

GCL-POLY ENERGY 3800 HK

BUY

UNCHANGED

TARGET PRICE	HKD2.52
CLOSE	HKD2.14
UP/DOWNSIDE	+17.9%
PRIOR TP	HKD3.14
CHANGE IN TP	-19.6%

HOW WE DIFFER FROM CONSENSUS		MARKET RECS	
TARGET PRICE (%)	(0.5)	POSITIVE	29
EPS 2014 (%)	(10.3)	NEUTRAL	5
EPS 2015 (%)	(5.2)	NEGATIVE	4

Improved outlook

■ Poly prices look set to stabilise

The spot price for poly has declined rapidly over recent months, due to increased supply from rush-in orders before the ban on processing trade effective January and lower demand as construction slowed for solar projects in winter. We expect poly prices to stabilise and recover mildly, as: 1) current prices are lower than the cost level for many players, and 2) demand should recover as solar projects resume construction in March.

■ China solar demand should recover in 2015

NEA's proposed solar installation target for 2015 is 15GW, vs the 10.6GW installed in 2014. We believe quota constraint will no longer be a big issue. We also expect more installations from distributed solar, especially those built on vacant land. Other supportive policies such as renewable power quota should help. Solar power tariffs may be reviewed, which could trigger rush-in demand.

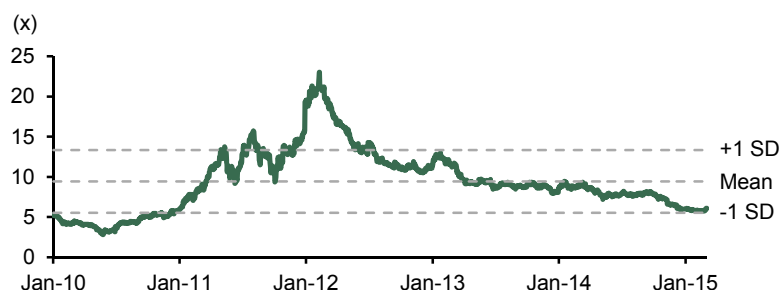
■ Other overhangs have eased

GCL Poly's captive power plant received an environment appraisal approval on 27 Jan. The company has scrapped its wafer disposal plan, and our concern that wafer demand will be impacted by the US anti-dumping decision has eased.

■ Maintain BUY with a lower TP of HKD2.52 (HKD3.14 previously)

We trim our EPS by 4.0-7.5% over 2014-16E, mainly due to lower ploy/wafer ASP forecasts. We lower our target 2015E EV/operating EBITDA 5% to 7.6x, which is 0.5 SD below the stock's historical mean, to reflect weaker sentiment on corporate governance concerns for GCL Poly. This gives a TP of HKD2.52 – BUY.

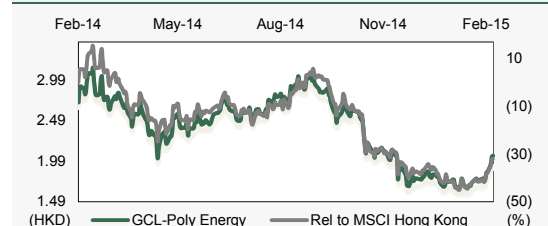
Trading at a historical trough level



Sources: GCL-Poly Energy; Bloomberg; BNP Paribas estimates

KEY STOCK DATA

YE Dec (HKD m)	2013A	2014E	2015E	2016E
Revenue	25,530	34,294	34,462	37,803
Rec. net profit	(1,089)	1,917	2,744	3,046
Recurring EPS (HKD)	(0.07)	0.12	0.18	0.20
Prior rec. EPS (HKD)	(0.07)	0.13	0.18	0.21
Chg. In EPS est. (%)	nm	(6.6)	(4.0)	(7.5)
EPS growth (%)	nm	nm	43.1	11.0
Recurring P/E (x)	neg	17.3	12.1	10.9
Dividend yield (%)	0.0	1.2	1.7	1.8
EV/EBITDA (x)	12.2	7.3	6.6	6.0
Price/book (x)	2.1	1.9	1.7	1.5
Net debt/Equity (%)	147.4	164.0	150.6	129.0
ROE (%)	(6.7)	11.3	14.6	14.4



