



Company Report: China Unicom (00762 HK)

公司报告: 中国联通 (00762 HK)

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Sluggish Subscriber Growth to be Improved in FY15, "Buy"

低迷的用户增长可在15财年中改善, "买入"

Rating:

Buy

Maintained

评级:

买入 (维持)

6-18m TP 目标价:

HK\$14.10

Revised from 原目标价:

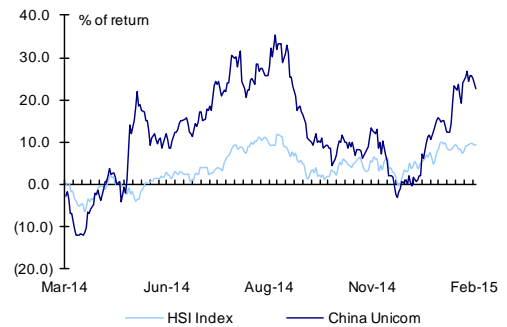
HK\$14.40

Share price 股价:

HK\$12.540

Stock performance

股价表现



Change in Share Price 股价变动	1 M 1 个月	3 M 3 个月	1 Y 1 年
Abs. % 绝对变动 %	(2.1)	5.9	16.9
Rel. % to HS index 相对恒指变动 %	(1.2)	3.3	8.9
Avg. share price(HK\$) 平均股价 (港元)	12.6	11.6	11.7

Source: Bloomberg, Guotai Junan International.

- **4Q14 results were lower than expectations**, due to lower than expected mobile ARPU and sluggish subscriber growth.
- **Revise down FY15-16 mobile revenue by 10.0%/16.0%, respectively**, due to the revision of mobile subscriber and ARPU estimations. The Company's FY15 subscriber addition guidance of 18 million was lower than expected due to intensifying market competition.
- **FY15-17 net profit margin is expected to be 4.2%/4.6%/4.8%, respectively**, due to the reduction of handset subsidies and benefit from the formation of Tower Company in FY15.
- **Maintain the investment rating of "Buy" and cut the TP from HK\$14.40 to HK\$14.10**. Due to the revisions of subscriber and ARPU estimations, FY15-16 EPS is revised down by 2.5%/5.0%, respectively. The new TP represents 21.8x FY15 PER, 19.8 FY16 PER, 18.4x FY17 PER and 1.1x FY15 PBR. We maintain the Company's investment rating of "Buy" due to the grant of formal FDD 4G operating license and improvement in profit margin.
- **14 财年第 4 季度业绩差于预期**, 是由于低于预期的移动 ARPU 及较弱的用户增长。
- **分别下调 15-16 财年移动收入预测 10.0%/16.0%**, 是由于移动用户和 ARPU 预测的调整。公司的 15 财年的 18 百万用户增长指引低于预期, 因市场竞争加剧。
- **预期 15-17 财年的纯利率为 4.2%/4.6%/4.8%**, 是由减少手机补贴及受益于 15 财年塔公司的成立。
- **维持公司的投资评级为 "买入" 及目标价从 14.40 港元下调至 14.10 港元**。基于调整用户数及 ARPU 值预测, 我们分别下调 15-16 财年每股盈利预测 2.5%/5.0%。新目标价相当于 21.8 倍 15 年市盈率、19.8 倍 16 年市盈率、18.4 倍 17 年市盈率及 1.1 倍 15 年市净率。我们维持公司的投资评级为 "买入", 基于正式授予 FDD 的 4G 运营牌照, 及利润率的提升。

Year End 年结 12/31	Turnover 收入 (RMB m)	Net Profit 股东净利 (RMB m)	EPS 每股净利 (RMB)	EPS 每股净利变动 (Δ %)	PER 市盈率 (x)	BPS 每股净资产 (RMB)	PBR 市净率 (x)	DPS 每股股息 (RMB)	Yield 股息率 (%)	ROE 净资产收益率 (%)
2013A	295,039	10,409	0.440	46.1	22.3	9.253	1.1	0.129	1.3	4.9
2014A	284,681	12,055	0.505	14.9	19.8	9.540	1.1	0.161	1.6	5.4
2015F	290,451	12,277	0.512	1.2	19.4	9.967	1.0	0.161	1.6	5.3
2016F	296,197	13,588	0.563	10.0	17.6	10.904	0.9	0.177	1.8	5.4
2017F	307,875	14,674	0.605	7.4	16.4	11.965	0.8	0.190	1.9	5.3

