminum still has around 10% demand growth.
- Sees more demand to come from auto and transportation, due to the lightweight trend.
- Construction of ultra-high-voltage power network and upgrade of rural grid to support demand from power sector.
- A substitute for copper, due to cost advantage; a substitute for steel, due to lightweight trend in automobiles.

Company

Bauxite sufficiency:

- Target to achieve 70% self-sufficient rate at 2015 and 80% at end of 2016.
- Guizhou Maochang mine has 2.8mnt capacity.
- Self-produced bauxite cost is Rmb245/t, cheaper than imported cost at Rmb500/t and domestic purchase at Rmb340/t.
- If import ban is lifted in Indonesia, bauxite FOB is expected to reduce from the current US\$60/t to US\$50/t.
- Capex for bauxite mine is Rmb2bn for 2.8mnt/year capacity.

Power cost:

- 3Q14: Rmb0.399/kwh, 1Q15: Rmb0.387/kwh, both incl. of VAT. Captive power cost at Rmb0.32/kwh
- Captive power now account for 32%.
- Direct power purchase increased to 50-51% now from 45% last year. Goal is to achieve 68% direct power purchase by end of 2015.
- Direct power price is negotiated with IPP on volume and price. Cost is Rmb0.05-0.06/kwh lower than grid power price.
- Power account for 40% of aluminum cost.

Cost reduction:

- 2015 target: -5% for alumina and -3% for aluminum.
- Aluminum production cost is reduced to Rmb11,450/t, through: 1) reduced per ton power consumption from 13,500kwh/t to 13,300kwh/t now, vs. country standard of 13,700kwh/t; and 2) reduced power price.
- Industry peers usually have higher captive power %, so they are less sensitive to lower grid price.

Labor cut:

- Headcount reduced to 75k at end of 2014; 15k staff cut in 2014, through: 1) discontinuation of contracts, and 2) early retirement.
- Chalco's parent is a central-gov't-owned SOE; labor cut decision is taking consideration of this SOE status. No social impact.

Non-core asset sales: Sales were almost completed in 2014; expects no major sales in 2015 or going forward.

Production volume:

- 2014 production: alumina: 12.02mnt out of 14.71mnt capacity, aluminum: 3.38mnt out of 3.84mnt capacity.
- 2014 implemented the flexible production scheme. Chalco has no plan to close capacity this year.
- 2015 production guidance is 13.2mnt alumina and 3.6mnt aluminum.

Cash flow and capex:

- Working capital management improvement in 2014: 1) Accounts receivable: receive payment upfront before shipment; and 2) Inventory: try to destock.
- Cash flow target in 2015: Rmb6.5bn operating net cash flow, vs. Rmb13.8bn in 2014.
- 2015 capex guidance at Rmb9.8bn (vs. Rmb8.7bn in 2014), management will control capex. The capex will be funded by: 1) working capital, and 2) A-share placement; no plan to increase debt.

A-share placement: No more than Rmb8bn, within which Rmb6bn to be used for two alumina plants, and the rest for working capital.

Finance cost averaged at 5.6% vsm 5.8% in 2014. The company has Rmb70bn RMB bank loans; will benefit from rate cuts.

SOE reform:

- Mixed ownership reform in Guizhou alumina plant.
- Incentive reform for top management in 13 subsidiaries.

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Aluminum Corp. of China Ltd. (2600.HK) - As of 5/26/15 in HKD
Industry : China Materials



Stock Rating History: 5/1/12 : U/NR; 1/13/14 : U/A; 10/8/14 : E/A; 12/16/14 : O/A; 4/17/15 : O/C

Price Target History: 1/17/12 : 3.1; 8/27/12 : 2.6; 10/4/12 : 2.5; 4/23/13 : 2.3; 3/24/14 : 2.4; 10/8/14 : 3.4; 12/16/14 : 4.5

Source: Morgan Stanley Research Date Format : MM/DD/YY Price Target --- No Price Target Assigned (NA)
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 Stock Ratings: Overweight (O) Equal-weight (E) Underweight (U) Not-Rated (NR) No Rating Available (NA)
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Aluminum Corp. of China Ltd. (601600.SS) - As of 5/26/15 in CNY
Industry : China Materials



Stock Rating History: 1/13/14 : NA/A; 10/8/14 : U/A; 12/16/14 : E/A; 4/17/15 : U/C

Price Target History: 10/8/14 : 3.37; 12/16/14 : 4.7

Source: Morgan Stanley Research Date Format : MM/DD/YY Price Target --- No Price Target Assigned (NA)
 Stock Price (Not Covered by Current Analyst) --- Stock Price (Covered by Current Analyst) ---
 Stock and Industry Ratings (abbreviations below) appear as ♦ Stock Rating/Industry View
 Stock Ratings: Overweight (O) Equal-weight (E) Underweight (U) Not-Rated (NR) No Rating Available (NA)
 Industry View: Attractive (A) In-line (I) Cautious (C) No Rating (NR)

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INDUSTRY COVERAGE: China Materials

COMPANY (TICKER)	RATING (AS OF)	PRICE* (05/27/2015)
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Aluminum Corp. of China Ltd. (2600.HK)	O (12/16/2014)	HK\$4.89
Angang Steel Company Limited (0347.HK)	O (11/28/2013)	HK\$6.71
Angang Steel Company Limited (000898.SZ)	O (08/30/2014)	Rmb7.81
Baoshan Iron & Steel (600019.SS)	E (04/17/2015)	Rmb9.47
Chinalco Mining Corp International (3668.HK)	E (06/18/2014)	HK\$1.14
G-Resources (1051.HK)	E (10/07/2013)	HK\$0.29
Jiangxi Copper (0358.HK)	E (10/08/2014)	HK\$15.70
Jiangxi Copper (600362.SS)	U (04/17/2015)	Rmb25.69
Jilin Jien Nickel Industry (600432.SS)	E (12/19/2014)	Rmb20.77
Lee & Man Paper Manufacturing (2314.HK)	U (07/01/2014)	HK\$5.13
Maanshan Iron & Steel (600808.SS)	U (04/17/2015)	Rmb6.48
Maanshan Iron & Steel (0323.HK)	E (04/17/2015)	HK\$3.13
Nine Dragons Paper (2689.HK)	U (07/01/2014)	HK\$6.75
Zhaojin Mining Industry (1818.HK)	O (01/20/2015)	HK\$5.86
Zijin Mining Group (2899.HK)	++	HK\$3.48
Zijin Mining Group (601899.SS)	NA (05/26/2015)	Rmb5.76

Stock Ratings are subject to change. Please see latest research for each company.

* Historical prices are not split adjusted.