Share price performance	1 Month	3 Month	12 Month
Absolute (%)	22.3	2.4	(26.0)
Relative to country (%)	15.2	(5.1)	(36.2)
Next results	March 2015		
Mkt cap (USD m)	4,272		
3m avg daily turnover (USD m)	21.6		
Free float (%)	68		
Major shareholder	Zhu Gongshan (32%)		
12m high/low (HKD)	3.15/1.66		
3m historic vol. (%)	56.1		
ADR ticker	GCPEF US		
ADR closing price (USD; 3 Mar 2015)	0.2697		
Issued shares (m)	15,483		

Sources: Bloomberg consensus; BNP Paribas estimates



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Investment thesis

We expect China's solar power installation to see high growth in 2015, off the low base in 2014, driven by: 1) removal of quota constraints; 2) higher growth in distributed solar power, especially those built on vacant land; 3) better financing support; 4) more supportive policies; and 5) possible feed-in-tariff cut to trigger rush-in demand.

We expect poly prices to stabilise in the near term as they are below the cost level for many smaller players, while demand recovery should also support prices.

Although we expect poly price to decline in the longer term on capacity expansion by existing players and lower industry cost levels, cost leaders such as GCL Poly should still be able to maintain margins and also expand market share at the loss of higher-cost smaller players.

Catalyst

Key catalysts include: stabilisation of spot poly price; supportive policy for renewable power to be announced around National People's Congress; and the launch of captive power plants and new FBR capacities

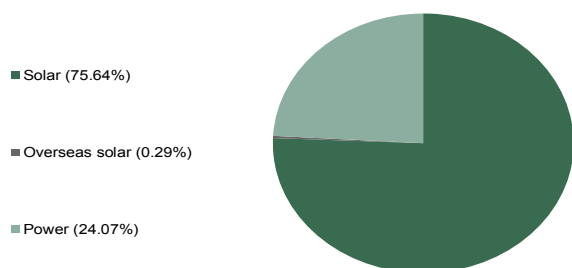
Risks to our call

Key risk to our call include: 1) further collapse in poly and wafer prices; 2) further delay in captive power plant and FBR capacities; 3) lower-than-expected solar power installation in China; 4) weaker-than-expected global solar demand; and 5) oil price volatility to affect market sentiment.

Company background

GCL-Poly Energy Holdings, together with its subsidiaries, is engaged in the manufacturing of polysilicon and wafers, the development and operation of environmental friendly power plants, as well as the operation of solar system integration business. It has two major segments: solar business, which manufactures and sells polysilicon and wafer to companies operating in the solar industry, and power business, which comprises the development, construction, and operation of power plants and sales of coals.

Principal activities



Key executives

	Age	Joined	Title
Zhu Gongshan	55	2006	Chairman/CEO/Founder
Shu Hua	50	2007	Executive President
Sha Hongqiu	54	2007	Executive President

<http://www.gcl-poly.com.hk/>

Key assumptions

		2014E	2015E	2016E
Polysilicon unit cost	USD/kg	15.57	14.26	13.47
Polysilicon ASP	USD/kg	21.89	19.5	17.68
Wafer shipments	MW	12,809	14,000	15,600
Wafer ASP	USD/W	0.22	0.21	0.2
Wafer unit cost	USD/W	0.17	0.15	0.15
Solar capacity addition	MW	616	1,500	1,200

Source: BNP Paribas estimates

Earnings sensitivity

	Change	2014E	2015E
ASP (%)			
Wafers	1	7.3	5.4
Poly	1	0.8	0.5
Unit cost (%)			
Wafers	(1)	6.3	4.3
Poly	(1)	0.6	2.0
Interest rate	25bp	(3.0)	(2.1)