Shares in issue (m) 总股数 (m)	23,947.0	Major shareholder 大股东	China Unicom Group 75.6%
Market cap. (HK\$ m) 市值 (HK\$ m)	300,295.4	Free float (%) 自由流通比率 (%)	23.5
3 month average vol. 3 个月平均成交股数 ('000)	43,947.8	FY15 Net gearing (%) FY15 净负债/股东资金 (%)	51.9
52 Weeks high/low (HK\$) 52 周高低	14.140/9.170	FY15 Est. NAV (HK\$) FY15 每股估值 (港元)	14.9

Source: the Company, Guotai Junan International.

4Q14 Results Review

4Q14 results were lower than expectations, which was due to lower than expected mobile ARPU with and sluggish mobile subscriber growth.

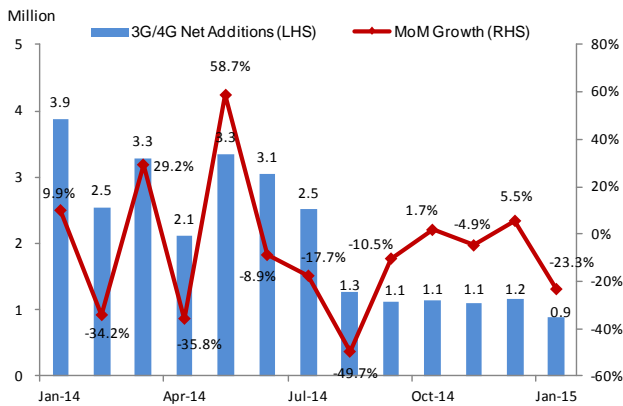
Table-1: China Unicom's 4Q14 Income Statement

RMB (Billion)	4Q14	4Q13	3Q14	QoQ	YoY	Comments
Total Revenues	69.3	74.9	65.8	5.3%	(7.5%)	Affected by the launch of VAT and slower subscriber growth
Interconnection Charges	(3.5)	(5.2)	(3.6)	(2.8%)	(32.7%)	
Depreciation & Amortization	(18.7)	(17.1)	(18.3)	2.2%	9.4%	
Networks, Operations & Supports	(10.1)	(9.0)	(9.7)	4.1%	12.2%	
Employee Benefit	(8.8)	(8.9)	(8.9)	(1.1%)	(1.1%)	
Costs of Telecom Products Sold	(11.2)	(15.2)	(6.6)	69.7%	(26.3%)	
Other Operating Expenses	(15.0)	(16.6)	(12.7)	18.1%	(9.6%)	
Finance Costs	(0.8)	(0.7)	29.8	(102.7%)	14.3%	
Interest Income	0.1	0.0	2.9	N.A.	N.A.	
Other Income - net	0.6	0.4	0.6	0.0%	50.0%	
Net Profit	1.5	2.0	3.9	(61.5%)	(25.0%)	
EBITDA	20.8	20.0	24.3	(14.4%)	4.0%	YoY improvement thanks to the reduction of handset subsidies
EPS (RMB)	0.1	0.1	0.2	(50.0%)	0.0%	
EBITDA Margin (%)	30.0	26.7	37.0	(7.0ppt)	(3.3ppt)	
Net Profit Margin (%)	2.2	2.7	5.9	(3.7ppt)	(0.5ppt)	

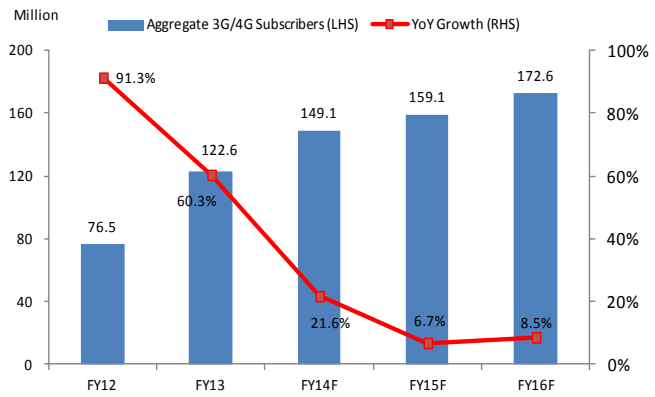
Source: the Company.

MIIT granted the formal FDD-LTE 4G operating license in Feb. 2015. The grant of formal FDD-LTE 4G operating license from MIIT in Feb 2015 was earlier than expected. We expect China Unicom can improve its subscriber growth with the earlier launch of related 4G services. China Mobile (00941 HK) had more than 90% of the 4G user market share and we think the launch of 4G services could shorten their discrepancy. China Unicom had 424k 2G base stations and 565k 3G/4G base stations (with 100k 4G) by the end of 2014. The Company plans to build 35.6k base stations in FY15, which could significant improve the 4G network coverage to support user growth.

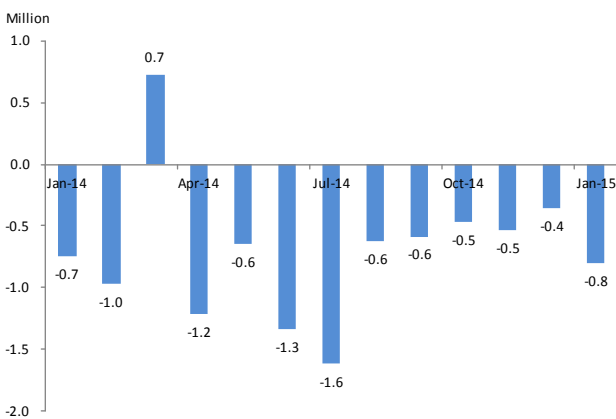
Revise down FY15-16 mobile revenue by 10.0%/16.0%, respectively. 3G/4G subscriber net additions in FY14 were 26.5 million, down 42.6% yoy, lower than expected. The slowing down of user growth was related to the reduction of handset subsidies and stronger market competition. FY14 handset subsidies were RMB4.6 billion, down 40.4% yoy, lower than expected. 2G subscriber net losses in FY14 were 8.4 million, up 87.6% yoy. In FY14, mobile ARPU was RMB44.1, down 8.5% yoy; 2G ARPU was RMB28.0, down 11.9% yoy; 3G/4G ARPU was RMB63.6, down 15.3% yoy. Mobile broadband service accounted for 68.2% in FY14, up 8.8ppt yoy, and we expect stronger data business would impose a positive impact thanks to lower VAT tax rate. China Unicom is going to open its 4G services to all mobile subscribers including 2G and 3G subscribers in FY15 which could encourage low end users to use the 4G service. Due to the expansion of 4G base stations and the grant of formal FDD 4G operating license, we expect FY15-17 3G/4G subscriber net additions to be 10.0 million/13.5 million/16.00 million, respectively. We revise down FY15-16 3G/4G subscriber net addition estimations by 75.0%/74.5%, respectively. We expect FY15-17 3G/4G ARPU to be RMB61.5/64.0/RMB67.0, respectively. FY15-16 mobile revenue is revised down by 10.0%/16.0%, respectively.

Figure-1: China Unicom's Monthly 3G/4G Subscriber Net Additions and MoM Growth


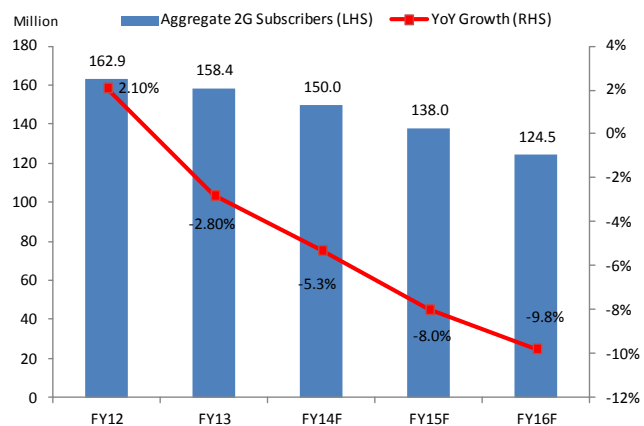
Source: the Company.