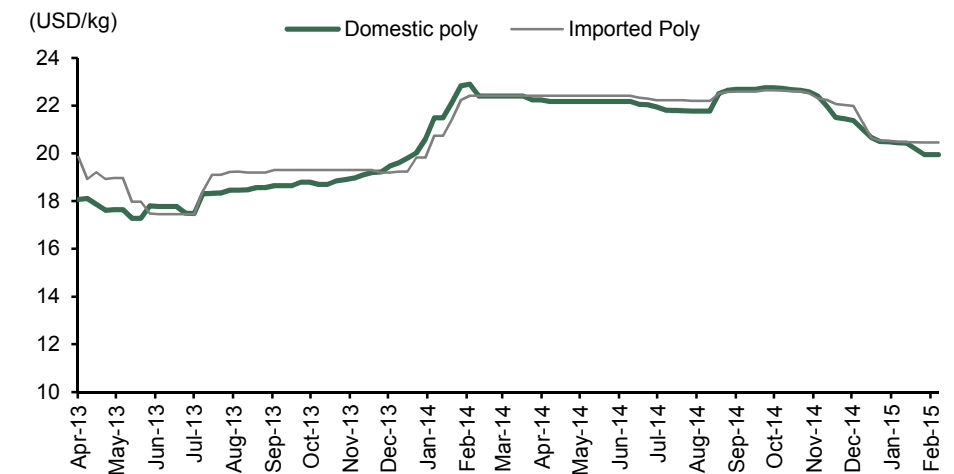
Source: BNP Paribas estimates

- Earnings are more sensitive to wafer price change than to poly price change.
- Earnings are more sensitive to ASP change than to cost change.
- Earnings are very sensitive to interest rate changes due to the company's high gearing levels.

Polysilicon prices look set to stabilise

Spot poly prices have fallen sharply since 4Q14 on higher supply and sluggish demand. We expect poly prices to stabilise as supply declines and demand recovers. Meanwhile, current spot price for poly is lower than the production cost of many smaller players, which could help to support pricing levels.

EXHIBIT 1: Poly price trend

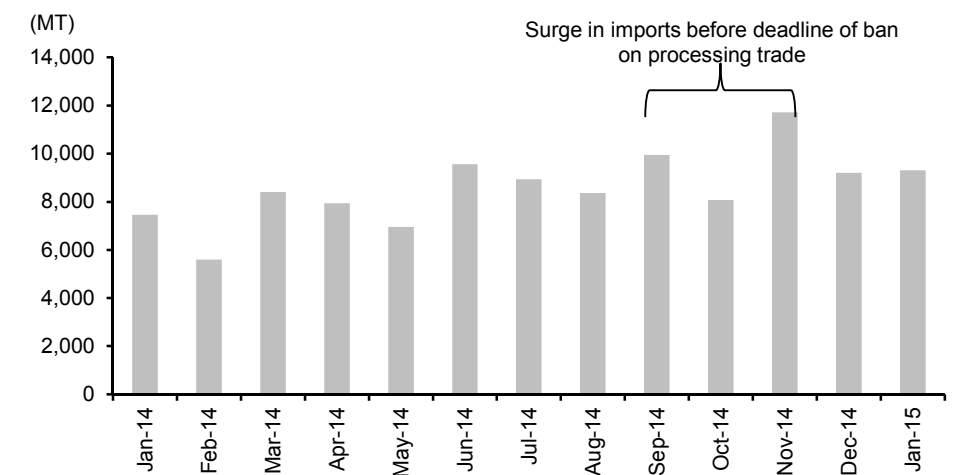


Source: Solarzoom

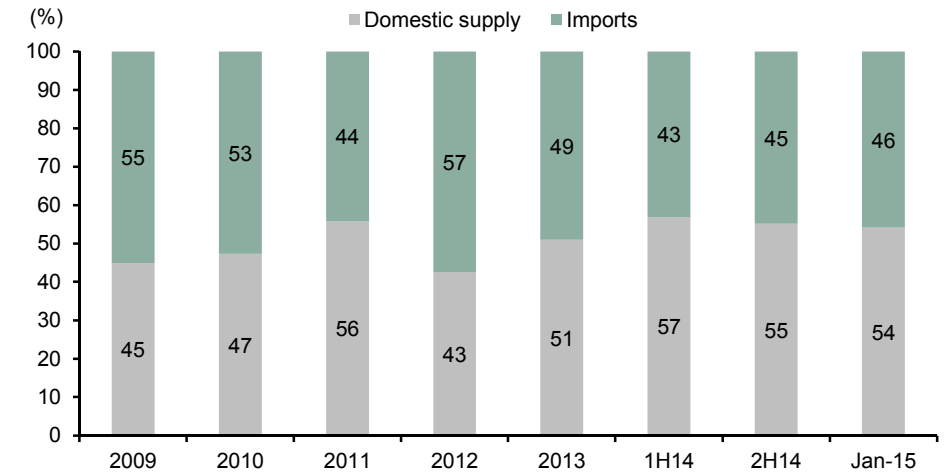
The increase in supply was due mainly to rush-in imports during September-November 2014, as the China Government has banned processing trade starting from January 2015. In 2014, 70.5% of total poly imports were carried out under processing trade, which is exempt from any tariff (including normal tariff and anti-dumping tariff).