Figure-2: China Unicom's Aggregate 3G/4G Subscriber Estimations and YoY Growth


Source: the Company, Guotai Junan International.

Figure-3: China Unicom's Monthly 2G Net Addition Subscribers


Source: the Company.

Figure-4: China Unicom's Aggregate 2G Subscribers Estimations and YoY Growth


Source: the Company, Guotai Junan International.

Benefit from the formation of Tower Company and profit margin improvement. China Unicom is expected to benefit from the formation of Tower Company in FY15 with the sharing of infrastructure resources from other telecom operators. FY14 net profit was 4.2%, up 0.7ppt, thanks to the reduction of sales and marketing expenses. We expect the Company would stabilize its net profit margin in FY15 and make improvement in FY16-17 due to the benefit from the formation of Tower Company and reduction of handset subsidies. FY15-17 net profit margin is expected to be 4.2%/4.6%/4.8%, respectively.

Profit Forecast Revisions:

FY15-16 net profit is revised down by 2.5%/5.5%, respectively. Due to the revision of mobile subscriber and ARPU estimations, we revise down FY15-16 total revenue by 9.1%/14.5%, respectively. FY15-16 net profit is revised down by 2.5%/5.0%, respectively.

Table-2: Operational Metrics Revisions

(Million)	OLD			NEW			CHANGE		
	2015F	2016F	2017F	2015F	2016F	2017F	2015F	2016F	2017F
Net Addition Subscribers									
-3G/4G	40.0	53.0	N.A.	10.0	13.5	16.0	(75.0%)	(74.5%)	N.A.
-2G	(12.0)	(13.5)	N.A.	(12.0)	(13.5)	(16.0)	0.0%	0.0%	N.A.
-Local Access Line	(5.5)	(4.5)	N.A.	(6.7)	(7.5)	(8.2)	21.8%	66.7%	N.A.
-Fixed Line Broadband	4.0	3.8	N.A.	4.0	3.8	3.6	0.0%	0.0%	N.A.
ARPU (RMB)									
-3G/4G	64.4	61.0	N.A.	61.5	64.0	67.0	(4.5%)	4.9%	N.A.
-2G	28.7	27.2	N.A.	27.0	25.5	24.4	(5.9%)	(6.3%)	N.A.
-Fixed Line Broadband	59.7	59.0	N.A.	63.0	63.8	64.7	5.5%	8.1%	N.A.
-Local Access Line	18.9	18.7	N.A.	17.0	15.8	15.0	(10.1%)	(15.5%)	N.A.

Source: Guotai Junan International.

Table-3: Financial Estimation Revisions

RMB (Million)	OLD			NEW			CHANGE		
	2015F	2016F	2017F	2015F	2016F	2017F	2015F	2016F	2017F
Total Operating Revenue	320,710	347,598	N.A.	291,616	297,342	309,040	(9.1%)	(14.5%)	N.A.
-Mobile Revenue	99,327	107,563	N.A.	89,394	90,353	91,348	(10.0%)	(16.0%)	N.A.
-Fixed Line Revenue	1,445	1,510	N.A.	1,344	1,382	1,446	(7.0%)	(8.5%)	N.A.
-Unallocated Revenue	1,344	1,382	N.A.	1,344	1,382	1,446	0.0%	0.0%	N.A.
-Sales of Telecom Products	40,494	38,068	N.A.	40,494	38,068	36,929	0.0%	0.0%	N.A.
Net Profit	13,377	15,098	N.A.	13,043	14,343	15,437	(2.5%)	(5.0%)	N.A.
EPS (RMB)	0.558	0.625	N.A.	0.544	0.594	0.636	(2.5%)	(5.0%)	N.A.

Source: Guotai Junan International.

Valuation:

Maintain the investment rating of “Buy” and cut the TP from HK\$14.40 to HK\$14.10. We maintain the Company’s investment rating of “Buy” with the grant of formal FDD-LTE 4G operating license and benefit from the formation of Tower Company in FY15. The new TP represents 21.8x FY15 PER, 19.8x FY16 PER, 18.4x FY17 PER and 1.1x FY15 PBR.

Table-4: Peer Comparisons:

Company	Ticker	Currency	Price	PER			PB			ROE(%)	D/Y (%)	EV/EBITDA	ROA(%)
				15F	16F	17F	15F	16F	17F	15F	15F	15F	15F
HK Listed Companies													
China Unicom Hong Kong Ltd	762 HK	HKD	12.540	16.3	13.8	13.8	1.0	1.0	0.9	6.3	2.2	3.6	2.9
China Mobile Ltd	941 HK	HKD	102.800	14.8	14.2	14.2	1.9	1.8	1.7	12.4	2.9	5.5	8.5
China Telecom Corp Ltd-H	728 HK	HKD	4.780	15.3	13.5	13.5	1.1	1.0	1.0	6.7	2.2	4.0	3.6
Pccw Ltd	8 HK	HKD	4.930	14.7	12.8	12.8	3.6	3.3	3.0	23.2	5.0	5.5	4.3
Hong Kong Telecom	6823 HK	HKD	10.300	19.5	17.9	17.9	2.1	2.0	2.0	10.3	5.3	8.8	4.7
Smartone Telecom	315 HK	HKD	15.240	19.0	17.8	17.8	4.7	4.2	3.8	23.8	3.4	5.4	8.7
Hutchison Telecomm Hong Kong	215 HK	HKD	3.810	19.3	17.5	17.5	1.6	1.6	1.5	8.2	3.8	7.7	4.5
Simple Average				17.0	15.4	15.4	2.3	2.1	2.0	13.0	3.5	5.8	5.3
Weighted Average				15.2	14.2	14.2	1.8	1.7	1.6	11.2	2.8	5.2	7.1
US Listed Companies													
At&T Inc	T US	USD	34.000	13.5	13.2	13.2	2.1	2.0	1.9	14.6	5.5	6.2	5.3
Verizon Communications Inc	VZ US	USD	48.920	13.6	12.9	12.9	16.7	14.7	10.0	n.a.	4.5	6.9	7.9
Centurylink Inc	CTL US	USD	36.130	14.8	15.2	15.2	1.4	1.3	1.3	8.0	5.7	6.0	3.2
Simple Average				14.0	13.8	13.8	6.7	6.0	4.4	11.3	5.2	6.4	5.4
Weighted Average				13.6	13.1	13.1	9.5	8.4	6.0	13.9	5.0	6.6	6.5
JP Listed Companies													
Nippon Telegraph & Telephone	9432 JP	JPY	7600.000	15.4	13.6	13.6	1.0	0.9	0.9	6.2	2.4	4.6	2.7
Kddi Corp	9433 JP	JPY	8034.000	15.5	13.7	13.7	2.5	2.3	2.0	15.5	2.1	6.4	9.5
Ntt Docomo Inc	9437 JP	JPY	2235.000	20.5	18.6	18.6	1.6	1.6	1.5	7.8	3.0	7.0	6.4
Softbank Corp	9984 JP	JPY	7089.000	12.4	14.9	14.9	4.3	3.2	2.6	30.2	0.6	7.9	4.3
Simple Average				15.9	15.2	15.2	2.3	2.0	1.8	14.9	2.0	6.5	5.7
Weighted Average				16.1	15.4	15.4	2.3	2.0	1.7	14.7	2.0	6.5	5.6
EU Listed Companies													
Vodafone Group Plc	VOD LN	GBp	226.250	38.4	36.6	36.6	0.8	0.9	1.1	3.2	5.0	7.0	2.6
Deutsche Telekom Ag-Reg	DTE GR	EUR	16.740	23.4	20.5	20.5	2.9	2.6	2.5	11.9	3.3	6.6	3.9
Swisscom Ag-Reg	SCMN VX	CHF	553.000	16.9	16.8	16.8	5.2	4.4	4.1	26.5	4.1	8.2	8.3
Telenor Asa	TEL NO	NOK	153.200	15.5	13.7	13.7	3.5	3.2	3.0	21.0	5.3	6.8	8.1
Telecom Italia Spa	TIT IM	EUR	1.090	15.8	15.1	15.1	1.2	1.1	1.0	7.7	1.2	5.6	2.6
Simple Average				22.0	20.5	20.5	2.7	2.4	2.3	14.1	3.8	6.9	5.1
Weighted Average				26.5	24.6	24.6	2.3	2.1	2.1	11.2	4.1	6.9	4.3
Other Developed Market													
Telstra Corp Ltd	TLS AU	AUD	6.315	18.6	17.2	17.2	5.7	5.7	5.4	30.6	4.9	8.4	12.7
Singapore Telecom Ltd	ST SP	SGD	4.110	17.5	16.5	16.5	2.8	2.7	2.5	15.4	4.2	14.5	9.5
Simple Average				18.1	16.8	16.8	4.2	4.2	4.0	23.0	4.5	11.5	11.1
Weighted Average				18.1	16.9	16.9	4.4	4.3	4.1	23.8	4.6	11.1	11.3
Overall Average				17.4	16.3	16.3	3.7	3.3	2.9	15.2	3.8	7.4	6.5
Overall Weighted Average				17.9	16.8	16.8	4.1	3.7	3.1	14.9	3.7	7.3	6.9