Imports volume have normalised since December 2014. Although imports can be continued under processing trade until August 2015 as some smaller import/export agencies are still allowed to execute their contracts, we expect import volume to fall from high levels of 4Q14.

EXHIBIT 2: Monthly poly imports



Source: China Customs Administration

EXHIBIT 3: Poly: domestic vs imported

Sources: China Customs Administration; China Silicon Association

On the other hand, we expect demand for solar products to pick up. Late 4Q and early 1Q are usually weak seasons for solar demand as most construction activity tends to be suspended due to cold weather. We expect solar projects to resume construction in March, thus supporting solar demand in the near term.

Although we expect poly prices to decline in the longer term on capacity expansion by existing players and lower industry cost levels, cost leaders such as GCL Poly should still be able to maintain margins and expand market share at the loss of higher-cost smaller players.

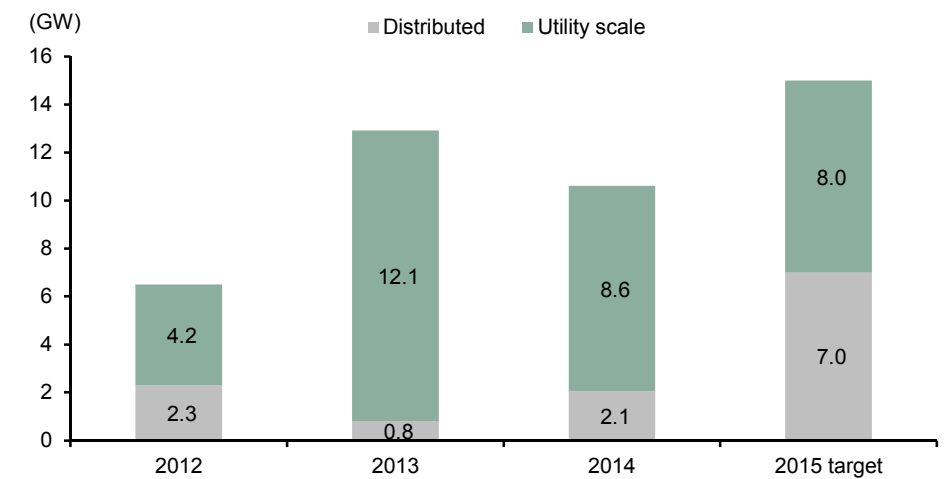
China solar demand should recover in 2015

Although solar power installation was disappointing in 2014, we see upside risk to demand for 2015.

NEA's initial proposals for solar power installation targets for 2015 are 8GW for utilities and 7GW for distributed solar power projects. Out of the 7GW target for distributed solar, 3.85GW relates to <20MW projects to be built on vacant lands, fishing ponds and agricultural greenhouses. For rooftop projects, there is no quota restriction.

Unlike for the 2014 target, we are more confident about the solar installation target for 2015, given: 1) quota issues have mostly been resolved, so this should no longer be a big constraint for solar installations this year; 2) many distributed solar projects that are being built on vacant land are at an initial preparation phase as they were started only in 4Q14; 3) improved growth prospects for the rooftop segment on further policy support; and 4) improved financing conditions given the interest rate cut environment

Furthermore, additional supportive policies such as renewable power quota may be announced later this year. Meanwhile, solar tariffs may be reviewed in 2015 after wind power tariff cut. There could lead to rush-in demand if the on-grid tariff is cut.

EXHIBIT 4: China targets higher solar installation in 2015

Source: NEA

Other overhangs have also eased

Apart from weak polysilicon prices, other overhangs for GCL Poly include:

Cost-reduction measures: We were previously concerned that captive power plants and FBR capacity additions may be delayed further. But, the Ministry of Environmental Protection granted approval for the environment appraisal for GCL Poly's captive power plant on 27 January. This provides better visibility for the launch of its captive power plant.

Wafer disposal and wafer demand: The company has abandoned its plans to dispose of the wafer business, and Shanghai Chaori has been repositioned as a solar system service provider (EPC, financing, etc). While we previously were concerned that wafer demand would be affected by US anti-dumping, the final anti-dumping determination from the US DOC removed this overhang: using wafers produced overseas will not help module players avoid anti-dumping tariffs, which means wafer demand will not be diverted to non-China producers.

Corporate governance: The key concern is related to the connected transaction with GCL System Integration (002506 CH, former Shanghai Chaori). The company has so far entered into six wafer sales agreements with GCL System Integration. Total purchased volume is around 560.7MW, representing only 4% of our wafer sales forecast for 2015. Given GCL System Integration's capacity, we believe the related transactions are unlikely to represent a large part of GCL-Poly's wafer sales. Meanwhile, the price of wafer sales also looks fair. We estimate a blended ASP of around USD0.22/W, which is higher than GCL-Poly's ASP of USD 0.21/W in 3Q14.

EXHIBIT 5: Connected transactions with GCL System Integration

Date of agreement	Customer	Supplier	Transaction matter	Consideration (RMB m)	Volume (MW)	Unit price (RMB/piece)	ASP (RMB/w)	ASP (USD/w)
26/08/2014	First Silicon Wafer Sales Agreement	Taicang GCL Photovoltaic, Suzhou GCL Photovoltaic, Changzhou GCL Photovoltaic and Jiangsu GCL Silicon Material	P2 polycrystalline wafer of 13M pieces S3 polycrystalline wafer of 17M pieces	189.8	130.7	6.1 for P2 6.5 for S3	1.45	0.23
23/09/2014	Second Silicon Wafer Sales Agreement	Taicang GCL Photovoltaic, Suzhou GCL Photovoltaic, Changzhou GCL Photovoltaic and Jiangsu GCL Silicon Material	S2 polycrystalline wafer of 4M pieces S3 polycrystalline wafer of 3M pieces	36.3	30.8	5.1 for S2 5.3 for S3	1.18	0.19
1/12/2014	Shanghai Chaori	Third Silicon Wafer Sales Agreement	GCL-Poly (Suzhou) New Energy Co				1.45	0.23
1/5/2015		Fourth Silicon Wafer Sales Agreement					1.45	0.23
14/01/2015		Fifth Silicon Wafer Sales Agreement	Suzhou GCL Photovoltaic and GCL-CSI (Suzhou) Photovoltaic Technology Co				1.24	0.20
3-Feb-15		Sixth Silicon Wafer Sales Agreement	GCL-Poly (Suzhou) - amendment				1.43	0.23
			S3 polycrystalline wafer of 21M pieces	132.3	94.5	6.3	1.40	0.23
Grand Total				799.5	560.7			0.22

Source: GCL-Poly Energy

Maintain BUY with a new TP of HKD2.52

The company has made a positive profit alert, guiding that 2014E net profit will be no less than HKD1,800m, which is below the Bloomberg consensus estimate of HKD2,171m and our previous forecast of HKD2,052m. We believe the key reason is lower-than-expected ASP for both poly and wafer.

We cut our poly ASP assumptions 2% for 2014 and 5% for 2015. We also lower our wafer ASP assumptions 4% for 2014 and 9% for 2015.

However, our lower ASP assumptions are partly offset by other positives: 1) we lower our finance cost estimate by 50bps as the PBOC has cut benchmark interest rate twice since November 2014 and another cut is widely anticipated this year. According to management, GCL Poly can normally borrow at the benchmark interest rate with no mark-up; 2) we cut our unit fuel cost assumption for the company's gas-fired power plants after the recent city gate gas price cut by the NDRC; 3) we raise our 2015- 2016 solar projects installation forecasts as we are now more positive on China demand for 2015. Our forecast is below the company's installation target of 2GW for 2015 and 2.5GW for 2016

As a result, we trim our earnings forecasts 4-7% over 2014-16. We cut our target 2015E EV/operating EBITDA multiple by 5% to 7.6x, which is 0.5 SD below the stock's historical mean, to reflect weaker sentiment on corporate governance concerns. This generates a new TP of HKD2.52 (HKD3.14 previously), implying about 18% upside from current levels – maintain BUY.