Source: Bloomberg.

Financial Statements and Ratios:

Income Statement					
Year end Dec, RMB m	2013A	2014A	2015F	2016F	2017F
Revenue from the Mobile business	151,133	155,095	160,385	167,539	179,318
Revenue from the Fixed-line business	86,566	88,481	88,231	89,210	90,185
Unallocated service revenue	947	1,302	1,341	1,380	1,443
Sales of telecom products	56,393	39,803	40,494	38,068	36,929
Total revenue	295,039	284,681	290,451	296,197	307,875
Interconnection charges	(20,208)	(14,599)	(15,097)	(16,251)	(17,394)
Depreciation & amortization	(68,196)	(73,868)	(74,684)	(76,939)	(79,840)
Networks, operations & support expenses	(33,704)	(37,851)	(38,948)	(40,117)	(41,320)
Employee benefit expenses	(31,783)	(34,652)	(36,742)	(37,321)	(39,100)
Costs of telecommunications products sold	(63,416)	(43,397)	(42,149)	(38,101)	(35,853)
Other operating expenses	(61,964)	(61,411)	(63,765)	(66,145)	(71,391)
Total operating expenses	(279,271)	(265,778)	(271,385)	(274,873)	(284,898)
Operating profit	15,768	18,903	19,066	21,323	22,977
Finance costs	(3,113)	(4,617)	(4,538)	(5,199)	(5,555)
Interest income	173	283	254	302	348
Other income - net	887	1,362	1,444	1,530	1,622
Profit before income tax	13,715	15,931	16,225	17,956	19,392
Income tax expenses	(3,306)	(3,876)	(3,947)	(4,369)	(4,718)
Net profit	10,409	12,055	12,277	13,588	14,674
EPS (RMB)	0.440	0.505	0.512	0.563	0.605

Cash Flow Statement					
Year end Dec, RMB m	2013A	2014A	2015F	2016F	2017F
Profit before income tax	13,715	15,931	16,225	17,956	19,392
Net interest expenses (income)	2,790	3,830	4,285	4,898	5,207
Depreciation & amortization	68,196	73,868	74,684	76,939	79,840
Other non-cash items	(5,872)	5,696	16,604	(13,155)	11,476
Working capital change	7,781	(2,263)	(1,329)	15,275	2,121
Interest received	173	283	254	302	348
Interest paid	(5,082)	(4,631)	(4,538)	(5,199)	(5,555)
Income tax paid	(3,219)	(4,620)	(3,947)	(4,369)	(4,718)
Net cash inflow from operating activities	78,482	88,094	102,237	92,647	108,111
CAPEX	(72,758)	(69,586)	(100,000)	(85,000)	(80,000)
Others	(4,352)	(5,733)	(1,692)	(959)	(435)
Net cash outflow from investing activities	(77,110)	(75,319)	(101,692)	(85,959)	(80,435)
Proceeds from bank & other loans	186,995	178,144	133,067	143,284	150,300
Repayment of bank & other loans	(183,350)	(206,053)	(123,853)	(140,340)	(160,338)
Dividend paid	(2,686)	(3,677)	(4,789)	(4,877)	(5,398)
Others	967	22,613	(145)	(130)	(117)
Net cash inflow from financing activities	1,926	(8,973)	4,281	(2,063)	(15,553)
Cash & cash equivalents, beginning of year	18,250	21,506	25,308	30,134	34,758
Net change in cash & cash equivalents	3,298	3,802	4,826	4,625	12,123
Effect of FX rate	(42)	0	0	0	0
Cash & cash equivalents, end of year	21,506	25,308	30,134	34,758	46,881

Source: the Company, Guotai Junan International.