EXHIBIT 6: Changes to key assumptions

	2014E	2015E	2016E
Poly ASP (USD/kg)			
Current	21.89	19.50	17.68
Previous	22.39	20.45	17.84
Change (%)	(2)	(5)	(1)
Wafer ASP (USD/W)			
Current	0.22	0.21	0.20
Previous	0.23	0.23	0.22
Change (%)	(4)	(9)	(9)
Wafer shipment (MW)			
Current	12,809	14,000	15,600
Previous	11,793	13,440	15,600
Change (%)	9	4	0
Bank borrowing rate (%)			
Current	7.0	6.5	6.5
Previous	7.0	7.0	7.0
Change (%)	0.0	(0.5)	(0.5)
Unit fuel cost for gas-fired power plants (HKD/MWh)			
Current	669	655	625
Previous	648	681	681
Change (%)	3	(4)	(8)
Solar farm capacity addition (MW)			
Current	616	1,500	1,200
Previous	600	900	800
Change (%)	3	67	50
Net profit (HKD m)			
Current	1,917	2,756	3,079
Previous	2,052	2,859	3,294
Change (%)	(7)	(4)	(7)

Source: BNP Paribas estimates

Financial statements

GCL-Poly Energy

Profit and Loss (HKD m) Year Ending Dec	2012A	2013A	2014E	2015E	2016E
Revenue	22,348	25,530	34,294	34,462	37,803
Cost of sales ex depreciation	(17,770)	(19,160)	(23,402)	(20,871)	(21,589)
Gross profit ex depreciation	4,578	6,370	10,892	13,590	16,214
Other operating income	784	965	1,068	948	1,068
Operating costs	(3,481)	(2,285)	(2,775)	(2,686)	(2,946)
Operating EBITDA	1,881	5,049	9,184	11,852	14,336
Depreciation	(2,829)	(3,330)	(3,835)	(4,760)	(5,945)
Goodwill amortisation	0	0	0	0	0
Operating EBIT	(948)	1,719	5,349	7,092	8,391
Net financing costs	(2,309)	(2,416)	(2,827)	(3,154)	(3,705)
Associates	3	21	30	48	57
Recurring non operating income	(7)	(5)	5	5	5
Non recurring items	0	424	0	0	0
Profit before tax	(3,261)	(256)	2,557	3,991	4,749
Tax	(124)	(190)	(537)	(838)	(997)
Profit after tax	(3,385)	(446)	2,020	3,153	3,752
Minority interests	(130)	(218)	(103)	(409)	(706)
Preferred dividends	0	0	0	0	0
Other items	0	0	0	0	0
Reported net profit	(3,516)	(664)	1,917	2,744	3,046
Non recurring items & goodwill (net)	0	(424)	0	0	0
Recurring net profit	(3,516)	(1,089)	1,917	2,744	3,046
Per share (HKD)					
Recurring EPS *	(0.23)	(0.07)	0.12	0.18	0.20
Reported EPS	(0.23)	(0.04)	0.12	0.18	0.20
DPS	0.00	0.00	0.02	0.04	0.04
Growth					
Revenue (%)	(12.4)	14.2	34.3	0.5	9.7
Operating EBITDA (%)	(79.0)	168.4	81.9	29.0	21.0
Operating EBIT (%)	(113.5)	(281.3)	211.1	32.6	18.3
Recurring EPS (%)	nm	nm	nm	43.1	11.0
Reported EPS (%)	(182.2)	(81.1)	(388.5)	43.1	11.0
Operating performance					
Gross margin inc depreciation (%)	7.8	11.9	20.6	25.6	27.2
Operating EBITDA margin (%)	8.4	19.8	26.8	34.4	37.9
Operating EBIT margin (%)	(4.2)	6.7	15.6	20.6	22.2
Net margin (%)	(15.7)	(4.3)	5.6	8.0	8.1
Effective tax rate (%)	-	-	21.0	21.0	21.0
Dividend payout on recurring profit (%)	-	-	20.0	20.0	20.0
Interest cover (x)	(0.4)	0.7	1.9	2.3	2.3
Inventory days	60.3	37.2	38.4	55.5	53.9
Debtor days	128.4	141.1	137.2	165.1	166.5
Creditor days	172.1	217.8	203.1	208.9	203.1
Operating ROIC (%)	(2.2)	4.0	11.1	11.6	11.6
ROIC (%)	(2.0)	3.7	10.2	10.8	11.0
ROE (%)	(19.1)	(6.7)	11.3	14.6	14.4
ROA (%)	(1.6)	2.1	6.0	6.8	6.8
*Pre exceptional, pre-goodwill and fully diluted					
Revenue By Division (HKD m)					
Solar	13,889	18,121	25,939	26,266	28,102
Overseas solar	2,652	700	99	99	99
Power	5,807	6,709	8,256	8,096	9,602

Sources: GCL-Poly Energy; BNP Paribas estimates

Financial statements

GCL-Poly Energy

Cash Flow (HKD m) Year Ending Dec	2012A	2013A	2014E	2015E	2016E
Recurring net profit	(3,516)	(1,089)	1,917	2,744	3,046
Depreciation	2,829	3,330	3,835	4,760	5,945
Associates & minorities	127	197	68	356	644
Other non-cash items	0	0	0	0	0
Recurring cash flow	(559)	2,438	5,821	7,860	9,634
Change in working capital	(742)	4,294	(6,715)	(2,250)	(963)
Capex - maintenance	0	0	0	0	0
Capex - new investment	(4,473)	(4,169)	(9,270)	(16,625)	(12,831)
Free cash flow to equity	(5,774)	2,564	(10,164)	(11,014)	(4,160)
Net acquisitions & disposals	0	0	0	0	0
Dividends paid	(851)	0	(383)	(549)	(609)
Non recurring cash flows	875	(1,173)	0	0	0
Net cash flow	(5,750)	1,391	(10,548)	(11,563)	(4,769)
Equity finance	1	0	1,847	4,200	2,986
Debt finance	4,324	2,776	6,078	11,161	7,331
Movement in cash	(1,425)	4,167	(2,623)	3,798	5,547
Per share (HKD)					
Recurring cash flow per share	(0.04)	0.16	0.38	0.51	0.62
FCF to equity per share	(0.37)	0.17	(0.66)	(0.71)	(0.27)
Balance Sheet (HKD m) Year Ending Dec	2012A	2013A	2014E	2015E	2016E
Working capital assets	12,658	13,808	19,094	20,618	22,440
Working capital liabilities	(10,270)	(15,714)	(14,284)	(13,559)	(14,418)
Net working capital	2,389	(1,906)	4,809	7,059	8,022
Tangible fixed assets	42,233	43,995	49,430	61,295	68,181
Operating invested capital	44,621	42,090	54,239	68,354	76,203
Goodwill	899	853	853	853	853
Other intangible assets	0	0	0	0	0
Investments	451	536	571	624	686
Other assets	2,067	3,201	3,201	3,201	3,201
Invested capital	48,038	46,680	58,864	73,031	80,943
Cash & equivalents	(9,510)	(14,249)	(11,626)	(15,424)	(20,971)
Short term debt	20,170	26,331	29,213	35,329	39,937
Long term debt *	16,741	14,460	17,656	22,701	25,423
Net debt	27,401	26,542	35,243	42,606	44,390
Deferred tax	0	0	0	0	0
Other liabilities	2,867	2,132	2,132	2,132	2,132
Total equity	16,210	16,146	17,680	19,875	22,312
Minority interests	1,560	1,859	3,809	8,417	12,109
Invested capital	48,038	46,680	58,864	73,031	80,943
* includes convertibles and preferred stock which is being treated as debt					
Per share (HKD)					
Book value per share	1.05	1.04	1.14	1.28	1.44
Tangible book value per share	0.99	0.99	1.09	1.23	1.39
Financial strength					
Net debt/equity (%)	154.2	147.4	164.0	150.6	129.0
Net debt/total assets (%)	40.4	34.6	41.6	41.8	38.2
Current ratio (x)	0.7	0.7	0.7	0.7	0.8
CF interest cover (x)	0.4	3.8	0.7	2.8	3.3
Valuation	2012A	2013A	2014E	2015E	2016E
Recurring P/E (x) *	neg	neg	17.3	12.1	10.9
Recurring P/E @ target price (x) *	neg	neg	20.4	14.2	12.8
Reported P/E (x)	neg	neg	17.3	12.1	10.9
Dividend yield (%)	0.0	0.0	1.2	1.7	1.8
P/CF (x)	(59.2)	13.6	5.7	4.2	3.4
P/FCF (x)	(5.7)	12.9	(3.3)	(3.0)	(8.0)
Price/book (x)	2.0	2.1	1.9	1.7	1.5
Price/tangible book (x)	2.2	2.2	2.0	1.7	1.5
EV/EBITDA (x) **	31.6	12.2	7.3	6.6	6.0
EV/EBITDA @ target price (x) **	34.8	13.4	7.9	7.1	6.4
EV/invested capital (x)	1.3	1.3	1.2	1.2	1.1
* Pre exceptional, pre-goodwill and fully diluted ** EBITDA includes associate income and recurring non-operating income					