Balance Sheet					
As at Dec, RMB m	2013A	2014A	2015F	2016F	2017F
PP&E	431,625	438,321	474,440	517,501	557,661
Lease prepayments	8,038	9,211	9,579	9,963	10,361
Goodwill	2,771	2,771	2,771	2,771	2,771
Other non-current assets	34,527	38,195	40,431	42,670	44,912
Non-current assets	476,961	488,498	527,221	572,905	615,705
Inventories & consumables	5,536	4,378	5,013	4,869	4,892
Account Receivables	14,842	14,671	5,517	16,555	17,798
Prepayments & other current assets	9,664	10,029	7,207	11,912	9,563
cash & cash equivalents	21,506	25,308	30,134	34,758	46,881
Other current assets	662	2,188	2,296	2,409	2,528
Current assets	52,210	56,574	60,167	70,503	81,663
Total assets	529,171	545,072	587,389	643,408	697,368
Accounts payable & accrued liabilities	102,212	120,371	130,116	135,554	144,400
Amounts due to related parties	5,810	5,164	5,568	6,013	6,503
Commercial papers	35,000	9,979	19,818	23,549	14,476
Short-term bank loans	94,422	91,503	105,228	121,013	139,165
Current portion of other obligations	2,672	2,698	3,050	3,437	3,862
Advances from customers	49,841	46,892	51,724	55,182	59,888
Others	5,282	15,313	4,794	4,999	5,273
Current liabilities	295,239	291,920	320,299	349,747	373,568
Long-term bank debt	2,481	2,420	2,580	2,742	2,920
Deferred revenue	1,269	1,497	1,527	1,558	1,619
CB	11,002	0	0	0	0
Others	281	21,694	23,854	26,227	28,836
Non-current liabilities	15,033	25,611	27,961	30,526	33,375
Total liabilities	310,272	317,531	348,259	380,273	406,943
Share capital & other statutory capital reserve	177,611	179,101	177,643	177,643	177,644
Other reserves	(19,529)	(19,482)	(19,482)	(19,482)	(19,482)
Retained profits	60,817	67,922	80,969	104,974	132,263
Shareholders' equity	218,899	227,541	239,130	263,135	290,425
BPS (RMB)	9.253	9.540	9.967	10.904	11.965

Key Financial Ratios					
Year end Dec	2013A	2014A	2015F	2016F	2017F
Operating margin (%)	5.3	6.6	6.6	7.2	7.5
Net profit margin (%)	3.5	4.2	4.2	4.6	4.8
ROA (%)	2.0	2.2	2.2	2.2	2.2
ROE (%)	4.9	5.4	5.3	5.4	5.3
Net gearing (%)	56.7	49.8	51.9	55.1	49.9

Company Rating Definition

The Benchmark: Hong Kong Hang Seng Index

Time Horizon: 6 to 18 months

Rating	Definition
Buy	Relative Performance >15%; or the fundamental outlook of the company or sector is favorable.
Accumulate	Relative Performance is 5% to 15%; or the fundamental outlook of the company or sector is favorable.
Neutral	Relative Performance is -5% to 5%; or the fundamental outlook of the company or sector is neutral.
Reduce	Relative Performance is -5% to -15%; or the fundamental outlook of the company or sector is unfavorable.
Sell	Relative Performance <-15%; or the fundamental outlook of the company or sector is unfavorable.

Sector Rating Definition

The Benchmark: Hong Kong Hang Seng Index

Time Horizon: 6 to 18 months

Rating	Definition
Outperform	Relative Performance >5%; or the fundamental outlook of the sector is favorable.
Neutral	Relative Performance is -5% to 5%; or the fundamental outlook of the sector is neutral.
Underperform	Relative Performance <-5%; or the fundamental outlook of the sector is unfavorable.

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