Sources: GCL-Poly Energy; BNP Paribas estimates

Disclaimers and Disclosures

APPENDIX

DISCLAIMERS AND DISCLOSURES APPLICABLE TO NON-US BROKER-DEALER(S): BNP Paribas Securities (Asia) Ltd

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Company	Ticker	Disclosure (as applicable)
GCL-Poly Energy	3800 HK	6

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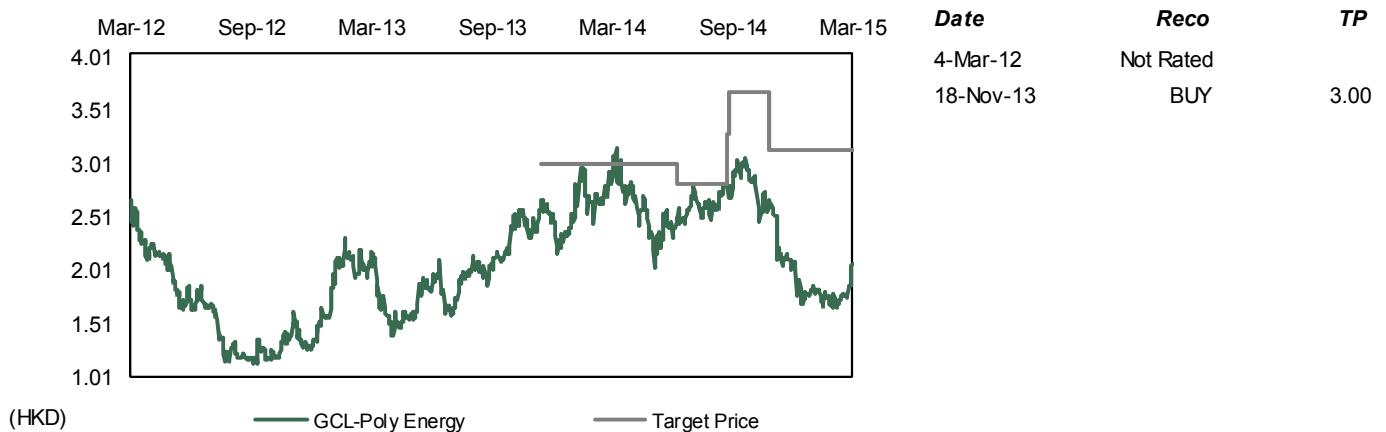
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History of change in investment rating and/or target price

GCL-Poly Energy (3800 HK)



Penny Chen started covering this stock from 12-Jun-2014

Price and TP are in local currency

Valuation and risks: Key risk to our EV/EBITDA-based TP include: 1) further collapse in poly and wafer prices; 2) further delay in captive power plant and FBR capacities; 3) lower-than-expected solar power installation in China; 4) weaker-than-expected global solar demand; and 5) oil price volatility to affect market sentiment.

Sources: Bloomberg; BNP Paribas

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